The Myth of The Toronto Condo Bubble

by Brad J. Lamb

Brad J. Lamb

President, Broker, Brad J. Lamb Realty Inc.
CEO, Lamb Developments Corp.

Brad J. Lamb has been selling real estate in Toronto since 1988. In 1995 he founded Brad J. Lamb Realty Inc., a boutique brokerage operation specializing in urban condos, lofts, and townhomes. Since being licensed, Brad J. Lamb has sold over 21,000 properties for over $7.5 billion.

Currently with a staff of eight administrators and twenty-three licensed sales representatives, Brad J. Lamb Realty Inc. is the dominant name in the central Toronto real estate marketplace.

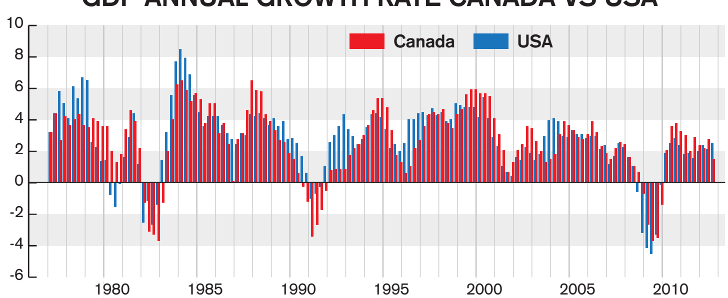
The company consists of two sales divisions, re-sale and new sale. A few of the over one hundred new projects handled exclusively by Brad J. Lamb Realty Inc. since 1996 are: *Toy Factory Lofts, Radio City, Spire, 550 Wellington Condominium and Hotel, 75 Portland, Quad, Gläs, Zen Lofts, Tip Top Lofts, East, Mozo, Garment Factory, The Printing Factory, Robert Watson Lofts, The Glasshouse, six50 King West, The Ninety, Parc, Cube, Flatiron Lofts, The King East, Worklofts, Theatre Park, The King Charlotte, One Eleven,* and *The Brant Park.* The company prides itself on excellence. Every sales representative and employee working at Brad J. Lamb Realty Inc. is a specialist offering a tremendous level of experience and knowledge to our widespread client list.

Brad J. Lamb founded Lamb Development Corp. in 2002 as a response to the city's demand for ethical modern development. His development company has developed almost 2,000 units in Toronto, Ottawa, and Montreal; projects such as *Gläs, East, Zen Lofts, East, 169 John, The King East, Mondrian, McGill Ouest, The East Market, Worklofts, Flatiron Lofts, Riverside Towns, Theatre Park, The Brant Park,* and *the King Charlotte, Mondrian, Gotham* and *SoBa* (in Ottawa), and *6th and Tenth* (in Calgary) with several more on the drawing board. Lamb Development Corp's mandate is to create beautiful and stylish homes in urban environments for the every man.

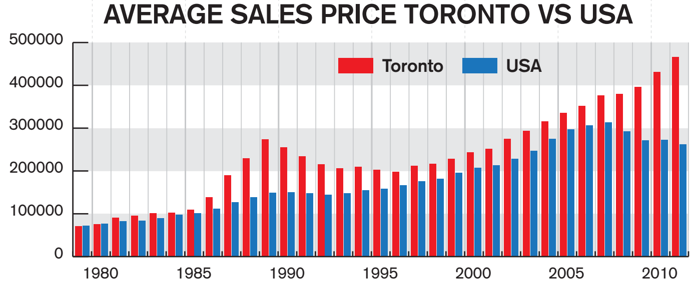
THE MYTH OF THE TORONTO CONDO BUBBLE

There has never been a significant North American real estate correction without an accompanying recession, as seen by the following charts which show both U.S. and Canadian GDP against average real estate prices. We can see the last three recessions were the only instances where any drop occurred in average prices (1982, 1991, 2008). In Toronto, a bubble bursting type of real estate correction did not occur in 1982 or 2008, but it did take place in 1991 where condo prices dropped by 40% and average prices dropped by 25%. This recession was particularly worse for Canada than the United States. You can see that while the U.S. suffered a mild slowdown through negative GDP, the average real estate price dipped only slightly in 1992 and recovered quickly. GDP bounced back quickly to a roaring 4% annually while in Canada it took 3 years for our GDP to match that of the U.S. The United States never had a deck clearing real estate event. The Canadian recession of 1991 was devastating to Toronto real estate. With bank rates at over 12.5% and unemployment eventually climbing to over 12%, this double whammy destroyed the real estate economy of Toronto and devastated the valuations of condominiums. Time to sell swelled to a year in some cases and prices plummeted by as much as 50%. It took until 2002, or twelve years, for average prices to regain what was lost in this recession. The United States took just 3 years until 1994 to recapture the slight losses earned through their

