

CANADA

Perspective

■ ■ 2020

INSIDE

- Focusing on long-term trends amid uncertainty
- Technology permeating all aspects of real estate
- Opportunities in emerging talent centres

BentallGreenOak 

THEMES SHAPING THE YEAR AHEAD

Slower economic growth is upon us, but we don't see an imminent recession with central banks easing monetary policy and a likely handoff to governments for more fiscal stimulus. In this environment, healthy real estate operating fundamentals will continue to attract strong investment capital. Our 2020 Perspective highlights 10 key themes that we think will shape the beginning of a new decade.

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COUNTERACTING THE SLOWDOWN

ONUS ON FISCAL POLICY TO DRIVE GROWTH

The global economy has downshifted from “synchronized growth” to a more tepid outlook. The Organisation for Economic Co-operation and Development (OECD) leading indicators, having lost momentum over the past 12 months, reflect this cautious sentiment. This is translating into a weaker global growth forecast of 2.9% for 2019 and 2020. The forecast does not call for recession, but it reflects a marked slowdown from average annual growth of more than 3.6% in 2017 and 2018.

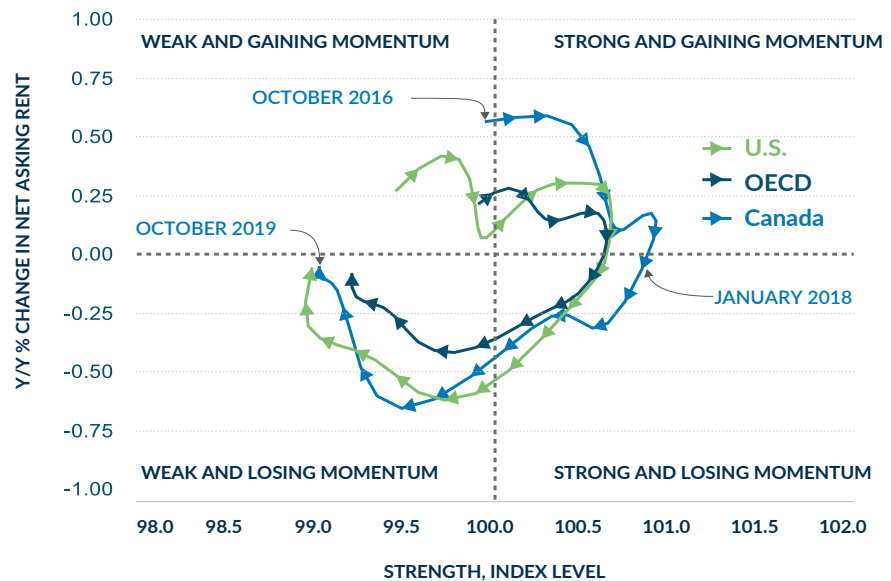
Much of this outlook revolves around soft industrial output and slowing trade activity, which could

deepen if progress toward a China–U.S. trade resolution stalls. Other political events such as Brexit and the Hong Kong protests could escalate and further cloud the global outlook.

Against this uncertain and fragile backdrop, central bankers have taken a dovish stance. In addition to keeping benchmark rates low, the Federal Reserve, European Central Bank and Bank of Japan are now engaged in quantitative easing. Meanwhile, the Bank of Canada and Bank of England have halted their rate-hike path, with possible cuts on the horizon.

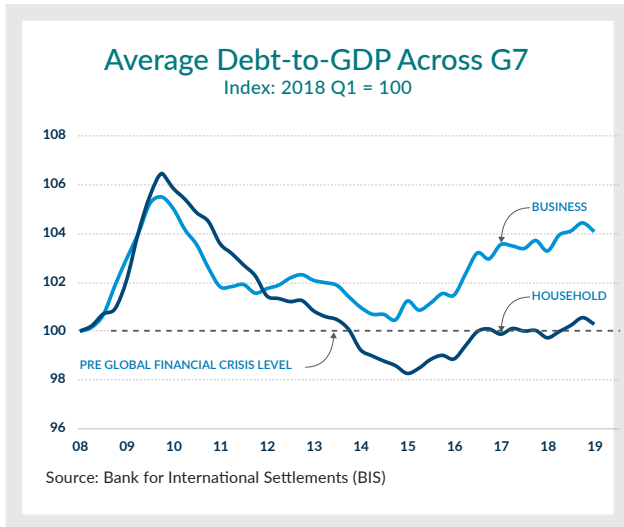
OECD Leading Indicator 3-Year Trend

Much of the OECD global growth forecast of 2.9% for 2020 revolves around soft industrial output and slowing trade activity, which could deepen if progress toward a China–U.S. trade resolution stalls.



Source: Macrobond, Organisation for Economic Co-operation and Development

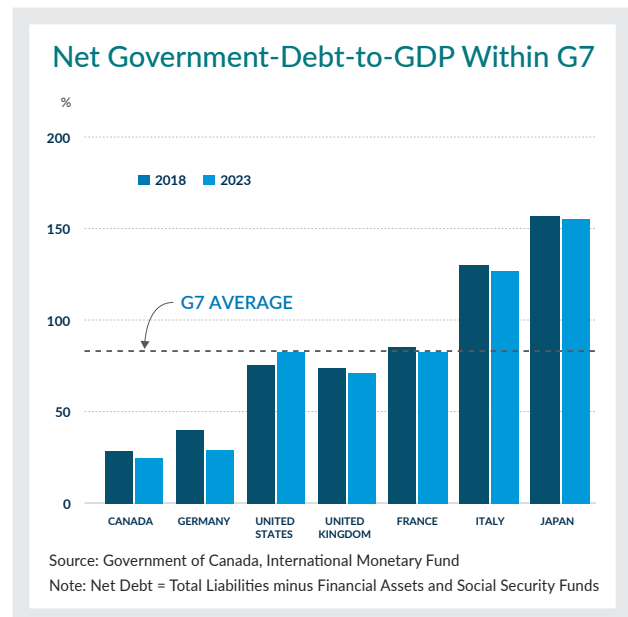
“During down cycles, conventional monetary policy is the weapon of choice to stimulate the economy.”



During down cycles, conventional monetary policy is the weapon of choice to stimulate the economy. In conjunction with government spending and quantitative easing, by lowering interest rates, central bankers played a key role in steering the global economy out of the Global Financial Crisis (GFC). However, with interest rates near historically low levels, there may not be enough firepower left on the monetary front to stimulate growth. The effectiveness of the transmission mechanism depends on whether the household and private sectors are positioned well enough to drive aggregate demand. Across the G7, for the most part, households have done a decent job of deleveraging, while businesses have picked up the pace of debt accumulation over recent years.

Monetary stimulus may be least effective in Canada, where the policy rate has remained below 2% for more than a decade. To put this in perspective, the overnight rate never breached below 2% prior to the GFC. This in part has driven home prices in key gateway markets such as Vancouver and Toronto to historic highs, lifting household

debt in the process. Household and business debt continue to outpace income growth, and as a result debt-to-GDP in Canada is the highest among G7 nations. Accommodative monetary policy should aid the process of deleveraging, but is unlikely to have the same stimulative impact as in previous cycles. The onus then falls on fiscal stimulus to provide support in an environment of sluggish growth, and fortunately Canada is in a better position in this regard. Within the G7, Canada has the lowest net government-debt-to-GDP ratio.



