INVESTMENT FORECAST

OFFICE

Detroit Metro Area

IPA | INSTITUTIONAL PROPERTY ADVISORS

2020

Detroit Vacancy Stable Near 12-Year Low, Sparking Increased Development

Vacancy is hovering near the 12-year low. Strengthening demand for office space amid a lack of speculative construction and the conversion of vacant office buildings into alternative uses is holding vacancy tight. Although deliveries will climb in 2020, heavy pre-leasing will lessen the impact on vacancy and push rent higher. The expansion of One Campus Martius is the largest building due in the market this year. The 310,000-square-foot addition to the former Compuware building in Detroit is already fully leased. Deliveries will remain heightened as Ford's Michigan Central Station, Hudson's Tower and a new headquarters for TCF Financial are finalized. These developments and newly renovated buildings will add more than 2 million square feet to inventory over the next few years. Meanwhile, rapidly rising rents in downtown Detroit have some tenants searching for less expensive space outside the core. This is generating office demand in the New Center and Midtown neighborhoods of Detroit. Suburban vacancy has also tightened considerably from the cyclical peak. The suburbs are scheduled to receive 400,000 square feet of office space in 2020. One significant project is the 140,000-square-foot Henry Ford Health System outpatient building in Royal Oak.

Brighter economic outlook draws new investors. Detroit's broadening renaissance will bolster the office market this year, led by expansion in the automotive technology segment. As auto companies and their suppliers fill space, investors are taking notice. Many buyers are attracted to highly vacant buildings in the suburbs for their value-add potential. Properties that can be quickly upgraded and retenanted at market rate rent are most desired. Vacancy above the metro average has more buyers searching in Southfield, where over the past year many buildings traded below the market average of $128 per square foot. Marketwide, investors are drawn by cap rates that average in the low-8 percent range, well above yields available in most other major metros.

2020 Market Forecast

Employment up 0.04% — After losing 500 positions last year, employers will add 750 jobs in 2020, including 250 office-using positions.

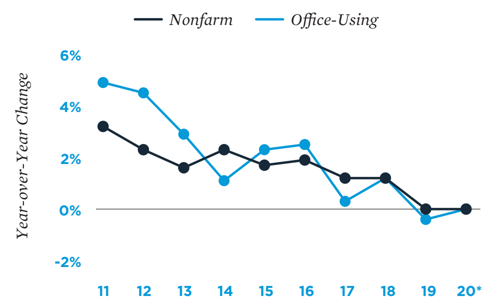
Construction 1.2 million sq. ft. — Deliveries nearly double last year's 550,000 square feet, reaching the highest level since 2007. The city of Detroit will receive about half of the new space in 2020.

Vacancy up 20 bps — Supply will rise above demand, inching vacancy up to 15.3 percent in 2020. The rate, however, is down 260 basis points since 2015.

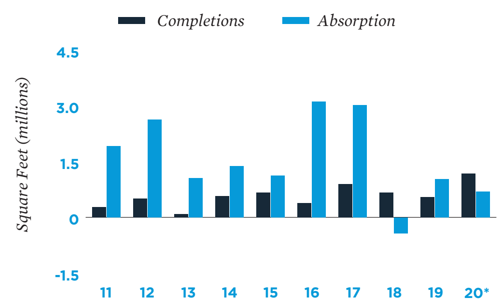
Rent up 3.2% — After rent jumped 4.3 percent during 2019, the average asking rent ends 2020 at $21.10 per square foot. Roughly 34 percent below the national level.

Investment — Class B medical office assets throughout the metro remain a prime target of buyers at first-year returns that are typically in the 6 to 7 percent range.

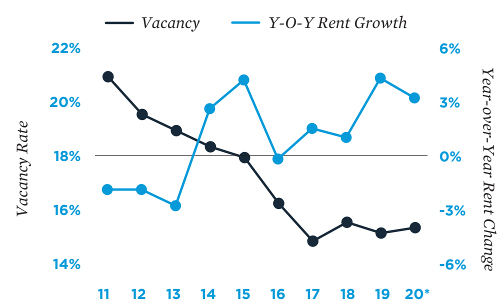
Employment Trends



Office Supply and Demand



Vacancy and Rent Trends



* Forecast

Sources: CoStar Group, Inc.; Real Capital Analytics

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Metro-level employment, vacancy and asking rents are year-end figures and are based on the most up-to-date information available as of December 2020. Asking rent is based on the full-service marketed rental rate. Average prices and cap rates are a function of the age, class and geographic area of the properties trading and therefore may not be representative of the market as a whole. Sales data includes transactions valued at $1,000,000 and greater unless otherwise noted. Forecasts for employment and office data are made during the fourth quarter and represent estimates of future performance. No representation, warranty or guaranty, express or implied may be made as to the accuracy or reliability of the information contained herein. This is not intended to be a forecast of future events and this is not a guaranty regarding a future event. This is not intended to provide specific investment advice and should not be considered as investment advice.