The Lee Office Brief

Q2 2014

Click below. Interactive tabs

LEE & ASSOCIATES®

COMMERCIAL REAL ESTATE SERVICES

100% increase in transaction volume over 5 years

$7.9 billion transaction volume 2013

778 agents and growing nationwide

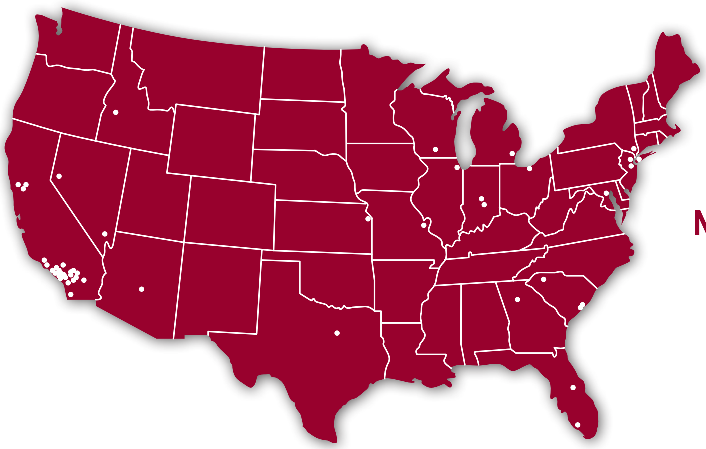
LOCAL EXPERTISE. NATIONAL REACH. WORLD CLASS.

At Lee & Associates® our reach is national but our expertise is local market implementation. This translates into seamless, consistent execution and value driven market-to-market services.

Our agents understand real estate and accountability. They provide an integrated approach to leasing, operational efficiencies, capital markets, property management, valuation, disposition, development, research and consulting.

We are creative strategists who provide value and custom solutions, enabling our clients to make profitable decisions.

OFFICE
INDUSTRIAL
RETAIL
INVESTMENT
APPRAISAL
MULTI-FAMILY
LAND
PROPERTY MANAGEMENT
FACILITY SERVICES
VALUATION & CONSULTING



NATIONWIDE LOCATIONS

Cleveland, OH • Long Island-Queens, NY • Chesapeake Region , MD • Charleston, SC • Edison, NJ • Orlando, FL • Fort Myers, FL • Kansas City, KS • Manhattan, NY • Greenville, SC • Atlanta, GA • Greenwood, IN • Indianapolis, IN • Long Beach, CA • Little Falls, NJ • Boise, ID • Palm Desert, CA • Santa Barbara, CA • Antelope Valley, CA • Dallas, TX • Madison, WI • Oakland, CA • Reno, NV • San Diego, CA • Ventura, CA • San Luis Obispo, CA • Southfield, MI • Santa Maria, CA • Calabasas, CA • St. Louis, MO • Chicago, IL • Victorville, CA • Temecula Valley, CA • Central LA, CA • Sherman Oaks, CA • West LA, CA • Pleasanton, CA • Stockton, CA • Las Vegas, NV • Phoenix, AZ • Carlsbad, CA • Industry, CA • Los Angeles, CA • Riverside, CA • Ontario, CA • Newport Beach, CA • Orange, CA • Irvine, CA

National Economic Overview

The US office property market continued on a steady course of progress, shaving another 10 basis points off the vacancy rate for the third consecutive quarter. The benchmark rate now stands at 11.4%. While there are several markets outperforming the national average, net absorption and leasing activity is consistently positive across the country in both primary and secondary markets. The national economy is expanding just enough to keep job growth positive and office space users are capturing a disproportionate share of employment gains. Rents are on the rise, as well. The combined rate for all building classes rose slightly in the second quarter to $23.99, up 3.4% year-over-year. However, several markets have seen more rapid rent growth over the past year. San Francisco office rental rates have risen by 12.8% in just four quarters. Houston's rents are up 6.4% in the same period and Dallas rents are also up by 4.5%.

The national office market posted 24,500,000 square feet of net absorption in the second quarter, well above the 18,000,000 registered in Q1. All building classes picked up the pace in Q2. Class A and class B net absorption was evenly split at 10,000,000 square feet each, but net absorption in suburban markets is out-pacing that of the Central Business Districts. Class C net absorption rebounded to just over 3,500,000, up from just over 1,000,000 in Q1. Overall, net absorption for all office property types is up 35% year-over-year. These numbers are particularly impressive given the fact that many users can still accommodate significant internal growth by "reabsorbing" existing space that was underutilized during the recession. Add the fact that space allocated to each worker is trending down as businesses move toward more open floor plans to accommodate the preferences of the millennial generation that now make up over 35% of the workface. These workers are attracted to the new "creative" space design, which promotes communication and collaboration through the use of more common areas for socializing and recreation. Privacy for these workers is less important than their baby boomer counterparts, largely due to their preference for communicating via text, email and social media.

Construction activity is also up compared to the same period in 2013. 95,000,000 square feet of office property is underway, up a healthy 27% over 2013's second quarter. Deliveries year-to-date are up by 17% to 21,000,000. It is important to note, however, that over half of the current construction activity is concentrated in just 7 markets, led by Houston at 17,000,000 square feet. Preleased space accounts for over 65% of the square footage under construction, which reflects large build-to-suit deals in major markets. However, that number is trending down as healthier market metrics are encouraging more speculative projects.

The sale market is also making significant gains. Cap rates for the highest quality office properties are sub 5%, but the average cap rate for all office property classes nationwide is still in the 7.5% range. Demand for property acquisition in major markets is strong, and competitive bidding for quality assets is becoming more common. In Q2 of 2014, over $52 Billion in office property sales took place, up sharply from $15 Billion in the first quarter.

The office market has certainly come a long way from its low point in 2009, and the current trajectory appears to be sustainable. Now let's take a closer look at key economic factors and use trends that will influence market performance over the next several quarters:

Click below on interactive tabs

GDP GROWTH | JOB GROWTH | MONETARY POLICY | POLITICS | DEFICITS | A LOOK AHEAD

GDP GROWTH

Gross Domestic Product (GDP) has long been a primary benchmark for assessing economic health. First quarter GDP was negative, but preliminary estimates for Q2 suggest a surge that will put the nation back on course to continue growing the 2% range, which is still substantially less than in previous recoveries. Many blame the depth and breadth of what came to be known as the 'Great Recession', which hit all elements of the economy hard, especially the financial sector. While it is true that our overall economy has improved, there remains an element of uncertainty that has kept GDP advancing at a sluggish pace. Consumer spending growth, which accounts for 70% of GDP, has been nominal as consumers focus on reducing debt accumulated during the recession. The bright spot when it comes to economic growth is related to energy production, as advances in methods to free up natural gas and oil are fueling an energy boom. North Dakota, which now boasts the lowest unemployment rate in the nation, has led the way with its Bakken oil field production. Along with generating good-paying jobs, energy production boosts GDP growth by reducing imports, a key component of the GDP formula. Growth in the tech sector is also giving a boost to GDP, which will continue to support strong gains in the office property market.

