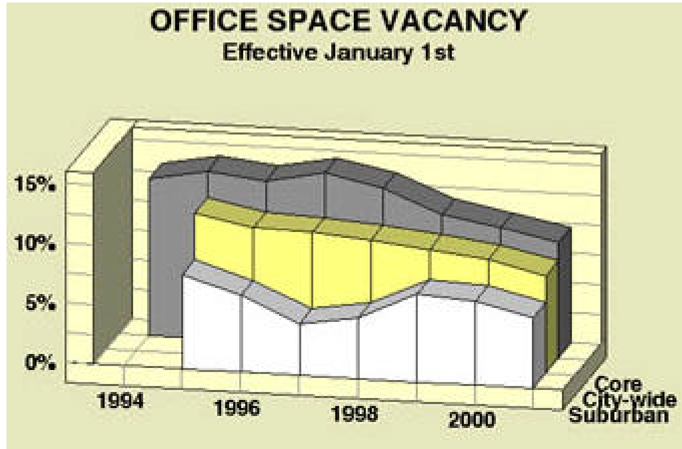
2000 to 2001 Saskatoon Office Study

by Tim Ochitwa and Doug Martin, AACI

1.0 Highlights



The forecast of “fragile optimism” was warranted coming into 2001. The activity level from the previous years carried into the year with modest improvements in most categories of the market. This resulted in an overall reduction in city vacancy from 9.2% to 8.1% with noticeable improvement in the central core neighbourhood where vacancies decreased from 10.6% to 9.6%.

- Vacancy in the suburban market also decreased from 7.1% to 5.9% with a solid absorption level of some 47,000 square feet. The positive absorption came from all sectors of the office market and was not the result of any major shift in one neighbourhood, simply a market strengthening throughout.

- The Saskatoon Public School Board reversed plans to renovate the Bay Store. They have purchased, and are in the process of renovating the former Army & Navy building. It is in the process of being converted from a retail use to office space and will include approximately 16,684 sq.ft. of office space for rent. This area was not included in this report as it is not ready for occupancy.

- **New construction** in 2000 was limited to an office building in the Sutherland Industrial neighbourhood.

- The only significant office sale in 2000 was the Royal Bank Building, for $4,000,000 or $117.94/sq.ft. rentable. The major tenant in the building is the Royal Bank which is signed to a long-term lease. This purchase by Princeton Developments Ltd. ties up the majority of the block. Princeton have announced intention to develop a retail strip development on 21st Street to incorporate part of this Royal Bank site.

- The "South Downtown" site remains in the news. This is the block bounded by 1st and 2nd Avenues and 19th and 20th Streets. Plans for a 91,000 sq.ft. retail development including a ten-screen theatre complex; a book store; plus additional retail; and underground parking were delayed again due to some financial turmoil of the main tenant, Cineplex Odeon. Princeton states they hope to be able to salvage the project once restructuring is completed.

- SaskTel has recently down-sized which resulted in a large block of space available in the rental market.

- There are two potential development sites in the downtown core were in the news. Both sites are located on 22nd Street. The site at the corner of 1st Avenue East, presently a SaskTel parking lot, is in a pre-leasing state with the potential for a multistorey commercial/office building. The site at the corner of 3rd Avenue East was purchased in 2000 with no announcement or time frame regarding potential development yet.

2.0 Forecast

The forecast for the central core and the suburban markets continues to be cautiously optimistic for 2001. The general outlook and mood of individuals involved in both the office market and other sectors of the market going into 2001 is positive, but reserved. Commercial real estate agents are reporting high levels of activity. Tempering this optimism is a realization that the community relies heavily on the resource and agriculture sectors of the economy. With world commodity prices having gone through further turmoil during 2000, there is an underlying mood of caution.

- Rental rates are expected to remain fairly stable in 2001. With the better quality rental space in the core showing vacancy levels in the 15% range, owners will have marginal opportunity to increase effective net rental rates.

