RESEARCH

NATIONAL
2Q15 OFFICE MARKET

Newmark Grubb Knight Frank

BREAK TIME'S OVER: OFFICE MARKET GROWTH RESUMES

As expected, the economy and the office market moved past their first-quarter malaise—brought on by the harsh winter, the negative effects of the strong dollar and the decline in shale oil exploration and investment. Economic growth resumed, and the office market returned to its 2014 growth trajectory featuring strong metrics across the board.

Absorption Rebounds

Tenants absorbed 16.0 million square feet in the second quarter, the strongest performance since the third quarter of 2012 and well above the 8.9 million square feet delivered. Absorption was positive in 48 of the 58 markets tracked by NGKF, led by Dallas, Silicon Valley and Boston, each absorbing more than 1 million square feet. Negative absorption was highest in Washington, DC, with negative 825,000 square feet, and Houston, with negative 506,000 square feet—markets whose respective primary industries, government and energy, are restructuring.

The surge of absorption in the second quarter raised the first half total to 20.3 million square feet, which fell short of the year-ago period by 29%—a legacy of the harsh weather in the first quarter of this year. Forty-five of the 58 markets tracked by NGKF posted positive first-half absorption, led by Dallas, Silicon Valley and Boston—the market leaders in the second quarter as well. At the other extreme, three markets accounted for a combined 6.8 million square feet of negative absorption: the aforementioned Washington, DC, Houston and—surprisingly—Manhattan, a strong market where several large blocks of space became available, as landlords sought to reposition their properties and push rents.

TENANTS ABSORBED 16.0 MILLION SQUARE FEET IN THE SECOND QUARTER, WELL ABOVE DELIVERIES

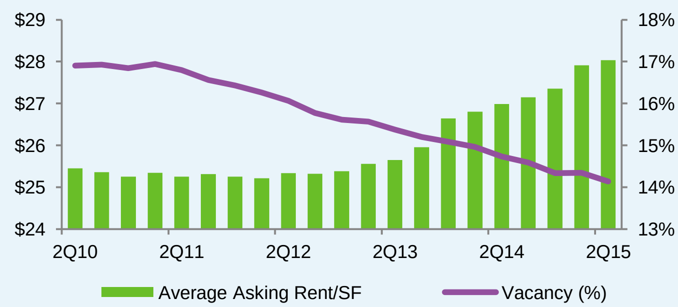
Absorption can be measured as a share of occupied space, which is a good indicator of market momentum, a sign that empty space is being filled at a rapid clip. Using this metric, first-half absorption was strongest in a range of markets across the West and South, led by Charleston, South Carolina, at 3.7%, far above the U.S. rate of 0.5%, followed by Silicon Valley at 3.3% and Greenville, South Carolina, at 2.4%. Absorption was weakest in Westchester County, New York, at negative 2.8%; Wilmington, Delaware, at negative 2.0%; and Oklahoma City and Houston, tied at negative 1.3%.

Current Conditions

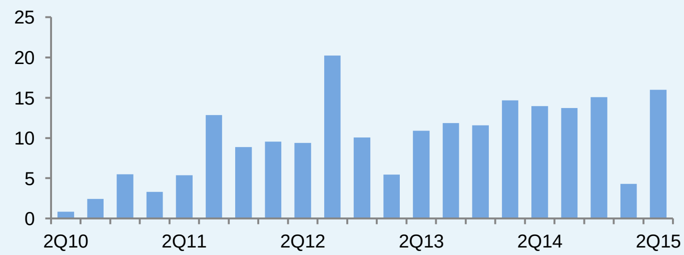
- Tenants absorbed 16.0 million square feet in the second quarter, well above the 8.9 million square feet delivered.
- Construction maintained its steady advance, ending the quarter with 85.6 million square feet in the pipeline.
- The robust pace of absorption pushed the vacancy rate lower to 14.1%.
- The average asking rent ended the quarter at $25.43/SF, up 0.4% from last quarter and up 3.9% from a year ago.

