Greater Montreal **Investment Insights Report**

Colliers Canada | Spring – Summer 2022

Accelerating success.

Greater Montreal **Investment Insights Report** Spring – Summer 2022

Investment Activity

Investment activity in the first half of 2022 remained stable, as steps are taken to mitigate the anticipated economic fallout caused by the onset of recent inflationary pressures. While concerns over the pandemic are subsiding in most major markets, its lasting impact on the commodities market continues to expose supply-chain issues. The imbalance between supply and demand is still being tested in retail and warehousing sectors as e-commerce trends intensified and Quebec import volumes rebounded in 2021. Meanwhile, an oversaturation of residential buyers threatens to reduce vacancies amidst worries that the development pipeline could face obstacles ranging from higher construction costs to inclusionary zoning.

Furthermore, the Bank of Canada (BoC) is now faced with correcting the rapid rise of domestic inflation by introducing a series of interest rate hikes over the next year or so. The latest numbers show that inflation moved a full percentage point past February's 31-year record of 5.7% to 6.8%. The Big 6 are forecasting the target rate to sit somewhere between 2.00% to 2.50% by year-end.

How these corrective measures impact the Canadian commercial real estate market is favorable for cash buyers, but less so for owners with low debt-service coverage and destabilized cash flow. In the short-term, the outlook on the Canadian economy shows a willingness to maintain resiliency through historic lows in unemployment and persistent capital investments.

Market Watch

BoC increase in policy rates

Labour shortage

Rising construction costs

Cap rate decompression

Investor Confidence in Office Assets Renewed by Major Institutional Players

Investor risk appetite in the Greater Montreal Area shifted on the side of private buyers for the first time since early 2019, as a considerable number of properties exchanged hands during the first half of year. Canderel led a consortium of investors through a complex acquisition of Cominar REIT's commercial portfolio in early March. The $5.7-billion transaction resulted in the transfer of several office and retail assets acquired by Groupe Mach, a Quebec-based private firm. Blackstone's portfolio company, Pure Industrial, took control of 190 industrial properties across Montreal, Quebec City, and Ottawa.

Investment activity is picking up in the office sector, as major buyers made significant moves to acquire key properties. Gaming manufacturer, NetEase, purchased the home of Microsoft's AI Research Hub in the Mile-Ex for $51 million in early March. Meanwhile, Blackstone moved to acquire 1100 Atwater and the Air Canada Tower in a $230-million transaction, thereby strengthening their partnership with

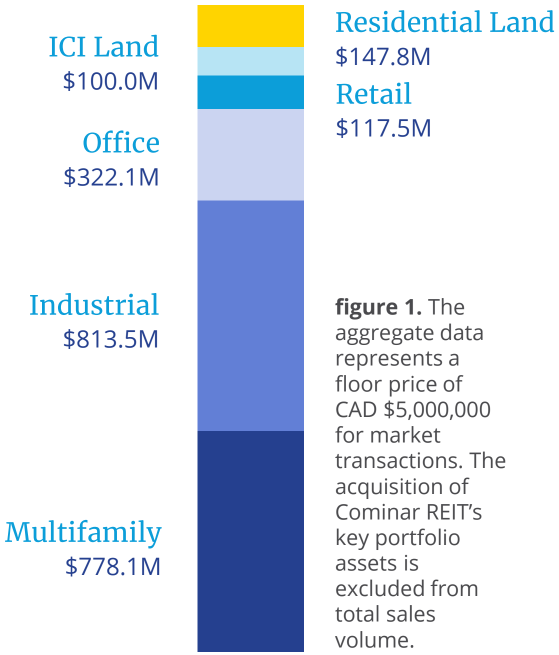

figure 1. The aggregate data represents a floor price of CAD $5,000,000 for market transactions. The acquisition of Cominar REIT's key portfolio assets is excluded from total sales volume.

Source: Colliers Canada Research, Institut de la statistique du Québec, Altus Data Studio, May 2022

Kevric and further enhancing their Canadian presence. Both properties held strong covenants and low vacancies at the time of sale.

Industrial remains a dominating force in the investment sphere as more than $800 million in commercial assets traded, year-to-date. However, the warehousing sector faces concerns over lingering supply-chain issues exacerbated by growing costs in construction and energy prices, as well as heightened demand for consumer goods. Quebec imports grew by as much as 15% in 2021 following a brief deficit in 2020 where signs of congestion created bottlenecks in the supply chain.

Multi-family investments have not shown signs of slowing down as volume traded climbed by more than 20% YoY. Centurion Apartment REIT bought the remaining stake of a 30-property apartment portfolio from Habitations Trigon at a 4.50% cap, making it the second largest residential landlord in Quebec. Centurion now has an additional 3,678 units in its residential portfolio. And although quarterly retail investment activity continues to fluctuate, there has been growing interest in nodes that are largely anchored by essential services. Year-over-year retail investment volume is down 33% year-to-date.

