Office Insight

Atlanta | Q1 2014

Consistent demand for quality space forces tenants to commit or consider other alternatives

Economy

The local job market has seen a marked improvement when compared to this time a year ago and considerably so when compared to unemployment highs immediately following the recession. February's unemployment rate was 6.9 percent, 1.4 percentage point lower than in February 2013 and 3.8 points lower than the post-recession high. We anticipate growth in the commercial construction sector will continue adding to the metro's employment base. The Falcons and Braves stadiums, a myriad of new multifamily developments, and select industrial and office builds will work to plane out any uneven growth seen in the area's supply of new single-family construction. Improvements in consumer confidence, solid retail spending data, low interest rates and the return of spring are encouraging for metro Atlanta's economy.

Market conditions

First quarter market activity underscores further tightening of office real estate fundamentals. Driven primarily by the improving jobs situation and limited threat of new competing development, metro vacancy rates have been allowed to drop for 10 quarters in a row. At 19.7-percent the metro vacancy rate is 1.2 points lower than a year ago. Additionally, first quarter absorption exceeded 1.1 million square feet following a period of brisk leasing activity in the 50,000-to-100,000-square-foot segment. Class A buildings in the Central Perimeter and Northwest submarkets benefited from the demand. State Farm, Career Sports & Entertainment, and Allscripts account for a few of the move-in's over the quarter.

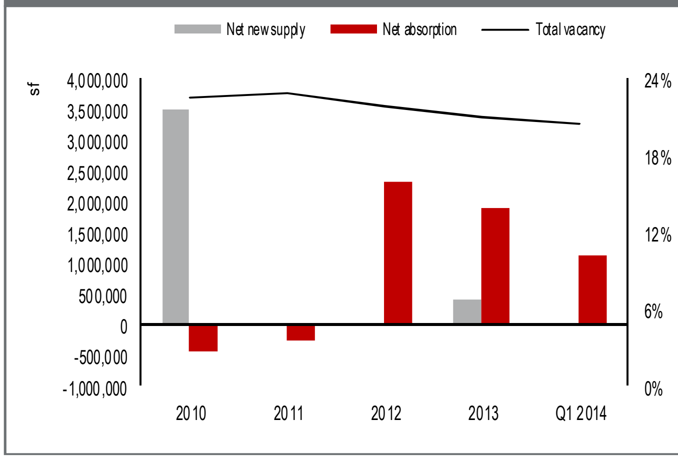
All this positive momentum in a supply constrained market acts to shift negotiating position to the landlord's favor, specifically in well-located quality buildings. Blocks of Class A office space in the Central Perimeter, North Fulton, and Buckhead submarkets are disappearing - as are concession packages. Tenants with requirements for office space in northern submarkets, which total 4.8 million square feet and account for 63.3 percent of all known interest, are increasingly being forced to commit. Otherwise, options are limited to alternate areas or building quality, or renewing in place.

Outlook

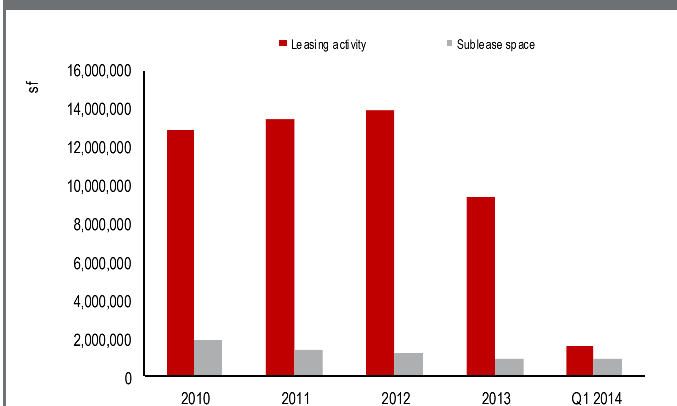
Assuming tenant demand remains robust, and there is little evidence to suspect otherwise, Class A vacancy rates will continue to compress metrowide. We expect this to be the trend until new speculative multi-tenanted office space is delivered. Additionally, Class B product beyond the most active micromarkets, will begin to tighten as tenants are edged out of higher-quality options. Midtown, Downtown and the Northeast will begin to see a decline in space availability later in the year. Look to health in the professional business services sector for short-term movement. Occupiers related to the financial and construction sectors will be increasingly active long-term.

Key market indicators		12-month forecast	
Supply	Supply	→	133,276,012 sf
	Direct vacancy rate	↓	19.7%
	Total vacancy rate	↓	20.4%
	Under construction (% preleased)	↑	830,938 sf (55.0%)
Demand	Leasing activity 12 mo. % change	↑	-33.0%
	YTD net absorption	→	1,117,665 sf
Pricing	12-month overall rent % change	↑	0.5%
	Class A overall asking rent	↑	$22.45 psf
	Class B overall asking rent	↑	$16.37 psf

Net new supply, net absorption and total vacancy



Leasing activity vs. sublease vacant space



Sublease space only includes vacant space

Tenant perspective

After many years in which leverage across the market remained firmly in the tenant's favor, bargaining conditions have begun to moderate within certain Atlanta submarkets. Large block availabilities have dissipated in Central Perimeter, North Fulton, and Buckhead, where leasing velocity has been brisk. Midtown has also started to see the vacancy rate falling off as employers add back jobs or relocate to the city's Urban core. Average concessions in these submarkets have begun to dip and effective rental rates incrementally rise.