Market Analysis

Asking Rent and Vacancy



Net Absorption
Square Feet, Millions



Market Summary

	Current Quarter	Prior Quarter	Year Ago Quarter	12 Month Forecast
Vacancy Rate	14.1%	14.3%	14.7%	↓
Net Absorption*	16.0	4.3	14.0	↔
Average Asking Rent/SF	$28.03	$27.91	$26.99	↑
Under Construction*	85.6	79.1	61.2	↑
Deliveries*	8.9	7.7	6.9	↑

* Square feet, millions

In the slow-growth Midwest, Detroit posted the strongest first-half absorption metrics, outpacing much-larger Chicago and the more dynamic Minneapolis-St. Paul and Columbus markets. Detroit office tenants absorbed more than 1 million square feet year-to-date through June, good for 7th place among NGKF's 58 tracked markets. Chicago, Minneapolis and Columbus absorbed between 400,000 and 800,000 square feet apiece. Detroit is staging a fairly remarkable recovery, given the depth of its decline during the recession and the poor performance of its labor market for several years before that. Credit the surging global demand for vehicles and the region's surprising emergence as a technology hub—concentrated on the automobile industry, but branching into other sectors of the economy.

Supply Pipeline Expands Gradually

Construction activity advanced at a modest pace, ending the second quarter with 85.6 million square feet in the pipeline. This was up from 79.1 million square feet in the first quarter and up from 61.2 million square feet in the year-ago quarter. Space in the pipeline remained below the pre-recession peak of 110.6 million square feet. Houston, Manhattan and Silicon Valley each had more than 8 million square feet under construction at mid-year. Nearly two-thirds of the space under construction at mid-year was pre-leased, up modestly from earlier in the current cycle.

Central business district markets (CBD) accounted for 45% of space under construction at mid-year, above their 31% share of the total inventory—reflecting the growing demand for space in downtown markets.

As a share of the total inventory, construction activity was highest by far in Silicon Valley at 11.7%, compared with the U.S. average of 1.8%. Rounding out the top three high-construction markets after Silicon Valley were Seattle and San Francisco.

Major projects still in the construction pipeline included 3 World Trade Center in Lower Manhattan, a 2.8 million-square-foot project that is about one-third pre-leased; Apple's new donut-shaped headquarters, a 2.8 million-square-foot build-to-suit in Cupertino, California; and FMC Technologies Campus, a 1.7 million-square-foot build-to-suit in Houston. Space completions through the first half of 2015 totaled 16.5 million square feet, 17%—or 2.4 million square feet—above the comparable period in 2014. First-half completions were comfortably under the 20.9 million square feet absorbed during the period, meaning that there was enough demand for the new supply while continuing to backfill existing supply.

The list of high-profile projects coming online in the second quarter included a 578,000-square-foot build-to-suit for Cox Communications in Atlanta; a 435,000-square-foot build-to-suit for Facebook in San Francisco; and Colorado Tower, a 373,334-square-foot multi-tenant property in Austin that was 97% pre-leased when it opened.

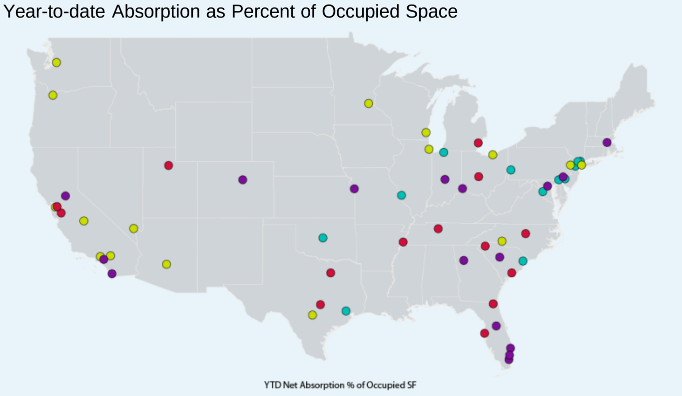
Shrinking Options for Tenants

The robust pace of absorption in the second quarter combined with the steady delivery of new supply pushed the vacancy rate lower to 14.1%, down from 14.3% in the first quarter and down from 14.7% one year ago. This is the lowest level since the third quarter of 2008, but still above the pre-recession nadir of 12.8% in the fourth quarter of 2007.

