Midtown Manhattan Office, Q2 2020

Leasing flounders, but rents remain steady quarter-over-quarter

Leasing Activity	Net Absorption	Availability Rate	Vacancy Rate	Average Asking Rent
1.29 MSF	(1.10) MSF	12.2%	8.6%	$87.04 PSF

*Arrows indicate change from previous quarter.

- Midtown finished Q2 2020 with 1.29 million sq. ft. of leasing activity, 69% below its five-year quarterly average, and down 68% year-over-year.
- Diminished leasing activity combined with several 50,000+ sq. ft. space additions drove quarterly net absorption to negative 1.10 million sq. ft.
- The availability rate increased 40 basis points (bps) quarter-over-quarter to 12.2%.
- At $87.04 per sq. ft., the Midtown average asking rent remained essentially flat quarter-over-quarter.
- The average tenant improvement (TI) allowance for new leases reached nearly $107 per sq. ft. and 14 month of free rent.
- The taking rent index notched a drop of 90 bps quarter-over-quarter to 92.3% - its lowest point since Q3 2018.
- CBRE Econometrics Advisors' rent forecast for Midtown anticipates average asking rent to decline between 10 and 16% by Q1 2021 before beginning to recover.

MARKET OVERVIEW

Virology, not the business cycle, has dictated the course of the world's economy this year. COVID-19 forced a nationwide shutdown of most economic activity in March, with the largest economic centers, especially the Northeast and Pacific coast, facing the strictest lockdowns. The economic fallout proved severe, pushing unemployment to over 14% and likely causing the economy to contract by more than 30% per annum in the second quarter.

The impact of COVID-19 on the Midtown market was plainly felt in Q2 2020. Leasing activity fell to its lowest quarterly total on record, at 1.29 million sq. ft. – 69% below the five-year quarterly average, and 30% below the second lowest quarter ever, Q1 2009. Despite the precipitous drop in leasing activity, renewal activity remained on pace, with 1.22 million sq. ft. of renewals, only 2% off the five-year quarterly average. The uncertainty that accompanied the onset of the pandemic has led many occupiers to complete renewal transactions in order to push longer-term commitments and relocation decisions down the line.

Figure 1: Top Lease Transactions | Q2 2020

Size (Sq. Ft.)	Tenant	Address
232,138	TikTok	151 West 42nd Street
143,331 (R)	Allen & Overy	1221 Avenue of the Americas
120,075 (R)	Mitsubishi International Corporation	655 Third Avenue
59,052	Colliers International	1114 Avenue of the Americas
55,877 (R)	Bank of America Corporation	1540 Broadway

Renewal (R), Expansion (E), Renewal and Expansion (RE).

Source: CBRE Research, Q2 2020.

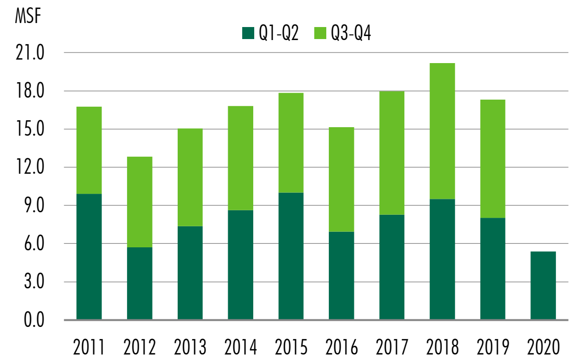
Space additions were minimal through the first months of the quarter, though in June blocks over 50,000 sq. ft. accounted for more than 1 million sq. ft. of added space, raising Midtown's availability rate by 40 basis points (bps) to 12.2%. Midtown's average asking rent remained essentially flat quarter-over-quarter, down 1% year-over-year, and remained within 3% of its all-time high. CBRE Econometric Advisors' rent forecast for Midtown anticipates average asking rent to decline between 10 and 16% by Q1 2021 before beginning to recover.

