



CELEBRATING
100
YEARS

PERSPECTIVE

▲
COMMERCIAL REAL ESTATE
CAP RATES ACROSS
CANADIAN MARKETS
▼

Q3
2017

**SUBTLE SHIFT IN
OUTLOOK FOR
TOMORROW'S MARKETS**

CAP RATE SURVEY REPORT »

EXECUTIVE SUMMARY

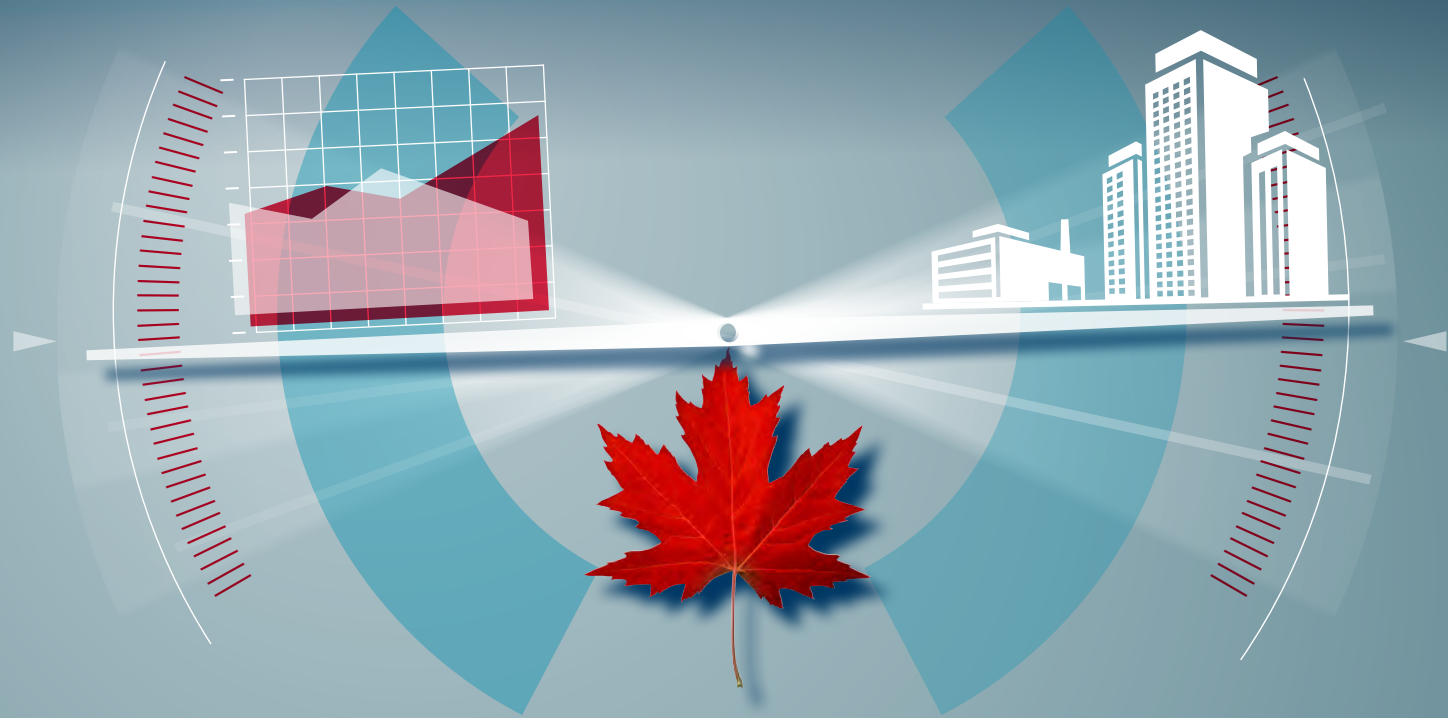
 *Yield stability is anticipated in leading gateway markets. Further cap rate compression is possible in higher-yielding asset classes & regions.* 

It is important to remember that the Bank of Canada implemented its first interest rate rise in seven years as recently as mid-July 2017. So it's no surprise that rising interest rates have done little more than scratch the surface of heated demand for Canadian commercial real estate.

