

Cleveland Office Market

Market Uneven as 2021 Begins, Though Signs Point to Guarded Optimism

Demand for space in the Greater Cleveland office market remained tepid as 2020 transitioned into the first quarter of 2021. After posting nearly 500,000 square feet of negative absorption in fourth-quarter 2020, the office market gave back space in first-quarter 2021 by posting 118,097 square feet of negative net absorption. This negative absorption increased the overall vacancy rate by 40 basis points from the previous quarter to 18.3% for all office properties.

Increased Rental Rates, ARP Indicate Potential

Despite challenges that continue to face commercial real estate in the wake of the pandemic, the average asking rental rate climbed back up across the Greater Cleveland office market, finishing the first quarter at \$18.33/SF for all classes, up \$0.18/SF from the last quarter. That development, along with the passage of the American Rescue Plan (ARP), indicate market potential. Provisions within the ARP that focus on vaccination and increased testing, along with support for mass transit and restaurants, all could help boost office reoccupation. This potential, contrasted with the negative absorption, shows the market's unevenness, though with signs leading to guarded optimism.

Current Conditions

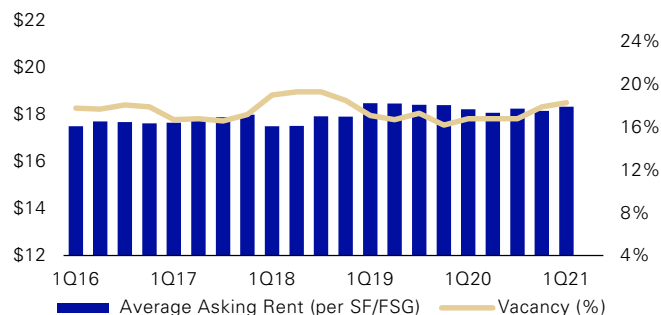
- The office market has experienced two straight and three out of the last four quarters of negative absorption.
- The vacancy rate increased by 40 basis points to 18.3%.
- The average asking rental rate rose by \$0.18/SF from the first quarter and is \$0.11/SF higher than one year ago.
- The CBD and the suburban submarkets performed relatively equally in the first quarter – especially in terms of negative net absorption and in Class A available sublease space.

Market Summary

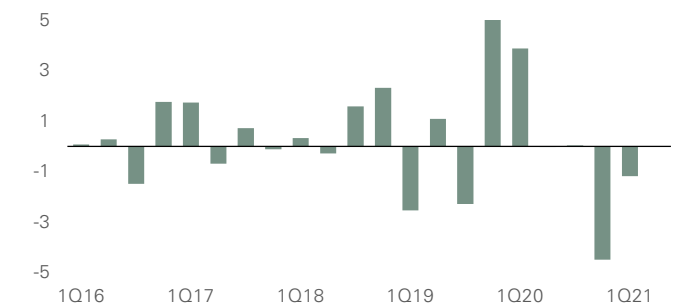
	Current Quarter	Prior Quarter	Year Ago Period	12-Month Forecast
Total Inventory (SF)	39M	39M	39M	→
Vacancy Rate	18.3%	17.9%	16.8%	→
Quarterly Net Absorption (SF)	(118,097)	(449,504)	388,084	→
Average Asking Rent/SF	\$18.33	\$18.15	\$18.22	↑
Under Construction (SF)	100,000	100,000	100,000	→

Market Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION (SF, Hundred Thousands)



RESEARCH Q1 2021

Looking back historically over the Cleveland office market's overall performance, first-quarter 2021's vacancy (18.3%) was within a half a percentage of what it was five years ago in first-quarter 2016 (17.8%), despite being the market's highest vacancy since fourth-quarter 2018's 18.5%. In between, despite a gradual vacancy dip in 2017 and a gradual uptick in 2018, the market has remained relatively steady from a vacancy standpoint over the past five years.

The Central Business District's overall asking rental rate increased by \$0.28/SF to \$19.38/SF during the first quarter, while its vacancy rate increased by 40 basis points to 20.5% due to 57,286 square feet of negative absorption. Of note was a \$0.53/SF increase in the CBD's Class A average asking rent to \$25.34/SF, the largest jump of any Class A rate. The CBD's Class B average asking rent decreased by \$0.07/SF to \$17.85/SF.

CBD and Suburbs Netted Similar Absorption

The CBD's 57,286 square feet of negative absorption was like the collective suburban submarkets, which tallied 60,811 square feet in negative net absorption in the first quarter, indicating a fairly even performance across the board amongst the submarkets. Despite relatively poor performance this past quarter, the suburban submarkets have a combined vacancy rate that remains lower than the CBD's rate; at 16.5%, the suburbs enjoyed a vacancy rate that was 4.0% lower than the CBD's, despite an increase of 30 basis points from the previous quarter. The average asking rental rate for the suburbs increased by \$0.10/SF to \$17.31/SF, still well below the CBD's \$19.38/SF.

