

CANADA

# Perspective

■ ■ ■ MID-YEAR 2021

## The great reopening

### INSIDE

Canada's comeback on the vaccine front

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Reopening boost for real estate fundamentals

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Investment activity gains momentum

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# A LOOK AHEAD AT THE MID-YEAR POINT

There's an overwhelming sense of optimism as the rate of vaccination climbs and economies begin to reopen. Canada was slow out of the gate but now leads all G7 countries in rate of first doses and is quickly gaining ground on fully vaccinated rates. Herd immunity will be critical to providing protection against rising variants and preventing further lockdown measures.

Canada's economy proved resilient through the second COVID-19 wave, with growth surpassing consensus expectations. The third wave led to a notable pullback in economic activity in April and May, due to reimposed lockdown restrictions. But the second half of the year is poised to deliver a boom, underpinned by robust fiscal stimulus, businesses and schools reopening, workers returning to the office and expectations for consumers to unleash some of their excess income on leisure and travel. According to Oxford Economics, gross domestic product (GDP) is expected to grow by 6.8% in 2021 and 3.5% in 2022.

U.S. President Joe Biden's fiscal stimulus plans of more than USD \$4 trillion are anticipated to help boost U.S. GDP growth by 7.7% in 2021 (the

fastest rate since 1951) and 4.5% in 2022. Canada's integrated economy should benefit strongly from this activity; however, continued border restrictions are a threat to the health of Canadian businesses. Regardless of the reopening timeline, Canada will benefit from stronger U.S. demand, boosted by infrastructure spending, especially if a more regional approach to global trade evolves.

There are concerns that U.S. and Canadian economies are at risk of overheating, but we believe that most inflationary pressures will prove transitory. Market-based inflation expectations have begun to unwind, and the yield curve has flattened. However, supply chain disruptions and capacity constraints may enable strong price pressure to persist in certain segments of the economy, including real estate construction.

The Federal Reserve has signaled a more hawkish tone on interest rate policy, but the market continues to price in a late 2022/early 2023 start to a rate hiking cycle. Should a higher inflation environment persist, commercial real estate is well-positioned to outperform due to

the protections inherent in lease structures hedging against rising costs.

One silver lining from the pandemic has been the rise of high-frequency data to observe economic conditions in real time. Mobility data show a strong snapback in activity once restrictions are lifted. OpenTable reservations indicate that many are excited to get out and socialize. However, there is trepidation about utilizing public transit, which is showing a more measured recovery across large North American metropolitan areas. Lower transit usage is also a function of a slow trickle back to the office (shown in physical occupancy rates), even in cities where economies have been open for months. We hope these types of data will provide early signs to identify or confirm structural shifts brought on or accelerated by the pandemic.



# A LOOK AHEAD AT THE MID-YEAR POINT

Commercial real estate has proven to be resilient, with rent collections and capital value preservation that, so far, has surpassed expectations set at the onset of the pandemic. However, the impact has not been felt evenly across sectors. Enclosed shopping centre valuations have been hit hard, while fundamentals and pricing for defensive, food-anchored strip centres remain strong. The strength of the recovery in retail will be heavily dependent on the health of small business once government support is withdrawn.

The urban multi-family rental market faced sharp declines in occupancy and rents but is beginning to

recover. Meanwhile suburban and secondary markets faced little disruption to demand for apartments as the pandemic accelerated outward migration. Immigration is poised to pick up, as nonpermanent resident permits are on the rise in early 2021. This should support an increase in rental demand.

Industrial real estate pricing continues to soar, driven by strong demand from tenants and investors and an insufficient supply of modern logistics properties.

Ecommerce penetration has accelerated over the past year and will continue to drive leasing activity under historically tight conditions.

The outlook for the office sector remains tepid. Hybrid work strategies are becoming more prevalent, even among many blue-chip companies. But we may see less office space rationalized than sentiment had indicated early in the pandemic. Office fundamentals have softened, and there are indications that the pace of deterioration has slowed. However, it's unclear whether the worst is over or the market is on pause pending a further evaluation of return to office strategies.

Amid renewed optimism, we're mindful of the challenges and risks that lie ahead. With high vaccination rates, Canada is well-positioned to contain

spread of the delta variant, but there is a downside risk to the global economic recovery. After the initial household splurge to celebrate the great reopening, will Canadian consumers continue to spend, especially with elevated household debt? How will inflationary pressures influence interest rates policy and the impact for real estate and valuations? We'll unpack these issues and more in the following mid-year outlook.



# QUICKTAKE: SECTOR OUTLOOKS OVER THE NEXT 12 MONTHS

BENTALLGREENOAK

CANADA PERSPECTIVE | MID-YEAR 2021

CANADA					U.S.				
	Operating Fundamentals	Investor Sentiment	Overall Outlook	In Short		Operating Fundamentals	Investor Sentiment	Overall Outlook	In Short
Office	Mixed	Mixed	Mixed	Rising vacancy, new supply and evolving workplace strategies cloud the outlook. Return to the office in H2/21 should bring more clarity.	Office	Negative	Mixed	Mixed	Uncertainty lingers as the return to office has been slow. Suburbs seeing smaller uptick in vacancy that CBD submarkets.
Retail	Negative	Mixed	Mixed	"Experience-oriented" tenancies will receive short-term boost, but "needs-based" retail remains the active bid for investors.	Retail	Negative	Mixed	Mixed	Investors showing appetite for well-located, necessity-based retail. Nascent optimism that the bottom in values is near.
Industrial	Positive	Positive	Positive	Dearth of industrial product to satiate record demand from tenants and investors. Rents and values should continue to rise.	Industrial	Positive	Positive	Positive	Demand for space grew significantly in H1/21 and continues to outstrip supply. Property values are surging.
Multi-Family	Mixed	Positive	Positive	Evidence of a bottoming in fundamentals is emerging. Attractive financing offers compelling risk/return profile.	Multi-Family	Mixed	Positive	Positive	Rental demand is strong. Significant upward pressure on rents should persist as construction has tapered.

Source: BGO Research

## Outlook Key for Next 12 Months



CANADA

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# ECONOMY

The great re-opening

# CANADA JUMPS FROM WORST TO FIRST ON VACCINATION

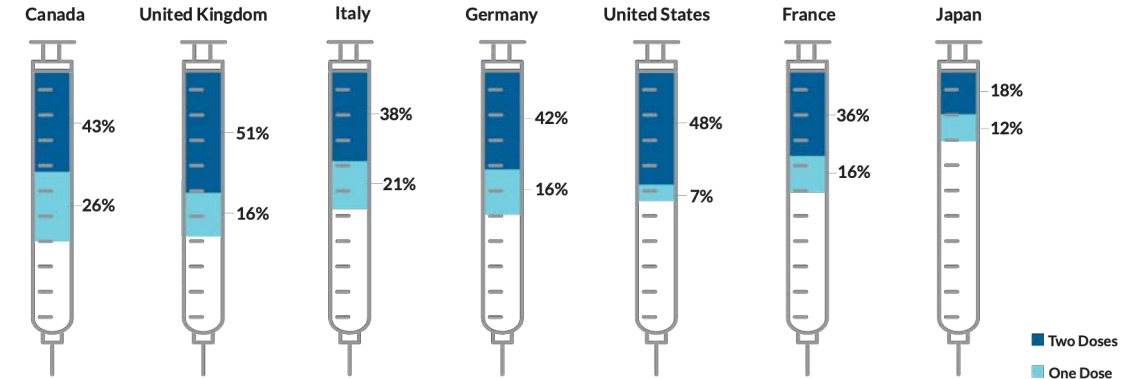
- Half-way through 2021, the Canadian economy is emerging from a third COVID wave and is poised to pick up steam for the remainder of the year as lockdown measures are eased. Economic activity was responsive coming out of the first wave, as consumption and employment bounced back, setting a promising precedent.
- Vaccinations picked up substantially in the spring, as Canadians were eager to get inoculated. At 69%, Canada now boasts one of the highest inoculation rates in the world and ranks second within the Organisation for Economic Cooperation and Development. As of July 11, 2021, 43% of the population had been fully vaccinated and another 26% had received one dose. The one-dose vaccination rate has tapered off for the U.S. and the U.K., but they continue to lead the G7 with the highest percentage of fully vaccinated people.
- The second-dose vaccination rate in Canada is gaining momentum, implying a steady flow of supply and a commitment of Canadians to get fully vaccinated — two key factors in achieving herd immunity and a sustained economic recovery.
- Mobility is an insightful barometer that sheds light on how quickly the recovery may unfold. Previous waves indicated that

households showed little anxiety to re-engaging with society once lockdown measures were eased.

