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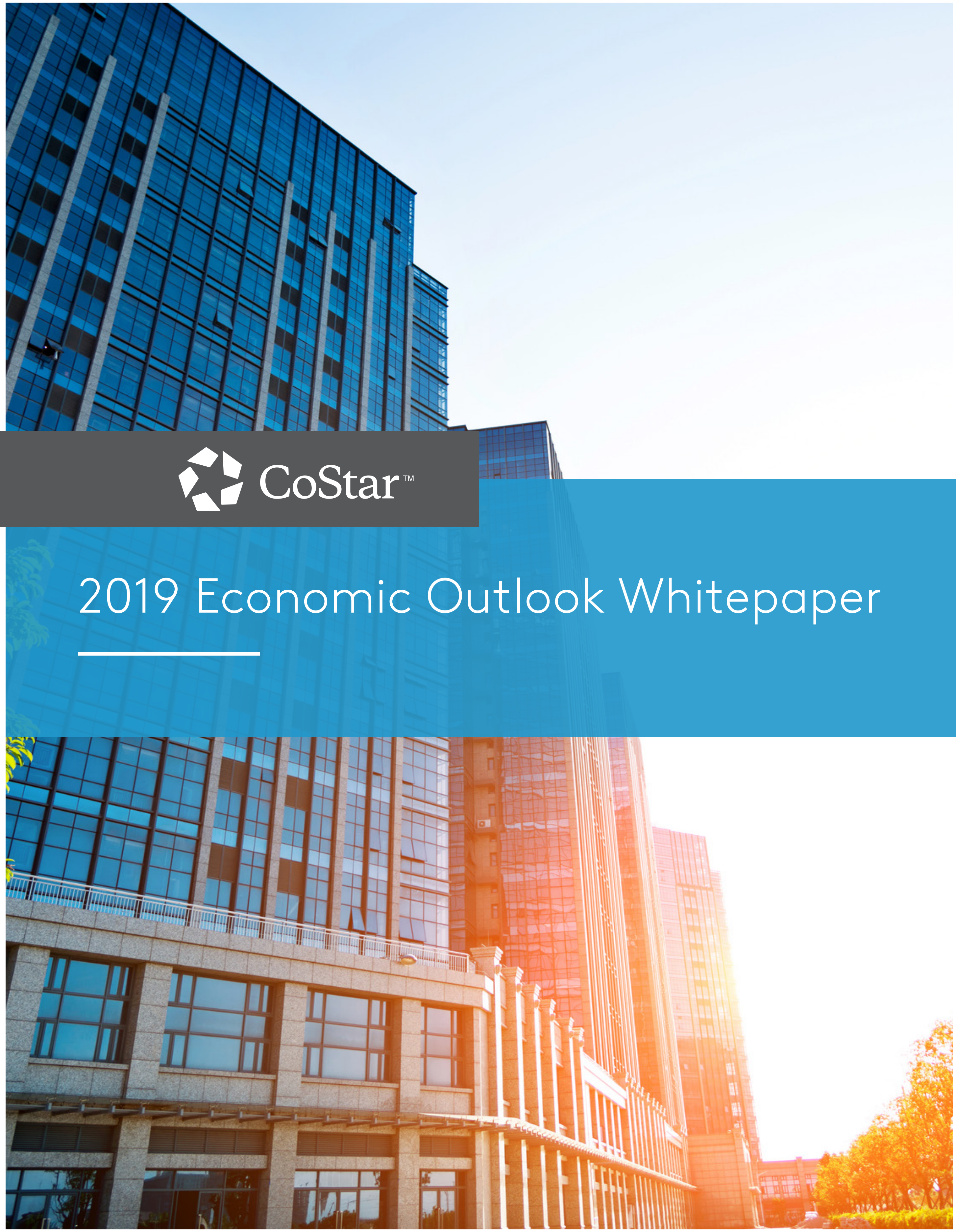

CoStar

2019 Economic Outlook Whitepaper

Expectations are for the economy to grow by approximately 1.8% to 2.0% in 2019, with the Bank of Canada (BoC) expecting growth as high as 2.1%.

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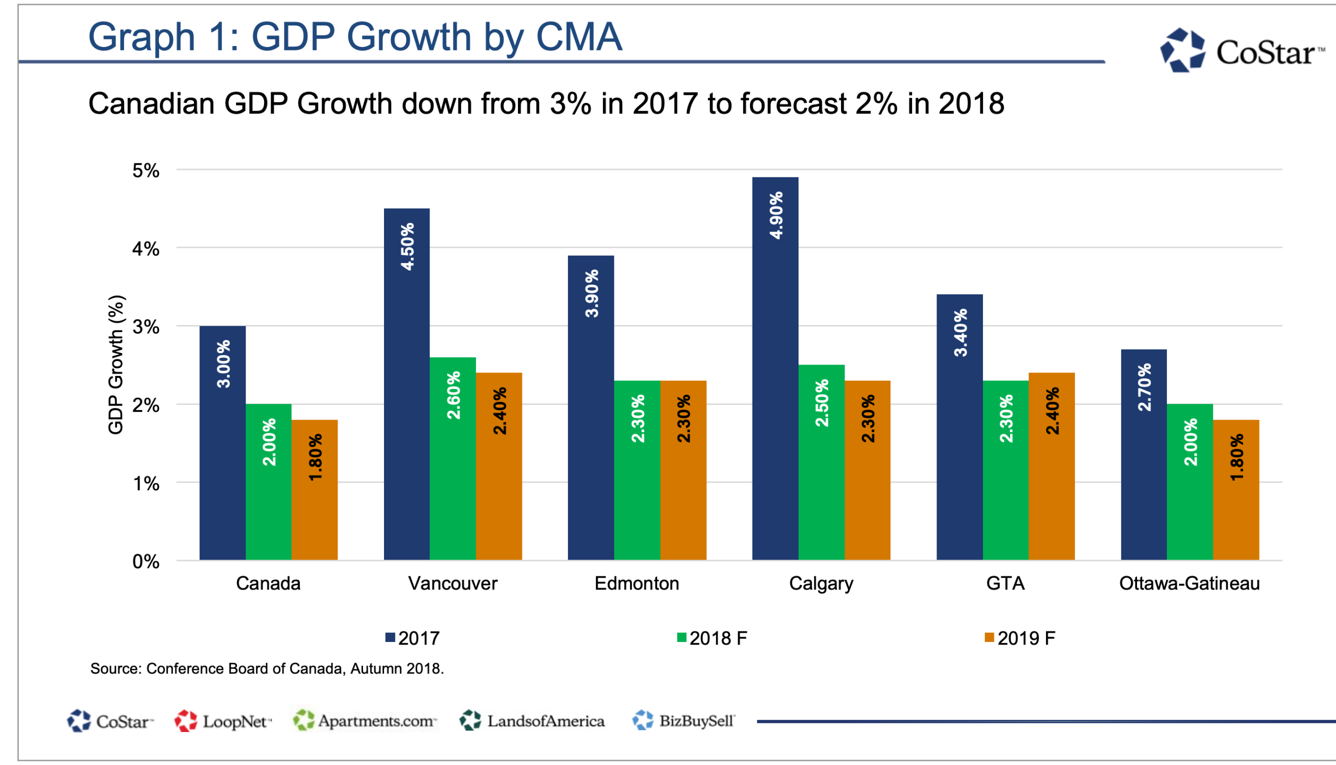
NATIONAL OVERVIEW

As 2018 comes to an end, it is worth looking back at how commercial real estate markets across the country performed, and look forward to what to expect in 2019 and beyond. On the surface, the Canadian economy has been performing well, with unemployment expected to remain at 5.8% through the end of 2018 and GDP growth for 2018 expected to come in at approximately 2.0% - 2.1%. However, the economy has slowed significantly from the 3.0% growth experienced in 2017. This is the result of many factors, including the slowdown in key sectors such as housing, retail sales, and oil. It is also a result of issues related to economic capacity constraints due to low unemployment rates and limited business investment in 2018.

The lack of investment can be partially blamed on U.S. tax reform in January of 2018, but also the drawn-out and negative-rhetoric-infused renegotiation of NAFTA and the uncertainty that it created. This prompted many to press the pause button on business investment decisions. Now that Canada, the U.S. and Mexico have come to a trade deal in principle, replacing NAFTA with the USMCA (aka NAFTA 2.0), this uncertainty has been removed. Unfortunately, it has been replaced with uncertainty about global economic growth in the face of the U.S. China trade war, Brexit, emerging market concerns, central banks raising interest rates, recent stock market troubles particularly in the tech sector, and oil prices.

Domestically, the Canadian economy continues to slow. Although strong employment and rising wages will counteract rising interest rates, any expectation of a rebound to strong retail sales should be taken with caution. Even the Bank of Canada (BoC) acknowledges that households are being impacted by rising interest rates, and the increase in total retail sales they are counting on to partially drive the economy in 2019 will be the result of population growth. Expectations are for the economy to grow by approximately 1.8% to 2.0% in 2019, with the BoC expecting growth as high as 2.1%. Although all markets have slowed dramatically from last year, Vancouver, Toronto, Calgary and Edmonton will lead the pack and are expected to perform above trend, at 2.3% to 2.4% in 2019.



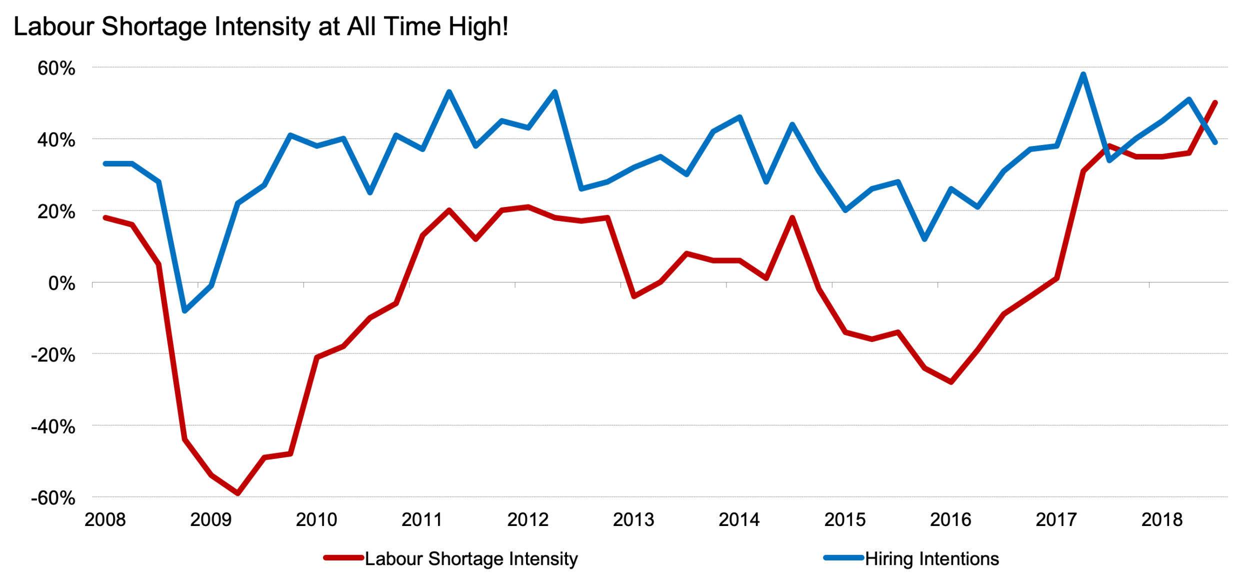
Despite the relatively strong GDP growth forecast, Alberta's recovery has hit a blockage in the pipeline to economic activity. Although the federal Liberals and Alberta NDP parties successfully worked together in favour of the Alberta interests, backing the Trans Mountain pipeline with a $4.5 billion investment, this project was ultimately further delayed and sent back to the consultation phase. Finance Minister Bill Morneau said that the Federal government invested in this project to demonstrate to potential "investors considering Canada as a place to build big, important, transformative projects like the Trans Mountain expansion." He continued, "We want you to know that you have a partner in Ottawa." Unfortunately, it was not enough to get the project moving just yet. Furthermore, the Keystone XL expansion project has hit further roadblocks, and is being delayed once again. The pipelines delays, whether related to oil or natural gas, highlight the issue facing Alberta, as we are unable to get our oil to market.

This is clearly visible when viewing the massive discount that Western Canadian Select (WCS) is being traded at compared to West Texas Intermediate (WTI). The discount has narrowed from US$50 per barrel in mid-October 2018 to roughly US$35 per barrel in late November. This still represents a 65% discount, and it has been estimated that this discount is costing over $80 million in revenue every day, which is having a significant impact on the Albertan, and Canadian economies. With the current state of affairs effectively costing Alberta $80 million per day, the Alberta government is looking at all possible solutions, and everything is on the table, ranging from a temporary 8.7% production cut that will go into effect on Jan. 1, 2019 and increased oil by rail car shipments, to the more permanent pipeline solution and even building more refineries in Alberta specifically and Canada in general.

The slowdown in economic activity is partially a result of exceptionally low unemployment rates, but is also causing a slowdown in employment growth. With the unemployment rate at 5.8%, it is

no surprise that many companies reported to the Bank of Canada, through its autumn Business Outlook Survey, that they are facing unprecedented labour shortage intensity. However, it is also ironic that hiring intentions are easing. With the unemployment rate at 5.8%, employment growth will be hard to come by when it is near 40-year lows, however, the inability to hire results in stalled productivity and output growth, which in turns slows economic activity. This, combined with the uncertainty discussed earlier, seems to be easing hiring intentions.

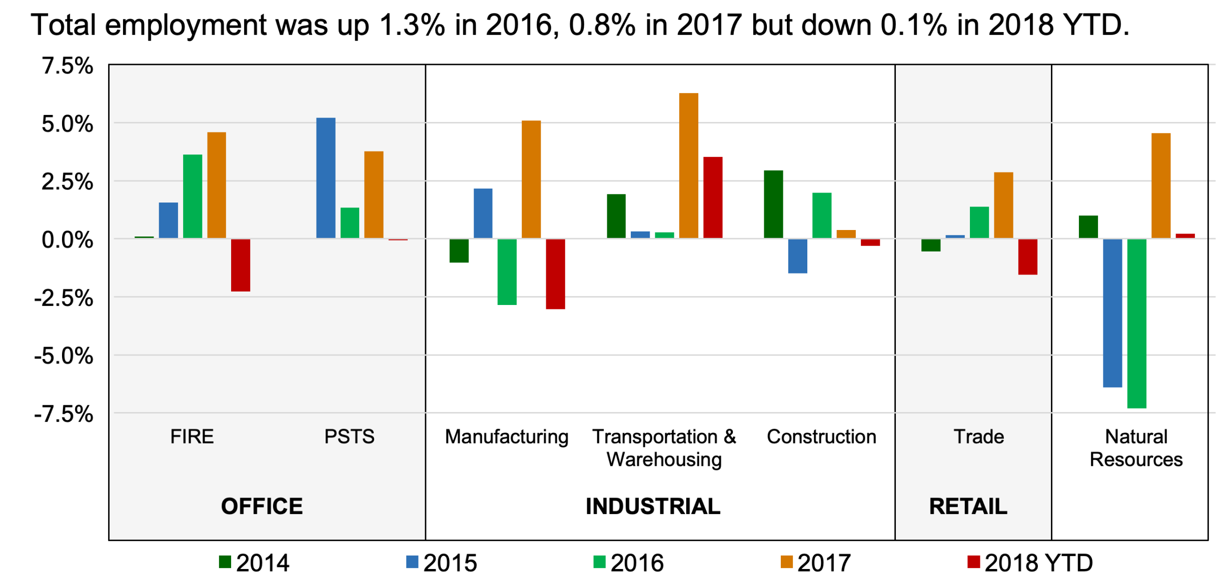
Graph 2: Low Unemployment Results in Labour Shortage



Source: Bank of Canada Business Outlook Survey, Autumn 2018.

The office-using employment sectors, specifically Finance, Insurance and Real Estate (FIRE) and Professional, Scientific and Technical Services (PSTS) have been mixed, with the FIRE sector down -2.3% in 2018, up through October, and the PSTS down -0.1% over the same period. Many of the FIRE sector job losses can be attributed to the slowdown in the residential real estate market, the new mortgage qualifying rules and higher interest rates, which appear to be more persistent as opposed to just delaying. The industrial market continues to be driven by transportation and warehousing, as well as distribution activity for retail (both bricks and mortar and e-commerce). As a result, Canada has seen strong employment growth of 3.5% in 2018 year-to-date in this sector. Manufacturing, on the other hand, has lost approximately 50,000 jobs in 2018 year-to-date, resulting in -3.0% in employment growth. This sector continues to face hardships, due to high energy costs in Canada, specifically in Ontario, and Canada's relative uncompetitive position in regard to productivity and corporate tax rates.

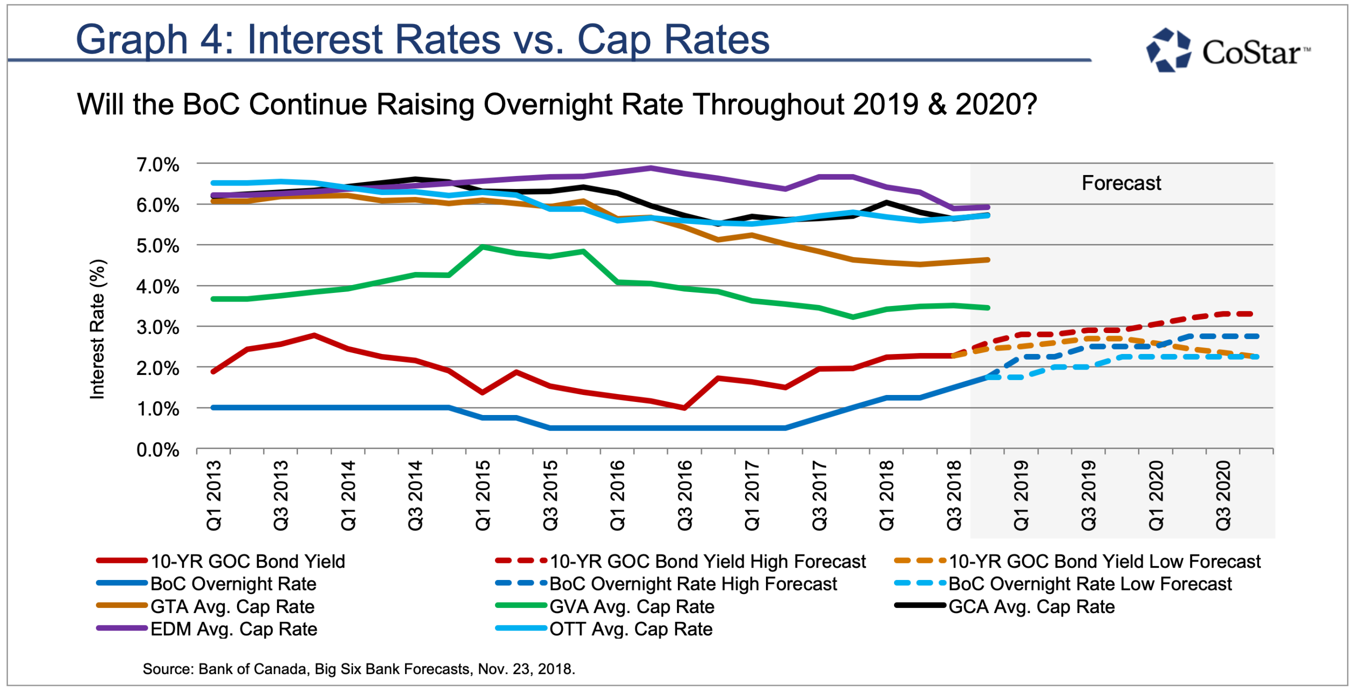
Graph 3: Employment by Sector & Type of CRE Use



Source: Statistics Canada, October 2018.

