

Savills Studley Report Chicago CBD office sector

Q1 2018



SUMMARY

Market Highlights

LEASING DECLINES

Following a strong quarter of activity, with 3 million square feet (msf) leased – quarterly activity decreased to 2.2 msf in the first quarter. Tenants have leased 11.5 msf in the four most recent quarters, exceeding the long-term market average by 26.2%.

AVAILABILITY INCHES DOWNWARD

The market's overall availability rate decreased by 50 basis points from 16.2% to 15.7%. The Class A availability rate fell by 40 basis points to 16.4%.

RENT GROWTH SLOWS

The Class A gross asking rent increased by 0.4% during the quarter, averaging \$44.72. The overall Downtown asking rent rose by 1.4%, from \$39.36 to \$39.91.

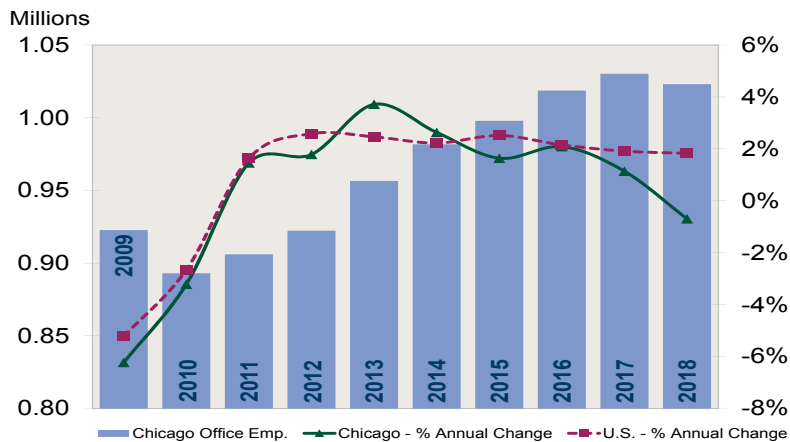
SALES UP

Office property sales during the last six months (through February 2018) totaled \$2.6 billion, a 4% increase compared to the previous six month total of \$2.5 billion. Sales in Chicago's Suburban market totaled \$800 million while Chicago CBD witnessed sales of \$1.8 billion during this period.

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"Chicago is on the cusp of another wave of development activity, including projects in emerging micro-districts like Fulton Market and the Clybourn Corridor. Unless Chicago lands Amazon, it remains to be seen whether current demand is sustainable as more than 7 msf delivers downtown in the next three years."

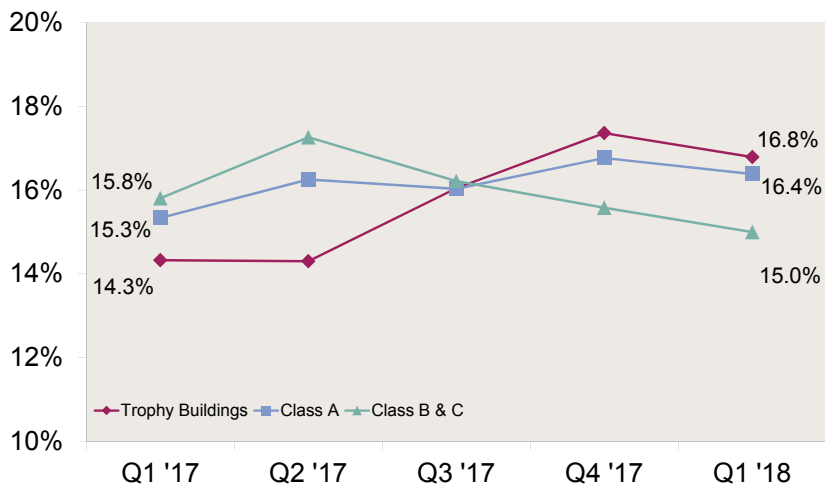
Eric Feinberg, Executive Vice President
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Office-Using Employment Trends

