Manhattan office market insights

Q3 2022

AVISON YOUNG

Key office takeaways

Recovery rate

- Manhattan is ranked the **#7 office market in the U.S. in terms of return-to-office efforts at 46.0%**, compared with the same week in 2019 (pre-COVID).
- While Manhattan return to office was slightly weaker than last quarter, **Manhattan return to office levels are currently 5.7 percentage points above the U.S. market average.**

Office demand

- Leasing activity in Q3 2022 reached 8.1 million square feet (msf), up 17.4% from Q2. **Year to date (YTD) leasing activity is 19.9% greater than Q1-Q3 2021.**
- **Q3 2022 net absorption has achieved its highest quarterly post-COVID value at positive 641,000 square feet (sf).** This is well above the post-COVID average quarterly net absorption of -2.9 msf.
- **From Q1 through Q3 2021, 20 deals over 100,000 sf were signed. From Q1 through Q3 2022, 33 deals over 100,000 sf have been signed** – signifying that larger tenants are navigating the market with more conviction, which could lead to stronger activity by follow-on tenants.

Office supply

- The **total availability rate has seen its first quarter-over-quarter decrease to date in 2022, sitting at 18.4% in Q3 2022.** The sublease availability rate has remained at 4.5% (23.3 msf) from Q2 while the direct availability rate decreased 20bp to 13.9% (95.8 msf) from Q2.
- A significant amount of new construction, including renovation projects, **totaling 6.2 msf, will be delivered by year-end 2022, 3.1 msf of which is pre-leased.** This may cause a temporary increase in vacancy rates.

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Key office takeaways

Pricing trends

- In an effort to compete with Trophy properties, landlords of **class A properties** are offering historically large concession packages, causing **the gap between base and net effective rents to widen from $9.83 psf to $18.18 psf (March 2020 to September 2022).**
- Class B and C properties, while still struggling to compete with higher quality assets, have seen stronger demand than last quarter. **Class B and C net effective rents are 4.9% higher than in March 2020.**
- **Trophy net effective rents continue to rise, currently surpassing March 2020 levels by 15.0%.**

Capital Markets

- **Investment activity in Q3 has slowed compared to Q2 ($670M vs $959M).** This can be attributed to rising interest rates that are stressing asset values. As a result, we could expect a continuing slowdown in office investment activity in the coming quarters. There are, however, multiple large profile sales that are currently under contract that could help offset the slowdown for the rest of 2022.
- **The spread between office cap rates and 10-year Treasury rates of 150bp in Q3 2022** has compressed during recent quarters. This should inhibit demand for all but the most desirable, cash flowing properties given the rarity of that class of office properties coming to market.

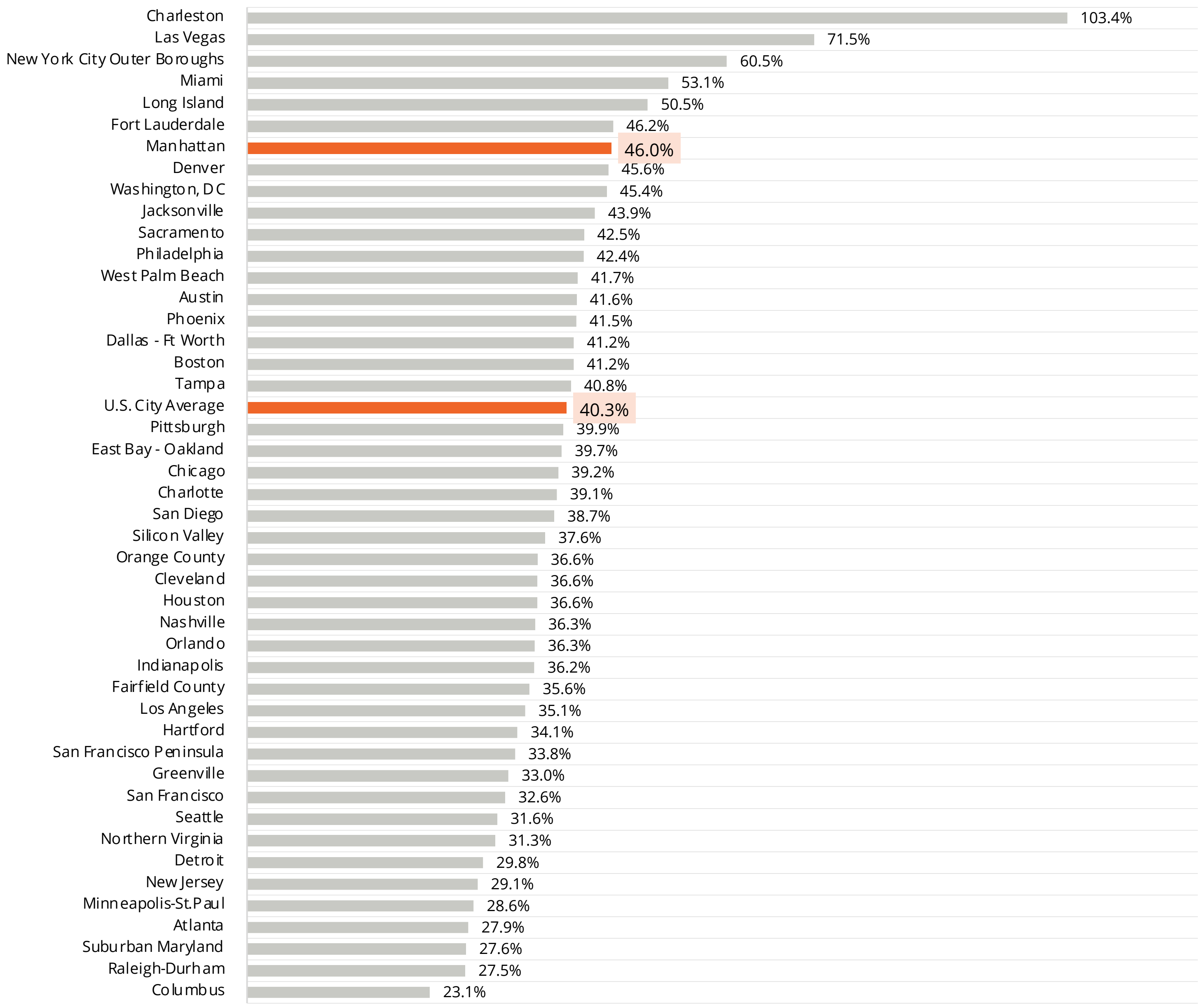
U.S. return-to-work rates since COVID

46.0%

Manhattan office visitor volumes, week after Labor Day 2022 vs. week after Labor Day 2019.

Manhattan return-to-office rates currently sit at just under half of pre-COVID levels, leaving only a few U.S. office markets ahead of Manhattan.

View vitality index



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

Manhattan visitor volumes by property

65.4%

Manhattan total visitor volumes, week after Labor Day 2022 vs. week after Labor Day 2019.

Overall Manhattan visitor volumes are at 65.4% of pre-COVID levels when comparing the week after Labor Day, largely attributed to education. As schools continue to return to pre-COVID normalcy, overall Manhattan visitor volumes will continue to rise.

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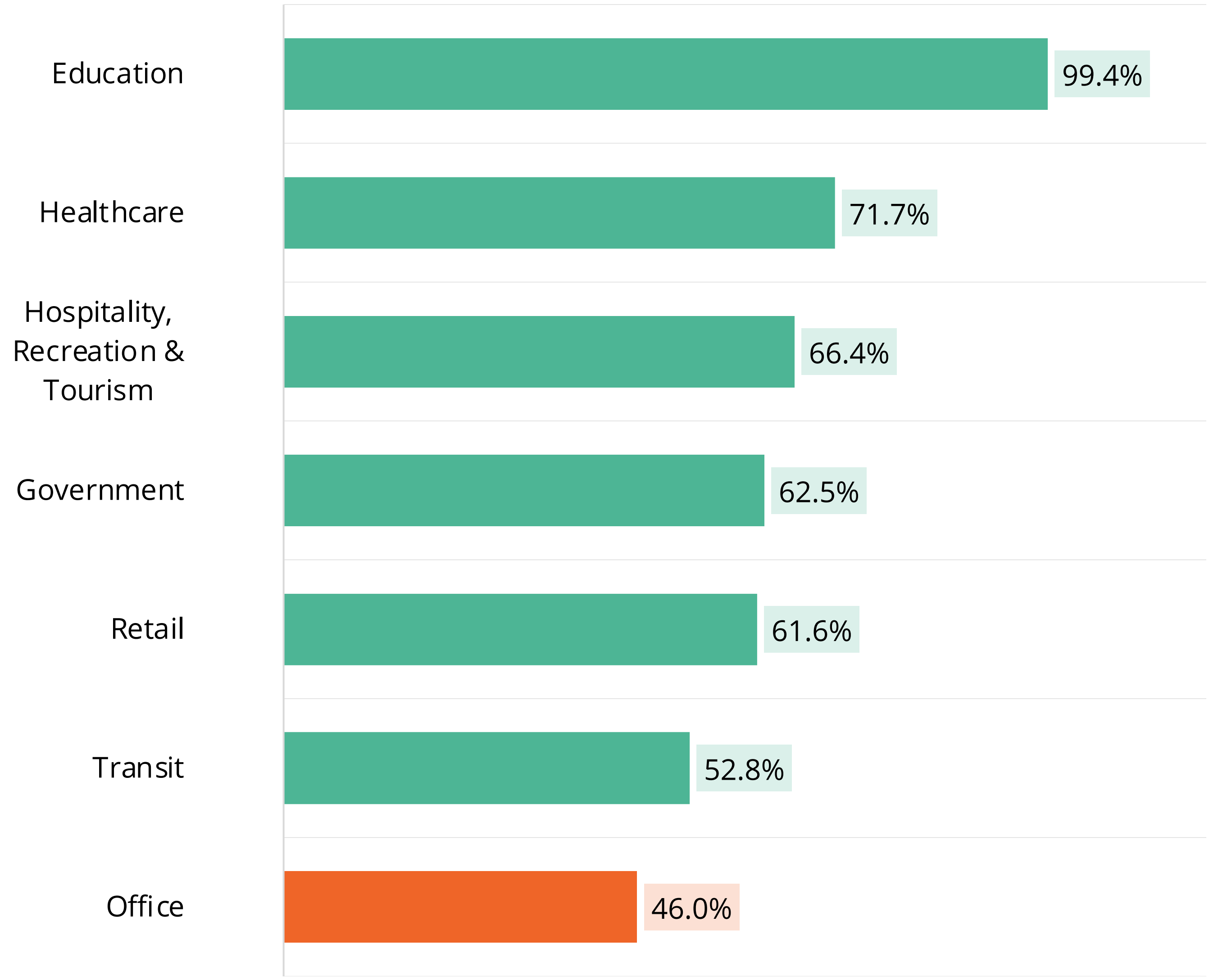

Note: Representative locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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Manhattan office visitor volumes

51.0%

average office visitor volumes of major industries*, week after Labor Day 2022 vs. week after Labor Day 2019.

Office visitor volumes for major industries in Manhattan continue their upward trend, currently at over half of pre-COVID levels.

