

Cleveland Office Market

Workers Began Office Return, Yet Tepid Demand Inhibited Market Progress

Conditions in the Greater Cleveland office market were uninspiring during the second quarter of 2021, precipitated by 365,916 square feet of negative net absorption. Total absorption remained in negative territory for the year, with an overall loss of 502,948 square feet from the first two quarters of 2021.

The negative absorption increased the market's vacancy rate for the third quarter in a row, and by 90 basis points this past quarter, to 19.3% for all office properties. The continued specter of the COVID-19 pandemic is one reason that space has continued to come back to the market. Office space demand over the last several quarters has been lukewarm, and lease occupations from leases signed in recent months didn't outweigh the loss of space. In fact, overall market vacancy is up 2.5%, or 250 basis points, from one year ago.

The overall average asking rental rate dropped by \$0.19/SF to \$18.15/SF for all classes, though it is up \$0.08/SF since second-quarter 2020. A silver lining was that the overall average asking rental rate has stayed above \$18.00/SF for the last 10 quarters.

The overall Class A average asking rental rate of \$22.15/SF represented a decrease of \$0.45/SF from the first quarter, while the Class B average asking rental rate dipped by \$0.05/SF to \$16.36/SF.

Current Conditions

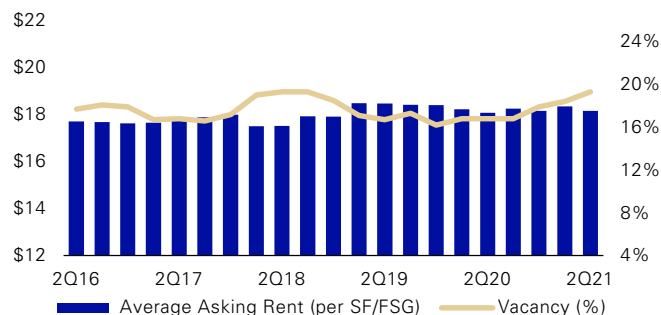
- The office market has experienced three straight and four out of the last five quarters of negative absorption – and it has lost over half a million square feet in negative absorption so far this year.
- The vacancy rate increased by 90 basis points to 19.3%.
- The average asking rental rate decreased by \$0.19/SF from the first quarter and is \$0.08/SF higher than one year ago.
- Office redevelopment projects in the CBD dotted the headlines.
- Class B “zombie” space continued to impact the perception of vacant space in the CBD.

Market Summary

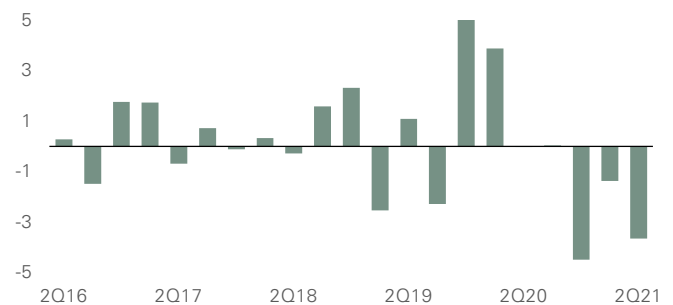
| | Current Quarter | Prior Quarter | Year Ago Period | 12-Month Forecast |
|-------------------------------|-----------------|---------------|-----------------|-------------------|
| Total Inventory (SF) | 39M | 39M | 39M | → |
| Vacancy Rate | 19.3% | 18.4% | 16.8% | → |
| Quarterly Net Absorption (SF) | (365,916) | (137,032) | (3,044) | → |
| Average Asking Rent/SF | \$18.15 | \$18.34 | \$18.07 | → |
| Under Construction (SF) | 145,000 | 100,000 | 100,000 | ↑ |
| Deliveries (SF) | 0 | 0 | 0 | ↑ |

Market Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION (SF, Hundred Thousands)



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Workers slowly began to reoccupy office space throughout the Cleveland market in the second quarter, but overall demand for new space did not return to the momentum of fourth-quarter 2019 and first-quarter 2020, where the combined positive absorption for those two quarters was 904,328 square feet.

