2Q23

Cleveland Office Market Overview

Market Observations

Economy

- The Cleveland-Elyria-Mentor Metro's economy gained back a modest amount of jobs in the second quarter of 2023, as total nonfarm payroll employment increased in May by just 0.6% year over year. Employment for both the United States and the Cleveland-Elyria-Mentor Metro has been trending downward since spiking in April 2021 when the pandemic recovery took hold.
- Office-occupying or adjacent industries all saw annual job losses, along with the information and trade/transportation/utilities sectors.
- The number of office jobs has slowly rebounded to just under pre-pandemic levels, with its most recent peak taking place in December 2021. Employment rates in the Cleveland market were steady at the beginning of 2023, but dropped as the second quarter of 2023 began. Unemployment dropped dramatically after its peak in April 2020, then has slowly decreased since.

Major Transactions

- There were very few notable leases within the Cleveland market in the second quarter of 2023, as office leasing activity in the Cleveland market continued to be slow.
- One notable lease of over 20,000 SF in the second quarter of 2023 was Sotera Health Services, LLC signing a 23,611 SF lease expansion at 9100 South Hills Blvd., one of three buildings in this prominent Broadview Heights office complex.

Leasing Market Fundamentals

- The Greater Cleveland office market gave back 58,688 SF in negative net absorption in the second quarter of 2023. This caused the vacancy rate to increase by 40 basis points to 21.9% in the second quarter of 2023 from 21.5% in the first quarter of 2023.
- Total leasing activity in the Cleveland market has trended down since 2018, with the exception of 2022, a year that included the 1.0-million SF sale-leaseback in the fourth quarter of 2022 by Sherwin-Williams's under-construction headquarters that skewed that year's numbers.
- The Cleveland office market's overall average asking rental rate increased by $0.17/SF from the first quarter of 2023 to $18.99/SF, tied for the highest mark in at least 20 years but still not demonstrating a significant amount of growth over time.
- The overall market's Class A average asking rental rate of $22.53/SF was an increase of $0.48/SF from the first quarter of 2023, and the Class B average asking rental rate decreased by $0.38/SF to $16.44/SF.

Outlook

- Sublease and direct space availability both increased in the midst of the pandemic, rebounded as the pandemic subsided and have risen slowly again since the first quarter of 2022. Market vacancy has followed suit. As economic uncertainty continues, coupled with the continued hybrid work-from-home vs. in-office conundrum, it is expected that availabilities will continue to rise, along with vacancy.
- Nine of the last 10 quarters (the exception being 2020 as the pandemic took hold) have all seen year-over-year asking rental rate growth, and that trend continued in the first two quarters of 2023. Landlords have advertised higher lease rates as some have made improvements to amenities, as well as a need to recoup some losses.

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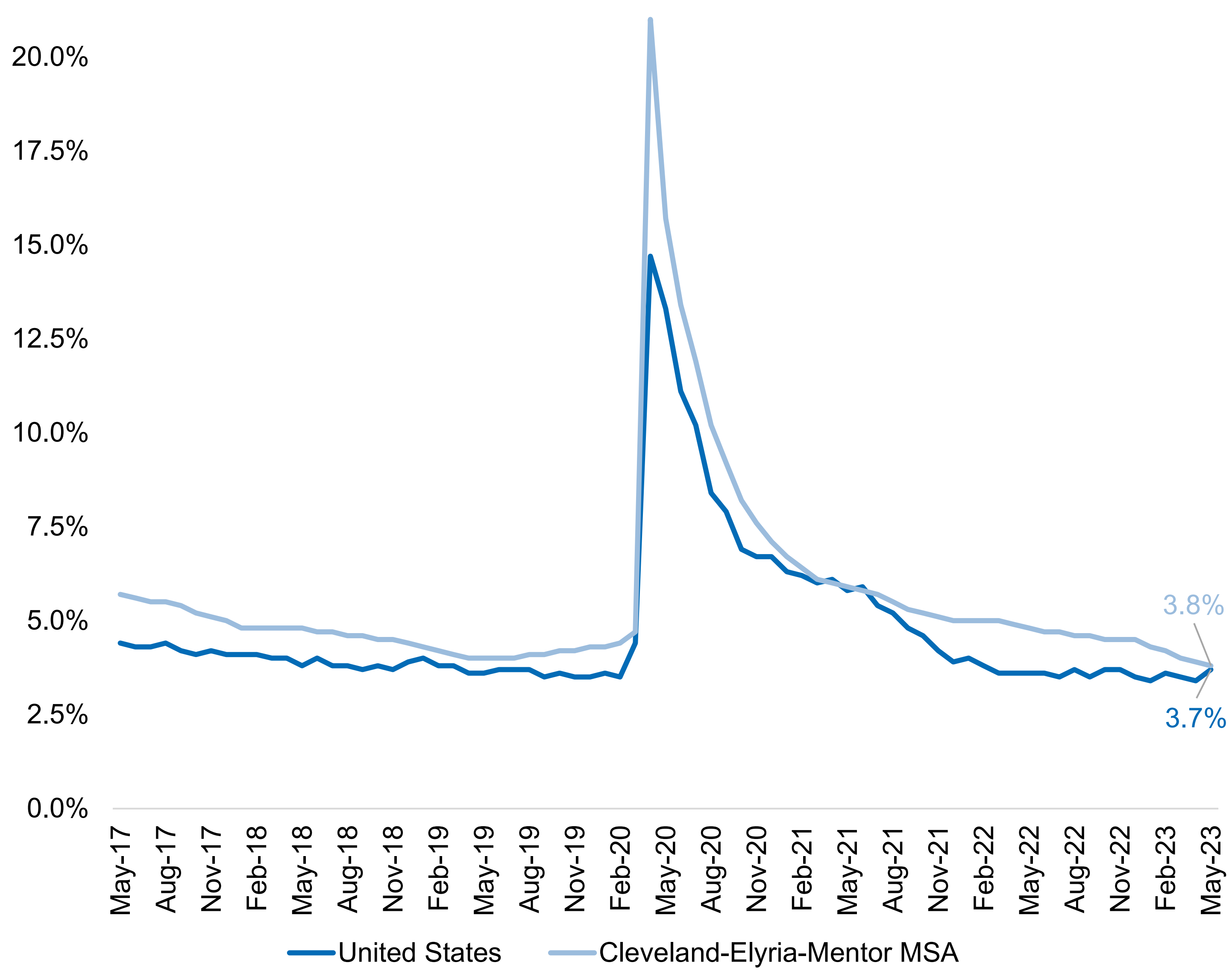
Economy

