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# Investing in raw land

**For investors with a mind to diversify their portfolios, investing in raw land might just be the answer. Here's how to make a big profit**

*By Peter Mitham*

**R**ed Water, Alta. isn't the sort of place that pops up first on most investors' radars. Tucked away in Sturgeon County about a half-hour's drive north of Edmonton, the community of 1,500 is set in the middle of farmland.

But the town boomed after oil was discovered here in 1948, a scenario that's repeating itself as multi-national energy company Northwest Upgrading Inc. develops a \$1.6-billion bitumen upgrader as part of the booming Northern Alberta tar sands action. The project is bringing 2,000 people to Red Water.

"Where are these people going to live?" asks Vaughan Minor, president and CFO with Burlington, Ont.-based Edgeworth Properties Inc., which saw an opportunity in the influx and has acquired three parcels in the area.

Edgeworth plans to add value to the undeveloped parcels through residential development, with a commercial component thrown in to serve the needs of workers. The new development will boost the value of the properties in a region with significant long-term potential.

Edgeworth's strategy reflects the typical strategy of those who invest in land. A nice piece of land may have recreational value in itself or be a source of natural resources, but the real value comes from development. It's why the biggest land rushes in history are usually triggered by demand for properties that are likely to be in short supply as communities grow.

"We look for land that's in the path of development," Minor explains.

While there's some value in subdividing, servicing and selling property to others to develop, Minor said Edgeworth typically seeks well-located properties with development potential. A quarter-section (160 acres) of land is an ideal investment in Alberta because it is typically bounded by four roads, which provide access, and can be divided up as demand allows. Smaller parcels are possible in urban areas, where land often has to be subdivided eventually.

Edgeworth currently has about 15 properties comprising approximately 1,500 acres, in locations ranging from

Edmonton to Red Water, Lacombe to Fort McMurray.

"Long term, land will always go up in value. There are dips, as we saw in the last 18 months or so, but when things get straightened around it always goes up in value," Minor says.

### Financing and the state of the market

The one challenge, especially in the current environment, is financing because raw land doesn't yield cash flow. It's raw, after all – there's nothing on it adding value or generating income. The constriction of financing following the roiling of financial

where some of the opportunities lie.

The value of land sales last year versus 2008 dropped 28 per cent in Toronto, 37 per cent in Vancouver and 63 per cent in Calgary. Collectively, the country's five major centres saw \$5.2 billion in land sales in excess of \$1 million in 2008, and less than half that last year.

But through 2009, the Edmonton and Montreal markets, which posted year-over-year declines of 78 per cent and 64 per cent, respectively, saw transaction values increase 96 per cent and seven per cent between the first and second halves of 2009. The markets were the only two in Canada to strengthen last year.

A variety of factors drove the activity,

### Financing tips

The credit crunch may be easing but lenders remain wary of financing large real estate investments unless there's a demonstrable prospect of payback. Tips to get lenders onboard include:

- **Be willing to make a greater down payment.** Being able to count on a mix of investors before you ask the bank for money may boost your chances of securing financing. While top-grade projects are still desirable, projects with greater risk demand that you show you're able to do your part to carry the investment.
- **Cultivate cash flow.** Some land investments may be prime grazing land for farmers, or include woodlots that will generate income from timber sales. Consider what your property offers beyond development opportunities. The cash flow may boost lenders' confidence that you'll be able to service the debt you're taking on to buy the site.
- **Have an exit strategy.** Raw land isn't a passive investment; having a business plan will help keep you on track, and may help satisfy lenders' questions about how you're going to finance the purchase (and repay them).

markets in late 2008 put brakes on investment and development activity, effectively shutting down land markets on two fronts.

Buying properties that didn't have cash flow was virtually impossible in an environment where lenders wanted guarantees of repayment, while adding value to land and selling it off became difficult as development ground to a halt. Signs of recovery have reappeared only recently, and then only in select markets where lenders have seen a return of equity and loosened their purse strings.