- The Synchrotron facility at the University of Saskatchewan is under construction and expected to add to the “optimism” level in the marketplace although major additions to the office market are not contemplated as a result of this project. Studies of other cities with synchrotrons, conducted at Innovation Place, suggest the facility will have a positive effect on the office market, but not require significant new office development.

- The anticipated construction start on the South Downtown retail development by Princeton will have a significant impact on the central core; further entrenching the core, along with the Midtown Plaza, as the major centre for retail in the city.

- Two larger “blocks” of space are available for lease in the core, the result of government tenants being relocated.

In summary, the outlook is similar to the previous year with a modest improvement anticipated.

3.0 Study Criteria

The study area is broken into two major components. The central core area is considered separately from the suburban space.

The study includes above-grade office space and excludes main floor commercial retail space. The total inventory (net of demolitions or changes) was relatively stagnant during 2000 with a marginal increase from 5.17 million sq.ft. to 5.23 million sq.ft. with a 60%/40% split between core and suburban space respectively.

Building Type categories are provided as a general breakdown showing the rental space separate from government, medical and owner-occupied. Buildings are included in a category if over 50% of the use applies to one category.

Building Classes are distinguished in the rental category of space with a breakdown to Class A, AB, B or C. Items such as rental rates, quality of finish, location and age were used to determine the different categories, with emphasis on achievable rental rates.

Judgement calls are necessary for some buildings not falling clearly into one class or another. The AB category recognizes some of the city's better quality buildings, which form a significant part of the quality office accommodation in the city.

Crossover space refers to tenants in transition. The vacancy figures are as of a specific date, being January 1, 2000. Tenants occupying one space with tenant improvements underway in another location are shown in occupancy in the building they physically occupy, thus preventing double accounting.

4.0 Central Core Market

The central core area is defined by Idylwyld Drive to the west, 25th Street to the north and the South Saskatchewan River to the east and south.

Saskatoon has a relatively small central core, compared to other larger Western Canadian cities, with an inventory of approximately 3.15 million square feet. As a result, the addition of buildings in the 100,000 sq.ft. category can have a significant impact on vacancies over the short term. Establishing absorption figures over a period of time is one of the objectives of these studies. The information gathered and summarized on the following Table #1 is effective January 1, 2001.

Table #1
Central Core and Suburban Office Inventory - City of Saskatoon
Executive Summary - Effective January 1st, 2000 to January 1st, 2001

Category	Total Space Jan 1, 2001 Square feet	% of Total	Vacancy Jan 1, 2001	2001 % Vacant	2000 % Vacant	Absorption in 2000 (sq. ft.)
Rental Class A	433,842	13.8%	71,366	16.4%	14.9%	(6,895)
Rental Class AB	439,570	14.0%	51,141	11.6%	13.2%	2,650
Rental Class B	546,142	17.4%	79,515	14.6%	15.5%	4,969
Rental Class C	256,639	8.2%	56,298	21.9%	31.5%	33,594
Total Rental	**1,676,193**	**53.3%**	**258,320**	**15.4%**	**17.5%**	**34,318**
Owner Occupied	411,065	13.1%	10,025	2.4%	1.3%	(4,300)
Government	866,221	27.5%	31,246	3.6%	3.8%	1,664
Medical	191,371	6.1%	2,190	1.1%	1.6%	854
Subtotal	**3,144,850**	**100.0%**	**301,781**	**9.6%**	**10.6%**	**32,536**
Under Construction	n/a	n/a				
Total Core	**3,144,850**	**100.0%**	**301,781**	**9.6%**	**10.6%**	**32,536**
Core	3,144,850	60.2%	301,781	9.6%	10.6%	32,536
Suburban	2,077,405	39.8%	122,086	5.9%	7.0%	47,074
City Total	**5,222,255**	**100.0%**	**423,867**	**8.1%**	**9.2%**	**79,610**
Under Construction	**n/a**					

The overall vacancy level in the central core continues to improve marginally, down to 9.6% from 10.6% last year.

