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Orlando Office Insight Report

Q2 2021

AVANT
by AVISON YOUNG

Key takeaways

Economic conditions

- Reopening efforts and steadily rising vaccination rates have enabled the Orlando unemployment rate to rebound from a high of 22.6% to **5.6%,** although work from home strategies still vary widely by company.
- Office-using job losses have totaled **6.9%** compared with 14.2% for other industries' job losses, underscoring the disproportionate impact the pandemic had on the discretionary segments of the local economy.

Recovery rate

- Florida was ranked **#4** in a WalletHub study of the top U.S. states for their rates of recovery, with industries gaining the most jobs over the year including leisure and hospitality, professional and business services, and trade, transportation and utilities.
- While the pandemic has had a considerable effect on Florida's population, its effect on the business economy was lessened (compared to markets like New York and California) as the state has been largely open for the last few quarters, enabling the business base to return to work and begin to move deals forward.

Office demand

- A majority of current leasing activity is comprised of smaller deals under **10,000 sf**, requiring multiple deals to backfill larger floor plates that have been placed on the market.
- Sublease opportunities will continue to come on the market for the remainder of the year, coming primarily from large corporate users looking to downsize their footprints.
- While not a market wide trend, many office tenants are still pushing for shorter term leases if they are expiring soon. That said, the signing of several significant new-to-market deals over the last month is an encouraging sign.

Key takeaways

Office supply

- Direct and sublease vacancy are at their highest point in six years, totaling **13.9%**.
- The sublease market in Orlando remains one of the most saturated in the South, comprised of over **760,000 sf** of space with more on the way. Many listings are opportunistic in nature and listed by tenants who have more space than they require and are not indicative of a tenant in financial distress. The good news is that activity on sublease space has been solid, with over 78,000 sf of a 108,000-sf sublease in Lake Mary already backfilled by two "new to market" tenants.

Pricing trends

- Average base rents have increased by **6.7%** from peak-to-trough due in part to an increased supply of class A space as landlords secured new tenant commitments and lease renewals through favorable lease provisions while keeping rents relatively steady.
- Demand is starting to increase as the business economy gains momentum, employees come back to the office, and tenants that postponed their long-term occupancy strategies re-enter the market.

Capital markets

- Office investment activity has been steady in Orlando, with total transaction volume of **$359.3 million** for the period from Jan 2020 through Jun 2021. The largest sale was DRA Advisors' **$63 million** acquisition of the 280,000-sf 20 N Orange building in the urban core.
- Paralleling other Florida markets, there has been an increase in both the number of deals being brought to market and the corresponding investment interest, however a considerable delta remains between the two as too many investors are chasing too few deals.

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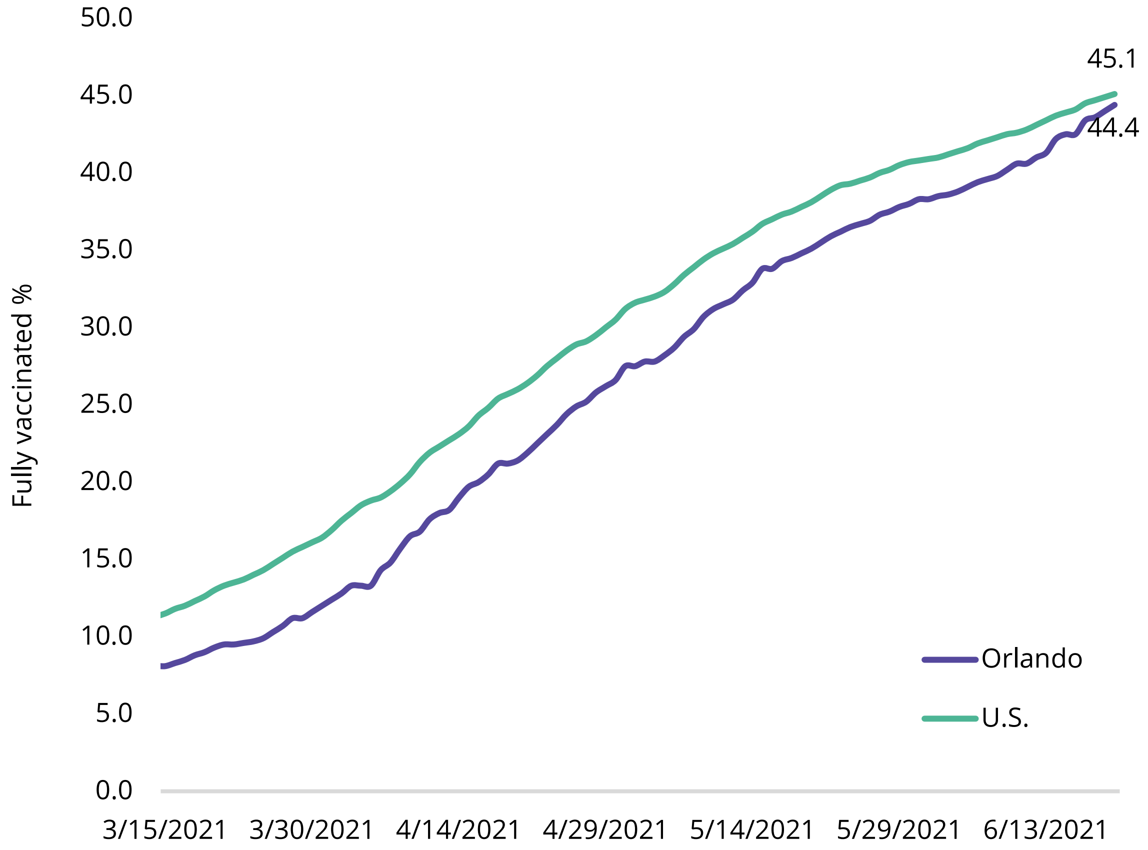
Vaccination rates

44.4%

Share of total Orlando population that is fully vaccinated

Orlando proportionate vaccination rates continue to lag the U.S. average however it has not hindered business reopening efforts and foot traffic in the urban core is increasing.



