The Newsletter for Apartment Owners since 1983

Issue 52 | January 2015

Goodman report:

2014 Greater Vancouver Rental Apartment Review

In this issue:

View properties online at www.goodmanreport.com

Oil crash: The impact on you

As you're all aware, the price of crude oil has fallen from a recent high of US $105 to around US $47 a barrel, the lowest since 2009. Oil is a commodity, and as its supply increases, its price decreases. For the most part, the new prices fall well below the costs of production, and this will have ramifications for regions both oil-producing and not, with the latter benefitting more. We have already seen an uptick in Ontario's manufacturing-based economy because of the fall in the Canadian dollar, which is directly related to the fall in oil prices.

Consider what this means for our economy overall. There's no question that Alberta's energy sector will see a significant reduction in jobs, especially in the North. Oil sands projects, which are capital-intense, have already seen cancellations and exploration cutbacks by major players; unquestionably, more will come, with corresponding decreases in jobs and impact on provincial revenue. Many of the new proposed megaprojects, such as the Northern Gateway pipeline and even the twinning of Kinder Morgan's Trans Mountain pipeline, may have to be postponed, not only because of environmental concerns and First Nations challenges, but because of the sheer economics of the oil industry. British Columbia's LNG projects are probably safe for now; however, in a world of uncertainty, no one has a crystal ball.

What does all this have to do with apartment buildings in Vancouver? On the surface, probably very little. We can find no direct correlation between the price of crude and the values of apartment properties. Scratching the surface, however, could help shed light on the possible effects of these trends on you. The uncertainty lies in what will happen to interest rates: in our view, the single most important variable with which to concern yourself. We know that housing prices and apartment values are directly related; you could say they're the same melodies, just with different lyrics. If housing prices fall, could apartment values be far behind? We're not suggesting a collapse, but let's not discount the possibility of a housing correction.

> "Another factor is that there has been a lot of private money chasing very few properties, driving cap rates down to the unprecedented lows we're presently experiencing."

Whither cap rates?

Since the early 2000s, cap rates have fallen from 5–6% to their current 3–4%. Why? A leading factor has been demand from offshore and institutional buyers, within a low interest-rate environment in which the investor has been able buy and finance at less than the cap rate paid, thereby attaining positive or at least break-even cash flow, regardless of the level of financing. Another factor is that there has been a lot of private money chasing very few properties, driving cap rates down to the unprecedented lows we're presently experiencing. These lows aren't unique to the Greater Vancouver area: demand for assets is similarly driving cap rates down in most metropolitan markets in North America.

> "If housing prices fall, could apartment values be far behind?"

Banks, trust companies and private lenders have been falling over one another to finance properties over the last few years, especially if a buyer pursues CMHC insurance, which lowers borrowing costs even further. This demand for assets has become intense, with no signs of abatement; we're still in a very active liquid market marked by historically low vacancy rates, perceived low investment risk and a growing acceptance that renting is a reasonable alternative to owning.

> "Deflation is a word we seldom hear."

Deflation is a word we seldom hear. Certainly Canada has not experienced deflation of any significance since the Great Depression. On January 21st, 2015, in a move few would have predicted, the Bank of Canada announced a loosening of their monetary policy with a cut in the overnight key rate to 0.75%. According to Andrew Barr of the *National Post* on January 21st, 2015, "This decision is in response to the recent sharp drop in oil prices which will be negative for growth and underlying inflation for Canada."

If Canada should enter into a deflationary mode, rental apartment buildings will not be immune from its impact.

On the brighter side, the low cost of energy is driving consumer spending. By some estimates, multi-billions of dollars formerly paid in higher gas prices at the pump are suddenly being spent on consumer goods. Ontario's manufacturing-based economy is taking off. Initially, this spending spike, along with increasing consumer debt, had many experts suggesting the Bank of Canada would increase interest rates. Quite the opposite has occurred. However, if the Bank of Canada perceives the need to slow down the economy fuelled by rising consumer spending and escalating home prices, look for increasing rates in late 2015 or early 2016.

Considering all these factors, how should we interpret the mix? It's our view that once interest rates finally increase (and they will increase), the value of apartment buildings might level off or slightly decline. The biggest risk to all owners is a reduction in consumer confidence driven by rising unemployment and general uncertainty. Many suggest consumer confidence often falls from threats (real or perceived) to their own pocketbook. Often these threats are intensified by headlines. If the overall economy starts to contract, we will see a general decline across the board. Uncertainty and consumer confidence could lower demand from foreign investors and institutional buyers, as money usually flows to safety, not volatility. If purchasers still view B.C. as a long-term safe haven, then your asset should hold its value; however, any increase in interest rates down the road will have an impact as a correlation exists between interest rates and cap rates, albeit not a linear one. For example, let's assume that interest rates increase by 1% and that increases to cap rates are only 30% correlated. Thus a 3% cap rate would become a 3.3% cap rate, and a building formerly worth $5 million would drop perhaps to $4.5 million.

Concerned? Perhaps now's the time to list your asset. It's our experience that when demand slows down, it's generally too late to achieve top dollar. Remember: the market isn't arbitrary. It never lies and currently is very strong.

Why list with the Goodman team

We sell both large and small apartment complexes and have been doing so successfully since 1983. Every client is on our A-list. Our database reaches world-wide, and we challenge anyone else in this industry to match our marketing strengths. Our new website and your listing will reach 50,000 potential buyers.

Our team doesn't buy listings, but over the years, we've shown remarkably consistent accuracy in predicting selling prices, both for our own listings and for those of other agents. We strive to provide you with excellent service, value and expertise.

If you're considering a sale, contact us, visit our office and let us show you how we can help. We're happy to hear from you at any time. Call us at 604-899-1122 or email David Goodman at david@goodmanreport.com or Mark Goodman at mark@goodmanreport.com.

Year-to-year comparison: The story behind the stats

The 2014 numbers are in. At year-end, we find the category of building sales at its highest level since 2007, while total dollar volumes have also registered significant gains over 2013. One of the key barometers, the average price per suite, has shown mixed results. Nevertheless, unrelenting demand for rental apartment investment has continued throughout the year.

