BEYOND THE GLOBAL HEALTH CRISIS

Marcus & Millichap

REGIONAL REPORT SOUTH

SUMMER 2020

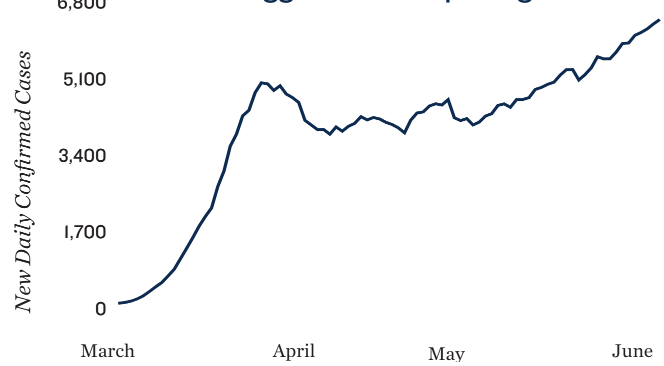
Aggressive and Flexible Reopening Strategies Bolster Southern Markets' Prospects as Local Economies Regain Traction; Recent Uptick in Cases Presents Risk

South positioned for rapid recovery barring second wave. Most Southern states largely avoided the worst of the health crisis before adopting flexible and early reopening plans that could pay dividends for the local economies. Assuming a recent flare-up of the virus does not force businesses to close again, the aggressive relaxing of lockdown policies has the potential to save a greater number of small businesses relative to much of the nation. Notably, the resumption of a higher percentage of business activity before most loans made through the Payroll Protection Program expire maximizes the popular government program's effectiveness across many Southern states. As a result, commercial real estate fundamentals in the South could face lower hurdles as the economy recovers.

Some metros far ahead of nation will attract investors. Many of the smaller markets where the global health crisis has thus far had a lower impact are moving forward more quickly, supporting an abbreviated path to economic normalcy. Charlotte and Nashville lead this group largely due to the strength of the local markets prior to shutdown orders. In Nashville, for example, Amazon had already announced plans to hire more than 5,000 workers and it could bolster those numbers in the coming year. Although neither market is expected to recoup all the positions lost during the pandemic by year end, the overall downside in employment is mitigated relative to the national average. The attractive yields and reduced uncertainty present before the health crisis should bring investors back into the market ahead of areas where economies are slower to open.

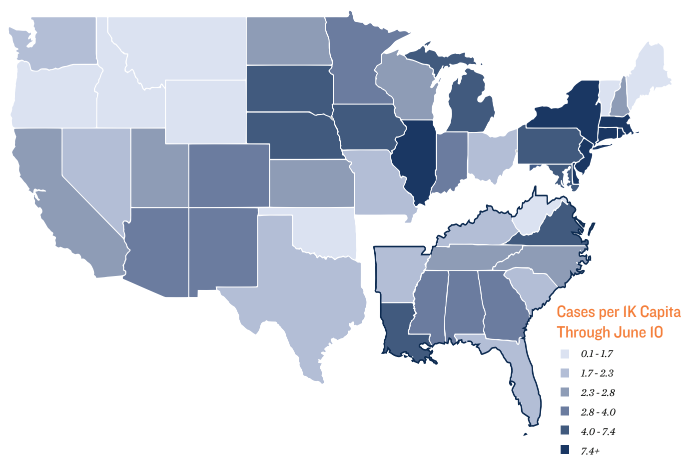
Downside risks in some markets unavoidable. Orlando has one of the most uncertain paths forward due to the metro's reliance on the tourism sector. Prior to the health crisis, Orlando welcomed the most visitors in the U.S. annually, and 20 percent of the local jobs were in the leisure and hospitality sector. The consequences of shutting down the major theme parks cloud the short-term outlook, though local tourism should regain traction as reopening plans unfold. Disney World is scheduled to begin reopening in phases by July 11, and the financial strength of the parent company will dampen the long-term impact. Other markets that face elevated risk include Miami and New Orleans. The former has high population density while an above-average outbreak in New Orleans following Mardi Gras prevented the city from adopting an aggressive reopening timeline.

