New York City

Market Report
Second Quarter 2017

Avison Young's 2017 Second Quarter Manhattan Market Report includes our insights on office leasing, investment sales, debt and equity, valuation and advisory, and retail activity. While there have been some signs of softness in related activity, there are other factors in play that have created opportunities. In the following pages, we hone in on some of the challenges, but remain optimistic as to what the future could hold for the New York City real estate market.

Overall office leasing for Manhattan turned out soft for the second quarter, however, there was enough diverse tenant activity that kept the market afloat through mid-year. From notable renewals and expansionary activity at the high end, to a healthy mix of smaller new deals, the Manhattan market remains in equilibrium with a vacancy rate still at 10.7 percent. Expect a good mix of real estate options to satisfy healthy demand.

In looking at the investment sales and related debt and equity markets, although the dollar volume of transactions experienced a slight uptick in the second quarter over the first, one can not ignore the reduction in overall activity through mid-year. While the China-based HNA Group's closing of its $2.2 billion ($1,282 per square foot) acquisition of 245 Park Avenue added to recent quarterly dollar volume levels, both cross border as well as domestic capital directed to the real estate asset class overall is being impacted partly by political and economic uncertainty, dampening also the number of transactions being executed. We keep a watchful eye on the disparity between buyer and seller expectations and the impact on market activity levels by all national and international participants.

During the past few years up until the middle of 2015, pent up demand and a more positive political and economic environment prompted increased investment and a "land grab" mentality. This was the case particularly for condo development and other significant projects, coupled with a wave of rising prices. Since this time, valuation and advisory professionals point out the transitioning market forces and their impact on land values and sales, which have been down for nearly two years. Recent uncertainty over this latter time period has placed many large-scale developers on the sidelines, with sales that are taking place also being of smaller scale and by less recognized participants. Time will tell if whether or not the market is reflecting an adjustment or a more prolonged correction.

For the retail property sector, while some are predicting the death of brick and mortar, our colleagues believe there is still market share to be gained with physical store locations. As such, the brick and mortar store will survive, but under new conditions. With this adjustment, expect the requirements of physical stores to be smaller in nature and fewer in location, serving more as a showroom or experiential destination.

As global uncertainty continues to weigh on property markets overall, we believe opportunities remain in New York City across a variety of quality assets. Please reach out to any Avison Young team to assist you with your strategic real estate decisions.

Best,

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Second Quarter 2017 / New York City

Office Leasing

Market Facts

-14%
Year-over-year decline in Manhattan leasing volume through 1H17

5.0M SF
Second quarter Manhattan leasing volume

7%
Year-over-year increase in Downtown leasing volume through 1H17

10.7%
Second quarter vacancy rate, Manhattan overall in equilibrium

Soft Second Quarter Volume, But Diverse Leasing Activity Keeps Overall Markets Afloat Through Mid-Year

Second quarter office leasing velocity for the Manhattan market of 5.0 million square feet is down 32.0 percent year-over-year. However, following stronger first quarter performance, volume for the entire first half of the year is down 14.0 percent year-over-year. While top activity through the first half of the year was more weighted toward sizable renewals by FIRE and TAMI tenants, significant transactions also became more diversified with lease signings commenced largely by notable government/public administration tenants.

Midtown Leasing Velocity Slows; Hudson Yards Remains Attractive to Finance and Legal Services Entities

Second quarter leasing activity for Midtown ended down 35.0 percent year-over-year (3.2 million versus 5.0 million square feet), with volume for the full first half of the year down 23.0 percent (7.7 million versus 10.0 million square feet). For the second quarter alone, four of the eight large block leases (greater than 100,000 square feet) were executed in Midtown by both financial and legal services tenants. Two of such leases were in Hudson Yards, which continues to attract the largest of these tenant types (digital wealth management firm JPMC Digital with its 305,000-square-foot new lease at 5 Manhattan West and legal firm Cooley LLP with its 131,000-square-foot new lease at 55 Hudson Yards). Outside of the large block activity, the average deal size ranged from 20,000 to 30,000 square feet (compared to 30,000 to 40,000 square feet one year ago). The overall Midtown vacancy rate of 11.0 percent for the second quarter was in line with last quarter and up from 10.1 percent year-over-year. The increase is attributed to more available Class A space on the market in the Plaza District and Sixth Avenue/Rockefeller Center submarkets. The overall (all classes) average asking rent of $86.72 is down 1.0 percent from last quarter, but up close to 4.0 percent year-over-year. The highest asking rents for available Class A space remain in the Plaza District and are close to the $103.00 per square foot level, down from the $107.00 per square foot level last quarter. With the year-over-year rise in vacancy in Midtown, particularly in the Plaza District, this could signal a potential shift among tenants who seek alternative newer and more efficient space requirements. This was recently exemplified by private equity firm Silver Lake's announcement to relocate from 9 West 57th Street to 55 Hudson Yards, joining other finance and legal service entities.