JOB GROWTH

The current cycle of economic expansion has often been referred to as a "jobless recovery." The unemployment rate has been slow to fall from its peak of 10% back in 2010. Moreover, much of the reduction in the unemployment rate, which now stands at 6.2%, has come from discouraged job seekers leaving the workforce rather than through the creation of new jobs. This has made the traditional unemployment rate a less reliable indicator of economic health. The Labor Participation Rate, which measures the percentage of the potential workforce engaged in work activity, is a more telling indicator. That index stands at approximately 63%, the lowest it has been in four decades. There has also been a shift to more part time jobs, as employers wary of unknown costs of the Affordable Care Act and it's affect on the economy, are hiring workers below the law's 30 hour per week threshold for full time employment. That said, net job growth is becoming more consistent, month-to-month. Good news came in May as revised estimates for new job creation hit 288,000, the best month of 2014, by a large margin. The office market is the prime beneficiary of the improving job picture, as growth in office using jobs is leading the way. Markets with the highest levels of net absorption have rapidly growing tech sectors, San Francisco being a prime example.

MONETARY POLICY

In addition, to keeping its benchmark rates near zero for several years now, the Federal Reserve Bank has been engaged in a massive bond buying program meant to increase the flow and decrease the cost of capital throughout the economy. The Fed has added over $4 Trillion to its balance sheet for the program known as Quantitative Easing (QE) with mixed results. Until recently, the central bank was buying back US Treasuries and purchasing Residential Mortgage-Backed Securities (RMBS) at a rate of $85 Billion per month. In December of 2013, the Fed began scaling the program back, reducing monthly purchases by $10 Billion per month. Inflation fears associated with the Fed pullback have not yet materialized. If the program can be up unwound without igniting an inflationary cycle, confidence should increase and office lease and sale activity could accelerate. However, as QE is phased out, mortgage rates are likely to rise, which could put pressure on cap rates to move back up to maintain the spread to the cost of capital.

POLITICS

With the midterm elections just a few months away, it is unlikely that any significant legislation will be enacted this year. Immigration reform, balancing the budget and other big issues will be on the back burner, at least until next year. Current gridlock in Congress due to having opposing parties in control of the Senate and House of Representatives, has Congressional approval ratings at all time lows, and several political scandals within the Executive Branch have captured media headlines in recent months.

Concerns over the poor rollout of the Affordable Care Act and confusion over the potential impact of multiple changes to the law by executive order, has created additional uncertainty over the cost of the controversial health care law. Forward planning for expansion is more difficult as a result, which could negatively affect absorption in the near term.

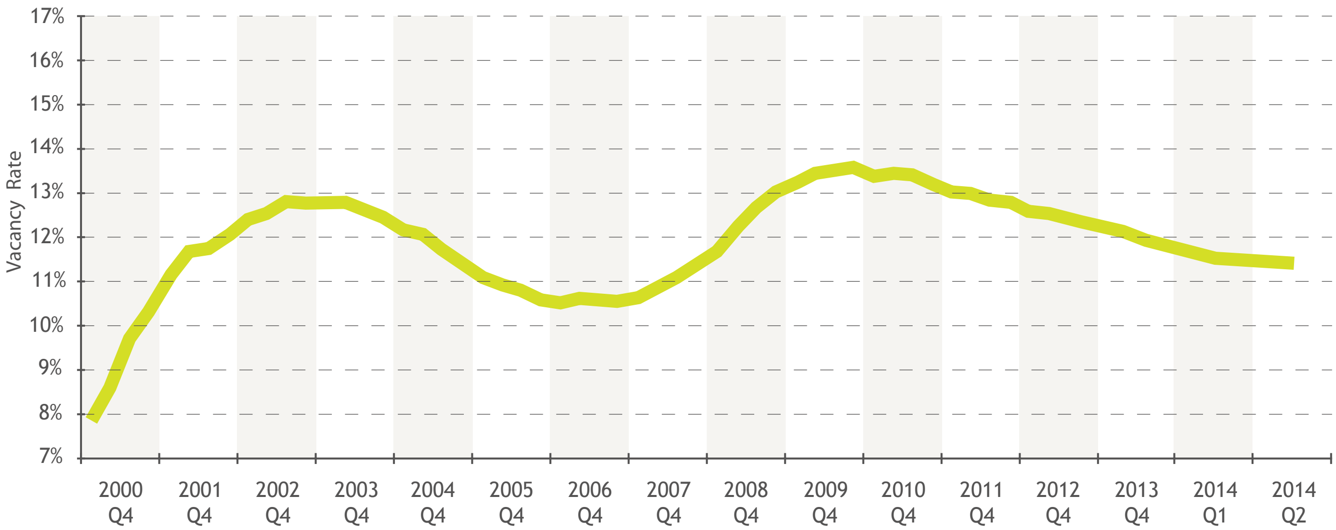
DEFICITS

Federal deficit spending fell in the 2013 fiscal year to $680 Billion, a staggering sum, but down from over $1 Trillion the year before. The narrowing gap can be attributed to the increases in income and capital gains tax rates, mandatory cuts due to Sequestration, the winding down of two wars and other cost cutting measures at the federal level. The national debt, at over $17 Trillion, is still rising with no change in trajectory in sight at the moment. The Affordable Care Act has captured the recent headlines on the entitlement front, but concerns over unfunded liabilities for Social Security, Medicare and Medicaid over the long term are still looming as the Baby Boom generation, the largest in American history, moves into retirement. Attempts by the US House of Representatives to legislate spending cuts are generally considered dead on arrival when they reach the US Senate. When the Fed finally starts raising interest rates, debt service on US Treasuries will increase accordingly, exacerbating the deficit issue. How federal deficits will impact absorption directly is unknown. At minimum, it will add to the uncertainty over other issues facing the office property market.