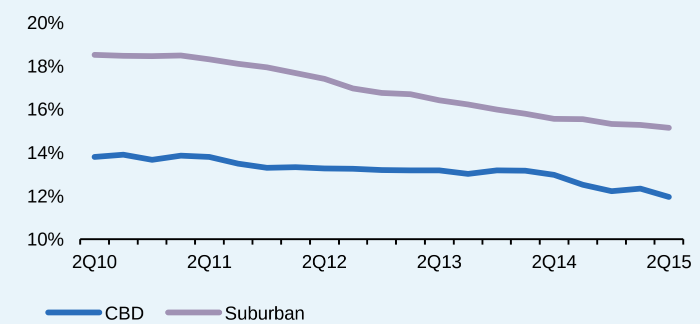
TWO-THIRDS OF THE SPACE UNDER CONSTRUCTION WAS PRE-LEASED, UP MODESTLY FROM EARLIER IN THE CYCLE

Demand Momentum Map

Year-to-date Absorption as Percent of Occupied Space



Vacancy Rate, CBD vs. Suburban



Source: CoStar, Newmark Grubb Knight Frank

Vacancy was lowest in San Francisco at 4.7% and highest in Northern New Jersey at 23.0%. Over the past four quarters, vacancy tightened in 48 of the 58 NGKF-tracked markets, led by Jacksonville, Florida, down by 337 basis points, well above the 60-basis-point decline in the U.S. Other markets that recorded rapid vacancy declines included Salt Lake City and Tampa-St. Petersburg. At the other extreme, Houston posted a year-over-year vacancy increase of 271 basis points. Other markets where vacancy rose by a percentage point or more over the past four quarters included Westchester County, New York, and Wilmington.

Rents Escalate at a Moderate Pace

The average asking rent across the U.S. ended the second quarter at $28.03/SF full service, up 0.4% from the prior quarter and up 3.9% from the second quarter of 2014. San Francisco, Nashville and Silicon Valley posted double-digit rent gains over the past four quarters. Markets with negative rent movement during this period included Salt Lake City, Oklahoma City and Washington, DC.

THE ECONOMY WILL CONTINUE TO GENERATE MODERATE TO STRONG DEMAND FOR OFFICE SPACE

Markets across the U.S. report a wide range of tenant reactions to rising rents, depending on how quickly rates have increased. Rents were close to the bottom of the recession cycle five years ago. Since then, asking rents have risen by an average of 12.1% across the U.S., ranging from San Francisco, where rents have increased more than 70%, to Las Vegas, where rents remain 20% lower than they were five years ago. Thus, some markets and submarkets continue to favor tenants, while others are extreme landlord markets. Tenants in the former category will have more options to choose from, more negotiating leverage and more opportunities to move up to higher quality space. Tenants in the latter category will face sticker shock when they go to renew, will have fewer options, and may consider trading down in the quality of their space.

What to Expect

Recovered from its first-quarter malaise, the economy now appears in good health, fueled by resilient consumers, a solid labor market and continued low interest rates. Office employment, which includes the sectors of professional and business services, finance and information, has been growing at a steady 3.0% annual rate since late last year, beating total employment, which has been expanding in the low-2% range. This is showing up in strong absorption of office space, steady rent growth and declining vacancy rates. Construction is also increasing, but has not yet caught up with demand.