Class A office space was dealt a setback in both the CBD and collective suburban submarkets in the first quarter. The CBD gave back 72,630 square feet in Class A negative net absorption, while the suburbs gave back 82,012 square feet. However, the CBD's Class A vacancy rate was 14.7% and the suburban Class A vacancy rate was 16.8%, both below the overall 18.3% vacancy.

CBD News

A central headline in the CBD once again involved paint and coating manufacturing company Sherwin-Williams. Just prior to the new year, the company was awarded \$70.0 million in loans from the Ohio Controlling Board to help finance the construction of its planned new 1.0-million-square-foot CBD headquarters and 500,000-square-foot R&D facility that will be located in Brecksville, in the South submarket. In February, the company released a preliminary HQ site plan and announced that it will break ground on both facilities by fourth-quarter 2021.

Other noteworthy news items in the CBD from the first quarter included: Cleveland City Council approving tax increment financing (TIF) for the \$13.0-million redevelopment of the 145,000-square-foot Western Reserve Building, located at 1468 West 9th Street; Cross Country Mortgage being awarded an

eight-year, 1.655% job creation tax credit by the Ohio Tax Credit Authority for its planned headquarters relocation and redevelopment of a six-acre block between East 21st and East 22nd streets from Superior Avenue to Payne Avenue; Minute Men Staffing Services announcing a 45,000-square-foot addition to its existing 38,066-square-foot headquarters, located at 3740 Carnegie Avenue; the Erieview District winning a listing on the National Register of Historic Places from the Ohio Historic Preservation Office (which will open up historic preservation financing options and more to the 30-plus buildings located within it); and iHeart Media Cleveland announcing an upcoming move of its regional offices and radio stations from the South submarket to approximately 10,000 square feet of the ground floor retail/office portion of the Residences at the 668 Euclid Avenue apartment building.

A noteworthy CBD building transfer that took place in the first quarter was the 452,419-square-foot 55 Public Square building. This strategically located, yet largely empty, asset transferred for \$14.0 million, or \$34/SF, to K&D Group, one of Northeast Ohio's largest privately-owned commercial and residential property management and development firms. The 22-story property has been in trouble for some time as its garage deteriorated, building improvements were placed on the backburner, prior sales fizzled, new leasing was paused and foreclosure fights persisted. K&D intends to proceed with an approximate \$80.0-million redevelopment of 55 Public Square into a mixed-use asset that includes over 150 apartments on the lower levels, office space on the upper levels and a new restaurant. The company plans to seek historic tax credits for the project.

Also in the CBD, as the quarter ended AML Rightsource, LLC announced it will move its headquarters from the 200 Public Square building to 1300 East 9th Street. The company signed a 50,371-square-foot lease and is expected to occupy space on the second and third floors by the fourth quarter of 2021. The company also announced that the Ohio Tax Credit Authority supported the project with a job creation tax credit that will assist in the move, as well as in the creation of up to 273 new jobs in the metropolitan Cleveland area by the end of 2024.

Suburban Submarkets

The South's overall asking rent was the only decrease for any submarket in the first quarter, by \$0.10/SF to \$17.01/SF from the prior quarter, while the Southwest's rental rate had the largest increase of any submarket, by \$0.71/SF to \$14.66/SF, though it stayed the lowest in the market. The West also experienced an increase in average asking rent, by \$0.26/SF to \$16.31/SF. Aside from the CBD, the largest positive shift in the Class A average asking rental rate took place in the West, where it increased by \$0.49/SF to \$19.89/SF. The overall suburban submarkets' Class A average asking rental rate increased by \$0.16/SF to \$20.95/SF.

RESEARCH Q1 2021

The East submarket's asking rent was once again the highest of the suburban submarkets and increased by \$0.21/SF from fourth-quarter 2020 to \$18.86/SF. Although the East's vacancy rate increased by 70 basis points to 14.1%, it was the tightest submarket in the area. Of the suburban submarkets, the East lost the most space in first-quarter 2021, having given back 43,459 square feet to begin the year.

In the East, the 42,800-square-foot Class A asset at 32125 Solon Road in Solon transferred to an investor group named Red Solon LLC, headed by real estate developer and salon owner Dino Palmieri for \$1.18 million, or \$27/SF. This was notable because as the first quarter ended, the building's tenant BDO was set to move to the CBD's 1300 East 9th Street, rendering the asset largely vacant. The East's vacancy is tighter than the rest of the market, and the new ownership group is confident that this building will gain back occupancy.