As we head into 2020, an intensifying geopolitical climate could have a trickle-down impact on the real economy. In the event of an entrenched global downturn, economic stimulus will be more reliant on fiscal policies this time around. This is particularly true for Canada, where a stable political landscape and historically prudent fiscal spending are competitive advantages.



FOCUSING ON LONG-TERM TRENDS AMID UNCERTAINTY

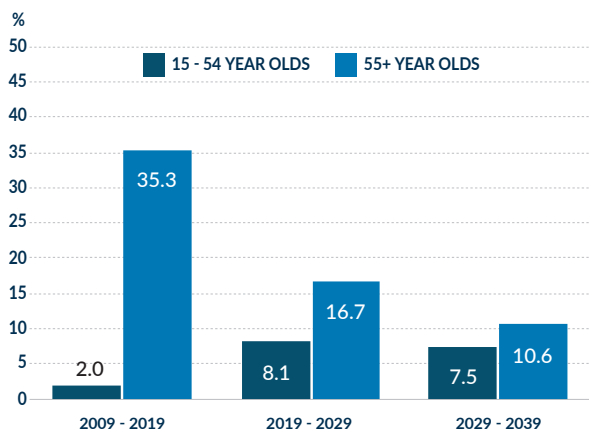
IMPLICATIONS OF AGING DEMOGRAPHICS

In Canada, the number of people aged 55 and over has grown more quickly over the past decade than those aged between 15 and 54. This trend is expected to persist over the next two decades, albeit at a slower pace. By 2039, approximately 30% of the population is projected to be above the age of 55. To understand the implications for commercial real estate, we need to examine the underlying trends associated with this shift in demographics.

According to research by Environics, most older residents of Canada are located outside of the six

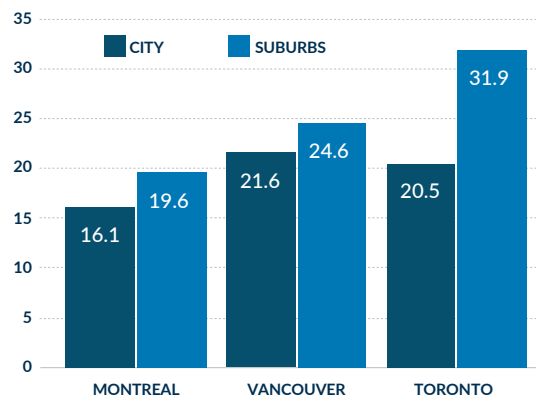
largest census metropolitan areas, particularly within medium-sized cities and rural areas. Environics has found that older residents in Toronto, Montreal and Vancouver aren't necessarily relocating closer to the urban cores as they downsize. In fact, the suburban populations are older than those of the urban centres in these three cities and have been and continue to age at a much faster clip. This is most evident in Toronto, where the suburbs are expected see the 55+ population expand by a staggering 32% over the next decade. In the case of Vancouver, the suburbs have a much higher concentration of this age cohort than the city.

Canada Population Growth



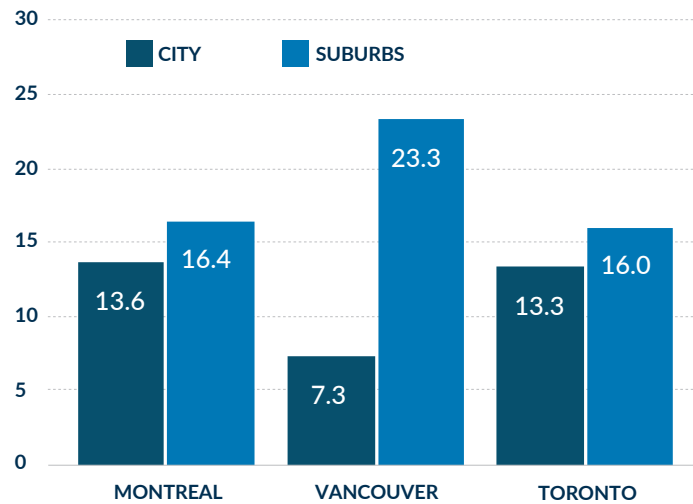
Source: Environics

Projected Growth of 55+ Age Group from 2019 to 2029





55+ Age Group as Percentage of Total Population



Source: Environics

Consumption patterns are likely to favour more experiential, service-oriented retail than material goods.

The baby boomer generation is also staying in the labour market longer. Over the past two decades, the labour participation rate within the 60 to 64 age cohort has risen from 35% to 57% and that for the 65 to 69 age cohort has risen from 12% to 27%. The share of total national income for the 55+ age group is 37% and rising due to their growing size and extended working life. Trends suggest that their propensity to consume should remain strong and rival that of the millennial and younger generations.

While their earning power remains strong, their consumption patterns are likely to favour more experiential, service-oriented retail than material goods. In addition, in locations where these demographics are more prevalent, retail centres with medical offices and other health and wellness services are poised to outperform.

There is a strong positive correlation between an aging population and the rise in renter households

and apartment living. As empty nesters downsize from the family home, many are choosing rental apartments for the convenience, amenities and social aspects that high-rise communities provide. Purpose-built rental and independent and assisted living seniors residences provide a bridge to longer-term care facilities where additional nursing and memory care may be required. As mobility declines in later years, online consumer staples could experience additional demand benefiting logistics and cold storage industrial facilities.

In terms of location, purpose-built rental housing within the urban cores of Toronto, Montreal and Vancouver should see upside; however, the demographics also provide support for the suburban nodes within these top three markets. Regardless of whether it's the suburbs or the urban core, walkable communities with strong retail amenities and good public transit accessibility will be in high demand.



TECHNOLOGY PERMEATING ALL ASPECTS OF REAL ESTATE

PROPTech FINDING PRODUCT/MARKET FIT

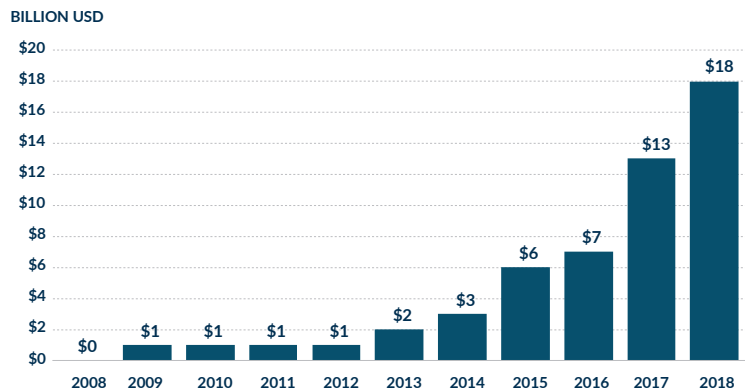
As Marc Andreessen (Andreessen Horowitz) famously said in a 2010 Wall Street Journal article, “software is eating the world,” meaning that a broad economic and technological shift was occurring in which digitally native companies were taking over large facets of the traditional economy. There are various examples in the real estate space – Airbnb, Amazon, Uber, and Zillow being the most prominent. For the most part, real estate incumbents continue to eat their own lunch, but software is undoubtedly penetrating the real estate world at an increasing rate in much the same way that it has other industries in recent years. While there will always be outliers that fundamentally disrupt business models,

most of the technology companies focused on real estate are innovating on existing processes and practices and working to eliminate inefficiencies.

