HOUSING RESEARCH REPORT

Optimizing Demand and Supply Side Housing Assistance Programs

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Carleton UNIVERSITY

Optimizing Demand and Supply Side Housing Assistance Programs

A Background Brief

Prepared for Canada Mortgage and Housing Corporation

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Executive Summary:

This report examines the historic context for supply side and demand side approaches to housing assistance. The report provides historical context for supply-side approaches in Canada and examines trends in rental housing and affordability.

- housing starts are sufficient in total volume to meet demographic requirements,
- new supply is not creating a sufficient numbers of rental units in the market, and is not addressing a shortage of low rent options.
- Despite 275,000 rental housing starts (2001 – 2015) *net* growth of purpose built rental is only 85,000 units.

Furthermore, the report demonstrates that 58% of renters paying below market rents are still in core housing need, and suggests the gap between what these low income households can afford (at 30%) and what they pay may not be large. Demand side options could play a role in addressing this gap.

The report outlines the prevailing arguments on the advantages and limitations of a supply and demand approaches and asks a series of questions to tease out the accuracy and validity of assumptions about housing affordability and adequacy of the housing supply in Canada to better understand the problem that is being solved through affordable supply or rent subsidy approaches.

The Canadian approach has typically been a hybrid approach that blends creation of supply with demand side subsidies to reduce the rent. In many of social housing units, rent is reduced to a 25 30% rent-to-income (RGI) scale through a rent subsidy. Internationally, the trend is a separation of supply and demand mechanisms with an evolution of assistance into two distinct sets of programming, one focused on supply, at economically sustainable rent levels and the other on improving individual capacity to pay a modest rent.

The context and nature of the housing challenge have evolved and the traditionally divisive and somewhat ideological premise that supply and demand options were mutually exclusive have largely evaporated. There is room to consider how each can be used to address the gap in affordable rental housing supply in Canada.

The value of the not for profit sector in continuing the long term asset ownership and, potentially, renewal of affordable housing units is important in the context of the diminishing supply of affordable rental housing in the market. Armed with appropriate public support (grants, loans and potentially some tax mechanisms such a vendor tax credits) there could be an expanded role for the non-profit sector to emulate the practices of REITs and institutional investors – to acquire existing assets (especially smaller to mid-sized properties), invest in the rehabilitation and retrofitting and then preserve the existing affordability.

Résumé

Ce rapport examine le contexte historique dans lequel s'inscrivent les approches de l'aide au logement fondées sur l'offre et la demande. Il commence par fournir le contexte historique de ces approches au Canada puis examine les tendances du logement locatif et de l'abordabilité.

- Le nombre total de mises en chantier d'habitations est suffisant pour répondre à la demande démographique.
- L'augmentation de l'offre n'est pas suffisante sur le marché locatif; elle ne permet pas de réduire la pénurie de logements locatifs à prix modique.
- Malgré les 275 000 logements locatifs mis en chantier entre 2001 et 2015, la croissance *nette* de l'offre sur le marché locatif primaire n'a été que de 85 000 unités.

De plus, le rapport montre que 58 % des locataires payant un loyer inférieur au loyer du marché éprouvent encore des besoins impérieux en matière de logement. Ce taux laisse entendre que l'écart est probablement mince entre ce que les ménages à faible revenu peuvent se payer (30 % de leur revenu) et ce qu'ils paient. Les options liées à la demande pourraient s'attaquer à cet écart.

Le rapport présente les avantages et les limites des approches fondées sur l'offre et la demande aujourd'hui. Il pose une série de questions pour déterminer si les hypothèses sur l'abordabilité des logements sont exactes et valides et si l'offre de logements au Canada est adéquate. Le but est de mieux comprendre le problème auquel tentent de répondre les approches reposant sur l'offre de logements abordables ou le supplément au loyer.

L'approche canadienne a toujours été hybride, c'est-à-dire qu'elle agit sur l'offre et la demande au moyen d'une croissance de l'offre et de subventions pour réduire le loyer. Pour de nombreux logements sociaux, un supplément au loyer vient réduire le loyer afin que celui-ci ne dépasse pas 25 à 30 % du revenu du locataire; on parle alors de loyer proportionné au revenu. Sur la scène internationale, la tendance consiste plutôt à séparer les mécanismes de l'offre et de la demande et à envisager l'aide au logement selon deux programmes distincts : un axé sur l'offre, où le loyer est économiquement viable, et l'autre axé sur l'amélioration de la capacité individuelle de payer un loyer modeste.

Le contexte et la nature du défi à relever dans le domaine du logement ont tous les deux évolué. La prémisse traditionnelle, quelque peu idéologique et axée sur la division, veut que l'offre et la demande soient mutuellement exclusives. Or cette prémisse ne tient à peu près plus. Il est temps de se demander comment chaque côté de l'équation peut contribuer à combler les lacunes dans l'offre de logements abordables au Canada.

Vu la décroissance de l'offre de logements locatifs abordables sur le marché, le secteur sans but lucratif joue un rôle important dans le maintien de la propriété d'actifs sur une longue durée. Il pourrait aussi peut-être assurer le renouvellement du parc de logements abordables. Avec l'aide publique appropriée (subventions, prêts et peut-être des mécanismes fiscaux comme des crédits d'impôt pour les fournisseurs), le secteur sans but lucratif pourrait être encore plus

présent en adoptant les pratiques des fiducies de placement immobilier (FPI) et des investisseurs institutionnels. En effet, cela leur permettrait d'acquérir des actifs existants (en particulier des propriétés de taille petite à moyenne), d'investir dans leur modernisation et leur remise en état, puis de protéger leur abordabilité.

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1. Introduction

There has been a long debate in housing policy circles about the relative merits of building homes (supply approach) to assist low-income households deemed to be in need, versus simply providing some form of allowance to assist them in paying their rent (demand approach).

Historically supply and demand options were perceived and considered as alternative options. The evidence, partly in Canada, and more widely internationally has transitioned to identify these as complementary measures. That said, depending on policy objectives (especially the issue of supply vs. demand) there are aspects of each approach that are more effective in achieving certain objectives and outcomes.