Midtown South Steadily Grows More Diverse Beyond Traditional Technology Tenant Base

Midtown South continues to grow in appeal beyond its traditional technology tenant base. During the second quarter, the market has earned the attention of diverse tenants such as the New York City Department of Citywide Administrative Services (349,777-square-foot renewal at 109 East 16th Street in Gramercy Park by this government/public administration entity) and Aetna (145,671-square-foot new lease at 61 Ninth Avenue for this health insurance entity in Chelsea). The average deal size outside of these two transactions ranged from 15,000 to 20,000 square feet (compared to 30,000 to 40,000 square feet one year ago). However, with the two aforementioned large block deals, leasing volume for Midtown South was just down 11.0 percent year-over-year for the second quarter (931,000 versus 1.0 million square feet) and down 10.0 percent (2.0 million versus 2.2 million square feet) for the full first half of the year. As a result, the overall vacancy rate for Midtown South is now at 7.7 percent, which is below the 7.8 percent in the prior quarter and above the 6.8 percent in the prior year. The year-over-year increase is attributed to the addition of 170,000 square feet of direct space that recently came online in the SoHo/NoHo submarket, in addition to over 270,000 square feet of space (Tommy Hilfiger – 601 West 26th Street) put on the market last year in Chelsea. Overall average asking rent of $72.02 is down less than 1.0 percent from the prior quarter and up almost 14.0 percent from one year ago, with the highest asking rent for available Class A space being in Chelsea, which remains at triple-digit levels.

Downtown Takes a Quarterly Pause, But Broadened Leasing Activity Keeps Mid-Year Volume Positive

Downtown office leasing volume (852,000 versus 1.3 million square feet) was also down 35.0 percent year-over-year for the second quarter, but up for the first half of 2017 (3.7 million versus 3.5 million square feet) by 7.0 percent. Outside of large block leasing executed by the Human Resources Administration (193,000-square-foot new lease at 375 Pearl Street by this government/public administration entity) and Spotify (100,000-square-foot expansion at 4 World Trade Center by this TAMI entity), the average deal size ranged from 15,000 to 20,000 square feet (compared to 25,000 to 35,000 square feet one year ago). The overall vacancy rate for Downtown is at 12.1 percent, below the 12.8 percent in the previous quarter and above the 10.4 percent

MARKET DATA POINTS

Manhattan Overall

Indicator	2Q16	2Q17
Vacancy	9.60%	10.70%
Rent	$76.43	$79.34
Absorption	301,684 SF	629,668 SF

Midtown Overall

Indicator	2Q16	2Q17
Vacancy	10.10%	11.00%
Rent	$83.74	$86.72
Absorption	257,115 SF	(85,348) SF

Midtown South Overall

Indicator	2Q16	2Q17
Vacancy	6.80%	7.70%
Rent	$63.40	$72.02
Absorption	(143,441) SF	74,034 SF

Downtown Overall

Indicator	2Q16	2Q17
Vacancy	10.40%	12.10%
Rent	$60.45	$65.15
Absorption	188,010 SF	640,982 SF

year-over-year. The quarterly decline is the result of a smaller amount of large-block space that came online, while year-over-year a large amount of space at 3 World Trade Center became available. Overall asking rents of $65.15 are up 1.0 percent from the prior quarter and up close to 8.0 percent year-over-year.

Although overall leasing turned out soft for the second quarter, there was enough diverse tenant activity that kept the Manhattan real estate market afloat through mid-year. From notable renewals and expansionary activity at the high end, to a healthy mix of smaller new deals, vacancy for Manhattan remained at 10.7 percent from the prior quarter and the market in equilibrium. Expect a good match of space options for a growing tenant mix.

Trends to Watch

- The potential contraction in vacancy levels cited in the first quarter for the Downtown market played out during the second quarter. Watch for more broadened significant leasing activity, as more price sensitive players search for low-cost space options.
- The overall Manhattan market remains in equilibrium, with vacancy within the 9.0 to 11.0 percent range. Expect a continued mix of real estate alternatives to satisfy healthy demand.
- Watch for more owners and landlords to increase their capital spend on the modernization of their buildings in order to remain competitive in their offerings.

Largest Blocks of Contiguous Space Currently Available

Address	Square Feet	Market
3 World Trade Center	1,803,484	World Trade Center
550 Madison Avenue	852,796	Plaza District
180 Maiden Lane	551,683	Financial District
1 World Trade Center	505,244	World Trade Center
32 Old Slip	346,618	Financial District

Notable Lease Transactions

Tenant	Address Submarket	Size Lease Type
HSBC	452 Fifth Avenue Grand Central	548,000 SF Renewal
NYC Department of Citywide Administrative Services	109 East 16th Street Gramercy Park	349,777 SF Renewal
JPMC Digital	5 Manhattan West Penn Plaza/Garment	305,365 SF New lease
Human Resources Administration	375 Pearl Street TriBeCa/City Hall	193,821 SF New lease
Mizuho Americas	1271 Avenue of the Americas Sixth Avenue/Rockefeller Center	148,000 SF New lease