Global investment in property technology (PropTech) companies grew from just USD\$1 billion less than a decade ago to USD\$18 billion in 2018. PropTech lies at the intersection of the physical and digital worlds, and the integration is becoming more seamless. But PropTech is just one part of a much wider digital transformation in the property industry. James Dearsley, a thought leader in the space, suggests that this evolution includes changes in both the technology and the mentality of the real

Value of Fundraising by PropTech Companies Worldwide

PropTech lies at the intersection of the physical and digital worlds, and the integration is becoming more seamless.



Source: Statista



“The biggest challenge facing organizations isn’t necessarily the technology stack, but the cultural shift that is required to fully utilize and leverage data and technology.”

estate industry and its consumers, as well as the attitudes, movements and transactions related to both buildings and cities. It often leverages artificial intelligence (AI), machine learning, robotics, process automation, big data and blockchain technology to create innovative solutions.

Understanding the PropTech landscape can be an overwhelming task even for those who are immersed in it every day. Technology is being infused into every facet of the business, from brokerage and leasing, construction and operations to investment and financing, asset management, fundraising and client services. New solutions can be divided into four broad categories based on the targeted outcome: generating more revenue, reducing costs, improving customer service, or formulating strategy.

The biggest challenge facing organizations isn’t necessarily the technology stack, but the cultural shift that is required to fully utilize and leverage data and technology. One of the biggest challenges facing the industry is how to upskill the existing workforce and how to add additional skillsets in a challenging hiring environment. The war for talent is playing out across the real estate

industry as companies now find themselves competing with other industries for top engineering, computer science and math graduates.

The acceleration of real estate technology, particularly with respect to sensors, smart buildings and the Internet of Things (IoT), will be underpinned by the deployment of 5G, which provides connectivity at lightning-fast speed. 5G will enable a huge range of new business cases for the IoT. With so much data being generated, how much of it will be useful? How much should be retained? How will data risks be mitigated? How will the data be analyzed and made actionable? When it comes to making use of data, the challenge is creating not only a robust data governance model, but also critical business rules necessary to align with a digital transformation strategy.

Investment managers who have a strategy and can separate the wheat from the chaff in implementing technology solutions and leveraging internal data will have a competitive advantage. And in this tech-driven, winner-take-all world, that means better performance, greater accumulation of assets under management (AUM) and more real-time insights gleaned from a growing portfolio of assets.



INCREASING PORTFOLIO RESILIENCE

SUSTAINABLE INVESTING HELPS DRIVE PERFORMANCE

Portfolio resilience is top of mind for investors, in terms of both protecting cash flows and valuations from a cyclical downturn and ensuring that assets endure over the long term. Asset managers have levers to pull to position assets for the next downturn, including locking in occupancy and lease terms with new and existing tenants, undertaking major capital projects to better position properties competitively, and bringing additional focus to monitoring of tenant credit. But central to constructing a “portfolio of tomorrow” is the

incorporation of climate change and environmental, social and governance (ESG) factors into the investment decision-making process.

For the first time, the Bank of Canada has flagged climate change as a vulnerability of the Canadian financial system. This could represent a pivotal moment in the low-carbon economy shift in Canada. Within its May 2019 Financial System Review the bank stated that climate risks “can be managed most effectively when investors and

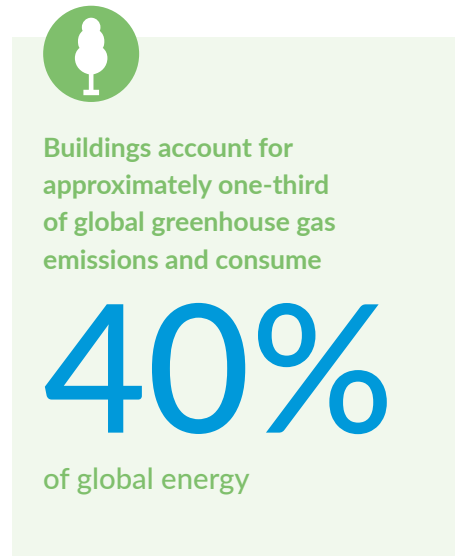


“Assets will be increasingly scrutinized for carbon-related risks.”

authorities know what exposure firms face.” Broadly speaking, across industries there has historically been little disclosure by businesses on how climate change and other ESG factors will impact their assets and operations, let alone consistent and comparable information available to investors.

However, research from BentallGreenOak, REALPAC and UNEP FI has affirmed a consensus view on the increasing role ESG is playing in the real estate investment decision-making process. This was one of the largest ESG-focused surveys of global real estate investors ever conducted and included investment managers representing over USD \$1 trillion in assets under management in North America, Europe and the Asia-Pacific region. This viewpoint is critical, as buildings account for approximately one-third of global greenhouse gas emissions and consume 40% of global energy. As investors and consumers shift to lower-carbon energy sources, assets will be increasingly scrutinized for carbon-related risks.

Flooding, hurricanes, wildfires, landslides, droughts, heat waves, food and water scarcity and rising sea-levels — all these climate-related events present both physical and operational risks for real estate assets. Sustainability practices have now become a prerequisite for fund managers whose institutional investors require their consideration in underwriting, operations and asset management and increased transparency in ESG disclosure (measuring and reporting) as part of de-risking a portfolio. And as a fiduciary, it's now essential to take into consideration climate change impacts,



from both a risk mitigation and a value creation perspective, to enhance the long-term financial and operational resiliency of real estate portfolios. Higher tenant satisfaction, lower tenant turnover, and lower operating expenses are just a few of the metrics that demonstrate the return on investment from sustainability initiatives.

More investors are beginning to understand the correlation between sustainability and financial performance. And more data is beginning to prove out that sustainable investing produces superior returns. With the United Nations Environment Programme (UNEP) being the latest to ring the alarm bells on rising global temperatures in its *Emissions Gap Report*, expect to see more discussion and action among real estate stakeholders in the year ahead.



PORTFOLIO CONSIDERATIONS IN A LOW-YIELD ENVIRONMENT

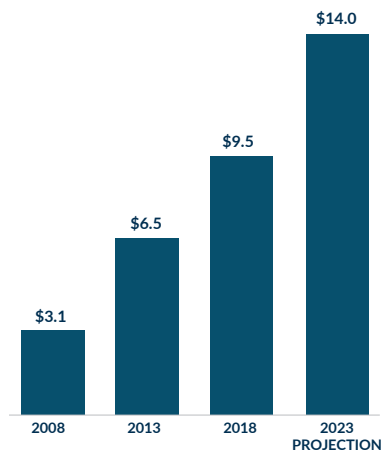
REAL ESTATE'S PORTFOLIO ENHANCING ATTRIBUTES

Capital is expected to continue to flow into private real estate in the year ahead. In times of increased economic and political uncertainty, real assets in liquid markets not only provide safety and diversification, but often outperform those directly linked to financial markets on a risk-adjusted basis. There is currently close to USD\$16 trillion in negative-yielding debt around the globe. Consensus expectations for global equity returns over the next decade are in the mid single digits. In such a low-return environment, even the most conservative investors are looking to reallocate capital into real assets.

