Canada Industrial, Q2 2016

Growing divide among primary and secondary industrial markets

Availability Rate 5.6%

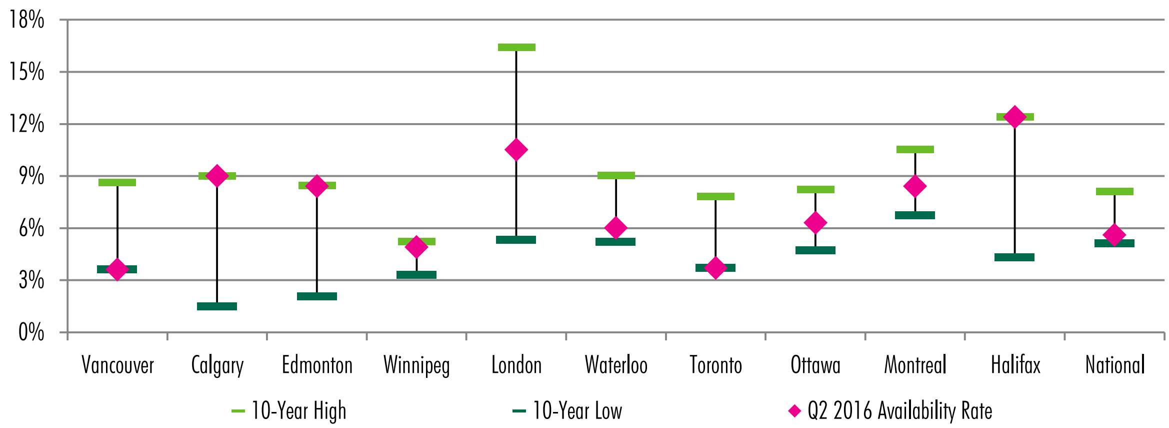
New Supply 3.3 MSF

Average Net Rent $6.49 PSF

Net Absorption 1.6 MSF

*Arrow indicates change from previous quarter.

Figure 1: Availability Rates by Market



Source: CBRE Research, Q2 2016.

- A growing bifurcation is clearly evident among Canada's industrial markets, with the GTA and Vancouver largely driving the market while the remaining markets follow behind.
- Canada's export market has fallen short of expectations despite generally ideal conditions. Challenges are clearly evident in the Canadian trade sector, largely as the most recent results of the Canadian trade deficit reached the second largest gap on record, at $3.28 billion.
- Construction activity has slowed down considerably from just under a year ago, with 11.9 million sq. ft. under construction, most of which is located in the GTA or Vancouver. 843,522 sq. ft. of new supply was completed in Edmonton this quarter, the second highest level by a single market this quarter.

The divergence among primary and secondary markets remains divided this quarter, largely resulting in uneven demand across Canada's industrial markets. Figure 1 highlights the highest and lowest availability rates achieved over the past 10 years, and compares it with the Q2 2016 availability rate. While Vancouver and the Greater Toronto Area (GTA) reached record low availability rates, at 3.6% and 3.7%, respectively, Calgary, Edmonton, and Halifax reached record high availability rates this quarter.

The tale of two markets remains an active trend among conditions between primary and secondary markets, and the gap continues to widen further following favorable demand conditions for all types of space in the GTA and Vancouver.

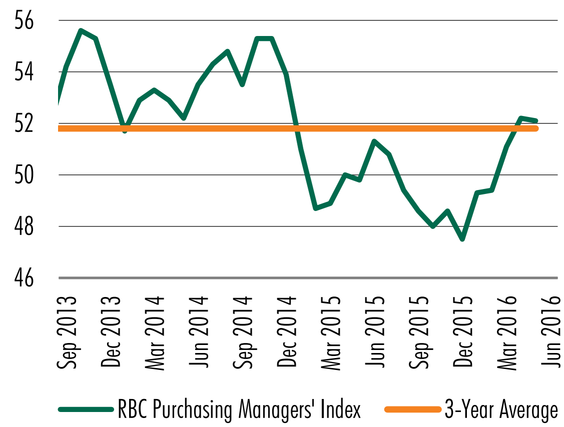
After more than 40 years of membership, the British people have voted to leave the European Union (E.U.). Over the short-term, economic impacts from this decision will likely be somewhat muted in Canada. As such, the near-term impact on Canadian market fundamentals should be minimal. In the current environment, Canadian markets will likely be viewed with enhanced status as havens for global capital.

