

CHICAGO OFFICE MARKET

CHICAGO OFFICE MARKET HITS PAUSE BUTTON DURING GLOBAL PANDEMIC

The second quarter of 2020 was one unlike anything the market has experienced before with the start of the pandemic. Chicago's office market continues to contend with the effects of the global pandemic, ranging from the initial shutdown of the economy, widespread layoffs and financial uncertainty. Overall, the metro office market came out of the second quarter fairly unscathed with only a ten-basis-point increase in vacancy to 16.8%. Rental rates increased to \$30.17/SF. This increase was largely due to rising taxes and operating expenses, as opposed to higher asking rates.

At the beginning of the pandemic, many anticipated substantial gains in the amount of sublease space that would become available. Both Downtown and in the suburbs, there has been an increase but not the spike originally anticipated. Sublease availability increased minimally to 6.53 million square feet from 6.46 million square feet at a metro level. Downtown, roughly 750,000 square feet of new sublease space became available, pushing the availability rate up ten basis points to 2.7%. Large subleases were added to the market during the quarter from Career Builder, Flexport, Aspen Dental, Zurich Insurance, R1 RCM, Narrative Science and Quintairos, Prieto, Wood & Boyer. The new sublease spaces that have become available have an average remaining term of around six years. The suburbs saw less new sublease space come onto the market, with just around 315,000 square feet during the quarter.

In the three and a half months since employees have been working from home, many companies have changed work-from-home policies, initially praising work-from-home productivity, but later realizing that collaboration in the office is best for many types of job functions. Despite the desire for employees to return, the logistics have been more challenging, preventing high numbers of employees from actually returning. According to Kastle Systems, a building security system provider, as of June 17th, only 16.2% of employees in the Chicago Metro had returned to the office. As companies determine the safest return strategies, the market should anticipate increasing amounts of sublease space, as well as direct vacancy driven by layoffs across many office-using industries in Chicago. Tech firms, such as GoGo Wireless, SpotHero and Glassdoor, have all had layoffs. Airline manufacturer Boeing is laying people off, as are Chicago Public Schools, Northwestern University and global marketing firm Edelman. While a high amount of new unemployment filings claim to be temporary furloughs, meaning employees hope to return, the impact of these cuts will still be felt on the office market.

CURRENT CONDITIONS

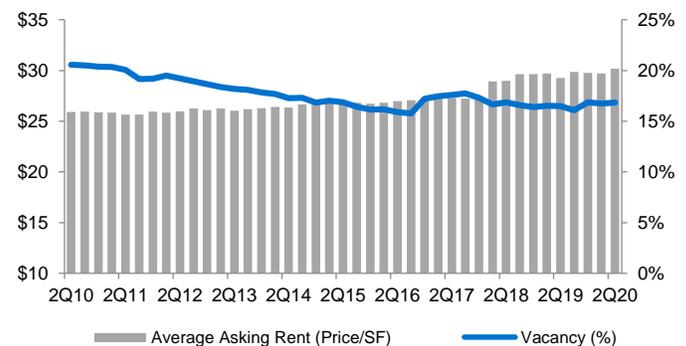
Metro absorption was 444,000 square feet during the quarter.

Metro vacancy increased ten basis points to 16.8%.

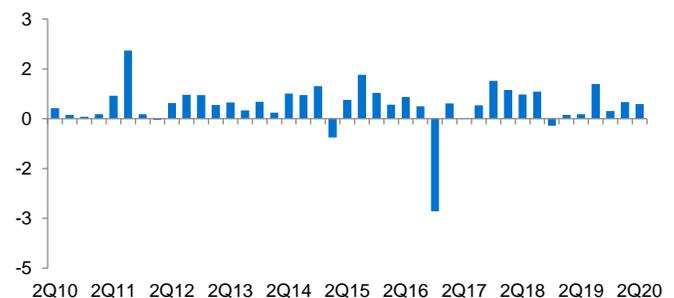
6.0 MSF of space is currently under construction including the three new office towers in the CBD.