Rising COVID-19 Cases Test South's Aggressive Reopening*



Attractive Cap Rates in Growth Markets Lure Investors

Market	Apartment	Multi-Tenant Retail	Office	Industrial
Atlanta	5.9%	7.7%	7.3%	7.1%
Charlotte	5.9%	7.2%	6.9%	6.7%
Fort Lauderdale	5.9%	6.3%	6.8%	6.0%
Jacksonville	6.5%	7.3%	8.0%	7.6%
Miami	5.6%	6.3%	5.8%	6.0%
Nashville	5.8%	7.3%	6.5%	7.0%
Orlando	5.5%	7.2%	7.5%	6.8%
Tampa-St. Petersburg	6.4%	7.2%	7.4%	7.1%
West Palm Beach	6.4%	6.8%	6.5%	6.7%



** Seven-day moving average; March 15-June 10*

Sources: State and local health departments and hospitals; The New York Times

Several Southern Markets Among Leaders in Recovery Barring Second Shutdown

Shorter **Economic Downturn** *Longer*

Stronger **Economic Recovery** *Weaker*

Short Downturn/Strong Recovery

- V-shaped economic recovery
- Fewer new cases support phased reopening over the summer
- Government stimulus enables companies to rehire workers
- Commercial property construction projects suffer minor delays
- Investors and lenders resume activity after brief uncertainty period

Extended Downturn/Strong Recovery

- Extended U-shaped economic recovery
- Prolonged business closures accentuate economic costs
- Additional federal stimulus key to boosting consumer spending
- Health concerns extend delays of projects that have broken ground
- Liquidity constrained during shutdown, limiting investment activity

Short Downturn/Weak Recovery

- ✓-shaped economic recovery
- Economy reopens but people remain cautious of contagion
- Constrained corporate budgets limit rehiring, lower spending
- Projects in planning stages are reevaluated
- Investors focus on stabilized or resilient assets in populated areas

Extended Downturn/Weak Recovery

- L-shaped economic recovery
- Lack of health solution keeps some businesses closed late into year
- Extended period of high unemployment notably curbs spending
- Both active and planned development projects face delays
- Investors hold a long-term perspective, fewer listings come to market

Short Downturn/Strong Recovery

V-shaped recovery possible for significant share of commercial real estate. The national outlook brightened in May as job growth soared well beyond expectations, providing evidence that businesses and consumers are anxious to reignite the economy. Southern cities with business-friendly climates should reap the benefits of a rapid expansion, particularly as some coastal cities proceed with a more cautious approach. Strong local markets, including Nashville, Charlotte and Atlanta, are best positioned to take advantage of a V-shaped recovery. Among investment real estate, industrial properties and apartments across the region could rebound quickly if reopening proceeds unimpeded. Metros that rely heavily on tourism are the least likely to follow this economic path.

Short Downturn/Weak Recovery

Possibility of checkmark-shaped recovery elevated. Reopening resulted in the addition of millions of jobs to payrolls, though the number of permanent closures remains in doubt. Under this scenario, Southern businesses will resume operations quickly, though consumer demand will be insufficient to return local economies to previous levels for an extended period. Additional stimulus could be necessary to avoid the slow-growth pattern witnessed following the last downturn, including support for small businesses that are incapable of handling operations under social distancing.

Extended Downturn/Strong Recovery

A U-shaped recovery possible if health crisis persists. Swift reopening of local economies comes with additional risk of overwhelming local healthcare networks, requiring businesses to close. Additionally, large gatherings may result in a flare-up in COVID-19 cases, encouraging local leaders to tighten safety protocols temporarily. As a result, a prolonged shutdown until a medical solution is identified and distributed is possible across the South. However, the relatively dispersed population base should dampen the likelihood of this scenario. Also, an extended downturn might encourage workers in high-cost markets to migrate to low-cost Southern metros as technology firms increase remote work flexibility and low interest rates bolster housing demand.

Extended Downturn/Weak Recovery

Some markets face possibility of protracted recovery. The impact on tourism is the most significant wild card relative to this scenario. If Disney World and Universal Studios have trouble reopening and attracting park visitors, the implications to Orlando's economy could be significant. Other Florida markets are also at risk due to an above-average reliance on visitor spending. Jacksonville, meanwhile, was among the last markets to emerge from the previous downturn, though that scenario is unlikely to be repeated given the nature of the current recession.

