

ARE RICH CHINESE CAUSING THE CANADIAN HOUSING BUBBLE? A SHORT REPORT



Are rich Chinese driving up Canadian property prices, or is it just a myth?

In recent decades in Canada, property prices have been surging to record heights in both Vancouver and Toronto. Inhabitants in both cities have been voicing concerns about the growing unaffordability of housing. In Vancouver and Toronto, it's commonly believed that rich Chinese are the main cause of the surge in property prices. The myth is that many Chinese are coming into the country and are willing to overpay for a property.

So is the myth fiction or reality?

First, let's start by explaining why affordable property prices are so important.

Housing is usually the largest chunk of the cost of living. Cost of living is closely associated with wages; it's part of the overall package that translates into "what

do I get for my labor?" If the value of that overall package is reduced because of increased living costs, it becomes harder for a city's businesses to attract and retain labor. Businesses will need to offer higher wages to balance the increase in the cost of living. They will incur higher expenditures and might need to increase their prices to stay profitable. But their product might not be competitive in the global market at a higher price. If the product doesn't offer added value, it could lose competitiveness. As a result, the business will need to relocate to a less expensive city in order to remain competitive, leading to a weakened economy. This has been the experience in Canada over the past year, with both Vancouver and Toronto creating fewer new jobs together than Montreal, the latter having property prices nearly half of process in the other two.

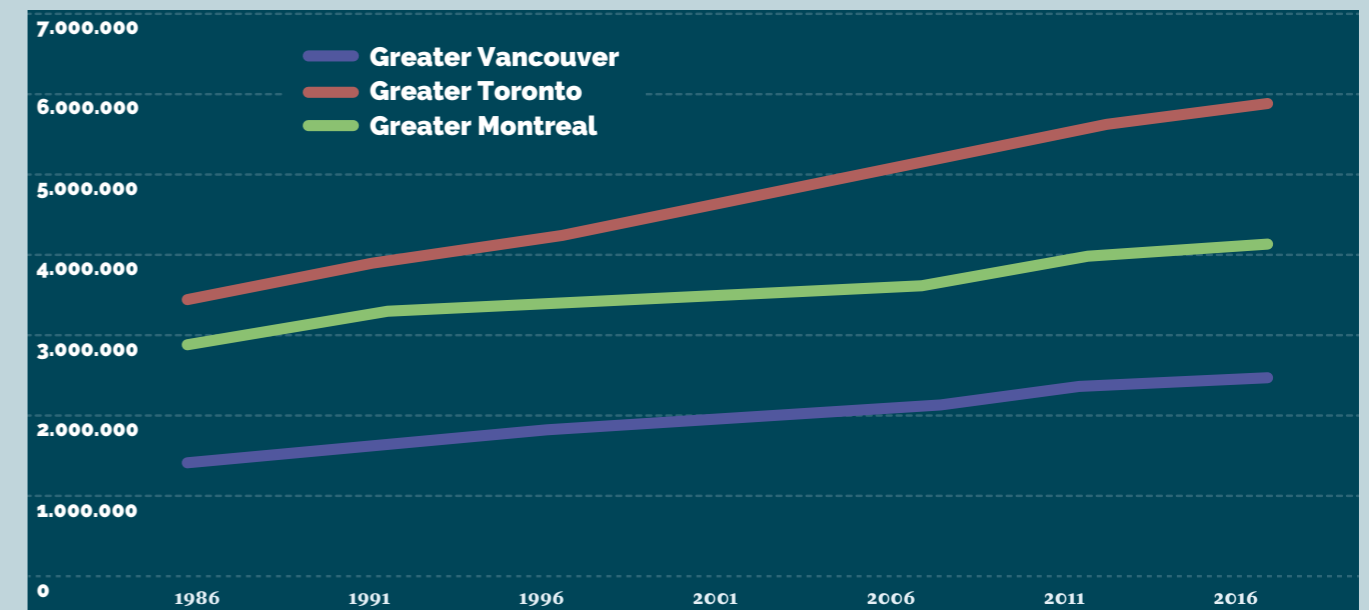
DEMOGRAPHY IS USUALLY THE MAIN DRIVER BEHIND SURGE IN PRICES.

In the last 30 years, Vancouver's population grew by 78.5% and Toronto's by 73%. Montreal's grew by 40%. Furthermore, starting in the mid-1970s, Montreal

experienced two decades of demographic stagnation due to a flight of Anglophones from the province after a separatist French-Canadian party came to power in Quebec. This alone could explain the rate of price increases, but many other factors also came into play.

POPULATION BY CENSUS AREA

SOURCE: STATCAN



ARE AMERICANS LEAVING THE LAND OF TRUMP SETTLING IN CANADA IN HIGH NUMBERS?

