NATIONAL REPORT

CANADA MULTIFAMILY

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

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Evolving Demographics and Increasing New Supply to Provide Some Vacancy Stabilization

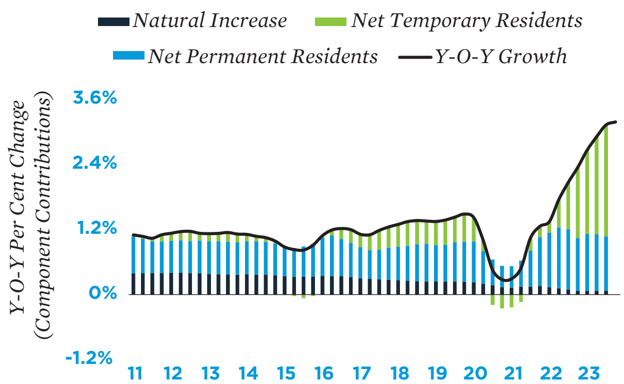
Vacancy rate to remain tight 2024. Canada's multifamily vacancy rate dropped to 1.5 per cent in 2023, the lowest level on record. Demand tailwinds, including historic population growth, robust employment gains and elevated homeownership costs, pushed demand ahead of supply, resulting in the ultra-low vacancy rate and an 8.4 per cent rent increase. In 2024, however, Canada's population growth is projected to soften, and job creation is expected to moderate. Demand for purpose-built rentals, as a result, will increase at a milder pace. With total completions also reaching a new high, the national vacancy rate will stabilize around 1.5 per cent. This will likely cause rent growth to moderate but hold above the nation's long-term standard, given still healthy demand dynamics amid ongoing population expansion and homeownership challenges.

Lower population gains to soften demand growth. One of the main drivers for the fast-declining vacancy rate over the past two years was a record-breaking inflow of new immigrants. As newcomers are primarily renters, apartment demand has risen sharply since 2022. The resulting low vacancy rates and soaring rent increases, however, have prompted a change to Canada's immigration policy. A 35 per cent reduction of study permits and a new set of restrictions for work permits were announced at the start of 2024. Since foreign students and workers accounted for nearly 70 per cent of the population growth last year, this cap on new international students will meaningfully impact population growth in 2024. While remaining above the long-term average, lower population gains will alleviate some demand pressure in the multifamily sector this year.

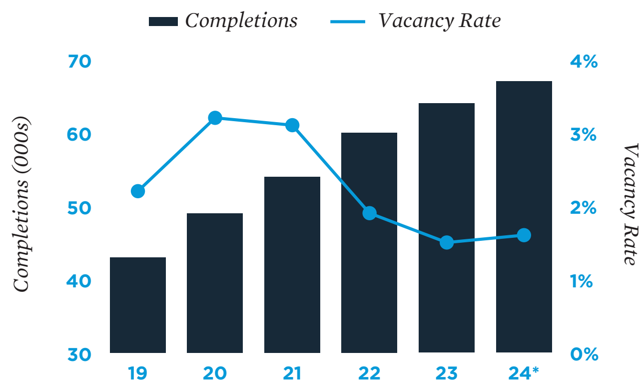
Upward momentum from labour market to fade. Canada's job market performance in 2023 – a 2.1 per cent increase in total employment and a 5.4 per cent advancement in wages – beat many economists' expectations. Apart from record population gains, this strong job and earnings growth also fueled apartment demand. However, as elevated interest rates persist into 2024, the pace of job creation is expected to soften in the near term. Job openings will also remain on a downward trajectory. This should result in higher unemployment rates and more moderate wage growth in the coming months, causing rental demand pressures to ease slightly. The turnover rate will also likely inch lower, which should help whittle down rent growth in metros with rent control policies.

Completions to reach a record high. Surging rental demand over the past few years has spurred development activity in a number of metros. Vancouver's apartment construction starts, for instance, jumped from below 8,000 units in 2021 to over 12,000 in 2023. In addition, a variety of government efforts to boost housing construction, such as the Enhanced GST Rental Rebate and the ongoing discussion of creating a pre-approved home design catalogue, are also good news for builders. These supply-side tailwinds will keep Canada's total apartment completions on an upward trajectory, with new supply projected to approach 70,000 units this year. The climbing new supply, coupled with relatively modest demand growth, will help stabilize the national vacancy rate and soften rent growth in 2024.

