

# Intentional Apartment Developer

A Programmatic Guide for  
Planning, Designing, Building,  
Leasing, Managing, and Selling

**DEREK LOBO**

*produced by*

**APARTMENT**  
University

# Advanced Praise



“Apartment supply is important for our country. Derek Lobo has assembled a resource that aims to help developers in their efforts to pivot to apartment development.”

**Mark Kenney**

President and CEO  
CAPREIT

“I wish I had this book before I built my first apartment, but I had access to the author, and he’s guided me through multiple successful apartment developments.”

**Rob Piroli**

President  
Piroli Construction

“I have known Derek since he launched his first business in 1986. Over these 35 years, he has earned a reputation as the “go-to apartment expert” in Canada. *The Intentional Apartment Developer* is a compilation of decades of his know-how and will definitely be helpful to apartment developers and the real estate fraternity.”

**George Przybylowski**

Vice President, Real Estate  
Informa Canada

“*The Intentional Apartment Developer* is a complete guide to all the topics needed to be considered when developing an apartment building. In this big puzzle with moving parts, Derek and his team helped us ask the right questions and make quality decisions.”

**Oren Vered**

President  
Vared Group

# The Intentional Apartment Developer

Derek Lobo

Produced by Apartment University

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# Dedication



I dedicate this book to all the courageous men and women  
who put it all on the line to build rental apartments.

These people are my heroes!



# Table Of Contents



Advanced Praise • iii  
Other Books by Derek Lobo • iv  
Dedication • vii  
Table Of Contents • ix  
List of Figures • xi  
Before We Get Started... • xiii  
Acknowledgements • xix  
Foreword • xxi  
Overview • xxiii  
Introduction • xxvii

## **PART 1: What to Build • 1**

The Feasibility Study • 3  
Rental Apartments by the Numbers • 19  
Apartments of the Future • 37  
Reducing Municipal Taxes and Operating Costs • 57

## **PART 2: Land • 77**

Finding and Acquiring Land • 79  
Intensifying Existing Developments • 99

## **PART 3: Financing the Building • 117**

Finding Money • 119  
Building with a Joint Venture Partner • 137

## **PART 4: Filling Up the Building • 165**

The Marketing Plan • 167  
The Sales and Leasing Plan • 183  
The Four Factors That Drive Rent • 205

## **PART 5: Selling Your Apartment • 221**

The Merchant Builder • 223  
The Big Question • 233  
Intergenerational Wealth • 247  
Epilogue • 255  
My Notes • 257

# Setting the Stage

Next, I want to share some concepts that will set the stage for your journey forward so you can better understand my mindset and motivation. My success in business is all about providing an **Apartment Development FULL Service Experience™**. This consists of two key ingredients:

1. Being available
2. Adding value

**Being available** is accomplished by “staying in traffic” (a term I often use) and remaining easy to connect with. **Adding value** is the glue that creates a mutually beneficial relationship and keeps clients coming back to the experience you provide them.

**Apartment Intelligence and Leadership** is our motto, and we do this through seven essential elements. We’ll cover these in more detail later.

**We transact apartments, and much more...**

Apartment & Land Brokerage  
Feasibility Studies  
Consulting  
Education  
Coaching  
Events

**APARTMENT**  
Intelligence & Leadership

*for*

New Apartment Development  
Purpose-built Apartments  
Affordable Housing  
Student Housing  
Intergenerational Family Real Estate  
Office Conversions to Rental  
Mid Market  
SFR / BFR

Figure 0.1 - Rock Advisors - What We Do

I value and appreciate the success I have realized to date and continue to create for others. Our team is filled with like-minded individuals who are focused on our niche industry. Most prototypical brokerage firms are broad in scope and narrow in providing a unique client experience. From the outset, I have been laser-focused on the apartment industry. Today, we have in-house capabilities that include research, underwriting, lease-up, custom content creation, marketing asset production, publishing, interactive webinars, live-event production, and brokerage.

What do I mean by an **Apartment Development FULL Service Experience™**? It is a beginning-to-end process—from the inception of the new apartment construction project, all the way to the end—which could be the setup of ongoing asset management or the sale of the asset.

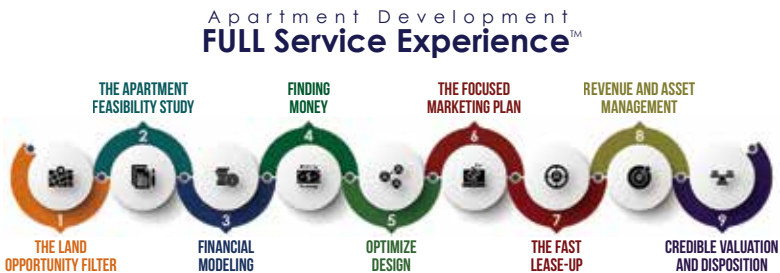


Figure 0.2 - Apartment Development FULL Service Experience™

This **Apartment Development FULL Service Experience™** was designed for three important reasons:

1. Help you make more money
2. Arm you with insight to avoid pitfalls that cause developers to lose money
3. Bring together resources to execute best practices

If you're reading this and perhaps thinking, "This guy is just selling me his business," you're right. But here's the real message I want you to take away: at the end of the day, you

can gain your experience by learning from your own mistakes and victories, *or* you can leverage the wisdom of decades of hands-on knowledge, strategy, and tactics, and immediately deploy that wisdom and knowledge on your very first (or next) project! There is no need to wait while you learn from your mistakes and develop your personal experiences.

