2021 CANADIAN ECONOMIC OUTLOOK AND MARKET FUNDAMENTALS THIRD QUARTER UPDATE

23RD ANNUAL EDITION

MORGUARD

Q3

Morguard

2021 CANADIAN ECONOMIC OUTLOOK AND MARKET FUNDAMENTALS THIRD QUARTER UPDATE

23RD ANNUAL EDITION

MORGUARD

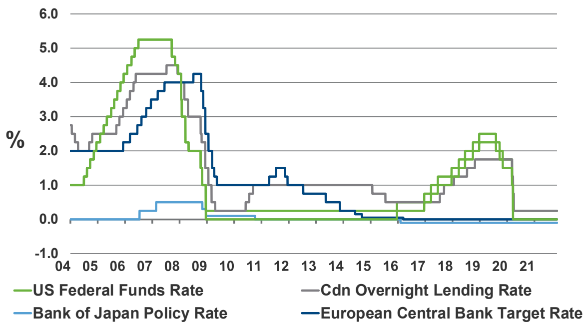
Q3

Any request for reproduction of this research report should be directed to:

Keith Reading
Director of Research
905-281-5345
kreading@morguard.com

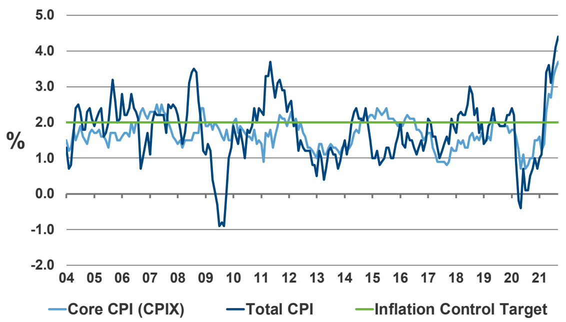
TABLE OF CONTENTS

Official Policy Rates
International Monetary Conditions



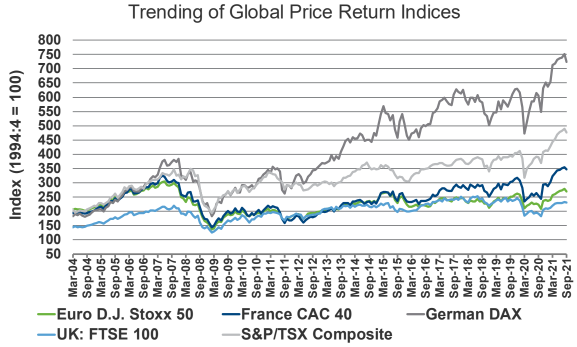
Source: Bank Of Canada, Federal Reserve Board, European Central Bank, Bank of Japan

National Inflation
CPI Measures, % Change Over 1 Year Ago



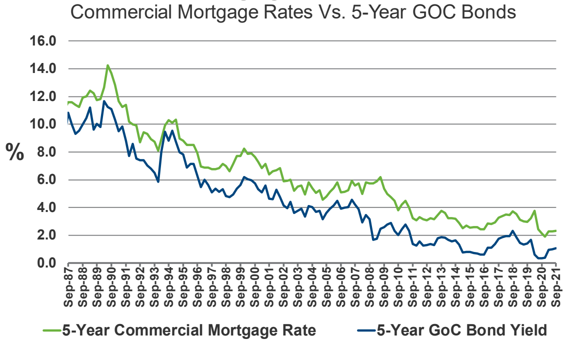
Source: Bank Of Canada, Statistics Canada

