NATIONAL REPORT
CANADA INDUSTRIAL

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

3Q/25

Tariff Headwinds Clash With Interest Rate-Driven Tailwinds

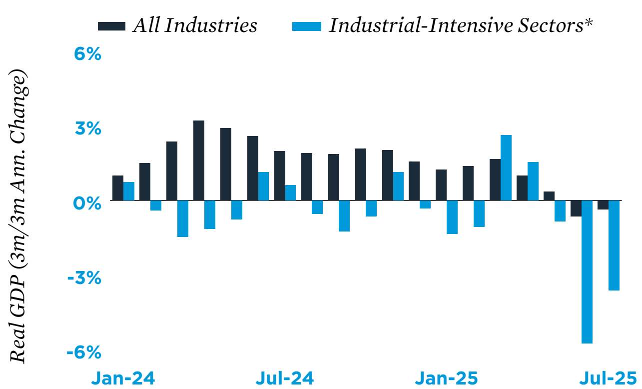
Fundamentals affected by trade policy shifts. While most of Canada's exports have been exempt from import duties under USMCA, higher tariffs on non-exempt goods – such as aluminum, steel, copper and pharmaceuticals – in addition to lingering uncertainty from stalled trade negotiations, have weighed on Canada's economic growth. The impact has been particularly pronounced in the manufacturing, transportation, warehousing and wholesale industries, which has in turn weighed on industrial property performance. Demand for space continued to be weak, with net absorption remaining negative in the third quarter. Although trade policy will stay a key determinant of the sector's near-term outlook, lower interest rates could stimulate domestic consumption and support space demand.

Space demand recovering gradually. With no trade deal reached before the Aug. 1 deadline, the U.S. has raised tariffs on non-USMCA-compliant Canadian goods to 35 per cent and imposed an additional 50 per cent duty on all copper products. This escalation dampened earlier expectations for a swift rebound in space demand. As a result, net absorption remained negative in the third quarter following a 3.2 million-square-foot contraction in the second quarter. That said, the decline appears to be narrowing. Modest improvements in Alberta and British Columbia could be precursors to recovery. These could also potentially carry through year-end, supported by lower interest rates. Even so, persistent trade policy uncertainty will continue to be a key headwind for industrial space demand.

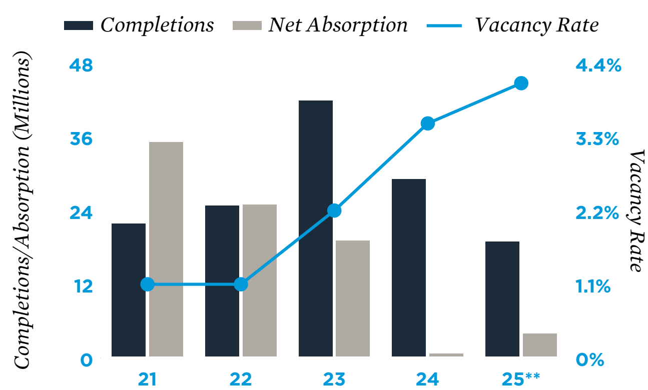
Ontario and Quebec most exposed to trade headwinds. Home to Canada's key manufacturing hubs for motor vehicles and aluminum products, and with supply chains deeply integrated with the U.S., Ontario and Quebec have borne the brunt of the ongoing trade dispute. Between the second and third quarters, 3.6 million square feet of space was vacated across Toronto, Ottawa, Southwestern Ontario and Montreal — a drop noticeable at the national level. Although large-scale job losses in trade-independent sectors have yet to emerge, businesses, especially third-party logistics providers, are still cautious about expanding under current conditions. Looking ahead, Ontario and Quebec's fundamentals will be shaped most directly by future trade policy developments, while British Columbia and Alberta are poised to benefit sooner from lower interest rates.

Rents declining amid rising vacancy rates. With construction slowing across all major metros, total completions are projected to decline for a second straight year in 2025. Of the 19 million square feet slated for delivery, 13 million will come from Toronto and Vancouver. This restrained pipeline should help cap vacancy rates despite ongoing pressure on space demand. After a year of slowing rent growth, average marketed rates continue to soften. Already, Toronto, Vancouver, Montreal and Southwestern Ontario are posting annual declines. As a result, the national average has effectively flatlined year to date and is forecast to record its first annual decrease by the fourth quarter amid rising vacancy rates.