Global weakness persists in China, the eurozone, the Middle East and many emerging markets, with the IMF forecasting the lowest rate of growth this year since the recession. But the U.S. economy has managed to push ahead despite these headwinds and will continue to generate moderate to strong demand for office space from tenants and very strong demand from investors.

Select Leasing Transactions

Tenant	Market	Building	Type	Square Feet
Verizon Wireless	Northern New Jersey	295 N Maple Ave	Sale/Leaseback	1,400,000
Skadden, Arps, Slate, Meagher & Flom	New York, NY	400 W 33rd St	Direct	538,321
Amazon	Seatte, WA	399 Fairview Ave N	Direct	418,999
Morgan Stanley	New York, NY	750 Seventh Ave	Direct	400,000
Amazon	Seatte, WA	300 Boren Ave N	Direct	391,005

Select Sales Transactions

Building	Market	Sale Price	Price/SF	Square Feet
11 Madison Ave	New York, NY	$2,500,000,000	$1,130	2,212,389
730 Fifth Ave (Crown Building)	New York, NY	$1,775,000,000	$4,438	400,000
233 S Wacker Dr (Willis Tower)	Chicago, IL	$1,300,000,000	$343	3,787,238
230 Park Ave	New York, NY	$1,200,000,000	$990	1,212,576
701 5th Ave (Columbia Center)	Seattle, WA	$725,000,000	$478	1,516,204

