CALGARY SECOND QUARTER 2018

COMMERCIAL OFFICE MARKET OVERVIEW

Downtown Market

OVERALL RATE **25.9%**
+ 0.3% FROM Q1 TO Q2

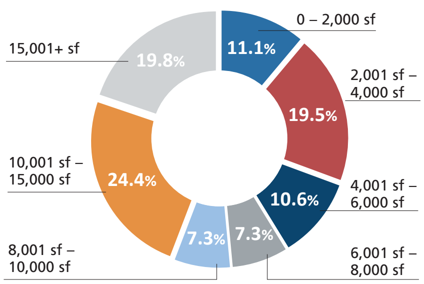
CLASS AA **19.0%**
– 0.8% FROM Q1 TO Q2

CLASS A **26.1%**
+ 1.2% FROM Q1 TO Q2

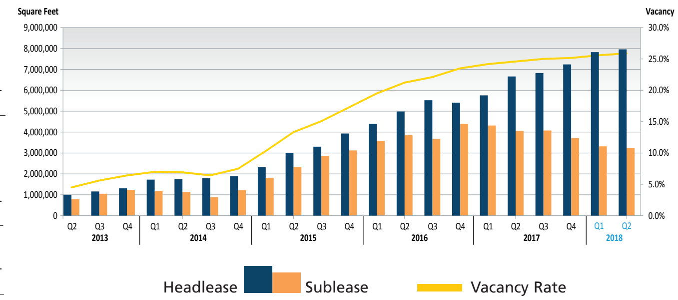
CLASS B **35.0%**
NO CHANGE FROM Q1 TO Q2

CLASS C **25.5%**
+ 1.6% FROM Q1 TO Q2

DISTRIBUTION OF OPTIONS BY SIZE RANGE



5-YEAR HISTORIC VACANCY



Vacancy in Calgary's Downtown remained generally steady as 2018 reached its mid-point, rising by just 0.3% to 25.9%. Net absorption during the second quarter was negative 129,000 square feet (sf). While overall vacancy in the Downtown market increased, the uptick is largely due to our inclusion of spaces that come available for lease and sublease later this year. More than half of this space – approximately 79,000 sf – comes available during the second half of 2018.

Expectations of continued economic recovery remain, with sentiment among many numerous businesses turning decidedly positive according to a survey by Calgary Economic development and the Calgary Chamber of Commerce. Among respondents, 60% believe economic improvement will be the theme of the coming 12 months and 40% planning to expand their employee count.

As with the first quarter of the year, several large transactions took place during Q2. Landlords experienced an ongoing flurry of activity as companies made moves to capture the opportunity to lock-in lower rates for longer terms.

Notable Q2 transactions included Paramount Energy's 55,000 lease in Calgary City Centre and Alberta Energy Exchange's sublease in Eau Claire Tower. Sublease activity, as well as ongoing rollover, continued to erode the large supply of sublease vacancies on the market. Barclay Street has been tracking an ongoing reduction in the ratio of sublease to headlease spaces. At the end of June, this ratio sat at 29%/71%, down from 30%/70% in Q1.

Our take on the above is a confirmation of our Q1 assessment: we're seeing the bottom of the market in the Downtown. As anticipated, the historically large volume of sublease space is slowly but surely dissipating as noted earlier, as Landlords and would-be sublandlords continue to exercise restraint in marketing additional space. Looking ahead, the unleased office portion of TELUS Sky represents the most significant space on the horizon and it will potentially add the better part of one percentage point to Downtown vacancy.

Beltline Market

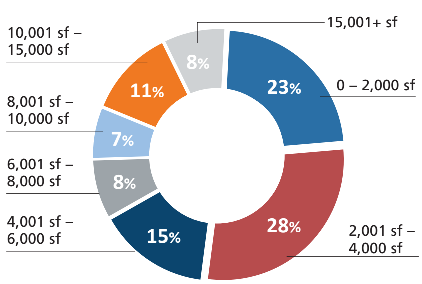
OVERALL RATE **23.6%**
+ 1.3% FROM Q1 TO Q2

CLASS A **26.0%**
+ 2.2% FROM Q1 TO Q2

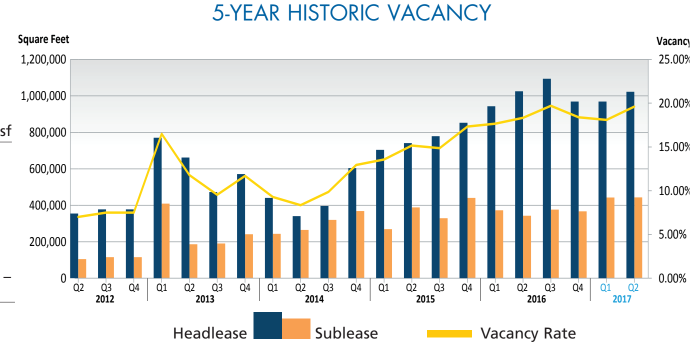
CLASS B **23.4%**
+ 0.1% FROM Q1 TO Q2

CLASS C **17%**
+ 2.8% FROM Q1 TO Q2

DISTRIBUTION OF OPTIONS BY SIZE RANGE



5-YEAR HISTORIC VACANCY



Vacancy in Calgary's Beltline office market increased slightly by 1.3% over the second quarter of 2018, ending June at 23.6%. Net absorption during Q2 was negative 64,000 square feet (sf). While overall vacancy increased, the uptick is largely due to our inclusion of spaces that come available for lease and sublease later this year. More than half of this space – approximately 37,000 sf – comes available during the second half of 2018.

