Office Insight

Orlando | Q1 2014

Rising asking rates in key submarkets signal a shift in landlords' office outlook

Economy

After finishing strong in 2013, Orlando's local economy is carrying that momentum into 2014. Although total employment remains lower than the December level, this is most likely due to seasonal factors related to the area's labor market. Looking at employment from an annual perspective, we can get a clearer picture of the trend in the labor market. As of February 2014, total nonfarm payrolls stood at 1.088 million, corresponding to a 3.6 percent annual increase and roughly 34,000 jobs added over the year. A resurgence in construction activity related to broader economic improvements has been a key driver of growth in the Orlando area. As of February 2014, construction employment posted the highest annual growth rate among the different labor sectors, increasing employment by 10.4 percent or 5,000 jobs compared to a year ago. Furthermore, office-using sectors have shown significant improvement as well during the first quarter. Professional and business services employment stood at 180,300 positions as of February, an increase of 700 jobs or 0.4 percent from December 2013. On an annual basis, this sector increased employment by 7,200 positions or 4.2 percent. For the year ending February 2014, the financial services sector grew at 2.9 percent, adding 2,000 positions over the year.

Market conditions

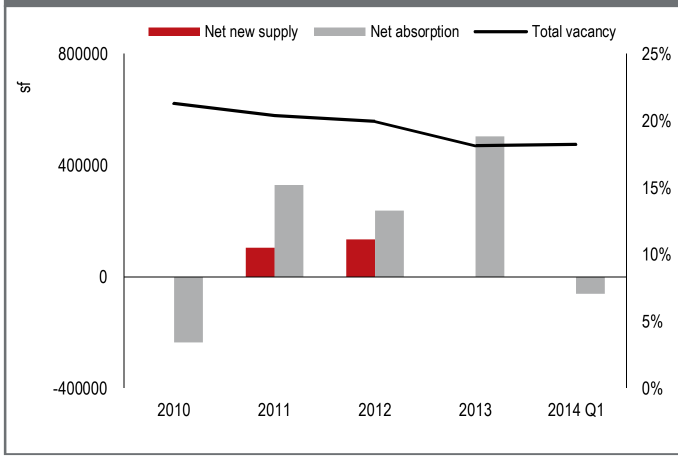
Overall, office market conditions in the first quarter dipped off a bit, with the overall market registering negative total net absorption of 61,676 square feet or 0.2 percent of the total stock. Although not the strong start we had hoped for, the four quarter rolling total, which gives an indication of the absorption trend, stands at a positive 605,570 square feet. With that, the quarter's negative absorption resulted in a 200 basis point increase in the total vacancy rate to 18.0 percent. While the rate ticked up over the quarter, it remains 190 points below the five year moving average of 19.9 percent. Out of the seven submarkets, only three (CBD, Lake Mary and the University Area) posted positive direct net absorption, while only two(Lake Mary and the University Area) posted positive direct and total net absorption. The University Area lead the way, absorbing 1.4 percent of its stock, followed by Lake Mary at 0.5 percent. The CBD remained flat in terms of total net absorption during the quarter.

Outlook

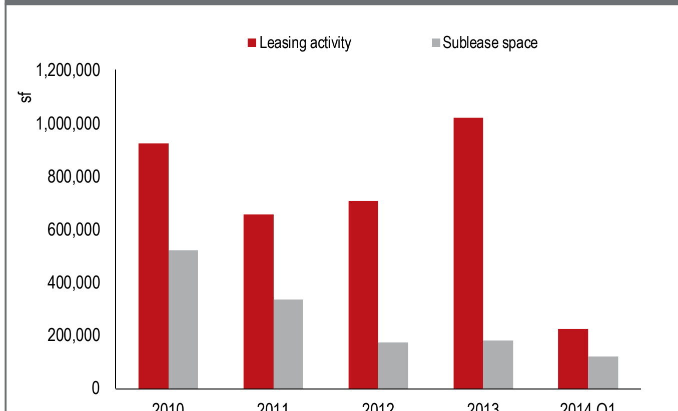
While office market conditions didn't perform up to our expectations during the first quarter, we expect an improvement heading into the remainder of 2014. Driving this outlook is the strong growth we are seeing in Orlando's job market, along with new infrastructure developments that will attract new businesses to the area and provide a boost to the local economy. With targeted investments being made in Orlando's emerging life science's industry, along with other efforts to sustain and grow the area's modeling, simulation and training industry, the Orlando office market will be positioned well to benefit from these investments in the future.