In Greater Vancouver, a total of 123 rental buildings changed hands in 2014, up 31% from the 94 sold in 2013. It is interesting that 31 of these 123, comprising approximately 700 rental suites, have been or are slated to be demolished. Most of the buildings to be taken down are two to three-storey wood-frame buildings about 55 years old that had or have clearly reached the end of their economic lives.

The great majority of these types of transactions have been occurring in Burnaby's Metrotown area now that council has significantly amended the local Official Community Plan. The demolished structures will be replaced with several thousand new highrise condominiums, to be purchased both by owner-occupiers and by investors. From the current investor-buying activity, we estimate that virtually all of the demolished suites will be replaced by investor-purchased units going back into the rental pool. An unprecedented 23 rental buildings sold in Metrotown in 2014, 14 of which will be demolished to make way for new market housing with average suite prices of $272,000, up 6% from 2013's figure of $257,000. (Note that the "price per suite" in Metrotown can be misleading as redevelopment of the land is defined as the "highest and best use.") Unlike Vancouver, Burnaby provides an example of free-market forces allowing for the unrestricted demolition of rental apartment buildings, and ironically this in an NDP stronghold!

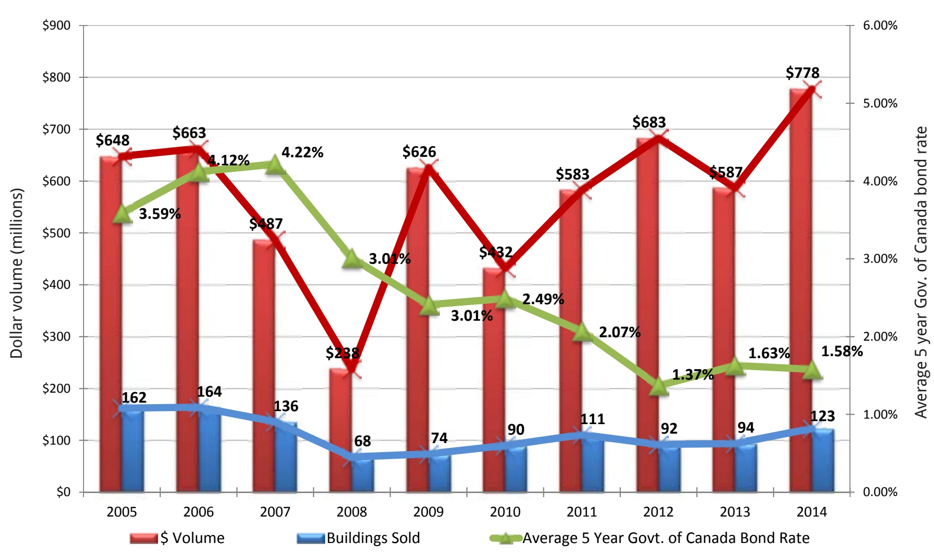
Vancouver itself recorded 62 sales, up modestly from the 54 figure of 2013, while the suburbs experienced a major increase also to 61, up 53% as compared to 2013's less buoyant 40. More specifically, amongst Vancouver neighbourhood transactions, the Eastside has held steady at 14 sales in 2014 versus 15 in 2013, as has Kitsilano at 9 sales, up slightly from the 8 recorded a year earlier. South Granville declined to 10 sales versus 11 in 2013, while Kerrisdale soared to 10 compared to just 3 in 2013. Marpole showed no change at seven while the West End at 11 sales was up marginally from last year's 10.

Total dollar volumes for Greater Vancouver increased to a record-breaking $778 million as compared to $587 million in 2013, up 33%. Vancouver, however, countered the trend with volume dropping to $342 million, an 11% decrease over 2013's figure of $385 million, whereas suburban dollar volume soared to $436 million, also a record high and representing a whopping 116% increase over 2013's $202 million.

2014's average price per suite for Greater Vancouver advanced 3% to $237,000, from $230,000 in 2013. Vancouver average prices, in fact, increased to $298,000, up 14% over 2013's figure of $262,000, whereas the suburban figure was 10% higher at $204,000 compared to 2013's $186,000.

When we analyze overall performance in terms of average price per suite in Vancouver's seven distinct communities for 2014 versus 2013, we receive contradictory messages. On the positive side, Kerrisdale average values hit an all-time high of $443,000 per suite, up 12% over 2013's $394,000, driven primarily by several sales of co-op and rental properties (the buildings were resting on C-2 zoned land purchased solely for redevelopment). The Eastside also served up a dramatic increase in average pricing, climbing 25% to $207,000 in 2014 as compared to

