

Surprising Cause of the Toronto Real Estate Bubble

Early Transfer of Family Wealth

With the average home price in the Greater Toronto Area (GTA) skyrocketing more than 450% over the last 25 years, homeownership has never been more challenging for new home buyers (Wells, 2022). But, for some, homeownership comes much easier than others. In Ontario, roughly 40% of parents of younger homeowners help their children financially to purchase their home, with the average gift being north of \$70,000. As well, 38% of these parents also help with their children's mortgage payments suggesting that a significant portion of new homeowners would struggle to sustain their financial obligations unless parents financially assisted (Fox, 2022).

There used to be a simple formula in personal finance to assess whether a property is within one's financial means: aim to buy a home that is four times or less than one's annual income. However, for the average Torontonian, following this rule has become unrealistic. In Toronto, the average home price hovered around eight times the average local household income before 2020. As of the end of 2021, it has reached 10 times the average Torontonian income (Alini, 2021), which demonstrates how unattainable homeownership has become.

However, there is a different story, specifically on the more privileged families. A study by CIBC Economics from October 2021 concluded that there was \$10-billion worth of down payment gifts in Canada's housing market in 2020 alone, with average gifts of \$130,000 in the GTA (Tal, 2022). I understand that the housing crisis prompts this early transfer of wealth. However, this transfer of wealth is also exacerbating the crisis, as these more fortunate home buyers bid higher for properties, feeding into the vicious cycle of unaffordable homeownership.

For many of these parents, it is important that they help their children with their home purchase, as they have made a significant amount of money on the sale of their own primary residence and they feel that their children are now suffering on the buyers' side. These parents feel that they should help kick-start their children's independence, and for the more privileged families, it is their way of keeping the "old money" alive and within the family. Studies have also found that a portion of the parents have also been borrowing against their retirement funds and other investments to help fund their children's home purchases, potentially putting their retirement at risk financially.

Housing Supply Lagging Behind Demand

Net migration gain—whether from international sources, other parts of Canada, or other regions of Ontario—continues to be the primary factor contributing to the population growth for the GTA. According to Statistics Canada, the GTA has had a population growth of 54% over the last 25 years. The GTA is projected to be the fastest-growing region of the province, accounting for over 55% of Ontario's net population growth by 2046. The GTA's population is projected to increase from 6.9 million in 2022 to 10.0 million in 2046 (Ontario Population Projections, 2022). Not surprisingly, a good portion of all newcomers into the province settle in the city centre due to the amenities and opportunities available.

The main cause of the GTA housing unaffordability issue is the inability of the city to keep up the supply of homes to meet the demand due to the continued population growth. Canada has the lowest housing units per 1,000 people among all G7 countries. In the GTA, the root causes of the limited supply are a result of the constrained land supply, complex and bureaucratic approval processes, lengthy building times, and a tight supply of skilled labour. The rapid population growth adds to the heavy competition for the limited housing available, which

drives up prices. The fees and taxes charged by the three levels of government also add to roughly 25% of the cost of a new housing unit in the GTA (Wilkes, 2022). The historically low interest rate is also a somewhat irrational and compelling force, driving buyers into the market as they continue to see property prices climb.

With the supply constantly lagging behind demand, the prices of homes can only face upward pressure. The wealthy families helping their children purchase homes also continue to drive up home prices, as they participate in multiple offers, setting newer and higher record sale prices. This process, in turn, displaces those who are not fortunate enough to have the financial assistance when buying homes, making homeownership in a seller's market further from reality. The steady migration of newcomers has risen in smaller and remote towns where homes are still affordable. However, this process has driven up home prices, resulting in bidding wars on even modest starter homes in these towns.

Band-Aid Policies

The government has attempted to deliver solutions for the housing crisis, however, the focus has mostly been on tax-and-restrict approaches to cool demand for housing in the short term, rather than increasing the supply. The government has also attempted to cool the housing demand via levying foreign buyer taxes though this approach has brought measly returns to the government and minimal impacts on housing affordability since the true cause of this housing crisis is a supply shortage, not foreign buyers.

