Fourth Quarter Market Report 2018 / New York City

Office Leasing

Market Facts

17%
Year-over-year growth in Manhattan leasing volume for 2018

79%
Co-working percentage of FIRE leasing volume for 2018 in Midtown South

12%
Annual rental rate increase for Midtown South, highest for Manhattan

9.7%
Fourth quarter vacancy rate, Manhattan overall in equilibrium

*At Avison Young, we track office properties that are 20,000 square feet and greater

FIRE, Co-Working and Significant Tenant Renewals and Expansions Propel 2018 Leasing Velocity to Record High and Push Vacancy Below 10.0 Percent

By Market: Co-Working as a Percentage of Total FIRE Leasing Volume for 2018

- **20% of the 49%** Midtown
- **79% of the 36%** Midtown South
- **32% of the 23%** Downtown
- **31% of the 43%** Manhattan

Manhattan office leasing volume reached a record high of 37.0 million square feet in 2018. Contributing to the rise, was financial services, insurance and real estate (FIRE) activity that was heavily supported by a growing share of co-working throughout the year. In addition, a significant number of large tenants renewed their leases and expanded their footprints during the year. These included three leases that were executed in the fourth quarter, each for office space of 350,000 square feet or more.

Overall fourth quarter office rents remained stable year-over-year at an average $78.57 per square foot, while the vacancy rate declined by 50 basis points to 9.7 percent by year-end.

Accordingly, the Manhattan office leasing market remains in equilibrium.

Midtown: Vacancy Rate Pushed Lower Largely by Renewals and Significant Financial Services Activity

Midtown leasing activity throughout 2018 was robust and rose nearly 20.0 percent year-over-year, as the market continued to capture the lion's share of large-block transactions greater than 100,000 square feet. Midtown also benefited from a number of renewals and expansions and several large occupiers that pre-leased blocks of space in newer properties. FIRE tenants executed the majority of transactions within this market during the year with the largest lease in excess of 1.2 million square feet at 1 Columbus Circle for Deutsche Bank, which is relocating from Downtown.

FIRE Tenants Take Top Leases in Midtown

Tenant Industry	New Address Submarket	Size (SF) Lease Type
Deutsche Bank Financial Services	**1 Columbus Circle** Times Square/West Side	**1,213,998** New Lease
JP Morgan Chase & Co. Financial Services	**277 Park Avenue** Plaza District	**855,000** Renewal
Pfizer Health Services	**66 Hudson Boulevard** Hudson Yards/ Manhattan West	**800,000** New Lease*
1199 National Benefit and Pension Funds Government/Public Administration	**330 West 42nd Street** Times Square/West Side	**521,374** Renewal
Bloomberg LP Financial Services	**120 Park Avenue** Grand Central	**468,000** Renewal
JP Morgan Chase & Co Financial Services	**390 Madison Avenue** Grand Central	**418,241** New Lease*
Latham & Watkins Legal Services	**1271 Avenue of the Americas** Sixth Avenue/Rockefeller Center	**407,000** New Lease*
Evercore Partners Inc. Financial Services	**55 East 52nd Street** Plaza District	**350,000** Renewal/ Expansion
Pfizer Health Services	**219 East 42nd Street** Grand Central	**350,000** New Lease
Peloton Retail/Wholesale	**441 Ninth Avenue** Hudson Yards/Manhattan West	**312,000** New Lease*

** Transaction executed on a pre-leasing basis*

The strong leasing activity in Midtown resulted in a 70-basis point decline in the vacancy rate to 9.5 percent from the previous year. Meanwhile, the overall average asking rent of $85.52 for the fourth quarter declined less than 1.0 percent from one year ago and was relatively stable compared to the prior quarter.

70 BPS
VACANCY RATE DECLINE

Midtown South: Dominant Tech Transactions Drive Leasing Velocity

Robust leasing velocity in Midtown South in 2018 was propelled by technology firms that regained their dominance. By year-end, technology/advertising/media/information (TAMI) tenants such as Google and Twitter accounted for 37.0 percent of the total 7.2 million square feet of leasing activity in Midtown South. FIRE accounted for 36.0 percent of the total and within that sector, 79.0 percent of that space was taken by co-working tenants.