NATIONAL
2Q15 OFFICE MARKET

Market Statistics

Market	Inventory SF	SF Under Construction	SF Absorbed This Quarter	SF Absorbed YTD	% Vacant	Average Asking Rent/SF
Atlanta	143,568,063	500,000	633,904	1,058,284	18.6%	$21.24
Austin	61,755,192	2,103,554	588,350	1,217,903	11.9%	$30.23
Baltimore	77,337,193	355,727	467,005	609,550	12.9%	$21.42
Boston	176,598,048	3,500,982	1,055,371	1,565,404	11.1%	$35.46
Broward County, FL	32,677,690	143,535	164,207	237,312	13.2%	$24.48
Charleston, SC	11,302,070	0	127,055	381,087	8.3%	$19.62
Charlotte	66,986,579	1,687,068	148,383	270,796	12.3%	$21.86
Chicago	247,929,552	3,393,595	560,741	435,610	17.0%	$26.79
Cincinnati	59,746,955	964,148	226,661	479,905	15.9%	$15.61
Cleveland	39,043,615	0	140,717	197,270	18.3%	$17.52
Columbia, SC	10,655,693	0	48,057	130,539	12.5%	$15.62
Columbus	54,937,028	941,507	279,957	781,258	10.8%	$16.65
Dallas	231,164,774	5,930,316	1,771,674	3,059,914	18.4%	$22.35
Delaware	16,798,706	0	-78,180	-268,758	19.0%	$23.48
Denver	92,413,184	2,600,090	512,111	1,029,930	13.5%	$24.57
Detroit	72,540,090	85,000	471,697	1,034,725	20.3%	$18.81
Fairfield County, CT	41,964,061	0	227,132	-54,142	23.0%	$35.00
Fresno	19,646,536	16,410	9,485	29,302	12.9%	$19.92
Greenville, SC	14,014,221	0	7,375	292,101	12.4%	$15.69
Houston	219,583,567	8,827,084	-506,458	-2,379,441	15.9%	$28.17
Indianapolis	60,420,826	387,400	292,843	401,848	11.4%	$17.45
Inland Empire, CA	30,885,970	0	13,607	156,068	15.3%	$19.44
Jacksonville	31,640,829	24,000	289,733	590,456	15.7%	$18.11
Kansas City	71,696,056	20,000	299,855	534,045	14.3%	$17.90
Las Vegas	37,326,415	145,000	-30,140	76,534	21.6%	$19.77
Long Island	55,398,680	0	163,244	88,971	12.1%	$26.13
Los Angeles	191,783,523	2,002,495	704,229	1,162,543	15.1%	$33.72
Manhattan	450,945,632	8,625,432	-45,945	-3,324,109	8.2%	$68.80
Memphis	33,544,239	610,000	37,700	440,389	14.4%	$16.59
Miami	47,056,369	251,512	203,710	361,160	14.1%	$31.44
Milwaukee	45,697,763	358,017	220,116	241,054	12.5%	$16.26
Minneapolis	128,933,562	1,068,479	111,540	509,258	11.2%	$17.72
Myrtle Beach, SC	2,583,940	0	-19,423	-16,999	9.9%	$12.16
Nashville	49,886,250	2,517,997	653,366	848,124	7.3%	$22.60
New Jersey Northern	165,901,420	393,900	626,399	544,831	23.0%	$24.41
New Jersey Southern	17,075,059	250,000	-16,116	-123,636	18.1%	$20.57
Oakland/East Bay	71,331,661	105,000	752,669	925,763	13.6%	$26.29
Oklahoma City	14,700,166	814,541	-97,506	-153,692	19.1%	$14.50
Orange County, CA	91,352,028	425,044	122,335	962,164	12.0%	$26.04
Orlando	68,123,552	80,000	212,411	523,100	10.8%	$19.97
Palm Beach	25,875,649	0	166,635	256,349	17.9%	$28.31
Philadelphia	106,703,989	2,001,400	524,642	745,176	15.0%	$25.70
Phoenix	74,130,897	2,878,959	168,413	223,650	21.5%	$21.72
Pittsburgh	52,937,091	1,636,000	-178,199	-263,299	16.0%	$21.74
Portland	56,346,587	512,180	208,695	265,859	10.7%	$22.48
Raleigh/Durham	59,447,538	543,269	768,918	1,011,806	12.3%	$20.54
Sacramento	58,801,439	110,157	-176,095	-168,542	19.2%	$21.96
Salt Lake City	30,827,472	1,476,130	560,787	627,562	8.4%	$20.51
San Antonio	44,048,804	772,822	130,996	146,467	13.2%	$20.31
San Diego	70,628,151	1,726,076	390,703	858,567	13.1%	$28.92
San Francisco	76,797,742	4,267,595	129,856	265,943	4.7%	$65.71
Seattle	118,442,888	7,365,706	156,055	434,778	11.9%	$31.16
Silicon Valley	71,697,253	8,352,868	1,748,811	2,147,768	9.0%	$41.28
South Bend/Mishawaka, IN	4,081,754	0	5,878	-42,578	10.8%	$17.85
St. Louis	75,838,588	0	211,794	-290,975	14.3%	$18.44
Tampa/St. Petersburg	64,184,143	221,998	551,844	937,909	13.8%	$21.24
Washington, DC	364,199,758	4,586,357	-825,543	-1,137,832	16.6%	$36.19
Westchester County, NY	27,823,854	0	82,512	-609,438	23.0%	$27.08
National	**4,739,760,354**	**85,579,350**	**15,976,573**	**20,265,591**	**14.1%**	**$28.03**

ECONOMIC CONDITIONS

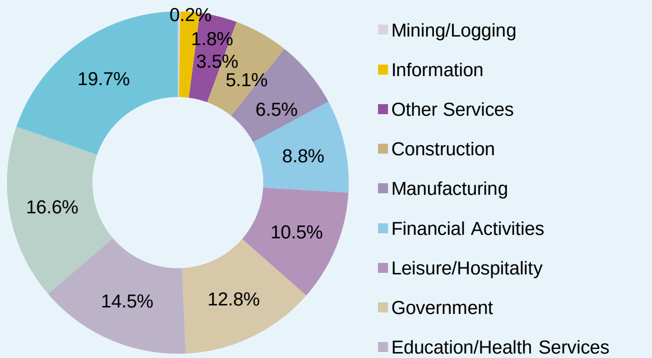
Job growth rebounded in the second quarter following a harsh winter and a port strike. Employers added 664,000 net new payroll jobs, seasonally adjusted, up from 586,000 jobs in the first quarter. Office employment has been outperforming the overall labor market, growing at a rate of 3.0% over the past 12 months, compared with the 2.1% increase in total nonfarm employment during this period.