There is optimism that the Cleveland office market will begin to trend towards its pre-pandemic upswing, though the timing is still uncertain as occupiers and tenants in the market face tough leasing decisions. Additionally, the State of Ohio recently moved up to number 7 in *Chief Executive* magazine's Best & Worst States for Business. With Ohio's tax incentive climate, as well as the pro-business attitude of many cities and suburbs, this provides additional positivity for companies to consider the state for expansion or relocation.

CBD News

The Central Business District led the market in negative net absorption for two consecutive quarters, as this submarket gave back 311,168 square feet in the second quarter, bringing the total space returned so far this year to 368,454 square feet. The occupancy loss caused the CBD's vacancy rate to increase by 170 basis points to 22.2%, the second highest in the market.

The Cleveland CBD is still a desirable location for prominent local, regional and national companies as they weigh space options coming out of the pandemic. For example, law firm McCarthy, Lebit, Crystal & Liffman Co., L.P.A. signed a 26,678-square-foot lease to relocate by the end of summer to 1111 Superior Avenue from the Midland Building in the Landmark Office Towers complex located at 101 West Prospect Avenue.

Also in the CBD, Cleveland gaming company Jack Entertainment signed a 15,000-square-foot, two-floor lease in the iconic Terminal Tower, located at 50 Public Square, while documentary film company Transition Studios leased 8,754 square feet in Playhouse Square's Idea Center, located at 1375 Euclid Avenue.

The overall asking rent in the CBD decreased by \$0.36/SF to \$19.02/SF, as the submarket remained the highest average in the market. Both the Class A and the Class B asking rents in the CBD dipped, the Class A by \$0.52/SF and the Class B by \$0.23/SF.

Perhaps the most enduring theme of the second quarter was redevelopment. News of several such projects in the CBD came out involving several prominent office buildings. One example is the 1.4 million-square-foot Centennial, a \$460.0-million reimagining of the former Union Trust/Huntington Building at 925 Euclid Avenue. The project received a 20-year \$5.0-million loan from Cuyahoga County Council in April to complement already-approved aid from the City of Cleveland and \$25 million in state historic tax credits. Owner/developer The Millennia Companies is also expected to seek funds from the Ohio Development Services Agency's new transformational mixed-use development (TMUD) program, which was signed into law at the end of 2020.

Another newsworthy project in the second quarter was the \$59.2-million 55 Public Square redevelopment. Owners K&D Group purchased the office tower in the first quarter and have begun work on the building's attached parking garage. The project will also include interior and exterior repairs facelifts, the opening of the long-closed, attached 10,000-square-foot restaurant space (and include a new rooftop deck) and the repurposing of several of the 22 floors to over 200 apartments. Seven floors (floors 16-22) of renovated office space are likely to remain. On June 30th, the Ohio Development Services Agency awarded the project \$5 million in competitive state tax credits.

In the Historic Warehouse District, a similar redevelopment aims to start construction this summer at the Rockefeller Building, located at 614 West Superior Avenue. In late-April, the Cleveland Landmarks Commission approved renovation plans that call for 436 apartments on floors 4-16. Approximately 28,000 square feet of office is due to remain on the second and third floors.

In the CBD's Superior Arts District, Cross Country Mortgage held a groundbreaking ceremony for its new 168,000-square-foot headquarters campus at 2152-2160 Superior Avenue. The project includes the restoration, renovation and conversion of four industrial buildings dating back to 1913. The company expects construction to be completed by the end of the year. Less than a mile east in the MidTown/AsiaTown community, phase 1 of the 45,000-square-foot Culture33 redevelopment was underway. The project is a repurposing of the former Dave's Supermarket property at 3301 Payne Avenue into an office/commercial complex that is due to deliver in third-quarter 2021.