LEASING ACTIVITY

Midtown finished Q2 2020 with 1.29 million sq. ft. of leasing activity, 69% behind the five-year quarterly average, and down 68% from the previous quarter. Considerable uncertainty, about both the local Manhattan real estate market and the national economy, has led many tenants and landlords to adopt a wait-and-see approach. Tenants are, in general, favoring short term leases and extensions-in-place in lieu of committing to major relocations or long-term solutions, a trend played out in Midtown's top quarterly transactions, where three of the top five transactions were renewals. The two largest were Allen & Overy's 143,000 sq. ft. extension at 1221 Avenue of the Americas and Mitsubishi International Corporation's 120,000 sq. ft. renewal at 655 Third Avenue. Despite the notable shift to renewals, the largest Midtown transaction of the quarter was TikTok's new, long-term lease of 232,000 sq. ft. at 151 West 42nd Street – a welcome vote of confidence in Midtown during an otherwise skittish quarter.

All submarkets recorded leasing activity below their five-year averages. Times Square/West Side and Grand Central showed the strongest performances, collectively accounting for 58% of all of Midtown's leasing activity. Led by the TikTok deal, Times Square/West side saw 391,000 sq. ft. of activity, only 15% below the five-year quarterly average. Grand Central reached 361,000 sq. ft. of leasing, 54% below its five-year quarterly average.

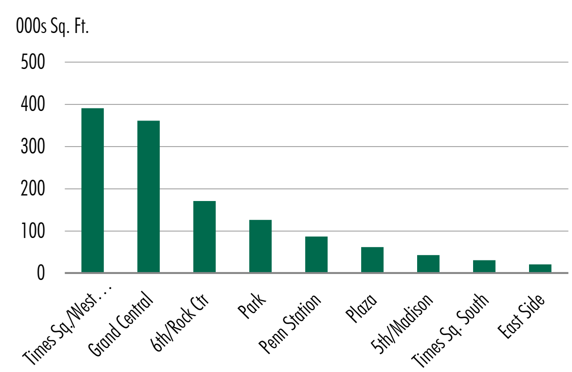
Figure 2: Leasing Activity | Historical



Source: CBRE Research, Q2 2020.

The remaining submarkets struggled, with leasing activity totals severely below historic norms. Park Avenue, Fifth/Madison and Penn Station all experienced their worst quarters since the peak of the Financial Crisis. Park Avenue notched 126,000 sq. ft. of leasing, 73% below the five-year quarterly average, but enough to manage a first half 3% better than in 2019. Fifth/Madison faired even more poorly, with 43,000 sq. ft. of activity, coming in 80% below the five-year average and closing the first half of 2020 69% behind last year's leasing numbers. Penn Station, with no leasing activity in its marquee new construction buildings, reached 87,000 sq. ft. of activity – a staggering 89% below the five-year quarterly average. However, strong Q1 figures led Penn Station to close the first half with 25% greater leasing activity than the same time last year.

Figure 3: Quarterly Leasing Activity | By Submarket



Source: CBRE Research, Q2 2020.

The East Side and Times Square South, at 21,000 sq. ft. and 31,000 sq. ft., posted their poorest quarters of leasing ever recorded. The East Side managed 194,000 sq. ft. of activity for the first half of the year, down 56% from last year, and the worst first half historically. Similarly, Times Square South posted 416,000 sq. ft. of activity in the first half, down 45% from H1 2019, and the slowest first half of a year since H1 2009.

In terms of industries, financial services - Midtown's perennial stalwart - accounted for 37% of total leasing activity. A host of smaller deals ranging in size from 10,000 to 25,000 sq. ft. helped to drive financial services leasing. In contrast, the technology sector provided 28% of Midtown's leasing for the quarter, largely due to TikTok's 232,000 sq. ft. lease at 151 West 42nd Street. In the first half of 2020, technology occupiers have accounted for 18% of leasing activity – second only to financial services – continuing the trend of tech's Midtown ascendancy.