Source: CDC

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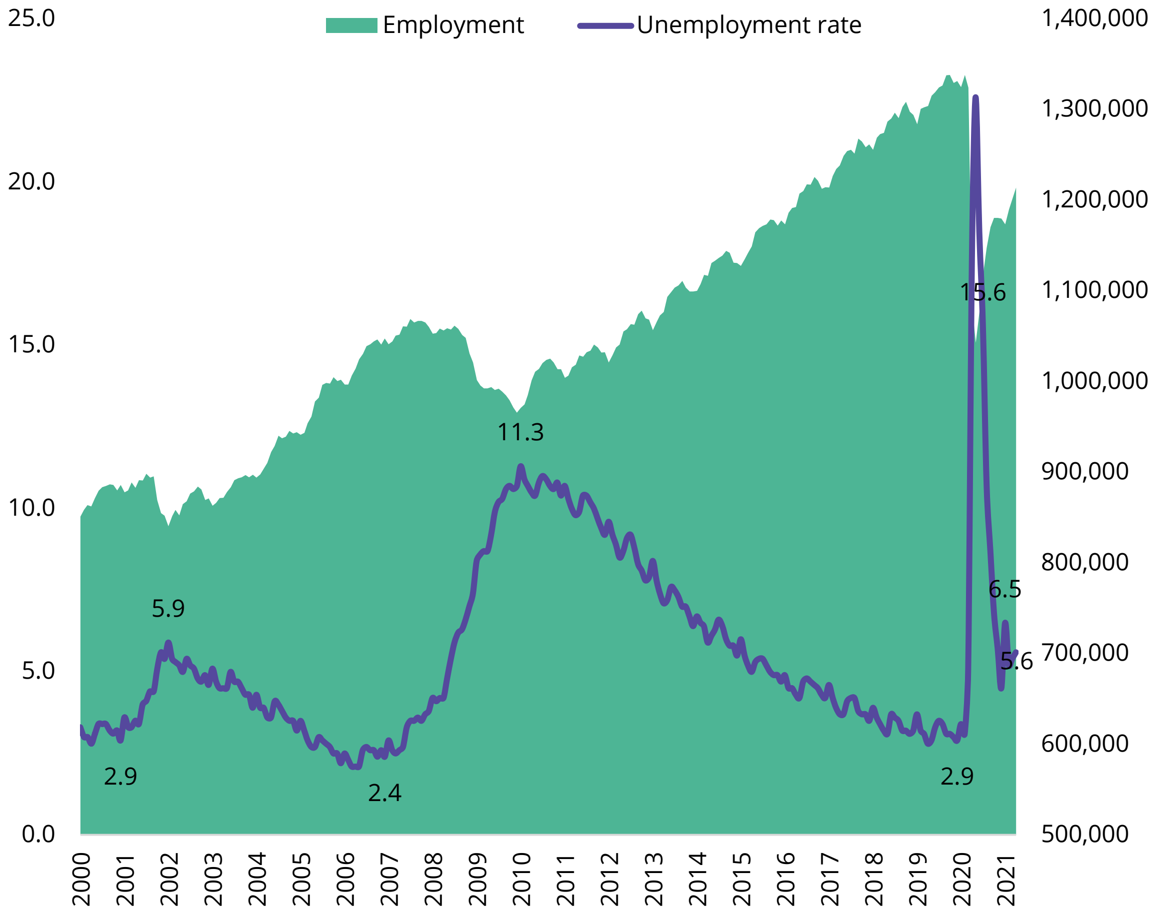
Employment and unemployment rate

5.6%

Orlando unemployment rate as of April 2021, down 1700 bps since the record high reached in May 2020

Historically tightened labor market conditions were halted by the pandemic with nearly 300,000 job losses between February and May 2020. However, reopening efforts have enabled the economy to add over 171,000 jobs since May 2020.



Note: Not seasonally adjusted data.
Source: Bureau of Labor Statistics

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Office-using job gains and losses

-6.9%

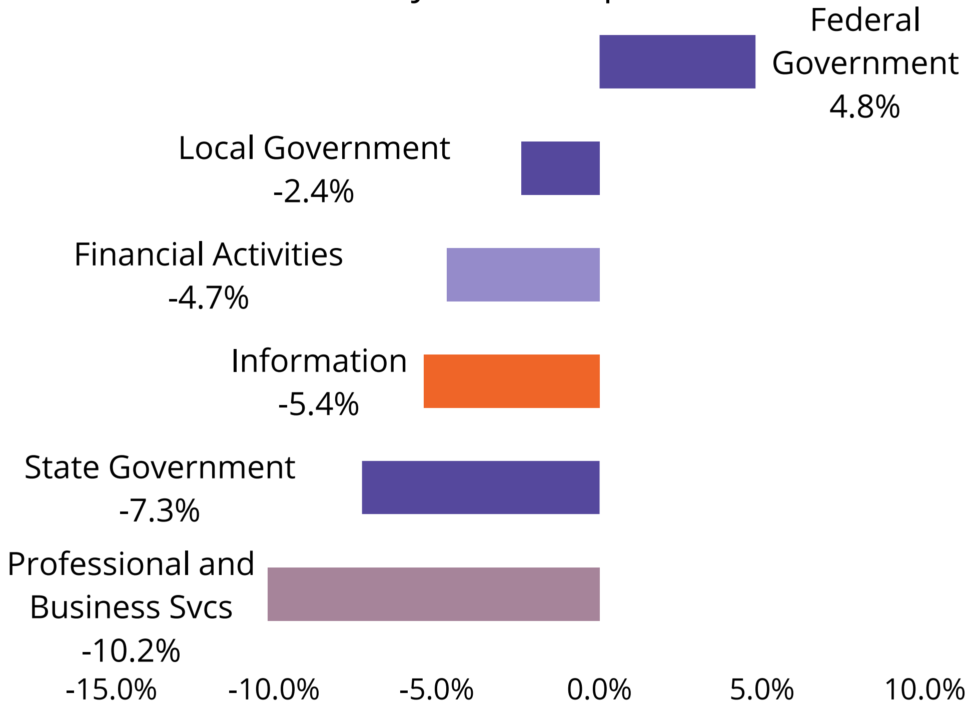
Change in office-using employment during the pandemic

Orlando MSA job losses are down significantly by 14.1% since the start of the pandemic with office-using jobs contracting by 6.9%. As was the case with the global financial crisis over a decade ago, the impact of this recession is expected to be felt in Orlando's office market to some degree for years to come.

