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Indianapolis office market report

Q3 2021

AVANT
by AVISON YOUNG

Key takeaways



Economic conditions

- Indianapolis unemployment rate of **3.7 percent** as of August 2021 was back to 2017 levels with persistent downward pressure since May 2020.
- Historically new record labor market conditions were halted by the pandemic with nearly **163,409 job losses** between February and April 2020. Resiliency of the Indianapolis market appeared quickly after initial shock of pandemic as the economy has **added 19.4 percent** job growth since April 2020.



Recovery rate

- City of Indianapolis vaccination rate of **48.7 percent** far below national average, however full MSA rate of **53.5 percent** was on par with national trends; this may be preventing office-using workforce from fully returning to pre-COVID rates, showcasing lagging recovery of **4.9 percent** compared to general economy of Indianapolis increasing **0.6 percent**.



Office demand

- Leasing activity has reduced, decreasing by **51.8 percent** compared with long-term historical averages.
- Negative absorption surpasses the lows of the early 2000's recession of **-1.8 percent** from 2020 through the third quarter at **-3.7 percent**. Current trending does mirror the post dot-com recession, which experienced a significant upshoot to enter a new cycle.

Key takeaways



Office supply

- The Q3 2021 **vacancy rate** has surpassed the highs experienced in the Global Financial Crisis in terms of direct and total percentages at **20.2 percent**, with sublease rates trickling upward.
- The sublease market is still not at historical records, accounting for **3.6 percent** of all vacant space. However, with recent announcements by large tenants reevaluating their space needs, this number is expected to continue to increase in the near-term.



Pricing trends

- Asking rents have **remained stable** since the beginning of COVID, however this is largely due to **inactivity** in the market. Landlords have not yet had large tenant considerations since the beginning of COVID, with **increasing sublease space** entering the market asking rents are expected to **decline in the near-term**.



Capital markets

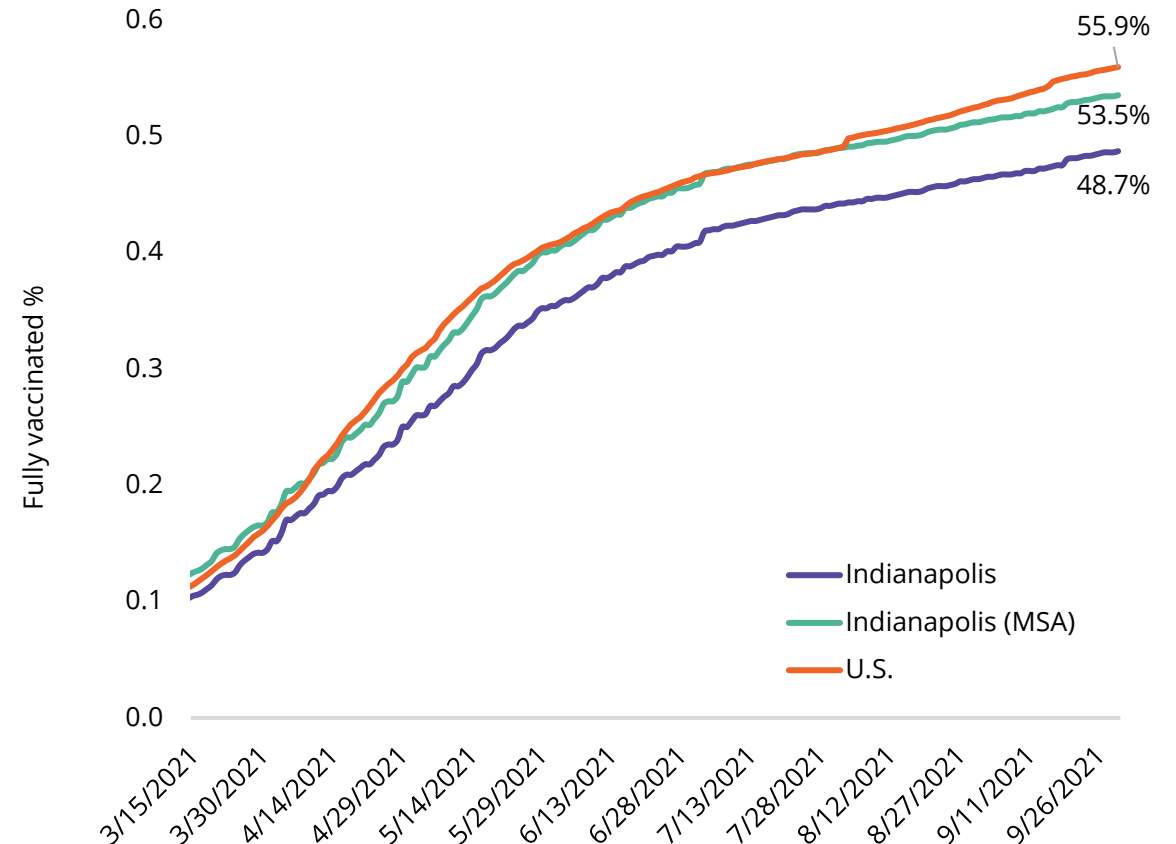
- Office sales activity remains **consistent** during since just before the pandemic, decreasing by only **6.8 percent** compared with the prior five-year average dollar volume.
- Office sale pricing remains **stable** throughout the pandemic, hovering around **\$140/psf**, just below the pre-pandemic levels set in 2019 of **\$146/psf**.