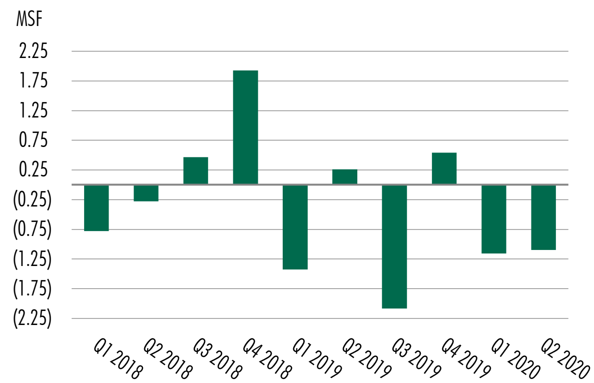
Leasing velocity paints a slightly rosier picture of activity in Midtown during the second quarter at only 54% below the five-year norm as renewals buoyed the total. Despite the abrupt drop off in new leasing, renewal figures remained on pace, less than 2% below the five-year quarterly renewal average. As occupiers push off relocation decisions, renewals, particularly short-term, have become increasingly popular. Renewals' share of total leasing velocity—typically 24%— skyrocketed in Q2 2020 to 48%. It is possible that pent-up demand will manifest itself in a resurgence of new activity figures in the next four quarters.

NET ABSORPTION AND AVAILABILITY

Quarterly net absorption reached negative 1.10 million sq. ft., raising Midtown's availability rate 40 bps to 12.2%. While historically slow leasing clearly had an effect, the first two months of the quarter saw few space additions, either direct or sublet, as landlords watched to see how the pandemic and accompanying economic uncertainty played out.

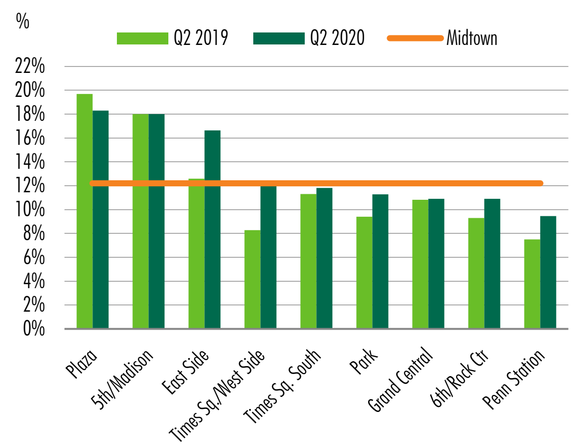
By June, space additions were picking up to a more normal pace, with one million sq. ft. of blocks over 50,000 sq. ft. coming online.

Figure 4: Net Absorption | Quarterly



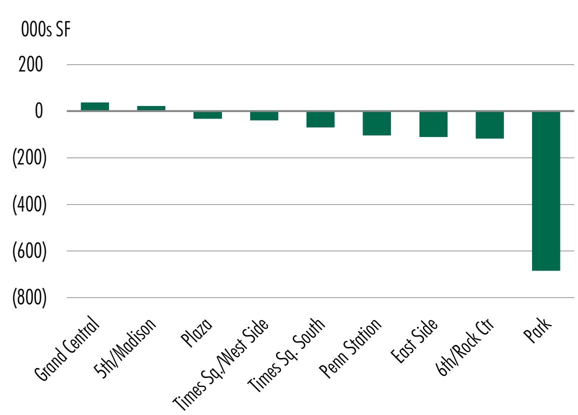
Source: CBRE Research, Q2 2020.

Figure 5: Availability Rate | By Submarket



Source: CBRE Research, Q2 2020.

Figure 6: Quarterly Net Absorption | By Submarket



Source: CBRE Research, Q2 2020.

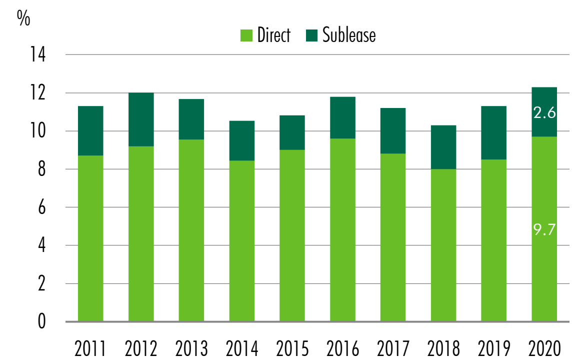
Seven of Midtown's nine submarkets experienced negative net absorption in the second quarter. Park Avenue fared the worst, posting negative absorption of 684,000 sq. ft., in part due to blocks at 390, 200, and 237 Park Avenue being made available. The additions contributed to a 240-bps jump in the availability rate to 11.3%, the highest rate since January 2018. While six other submarkets saw negative absorption in Q2, the figures were relatively mild in comparison. Sixth/Rockefeller posted negative 118,000 sq. ft with a quarter-over-quarter availability increase of 30 bps to 10.9%. The East Side experienced negative 110,000 sq. ft. of absorption, translating to a 50-bps increase in the availability rate, reaching 16.6%, the highest level since Q4 2009. Penn Station saw a similar trend – negative absorption of 103,000 sq. ft. and an accompanying increase of 40 bps in the availability rate to 9.5%.