Key market indicators		12-month forecast	
Supply	Supply	➤	28,248,216 sf
	Direct vacancy rate	▼	17.5%
	Total vacancy rate	▼	18.0%
	Under construction (% preleased)	➤	0 sf (0.0%)
Demand	Leasing activity 12 mo. % change	▲	-78.0%
	YTD net absorption	▲	-61,676 sf
Pricing	12-month overall rent % change	➤	0.0%
	Class A overall asking rent	▲	$21.72 psf
	Class B overall asking rent	➤	$17.56 psf

Net new supply, net absorption and total vacancy (YTD)



Leasing activity vs. sublease vacant space (Q1 Comparison)



Sublease space refers to vacant space

Tenant perspective

Although the pace of demand activity has decreased in the first quarter compared to the fourth quarter of 2013, we don't see this continuing into the remainder of the year. Strong job growth and key investments in local industry clusters will continue to grow the local economy. The new SunRail commuter train line, which is set to begin service in May, is already spurring commercial investment in and around the areas where the stations are located. Lake Mary, Maitland, the CBD and the Southwest submarkets are all poised to see an increase tenant demand related to the new train system.

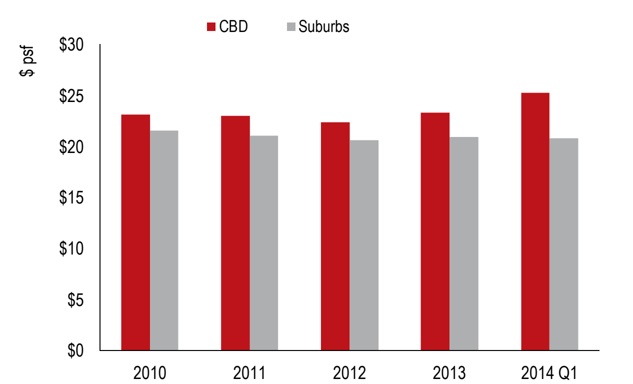
While no new significant office space is slated to be delivered this year, tenants can expect leverage in the market to continue shifting in the direction of landlords, as demand for quality space ramps up in response to increased economic activity.

Landlord perspective

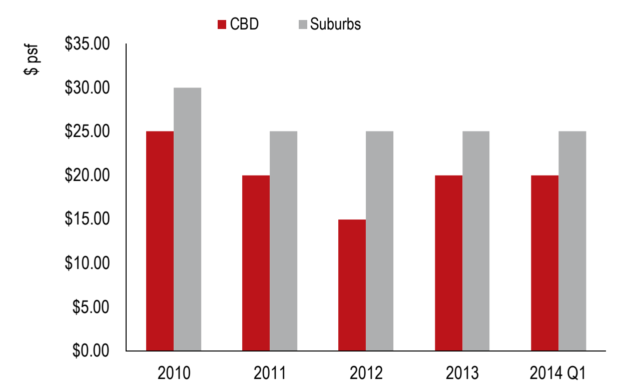
As local economic conditions strengthen, and with no new construction slated to be delivered in the near future, office landlords in certain submarkets are feeling more optimistic about raising asking rates. The rate hikes were mainly concentrated in Class A space; four out of the seven submarkets(Southwest, Lake Mary, CBD and the University Area) saw landlords increase Class A asking rates, both on a quarterly and annual basis.

In the near-term, landlords in newer, more modern Class A buildings located in the urban core and along the new passenger train route will have the upper hand in Orlando's office market, as these are the locations slated to attract a significant amount of future investment and tenant demand.

