MARKETBEAT

INDIANAPOLIS

Office Q3 2020

CUSHMAN & WAKEFIELD

		YoY Chg
18.5%	Vacancy Rate	▲
14K	Net Absorption, SF	▼
$21.30	Asking Rent, PSF	▲

Overall, All Property Classes

ECONOMIC INDICATORS Q3 2020

		YoY Chg
1,050.2K	Indianapolis MSA Employment	▼
7.6%	Indianapolis MSA Unemployment Rate	▲
8.8%	U.S. Unemployment Rate	▲

Source: BLS, Moody's Analytics

ECONOMIC OVERVIEW: Signs of Economic Recovery Evident, Late Year Headwinds Apparent

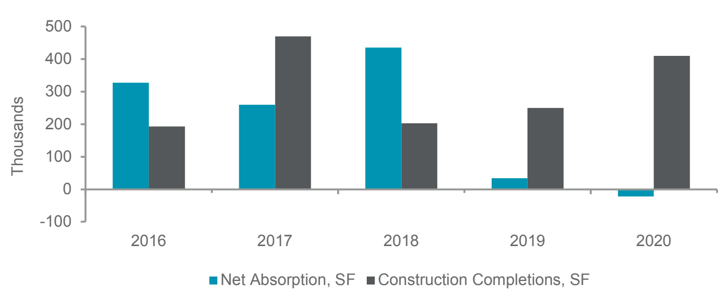
Throughout the third quarter the economy began to produce more favorable conditions as many COVID-19 restrictions loosened across the country, allowing many leading economic indicators to rebound. Over the span of four months the US has experienced nearly eleven million jobs restored leaving the national unemployment rate at 8.8%. Indianapolis tracked similarly, with nonfarm employment rising by over 100,000 jobs from the trough produced in April, ultimately lowering the unemployment rate to 7.6%. US core retail sales, which most closely tracks the consumer spending component of GDP, steadily increased through July, before slowing in August and September. The slowdown can partially be attributed to the expiration of the $600 per week unemployment subsidy in July which cut incomes by an estimated $70 billion in August. This news was followed by recent concerns regarding September employment data where nonfarm payrolls missed analyst expectations by nearly 200,000 jobs. Both events signal developing economic uncertainty despite positive backward-looking economic indicators and could carry into the end of the year if not addressed by government intervention.

Upon the arrival of COVID-19 in the U.S., the economy entered a recession in March 2020, recording the worst decline in post-war history in Q2 2020. Mounting evidence indicates that the recovery began in May or June with Q3 2020 data likely reflecting that. But, until there is a public health resolution to the pandemic, the recovery is likely to remain uncertain and gradual. Only then can households and businesses become more confident. Access the most recent research on CRE and the state of economy here.

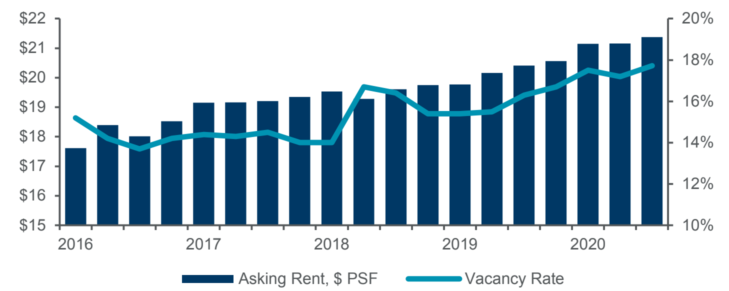
DEMAND: Suppressed Second and Third Quarter Demand Beginning to be Realized

The Indianapolis office market began to realize the negative impact of the pandemic as many occupiers were forced to reevaluate their office footprint. As a result, leasing velocity has slowed while putting upward pressure on vacancy rates. Despite the easing of many health and safety restrictions, overall market vacancy rose to 18.5% or a 62-basis point increase quarter-over-quarter (QOQ) and 130-basis point increase year-over-year (YOY). Leasing velocity has been cut by almost half YOY with 336,000 square feet (sf) leased in the third quarter 2020, down from 668,000 sf. Absorption-wise, 14,000 sf of space was absorbed in third quarter overall while 68,000 sf came in the form of direct absorption, both of which were primarily driven by the completion of 287,000 sf of new construction that hit the market at roughly 90% occupied. The large variation in direct and overall absorption indicates that a large amount of sublease space was negatively absorbed. In terms of sublease vacancy, the third quarter faced a 15-basis point increase QOQ, settling at 0.73%. This is a significant trend we are tracking as many COVID-19 contingency plans have involved placing all or part of an occupant's office space on the market for sublease as businesses close offices or transition employees to a work-from-home model. With leasing velocity tracking at low levels combined with economic uncertainty entering the fourth quarter, demand fundamentals will remain soft, putting further pressure on vacancy rates and leasing activity.

