BEYOND THE GLOBAL HEALTH CRISIS

Marcus & Millichap

MARKET REPORT *Miami-Dade Metro Area* 2H/20

Pandemic and Lower Taxes to Accelerate Movement to Miami, Though Strong Impact to Tourism Weighing on Economic Growth

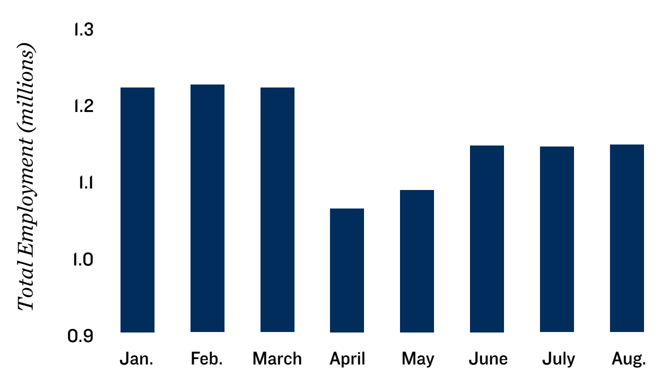
Long road ahead to full recovery of Miami's employment base. The prominent travel and tourism sector in Miami felt the brunt of the pandemic impact as leisure and hospitality employment fell by almost 70,000 positions in March and April. This one sector comprised 42 percent of the 162,000 jobs lost across the metro during that time frame. The unemployment rate rapidly climbed from a record low of 1.8 percent in February to a new high of 14.2 percent in July, though it has since fallen considerably as of August to 7.6 percent with companies steadily bringing back workers. More than 83,000 staffers have been added back to payrolls since May, though the metro faces a long and uneven recovery as this accounts for roughly 52 percent of jobs lost during the lockdowns.

Company relocations to Miami cushion the office market. The pandemic has spawned significant in-migration to Miami-Dade and the rest of South Florida as employers and workers are favoring less density and suburban areas. Some recent announcements have highlighted this trend as Blackstone stated it will open an office in Miami, bringing up to 215 high-paying technology-based positions to the metro. The ability to recruit and retain top-tier talent has helped to diversify the economy with stable growth of financial, professional and tech firms, leading to less reliance on tourism. Lower taxes and a young and educated workforce open the door for other firms to add regional headquarters to the metro, which will help to bolster the office market. Uncertainties still exist, though, with a high volume of aviation and cruise-related tenants facing difficulties.

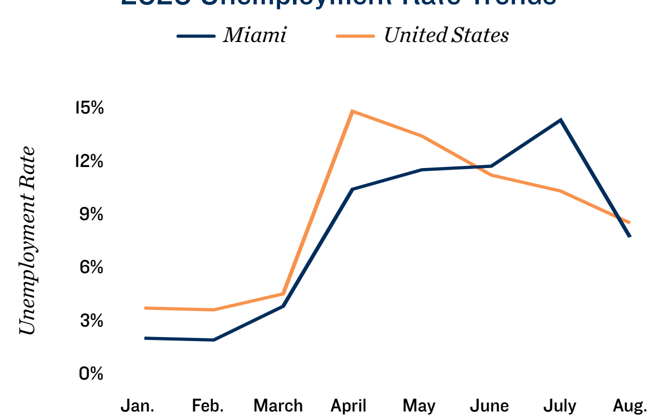
Lifted restrictions on occupancy provide a tailwind for retailers. Disruptions to domestic and international travel have been a hurdle for many Miami retailers that cater to visitors. Reduced spending will be particularly difficult for small businesses that do not have the needed cash reserves, contributing to elevated vacancy rates over the coming year. Store closures do present an opportunity for investors to renovate and upgrade empty space and retenant with retailers more suited for a post-pandemic environment, such as medical services that have increasingly located in strip malls and shopping centers. With Florida at advanced stages of reopening in contrast to other states, lifting occupancy limits for restaurants and businesses, momentum is building a steady recovery for the retail sector.

Migration to South Florida to hold investors' attention. Over the near term, the four main property types still face uncertainties with softening demand for some segments and a robust pipeline of new development. An array of demand drivers remain in place, though, including a growing population, deep talent pool and favorable business climate, which will keep investors active in the search for remaining upside. Investors will continue to target emerging neighborhoods including Wynwood, Little Havana and North Miami Beach, where the transformation of such areas has attracted employers and young professionals. Rezoning has allowed for increased residential and office development, which has led to firms such as Spotify to take up space in Wynwood, where soon it will open its Latin American headquarters.

