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POSITIVE TRACTION

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Real estate officials expect conditions to support turn-around in downtrodden commercial market

Calgary's commercial real estate market is showing signs it is finally moving on from tough economic conditions that sent vacancy rates soaring and rents plummeting over the past two years, say officials.

"There is a sense in the market that the worst is behind us and that conditions will gradually improve," said Joe Binfet, managing director/broker of Colliers International in Calgary.

"Tenants are making decisions, and we are seeing an increase in junior oil and gas companies taking space.
Binfet pointed to "positive traction" in the energy sector helping the office market, with WTI prices rising about $50 US per barrel and recent pipeline approvals from the federal government.

"The bottom line is that until we see a significant upturn in energy prices, the major companies will be slow to hire and demand for office space downtown will remain tepid," he added.

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Todd Throndson, managing director and principal of Avison Young in Calgary, said 2016 was a year of multiple stories in the city's commercial real estate market.

"The one market that really had a difficult time was the downtown market, and that is a different story than most of the other markets. That is important to understand," he said.

"You saw vacancy increase. You saw negative absorption. You saw rental rates plummeting. You saw sublease space being leased at very, very low rental rates."

Throndson added that while transactions levels in all commercial sectors were down, activity did improve as 2016 progressed.

"There was no demand at the beginning of the year. Nothing was going on," he said. "People were really worried. They were really uncertain, and it was a very difficult time. But as the year progressed, people started to realize on a lot of the cost-cutting measures that they had undertaken, and the energy markets started to stabilize at a more reasonable number. That allowed businesses to start having a little bit more confidence in what they were doing."

According to a year-end report from Barclay Street Real Estate, Calgary's downtown office market took the brunt of the downturn:

• Downtown office: 2016 Q4 vacancy, 23.5 per cent; 2016 absorption, -2.5 million square feet; 2015 Q4 vacancy, 17.29 per cent; 2015 absorption, -3.9 million square feet.

• Beltline office: 2016 Q4 vacancy, 17.9 per cent; 2016 absorption, -41,000 square feet; 2015 Q4 vacancy, 17.33 per cent; 2015 absorption, -429,000 square feet.

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• Industrial: 2016 year-end vacancy, 7.58 per cent; 2016 absorption, 429,863 square feet; 2015 year-end vacancy, 6.57 per cent; 2015 absorption, 2.15 million square feet.

• Suburban office: 2016 Q4 vacancy, 22.6 per cent; 2016 absorption, -458,000 square feet; 2015 Q4 vacancy, 18.33 per cent; 2015 absorption, -961,000 square feet.

• Retail: 2016 Q4 vacancy, 3.4 per cent; 2015 Q4 vacancy, 2.7 per cent.

"The downtown market will remain challenging," said Binfet. "With vacancy in the 23 per cent range, I expect that landlords will continue to be aggressive in securing existing tenants in their portfolio as well as new prospects. We will continue to see tenant inducements such as free rent, furnished space and improvement allowances until conditions improve."

He added the suburban office market has a more diversified tenant base with finance, medical, insurance and some technology companies in the mix, and will not be impacted as severely as the downtown market.

The industrial market, meanwhile, was extremely resilient in 2016 and will continue to be so in 2017, said Binfet.

"Calgary has established itself as the distribution centre for Western Canada, and logistic companies that previously thought Calgary was too expensive have circled back and are looking to be opportunistic in establishing a foothold in our market," he said.

"We have seen an uptick in investment activity in Calgary. There are plenty of buyers in the market, but we have not yet seen the deep discount in pricing that many were expecting."

Throndson said there will still be a three-to-six-month period of time when more downtown office space will come onto the market and vacancy will increase. But then the market will enter a flat period when conditions stabilize as cost-cutting measures subside and companies will look for opportunities.

"But I see a 12-to-24-month time span where things are relatively flat, and then in 2019 we're going to start to see growth back into the market," he added.