GDP ANNUAL GROWTH RATE CANADA VS USA

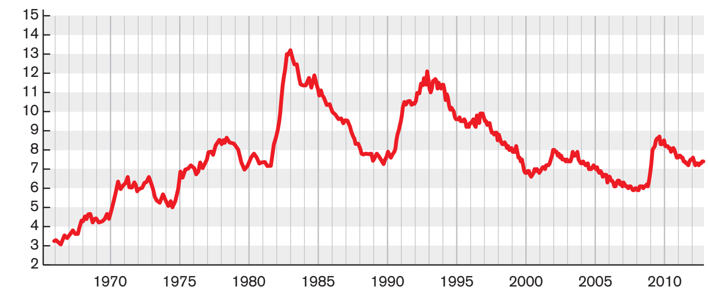


AVERAGE SALES PRICE TORONTO VS USA

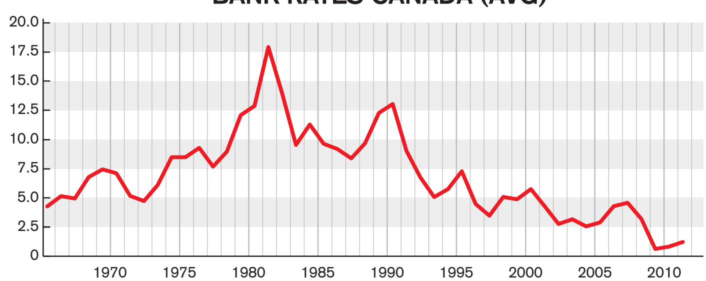


recession. If we look at the Canadian version of the "great recession" of 2008, we see that it was shallower and shorter than the U.S. version. Economic recovery was faster in Canada as well. The interest rate and unemployment rate charts show that we are still slowly recovering from this recession and are now most likely in the early days of a long period of economic growth. This would likely indicate upcoming higher prices and steady to higher volumes for real estate. There is no evidence of an imminent recession or real estate bust. It is worth noting that every time the U.S. has led Canada into a recession by a few months. We have never suffered a recession alone. So, if you believe that the U.S. is imminently headed into a new terrible recession then, "batten down the hatches," otherwise Toronto real estate prices are headed up.

CANADA UNEMPLOYMENT RATE



BANK RATES CANADA (AVG)



Based on known economic data, to see a significant drop in real estate prices we need a significant recession. The recipe for an imminent recession is a combination of the following; high economic growth, high inflation, high interest rates, followed by low unemployment – essentially, a runaway train that must be derailed. This is clearly not the case in North America or Europe. The above economic data indicates that a so-called real estate bubble is not imminently going to burst. It is more likely that the damage done in 2008-2009 is the extent of what will happen this time around. The train was derailed in 2008 in essence, and now it needs to build up speed and runaway to clear the path for the next recession. Based on past data, this will likely be at least 9 years from now and possibly as far away as 20 years. With the current extremely slow recovery, coupled with very low interest rates, and high government debt, it may take a very long time to rebuild the economy to "runaway train" status. Every recession brings different real estate

Theatre Park
King St. West Theatre Row
Toronto

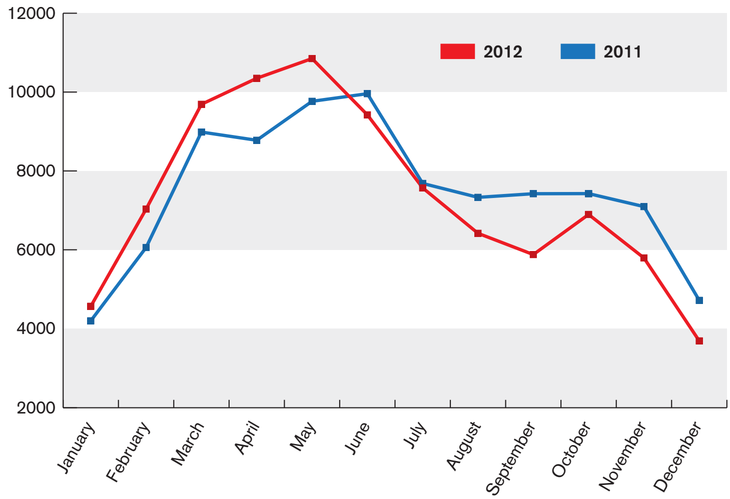
corrections. 1982 brought minimal real estate value changes to both the U.S. and Canada, 1991 was devastating for Canada (particularly in Toronto), but mild for the U.S. We know that the 2008 recession was a disaster for the U.S., but relatively mild for Canada and Toronto. I would argue that because 1991 was so mild for the U.S. real estate market it had more steam to release in the 2008 recession as it ran for 25 years with minimal disruption. Canada and Toronto's 1991 recession was so long and deep that real estate didn't recover until 2002. Toronto and Canada had less steam to release in 2008. This could be why our prices corrected marginally. The likely scenario for a real estate bubble bursting will be around the start of negative growth, significantly higher interest rates, rising inflation, and significantly rising unemployment. It will likely be precipitated by explosive growth of GDP, interest rates, employment, and inflation. Fear a real estate bubble when Canada strings together a few years of 4+% economic growth in GDP.

