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2021

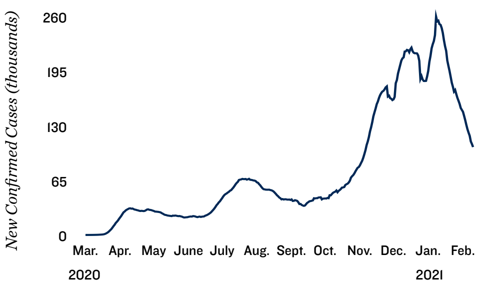
U.S. Commercial Real Estate

INVESTMENT OUTLOOK

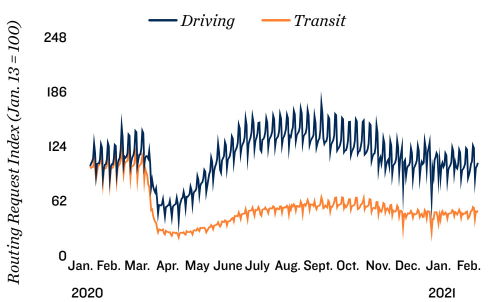
OFFICE

Health Crisis Upends Commercial Real Estate; Uncertainty Will Carry Well Into 2021

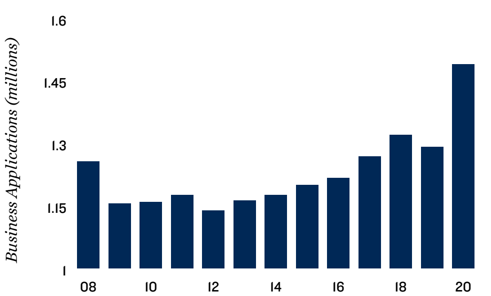
Daily U.S. COVID-19 Cases Ease From Spike



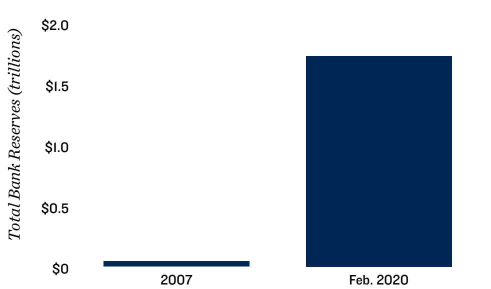
Aversion to Public Transit



New Business Applications Surge



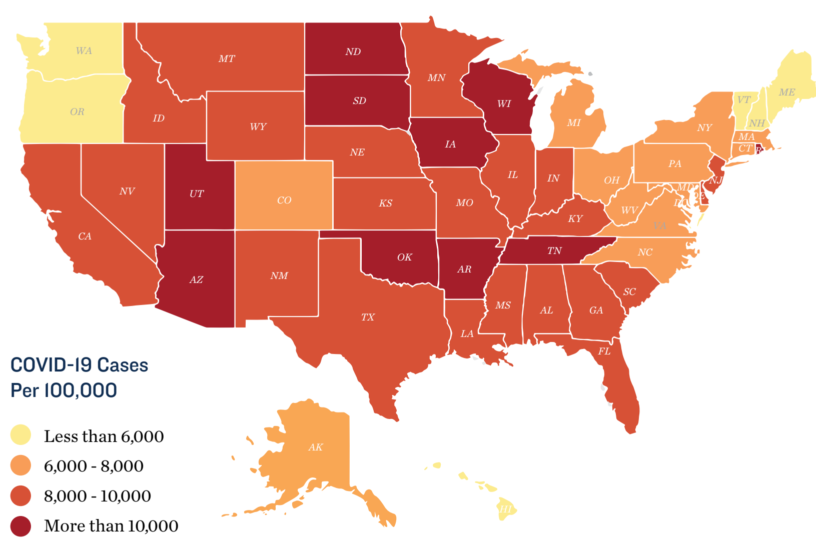
Banks in Stronger Position Than in 2007



Pandemic transforms commercial real estate. COVID-19 changed the world in early 2020 as efforts to curb the spread of the pandemic had a dramatic impact. Stay-at-home orders, the need to physically distance, and having to abide by health and safety protocols had harsh effects on many real estate sectors. Hospitality, seniors housing and brick-and-mortar retail were hit hard while others including necessity-based retailers, medical offices, e-commerce retailers, life science and pharmaceutical firms, and many industrial segments thrived. As of February 2021, more than 486,000 Americans have died from the coronavirus and after reaching a peak in mid-January that strained healthcare systems across a wide swath of the U.S., cases, hospitalizations and deaths have begun to taper.

Health crisis exacerbated demographic shifts. Employers laying off workers and sending staff home to work remotely contributed to an acceleration of demographic changes that were already underway. Economic uncertainty led many households to search for lower-cost housing, while the need to work from home and attend school online generated demand for larger spaces. Commute times became less of a factor in housing decisions, pushing residential and apartment demand away from dense urban cores that are more reliant on mass transit to the benefit of suburbs as well as secondary and tertiary markets. Although driving returned during the summer months, public transit usage remains well below the pre-coronavirus level as fewer people are commuting to offices and physical distancing protocols limit ridership. Higher unemployment is also leading to more people spending time at home, which consequently may have boosted new business applications to the highest rate since the Great Recession. This surge in entrepreneurship could have positive results in the years ahead.

Coronavirus Cases Continue to Spread*



** As of Feb. 11, 2021*

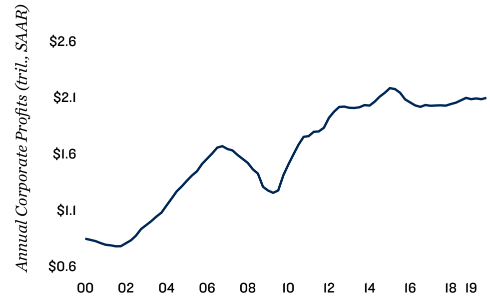
Sources: Apple; Federal Reserve; New York Times; U.S. Census Bureau

Government Response, Market Liquidity, Fast-Tracked Vaccine Development Provide Optimistic Outlook

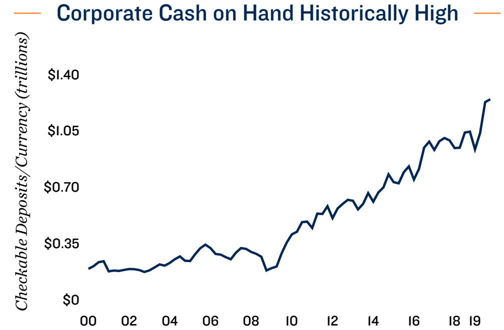
Economy jolted as coronavirus spread. The economy was on relatively solid footing heading into the pandemic. Company profits were hovering near the 20-year peak and corporate cash on hand had set a new high, supplying many firms with cushions to weather a downturn. Bank reserves were also significantly above those registered in 2007, providing a much healthier comparison to the start of the Great Recession. Through the health crisis, the money supply has remained liquid as the federal government quickly infused cash into the market and funded stimulus measures via the CARES Act and other legislation. The Paycheck Protection Program (PPP) was one of several systems that assisted in keeping people employed and allowed businesses and households to make rent payments. Additional infusions in 2021 will provide further economic stimulus.

Immunizations provide a path forward. In response to the coronavirus, the government initiative Operation Warp Speed was established to fast track the development and approval of vaccines to combat COVID-19. By the end of 2020, two vaccines had been approved and others were in trial phases. Inoculations were underway by mid-December, providing some hope, especially to real estate segments hit hard by the pandemic. Immunization efforts, however, were slow to ramp up, extending the time needed before enough people are vaccinated to a level that would provide herd immunity and allow a freer movement of people. Although clarity is in sight, these delays will prolong uncertainty for investors well into 2021.

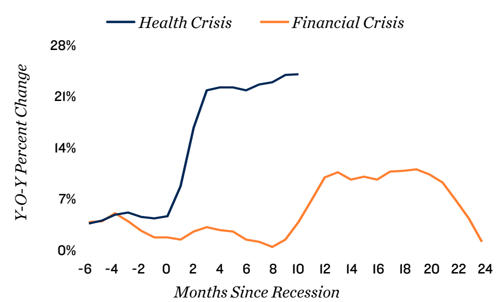
Pre-Crisis Profits Near Record



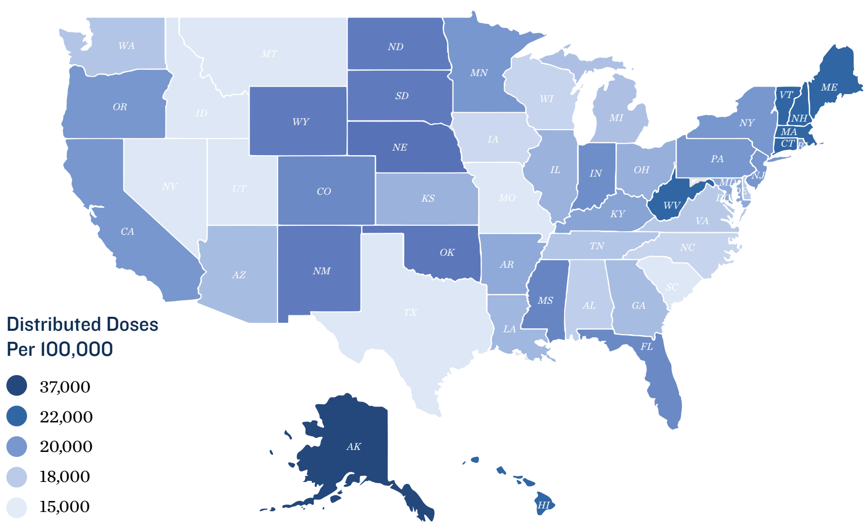
Corporate Cash on Hand Historically High