At the end of the day, people still need a place to live, and they will do whatever it takes to become homeowners. This means they will overbid on homes. This is why such a large number of young home buyers have been digging into the bank-of-mom-and-dad for down payment support, who afterwards continue to face challenges paying their mortgage and other

bills and face difficulty in mortgage renewals. Many new home buyers are now resorting to more expensive, higher-risk sources of financing with the B and C lenders.

Many people argue that due to the huge disparity between the varied abilities to become a homeowner, there needs to be a push for “generational fairness” when it comes to the cost of housing. Political advocacy groups such as “Generation Squeeze” advocate that taxing homes over \$1 million is one of the ways to address the affordability crisis. This surtax would reduce tax shelter on the principal residence and discourage homeownership as a means for wealth accumulation, which will, in turn, help place some downward pressure on property prices. Generation Squeeze also explains how the revenue collected by the surtax could then be used to subsidize low-income households, green co-op housing, or purpose-built rentals (A Price on Housing Inequity, 2022).

Developing Unconventional Solutions

With or without the financial assistance from the older generation for home purchase, it seems that homeowners now must be more conscientious of their finances to ensure that they do not enslave themselves financially. This could be done by improving one’s credit score ahead of time with some planning to avoid, if possible at all, obtaining mortgages from B or C lenders who charge higher interest rates. In my opinion, Canadian students are not educated enough about the importance of being financially responsible, and this is a critical skill that everyone needs. The school curriculum must include financial literacy from a young age so children can learn the fundamental components of financial management: earn, spend, save and invest, borrow, and protect (The Five Key Components of Financial Literacy, 2022). Once children move out of their parents’ homes and live independently, they can budget their after-tax income better so they do not overspend and ensure a net positive cash flow after paying their

expenses. To plan even further down the road, we also need to ensure that we have a sustainable investment strategy in place to be financially sound for retirement.

One other way of avoiding the homeownership financial enslavement is to consider purchasing properties that can be rented out to tenants within the same building and have tenants pay rent to help subsidize the property's mortgage payments. Of course, being a landlord comes with responsibilities, however this is an excellent way to help new homeowners get into a home, which they can better afford with less financial exposure once rented.

Another solution to the ever-soaring GTA housing prices is to consider home-sharing. The government can develop laws that will allow individuals to enter into homeownership together and even allow the transfer of ownership when situations and relationships evolve; this would allow people to get into homeownership easier by pooling their financial resources together.

The bidding wars on homes and the lack of sufficient credit scores to qualify for mortgages have both discouraged many home buyers from giving up on home purchases. Still, there is one viable solution that my parents take part in to help those families with the above challenges, which is to participate in "rent-to-own" (RTO) programs. Potential home buyers would find a home within their price range, find an investor who would qualify for a mortgage on the property, and the two parties would reach a contractual agreement so that the buyer-tenant would pay their monthly rents and an RTO fee to the investor who holds title to the home. A pre-agreed period would be settled until the tenant-buyers have a good enough credit score to qualify for their mortgage. RTO programs make homeownership possible because it allows the possibility of putting an offer in on a home without any financing conditions in a competitive market, and allows buyers to lock in a pre-agreed upon home purchase price a number of years away based on a passive appreciation percentage in that market.

Much Needed Permanent Government Policies

The GTA shortage of affordable housing supply intensifies inequality, drags on economic growth, and depresses the collective standard of living in the area. Although the older generations help their offspring by financially supporting their home purchase, doing so is rapidly driving up home prices further, making them even more unaffordable. It is imperative that the government at every level step in and develop long term solutions to help increase housing supply, whether by simplifying the development approval process, reducing fees on new development projects, regulating the home bidding process, so it is transparent to all bidders, or placing a cap on the final sale price from the listing price.

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