Times Square South notched negative 70,000 sq. ft. of net absorption, resulting in availability rising 40 bps quarter-over-quarter to 11.8%. While two other submarkets saw negative absorption, the figures were largely muted. Times Square/West Side posted negative 39,000 sq. ft., yielding an availability rate increase of 10 bps to 12.3%, the highest rate since May 2015. Plaza saw 33,000 sq. ft. of negative absorption and a 30-bps increase to 18.3%.

Fifth/Madison and Grand Central both managed positive net absorption in the second quarter, though it was a result of so little space being made available rather than strong leasing. Fifth/Madison reached positive 23,000 sq. ft. of absorption, leading availability down slightly to 18.0%, while Grand Central experienced 37,000 sq. ft. of positive absorption, though availability remained flat quarter-over-quarter.

Despite concerns about the broader economic situation translating to a sudden glut in sublease space, there has been no meaningful change – yet. Quarter-over-quarter sublease availability remained flat at 2.6% and is down 20 bps from year-end 2019. Sublease space totaled 6.34 million sq. ft. and represented 21% of all available space, in line with the five-year average of 20% and well below the ratio reached during past recessions.

Figure 7: Sublease and Direct Availability Rate | Historical

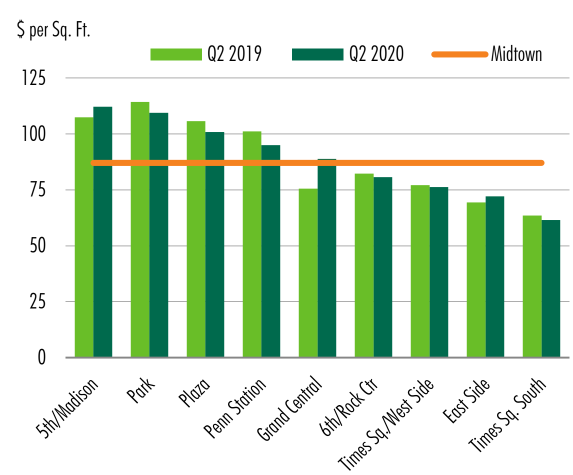


Source: CBRE Research, Q2 2020.

AVERAGE ASKING RENT

Midtown's Q2 2020 average asking rent was $87.04 per sq. ft., flat quarter-over-quarter but down a little more than 1% year-over-year. Quarter-over-quarter, only Penn Station and Times Square/West Side saw changes of more than 2%, with Penn Station rising 3% to $94.94 per sq. ft., and Times Square/West Side falling 3% to $76.31 per sq. ft.

Figure 8: Average Asking Rents | By Submarket



Source: CBRE Research, Q2 2020.

Penn Station's increase was due to a 150,000 sq. ft. block of space coming available at 460 West 34th Street, combined with space getting leased in buildings below the submarkets' average asking rent. In contrast, the 3% decrease in Times Square/West Side's rents were a result of TikTok taking a large block of premium-priced space off the market. Midtown's most expensive submarkets saw average asking rents drop slightly quarter-over-quarter. Plaza and Park Avenue both fell a little under 2% to $100.85 per sq. ft. and $109.39 per sq. ft., respectively. Fifth/Madison saw a slightly smaller decrease –just over 1% – to $112.21 per sq. ft, retaining its position as the most expensive submarket in Manhattan. All the remaining submarkets saw rents stay flat quarter-over-quarter due to a combination of slow leasing and few blocks of space coming available.

