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# MAKING A COMEBACK



## Calgary's commercial real estate market could be poised for a rebound in 2018

All eyes will be on Calgary's commercial real estate market this year, with hopes that the downtown office sector, which continued to struggle in 2017, will rebound in 2018.

The office market has grabbed everyone's attention over the past three years, as vacancy rates have soared to historically high levels following the collapse of oil prices and the subsequent waves of layoffs that ravaged employment ranks in downtown Calgary. Thousands of people were cut loose, and a vast amount of office space suddenly became vacant in the downtown core.

According to Avison Young, the city's downtown office vacancy rate ended 2017 at 26 per cent, up from 25.7 per cent in the third quarter and 23.9 per cent one year earlier, but down from the peak vacancy rate of 26.4 per cent, recorded at the end of the second quarter of 2017.

Here are the telling numbers of what has happened in the office market. Avison Young says the total amount of vacant office space in Calgary has tripled to 17.9 million square feet in the last three years, from 5.9 million square feet in the fourth quarter of 2014.

But a corner has perhaps been turned, because the rate of new vacancies is slowing down. The amount of empty office space across Calgary jumped by 94 per cent in 2015. However, that figure was down to a 41 per cent increase in 2016, and plummeted to only 10 per cent in 2017.

"Second quarter 2017 was the peak vacancy for this downturn," said Todd Thronson, Avison Young principal and managing director of the company's Calgary office. "Even though Telus Sky will bump vacancy up when it comes on stream in late 2018, given our current economic situation and forecasting, the increase will not cause the vacancy rate to rise above the high-water mark recorded in 2017."

Telus Sky is the last downtown office building still under construction from the most-recent building cycle.

It will add 460,000 square feet to the downtown office inventory, and is only 39 per cent leased.

Avison Young is forecasting absorption – the net change in occupied space – to be flat for the first half of 2018, but rise to about 100,000 square feet in each of the last two quarters of the year.

Absorption in downtown Calgary was -189,000 square feet in 2017. While still negative, it's a huge improvement compared with -3.1 million square feet in 2015 and -2.2 million square feet in 2016.

"While energy and energy services companies continue to make up a large share of the leasing transactions being recorded, increases from areas such as information and technology, not-for-profits, government, business services and green technology are definitely being noticed," said Thronson. "Also, activity by smaller tenants is growing noticeably. Demand for space less than 5,000 square feet continues to be high."

According to a year-end downtown office report by Barclay Street Real Estate, overall, leasing activity during the fourth quarter was about trading spaces and upgrading in the process.

"This was demonstrated in the notable increase in B-Class availability and corresponding decreases in AA-Class and A-Class vacancies during the quarter. With the attractiveness of the downtown market steadily increasing over the previous two years, firms that have right-sized and are adequately capitalized have begun taking advantage of the headlease market, where substantial reductions in pricing and aggressive incentives among A and AA spaces have made entering into long-term leases much more affordable," said the report.

"The C-Class market has also become increasingly appealing for budget-conscious start-ups, offering numerous single-office and shared-office setups available with lease rates often in single digits. Firms with leases expiring over the coming 12 to 15 months can look forward to ample opportunities to upgrade their spaces and, in most cases, simultaneously reduce their real estate expenditures. As such, we anticipate seeing a renewed flight to quality through 2018."