2020 Employment Trends

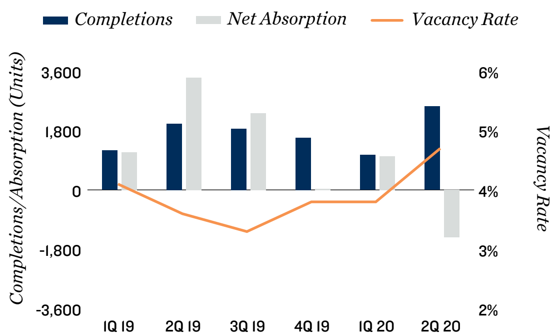


2020 Unemployment Rate Trends

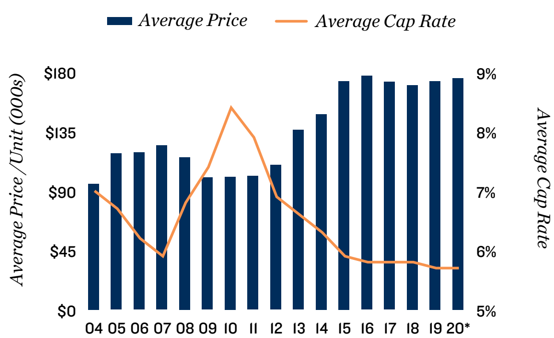


Source: BLS

Apartment Completions and Absorption



Apartment Price and Cap Rate Trends



** Through second quarter*

Sources: Real Page Inc.; CoStar Group, Inc.; Real Capital Analytics

APARTMENT

Areas Outside the Urban Core Sustain Investment Appeal; Development Pipeline Softening Short-Term Operations

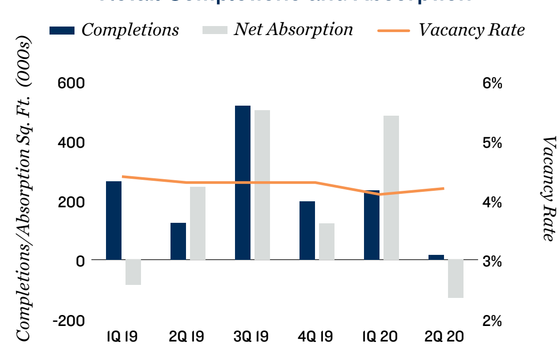
- Deliveries rose sharply in the second quarter with the completion of more than 2,500 units, the second highest quarterly total in at least 20 years. Supply growth over the past year climbed just above 7,000 units.
- Fewer move-ins and a surge in new apartments resulted in negative net absorption of 1,430 units in the second quarter, increasing the market vacancy rate to 4.7 percent, up 90 basis points from the start of the year.
- The average effective rent fell 1.4 percent quarter to quarter at midyear, declining to $1,682 per month. The effective rent in the Class C segment recorded a 2.3 percent gain to $1,223 per month, while Class A rent fell 3.3 percent to $2,166 per month.
- Trading velocity slowed in the second quarter as closing deals became more challenging. Little Havana and North Miami Beach remained prime targets for elevated cap rates and value-add opportunities as initial yields pushed past the mid-6 percent range.
- The average cap rate recorded in Miami-Dade County remained stable at 5.7 percent over the past year, while pricing inched up moderately to average $175,000 per unit.

RETAIL

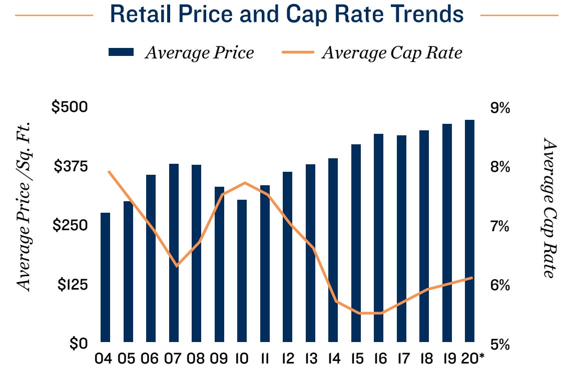
Investment Sales Slowly Return to the Sector; Challenges Remain Ahead for Impacted Businesses

- With many construction sites hitting pause in the second quarter, retail supply growth fell to its lowest quarterly total in more than a decade with the delivery of 16,300 square feet, bringing the four-quarter total to 965,000 square feet.
- The market vacancy rate drifted 10 basis points higher in the second quarter to a still-tight 4.2 percent with a net 129,000 square feet of retail space vacated. Vacancies are likely to rise as forbearance periods end and store closures mount.
- Softening demand for retail space compressed the average asking rent in the second quarter by 2.6 percent to $33.63 per square foot. Rent at multi-tenant properties declined 0.9 percent in the same quarter to $36.05 per square foot.
- Prices recorded over the four-quarter period ended at midyear averaged $468 per square foot, while the average cap drifted 20 basis points higher to land in the low-6 percent band. Single-tenant properties transacted closer to $500 per square foot and registered an initial yield in the upper-5 percent territory.
- Sales activity pulled back in the second quarter with increased challenges in bringing deals across the finish line, though deal flow has since steadily increased with a healthy investor appetite for retail assets in Miami-Dade.

