Q2 2022

OTTAWA MARKET REPORT

By Darren Fleming, CEO & Broker of Record, Real Strategy Advisors

Data provided by CoStar

OVERVIEW

Although most COVID-19 restrictions had been lifted in the second quarter of 2022, the anticipated large-scale return of office workers still hasn't happened. From the increasing adoption of hybrid work models to the seventh COVID-19 wave, Ottawa's office market recovery is still slow and sprawling to say the least. The majority of public sector employees continue to work from home and there's still no clear expectation when that might change.

Canada still continues to experience record inflation, which reached a year-over-year 8.1% increase in June following a 7.7% increase the month before (Statistics Canada). This has lead the Bank of Canada to implement several interest rate hikes as a cooling measure. Finally, the country is also in the midst of a serious labour shortage causing competition for top talent to escalate. All of these factors are causing economists to warn about a possible "moderate and short-lived" Canadian recession in 2023 (Royal Bank of Canada).

Even with these cloudy economic forecasts (e.g. The Conference Board of Canada has decreased the country's expected economic growth to 3.5% for 2022 and 2.6% in 2023, down from 4.0% and 3.3% respectively), the situation in Ottawa isn't as dour. People in Ottawa have still been feeling the squeeze on gas, groceries, and the general cost of living but, when compared to other major Canadian markets. This can be attributed to the high population of well-paid public servants continuing to consume goods/services which allows Ottawa's local economy to remain fairly stable.

According to Ottawa Employment Trends, the unemployment rate as of June was down a whole percentage point to 3.9% from a month earlier. That's 5.1% lower than the peak in August of 2020. At the same time, the continued lack of government employees occupying downtown office space have decimated some of the older assets, several of which are now even being considered for residential or mixed-use redevelopment.

When it comes to commercial office space, the major trends of tenants continuing to downsize (or right-size) space while at the same time, showing a preference for higher quality buildings, with excellent transit accessibility and good parking are still holding strong. As a result, Class A property vacancies aren't far off their historical average as they steal tenants from Class B & C landlords. These owners are now feeling the squeeze to make considerable capital investment into properties in order to attract and retain tenants.

