RESEARCH BRIEF
CANADA MONETARY POLICY

IPA INSTITUTIONAL PROPERTY ADVISORS
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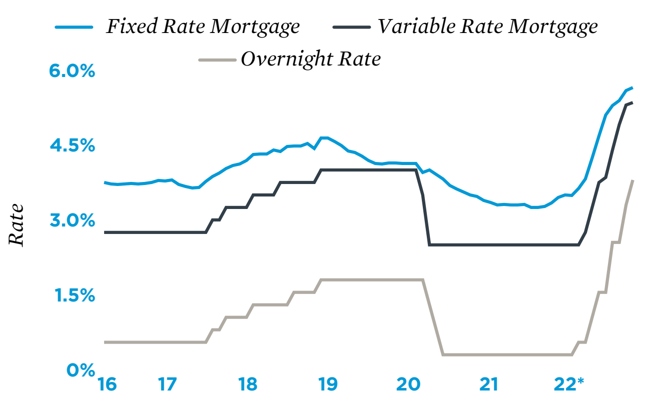
Sticky Inflation Results in Additional Interest Rate Hike; Pace of Policy Tightening Slows

Bank of Canada remains hawkish. Ongoing rapid inflation, fueled by supply chain bottlenecks and excess demand stemming from a relatively healthy labour market, led the BoC to raise the overnight rate by an additional 50 basis points in October. This is the sixth rate hike this year, bringing the policy rate to 3.75 per cent — the highest it has been since early 2008. While inflation has softened, reaching 6.9 per cent in September — which is down from the high of 8.1 per cent witnessed in June — price growth remains well above the target of 2.0 per cent. The Bank, however, is now considering the overall health of the economy and the possibility of an upcoming recession, not just price growth. This may be a reason why the BoC is slowing the pace of its tightening schedule, possibly indicating that its quantitative tightening program is nearing an end, with one further rate hike expected in December.

Mortgage rates expected to rise. With the overnight rate trending upward, mortgage rates will likely follow. Both fixed and variable rates have already eclipsed 5 per cent, and are likely to continue toward 6 per cent in the coming months. While this elevated cost of borrowing has caused housing prices to cool from recent highs, they are still historically elevated, due to the limited supply of single-family homes. Combined with higher debt servicing payments, many potential buyers are still kept on the sidelines, due to affordability challenges. Given these current barriers to homeownership, it further highlights the need for purpose-built rentals as an affordable housing solution.

Rates Continue on Upward Trend

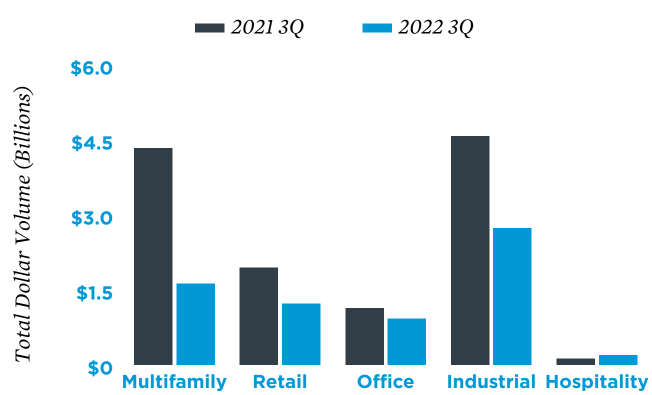


Commercial Real Estate Outlook

Increasing borrowing costs likely to hinder development activity. Rising interest rates, plus elevated construction costs due to supply chain disruptions, labour shortages and government policies, have caused many developers to question the feasibility of upcoming multifamily projects. Some timelines have been pushed, while certain projects have been outright canceled, as firms cannot receive financing when minimum requirements are not being met. Future development activity, as a result, may slow, further amplifying the supply and demand imbalance that exists within Canada's housing market. Over the long term, this will likely result in additional affordability challenges, as robust population growth — fueled by immigration — will result in sustained housing demand. Local governments in Vancouver and Ontario are beginning to take action in order to speed up timelines and minimize administrative costs. However, these new policies will take time before the full impact is realized.

Investors take a wait-and-see approach. Even with sound underlying fundamentals for almost all asset types, it is likely that investor enthusiasm will ease as rising borrowing costs continue to create uncertainty within the transaction market. Many buyers are currently waiting to determine where interest rates will stabilize. A significant price expectations gap also exists between buyers and sellers. Expectations should realign, however, when interest rate hikes plateau and sellers come to terms with the new investment environment. Once uncertainty mitigates, healthy property performance for most asset types will likely act as a backstop to the transaction market, allowing positive investment sentiment to build.

Rising Borrowing Costs Slow Investment



** Through October 26*
Sources: IPA Research Services; Altus Data Solutions; Bank of Canada; Canada Mortgage and Housing Corporation; Capital Economics; CoStar Group, Inc.; Statistics Canada