MARKET REPORT

Industrial

Southwestern Ontario Metro Area

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

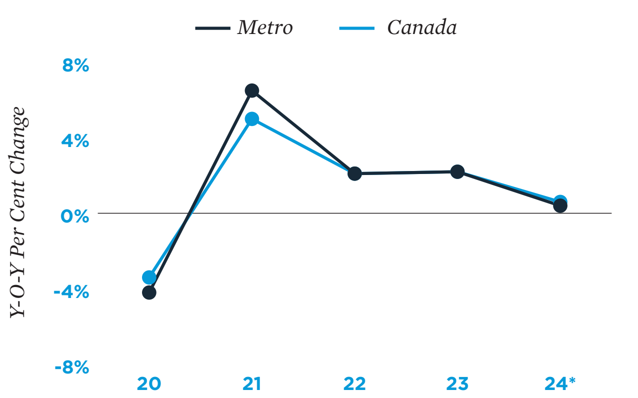
2Q/24

Further Expansion in Manufacturing Sector Partially Offsets Historic Supply Growth

Vacancy rate drifting higher as demand normalizes. Consistent with the national trend, the industrial vacancy rate in Southwestern Ontario is currently on an upward trajectory. A historic amount of new supply is taking longer to be absorbed, due to a slowdown in space demand caused by elevated interest rates. Softening demand, along with ongoing supply growth, is expected to persist for the remainder of the year, likely pushing the vacancy rate above 3.0 per cent. However, this factor will open up more opportunities for future tenants, who previously struggled to find available space when vacancy rates dropped below 1.0 per cent between 2021 and mid-2023. With rents roughly 30 per cent below that in Toronto, the metro also offers lower-cost options to those who have been priced out of the GTA market.

EV manufacturing driving long-term demand. The ongoing near-shoring of supply chains and the development of advanced manufacturing in Ontario continues to fuel industrial space demand in the metro. Following plans by Stellantis and Volkswagen to build EV battery manufacturing plants, other manufacturers, including Bobaek, DS Actimo, and Kautex Textron, have also announced investments in the region. The metro's appeal acts as a framework for the EV sector's expansion in other parts of Ontario as well. Honda is set to build an EV battery plant near its manufacturing facility in Alliston, while Umicore is also building a battery materials production plant in Loyalist. This EV expansion within the region is likely to create clustering effects, supporting robust employment growth, as well as long-term demand for both manufacturing and distribution space.

Employment Trends



** Forecast*

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

Industrial 2024 Outlook

6,000 JOBS *will be created*

EMPLOYMENT:

Job creation is projected to decelerate notably as elevated interest rates slow hiring activity. However, the metro's expanding population and diversifying economy will help maintain positive growth in total employment.

5.0 MILLION SQ. FT. *will be completed*

CONSTRUCTION:

After a record year of new construction in 2023, completions are expected to continue rising this year. Developers have significantly increased building intentions due to substantial demand growth, which will cause new supply to reach new highs in 2024.

160 BASIS POINT *increase in vacancy*

VACANCY:

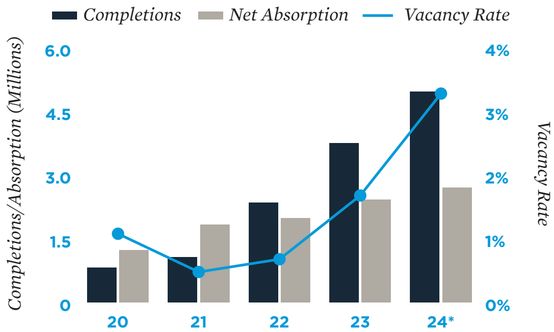
Elevated completions and softening pre-leasing activity will lead to higher vacancy in 2024. Tenants can expect to see more openings as the year progresses, with vacancy estimated to exceed 3.0 per cent by year-end.

4.2% INCREASE *in asking rent*

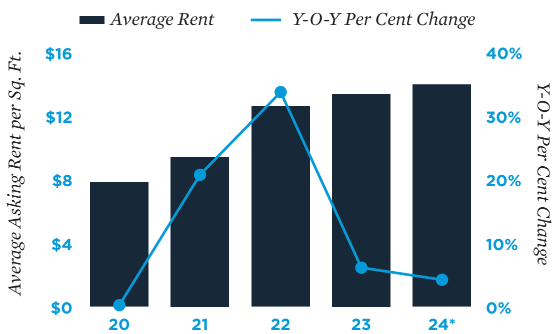
RENT:

Industrial rents will remain on an upward trajectory, but the rate of increase is expected to trend lower after double-digit percentage increases recorded in recent years. The average asking rent is expected to end 2024 just below $14 per square foot.

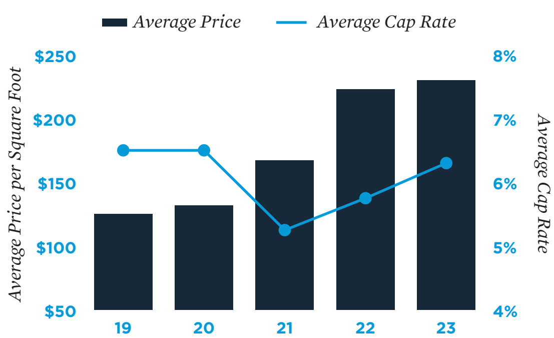
Supply and Demand



Rent Trends



Sales Trends



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Price: $250

1Q 2024: Trailing-12-Month Period

CONSTRUCTION

4,712,000 sq. ft. completed

- Led by elevated levels of completion in the final quarter of 2023 and the first quarter of 2024, the 12-month new construction rose by over 3 million square feet, which is equivalent to a 190 per cent annual increase.
- Cambridge saw the most completions, totaling 2.2 million square feet, followed by Hamilton and Kitchener, each with 1 million square feet delivered.

VACANCY

190 basis point increase in vacancy Y-O-Y

- Driven by an acceleration of new supply growth, the vacancy rate has been trending upward since the third quarter of 2023, reaching just below 3.0 per cent in the first quarter of 2024.
- Despite this overall increase in vacancy, Waterloo and Stratford saw near-full occupancy rates, while vacancy declined in Guelph.

RENT

8.5% increase in the average asking rent Y-O-Y

- Healthy space demand kept industrial rents on an upward trajectory. The rate of increase, however, has decelerated significantly, down from 39 per cent year-over-year seen in late 2022.
- The highest annual rent growth of 34 per cent was observed in St. Catharines, followed by 22 per cent in Brantford and 14 per cent in Guelph.

Investment Highlights

- Total dollar volume dropped by 20 per cent in 2023 as elevated interest rates hindered transaction activity. Despite this overall decrease, total sales registered a 45 per cent year-over-year increase in the fourth quarter, potentially signaling improving investor confidence. Moreover, demand tailwinds stemming from supply chain onshoring and substantial development in e-commerce continued to support fundamentals, which kept total investment well above the pre-pandemic average.
- Cambridge, Hamilton and Kitchener maintained their positions as the top three most invested regions in 2023. Sales in Kitchener also bucked the regional trend, with total dollar volume rising by 14 per cent last year. In addition, investors turned their attention to the growth potential of the Niagara region's manufacturing sector. Total dollar volume rose more than 30 times in Grimsby, fueled by a significant rise in medium- and large-size deals.
- The average sale price stagnated in 2023 due to lower buyer demand, registering just a 3 per cent increase. With the average price 23 per cent below the national average, Southwestern Ontario remained one of the least costly industrial markets for investors. Driven by rising interest rates and relatively stable prices, the metro's average cap rate rose by approximately 50 basis points and sat just above 6.0 per cent last year.