A glance at figures from [Avison Young](#) (Canada) Inc. shows just how severe the downturn remains, and

including access to financing, access to product and greater business confidence by players such as Edgeworth, which recently closed a deal on Edmonton's south side for a 116-acre property. Stimulus financing played a role in Montreal where governments have been keen to kick-start economic activity.

"There's a lot more government assistance for companies moving into the marketplace than there is in Ontario," observes [Peter De Guerre](#), senior vice-president and an investment land specialist in Avison Young's Toronto office.

The funding has stimulated land purchases, buoying the Montreal market despite broader circumstances.

## Where can you buy the best land investment?

Vancouver, Edmonton and Toronto may be among the best metropolitan areas for raw land investment, but they all have common traits shared with smaller pockets in Quebec and Atlantic Canada:

- ➔ **They're developable.** Tracts ideal for land investors are typically in the path of development, meaning they'll be suitable for development in the near future, or are ripe for rezoning and subdivision for sale to developers.
- ➔ **They're desirable.** Real estate may be all about location, and that's especially true of raw land. Well-developed metropolitan areas are often short on new sites for development, meaning investors with sites ready to go and next to amenities such as transportation corridors or retail and service hubs (in the case of residential sites) stand to see a good return on their investment through development or sale to developers.
- ➔ **They're financeable.** Being able to demonstrate a viable exit strategy from the property is important in convincing lenders that the site is worth financing. Some jurisdictions offer incentives and financing to assist investors and developers with land purchases, so investigate what options are available in the area where you're looking.

### Where to buy

Resource-rich regions have also done well, he says, pointing to figures for the Edmonton market but also noting the demand for property in Atlantic Canada. Newfoundland, Nova Scotia and New Brunswick all have energy projects on the go that are fuelling demand for housing, and in St. John's, commercial space. Owners with land to offer developers are sitting pretty here, despite the slow recovery.

Residential sites are key opportunities in most markets as the recovery gathers steam, however. While developers may be working through sites accumulated prior to the correction of 2008, De Guerre says residential is a known quantity for most investors. The returns are less variable than with other forms of development, boosting confidence in the outcome.

"Residential is cookie-cutter. You know you're going to get your nine per cent, 10 per cent return," he says.

Throw in appreciation in land values and the return to investors could be significant.

He points to development sites in Brampton that sold for \$500,000 an acre a few years ago that are now worth more than \$1 million an acre. The strength is driven by the lack of suitable development sites, and the definite margins reassure investors in a turbulent market.

"Serviced lots are at their all-time low," he says. "So the indicators that I'm seeing are that land values are holding firm or going up, availability is going down. There's still 150,000 new residents coming to Ontario every year."

Still, De Guerre encourages land investors to consider other opportunities for adding value. Greater risk stands to

bring greater reward, and he points to moves by some of the continent's bigger players as an indicators of what's possible.

Developers are looking for major shopping centre sites and institutional development opportunities, for example. He points to a pending deal for 86 acres at the regional airport in Buttonville, for example, which a well-known retail developer is eyeing for a shopping complex. Similarly, Pitt Meadows Regional Airport in British Columbia recently sold a portion of its acreage for industrial development.

"[Residential] is something you know going in the door what your likely profit is going to be when you finish the project," De Guerre says. "Yet I don't think there's the upside that a lot of people are looking for. The significant lift that you get when you buy something and look at it as an investment."

### National land investment activity

Market	First Half 2009	Second Half 2009	\$ Change	% Change	Total 2009	% of Total	Total 2008
Vancouver	\$347,925,970	\$301,648,757	-\$46,277,213	-13%	\$649,574,727	25%	\$1,026,150,076
Edmonton	\$70,381,165	\$137,918,635	\$67,537,470	96%	\$208,299,800	8%	\$945,102,982
Calgary	\$222,029,219	\$156,479,314	-\$65,549,905	-30%	\$378,508,533	15%	\$1,009,446,592
Toronto	\$493,685,008	\$481,550,198	-\$12,134,810	-2%	\$975,235,206	38%	\$1,361,784,571
Ottawa	\$55,948,650	\$26,264,640	-\$29,684,010	-53%	\$82,213,290	3%	\$97,402,293
Montreal	\$133,103,394	\$142,099,105	\$8,995,711	7%	\$275,202,499	11%	\$769,806,878
Total	\$1,323,073,406	\$1,245,960,649	-\$77,112,757	-6%	\$2,569,034,055	100%	\$5,209,693,392

Source: Avison Young, RealNet Canada's databases

## Demand spurs investment

### Deals out West

Yet a market such as B.C. reflects the best and worst of current land investment prospects.