Renters Eye a Move to the More-Affordable South Following Global Health Crisis; Apartments Well Positioned for Near-Term Strength

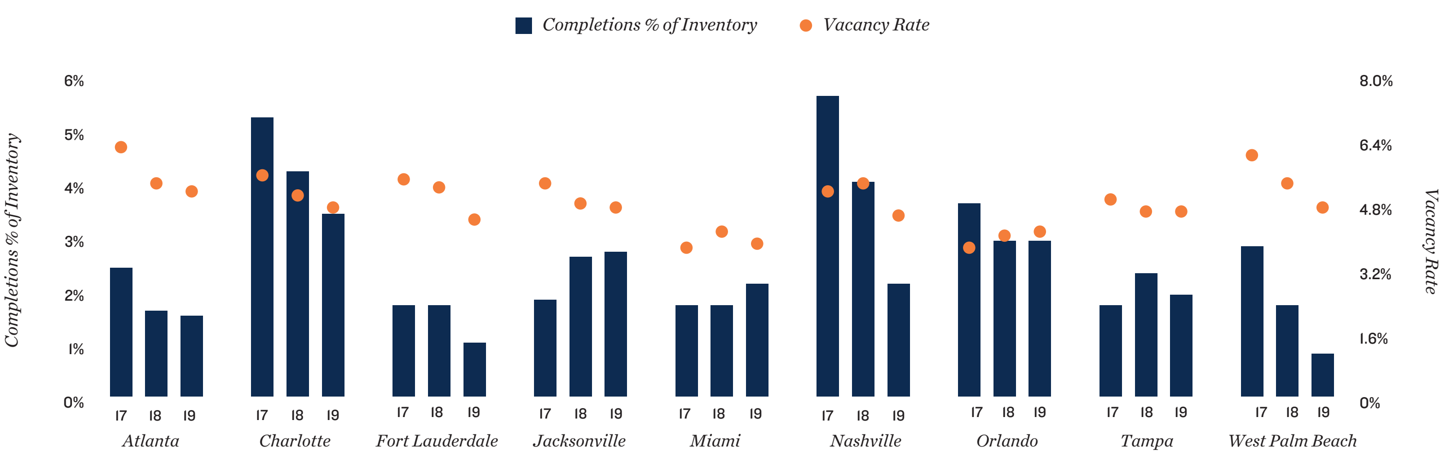
Less-strict eviction policies provide flexibility. Most Southern states have echoed timelines similar to those set forward by the federal government with regard to handling tenants behind on rent. Several states extended protections for renters beyond the federally mandated properties, while governors and courts have frequently pushed timelines as conditions warrant. Although moving timelines can result in uncertainty for apartment owners and tenants, balancing the needs for both groups should maximize apartment performance. Florida currently has the longest eviction moratorium in the region, extending to July 1. Other states are already proceeding with evictions, though owners and tenants have shown a willingness to cooperate before proceeding with formal evictions.

Dispersed working practices bolster opportunities for apartment operators. As companies experiment with dispersed workforces, including Google, Facebook and Twitter, the prospects for new tenants in Southern metros will increase. Markets with a vibrant downtown may attract millennials that are able to work from home. Despite Facebook announcing pay cuts for those who choose to work from home, the attractiveness of Nashville, Charlotte and other metros should be sufficient to siphon renter demand away from the coasts. During the recent economic expansion, a bevy of core Class A apartments were developed, providing renters with options when considering a transition.

Florida apartment operations face uneven recovery. Several markets in the state are projected to perform in line with the national average, including Jacksonville, Tampa and Fort Lauderdale. Other metros, however, depend on a more nuanced reopening strategy that could extend their timelines. In Orlando, kick-starting the tourism industry may be key to maintaining apartment operations. Many of the leisure and hospitality workers who reside in the metro are renters, and a protracted shutdown will disproportionately impact this group. Extending federal unemployment benefits may have the largest impact in Orlando. Densely populated Miami, meanwhile, depends heavily on international trade and travel, which could take longer to recover than local industries.

