RESEARCH BRIEF
CANADA RETAIL SALES

IPA INSTITUTIONAL PROPERTY ADVISORS
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Select Property Types Could Outperform Amid Softening Consumer Confidence

Economic uncertainty weighing on spending outlook. Household consumption was on the rise heading into 2024. Once the Bank of Canada began its monetary easing cycle, retail sales started trending up, jumping 6.0 per cent between June and December. This was highlighted by the 5.6 per cent annualized surge in consumption growth last quarter. At the same time, historic population gains also fuelled a 26 per cent increase in retail sales between 2021 and 2024, aiding the broader sector despite a restrictive interest rate environment. Looking ahead, however, ongoing trade disputes and economic uncertainties are beginning to hurt consumer confidence. The Bank of Canada's recent consumer survey showed that households are raising precautionary savings. Consequently, total retail sales fell 0.6 per cent monthly in January, which, after accounting for inflation, translated into a 1.1 per cent drop. Preliminary nominal sales estimates for February point to a further decline of 0.4 per cent.

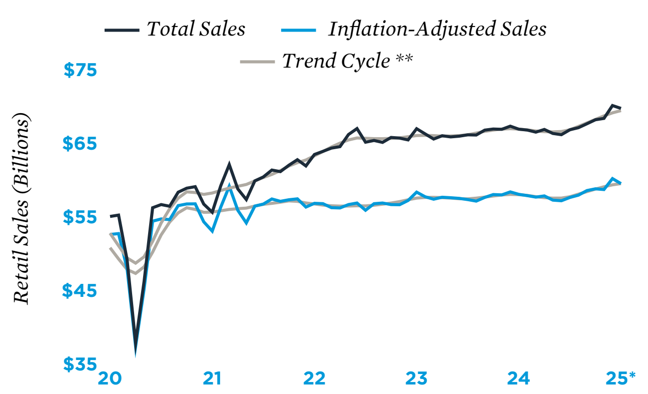
Further room for additional easing. While the central bank may pause its rate cutting cycle in April, weakening economic conditions leave room for this to be a temporary hold. With preliminary indicators for February suggesting softening retail sales, annualized consumption is likely to ease to sub-2.0 per cent in the first quarter, with some major banks penciling an outright contraction in the following quarters. Since consumption is the largest share of GDP, economic growth could stall if tariff uncertainties linger for an extended period of time. As a result, additional rate cuts are likely, with terminal rate forecasts ranging from 1.75 per cent to 2.50 per cent.

Commercial Real Estate Outlook

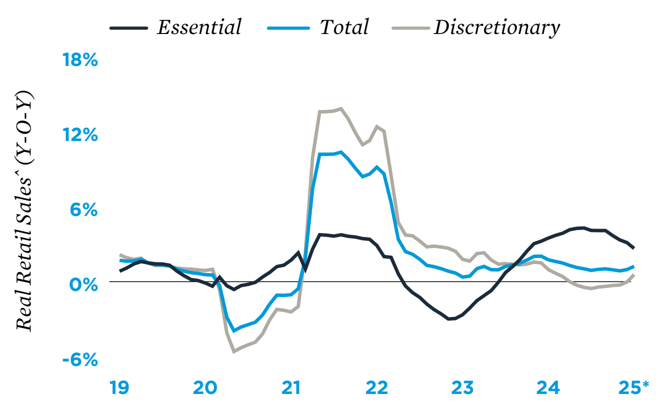
Industrial faces challenges, but also offers opportunities. The industrial sector has undergone a rebalancing since early 2022, with vacancy rising 250 basis points to 3.5 per cent as of the end of 2024. The impact of elevated interest rates curbing both business and consumer spending, in addition to historic supply growth, pushed vacancy up and has largely stabilized asking rents. While a climbing share of e-commerce in total retail sales may help industrial assets, as online spending went up 12 per cent year over year in January, the property type is also the most exposed to tariffs. This could push vacancy higher than originally forecasted. Nevertheless, trade headwinds present opportunities. Not only are some firms stockpiling inventory in the short term, but there are also discussions around the removal of interprovincial trade barriers, nearshoring and massive energy investment. Though these policies will take time, they present opportunities for industrial investors with a long-term strategy.

Stable retail attracts investors. While discretionary spending has picked up in recent months due to lower interest rates, non-discretionary spending tends to outperform in uncertain times. This was seen over the past two years, where essential spending gained momentum in early 2023 amid inflation and elevated interest rates. With tariffs clouding Canada's economic outlook and deteriorating consumer confidence, these more essential-based products will likely continue to capture redirected spending. As a result, necessity-based, grocery-anchored strip and neighbourhood centres will keep generating positive investor sentiment amid lower borrowing costs.

Retail Sales Show Strong Gains in Recent Years



Essential Spending Has Driven Sales



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** Through January; ** Smoothed seasonally adjusted time series; ^Trailing 12-month total*
Sources: IPA Research Services; Altus Data Solutions; Capital Economics; CoStar Group, Inc.; Desjardins Economics; RBC Economics; Statistics Canada; TD Economics