MARKET DATA POINTS

Manhattan Overall

Indicator	4Q18	4Q17
Vacancy	9.70%	10.20%
Rent	$78.57	$78.54
Absorption	2,638,775 SF	3,116 SF

Midtown Overall

Indicator	4Q18	4Q17
Vacancy	9.50%	10.20%
Rent	$85.52	$86.22
Absorption	742,498 SF	166,127 SF

Midtown South Overall

Indicator	4Q18	4Q17
Vacancy	7.70%	7.80%
Rent	$81.19	$72.55
Absorption	852,716 SF	(71,075) SF

Downtown Overall

Indicator	4Q18	4Q17
Vacancy	11.80%	12.10%
Rent	$62.04	$63.79
Absorption	1,043,561 SF	(91,936) SF

Data as of 1/8/2019

TAMI Tenants Boost Midtown South Leasing Activity

Tenant Industry	New Address Submarket	Size (SF) Lease Type
Discovery Communications TAMI	**230 Park Avenue South** Gramercy Park	**362,658** New Lease
Ralph Lauren Retail/Wholesale	**601 West 26th Street** Chelsea	**350,000** Expansion
Facebook TAMI	**770 Broadway** SoHo/NoHo	**320,000** Expansion
Google TAMI	**315 Hudson Street** Hudson Square	**280,000** New Lease
Twitter TAMI	**249 West 17th Street** Chelsea	**215,000** Expansion
Google TAMI	**345 Hudson Street** Hudson Square	**180,000** New Lease
WeWork Real Estate	**18 West 18th sStreet** Chelsea	**167,000** New Lease
NYU Langone Medical Center Health Services	**1 Park Avenue** Gramercy Park	**150,000** Expansion
New York University Educational Services	**105 East 17th Street** Gramercy Park	**125,000** Renewal
WeWork Real Estate	**154 West 14th Street** Chelsea	**122,000** New Lease

As a result of the resilient leasing velocity for Midtown South, the overall vacancy rate was 7.7 percent by the end of the fourth quarter, compared to 7.8 percent a year ago. Average asking rents in Midtown South saw the highest rental increase throughout any of the markets in Manhattan, rising 12.0 percent year-over-year to $81.19 in the fourth quarter, up almost 2.0 percent from the prior quarter. Contributors to the yearly increase included new developments at 300 Lafayette Street in Soho, and 40 10th Avenue and 412 West 15th Street, both in Chelsea. Class A taking rents at the latter hit a high-water mark when a financial service firm leased 3,738 square feet for $195.00 a square foot on the top floor of the newly constructed boutique office tower at 412 West 15th Street. Even with concessions including,12 months free rent and a tenant allowance of $125.00 per square foot,this building remains the highest priced on a net effective rent basis in Midtown South in 2018.

$81.19
OVERALL AVERAGE ASKING RENT

Downtown: Government/Public Administration Activity Makes a Come Back; Market Continues to Diversify

Downtown leasing activity for the full year experienced a 14.0 percent annual decline. However, fourth quarter volume soared 125.0 percent year-over-year and reached a post-2013 quarterly high. While leasing among FIRE tenants contributed 23.0 percent to total annual volume, the rise was primarily due to a resurgence of government/public administration tenant activity during the fourth quarter, which was less prevalent throughout most of the year.

Top Fourth Quarter Leases Downtown

Tenant Industry	New Address Submarket	Size (SF) Lease Type
NYCHA Government/Public Administration	**90 Church Street** Tribeca/City Hall	**422,264** Renewal
Pace Univesity Educational Services	**161 William Street** Tribeca/City Hall	**214,466** Renewal/ Expansion
Cahill Gordon & Reindel Legal Services	**32 Old Slip** Financial District	**201,621** New Lease
Hudson River Trading Financial Services	**3 World Trade Center** World Trade Center	**135,000** New Lease
NYPD Government/Public Administration	**375 Pearl Street** Tribeca/City Hall	**106,000** New Lease

Overall Downtown leasing activity continues to diversify and top transactions during the fourth quarter also included two large block renewals and expansions. As a result of healthy leasing, the Downtown overall vacancy rate hit a new two-year low, falling to 11.8 percent by the end of the fourth quarter, down from 12.1 percent a year ago. Downtown's average asking rent of $62.04 declined less than 3.0 percent from one year ago and is down less than 2.0 percent from the prior quarter.

11.8%
NEW TWO-YEAR VACANCY RATE LOW

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Largest Blocks of Contiguous Space Currently Available

3 World Trade Center
World Trade Center
1,354,502 RSF

151 West 42nd Street
Times Square/West side
495,717 RSF

63 Madison Avenue
Gramercy Park
447,388 RSF

1 World Trade Center
World Trade Center
329,981 RSF

250 Broadway
Tribeca/City Hall
313,996 RSF

Trends to Watch

With tech giants such as Amazon, Google and Facebook expanding their presence in the New York City market, expect other innovative companies to increase their footprint.