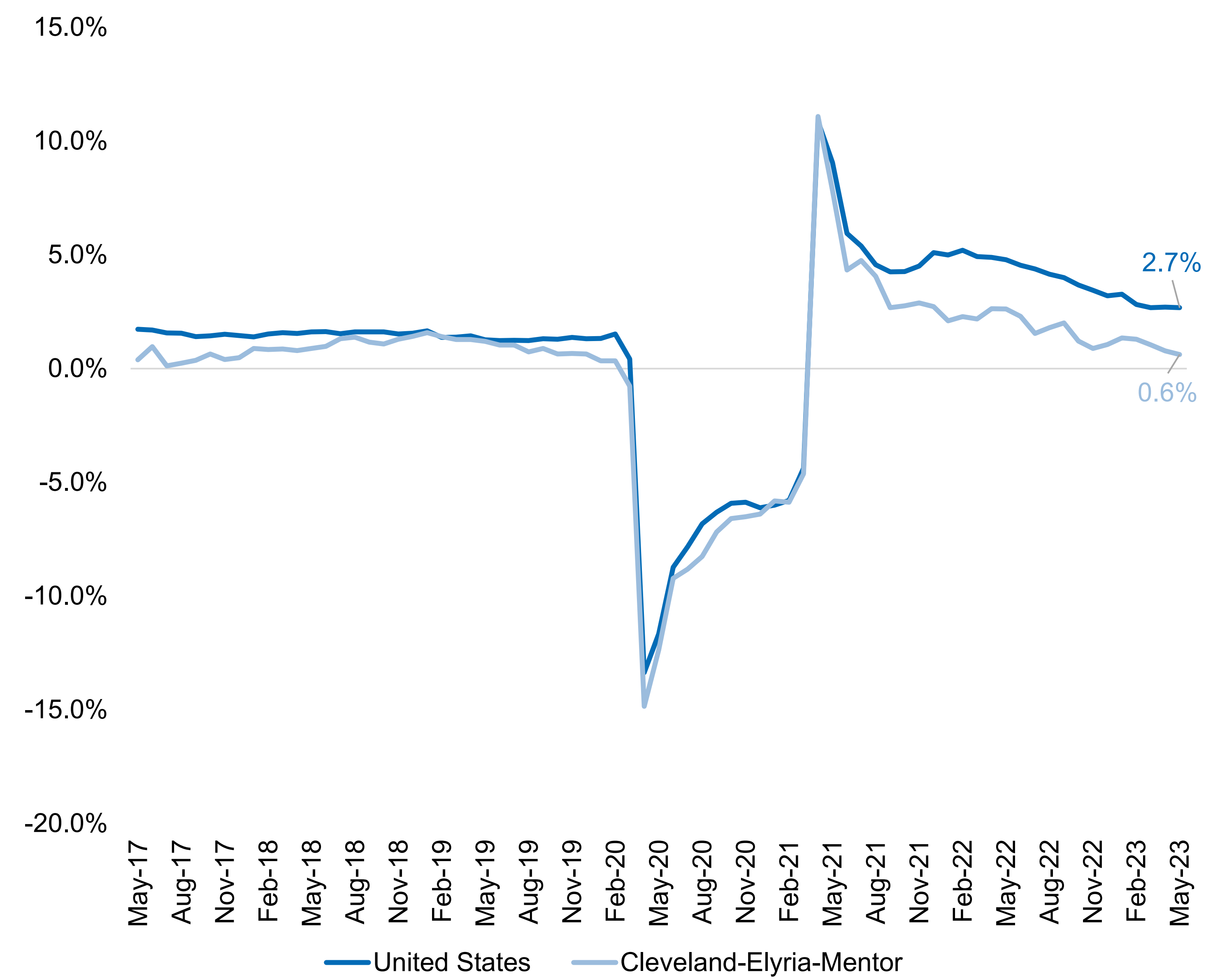
Employment Trends Signal a Slowing Economy

The Cleveland-Elyria-Mentor Metro's economy gained back a modest amount of jobs in the second quarter of 2023, as total nonfarm payroll employment increased in May by just 0.6% year over year. The national total payroll employment number was up more significantly in May, by 2.7% year over year. Employment for both the United States and the Cleveland-Elyria-Mentor Metro has been trending downward since spiking in April 2021 when the pandemic recovery took hold.