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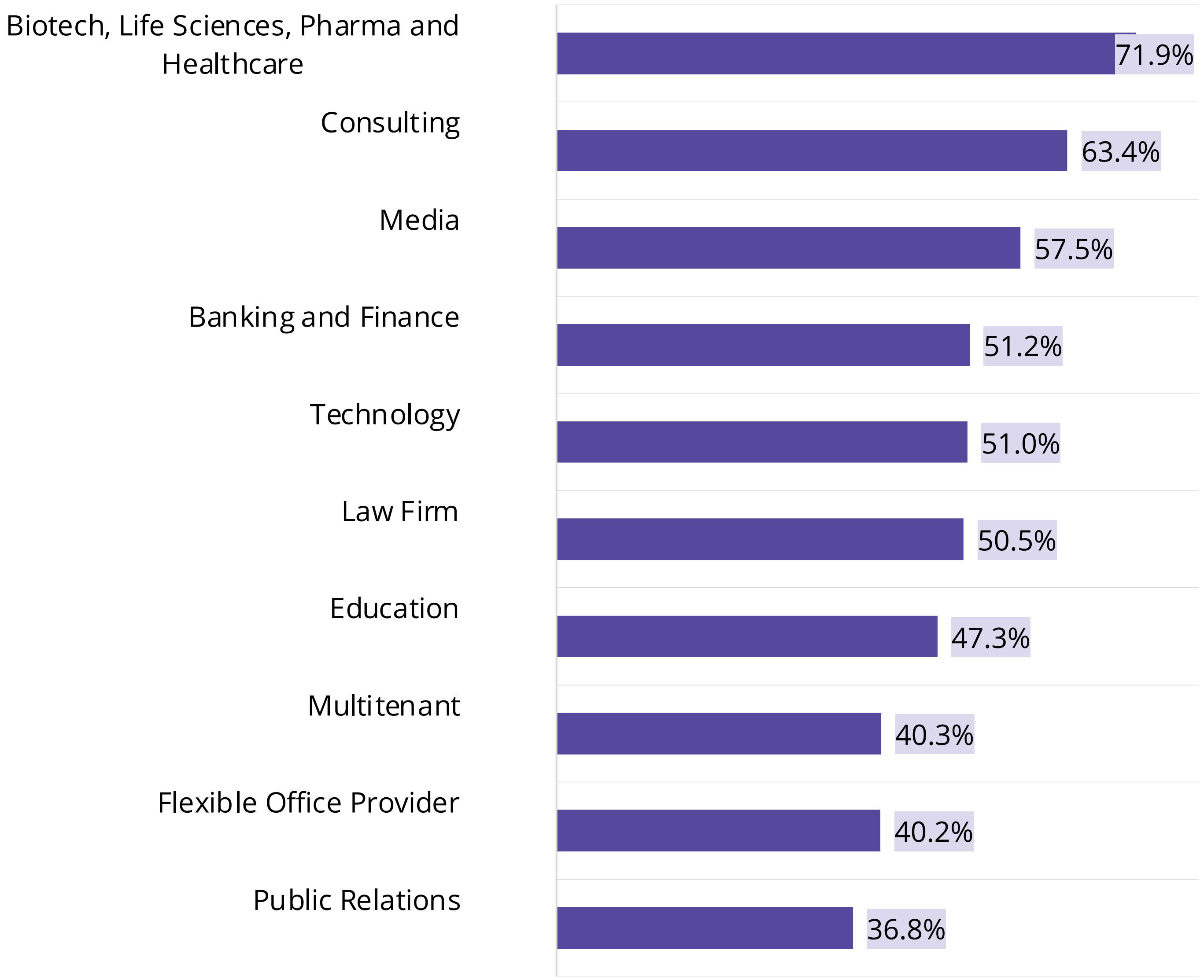

Note: Representative locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young
*Average of industries shown

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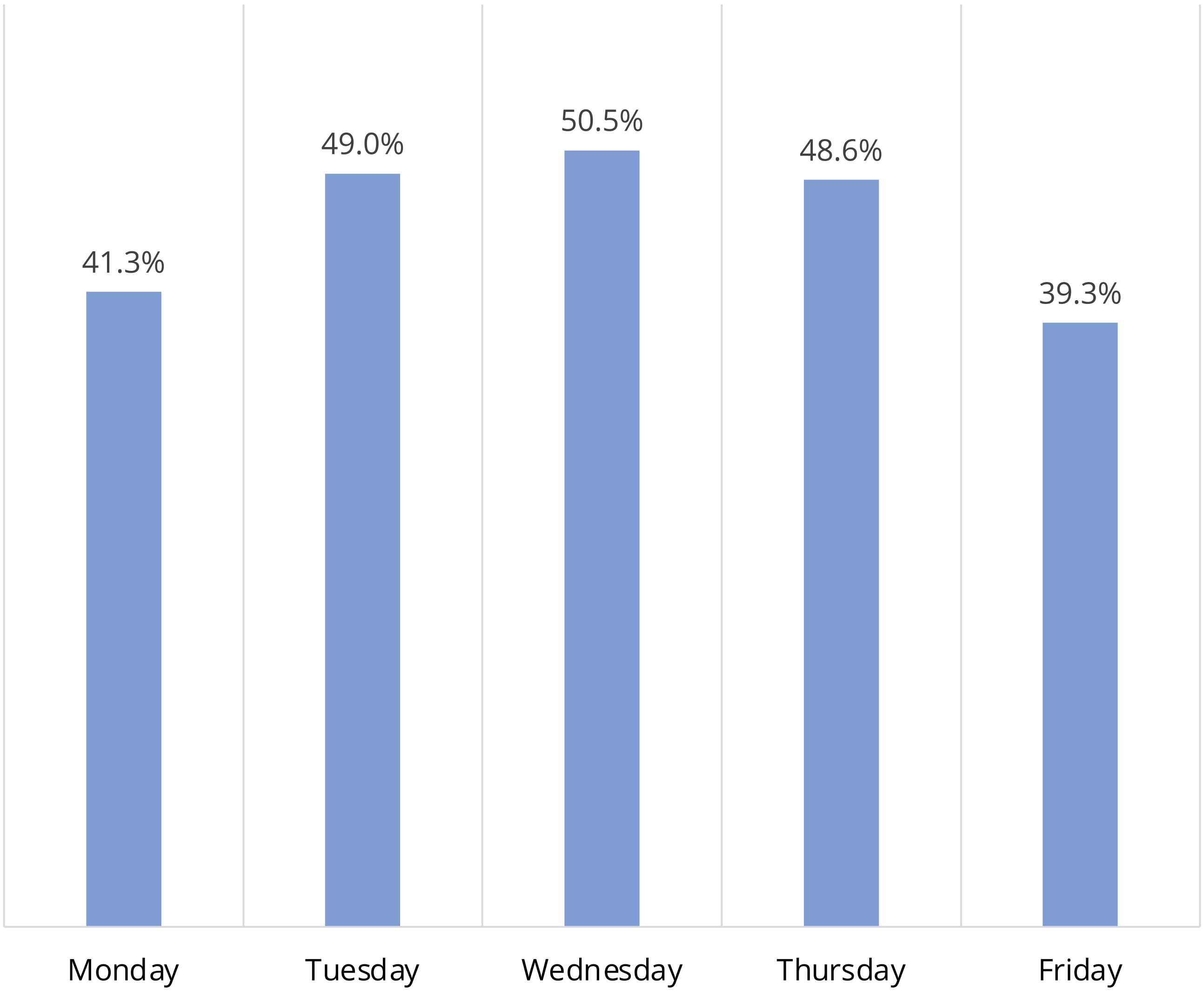
Manhattan return-to-office by weekdays

46.0%

Manhattan office visitor volumes, week after Labor Day 2022 vs. week after Labor Day 2019.

Midweek Manhattan office visitation increased to more than half of pre-COVID levels. Wednesday sees the strongest return to office, while Monday and Friday see the weakest.



Note: Representative fully occupied offices.
Source: Orbital Insight, AVANT by Avison Young

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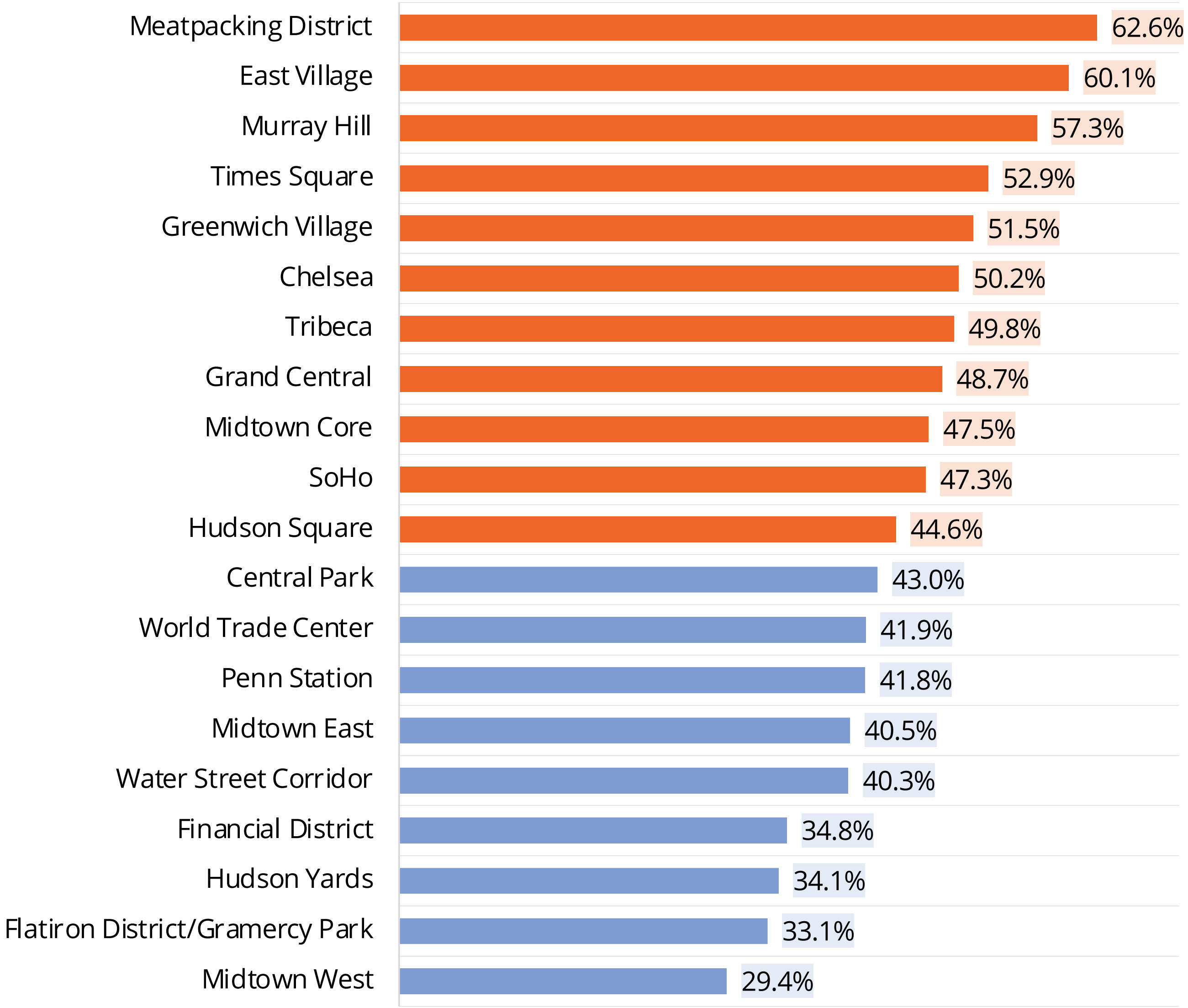
Manhattan return-to-office by submarket

56.1%

visitation at top submarkets, week after Labor Day 2022 vs. week after Labor Day 2019.

Offices located in mixed-use neighborhoods and in most transit-oriented districts have reported stronger office visitor volumes relative to peer submarkets.

Explore Vitality Index



Note: Representative fully occupied offices
Source: Orbital Insight, AVANT by Avison Young

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Post-COVID office activity heat map

More than 1,300 leases have been signed since April 2020 with Trophy and class A properties (top 25.0%) capturing 62.2% of the number of closed deals.

