RESEARCH BRIEF
CANADA INDUSTRIAL

IPA INSTITUTIONAL PROPERTY ADVISORS
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JANUARY 2025

Manufacturing Sector Poised for Strong 2024 Finish Amid Looming Trade Tensions

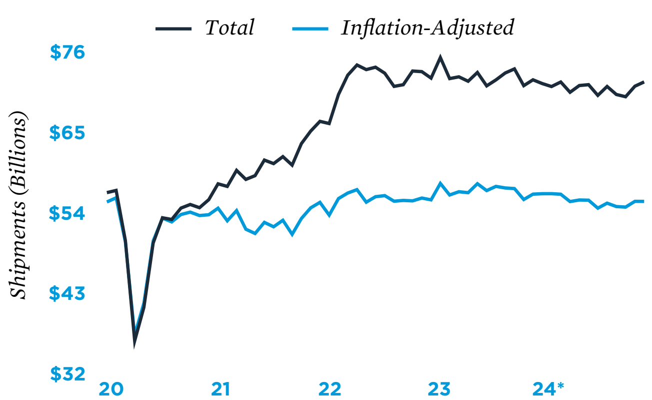
Manufacturing sales expanded in November. Sales of manufactured goods rose by 0.8 per cent month over month in November, driven by a 9.3 per cent increase in sales of aerospace products and parts and a 2.6 per cent gain in petroleum and coal product sales. When adjusted for inflation using the Industrial Product Price Index, however – which rose by 0.6 per cent – sales volume remained unchanged, indicating little to no growth in November's real GDP. Nevertheless, new orders climbed in both nominal and real terms, likely spurred by a weaker Canadian dollar and early purchases from U.S. buyers anticipating potential tariffs. With total inventory rising at a slower pace relative to total sales, the inventory-to-sales ratio declined to its lowest level since September 2023. As Canada's economy continues to perform below potential, this downward trend suggests that businesses have probably become more cautious about building up inventory due to uncertainty around future sales.

Central Bank expected to stay dovish. In response to the announcement of a potential 25 per cent tariff on Canadian exports to the U.S., export orders might be seeing a temporary surge, driving an increase in manufacturing sales in December. This may have introduced a short-term uptick in manufacturing output in 2024's final quarter. The tariff threat is expected to weigh on business investment regardless, however, and ultimately dampen trade volumes once implemented. This potential headwind will keep the Bank of Canada on its easing path, with the possibility of more proactive policy measures dependent on how trade relations with the U.S. evolve.

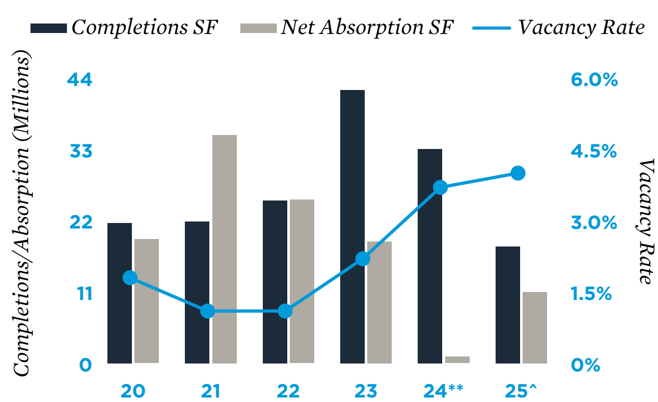
External shock could impact industrial sector outlook. The anticipated uptick in manufacturing GDP in the fourth quarter of 2024 likely coincided with a surge in industrial space demand, which pushed net absorption over 8 million square feet in the final three months of last year. Early estimates for January are showing absorption slipping back into negative territory, though, indicating that the sector's rebalancing is ongoing. Looking ahead, space demand is poised to stay soft until lower interest rates stimulate consumer spending and business investment. The vacancy rate is projected to rise further as a result, landing in the 4.0 per cent to 4.5 per cent range to end 2025. Trade tensions pose a major risk to the outlook, as industrial-intensive sectors are expected to bear the brunt of the potential tariff impact. This could prolong the rebalancing process in the industrial sector and push the vacancy rate to a higher level.

Positive long-term outlook intact. Investment activity improved last year on the heels of falling interest rates, particularly in the segment of properties valued under $20 million. With the vacancy rate likely to peak this year and interest rates expected to decline further, larger projects will become easier to finance, which may entice sidelined capital to reenter the market. Trade tensions will be the primary risk investors monitor, as it could delay a broad-based recovery in property sales. Still, long-term industrial prospects remain positive. Supported by a larger consumer base, nearshoring, industry diversification and increased energy production capacity, the outlook bodes well for investors seeking long-term returns.

Manufacturing Sales Rose with Risks Ahead



Industrial Supply and Demand



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* Through November; ** Estimate; ^ Forecast
Sources: IPA Research Services; Altus Data Solutions; Capital Economics; Statistics Canada