RESALE ANALYSIS

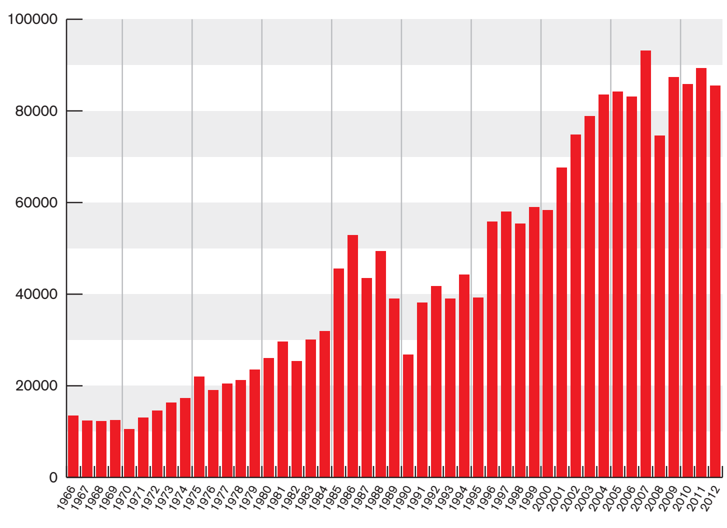
MLS SALES 2012 VS 2011
Recently, the Toronto MLS has been recording an approximate 10% drop in sales volumes and smaller increases in average pricing. The condominium MLS data shows a small decrease in values in the 1-2% range.

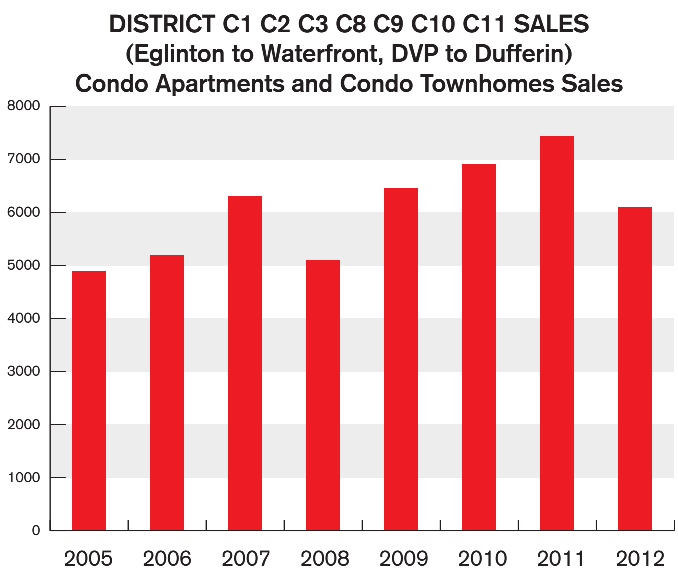
MLS RESALE TOTAL
Overall, 2011 and 2012 will be very similar in total sales. The main observation for 2012 was a spring surge and an autumn fall-off. Why did this happen? The Federal government changed the CMHC high ratio amortization rate from 30 to 25 years and raised the down payment requirement for $1.0 million+ properties from 5% to 20%. This motivated first-time buyers and $1.0M+ buyers to beat the legislative change and buy in the spring. This excess volume of spring buyers created a reduction in autumn buyers. Based on the MLS data above, 2012 will be the fourth best year in the history of Toronto MLS, a clear sign that prices are not correcting into a bubble-style of collapse.