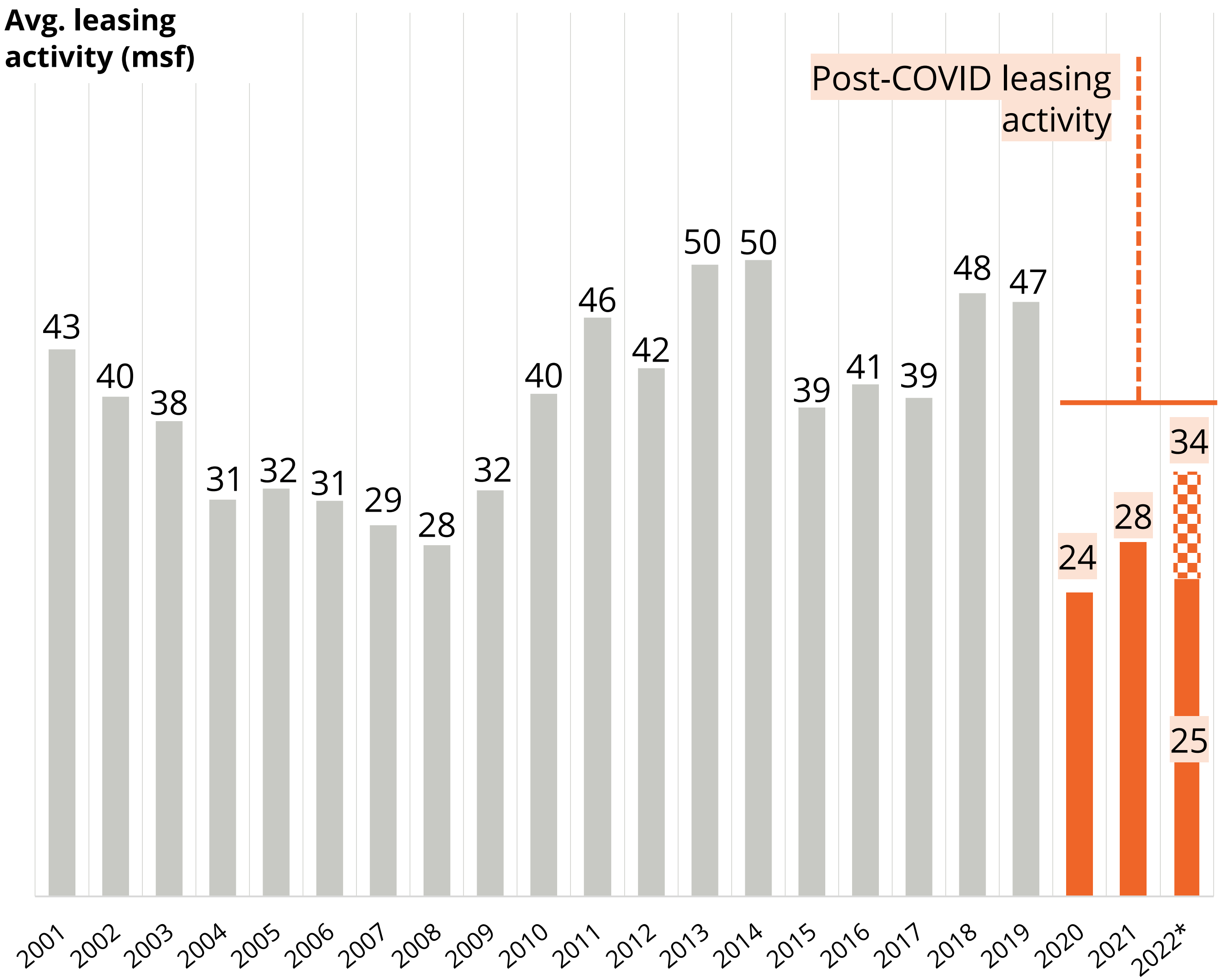
Source: AVANT by Avison Young

Office leasing activity

+19.9%

Q1-Q3 2022 vs. Q1-Q3 2021 Manhattan office leasing activity.

With 8.1 msf of leasing activity in Q3, YTD leasing activity through Q3 has outperformed 2021's leasing activity through Q3 (25.2 msf vs. 18.8 msf). With this rate of leasing activity, 2022 total leasing activity is expected to reach over 34.0 msf by year-end, which would outperform both 2020 and 2021. Through Q3 2021, 20 deals over 100K sf were signed. Through Q3 2022, 33 deals over 100K sf have been signed, showing that larger tenants are navigating the market with more conviction that could lead to stronger activity by follow-on tenants.



*2022 data prorated based on Q1 – Q3 2022
Source: CoStar

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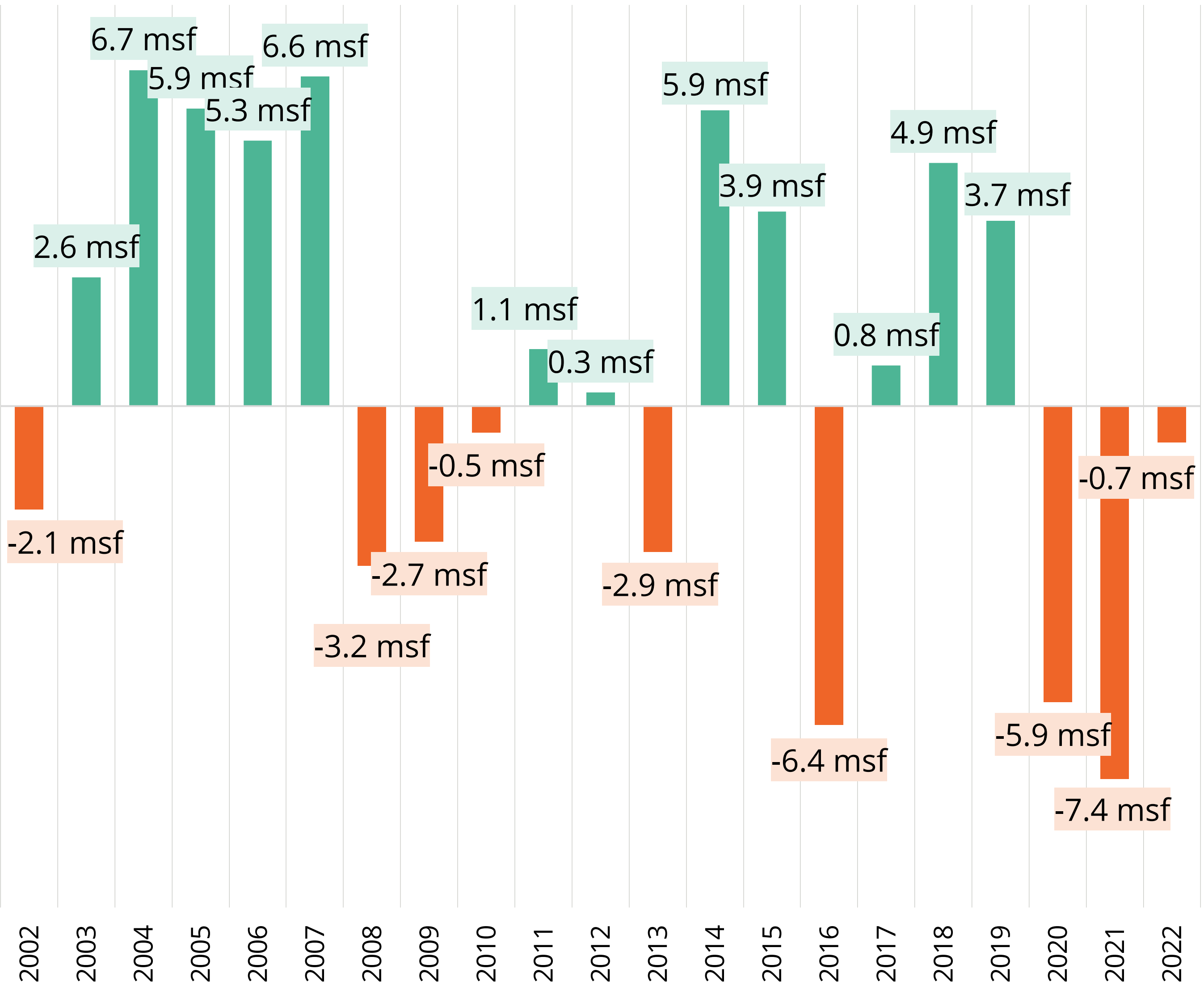
Net absorption

-0.7 msf

net absorption, YTD 2022.

Manhattan reported positive absorption in Q1 2022 (+0.1 msf) but regressed in Q2 2022, largely due to an abundance of new sublet space. In Q3, however, leasing activity picked up steam – resulting in a quarter of positive absorption. Q3 2022 brings YTD absorption up to approximately -700,000 sf.



Source: CoStar

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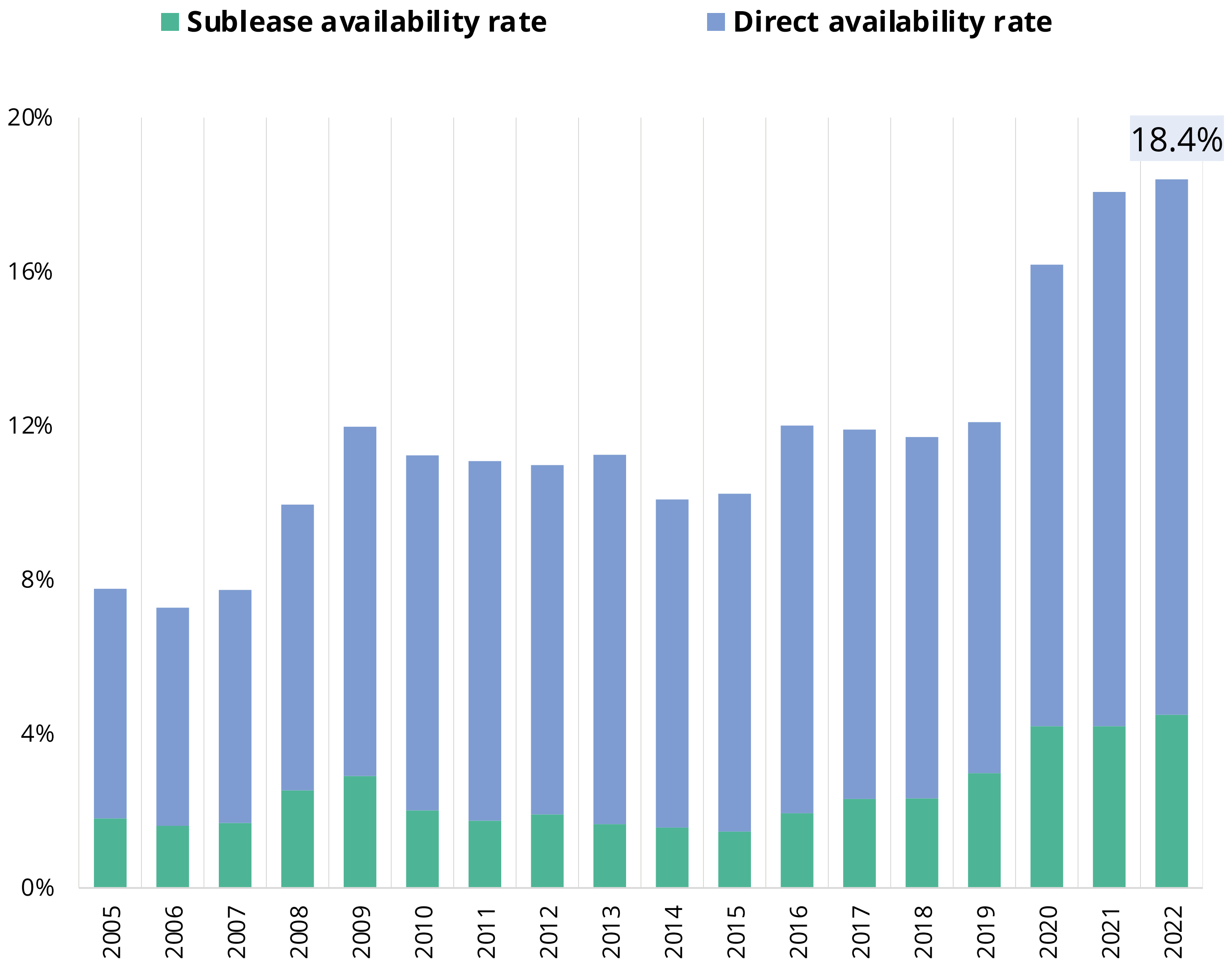
Office market availability rate

18.4%

total availability rate as of Q3 2022, down from 18.6% in Q2 2022.

Overall office availability has slightly decreased from 18.6% since Q2 2022, mainly as a result of direct available spaces declining. Direct availability rate has decreased by 20bp to 13.9%, while sublease availability rate remained at 4.5% from last quarter. This is the first quarter YTD where availability has declined quarter-over-quarter.