The consensus is that the BoC will resume raising its Overnight Rate again in Q1 2019, and ultimately will increase the rate by 75 basis points (bps) in 2019 to 2.50% by year-end 2019. They are attempting to normalize the overnight rate again, and although they have stated that they are doing this in a "gradual" manner, we are five interest rate hikes into this process, which started in July of 2017, and although households are feeling the impact, it usually takes at least six quarters for a rate hike to fully impact the economy. The fact that households are feeling the pain already, and that the economy is starting to slow due to the housing market and retail sales, could be a reason for the BoC to pause and further reflect on its rate hike path. This is creating a divergence in projections for interest rate hikes, with some economists expecting the Overnight Rate to peak at 2.25% in Q4 2019, while others expect it to peak at 2.75% in Q2 2019. Furthermore, the projections for the Government of Canada 10-year bond yield are diverging, with some projecting the yields to peak at 2.70% in Q4 2019 and start decreasing from there, where others see them increasing further, to 3.30% by year-end 2020.

In addition to impacting households and retail sales, rising interest rates have had an impact on cap rates, specifically in the Greater Vancouver Area (GVA) and now the Greater Toronto Area (GTA). Both the GVA and GTA have been experiencing the lowest cap rates in Canada, and although high demand asset sales continue to surprise on the low side, the overall four-quarter rolling average cap rate in these markets has been on the rise in 2018. As interest continues to increase, expect cap rates to do the same.



So What about Commercial Real Estate?

Despite all of this, commercial real estate markets across Canada continue to experience strong fundamentals, or at least improving fundamentals in the case of Alberta. Even though construction activity has picked up in many markets, the supply and demand dynamics in play seem to be balanced or skewed to too much demand with not enough supply for many markets. The development pipeline continues to pick up steam; however, construction costs have followed suit. Although costs generally creep up when construction activity moves up due to a scarcity of labour, the most recent increase is partially due to steel tariffs put in place by the U.S., with President Trump maintaining that Canada is a "National Security" threat, highlighting the fact that we are not out of the trade war issue just yet.

The fact that the development pipeline is underway means that monumental new office supply in markets like Toronto and Vancouver is also underway, as demand from the high-tech and FIRE (finance, insurance and real estate) sectors are losing some of their luster. The FIRE sector has been a strong perennial contributor to office demand. However, with the housing market being impacted by rising interest rates and new mortgage qualification rules, demand for space from the FIRE sector is likely going to slow. Furthermore, much of the recent office space demand has come from the high-tech sector, driving both vacancy down and kicking off many construction projects.

However, as of mid-November 2018 the high-tech sector has taken a hit for multiple reasons, with the average stock prices of the FAANG (Facebook, Amazon, Apple, Netflix and Google) group down approximately 25% from its highs earlier in 2018. Although there is no direct and conclusive correlation between stock prices and demand for space, this impact to stock prices, if sustained, will likely have an impact on capital raising abilities, and in turn on new investment and expansion by these companies down the road, which will potentially impact future demand for new office space. More importantly, the impact of broader, sustained and permanent lower equity prices on the economy, both direct and wealth effects, could result in a detraction to GDP growth of up to 0.9% by 2020.

On the retail and industrial side, the impact of higher interest rates on household budgets cannot be understated. Rising interest rates are increasing debt servicing costs, and this, along with the slowing housing market and slowing economy, are starting to impact consumer confidence and retail sales. Even the BoC, which has been and is expected to continue increasing the Overnight Rate from the current 1.75% to 2.50% by year-end 2019, has acknowledged that individual household retail sales are slowing and by virtue households are experiencing stress due to higher interests rates. Although income growth has begun to pick up, ultimately consumer confidence has started to weaken and households are being forced to make tougher decisions on how they spend. The result it is that discretionary items will become even more discretionary.

When you adjust for inflation, retail sales have decreased for three consecutive months, with much of retail sales growth in 2018 being fueled by inflation and population growth. In fact, the BoC is hanging its hat on the assumption that although retail sales per capita will be weak, total retail sales will continue to grow primarily due to population growth. To extend this into retail performance, other than premier retail destinations, which are expected to continue to see strong performance, same-store retail sales in areas that are attracting new immigrant households will likely see stronger same-store sales growth compared to areas that do not.

Looking Forward to 2019

There are potential storm clouds appearing on the horizon, and as we head into 2019 it will be important to pay attention to the following economic indicators:

- **Global Economic Slump:** This includes the impact of the U.S. vs. China Trade War, Brexit, Emerging Markets concerns, and finally the Tariffs that the U.S. has imposed on Canadian steel and aluminum, which are still in effect.

- **Rising Construction Costs:** These costs are high due to an overall increase in commercial real estate construction activity, but also due to the steel tariffs imposed by the U.S.

- **Rising Interest Rates:** Rising interest rates and debt servicing costs are impacting the housing market, the FIRE (Finance, Insurance and Real Estate) sector, Consumer Confidence and Retail Sales. Household budgets and discretionary spending are under pressure, resulting in slowing retail sales growth.

- **Oil Prices, Pipelines and Refineries:** Due to limited pipeline capacity, delays in the projects designed to alleviate those constraints, and increased production, the price of Western Canadian.

- **Easing Inflation:** Inflation in general, but specifically energy prices, have been impacting Canadians and household budgets for much of the last year. However, with the price of energy easing, inflation has started to fall off from the forecasted 2.2% in 2018 to 1.7% in 2019. This will also remove inflation targeting from the BoC's rationale for increasing interest rates.

- **Canadian Competitiveness:** The U.S. tax reform that came into effect in January 2018, known as the "Tax Cut and Jobs Act" and which lowered corporate tax rates and allows for immediate expensing, has made the U.S. economy and companies located there much more competitive when compared to Canada. These changes resulted in a decrease of investment in Canada and an increase in the U.S. The Liberal Federal government has responded by announcing its own accelerated depreciation of capital spending for companies in Canada, which will only serve to re-level the playing field when compared to the U.S. Further highlighting the need for Canada to take competitiveness seriously is GM's recent announcement that they will be winding down operations at their Oshawa, Ontario manufacturing plant, which has been in operations for approximately 100 years and once employed between 30,000 to 40,000 people.

VANCOUVER

British Columbia & Vancouver Economic Overview

British Columbia (BC) and Vancouver have been front runners in economic growth and are projected to continue leading the country in 2019. BC managed to maintain GDP growth of over 3.8% in 2017, and is projected to grow by 2.3% and 2.7% in 2018 and 2019, respectively. Despite efforts, by several levels of government, to slow down the housing market, Vancouver continues to experience affordability issues. However, with the slowdown in the housing market, the construction and Finance, Insurance and Real Estate (FIRE) sectors have experienced pullbacks, which will result in slowing economic activity and employment growth in 2019. Vancouver's economy is forecasted to grow by 2.6% in 2018, just shy of the front runner Montreal at 2.9%, and then slow to 2.4% in 2019.

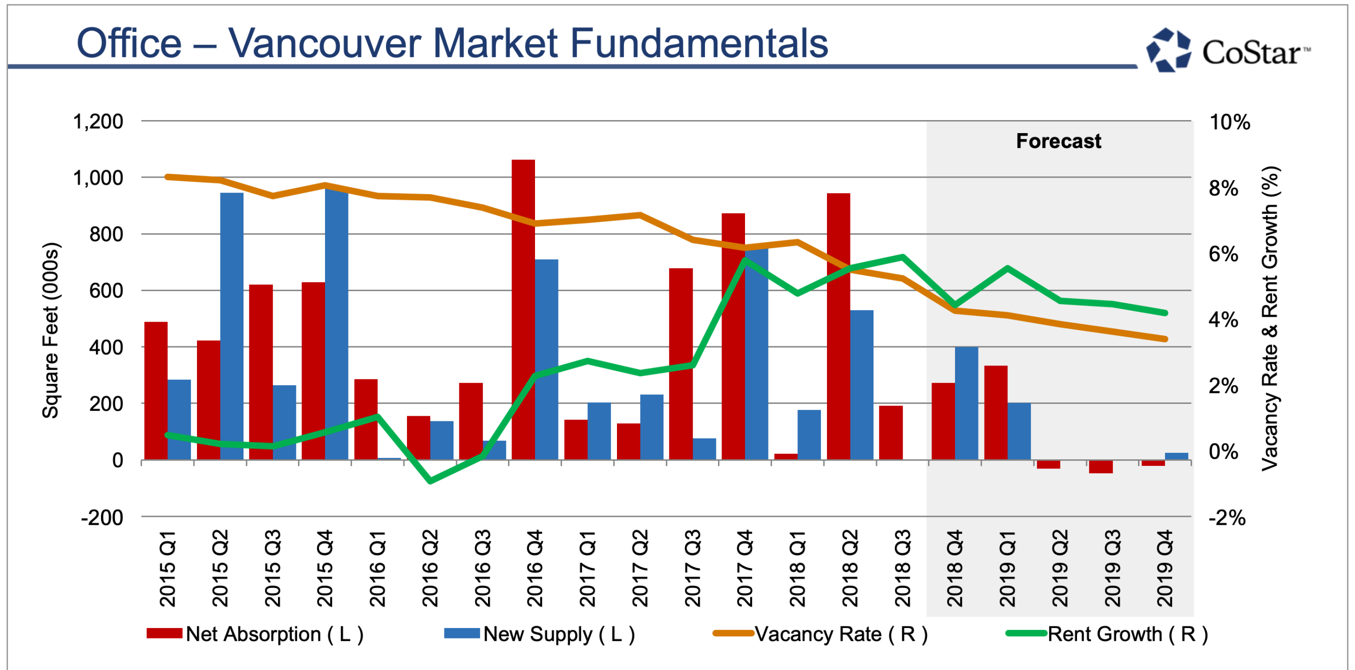
The Vancouver area saw a -3.5% decrease in employment between February 2018 and July 2018, which was due to the slowdown in the residential real estate market and construction activity. However, since then there has been a 1.5% rebound in employment to October 2018, and year-over-year employment is up 1.2%. Employment growth is forecasted to come in at approximately 2.0% in 2019, and although this is up from the approximate 1.0% expected in 2018, it is down dramatically from the 4.8% growth experienced in 2017. This slowdown will be a factor, along with the high cost of living, in the decrease of interprovincial migration. However, the unemployment rate is expected to end 2018 at 4.7%, well below the current national average of 5.9%. This low unemployment rate is being fueled by the tech sector, with Vancouver home to tech unicorns like Hootsuite, Slack and Avigilon, and announcements from companies like Amazon and Kabam, which are leasing office space and highlighting the fact that they see Vancouver as a key part of their long-term expansion plans.

Vancouver Office Overview

The Greater Vancouver Area (GVA) office markets remain deeply embedded in favour of landlords. The office market vacancy rate decreased by 180 bps year-over-year, and is expected to end 2018 at 4.4%, with the downtown market down approximately 250 bps to a painful (for tenants) 2.8%. The market continues to experience strong demand from high-tech companies such as Amazon and Kabam, and co-working companies, such as WeWork, International Workplace Group (IWG – Regus) and Spaces, which continue to announce new and expanded operations in the Vancouver market. Because of this dynamic between low vacancy and strong demand, net asking rental rates are on the rise. However, the year-end 2018 average net asking rental rate, at $23.68/sq. ft. per annum, is up only 0.6% year-over-year due the mix of available space and given that most of the highest quality space has been leased. It is important to note the difference between the downtown and suburban markets. As noted above, the Downtown vacancy is a mere 2.8%, whereas suburban vacancy is down "only" 140 bps year-over-year to end 2018 at 5.3%.

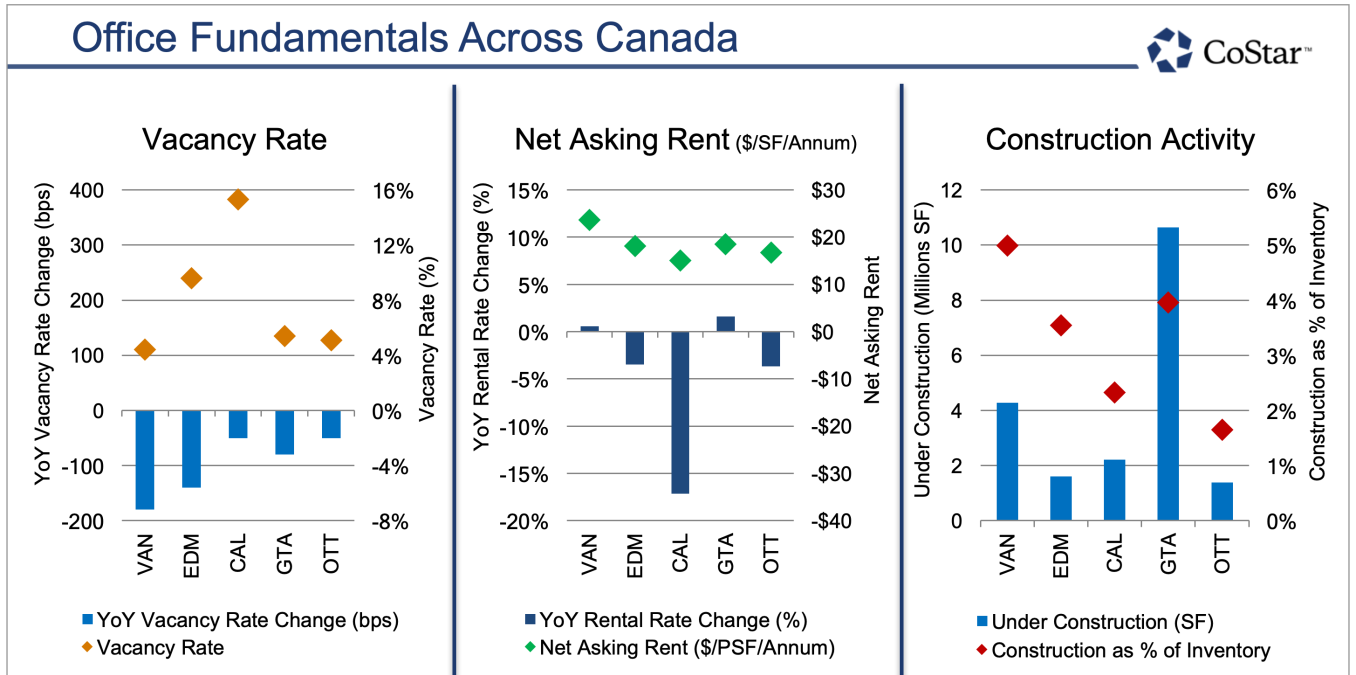
For a tenant looking for over 50,000 square feet (SF) of contiguous space today, there are only two options; if that same tenant were looking for 100,000 SF of contiguous space today, they'd find no current options in the market, and would need to wait until the next supply wave is delivered. Due to the limited options currently available, construction activity has picked up, particularly downtown, with current and expected construction projects now representing approximately 5% of the current GVA market office inventory, compared to just 2.1% at year-end 2017.

The downtown market is the epicenter of this construction boom, with construction representing approximately 10% of the existing downtown office inventory. Much of this space will not be available for several years, and as a result demand continues to spill over into the suburban markets. With exceptionally low vacancy and limited new supply expected in the short term, expect leasing activity to be slow, with vacancy remaining tight and rental rates continuing to increase.



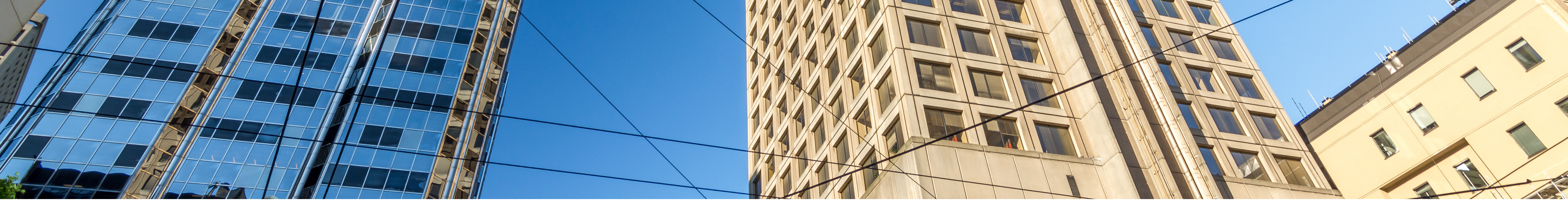
Office – Vancouver Market Fundamentals

Source: CoStar Group, Q4 2018.