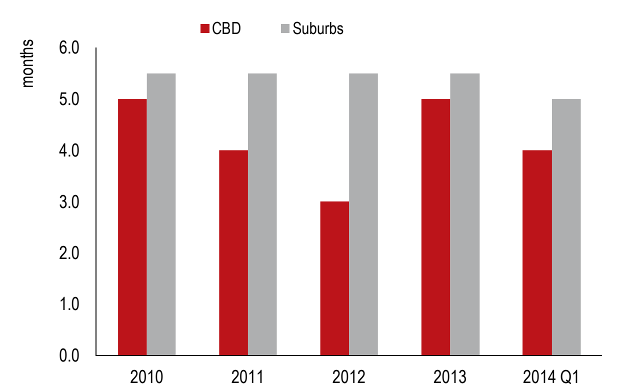
Class A overall asking rents



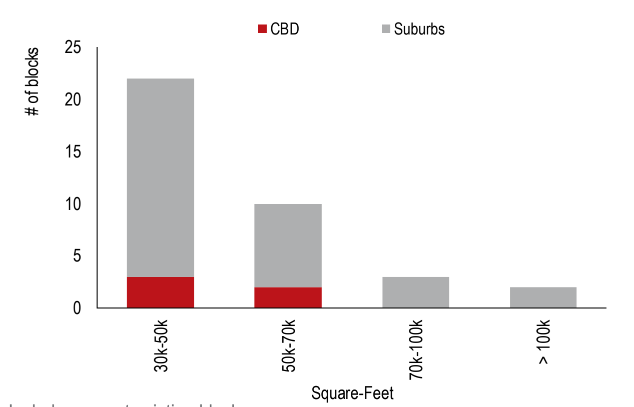
Class A tenant improvement allowance



Class A free rent

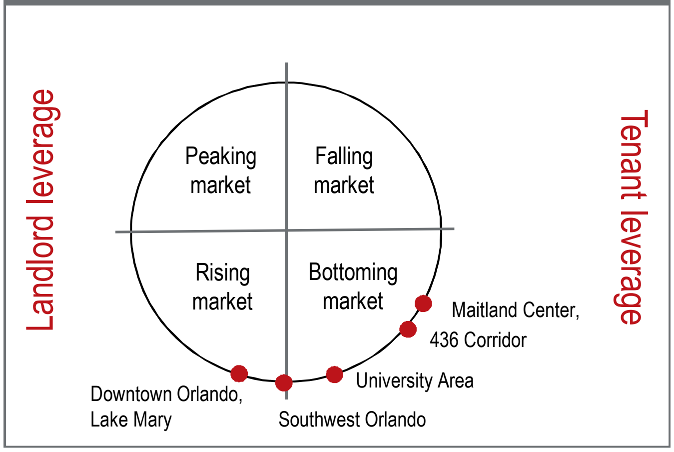


Class A blocks of contiguous space

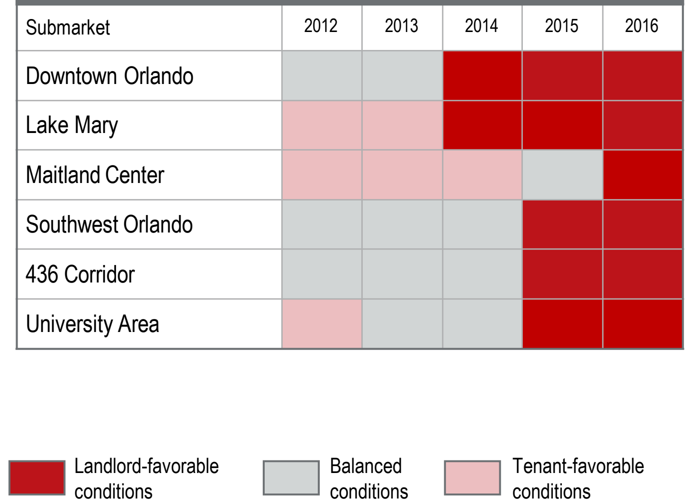


Includes vacant existing blocks

Property clock



Submarket leverage



Completed lease transactions

Tenant	Building Name	Submarket	Square Feet	Type
Accredo Health	6272 Lee Vista Boulvard	436 Corridor	78,000	Renewal
Booking.com	8529 SouthPark Circle	Southwest	44,541	Expansion
Cisco Systems	12001 Research Parkway	University Area	10,924	Renewal
Trust International	3504 Lake Lynda Drive	University Area	10,000	New

Sales activity

Address/Building Name	Submarket	Buyer	Seller	Size(SF)	$/SF
851 Trafagar Court	Maitland Center	Crocker Partners	Windsor Realty Fund	174,048	85
215 Celebration Place	Celebration	Terracap Management	CBRE Global Investors	125,490	142
300 Promera Boulevard	Lake Mary	Banyan Street Capital	Sun Life Financial	122,655	112

Orlando methodology: Inventory includes all Class A & B office properties > 30,000 square feet, excluding all condo, medical and government owned buildings, and owner occupied buildings

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