Why Canada is a land of real estate opportunity

For investors, the real estate market is truly global, but Canada deserves pride of place.

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Sophisticated investors know that the real estate market is global in scope, but success ultimately comes down to making good choices. When they do that, Canada should be on their investment map.

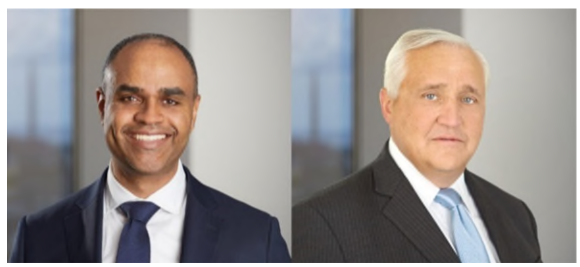
"From a demand perspective, Canada had the fastest growing population in the G7 over the last five years," says Ken McKinnon, Senior Managing Director, Head of Relationships, at Institutional Mortgage Capital (IMC), an investment fund manager and commercial mortgage lender that serves institutional and private wealth clients across Canada. "Real estate growth is expected to continue over the next five to 10 years to support the previous population growth."

One big reason is immigration. Canada is one of the few countries in the world that has been actively seeking more immigrants, which is fuelling demand for real estate in both concentrated centres and the middle markets. Canada has added 2.9 million people in the past three years.

Developers are racing to keep up. For example, at the end of 2023 Toronto had 238 cranes on construction sites, nearly 200 more than any other city in North America. A series of projects now approved or underway in the city will leave it with seven new "supertall" (more than 300 metres high) buildings by 2030—the fifth largest concentration of mixed-use residential skyscrapers in the world.

New construction will deliver tens of thousands of units over the next five years, but that will not be nearly sufficient to meet the demand from new residents. Other types of real estate, such as grocery-anchored retail, student housing, storage facilities and industrial, will benefit from the population growth as well.

McKinnon and his colleague Robert Fitzpatrick, IMC's Senior Managing Director, Head of Core & Core Plus Investments, say the country's potential as a real estate market has more behind it than strong population growth. While the Canadian economy is expected to trail the United States in terms of growth this year, its underpinnings are fundamentally strong. That makes it attractive to investors who, like IMC, take a long-term view. "Canada came out of the 2008 recession with a strengthened global reputation," Fitzpatrick says. "Our financial system held up remarkably well relative to other developed countries, and Canada has come to be seen as a safe haven."



***Robust population growth and a stable financial system should support commercial real estate over the long term, say IMC's Ken McKinnon (left) and Robert Fitzpatrick*.**

Real estate investment also plays to the economy's strengths, Fitzpatrick adds. Canada is the world's second-largest country geographically, but its population centres are concentrated, which increases demand for property in the areas with the most people, jobs and industries, such as the Greater Golden Horseshoe Area (which includes Toronto) and British Columbia's Lower Mainland (which includes Vancouver). "From the East Coast to the West Coast, about 90 per cent of the population is close to the U.S. border," he adds, "and there are a few additional middle markets further away, such as Edmonton and Winnipeg, that are strong, too."

Other global markets, particularly the U.S., are larger and may be seen as more dynamic. But Canada compares favourably with them on a risk-adjusted return basis. That's in part because Canadian lenders are less numerous and more risk-averse than in the U.S., for example. "This helps make the Canadian market much more stable," Fitzpatrick says, "so when you compare a 10 to 15 per cent return in Canada to the U.S., the Canadian investment will be much less volatile. It's a smaller market than the U.S.—about 10 per cent of the size—but what we find is that it's far more secure."

The potential of the Canadian market is clear, but that doesn't make it an easy one for investors to navigate. Canada's size—small, compared to the nearby behemoth U.S.—is one barrier to entry. Also, the credit environment in Canada is more rigid than in some larger markets. "You generally have to put a substantial amount of equity into a commercial financing—a minimum of 25 per cent and up to 40 per cent," Fitzpatrick says.

Those characteristics, however, can also provide benefits, Fitzpatrick and McKinnon say. The IMC team, which has been together since 1998 and has originated more than 1,400 commercial mortgages with a total value of more than $14 billion, has certainly learned how to leverage the advantages.

"In a larger market, investors see one potentially lucrative real estate transaction and then you might get 30 lenders going after it," Fitzpatrick says. That contrasts sharply with Canada, where "we've got a relatively conservative and stable banking system, with six large financial institutions and a very strong insurance sector," McKinnon explains. And while rigid credit requirements can be a steep entry point, they also breed stability. "We haven't seen very much in Canada in the way of defaults or loan losses," he says.

Over the next 10 to 15 years, IMC sees mid-market lending as attractive. IMC does that through its Active Mortgage Fund and Real Estate Debt Funds, which have an average loan size of between $5 million and $10 million. (Its partner firm, IWS Equity, takes the same approach with its real estate equity funds.) Of course, to find the right opportunities, you have to know where and how to look for them. And experience matters. "Most international investors we speak with would love to invest in Canada but don't know how to do it," McKinnon says. "We've been successful here for 25 years. We're investing long-term in a strong market where we have experience."