The biggest net change in vacancy occurred in the Class C category with a 9.6% drop from 31.5% to 21.9%. One of the main reasons for this dramatic decrease was the removal of a vacant building from this class which is now occupied by a government tenant and moved to the government category. Class A space showed a 1.5% increase to 16.4% due primarily to SaskTel down-sizing. Class AB and B space showed drops in vacancy of 1.6% and 0.9%, down to 11.6% and 14.6% respectively.

The overall performance of the central core rental space is positive, a trend which should continue, barring any major inventory additions to the market.

The improvement of the central core vacancy is a result of improvements in most categories with no major shift in tenants or addition of a major tenant to the core.

5.0 Central Core Rental Rates

Effective rental rates are the net return to the landlord after incentives for tenant improvements, free rent, and any other inducements, and represent a truer picture of market rent. During 2000 there was no significant change in effective rental rates. However, landlords have shown resistance to extreme incentives in the better quality space, a trend more prevalent a couple of years ago. With few major blocks of vacant space in the central core area, some strengthening in rental rates in the A and AB categories is suggested in 2001.

Leasing programs undertaken in 1997, with zero net effective or lower rental rates, ceased in 1998 and 1999. Effective net rental rates for Class B buildings in 2000 moved into the $2.50 to $5.00/sq.ft. range. The better quality buildings are showing net effective rents primarily in the $5.00 to $7.00/sq.ft. range. In some cases renewals are higher than this, around the $7.00 to $10.00/sq.ft. level depending upon the level of tenant finish provided in the previous term.

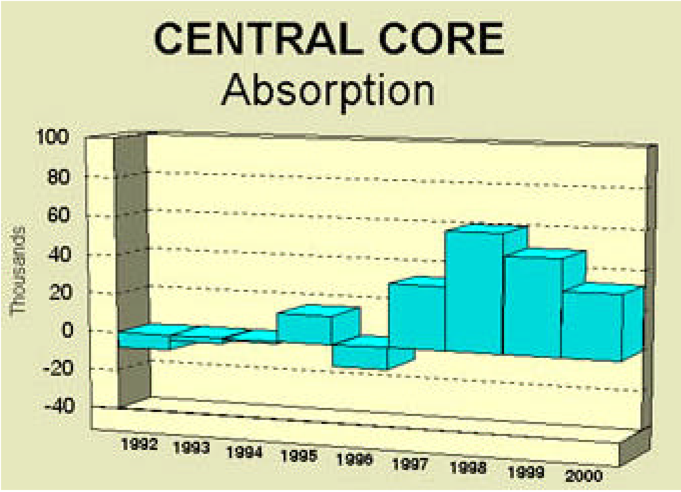
Typical tenant inducements include a $15.00 to $25.00/sq.ft. tenant improvement allowance. The higher end of this range is likely to include free rent. In other words, the inducement allowance is all-inclusive. A summary of the face rates and occupancy costs for typical classes of space is shown in Table #2 below:

Table # 2
2000 Face Rental Rates and Operating Costs by Class

Class	Asking Face Rate/Sq.ft.	Operating Cost/Sq.ft.
A	$10.00 - $13.50	$8.00 - $8.75
AB	$8.00 - $12.00	$7.50 - $10.50
B	$4.00 - $10.00	$5.50 - $8.50
C	$0.00 - $4.00	$4.00 - $7.30

The 1997 reassessment had a positive effect on most buildings in the central core through reduced operating costs. This has a positive effect on keeping tenants in the core and attracting tenants back to the core. The results of the latest reassessments are not known yet.

6.0 Central Core Absorption



The year 2000 saw a continued positive absorption of some 33,000 sq.ft., continuing a trend which began in 1997. The rental class space led the way with some 34,000 sq.ft. absorbed with positive performance in all other classes of space except Class A. The Class C space showed the largest improvement due, in large part, to a building becoming occupied by a government tenant. As suggested, no significant introduction of new tenants to the core triggered the absorption. The figures represent a modest improvement through the entire market.