It would make sense that if Americans were planning to move to Canada, Toronto and Vancouver would be their favored destination. The US is the richest country in the world, and even if only 0.1% of its population were to relocate to either of the two cities post-Trump, it would completely unbalance the market. So are the numbers correlated? Are people fleeing Trump's America the real cause of the recent surge in property prices in Toronto and other Canadian cities?

We have gone through all the recent temporary and permanent immigration numbers. Although there could be a slight increase in the number of Americans coming to live in Canada, that increase cannot be deemed large enough to have a significant impact on property prices on its own.

ARE FOREIGNERS CAUSING THE PRICE SURGES?

Last year, the City of Vancouver introduced an additional 15% property transfer tax on foreign nationals, foreign corporations and trusts that are buying property in Metro Vancouver. Foreigner nationals

are those who do not have permanent residence in Canada. Data suggested that foreign investors were investing billions in Vancouver's property market and driving up prices. Unfortunately, that resulted in many equating the phrase "foreign investors" with "wealthy Chinese". Vancouver has a large Chinese minority, with roughly 30% of its inhabitants tracing their ancestry to China as far back as 1858. The common mistake is to think that a rich Chinese-looking individual living in Canada is foreign. You can live your whole life in Canada, have Chinese ancestry and be rich – these characteristics are not mutually exclusive. In most cases, these individuals are Canadians, perhaps even multi-generational Canadians. Very few of them don't hold citizenship or permanent residence status.

So if there are rich Chinese foreigners, how could they be getting inside Canada? There are a few possible ways:

1. Temporary immigration, student visa
2. Touristic/business/ family visa
3. Permanent immigration, mainly the investor or entrepreneur program.

TEMPORARY IMMIGRATION, STUDENT VISA

Currently, the total number of Chinese students in Canada exceeds 100,000. The tuition fees for international students can reach 20,000 USD per year, and further costs associated with their stay makes it probable that a good proportion of those students are from wealthy families. It's possible that some of these families are buying properties for their children to live in as they study. There are no data on that subject, but these people would be considered foreign buyers and the 15% buyer tax would be applied to them.

VISITOR VISA

In Feb. 8, 2015, Canada and China signed a reciprocal agreement on issuing long-term and multiple-entry visas. Visas will have a validity of up to 10 years and permit a stay of up to 180 days per year. Some 610,000 Chinese visited Canada in 2016, a bit less than the number of Canadians that visited China. It's also possible that a wealthy Chinese person with a tourist visa would buy a property and come to spend some time in it. In the end, many immigrant investors don't want to spend the whole year in Canada and don't want to be liable for taxes. If there are any, there's no way

to know, since statistics aren't compiled on the matter. It wouldn't be logical for someone without residence status in Canada to purchase a property, but wealthy Chinese are also advised to invest money outside of China. Nevertheless, there were more than 4 million international visitors to Canada in 2016. Americans come in far greater numbers and are more likely to buy a property in Canada than any other foreigner, although their purchases would be more scattered and not necessarily centered in Vancouver and Toronto. We can suspect that some wealthy Chinese on a visitor visa are buying properties and most likely when they are in the process of immigrating to Canada, but we can't estimate the frequency of those purchases. These individuals would be considered foreign buyers and the 15% buyer's tax would apply.

IMMIGRANT INVESTORS

Since the inception of the Canadian Immigrant Investor Program in 1986, Vancouver received more than half of all immigrant investors. That's possibly 50,000 High Net Worth families in the course of the program. It's possible that because of the city's small physical size and its high population density that immigrant

investors flocking there might, over decades, have caused property price to surge above expectations.

Nevertheless, over the last 5 years Vancouver has lost some of its appeal to immigrant investors, and newcomers have diverted to Toronto. There are no reasons

to believe that new immigrant investors will carry significant weight in the property market of a city of 2.5m inhabitants. It's not backed by any numbers, and since the termination of the Federal Immigrant Investor Program in 2010, the number of immigrant investors has (logically) dropped every year since.

