RESEARCH BRIEF
CANADA BUSINESS OUTLOOK SURVEY

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

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Confidence Rebounds, but Further Trade Progress Needed for Sustained Recovery

Business sentiment improves, but sales outlook stays weak. As of June, the worst-case tariff scenarios first anticipated by businesses looked less likely to appear, leading to a slight recovery in business sentiment in the Bank of Canada's Business Outlook Survey. Preferential treatment under the USMCA allowed tariff exemptions for the majority of surveyed firms – particularly exporters, who saw a more pronounced improvement in their outlook through June. Yet broader sales indicators weakened notably, reflecting growing concerns about a slowing economy stemming from the impact of tariffs. The Indicator of Future Sales (FSI) fell to a six-quarter low, reinforcing expectations that GDP growth slowed in the second quarter.

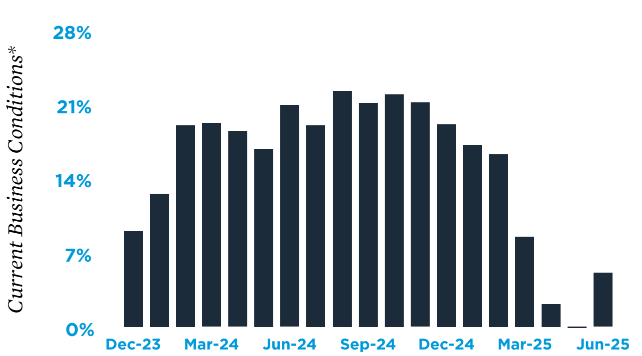
Firms' response points to fading risk of stagflation. While most firms reported they were not directly affected by tariffs, cost pressures stayed widespread due to tariff-related expenses, such as costs for sourcing alternative suppliers and developing new markets. Instead of raising prices, however, firms indicated that their primary strategies to cope with rising costs would be to reduce profit margins and find operational efficiencies. Meanwhile, businesses' expectations for wage growth over the coming year kept trending downwards, nearing pre-pandemic levels. These developments suggest that inflationary pressures will remain contained in the near term. Combined with a weaker sales outlook, this lowers the risk of stagflation and gives the Bank of Canada more flexibility to shift towards supporting a slowing economy through further interest rate cuts.

Commercial Real Estate Outlook

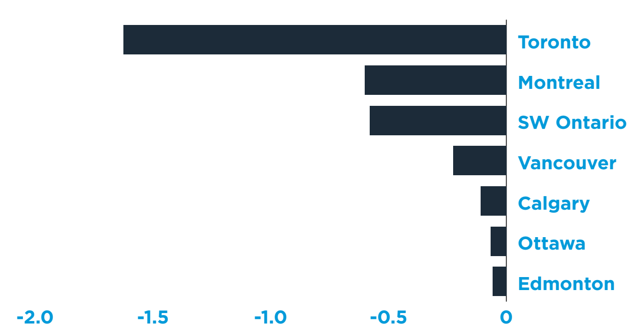
Industrial sector hinges on trade policy developments. While uncertainties have eased since April, subdued demand and ample existing capacity continue to weigh on business investment. In the second quarter, only 39 per cent of firms reported difficulty meeting unexpected increases in demand – below the historical average of 45 per cent. Investment plans were still primarily focused on maintaining existing capital rather than expanding capacity or improving productivity. This low investment intention is expected to keep translating into soft industrial space demand. Early quarter-to-date data shows that net absorption has stayed in negative territory in the third quarter, though Ontario and Quebec exhibit more pronounced weakness. The ongoing trade talks ahead of the August deadline will be a key development closely watched by businesses. A trade agreement with the U.S. – whether limited or comprehensive – would significantly reduce uncertainty, potentially paving the way for a recovery in the industrial sector. Conversely, if tariff threats persist, the sector is likely to remain under pressure for an extended period.

Retail holds firm on consumer strength. The latest consumer expectations survey indicates a sharp decline in consumer confidence in the second quarter. RBC's Consumer Spending Tracker, however, indicates that cardholder spending rose by 2.6 per cent on a quarterly basis. This resilience in actual consumer spending likely reflects improved household financial health entering 2025, as well as continued job creation in Canada's labour market year to date. As a result, the retail sector is expected to remain resilient this year. The vacancy rate will likely end 2025 below 2.0 per cent.

Business Conditions Have Improved



Tariff-Exposed Regions See Weaker Demand



Quarter-to-Date 3Q25 Industrial Net Absorption (Millions of Sq. Ft.)

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** Percentage of firms reporting positive sentiment minus the percentage reporting negative sentiment*
Sources: IPA Research Services; Altus Data Solutions; Bank of Canada; RBC