

CLEVELAND OFFICE MARKET

CLEVELAND OFFICE MARKET STABLE AT MIDPOINT OF YEAR

Conditions in the Greater Cleveland office market held steady during the second quarter of 2018, despite 50,490 square feet of negative net absorption. Total absorption for the first half of the year remained in positive territory with 7,887 square feet. The East was the only submarket to post positive net absorption in the second quarter, netting 16,198 square feet in rebounding from the largest tally of negative absorption of any submarket in the first quarter.

The overall negative absorption increased the market's vacancy rate by 50 basis points from the prior quarter to 16.6% for all office properties. Dating back to the second quarter of 2013, when the vacancy rate was 19.6%, the current 16.6% vacancy rate marked a full 3.0% decrease in five years. The average asking rental rate climbed back up slightly across the majority of the Greater Cleveland office market, finishing the second quarter at \$17.70/SF for all classes.

CBD ACTIVITY GARNERS CONSISTENT HEADLINES

The Central Business District's asking rental rate was down \$0.01/SF to \$18.90/SF during the second quarter, and its vacancy rate increased by two basis points to 19.4%, even though its year-to-date absorption was a positive 220,387 square feet, eclipsing its 193,445 square feet of positive year-to-date absorption one year ago. The CBD saw its usual share of robust activity this past quarter through building transfers, pending sales, key announcements and a handful of companies occupying large spaces.

The largest sale of the quarter was the 1.3 million-square-foot 925 Euclid Avenue building (formerly known as the Huntington Building), which transferred for \$40.0 million, or \$29/SF, to Millennia Companies. Millennia has become a major player in the CBD over the last couple of years, having previously purchased Cleveland's tallest building, Key Tower, located at 127 Public Square, in early 2017, as well as the Statler Arms apartment complex in January. The company has also recently been involved in redeveloping other CBD multi-family, restaurant and office assets. Although plans for 925 Euclid Avenue are still being formulated, it is believed that Millennia will proceed with a mixed-use redevelopment that includes apartments, offices, a hotel, dining establishments and additional retail.

The most active CBD owner/developer in the second quarter was the K&D Group, which made headlines with at least four different projects.

CURRENT CONDITIONS

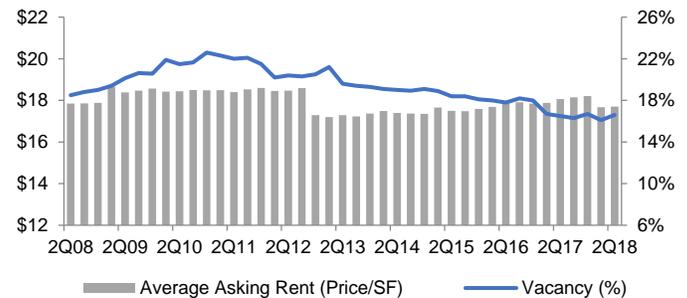
Overall office market remained steady, despite slight uptick in vacancy and some negative absorption; rents did climb slightly, however

CBD activity was robust: completed and pending sales, large tenants occupying space, the K&D Group making splashes, a future new home for the Cleveland Police HQ, big plans for the Superior Arts District, etc.

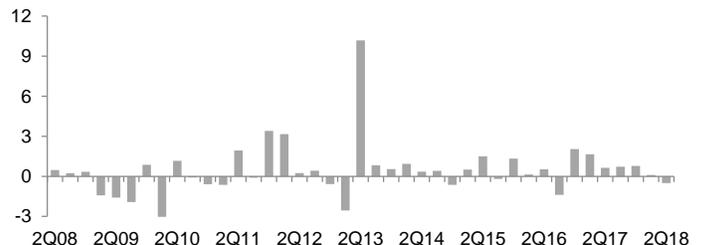
Two highly-anticipated high-end new office buildings delivered: Link59 in the CBD's Midtown micromarket and the Van Aken District office complex

MARKET ANALYSIS

Asking Rent and Vacancy



Net Absorption (SF, Hundred Thousands)



MARKET SUMMARY

	Current Quarter	Prior Quarter	Year Ago Period	12 Month Forecast
Total Inventory	36 MSF	36 MSF	36 MSF	↑
Vacancy Rate	16.6%	16.1%	16.8%	↓
Quarterly Net Absorption	(50,490)	58,377	63,927	↑
Average Asking Rent	\$17.70	\$17.68	\$18.06	↑
Under Construction	327,352	352,575	324,575	↑
Deliveries	127,575	0	0	↑

