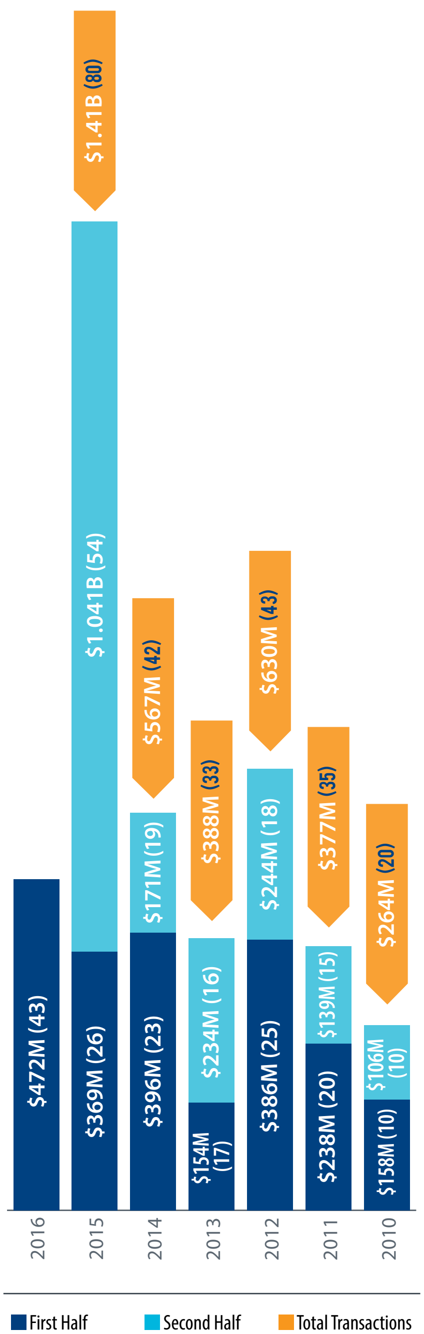
Fall 2016 Multi-Family Investment Report

British Columbia

MARKET TRENDS
MULTI-FAMILY INVESTMENT SALES
(> $5 million) January 1 to December 31



Elevated deal velocity boosts BC multi-family transactions to record first-half sales

Investors' seemingly insatiable appetite for BC multi-family assets – despite an apparent lack of product and capitalization rates that remain highly compressed – powered sales volume to record territory in the first half of 2016. Following the record-setting back half of 2015 when 54 transactions valued at more than $1.0B were completed, multi-family investment activity remained elevated in the first half of 2016 with 43 transactions valued at $472M recorded from January to June – a first-half record. This compares with 26 deals valued at $370M in the first half of 2015 and 23 deals valued at $396M (the previous first-half record) in the first half of 2014. (Avison Young only tracks multi-family investments trading at more than $5M.)

Premium pricing and highly compressed cap rates continued to define BC's multi-family investment market, particularly within Metro Vancouver. Private investors were involved as buyers and vendors in every transaction in the first half of 2016. Most institutional investors simply do not have a mandate to acquire properties with such low cap rates and, combined with a lack of assets of scale available for purchase in BC, have largely avoided the asset class with limited exceptions during the past 18 months. Strong demand for multi-family product has pushed select properties to a 2% (or slightly less) cap rate and those properties with cap rates of 3% to 4% may continue to compress further yet.

Listings remained tight and large deals few and far between in the first half of 2016 with the largest deal being the sale of the Berkeley for $43M. Seven other deals exceeded $15M while 10 other deals were between $10M and $15M. Supply constraints have limited deal velocity while those properties that do trade achieve a significant premium.

Multi-family building sales in Metro Vancouver were included in the new 15% levy on residential purchases made by foreign nationals that was introduced on August 2, 2016. While the impact on multi-family sales will not likely be known until year-end, the levy is not anticipated to have a significant effect on deal volume or pricing in the second half of 2016. Foreign capital may shift to other asset classes, such as retail or office investments, or move to other BC markets if the tax succeeds in making multi-family properties too expensive for foreign nationals to acquire. However, price increases in communities outside of Metro Vancouver, such as Victoria and Nanaimo, had already been registered prior to the introduction of the tax.