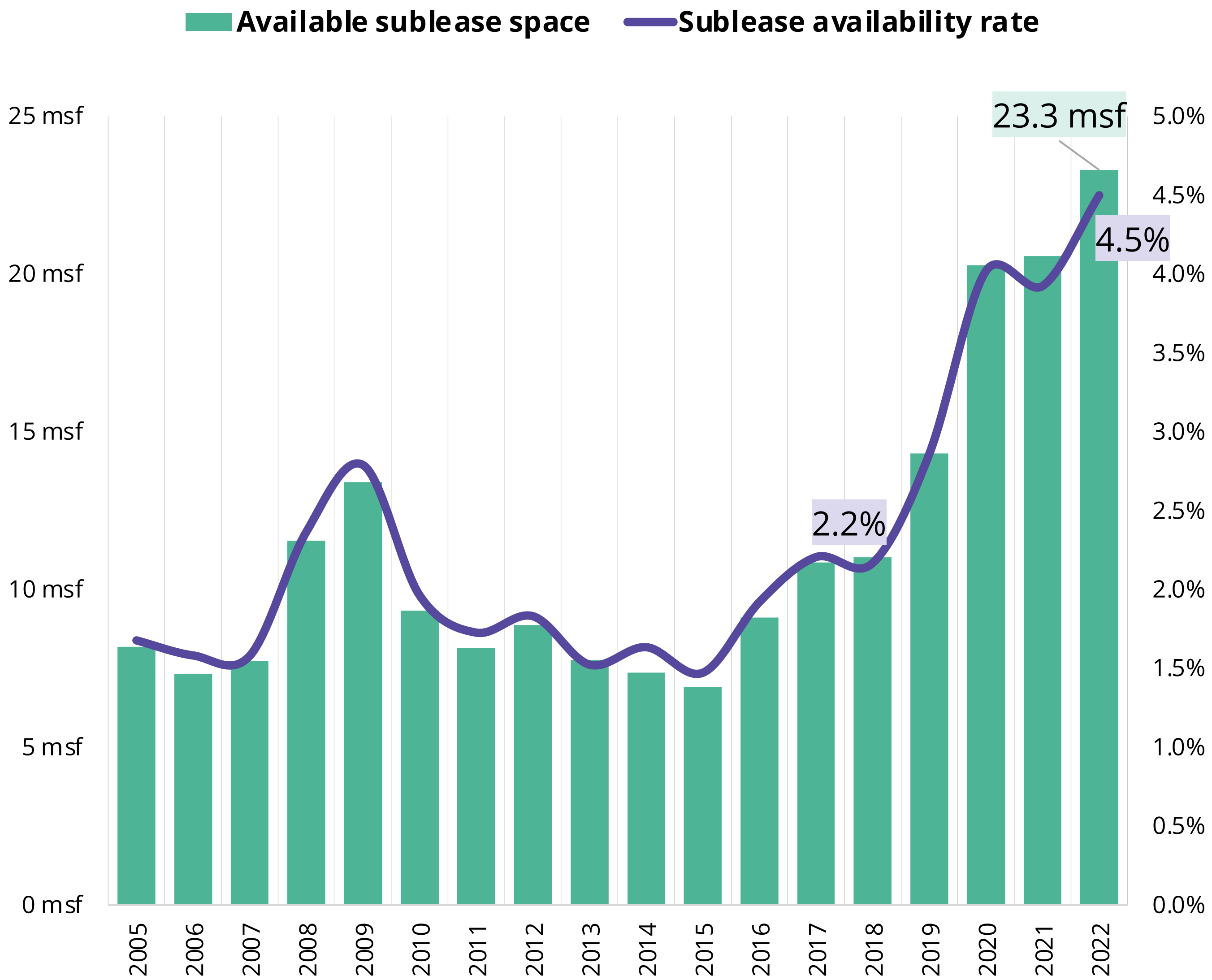
Source: CoStar
Note: Availability rate includes all availabilities, both direct and sublet, for existing, under construction and under renovation properties.

Available sublease space

23.3 msf

slight dip in available sublease space in Manhattan from Q2 2022.

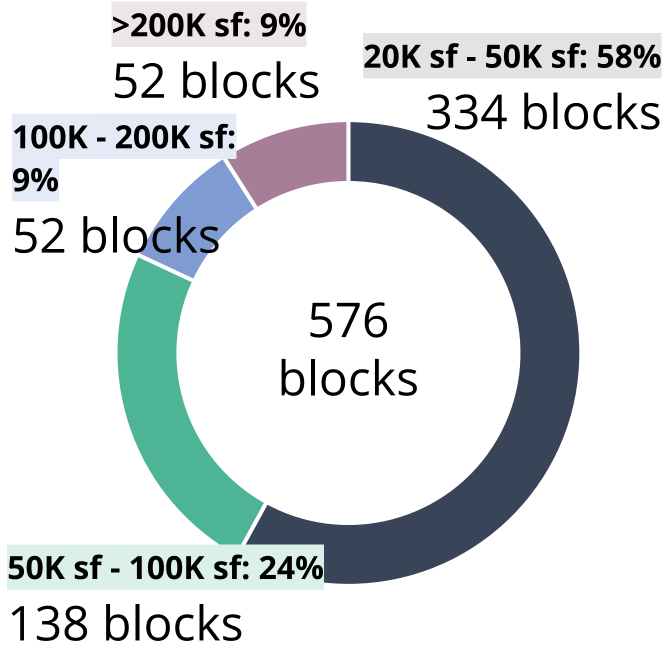
Total sublease availability has marginally shrunk quarter-over-quarter, decreasing by about 100,000 square feet. This slight shift was not enough to move the sublease availability rate, as it remains at 4.5% since last quarter.



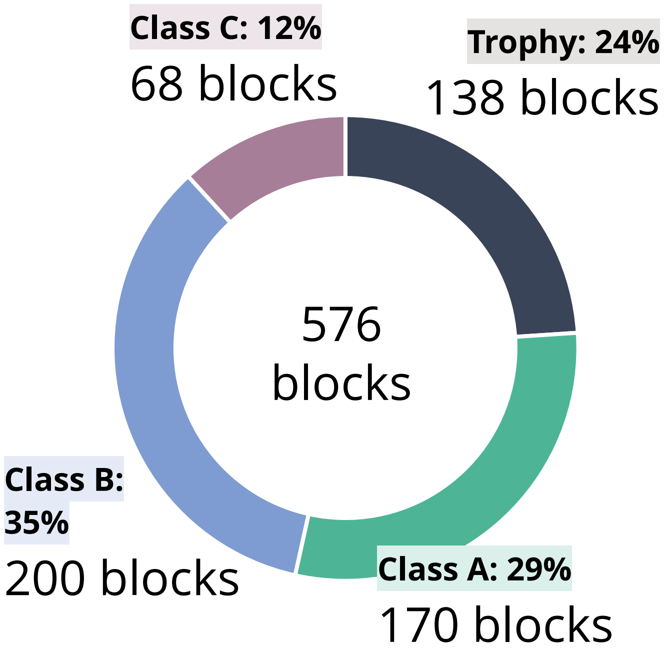
Source: CoStar
Note: Availability rate includes all availabilities, both direct and sublet, for existing, under construction and under renovation properties.

Office large-block availabilities (20,000+ sf)

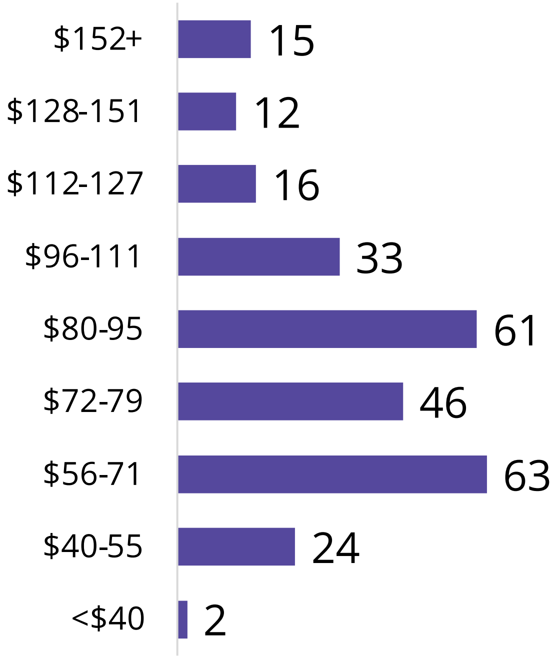
Number of blocks by size



Number of blocks by Class



Asking rents*



Note: Availability rate includes all availabilities, both direct and sublet, for existing, under construction and under renovation properties.
*Note: 20,000+ sf blocks. Asking rents for some blocks are undisclosed.
Source :CoStar, AVANT by Avison Young