Office Fundamentals Across Canada

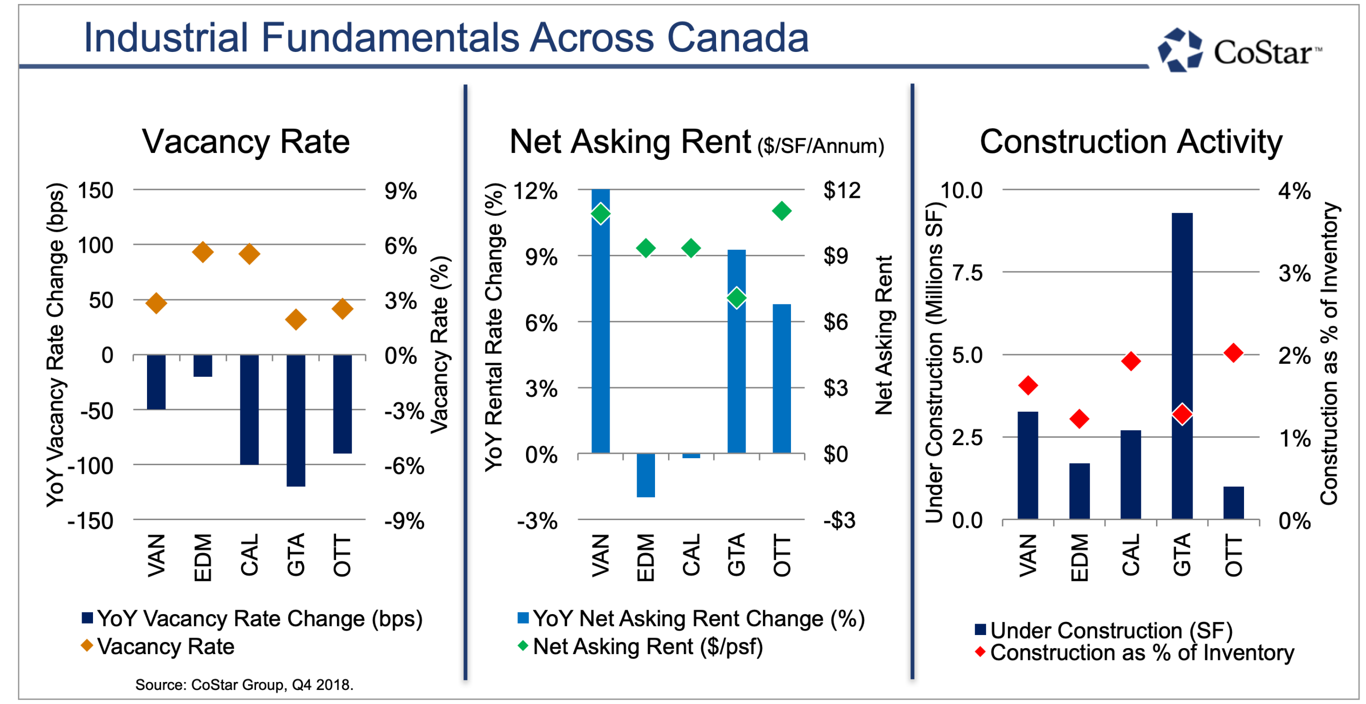
Source: CoStar Group, Q4 2018.

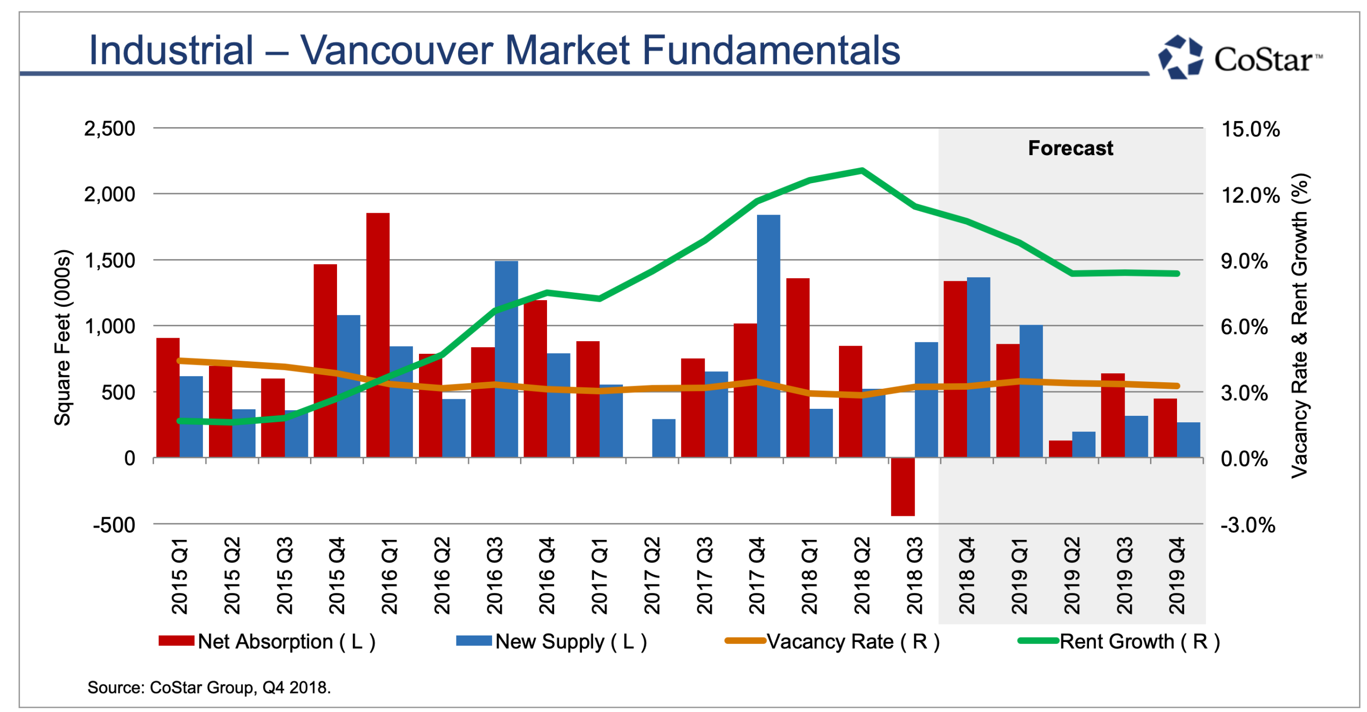


Vancouver Industrial Overview

Like the Vancouver office market, the industrial market remains deeply entrenched in the favour of landlords. The industrial market has also experienced strong demand for space from owner-users on the sale side, who are driving up prices as they look to extricate themselves from the strong landlord controlled market, and the transportation and warehousing sector on the leasing side. As a result, the industrial vacancy rate has experienced a 50 bps drop year-over-year, to 2.8%. However, there was a spike in vacancy in Q4 2017 due to approximately 1.8 million SF of new supply that came online. Supply and demand have been somewhat in check, meaning what is built is pretty much immediately leased or sold, and vacancy has not swung wildly. However, with low vacancy and availability to begin with, and immediate demand for space that becomes available, the average net asking rental rate continues to increase, up 12.0% year-over-year to end 2018 at $10.90/SF per annum.

For a land constrained market, Vancouver is experiencing strong construction activity to feed demand. Even though there has been approximately 2.0 million SF of new supply delivered over the last year, there was still over 3.0 million SF under construction at year-end 2018, with more projects expected to commence. This increase in construction activity is welcomed in a market that is expected to see economic growth and demand for space remain strong. However, the dynamic of low vacancy and high rents is expected to remain in place.

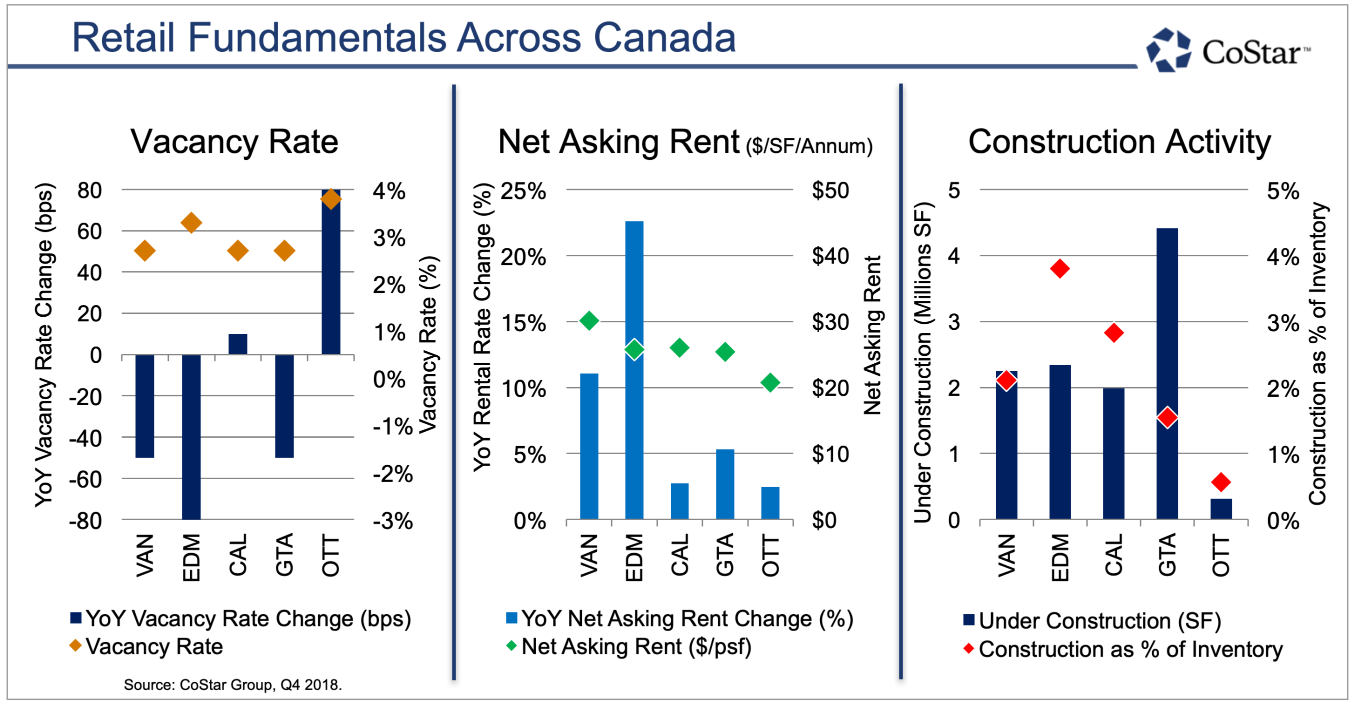


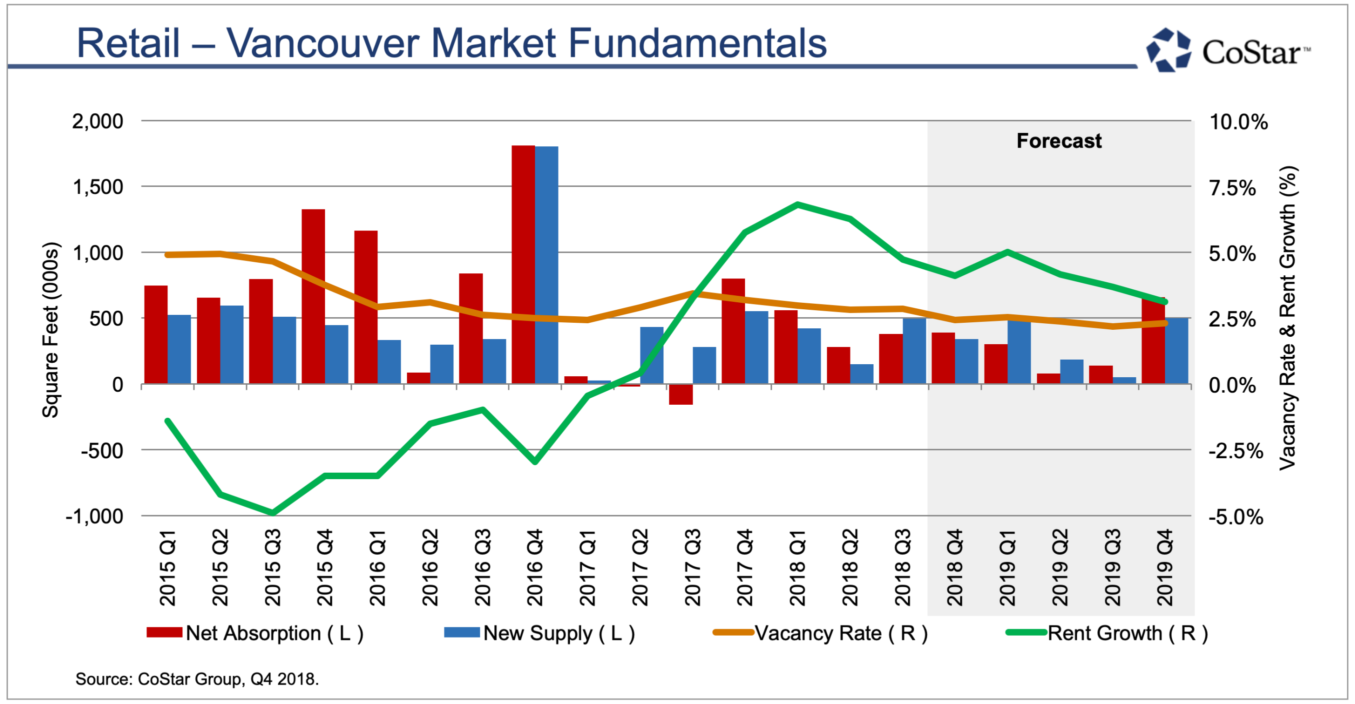


Vancouver Retail Overview

Although BC retail sales growth has slowed, from a whopping 9.1% in 2017 to under 3% in 2018 year-to-date, the Vancouver retail market continues perform well, receiving new international retailers who are either looking to enter the Vancouver market, or are using Vancouver as a launching pad to reach the rest of Canada. The Vancouver retail market has experienced a 50 bps decrease in vacancy year-over-year to end 2018 at 2.7%, which came at a time when there was 1.1 million SF of new supply, and Sears had vacated all of its stores (Q1 2018). The average net asking rental rate has increased by over 11.0% year-over-year to end 2018 at $30.14/SF per annum. With exceptionally low vacancy rates and strong increases in net asking rents, it comes as no surprise that construction activity has moved up from 1.7 million SF in Q3 2017 to 2.2 million SF as of year-end 2018, representing 2.0% of the existing retail inventory. This new supply will be a welcomed addition for tenants who are struggling to find space amid low vacancy and increasing rents.

Landlords of premier quality properties continue to work on improving their properties and making them experiential destinations. They are doing this to attract more traffic and shoppers, and to combat the e-commerce threat by differentiating themselves from the rest of the pack. Expect to see this activity, along with more intensification and repurposing of parking lots in suburban malls (such as the redevelopment of Oakridge Centre and Brentwood Town Centre) going forward. Although retails sales growth is expected to remain positive, higher interest rates and rising debt servicing costs will take a bite out of retail sales. The retail market remains bifurcated with the haves and have-nots, with the "haves" properties continuing to see strong tenant demand, low vacancy rates and rental rate growth. In turn, the "have nots" will suffer disproportionately.





Alberta's GDP growth is only expected to reach 1.7% in 2019.

ALBERTA

Alberta Economic Overview

Although the Albertan economy is expected to be one of the strongest performing provincial economies in 2018, economic growth has been downgraded. Previously recorded GDP growth of -3.9% in 2016, 4.9% in 2017, and forecasts of 2.5% in 2018 have been revised to -4.2%, 4.4% and 2.3%, respectively, reflecting that the downturn was more severe and the bounce back was less exceptional than originally believed. Furthermore, Alberta's GDP growth is only expected to reach 1.7% in 2019, highlighting the fact that without new pipelines or any new way to get Alberta's resources to market, economic growth has effectively stalled. The expansion of the Trans Mountain pipeline, now owned by the Government of Canada, remains back in the regulatory approval stage. In addition, the Keystone XL pipeline has received a stop-work order while the courts decide if the environmental effects of the pipeline were fully considered. Even though a decision is expected by February 2019, the court order as it stands prevents TransCanada from finalizing contracts, purchasing materials, conducting land surveys and discussing federal permits, and ultimately could put the 2019 construction season in jeopardy and delay the project by up to one year.

By comparison, Calgary and Edmonton are expecting GDP growth of 2.5% and 2.3%, respectively in 2018, with both forecasted to grow by 2.3% in 2019. On the job front, Alberta's unemployment rate continued to decline in 2018, from 7.8% at year-end 2017 to an expected 6.8% at year-end 2018. In Calgary, the wholesale trade as well as transportation and warehousing sectors will lead the way, primarily due to the Western Canada distribution hub status that Calgary enjoys, but also as a result of the expected further increase in the oil by rail as Alberta finds ways around pipeline delays. In Edmonton, the downtown revitalization and other construction projects are expected to drive the employment market in the short term.

Oil production has been increasing for years, but the failure to simultaneously build pipelines has created an astronomical and record setting spread between the Western Canadian Select (WCS) and West Texas Intermediate (WTI) oil companies. The WCS-WTI spread at mid-year 2018 was approximately USD$18/barrel when WTI prices were at approximately USD$66/barrel, however, the spread moved up to approximately USD$50/barrel in the fall when WTI was priced at USD$70/barrel. Since then the situation hasn't improved. Although the WCS discount has since decreased to USD$35/barrel, the price of WTI has also decreased, down to approximately USD$50/barrel. Ultimately this discount is costing the Canadian economy, and specifically the Albertan economy, an estimated $80 million per day. This situation is so dire that the provincial government has imposed an 8.7% production cut and invested in rail cars in order to increase oil by rail. They also began investigating the building of refineries in Alberta to both alleviate the pipeline blockage and get Alberta back to work.

