Manhattan office market insights

Q4 2021

AVISON YOUNG

Key office takeaways

Economic conditions

- The Manhattan labor market continued to strengthen in the fourth quarter, demonstrated by the **unemployment rate decreasing by 40 bp to 6.5% from September 2021 in October 2021.** The unemployment rate approached the 2000 to September 2021 historical average of 6.1%.

- **New York MSA office employment decreased by 2.9% from February 2020 to October 2021**, though private-sector office employment declined by a comparatively modest 2.6%.

Recovery rate

- Manhattan is tied with Boston for the **#2 office market in the U.S. in terms of return-to-office efforts at -51.7%** compared with the same week in 2019.

- Representative Manhattan-based **banking and finance employers** have mandated hybrid work schedules, resulting in a comparatively strong **return-to-office rate of -36.6%** compared with the same week two years ago.

Office demand

- Leasing activity rebounded from 2020 levels, **increasing by 16.6% year-over-year to 28.1 msf**, but remained **-32.4% compared with the prior 20-year annual average.** Q3 to Q4 2021 was the most active six-month period since Q4 2019 to Q1 2020.

- Trophy-quality buildings continued to capture an outsized share of post-COVID demand as large-scale tenants almost universally 'traded up' by relocating to similar or higher-quality offerings. **Trophy properties, the top 10.0% of the market, have captured 40.9% of leases.**

Key office takeaways

Office supply

- The **total availability rate remains near record levels, totaling 18.1% as of Q4 2021.** Stronger deal flow partially offset new availabilities from Q3 to Q4 as the sublease availability rate decreased by 20 bp to 4.4% but the direct availability rate increased by 10 bp to 13.9%.
- Strengthened demand for high-quality properties caused the **Trophy availability rate to decrease by 70 bp to 13.0% year-over-year.**

Pricing trends

- **Class A net effective rents softened by 13.4% from the pre-COVID peak to December 2021.** Base rents have steadied near all-time highs, though record levels of concessions that are being offered to induce long-term tenant commitments have caused net effective rents to soften.
- Healthy demand for high-quality properties has caused **Trophy net effective rents to moderate by just -1.0% from December 2019 to December 2021.**

Capital markets

- Investment demand demonstrated signs of strengthening in the fourth quarter as several high-profile assets traded and others reportedly went under contract. **Total office investment volume increased from $6.3B in 2020 to $6.7B in 2021.**
- **Asset pricing decreased by 13.8% since 2019** as investors adopted more conservative underwriting assumptions given prevailing office occupier market uncertainties.
- The **spread between office cap rates and 10-year Treasury rates of 321 bp** remained wider than the long-term historical average.

Let's review some key economic and demographic trends

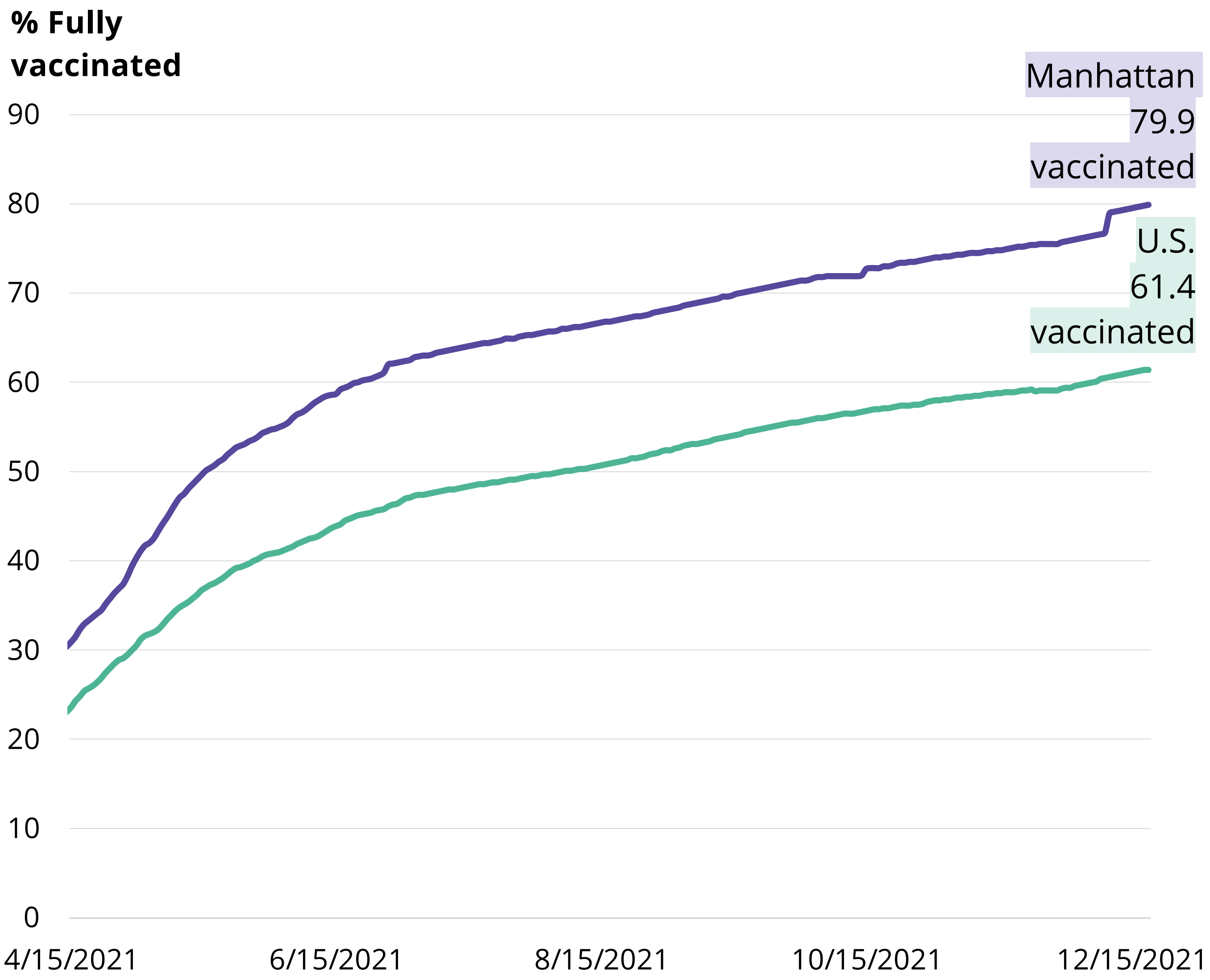
Competitive office labor market conditions have partly enabled employers to continue to adopt hybrid work strategies.

Vaccination rates across population

79.9%

Share of total Manhattan population that is fully vaccinated.

The State of New York instated more stringent mask mandates on December 10, 2021 for all indoor public places that do not mandate vaccinations, including offices, to combat the spread of the Omicron variant. This requirement will be reassessed on January 15, 2022. Further, the City of New York mandated that all private-sector employees must show proof of at least two vaccination doses after December 27, 2021.



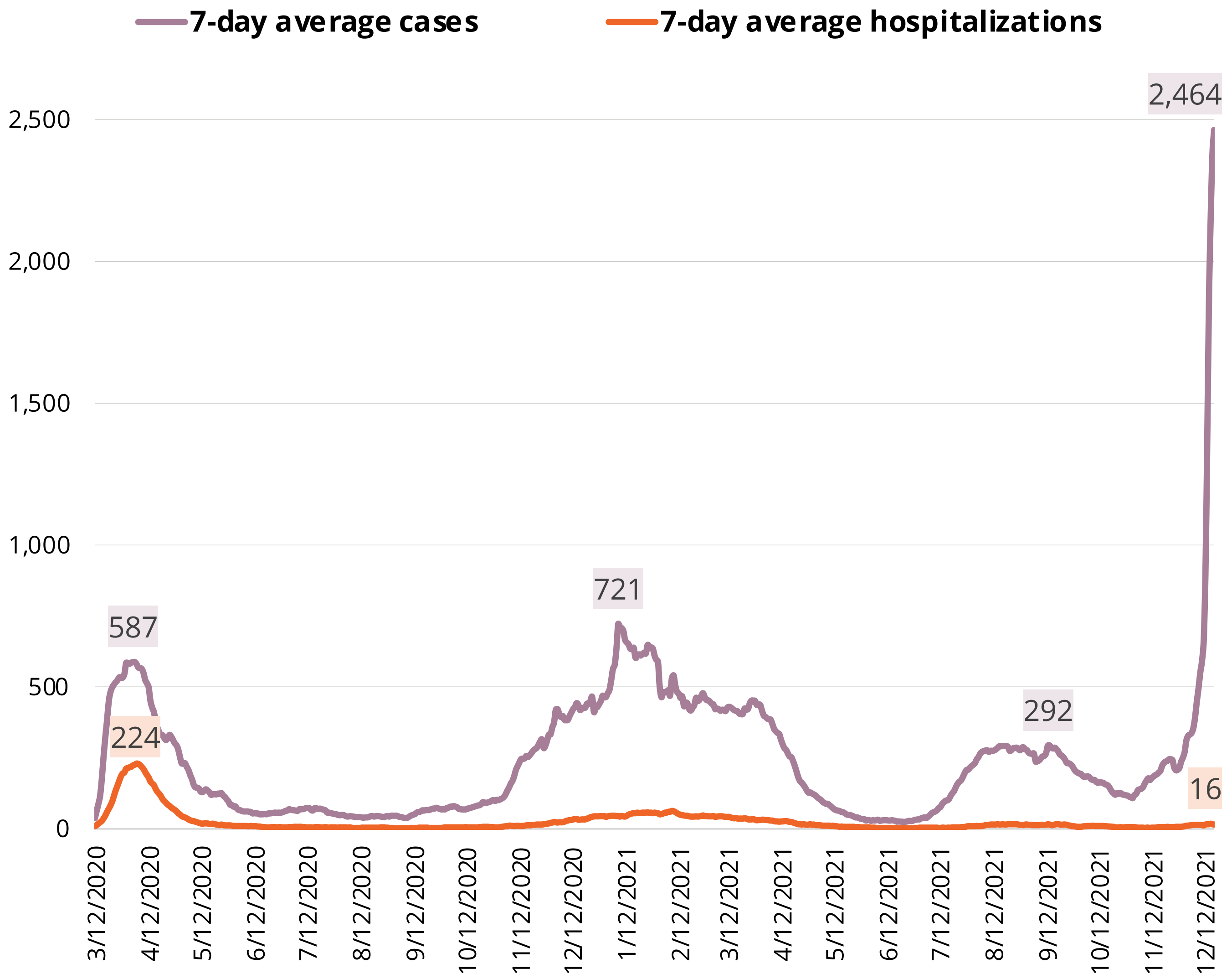
Source: Center for Disease Control

7-day COVID-19 cases vs. hospitalizations

16.4x

7-day average Manhattan COVID-19 cases, December 18 2021 vs. October 18, 2021.

COVID-19 case counts have spiked to new heights since Thanksgiving, though hospitalizations remain consistent relative to the 7-day moving averages that have been reported since mid-2020.



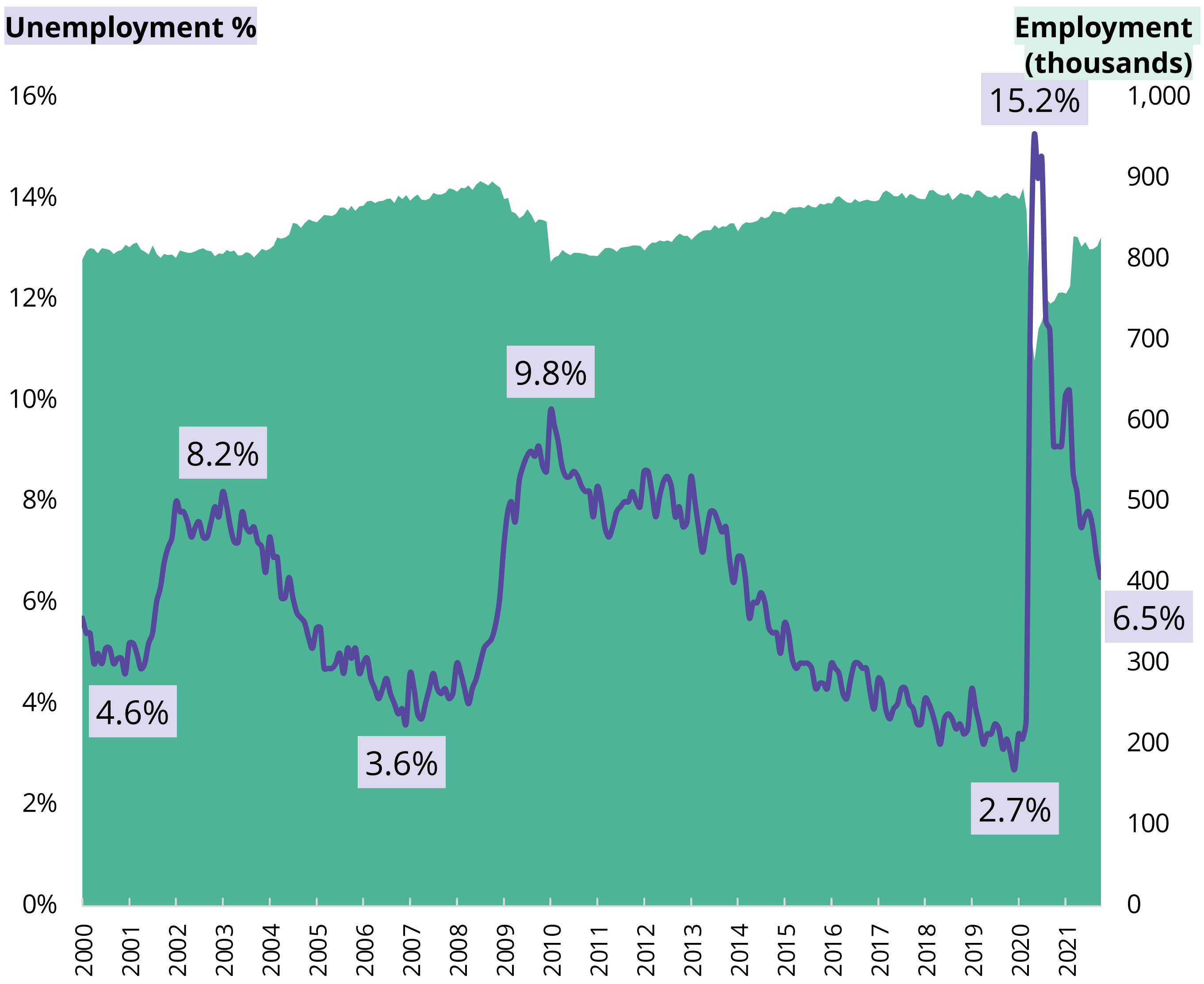
Source: NYC Department of Health and Mental Hygiene

Employment and unemployment rate

6.5%

Manhattan unemployment rate as of October 2021, approaching the 2000 to 2021 average of 6.1%.

Hiring efforts have ramped up in recent months, especially in the retail and hospitality industries, as the Manhattan economy steadily reopened since mid-2020. The unemployment rate resultantly decreased by 260 bp and the labor force increased by 10.4% from October 2020 to October 2021.



Note: Not seasonally adjusted
Source: Bureau of Labor Statistics

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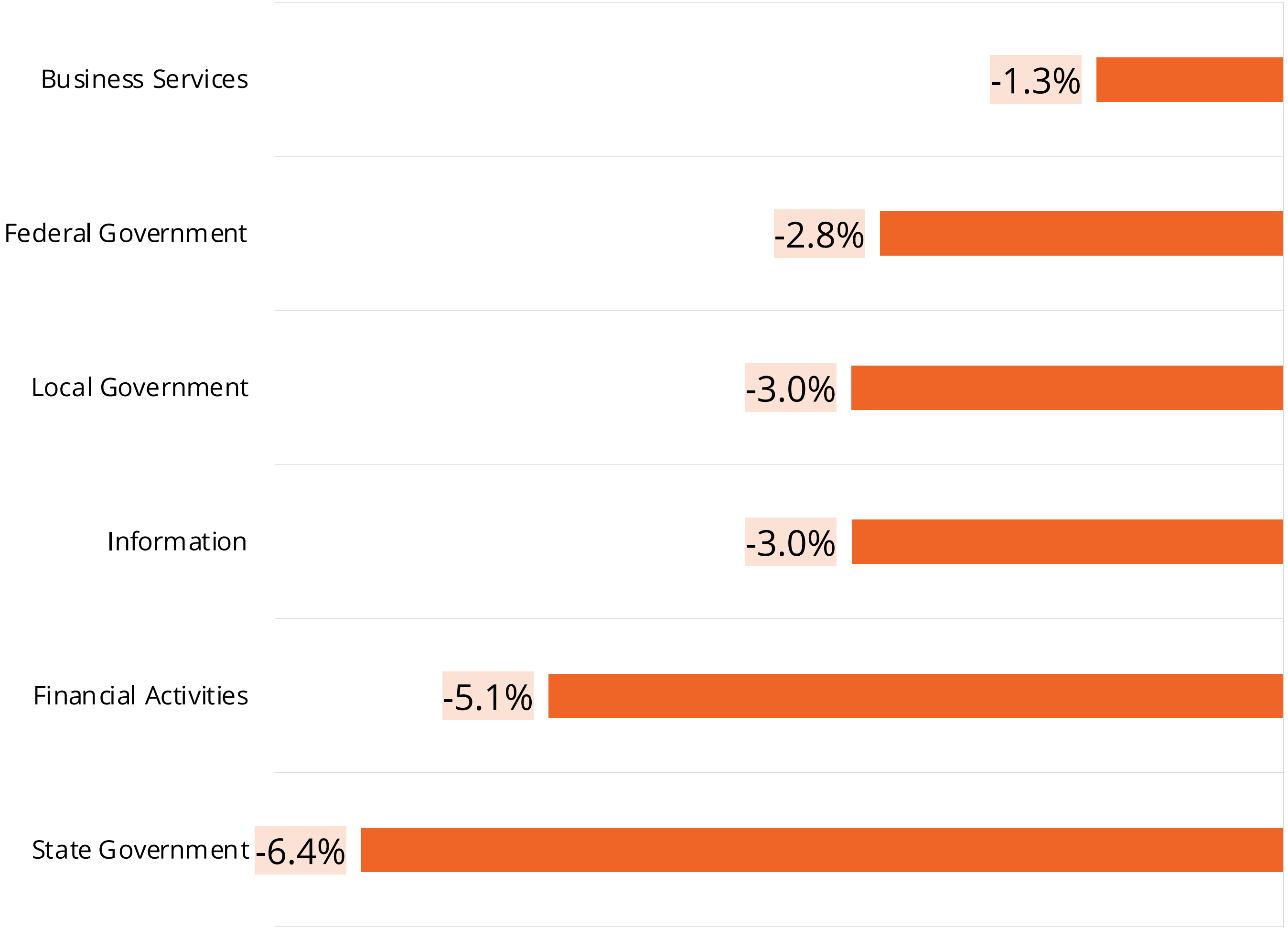
Office-using job gains and losses

-2.9%

change in office-using employment during the pandemic.