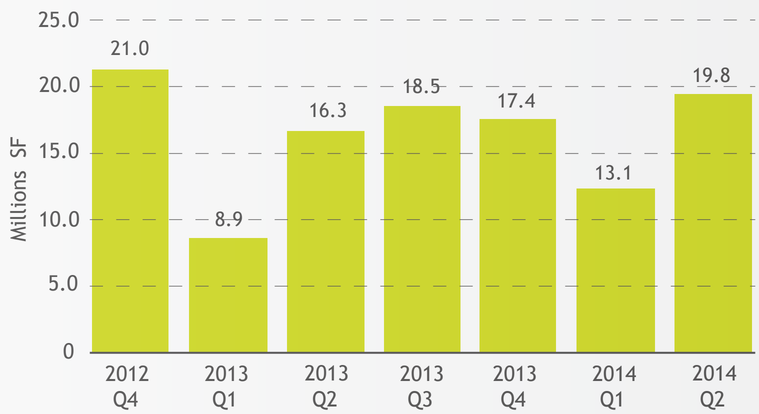
A LOOK AHEAD. The office property market should continue to improve through the balance of 2014. Vacancy will continue its steady decline and rental rates will move up accordingly. Net absorption will stay in positive territory, as the economy remains in expansion mode. Markets heavy in energy and technology will be the top performers. Keep a close eye on Houston (energy) and San Francisco (technology), as both those markets are leading the charge in their respective niches.

The generational shift from Baby Boomers to Millennials will continue to influence how space is utilized and could even slow net absorption as companies shift from traditional to more creative space designs. Institutional investors will expand their acquisition criteria to include older properties in gentrifying areas that can be retrofit to satisfy the growing need for creative space alternatives.

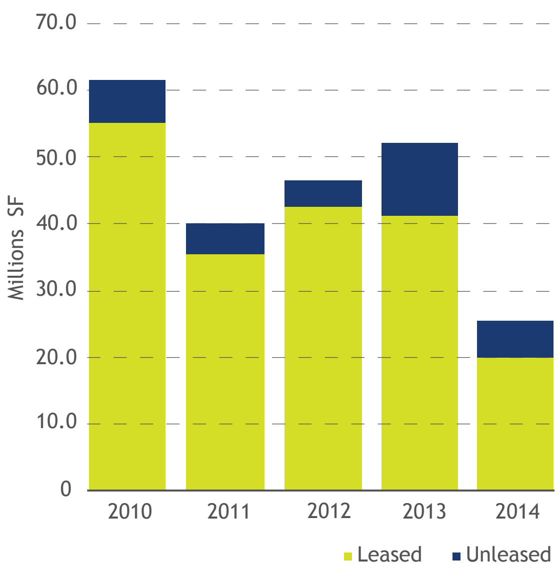
Vacancy Rate 2000 - 2014



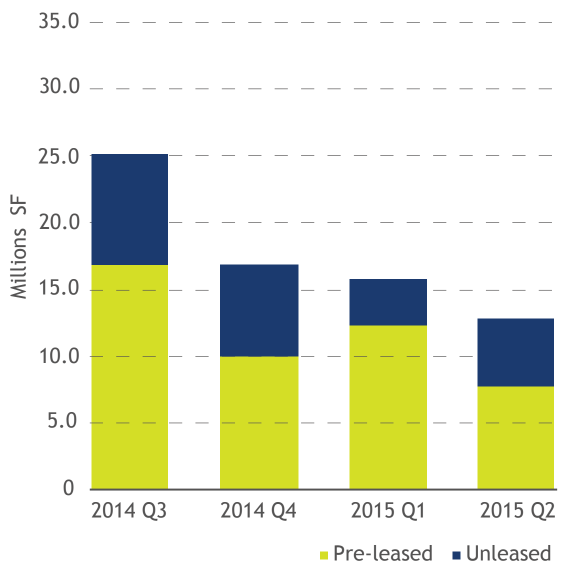
Net Absorption



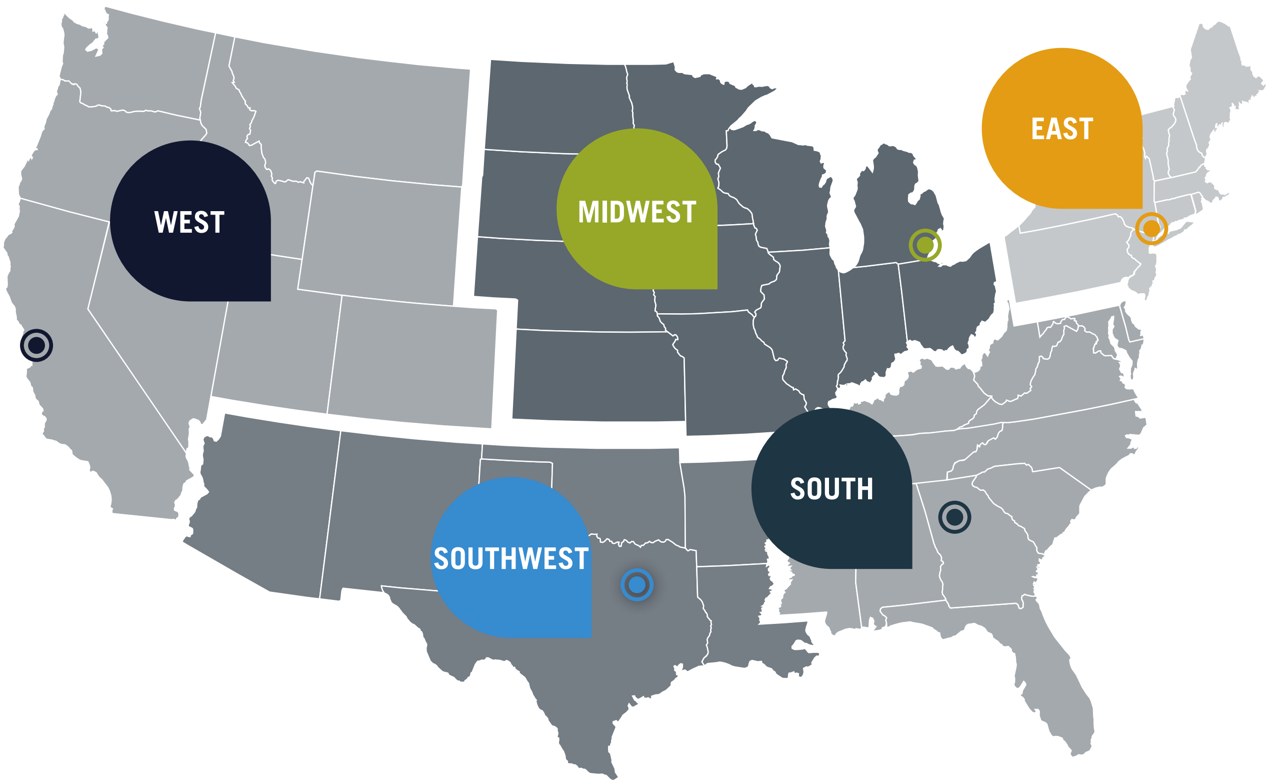
Recent Deliveries



Future Deliveries



Key Market Snapshots



To view a key market snapshot either click on a section of the interactive map above or on the cities below.