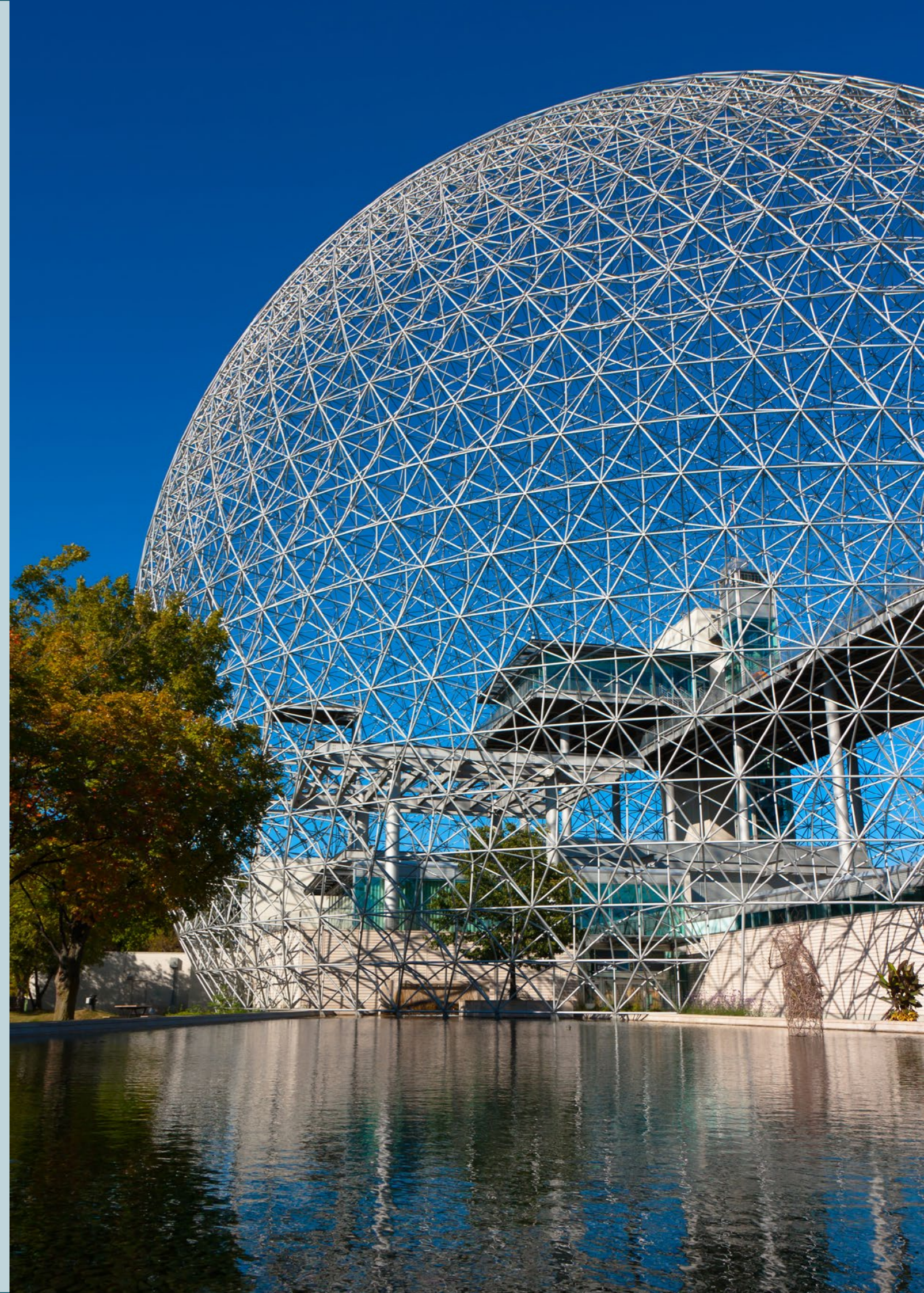
PRINCIPAL APPLICANT (EXCLUDES SPOUSES & DEPENDENTS)

SOURCE: CANADA IMMIGRATION & CITIZENSHIP

CATEGORY	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Entrepreneur	819	579	445	370	292	184	126	114	131	74
Investor	2,186	2,006	2,817	2,86	3,21	2,973	2,607	2,355	2,077	1,547

There is no precise way to know how many of today's Immigrant Investors settle in the Toronto area. Since the end of the FIIP in 2010, only the Quebec program is open and applicants must intend to settle in Quebec. Nevertheless, we estimated last year that roughly 45% of all immigrant investors chose to relocate to Greater Toronto. Therefore, only an estimated 6600 families from the Immigrant Investor program might have resettled in Toronto between 2010 and 2015. During that period, 30% of the country's total Permanent Immigrants ended up in Toronto. More than

80,000 people a year immigrate to Toronto from abroad. This is in line with the city's population growth in the last decade. That is double the amount received by Montreal, and nearly triples that of Vancouver. The sheer number of immigrants coming in puts significantly more weight on property prices than the hundreds of immigrant Investor families believed to be coming in every year via the Quebec Immigrant Investor Program. Furthermore, not every immigrant investor is Chinese; roughly 80% of the main applicants are today, but this was not always the case in the '80s and '90s.