Private-sector office employment in the New York MSA decreased by 2.6% from February 2020 to October 2021, a less severe contraction compared with the 6.7% job losses in this sector reported during the Global Financial Crisis.

New York Metropolitan Statistical Area
February 2020 to October 2021



Source: Bureau of Labor Statistics

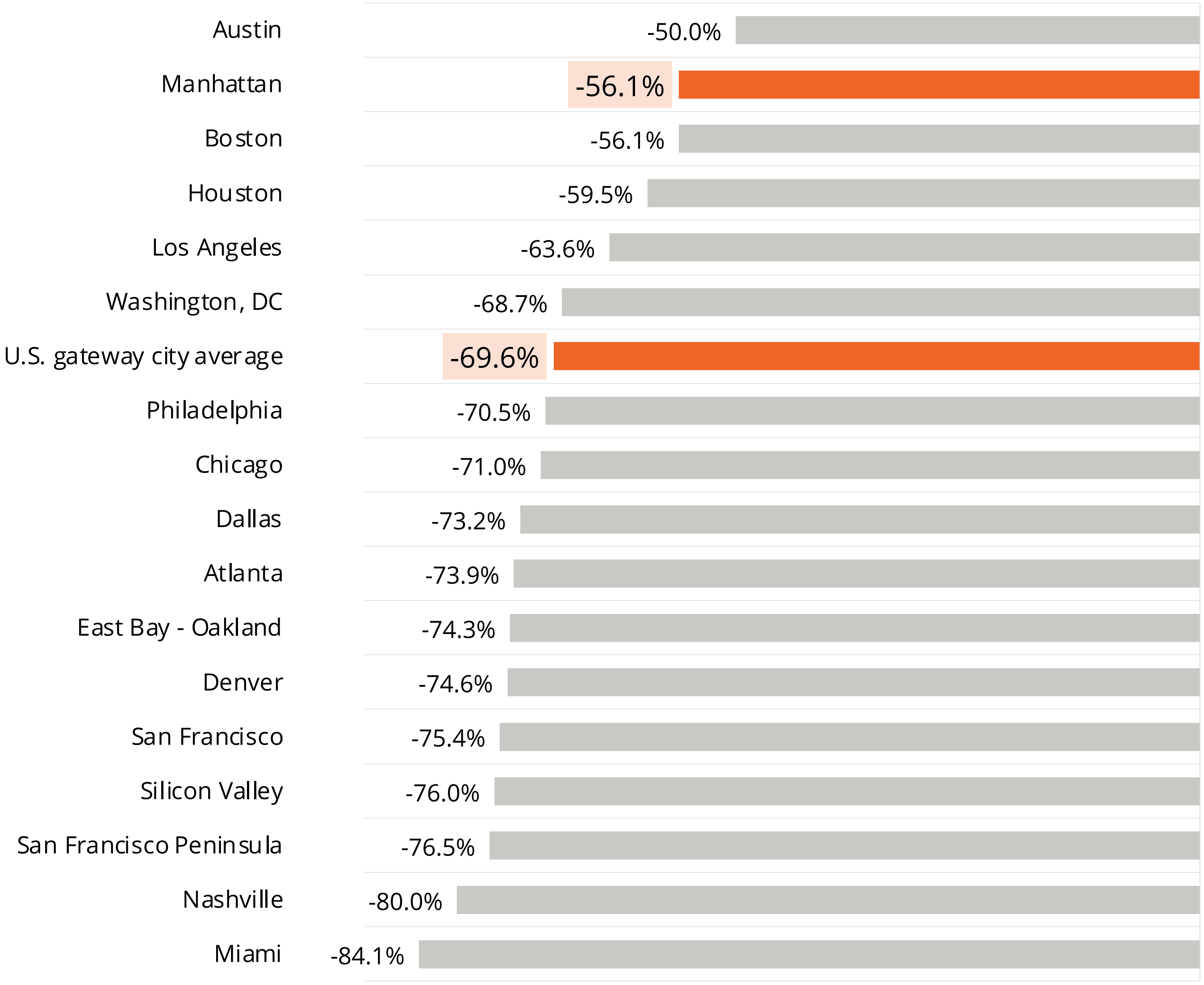
U.S. return-to-work rates since COVID

-69.6%

Office visitor volumes, week of December 13, 2021 vs. week of December 15, 2019.

Office visitor volumes have generally risen in recent months, particularly after Memorial Day and after Labor Day, but remain considerably lower than pre-pandemic levels. The next major litmus test for return-to-office efforts will be January 2022.

View vitality index



Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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U.S. return-to-work rates since COVID

-71.1%

Tech office visitor volumes, week of December 13, 2021 vs. week of December 15, 2019.

Competitive labor market conditions and some employees' productivity outside of the office have caused many tech companies to adopt hybrid or remote work strategies.

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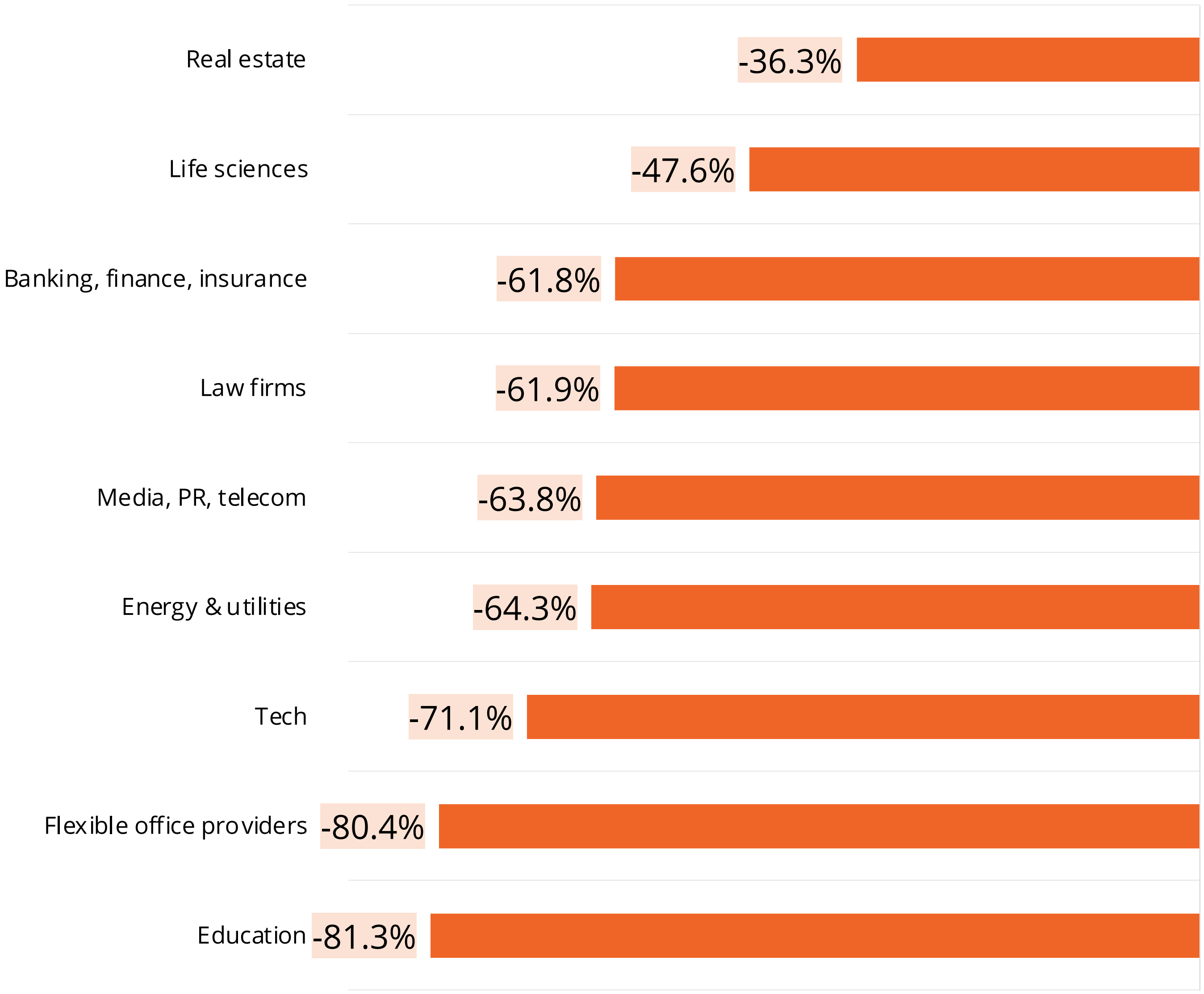

Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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Manhattan visitor volumes

-25.6%

Week of December 16, 2019 vs. week of December 13, 2021

Education (+7.3%), healthcare (-8.5%) and government (-10.7%) locations have effectually returned to pre-COVID visitor volumes; however, office (-51.7%) and hospitality (-45.5%) locations have struggled to return to pre-COVID normalcy.

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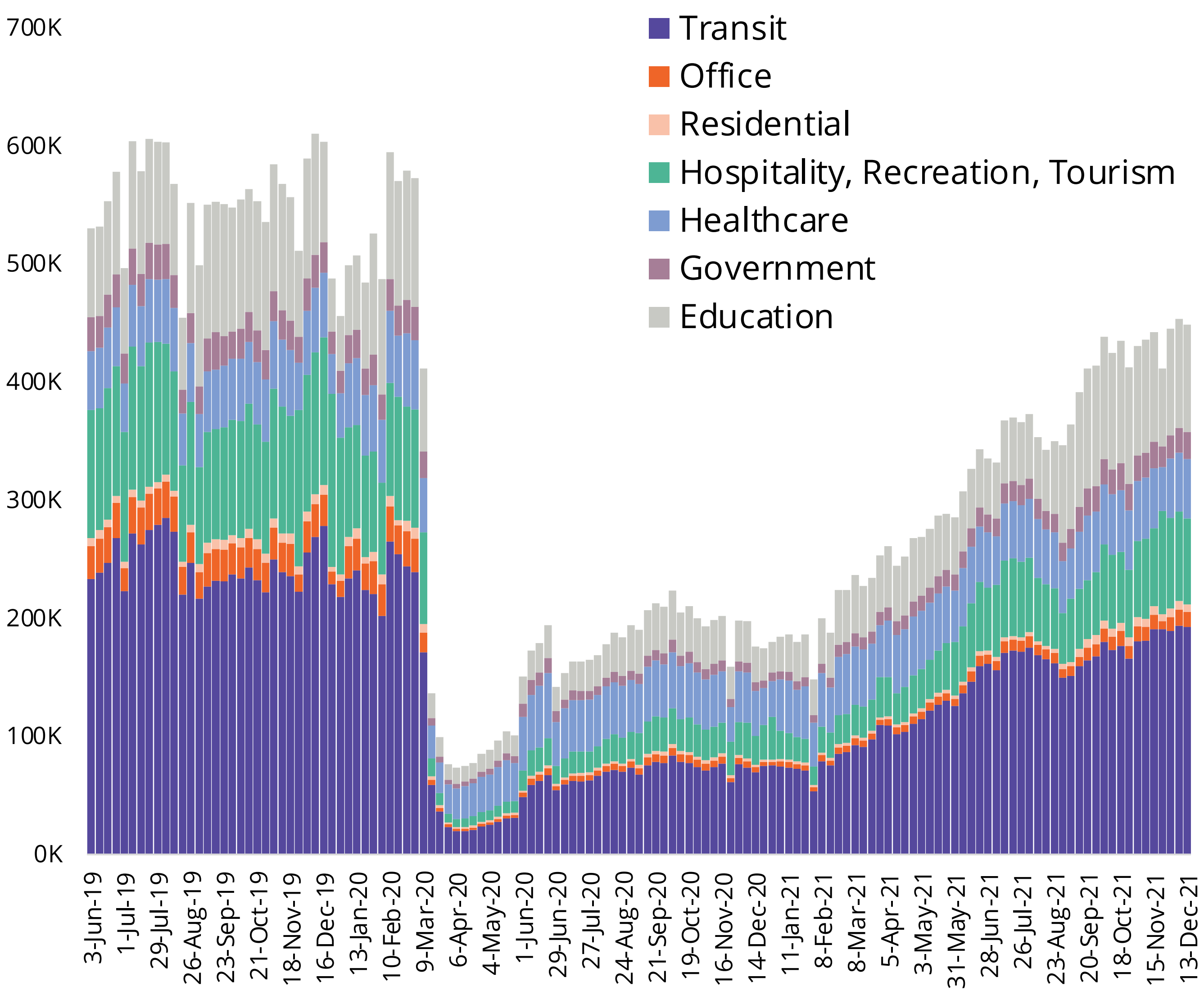

Note: Representative areas of interest. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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Manhattan office visitor volumes

-51.7%

Week of December 16, 2019 vs. week of December 13, 2021

Return-to-office efforts have gained momentum in recent months. Visitor volumes are +19.7% versus the week of September 20, 2021—after Labor Day and religious holidays—and +8.9% versus the week after Thanksgiving.

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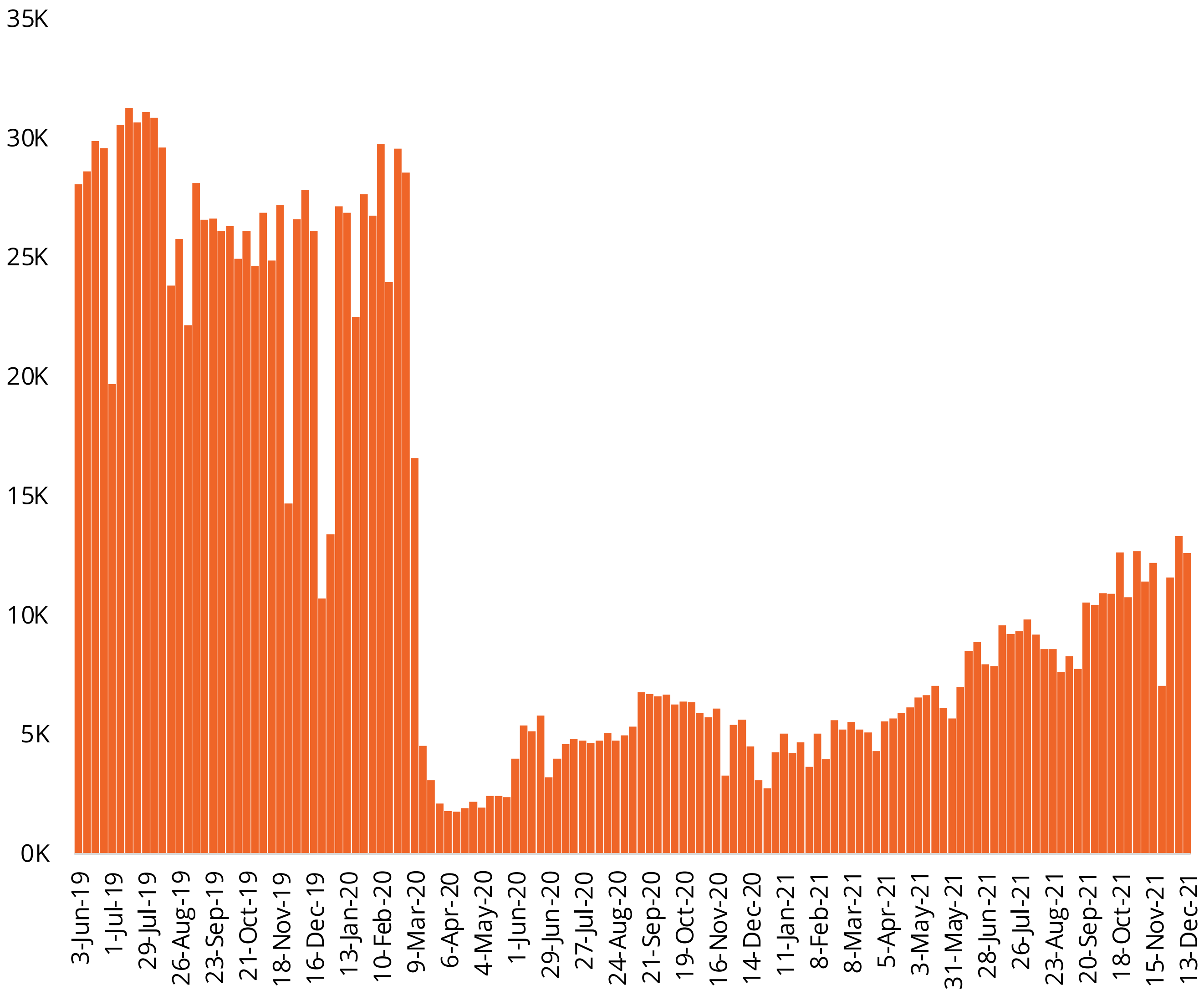

Note: Representative areas of interest. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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Local return to work efforts by industry

-36.6%

Banking and finance office visitor volume vs. week of December 16, 2019

Manhattan financial services firms have adopted hybrid work strategies, though creative companies and law firms have adopted comparatively remote work strategies.

