

Presentation to North Cowichan Developers' Forum

George Parker – 31 October 2023

Mulholland & Parker
Land Economists Ltd.

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1) Introduction – my role (5 minutes)

2) Market research (15 minutes)

Group discussion on market prices today.

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**Group discussion about various
development economics assumptions.**



1) Introduction – my role

I am a land economist, which means I help clients understand development, typically in two ways:

- 1) Market research: Gathering quantitative and qualitative data about local markets, including costs, prices, timelines, and perspectives.
- 2) Financial analysis: Modelling the flow of money through development projects to answer particular questions.



1) Introduction – my role

Questions like:

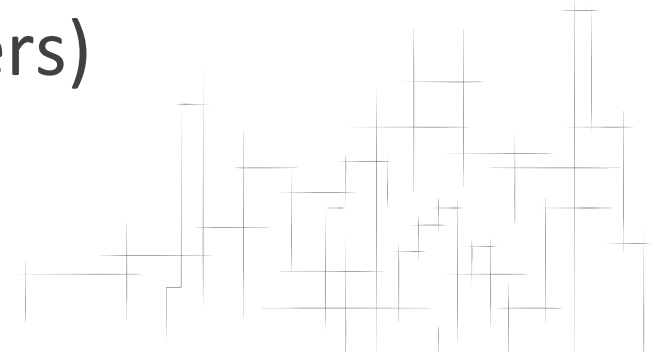
- Is a given type of development financially viable in a given location?
- How much land value would a particular land use support in a given location?
- What would be the anticipated economic impact of a given development?



1) Introduction – my role

We have been retained to perform both of these roles for North Cowichan, with the overall aim of identifying supportable Community Amenity Contribution (CAC) rates:

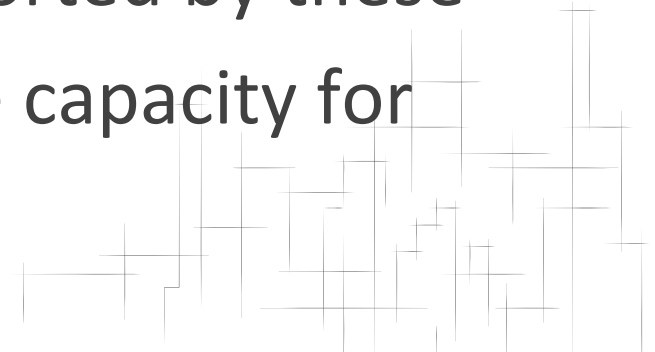
- 1) We conducted **market research** in August and submitted a market research report. This work included online research from several sources as well as interviews with 10 local experts (realtors, developers, and builders)



1) Introduction – my role

We have been retained to perform both of these roles for North Cowichan, with the overall aim of identifying supportable CAC rates:

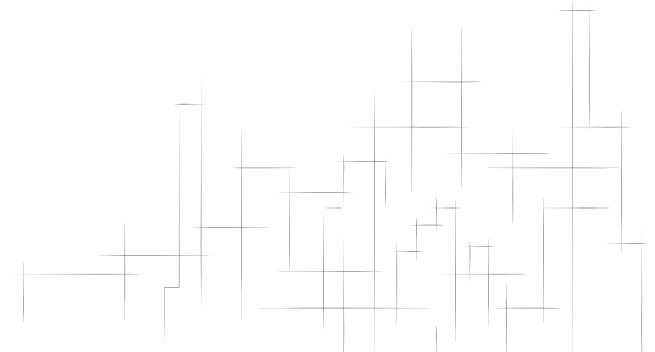
- 2) We are currently in the process of creating a **financial model** of 18 different residential development styles in each of North Cowichan's five urban neighbourhoods. By comparing the land values supported by these scenarios, we will determine the capacity for CACs in North Cowichan.



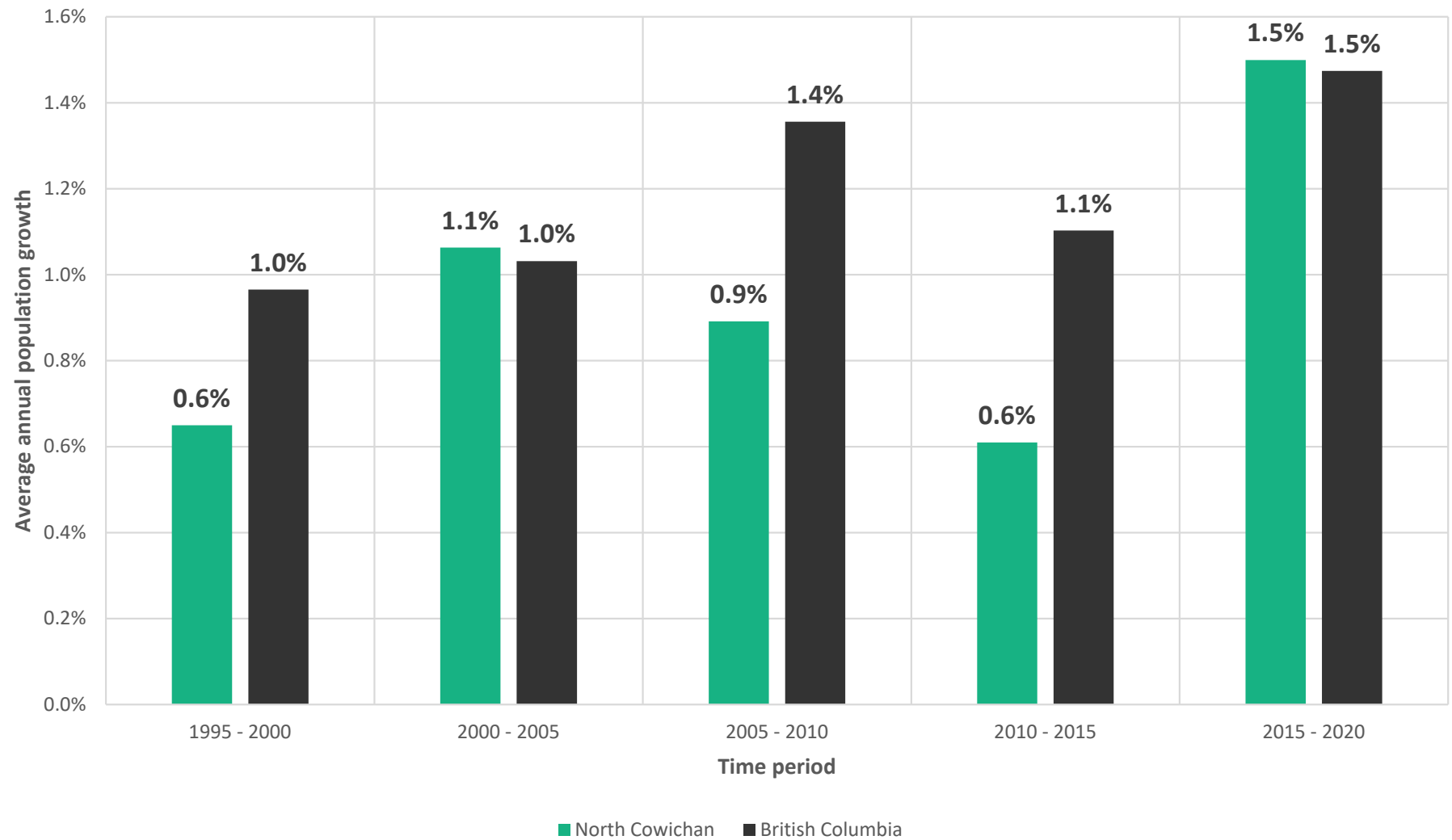
1) Introduction – my role

The purpose of this Open House is to:

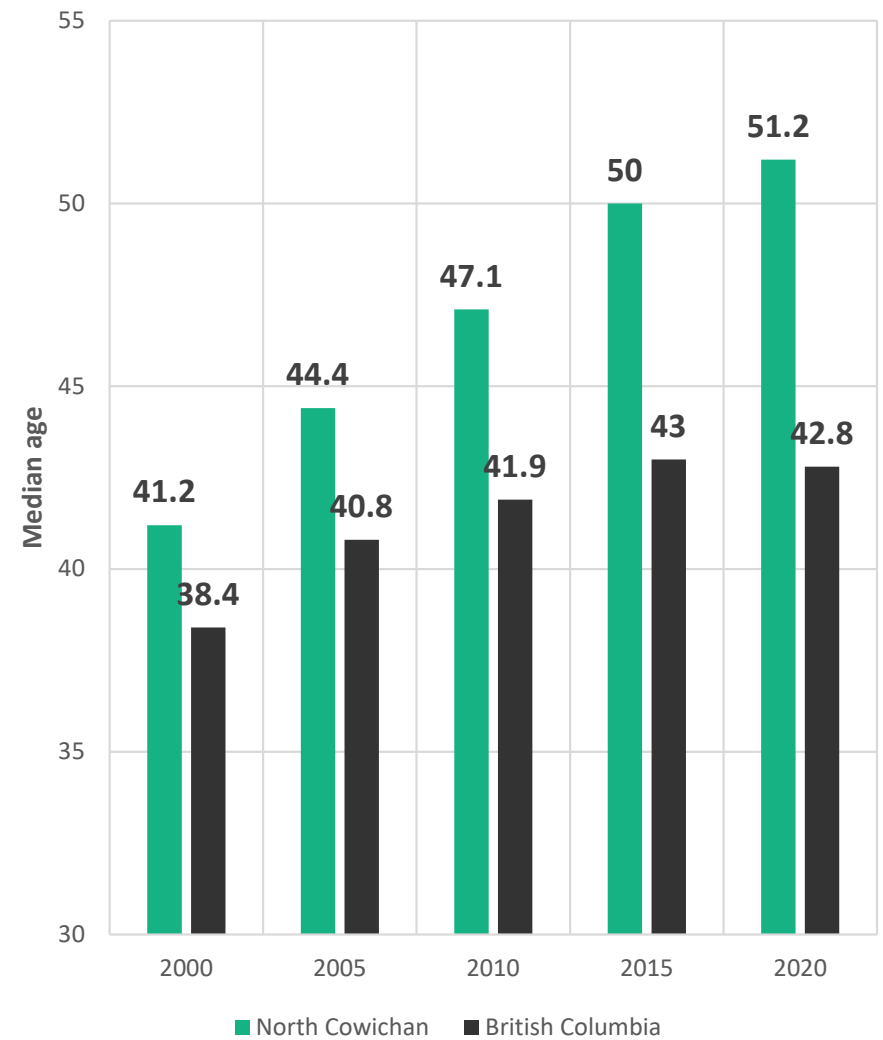
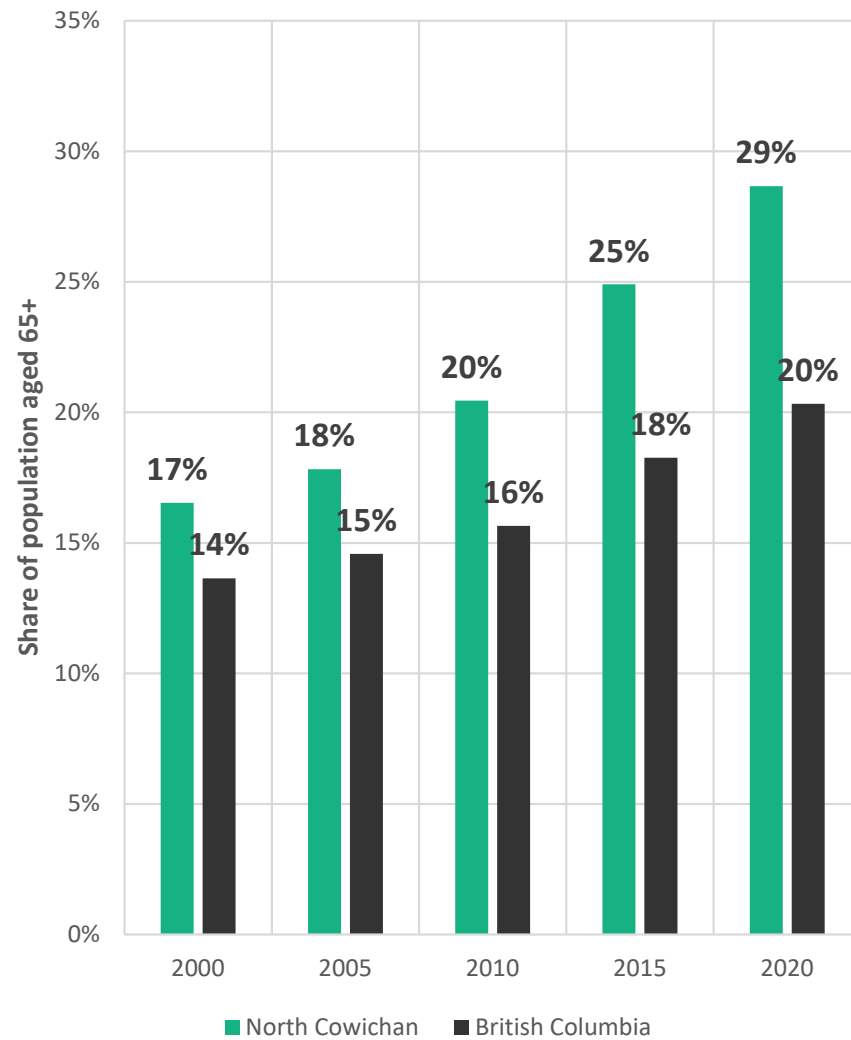
- Share with you my research findings
- Ground-truth assumptions about construction costs, profit margins, etc.
- Gather any other input about local development conditions.



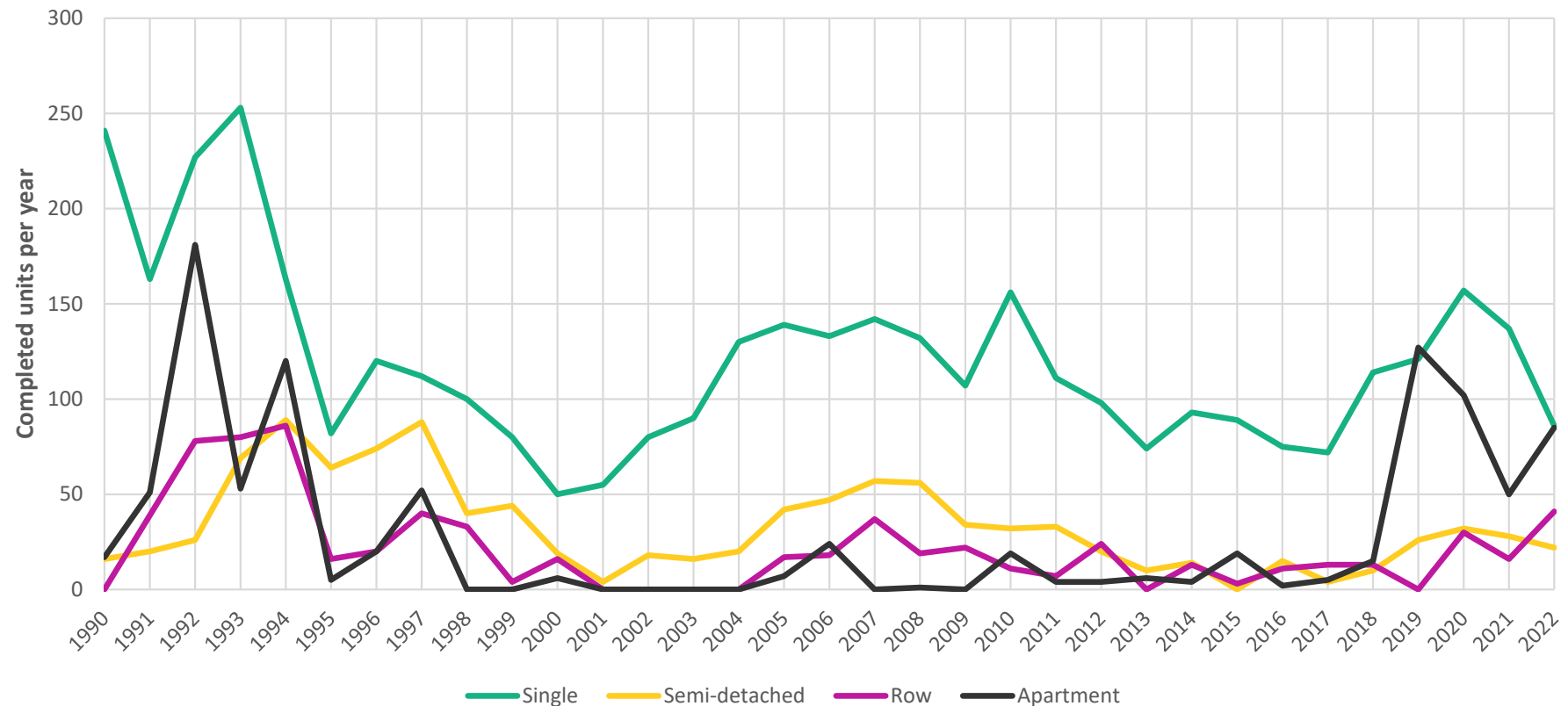
2) Market research – long-term trends



2) Market research – long-term trends



2) Market research – long-term trends



Share	Single family	Duplex	Townhomes	Apartments
1990 - 2022	59%	16%	10%	14%
2013 - 2022	59%	9%	8%	24%

2) Market research – recent trends

INFLATION

- Considerable inflation occurred in the first half of 2022: About 6% in 6 months, compared to a long-run average of 2% per year.
- Causes:
 - COVID-19 and the Invasion of Ukraine caused worldwide logistical problems
 - Canadian consumer sectors are increasingly prone to monopoly and oligopoly
 - Financial supports for households and industries during COVID increased the money supply.

2) Market research – recent trends

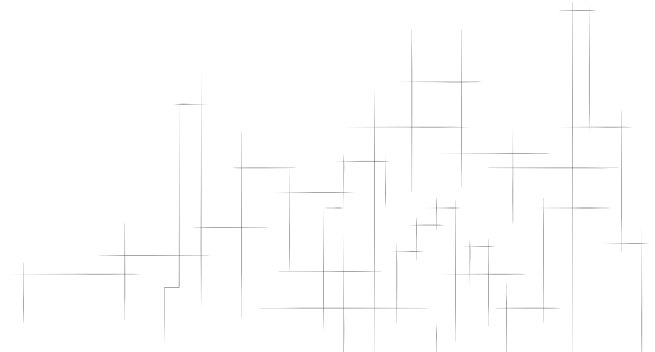
INTEREST RATES

- The Bank of Canada – Canada's arms-length monetary body – controls the Policy Interest Rate to try to keep inflation at approximately 2% per year.
- So in times like these, they INCREASE the interest rate to get people and firms to spend less money on goods and services, and more money on savings and debt. The aim here is twofold:
 - To encourage financial institutions to offer higher interest rates, to encourage household saving.
 - To mortgage payments through their interest component.

2) Market research – recent trends

INTEREST RATES

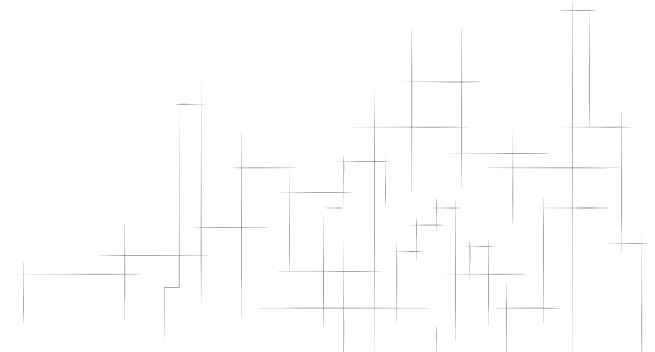
- The combination of high inflation and high interest rates has a powerful impact on the housing market as they both:
 - Make construction and financing more expensive
 - Reducing households' capacity to pay for housing.