VIEW DASHBOARD

Total change in Orlando* job gains/(losses)

February 2020 to April 2021



Note: Not seasonally adjusted data. *Metropolitan statistical area.
Source: Bureau of Labor Statistics

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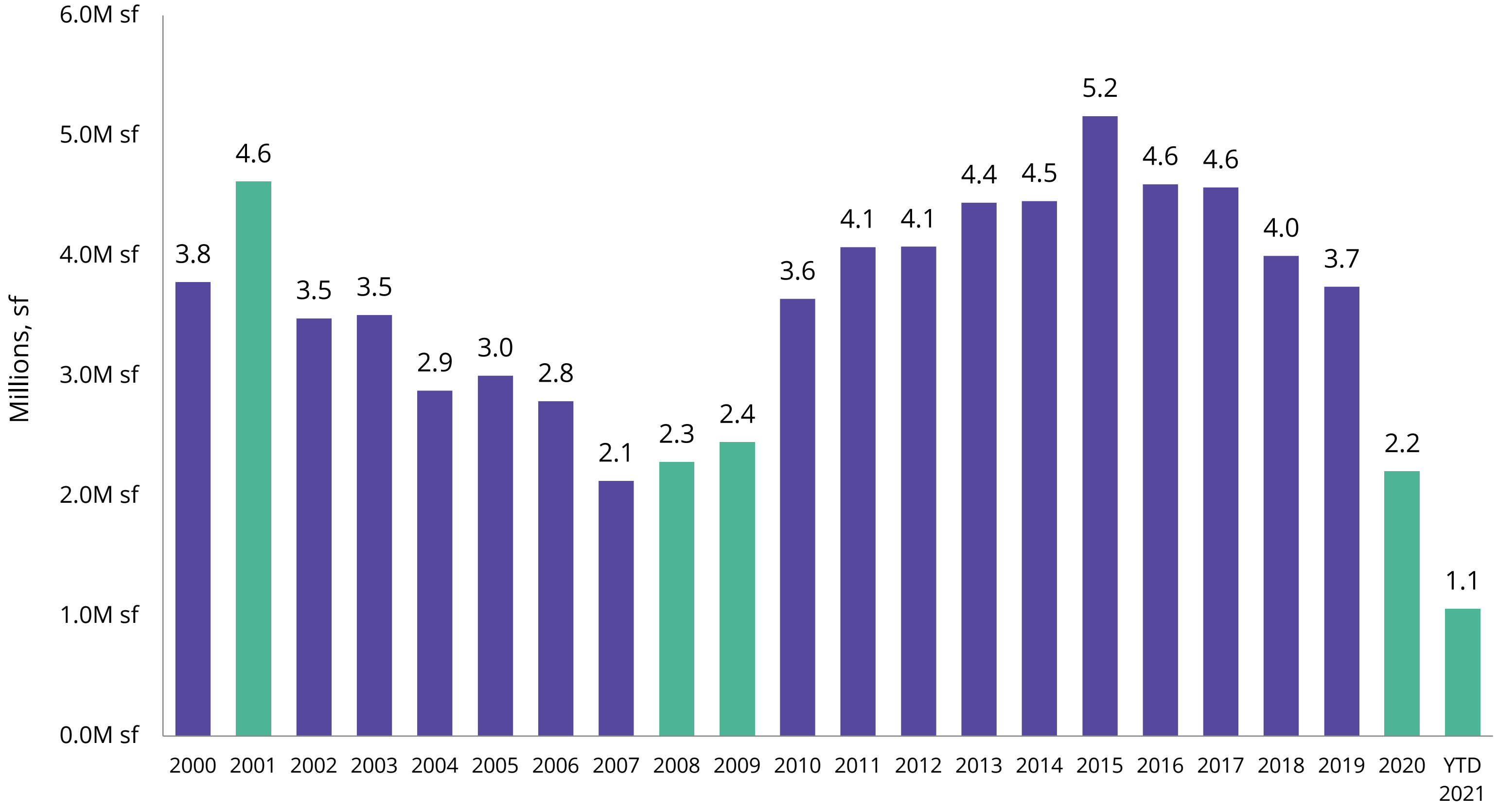
Office leasing activity

48.1%

Year-to-date 2021 leasing activity compared to YE-2020

While leasing activity at the midway point of the year has fallen short of being half of the prior year's activity, leasing interest remains strong and should pick up through the remainder of the year.