LEASING

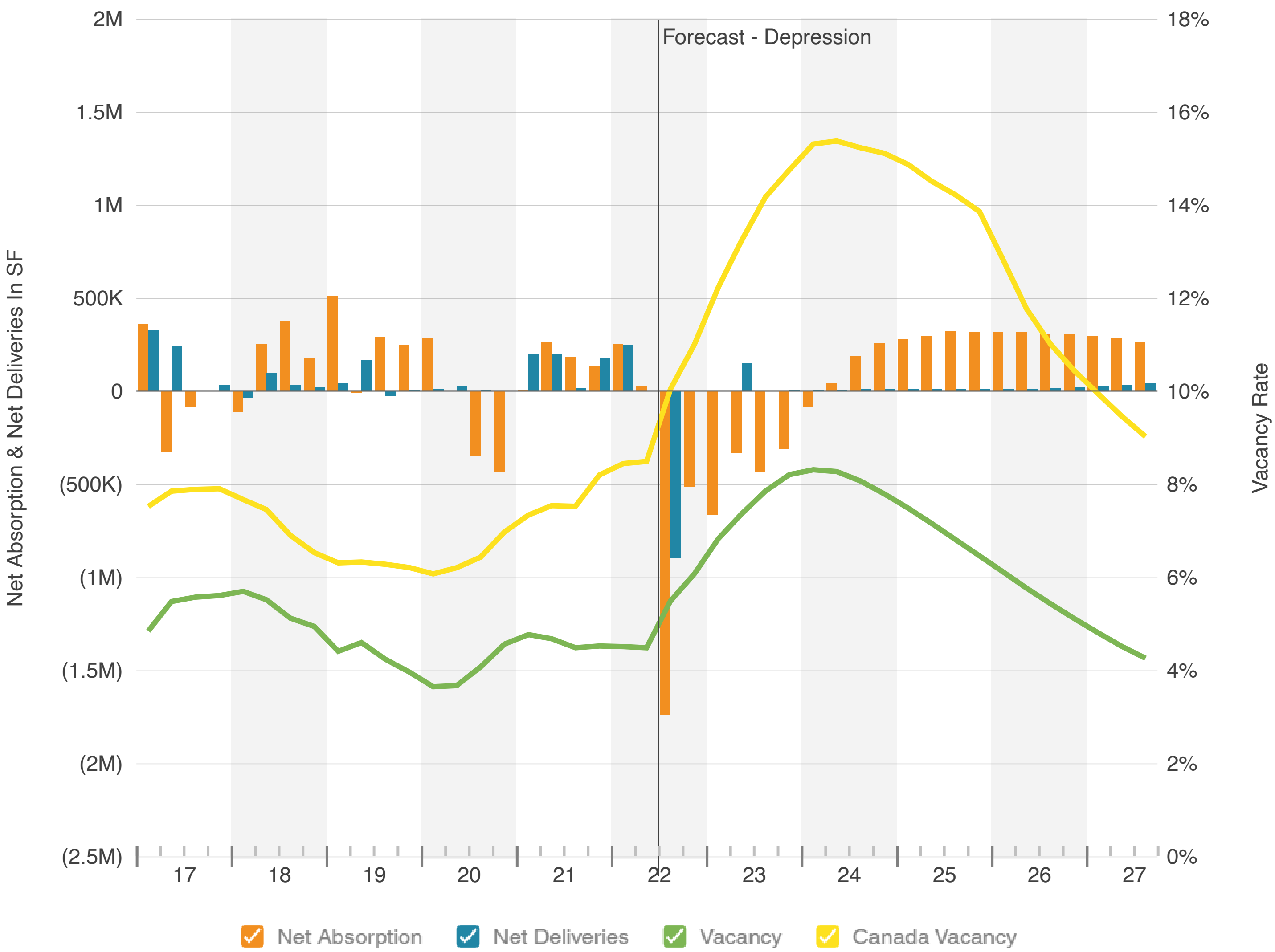
By end of Q2, demand for space slightly exceeded the amount of new space coming onto the market, resulting in virtually neutral absorption. Although this is a positive sign of stability, the leases getting signed are shorter, and offices are generally smaller. As such, Real Strategy Advisors is predicting there could still be a lot of excess space coming back onto the market over the next 12-18 months.

Office availability in Ottawa now sits at 6.4%, which is considerably lower than the national rate of 11.1% and mainly due to federal government tenants who continue to pay for their space in spite of it sitting vacant. We do not expect this trend of tax dollars paying for empty offices to continue indefinitely.

The physical presence of public servants has long underpinned the stability of Ottawa's office sector. Therefore, as the Government of Canada continues to implement hybrid work via the creation of co-working sites in suburban buildings vs. densely occupied downtown offices by reducing their overall office footprint. The federal government has also committed to making their real estate portfolio carbon neutral over the next 25 years and will be exiting older office buildings in favour of newer and more energy-efficient ones. The pace of this program's implementation, labeled GCWorkplace (link), remains unclear.