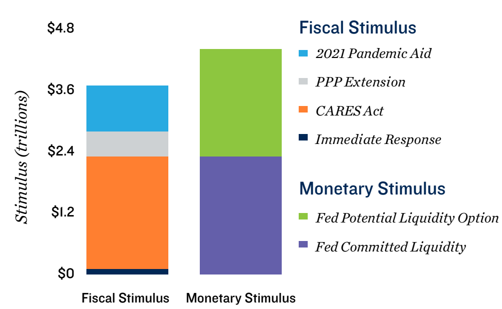
Money Supply Gets Big Boost



Immunizations Ramping Up Across the Nation*



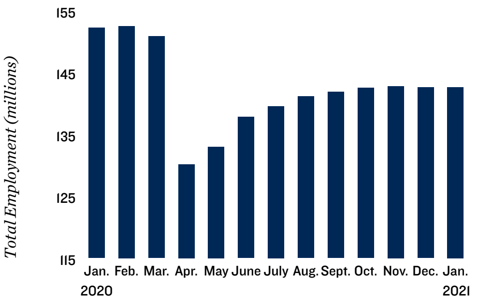
Government Stimulus Response



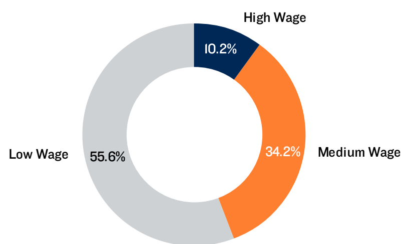
** As of Feb. 11, 2021*

Sources: BEA; Federal Reserve; U.S. Census Bureau

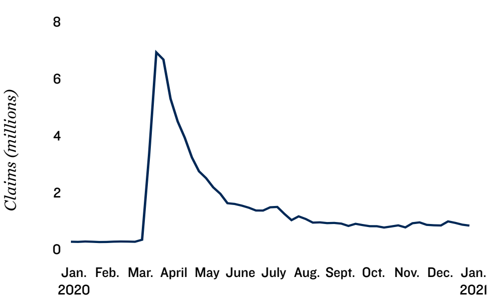
Employment Trends



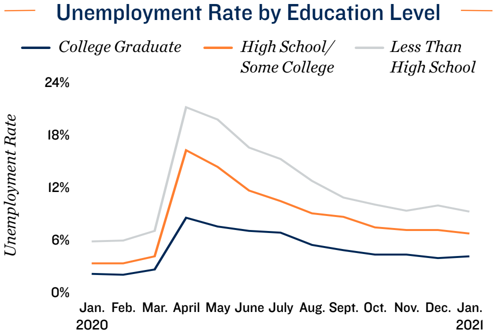
Share of Job Losses*



Unemployment Claims



Unemployment Rate by Education Level



** February to December 2020*

Sources: BLS; ETA

Possibilities for Second Growth Surge or Double Dip in 2021 Hinge on Vaccine Rollout and Labor Recovery

Vaccine distribution to play a critical role in economic outlook. The nation's economic situation has regained much of the momentum lost last spring as it continues along an upward path in 2021. Ongoing health challenges and other potential hurdles may suspend or abate that progress, however. If the current set of COVID-19 vaccines are distributed as efficiently as predicted, then enough people may be inoculated by midyear to safely allow most businesses to fully reopen. Employed consumers with idle cash on hand from months in sequestration will be able to more freely travel and patronize bars, restaurants, entertainment venues, and brick-and-mortar retailers, potentially boosting the economy. If, however, the pace of the vaccine rollout is slowed or the nature of the virus changes, these exogenous encumbrances to the economy will remain in place longer. Employers who are challenged by physical distancing requirements and areas of the country where infection risk is higher will fall further behind other segments of the economy. This disparity, if severe enough, could lead to another quarterly economic contraction. The fortitude displayed during the second half of 2020 makes this scenario improbable, however, especially with continued government support.

Economy has been resilient so far, aided by robust federal aid. The forced closure of many businesses last year led to the sharpest decline in Gross Domestic Product in the post-World War II era. After sliding 5 percent in the first quarter, U.S. GDP fell an annualized 31.4 percent in the April-to-June period as 22 million jobs were shed and the unemployment rate soared to 14.8 percent. This unprecedented shock was met with an equally unprecedented government response. Applying lessons learned during the last downturn, the Federal Reserve and Congress collectively delivered roughly $5 trillion in aid within a matter of weeks, divided between direct fiscal stimulus and added financial market liquidity. These actions, followed by the implementation of other lending programs and federal legislation in subsequent months, helped GDP leap 33.4 percent in the third quarter and a more modest 4 percent in the fourth quarter. The strong gains made in the second half of the year mostly offset the earlier losses, translating to an overall economic contraction of 3.5 percent in 2020.

Labor market recovering but some sectors are falling behind. Over half of the jobs lost in March and April last year were restored or replaced by December, but as 2021 progresses certain industries face a longer road to total recovery than others. Physical distancing requirements and travel restrictions had a disproportionate impact on the leisure and hospitality sector, which encompasses hotels, bars, restaurants and other entertainment venues. While the overall employment base remained 6.5 percent below its pre-pandemic level at the start of 2021, the leisure and hospitality sector was still down 23.2 percent. Conversely, staff working in essential services or in positions more easily shifted to a remote setting were better protected. The number of jobs in financial activities, construction and in the trade, transportation and warehousing sector were all at or within 3 percent of their February 2020 mark by the start of the new year. How the labor market improves going forward will depend on how well vaccines are administered. If infection rates drop enough to permit widespread reopening and social patterns normalize, many of the jobs most impaired by the health crisis could quickly return, although not all roles are likely to be restored this year as some employers have permanently closed.

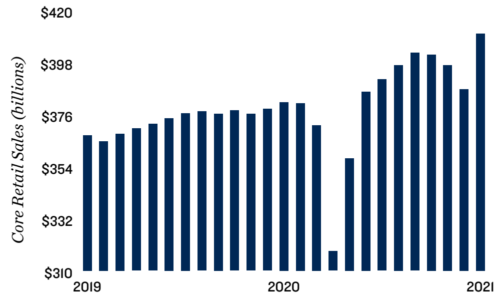
Administration Weighs Policy Goals Against Stimulus Needs While the Federal Reserve Guides Inflation

Biden administration must balance policy objectives and health crisis management. President Biden campaigned on a platform of widespread legislative reform, including taxation, healthcare and public spending on infrastructure. Achieving these goals must be managed in relation to the immediate needs of the health crisis. Some intended policy reforms, such as increasing taxes on businesses and investors, could weigh on economic growth in the short term. Even if political division in Congress does not preclude the passage of wide-sweeping changes, the focus of the legislative and executive branches will likely to be dominated by the health crisis through at least the middle of the year. Making more substantial alterations to laws and regulations could create uncertainty among consumers and investors, dampening the intended effects of stimulus measures that the Biden administration is currently pursuing.

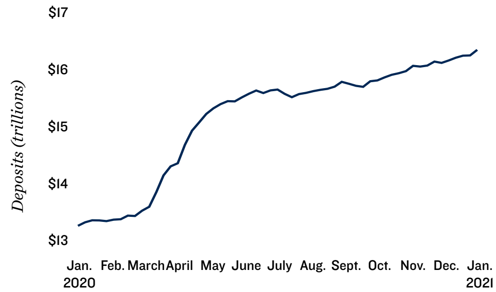
Additional federal aid likely incoming; holds significant implications on growth. The $900 billion stimulus package passed at the end of last year is serving as a vital economic stopgap as the country deals with the difficult health challenges. Many of the legislation's key benefits, such as renewed federal unemployment insurance, will nevertheless fade by the spring. The Biden administration is therefore pursuing a $1.9 trillion stimulus package to further buttress the economy. The legislation would include a third round of larger direct payments to taxpayers as well as expanded unemployment benefits, rental assistance, and funding for state and local governments. While the final stipulations of the bill are almost certain to change, the incoming aid will uplift the economy in the near term, but at the cost of introducing some potential longer-term risks. The extensive deficit spending necessitated by the health crisis will likely result in an overall higher tax burden down the line, whether at the local or federal level or both. The ample amount of liquidity injected into the market also raises inflation risk.

The Federal Reserve continues to carefully monitor inflation. As this year progresses, the Fed will have to walk a tightrope balancing economic growth and the potential for accelerated inflation. The Federal Open Market Committee has already signaled that it is willing to allow inflation to rise above a 2 percent annual growth rate following multiple years of below-target increases. To what extent above that threshold the FOMC will permit is as of yet unclear. Even so, the Fed may still be forced to raise interest rates and tighten monetary policy later this year if the risk of spiraling inflation becomes likely. This shift in policy could elicit an unintended reaction from the market, derailing economic growth in unexpected ways. If the central bank acts too early it could also prematurely temper economic growth. Even if the FOMC executes its strategy flawlessly, high inflation could still occur. Recent government actions have injected ample liquidity into the market. At the same time, many consumers have added to their savings while staying at home, expanding their potential spending power. The financial standings of many households have also improved via rising home equity values, a byproduct of a competitive single-family housing market fueled by low interest rates and recent lifestyle changes. All of these factors together create a scenario in which, once the health crisis is mitigated, consumer spending substantially jumps ahead of the available supply of goods and services, raising prices. Depending on the timing, however, this wave of spending could also act as its own form of stimulus.

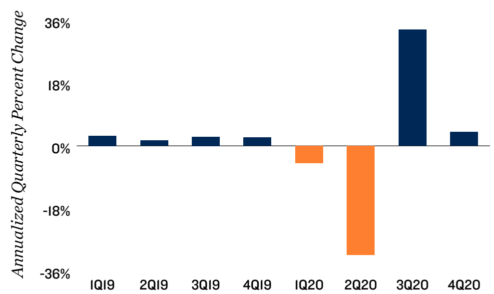
Core Retail Sales Bounce Back



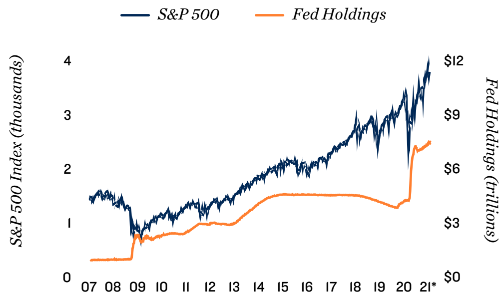
Savings Deposits Steadily Climbing



GDP Growth Trends



Fed-Injected Liquidity Lifting Equity Prices

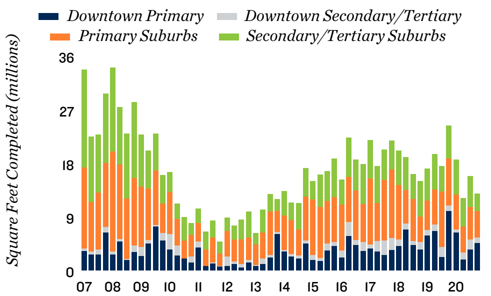


** Through January*

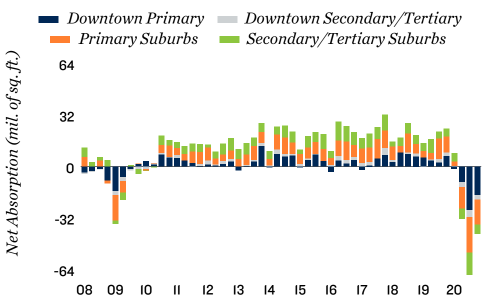
Sources: BEA; Federal Reserve; Standard & Poor's; U.S. Census Bureau

OFFICE

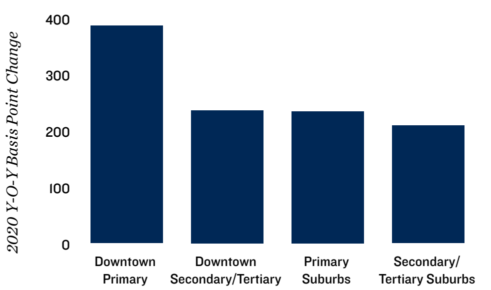
Office Construction



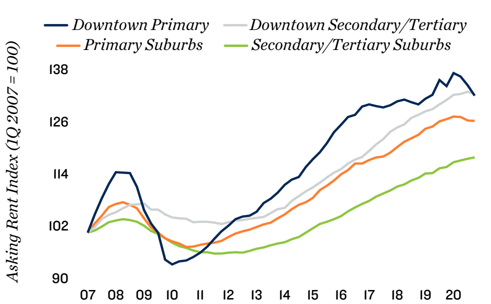
Absorption Downtown vs. Suburbs



Largest Vacancy Change in Downtown



Rent Index Falls Most Downtown



Source: CoStar Group, Inc.

