EQUITON® | VIEWPOINT

Q1 2024 Commentary and Outlook:

POSITIONED FOR STRATEGIC GROWTH AT A PIVOTAL MOMENT FOR RENTALS

Throughout the first quarter of 2024, Canadian real estate navigated interest rate uncertainty, a slower economy, and stabilizing inflation as anticipation built for a potential rebound in the market.

The initial optimism over February's lower inflation waned as March posted a 10 basis-point rebound to 2.9%[1]. As such, interest rates held at 5.0% for the Bank of Canada's fifth consecutive meeting in March[2], where they remained at the end of the quarter. The central bank expects inflation to hover around 3.0%[3] until the second half of the year. Slowing economic growth[4] this past quarter bolstered the case for a mid-year rate cut — a possible turning point. Lower rates are expected to reinvigorate transaction activity across all property categories and ease construction costs.

That said, early 2024 still presents rich possibilities for investors in the Canadian multi-family space. Growing rental prices and occupancy rates maintain near-record highs, supported by ever-rising immigration and low supply. An undervalued environment provides a buyer's market, creating an opportunity to bolster portfolios with new acquisitions presenting long-term growth potential.

Against this backdrop, the Equiton Residential Income Fund Trust (the Trust) ended the quarter with a net return of 2.12% (Class F DRIP).

Rental Market Pressure to Grow in Coming Quarters

Residential transactions showed decreased activity during the quarter. In the GTA, single-family home sales fell to 51% below the 10-year average[5].

However, new listings surged in major cities[6] across Canada, suggesting potential buyers may not be far behind.

A rate cut is likely to renew confidence among prospective homeowners navigating increased living expenses and challenging mortgage rates. Regardless, for most it may not be enough to support the transition from renting to ownership. The Canada Mortgage and Housing Corporation (CMHC) projects the national average home price could reach 2022's historic $816,720[7] by 2025 and surpass it the following year. In the agency's view[8], homeownership barriers will drive record rental occupancy and rent increases on unit turnover in 2024[9].

Strong Rental Market Offers Value Amid Affordability Issues

With high prices making single-detached homes unaffordable for many, rentals continued to offer Canadians much-needed value. For example, a representative two-bedroom condo cost 40.8%[10] more to own than to rent in the GTA in Q1'24.

[1] https://www150.statcan.gc.ca/n1/daily-quotidien/240416/dq240416a-eng.htm?indid=3665-1&indgeo=0
[2] https://financialpost.com/news/economy/bank-of-canada-holds-interest-rate-march-6-2024
[3] https://www.bankofcanada.ca/2024/04/mpr-2024-04-10/
[4] https://thoughtleadership.rbc.com/forward-guidance-our-weekly-preview/
[5] https://www.bildgta.ca/march-shows-third-month-of-record-lows-for-new-home-sales-presenting-unique-buying-opportunity-for-new-home-purchasers/
[6] https://trreb.ca/wp-content/files/market-stats/market-watch/mw2404.pdf
[7] https://www.crea.ca/media-hub/news/february-home-sales-rise-as-buyers-scoop-up-first-of-the-2022-spring-listings
[8] https://assets.cmhc-schl.gc.ca/sites/cmhc/professional/housing-markets-data-and-research/market-reports/housing-market-outlook/2024/housing-market outlook-spring-2024-en.pdf
[9] CMHC 2024 Market Outlook.
[10] https://www.nbc.ca/content/dam/bnc/taux-analyses/analyse-eco/logement/housing-affordability.pdf

In Vancouver, the expenses of owning a representative two-bedroom condo exceeded renting by 66.3%. Meanwhile, in relatively affordable condo markets, such as Ottawa and Edmonton, the difference worked out to 10.5% and 9.2%, respectively.

In March, purpose-built apartment rents grew by an average of 12.7% Y/Y[11] versus rental condos' 3.9% Y/Y nationally. Demand remained favourable in the Greater Toronto and Hamilton Area. Vacancies declined in the last quarter despite the significant addition of 1,700 new rental units[12].

Rentals and Condos Lead New Canadian Housing Development

The past year's economic challenges sidelined many single-detached homebuilders well into the quarter. Housing starts in the category dropped 20.0% Y/Y[13] in major Canadian cities at the end of 2023. However, robust purpose-built rental and condo apartment construction, up 7.3% the same year, helped offset overall homebuilding declines.

Purpose-built rental starts slowed in the quarter but were up 176% since construction activity hit a low in Q3'22. Meanwhile, purpose-built rental units under construction reached a multi-decade high[14]. That said, CMHC anticipates[15] that these units will fail to meet outsized demand as they come online in future quarters. Accordingly, high-cost-of-living regions like the GTA will continue to experience tight rental markets.