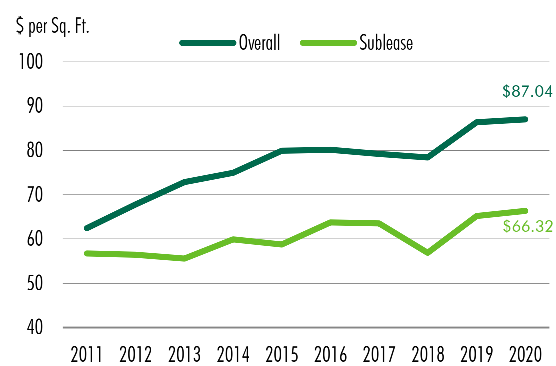
Year-over-year changes in asking rent were more substantial. Grand Central, by far the biggest mover, jumped 18% from Q2 2019 – a result of expensive blocks of space coming online in prior quarters at 1 Vanderbilt Avenue as the building nears completion. Fifth/Madison had the second greatest annual jump, rising 4% as pricier blocks came on and less expensive ones were leased. The East Side was the only other submarket to notch an upward movement in average asking rents year-over-year, rising a modest 4% to $72.08 per sq. ft. It is important to note that while these submarkets did experience rental rate increases year-over-year, they occurred well before Q2 2020 and in no way reflect repricing initiatives due to the COVID crisis.

Penn Station experienced the greatest drop in average asking rents year-over-year, falling 6% due to premium-priced new construction space getting leased in the Hudson Yards neighborhood as opposed to falling demand. Plaza and Park saw drops of 5% and 4%, respectively, year-over-year, though those too were reflective of 2019's strong leasing numbers which removed higher-priced space from the market.

For Midtown, the various submarket fluctuations resulted in an asking rent decline of 1% from the prior year, remaining within 3% of the market's all-time high. The sublease average asking rent in Midtown remained remarkably stable quarter-over-quarter at $66.32 per sq. ft. as space additions were relatively minimal.

Though asking rents have largely held steady since the advent of COVID-19, rent adjustments are on the horizon. CBRE Econometric Advisors forecast a 10–16% decline in Midtown average asking rent by Q2 2021 before seeing pricing begin to recover. Newer, amenity-rich buildings with stable occupancy levels are expected to fare better than the market overall, while older/unimproved buildings and those with higher levels of upcoming tenant roll can be expected to face pressure to drop rents.

Figure 9: Average Asking Rent | Historical



Source: CBRE Research, Q2 2020.

TAKING RENT INDEX

The taking rent index decreased 90 bps quarter-over-quarter to 92.3% – the lowest figure since October 2018. However, the index has remained steady of late, fluctuating between outer bands of 92% and 96% over the past 12 months, the tightest range among Manhattan's three markets.

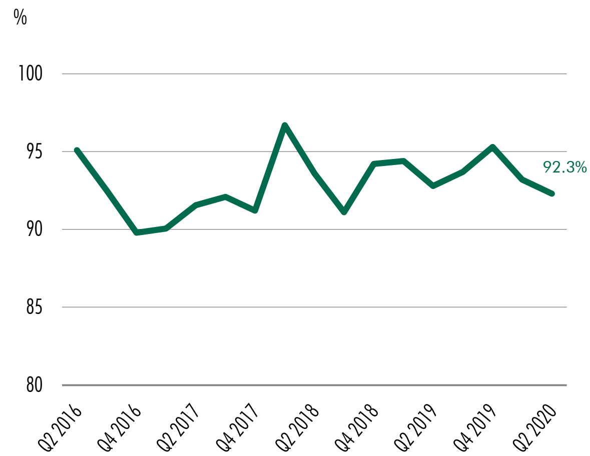
Concession packages for new leases of raw space completed over the past 18 months averaged nearly $107 per sq. ft. in tenant improvement allowance (TI) and 14 months of free rent. Tenant improvement allowances remain at all-time highs: 73% of the transactions since Q1 2019 have had TI values between $90 and $120 per sq. ft. Sentiment seems to be that the market will bear temporary instances of elevated free rent values and additional TI allowance to get deals completed. These occurrences are not yet widespread, nor is there enough deal flow to see an impact on market averages.

DEVELOPMENT PIPELINE

Due to COVID-19, New York State shut down all non-essential construction, likely resulting in some revision for near-term delivery dates. However, many major construction projects received waivers to continue work; the moratorium was lifted on June 8th, 2020. Whether longer-term deliveries will be adversely affected is not yet clear.