AUM in alternative categories such as private debt, real estate, infrastructure, natural resources, hedge funds and private equity have increased more than three-fold over the past decade. Alternatives research firm Preqin predicts that AUM in global portfolios will jump from USD\$10 trillion in 2018 to USD\$14 trillion by 2023. Similar projections by PwC anticipate that investment in alternatives will increase to as much as USD\$21 trillion by 2025.

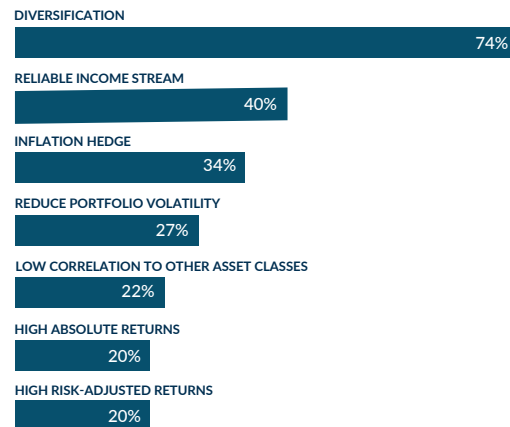
Investors typically cite several reasons for using alternatives, including higher absolute returns, higher risk-adjusted returns, low correlation to

Projected Growth of Global Alternative Assets Industry
AUM (USD\$ Trillions)



Source: Preqin, 2019

Main Reasons for Investing in Real Estate Assets
(Proportion of Investors)



other asset classes and reduced portfolio volatility. In a recent Preqin survey, investors cited diversification, reliable income stream and inflation hedge as the three most common reasons for incorporating real estate into their portfolios.

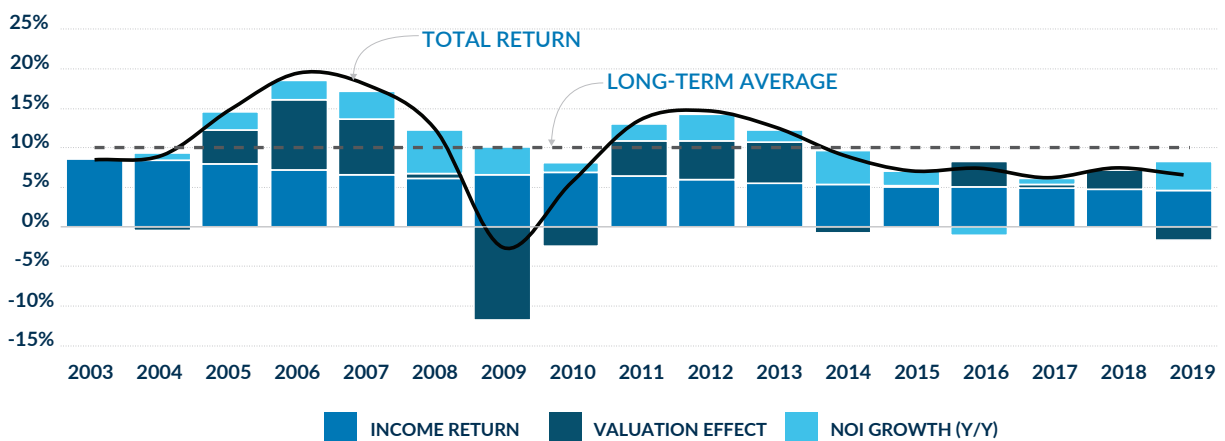
There is a consensus view that public market valuations are peaking. And investors and fund managers in alternatives indicate fulsome valuations are the biggest challenge to future real asset returns. But with heightened market uncertainty, investors are looking to increase portfolio resiliency through alternatives, seeking stable income yield and geographic and sector diversification to underpin their cash flows. Approximately 70% of the total return from real estate is historically derived from the income in comparison to capital appreciation. Income returns for private real estate in Canada have been remarkably predictable, exhibiting much less volatility than in other advanced-economy real estate markets. We expect private Canadian real estate to generate a 4% to



Solo District Burnaby, BC

5% income return with inflation-like capital appreciation of 1% to 2% over the next year. While the expected investment performance of 5% to 7% total return is below the long-term average for investment-grade, private real estate, it remains attractive on a relative basis.

Decomposition of Canadian Private Real Estate Investment Returns (Total Returns, Standing Investments)



Source: MSCI REALPAC Canada Quarterly Property Index, Q3 2019, 4-Quarter Trailing Return



THE HOUSING AFFORDABILITY CRISIS

MORE RENTALS PART OF THE SOLUTION

Housing affordability is a complex social and economic issue that affects many of the world's most prosperous cities. Income disparity, land scarcity, rising construction costs, strong population growth and a surplus of investment capital all play a role in the issue. But the main culprit in Canadian cities is a dearth of adequate housing supply. Bureaucratic planning, zoning, and approval processes are simply insufficient to keep pace with soaring demand.

Many of the federal policies implemented in recent years have been targeted at helping first-time home buyers, including increasing the amount they can withdraw from their RRSP for a down payment, and the introduction of a shared-equity program to

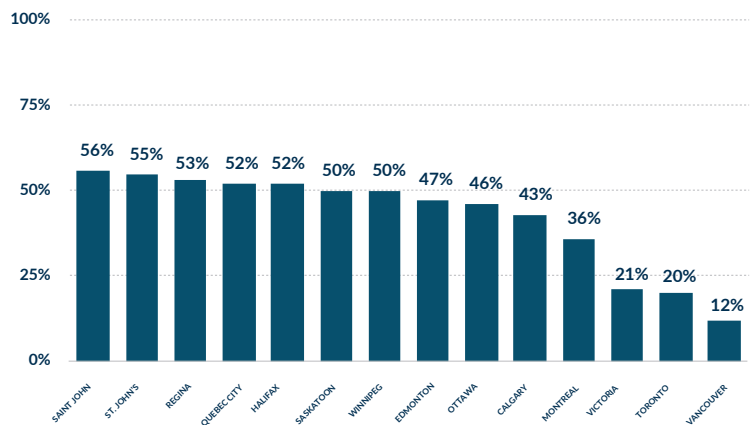
effectively subsidize down payments. The problem with many proposed solutions is that they are short-term, aimed at helping buyers afford housing at current prices, rather than getting at the core problem, which is a lack of supply, and of the right type of supply.