MARKET ANALYSIS

Asking Rent and Vacancy



Net Absorption (SF, Millions)



MARKET SUMMARY

	Current Quarter	Prior Quarter	Year Ago Period	12 Month Forecast
Total Inventory	240.0 MSF	238.9 MSF	236.8 MSF	↑
Vacancy Rate	16.7%	16.8%	16.5%	↓
Quarterly Net Absorption	484,147	314,358	119,441	↓
Average Asking Rent	\$29.70	\$29.76	\$29.69	↑
Under Construction	6.93 MSF	3.42 MSF	5.18 MSF	↑
Deliveries	737,018	2.58 MSF	21,562	↑

CBD REVIEW

Downtown Chicago saw vacancy increase 20 basis points for the quarter as absorption slowed and new construction delivered. At 13.7%, total vacancy is back up to where it was at the end of 2019 when the post office renovation delivered. Rental rates also increased to \$37.98/SF, as mentioned earlier, largely due to the rising taxes and operating expenses owners are facing. This will continue to be an issue as asking rents are declining, but the operating costs of running buildings in a post-pandemic world, where a building needs more touchless technology, additional cleaning and improved air filtration systems, are likely to be significantly higher.

There was just over 1 million square feet that delivered Downtown this quarter, which contributed to the rise in vacancy. The redevelopment of the top floors at Macy's was completed this quarter delivering 700,000 square feet of new office space to the market, the first tenant moved in as well. Numerator became the first tenant in a move from Willis Tower to the East Loop building, doubling its footprint to 60,000 square feet. The other deliveries were in Fulton Market, which is on track to have buildings delivering throughout the next several quarters. This quarter included 905 West Fulton Market and 1375 West Fulton Market. 1375 West Fulton is a 300,000-square-foot, 13-story building developed by Trammell Crow Co. Glassdoor is currently the only tenant committed to the building, where it has signed a lease for 50,000 square feet.

SUBURBAN REVIEW

In the suburbs, vacancy remained flat at 21.6%, the first time in three quarters it hasn't increased. Rental rates remained unchanged as well at \$22.34/SF. This lack of increase is unsurprising, considering landlords are trying to fill buildings and secure existing tenants in anticipation of a longer economic slowdown. Many are anticipating that the pandemic could further encourage the return to the suburbs that many suburban landlords have been anticipating for a while. The combination of older millennials being forced to work from home and shelter in place with small children in small city residences and the challenges of maintaining social distancing guidelines in large office towers, where the majority of employees take public transit, is fueling a renewed interest in suburban office properties. Some tenants feel more secure signing smaller, short-term leases for offices in the suburbs where employees can drive to work and take the stairs while they figure out their next steps in regards to making larger CBD headquarters safe.

LEASING VELOCITY

Leasing velocity slowed to a trickle as office workers were shut in their homes and companies that were forced to make decisions opted for renewals or extensions when possible. This tumble in leasing activity came after first-quarter volume was one of the highest in recent years, with 4.6 million square feet of leasing volume across the metro. The second quarter closed with only 1.5 million square feet, bringing the year-to-date 2020 total to 6.2 million square feet, sizably less than half the 20 million square feet completed in 2019.

The list of large renewals includes suburban tenants Allstate renewing for 94,000 square feet in Woodridge, The American Board of Radiology for 71,000 square feet in Oak Brook and Lewis University for 28,000 square feet in Oak Brook. Downtown, NFP renewed for 37,000 square feet at 500 West Madison and Pinterest renewed for 31,000 square feet at 111 North Canal. As mentioned, new leases were limited but XPO Logistics signed a new lease for 50,000 square feet at 263 Shuman Boulevard, PPC Investment Partners LP signed a lease at the 110 North Wacker for a 30,000-square-foot building scheduled to be delivered in the fall.