Global Indices
Trending of Global Price Return Indices



Source: RBC Capital Markets

Mortgage Spreads
Commercial Mortgage Rates Vs. 5-Year GOC Bonds



Source: RBC Capital Markets, Bank of Canada

BANK OF CANADA'S POLICY STANCE WAS UNCHANGED

The Bank of Canada (BofC) maintained its accommodative monetary policy stance during the third quarter, in keeping with the trend of the past year. In a September 8th release, the bank stated its intention to hold the overnight rate at 0.25%. In addition, the Bank Rate was held at 0.5% and the deposit rate at 0.25%. At the same time, the Bank's quantitative easing program was maintained at a target pace of $2.0 billion per week. Moreover, the Bank announced it would maintain the overnight rate at the effective lower bound until the nation's economic slack is absorbed and a 2.0% inflation target is achieved for an extended period of time. In July, the Bank forecast the inflation target would be achieved and likley sustained in the second half of 2022. The Bank's rationale for holding off on policy changes during the third quarter was tied to the weaker-than-expected second-quarter Canadian economic performance. Canada's economic recovery slowed significantly between the beginning of April and the end of June, with output declining by 1.0%. However, the Bank anticipated a stronger second half. By 2022, inflation levels were expected to ease, having eclipsed the 4.0% mark. The Bank forecasted a gradual reduction in monetary stimulus, which was implemented in 2020 to offset the pandemic-driven economic downturn. The reduction assumes Canada's economic recovery continues at a relatively healthy pace. The Bank is expected to maintain an accommodative monetary policy position until at least the spring of 2022.

PRICE GROWTH ACCELERATED

The price of goods and services increased at an accelerated rate during the third quarter. The Canadian Consumer Price Index (CPI) rose 4.1% year-over-year as of August, which represented the highest rate recorded since March 2003. There were two main factors that contributed to the accelerated price growth of the third quarter. The first was the upward pressure on prices during the quarter, and the second was markedly lower prices in effect a year ago, according to Statistics Canada. The CPI rose 3.2% year-over-year in August, excluding gasoline. Gasoline prices have increased by 32.5% over the same time period. Price growth was reported in seven of the eight major spending components tracked in the CPI in August, with transportation accounting for the largest share of the increase. Clothing and footwear prices declined year-over-year. The Homeowners' replacement cost index rose 14.3% in August, which represented the largest year-over-year increase since September 1987. Geographically, Atlantic Canada, Alberta and Quebec posted above-average inflation of 4.4% or higher. British Columbia and Saskatchewan have seen more moderate price growth. The regional disparity was a function to some extent of significant shifts in oil pricing. Inflation was expected to moderate in 2022, with the easing of the negative impacts of the pandemic.

EQUITY MARKET BOUNCED BACK FROM LATE QUARTER DOWNDRAFT

Both the U.S. and Canadian equity markets bounced back from a late third-quarter downdraft. The S&P/TSX Composite Index (S&P/TSX) ended the third quarter just shy of the all-time high set in August. The S&P 500 performance pattern was somewhat similar, as the index neared a record-high by the end of September. North American equity markets began the third quarter on a high, with five consecutive monthly gains reported up to and including August. However, the S&P/TSX was edged down slightly and S&P 500 dropped 5.0% in September. The downdraft was a byproduct of several risk-related concerns including the inflation outlook, the U.S. debt ceiling, the Evergrande crisis in China, and the timing of monetary policy loosening measures. By the end of the third quarter, however, the S&P/TSX was up 0.17% and the S&P 500 approached the most recent record high having rebounded from the late third-quarter downdraft.

INVESTMENT ACTIVITY REMAINED ROBUST

Commercial real estate investment activity remained robust during the third quarter, having surpassed the pre-pandemic level in the first half. More than $10.0 billion of investment capital had already been injected into the asset class with one week remaining in the quarter. As a result, 2021 was shaping up to be one of the more active years on record. Industrial assets remained a prized asset class with investors, resulting in the sale of several big box properties during the third quarter. The multi-suite residential rental sector was another preferred target of investors during the third quarter, in keeping with the trend of the past few years. The sector was expected to set a record-high national transaction volume total for 2021. Investor optimism and activity in the nation's office sector has increased recently, with the continued roll out of vaccines and anticipated return of workers to their respective offices. However, relatively few prime assets transacted during the third quarter and year-to-date. Similarly, investor interest in acquiring retail assets has increased, particularly for properties with needs-based anchors and additional density. Once again, few significant transactions have been completed year-to-date. In general, investor confidence levels have been buoyed by improved property fundamentals and the belief that the worst of the pandemic's negative impacts will continue to wane. Investment activity is expected to continue at a healthy pace over the balance of 2021 and into next year, assuming product availability and a return to a somewhat more normal performance pattern.