CAD $2.3B
Total Sales Volume

CAD $5.7B
Canderel-led Cominar Portfolio Transaction

CAD $147M
Notable Transaction | Air Canada Tower

Source: Colliers Canada Research, Institut de la statistique du Québec, Altus Data Studio, May 2022

"Investment activity remains relatively stable, with assets trading at nearly $2.3 billion YTD..."

Investors ramped up transactional activity in response to the Bank of Canada's recent decision to raise the overnight policy rate (OPR), as 2022 investment volumes remained on par with H1 averages from the last three years. Investment activity remains relatively stable, with assets trading at nearly $2.3 billion YTD, as demand for warehousing and distribution centers (DC) continued to be the primary driver of investment trends. Moreover, the industrial sector's supply and demand imbalance not only drove price per square foot values up by 34% YoY, but the impact of a sub-1% vacancy rate pushed net rents 40% higher YoY.

Although the office sector is slow to regain the momentum it had prior to the pandemic, investors are moving in to purchase best-in-class properties and diversify their holdings. Landlords have been reliant on an influx of users to reduce downtown vacancies over the next several months despite users' impulse to strategically right-size while bending to flexible work demands. Investment volumes tipped upwards for a fourth consecutive quarter, largely driven by investments made toward Class A office properties in both downtown and suburban markets.

Appetite for multi-family assets remains strong, following a 217% increase in YoY sales volume. A month-over-month analysis of the development pipeline in the GMA showed a steady growth in April 2022 housing starts, up 46.4% from the previous month to more than 34,000 units.

Source: Colliers Canada Research, Altus Group, CMHC, May 2022

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$373 PSF
Retail
Up 36.3% YoY

$446 PSF
Office
Up 27.8% YoY

$197 PSF
Industrial
Up 34.4% YoY

$182,381/Unit
Multi-Family
Up 44.5% YoY

Greater Montreal Sales Volume by Asset Class, 2017 – 2022 YTD

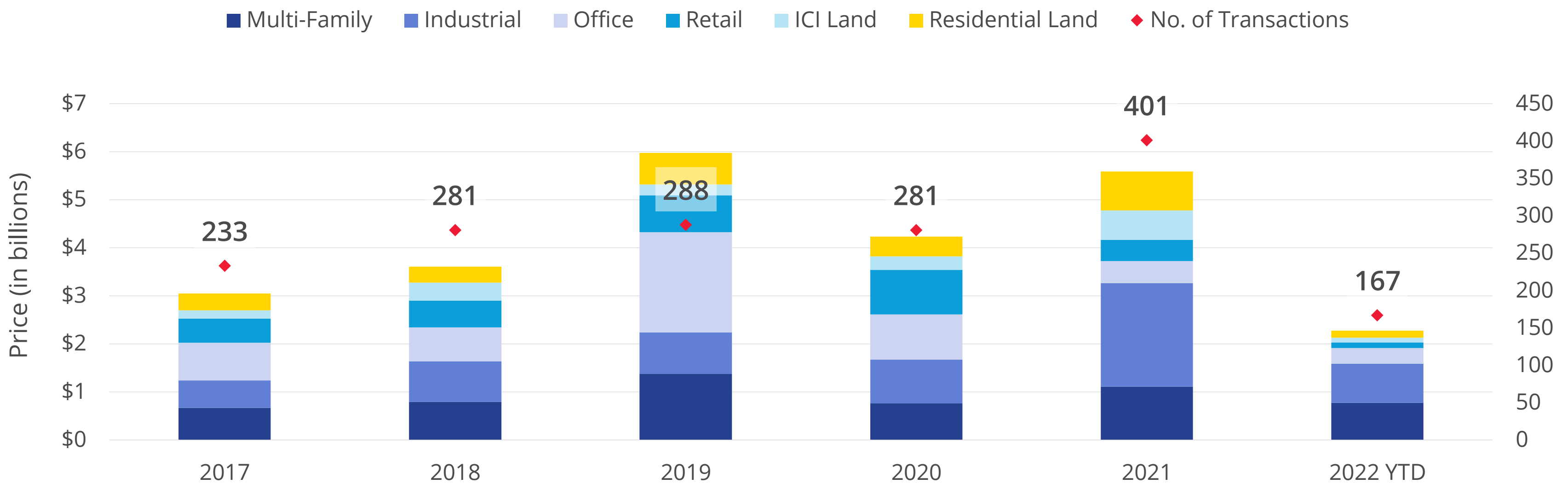

figure 2. The aggregate data represents a floor price of CAD $5,000,000 for market transactions.

Source: Colliers Canada Research, Altus Group, CMHC, May 2022

Industrial & Multi-Family Assets Appeal to Institutional Investors and Private Buyers

At the height of the pandemic, public health restrictions played a principal role in shifting consumer spending away from physical retail locations over to online stores. Between 2020 and 2022, institutional investors were keen on leveraging warehouses and DCs as part of a growing demand to accommodate last mile strategies and logistics needs fed by pent-up consumption. Although the Port of Montreal reported a decline of 3.09% in 2021 cumulative cargo volumes, 2022 inbound traffic in metric tons increased nearly 4% from the previous year. The effects of these pressures continue to weigh heavily on the city's diminishing supply of warehousing space.