Markets By The Numbers

Submarket	Inventory (SF)	Direct Vacant (SF)	Sublet Vacant (SF)	2nd Quarter 2017 Overall Vacancy Rate	2nd Quarter 2017 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	54,672,316	5,510,819	889,377	11.7%	169,917	310,778	1,733,000	$73.66	$56.33
Penn Plaza/Garment	25,414,784	1,548,757	525,234	8.2%	302,586	178,931	6,716,000	$79.77	$60.06
Plaza District	76,789,890	7,988,014	2,005,574	13.0%	(410,294)	(1,859,326)	670,000	$104.31	$59.88
Sixth Avenue/Rockefeller Center	55,834,791	4,495,318	1,109,214	10.0%	181,250	96,406	0	$87.11	$56.04
Times Square South	24,493,961	2,299,403	547,498	11.6%	(177,658)	192,275	0	$80.72	$57.84
Times Square/West Side	37,234,925	2,589,779	545,361	8.4%	(151,149)	163,618	0	$80.32	$59.98
Total	274,440,667	24,432,090	5,622,258	11.0%	(85,348)	(917,318)	9,119,000	$90.00	$58.29
Midtown South									
Chelsea	22,910,054	1,042,585	748,205	7.8%	47,234	40,242	270,000	$141.51	$51.59
Hudson Square	13,749,608	898,671	330,933	8.9%	52,156	99,716	0	$92.29	$72.09
Gramercy Park	30,536,623	1,468,981	583,068	6.7%	133,570	138,702	0	$72.21	$63.20
SoHo/NoHo	8,624,666	621,160	167,234	9.1%	(158,926)	(167,822)	0	$93.94	$71.43
Total	75,820,951	4,031,397	1,829,440	7.7%	74,034	110,838	270,000	$99.66	$62.38
Downtown									
TriBeCa/City Hall	19,824,655	1,267,967	204,856	7.4%	124,414	(109,687)	0	$54.74	$62.53
Financial District	51,658,758	5,004,456	889,661	11.4%	307,624	(106,765)	0	$60.44	$49.80
World Trade Center	28,752,165	4,307,821	464,630	16.6%	208,944	(1,229,972)	0	$77.74	$47.27
Total	100,235,578	10,580,244	1,569,147	12.1%	640,982	(1,446,424)	0	$66.95	$53.37
Manhattan Overall Total	450,497,196	39,043,731	9,020,845	10.7%	629,668	**(2,252,904)**	9,389,000	$83.77	$59.15