Population Growth Hitting Multi-Year High

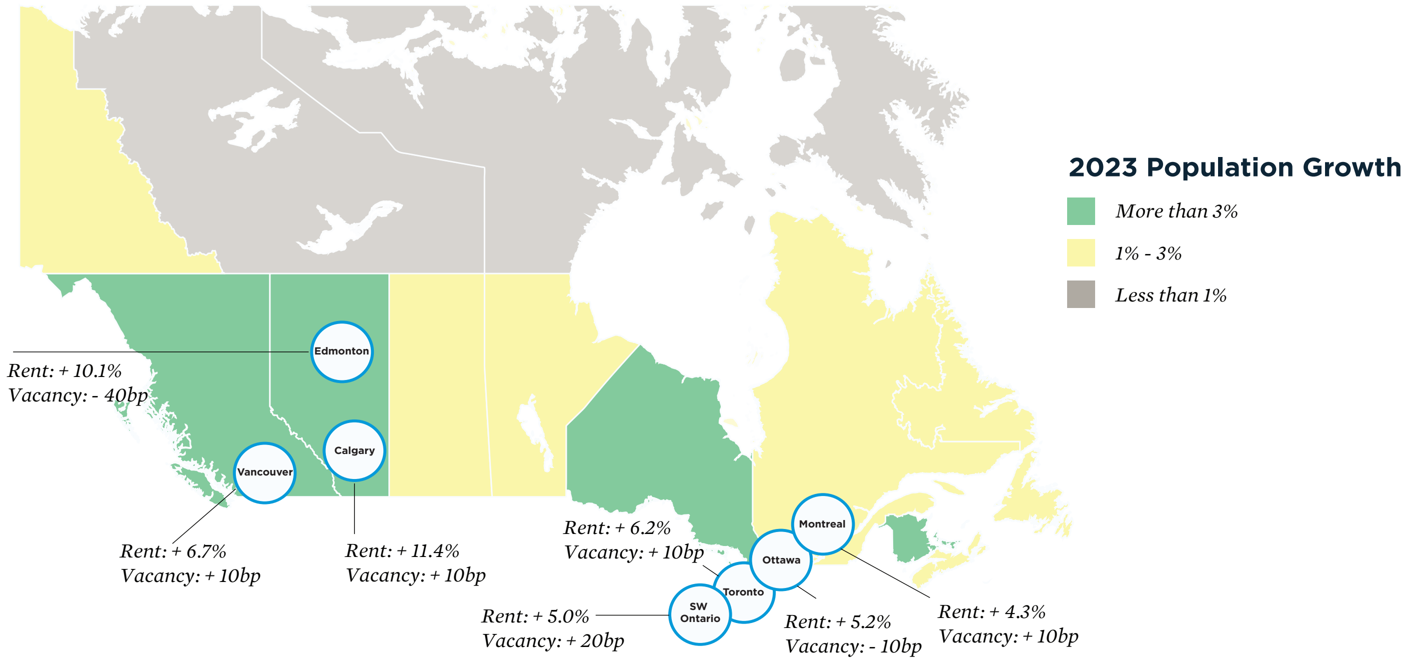


Supply and Demand



* Forecast
Sources: IPA Research Services; Canada Mortgage and Housing Corporation; Statistics Canada

2024 Rent Growth and Vacancy Change Forecasts



Sources: IPA Research Services; Canada Mortgage and Housing Corporation, Statistics Canada

WESTERN CANADA

- **Calgary, Alberta:** Record population growth suppressed the vacancy rate to 1.4 per cent in 2023, marking the first time since 2014 that it has dipped below the national average. This year, the metro will continue to see elevated resident inflows, which will further support rental demand. An influx of new supply, however, will provide some balance to the market.

- **Edmonton, Alberta:** Thanks to its lower cost of living, Edmonton has witnessed a surge in rental demand in recent years. The metro's vacancy rate fell the most among major metros in 2023, which led to a 6.4 per cent rise in the average effective rent. Besides new residents moving into the metro for job opportunities, the rising student population will also support long-term demand.