As the head of Canadian Mortgage and Housing Corporation (CMHC), Evan Siddall, recently quipped, "This glorification of home ownership is this odd North American thing that's counter intuitive." Because rental housing is most likely to fit household budgets, it should play a critical role in addressing the issue of housing affordability. According to RBC Economics, less than one-quarter of Canadian households in Toronto and Vancouver

Proportion of Families Who Can Afford To Own a Home

% of families whose income meets debt service requirements for an average priced home, Q1 2019

Rental housing should play a critical role in addressing the issue of affordability.



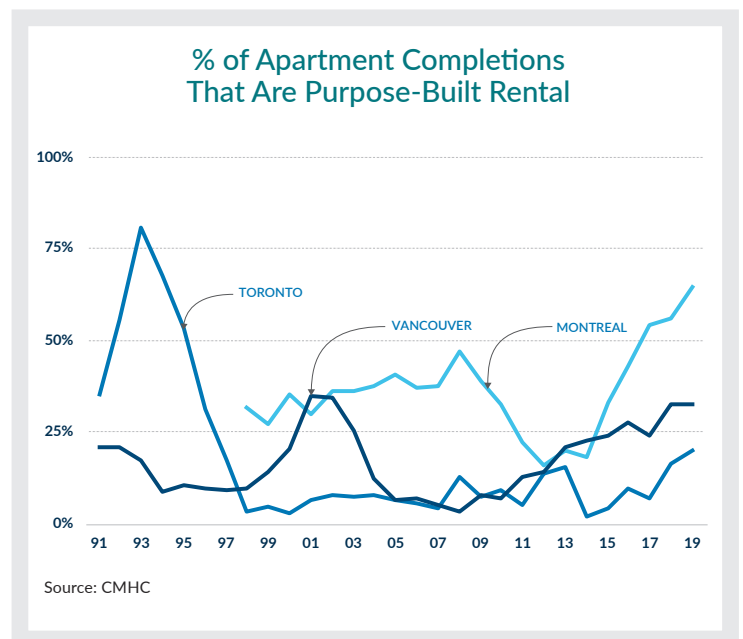
Source: RPS, Statistics Canada, Bank of Canada, RBC Economics Research

can afford to own an average priced home in their respective market. Although the level of purpose-built rental construction has ramped up in recent years as low interest rates and rising rents have made projects feasible again, it's still nowhere close to where it needs to be to meet demand. Less than one-third of the new apartment supply being delivered in these markets is purpose-built rental. And to be feasible, projects must be primarily targeted at more-affluent renters. This merely achieves a trickle-down effect, whereby lower-priced rentals only become available when renters “move-up,” as opposed to creating new supply directly targeted at rents that are affordable for those making a living wage.

In the U.S., the National Apartment Association conducted a countrywide survey to better understand factors that impact the new supply of apartments. The survey measured development complexity including the impact of community involvement, construction costs, affordability issues, infrastructure, density and growth restrictions, land supply, environmental restrictions, approval process complexity, political structure and time to develop a new property. The key take-aways from the survey were that: 1) in addition to the importance of land availability, input from local citizens significantly influences development (or lack thereof – NIMBYism); 2) rising land and labor costs are inhibiting the production of affordable housing; and 3) complex approval systems are correlated with affordability issues. These findings ring true in Canadian markets as well. In fact, housing affordability is a global crisis, particularly in metro areas, where prosperous cities have become victims of their own success.



Novus, Toronto, ON





RISING DEVELOPMENT COSTS

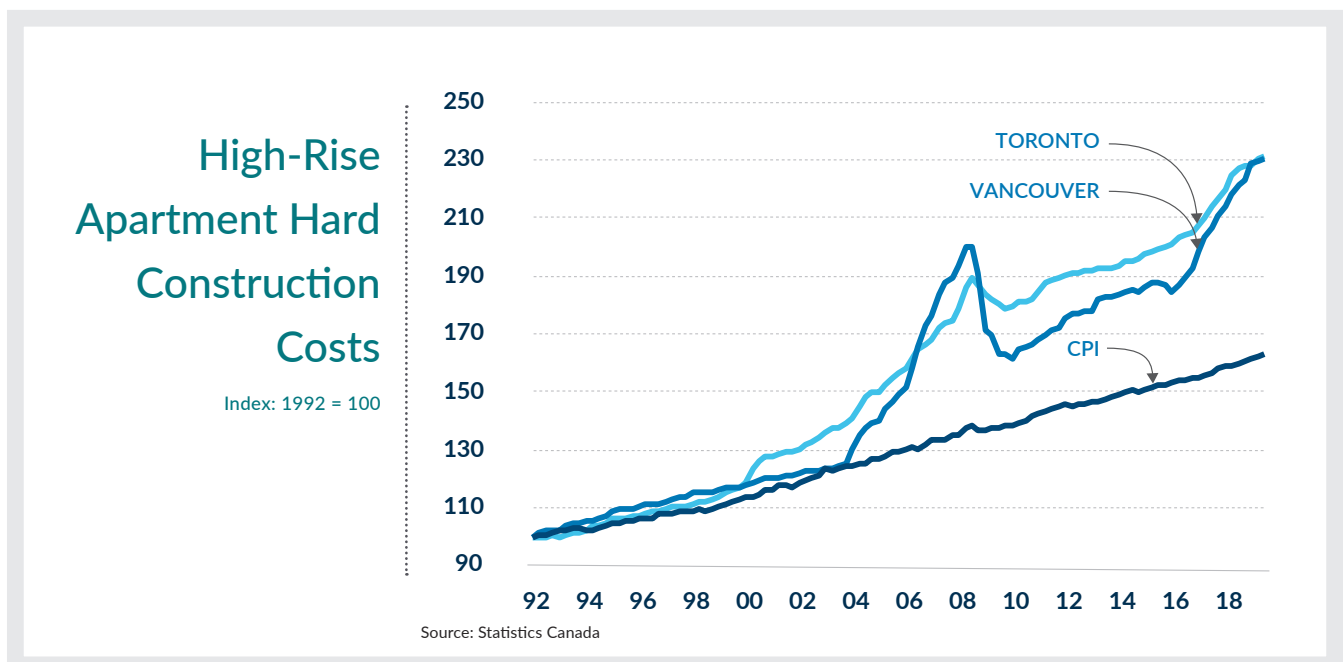
RESTRAINING NEW SUPPLY

Rising replacement costs have been a key factor in extending the positive cycle for commercial real estate occupancy and rent growth. But high costs have also exacerbated affordability challenges for both households and businesses. While headline consumer price indices show a benign inflation environment, the cost to build continues to soar.

Fortunately, there is emerging evidence of price-pressure relief on construction materials, but land costs, labour costs and development fees and other municipal charges are expected to continue to outpace inflation. Slow approvals in planning and

rezoning processes also add significant time and cost to development projects. The challenges are most acute in the multi-family residential markets in Toronto and Vancouver, where the construction industry is running up against capacity challenges, despite a pullback in investment in low-rise home construction. Even with the strong rent growth in Canadian markets, project economics are becoming more challenging.

