CBRE

MARKETVIEW

## Midtown South Manhattan Office, Q2 2017

# Leasing activity dips to 2013 level

| Leasing Activity | Net Absorption | Availability Rate | Vacancy Rate | Average Asking Rent |
|---|---|---|---|---|
| ▼ 1.01 MSF | ▲ 0.20 MSF | ▼ 10.7% | ▲ 6.6% | ▼ $71.90 PSF |

*Arrows indicate change from previous quarter.

- A dearth of large deals caused leasing activity to drop well below historical averages in Q2 2017, to 1.01 million sq. ft.
- Despite slow year-to-date leasing, activity in the 10,000–25,000-sq.-ft. segment is outperforming its five-year quarterly average.
- Rents declined 3% quarter-over-quarter to $71.90 per sq. ft., due to the removal of premium-priced space in new construction in Chelsea.
- Availability declined to 10.7%, although it stands at 230 basis points (bps) above its Q2 2016 level.
- Leasing across industries was more varied than in the recent past, with insurance accounting for 23% of leasing activity and apparel/retail sales making up 28%. Tech, typically Midtown South's major driver of leasing, accounted for 14% of all activity.

### MARKET OVERVIEW

Midtown South has been relatively quiet compared to the constant flow of leasing witnessed from 2013 to 2015. The below-average leasing is a result of the dearth of large, quality space options available to tenants. While leasing activity in Midtown and Downtown has been bolstered by transactions larger than 100,000 sq. ft., Midtown South has seen only one transaction of this size during the quarter. Absorption was only slightly negative in Q2 2017, which kept the availability rate relatively stable quarter-over-quarter. Average asking rents also remained stable, since the market has not seen any fundamental changes to demand or supply during Q2 2017.

Figure 1: Top Lease Transactions

| Size (Sq. Ft.) | Tenant | Address |
|---|---|---|
| 145,741 | Aetna, Inc. | 61 Ninth Avenue |
| 86,524 | MAC Cosmetics | 233 Spring Street |
| 63,278 (R) | Sequential Brands | 601 West 26th Street |
| 61,611 | Harry's Razor Company | 1 Hudson Square |
| 52,000 (E) | Capital One | 11 West 19th Street |

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

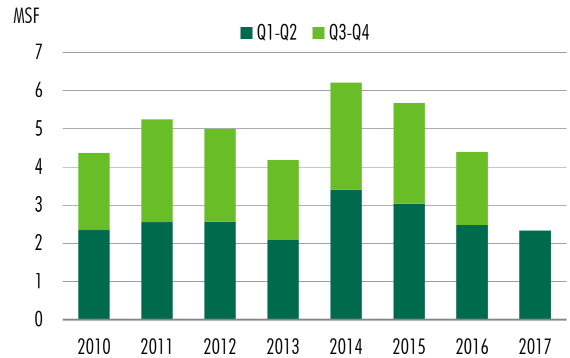
Source: CBRE Research, Q2 2017.

## LEASING ACTIVITY

Leasing activity in Q2 2017 totaled 1.01 million sq. ft., down 20% from the quarterly average of 1.26 million sq. ft. While large leases have buoyed Midtown and Downtown, Midtown South's lack of large transactions has caused leasing activity to lag the levels seen in 2014 and 2015. The only transaction bigger than 100,000 sq. ft. occurred at 61 Ninth Avenue, a new development, with Aetna committing to 146,000 sq. ft., moving 250 employees from Hartford, Connecticut. Year-to-date leasing trails that of 2016 by 6% and is at its lowest mid-year total since 2013. However, while leasing in most size segments across Midtown South was behind historical averages, activity in the 10,000-25,000-sq.-ft. segment has been an area of strength, outperforming its five-year quarterly average of 726,000 sq. ft. by 11%.

