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Making rental development profitable

Centurion Asset Management CEO **Greg Romundt** tells *WP* why he believes rental developments are the next smart play in real estate

THERE'S A new real estate boom coming to Canada, but it's not centred on condos. It's being driven by perhaps the least sexy part of the housing market: rental apartments.

"As an industry nationally, we're going to build as many apartments in the next 10 years as we've built in the last two generations," says Greg Romundt, president and CEO of Centurion Asset Management. "We're very bullish [about rental apartments]. That's where we think the biggest opportunity is and what we're most excited about."

According to Romundt, a confluence of factors is driving demand for rentals, pushing rents to a place where rental developments are profitable again. The first is immigration, which is causing demand for rental housing to far exceed supply. There's often a false logic that dominates among investors and developers: that newcomers to Canada will buy property even before they land. But Romundt says that while the immigrant experience might result in homeownership down the road, at least during the first few years of settling in, most immigrants rent.

The second trend is regulation. Government actions to prevent a runaway housing market where buyers can purchase with no money down have increased the barrier for ownership, forcing more people to rent.

The third trend is millennial demand. As a generation, millennials tend to value experience over ownership, preferring to live in downtown cores where they can't afford to buy. They're marrying later, if at all, and having fewer kids. Renting facilitates the lifestyle choices many millennials are making.

The fourth trend is age. Greying baby boomers are realizing they don't need the big house in the suburbs now that the kids have moved out. Instead, they're looking for a hassle-free rental property after cashing in on their home, maybe even spending half the year somewhere warm.

"As an industry nationally, we're going to build as many apartments in the next 10 years as we've built in the last two generations" Greg Romundt, Centurion Asset Management

"We've got a lot of old rental product in this country, and there's only so much you can do with it," Romundt adds. "Not everyone wants to live in a renovated 50- to 60-year-old apartment. There are lots of people who are willing to pay a little bit more for brand-new buildings with higher levels of amenities closer to transit."

Centurion is betting on this confluence of factors to drive demand for rental stock. Through Centurion Apartment Real Estate Investment Trust, Centurion is investing in a portfolio of existing rental apartments in Canada and the US. It's the new rental developments that Romundt is most excited about, though, which the firm invests in through Centurion Real Estate Opportunities Trust.

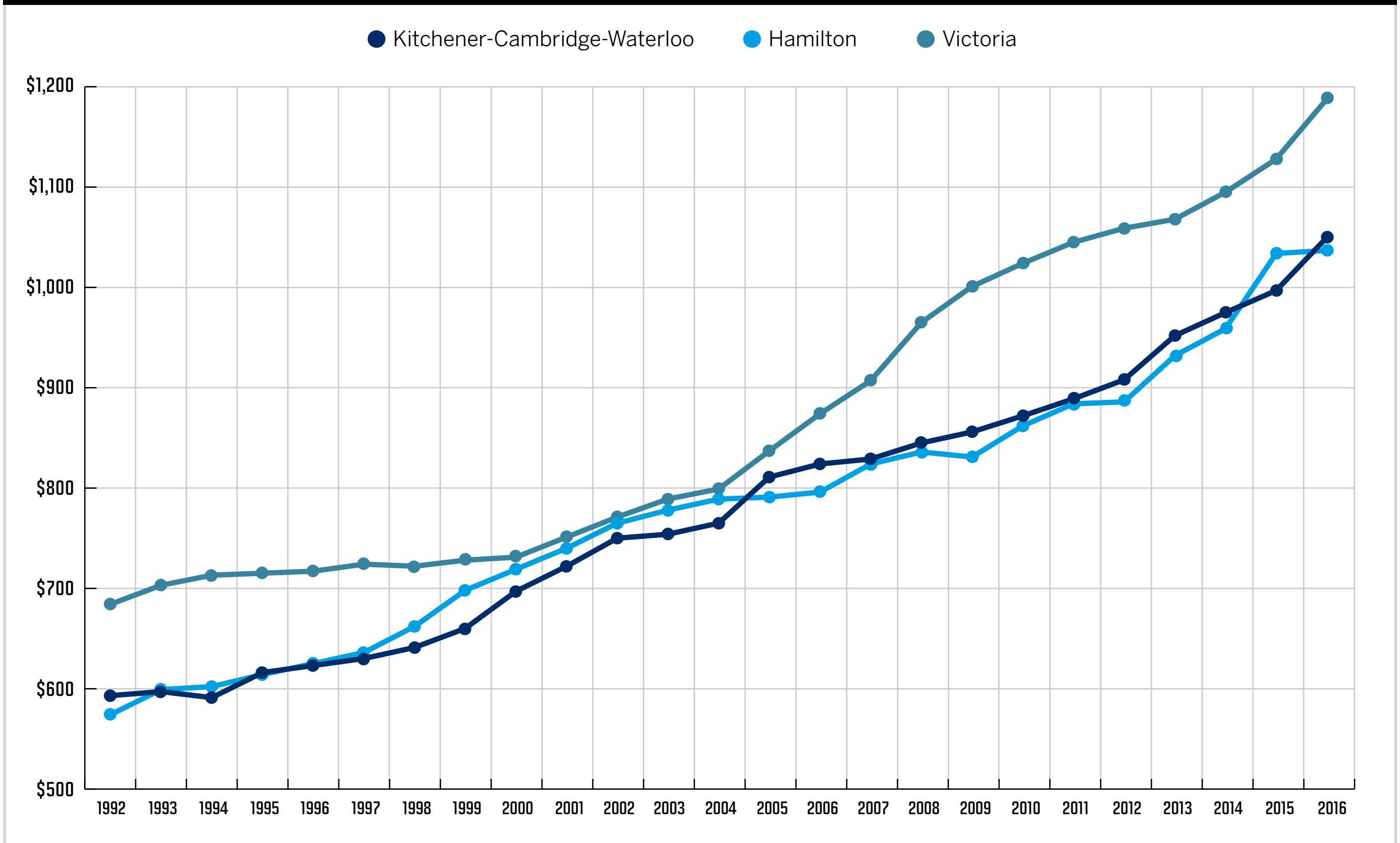
Both trusts are designed to offer investors returns from investments in rental housing. The aim is to provide individual investors with monthly income, diversification and solid annual returns. It's an ambitious play, but Romundt has come up with a strategy to realize those ambitions.