2) Market research – recent trends

THE SUPPLY SIDE: BARRIERS TO DEVELOPMENT

- 1) High costs
- 2) High interest rates
- 3) Slow approvals
- 4) Restrictive land use designations within the OCP



2) Market research – recent trends

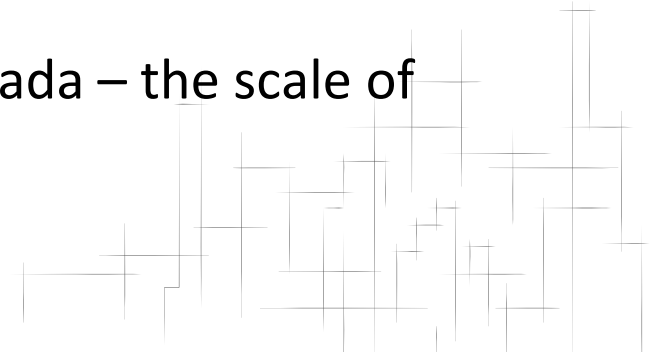
A NOTE ON HOUSING SHORTAGE

- 1) Canada and particularly BC do have a major housing shortage, causing housing to be widely unaffordable.
 - 2) This shortage is provincial and national in scale, and no single municipality is large enough to solve the problem alone.
 - 3) Increasing supply is the answer, but to work this increased supply must be widespread – every region of BC needs to significantly densify.
 - 4) In short, North Cowichan cannot single-handed solve the crisis.
- 

2) Market research – recent trends

THE DEMAND SIDE

- 1) COVID-19 was expected to cool Canada's housing market. Instead, 2020 set record sales and 2021 topped those sales.
- 2) Overall, the national MLS Home Price Index increased by 25% in 2021.
- 3) The COVID housing boom was geographically lopsided: housing prices in urban centers stagnated while those in more peripheral areas like North Cowichan soared.
- 4) Demand came to North Cowichan from across Canada – the scale of migration from Ontario was unprecedented.

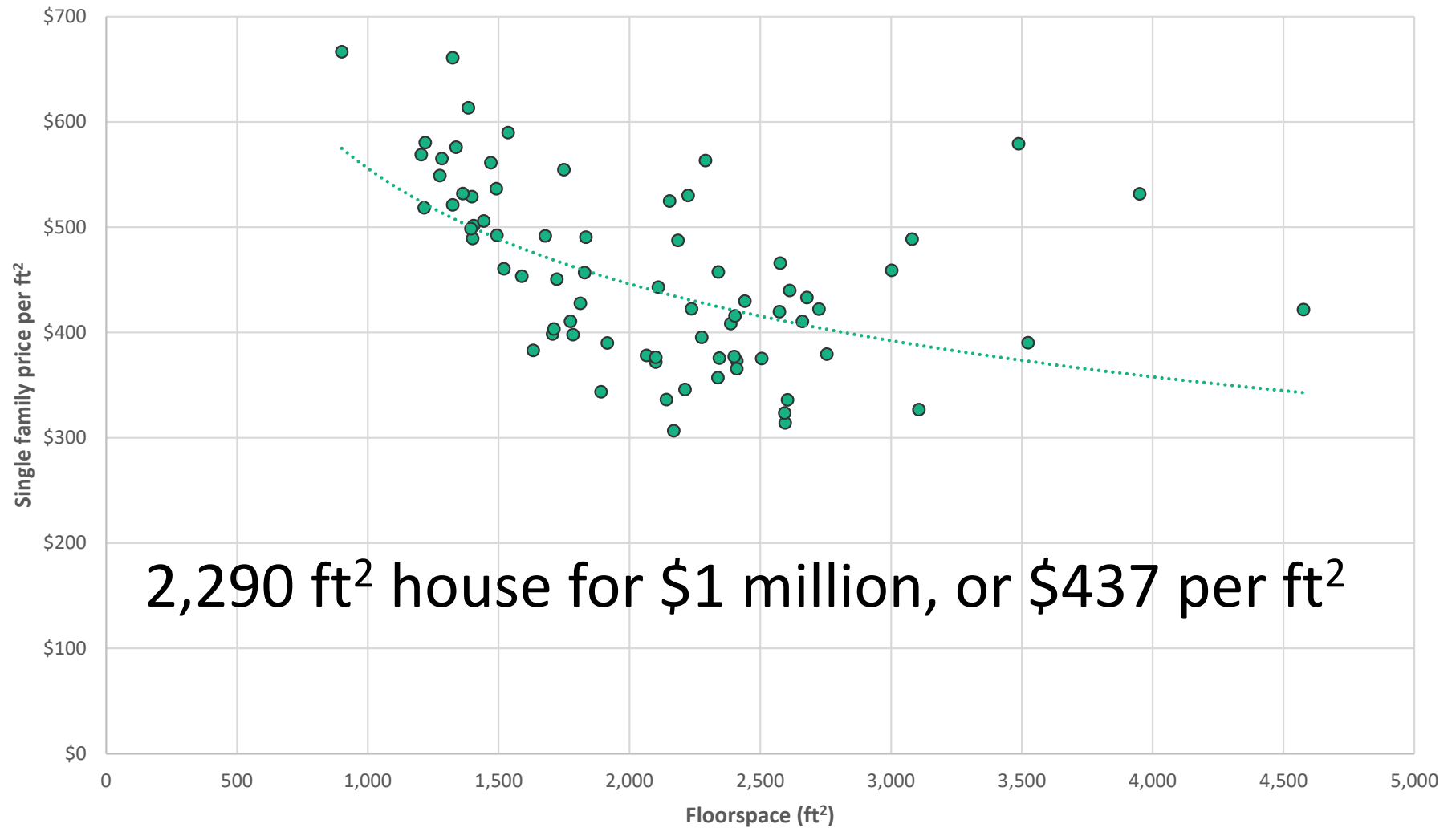


2) Market research – recent trends

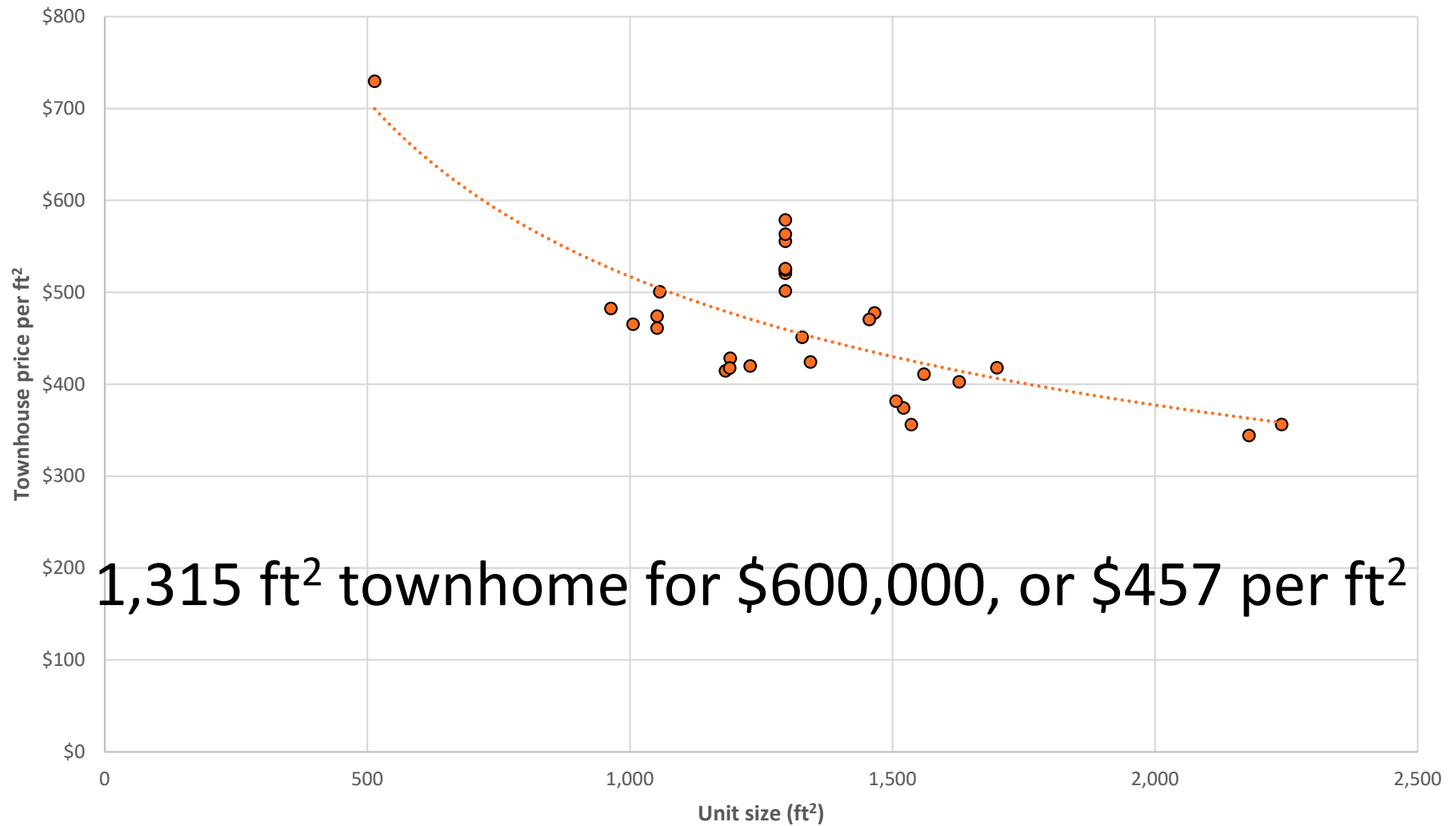
THE DEMAND SIDE

- 5) Then in summer of 2023, the Bank of Canada increased interest rates by a factor of 20 (from 0.25% to 5%), causing residential prices across Canada to stabilize or even fall.
- 6) According to realtors, housing prices in the Cowichan Valley peaked in February 2022 and have since decreased by 5% on average.
- 7) The pace of sales has also slowed down since the COVID housing boom.
- 8) High interest rates limit the budget of households using mortgages, but downsizing seniors are largely immune. The current situation therefore benefits seniors at the expense of younger households.