Companies Delay Office Space Decisions as They Await Clarity; Health Crisis Redefines Sector Outlook

Coronavirus drives office sector transformation. The significant pandemic-driven changes to the office sector last year will carry into 2021 and beyond as companies adopt innovative new operations models. Buildings, particularly in the urban core, emptied last year as companies downsized and shifted their staff to working from home. To meet health and safety standards, facility operators quickly enhanced their cleaning procedures, upgraded HVAC systems, erected plexiglass barriers, closed shared spaces and added other physical-distancing measures to keep workers safe. But the biggest question office investors face is whether companies will bring their workforce back to the office, and if they do, when that will be. Companies have become increasingly nimble, adding sophisticated remote-work capabilities, and many have suggested that staff will have the option to work remotely for an extended period. This has allowed workers to migrate from downtown housing to larger, lower-cost options in the suburbs and to smaller cities across the country, begging the question of how long it will take for the urban core, particularly in gateway cities, to recover.

The future of office space demand. Most companies have effectively halted their office space expansion plans, shelving growth strategies until the vaccine reaches a critical mass of the population and clarity on the future of office work emerges. Business leaders know that they will have to entice workers back to the office at some point, but they are not sure when that will be. Most employees, particularly younger staff members in the early stages of career development, prefer to return to the office at least some days where they can more easily collaborate, build relationships and be mentored. Until the health risks are addressed, however, companies are reluctant to place their employees at risk. As a stop-gap solution, many firms are negotiating short-term extensions for expiring leases, often paying a modest premium for the shorter lease duration. One of the most important unanswered questions business leaders face is at what level their workers will return to the office full time and if they will need to enhance the space allocations per employee to increase physical distancing in the office. This created a significant band of variance in the outlook for office space demand — if a significant portion of the labor force continues to work from home after the pandemic, then the need for office space will likely fall, but if companies expand the allocated space per employee, space demand could remain stable or even grow.

Labor force drives office strategies. Historically, companies often relocated new hires to principal office locations, but a recent trend accelerated by the pandemic has been the opening of satellite offices located proximate to concentrations of prime personnel. Millennial workers, many now focused on family formation, have capitalized on the work-from-home opportunity to relocate to suburban areas and to smaller, secondary and tertiary cities. Companies have begun to adapt, targeting low-rise suburban space closer to employees. This lower-cost space, often with now-favored private entrances, offers employers more space per employee for physical distancing and more control over the workspace to moderate potential health risks. This trend shift, reminiscent of the 1980s baby boomer-driven suburban expansion, could reshape the office market in coming years.

Visit MarcusMillichap.com to explore the industry's largest inventory of exclusive Office listings.

Momentum Markets

Atlanta
Charlotte
Minneapolis-St. Paul
Raleigh
Riverside-San Bernardino
Sacramento
Tampa-St. Petersburg
West Palm Beach

- Entries in momentum markets are either outperforming the U.S. average or are holding steady. These metros are also gaining traction due to pandemic driven in-migration.
- Southern markets dominate this segment as the coronavirus sped up the trend of migration to metros with lower-cost housing such as Atlanta, Sacramento and Charlotte in the Sunbelt.

In-Migration Tailwinds

Boston
Houston
Indianapolis
Kansas City
Orlando
Phoenix
San Diego
Seattle-Tacoma
St. Louis
Washington, D.C.

- Metros in this segment have vacancy that is moderate or higher than the U.S. level due in part to restrained negative absorption. Pandemic-related migration also support rent gains in some markets.
- Higher job gains are drawing residents to these metros that include areas with growing tech employment including Seattle-Tacoma, Boston and Indianapolis.

Nearing Recovery

Baltimore
Cincinnati
Cleveland
Columbus
Fort Lauderdale
Las Vegas
Louisville
New Haven-Fairfield County
Oakland
Pittsburgh

- Although these markets have registered a temporary loss in absorption, a restrained development pipeline will not pose an overdevelopment problem in the near term.
- Smaller markets dominate this segment, many in the Midwest. Some metros such as Louisville, Cincinnati and Cleveland also have less available sublease inventory.

Development Overhang

Austin
Chicago
Dallas/Fort Worth
Miami-Dade
Nashville
Salt Lake City
San Antonio
San Jose

- These markets are characterized by rising vacancy driven mainly by an increase in inventory amid a slowdown in leasing activity.
- Markets with a growing population and tech employment base dominate this category as construction projects started in a different environment pre-pandemic and the recent increase in sublease space is imposing supply pressures.

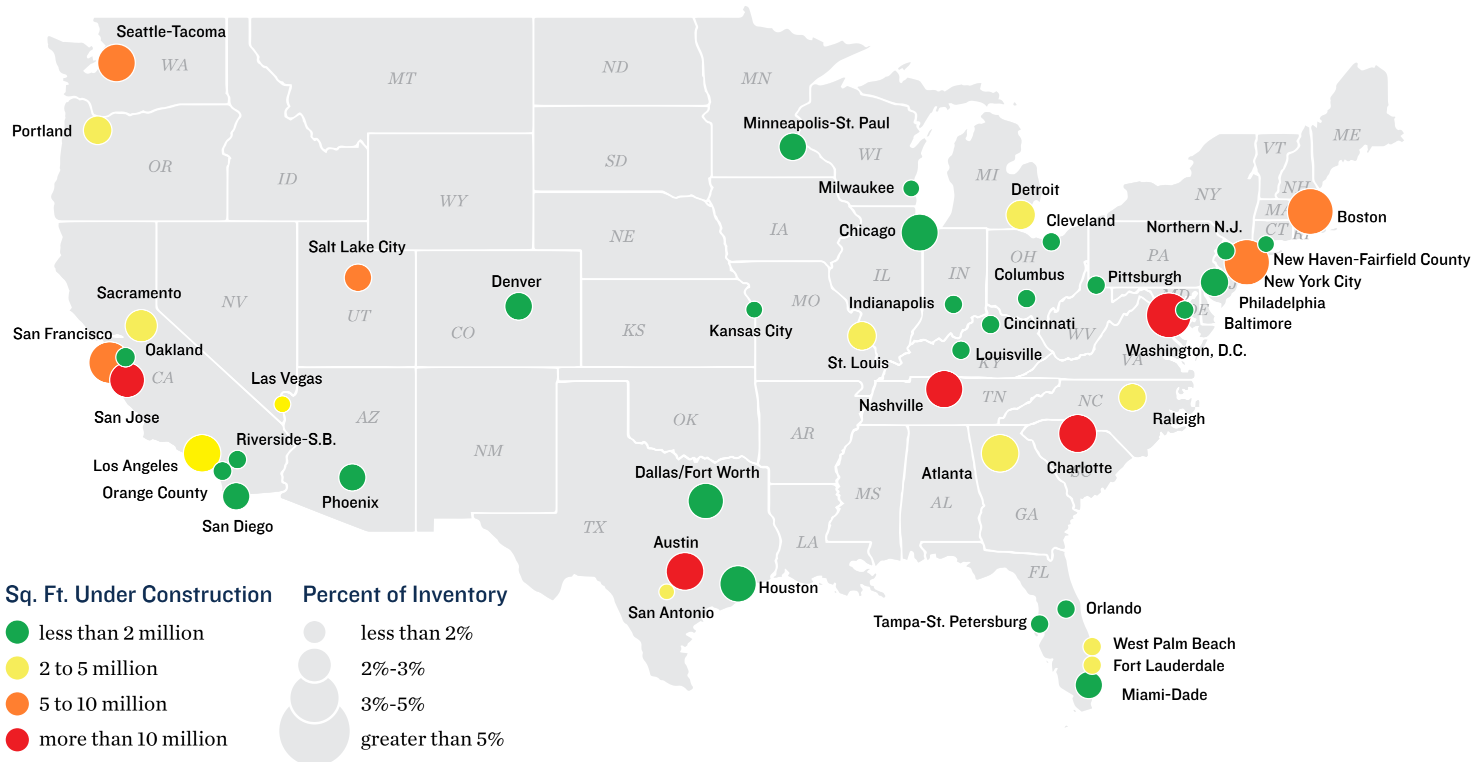
Protracted Recovery

Denver
Detroit
Los Angeles
Milwaukee
New York City
Northern New Jersey
Orange County
Philadelphia
Portland
San Francisco

- The pandemic hit these markets harder, producing significant amounts of negative absorption and resulting in rising vacancy.
- This segment includes the gateway metros of Los Angeles, New York City and San Francisco. Workers vacating office towers and companies offering space for sublease will extend the time for fundamentals to improve.

Office Construction Concentrated in Few Markets

Square Feet Under Construction at Year-End 2020



Markets With Highest Vacancy

Market	% Vacant 2020	Y-O-Y Basis Point Change
Houston	22.4%	200
Dallas/Fort Worth	21.2%	320
Washington, D.C.	18.9%	210
Atlanta	18.2%	320
Chicago	18.0%	260

Markets With Lowest Vacancy

Market	% Vacant 2020	Y-O-Y Basis Point Change
Louisville	7.8%	40
Riverside-San Bernardino	10.3%	160
Raleigh	10.6%	170
Seattle-Tacoma	11.0%	330
Kansas City	11.2%	190