The major contributors to the uptick in vacancy were A Class and C Class properties, with the

Beltline Market (cont.)

most significant space being Citadel West which has been listed for sublease by CH2M Hill. This was the primary driver of the above-noted space available between July and December of this year.

Looking further out, the pipeline of pending leases more than seven in the future has diminished significantly, making this 'shadow vacancy' negligible. Additionally, with Mount Royal Village – West and the RECA Building delivered, we anticipate the pipeline of future excess space will remain constricted in comparison to the previous three years.

With the Beltline expected to see vacancy remain above 20% well into 2018, conditions in this submarket continue to heavily favour the Tenant. As such, Landlords remain motivated to keep tenants and attract new prospects. This is particularly true for owners of B Class and C Class properties who must reconcile offering the very low rates expected by tenants with the higher operating costs in their properties. To this end, Landlords have become increasingly amenable to gross deals that allow for all costs to be rolled-up into attractive packages.

Suburban Markets

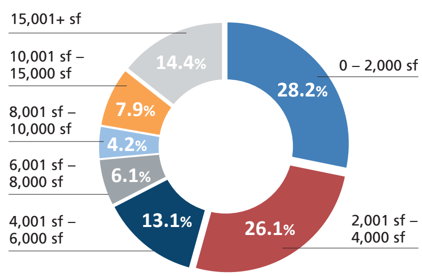
OVERALL RATE **20.5%**
+ 2.8% FROM Q1 TO Q2

CLASS A **21.1%**
+ 3.9% FROM Q1 TO Q2

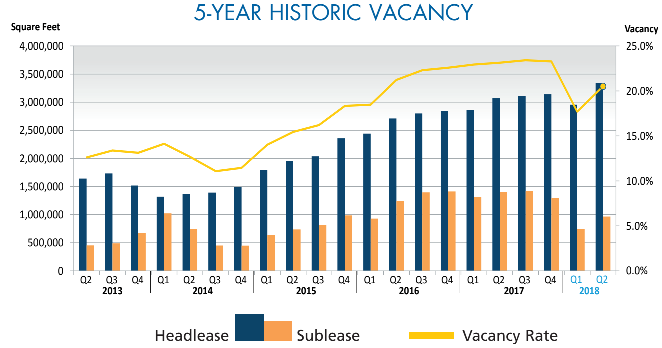
CLASS B **25.7%**
+ 1.6% FROM Q1 TO Q2

CLASS C **10.8%**
– 0.4% FROM Q1 TO Q2

DISTRIBUTION OF OPTIONS BY SIZE RANGE



5-YEAR HISTORIC VACANCY



Vacancy in Calgary's suburban office markets increased by 2.8% over the second quarter of 2018, ending June at 20.5%. Net absorption during Q2 was negative 554,000 square feet (sf) with the uptick is largely due to our inclusion of spaces that come available for lease and sublease later this year.

More than 367,000 sf comes available for lease during the second half of the year; over half of he negative absorption calculated for this period. The majority of this is full-floor and multi-floor options in buildings such as 140 Quarry Park Boulevard, Ronmor Business Centres I & III and Dominion Bridge.

Despite the recent uptick in vacancy, rental rates remained stable for higher quality product while Landlords have become increasingly motivated to complete leases with less resistance in B and C Class properties to maintain their tenant bases. Speaking to the latter, the rent expectation gap between owners and tenants has narrowed significantly but with the very low rents we've seen during the past 24 month, little room remains for negotiation downward.

The end of the building cycle that began in mid-2014 reached its final stages, with the Macleod Professional Centre due later this year and completion of the design-built Hexagon Campus expected in early 2019. At June 30th, these buildings are 40% and 100% pre-leased, respectively. A couple of smaller projects such as Aviation Medical Centre (27,000 sf) and One North Business Centre (20,000 sf) are also nearing completion.

In response to the significant volume of new inventory brought to market during the past four years, we continue to see a considerable number of Landlords with older or less conveniently-accessible properties moving forward with show-suiting programs in hopes of stimulating competitive activity.

Reference

Varcoe, C. (June, 2018). Four in 10 Calgary companies look to add staff as confidence grows in economy. Calgary Herald. http://calgaryherald.com/business/energy/varcoe-four-in-10-calgary-companies-look-to-add-staff-as-confidence-grows-in-economy

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