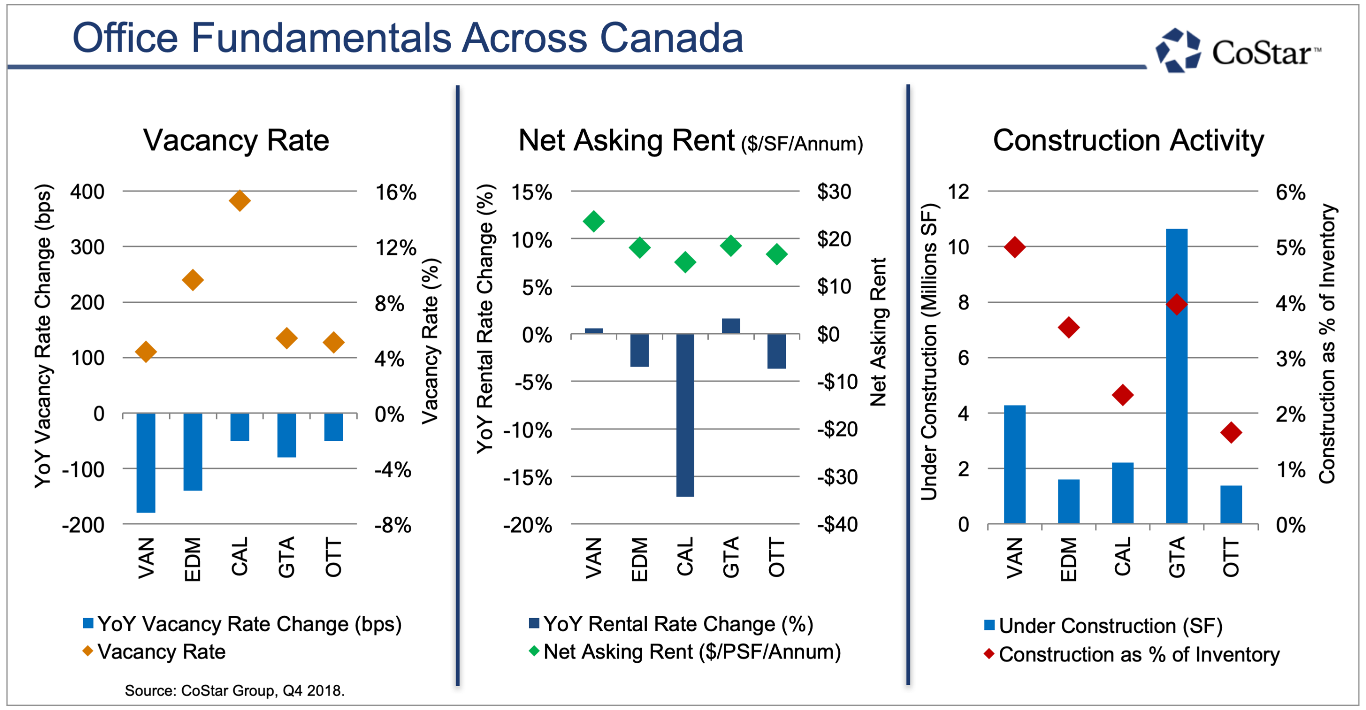
Calgary Office Overview

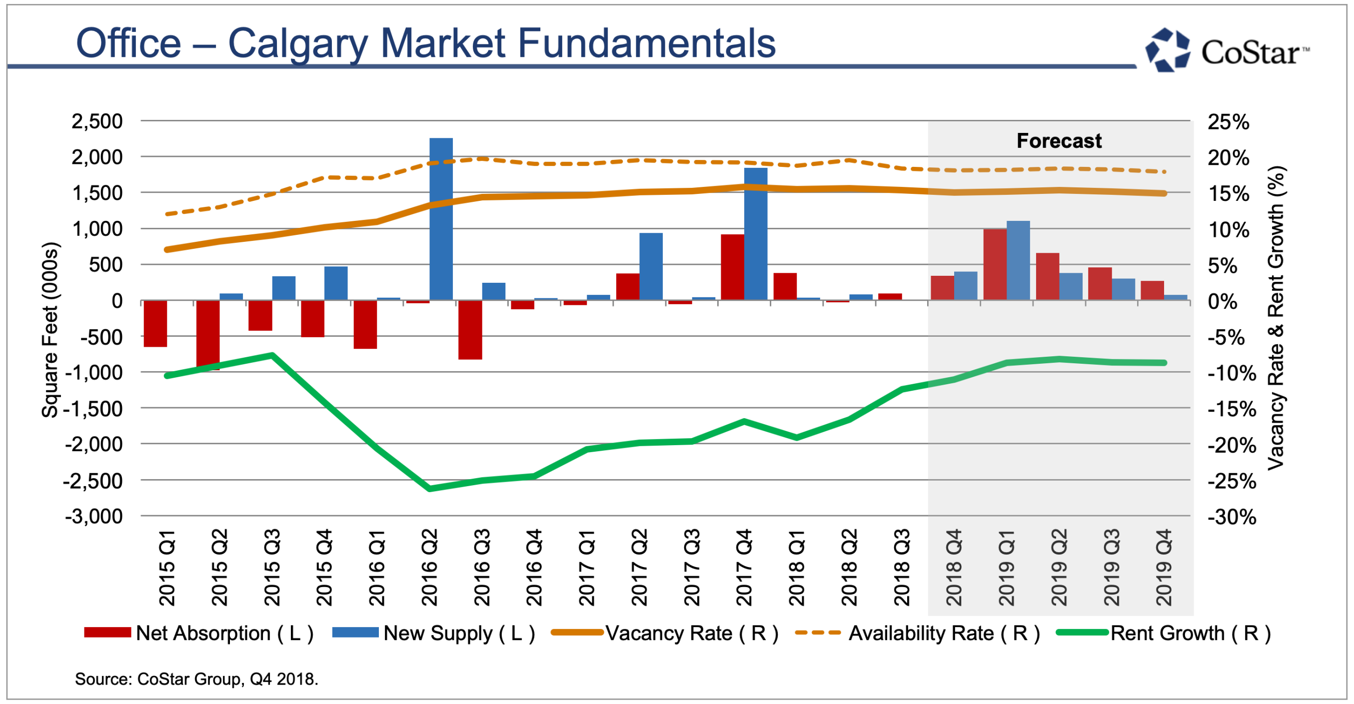
The Calgary office market remains in the doldrums, with vacancy at approximately 15.0% at year-end 2018 and availability at 18.1%. Although vacancy has slowly decreased, down 50 bps year-over-year, it is expected to increase in the first half of 2019 after the delivery of TELUS Sky, a 761,000 SF office tower being completed in Q1 2019. TELUS Sky is the last major downtown office development from the last construction cycle, and although it is currently 64% preleased, it will be adding vacant space to the market directly and indirectly as it draws tenants from other properties. As a result, overall vacancy is expected to increase by 30 bps in the first half of 2019 to 15.3% in Q2 2019.

Calgary is one of the only major markets in Canada where downtown vacancy, at 19.9%, is higher than suburban vacancy, at 12.4%, and the downtown net asking rent, at $13.24/SF per annum, is below the suburban rent, at $16.96/SF per annum. With the current level of demand and the amount of vacant and available space in the market, this dynamic is expected to continue for the foreseeable future. This is creating opportunities for tenants, who normally wouldn't be able to consider downtown office space, to now move into Class A downtown buildings. Since TELUS Sky is a downtown development, it is worth examining how it will impact the downtown market. Current vacancy downtown is 19.9%, as of year-end 2018, and once TELUS Sky is delivered, vacancy will crest the 20% mark to 20.1% in early 2019 before starting to fall once again.

Downtown availability is much higher at 22.3%, and is expected to move up to 22.5% by Q1 2019 before starting to descend once again. Although total vacant space continues to increase, sublet space accounted for only 24.0% of total vacant space, compared to 38.0% at year-end 2016. However, this does not account for shadow sublet vacancy, - which will likely push the vacancy rate as well as the proportion of sublets much higher.

Overall net asking rental rates continue to fall, down -13.3% year-over-year in 2018, and given the current vacancy hangover and the expected economic and employment growth, rents are expected to continue falling until they finally stabilize in 2021.

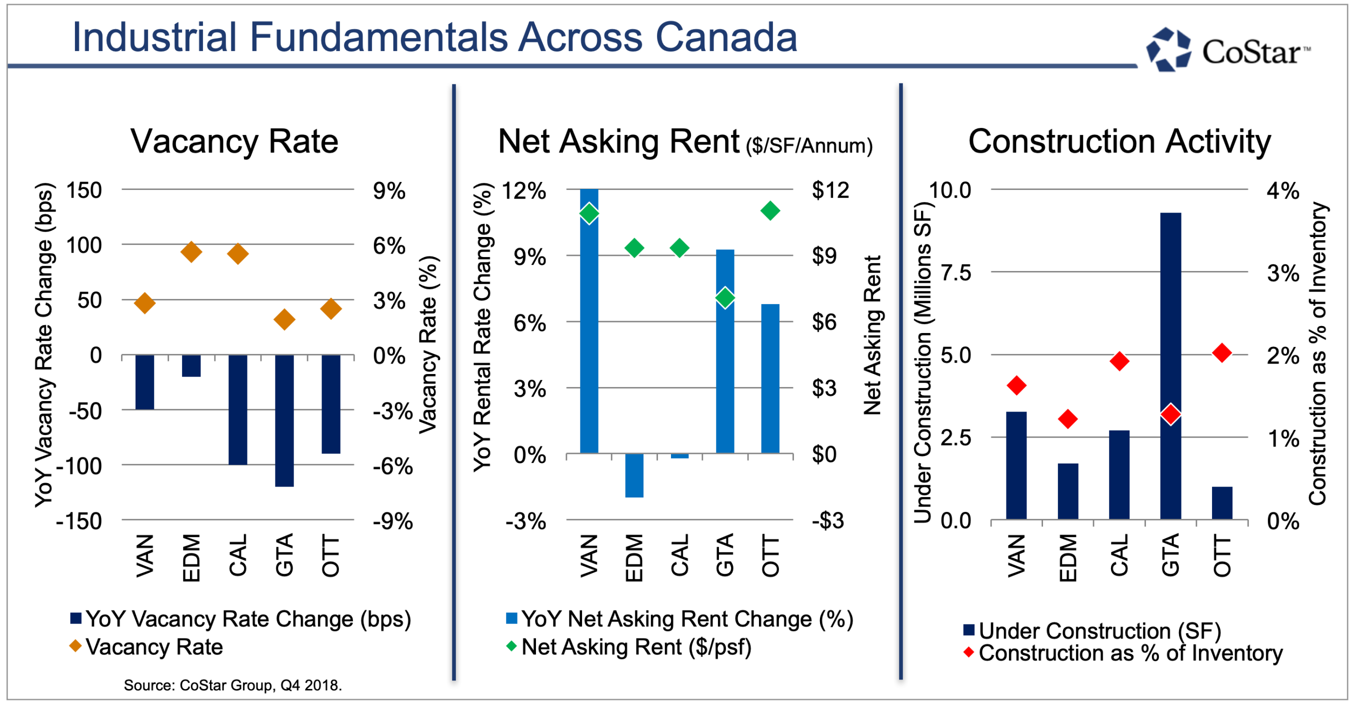


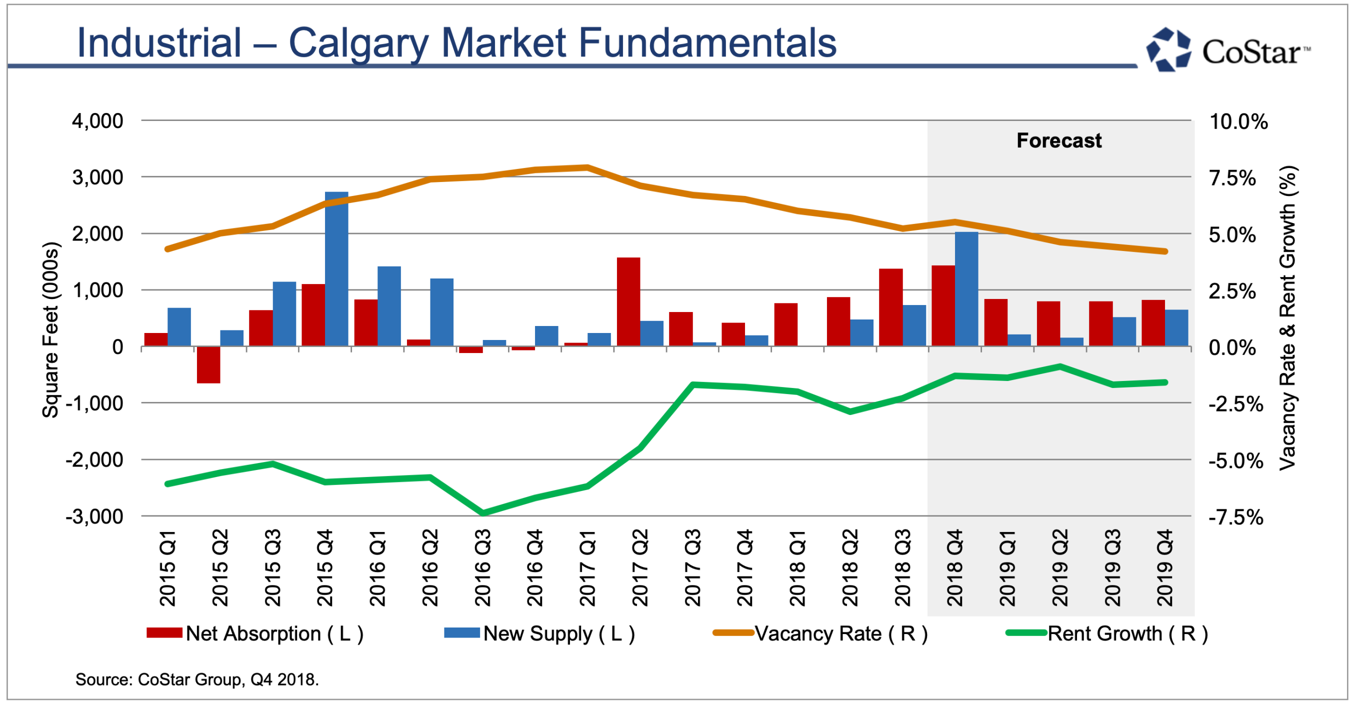


Calgary Industrial Overview

On the industrial side, the Calgary industrial market remains healthy, and has been the safe and steady asset type in Calgary primarily due to its status as a key Western Canada distribution hub. A perfect example reflecting this status is the new 600,000 SF Amazon Western Canada distribution centre in Balzac, just north of Calgary. This project has created a mini hiring boom in the area, creating 1,000 permanent and seasonal jobs in the Calgary market.

Calgary's industrial vacancy rate has decreased by 100 bps year-over-year to end 2018 at 5.5%. However, net asking rents were also down, by -0.2% year-over-year to $9.34/SF per annum. There is currently only 2.6 million SF of industrial space under construction, representing only 1.9% of the current inventory, and although the vacancy rate is expected to continue creep down to between 4.0% and 4.5% by year-end 2019, expect construction activity to pick up to a point that will finally see vacancy move back up in 2020 and beyond with average asking rental rate growth turning positive.



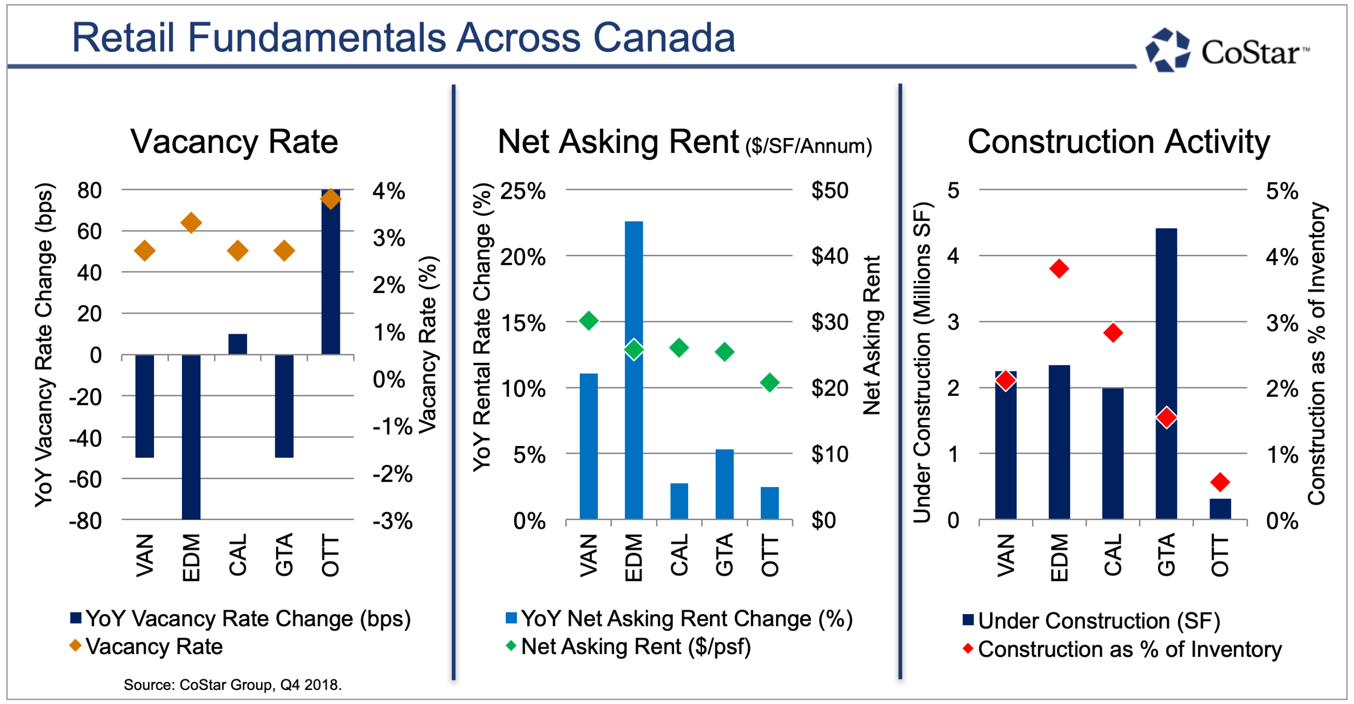


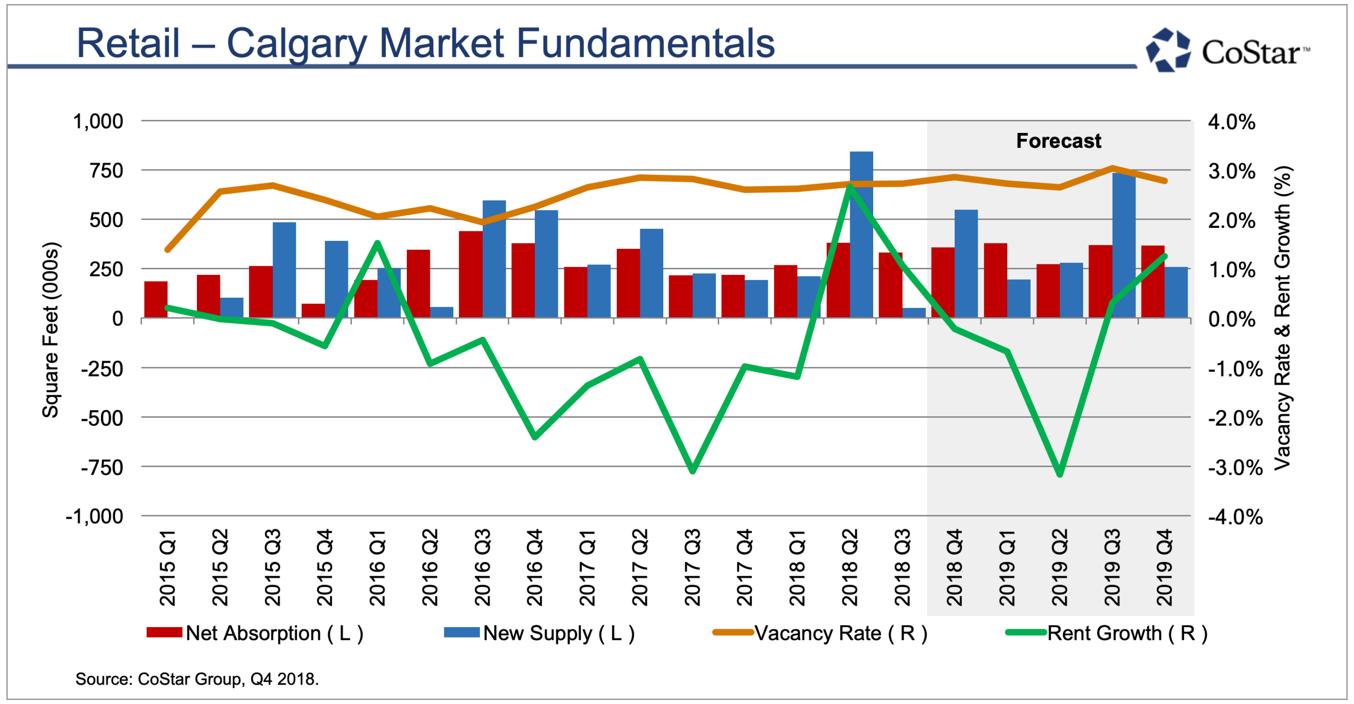
Calgary Retail Overview

The Calgary retail market remains tight, despite the 1.2 million SF of new supply, delivered in 2018 at the same time all Sears locations closed down. The vacancy rate moved up a miniscule 10 bps year-over-year to 2.8% at year-end 2018, and net asking rents increased by 2.8% over the same period to $26.06/SF per annum.