LEASING

NET ABSORPTION, NET DELIVERIES & VACANCY

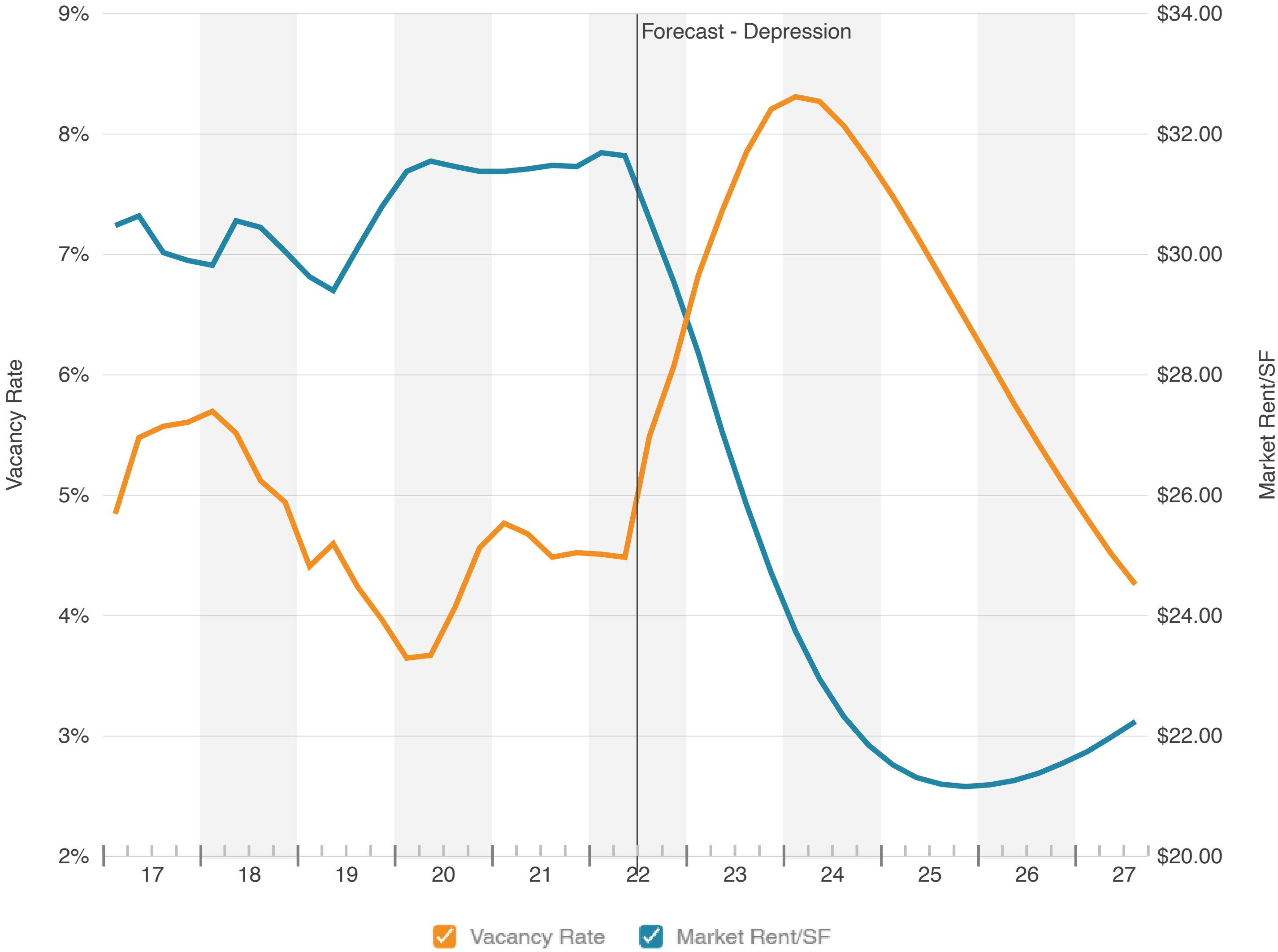


* Images provided by CoStar

Ottawa's office vacancy is now 4.4% and, although the overall space available for sublet has decreased when compared to this time last year, subletting is on the rise in submarkets like Kanata and Ottawa's downtown core. Like their public servant counterparts, many tech firms and other companies are also moving forward with hybrid working models and signing shorter term leases. However, private sector and not-for-profit tenants are expecting large cash allowances to offset construction costs. All these shifts coincide with the move to better quality space given the tenant-tilted market. Class B and Class C landlords will have no option but to upgrade.

LEASING

VACANCY & MARKET RENT PER SF



* Images provided by CoStar

NOTABLE LEASES

TOP OFFICE LEASES PAST QUARTER

Building Name/Address	Submarket	Leased SF	Tenant Name
Ericsson	Kanata	248,579	Ericsson
Transportation Building	Lowertown	26,000	Global Relay Communications
495 March Rd	Kanata	18,025	Alphawave IP
Hunt Club Crossing	Colonnade/Rideau Heights	16,144	Knak Inc.
Park of Commerce	Blair/Ogilvie	14,987	CIMA
2286 Carling Ave	Queensview/Morrison	11,092	Sage Tattoo
309 Legget Dr	Kanata	10,354	Alphawave IP
1031 Bank St	Glebe	10,354	CAA North & East Ontario