Markets With Highest Absorption

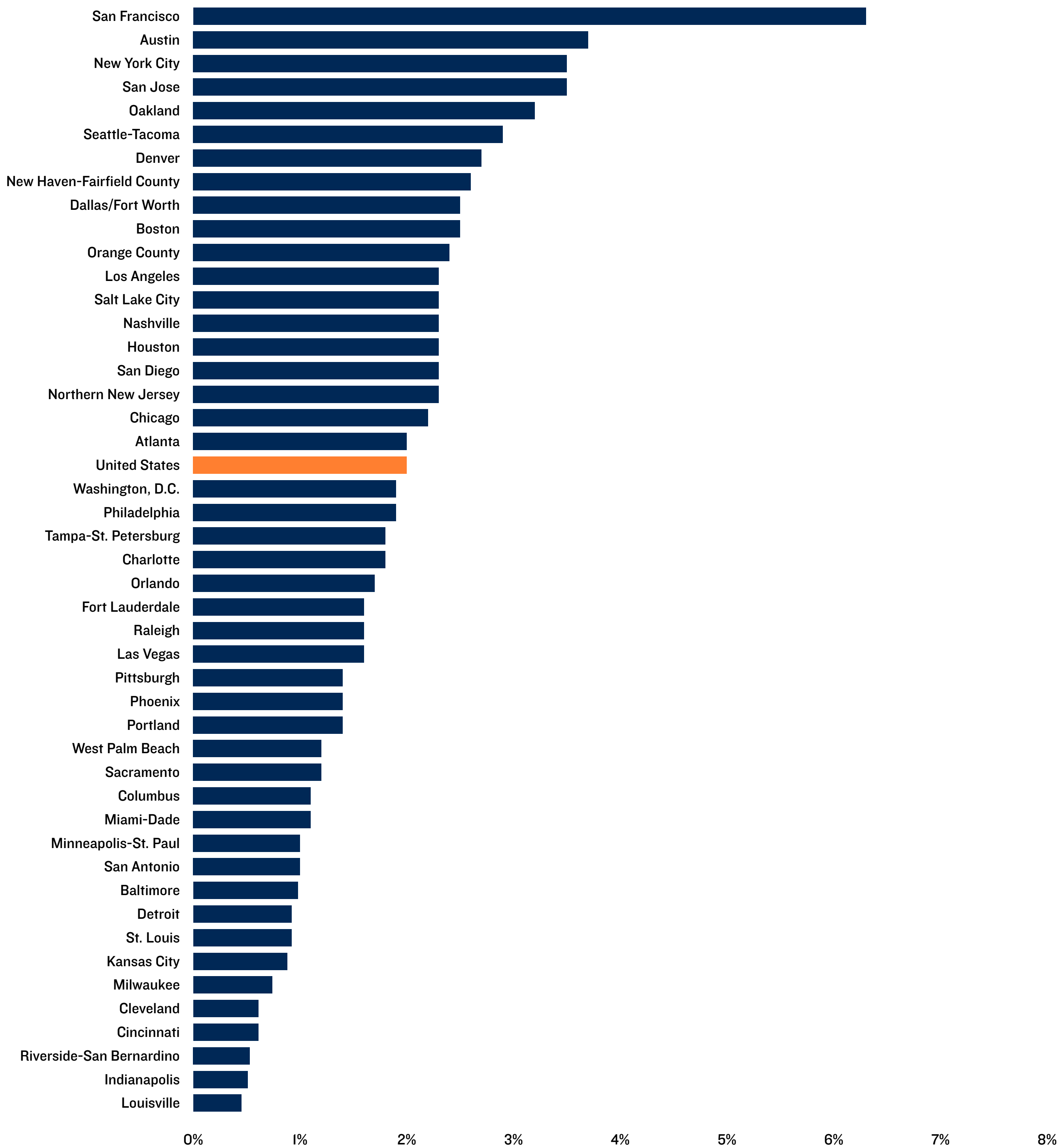
Market	Net Absorption Square Feet	Y-O-Y Change
Raleigh	337,146	-0.9%
Louisville	126,629	-0.8%
Indianapolis	-139,389	-1.2%
Las Vegas	-210,129	-1.3%
Milwaukee	-215,610	-0.8%

Markets With Weakest Absorption

Market	Net Absorption Square Feet	Y-O-Y Change
New York City	-19,093,570	-4.0 %
Los Angeles	-12,329,657	-4.7%
San Francisco	-11,125,035	-6.8%
Dallas/Fort Worth	-8,610,225	-2.0%
Chicago	-8,153,149	-2.7%

Source: CoStar Group, Inc.

Gateway and Tech Markets Lead Nation in Available Sublease Inventory



Available Sublease Space Year-End 2020 (Percent of Total Inventory)

Source: CoStar Group, Inc.

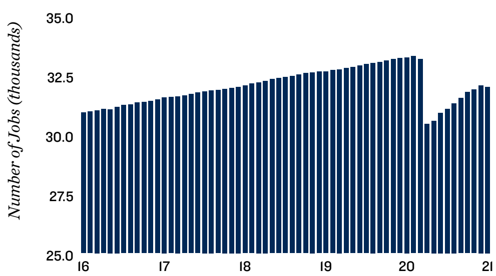
Office Data Summary

Market Name	Office-Using Employment Growth				Completions (000s of Sq. Ft.)				Vacancy	
	2017	2018	2019	2020	2017	2018	2019	2020	2017	2018
Atlanta	3.1%	0.6%	3.1%	-3.9%	3,160	2,510	2,660	3,410	15.5%	15.5%
Austin	5.1%	7.1%	5.5%	5.8%	2,720	3,460	2,370	3,040	11.1%	11.3%
Baltimore	0.3%	1.6%	3.3%	-3.4%	1,170	1,120	640	340	12.5%	12.1%
Boston	1.4%	2.2%	1.1%	-1.4%	3,250	3,650	2,410	1,740	11.4%	10.6%
Charlotte	2.7%	2.6%	2.6%	1.1%	2,260	680	3,070	500	11.7%	10.7%
Chicago	1.2%	0.5%	-0.1%	-3.9%	3,030	3,320	4,840	4,470	16.4%	15.5%
Cincinnati	-0.2%	0.7%	3.5%	-5.0%	640	310	240	90	13.1%	13.5%
Cleveland	1.0%	1.9%	0.1%	-8.3%	340	860	360	240	10.5%	10.2%
Columbus	0.3%	0.8%	-0.8%	-2.1%	1,500	1,100	970	580	10.4%	11.7%
Dallas/Fort Worth	1.9%	3.8%	3.6%	2.8%	10,160	6,380	7,580	3,630	18.4%	18.6%
Denver	2.8%	2.5%	2.5%	1.8%	2,480	3,690	1,440	1,290	14.3%	14.4%
Detroit	0.3%	0.7%	-0.3%	-5.2%	990	720	570	410	14.8%	15.3%
Fort Lauderdale	2.5%	2.2%	0.6%	-4.2%	640	450	440	540	13.0%	12.9%
Houston	2.6%	2.1%	2.6%	-0.3%	4,860	1,880	1,880	2,020	19.9%	20.1%
Indianapolis	2.2%	-0.2%	0.7%	0.7%	900	1,010	490	580	10.9%	11.2%
Kansas City	0.7%	-1.6%	0.1%	-2.6%	1,020	730	830	1,420	10.3%	10.0%
Las Vegas	3.9%	4.3%	2.4%	-8.7%	660	570	270	570	15.3%	14.6%
Los Angeles	1.5%	2.2%	0.5%	-6.6%	2,500	1,950	2,190	1,950	13.8%	13.6%
Louisville	-0.4%	0.2%	3.0%	-5.5%	260	160	400	360	7.9%	7.7%
Miami-Dade	2.3%	1.4%	1.3%	-1.1%	910	1,270	320	910	11.8%	12.1%
Milwaukee	1.3%	-2.5%	-0.7%	-4.4%	1,490	320	670	760	12.3%	11.2%
Minneapolis-St. Paul	0.7%	1.3%	-0.1%	-1.8%	1,310	1,700	1,370	590	10.7%	11.2%
Nashville	4.4%	4.1%	4.3%	1.2%	2,840	1,350	2,310	2,020	10.1%	10.0%
New Haven-Fairfield County	-1.6%	-0.3%	1.5%	-6.8%	140	100	670	290	17.1%	17.4%
New York City	2.4%	2.5%	2.2%	-7.7%	2,680	4,580	11,120	5,260	11.0%	10.6%
Northern New Jersey	1.6%	0.5%	0.1%	-5.2%	670	200	550	450	16.0%	15.2%
Oakland	1.2%	2.0%	0.2%	-3.4%	170	800	1,300	400	11.7%	11.6%
Orange County	1.2%	1.5%	2.6%	-5.2%	2,100	850	1,370	210	13.6%	13.1%
Orlando	4.4%	2.6%	2.7%	-2.6%	630	680	510	1,860	11.1%	10.2%
Philadelphia	1.0%	-0.4%	1.0%	-4.3%	1,290	3,070	1,760	730	13.0%	13.4%
Phoenix	3.4%	4.1%	3.3%	-2.6%	2,250	1,220	3,170	2,160	16.3%	15.9%
Pittsburgh	0.0%	0.8%	1.9%	-2.6%	510	340	630	820	12.1%	11.4%
Portland	1.7%	1.7%	3.2%	-3.2%	610	1,700	140	1,130	9.6%	10.2%
Raleigh	3.1%	3.2%	2.2%	3.1%	2,390	2,070	1,840	2,250	10.5%	9.9%
Riverside-San Bernardino	1.8%	2.0%	2.3%	-2.8%	210	270	260	580	11.0%	9.9%
Sacramento	0.7%	0.9%	1.8%	0.2%	60	260	530	620	12.7%	12.4%
Salt Lake City	3.0%	2.8%	2.7%	-2.1%	2,450	2,470	2,560	3,110	10.5%	8.8%
San Antonio	1.8%	2.9%	1.0%	-2.9%	1,540	760	1,380	780	11.4%	11.3%
San Diego	3.5%	2.2%	2.9%	0.8%	770	650	480	1,230	13.2%	12.9%
San Francisco	4.3%	6.1%	5.3%	-2.1%	880	4,310	3,360	610	9.2%	8.1%
San Jose	3.9%	3.0%	3.4%	-2.6%	8,680	3,140	1,830	1,840	11.9%	11.1%
Seattle-Tacoma	3.1%	3.9%	3.1%	2.3%	3,580	1,750	3,310	4,490	9.4%	7.6%
St. Louis	0.7%	0.1%	-0.1%	-2.4%	930	310	850	520	10.0%	10.7%
Tampa-St. Petersburg	2.9%	3.0%	2.7%	-2.0%	440	550	940	1,020	10.7%	9.9%
Washington, D.C.	1.5%	1.4%	2.9%	-1.9%	4,040	4,260	5,570	3,990	17.5%	17.2%
West Palm Beach	1.7%	1.5%	0.1%	-3.5%	80	70	430	220	14.4%	13.3%
United States	1.7%	2.0%	1.7%	-3.5%	91,710	80,240	88,020	70,640	13.3%	12.9%

