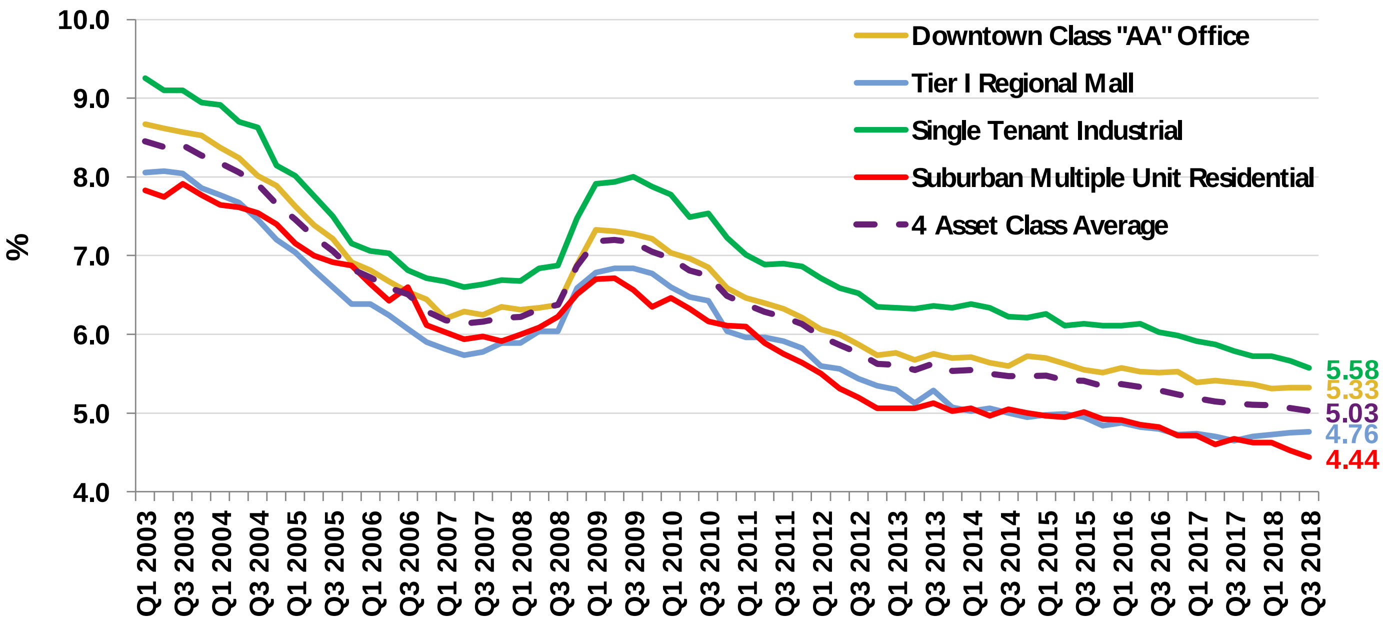
Demand for product continues to outpace supply, yet investors remain cautious…

The latest results from Altus Group's Investment Trends Survey (ITS) for the 4 Benchmark asset classes show that appetite for investment remains attractive amid rising prices due to product shortage, particularly for private investors and opportunity funds. The overall Capitalization Rate (OCR) compressed slightly to 5.03% in **Q3 2018**, compared to 5.07% for Q2 2018 and 5.13% for Q3 2017.

OCR Trends – 4 Benchmark Asset Classes



Source: Altus Group

Market highlights for the quarter include:

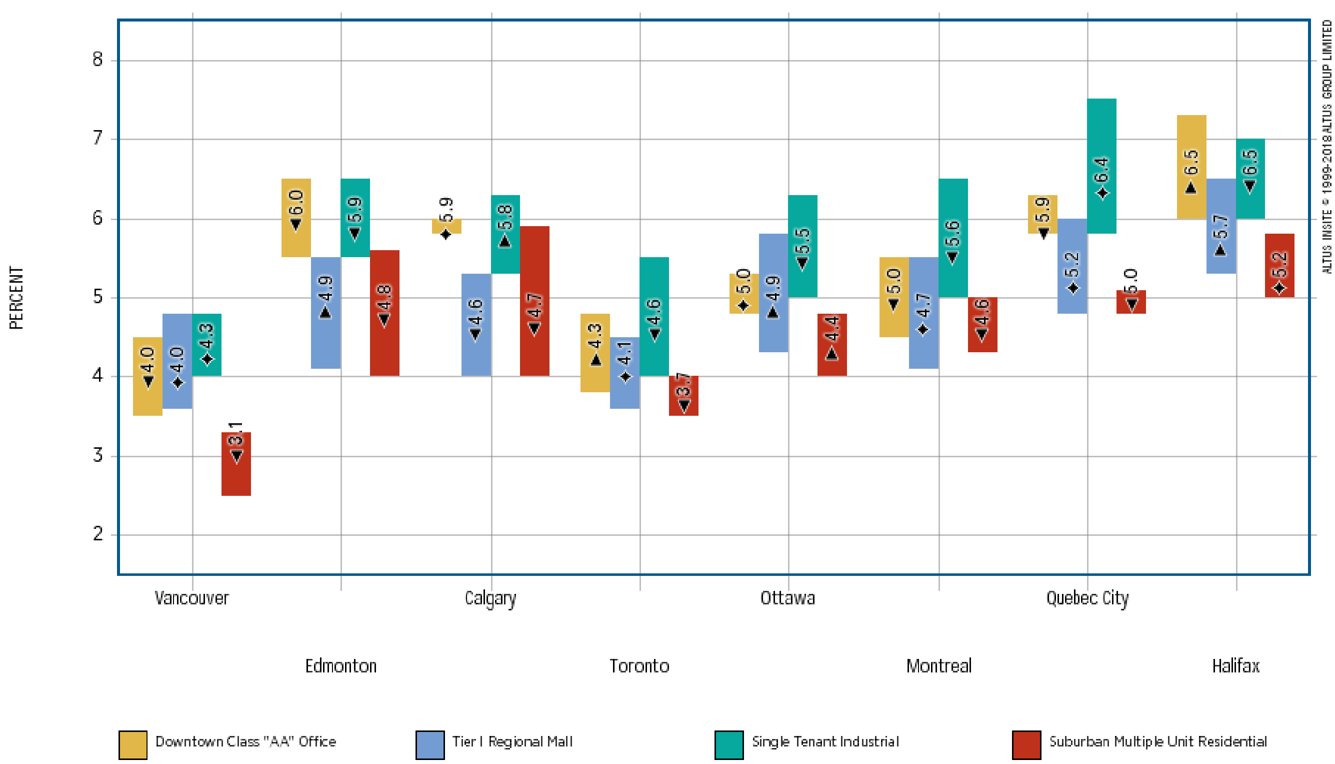
- **Overall cap rates are down across most markets with the exception of Ottawa,** which had a slight uptick in cap rates, and **Halifax, where rates were stable**. Large institutional investors continue to rebalance their portfolios to protect cash flow, focusing on investment growth while limiting risks.
- **Downtown Class "AA" office cap rates for Toronto and Halifax have moderately gone up, while Calgary and Ottawa remain flat, and the remaining markets marginally decreased.** As high-quality office product grows more scarce and prices continue to rise in core markets, some investors are looking for higher yields in other attractive markets.
- **Toronto, Montreal and Quebec City cap rates for Tier I Regional Malls remain stable, Edmonton, Ottawa and Halifax rates have gently climbed, while Vancouver and Calgary rates have declined**