Vaccination rates

53.5%

Share of total Indianapolis MSA population that is fully vaccinated

Within Marion County, vaccination rates fall well under U.S. averages, with broader adoption for the surrounding counties of the Indianapolis MSA.



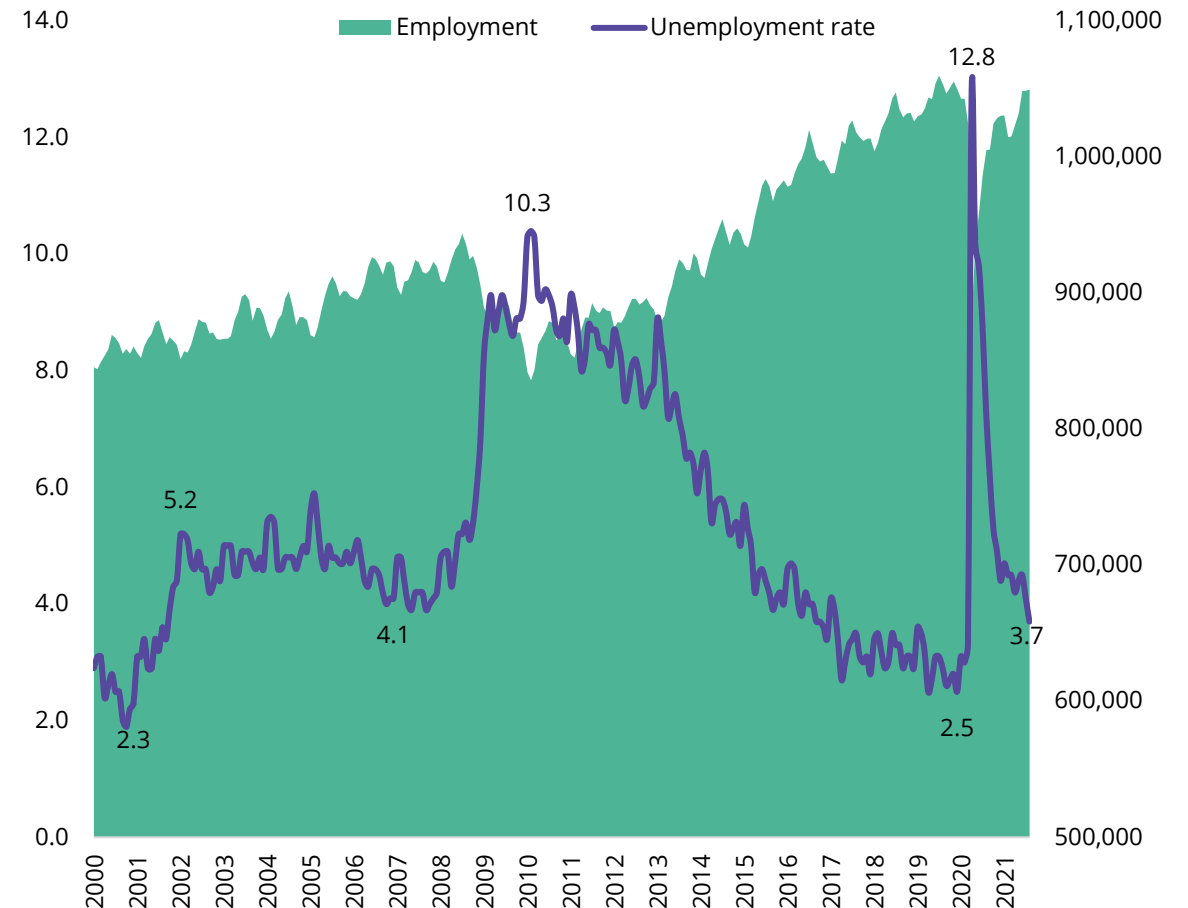
Source: CDC

Employment and unemployment rate

3.7%

Indianapolis unemployment rate as of August 2021, dipping below 4.0% for first time since COVID

Historically tightened labor market conditions were temporarily paused by the pandemic with 163,409 job losses between February and April 2020. However, Indianapolis' employment has since surged, and now has nearly 7,000 more employed than just prior to the pandemic.