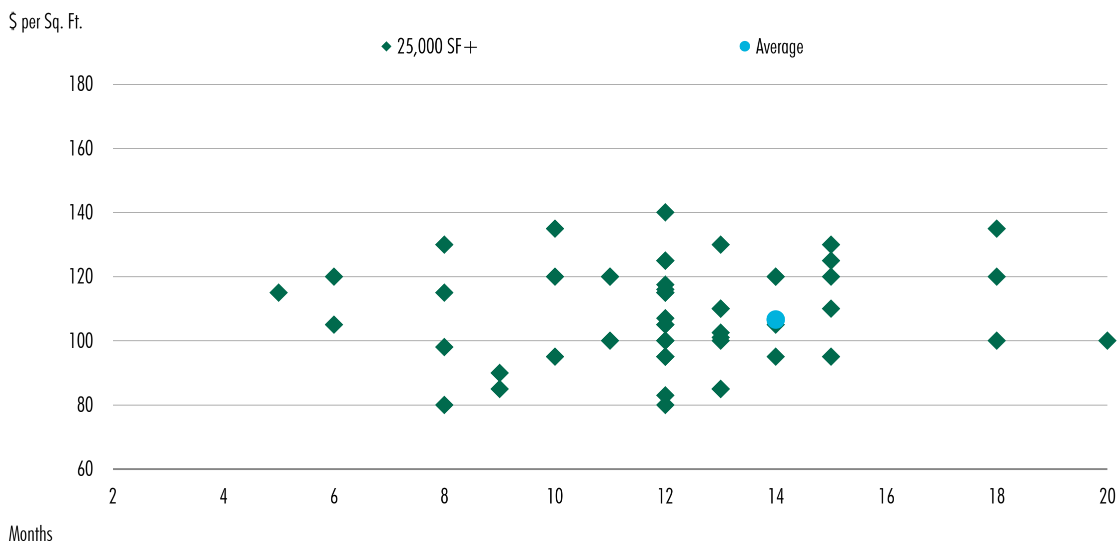
The development pipeline in Midtown currently has four major office construction projects: One Vanderbilt Avenue, 50 Hudson Yards, 66 Hudson Boulevard and Two Manhattan West. Collectively, these projects account for 9.29 million sq. ft. in new development and are 55% pre-leased.

Figure 10: Taking Rent Index | Historical



Source: CBRE Research, Q2 2020.

Figure 11: Concession Values | Rent Abatement and T.I. Allowance*



*This study examines all direct new leases larger than 25,000 RSF with a term length of at least 10 years (omits renewals and expansions). Represents a blended average of 2019 – YTD 2020.

Source: CBRE Research, Q2 2020.

SL Green's One Vanderbilt Avenue is a 1.64 million-sq.-ft. office building in the Grand Central submarket which stands at 73% pre-leased.

The remainder of the new construction projects are in the Hudson Yards neighborhood, part of the Penn Station submarket. Related's 50 Hudson Yards is a 2.90 million sq. ft. future development, currently 71% pre-leased.

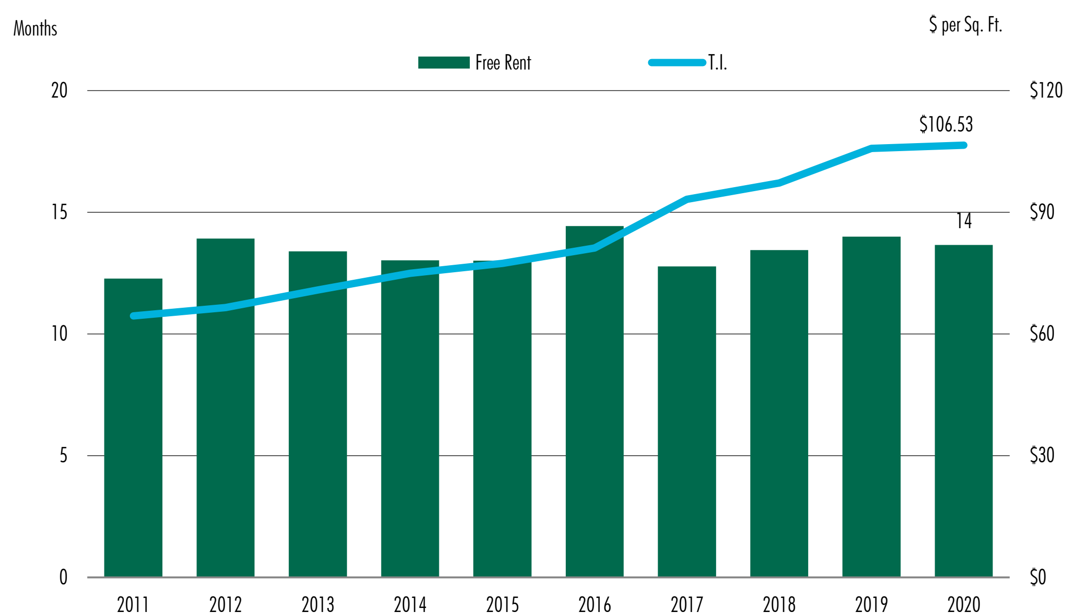
Brookfield Properties' Two Manhattan West, a 1.90 million sq. ft. office building, speculatively broke ground during Q2 2019 and shortly thereafter secured its anchor tenant in Cravath, Swaine & Moore LLP, which committed to 482,000 sq. ft.