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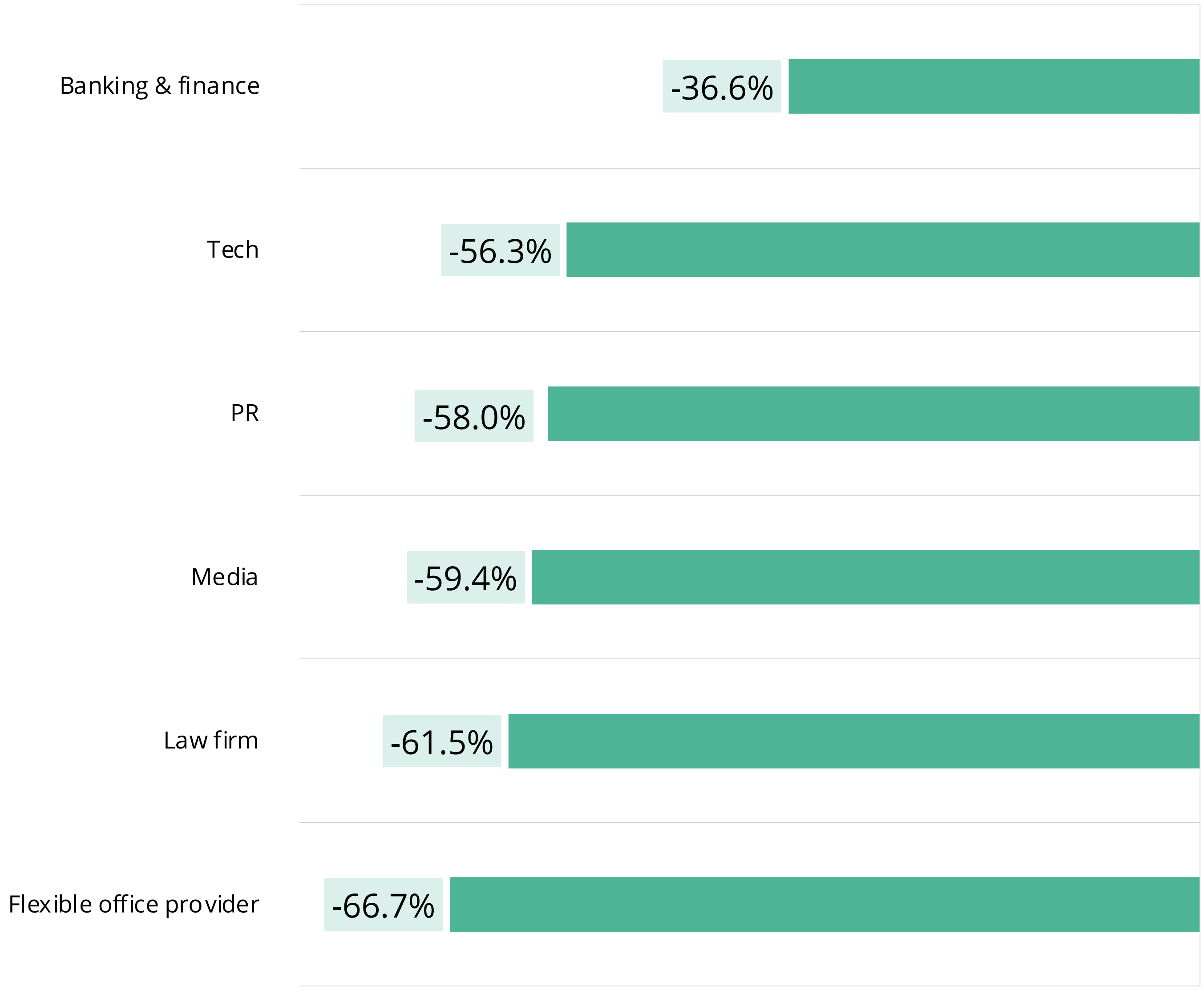

Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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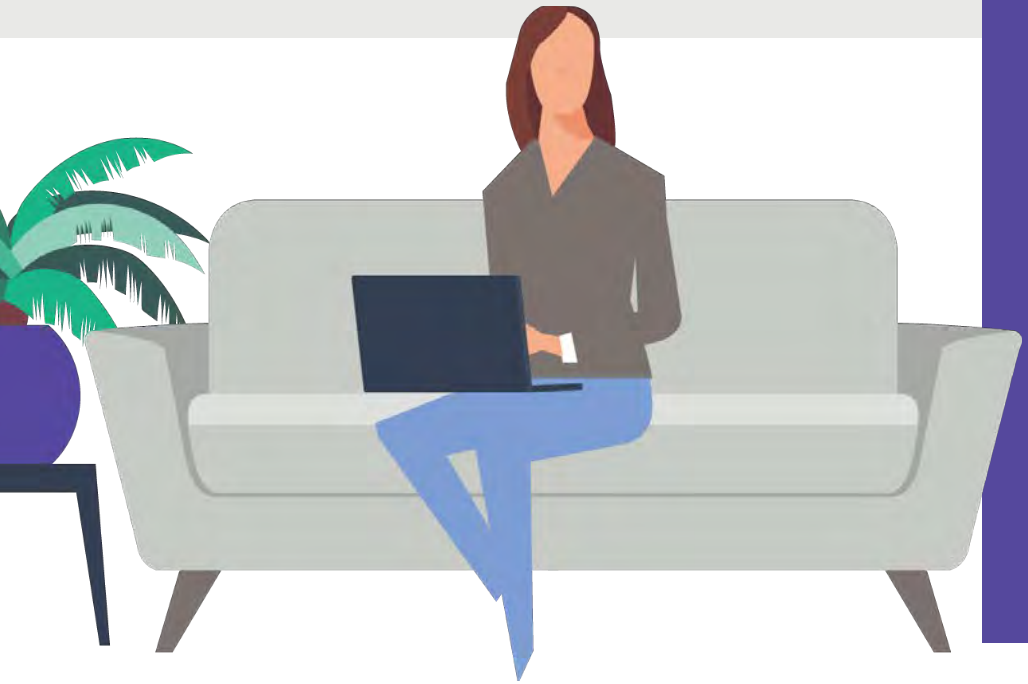
Return-to-office survey

A recent survey conducted before the onset of the Omicron variant concluded that most Manhattan employees had not returned to the office in October, though nearly half had expected to return to the office in early 2022.



28%

of Manhattan office workers had returned as of October 2021

49%

of Manhattan office workers had expected to return by the end of January 2022

Source: Partnership for New York City (November 2021)

Let's look at office occupier market conditions

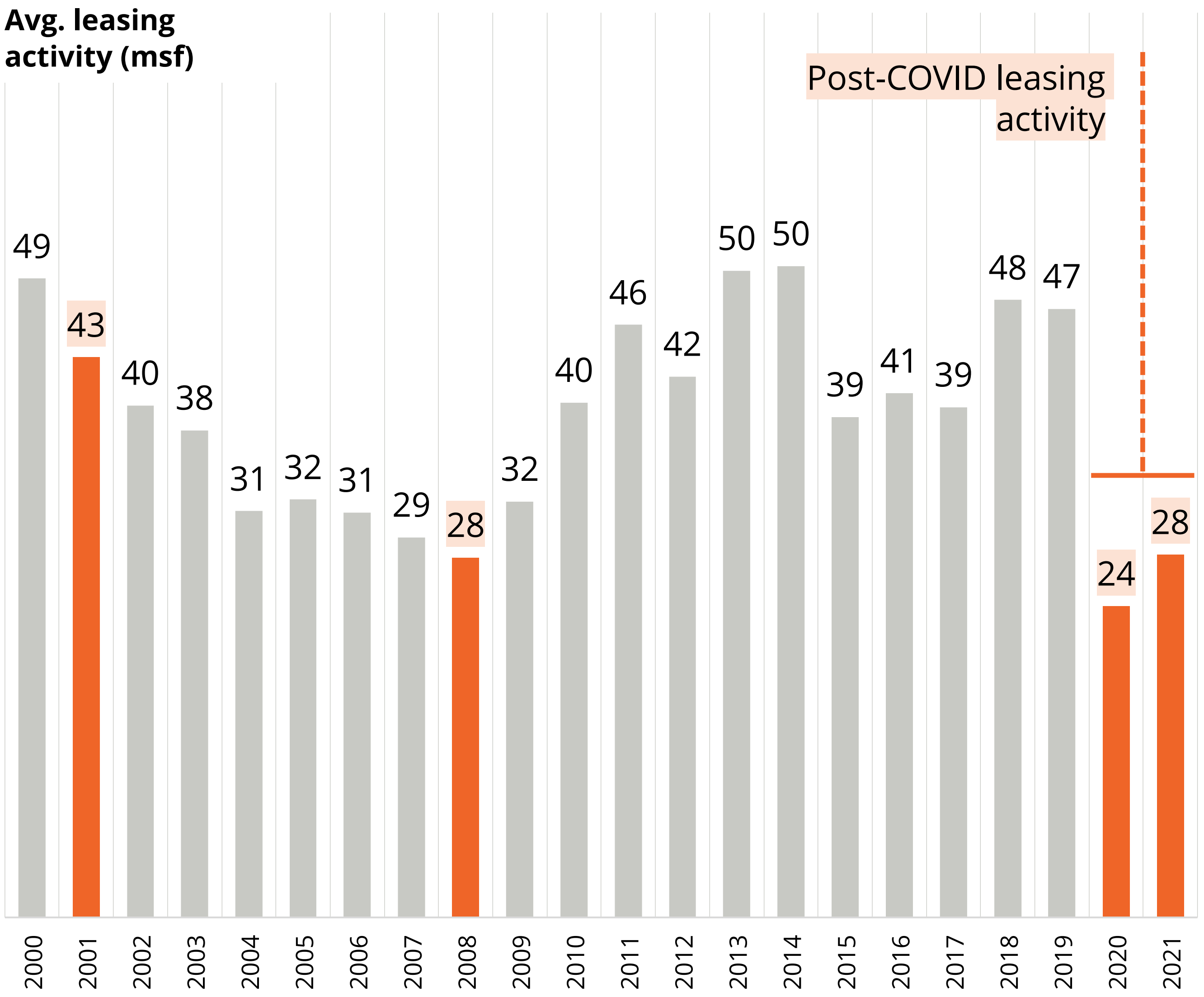
The 'tale of two markets' persisted in 2021, with demand concentrated on transit-oriented Trophy properties while commodity offerings comparatively struggled.

Office leasing activity

-32.4%

2021 vs. prior 20-year annual average leasing activity.

Leasing activity rebounded in recent months as tenants that had postponed their real estate decisions more willingly signed long-term commitments. The latest six-month period of leasing activity of 16.8 msf was the most active six-month period since Q4 2019 to Q1 2020 (24.3 msf). The 2021 leasing activity of 28.1 msf surpassed the 2008 leasing activity of 27.8 msf, a 16.6% year-over-year increase.



Source: CoStar

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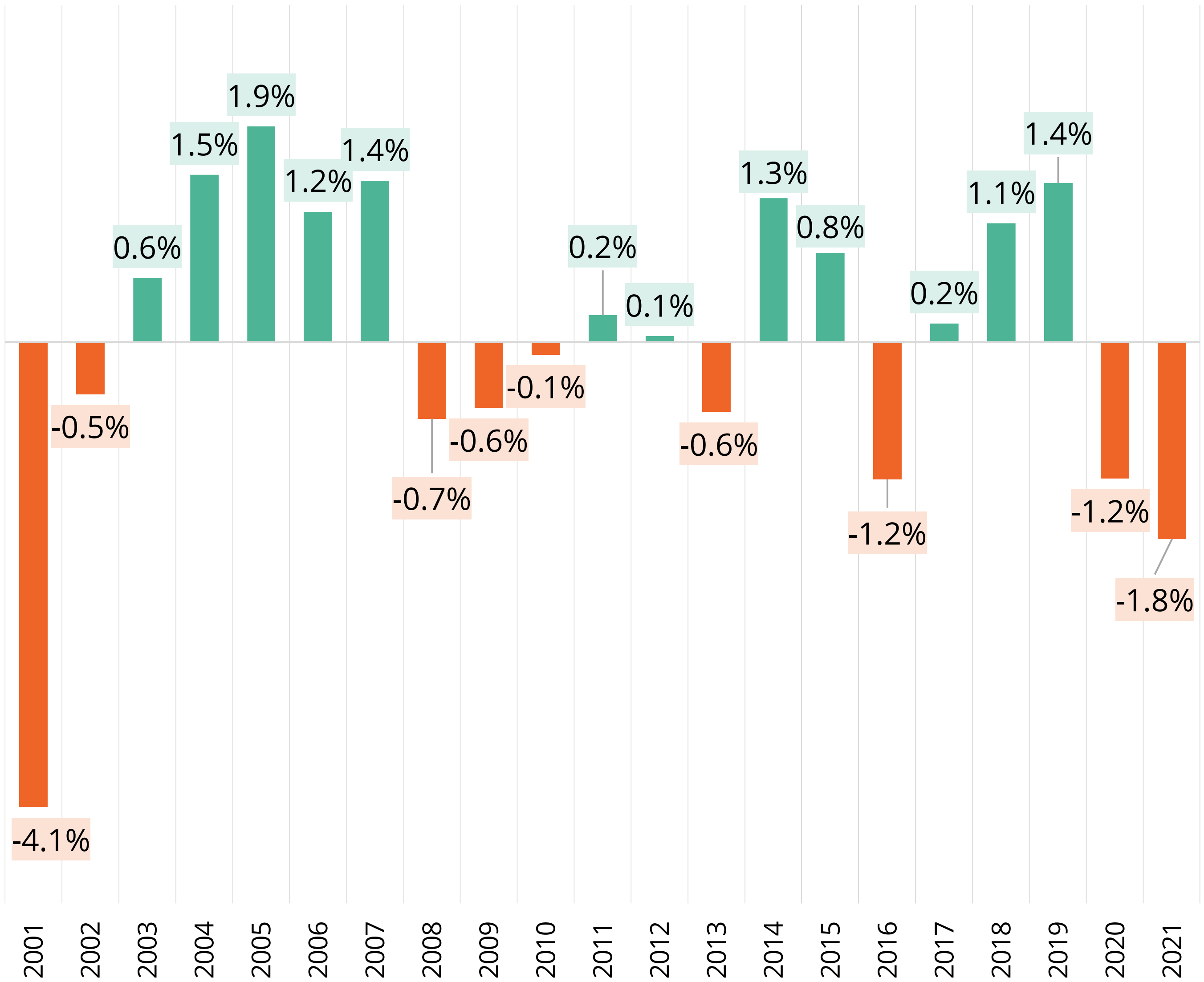
Absorption as a share of inventory

-3.0%

net absorption as a percentage of inventory, 2020 through 2021.

Negative absorption persisted in 2021, despite a bounce-back in demand relative to 2020 levels. Net absorption totaled -5.9 msf in 2020 and -8.6 msf in 2021, the weakest period of net absorption since 2001.



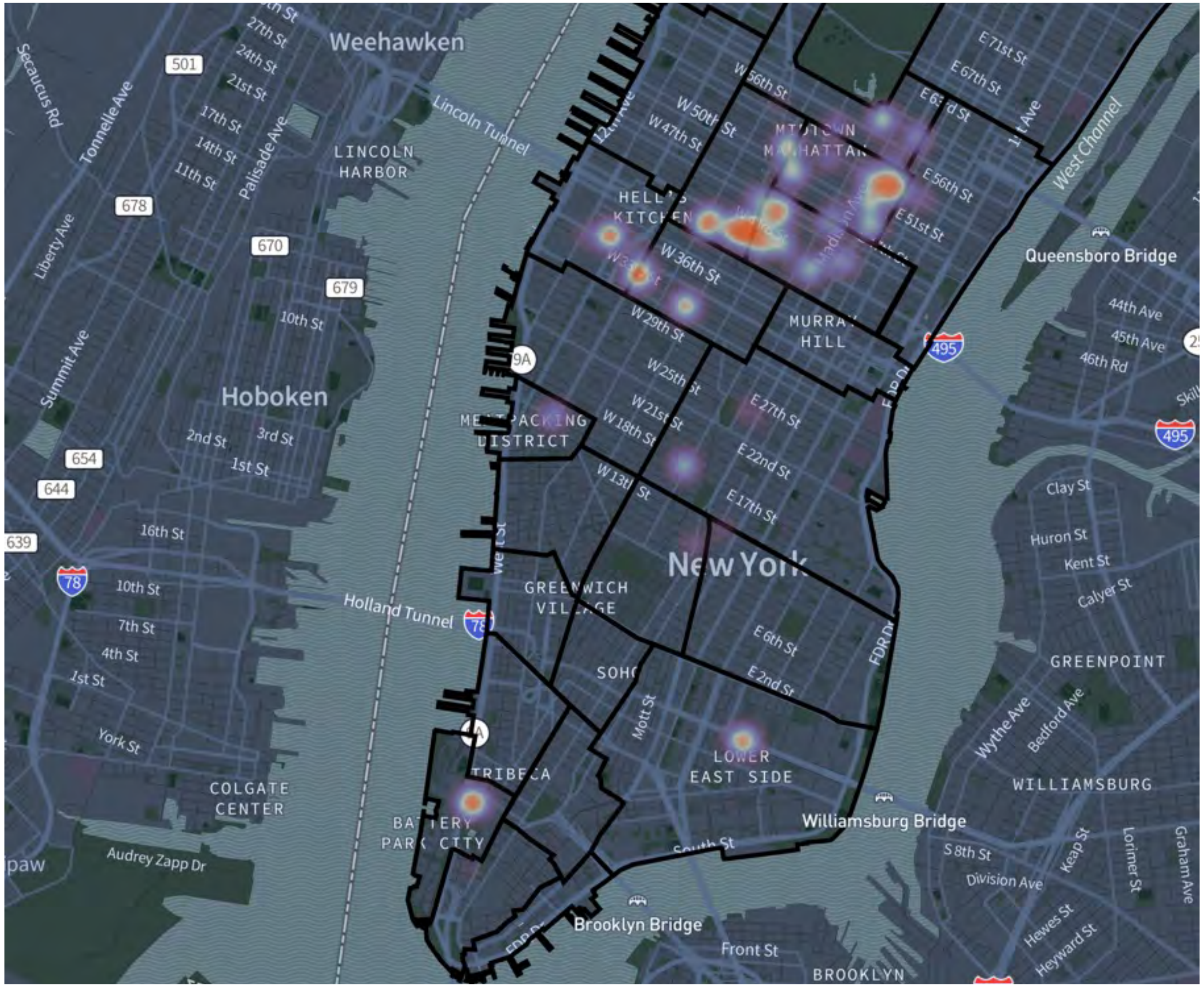
Source: CoStar

Heat map of post-COVID Trophy leases

40.9%

Trophy properties' share of post-COVID leasing activity by number of leases.

