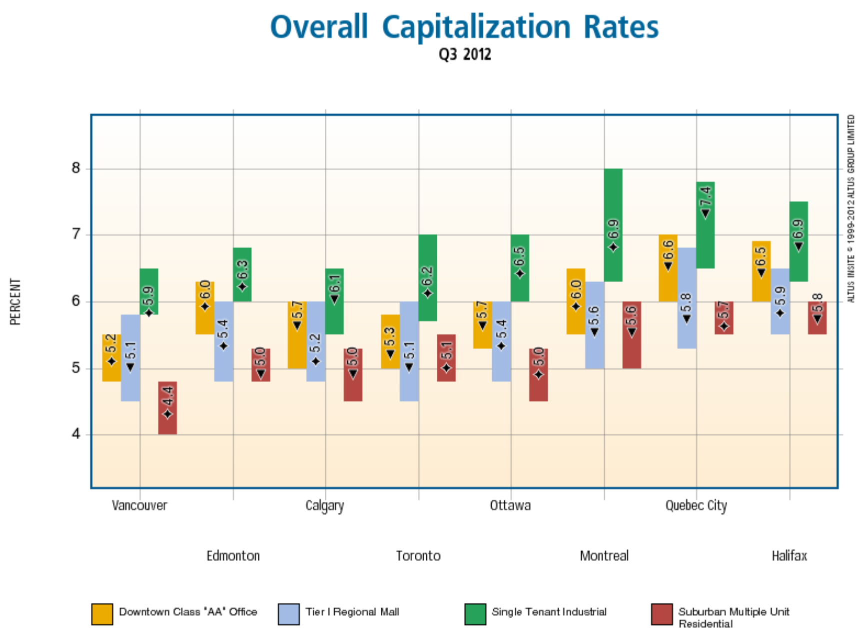
More Cap Rate Compression… 10 basis points at a time

Altus InSite Q3 2012 Investment Trends Survey Summary Outlook

Commercial Real Estate continues to be a destination for global capital seeking yield. This ongoing pressure to place capital is resulting in continued compression on cap rates. In spite of global economic uncertainty and tepid GDP growth, Canadian investors maintain a positive outlook towards the commercial real estate market, according to the latest quarterly results of the Altus InSite Investment Trends Survey. For most of the asset classes included in the survey, a quarter of all respondents anticipate more increases in values in the next 12 months while 70% foresee stability. This relatively bullish attitude is reflected in the continued, yet steadily modest, cap rate compressions recorded in 2012 for most asset classes.

After breaking pre-recession record-low levels in the first part of 2011, average cap rates have been steadily compressing by a few basis points every quarter, fuelled by investors' appetite for income-generating properties. Every time we seem close to reaching a peak in values, market conditions improve and investors are ready to go down a few more points. Out of the 32 asset classes/cities surveyed every quarter, 23 have registered cap rate compression ranging between 10 and 30 bps since Q2 2012, while cap rates in 8 categories stood still, indicating these products might have reached a plateau. This is the case for Suburban Multiple Unit Residential properties in Vancouver (4.4%), Toronto (5.1%) and Ottawa (5.0%).

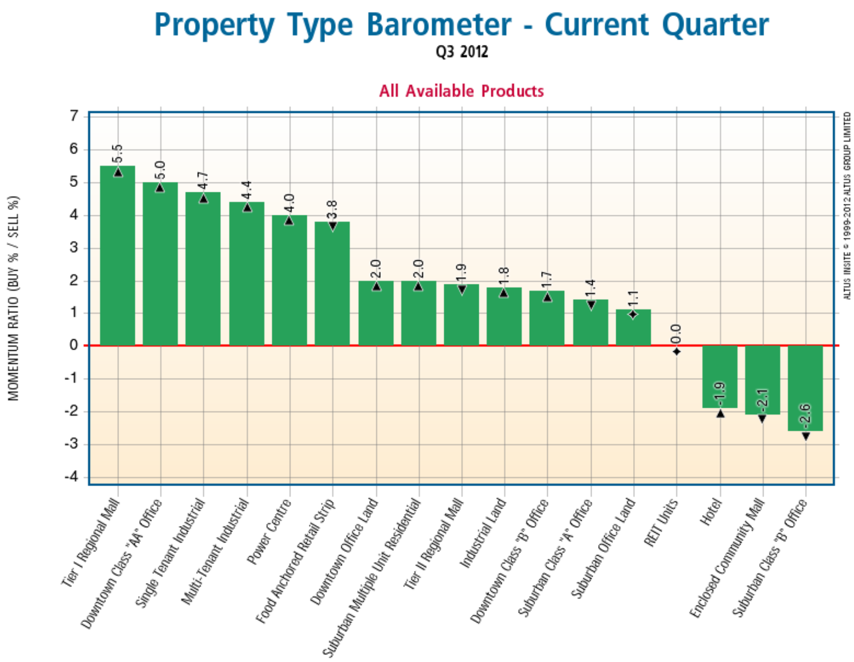


Single Tenant Industrial shows a more unpredictable pattern with cap rates decreasing in Quebec City (30 bps), Halifax (20 bps) and Calgary (10 bps), going up in Ottawa (+10 bps) and not moving in Vancouver, Edmonton, Toronto and Montreal. Cap Rates for Tier 1 Regional Mall have compressed by 10 to 20 bps in all eight major markets, with slight regional differences ranging from a low of 5.1% in Toronto and Vancouver to a high of 5.9% in Halifax. Halifax and Quebec City's expected yields for Tier 1 Regional Mall have moved below the 6.0% mark for the first time ever this quarter. We have also notice coast to coast compression ranging between 10 to 20 bps for all downtown class AA office markets, except for Calgary, which stayed the same.

Downtown Class AA Office markets in Vancouver (5.2%) and Toronto (5.3%) continue to boast the most aggressive yields. Moving East to Quebec City and Halifax will provide investors with a full 120-140 extra bps.

Downtown class AA Office is making a big return in terms of investors' preference this quarter, jumping from 6th place to 2nd position. Most respondents' motivation for Office investments are Cash flow Upside/growth (74%), Capital Appreciation (50%) as well as Availability and Low Cost of Debt/Equity (50%)

Tier 1 Regional Mall retains the top position while Single Tenant industrial has climbed from 4th to 3rd position since last quarter. Only 3 asset types are in negative territory, which mean more respondents would consider disposing of this asset type than acquiring it, namely: Hotels, Enclosed Community Malls and Suburban Class B Office. Since the very first Altus InSite surveys, started in 2000, these assets have consistently been among the least preferred investment choices on the Product Type Barometer.



Fuelled by availability of capital and historically low interest rates and flexible mortgage terms, commercial real estate investment activity remains strong this year as we see the biggest players reaping trophy assets at historically low cap rates or swallowing rivals with hundreds of millions of dollars. As the amount of capital entering the real estate market continues to grow and outpace the sums exiting the market, we can expect more modest cap rate compressions. But this quarter's Investment Trends Survey results seem to indicate we are getting close to reaching a plateau in certain market segments.

Every quarter, senior Altus Group professionals reach out to over 300 investors, managers, owners, lenders, analysts and other market stakeholders to survey their opinion on value trends and perspectives. Conducted with the same benchmark properties for over 10 years, the survey provides valuable insights on valuation parameters for 32 asset classes in Canada's 8 largest markets. For more detailed survey results, please contact support@altusinsite.com.