Data as of 7/5/2017

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Investment Sales

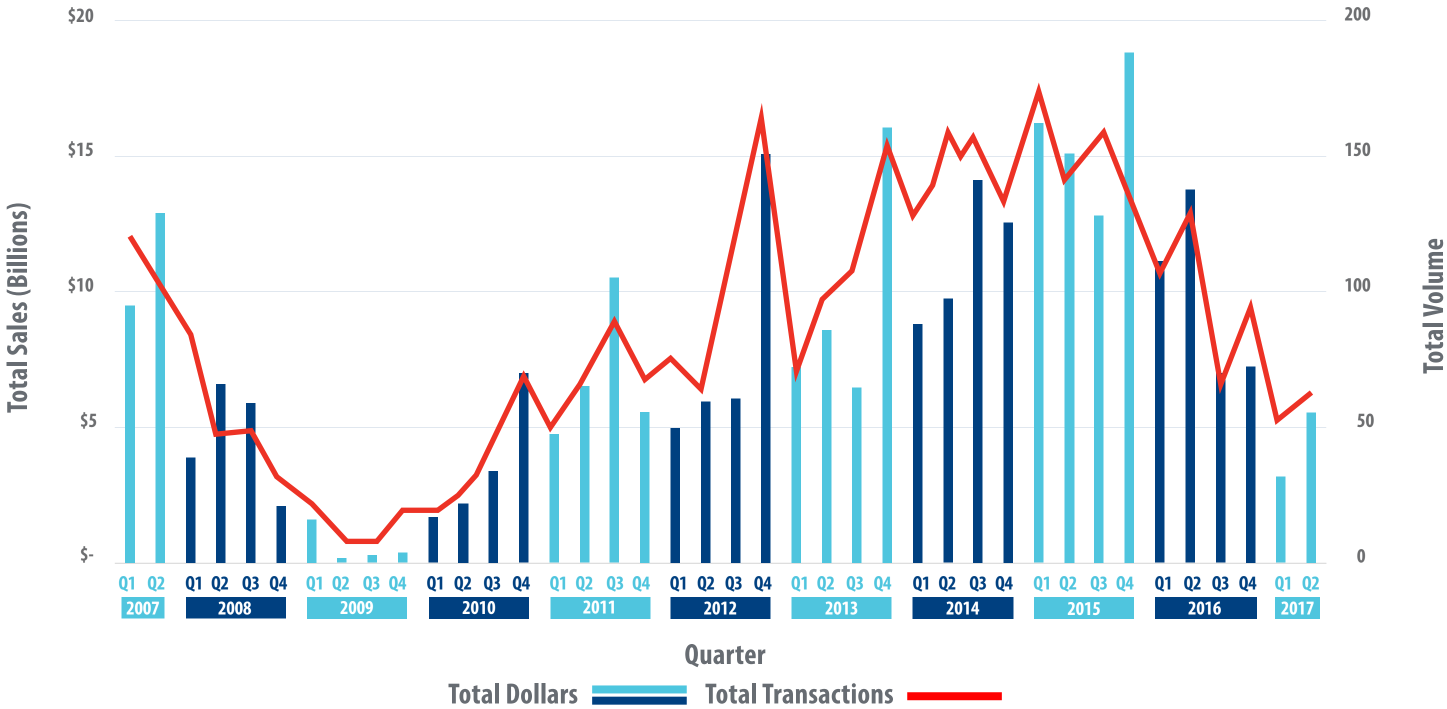
Overview

In the second quarter of 2017, the Manhattan investment sales market experienced a slight uptick from the prior period, with the total dollar volume faring better. Increasing foreign capital is redefining the City's buyer pool, with a particular affinity to the trophy asset class. Chinese capital has accounted for half of the total dollars invested since the beginning of 2017, which has helped buoy market volume and pricing. Threatening a strong market rebound are the capital controls from the Chinese government, rising interest rates, the wall of maturing CMBS debt originated around the 2007 peak, and e-retail's war on brick and mortar stores. Further influencing the direction of the market are the ever-changing preferences and regulations in the city's residential market – a chain reactor to the development market. Despite the shifting market conditions on the horizon, the pendulum of investor sentiment is swinging toward optimism.

Quarterly Growth, Weakness with an Upside

The number of property trades is the best measure by which to gauge the activity in the market. Avison Young tracks the sale of properties in Manhattan with a sales price of $10 million or greater and the trends in this market tranche are becoming clearer. From the third quarter of 2013 through the second quarter of 2016, the Manhattan market averaged 141 transactions per quarter and never recorded less than 112 in that 12-quarter span. In the trailing four quarters ending 2Q 2017, the average transaction count dropped to 71, with the most recent tally at 66 for this second quarter. At the end of the first half of 2017, the annualized forecast of total transaction volume was on pace to be 40.0 percent lower than 2016, and a 60.0 percent drop-off from 2015. At the current pace, 2017 is shaping up to have the lowest sales count since the period from 2008 to 2010, the last market trough. Dollar volumes tell a similar story at the year's halfway mark. The first quarter's $3.2 billion in dollar transactions was improved to $5.6 billion in the second quarter, but this increase was largely attributable to a single $2.2 billion purchase while the first quarter lacked any billion dollar transactions. The dearth of recent activity has impacted several of the predominant market statistics. Multi-family properties have historically accounted for approximately one third of the total transactions of a given quarter while in 2017 that percentage has grown to more than half. Dollar volumes statistics have shifted as well. Office trades typically account for roughly half of the dollar volume and that measure has increased to over three quarters in 2017. At a time where there is uncertainty amongst the pool of incumbent investors, foreign capital sources are increasing their exposure to New York City real estate and adding more complexity and diversity to an expanding marketplace. The upside to this expansion is the growth in the number of investors participating in the New York City real estate market, as well as the degree of future price competition as the market begins to accelerate.