The Trophy sector has accounted for 40.9% of leasing activity in terms of the number of leases signed since April 2020 despite comprising just the top 10.0% of the market in terms of the number of properties. Offices that are situated near transit hubs such as Grand Central Terminal and Times Square have fared exceptionally well.



Note: Trophy properties represent the top 10% of the Manhattan office market in terms of rents and build date.
Source: AVANT for Avison Young

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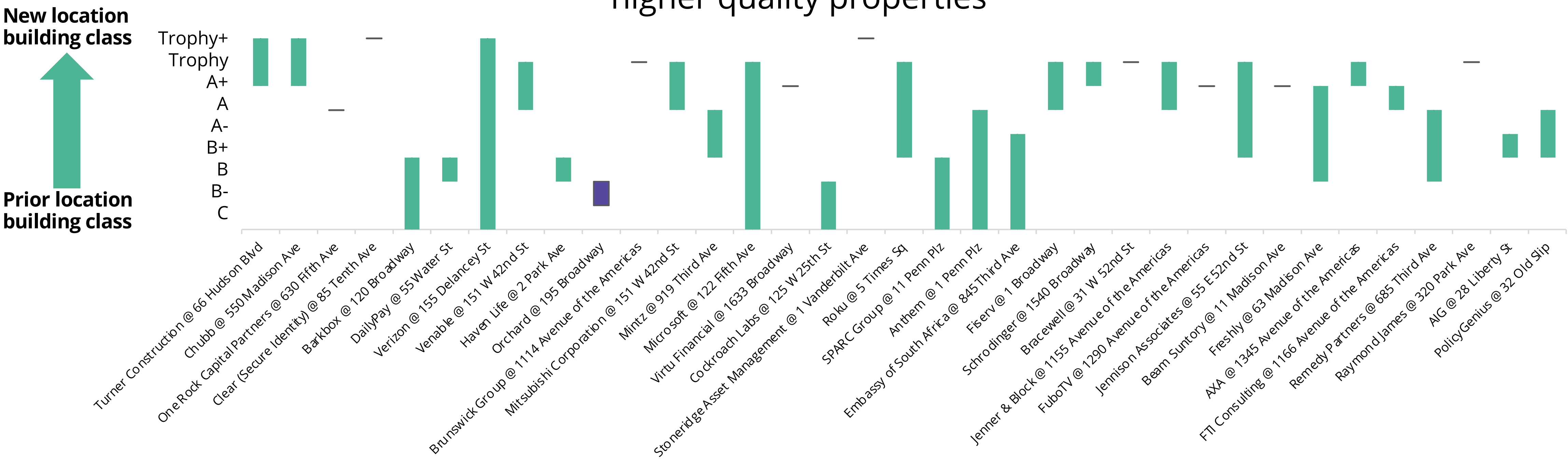
Post-COVID flight-to-quality trend

34 / 35

Relocations by 50,000-sf tenants to the same or higher quality properties



Source: AVANT by Avison Young

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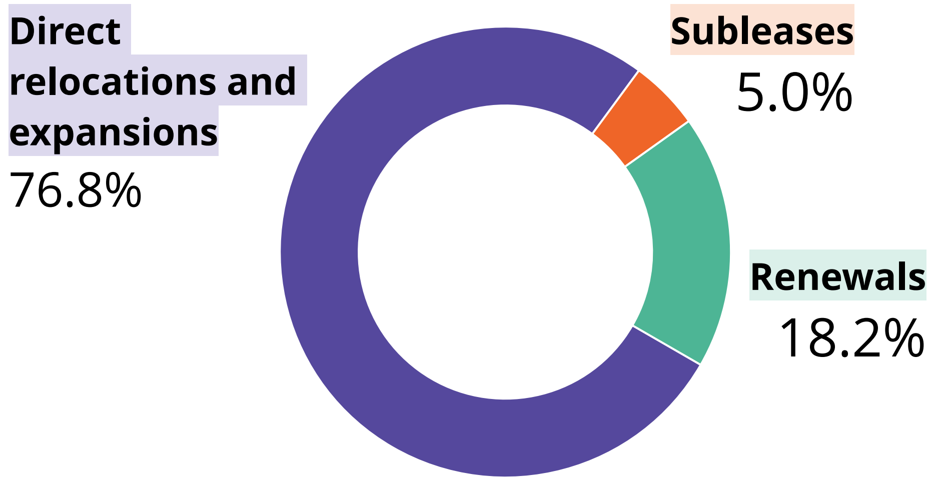
Transaction activity by lease type

-26.9%

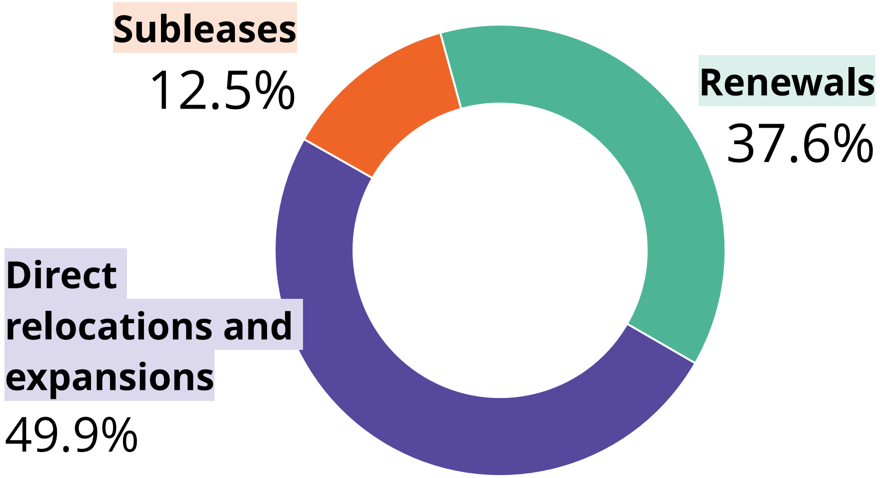
percentage point change in direct relocations, 2018 to March 2020 vs. April 2020 to December 2021.

Subleases, especially built suites, and renewals have become attractive options for tenants navigating their long-term occupancy strategies during the pandemic. The proportionate share of direct relocations and expansions has declined, though opportunistic and forward-thinking occupiers are increasingly signing long-term commitments as the supply of high-quality options declines and tenant leverage persists in many market segments.

From 2018 through March 2020



From April 2020 through December 2021



Source: AVANT by Avison Young

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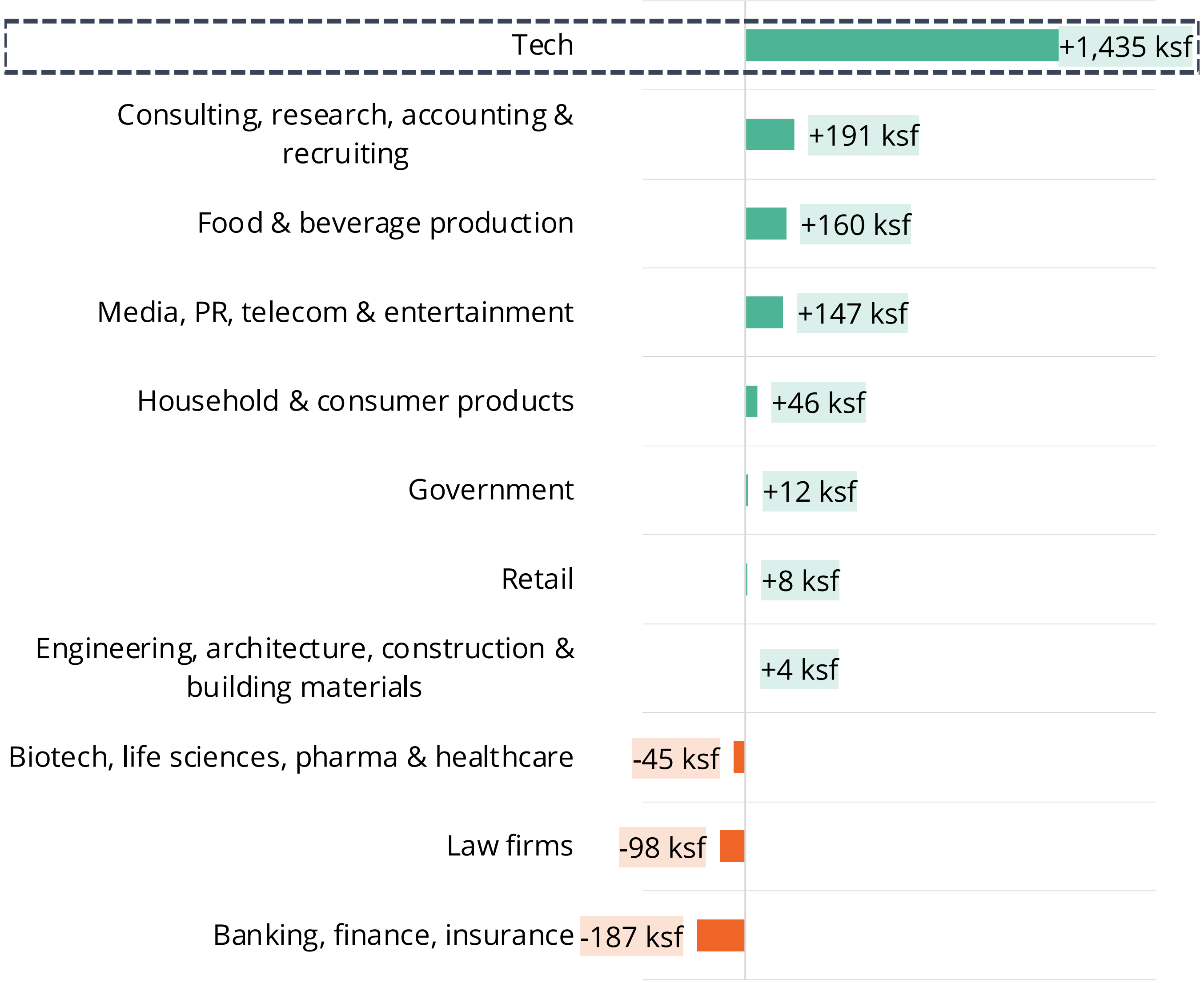
Industry expansions and contractions

+1.4 msf

net absorption by tech companies, April 2020 to December 2021.

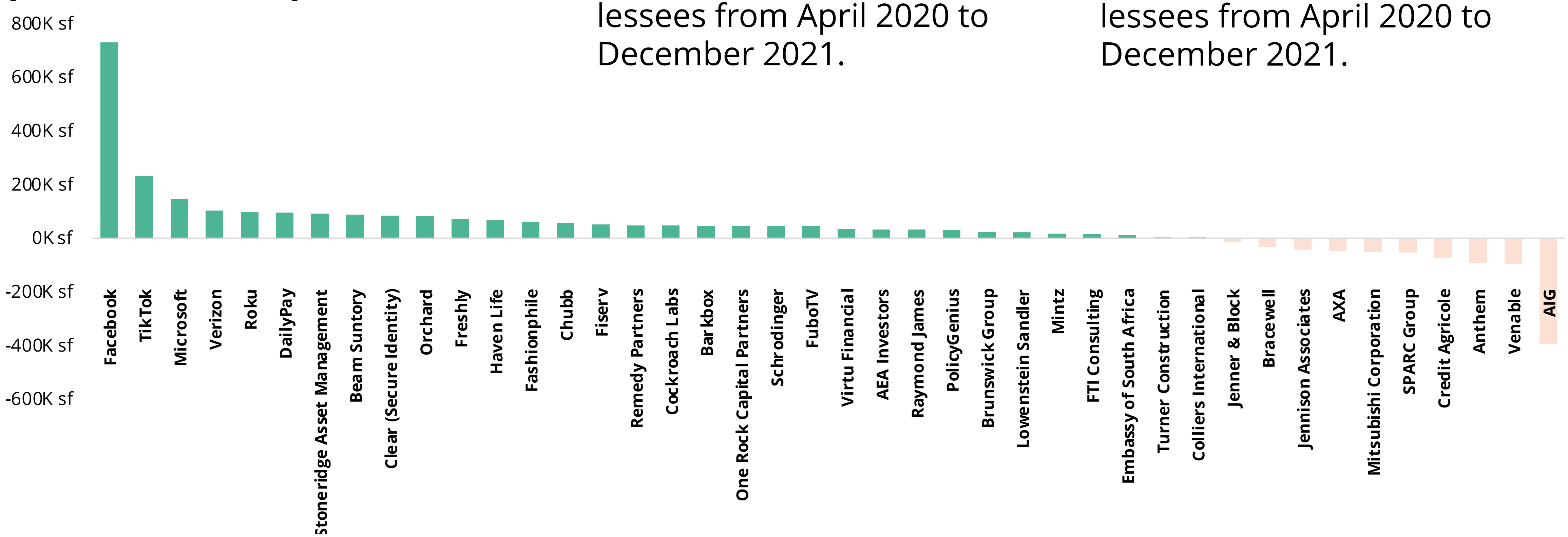
Tech companies have continued to expand their presences in Manhattan, recognizing the city's long-term draw for talent. Conversely, mainstay banking, finance and insurance companies and law firms have consolidated their Manhattan footprints since April 2020.



Note: 50,000+ sf leases only
Source: AVANT by Avison Young

AVANT by AVISON YOUNG

Major post-COVID expansions/ (contractions)



2.6 msf

expansions by 50,000-sf lessees from April 2020 to December 2021.

-890 ksf

contractions by 50,000-sf lessees from April 2020 to December 2021.

Note: 50,000+ sf leases only
Source: AVANT by Avison Young

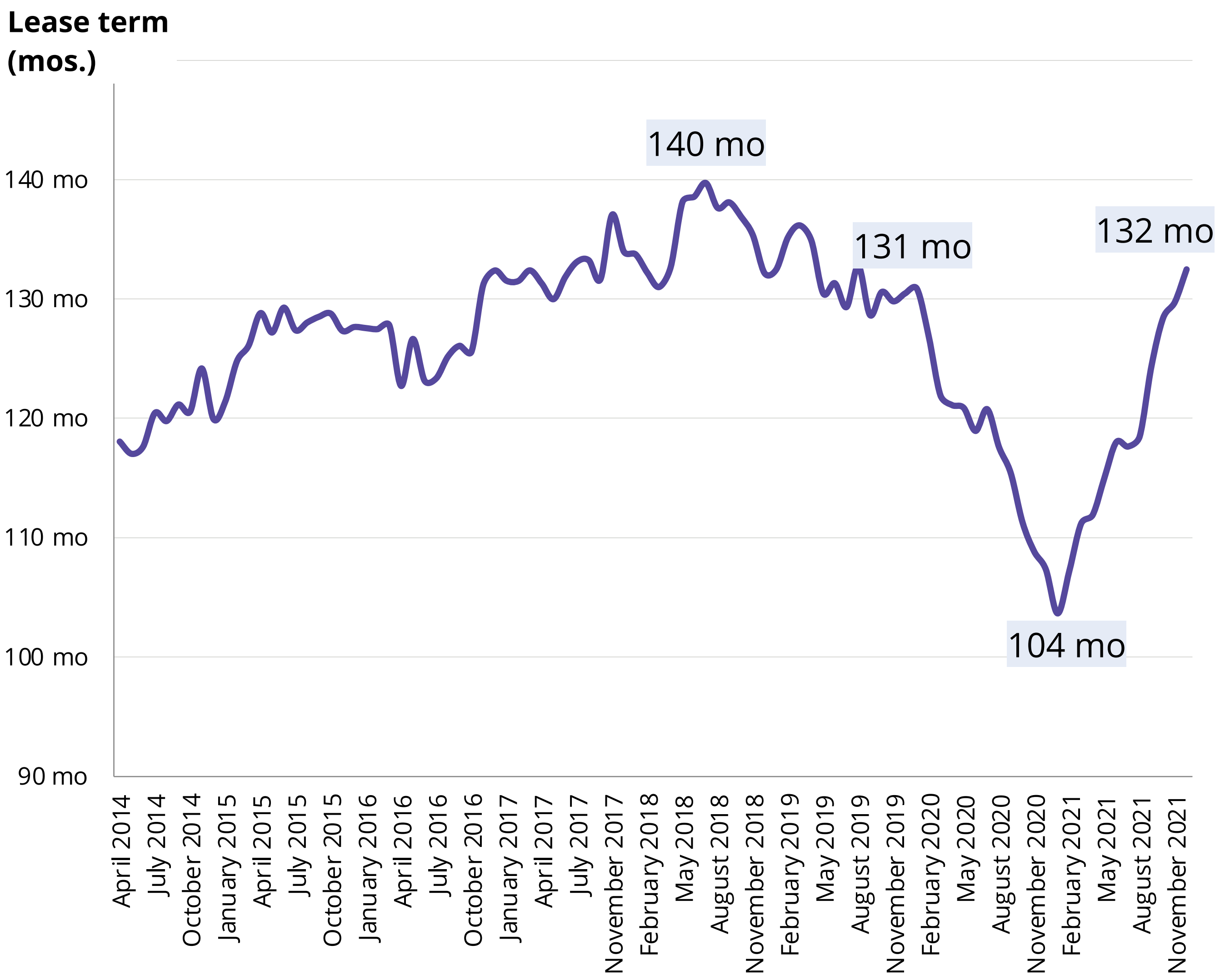
AVANT by AVISON YOUNG

Trophy average lease term

132 mo

current 12-month moving average lease term length for Trophy properties.