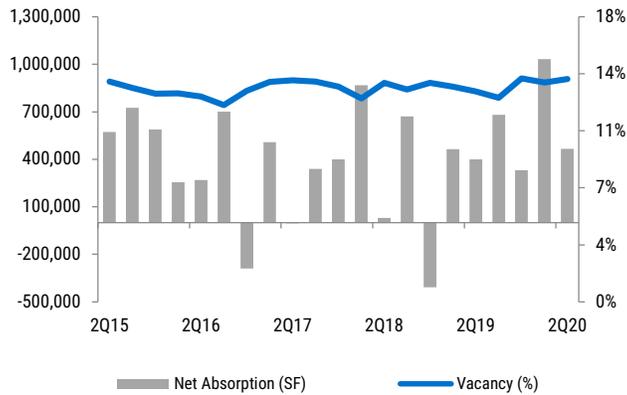
CAPITAL MARKETS

In a quarter when almost no buildings traded hands, one of the only sales came from German real estate firm Deka Immobilien purchasing 905 West Fulton Market for \$86.5 million. Thor Equities sold the 98,000-square-foot building, which is 100.0% occupied by Mondelez. At \$879/SF, this is a new record high, breaking the previous record of \$774/SF set last year by 811 West Fulton Market. Mondelez has signed a 15-year lease in the building, moving employees to Fulton Market from Deerfield. The other main sale for the quarter was 225 West Wacker. Spear Street Capital closed on the 650,000-square-foot building that includes tenants such as Cushman & Wakefield and Crowe. Spear Street Capital paid \$323/SF, slightly less than the \$335/SF Mirae Asset paid to acquire the building in 2013.

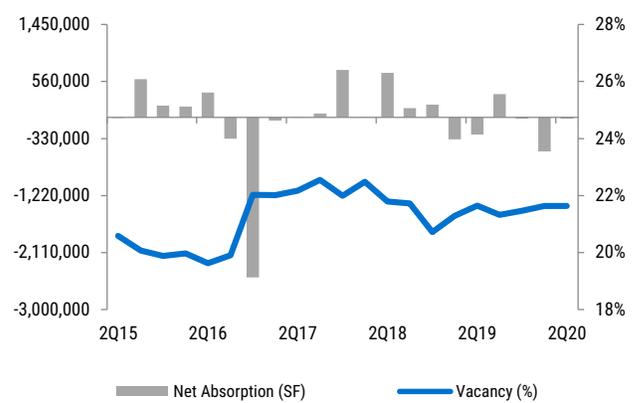
LOOKING FORWARD

Unsurprisingly, the Chicago office market wavered with the challenges presented by the pandemic. While Chicago and Illinois seem to be on the right track in taking precautions while reopening the economy, rising cases across other areas of the U.S., public transit concerns, work-from-home policies, failing industries and a second wave of infection are all lingering concerns for real estate decision makers. Although the length and depth of this market correction remains unknown, Chicago is in a strong position, thanks to early actions and its diverse economy.

CBD NET ABSORPTION AND VACANCY



SUBURBAN NET ABSORPTION AND VACANCY



CBD LEASE TRANSACTIONS

Tenant	Building	Submarket	Type	Square Feet
Pinterest	111 N Canal St	West Loop	Renewal	31,000
PPC Investment Partners LLP	110 N Wacker Dr	West Loop	Direct	30,000
Schiller Ducanto & Fleck LLP	321 N Clark St	River North	Direct	27,000
Wilkie Farr & Gallagher LLP	300 N L aSalle St	River North	Sublease	25,000
Bollinger Connolly Krause	500 W Madison St	West Loop	Renewal	21,000

SUBURBAN LEASE TRANSACTIONS

Tenant	Building	Submarket	Type	Square Feet
Allstate Life Insurance	9022 Heritage Pkwy	I-88 East	Renewal	94,000
The American Board of Radiology	814 Commerce Dr	I-88 East	Renewal	71,000
XPO Logistics	263 Shuman Blvd	I-88 West	Direct	50,000
Lewis University	1111 W 22nd St	1-88 East	Renewal	28,000
Colgate Palmolive	1700 E Golf Rd	Northwest	Renewal	15,000