Zombie Space Factors Into Class B Vacancy

Four properties impact the perception of vacant space in the CBD. These properties, termed 'zombie properties,' have large blocks of vacant space that are not actively marketed to the office community or are in limbo pending building redevelopment. These properties include buildings that are awaiting conversion from office to residential or hotel (or a mix), or are being marketed for sale. The Higbee Building has space that is not being marketed because of a likely expansion by the owner, Bedrock, which occupies a lot of space in the building already.

The CBD's current Class B zombie properties include: Tower at Erieview/1301 East 9th Street; 45 Erieview Plaza; Higbee Building/100 Public Square; and 1801 Superior Avenue/former Plain Dealer building. Zombie space adversely impacts the vacancy rate of the Class B CBD market. The Class B CBD market has 28.76% vacancy. When the zombie properties are removed from the inventory survey, the vacancy rate declines to 24.58%, a drop of 4.18 percentage points. The amount of vacant and available space in the CBD is currently overstated when the zombie properties are included.

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Suburban Submarkets

The East submarket's vacancy rate increased by 170 basis points to 15.5% this past quarter, which tied with the CBD for the largest jump in vacancy, despite remaining the tightest submarket in the area. Rental rates remained stable in the East at \$18.91/SF, up \$0.05/SF from the previous quarter. The Class B asking rental rate did well and helped pace the overall rate in the submarket as it stood at \$16.72/SF, up by \$0.49/SF. The Class A rate dipped by \$0.29/SF to \$22.86/SF. The overall Class A and Class B asking rental rates in the East still all remained second in the market behind the CBD. Absorption-wise, the East gave up the second most amount of space, with 147,564 square feet of negative absorption. Year-to-date, the East has accumulated 191,023 square feet in the negative.

A noteworthy development in the East was the two-building portfolio sale of 6085 and 6095 Parkland Boulevard, known as Eastpoint I and II, in Mayfield Heights. The Class A buildings, which make up a total of 172,788 square feet, sold from Founders Properties LLC to an affiliate of Realife Real Estate Group for \$16.5 million, or \$95.49/SF.

The suburban office submarkets as a whole saw a vacancy increase of 30 basis points from last quarter to 16.9%. The overall average asking rental rate for the suburban submarkets decreased \$0.04/SF to \$17.29/SF. The suburban submarket with the highest overall asking rent was the East. The South's overall asking rent was up \$0.05/SF to \$17.11/SF from the prior quarter, while the West's rent decreased \$0.82/SF to \$15.49/SF, the largest decrease not only in the suburbs but the entire office market. The lowest rental rate in the market came in the Southwest, which had an increase of \$0.02/SF to \$14.68/SF.

The West submarket netted 5,981 square feet of positive

absorption, which led to a 10-basis-point decrease in vacancy to 16.5%. Of note in the West was the Class A average asking rental rate dropping by \$1.75/SF to \$18.14/SF, a decrease that led all submarkets and classes.

The South gained the most space of any suburban submarket in the second quarter, with 95,737 square feet of positive absorption, which prompted a 120-basis-point decrease in vacancy to 17.2%. Through the first two quarters, the South has accrued the most space of all the suburban submarkets, 82,596 square feet in positive absorption. The South also had a \$0.17/SF increase in the average asking Class A rental rate to \$20.44/SF.

News of note in the South was the announcement that professional services firm CBIZ intends to occupy approximately 50,000 square feet of a proposed 125,000-square-foot Welty Development Class A office project on Rockside Woods Boulevard in Independence. Welty plans to break ground in third-quarter 2021, with completion scheduled for the fall of 2022. MAI Capital Management announced a move from the CBD to Independence in April and is expected to relocate to CBIZ's current 57,371-square-foot suite at Park Center Plaza III, 6050 Oak Tree Boulevard, by the middle of 2022. MAI, a wealth management firm, was granted an eight-year, 1.77% Job Creation Tax Credit by the Ohio Tax Credit Authority in April.

Also in the South submarket, Premier Development Partners received approval from the Broadview Heights Planning Commission and City Council to build a two-story, 42,000-square-foot office building, to be known as "Property Two Building" on Town Centre Drive, adjacent to "Property One Building." The construction start date is currently unknown, as the ownership group has indicated that tenant lease commitments would be the catalyst to jumpstart the development.