Like many other businesses, apartment development success is greatly enhanced by “who you know,” which relates back to my earlier statement about “bringing together resources to execute best practices.” My business has flourished because of long-lasting, intergenerational, and mutually beneficial relationships, which is the result of working with clients from the early stages of their vision all the way through to completion and/or sale.

Collaboration is key. I have learned from my mentors that sometimes perceived competitors can be ideal collaborators when you both share the same “hero.” What’s important to note is that collaboration doesn’t involve the exchange of money. When combining resources and talent, powerful results can be attained by working with others to achieve a common purpose and serve the same end-client. I love to collaborate, and it has yielded many opportunities and benefits!

## **Learning On Demand**

One more item before we get started, and I’ve saved the best for last. I am personally excited for the future-based focus we’ve developed. Part of that focus has resulted in the creation of our new online learning portal, *Apartment University*, which can be found at [derek-lobo.com](http://derek-lobo.com). This project is the result of assembling our collected amortized knowledge and presenting it in a skills-on-demand and lifelong learning platform. Learning has been siloed for such a long time, but



today we have the technology to multiply the educational experience for anyone.

We have deployed a modern Content Management System (CMS), also known as a Learning Management System (LMS), and assembled an industry-first tool that is invaluable to the aspiring apartment developer. This learning portal is aimed specifically at the needs of new apartment developers, developers who are pivoting to apartments, affordable and student housing developers, and many other sectors that support the apartment development process (research, financing, marketing, leasing, staff development, etc.). These needs are filled and delivered through:

- Courses
- Videos
- Interviews
- eBooks
- Business tools
- Webinars
- Events
- Coaching
- Skill development
- Industry strategy and insight

I personally want to invite you to explore *Apartment University*. Check it out for free and explore this resource—there's no other like it anywhere!



Figure 0.3 - Apartment University Learning Portal

# Starting the Journey

I want to be your ROCK ADVISOR: a solid voice of wisdom, strategy, and focus. I appreciate the time you are dedicating to absorb this book. Dig into these pages—mark them up, dog-ear the corners, highlight key points that resonate with you, and extract the value contained within. And don't forget to claim your free gift, which I shared earlier.

To begin this journey together, I invite you to turn the page and take the path, step-by-step, through *The Intentional Apartment Developer*.

# Acknowledgements



A project, such as this, does not happen on its own or without the collective efforts of a team of like-minded, focused people! With that in mind, I need to thank those who've been directly and indirectly involved in the creation of this endeavor.

It all starts with our Rock Advisors team, who pull together the content, expertise, knowledge, relationships, and skills to make my vision a reality. They are the gears of the machine that creates, markets, and sells.

Of course, none of this would matter if it weren't for our clients and collaborators! They are the visionaries of the apartment development industry, and I am eternally thankful for their business, trust, and friendship.

I also wish to extend my appreciation to Dan Sullivan, whose mentorship and friendship have been pivotal in shaping my strategic thinking and opening new avenues for me to explore both at work and at home.

Thank you all!

# Foreword



News of the scarcity of rental housing has never been more prominent—for good reason. Rental housing is crucial for many people in our society: immigrants, young people, families, foreign students, and seniors. It's vital to serve these groups for the well-being of society and our country. Our economy cannot grow if there is an absence of affordable housing. According to a 2018 Statistics Canada survey ([150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=1110000801](https://150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=1110000801)), 73 percent of the Canadian population earns less than \$50,000 before taxes. As some of the nation's largest rental housing providers, we believe that supply is the key to a healthy and sustainable rental market.

For more than three decades, we have seen Derek become a leader in the apartment industry, and an advocate of new apartment development. *The Intentional Apartment Developer* is a road map for becoming an apartment developer.

This book serves as a guide for developers who want to build rental apartments. If you're an experienced developer, there are many valuable lessons contained in this book. If you're new or pivoting to apartments, this book is for you.

Our wish for you, the intentional apartment developer, is to fully embrace the social and economic significance of this important and impactful journey.

**Mark Kenney**  
President and CEO  
CAPREIT

**Bob Dhillon**  
President and CEO  
Mainstreet Equity Corp

**Philip Fraser**  
President and CEO  
Killam Apartment REIT

# Overview



Historically, multifamily development has been the best opportunity for a developer seeking both short-term capital gains and longer-term wealth creation. With the information in this text, developers—especially first-time developers—can take full advantage of this opportunity.

We have assembled a comprehensive suite of resources: the original *Apartment Developer University* webinar series, the *Apartment Developer University* 13-book series, and the resources available at our learning portal: *Apartment University* at [derek-lobo.com](http://derek-lobo.com). Together, they help equip multifamily developers with the necessary knowledge, advice, skills, and proven processes to successfully compete in the marketplace.