"We want to be investing our capital where we think people are going," he says. "Boiled down, we're looking at the exurbs of 'MTV' [Montreal, Toronto and Vancouver]."

Romundt explains that urban centres, especially in Toronto and Vancouver, are still too expensive to drive profitable rental developments. Condos remain king, and a developer can make more by selling condos than they could by building rental stock. This means that a successful strategy needs to step outside those city centres.

"Look at Hamilton," Romundt says. "Hamilton has just gone through this explo-

RENTS ON THE RISE IN THE CANADIAN EXURBS



Source: CMHC Rental Market Survey

sion in the last five years. I think part of that is because people are buying into it who couldn't buy into Toronto."

Romundt is also looking at where the momentum is heading, taking into account the factors that come along with movement to the exurbs, including more jobs, rising incomes, low vacancy rates and rising rents. Combinations of these factors make a city an appealing investment opportunity.

In Ontario, that means locations like Kitchener, Cambridge, Waterloo and Aurora. In BC, it's Victoria, Burnaby, Abbotsford and Surrey. Montreal is something of an exception with its lower property values, though they're set to rise. Anticipating growth, Centurion is investing in new developments and rental stock in the city of Montreal proper.

Centurion's other screen is partnership. The company doesn't scope out sites and build them, but rather invests with solid development partners, providing those developers with expertise on suite sizes, suite mix, location, pricing and amenity packages.

"We allow them to bring their building skills, and we can provide debt and equity management," Romundt says. "We provide the skills that we have in-house, and they bring the skills that they have."

When Centurion turns down a deal, it's often because it doesn't see a good fit with the partner – Romundt is as careful about who he goes into business with as he is about where he's investing. Even if the potential partner a solid builder, the two firms might have misaligned goals.

Romundt is confident about the forces driving demand for rental housing. He thinks rentals will always be the lowest-volatility sector in the real estate field because of a core need for housing. Even if prices go down, despite the fundamental tailwinds driving them up, this core need will keep smart investments in good locations paying dividends.

"When I look at apartments, I say, 'We have 400,000 new people per year we've got to provide housing to,'" he explains. "The tailwind is exceptionally strong. I know with virtual certainty that because of that imbalance, if I can build a property, I'll be able to fill it. Now, I might not get the dollars that I want right away. So instead of getting $2 a foot, I might get $1.80 on lease-up. I might not make the returns that I want on the desired time horizon, but we know that the demand drivers are just never going away and we'll get there eventually." **WP**