Mitigating Construction Headwinds Through Self-Performing Capabilities

Industry organizations attribute growing rental construction, in part, to recent government policies. Both low-interest loans and the removal of federal and provincial taxes on purpose-built rentals have helped improve certainty for builders. Additionally, the Province of Ontario tabled changes[16] designed to limit municipal development proposal wait times to 90 days. While a welcome start, policy changes alone will not necessarily erase key obstacles to scaling up construction.

For instance, government charges and fees have come to represent more than 31.0%[17] of the total cost of building a home in major cities. A significant reduction in taxes on development and construction would provide a much-needed boost for the sector. The Canadian Chamber of Commerce's Housing and Development Strategy Council* recently recommended expanding tax relief to rental projects under construction. A shortage of skilled labour has contributed to elevated construction costs, presenting a challenge of its own.

As governments weigh courses of action, Equiton has taken a proactive stance to mitigating prevailing uncertainties. The firm's development arm, Equiton Developments, is in the process of building its self-performing construction capabilities. Bringing construction in-house will enable Equiton to manage its own timelines and create operational efficiencies in all economic environments.

**Equiton is a member of the Housing and Development Strategy Council*

[11] https://rentals.ca/blog/april-2024-rentals-ca-rent-report
[12] Zonda Urban National Rental Take Q1-2024
[13] https://www.cmhc-schl.gc.ca/media-newsroom/news-releases/2024/apartment-construction-sustains-housing-starts
[14] https://www.urbanation.ca/news/gtha-condo-rents-down-7-past-6-months
[15] https://www.cmhc-schl.gc.ca/professionals/housing-markets-data-and-research/market-reports/housing-market/housing-market-outlook
[16] https://ontarioplanners.ca/inspiring-knowledge/policy-submissions-legislative-corner/legislative-corner/press-releases/2022/bill-109,-more-homes-for-everyone
[17] https://indd.adobe.com/view/a9fd23de-79a7-484f-a423-b58e29f2776d

In partnership with Ottawa developer Main and Main, Equiton is expected to bring the first tower of its 1,100-unit Maison Riverain project online in early 2025. Future phases will benefit from federal and provincial tax cuts on purpose-built rentals.

Non-Permanent Resident Caps Anticipated to Have Low Immediate Impact

In order to ease extreme housing pressures, the federal government has taken steps to pare back temporary resident arrivals[18] with the intent to reduce temporary residents to 5.0% from 6.5% of the total population over the next three years. This would cut Canada's roughly 2.5 million non-permanent residents by about 20.0% from current levels.

Similarly, Canada will implement a temporary cap on new international study permits, reducing admissions by 35.0%[19] in 2024 and 2025. These changes are expected to disproportionately impact Ontario and British Columbia, where many temporary residents arrive.

The impact of these immigration caps may be short-lived due to the rate at which demand is growing. For example, reduced student admissions could moderate rental growth in the near term, but are unlikely to reduce overall demand.

Given these points, permanent immigration to Canada remains a chief contributor to mounting housing demand. Federal government immigration targets[20] will admit 485,000 permanent residents in 2024. In addition, another million are expected in 2025 and 2026.

The rapid pace of Canada's population growth now ranks it among the fastest-growing advanced economies[21].

According to CMHC, maintaining current immigration trends through 2030 would require an additional four million housing units to restore affordability. Equiton has focused its acquisitions on high-growth regions, particularly the GTA, to meet demand for housing where it is highest.

Federal Housing Plan and Budget Outlook

This past quarter saw the introduction of a new federal housing plan[23] and budget.

Generally, the government's housing plan pledged several measures to make home ownership more attainable in addition to increasing housing supply. To that end, the government expanded its low-cost rental construction loan program by an additional $15 billion. Also, it committed $6 billion to infrastructure and plans to open underutilized public lands for development. The plan's ambitious target is to encourage the creation of 3.87 million homes by 2031, with a focus on rentals.

Demand-side measures gave first-time homebuyers access to 30-year mortgages when buying new builds and an increased $60,000 withdrawal limit for the RRSP Homebuyers Plan. The government also barred corporations from purchasing single-family homes. The targeted nature of these measures is unlikely to stoke undue demand among prospective owners. On the other hand, overall construction productivity may receive a much-needed boost.

[18] https://www.reuters.com/world/americas/canada-plans-reduce-temporary-residents-cap-future-intake-2024-03-21

[19] https://www.canada.ca/en/immigration-refugees-citizenship/news/2024/01/canada-to-stabilize-growth-and-decrease-number-of-new-international-student-permits-issued-to-approximately-360000-for-2024.html

[20] https://www.canada.ca/en/immigration-refugees-citizenship/news/notices/supplementary-immigration-levels-2024-2026.html

[21] https://www.bloomberg.com/news/articles/2024-03-27/population-gains-in-canada-set-record-but-slower-growth-ahead

[22] https://assets.cmhc-schl.gc.ca/sites/cmhc/professional/housing-markets-data-and-research/market-reports/housing-supply-report/housing-supply-report-2024-spring-en.pdf

[23] https://www.pm.gc.ca/en/news/news-releases/2024/04/12/announcement-canadas-housing-plan

Capital Gains Tax Increase May Impact Some, But Not All, Real Estate Investors

Beyond housing and affordability measures, the federal budget increased the capital gains tax inclusion rate effective June 25. Individuals will pay taxes on 66.7% of realized capital gains exceeding $250,000, while companies will pay the higher inclusion rate on all investment profit.