In 2019, public investors made significant purchases on several aging multi-residential properties during a period of annual declines in available units. At the time, vacancy reached a 15-year low of 1.6%, due to a surge in on-island net migration, among other factors. More recently, public investors and REITs are increasingly leaning away from retail and industrial assets, while investing almost exclusively on rental properties in mainly tertiary markets like the South Shore.

Source: Colliers Canada Research, Altus Group, The Port of Montreal, May 2022

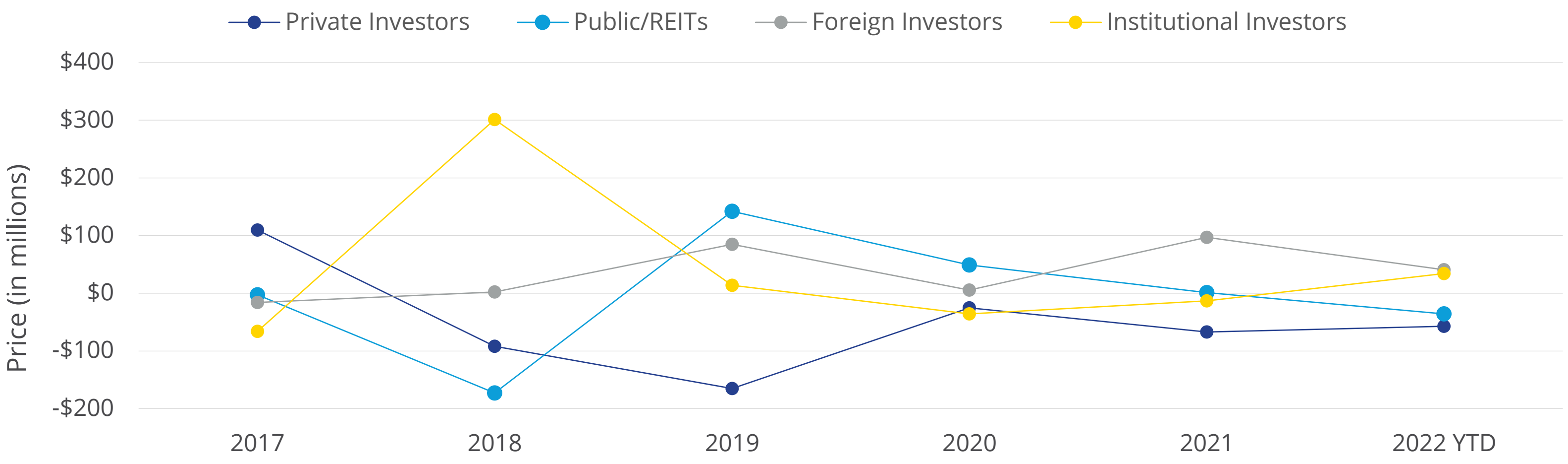

figure 3. Net Acquisitions Volumes by Investor Type, 2017 – 2022 YTD

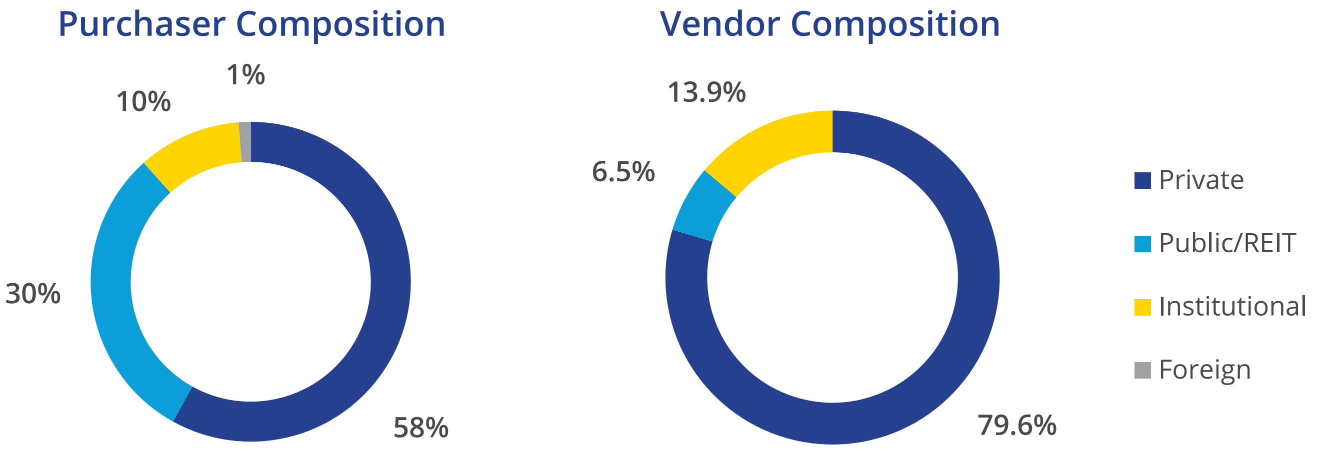

figure 4. Investor profile composition, 2022 YTD

Source: Colliers Canada Research, Altus Group, The Port of Montreal, May 2022

The Spread Begins to Narrow as Bank of Canada Tackles Inflation

The decompression of cap rates has yet to unfold as both the Canadian and Montreal Cap Rate averages remain at all-time lows of 5.33% and 5.02%, respectively. A large portion of transactions occurred in January and February as investors raced to close deals as the low interest economy comes to an end.