Investors poised to return. The allure of low interest rates will attract investors to Southern apartments when more clarity on pricing returns. Rent collection rates have been better than expected, largely due to elevated unemployment benefits and the low overall cost of rent in these markets. Only South Florida has rents above the national average, and elevated household incomes keep affordability lower than many coastal markets. Apartment buyers with access to inexpensive capital will move back into the market in the coming months as pricing expectations come into focus. The relatively short duration of apartment leases and favorable landlord laws will also encourage investors.

South Apartment Supply and Demand



Source: RealPage, Inc.

Retail Market in the South Expected to Outperform U.S.; Tourism-Dependent Areas Face Longer Recovery

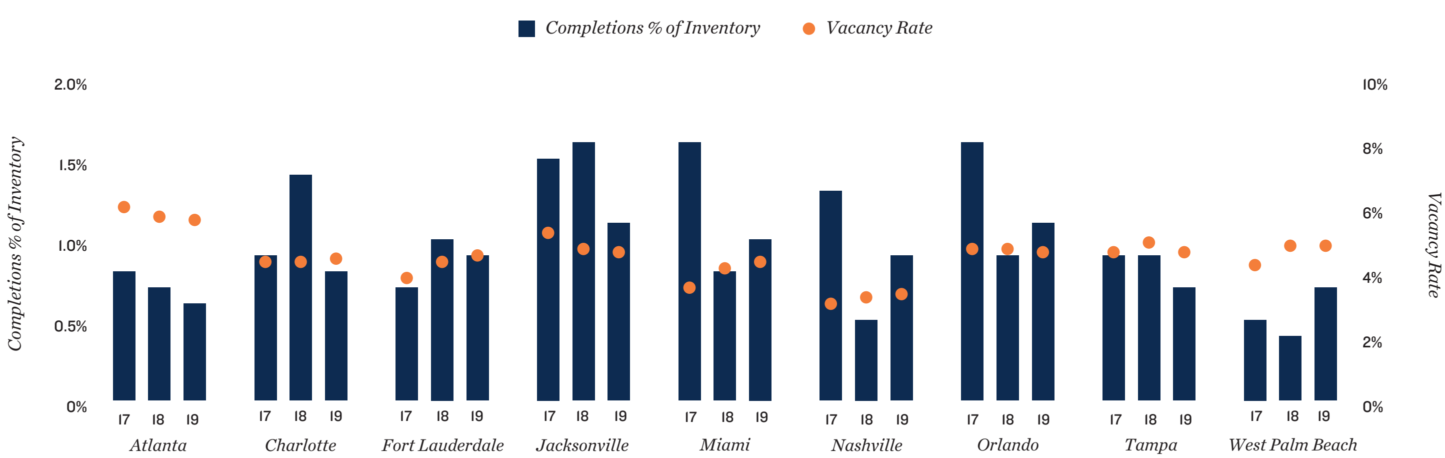
Southern retail in better position than most. A combination of bold reopening timelines and relatively dispersed communities could save more retailers in the South relative to other regions of the country. Sunny weather and low public transportation usage also support an optimistic outlook for many retailers in these markets. Consumers will ultimately be the linchpin that determines how many establishments remain open, though initial traffic counts are encouraging assuming a second wave of infections does not overwhelm local healthcare systems. Nonetheless, the economic damage is substantial and a sizable share of national department stores and local restaurants will shutter permanently.

Bifurcation in retail market dictates metro-level results. Essential retailers and fast-food restaurants are performing well across the nation and in the South. Grocery-anchored centers should continue to draw a heavy amount of traffic following the pandemic and will likely be the first multi-tenant locations to attract expanding or relocating retailers as the economy regains momentum. Single-tenant properties may also receive a boost, particularly those with a drive-thru on heavily trafficked corners. Strip centers, particularly those in mid-block locations, may struggle without the right mix of tenants. On the other hand, lower foot traffic in these locations could attract at-risk consumers seeking retail goods while avoiding crowds.

Several markets face above-average risk. Tourism accounts for more than 12 percent of all jobs in Florida and contributes $91 billion to the gross state product. Although retailers that cater to the local population should come back faster than the nation as doors are opened earlier, locations that rely on tourism spending may need additional stimulus to return. Undoubtedly, many retailers will be forced to shutter until international travel resumes and Americans feel more confident in their financial situation. Newly built entertainment districts in core locations of Nashville, Buckhead in Atlanta, Miami and Charlotte may also struggle to reopen the longer the global health crisis persists.

