Top 10 Real INSIGHTS

2019 Saskatchewan Real Estate Forum

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ISSUE 24

TOP 10 | REAL INSIGHTS

2019 Saskatchewan Real Estate Forum

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1. MAJOR AMOUNTS OF NEW CAPITAL INVESTMENT FLOWING INTO THE PROVINCE

Line 3 and BRT infrastructure projects will generate jobs and help to fuel the provincial economy.

Saskatchewan has experienced a remarkable growth in investment in the past decade. Since 2007, Saskatchewan has reached an estimated $135.5 B in new investment. While the decline in oil and other commodity prices in the past few years has had some impact on investment, there is still a considerable amount of activity ongoing.

Work on Enbridge's Line 3 Replacement is well underway. In Saskatchewan, the company estimates the pipeline will create about 9,175 direct, indirect and induced jobs, and generate $1.0654 B in GDP and $183.9 M in taxes.

The $5.3 B Canadian portion of the Line 3 Replacement Program involves the replacement of approximately 1,070 kilometres of Line 3 pipeline between Hardisty, Alberta and Gretna, Manitoba, with new pipeline. About 40% of the new pipe was installed in 2017. Construction on the remainder of the pipeline started last fall.

The 2017 Fraser Institute Annual Survey of Mining Companies ranked Saskatchewan the 2nd most attractive jurisdiction in the world for mining investment. In 2016, the Fraser Institute ranked Saskatchewan first in Canada and fourth in the world for oil and gas investment.

Approval of $120 M for a bus rapid-transit system that will cross Saskatoon is anticipated to attract mixed-use Transit Oriented Development – mixed-use 'transit villages' along the new corridors. Construction of the system could begin in 2019 and be completed within three years.

Three lines are proposed for the Bus Rapid Transit (BRT) system. The City of Saskatoon says that the new system would improve travel speed, reliability, capacity, and customer experience and says it is central to a future transit plan for the city.

In Saskatoon, the North Commuter Parkway was one of the largest infrastructure projects in the province's history with a total budget of $211.4 M. The bridge, which opened officially in October 2018, spans the South Saskatchewan river at the northern edge of the city connecting residential developments in the northeast to the city's industrial areas in the east and south. The bridge is anticipated to be a key driver of economic growth for the region and traffic volumes are set to hit upwards of 20,000 cars per day in coming years.

Saskatchewan is the 2nd most attractive jurisdiction in the world for mining investment.

In last April's provincial budget, $2.7 B was allocated to infrastructure spending. Saskatchewan's Crown corporations will invest more than $1.5 B into infrastructure in 2018-19 while executive government ministries and agencies have more than $1.2 B in capital investments outlined in the Saskatchewan Builds Capital Plan, a key component of this year's budget.

The plan features nearly $691 M of investment in transportation infrastructure, including $330 M to continue construction of the Regina Bypass.

2. THE PROVINCE'S DIVERSE ECONOMY HEDGES AGAINST OIL SLOW-DOWN

Saskatchewan is the world's largest potash producer, a top supplier of uranium, and the largest exporter of lentils, dried peas, oats and canola.

The province's flourishing manufacturing and technology sectors are built on a strong resource base. Saskatchewan boasts some of the world's top dry-land agricultural equipment manufacturers and world-leading biotechnology and carbon capture and storage technology. This diversity has been instrumental in Saskatchewan's success in recent years.

Saskatchewan has experienced steady GDP growth over the past decade. The province posted a GDP of $60.6 B in 2017.

Saskatchewan's trade sector will get a boost from increased global demand for key commodities, such as potash, oil and agricultural products. This will help lift the province's economic growth to 2.2% this year, according to The Conference Board of Canada's Provincial Outlook: Winter 2019.

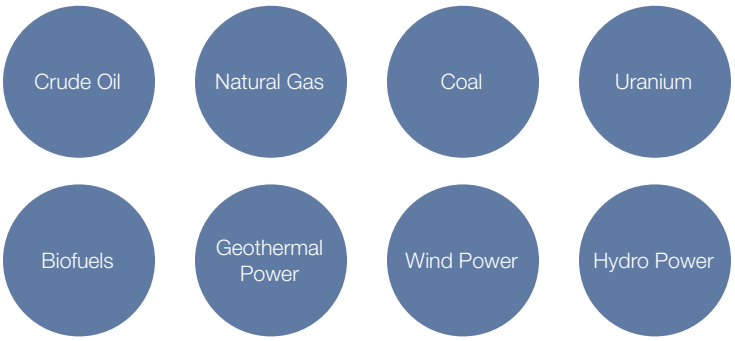
In December, manufacturing sales were up 11.5% year-to-date, driven by increased woods, metals, and food sales. Potash production was up 5.3% through August, and the global outlook for the sector is improving, with supply tightening and demand increasing. Prospects for the crop sector in 2018 have improved, with total wheat production now set to expand relative to 2017, according to TD.