SPACE DEMAND / DELIVERIES



DIRECT VACANCY & ASKING RENT



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PRICING: Asking Rents Grow Slightly, Future Growth Expected To Taper Off

Coming off 5.0% YOY rental growth in the second quarter 2020, the third quarter saw rental rate growth YOY slide to 3.9%, settling out at $21.30 per square foot (psf). From a QOQ standpoint, rents grew only $0.10 psf from the second quarter. In general, the market has held steady with regards to downward pressure on rental rates, thus far, but the headwinds from slowed leasing velocity and growing vacancy rates are sure to test the wherewithal of landlords. Another key metric to keep an eye on is sublease space pricing and its effect on overall rental rates. The expectation for future quarters is that new sublease space will continue to account for a larger share of overall vacancy while competing with direct availabilities. Because sublease space often comes at a discount to direct availability, this new market dynamic will likely drive overall asking rates lower.

SUPPLY: Construction Deliveries Drive Demand Metrics, Construction Starts Delayed

During the third quarter nearly 287,000 sf of new construction delivered, bringing year-to-date (YTD) total to just under 410,000 sf. The deliveries proved strategic to demand fundamentals as 256,000 sf of the total 287,000 sf delivered to the market as fully occupied, propping up absorption numbers in a significant way. Three projects remain in the current construction pipeline totaling 304,000 sf and all are expected to deliver to the market in 2021. Two of the projects are build-to-suit in nature and account for nearly 80% of the total pipeline square footage. For the foreseeable future, we expected new construction projects to struggle breaking ground without significant preleasing activity.

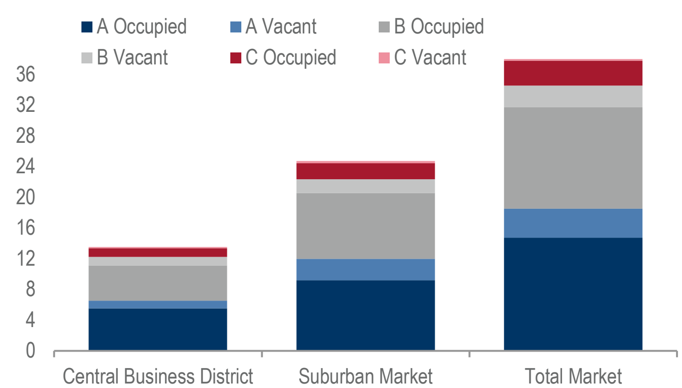
SALE ACTIVITY: Investment Sale Activity Slow, User Sale Activity Up

The volume of sale activity in 2020 is tracking at nearly half of the volume experienced in 2019 with just, 1.1 million square feet (msf) of space trading hands through three quarters. Many investors have been “pencils down” on deals in most cases due to the unsettled impacts on values in the current market. At the right discount many buyers are willing to bid on quality core office assets due in part to the significant “dry powder” that remains in the investment market. Sellers, on the other hand, continue to be unwilling to accept discounted pricing in favor of near-term market improvement. The value gap between buyers and sellers remains a significant stop hold on investment activities. In future quarters while the headwinds of the current market conditions persist, many investors are preparing funds to invest in distressed assets. Much of this activity will likely not take place until 2021 at the earliest as it takes time for distressed opportunities to emerge.

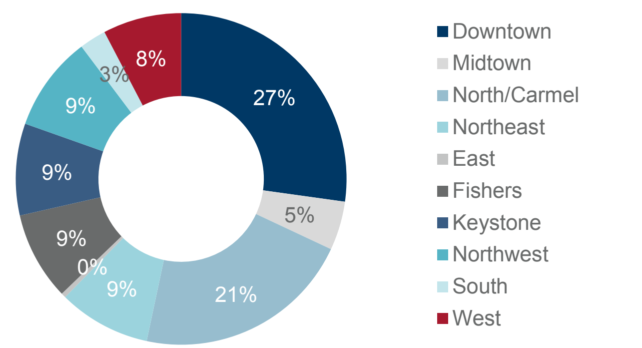
Outlook

- The third quarter saw signs of economic recovery, but late quarter headwinds seem to be developing despite positive backward-looking economic indicators and could carry into the end of the year if not addressed by government intervention.
- Suppressed second and third quarter leasing velocity has instigated a rise in vacancy rates. Expect continued stifled leasing velocity married with questionable economic headwinds which will put demand fundamentals on a continued undesirable trajectory, ultimately leaving vacancy rates and absorption levels negatively affected.
- The market has held steady with regards to downward pressure on rental rates, thus far, but the headwinds from shallow leasing velocity and growing vacancy rates are sure to test the wherewithal of landlords.