The purpose of this paper is to help contribute to public policy thinking about the relative advantages and disadvantages of "demand side housing assistance" and "supply side housing assistance" for affordable housing. The paper is also intended to advise public policy thinking about circumstances where it is best to use one form of assistance over another as well as when it may make sense to use both simultaneously.

Some definitions

Demand Side Housing Assistance refers to a variety of assistance mechanisms where funds are provided to a household to assist with the payment of its housing expenses.

This form of assistance is labelled "demand side", referring to the interplay between the demand and supply of housing. "Demand Side Housing Assistance", as the "housing" qualifier suggests, excludes general income support programs where the assistance is not related to the housing circumstances of the household. "Demand Side Housing Assistance" can generically take two forms: (i) a housing or rental allowance provided to a household and which is often portable; or (ii) a rent supplement, which may provide assistance in covering rent but is project linked, usually via a contract with a landlord.

"*Supply Side Housing Assistance"* refers to financial support or incentives provided to investors in residential building/units to stimulate the construction of housing and thus to augment the "supply" of housing in a market.

Purer forms of supply stimulus (such as former assisted rental programs in the 1970's in Canada) are directed primarily to private, for-profit proponents and do not necessarily link incentives to conditions such as holding rents low. In some instances, supply side measures have also incorporated implicit or explicit assistance directed to meeting low income need or to holding rents below a market level.

While notionally identified as a supply program, non-profit housing in Canada is in fact a hybrid approach – they seek to achieve two policy objectives: add new supply and set rents (an implicit rental allowance) at an affordable level to respond to ineffective demand.

Supply-side assistance in its hybrid form may be limited to publicly owned, or open to community-based non-profit organizations and/or to privately owned organizations.

In many other countries demand side assistance is "stacked" or provided in tandem with supply side assistance. In such instances, the public policy goals of the "supply side" assistance are directed towards enhancing the aggregate supply of housing; whereas the "demand side housing" assistance would target households with lesser means with the public policy goal of enhancing housing affordability amongst more modest income households.

2. Traditional rationale for supply programs

In Canada and internationally, early policy approaches predominantly focused on supply and building new housing to meet rapidly expanding demand in the post war period. During the war years there was a cessation of house building activities as resources were directed almost exclusively to wartime production. Thus there was a backlog in housing supply. This was immediately challenged by the transition to a post war recovery and economic expansion.

Demand arose from returning veterans, a high volume of new migrants, and related new household formation. With a substantial under supply of housing, policies and programs were implemented both to create the necessary institutional infrastructure (housing technology and standards, production, financing, legal frameworks like land titling, and transaction mechanisms etc.) and to directly intervene in the market (e.g. via CMHC).

While only a secondary consideration, some efforts were directed toward ensuring housing at moderate cost/rent for lower income households and thus a state directed public housing model emerged in part influenced by similar models in European and commonwealth countries. In the absence of an established housing system and industry in Canada, governments were pro-active and directly involved in many activities now considered private market functions.

The scale of public provision was much larger in European countries where cities and housing stock had been physically destroyed. As such, one legacy is typically a much larger public and social housing stock in many Western European countries compared to those like Canada, the US, Australia, where there was no such destruction, and thus a smaller requirement to replace lost housing.

In wartime industrial areas in Canada and the US there had been quickly built accommodations for wartime workers, much poorly built and in need of replacement and so called slum clearance programs were designed to replace these areas, sometimes with new publicly owned and managed housing. Initially this was intended for moderate-income working families – it was not initially targeted to low income households in need.

As institutional frameworks and a formal housing markets matured, the nature of housing problems evolved. Among other things, issues of market failure left some households unaddressed, notably those lacking income and effective demand.

Thus public interventions shifted their focus from market making to supplementing or complementing and enabling. In overview, the key policy drivers were:

1. Health and safety – slum clearance and rehousing
2. Demographic and economic boom – crowding out of low cost supply
3. An absolute shortage of supply/shortage of low rent supply
4. Special Needs and Non Market Areas.

The outcomes of this shift were a more narrowly targeted provision of publicly developed housing for lower income households, and subsequently as public housing became increasingly associated with concentrations of poverty and ghettoization, a shift to development of low rent "affordable housing " via community based non-profit and cooperative associations.

As noted earlier this later form of social housing supply was not solely a supply approach, it was intended to address affordable need. Initially this was developed with breakeven rents. However as costs increased (in the mid 1970's), these breakeven rents were no longer low enough to be affordable. In order to ensure these rents were affordable to low income households it was necessary to layer in some ongoing subsidy. Initially these were provided as separate rent supplements stacked on non-profit or co-op programs. Subsequently (beginning 1978) rent subsidies were combined into a single program (again supporting non-profit and cooperative development). To the extent that the subsidies were paid to the operators of the project and were intended to ensure that the project was viable even with low tenant contribution, this remain categorized as supply side programs.

3. Current rationale for supply approaches

Overtime, the imperatives for direct public provision of housing have shifted. In particular, as the housing industry in all centres matured it produced a sufficient quantity of new housing to meet ongoing demand.

Today, if we compare the potential housing demand, based on population and household formation (including both domestic and immigrant households) there is a reasonable balance between housing demand and supply in Canada. Projected household growth between 2011 and 2016 was between 150,000 to 170,000 households per year; actual starts over that period averaged 178,000 per year. There are some exceptions with short-term disruptions and some unique market conditions (e.g. Vancouver constrained land supply), but in general there is a reasonable supply-demand balance.

