ESSENTIAL WORKERS, WORKFORCE HOUSING, & PROPERTY INVESTING

Author Bio

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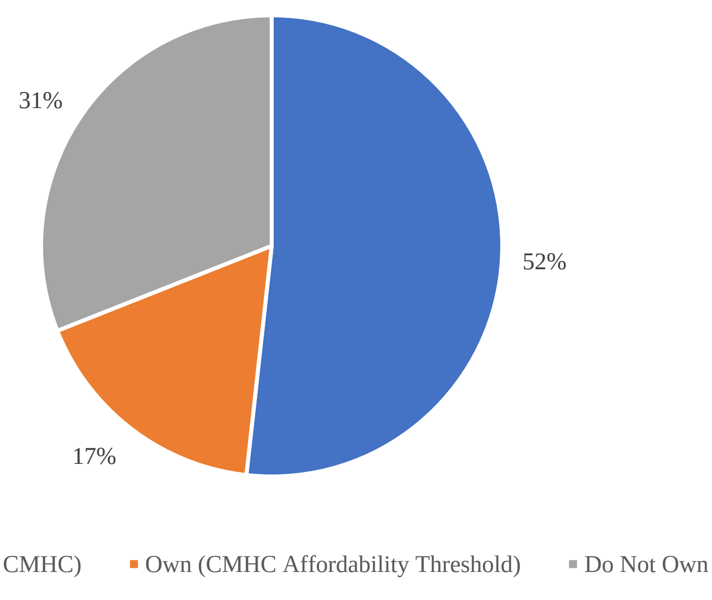
HOMEOWNERSHIP IN CANADA

For many Canadians, owning a home is an essential component of the Canadian dream. As such, the last century of policy has facilitated homeownership in Canada (Statistics Canada, 2019). However, many variables, including income, influence homeownership in Canada.

According to Statistics Canada (2015), variables that increase the likelihood of homeownership include age, education, and income. This suggests that an older individual, with a university education, and substantial income would have a high probability of owning a home in Canada. Not surprisingly, household debt decreases the likelihood of homeownership in Canada (Statistics Canada, 2015). Although homeownership in Canada is considered to be quite strong, one in every four Canadian households spends as much as 30% or more of their total pre-tax income on their mortgage payments (Statistics Canada, 2019). Moreover, Canada has the highest household debt of all G7 countries (Organisation for Economic Co-operation and Development, 2020). According to Canadian Mortgage and Housing Corporation (CMHC) (2018), "housing is considered affordable if it costs less than 30% of a household's before-tax income." Based on these metrics, as much as 17% of Canadians own homes that are just within their budget (Figure 1).

FIGURE 1 – CANADIAN HOMEOWNERSHIP



Canadian Mortgage and Housing Corporation (2018) and Statistics Canada (2019)

As such, those at the CMHC threshold are the most likely of homeowners to consider more affordable living scenarios such as renting. As of the first week of June, 2020, the CMHC changed borrowing requirements because "COVID-19 has exposed long-standing vulnerabilities in our financial markets, and we must act now to protect the economic futures of Canadians" (Deschamps, 2020). As barriers to homeownership appear to be on the rise, high quality rental units are likely to be demanded. Workforce housing is a popular rental asset class among those that are gainfully employed but just fall short of homeownership (Haughey, 2002).

ESSENTIAL WORKERS & WORKFORCE HOUSING

While many Canadians have been asked to stay home during COVID-19, millions with essential jobs have had to work during the pandemic (Government of Canada, 2020a). Specifically, essential workers make up close to 40% of the Canadian population (Avenue Living, 2020a). According to the Government of Canada (2020b), essential workers span industries including energy and utilities, information and communication, finance, healthcare, food, water, transportation, safety, government, and manufacturing. These individuals have provided essential services to their communities in order to keep them safe and fulfill their basic needs.

The efforts of essential workers have not been overlooked, as many are now calling for pay increases (Britneff, 2020; Di Donato, 2020; Wherry, 2020). Some companies, like Avenue Living and Loblaws, were proactive in the early weeks of the COVID-19 pandemic, giving their essential workers wage increases (Toneguzzi, 2020; Wherry, 2020). After such calls and actions of some businesses, the Government of Canada has provided the provinces and territories $3 billion to boost the wages of essential workers (Global News, 2020). The Prime Minister stated that these "workers are risking their health to provide us with essential care and services, and we need to make sure that they are paid properly for the work they do every day. We're stepping up, and working with the provinces and territories, to give a much-needed wage boost to Canadians who are helping keep our country and economy strong during this difficult time" (Government of Canada, 2020a).