Greater Vancouver 10-year multi-family performance



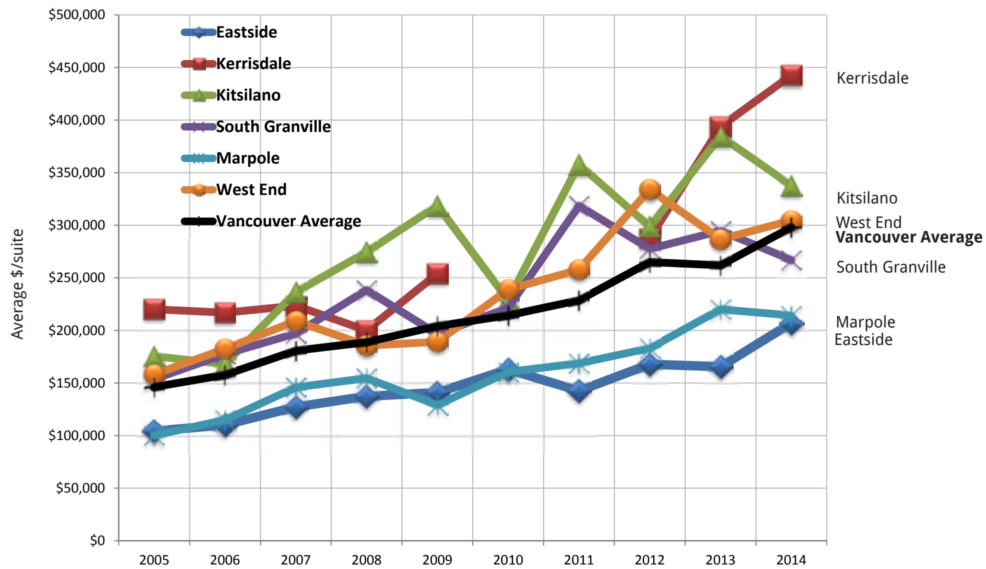
Source: Goodman Report

$166,000 in 2013. Playing catch-up in their attraction to the Eastside, investors are finally recognizing that rents and asset values there have lagged well behind Westside pricing. A third area to register an increase was the West End, where average prices climbed to $304,000 per unit, up 6% over 2013's $287,000. By contrast, Kitsilano, Marpole and South Granville, despite strong activity, bucked the trend with average price decreases of 3–12% (see Activity highlights, page 6). It should be noted that in 2013, two rare sales in UBC, included in Kitsilano averages ($1,082,000 and $407,000 per unit), artificially boosted the numbers. For this newsletter and moving forward, the *Goodman Report* will create a distinct category for University Endowment Land transactions.

Meanwhile, in suburbs other than Burnaby, New Westminster registered a meager 1% increase to $131,000 in 2014, from 2013's figure of $130,000. Even North Vancouver's strong performance with 15 buildings sold showed a 6% drop in average prices to $240,000 from $256,000 for the previous year. It's worth noting that North Vancouver's elevated averages in 2013 were skewed somewhat by our sale of 3701 – 3817 Princess Avenue, a 57-unit, 9.5-acre, recently renovated luxury townhouse project, for $24.15 million ($424,000 per unit). The remaining areas of Langley, Surrey, Maple Ridge, White Rock, Coquitlam, Port Coquitlam, Mission, Port Moody, West Vancouver and Delta had a sprinkling of sales (see Apartment building sales, page 7).

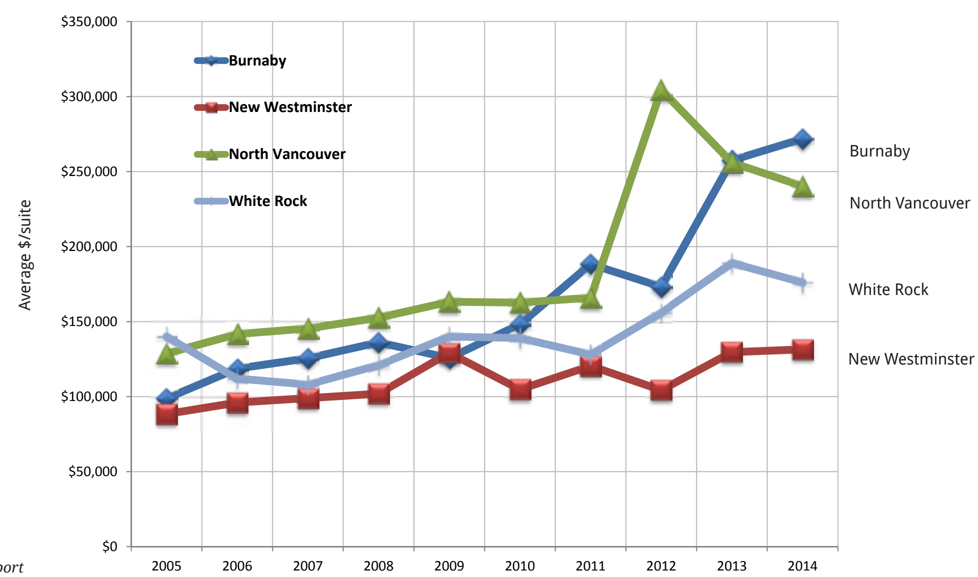
Vancouver neighbourhoods 2005–2014

Average price per suite



Suburban neighbourhoods 2005–2014

Average price per suite



Source: Goodman Report

Activity highlights | 2014 compared to 2013

Building transactions

Area	2014 Buildings sold	2013 Buildings sold	% change	2014 Suites sold	2013 Suites sold	% change
Vancouver	↑ 62	54	+ 15%	↓ 1,147	1,472	- 22%
Suburban	↑ 61	40	+ 53%	↑ 2,135	1,084	+ 97%
Totals	↑ **123**	**94**	**+ 31%**	↑ **3,282**	**2,556**	**+ 28%**

Dollar volumes

Area	2014	2013	% change
Vancouver	↓ $341,832,000	$385,491,984	- 11%
Suburban	↑ $436,084,500	$201,601,500	+ 116%
Totals	↑ **$777,916,500**	**$587,093,484**	**+ 33%**

Average price per suite

Area	2014	2013	% change
Vancouver	↑ $298,023	$261,883	+ 14%
Suburban	↑ $204,255	$185,979	+ 10%
Totals	↑ **$237,025**	**$229,692**	**+ 3%**

Neighbourhood transactions / average price per suite

Vancouver areas	2014 transactions	2013 transactions	$ per suite (2014)	$ per suite (2013)	% change
Eastside	↓ 14	15	↑ $206,930	$165,507	+ 25%
Kerrisdale	↑ 10	3	↑ $442,588	$393,828	+ 12%
Kitsilano	↑ 9	8	↓ $337,803	$384,685	- 12%
Marpole	— 7	7	↓ $214,250	$220,044	- 3%
South Granville	↓ 10	11	↓ $267,186	$294,697	- 9%
West End	↑ 11	10	↑ $304,489	$286,687	+ 6%
Suburban areas	**2014 transactions**	**2013 transactions**	**$ per suite (2014)**	**$ per suite (2013)**	**% change**
Burnaby	↑ 23	15	↑ $271,808	$257,496	+ 6%
Langley	↑ 3	2	↓ $95,779	$116,146	- 18%
Surrey	↑ 3	2	↑ $159,934	$97,500	+ 64%
New Westminster	— 8	8	↑ $131,458	$129,582	+ 1%
North Vancouver	↑ 15	7	↓ $240,270	$255,906	- 6%
White Rock	↑ 3	2	↓ $176,188	$189,259	- 7%