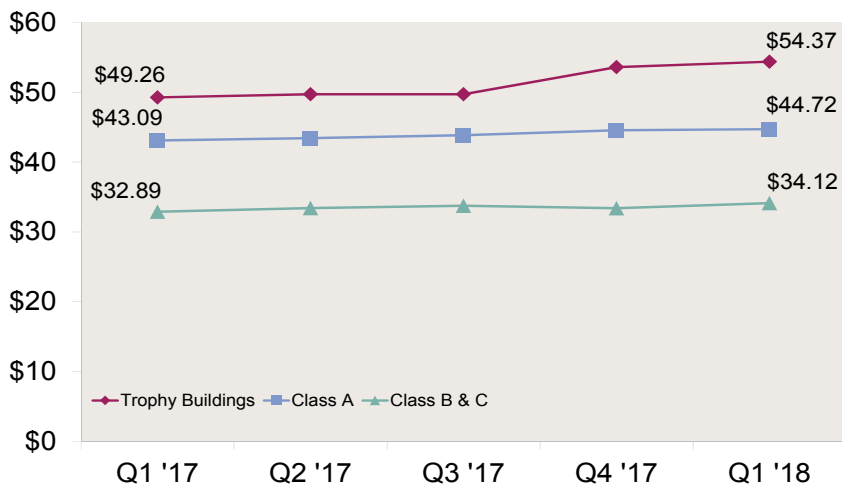


Source: Bureau of Labor Statistics^

Availability Rate Trends



Asking Rent Trends (\$/sf)



Just an Anchor Tenant Away

The resurgence of cities, often at the expense of suburban locales, has been a key theme of this cycle. Chicago's downtown Loop has certainly participated in this urban renaissance. Recent data from the Illinois Department of Employment Security shows that as of March 2017, the central area of Downtown Chicago has nearly 594,000 private sector jobs, a 23.9% gain from the 479,000 in 2010. In comparison, all of Chicago land posted growth of only 13.5%. For the first time on record, a majority of jobs in the greater Chicago region were concentrated within the Loop.

Much like labor markets, the region's office markets have experienced a very uneven recovery. Downtown's Class A availability rate ended the first quarter at 16.4%, down by 330 basis points from its peak mark of 19.7% in 2010. In contrast, Suburban Chicago's Class A rate was 26.7%, which is 170 basis points higher than at the close of 2010 (25.0% availability). Leasing activity Downtown has averaged 2.6 msf in the last three years, 8% above its historical average. In contrast, Suburban Chicago has averaged 1.3 msf, falling short of its average by 7%.

Financial institutions have long preferred prominent Downtown locations. During the first quarter of the year, leasing was relatively steady with several leases by financial sector firms completed. A trio of financial transactions boosted quarterly totals. Citadel inked a 408,000-sf renewal at 131 S Dearborn Street. Bank of America completed a 405,000 sf renewal and expansion at 540 W Madison Street and Morgan Stanley leased 122,000 sf at Willis Tower.

Financial institutions have long preferred prominent Downtown locations. Other employers are following younger talent to the energy and buzz of Downtown Chicago. Recent examples of companies moving within the Loop include Shure, Nielsen, and Peapod. Many of the largest relocations were announced last summer. Peapod, for example, announced plans to shift its headquarters from Skokie to the West Loop. The company, founded in 1989, is a relative veteran in the grocery delivery sector. The move Downtown is part of its battle to keep up with Instacart and Amazon, which are plowing a lot of resources into this evolving sector. Last year Amazon announced plans to double its space and staff at 227 W. Monroe Street.

Amazon HQ2 in Focus

Chicago remains a contender among the 20 cities on Amazon's HQ2 list. Amazon has a

particularly massive need for labor, expecting to hire 50,000 workers wherever it ultimately decides to base its second headquarters. Recent analysts seem to put higher odds on Boston, Atlanta or Northern Virginia as winners. Chicago has its competitive advantages, including being attractive to recent college grads. Its logistical advantages are often overlooked. O'Hare, the second busiest airport nationally, offers connections and transport to global destinations. Amazon has already built several massive warehousing/logistics facilities outside of Chicago. HQ2 is primarily an office investment, but a location at the center of the second biggest industrial market in the U.S. may offer benefits to the Seattle-based behemoth.