These resources will change, or add to, a developer's perspective on building apartments, enabling them to confidently serve their customers and become successful programmatic (according to a program or defined method) builders.

## The Hero Builder

We've always been fascinated by the first-time apartment developer who one day risks everything to develop a specific piece of land to fulfill a vision. That individual commits financial resources, personal covenant, and a huge investment in time to build a multifamily development. It is, however, that first apartment building that opens up an opportunity to grow into a successful merchant apartment builder.

*The Intentional Apartment Developer* is about this hero. It's about creating a bigger, better, more exciting future, with reliable, actionable strategies that lead to successful development.

## Our Mission

Typically, a developer who has experience in other asset classes has 90 percent of the skills needed to become a successful apartment builder. Our mission is to enable that developer to access the key remaining 10 percent. We can teach the developer how to think, communicate, take action, achieve results, and pivot existing skills into becoming a successful, vertically integrated builder.

This book is specifically targeted to new apartment developers, their staff, and the commercial real estate fraternity that supports them. We have a team of dedicated professionals who can facilitate planning, feasibility, financing, design, and ultimate disposition of apartments. By becoming a well-informed apartment developer, it is possible to leave behind the competition of the cyclical asset classes and enter an in-demand asset class where the wealth stays with the developer and the business for years to come.



Figure 0.4 - A Developer of Developers - It's Who We Are

The “why” behind building apartments always comes back to the developer’s family and legacy. It’s about wealth preservation, tax deferral, and cash flow. And the reason this all works is that rentals are the best way for a real estate family to transition wealth from one generation to another.

We want developers, their families, and future generations to enjoy the fruits of sound financial planning to enable a smooth transfer of their hard-earned assets for a bigger and more exciting future.

## The Fundamentals of Success

The following chapters introduce developers to the principles and fundamentals necessary to begin, develop, lease-up, and sell or keep a viable project. We encourage developers to explore our learning portal for in-depth presentations of pertinent topics led by leading industry experts. It also is a chance to meet other developers just like you.



In our experience, developers love meeting other developers. Our conferences and field trips provide developers the opportunity to share experiences and common best practices in a stress-free, supportive atmosphere. Along with our other resources, such events prepare developers to build confidently, face challenges successfully, avoid the pitfalls that may cause them to lose money, and ultimately, complete projects that meet the developer’s original financial and personal objectives.

# Introduction



This book contains a wealth of information. It's a compilation of over 30 years of amortized knowledge solely focused on building wealth through apartment development. By combining those years of experience with our proven, unique processes and dedicated teams of professionals, a developer can take advantage of an asset class that has long-term stability and profitability, and be on the way to building a successful, wealth-generating business. We strive to fully inform the developer so they become an “apartment scientist.” With our teams taking care of the details, they're free to focus on building a business that programmatically builds successful rental apartments time and time again.

## **Our Apartment Development FULL Service Experience™**

This book is really our Apartment Development FULL Service Experience™, beginning with an apartment's conception to either its final sale or long-term ownership, and organized into distinct stages that are easy to understand.