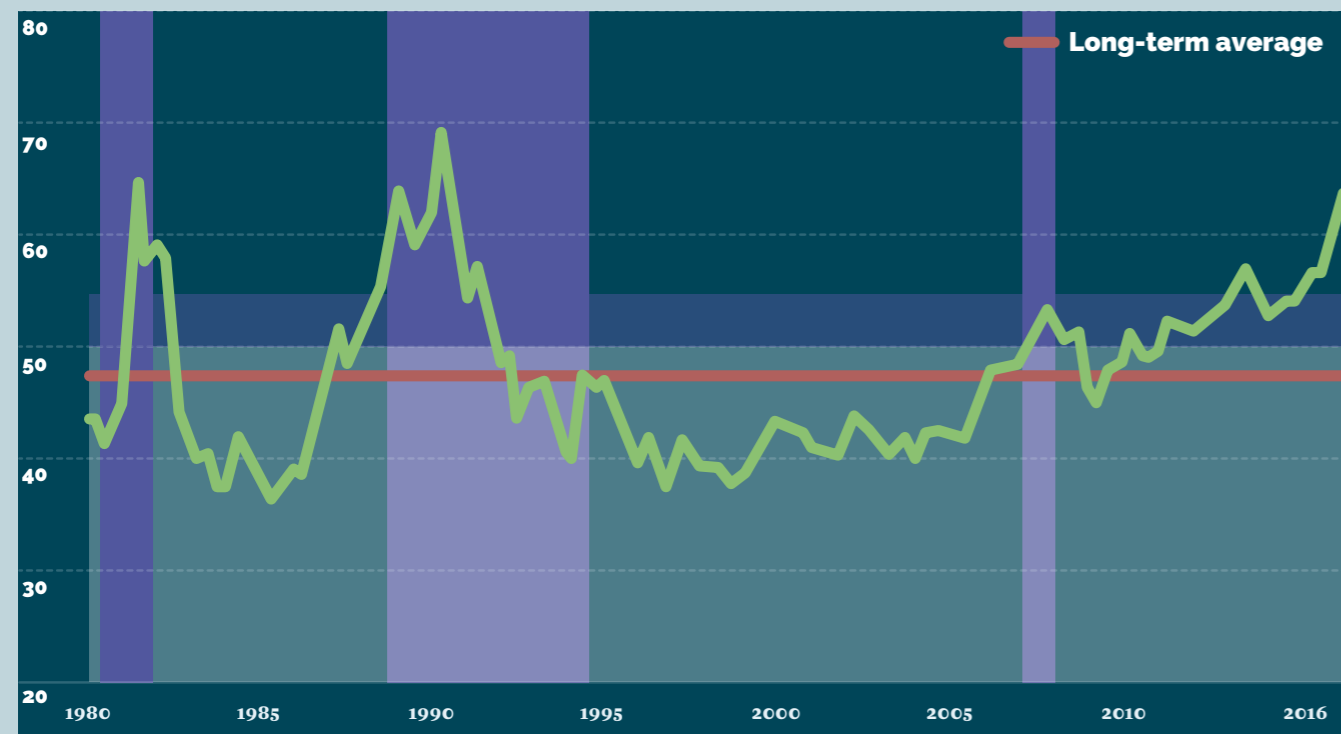


ARE VANCOUVER AND TORONTO ALONE IN THEIR ORDEAL?

Most of the world's big cities have problems with housing affordability. Sure, the Chinese are probably behind the problem in Shanghai – but did they cause the unaffordability of property in Tehran? In Kiev? In Vancouver in 1981? Figures show that both Toronto and Vancouver have had problems with housing affordability in the past, and the trends are linked with the national economy. Both of Canada's main cities have experienced the same trends in affordability, with Vancouver having historically a more expensive property market.