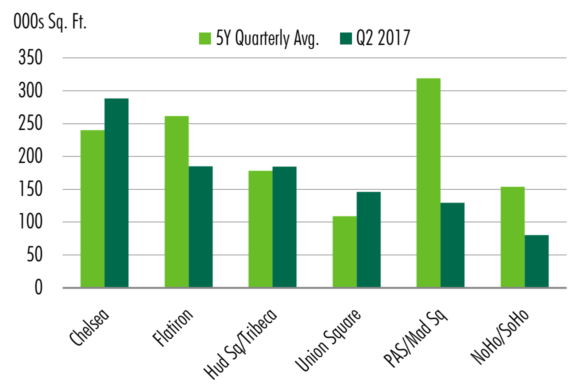
Leasing activity varied widely by submarket. Chelsea registered 288,000 sq. ft., nearly the same total as last quarter and 20% ahead of its five-year quarterly average. The addition of new construction inventory in this submarket has been a draw for leasing thus far in 2017. Aetna was the second insurance company to take space in Chelsea new construction this year, following Argo Group's lease last quarter. Union Square achieved 146,000 sq. ft. of leasing activity, outperforming its five-year quarterly average by 34%; deals such as the 53,000 sq. ft. leased by a tech tenant at 225 Park Avenue South exemplified continued interest in new or updated product. While technology leasing usually leads in this market—and still drove 14% of leasing activity this quarter—leasing across industries was more varied. Insurance accounted for 23% and apparel/retail sales made up 28%; in particular, MAC Cosmetics' 86,524-sq.-ft. lease at 233 Spring Street (1 SoHo Square) and Harry's Razor Company's 61,611-sq.-ft. transaction at 1 Hudson Square propelled the apparel/retail industry's strong quarter.

Figure 2: Leasing Activity | Historical



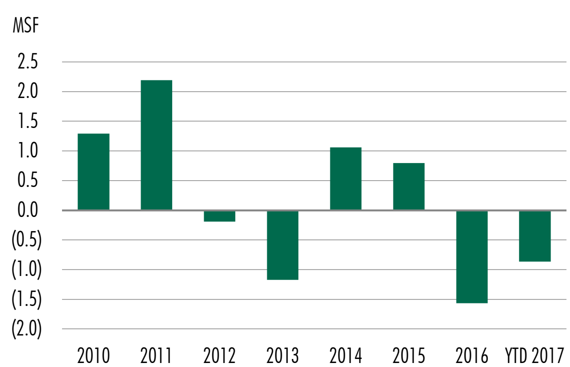

Source: CBRE Research, Q2 2017.

Figure 3: Leasing Activity | By Submarket




Source: CBRE Research, Q2 2017.

Figure 4: Net Absorption | Historical




Source: CBRE Research, Q2 2017.

The Park Avenue South/Madison Square submarket's leasing totaled 129,000 sq. ft., trailing its five-year quarterly average by 59%. While this was the second consecutive quarter of below-average activity, limited new space came to the market, keeping availability relatively unchanged since Q2 2016. NoHo/SoHo registered 80,000 sq. ft. of leasing activity this quarter—48% below the five-year quarterly average of 154,000 sq. ft.—marking the fourth consecutive quarter with leasing below 100,000 sq. ft. Unlike Park Avenue South/Madison Square, availability in NoHo/SoHo has nearly tripled since Q2 2016.

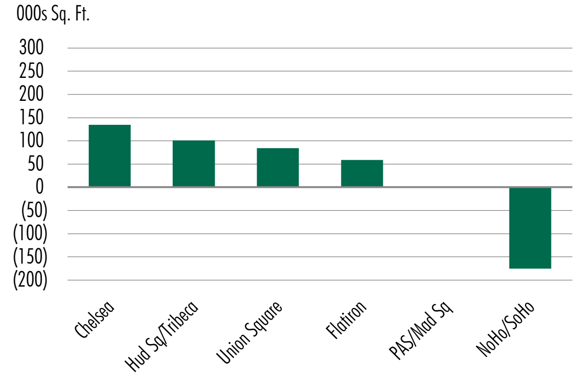
## NET ABSORPTION

Despite a slow quarter for leasing, because Midtown South saw little space added to the market, it achieved 204,000 sq. ft. of positive absorption—the only one of the three Manhattan markets to reach positive territory this quarter. However, the year-to-date total stands at negative 868,000 sq. ft., as the market continues to digest 1.44 million sq. ft. of new construction inventory added at the outset of the year.

Only NoHo/SoHo had negative absorption in Q2 2017. The submarket experienced its sixth consecutive quarter of negative absorption; its year-to-date negative 300,000 sq. ft. of net absorption is the second largest submarket total. While Chelsea witnessed negative 703,000 sq. ft. of net absorption in Q1 2017, that total diminished to negative 569,000 sq. ft. due to strong leasing this quarter.