Investment capital is drawn to development for incremental yield relative to acquiring in-place income from operating assets. Development can





L'Avenue, Montreal, Quebec

be a means of building resiliency in a portfolio by creating assets with a longer economic life. This wall of capital has pushed land values to extraordinary heights, particularly in multi-family residential, where purpose-built rental developers face fierce competition from condominium developers in acquiring land. As a result, markets where there is a lack of approved sites to meet demand, such as Toronto, have seen high-rise land values increase by as much as 150% to 200% over the past three years. Expect this trend to continue as new residential construction is now exempt from rent control in Ontario.

Soft costs including everything from development charges and other municipal levies to management fees, HST, financing costs and design consultant charges are also growing at an alarming rate as municipalities look to new development to fund community improvements and infrastructure.

Hard building costs have also been on the rise. And although tariffs on construction materials such as aluminum and steel receive most of the headline blame for increased costs, they pale

Markets where there is a lack of approved sites to meet demand, such as Toronto, have seen high-rise land values increase by as much as

150% to 200%

over the past three years

in comparison to the impact of wage inflation resulting from tight labour markets. A decline in labour productivity has exacerbated this increase. For example, construction trades that are working across different types of commercial projects to meet demand, as opposed to specializing, are creating inefficiencies. A demographic transition is also adding to productivity declines — over one-fifth of the current workforce in the construction trades is anticipated to be replaced over the next 10 years as older workers move into retirement. Significant knowledge transfer will need to occur to prevent further dips in productivity.

These barriers to new supply are helping drive rents and asset values higher. While it looks as though cost pressures may have peaked for this cycle, growth is anticipated to remain above the rate of inflation. Accordingly, investors can expect rising replacement costs to continue to exert upward pressure on rents over the medium term.

OPPORTUNITIES IN EMERGING TALENT CENTRES

BEYOND TORONTO AND INTO THE GREATER GOLDEN HORSESHOE

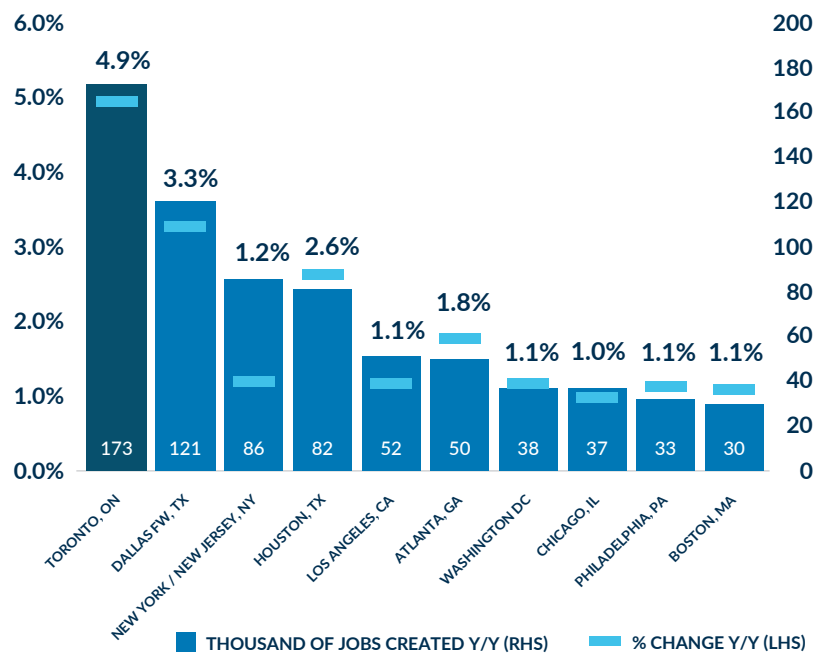
The Greater Golden Horseshoe (GGH) accounts for approximately 25% of Canada’s population and labour force. This mega-region consists of the Greater Toronto Area (GTA) (the City of Toronto and its surrounding suburbs) plus the surrounding areas that include Oshawa, Hamilton, St. Catharines-Niagara, and Kitchener-Cambridge-Waterloo (KCW). Factors such as shifting demographics, housing affordability and improved regional transit are increasing household mobility and blurring the

lines between primary and secondary markets. These dynamics are presenting interesting opportunities in certain property types within these traditionally second-tier cities.

Under Canada’s open immigration policy, incoming residents from abroad tend to gravitate toward large, multicultural metro areas, especially those with abundant job opportunities. This is particularly true for the GTA, which is home to a thriving job

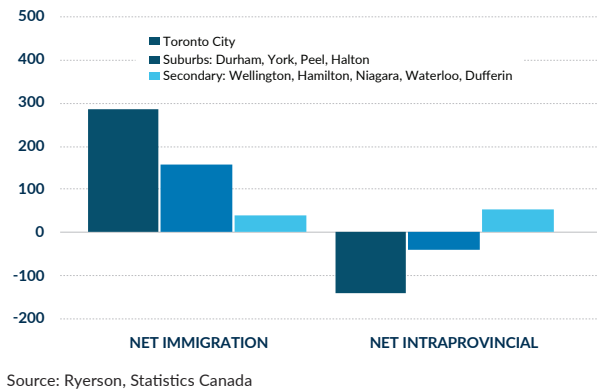
Metro Employment Growth Over the Past 12 Months

As of October 2019



Source: Statistics Canada; U.S. Bureau of Labor Statistics

Migration Trends Within the Greater Golden Horseshoe Thousand Persons, 2013 to 2018



market. Over the past year the GTA has generated over 170,000 jobs – more than three times its long-term average. This pace of job creation has outperformed by a wide margin that of other major North American cities.

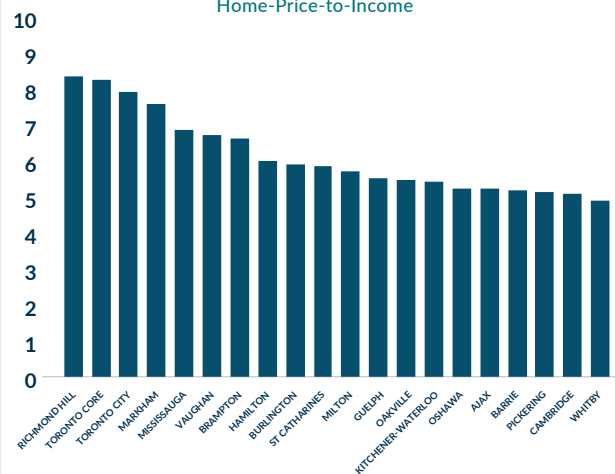
Population growth trends show that immigration has been a key driver for both the City of Toronto and its suburban areas. However, there is a drag on growth in the GTA as it is weighed down by an outflow of intraprovincial migration. This implies a “sprawling” effect as residents migrate to other parts of the province, largely within the secondary markets of the GGH. In fact, these secondary markets are seeing positive net intraprovincial migration. It is worth noting that this trend has picked up substantially. In 2008, the secondary markets saw a population increase of just 3,000 due to intraprovincial migration, while 11,600 residents relocated to this part of Ontario in 2018.

This trend is driven by the housing affordability challenges across most parts of the GTA. Home-price-to-income ratios are generally more favour-

able in the secondary markets of the GGH. This could serve as a “pull factor” for intraprovincial migration to this area, especially the KCW and Oshawa areas. Interestingly, net negative intraprovincial migration is most prominent in the 25 to 34 age group. Given that these residents are relatively early in their earning years, they are most sensitive to rising housing costs.