Growth in Industrial Sectors Plummeted

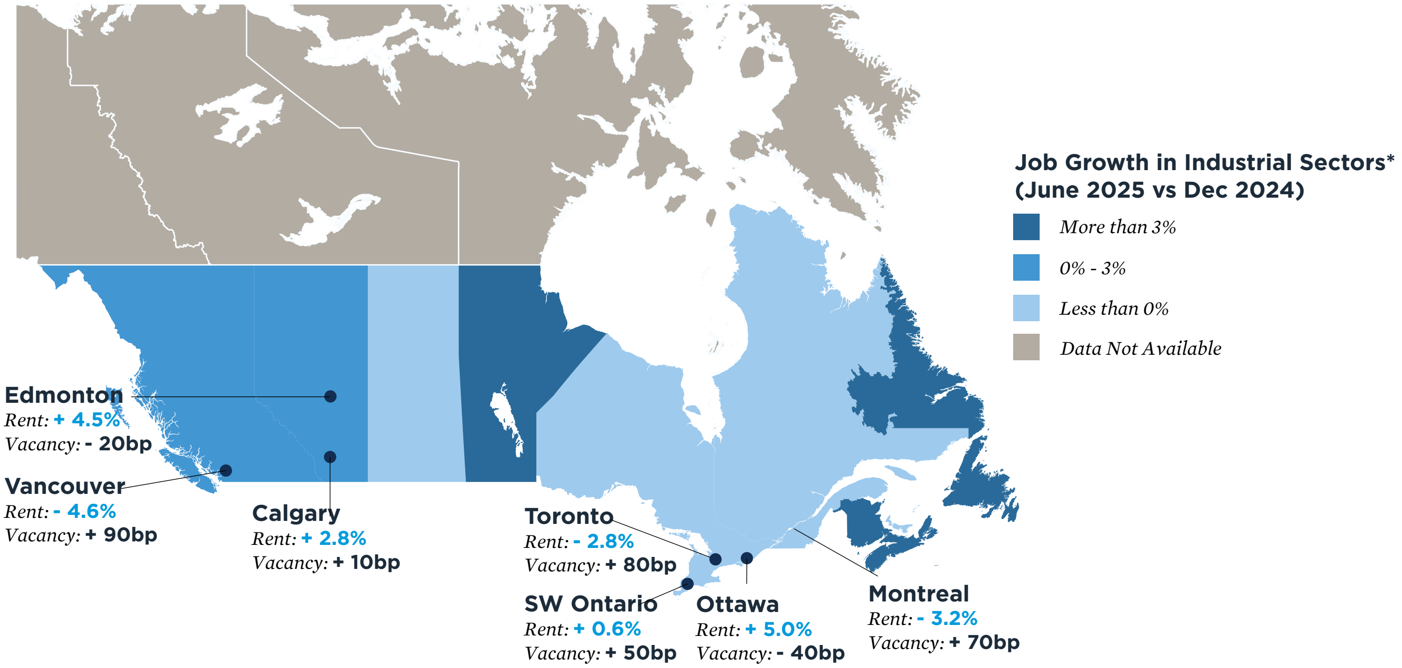


Industrial Supply and Demand



* Includes transportation, warehousing, manufacturing and wholesale sectors;
** Forecasts
Sources: Altus Data Solutions; Statistics Canada

2025 Metro Forecasts



** Includes transportation, warehousing, manufacturing and wholesale sectors*
Sources: Altus Data Solutions; Statistics Canada

WESTERN CANADA

- **Calgary, Alberta:** Calgary's industrial market has remained resilient in 2025 despite trade tensions and slower population growth. Lower interest rates are expected to support activity through year-end, while limited new supply will help contain vacancies. Over the longer term, the city's new Industrial Action Plan – focused on land supply, infrastructure, and development incentives – aims to attract investment, boost competitiveness and drive future construction and economic growth.