Unemployment Rate, Seasonally Adjusted



Nonfarm Payroll Employment, Non-Seasonally Adjusted, 12-Month % Change

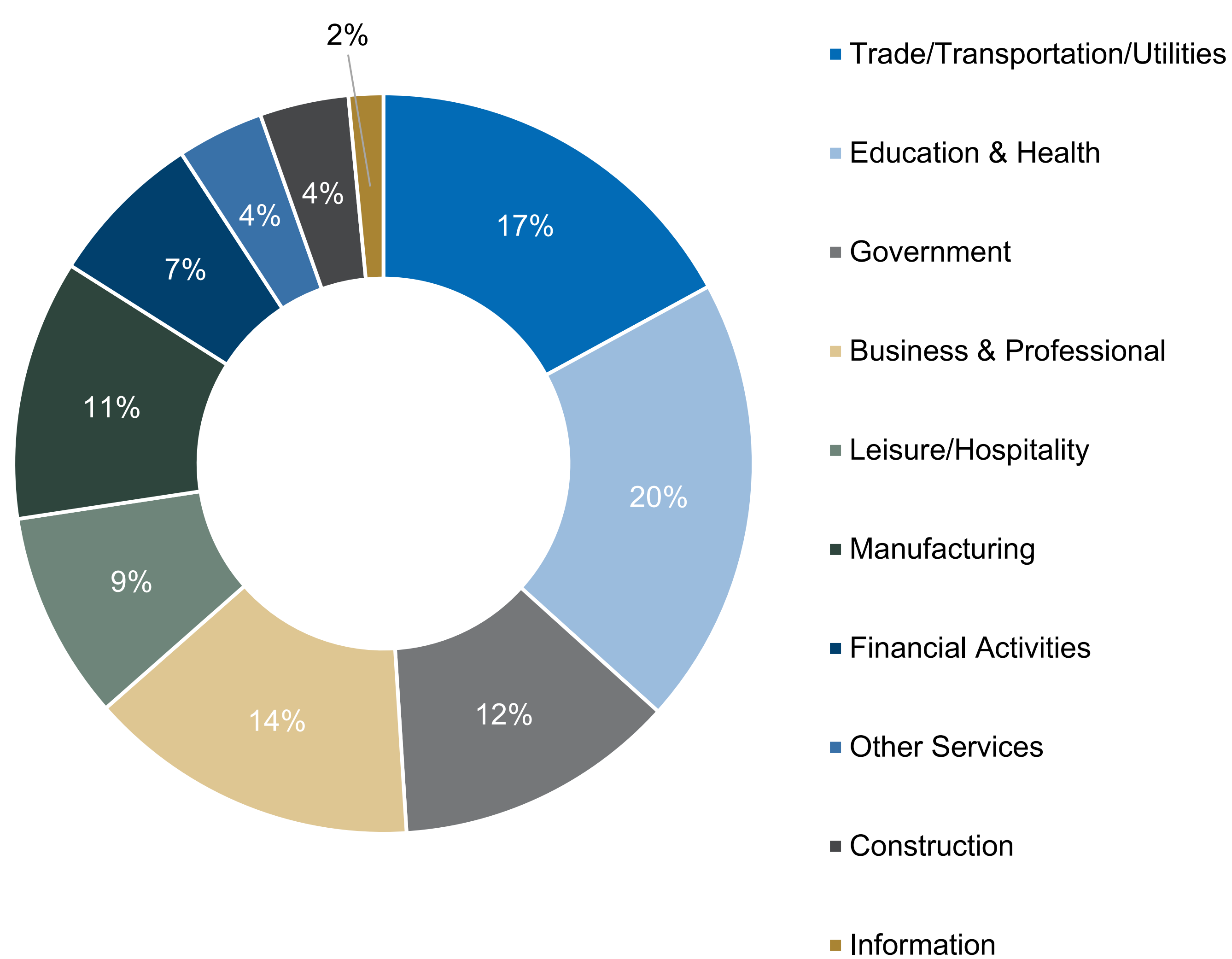


Source: U.S. Bureau of Labor Statistics, Cleveland-Elyria-Mentor MSA

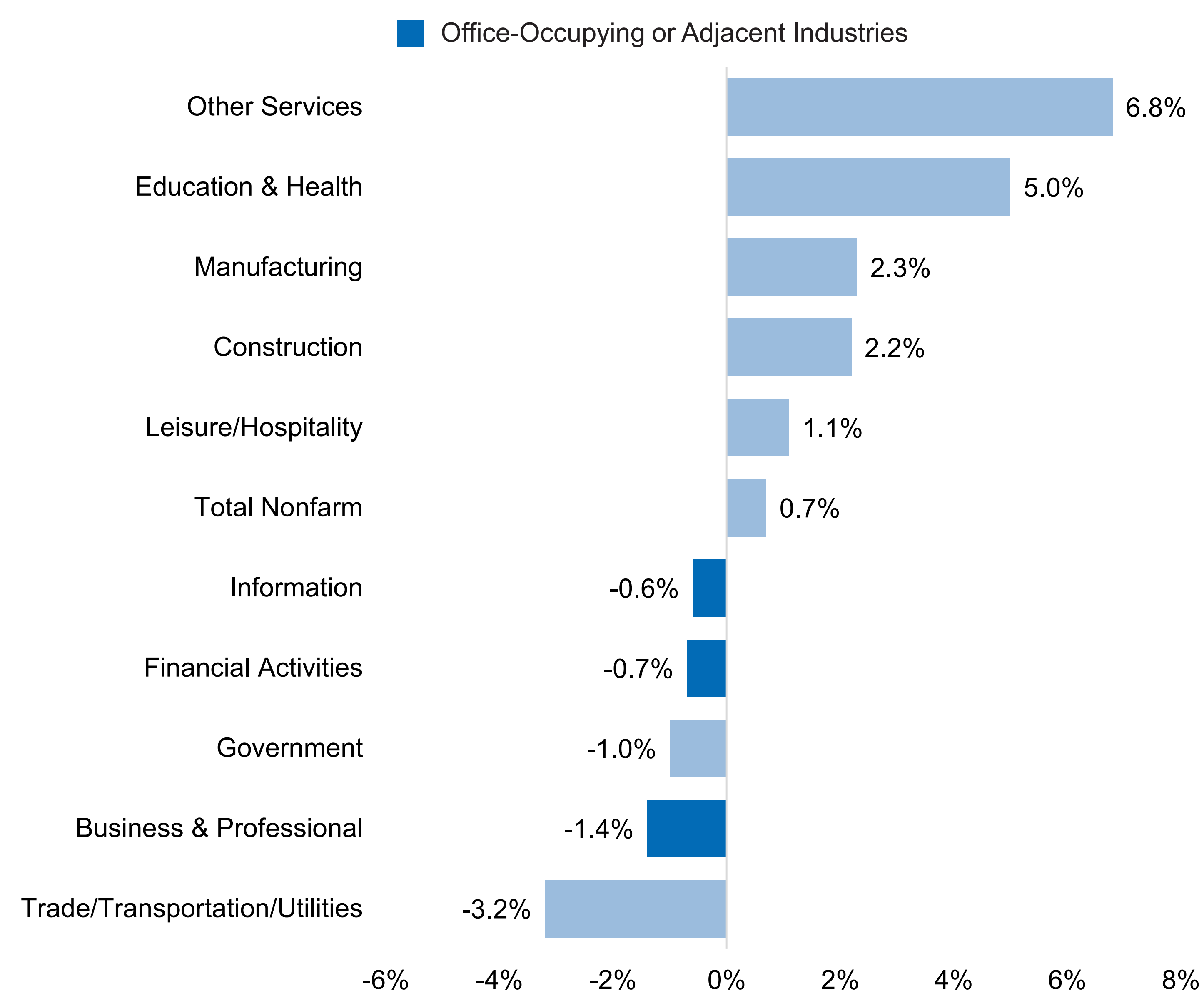
Office-Occupying or Adjacent Industries All Suffer Job Losses

Six industry sectors in the Cleveland market saw employment gains, according to preliminary year-over-year numbers from the Bureau of Labor Statistics, from May 2022 to May 2023. Office-occupying or adjacent industries all saw annual job losses, along with the information and trade/transportation/utilities sectors. The negative job growth in the office-using sector does not bode well for the office market going forward.

Employment by Industry, May 2023



Employment Growth by Industry, 12-Month % Change, May 2023*

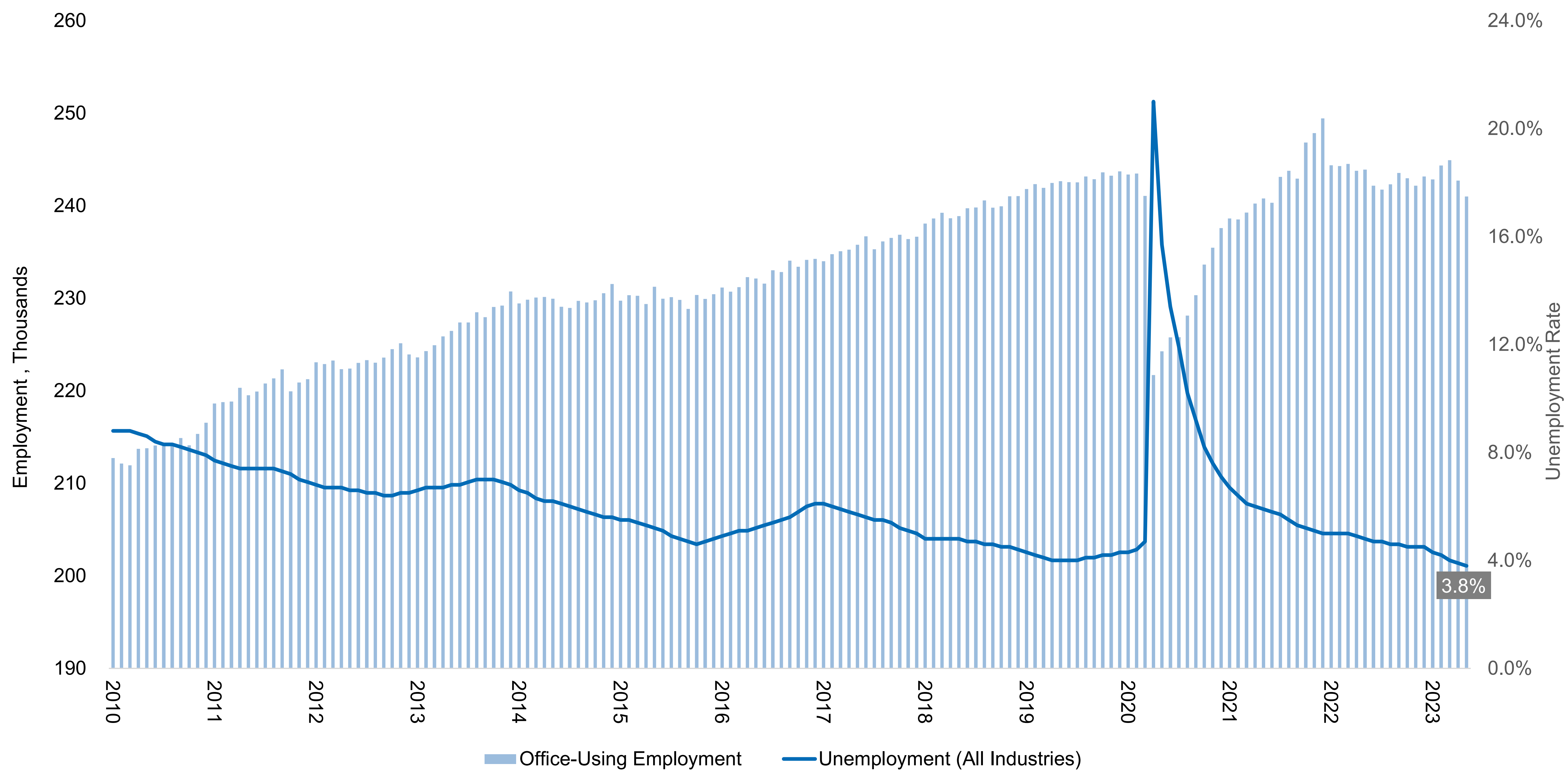


Source: U.S. Bureau of Labor Statistics, Cleveland-Elyria-Mentor MSA
*Note: May 2023 data is preliminary.