The unemployment rate fell to 5.3% in June, down from 6.1% a year ago, while the U-6 rate, which measures slack in the labor force, was 10.5%, down from 12.0% a year ago.

Despite shortages of skilled workers, wage growth in June increased just 2.0% from a year ago, in the range it has occupied since the recession. Low wage growth has restrained inflation and the pace of the recovery. The 12-month inflation rate was 0.1% in June, while the core rate excluding food and energy was 1.8%, below the Federal Reserve's target rate of 2.0%.

Employment By Industry

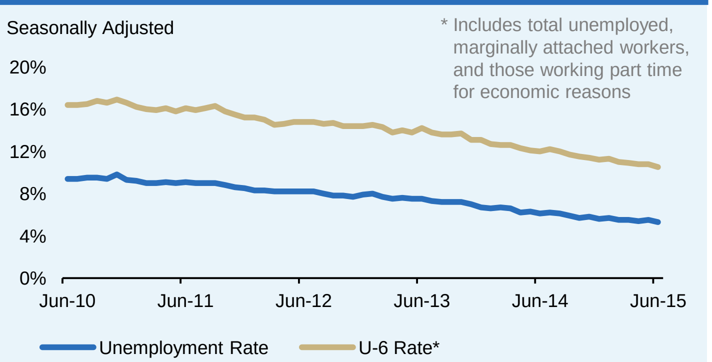
United States, 2014 Annual Average



Source: U.S. Bureau of Labor Statistics

Unemployment Rate

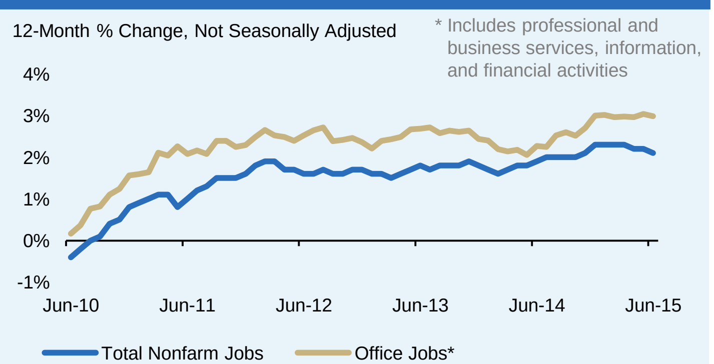
Seasonally Adjusted



Source: U.S. Bureau of Labor Statistics

Payroll Employment

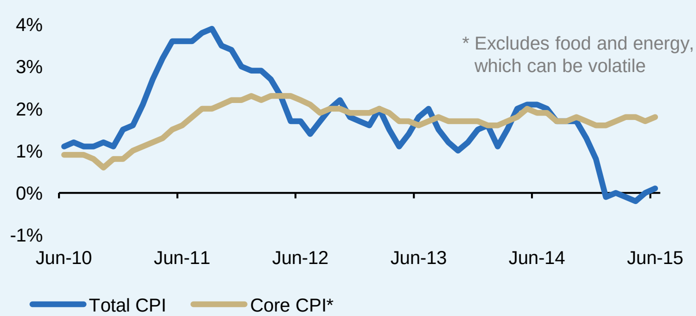
12-Month % Change, Not Seasonally Adjusted



Source: U.S. Bureau of Labor Statistics

Consumer Price Index (CPI)