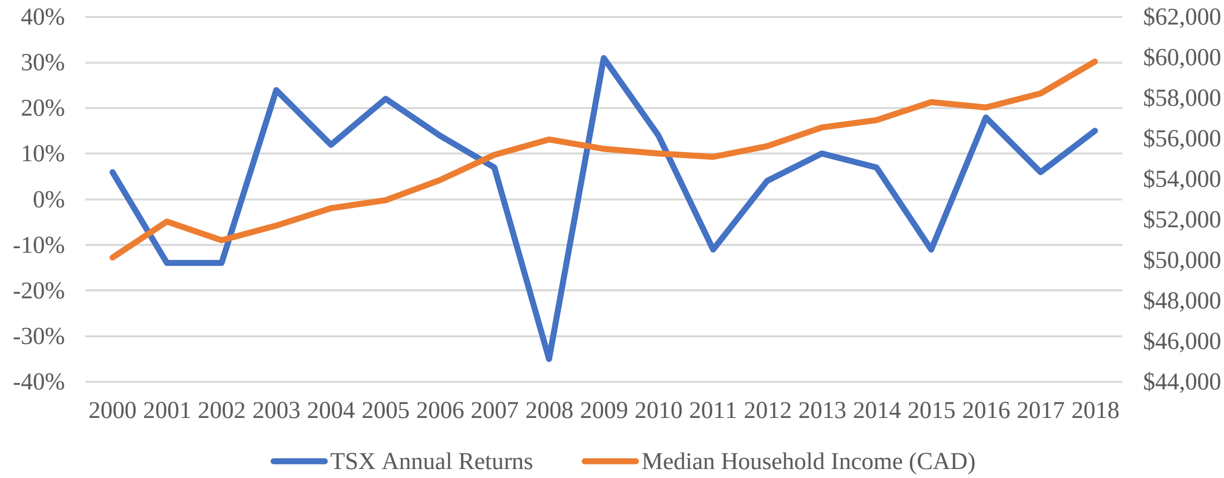
Some essential workers, including those in healthcare, are well compensated. However, several essential workers are considered to be underpaid (Britneff, 2020; Di Donato, 2020; Wherry, 2020). Although Wherry (2020) and others suggest COVID-19 may change how we define and compensate essential workers, many earn wages that are equal to, or less than, the Canadian median income. According to McQuarrie (2020), excluding those in healthcare, the average wage of essential workers is almost 20% less than employees in other industries. Despite essential workers being gainfully employed and realizing income increases in economic uncertainties (Statistics Canada, 2020a), many rent their homes as homeownership is simply not a financial reality.

Workforce housing is a term that has gained in popularity among real estate and housing institutions. The term workforce housing is generally understood as housing for those earning 60% to 120% of the area median income (Haughey, 2002). It is typically rented and occupied by essential workers, that earn more than minimum wage, but are unable or unlikely to purchase a home near their workplace (Haughey, 2002). According to Avenue Living (2020a), a western Canadian apartment building owner and operator, "workforce housing is geared to a city's 'essential workers,' who are the backbone of every city." Avenue Living (2020a) further suggests there is a "strong demand for workforce housing from the essential workers demographic" as they are looking for "quality, safe housing, and will respect and treat the housing well." Therefore, rent collections from this real estate asset class are highly dependable.

THRIVING IN ECONOMIC DOWNTURNS

As per Haughey's (2002) definition, many essential workers living in workforce housing have earnings close to the Canadian median household income. Comparing the last two decades of economic cycles to the inflation-adjusted Canadian median household incomes, the data suggests incomes are consistent and, in some cases, increase in economic downturns (Figure 2). From 2000 to 2018, the Toronto Stock Exchange (TSX), showed annual gains and losses of more than 30%. In three of the five economic downturns, inflation-adjusted median household income increased. In 2001, when the TSX losses were 14%, median household income increased by 3.5%. In 2008, one of the largest recessions on record with a TSX loss of 35%, the median household income increased by 1.4%. Similarly, in 2015, the median household income increased by 1.6% despite the 11% decrease in the TSX. Moreover, in the other two economic downturns of the 18 years, median household income remained relatively unchanged.