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Office development pipeline

25 properties

proposed, under construction

18.3 msf

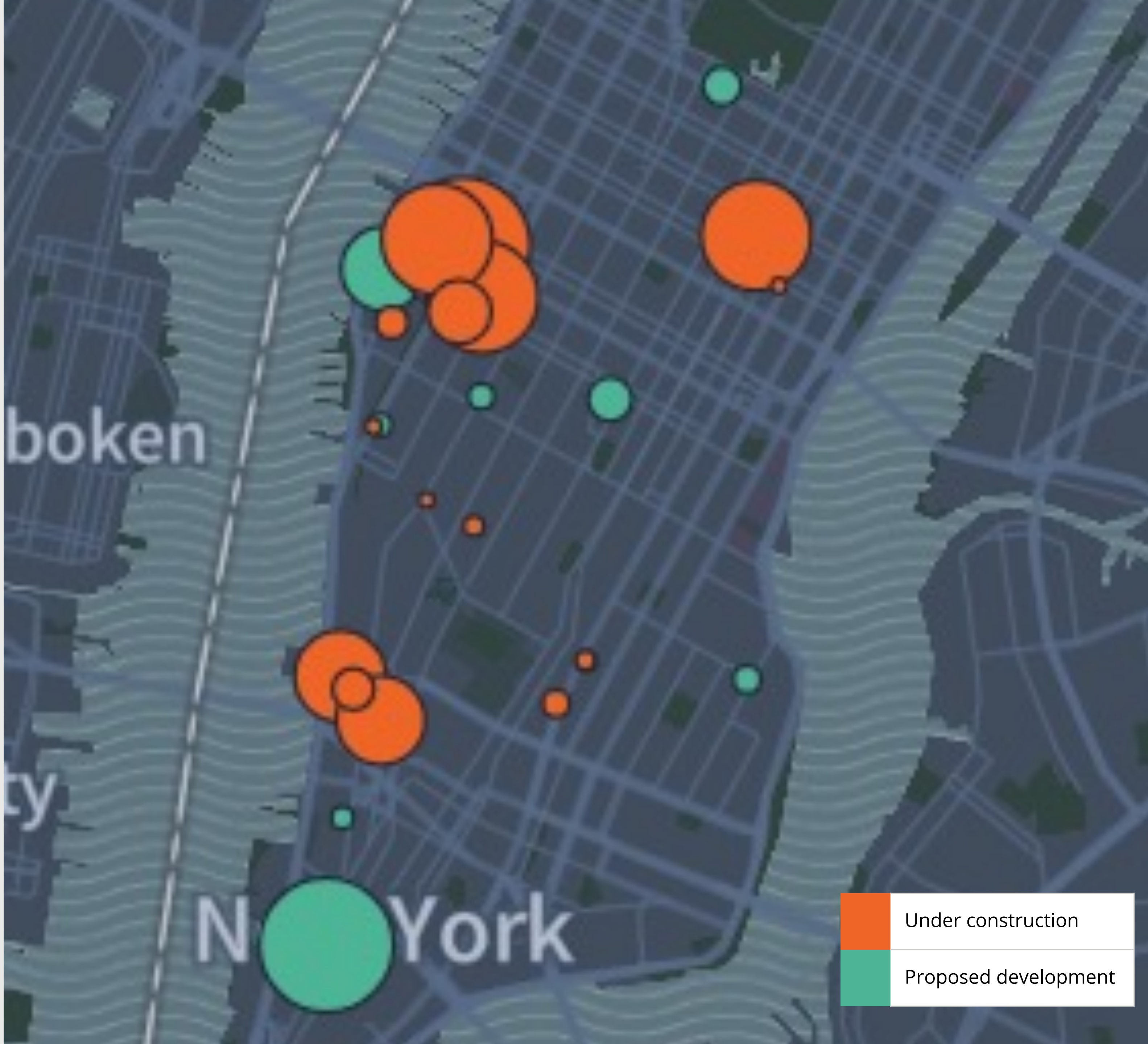
proposed, under construction

3.5%

share of office inventory

1931

average delivery date of Manhattan offices

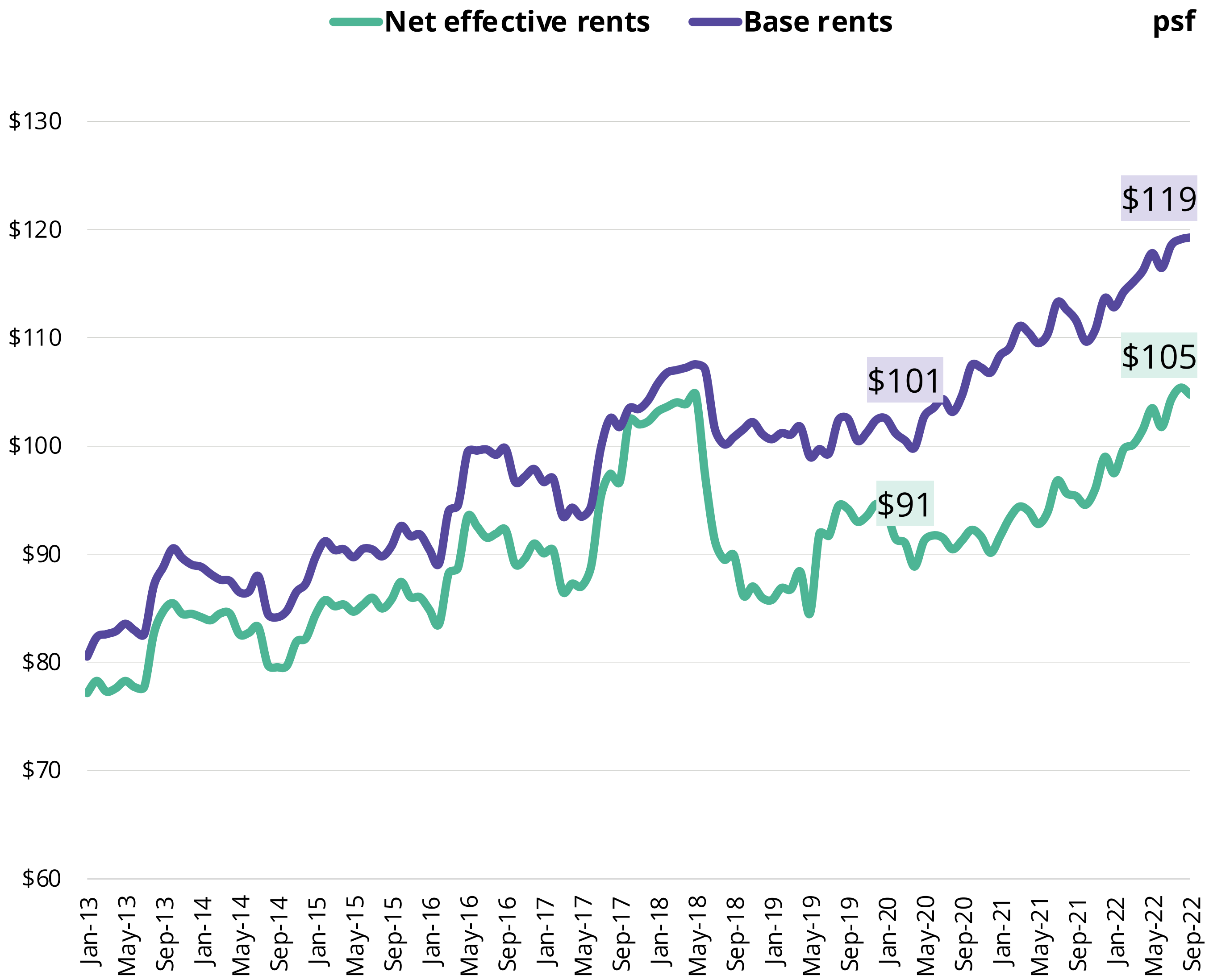


Trophy net effective rents and base rents

+15.0%

Trophy direct relocation net effective rents, September 2022 vs. March 2020.

Trophy base rents have reached all-time highs, while net effective rents sit slightly above the pre-COVID peak in May 2018. Both base and net effective rents of Trophy assets continue an upward trend amidst an uncertain economic future.



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

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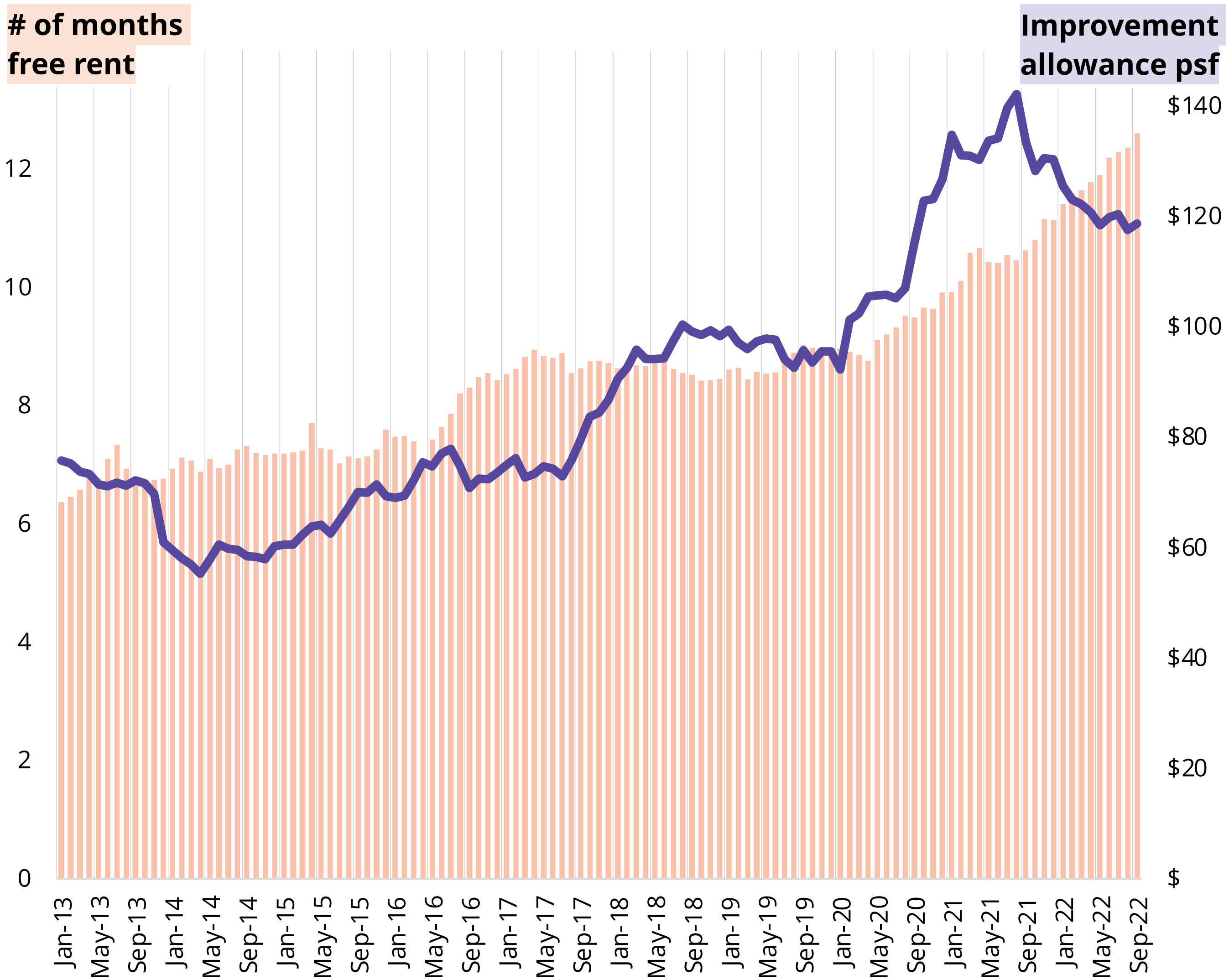
Trophy office concessions packages

+15.9%

Trophy direct relocation tenant improvement allowances, September 2022 vs. March 2020.

Trophy concession packages increased significantly following the pandemic, however, there has been a recent drop-off in average tenant improvement allowances. This recent decline represents a sign of continued strong demand for Trophy properties.



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

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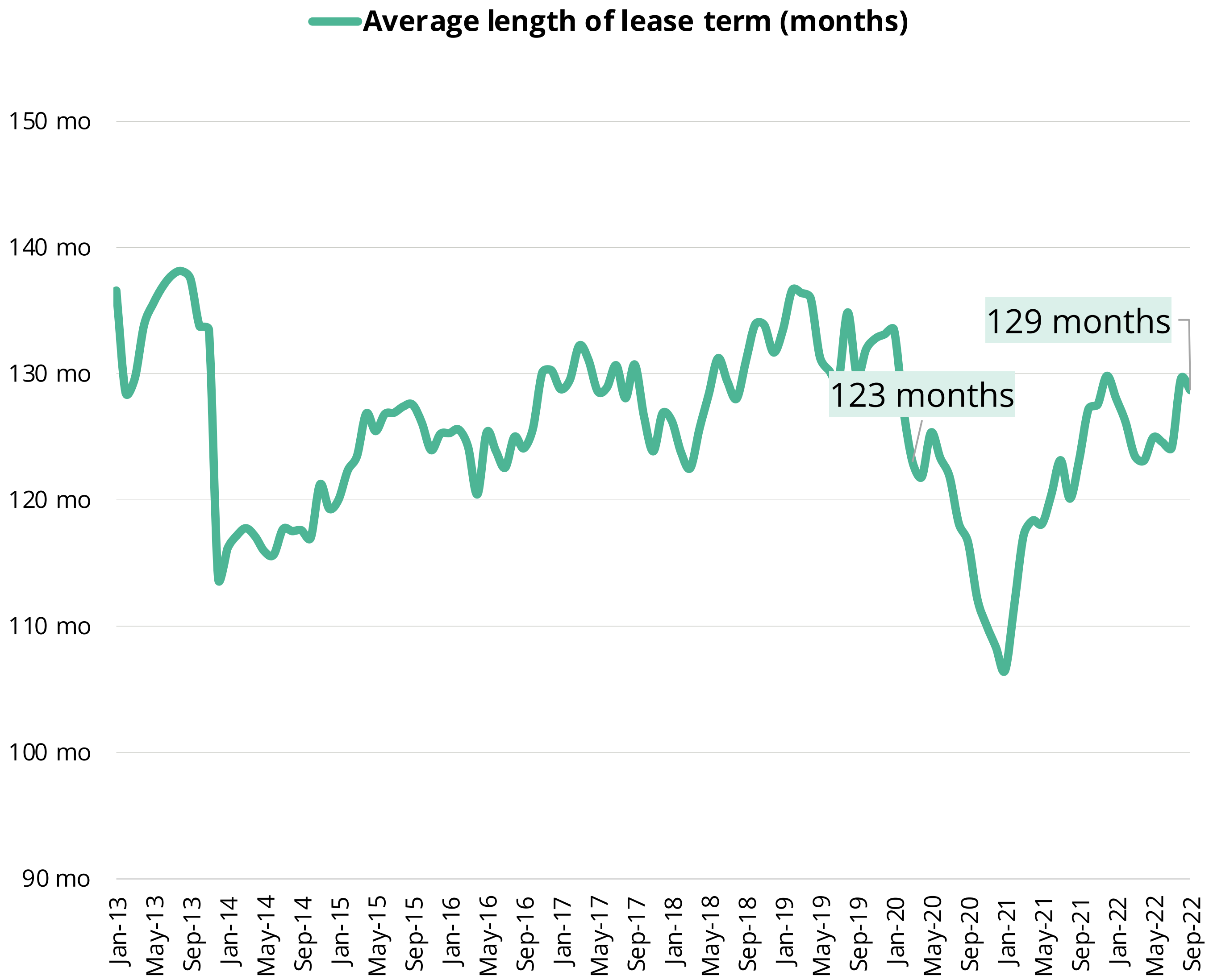
Trophy average length of lease term

+4.6%

Trophy average length of lease term, September 2022 vs. March 2020.

Trophy properties have seen consistently high demand over the last several years. While demand was still high through the pandemic, the average length of lease term saw a significant decrease as tenants were wary about making long term commitments. However, terms have since returned to pre-COVID normalcy, averaging just over 10 years per lease.