That said, a key observation of the quarter is that the narrowing spread between cap rates and the 10-year government of Canada bond yield is putting a lens on markets and asset classes where returns are potentially higher. As a result, markets with greater yield potential could experience further modest cap rate compression, within this rising interest rate environment.

On the other hand, Vancouver and Toronto's hot CBD office and industrial asset classes are expected to see greater cap rate stability. In addition, strong market fundamentals will act as a counterweight, mitigating the impact of interest rate increases over the near term.

Demand for Canadian commercial real estate will remain robust through 2018. It's important to remember that while interest rates are rising, they remain near historic lows and fundamentals in gateway markets remain strong. That said, institutional buyers will be diligently scrutinizing returns from potential real estate acquisitions, and generally, we expect cap rates will stabilize.



“Canada’s real estate markets are at a point of inflection. Where we go from here depends on how quickly interest rates rise in 2018.”

Are Cap Rates Stabilizing in Top Canadian Markets?

Rising interest rates are acting as a counterweight against strong fundamentals in heated markets like Vancouver and Toronto, and cap rates across asset classes like CBD office and industrial are slowing their descent and heading towards greater stability.

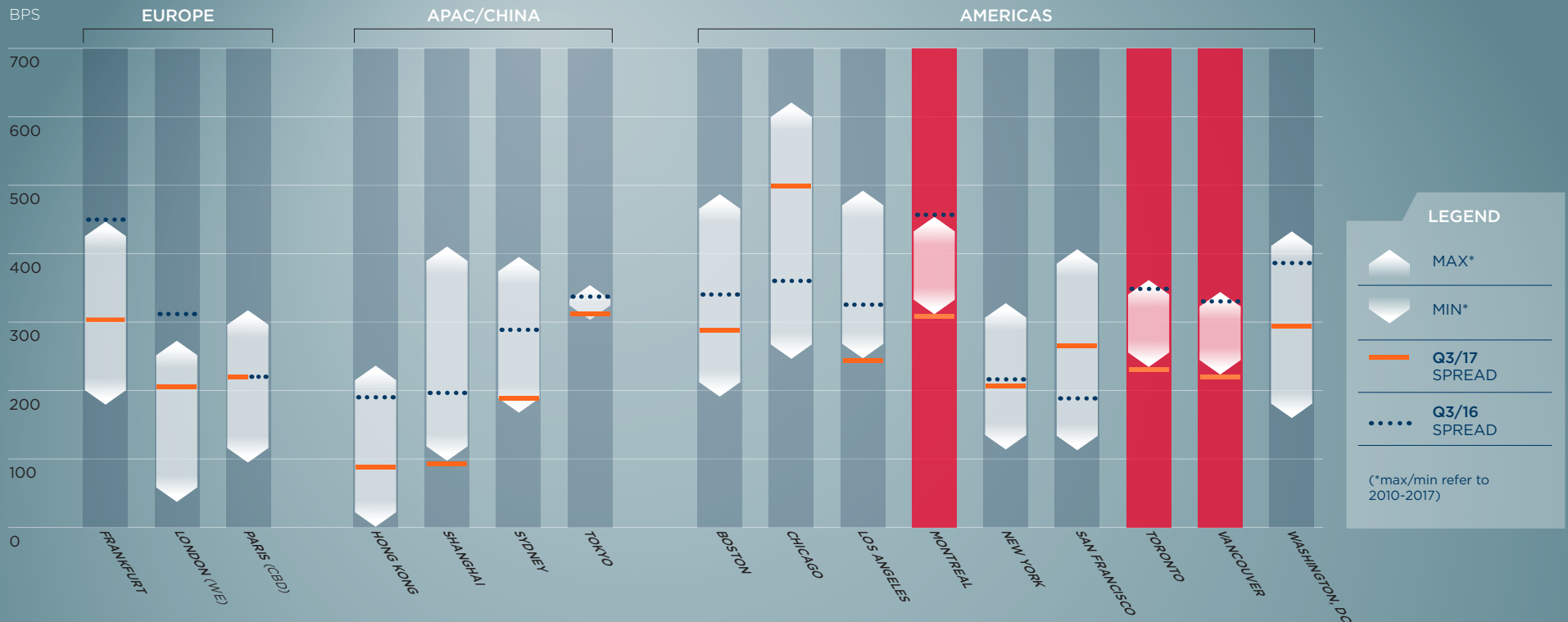
While the timing and impact of hikes are difficult to predict, there is no question that increases act as a tax on personal consumption, a key driver of the Canadian economy.