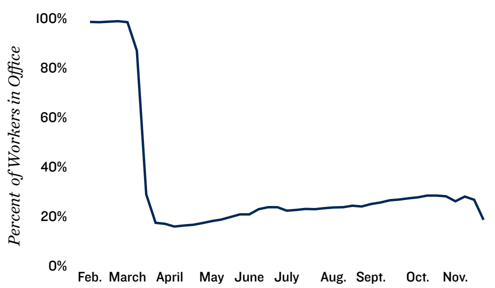
Rate		Asking Rent per Sq. Ft.				Average Price per Sq. Ft.				Market Name
2019	2020	2017	2018	2019	2020	2017	2018	2019	2020	
15.0%	18.2%	$22.55	$23.35	$24.13	$24.54	$162	$185	$196	$215	Atlanta
11.5%	17.0%	$23.80	$25.29	$26.34	$26.33	$296	$321	$349	$365	Austin
11.8%	12.8%	$21.84	$21.76	$21.63	$21.70	$151	$160	$166	$169	Baltimore
11.3%	13.6%	$29.96	$29.27	$30.81	$29.14	$283	$298	$323	$319	Boston
10.7%	12.6%	$23.56	$24.65	$26.22	$27.30	$201	$219	$239	$258	Charlotte
15.4%	18.0%	$21.64	$22.22	$22.30	$22.42	$169	$184	$194	$191	Chicago
13.3%	14.0%	$14.16	$14.43	$14.59	$14.41	$108	$110	$113	$118	Cincinnati
10.9%	11.6%	$15.97	$16.06	$16.04	$16.18	$96	$100	$99	$97	Cleveland
10.5%	12.7%	$14.52	$14.85	$14.90	$14.91	$109	$115	$121	$122	Columbus
18.0%	21.2%	$20.79	$21.16	$21.20	$21.52	$195	$209	$217	$230	Dallas/Fort Worth
14.1%	17.7%	$22.12	$22.93	$23.28	$23.80	$187	$209	$219	$213	Denver
14.8%	16.2%	$17.07	$17.23	$17.56	$18.34	$118	$127	$128	$124	Detroit
13.7%	16.6%	$20.27	$21.29	$21.55	$22.35	$216	$221	$243	$270	Fort Lauderdale
20.4%	22.4%	$20.66	$20.72	$21.19	$21.09	$183	$194	$197	$200	Houston
10.7%	11.4%	$18.23	$19.11	$18.88	$19.10	$129	$136	$145	$145	Indianapolis
9.3%	11.2%	$18.01	$18.65	$19.26	$19.39	$130	$137	$146	$144	Kansas City
13.8%	15.1%	$19.69	$20.33	$21.47	$21.40	$181	$192	$212	$229	Las Vegas
13.2%	16.9%	$34.91	$35.97	$37.78	$37.83	$402	$433	$457	$467	Los Angeles
7.4%	7.8%	$15.89	$16.75	$16.41	$16.40	$138	$145	$146	$141	Louisville
12.4%	14.5%	$31.42	$32.12	$32.91	$34.12	$302	$324	$332	$354	Miami-Dade
13.3%	14.5%	$15.70	$15.56	$15.52	$16.01	$138	$148	$146	$150	Milwaukee
11.0%	12.1%	$15.35	$15.92	$16.24	$16.56	$145	$149	$157	$166	Minneapolis-St. Paul
10.6%	13.7%	$24.38	$24.99	$26.00	$26.27	$225	$249	$275	$283	Nashville
17.2%	17.8%	$26.83	$24.61	$25.08	$26.69	$199	$216	$225	$228	New Haven-Fairfield County
11.2%	14.7%	$59.20	$58.35	$60.16	$59.93	$605	$608	$602	$576	New York City
14.9%	17.1%	$24.49	$25.08	$25.31	$25.56	$192	$199	$210	$204	Northern New Jersey
12.1%	14.2%	$35.91	$38.16	$38.91	$39.06	$313	$333	$355	$365	Oakland
12.7%	15.9%	$28.31	$29.45	$29.91	$29.32	$289	$309	$321	$340	Orange County
9.6%	12.3%	$20.01	$20.83	$21.29	$21.77	$185	$198	$202	$211	Orlando
12.8%	14.8%	$21.98	$22.34	$22.85	$23.05	$163	$171	$181	$183	Philadelphia
14.7%	17.6%	$22.64	$23.07	$24.01	$24.69	$183	$204	$213	$234	Phoenix
11.6%	13.4%	$21.34	$20.97	$21.15	$21.29	$140	$143	$145	$148	Pittsburgh
9.9%	13.6%	$24.38	$25.25	$25.08	$24.86	$251	$264	$285	$283	Portland
8.9%	10.6%	$22.71	$24.13	$24.73	$25.25	$172	$197	$221	$243	Raleigh
8.7%	10.3%	$20.02	$20.14	$21.17	$21.88	$186	$194	$212	$235	Riverside-San Bernardino
11.2%	13.5%	$21.92	$22.88	$23.42	$24.07	$185	$192	$199	$208	Sacramento
8.7%	12.4%	$20.22	$20.66	$21.20	$21.43	$167	$176	$181	$191	Salt Lake City
11.5%	13.6%	$19.65	$20.25	$21.00	$21.13	$177	$193	$207	$228	San Antonio
12.6%	15.7%	$30.26	$30.54	$31.65	$32.18	$298	$312	$320	$336	San Diego
8.8%	15.7%	$57.05	$61.75	$66.14	$59.91	$539	$582	$630	$681	San Francisco
9.4%	12.8%	$46.59	$48.81	$50.03	$49.16	$453	$528	$568	$588	San Jose
7.7%	11.0%	$29.39	$29.89	$32.41	$30.96	$327	$345	$375	$414	Seattle-Tacoma
10.1%	11.4%	$17.92	$18.61	$18.75	$19.24	$126	$129	$129	$131	St. Louis
10.4%	12.2%	$20.80	$21.63	$22.25	$22.56	$173	$180	$190	$193	Tampa-St. Petersburg
16.8%	18.9%	$35.87	$36.54	$36.79	$36.87	$291	$305	$315	$334	Washington, D.C.
13.6%	14.4%	$21.64	$22.38	$23.59	$24.50	$252	$266	$291	$280	West Palm Beach
12.8%	15.2%	$27.29	$27.78	$28.55	$28.52	$241	$257	$276	$283	United States

Sources: BLS; CoStar Group, Inc.; Real Capital Analytics

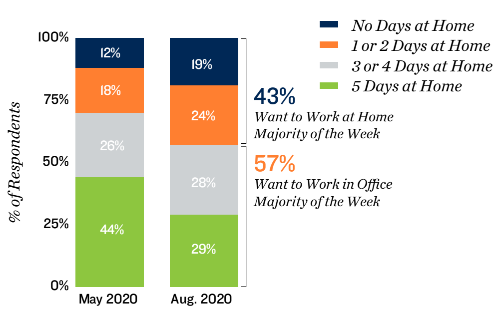
Office-Using Jobs Returning



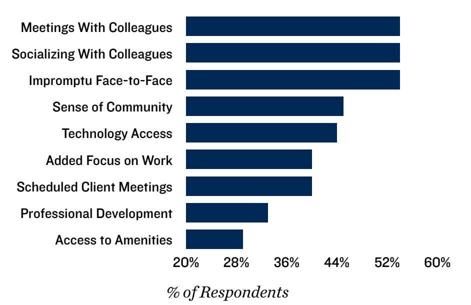
Return to Office Slows After Steady Climb



Workers Value Benefits of Offices



Employees' Reasons to Return to the Office



** Through January 2021*

Sources: BLS; Gensler; Kastle Systems

Uncertainty Will Remain in Office Sector Until Firms Can Gauge Long-Term Space Requirements

Office-using jobs are returning. During the March and April 2020 lockdown, nearly 2.9 million positions in traditional office-using segments were eliminated, a 9 percent reduction from the pre-coronavirus level in February. Through December, more than half of these positions had returned; however, not all parts of the nation are faring equally. Double-digit losses were posted during the first two months of the pandemic in metros including Los Angeles, Las Vegas, Detroit and Cleveland, while cities with large tech or government sectors such as Austin, Denver, Washington, D.C., and Salt Lake City were able to stem sizable job cuts as a number of office employees were able to work remotely.

Office demand beyond the pandemic to take multiple forms. Since firms sent employees to work at home, many are evaluating how they intend to use office space in the future and will be reassessing floor-plate requirements beyond COVID-19. In a recent study, many employees indicated a preference for being in an office at least part of the time but preferred the flexibility to work remotely some days. Before staffs return to offices, open layouts may need to be made less dense or altered with barriers between workers to adhere to physical-distancing protocols. Individual space may shrink and be shared as employees work from home more often, while collaborative and communal space may be expanded to ensure physical distancing. Cubicles may need to be altered to accommodate the rise in videoconferencing as more workers remain local instead of traveling to meet with clients. Office needs will depend on the industry and the type of work being done. What benefits one firm will not work the same way for another. Companies that are task oriented or conduct business primarily by telephone such as call centers may decide to permanently give up space, while creative, sales, client-oriented or service-based firms may keep or look to expand space requirements.

Available subleases will proliferate throughout 2021. The current demand for office space varies greatly among business sectors and job requirements. Remote working is being successfully achieved by many employees across a wide swath of companies including tech firms. Companies with a task-oriented labor force that can easily work from home are considering downsizing offices, especially those that sustained revenue declines. In contrast, positions requiring more collaboration will find it beneficial to work in offices. These firms may shift from smaller square footage per employee to larger collaborative spaces with open, flexible layouts that can be reconfigured to accommodate physical distancing so employees can safely return to the office. Companies in other segments such as back-office operators have found that they can permanently shift staff to work remotely, or to areas with more affordable rent, saving costs as leases come up for renewal. Businesses downsizing space needs raised the total sublease space available by 43 percent year over year in the fourth quarter. The surge in floor plates available for sublease will likely put downward pressure on rent in 2021 as lower rates are often offered to attract users. Companies with lease expirations looming and a lack of clarity on space needs may find a shorter-term solution in a sublease. Subleases can also give firms the ability to move into a more prominent space or building, at potentially lower rates, which may generate demand in Class A buildings and leave older, lower-quality space available well beyond the pandemic.

Suburbs Gaining Momentum, Benefiting Garden-Style Office Buildings

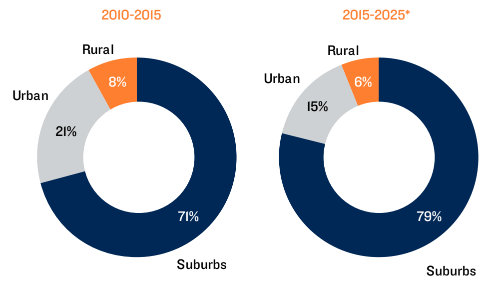
Changing demand drivers shift focus to suburbs, less-dense cities. As the coronavirus spread during 2020, the lower density of the suburbs and smaller metros appealed to businesses and residents seeking to avoid heavily populated areas, public transit and small enclosed spaces, including elevators. Many employees sent home to work found the space available to them lacking and began to search for larger, affordable residences with room to work and school their children from home. These factors led more people to residences in the suburbs, accelerating a trend that had already begun as the millennial cohort aged into their 30s and began to marry and start families. Companies wanting to be closer to where their employees live are reassessing space needs with some firms establishing satellite accommodations outside the main office in the central part of the city to foster collaboration and maintain the company culture.

Hub-and-spoke model benefits suburbs. As companies reevaluate space requirements, some are opting to downsize their higher-cost offices in the urban core and lease smaller spaces in suburban areas closer to employees in a hub-and-spoke-style arrangement. In some instances, sublease or coworking space is sought for its immediate occupancy, shorter lease terms and lower capital expenditures. This system cuts down on commute times while allowing staff to interact with colleagues in a nearby location when collaboration is necessary. Firms can also maintain their corporate culture and assist employees in finding a work-life balance, which may attract new workers. Not every industry or metro will fare equally in this type of system. Cities with high housing prices in the core and business sectors in which remote working is easier to achieve will benefit the most.

