



YEAR OVER YEAR COMPARISON

CHARLOTTE OVERALL MARKET

	Vacancy	Avg. Rents
Q2 2012	18.89%	\$19.15
Q2 2014	14.57%	\$21.73
Q2 2016	12.35%	\$24.04

Market wide rates up 25% over 4 years with vacancy down 6.63%

SOUTHPARK

	Vacancy	Avg. Rents
Q2 2012	15.93%	\$21.18
Q2 2014	13.53%	\$24.85
Q2 2016	14.90%	\$28.18

Rates are up 33% in 4 years with vacancy down 1%

DOWNTOWN

	Vacancy	Avg. Rents
Q2 2012	15.87%	\$23.18
Q4 2014	10.84%	\$25.21
Q4 2016	9.11%	\$27.69

Rates are up 19% with vacancy is down 6.76%

AIRPORT

	Vacancy	Avg. Rents
Q2 2012	28.95%	\$16.39
Q2 2014	19.33%	\$16.73
Q2 2016	19.16%	\$19.53

Rates are up 20% with vacancy down 9.8%

And So the Story Goes

Charlotte's vacancy rate as of July 2016 was just north of 12%, with an average rental rate of \$24.04/SF. By comparison to some of our rival cities, \$24.04/SF seems like a bargain. However, we have to dissect the average rate in the context of the post "great recession". In 2011, we predicted that the Tenant's upper hand in leverage from 2008-2011 would begin to slowly ease, beginning Q3 2012. In our 2012 mid-year market report, the Charlotte overall average rental rate was \$19.15/SF. Rent concessions for the Tenant were still healthy, with at least one month free per year of term. Tenant upfit allowances were strong and rates for the most part were manageable. In a four-year period, average rental rates have jumped 25%, or 6.25% per year. For those of you that thought a 3%- 3.5% annual rent escalation was high in 2012 when you signed your lease, you actually beat the market by almost double.

Rate increases are even more profound in submarkets such as SouthPark, where rents have climbed 33% in 4 years, increasing by \$7.00/SF on average. This would have to be a supply and demand issue; as Landlords could only increase rates at this pace if there was hardly any space for Tenants to choose from. Right? Wrong! SouthPark's vacancy in 2012 was 15.9%. Today it is 14.9%. As we have detailed in past market reports, our rental rate run-away train is stemming mostly from the investment sales arena. When buildings are sold, the buyer purchases a stream of cash flows paid by Tenant rents. Some of the cash flows are real (locked in by leases). Others are estimated, based on lease-up assumptions. Do you think these cash flows are ever projected to flat line or even decrease throughout a 10 year hold period? Of course not. And so the story goes, that rents will continue to climb and Tenants will continue to pay them. At least, that's the thought shared by some in the Landlord community.

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Landlords and investors aren't completely to blame for this ideology. We are also witnessing a percentage of Tenants, some who choose to be unrepresented, sign real estate deals that shouldn't be signed. Way too much money is being left on the table due to a lack of strategy, process and knowledge of the market. And once a Landlord gets its unprecedented rental rate, the new precedent is set. This is precisely why you now hear the saying touted around Charlotte: "\$30 per square foot is the new \$20 per square foot." Now, does this mean that all higher rent deals are bad for the Tenant? Absolutely not. For example, most Landlords who deliver new construction can only negotiate so far on their rental rate, due to lender requirements. And, a percentage of the Tenant field only wants the best and is willing to pay premium rental rates. That's perfectly fine when image is a cornerstone of the business. But, the principles of sound real estate deals do not change, even with higher rental rates. A thorough understanding of the lease variables is perhaps now more important than ever. Total transaction costs are what we are fighting for, not just the rental rate.

NOTABLE INVESTMENT SALES TRANSACTIONS

Building	Submarket	Price	Price/
One Wells Fargo Ctr	Downtown	\$284,000,000	\$284
SouthPark Ctr 1 & 2	SouthPark	\$44,000,000	\$190
Morrison/Roxborough	SouthPark	\$33,500,000	\$188
Fairview Ctr 1 & 2	SouthPark	\$33,750,000	\$186

Construction Costs

There is another phenomenon contributing to the run-up that deserves special attention. Not too long ago, general contractors were folding up shop. The field had become too crowded and profit margins of 3% and 5% were unsustainable. Today, construction demand is at its highest level in years. Profit margins for interior office upfits are now in the 10%-15% range. Modest Tenant upfits that were built for \$25/SF in 2014, are now \$30/SF-\$35/SF. Upfits in the \$60/SF- \$70/SF range, once reserved for law firms and the like, are now common, especially for smaller Tenants, who get little to no benefit from economies of scale.

The major hurdle in real estate transactions today is that Tenant Improvement (TI) allowances have not increased commensurate with rental rates and construction costs. Landlords today are expecting Tenants to pay increased rental rates, and to fund upfit costs to cover the delta between the true costs to build the space out and the TI allowance. Additionally, we are finding that some of the newly constructed buildings are not delivering the shell in the same condition as in years past. A common practice for Landlords has historically been to stack the ceiling grid, tile and lights on the floor of the shell office space. Variable Air Volume (VAV) boxes were also placed throughout the space to regulate air flow and temperature from the main building HVAC system. These "above ceiling" costs were many times funded in the building shell price, and not passed through to the Tenant to be used against the TI allowance. Today, even with the increased construction costs and elevated rental

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rates, some owners are choosing to deliver the space with no ceiling and minimal VAV's, which easily adds another \$10/SF to the upfit costs out of the gate. While some of the larger Tenants, and those that are flush with cash, may be accustomed to funding a portion of the upfit, the majority of Tenants continue to resist the notion of funding the buildout of a space they do not own.