Retail Completions and Absorption



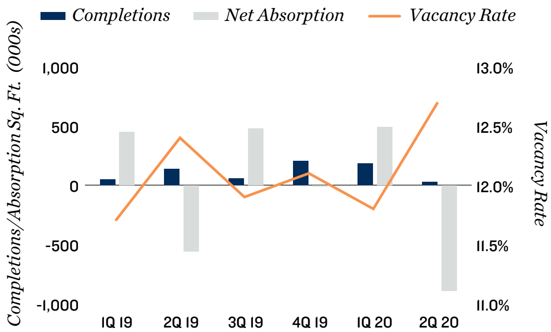
Retail Price and Cap Rate Trends



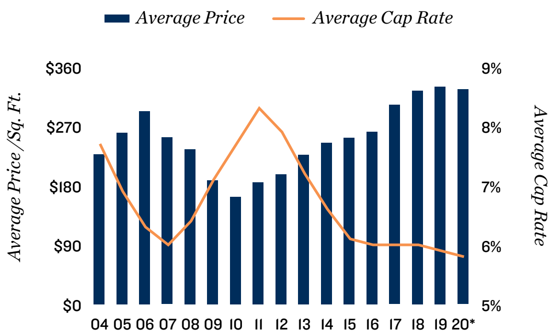
** Through second quarter*

Sources: CoStar Group, Inc.; Real Capital Analytics

Office Completions and Absorption



Office Price and Cap Rate Trends



* Through second quarter

Sources: CoStar Group, Inc.; Real Capital Analytics

OFFICE

Immediate Impact to Leasing Lifts Vacancy; Investment in Medical Office Sustained During Health Crisis

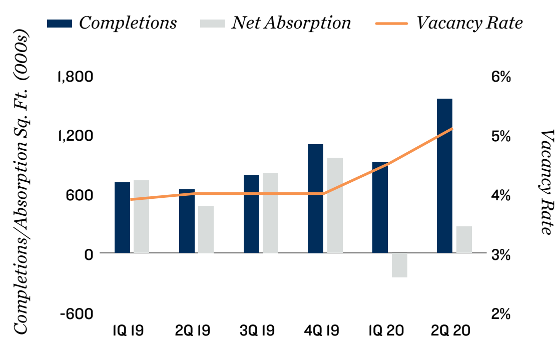
- Just over 27,000 square feet of office space was delivered in the second quarter, bringing the 12-month total to 470,500 square feet. The largest delivery this year is 545 Wyn, which brought 300,000 square feet to the Wynwood neighborhood.
- After hovering just above the cycle low in the first quarter, the vacancy rate rose 90 basis points to 12.7 percent at midyear with net absorption falling to negative 894,000 square feet.
- Rent growth maintained an upward trajectory in the second quarter, climbing 3.8 percent to an average of $36.48 per square foot, though risks remain, which could soften rent gains moving forward. Class A space was leasing for $44.34 per square foot in the second quarter.
- Office properties transacted at an average of $325 per square foot over the yearlong period, holding relatively stable. Initial yields fell into the upper-5 percent area, down 20 basis points from the prior yearlong stretch.
- While transaction activity slowed in the second quarter, investors continued to target medical office properties, leading this segment to comprise a greater share of overall deal flow.

INDUSTRIAL

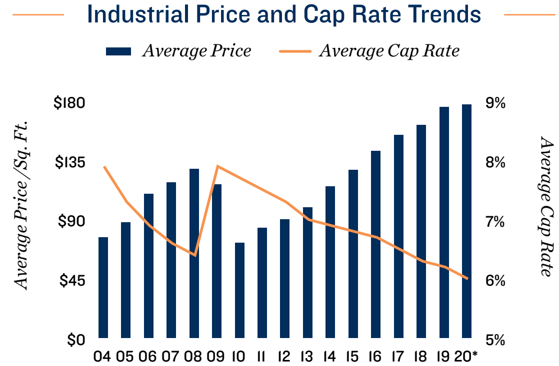
Industrial Properties Less Impacted by Pandemic, Though Long Recovery to Weigh on Growth in the Sector