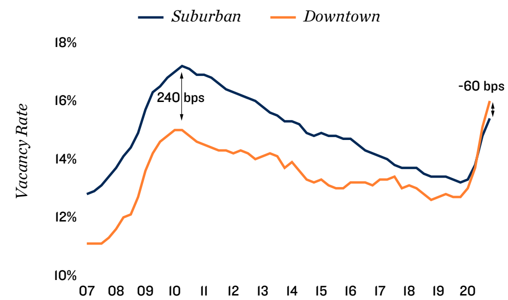
Low-slung, non-elevator buildings with ample parking are desired. Hesitancy from many workers to use public transit or gather in small, enclosed spaces in densely populated areas is drawing companies out of towers in the urban cores. Garden-style buildings with offices that can be accessed directly from the outdoors by open stairwells instead of an elevator are being favored during the pandemic. These properties are typically located in suburban areas and provide ample free parking. Buildings offering lower rents, providing a cost savings beyond the pandemic, are attractive to firms with diminished revenues this year. The trend of companies moving to the suburbs was already underway due to changing demographics but sped up during the pandemic.

Investors favoring suburban assets. Investment in the suburbs has outpaced that of the urban core during the past five years and through the first three quarters of 2020 accounted for 77 percent of total dollar volume of assets $2.5 million and greater, the highest percentage since 2009. This dynamic is due in part to a larger inventory of suburban assets, more suburban medical offices trading, and fewer high-priced towers in the core changing hands. Through the end of 2020, the average price of suburban properties was 33 percent lower than downtown buildings. Suburban buildings typically offer investors the potential for lower price points and higher yields. Lower-slung assets along main transit arteries, in amenitized neighborhoods and with essential tenants will be highly desired. Well-located older assets with renovation potential are likely to provide value-add opportunities as firms hit hard by the pandemic seek lower-cost office space.

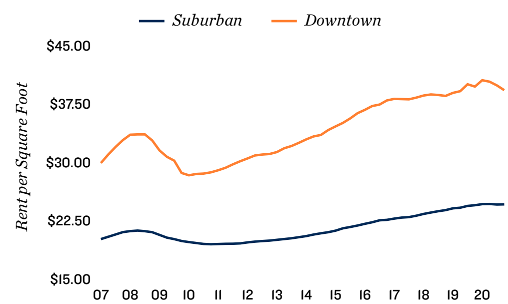
Household Growth Shifts to Suburbs



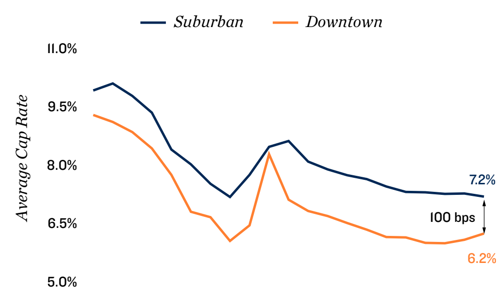
Vacancy in Core Rises Above Suburbs



Lower Rent Available in Suburbs



Suburban Properties Offer Higher Returns



** Forecast*

Sources: CoStar Group, Inc.; John Burns Real Estate Consulting; Real Capital Analytics

Strong Growth Among Necessity-Based Users Produces Medical Office Dichotomy

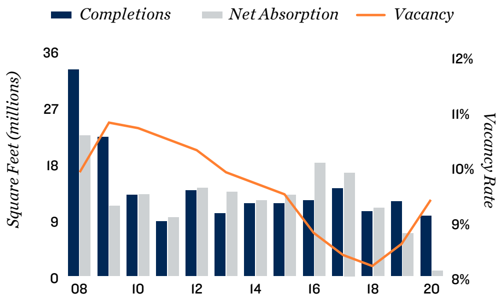
Changes are needed to accommodate increased safety protocols. While necessity-based medical facilities including dialysis and urgent care centers remained open during the pandemic, many other medical office tenants were shuttered while stay-at-home orders were in effect, postponing or delaying appointments. This resulted in many medical providers reducing hours and restricting patient loads to ensure safe physical distancing and sanitation, cutting into revenues. At the trough in April, personal consumption expenditures on health services (excluding pharmaceuticals) were down 32 percent on an annualized basis. In the spring, almost 2.3 million healthcare and social assistance positions were cut during the lockdown as medical providers closed and many elective procedures were delayed. As of January 2021, healthcare employment remained roughly 898,800 positions below the pre-pandemic level.

Decline in leasing softens fundamentals. Developers had more than 10 million-square-feet of medical offices under construction in the nation's major metros at the end of 2020 with completion dates into 2023. More than half of the underway inventory is due in 2021, although some projects could be delayed, providing the lowest delivery pace in more than 10 years. Reduced deliveries in 2020 still outpaced net absorption, raising vacancy to 9.4 percent, a year-over-year jump of 80 basis points and the highest rate since 2015. Leasing activity will likely recover relatively quickly once patients feel comfortable returning to medical providers for checkups and elective procedures. Competition for tenants may come from alternative buildings such as shopping centers being used for medical practices. Although vacancy ticked up, the asking rent rose 2.3 percent year over year to $21.43 per square foot on average at year end, setting a 12-year high and keeping investors active. Buyers have focused on buildings with necessity-based medical and lab tenants.

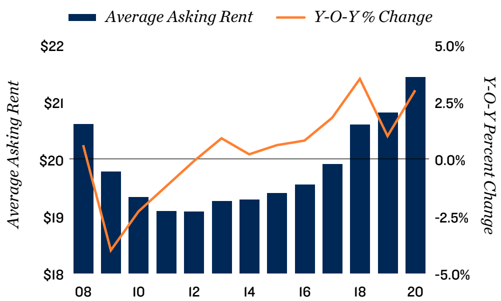
Telemedicine gains traction during pandemic. Greater use of telemedicine may change the needs of medical office space in the future. Although the use of telemedicine had been on the upswing in recent years, the coronavirus accelerated the adoption as more health insurers covered the cost to keep patients at home. Post-COVID-19, a rise in use of video consultations could allow for an increase in patient load and may require altering medical offices to accommodate virtual appointments. Looking forward, demographic trends favor increased demand for medical office space as the last of the baby boom generation ages into retirement. Between 2020 and 2025, the population age 65 and older is expected to jump 17 percent. These tools will be more useful as people age and their mobility becomes more limited.

Pandemic has highlighted need for medical lab space. The search and increased funding for vaccines and therapeutics to combat COVID-19 has generated the need for lab space by biotech, medical-device makers, and pharmaceutical companies. The coronavirus has also focused attention on the need to onshore the supply chain used to produce medical and life science goods. Innovations in artificial intelligence, gene and cell therapies, as well as an aging population that will use more of the products generated by these firms, should keep demand for lab space elevated in the years ahead. The rise in demand should benefit metros with large life science clusters, including Boston, San Diego, Raleigh and San Francisco, as well as expanding hubs in Philadelphia and Baltimore.

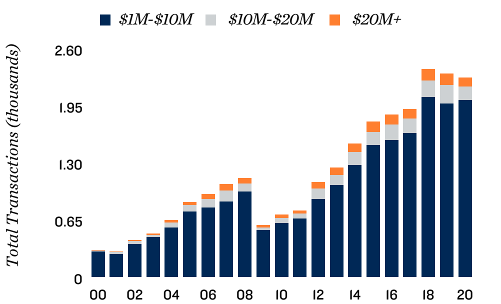
Absorption Slows, Pushing Vacancy Up



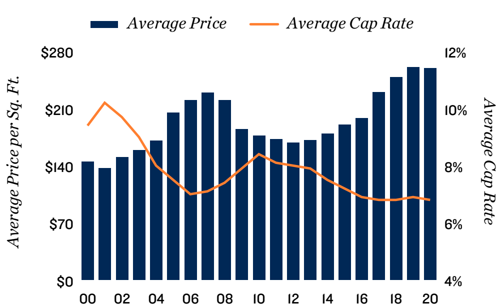
Rent Reaches New High



Transaction Activity Wanes



Price Dips From 20-Year Peak



Sources: CoStar Group, Inc.; Real Capital Analytics

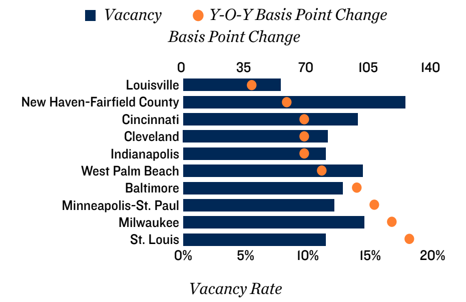
Smaller Midwest Markets Outperform Gateway Metros During Pandemic; South Dominates Rent Growth

Gateway metros face long road to recovery. As the pandemic took hold, office towers in major urban population centers cleared out as staff began working from home. Markets with highly utilized public transportation systems including New York City, San Francisco and Chicago registered the largest decline in office users as personnel stayed away from high-density enclosed spaces. These cities will face the most difficult recovery as their very nature tends to be contrary to physical distancing, causing many employees to prefer working from home. Buildings featuring updated HVAC systems and touch-free surfaces will be favored as society re-adapts to working from the office once vaccines are widespread, and they will likely generate additional tenant interest as businesses reopen offices. These properties, however, will confront competition from a surge in subleased space becoming available that may provide companies seeking marquee space with a more prestigious floor plate at a discounted rate. San Francisco, Austin, San Jose, Oakland and New York City lead the nation, with all having more than 3 percent of total inventory available for sublease.

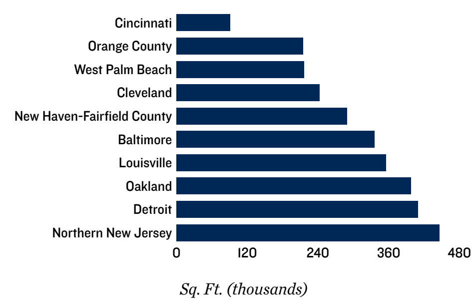
Lower cost of living benefits smaller metros. Employees able to work from anywhere are choosing to relocate to less-expensive quarters outside the urban cores. More affordable rents and home prices are drawing many of these workers to the suburbs and secondary/tertiary cities. Metros where year-end 2020 office-using employment had risen above the pre-COVID-19 level include tech powers Austin, Seattle-Tacoma and Raleigh. Employment in these cities should do well in 2021 as many tech firms continue to expand. A number of Midwest markets are also outperforming as firms seek to lower costs. Louisville, Indianapolis, Cleveland and Kansas City were among metros registering the lowest vacancy increases year over year in 2020. Cities in the nation's midsection also rank among those having the least amount of construction underway and sublease space available, which should help to steady the fluctuation in the vacancy rate during the year ahead. Beyond the pandemic, lower rents in these markets should continue to lure expanding office users.