Investment opportunities to emerge. Relative to the nation, buyers will remain aggressive when pursuing single-tenant opportunities, particularly in Florida. Initially, single-tenant, net lease properties occupied by creditworthy tenants will be targeted while some price exploration is necessary before moving forward on franchisee deals. Investors could find new opportunities in tourist areas that were previously too expensive to justify an acquisition. Grocery-anchored centers, particularly those with an additional traffic generator such as a Starbucks will retain attractiveness while strip centers will take longer to attract buyers following the economic downturn.

South Retail Supply and Demand



Source: CoStar Group, Inc.

Southern Office Market Has Potential to Attract New Firms as Slow Reopening Strategies Hamstring Coastal Employers

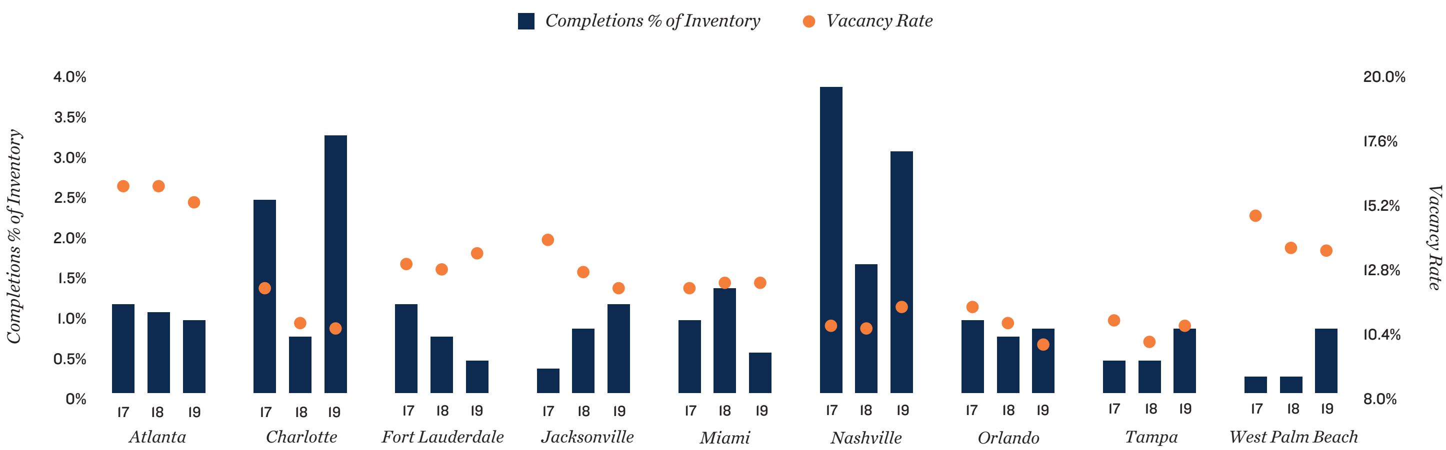
Potential worker migration could benefit local office markets. If dispersed working gains momentum, the potential for hybrid models may also emerge, encouraging some companies to search for lower-cost office space in Southern metros. Major tech companies may need to expand their local footprints to maintain a presence for a potentially larger local workforce. Additionally, support firms may find more flexibility across the country rather than keeping a large presence in an expensive coastal tech market. Metros with an existing base of technology firms stand to receive the largest benefit, including Nashville, Charlotte, Raleigh-Durham and to a lesser extent Atlanta and Miami.

Extended office shutdown elsewhere could benefit Southern markets. If reopening strategies become prohibitive in markets where skyscrapers dominate the local landscape, a permanent or temporary relocation of some departments may be necessary for companies to maximize productivity. As firms eager to return to office environments search for locations with vacancy in low-rise buildings, markets in the South could stand to benefit. Approximately 56 percent of the office space in nine large metros across the region are in low-rise buildings, and 11.5 percent of that space was vacant at the beginning of the global health crisis. Additional demand may come from local firms moving out of core city locations, particularly in Miami and Atlanta.