SAN FRANCISCO

DALLAS / FORT WORTH

DETROIT

ATLANTA

NEW YORK

SAN FRANCISCO OVERVIEW

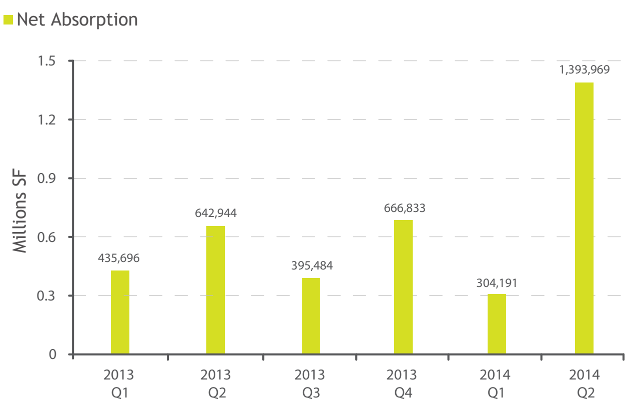
It's good to be a landlord in San Francisco. Market metrics have been shifting the advantage to office property owners for the past several years, and Q2 2014 results show that the trend is accelerating. Net absorption for the quarter came in just under 1.4 million square feet, while lease rates are up 12.8% from a year ago and a whopping 59% since 2010. Those numbers confirm that San Francisco is outperforming nearly every major market in the country. Development activity is also on the upswing. Roughly two thirds of the 5.6 million square feet currently under construction is preleased. Even with the new inventory, leasing activity has been strong enough to keep vacancy heading lower. The benchmark rate now stands at 8.3%, down 80 basis points since the first quarter and the lowest of the nation's 20 largest markets.

What's driving this explosive growth? Technology. The city by the bay is being driven by all things tech, which accounts for nearly 60% of leasing activity in 2014. Salesforce.com and LinkedIn both inked deals in the second quarter combining for over 1.1 million square feet of new leasing activity. Dropbox and Splunk, Inc. also signed leases for over 90K square feet this year.

The unemployment situation paints an even rosier picture for the region. The unemployment rate fell to 4.4% in the second quarter, well under the statewide and national rates of 7.4% and 6.2% respectively. Job growth is coming mainly from Professional and Business Services, which includes much of the technology sector.

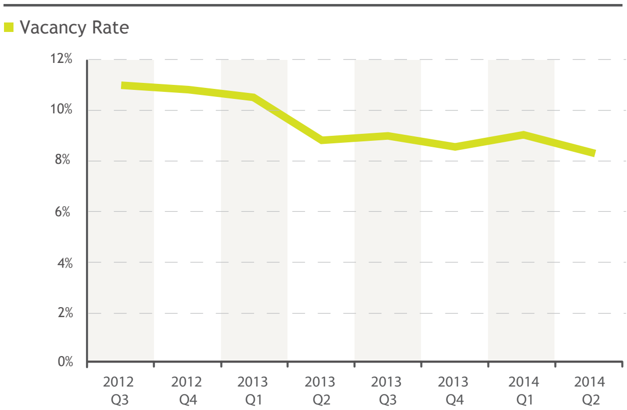
Net Absorption

Past 6 Quarters



Vacancy Rate

Past 8 Quarters



8.3%	$43.90	1,393,969	88,038,000	5,616,976
VACANCY	**AVG. SF RENTAL RATES**	**NET SF ABSORPTION**	**OFFICE SF INVENTORY**	**SF UNDER CONSTRUCTION**

SAN FRANCISCO OVERVIEW (continued)

Opportunities

Tenants:

- Those willing to pre-commit and pay a premium price will be able to secure new, state-of-art space for long term occupancy in an amenity-rich environment.
- Concentration of talented tech workers in the area will help fuel business expansion

Buyers:

- Long term rent growth potential will allow buyers to pay more in competitive bidding situations.

Landlords:

- Competition for space will allow landlords to keep rents moving up.
- Reduced credit risk due to strong credit tenants moving into the region.

Sellers:

- Cap rates will stay low.
- Demand for quality assets will increase competitive bidding.

Developers:

- Those with projects underway will achieve higher than expected returns due to rapidly rising rents.
- Anticipated rent growth will make riskier projects easier to pencil.

Challenges

Tenants:

- Competition for larger blocks of quality space will increase.
- Rising rents due to tech boom could drive some existing tenants from the area.

Buyers:

- Very little product for sale will force buyers into riskier acquisitions.

Landlords:

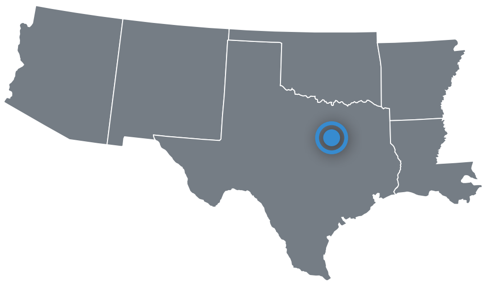
- Lower quality space being vacated by tenants moving to new buildings will take longer to lease and cost more to retrofit to meet tenant preferences.

Developers:

- Scarcity of development opportunities due to intense competition.

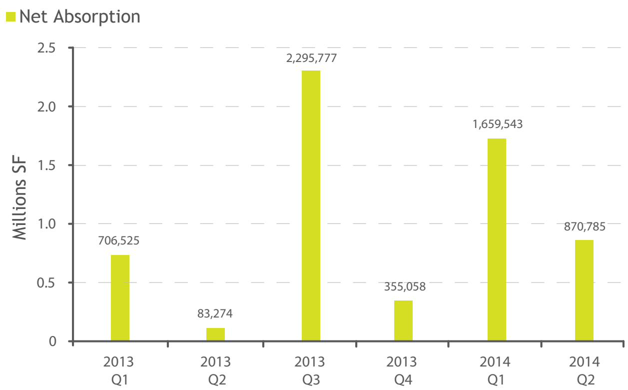
A LOOK AHEAD. San Francisco's near term future looks as bright as any metropolitan region of the country. The area is already a growth leader, and that growth is being fueled by the business sector expected to produce the most jobs over the next several years. Given its current trajectory and momentum, rents should continue to move up aggressively and net absorption will rise as larger tech users take down large blocks of space. Development will continue, but the availability of opportunities to build will become more limited. Tenants in less growth-oriented industries may be forced from the area due to rising rents.

