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BOMA CALGARY NEWS

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By Sandy McNair

Calgary's Office Markets are Fragmenting with Implications for All Stakeholders

A Look at Drivers, Dynamics and Outcomes

"This time, it is different" is one of few phrases that often will get a conversation going in an unhealthy direction, quickly. Sometimes this phrase has been used to suggest that the laws of nature and the business cycle have been altered, at least for now, and some imbalance in demand and supply will have a unique and significantly more positive outcome than ever experienced before.

Each business cycle has its own personality, drivers and dynamics. For more than a decade commercial real estate investments have benefited, relative to the stock markets, bond markets and many other investment options, from increasing investment appeal, transparency and performance. Strong inbound capital flows, compressing cap rates and excellent yields have been felt widely across the commercial real estate industry. If you wish, "high waters float all boats" has been the theme and the outcome for many investors.

Given the underlying drivers and current market dynamics in Calgary and most of the major office mar-

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kets across Canada, we see a widespread pivot towards highly divergent outcomes for each industry participant and stakeholder. Going forward, the theme will be "concurrent big winners and big losers" where the averages are dangerous as they tend to conceal rather than reveal the very specific and localized patterns that will shape future performance.

To date, many in the commercial real estate industry have used a simple two-dimensional matrix to segment the larger office markets into clusters with the desired homogenous characteristics that generate similar and predictive performance patterns: geographic districts (downtown, midtown/beltline and suburbs) and nodes (downtown core, downtown east and downtown west, for Calgary examples) as well as building class (class A, B, C). The expectation being, that if my subject property is a class A building located in the downtown core, then I can expect my current status and future performance to match the average of all class A buildings in the downtown core and furthermore, that the variance across the peer group will be small.

Relying on the averages is already dangerous. If we isolate a group of just eight downtown core class A buildings in Calgary, they have an average availability rate of 21.5 per cent compared to the rest of the downtown core class A buildings that have an average availability rate of four per cent. Not very similar or very predictive.

Perhaps what is needed is to dig much deeper and look at more attributes to more accurately fragment the marketplace into similar and predictive tranches. But which attributes? How do we measure some of them and is the data collectible, accurate or current?

As a starting point we have explored typical floor size and somewhat arbitrarily segmented the market into three tranches using 16,000 square feet and 29,000 square feet as break points for small, medium and large typical floor sizes. Fact #1: The Calgary downtown core class A inventory is 45 per cent, 46 per cent and nine per cent small, medium and large floor plates respectively. Fact #2: The office space currently available for lease is currently located 63 per cent, 37 cent and zero per cent in those same downtown core class A buildings with small, medium and large floor plates respectively. Facts #3 and #4: When we change the view to the total of class A, B and C in all of downtown Calgary (downtown west, downtown core and downtown east), the inventory is 44 per cent, 47 per cent and nine per cent for small, medium and large floor plates and the total office space available for lease is currently located 62 per cent, 38 per cent and zero per cent in buildings with small, medium and large floor plates. Given the current dynamics of Calgary's oil industry and gas industry, buildings with smaller floor plates are currently feeling the most pressure, by a significant margin. Fact #5: Comparing Calgary to the other five major markets in Canada, only Calgary has the above noted material skew of the available space towards office buildings with small floor plates. Owners and managers of buildings with small floor plates will need to work very smart and harder than others to outperform their peers.

Many buildings and their sub-markets are at a pivot point in terms of appeal and future performance.

The office leasing and investment markets are far more fragmented than ever before. The substantial new supply of significantly different office buildings has altered the 'commodity' mindset of office spaces. Many office space occupiers now view space as increasingly distinctive and as an important element in their strategy to win the battle for talent. Office buildings and spaces are now being differentiated by:

- Design (more daylight, personal control of temperature and airflow, higher occupant density, lower energy consumption, better environmental footprint);
- Property manager and their brand (there are stark differences in awareness, use and satisfaction with communication channels established between occupiers and their property managers, responsiveness, issue resolution rates, intentions to stay, referral and recommendation rates for buildings and their property manager's brand);
- Positioning (relative to other buildings in that geographic node, building class, floor plate size, vintage, and other increasingly important attributes); as well as
- Capital investment (previous, current and future upgrades in building and occupant performance, occupancy costs, image and appeal).