Overall Office-Using Employment Fluctuates While Unemployment Dropped

The number of office jobs has slowly rebounded to just under pre-pandemic levels, with its most recent peak taking place in December 2021. Employment rates in the Cleveland market were steady at the beginning of 2023, but dropped as the second quarter of 2023 began. Unemployment dropped dramatically after its peak in April 2020, then has slowly decreased since.

Office-Using Employment* and Unemployment Across All Industries



Source: U.S. Bureau of Labor Statistics, Cleveland-Elyria-Mentor MSA
Note: May 2023 data is preliminary.
*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.

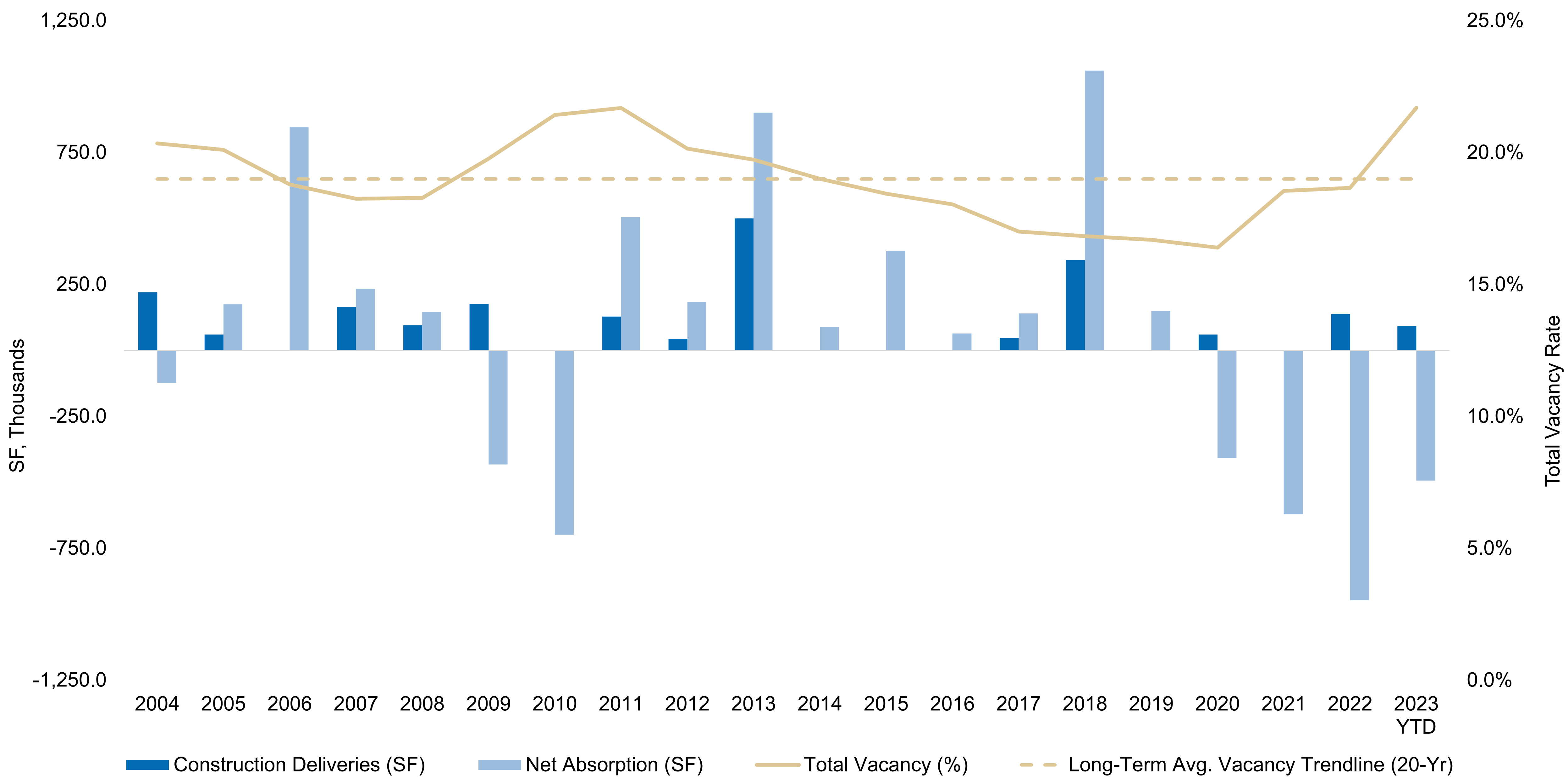
2Q23

Leasing Market Fundamentals

Vacancy Increases Slightly in 2Q23

The Greater Cleveland office market gave back 58,688 SF in negative net absorption in the second quarter of 2023. In fact, 11 of the last 15 quarters, including the last five in a row, generated negative absorption. Negative absorption caused the vacancy rate to increase by 40 basis points to 21.9% in the second quarter of 2023. The total vacancy for 2023 year to date is 21.7%, up significantly from 18.66% for the year 2022. The CBD's vacancy rate in the second quarter of 2023 was 23.8%, 50 basis points higher than the previous quarter, while the suburban vacancy rate was lower than the CBD at 20.4%, despite rising by 30 basis points from the first quarter of 2023.