The retail market remains bifurcated with the haves and have nots. As landlords of premier quality properties continue to work on improving their properties, making them experiential destinations in order to combat the e-commerce threat, they are further differentiating themselves from the rest of the pack, attracting more shoppers and the new and better retailers. Expect to see this trend, along with more mixed use intensification and repurposing of parking lots in suburban malls, going forward.

Even though the economy is slowing once again and households are trying to get their budgets back in order in the face of increased debt servicing costs, retail sales growth in Alberta is expected to remain positive in 2018. However, it has slowed dramatically compared to its 7.1% growth reported in 2017. As a result, vacancy is expected to remain in check despite the approximately 2.0 million SF currently under construction, representing 2.8% of the existing retail inventory. Rental rate growth, although volatile over the short term, is expected to remain positive, near 2.0% over the coming years.



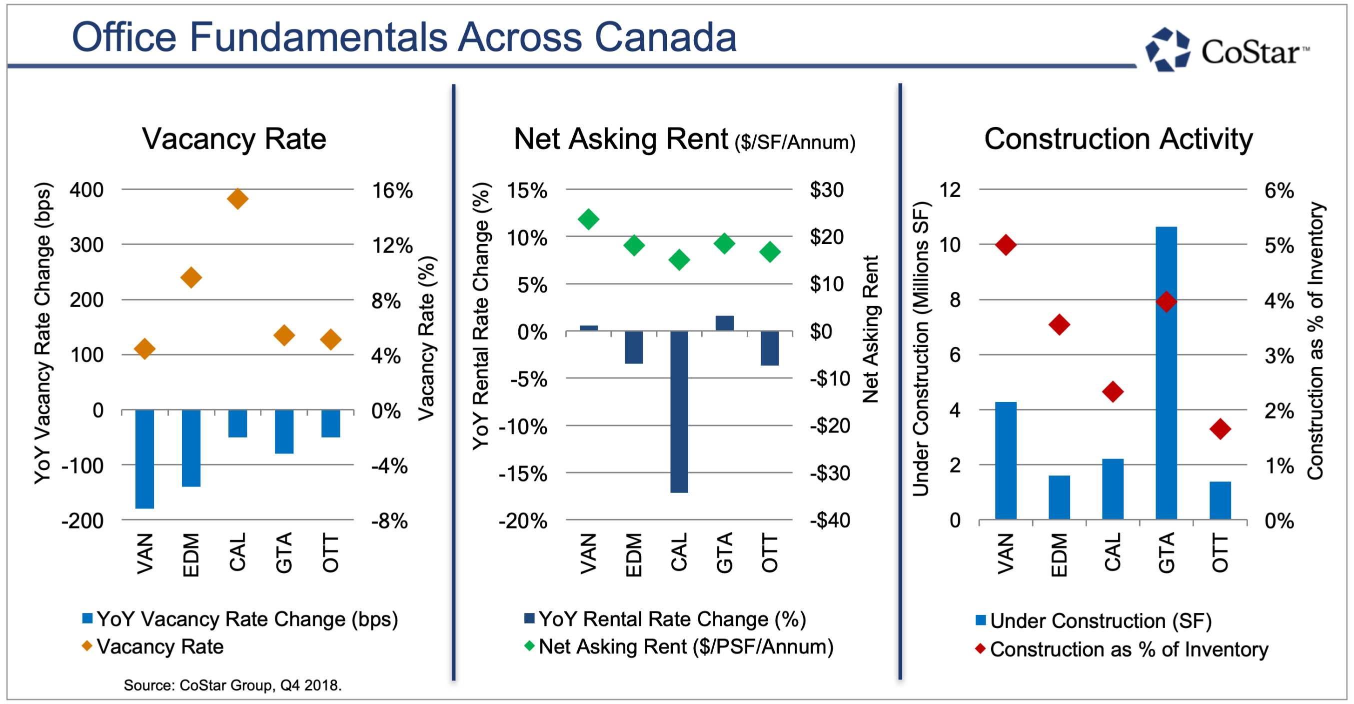


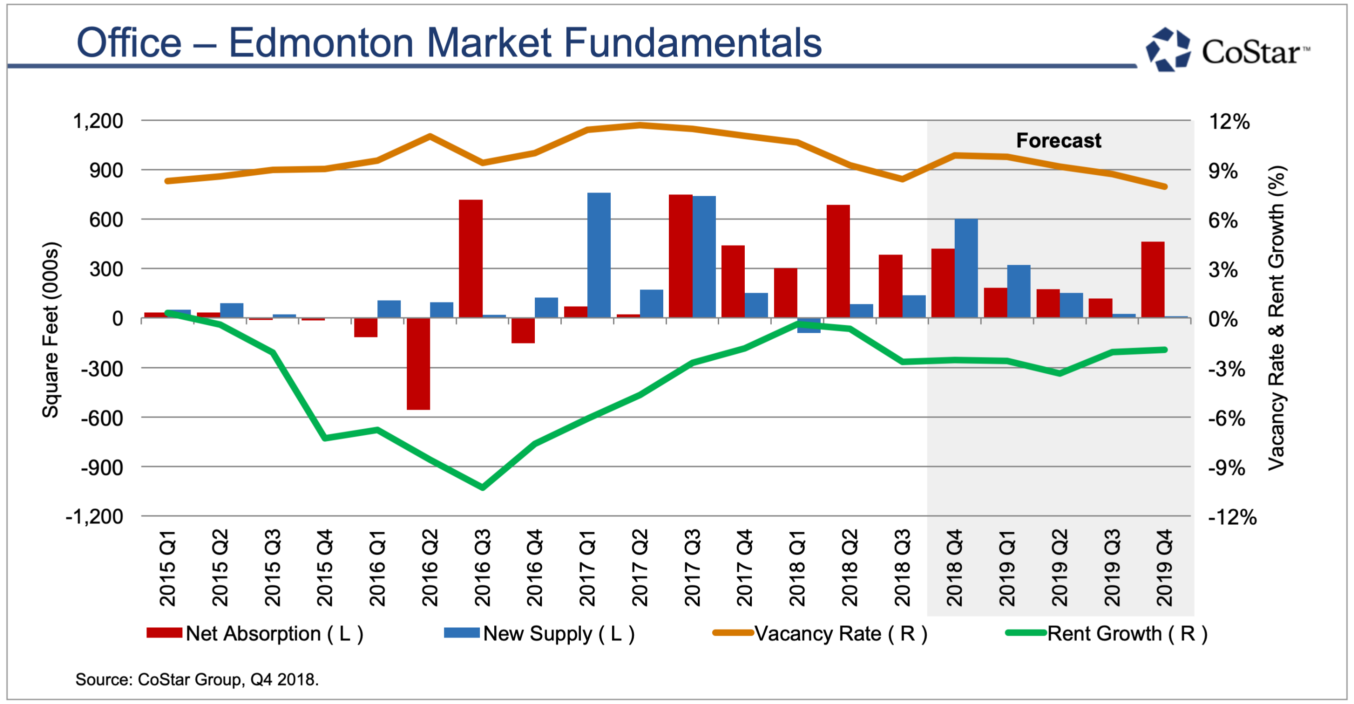
Edmonton Office Overview

Unlike Calgary, which is heavily reliant on oil and gas, the Edmonton economy is much more diversified with government (provincial), health and technology playing bigger parts. As a result, the Edmonton office market continues to perform well, with vacancy down 140 bps year-over-year to end 2018 at 9.6%. However, net asking rents for the office market have decreased by 3.5% over the same period to $18.14/SF per annum. Like Calgary, Edmonton is one of a few markets, where downtown vacancy, at 11.1%, is higher than suburban vacancy, at 7.8%. However, this has more to do with new supply driving up vacancy in some of the older, less competitive buildings.

Edmonton's downtown has changed dramatically, becoming more dynamic and attractive, with both Enbridge Centre and Edmonton Tower, completed in 2017, delivering almost 1.2 million SF in total. The office portion of the Stantec Tower, at approximately 800,000 SF, accounts for half of the 1.6 million SF of office space currently under construction, and is expected to be delivered later this year. The building is the tallest in Edmonton, as well as the tallest in Western Canada. It is 97% preleased, and as a result, will not directly impact the office market vacancy. However, as tenants complete their moves to this new tower, expect vacancy to increase in the older buildings that these tenants leave.

Downtown landlords of older stock properties will need to either invest in renovations to compete with the standards set in the three new towers; repurpose their properties; or suffer higher vacancies. A perfect example of this situation: AIMCo's plans for HSBC Bank Place, a 317,000 SF office tower on 101st Street. Preliminary work began in June 2018. AIMCo planned to completely overhaul both the exterior and interior of the building with a triple-glazed curtain wall system; install floor-to-ceiling view glass and new mechanical and electrical systems; and achieve LEED Gold Certification and WELL Gold Certification. AIMCo also announced that upon completion in late 2019, it will be relocating its Edmonton-based headquarters to HSBC Place.

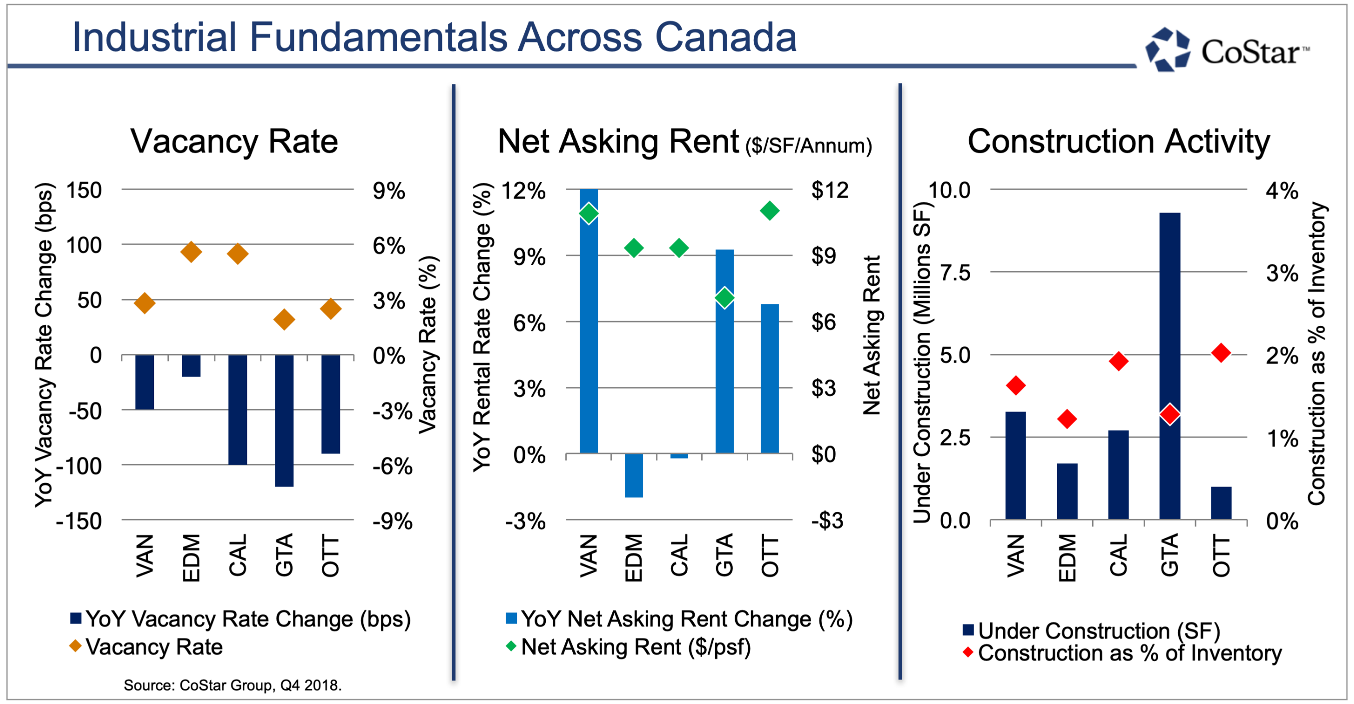


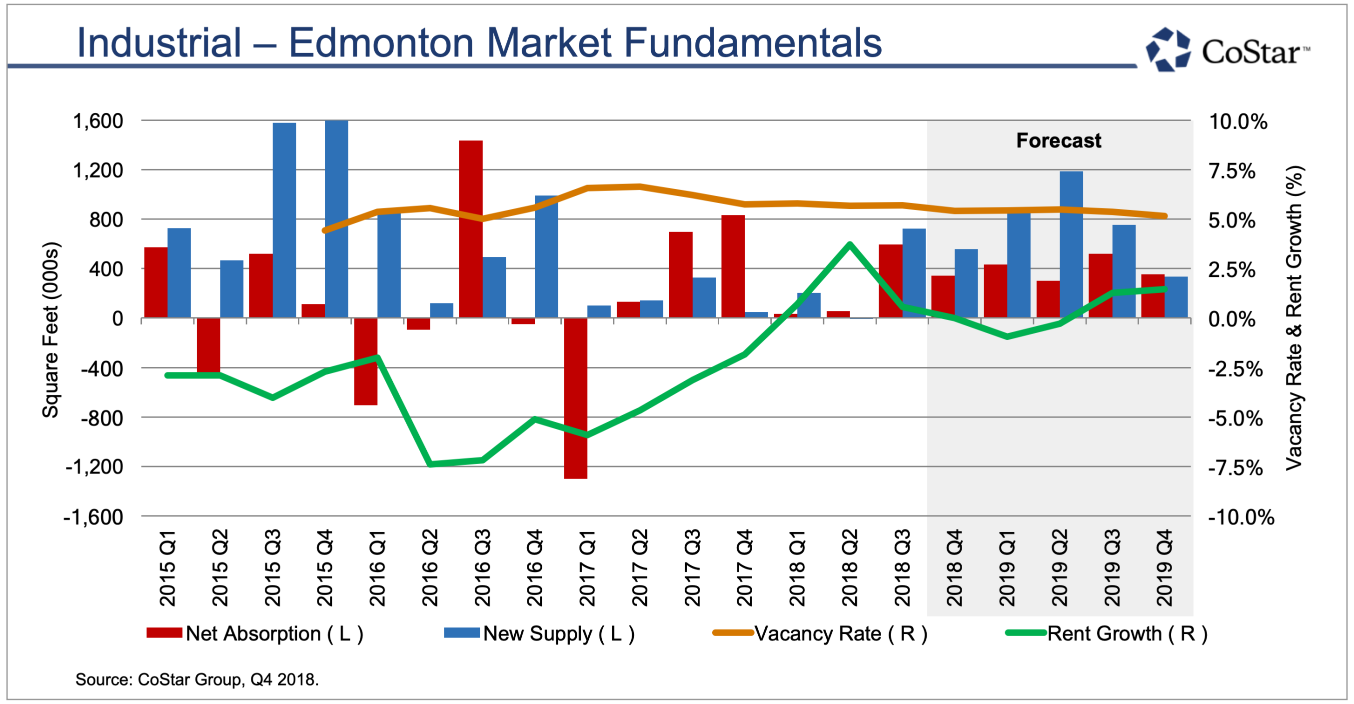


Edmonton Industrial Overview

The Edmonton industrial market has experienced a 20 bps decrease in vacancy year-over-year to end 2018 at 5.6%. However, over the same period the average net asking rental rate moved down 2.0% to $9.34/SF per annum. The industrial market experienced increased tenant demand from the oil sector, but due to the latest developments this will likely pause. Increased demand from both the cannabis industry and cryptocurrency miners, due to the low cost of energy in Alberta, will likely remain in play.

Looking forward, the Edmonton industrial market should eventually benefit from the expansion of the Trans Mountain pipeline once completed, but more immediately from tenants seeking industrial space for high energy uses. There has been approximately 1.2 million SF of new supply delivered in the last year; however, there is currently over 1.7 million SF under construction, up from 1.2 million SF at year-end 2017. With the current level of demand and the pace of construction activity, expect the industrial market to stay relatively balanced. Despite some weakness in rental rates, growth is expected to turn positive in late 2019 and beyond.