- In British Columbia, Alberta, Ontario and Quebec, mobility trends are beginning to show signs of life as restrictions are lifted. Lockdown fatigue and vaccination could result in a quicker bounce back from the third wave. This bodes well for the demand side of the economy.
- Mobility around retail points of interest has increased in recent weeks and is nearing pre-COVID levels. This signals that households are unwinding excess income accumulated during the pandemic, providing a much-needed boost to the beleaguered services sector.
- Meanwhile, activity around transit nodes and workplaces has been relatively flat throughout the pandemic and remains well below pre-COVID levels, especially within large metro areas. This mainly reflects that a sizable part of the labour force continues to work from home.
- As the economy reopens and consumption gains traction, the next step in the recovery will depend on how quickly the rest of the workforce returns to the office. A revival of urban centres will be a giant leap forward towards full recovery.

## VACCINATION ACROSS THE G7

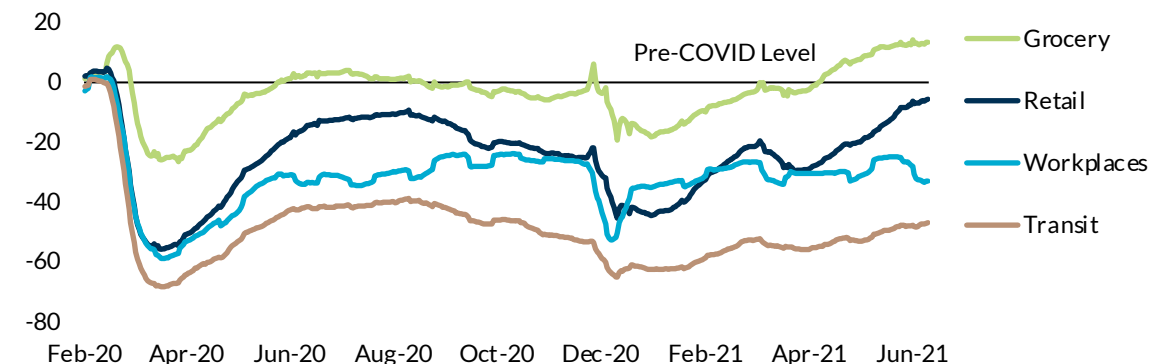
JULY 11, 2021



Source: Our World in Data

## MOBILITY BY POINTS OF INTEREST

JULY 9, 2021, 14-DAY MOVING AVERAGE

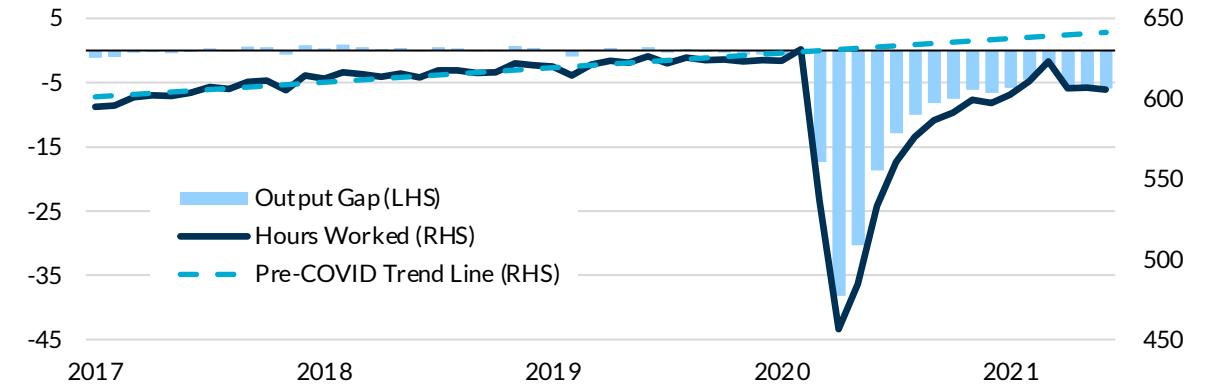


Source: Google Mobility

# HEALTH OF LABOUR MARKET

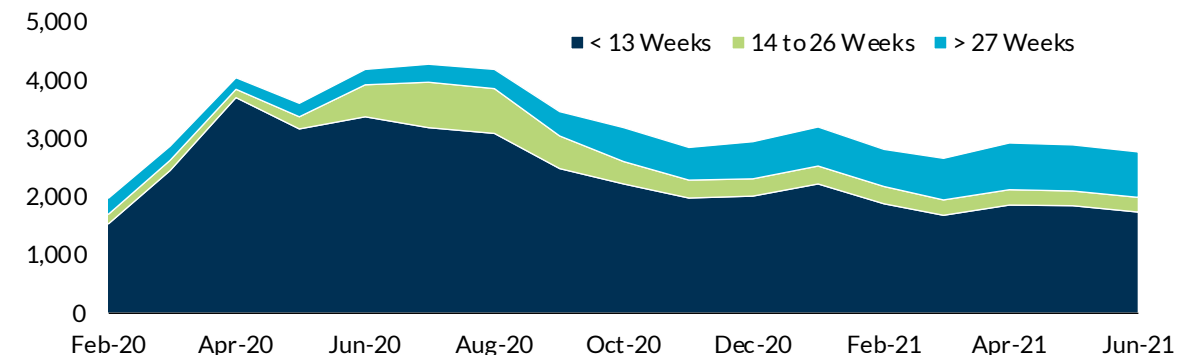
- Near-term monetary policy will continue to be guided by the health of the labour market. Unemployment rate is 7.8% as of June, which is 2.2 percentage points above the pre-pandemic low in early 2020. Consequently, the Bank of Canada is expected to leave interest rates unchanged until late 2022 at the earliest.
- The labour market has been resilient, but there is still plenty of slack. Aggregate hours relative to the pre-COVID trend have narrowed substantially but have yet to fully recover.
- Coming out of down cycles, companies tend to overuse existing labour capacity in the early stages before expanding their full-time workforce. The underutilization rate, which captures people who are available and actively looking for work remains elevated.
- Therefore, long-term unemployment continues to rise as the amount of people who have been jobless for over 27 weeks garners a larger share. This could be a function of government support schemes preventing some from re-entering the labour market, especially considering the ongoing health risks.
- Extended periods of unemployment could widen the skill mismatch and have a lasting impact on productivity beyond COVID. The hospitality sector has been hardest hit and is seeing some permanent closures and downsizing. With a smaller potential labour force, those unemployed in this sector may need to “reskill” to enter other parts of the labour market.
- As we emerge from the third wave, the hospitality sector is poised to get a much-needed boost. Encouragingly, early openings from other parts of the world indicate an eagerness for households to spend. This should support wage growth in high-contact sectors, which have seen an outsized decline in income.
- Large metro areas such as Montreal, Toronto and Vancouver (MTV) were COVID hotspots and saw prolonged periods of lockdowns compared to the rest of the world. Given how quick spending in U.S. cities has bounced back, the MTV markets are expected to see heightened economic activity in the near term. This is especially true for the urban centres, as the professional services sectors begin to resume normal operations. Border reopening will also be a boost for these cities and their services sectors that thrive off tourism.
- Despite a positive near-term outlook, the overall number of jobs remains about 2% from a full recovery. Over the longer term, the health of the labour market in Canada is still highly dependent on immigration — particularly highly skilled workers — to support a thriving tech sector and to backfill an aging workforce.