# Apartment Development Full Service Experience™

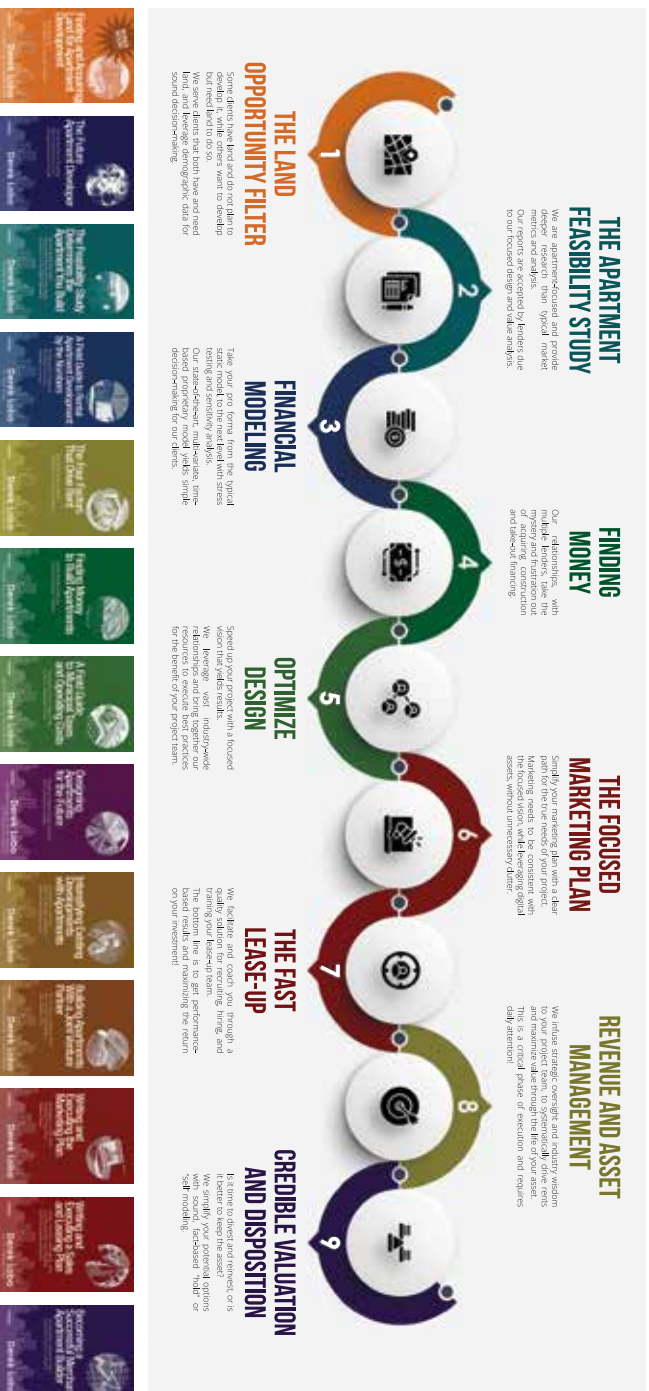


Figure 0.5 - Apartment Development FULL Service Experience™ - Detailed

Our relationship with the developer begins early in the process. Often, we are one of the first professionals they engage. Our goal is to determine whether a potential project can be developed into a profitable investment. We evaluate where they can expect the highest rents, where demand is highest, and where municipal taxes are lowest. We then proceed to an opportunity study, using in-depth demographic and economic data to help pinpoint the best opportunities.

From there, we prepare a project feasibility study. Many times, it's at this stage that developers come to us. They may already own a piece of desirable land or wish to buy one, but aren't quite sure how, or if, to proceed.

It's at this point we can provide the clarity needed for decision-making. If based on our experience we don't think a deal is viable, it's a free, fast "no." If we think a project is viable, then the developer should proceed with a financial feasibility study, which will show how the deal pencils out using a variety of metrics such as development yield and initial rate-of-return (IRR). Later, we can arrange for a joint venture (JV) partner. In our experience, most developers know how to get construction financing, but finding mezzanine and equity financing (when needed) is a bigger challenge. If needed, we will connect developers with potential mezzanine and equity financing partners.

Working with the design team, architects, landscapers, and interior designers comes next to ensure the developer is designing a building that will get them the highest rent possible. Many of the decisions such professionals make are based on our feasibility study. Since we know what the resident profile looks like—whether it be young urban professionals, affluent seniors, or singles—design decisions based on the potential renters' needs can be made.

At this point, actual construction begins. While that proceeds, we will continue to write and execute a thorough marketing plan, which began when the hoarding went up. We compile a priority waiting list—that part is vital. Once the marketing plan is done, we'll begin the initial lease-up phase. That means hiring, training, and managing the staff for the actual lease-up after certificate of occupancy.

Developers who hold on to their buildings often decide to continue working with us on a consulting basis to help manage their properties. That usually means advice on rental rates and taking steps to minimize turnover. If the developer is a merchant builder, we may proceed to the broker stage and sell the building.

## **Why Apartments?**

Why not focus on retail or single-family homes? Isn't that where the traditional money is made? To get to these answers, we must look at the big picture.

The dot-com bubble (and consequent bursting), the financial crisis of 2008, and the COVID-19 pandemic caused much uncertainty in rental markets. However, apartments have historically been decoupled from the ebb and flow of economic cycles. Rental apartments are often the first sector to recover after an economic downturn—this was the case following the 2008 financial crisis. Today, if we look closely at rental market conditions, we'll see that the underlying factors are still very favorable. In short, rental markets have a very bright future.

Over the past decade, new A-Class (top of the market) buildings have created a sweet spot. From the investors' point of view, investors and pension funds have money available and are underweighted in rental apartment buildings. They've come

to realize that apartments are a stable asset class, despite changing economic conditions.

## **What If You're a Renter?**

Across North America, there's a shortage of high-quality rental units (in some areas). From the renters' perspective, it means they must wait longer and pay more. We don't see this situation changing anytime soon.

In many markets, changing demographics and rising homeownership prices often create conditions where consumers look into high quality rental options over home purchases. We think that this will drive the rise of the rental market, further informing developers that their number one priority as entrepreneurs should be to seek out those opportunities and capitalize on them.

## **The Apartment Builder's Legacy**

Institutional investors do not want to buy buildings designed and built in the 1950s, '60s or '70s. None of these are buildings that current renters want to live in. Buyers and renters are looking for up-to-date apartments, which look like high-end office buildings on the outside and condominiums on the inside. Apartments built this way command the highest rent, the highest net operating income (NOI), and lowest cap rate.

In addition, interest rates have been at an all-time low for the past few years and are likely to remain low into the foreseeable future. This means there are financiers ready, willing, and able to invest in new buildings and developments—we just need the developers to build them.

## A Perfect Storm

Let's put all this information into perspective. We know the single biggest expense when developing an apartment is the cost of capital. Over the past few years, financing costs have been at an all-time low, quality renters are plentiful, and financiers have money.



*Together, this has created a perfect storm.*

## Becoming an Apartment Scientist

Our company's mission is to help developers gain the confidence to proceed to a successful project. Apartment development has a long, bright future. With our help, condominium, industrial property, hotel, and shopping center developers can position themselves as programmatic builders. This opens up an opportunity to create a new business within an existing one that will protect their wealth, create a steady stream of cash flow, and defer taxes through depreciation.