The acquisition of multi-family assets with an eye to redevelopment into condominiums was prevalent in Burnaby as well as Vancouver in the first half of 2016, with the prices paid on a per-door basis providing a strong indication of the likely fate of these typically older apartment buildings. While there has been growing community opposition to this practice, particularly in Burnaby, the likely redevelopment and pending demolition of older and often less expensive rental housing in the Metrotown area will likely proceed, and investors will continue to seek out

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multi-family properties deemed suitable from a rezoning and locational perspective for redevelopment.

"With respect to financing, the lending community has become very selective in recent months as overall market uncertainty continues," says **James Paleologos**, a senior associate with **RealTech Capital Group**. "2016 started strong and many banks had already placed the majority of their annual budgets by mid-spring. This strong start to the year has allowed them to essentially halt or slow down lending while they assess the market in the wake of the foreign buyers' tax announcement.

"While term debt is still relatively available, conventional lenders' spreads above the bond have begun to increase by 20 to 40 basis points and lenders who were able to underwrite apartments aggressively have become more conservative for the time being," adds Paleologos. "**Canada Mortgage and Housing Corp. (CMHC)**, on the other hand, has lowered its underwriting cap rates and has only experienced minimal lender spread increases by five to 10 basis points. In the current apartment financing market, we are frequently able to achieve higher loan amounts with CMHC than we can using a conventional underwriting while still receiving the low rate associated with an insured mortgage."

Little product is anticipated to come to market in the second half of 2016 and that could lead to further downward pressure on cap rates while foreign capital is likely to take a pause and evaluate the impact the tax has on sales activity. Residential land sales and assemblies are likely to slow and some may be dropped, but this is expected to be temporary as developers reevaluate residential land values and potential joint ventures backed with foreign capital.

Higher pricing is anticipated to continue to drive sales volume in 2017 as a constrained supply of available assets lead to more off-market sales and lower cap rates, as investors acquire properties as a form of capital preservation as opposed to purchasing income-generating assets. The drive to acquire rental properties will be further supported by the higher rental rates that quality well-located assets can command from tenants due in part to CMHC-posted vacancy rates of just 0.8% in the Vancouver census metropolitan area and 0.6% in the city of Vancouver itself.

Higher rents, extremely low vacancy and incentives from municipal governments will continue to drive the development of purpose-built rental buildings, but demand will continue to outpace the delivery of new units for many years to come. Community opposition against higher-density residential development, particularly in the city of Vancouver, continues to impede delivery of additional rental (and strata) units that could boost supply and help alleviate pressure on the supply of the rental housing. Purpose-built rental buildings may match or exceed the price-per-square-foot achieved for new strata product in certain Vancouver neighbourhoods such as Mount Pleasant due to strong demand and willingness of tenants to pay higher rents to live in the popular area.

Expect the acceleration of the wind-up of residential strata corporations throughout Metro Vancouver in 2017 as amended regulations introduced in early 2016 lowered the threshold necessary for a strata council to dissolve the strata in order to sell the property for redevelopment.

While the vast majority of multi-family transactions in the first half of 2016 occurred within Metro Vancouver (particularly in Vancouver proper), a renewed focus on secondary markets is anticipated as pricing and the foreign buyer's tax force those investors chasing higher yields and available supply to increasingly consider other markets in BC. ■

Darren Donnelly, chair of the commercial real estate group at **Clark Wilson LLP**

Q&A

Avison Young speaks with Darren Donnelly, Partner, Clark Wilson LLP, about recent changes to BC laws related to the dissolution of stratas

What does the recently amended legislation allow for that is different from what was permitted previously? What is the impact of this change?

Strata corporations are now permitted to wind up if two things happen: first owners controlling at least 80% of the votes resolve to wind up and then the resolution is confirmed by the court. Previously a unanimous resolution was required, which was virtually impossible for any strata corporation with more than a couple of dozen owners.

Of course, winding up a strata corporation only means that all of the individual former strata lot owners then become co-owners of the single pre-development legal parcel. In order to then sell the parcel, the only practical way to proceed – assuming no unanimity among the owners – is to appoint a liquidator to carry out the sale. This is provided for in the Act, although there is not much detail.

The impact should be to add to the supply of multi-family development lands. They should be attractive sites, given that they

Strata corporations are volatile creatures and great care must be taken to implement a process that is fair and transparent
- Darren Donnelly

will already be zoned for multi-family use and in many cases be part of an official community plan which contemplates increased density.