According to the RBC Purchasing Managers' Index, Canadian manufacturers expected a slower outlook, notably in major manufacturing regions. After reaching a 16-month record high in April at 52.2, the RBC PMI dropped off in June to 51.8.

Despite a relatively low Canadian Dollar and a strengthening US economy, demand for exports has fallen short of expectations marked by the 21st consecutive month in a trade deficit. Challenges are clearly evident in the Canadian trade sector as the most recent numbers from Canada's trade deficit revealed the second largest gap on record, at $3.28 billion.

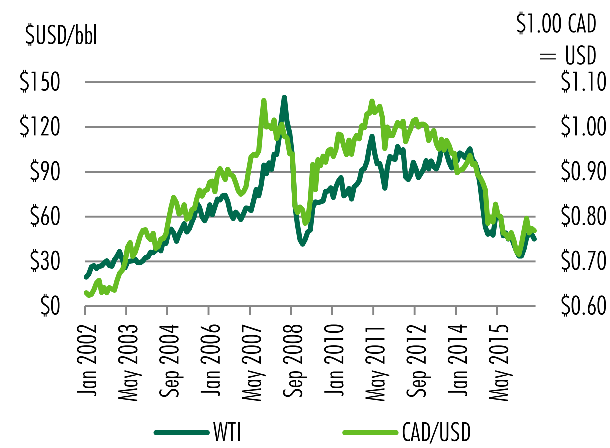
The transportation and warehousing industry continues to report positive news for Canadian industrial activity, largely as e-commerce delivery and distribution logistics remains highly active in the Canadian industrial market. Urban and semi-urban markets remain the most competitive for those looking to secure industrial inventory on the fringe or nearby the urban market to reduce the last mile between producer and consumer. Similarly, some developers are taking advantage of obsolete light industrial buildings near the outskirts of the core or downtown to repurpose inventory into office space or for multi-family uses. Despite a focus on small and mid bay product, demand for large bay industrial facilities for distribution uses still remains competitive in many of Canada's major markets, especially in major distribution hubs such as Calgary or the GTA.

Figure 2: Manufacturing Purchasing Managers' Index



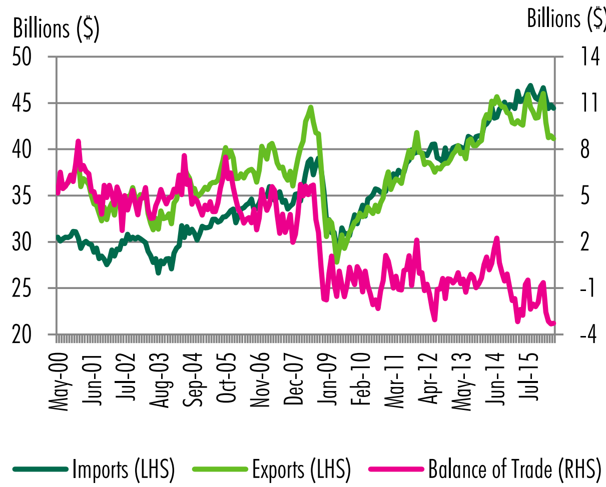
Source: Royal Bank of Canada, June 2016.

Figure 3: WTI Crude Oil Price & CAD/USD Exchange Rate



Source: U.S. Energy Information Administration, Thomson Reuters, CBRE Research, Q2 2016.