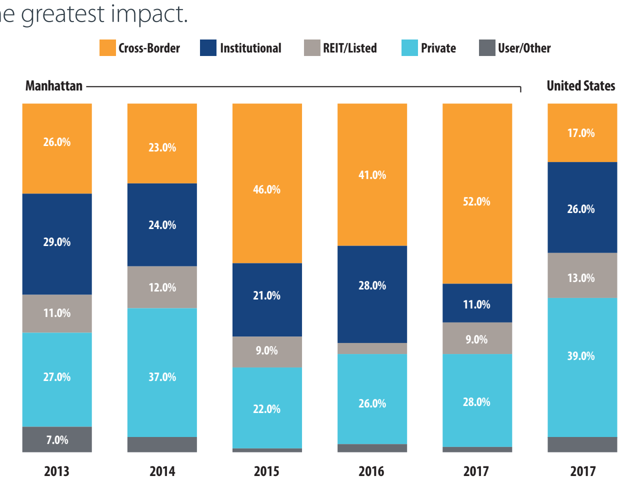
Quarterly Total Dollars & Transactions



Cross Boarder Capital and Chinese Controls

At a time when domestic investors have pulled back, foreign parties have ramped up their holdings in Manhattan. The preference for trophy assets and the willingness to pay record prices, is creating a further disconnect in the bid-ask spread for non-trophy office properties in the city. Tracking the amount of investment dollars in Manhattan real estate from cross-border sources, the percentage has increased from the mid-20 percents from 2011 through 2014 to over 50 percent in 2017 thus far. When comparing Manhattan to the overall United States, as a benchmark, over three times the percentage of dollars coming across the border have targeted Manhattan. In May 2017, HNA purchased 245 Park Avenue for $2.2 billion which represents a quarter of all dollar volume for the first half of the year. Moreover, aside from being the sixth largest transaction in Manhattan history, the trade penciled out to $1,282 per square foot, among the highest price per pound for this type of asset. HNA is just the latest Chinese company to make a big bet on Manhattan. Since the beginning of 2013, Chinese companies alone have poured nearly $18 billion into Manhattan real estate. This flow of funds, however, may soon be threatened.

At the end of last year, the Chinese government unrolled capital controls aimed at keeping more capital within its borders. The move is intended to combating slowed growth and a weak currency as investment dollars leave the country in search of higher returns and/or greater perceived security. In 2016, Anbang Insurance Group withdrew its $14 billion bid to purchase Starwood Hotels & Resorts after the government quashed the deal because it would push the company's overseas assets above the allowable 15 percent threshold (Anbang purchased the Waldorf Astoria in 2015 for $1.95 billion). If the Chinese government continues to increase movement to capital barriers, the major Chinese players may be regulated out of the market. The Asia Society reported last year that Chinese investors are expected to deploy only $58 billion into U.S. real estate between 2016 and 2020, a more than 50 percent drop from the $110 billion invested in the slightly longer six-year period spanning 2010 and 2015. With Manhattan as a primary target for funds, it is likely to experience the greatest impact.



Impediments to Resuming Normal Activity

The slumping market is far from dead. There is no catastrophic event causing the current correction. Instead, market forces have put a brake on activity while macro-economic uncertainty is sorted out. It is inevitable that the cycle will once again pick up steam as these influences unfold. We have identified several near-term impediments to the full recovery below.

- Chinese governmental regulations on capital allocations outside the country
- General investor sentiment
- Rising interest rates
- Pre-recession CMBS loans struggle to refinance
- Slumping residential market, slow condo sales and heavy concessions in rental market
- Dearth of construction financing and stalled construction sites needing funding
- E-retail depressing brick and mortar retail values
- Lack of clarity in Trump's proposed tax policy
- A beneficial proposal for capital infrastructure from Washington

Trends to Watch

- Market activity will struggle to build on the second quarter's growth through the summer months
- Chinese retail and institutional investors will shift less wealth outside of the country
- Increases in the cost of capital simultaneously with an increase in demand for capital

Top Second Quarter 2017 Sales

Buyer **Address** Seller	Size Type	Price Price/SF
HNA Group JV 181 West Madison Holding LLC **245 Park Avenue** NYSTRS JV Clarion Partners JV Brookfield Prop Partners	1,723,993 SF Office	$2.2 Billion $1,282/SF
NY REIT **825 Eighth Avenue** DRA Advisors JV George Comfort & Sons JV Feil Organization JV RCG Longview	2,055,583 SF Office	$698.0 Million $681/SF
Ivanhoe Cambridge JV Callahan Capital Partners **85 Broad Street** MetLife RE Investors JV Beacon Capital Partners	1,100,000 SF Office	$652.0 Million $593/SF
RFR Realty **95 Morton Street** Brickman Associates	217,084 SF Office	$205.0 Million $949/SF
Silverstein Properties **619 West 54th Street** Taconic Investment Partners	326,861 SF Office	$149.0 million $509/SF

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Debt & Equity

Further Analysis of Theories Behind Reduced Real Estate Sales

It is a known fact that the volume of real estate sales in Manhattan has dropped precipitously in 2017 and there are various theories among property owners and brokers as to why this is the case. Let us further examine these theories.

Political and Economic Uncertainty

Uncertainty due to politics is the theory most often mentioned. Here, policies pertaining to capital gains tax, infrastructure projects and just "Trump wild card" uncertainty are cited as potential obstacles for market participants to accept low cap rates and high prices on a per square foot basis.

General economic uncertainty is cited as a concern in the marketplace, as companies that are not expanding has caused prospective buyers to underwrite properties more conservatively. Accordingly, landlord concessions have been increasing while rents have stayed fairly static. This has caused net effective rents to drop across the board.

Foreign Investor Appetite Once Hefty, Now Curtailed

The impact of foreigner investor appetite is another reason for the decline in real estate sales velocity. In 2016 and prior there was an influx of Asian foreign capital, particularly from China, as well as from Russia that flooded the market. This healthy activity propped up Class A markets across all property types. Now with these groups clearly pulling back, demand as a whole has fallen along with it. A few exceptions exist, as with China-based HNA Group's acquisition of 245 Park Avenue for $2.2 billion ($1,227 per square foot) that closed the second quarter of this year.