What the Experts Say

While opinions differ, the consensus view among economists is that the Canadian economy will slow over

the next few years. Oxford Economics is projecting that real GDP will soften to 1.9% in 2018 from an estimated 3.0% in 2017, with long-run interest rates rising from 1.81% in 2017 to 2.62% in 2018.

There are many conflicting views on where interest rates will go with forecasts clearly dependent on Bank of Canada policy. Any material slowdown in the economy would impact profitability and slow expansionary momentum across traditional drivers within office and industrial markets.



The Canadian Experience

If we look at prime office cap rate spreads to 10 year Government of Canada bond yields across CBD markets globally, Canadian markets are currently at the low end of the range. Further, we are at the cyclical low for cap rates in key gateway markets, which have continued to decline over the past year.

Vancouver and Toronto have seen the most downward compression since the financial crisis. Based on the outlook provided by our experts across Canadian markets, cap rates should see greater stability and less compression as we head into 2018.

The U.S. Experience

In the U.S., the Federal Reserve has bumped interest rates three times since late 2016, with a further increase expected this December. While the tension between rising interest rates and historically low cap rates has increased, a shift in transaction volumes towards higher-yielding assets and fewer trophy-asset trades appears to be driving the recent upward pressure on cap rates in key major metros.

Within Canada, hot markets like Vancouver and Toronto have not yet seen any upward shift in cap rates. In part, this is because of the strength in underlying fundamentals, including upward pressure on lease rates across industrial and CBD office markets.

What to Expect Moving Forward

- Some institutional investors will look to balance returns by selectively investing in secondary markets or higher yielding asset classes, for instance suburban office.
- Greater cap rate stability, with compression possible within asset classes and markets that have a stronger possibility of yield growth.
- Specific trophy assets may buck anticipated trends, hitting new cap rate lows.
- Fundamentals such as covenant, underlying lease term and anticipated rental rate pressure, will play a more critical role in investment decisions.
- Further increases in interest rates could push cap rates up modestly in 2018.