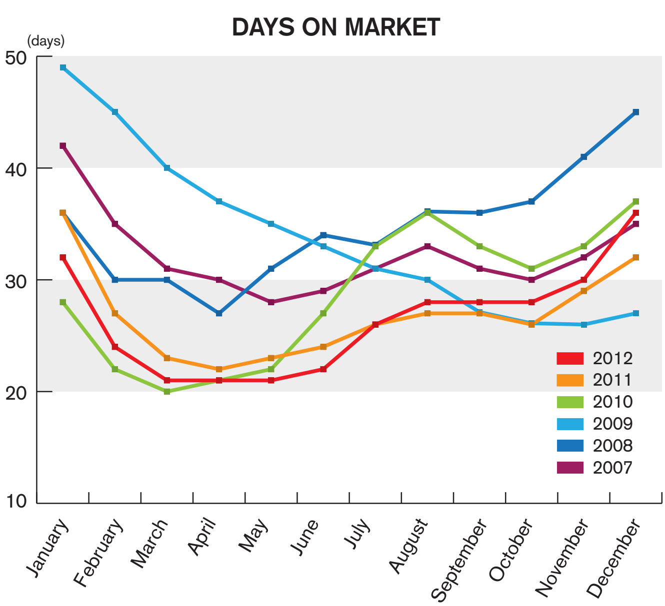
MLS SALES 2012 VS 2011



MLS RESALE TOTAL







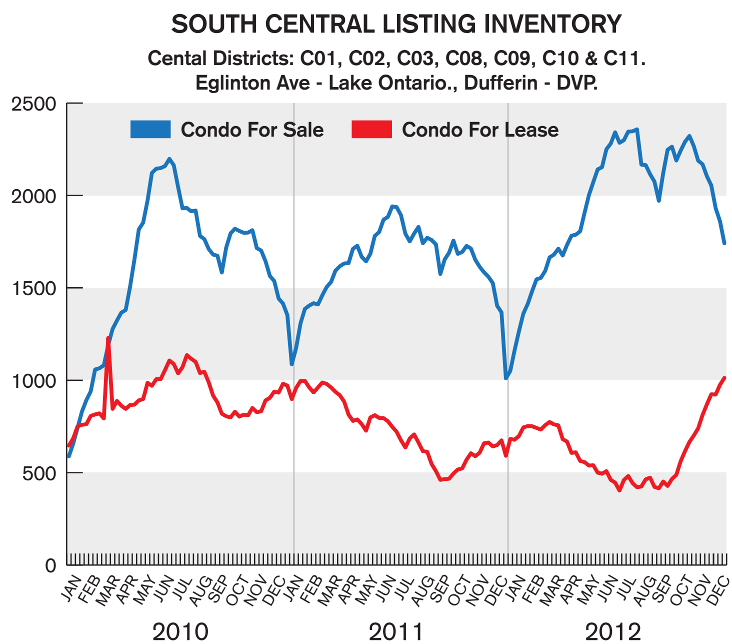
DISTRICT C1-3, C8-11 SALES

This graph shows that central Toronto MLS condominium sales in 2012 will be the 5th best ever and better than virtually every year in the 2000's. This is not a sign of a bubble forming or bursting.

DAYS ON MARKET

What this chart shows is a slight slowdown in time to sell that took place primarily in the summer of 2012. Overall, it shows a healthy resale market, with days on market currently at 27 days. Keep in mind that during the bursting bubble of the 1991 recession, days on market extended to over 6 months (180 days) and in many cases extended to over 1 year (365 days). The graph shows 2012 to be one of the healthiest markets ever and in comparison to the mild slowdown we experienced in 2008, significantly better when time to sell rose to 47 days.

The roughly 10% reduction in Toronto resale activity over the last 6 months of 2012 is primarily due to the CMHC's rule changes. It appears this 10% consisted mainly of 1st time fringe buyers and $1.0 million+ high ratio buyers. They were essentially priced out of the buying economy. It is likely that many of these buyers leased a condominium in the interim (note the increase in condo rental volume through the summer of 2012 as available investors plummeted). It is also very likely that these buyers will be back in 2013 with a slightly higher income, and a larger deposit. The good news is that affordability changed little over the year. So while the last half of 2012 reflected a slowdown, 2013 is likely to see this 10% surge of buyers re-enter the market. In the end, it is probable that Flaherty's move simply removed a number of buyers for one year only to see them buy the next year, causing a short-term anomaly and a simple shift of buying volume from one year to the next.



SOUTH CENTRAL LISTING INVENTORY

You can see in this chart that when seller's took their condo properties off the market, they put them up for lease. This is seen by the inverse relationship of dropping sale inventory and rising rental inventory. What is most interesting about this chart is the sheer lack of condominiums for rent in the central core. Generally, 480-950 condos are available at any time south of Eglinton, with several hundred thousand units built, the vacancy rate is below 0.5%. This bodes very well for the condominium investor who buy for the long term and lease their investment properties.

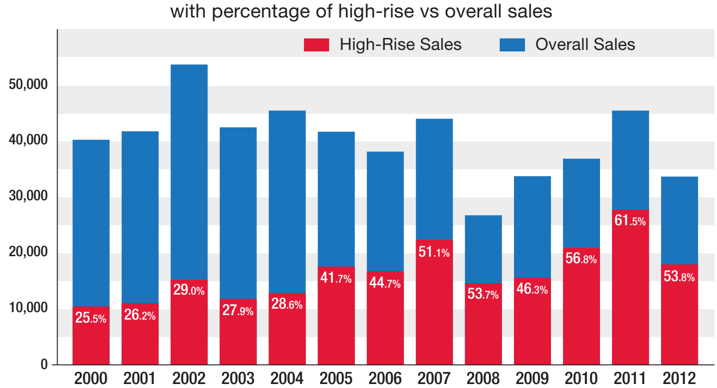
"It is also very likely that these buyers will be back in 2013 with a slightly higher income, and a larger deposit."

NEW CONDOMINIUM SALES ANALYSIS

For a strange reason, many individuals in Toronto seem to long for a biblical-style condominium meltdown. Condominiums are the punching bag of housing and of the economy; despite being single-handedly responsible for the resurgence of Toronto, and its main sponsor as a great world city. This odd viewpoint is probably mostly due to the condominium's awesome success as a housing choice in Toronto. I cannot tell you how many times I have been asked, "Who is going to live in all of these condominiums?" The answer to that question is, "the majority of home buyers." (see chart below)

The reality of the housing industry is clearly shown here. Condominiums are now 60% of new sales because they are what people either want or can afford. The number to focus on is total home sales. 2012 will be the second worst year in the last 12 years. Condominiums will be the biggest component of that, and to date we have not seen any perceived bubble bursting. 2012 will be the 4th best year in the history of Toronto for new condo sales. Overall home sales will be the second worst in 12 years eclipsed only by 2008 during the great depression. What this graph shows is that approximately 40,000 homes sell each year, and going forward over 20,000 of these every year will likely be condominiums. No one ever moans about the imminent collapse of the low rise single family home market, but that is exactly what has happened. We can see that through to 2004, it represented over 70% of the 40,000 new homes sold every year and now it is less than 50%. So why then, when condos have just replaced low rise single family homes as the major contributor to new homes sales, do people worry constantly about a crash? It is because condos are visible, tall, disruptive, and change the neighbourhood dramatically. It has nothing to do with their sustainability. It is purely political.