Secondary Reasons Related to the Luxury Condo and Retail Market

A secondary reason for the decline in sales volume is a potential overflow effect from luxury condo woes. The high-end luxury market was the first to feel the pullback, especially due to the decreased foreign demand. This has possibly exacerbated the willingness of prospective buyers to take a step back.

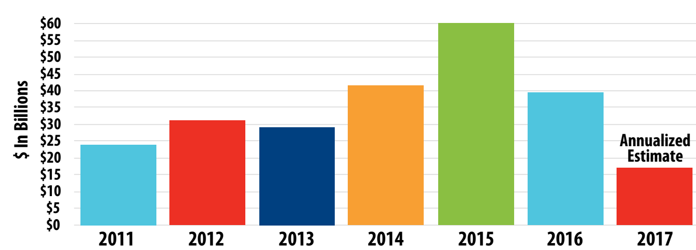
Retail rent softness is also occurring. As high street retail has seen lower rents due to retailers lack of willingness to have loss leader locations, at the same time they are also feeling the effects of e-retailers and e-commerce trends on their sales.

Financing Trends

Financing leverage has also become more conservative. While long-term interest rates have stayed low, LIBOR has crept up with 30-day LIBOR now at 1.15 percent, moving roughly 50 basis points higher within the last six months. This has caused acquisition financing to become slightly more expensive. More importantly, senior lenders are looking to do lower leverage, which causes the junior financing/mezzanine tranches to be larger, thus impacting pricing.

While the New York City market remains robust despite the pullback in real estate sales, there is clearly a record gap in the bid/ask spread, as sellers are still wanting top-of-the-market pricing.

Manhattan Commercial Property Sales

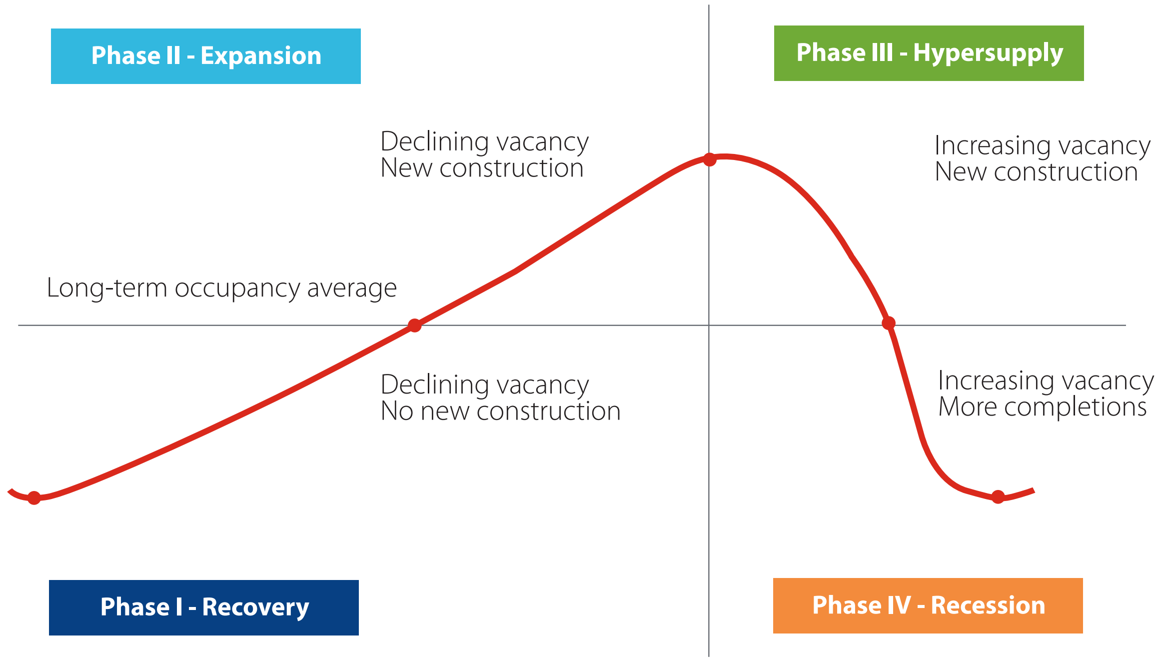


Trends to Watch

- Look for the New York City investment sales market to be on pace for a 51.0 percent drop in volume in 2017 versus 2016
- Foreign investment demand has taken a pause due to political and economic uncertainty, potentially expect more to come
- Watch for further softening of prices in both the New York City luxury condominium market and in high street retail rents

Valuation & Advisory

Market Cycle Quadrants



Source: Mueller, Real Estate Finance, 1995.

The Development Land Market – A Current State of Transition

As real estate markets begin to show signs of transitioning from an expansion phase to one of over-supply, land is one of the first asset classes to show weakness. The requisite multi-year periods to go from site acquisition/assemblage to completion/full absorption, exposes investors and developers to the added risk that market conditions could go from expansion to recession. Given the timelines for development, land in particular, is one of the first asset classes to retreat as real estate markets become over-heated.