## Start with the End in Mind

In anticipation of building and keeping (at least some) of the apartments built by a developer, we coach their estate for an efficient transfer of assets to the next generation. If they'd rather become a merchant builder, we want them to think about their legacy. (Merchant builders, also referred to as merchant developers, are those developers who build properties and sell them rather than holding on to such properties for extended periods.)

We have created our process so that the aspiring developer can become a successful apartment developer/owner or a

successful merchant builder. We've been able to do so based on decades of relationships, hands-on experience, writing books/publications, executing seminars/events, and our business process that connects developers with competent industry resources and experts.

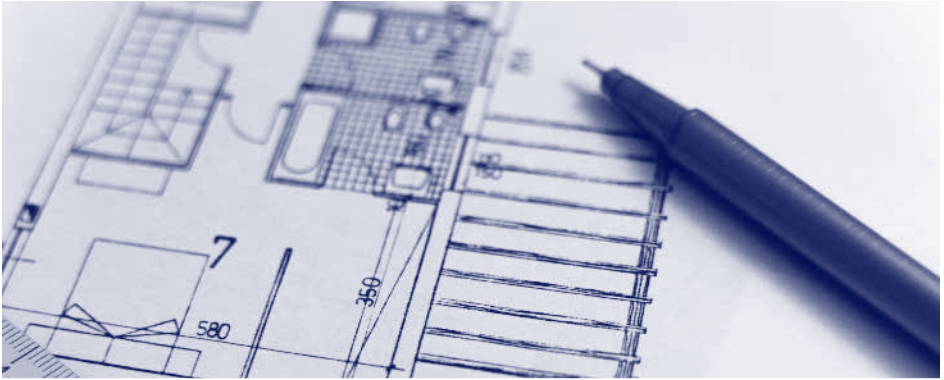


Take a moment to think about the home-building market of the 1960s and '70s. Most cannot name any of the builders from that time. However, these businesses are mostly still around and active in the industry. The companies that have been passed on to children and grandchildren are all benefiting from a stable, rental income because rental buildings are all about wealth creation, not short-term business income. As a result, those buildings have become the builder's legacy.

*Apartment buildings build wealth.*



Changing a builder's focus from short-term income to long-term income is not difficult. Once apprised of the knowledge contained in the *Apartment Developer University* book series (which is now part of our learning portal) and resources available through the *Apartment University* learning portal, builders will see the proposition of building rental apartments in a different light. They'll now have an opportunity to accumulate the know-how needed to take advantage of this asset class in the pursuit of their long-term financial and personal goals.

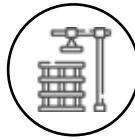


# PART 1: What to Build



# 1

## The Feasibility Study



Broadly speaking, a feasibility study is a technique used to assess a project's viability before the investment of invaluable time and resources. The aim is to objectively evaluate the strengths, weaknesses, opportunities, and threats of a proposed purpose-built rental project, whether it be through a sole developer or a joint venture partnership. The study provides the developer or development group, and potential investors, with the confidence that they're building the most profitable project for their specific site. The assessment is built on detailed demographic and economic analysis, combined with rental comparables. Ultimately, the most profitable building to develop will be the one that best meets the renters' needs. Though the developer's opinion is valuable, the overriding factor is where the data is leading them.

*A feasibility study is the foundation  
of a successful project.*



A feasibility study serves two different purposes. First, it's needed for internal decision-making. Without a good grasp of



the market, and the financials and potential outcomes, solid decision-making is next to impossible. Second, investors and lenders will demand a detailed study to assure themselves that the developer has thought the project through adequately and knows deep down that the project is viable and has sound data to back up those claims.

For a developer considering whether to build or not, the study answers five crucial questions:

1. Should they build?
2. What should they build?
3. What is the depth of the market?
4. How much rent can they charge?
5. How much will their building be worth after they build in order to either sell or refinance?

Once those answers are available, developers stand a much better chance of reaching their intended goals.

## Should You Build?



*For more on where you might build, see Chapter 5: Finding and Acquiring Land*

## What Makes a Good Rental Site?

**Four factors drive rent:** location, unit mix and sizing, amenities, and the property management platform.

While a developer can't change your location, they can choose to develop in a site that naturally appeals to renters. Renters aged 40 to over 50 desire close proximity to employment

and walking trails. They are typically less concerned with transit connections and rely on local and regional highway connections to commute. Many of these renters are downsizing and well into their established careers. They want access to commercial retailers and they don't want to increase commuting time, which means good highway access—plus they like eating out at restaurants.

Although interior amenities are important, community amenities are equally as important. A building doesn't exist in a vacuum, and neither do residents. The community amenities are what an individual is likely to require day-to-day. The closer these amenities are to the site, the stronger the site becomes for rental development. Community amenities include such things as availability of transit, parks, green space and outdoor recreational facilities, shopping, and health-care facilities.