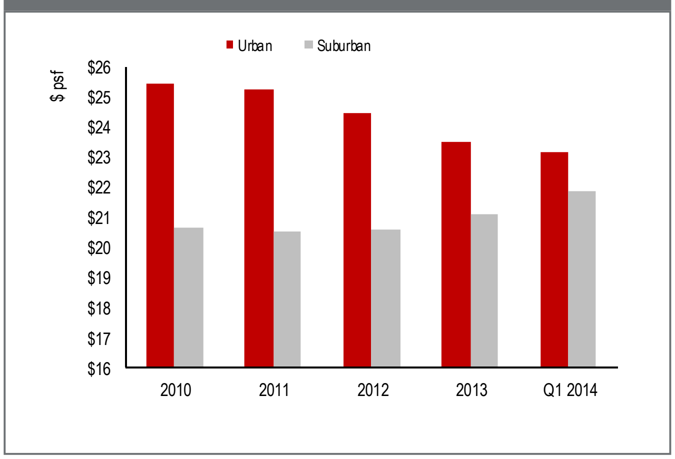
Outside of these areas, conditions throughout the rest of Atlanta are still relatively tenant-friendly. This is particularly true for Class B and vintage Class A buildings. Many of those assets experienced broad occupancy losses as tenants traded up with respect to quality in the years since the recession.

Landlord perspective

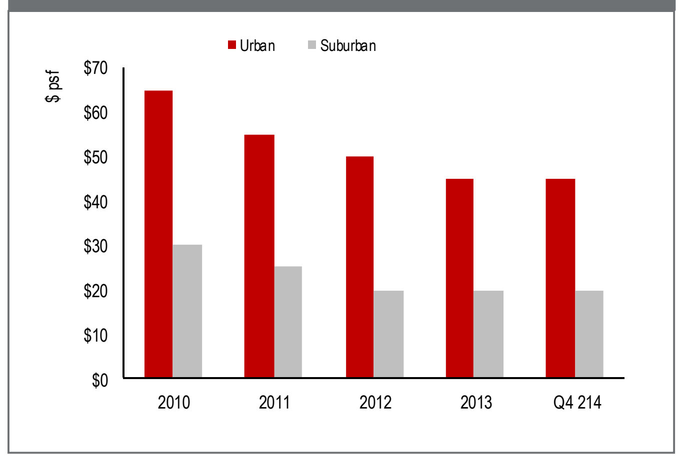
At a micro level, owners in the geographies with burgeoning demand have already begun to capitalize on the tightening conditions. We have seen owners ease the pedal on tenant improvement allowances and deals done in the same building are now not as steeply discounted as they were just 12 to 18 months ago.

Asking prices, however, are still somewhat flat across less active geographies. Once landlords do become comfortable enough with the level of demand to increase asking prices, rents are not likely to jump significantly. Historically, average Atlanta rates have ranged by just a few dollars given the bullish attitude toward speculative development here. There are low barriers of entry to build that historically have resulted in increasing inventory.