Given the growing share of co-working space, expect more landlords and property owners to throw their hats into the ring and offer flexible space options of their own.

Expect the Downtown market to continue to diversity beyond the traditional financial services industry, with a boost in government, legal and tech activity in the near term.

Markets by the Numbers

Submarket	Inventory (SF)	Direct Vacant (SF)	Sublet Vacant (SF)	4th Quarter 2018 Overall Vacancy Rate	4th Quarter 2018 Net Absorption (SF)	Year-To-Date Absorption	Current Under Construction* (SF)	Overall Average Asking Rent Class A	Overall Average Asking Rent Class B
Midtown									
Grand Central	54,819,358	4,848,512	1,013,095	10.7%	353,489	27,169	1,733,000	$76.54	$58.69
Penn Plaza/Garment	19,969,798	1,129,689	626,224	8.8%	498,048	192,055	0	$71.26	$60.69
Hudson Yards/ Manhattan West	11,035,904	794,953	75,266	7.9%	80,573	(870,219)	5,517,000	$114.43	$0.00
Plaza District	76,861,806	5,753,551	1,895,651	10.0%	41,273	1,326,550	705,244	$98.47	$63.39
Sixth Avenue/ Rockefeller Center	55,985,260	3,690,903	782,981	8.0%	498,166	789,265	0	$93.64	$63.73
Times Square South	24,964,930	1,682,550	549,391	8.9%	91,998	327,826	0	$72.24	$57.78
Times Square/West Side	37,362,312	3,086,329	643,450	10.0%	(821,049)	(135,663)	0	$81.33	$61.81
Total	**280,999,368**	**20,986,487**	**5,586,058**	**9.5%**	**742,498**	**1,656,983**	**7,955,244**	**$89.50**	**$59.98**
Midtown South									
Chelsea	23,161,279	931,726	711,019	6.9%	395,140	243,488	0	$141.60	$60.58
Hudson Square	14,134,729	822,028	235,264	7.5%	945,454	208,203	0	$88.51	$61.71
Gramercy Park	30,808,894	2,353,384	422,923	9.0%	(545,523)	(715,264)	115,000	$83.55	$63.63
SoHo/NoHo	8,859,381	306,111	151,356	5.2%	57,645	316,099	0	$143.54	$63.23
Total	**76,964,283**	**4,413,249**	**1,520,562**	**7.7%**	**852,716**	**52,526**	**115,000**	**$98.60**	**$62.38**
Downtown									
TriBeCa/City Hall	18,957,427	1,085,563	226,977	6.6%	323,801	(80,284)	0	$62.77	$53.30
Financial District	53,199,740	4,923,866	1,100,443	11.3%	488,004	248,625	0	$58.72	$52.11
World Trade Center	26,276,698	3,305,861	1,030,687	16.5%	231,756	158,517	310,000	$70.40	$48.46
Downtown Total	**98,433,865**	**9,315,290**	**2,358,107**	**11.8%**	**1,043,561**	**326,858**	**310,000**	**$63.73**	**$51.59**
Manhattan Overall Total	**456,397,516**	**34,715,026**	**9,464,727**	**9.7%**	**2,638,775**	**2,036,367**	**8,380,244**	**$82.65**	**$59.12**

Data as of 1/8/2019

* Excludes 7.7 MSF coming online within the next 12 months.

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Fourth Quarter 2018 / New York City

Investment Sales

2018 Summary

The investment sales market in 2018 was a snowball of positive momentum. Rebounding from a corrective market in 2017, the year started strong and stayed strong. Taking into consideration that sales are often a rear view mirror of six to nine months due to the length of a real estate transaction, the market is upward trending once again. Year-over-year dollar volume rose 35 percent for all New York City property sales, coming in at $45 billion by year-end with 1,565 sales. While this total dollar volume is significantly less than the market peak of $76 billion for 2015, it is in well above the10-year average of $41 billion.

Retail property sales rose 8 percent year-over-year to $4.7 billion. Transactions totaled 365, falling into two groups – well positioned assets that draw their value from their location or prominence, or strategic purchases by investors taking advantage of historically low pricing and confident in a retail resurgence within the next decade.