- **Edmonton, Alberta:** Vacancy eased in the third quarter after rising briefly in the first half. Population growth, lower interest rates and rising energy production are expected to keep absorption ahead of completions through year-end. Space demand has been led by small-bay spaces with the Nisku-Leduc submarket seeing particularly strong absorption and a sharp drop in vacancy.

- **Vancouver, British Columbia:** While space demand has shown signs of stabilizing, leasing remains concentrated in smaller properties, with larger commitments on hold amid trade policy uncertainty. Elevated completions are adding further pressure, with 3 million square feet expected this year pushing vacancy to 3.5 per cent by the final quarter. Beyond 2025, a slowdown in new supply should help ease the drag on fundamentals.

EASTERN CANADA

- **Montreal, Québec:** Prolonged trade disruptions have pushed vacancy above 5.0 per cent, with 2.8 million square feet vacated so far this year. Meanwhile, construction activity is ramping up, with 4.5 million square feet underway that will add to future completions.

- **Ottawa, Ontario:** Amazon's new distribution facility signals confidence in the metro's logistics positioning, highlighting strong demand for large-format space and e-commerce-driven absorption. Disciplined development is keeping vacancy low and rents rising, making the metro a stable and resilient industrial hub.

- **Southwestern Ontario:** Southwestern Ontario's industrial market remains resilient, with positive absorption supported by healthy hiring and population inflows. Long-term growth is expected from a diversified economy, migration trends, as well as expansion in electric vehicle and battery production.

- **Toronto, Ontario:** Small-bay industrial assets are outperforming larger warehouses, driven by scarcity, faster leasing and resilient local tenant demand. Limited new development and insulation from trade-sensitive sectors make small-bay properties a defensive, growth-oriented segment, while large-bay facilities face higher vacancy and slower absorption amid cross-border trade risks.

2025 National Forecast

EMPLOYMENT

0.2% increase Y-O-Y

- Total employment is expected to increase only marginally in 2025, as prolonged trade tensions weigh on job growth. Trade-dependent metros, such as Montreal and Toronto, are projected to see contractions.

CONSTRUCTION

19 million square feet completed

- Completions are expected to drop to their lowest level since 2019. Clear guidance on trade policy will be crucial to rebuilding developer confidence and restarting project pipelines.

VACANCY

60 basis point increase Y-O-Y

- Amid trade disruptions, weakening space demand is expected to push the vacancy rate to 4.1 per cent by year-end. Toronto, Montreal and Vancouver will account for the bulk of this increase.

ASKING RENT

1.7% decrease Y-O-Y

- After remaining flat through mid-2025, the national average asking rent began to decline in the third quarter. This trend is expected to continue through year-end as the vacancy rate climbs.

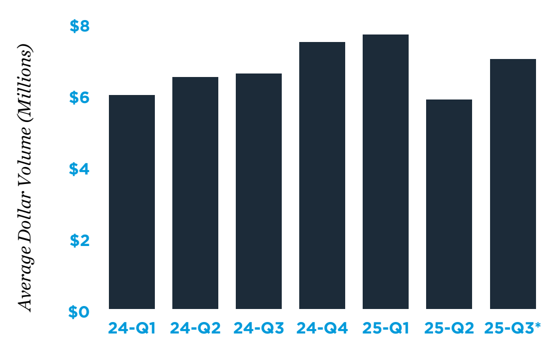
Investment Outlook

- **Investors shift to smaller assets amid trade risks.** Total dollar volume fell 20 per cent in the second quarter compared with the first quarter, while the number of transactions increased 5 per cent. This caused the average dollar volume per transaction to fall to just $5.9 million, indicating investors adopted a defensive stance, favouring smaller properties. These assets are typically multi-tenanted and occupied mainly by local distributors and wholesalers, providing some insulation from global trade disruptions.

