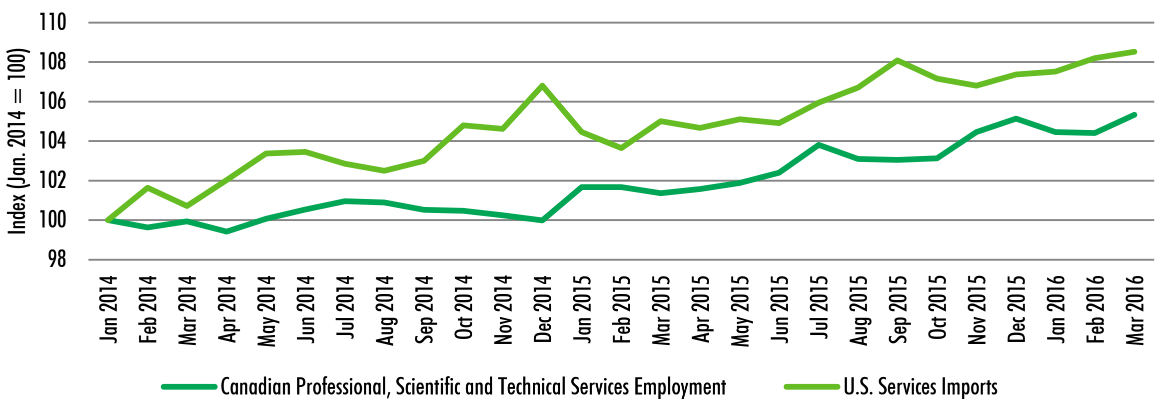
Canada Office, Q1 2016

Disparities among major markets has grown more pronounced in 2016

Vacancy Rate	Net Absorption	Under Construction	New Supply	Class A Net Rent
▲ 12.5%	▲ 0.5 MSF	▼ 15.6 MSF	▼ 2.0 MSF	▼ $20.84 PSF

*Arrows indicate change from previous quarter.

Figure 1: Canada's exports of services to the U.S. is benefiting some Canadian office markets



Source: CBRE Research, Q1 2016.

- The Bank of Canada's recent Business Outlook Survey highlighted that although corporate hiring intentions are up from the previous period, they remain muted.
- Due to the low Canadian dollar, Canadian firms are benefitting from a cost advantage compared to their U.S. counterparts, and they have seen growth as U.S. imports of services increases.
- After two consecutive quarters of negative net absorption, demand for office space in Canada picked up, with positive 491,200 sq. ft. of positive net absorption in Q1 2016, split relatively evenly between downtown and suburban markets.
- National overall vacancy ended Q1 2016 at 12.5%, up 140 basis points (bps) year-over-year.
- Tenant inducement packages continue to increase, therefore net effective rents (NERs) continue to come down, reflecting a challenging situation for landlords.

The national office market remains regionally segmented. Western Canada, due to weakness in Alberta, experienced negative net absorption once again, at negative 950,000 sq. ft. in Q1 2016, whereas Eastern Canada, with Toronto leading the charge, experienced 1.4 million sq. ft. of net absorption. Although oil prices increased in Q1 2016, Calgary office market fundamentals continued to weaken with downtown vacancy cresting the 20.0% mark and more layoffs to come.

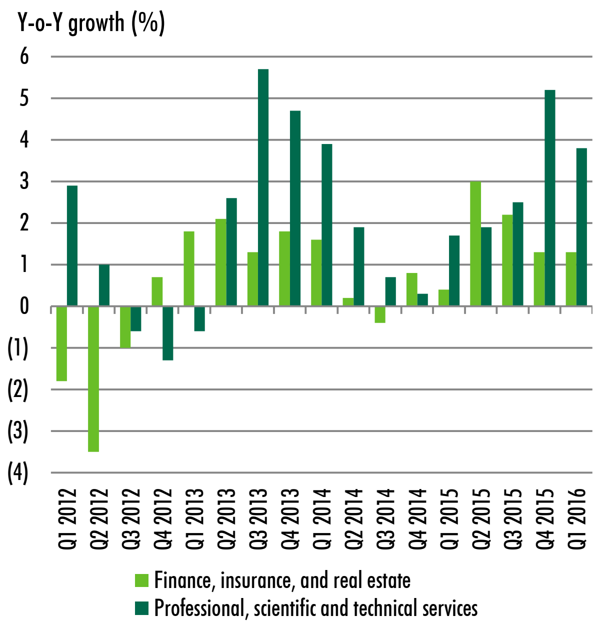
At the other extreme, Toronto's office market is the strongest in Canada, with downtown vacancy at 5.3%. Much like Vancouver and Montreal, Toronto is experiencing broad demand from several sectors, including the professional, scientific and technical services (PSTS) sector. Due to the low Canadian dollar, Canadian firms are benefitting from a cost advantage compared to their U.S. counterparts, and they have seen growth as U.S. imports of services increases.