A target renter will also desire specific social amenities. For example, young professionals want a varied and exciting nightlife, like bars, pubs, clubs, and theater. Also, since they commute to work, they need access to good transit. Though many seniors and retirees remain in the workforce, a majority are retired and do not commute daily. They're more concerned with having their daily conveniences within walking distance—amenities like cafés, restaurants, and parks—and having access to health-care services such as hospitals and pharmacies. This might sound a bit cliché, but ultimately when we study the reasons why older people downsize into apartments, we find that when they live in close proximity to those services, they're more comfortable.

Normally, when considering a new development, the developer is not targeting families. How can they expect a family to pay top-of-market rent for a two-bedroom apartment when that same amount will allow them to rent a house in a secondary market? Lower-density products in secondary and tertiary markets are better suited for children and families. These

families also need sports facilities and schools, which are not something found in dense urban environments.

## **Understanding the Different Markets**

There are five distinct markets: urban (city downtown), suburban/urban (outside of downtown but with significant development), suburban (cities near a large urban area), secondary (cities at a distance from large urban areas), and tertiary (small towns).

Development profit varies between those markets. A downtown (urban) high-rise has the lowest development yield, a suburban/urban mid-rise has a higher yield, and a low-rise in a suburban location has the highest yield.

## **Urban Versus Suburban Renters**

The young downtown urban renter sleeps in the apartment but lives in the building and neighborhood, whereas suburban renters live in the streets and play in their units (that is, they use the streets to drive places, but their home is where they spend their leisure time). By suburban renters, we also mean renters in secondary and tertiary markets.

Normally, smaller units are built in urban markets, the unit sizes growing as one moves outside of the downtown core. There, neighborhood amenities are scarcer, and residents spend more time indoors as those communities have fewer local amenities.

## **Secondary and Tertiary Markets**

Secondary and tertiary markets typically refer to suburban communities or municipalities that surround major markets.

Tertiary markets are typically smaller communities, many of which are towns some distance from larger urban centers. Because of their size, planning and zoning usually takes less time. These municipalities generally don't have the backlog that busier primary markets do. In addition, developers have more direct relationships with municipal planners, making negotiations easier. In combination, this makes development very attractive.

## Markets and Demand

Downtown sites have a proven market and demand, making financing easier to arrange. Incomes are generally higher with a greater percentage of renters versus those who will (or have) bought. However, competition for renters is intense. Land prices are also high due to competing developers and usage—whatever development may potentially offer the greatest return can achieve the greatest land value—especially in some specific local areas.

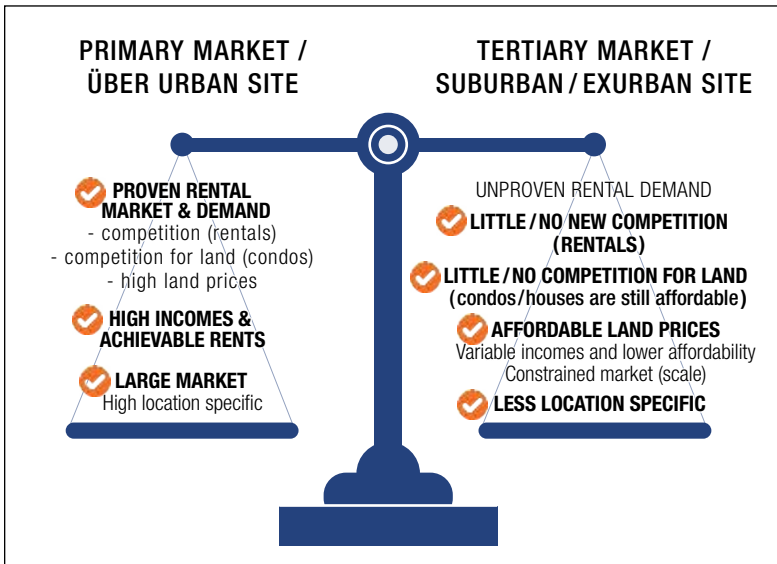


Figure 1.1 - Markets and Demand

In secondary and tertiary markets, demand for rental is often unproven, which means an extensive study to prove the existence of rental demand. Incomes are typically lower compared to a more urban location, with reduced affordability. However, this doesn't matter because land cost is lower, and a developer doesn't need to collect as much money per square foot to make a viable investment. Since the rental pool is smaller, a smaller development is adequate. And finally, since there is less new competition for renters, land and the specific location is less critical.

## **What Should You Build?**

Once a developer has decided on a building's location, finding out what to build becomes the priority. The feasibility study's objective is to uncover the details of a specific development site that affect viability and profitability. These details are specific to that site: current market conditions, current investor interest, and current potential renter availability. A developer can now position their development, so it stands above the competition.

## **Who Rents What?**

The first consideration is to identify who the target renters are. The way units are designed will be different based on the type of available renter.