**LABOUR MARKET PRODUCTIVITY**  
MILLION HOURS WORKED, JUNE 2021



Source: Statistics Canada

**UNEMPLOYMENT BY TENURE**  
THOUSAND PERSONS, JUNE 2021

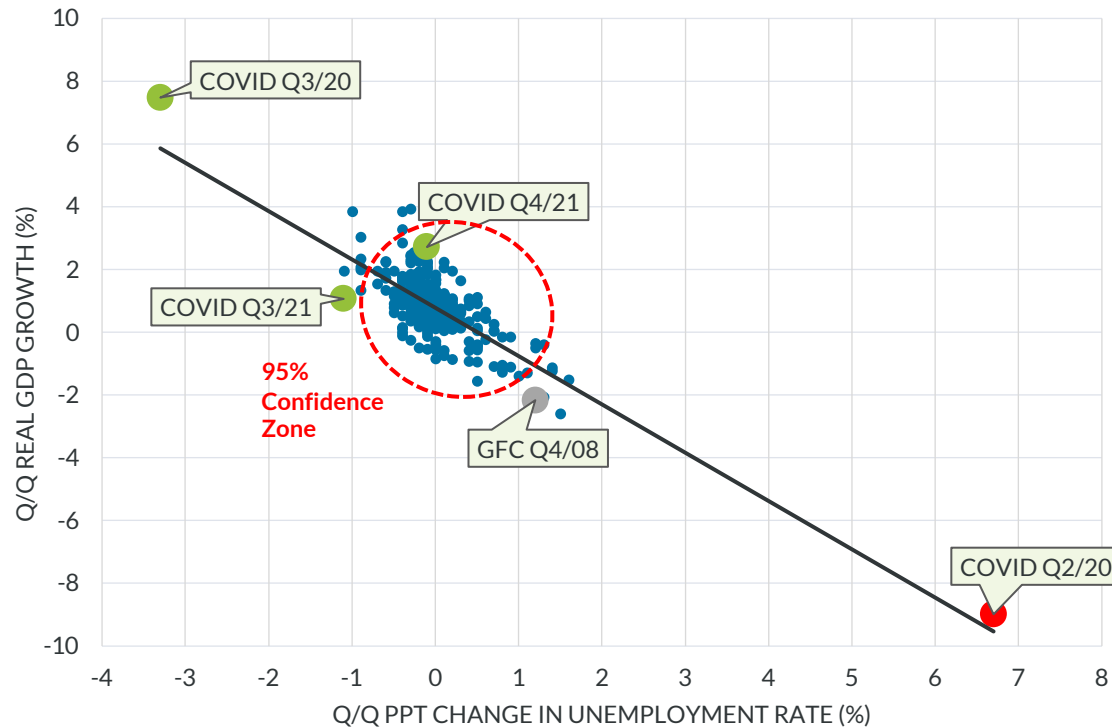


Source: Statistics Canada



# U.S. ECONOMIC RECOVERY LIKE NO OTHER

REAL GDP VS UNEMPLOYMENT RATE  
1948 Q1 TO 2021 Q1

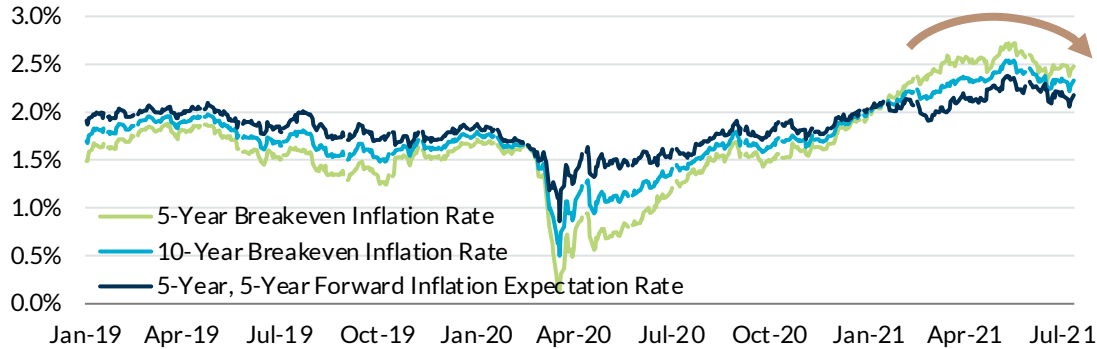


Source: Oxford Economics, Macrobond

- With a much quicker initial vaccine rollout, the U.S. is poised to lead the global recovery. It has experienced a downturn like no other as fundamentals diverged rapidly from trend, even when compared to the global financial crisis (GFC). Encouragingly, the bounce back from earlier waves was just as swift and is a promising sign for the rest of 2021.
- The labour market has made significant progress, but there are still 7.5 million fewer Americans employed compared to February 2020, according to the Bureau of Labor Statistics (BLS). Unemployment has been on a steady decline and is currently at a pandemic low of 5.8% as of May. Initial jobless claims are down significantly, averaging around 400K over recent weeks and well below the 6 million peak in April 2020. This suggests that the pace of layoffs is subsiding as employers hire for the summer travel season and begin to ramp up output in the latter half of 2021.
- Oxford Economics is forecasting 7% real GDP growth for 2021 and 4.0% for 2022. Risks to the outlook are balanced with upside risks from pent-up savings potentially juicing consumer spending, but is offset by downside risks from the spread of the delta variant.
- As of July 11, the full and at least one dose vaccination rates in the U.S. are 48% and 55%, respectively. However, the pace of new vaccinations has slowed, falling to only 400,000 doses per day in June from the April peak of 3.4 million. At 29%, the proportion of people who are uncertain and unwilling to receive a vaccine in the U.S. is one of the highest in the G7. This vaccine hesitancy and the delayed arrival of vaccines for children could pose a challenge to achieving herd immunity.
- With strong trade ties and cross-border activity, the recoveries in the U.S. and Canada are closely linked and will have to progress in unison to some extent. While Canada is nearing the "open-border" vaccination threshold of 75%, the U.S. has tapered off on the inoculation front. This could potentially stall the recovery, as some states with low vaccination rates are currently experiencing a rise in variant cases.

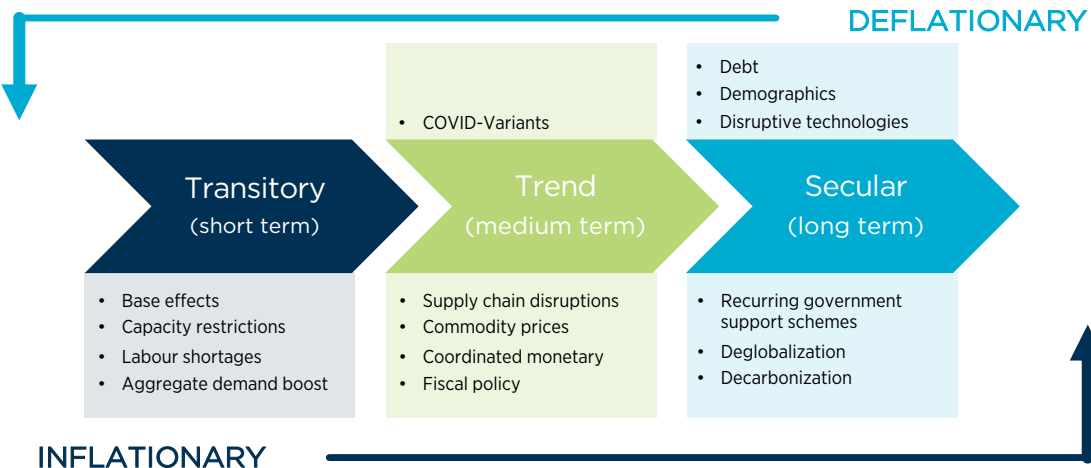
# TRANSITORY OR SECULAR INFLATION?

**U.S. INFLATION EXPECTATION**  
AS OF JULY 12, 2021



Source: Federal Reserve Bank of St. Louis

## INFLATION TUG OF WAR



Source: BGO Canada Research

- Inflation is rising well over central bank targets. The latest reading in June is 5.4% for the U.S. as the Federal Reserve targets “average inflation,” allowing the economy to run hot until there is evidence of a sustained recovery. The same is true in Canada, where the headline consumer price index registered 3.4% year-over-year in May, marking the third consecutive month of above 2% inflation.



