Q1 2023

OTTAWA MARKET REPORT

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

Data provided by CoStar

OVERVIEW

The inflation rate fell to 5.2% in February (below the expected 5.4%) and was down from 5.9% in January.[1] This is in large part due to the Bank of Canada's monetary tightening campaign, which continued into the new year seeing the target overnight interest rate raised from 4.25% to 4.50% in late January.[2] Net inflation has consecutively fallen (albeit slowly) for almost six months now. Despite the progress, many economists are still calling for a mild economic recession this year which will likely trigger monetary easing policies to help fuel a recovery in 2024.[3]

Looking at Ottawa-Gâtineau more specifically, the region closed-out the first quarter of 2023 with an unemployment rate of 4.1%.[4] Over the past year, the unemployment rate has decreased by 0.4%[5] and is a far cry away from the 9.5% peak unemployment observed in June 2020.[6] That said, it's 6,100 new part-time positions [7] that are responsible for the net employment increase during the first quarter as there was a decline of 4,000 full-time jobs.[8] Although the city's combination of public and private sectors is a strong one, people are not insulated from economic impact and the near-universal higher costs of living.

1: https://tradingeconomics.com/canada/inflation-cpi
2: https://www.bankofcanada.ca/core-functions/monetary-policy/key-interest-rate/
3: https://www.budget.canada.ca/2023/report-rapport/overview-apercu-en.html#a5
4,5,6,7,8: https://www150.statcan.gc.ca/n1/daily-quotidien/230406/t007a-eng.htm

The public sector's return to the office initiative is now in motion and has been ramping up since the end of 2022. The directive is in line with the standard hybrid work expectations of two to three days per week spent at the office that has been playing out in the private sector. Given the tumultuousness in the tech sector of late, restructuring has seen impacts on the Kanata market with vacancy rates of 7.9% (the Central Business District's vacancy is 8.0% for comparison). Subleases and vacancy rates will likely continue to rise as most tenants require less space now (and come renewal) due to hybrid plans.

We are currently observing a lot of the same trends from the end of 2022 so far this year. Mainly: lower leasing demand due to the general uncertainty of will-they, won't-they hybrid work models. Most organizations still look at in-office attendance as vital but are focusing on the areas where this is most necessary. Employers will need to stay attuned and account for what their employees value most (autonomy, flexibility, and work-life balance) to figure out the optimal hybrid model and how that translates to office square footage.

All of these questions and current conversations tie into the decarbonization discussion too. With emissions and net-zero targets set for the coming decades, owners and operators will need to upgrade their buildings to meet these goals and attract tenants. Whereas historically, Class A and B buildings downtown followed similar vacancy trends, the 'flight to quality' trend that's been observed has inverted the relationship. Older spaces will struggle to retain tenants in a market where better and more modern space is available with increased incentives.