2) Market research – prices



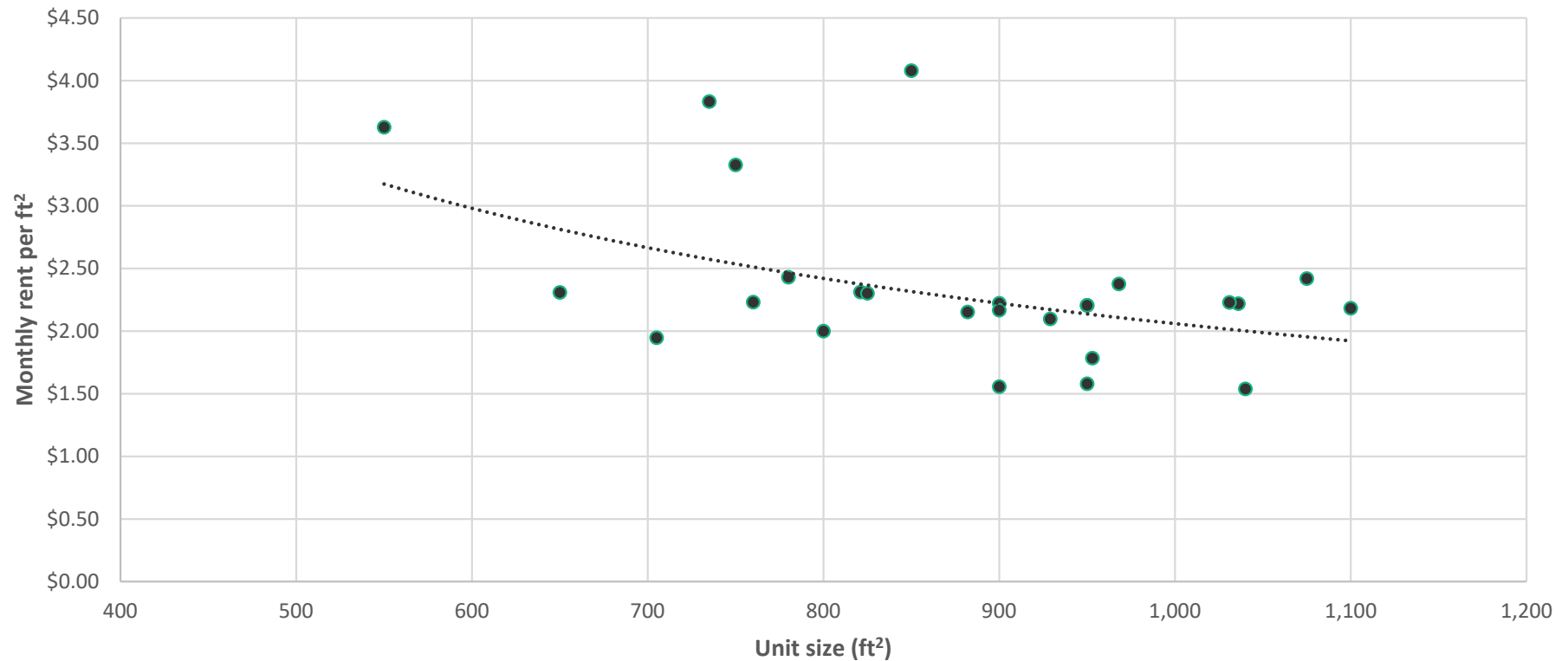
2) Market research – prices



2) Market research – prices

	Apartment size (sf)	Price
1-bedroom	600	\$360,000
2-bedroom	800	\$440,000
3-bedroom	1,100	\$550,000

2) Market research – prices

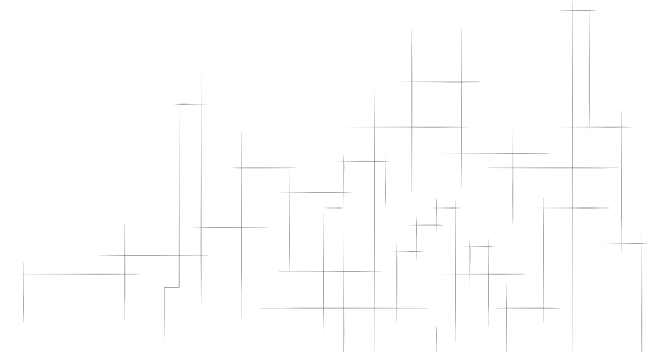


	Apartment size (sf)	Monthly rent
1-bedroom	635	\$1,650
2-bedroom	820	\$1,900
3-bedroom	1,030	\$2,350

3) Financial analysis – how CACs work

Community amenity contributions (CACs) and **density bonusing** are mechanisms that allow municipalities to acquire neighbourhood amenities in exchange for increased density.

They are based on the same economic principle but use different policy mechanisms.



3) Financial analysis – how CACs work

These funds are typically applied to:

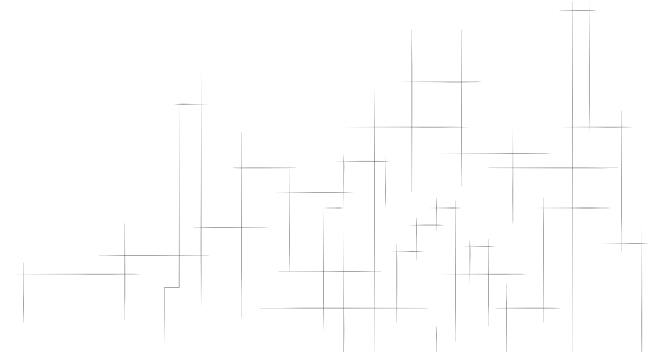
- Affordable housing
- Community facilities
- Park improvements
- Street beautification
- Fire halls
- Transit infrastructure



3) Financial analysis – how CACs work

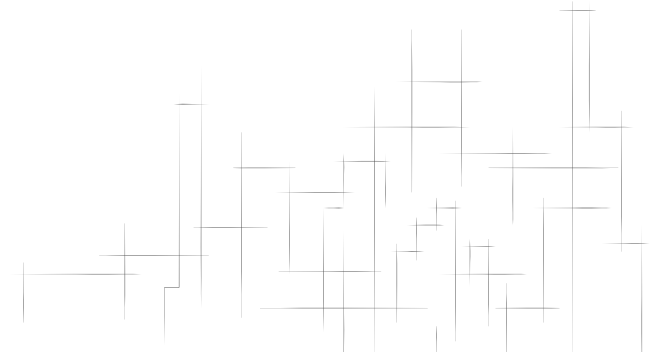
Density bonusing is codified directly into the zoning bylaw; it is part of the parcel's zoning and does not require rezoning to be used.

Typically the zoning will specify two densities: a lower density that may be developed as-of-right with no contribution, and a higher maximum density that may be developed if a contribution is provided.



3) Financial analysis – how CACs work

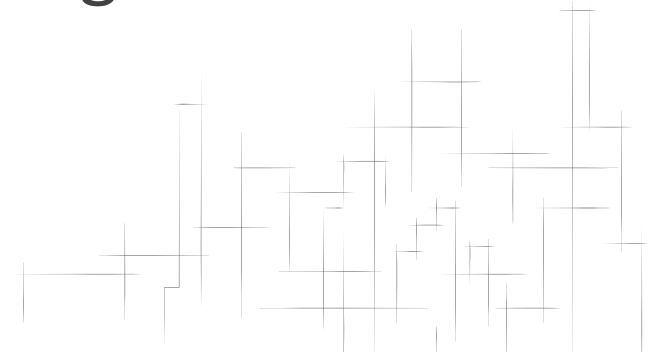
Density bonusing is expressly permitted by the Local Government Act, Section 482.



3) Financial analysis – how CACs work

Community amenity contributions are the product of negotiation between the developer and the municipality. This may only take place during the rezoning phase.

This power is not expressly granted by any statute but is an automatic extension of the municipality's power to legislate zoning.

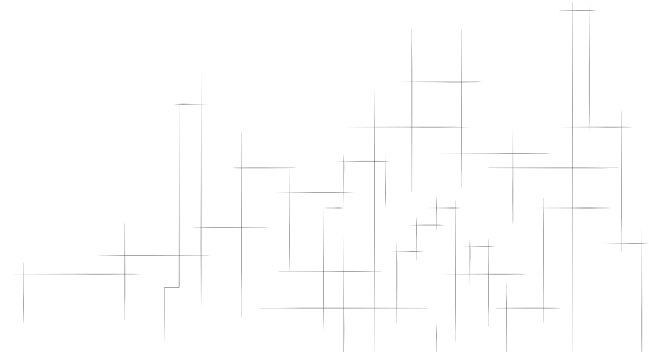


3) Financial analysis – how CACs work

What is the maximum size of an amenity contribution?

Since contributions are always voluntary and developers always have a lower-density option that doesn't require a payment, there's a point at which the bonus density isn't “worth it” to the developer.

This amount can be calculated.

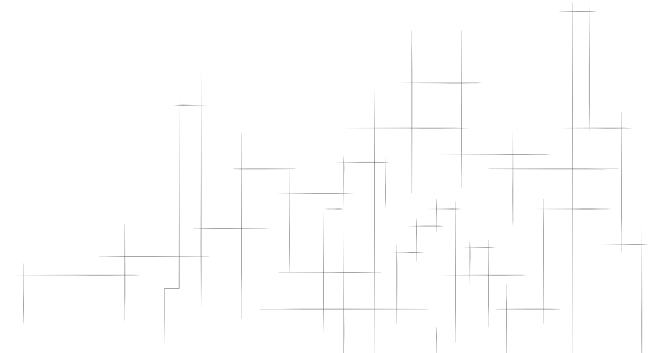


3) Financial analysis – how CACs work

Consider the following equation:

$$\text{Revenue} - \text{project costs} - \text{profit} = \text{land price}$$

The money for a CAC has to come from some combination of these four items.

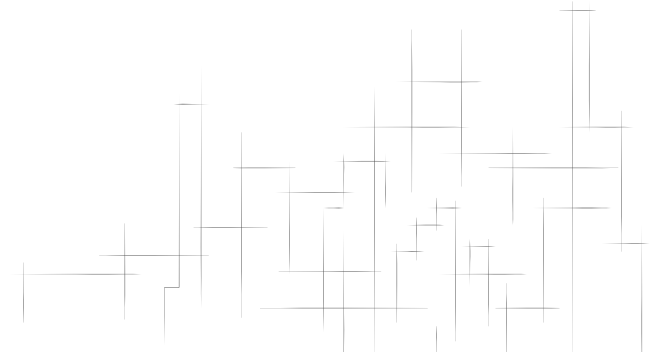


3) Financial analysis – how CACs work

Consider the following equation:

$$\text{Revenue} - \text{project costs} - \text{profit} = \text{land price}$$

Revenue is set by the market. If the developer could charge more, they already would have.

