

POSTED ON 28/04/07

PORTFOLIO STRATEGY

## Alberta real estate: This boom may never go bust



ROB CARRICK

Alberta real estate is quite the investment.

Homeowners in the province know that, and so do shareholders of a few Alberta real estate companies and REITs, or real estate investment trusts. Take apartment landlord **Boardwalk REIT** - it's up 88 per cent in the past 12 months and a total 175 per cent in the past three years. Or how about land developer **Melcor Developments Ltd.**? It surged 44 per cent in the past year, and 504 per cent in the past three years.

There are signs that the Alberta real estate market is cooling a little after an absolutely insane year in 2006, which raises the question of how much more upside these stocks have. The answer from veteran real estate analyst Frank Mayer of Desjardins Securities: plenty.

Mr. Mayer said the value of Alberta real estate reflects the province's economy, which has been the strongest in the country by far of late and should continue to do well. "Alberta won't necessarily be the provincial leader in economic growth every year, but over the next five years it should do pretty damn well," he said.

**Print Edition - Section Front**



[Enlarge Image](#)



The Portfolio Strategy column has previously investigated the benefits of investing in Canada's most economically strong province through an Alberta Portfolio of stocks and mutual funds. The most recent version of the portfolio was created Oct. 2 and has gained 21 per cent, which compares with 15 per cent for the S&P/TSX composite index.

In a report he wrote this month along with colleague Jeff Roberts, Mr. Mayer makes a compelling case for focusing on Alberta's real estate market. Here are the five stocks he highlights.

Boardwalk, which has half of its 35,000 apartment rental units in Alberta, where average market rents rose by 40.5 per cent last year.

Melcor, a developer that was founded in 1923 and has been profitable for 18 consecutive years.

**Genesis Land Development Corp.**, which is a developer of what Mr. Mayer describes as prime development land in and around the city of Calgary.

**Artis REIT**, which owns office, retail and industrial properties in Alberta and other western provinces.

**Mainstreet Equity Corp.**, which buys underperforming apartments and townhouses and has almost two-thirds of its portfolio in the Calgary and Edmonton areas. (Full disclosure: I have bought Mainstreet and Melcor in the past six months.)

With the exception of Boardwalk, these stocks aren't much followed by other analysts and have next to no profile with investors. Mr. Mayer said this is because of the fact the Alberta base of these stocks is far from Bay Street, and that these are comparatively small companies that don't generate big trading volumes.

There's an element of risk in these stocks because of their lack of size and liquidity, but a bigger concern may be that the boom cycle in the Alberta real estate market could turn to bust. It's happened before.

Following the 1973 Yom Kippur War in the Middle East, soaring world oil prices caused a surge of economic activity in the province. Here's a telling factoid provided by the CBC on a website accompanying its *Canada: A People's History* TV series: At the peak of Alberta's boom, the value of building permits issued by the city of Calgary topped New York and Chicago. A global economic recession and falling oil prices ended the party in the late 1980s, leaving Alberta with the highest levels of house foreclosures and bankruptcies in the country.

Mr. Mayer was just beginning his career as a real estate analyst back in the early 1970s, and he says he recommended several Alberta-based real estate companies. "Having gone through that period, having seen the boom and then the bust, one can't help but ask, what are the parallels to the current situation," he said.

His conclusion is that another real estate bust in Alberta is unlikely. For one thing, low taxes in the province should help sustain economic growth. Oil is another factor. Whereas the economics of oil collapsed in the early '80s, today demand is too strong and supplies too tight for that to happen. There's also the economic activity created by Alberta's oil sands, which have become much more significant than they were decades ago.

Alberta's economic growth rate of 6.8 per cent last year was three times the national average. A provincial economic forecast produced earlier this year by Toronto-Dominion Bank said Alberta will lead this country again this year, though by less of a margin, and then fall behind a few other provinces in 2008. Still, TD sees Alberta leading the country in such key areas as job growth and retail spending.

There's a similar outlook for Alberta's residential real estate market - not as hot as 2006, but still strong. "We expect both [housing] starts and existing-home sales to decline from the record levels experienced in 2006, yet remain among the highest in history," Canada Mortgage and Housing Corp. said in its first-quarter housing market outlook.