UNIT TYPE	TARGET RENTER	
	Primary Market	Secondary & Tertiary Market
Bachelor	Students, shelter renters	AVOID
One Bedroom	25-35 y/o early career divorcees (minority), single downsizers	25-35 y/o early career divorcees, single downsizers
One Bedroom + Den	Roommates, divorcees, single downsizers	Divorcees, single downsizers
Two Bedrooms	Roommates, young couples (high income), older downsizers (minority)	Older downsizers, divorcees (high income), young couples (minority)
Two Bedrooms + Den	Roommates, older downsizers	Older downsizers, couples (minority)
Three Bedrooms	AVOID (but roommates)	AVOID (but older downsizers)

Figure 1.2 - Target Renters for Different Unit Types

Different renters have different priorities:

- Roommates want equity in bedroom size and bathroom access.
- Downsizers need storage, expect upgraded kitchens, and in-suite space to entertain.
- Younger residents need entertainment space as well but will consider common areas as a solution.
- Divorcees may want one-bedroom units plus a den.
- Families may want three-bedroom units.

The feasibility study will reveal the availability of each of these groups, along with household incomes, work and leisure habits, and age distribution. This makes unit design decisions easier.

## Materials, Finishes, and Amenities

Material choice, finish level, and amenities can depend on whether you're keeping the building or selling it.

How much amenity space should be built?



*Typically, we recommend between 15 and 25 square feet of functional interior amenity space be allocated per unit. Smaller buildings typically offer 20 to 25 square feet, while larger developments, which have the benefit of scale, can allocate between 15 and 20 square feet of amenity space per unit. Once this space is allocated, the developer needs to decide how it will be used and what proportion is ideal for each amenity.*

Buildings developed with long-term holding in mind typically provide more amenities because the developer wants the building to remain competitive with other local comparable properties over a much longer time frame.

Buildings developed for sale compete with the immediate market. There's less concern with the long-term viability of the project. These properties are designed to compete with the existing market and what's in the development pipeline.

Please refer to Chapter 13, "The Big Question," for a more detailed look at the "build-to-hold or build-to-sell" question.

## Phased Developments

Phased development makes sense under one of the following circumstances:

1. When the lot area allows for multiple buildings
2. When multiple buildings, leased over time, don't oversaturate the market

Though newer buildings compete with older ones, they also exist together, and because of their proximity, affect one another. The benefit is that amenities can be shared between the buildings, thereby maximizing rentable space.

## What Is the Depth of the Market?

If a market is reaching saturation, lease-up and absorption will be affected. A simple way to understand the depth of a given market is to look at the number of apartments per 100 people.

$$\text{RENTAL DENSITY} = (\text{RENTAL UNIVERSE} / \text{POPULATION}) \times 100$$

By adding the additional new units, a developer can determine the expected rental density and proximity to market saturation.

## How Much Rent Can Be Charged?

A proposed project's competition can be established with a thorough market survey. We concentrate on A-Class products, such as a condominium and a new high-quality rental product, and B-Class products that have been renovated to an A-standard even if it's in a B-Class building.



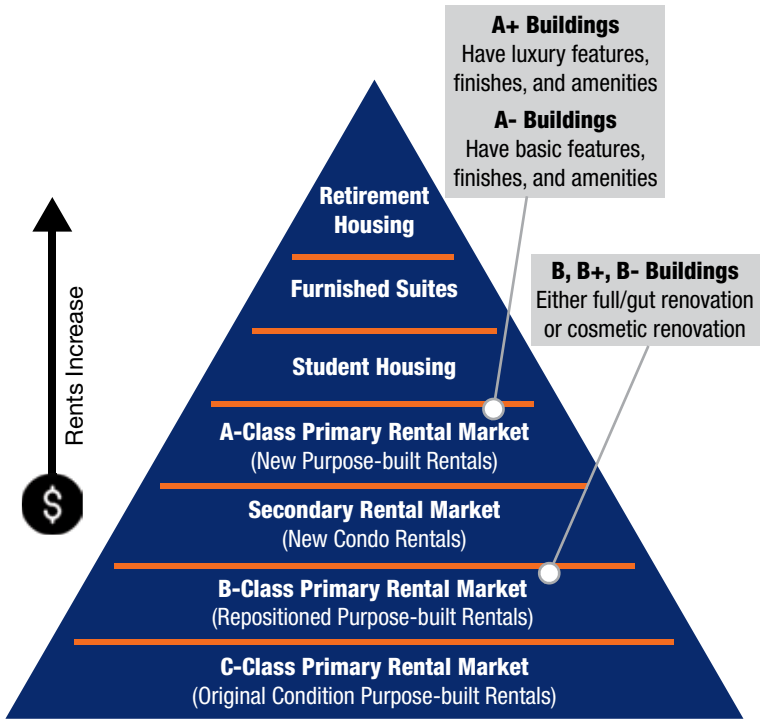


Figure 1.3 - Rental Rates Versus Building Class

In some markets, even by casting a wide net, developers often find they are building in a neighborhood with no direct competition. This is not an undesirable situation, but it makes it more challenging to predict what the optimum rents should be. Though they may be setting top-of-the-market rents, they need to balance their pro forma with what the market will bear.

## Comparables

To get a basic idea what the rental market looks like, we review comparables. There are different types of comparables: new-in-the-market and older comparables.

## **New Comparables**

Depending on the market, finding new rentals is fairly easy. If a building is in a secondary or tertiary market, direct comparables may be more difficult to find, necessitating the need to look further afield. For those, we search in other communities with the same demographics, income and population size, and competition.