While the Olympics have added lustre to the generally rosy glow that surrounds Western Canada's resource-oriented economy, a lack of land close to urban centres has limited investment while outlying areas continue to reel from the effects of the recession.

The circumstances present challenges and opportunities for investors.

Some investors have been able to snap up parcels from distressed developers who weren't able to weather the financial storm (some resorts have been offering lots at 50 per cent discounts in order to move them). Others took advantage of the downturn to reposition properties in anticipation of better times, knowing that a dip in markets such as the Lower Mainland was likely to be brief.

"While the marketplace is really,

Noah Rechtsman, an investment sales specialist in the Toronto office of Cushman & Wakefield LePage, believes a number of factors are buoying the land investment market this spring. These include:

- ➔ **HST.** British Columbia and Ontario will adopt a 13 per cent harmonized federal and provincial sales tax on July 1, 2010. While exemptions are in place for properties priced below a certain threshold, uncertainty over the impact of the tax is widely believed to be shifting some sales forward. In turn, developers are factoring it into land purchase decisions now.
- ➔ **Rising interest rates.** "It is widely believed that interest rates will increase over the next few years and as such, it is viewed as a motivator for consumers to buy homes now," Rechtsman says. The activity is drawing inventory through the development pipeline and giving developers the cash needed to buy fresh sites.
- ➔ **Attractive pricing.** Downward pressure on pricing after September 2007 has pushed land prices to levels that are far more appealing than they were two years ago. "Pricing is competitive, especially within established areas," Rechtsman says.
- ➔ **Low inventories.** Strong demand has left developers with few sites to develop, prompting them to seek new opportunities. "Many developers are now finding themselves in a scenario with low inventory of homes to sell and/or lots to build on," Rechtsman says. "Within the [Greater Toronto Area], land that has been designated for residential development is viewed as a valuable commodity."

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really strong in the cities, rural B.C. is definitely a buyers' market with good deals all over the place," says Rich Osborne, president of Landquest Realty Corp. in New Westminster. A veteran of the recreational property and B.C. land market with four decades of experience, Osborne's optimism is clear: "It's a super-good time to be buying."

Raw land runs from \$1,000 an acre for larger acreages in the province's interior up to \$100,000 an acre for smaller acreages in Fraser Valley communities such as South Surrey just east of Vancouver.

He points to a property on Tyaughton Lake north of Whistler as an example of the deals available.

