AVISON YOUNG

FEBRUARY 2017

Debt Market Monitor

National Debt Capital Markets Services

Fed challenged by higher interest rates and stronger U.S. dollar

The new U.S. administration has a bit of a dilemma on its hands: To raise interest rates or stand pat for a longer period. Interest-rate increases could throw a wrench into the growth engine, and taking no action on interest rates allows a government-stimulated economy to advance synthetically.

The economy seems to be gaining traction, and some observers have gone so far as to say that there is a mini-economic boom on the horizon. The 4.6% jobless rate is now below what policy makers believe is the "natural" or normalized unemployment level in the U.S. Even the commonly referenced U6 unemployment rate declined in November 2016 from 9.5% to 9.3% – a level which is only slightly higher than the pre-crisis rate of 8.9%. This rate measures underemployment and includes part-time workers who would prefer full-time positions. So the data-dependent Federal Reserve (the Fed) moved for the second time in a decade to raise the federal funds rate. The usually reluctant Fed's move demonstrates the group's confidence in the progress that the economy has made – and that progress will continue. The Fed is highly sensitive to the inflation rate. If inflation starts to accelerate, the Fed would be forced to raise rates faster than it would like and, potentially, create the risk of a recession – the last thing that it would want.

In a rising interest-rate environment generally, the value of the currency rises as well. A stronger U.S. dollar increases the likelihood for more inflation. Increasing interest rates while keeping inflation in check is a delicate balancing act when you consider all of the variables that come into play. The recent height of the U.S. dollar marked a level not seen in more than a decade. This appreciation of the U.S. dollar has caused the Bank for International Settlements (BIA) to issue a warning that the strength of the U.S. dollar risked triggering a banking crisis in emerging markets. Emerging market non-bank borrowers have accumulated in excess of $3 trillion in U.S.-dollar-denominated debt, according to the BIA. When the dollar rises, the more expensive it becomes to pay back the debt. As the former chairman of the U.K. Financial Services Authority put it: The large increase of emerging market debt, much of it in U.S.- denominated dollars, is one of the biggest risks in the financial system right now. All that money is owed to somebody, and a failure to pay it back will cause big ripple effects.

With relatively low inflation, the Fed has been able to take its time raising interest rates. More recently, inflation has been gaining some momentum; and, if it continues along the current trajectory, the Fed may be forced to play its hand earlier than preferred. By most accounts, predicting the Fed in 2016 was difficult; however, predicting the Fed in 2017 will be even more challenging. This year has begun with oil prices firming, housing costs increasing, more people working and having money to purchase goods, and a driven administration to lay out the playing field with incentives such as lower taxes and regulations.

What could drive inflation up ahead of its time?

Fiscal Snapshot

Bank of Canada Rate

	BoC Rate	Bank Prime Lending
January 2017	0.75	2.70
One month ago	0.75	2.70
One year ago	0.75	2.70

Government of Canada Benchmark Bond Yields

	5-Year	10-Year	Long
January 2017	1.11	1.75	2.41
One month ago	1.11	1.72	2.31
One year ago	0.67	1.22	2.03

Indicative Commercial Mortgage Spreads* Over Government of Canada Bond Yields

Conventional	5-Year	10-Year
January 2017	1.70 - 2.10	1.85 - 2.35
One year ago	1.75 - 2.00	1.85 - 2.25

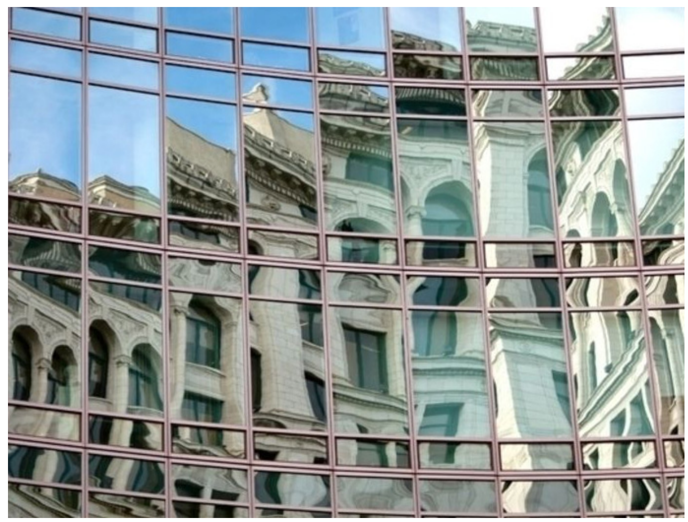
Insured	5-Year	10-Year
January 2017	0.90 – 1.10	1.00 – 1.10
One year ago	0.90 - 1.25	0.95 - 1.25

*Spreads are indicative of high quality real estate in major Canadian markets.

Highlighted Transaction

Asset Type	Multi Family Residential
Location	Major Canadian city
Facility Details	A CMHC insured first mortgage in the amount of $11,410,000 for a 7 year term, 25 year amortization funded at a very competitive rate of interest.

Intelligent Debt Financing Solutions



The Avison Young National Debt Capital Markets dedicated team is focused on providing innovative North American-wide debt and equity solutions to accomplish goals. We originate debt and equity for all types of real estate and all types of clients. Debt origination includes fixed and floating rate structures, permanent and construction financing, structured finance, bridge and mezzanine debt and insured agency financing - CMHC and Fannie Mae / Freddie Mac.

Our years of combined debt/equity capital markets experience has created meaningful relationships that we can put to work for you.

Please contact our National Debt Capital Markets team for more details related to debt financings or real estate transactions.

Norm Arychuk, Broker*
416.673.4006
norman.arychuk@avisonyoung.com

*Licence #: M09002260
Brokerage Licence #10637

Michael Ho, Mortgage Agent**
416.673.4012
michael.ho@avisonyoung.com

**Licence: # M15000834
Brokerage Licence #10637

Avison Young is the world's fastest-growing commercial real estate services firm. Headquartered in Toronto, Canada, Avison Young is a collaborative, global firm owned and operated by its principals. Founded in 1978, the company comprises over 2,200 real estate professionals in 77 offices providing value-added, client-centric investment sales, leasing, advisory, management, financing and debt placement services to owners and occupiers of all property types.

NORTH AMERICAN CAPITAL MARKETS OFFICES

Calgary | Edmonton | Mississauga | Montreal | Toronto | Vancouver | Boston | New York | Washington DC | Chicago | Raleigh-Durham | Nashville | Atlanta | South Florida | Houston | Phoenix | San Francisco | Los Angeles | Orange County | Mexico City

EUROPEAN CAPITAL MARKETS OFFICES

Coventry | London | Hamburg | Frankfurt | Munich | Dusseldorf

AVISON YOUNG

Intelligent Real Estate Solutions

avisonyoung.com

Avison Young Commercial Real Estate (Ontario) Inc., Brokerage
18 York Street, Suite 400
Mailbox # 4
Toronto, Ontario, Canada M5J 2T8
416.955.0000

CANADA'S BEST MANAGED COMPANIES