METRO SALE TRANSACTIONS

Buyer	Building	Submarket	Price Per SF	Square Feet
Spear Street Capital	225 W Wacker Dr	West Loop	\$323	650,000
Deka International	905 W Fulton	Fulton Market	\$879	98,454
J Michael Van Zandt	4255 Meridian Pkwy	I-88 West	\$65	44,825

SUBMARKET STATISTICS

	Total Inventory (SF)	Under Construction (SF)	Total Vacancy Rate	Qtr Absorption (SF)	YTD Absorption (SF)	Class A Asking Rent (Price/SF)	Class B Asking Rent (Price/SF)	Total Asking Rent (Price/SF)
CBD Total	145,048,127	6,023,984	13.7%	465,976	1,497,865	\$39.92	\$36.47	\$37.98
Central Loop	37,003,331	-	13.3 %	150,141	316,420	\$39.14	\$38.66	\$38.57
East Loop	25,352,415	652,452	16.4%	36,061	111,997	\$36.05	\$33.81	\$34.54
Fulton Market	5,564,813	1,816,336	17.9%	67,505	348,788	\$36.26	\$31.33	\$32.80
North Michigan Avenue	10,496,574	-	10.2%	6,508	(90,774)	\$40.15	\$36.20	\$37.16
River North	13,834,718	1,286,651	11.6 %	(70,807)	(129,786)	\$38.80	\$30.90	\$35.76
West Loop	52,796,276	2,920,997	13.4 %	276,568	905,190	\$41.72	\$36.90	\$40.70
Suburban Total	95,595,582	-	21.6%	(21,345)	(552,432)	\$23.53	\$21.39	\$22.34
I-88 East	21,963,464	-	16.9%	254,796	33,179	\$25.82	\$21.35	\$23.45
I-88 West	13,480,084	-	19.4 %	27,755	(148,452)	\$22.18	\$20.56	\$21.57
North	24,766,832	-	19.2 %	(232,967)	(154,217)	\$23.91	\$21.08	\$22.20
Northwest	22,754,801	-	31.4%	(20,278)	(372,447)	\$21.70	\$21.00	\$21.23
O'Hare	12,994,401	-	19.4%	(50,561)	89,487	\$27.72	\$24.54	\$25.17
Chicago Metro	241,007,709	6,023,984	16.8 %	444,631	945,433	\$31.68	\$29.06	\$30.17

ECONOMIC CONDITIONS

The pandemic has had a serious and potentially long-lasting impact on the global and local economy. The measures that governments have taken to stem the spread of the virus are being felt at every level, and the U.S. record-long bull run has officially come to an end. The U.S. saw unemployment spike at record high levels, with 20.5 million jobs lost in April alone, the most since the Great Depression. The national unemployment rate hit its peak in April at 14.7%.

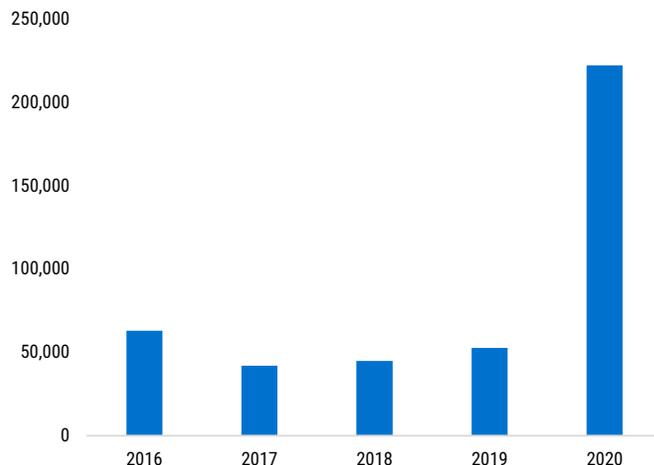
As May closed out, many were surprised to see that unemployment fell to 2.5 million jobs, driving the unemployment rate down to 13.3%. Chicago's unemployment rate fell by 2.1% to 15.4%. Additionally, consumer spending surged as people started leaving their homes again and regulations in some states were lifted. The debate remains open on whether this will be a U-shaped recovery or if it will look more like a Nike 'swoosh' with a quick fall and slow climb up.