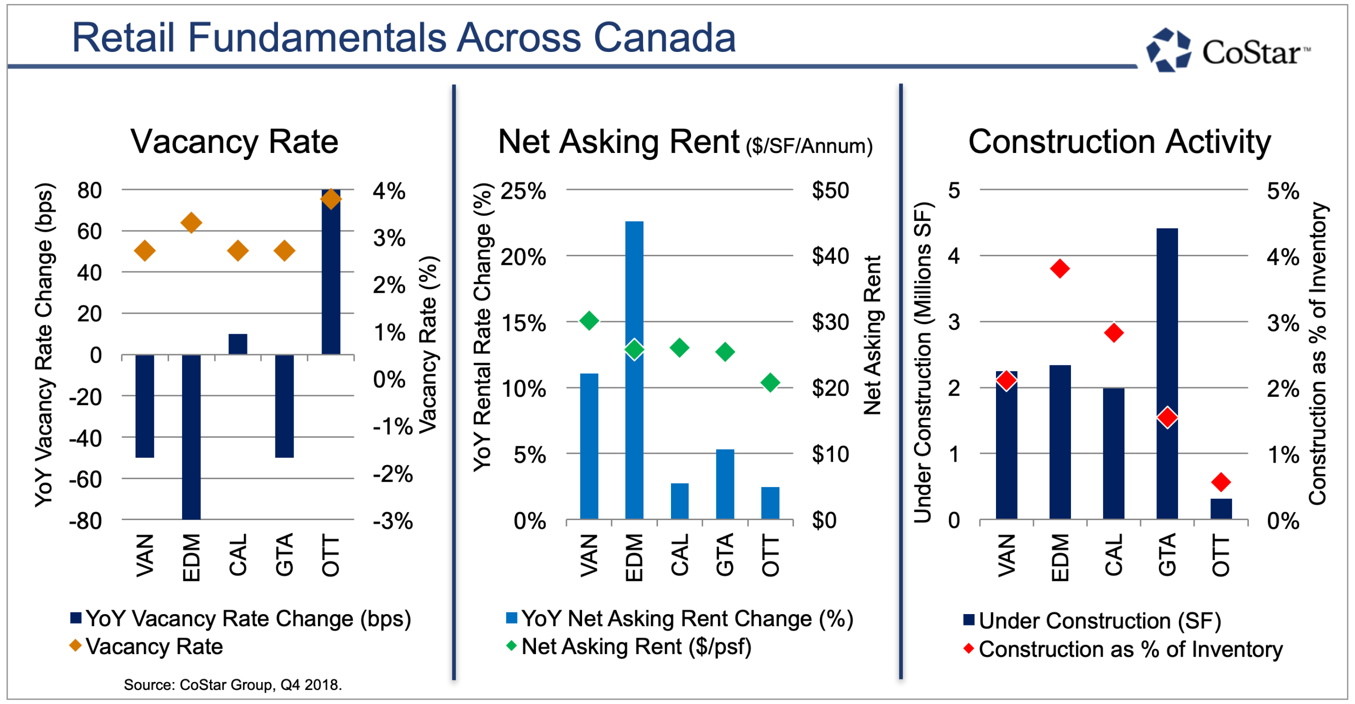


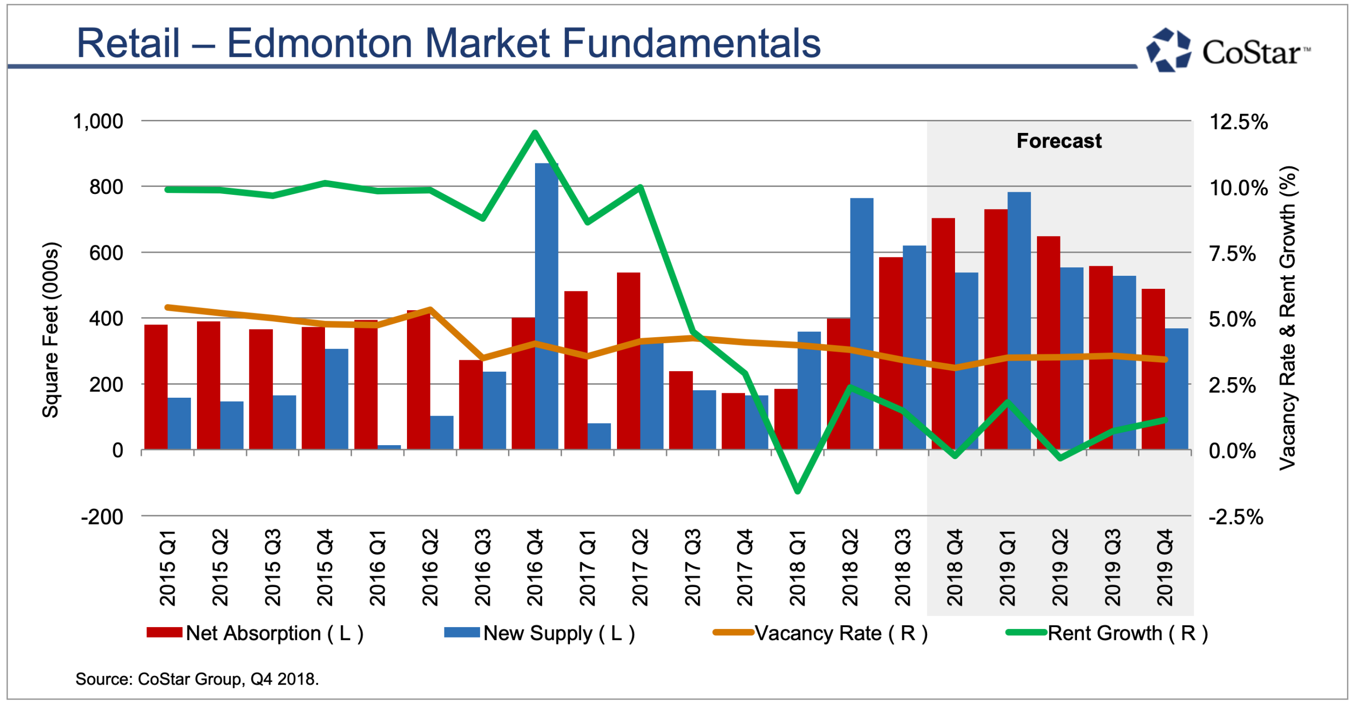
Edmonton Retail Overview

The Edmonton retail market remains strong, with retail vacancy down 80 bps year-over-year to end 2018 at 3.2%, and the average net asking rental rates up 22.6% year-over-year to $25.76/SF per annum. This strong performance was achieved despite the 1.9 million SF of new supply delivered during the same period that Sears closed all of its locations in Edmonton. It should be noted that part of the jump in rents is due to the mix of available space on the market; same store rents have also increased and we have seen premiums in achieved rents in relation to cannabis dispensaries.

Landlords continue to battle e-commerce, with those who are willing and able making capital investments to their properties to differentiate themselves and create more experiential destinations. Expect to see this trend continue, along with more mixed use intensification and repurposing of parking lots in suburban malls going forward. Construction activity remains strong, with 2.3 million SF currently under construction, up from 1.6 million SF at year-end 2017.

Despite the fact that the economy is slowing once again, and that households are trying to get their budgets in order as debt servicing costs increase, retail sales growth in Alberta is expected to remain positive in 2018. However, such growth has slowed dramatically from 7.1% growth seen in 2017. As a result, vacancy is expected to remain in check despite the approximately 2.3 million SF currently under construction, representing 3.7% of the existing retail inventory, and rental rate growth, although volatile over the short term, is expected to remain slightly positive over the coming years.





Ontario saw its economy grow by 2.8% in 2017, and like the rest of Canada, is expected to slow in 2018 and beyond, with 2018 and 2019 GDP growth expected to come in at 2.2% and 2.0%, respectively.

ONTARIO

Ontario Economic Overview

With the uncertainty of the NAFTA/USMCA renegotiations now effectively behind us, we can focus on the economy in general. Ontario saw its economy grow by 2.8% in 2017, and like the rest of Canada, is expected to slow in 2018 and beyond, with 2018 and 2019 GDP growth expected to come in at 2.2% and 2.0%, respectively. Similarly, the Greater Toronto Area (GTA) and Ottawa-Gatineau region are expected to see a slowdown from 3.4% and 2.7% in 2017 to 2.3% and 2.0% in 2018, and 2.4% and 1.8% in 2019, respectively. However, both markets will see economic growth remain above both the Ontario and Canadian trend rates.

Growth in sectors that support the Ontario economy were somewhat mixed in the first three quarters of 2018. On the office space side, the Finance and Insurance sectors benefited from growth in depository and credit intermediation services. However, in regard to the other side of the FIRE sector, Real Estate was up in the third quarter of 2018 but activity remained well below that seen in late 2017, just prior to the new mortgage rules came into effect. Public administration is expected to slow as a result of Federal government spending plans, which will impact Ottawa specifically; however, the high-tech sector is expected to continue growing in the GTA and Ottawa, driving demand for space. On the industrial space side, manufacturing, transportation and warehousing, as well as the construction sectors, all experienced declines in the second half of 2018. Construction activity was down overall due to decreased residential construction, whereas the drop in manufacturing was partially as a result of temporary shutdowns of some automotive assembly plants and a slowdown in metals due to a decrease in international demand following the tariffs put in place by the U.S.

The long term trend of a declining importance of manufacturing to Ontario's economy was further exacerbated by the recent announcement that GM will be closing its Oshawa assembly plant at the end of 2019. Ultimately the automotive manufacturing sector will not see much positive impact from the renegotiated USMCA deal, considering the deal only requires 40% of car parts to be made by workers who are paid USD$16 per hour or more, whereas the average wage of a labourer at the Oshawa assembly plant is CAD$32 per hour, or US$24, as of Nov. 30, 2018.

It should come as no surprise that with a slowdown in economic activity, employment growth has also weakened in 2018. However, employment growth is still expected to come in at 1.6% in Ontario, well above the national average of 1.2%. With the unemployment rate expected to be at 5.6% as of the end of 2018, employment growth is increasingly hard to come by.

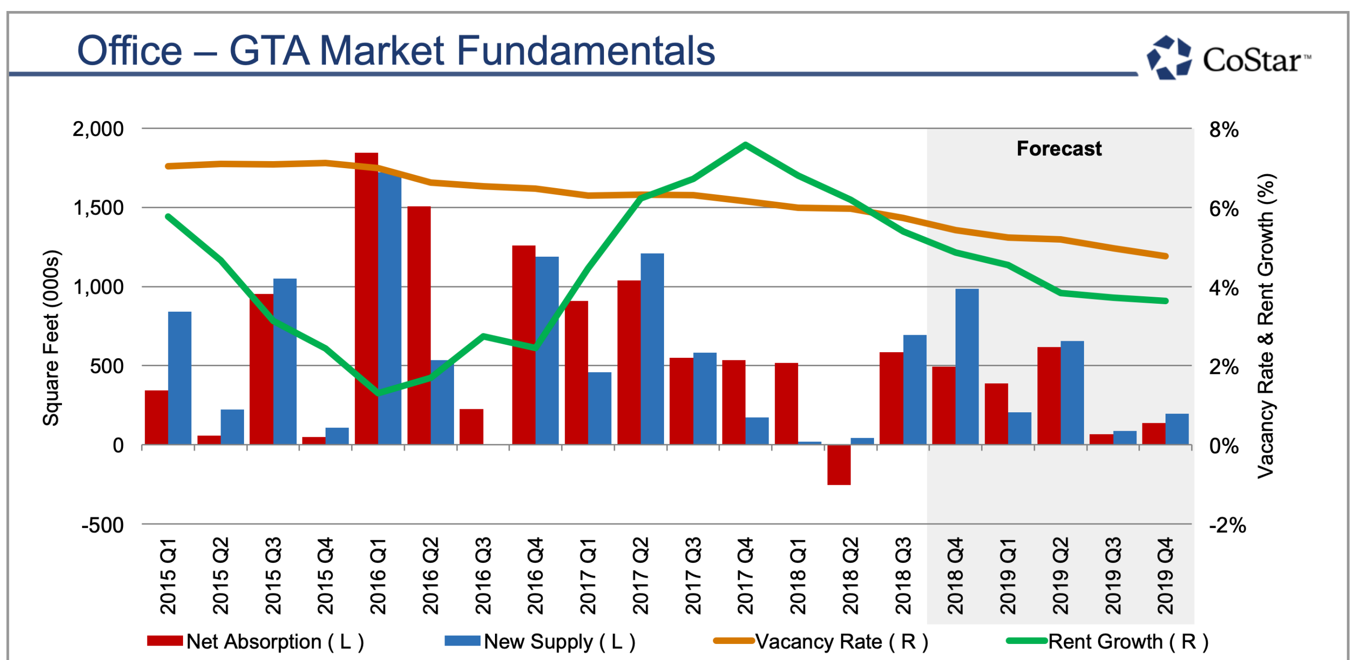
Once again, the impact of higher interest rates on household budgets cannot be understated. Although income growth has started to pick up, rising interest rates are increasing debt servicing costs, and this along with the slow housing market and slowing economy are starting to impact consumer confidence and retail sales. TheBoC, which has been and is expected to continue increasing the Overnight Rate from the current 1.75% to 2.50% by year-end 2019, has acknowledged that retail sales per capita is slowing and by virtue households are experiencing stress due to higher interests rates. When you adjust for inflation, retail sales growth in 2018 has been weak, and the BoC is hanging its hat on the assumption that although retail sales per capita will be weak, total retail sales will continue to grow primarily due to population growth.

GTA Office Overview

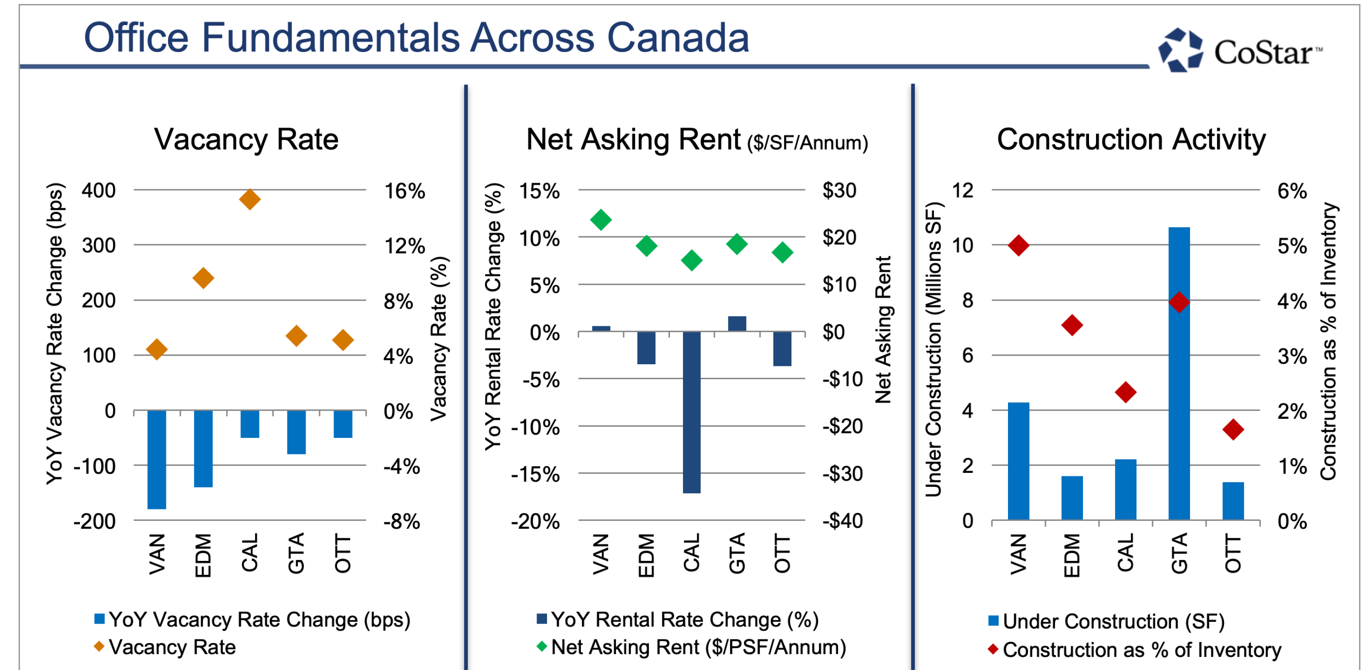
The GTA office market is experiencing exceptionally strong performance and is deeply entrenched in landlord control. The overall market vacancy rate is down 80 bps year-over-year to end 2018 at 5.4, with the average net asking rental rate up 1.6% over the same period to $18.50/SF per annum. With strong demand from finance and technology companies that continues to drive vacancy down, rental rate growth is expected to remain above 2% until approximately 2021, just after the next wave of new supply starts coming online.

There are currently only nine existing properties in the GTA that can accommodate a tenant looking for 100,000 SF or more of contiguous space. The good news on the supply front is that construction activity continues to increase, with approximately 10.5 million SF now under construction or about to kick off, representing 4.0% of existing inventory. These projects include CIBC Square at just under 1.6 million SF with CIBC as the lead tenant; the 1.2 million SF office project at 160 Front St. W., which was announced by Cadillac Fairview in June, 2018 with the Ontario Teachers' Pension Plan as the lead tenant; and the 829,910 SF speculative project at 16 York St., also being developed by Cadillac Fairview. Furthermore, Oxford Properties continues to market its proposed 1.4 million SF (60-story) office tower, The HUB, at 30 Bay St. Although there is a mountain of new supply in the development pipeline, it should be noted that this new supply will do virtually nothing to alleviate the tight market conditions until it starts being delivered between 2020 and 2022.

Downtown vacancy remains exceptionally tight, at 3.2% at year-end 2018, and although this is down 50 bps year-over-year, it is up 20 bps from Q3 2018, whereas the suburban market vacancy rate has decreased by 100 bps year-over year, to 6.5%. Although suburban vacancy is now falling faster than downtown vacancy, with the delta between downtown and suburban vacancy narrowing from 380 bps a year ago to 330 bps at year-end 2018, there continue to be many opportunities in the suburbs for tenants who do not need to be downtown. Furthermore, tenants will likely need to pay more attention to the suburban markets if they need a large amount space before 2020. With demand remaining strong, and new supply limited in the short term, expect rental rates to continue edging up.



Source: CoStar Group, Q4 2018.



Source: CoStar Group, Q4 2018.

Office Market Contiguous Space

If you're looking for 100,000 SF in Vancouver or Edmonton today … good luck!