slightly this quarter. Although the retail sector has experienced some instability due to the disruption caused by e-commerce, retail property owners will continue to focus on transit-oriented development and adopt the mixed-use concept embracing the "live-work-play-eat-shop" paradigm shift.

- **The industrial suburban markets are beginning to see a revival due to limited availability in urban markets.** Interest in industrial product looks promising with **a decline in industrial cap rates across most major markets, with the exception of Calgary which saw a slight increase.**
- The overall outlook for suburban multi-unit residential remains modest. **Suburban multi-unit residential cap rates have compressed across all markets, except for Ottawa, showing a moderate lift, and Halifax, which remains flat**. Volatility in the housing market continues to linger with the rise in mortgage rates causing buyers to put off their purchases as the housing affordability crisis prevails. Thus, investors are looking towards secondary and tertiary markets for multi-family residential products as these cities continue to move forward with their plans for densification and provision of projects geared towards mixed-use and transit-oriented development.

Overall Capitalization Rates

Q3 2018



Arrows indicate directional movement from previous survey

Movement is defined as a change of more than 0.10 and due to rounding some arrows may not reflect actual movement.

Other highlights for Q3 2018 include:

- Although rising interest rates may play a factor in market cap rate increases, **commercial real estate in Canada has not yet been fully impacted and is expected to hold steady** with modest increases despite another suspected hike in interest rates. **Investment activity remains healthy** and demand for product continues to be strong, particularly for industrial product, though investors continue to remain cautious. Of the 128 combinations of products and markets covered,
  - 70 had a "positive" momentum ratio (i.e. a higher percentage of respondents said they were more likely to be a buyer than a seller in that particular segment) compared to 83 in Q2;
  - 50 had a "negative" momentum ratio compared to 42 in Q2; and
  - 8 were neutral.

  The 3 products/markets which showed the most positive momentum were: Ottawa multi-tenant industrial, which remained unchanged from Q2 2018, followed by Edmonton multi-tenant industrial, and Calgary multi-tenant industrial.
- As the drawn-out **NAFTA (USMCA) negotiations** have come to a close, government officials anticipate the trade agreement will alleviate a certain amount of uncertainty, especially in the manufacturing sector, and will reinforce moderate economic growth.
- ITS participants anticipate that **cap rates will likely remain flat**, while multi-unit residential and industrial benchmark properties will continue to see modest cap rate compression.
- **Rents for industrial space continue to rise across Canada** as demand surges ahead of supply. With the intensification of e-commerce and the upcoming legalization of cannabis spurring demand for larger production and cultivation space, developers are being forced to look towards outer regions and rapidly move ahead with construction of new supply.
- **The Western markets continue to recover from the energy downturn as investments improve, exports strengthen, and employment and population growth accelerate.** However, markets will continue to be faced with challenges and difficulties amid rising energy prices and a lower Canadian dollar driving up consumer prices, lack of investment product, growing labour shortages, and slower wage increases.
- All the while, **it is expected that the Bank of Canada will gradually tighten interest rates by the end of 2018** in order to ease future inflation. According to RealNet Investment Transactions results, national investment activity volume is $15.2B for Q2 2018, up from the previous quarter, suggesting investor sentiment has improved, albeit towards a lower risk tolerance approach.

Every quarter, senior Altus Group professionals reach out to over 200 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 more than 15 years, the survey provides valuable insights on investor preferences and valuation parameters for 32 asset classes in Canada's 8 largest markets. For more detailed survey results, please contact datasolutionsinfo@altusgroup.com.