DALLAS / FORT WORTH OVERVIEW



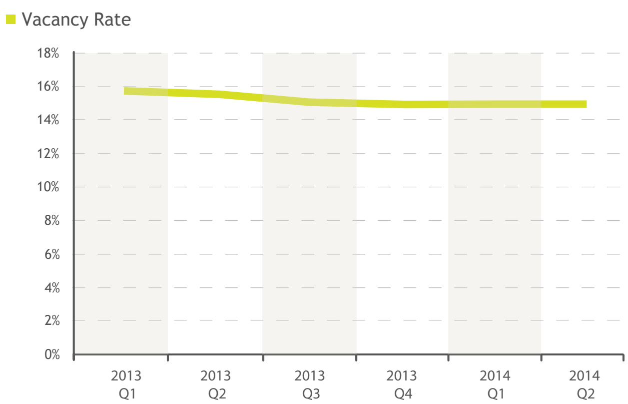
Net Absorption

Past 6 Quarters



Vacancy Rate

Past 6 Quarters



Since the US emerged from recession in 2010, the Dallas/Fort Worth (DFW) economy has outperformed nearly every major market. Leading indicators are signaling further growth and business expansion. The unemployment rate now stands at 5.0%, compared the national rate of 6.2%. Population growth is robust and leasing activity is up. Large corporations have decided on DFW for expansion, most notably Toyota Motor Company, State Farm Insurance and Santander Consumer USA, each signing leases that will create thousands of new, high-paying jobs. The Texas state government remains active in pursuing major companies from around the world, as it touts lower tax rates, a diverse labor base and land for future growth, all critical components of long range expansion strategies.

The vacancy rate held steady at 14.9% during Q2 of 2014, in part to due significant deliveries of new product, some of which was not pre-leased. However, confidence in market growth should keep the construction boom going. Close to 1,000,000 square feet was delivered in Q2 and another 4,900,000 is underway. If not for this spike in construction, the vacancy picture would be much tighter. DFW is one of just a few markets in the country with speculative development underway.

Net absorption was positive at 870,785 for Q2. Suburban submarkets are seeing the bulk of the net absorption, as that is where most of the construction activity is centered. Several big move-outs during Q2 did put a damper on net absorption, but with so many big move-ins expected, the absorption picture looks good going forward. Rents are also moving up, but not enough to dampen the enthusiasm of expanding businesses. The average asking lease rate for the DFW area settled at $21.01, which is up $.92 year-over-year. Class A rates are heading up at a higher pace, but rent growth in all building classes varies widely by submarket.

14.9%	$21.01	870,785	338,874,654	6,323,099
VACANCY	**AVG. SF RENTAL RATES**	**NET SF ABSORPTION**	**OFFICE SF INVENTORY**	**SF UNDER CONSTRUCTION**

DALLAS / FORT WORTH OVERVIEW (continued)

Opportunities

Tenants:

- Tenants with stabilized space requirements will benefit by committing to longer term leases at current pricing structure.

Buyers:

- Owner/user buyers will have to compete for good properties, but successful bidders will fix occupancy cost before the Federal Reserve makes a move on interest rates.

Landlords:

- Concession packages will decline as tenants compete for space in a market with lower vacancy.

Sellers:

- High demand is compressing cap rates and increasing competition from motivated buyers.

Developers:

- With such strong leasing activity, preleasing requirements will be reduced, allowing more projects to receive funding and get underway.

Challenges

Tenants:

- Occupancy costs will rise with rents and choice of existing quality product will be reduced.

Buyers:

- Shortage of existing product for sale could delay expansion plans, as build-to-suit becomes the preferred option for owner/occupants.

Landlords:

- For those suffering major move-outs in older spaces, retrofit costs to return space to competitive status will increase.

Sellers:

- Those owners with CMBS loans containing significant defeasance costs will be forced to keep assets that would otherwise be sold.

Developers:

- Land prices and construction costs are on the rise, increasing risk and lowering projected returns.

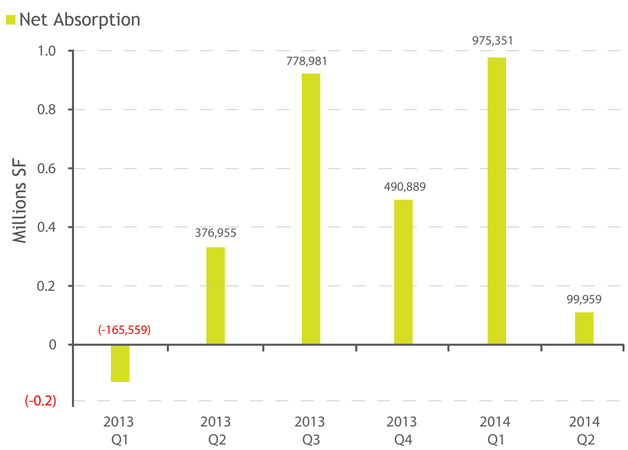
A LOOK AHEAD. The Dallas/Fort Worth area is outperforming virtually every market in the country outside the State of Texas. It touts a business friendly environment, a deep and diverse labor base, an affordable quality lifestyle and room to expand in all directions. Accordingly, major corporations will continue to be attracted to the area. Market restrictions like high tax rates, a lack of land and higher living costs associated with other major markets, gives the Dallas/Fort Worth office market a massive advantage, especially in attracting the biggest companies who must think long term. Net absorption has been consistently positive for four straight years and that trend should continue. Lease rates will rise, but slowly, as continued speculative construction will keep landlords competing for the best tenants. Look for more major companies to announce plans to relocate or expand in the Dallas/Fort Worth areas in the next several years.

DETROIT OVERVIEW

The Detroit office market continues to gain momentum even as the city faces the nation's largest ever municipal bankruptcy proceeding. Absorption was positive in both suburban and downtown areas, and vacancy is inching down to levels seen in other major markets hit hard by the 2008 financial crisis. Overall, vacancy stands at 16.7%. The Airport District's rate is lowest at 4.9%, while Pontiac posted the highest rate of 29.2% in Q2.

Net Absorption

Past 6 Quarters

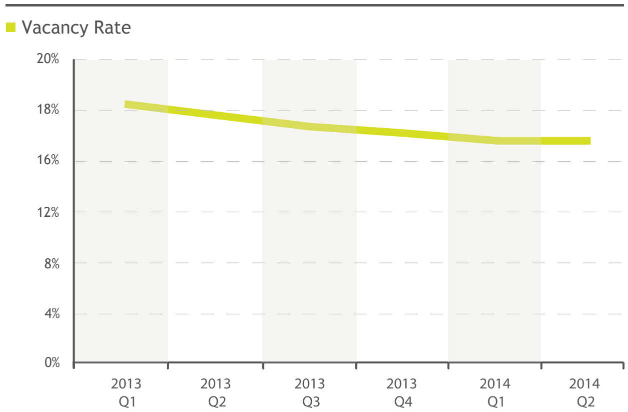


Leading economic indicators are heading in the right direction. Unemployment rates in Detroit and the State of Michigan have fallen to 8.0% and 7.3% respectively, but are still above the national rate of 6.2%. The slow improvement in unemployment mirrors the positive but nominal net absorption figures, as job growth is the key driver of occupancy growth. Detroit has a long way to go in terms of a return to market equilibrium, but more businesses are going back on offense, choosing to expand while occupancy cost remains relatively low.