Perhaps the most significant news regarding K&D came in June, when the company was awarded \$50.0 million in state historic tax credits to help partially fund the \$100 million-plus redevelopment of the city's iconic Terminal Tower, located at 50 Public Square. The project includes the transformation of 12 of the building's lower floors into 300-plus apartments as well as updating existing office spaces and the addition of a restaurant and rooftop deck. In April, K&D sold the 54,000-square-foot Stonebridge Center office building, located at 2019 Center Street, for \$1.7 million, or \$31/SF, to The Hive My Place, Ltd.

K&D made headlines again the following month by announcing its intent to initiate improvements to the 435,000-square-foot Post Office Plaza office building, located at 1500 West 3rd Street, a building the company purchased in the third quarter of 2017. Shortly after this came news of K&D signing a letter of intent to purchase 55 Public Square, a 22-story, 427,000-square-foot property the company plans to partially convert into apartments. The proposed purchase price and closing date are still to be determined.

A couple of key CBD leases also began this past quarter, including Forest City's headquarters occupation of 147,795 square feet at Key Tower and Electronic Merchant Systems' relocation from the South submarket to 48,433 square feet at 250 West Huron Road.

GBX Group (formerly global X) formally settled into its new headquarters at 2101 Superior Avenue at the end of the first quarter. This kicked off the transformation of the Superior Arts District, which was formally designated as an arts improvement district by the city of Cleveland earlier in the year. One component of that plan is to use federal funding to turn Superior's center traffic lane into a buffered bicycle lane that stretches from Public Square to East 55th Street. GBX Group is the largest stakeholder along this stretch of town, having had a hand in redeveloping several buildings, and it is the driving force behind the anticipated remaking of several more of its properties in the district. The company focuses on acquiring historic real estate in urban markets that have significant tax and other incentives available to them. Adding to the newfound excitement in the district was the announcement that the Cleveland Police Department had selected the 250,000-square-foot former *Plain Dealer* building at 1801 Superior Avenue as its new headquarters. The nearly \$60 million deal includes the purchase and renovation of the building by second-quarter 2019. Cleveland.com/Advance Ohio, currently the largest tenant in the building, has tentative plans to stay in the CBD by moving to the Western Reserve Building, located at 1468 West 9th Street.

Another CBD development was the announcement of the planned purchase of the 575,000-square-foot AECOM Centre, located at 1300 East 9th Street, by New Jersey investor Rugby Realty. This transfer was expected to close at the end of the second quarter or beginning of the third quarter. Rugby intends to aggressively market the building's existing vacancy as well as make several common area improvements.

Technology company MCPc occupied 20,000 square feet at the brand-new 61,575-square-foot Link59, which Hemingway Development delivered in the second quarter at 5900 Euclid Avenue. Growth Opportunity Partners also moved into 5,600 square feet at MidTown's newest office building.

Despite the continued optimism and vitality of the CBD office market, planned and ongoing conversions to multi-housing will continue to shrink inventory over the next few years.

VAN AKEN DISTRICT OFFICE DELIVERS IN EAST Suburban Submarkets Compete With But Still Fall Short of CBD

The suburban office submarkets saw an overall average asking rental rate increase of \$0.11/SF, which reached \$16.55/SF despite an 80-basis-point increase in overall suburban vacancy to 13.8%. The East submarket's overall asking rent was once again the highest of the suburban submarkets, having increased \$0.35/SF from first-quarter 2018 to \$18.84/SF. The South's overall asking rent was down \$0.15/SF to \$15.94/SF from the prior quarter, while the Southwest's rental rate decreased \$0.46/SF to \$15.14/SF, and the West's rent increased by \$0.40/SF, the most this past quarter, to \$14.81/SF.

Although the East's vacancy rate increased slightly to 13.3%, it was still the second-tightest submarket in the area and was home to significant activity. The highly anticipated new, 66,000-square-foot Class A multi-tenant office building at the Van Aken District's mixed-use development, located at 20159 Van Aken Boulevard in Shaker Heights, delivered in the second quarter. Despite a scheduled third-quarter formal grand opening, law firm McGlinchey Stafford occupied its 18,000-square-foot lease, while ABA Insurance moved into 17,500 square feet, and Paragon Advisors occupied 6,320 square feet. After an increase of \$0.11/SF to \$23.31/SF, the East's Class A asking rent remained the highest in the entire market.