GTA YEARLY NEW HOME SALES
with percentage of high-rise vs overall sales



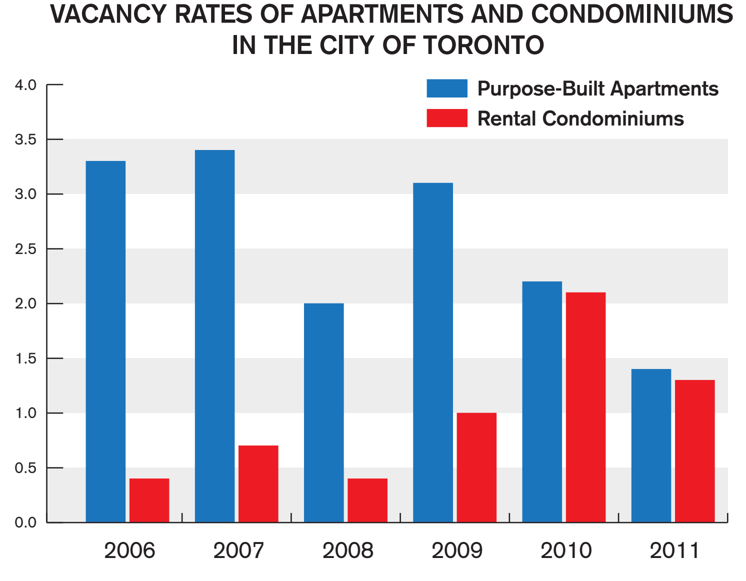
CONDO SALES REPRESENT THE BIGGEST SHARE OF NEW HOME SALES

RESIDENTIAL RENTAL ANALYSIS

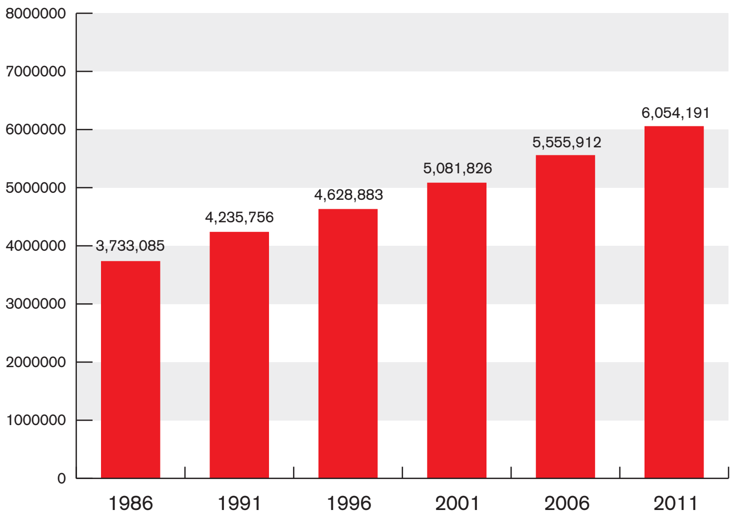
There is a misconception that too many condos are being built. While we can sell as many new condominiums as we like, the industry's current capacity to build cannot exceed 13,000 completions per year. With housing demand at 20,000 units per year, the industry cannot keep up with demand. Over the long term, this will have a serious impact on supply. The new condo market must by necessity now fill two requirements;

1. the majority of new rental housing,
2. the majority of new residences for home buyers.

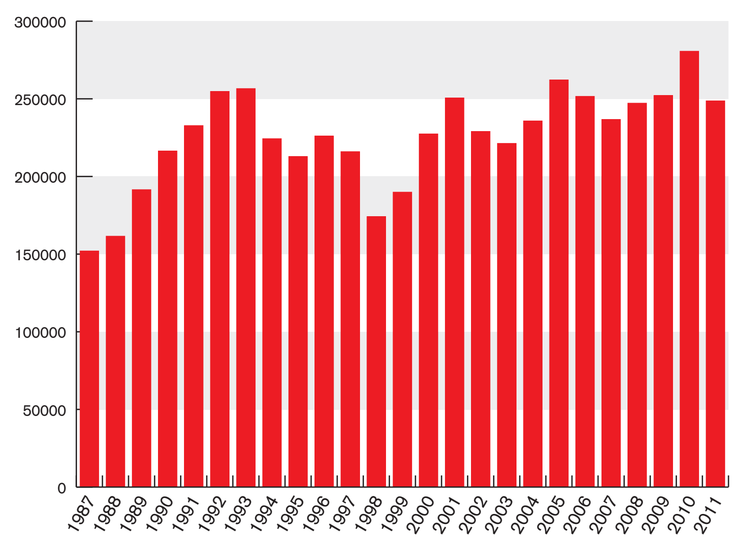
There is a need in Toronto's GTA for 10,000 new purpose built rentals per year. This is just to satisfy the growth of new residents that need to rent every year. Private industry is not building a meaningful amount of purpose-built apartment buildings and neither is the government. So who then is building rental property in the city? Since 2007, the condominium market has added 27,000 units dedicated to the rental economy (as



GTA POPULATION



CANADA IMMIGRATION



shown by the graph **TORONTO REAL ESTATE BOARD RENTALS**). This represents 25% of all the condominiums built since 2007. The only thing separating Toronto from astronomical increases in the prices of rental accommodations is the condominium market. It is however, not anywhere close to enough. With just 5000 new condo units currently going into the rental economy each year, there is a shortfall of 5000 units. This has caused the vacancy rate for purpose-built apartments to drop from 3.5% to 1.4% in a short period of time. The vacancy rate for central condominiums is now below 1%. There has been a shortfall of new-built apartments for over 40 years due to rent control legislation that was brought into the province in the 1970's. This is not fixable in the near or medium term which is why rental prices in the free market have risen 25-30% over the last four years.