The first half of 2022 has had one word on the minds of investors: Inflation. The Bank of Canada kept rates low for too long and find themselves fighting inflation of 6.7% at all costs. Successive interest rate hikes seem to be the medicine. As it pertains to commercial real estate, the reasoning is that rising interest rates will prompt borrowers to dial back their investments to help mitigate the ballooning of valuations. The 10-year GoC bond increased to its highest level since 2017, up 43 basis-points (bps) YoY to 1.93%. As the gap between cap rates and bond yields tighten, we can expect a decompression of cap rates in the near-term future.

Source: Colliers Canada Research, Bank of Canada, May 2022

Montreal Cap Rate Spread to 10-Year GoC Bond Yields

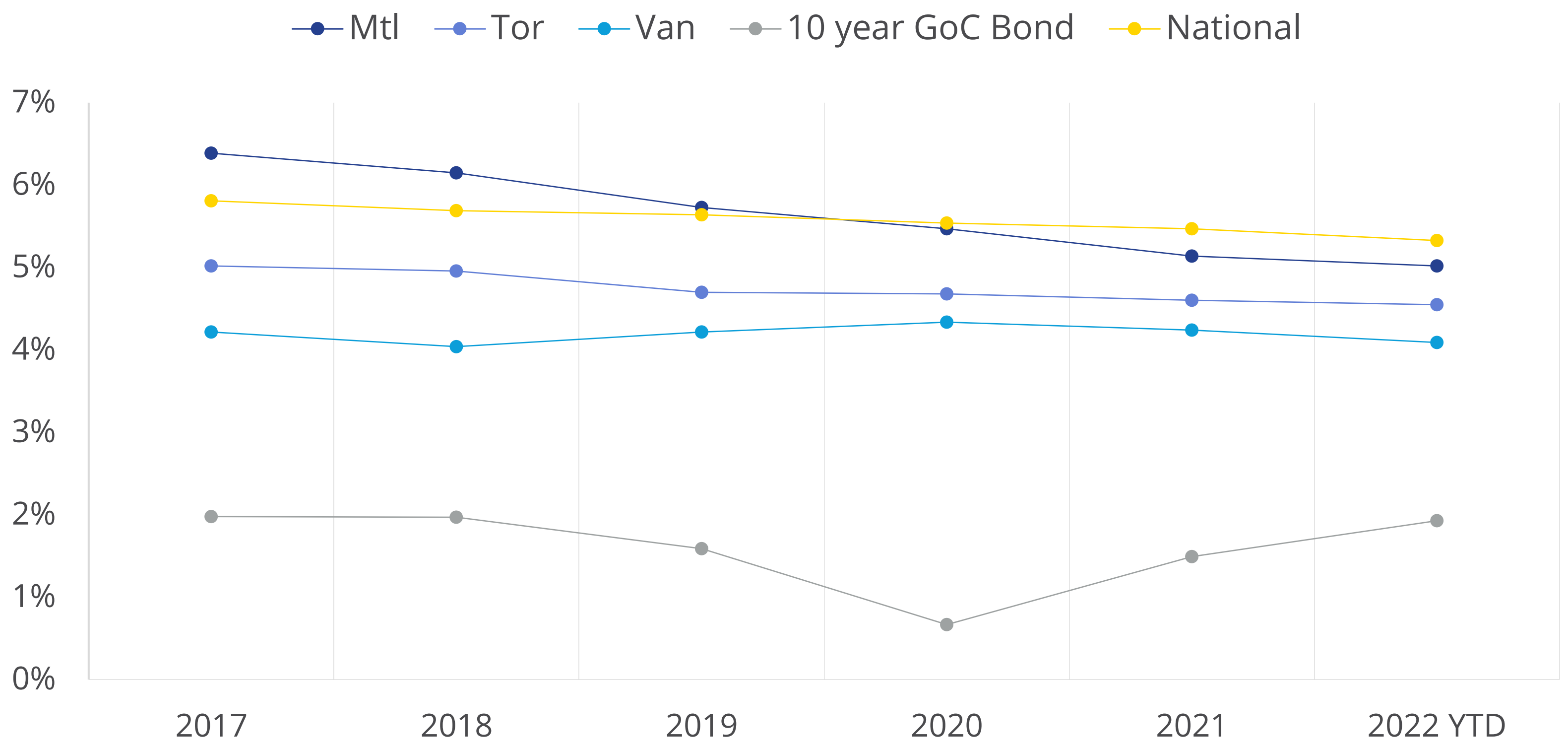

figure 5. Cap rate averages in Montreal are on par with National averages, but the spread has yet to expand.

