

WHAT'S YOUR BUILDING WORTH?

TIM STOATE

It may surprise you to learn that this depends a lot on your energy costs. Why? Because the value of your building essentially comes down to two factors: your net operating income and the capitalization rate (cap rate).

The cap rate is essentially out of your hands – it is what investors think is a reasonable return for an investment in your kind of real estate. Right now, a reasonable estimate of the cap rate is around 7% for the Toronto market.

Net operating income, on the other hand, is very much under your control. And the better you can control your expenses, the higher your net income is likely to be.

To calculate the value of your building, you simply divide your net operating income (NOI) by the cap rate. For example if a building yields a net income of \$70,000 and the cap rate is 7%, the value of the building is \$1 million (\$70,000 divided by 7%).

Now consider that the number one controllable expense for your building is energy costs and you'll start to see how improving the energy efficiency of your building can help you to improve your building's value. With a 7% cap rate, for example, a \$10,000 increase in NOI increases the value of your building by \$143,000.

One of the easiest ways to secure a \$10,000 or more increase in NOI is to improve the energy efficiency of your building. A well-planned and comprehensive retrofit can easily deliver utility bill savings of 15% or more and a payback of under five years. And the result is a more valuable building.

Savvy investors already understand this simple arithmetic. In fact, they will often deliberately look for buildings with poor energy performance knowing that they can quickly increase the building's value by improving its energy efficiency.

But the case for improving energy efficiency to boost your building's value is about to get even more compelling. As of July, you will be paying HST on your gas, electric and water bills – an overnight 8% cost increase. If you do nothing, that 8% is going to take a big chunk out of the value of your building.

Say, for example, your annual utility costs are \$500,000. The HST will add \$40,000 to that bill and, even more alarmingly, will reduce the value of your building by close to \$572,000 (\$40,000 divided by 7%).

But if you implement energy saving measures that save you a conservative 14% on your annual utility costs, the result is much different. Instead of watching your building's value decline by \$572,000, you will see it increase by \$508,000. The net result is that you will have gained more than \$1 million in value for your building compared to what would have been the case if you had done nothing (avoided value loss of \$572,000 plus increase in value of \$508,000).

Let's put it another way. You and your brother own identical buildings – identical in value and NOI and energy costs. He does the energy retrofit and you do not. One year later you both sell your building on the same day to the same buyer, but your brother sells his for \$1,080,000 more. How does that make you feel? And how would it make you feel if the purchaser does the energy retrofit you did not do and then re-sells the building for \$1,080,000 more than he paid you for it?

Now let's look at the return on investment generated by the energy retrofit. Let's say the capital cost of the retrofit is \$400,000 and the increase in NOI generated by this investment is \$75,600 (\$70,000 in energy cost savings plus \$5,600 in avoided increased tax costs as a result of the HST). The results are solid: a seven year return on investment of 32.3%, a seven year internal rate of return of 7.5%, and a 5.3 year payback. What other sure-bet investments do you know that will generate these kinds of returns?

Then look at what it means in terms of building value. Here, your \$400,000 investment has delivered \$1,080,000 in maintained and increased building value, a return of 270%!

By going forward with an energy retrofit now there is a quadruple win for the owner of a building:

- 1) Lower operating costs translate into an increased Net Operating Income (NOI) and therefore protects or increases the building's value.

- 2) Incentives that will help offset the capital costs of upgrades are still available, but many programs expire by December 2010 – check our website at www.TowerWise.ca for a list of programs.
- 3) Efficiency improvements can more than recoup the 8% HST increase – many retrofits can improve efficiencies by 15% or more
- 4) The reduced costs makes the building more competitive in the market place – (and this is even more so if a building becomes sub metered, in which case consumers will be far more concerned about their all-in cost)

The best news of all is that our free TowerWise Conservation Incentive Advisor Service is here to help you gain access to incentive programs and get started with a retrofit today. If your building is in the 416 area code, pick up the phone and call Rob Detta Colli at 416-450-7989 or advisor@towerwise.ca. Rob can provide free advice and one-window access to incentive programs that can help you reduce gas, electric and water bills.

And if you still need to be convinced about the potential for energy retrofits to increase your building's value, crunch the numbers for yourself using the return on investment calculators on the TowerWise website. Just click on "Calculators" in the Quick Links menu in the left column. ♦

TIM STOATE | ASSOCIATE DIRECTOR, MANDATE RELATED FINANCE | TORONTO ATMOSPHERIC FUND

CHARITABLE FOUNDATION DONATES \$5,000 TO OOLAGEN

The Greater Toronto Apartment Association (GTAA) is helping to make a big difference in the lives of at-risk youth in Toronto. A recent gift, of \$5,000, made to Oolagen, a youth mental health centre, is helping with much needed repairs and renovations to the Annex House – one of two residential treatment facilities they operate in downtown Toronto.

The Annex House is nearly 100 years old and houses some of the most vulnerable kids in Toronto. Many of these youth have lived through extreme physical, emotional and sexual abuse and without treatment they all are at huge risk of homelessness. The house they call home with its worn floors, broken stove and inadequate washroom facilities is, with the help of the GTAA, getting some of the attention it needs and deserves.

"The donation from the GTAA will help do a lot of the needed repairs and in doing so will also provide a better, more home-like atmosphere for the kids. Importantly, the support of the GTAA will also let the youth know that people do care and are making an investment in their future," said Bob Engel, Oolagen's Executive Director.

Oolagen first opened its doors, in 1967, to provide a safe and secure home in Toronto for at-risk youth. Since then their programming has expanded to include two residential

treatment homes, three school-based programs, a walk-in clinic and various programs that help troubled Toronto youth and their families. A University of Toronto teaching facility, each year they reach more than 4,000 youth and families through treatment and prevention programs. Oolagen's partners include the Children's Aid Society (CAS), Catholic Children's Aid Society, Jewish Child and Family Services, Toronto District School Board and Native Child and Family Services.

Each year, thousands of Toronto youth – one in five or 20 per cent – struggle with difficulties that impede their success in school or in life. Some of the issues young people deal with include depression, anxiety, suicidal ideation, gang violence, bullying, eating disorders and other social and emotional difficulties that impede their success in school and in life.

Studies show most mental health disorders in youth are treatable. In order to overcome these problems, they must get the help they need while they are young. If not, their unresolved issues can lead to school failure, family conflicts, drug abuse, homelessness, violence and even suicide – all which profoundly impact families and our society as a whole.

To find out more about Oolagen visit www.oolagen.org ♦