Note: Not seasonally adjusted data.
Source: Bureau of Labor Statistics

Office-using job gains and losses

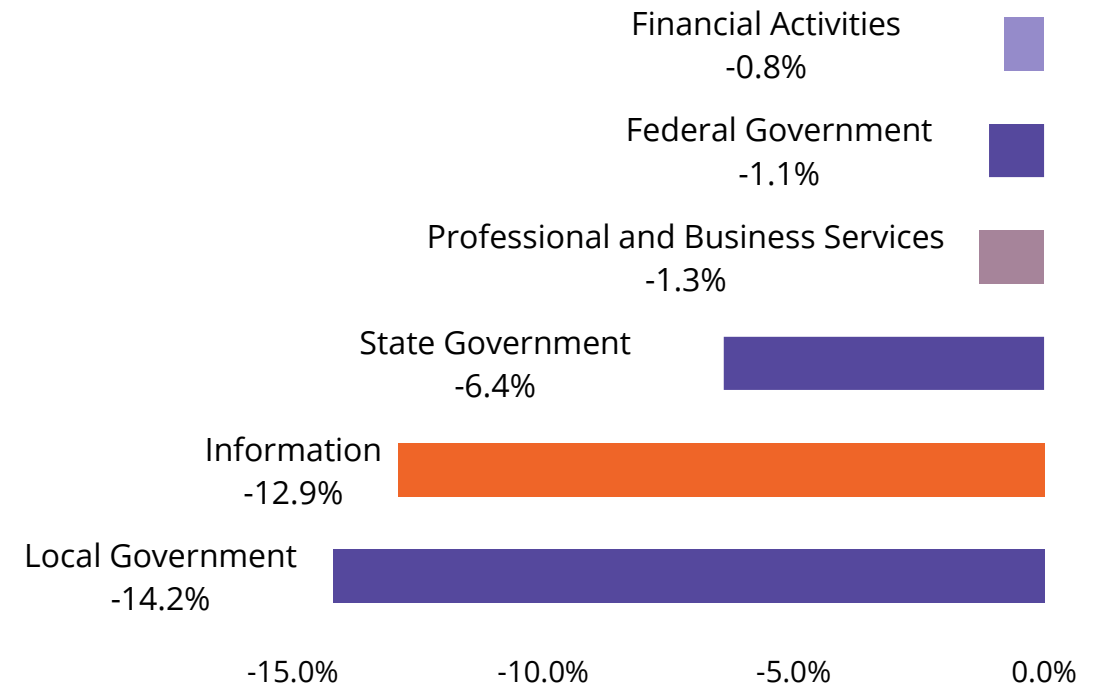
-4.9%

Change in office-using employment during the pandemic

Indianapolis MSA job losses have increased by 0.6% since the start of the pandemic, though office-using jobs contracted by 4.9%. This recession's impact on the MSA was severe and quick, however the resiliency of Indianapolis continues to exhibit positive momentum. The office-using labor market has been slower to recover.

Total change in Indianapolis MSA* job gains/(losses)

February 2020 to July 2021



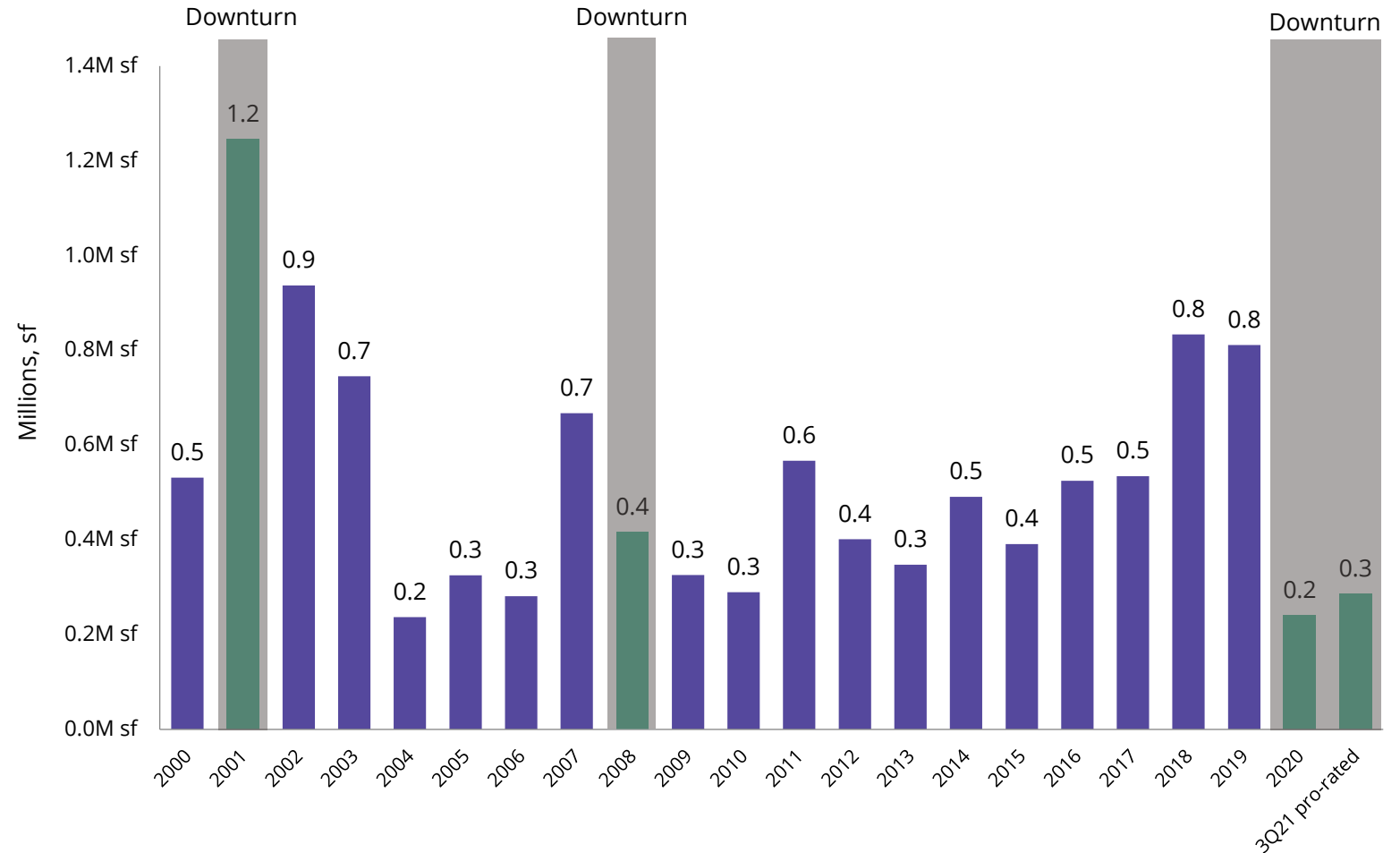
Note: Not seasonally adjusted data. Metropolitan statistical area.
Source: Bureau of Labor Statistics

