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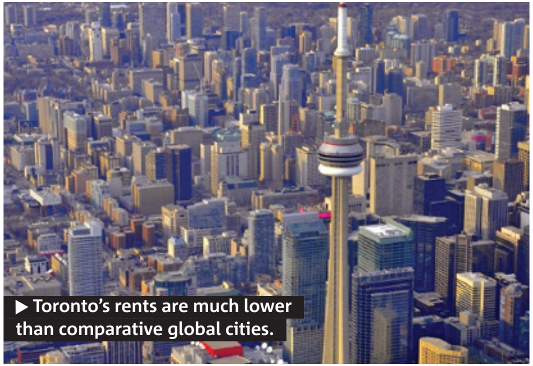
Your condo as an investment

▶ Toronto's condo market shows no sign of slowing down
▶ Astute investors may need to react to rising costs, shrinking rental incomes

ISTOCK IMAGES



▶ Toronto's rents are much lower than comparative global cities.

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Toronto is currently the dominant North American condo market, with over 18,000 units being sold annually over the past five years, according to findings by Urbanation, the Toronto-based condominium market research firm, and a great number of the buyers have no intention of living in them. The study found that "With many downtown condominium projects selling over 70 per cent of their units to investors, developers need to keep a keen eye on index price movement and rental transaction activity."

A number of factors are behind the explosive growth of condos in the GTA. First and foremost is an influx of foreign buyers: Offshore investors are buying up Toronto condos sight unseen for the purpose of investment.

So is the Toronto condo rental market saturated? It depends who you talk to. Shana Bahrami, a licensed realtor affiliated with Right at Home Realty Inc., maintains that "The Toronto real estate market continues to exhibit strength in the demand for new condominiums, particularly as investment properties for those with new money. This trend indicates that any suggestion of a developing 'condo bubble' represents ongoing conjecture, rather than market reality."

And a Canada Mortgage and Housing Corporation study from the fall of 2010 found that "The average vacancy rate for purpose-built apartment buildings in the GTA declined to 2.1 per cent in October 2010 from 3.1 per cent in October 2009. The average rent for two-bedroom apartments common to last year's survey increased by 1.8 per cent."

All that may change this year as a result of the pervasive condo construction in Toronto. According to CMHC statistics, "A surge of nearly 8,000 condominium apartments were completed in the June to September 2010 period. These new units likely worked to push vacancies higher." And as of last June, "there were over 34,000 units near completion in the GTA."

With 20 per cent of the GTA condo market being rental, what happens when all these units hit the street this year? The quandary for investors is that rental rates are not rising relative to the increasing prices and costs paid by investors, and Toronto's rents are much lower than comparative global cities.

A study by Adrienne Warren published by the Scotiabank Group in March, is optimistic that Canada's residential activity will remain buoyant, but rentals may go soft. "It is also highly unlikely that Canada will experience a U.S.-style housing collapse. The roughly 25 per cent correction in U.S. home prices from their 2006 peak was primarily the result of weak lending practices and high-risk mortgage products largely absent in Canada," says Warren.

"Canada's average rental apartment vacancy rate in major urban centres edged down slightly last year to 2.6 per cent, and has remained historically low throughout the past decade. Vacancy rates for rented condominium apartments are low, at 2.0 per cent or less in six of the 10 CMAs surveyed by CMHC.