* Statistics provided by CoStar

RENT

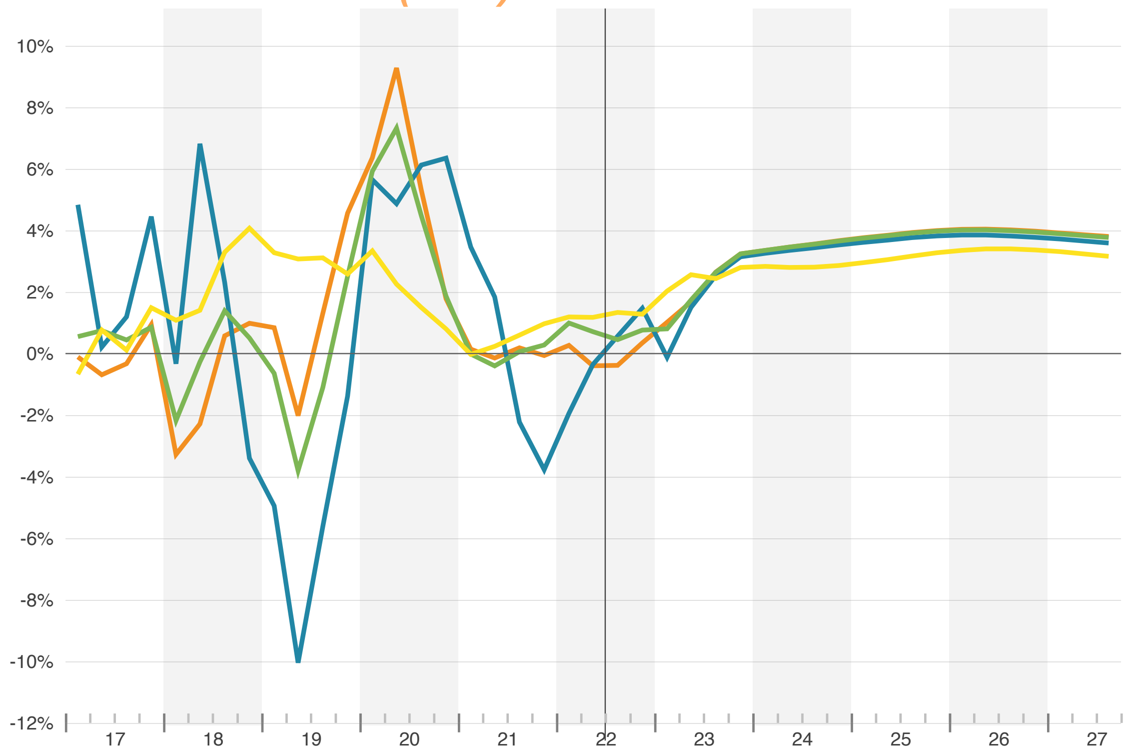
Given the less than stellar leasing market, market rent and growth is still fairly stagnant. Since Ottawa has a higher than normal density of public sector tenants, there hasn't been the same level of rental rates declines like in other major cities. That said, rent growth over the past 12 months has only been 0.5% and the asking rates actually decreased ever so slightly in the second quarter this year on account of more space being available.

As the market recovery takes hold, we're expecting to see rents stabilize and start to return to an upward trajectory. As we've been noting for some time, rental rates have generally remained stable throughout the pandemic as landlords (especially of Class A properties) have opted for shorter leases (one to three years), more lenient termination and sublease clauses, as well as increased improvement allowances and outfitting periods. The trend of shorter lease durations indicates that everyone wants to see what the long-term effects of hybrid work are before locking in.