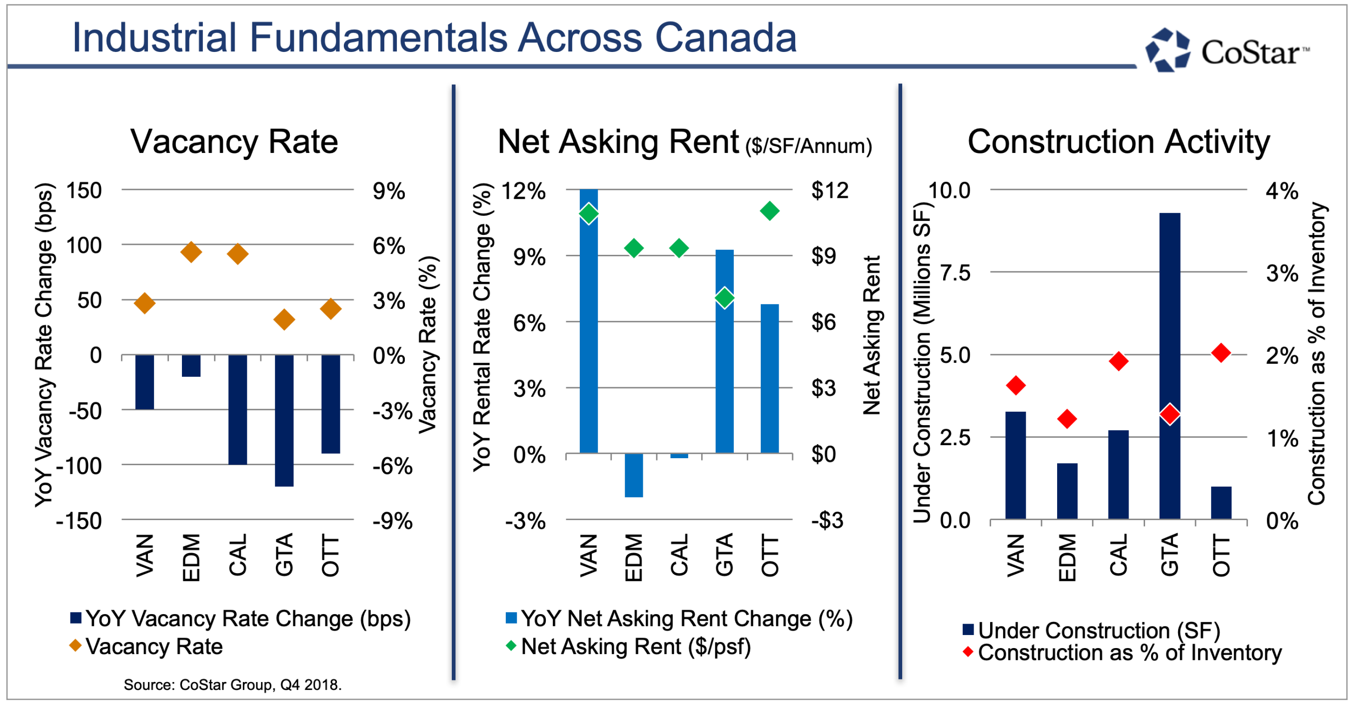
MARKET	BUILDING STATUS	VANCOUVER	EDMONTON	CALGARY	TORONTO	OTTAWA
>100,000 SF	Existing	0	0	14	9	1
	Under Construction	3	0	1	7	0
	Proposed	3	1	10	27	4
	Total	**6**	**1**	**25**	**43**	**5**
50,000 SF < 100,000 SF	Existing	2	6	35	32	5
	Under Construction	3	0	2	11	0
	Proposed	3	1	13	34	10
	Total	**8**	**7**	**50**	**77**	**15**

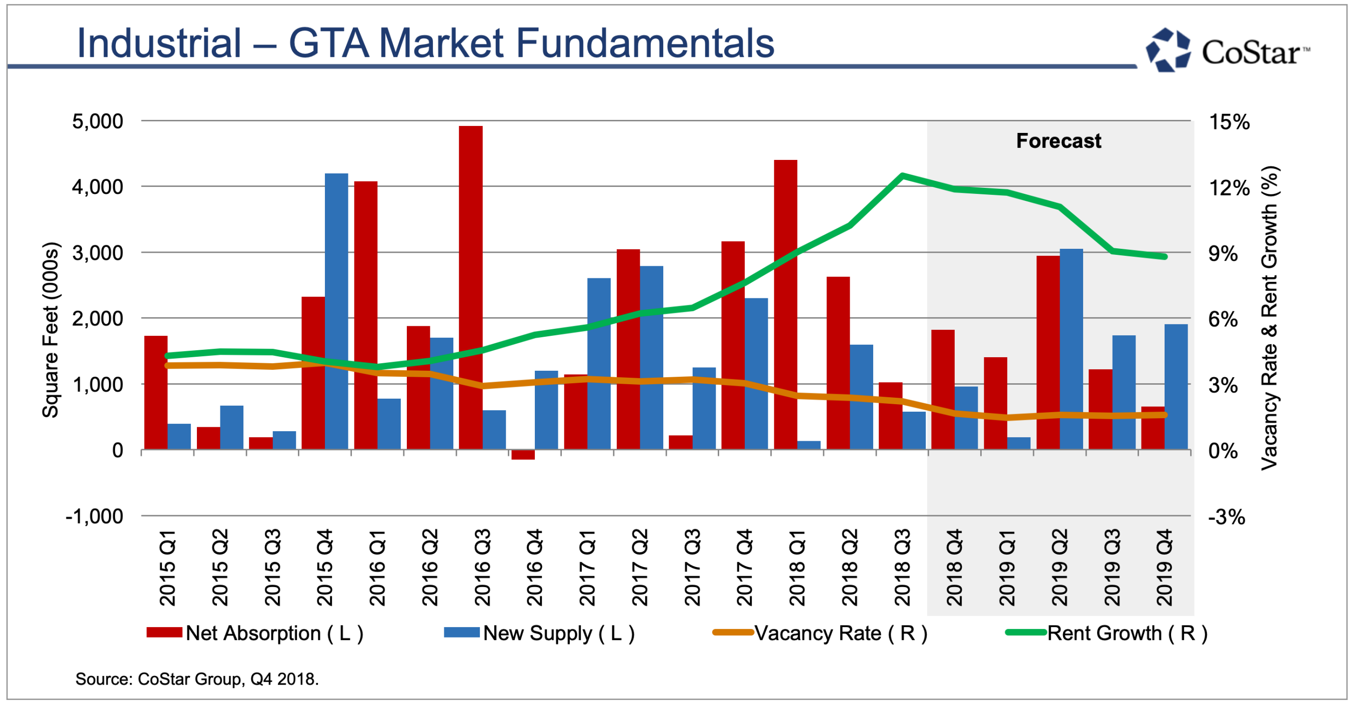
Source: CoStar Group, Q4 2018.

GTA Industrial Overview

Despite the bad news on the manufacturing side, the GTA industrial market, which is being driven by the transportation and warehousing sector, has experienced continued strong demand. Overall GTA vacancy has decreased by 120 bps year-over-year to end 2018 at 1.9%. To keep up with demand, construction activity has been equally strong. There has been approximately 5.0 million SF of new supply delivered over the last year, with an additional 9.5 million SF currently under construction.

Unfortunately this construction activity has not been enough to keep up with demand, and furthermore, the GTA is now facing land shortages, which will impact the amount of future construction activity. Projections show that the GTA industrial vacancy rate will continue edging down to approximately 1.3% to 1.5% early in 2019, before starting to climb slightly back above the 2.0% range by 2020. There remains strong demand from transportation, warehousing and logistics tenants, as well as non-traditional tenants focused on film and cannabis industries, and as a result of this strong demand and limited supply, the average net asking rental rate continues to increase, up 9.3% year-over-year, to $7.07/SF per annum at year-end 2018.



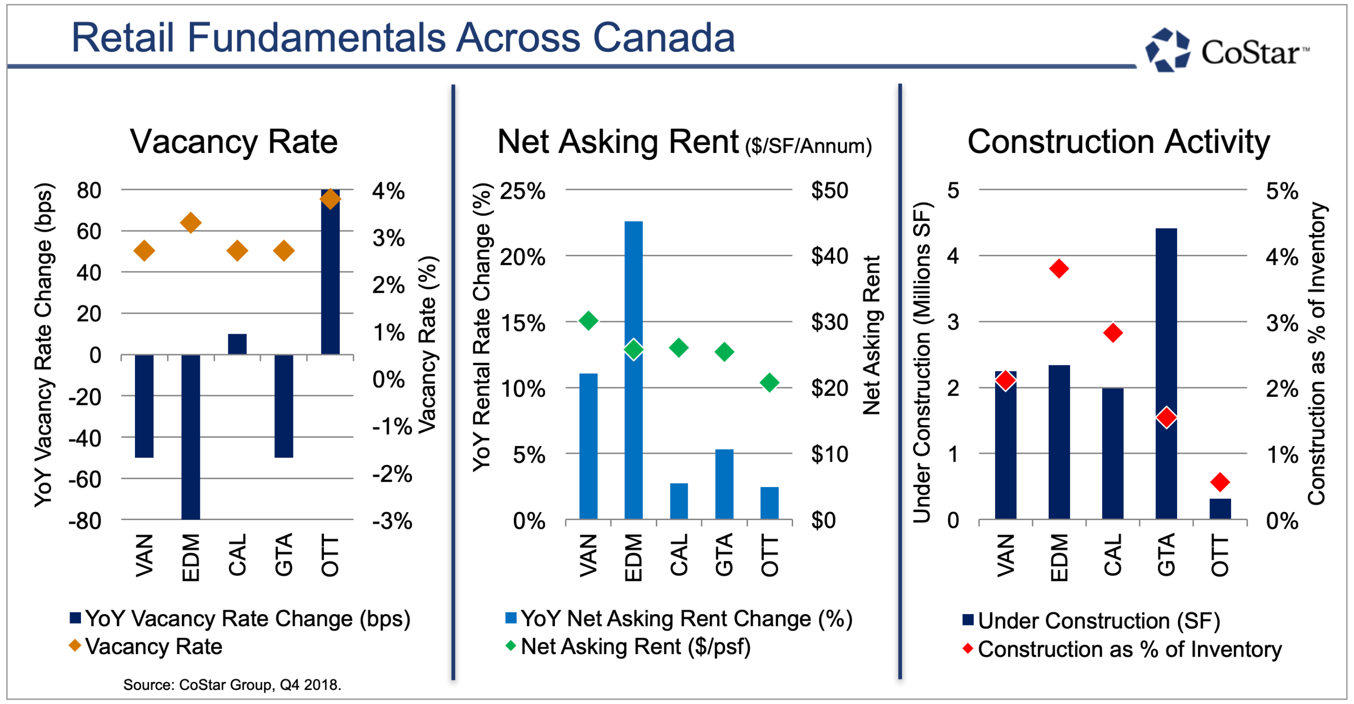


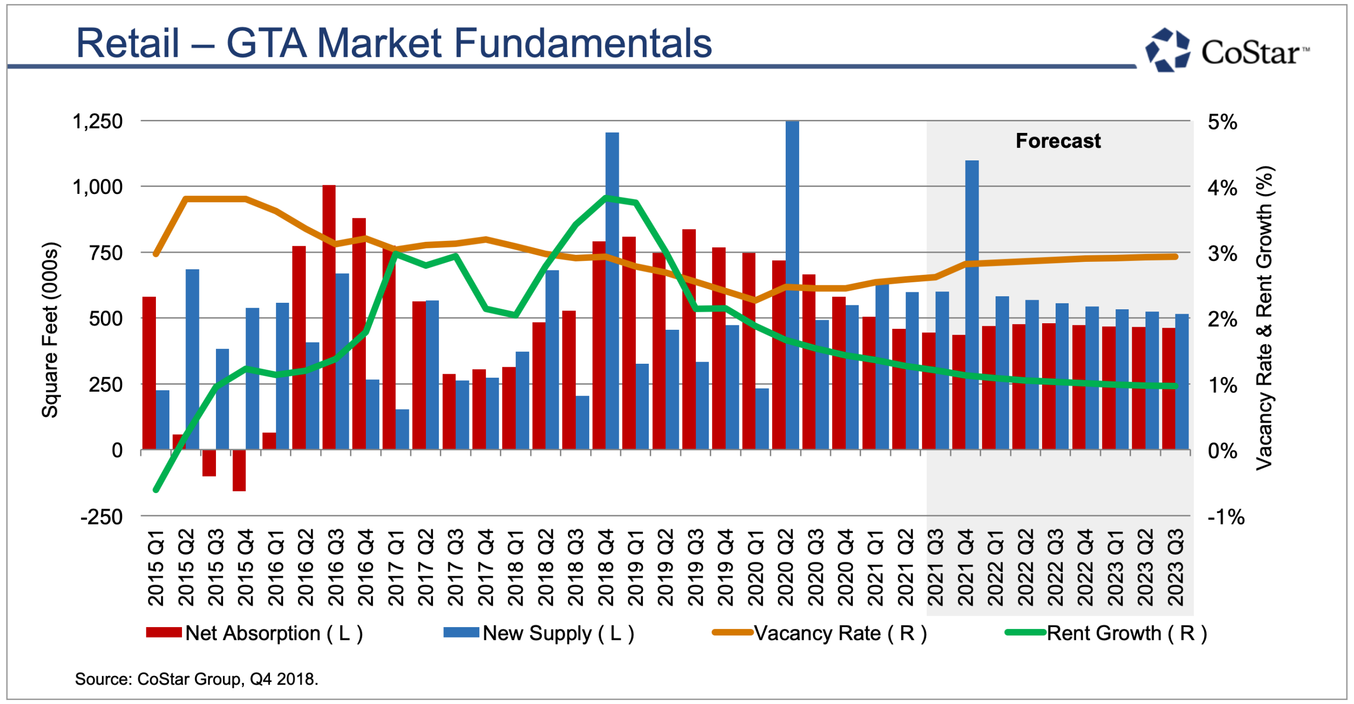
GTA Retail Overview

Similar to Vancouver, the GTA retail market continues to receive new international retailers who are either looking to enter the GTA market, or are using the GTA as a launching pad to reach the rest of Canada. The GTA retail market vacancy rate has edged down, by 50 bps year-over-year to end 2018 at 2.7%, with the average net asking rent up 5.3% over the same period to $25.40/SF per annum. Construction activity has been relatively slow, with only 1.5 million SF of new supply delivered over the past year, and construction activity is virtually unchanged from year-end 2017, at 4.4 million SF as of the end of 2018, presenting a mere 1.5% of existing inventory. Despite the new vacant space that came to the market as a result of Sears Canada closing in Q1 2018, the limited amount of new supply is not enough to satisfy the demand from tenants who are struggling to find space amid low vacancy and increasing rents. As a result of this demand, vacancy is expected to actually decrease to approximately 2.5% before once again increasing in 2021.

Despite the impressive fundamentals, there are some clouds on the horizon. The latest national GDP data indicates that retail activity has come off the boil. Furthermore, retail sales have been showing weakness for some time, with much of the total increase as a result of inflation and population growth. Although retails sales growth is expected to remain positive, higher interest rates, which are expected to continue increasing in 2019, along with increasing debt service costs will take a bite out of retail sales. As a result, GTA retail sales are only expected to increase by 0.6% in 2018 but then rebound to increase by 1.4% in 2019, compared to 5.0% in 2017.

In order to combat the effects of e-commerce on the retail market, landlords of premier quality properties continue to work on turning them into experiential destinations. Such an endeavor often goes beyond simply adding more restaurants and services in malls. It can also include ventures such as Ivanhoe Cambridge and Cirque du Soleil, who have teamed up to offer family entertainment centres in shopping centres, due to launch in 2019. Landlords are looking at ways to further differentiate themselves from the rest of the pack in order to attract more shoppers as well as new and better retailers. Expect to see intensification of retail properties and repurposing of parking lots in suburban malls (Yorkdale Mall being one example), and redevelopment (like Aoyuan's plans for Newtonbrook Plaza).