Saskatchewan is Canada's most important grain-producing region, supplying more than one-third of the world's exports of durum wheat.

The pulse crop sector has grown into a billion-dollar export industry that employs more than 1,000 people.

Saskatchewan's $4.3 B food processing industry includes more than 300 processors and employs over 5,000 people. The province has plans to increase value-added agriculture expansion to $6 B by 2020.

Saskatchewan produces over one third of Canada's primary energy, and is one of the few places in the world that produces all of these types of energy:



In 2017, the combined estimated value of oil and gas production was over $9.2 B. In 2017, the province produced 177.2 M barrels of oil.

Saskatchewan is the world's leading supplier of uranium – 90% is exported, with the remaining 10% fueling nuclear reactors in Canada. The province's uranium is responsible for 6% of the electricity generated in the United States.

3.INCREASED DEMAND FOR QUALITY OFFICE SPACE

Vacancy rates are coming down in Saskatchewan's two biggest cities and more tenants are looking for quality space. But new construction of AAA space in Saskatoon may change the situation in that market.

Demand for Class A office space characterizes the markets of Regina and Saskatoon.

REGINA

Brokers, appraisers and property managers believe tenant demand is going to increase for all office asset types except Class C over the next 12 months.

"We're seeing a shift in general attitude," said Craig Hennigar, Vancouver-based director of market intelligence at Colliers International. "The general view is things are on the upswing and there will be a pick-up in rents and tenant demand in the next year," he said.

Limited new construction in 2018 has kept the vacancy rates for competitive and non-competitive office space at 8% throughout the later part of the year, with inventory of 7.1 M sq. ft. as of November 2018, Avison Young reports.

A combination of additional inventory hitting the market over the last couple of years at the same time the provincial government, the biggest employer in the provincial capital, was scaling back was the biggest factor in the vacancy rate heading upwards.

Demand for non-CBC office space remains healthy and the vacancy for Class A downtown office space is forecasted to dip under 4% by the end of 2019, according to Avison Young.

SASKATOON

In the third quarter of 2018, downtown office vacancy rate decreased to 16.8%, resulting in positive absorption of nearly 25,000 sq. ft., reported ICR Commercial Real Estate. During the same time period, vacancy in the suburban market rose to 18.8% with a negative absorption of more than 80,000 sq. ft.

"A flight to quality space will likely continue as existing office users look to migrate to higher-quality space," the report said.

Blair Sinclair, EVP of investments and development at Triovest says that the vacancy rate for Class A office space is just 6%. "That equates to 60,000 square feet and none of it is contiguous," he said.

"We saw that the City of Saskatoon was in desperate need of AAA-class office space," Sinclair said. "There is none of that in the city. The last new building built was in 2010 and we built that one too. We knew that if we built, there would be a flight to quality and our logic and our strategy has paid off immensely."

Triovest has two office buildings currently under construction at River Landing. The East Tower is a 13 storey, 185,000 sq. ft. building with a fitness centre, conference space and retail component. The building is 60% leased and is slated for completion in Fall 2019.

The second building is the Nutrien Tower. At 18 storeys it will be the tallest building in Saskatoon once it is completed in late 2021 or early 2022. Nutrien's president and CEO Chuck Magro said that approximately 400 company employees will occupy the top eight floors of the building.

The two new towers at River Landing will be the first Class A buildings to be delivered since the 1980s.

Meanwhile the River Quarry on 4th is being redeveloped and is targeting a LEED Gold certification. The office building offers floorplates up to 18,461 sq. ft. A fourth storey will be added which will result in 64,020 of contiguous square footage. The former headquarters for Saskatoon Police Service sold for $10.7 M to Duchuck Holdings Ltd. at the end of 2016.

4.INDUSTRIAL SECTOR SEES HEALTHY GROWTH

Trade optimism and growth in manufacturing muffles vacancy and spurs new development.