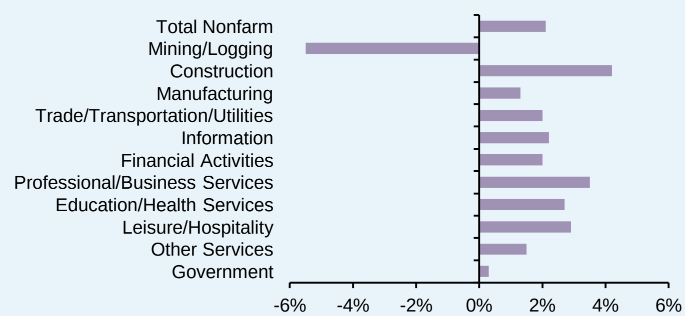
All Items, 12-Month % Change, Not Seasonally Adjusted, 1982-84=100



Source: U.S. Bureau of Labor Statistics

Employment Growth by Industry

June 2015, 12-Month % Change, Not Seasonally Adjusted



Source: U.S. Bureau of Labor Statistics

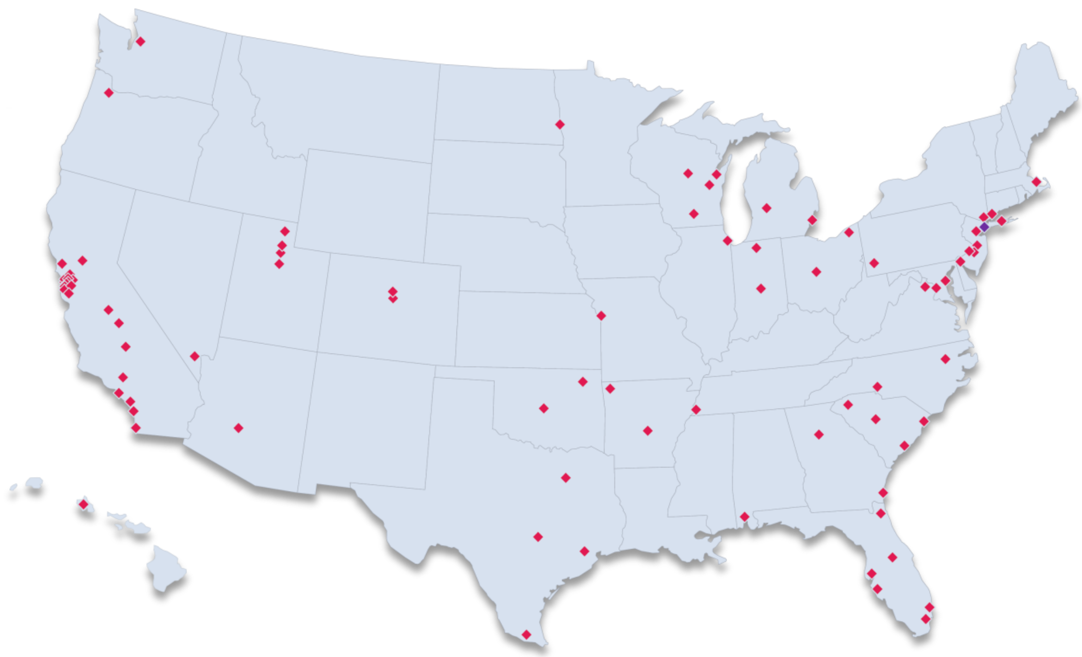
RESEARCH

Newmark Grubb Knight Frank

Chicago
500 W Monroe St
Suite 2900
Chicago, IL 60661
312.224.3200

Robert Bach
Director of Research - Americas
312.224.3244
rbach@ngkf.com

Newmark Grubb Knight Frank United States Office Locations



Newmark Grubb Knight Frank has implemented a proprietary database and our tracking methodology has been revised. With this expansion and refinement in our data, there may be adjustments in historical statistics including availability, asking rents, absorption and effective rents.

Newmark Grubb Knight Frank Research Reports are also available at **www.ngkf.com/research**