Figure 4: Canada Imports and Exports



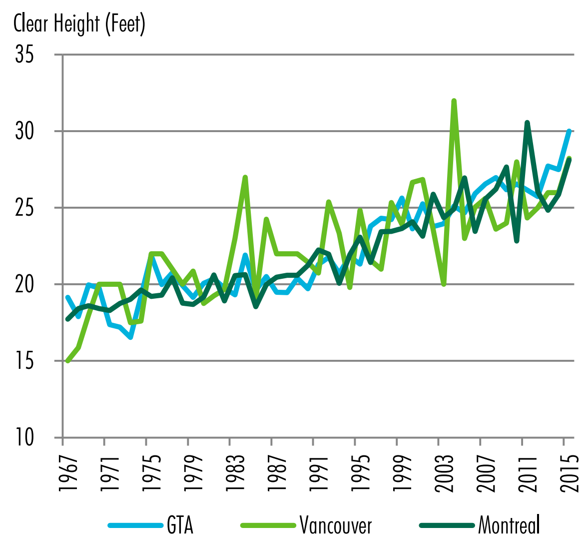
Source: Statistics Canada, May 2016.

Functional and locational obsolescence is becoming a greater risk for some developers and building owners as e-commerce distribution and evolving tenant demand changes the industrial marketplace. Higher ceiling heights, extended trailer parking, greater bay depth, and mezzanines are considered modern building features that a growing number of users are demanding in current generation space. In some markets, highly specialized, older generation, and non-operational manufacturing facilities are now being considered functionally obsolete in the ever-changing landscape of the market.

Locational obsolescence has also resulted in tenant demand for industrial space shifting towards more location-driven real estate decisions. While the optimal location differs among user type, buildings positioned near transit infrastructure, labour pools, and population centres are considered the most favorable for transportation and distribution industry.

In the GTA and Calgary, Canada's two major distribution hubs, industrial buildings near intersecting highways generally achieve the highest sale prices, reaching upwards of $200 per sq. ft. or higher in some segments of the market. Similarly, sales prices can reach nearly $300 per sq. ft. or higher in Vancouver, Richmond, or Burnaby for top quality product in ideal locations. However, some markets are experiencing higher levels of obsolescence than others; while Vancouver does not have a major problem with obsolete product, as space is often absorbed or redeveloped into residential, office, or mixed use buildings, it is expected that roughly between 10-20% of Montreal's available space is functionally or locationally obsolete.

Figure 5: Average Building Clear Height by Year Built



Source: CBRE Research, Q2 2016.

Figure 6: Modern Industrial Building Features

Building Features	*Site Layout*
Bay depth – Buildings built with deeper bay depth, typically 250'	**Transportation infrastructure** — Nearby transportation infrastructure, including ports, airports, intermodal yards, and highways.
Ceilings heights — Higher ceiling heights are becoming standard on new builds, typically 32-36'	**Expanded employee parking** – Employee parking available, typically 1 stall per 1,000-2,000 sq. ft.
Racking systems – Racking systems and mezzanine space	**Excess Land** – Excess land for expansion or for trailer parking available
Automated machinery - Automated storage and retrieval systems	**Trailer Parking** – Double-wide trailer parking and 360 degree circulation available
Column width - Wider column spacing, typically 50'	**Coverage Ratio** -- Low coverage ratio, typically 40-50%

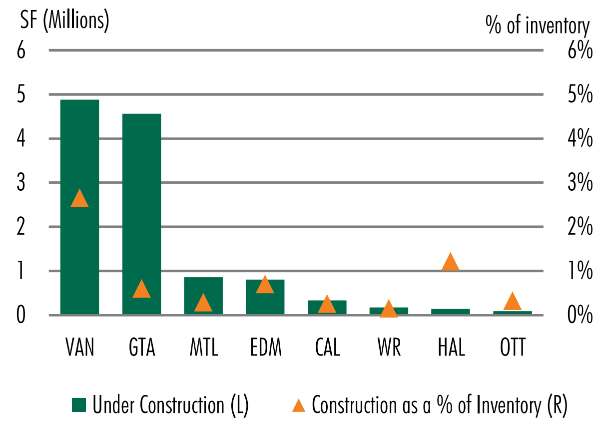
Source: CBRE Research, Q2 2016.