Landlords that operate Trophy-quality properties, especially transit-oriented offices, are mandating tenants to make long-term lease commitments due to a growing supply-and-demand imbalance. Lease term lengths at these exclusive properties are now on par with pre-COVID averages.



Note: Includes all lease types. Trophy properties represent the top 10% of the Manhattan office market in terms of rents and build date.
Source: AVANT by Avison Young

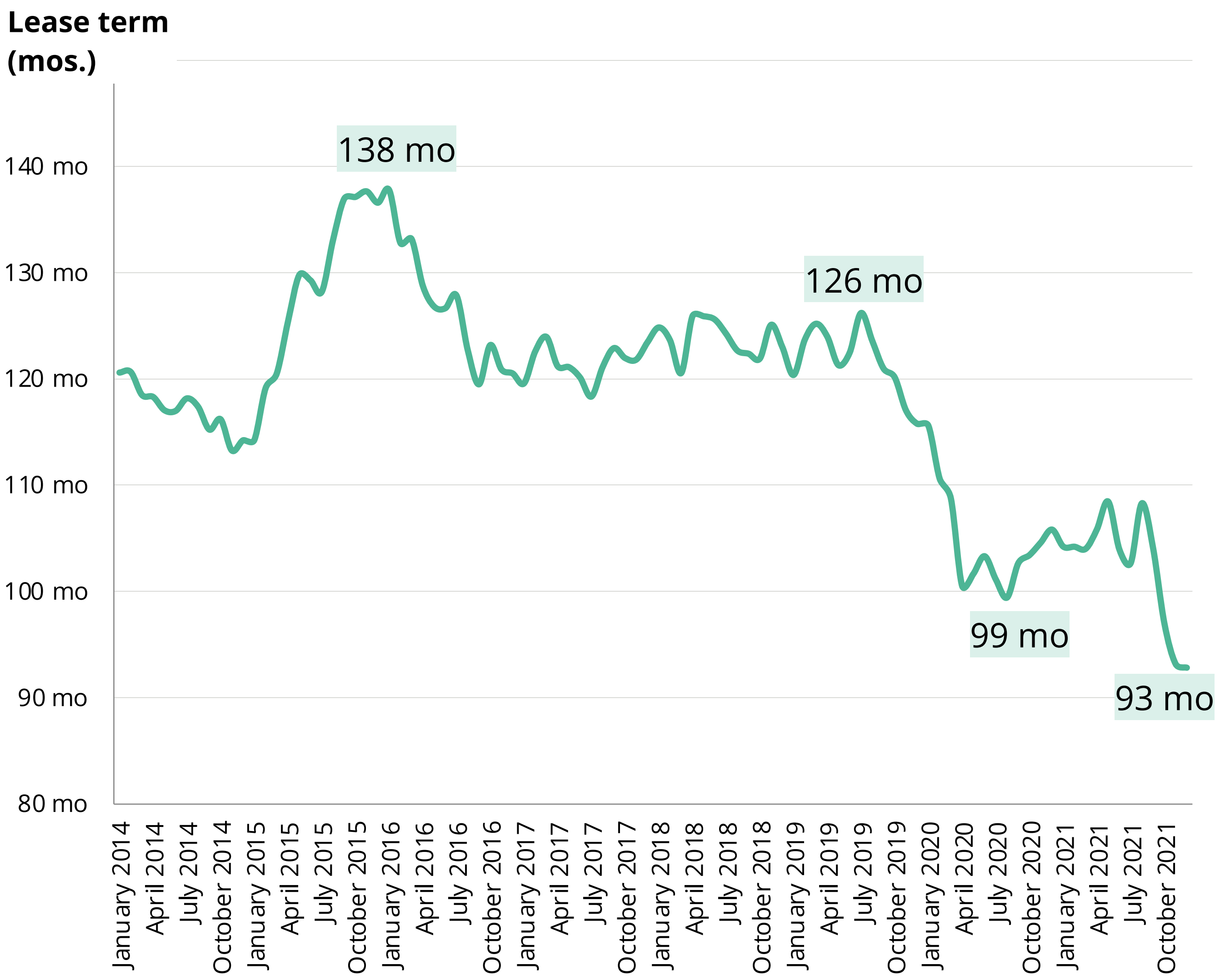
AVANT by AVISON YOUNG

Class A average lease term

93 mo

current 12-month moving average lease term length for Class A properties.

Lease term lengths are at a post-pandemic low, highlighting tenants' continued negotiating leverage in this market segment. The average lease term length as of December 2021 was -33.4 mo or -26.5% compared with the July 2019 average.



Note: Includes all lease types. Class A properties represent the top 25% but not the top 10% of the Manhattan office market in terms of rents and build date.
Source: AVANT by Avison Young

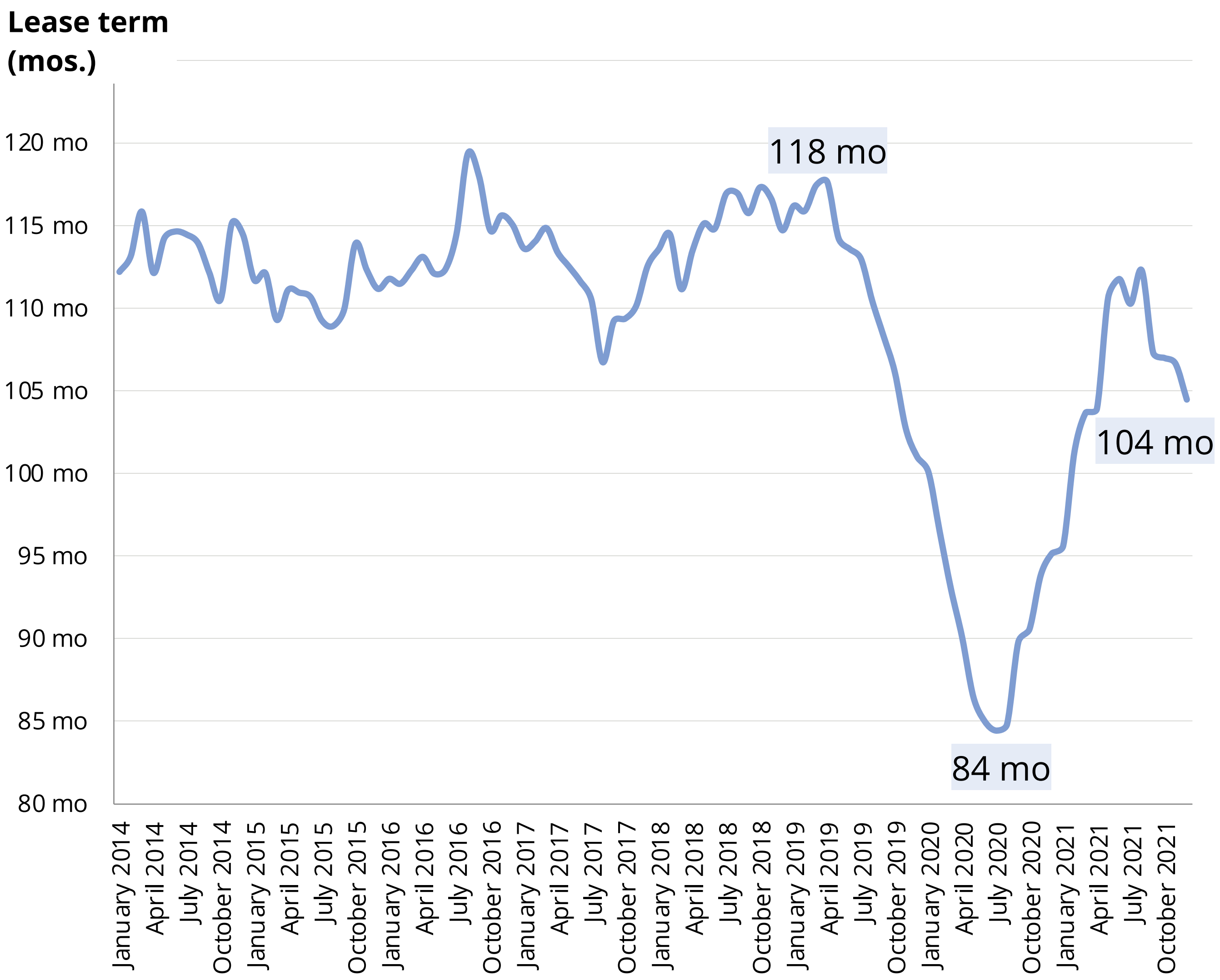
AVANT by AVISON YOUNG

Class B and Class C average lease term

104 mo

current 12-month moving average lease term length for Class B and Class C properties.

Lease term lengths in the commodity sector have decreased in recent months after recovering from a low of just 84 months in July 2020, the greatest term length compression of any market classification given the prevailing supply-and-demand imbalance that favors tenants.



Note: Includes all lease types
Source: AVANT by Avison Young

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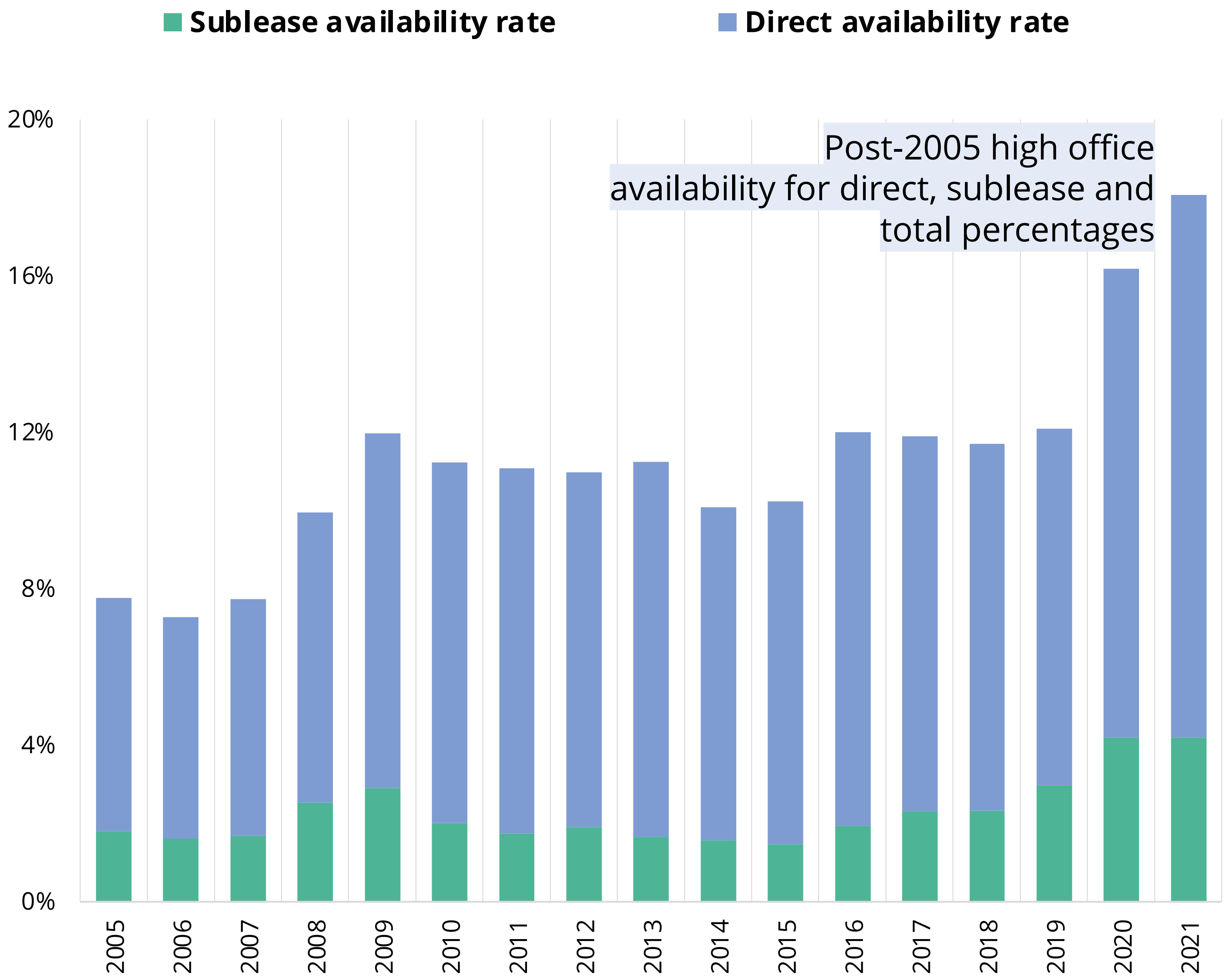
Office market availability rate

18.1%

total availability rate as of Q4 2021, down from 18.2% as of Q3 2021.

Strengthened demand partially offset new availabilities from Q3 to Q4, with sublease availabilities decreasing 20 bp to 4.4% but direct availabilities increasing 10 bp to 13.9%. The direct availability rate represents a post-2005 year-end high, while the sublease availability rate equals the year-end 2020 peak. The Q4 2021 Trophy total availability rate of 13.0% represents a 70 bp decrease from 2020 levels.



Source: CoStar

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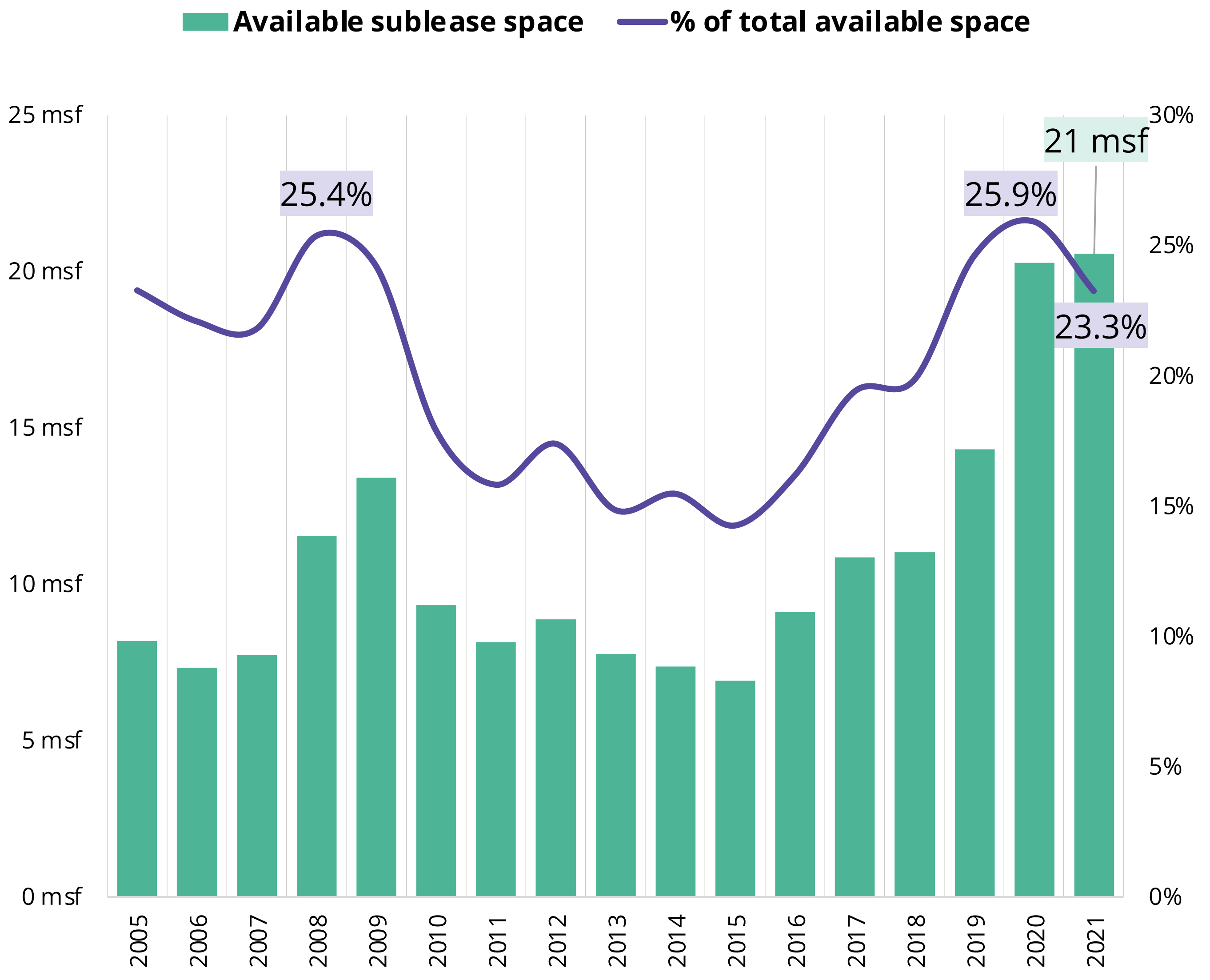
Available sublease space

20.6 msf

post-2005 record levels of available sublease space in Manhattan.

The share of sublease-to-total available space of 23.3% has declined from 25.9% as of year-end 2020, however, and this ratio is lower than Global Financial Crisis levels.



