RESEARCH BRIEF
CANADA GDP

IPA INSTITUTIONAL PROPERTY ADVISORS
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Canadian Economy Stagnates, Supports Bank of Canada's Pause in Monetary Tightening

Growth ground to a halt in final quarter of 2022. Canada's GDP was unchanged in the fourth quarter of last year, which was mainly driven by a fall in the pace of inventory buildup, as well as weak residential and business investment. These declines, however, were offset by positive net trade and a 2.0 per cent annualized increase in household consumption. While no growth was much weaker than the 1.6 per cent annualized consensus, the preliminary estimate for January suggests a 0.3 per cent gain in GDP. If true, this would imply positive first quarter growth, indicating the economy could potentially avoid a recession. Future economic contraction, however, still remains a possibility as the economy absorbs elevated interest rates.

Stalling GDP could provide silver lining for real estate industry. Throughout last year, rising interest rates pushed many potential buyers to the sidelines and caused price expectation gaps among market participants. Consequently, investment activity slowed significantly. In the second half of 2022, total dollar volume transacted was down roughly 45 per cent when compared to the same time period in the prior year. However, with Canada's economy slowing at a faster pace than the Bank of Canada expected, the overnight rate should remain unchanged at 4.5 per cent. This likely pause in monetary tightening should bode well for real estate transaction activity, as uncertainty should soon abate and underlying fundamentals remain healthy for almost all property types. Positive investor sentiment, as a result, should begin to build once this pause is absorbed by the market. This is likely to cause an uptick in sales activity as buyers look to get ahead and capitalize on pricing opportunities.

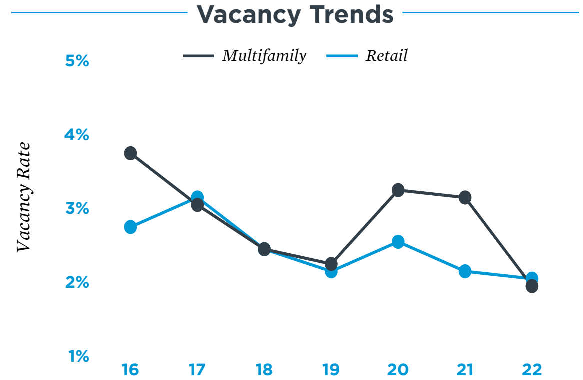
Commercial Real Estate Outlook

Retail sector well-positioned, despite slowing economy. Household consumption increased by 2.0 per cent annualized in the fourth quarter of last year, suggesting that retail spending activity held firm. As a result, retail-related CRE assets should remain a favoured property type among the investment community, despite heightened borrowing costs. Over the past couple years, retail has offered higher yields when compared to other assets and continues to witness healthy rent growth — due to sustained demand, limited supply and elevated construction costs. To end 2022, the national vacancy rate hovered around 2.0 per cent. Consequently, even with a slowing economy, retail will likely remain a preferred investment option. Single-tenant assets with non-discretionary tenants, such as grocery stores and pharmacies, will stand out as the essential nature of the products offered attracts consumers, despite tightening budgets.

Immigration supports positive multifamily outlook. During 2022, national apartment vacancy fell 120 basis points to 1.9 per cent. This caused rent growth to reach 7.3 per cent year-over-year, both of which were the largest on record. These robust fundamentals were a byproduct of homeownership challenges, but mainly due to a record level of new immigrants arriving in Canada. While the economy continues to show signs of weakening, the apartment rental market remains well-positioned to weather a short-term slowdown. Immigration levels are expected to surpass 2022's historic numbers, and new supply continues to lag behind population growth. Consequently, vacancy is expected to continue on its downward trajectory, which supports further rent growth.

Economy Grapples with Elevated Interest Rates

Vacancy Trends



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