The West submarket netted the most negative absorption of the quarter at 31,096 square feet, prompting a 90-basis-point increase in vacancy to 15.9%. Nonetheless, as noted earlier, the West's overall asking rental rate increased, led by a \$0.14/SF increase in the average asking Class A rental rate to \$16.98/SF.

The South submarket, which netted the second-largest amount of negative absorption at 25,227 square feet, remained the tightest with an 11.3% vacancy rate. This marked a 40-basis-point increase in vacancy from the previous quarter. The South continues to attract businesses, as evidenced by insurer Medical Mutual leasing 324,539 square feet at the former American Greetings headquarters at 1 American Road/10601 Memphis Avenue. The company will consolidate its suburban operations at this space by early 2020. Already-established tenant Inogen also announced an approximately 50,000-square-foot expansion at this property. Additionally, Great Lakes NeuroTechnologies announced a planned move from Valley View to 6100 Rockside Woods in Independence, having leased 7,500 square feet there.

SELECT LEASE/USER TRANSACTIONS

Tenant	Building	Submarket	Type	Square Feet
Medical Mutual	1 American Rd./10601 Memphis	South	New	324,539
Inogen	1 American Rd./10601 Memphis	South	Expansion	~50,000
Cedar Brook Financial Partners	5885 Landerbrook Dr.	East	Renewal	15,812
Ports Petroleum Company, Inc.	1450 Firestone Pkwy.	Akron	Renewal	15,000
Kokosing Construction Company	4614 Prospect Ave.	CBD	New	14,700

SELECT SALE TRANSACTIONS

Building	Submarket	Sale Price	Price/SF	Square Feet
6225 Oak Tree Blvd.	South	\$4,775,000	\$115.22	41,442
7170 Chagrin Rd.	East	\$212,500	\$62.83	3,382
6175 SOM Center Rd.	East	\$975,000	\$48.75	20,000
2019 Center St.	CBD	\$1,700,000	\$31.48	54,000
925 Euclid Ave. + Annex	CBD	\$40,000,000	\$29.41	1,360,000

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 Average Asking Rent (Price/SF)
CBD Total	18,161,035	0	19.4%	(9,302)	220,387	\$22.03	\$18.35	\$18.90
East	7,915,107	305,000	13.3%	16,198	(71,275)	\$23.31	\$16.35	\$18.49
South	6,008,548	0	11.3%	(25,227)	(70,844)	\$20.60	\$14.08	\$15.94
Southwest	1,431,560	22,352	22.9%	(1,063)	(30,822)	\$18.00	\$13.20	\$15.14
West	3,196,955	0	15.9%	(31,096)	(39,559)	\$16.98	\$13.89	\$14.81
Suburban Total	18,552,170	327,352	13.8%	(41,188)	(212,500)	\$20.45	\$14.73	\$16.55
Market Total	36,713,205	327,352	16.6%	(50,490)	7,887	\$21.15	\$16.55	\$17.70

ECONOMIC CONDITIONS

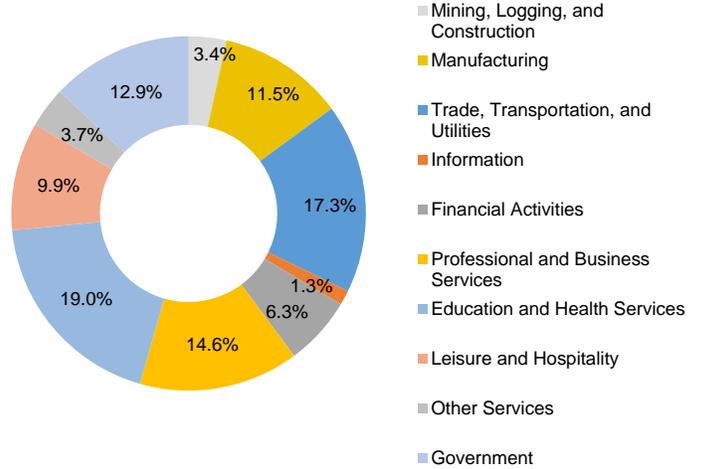
The Greater Cleveland economy continued to add more jobs throughout the first half of 2018, as total payroll employment grew in May by 1.3% year-over-year. Overall payroll employment for the United States also grew in May, by 1.6% year-over-year.