- While base effects partly explain the recent inflation surge, extended lockdowns have reduced production capacity, caused supply chain disruptions and created labour shortages, resulting in demand and supply imbalances. These imbalances may be exacerbated in the coming months as consumption picks up, but we expect them to fade into 2022 as the economy gets past the reopening burst and supply catches up.
- The New York Federal Reserve’s Survey of Consumer Expectations for June showed that median inflation expectations over the next 12 months jumped to 4.8%. Similarly, June data from the Canadian Federation of Independent Business show that a shortage of both skilled and unskilled labour is a concern for a rising

share of small businesses, with the unskilled measure at its highest level since October 2018 – a recipe for wage growth.

- To date, inflation has had a limited impact on bond prices. As a result, real estate pricing continues to screen attractive when looking at cap rate spreads over risk-free rates. Cap rate spreads vary by sector but are generally in line with long-term averages. This suggests that there is ample room to absorb increases in bond yields without having a similar magnitude yield impact values.



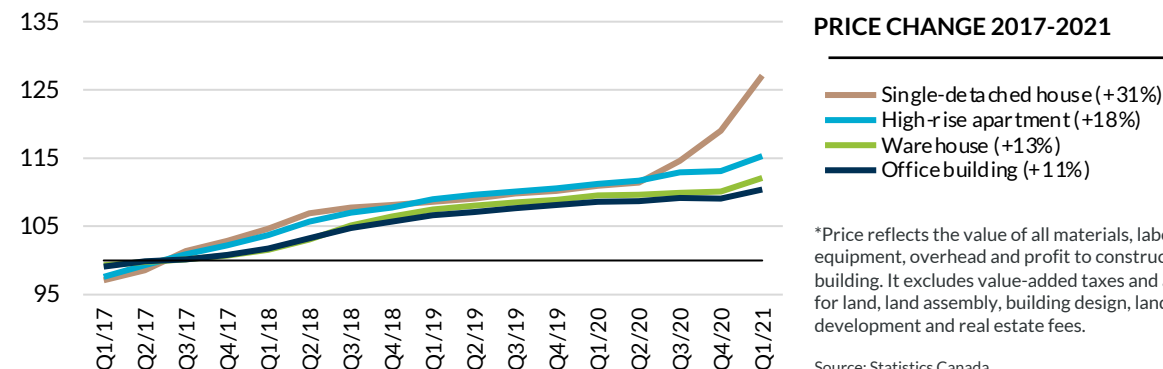
- The market is also beginning to price in lower longer-term inflation expectations, as breakeven inflation rates for five- and 10-year U.S. treasuries have been receding in recent weeks. This suggest that the secular deflationary forces of elevated debt, aging demographics and disruptive technological innovation may be greater than inflationary forces, such as peak globalization, and the future investment required for a transition away from fossil fuels. The big unknown on the secular inflation debate is the potential impact of recurring fiscal stimulus as governments around the world shift towards more sustained budget deficits.

# REAL ESTATE OFFERS INFLATION PROTECTION

- Despite our belief that inflationary forces will be fleeting, should a high inflation environment persist, the inherent characteristics of commercial real estate make it relatively more attractive than other asset classes. Lease structures often include periodic rents steps, and they also often possess the ability to pass on rising operating costs to tenants — two critical components for an effective hedge.
  - However, the type of inflation also matters. For example, cost-push inflation without economic growth (stagflation) makes it difficult to pass through costs without a corresponding increase in tenant demand.
  - Inflation protection also varies across property types. For the reasons noted above, short-duration leases like those found in multi-family rental offer a greater hedge than long-term leases found in office buildings. And importantly, current supply-demand property fundamentals also play a significant role in the strength of the hedge. For sectors such as office and retail, this is a more challenging time.
  - In sectors like residential and industrial, we are seeing the greatest impact on rising construction costs. The linkage between replacement costs and rental rates is more direct in these sectors and should provide a stronger hedge.
- Empirical evidence is scant on the hedging strength of private real estate, especially across sectors, as many private return indices lack sector-level data during periods of high inflation. However, academic research analyzing NCREIF Property Index Returns that start in 1978 (higher inflationary period) has found evidence in the U.S. that diversified portfolios of real estate have been a strong hedge against both expected and unexpected inflation.
  - We analyzed comparable property return data in Canada and the U.S. from MSCI and looked at the corresponding change in capital appreciation compared to increases in the respective Consumer Price Indices (CPI). Though a low inflationary environment was present for the duration of the time-series observed, we found that capital growth outperforms when inflation is above 2% by a noticeable margin. During periods when CPI growth is within the “normal” 1% to 2% range, average capital growth is around the 2% mark and suggests that real estate values tend to align well with the ebb and flow of the business cycle.

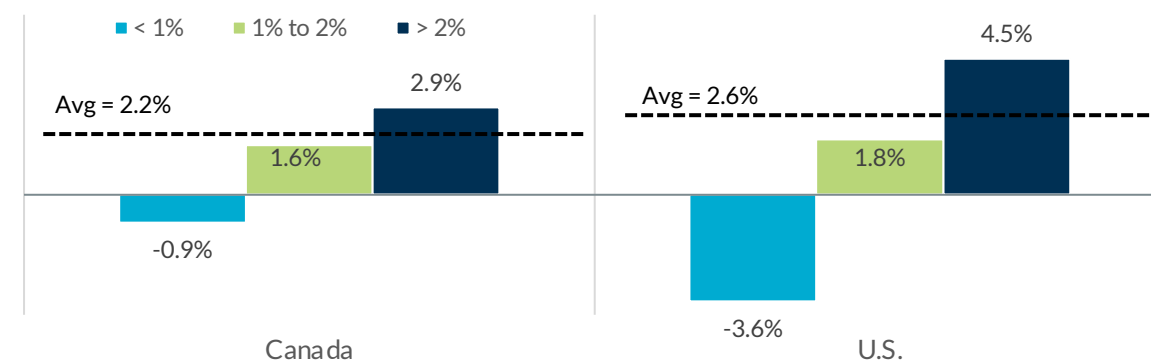
## BUILDING CONSTRUCTION PRICE INDEX\*

11 CANADIAN CMAS, INDEX, 2017=100



## INFLATION VS CAPITAL GROWTH

Y/Y % CHANGE FOR 2000-2020



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# INVESTMENT MARKET

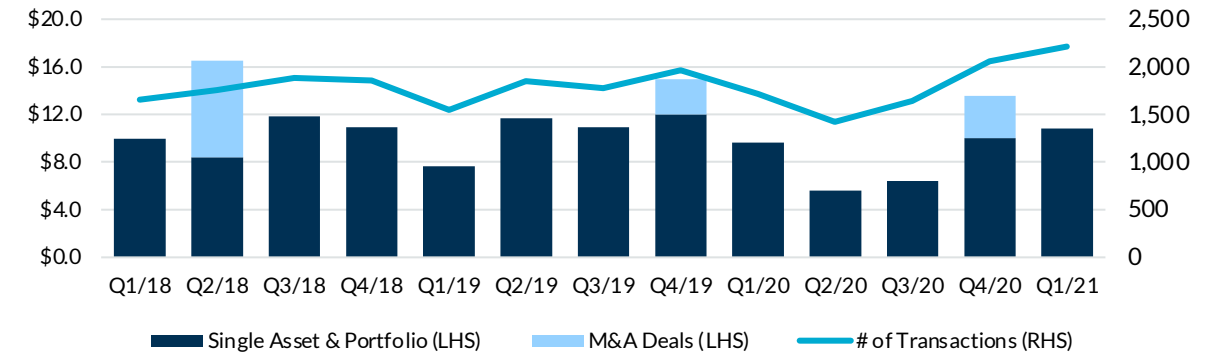
“Transaction activity gains momentum, setting up strong second half of the year.”