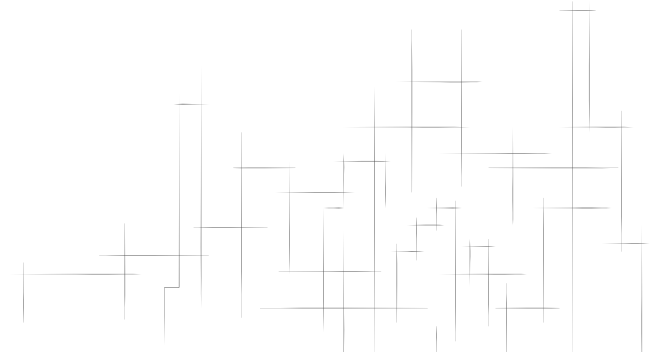


3) Financial analysis – how CACs work

Consider the following equation:

$$\text{Revenue} - \text{project costs} - \text{profit} = \text{land price}$$

Costs are set by the market. If the developer could lower them, they already would have.

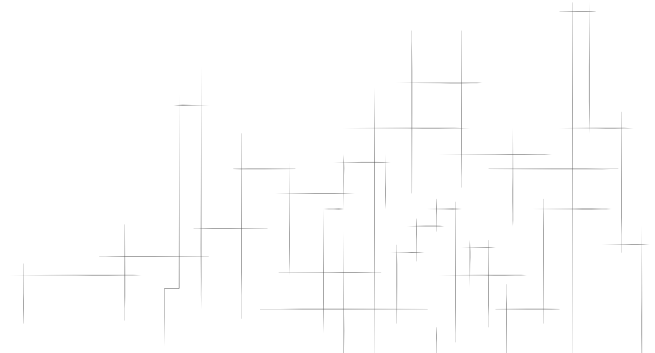


3) Financial analysis – how CACs work

Consider the following equation:

$$\text{Revenue} - \text{project costs} - \text{profit} = \text{land price}$$

Developers are not very willing to reduce this item.

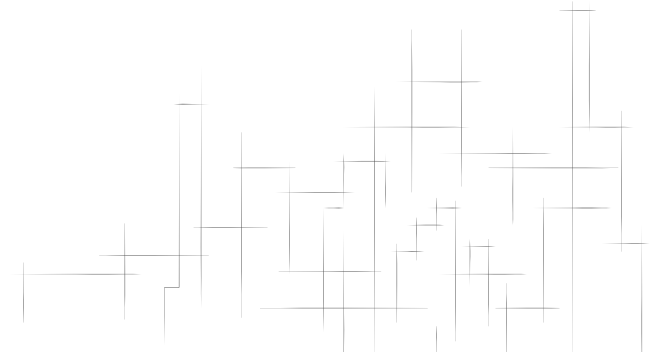


3) Financial analysis – how CACs work

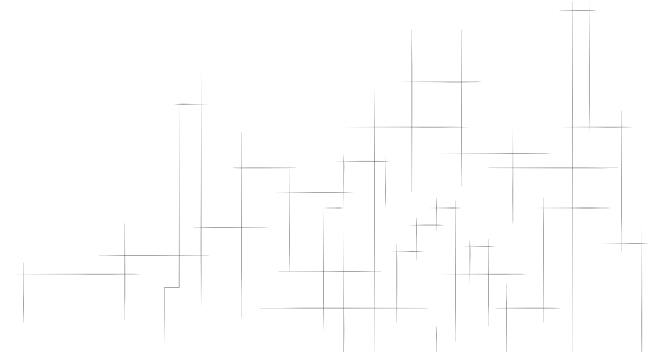
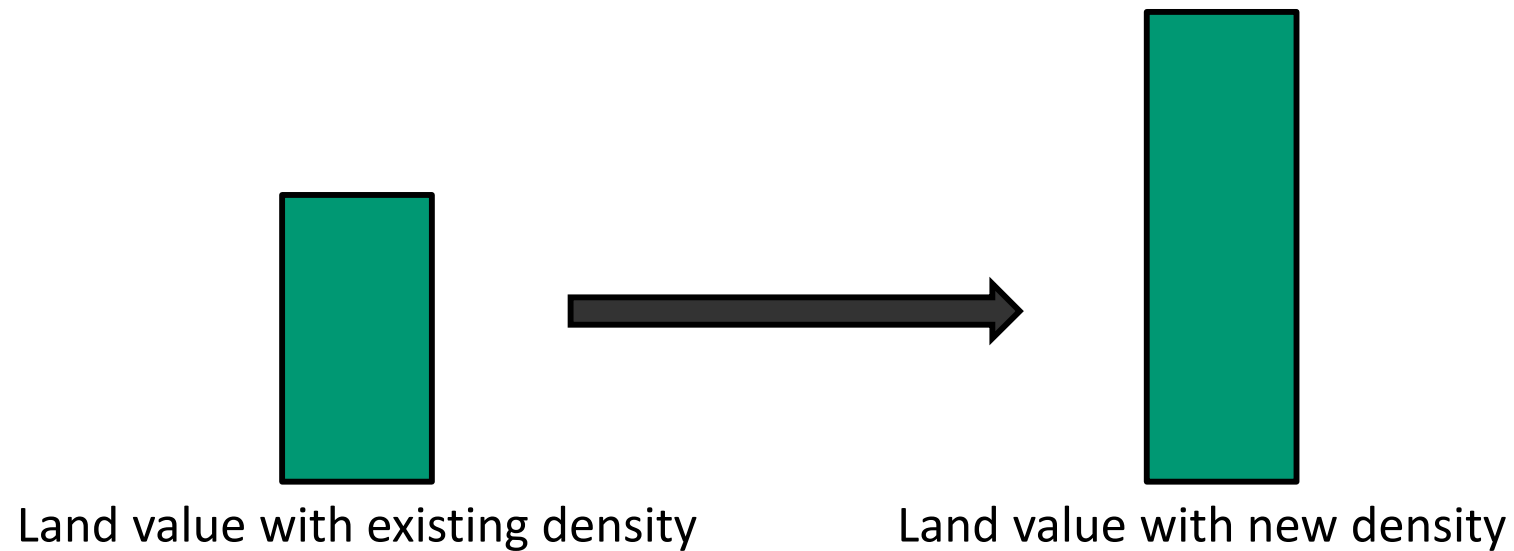
Consider the following equation:

$$\text{Revenue} - \text{project costs} - \text{profit} = \text{land price}$$

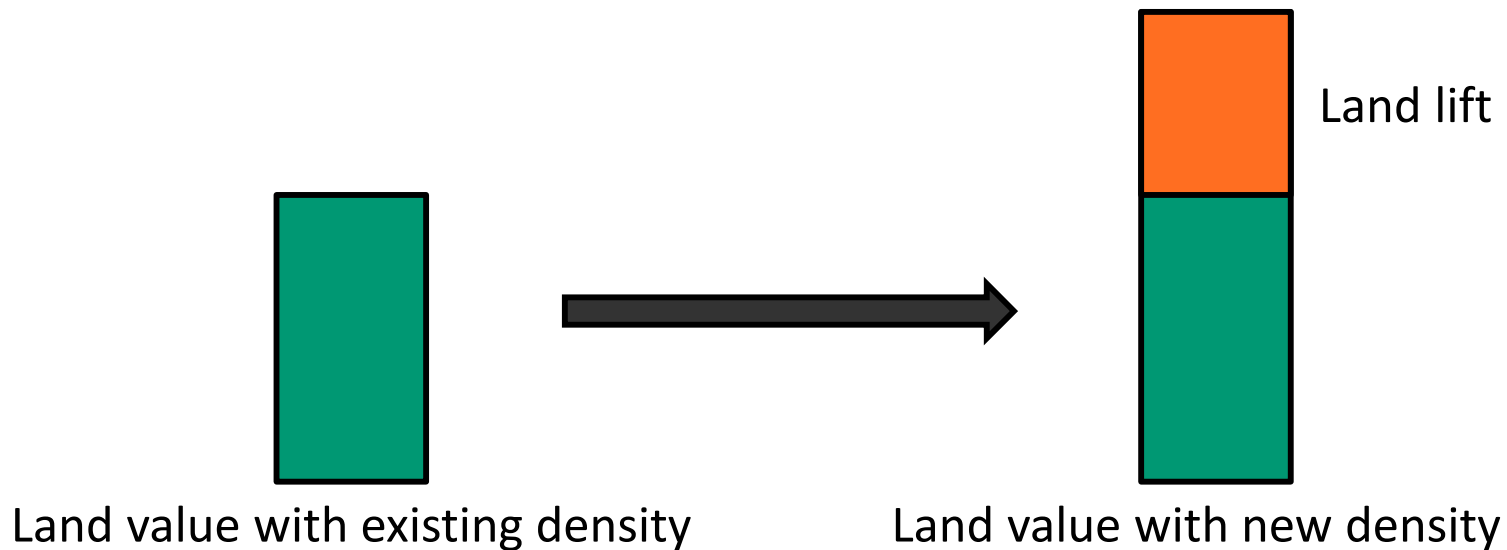
By process of elimination, CACs come mostly out of land cost.