The West submarket netted 579 square feet of negative absorption, which kept the submarket's vacancy flat from the previous quarter at 16.6%. Of note in the West was the transfer of the Millennium Place East and West buildings. Located at 25111-25175 and 25209-25249 Country Club Boulevard, these two buildings measure a total of 140,400 square feet and sold to Grow Scale, a boutique real estate investment firm located in San Francisco, for \$11.0 million, or \$78/SF.

The South's vacancy rate dipped by 10 basis points from the last quarter to 18.2% as a result of 5,794 square feet of positive absorption and was the only submarket to yield in the positive. The first quarter's largest office sale, in terms of price per square foot, took place here as the 41,442-square-foot 6225 Oak Tree

Boulevard in Independence was purchased by Liberty Home Mortgage as its future headquarters for \$4.0 million, or \$97/SF.

The Southwest submarket's vacancy rate increased from the previous quarter to 22.7% due to 22,567 square feet in negative net absorption. This submarket's Class B average asking rental rate increased the most from last quarter, by \$0.87/SF to \$15.12/SF.

Sublease Space Still a Factor

The sublease market again reflected an ongoing tension between the possibility of more remote work and the need for more space per employee for those in the office due to physical distancing.

First-quarter 2021 saw the largest sublease vacancy percentage at 0.8% (tied with fourth-quarter 2020) since first-quarter 2013 (0.9%). In fact, sublet vacant space in first-quarter 2021 tallied 320,184 square feet, more than double that of one year ago (133,752 square feet) before COVID-19 took hold. As first-quarter 2021 ended, Class A available sublease space in the CBD totaled 224,715 square feet, while 224,008 square feet of Class A sublet space was available in the suburban submarkets, another demonstration of the parity between the CBD and the suburbs in first-quarter 2021.

Ultimately, the sublease conundrum for office tenants is how to control occupancy costs during a period of economic dislocation, while also retaining the space needed to implement a new workplace strategy. With effective vaccines slowly rolling out, that point might not be too far away, but with such little movement in the past year, it's hard to imagine an uptick in absorption until the pandemic is fully dealt with.

Select Lease/User Transactions

Tenant	Building/Address	Submarket	Type	Square Feet
AML Rightsource, LLC	1300 East 9th St.	CBD	New	50,371
Checkpoint Surgical	6050 Oak Tree Blvd.	South	New	13,721
iHeart Media	668 Euclid Ave.	CBD	New	10,000
Stout Risius Ross, LLC	1300 East 9th St.	CBD	New	7,044
Vecmar Computer Solutions	1500 W. Third St.	CBD	New	5,000