Source: CoStar

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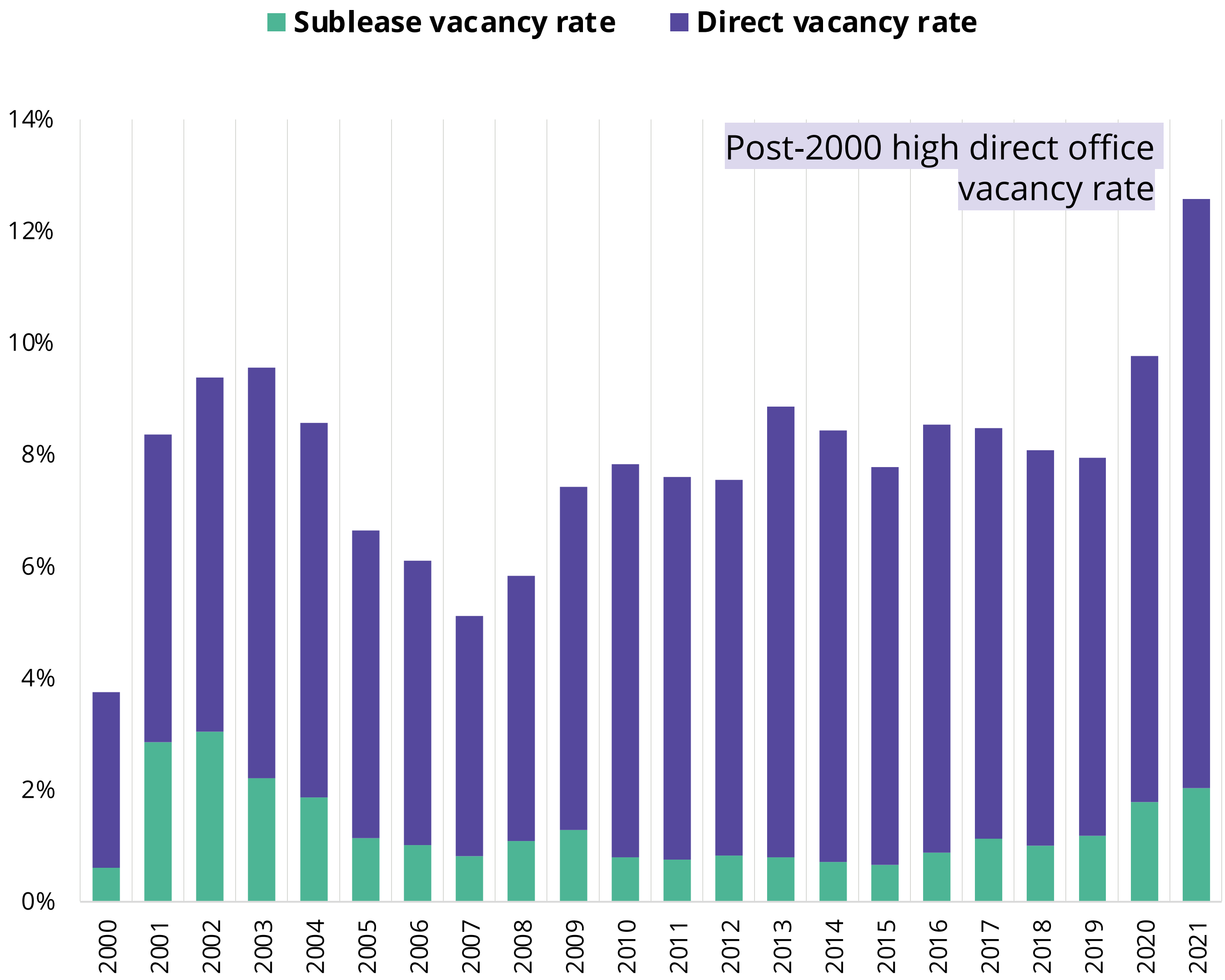
Office market vacancy rate

12.6%

post-2000 high Manhattan office total vacancy rate as of Q4 2021.

At 10.6%, the direct vacancy rate in 2021 reached a post-2000 peak. However, the sublease vacancy rate of 2.0% remained lower than 2001 (2.9%) and 2002 (3.0%) levels, which were reported during the Dot-com recession and amidst a flurry of relocations out of Downtown Manhattan after 9/11.

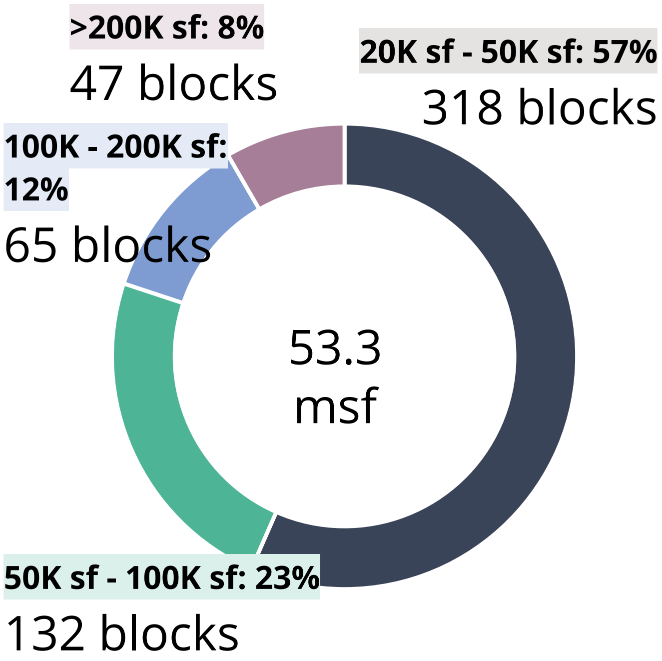


Source: CoStar

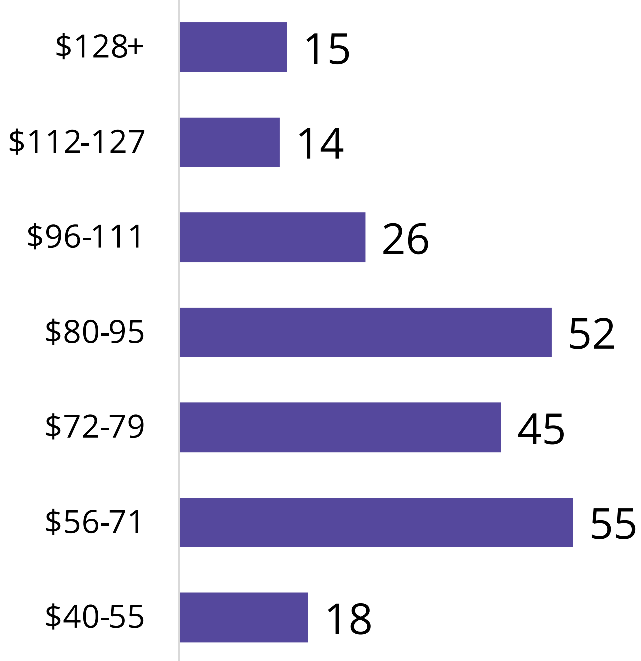
AVANT by AVISON YOUNG

Office large-block availabilities

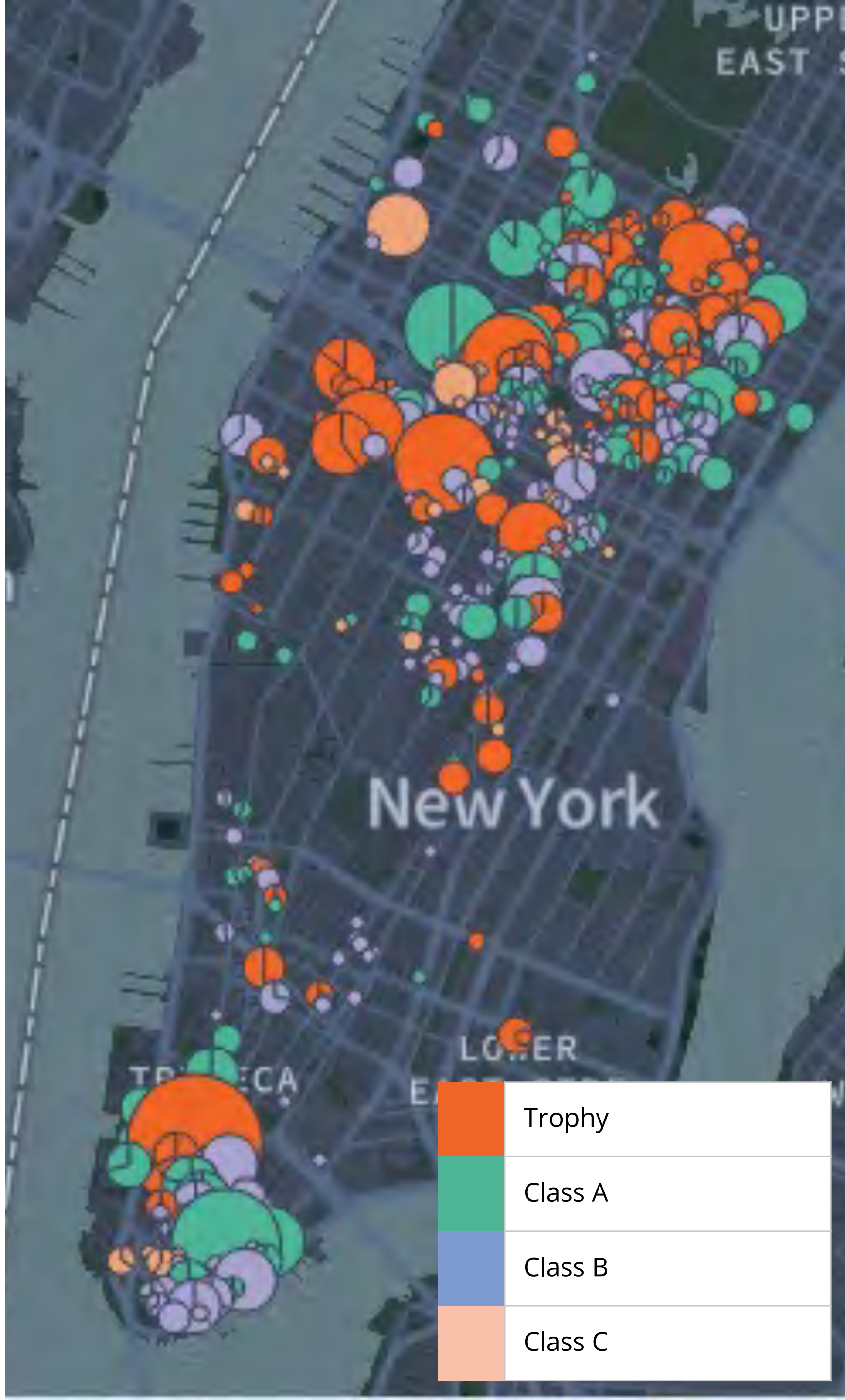
Number of blocks



Asking rents*



Note: 20,000+ sf blocks. Asking rents for some blocks are undisclosed.
Source: CoStar, AVANT by Avison Young

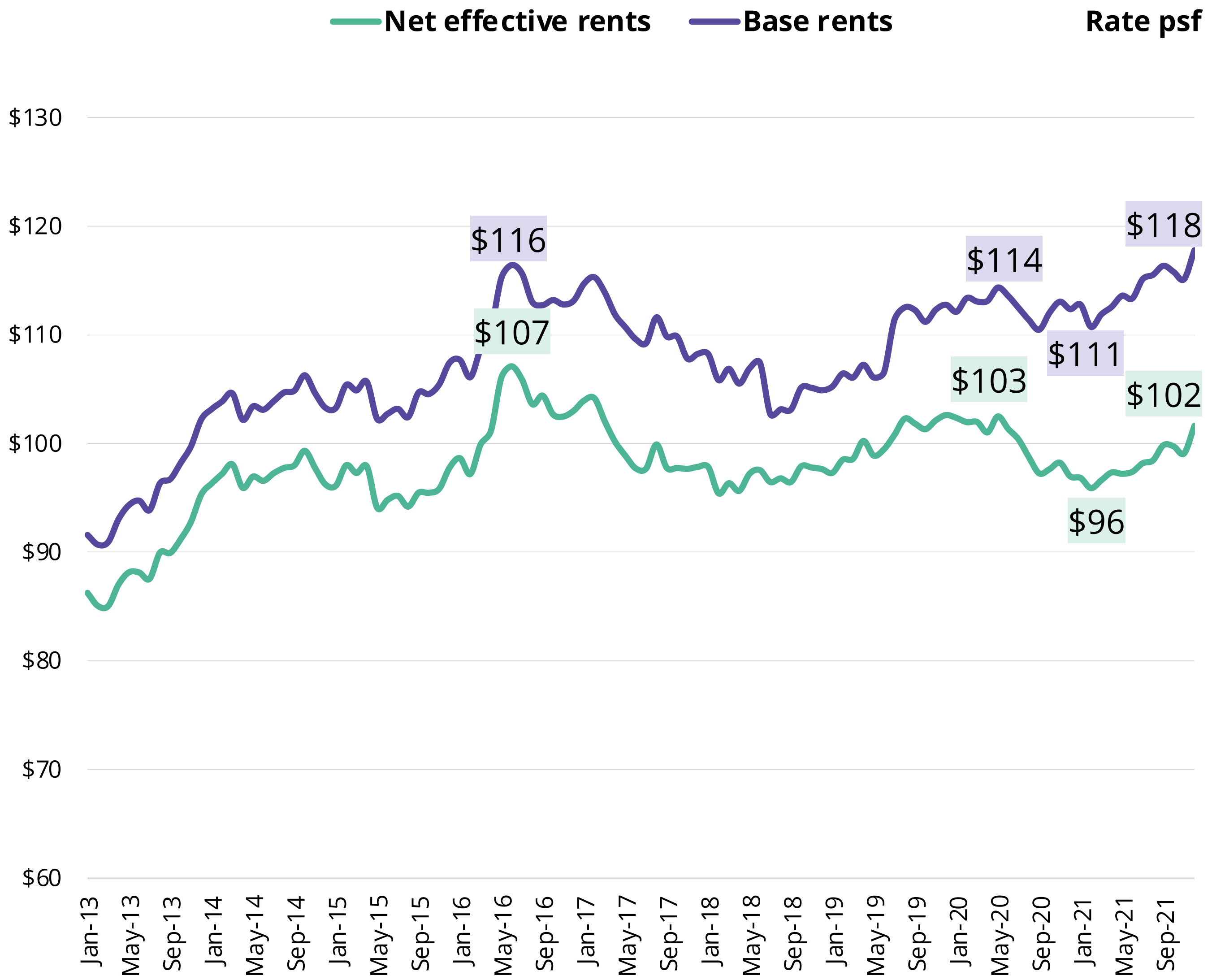


Trophy net effective rents and base rents

-1.0%

December 2019 vs. December 2021 Trophy direct relocation net effective rents.

Trophy base rents have climbed to all-time highs and net effective rents have increased by 6.0% from the post-COVID low in February 2021, underscoring how demand has accelerated for top-of-market properties.



Note: Direct relocations only. Trophy properties represent the top 10% of the Manhattan office market in terms of rents and build date.
Source: AVANT by Avison Young

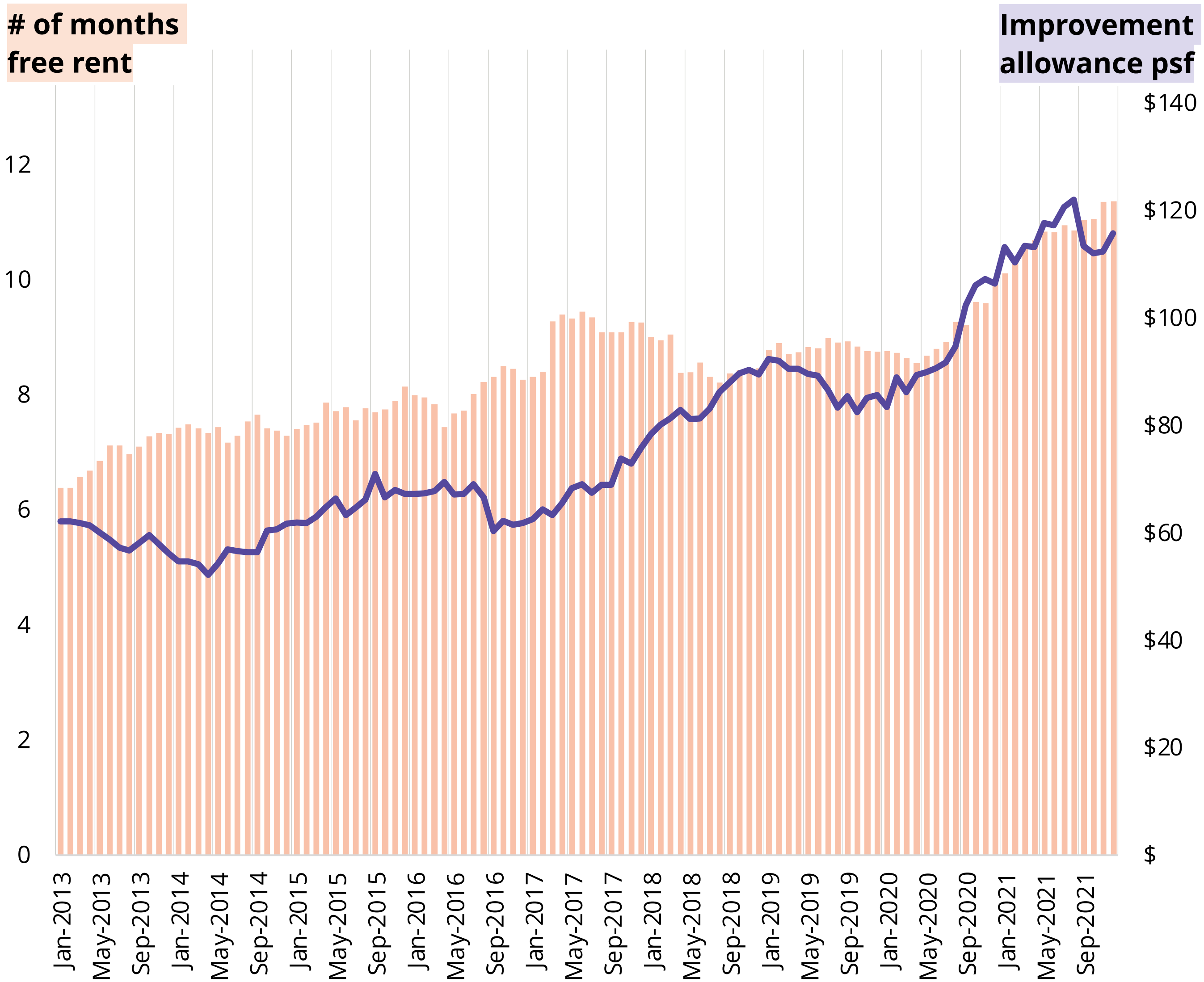
AVANT by AVISON YOUNG

Trophy office concessions packages

+8.8%

year-over-year increase in tenant improvement allowances for Trophy direct relocations.