What would be the process once a strata decides to dissolve?

Although the legislation is far from perfect, and the court part of the process is as yet untested, the formal process is fairly simple in concept: The owners vote to wind up and appoint a liquidator; the court approves both of these resolutions; the liquidator arranges a sale and the owners approve it; the court grants an order vesting title in the liquidator who then completes the sale to the purchase and distributes the proceeds to the owners and mortgagees.

But that process is awkward. In practical terms, for example, the sale needs to be arranged and unconditional before it ever gets to court. The court will need to make orders which recognize many realities and logistics not addressed in the legislation.

How much are strata owners really involved? Walk us through the process.

Strata corporations are volatile creatures and great care must be taken to implement a process that is fair and transparent and respects the rights and concerns of the individual owners. We are dealing with people's homes. It is tempting for those of us used to dealing with commercial properties and developments to view the purchase and sale aspect primarily in economic and business terms, but that is simply not the basis on which many of the owners will make their decision. Handled indelicately, misinformation and emotion may play a big role.

Once talk of a wind up starts within a strata, it is very important for the strata council to organize an informal information meeting. Next, preliminary professional advice should be sought from the strata's property manager and lawyer. Generally, it is in the owners' best interests, individually and collectively, to act together. If there is significant interest in proceeding, they should take steps toward hiring a broker and gaining an understanding of the market for the property, typically as a re-development site.

The strata council should then seek formal authorization from owners to enter into a listing agreement and to incur expenses, primarily for legal advice. The property should be widely marketed, as eventually the court will no doubt wish to be satisfied that the selling price was maximized.

The strata council should select an offer to recommend and a non-binding straw poll of the owners should be taken to ensure a very high likelihood of success when the formal vote is taken. Once the purchaser's subject conditions, if any, are removed, a special general meeting of the owners should be convened to pass the necessary resolutions. It is important to note that the vote should not be taken before the deal is firm as the Act requires the owners to almost immediately apply to court to confirm the resolutions – no judge is going to order a wind up if the deal is not firm. And the court process is likely to be very expensive, as each and every owner, mortgagee and other chargeholder must be formally served with extensive court materials.

Depending on many variables including the size of the strata, the degree of opposition to the proposed sale, and the availability of court time, the court process may vary from 60 days to many months. Following the court order, closing will likely follow within 60 to 90 days. In most cases, the purchaser will allow owners to reside in their units as tenants after closing for a negotiated period of time. All in all, it would be surprising to concluded in less than a year, starting with the first informal meeting.

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2017 MARKET OUTLOOK

Pricing	New Listings	Vacancy Rate	Sales	Cap Rates
↗	↔	↔	↘	↘

- Tight supply and more off-market deals will continue to exert upward pricing for well-located quality assets in Vancouver as well as Burnaby and New Westminster
- Purpose-built rental buildings will match or exceed the price-per-square-foot achieved by new strata development in select neighbourhoods
- Capitalization rates remain highly compressed as purchasers increasingly disregard the metric with the goal being capital preservation as opposed to ROI
- Near zero vacancy and elevated housing prices will fuel continued increases in residential rental rates