No market is currently overbuilding and most construction activity is less than 1% of the total market inventory, excluding Vancouver and Halifax, at 2.7% and 1.2%, respectively. Construction activity remains concentrated in the GTA and Vancouver where 80% of the current construction activity across Canada is situated in these two markets alone.

Despite the strong activity throughout most of the GTA's submarkets, Milton continues to struggle with absorbing the levels of vacant new supply in the market. 1.3 million sq. ft. was delivered to Milton this quarter, approximately 85% of which was vacant upon completion. As a result of the relatively small market size and the levels of new supply delivered to the market recently, Milton's availability rate has nearly tripled from only two years ago. However, it is expected that once the market absorbs the influx of new supply availability rates will return to previous levels.

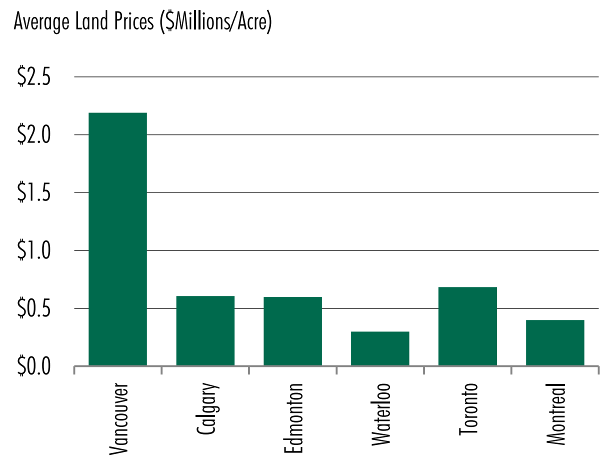
There has been an apparent construction slowdown in both the Alberta markets. As a result, 1.1 million sq. ft. is under construction this quarter between Calgary and Edmonton compared with 8.8 million sq. ft. that was under construction a year ago. Land is dictating certain factors of the industrial market, however, the high cost of land has not stopped those interested in purchasing and developing land in primary markets.

Figure 7: Construction and New Supply



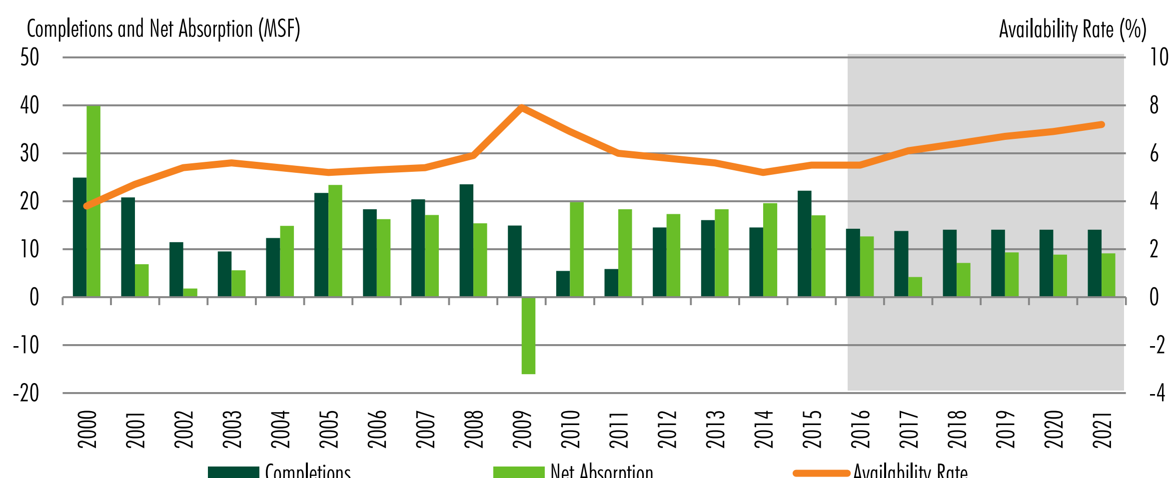
Source: CBRE Research, Q2 2016.