Source: AVANT by Avison Young

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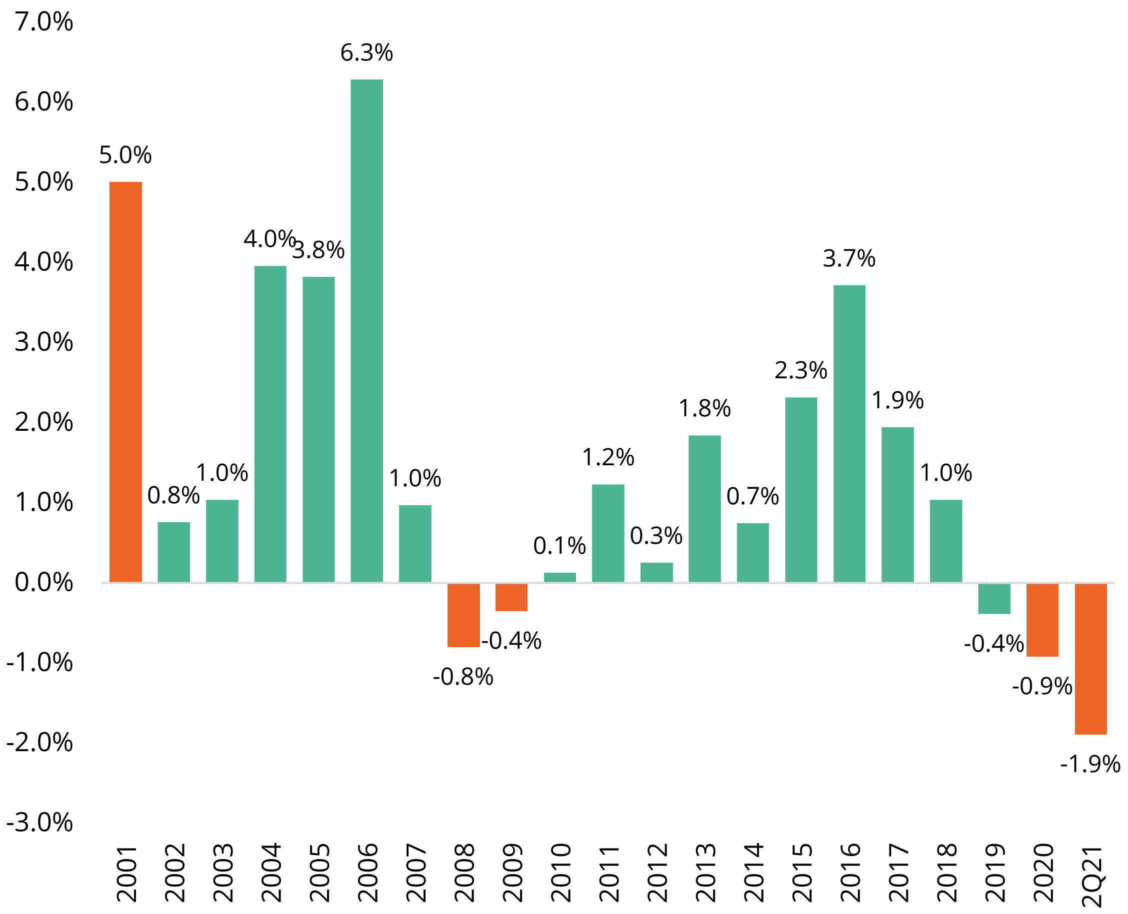
Absorption

-2.8%

Net absorption as a percentage of inventory, 2020 through Q2 2021

Negative absorption from 2020 to 2Q21 has totaled 1.1 million sf, totaling -2.8% of the existing stock. This negative absorption significantly surpasses the low of the global financial crisis (-0.8%).



Source: AVANT by Avison Young

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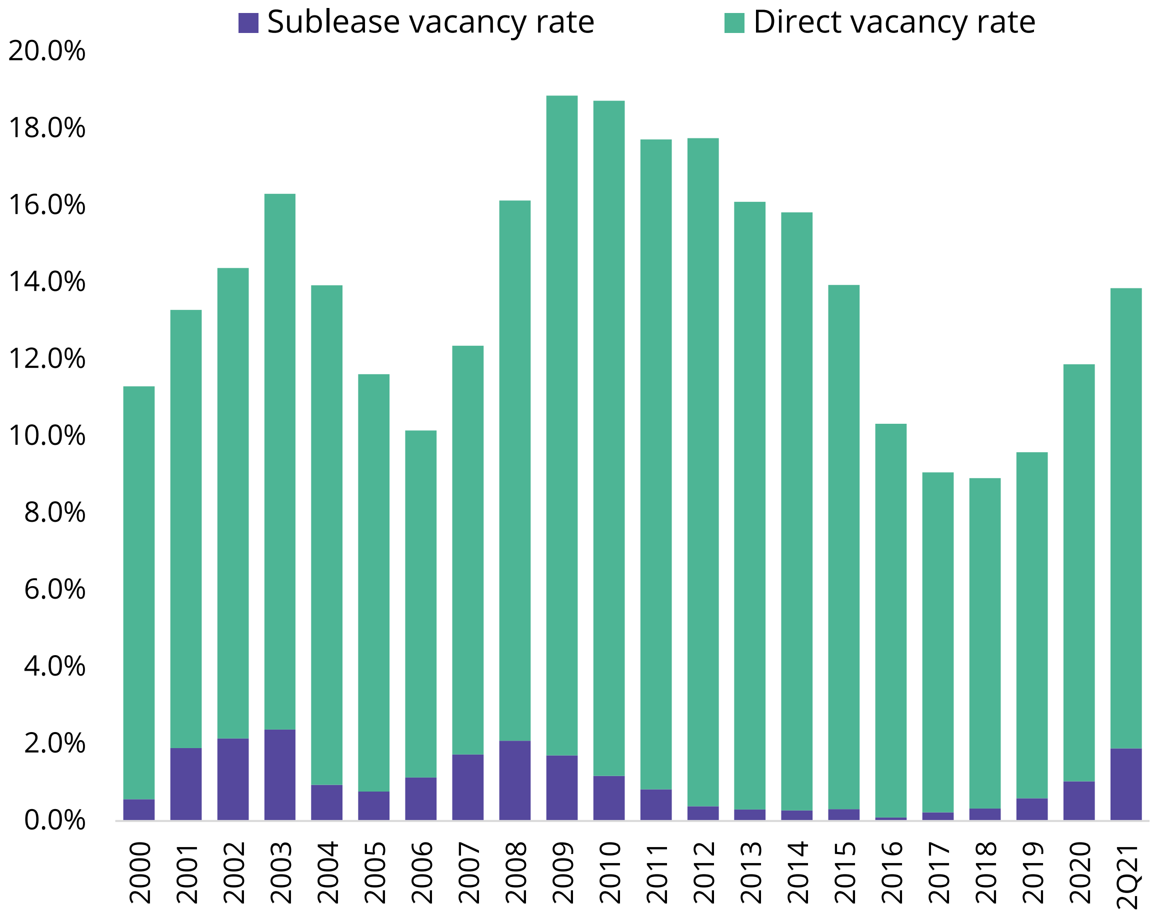
Vacancy rate

13.9%

Current vacancy at the highest level in 6 years

The Q2 2021 vacancy rate is at its highest point since 2015 but remains well below the 18.9% recorded in 2009, which was the highest rate in the previous 20-yr period. Overall rents for the current quarter have increased by 0.8% Y-o-Y.