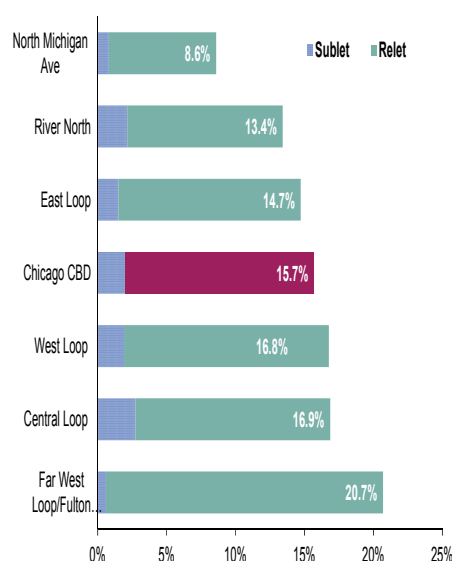
Should Chicago fail to attract Amazon, it remains debatable whether current rents can be sustained, and if availability can remain low, as the delivery of new inventory looms. Approximately 5 million square feet of new downtown product will come online in the next 12 months, the majority of which remains uncommitted by tenants. While companies have been considering space at the Old Post Office and 625 West Adams Street, there have been no commitments at either project to date.

Dueling Developments

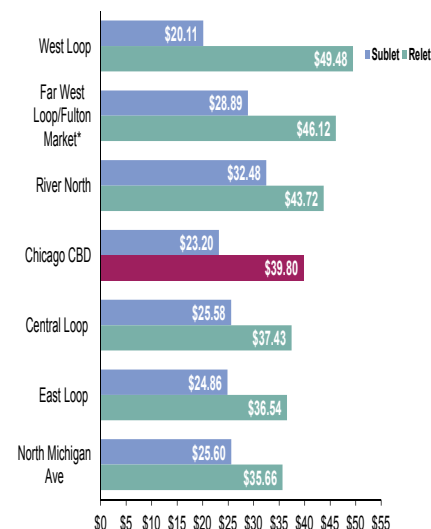
Landing HQ2 would be a lightning rod for development activity in the region. It would very likely push forward some of the transformative redevelopment projects being proposed in the South Loop or North Side. None of the most recently delivered glass towers in the Loop, or the next set of buildings under way could fulfill Amazon's short-term need for 1.0 msf in 2019. The two West Loop trophy towers that delivered in 2017 (150 N Riverside Plaza and River Point) each have only about 50,000 sf remaining for lease. The next set of buildings delivering later this year includes two more West Loop buildings catering to traditional tenants (625 W Adams and 151 W Franklin) and multiple warehouse teardowns or conversions in River North and Fulton Market. The Post Office conversion will have 2.7 msf available in January 2019.

Consequently, the list of viable candidates for a Chicago Amazon HQ2 turns to the massive and complicated redevelopments such as Sterling Bay's 70-acre riverfront Lincoln Yards on the North Side or Related Midwest's 62-acre site along the Chicago River in the South Loop. A South Loop development of this scale would be the first such office campus of this size in this area. Another alternative would be a campus-style development in Fulton Market. The transformation of Fulton Market was initially accomplished in a very piecemeal fashion – 50,000 sf to 100,000 sf at a time.

Availability Rate Comparison



Rental Rate Comparison (\$/sf)



Major Transactions

Tenant	Sq Feet	Address	Market Area
Citadel	408,000	131 S Dearborn St	Central Loop
Bank of America	405,000	540 W Madison St	West Loop
Morgan Stanley	122,000	233 S Wacker Dr	West Loop
TTX	100,000	101 N Wacker Dr	West Loop
Tempus Labs	83,622	600 W Chicago Ave	River North
Spaces Coworking	78,265	620 N LaSalle Dr	River North
Gartner	74,450	350 N Orleans St	River North
Kemper	64,956	200 E Randolph St	East Loop
Scientific Games	57,071	350 N Orleans St	River North
C.H. Robinson	56,800	315 N Racine Ave	Far West Loop/Fulton Market
Sum of Top 10 Leases	1,450,164	Sum of 1st Qtr Leasing Activity	2.2 MSF

The movement of Google and McDonald's into Fulton Market signaled the arrival of the submarket as a corporate destination. More than 6.5 msf of new office space is either under way or in the planning stages in Fulton Market. Roughly half, (49%) of the 1.7 msf currently underway has been pre-leased. Developers have much more proposed product, just waiting for an anchor tenant or two, though. Sterling Bay's proposal for the former Coyne College campus calls for three buildings totalling 1.6 msf. Advertising firm WPP Group has committed to just over 250,000 sf at 333 N. Green. Local developer Shapack Partners Focus Development and Walton Street Capital are seeking approvals for a 17-story office tower at 167 N. Green Street just South of Sterling Bay's project. The proposal envisions a 50-foot-wide public square called the Mews which can be used for markets, entertainment and retail pop-ups.