The city grows by 100,000 people every year and Canada adds 250,000 new residents every year. It is likely that these numbers will only increase over time.

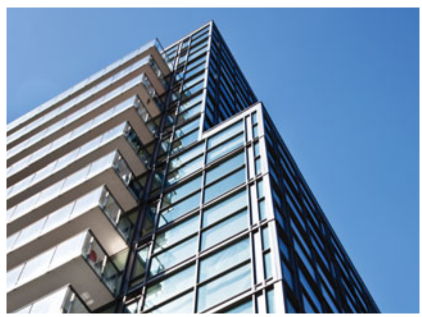
Condo rental prices have dramatically increased over the last four years. This example on the right shows a 28% increase in rents over 48 months. This example is a 400 sq.ft. junior 1 bedroom at gläs condominium, located at King Street West and Spadina Avenue.

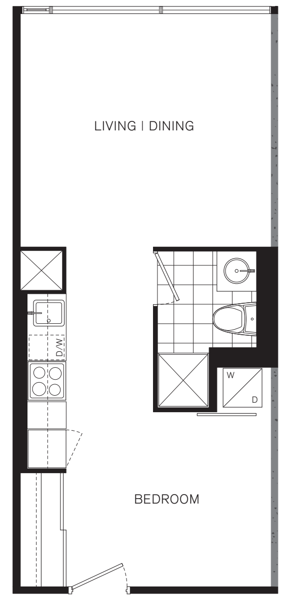
This demand for rental housing will continue to grow as buyer affordability issues accelerate. In essence, fewer and fewer people will qualify to buy a property in a city that will continue to get more expensive. This will continue to be an enormous contributor to new condo sales, as condominium investments have proven to be a lucrative, easily managed, safe place to invest funds for the small, inexperienced, local and international, investor.

One can see the phenomenal wealth-building that occurs when buying Toronto condominiums over the long term. Currently, with massive negative media attention overstating Toronto's current

RENT INCREASE AT GLÄS 410 SQ.FT. JR. 1 BEDROOM

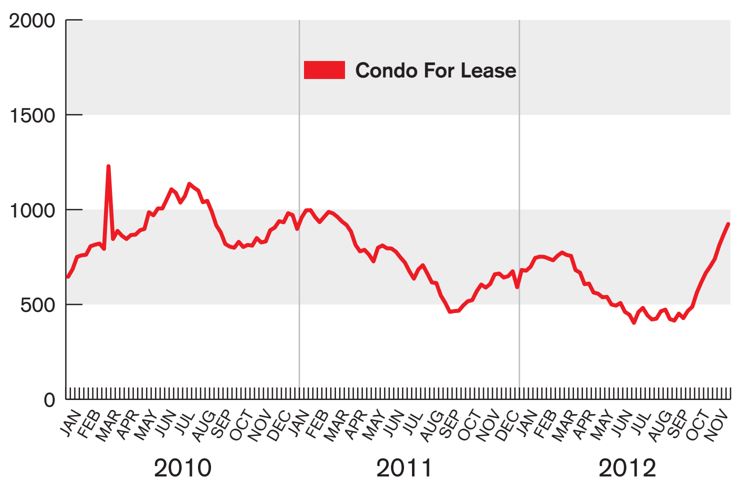
YEAR	RENT
2012	$1,400
2011	$1,350
2010	$1,225
2009	$1,100





SOUTH CENTRAL LISTING INVENTORY

Cental Districts: C01, C02, C03, C08, C09, C10 & C11.
Eglinton Ave - Lake Ontario., Dufferin - DVP.



BUYING A CONDO AS AN INVESTMENT

All examples are based on current opportunities.

JUNIOR 1 BEDROOM

PURCHASE PRICE: $238,900

DEPOSIT (25%) $59,725, MORTGAGE OF $179,175 (MORTGAGE: 3.09%, 25 YEAR AMORTIZATION)

MONTHLY MORTGAGE AMOUNT:	$856.23	(monthly payments)
CONDOMINIUM FEES:	$202.00	
MONTHLY TAXES:	$180.00	

*capital gains are calculated using an annual appreciation of 4% (Toronto has averaged 6% over the last 10 years)
*rental rates subject to 3% annual increase