This sprawling migration has positive implications for real estate across most commercial property types. Logistics space will be in demand to provide more same-day services to customers. Necessity-based retail within these secondary markets will have additional consumer demand. As a critical mass of labour builds, it should generate demand for traditional and flex office space. And purpose-built rental apartments should also benefit from this migration trend, as renting is often an entry point in relocating to a new city.

Housing Affordability Across the Greater Golden Horseshoe Home-Price-to-Income





FUTURE OF WORKPLACE-AS-A-SERVICE

FLEX OFFICE PAUSES AFTER THE FAILED WEWORK IPO

Be careful not to interpret the failed WeWork IPO as a sign of impending doom for the broader flexible office market. Quite simply, there were too many red flags tied to its valuation, corporate governance, business model and path to profitability, especially through a full business cycle. But despite WeWork's woes, expect demand for flexible office solutions to continue as there has been a paradigm shift in how office space is being secured and used.

Occupiers like flexible office space for its convenience and optionality. It's a way to enter a new market or grow in an existing market. Modern, tech-enabled buildouts with highly amenitized communal spaces are attractive for employees. For employers, it's a way to promote innovation and helps with attracting and retaining talent. And given new changes to lease accounting rules, short-term office solutions are a way to unload non-core balance sheet assets (long-term leases) and outsource corporate real estate functions. To be sure, flex office operators have been an absorption accelerator during this expansion. But as WeWork downshifts, the pace of flex office absorption will undoubtedly slow despite its positive attributes noted above.

According to CBRE, flexible office space penetration in Canada is only 1.6%, and of that WeWork has only 25% market share. Thus, the possible failure of WeWork does not pose a systemic risk

to the Canadian office market. This is reflected in the strength of the operating environment in Toronto, Vancouver and Montreal, where strong end-user demand has pushed the vacancy rate to record lows. Although coworking was the genesis of WeWork and many other flex office providers, most of the growth in recent years has come from enterprise users. In the event WeWork were to give back space, many of its locations are in highly desirable urban areas that may even benefit from an increase in rent from releasing such space. In many such cases another flexible office space operator may step in. Occupiers will continue to seek flexible space as an increasingly large component of their real estate and talent management strategies.

“The possible failure of WeWork does not pose a systemic risk to the Canadian office market.”

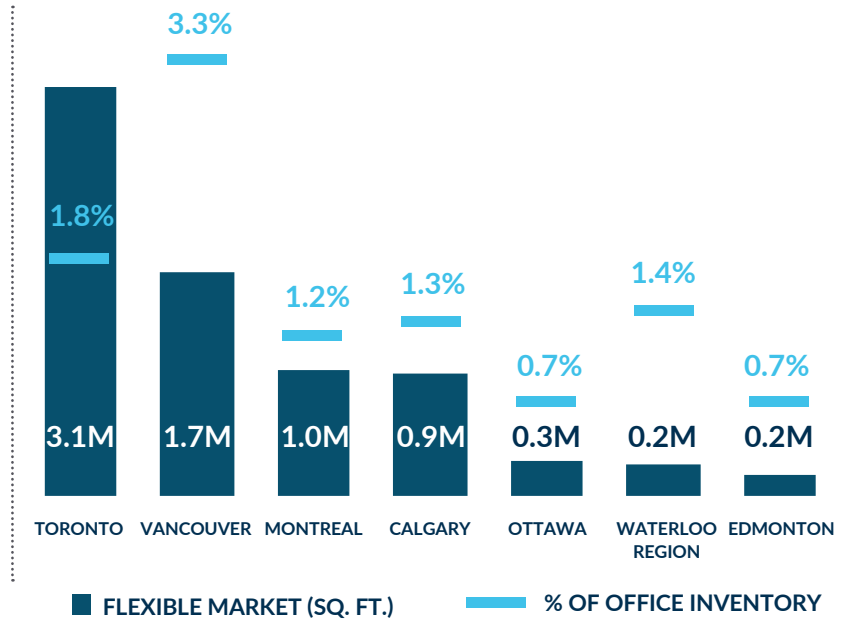
Several key structural forces underpin the demand for flexible office space. Work is becoming more project-based — a “set of tasks” rather than a “place you go.” As such, there will be increasing pressure for businesses to provide their employees with the

tools and options to work anywhere. In addition, the traditional relationship between employee and employer is evolving, and a more flexible labour landscape is emerging. Contingent workers are becoming an increasingly large share of the labour force, driven by new technologies that enable projects to be matched with skills in the gig economy. Expect these trends to continue to shape demand for “workplace-as-a-service” and for landlords to evolve their strategies to infuse flexible space into their product offerings.



Flexible Office Space Penetration by Market

Occupiers will continue to seek flexible space as an increasingly large component of their real estate and talent management strategies.



Source: CBRE, Q2 2019



EXTENDED RUNWAY FOR INDUSTRIAL

SUPPLY CONSTRAINTS TRUMP ANY PULLBACK IN DEMAND

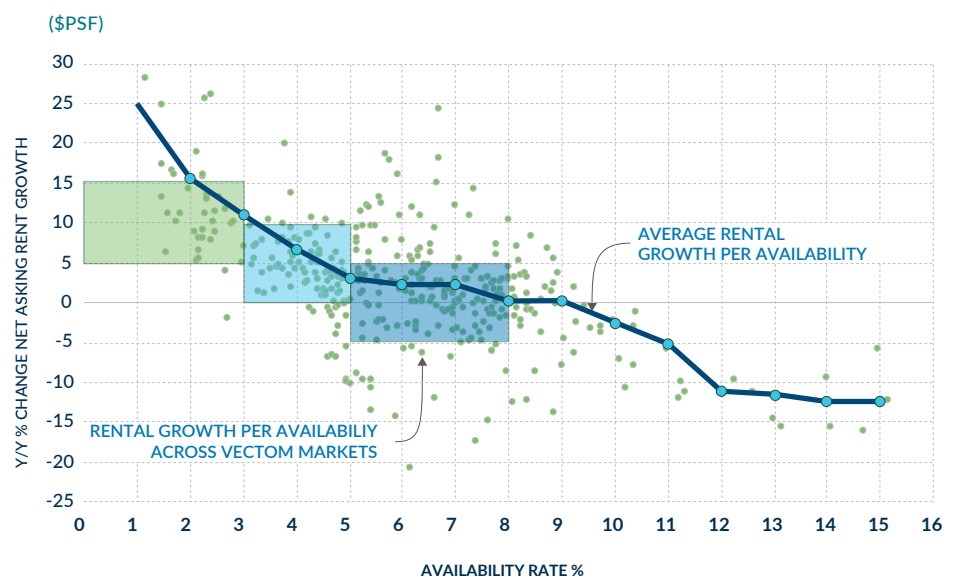
Technology continues to significantly disrupt the retail and industrial sectors as consumers buy more goods online. Ecommerce has driven demand from warehousing and logistics users to new heights. Speed is essential in this new environment, as rising service level expectations mean occupants need to be close to end consumers and must drive higher throughput of goods in their facilities. Ecommerce still accounts for less than 10% of all retail sales, but is growing at 34% annually, according to Statistics Canada's latest figures. Online grocery shopping is still in its infancy, but given that food stores account for roughly one-third of core retail sales, even small shifts in digital sales represent significant dollar amounts.