Office leasing activity

-51.8%

**2020-pro-rated 2021 vs.
prior 20-year annual
average leasing activity**

There is no modern precedent for the post-COVID slowdown in leasing activity—not 2001 nor 2008—due to the sudden change in office occupiers' future workplace strategies and the 2020 recession.

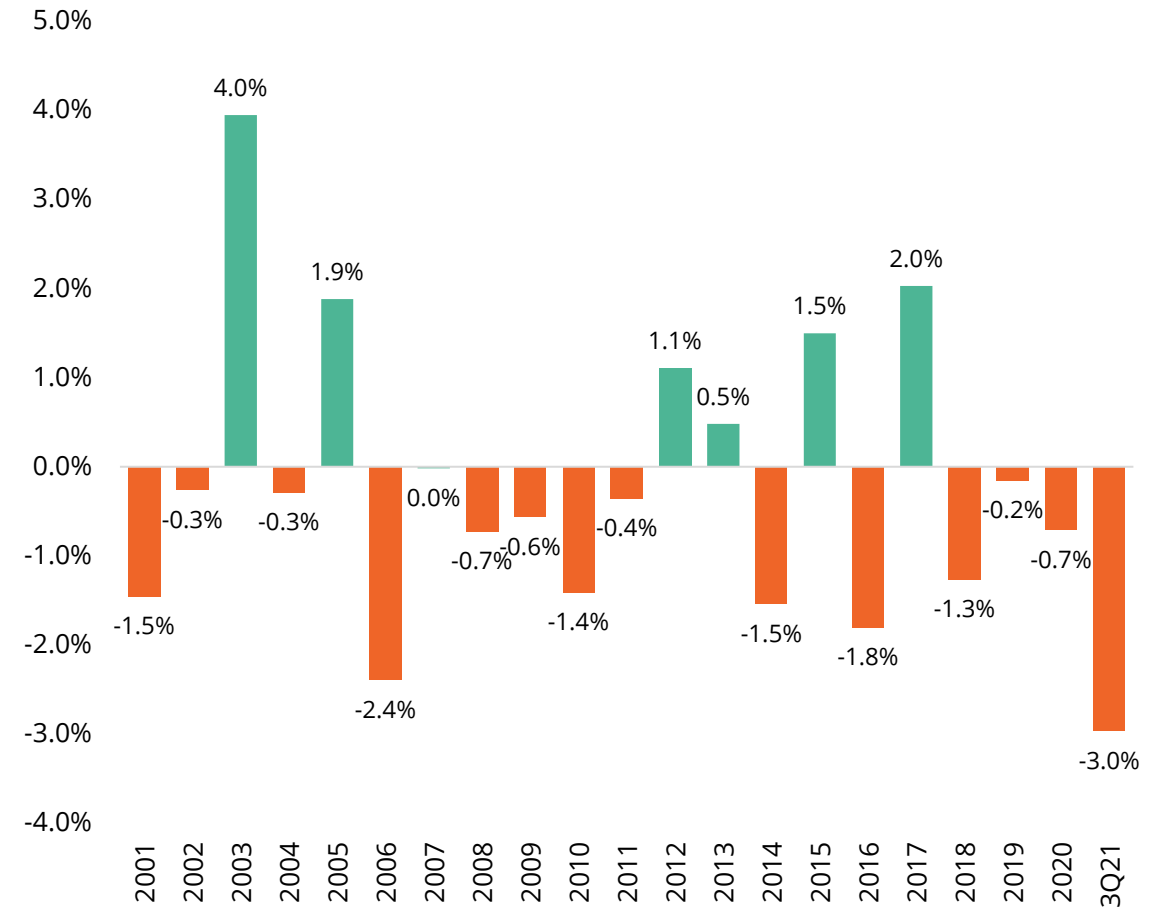


Source: AVANT by Avison Young

-3.7%

Net absorption as a percentage of inventory, 2020 through Q3 2021

Negative absorption from 2020 to 3Q21 has totaled 371.7 thousand sf, totaling -3.7% of the existing stock. This negative absorption surpasses the lows of the early 2000's recession (-1.8%) and is worse than the global financial crisis.