Many buildings and their sub-markets are at a pivot point in terms of appeal and future performance. Some buildings will require repositioning and even repurposing. Some will require new owners and managers to achieve their potential. Others will drift downward into a place of increased pain before the key changes are made.

For those investors, owners and managers who have been investing in their buildings and people, in their processes and culture and in a service-centric mindset, they will more clearly see the premium performance that accrues to the "big winners." Moving forward, strategy and execution matter. Now, they matter a lot.

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By Lloyd Suchet,
Executive Director,
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Sitting at the Crossroads of Western Canada

At BOMA we often talk about transportation in terms of the ability to move tenants from their home to their workplace and back. So when news of projects like the southwest leg of the ring road enters the public debate the temptation is to talk about its ability to reduce commute times. But infrastructure like the ring road does far more than just serve residents – it is also crucial in facilitating the growth of another industry that is important to commercial real estate.

Somewhat hidden by Calgary's emergence as a major energy centre is its growth as a western Canadian transportation hub. It turns out that like real estate, the transportation sector puts a high value on location. Calgary is centrally located within Western Canada meaning that as a hub it can lower transportation costs. However geography alone won't cut it unless there is the transportation infrastructure to accommodate the movement of goods.

Calgary sits on the crossroads of the Trans-Canada Highway and the CANAMEX corridor connecting Canada, the United States and Mexico. Similarly when looking at rail, Calgary is directly linked to both the Port Metro Vancouver and the Port of Prince Rupert, with lines continuing north, east and south.

The final piece is of course air service. Passenger volumes at YYC overtook Montreal for the first time in 2014, but the airport authority has also attracted increased dedicated cargo services. In fact, Calgary is one of only two airports in Canada with scheduled cargo service to both Europe and Asia.

Calgary's emergence as a transportation hub matters for commercial real estate for a number of reasons. First and foremost, this cargo requires physical space while it is stored and transferred to another mode or vessel. A nice example of this is CN's Calgary Logistics Park that opened in 2013 and allows the company to move goods even more efficiently. Similarly, the logistics of moving all these goods requires labour and therefore office space both on the industrial site and elsewhere. In fact, according to Calgary's 2014 census, the sector consists of 5,170 companies employing 78,700 Calgarians. And finally, the existence of efficient transportation networks tends to attract other businesses that rely on transportation. This is why large retailers like Sears, Walmart, Canadian Tire, Costco and now Sobeys have decided to locate their distribution centres in the Calgary region, and why CN is offering sites and warehouses for lease in their Logistics Park.

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Driving around Calgary International Airport tells us the same story, where according to the airport authority industrial space on airport lands has grown approximating 300 per cent since 2004. When you put all of this information together you get a picture of just how important transportation and logistics is to commercial real estate, and Calgary's economy as a whole.

A better understanding how infrastructure like roads and highways can enable economic development will hopefully lead to a more fulsome conversation when we address infrastructure and land-use issues in the future.

BOMA Insider

Welcome New BOMA Member Companies!

RecycleSmart Solutions Inc. – *Graeme Dobinson*

Westcare Facility Services Ltd. – *Sandy Stephenson*

Manulife Real Estate – *Peter Whitehead*

Petwin Properties – *Ted Kennedy*

Mariner Mechanical Ltd. - *Jason T. MacDonald*

Rocky Cross Construction North – *Ryan Thelwell*

Master Painters and Decorators – *Dana McCurdy*

GNRL Construction – *Chris Fotopoulos*

Process Color Print – *Stuart Parsons*

DOGS Security Company Canada – *Aly Bhimji*

Exp Services Inc. – *Sathya Ramachandran*

G.E.M Inc. – *Brian Eberle*

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Aspen Properties team accepts the BOMA BESt Level 3 Certificate for Palliser Complex.

Welcome new BOMA Calgary Member; Mariner Mechanical Ltd - Jason T. MacDonald.

