

'Milestone year' in office construction

Low vacancy rates, rising prices spur investor demand and surge in activity

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Canada's commercial real estate business has rolled into 2007 on the biggest surge in office construction in more than a decade.

Under construction across the country are 71 office towers -- close to four times the level of activity just two years ago. Once finished, those buildings will bring tens of millions of square feet of new space to the market, the bulk of it concentrated in downtown Calgary and Toronto.

"Certainly [2006] was a unique year," said Sandy McNair, president of Altus InSite Real Estate Information Systems Inc., which tracks the industry. "It was a milestone year. It's been quite a while since we've seen this happen anywhere."

The sod was turned on several major projects, including Toronto's long-dormant Bay-Adelaide site, where for years an unfinished elevator shaft stood as a reminder of how quickly fortunes turned at the end of the last boom in the early 1990s.

The biggest transformation of a skyline, by far, is taking place in Calgary, where demand from the energy sector has created the tightest office market on the planet, with vacancy rates for prime space well below 1 per cent. Close to half of all new office construction is taking place in Calgary, although other major centres besides Toronto are seeing activity, including Ottawa, Montreal, Edmonton and Vancouver.

Much of the momentum for construction is coming from the investor market, Mr. McNair said. Pension funds and other investors have watched prices soar for the few existing office towers that have traded hands. Those rising prices and falling vacancy rates have prompted them to put a shovel in the ground. "With prices so high, people are saying, 'I might as well get me a new one,' " Mr. McNair said.

Large existing landlords also are getting into the construction game as a way to renew their portfolio and retain existing tenants who want new, more efficient office space.

The new construction will begin to have a significant effect on the market in 2009, when close to 11 million square feet in new space will open -- a 2.7-per-cent increase to the national market, figures compiled by real estate firm CB Richard Ellis show.

That will be the largest chunk of new office space to hit the market in almost two decades, but it is still far less than was built during the last boom. In 1990, when building

reached its peak, close to 18 million square feet of office space came to market and national vacancy rates climbed to more than 15 per cent for the next five years.

Blake Hutcheson, president of CB Richard Ellis Ltd. in Canada, said the size of this wave of building is unlikely to have the same effect.

"In no way do we think there is a supply problem, not now, not in five years," he said. "This is a modest replenishment at a conservative level in a country that has been starving for new product for a decade."

But Mr. McNair said, "2009 is when it is going to get interesting," adding that the real issue will likely be landlords with older stock, especially in the Toronto market. The new generation of office towers now under construction will offer advances in technology and environmental building techniques. Those features could be a huge draw for tenants looking to reduce operating costs and retain staff.

In Calgary, Mr. McNair said the risk to new projects is the rising cost of construction and labour shortages. Demand is clearly there for new buildings, but getting them up is the greatest challenge, he added.

Looking ahead, Mr. Hutcheson said he expects the construction activity to continue next year, especially in Calgary where several projects are in the planning stages. Building an office tower can take anywhere from five to six years from conception to completion, he said, and many major projects are gearing up, including EnCana Corp.'s large new head office.

"It clearly is true that the construction business is back," he said.

Remaking the skyline

After more than a decade of relative quiet, Canadian developers returned to the downtown office market in full force in 2006 with a flurry of projects across the country. The most activity, by far, is taking place in Toronto -- the country's largest office market -- and Calgary, where vacancy rates for prime space are now lower than anywhere else in the world. Some examples:

TORONTO

Bay-Adelaide Centre

333 Bay St.

Owner: Brookfield Properties

Number of floors: 50

Completion date: 2009

RBC Centre

155 Wellington St. W.

Owner: Cadillac Fairview Corp. Ltd.

Number of floors: 43

Completion date: 2009

Telus Tower

25 York St.

Owner: Menkes Developments

Number of floors: 30

Completion date: 2009

CALGARY

Centennial Place

4th St. and 3rd Ave. S.W.

Owner: Oxford Properties

Number of floors: 40

Completion date: 2009

Livingston Place, Phase I &II

2nd St. and 3rd Ave. S.W.

Owner: Bentall Capital and bcIMC

Number of floors: 21 in each tower

Completion date: 2007

Jamieson Place

302 4th Ave. S.W.

Owner: Bentall Capital and bcIMC

Number of floors: 38

Completion date: 2009