Source: AVANT by Avison Young

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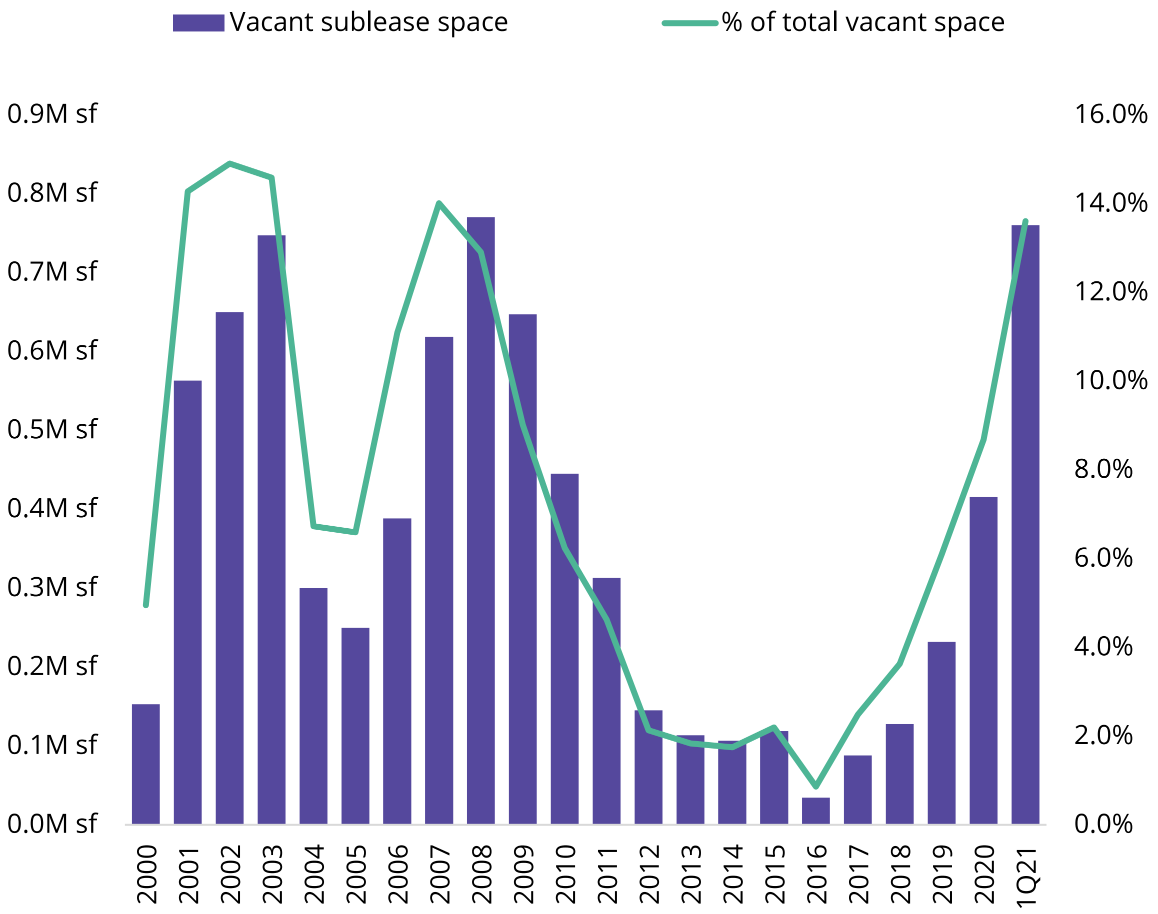
Vacant sublease space

0.7 msf

Sublease vacant space nearing levels of prior recessions

The share of sublease-to-total vacant space of 13.6% is nearing the peak levels seen during the global financial crisis (14.0%), and the early 2000's recession (14.9%).



Source: AVANT by Avison Young

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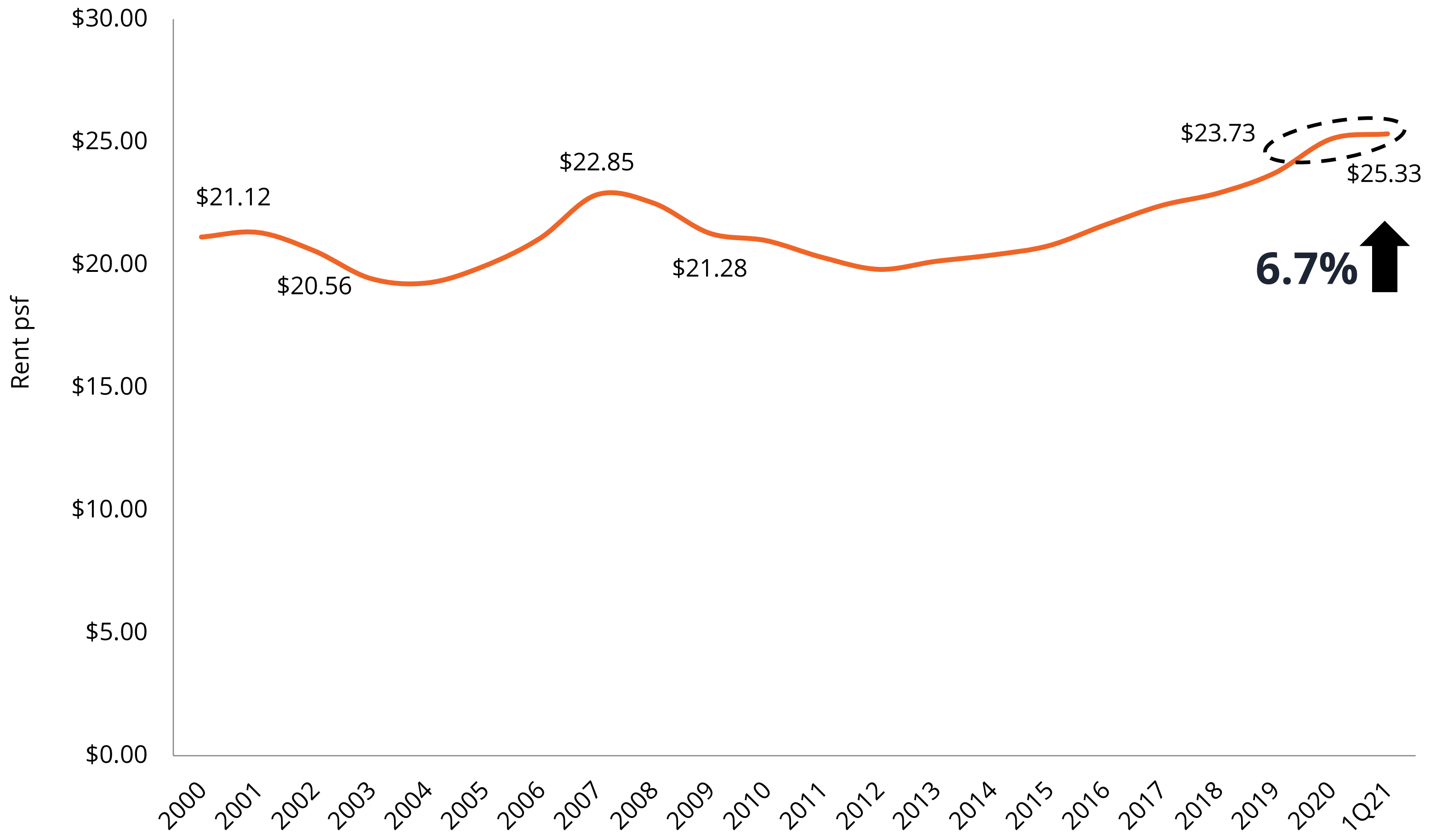
Base rents

