WESTERN INVESTOR

Alberta rebound: Economy accelerates in approach to "cruising speed"

Commercial real estate look towards a couple of other "R" words: rebound and recovery

Geoff Kirbyson Western Investor May 1, 2018

While many are hoping Alberta's energy-related downturn will soon be a speck in the rearview mirror, few are shouting it from the mountain tops. Stakeholders in both Edmonton and Calgary are still smarting from having their retail, office and industrial markets hammered to varying degrees over the past few years.

But the hammering is over and the rebuilding has apparently begun.

It is not the boom's second coming, but "people are a lot more positive now. We're seeing employment numbers get better and vacancy is stabilizing. The worst is over," said Brian Gettel, president of the Network Real Estate Intelligence, an Edmonton-based real estate research firm.

Improving economic fundamentals have a growing number of real estate players whispering about optimism returning to the market, particularly since late last year.

"We've seen a lot of activity and interest in the last three months," said Casey Stuart, Calgary-based vice-president of industrial at Barclay Street Real Estate Ltd.

"We've seen situations with multiple offers on properties, which are all good signs. The question is, 'can it be sustained?'"

It is certainly on pace. The last quarter of 2017 registered a total of 162 commercial real estate transactions in Calgary, worth $1.1 billion, according to Altus Group. That was up 52 per cent from the previous quarter. Residential and industrial land were the most active sectors, each at 20.4 per cent of activity.

The Royal Bank of Canada (RBC), however, said the "easy" stage of Alberta's economic recovery is drawing to a close and the more difficult part lies ahead.

RBC predicted the provincial economy will have grown by 4.1 per cent in 2017, but that says more about the low base the year before than when everything was firing on all cylinders.

"We expect key economic sectors, such as energy and capital investment, to reach a more sustainable 'cruising speed' after their initial post-recession blast-off in 2017. The good news is we also expect the recovery to continue to broaden across economic sectors. This means that while the headline growth number is poised to be much smaller in 2018 – our forecast is 2.3 per cent – more Albertans should feel the improvement in the economy," the bank said.

RBC predicts employment growth will accelerate while the jobless rate will decline significantly in 2018 but Albertans aren't likely to wave the all-clear flag any time soon.

"It will take until 2019 for Alberta's economy to recover fully from its severe recession in 2015 and 2016," the bank said, calling for GDP growth of 2 per cent in 2019.

Edmonton

Depending on which statistic you look at, things bottomed out in Edmonton in either 2015 or 2016. For example, the dollar value of land sold plummeted from $876.1 million in 2013 down to $310.9 million in 2016. Last year it inched up to $324.8 million. The dollar value of the buildings sold, meanwhile, fell from $1.7 billion in 2013 down to $1.0 billion in 2015 before recovering to $1.8 billion in 2016 and $1.9 billion last year.

In its 2017 market overview for Edmonton, the Network predicts 2018 will be a "growth year."

"A modest increase in activity is projected in both the building and land category and it is anticipated that there will be a stabilization in values," the report said.

Office space hasn't been a sought-after product of late in either Calgary or Edmonton but Gettel said Edmonton, in particular, takes a long time to rebound.

"We've got such a narrow office market in Edmonton. We had three new high-rise office towers being built. We've got two completed and the third will be finished this year. We hit the downturn and had a big source of new supply coming in, which drove our vacancy rate up. Lease rates tumbled in a real hurry because the market is so narrow," he said.

The main beacon the last couple of years has been retail, where vacancy rates remained low and lease rates didn't change appreciably with the economic downturn, thanks largely to a strong influx of young people.

Over the past two years, Alberta consumer spending has remained in the $6 billion per month bracket, second highest in Western Canada, according to Statistics Canada.

"We haven't had a lot of speculative property being built. A lot of the new retail built is suburban because we don't have a lot of land left in the mature areas. We haven't had a chance to build up any excess space," Gettel said.

Of course, it hasn't all been days of wine and roses in the retail sector. Losing Sears in regional malls, just three years after Target pulled out of Canada, is leaving blocks of empty space that aren't likely to be filled any time soon.

"There are no more anchor tenants like that anymore. You're going to have to divide it into smaller blocks," Gettel said.

Calgary

Three hours to the south, Stuart believes the industrial sector will lead Calgary back to the promised land.

The industrial vacancy rate dropped to 6.5 per cent at the end of the fourth quarter of 2017, down from 7.9 per cent a year earlier, thanks largely to the transportation and warehousing industries, as well as food and healthcare.

"Without question, industrial will have the most growth in terms of employment and new business opportunities," he said.

Gettel doesn't disagree. He said people tend to buy less land during a downturn but he's expecting to see some increased activity this year, particularly in industrial.

"If we see an uptick in land sales in 2018, that will be a clear sign that we're on the right path," he said.

As if on cue, Vancouver developer PC Urban Properties Corp. bought a 5.4-acre industrial site in Calgary this February, where it will convert the 40-year old business park into industrial condos. PC Urban expects to sell more than 100,000 square feet at $230 to $245 per square foot, said Sean Ferguson, associate vice-president, industrial, for Cushman & Wakefield, the listing agents for the property.

"We've had a lot of interest," Ferguson said.

Stuart believes Calgary's geographic location is a big advantage from a logistics perspective and was largely behind a large investment from CN Rail, which built an intermodal park just east of the city a few years ago.

"We've seen some growth there. There are three companies distributing out of the park. We've created some infrastructure to support logistics throughout the Pacific Northwest, which includes the runway and international terminal upgrades at the Calgary airport, and rail and truck traffic," he said.

It also helps that Vancouver's industrial market is "overheated" with a vacancy rate below 2 per cent.

"There is extreme pressure on rental rates so we have seen a number of distribution companies relocating to Calgary or adding additional square footage here instead of in Vancouver," he said.

Calgary's office market is still "subdued" with vacancy rates hovering in the 25 per cent range for both suburban and downtown but just how long the recovery will take is the real wildcard. Stuart said most estimates are around five years.

"The office market is still in a lot of pain. Unless we see some new entrants, the existing companies that are here aren't expected to have enough growth to absorb a lot of the square footage that's vacant today," he said.