Building size, midrise/highrise, sales over $10 million

Type	2014	2013
Size (over 50 units)	8 of 123 sales (7%)	13 of 94 sales (14%)
Midrise/highrise	6 of 123 sales (5%)	8 of 94 sales (9%)
Over $10 million	13 of 123 sales (11%)	17 of 94 sales (18%)

Apartment building sales | Greater Vancouver | January 1st to December 31st, 2014

Vancouver (Eastside)

Address	Suites	Price ($)	$/Unit
* 242 E. 14th Ave	20	4,420,000	221,000
609-619 Heatley Ave	19	3,700,000	194,737
** 7350 Fraser (DS)	22	6,500,000	295,455
2035 Pandora	7	1,380,000	197,143
* 2038 Pandora	6	1,200,000	200,000
555 E. 6th Ave	45	8,880,000	197,333
944 E. 8th Ave	6	1,250,000	208,333
5017 Main	8	1,980,000	247,500
677 E. 7th Ave	42	8,087,500	192,560
1916 E. 5th Ave	7	1,635,000	233,571
* 7915 Knight	12	1,820,000	151,667
1404 E. 21st Ave (TH)	9	2,760,000	306,667
2345 Dundas	47	8,120,000	172,766
Total	**250**	**$51,732,500**	**206,930**

Vancouver (Kerrisdale)

Address	Suites	Price ($)	$/Unit
* 6455 W. Boulevard (DS; SP)	18	9,000,000	500,000
6415 W. Boulevard (DS)	20	8,100,000	405,000
6367 W. Boulevard (DS)	22	11,000,000	500,000
2109 W. 48th Ave (DS)	11	4,400,000	400,000
5926 Yew	14	4,500,000	321,429
2182 W. 39th Ave	21	6,873,500	327,310
* 6356 E. Boulevard (DS)	11	4,710,000	428,182
* 6344 E. Boulevard (DS)	10	5,075,000	507,500
6020 E. Boulevard (DS) 6040 E. Boulevard (DS)	27	14,500,000	537,037
Total	**154**	**$68,158,500**	**$442,588**

Vancouver (Kitsilano)

Address	Suites	Price ($)	$/Unit
2200 Vine (MU)	6	2,000,000	333,333
1855 W. 2nd Ave	36	8,640,000	240,000
* 2358 York Ave	11	3,938,000	358,000
2358 Cornwall	8	5,025,000	628,125
2280 Vine St	18	5,150,000	286,111
* 2174 York	11	3,800,000	345,455
2394 Cornwall	20	8,500,000	425,000
2150 W. 1st Ave	10	3,050,000	305,000
2847 W. 4th Ave (DS)	12	4,487,000	373,917
Total	**132**	**$44,590,000**	**$337,803**

Vancouver (Marpole)

Address	Suites	Price ($)	$/Unit
1425 W. 70th Ave	6	1,200,000	200,000
1125-1157 W. 71st Ave	19	3,998,000	210,421
1235 W. 70th Ave	9	2,300,000	255,556
8666 Laurel	8	1,570,000	196,250
8616 Fremlin	8	1,782,000	222,750
8656 French	10	2,005,000	200,500
Total	**60**	**$12,855,000**	**$214,250**

Vancouver (S Granville)

Address	Suites	Price ($)	$/Unit
* 2930 Cambie	14	3,070,000	219,286
2880 Fir	8	2,600,000	325,000
1009 W. 10th Ave	41	11,000,000	268,293
1676 W. 10th Ave	11	2,800,000	254,545
1225 W. 13th Ave	14	3,850,000	275,000
1546 W. 12th Ave	12	4,100,000	341,667
1395 W. 12th Ave	20	4,700,000	235,000
1396 W. 11th Ave	20	4,350,000	217,500
1338 W. 10th Ave	10	3,200,000	320,000
2525 Birch St	17	4,950,000	291,176
Total	**167**	**$44,620,000**	**$267,186**

Vancouver (West End)

Address	Suites	Price ($)	$/Unit
1540 Burnaby	22	6,300,000	286,364
1075 Nelson (DS)	23	9,000,000	391,304
* 1325 Pendrell St	21	5,175,000	246,429
1168 Pendrell St	23	5,890,000	256,087
1137 Bute St	33	8,100,000	245,455
1444 Alberni (DS) (HR)	129	40,000,000 (EST)	310,078
1104 Haro (DS)	19	7,275,000	382,895
950 Jervis (HR)	41	14,083,000	343,488
1133 Barclay	31	9,225,000	297,581
1235 Burnaby	10	3,240,000	324,000
1275 Comox	24	6,200,000	258,333
Total	**376**	**$114,488,000**	**$304,489**

Vancouver (UBC)

Address	Suites	Price ($)	$/Unit
5555 Toronto Rd (TH) (DS)	**8**	**$5,388,000**	**$673,500**

* Sold by The Goodman Team

** *December 2013 sales.*

Burnaby

Address	Suites	Price ($)	$/Unit
6018 Wilson (DS)	21	9,350,000	445,238
4250 Maywood	18	3,450,000	191,667
6377 McKay (DS)	7	2,200,000	314,286
7110 Linden	30	4,700,000	156,667
4505 Grange	30	5,835,000	194,500
6616 Nelson (DS)	23	6,200,000	269,565
6635 Dunblane (DS)	38	10,500,000	276,316
6779 Sussex	9	2,115,000	235,000
5900 Olive (DS)	71	25,500,000 (EST)	359,155
4325 Maywood	16	3,500,000	218,750
4960 Sanders (HR) 5050 Sanders (HR)	206	54,000,000 (EST)	262,136
6363 McKay (DS)	7	2,300,000	328,571
4929 Imperial (DS)	10	2,314,000	231,400
6425 Silver (DS)	48	10,400,000	216,667
4971 Imperial (DS)	29	6,875,000	237,069
6695 Dunblane (DS)	38	9,360,000	246,316
4909 Imperial (DS)	8	2,956,500	369,563
6844 Balmoral	6	1,800,000	300,000
6832 Balmoral	6	1,800,000	300,000
** 6592 Dunblane (DS)	9	3,200,000	355,556
** 6650 Dunblane (DS)	17	6,075,000	357,353
** 6579 Marlborough (DS)	17	6,050,000	355,882
Total	**664**	**$180,480,500**	**$271,808**