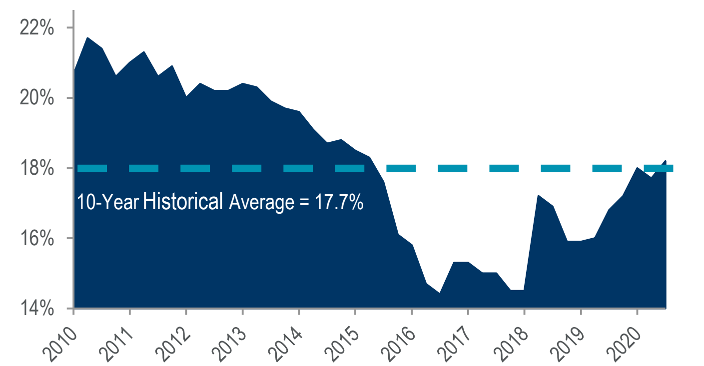
LEASING DEMAND BY CLASS OF SPACE (MSF)



VACANT SPACE BY SUBMARKET



DIRECT VACANCY RATE VS. 10 YEAR HISTORICAL AVERAGE



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MARKET STATISTICS

SUBMARKET	INVENTORY (SF)	SUBLET VACANT (SF)	DIRECT VACANT (SF)	OVERALL VACANCY RATE	CURRENT QTR DIRECT NET ABSORPTION	YTD DIRECT ABSORPTION (SF)	YTD LEASING ACTIVITY (SF)	UNDER CNSTR (SF)	OVERALL AVG ASKING RENT (ALL CLASSES)*	OVERALL AVG ASKING RENT (CLASS A)*
Downtown	11,700,659	80,627	1,839,737	16.4%	37,710	13,558	166,699	66,000	$23.89	$25.68
Midtown	1,831,816	3,667	332,931	18.4%	3,358	-2,265	45,690	0	$17.34	$21.97
East	510,538	0	32,418	6.4%	-8,198	25,435	3,853	0	$15.42	N/A
Fishers	1,963,877	1,475	607,341	31.0%	61,333	114,713	61,458	168,000	$20.96	$21.92
Keystone	4,108,371	40,574	591,496	15.4%	-56,833	25,411	171,566	0	$23.71	$24.60
North/Carmel	7,874,481	117,096	1,392,475	19.2%	81,915	-160,401	300,024	70,000	$22.95	$24.50
Northeast	3,186,958	21,121	616,300	20.0%	-40,998	-58,841	68,148	0	$18.48	$20.40
Northwest	3,788,471	12,368	644,895	17.4%	-31,211	90,823	159,318	0	$18.55	$20.07
South	1,401,063	3,045	181,532	13.2%	-2,487	7,212	56,096	0	$19.07	$22.03
West	1,891,692	0	541,887	28.7%	-30,378	-77,525	41,802	0	$15.18	$17.20
Class A	18,513,236	179,718	3,581,158	20.3%	219,160	158,022	672,976	304,000	$23.60	
Class B	16,060,592	91,132	2,761,053	17.8%	-208,815	-181,033	300,722	0	$19.07	
Class C	3,684,098	9,123	438,801	12.2%	3,866	-1,131	100,956	0	$15.32	
TOTAL	**38,257,926**	**279,973**	**6,781,012**	**18.50%**	**14,211**	**-21,880**	**1,074,654**	**304,000**	**$21.30**	**$23.60**