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

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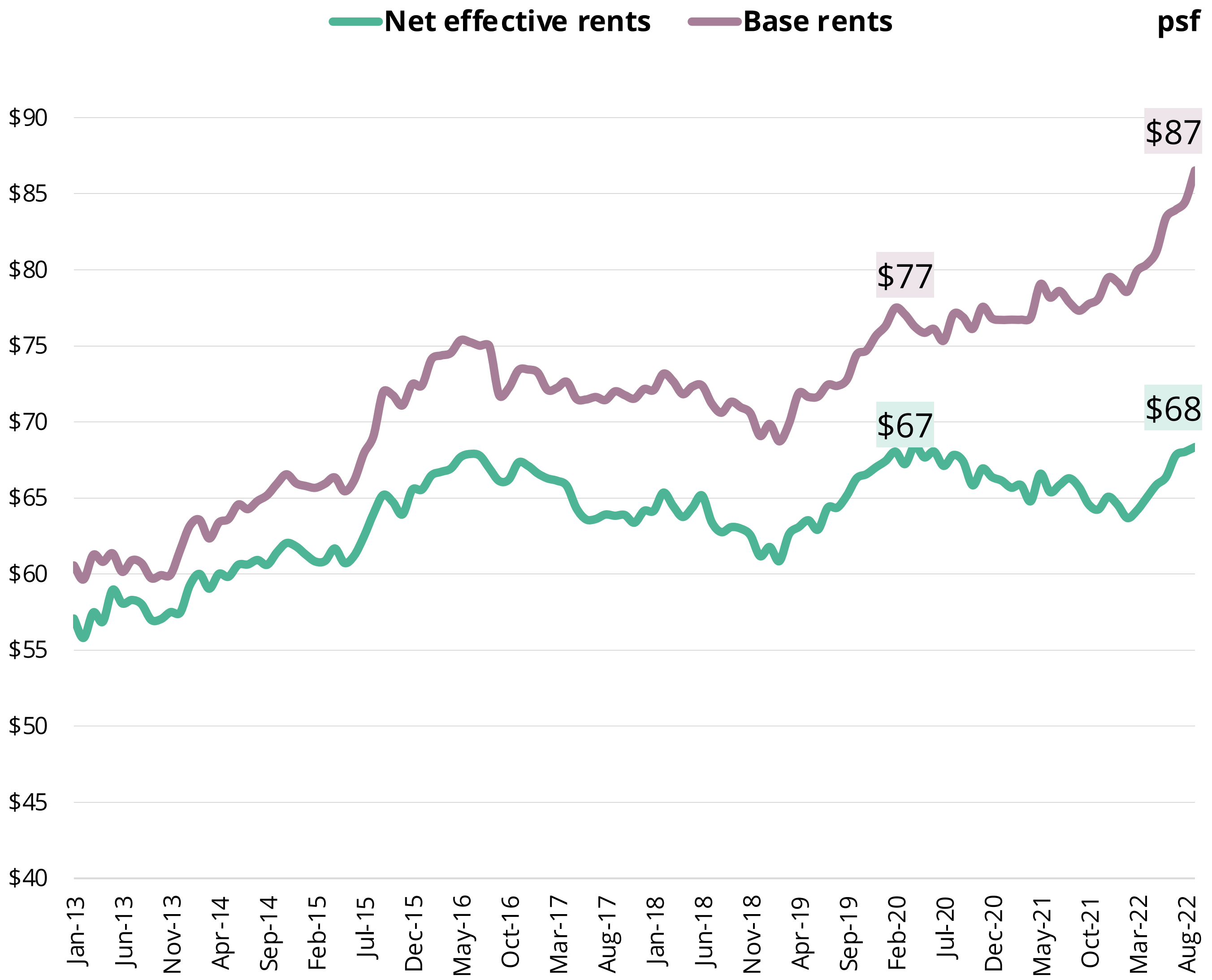
Class A net effective rents and base rents

+1.7%

Class A direct relocation net effective rents, September 2022 vs. March 2020.

Within the class A sector, demand is shifting towards higher quality assets in addition to landlords continuing to offer considerably large concessions. Class A net effective rents have now surpassed pre-COVID levels by 1.7% as a result. Additionally, this has caused the gap between base and net effective rents to continue to widen.



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

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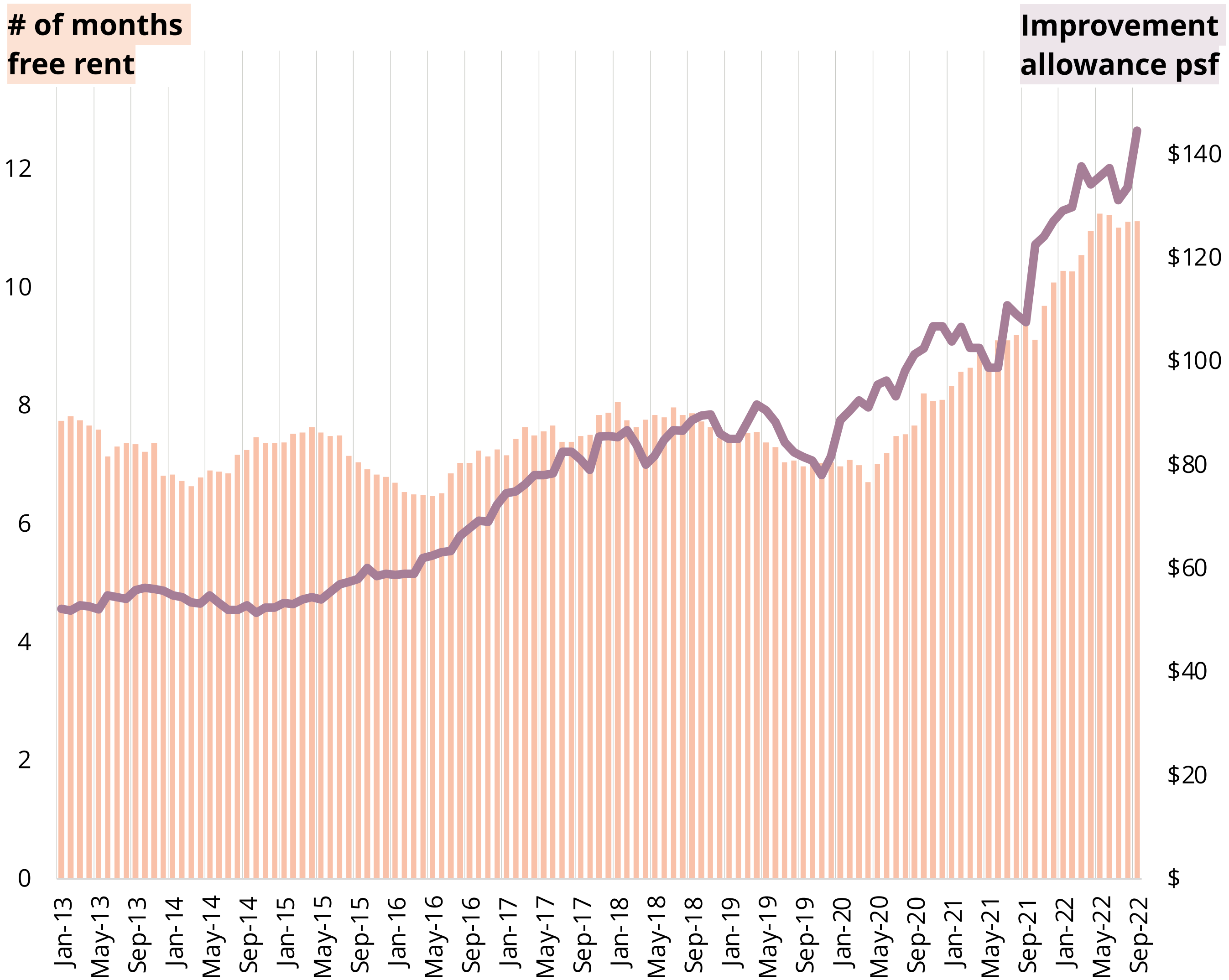
Class A office concessions packages

+56.3%

Class A direct relocation tenant improvement allowances, September 2022 vs. March 2020.

Class A free rent periods (11.1 months) and tenant improvement allowances ($144.53 psf) are both at or near record highs when normalizing for 10-year lease terms. Landlords continue to offer generous concessions packages to remain competitive with Trophy assets.



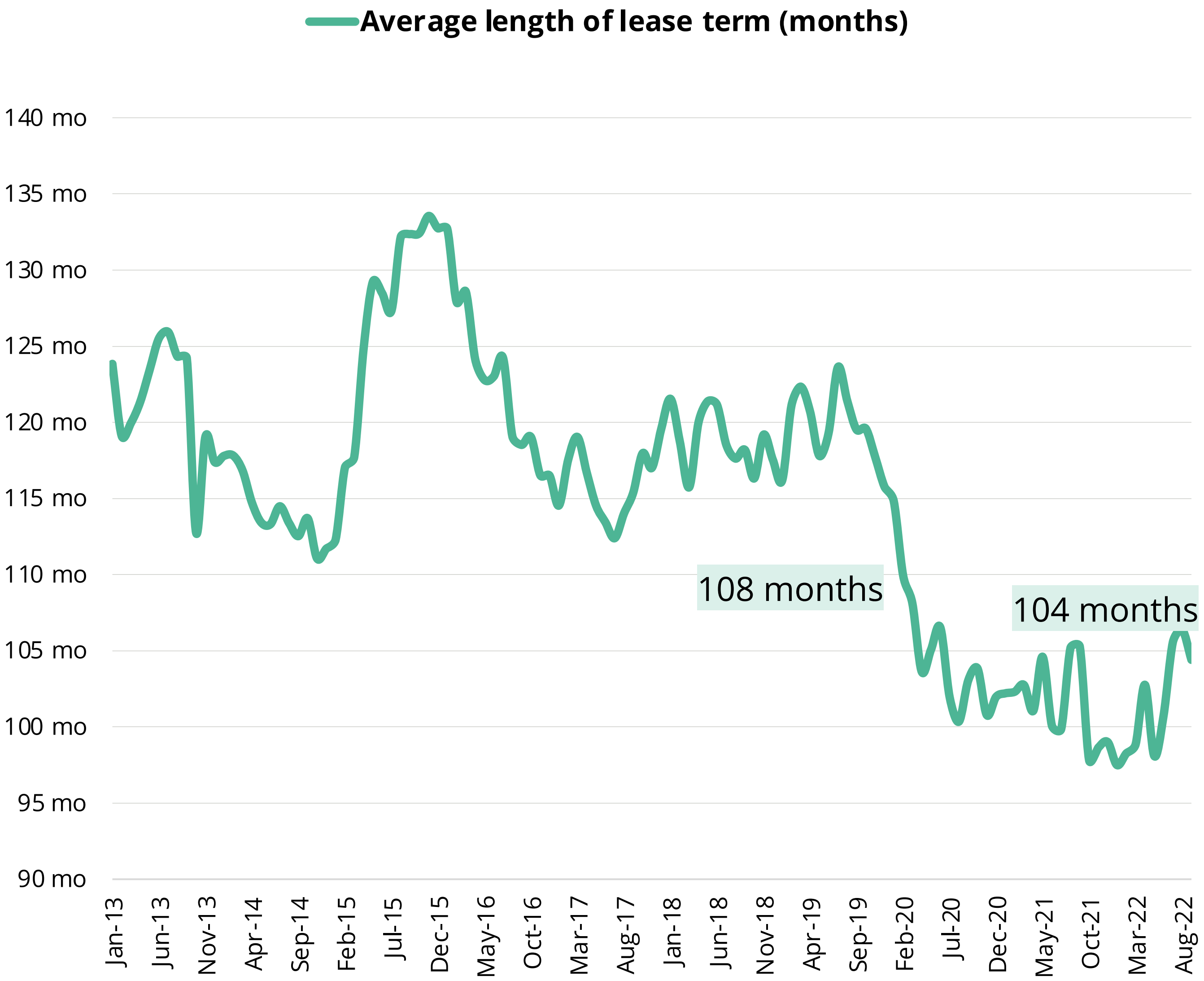
Note: Direct relocations only. Normalized to 10-year lease terms. Class A properties represent the top 25% but not the top 10% of the Manhattan office market in terms of rents and build date.
Source: AVANT by Avison Young

Class A average length of lease term

-3.4%

Class A average length of lease term, September 2022 vs. March 2020.

Class A properties were reporting a decrease in average length of lease term in late 2019, which got further accelerated by the onset of the pandemic in March 2020. Term lengths have begun to recover but still sit 3.4% below pre-COVID levels at 8.7 years per lease, on average.