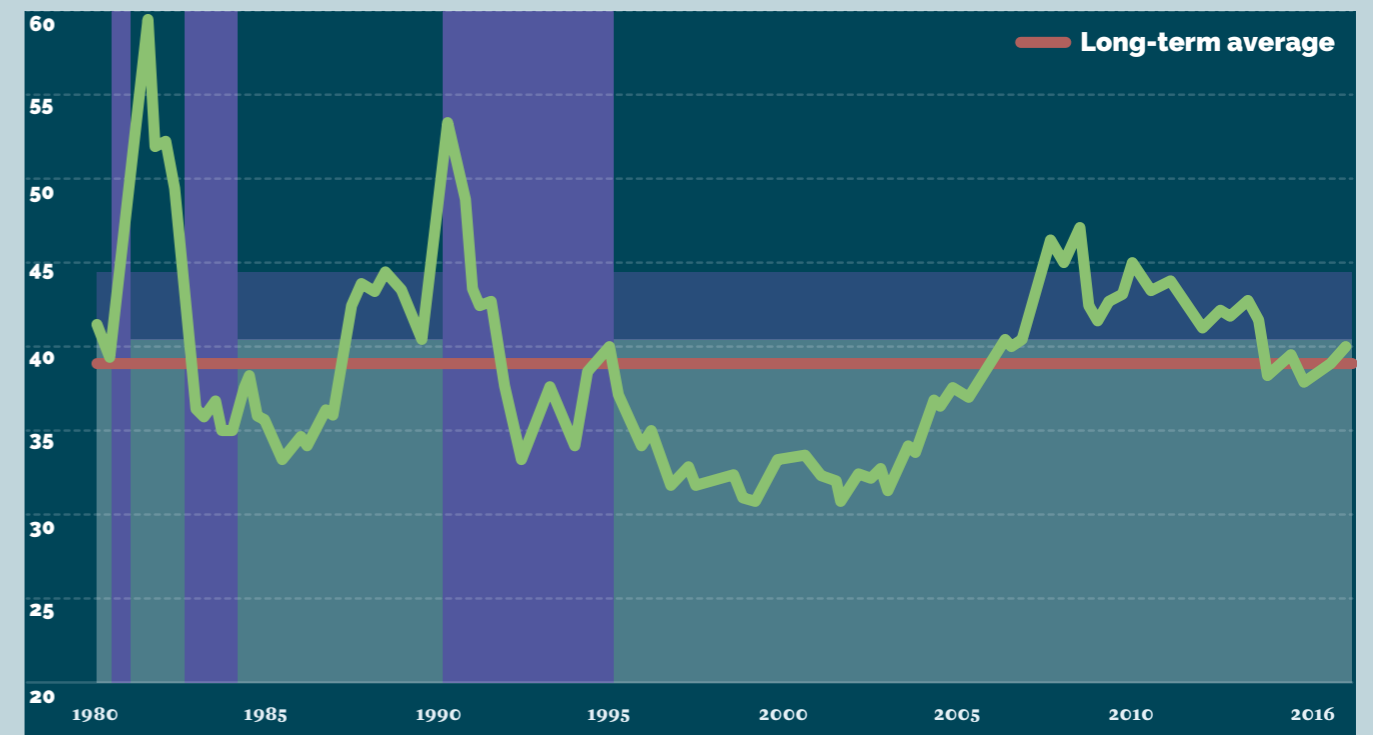
RBC AFFORDABILITY MEASURE- AGGREGATE - TORONTO

OWNERSHIP COSTS AS % OF HOUSEHOLDE INCOME



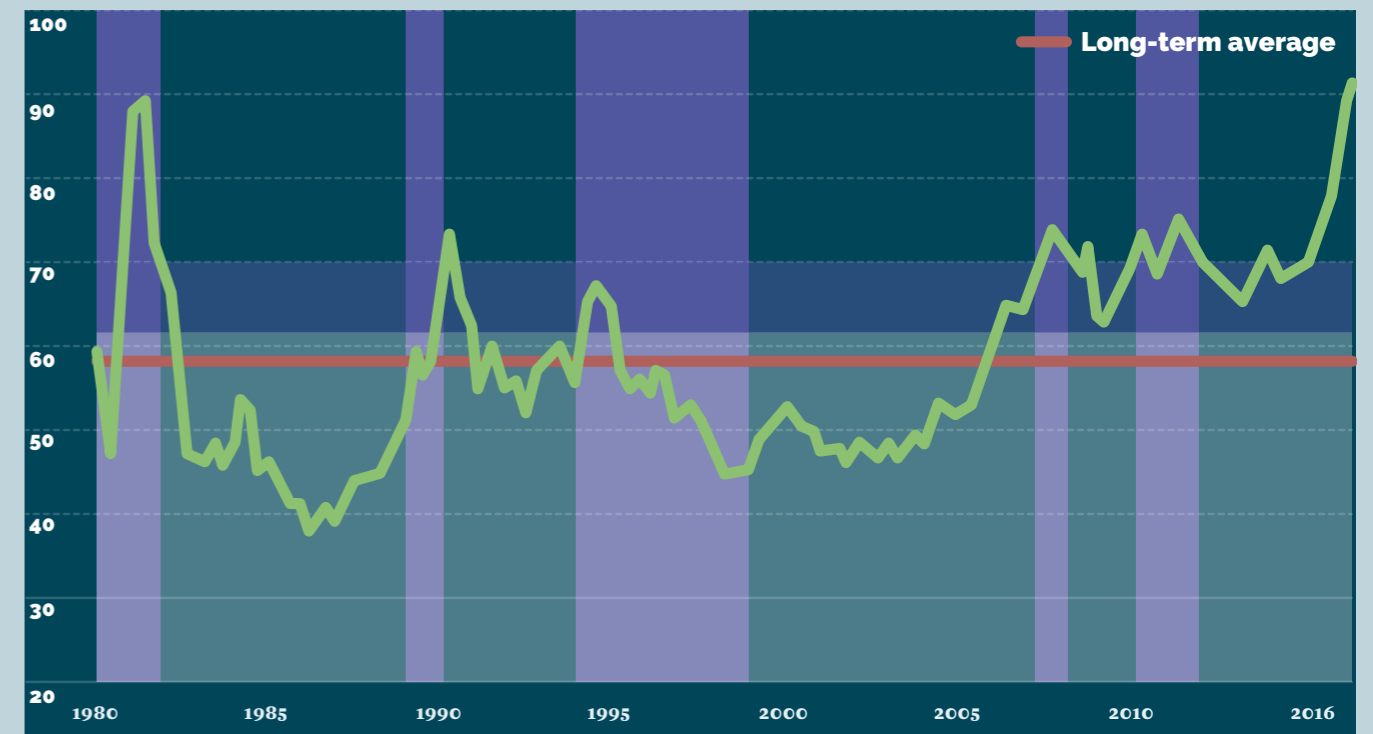
RBC AFFORDABILITY MEASURE- AGGREGATE - MONTREAL

OWNERSHIP COSTS AS % OF HOUSEHOLDE INCOME



RBC AFFORDABILITY MEASURE- AGGREGATE - VANCOUVER

OWNERSHIP COSTS AS % OF HOUSEHOLDE INCOME



The reality of the matter is that housing is becoming more and more unaffordable. This is a global trend, and not limited to Canada.

The only large cities where people spend less than 35% on their mortgage are in the US, and those numbers do always paint

COUNTRY	CITY	MORTGAGE AS % OF INCOME
Ukraine	Kiev	419
Argentina	Buenos Aires	343
China	Beijing	299
China	Shanghai	290
Russia	Moscow	283
Brazil	Rio de Janeiro	268
Iran	Teheran	264
Colombia	Medellin	254
Azerbaijan	Baku	245
Hong Kong	Hong Kong	239
Peru	Lima	205
Vietnam	Ho Chi Minh City	189
Egypt	Cairo	171
Turkey	Istanbul	165
UK	London	163
Lebanon	Beirut	149
Singapore	Singapore	138
Israel	Tel Aviv	135
Italy	Rome	133

a reliable picture because of the large disparity in property prices between “bad” and “good” neighborhoods.

Here is a table showing some of the main world cities and mortgages as a % of income:

COUNTRY	CITY	MORTGAGE AS % OF INCOME
Mexico	Mexico City	128
France	Paris	99
Japan	Tokyo	97
Canada	Vancouver	92
Australia	Sydney	89
Norway	Oslo	76
US	New York	74
US	San Francisco	68
Switzerland	Geneva	63
Canada	Toronto	59
Germany	Berlin	57
Denmark	Copenhagen	53
Qatar	Doha	48
Belgium	Brussels	46
Canada	Montreal	43
US	Los Angeles	41
UAE	Dubai	40
South Africa	Johannesburg	34
Saudi Arabia	Riyadh	20

SOURCE: NUMBEO.COM

Data show that Canadian cities are not those suffering the most from housing unaffordability. Quite the opposite: in fact, North Americans have generally benefited from large homes. When you look at the cities below Montreal in our list, Los Angeles has a significant price disparity between the bad and the good neighborhoods, whereas the other ones have access to very cheap labor in comparison to Canada, thus reducing construction costs.

There are also fiscal reasons that cause property prices to surge. Property transfer taxes and the overall round trip-costs of transactions, when absorbed, lead to price hikes. Also, property markets with low annual property taxes tend to attract more investors, as the cost of holding property is low.

ARE WE CAUSING OUR OWN PROBLEMS?