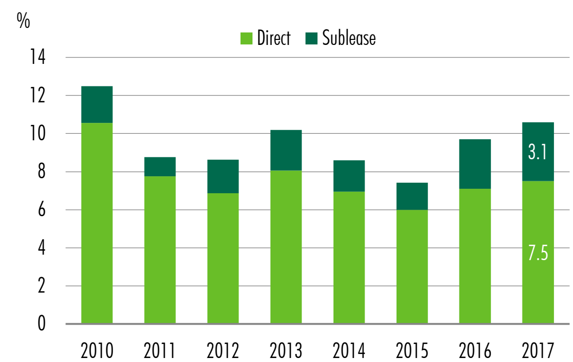
Hudson Square/Tribeca saw positive net absorption of 101,000 sq. ft. in Q2 2017, with above-average quarterly leasing led by the MAC Cosmetics and Harry's Razor Company transactions. Union Square experienced positive net absorption for the second straight quarter, with 84,000 sq. ft. in Q2 2017, bringing its year-to-date total to 189,000 sq. ft.

Figure 5: Quarterly Net Absorption | By Submarket



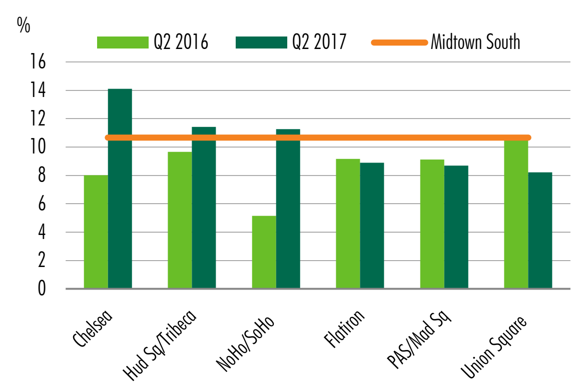

Source: CBRE Research, Q2 2017.

Figure 6: Sublease and Direct Availability Rate | Historical




Source: CBRE Research, Q2 2017.

Figure 7: Availability Rate | By Submarket




Source: CBRE Research, Q2 2017.

## AVAILABILITY

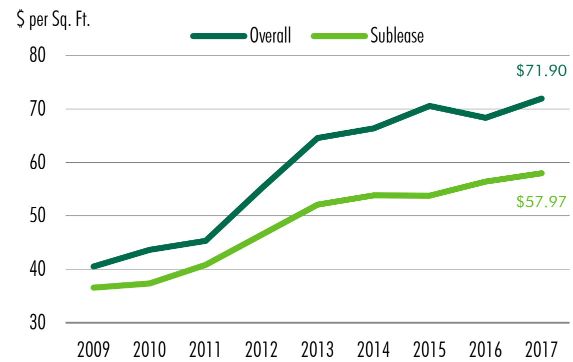
The availability rate declined to 10.7%, a 20-bps improvement from the previous quarter, but still 230 bps higher than Q2 2016's level. Strong leasing in Chelsea, Union Square and Hudson Square/Tribeca led each submarket to post a 50-bps decline in availability from Q1 2017. Union Square, the smallest market in Midtown South at 4.43 million sq. ft., experienced the largest quarterly basis-point drop in availability; at 8.2% it is now the tightest submarket. Although Chelsea saw the second largest basis-point decline of the quarter, it still has the highest availability rate of any Midtown South submarket, at 14.1%. The addition of a number of new construction projects boosted its availability rate at the start of the year.

NoHo/SoHo saw its availability rate rise to 11.3%, its sixth consecutive quarter of increasing availability. In June, three mid-sized spaces came the market. The largest was 58,000 sq. ft. of direct space on the top two floors at 568 Broadway, reportedly asking $80 per sq. ft. Another 43,000 sq. ft. was added at 400 Lafayette and 25,000 sq. ft. of space was added at 100 Avenue of the Americas.

## AVERAGE ASKING RENT

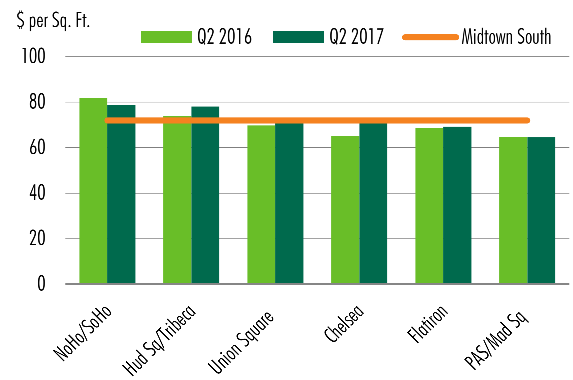
The average asking rent declined 3% from the previous quarter to $71.90 per sq. ft., yet it remains 4% higher than a year ago. Midtown South has the lowest availability rate of the three markets and has very limited supply of large blocks of space, which has kept pricing relatively stable over the past few years. The quarterly decline was not a result of market conditions, but has caused by the leasing of premium-priced space at 61 Ninth Avenue and 225 Park Avenue South. Concurrently, the submarkets where these properties exist also saw declines in their average asking rent.