That said, there remain some policy reasons to facilitate and encourage general supply and also to redirect the form of supply to more effectively respond to emerging demand and requirements. These include:

- Ongoing population growth and resulting housing demand;
- Demographic and socio-economic change (e.g. smaller households, aging population);
- Some practices wherein landlords may select what they perceive to be lower risk working tenants (e.g. when employment and income checks reveal dependence on income or rental assistance), which implicitly result in discriminatory treatment and exclusion of lower income

and benefit dependent tenants (public and non-profit landlords may be less adverse, which creates a basis for direct supply and public/community-based landlords);

- A mismatch in the form of supply versus demand, notably the issue of insufficient purpose built rental construction (compared to the number and share of renter households);
- The need to replace aging and obsolete housing stock (e.g. homes in poor condition, homes with poor energy efficiency, or homes that underutilize their land footprint);
- Place making and renewal - neighbourhood intensification and redevelopment;
- Market supply is not affordable to low-moderate income households and therefore it is necessary for government to intervene to help lower the cost or rent of new homes to a more affordable level. In a purist perspective this is not necessarily a supply approach – government could provide a similar level of financial assistance to enable someone to live in existing housing.
- Housing required for special needs populations, which may not be created in the market (with exception of seniors care facilities). Notably this includes housing appropriate for individuals exiting homelessness and shelters who require smaller units together with ongoing supports and minimal (sub market) rents.
- Supply programs create assets, and provide an ongoing flow of housing services to a series of beneficiaries over time. They also have real estate value which, depending on rent levels and cash flow, can potentially be leveraged in the future to fund renewal or additional housing.

3.1. Limitations of Supply approaches

A key limitation of this approach is the cost per household assisted. Today, it requires upwards of $100,000 (and in higher cost centres over $150,000) in subsidy to facilitate new development at moderately affordable rents. With constrained capital budgets few homes are constructed and only one household can be assisted (although if their situation improves they may move on and enable a flow of tenants over a lifetime). With low volumes of new social housing, juxtaposed against a long waiting list, this creates a lottery effect and issues of horizontal equity.

Once built the unit is in a fixed location, which over time may not be the most convenient for all tenants relative to their place of work or supports. But to retain assistance they may remain in the unit.

In addition to initial cost there are ongoing operating costs and as the asset ages a need to reinvest in capital replacement (windows, roof boiler etc.).

Social housing portfolios with ongoing subsidy require an administrative regime to ensure that costs and rents remain consistent with program intent, which add to administrative costs both for the provider (via reporting requirements) and for the funder (compliance monitoring costs).

When the supply program is combined with an affordable (often income based, RGI) rent the rental revenues may be low and insufficient to permit sound asset management and to facilitate future leverage. A property where the net rent is below operating expenses is not an asset; it is an ongoing subsidy liability.

4. Rationale for demand approaches

The primary rationale for demand side options is to specifically address the issue of affordability. Where a household is deemed to experience an affordability challenge they have insufficient income to pay the rent without this consuming an excessive proportion of their income. The traditional benchmark of "excessive" is 30% of income, although in some jurisdictions a higher proportion has been adopted (e.g. in the US paying greater than 50% is considered to be in "worst case need, and in Australia is referred to as heavily burdened).

By supplementing capacity to pay, via a rental allowance, a household can have effective demand. That is, they are able to find and rent a home in the market. Under such an interpretation the demand side assistance can have a market impact and potentially stimulate a market supply response. In most cases, however, this does not occur. Typically the amount of the rental allowance is sufficient to provide some relief from high shelter cost burdens, but insufficient to create effective demand, especially at the premium price that a new unit is likely to command.

The counterpoint is of course that if the allowance is too large; it will have an inflationary effect on rents and will impose a higher subsidy expenditure on government. This effect can be controlled through the design of the assistance. Typically, this is a shared payment with the recipient required to cover some portion of the rent, which then provides an incentive to seek out the lowest possible available option that meets their requirements. (This is typically a percent of gap model, where the program pays for example 75% of the difference between 25% or 30% of their income and a maximum market rent).

A further rationale for demand side rental allowances is that they can assist households in their current home and to do so can provide immediate assistance versus waiting for a new affordable home to be constructed (potentially a 2-3 year process).

Rental assistance is aspatial – it can be used in a wide range of locations, and thus provides choice in where recipients can live. This can include the ability to locate nearer to place of employment or other specific amenities (stores, health facilities, public transportation, etc.).

Rental assistance can also enable recipients to remain in current location or even current dwelling (with additional rental subsidy), where they may have an established social network and supports from relatives, friends and neighbours. Conversely, supply programs create a unit in a fixed location, and to participate it may be necessary to relocate to that location (which may break the social network of other local links).

4.1. Limitations of demand side approaches

In and of themselves demand side rental assistance programs do not add to housing supply. However, as discussed later they can be an effective mechanism to indirectly support new supply.

Although demand-side programs can assist with affordability, unless there are inspection and condition standards associated with the assistance (and enforced at original commencement of the assistance) rental assistance programs do not ensure recipients live in sound and safe housing.

Therefore, households could continue to be in *core housing need* by living in inadequate or unsuitable housing.

While there is an absence of empirical evidence, some argue that demand side assistance (especially in a low vacancy, supply constrained market) can lead to rent gouging, and potentially to rent inflation.

5. Selecting policies fit for purpose – defining prevailing policy challenges

In selecting and designing policy approaches it is critical to first carefully assess the problem to which policies are being applied. In the current Canadian context some critical considerations include:

- Predominant problem is affordability
- Adequacy of current supply
- Price/affordability of new supply
- Dynamics of price change in existing stock
- Mismatch in current stock

Briefly each of these is reviewed below

5.1. Predominant problem is affordability

While the early post war policy concerns were related to an absolute shortage of supply, and to some degree the poor condition of rapidly built wartime worker housing, the nature of the housing problem has changed. Today Canada's housing industry produces a sufficient quantity of housing (relative level of housing requirements versus starts was noted earlier). The more critical concern today is affordability.

CMHC has developed and widely uses a methodology to assess housing need – those not fully served by the housing market (Core Housing Need). This assesses whether a households lives in poor quality housing (adequacy), whether it is living in crowded conditions (suitability), or whether it pays more than 30% for income (affordability) or any combination of these. It also removes households that are assessed to have sufficient income to acquire housing above these three housing standards.