Multi-family properties saw a healthy overall dollar volume of $13.6 billion across 750 trades. This contrasted with mixed pricing fundamentals--an increase in cap rates to 4.52 percent and decline in the price per square foot to $525--instigated by a widening bid-ask spread as investor supply and regulatory risks kept investors conservative in their underwriting. The influx of 60,000 units under construction across New York City, and expected regulatory changes that are forthcoming in 2019, will continue to affect the fundamentals of this asset class.

Office continued to dominate the market in dollar volume and saw 164 sales valued at $18.8 billion. A significant number of the high-dollar trades were above $100 million. That said, the smaller office assets have seen success with relatively strong pricing per square foot.

Development sites were the surprise asset class of 2018, with a dramatic increase in trades, rising 16.0 percent year-over-year to 163 sales valued at $4.5 billion. While location has been the major factor contributing to variability in pricing, the success of development site trades suggest investor confidence remains high.

Factors that will have a major impact in 2019:

1. Amazon has been leading tech sector optimism with the selection of Long Island City for its second headquarters, a move that will generate 25,000 new jobs and occupy four million square feet of office space – with the possibility of expanding to 40,000 new jobs across eight million square feet.

2. Google, which set a city-wide record with it's purchase of Chelsea Market and the recently announced $1 billion campus, Google Hudson Square, signaled its intention to focus on building out it New York presence.

3. Opportunity Zones will bring considerable transaction activity to the boroughs, which hold the most designated census tracts. We expect that the proportion of the City's dollar volume coming from the boroughs to increase dramatically over the next year.

4. Canada, 2018's top foreign investor in Manhattan real estate, and other foreign dollar players, will continue to invest heavily in Manhattan real estate, keeping foreign dollar volume strong despite China's diminished position.

5. The bull market will temper off, and the resulting market jitters will incentivize investors chasing yield to seek the safe returns of physical assets.

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Avison Young's Tri-State Investment Sales group tracks confirmed transactions above $5 million ($1 for retail properties and office condominiums) sold in Manhattan below 96th Street.

Top Fourth Quarter 2018 Sales

Buyer Address Seller	Size (SF) Type	Price Price/SF
Vanbarton Group **425 Lexington Avenue** JP Morgan	750,000 Office	$700.0 million $933
Slate Property Group JV Green Oak **271 West 47th Street** Jack Parker Corp	464 units Multi-Family	$290.0 million $625,000/unit
TH Real Estate JV Taconic Investment Partners **440 Ninth Avenue** Unizo Holdings	398,800 Office	$269.0 million $675
A&E Real Estate Holdings **575 Amsterdam Avenue** Merrill Smith Zuniga	266 units Multi-Family	$220.0 million $827,068/unit
Daishin Securities **400 Madison Avenue** ASB Real Estate	184,859 Office	$194.5 million $1,052

Trends to Watch

How will the emerging bear market affect business activity, and thus the ability of landlords to lease new space?

To what extent will emerging rent regulations make it more difficult for non-institutional players to compete in the multifamily space?

Will other tech companies follow Amazon and, Google to turn New York City into the new Tech Capital? And if so, which ones?

Fourth Quarter 2018 / New York City

Retail Leasing

State of the Retail Market

Asking retail rents in Manhattan in 2018 declined by 20.0 percent on average year-over-year, and landlords offered concessions such as short-term leases, tenant allowances, free rent and participation in store build-outs. While the supply of retail space across Manhattan outweighed tenant demand, leasing activity remained brisk. Quick service restaurants continued to lead the market in leasing, followed by fitness and medical establishments. In addition, a variety of retailers used pop-up stores as a way to test the waters and try out new concepts.

Pop-Up Stores, Not Only Just for the Holiday Season

During the holiday season, local retailers opened pop-up and other short-term shops to take advantage of the heavy holiday foot traffic. It is estimated that over 65 million people visit New York City annually, with millions arriving between November and January.

Gucci, which opened a pop-up venue at 375 West Broadway in Manhattan, exercised the option to extend its lease during the fourth quarter of 2018. Gucci has been successful at this location because the shop has been offering events, performances and multimedia shows in addition to selling apparel and accessories.

The pop-up phenomenon has spread beyond the borders of New York City to malls nationwide. Storefront, which is a website that connects short-term tenants with vacant retail space, saw a 20 percent increase in its listings in malls in 2018, up from 5.0 percent in 2013. Amazon now has pop-up stores in 17 malls across the country. Traditional retailers such as Bloomingdale's and Macy's have dedicated space in their locations for various pop-up brands. In-store pop-ups are helping drive traditional retailers' online sales, which rose 10.2 percent year-over-year.