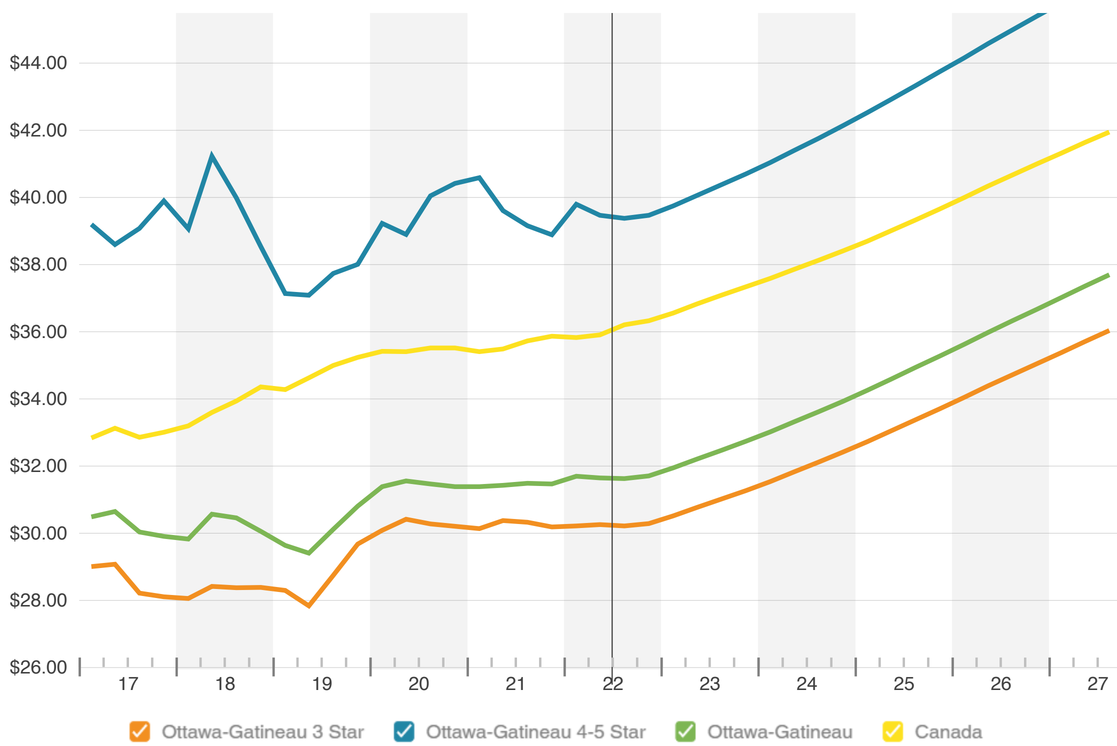
RENT

* Images provided by CoStar

MARKET RENT GROWTH (YOY)



MARKET RENT PER SQUARE FOOT



SALES

Real Strategy Advisors remarked last volume how the story for the year so far has been large portfolio transactions (sales volumes of $975 million over the past year). Although that is the case, when we zoom out and look at the pandemic as a whole, institutional investors have also been divesting from office space. Why? Office buildings are now seen as riskier investments than pre-pandemic, due to the potential for long-term decrease in tenant demand due to hybrid work.

Some of the biggest transactions this year have been the purchase of Park of Commerce (a three-tower office complex) by Crown Realty Partners as well as the two neighbouring office buildings on Bank Street purchased by BTB REIT. Then there's the purchase of a 24-property portfolio for $155 million by Woodbourne Capital Management and Epic Investment Services. The portfolio included five office properties in the southern and eastern suburbs.

In those first two cases, the strategy is clearly banking on the fact that people will still want high-quality, modern office space downtown with lots of nearby amenities like restaurants, gyms, transportation, and retail. Whereas, The location of the offices in the third portfolio transaction suggests that the buyers would like to market them to organizations looking to meet a demand for a more distributed workforce and need for suburban locations with ease of access for employees.