# MOMENTUM CARRIES INTO 2021

- Institutional investors were on the sidelines early in the pandemic but got back in the game for the remainder of 2020. This momentum carried over into 2021 and with rising vaccination rates and a stronger economic outlook, investors are expected to be even more active in the second half of the year.
- Canadian commercial real estate transaction activity accelerated in each of the last three quarters, according to real estate firm CBRE. Despite lower deal flows in challenged big ticket sectors such as retail and office, nearly \$40 billion in volume was transacted over the past four quarters. At this pace, CBRE estimates that 2021 is likely to register approximately \$43 billion in volume, the third most active year on record.
- Recent buying activity has been dominated by private investors, who have been active in mid-market transactions (\$25-\$100M). With a higher risk profile and less bureaucracy, they have been able to quickly capitalize on a larger volume of smaller deals compared to their institutional counterparts.
- Preferred sectors for investment continue to be industrial, multi-family and food-anchored retail. As income-producing property pricing has become more fulsome, many investors have turned their focus to industrial and residential land to replenish future development pipelines, where yields are more attractive. Consequently, residential, industrial and land transactions accounted for more than 80% of investment activity in Q1 of 2021.
- We expect a strong second half of the year, as we are seeing larger portfolios brought to market. Investors will likely continue to trim noncore assets after re-evaluating portfolio strategies under pandemic conditions. The past year has highlighted the importance of a diversified portfolio strategy and its ability to reduce volatility and generate steady, predictable cash flows. For many, this will include adding specialized property sectors — such as data centres, cold storage and life sciences — to expand the opportunity set and provide greater resilience to economic downturns.
- In 2020, Canada was the worst performing country in the MSCI Global Annual Property Index, due to its heavy weighting in retail, specifically enclosed malls. Our market expectations for performance have improved for 2021 — with income returns above 4% and capital appreciation that is likely to be flat — to 2%. Much of that performance hinges on the recovery in the retail sector and further price discovery in office.

## CANADIAN COMMERCIAL REAL ESTATE INVESTMENT VOLUME

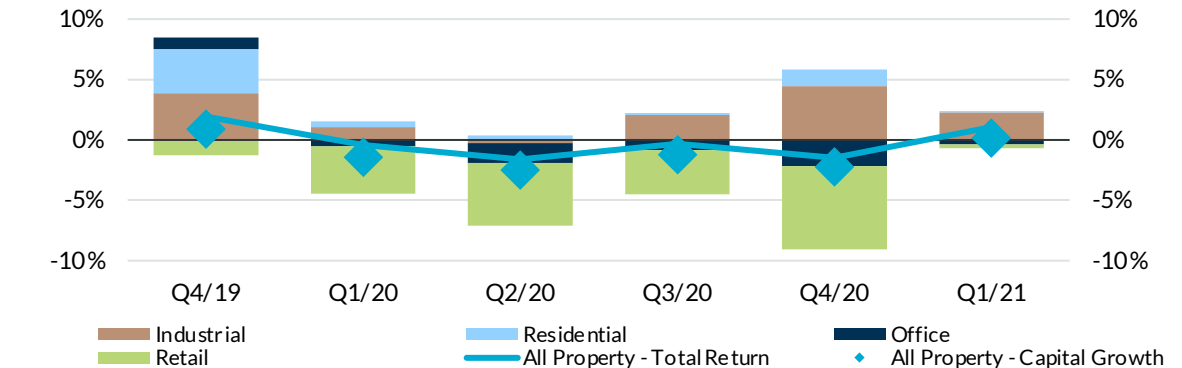
\$ BILLIONS



Source: CBRE

## CANADIAN INSTITUTIONAL REAL ESTATE: CAPITAL APPRECIATION BY SECTOR

% CHANGE Q/Q

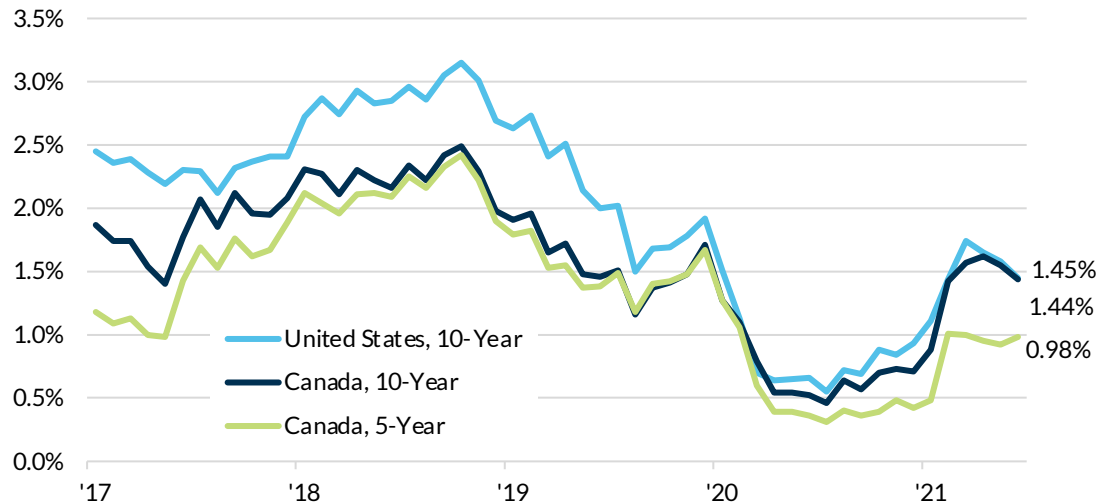


Source: MSCI/REAPAC Canada Property Index

# INCREASED COMPETITION OFFERS ATTRACTIVE DEBT PRICING

- The commercial mortgage market remains highly competitive and is expected to be so for the foreseeable future. Competition is inducing further compression in lending spreads and more favourable structures for borrowers.
- There continues to be strong demand for mortgage financing, as borrowers look to take advantage of favourable market conditions and overall attractive interest rates.
- Lending spreads for high-quality commercial mortgages compressed by 10 to 15 basis points at the low end of the range in the first half of the year but appear to be leveling off. Much like corporate bond spreads, current mortgage spreads are slightly below the pre-COVID level.
- Preferred sectors for lenders mirror those on the equity side. Notably, there is a bifurcation between more fundamentally sound industrial and multi-family and more challenged office and retail.
- However, the gap appears to have narrowed during the past quarter, which we believe is a function of the generally improved market sentiment and necessity for lenders to look outside of industrial and multi-family mortgages to meet their targets.
- Like the equity investment underwriting, environmental, social and governance (ESG) factors are increasingly being incorporated into the loan origination process. This lens is critical to mitigating loan risk, due to the potential obsolescence of the underlying asset security.

## GOVERNMENT BOND YIELDS



Source: MSCI/REAPAC Canada Property Index

## COMMERCIAL MORTGAGE SPREADS OVER GOVERNMENT OF CANADA BOND YIELDS

### Commercial

5-Year Term

**135–75 bps**

10-Year Term

**145–85 bps**

### CMHC-Insured Residential

5-Year Term

**80–95 bps**

10-Year Term

**90–105 bps**

Source: BGO Mortgage Investments, BGO Canada Research

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Perspective on

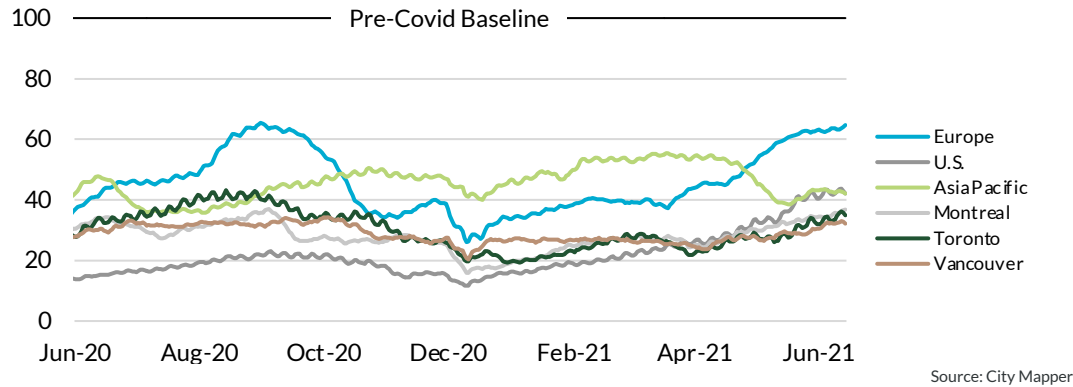
# OFFICE

“Fundamentals continue to soften but is the worst behind us with a return to office?”