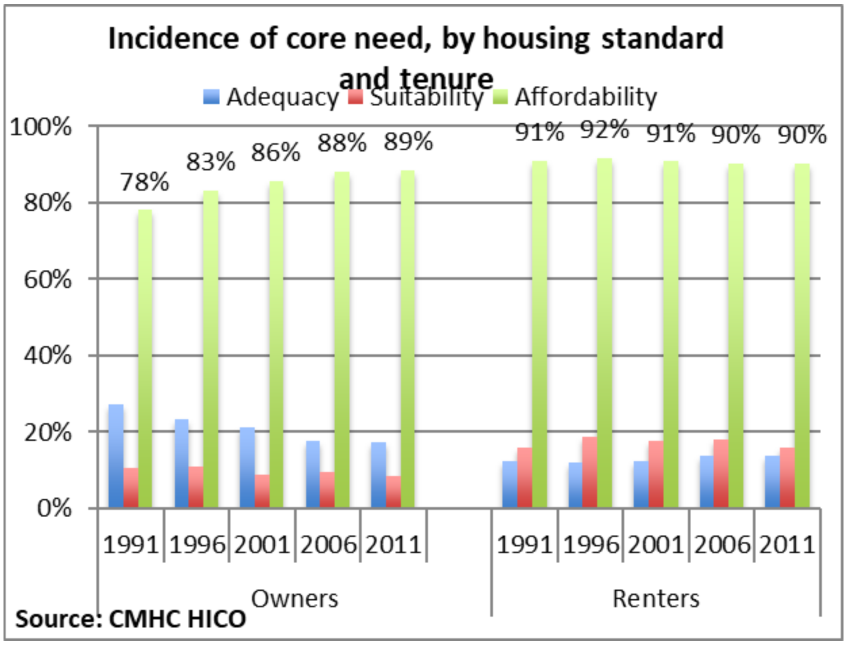


Figure 1: Core need trends

Looking only at households that are in core need and experience one or more of these defined problems it is found that the predominant issue relates to affordability and this situation has prevailed for over two decades (Fig 1). Among both owners and renters in core need the vast majority (90%) in need face an affordability issue (pay over 30% for shelter). Almost one-fifth have multiple problems, but usually one of these is affordability (for these reason, totals above will sum to over 100%). In some cases households unable to afford larger units experience a crowding (suitability problem) and others often by default "select" units in poor repair because they cannot afford better quality dwellings.

Both supply options and demand approaches can potentially respond to these needs, but for those only with an affordability problem a housing allowance may be more effective than supply-side approaches because it directly affects the individual household's ability to afford shelter costs.

5.2. *Adequacy of current supply*

CMHC monitors and publishes very comprehensive data on housing starts and completions, including built form and intended market as well as some additional data on rents and prices of that supply. This is available for all Census Metropolitan Areas and Census Agglomerations across the country.

Historically new housing construction has favoured ground-oriented dwellings, notably detached and semi-detached homes (Fig 2). Since 1990, apartments have averaged only 30% of all starts, but in 2015 this has reached as high as 48%.

In part this reflects intensification and a shift to apartment condominiums in higher cost markets. With an aging population, this may also reflect increasing demand from down-sizing seniors (who can downsize but remain as owners), as well as young new households seeking to jump onto the ownership ladder. It appears that the industry is responding to demand for smaller apartment type units although without comparing local demographics to actual output it is difficult to determine if the right type of homes are being added and if they are in the right locations.

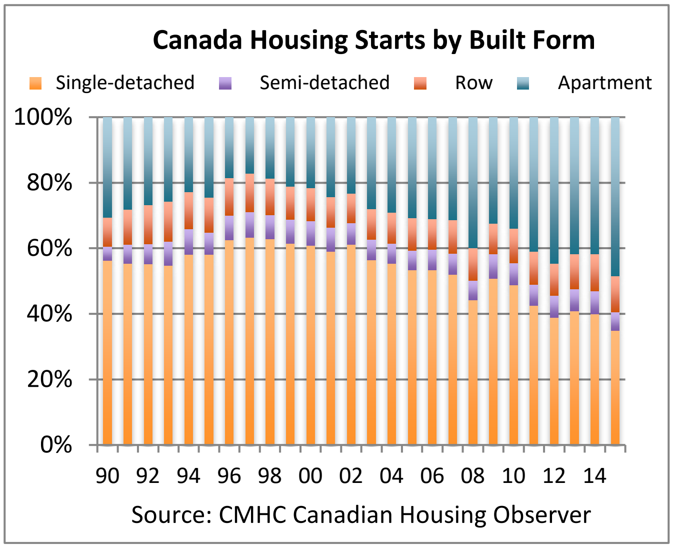


Figure 2a: Housing starts by Built Form

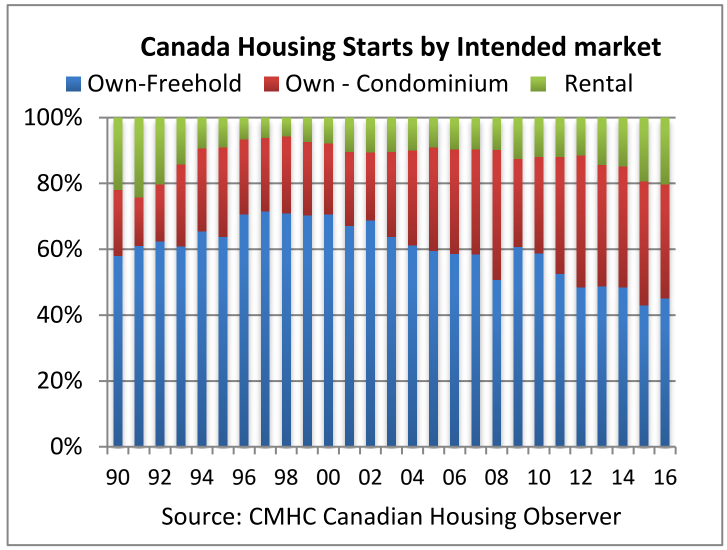


Figure 2b.: Housing Starts by Intended Market

While this varies marginally in different centres, the data reveal a long-term pattern that has strongly favoured the homeownership sector, with minimal levels of new purpose built rental housing.