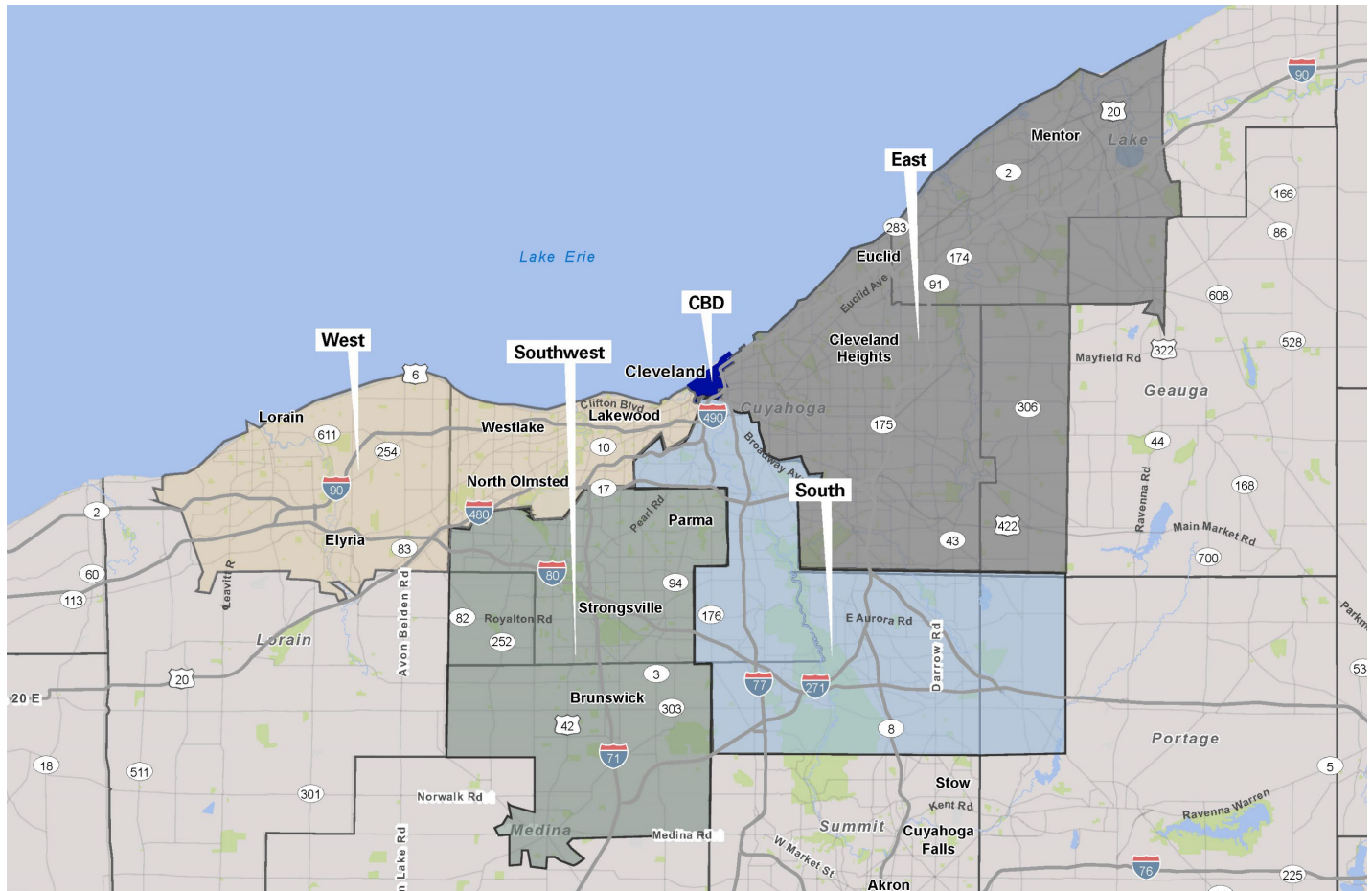
Select Sale Transactions

Building/Address	Submarket	Sale Price	Price/SF	Square Feet
6225 Oak Tree Blvd.	South	\$4,000,000	\$96.52	41,442
25111-25175 & 25209-25249 Country Club Blvd.	West	\$11,055,000	\$77.74	140,400
26600 Renaissance Pkwy.	East	\$695,000	\$55.60	12,500
55 Public Square	CBD	\$14,000,000	\$30.94	452,419
32125 Solon Rd.	East	\$1,175,000	\$27.00	42,800

Submarket Statistics

	Total Inventory (SF)	Under Construction (SF)	Total Vacancy Rate	Quarter 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	17,949,109	0	20.5%	(57,286)	(57,286)	\$25.34	\$17.85	\$19.38
East	8,734,517	0	14.1%	(43,459)	(43,459)	\$23.15	\$16.23	\$18.86
South	7,408,056	0	18.2%	5,794	5,794	\$20.22	\$15.13	\$17.01
Southwest	1,344,084	0	22.7%	(22,567)	(22,567)	\$14.75	\$15.12	\$14.66
West	3,587,003	100,000	16.6%	(579)	(579)	\$19.89	\$13.36	\$16.31
Suburban Total	21,073,660	100,000	16.5%	(60,811)	(60,811)	\$20.95	\$15.31	\$17.31
Market Total	39,022,769	100,000	18.3%	(118,097)	(118,097)	\$22.66	\$16.65	\$18.33

Cleveland Office Submarkets



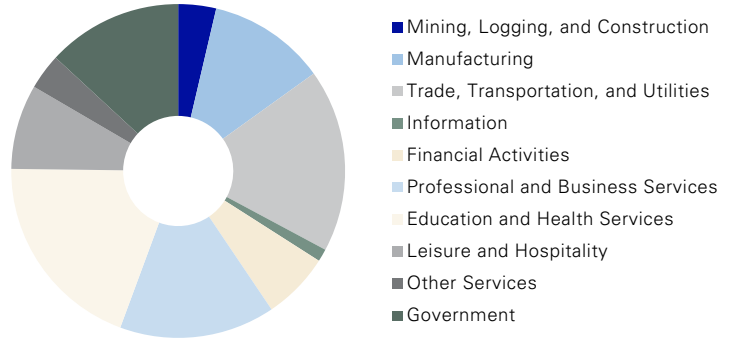
Economic Conditions

The Greater Cleveland economy lost a significant number of jobs early in first-quarter 2021, as total payroll employment declined in January by 7.5% year over year. The national total payroll employment number was also down, by 6.1% year over year.