We expect a variety pop-up stores of all types that are able to offer exciting new concepts to continue to thrive, creating a "win-win" situation for both the store and the property owner. These shops also will serve as a complementary driver to further expand online traffic, even beyond the holiday season.

National and Local Score Card

Nationally, retail sales rose 5.1 percent year-over-year between November 1 and December 24, with total sales for online and in-store purchases together topping $850 billion, a six-year high according to a report by MasterCard. Online sales during this period rose 19.0 percent to a record $123.7 billion, up from $93.9 billion in 2017.

Major retailers opened 3,083 stores nationwide in 2018, Coresight Research reported. Seasoned retailers, including Amazon and AT&T, are opening new concept stores, with some being cashier-free.

Notable Fourth Quarter Retail Transactions

Tenant	Building	Size (SF)	Lease Type
Ikea	999 Third Avenue	17,530	New Lease (first U.S. city-center store)
Tiffany & Co.	6 East 57th Street	73,350	Sublease (Nike space during three-year renovation)
Gucci	375 West Broadway	10,000	Renewal/Extension
E by Equinox Madison Avenue	30 East 85th Street	14,000	New Lease (stand-alone luxury health club)
Woolrich	121 Wooster Street	7,800	Expansion
Hamleys	2 Herald Square	30,000	New lease (first U.S. store)
Cotton Citizen	11 Howard Street	207-room boutique hotel	New lease (first NYC store)
Microsoft	300 Lafayette (TBD)	80,000	New lease (currently eyeing for SoHo flagship store)
Burrow House Furniture	125 Greene Street	2,800	New lease (first brick-and-mortar store)
Redemption	102 Wooster Street	5,000	New lease

In Manhattan, brand names have opened and expanded, including FAO Schwarz at Rockefeller Center, Nike's new 68,000-square-foot-Fifth Avenue flagship store that includes customized sneakers and digital shopping, and Starbucks' new and massive 21,422-square-foot Reserve Roastery and Tasting Room in the Meatpacking District at the newly developed 61 Ninth Avenue property. These leases exemplify how landlords are taking advantage of both vacant and new space in some of the most heavily trafficked areas in the city.

Major retailers closed 5,524 stores nationwide in 2018, however, according to Coresight Research.

Throughout the country, brick-and-mortar stores have fallen victim to online shopping and other market forces.

Nationally, Sears announced the closing of 80 more stores (in addition to the 40 previously announced), the Gap is closing hundreds of mall stores, Victoria's Secret is closing 20 stores and Gymboree announced significant closures that could total half its 900-store base.

Locally, long-time Manhattan retailers announced they were vacating prime Fifth Avenue locations including Lord & Taylor and Henri Bendel, which will be closing its flagship and all 23 of its stores.

Looking Ahead to the Future of Retail

The world of retail remains fascinating and challenging. The amount of energy and creativity that is being deployed by existing and new retailers is unprecedented. The need to survive has brought out the best in all of them. Keep an eye open for additional new and exciting concepts to hit the streets of Manhattan in 2019 and beyond, especially as the retail market is expected to stabilize. If technology continues on its accelerated path, we can expect to see and experience retail formats that are currently unimaginable. The future of retail remains challenging for some and a land of opportunity for others.

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Trends to Watch

We believe pop-up shops are here to stay. Watch for those with exciting new concepts beyond just selling of traditional merchandise to thrive, creating a win-win for both landlords and retailers.

E-commerce trends will continue to change shopping behavior over the next three to five years. Accordingly, we expect some sort of online shopping experience to complement more brick-and-mortar strategies and vice versa.

Many retailers will focus on customization this year and will come up with ways to implement new technology into their online and physical platforms. As a result, expect new concepts that enhance the consumer. experience on an even greater personal level to arise.

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Debt & Equity

Flight to Quality Towards Real Estate Amidst Late-Year Stock Market Declines

The good news for property owners/borrowers in the fourth quarter of 2018 is that interest rates fell by approximately 50 basis points from their high in the previous quarter. Unfortunately, spreads increased by about one half of that amount, negating the net interest rate gains somewhat. Much of the decrease in interest rates was primarily due to the flight to quality when the stock market went into an end-of-the-year swoon versus any bullishness in the bond market.