While almost one-third of households are renters, only 11% of starts since 2000 have been intended for rental use. In part reflecting the increase in apartments, there has been a small increase in the share of rental starts up to 19% in 2015.

Rental options are augmented by investors purchasing dwellings and condominiums as investor landlords and thereby adding to rental supply. Across the 11 larger cities surveyed by CMHC, rented condominiums range from 15-35% of all condominiums (but these typically have rents well above the overall market average, so this is seldom affordable supply). Many dwellings ebb back and forth between being owner occupied and tenanted.

As a general observation, new housing starts, while sufficient in total volume to meet demographic requirements are not creating sufficient rental options. This issue is more acute in certain markets and reflected in very low rental vacancy rates. Nor is new supply addressing a shortage of low rent options.

5.3. Price/affordability of new supply

With the predominant policy concern one of affordability, data and insight into the pricing of newly constructed housing is needed to help monitor this issue and to help shape policy responses in the event of market failure.

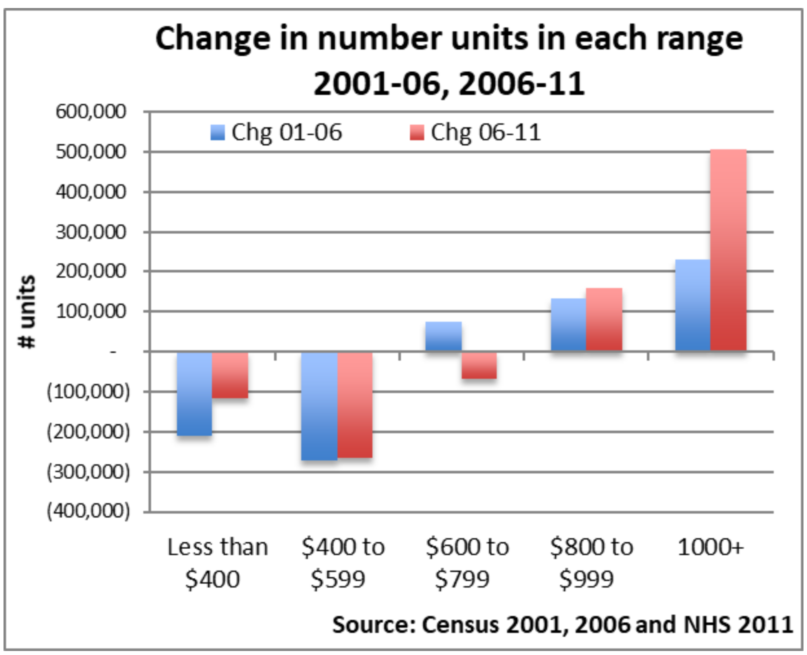
The starts data provides some insight into the price levels of new supply, albeit only for newly constructed single-family detached and semi-detached homes (now less than half of all starts). Similar data for condominium (row and apartments) is not published. Generally, the purchase price of newly completed single-family detached and semi-detached units is above the existing median home price. So new additions to stock while creating supply and thereby having some market influence, do not add many lower priced/rent affordable homes.

Separately, in the rental sector, there is no data on the rent for newly completed units, although once these are stabilized one year after completion they are added into CMHC's rent survey. This provides data on rents by period of construction and aggregates units built in the past 10 years (but does not separate out individual latest years). Rental units completed in last 10 years (excluding those under IAH subsidy programs) tend to have rents well above (usually at 30-40% higher) the overall rental average in each local market.

While there will be some moderately priced homes constructed (and in the multi residential condominium form these can be at lower price ranges), in the main new supply does not generate affordably priced homes either for sale or rent.

It is also important to note that new starts (at roughly 180,000-200,000 homes per year) add less than 2% to the existing stock (which in 2011 was 13.3 million dwellings). Availability of options at low to moderate rents and prices is dominated by older existing homes. Accordingly intelligence and insight into the existing stock is critically important.

5.4. Dynamics of price change in existing stock



Within the existing stock of some 13 million homes (of which 4 million are rented) there is an ongoing shift as properties are purchased and sold. In some cases this includes shifts between tenures. Homes may be rented or occupied by an owner with a rental apartment in a secondary suite, but a new owner wants use of the entire property. By the same token some new owners seek a "mortgage helper" and rent out part of their home, adding rental supply through secondary suites.

The overall change in rental stock does however tend to reduce the availability of lower rent options. Census data on rents paid reveals the change in the rent distribution over time and clearly reveals a trend of reduced availability in the lower rent ranges and growth at higher rent levels. In the decade from 2001-2011 over 860,000 rental units, representing one-fifth of all rentals moved out of lower more affordable rent ranges (below $600 per month). [1]

[1] This is not adjusted for price/rent inflation.

This occurs in part through demolition and replacement, especially in cities where intensification is occurring. Typically the units lost were lower-rent while replacements are condominium units or higher-rent rental properties. In some cities rental units have also been lost as entire properties have been converted to condominiums and sold to individuals (although this has contributed to some lower-cost entry-level ownership).

Another notable phenomenon is the acquisition of “under-performing” rental properties by institutional investors and REITs who then undertake some modernization and rehabilitation with the consequence that rents subsequently increase, often above more affordable levels that may previously have existed. This generally involved larger structures of 100 units or more.

In the formal rental section of purpose built structures, as monitored by the CMHC rent survey (accounting for 1.9 million of the 4 million rented homes) the total number of rented units actually declined between 2001 and 2011 (reduced by 75,000 units) but grew between 2011 and 2015. In 2015 this purpose built universe is 85,000 units larger than it was in 2001. However over the same period total rental starts exceeded 275,000 units, suggesting that some 190,000 purpose built existing units were removed – most likely those at lower rents.

5.5. Mismatch in current rental stock

While the overall number of homes and level of new home construction is generally in balance with demographic requirements there is a significant mismatch in the price level and availability of existing housing. Given the accepted norm that a household should not pay more that 30% of their gross income for shelter we can examine how well the existing stock of housing meets existing requirements.

