

FEATURE Tight markets, battles over lease rates will mark commercial real estate market this year

OUTLOOK 2013

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Vancouver is entering 2013 ranked as the fourth-best market in Canada for real estate investors. But a number of issues could derail what appears as though it could be a strong year in commercial real estate.

The main obstacle: a lack of product, particularly industrial space and multi-family property, to satisfy demand. And, while the downtown office sector tightens, existing landlords expect to face challenges as key tenants prepare to migrate to new top-tier space.

In the annual *Emerging Trends* report, PricewaterhouseCoopers (PWC) and the Urban Land Institute rank Vancouver behind Calgary, Edmonton and Toronto in the "markets to watch in 2013" category. Vancouver's fourth-place ranking is down from second at the same time last year.

"Vancouver's economy has sharpened up and will look to continue that trend into 2013, but [our] survey results show declines in all three categories," the report, which is composed by interviewing industry leaders, stated.

One telling quote underlines the survey's findings: "Overbuilt Vancouver is flat. Lots of supply."

Development prospects showed similar movement down in value and rank, falling from first last year to fifth in 2013.

"Vancouver's government red tape continues to make it more difficult to develop real estate every year. Home-building prospects

also do not look as strong year-over-year, down from first to sixth," PWC stated.

Office market

This will be a year of jockeying for space and deals in Vancouver's downtown, with the office vacancy rate falling below 3 per cent for the first time since 2008. It looks good for landlords, except this may be the last time for such low rates in many years, because 2013 also marks the construction of the biggest wave of new buildings in more than 20 years. By 2015, more than 1.5 million square feet of new space will be completed, which could drive the vacancy rate up to double digits according to Avison Young.

Rob DesBrisay, an office specialist with NAI Commercial, says landlords could be willing to barter by the third quarter of this year. That is when the law firm of Bull, Houser & Tupper vacates four floors, about 60,000 square feet, of space at Royal Centre in preparation for its move into the new Telus Garden tower.

That move will signal the start of landlords offering inducements to retain and attract tenants, suggests DesBrisay, adding that it could also signal a reduction in lease rates.

"I think lease rates are peaking right now, but I know I'm in the minority," he said.

Office tenants may start bargaining hard on five-year leases as landlords eye the coming office competition, however. With little fresh blood coming into the office sector – video gaming and engineering firms appear to be the only new tenants on the horizon this year – there will be pressure on building owners



Telus Garden will be the first of six new office buildings to open – and it is already drawing tenants from existing Vancouver office towers.

to strike deals. NAI believes the vacancy rate for AAA space is now about 2 per cent, which will hold for at least this year. After that, overall office vacancy rates downtown will likely settle at "a healthy rate" of around 8 per cent NAI predicts, noting that none of the latest towers is large enough to seriously skew the market.

MNP Tower, at 275,000 square feet, and Telus Garden, with 465,000 square feet, will both hit the market in 2014 and will be joined by Cadillac Fairview's mixed-use makeover of Pacific Centre, which will deliver another 280,000 square feet of offices. Bentall Kennedy's 745 Thurlow Street will add 365,000 square feet when it completes in 2015, and is already 50 per cent pre-leased to law firm McCarthy Tétrault. Other projects in the pipeline post-2015 include 180,000 square feet by Aquilini Development

and Construction; 200,000 square feet by Reliance Properties/Jim Pattison Developments; Manulife's 250,000-square-foot tower on Howe Street; and a proposal for a 400,000-square-foot building on West Pender Street by Credit Suisse/Swiss Real Group Canada.

As Avison Young notes, unless there is a huge uptick in leasing demand, "the current slate of downtown projects seeking rezoning exceeds market requirements."

A report on downtown office construction by the Altus Insite shows that of the 1.5 million square feet under construction, 556,048 square feet have been leased, leaving about 1 million square feet yet to be taken up. Across Metro Vancouver there are 3.6 million square feet under construction, with only 30 per cent of this space leased up as of the third quarter

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