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

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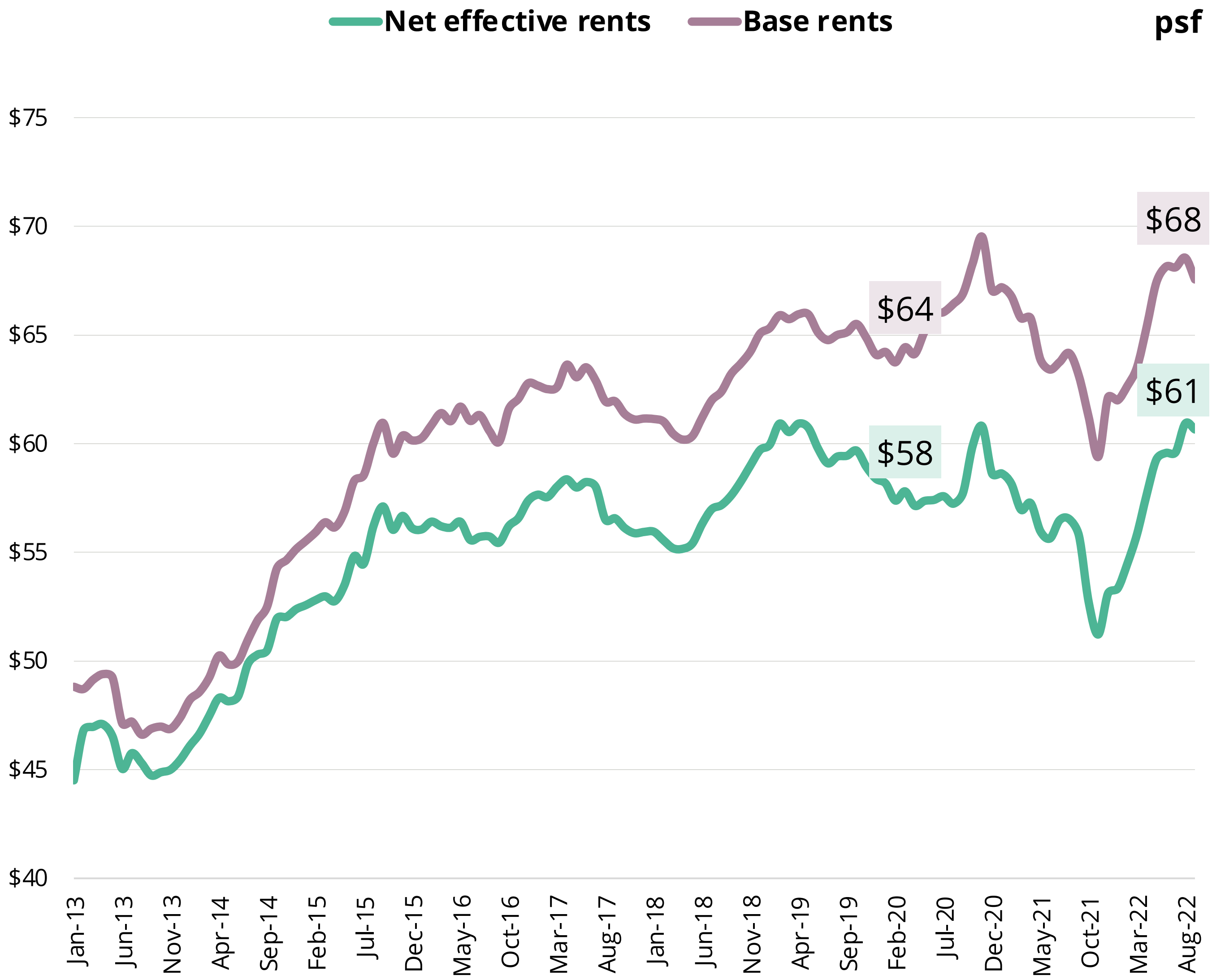
Class B and C net effective rents and base rents

+4.9%

Class B and C direct relocation net effective rents, September 2022 vs. March 2020.

Class B and C buildings' base and net effective rents rapidly decreased from 2020 through late 2021 but are now higher than pre-COVID levels. Tenants currently occupying class B and C buildings are largely renewing or moving to higher quality buildings within the asset class, causing the class B and C market to effectively rise.



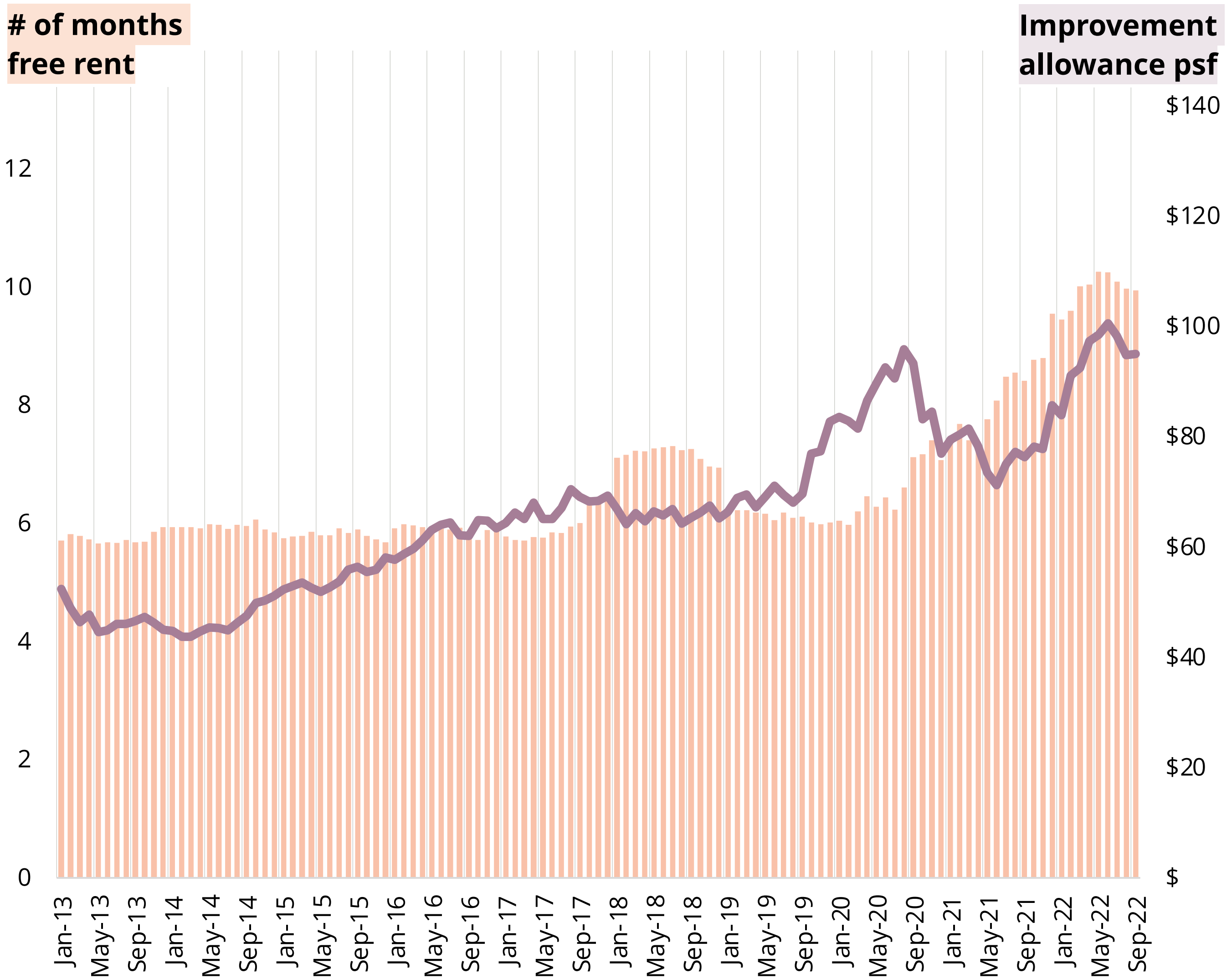
Note: Direct relocations only.
Source: AVANT by Avison Young

Class B and C office concessions packages

+16.6%

Class B and C direct relocation tenant improvement allowances, June 2022 vs. March 2020.

Free rent periods (9.9 months) and tenant improvement allowances ($95.05 psf) both experienced a slight decrease from Q2 2022 but remain near class B and C record highs when normalizing for 10-year lease terms. Although landlords are still feeling pressure to offer large concession packages, both free rent periods and tenant improvement allowances appear to be stabilizing.



Note: Direct relocations only. Normalized to 10-year lease terms
Source: AVANT by Avison Young

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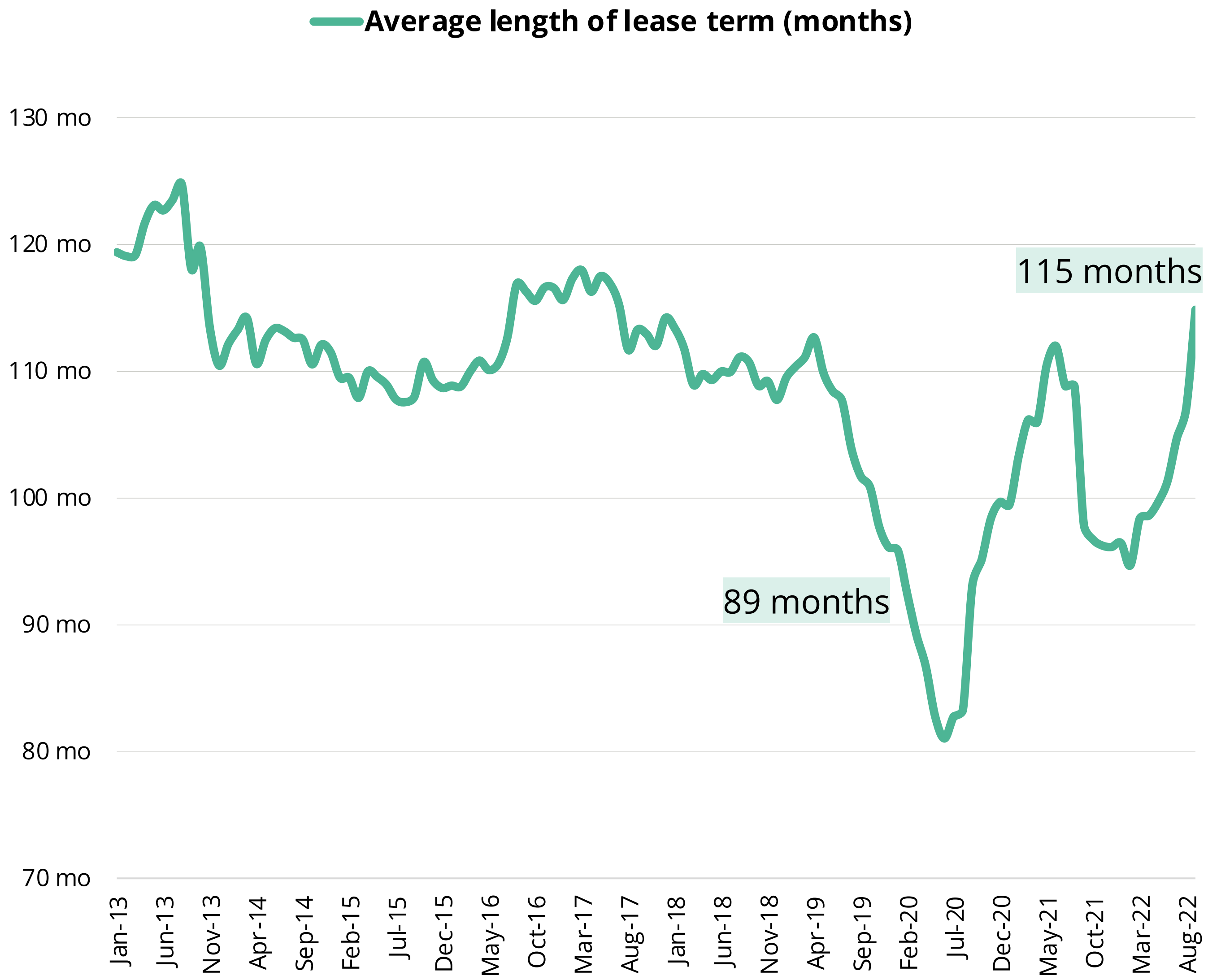
Class B and C average length of lease term

+28.8%

Class B and C average length of lease term, September 2022 vs. March 2020.