Select Lease/User Transactions

| Tenant | Building/Address | Submarket | Type | Square Feet |
|--|--|-----------|-----------|-------------|
| CBIZ | Welty Development/Rockside Woods Blvd. | South | New | ~50,000 |
| McCarthy, Lebit, Crystal & Liffman Co., L.P.A. | 1111 Superior Ave. | CBD | New | 26,678 |
| Aerotek, Inc. | 6200 Oak Tree Blvd. | South | New | 19,910 |
| JACK Entertainment | 50 Public Square | CBD | New | 15,000 |
| Avantia, Inc. | 9525-9655 Sweet Valley Dr. | South | Extension | 9,789 |

Select Sale Transactions

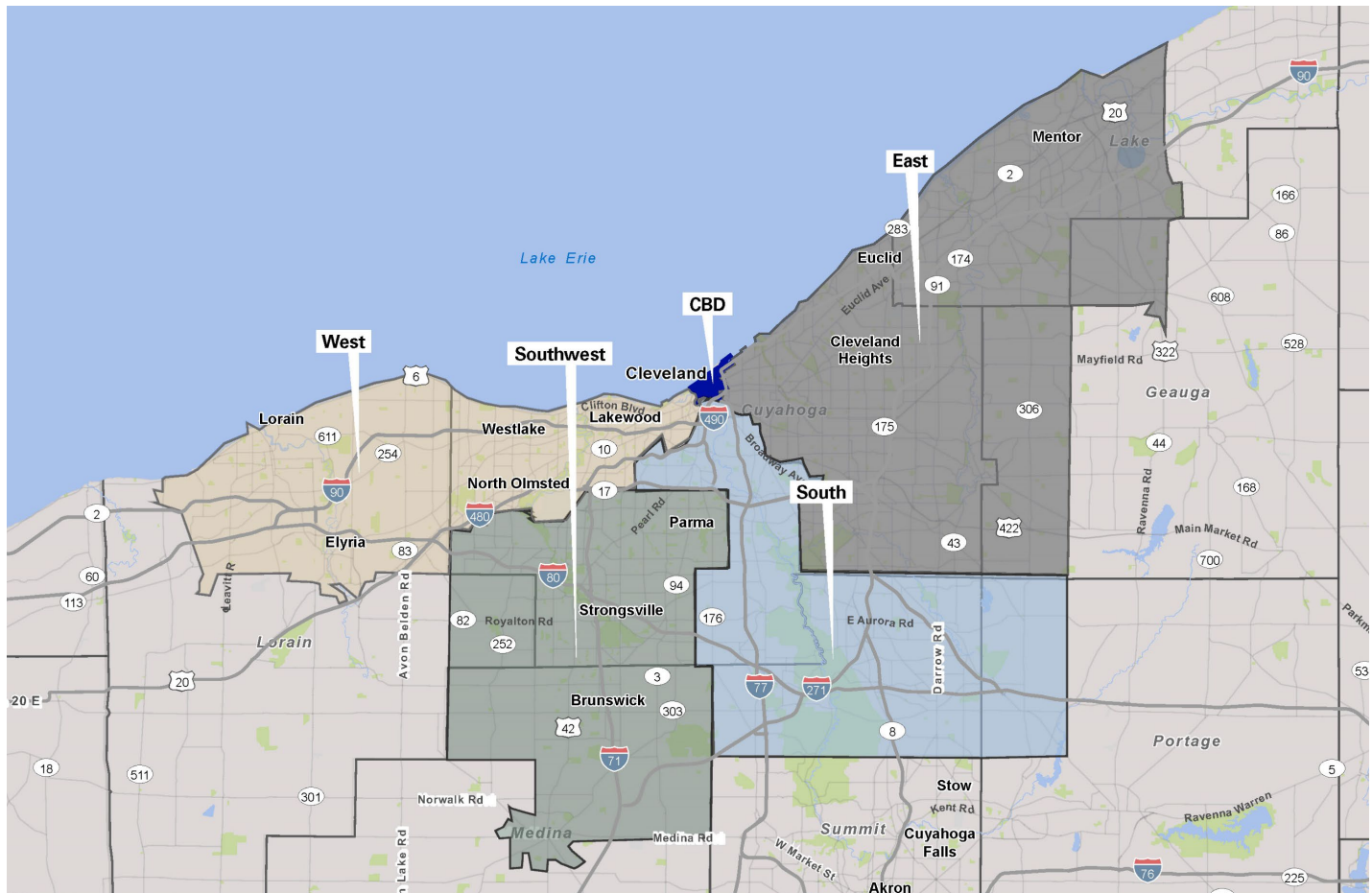
| Building/Address | Submarket | Sale Price | Price/SF | Square Feet |
|--|-----------|--------------|----------|-------------|
| 2603 Riverside Dr. | East | \$1,992,857 | \$172.96 | 11,522 |
| 6085 & 6095 Parkland Blvd. (two bldg. portfolio) | East | \$16,500,000 | \$95.49 | 172,788 |
| 6830 Cochran Rd. | East | \$1,300,000 | \$77.27 | 16,825 |
| 3404 Lorain | West | \$435,000 | \$71.92 | 6,048 |
| 100 Executive Pkwy. | South | \$3,210,000 | \$68.48 | 46,875 |