The census (National Household Survey) in 2011 provides the distribution of renters by rents actually paid and by income level. Using the 30% norm we can convert income bands’ affordable rent levels and compare this to the number of units in each related rent band (some interpolation is required as the rent ranges do not precisely align with income bands).

Following this methodology the number of existing units by rent range can be compared with how many units would theoretically be required, if all paid rent at 30% of income. Not surprisingly this reveals a gross shortfall of rental units in the lower rent range, extra units in the mid ranges (these are however occupied by people spending over 30% who cannot find lower rent units) and a theoretical shortage of higher priced units (households could afford to pay rents of $1,500 or more but have found and selected lower cost units).

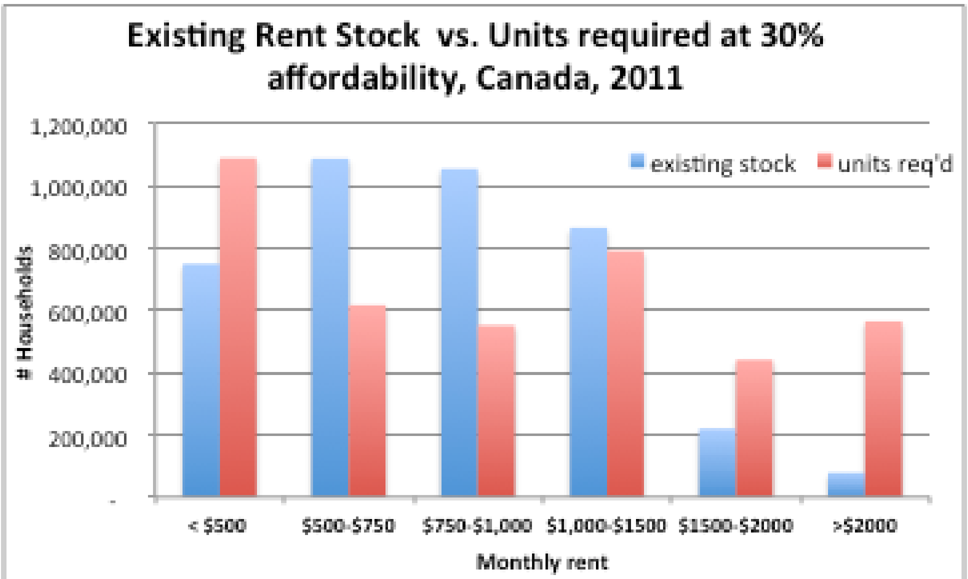


Figure 4: Rent and affordability mismatch, 2011

The second chart (Fig 5) shows the net shortfall or surplus in each rent range. However this underestimates those experiencing affordability problems. Not all low rent units are occupied by lower income households, and some lower income households live in more expensive units. In the mid-ranges while rents may exceed 30% of their income, higher income households (that can afford to pay over $1,500) may be crowding out lower or moderate-income households.

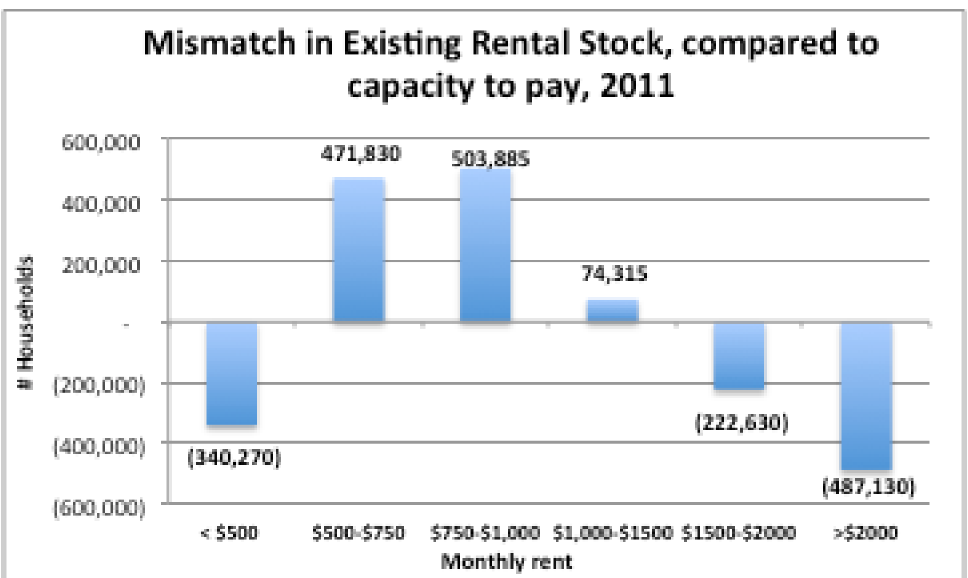


Figure 5: Shortage and surplus in rental stock, 2011

Given this mismatch but overall sufficient number of homes, there is an obvious role of rental assistance to lessen the burden of those in the $20,000-$40,000 income band paying a high proportion of rent for their housing.

This is a generalized assessment undertaken at a national scale. It overlooks the reality that more affordable units may not be of sufficient size for their household (i.e. a 4 person household cannot reasonably live in a bachelor studio). It also overlooks the fact that existing affordable (to them) home may be in a distant location (i.e. another province).

To correct for these methodological problems a customized data file was generated from the 2011 NHS data (Fig 6). This determines levels of affordability and required units taking into account both appropriate unit size *for each household* and the location of that unit. The term “norm rent” is applied here to identify the average market rent for a suitable and adequate unit for each household size.