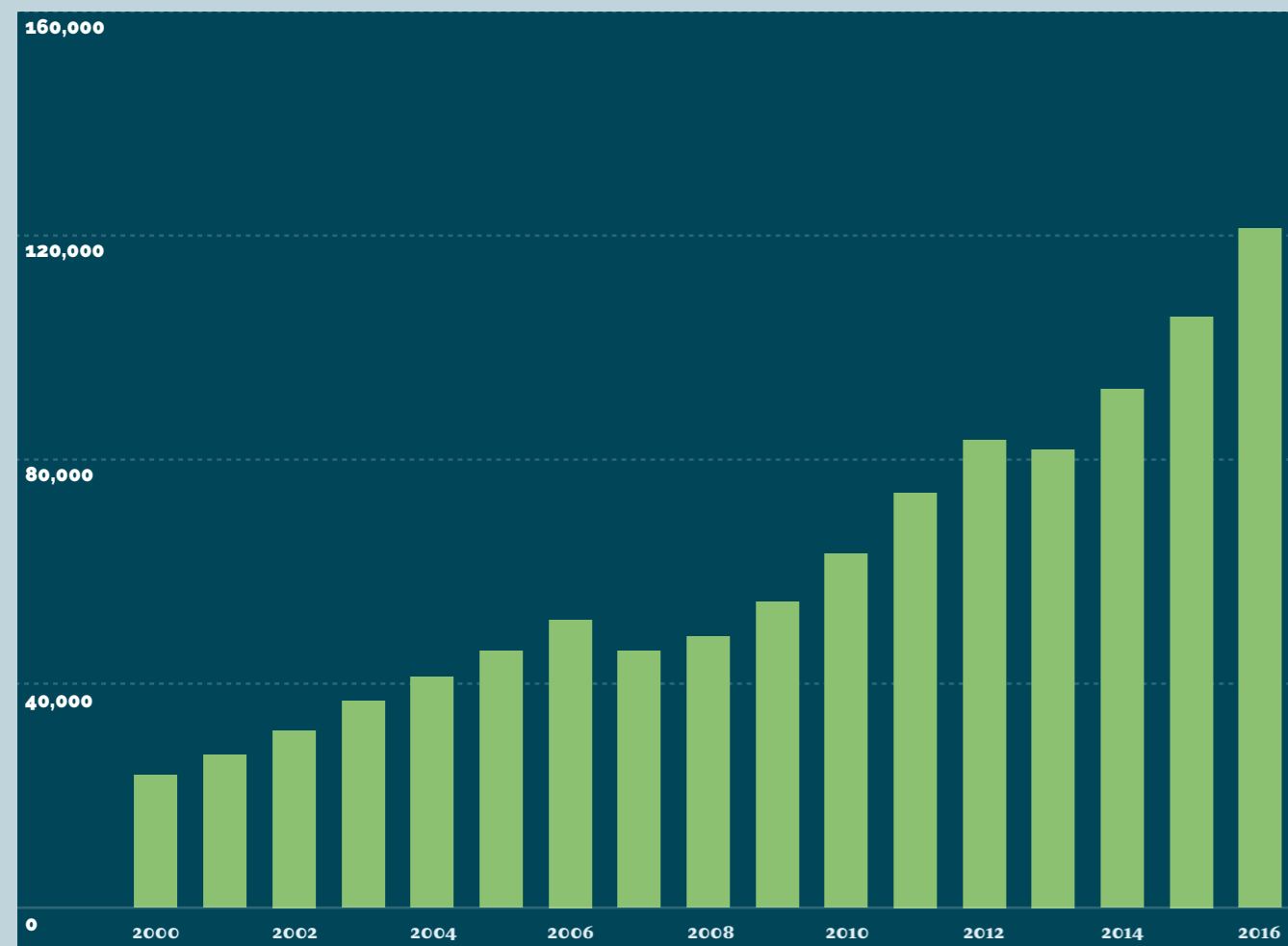
What we saw lately in Toronto and Vancouver was confidence in the market born out of the myth that rich Chinese were coming in exaggerated numbers and overpaying for properties.

That myth, which was repeated and embellished over and over, led people to believe that prices can naturally only go up. Canadians with a bit of money in Toronto and Vancouver started buying investment properties in the hopes of flipping them in a few years and making good money. It soon became a trend. An analysis conducted by the Ministry of Finance found that 121,100 people in the Greater Toronto & Hamilton Area owned at least one other home in 2016. And that number has been gaining momentum the last few years.



