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Cushman & Wakefield: First Half of 2012 Office Markets Expected to Taper off across the Country as Development Deals Take a Wait & See Approach

Activity Expected to Gain Momentum in the Latter Half of the Year

TORONTO--(BUSINESS WIRE)--A general slowing of demand for office space across the country is expected over mid-2012, according to the 2012 Office Outlook, released by Cushman & Wakefield (C&W) today. However, both suburban and central office demand is anticipated to regain momentum in the latter half of 2012.

"As the number of deals in progress slows, driven by uncertain global economic news and the related fall in business and consumer confidence, the capacity to meet demand for new space in most major markets will create a serious shortage of central inventory in the second half of 2012 and beyond," says Pierre Bergevin, President and CEO, C&W Canada. "Moreover, the resulting effect of shrinking inventory will see some central markets across the country continuing to show declining vacancy rates which undoubtedly will result in an increase in Net Effective Rents."

"The shipbuilding announcement is a game changer, both tangibly and intangibly"

By the end of 2012, Calgary should be the tightest market in the country, with Class A vacancy scraping the bottom of the barrel at 1.2%. Vancouver will be close behind with a new low of about 1.9%. While central Toronto will see some softening due to inventory returning to market as scheduled development projects are completed. Montreal has impressed all observers as its Class A vacancy has dropped significantly. One factor that will contribute to stronger near-term demand is lower interest rates.

Vancouver

Influenced heavily by resource and commodity markets, the recent strengthening demand in Vancouver's suburban office market is expected to continue well into 2012. This trend in demand should remain positive – if modest – through 2012, gaining momentum in 2013.

In Vancouver's central market, infrastructure investment and a sustained residential housing market boom have supported a stable economy with greater resilience than most other Canadian markets. With no new office developments in 2011, the vacancy rate has remained low, at only 3.7% in the third quarter of this year. New developments that were announced this year – Telus Garden, a 465,000 sq. ft., 22-storey office tower, Bentall's 365,000 sq. ft. office development on Thurlow, and Oxford's new development, University Club, at 265,000 sq. ft..

"These new developments will bring some much needed new office space to downtown Vancouver," says Hendrik Zessel, Senior Managing Director, C&W Vancouver. "The result will be some upward movement in vacancy, but we expect to continue to see modest absorption in 2012, with demand picking up by 2013 and beyond."

Calgary

With central Class A vacancy at an astonishingly low 4.0%, the market in downtown Calgary is now characterized by an extreme shortage of large blocks of space – which is not expected to change in the foreseeable future. The Bow, set to bring 1.9 million sq. ft. of space to the market in the second quarter of 2012 is not only already 100% leased, but the space that will be displaced by the two companies moving there, Encana and Cenovus, is also substantially leased.

“High oil prices, combined with strong continued capital investment in heavy oil projects in northern Alberta have been the primary drivers behind the strong demand,” says Bob MacDougall, Senior Managing Director, C&W Calgary. “Much of the demand has come from junior oil and gas companies trying to lock down future space to accommodate expected growth.”

In 2012, central demand will continue to be robust and vacancy will continue to tighten. Demand will likely shift to suburban markets as opportunities in downtown Calgary run out.

Edmonton

Overall vacancy is expected to increase in 2012 as a result of the market dynamics caused by recently completed Epcor Tower in the downtown core. At 625,000 sq. ft., 185,000 sq. ft. of that space remained vacant in the third quarter of this year. On top of that, 300,000 sq. ft. of space was returned to the market due to the relocation of Epcor and the Federal Department of Justice into this new tower from several other downtown properties.

Regardless, confidence in Edmonton’s economy is strong, despite continuing global economic uncertainty. The average gross rental rates were $33.88 per sq. ft. in the central market, and $28.63 per sq. ft. in the suburbs, representing a slight increase in the downtown, and a slight decrease in the suburban market.

“We have been seeing growing confidence in the central market as vacancy is absorbed,” says Shane Asbell, head of the office leasing team, C&W Edmonton. Leasing activity should remain brisk as tenants look to take advantage of attractive rental rates and generous inducement packages offered by landlords.”

Toronto

Unlike other major Canadian markets, Toronto’s downtown market demand is expected to remain buoyant due to Tenants moving into new space resulting in more Class AAA inventory (approximately 1 million sq. ft.) coming back to the market. Additional factors such as the revitalization of Union Station, the massive Waterfront project, and thousands of new condominiums that have given rise to densely populated urban communities will ensure that Toronto’s central market will remain an attractive business location in 2012 and beyond. New LEED developments saw extremely strong demand in 2011 as tenants sought both quality and location, along with the opportunity to implement workplace strategies that would attract and retain the young educated workforce that live and work in growing numbers downtown.