Only one industry sector saw employment growth from January 2020 to January 2021: financial activities, at positive 0.8%. All other sectors saw a drop in the past year. The leisure and hospitality industry contracted the most, by negative 18.6%; followed by other services at negative 15.2%; manufacturing at negative 9.7%; the information sector at negative 7.6%; professional and business services at negative 7.5%; government at negative 7.1%; education and health services at negative 6.4%; trade/transportation/utilities at negative 3.7%; and mining/logging/construction at negative 2.5%.

Employment By Industry

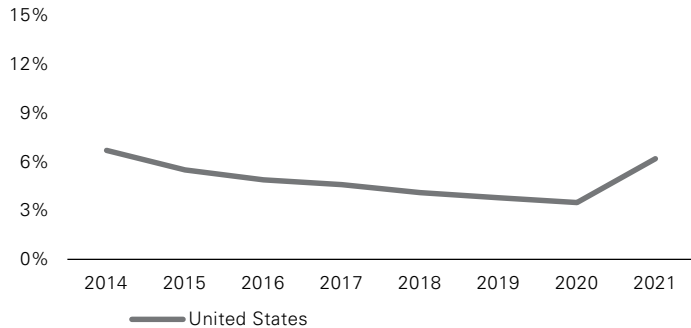
CLEVELAND-ELYRIA-MENTOR



Source: U.S. Bureau of Labor Statistics

Unemployment Rate

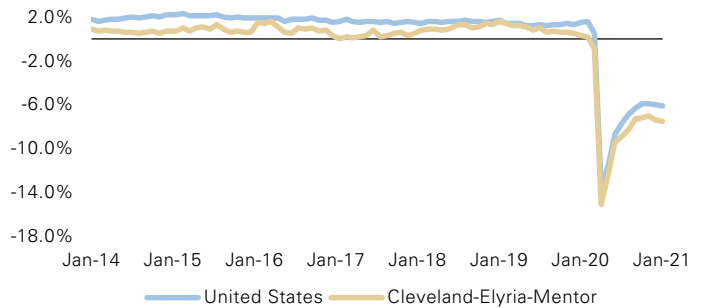
SEASONALLY ADJUSTED



Source: Source: U.S. Bureau of Labor Statistics

Payroll Employment

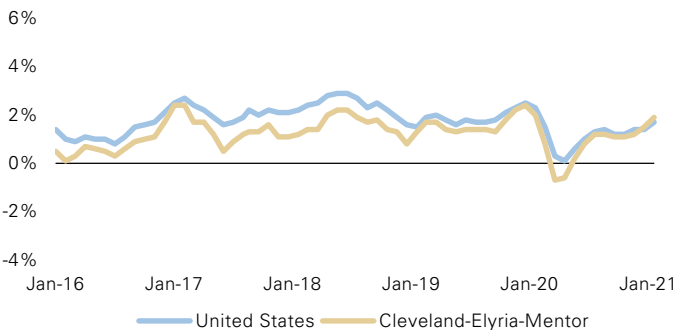
TOTAL NONFARM, NOT SEASONALLY ADJUSTED, 12-MONTH % CHANGE



Source: Source: U.S. Bureau of Labor Statistics

Consumer Price Index (CPI)

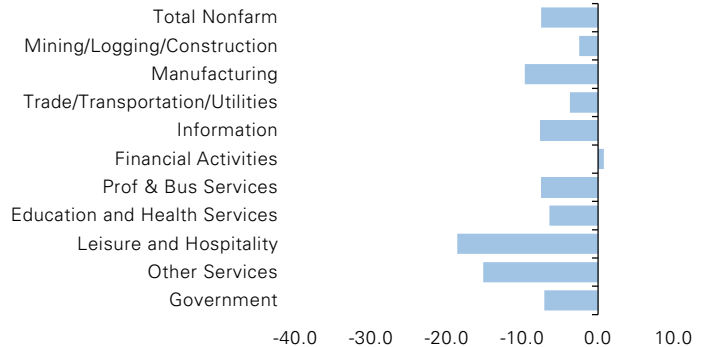
ALL ITEMS, 12-MONTH % CHANGE, NOT SEASONALLY ADJUSTED



Source: Source: U.S. Bureau of Labor Statistics

Employment Growth By Industry

CLEVELAND-ELYRIA-MENTOR, JANUARY 2021, 12-MONTH % CHANGE, SEASONALLY ADJUSTED



Source: Source: U.S. Bureau of Labor Statistics

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