RESEARCH BRIEF
CANADA GROSS DOMESTIC PRODUCT

IPA INSTITUTIONAL PROPERTY ADVISORS
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JUNE 2023

Canada's Economy Remained Resilient to Start 2023, Despite Elevated Borrowing Costs

Economy returns to positive growth territory. Canada's economy grew at a stronger-than-expected pace in the first quarter. Gross domestic product expanded 3.1 per cent annualized, which was above the preliminary estimate of 2.5 per cent. This indicates that Canada avoided recession for the time being as it comes after the economy contracted slightly in the final quarter of 2022. Healthy growth to begin the year was largely due to an uptick in household consumption, which grew 5.7 per cent annualized and helped offset the fall in government spending and residential investment. Looking forward, the latest preliminary estimate suggests that GDP increased 0.2 per cent month-over-month in April, after it was unchanged in March. If the estimates materialize, then GDP growth for the second quarter should surpass the Bank of Canada's forecast of 1.0 per cent, as it appears likely that GDP rose again in May.

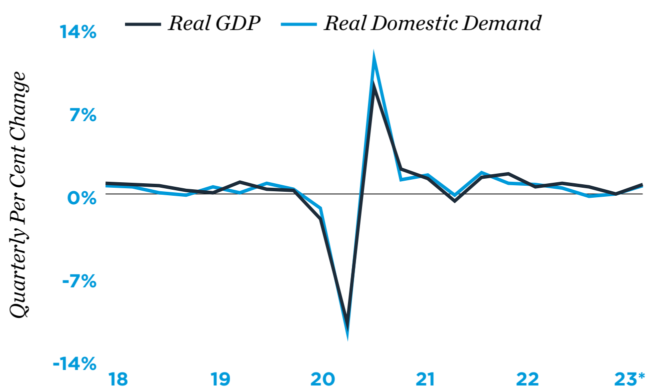
Resilient economy supports case for another rate hike. While economic growth is a positive outcome, it also provides further inflationary pressures. Both GDP and inflation are now topping expectations, which may force the BoC to raise interest rates further. Although the positive economic performance does increase the likelihood of additional hikes, inflation on balance is trending down and cracks in the labour market are beginning to form, making the possibility of keeping rates flat more likely than not. Despite the overhang of a possible rate hike creating further uncertainty in the investment market, transaction activity could gain momentum over the latter half of the year, as price expectation gaps mitigate and market participants look to capitalize on sound fundamentals.

Commercial Real Estate Outlook

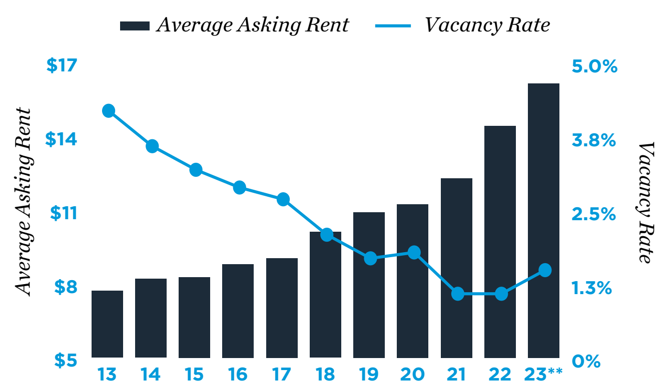
Industrial well-positioned. Between 2020 and the end of 2022, e-commerce related space demand drove the national industrial vacancy rate down 70 basis points, which helped the average asking rent grow nearly 40 per cent. While e-commerce sales are softening, they remain well above the long-term average, which was again supported by the 5.7 per cent annualized gain in household consumption witnessed in the first quarter. Also, due to the ongoing trend of nearshoring, Canada's manufacturing sector is growing as the nation is becoming a popular destination for firms seeking easier access to North American markets, while at the same time mitigating supply chain risks. This is especially true for the automotive industry as Canada is becoming a hotbed for EV battery manufacturing. This emerging demand driver was highlighted by the 7.8 per cent quarterly rise in vehicle sales, as well as the strong rebound in automotive exports. The long-term outlook remains positive for Canada's industrial sector, despite the expected uptick in vacancy due to an influx of new supply.

Healthy consumption supports retail sector. As a result of household consumption rising 5.7 per cent annualized in the first quarter, retail will likely remain a preferred investment option. This is especially true for grocery-anchored centres as they offer stability and risk minimization in times of economic uncertainty. This is due to the essential nature of the products offered as well as the diversified tenant mix. Due to this, sales velocity was relatively more constant in 2022 when compared to other asset types, as total dollar volume transacted only fell 8 per cent year-over-year.

Canada's Economy Remains Resilient



National Industrial Rent and Vacancy Trends



* Through 1Q; ** Forecast

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