NEW YORK CITY

EXECUTIVE SUMMARY

- Technology, co-working, rent reform and the presidential election will all have varying effects on the office leasing and investment market in 2020.
- Expect new development to continue to drive up pricing in the Manhattan office leasing market, while much of the new amenity-rich construction will continue to experience some amount of pre-leasing.
- Office vacancy is expected to increase slightly given just modest office-using employment demand forecasted for 2020.
- While the impact of rent-reform regulation is expected to cause a decline in multifamily investment, office and retail investment is likely to remain flat in 2020.
- Traditional retail will continue to feel the impact of online shopping, resulting in the continuation of downward pricing adjustments.

Going into 2020, New York's commercial real estate market will benefit from continued leasing demand by technology, advertising, media and information (TAMI) firms and low interest rates. These factors should sustain office leasing volume and investor interest throughout the year. However, both are at risk of being offset by ongoing geopolitical uncertainty related to the US-China trade tensions as well as the typical slowdown seen during a presidential election year.

The New York City economy continues to outpace New York State and the nation's economy in terms of private-sector job growth. As of the latest monthly job report released for November, year-over-year job growth within the private-sector of New York City grew 1.8% in comparison to 1.3% for New York State and 1.6% nationally. The greatest office-using employment gains were again seen in the educational and health services sectors, while continued job increases were also noted in professional and business services and technology. These gains offset losses reported in the financial sector, where some large companies have announced downsizing or job relocations out of New York City over the past year. The expectation for 2020 is for office-using employment in New York City to remain positive, but to grow at a slower rate than in recent years.

For 2019, strong employment gains translated into Manhattan office leasing volume that set a new record high of 38.7 msf, up from the 37.0 msf recorded in 2018. The prior record high was in 2001 at 39 msf. While 2019 leasing volume was buoyed by robust activity from TAMI tenants, transactions executed by co-working occupiers were also a strong driver of demand in 2018 and early 2019. However, towards the end of 2019, that demand contracted dramatically given recent headwinds faced by particular operators. This contraction is expected to carry over into the new year. Accordingly, leasing volume is likely to measure a slight decline in 2020. Since the turn of the century, office leasing volume has also measured a decline during a presidential election year, as tenants have taken a "wait and see approach" before making their occupier decisions. As a result of these two factors, New York City vacancy is expected to rise slightly in 2020.

New development in the office leasing pipeline will likely drive up pricing in the Manhattan office leasing market, keeping overall average asking rents above the $80.00 per square foot (psf) level and even higher for new, premium product. As in the past, it is expected that pre-leasing in these new amenity-rich construction projects will also put upward pressure on pricing.

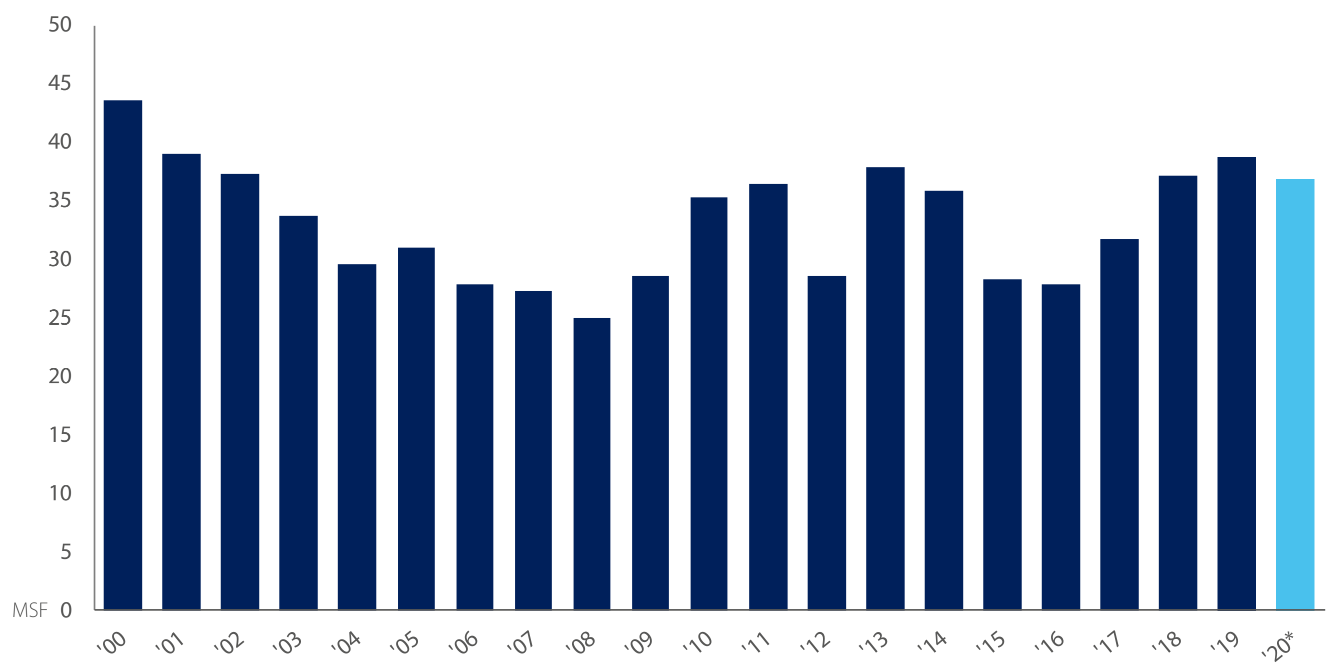
KEY MARKET METRICS – 2020 EXPECTATIONS

Annual growth rates, estimated for year-end 2020 vs year-end 2019.