Sunbelt markets record largest rent gains. Southern metros are prominent in the list of major U.S. metros with the highest annual asking rent growth last year. West Palm Beach, Charlotte, Fort Lauderdale and Miami-Dade each posted increases of more than 3.5 percent. These metros offer lower rates than larger Northeast markets, luring more financial and tech firms to increase operations in Southern markets. Riverside-San Bernardino, Sacramento and Phoenix also ranked in the top 10 nationwide. Phoenix in particular has been successful in drawing new companies to the Southwest. The largest rent jump of 6.4 percent was recorded in New Haven-Fairfield County. The metro registered one of the smallest vacancy increases during the same period but still has one of the nation's highest office vacancy rates.

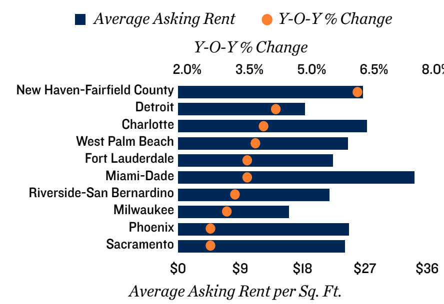
Smallest Vacancy Rise



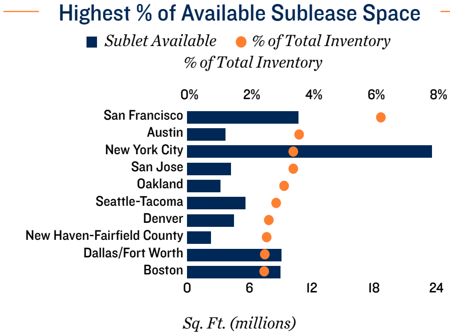
Lowest Level of Deliveries



Largest Rent Growth



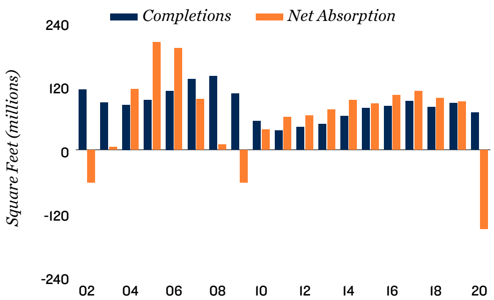
Highest % of Available Sublease Space



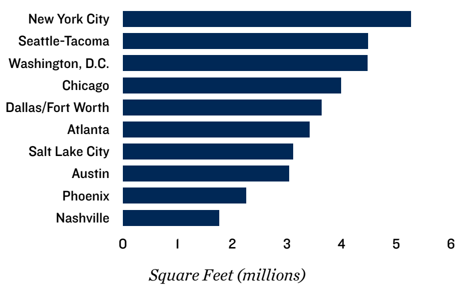
Source: CoStar Group, Inc.

Companies Reevaluating Space Requirements, Generating Shifts in Office Fundamentals

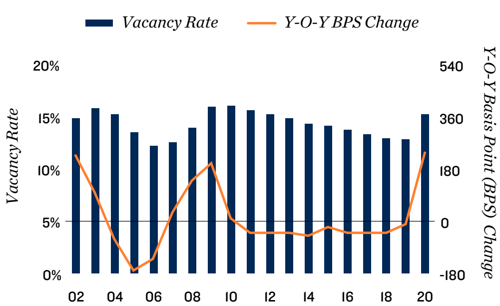
Absorption Tumbles as Space Needs Reassessed



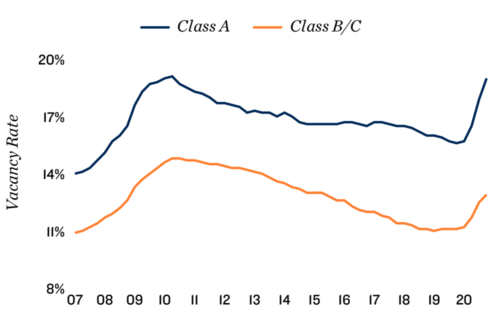
Largest Inventory Gains in 2020



Uncertainty Challenges Demand



Class B/C Office Less Challenged



Source: CoStar Group, Inc.

Construction projects begun before the health crisis are delivering. Office developments started in a significantly different economic climate were completed in 2020, raising new inventory by 70.6 million square feet, slightly above the 10-year average margin. Finalizations were concentrated in five larger metros, which accounted for nearly 22 million square feet. Chicago, Dallas/Fort Worth, New York City, Seattle-Tacoma and Washington, D.C., each received more than 3.6 million square feet. Looking ahead, a lack of clarity on space decisions by a number of companies has delayed construction on some projects underway, pushing openings later into 2021. In addition, the groundbreakings on more planned projects have been delayed or canceled, which will likely slow deliveries in the years ahead.

Technology companies continue to add office space. Tech firms in particular have been in expansion mode during the pandemic even though many of their staffs are working remotely. Amazon added 2 million square feet to its campus in Seattle-Tacoma and signed leases for additional buildings underway in nearby Bellevue. The company has another 2.1 million square feet under construction at its HQ2 in the Washington, D.C., metro, that are expected to be completed in 2023. In Tennessee, the firm will occupy 3.2 million square feet in the Nashville Yards development and another 500,000 square feet is set to open in Boston during 2021. Nearby in Cambridge, Google is due to move into a 420,000-square-foot building in 2022. The company also has 1.7 million square feet expected to deliver during 2021 in Mountain View, California. Microsoft is set to expand into roughly 500,000 square feet in Atlanta, while Facebook and Apple have penned multiple new leases.

Vacancy heads higher as leasing decisions are delayed. The office vacancy rate for the U.S. held between the mid-12 percent to the low-13 percent zone over the past six years. The pandemic, however, slowed leasing activity beginning in the first quarter of 2020 as many companies paused to reassess the impact of the pandemic on their future space requirements. Some firms have vacated floor plates or put expansion plans on hold, while new projects continue to come online. As a result, net absorption fell out of positive territory in the second quarter of 2020. The vacancy rate change was especially pronounced in Class A inventory, having jumped 340 basis points during 2020 to 18.9 percent, the highest rate since 2010. In comparison, the Class B/C rate climbed 180 basis points to 12.8 percent, a rate last surpassed in 2015. Some operators of buildings with rising vacancy are being more flexible on lease terms to fill space and allowing companies to renew leases on a short-term basis until they have more certainty on their long-term space needs. As a result, roughly 27 percent of office leases are due to expire in 2021 and another 24 percent in 2022. Looking forward, vaccines will provide tenants with additional clarity on office needs as the year progresses and many firms are likely to implement a hybrid of remote and in-office schedules, limiting the amount of vacated space. In the meantime, companies with business picking up during the pandemic, including many tech and financial organizations, will drive leasing activity during 2021.

Rising Vacancy, Increased Subleasing Activity Suppress Outlook on Rental Rates

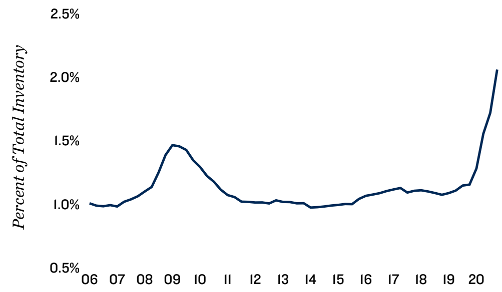
Sublease availability surges. New buildings coming online with unleased floor plates will face additional competition from an influx of subleased space being marketed. A number of firms that have successfully moved to working remotely are not re-leasing some or all office inventory and those without leases expiring are trying to sublease their floor plans. As a result, space available for sublease soared to the highest level in more than 15 years during 2020. The increase in competing floor plates will likely keep vacancy on an upward trajectory in 2021 and suppress rent gains in some submarkets. Lower rates for sublease space will likely attract firms seeking to move into higher-quality offices at a reduced price point, benefiting inventory in Class A buildings. Markets with large tech workforces, including San Francisco, San Jose, Austin and Seattle-Tacoma, dominate the list of U.S. metros with available sublease space.

Absorption tumbles. Companies giving back space contributed to a surge in vacant stock, sending net absorption into negative territory for the first time since the Great Recession. Occupied stock dropped by 149.1 million square feet last year, more than double the reduction of 61 million square feet recorded in 2009. The decline in occupied inventory was widespread. Major markets with an active delivery pipeline, including Dallas/Fort Worth, Houston, Washington, D.C., and Atlanta, registered weak absorption during 2020, pushing vacancy in these metros up more than 200 basis points annually to more than 18 percent. Only two major metros in the nation, Raleigh and Louisville, posted positive net absorption. Both benefited from limited supply of new inventory.

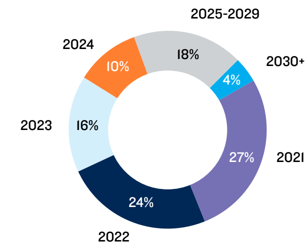
Pandemic weighs on rent gains. Rent growth slowed after reaching a nationwide peak of $28.91 per square foot during the first quarter of 2020 due to a rise in vacancy and a jump in sublease space being marketed. Between March and December of last year, the average asking rent receded to $28.52 per square foot, a 1.3 percent decline. On an annual basis, however, the rate dipped only slightly. Metros with above-average rent improvement year over year in 2020 include the smaller markets of New Haven-Fairfield County, West Palm Beach and Charlotte. Nationwide, leasing demand will be soft until workers are back in offices and uncertainties brought about by the coronavirus are sorted through, weighing on rent advances well into 2021. Rates are also facing stiff competition from the surge in sublease space that is typically offered at a lower price point, posing a challenge to operators trying to maintain rents as vacancy trends higher. In addition, companies leveraging an uptick in vacancy as an opportunity to move into more desirable space are leaving lower-rent floor plates available, putting further downward pressure on asking rent.

Rent growth eases among office classes. So far, long-term lease commitments are assisting in slowing the rate of office rent decline among classes. Since reaching a peak of $35.55 per square foot in March of 2020, Class A rent has declined 1.4 percent through the end of last year. The rate was up 0.3 percent annually but well below the prior year's 2.8 percent jump. Class B/C rent has followed a similar path, rising to a new high of $24.47 per square foot in the first quarter of 2020, but it slipped 1.5 percent to $24.11 per square foot by the end of December. On an annual basis, the rate decreased 0.7 percent, after a 2.4 percent climb 12 months earlier.