Long-term office outlook bright despite potential of dispersed workforces. The underlying fundamentals of the region's office market were healthy heading into the pandemic. Only Atlanta and Fort Lauderdale recorded vacancy above the national average while many Southern markets were rising in attractiveness to West Coast-based office users. In Nashville, for instance, Amazon had announced plans to expand its presence after canceling the construction of a second headquarters in New York City. Charlotte had also recently emerged as a nascent hotbed for startups, along with the Raleigh-Durham area. In Florida, office markets have traditionally been steady with little overbuilding, supporting a healthy recovery when the economy returns to normal.

Investors weigh options for office assets. Transaction activity is expected to slowly climb as the economy regains momentum. Large tech firms that have benefited from the shutdown may consider deploying capital to their own space if presented with the opportunity. Firms that need to downsize may leave sizable swaths of dark space in downtown locations, generating a few discounted sales. Distressed deals that do emerge may attract buyers intent on repurposing the space. Owner-users, meanwhile, will focus on low-rise office buildings located in suburban areas where social distancing is easier to manage.

South Office Supply and Demand



Source: CoStar Group, Inc.

Nearshoring and Surge in Online Shopping Well Beyond Health Crisis Will Benefit Southern Industrial Sector

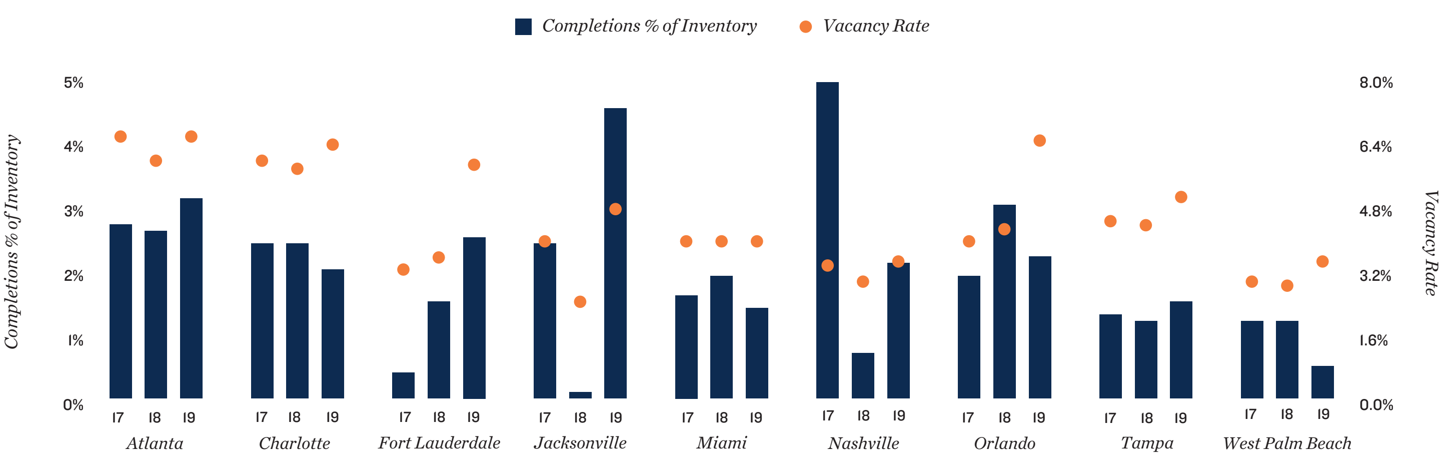
Warehouse and distribution centers remain healthy. Although shutdowns across the South were less prohibitive than elsewhere, many consumers stayed home to avoid contracting COVID-19. As a result, delivery warehouses remained busy across the region. Disciplined development during the most recent expansion limited supply-side threats heading into the recession. In Nashville, for example, vacancy was below 3 percent in the first quarter. Entering the global health crisis, approximately one-half of the major metros in the South recorded vacancy rates below the national average, a trend that should persist barring a second shutdown. As a result, the sector should be among the best performing during the recovery.