Heated Investment Markets

In recent years up until about mid-2015, economic, political and global events have contributed to a surge of foreign investment in New York City real estate that competes with domestic investment. Foreign interests include financial institutions, pension funds, sovereign funds and wealthy individuals, among others. Whether seeking greater yield than obtainable at home, or just a safe haven to park capital, the resulting surge in foreign investment has significantly contributed to the five-year wave of rising prices for all assets in this cycle (office, hotel, retail and residential), which has extended to land.

For residential condominiums, the surge in foreign investment gave rise to the ultra-luxury residential condo phenomenon of billionaire's row on West 57th Street. With these projects came stratospheric pricing for ultra-luxury condos that had a spillover effect on price advances for the broader condo market.

Land Rush and EB-5 Investment

Initially propelled by pent up demand and a low supply of new product, condo prices soared to new highs in the post financial crisis economy. Increases were buoyed by international investment, the city's improving economy and record low debt costs. These forces contributed to a "land grab" mentality for condo development land by both foreign and domestic players.

Some notable examples of foreign investment in land include: the Kwee family's $300 million purchase of a 49.0 percent interest in Hine's MOMA Tower project in late 2013 (a land site at the time), Extell's One57 backed by investors from Abu Dhabi, and, the Qatar Investment Authority's purchase of a 44.0 percent stake in Brookfield's $8.6 billion mixed-use Manhattan West project in October 2015.

Wealthy Chinese and East Asians have also poured money in smaller increments into local real estate projects via the EB-5 program that allows foreigners to get a green card in return for investing more than $500,000 in a local business and creating more than 10 full-time U.S. jobs. Syndicated EB-5 money has gone toward financing major New York projects such as the International Gem Tower on West 47th Street, a portion of Hudson Yards developed by Related Companies and Oxford Properties Group and the New York Wheel, the huge observation wheel under construction on Staten Island, to name a few.

Transitioning Market Forces

During the few short years from 2012 to 2015 Manhattan condo land values had more than doubled to values of $900 or more per square foot of zoning floor area. Since mid-2015, however, market headwinds have put a damper on land sales. These have included:

- Slower sales market for new condos (increased supply from new completions, declining number of contracts signed, and longer listing times leading to declining prices in many areas)
- Construction cost inflation that exceeds general CPI growth
- A Federal Reserve committed to raising its benchmark rates
- Increasingly skittish lenders with diminishing appetites for new condo developments that has resulted in higher interest rates and lower levels of funding against project costs
- Loss of the 421a tax abatement program in 2015 that was renewed in April of 2017, albeit with far more restrictions
- A divisive Presidential election that has presented uncertainty for tax policies, the economy, and global relations both during, and continuing after the election

The impact of these forces has been chronicled by reports and quotes from leading brokers. They note that land sales activity has been down for nearly two years. The decline in activity is evidenced by:

Bids for land that are typically 20.0 percent to 30.0 percent lower than where they were in the second quarter of 2015

- A 40.0 percent to 50.0 percent drop in the number of annually completed deals since mid-2015
- A 70.0 percent reduction in total dollar value of closed deals in 2016 from the prior year

Reflecting decisions by large-scale developers to remain on the sidelines at the market's current pricing metrics, the sales that are taking place are of a smaller scale and by less recognized participants. Also, with sellers typically slow to succumb to the new market realities, few have capitulated on pricing. The sales that are taking place often reflect market exceptions by idiosyncratic buyers who are either not in sync with the rational market, or strong enough to refute a seller's price.

Trends to Watch

Whether the market is reflecting an adjustment or a more prolonged correction remains to be played out. The outcome will certainly be influenced by factors such as:

› How fast and by how much the Federal Reserve raises its base rates, as well as the extent of the correlation between Fed policy and lender rates for both development and condo purchases. As a result, also watch condo unit sales trends going forward.

› The state of political and economic conditions at the global level.

› The future of the EB-5 program for bringing foreign capital to New York, and whether or not foreign investors perceive New York as becoming too expensive and they begin to seek diversification for better risk-adjusted returns in other markets.

AVISON YOUNG

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Retail Leasing

State of the Retail Market

There is no shortage of articles in the trades predicting the death of brick and mortar retail. We all read how the pessimists point to more vacant stores and bankruptcies as household retail names fall like dominoes. In addition, it is very easy to point to the doubling of money spent on e-commerce as the cause, and simply say the end is near for brick and mortar.

Even though consumers spend twice as much online today as they used to, that number is still less than 15.0 percent of total consumer spending. The numbers are likely to rise, but there is still and will likely always be market share to be gained with physical locations.