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The Southwest submarket's aforementioned average asking rental rate increase came, despite 8,902 square feet of negative net absorption. The vacancy rate in the Southwest increased 60 basis points to 23.3%. The Southwest continued to post the highest vacancy rate and the lowest average asking rental rate of the suburban office submarkets.

| 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 | 45,000 | 22.2% | (311,168) | (368,454) | \$24.27 | \$17.26 | \$19.02 |
| East | 8,734,517 | 0 | 15.8% | (147,564) | (191,023) | \$22.86 | \$16.72 | \$18.91 |
| South | 7,408,056 | 0 | 17.2% | 95,737 | 82,596 | \$20.44 | \$14.85 | \$17.11 |
| Southwest | 1,344,084 | 0 | 23.3% | (8,902) | (31,469) | \$14.75 | \$15.08 | \$14.68 |
| West | 3,587,003 | 100,000 | 16.5% | 5,981 | 5,402 | \$18.14 | \$13.39 | \$15.49 |
| Suburban Total | 21,073,660 | 100,000 | 16.9% | (54,748) | (134,494) | \$20.58 | \$15.42 | \$17.29 |
| Market Total | 39,022,769 | 145,000 | 19.3% | (365,916) | (502,948) | \$22.15 | \$16.36 | \$18.15 |

Cleveland Office Submarkets



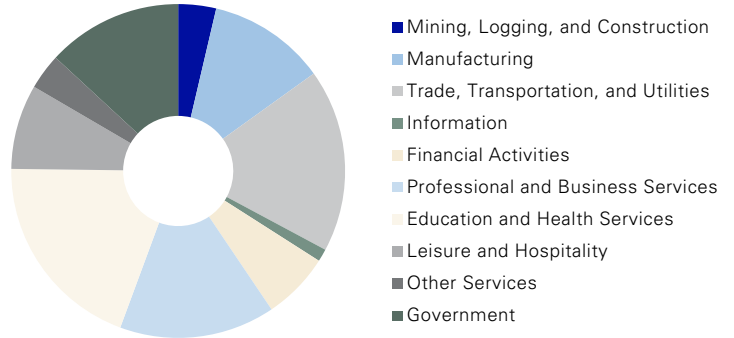
Economic Conditions

The Greater Cleveland economy gained back a number of jobs in second-quarter 2021, as total payroll employment increased in May by 6.2% year over year. The national total payroll employment number was also up, by 9.0% year over year.