CAP RATE TREND WAS LARGELY UNCHANGED

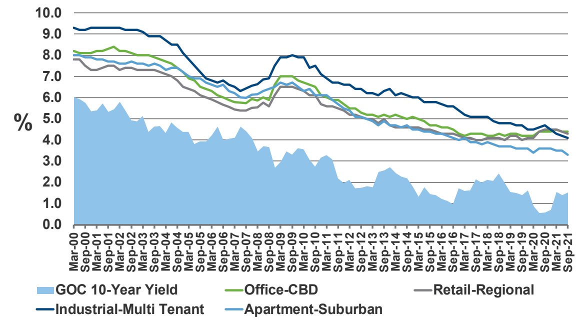
The Canadian commercial real estate asset class cap rate trend was largely unchanged during the third quarter, continuing the year-to-date pattern. Industrial sector cap rates continued to compress at a modest rate, with major market averages falling to the benchmark low. Multi-suite residential rental sector cap rates also rested at the benchmark low as of the end of the third quarter, according to Altus Group survey data. There was some variation in retail cap rates reported during the third quarter. The variation was geographic and by product sub-category. Tier 1 regional centre cap rates were slightly lower in four of the eight major Canadian markets tracked quarter-over-quarter. The surveyed averages were down in seven of the eight markets for food-anchored retail strips. In the office sector, overall cap rates were down slightly for class AA properties in downtown Vancouver quarter-over-quarter. Rates were up in Calgary and Edmonton and flat in eastern Canada. This pattern was in place through much of the past year, a period during which leasing market fundamentals softened substantially. The consistency of the office sector cap rate trend of the past year was in keeping with the broader third-quarter commercial real estate asset class trend.

INVESTMENT MARKET CONDITIONS TO GRADUALLY STRENGTHEN

Canadian commercial property sector investment market conditions are expected to gradually strengthen over the near term. The outlook is predicated on the nation's continued economic recovery and emergence from the negative effects of the pandemic. Economic growth will fuel demand for commercial space and healthier rental market fundamentals. Occupancy will increase in the office and retail sectors with the return of workers to their offices and increased physical capacity in the country's malls and stores. Industrial availability will remain constrained, with demand largely outdistancing supply. Multi-suite residential rental market conditions will tighten, with the return of international migrants and post-secondary students to universities and colleges. The stabilization and strengthening of rental market fundamentals will support moderately stronger investment performance, investor confidence levels, and owner balance sheets. Barring a significant shift in the near-term economic or public health outlooks, investment market conditions will gradually strengthen.

Yield Spreads

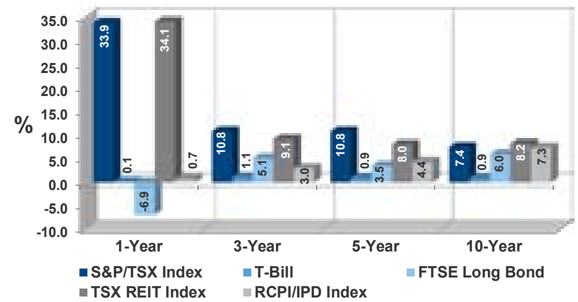
Cap Rates vs. 10-Year GOC Bonds



Source: AltusInSite, Bank of Canada

Relative Performance

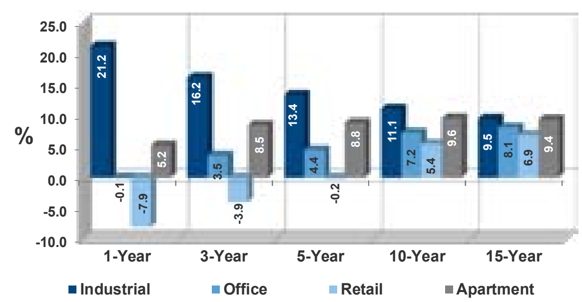
Comparing Annualized Returns To June 2021