Figure 8: Average Asking Rent | Historical



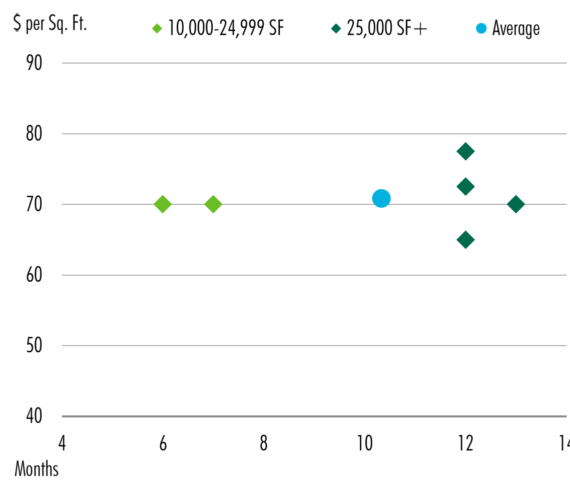

Source: CBRE Research, Q2 2017.

Figure 9: Average Asking Rents | By Submarket




Source: CBRE Research, Q2 2017.

Figure 10: Concession Values | Rent Abatement and T.I. Allowance*




*Identical concession packages will overlap in graphic. Average excludes highest and lowest values.

Source: CBRE Research, Q2 2017.

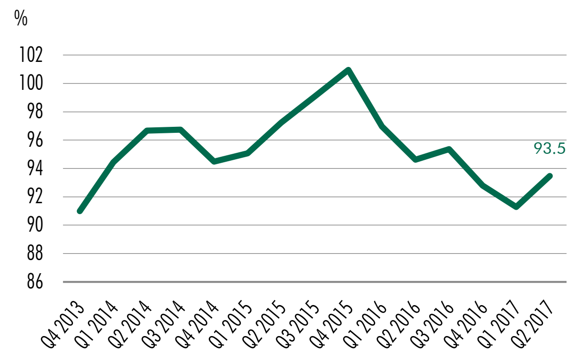
Chelsea, home to new speculative development, saw pricing decline as one of these developments secured Aetna for the entire building; the removal of this 146,000 sq. ft. of premium-priced space drove the average asking rent down to $71.14 per sq. ft. Although this is a 9% decline quarter-over-quarter, the submarket still remains 9% above Q2 2016's average of $65.14 per sq. ft.

NoHo/SoHo saw average asking rents dip below $80 per sq. ft. for the first time since Q1 2016, dropping to $78.74 per sq. ft. this quarter. Despite the decline, the submarket still boasts the highest average asking rent of any in Midtown South.

### TAKING RENT INDEX

The taking rent index posted a 219-bps increase quarter-over-quarter, to 93.5%. Concession packages for new leases of raw space completed during the quarter included an average of $71 per sq. ft. in tenant improvement allowance and 10 months of free rent.

Figure 11: Taking Rent Index | Historical




Source: CBRE Research, Q2 2017.

## INVENTORY AT A GLANCE


| Submarket | Total Size (Mil. Sq. Ft.) | No. of Buildings |
|---|---|---|
| Chelsea | 15.44 | 51 |
| Flatiron | 11.35 | 59 |
| Hudson Square / Tribeca | 15.72 | 35 |
| NoHo / SoHo | 7.86 | 50 |
| Park Avenue South / Madison Square | 19.45 | 58 |
| Union Square | 4.43 | 28 |
| **TOTAL INVENTORY** | **74.25** | **281** |

## 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 10,000 sq. ft. or greater consummated over the past 3 months

Leasing Activity — Total amount of sq. ft. leased within a specified period of time, including pre-leasing and purchases of space for occupancy, excluding renewals.

Leasing Velocity — Total amount of sq. ft. leased within a specified period of time, including pre-leasing and purchases of space for occupancy, including 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.

## SURVEY CRITERIA

CBRE's market report analyzes fully modernized office buildings that total 50,000+ sq. ft. in Midtown South, 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.

## CONTACTS

**Nicole LaRusso**
*Director, Research & Analysis*
+1 212 984 7188
Nicole.LaRusso@cbre.com

**Mike Slattery**
*Research Manager*
+1 212 656 0583
Michael.Slattery@cbre.com

To learn more about CBRE Research, or to access additional research reports, please visit the Global Research Gateway at: www.cbre.com/researchgateway.