Figure 8: Average Land Cost by Select Market



Source: CBRE Research, Q2 2016.

Figure 9: Market Fundamentals and Forecast



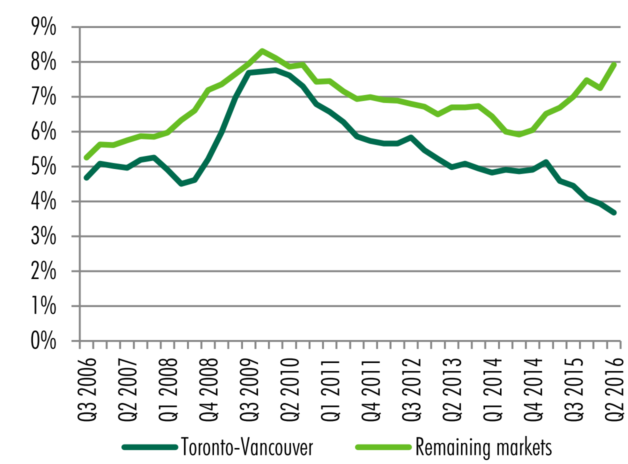
Source: CBRE-EA, Q1 2016.

However, there are markets in Southwestern Ontario, notably submarkets in Waterloo and London, that present several opportunities as the cost to purchase land is significantly cheaper than industrial markets nearby.

Availability rates in the GTA and Vancouver have compressed on a year-over-year basis, falling 50 bps to 3.7% in the GTA and 260 bps to 3.6% in Vancouver as both markets continue to achieve record low availability levels. Food users continue to dominate the landscape of Calgary's industrial market, but as a result of several quarters of economic uncertainty smaller sublease listings in manufacturing and oilfield service related buildings continue to negatively weigh on Calgary's availability rate.

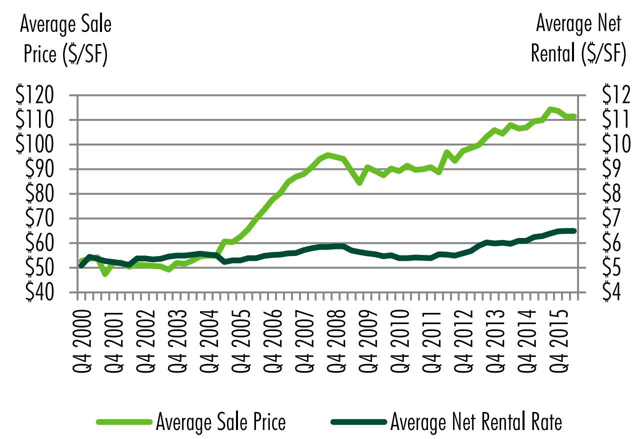
The gap between sale and lease rates continues to widen as buyer interest heats up. As net rental rates in Calgary and Edmonton steadily decline, sale prices are continuing to remain relatively strong, especially for Class A trophy assets. Lease rates in the GTA continue to remain steady while sales result in multiple bid offers and aggressive price increases based on the increasing demand from both institutional and local investors.