Source: © MSCI Real Estate; RBC CM; TSX Datalinx; SCM; PC Bond Analytics

MSCI Returns

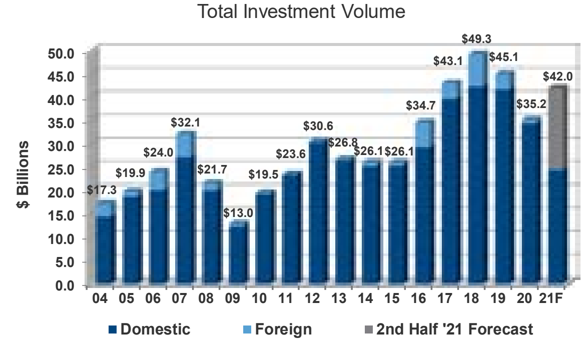
Annualized Returns By Property Type To June 2021



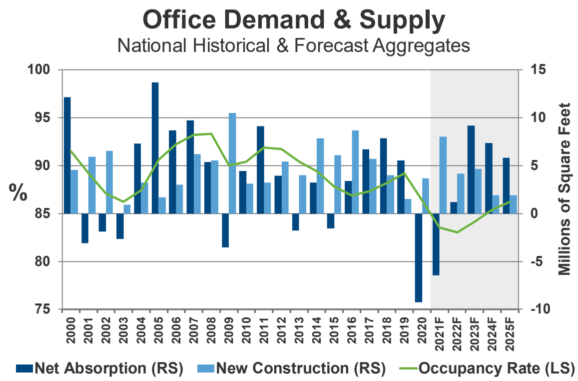
Source: © MSCI Real Estate 2021

Investment Activity

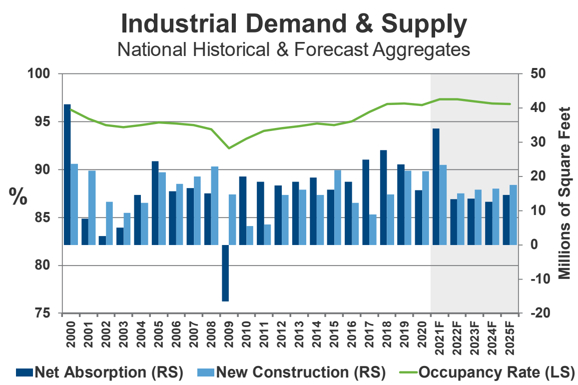
Total Investment Volume



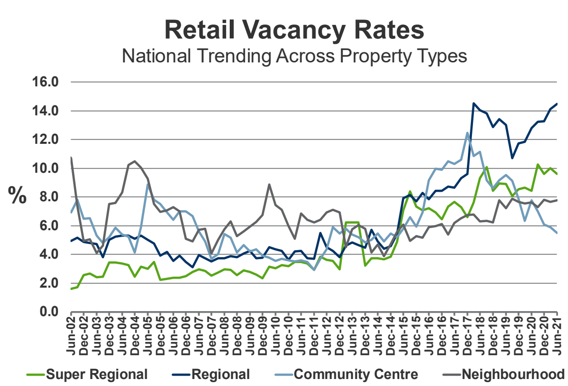
Source: CBRE Limited; Morguard



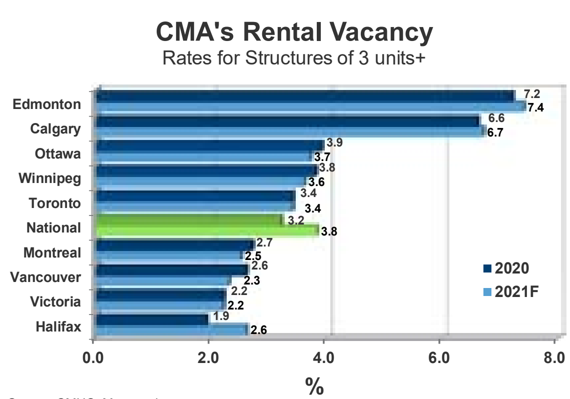
Source: CBRE Limited; CBRE Econometric Advisors