EMPLOYMENT AND MACROECONOMIC DRIVERS

The economy took a positive turn in Q1 2016, with annualized growth of 2.4%, up from 0.4% in Q4 2015. Although Q1 2016 was expected to be strong, with exports being the largest contributor to growth, the remainder of 2016 expected to be slower until the economy picks up in 2017. Furthermore, the economy remains regionally segmented, with Vancouver and Toronto expected to experience strong economic growth and markets like Calgary expected to see contraction. This will only be compounded further by the forest fires in Fort McMurray.

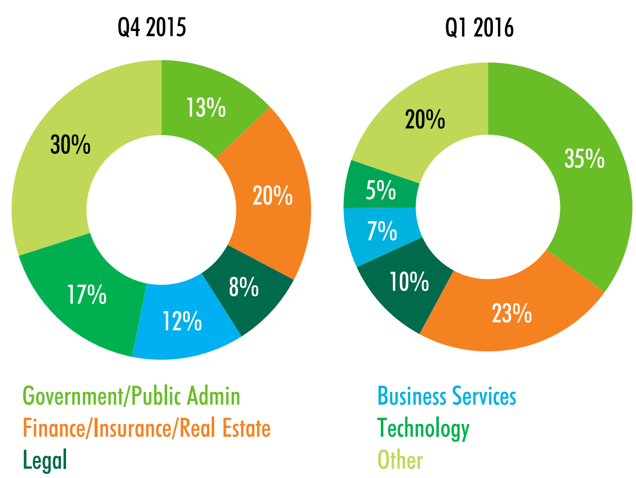
The Bank of Canada's spring 2016 Business Outlook Survey shows that hiring intentions have moved up from the low point reported in the winter 2015/2016 survey. Although, hiring intentions remain below historical averages, they were particularly strong among firms tied to exporting. On the actual job front, office using employment is up 3.1% year-over-year, compared to just 0.7% for total employment, with finance, insurance and real estate (FIRE) growing by 0.7% compared to professional, scientific and technical services and business services growing by 3.9% each.

Figure 2: Office-using employment



Source: CBRE Research, Q1 2016.

Figure 3: Significant Transactions Office (Top 5 Industries)



Source: CBRE Research, Q1 2016.

LEASING DEMAND/TRENDS

After two consecutive quarters of negative net absorption, demand for office space in Canada picked up, with positive 491,200 sq. ft. of positive net absorption in Q1 2016, split relatively evenly between downtown and suburban markets. Most markets experienced positive or flat net absorption, with Calgary being the outlier, at negative 1.1 million sq. ft. given back, the majority of which (over 1.0 million sq. ft.) was downtown. Strong positive net absorption in the Greater Toronto Area (GTA) is partially due to the 1.0 million sq. ft. of new supply downtown, however, as tenants complete their moves to the new supply, some space that has not been backfilled is expected to come back to the market.

We tracked approximately 2.6 million sq. ft. of significant deals done in Q1 2016, compared to 3.7 million sq. ft. in Q4 2015. Close to a 57.9% of these significant leases done across Canada in Q1 2016 were attributed to government/public admin or FIRE tenants, compared to only 32.7% of significant deals in Q4 2015. It should be noted that firms in both of these sectors are currently engaging in relocations and space rationalization as opposed to expansions at this time. Furthermore, technology firms only accounted for 5% of significant deals this quarter compared to 17% in Q4 2015, however demand from technology .tenants is expected to continue.