6.7%

Peak-to-trough change in rents since the onset of the pandemic

Base rents have increased notably since the onset of the pandemic and the resulting recession due in part to an increased supply of class A space, which is the opposite of what occurred in the prior two recessions.



Source: AVANT by Avison Young

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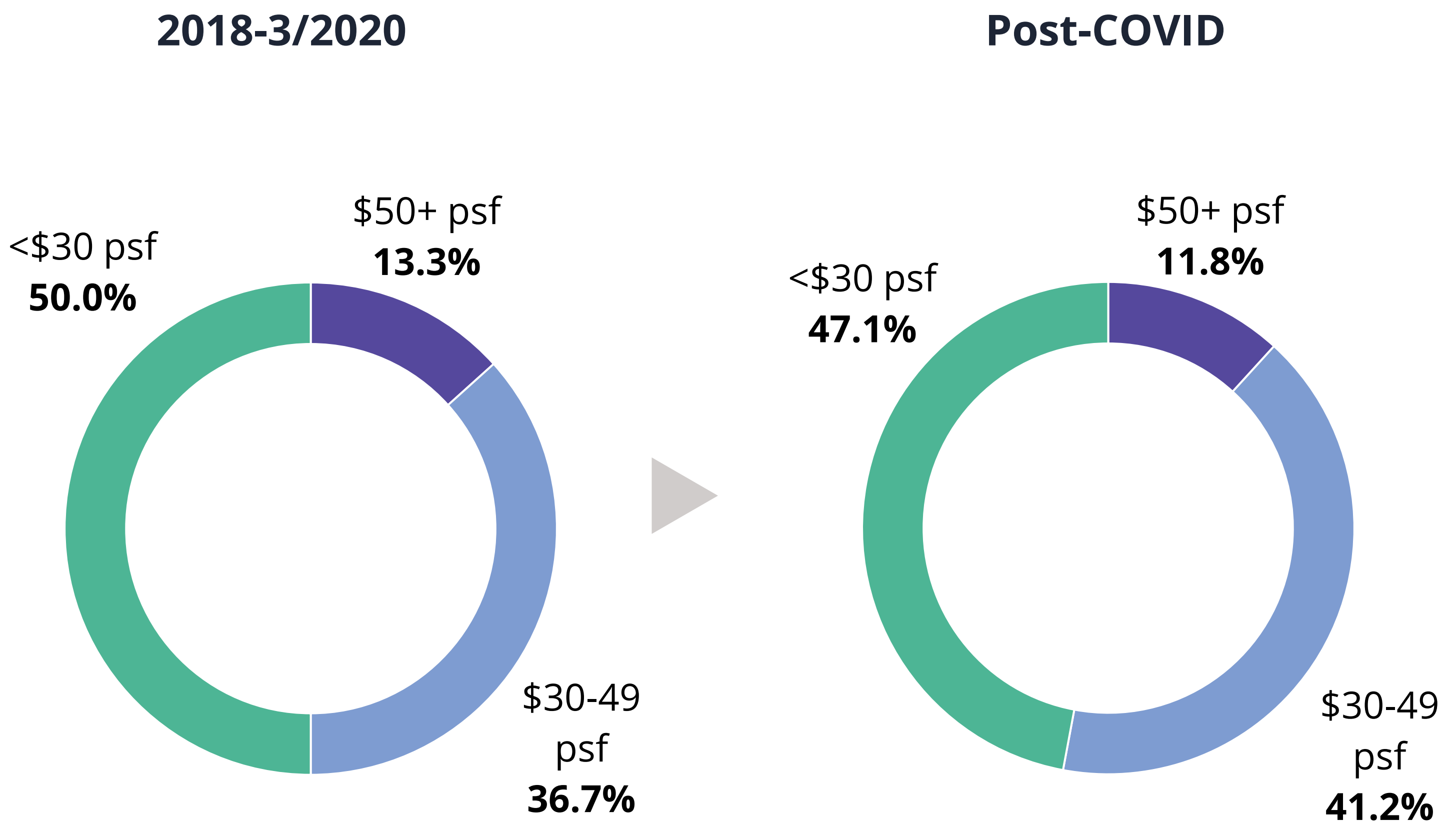
Concession trends pre-COVID vs. post-COVID

11.8%

Number of all class A deals since March 2020 with TI allowances above $50 per sf

While renewals are common and allow tenants time to evaluate their future floor plate needs, some tenants are now more willing to extend deal terms in order to secure higher TI allowances on new deals.