Source: CBRE Limited; CBRE Econometric Advisors



Source: © MSCI Real Estate 2021



Source: CMHC; Morguard

EROSION OF SUPPLY FUNDAMENTALS SLOWED

The erosion of Canadian office leasing market supply fundamentals eased during the third quarter. The national vacancy rate rose by a relatively modest 40 bps to 15.7% over the three-month period, which represented a 21-year high. However, 40-bps rise in the national vacancy rate was modest compared with the previous five quarters. Vacancy increased by an average of 100 bps over the five-quarter period as tenants looked to reduce expenses during a period of heightened economic and public health uncertainty. In addition, the shedding of excess space onto the sublet market slowed during the third quarter, for the first time since the onset of the pandemic. A total of 15.4 million square feet of sublease space was available in the country's major urban centres combined at the end of September, down from the 15.8 million square feet reported last quarter by CBRE. Some of the space had been successfully sublet while fewer tenants looked to sublease space as a sign of rising business confidence levels. To some extent, the rise of the pandemic's fourth wave put a damper on the plans of Canadian corporations to return to the office. However, it appeared that the national leasing market may begin to recover in short order. National office supply fundamentals are expected to stabilize early next year, following a period of modest erosion.

AVAILABLE SUPPLY WAS EXTREMELY LIMITED

The supply of available space in Canada's industrial leasing market was extremely limited during the third quarter. The national availability rate rested at a 21-year low of 2.0% at the end of September 2021, down 20 bps quarter-over-quarter and 150 bps from a year ago. A rate of 0.9% or lower was reported by CBRE for Toronto, Vancouver, London, and Waterloo Region. Only Calgary and Edmonton posted availability rates higher than 3.5% at 5.6% and 8.4%, respectively. For the most part, tenants were forced to look to new builds as a source of expansion space or to relocate. However, most of the 34.1 million square feet of space under construction has been pre-leased. Leasing demand continued to outdistance supply during the third quarter, driven in large part by e-commerce, logistics, and distribution companies. Increasingly, tenants have looked to the periphery of the country's major urban centres to expand. The demand-pressure coupled with tight conditions drove market rents higher. The national average market rent moved into double-digit territory during the third quarter, as landlords continued to command a premium when leasing space. According to CBRE, the national average rent increased by 34.5% over the past three years, as available options dwindled. Looking ahead to 2022, available supply will remain extremely limited, which will drive rents to a new benchmark.

EARLY SIGNS OF RENTAL MARKET RECOVERY WERE OBSERVED

The early signs of a multi-suite residential rental market recovery from the negative effects of the pandemic were observed during the third quarter. Rental demand increased in some submarkets where it had previously declined. In these same submarkets, vacancy had increased relatively sharply over the past 12 to 15 months. More specifically, the return of post-secondary students and job growth resulted in moderately stronger demand in the central areas of several cities. In Toronto, for example, bidding wars on some units in the city's central area were reported. At the same time, some landlords reported an increased volume of rental inquiries and tours. According to rentals.ca and bullpen Research and Consulting data, rents have risen year-over-year and stood just 10.0% below the pre-pandemic peak at the end of September 2021. During the pandemic in 2020, larger unit-size rents increased as renters looked to rent outside of the central areas of major cities. However, renters have begun to return with the loosening of pandemic restrictions. This dynamic was an indication of the early signs of a rental market recovery reported in the third quarter.

ECONOMIC RECOVERY PACE PICKED UP

Canada's economic recovery pace picked up during the third quarter, having slowed substantially in the previous quarter. Real Gross Domestic Product (GDP) was forecast to rise by roughly 4.0% in the third quarter, following a 1.1% contraction over the previous three-month period. The third quarter began with a slight contraction of 0.1% for July, which was followed by a 0.4% advance in August. Previously, Statistics Canada had forecast a 0.7% advance for August, However, ongoing supply disruptions continued to reduce output. The recent economic progress was driven in large part by increased activity and output in the nation's services sector, which was forecast to continue over the next six to 12 months. However, there were several downside risks that could slow Canada's economic recovery over the balance of the year and into early 2022. One of the main risks was a renewed surge in COVID-19 infections and hospitalizations. In addition, supply chain disruptions were expected to dampen growth over the near term, along with inflation. By 2022, Canada's economic recovery is projected to strengthen, having picked up steam during the third and fourth quarters of 2021.