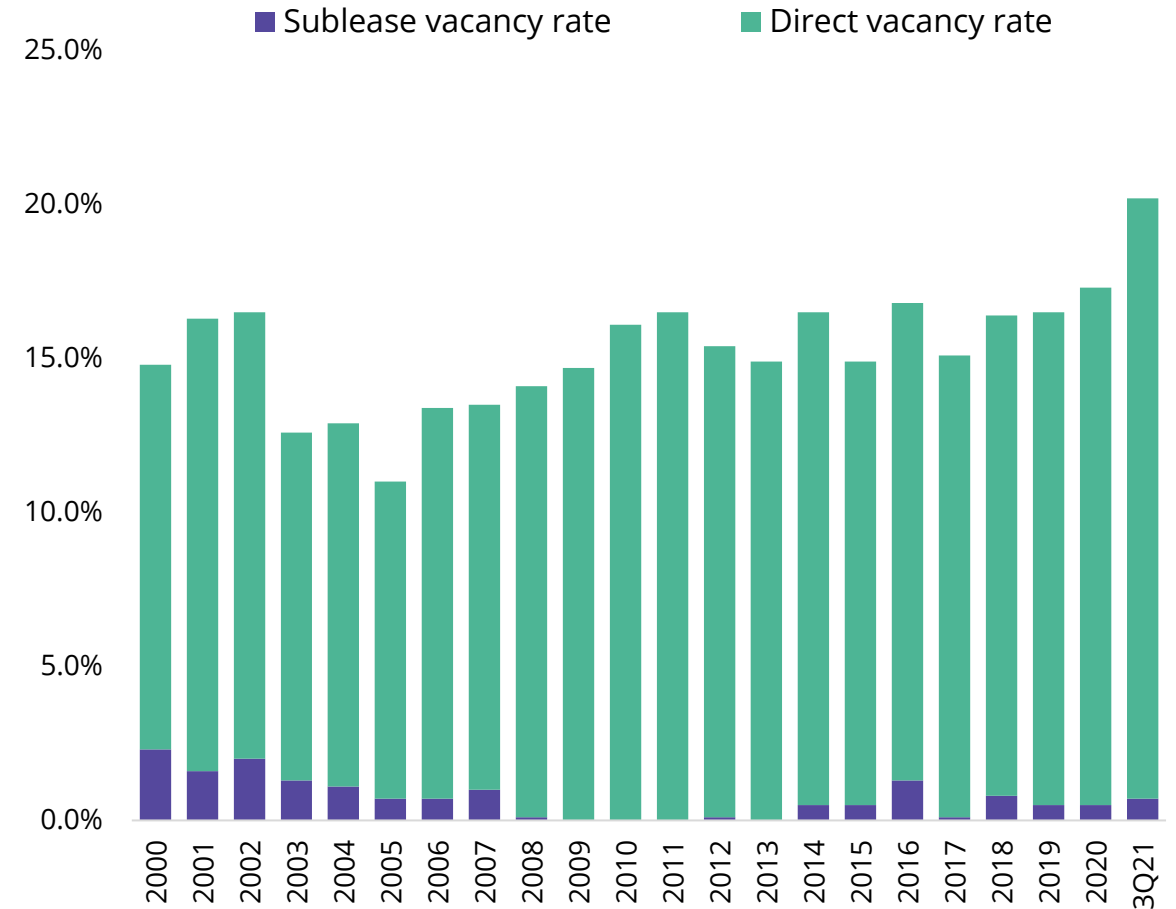
Source: AVANT by Avison Young

Vacancy rate

20.2%

Highest Indianapolis vacancy since the Global Financial Crisis

The Q3 2021 vacancy rate is on par with the midst of the Global Financial Crisis in terms of sublease, direct and total percentages. Asking rents continue to remain resilient, however this could be an aspect of limited activity in the leasing environment, as near-term availabilities appear to be on their way to the market.