Rental rates reflect full service asking

KEY LEASE TRANSACTIONS Q3 2020

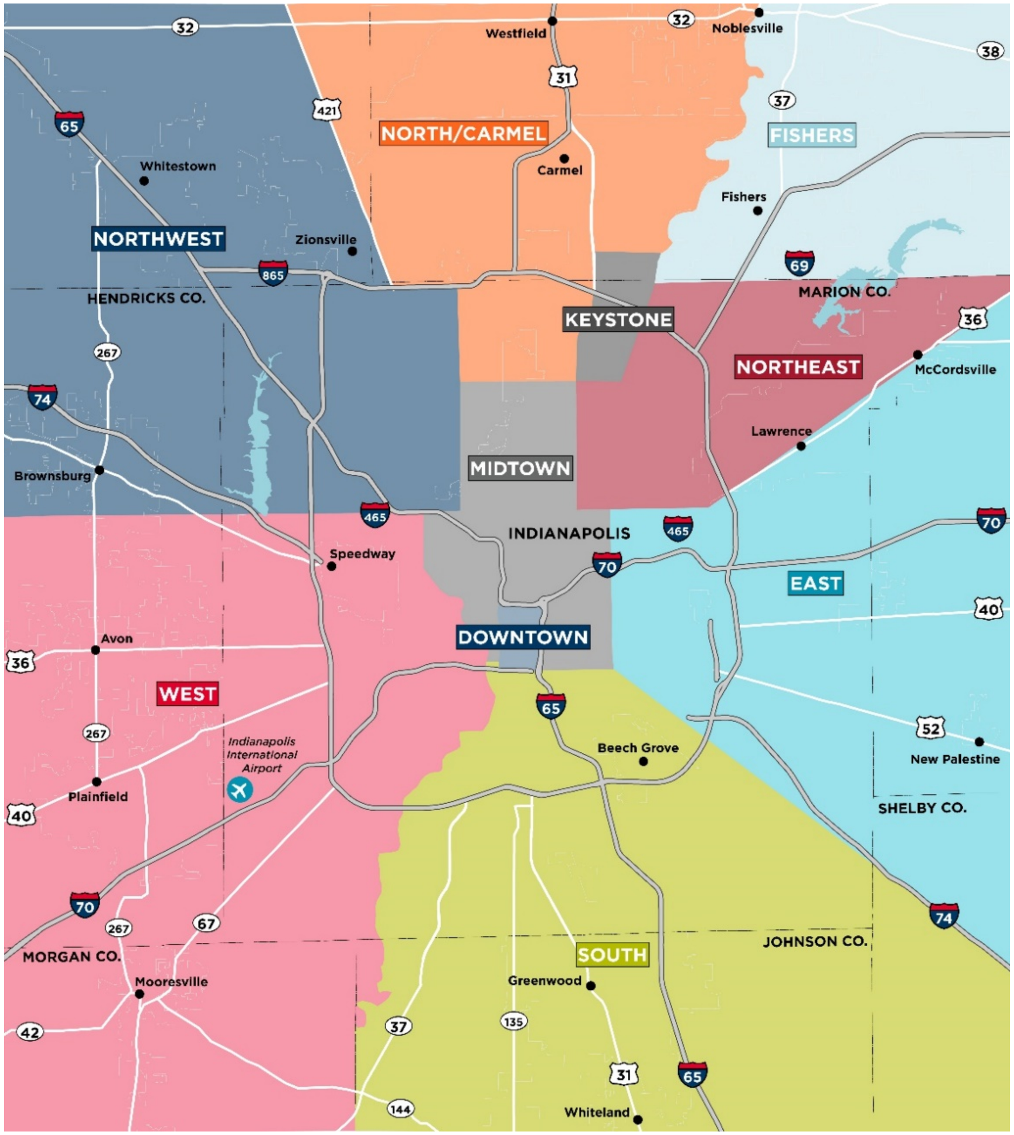
PROPERTY	SUBMARKET	TENANT	RSF	TYPE
13085 Hamilton Crossing Blvd., Indianapolis	North/Carmel	Aptiv	88,200	New Lease
9045 River Road, Indianapolis	Keystone	USIC	47,060	Renewal*/Expansion
111 Monument Circle, Indianapolis	Downtown	HNTB	40,947	Renewal*/Expansion
225 South East St., Indianapolis	Downtown	Elements Financial	31,651	Renewal*
310 E 96th St., Indianapolis	North/Carmel	Herman & Kittle Properties	26,376	New Lease

Renewals not included in leasing statistics

KEY SALES TRANSACTIONS Q3 2020

PROPERTY	SUBMARKET	SELLER / BUYER	SF	PRICE/$ PSF
1752-1776 N Meridian St	Midtown	1776 Real Estate LLC | Chatham Park Development	86,343	$6.3M | $73
3850 Shore Dr	West	Eagle Properties LLP | Kundi Eenterprises LLC	28,225	$1.9M | $68

OFFICE SUBMARKETS



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