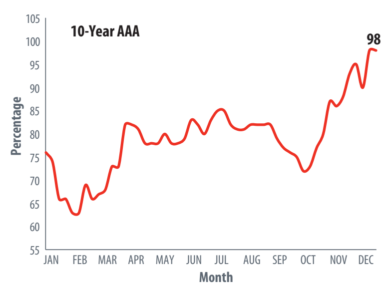
Asking Spreads Over Treasurys

Asking Spreads Over Treasurys
10-year loans with 50-59% LTV

	12/14	Month Earlier
Office	160	150
Retail	152	141
Multi-family	142	131
Industrial	142	131

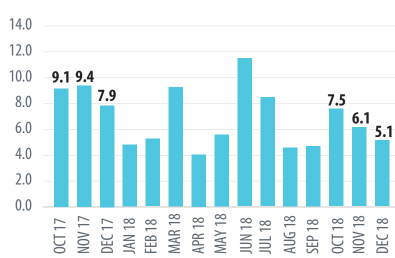
Source: Trepp, Avison Young

CMBS New-Issue Spread Over Swaps



Source: Commercial Mortgage Alert, Avison Young

U.S. CMBS Monthly Issuance



Source: Commercial Mortgage Alert, Avison Young

Recent Casualties

There are certainly pockets of weakness in several areas. Condo sales have seen both a modest price decrease and a slowing of velocity throughout the five boroughs. Retailers are vacating prime Manhattan stores. Lord & Taylor recently became the latest retailer to announce that it was closing its flagship store in Manhattan, a trend that Polo Ralph Lauren essentially started 18 months ago. Henri Bendel decided to close not only its flagship in Manhattan, but all 23 of its stores. Chinese capital, which has underpinned the market over the last five years, has been conspicuous by its absence. The way that the U.S. Government treated Chinese company HNA (forcing it to sell its position in 850 Third Avenue) has spooked other Chinese investors from investing at all. Without foreign investment, the high-end market has stagnated.

The Good – Bright Spots for Owners, Developers and Large Occupiers

Despite the aforementioned weakness, there are many positives in the New York City market. Office rents are spiking in certain sub-markets. Rockpoint Group attained a rental rate of $195 and $180 PSF for the top two respective floors at 412 West 15th Street, illustrating tenant appetite for the best space in the market (with amazing outdoor space included). WeWork continues to take large blocks of space. The Related Companies is successfully leasing space at Hudson Yards as fast as they can get the buildings on line (including a large expansion by Google). The last building in Related's master plan is located at 50 Hudson Yards at West 34th Street and 10th Avenue. This property will be 58 stories and include a 300-seat auditorium. Although not coming on line until four years from now, the property has secured BlackRock as the anchor tenant. Multi-family rental rates in most of the city remain strong with Brooklyn especially red-hot. In addition, when Amazon announced that it was opening a second headquarters in Queens last month, the news lifted the entire borough.

The Bad, But No Recession Imminent

If one looks outside of New York City, things are not quite as rosy. In retail for example, we saw bankruptcies from Sears and Toys "R" Us, making it difficult for some shopping malls to secure financing. Exacerbating the situation is the volatility in the stock market and the tightening by the Federal Reserve. We can't ignore the domino effect that stock market underperformance will have on the real estate sector. Clearly, some participants will pause until the market stabilizes, particularly after seeing what happened in 2008 after the Lehman Brothers' collapse. While there is no 100 percent direct correlation between the stock market and the real estate market, it certainly affects everybody's balance sheet, causes investors to go into "risk off" mode and could ultimately cause capitalization rates to rise (and property values to drop) during 2019. The last downturn a decade ago was due primarily to an extraneous event that caused investors to panic. The housing crisis, caused by high-leverage and no-income check loans, has not been replicated in the current environment. A recession also does not appear imminent based on several advanced indicators. Thus the forecast here is that the market will continue to be bifurcated into the wanted and the unwanted.

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Trends to Watch

Interest rates declined in the fourth quarter though most of the decreases were likely due to a flight to quality during the late-year stock market decline.