YEAR	YEAR 1	YEAR 5	YEAR 10
Condo Value:	$248,456.00	$290,658.38	$340,029.19
Capital Gain:	$9,556.00	$51,758.38	$114,730.36
Total Monthly Cost:	$1,238.23	$1,238.23	$1,316.23
Monthly Rent:	$1,395.00	$1,570.08	$1,820.16
Annual Rent Profit:	$1,881.24	$3,982.20	$6,047.16
Annual Mortgage Principle Paid:	$4,842.81	$5,474.46	$6,380.20
Annual Return from Rent:	$6,724.05	$9,456.66	$12,427.36
Rent Profit Over Term:	$1,881.24	$14,581.13	$38,637.74
Mort. Principle Paid Over Term:	$4,842.81	$25,763.88	$55,292.54
Total Profit:	$16,280.05	$92,103.39	$208,660.64
Annual rate of return from rent:	**11.3%**	**15.8%**	**20.8%**
ANNUAL RATE OF RETURN FROM TOTAL PROFIT	**27.3%**	**154.2%**	**349.4%**

pause in price growth, and unsolved European and U.S. government debt issues, many investors have taken a break. A break to where? They have not taken their money somewhere else, rather they are sitting on cash, waiting for a sign to re-enter the marketplace. As you can see from the above investment option, the opportunity to earn vast financial rewards still abound in the Toronto condo market. There is however, recent evidence that investors are coming back as seen by some very successful new condo sales programs late in 2012. The overall availability of condo rentals in the central core is very tight, which bodes well for condo investors. The long term view for returns on condo investments is extremely attractive based on this chart. With so little inventory, rental prices must rise, and they have. The supply of rental condominium product is totally inadequate. It averages between 480-900 units.

THE RESURGENCE OF THE TORONTO OFFICE TOWER

There are at least 16 office towers under development that will add approximately 4 million square feet over the next 4 years. Due to the condo boom, office vacancies are down as retail and office businesses are looking to be within reach of the new downtown pool of young talent. This symbiotic relationship is giving long term sustainability to new condominium developments.

Usually 3-4 years after a recession, the vacancy rates for office space would be at its peak, but the explosive demand for downtown space has made vacancy rates among the tightest in history. 4.5 million square feet of office space has been completed since 2009 and a second boom of 4 million square feet will be completed in 2014-2016.

The current vacancy rate in the downtown core is 4.5% compared to an average of 9.2% over the past 20 years. This is contributing to the boom of new office buildings downtown.

"4.5 million square feet of office space has been completed since 2009 and a second boom of 4 million square feet will be completed in 2014-2016."

Recent large transactions in the central core show a tremendous level of confidence in the commercial real estate industry. Allied Property and Riocan just bought the Globe and Mail property for $136 million, and are negotiating to buy the balance of that property at the corner of Front and Spadina. This group also recently bought the Bianchi Collision property at King and Portland. Both will be large scale office, retail and residential developments and combined will greatly exceed $1.0 billion in development.

Some of the companies to recently expand or relocate to downtown Toronto are: SNC Lavalin, PWC, Telus, Coke, Google, Corus, Deloitte, RBC, Salesforce.com, and KPMG, showing confidence in the city's core despite higher real estate taxes.

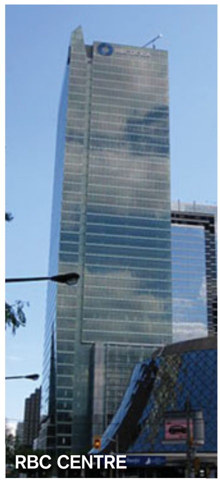
The allure of living downtown and working downtown is attractive to many young professionals, giving them a higher standard of living and quality of life with increased levels of discretionary spending just by giving up a car. We have seen this time after time with the demand for condominium tower parking coverage decreasing in some cases to less than 30%.

Many billions of dollars from the office sector of the development industry is stimulating the GTA economy, furthering a need for new housing. It is unlikely in this environment of office space expansion that we will see a protracted, deep reduction in residential prices. Historically speaking, it has never happened.

NEW OFFICE TOWERS

Southcore Financial Centre (18 York/Bremner Tower)
Bay Adelaide Centre (West, East, North towers)
Telus Tower
21 Don Roadway (Lever Bros)
FCP rejuvenation
Maple Leaf Square
388 King Street West
71-95 King Street East
RBC Waterpark Place III
RBC Centre (Wellington)
111 Richmond Street
QRC West (134 Peter)
Oxford Place


RICHMOND ADELAIDE III

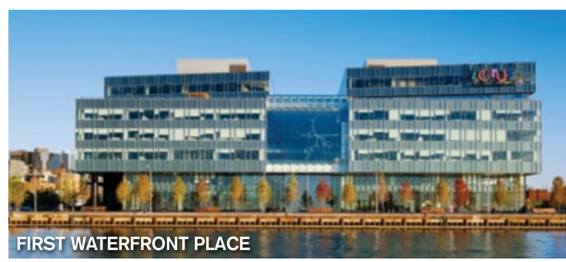

RBC CENTRE


MAPLE LEAF SQUARE


TELUS TOWER

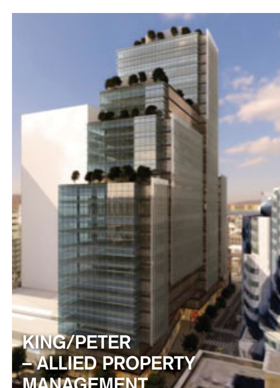

18 YORK ST


111 RICHMOND


FIRST WATERFRONT PLACE


BAY ADELAIDE CENTRE


21 DON ROADWAY


KING/PETER – ALLIED PROPERTY MANAGEMENT

NEW HOTELS AND PUBLIC BUILDINGS

The last eight years have been the biggest hotel boom in the history of Toronto. With the Standard Group, Morgan's Group, W, Kimpton, Gansevoort, and several more hotel companies chomping at the bit to get access to Toronto. We can expect more world-class hotels and the expected surge in work and pleasure related visits to Toronto further stimulating our economy.