Historical Construction Deliveries, Net Absorption, and Vacancy

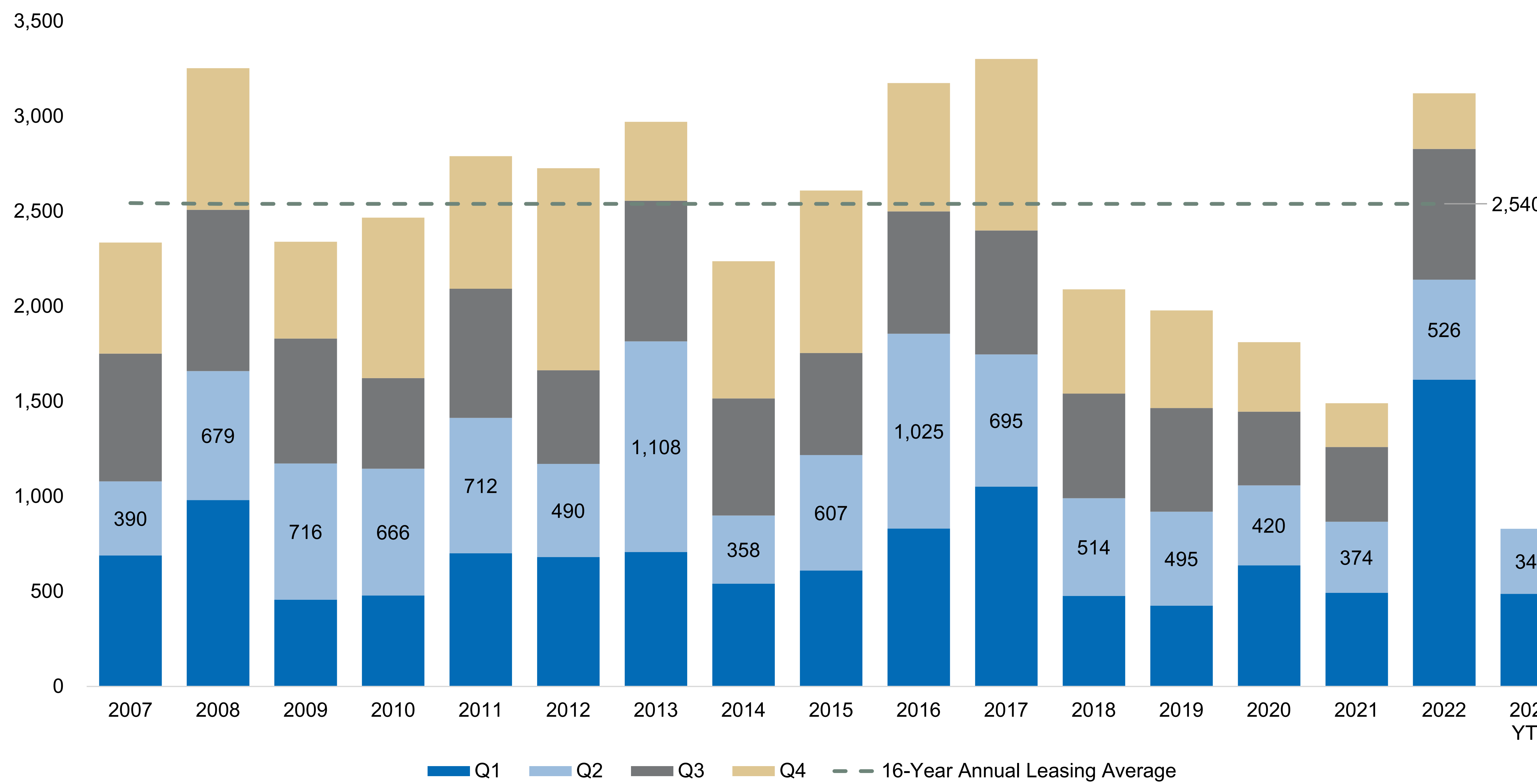


Source: Newmark Research

Leasing Activity Pace Has Slowed in Recent Years

Total leasing activity in the Cleveland market has trended down since 2018, with the exception of 2022, a year that included the 1.0-million SF sale-leaseback by Sherwin-Williams for its under-construction headquarters that skewed that year's numbers. Office space demand over the last several quarters has been lukewarm and is poised to continue its malaise until economic conditions improve and companies make further decisions regarding the in-office versus work-from-home mix.

Total Leasing Activity (thousands SF)

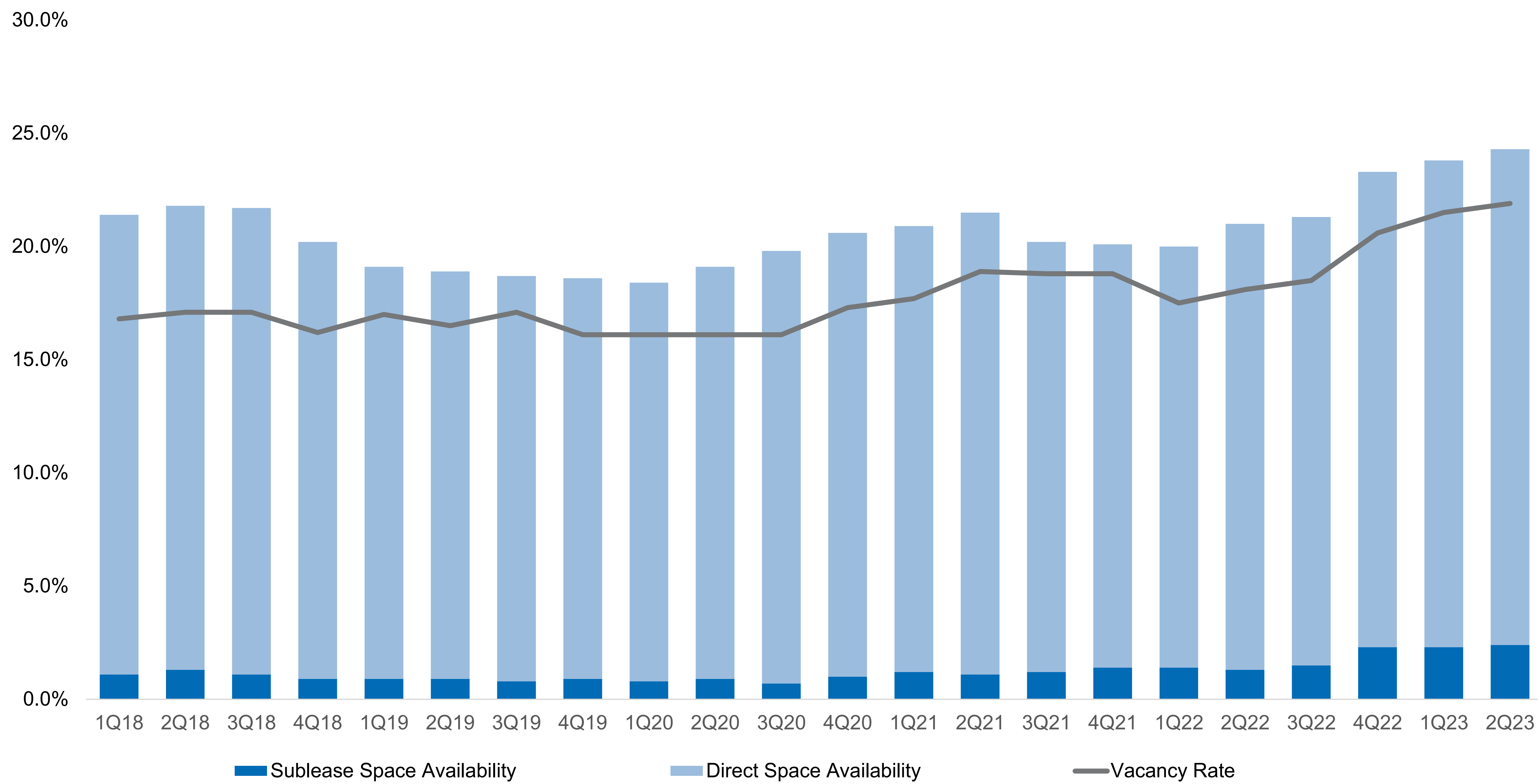


Source: Newmark Research, CoStar

Availability Increases as Office Demand Remains Tepid

Sublease and direct space availability both increased in the midst of the pandemic, rebounded as the pandemic subsided and have risen slowly again since the first quarter of 2022. Market vacancy has followed suit. Amongst some larger examples, the second quarter of 2023 saw 800 Superior in the Central Business District list a total of 45,090 SF of sublease space, while the East submarket's 6085 Parkland and 6060 Parkland added 28,870 SF and 15,842 SF of sublease space, respectively. The Cleveland office market's health, in terms of availability and vacancy, has not been optimal for several years.