LABOUR MARKET RECOVERY CONTINUED TO UNFOLD

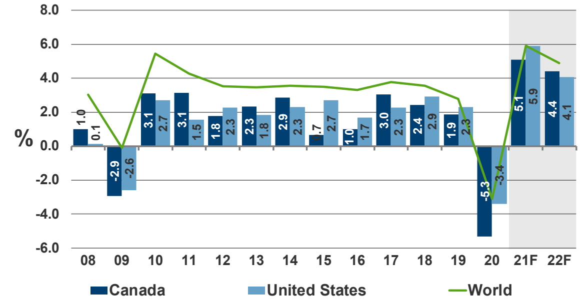
Canada's labour market recovery continued to unfold during the third quarter, despite the potentially negative impacts of the fourth wave of the pandemic. National employment levels continued to rise. Employment had surpassed the pre-pandemic level of February 2020 by the end of September, having recouped the unprecedented losses tallied in the spring of 2020. Employment levels were at or above the pre-pandemic level in both the public and private sectors. In addition, labour market participation had already returned to the pre-pandemic level. The national unemployment rate continued to decline during the third quarter. The unemployment rate edged 20 bps lower in September to 6.9%, marking a fourth consecutive monthly decline. The rate had trended steadily downward since reaching a peak of 13.7% in May 2020. The nation's services sector continued to account for a larger share of employment growth during the third quarter, in keeping with the recent trend. Service-producing employment increased by roughly 142,000 during the quarter, although accommodation and food services has yet to return to the pre-pandemic level. Despite the employment gains of the past several months, some sectors continued to struggle to fill vacancies. Restaurant and retail store operators were often unable to source employees. The supply demand mismatch was expected to persist over the near term, with the continued unfolding of the nation's labour market recovery.

RESALE HOUSING ACTIVITY STABILIZED

Canada's resale housing activity continued to stabilize in the third quarter, following a period of moderation. Activity levels settled into a pattern that was above the pre-pandemic era. Approximately 48,900 sales were recorded in September, in surpassing the 45,000 mark for a fifteenth consecutive month. Although sales increased by 0.9% year-over-year, they were down 12.0% quarter-over-quarter. Housing market conditions remained relatively tight with just 2.1 months of inventory available as of September 2021. Market conditions favoured sellers across much of the country, except for Alberta and Saskatchewan. In addition, resale housing prices continued to rise during the third quarter. The average Canadian home price increased 1.2% month-over-month in September. The MLS home price index posted a firmer 1.7% increase over the same time-period. Additionally, the Teranet-National Band index rose 1.0% month-over-month in August, marking a 22nd consecutive rise. Home prices are expected to continue to rise over the near term, as demand continues to outstrip supply. Housing market conditions will continue to stabilize in 2022, due in large part to tighter mortgage rules and a lack of supply which was also the case during the third quarter.

Economic Growth

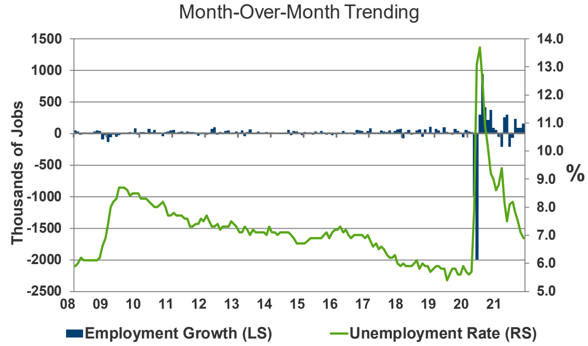
Real GDP Growth - Historical & Forecast



Source: Conference Board Of Canada (Sept 2021); International Monetary Fund (October 2021)