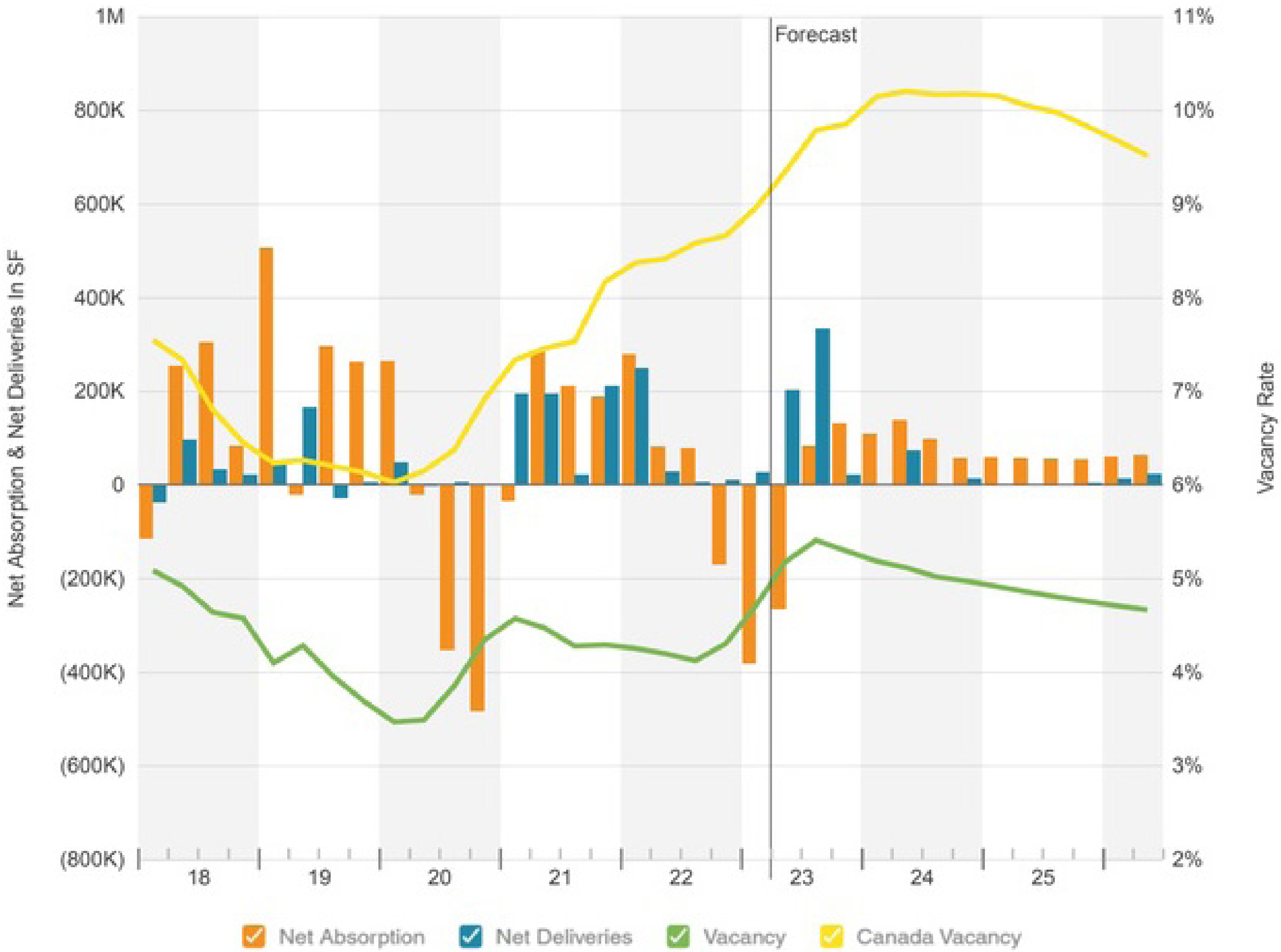
LEASING

The first quarter of 2023 saw a lot of space come back onto the market resulting in negative net absorption (~375,000 SF). With roughly 25,000 SF in net deliveries and tenants continuing to shed space, the vacancy rate continued its steep ascent that started in the latter half of last year. Whereas the national vacancy rate started to climb at the beginning of the pandemic and has continued to do so, Ottawa was able to buck the trend from early 2021 to mid-2022. Although the city's vacancy rate sits much lower than the national average, it is increasing at a faster rate.

Demand for outdated offices has disappeared and tenants are looking for magnetic spaces that foster collaboration and productivity. Other important factors driving the leasing activity are a desire for shorter commute times and improved office profiles or layouts. Tenants are looking for accessible spaces that will encourage office utilization along with opportunities for more employee (even client) engagement.