Available Sublease Space Soars

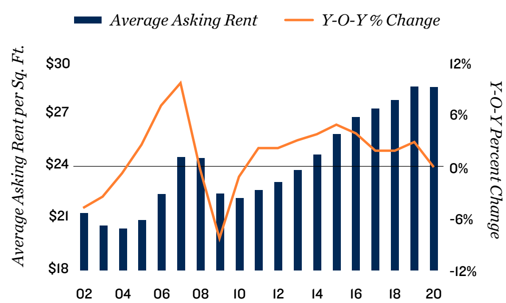


Lease Expirations by Year: 2021 Favored

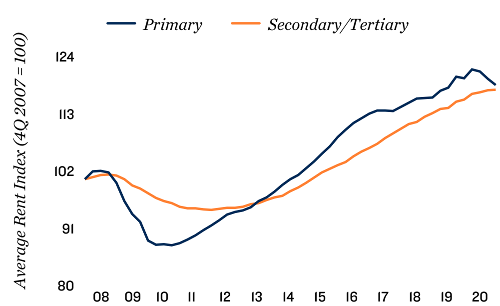


*Percent of Office Leases**

Asking Rent Growth Slows



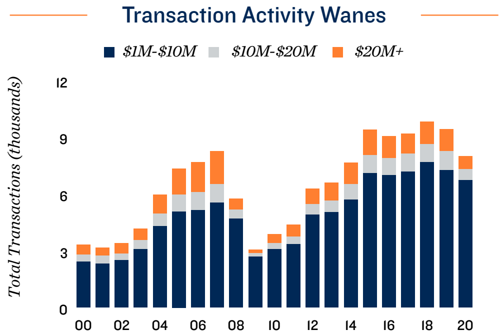
Office Rent Index

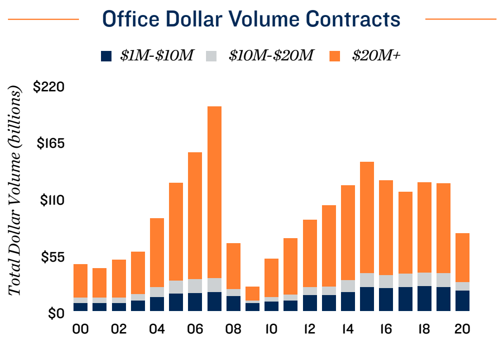


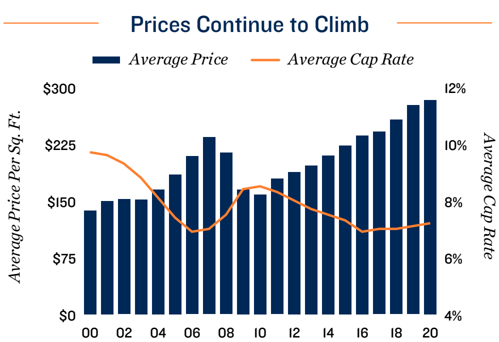
* *Not including leases with unknown expiration dates.*

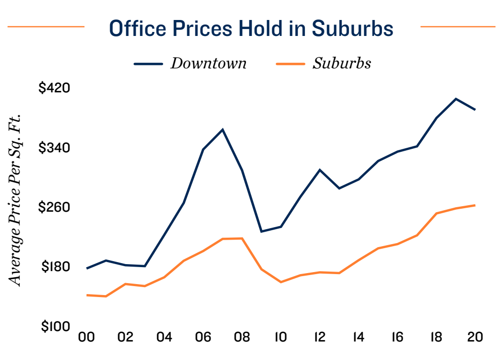
Source: CoStar Group, Inc.

Deal Flow Keeps Moving Despite Cloudy Long-Range Outlook; Flight to Safety Pushes Prices Higher









Sources: CoStar Group, Inc.; Real Capital Analytics

Office transactions picked up after slow spring. Stay-at-home orders and a decline in foreign investment cut purchasing during the second quarter of last year, contributing to trading activity and dollar volume retreating to their lowest levels in more than five years in 2020. Year over year in March trading decreased roughly 40 percent. The largest decline was in the $20 million-plus price tranche as many institutional investors and REITs stepped to the sidelines to wait for more clarity. Fewer transactions by private investors also cut deal flow in the $1 million to $10 million span by roughly 33 percent, lowering dollar volume by 41 percent over the same period. Despite the slow transaction velocity in the spring, purchasing activity picked up in the second half of the year as shelter-in-place orders were lifted. Transactions and dollar volume in all office classes and price tranches jumped from March to December. Class B/C buildings with valuations between $1 million and $10 million drove deal flow.

Primary markets favored. During the second half of 2020, primary markets recorded the largest percentage increase in sales activity. The volume of trading in the $20 million-plus segment surged the most among price tranches as prime assets were sought. During the fourth quarter, rising primary metro vacancy contributed to the average cap rate in these settings shifting up 10 basis points to 6.6 percent. Investors favored buildings in Dallas/Fort Worth, Houston and Los Angeles as capital continued to move to the south. These three markets accounted for roughly 10 percent of the all transactions during 2020. Among secondary markets, assets in Phoenix, Philadelphia, Denver and Austin most often changed hands. Nationwide, the average cap rate in secondary markets held steady year over year at 7.3 percent, while the rate in tertiary metros rose 10 basis points to 7.8 percent. Tertiary metros targeted by investors during 2020 were growing tech hubs including Raleigh and Indianapolis.

Demand for prime assets keeps prices rising. The average price nationwide rose 1 percent in the second half of 2020 to $283 per square foot and up 3 percent annually as buyers shifted focus to medical office, life science or quality assets in prime office markets. Increased interest in premium buildings outside the urban core pushed the average price for suburban assets up 2 percent in 2020 to nearly $260 per square foot. During the same span, the average price of downtown buildings dipped slightly to an average of nearly $388 per square foot as fewer trophy towers transacted. The added risk profile of urban assets led to the average cap rate for office assets nationwide rising 10 basis points in the fourth quarter, but the rate is still holding in the low-7 percent bracket. Financing remains available with nearly half of transactions being funded by local, regional and national banks.

Some metros face acute pricing challenges. Not all markets fared as well across the country last year. Vacant office towers in New York City contributed to a price drop of over 4 percent in 2020. Other metros with price pressure include Northern New Jersey and West Palm Beach. In comparison, strong buyer demand amid relatively tight vacancy contributed to double-digit price gains in Riverside-San Bernardino and Seattle-Tacoma. The former metro is bolstered by some relocations out of nearby larger cities, while the sizable technology presence in Seattle-Tacoma is seen as a long-term stabilizer.

Buyers Follow Tenants, Employees to Suburbs; Properties That Held Up During Pandemic Targeted

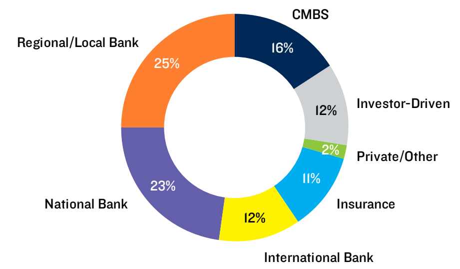
Suburban office assets gaining favor. Tenant trepidation in addition to higher price points in city cores have more investors willing to expand their search boundaries. More buyers are considering suburban assets, especially in neighborhoods near major transit arteries and urbanized amenities. Buyers are willing to pay for high credit tenants with long-term leases. Net lease assets and properties with a roster of tenants in critical or expanding industries are receiving increased attention. Buildings equipped with updated features that enable tenants to return to offices and amenities that allow for physical distancing are also desired. During the year ahead, many suburban submarkets are expected to outperform urban areas due to heightened leasing demand, a slower pace of construction, and favorable demographic trends.

Downtown assets should not be dismissed. Barriers to entry, access to talent, and a wide variety of amenities make core assets attractive, especially once workers return to offices. In the short term, however, the delivery of towers started before the pandemic will increase competition for tenants, likely delaying downtown rent growth in many markets. These new properties, especially those with post-coronavirus amenities, will likely draw REIT and institutional capital. Buyers seeking value-add plays may focus on well-located assets in urban centers with high vacancy that can be readily updated to enhance physical distancing and attract additional tenants once immunizations are widespread.

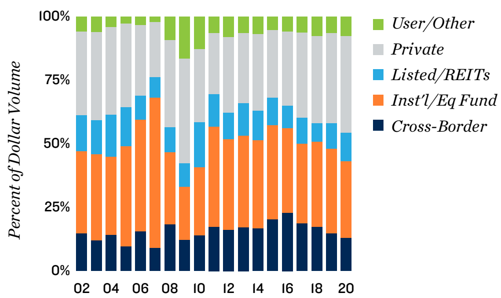
Investors fix eyes on office assets that thrived during the coronavirus. Many buyers in a move to safety are seeking properties that held up through the pandemic and have a positive long-term outlook. The need for flu shots, COVID-19 tests and vaccines, as well as an aging population, are generating buyer interest in medical office and lab space. Net lease assets or buildings backed by a hospital system in particular are receiving attention. Tenants at these facilities, including urgent care, dialysis centers and lab users, that remained open during the shutdown have also received greater investor demand. After pausing during the spring and summer of 2020, foreign investors have begun to return, many targeting life sciences buildings, boosting interest in metros with a large biotech sector including Raleigh, Boston and Philadelphia. Buyers seeking lower entry costs and higher yields may focus on assets in smaller but growing hubs such as Salt Lake City and Indianapolis. The competition for medical office and lab properties has tightened the supply of listed investment-grade assets, contributing to higher pricing.

Uncertainty will restrain deal flow. Looking ahead to this year investors will remain cautious, scrutinizing the credit worthiness of tenants and lease terms. Many buyers will focus on buildings in desirable growing markets that are well leased to essential tenants with long terms. Some companies in need of recapitalization or to improve balance sheets may be willing to negotiate a sale-leaseback opportunity, providing some additional buying options. While interest rates are historically low, some buyers may nevertheless wait on the sidelines for the desired transaction given current ambiguities with the property type. Even with vaccines on the way, it will take some time for widespread inoculations to make employees feel safe enough to use public transportation and return to offices in large numbers. These factors will delay clarity on the long-term outlook of many office assets, especially in metro cores.

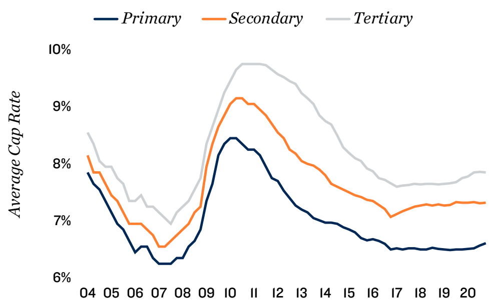
Banks Drive Lending Activity in 2020



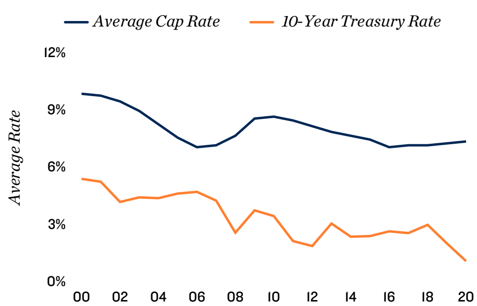
Private Buyers Lead Dollar Volume



Cap Rates Hold in Primary Markets



Cap Rate vs. Treasury Gap Widens



Sources: CoStar Group, Inc.; Federal Reserve; Real Capital Analytics

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