Total Saskatchewan exports to the United States in 2017 were $29 B. The U.S. remains Saskatchewan's No. 1 market, by far, with just over half of its 2017 exports being shipped south.

The announcement of USMCA has resulted in an increase in activity and a more positive outlook across all sectors, ICR Commercial Real Estate reports.

SASKATOON

The Saskatoon industrial landscape continued to improve in 2018 following several years of excess supply and high vacancy rates triggered by the wave of construction which ended in 2013, CBRE reports.

In the city's industrial market, rental activity is picking up after landlords acknowledged that current conditions demand lower net effective rental rates to attract and hold onto tenants according to PWC Emerging Trends 2019.

Vacancy rate at 7.7% going into 2019

Saskatoon has an industrial inventory of 18.7 M sq. ft. New construction remains slow. Investors have been reluctant to risk adding to the current oversupply of space. An increase in purpose-built construction by owner occupants this Spring is forecasted by ICR.

North of the city, Bold Growth Inc., is building a $12 M, 56,018 sq. ft. cultivating and processing facility on a 62 acre site. The Saskatoon company aims to become a grower and wholesaler of recreational and medicinal marijuana.

2018 saw the leasing of the remaining industrial space from the previous development cycle. Going into 2019, the city's vacancy rate sits at a 7.7% with rents at $9.25 psf. Overall, fundamentals in the industrial sector look strong and there remains significant runway for further growth, CBRE says.

The Marquis Industrial area reported a vacancy of 6% with asking average net rental rate of $11.86 psf. The lowest vacancy can be found in Sutherland, which is 0.6% with an asking net rental rate of $8.50 psf. The highest is in the CN area at 13.2% with an asking rate of only $7.85 psf net, ICR reports.

REGINA

The city's industrial market continued to gather momentum throughout the final quarter of the year with year-over-year vacancy decreasing to 4.4%, and year-over-year absorption at 18,377 sq. ft. With available space at a competitive balance, average asking rates have remained stable. Rates are expected to stay stable while the market continues in a competitive state. Average asking rates are $11.10 psf, ICR reports.

Year-over-year vacancy decreasing to 4.4%

"We didn't overbuild in the busy times, so there's still a happy medium between too much product and not enough," Glen Hill, Regina-based SVP at Colliers International said.

Brightenview Development International has built the 80,000 sq. ft. Global Trade Exhibition Centre and is expecting its first tenants this Spring.

Dream HL Commercial finished construction on the Phase I of Harbour Landing Commercial campus in south Regina. The campus is a service-oriented "industrial prestige" development.

The former Sears warehouse is being redeveloped by Hungerford Properties. Now known as Titan Business Park, the building was refurbished into a 176,000 sq. ft. warehouse facility with 26' ceilings. There was 89,750 sq. ft. of warehouse space available for lease at the time of writing.

Last year, OneLeaf Cannabis Corporation, a company based in Saskatchewan, started construction on a multi-million-dollar, 44,000 sq. ft. production plant in the Sherwood Industrial Park.

In Regina, net asking rates on new space is averaging $13 psf while existing space ranges between $9 to $10 psf, Avison Young reports. Avison expects lease rates to rise slightly in 2019.

5. DEBT MARKETS REMAIN BUOYANT

Alternative lenders are playing a growing role in Canada's real estate markets.

Alternative lenders are playing a growing role in Canada's real estate market as the industry searches for new sources of financing, risk-averse banks become pickier, and investors look for yield.

In 2019, the greatest growth in originations is expected from alternative lenders such as mortgage REITs and debt funds (49% anticipate growth greater than 5%) according to the commercial real estate finance outlook survey.

A recent study conducted by Altus Group found that more than 82% of the 400 development executives surveyed are using at least one alternative lending vehicle to fill their capital stack. These debt funds have created competition for traditional banks. Debt funds are not subject to the same strict restrictions as banks — making them more appealing to borrowers in need of quick and more creative financing options.

"… (T)he debt portion of the capital stack is actually very attractive for several reasons — one, returns are still good at this point, and two, it actually provides a little more protection [and] a little lower risk, because they are lower on the capital stack," Altus Group Senior Executive Vice President of Advisory Rick Kalvoda said. "Any drop in [property] value first comes away from the equity, then goes down to mezzanine financing, bridge loans, then goes down to senior loans — which is where a lot of these debt funds operate in the lending space."