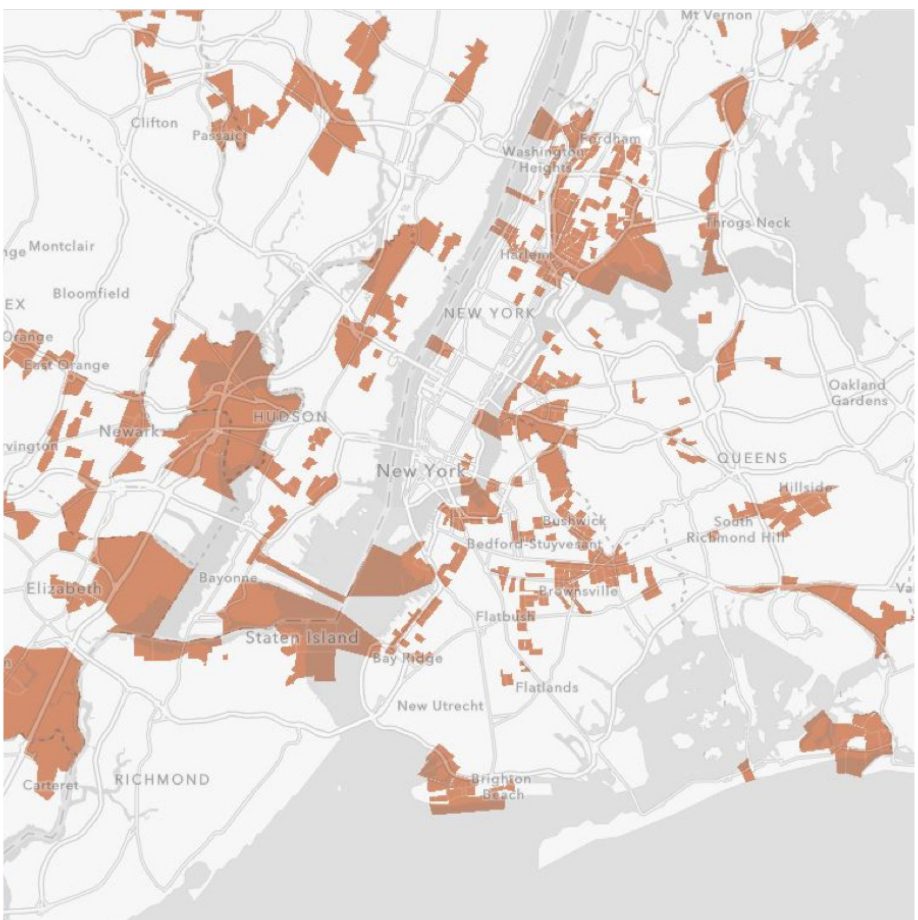
The financing market continues to be bifurcated. Multi-family, Class A office and credit tenant deals continue to have very strong demand from both debt and equity groups alike.

Weak sectors include shopping malls, tertiary markets and unflagged hotels. These are becoming more difficult to finance without huge equity infusions.

Fourth Quarter 2018 / New York City

Valuation & Advisory

Opportunity Zones To Incentivize Development



Source: https://esrimedia.maps.arcgis.com/apps

As part of the tax cuts passed for 2018, the U.S. government created Opportunity Zones (OZs) to encourage investment in lower-income or economically challenged areas. Within New York City, there are 306 designated OZs.

OZs Revisited

OZs provide tax incentives to investors whereby tax on a capital gain can be deferred if the funds are reinvested into an OZ within 180 days. Investors can allocate funds to OZs via Qualified Opportunity Funds (QOFs), investment vehicles set up to invest in recognized "original use" or substantially improved properties within OZs. In applying the substantial improvement test, the qualified OZ business can ignore the cost allocated to land and invest an amount over a 30-month period equal to or greater than the cost allocated to the existing improvements to satisfy the requirement.

Tax Benefits and Compliance

The tax benefits of a QOF investment vary depending on how long the investment is held. For investments held for five years, 10.0 percent of the tax on the deferred gain is excluded. If held seven years, it increases to 15.0 percent. If held for 10 years or more, the investor would not owe any tax on the appreciation of the QOF investment.

To meet the test of compliance, investors and/or QOFs will need to get appraisals in order to break out land from the building improvement values in order to demonstrate they have satisfied the required capex multiple when undertaking a substantial building renovation.

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Trends to Watch and Questions to Ask

Because of these generous tax incentives, there has been a high level of expressed interest from developers in OZs that can be expected to translate into new property development.

What metrics would be appropriate for determining whether tangible property has "original use" in an OZ?