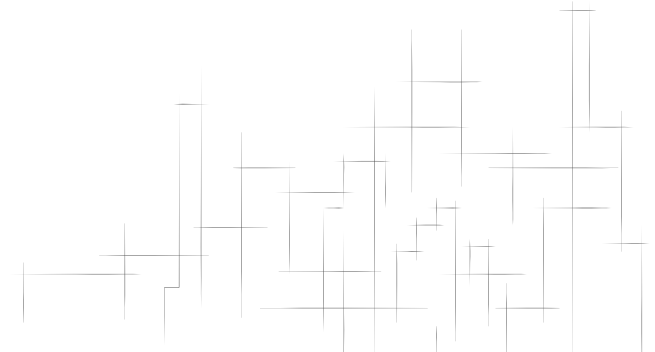
3) Financial analysis – how CACs work



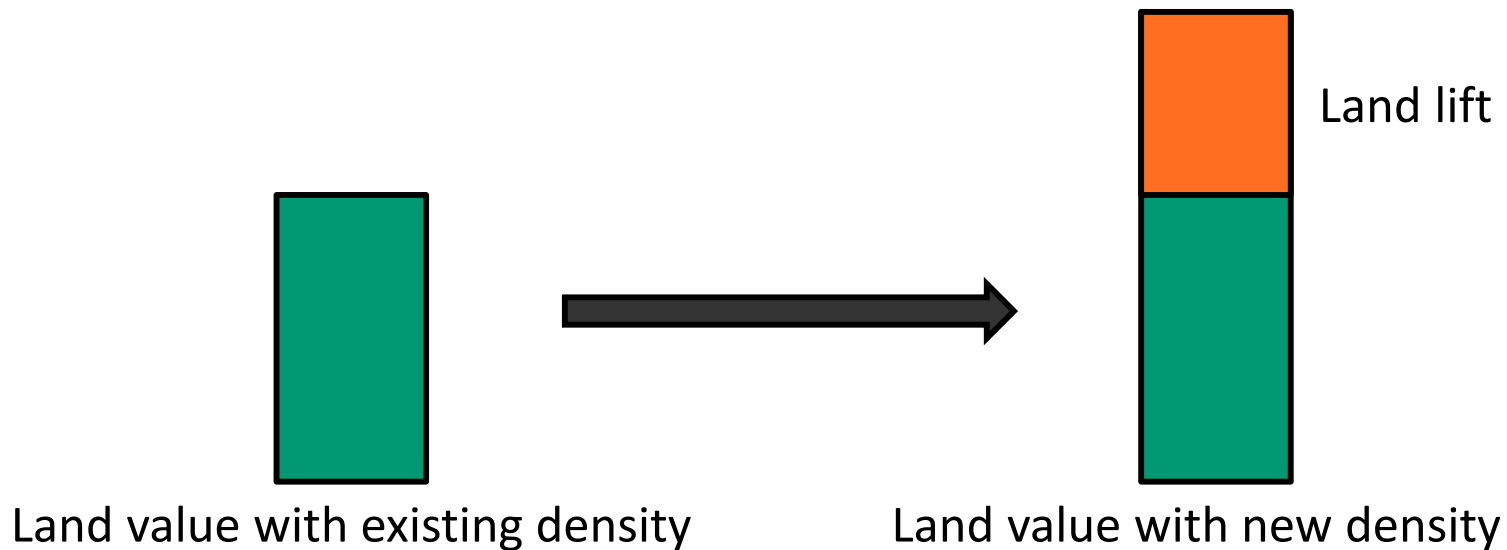
3) Financial analysis – how CACs work



With more density, the developer can afford to pay **this much** more for the land.



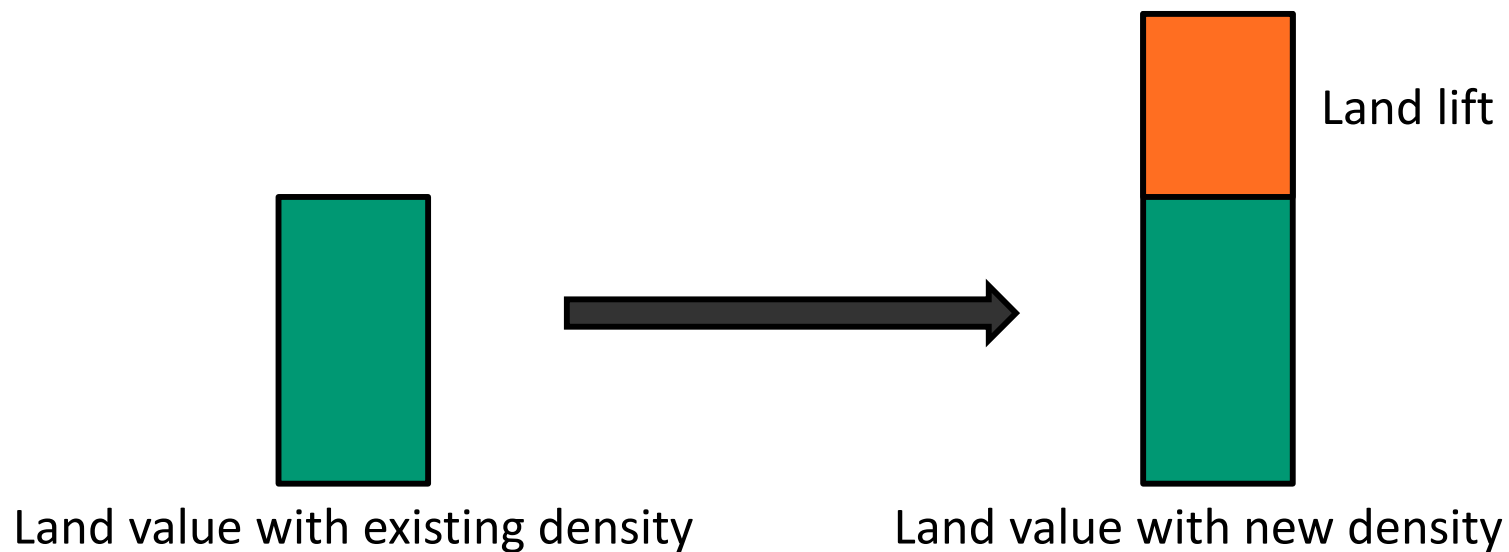
3) Financial analysis – how CACs work



So, assuming the developer did not pay too much for the land, they should be willing to part with **this much** money to access the higher density option.



3) Financial analysis – how CACs work



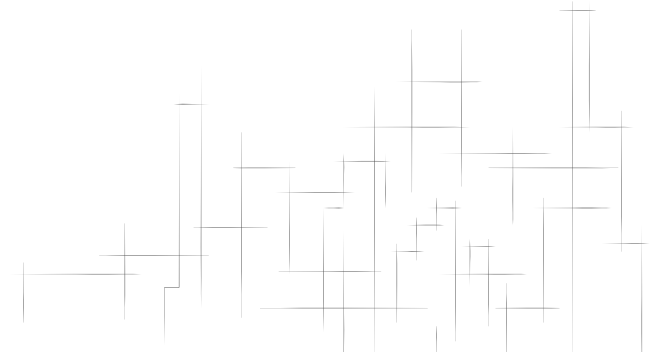
In summary, the land lift amount represents the maximum size of an amenity contribution.



3) Financial analysis – how CACs work

Land lift is always created whenever land is rezoned.

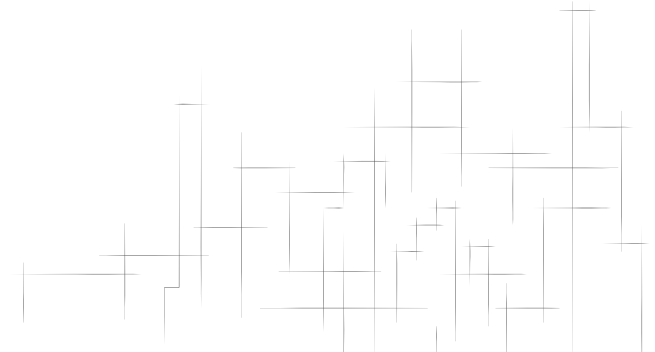
Without a CAC mechanism of some kind, this land lift is split between the developer who buys the land, and the previous landowner who sells it to them.



3) Financial analysis – how CACs work

There's nothing wrong with this arrangement.

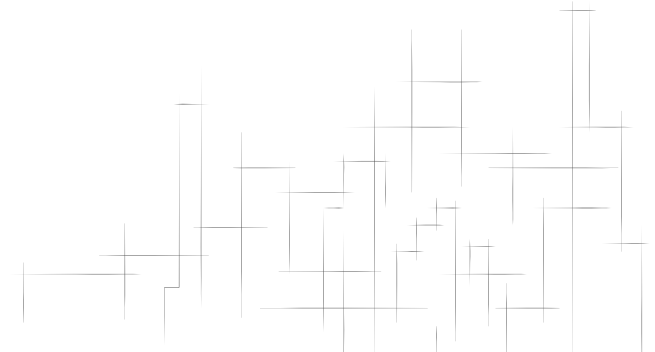
It has the advantage of giving landowners an incentive to support denser development since they stand to benefit from speculative value.



3) Financial analysis – how CACs work

But this new value is the direct result of a change in zoning – the community's policy – and not a result of:

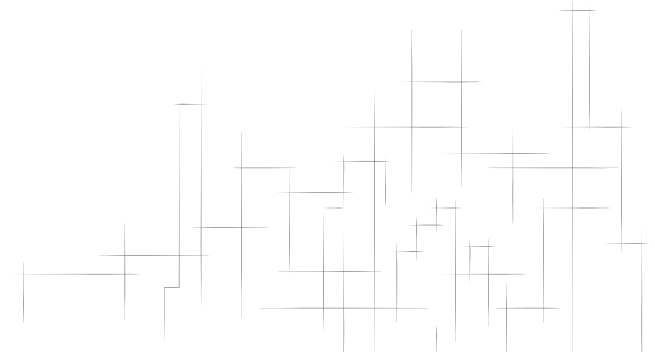
- 1) The previous landowner's labour (all they did was wait)
- 2) The developer's labour (the value they add comes later).



3) Financial analysis – how CACs work

So why shouldn't the community reclaim this value created through legislation?

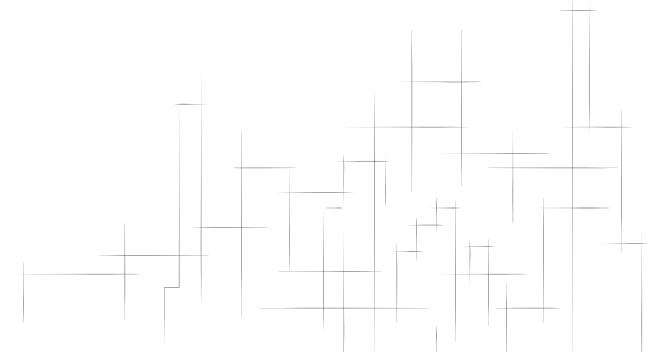
And why shouldn't new development fund the creation of the amenities it necessitates, such as fire halls, parks, etc.?



3) Financial analysis – how CACs work

Aside #1

I should point out now that even when CACs are used to pay for infrastructure and amenities, there is usually still an “assist factor”: property taxes from existing development pays a share as well.