Aggregating this data to the national level it identifies the mismatch in 2011. The number of affordable (below norm rent) units required is 1,273,785,[2] while the number in the stock is 2.226 million, a theoretical "surplus" of 953,103 units below norm rents

Comparison of Household Affordability with Actual Supply (2011)			
	Actual Rent Level is:		
Affordable Rent is:	Below Norm (1)	Above Norm	Total
Below Norm (1)	954,545 (2)	319,240 (3)	1,273,202
Above Norm	1,271,765 (4)	1,204,560 (5)	2,173,078
Total	2,226,305	1,523,800	3,750,105

Notes:

1. Norm rent based on National Occupancy Standards and regional median rents for appropriate units bedroom size; From NHS 2011.
2. HH cannot afford (@30%) to pay more than Norm Rent and currently occupies unit renting below Norm Rent.
3. HH cannot afford (@30%) to pay more than Norm Rent but currently does pay more.
4. Household could afford to pay more than Norm Rent but currently occupies a unit renting below Norm Rent.
5. Household could afford unit above Norm Rent and currently pays above Norm Rent.

Figure 6: customized mismatch

Indeed in 2011 there were 989,380 renter households in core housing need and of these 893,735 experience an affordability problem (CMHC HICO). Yet this custom analysis identifies only 319,240 paying above norm rents.

What this tells us is that the remaining 575,000 are in core need even though their rents are below the norm. However, this also suggests that the gap between what they could afford (at 30%) and what they pay is not large. This in turn indicates that options such as rental assistance might be quite effective in addressing the affordability problems faced by these households.

[2] This figure (1.273 million) should not be confused with the *core housing need* count of 1.5 million which also covers owners and adequacy/suitability problems. The number of "required units" (1.273 m) will include households currently occupying social housing, who might otherwise be in core need. It is estimated that 360,000 of these units are occupied by RGI households, presumably these will fall into cell (2).

6. Theoretical Underpinning of Supply and Demand Approaches [3]

The supply-demand debate is often contested on the basis of specific program designs respectively associated with each side: supply is seen as non-profit housing while demand is linked to housing allowances, including portable shelter allowances but also encompassing rent supplements tied to specific projects.

Leaving aside the particular program designs that colour the definition, the principle distinction between demand and supply approaches is:

- Under demand approaches, a household's total income is augmented, with a condition that this additional income is used in total or part to pay for housing. As a result, even with no change in the dwelling the household's shelter to income ratio will decline.
- Under a supply approach, the focus is on directly producing housing, or on stimulating production. The household income is not affected; it remains constant. In the indirect stimulation mode, affordability may ultimately be influenced by relative price decline (if broader induced supply is significant enough).

If one accepts this pure definition of each approach, it is evident that most versions of the non-profit program are not pure supply programs. The production of the unit is not in itself sufficient to address the policy objective of reducing affordability.

The rent for such units is reduced to a prescribed level based on a 25%-30% rent to income (RGI) scale; this subsidy implicitly represents a housing allowance. So in essence, non-profit is a blended or hybrid approach.

While both approaches, supply and demand, can and have been used to address affordability problems, each has a different impact on the benefit provided to a client as well as on the cost to government.

6.1. Impacts on consumer behaviour: demand approaches

A demand approach effectively increases income for non-housing use. This is achieved either with unrestricted cash transfer (e.g. income assistance) or through conditional transfers (e.g. shelter allowance).

At any given income level a household will trade off between shelter costs and non-shelter costs to maximize household utility. A CMHC analysis (CMHC, 1994) graphed actual household behaviour using Statistics Canada household expenditure data and showed that the income consumption curve is very steep: as income increases, very little, and progressively smaller proportions of the increase, is allocated to housing. In particular, low-income households typically expend a high proportion of income on shelter (in 2011 one in five renters paid more than 50%), limiting income for other necessities.

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[3] Discussion in this section draws from the 1994 paper and data and references had not been updated. The arguments remain valid in today's context.

Given this aggregate behaviour, and related economic theory, an unrestricted cash transfer would be expected to cause a marginal increase in housing consumption. However at the individual level, transaction costs and unavailability of the right bundle of housing goods at this marginally higher budget level may preclude moving. Moreover, while the aggregate trade off (income consumption curve) reflects actual behaviour, the shelter ratios at low-income levels are very high; suggesting that theory notwithstanding, low income households would still seek out lower priced housing if it were available.

In the case of a household occupying adequate and suitable housing, as is the case for 74% of renters in core need, an increase in consumption would not be desirable from a policy perspective. The funds are provided to improve affordability by increasing income to the point where shelter is 30%; but as soon as a single dollar is spent on more housing they exceed 30% (of the new assisted income) thereby counteracting the policy objective.

For this reason, in situ rent supplement, or a shelter allowance where current housing is one criterion for determining the level of benefit can control for change in consumption.

In the case of either unrestricted or conditional cash transfer, the cost to the government and the value of the benefit to the client are identical.

6.2. Impacts on consumer behaviour: supply approaches

In the supply situation, where the objective is to reduce cost with no change in income, the traditional, though not exclusive, approach has been to provide a new (non-profit) unit. Usually, the non-profit unit represents a higher level of amenity (especially when new, albeit modest) than the household could afford without assistance.

Moreover, in addition to the relatively higher level of amenity, the RGI scale lowers the cost. The value of the benefit to the client is therefore the difference between their RGI rent and the assessed market rent. The cost to government however, is the difference between the RGI revenue and full economic cost - so is normally higher than the benefit perceived by the client.

If given a cash equivalent transfer, our knowledge of the typical shelter to non-shelter trade off (Fallis 1993, CMHC, 1994) tells us that the household would likely not have chosen to spend the full amount on shelter because this would have sub-optimized non-shelter expenditures.

Hosios (1990) has demonstrated the degree to which the amenity level provided through a non-profit unit exceeds that which would be otherwise consumed by the household if they rent a unit at the average market rent (AMR) level. The study found that the assessed market rent (reflecting actual bundle of services/amenity and using 1988 national weighted average of non-profit unit rents) was 47% higher than the average market rent in the same location.

Since AMR underlies social housing client eligibility we can assume that using the RGI scale clients will pay no more than AMR, and many less, so this 47% reflects a minimum gap or amount of additional housing consumption enjoyed by the program clients. The same study found the economic rent of new units (once again weighted national average), which determines the cost to government to be 94% higher than AMR.