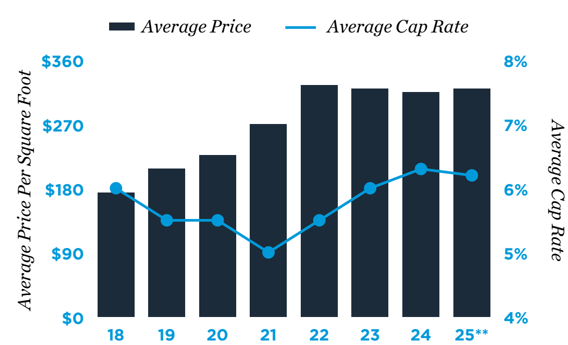
- **Caution and resilience reshape near-term industrial investment**. As long as trade tensions persist, investors will likely continue favouring smaller, lower-risk properties that offer stable cash flow and quicker turnover. Larger industrial assets, especially those linked to cross-border logistics or export-oriented sectors, are experiencing slower absorption and higher vacancy. While lower interest rates could eventually spur leasing activity for large-bay facilities, a cautious approach is likely to remain a defining feature of investment behaviour.

- **Gain in sale prices could continue amid declining interest rates.** The average sale price increased slightly in the second quarter compared with the level in 2024, supported by gains across most metros. In Vancouver and Southwestern Ontario, however, prices declined due to cooling investment activity. Looking ahead, valuations could see additional upside from lower interest rates, which will put downward pressure on cap rates.

Dollar Volume Per Transaction Trend



Industrial Investment Sales Trends



** Preliminary estimate; ** Trailing 12-month through 2Q*

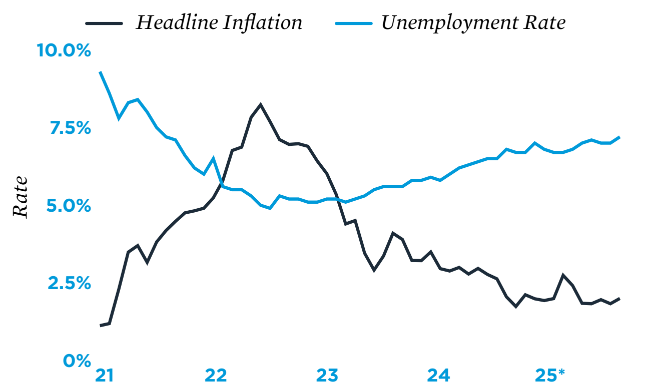
Sources: Altus Data Solutions; Statistics Canada

Long-Term Financing Costs to Head Lower as Central Banks Stay on Easing Path

Bank of Canada expected to maintain dovish stance. As widely anticipated, the BoC reduced its overnight rate by 25 basis points to 2.5 per cent at the September policy meeting. Since July, Canada's labour market has shown signs of softening, with nearly 110,000 jobs lost between then and August, pushing the unemployment rate to 7.1 per cent. On the inflation front, recent data indicate that upward price pressures have moderated, even amid higher costs linked to trade disruptions. Meanwhile, the removal of most retaliatory tariffs on U.S. goods has eased the risk of future inflation. Taken together, these factors shifted the balance of economic risks and prompted the BoC to resume rate cuts following its pause since March. While the bank offered limited forward guidance on policy actions for the remainder of 2025, a weakening economy is likely to strengthen the case for additional rate cuts. For the remainder of the year, most Canadian exports will likely continue to benefit from tariff-free treatment under USMCA, but the August tariff hike on non-USMCA-compliant goods and stalled trade negotiations have done little to reduce uncertainty, This will be the major headwind for business investment, and the resulting drag on economic growth could prompt further support from the central bank.

Parallel rate reductions across the border to ease borrowing costs. Alongside Canada's rate reductions, the U.S. Federal Reserve also cut interest rates at its September policy meeting, with projections indicating the possibility of two additional cuts before year-end. If these reductions materialize in both countries, borrowing costs for long-term capital – particularly 5- and 10-year financing, which are commonly used by commercial real estate buyers – could decline meaningfully. Lower financing costs would likely stimulate consumer spending, bolstering demand for industrial space, while also unlocking capital that has remained on the sidelines. This influx of available capital could support new development, acquisitions and refinancing activity, providing a boost to market liquidity and investment confidence.

Current Conditions Support Further Rate Cuts



Long-Term Rates Down from July Peak

** Through August; ** Through September 24*

Sources: Altus Data Solutions; Bank of Canada, Statistics Canada

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