Source: Colliers Canada Research, Bank of Canada, May 2022

"...interest rate hikes are retaining future homeowners in the rental market."

The industrial and multi-family markets continue to be the jewel for investors. Both asset classes have been facing similar supply and demand issues.

For industrial, the insatiable demand has put the average net asking rent to $11.77. Traditionally, Montreal's market rested between a $4-$6 range from 2015 to 2018. With no rental price ceiling in sight, the higher expected growth in NOI has meant investors are comfortable accepting lower cap rates with Class A industrial selling as low as 3.25%.

The successive interest rate hikes are retaining future homeowners in the rental market, leaving investors bullish on Montreal's multi-family rental growth prospects. High-Rise multi-family has traded for as low as a 3% cap rate.

The office and retail sectors had a slight uptick in activity mainly due to the Cominar deal. Office properties are expected to gain attraction as the return-to-office comes into effect. Retail properties have sold under two conditions. Firstly, investors continue to find value in grocery and pharmacy anchored assets with cap rates as low as 5%. Secondly, those properties with obsolete retail formats and higher vacancies have seen their highest-and-best use tested in exchange for the development of larger density multi-family, mixed-use, and transit-oriented developments.

Source: Colliers Canada Research, May 2022

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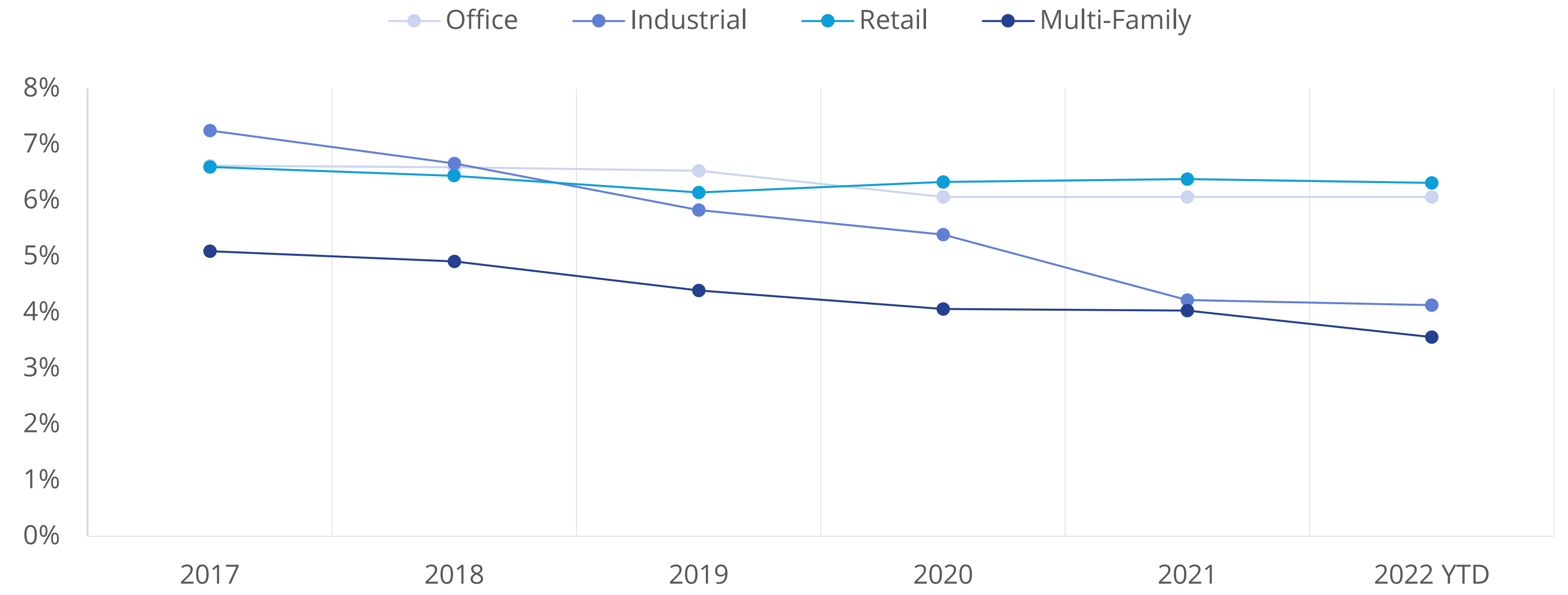


figure 6. Montreal's Historical Cap Rate Analysis by Asset Type, 2017 – 2022 YTD

3.56% Multi-Family	4.13% Industrial	6.06% Office	6.31% Retail

figure 7. Montreal Cap Rate Analysis by Asset Type.

Source: Colliers Canada Research, May 2022

Montreal Cap Rates High and Lows, H1 2022

Cap rates continue to trend downward as investors look to lock-in investments before multiple rate hikes limit purchasing power. Industrial and Multi-Family are the only asset classes reaching the low 3% range.