Labour Market

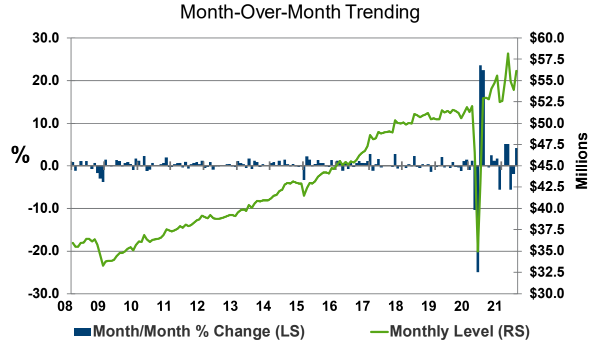
Month-Over-Month Trending



Source: Statistics Canada

Retail Sales

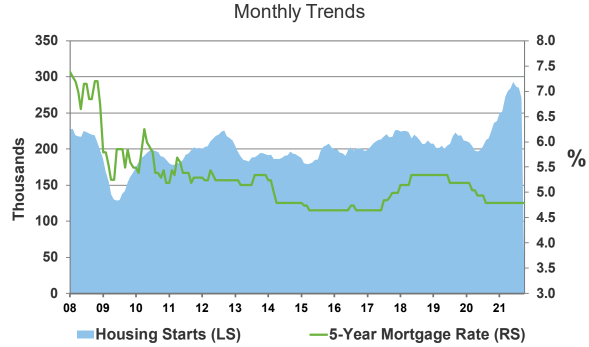
Month-Over-Month Trending



Source: Statistics Canada

Housing Market

Monthly Trends



Source: Statistics Canada, CMHC, Bank of Canada

OFFICE

Property	Date	Price	SF	PSF	Purchaser	City
1870 Alta Vista Dr	Sep-21	$31.6 M	112,000	$282	Groupe Mach	Ottawa
275 Viger East Ave	Aug-21	$74.0 M	200,771	$369	BentallGreenOak	Montreal
5875 Explorer Dr	Aug-21	$17.6 M	51,595	$340	Groupe Mach	Toronto
1415 Joshuas Creek Dr	Jul-21	$32.7 M	86,463	$378	Canadian Urban	Toronto
59 Hayden St (units 400-600)	Jul-21	$27.3 M	39,267	$694	Fidelity Property Mgt.	Toronto

INDUSTRIAL

Property	Date	Price	SF	PSF	Purchaser	City
KingSett Mississauga Portfolio	Sep-21	$61.1 M	261,817	$233	Berkshire Axis	Toronto
735 Intermodal Dr	Sep-21	$38.0 M	159,645	$238	Pure Industrial REIT	Toronto
7400-7420 Bramalea Rd	Aug-21	$90.2 m	328,268	$275	Pure Industrial REIT	Toronto
Henday Park Portfolio	Aug-21	$94.6 M	618,363	$153	Sun Life Assurance	Edmonton
202 South Blair St	Aug-21	$40.6 M	306,704	$132	Soneil Investments	Toronto
1160-1170 Birchmount Rd	Aug-21	$78.5 M	362,682	$216	Soneil Investments	Toronto
Huntington Portfolio	Jul-21	$50.1 M	217,214	$230	Crestpoint	Ottawa
3100 des Batisseurs St	Jul-21	$35.0 M	178,542	$196	Dream Industrial REIT	Montreal
Artis REIT GTA Portfolio	Jul-21	$750.0 M	2,526,632	$297	Pure Industrial REIT	Toronto
Carttera Private Equities Portfolio	Jul-21	$183.0 M	605,423	$302	LaSalle Investment Mgt.	Toronto

RETAIL

Property	Date	Price	SF	PSF	Purchaser	City
1465 Merivale Rd	Sep-21	$32.9 M	78,848	$417	GWL Realty Advisors	Ottawa
8134 Yonge St	Aug-21	$17.9 M	12,100	$1,479	Kaka Plaza Corporation	Toronto
Devimco Portfolio	Jul-21	$40.2 M	119,303	$295	Broad Group	Montreal
170 North Queen St	Jul-21	$31.5 M	81,450	$387	Memory Express	Toronto
Sinclair Place	Jul-21	$15.0 M	28,492	$526	Li Limited Group	Toronto

