The Office Report Q4 2012

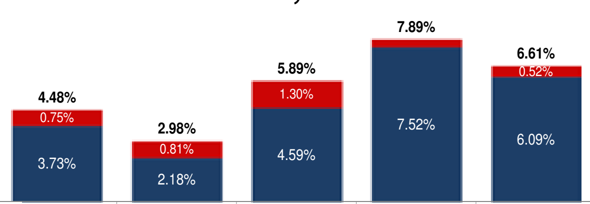
AVISON YOUNG Intelligent Real Estate Solutions

Calgary Overall - Vacancy 4.5%

Although still below the 5% mark, vacancy in Calgary's office leasing market has risen for the first time in 9 quarters. Although this may be interpreted as the front-end of a market swing, it is likely that vacancy will continue to remain low in the short term due to persistent demand for quality space. Overall market absorption spiked to an enormous 1.8 million sq. ft. for the quarter, entirely due to the completion of the Bow in Downtown, making overall annual absorption for the year reach 3.1 million sq. ft. This may appear to indicate healthy growth and activity, but excluding the Bow would cause absorption to fall well below the 5-year average, providing evidence towards a decelerated leasing market. It is difficult to determine whether the poor absorption for the quarter was a function of scarcity or a function of diminished demand. The fact that Class AA/A vacancy remains so low supports the argument that absorption is languid due to scarcity. On the other hand, energy corporations would not hesitate to lease any available space if it was imperative to their operations, meaning that demand could also be exemplified through Class B/C absorption in the Downtown. The fact that both B and C Class vacancy in the Downtown rose throughout the quarter implies that demand may in fact be tapering.

Calgary's economic indicators remain strong when compared to weakening national figures. National GDP growth failed to reach an already low forecast of 0.8% year-to-date for the third quarter, climbing to a meager 0.6%. The shortcoming of GDP can largely be attributed to exports realizing their worst rate of decline in three years. In Alberta, annual GDP growth was expected to expand by 3.7% by year end 2012, which was nearly double the growth forecast for Canada and the US, and is forecasted to expand by 3.5% in 2013. Unemployment in Alberta remained the lowest provincial rate in the country, resting steadily at 4.4% as of November. Despite a boom in consumer spending, falling oil and gas prices continue to produce a sense of caution within Alberta's economy. Drilling activity in Alberta fell below 2011 figures for the seventh straight month in December with 284 active rigs. This figure represents a 17.4% drop in activity year-over-year, with B.C. and Saskatchewan experiencing similar declines in activity of 20.4% and 12.6%, respectively. Natural gas prices are expected to remain compressed in 2013. Pipelines leading out of the province are also effectively full, causing the value of crude oil to deteriorate. As a result, producers are scrambling to find new ways to export product into the US market, including the use of rail cars. This has added pressure towards the stalled Keystone XL pipeline, which would increase overall exportation capacity to the Pacific Rim and US markets. Furthermore, this has also added pressure towards market diversification efforts. Most notably, Enbridge's proposed Northern Gateway pipeline will open new markets in Asia and vastly increase the volume of international exports, yet remains hindered by political impediments.