# A SLOW TRICKLE BACK TO THE OFFICE

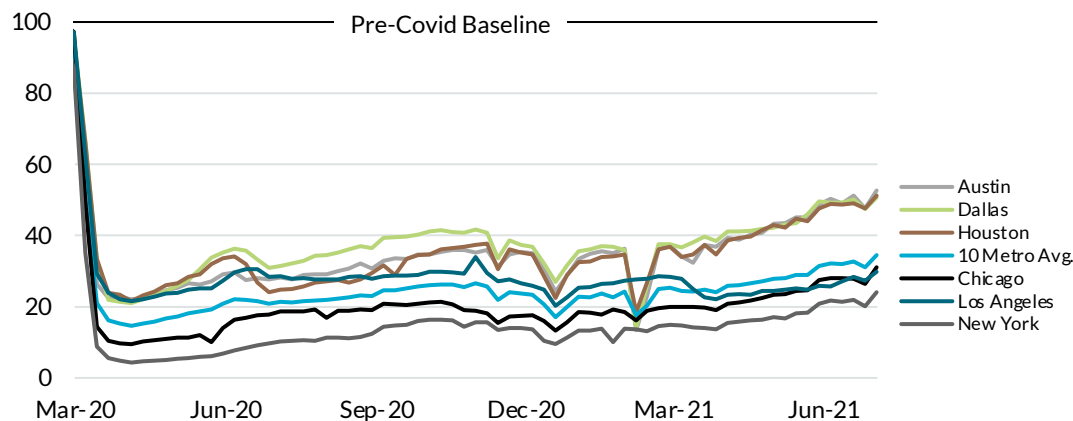
## TRANSIT TRIPS

% RELATIVE TO PRE-COVID BASELINE, JULY 7, 2021



## KASTLE BACK-TO-WORK INDEX

% RELATIVE TO PRE-COVID BASELINE, JULY 14, 2021



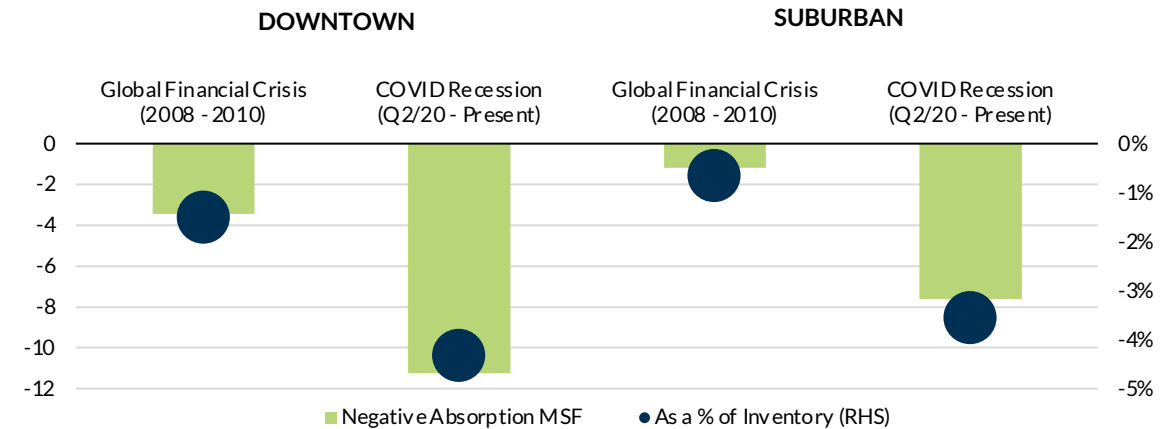
- The health of the office market and recovery in urban areas will depend on how quickly employees return to the office and in what capacity.
- Despite a rise in mobility as lockdown restrictions ease, inflow into urban centres remains well below pre-COVID levels but at varying degrees across global regions. Public transit trip planning data, used as a proxy for urban mobility, highlight that major cities in Europe are much closer to normal levels. Meanwhile, amid a rise in cases and lower vaccination rates, mobility in large Asian cities has slowed of late.
- With a faster rollout of vaccinations, major U.S. cities benefitted from earlier openings, and urban mobility is improving at a quicker pace compared to Canadian cities. Public transit usage in Montreal, Toronto and Vancouver remains well below normal levels.
- A more direct proxy for on-site office occupancy is office key card/access activity. Kastle Systems' back-to-work index indicates that physical occupancy within office buildings is rising across major U.S. metro areas, but at a measured pace. Even in cities such as Houston, Dallas and Austin, which have been open for months, there has been a slow trickle back. These data provide an indication of what may transpire in Canadian cities in the months ahead as economies fully reopen.
- Over the longer term, the health of the office sector is much more uncertain and depends on a myriad of factors that revolve around the evolution of workplace strategies and utilization of space.
- Countless employee-based surveys have indicated an overwhelming desire for a hybrid workplace model. More and more employers are adopting a flexible model. A recent survey of 236 Canadian organizations, by the Conference Board of Canada, indicated that post-vaccine rollout, on average, 52% of the workforce will either be hybrid or fully remote. These figures compare to just 12% before the pandemic.
- It's clear that there will be a shift towards more remote work. But it's also increasingly clear that there is no "one-size fits all" strategy. Each employer strategy will take time to implement, and there's likely to be many iterations to "get it right." As a result, the ultimate impact on office space utilization remains unclear.
- There are a number of factors that will influence the recovery of the office sector, and it will vary across cities. Commute times, industry/tenant concentration, lease maturity cycle and development pipelines will all play key roles in dictating the office sector landscape in a post-pandemic world.



# FUNDAMENTALS DETERIORATING, BUT AT A SLOWER PACE

- Office fundamentals have shifted significantly over the past year, tilting the balance of power in favour of tenants. Negative absorption has already surpassed the level reached in the global financial crisis. Compared to the suburbs, downtown markets have been hit harder, as excess space was shed as workers vacated the core to work from home.
- Downtown vacancy is 14.9% nationally and has now reached the highest level since the real estate crash of the 1990s, having risen 560BPS during the pandemic. Meanwhile suburban vacancy has risen by 510BPS, to 15.7%.
- The rise in vacancy is most pronounced in downtown Toronto, where it has increased by 790BPS, to 10.0%, in just one year. Downtown Vancouver has also experienced considerable upward pressure on vacancy, which rose by 400BPS to 6.6%. Downtown class A has been more resilient to date but has certainly not been immune.
- Headline rents have generally held up well but don't reflect incentives by landlords and the underlying market weakness. According to CBRE, Toronto and Vancouver average net asking rents have declined by ~9.4% and 0.5%, respectively, since the start of the pandemic.
- Tenant-favourable conditions in downtown Toronto and Vancouver are likely to persist, given the 9.3 and 3.5 million square feet (SF) of incoming new supply over the next two to three years. While a sizable portion of this space has been pre-leased, addressing the lower-quality backfill space may prove challenging as remote work weighs on absorption.
- Sublease vacancy spiked to historic levels as many firms looked to downsize their footprint. Encouragingly, the shedding of sublease space has subsided over recent quarters. While some of it has shifted into direct vacancy as leases expire, we are seeing tenants take back space in anticipation of a return to the office.
- Another promising sign is how responsive lease tour activity has been in 2021, up until the latest lockdown measures were introduced. With economies open once again, we expect improving activity to continue. Data from VTS in U.S. markets shine a light on similar trends where lease tour activity has resumed to pre-COVID levels in many markets.
- We see the current environment as the beginning of a "pause" in the market, rather than an inflection point, as firms work on getting back to the office. Only then will they be able to fully assess their space requirements and begin to make more long-term decisions.