	VICTORIA			VANCOUVER			CALGARY			EDMONTON			WINNIPEG			LONDON		
	RANGE			RANGE			RANGE			RANGE			RANGE			RANGE		
DOWNTOWN OFFICE	LOW	HIGH	👁️	LOW	HIGH	👁️	LOW	HIGH	👁️	LOW	HIGH	👁️	LOW	HIGH	👁️	LOW	HIGH	👁️
AA	5.00%	5.50%	▼	3.75%	4.50%	◀▶	5.00%	5.75%	◀▶	5.75%	6.75%	▲	N/A	N/A	N/A	N/A	N/A	N/A
A	5.25%	5.75%	▼	4.00%	4.75%	◀▶	5.75%	6.50%	◀▶	6.75%	7.50%	▲	5.50%	6.25%	◀▶	6.50%	8.25%	◀▶
B	5.50%	6.00%	▼	4.25%	4.75%	◀▶	6.75%	7.75%	◀▶	7.75%	8.75%	◀▶	6.25%	6.75%	◀▶	8.00%	9.00%	◀▶
SUBURBAN OFFICE																		
A	5.50%	6.00%	▼	4.50%	5.25%	◀▶	6.25%	6.75%	▲	6.25%	6.75%	▲	6.25%	6.75%	◀▶	6.00%	8.00%	◀▶
B	5.75%	6.25%	▼	5.25%	5.75%	◀▶	6.75%	7.75%	◀▶	7.00%	7.75%	▲	6.75%	7.50%	◀▶	8.00%	8.75%	▼
INDUSTRIAL																		
A	5.25%	6.00%	◀▶	4.00%	4.50%	◀▶	5.25%	5.75%	◀▶	5.75%	6.50%	◀▶	6.50%	7.00%	◀▶	6.75%	8.00%	◀▶
B	5.75%	6.25%	◀▶	4.50%	5.00%	◀▶	5.75%	6.25%	◀▶	6.50%	7.50%	◀▶	7.00%	7.75%	◀▶	7.75%	8.75%	▼
APARTMENT																		
High Rise	3.50%	4.25%	▼	2.50%	3.00%	◀▶	5.00%	5.50%	◀▶	4.50%	5.00%	◀▶	4.75%	5.75%	◀▶	4.50%	5.75%	◀▶
Low Rise	3.50%	4.25%	▼	2.75%	3.50%	◀▶	5.00%	5.50%	◀▶	5.75%	6.25%	◀▶	5.00%	5.75%	◀▶	5.75%	6.50%	◀▶
HOTEL																		
Full-Service Downtown	6.00%	7.00%	◀▶	5.00%	6.25%	◀▶	7.00%	8.00%	◀▶	8.00%	9.00%	◀▶	8.00%	9.00%	▼	8.00%	8.50%	◀▶
Full-Service Suburban	7.00%	8.00%	◀▶	6.00%	7.50%	▼	8.25%	9.25%	◀▶	8.50%	9.50%	◀▶	9.00%	10.00%	◀▶	8.50%	9.50%	◀▶
Limited-Service Suburban	7.50%	8.50%	◀▶	7.00%	8.00%	◀▶	9.00%	10.00%	◀▶	9.00%	10.00%	◀▶	9.50%	10.50%	◀▶	9.00%	10.00%	◀▶
RETAIL																		
High Street	4.75%	5.25%	◀▶	3.25%	4.00%	◀▶	N/A	N/A	N/A	6.00%	6.50%	◀▶	N/A	N/A	N/A	6.00%	7.00%	◀▶
Regional Mall - Top Performer	5.00%	5.50%	◀▶	4.25%	4.75%	◀▶	5.00%	5.50%	◀▶	5.00%	5.75%	◀▶	5.50%	6.00%	◀▶	5.75%	6.00%	◀▶
Power Centre	5.00%	5.50%	◀▶	4.75%	5.25%	◀▶	5.50%	6.00%	◀▶	5.25%	6.00%	◀▶	5.75%	6.25%	◀▶	6.00%	6.50%	◀▶
Community Commercial Centre	5.25%	6.00%	◀▶	4.50%	5.25%	◀▶	5.00%	5.50%	◀▶	6.50%	7.25%	▲	5.75%	6.25%	◀▶	6.50%	8.00%	◀▶
Strip Plaza Anchored	5.00%	5.50%	◀▶	4.25%	5.00%	▲	5.25%	5.75%	◀▶	5.50%	6.25%	◀▶	5.75%	6.50%	◀▶	5.75%	6.50%	◀▶
Strip Plaza Non-Anchored	5.25%	6.00%	◀▶	4.50%	5.25%	▲	5.75%	6.25%	◀▶	6.50%	7.25%	▲	6.50%	7.00%	◀▶	5.75%	7.00%	◀▶