Ports and distribution hubs face new future. Miami, Jacksonville, New Orleans and Savannah are home to major container ship facilities in the region. If global supply lines evolve and nearshoring manufacturing gains momentum, the Southern ports could benefit from trade with Central and South America. Atlanta's major distribution network would also benefit as more goods pass through the area. An increase in trade with the European Union, which is also considering reshoring manufacturing, could provide a limited boost to the ports and distribution hubs as well. Low energy prices, meanwhile, will hamper export port operations in Louisiana until the supply overhang is absorbed and global demand for refined oil and gas rebounds.

Last-mile and cold-storage demand to persist following pandemic. Although a significant share of retail spending will move back into traditional brick-and-mortar locations, some consumers will permanently adopt health crisis habits. Older and vulnerable residents across the South are expected to remain away from crowded locations long after the worst of the threat is over. Some of the consumers who have been introduced to the convenience of purchasing goods online will also increase their permanent share of e-commerce shopping, elevating demand for both last-mile and cold-storage facilities. Furthermore, a work-from-home climate may encourage remote employees to have office products delivered and bill them back to companies.

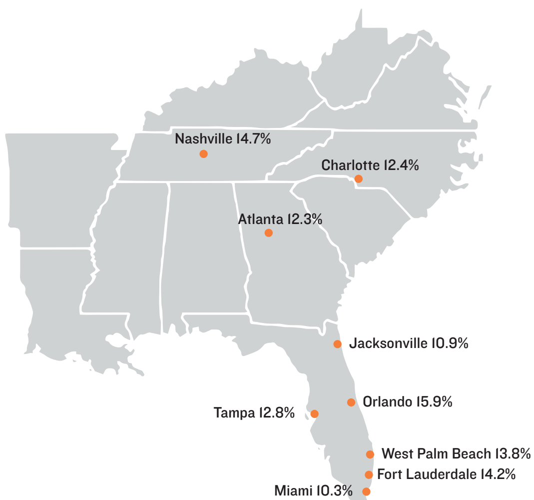
Buyer demand for industrial properties remains stout. Investors seeking real estate are keen on warehouse and distribution centers, often paying pre-pandemic prices for assets with favorable lease terms and national credit tenants. This trend should continue well beyond the health crisis as property performance for these categories remains strong or improves. Other industrial assets may need to find new pricing agreements, particularly those that support global supply chains as an increase in shipping to the South may elevate demand in the area. Industrial properties associated with the energy sector, such as light manufacturing or warehousing, could see a decrease in investor and tenant demand.

South Industrial Supply and Demand

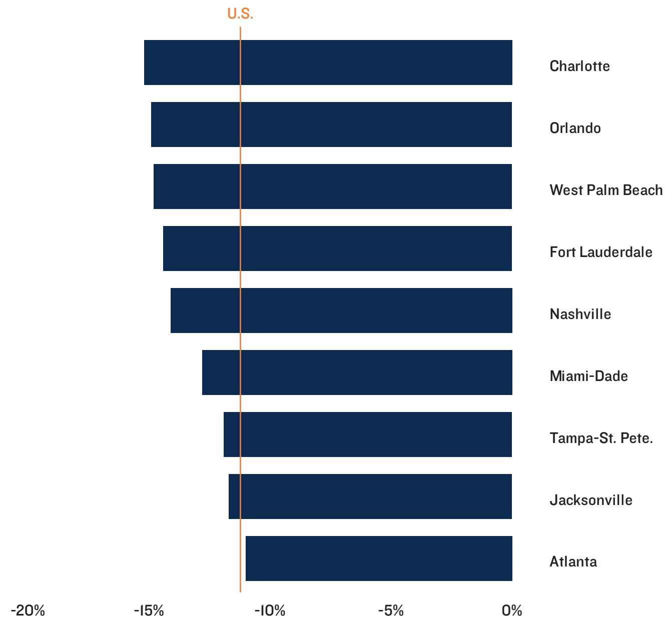


Source: CoStar Group, Inc.

