MARKET REPORT

Multifamily

Southwestern Ontario Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

A DIVISION OF MARCUS & MILLICHAP, BROKERAGE

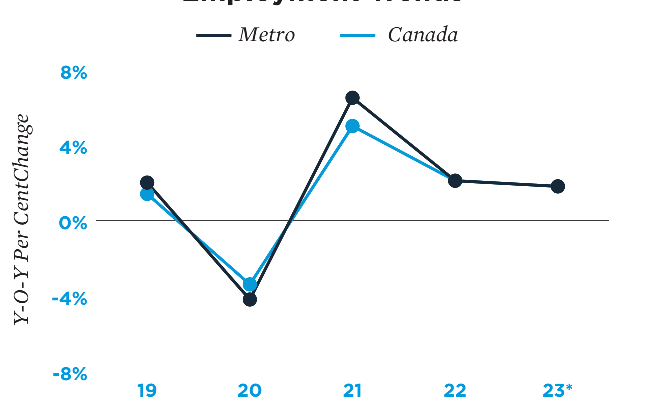
3Q/23

Structural Shift to Hybrid Work and Emerging Employment Opportunities Aid Positive Outlook

Demographic tailwinds support property performance. Southwestern Ontario's multifamily sector has experienced healthy demand in recent years. The metro's vacancy rate fell 60 basis points to 1.7 per cent in 2022, helping annual rent growth surpass 7.0 per cent. This was due to a growing number of households being priced out of the Toronto market, coupled with the structural shift toward hybrid work, causing people to leave downtown cores for more suburban settings. Of the region's population growth, which surpassed 2.0 per cent in 2022, roughly one-third was a result of intra-provincial migration. While on-site work has gained some momentum, causing a share of the population to relocate back to Toronto, historic immigration — along with the emergence of advanced manufacturing — is likely to continue to support healthy apartment demand over the coming years. The vacancy rate is expected to trend down once again in 2023, which will keep rent growth above the metro's long-term average. However, an influx of new supply and a slowing economy may soften the rates of change when compared to last year.

Electric vehicle sector to support long-term demand. With both Volkswagen and Stellantis announcing Southwestern Ontario as the location for their new EV battery manufacturing facilities, the region is beginning to carve out a key place in the global supply chain for electric vehicles. Population growth is likely to remain elevated over the coming years as employment opportunities are expected to increase significantly. Investor sentiment should remain positive, which may support further development within the region.

Employment Trends



* Forecast

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

Multifamily 2023 Outlook

26,700
JOBS
will be created

EMPLOYMENT:

Healthy population growth initiated by the pandemic, coupled with the emergence of advanced manufacturing in electric vehicles, should support employment gains this year. However, labour growth may ease when compared to last year as the economy fully absorbs rising interest rates.

3,600
UNITS
will be completed

CONSTRUCTION:

Development activity is expected to remain elevated in 2023, with numerous new developments and office conversions underway. Many developers are focusing on mixed-use projects that combined residential, retail and recreational spaces.

20
BASIS POINT
decrease in vacancy

VACANCY:

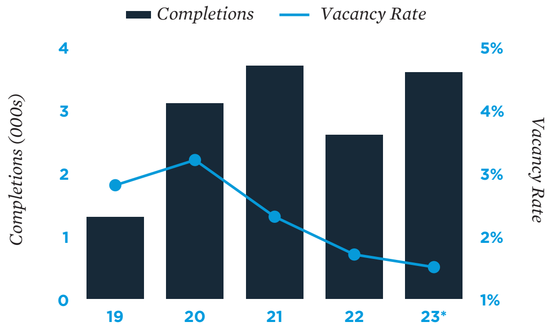
An influx of permanent and temporary residents, due to a high concentration of employment opportunities and educational institutions, will keep availability on a downward trajectory. The vacancy rate is expected to end the year at 1.5 per cent.

6.0%
INCREASE
in effective rent

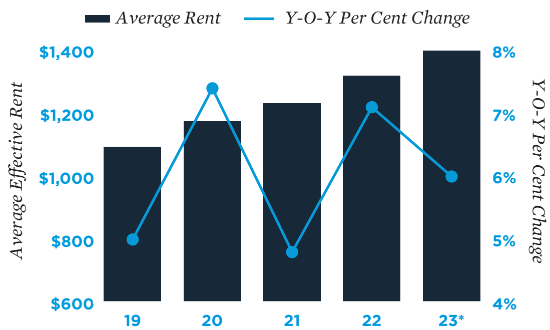
RENT:

Following the 7.1 per cent growth rate seen last year, rents will continue to climb, though at a slower pace due to moderating demand. The average monthly rent will reach roughly $1,400, a near $200 increase since the beginning of the health crisis.

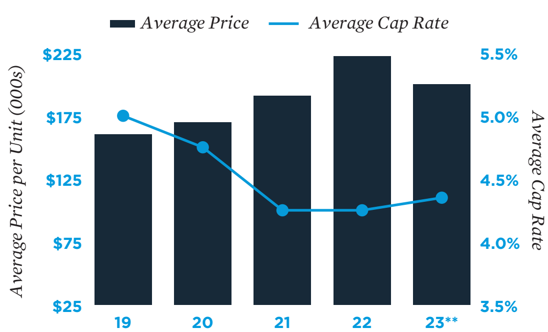
Supply and Demand



Rent Trends



Sales Trends



** Forecast; ** Through 2Q*

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

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2022 Overview

CONSTRUCTION

2,592 units completed

- Supply chain bottlenecks, along with rising material and labour costs, caused development activity to slow last year. New supply fell by roughly 30.0 per cent when compared to 2021.
- Outside of Guelph, university towns like St. Catharines, Kitchener-Waterloo, London and Hamilton witnessed relatively stable construction.

VACANCY

60 basis point decrease in vacancy Y-O-Y

- The vacancy rate dropped below 2.0 per cent for the first time since 2013 amid historic immigration and an elevated level of domestic in-migration.
- As students returned to campuses for the first time since 2020, regions with a large university presence, such as Kitchener-Waterloo and Hamilton, saw the largest vacancy drops.

RENT

7.1% increase in the average effective rent Y-O-Y

- Robust population growth amid historic immigration, coupled with the return of in-person learning, caused annual rent growth to near record levels and sit roughly 300 basis points above the region's pre-pandemic average.
- With new supply falling 30.0 per cent annually last year, the metro's supply-demand imbalance rose, which put further upward pressure on rents.

Investment Highlights

- Investment activity contracted markedly over the second half of 2022 as property underwriting became a challenge. Price expectation gaps emerged, causing many market participants to move to the sidelines. Total dollar volume transacted fell roughly 70.0 per cent year-over-year. However, sales activity did gain some momentum in the final quarter as interest rates showed signs of stabilizing. While sales volumes did contract again in the first quarter of 2023, further momentum was witnessed in the second quarter as total dollar volume rose 140 per cent quarter-over-quarter.
- Southwestern Ontario saw a double-digit percentage increase in its average sale price to over $220,000 per unit in 2022. With rising interest rates cooling demand over the second half of last year, the average sale price has declined roughly 10.0 per cent as of the end of June 2023. Cap rates, as a result, have inched up slightly and hovered just below 4.4 per cent.
- Multifamily is one of the most sought-after asset types among investors in Southwestern Ontario, due to the region's diversified, and thus more robust, demographic composition relative to other metros. Steady population growth throughout the pandemic has strengthened local rental demand, positioning the market to better weather economic downturns.

Price: $250