Only one industry sector saw employment loss, according to preliminary numbers from the Bureau of Labor Statistics from May 2020 to May 2021: government, at negative 0.5%. All other sectors saw an increase from the past year. The leisure and hospitality industry gained the most, by 43.0%; followed by other services at 14.6%; the information sector at 7.0%; mining/logging/construction at 6.9%; professional and business services at 6.0%; trade/transportation/utilities at 4.3%; financial activities at 3.9%; education and health services at 3.4%; and manufacturing at 0.5%.

Employment By Industry

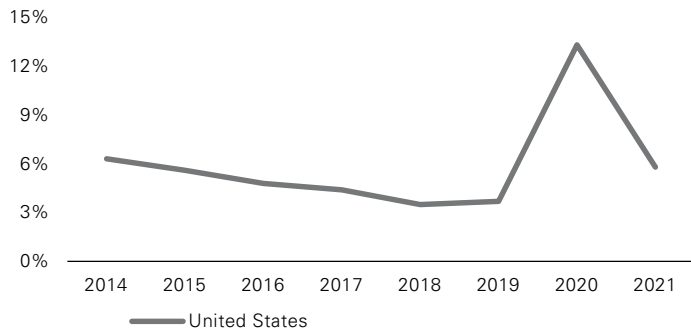
CLEVELAND-ELYRIA-MENTOR



Source: U.S. Bureau of Labor Statistics

Unemployment Rate

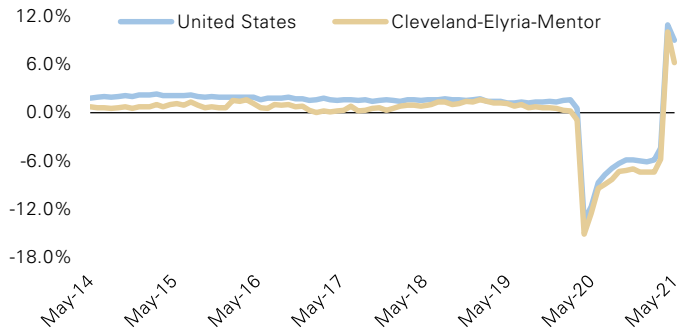
SEASONALLY ADJUSTED



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

Payroll Employment

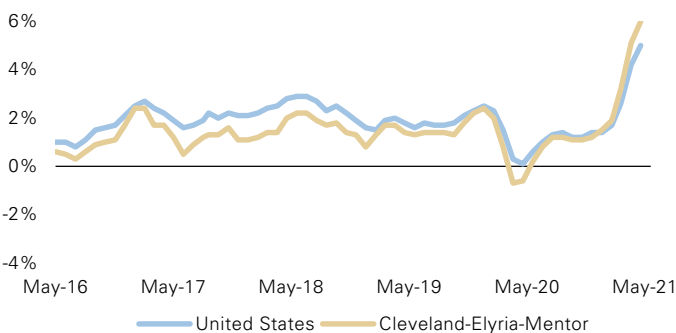
TOTAL NONFARM, NOT SEASONALLY ADJUSTED, 12-MONTH % CHANGE



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

Consumer Price Index (CPI)

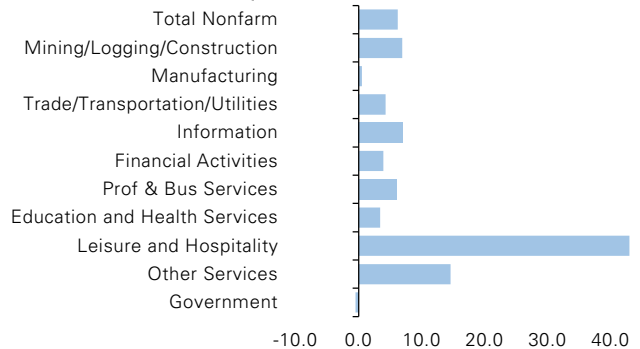
ALL ITEMS, 12-MONTH % CHANGE, NOT SEASONALLY ADJUSTED



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

Employment Growth By Industry

CLEVELAND-ELYRIA-MENTOR, MAY 2021 (preliminary), 12-MONTH % CHANGE, SEASONALLY ADJUSTED



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

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