April Unemployment Rate

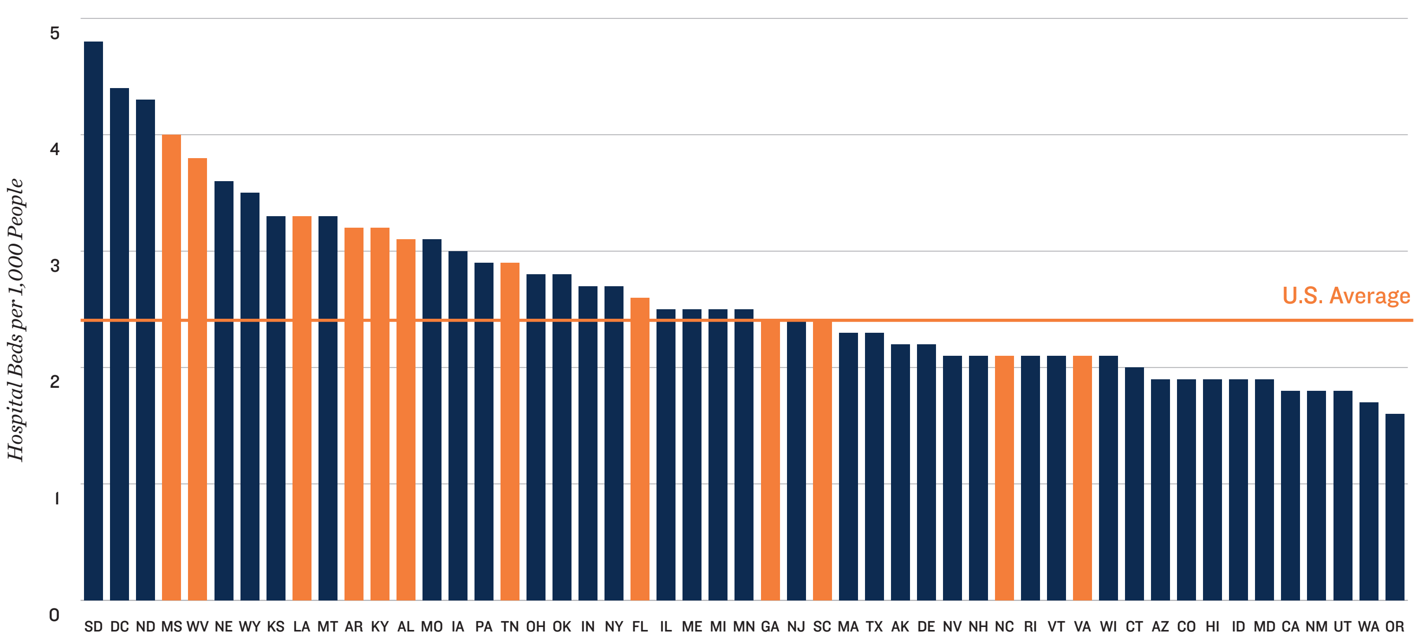


Share of Jobs Lost in March and April



March/April Cumulative Percent Change

Healthcare Capacity Key to Managing Crisis



Sources: American Hospital Association; Bureau of Labor Statistics

Demographic Tailwinds Support Long-Term Outlook in the South

Metro	5-Year Average Annual GMP Growth	5-Year Population Growth	Avg. Annual Increase	5-Year Household Income Forecast	Avg. Annual Increase	5-Year Household Growth	Avg. Annual Increase
Atlanta	4.4%	392,500	1.3%	$81,596	2.7%	169,000	1.5%
Charlotte	4.2%	178,300	1.3%	$72,311	2.5%	95,900	1.8%
Fort Lauderdale	3.6%	93,900	0.9%	$70,936	3.1%	55,900	1.4%
Jacksonville	4.0%	77,100	1.0%	$78,523	3.9%	44,500	1.4%
Miami	3.6%	103,800	0.7%	$66,108	3.3%	57,200	1.1%
Nashville	4.4%	138,500	1.4%	$79,764	3.1%	64,400	1.6%
Orlando	4.6%	219,800	1.6%	$74,248	3.2%	115,000	2.3%
Tampa-St. Pete.	3.8%	147,200	0.9%	$70,813	3.7%	92,600	1.4%
West Palm Beach	4.2%	111,300	1.4%	$84,011	4.8%	64,000	2.0%

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Sources: Marcus & Millichap Research Services; Bureau of Labor Statistics; CDC; CoStar Group, Inc.; Moody's Analytics; RealPage, Inc.; state and local health departments; U.S. Census Bureau