Coquitlam

Address	Suites	Price ($)	$/Unit
1035 Howie	**42**	**$5,800,000**	**$138,095**

Delta

Address	Suites	Price ($)	$/Unit
5558 15B Ave	**20**	**$3,287,500**	**$164,375**

Langley

Address	Suites	Price ($)	$/Unit
5630-40 201A St	43	3,815,000	$88,721
20117 56 Ave	88	8,732,000	$99,227
Total	**131**	**$12,547,000**	**$95,779**

Maple Ridge

Address	Suites	Price ($)	$/Unit
11960 222nd St	**59**	**$4,800,000**	**$81,356**

New Westminster

Address	Suites	Price ($)	$/Unit
* 516 Ash St	28	3,375,000	120,536
420 Ash St	42	5,728,000	136,381
206 Carnarvon St	12	1,550,000	129,167
503 Agnes St	15	2,100,000	140,000
1009 Third Ave	35	4,200,000	120,000
221 Seventh St	39	5,170,000	132,564
309 Agnes St	22	2,900,000	131,818
228 Manitoba	8	1,400,000	175,000
Total	**201**	**$26,423,000**	**$131,458**

North Vancouver

Address	Suites	Price ($)	$/Unit
170 W. 4th	36	7,000,000	194,444
* 151 E. Keith (HR)	88	25,500,000	289,773
141 & 147 E. 21st St	39	7,800,000	200,000
163 W. 5th	42	8,900,000	211,905
146 E. 12th	18	3,730,000	207,222
1549 Chesterfield	13	3,000,000	230,769
* 240 St. Andrews	19	2,800,000	147,368
2601 Lonsdale	12	2,737,500	228,125
321 E. 2nd	36	7,926,000	220,167
310 E. 2nd	48	9,900,000	206,250
2855 - 2875 - 2931 Mountain Hwy (DS)	45	13,500,000	300,000
857 W. 15th (ST)	25	8,360,000	334,400
Total	**421**	**$101,153,500**	**$240,270**

Port Coquitlam

Address	Suites	Price ($)	$/Unit
** 2550 Gordon Ave	**11**	**$1,193,000**	**$108,455**

Port Moody

Address	Suites	Price ($)	$/Unit
3048 Henry	**37**	**$4,930,000**	**$133,243**

Surrey

Address	Suites	Price ($)	$/Unit
9801 King George (HR)	266	48,000,000 (EST)	180,451
15915 84th Ave (ST)	33	6,200,000	187,879
10138 Whalley Boulevard	154	18,250,000	118,506
Total	**453**	**$72,450,000**	**$159,934**

West Vancouver

Address	Suites	Price ($)	$/Unit
425 6th Street (SP)	**16**	**$8,925,000**	**$557,813**

White Rock

Address	Suites	Price ($)	$/Unit
15151 Prospect	25	4,125,000	165,000
1285 Martin St	29	4,590,000	158,276
1081 Martin St	26	5,380,000	206,923
Total	**80**	**$14,095,000**	**$176,188**

The sale information provided is a general guide only. There are numerous variables to be considered such as:

1) Suite mix
2) Rental/sq. ft.
3) Rent leaseable area
4) Buildings' age and condition
5) Location
6) Frame or highrise
7) Strata vs. non-strata
8) Land value (development site)
9) Special financing

(HR) Highrise
(MR) Midrise
(TH) Townhouse
(ST) Strata
(DS) Development site
(EST) Estimated price
(SP) Share purchase
(NC) New construction
(MU) Mixed-use

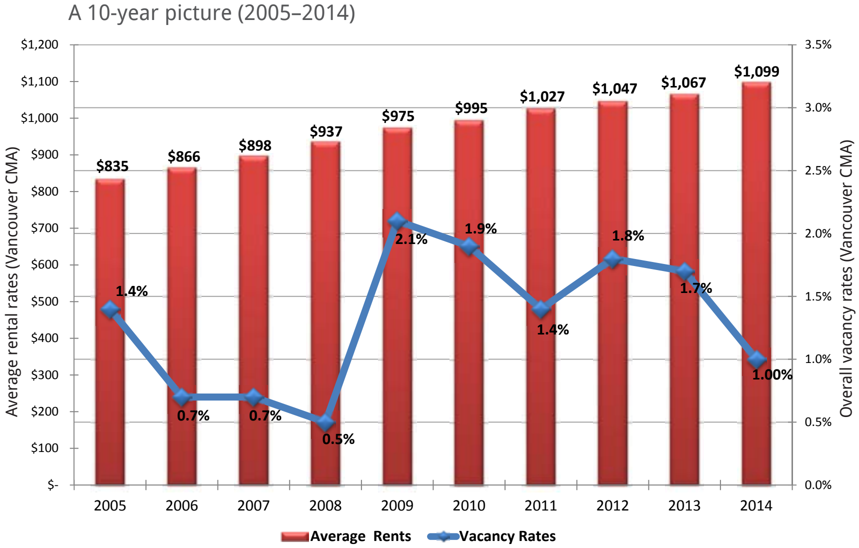
The CMHC speaks

Released in mid-December, the CMHC *Rental Market Report, Vancouver and Abbotsford-Mission CMAs* summarizes vacancy and rent averages, supply and demand factors and secondary market trends:

> The Vancouver Census Metropolitan Area (CMA) rental market tightened as growth in demand outstripped an increase in supply. Purpose-built rental apartment vacancy rates declined to 1.0 per cent in October 2014 from 1.7 per cent in October 2013. Tighter purpose-built rental apartment market conditions were rather uniformly observed across the various market segments with just a few exceptions (e.g. bachelor suites in White Rock, Langley City and Langley District Municipality, and one-bedroom units in Richmond, Mount Pleasant / Renfrew Heights, and North Vancouver District Municipality). Similarly, lower vacancy rates were also noted for the rental condominium apartments in the Vancouver CMA, which continued to have vacancy rates below those for purpose-built rental apartments. Four main factors fuelled the growth in rental demand during the past year:
>
> 1. Stronger labour market conditions, particularly for the younger 15 to 24 and 25 to 44 age cohorts;
>
> 2. Higher post-secondary student enrolment;
>
> 3. Higher home prices, which may delay movement to home ownership; and
>
> 4. Higher net migration.
>
> The supply of rental units increased for both purpose-built rental apartments as well as rental condominium apartments. The number of purpose-built rental apartments (including townhouses) edged up 0.5 per cent to 109,217 units in October 2014.
>
> Submarket Results: Tight Conditions Overall
>
> Purpose-built rental apartment vacancy rates were below three per cent for all the major rental markets in the Vancouver CMA. Market conditions were especially tight in the City of Vancouver where vacancy rates were below one per cent for most submarket areas including the West End / Downtown, South Granville / Oak, and Kitsilano / Point Grey. Student and faculty rental demand drove the average vacancy rate in the University Endowment Lands down to just 0.2 per cent, which was the same level as English Bay. Outside of the City of Vancouver, West Vancouver, North Vancouver City and North Vancouver District Municipality (DM) also had vacancy rates below one per cent. Burnaby, Richmond, the Tri-Cities, White Rock, and New Westminster had vacancy rates below two per cent. Vacancy rates for the remaining markets were between two and four per cent.[1]

Greater Vancouver CMA average rents and vacancy rates

A 10-year picture (2005–2014)



Source: CMHC & Goodman Report

Media misses the mark on CMHC trends

The latest CMHC rental apartment survey generated an unusual response from local media. A commentator appeared fixated on the estimated percentages of foreign owners: 2.3% for Metro Vancouver condos overall and nearly 6% in the downtown. While offshore investors, especially those from China, have been a hot topic, the surprisingly overlooked story is how our vacancy rates have decreased to 1% throughout Greater Vancouver and to 0.5% in Vancouver proper.

> "... the surprisingly overlooked story is how our vacancy rates have decreased to 1% throughout Greater Vancouver and to 0.5% in Vancouver proper."

[1] Fall 2014, pp 2–3.

Maximizing your return on investment

We're all aging, much as we deny or fight it. And so are Greater Vancouver's rental apartment buildings, the overwhelming majority of which are well over 50 years old. Increasingly, long-term owners are facing the stark reality that their net income is eroding as rents from tired or poorly managed assets fall ever below market norms. Exacerbating the worry of diminishing returns is the growing need for major capital replacements. Beyond the "usual suspects" such as painting, flooring and appliances, owners have to contend with unpleasant capital cost items such as roofs, piping, elevators, balconies, windows and the dreaded underground parkades and related concrete and water problems. While such capital expenditures don't necessarily generate higher rental income or attract new tenants, remediations are necessary for keeping buildings efficient over time.

Operating a rental apartment building at maximum efficiency isn't simple. Many of our clients, big and small, opt for professional property management, while others establish disciplined in-house approaches. Unfortunately, we also encounter many single-building owners, often with second-generation family members guiding operations, who don't realize that they're only earning a subpar 2–2.50% return on investment even though they're aware of the elevated value of their assets in today's market. Their properties are seriously underperforming.

As commercial agents specializing in rental apartments, the Goodman team sees and appreciates the big picture, having experienced much over our combined 45 years together, including the sale of more than 400 buildings. We understand landlord-tenant relationships thoroughly. Yet we're often surprised, if not disappointed, at finding rents for seemingly decent suites at 20–30% under the reported CMHC averages. Sustaining rents significantly below market not only means thousands of dollars lost annually but also severely decreases an asset's value.

Take a look at how this works. Picture a typical one-bedroom suite in a 56-year-old wood-frame building in Vancouver's South Granville, generating only sub-market income. According to CMHC, one-bedrooms in this neighbourhood average $1,156 per month. Surprisingly, when we inspect buildings in South Granville, we sometimes discover that the one-bedroom rent is just $900, with parking and laundry components similarly below market. Acknowledging that the rent is under market, the owner rationalizes that lower rents mean less turnover and less need for expenditures on upgrades, allowing the landlord to sleep easier. Let's not forget the equally appreciative tenants who also enjoy their sleep, stretching one-year leases into 10-year stays. Many an owner thus overlooks what the new entrepreneurs on the block recognize only too well: that the older, inefficient suite in South Granville could, with a major retrofit, command monthly rent of $1,575, so as to compete with a 10-year-old condo rental. Often unwittingly, the owner thus subsidizes a very grateful tenant to the tune of approximately $675 per month. Upgrades might include a modern kitchen and bathroom, a new washer and dryer, fresh flooring, a renovated lobby and new windows, to name a few. We have many investors keen to buy underperforming properties in good locations and upgrade them to market value.

We remind our readers that every B.C. landlord should keep on top of the market by regularly referencing CMHC's annual rental report (online under Reports at www.goodmanreport.com). At the Goodman team, we ourselves review hundreds of operating statements, visits scores of buildings and receive an endless number of queries. We exchange information with appraisers, lenders, accountants, lawyers, property managers, caretakers, sellers and investors constantly.

> "... the Goodman team sees and appreciates the big picture, having experienced much over our combined 45 years together, including the sale of more than 400 buildings."

> "Sustaining rents significantly below market not only means thousands of dollars lost annually but also severely decreases an asset's value."