MULTI-FAMILY TRANSACTIONS (GREATER THAN $10 MILLION) FIRST HALF 2016

PROPERTY	MUNICIPALITY	PRICE	Price Per Door	DATE
Winsome Place 7760 120th Street	Surrey	$10,802,977	$154,328	June 2016
The Berkeley 1770 Davie Street	Vancouver	$43,000,000	$741,379*	June 2016
1033 Granville Street	Vancouver	$10,000,000	$1,250,000*	June 2016
Sharmerob Manor 1929 West 3rd Avenue	Vancouver	$19,800,000	$373,585	May 2016
831-835 Dunsmuir Road	Esquimalt	$17,000,000	$200,000	May 2016
Reid Manor 1875 West 7th Avenue	Vancouver	$13,500,000	$346,154	May 2016
6525, 6559 & 6585 Sussex Avenue	Burnaby	$32,680,000	$518,730	May 2016
2910 Alder Street	Vancouver	$12,400,000	$344,444	May 2016
6556, 6566, 6580 & 6596 Marlborough Avenue	Burnaby	$14,500,000	$322,222	May 2016
The Crest 775 Terminal Ave North	Nanaimo	$20,500,000	$169,421	May 2016
6525 Telford Avenue	Burnaby	$20,888,888	$386,831	April 2016
530 Cottonwood Avenue	Coquitlam	$11,880,000	$565,714	April 2016
1580 Everall Street	White Rock	$10,925,000	$191,667	March 2016
MC2 8101 Nunavut Lane, 488 West 64th Avenue	Vancouver	$26,898,000	$244,527	March 2016
3731 & 3743 West 4th Avenue; 1975 Alma Street	Vancouver	$18,000,000	$486,486	March 2016
Emery Village Apartments 1200-1259 Emery Place	North Vancouver	$39,550,000	$648,361**	March 2016
Silver Star Apartments 6425 Silver Avenue	Burnaby	$14,150,000	$294,792	March 2016
The Josephine & The Westwood 2116 & 2150 West 39th Avenue	Vancouver	$17,500,000	$416,667	March 2016
2105 West 47th Avenue	Vancouver	$14,149,888	$643,177	March 2016
Dorchester 170 East 5th Street	North Vancouver	$16,250,000	$306,604	March 2016
1059 & 1075 Nelson Street	Vancouver	$68,000,000	$1,333,333	March 2016
4971, 4929 & 4909 Imperial Street & 6695 Dunblane Avenue	Burnaby	$28,700,000	$337,647	February 2016
Beverly Manor 1190 West 10th Avenue	Vancouver	$12,000,000	$342,857	February 2016
6366 Cassie Avenue & 6433 Mckay Avenue	Burnaby	$25,750,000	$271,053	February 2016
Warrington Apartments 1485 Davie Street & 1186 Nicola Street	Vancouver	$36,500,000	$715,686	February 2016
Graystone Manor 1750 West 13th Avenue	Vancouver	$18,100,000	$385,106	January 2016
Karin Manor 7230 Elwell Street & **Walker Manor** 6947 Walker Avenue	Burnaby	$12,400,000	$200,000	January 2016
1059 &1075 Nelson Street	Vancouver	$60,000,000	$1,176,471	January 2016
1070-1080 Barclay Street	Vancouver	$59,000,000	$766,234	January 2016
1180 Broughton Street	Vancouver	$11,000,000	$523,810	January 2016
Vallejo Court 1009 West 10th Avenue	Vancouver	$12,850,000	$313,415	January 2016
5868 Olive Avenue	Burnaby	$12,490,000	$265,745	January 2016
Brunswick Apartments 396 East 2nd Avenue	Vancouver	$12,680,000	$239,245	January 2016

Multi-family assets purchased for redevelopment *Mixed-use **Townhouse complex

Sources: Avison Young & RealNet Canada

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Are there particular building characteristics that should be considered when condo owners are debating whether or not to wind up the strata?

The changes to the Act are a recognition that many strata buildings are rapidly nearing the end of their useful lives. The *Strata Property Act* was amended a few years ago to introduce mandatory depreciation reports. These reports have helped crystallize the dire circumstances of many older buildings. The report may set out millions of dollars in required capital expenditures, which many owners will not be able to afford, creating an imminent crisis. At the same time, the report may scare off individual-unit purchasers, lowering the market value of each unit, providing further incentive to wind up.

At the other end of the spectrum are buildings that have been well-maintained, but are located in areas designated for significant upzoning (for example, the West End). In these cases, the building's good condition may work against a wind-up. The court may decide that a windfall for the owners resulting from a high re-development value is not a compelling enough reason to force up to 20% of owners to vacate perfectly good homes against their will. It will be very interesting to see how the first court cases unfold. ■

SNAPSHOT OF BC VACANCY RATES

AREA	OCTOBER 2015*	APRIL 2015	% CHANGE
Vancouver CMA	0.8%	1.4%	-0.6%
Abbotsford CMA	0.8%	3.6%	-2.8%
Chilliwack	2.7%	4.3%	-1.6%
Victoria CMA	0.6%	1.2%	-0.6%
Nanaimo	2.0%	2.9%	-0.9%
Kelowna CMA	0.7%	1.9%	-1.2%

Source: CMHC; CMA: census metropolitan area
**Most up-to-date vacancy provided by CMHC; new figures expected in late fall 2016*

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