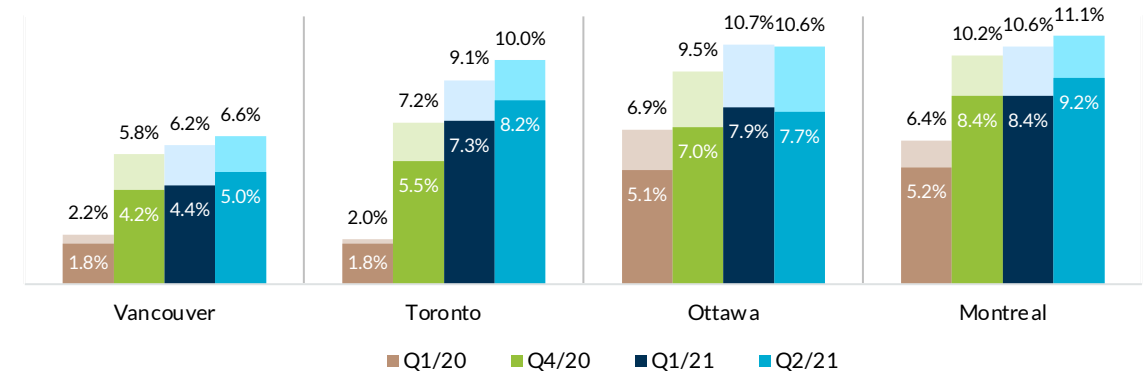
## CANADA OFFICE ABSORPTION: GFC VS COVID RECESSION



Source: CBRE

## DOWNTOWN OFFICE VACANCY

DARK BARS = CLASS A, LIGHT BARS = OVERALL



Source: CBRE

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Perspective on

# RETAIL

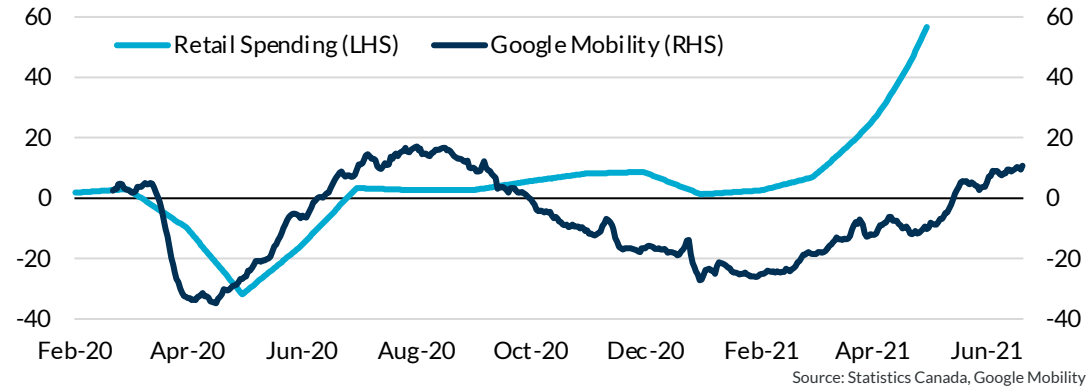
“Consumer spending to shift back towards the experience economy.”



# HOUSEHOLDS LEAD RECOVERY

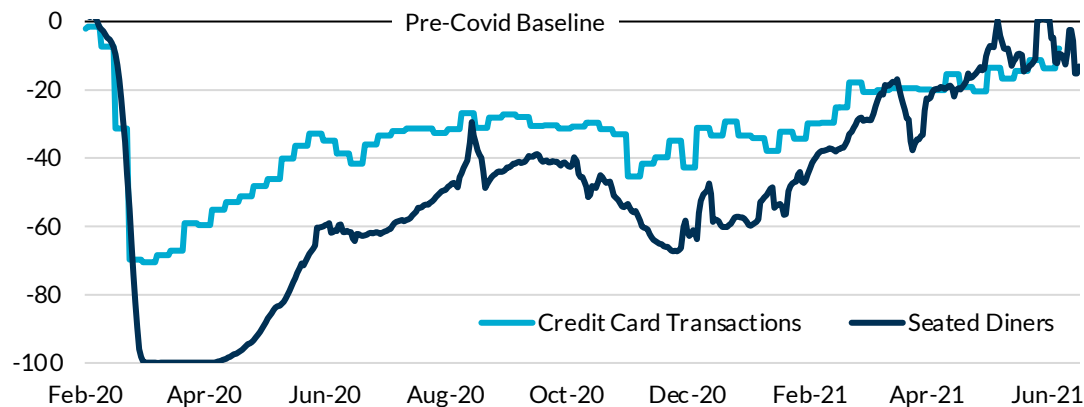
## CANADIAN RETAIL SPENDING VS MOBILITY

Y/Y % CHG



## U.S. FOOD SERVICES SPENDING

% RELATIVE TO PRE-COVID BASELINE



- Mobility in Canada is showing signs of life as cities begin to reopen. Economic growth will be heavily dependent on the consumer in the near term, as housing and commodities have shown signs of cooling and business investment is expected to lag.
- Oxford Economics estimates that there is more than USD \$4.7 trillion in excess savings globally. The improvement in household balance sheets is a function of forced cutbacks on services spending and a variety of income support schemes. Canada has the second highest level of excess household savings, at 11.3% of GDP, next to the U.S. (11.6%). For context, the average for advanced economies is about 6%.
- According to the Bank of Canada, the average household spent \$4,000 less in 2020 relative to trend. Furthermore, Statistics Canada data suggest a staggering \$160,000 per household in net wealth was created since Q4 of 2019, thanks to soaring property values and stock prices. This excess spending capacity is poised to be unleashed over the near term as restrictions are lifted and people venture out to bars, restaurants and live entertainment.
- Retail sales rebounded strongly since the initial lockdowns last spring as retailers adapted quickly to online and curbside pickup. These strong 2020 sales will make 2021 comparisons difficult to beat as consumer spending rotates towards services spending.
- Earlier openings in the U.S. provide an indication of how quickly spending may rebound in services. Credit card transactions on food services and restaurant seatings are close to a full recovery to pre-COVID levels. It's likely that the Canadian consumer will behave with the same enthusiasm, at least in the early stage of the recovery throughout the summer months.
- While a near-term rebound in spending will provide some much-needed relief for the "experience economy," the long-term recovery remains more uncertain, and we believe a more cautious or focused consumer will emerge in a post-pandemic world. Consumers may take a more minimalist approach to their consumption habits, focusing on essentials and daily needs, and they may be much more discerning on discretionary spending and big-ticket items, asking, "Do I really need this?"
- This shift in consumer behavior will have implications for the performance of different retail formats. Those that cater to discretionary spending are likely to face even greater competition for consumers' attention and dollars.

CANADA

Perspective on

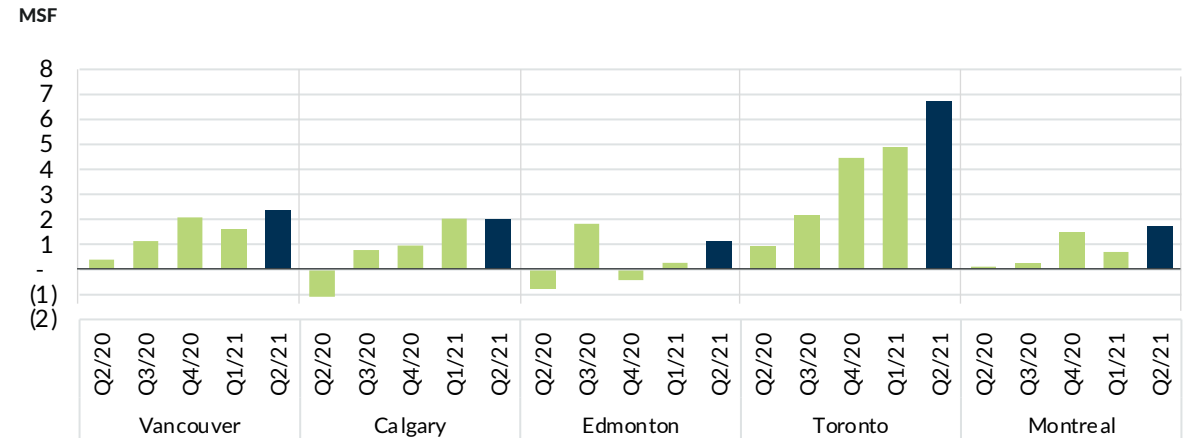
# INDUSTRIAL

“Rising construction activity not enough to satiate demand.”