Equiton expects individual real estate owners, a significant portion of the rental market, to pause transactions in the short term to avoid incurring higher tax charges. "Mom-and-pop" investors own 23.0% of condos and 11.2% of houses in Canada, more than corporate and foreign investors combined[24].

As such, institutional real estate corporations will likely execute the majority of transactions this year. With access to large pools of free capital, they are strongly positioned to buy and sell assets strategically.

The Importance of Resident Satisfaction

Building vibrant communities and fostering resident satisfaction remain key to growing a resilient business. Satisfied residents have longer tenures and contribute to higher occupancy rates, providing a source of stable, long-term rental returns.

Exploring this dynamic, Equiton began monitoring resident satisfaction measures portfolio-wide as part of its Environmental, Sustainability, and Governance (ESG) efforts. The first full year of results available in Q1'24 revealed a 7.2% Y/Y increase in overall satisfaction among Equiton residents.

This improvement reflects the effectiveness of Equiton's active approach to property management. Its subsidiary, Equiton Living, stations trained Resident Managers at every property to maintain open communication and respond to resident needs. Three Equiton properties won the 2023 SatisFacts Resident Satisfaction Award, which recognizes superior resident satisfaction and retention rates, in Q1'24.

Green Upgrades Produce Long-Term Benefits

As Canada builds toward a net-zero future, energy-efficient improvements to existing housing play an increasingly essential role. Upgrades to building envelopes, appliances, and electrical and water systems provide lasting environmental benefits and reduce costs.

As a contributor to climate efforts, Equiton continued to make property upgrades that generate cost savings over the long term. This past quarter, key properties comprising 200+ units received motion-sensing LED lighting throughout common and parking areas. These improvements are expected to reduce hydro consumption by dimming when not in use. To reduce water consumption, Equiton's water fit-up program installed showerhead regulators and replaced toilets at properties totalling 150+ units.

This builds on Equiton's longstanding hydro and water sub-metering programs, which incentivize residents to conserve utilities.

Equiton has continued to make progress on its waste audit program. The program monitors waste outflow with the aim of reducing costs. Next quarter, Equiton expects to complete waste audits across all properties and continue lighting, water, and boiler-room upgrades.

[24] https://www.theglobeandmail.com/business/commentary/article-housing-crisis-residential-home-sales-investors/

A Turning Point for Canadian Real Estate?

Key rental measures experienced marked growth in Q1'24 even as the market shifted from last year's record-setting pace[25]. Housing affordability pressures and population growth continued to drive rents, while new rental supply was quickly absorbed. Rentals continue to provide Canadians with an alternative to less accessible housing options.

Into the second quarter, macroeconomic conditions — such as slowing inflation and employment[26] — increasingly indicate that a favourable interest rate decision could be feasible this year. If a rate cut occurs, investors could anticipate revitalized conditions for construction, financing, and acquisitions. As the year unfolds, Equiton continues to actively monitor the market to uncover opportunities to improve resident satisfaction and reward investors.

[25] https://equiton.com/2023-rental-market-commentary/
[26] https://thoughtleadership.rbc.com/the-canadian-economic-slowdown-is-not-over/

Forward-Looking Information

Certain information in this communication contains "forward-looking information" within the meaning of applicable securities legislation. Forward-looking information may relate to future events or the Trust's performance. Forward-looking information includes, but is not limited to, information regarding the Trust's distributions, growth potential and volatility, investor returns, ability to achieve operational efficiencies, objectives, strategies to achieve those objectives, beliefs, plans, estimates, projections and intentions; and similar statements concerning anticipated future events, results, circumstances, performance or expectations and other statements that are not historical facts. These statements are based upon assumptions that the management of the Trust believes are reasonable, but there can be no assurance that actual results will be consistent with these forward-looking statements. Forward-looking information involves numerous assumptions, known and unknown risks, and uncertainties that contribute to the possibility that the forward-looking statements will not occur and may cause actual results to differ materially from those anticipated in such forward-looking statements. Some of these risks are discussed in the section "Risk Factors" in the Offering Memorandum. These forward-looking statements are made as of the date of this communication and the Trust is not under any duty to update any of the forward-looking statements after the date of this communication other than as otherwise required by applicable legislation.

For more information, please contact:

Geoff Lang
Senior Vice President, Business Development,
Advisor Channel, Equiton Capital, Wholesale
E: glang@equiton.com
T: 1.416.758.8700 x103