In Chicago at the end of 2019, unemployment was at a record low of 2.8% and quickly jumped more than six times that to 17.5% for April and then falling to 15.4% in May. Mass layoffs for the first six months of the year are already higher than they were for the last four years, combined with 222,354 layoffs occurring in Illinois. As expected, with business and leisure travel coming to a total halt, the leisure and hospitality industry have taken the hardest hit in Chicago, with employment falling 48.7% year-over-year.

As Chicago and the rest of Illinois enters Phase 4 of reopening at the start of the third quarter, there remains hope that the city and state will be able to keep infections rates low so that the economy can continue what is sure to be a long and difficult recovery. While the hit to summer tourism and conventions will certainly hurt the economy, Chicago is well positioned as a diverse economy with no dependence on a single industry.

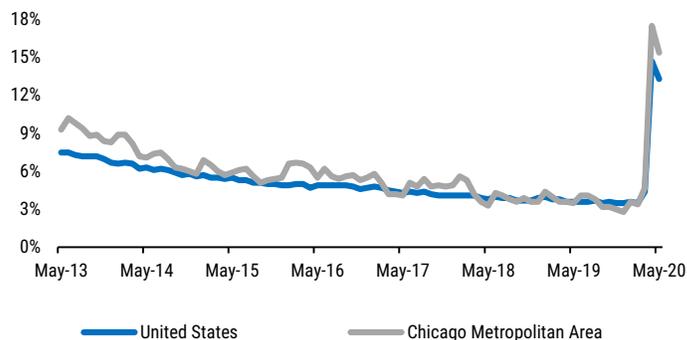
LAYOFF STATS

IL Mass Layoffs (Initial Claims), May 2020



UNEMPLOYMENT RATE

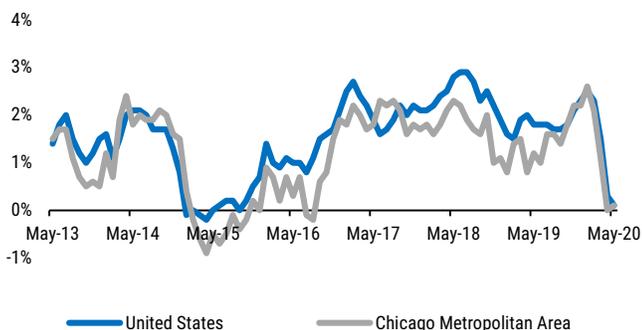
Seasonally Adjusted, May 2020



Source: U.S. Bureau of Labor Statistics

CONSUMER PRICE INDEX (CPI)

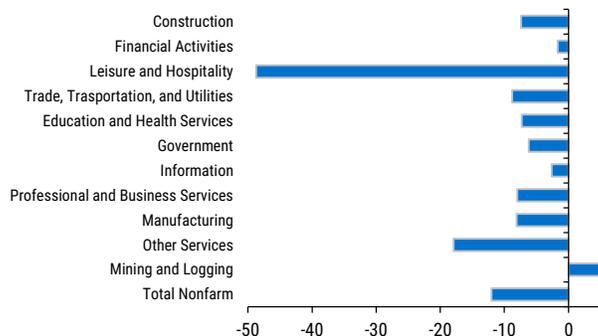
All Items, 12-Month % Change, Not Seasonally Adjusted,