# STRONG INDUSTRIAL DEMAND PERSISTS

- The industrial market has thrived under pandemic conditions. Q2 of 2021 was the strongest quarter of absorption on record this century. The national availability declined by 60BPS this quarter to 2.3%, the lowest level on record. Average net asking rents continue to face considerable upward pressure, increasing by 7.1% year-over-year to \$9.82 per square foot (PSF), another record high.
- The economic impact of the pandemic was felt unevenly across sectors. While service-oriented sectors were hit hard, the logistics and goods-producing side of the economy faced less operational disruptions. Meanwhile higher-than-normal ecommerce activity drove demand for industrial space, accelerating a trend that was already well entrenched.
- Despite a setback in early 2020, absorption levels rebounded well throughout the pandemic. Much of this strength resided in the Montreal, Toronto and Montreal markets, where distribution channels have grown substantially over recent years to serve their large and growing population bases.
- Montreal (1.4%), Toronto (1.2%) and Vancouver (1.1%) remain the tightest industrial markets in North America, measured by availability. The lack of availability has driven rental rates to historic highs, and this trend is likely to persist.
- Development activity, while elevated by historic terms, has not been enough to meet demand. Volume under construction is up by 30% year-over-year as of Q2 of 2021, to 27 million SF, but that accounts for merely 1.0% of total inventory. And most of the incoming new supply is pre-leased (18.2M SF), and the remaining speculative space is likely not enough to satiate demand.
- Montreal, Toronto and Vancouver are currently seeing 3.8, 9.4 and 5 million SF of construction activity. Collectively, they account for 69% of the national development pipeline and should continue to garner interest from developers and investors.
- Despite a strong outlook, there are headwinds. With the lack of available space, growth is dependent on delivering new supply. This is becoming increasingly challenging due to a scarcity of land, a challenging entitlement process and rising construction costs.
- Montreal, Toronto and Vancouver have seen average land prices soar. Development costs are further exacerbated by near-term inflation in materials prices. These conditions are major headwinds to the growth of the industrial sector for the foreseeable future.

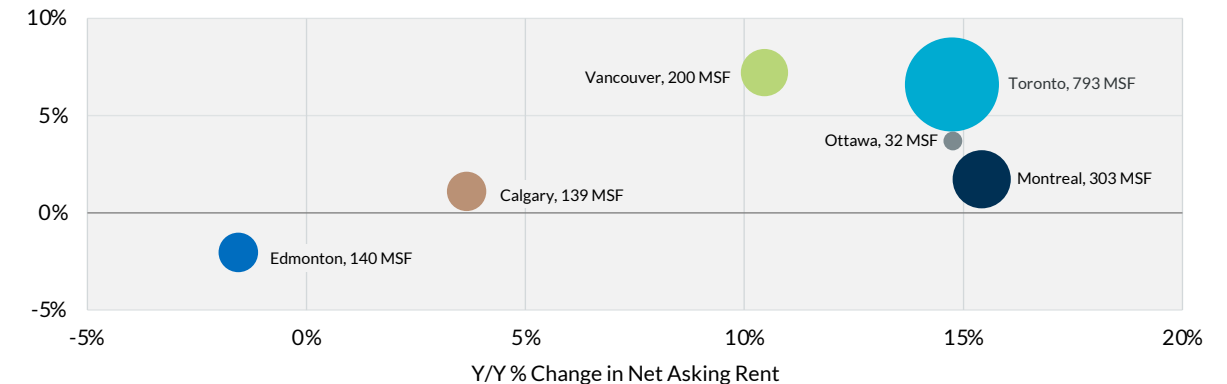
## INDUSTRIAL NET ABSORPTION



Source: CBRE

## INDUSTRIAL NET ASKING RENTS \$PSF

Q/Q % Change in Net Asking Rent



Note: Size of the bubble reflects the size of the market in millions of square feet  
Source: CBRE

CANADA

Perspective on

# MULTI-FAMILY

“Rental recovery underway.”

BentallGreenOak 

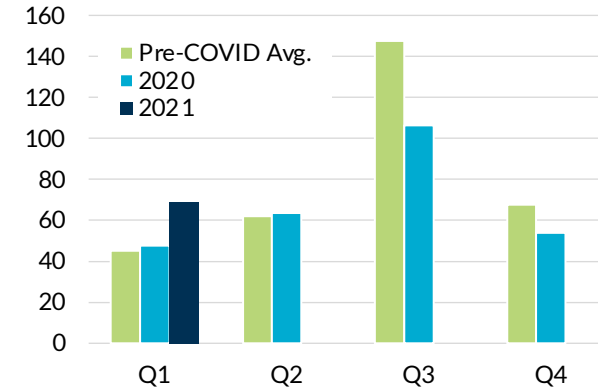
# DEMAND DRIVERS RE-EMERGE

- Purpose-built rental vacancy remains elevated in many markets across the country. The national vacancy rate increased 120 bps to 3.5% in 2020, according to the Canada Mortgage and Housing Corporation (CMHC). This was the highest level since 1998. Vacancy rates remain higher in Alberta (which never fully recovered from the oil price shock of 2015) and in the urban areas of Toronto and Vancouver, where vacancy rates are in the high single digits according to local market experts.
- However, there are emerging signs of a recovery as immigration – a key source of rental demand – is beginning to pick up. In particular, the pace of both permanent and nonpermanent residency is up significantly in Q1 of 2021. These largely include international students and temporary foreign workers. Compared to pre-COVID Q1 trends, international study and temporary worker permits approved for Q1 of 2021 are up 52% and 61%, respectively.
- In this early stage of the recovery, we're more interested in nonpermanent residents, as they are a better indication of the potential incremental change in housing demand. While the increase in permanent residency permits is also encouraging, these figures largely represent a change in status as the federal

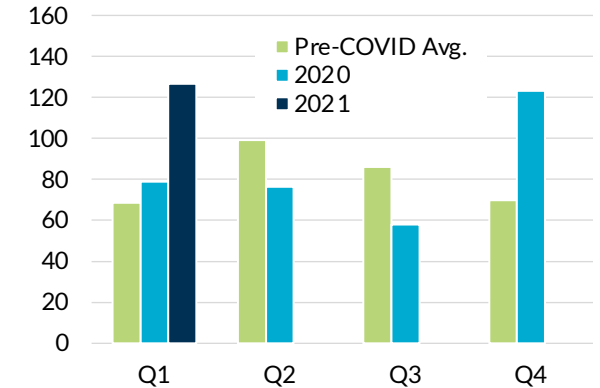
government draws on a pool of applicants who are already in the country to reach its increased immigration targets.

- There are other encouraging signs that might suggest stronger demand within prime renter segments. Many post-secondary institutions are expecting to reopen campuses for both domestic and international students in the fall, albeit at a slow and measured pace. Additionally, hiring intentions remain strong; total job postings on Indeed were up 23% on June 4, compared to early February 2020. Postings for "in demand" sectors targeted under various economic migrant programs – such as software developers, construction and nursing – were up even higher at 60%, 55% and 54% respectively.
- As a result of remerging demand, data from Rentals.ca suggest that rents may have bottomed and are on the road to recovery. CMHC only provides data on an annual basis. Consequently, we've relied on more timely data from Rentals.ca to gauge momentum shifts and inflection points at the market level. Six of the eight major markets we observed exhibited month-over-month rent increases in each of last three months, with Kitchener, Calgary and Montreal also now showing year-over-year increases.

## INTERNATIONAL STUDY THOUSAND PERMITS



## INTERNATIONAL TEMPORARY WORKER THOUSAND PERMITS



Source: Immigration Refugee Citizenship Canada

## ONE-BEDROOM MONTHLY RENTS 3-MONTH MOVING AVERAGE, M/M % CHANGE

	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21
Vancouver	-1.8%	-0.1%	-1.5%	0.0%	0.5%	1.4%	0.6%	1.6%
Toronto	-2.1%	-2.3%	-2.3%	-2.0%	-1.3%	-0.4%	0.1%	0.5%
Ottawa	-2.0%	-1.1%	-1.8%	-0.5%	-1.0%	-0.6%	0.3%	1.5%
Kitchener	-3.0%	-3.2%	-1.9%	1.2%	2.1%	1.9%	1.9%	1.3%
Montreal	-0.5%	-0.7%	-1.4%	-1.1%	-1.3%	-0.2%	1.0%	1.5%
Hamilton	0.0%	-1.2%	0.0%	-0.7%	0.0%	-1.7%	-1.3%	-0.3%
Calgary	0.1%	-0.3%	-0.5%	0.1%	1.0%	1.0%	-0.3%	0.2%
Edmonton	-0.6%	-0.2%	-0.4%	-0.3%	0.3%	-0.9%	-0.8%	-1.3%

Source: Rentals.ca



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For more information, please visit [www.bentallgreenoak.com](http://www.bentallgreenoak.com)

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