

## My Thesis Revisited

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On April 5, 2021, I published [My Thesis](#). In it, I predicted that “the global pandemic of 2020-2021 will benefit the commercial real estate industry by accelerating three established secular trends—(i) urban intensification, (ii) humanistic operation and (iii) stress-tested leadership”. At the outset, I noted the following: “I can’t prove my thesis. Only human behaviour over time will do that...or not. What I can do is articulate the historical basis for predicting what I believe will happen. History’s a good guide, though not a perfect one.” In conclusion, I noted the following: “I look forward to learning more as this plays out, and I have no doubt there will be surprise along the way.”

There has been no shortage of surprise in the last three years, but it has been more cyclical than secular, more geopolitical than local, and it has brought significant short-term challenge and possible long-term opportunity. Despite the surprise, I believe human behaviour has generally supported my thesis with respect to ongoing urban intensification. Cities worldwide continue to thrive and expand, though certainly not without ongoing cyclical and logistical challenge.

There remains no shortage of contrary views. They tend to dominate the public narrative, at least in North America. The most emphatically contradictory view is that many cities in North America will descend into an “urban doom loop” as a result of the pandemic.

### I. THE URBAN DOOM LOOP

It goes like this. In response to the global pandemic, people flee the cities. As a result, demand for urban housing and urban commercial real estate declines precipitously, ultimately putting material downward pressure on the municipal tax base, which in turn erodes municipal services and intensifies all forms of urban malaise, especially crime, all of which induces more people to flee the cities, and on and on in a continuous downward spiral.

This just hasn’t happened, not in American cities and not in Canadian cities. One of the more informative articles in this regard, [Whatever Happened to the Urban Doom Loop?](#) by Rogé Karma, was published in *The Atlantic* on March 22 of this year. It’s an opinion piece, to be sure, but the human behaviour it describes in respect of American cities is difficult to contradict. Allied’s similar experience in Canada’s major cities is as difficult to contradict.

Why then has this dire prediction become such a pervasive part of the public narrative in North America? In part, it’s because the notion of post-pandemic urban doom has been confused with a very real and challenging cyclical reality.

## II. THE CYCLICAL DOWNTURN

This manifested itself in 2022 when central banks worldwide began responding to intense inflationary pressures by raising interest rates rapidly and dramatically, which impacted many sectors, including of course commercial real estate. Given the economic excesses that arose from years of extraordinarily “cheap” capital, the rapid escalation in interest rates was necessary and will prove to be curative.

More than any imagined downward spiral, the rapid escalation in interest rates put owners of commercial real estate under pressure. While significant, this pressure is not an existential threat to most owner-operators of Canadian commercial real estate. Operating fundamentals deteriorated and continue to be challenging, especially in the office sector. This separated the “haves” from the “have-nots” among the owner-operators of office space in Canada, with those focused on distinctive urban office space in mixed-use, amenity-rich neighbourhoods being among the haves.

In my view, all major owners of **urban** office space in Canada’s major cities are among the haves. All have strong balance sheets and highly developed operating capability. All remain under significant cyclical pressure, from which they’ll emerge stronger in the years to come, but they’re certainly not succumbing to any kind of urban doom loop. Indeed, the major owner-operators of urban office space in Canada’s quartet—Montréal, Toronto, Calgary and Vancouver—will perform well coming out of the downturn. And while it never feels that way in the throes of a downturn, all downturns come to an end and give way to recovery.

## III. THE FUTURE OF CANADIAN COMMERCIAL REAL ESTATE

This brings me to revisiting my original thesis.

Most of the behaviour I’ve observed in the past three years suggests that Canadians remain committed to the city as the principal venue for living, working and playing. Demand for urban accommodation has not declined, but rather accelerated, putting upward pressure on prices and rental rates. Demand for urban office space did not collapse, though the supply-demand dynamic currently favours users and has put downward pressure on net-effective rental rates. Although urban retail users bore the economic brunt of the pandemic, they looked right through it in the end and continue to commit to strong urban locations on terms favourable to owner-operators.

Canadians are betting on, and committing to, the city more than ever, in part because the pandemic made us aware of how much we cherish the rich and varied attributes of urban life and how much we took them for granted until we were sent *en masse* into domestic isolation for a protracted period of time. Perhaps most importantly, as has been the case throughout recorded history, **the city continues to be where everything that constitutes human culture receives its most intense, diverse and consequential expression.** For these reasons, I continue to predict that urban intensification will accelerate in Canada and throughout the world.

The pandemic heightened the importance attributed to ESG and EDI. In the past three years, vocal opposition has emerged, much of it in the context of highly politicized culture wars in North America. There’s also been more thoughtful assessment in Canada of certain historical premises underlying substantive elements of EDI, with a particularly strong reaction to the proliferation of cancel culture. This ongoing assessment will refine our understanding of, and commitment to, ESG and EDI, not undermine it. This entire process is very human, and as such it won’t be simple, linear or free of controversy. Nevertheless, I continue to predict that these critical elements of humanism and social responsibility will humanize the operation of commercial real estate going forward.

The pandemic stress-tested the next generation of leadership in Canadian commercial real estate. In the past three years, the stress-testing took on an altogether different form, but with similar positive effect. The founding generation was stress-tested in the severe cyclical downturn of 1990s and was instrumental in reconstructing the industry as the downturn gave way to recovery. The founding generation continues to give way to its successor generation. Because of the pandemic and the cyclical downturn, the successor generation has undergone crisis-conditioning in a meaningful and beneficial way and will be better prepared to guide the industry into the future.

To summarize, my thesis continues to be based on how I expect future evolution in Canadian commercial real estate to flow from past evolution. Commercial real estate is not static; it's wholly dynamic, like all other business activities. Because of historic and recent human behaviour, I continue to believe strongly in the three secular trends I discussed in My Thesis—(i) urban intensification, (ii) humanistic operation and (iii) stress-tested leadership.

My job over nearly four decades has been to anticipate how commercial real estate will evolve in Canadian cities. My job today is to anticipate how it will evolve going forward, particularly as it relates to Allied's business. Allied owns and operates three categories of distinctive urban office space in Canada's major cities—**Allied Heritage** ("Class I office space"); **Allied Modern** (office space developed or redeveloped in the last decade); and **Allied Flex** (office space in buildings on underutilized land to be redeveloped in the next decade). There is evident and quantifiable demand for all three categories of office space, which is consistent with my belief in urban intensification. There is strong and quantifiable engagement among users of Allied office space, which is consistent with my belief in humanistic operation. The next generation of leadership at Allied is in place and performing well, which is consistent with my belief in stress-tested leadership.

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This commentary contains forward-looking information, including statements about (i) the possible evolution of Canadian commercial real estate and (ii) the possible acceleration of secular trends in Canadian commercial real estate. Although the forward-looking information is based on what the writer in his capacity as Founder & Executive Chair of Allied believes are reasonable assumptions, there can be no assurance that this information will prove to be accurate. This commentary reflects perspectives and beliefs as of April 5, 2024, and Allied undertakes no obligation to update forward-looking information, except as required by law. Allied cautions the reader not to place undue reliance on this information.