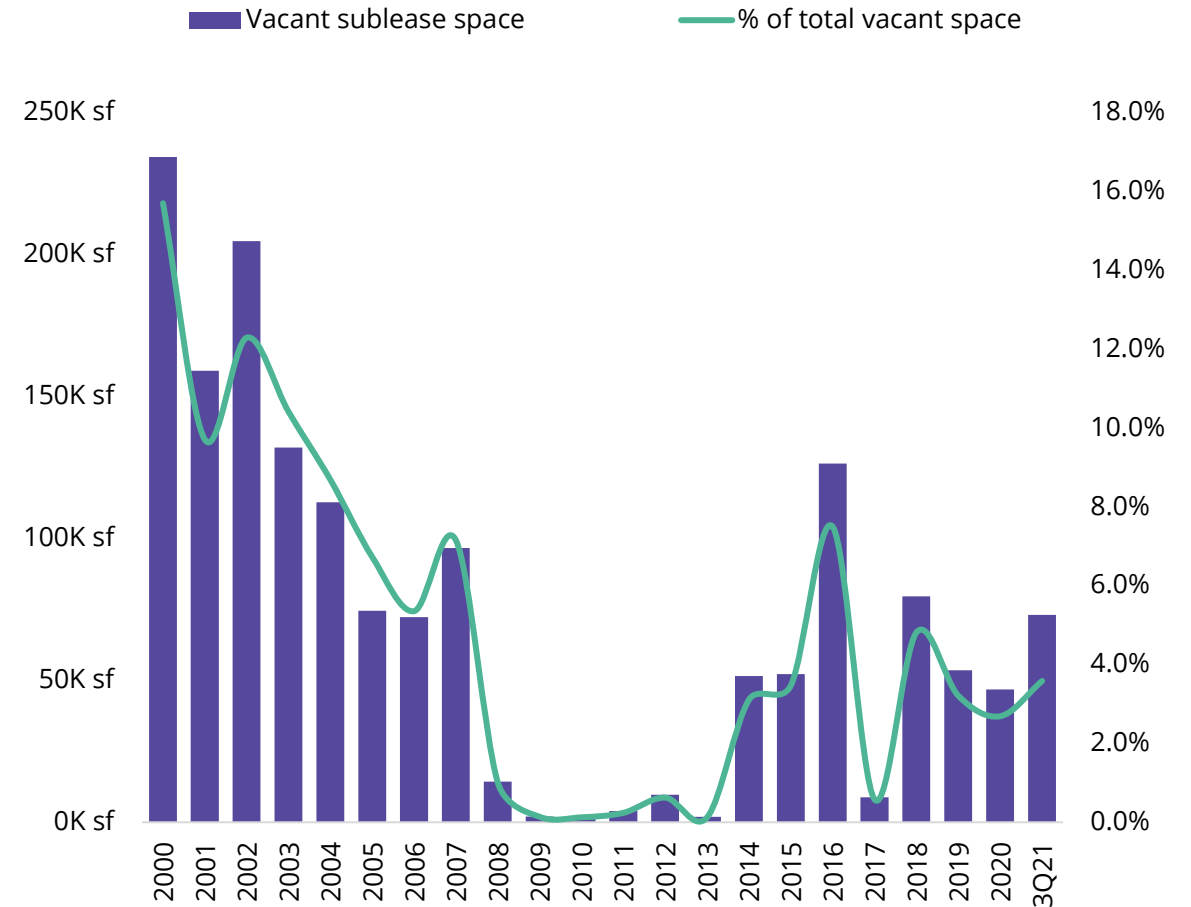
Source: AVANT by Avison Young

Vacant sublease space

73.1 ksf

Sublease vacant space is rising, and expected to continue to increase

The share of sublease-to-total vacant space of 3.6% and rising is nearing levels of the period following 2001 due to 9/11 and the Dot-com Recession. This trend is expected to continue into 2022 as the return to work has users reevaluating their office footprints.



