



Is Real Estate Investment a Good Idea in Today's Market?

~Anita Lamarche, REALTOR® and Real Estate Investor

The start of 2018 has been full of challenges for the Calgary real estate market, with a combination of the introduction of the mortgage stress test (requiring buyers of homes with 20% or more down payment and no mortgage insurance to qualify at the Bank of Canada overnight rate or 2% higher than the contract mortgage rate - whichever is greater) as well as some small but successive interest rate hikes. This has reduced the buying power of consumers and lead to some market adjustments,

with a recent decline in home sales across the country during the first half of 2018. And in Calgary, with our local economy in a slow recovery from recession and countering effects of lending changes, real estate sales volume has softened just over 20% for the year to date.



However, with a shift to more of a buyer's market plus greater selection (more listings) and more attractive entry prices in certain types of properties and neighborhoods – this could be a lucrative opportunity for real estate investors - especially those with a longer term view of the market.

Below is a simplified illustration of the financial performance and projections for my first income property, purchased in 2017. The duplex with a basement suite currently generates \$2,400/month gross rent and is just slightly cash flow positive. This means the property generates a small amount of income, after covering the mortgage, taxes, insurance and allowances for vacancy and maintenance (approximately 10% of gross rent). At first glance, having an income property that doesn't generate significant cash flow may seem counter intuitive. But with investment property, the real magic is in having SOMEBODY ELSE pay the ongoing mortgage and expenses while YOU earn equity three ways:

1. **Cash flow**
2. **Principal recapture** (equity earned as the mortgage gets paid down) and
3. **Passive Appreciation** (assuming real estate prices rise over the long term)

And with a small amount of cash needed up front, usually 10-20% down for a non-owner occupied residence, LEVERAGE works for you providing for a higher return on your invested capital.

Here is a simple illustration of what your returns might look like with a \$400K property investment:

	Year 1	First 5 Years Scenario
Cash investment (down payment and improvements)	\$80K	\$80K
Cash Flow @ \$100/mo (net after covering all costs and allowances)	\$1.2K	\$7.5K (includes rent escalation)
Principal Recapture (equity through mortgage paydown)	\$10K	\$55K (paydown accelerates)
Passive Appreciation (est. 3%* of \$400K)	\$12K	\$63.6K (appreciation is compounded year over year)
Total Return	\$23.2K	\$126.1K
Return on Invested Cash	29%	158% (31.6% annualized)

**Real estate property values average increase is approximately 6% over a 100-year period; 3% is a conservative view for longer term appreciation when considering historical averages.*

You can also potentially earn Active Appreciation if you renovate or update an under-performing property and the resulting increase in market or appraised value is greater than your capital investment. For example, you could do a modest renovation to update a kitchen and bathroom, flooring, entry doors and paint. If you spent \$40K but the property value increased by \$75K, you would have generated another \$35K in active appreciation – in addition to the cash flow, principal recapture and passive appreciation earned from the property.

Returns on invested cash in excess of 20%, over a period of years, can make a significant contribution to your personal wealth and position you for earlier retirement. Plus equity can be tapped into by refinancing or using readvancable mortgage products to allow you to access capital to invest in more properties over time (possibly with partners or joint venture financing agreements depending on your financial circumstances). Or some more conservative investors may choose to have the investment get paid down so it generates more cash flow and income during their retirement years. Either way, income properties are a sound investment with potentially very attractive returns, secured by real property.

Of course, not everyone may be cut out to be landlords. We've all heard horror stories about bad tenants and unsavoury situations for landlords. We can't pretend it's all unicorns and rainbows being a rental property owner. But if you take extra steps up front to screen tenants (background and reference checks), do regular inspections of the property and take other safeguards, you can avoid a lot of headaches. Many investors also choose to be more passive with management - working with a property manager who will find and screen tenants, collect rent and coordinate property maintenance. This can also be a great business model if you choose to own rental investments in other cities or provinces than

where you live, or scale up your portfolio. Property management costs generally range from as low as 5% to as high as 12% of gross monthly rent; typically in Calgary property managers charge 8-10% of gross rent and may collect an additional fee up front when the unit is first rented. For some investors, they feel that is money well spent. Other investors like me may choose to be more hands-on with their first income properties to gain a real appreciation for the work a property manager does - and have direct control over the quality of tenants they select. So far, this model is working for me (fingers crossed).

If you are intrigued and wondering how you might get started, consider the equity in your home as a potential source of down payment and possibly an operating line if you decide to make some improvements to an under-performing or distressed property (I.e. renovations that will not only increase the value of the units more than the cost, but will also result in attracting better tenants and higher rents). Many investors get started by using some of their home equity and it is generally fairly easy to secure a mortgage for a second or third residence as long as your credit score and income qualify.

If you are interested in learning more, I would be happy to meet with you and review your goals and current opportunities in the market. And I am aligned with some excellent Mortgage Brokers and other investment-specialist accountants and contractors to help you build a team of professionals which will support your success. For more information, please contact Anita Lamarche of CIR Realty at 403.818.9623.

.....

About the author:

As a CIR REALTY Agent and member of Leading Real Estate Companies of the World™, my goal is to ensure that you have the best real estate experience possible. Whether you are looking to sell your current home, purchase a home locally or around the world or find profitable investment properties, I have the resources and expert knowledge to make sure that you get the best service and the best possible price for exactly what it is you are looking for.

With over 35 years as a Calgary resident in all quadrants including city and acreage living, investment property ownership and a successful career in marketing, I am here to serve you and to connect you with professionals who will protect your interests every step of the transaction. I am 100% committed to my Clients and am honoured to be able to help them with their most important assets - their home and investments.