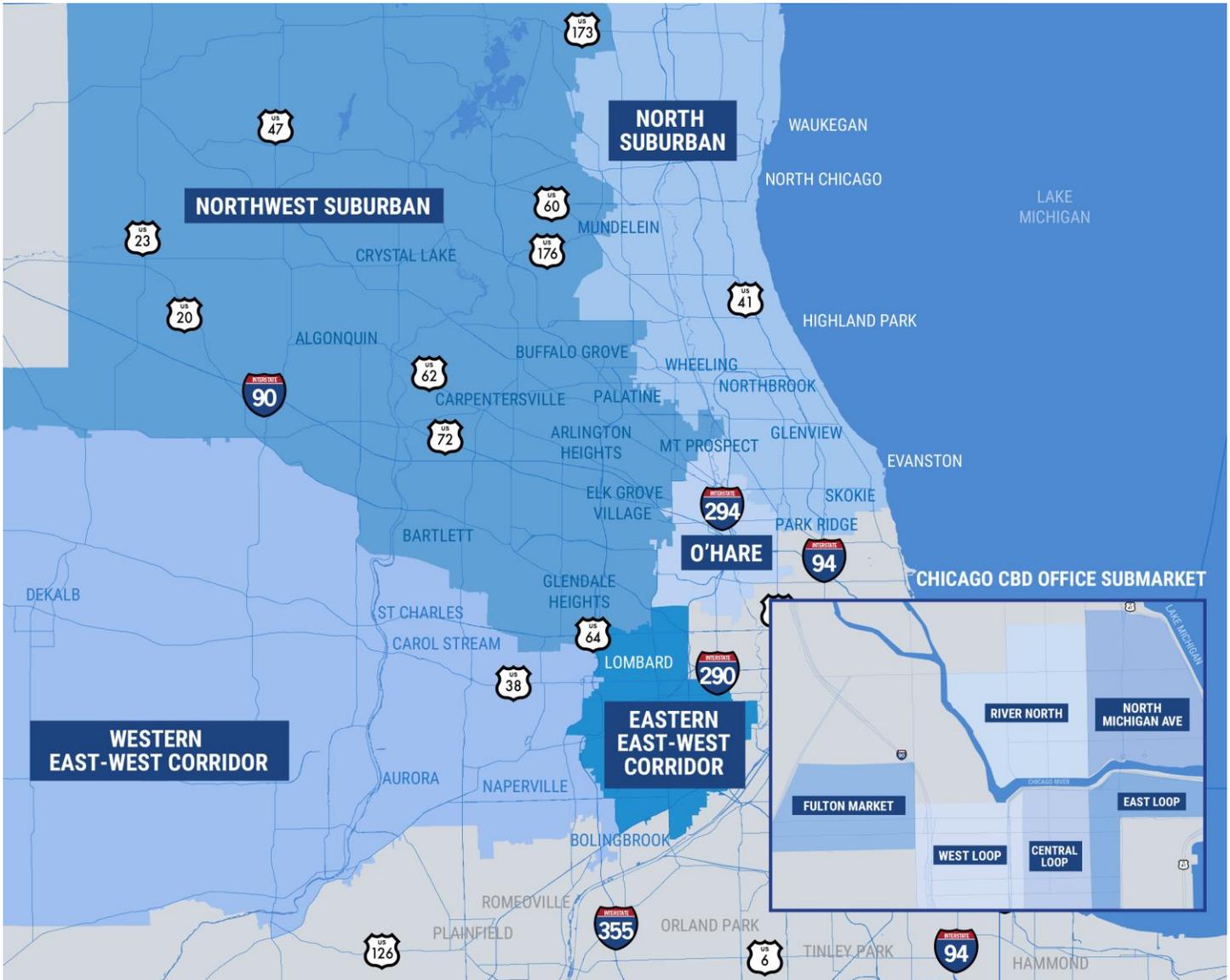
Source: U.S. Bureau of Labor Statistics

EMPLOYMENT GROWTH BY INDUSTRY

Chicago, May 2020, 12-Month % Change, Seasonally Adj.



Source: Bureau of Labor Statistics



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