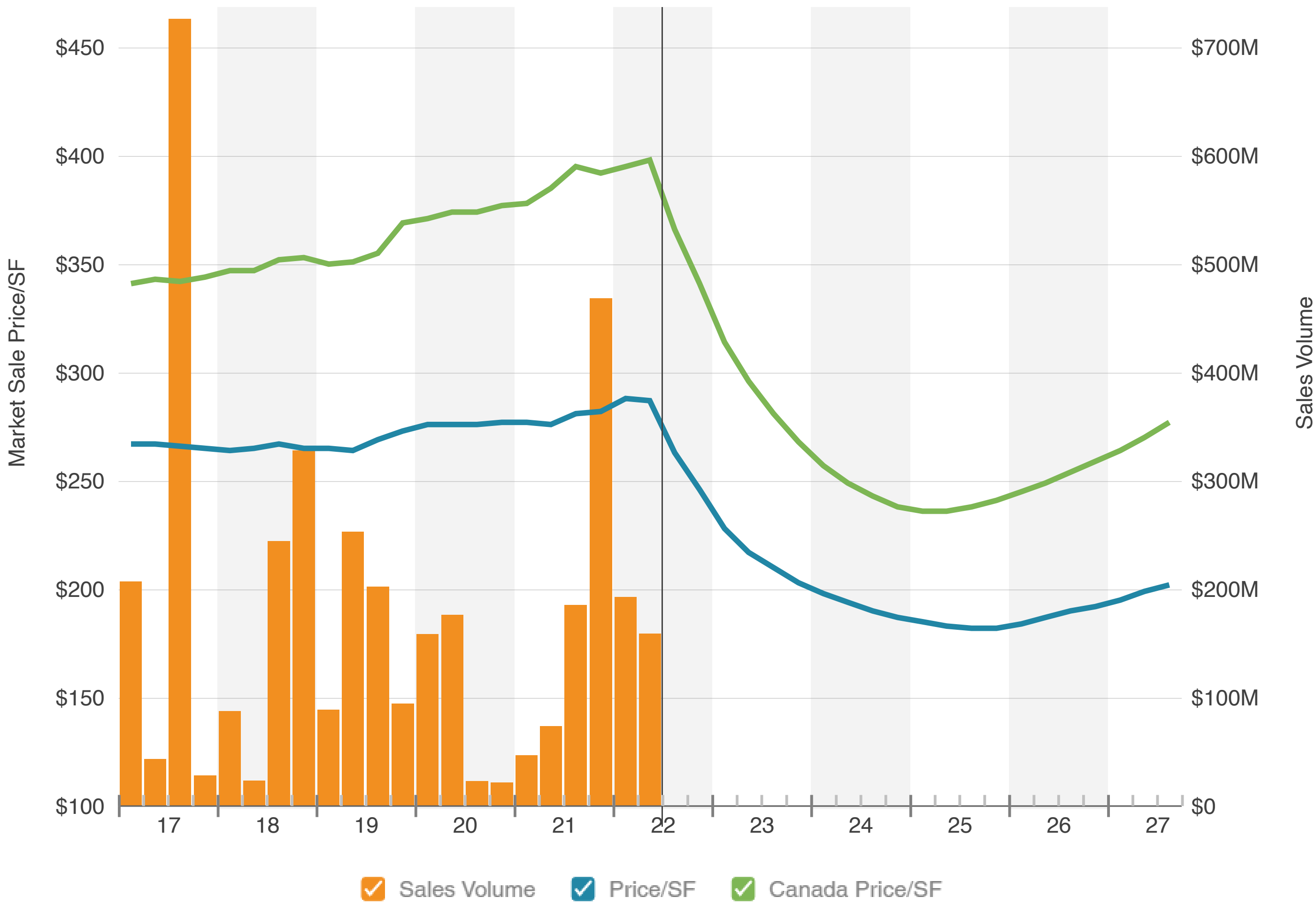
Recent Significant Sales:

- 700 Silver Seven Rd with 73,330 SF sold for $15,450,000 ($211/SF) in early June

- Kinaxis Phase 1 at 8700 Campeau Dr with 150,000 SF sold for $61,650,000 ($411/SF) in late June
($250/SF) in mid-March