Overall Market Sublease and Direct Availability Percent vs. Vacancy Rate

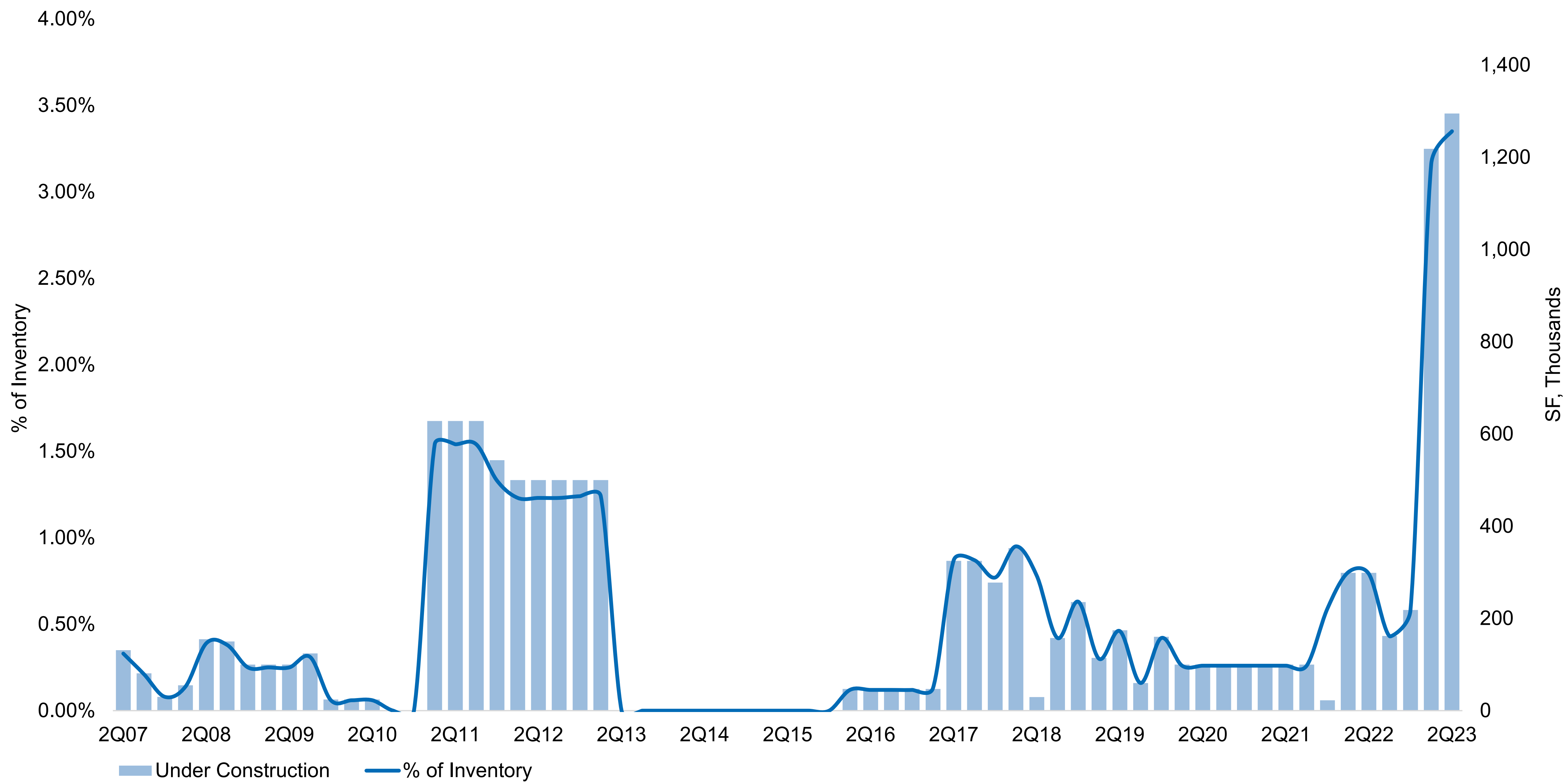


Source: Newmark Research

Office Construction Minimal

Office construction in the Cleveland market in recent years has been minimal. Currently, the 1.0 million SF Sherwin-Williams headquarters project in the CBD is the largest development the market has seen.