The results of REALPAC's Q4 2018 Canadian Real Estate Sentiment Survey states that overall debt capital remains available and lenders continue to be competitive. Less established groups without a track record may experience increased difficulty in acquiring credit. One person who was surveyed stated:

"No problem with debt for established companies with relationships with the major banks and insurance companies. For others, [lenders] may decide to cut back for the newer entries into the market and less established ones, as it is the established players that really will continue to get what they need because of the relationship side of the business as opposed to just standing on the economics of the deal."

62% of those who were surveyed believe that the availability of debt capital will remain the same at the end of 2019 as it was at the end of 2018.

6. MULTI-RES SECTOR SHOWING SIGNS OF LIFE - GETS A BOOST FROM NEW MORTGAGE RULES

Vacant units are slowly being absorbed and rents are holding steady.

Provincial employment growth continues to be sluggish, following two years of recession. However, employment opportunities are expected to increase over the next two years with steady economic growth, CMHC reports.

It goes on to state that "as Saskatchewan's economy generates more employment opportunities, net interprovincial migration is expected to improve. International migration will continue to support new household formation and population growth".

"Rental demand in the Saskatoon CMA is expected to strengthen throughout the forecast period, supported by continued employment and population growth. As a result, the purpose-built apartment vacancy rate will trend lower in 2018 and through 2020 but remain elevated by historical standards."

The average vacancy rate for the City of Saskatoon in 2018 was 7.7% and is forecasted to drop to 7.0% in 2019. The average rent for a two-bedroom unit was $1,085 and will increase only slightly over the next couple of years.

A building blitz of new rental properties has added nearly 1,500 new units in the past eight years, with another 172 rental apartments completed in 2018.

In Regina, the significant increase in rental supply over the past few years will limit the decline in the apartment vacancy rate through 2020. The average two-bedroom rent is forecast to increase modestly over the next two years. An elevated apartment vacancy rate will mitigate the degree to which property managers and landlords are able to increase rental rates in 2019 and 2020.

The average vacancy rate for the City of Regina in 2018 was 6.6% and is forecasted to drop to 6.0% in 2019. The average rent for a two-bedroom unit was $1,116 and is not expected to change significantly in 2019.

In December, Boardwalk sold two of its Regina portfolios: the Kenley Apartments for $15.9 M - the 140-unit portfolio was comprised of eight buildings, ranging from 8 units to 32 units; and the 641-unit Boardwalk Estates portfolio for $71.7 M.

Sam Kolias, Chairman and Chief Executive Officer of Boardwalk REIT, restated his firm's long-term strategic goal to have a portfolio about 50% in Alberta and Saskatchewan and 50% in other high growth and under-supplied markets.

* Vacancy and Rental Rate date from CMHC Housing Market Outlook - Fall 2018

7. LOW VACANCY CHARACTERIZES THE RETAIL SECTOR

Despite a lack of growth in retail spending in 2018, vacancy is low, and rents remain fairly stable.

The province's labour market has remained subdued this year. A lack of new hiring has weighed on retail spending this year (+0.7% YTD), TD reported in its December 2018 Provincial Economic Forecast.

In Regina, consumer spending remained stable in 2018 which supported its retail market. Vacancy rose slightly to 3% in Q3 2018 and rental rates have remained stable ranging from $20 to $35 psf for existing neighbourhood and regional centres and $32 to $42 psf for new space, reports Avison Young.

Currently the Aurora retail centre is under construction. Costco has already opened with Landmark Cinemas to open soon.

Phase I of the Acre 21 development was complete at the end of 2018 with 11 new retail business. The complex has secured, Metro Liquor Store, Shoppers Drug Mart, Dairy Queen, McDonald's, Boston Pizza, Popeye's Chicken and a Domino's Pizza with a Save On Foods as anchor. Phase II is set to begin construction this Spring.

Strong population growth in Saskatoon is providing fuel to the city's retail sector.

According to a new report from Saskatchewan Edge, 8th Street in Saskatoon continues to be one of the busiest retail corridors in town with a vacancy rate at 3.6%. There is less than 37,000 sq. ft. of vacancy on the city's "golden mile" and rates are staying steady about $29.89 psf.

Vacancy in the central business district is 4.3% and rates are $23.69 psf.

The tightest market mid-way through 2018 was Broadway, where vacancy was just 1.1% and asking rates averaged $22 psf.

At the end of 2018, Mountain Equipment Co-op announced plans to open its first Saskatchewan location at Midtown Mall in Saskatoon. MEC will take over the food court space and the new food court will be moved to the second floor and take over space that was vacated by Sears in the Fall of 2017. The new 20,000 sq. ft. store is expected to open in May 2020.

