Misfiring markets spark swing to real estate

BY RANDY RAY

Tom Gasparec plans to retire wealthy, but he's not counting solely on stocks and mutual funds to get him there.

Frustrated by big losses in his investment portfolio, and spooked by repercussions from Sept. 11, the 25-year-old Toronto software sales rep has purchased two residential income properties and is looking for a third.

As a landlord, he's hoping record low mortgage rates, rising property values and continuous rental income will produce better returns than his faltering market investments.

Mr. Gasparec, who works for Conexsys Communications Ltd. in Mississauga, Ont., purchased his first investment property, a semi-detached bungalow in Mississauga, in December, 1999, when markets were on the rise. Last December, with stocks still reeling from the terrorist attacks, he bought a one-bedroom condo in downtown Toronto. Soon, he plans to buy a multifamily building.

"I will still play the markets, but this is my way of diversifying and getting into something that will generate steady and decent returns," he says. "Real estate is real property — you can only lose so much, even if the market tanks."

So far, his strategy is working. By mid-March, the rental properties he purchased for $175,000 apiece had risen in value to $225,00 and $190,000. After paying taxes, maintenance and mortgage — at interest rates of 5.75 per cent and 2.6 per cent — he's clearing $500 a month in income.

"By paying off the mortgages faster, my goal is to have both properties paid off in 10 or 11 years," says Mr. Gasparec.

Stories like Mr. Gasparec's are catching the attention of investors across Canada, many of whom watched helplessly last year as plunging markets broadsided their stock portfolios.

But not everyone is enamoured of the move into rental properties. Some investment experts maintain that real-estate investing is more perilous than playing the markets.

"If a client tells me he is getting into property rentals, I say 'don't do it, I hate it,' " says Warren Baldwin, regional vice-president of T.E. Financial Consultants in Toronto. "The fact is, most people aren't qualified to handle the landlord-tenant situation — you really have to look at yourself in the mirror before you become a landlord. It has the potential to keep you up at night, and wake you up at night."

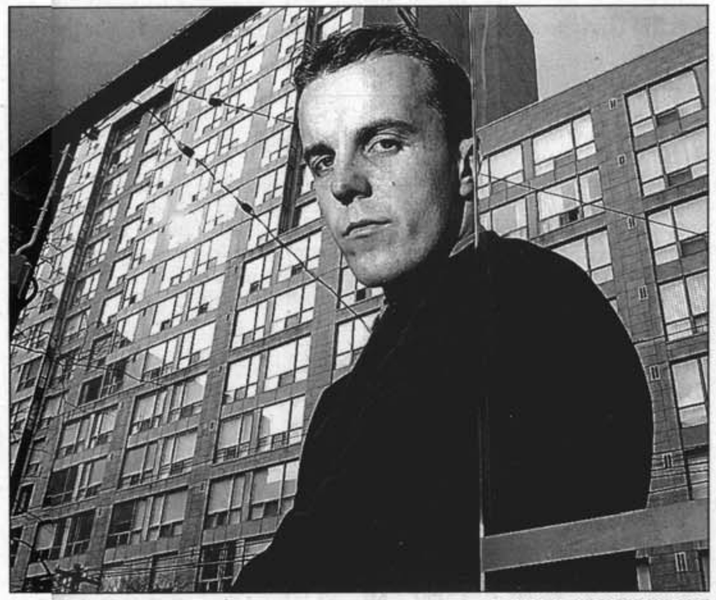
Still, with one- and five-year mortgage rates at between 3 and 6 per cent, and real-estate experts boldly predicting double-digit gains in property values in the coming year, clients are flocking to real-estate agents. In most cases, agents say clients hope to own a handful of paid-off properties within 10 to 15 years that will be worth considerably more than they paid and generate a significant income stream.

Janet Munro, an Ottawa agent with RE/MAX Metro-City and herself the owner of a rental property, says 25 per cent of her clients are in the market for income properties, a threefold increase since the late 1990s. Toronto real-estate broker Kim Egerton reports four times as many inquiries as a year ago.

Income-property options include homes, condos and multi-family properties, vacant land and recreational property, such as a cottage or ski chalet.

Most experts dismiss vacant land and leisure property because there's little potential for year-round cash flow, and gains in value, especially for vacant land, can take years.