Toronto is now considered one of North America's "fun spots" competing for weekend visitors with Los Angeles, New York, Las Vegas, and Miami. A new world-class casino is now in the works. It is no longer a Canadian back water, rather a world class city on the world stage.

We have also recently expanded our universities, colleges, and public buildings with new or expanded facilities.

This is not the doings of a poor city of have not's. Toronto ranks as the number 1 city in North America for cities with skyscrapers being built; an incredible 147 in Toronto, versus 72 in New York City, and 21 for Vancouver. This is nothing less than the complete redefining of Toronto. This is similar to the great expansion of Chicago and New York City in the 1860's bringing them into the state of world-class cities. This is our time. The sheer volume and velocity of money already invested in Toronto makes a 1991-style correction unlikely, we are a much larger and richer city and have the financial ability to weather slowdowns as we did in 2008.

I have spent many hours analyzing data and speaking to many hundreds of consumers. Along with conceptualizing the recent and future changes to Toronto, I have considered all of it and despite the biased, sensationalized, and ignorant media coverage to the contrary, I am very optimistic about the next 10 years and beyond for Toronto and the condo industry. I say, do not be misled by the naysayers and Chicken Little's. I believe condominiums are the one and only real future of residential development in Toronto.

"This is nothing less than the complete redefining of Toronto. This is similar to the great expansion of Chicago and New York City in the 1860's bringing them into the state of world-class cities."

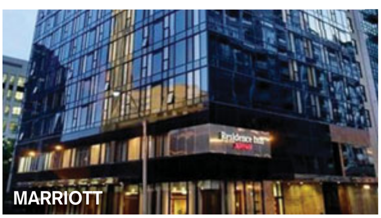
NEW HOTELS

Four Seasons
The Ritz-Carlton
Thompson Hotel
King Edward
Trump Tower
The Hazelton Hotel
Marriott
Le Germain
Shangri-La
Hilton
Delta


DELTA


THOMPSON


RITZ-CARLTON


MARRIOTT


THE HAZELTON


LE GERMAIN


FOUR SEASONS


TRUMP TOWER


SHANGRI-LA

NEW PUBLIC SPACE

- Ripley's Aquarium of Canada
- Art Gallery of Ontario
- Four Seasons Centre for the Performing Arts
- Ted Rogers School of Management
- Li Ka Shing Institute @ St. Michael's Hospital
- National Ballet School
- Ryerson's Mattamy Athletics Centre
- Union Station Revitalization
- Underpass Park
- Puente de Luz Bridge
- Royal Ontario Museum
- Gardiner Museum
- Ontario College of Art & Design
- George Brown College Waterfront Campus
- The Royal Conservatory of Music
- MaRS Centre Phase 2
- Nathan Phillips Square re-design
- June Callwood Park
- St. Lawrence Market North
- CAMH Queen Street Redevelopment
- Sony Centre for the Performing Arts (formerly Hummingbird Centre)
- Daniels Spectrum (formerly Regent Park Arts and Cultural Centre)
- Waterfront Toronto (Lower Donlands, East Bayfront, West Don Lands, Portlands, Centre Waterfront)

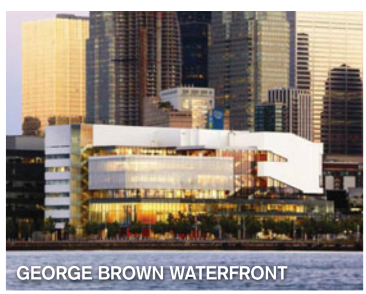

RIPLEY'S AQUARIUM

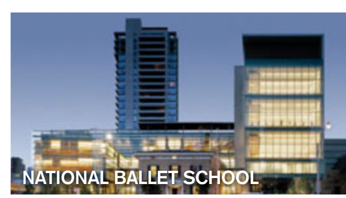

SONY CENTRE

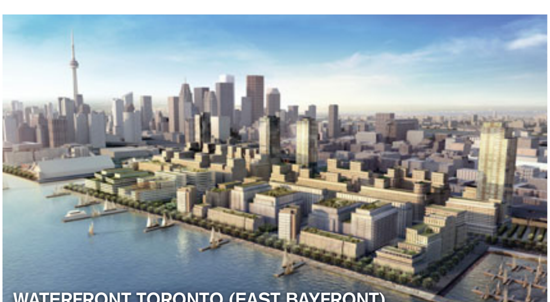

THE ROYAL CONSERVATORY OF MUSIC


FOUR SEASONS CENTRE


ROYAL ONTARIO MUSEUM


GEORGE BROWN WATERFRONT


NATIONAL BALLET SCHOOL


WATERFRONT TORONTO (EAST BAYFRONT)


ART GALLERY OF ONTARIO

"I have spent many hours analyzing data and speaking to many hundreds of consumers. Along with conceptualizing the recent and future changes to Toronto, I have considered all of it and despite the biased, sensationalized, and ignorant media coverage to the contrary, I am very optimistic about the next 10 years and beyond for Toronto and the condo industry."

— Brad J. Lamb

BRAD J. LAMB
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