Source: AVANT by Avison Young

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Orlando's construction pipeline

23 properties

proposed or under construction

3.8 msf

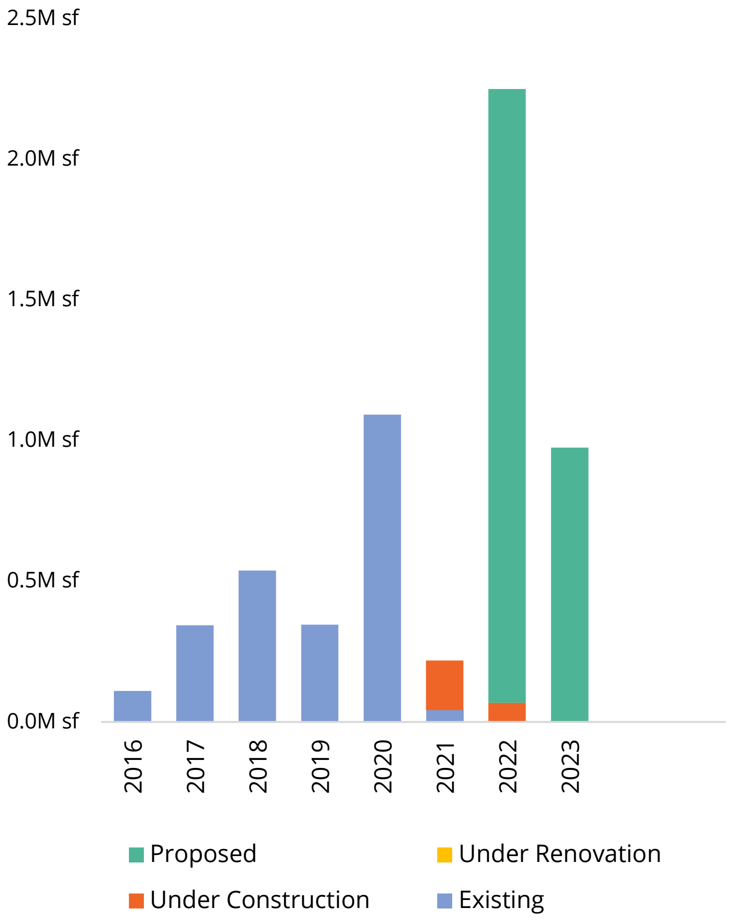
proposed or under construction

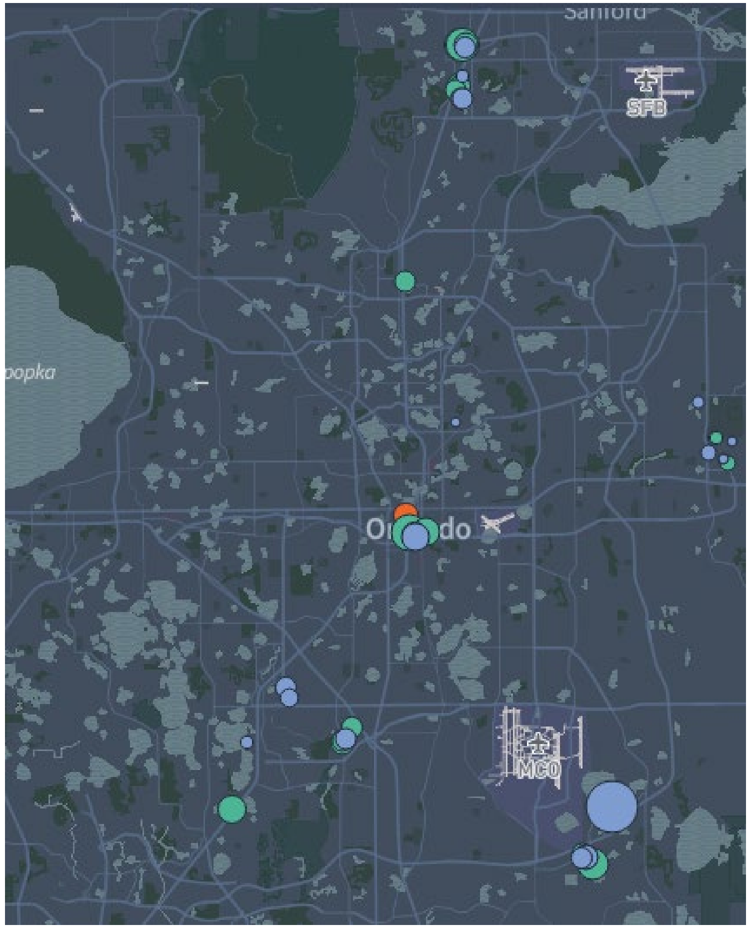
8.9%

share of office inventory

2.4 msf

New construction deliveries in Orlando since 2016





Source: AVANT by Avison Young

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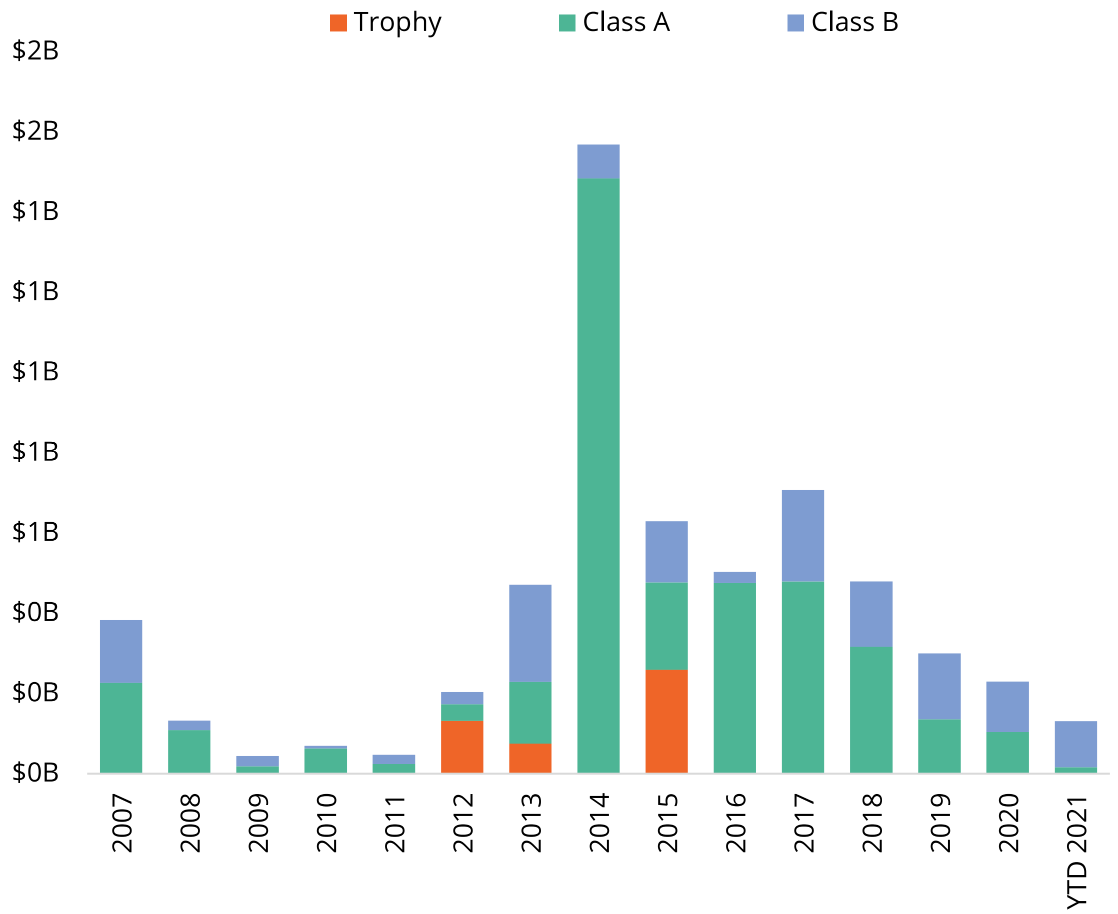
Office investment dollar volume