"You want an asset that puts money into your pocket," says Ms. Egerton of Royal LePage Real Estate Services Ltd. in Toronto. "Vacation properties and empty lots often take money out of your wallet because there is not always income."



TIBOR KOLLEY/THE GLOBE AND MAIL

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Would-be investors don't have far to look for examples of income properties that are outdistancing equity markets, although high demand in some centres can make good properties hard to find.

In the Vancouver area, real-estate Web-site owner and newsletter publisher Ozzie Jurock says the "triple whammy" of low prices, a low vacancy rate and rock-bottom interest rates presents investors with the opportunity of a lifetime.

He knows investors in Vancouver-area communities such as Surrey who have put $18,750 down on $75,000 condominiums and are pocketing $221 a month after expenses, for a 14-per-cent annual return on their downpayment.

In downtown Vancouver, Calgary and Edmonton, buyers can get one-bedroom condos for $130,000 and earn returns of 12 to 18 per cent on initial investments of $32,500, he says.

In Toronto, Richard Ling, vice-president of Harvey Kalles Real Estate, says investors with a $25,000 downpayment can find downtown condos for $165,000 that will turn a monthly profit, after expenses, of $125 for unfurnished units and $625 for furnished units.

"That compares to $371.25 in a GIC that is paying 1.05-per-cent interest and who knows what on the stock market, where prices can go up or down," he says.

Agents say investors are making solid returns because of low interest rates and rising rents as a result of a shortage of rental units.

In Vancouver, where the vacancy rate is 1 per cent , Mr. Jurock says some 1,000-square-foot apartment units that rented for $950 when the rate was 1.4 per cent a year ago now command $1,650. Generally speaking, however, rent increases have been more modest, ranging from 2.7 per cent in Oshawa, Ont., and Victoria to 8.8 per cent in Calgary, says the Canada Mortgage and Housing Corp.

CMHC sees no signs that vacancy rates are headed dramatically higher. Rates in Canada average 1 per cent and are expected to rise to 1.3 per cent in 2003, says Michel Laurence, CMHC's senior adviser, economic and housing analysis.

There's also money to be made as income properties appreciate in value, housing experts say.

In Ottawa, where sale prices for all houses have increased by 13.6 per cent in the past 12 months, continuing demand and a shortage of supply for condos has increased prices by 20.4 per cent in the first two months of 2002, on the heels of a 14.9-per-cent gain last year, says Alain Miguelez, senior market analyst for CMHC's Ottawa office. Sale prices for row housing, semi-detached homes and bungalows are up 13.6 to 24 per cent in January and February of this year over the same months last year, he says.

In Vancouver, Mr. Jurock is forecasting a 2002 price increase of as much as 30 per cent in the condo market; in Toronto, Mr. Ling expects well-located, prime condos to rise at least 10 to 15 per cent.

Mr. Ling and other agents stress, however, that not all properties will show such large price increases. Canadian Real Estate Association statistics show that house-price increases across Canada in 2001 averaged 4.8 per cent .

While owning rental properties and having tenants pay the bills may sound like a good way to build wealth, experts stress that donning a landlord's hat isn't for everyone, largely because of the potential hassles.

"It is quite possible to do well owning individual properties but the first question I ask is how active do you want to be in this investment," says David Christianson, a senior adviser at Wellington West Total Wealth Management in Winnipeg. "There are a lot of risks and plenty of headaches, including tenant problems, rising interest rates, changes in the economy, declines in the neighbourhood, uninsured perils, loss of personal interest in the project and the risks posed by the lack of liquidity."

Robb Boyd, principal responsible for products, services and marketing at Edward Jones in Mississauga, cautions against liquidating a large part of a stock portfolio to buy income properties. By selling now, you'll likely take a heavy loss on your equities, Mr. Boyd says, and, if you give up on the markets, you'll sacrifice the diversification that's one of the golden rules of investing.

Mr. Baldwin says that with markets on a recent upswing, they could bring solid single-digit returns over the next year without the headaches of managing property. He also notes that stocks and mutual funds are more liquid than property and offer opportunities to invest outside Canada.

Others say that rising property values may mean investors have already missed the real-estate boat.

"Investing in income properties was a better prospect a year ago," says Frank Clayton, president of Clayton Research Associates in Toronto.

"Mortgage rates can go no lower and as far as the little investor is concerned, it looks like the stock market has turned the corner — although who knows?"

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