FIGURE 2 – TSX & MEDIAN HOUSEHOLD INCOME



Based on Statistics Canada (2020a) and Yahoo Finance (2020)

Despite the stock market fluctuations, inflation-adjusted Canadian median household income has steadily increased. Additionally, as many individuals living in workforce housing are essential workers and earn incomes comparable to the Canadian median, this real estate asset class is likely to garner consistent revenue from rent collections, regardless of the economic climate.

WORKFORCE HOUSING INVESTMENT

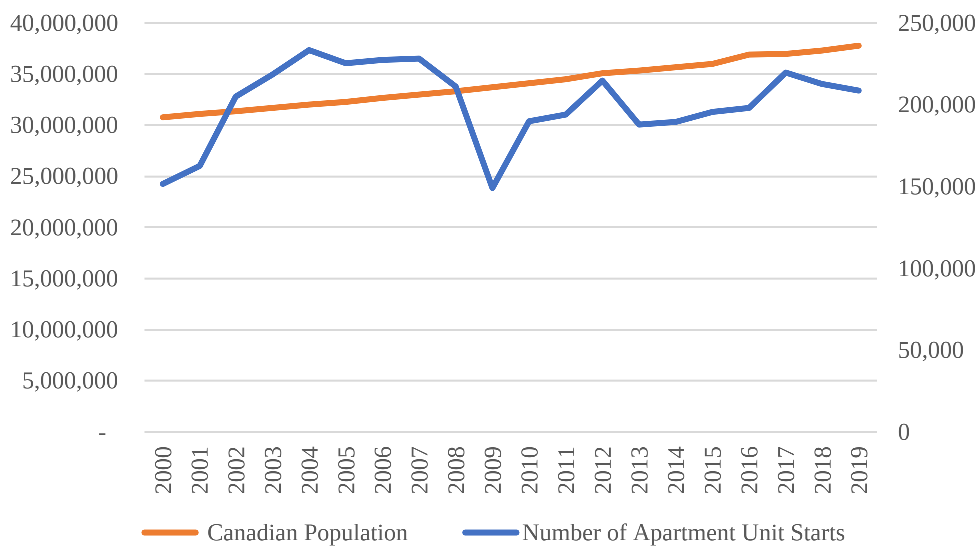
In times of crisis, consumer behaviour changes dramatically (Wilson, 2020). However, a steadfast priority in any economic climate is shelter. Based on Maslow's (1943) hierarchy of needs, physiological needs such as food and shelter are foundational. Maslow (1943) purports that physiological needs are fulfilled before any other need type. According to Reed and Crawford (2014), in recessions, consumers prioritize the fulfillment of physiological needs (e.g. paying rent) over all other need types. Similar consumer spending behaviour has been identified among households on employment insurance, as rent was shown to be the top prioritized expense despite limited financial resources (Ganong & Noel, 2019). The theoretical, and empirically validated, prioritization of consumers' physiological needs provides general investment confidence in residential real estate in times of economic expansion and contraction. However, some residential asset classes, such as workforce housing, present more specific advantages.

Multi-family rental properties in Canada are in high demand (Western Investor, 2019). According to Avenue Living (2018), workforce housing is "outperforming the multifamily asset class for several years, and it is expected to continue its performance in the near term, based on limited new supply and higher demand from a lack of alternative housing options." The demand for workforce housing assets is expected to increase due to population growth, immigration, urbanization, and homeownership affordability (Avenue Living, 2018; Statistics Canada, 2015).

Furthermore, many assets in this class are aging, undervalued, and present an opportunity for renovations and upgrades to increase rental revenue from dependable and likely long-term tenants.

Although new multi-family residential properties receive rent premiums as compared to older assets, they are likely to have more stringent cashflow requirements and higher vacancy rates (Avenue Living, 2019). Furthermore, many essential workers that cannot purchase homes in Canada would also be unlikely to rent these new residential properties due to rental premiums. There has been, and we will continue to see, demand for workforce housing by essential workers. Specifically, the number of new apartment unit builds, or starts, fluctuates as the Canadian population continues to increase (Figure 3).