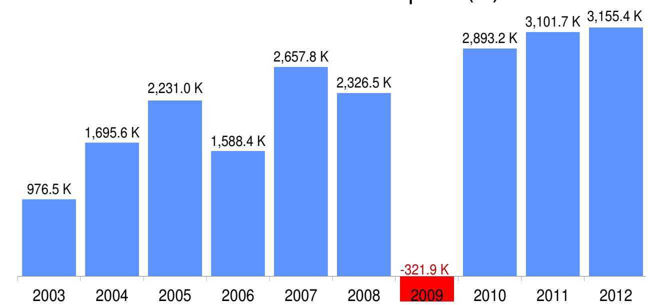
Overall Calgary
Office Vacancy Rates



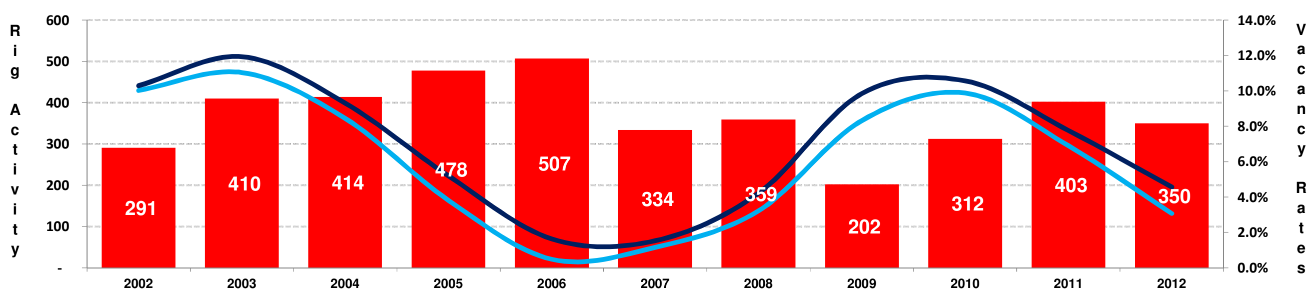
Class	Overall	Downtown	Beltline	North	South
Total SF	66,300,000	40,700,000	6,500,000	8,700,000	10,400,000
Quarterly Change	0.18%	0.15%	0.86%	0.03%	0.01%

Headlease Sublease

Overall Calgary
Annual Office Absorption (sf)



Canadian Drilling Rig Activity & Calgary Office Vacancy Rates



*Source: Canadian Association of Oilwell Drilling Contractors

Vacancy Rates calculated as a 4-quarter average

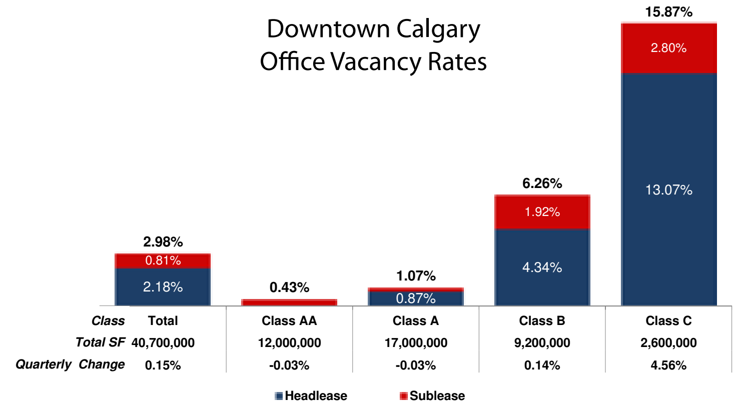
Downtown - Vacancy 3.0%

Calgary's downtown leasing market continued to remain stagnant with a vacancy rate increase of 0.15%. This was driven largely by a rise in Class C vacancy, which grew from 11.3% to 15.9% since last quarter. Quarterly absorption spiked to an enormous 1.7 million sq. ft. as a result of the Bow coming online. This figure, however, poorly reflects the pace of the downtown leasing market, as overall absorption was less than the amount of absorption added by the Bow. This means that already existing space ultimately experienced negative absorption. There are numerous factors that may be driving this trend; most significantly, the lack of quality space in the downtown is causing tenants to consider the Beltline and Suburbs as viable options. This pattern becomes clear when observing Class A absorption over the last 8 quarters, which continued to see growing levels of activity in the Beltline and Suburbs while Downtown activity diminished (fig. 1).

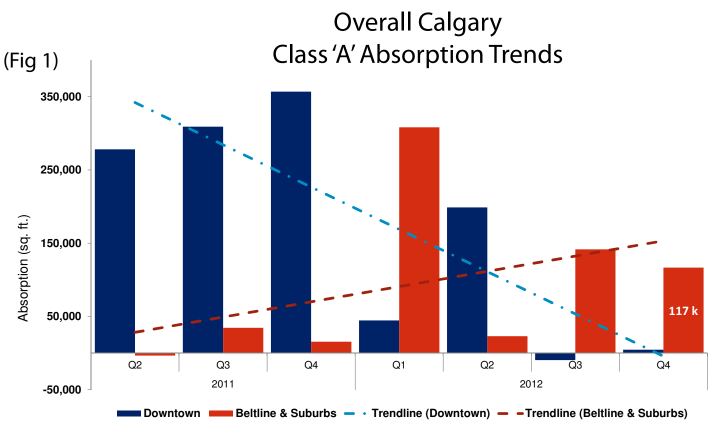
Heavy demand, combined with the lack of available options, continued to fuel a "flight to quality" trend within the downtown office leasing market. Tenants seeking higher quality space relocated to whatever better space became available, producing a domino-effect as tenants further down the chain leased up their previous occupancies. This flight to quality pattern effectively pushed C Class vacancy up, as previous C Class tenants continued to seize the opportunity to move into Class A and B spaces. Supporting this claim is the trend of Class B/C space continuing to comprise the highest percentage of vacancy within the downtown (fig. 2). This movement has spurred the redevelopment of many Class C properties in the Central Business District in an effort to bring higher quality options to market.