In Canadian markets, this strong demand is decreasing industrial availability, which stands at 2.9% as of Q3 2019, the lowest level on record. Under these tight conditions, net asking rents have increased by a staggering 15.7% year-over-year, to \$8.63 per square foot.

When observing the relationship between availability and rent growth across the six major markets in Canada, shown in the chart below, rent growth appears to stabilize at around 2% per annum within the 5% to 8% availability range. Below 5% rent growth begins to increase sharply and trend toward double digits. Looking at Toronto and Vancouver,

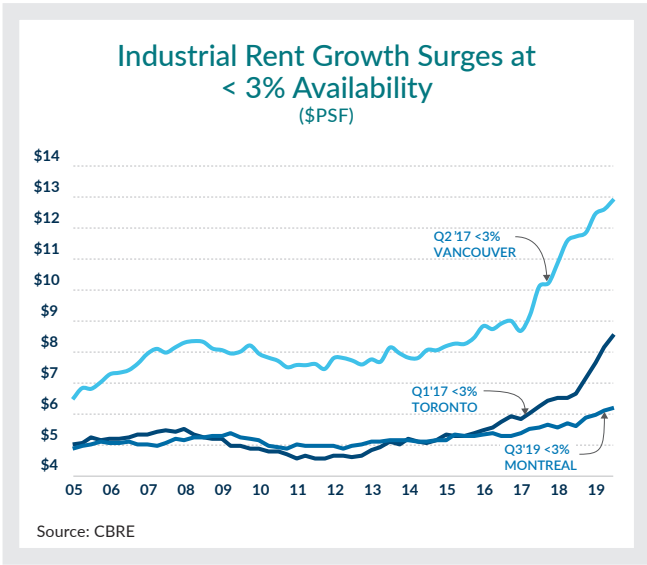
Canadian Metro Industrial Rent Growth vs. Availability

In Canadian markets availability stands at 2.9% as of Q3 2019



Source: BentallGreenOak Research, CBRE

Note: Quarterly observations from 1995 - 2019: Vancouver, Edmonton, Calgary, Toronto, Ottawa and Montreal



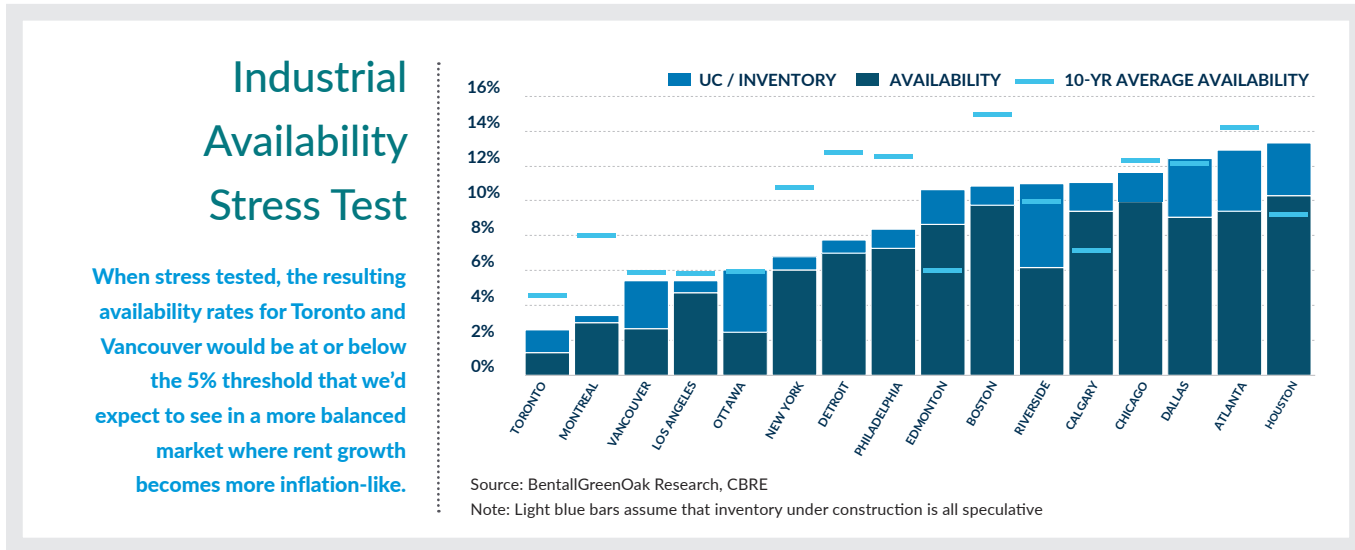
inflection points of strong rent growth occur at 3% availability. Industrial availability in Montreal has just breached 3% and is poised to follow the same trend.

Toronto, Vancouver and Montreal are among the five tightest industrial markets in North America. Historically, due to shorter development time-frames, industrial construction pipelines tend to be more responsive to tight conditions. In similar environments, over-building has been a downside risk that disrupts fundamentals. And development activity has reached record levels in Toronto and Vancouver, but still only accounts for 1.2% and 2.5% of existing inventory, respectively. When stress tested, assuming this new supply enters the market vacant, the resulting availability rates for Toronto and Vancouver would increase to

2.4% and 5.0%, respectively – at or below the 5% threshold that we’d expect to see in a more balanced market where rent growth becomes more inflation-like.

To be sure, this is an unlikely scenario, as 60% and 77% of the incoming new supply has been pre-leased in Vancouver and Toronto respectively. In Montreal, the current construction volume accounts for only 0.4% of inventory, and with an availability rate of 2.8%, this market is even less vulnerable to a supply shock. While Calgary and Edmonton only account for 15% of the total industrial market, their elevated availability rates do pose a downside risk.

Overall, there appears to be minimal risk of significant dislocation within the Canadian industrial sector, as conditions are tight enough to withstand a pullback in demand across the country’s biggest markets. Persistent low vacancy in Toronto, Vancouver and Montreal should continue to drive robust rental growth as we head into 2020.



TWO
ST. THOMAS



ABOUT BENTALLGREENOAK

BentallGreenOak is a leading, global real estate investment management advisor and a globally-recognized provider of real estate services. BentallGreenOak serves the interests of more than 750 institutional clients with approximately \$48 billion USD of assets under management (as of September 30, 2019) and expertise in the asset management of office, retail, industrial and multi-residential property across the globe. BentallGreenOak has offices in 24 cities across twelve countries with deep, local knowledge, experience, and extensive networks in the regions where we invest in and manage real estate assets on behalf of our clients. BentallGreenOak is a part of SLC Management, which is the institutional alternatives and traditional asset management business of Sun Life.

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ON THE COVERS

FRONT COVER: Quarry Park, Calgary, AB

INSIDE BACK: 2 St. Thomas, Toronto, ON

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