Looking Forward

Capturing Amazon would at least temporarily push Chicago off the long-term path followed by

so many Midwest and Northeast metros – the loss of employers and households to warmer, lower-cost Sunbelt markets. Over the long term Chicago is likely to face one of its chronic challenges – population decline. The flow of people and businesses from the suburbs to the city may actually prove more transitory than the migration of people to other regions of the country entirely.

The greater Chicago region has already seen a net loss of domestic households, with an outmigration of nearly 200,000 residents between 2014 and 2016. In some cities such as New York City or Miami, the influx of people from other countries offsets much of the domestic migration. Foreign relocation to Chicago totals only about 60,000, only covering about one-third of the loss. Some of the net loss is to suburban areas – defying the notion that all Chicago residents are moving to the city. Additionally, though, the flow to warmer and lower-cost regions such as Phoenix and Los Angeles as well as Dallas and Houston is in full force.

Map	Submarket	Total	Leasing Activity		Available SF			Availability Rate*			Asking Rents Per SF		
		SF (1000's)	Annual Leasing Volume	Annual Net Absorption	This Quarter	% Change from Last Qtr.	Year Ago	This Quarter	pp Change from Last Qtr. ⁽¹⁾	Year Ago	This Quarter	% Change from Last Qtr.	Year Ago
1	West Loop	49,098	5,191	102.0	8,231	-3.4%	8,894	16.8%	-0.6%	18.1%	\$43.11	2.0%	\$40.80
	West Loop - Class A	34,764	4,153	141.1	5,705	-4.9%	6,271	16.4%	-0.8%	18.0%	\$46.22	2.0%	\$43.95
2	Far West Loop/Fulton Market	4,562	716	(22.6)	944	-26.8%	457	20.7%	-7.6%	10.0%	\$45.91	-0.8%	\$35.84
	Far West Loop/Fulton Market - Class A	2,011	428	(87.1)	617	-28.8%	143	30.7%	-12.4%	7.1%	\$50.73	0.3%	\$47.75
3	Central Loop	40,554	2,506	17.1	6,840	-4.3%	6,700	16.9%	-0.8%	16.5%	\$35.85	1.5%	\$35.45
	Central Loop - Class A	15,072	907	(96.0)	2,515	-0.9%	2,111	16.7%	-0.1%	14.0%	\$40.24	-0.7%	\$41.69
4	East Loop	20,254	1,557	348.7	2,982	-0.5%	3,062	14.7%	-0.1%	15.1%	\$36.01	-0.6%	\$35.49
	East Loop - Class A	8,078	367	2.2	1,164	-2.8%	1,176	14.4%	-0.4%	14.6%	\$39.87	-1.0%	\$38.95
5	North Michigan Avenue	9,489	326	132.3	815	-1.1%	1,080	8.6%	-0.1%	11.4%	\$35.22	-1.0%	\$35.21
	North Michigan Avenue - Class A	4,193	185	3.9	388	-2.6%	422	9.3%	-0.2%	10.1%	\$39.33	-3.3%	\$39.28
6	River North	16,114	1,227	(3.3)	2,162	15.3%	1,615	13.4%	1.8%	10.0%	\$43.63	2.8%	\$40.91
	River North - Class A	5,868	535	51.2	1,075	46.1%	609	18.3%	5.8%	10.4%	\$46.84	-4.4%	\$47.99
1-6	Chicago CBD Total	140,071	11,524	574.1	21,974	-3.0%	21,808	15.7%	-0.5%	15.6%	\$39.91	1.4%	\$38.04
	Chicago CBD Total - Class A	69,987	6,575	15.3	11,464	-2.3%	10,731	16.4%	-0.4%	15.3%	\$44.72	0.4%	\$43.09

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*Rent and availability rates in submarkets with a limited amount of inventory are sometimes subject to large fluctuations.

(1) Percentage point change for availability rates.

Unless otherwise noted, all rents quoted throughout this report are average asking gross (full service) rents psf.

Statistics are calculated using both direct and sublease information.

Short-term sublet spaces (terms under two years) were excluded.

^Unless otherwise noted, source for data is Savills Studley.

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