Figure 4: Office Market Statistics Summary Q1 2016

Submarket	Inventory (SF)	Vacancy Rate (%)	Rate Change (bps YOY)	Sublet Space (% of vacant space)	Net Absorption (SF)	YTD Net Absorption (SF)	New Supply (SF)	Under Construction (SF)	Class A Net Rent ($/SF)
VANCOUVER	46,514,398	11.6	140	8.7	147,925	147,925	433,728	1,156,976	26.36
Downtown	23,592,419	8.8	141	10.8	267,172	267,172	0	475,000	32.84
Suburban	22,921,979	14.3	151	7.4	(119,247)	(119,247)	433,728	681,976	23.58
CALGARY	63,982,098	19.8	664	38.7	(1,057,214)	(1,057,214)	57,000	4,438,368	23.29
Downtown	40,013,558	20.2	839	43.0	(1,042,710)	(1,042,710)	0	3,009,000	23.74
Suburban	23,968,540	19.1	370	31.1	(14,504)	(14,504)	57,000	1,429,368	22.90
EDMONTON	24,897,953	12.5	113	14.4	(42,972)	(42,972)	65,923	2,028,224	21.99
Downtown	15,018,421	11.1	100	14.6	(63,098)	(63,098)	0	1,771,500	22.51
Suburban	9,879,532	14.6	134	14.0	20,126	20,126	65,923	256,724	21.34
WINNIPEG	11,478,671	10.5	71	0.8	2,432	2,432	0	365,000	15.40
Downtown	8,632,050	10.1	3	0.2	36,767	36,767	0	365,000	15.40
Suburban	2,846,621	11.9	275	2.1	(34,335)	(34,335)	0	0	N/A
LONDON	5,624,177	14.2	(59)	0.1	30,476	30,476	32,000	50,630	14.13
Downtown	4,409,754	15.6	(53)	0.1	7,185	7,185	0	0	14.13
Suburban	1,214,423	9.3	(64)	0.0	23,291	23,291	32,000	50,630	N/A
WATERLOO REGION	14,331,085	13.3	230	7.4	(35,437)	(35,437)	15,300	393,768	13.84
Downtown	5,071,683	9.4	51	18.4	1,909	1,909	0	106,158	11.90
Suburban	9,259,402	15.4	325	3.7	(37,346)	(37,346)	15,300	287,610	14.50
TORONTO	156,601,254	9.6	(2)	14.5	834,213	834,213	1,117,826	4,298,659	21.04
Downtown	84,038,525	5.3	(41)	19.9	801,157	801,157	1,017,826	2,718,503	30.11
Suburban	72,562,729	14.6	43	12.3	33,056	33,056	100,000	1,580,156	17.27
OTTAWA	40,496,745	10.4	18	7.2	95,274	95,274	0	555,885	18.55
Downtown	18,686,218	9.5	32	7.0	21,913	21,913	0	0	22.87
Suburban	21,810,527	11.1	5	7.3	73,361	73,361	0	555,885	16.53
MONTREAL	72,543,148	13.4	28	12.2	453,505	453,505	232,000	1,811,512	18.97
Downtown	43,782,474	10.8	(20)	13.8	184,897	184,897	0	747,200	22.62
Suburban	28,760,674	17.4	102	10.6	268,608	268,608	232,000	1,064,312	15.31
HALIFAX	12,478,680	14.7	129	9.9	62,998	62,998	0	520,000	17.96
Downtown	5,077,340	14.5	153	16.0	747	747	0	300,000	19.30
Suburban	7,401,340	14.8	110	5.8	62,251	62,251	0	220,000	15.87
NATIONAL	448,948,209	12.5	133	17.6	491,200	491,200	1,953,777	15,619,022	20.84
Downtown	248,322,442	10.3	142	22.8	215,939	215,939	1,017,826	9,492,361	24.41
Suburban	200,625,767	15.1	121	13.2	275,261	275,261	935,951	6,126,661	18.46

Source: CBRE Research, Q1 2016.

SUBLEASE VACANCY

After increasing for five consecutive quarters, overall sublease vacancy actually dropped in Q1 2016 to 9.8 million sq. ft., down from a record 9.9 million sq. ft. in Q4 2015. 4.9 million sq. ft., or 49.9%, of this total is in Calgary alone, of which 3.5 million sq. ft. is in downtown Calgary. Nationally, sublet space now accounts 17.6% of overall vacant space, down from 18.2% last quarter. Excluding Calgary, where sublet space represents 38.7% of total vacant space, all other markets are below the national average.

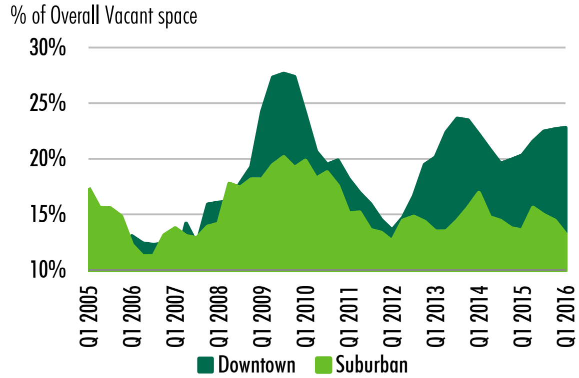
LEASE RATES

Average occupancy costs continued to decline with overall Class A asking rents down 1.5% year-over-year. The drop in downtown Class A net rents remains larger (negative 2.7%) than the drop in the suburbs (negative 1.0%). On the flip side, taxes and operating costs continue to rise, but at a slower pace. In general, and to the benefit of tenants, tenant inducement packages continue to increase, therefore net effective rents (NERs) continue to come down, reflecting a challenging situation for landlords.

CONSTRUCTION AND NEW SUPPLY

There is currently 15.6 million sq. ft. of office space under construction across the country, down from 19.1 million sq. ft. in Q1 2015. The Calgary, Toronto and Edmonton markets are experiencing the most construction activity. This new supply, particularly in Calgary, will further impact the markets, which are currently suffering from weaker demand. This will provide further catalyst for downward pressure on rental rates.

