

Compounding mishap a matter of interest in celebrating real-estate gains

Canadian Press

Monday, January 29, 2007

TORONTO (CP) - It seems impressive: a 264 per cent rise in Canada's average home price over 25 years - so impressive that it prompted the Re/Max real-estate organization to proclaim an 11 per cent average annual increase.

"Conventional wisdom used to be that real estate was a relatively safe, long-term investment that typically appreciates at a rate of five per cent annually. These statistics clearly tell a different tale," declared Re/Max executive vice-president Michael Polzler.

Actually, they don't.

Re/Max made a basic arithmetical error by computing a simple average, without taking account of the compounding effect that annual increases have as they are added on top of one another.

After media inquiries, Re/Max issued a clarification: "Nationally, the compounded annual rate of return is 5.3 per cent" - which confirms the conventional wisdom.

The biggest local annual compound growth rate that Re/Max tracked, in Barrie, Ont., was 6.4 per cent, while the smallest was in Regina at 3.6 per cent - which after property taxes and maintenance costs rounds to something close to zero, not counting mortgage interest and inflation.

"Home ownership has always been more of a necessity of life than an investment vehicle," Polzler clarified.

"The percentage increases that have occurred across the country over the past 25 years show that real estate is also a solid investment."

Of course, even this assessment might need clarification for those who bought at the previous property-market peak in 1989.

For example, someone who paid that year's Canada Mortgage and Housing Corp. estimated average price of \$147,000 for a Canadian home, then watched its value plummet in the mid-'90s before reviving to the Re/Max estimated 2006 price of \$277,000, would have a 17-year gain of 88 per cent - representing a compound annual growth rate of 3.8 per cent.

So add "timing, timing, timing" to the old real-estate adage about investing in

"location, location, location." In Toronto, after its exuberant 1980s bubble, the annualized 1989-2006 gain from \$273,000 to \$352,000 was just over one per cent.

© The Canadian Press 2007

CLOSE WINDOW

Copyright © 2007 CanWest Interactive, a division of CanWest MediaWorks Publications, Inc. All rights reserved.