The "excess consumption" that has been identified under the supply (non-profit program) approach raises an important issue in the context of emerging trends promoting "enabling" strategies within social policy reform.

The preceding assessment of program impacts of housing consumption is a standard feature of housing economics. Fallis (1993) has attempted to integrate such analysis with labour market analysis, an area of study that examines the impact of income transfer on labour market participation. In integrating these two sets of economic literature, Fallis determines the relative impact of housing policy instruments (non-profit, housing allowances) and income assistance on labour market participation.

Fallis concludes that providing non-profit housing will reduce labour participation more than an equally costly (income equivalent) income assistance program. A housing allowance, depending on how its design affects the quantity of housing consumed will fall somewhere between the two other alternatives. However, minimizing the quality of housing provided (either by acquiring, or through rental allowances enabling improved access to modest existing rental properties) will lessen this effect.

This is an important finding if housing policy wishes to align itself with emerging emphasis on enabling, and maximizing incentives (or minimizing disincentives) to work and to achieve the stated goal of the federal 2016 Budget to “ensure that these [new] investments are most effective and to help the social housing sector achieve self-reliance”.

7. *Brief review of international practice – integrated approaches*

Across a wide range of countries there has been a clear shift in favour of demand side measures. Government expenditures on supply side construction programs have been steadily declining while those directed toward various types of housing allowance have had an upward trajectory (see for example Whitehead and Scanlon, 2011; Murie, 2013 and the UNECE 2015).[4]

There have been a range of reforms across Western Europe and elsewhere, including Australia and the US typically prompted by growing expenditures coupled with financial deficits.

Commenting more particularly on the UK, Gibb and Whitehead (2007) observed "the major objectives of fiscal constraint and related restructuring included bringing public expenditure under control, ensuring that a high proportion of housing costs were paid by the direct beneficiaries and targeting available subsidy more directly on those in housing need". In the UK context this has been reflected in expansion of their housing allowance (Housing Benefit), and a shift in the way new social housing is funded (reduced level of grant, an increased requirement in equity contributions from housing associations own reserves and an increase in rents, both in existing and new developments up to 80% of market levels).

A recent international review, also undertaken for CMHC (Pomeroy and Phinney, 2016) examined and summarized the supply and demand trends across six countries:

> *One of the key findings in this review is that there has been a very minimal supply response to persisting affordability issues. Governments have not reacted or responded in any significant way to fund, incent or facilitate new market or affordable supply. Where new supply programs continue, they typically create units that rent only slightly below average market levels, and arguably are not affordable to traditional clients of social housing programs.*
>
> *The related finding is that there has been a trend toward person/household subsidies, in various forms of housing allowance. These bridge the gap to make moderately affordable rental more affordable to lower income households (e.g. Housing Benefit (England), rent allowances (NZ, Ireland and Australia) and Sec 8 Vouchers (U.S.)).*
>
> *Effectively, the trend is to separation of supply and demand mechanisms with an evolution of assistance into two distinct sets of programming, one focused on supply, at rent levels that better support financing and development feasibility and long term sustainability; and the other on improving individual capacity to pay a modest rent to more directly address*

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[4] Kenneth Gibb & Christine Whitehead (2007) Towards the More Effective Use of Housing Finance and Subsidy; Social Housing in Europe II A review of policies and outcomes Edited by Kathleen Scanlon and Christine Whitehead, LSE; A Murie, Chapter 10 in J. Chen et al. (eds.), The Future of Public Housing: Ongoing Trends in the East and the West ;United Nations Economic Commission For Europe (2015) Social Housing in the UNECE Region Models, Trends and Challenges.

affordability, is likely a healthy trend. It creates opportunities to address affordability through multiple approaches

The notable fact about these trends however is not that demand side housing allowances have replaced or displaced new supply; rather they have been complementary and engaged as a key element of new supply initiatives.

With new supply programs creating supply at or just below full market rents, they have sufficient rental income to generate solid net income. This then creates capacity to borrow to cover capital costs (in contrast to earlier approaches in those countries that were more dependent on either capital grants or on direct government finance with subsidized repayment).

This establishes a more viable and sustainable development and asset management model, but does not respond to the issue of affordability for low-income households and the traditional clients of social housing. The affordability issue is however addressed more directly in enabling such households to be eligible, when needed, to receive a housing allowance that bridges the gap between viable rents and low or income related rent payments.

Separating the housing allowance from the dwelling and linking it directly to the household also creates portability and mobility. As such the dual approach can be effective in ensuring that assisted households are not constrained to alternative locations, for example to be close to employment and support or health services. It can also reduce or remove the disincentive to move and crowd out other needy households from the limited rationed assistance that a small stock of social housing creates. And depending how the housing allowance is designed and interfaced with general income support, it can reduce or remove work disincentives.

8. Conclusions

This brief overview clearly shows that as the context and nature of the housing challenge have evolved, thinking and practice have similarly adjusted.

The traditionally divisive and somewhat ideological premise that supply and demand options were mutually exclusive have largely evaporated.

The former favoured by an entrenched non-profit sector pre-occupied with adding new non-market supply and the latter heavily promoted by the private landlord sector, upset by competition from the publicly subsidized non-profit competition for tenants. Now the community sector actively encourages and accepts the use of rental assistance and recognizes the value of this policy option as a way to enable supply, rather than as a detraction from it.

It can also be observed that the community based non-profit sector has played an important role, in Canada and internationally, not so much as the builder of affordable housing but over time as effective owners. By holding assets under a non-profit mandate, they have helped to preserve the affordability inherent in stock developed at historically lower cost.

The value of the not for profit sector is not so much in development as in long term asset ownership and, potentially, renewal.

Armed with appropriate public support (grants, loans and potentially some tax mechanisms such a vendor tax credits) there could be an expanded role for the non-profit sector to emulate the practices of REITs and institutional investors – to acquire existing assets (especially smaller to mid sized properties), invest in the rehabilitation and retrofitting and then preserve the existing affordability.

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