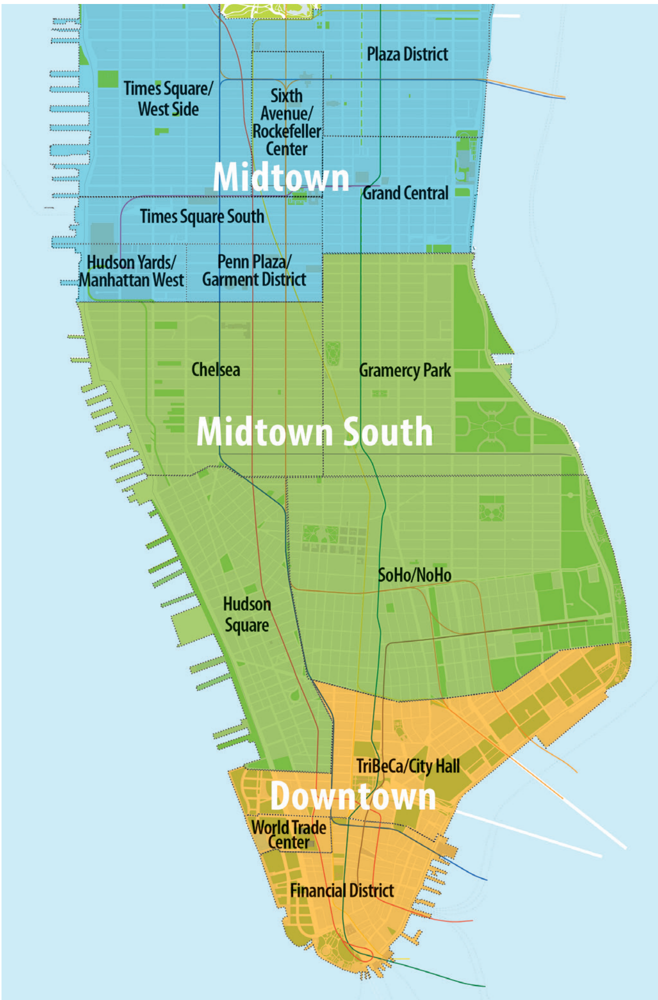
Should the use of tangible property be determined based on its physical presence within an OZ, or based on some other measure?

What if the tested tangible property is a vehicle or other movable tangible property that was previously used within the OZ but acquired from a person outside the OZ?

Should some period of abandonment or under-utilization of tangible property erase the property's history of prior use in the OZ? If so, would this enable subsequent productive utilization of the tangible property to qualify as "original use?"

Should the rules appropriate for abandonment and underutilization of personal tangible property also apply to vacant real property that is productively utilized after some period? If so, what period of abandonment, underutilization, or vacancy would be consistent with the statute?

About the Market



Midtown

Plaza District: Borders East 62nd and West 59th Streets on the north, Seventh Avenue on the west, East 47th and West 56th streets on the south and the East River on the east (includes prior Park Avenue submarket)

Grand Central: Borders East 47th Street on the north, Fifth Avenue on the west, East 35th Street on the south and the East River on the east

Sixth Avenue/Rockefeller Center: Carved out section that borders West 56th Street on the north, Seventh Avenue on the west, West 41st Street on the south and Fifth Avenue on the east

Times Square/West Side: Borders West 64th Street on the north, the Hudson River on the west, West 41st Street on the south and Fifth Avenue on the east (includes Columbus Circle)

Times Square South: Borders West 41st Street on the north, the Hudson River on the west, West 36th Street on the south and Fifth Avenue on the east

Penn Plaza/Garment District: Borders West 36th Street on the north, the Hudson River on the west, West 30th Street on the South and Fifth Avenue on the east

Hudson Yards/Manhattan West: Carved out section that borders West 36th Street on the north, the Hudson River on the west, West 30th Street on the south and Ninth Avenue on the east

Midtown South

Chelsea: Borders West 30th Street on the north, the Hudson River on the west, West 12th Street on the south and Fifth Avenue on the east (includes prior Flatiron submarket)

Gramercy Park: Borders East 35th Street on the north, Fifth Avenue on the west, East 12th Street on the south and the East River on the east (includes prior Union Square/Madison Square/Park Avenue South submarkets)

Hudson Square: Borders Morton Street on the north, the Hudson River on the west, Chambers Street on the south and Sixth Avenue/Avenue of the Americas on the east

SoHo/NoHo: Borders East 12th Street on the north, Sixth Avenue/Avenue of the Americas on the west, Canal Street/East Broadway on the south and the East River on the east (includes Greenwich Village)

Downtown

Tribeca/City Hall: Borders Canal Street/East Broadway on the north, West Street on the west at Warren Street, Ann Street on the south and the East River on the east (all of upper-lower Manhattan); (includes prior insurance submarket)

World Trade Center: Borders Vesey Street on the north, the Hudson River on the west, Albany Street on the south and Church Street/Trinity Place on the east

Financial District: Borders Albany and Ann Streets on the north, the Hudson River on the west, South Street on the south and the East River on the east (rest of lower Manhattan)

Notes

Notes

New York City

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