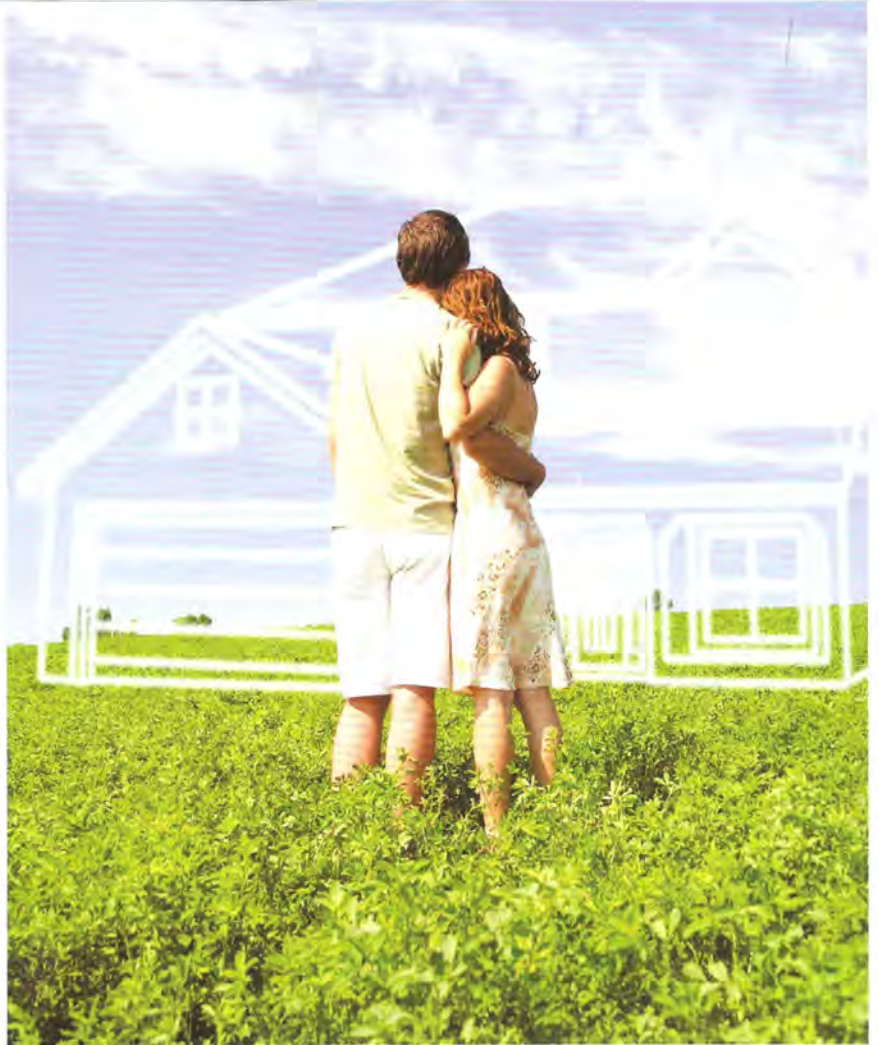
The two-acre property was originally listed at \$299,000 in 2008 and quickly attracted an offer. But the deal didn't complete and successive price reductions as the market turned failed to draw buyers. The owners eventually found a buyer in November 2009 who paid \$187,000, or \$93,500 an acre for the land.

The drop in value reflects the less frenetic pace of the market and virtual absence of speculation, which remains tipped in buyers' favour. Osborne says it also shows signs of increasing exit opportunities as the forest sector strengthens; properties that might have been eyed strictly for recreational development a short time ago are seeing renewed interest for timber harvesting.

"This kind of market we're in is for people wanting to buy long term and people who actually want to have a piece of land for various purposes and can see the opportunity," Osborne says.

And it's the opportunities Canada offers that attract the investors Edgeworth has attracted. About half of its 4,000 investors are located overseas, primarily Asia where the company has eight offices. Asian investors like Canada, and are particularly bullish about Alberta because of its abundance of raw land and the shine of the resource sector. Also, they're looking for safety.

"They do their homework, but they love land, they love oil, they love Canada – and specifically Alberta," Minor says. "On top of that we've got the best banking system in the world, so that just does nothing but help us." 🏠



### What to look out for when buying raw land

The land may be undeveloped but that doesn't mean your investment approach should be. The due diligence required will be just as great – if not greater – than a property with improvements, as you'll want to take the future prospects of the site into account. Short of hiring a development consultant, there are a few points a small investor can take into account when considering purchasing raw land:

- ➔ **Remediation requirements.** Site ecology is an important consideration as site contamination or potential restrictions on property use thanks to watercourses may pose obstacles to future development.
- ➔ **Rental arrangements.** Raw land is typically undeveloped, but a site leased for grazing purposes or other agricultural uses may demand that you factor the tenant's needs into your own development schedule. Alternatively, income from the tenant may cover some of your holding expenses while you draft development plans.
- ➔ **Holding costs.** Raw land will typically incur carrying costs, such as property taxes and other charges that won't. Accounting for these costs within your investment strategy may determine whether you're able to hold the property for the long term or if it's necessary to prepare the property for development immediately upon purchase.
- ➔ **Zoning and servicing.** Requirements of the local municipality may limit land uses, or stipulate servicing requirements on the part of users. Proximity to services will enhance a parcel's value, facilitating the addition of value through development. Changing the zoning or subdividing may be another means of adding value.