

# NUANCES OF INVESTMENTS IN APARTMENTS



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Every day we receive dozens of calls with questions from those who are interested in investing in apartments during the excavation stage. In this article I would like to answer some of the most frequently asked questions regarding this topic.

### **1. What is the minimum amount of money needed to start investing?**

I would estimate you would need 30-40 thousand. Not often, but occasionally we have transactions where the total deposit does not exceed this amount. But we must not forget that it is not at all necessary to have this money in a bank account; in most cases it is sufficient to competently use the credit resources provided by a variety of different banks and credit organizations.

I would divide investors working with us into three categories: 1) Those who operate with more than a million dollars are the so-called big investors, they have been working with us for years and have been purchasing apartments in many projects with which we work; 2) Investors operating with amounts of 100 to 500 thousand; and 3) Smaller investors whose

total operating capital is no more than 100 thousand. Our average client belongs to the second category and most often has about 100-150 thousand of their own money, plus credit resources.

However, among our clients are those who started creating an investment portfolio with a sum of 30 thousand or less and now operate in the hundreds of thousands. So as they say, "as long as there is a desire."

### **2. How are the returns of 100% per annum on the invested capital?**

When buying an apartment at the initial stage of construction, it is necessary to contribute about 15% of the value of real estate, and this amount is paid not once but in equal instalments.

Usually, during the first two years of construction, on average, during the construction period, you invest about 10% of the price of the apartment. The apartment being built should be increased by 10% per year, so that your deposit would bring 100% of the income in an annual equivalent, which is very easy to achieve with the right choice of the project.

Projects with which we work are usually added at a price of at least 5% per year regardless of market conditions. That is, if the real estate market is standing still and there is no rise in price, the yield of your deposit is about 50% per year and the real estate market is growing at 5% per year.

As statistics for the last 50 years has shown, the average price increase in real estate in Canada is 6% per annum, and your deposit already brings 100% per annum.

What can we say about the last few years when the condominium market grew much more than 10% per year?

### **3. What should I do if, at the end of construction, the bank for some reason does not give a loan?**

Let's consider the following example. The apartment bought at the stage of excavation for 500 thousand, usually at the end of construction costs 600-650 thousand. When issuing keys, you need to add an



additional 5% of the cost of the apartment, bringing your total deposit, which now becomes a down payment to 20% of cost, respectively. To close the transaction you need a loan of 400 thousand, with the market value of the property being purchased at 600-650 thousand. That is, you need a loan of about 60% of the real value of the loaned property.

And even if the central banks, regulated by the rules for the issuance of mortgages by the established state, for one reason or another cannot qualify you, there are many financial institutions in the credit market that will be happy to give you the necessary amount without any questions.

Of course, the lending rate will be higher, but if you do not plan to keep the apartment for years, and plan to sell it in a year and a half to minimize taxes, the difference in the lending rate will not affect the yield

on the transaction. Finally, you always have the option to resell the contract before closing the deal. Of course, in this case, it will be necessary to practically divide the profits received by paying the state all the necessary taxes in full, but even then the return on investment will remain quite high, except for this sale of an assignment today is an extreme measure, which is not often met.

***4. How important is it that in the first year after the completion of construction, the apartment would bring a positive Cash Flow (that is, the amount received from the rent completely covered the costs of mortgage, maintenance and fees)?***

Cash Flow is certainly always nice, but if you do not plan to rent an apartment for

many years, as in the case of financing a transaction, this aspect becomes absolutely irrelevant. Even if in the year after the construction is completed, while the apartment is rented out, you have a negative Cash Flow, the financing will not significantly reduce the return on investment. If you are focused on long-term lease and resale of real estate let's say in ten years, then of course you have to look for an option with a positive Cash Flow and naturally strive to get good financing. And there are such options, only they are no longer in Toronto but in cities located an hour's drive from Toronto.

Also, we should not forget that rental rates go up by leaps and bounds, and where Cash Flow is not available today, it will appear tomorrow. Even for those who are looking forward to a long-term lease, I want to remind that the profitability of the investment from the apartment leasing is more than two times lower than in the years of construction.

Yes it is certainly less tedious; you do not need to sell anything and buy a new one, but is it worth it? I advise you to resell and, even better, refinance, in order to collect all the invested money from apartments in a year or two after the end of construction. As a rule, having turned such operation on the received money you can get even two apartments at a stage of excavation.

***5. What is a guaranteed lease from a developer?***

Recently, in some places with an acute shortage of rental space, especially for real estate located in close proximity to universities, there are projects where the developer guarantees the buyer-investor a rent for several years upon completion of construction. This means that the investor who buys an apartment at the stage of excavation at the end of construction begins to receive monthly payments from the developer, which correspond to the rental amount for this apartment. This amount is prescribed in the contract at the time of signing the contract when buying an apartment at the beginning of construction.

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