RESEARCH BRIEF
CANADA RETAIL SALES

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

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Household Spending Losing Momentum; CRE Able to Weather Short-Term Slowdown

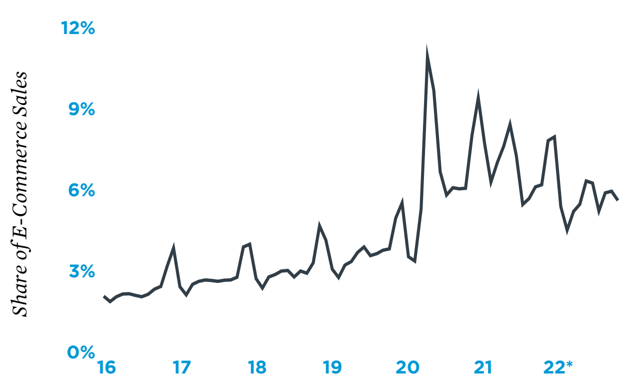
Retail sales remain sluggish. Consumption neared $62 billion in October, a 1.4 per cent monthly increase, or 6.5 per cent annually. After accounting for price growth, however, total volume remained unchanged as inflation-adjusted sales struggle to obtain momentum. October's gains were likely a byproduct of elevated gas prices. Preliminary estimates for November suggest that sales are expected to decline by 0.5 per cent. If these estimates come to fruition, consumption may be heading toward its second consecutive quarterly contraction, making a potential recession in the first half of 2023 more likely. Canada's commercial real estate sector, however, remains well positioned to weather a short-term economic slowdown.

Industrial demand to persist. E-commerce sales were up 156 per cent compared to 2019 levels in October, and are expected to remain elevated due to an evolving consumer profile. Nonetheless, activity has begun to slow in recent months. At its peak, online sales accounted for 11 per cent of total retail spending, but that figure has since tracked down, sitting at 4.5 per cent as of October. Industrial demand, consequently, will likely begin to soften over the coming months. Retailers will burn through just-in-case inventories, and a pullback in shopping will further curb space demand. Over the long term, however, inventory amounts should remain above pre-pandemic levels, and new demand drivers stemming from onshoring are expected to emerge. Therefore, despite economic headwinds and elevated borrowing costs, investor sentiment could remain positive, as limited supply keeps national vacancy hovering around 1.0 per cent and rent growth in the double-digit range.

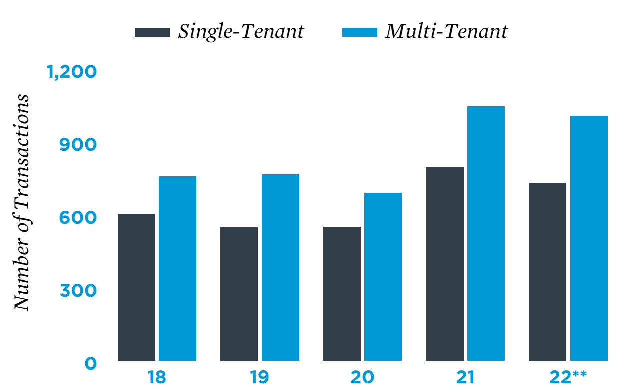
Travel spending slows, hotels well positioned. Canada's hospitality sector experienced a robust recovery throughout 2022, after being one of the hardest-hit industries at the onset of the global health crisis. In the summer, key income metrics, such as revenue per available room and the average daily rate, were both up 16 per cent when compared to pre-pandemic levels. Nonetheless, with elevated interest rates and heightened inflation eating into households' real disposable income, travel activity is beginning to soften. As of October, household accommodation-related spending was only up 8.0 per cent compared to 2019 values, down from 19.7 per cent witnessed in September. The outlook for the hospitality sector remains optimistic, however, as corporate travel is anticipated to climb closer to pre-pandemic measures. This new source of demand will likely act as a backstop to softening household travel spending, keeping underlying income metrics healthy.

Single-tenant retail sustains appeal. In recent years, retail assets gained attention from investors, due to elevated cap rates and sound fundamentals. With economic uncertainty ahead, single-tenant, essential retail is likely to continue to generate positive investor interest because of the necessity of the products offered. These non-discretionary retailers provide essential goods, which are consistently a part of consumer spending habits, making supermarkets and other necessity vendors resilient against economic downturns. As a result, grocery-anchored retail or single-tenant pharmacies, for example, should continue to experience generally stable demand, though muted compared to recent years due to elevated borrowing costs.

Online Sales Reverting to Long-Term Trend Line



Single-Tenant Sales Tick Up During Uncertainty



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** Through October; ** Trailing 12 months through 3Q*
Sources: IPA Research Services; Altus Data Solutions; Capital Economics; CoStar Group, Inc.; RBC Economics; Statistics Canada