- **Vancouver, British Columbia:** Vancouver continues to hold Canada's tightest multifamily market, with the vacancy rate stabilizing at 0.9 per cent in 2023. The metro's healthy apartment fundamentals have spurred construction activity in recent years, which is reflected by a significant level of construction starts. Consequently, total completions will increase notably in 2024, providing tenants with much-needed new supply. This will help uplift the vacancy rate back to 1.0 per cent by the end of 2024.

EASTERN CANADA

- **Montreal, Québec:** Montreal's tepid job market and relatively lower population gains are expected to soften rental demand growth within the metro this year. In the meantime, as construction starts have leveled off, new supply is projected to drop. The vacancy rate is forecast to stabilize at roughly 1.5 per cent over the short-term.

- **Ottawa, Ontario:** Tech workers, government employees and university students make up a large part of Ottawa's population. These residents will continue to support rental demand in 2024. As total completions are expected to decline, the vacancy rate will remain on a downward trajectory, ending the year at 2.0 per cent.

- **Southwestern Ontario:** The metro's diversifying economy and its close proximity to Toronto will help maintain healthy multifamily fundamentals. A notable increase in new supply is expected in 2024, which will raise the vacancy rate just above 2.0 per cent.

- **Toronto, Ontario:** Toronto will remain the top destination for newcomers to Canada. However, the recent change to Canada's international student program will cause a reduction in the number of new foreign students. This will slow population growth in 2024, alleviating some demand-side pressure.

2024 Forecast

EMPLOYMENT

0.6% increase Y-O-Y

- The pace of job creation is expected to slow in the first half of 2024 due to elevated interest rates. Possible rate cuts toward the second half are forecast to rekindle upward momentum in the labour market.

CONSTRUCTION

67,000 units completed

- Driven by large increases in Vancouver, Calgary and Southwestern Ontario, total completions will rise by 5.3 per cent in 2024. New supply in other metros will drop slightly but remain at elevated levels.

VACANCY

10 basis point increase Y-O-Y

- Softening demand growth and a higher level of new supply will help stabilize the vacancy rate over the course of 2024. The national vacancy rate will remain tight, below 2.0 per cent.

ASKING RENT

5.6% increase Y-O-Y

- As the vacancy rate remains low, rental rates will increase for another year. Calgary and Edmonton will lead with the highest rent growth, followed by Vancouver and Toronto.

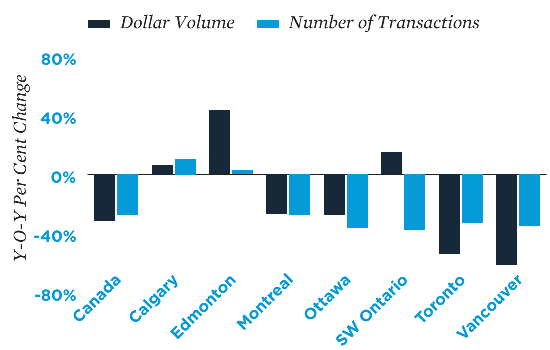
2024 INVESTMENT OUTLOOK

- **Higher financing costs dampened investment volume.** Total dollar volume fell 31 per cent in 2023, mainly due to rising interest rates over the first half of the year. As falling inflation rates prompted the Bank of Canada to remain on the sidelines during the second half, investment activity began to stabilize in the final six months. Despite the overall decrease, investors eyed the Alberta market for its robust fundamentals. Edmonton's multifamily investment jumped 43 per cent, which made the metro the third-most invested market in Canada. Calgary's total dollar volume also increased, by 6.0 per cent, with the number of trades rising by 11 per cent in 2023.

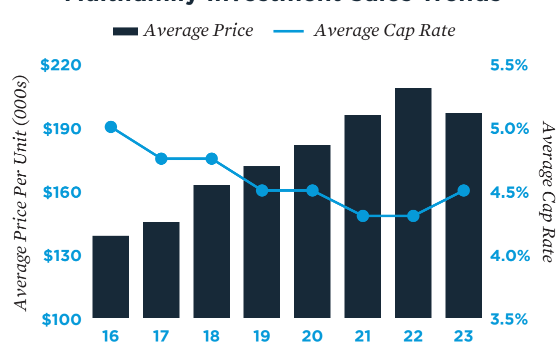
- **Prices continued to soften, pushing up cap rates.** As total investment dropped, the average sale price fell 6.0 per cent in 2023. This was led by a 15 per cent decline in Toronto and a 14 per cent drop in Vancouver. The falling prices, coupled with robust rent growth and rising interest rates, lifted the national average cap rate by 20 basis points.