FIGURE 3 – CANADIAN POPULATION VS. APARTMENT STARTS



Trading Economics (2020) and Statistics Canada (2020b)

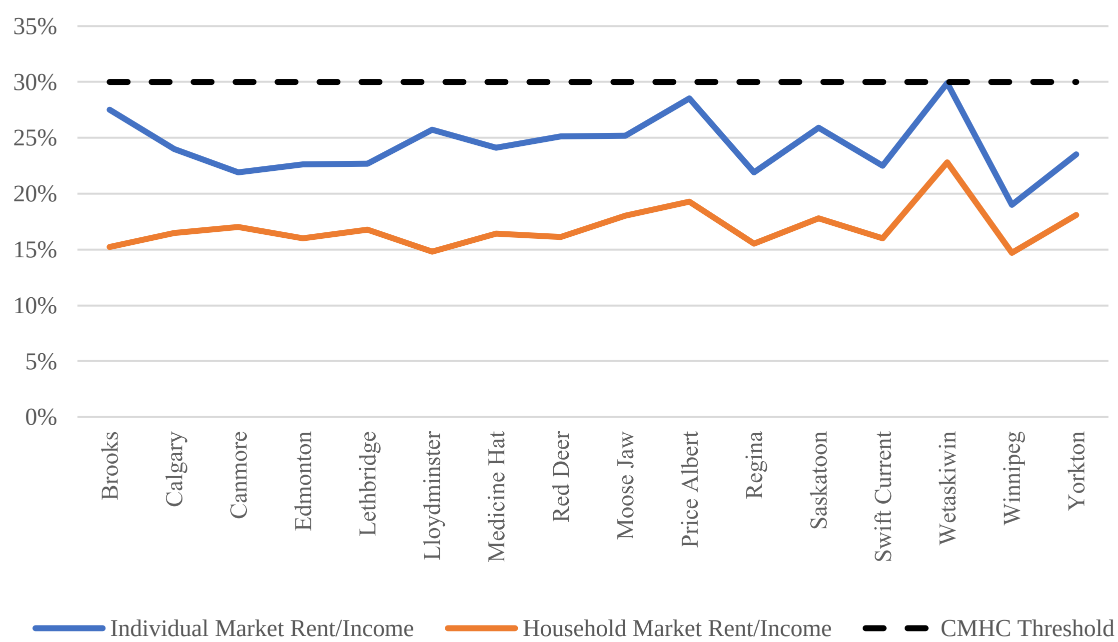
The "purpose-built multi-family rental market in Canada is largely made up of older properties" (Avenue Living, 2019). "The multifamily asset is a type of residential structure with more than one dwelling residence in the same building. Each building is classified from Class A to Class C" (Avenue Living, 2018). Nearly 90% of all assets in Canada are categorized as non-premium in the Class B or Class C. These assets were mostly constructed before 1979 and present several key advantages over newer and luxury properties. Some advantages include great locations, of which are often proximal to essential workers' employment, low vacancy rates, larger unit sizes, affordable rents, and opportunities for improvements that enhance rentability. Specifically, an opportunistic investor can acquire and renovated these assets for less than the cost of a new build. In addition, despite the limited supply and growing demand, there are still opportunities for those investing in workforce housing.

Given most of these assets were constructed several decades ago, 80% are owned by individuals, and 20% are owned by institutional investors (Avenue Living, 2019). "During the recent economic downturn, private owners suffered from receiving lower rental rates and higher vacancy rates, while deferred capital maintenance accumulated. In addition, many of these owners are transitioning through intergenerational events as primary stakeholders reach retirement age" (Avenue Living, 2019). As such, there is great potential to acquire these types of properties and consolidate. Even for those strategically, and heavily, invested in this asset class, there are significant market opportunities as the long-term demand looks promising.

INVEST IN THE EVERYDAY

Although homeownership is appealing to Canadians, many households do not own their dwellings due to several constraint variables. Given data suggests many Canadians are within the CMHC's (2018) affordability threshold and homeownership is likely to become more difficult (Deschamps, 2020), it is expected that individuals and families will look to renting as opposed to owning. Workforce housing provides an affordable and high-quality alternative to homeownership. To explicate this point, a comparison of key Alberta and Saskatchewan rental markets show that rent as a percentage of income, both individually and per household, is less than the CMHC's (2018) mortgage affordability threshold of 30% (Figure 4).

FIGURE 4 – RENT/INCOME VS. CMHC THRESHOLD



Avenue Living (2020b) and Canadian Mortgage and Housing Corporation (2018)

Occupants of workforce housing are highly dependable, have steady incomes, and are often essential workers. In economic downturns, essential workers often experience increase incomes and even thrive financially. Essential workers are more likely to rent Class B and Class C properties for many of the same reasons that they do not buy homes.

Compared to other asset classes, workforce housing presents a number of advantages including locations, unit sizes, vacancy rates, rental prices, and growth opportunities. While many real estate investors have their sights set on developing and acquiring new premium residential assets that have high-income tenants, investing in the *everyday* may be a more strategic and profitable endeavour.

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