LEASING

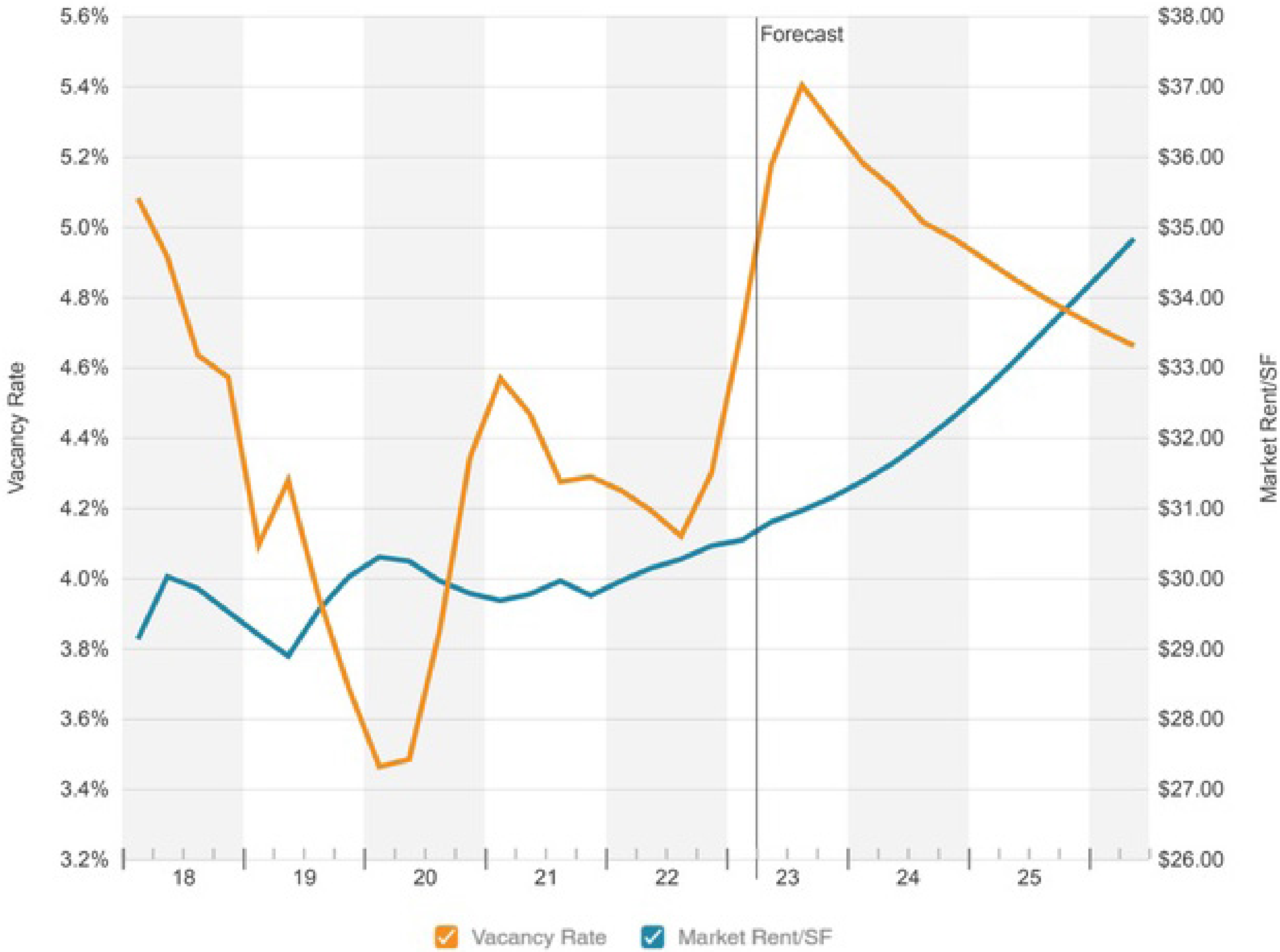
NET ABSORPTION, NET DELIVERIES & VACANCY