The biggest news with potential impact on the downtown leasing market was the federal approval of both the Nexen and Progress Energy takeovers by CNOOC and Malaysia's Petronas, respectively. Notably, under new rules implemented by Prime Minister Stephen Harper's cabinet, these deals would not receive approval. This has made it much more difficult for state-controlled enterprises to buy major energy companies. A more realistic option for international investment into the market is now through non-controlling joint venture agreements. This claim is supported by Encana's recent announcement of a $2.18 billion joint venture with PetroChina, which came less than a week after Harper's cabinet clarified rules on state-owned enterprise investment. Future joint venture agreements could have a significant impact in the downtown leasing market, opening up new availabilities as energy companies initiate new projects with international partners.

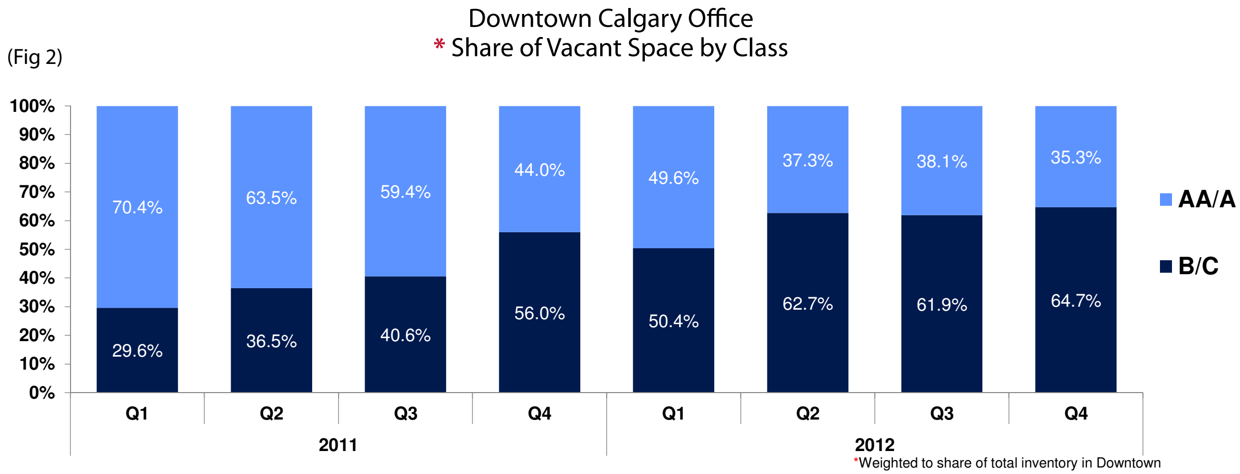
The Bow - Completed Q4 2012

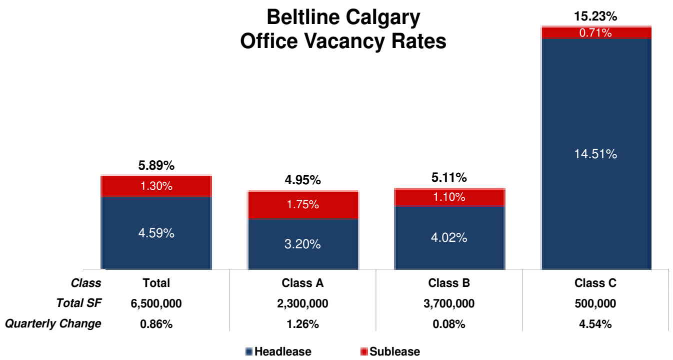


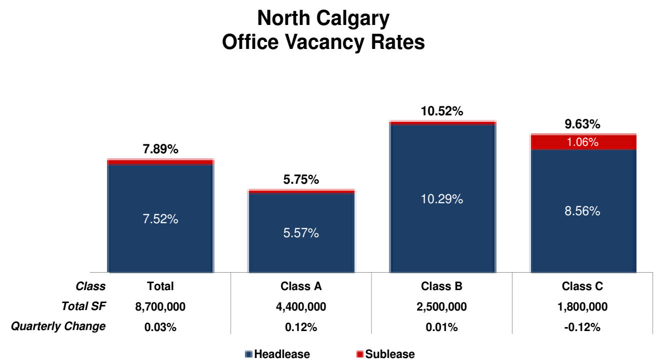
(Fig 1)