Lease rate trajectory is beginning to turn, as well. For the quarter, average asking rates for Class A space rose $.10 to $20.54, and Class B rates moved up $.06 to $17.11. Suburban and Downtown properties have been similarly affected. However, rates vary widely between suburban submarkets, as some areas were hit harder than others by the recession.

Vacancy Rate

Past 6 Quarters



Sale activity is rising, as private and institutional investors are showing more interest in Detroit due to its potential for net income growth. Sales since the beginning of 2014 include the Dan Gilbert acquisition of the 400,000 square foot First National building downtown and the $177 Million purchase of Southfield Town Center by 601 W Companies. Higher yields and pricing under replacement cost is fueling the activity for both value-add and stabilized assets.

16.7%	$17.49	99,959	196,541,041	89,168
VACANCY	**AVG. SF RENTAL RATES**	**NET SF ABSORPTION**	**OFFICE SF INVENTORY**	**SF UNDER CONSTRUCTION**

DETROIT OVERVIEW
(continued)

Opportunities

Tenants:

- Businesses that can move forward with expansion plans are able to lock in very low occupancy cost over time and mitigate moving costs with generous landlord concessions.

Buyers:

- Those with cash and a long term investment strategy can acquire quality assets under replacement cost.

Landlords:

- Owners of assets acquired at distressed property pricing will have a competitive advantage due to the basis.

Sellers:

- A larger pool of investors, attracted to the higher returns for Detroit, will boost investment sales.

Developers:

- Recent market performance is renewing interest from lenders to fund new projects in prime locations.

Challenges

Tenants:

- Remaining uncertainty over the outcome of the bankruptcy and its affect on future economic growth.

Buyers:

- Lenders are still cautious in lending in the Detroit area due to ongoing economic uncertainty.

Landlords:

- Vacancy still very high in some submarkets and is limiting rent growth.
- Landlords must continue to offer generous tenant concessions to fill space.

Sellers:

- Pricing of older product in high vacancy submarkets will remain low, as activity will be limited to value-add buyers.

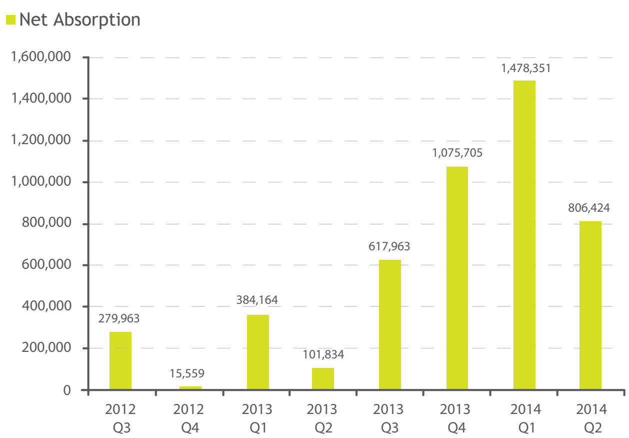
Developers:

- Strict pre-leasing guidelines from lenders will make new projects very difficult to finance.

A LOOK AHEAD. Recent activity appears to have signaled a turnaround in the Detroit area. The United States and Michigan economies continue to grow, and more businesses and investors are taking an interest in the resurgent Detroit market. The increase in activity at the institutional level is particularly important, as those investors look to the long term when making major acquisitions. This renewed interest bodes well for Detroit, and is increasing optimism within the business community at large. Looming uncertainty over the municipal bankruptcy will still weigh heavy on business and investor plans for growth and acquisitions. Employment growth is expected to continue through the balance of the year, keeping net absorption and rent growth on its current directory. It is also important to note that the stark differences in conditions submarket to submarket, which means that pockets of high activity in prime submarkets will account for most of the market growth, while other areas will take much longer to return to healthier conditions.

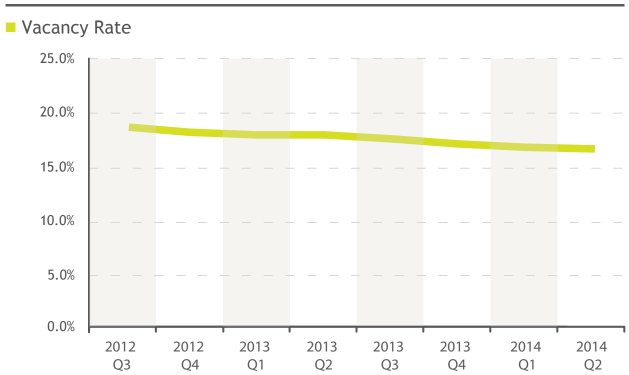
Net Absorption

Past 8 Quarters



Vacancy Rate

Past 8 Quarters



ATLANTA OVERVIEW

Atlanta's office market has stabilized. Overall activity is approaching pre-recession levels and the market has settled into a pattern of positive net absorption. With consistency comes certainty, and tenants are now clear on the fact that vacancy is on the way down, and that means rents will be on their way back up. Such is the case, as the overall lease rate by the end of Q2 came in at $19.62 up from $19.42 in the first quarter. Year-over-year rents are up by $0.30 per square foot or 1.5%. It is understandable that more tenants are making moves now to lock in long term deals before the market really takes off. Larger users may have to move the fastest, as there is an increasing likelihood of a shortage of large blocks of space as positive absorption continues.

The lack of new deliveries to the market has been helpful with regard to vacancy. Supply has been static for several quarters and that has given the office market a chance to make up ground lost during the recession. Estimates of actual vacancy vary; however, the direction of the benchmark rate is declining by all accounts, and that has signaled developers to get going with new projects sooner rather than later. Currently, there is just over 776,000 square feet of space under construction, concentrated in prime submarkets like North Fulton, Buckhead and the Central Perimeter, where lease rates above the regional average can be achieved.

Sale activity is lower year-over-year, more due to lack of supply than demand. As in other major metro markets around the country, interest in office properties in Atlanta from institutional investors remains at high levels. They recognize the current direction of the market as having potential for higher net income due to rising rents.