Much like class A properties, class B and C properties were reporting a decrease in average length of lease term before the start of the pandemic. However, class B and C properties have made a significant recovery in average length of lease terms, currently 28.8% above pre-COVID levels – and 10.6% above class A properties. This increase is largely driven by a handful of long-term education leases signed in class B and C buildings.



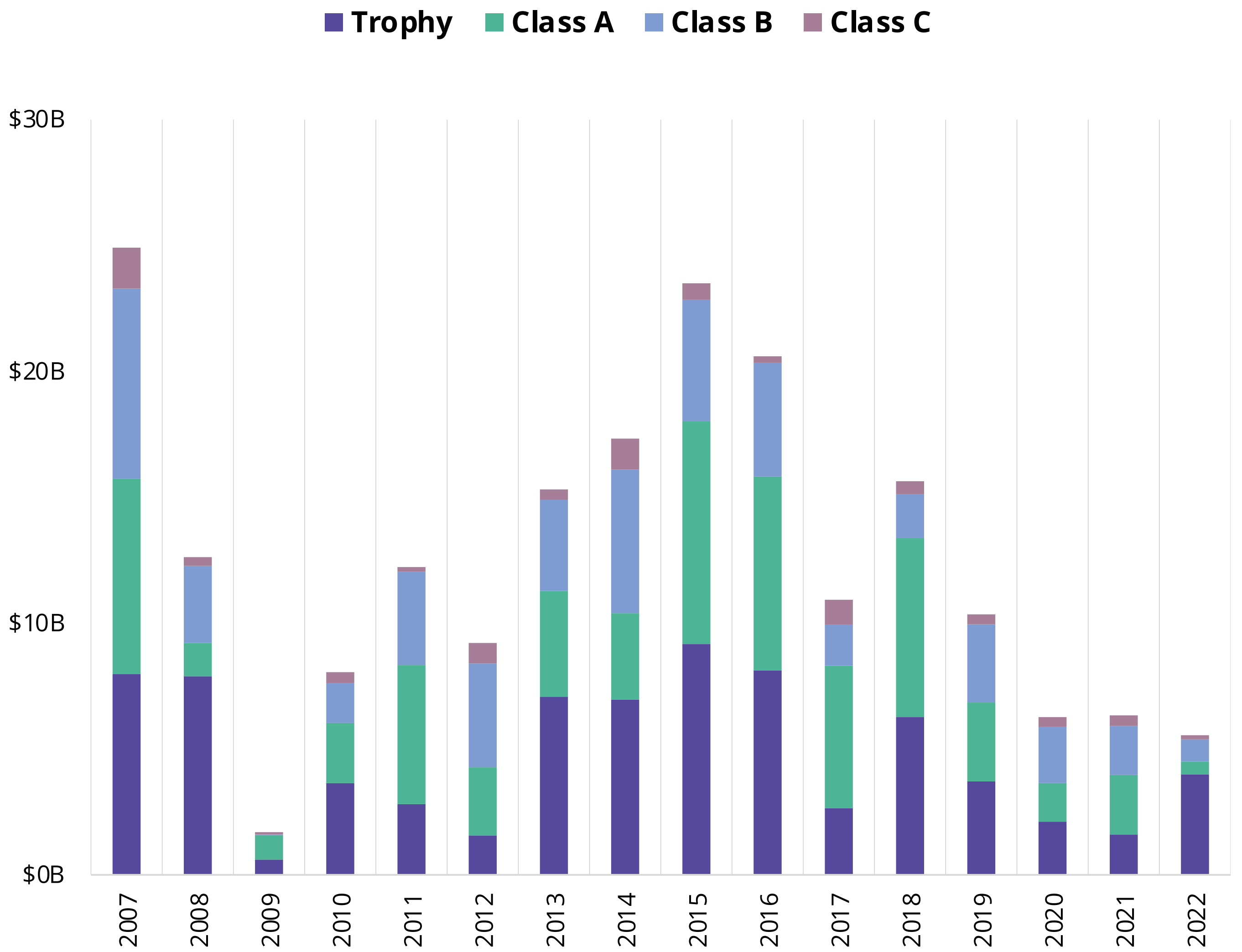
Note: Direct relocations only.
Source: AVANT by Avison Young

Office investment dollar volume

$5.6B

office dollar volume to date in 2022.

Total sale volume in Q3 2022 slowed relative to the previous several quarters. The only deals of $100M+ during the quarter were Meadow Partners' purchase of 95 Morton Street for $288 million and the sale of 321 East 61st Street to Memorial Sloan Kettering for $185 million. This could be attributed to rising interest rates that are beginning to dampen returns and valuations. A slowdown in investment activity in the coming quarters is likely to continue amidst continued economic and occupier uncertainty. This should hopefully be offset by several large profile office sales that are currently under contract.



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

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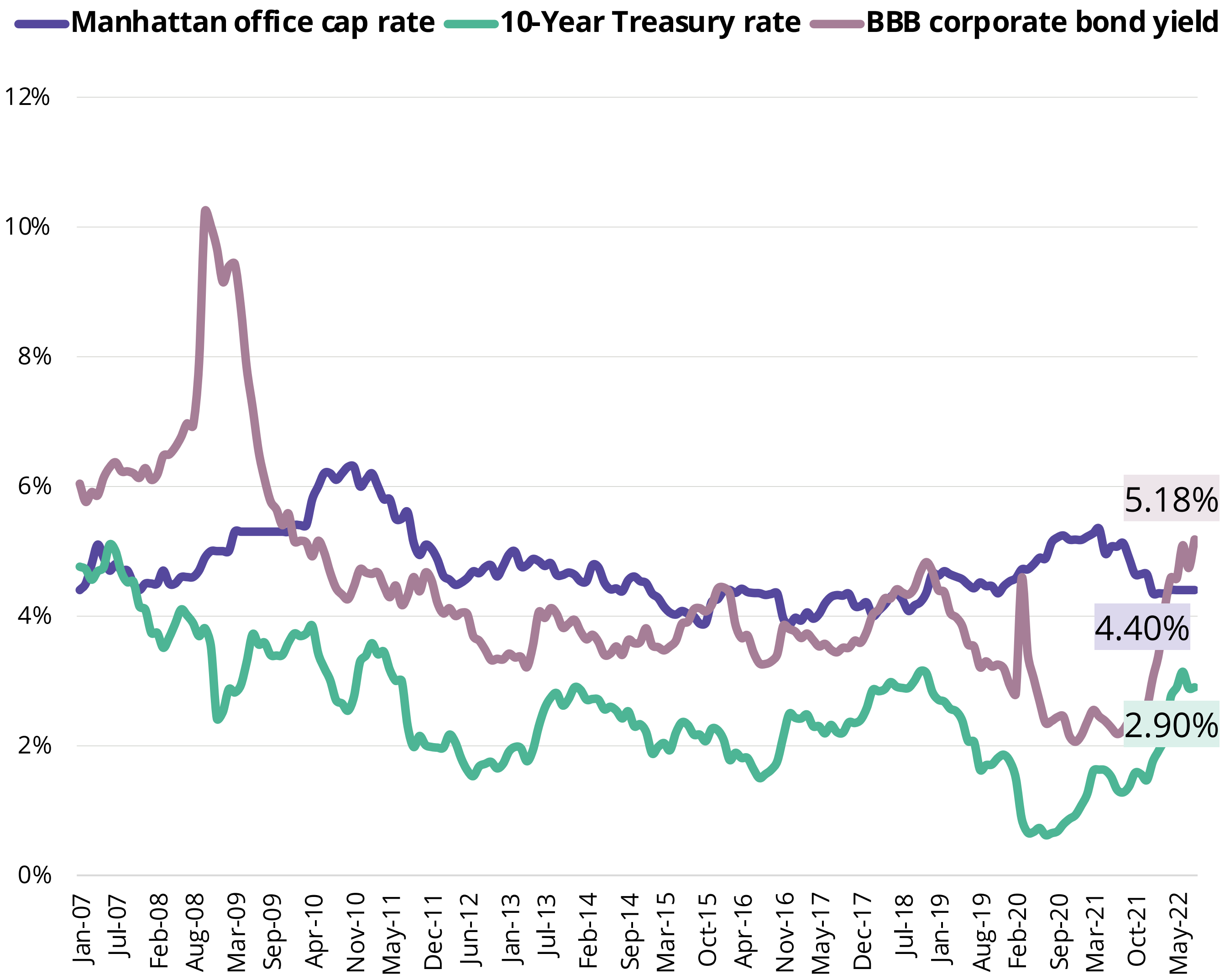
Office cap rates versus benchmark yields

150bp

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

The spread between office yields and the benchmark 10-year Treasury rate has compressed in recent quarters. This should inhibit demand for all but the most desirable, cash flowing properties. Those kinds of opportunities remain rare provided repatriation of capital difficulties and valuation uncertainties.



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

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Office market stats by submarket

By Submarket	Inventory (sf)	Availability Total %	Direct %	Sublet %	Net Absorption (sf) YTD	Average Asking Rent (psf) Q3 2021	Q3 2022
Central Park	31,529,727	18.4%	16.4%	2.0%	-382,304	$115.68	$118.72
Grand Central	81,496,380	17.9%	14.6%	3.2%	128,332	$78.34	$79.11
Hudson Yards	14,609,035	18.9%	10.3%	8.6%	2,030,742	$168.78	$172.06
Midtown Core	57,779,073	12.2%	8.9%	3.2%	576,593	$84.72	$104.17
Midtown East	24,078,041	21.9%	19.6%	2.3%	76,046	$84.93	$88.81
Midtown West	3,904,684	35.8%	13.0%	22.7%	41,022	$70.12	$68.28
Murray Hill	11,372,525	21.6%	16.6%	5.0%	-73,607	$69.47	$68.74
Penn Station	50,817,075	18.1%	13.3%	4.7%	-55,961	$63.98	$65.11
Times Square	36,637,204	22.5%	17.4%	5.1%	-1,005,849	$78.33	$76.62
Midtown Total	**312,223,744**	**18.2%**	**14.1%**	**4.1%**	**1,335,014**	**$81.23**	**$84.70**
Chelsea	17,040,777	27.3%	20.7%	6.6%	-338,171	$60.50	$59.94
East Village	776,641	39.1%	21.2%	17.9%	-201,066	$139.15	$139.15
Flatiron District/Gramercy Park	40,336,744	17.6%	12.9%	4.7%	-358,723	$74.81	$78.03
Greenwich Village	7,604,487	16.8%	15.6%	1.2%	-109,158	$73.44	$79.64
Hudson Square	10,530,988	19.1%	13.2%	5.9%	1,420	$64.87	$65.63
Lower East Side	2,572,716	21.4%	20.5%	1.0%	-28,780	$70.72	$86.97
Meatpacking District	8,238,954	6.2%	4.6%	1.5%	9,050	$126.51	$121.38
SoHo	6,908,270	15.1%	11.8%	3.3%	17,733	$86.28	$73.03
West Village	585,244	3.8%	3.2%	0.6%	-1,400	$67.63	-
Midtown South Total	**94,594,821**	**18.5%**	**14.0%**	**4.5%**	**-1,009,095**	**$73.34**	**$74.40**
City Hall	15,125,712	7.8%	6.5%	1.3%	29,178	$65.42	$64.03
Financial District	43,760,895	25.2%	19.6%	5.6%	-672,954	$62.04	$62.44
TriBeCa	9,186,115	15.2%	10.9%	4.2%	-1,125	$130.91	$129.10
Water Street Corridor	18,835,258	24.5%	15.1%	9.4%	-126,572	$66.37	$66.58
World Trade Center	25,867,107	12.8%	6.7%	6.1%	-278,496	$94.60	$94.65
Downtown Total	**112,775,087**	**19.1%**	**13.4%**	**5.7%**	**-1,049,969**	**$68.69**	**$69.07**
Upper East Side	1,151,541	4.3%	3.2%	1.1%	1,129	-	-
Upper West Side	2,147,989	3.5%	2.6%	0.9%	-4,900	$42.84	$43.84
Manhattan Total	**522,893,182**	**18.4%**	**13.9%**	**4.5%**	**-727,821**	**$77.02**	**$79.65**

Note: Availability rate includes all availabilities, both direct and sublet, for existing, under construction and under renovation properties.
Note: Asking rents for some blocks are undisclosed, therefore certain submarkets may not have asking rents.
Note: Direct and sublet availability may not sum to total availability due to rounding.

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