This brings us back to those five Alberta real estate stocks, all of which are still rated "top pick" by Mr. Mayer and Mr. Roberts. Each in its own way benefits from strong market conditions for homes and commercial properties in the province.

The story at Boardwalk and Mainstreet is a tight rental market that, according to CMHC, drove the vacancy rate in urban centres to a record low of 0.9 per cent last fall from 3.1 per cent a year earlier. Boardwalk is capitalizing on this by raising its rents steadily, but Mr. Mayer said the current average market rent is still well below the level that would justify building new apartments. Late-breaking note: Rules announced this week reduce the number of times a year that a landlord can raise rents to once every 12 months from once every six months, but outright rent controls were not introduced.

Melcor, which Mr. Mayer describes as "the quintessential Alberta real estate play" and deserving of a "must-own appellation" is a developer of land for single-family homes, larger residential projects and commercial real estate. Mr. Mayer estimates that the net asset value of Melcor's properties will rise by almost 28 per cent over the next 12 months, and that earnings per share will rise by a similar amount.

Genesis Land Development is a direct play on the Calgary real estate market, including residential housing. Resale housing prices in the city averaged a staggering \$415,321 in the first quarter, but Mr. Mayer cited a recent study by Royal Bank of Canada showing that affordability for buyers is not out of whack. Judging by the amount of pretax income needed to service the cost of mortgage payments, property taxes and utilities, RBC found that Calgary ranked behind Vancouver, Toronto and Montreal.

For a play on commercial real estate in Alberta, Mr. Mayer suggests Artis REIT. Artis gets more than two-thirds of its operating income from the province, and it will have significant opportunities to raise rents this year and next.

Confronted with the kind of gains these stocks made in the past couple of years, an investor would be justified in believing that the big money has already been made. Mr. Mayer noted that Melcor's share price has risen seven-fold in the past five years, but that doesn't faze him. Back in the last boom, he recalls, some Alberta real estate stocks rose by 50 times from bottom to top.

Mr. Mayer isn't forecasting similar gains this time around, but he does see significant upside for the likes of Melcor. With his calculator clicking in the background, he reels off a series of factoids about how much Alberta land prices have increased already and what this means for the future. His conclusion: "This is going to continue for a number of years."

\*\*\*\*\*

## **Land, Ho**

As goes Alberta's booming economy, so goes its real estate market. How can investors play this trend? Here are five Alberta-focused real estate stocks and real estate investment trusts that have been selected by analysts at Desjardins Securities as having significant upside potential. All are listed on the Toronto Stock Exchange.

### **Artis REIT**

Profile: Owns office, retail and commercial real estate in Western Canada, with a focus on Alberta.

Share price as of April 26: \$17.25

Desjardins' 12-month price target: \$18.80

Implied upside: 15 per cent (including yield on distributions)

### **Boardwalk REIT**

Profile: A major apartment landlord, with more than half of its 35,000 units located in Alberta.

Share price: \$45.20

Desjardins' 12-month price target: \$56.60

Implied upside: 28 per cent

### **Genesis Land Development**

Profile: A developer of land in the Calgary area

Share price: \$6.47

Desjardins' 12-month price target: \$11.25

Implied upside: 74 per cent

### **Mainstreet Equity**

Profile: Buys up underperforming apartments and townhouses and then renovates them.

Share price: \$18.36

Desjardins' 12-month price target: \$26

Implied upside: 42 per cent

### **Melcor Developments**

Profile: A developer of single- and multiple-family properties as well as commercial projects in the Alberta market.

Share price: \$28.61

Desjardins' 12-month price target: \$39.40

Implied upside: 38 per cent

*SOURCE: THOMSON DATASTREAM*

© Copyright 2007 CTVglobemedia Publishing Inc. All Rights Reserved.

**CTVglobemedia**

globeandmail.com and The Globe and Mail are divisions of CTVglobemedia Publishing Inc., 444 Front St. W.,  
Toronto, ON Canada M5V 2S9  
Phillip Crawley, Publisher