- The resilience of the industrial sector showed with the delivery of 1.55 million square feet in the second quarter, the strongest quarter of supply growth since the end of 2018. A logistics facility exceeding 530,000 square feet in Miami Gardens was the largest delivery so far this year.
- Net absorption of 264,000 square feet in the second quarter was well below supply growth, lifting the vacancy rate 60 basis points to 5.1 percent. Hialeah and Miami Lakes held some of the lowest rates at 3.8 percent and 3.7 percent, respectively.
- The average asking rent dipped 2.1 percent in the second quarter to $10.66 per square foot. On a year-over-year basis, rents were up 1.1 percent.
- Pricing for recently transacted industrial properties increased to an average of $178 per square foot, while initial yields declined 20 basis points to 6 percent. Hialeah and North Miami Beach remained prime targets of investors, where cap rates can average closer to 7 percent.
- Larger portfolio deals, which sustained momentum in the market in recent years, have become less common, though areas with new and modern space, including North Miami Beach and Medley, will maintain investor sentiment.

Industrial Completions and Absorption



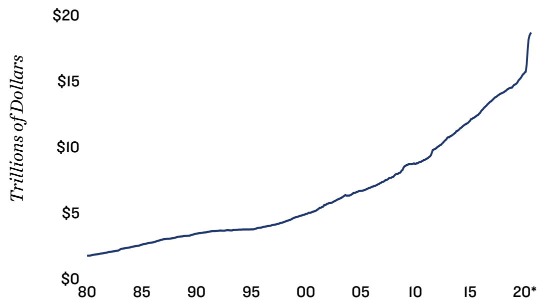
Industrial Price and Cap Rate Trends



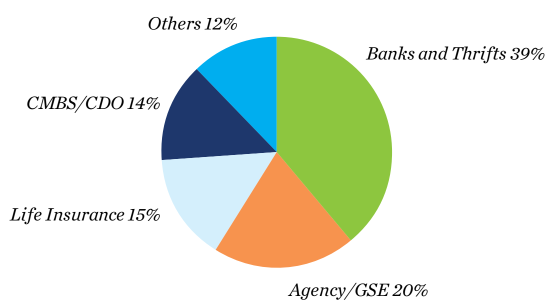
* Through second quarter

Sources: CoStar Group, Inc.; Real Capital Analytics

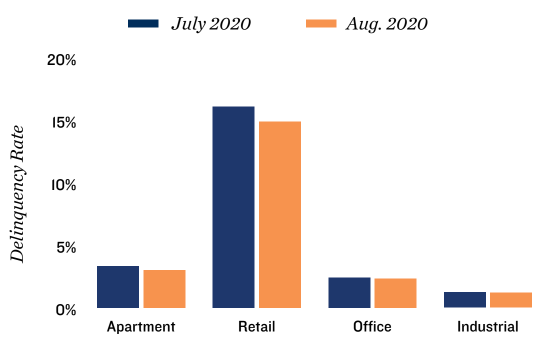
Fed Sharply Increases Money Supply During Health Crisis



Total Outstanding Mortgage Debt**



30+ Day CMBS Delinquency Rate



* Through August

** As of second quarter

Sources: Federal Reserve; Mortgage Bankers Association; Trepp

CAPITAL MARKETS

By TONY SOLOMON, Senior Vice President, Marcus & Millichap Capital Corporation

- **The capital markets are thawing relative to the height of the crisis.** Most lenders have adapted to dispersed working, and more information on the economic damage of the pandemic is affording buyers, sellers, and lenders risk and price clarity for large swaths of the commercial real estate sector. Both property performance and location can impact financing as some areas of the country outperform and the pace of recovery remains in doubt for others. Capital is readily available for assets that perform on or near par with pre-crisis levels, especially industrial assets, which buyers and lenders see as a safe part of their portfolios. Single-tenant retail with national credit tenants are also heavily favored by lenders, followed by grocery-anchored multi-tenant properties. Apartment rent rolls are more heavily examined, though financing remains available from the agencies and banks. Loans are more readily accessible for suburban office, while core buildings are more difficult to leverage. Some lenders continue to operate in the hospitality space, but obtaining financing is challenging.
- **Loan-to-value ratios were already declining prior to the pandemic and average 60 percent.** Freddie Mac is offering rates in the high-2 percent to high-3 percent range for seven-year terms. Debt service coverage is approximately 1.35 times. Life insurance companies will finance below 3 percent for apartments in some cases, and peak at 4 percent for retail. CMBS loans are available, though strict criteria makes deals more difficult to find. Rates bottom in the low-3 percent range for apartment and industrial and rise to 4 percent for office.

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Sources: Marcus & Millichap Research Services; Bureau of Labor Statistics; CoStar Group, Inc.; Federal Reserve; Mortgage Bankers Association; Real Capital Analytics; RealPage, Inc.; Trepp

Price: $250