Downtown Office			
Class A		Class B	
Low	High	Low	High
4.50%	5.50%	5.25%	6.00%

Suburban Office			
Class A		Class B	
Low	High	Low	High
6.00%	7.00%	6.75%	7.50%

Industrial			
Single-tenant		Multi-tenant	
Low	High	Low	High
3.25%	4.50%	4.00%	4.75%

Multi-Family / Apartment			
High-rise		Low-rise	
Low	High	Low	High
3.00%	4.25%	3.00%	4.00%

Retail					
Regional / Power		Food Anchored Strips		Enclosed Community	
Low	High	Low	High	Low	High
5.25%	6.50%	5.00%	6.00%	6.50%	7.50%

Source: Colliers Canada Research, May 2022

Montreal Land Sales Off to Strong Start as Investments in ICI Land Gains Traction

2022 continued with the same insatiable demand for land with $412 million invested. $163 million, or 40%, of total volume went to ICI land whereas historically land deals skewed heavily towards residential. The industrial boom explains this shift as 64% of ICI volume pertained to industrial development, most notably in the South Shore with a 35% market share YTD.

Residential land has also centered towards the South Shore with a 50% market share. The most notable transaction was Devimco's purchase of a 355,000 square feet, or 8-acre lot, in Brossard for $55 million. 43% of transactions focused on areas with medium density zoning. The large concern for residential developers is the hard cost of construction as materials, labour, and fuel continue to increase.

Source: Colliers Canada Research, Altus Group, May 2022

Sales Volume Overview, 2017 – 2022 YTD

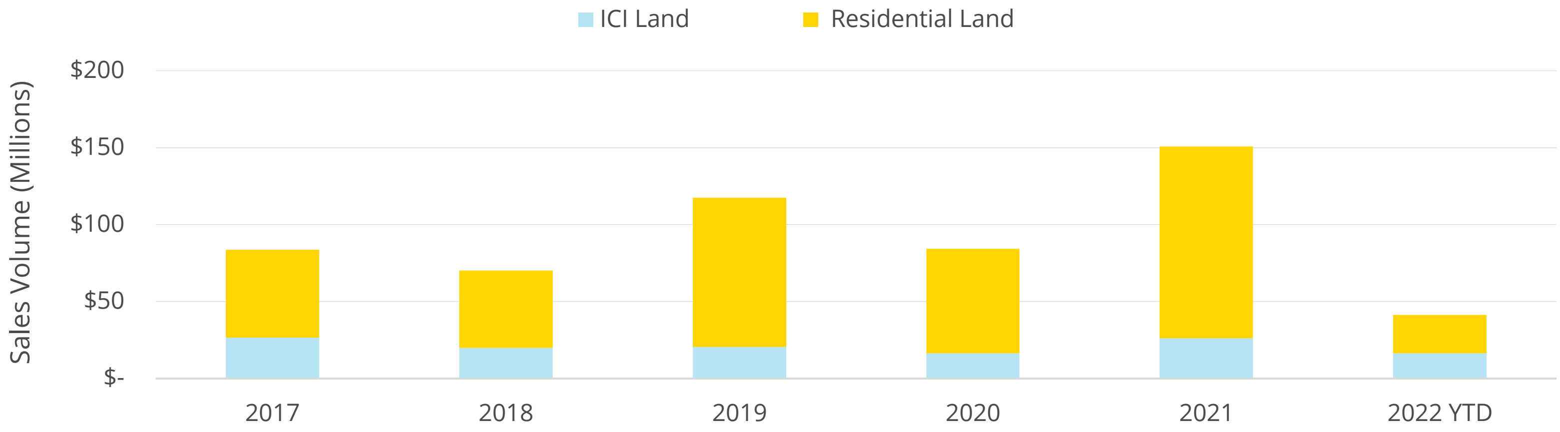
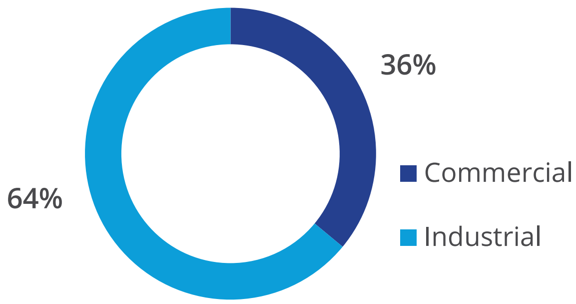


figure 8. Floor price for sales volume is at $1,000,000.