* Graph provided by CoStar

LEASING

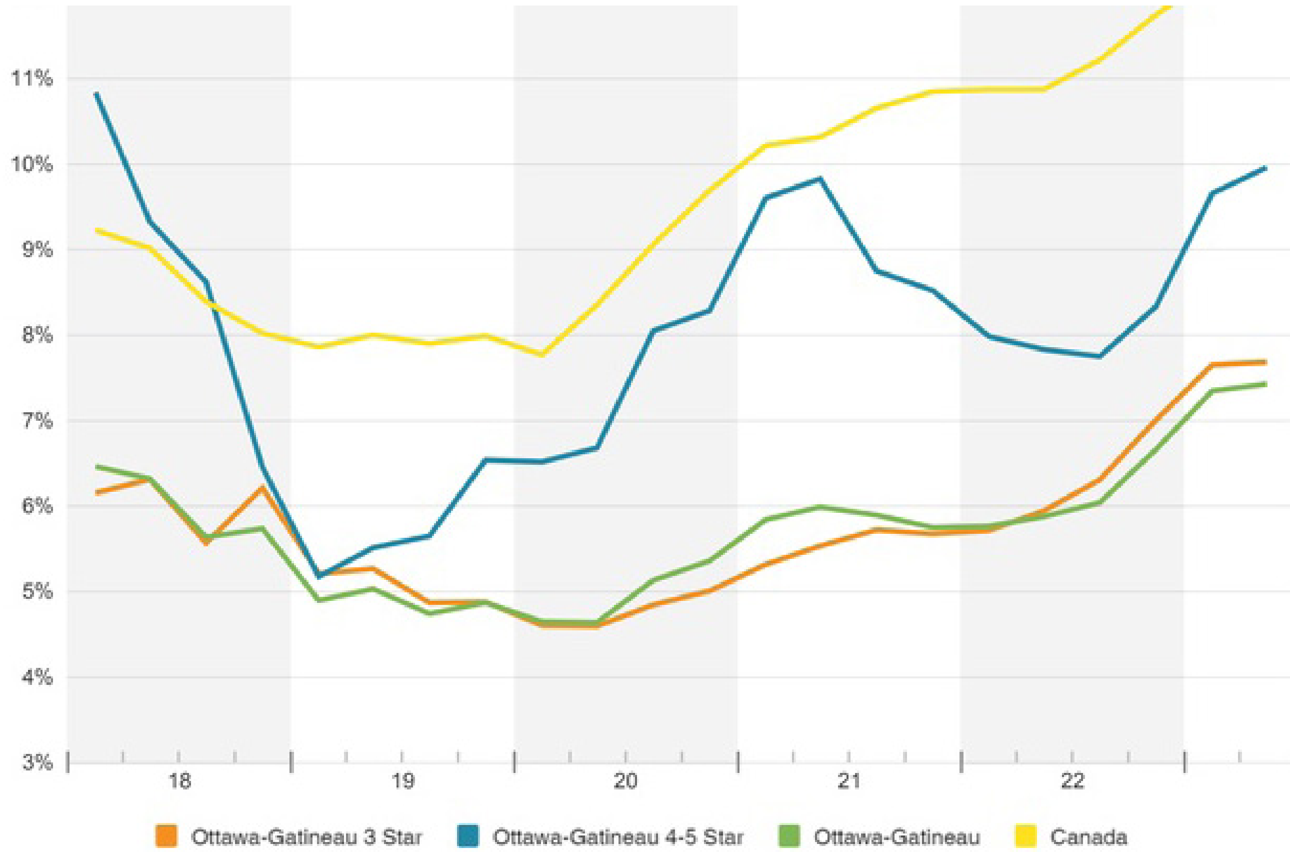
VACANCY & MARKET RENT PER SF



* Graph provided by CoStar

LEASING

AVAILABILITY RATE



TOP OFFICE LEASES PAST QUARTER

Building Name/Address	Submarket	Leased SF	Tenant Name
349 Terry Fox Drive	Kanata	248,586	Ericsson Canada Inc
360 Terry Fox Drive	Kanata	15,573	Emcon Emanation Control Ltd
535 Legget Drive	Kanata	13,334	Solace Systems Inc
123 Slater Street (Suite 800)	Downtown	10,556	Cuso International
100 Queen Street (Suite 940)	Downtown	7,550	La Vie Health Centre
10 Rideau Street (Suite 400)	Fringe Core	6,579	NEUF