3) Financial analysis – how CACs work

Aside #2

There is genuine disagreement between economists, planners, developers, and politicians about whether this approach to amenity cost recovery is ideal or sustainable. I acknowledge this disagreement.

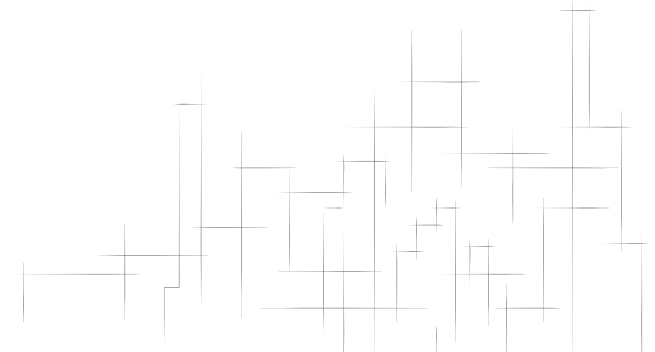
However, that's not my research question: I've been retained to calculate this land lift amount.



3) Financial analysis – how CACs work

Most municipalities don't ask for 100% of the land lift amount, but in the range of 25% - 75%. This has the following advantages:

- It leaves some room for error
- It leaves some land lift available for existing property owners and developers, as an incentive.

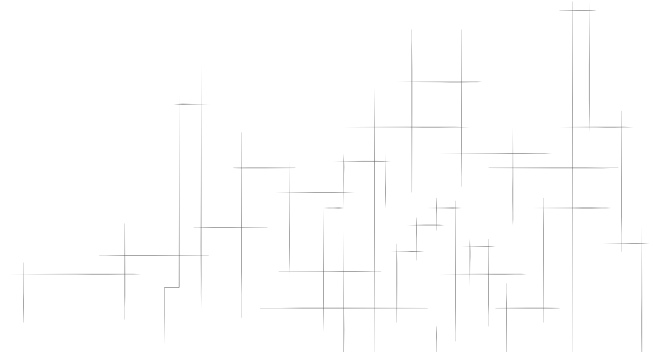


3) Financial analysis – how CACs work

Two approaches to land lift

Site analysis: calculated based on the site's specific characteristics

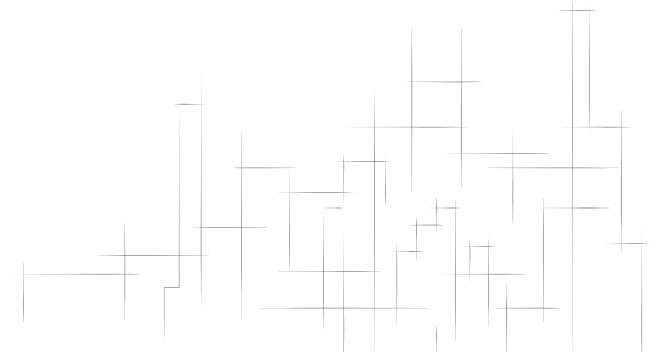
Blanket rates: Apply the same rate or formula to all rezonings, usually based on generic analysis or case studies



3) Financial analysis – how CACs work

Site analysis:

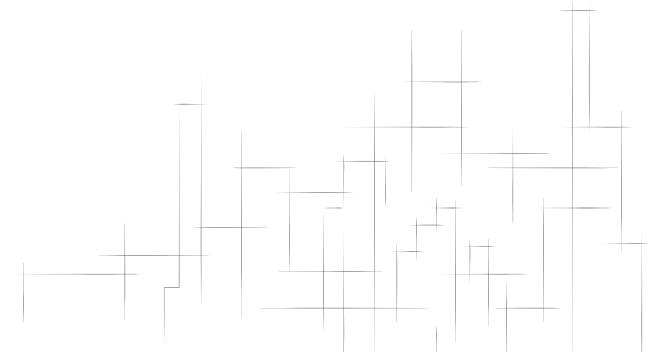
- Technically preferable and more accurate, but time-consuming and costly.
- Developers also find it unpredictable and would rather know the CAC rate in advance so they can make business decisions.



3) Financial analysis – how CACs work

Blanket rates:

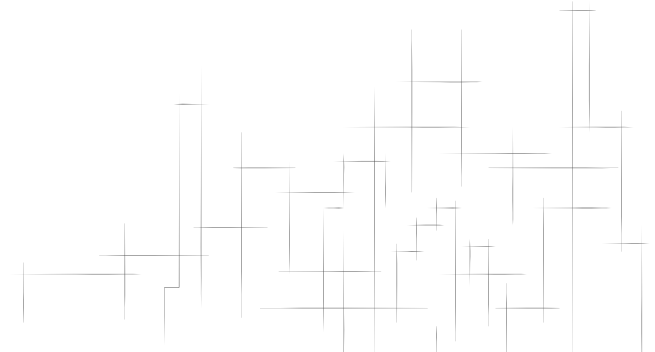
- Less accurate but more practical.
- Creates more developer confidence.
- Should be updated every 2 – 5 years.



3) Financial analysis – how CACs work

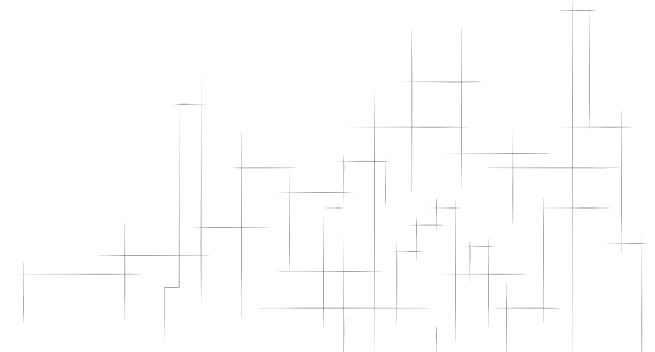
Amenity contributions can take the form of cash or in-kind spending, but **affordable housing on-site** can also be a CAC.

Instead of increasing costs, this just decreases revenue. The impact on land value is the same.

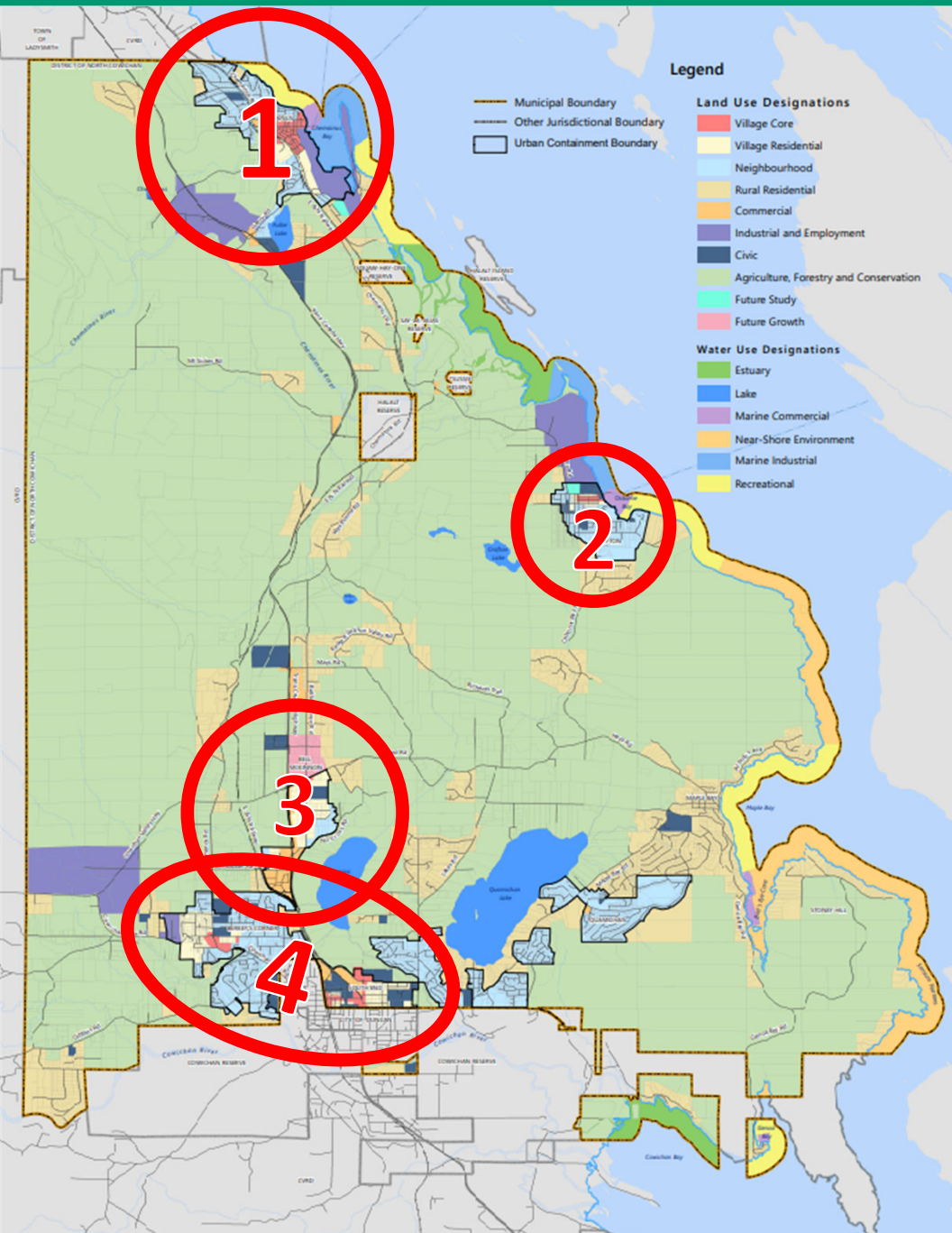


3) Financial analysis – Scenarios

So, to get a sense of supportable CAC rates, we will perform a financial analysis of 72 different scenarios in North Cowichan



3) Financial analysis – Scenarios



Geography

1) Chemainus

2) Crofton

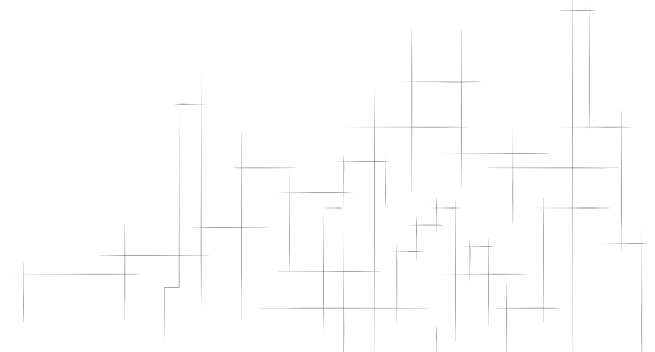
3) Bell McKinnon

4) South End

3) Financial analysis – Scenarios

Site size (based on examples from MCN):

- A 32,292 ft² (0.74 ac) site consisting of 4 single-family lots
- A 5.9 ac site consisting of one lot.