Trophy tenant improvement allowances are tellingly 12.4% lower than Class A tenant improvement allowances, partly demonstrating the dislocation in performance between these segments of the office market. Trophy free rent periods have continued to rise, however, reaching a new record high of 11.4 months in December 2021.



Note: Direct relocations only. Normalized to 10-year lease terms. Trophy properties represent the top 10% of the Manhattan office market in terms of rents and build date.
Source: AVANT by Avison Young

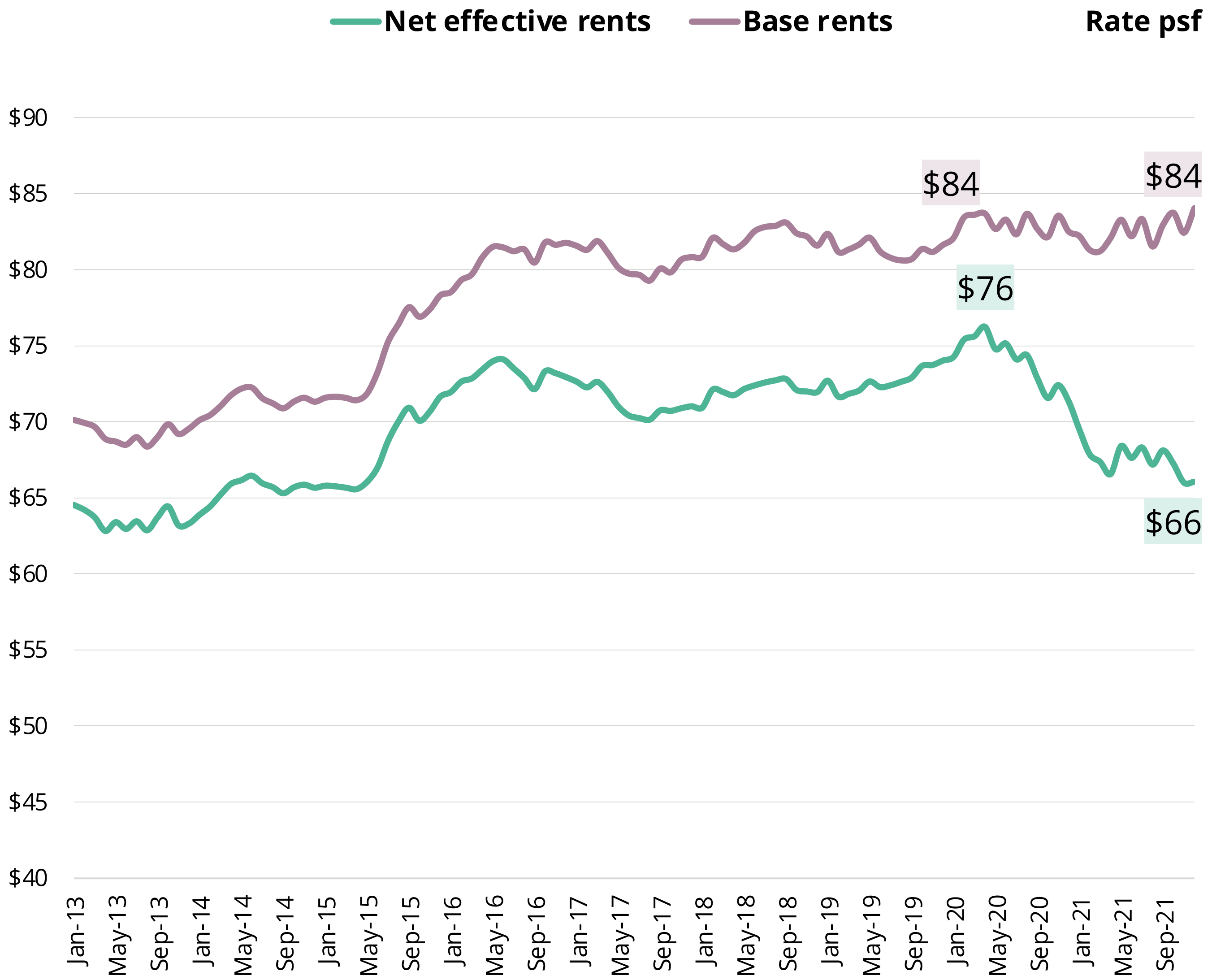
AVANT by AVISON YOUNG

Class A net effective rents and base rents

-13.4%

peak to December 2021 Class A direct relocation net effective rents.

Landlords have largely upheld base rents, which have stabilized at near-record levels throughout the pandemic; however, record levels of concessions packages have been offered to induce tenant commitments, causing net effective rents to soften.



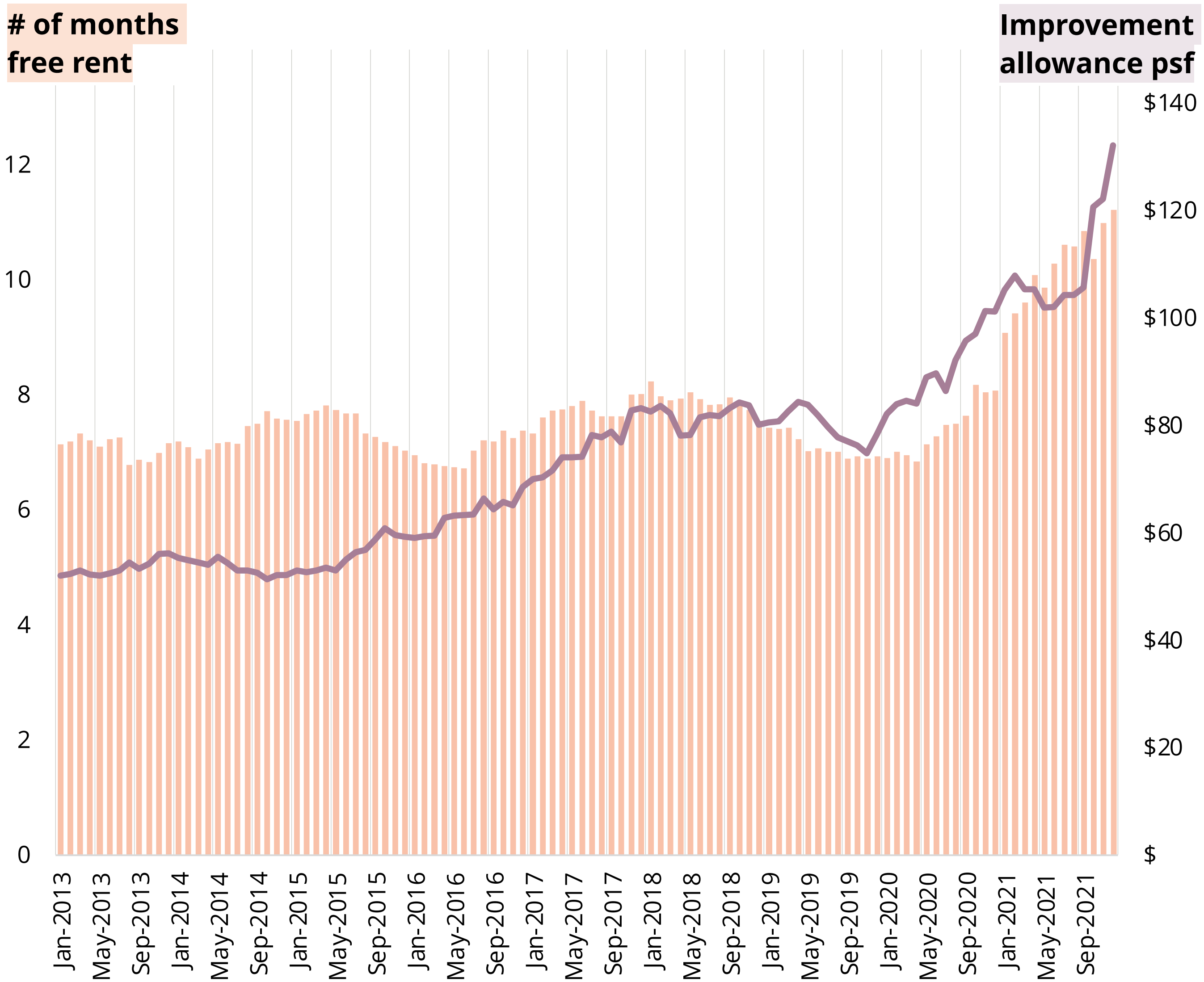
Note: Direct relocations only. Class A properties represent the top 25% but not the top 10% of the Manhattan office market in terms of rents and build date.
Source: AVANT by Avison Young

Class A office concessions packages

+30.5%

year-over-year increase in tenant improvement allowances for Class A direct relocations.

Free rent periods (11.2 months) and tenant improvement allowances ($132.17 psf) are both at record highs when normalizing for 10-year lease terms. Landlords continue to offer generous concessions packages to remain competitive in an environment with heightened levels of available space and increasing, albeit still tepid by historical standards, demand.



Note: Direct relocations only. Normalized to 10-year lease terms. Class A properties represent the top 25% but not the top 10% of the Manhattan office market in terms of rents and build date.
Source: AVANT by Avison Young

AVANT by AVISON YOUNG

Office development pipeline

42 properties

proposed, under construction

34.2 msf

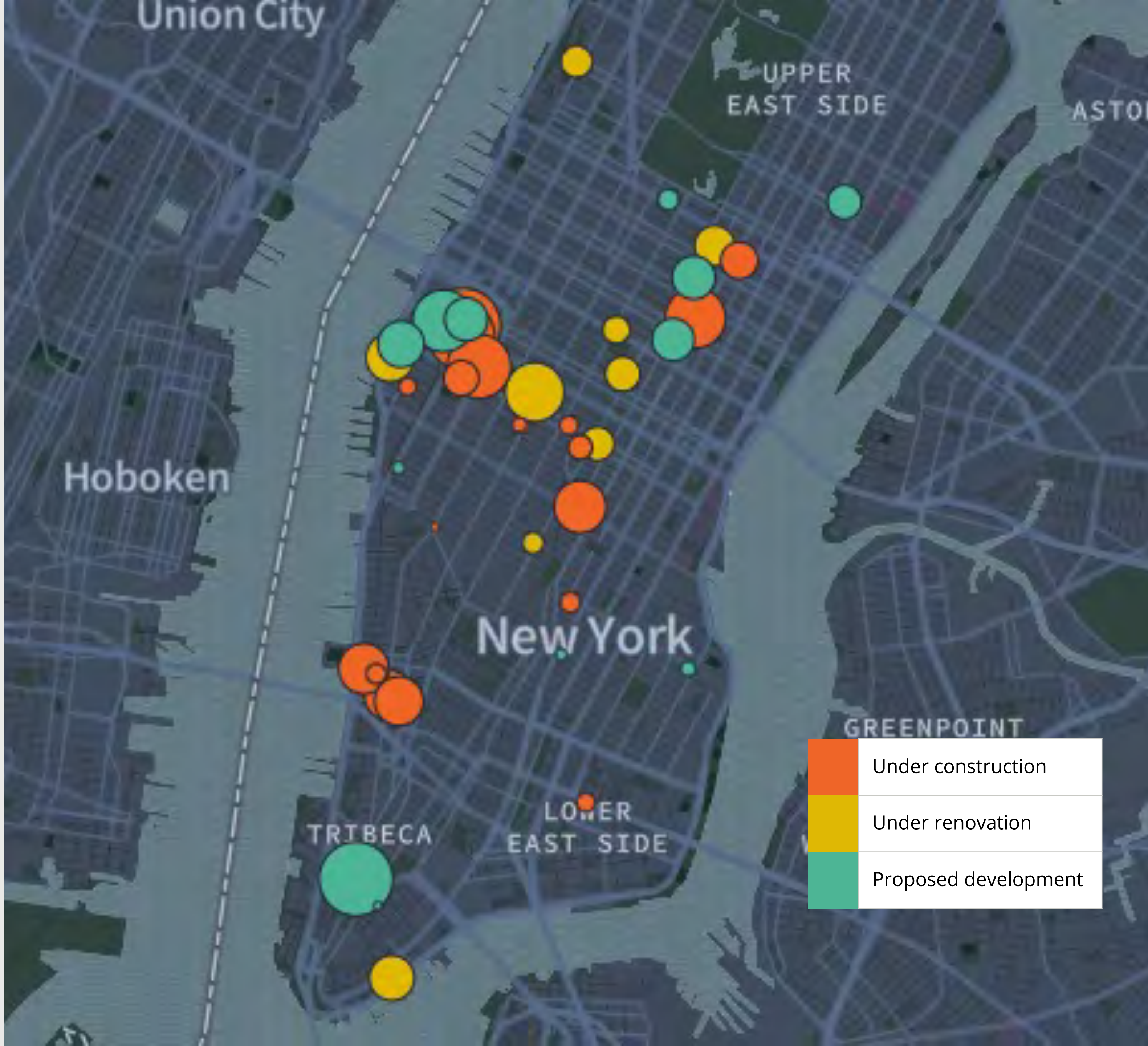
proposed, under construction

6.3%

share of office inventory

1931

average delivery date of Manhattan offices



Let's look at capital markets conditions

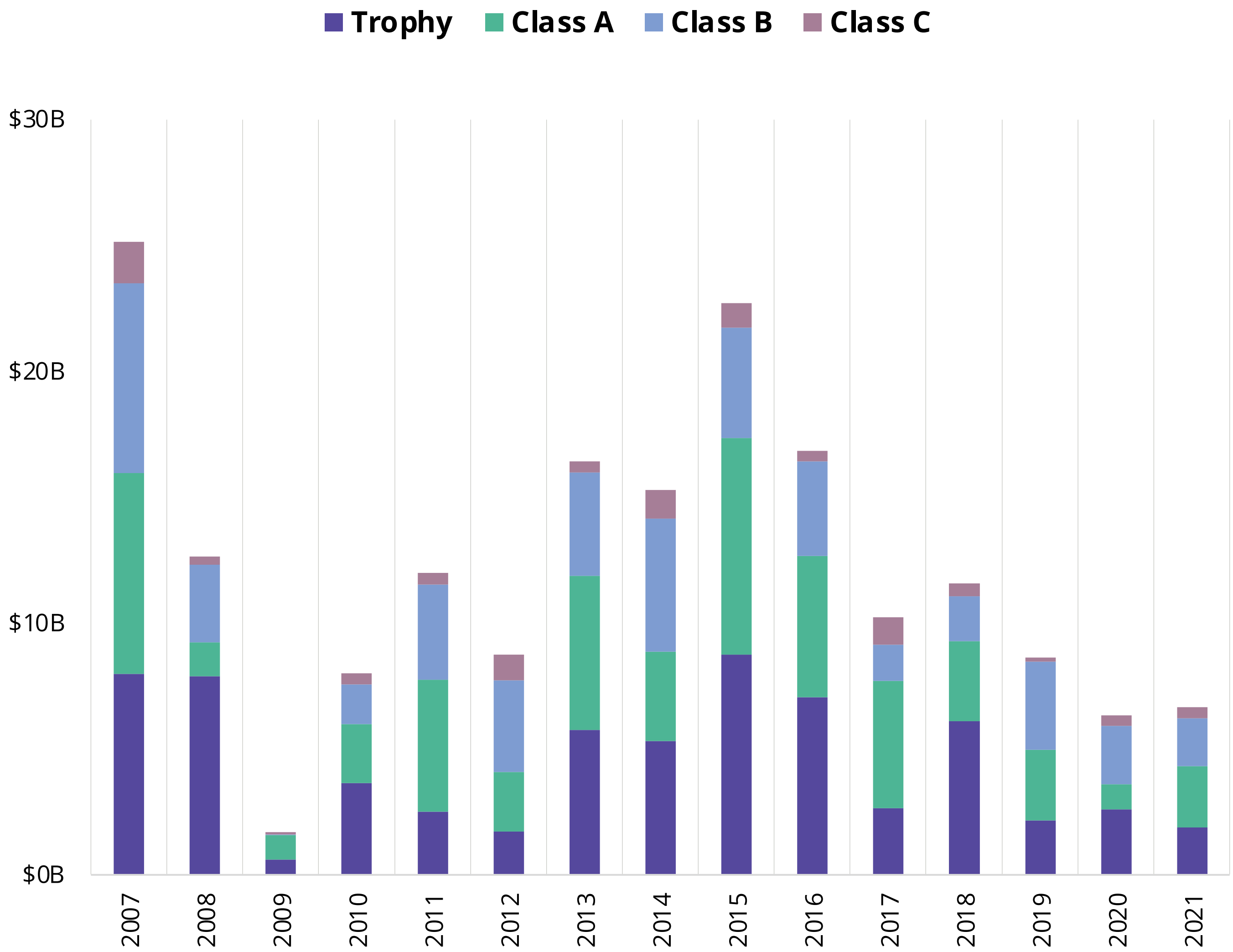
Institutional investors' continued focus on high-quality, cash-flowing properties indicates that a more active 2022 could be forthcoming.

Office investment dollar volume

$6.7B

office dollar volume in 2021, up from $6.3B in 2020.