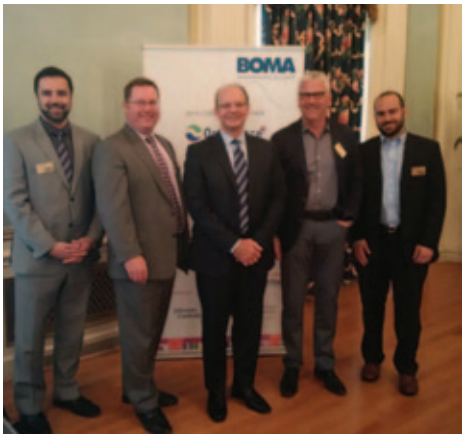
GWL Realty Advisors team accepts the BOMA BESt Level 1 Certificate for 72nd Ave Business Center.

CREIT Management LP team accepts the BOMA BESt Level 3 Certificates for Altius Centre and Calgary Place.

Triovest Realty Advisors team accepts the BOMA BESt Level 2 Certificate for the 707 Building and Level 3 Certificate for the 999 Building.

The GWL Realty Advisors team accepts their Level 3 Certificate for Fifth and Fifth.

Congratulations to the 2014/2015 BOMA Mentorship Program participants!



BOMA Calgary Executives and City Manager, Jeff Fielding.

Thank you to our wonderful volunteers for their help at the BOMA Stampede Breakfast.

Fifth Annual BOMA Stampede breakfast.

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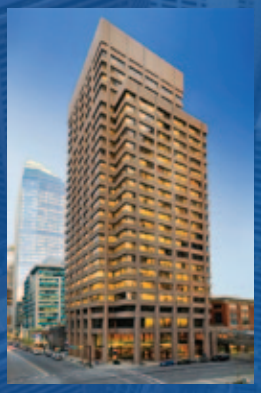

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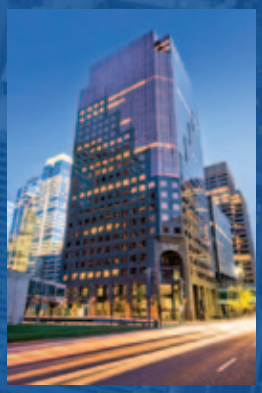

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Difficult Times Ahead – Vacancy Versus Developable Land

By David Parker

Throughout the little blip in our real estate sector the industrial market appeared to be doing quite well but there is concern today as, according to the latest Barclay Street Real Estate report, the huge amount of new construction taking place has affected the amount of vacancy.

Jon Mook, executive vice president of industrial leasing and sales, says the fact that there is 4.7 million square feet of industrial buildings currently under construction and much of that, over three million, is being built on spec has increased the vacancy rate to 4.8 per cent.

While this is still quite healthy compared to many cities across North America, it something we are not used to seeing.

The majority of those buildings will be completed by the end of this year so vacancy rates may get even a little higher, but when Calgary bounces back - and it will - the inventory will be of benefit. However, 2016 could be a difficult year in terms of the number of transactions completed.

One concern is that there is such a shortage of developable land within the city limits. The majority is controlled by the city and as they are certainly taking their time to bring it to market, there could be a land shortage by 2017-18 which means that any company wishing to develop or owner-build will have to move to Rocky View County.

Only four lots remain in the Walton International Group's portion of Point Trotter Industrial Park while none of the City of Calgary's lots there have yet to come to market.

And that doesn't bode well for Calgary as it will result in lost tax revenue.

Mook and his partner Casey Stuart have already sold lots in Fulton Industrial Park near Indus to companies who will make the move from their Calgary locations. And why not? Cheaper land, no business taxes and the location is easily accessible to the Stoney Trail and the Canadian Pacific intermodal switching zone.

One only has to take a meander behind CrossIron Mills in Balzac to see the amount of activity along Highway 566 including the half-million-square-foot distribution centre in High Plains Industrial Park being built by Ross Perot Jr. and where Gordon Food Services made the move form Centre Avenue in Calgary. More taxes lost.

It might be a little tough today for industrial realtors but before too long they just might have customers and nothing in the city to offer them.

I must just make another mention of the magnificent new metal bridge across Shaganappi Trail NW. The walkway approaches are so long and so high I predicted it would get little use. Now the costly structure that takes people from Canadian Tire to Best Buy appears to be nothing but an expensive place to hang banners.

I mentioned to a couple of councillors that although I drive beneath it at least twice a day, my people count on the bridge in the first three weeks was 11. The response was, "That's more than you'll see on a bike path." Nuff said.