H&M opened a two-level, 25,000 sq. ft. store in Regina at the Cornwall Centre as part of its continued expansion in Canada. However, Aldo, Roots and Gap have recently vacated the mall which is still dealing with 120,000 sq.ft. vacated by Sears.

Firm Capital Property Trust recently bought a 50% interest in a portfolio of seven retail properties in five provinces from Crombie REIT for $41.6 M. Among the properties acquired are:

- 13th Avenue Regina Safeway: 2915 13th Avenue, Regina, 40,717 sq. ft.
- University Park shopping centre: 2231 East Quance Street, Regina, 37,219 sq. ft., anchored by Sobeys

Both KingSett Capital (Cornwall Centre, Regina and Midtown Plaza, Saskatoon) and Morguard (Centre Mall, Saskatoon) are investing in expansions and upgrades to their market leading retail properties.

8. HOUSING SET TO REBOUND IN 2019

CMHC expects improved job growth and higher interprovincial migration numbers will propel housing prices by 10% this year.

Saskatchewan's housing market has been in a bit of a slowdown for the last few years. The general trend in housing prices for both Saskatoon and Regina has been downward, according to a report from the Canadian Real Estate Association.

SASKATOON

Saskatoon's market for new homes remains slightly oversupplied, leaving builders still cautious in 2018 after significant declines in starts in 2015 and 2016. The amount of construction will likely decrease again this year, but a rebound is in the cards for 2019, according to the Conference Board of Canada.

Saskatoon housing prices were down in the last quarter of 2018, according to the Royal LePage House Price Survey.

Matt Miller, a broker/owner with Royal LePage in Saskatoon, said a big factor in the slowdown was the falling price of oil. The housing market is tied to provincial and local economies, he said.

Miller said Saskatchewan doesn't really have a boom and bust market, which he said is a good thing. He noted that despite the slowdown, Saskatoon is still growing.

In the Re/Max 2019 Housing Market Outlook, it is reported that the average residential sale price decreased by approximately 4% to $333,187. The 2018 average sale price for condos was $245,564. The condo market is expected to stay strong with single millennials and students driving the demand for this product type.

REGINA

Regina's last quarter saw housing prices stay about the same, according to Royal LePage data.

Rob Reynar, with the Association of Regina Realtors, said the rules are forcing some people to leave the market altogether.

"These mortgage stress test rules have really weakened demand, not just locally, but right across the country in many markets that did not need weakened demand," he said.

Overall, the average sale price decreased by 6.5% in 2018 to $309,600. The average price for a condo was $250,000 and is forecasted to remain the same through 2019. Single millennials, young couples and downsizers are fueling demand for this housing type - Re/Max 2019 Housing Market Outlook.

At the end of 2018, 3,032 sales were recorded in Regina, a decrease of 7% from 3,270 in 2017 and the lowest since 2005 when 2,840 sales were recorded. Sales in January were up slightly by 1.2% year over year, reported the Association of Regina REALTORS® Inc.

Saskatchewan's housing sector has been sluggish for two years, with 2018 starts projected to be fewer than 1,500 units, down from 1,923 in 2017. CMHC expects better job growth, and higher in-migration could push starts as high as 1,775 units in 2019. Provincial housing sales are also forecasted to increase modestly, and average home prices could rise 10% to around $319,000.

Strong population growth in Saskatoon is providing fuel to the city's retail sector.

9. SIGNIFICANT DEVELOPMENT ACTIVITY TAKING PLACE IN SASKATCHEWAN

From River Landing in Saskatoon to Coopertown in Regina, major developers have faith in Saskatchewan's economy.

Dream Development is Saskatchewan's largest residential land developer. In the last three years, they have developed 3,700 lots and 70 acres for multifamily and commercial projects.

One of their current developments, Brighton, contains 235,000 sq. ft. of retail space and 100,000 sq. ft. of office space. At the time of writing, Wilson's Lifestyle Centre and Landmark Cinema were already open for business. Save-On-Foods will open in Summer 2019. Motion Fitness and The Keg have been confirmed for the site. Dream owns 50% of this Saskatoon development.

Last summer, Regina City Council approved the concept plan for the first neighbourhood area in Coopertown, which will allow Dream to begin development of an 1,100-acre parcel of land in 2019.