- **Easing of financial conditions to aid investment activity.** The year-over-year increase in investment seen in the final three months of 2023 suggests that sales volume will likely continue to improve in 2024, given expectations of easier financial conditions toward the second half of the year. Markets with higher yields and robust population growth, such as Calgary and Edmonton, could see more visible investment inflows.

Multifamily Transactions in 2023



Multifamily Investment Sales Trends



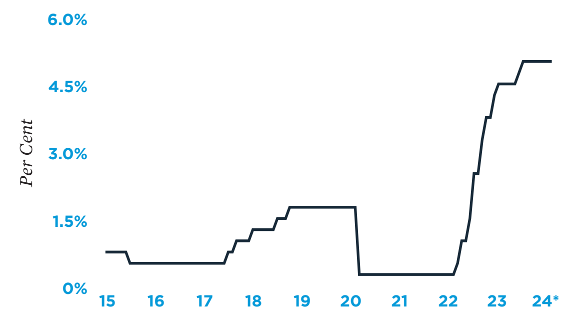
Sources: IPA Research Services; Altus Data Solutions

Bank of Canada On Track to Cut Rates by Mid-Year, Clearing Way for Investment Resurgence

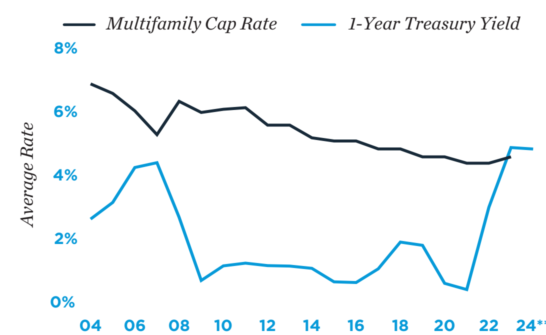
Rate cut by mid-year holds as a probable outcome. Economic data released in the first two months of 2024 points to sustained economic growth amid softening inflation. Canada's economy avoided two consecutive quarters of contraction, or a technical recession, and grew at a 1.0 per cent annualized rate in the fourth quarter of 2023. Advance estimates showed that this upward momentum likely continued into early 2024 as well. January's job report beat market expectations, with the unemployment rate ticking down for the first time since December 2022. Still robust economic performance has brightened growth prospects following the contraction recorded in the third quarter of 2023, which has consequently pushed back the timing of the first rate cut economists had anticipated. However, the rosy growth picture was, to a large extent, aided by record population growth. On a per capita basis, GDP has declined for six consecutive quarters. Coupled with other softening indicators, such as falling job vacancies, lower labour participation rates and sharp increases in part-time employment in recent months, it is now widely expected that the Bank of Canada will start lowering interest rates by mid-2024.

Sales activity to benefit as buyers focus on growth markets. Benefiting from population gains and a more relaxed financial environment, buyers who have remained on the sidelines due to elevated interest rates will likely re-enter the market in 2024. The small but noteworthy year-over-year increase in total dollar volume over the last three months of 2023 may be an early sign of positive momentum. The fixed income market has also priced in lower rates, as short-term treasury yields have fallen back below 5.0 per cent. Combined with a rising cap rate, this will gradually push risk-free rates below multifamily yields, helping the apartment sector regain competitiveness this year. In addition, sales volume may be increasingly concentrated in markets with stronger demand tailwinds, such as the Calgary and Edmonton markets, where the local economy is forecast to outperform the national average with population growth being little impacted by the recent change in immigration policy. Investors may, however, need to be wary of the declining turnover rate observed in select markets. As job and wage growth moderates, tenants in rent-controlled markets may feel increasingly reluctant to vacate when their contracts end. This could slow rent increase, limiting revenue growth for property owners.

Bank of Canada Overnight Rate



Treasury Bill Yield Has Likely Peaked



** Through February; ** 1-year treasury bill yield through February*

Sources: IPA Research Services; Altus Data Solutions; Bank of Canada

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