Most industry sectors saw growth from May 2017 to May 2018, including: mining, logging and construction (4.8% growth); manufacturing (4.1% growth); trade/transportation/utilities (2.8% growth); financial activities (0.5% growth); professional and business services (1.0% growth); education and health services (0.4% growth); and government (0.1% growth). Total nonfarm employment also saw an overall increase year-over-year by 1.3%. The information sector remained flat.

Conversely, the "other services" industry contracted the most, by 1.0%. The only other industry to report a negative change over the past year was the leisure and hospitality industry (negative 0.7%).

EMPLOYMENT BY INDUSTRY

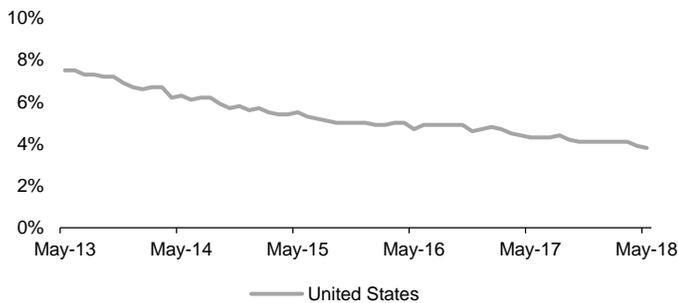
Cleveland-Elyria-Mentor



Source: U.S. Bureau of Labor Statistics

UNEMPLOYMENT RATE

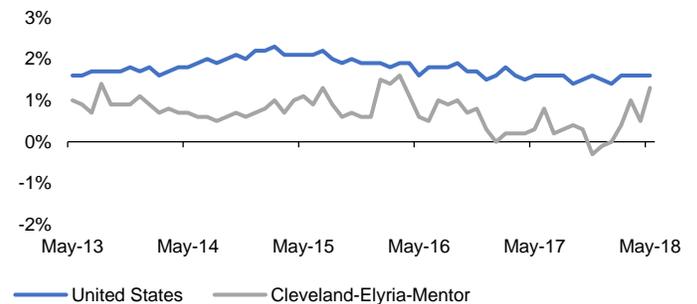
Seasonally Adjusted



Source: U.S. Bureau of Labor Statistics

PAYROLL EMPLOYMENT

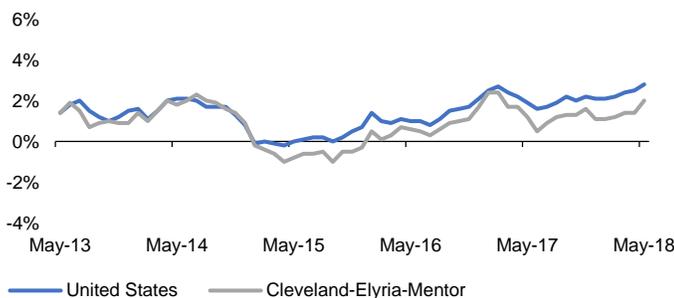
Total Nonfarm, Not Seasonally Adjusted, 12-Month % Change



Source: U.S. Bureau of Labor Statistics

CONSUMER PRICE INDEX (CPI)

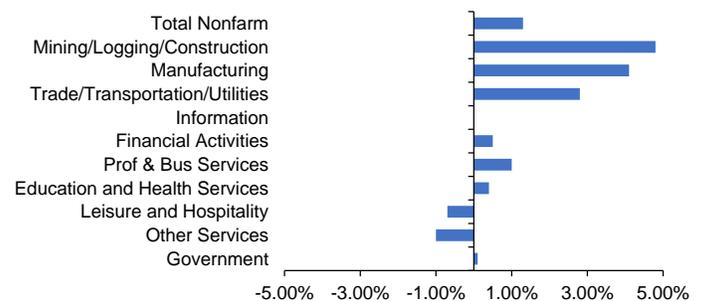
All Items, 12-Month % Change, Not Seasonally Adjusted



Source: U.S. Bureau of Labor Statistics

EMPLOYMENT GROWTH BY INDUSTRY

Cleveland-Elyria-Mentor, May 2018*, 12-Month % Change, Seasonally Adjusted



Source: U.S. Bureau of Labor Statistics (*preliminary)