16.9%	$19.62	2,227,958	210,348,158	776,642
VACANCY	AVG. SF RENTAL RATES	NET SF ABSORPTION	OFFICE SF INVENTORY	SF UNDER CONSTRUCTION

ATLANTA OVERVIEW (continued)

Opportunities

Tenants:

- Businesses desiring to upgrade to class A buildings can do so at rates well below other major metro markets.

Buyers:

- Upside potential for net income through rising rents will allow buyers to pay a premium for quality properties.

Landlords:

- Long term holders of office product will benefit from current rent trends.
- Concessions will decline with vacancy over the next several quarters.

Sellers:

- Lack of product available for sale will create competitive bidding for assets that do come to market.

Developers:

- Consistent reduction in vacancy and increase in absorption will loosen underwriting criteria for lenders.

Challenges

Tenants:

- For large space users, choice will diminish.
- Lack of new speculative product reduces choice of quality space.

Buyers:

- Lack of product for sale will keep cap rates low.
- Leverage buyers will be at a disadvantage if interest rates move higher.

Landlords:

- Large tenants lost to new developments could increase vacancy in older, class B properties.

Developers:

- Lease rates are still under threshold to pencil high quality product, except in prime submarkets.

A LOOK AHEAD. Atlanta's overall economy is returning to good health. The unemployment rate is coming down and positive job growth will keep it moving in the right direction. Vacancy declines will continue, as will gains in net absorption. Business outlook is optimistic, as more users are looking for opportunities to grow rather than reacting to fear of decline. Timing the delivery of new product to the actual needs of the business community will be key to Atlanta's long term market growth. Investor interest in Atlanta will increase as long as current market metrics continue.

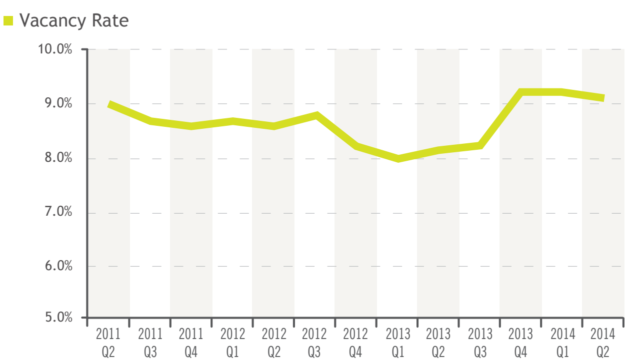
NEW YORK OVERVIEW

Net Absorption

Quarters 2011 - 2014

Vacancy Rate

Quarters 2011 - 2014



With demand pacing well ahead of current supply, the overall Manhattan office market continues to gain steam. The average asking rental rate for direct lease space now stands at $65.32 per square foot, up $4.21 since Q2 of 2013. Leasing activity for the second quarter came in at 8.2 million square feet, up 16.9% year-over-year. Year-to-date transaction volume stands at 20,125,265 square feet. The spike in leasing activity is not at all surprising given that, between May 2013 and May 2014, private sector job growth stood at 2.3%, as compared to the US rate of 2.1%, and the State of New York's 1.4%. Major office-using sectors of the market combined to create 20,000 new jobs; while education and health services added 27,000 and hospitality employment grew by another 9,800.

While demand has spiked, supply shrank by contrast. Availability declined 20 basis points to 11.3%, bringing the year over year rate down a full 100 basis points. In fact, Q2 2014 marked the first time since the downturn that the supply of available space dropped below 50 million square feet.

Contributing to the declines in availability is that there has been very little new construction in Manhattan over the past 10 years. However, several high profile developments, totaling over 9.6 million square feet, are scheduled for completion by 2018. Among these include the One World Trade Center, scheduled to be completed by Q4 of this year, which alone will add 3 million square feet to the Downtown market.

Sale and lease activity has been strong among Class B and even Class C product because of the popularity of their locales: SoHo, NoHo, the Gramercy Flatiron district, Hudson Square and Tribeca. The Downtown submarket is also faring better, as tenants, priced out of Midtown and Midtown-South, migrate south.

9.1%	$65.32	360,818	435,304,883	8,182,086
VACANCY	**AVG. SF RENTAL RATES ***	**NET SF ABSORPTION**	**OFFICE SF INVENTORY**	**SF UNDER CONSTRUCTION**

* Average Direct SF Rental Rates

NEW YORK OVERVIEW (continued)

Opportunities

Tenants:

- Along with several options for larger spaces, 100,000 square feet and up, tenants can make high value deals in soft submarkets.

Buyers:

- Given the popularity of locales where Class B and C buildings are found, buyers willing to renovate will achieve higher rates.

Landlords:

- As demand rises for small to mid-sized spaces, 5000-15,000 square feet, landlords can command high asking rents in the Midtown-South submarket.

Sellers:

- Manhattan's office sector remains a seller's market as demand outstrips supply by a wide margin.

Developers:

- Recent market performance is renewing interest from lenders to fund new projects in prime locations.

Challenges

Tenants:

- Supply of quality space is tightening quickly.
- Landlords are negotiating smaller concession packages.

Buyers:

- Strong demand from foreign cash buyers will make leverage deals harder to complete.

Landlords:

- Owners of large blocks of available space in Midtown will have to get more aggressive to secure tenants and be vigilant when leasing to often evanescent start-ups.

Sellers:

- Pricing of older product in high vacancy submarkets will remain low, as activity will be limited to add-value buyers.

Developers:

- Expect New York's new political leadership to tighten regulatory control.

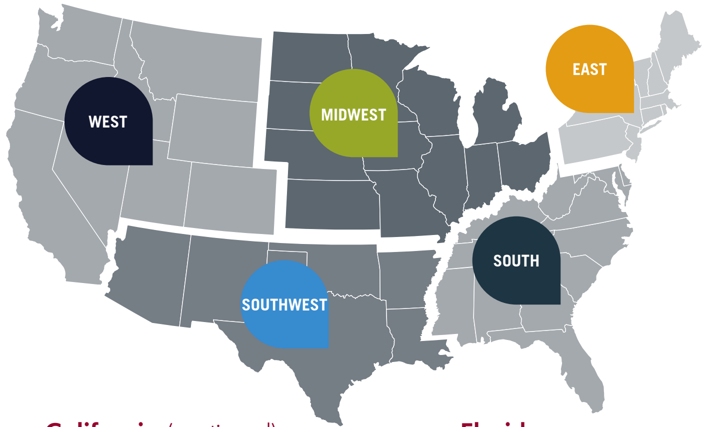
A LOOK AHEAD. With the One World Trade Center scheduled for completion at the end of Q4, adding 3 million square feet of space, expect the availability rate to go up. Even so, leasing activity will surpass last year's activity of 35.9 million square feet and sales volume will also increase. Average asking rents will continue to move up, perhaps by as much as 10-12 percent over 2013. Domestic investors must be willing to compete with foreign money driven by New York's rent growth and stability.