Figure 10: Availability Rates by Market



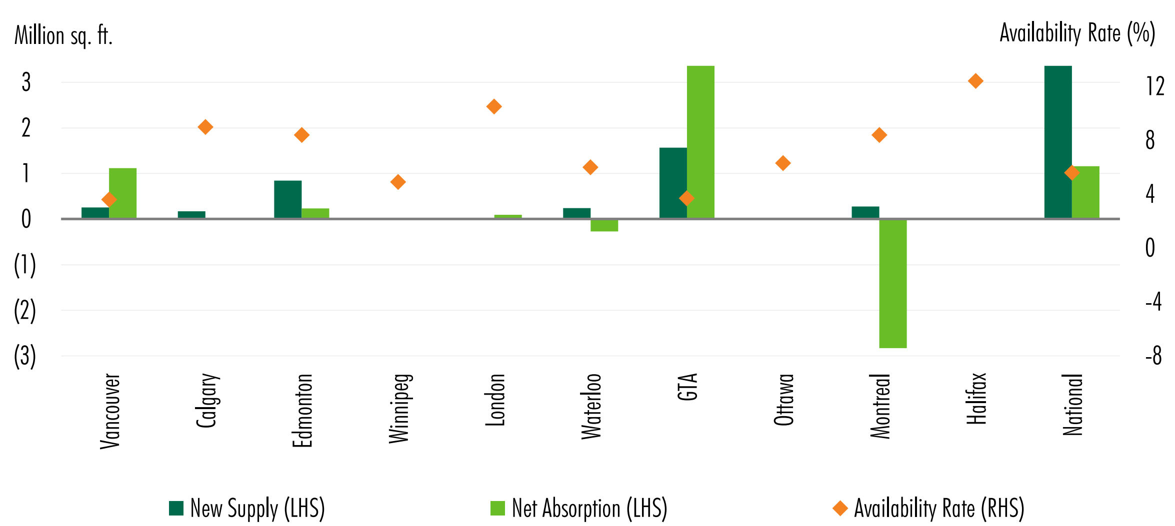
Source: CBRE Research, Q2 2016.

Figure 11: Average Sale and Lease Prices



Source: CBRE Research, Q2 2016.

Figure 12: Market Supply & Demand



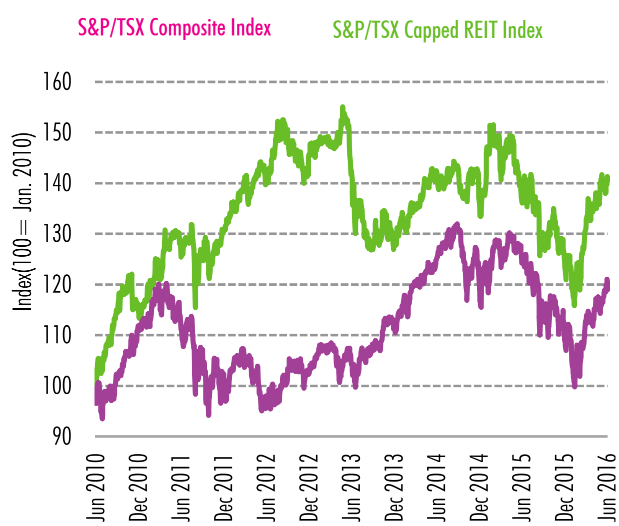
Source: CBRE Research, Q2 2016.

Figure 13: Q2 2016 Market Statistics Summary

Market	Inventory (SF)	Availability Rate (%)	Vacancy Rate (%)	Net Absorption (SF)	New Supply (SF)	Under Construction (SF)	Avg. Net Asking Rent ($/SF)
VANCOUVER	184,339,498	3.6	2.0	1,121,701	258,236	4,886,359	8.74
CALGARY	131,258,392	9.0	7.5	(4,193)	174,594	333,300	7.20
EDMONTON	114,454,984	8.4	4.9	237,837	843,522	802,013	10.58
WINNIPEG	77,301,348	4.9	4.8	4,390	0	65,360	7.62
WEST	**507,354,222**	**6.3**	**4.5**	**1,359,735**	**1,276,352**	**6,087,032**	**8.60**
LONDON	39,234,030	10.5	7.7	93,823	0	0	3.99
WATERLOO REGION	112,560,735	6.0	4.6	(270,176)	242,214	169,493	5.03
GTA	761,337,231	3.7	1.8	3,362,742	1,569,737	4,563,971	5.56
OTTAWA	29,882,403	6.3	4.8	(4,561)	0	94,917	8.99
MONTREAL	300,515,238	8.4	8.4	(2,833,384)	276,000	865,744	5.41
HALIFAX	12,073,582	12.4	12.3	(10,530)	0	147,000	7.74
EAST	**1,255,603,219**	**5.4**	**4.1**	**337,914**	**2,087,951**	**5,841,125**	**5.50**
NATIONAL	**1,762,957,441**	**5.6**	**4.1**	**1,697,649**	**3,364,303**	**11,928,157**	**6.49**