Tishman Speyer's 66 Hudson Boulevard, also known as The Spiral, is a 2.85 million sq. ft. building just north of the new development projects at Hudson Yards and Manhattan West.

Three deals have been completed at The Spiral: Pfizer, Inc. leased nearly 800,000 sq. ft. in Q2 2018, followed by AllianceBernstein L.P., which signed on for 189,000 sq. ft. during Q2 2019, while Debevoise & Plimpton committed to 531,000 sq. ft. at 66 Hudson Boulevard in Midtown's largest deal of 2020 so far.

JPMorgan Chase has begun to demolish its headquarters at 270 Park Avenue and plans to build a new 70-story headquarters on the site. The building would be one of the first skyscrapers to go up under the new Midtown East rezoning rules surrounding Grand Central terminal.

Figure 12: Concession Values | Historical*



*This study examines all direct new leases larger than 25,000 RSF with a term length of at least 10 years (omits renewals and expansions).

Source: CBRE Research, Q2 2020.

INVENTORY AT A GLANCE

Submarket	Total Size (Mil. Sq. Ft.)	No. of Buildings
East Side	21.4	46
Fifth Avenue / Madison Avenue	12.1	28
Grand Central	46.7	85
Park Avenue	28.6	37
Penn Station	27.7	33
Plaza	11.8	24
Sixth Avenue / Rock Center	45.5	45
Times Square South	19.4	48
Times Square / West Side	31.9	43
TOTAL INVENTORY	**245.1**	**389**

DEFINITIONS

Availability — Space that is being actively marketed and is available for tenant build-out within 12 months. Includes space available for sublease as well as space in buildings under construction.

Asking Rent — Weighted average asking rent.

Concession Values — The combination of rent abatement and T.I. allowance. The graph is for new leases for raw space of 25,000 sq. ft. or greater consummated year-to-date, this excludes expansion and renewal deals.

Leasing Activity — Total amount of sq. ft. leased within a specified period of time, including new deals, expansions, and pre-leasing, but excluding renewals.

Leasing Velocity — Total amount of sq. ft. leased within a specified period of time, including new deals, expansions, and pre-leasing and renewals.

Net Absorption — The change in the amount of committed sq. ft. within a specified period of time, as measured by the change in available sq. ft.

Rent Abatement — The time between lease commencement and rent commencement.

Taking Rent — Actual, initial base rent in a lease agreement.

Taking Rent Index — Initial taking rents as a percentage of asking rents. This graph represents a 6-month rolling weighted average (for size and month).

T.I. — Tenant Improvements.

Vacancy — Unoccupied space available for lease.

Percentage of Leasing by Industry —The percentage of sq. ft. leased by an industry based on transactions where a tenant and industry have been confirmed.

SURVEY CRITERIA

CBRE's market report analyzes fully modernized office buildings that total 150,000+ sq. ft. in Midtown, including owner-occupied buildings (except those owned and occupied by a government or government agency). New construction must be available for tenant build-out within 12 months. CBRE assembles all information through telephone canvassing and listings received from owners, tenants and members of the commercial real estate brokerage community.

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