Tenant Advice

With this unprecedented real estate market, now more than ever, Tenants need to align themselves with the best, most competent representation. Achieving great deals for Tenants still exists, it just takes more time, more effort and a more thorough education of the market. Sophisticated Tenants with sophisticated representation can be in the driver seat, assuming a proven process is implemented to achieve the goal. Give yourselves plenty of time to make a decision. If your lease is up in two years, get out in front of it by 18 months. And, be willing to think outside of the box. In an arena that may seem rigid and one dimensional, we are actually finding that all Landlords are not like minded. Some are actually very creative. Approach your next lease deal with a win/win mentality.

You will likely be impressed by the results.

NEW OFFICE DEVELOPMENT

Development	Submarket	Developer	Size	Speculative	Anchor Tenant	Delivery
Tryon Place	Downtown	Crescent Communities	715,000 SF	No	TBD	Q2 2018
300 South Tryon	Downtown	Spectrum Properties	632,385 SF	No	Babson Capital	Q2 2017
Portman Plaza	Downtown	Portman	350,000 SF	No	None	Q2 2017
500 East Morehead	Midtown	Beacon Partners	180,000 SF	Yes	None	Q4 2016
Capitol Towers	SouthPark	Lincoln Harris	236,250 SF Phase II	Yes	None	Q3 2017
Brigham Building/ Ballantyne	Hwy 51/SE	Bissell	287,507	Yes	None	Q4 2016
Waverly Corporate	Crownpoint	Childress Klein	154,000	Yes	None	Q3 2017
3130 Oak Lane	Airport	Gulf Corp.	90,000	Yes	None	Q3 2017

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CHERRY & ASSOCIATES
the office tenant rep experts

Charlotte Office Market Report August 2016

MARKET	Inventory/SF	Net Absorption YTD (SF)	Gross Absorption YTD (SF)	Direct Vacant SF	Direct Vacant %	Sublet Available SF	Total Available SF	Total Available %	Direct Gross Average Rent	Sublet Gross Average Rent	Gross Quoted Rents (Range)	SF Delivered YTD
CHARLOTTE	51,733,033	258,113	2,398,006	5,726,640	11.07%	660,826	6,387,466	12.35%	\$24.04	\$21.42	\$11.00- \$35.00	-
Submarkets												
Southpark	4,268,163	26,824	229,525	521,656	12.22%	114,484	636,140	14.90%	\$28.18	\$22.14	\$15.00 - \$34.00	-
Downtown	18,125,197	174,256	626,755	1,433,000	7.91%	217,354	1,650,354	9.11%	\$27.69	\$26.14	\$18.00 - \$35.00	-
Midtown	2,708,003	94,790	183,065	104,636	3.86%	47,836	152,472	5.63%	\$26.94	\$23.53	\$17.00 - \$33.50	-
Airport	8,726,597	(179,942)	458,079	1,562,882	17.91%	109,520	1,672,402	19.16%	\$19.53	\$16.49	\$13.50 - \$25.00	-
Highway 51/ Southeast	6,086,085	32,006	347,717	714,118	11.73%	47,897	762,015	12.52%	\$25.68	\$19.56	\$16.75 - \$32.50	-
North	3,135,383	101,839	159,228	337,370	10.76%	21,089	358,459	11.43%	\$19.69	\$15.00	\$13.25 - \$25.00	-
University	4,770,710	(28,569)	214,443	498,911	10.46%	72,915	571,826	11.99%	\$19.54	\$17.27	\$16.50 - \$22.50	-
Matthews/ Crownpoint	1,332,088	49,683	81,416	278,526	20.91%	17,052	295,578	22.19%	\$18.08	\$18.00	\$14.00 - \$24.00	-
Cotswold	224,401	1,492	10,377	11,532	5.14%	-	11,532	5.14%	\$25.51	-	\$19.50 - \$28.00	-
Park Road	854,966	(13,502)	44,642	111,891	13.09%	-	111,891	13.09%	\$20.12	-	\$12.00 - \$31.25	-
East	1,501,440	(764)	42,759	152,118	10.13%	12,679	164,797	10.98%	\$13.28	\$15.00	\$11.00 - \$16.00	-
SC TOTALS	1,544,386	10,723	155,160	186,351	12.07%	153,140	339,491	21.98%	\$19.57	\$14.49	\$13.50- \$26.50	-
SC Border Submarkets												
Lancaster County	549,023	462	123,537	65,499	11.93%	126,793	192,292	35.02%	\$19.41	\$12.00	\$14.00- \$24.00	-
York County	995,363	10,261	31,623	120,852	12.14%	26,347	147,199	14.79%	\$19.66	\$26.50	\$13.50- \$26.50	-