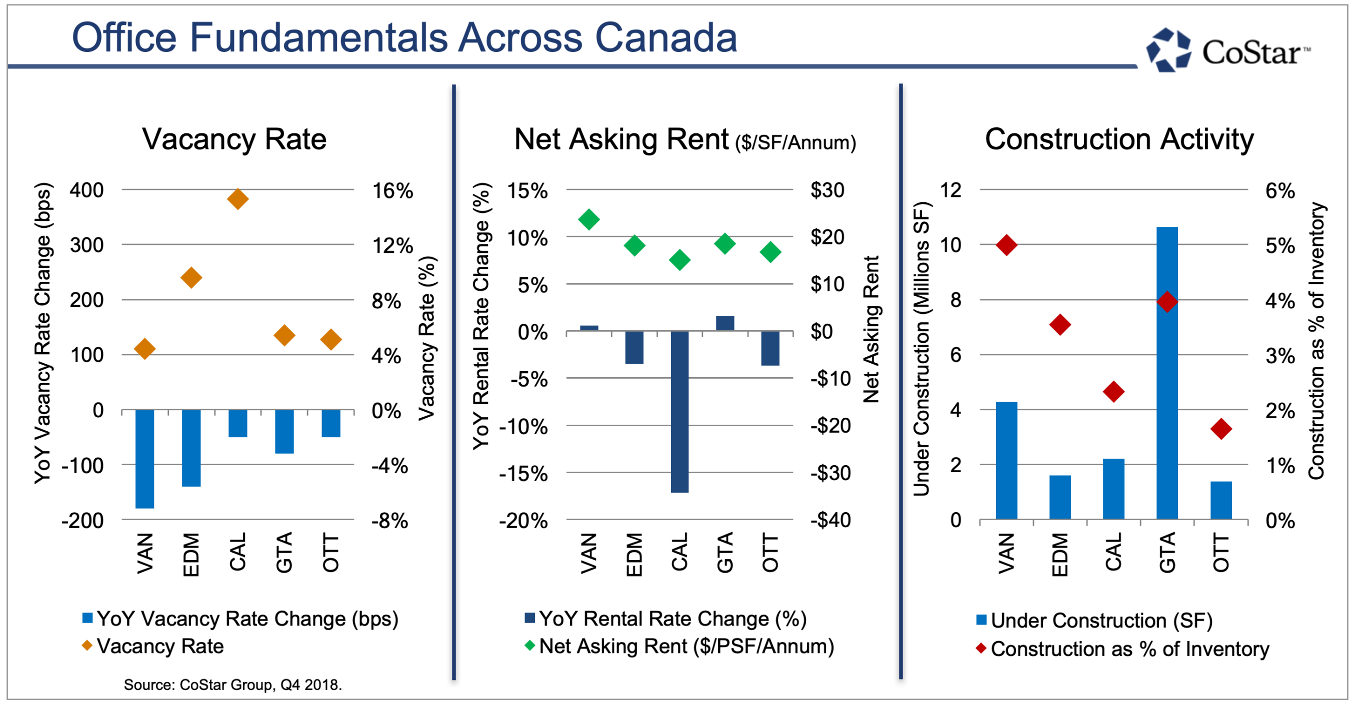


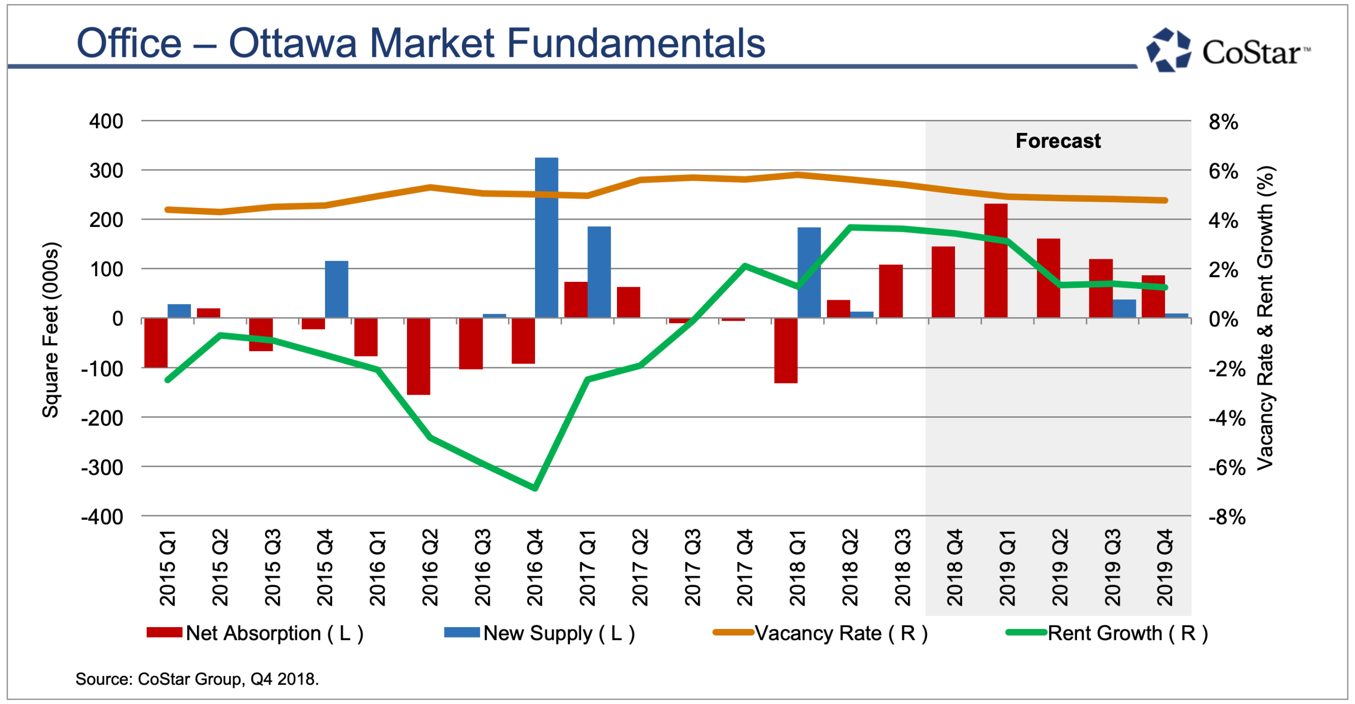


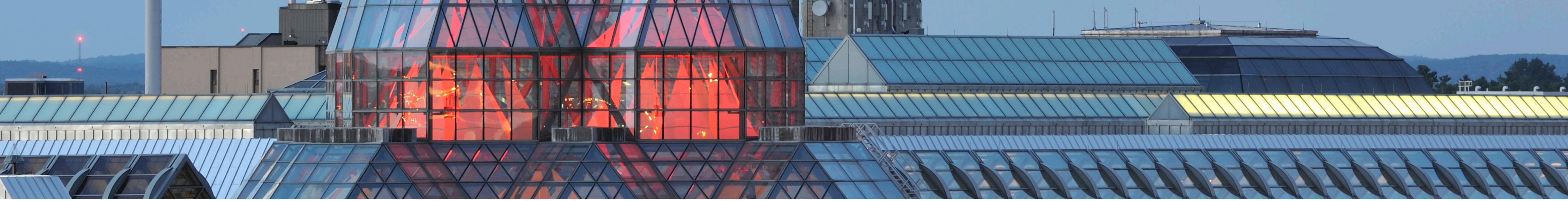
Ottawa Office Overview

Ottawa commercial real estate is experiencing a renaissance, with renewed interest in redevelopment or development opportunities along the LRT line and other well located properties. Although the LRT grand opening has been delayed to 2019, buildings with direct connections – or even just located along the route – are experiencing stronger demand, lower vacancy and better rent growth than those off the beaten track. Overall vacancy is down 50 bps year-over-year to 5.1%, however, net asking rents are also down, -3.7%, to 16.73/SF/annum. Construction activity has picked up, with 1.4 million SF under construction; however, this only represent 1.7% of the existing office inventory. Of the projects that are under construction, or planned, most are generally part of larger mixed-use projects, with only a portion slated to be office space. Take, for example, 900 Albert St., which is a mixed-use and transit oriented development comprised of 200,000 SF of office space, as well as 125,000 SF of retail and residential space. Like many of these projects, 900 Albert St. is located along the new Confederation LRT Line.

High-tech companies and the Federal government have long been part of the office market tenant mix in Ottawa, with the Federal government choosing to occupy more space in the suburban markets over the last few years. This has resulted in higher vacancy downtown – which equates to opportunities for high-tech tenants who might be looking for more urban locations with access to public transit. Expect demand to outstrip supply in 2019, with vacancy continuing to edge down.



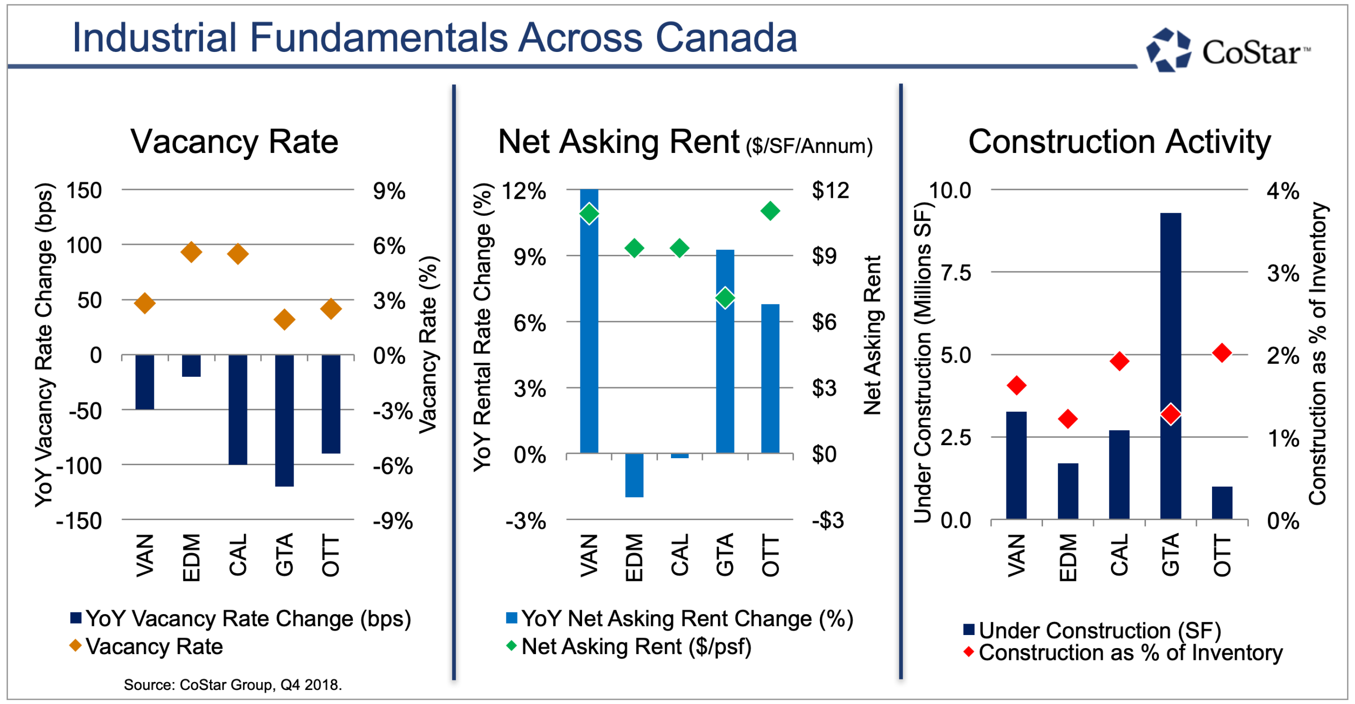


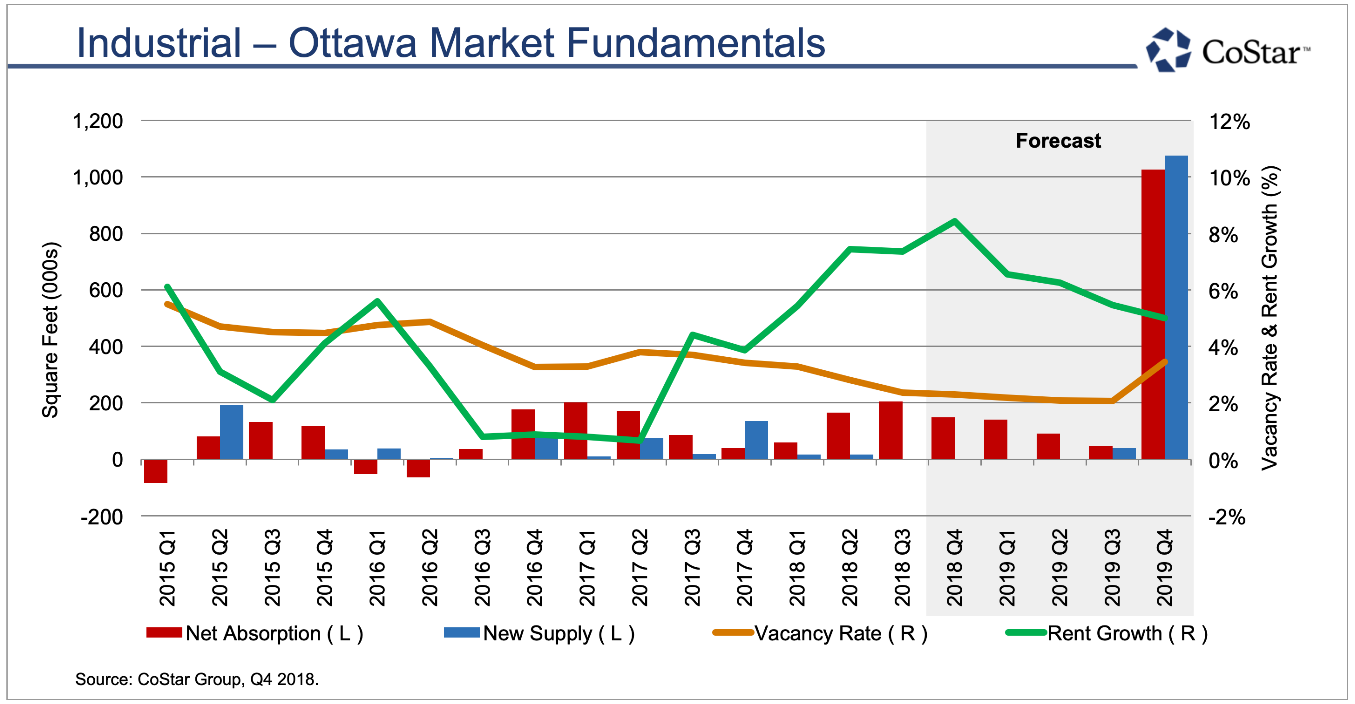


Ottawa Industrial Overview

The Ottawa industrial market has experienced relatively strong demand throughout 2018, but virtually no new supply. As a result, the vacancy rate has decreased by 90 bps year-over-year to end 2018 at 2.5%. Furthermore, net asking rents climbed 6.8% to $11.02/SF per annum over the same period. On the construction front, there is now 1.0 million SF under construction. However, this represents just one project: Amazon's new Ottawa fulfillment centre at 5371 Boundary Rd., just off of Highway 417. Both Broccolini and the City of Ottawa hope that this project will bring new life to the South Industrial submarket and kick of more new construction in the area.

Tenants in the market continue to be construction companies, but also microbreweries and cannabis companies. Looking forward, construction activity is expected to pick up in order to satiate the demand. However, this is not yet occurring, and as a result the market is expected to continue tightening in 2019, with strong rent growth above 5.0%.

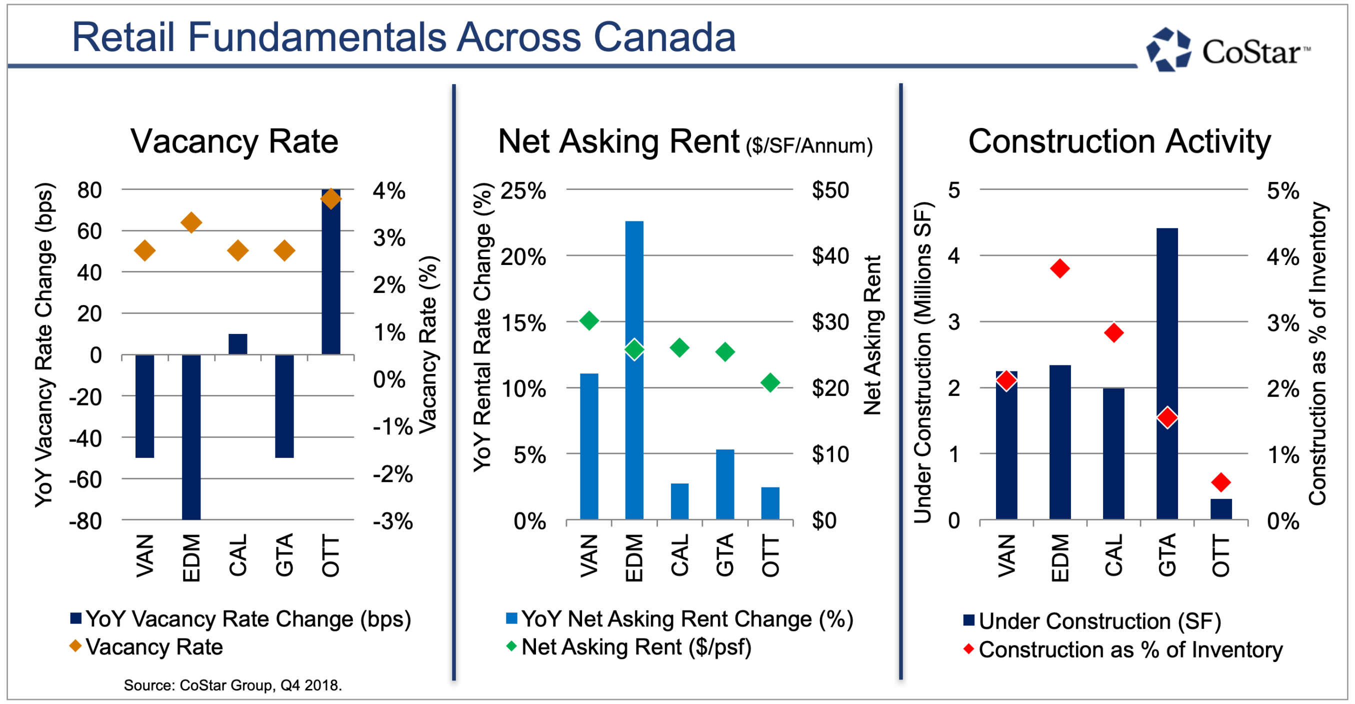


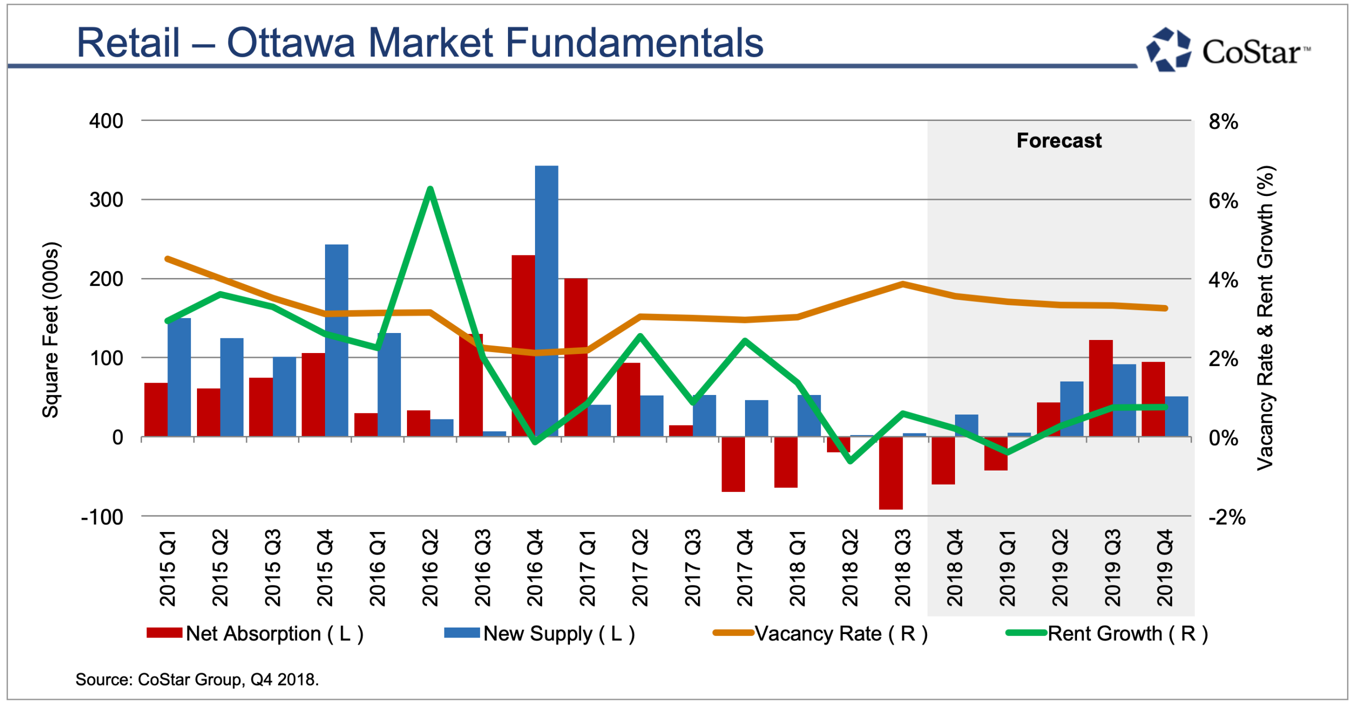


Ottawa Retail Overview

The Ottawa retail market has experienced an uptick in vacancy, primarily a result of Sears vacating three locations earlier this year. Vacancy is up 80 bps year-over-year to end 2018 at 3.8%. As a result, average net asking rental rates have only experienced a 2.5% increase year-over year to end 2018 at $20.72/SF per annum.

Construction activity remains slow, with only 125,000 SF of new supply delivered over the last year, and only another 313,000 SF currently under construction, mainly associated with the podiums of mixed use residential projects along the new LRT lines. The limited amount of new supply will likely not be enough to satisfy the demand from tenants looking for space. Expect vacancy to move down in 2019, to approximately 3.0%, but also expect limited net rent growth. Part of the overall issue with the retail market remains high household debt and increasing debt servicing costs due to rising interest rates. Expect this to take a bite out of retail sales in 2019. Furthermore, landlords continue to look for ways to differentiate their properties and make them more experiential destinations in order to combat the effects of e-commerce on the retail market, and the Ottawa market has not been immune to this. Expect to see renovations and intensification of retail properties and repurposing of parking lots, specifically along the LRT lines in the coming years.





About the Author:

Roelof van Dijk is a commercial real estate research professional, with over 15 years of real estate experience and 10 years of experience covering the Canadian commercial real estate market. Roelof has authored numerous articles and has appeared in and on BNN Bloomberg, CBC Radio, the Globe & Mail, National Post among others.

Prior to his career in commercial real estate, he worked as a project manager and urban planning consultant for residential developers in the Greater Toronto Area. Roelof holds an MBA with a focus on real estate, and a Bachelor of Urban and Regional Planning degree. He is currently CoStar Canada's Market Economist.

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