Office Under Construction and % of Inventory

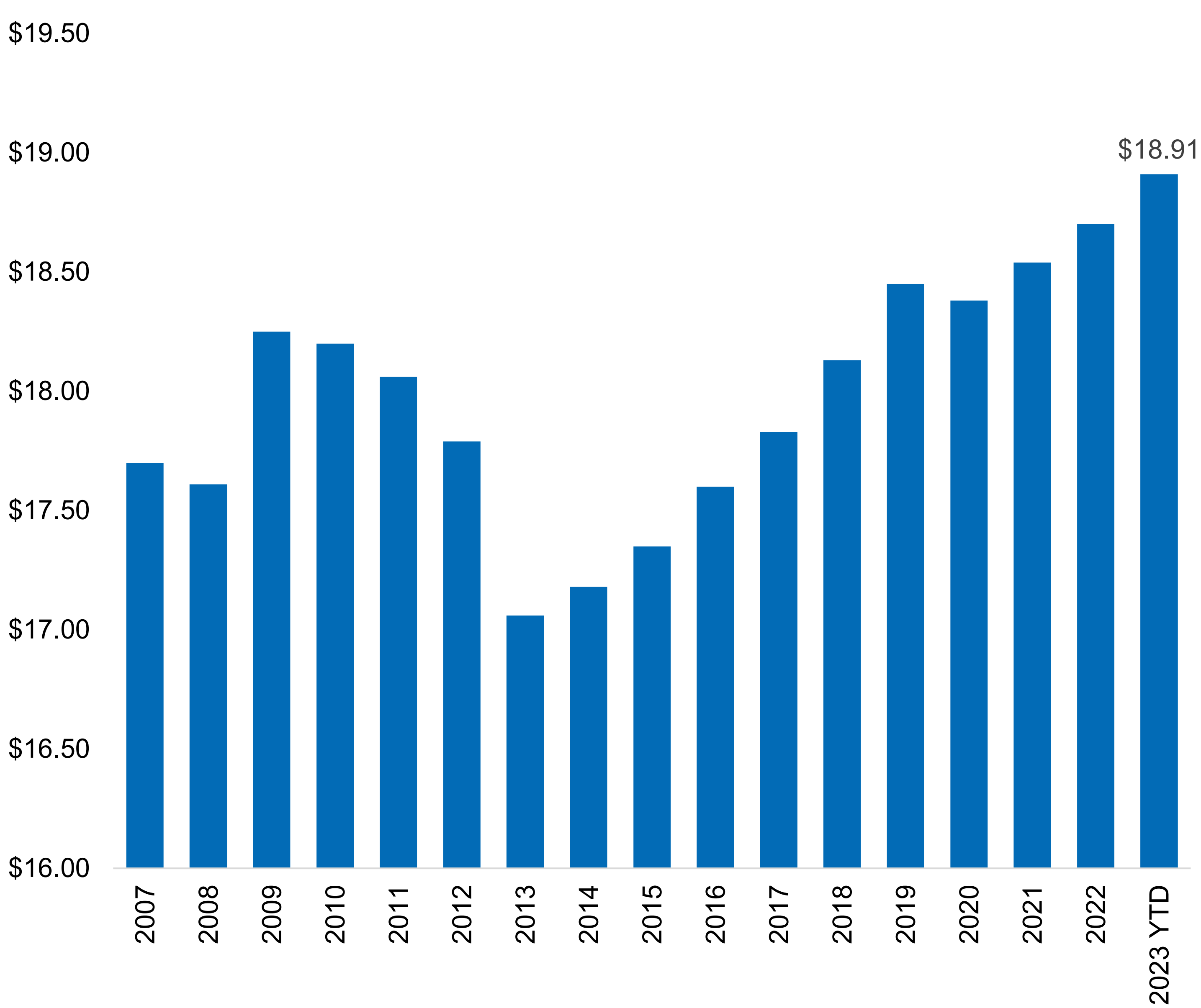


Source: Newmark Research

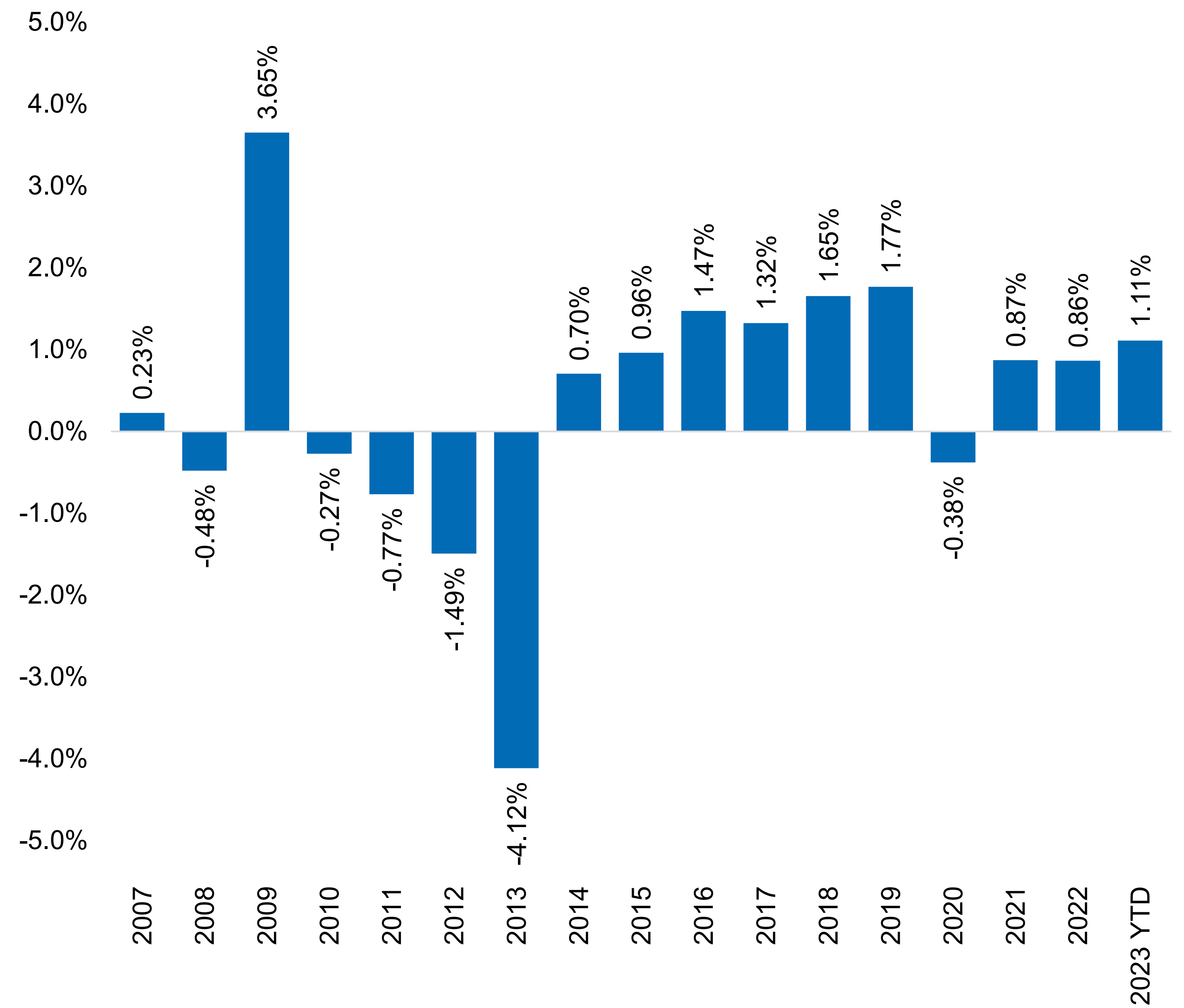
Overall Rents Climb Slowly

The Cleveland office market's overall average asking rental rate increased by $0.17/SF from the first quarter of 2023 to $18.99/SF, tied for the highest mark in at least 20 years but still not demonstrating a significant amount of growth over time. Nine of the last 10 quarters (the exception being 2020 as the pandemic took hold) have all seen year-over-year asking rental rate growth, and that trend continued in the first two quarters of 2023.