H1 2022 ICI Land Use Breakdown



H1 2022 Residential Land Use Breakdown

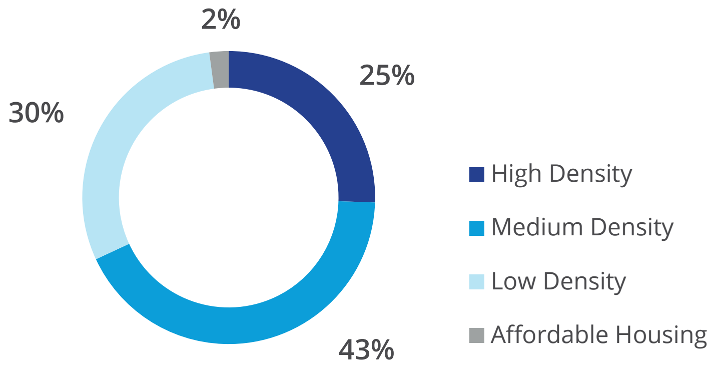


figure 9. Land Use Breakdown, H1 2022

Source: Colliers Canada Research, Altus Group, May 2022

Developers Look to Soften the Effects of Surging Construction Costs

Construction costs have been severely impacted by the global supply chain disruption. All asset classes saw a rise in cost year-over-year, most notably in the industrial development pipeline. Warehousing construction is up as much as 52%, or $55 a square foot. The average price per square foot is $150 for industrial properties at 150,000 square feet. Industrial builds of 250,000 square feet and above ranged from $125-$140. The second largest annual increase belongs to the multi-family builds between 13-39 storeys with a 10% increase, or $25 per square foot.

The continued appreciation of land valuations, in tandem with the constant rise of construction cost has made developers change how they purchase product with many having to place down deposits on steel and making larger orders in anticipation of future cost escalation.

Multi-Family / Apartment			
13-39 Storeys		40-60 Storeys	
Low	High	Low	High
$195	$250	$205	$265

Industrial	
Warehouse & Distribution	
Low	High
$125	$160

Source: Colliers Canada Research, Altus Group, May 2022

Retail					
Regional / Power		Food Anchored Strips		Enclosed Community	
Low	High	Low	High	Low	High
$220	$300	$150	$215	$115	$190

Office			
Class A 5-30 Storeys		Class A 31-60 Storeys	
Low	High	Low	High
$200	$285	$255	$375

Source: Colliers Canada Research, Altus Group, May 2022

Persistent Growth in Rental Rates Across Office and Industrial Properties

Throughout 2021 leading into 2022, both office and industrial properties were seeing similar patterns in rental growth. However, the uptick in industrial rental values was first observed as far back as 2018 when vacancies began declining as a result of growing logistics, warehousing, and manufacturing demands boosted by e-commerce activity. Since that period, net rental rates pushed further into the double-digits at a quarterly average of 13.5% to $11.77 per square foot in Q1 2022.

The office sector saw rates increase within the first few months of 2021 after the shift toward remote working was cemented into the work environment of numerous companies in tech, multimedia and other non-traditional industry sectors. Since Q1 2021, average net rent for offices in the GMA have rise by a quarterly average of 5.6%, now sitting at $19.57 per square foot.

The incremental supply of Class AAA and A downtown office availabilities, higher construction costs for move-in ready spaces, and additional amenities were key contributors in the gradual increase in face rates. Landlords seized an opportunity to offset the cost but raising face rates with the expectation that demand will pick up later in the year.