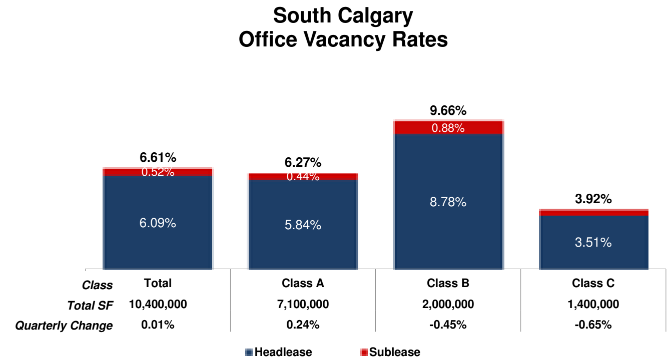


(Fig 2)









Beltline - Vacancy 5.9%

Vacancy in the Beltline differed from its most recent downward trend and experienced a 0.86% rise in overall vacancy. All property classes experienced rises in total vacancy, including Class A inventory which witnessed a significant vacancy increase of 1.26% since last quarter. As such, the Beltline experienced negative absorption for the first time in 5 quarters, amounting to -58,000 sq. ft. This may be the result of tenants seeking more affordable space in the suburbs; however, it is more likely to be a short-term anomaly rather than the front-end of a downward trend. High demand for space in the Beltline can still be exemplified through recent deals in new developments, including Matrix Solutions leasing 104,000 sq. ft. at Eleventh Avenue Place and Centre 10 becoming the future home for the National Energy Board, and Mawer.

A number of new developments coming to market should attract the attention of tenants seeking quality space in the Beltline. Notable projects include Centre 10, 20/20, Maxwell Bates and Eleventh Avenue Place, which will add 723,000 sq. ft. of new inventory to the Beltline in 2013. Once these developments are completed, expectations are that vacancy will continue downward as a direct result of scarcity in the downtown.

Suburban North - Vacancy 7.9%

The Suburban North office leasing market experienced minimal changes since last quarter. Vacancy remained flat at 7.9% due to a modest positive absorption of only 19,000 sq. ft. overall. This does not come as surprise, considering the Suburban North has yet to garner enough demand to attract the attention of significant office developers. Therefore, the North has yet to generate construction cycles like those seen in the Central Business District and Suburban South. The only new property completed was the Royal Vista Professional Centre, adding 38,000 of Class A space to the market.

Lower rental rates may effectively be drawing the attention of tenants seeking to escape increasing rental rates in the central business district. However, with a cumulative total of 255,000 sq. ft. of Class A space available, options are limited for tenants who seek to occupy large amounts of high quality space. Currently, the only development coming to market in 2013 is the Maple Reinders Building, which will add 19,000 sq. ft. of Class A space to the market. If demand spill-over from the core continues to push vacancy downward, it is possible that the North will see significant projects moving forward in the near future.

Suburban South - Vacancy 6.6%

The Suburban South continues to be one of the fastest growing and exciting markets for office leasing within Calgary. Approximately 256,000 sq. ft. of new inventory was added this quarter by completions at Quarry Park and Westmount Corporate Campus. Quarterly absorption spiked to 235,000 sq. ft., indicating healthy growth and activity within the market. Both Class B & C witnessed noteworthy decreases in vacancy, supporting the trend of central business district tenants relocating to suburban areas. Asking rates for Class A and newly constructed spaces were between $24 and $27 net per square foot on average.

A significant amount of new inventory is slated to become available in 2013. Noteworthy projects include West 85th and Westmount Court, which will add 59,000 sq. ft. of new inventory in the first quarter of 2013. Remington's Quarry Park is in the mix with 800,000 sq. ft. of space being built for Imperial Oil and another 350,000 sq. ft. of space being built on speculative basis. Demand spill-over from the core continues to be the key driving force for development in the Suburban South.

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AVISON YOUNG FEATURED OFFICE LISTINGS

444 Seventh
444 - 7th Avenue SW

108,455 SF Contiguous
+/- 247,362 SF (Fall 2016)
Downtown Office
Lease Opportunities

Trimac House
800 - 5th Avenue SW

38,538 SF of contiguous office space
Full Floor Opportunities
Downtown Office

1108
1108 - 4th Street SW

Up to 186,000 SF
Beltline Office
Lease Opportunities

634
634 - 6th Avenue SW

6,000 SF Floor Plates
Downtown Office Condos
Lease/ Sale Opportunities

Snowdon Block
2010 - 11th Street SE

22,284 SF Total
Suburban Office
Lease Opportunities

Maxwell Bates Block
2207 - 4th Street SW

32,925 SF Total
Suburban Office
Lease Opportunities

Zurich Court
1538 - 25th Avenue NE

47,402 SF Total
Main and 2nd Floor
Suburban Office
Lease Opportunities

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