MARKET REPORT
OFFICE

Montreal Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS
A DIVISION OF MARCUS & MILLICHAP, BROKERAGE

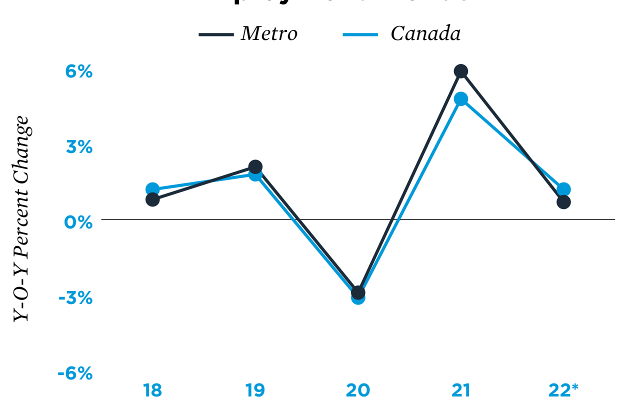
3Q/22

Drive to Reignite Core Helps Stimulate Leasing Activity; Tech and Life Science Enter Market

Flight-to-quality remains primary leasing trend. Montreal experienced an uptick in leasing activity in the first half of 2022, with Class A and high-tier Class B assets seeing the highest demand. Throughout the health crisis, downtown Montreal faced significant headwinds. However, over the past few quarters, the government, along with property owners, have taken steps to re-establish the downtown core, with increased amenities and a diverse array of new activities. Although net absorption is still negative, it appears the market is close to reaching an inflection point, as the magnitude of negative absorption is beginning to subside. Finance and real estate remain important drivers for local office demand, with tech and media companies becoming increasingly prominent as Montreal is beginning to establish itself as a leader in language translation artificial intelligence. This is causing an increase in demand for high-quality, centrally-located assets, resulting in strong investment activity as owners still have confidence that Montreal will become a leading tech market.

Life science companies entering Montreal. Demand in Montreal's suburbs has been comparatively stable during the pandemic. Areas like Saint-Laurent and South Shore offer high-tier Class A assets, which fit well with the general flight-to-quality trend. Furthermore, Moderna committed to the Greater Montreal Area as the location for its next research and innovation center, boosting the life science ecosystem. It is expected that additional companies will follow, elevating demand for high-quality research and development laboratories in Montreal's suburbs, encouraging further investment activity.

Employment Trends



* Forecast

Sources: Statistics Canada; CoStar Group, Inc.; Altus Data Solutions

Office 2022 Outlook

16,600
JOBS
will be created

EMPLOYMENT:

Employment growth is expected to slow compared to 2021, due to the omicron variant and economic uncertainty stemming from elevated inflation and rising interest rates. Additionally, Québec's aging population is resulting in increased retirements.

1,200,000
SQ. FT.
will be completed

CONSTRUCTION:

Montreal is set for a significant amount of deliveries in 2022, resulting from projects being delayed amid supply chain disturbances caused by the global health crisis. This influx of new supply could weaken near-term fundamentals if not quickly absorbed.

150
BASIS POINT
increase in vacancy

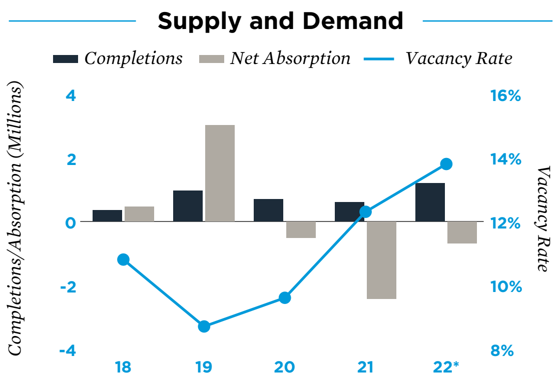
VACANCY:

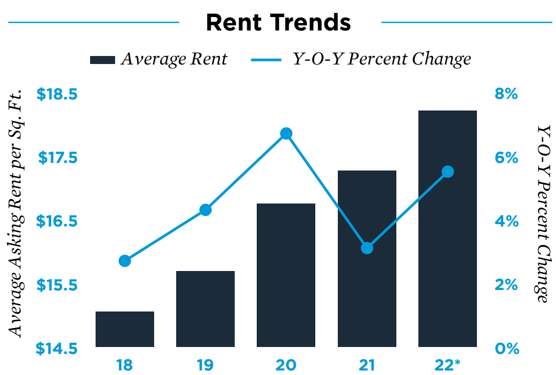
With net absorption remaining negative and companies still deciding their office strategies, vacancy will increase. The rate is expected to end the year at 13.8 per cent, lifted by a combination of hybrid work and the influx of new space, which is not fully pre-leased.

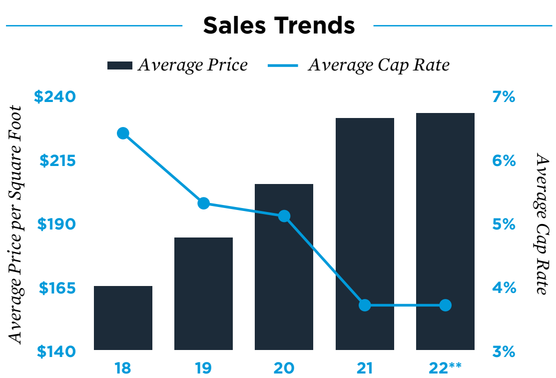
5.5%
INCREASE
in asking rent

RENT:

Even with negative net absorption and increasing vacancy, Montreal is still experiencing positive rent growth, due to the national flight-to-quality trend. Most leasing activity is happening within high-tier properties as they come to market, resulting in the average asking rent increasing to $18.21 per square foot by year-end.







** Forecast ** Through 2Q*

Sources: CoStar Group, Inc.; Altus Data Solutions

2Q 2022 - 12-Month Period

CONSTRUCTION

265,000 sq. ft. completed

- Construction slowed over the trailing-12-month period, due to uncertainty in the office market, and also because of rising costs and supply chain disruptions causing delivery dates to be pushed.
- During the yearlong period that ended in June, less office space finalized than in any other 12-month stretch over the past decade.

VACANCY

140 basis point increase in vacancy Y-O-Y

- Leasing activity has slowed over the trailing-12-month period, especially for lower-tier Class B and C properties, as hybrid work persists. Nonetheless, activity did increase when compared to the previous period.
- Vacancy remained elevated in the downtown, prompting many owners to enhance building amenities to attract workers back to the office.

RENT

0.1% increase in the average asking rent Y-O-Y

- Despite increasing vacancy and negative net absorption, the average asking rent still rose over the trailing-12-month period, though only marginally, with most leasing activity picking up in Class A assets.
- Class A leasing was stronger in the suburbs, experiencing positive absorption in each of the previous four quarters.

Investment Highlights

- Investment activity was robust throughout the first half of 2022, especially in the first quarter, increasing by nearly 120 per cent year-over-year, and 65 per cent since the first quarter of 2020. Like most other major metros, private Canadian investors led the way, with a 62 per cent share of total dollar volume transacted. This large increase in sales suggests that investors continue to believe in Montreal's potential as a world-class tech hub.
- The largest transaction thus far in 2022 was Blackstone's purchase of a two-office portfolio from Kevric Realty for $231 million. Both assets are centrally located with direct access to Montreal's public transit and underground networks. These properties have tech tenants as current occupiers, again reinforcing investors' belief in Montreal's tech scene. Additionally, Allied Properties REIT purchased six assets from Choice Properties REIT for nearly $102 million. Allied has been one of the most active investors in the Montreal region, purchasing several properties in recent years.
- Montreal has experienced the second-largest price growth across all major metros at 41 per cent since 2018, only trailing Vancouver. This again shows investors' confidence in the Montreal office market, due to the potential growth in the technology sector. Cap rates have also compressed significantly during that span, decreasing 270 basis points to 3.7 per cent.

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