NUMBER OF OWNERS WITH MORE THAN ONE RESIDENTIAL PROPERTY IN GTHA: 200-2016

SOURCE: MINISTRY OF FINANCE



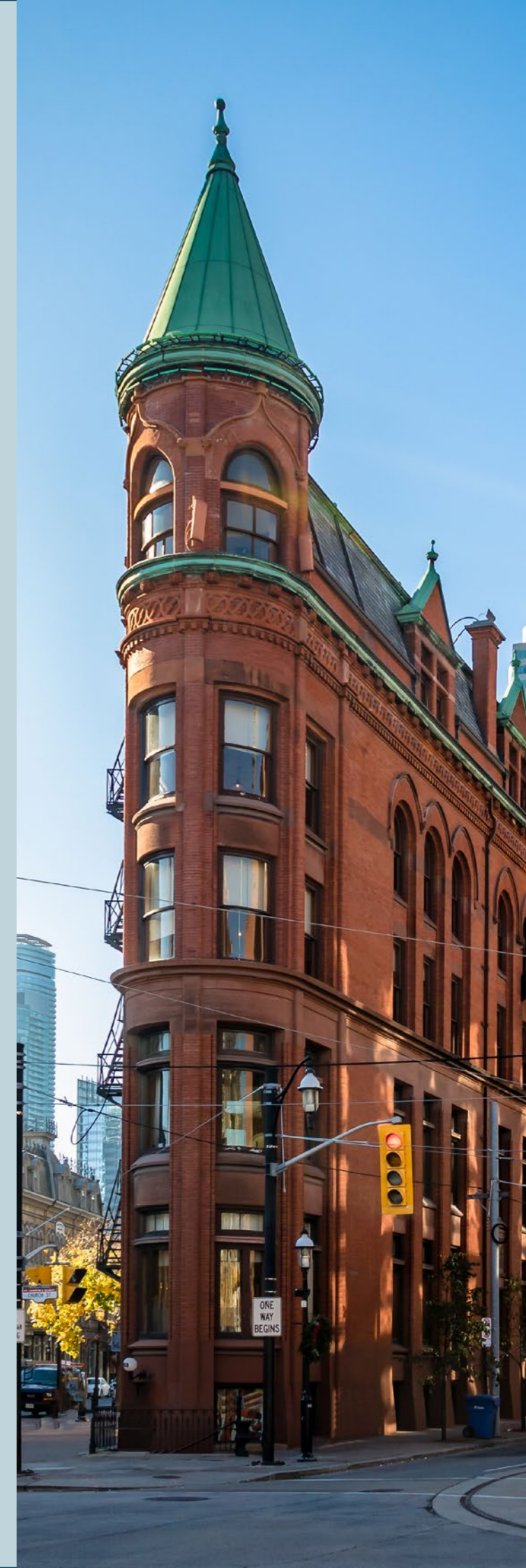
These numbers are for the number of owners, but each owner might own more than two properties. One owner can have numerous additional residential properties. I personally met an immigrant investor from Iran who bought an additional property for every member of his family, having been made to believe by realtors that this was the way to make

money in Canada. That same person, who had no income in Canada and limited wealth, was tricked into taking out numerous mortgages with low down-payments, in a move reminiscent of the predatory lending during the American mortgage crisis. These numbers also exclude Trusts and Companies whose investment activities include real estate.

These large investors can be both local and foreign and can force more volatile fluctuations, as they usually follow the same indicators.

The 2016 Census also revealed that Vancouver has 25k+ homes that are not regularly occupied, trumped only by Toronto, which has 100k of them. That's 4.5% of all the homes in Toronto, and this number has increased sharply in the last few years. Some areas of the downtown have a massive 20% of homes regularly unoccupied. The census is filled out by local residents; it's unlikely that someone abroad will get his mail redirected to him, fill out the census and return it to the government via international mail. In other words, these numbers are from local residents and are unlikely to include unoccupied properties of those residing abroad.

BETTER DWELLING estimates that 1 out of 3 houses for resale in Toronto have never been occupied. Those are mainly condo projects purchased by investors during pre-construction that are put on the market after construction. It gives us a slight idea of the amount of speculation taking place in the city.



Will the bubble burst?

The 15% tax imposed on foreign buyers had a cooling effect. It at least gives the naïve impression that the rich Chinese will be deterred and pessimism will enter in the market. People will wait for a bit to see what happens. The tax will trim the extra fat, but companies and trusts are likely to find ways around it. Foreigner investors, in the case of immigrant investors, are of course unaffected, so the myth of the rich Chinese buying a million-dollar property for more than the listed price might not die. But it's likely that investment companies will lower their investment in both Vancouver and Toronto. The bubble is unlikely to burst in Toronto because of

the number of new immigrants flocking the city, and Vancouver's prices have been up for a good amount of time (and naturally priced higher, for numerous reasons). Prices are more likely to adjust and stabilize once confidence in the market is tamed. There were many ways to slow down the surge in prices, ways that would decrease accessibility to unwanted buyers and increase accessibility to desired buyers. Nevertheless, it must be stated that Vancouver took a very long time to put its property market in order. The policies were implemented a decade or two too late, and growth in many sectors of the economy was reduced because of it. Toronto acted

fast, but the damage was done. Record unemployment due to low job creation was reported in 2017. On the opposite side, Montreal is breaking records with its lowest unemployment rate in 40 years and a record number of jobs created. Montreal has been attracting business in the last few years because of the quality of its workforce in relation to its cost, making products and services produced in Montreal very competitive in the global market.

After Vancouver and Toronto, is Montreal next? Prices have been steadily going up lately and the trend is likely to continue. Montreal's property market is very

different from other Canadian property markets. Montreal imposes rent control and possesses a large stock of rental properties. It also has a lot of empty lots around the downtown area, and its annual property tax is relatively high. Many factors make Montreal's property market less at risk than those of other Canadian cities. Nevertheless, Montreal has lately become arguably the most liveable Canadian city, and its healthy economy might accelerate its growth. Because it's so important for the city to maintain an affordable property market, cooling policies will be put in place sooner rather than later.



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