7.0 Suburban Market Overview

The suburban market is divided into five location groupings. First, peripheral core space includes office buildings north of 25th Street on 2nd Avenue and other buildings in close proximity to the central core, such as Queen Street and Broadway Avenue.

Second, the North Industrial grouping includes a significant concentration of office space in the Larkhaven Industrial area, in the neighbourhood of the Saskatoon Inn, plus other office buildings scattered throughout the North Industrial area.

Third, the southeast quadrant including 8th Street East, represents a significant portion of the overall inventory at 27.7%. This quadrant excludes office space at Innovation Place on the University Campus, the fourth category, which surpassed the southeast quadrant in size in 1998.

Innovation Place now represents 28.1% of the total suburban market. This sector of the market should continue to be the fastest growing area in the City over the next few years.

Finally, the category shown as "Other" is a catch-all category for buildings not included in the main groupings, including 22nd Street West, Pinehouse Drive and other scattered locations. The largest building in this group is the Cameco Head Office building on 11th Street West, containing some 145,000 square feet.

Table #3 Suburban Office Inventory - City of Saskatoon Sorted by Location						
Category	**Total Space Jan 1st, 2001 Square feet**	**% of Total**	**Vacancy Jan 1, 2001**	**2001 % Vacant**	**2000 % Vacant**	**Absorption in 2000 sq. ft.**
Peripheral Core	233,725	11.3%	1,180	0.5%	1.3%	1,885
North Industrial	392,987	18.9%	59,406	15.1%	15.0%	24,953
South East	576,412	27.7%	43,230	7.5%	6.8%	(7,688)
Innovation Place	584,437	28.1%	7,500	1.3%	5.0%	20,718
Other	289,844	14.0%	10,770	3.7%	6.2%	7,206
Total Suburban	**2,077,405**	**100%**	**122,086**	**5.9%**	**7.1%**	**47,074**
Under Construction	**n/a**	**n/a**				

8.0 Suburban Market Vacancy and Absorption

The suburban market showed a decrease in vacancy to 5.9% from 7.1% during 2000. Absorption continued positive with 47,000 sq.ft. absorbed. The absorption represents positive performance in all neighbourhoods. The absorption and vacancy is viewed as a positive performance from the entire suburban market versus outstanding performance from any particular neighbourhood.

Innovation Place continues to show strength with 20,000 sq.ft. of positive absorption during the year. The only modest change in vacancy was due to a new building brought into the inventory in the North Industrial area.

Total absorption at 47,000 sq.ft. indicates a stable suburban market.

9.0 Face Rates and Operating Costs

Face rates in suburban office space tend to be at similar levels as the central core buildings, primarily in the $4.00 to $8.00/sq.ft. range. There are now some examples of rental rates moving above this range, up to $12.00/sq.ft. for better quality accommodation. Rates toward the lower end of the range occur in office buildings located in industrial areas, with only average levels of finish. The higher end is limited to better quality office projects.

The main difference between suburban market and the core has been operating costs and parking considerations. Operating costs run in the $6.00 to $9.00/sq.ft. range in the core. The suburban market tends to operate in the $4.00/sq.ft. to $6.00/sq.ft. level. There has been some closing of this gap with the 1997 re-assessment and the proposed shift with the latest reassessment could see this gap shrink even further. The major advantage of a suburban location continues to be the availability of parking which is generally free.

10.0 Qualification

Readers of this study are welcome to use the information as deemed appropriate, providing **Brunsdon, Martin & Associates Ltd.** is quoted as the reference source. **Brunsdon, Martin & Associates Ltd.** is a real estate appraisal firm providing a wide range of appraisal and consulting services, with the primary market being the north central portion of the Province of Saskatchewan.

Special recognition and thanks is paid to all the building owners, property managers, real estate agents and government agencies who assisted with information upon which this report is based. Without their support this study would not be possible.