Source: AVANT by Avison Young

Office development pipeline

24 properties

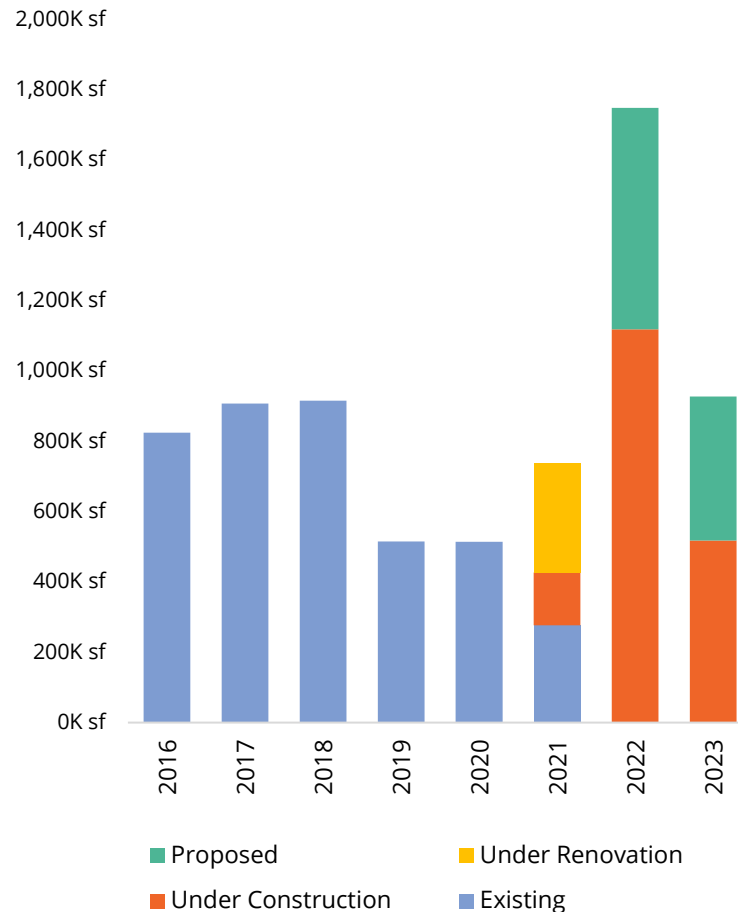
proposed or under construction

2.1 msf

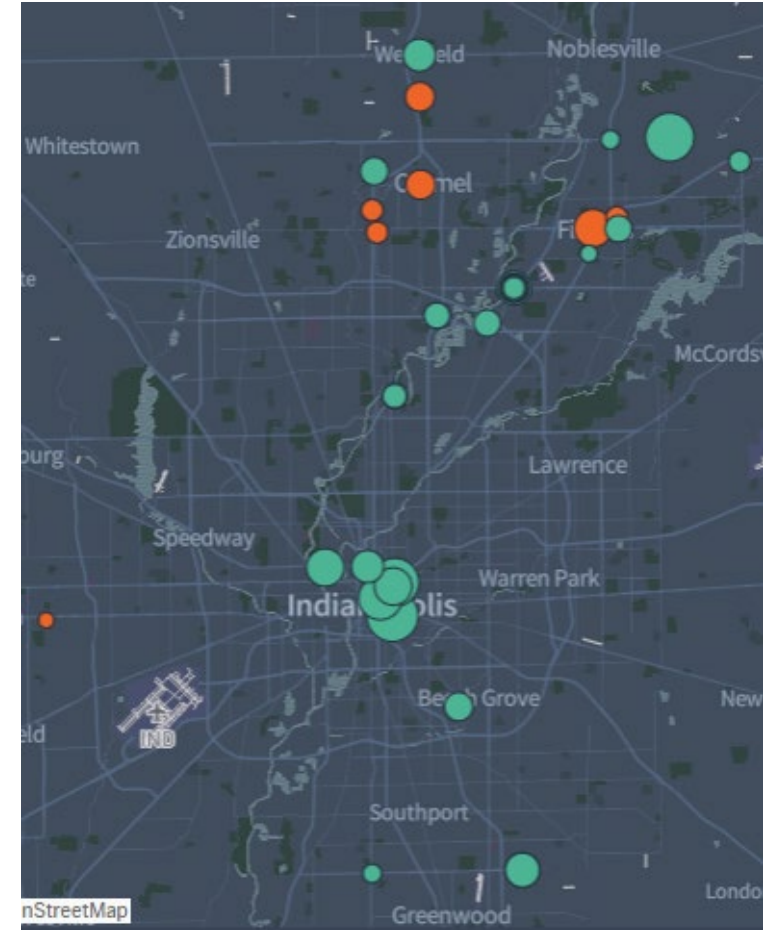
proposed or under construction

2.5%

share of office inventory



Source: AVANT by Avison Young

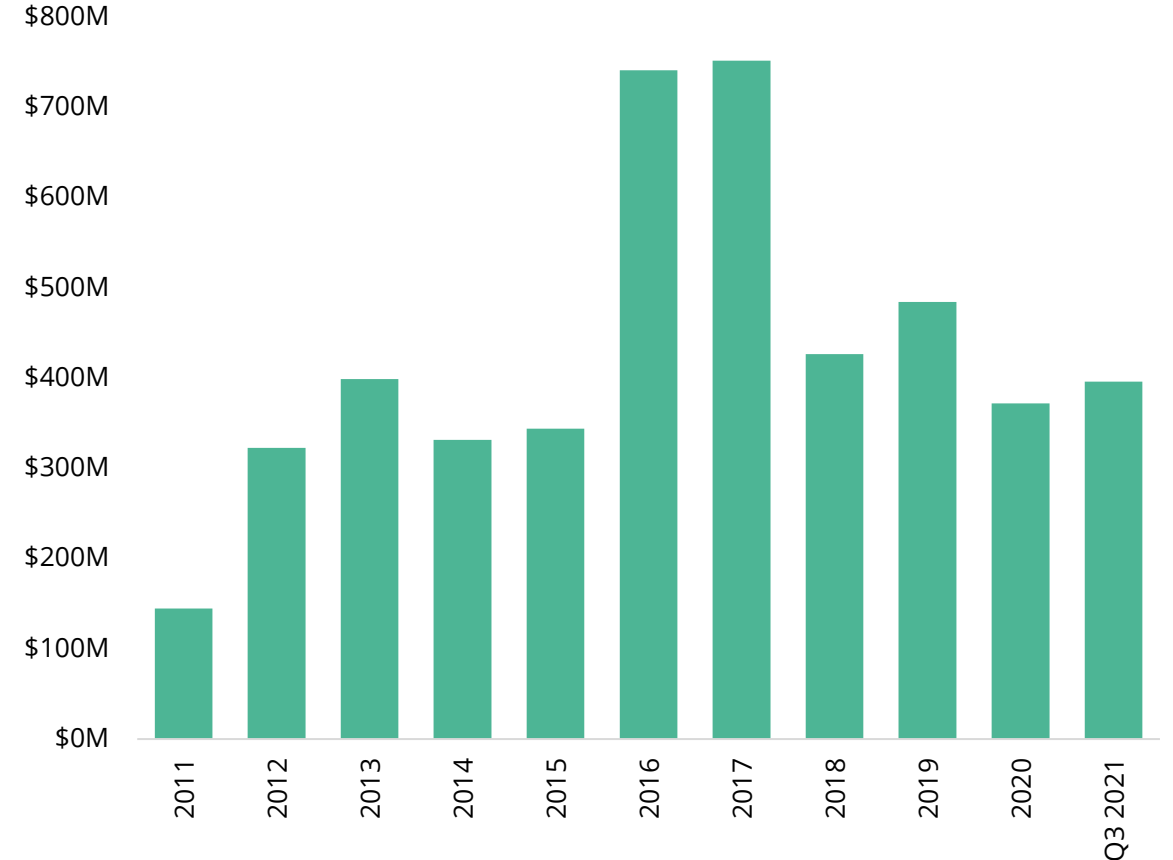


Office investment dollar volume

\$767.5M

Indianapolis office dollar volume 2020 to present

Office sales activity remains consistent during since just before the pandemic, decreasing by only 6.8 percent compared with the prior five-year average dollar volume. This is largely distorted, however, by the first quarter closing of Salesforce Tower for \$192.5M.