Beware the opportunity cost

Here's an idea of what you're missing when you don't upgrade. Assume for a moment that an 11-suite unrenovated building sells for $3,150,000 ($286,000 per suite) and a 2.5% cap rate. This building's operating statement, shown on the left-hand column of the chart below, could very well transform into the version shown on the right, should the building undergo a major retrofit and achieve the gross income indicated. Fully realized, the value jumps by one million dollars to approximately $4.15 million ($377,000 per suite), effectively generating a 4% yield. The cost of the upgrade is about $40,000 per suite or $440,000, resulting in a profit of roughly $560,000. While this is only meant as an exercise, rental apartment buildings are valuable assets, and we strongly encourage you to maintain your property and optimize rents. Doing so pays handsomely!

"... rental apartment buildings are valuable assets, and we strongly encourage you to maintain your property and optimize rents. Doing so pays handsomely!"

Before and after

Property example: wood-frame rental apartment building with 11 one-bedroom suites

Unrenovated: subpar income		Renovated: optimized income	
Units: 11 units at $900/mo (= $9,900) x 12 mo	$118,800	Units: 11 units at $1,585/mo (= $17,345) x 12 mo	$209,220
Parking: 6 stalls at $25 (= $150) x 12 mo	1,800	Parking: 6 stalls at $50 (= $300) x 12 mo	3,600
Laundry: 11 units at $3 (= $33) x 52 weeks	1,716	Laundry (in-suite included)	0
Gross income	122,316	Gross income	212,820
Less vacancies at 0.5%	(612)	Less vacancies at 0.5%	(1,064)
Effective gross income	$121,704	Effective gross income	$211,756
Less expenses at $3,900/suite	(42,900)	Less expenses* at $4,200/suite	(46,200)
NOI	$78,804	NOI	$165,556
Estimated value: $3.15 million ($286,367 per unit, 2.5% cap rate)		Estimated value: $4.15 million ($377,272 per unit, 4.0% cap rate) *Reflects need for higher operational costs	

What's really driving our real-estate values

Regardless of the type of real estate, land prices in Greater Vancouver have significantly appreciated over the years. Our well-known geographical constraints make for a chronic scarcity of zoned and developable land. Combined with low interest rates and strong immigration, these factors have sent our local real-estate prices to previously unimaginable new heights as compared to those in all other Canadian provinces.

Vancouver developers actively seek not only multi-family sites but also land offerings representing industrial, commercial, office, mixed-use and single-family development opportunities. Competition within our well-financed and highly qualified development community is intense, with premium offerings of land typically attracting multiple bids. We've learned that the Pearson Dogwood hospital site, consisting of about 25 acres at Cambie and 59th Avenue, recently received 10 proposals: this for a piece of land that might sell for approximately $200 million, depending on the terms.

Greater Vancouver has become a bona fide worldwide brand destination ranking with many other world-class metropolitan areas. We offer political stability and leading universities in a free, democratic and tolerant society with a secure banking system, and we've hosted successful Olympic and Expo experiences. A recognized gateway to Asia by shipping and air, we're the new home for thousands of immigrants each year. Finally, we're blessed here in Greater Vancouver with a mild climate and, in B.C., some of the most exquisite untouched wilderness on the planet. As for the Canucks, well, they're still a work in progress.

Whereas in the not-too-distant past it was local buyers who stepped up, today's sellers cater to a global audience. Canadian financial institutions, REITs, life insurance companies, syndications, and immensely wealthy groups and individuals from China, Dubai, Germany, London, Russia and elsewhere throw vast sums into our diverse real-estate vehicles including condos and single-family residences. In a recent article on the role of foreign investors in driving our prices to record highs, *Business in Vancouver* cites *Emerging Trends in Real Estate 2015*, a report by PwC and the Urban Land Institute based on interviews with leading developers, financiers and investors. BIV quotes the report as suggesting that offshore investors aren't looking for immediate proceeds from their properties: "Returns aren't the point:

safety of capital is, and a $5 million condo is more insurance policy than investment."[2] Consider the Russian oligarchs who have purchased homes in London over the past few years.

Back in 2004, our five-year Bank of Canada bond rate was 3.82%. In 2014, it stood at 1.58%. Low mortgage rates and scarcity of product have been rocket fuel for prices. In fact, during this 10-year period, values as tracked by the *Goodman Report* have increased 140% in the multi-family sector alone.

With Canada enjoying an extended period of low interest rates and Vancouver boasting a glittering reputation on the international stage, our real-estate market has maintained robust pricing for investors and homeowners alike.

Land is key

Have you checked your assessments lately? Of course they're higher than in previous years, as are your taxes. With respect to Vancouver's aging rental stock, 75–95% of the assessment figure is usually weighted toward the land component. As a building structure ages, it normally depreciates, while at the same time, the land value continues to rise. Before demand took off for densification (also called "intensification"), few older buildings in any asset class were torn down. Today, demolitions are commonplace where permitted, as higher densities in many instances have effectively caused many older properties to be reclassified as "land value."

A recent sale illustrates the profound impact of land on overall value and the manner in which developers influence pricing. In 2014, the Goodman team sold two older buildings in Vancouver's affluent Kerrisdale neighbourhood on C-2 zoned property (2.5 FSR) for approximately $300 per square foot gross buildable. The 10 separate co-op owners of one of the buildings and the landlord of the other (a traditional rental) worked together, realizing a significant premium over the traditional pricing model, by virtue of the fact that their buildings were sold for land value as a single development site. Fortunately for them, this particular zoning designation has no demolition restrictions (as compared to more typical RM-zoned areas). Our analysis suggested valuing the properties in this way rather than using the typical income or comparable approaches or valuing the co-op building as the sum of 10 individual units. In other words, the owners were compensated for the underlying redevelopment potential of their respective sites. They were very pleased with our advice: they each received approximately one million dollars more for their properties on the basis of land value!