Office Average Asking Rent, $/SF, FS



Year-over-Year Asking Rent Growth Rate

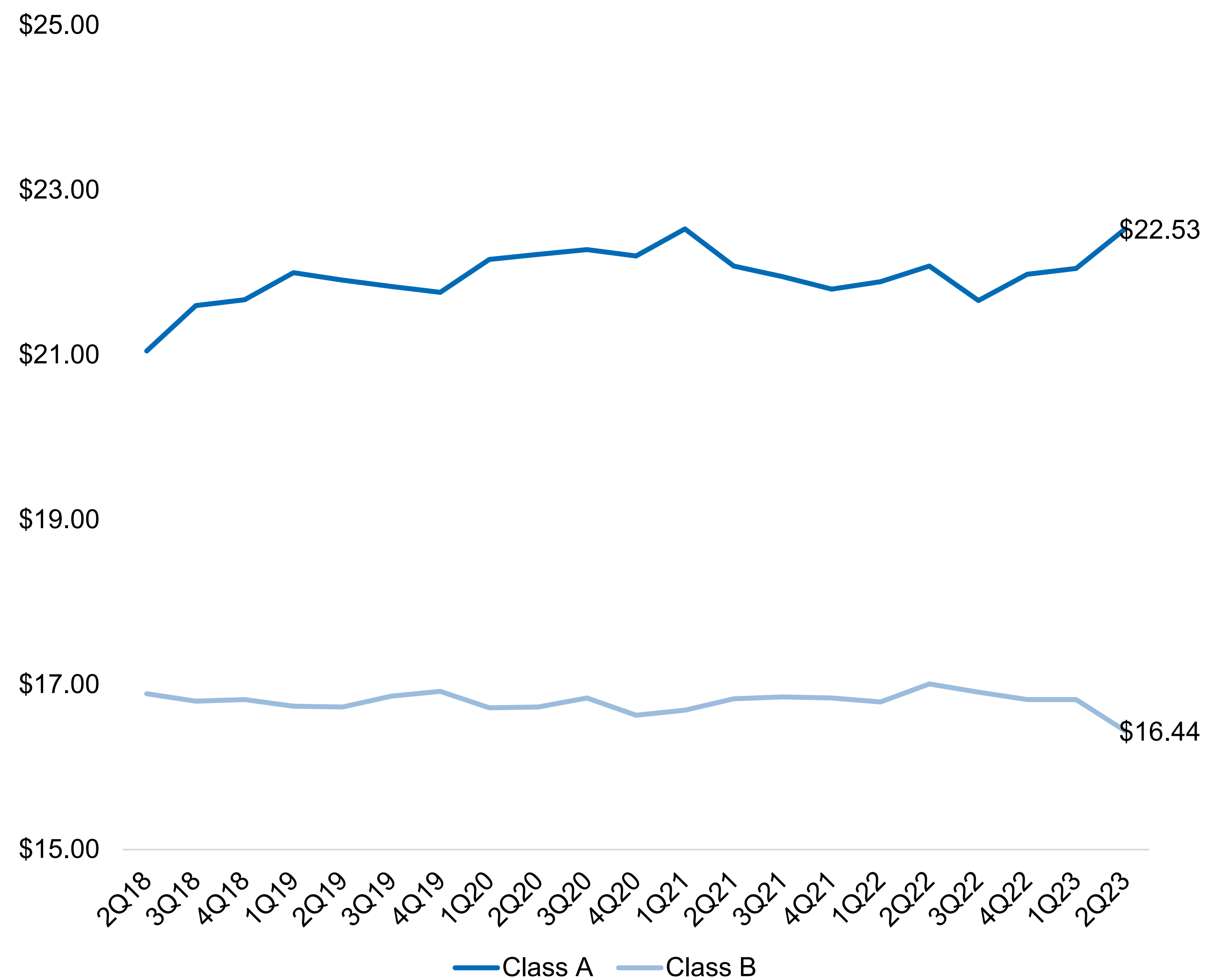


Source: Newmark Research, CoStar

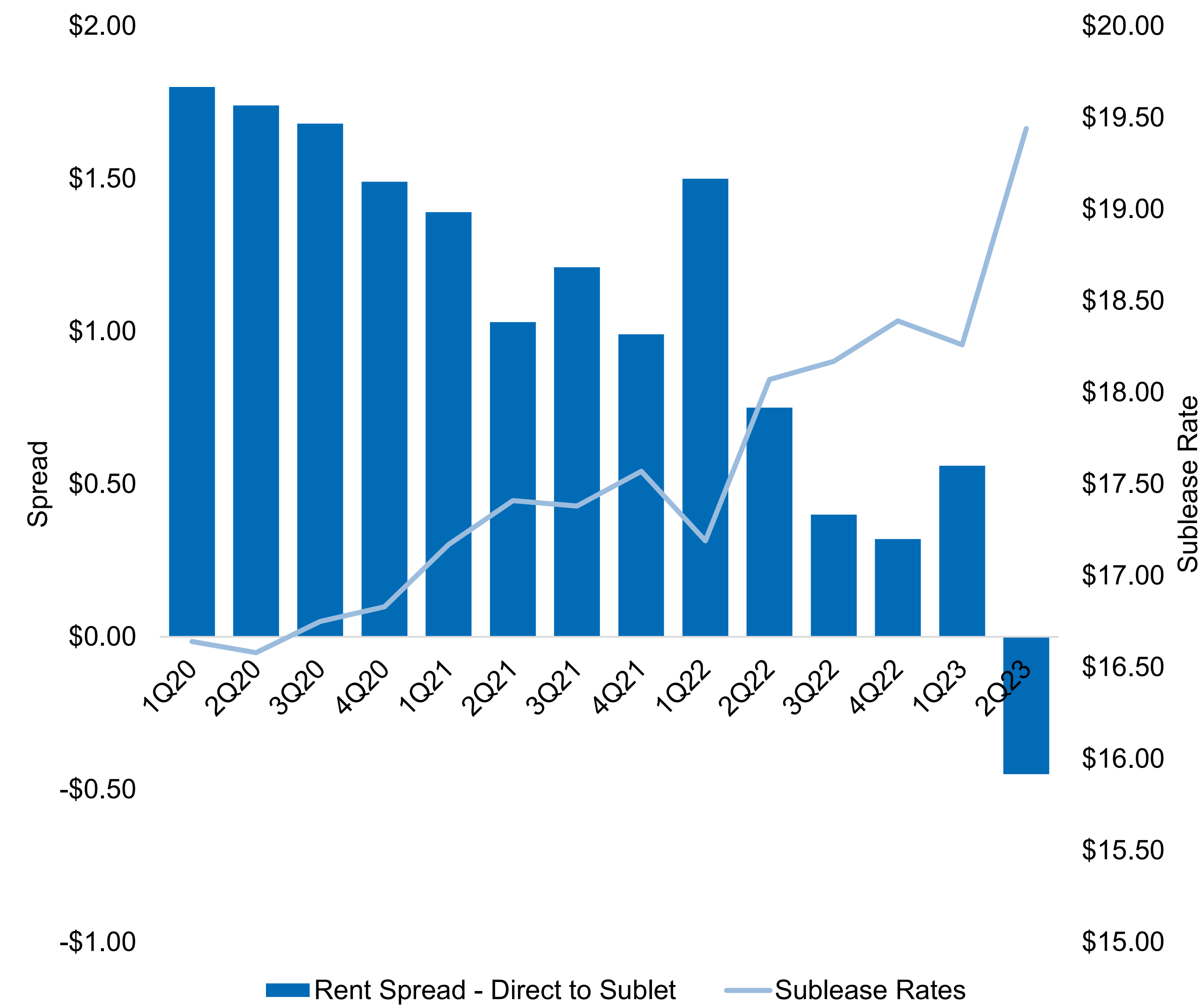
Class A and Class B Asking Rents Relatively Steady While Sublease Rates Climb

The overall market's Class A average asking rental rate of $22.53/SF was an increase of $0.48/SF from the first quarter of 2023, and the Class B average asking rental rate decreased by $0.38/SF to $16.44/SF, widening the gap between Class A and Class B rents. With a couple of exceptions, sublease rents have been steadily increasing over much of the last three years, as companies have shed excess space more. As a result, the spread between sublease space and direct space has shrunk recently.

Class A and Class B Asking Rents



Sublease Rates



Source: Newmark Research, CoStar

Office Leasing Activity Continues to Be Slow

There were very few notable leases within the Cleveland market in the second quarter of 2023.

Notable 2Q23 Lease Transactions

Tenant	Building(s)	Submarket	Type	Square Feet
Sotera Health Services, LLC	9100 South Hills Blvd.	South	Expansion	23,611
This lease expansion took place in one of three buildings in this Broadview Heights office complex.				
BrandMuscle	1500 W. 3rd St.	CBD	Direct Lease	12,880
BrandMuscle's lease at Post Office Plaza in the Public Square section of the CBD represents a significant downsize from its approximate 55,000 SF at 1100 Superior Ave., where its lease expires later this year.				
Cornerstone Family Office	5900 Landerbrook Dr.	East	Direct Lease	8,307
Landerbrook Corporate Center I in Mayfield Heights is located in an office-heavy hub withing the East submarket.				
JP Morgan Chase Bank	1300 E. 9th St.	CBD	Expansion	5,981
With over $11 million in recent renovations, 1300 E. 9th St. is an example of a building owner in Rugby Realty that recognizes that amenities and building improvements are attractive to current and prospective tenants.				

Source: Newmark Research

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