SALES

SALES VOLUME & MARKET SALE PRICE PER SF



113	5.3%	$236	10.8%
SALE COMPARABLES	AVG. CAP RATE	AVG. PRICE/SF	AVG. VACANCY AT SALE

* Images provided by CoStar

SUBMARKETS

SUBMARKET RENT

		Market Rent		12 Month Market Rent		QTD Annualized Market Rent	
No.	Submarket	Per SF	Rank	Growth	Rank	Growth	Rank
1	Alta Vista	$28.31	22	0.7%	16	-2.2%	21
2	Barrhaven	$33.80	2	-0.3%	23	1.9%	7
3	Belfast/Sheffield	$28.53	19	-0.6%	26	-11.2%	25
4	Bells Corners/Crystal Beac	$28.90	17	0.3%	18	5.8%	2
5	Blair/Ogilvie	$28.42	20	1.9%	4	0.1%	17
6	CBD	$36.75	1	-0.3%	24	-2.1%	20
7	Centrepoint/Qualicum	$31.34	8	0.3%	17	2.7%	4
8	Centretown	$33.74	3	0.1%	21	1.0%	14
9	Colonnade/Rideau Heights	$27.06	25	1.3%	7	0.5%	16
10	East Outer Ottawa	$28.40	21	1.5%	5	3.2%	3
11	Gatineau	$26.85	26	0.8%	14	-13.6%	26
12	Gatineau Downtown	$28.12	23	1.0%	11	0.8%	15
13	Glebe	$31.45	7	3.0%	2	-0.5%	18
14	Goulbourn/West Carleton	$30.71	10	0.9%	12	1.6%	9
15	Heron/Riverside	$32.06	6	-0.6%	25	1.2%	13
16	Hull Downtown	$30.21	11	2.4%	3	1.3%	12
17	Hunt Club/Walkley	$28.85	18	0.2%	19	-10.8%	24
18	Kanata	$29.05	16	1.2%	8	-8.0%	23
19	Lowertown	$32.07	5	1.1%	9	1.8%	8
20	Merivale	$30.02	12	1.0%	10	9.5%	1
21	Montreal Road	$29.40	15	0.9%	13	2.0%	5
22	NW Outer Ottawa	$27.76	24	5.6%	1	1.5%	10
23	Orleans	$29.41	14	1.5%	6	1.9%	6
24	Queensview/Morrison	$29.74	13	-0.2%	22	-7.9%	22
25	Tunney's Pasture	$30.75	9	0.1%	20	1.5%	11
26	Woodward/Carling	$32.17	4	0.7%	15	-1.1%	19

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SUBMARKETS

SUBMARKET VACANCY & NET ABSORPTION

		Vacancy			12 Month Absorption			
No.	Submarket	SF	Percent	Rank	SF	% of Inv	Rank	Construc. Ratio
1	Alta Vista	63,204	4.8%	15	(19,621)	-1.5%	22	-
2	Barrhaven	-	-	-	2,751	0.2%	16	-
3	Belfast/Sheffield	98,396	4.5%	14	55,683	2.6%	5	-
4	Bells Corners/Crystal Beac	37,262	2.8%	10	8,941	0.7%	14	-
5	Blair/Ogilvie	179,161	7.2%	19	(6,195)	-0.2%	21	-
6	CBD	1,312,522	7.3%	20	(182,126)	-1.0%	26	-
7	Centrepoint/Qualicum	9,597	0.7%	3	20,256	1.5%	11	-
8	Centretown	366,321	4.9%	16	18,264	0.2%	13	-
9	Colonnade/Rideau Heights	65,904	2.4%	9	63,379	2.3%	4	-
10	East Outer Ottawa	1,000	0.7%	2	(1,000)	-0.7%	19	-
11	Gatineau	133,380	1.7%	6	283,217	3.7%	1	0.6
12	Gatineau Downtown	-	-	-	4,960	1.7%	15	-
13	Glebe	49,228	7.2%	18	18,922	2.8%	12	-
14	Goulbourn/West Carleton	13,305	2.0%	7	159,440	24.2%	2	0.9
15	Heron/Riverside	82,809	3.9%	13	(20,771)	-1.0%	24	-
16	Hull Downtown	60,498	0.8%	4	79,444	1.0%	3	1.2
17	Hunt Club/Walkley	261,508	8.4%	21	50,429	1.6%	7	-
18	Kanata	636,628	8.8%	22	(48,020)	-0.7%	25	-
19	Lowertown	159,336	3.0%	11	53,153	1.0%	6	-
20	Merivale	37,785	30.1%	23	(20,365)	-16.2%	23	-
21	Montreal Road	70,694	2.3%	8	(885)	0%	18	-
22	NW Outer Ottawa	-	-	-	0	0%	-	-
23	Orleans	7,269	1.3%	5	40,820	7.6%	9	-
24	Queensview/Morrison	42,022	3.3%	12	(1,113)	-0.1%	20	-
25	Tunney's Pasture	49,518	0.7%	1	30,730	0.4%	10	-
26	Woodward/Carling	169,343	5.0%	17	40,896	1.2%	8	-

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