Figure 5: Sublease Vacant Space Historical



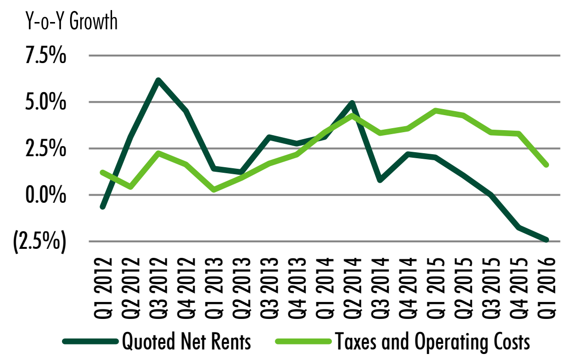
Source: CBRE Research, Q1 2016.

Figure 6: Quoted Net Rental Rates ($ per sq.ft./annum)

	Class A	Class B	Class C	Total
Central	24.41	16.63	14.85	20.00
Y-o-Y Change	▼2.7%	▼7.7%	▼9.9%	▼4.9%
Suburban	18.46	13.72	12.31	16.13
Y-o-Y Change	▼1.0%	▲0.9%	▼2.1%	▼0.3%

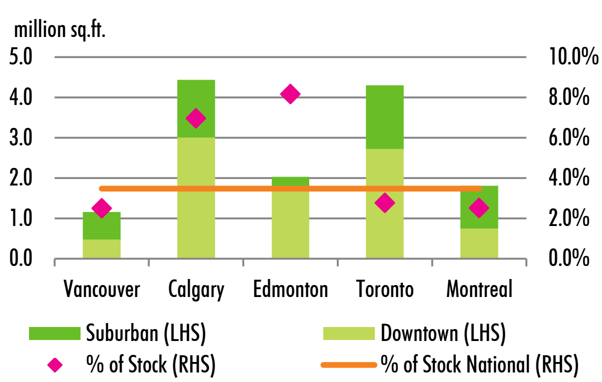
Source: CBRE Research, Q1 2016.

Figure 7: Quoted Net Rents vs. Taxes and Operating costs



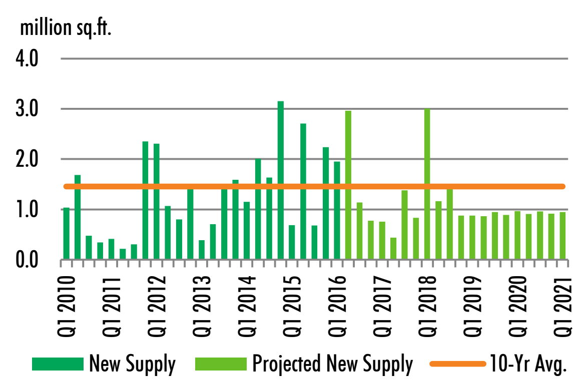
Source: CBRE Research, Q1 2016.

Figure 8: Office Construction by Metro



Source: CBRE Research, Q1 2016.

Figure 9: Office Construction Pipeline



Source: CBRE Research, Q1 2016.

Figure 10: Notable Lease Transactions

Size SF)	Tenant	Market	Submarket	Address	Tenant Industry
175,000	BMO	Toronto	Greater Core	250 Yonge Street	Financial Services-Banks
170,000	RSA Insurance Group	Toronto	Mississauga (Hwy 10/401)	Prologis Boulevard	Insurance
124,535	CIBC Mellon	Toronto	Downtown South	1 York Street	Financial Services-Banks
118,333	Desjardins	Montreal	Downtown	1050 Beaver Hall Hill	Financial Services-Banks
100,000	BCF	Montreal	Downtown	1100 René-Levesque Blvd. W	Legal
95,000	Traffic Tech	Montreal	West Island	Quartier Evolution	Other
65,979	Metrolinx	Toronto	Financial Core	30 Wellington Street W	Government
58,706	Centrica Energy	Calgary	Central Core North	237 4 Avenue SW	Energy
54,000	Field Law	Calgary	Central Core South	444 7 Avenue SW	Legal
42,500	Assent Compliance	Ottawa	Belfast-Sheffield	525 Coventry Road	Technology-Web
39,811	McElhanney	Vancouver	Downtown	858 Beatty Street	Engineering
32,995	Vidyard	Waterloo Region	Kitchener	8 Queen Street N	Technology-Software
25,148	Northern Commerce Inc.	London	Core	300 Wellington Street	Technology
19,800	Weatherford Canada Partnership	Edmonton	Southside	9426 51 Avenue	Energy
14,700	Public Works & Government Services Canada	Halifax	CBD	1505 Barrington Street	Government-Federal

Source: CBRE Research, Q1 2016.

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