Over the next 20-plus years, Coopertown is expected to accommodate a population of approximately 36,000 people, with over 650,000 sq. ft. of commercial space, including a main street urban centre with retail and civic uses. It is slated to be the largest Master Planned community in the City of Regina.

In Saskatoon, Arbutus Properties' Meadows Market officially opened in November. The 162,000 sq. ft. retail development contains Marshalls, Dollar Tree, PetSmart, Visions, Scotiabank, Co-op Liquor and Tim Hortons. The project is anchored by Costco, which opened in Fall 2016.

Artubus is also looking to buy and redevelop the city yards in Saskatoon. The city yards comprise about 32 acres of land north of downtown in the Central Industrial area. Originally a report from city hall administration suggested complete development of the property could take 25 to 30 years. A report on a more expedient way of moving forward with redeveloping the yards is expected early this year.

The River Landing development by Greystone, Triovest and a local developer is a mixed-use urban project situated on the edge of downtown Saskatoon. The three-phase, $300 M, mixed-use complex includes a hotel, condominiums and two office buildings including the Nutrien Tower. Construction is nearing completion on the 20-storey condominium tower and 155-room Alt Hotel, which are slated to open in 2019. Construction of a 13-storey office tower, complete with a four-level parkade began last summer. The two office towers included in the project total approximately 450,000 sq. ft. of Class A space. Both towers have already achieved pre-leasing of over 60%, including lease transactions by tenants such as TD, Ernst & Young and Nutrien.

The City is considering a replacement for the SaskTel Centre. The 30-year facility has two major tenants - Western Hockey League's Saskatoon Blades and the National Lacrosse League's Saskatoon Rush - but has not been updated sufficiently to handle major concerts and is inconveniently located. Bruce Urban, owner of the Rush, said in March that he would contribute 10%, or about $20 M, towards the cost of a new arena downtown.

Saskatoon's City council commissioned a report to investigate the feasibility of building a new arena downtown. The study was done by the same group that recently helped Edmonton develop its Ice District sports and entertainment zone. The report identified $101 M in cost upgrades that would have to go into SaskTel Centre today to bring it up to current standards.

Public consultation will be starting on the development of approximately 900 acres of land belonging to the University of Saskatchewan. The land, which is being transitioned from agricultural research could see 40,000 to 60,000 new homes built on it and represents a major urban development opportunity for the city of Saskatoon.

10. Are Public Policies Helping to Attract New Development?

While low commercial tax rates keep Regina & Saskatoon competitive, restrictive development policies may not.

Saskatoon and Regina have the lowest commercial-to-residential tax ratios of all major Canadian cities, according to a new Altus Group study. The Canadian Property Tax Rate Benchmark report found Saskatchewan's two biggest cities topped the list with ratios of 1.72 and 1.74, respectively. The average ratio of the 11 cities measured was 2.9.

"Lower commercial property taxes help make cities more competitive, promote job growth and investment and subsequently generate more stable and sustainable revenue," the report said.

Regina's city council voted down a proposal for a city land development strategy. Ward 3 Councillor Andrew Stevens said he was hoping to one day see land development "as a core business of the City of Regina."

The City of Saskatoon reported $40.7 M in land sales for 2017, however city official said that the City of Regina owns far less land than Saskatoon. It could take decades to acquire enough additional land to make further land development a viable strategy.

The City of Regina Official Community Plan directs at least 30% of population growth for the next 25 years to existing neighbourhood through intensification. It states that encouraging redevelopment of the city's underutilized lands is critical to achieving this growth.

In 2017, only 5% of growth went to already established neighbourhoods. This rate was the lowest in four consecutive years. In 2014, the city fell just short at 26%. A year later, the figure was 12%, then 11% in 2016.

The Underutilized Land Study that was conducted looks at potential regulatory, environmental, social and economic barriers to private sector redevelopment of various types of underutilized sites throughout the city

In this study, 788 Vacant Sites have been identified in the Intensification Area, 43 Vacant Buildings have been identified in downtown.

Regina's policy, implemented in July 2012, does not permit major office developments of more than 43,000 sq. ft. of floor space outside of the core area except in limited and specific contexts: for instance, an accessory to an institution.

Saskatoon and Regina have the lowest commercial-to-residential tax ratios of all major Canadian cities, according to a new Altus Group study. The Canadian Property Tax Rate Benchmark report found Saskatchewan's two biggest cities topped the list with ratios of 1.72 and 1.74, respectively. The average ratio of the 11 cities measured was 2.9.