$359.3M

Orlando office dollar volume 2020 to present

Office sales activity temporarily paused during the pandemic and, as a result, total sales volume from 2020 through year-to-date 2021 remains down 31.4% compared to the prior five-year average dollar volume.



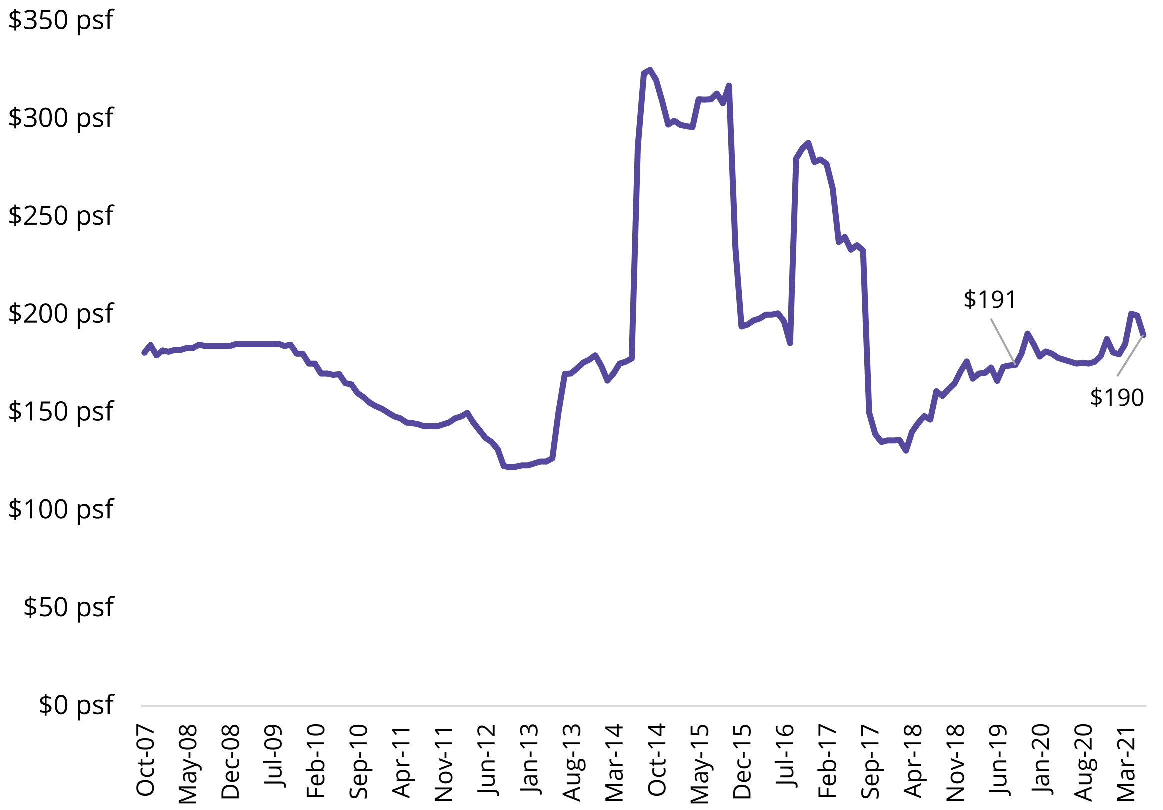
Source: AVANT by Avison Young

Office asset pricing

-0.4%

Orlando office pricing from November 2019 to present

Orlando's office pricing was minimally impacted during the pandemic as investors briefly put sales on hold. As investment activity has begun to pick back up, office pricing has recovered well in 2021, decreasing from $191 psf in November 2019 to $190 psf in June 2021.



Source: AVANT by Avison Young

Looking forward

Here’s what we can expect

- More sublease space is on the way, including 450,000 sf in the University area formerly occupied by Siemens, that will come online in July and will adversely impact an already **saturated sublease market**. Fortunately, that submarket is one of Orlando’s strongest, driven by well-capitalized tech and defense tenants, which will assist in the lease-up of the newly listed space.
- Investment activity is expected to remain steady as a **strong flow of available capital** chases deals in Orlando. Private equity will remain a strong player for deals and a seller’s market will continue to prevail as the delta between the number of deals brought to market and the number of active investors will remain.
- **Office leasing momentum** will build through the end of the year, and the increase in activity will help to offset some of the new space coming to the market. Larger deals will continue to move slowly as companies re-envision their future floor plates, leaving vacant spaces on the market for longer.
- The passage of Florida Senate Bill 50 will have **positive implications for commercial real estate** as it will dramatically cut the state tax portion of the business rent tax from 5.5% to 2.0% once Florida’s Unemployment Compensation Trust Fund is replenished to pre-pandemic levels. While every tenant will save on their overall business costs, considerable cost savings will be realized by larger occupiers in Florida.

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Let's talk

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