3) Financial analysis – Scenarios

Land use:

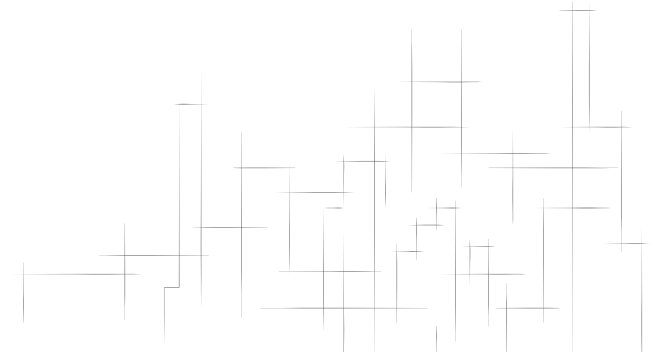
- Single family
- Duplex (8,073 ft² lots)
- Duplex (5,382 ft² lots)
- Townhouse at two densities (0.35 FSR – 1.8 FSR)
- Strata apartments at two densities (1.1 FSR – 2.5 FSR)
- Rental apartments at two densities (1.1 FSR – 2.5 FSR)
- Mixed use (strata apartments), at two densities (1.2 FSR – 2.5 FSR)
- Mixed use (rental apartments), at two densities (1.2 FSR – 2.5 FSR)



3) Financial analysis – Scenarios

Combining these geographic, site area, and land use options yields 72 scenarios.

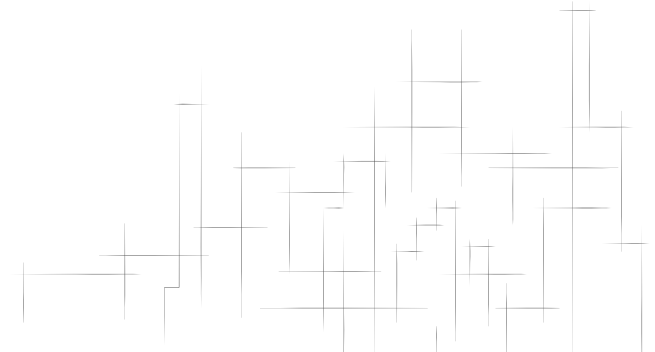
- We will model each development as if it happened today, to calculate its residual land value (the amount a developer could afford to pay for it).



3) Financial analysis – Assumptions

Profit:

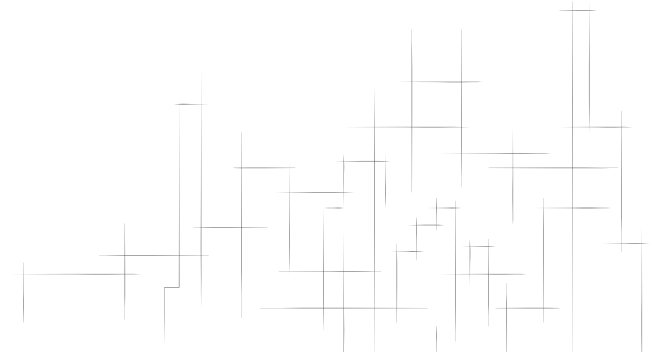
- Single family on small sites: 12% profit to cost
- Duplex on small sites: 13.5% profit to cost
- All other products for sale: 15% profit to cost
- Rental: 5.9% IRR
- Commercial: 7.75% IRR



3) Financial analysis – Assumptions

Price of vacant single family lots:

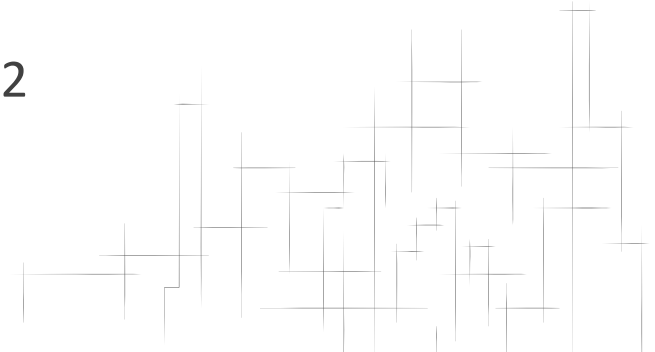
- \$200,000 - \$250,000 per lot



3) Financial analysis – Assumptions

Construction costs:

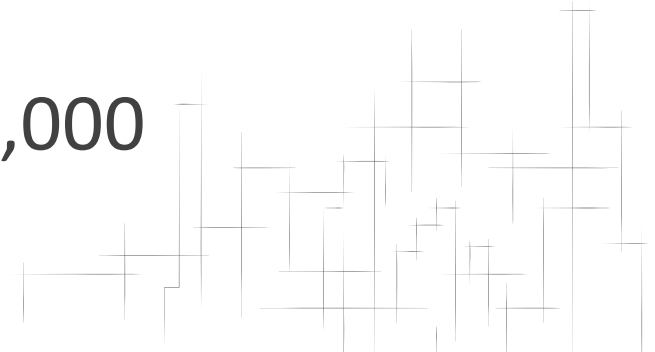
- Single family: \$220 per ft²
- Townhouse: \$242 per ft²
- 4-storey apartments: \$295 per ft²
- 6-storey apartments: \$304 per ft²



3) Financial analysis – Assumptions

Other hard costs:

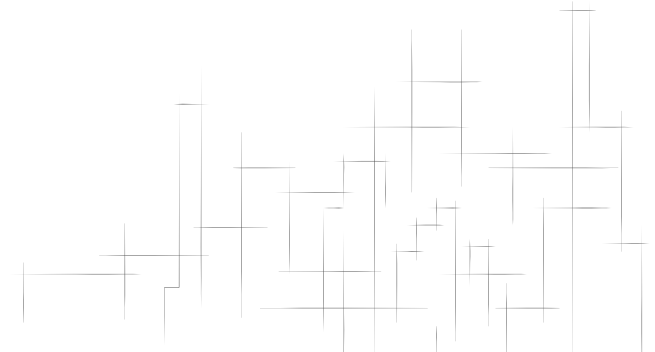
- Site servicing and geotechnical:
 - Small sites (32,300 ft²):
 - Four single family or duplex lots: \$50,000
 - Other uses: \$60,000
 - Large sites (5.9 ac):
 - One dwelling (acreage): \$50,000
 - Other uses: \$200,000



3) Financial analysis – Assumptions

Other hard costs:

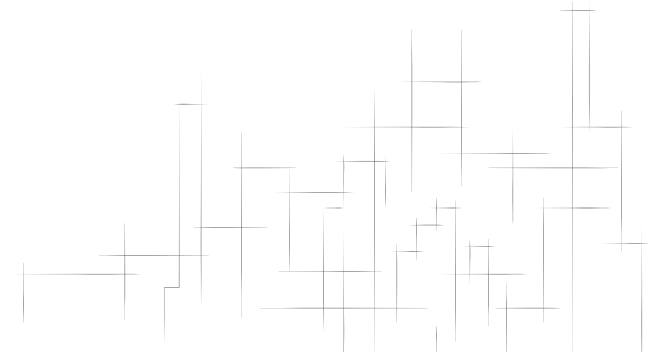
- Servicing connection fees:
 - Small sites (32,300 ft²):
 - Four single family or duplex lots: \$30,000
 - Other uses: \$50,000
 - Large sites (5.9 ac):
 - One dwelling (acreage): \$7,500
 - Duplex (5,400 ft² lots): \$600,000
 - Other uses: \$480,000



3) Financial analysis – Assumptions

Other hard costs:

- Furniture, fixtures, & equipment:
\$100,000 - \$150,000 per apartment building
- Landscaping, signage, and lighting:
\$50,000 per apartment building, mixed-use building, or large lot development.
- Surface parking: \$6,125 per stall
- Underground parking: \$60,000 per stall
- Hard cost contingency of 10%



3) Financial analysis – Assumptions

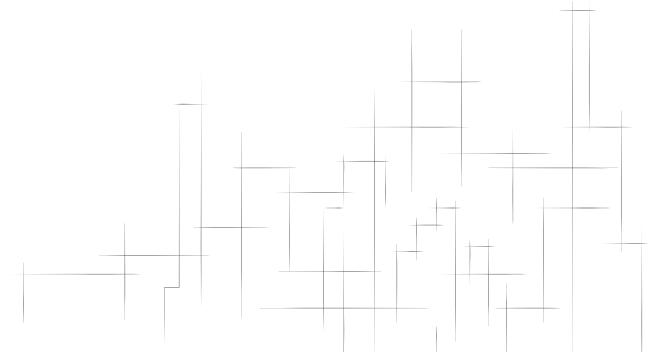
Soft costs:

- Generally ranging from 5% for single family up to 20% for mixed-use developments.
- DCCs: The current DCCs, plus:
 - 25% for inflation
 - An extra \$3.10 per ft² in Bell McKinnon
 - An extra \$7,261 per hectare for commercial sites in Bell McKinnon.

3) Financial analysis – Assumptions

Financing costs:

- Loan to value ratio:
 - Land loan: 50%
 - Construction loan: 75%
- 7% interest
- Planning time: 12 months
- Construction time: 12 – 24 months



4) Next steps

Next steps:

- Refine numerical estimates for costs and revenues based on today's discussion
- Conduct sensitivity analysis on some of these variables
- Produce a final analysis and accompanying report to be presented to Council in Nov/Dec
- Final report will be used by MNC to inform subsequent policy details for Affordable Housing and CACs.

Thank you!

I invite questions and discussion.