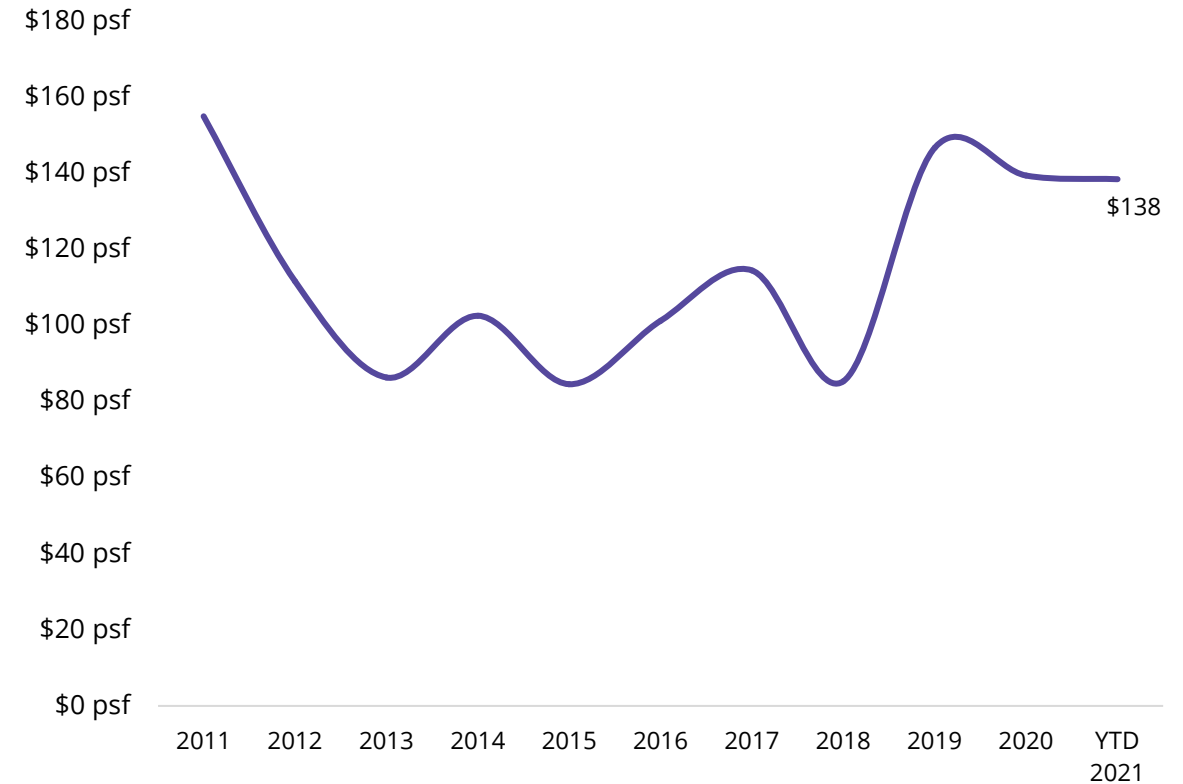
Source: AVANT by Avison Young,

Office asset pricing

-5.6%

Indianapolis office pricing from 2019 to present

Pricing softened slightly during the pandemic, however, has remained stable for nearly two years hovering around \$140/psf. Investment activity has been near average since the start of the pandemic, and is expected to remain relatively flat through 2022.



Source: AVANT by Avison Young

Looking forward



Here's what we can expect

- **No new construction in CBD**, is assisting the market from becoming overwhelmed by a new round of availabilities in an already softened environment. This trend is expected to continue as **construction costs continue to climb** to record levels, and lead-time for steel is 6-8 months.
- There is currently **no movement in rental asking pricing**, despite activity being flat, decreasing requirements, and vacancy increasing due to the low levels of activity in the market. When **activity begins to pick-up** as companies execute their return-to-office strategies, the pressure of **competition between landlords** will likely drive tenant favorable terms.
- **Office sub-leasing supply is incrementally rising and** will be a key area of focus for proving out the strength of the market. All eyes will be on **leasing activity** in the next 3-6 months, as tenants execute on a variety of strategies for their return-to-office space needs and define what that will mean in terms of transaction activity.
- **Asset pricing remains stable and is trending upward** as investors are focused on pursuing well-leased buildings in key locations throughout the market.



Looking forward



Here's what we can expect

- Recent announcements by some of the **largest employers** in Indianapolis will add **increased pressure** to the office market:
- **Rolls Royce** is giving back two-thirds of their total office space (~**270.0K sf**) due to COVID-related reevaluation of remote workforce. Implementing workforce return to office in **January, pushed back** from planned **Sept./Oct.**
- **Eli Lilly** has announced a pushback in planning their workforce **full office return** from **September to November** due to Delta variant concerns
- **Salesforce** will allow hybrid work **indefinitely**, leaving **uncertainty** on their future office space needs.
- The city of Indianapolis completed a **new Justice Center** which opens in **Fall, 2021**; this moves the correctional jail from CBD to nearby suburb, with courts scheduled to open in 2022. Currently there are around **100.0K sf** of “public defender’s offices/prosecutors offices/bail-bondsmen/public attorneys” offices in CBD. This move will likely alter office use and activity in this area by 2022. There is **no real office inventory** where Justice Center is being moved to, so many law offices are waiting to see what happens.
- **Large positive trend** in market is the recent accouchements of **inbound Biotech/Pharmaceutical** users aggregating around the **Fishers area**. This may lead to a clustering of Life Science users in the Indianapolis area.



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Let's talk

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