LEGEND » OUTLOOK: UP: ▲ DOWN: ▼ FLAT: ◀▶

BACK
◀◀

	KITCHENER/ WATERLOO			TORONTO			OTTAWA			MONTREAL			HALIFAX		
	RANGE			RANGE			RANGE			RANGE			RANGE		
	LOW	HIGH	👁️	LOW	HIGH	👁️	LOW	HIGH	👁️	LOW	HIGH	👁️	LOW	HIGH	👁️
DOWNTOWN OFFICE															
AA	N/A	N/A	N/A	4.00%	4.50%	◀▶	4.50%	5.25%	◀▶	4.50%	5.50%	◀▶	N/A	N/A	N/A
A	5.75%	6.25%	◀▶	3.875%	4.75%	◀▶	4.75%	5.50%	◀▶	5.25%	6.25%	◀▶	6.25%	6.75%	◀▶
B	6.25%	6.75%	◀▶	4.50%	5.25%	◀▶	6.00%	7.00%	◀▶	5.75%	6.75%	◀▶	7.00%	7.75%	▲
SUBURBAN OFFICE															
A	6.00%	6.75%	▼	5.75%	6.75%	◀▶	6.25%	6.75%	▼	6.00%	7.00%	◀▶	6.50%	7.50%	◀▶
B	6.75%	7.50%	▼	6.50%	7.50%	◀▶	7.00%	7.75%	▼	6.50%	7.50%	▲	7.50%	8.50%	▲
INDUSTRIAL															
A	6.00%	6.75%	◀▶	4.50%	5.00%	◀▶	5.75%	6.25%	◀▶	5.75%	6.75%	◀▶	6.25%	7.00%	▼
B	6.75%	7.25%	◀▶	5.50%	6.25%	◀▶	6.25%	7.25%	◀▶	6.50%	7.50%	◀▶	7.25%	7.75%	▼
APARTMENT															
High Rise	4.75%	5.50%	▼	3.50%	3.75%	▲	4.25%	4.75%	◀▶	4.25%	5.25%	◀▶	4.75%	5.25%	◀▶
Low Rise	5.00%	5.50%	◀▶	3.75%	4.50%	▲	4.50%	5.00%	◀▶	5.00%	6.00%	◀▶	5.50%	6.50%	▲
HOTEL															
Full-Service Downtown	8.00%	9.00%	◀▶	5.00%	6.50%	▼	7.00%	8.00%	◀▶	7.00%	8.00%	◀▶	7.50%	8.50%	◀▶
Full-Service Suburban	8.50%	9.50%	◀▶	6.50%	7.50%	▼	8.00%	9.00%	◀▶	8.00%	9.00%	◀▶	8.50%	9.50%	◀▶
Limited-Service Suburban	9.00%	10.00%	◀▶	7.25%	8.25%	◀▶	9.00%	10.00%	◀▶	9.00%	10.00%	◀▶	9.50%	10.50%	◀▶
RETAIL															
High Street	5.75%	6.75%	▼	3.50%	4.50%	◀▶	5.00%	6.00%	◀▶	4.50%	5.50%	◀▶	N/A	N/A	N/A
Regional Mall - Top Performer	6.00%	6.75%	◀▶	3.50%	4.50%	◀▶	5.00%	5.50%	◀▶	4.50%	5.50%	◀▶	5.25%	6.25%	◀▶
Power Centre	5.75%	6.50%	▼	5.00%	6.00%	◀▶	5.25%	5.75%	▼	5.00%	6.00%	◀▶	5.75%	6.75%	◀▶
Community Commercial Centre	6.00%	6.50%	◀▶	5.00%	6.00%	◀▶	5.75%	6.75%	◀▶	6.00%	7.00%	◀▶	6.75%	7.75%	◀▶
Strip Plaza Anchored	5.00%	6.00%	◀▶	4.75%	5.25%	◀▶	6.00%	6.50%	◀▶	5.50%	6.50%	▲	6.50%	7.50%	◀▶
Strip Plaza Non-Anchored	5.00%	6.25%	◀▶	4.75%	7.00%	◀▶	6.75%	7.75%	◀▶	6.50%	7.50%	◀▶	7.50%	8.50%	◀▶

CAPITALIZATION RATE

Cushman & Wakefield's Investor Council provides quarterly estimates of capitalization rates for the asset classes contained in this report based on our market expertise. The cap rate ranges are based on transaction data as well as demand and supply dynamics in the region. These estimates are meant to encompass the majority of assets within each class and may not represent outlier transactions or deals relating to assets with specific attributes that would significantly differentiate them.

