



METRO INDUSTRIAL VACANCY EXPECTED TO TREND DOWNWARD



Now that Canada's economy is moving into a growth phase, the Metro Vancouver industrial market is proceeding into recovery with little risk of setback anticipated. Although overall growth has yet to occur, some submarkets in the traditionally tight sector are witnessing small but steady improvements in sales and leasing activity, sales dollar volume and sale prices, and lease rates.

These are some of the key trends noted in Avison Young's Fall/Winter 2010 Metro Vancouver Industrial Overview, released today.

"The local industrial real estate market is neither accelerating nor decelerating - it's just rolling along," comments Avison Young Principal Robert Gritten. "But I wouldn't say we're in recovery yet."

Gritten says the number of industrial sales transactions and sales dollar volume are on pace to slightly exceed 2009 levels. But, unlike in 2009 and early 2010, most of the recent deals are based on future growth rather than downsizing, distress or forced relocations.

Metro Vancouver's industrial vacancy rate currently sits at 4.2% compared to 4.7% in spring 2010 and 4.4% in fall 2009. The vacancy rate remains above the 2.4% recorded in fall 2008, when vacancy rose above 2% for the first time since early 2006. The availability rate (which includes space being marketed but is not physically vacant, or new supply that is nearing completion and available for lease) is estimated to be 7.2%, down slightly from 7.5% in spring 2010, but up from 7% in fall 2009 and 6% in spring 2009.

"The slightly lower availability rate can be attributed to more tenants starting to gain confidence and, subsequently, make decisions based on expansion," says Avison Young Principal John Lecky.

Overall vacancy is expected to decrease in the next six to 12 months as leasing activity picks up, although increases in Canadian unemployment rates may temper demand.

Since peaking in 2008, rental rates have trended downward. However, landlords are beginning to witness more bids as tenants seek to capitalize on opportunities to relocate to newer and larger locations.

Average asking rents for large (75,000-sf-plus) distribution centres range from \$5.50 psf (year one) in the South Fraser Distribution Centre (a.k.a. Hopcott Centre) in Delta to the mid-\$6 psf level for new product elsewhere. The market must gain more traction before fall 2009 rates of \$6.50 to \$7.50 psf can be realized again.

Average asking rents for sub-50,000-sf new and class A spaces in the core areas of Richmond, Burnaby and Vancouver remain in the \$7.50 to \$8.50 psf range witnessed in spring 2010, down modestly from \$8 to \$9 psf in fall 2009. Rents for sublease space remain lower, but these opportunities are decreasing.

"Burnaby continues to outperform other districts as it records ongoing increases in sales and leasing activity," points out Avison Young industrial broker Kyle Blyth. "Meanwhile, large pockets of industrial space in areas such as Surrey, Langley, Richmond and Delta are slowly but steadily leasing up."

Demand for investment product remains strong as buyer confidence continues to rise and commercial real estate outperforms other sectors. Some deals have resulted from pent-up demand, while vendor and purchaser price expectations have narrowed. There continues to be a lack of available investment-grade product.

"The market has potential for a turnaround in early-to-mid 2011 as sale prices and vacancy hold steady, investors gain greater access to capital and credit, and owner-users and tenants require more space for expansion," says Blyth.

Meanwhile, developers are delaying speculative new-product deliveries until vacancies show sustained reduction.

"With current rents failing to justify land costs and lender demands continuing to be somewhat onerous, cautious developers are opting to market build-to-suit strata properties with multiple small or mid-sized bays rather than risk building large single-tenant or multi-tenant properties," notes Gritten. "Owner-users, who seek to build equity or consider expansion, are also showing resurgent demand for strata properties. But in many cases, lenders require strata properties to be significantly presold before financing construction."

In most areas of the region, prices for small ready-to-build sites, designed for owner-users, are continuing to hold. However, sales of large development land parcels are scarce throughout Metro Vancouver. As a result, pricing levels for large land parcels have fallen 10% in central areas, approximately 25% to 35% in secondary locations, and as much as 50% in tertiary markets since peaking in 2008.

According to the report, historically-low capitalization rates continue to hold, ranging from 6.25% for high-quality properties to 7.5% for class C buildings. These figures are comparable to the 6.5% to 7.5% range displayed in spring 2010, and can be attributed to the limited product available and the substantial amount of equity looking to be placed.

"The current ability to secure five-year financing below these yields has served to suppress escalation in capitalization rates for the foreseeable future," adds Lecky.

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