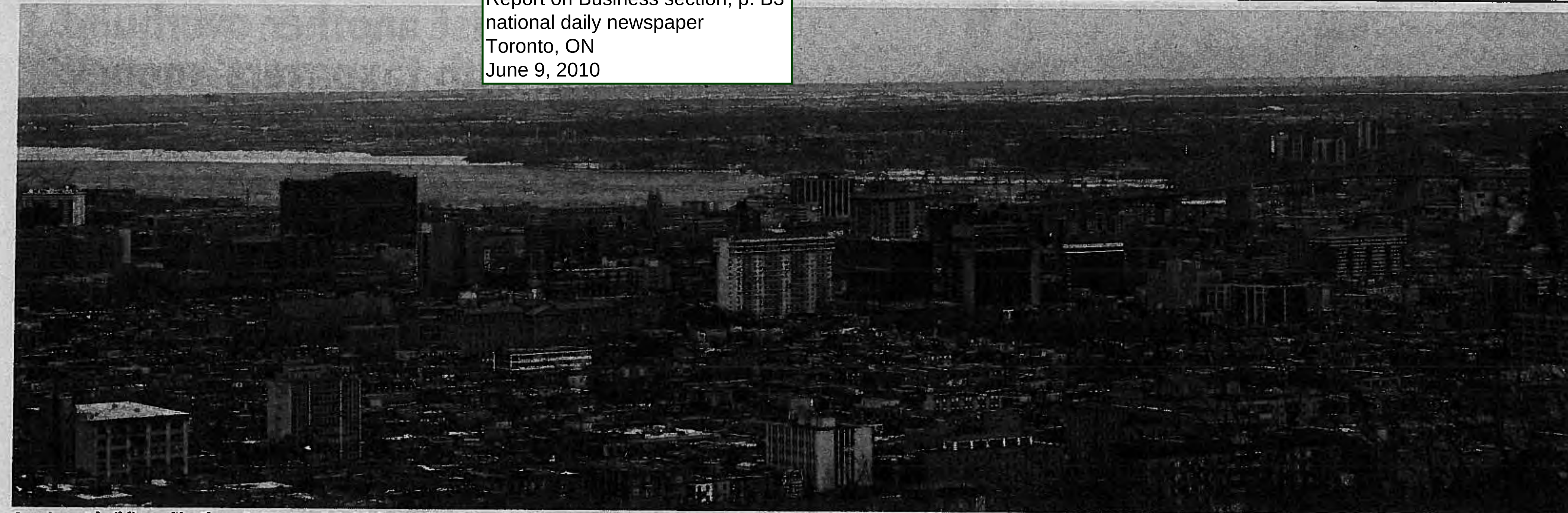
REAL ESTATE

The Globe and Mail
Report on Business section, p. B3
national daily newspaper
Toronto, ON
June 9, 2010



Apartment buildings, like these in Montreal, held their value through the recession because there were no distress sales; owners could refinance their debt inexpensively through CMHC. LEE BROWN/THE CANADIAN PRESS

Apartment buildings: slow, steady and sizzling hot

Low mortgage rates have made income-generating properties some of the most desirable real estate available in Canada

BY STEVE LADURANTAYE
REAL ESTATE REPORTER

For a few days in May, two near-identical apartment buildings in Cambridge, Ont., were among the hottest commercial properties in Canada.

With their sand-coloured brick and metal-panelled balconies they weren't particularly awe-inspiring pieces of real estate. But they had owners who were willing to sell for $46.7-million to the right buyer, making them a rarity in a sector that has seen a flurry of expensive deals as deep-pocketed real estate investment trusts scramble to snap up what little inventory is available.

Apartment buildings – there are about 100,000 of them across Canada, with the majority of them clustered along the Windsor-Quebec City corridor – may not return as much to their investors as shopping centres or office buildings, but they offer a lower-risk way to own income-generating properties.

They held their value through the recession for one main reason – there were no distress sales because owners could refinance their debt inexpensively through Canada Mortgage and Housing Corp. This ensured them access to credit at a time when other property owners found debt markets completely closed.

And with mortgage rates almost certain to move higher in coming months, buyers are scrambling to make purchases while rates sit near all-time lows. RealNet Canada, which tracks sales, shows first-quarter sales volumes actually decreased in most of the country at a time when other commercial sectors were showing sharp signs of recovery.

It has nothing to do with a lack of confidence in the sector, but rather illustrates how reluctant sellers are to part with their income-generating properties.

"What's happening is people who own them are quite happy and those who want to buy really have to spend a bit more than they may like," said RealNet president George Carras. "The most dominant owner profile in the sector is the private investors, and they tend not to want to trade."

> **"You can get money at ridiculously low rates and the big challenge is just finding quality product. There is no low-balling, and when something comes around, you see a ton of interest.**
>
> Rob Greer, Vancouver principal at Avison Young

Avison Young's Vancouver principal Rob Greer said REITs are compelled to pay whatever the private owners ask, lest they face higher financing costs later in the year for comparable properties.

It's a story similar to the one that has driven record price gains in the residential housing market. Except rather than families looking for new homes, the players are giant REITs who have raised billions of dollars of capital over the last year and are anxious to put that money to work.

They are finding reluctant sellers in the country's pension funds and private owners, who aren't likely to sell unless they get an attractive offer.

"You can get money at ridiculously low rates and the big challenge is just finding quality product," Mr. Greer said. "There is no low-balling, and when something comes around, you see a ton of interest."

Halifax-based Killam Properties started the year with a goal to spend up to $150-million on Ontario apartment buildings, and passed the $100-million threshold with the Cambridge deal earlier this week.

Chief executive officer Philip Fraser said it has become increasingly difficult to find relatively new buildings that met the company's criteria, and indeed there were never any "for sale" signs planted on the front lawn in Cambridge.

Rather, Killam's representatives knocked on doors around the province until it found an owner willing to take its money. It took over a 20-year, $10.1-million mortgage at 5.15 per cent, and took on an additional mortgage for $16-million at 4.5 per cent. It paid the rest in cash.

"The buildings in our portfolio are meant to keep their value over the long-term," he said. "Whether we bought them 10, 20 or 40 years ago the trend is that they increase over time. It's slow and it's steady, but that is the way this works."

Derek Lobo of Rock Apartment Advisors, which represents buyers who are interested in acquiring apartment buildings, said the owners who are selling are typically looking to reposition their portfolios into other asset classes.

"I call it dumping your dogs," he said. "Now is the time for them to unload buildings that don't make sense for them, because there are too many buyers and just not enough product."

Sam Kolias has another name for it – rebalancing his portfolio of properties. The chief executive officer of Calgary-based Boardwalk REIT has taken advantage of buyer interest by selling geographically isolated properties and then using the money to buy his own company's units, which he believes to be undervalued.

"The lesson some investors learned through the recession is that this is a great industry which is very stable," he said. "We miss the peaks, but we also haven't seen the valleys. That's what people are noticing now – how steady this asset class can be."