Significant Transactions

ADDRESS	TRANSACTION	PRICE / SF	BUYER / TENANT	SELLER
ATLANTA				
AT&T Midtown I & II	$205 million sale of 794,110 SF property	$258.15	Cole Real Estate Investments	Kan Am Group LLC
The Terraces	$190 million sale of 1,053,891 SF property	$180.28	MetLife, Inc	Royal Bank of Scotland Group PLC
999 Peachtree Street	$157.9 million sale of 621,007 SF property	$254.26	Franklin Street Properties Corporation	Jamestown
DALLAS				
Colonade	$205 million sale of 1,051,641 SF property	$194.93	Fortis Property Group, LLC	CBRE Global Investors
The Urban Towers	$126 million sale of 848,591 SF property	$148.48	Parallel Capital Partners, Inc.	CBRE Global Investors
Premier Place	$87.92 million sale of 409,894 SF property	$214.49	Illinois State Board of Investors	CBRE Global Investors
DETROIT				
Southfield Town Center	$177.5 million sale of 2,161,951 SF property	$82.10	The 601W Companies	The Blackstone Group
Earhart Corporate Center	$43.9 million sale of 200,000 SF property	$219.50	CapLease, Inc	Kojanian Management Corporation
Northeast Corporate Center	$21.5 million sale of 223,568 SF property	$96.17	Oxford Commercial	CW Capital Asset Management
NEW YORK				
5 Times Square	$1.55 billion sale of 1,101,779 SF property	$1,406.82	David Werner Real Estate	AVR Realty
388 Greenwich Street (2 Properties)	$778.05 million sale of 2,634,674 SF property	$597.80	SL Green Realty Corp	Ivanhoe Cambridge, Inc
450 Park Avenue	$545,75 million sale of 223,568 SF property	$1,630.46	Oxford Properties Group	Somerset Partners LLC
SAN FRANCISCO				
225 Bush Street	$350 million sale of 557,972 SF property	$627.00	Kylli, Inc. / Genzon Group	Flynn Properties / GEM
Pacific Place - 22 4th Street (Office/Retail/Hotel)	$415 million sale of 430,000 SF property	$965.00	JP Morgan	Jamestown
55 2nd Street	$278 million sale of 4379,328 SF property	$733.00	TIAA_CREF	Hines / Sumitomo

5

Nationwide Lee Offices



Arizona
Fred Darche
602.956.7777
Phoenix, AZ 85018

California
Clarice Clarke
805.898.4362
Santa Barbara, CA 93101
(Central Coast)

Brian Ward
760.346.2521
Palm Desert, CA 92260
(Greater Palm Springs)

John Hall
949.727.1200
Irvine, CA 92618

Mike Tingus
818.223.4380
LA North/Ventura, CA

Jeff Rinkov
323.720.8484
Commerce, CA 90040
(LA Central)

Joe Chavez
213.623.1305
Los Angeles, CA 90071
(LA ISG)

Greg Gill
562.354.2500
Los Angeles - Long Beach, CA

Duncan Lemmon
310.899.2700
Santa Monica, CA 90404
(LA West)

Steve Jehorek
949.724.1000
Newport Beach, CA 92660

Christopher Bonney
562.699.7500
City Of Industry, CA 91746

California (continued)
Craig Hagglund
510.903.7611
Oakland, CA 94607

Don Kazanjian
909.989.7771
Ontario, CA 91764

Bob Sattler
714.564.7166
Orange, CA 92865

Mike Furay
925.737.4140
Pleasanton, CA 94588

Dave Illsley
951.276.3626
Riverside, CA 92507

Dave Howard
760.929.9700
Carlsbad, CA 92008
(San Diego North)

Steve Malley
858.642.2354
San Diego, CA 9212
(San Diego UTC)

Tom Davis
209.983.1111
Stockton, CA 95206

Dave Illsley
951.276.3626
Murietta, CA 92562
(Temecula Valley)

Don Brown
760.241.5211
Victorville, CA 92392

Florida
Jerry Messonnier
239.210.7610
Ft. Myers, FL 33966
(Naples)

Tom McFadden
321.281.8501
Orlando, FL 32839

Georgia
Dick Bryant
404.442.2810
Atlanta, GA 30326

Idaho
Matt Mahoney
208.343.2300
Boise, ID 83703

Illinois
Brian Tader
773.355.3050
Rosemont, IL 60018

Indiana
Scot Courtney
317.218.1038
Indianapolis, IN 46240

Kansas
Nathan Anderson
913.890.2000
Overland Park, KS 66211
(Kansas City)

Maryland
J. Allan Riorda
443.741.4040
Columbia, MD 21046

Michigan
Jon Savoy
248.351.3500
Southfield, MI 48034

Missouri
Thomas Homco
314.400.4003
St. Louis, MO 63114

Nevada
Steve Spelman
702.739.6222
Las Vegas, NV 89119

Lyle Chamberlain
775.851.5300
Reno, NV 89501

New Jersey
Rick Marchiso
973.475.7055
Elmwood Park, NJ 07407

New York
Jim Wacht
212.776.1202
New York, NY 10022

Ohio
Brad Coven
216.282.0101
Cleveland, OH 44122

South Carolina
Bob Nuttall
843.747.1200
Charleston, SC 29492

Randall Bentley
864.704.1040
Greenville, SC 29601

Texas
Trey Fricke
972.934.4000
Addison, TX 75001

Wisconsin
Todd Waller
608.327.4000
Maddison, WI 53713

The Lee Office Brief

Q2 2014

lee-associates.com

The information and details contained herein have been obtained from third-party sources believed to be reliable; however, Lee & Associates has not independently verified its accuracy.

Lee & Associates makes no representations, guarantees, or express or implied warranties of any kind regarding the accuracy or completeness of the information and details provided herein, including but not limited to the implied warranty of suitability and fitness for a particular purpose.

Interested parties should perform their own due diligence regarding the accuracy of the information. The information provided herein, including any sale or lease terms, is being provided subject to errors, omissions, changes of price or conditions, prior sale or lease, and withdrawal without notice.

Third-party data sources: CoStar Group, Inc., The Economist, U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics, usgovernmentdebt.us, GlobeSt.com, Loopnet, CoStar Property, Lee Propriety Data, and Cocky Rooster Media.

LEE & ASSOCIATES®

COMMERCIAL REAL ESTATE SERVICES