DOWNTOWN OFFICE**CLASS AA**

A best-in-class office product, with more elaborate common areas, modern construction and building efficiencies, that commands the highest rents and tends to attract stronger covenant tenants, such as banks, government, insurance companies, etc. These buildings tend to be situated close to the core within their respective markets and have excellent access to major public transit hubs. Buildings are typically larger than 750,000 SF, with 5 to 10-year tenancies and some 15-year leases for inbound tenants. Occupancy levels assumed to stabilize at close to 95% of comparable market net rates.

CLASS A

A strong-performing asset, typically between 400,000 and 700,000 SF, which is well located, and may have smaller floor plate sizes, solid amenities and less elaborate common areas. The majority of the tenants have 5 to 10-year lease commitments. Occupancy levels assumed to stabilize at close to 95% of comparable market net rates.

CLASS B

Older office product, typically in the range of 100,000 to 250,000 SF. Buildings tend to be occupied with a diversified tenant mix but lack a large anchor tenant. Shorter lease commitments occur in this asset class with the average term ranging between 5 and 10 years. Average floor plate size can be significantly smaller. Generally not connected to the subway.

SUBURBAN OFFICE / INDUSTRIAL**CLASS A**

Newer high-quality suburban product, typically between 100,000 and 300,000 SF. Attracts good covenant tenants for 5 to 10-year lease terms.

CLASS B

Older suburban product that attracts a wider range of tenants and covenants for lease terms ranging between 3 and 10 years.

APARTMENT**HIGH RISE**

An apartment building greater than 4 storeys in height or having more than 80 units.

LOW RISE

Any apartment complex having fewer than 80 units.

HOTEL**FULL-SERVICE**

A hotel with extensive dining and meeting facilities. Quality ranges from upscale to luxury. Examples include Hilton, Westin, Hyatt, etc.

LIMITED-SERVICE

A room-focused hotel with minimal facilities. Quality ranges from economy to mid-scale. Examples include Comfort Inn and Super 8.

RETAIL**HIGH STREET**

Typically considered the street or section thereof where the greatest dollar value psf is generated from streetfront retail stores within each market.

REGIONAL MALL - Top Performer

Top-performing fully enclosed mall. These buildings tend to be greater than 800,000 SF and have a wide product offering, featuring destination retailers and 2 to 3 anchor tenants. Often located near large transit hubs and serve a trade area between 10 and 30 kilometres.

POWER CENTRE

Large format, category dominant retailers in an open-air configuration that may include "club" or discount department stores. Total GLA is typically between 100,000 and 1,000,000 SF.

COMMUNITY COMMERCIAL CENTRE

An enclosed centre anchored by a smaller department store, servicing a local community. Tenants may include general merchandise and convenience offerings, including a grocery store. Total GLA is typically between 100,000 and 400,000 SF.

STRIP PLAZA - Anchored

An open-air configuration of attached retail stores that may include retail PAD sites. They are often anchored by a food or drug store tenant. Tenants are generally servicing residents in the neighbourhood. These would include dry cleaners, take-out food stores, convenience stores, etc.

STRIP PLAZA - Non-Anchored

An open-air configuration of attached retail stores, not anchored by a grocer or drug store, that may include retail PAD sites. Tenants are generally servicing local neighbourhood residents.

IDEAS INTO ACTION



161 Bay Street, Suite 1500
Toronto ON M5J 2S1

cushmanwakefield.com

CONTACTS

CANADA EAST

Stefan H. Teague, SIOR, LEED GA
Executive Managing Director
Market Leader, Greater Toronto Area
Direct: +1 416 359 2379
stefan.teague@cushwake.com

CANADA WEST

Hendrik Zessel
Executive Managing Director and
Western Canada Leader
Direct: +1 604 640 5803
hendrik.zessel@cushwake.com

Stuart Barron, CPA, CA
National Director of Research,
Canadian Markets
Direct: +1 416 359 2652
stuart.barron@cushwake.com

