THE GOOD, THE BAD, THE POSSIBLE:

PURCHASING INVESTMENT REAL ESTATE IN TODAY'S ALBERTA ECONOMY

BY RICK HARRIS, REIA

As an Alberta real estate investor since 2002, I have seen The Good, The Bad, and The Possible of Alberta investment real estate.

My wife and I own investment properties in the Edmonton, Red Deer, and southern Alberta areas. In recent visits to our properties, I've seen the bumper sticker that seems to pop up every time there's an economic downturn and which is now more prevalent than ever: "Please God, give me one more Alberta oil boom. This time I promise not to piss it away."

Many of us investing in Alberta remember December 2008, when oil dropped to $51.20 a barrel from a high of $154.38 in March of that year; the downward trend seemed swift. And just as sudden as the decline in prices was the upswing to over $100. (January 2009, $47.99; January 2010, $81.66; by December 2010, $101.25.)

The Good

We all had to re-examine the bigger picture of the long-term real estate success formula that REIN has been talking about for years. We had to be more aware of GDP growth, job growth, population growth, increased rental demand, decreased vacancies, increased rents, increased property purchase demand, and increased property prices. All these factors lead to success when they are moving upward; the opposite is true when things are in reverse.

In January 2009, when oil bottomed out at $47.99, we saw property prices fall, property purchase demand decline, rents lower, vacancies increase, jobs disappear, people move out of cities and towns, and a decline in GDP growth.

The dramatic drop in oil prices in 2008 forced many of us to change our purchasing and rental practices. Can you remember what recommendations REIN gave us? Did you implement any of them?

Prior to 2008, many of us were not doing property analysis, and if we were, we were accepting properties in our investment real estate portfolio that did not meet the criteria for a great rental property.

Many of us had such awesome positive cash flow, we were spending on lifestyle and not on keeping our investment portfolio financially healthy.

We did not care if we had tenant turnover; another tenant was lined up to fill the vacancy. We were not being sharp with our pencils when it came to costs of operation. We did not give our properties the TLC—the tender loving care—they deserved. If we were in condominium complexes, we were not funding them and doing the building upgrades the way we should have been. Many of us underfunded reserve funds, forcing the Alberta government to revise legislation to make owners improve the viability and economic state of these reserve funds.

TLC Wake-Up Call

Luckily, many of us got the wake-up call, as the stress we were experiencing was no fun.

In 2010 and 2011, my wife and I continued to make purchases in our portfolio—some of our best purchases, in fact. We changed our 2008 and earlier purchasing practices and implemented a new "tender loving care" purchasing strategy for our investment real estate purchases.

Stage 1—The tender: We focused on every property we purchased, doing full renovations, including new appliances and replacing the standard bi-fold bedroom-closet doors with sliding mirrored doors—big hit! We pulled up the carpet in the living rooms, dining rooms, and hallways and replaced it with laminate flooring—also well received. We replaced the exhaust fans over the stoves with combo microwave–exhaust fans. We worked all the upgrades and new appliances into our mortgage financing.

Stage 2—The loving: We focused on the entire condominium complex, joining the Board of Directors. We reviewed the overall appearance of the building, its structure, and the reserve fund study. In most cases, we only had to slightly increase the condominium fees, which still gave us access to a larger fund. Sitting on the board, we made decisions to improve the curb appeal of the building, and also to paint the walls and trim, change the flooring, and improve the lighting in many common areas (the latter so our tenants and residents felt safer). This refresh gave each building a better overall appeal; remember, the building has only one chance to make a good first impression.

Stage 3—The care: We re-examined our mortgages, and as they came up for renewal we built in a rainy-day fund to ensure we could either take a mortgage-payment vacation or have access to a mortgage cash account. You won't believe how those two mortgages changes helped us going forward.

The year 2011 now seems like the distant past; how long did you stay true to your operational changes?

The Bad—The Slow Drip

What is interesting about the current economic downturn versus other downturns is its length. In March 2011, oil rebounded to $114.69; how many of you thought we were headed back to over $150 a barrel?

What started as a slow and steady decline accumulated in January 2016 at $29.01—five years in the making.

God gave us one more oil boom; did you recognize it or think you were in economic recovery forever? Or, as the bumper sticker asks, did you flush your financial wealth, knowledge, and lessons down the drain?

In March 2016 in Calgary, REIN changed its scheduled ACRE program to a Real Estate SOS, recognizing that we were in a lingering downturn. REIN had graphs showing us that this downturn was outlasting every other economic downturn in decades.

The REIN's SOS recommendations on the defence side included to provide excellent customer service, offer incentives to re-sign a lease, maintain the quality of the units, reduce rents, and change our tenant profile to be more accommodating. On the offence side, they were to improve the property, enhance tenant screening, and create new rental incentives—things you might never had tried before.

How many of you implemented the March 2016 REIN SOS defensive and offensive recommendations?

The Possible: 2017 and Beyond

We are at a point again where time is on our side; it has been a long recovery road back. In January 2017, we saw oil rise to $52.81—just over the low-price point of the 2008 economic downturn.

In the oil industry, we are starting to see a much friendlier environment: the Canadian government recently approved two oil pipelines and, with the change in the U.S. government, Keystone XL is back on the table. It will take some time to get these projects up and running, and to see their full positive economic impact.

In an interview with Victor D. Lillo, senior vice-president, Business Development, Westbridge Capital, he told me, "The significant production cuts from OPEC, combined with natural decline rates of producing oil wells, will impact the oil glut; further, it seems reasonable that the oil market will come roaring back as the oversupply is reduced and global demand rises." Lillo also observes that there will be significant returns to investors and companies engaged in the capex recovery speed.

Current Market Conditions

Are you caught up in the past, or are you paying attention to the now?

In a recent conversation with Monte Gannon, Realtor®, RE/MAX, Edmonton, about the market conditions in the Greater Edmonton area, he told me that January 2016 real estate sales were brutal and that January 2017 came bouncing back—he had his second best January since 2008.

Laura Henriksen, owner of Red Key Realty & Property Management, has seen a marked improvement in the Red Deer rental market. The largest number of vacancies was in her one-bedroom rentals; in late 2016, this number was over 51% of her entire vacancy portfolio. In Laura's words, "That was a huge number!"

By mid-February 2017, that number had dropped to less than 35%, and Laura says they are now having a hard time staying on top of the rental applications.

Many of us have, as real estate investors, lived through two economic downturns; did you implement lessons learned and the recommendations made?

Are you getting ready for The Next Possible?

Rick Harris, an active real estate investor since 2002, has developed his purchasing strategies and processes specializing in vacation and recreational properties, single-family homes and condo rentals.