	OFFICE	RETAIL
Rental Growth	↑	↓
Vacant Space	↑	↑
Construction Levels	↑	—
Leasing Volume	↓	→
Investment Volume	→	→

Since the turn of the century, office leasing volume has declined in a U.S. Presidential election year as tenants have taken a "wait and see approach" before making their occupier decisions. The same is expected in 2020.

HISTORICAL LEASING VOLUME ACTIVITY



* Forecasted / *Source: Avison Young*

The investment market for New York City office buildings is expected to continue to benefit from a low interest rate environment, as well as capital from both domestic and foreign sources. While an absence of inflationary pressures is expected to create the likelihood of a long period of ultra-low or negative rates, which opens up the possibility of further yield compression, lower interest rates are likely to extend the real estate cycle and this bodes well for the long-term investor. As a result, the New York City office market will continue to be an attractive, safe haven for many investors. However, the amount of available office product for sale remains limited, particularly when it comes to trophy office assets suitable for the large institutional investor. Although steady competition and a healthy bidding pool is expected when such assets do become available for sale, the number of trades in 2020 is likely to be limited.

Other factors that are expected to impact the investment market in 2020 include rent-reform regulation related to the local multifamily sector. Passed in mid-June, the comprehensive legislation related to the Housing Stability and Tenant Protection Act of 2019 introduces significant changes to the laws governing New York City's rent-regulated housing stock. Along with this rent regulation comes unintended consequences that impact an owner's ability to increase rents to cover operating expenses or property improvements. This new legislation coupled with overall economic and political uncertainty expected in 2020 is likely to keep investors of all types on the side lines. Although rent-reform regulation in New York City will only have an impact on the multifamily sector, which will result in a decline in investment volume within the segment, volume growth across all other property types is likely to be flat.

Expect the multi-family sector to be negatively impacted by recent rent regulatory changes with regard to stabilized rents in New York City. Related unintended consequences associated with property upkeep are also anticipated in the coming year. The chart below provides a brief overview of the major regulatory changes that impact an owner's ability to increase rents to cover operating expenses or improvements.

HIGHLIGHTS OF NEW RENT REFORM REGULATION

1. NYC rent regulation laws are made permanent vs expiring every 4-8 years.
2. High-rent vacancy and high-income deregulation statutes are repealed.
3. Statutory vacancy and longevity bonuses are repealed.
4. Owners can not raise preferential rent to full legal amount upon lease renewal.
5. Full legal regulated rent is only charged once tenant vacates.
6. Maximum collectible rent increase is set to a five-year average of Rent Guideline Board increases.
7. Annual Major Capital improvement rent increase capped at two percent.
8. Reimbursable Individual Apartment Improvement (IAI) spending capped at $15K, with stipulations.

Source: Avison Young

NUMBER OF CHAIN STORES BY BOROUGH

Borough	2019	2018	% Change
Bronx	1,003	1,043	-3.84%
Brooklyn	1,719	1,790	-3.97%
Queens	1,763	1,854	-4.91%
Manhattan	2,891	2,982	-3.05%
Staten Island	456	467	-2.36%
Total NYC	7,832	8,136	-3.74%

In regard to the state of the chains, national retailers have reduced their footprint in New York City by 304 locations, declining from 8,136 in 2018 to 7,832 stores in 2019 – a 3.7% decrease.

WHERE THE CHANGE IS OCCURRING

Retailer	Number of Stores, 2019	Difference 2018-2019	Largest Increase/Decrease
Dunkin' Donuts	636	+12	Manhattan
Metro PCS	468	-3	Manhattan
Starbucks	351	+24	Queens
Duane Reade/Walgreens	317	+54	Queens
Subway	287	-43	Queens
T-Mobile	245	-7	Queens
Baskin-Robbins	217	-10	Brooklyn/Queens
McDonald's	203	-4	Queens/Manhattan
CVS/Pharmacy	170	+12	Manhattan
7-Eleven	141	0	-

Source: Center for an Urban Future State of the Chains, 2019 Report

Expect more food and health chain openings in 2020, given a greater emphasis on healthier living and the success of plant-based food options that have been introduced in places such as Dunkin' Donuts.

In regard to the overall retail market in 2020, headwinds include higher tariffs on some electronics, footwear and apparel goods imported from China. For now, lower interest rates are putting more disposable income in consumer's pockets. However, potential price increases associated with higher tariffs for such goods must be considered, as well as the resultant impact of reduced consumer disposable income and ultimately lower retail sales for merchants.

The retail sector continues to adjust pricing to reflect the impact of ecommerce on traditional brick-and-mortar stores. Given the shift in the industry, the number of store closures could exceed more than 9,300 in 2020, particularly as traditional retailers are slow to adopt the optimal click and brick strategy. As a result, expect rents to continue to decline and the amount of vacant space to continue to rise for the sector in 2020. Retail leasing volume will likely be flat year-over-year. Alternatively, investors may take advantage of pricing adjustments causing a minor increase in investment activity while total dollar volume will remain flat. For retail, location matters more than ever before. New York City is over-retailed, and as a result, there is likely to be some attrition and phase out. Prime locations with many backfill options will see a disproportionate share of investor interest and premium pricing. Considered a positive trend, 2020 will welcome more alternative uses of space that include greater experiential options for consumers.