## **Older Comparables**

In markets with few comparable units, we rely on indirect market data. This means researching condo rentals and older, renovated buildings.

## **Other Considerations**

In our experience, tenants will pay for superior management. A competent, responsive, well-trained management team will make that apartment the market leader and be able to set rents higher than comparables. If a developer is concerned with rent per square foot, they may miss the value inherent in the charm and individual characteristics of the unit (the value proposition of a unit)—that is, its features, finishes, views, and overall functionality.

## **Individual Unit Advantages**

In some cases, a building with a high percentage of large units can actually perform better on an NOI basis than a building with many smaller units. Although there are fewer units overall, the rent collected per unit is higher. However, operating expenses are consistent and the overall NOI may experience an increase.

It pays to explore every avenue when setting a building's rents, including detailed unit analysis of every unit's pros

and cons. Some unit details will enable higher rents, generating extra money month after month.

## A Building's Value

The four key components of a building's value are:

- Rents
- Ancillary sources of income
- Operating expenses
- Cap rate

The ultimate end of a feasibility study is a project-wide operating pro forma. To this end, we're often asked to name the most important inputs. It's at this stage where first-time developers sometimes get it wrong: they're very good at land and construction costs but tend to "wing it" when it comes to setting rental rates. Further, they take a percentage of those (imprecise) rates to determine their operating costs. When doing that, they have just winged the foundation of their pro forma.

What the developer needs is line-by-line data—actual market data for rent and operating costs. Operating costs are not a percentage of income; they're line items in the budget the developer has researched. Setting market-maker rents is not only about what the building down the street is charging. A developer who designs a better building with amenities well matched to the intended target market can charge premium rents. Even if there are no direct competitors to base rents on, the opportunity to establish market-maker rents still does exist.

What really matters is the building's valuation and the return on investment (ROI), and how these feed into the developer's own financial portfolio and what they're trying to achieve. Once rents are set and operating expenses identified, developers can determine the building's valuation based on the property's NOI and an appropriate cap rate.

## Conclusion

The feasibility study's role cannot be underestimated. Its value to a developer will not only be measured by higher renter satisfaction, but also in knowing they have built the best possible product for those renters. At the same time, they have realized as much value from their property as possible. We've seen too many developers build a product that they would like to live in rather than try to understand the type of product that renters actually *want* to live in.

The feasibility studies we conduct are a valuable investment—an insurance policy—to ensure that the building considered is viable and both fulfills the developer's goal to maximize value and brings to market an attractive rental product.

## Stratford—Oxford Haus: A Sales Story



### Challenge

Peter Hyde, born in Shakespeare just outside of Stratford, Ontario, was a local developer who wanted to build rental apartments in Stratford. He had remediated a former business site and built office space on one portion, and he wanted apartments on the remainder. However, there was no proof of concept. He didn't know if Stratford, a community of 30,000, could absorb a four-building, 236-unit development.

The challenge for us was to determine five things: one, should he build; two, what should he build; three, how much would he be able to charge for the units; four, what was the depth of the local market; and finally, what would the building be worth after it was built.

## Action

We did our standard feasibility study, which revealed that without doubt, Stratford could absorb 236 units and he could charge enough rent to make a very good rate-of-return. Of course, this was only a report, so far. Further, Hyde had to be convinced. Over several meetings going over the details in the report, combined with our experience in apartment development, Hyde gained the confidence to begin building the four, 59-unit buildings.

Our next goal was to find capital. After the first building was built and leased, we brought in a buyer. They liked the project and they liked Hyde, but they were not convinced that Stratford could support all the extra units at equally high rents.

Hyde, still optimistic, built building two, which leased much faster with even stronger rents. We had proof that the concept did work. At that point, we brought the buyer—a major Canadian apartment owner—in again.

Based on the results of the first two buildings, they agreed to buy buildings three and four.

## Result

There's a high degree of predictability of rent and absorption based on studying a city, its economics and demographics, and the persona of the resident profile. We knew, for instance, that in Stratford the majority of renters would be older.

We built larger units to suit their needs. We also built a separate clubhouse designed to give the residents a place to gather socially and hold functions—anything that needed extra space and amenities.

By reading the market accurately, we built a building designed for that market and the residents who lived there. Peter Hyde's development proved that there is a demand for apartments in small centers like Stratford.

## Testimonial: Peter Hyde, Hyde Construction Ltd.



*I felt there was a great opportunity in Stratford, but I needed it well defined by a credible third party. When I was first introduced to Derek, we already knew that he understood the business I wanted to get into and he could provide the confidence we needed to proceed.*

*The feasibility study he produced helped us convince ourselves that there was indeed a viable opportunity there. Also, when we needed financing, we brought that same report to the lenders.*

*His team was there throughout development and lease-up, bringing credible buyers to the table. One of them bought the development—a buyer we have since developed a great relationship with.*

*Derek and his team's ability to offer a full service resulted in a better and more profitable project being built.*

*I highly recommend that any apartment developer involve them from the very beginning and keep them right through to the very end. Involving him and his team worked extremely well for us.*



Figure 1.4 - Stratford - Oxford Haus