MULTI-SUITE RESIDENTIAL

Property	Date	Price	# Units	/Unit	Purchaser	City
2670 Library Ln	Sep-21	$54.5 M	75	$726,000	Starlight Investments	Vancouver
Missao	Sep-21	$25.1 M	95	$264,673	Strategic Group	Calgary
Weston Common	Sep-21	$338.9 M	841	$401,902	Dream Unlimited	Toronto
200 Jameson Ave	Sep-21	$32.2 M	100	$322,000	Crestpoint	Toronto
1287 Costigan Rd	Sep-21	$62.6 M	105	$595,714	Realstar Group	Toronto
Island Park Towers	Aug-21	$267.0 M	642	$415,888	Homestead	Ottawa
Domaine Salaberry	Aug-21	$31.7 M	248	$127,621	Recan	Montreal
Rideau Tower	Jul-21	$28.4 M	143	$212,000	Har-Par Investments	Edmonton
Complexe Sur Le Parc	Jul-21	$21.2 M	160	$132,663	Hazout Group	Montreal
4750 Bathurst St	Jul-21	$19.0 M	64	$296,875	Starlight Investments	Toronto

* share sale

FORWARD-LOOKING STATEMENTS DISCLAIMER

Statements contained herein that are not based on historical or current fact, including without limitation statements containing the words “anticipates,” “believes,” “may,” “continue,” “estimate,” “expects” and “will” and words of similar expression, constitute “forward-looking statements.” Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, events or developments to be materially different from any future results, events or developments expressed or implied by such forward-looking statements. Such factors include, among others, the following: general economic and business conditions, both nationally and regionally; changes in business strategy; financing risk; existing governmental regulations and changes in, or the failure to comply with, governmental regulations; liability and other claims asserted; and other factors. Given these uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements. The publisher does not assume the obligation to update or revise any forward-looking statements.

ACKNOWLEDGEMENTS / RESEARCH RESOURCES

In the course of compiling the statistical information and commenting on real estate markets, national, regionally and across Canadian metropolitan areas, we acknowledge the assistance and feedback from the following parties in completing this report:

The Altus Group, Avison Young, Bank of Canada, Bank of Japan, BMO Economics, BMO Nesbitt Burns, British Bankers’ Association, Brunsdon Martin & Associates, CBRE Econometric Advisors, CBRE Limited, CIBC World Markets, Canada Newswire, Canadian Mortgage and Housing Corporation (CMHC), Canadian Mortgage Loans Services Limited, The Canadian Real Estate Association (CREA), Colliers International, Conference Board of Canada, Cushman & Wakefield, Developers and Chains e-news, Economy.com, European Central Bank, The Federal Reserve Board, Frank Russell Canada (RCPI), The Globe and Mail, ICR Commercial Real Estate, International Council of Shopping Centres (ICSC), Insite-Altus Research, International Monetary Fund, The Johnson Report (Winnipeg), Jones Lang LaSalle, Monday Report on Retailers, MSCI, The Network, Ottawa Business Journal, PC Bond Analytics, PricewaterhouseCoopers, RBC Capital Markets, RBC Economics, RealNet Canada Inc., Rogers Media, Statistics Canada, Scotia Capital, TD Economics, Toronto Star, Torto Wheaton Research, Urban Land Institute, United States Department of the Treasury, York Communications

ABOUT MORGUARD

Morguard’s core strength is real estate ownership, management and investment. With a strategic focus on high-quality assets and diversification, we realize the potential of real estate through consistent investment performance. Our primary business strategy is to generate stable and increasing cash flow and asset value by improving the performance of the real estate investment portfolio and by acquiring and developing real estate properties in sound economic markets.
We have developed a broad and efficient real estate platform in North America to manage our own real estate portfolio, as well as invest and manage real estate on behalf of institutional clients. Today, our owned and managed Real Estate Portfolio is valued at nearly $15 billion.

To contact us, visit MORGUARD.COM

55 City Centre Drive
Suite 1000
Mississauga, ON
L5B 1M3
905-281-3800

MORGUARD.COM