This year, a revival in demand materialized across suburban markets, particularly in the third quarter when the GTA saw about 550,000 sq. ft. of positive absorption across east, west and north suburban markets. Demand within these areas is expected to remain positive through the first half of 2012, though it may weaken through the latter half of 2012 in part due to global economic pressures, before picking up again in 2013 and 2014.

“As we look to 2012, we expect demand growth in Downtown Toronto to level off but remain healthy overall,” says Paul Morse, Senior Managing Director, Office Leasing. “This is a dynamic market with a bright future that will see new buildings coming on stream coupled with space being returned to market, easing low vacancy and meeting future tenant demands.”

“Our suburban markets as well appear to be recovering, although we expect some slowing in demand through 2012, with recovery moving into the picture by 2013. Meanwhile, low new supply in the GTA’s downtown and suburban markets has set the stage for faster recovery,” adds Morse.

Ottawa

In 2011, central Ottawa saw the addition of the 475,000 sq. ft. EDC building, which Export Development Canada has since relocated to. With that move, 400,000 sq. ft. of space is expected to come to market, softening central area vacancy rates in 2012. However, while central area vacancy may rise in the short run, demand is expected to remain at modest levels.

Thanks to the dominating presence of federal government, Ottawa’s office market tends to be the most stable in the country, and is far less likely to be impacted by broader issues such as global economic turmoil in 2012 and beyond.

In recent months, the federal government has become more active, leasing a total of about 100,000 sq. ft. during the second quarter of 2011. Though the government has indicated that future demand will be restricted, it will require a significant amount of space to allow for necessary upgrades of existing space over the next few years.

“While central area vacancy may rise in the short run, demand is expected to remain modest in the core,” says Alain Desmarais, Senior Managing Director, C&W Ottawa. “We expect rental rates to soften slightly over the next few quarters, and return to stability with the government continuing to lease space to address its aging buildings.”

Montreal

With the softening global economy and modest GDP growth expectations in the US economy, demand for office space in the Montreal markets will be modest, but is expected to remain positive in 2012 and 2013, and will gain additional momentum in 2014. With contiguous space in the central market of 50,000 sq. ft. and larger being almost non-existent, vacancy rates will continue to decline in 2012.

With little in the way of contiguous space, it is no surprise that new developments are on the horizon for Montreal. Announced this year, Kevric Real Estate Corporation will be building a $100-million condominium and office complex, which includes a 10-storey, 230,000 sq. ft., LEED-certified office building – in the heart of the international district.

“Lack of contiguous space will be a major concern to the user market in 2012,” says Louis Burgos, Senior Managing Director, C&W Montreal. “The market in Montreal has very quickly gone from a tenants’ market, to a landlord’s market, and we expect the Kevric project will see great interest in their space by businesses looking for offices in the 50,000+ sq. ft. range.”

Montreal’s business health in the next few years will be influenced by key industry drivers, which include aerospace, electronics, pharmaceuticals, software engineering, and telecommunications.

Winnipeg

With the recent completion of the $585-million airport terminal at James Armstrong Richardson International Airport and the $310-million Canadian Museum for Human Rights scheduled to open in 2013, along with the return of the Winnipeg Jets hockey team, confidence in Winnipeg’s future and economy is high. Looking ahead to 2012, office vacancy in Winnipeg is expected to increase slightly, with the exception of the Class A market, which will see tightening conditions over the next several quarters.

Winnipeg’s office market is experiencing growth as projects of various sizes are either already under construction or in the development stages. Next month, Centrepoint at 311 Portage Avenue will break ground as site work will start on this 200,000 square foot office/hotel development. Stantec Inc. will occupy approximately 55,000 square feet in this project which will also include a 154 suite Alt Hotel and 450 stall parkade. Additionally, there are also three major office building renovations in progress on Broadway Avenue (363 Broadway, 287 Broadway and 333 Broadway) with more planned for the Central Business District.

“The outlook for the office market is very optimistic,” says Ken Yee, Senior Executive Vice President, C&W Winnipeg. “New Class A construction, several Class B renovations and the return of the NHL is essentially icing on the cake. A decade of concentrated revitalization and over $1Billion in new projects and renovations has created an exciting vibe and a renewed confidence for downtown Winnipeg. We expect near term market fundamentals to be strong as upward trending lease rates begin to stir the market. ”

In Q3 2011, the class B CBD overall vacancy rate decreased by 0.2 percentage points, from 10.3% to 10.1%. We expect the vacancy rate in 2012 to remain steady to slightly lower in the 9.5% to 9.75% range. As tenants begin to migrate into newer buildings in late 2012/2013 we expect the vacancy rate to trend downwards to the 8% to 9% range, although it will fluctuate as the resulting vacant premises is absorbed by the market place.

The demand for office space is healthy as we are seeing office expansion in both the private and public sector. Increased tenant demand is expected from both the provincial and federal governments over the next 12 months.