Source: Colliers Canada Research, May 2022

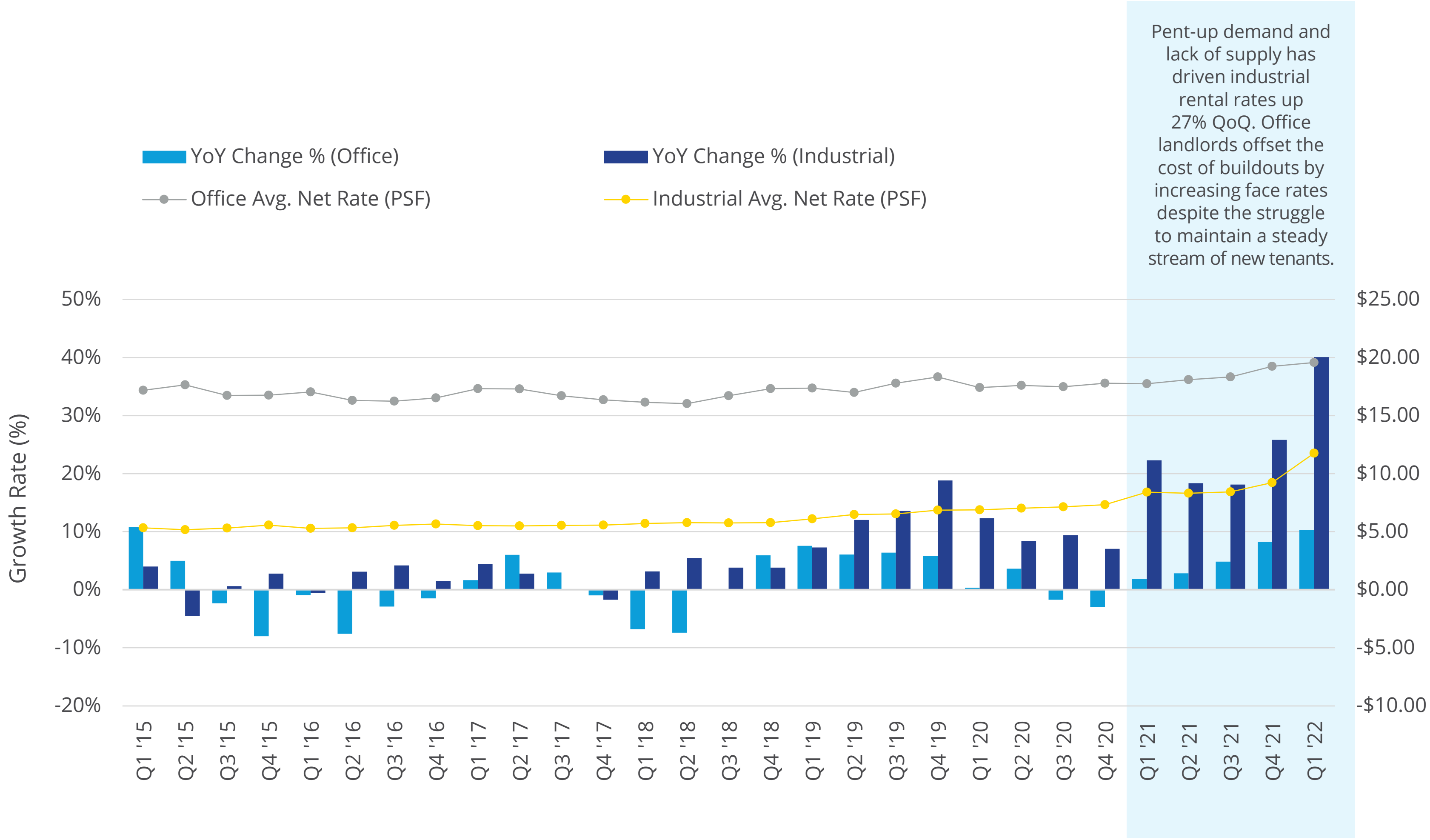


figure 10. Historical Rental Growth Rate, 2017 – 2022 YTD

Source: Colliers Canada Research, May 2022

Transaction Details

Address / Transaction Name	Transaction Date	Price	Price per SF / Unit	Type of Asset
7800 TransCanada Highway	February 2022	$95,661,500	$251 / SF	**Industrial**
1100 Atwater Avenue	March 2022	$84,000,000	$477 / SF	**Office**
1580 Eiffel Street	February 2022	$58,500,000	$314 / SF	**Industrial**
265 Hymus Boulevard	February 2022	$53,733,361	$398,321 / Unit	**Multi-Family**
50-90 Crépeau Street	March 2022	$51,000,000	$177,083 / Unit	**Multi-Family**
6795 Marconi Street	March 2022	$51,000,000	$486 / SF	**Office**
8550 Montview Road	January 2022	$42,000,000	$179 / SF	**Industrial**
3440 Saint-Elzéar Boulevard W.	February 2022	$41,563,200	$373,770 / Unit	**Multi-Family**
24-30 Sicard Place	January 2022	$40,000,000	$214 / SF	**Industrial**
5834-5940 Metropolitain Boulevard E.	February 2022	$15,600,000	$76 / SF	**Retail**
625-685 32nd Avenue	January 2022	$13,400,000	$351 / SF	**Retail**

Source: Colliers Canada Research, Altus Group, May 2022

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Featured Transactions

Transaction Name
Méga Centre Ste-Foy

Transaction Date
Sold December 2021

Price (CAD)
$98,500,000

Asset Size
524,000 SF

Price per SF
$188

Type of Asset
Retail

Transaction Name
Centre Carnaval Lasalle

Transaction Date
Sold August 2021

Price (CAD)
$70,000,000

Asset Size
-

Price per SF
$30 PPSF Buildable

Type of Asset
Covered Land PLAY

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Featured Transactions

Transaction Address
5025-5055 des Sources Boulevard

Transaction Date
Sold August 2021

Price (CAD)
$33,000,000

Asset Size
-

Price per Unit
$148,148 / Unit

Type of Asset
Multi-Family

Transaction Name
Marché Provigo

Transaction Date
Sold December 2021

Price (CAD)
$22,000,000

Asset Size
71,918 SF

Price per SF
$306 PSF

Type of Asset
Retail

Montreal Investment Team

Colin Worrell
Senior Managing Director
+1 514 764-8180
colin.worrell@colliers.com

Janina Francescutti É.A., AACI
Executive Vice President
+1 514 764-2848
janina.francescutti@colliers.com

Joe Rullier
Senior Vice President
+1 514 764-2832
joe.rullier@colliers.com

Vanessa Cohen
Senior Associate
+1 514 764-8186
vanessa.cohen@colliers.com

Chimène Constance
Senior Associate
+1 514 764-2834
chimene.constance@colliers.com

Anthony Kyriacou
Associate
+1 514 764-8167
anthony.kyriacou@colliers.com

Report Contributors

Eliezer Timolien
Senior Research Analyst
+1 514 764-8190
eliezer.timolien@colliers.com

Alessandro Migliara
Research Analyst
+1 514 764-2841
alessandro.migliara@colliers.com

Colliers International Montréal
1800 McGill College Avenue, Suite 400
Montreal, QC | H3A 3J6
+1 514 764-8190