The New Retail Store – The Showroom

Let's begin by admitting that brick and mortar will survive, but under new conditions than it has before. For apparel tenants, retail will be used mostly as a showroom. New customers can size the clothing and touch and feel the merchandise, but in all likelihood, end up placing orders online or have the items shipped to their home from an order placed at the store. The new retail store is the tenants' opportunity to capture the consumer's attention, by creating the desired experience to maximize retention and brand recognition.

Because of this, the showrooms are in all likelihood going to be more of a destination, requiring fewer and smaller locations in each city. The demand for space has and will decrease, which will stabilize the rents. Now we are seeing tenants that historically couldn't afford large space become the most active in today's market: food and fitness. In fact, the two largest deals of this past quarter are food halls: Cipriani leased 28,000 square feet at 30 Riverside Boulevard, and Union Fare signed for 21,000 square feet at 282 11th Avenue.

The 800-Pound Gorilla

Amazon is the 800-pound gorilla shaking up any industry it sinks its teeth into. Through automation, technology and innovation, they capture an exorbitant amount of the market share. But if brick and mortar is dead, why would Amazon be opening book store concepts, entering the grocery/supermarket business with Amazon Go, and mostly recently purchase Whole Foods for $13.7 billion this past quarter? It will be no surprise, after a certain period of time that the Amazon Wardrobe concept debuts in a physical location, much like Trunk Club which operated exclusively online until opening its first store on Madison Avenue in New York in 2014.

New Age Adaption

There is a balance between e-commerce and brick and mortar, where they can work hand in hand and complement one another. Our traditional retailers are still figuring it out. Newer innovative companies such as Warby Parker and Untuckit are active in their roll-out strategies, with the latter signing at 488 Madison Avenue during this quarter. Also after attending ICSC's RECon in Las Vegas in May, which saw a 4.0 percent increase in attendance year over year, the future of retail looks bright as long as one pays careful attention to trends and market activity and adapts to the new age.

Notable Market Quotes

"But good enough isn't good enough anymore in retail. Yes, some of that attrition is attributable to e-commerce, but more often than not it's stagnant management and brands and concepts that have had their day in the sun. Clearly, there's an evolution of platforms, and the higher responsibility to deliver a more vibrant customer experience has put a lot of these companies out to pasture."
– Shane Garrison, EVP, CO and CIO at RPAI

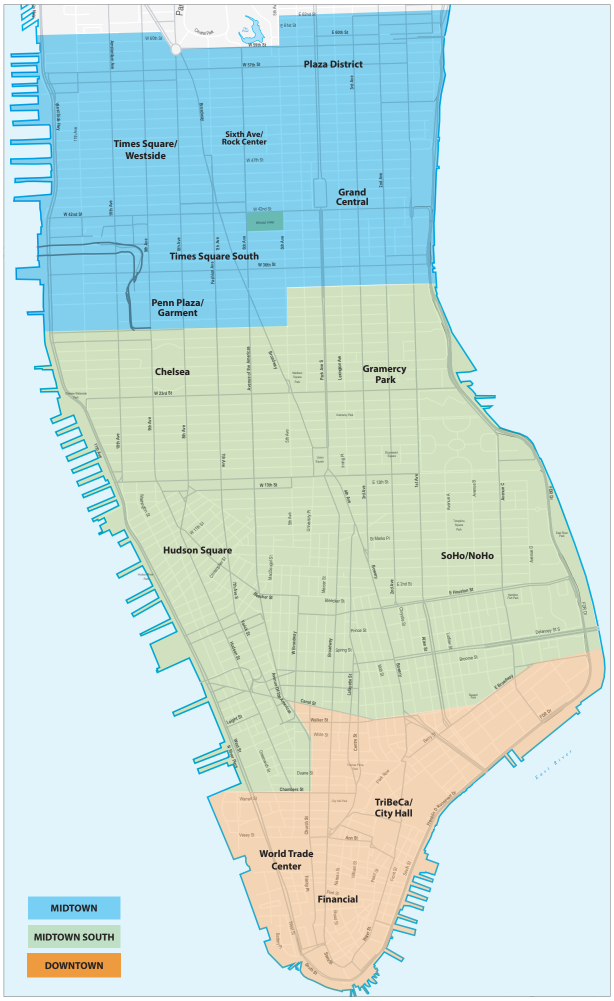
"When the dust settles, Manhattan will become a city of exciting showcase experiential stores, from existing retailers to online and other non-traditional retailers, dealing directly with the consumer who already has an understanding of the particular product."
– Jedd Nero, Principal and Executive Managing Director, Avison Young

"Experiential retail is here, and people need to focus on it, and people need to find a way to drive traffic."
– Mark Rose, Chairman & CEO, Avison Young

Trends to Watch

- Innovation and technology continues to shape not only how customers shop, but also how retailers do business
- Large retail companies look to purchase newer more successful models to help drive change and increase their market share. The most recent example is Walmart's announced $310 million acquisition of the men's clothing company Bonobos.

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 (includes Hudson Yards and Manhattan West)

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 6th 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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Second Quarter 2017

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