London

For 2012, office demand in London is expected to remain slow, but there may be a noticeable increase in the cost of large floor-plate transactions (new and renewal), given tightening availabilities in the core area. The Class A market will continue to show small gains, but should local leaders elect to re-locate municipal employees out of leasehold premises and into proposed new City Hall, London may see further erosion of the Class B market.

"Light absorption and little demand will likely keep London a tenant's market through 2012," says George Kerhoulas, Agent, C&W London Ontario. "However, it will be less favourable than in recent years – tenants requiring more than 20,000 sq. ft. are finding fewer options and landlords are increasingly less willing to negotiate."

Further, no significant office construction has occurred since One London Place in 1991 and the Galleria retrofit in 2000, and none is expected, keeping office inventory flat.

Atlantic Canada: Halifax, Moncton, Fredericton, Saint John

Office demand in Halifax should increase in each quarter in 2012. This is largely due to confidence bolstered from the ship building contract won by Irving Shipbuilding, which is a $25-billion contract to build combat ships for the Canadian Navy over the next 20 years. Absorption could easily ramp up to 20,000 sq. ft. per quarter by 2013.

Though Halifax is not immune to the impact of the European financial crisis or a potential softening in US demand for Canadian goods and services, the shipbuilding contract is of such significance in size and scope that it will certainly protect the city and area from external economic shocks in future and will inevitably act as an incredible catalyst for office market growth.

In Moncton, diversified business, and entrepreneurial flair of the people and businesses within the region are all key drivers in demand for office space. Some of the recent absorption has been related to Atlantic Lottery's outsourcing of some business services to CGI. As of yet, Atlantic Lottery has not returned any of its own space to market. Growing demand for goods and services, which ultimately supports the growth of companies using office space, continues to be fueled by a growing population. The Moncton CMA, including the neighboring city of Dieppe and the town of Riverview as well as Westmorland and Albert Counties, has the fastest growth rate of any urban region east of Toronto.

In Fredericton, the office market gained ground in 2011 and the pace is expected to remain relatively brisk through 2013. The addition of new Knowledge Park builds and the Conference Centre will create options for tenants, and suppress rents in existing buildings and/or create a class dichotomy in rents, accompanied by a flight to quality. This could decrease occupancy in older buildings.

The Greater Saint John area is a natural geographic gateway and strategic distribution hub, and while little change is expected in the coming year, Saint John's port positions it for large marine or energy related projects. Saint John's office occupancy declined slowly through 2011. By the third quarter, the city's office market was 12.1% vacant, and had given back 20,000 square feet. At 2.2 million square feet, the market has a low average rent of $11.83 per square foot. Given Saint John's historic connection to Irving, its port and location, the city also stands in line to benefit from engineering job growth and other economic spinoffs connected with the $25-billion dollar ship building contract recently won by Irving Shipbuilding in Halifax.

"The shipbuilding announcement is a game changer, both tangibly and intangibly," says Bill MacAvoy, Managing Director, C&W Atlantic. "While timing of visible impacts is not yet fully clear, this certainly removes downside risk in housing, retail, industrial, and office for a generation. Depending on the general economy, nationally, and regionally, the Atlantic region could post nation leading growth rates at certain times over the next 20 years"

St. John's

Newfoundland and Labrador is set to lead the Atlantic Provinces in growth in the coming year thanks to increasing levels of investment in natural resources and related boosts in income that the Royal Bank of Canada, for one, predicts will result in many years of solid economic performance. While natural swings in offshore oil production would typically result in uneven GDP growth, with the Hibernia South Extension and the Hebron project in full swing, long-term economic stability is assured.

In this active economy, few were surprised at the announcement that downtown St. John's will see its first office development in over 25 years. Being developed by East Port Properties Ltd., "351" is the first seawater heated and cooled building in Newfoundland and Labrador. A Canada Green Building Council LEED ® registered building; it has been designed to achieve Gold level certification. To be completed in 2013, the six storey, 165,000-square-foot office tower includes prime retail space and a 446-car parkade. It is likely that the new downtown development will see strong interest. Many companies have been located in the same buildings for years, and there is a growing desire to realize the efficiency advantages offered by modern space and efficient new office buildings.

The suburban market will see the completion of a 46,000-square foot building in the fourth quarter of 2012. Given its strong economy, St. John's will remain well insulated from global economic turmoil and office demand is expected to remain relatively strong.

"Continued demand resulting from mega project investment and development has driven rapid rent increases," says Susan Morrison, General Manager, C&W Atlantic, Newfoundland. "This is finally resulting in sorely needed modern additions to office inventory supply."

To obtain a full copy of the report visit www.cushwake.com or to arrange to speak with a Cushman & Wakefield expert, please contact Adam Weitner, Mansfield Communications at 416.844.0191/416-599-0024 ext. 238 or adam@mcipr.com

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Attached is the full report