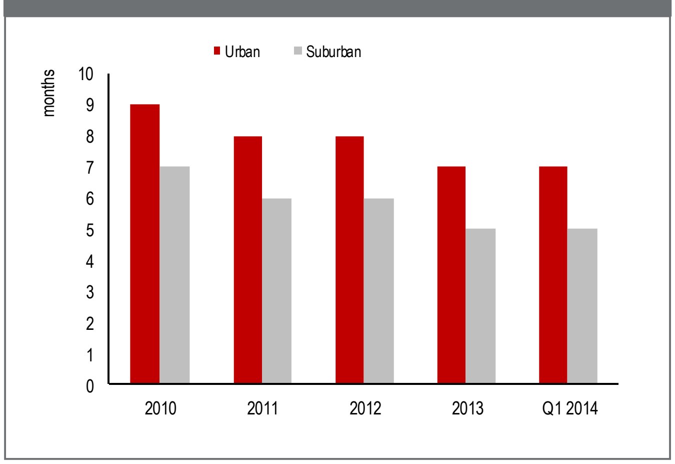
Class A overall asking rents



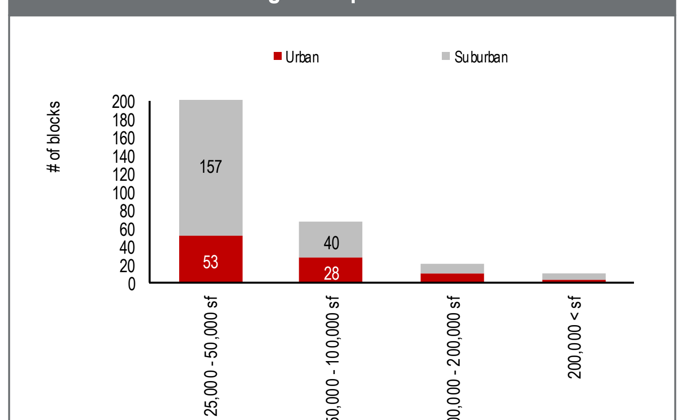
Class A tenant improvement allowances



Class A free rent

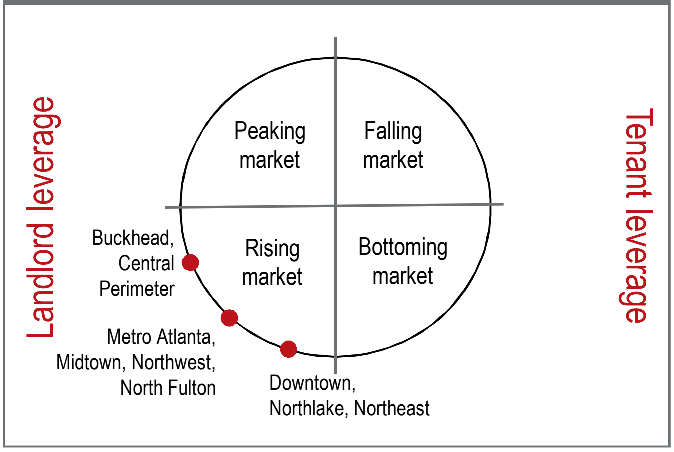


Class A blocks of contiguous space

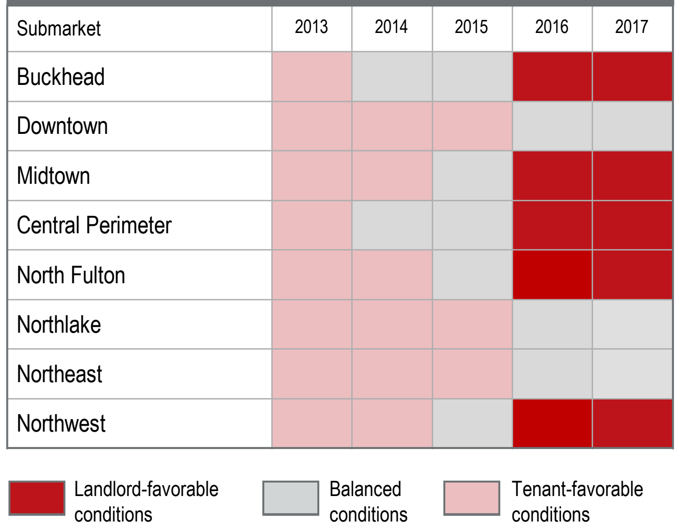


Includes available existing and UC/UR blocks contiguous within one floor

Property clock – current market conditions



Submarket leverage – market history and forecast



2013/2014 Completed lease transactions

Tenant	Address	Submarket	SF	Type
Fiserv	Cobalt Center	North Fulton	376,000	Relocation
The Coca-Cola Company	SunTrust Plaza	Downtown	276,000	Relocation
Georgia Power	2500 Patrick Henry Parkway	South Atlanta	112,000	Renewal
MailChimp	Ponce City Market	Midtown	110,000	Relocation
Allstate	Wildwood Plaza	Northwest	100,000	Relocation
PulteGroup	Capital City Plaza	Buckhead	100,000	New
Frazier & Deeter	Promenade	Midtown	96,000	Relocation
Spanx	Buckhead Atlanta	Buckhead	90,000	Relocation
Koch Industries	100 Peachtree	Downtown	82,000	Relocation
Emory Continuing Education	12 Executive Park	Northlake	75,000	Relocation

2013/2014 Completed sale transactions

Address	Submarket	Buyer / Seller	SF	$ psf	Comments
The Terraces	Central Perimeter	MetLife / Royal Bank of Scotland	1,016,685	$187	Foreclosure
Ravinia Center	Central Perimeter	CBRE Global Invest / Colonial Property	813,000	$177	Investment
Northlake Office Park	Northlake	Boxer Properties / Hudson Advisors	716,000	$29	11 Buildings
Wildwood	Northwest	GC Essential Asset / Columbia Property	697,000	$141	11 Buildings
Glenlake Towers	Central Perimeter	Highwoods Properties/ Dreilander Funds	505,000	$158	Value-add
The Plaza	Buckhead	Lone Star Funds / CW Capital	400,000	$170	Foreclosure
Primerica HQ	Northeast	CCIT / Duke Realty	365,000	$167	Single tenant
Perimeter Central Square	Central Perimeter	Crown Holdings Group / Pilgrams Pride	262,340	$68	Redevelopment

Atlanta methodology: Inventory includes all Class A & B office properties greater than 15,000 square feet, and excludes all office condo, medical, government and owner-occupied buildings

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