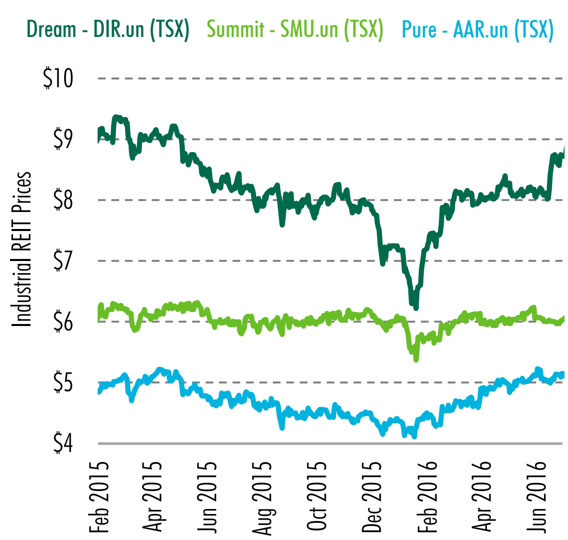
Source: CBRE Research, Q2 2016.

Figure 14: REIT Index vs. TSX Composite Index



Source: Thomson Reuters & CBRE Research, Q2 2016.

Figure 15: Industrial REIT Prices



Source: Thomson Reuters & CBRE Research, Q2 2016.

Figure 16: Notable Sale Transactions

Size (SF)	Sale Price ($MM)	Purchaser	Purchaser Type	Address	Price ($/SF)
994,942	100.0	Metrus Properties	Private Investor - Canadian	9501 – 9601 Highway No. 50, Vaughan, ON	101
658,209	83.8	Canadian Tire	Private Investor - Canadian	25 Dufferin Place S.E. & 5500 Dufferin Boul. S.E., Calgary, AB	127
502,809	63.2	Fiera Properties	Private Investor - Canadian	290144 Township Road 261, Balzac, AB	142
794,000	56.2	Crombie REIT	REIT	8265 Huntington Road, Vaughan, ON	142
355,316	45.7	Choice Properties REIT	REIT	18800 Lougheed Highway, Vancouver, BC	136

Source: RealNet, CBRE Research, Q2 2016.

Figure 17: Notable Lease Transactions

Size (SF)	Tenant	Tenant Industry	Address
634,992	Uline Canada Corporation	Transportation/Distribution	3333 James Snow Parkway, Milton, ON
249,643	SCI Logistics	Transportation/Distribution	6580 Millcreek Drive, Mississauga, ON
244,995	SCI Logistics	Transportation/Distribution	6175 Edwards Boulevard, Mississauga, ON
144,475	Hopewell Logistics	Transportation/Distribution	5805 51 Street SE, Calgary, AB
115,048	Sim Video International	Other	2820 Underhill Avenue, Burnaby, BC

Source: CBRE Research, Q2 2016.

Figure 18: Notable New Supply

Size (SF)	Property Name/Address	Developer	Speculative or Design-Build	Pre-Leased (%)
500,000	Overwaitea Foods Facility, Acheson, AB	N/A	Design-Build	100
434,213	8460 Mount Pleasant Way, Milton, ON	Sunlife	Speculative	0
207,051	8399 Lawson , Milton, ON	Prologis	Speculative	0
160,039	3495 Steeles Avenue, Brampton, ON	GWL	Speculative	0
145,000	3801 rue F.X. Tessier, Vaudreuil, QC	Triovest & Broccolini	Speculative	0

Source: CBRE Research, Q2 2016.

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