VICTORIA > Anne Tanner Personal Real Estate Corporation / Tim Sommer Personal Real Estate Corporation
METRO VANCOUVER > Bill Randall Personal Real Estate Corporation / Bob Watt / Boe Iravani Personal Real Estate Corporation / Brad Newman-Bennett / Brett Aura Personal Real Estate Corporation / Burton Van Alstine Personal Real Estate Corporation / Chris Driver Personal Real Estate Corporation / Chris Newton / Craig Haziza, CAH Realty Inc.† / Craig W. Ballantyne Personal Real Estate Corporation / Don Duncan Personal Real Estate Corporation / Edgar Buksevics Personal Real Estate Corporation / Harpreet Singh Personal Real Estate Corporation / Hudge Parmar Personal Real Estate Corporation / Jordan Sengara Personal Real Estate Corporation / Justin De Genova / Kevin Meikle, KHM Realty Ltd.† / Lee Blanchard / Mark Gallagher Personal Real Estate Corporation / Matthew MacLean Personal Real Estate Corporation / Peter Gibson Personal Real Estate Corporation / Phil Joubert Personal Real Estate Corporation / Ron Emerson / Scott MacPherson / **CALGARY** > Marc Rosso / Scott Stoddart / Tom Charlton / **EDMONTON** > Abdul Khurshed / Adam Martinson / Adel Hanafi / Adrian Ambrozuk / Afsar Khurshed / Chris Kamphius / David Cooney / Doug Bauer / Doug Rae / Howard McCann / Ian Newman / Jeff McCammon / Kyle Barton / Lance Frazier / Raphael Yau / Seif Jiwaji / **SASKATOON** > Lloyd Hedemann / **REGINA** > Miike Alport / Mike Hogan / Peyton Hogan / **WINNIPEG** > Chris Macsymic / Jonah Levine / Ken Yee / Martin McGarry / **LONDON** > Brent Rudell **/ David Jongerden */ Gary Pollack **/ Tyler Desjardine */ **WATERLOO** > Benjamin Bach */ Bob Vrenjak */ David Anderson **/ Jeff Fry */ Jordan Palmer */ Michael Klein **/ Michael Polzl **/ Nick Holzinger */ Scott Anderson **/ Stewart Campbell */ **GREATER TORONTO** > Alex Holiff */ Ali Asgary */ BJ Bhal */ Brad Warren **/ Brent Jorgens */ Craig Smith **/ Curtis Gallagher */ Dan Rogers **/ Dean Morrison **/ Don Rogers */ Earle Ruggles **/ Goran Brelih */ James Wu */ Jeff Thomas **/ Liam Sauro */ Luis Almeida */ Mark Cascagnette */ Michael Betel */ Mickey Swartz */ Moshe Elyovich **/ Nicholas Kendrew **/ Noah Rechtsman */ Paul Campbell */ Peter Mason **/ Phil Traikos */ Sam Buckley */ Tom McCarthy **/ Trevor Henke */ Vince Callaghan **/ **KINGSTON** > Martin Skolnick **/ Peter Kostogiannis ***/ Scott Botting */ Stacey-Ann MacDonald **/ **OTTAWA** > Nathan Smith ***/ Scott Brooker */ **MONTREAL** > Bernard Grant / Daniel Belanger / Erik Langburt / Jean Bussieres / Jean-Sebastien Vincent / Jenny-Kate Sgarbi / Lloyd Cooper / Marie-Josée Gareau / Ron Smith / **EASTERN CANADA** > Bill MacAvoy / Ian Franklin (Moncton) / James Boudreau (Halifax) / Susan Morrison (St. John's)

* Sales Representative ** Broker *** Broker of Record

† Craig Haziza is licensed with CAH Realty Inc. and has a contractual relationship with Cushman & Wakefield Ltd.

† Kevin Meikle is licensed with K.H.M. Realty Ltd. and has a contractual relationship with Cushman & Wakefield ULC, Brokerage

This report is provided for information purposes only. The information and statistical data contained herein were obtained from sources deemed reliable. We do not however, assume responsibility for inaccuracies. All opinions expressed and data provided herein are subject to change without notice. This report cannot be reproduced in part or in full in any format including electronic or printed media, without the prior written approval from Cushman & Wakefield ULC, Brokerage.