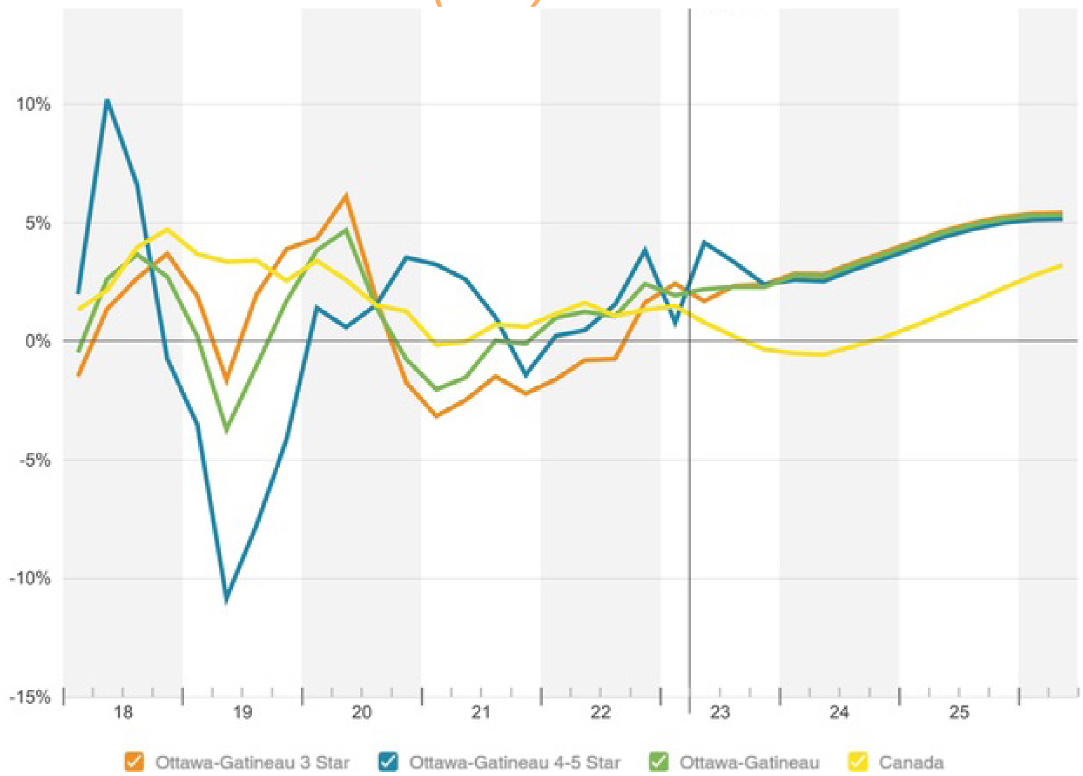
* Graph & statistics provided by CoStar

RENT

As has been the case throughout the pandemic in Ottawa, landlords have settled for shorter leases (less than five years as opposed to more), offer cash inducements, and extended fit-up periods instead of lowering rates. In fact, the last 12 months saw a 2% growth in market rent. The average rent continued to climb steadily, despite vacancies, increasing about 80 cents over the first quarter and sitting at ~$32.55/SF. Although rents in Ottawa have been under pressure when compared to their long-term history, they are expected to stabilize over the next quarter.

RENT

MARKET RENT GROWTH (YOY)



DAILY ASKING RENT PER SF

* Graphs provided by CoStar

SALES

Ottawa-Gatineau sales volume fell to its lowest point (~$50M), not seen since the first quarter of 2021. The overall sales price in Ottawa, which has been slowly decreasing since mid-2021, also went from ~$265/SF to ~$260/SF. All of this is likely reflective of the increased risk of commercial real estate in Ottawa as an investment.

With the advent and adoption of hybrid work, government and longtime tenants are no longer as stable as they once were. Furthermore, the federal government will be unloading millions of square feet of leased space over the coming years as part of their GCWorkplace and Greening Government Strategy programs. Although this space won't come onto the market all at once, the impact will still be felt by the region's commercial real estate market.

Significant Sales from Q1 2023:

- 1900 & 2000 City Park Drive (with 93,500 SF) was purchased by Colonnade BridgePort for $20,000,000