Investment demand demonstrated signs of strengthening in the fourth quarter, highlighted by Harbor Group International's $760.0M acquisition of 51 West 52nd Street and a foreign investor's 25.0% equity interest in One Madison Avenue. Several additional high-profile offices are under contract, including 441 Ninth Avenue for $1.0B, underscoring domestic and international investors' continued interest in cash-flowing office assets.



Source: AVANT by Avison Young
New York City Department of Finance
RCA

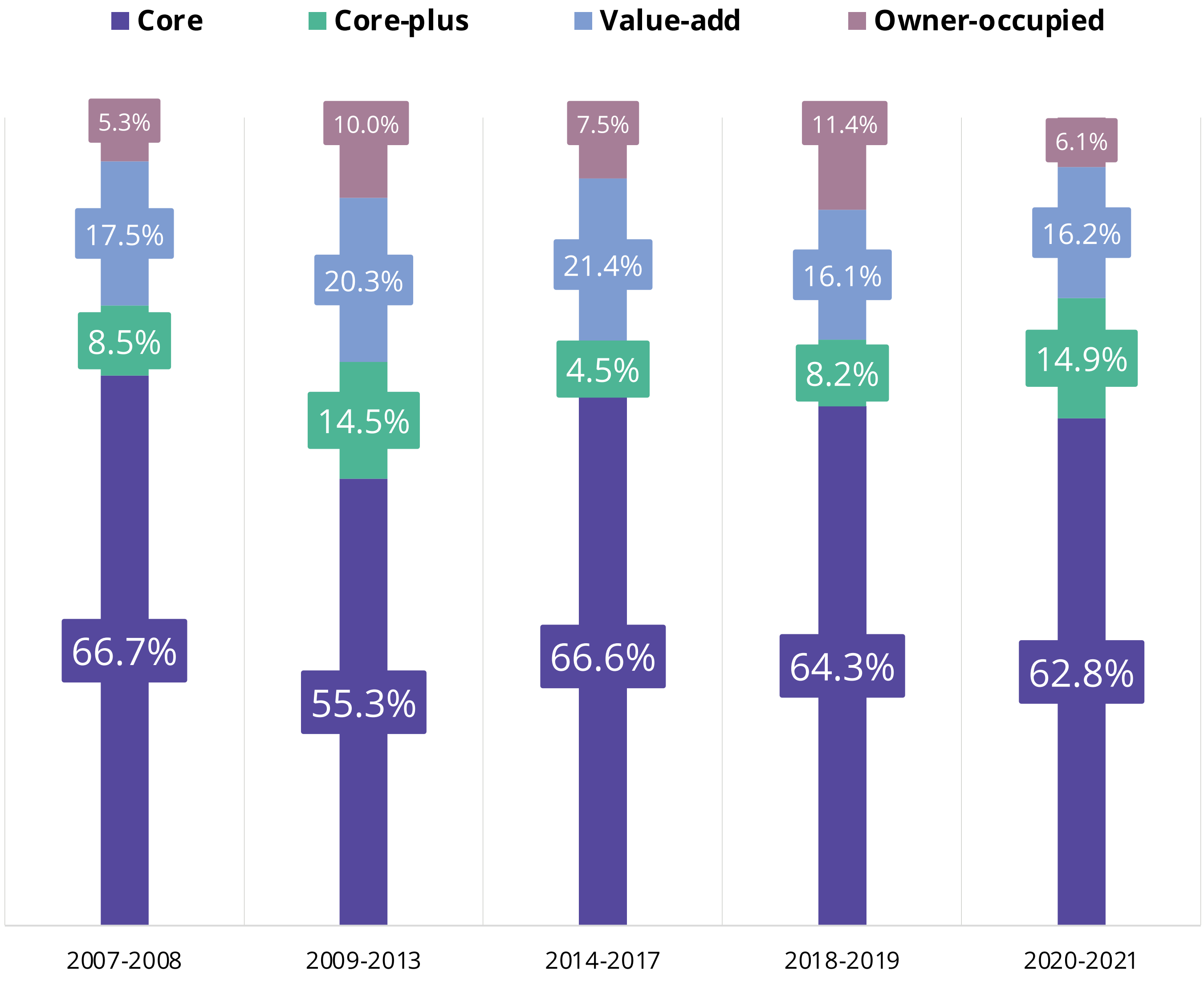
AVANT by AVISON YOUNG

Office investment asset profiles

62.8%

core office investments from 2020 to 2021.

Investors have continued to focus on core, cash-flowing assets given prevailing occupier market uncertainties and the broader flight-to-quality trend amidst a market flush with liquidity. Transitionary office properties that necessitate modest capital improvement programs in transit-oriented submarkets such as Grand Central have also garnered interest from yield-focused investors in recent months.



Source: AVANT by Avison Young
New York City Department of Finance
RCA

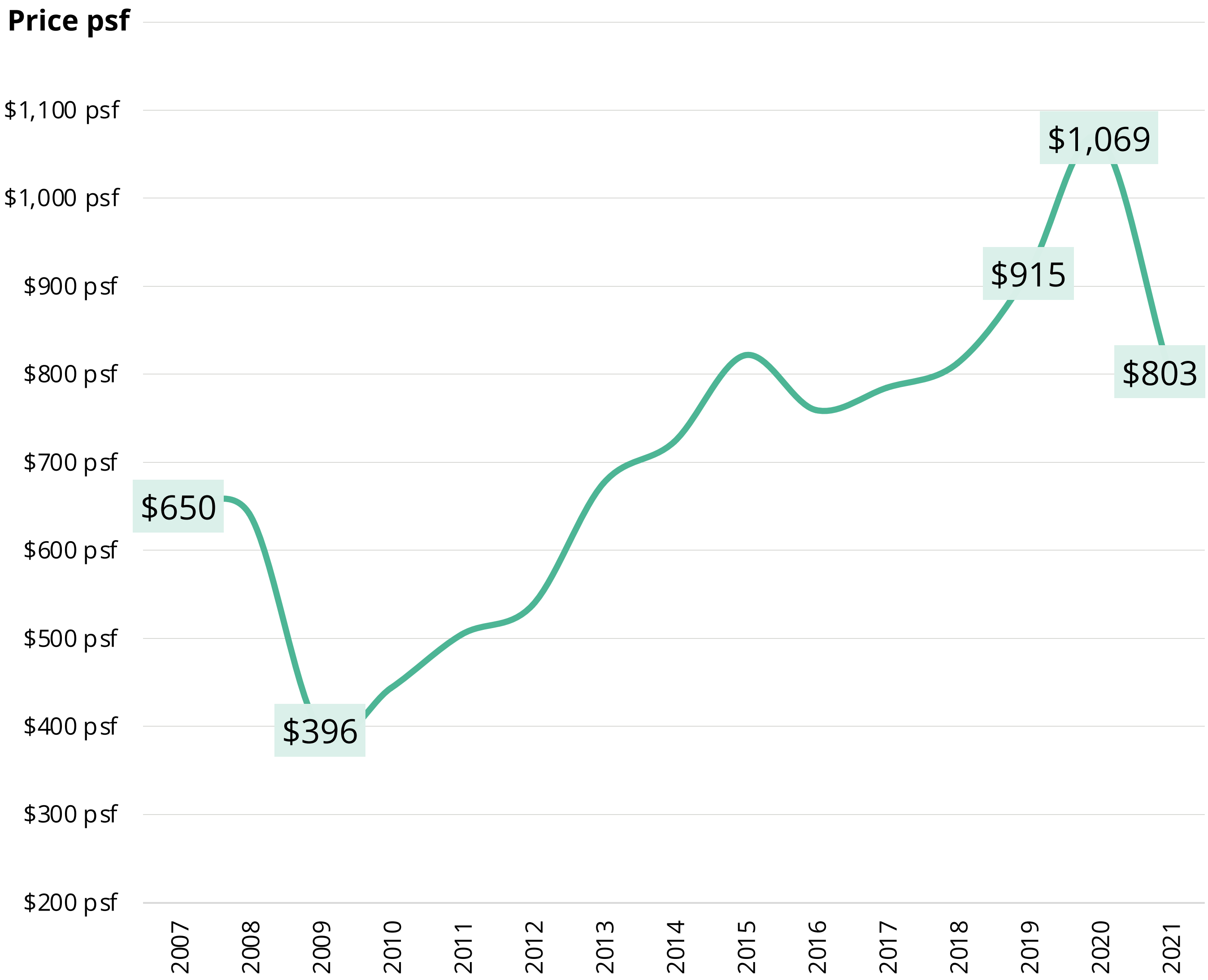
AVANT by AVISON YOUNG

Office asset pricing

-12.2%

office pricing, 2019 vs. 2021.

Office asset pricing has softened as investors have adopted more measured underwriting approaches compared with the pre-pandemic period. Still, asset values are positioned to rise incrementally in the coming months due to the profile of properties that are under contract and investors' continued appetite for Trophy and Class A properties.



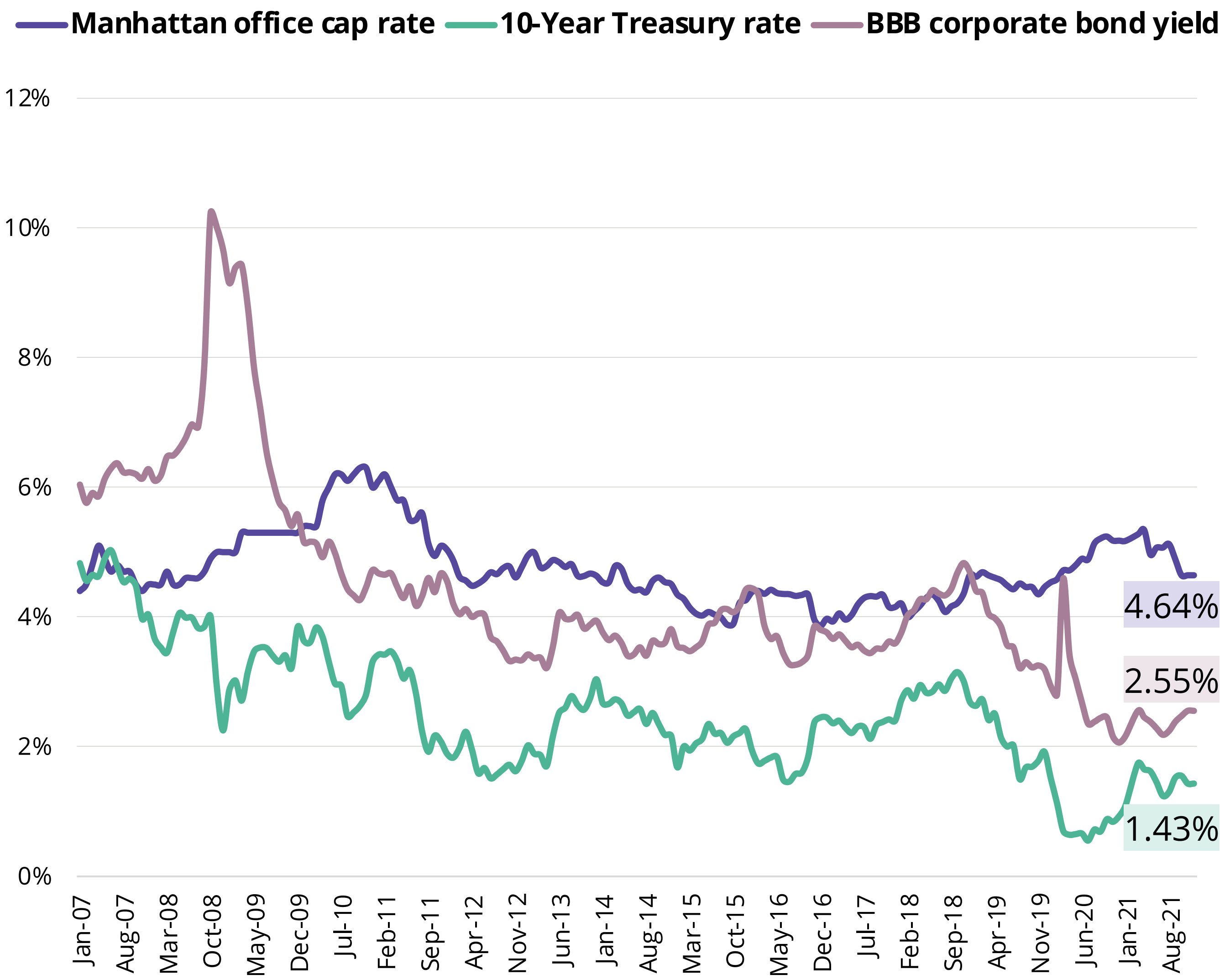
Source: AVANT by Avison Young
New York City Department of Finance
RCA

Office cap rates versus benchmark yields

321 bp

office cap rate spread vs. 10-year Treasury rate.

The spread between office yields and the benchmark 10-year Treasury rate remains wider than the 2007 to 2021 historical average of 224 bp, demonstrating that investors are still capturing sufficient risk-adjusted returns.



Source: AVANT by Avison Young
U.S. Department of the Treasury
Federal Reserve Bank of St. Louis

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Now, let's see what we can expect looking forward

Strong underlying employment fundamentals could be offset by slowed return-to-office efforts and continued weakness in the commodity office sector.

Here's what we can expect looking forward

- Underlying employment conditions are positioned to remain favorable, providing positive tailwinds if employers increasingly mandate employees to return to the office.
- However, the wide adoption of hybrid work strategies due to competitive labor market conditions and rising infection rates caused by new mutations of the virus have continued to complicate long-term office workplace strategies. Office demand should continue to rise from 2020 and early 2021 levels but may not approach pre-pandemic levels until more employees return to work.
- Market-level availability rates are poised to stabilize or decrease in 2022 due to stronger forecasted demand, though high-quality, transit-oriented properties are likely to capture an outsized share of leasing activity. The commodity sector may need to continue to compete based on pricing, causing rents to weaken in this sector.
- The elevated profile and scale of properties under contract and heightened levels of dry powder indicate that the investment sales market should be active in 2022. These conditions could cause asset pricing to rise incrementally from 2021 levels.

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You have questions. We have answers.

Get in touch

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Office insights glossary of terms

Demand

- **Leasing activity:** total square footage of relocations, renewals, expansions and subleases expressed when the leases are signed, not when tenants take physical occupancy of the space
- **Absorption:** period-over-period change in occupied square footage

Supply

- **Office inventory:** existing office properties that are 20,000+ square feet, including owner-occupied properties and excluding government owner-occupied properties
- **Direct vacancy rate:** space operated by landlords that is ready for immediate occupancy
- **Sublease vacancy rate:** space operated by sublandlords that is ready for immediate occupancy
- **Total vacancy rate:** sum of direct vacancy rate and sublease vacancy rate
- **Availability rate:** space that is vacant plus space that will become vacant over an indefinite time horizon, including spaces that are occupied by vacating tenants and under-construction properties

Office rents and concessions

- **Asking rents:** pricing guidance provided by landlords to tenants for available space expressed as full service (FS)
- **Base rents:** fair market value of market-level lease pricing based on representative executed leases, expressed as full service (FS)
- **Free rent period:** months of free rent that are typically provided upfront by landlords to tenants as a concession to offset the total cost of a lease and/or the construction timeline of an office suite
- **Tenant improvement allowance:** an allowance expressed in dollars per square foot provided from landlords to tenants to offset build-out, engineering, space planning and related permit costs
- **Net effective rent:** base rents discounted by the dollar values of tenant improvement allowance and free rent concessions expressed as full service (FS)

Capital markets

- **Investment volume:** office sales dollars expressed when the transactions close and based on inventory thresholds; partial-interest sale dollar amounts are not grossed-up to reflect the 100% value of the sale
- **Asset pricing:** unweighted average per-square-foot asset pricing of market-level closed sales
- **Cap rate:** net operating income divided by sale price; this measurement of market-level investment returns is calculated as an unweighted average based on closed investment sales

Vitality Index

- **Visitor volumes:** based on extrapolated, anonymized cell phone pings provided by Orbital Insight at custom, geofenced locations, the Vitality Index tracks visitor volumes at representative areas of interest across cities with dwell times of two minutes or more; for the Office Vitality Index, 8-10 representative, single-occupier properties are chosen to represent visitor volumes across cities and industries and data was captured

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Explore the latest data and insights

The office vitality index

Measuring the pace of our return to downtowns

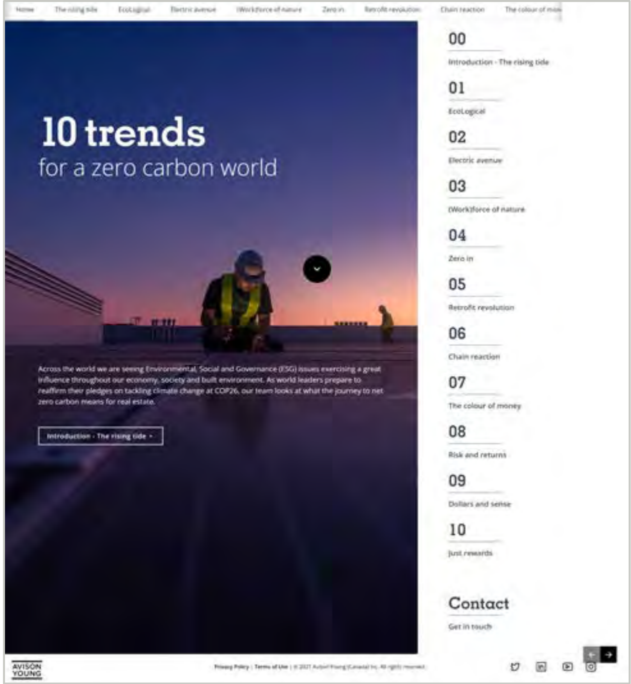
Our team analyzes how return-to-office efforts have evolved across cities and industries across North America

U.S. employment overview

Tracking trends in real-time

Our team takes a look at real-time movement of people in major cities across North America, and how the volume of foot traffic compares to pre-pandemic levels.

Deep-dive into the thought capital shaping real estate



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