When a developer identifies a property as having some potential, the development company typically prepares a proforma. This is a detailed financial analysis used to calculate the highest amount that a developer can pay for the land and still make a reasonable profit after building. The developer determines whether this figure, called a "land residual," is higher than the existing use of the property. If it is, the developer will aggressively seek to purchase the property. If not, then the developer won't acquire the site.

As redevelopment of older rental buildings (including condos, co-ops and social housing) located on high-density land becomes more widespread, we anticipate that more and more owners will naturally consider proposals when developers come knocking. The Goodmans' role in this process is to help an owner determine whether there may be interest from developers, with the goal of ensuring the highest potential sale price. We're very pleased that we helped achieve this result for our clients in Kerrisdale.

What's hot and what's not?

Hot

- Rumour: rent controls are being removed
- Filling up for $0.97 a litre
- Rental vacancies at 0.5% in Vancouver
- Astonishingly low CMHC five and 10-year rates (1.9% and 2.5% respectively)
- Unprecedented demand for apartment buildings
- Gold
- The *Goodman Report* (no fluff, no ads with often quoted accurate information)
- Cartoons
- Referendum on transit
- Burnaby's Mayor Corrigan

Not

- BC Ferries pricing: Where are you, Premier Clark?
- Highest gas prices in Canada (still)
- Highest wine prices in Canada (will get worse)
- Unused downtown bike lanes
- Unsynchronized traffic lights, especially along West Broadway, Oak to Arbutus
- Major layoffs ahead in Alberta energy sector
- Goodmans' intellectual property stolen
- Vancouver city manager Penny Ballem
- Deflation

"... they each received approximately one million dollars more for their properties on the basis of land value!"

[2] Frank O'Brien, "Vancouver a 'hedge city' to park foreign cash: study," *Business in Vancouver*, November 12, 2014.

Desperate tenants, stymied developers

Alongside the stalwart condo market, several developers have recently expressed interest in constructing new purpose-built rental buildings. With condos and single-family homes reaching prices inaccessible to many local residents, and with vacancy rates hovering at 1% in Vancouver CMA and 0.5% in Vancouver proper, tenants eagerly flock to the launch of any new rental building, paying rents typically 50% higher than in older rental buildings. They welcome the flexible advantages of modern, centrally located buildings that offer functional, attractive suites and elaborate amenity areas, all with no mortgage, taxes, monthly maintenance fees or routine repair bills.

Investors, including large pension funds and Canadian life insurance companies, seem similarly inclined of late about these newer purpose-built rentals, albeit for reasons differing from those of tenants. Particularly in Vancouver, given our aging rental stock, investors are showing a strong trend toward acquiring new buildings for their portfolios. The attraction of higher rental income coupled with less maintenance and capital expenditure is proving irresistible.

The latest CMHC rental apartment survey demonstrates what the Goodman team has long maintained: that the City of Vancouver has done a poor job of providing ample rental accommodation for its citizens. The fact that vacancies in Vancouver have plummeted to only 0.5% indicates availability of only 281 suites out of a total inventory of 56,176, down from 2013's already depressed figure of 1%.

Amid the stress on families and individuals frantically searching for suites, developers hoping to satisfy demand are equally frustrated in their efforts to create rental accommodation. They face dizzying levels of red tape, disincentives, financial extractions, sustainability requirements and other social engineering demands from a planning department effectively controlled by the city manager's office and by a few insiders who are ramming a square peg into a round hole while still failing to comprehend the meaning of Economics 101.

Beyond these bureaucratic impediments, a developer seeking to build a rental must endure the city's snail's-pace vetting process, which means waiting two to three years before receiving a building permit. Exacerbating the supply problem still further, the city prohibits a developer from tearing down a low-density, inefficient 50 to 80-year-old building in an existing multi-family zone and replacing it with a combination of higher-density rentals and market housing. Since so few development sites qualify for the Rental 100 Program, lifting the demolition moratorium now in effect for some eight years and eliminating the archaic zero-rate-of-change policy would serve our residents well, especially those seeking affordable rentals.

A call for action

Seeking re-election, Mayor Gregor Robertson pledged over 1,000 new rental units each year. In the opinion of the *Goodman Report*, he has a lot of serious work to do beyond that. Rather than focusing simply on the number of apartments to make available, his administration should show bold leadership in introducing structural changes that allow market forces to work.

The first step is permitting the demolition in the now "untouchable" RM-zoned areas of some older, low-density rental stock, to free up land for higher-density rentals and market housing. The city should actually allow owners to redevelop their properties on the basis of their existing zoning. What a concept: recognizing property rights! We'd love to see the city cultivate a market-driven environment by creating a separate body, independent from government, in charge of fast-tracking approvals so that developers could build what the market requires, including micro-units.

Everybody would benefit. Tenants would have expanded choices, the city would increase its tax base, thousands of new construction jobs would be created, and owners of older, low-density buildings would be able to sell them for appropriate land value. This issue of enabling affordable rentals should be dealt with as a priority, or very serious social and economic consequences will follow.

The good news? Incompetence among politicians and planners means inaction, and inaction severely restricts supply of housing. As we all know, limited supply results in still lower vacancies and still higher rents!

> "The city should actually allow owners to redevelop their properties on the basis of their existing zoning. What a concept: recognizing property rights! "

Political ability is the ability to foretell what is going to happen tomorrow, next week, next month and next year. And to have the ability afterward to explain why it didn't happen.

-- Winston Churchill (1874–1965)

> "They face dizzying levels of red tape, disincentives, financial extractions, sustainability requirements and other social engineering demands from a planning department effectively controlled by the city manager's office and by a few insiders who are ramming a square peg into a round hole while still failing to comprehend the meaning of Economics 101."

David Goodman
Direct 604 714 4778
david@goodmanreport.com

Mark Goodman*
Direct 604 714 4790
mark@goodmanreport.com
*Personal Real Estate Corporation

The Goodman Report
320 - 1385 West 8th Ave.
Vancouver, BC V6H 3V9

Greater Vancouver's #1 Multi-Family Investment Resource
www.goodmanreport.com

HQ Commercial