- 31 Hyperion Ct (with 39,879 SF) was purchased for $7,350,000

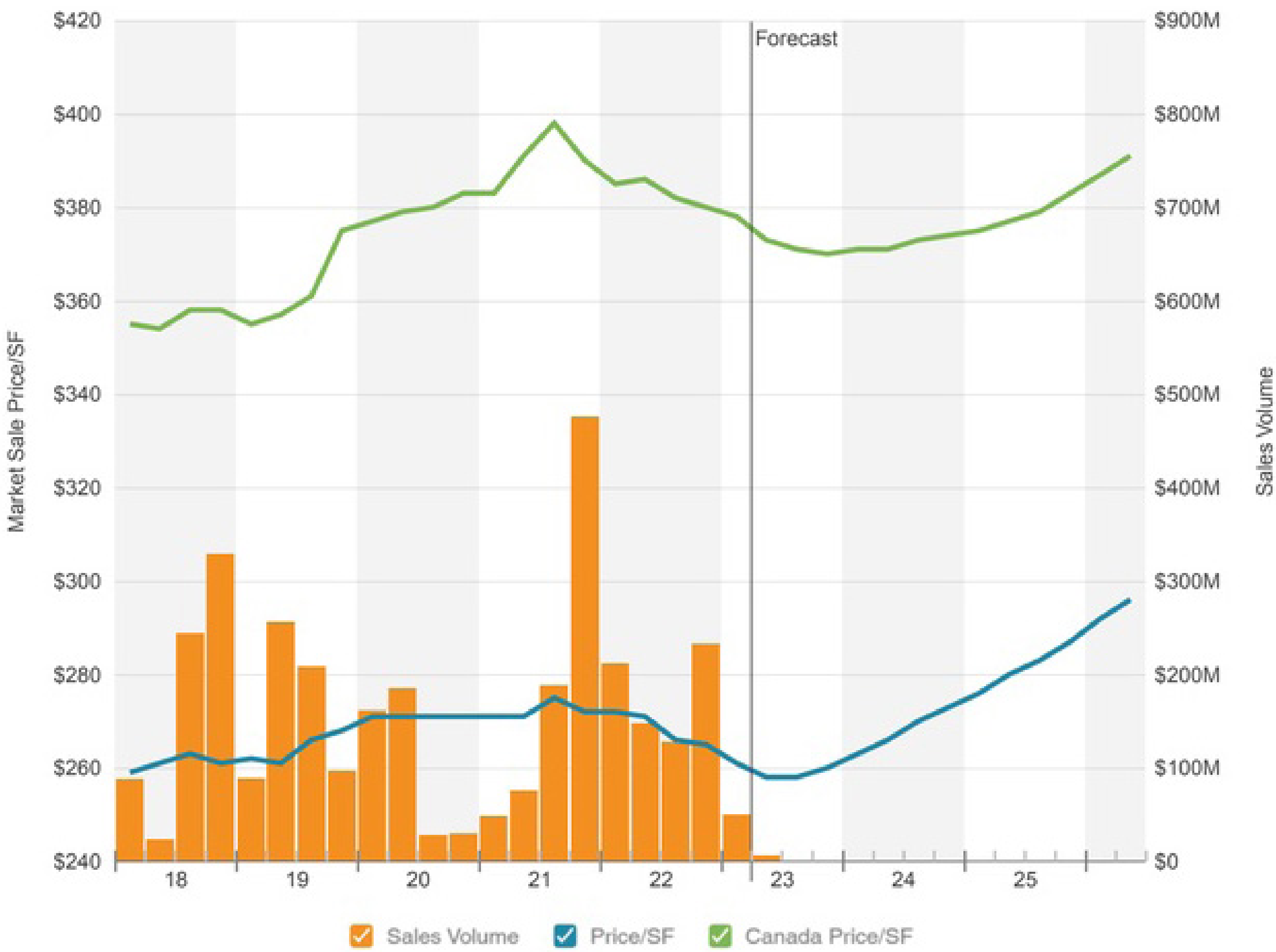
- 169 Colonnade Road South (with 11,896 SF) was purchased by Ziebarth Electrical Contractors Inc. for $4,200,000

- 380 Hunt Club Road (with 50,869 SF) was purchased by Vital Properties Inc. for $4,080,000

- 285-295 Montreal Road (with 7,000 SF) was purchased by Wabano Centre for Aboriginal Health Inc. for $2,700,000

SALES

SALES VOLUME & MARKET SALE PRICE PER SF



78	6.1%	$242	6.7%
SALE COMPARABLES	*AVG. CAP RATE*	*AVG. PRICE/SF*	*AVG. VACANCY AT SALE*

* Graph & statistics 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	CBD	$35.50	2	1.6%	8	2.2%	8
2	Centretown-Byward	$32.09	3	1.7%	7	2.5%	7
3	East Central	$28.67	8	2.0%	6	10.8%	3
4	Gatineau	$35.54	1	2.5%	4	3.4%	6
5	Greater Kingston	$26.91	9	1.1%	10	41.7%	1
6	Kanata	$28.84	7	1.4%	9	4.5%	5
7	Northeast Ontario	$25.97	10	2.6%	2	5.2%	4
8	Papineau-Pontiac	$30.16	5	8.3%	1	14.9%	2
9	Tunney's Pasture	$30.17	4	2.5%	3	2.1%	9
10	West Central	$29.89	6	2.4%	5	-1.2%	10

SUBMARKET VACANCY & NET ABSORPTION

		Vacancy			12 Month Absorption			
No.	Submarket	SF	Percent	Rank	SF	% of Inv	Rank	Construc. Ratio
1	CBD	1,470,825	8.0%	9	(64,413)	-0.4%	7	-
2	Centretown-Byward	785,429	5.8%	7	(203,160)	-1.5%	10	-
3	East Central	618,266	4.8%	6	92,765	0.7%	1	-
4	Gatineau	239,583	1.5%	1	(8,731)	-0.1%	4	-
5	Greater Kingston	92,109	3.4%	4	38,804	1.4%	2	-
6	Kanata	902,104	7.9%	8	(188,049)	-1.7%	9	-
7	Northeast Ontario	62,665	1.6%	2	(35,640)	-0.9%	5	-
8	Papineau-Pontiac	-	-	-	725	1.5%	3	-
9	Tunney's Pasture	124,484	1.7%	3	(86,186)	-1.2%	8	-
10	West Central	447,948	3.6%	5	(59,460)	-0.5%	6	-