



FY 2018 budget

*Observations on how the FY 2018 U.S. federal budget will
impact Washington real estate by JLL Research*

March 2017

*“Government puts the needs of
its people first”*

Executive summary



This FY 2018 budget proposal is just that, a proposal, and does not become law without Congress passing it. During the Obama administration, more budgets went unpassed than passed and thus why we are operating under continuing resolution today.

Based on how significant some of these changes are, bipartisan support is unlikely and even partisan Republican support could thin on certain initiatives such as cutting State Department funding by 30% in a fiscal year.

If Congress does not pass a budget, which seems more likely day by day, we would end up with more of the same – lack of clarity – both in terms of agency mission as well as federal government real estate, ahead. However, without passing it, we could also dodge some of the significant cuts likely to more dramatically impact the Washington region that the Trump administration proposed and even undertake certain initiatives, such as defense, separately through the National Defense Authorization Act (NDAA), creating a true win-win scenario for Washington.

Most importantly, don't panic, and don't run. In times of change, opportunity is created. You will see a lot of really negative headlines, but they are just those, headlines. It is important to assess each agency, sub-agency and location in these changing times and see how your organization or investment is not just impacted, but can benefit from these changes.

John Sikaitis

Executive summary



1

Northern Virginia is the real winner, maybe

- Only three executive-level branches saw proposed increases in budgets: Defense (9%); Homeland Security (7%) and Veterans Affairs (6%).
- If approved by Congress, these defense and homeland security investments will positively impact Northern Virginia and mission-critical government contractors.
- The administration calls for cuts to non-mission critical functions and specifically calls out IT. In FY 2016, technology contracts represented 41% of overall contracts. Should IT budgets be cut, any growth of mission-critical contractors could be equally negated by technology-focused contractors and thus why, to date, contractor leasing activity in Northern VA has been very quiet despite increased investor demand and activity.

2

Southwest is the short-term loser; long-term winner?

- Only four agencies saw a single-digit cut: NASA, Justice, Treasury and SBA and certain agencies such as Labor, State, EPA and Agriculture saw proposed cuts of 20+% in FY 2018 alone.
- Large cuts to many executive-level agencies will have the biggest direct negative impact on Southwest DC government product where leadership is based and where mission critical functions often times are not.
- Cuts to HQ functions in Southwest could be a long-term benefit to real estate owners there as Mall-centric locations (such as recent disposition of Cotton Annex) could be disposed by GSA for private use. Consider this, there is a 54% rent premium for office product at the Wharf to other Southwest office product.

3

Lobbying / government affairs could boom, fueling Trophy

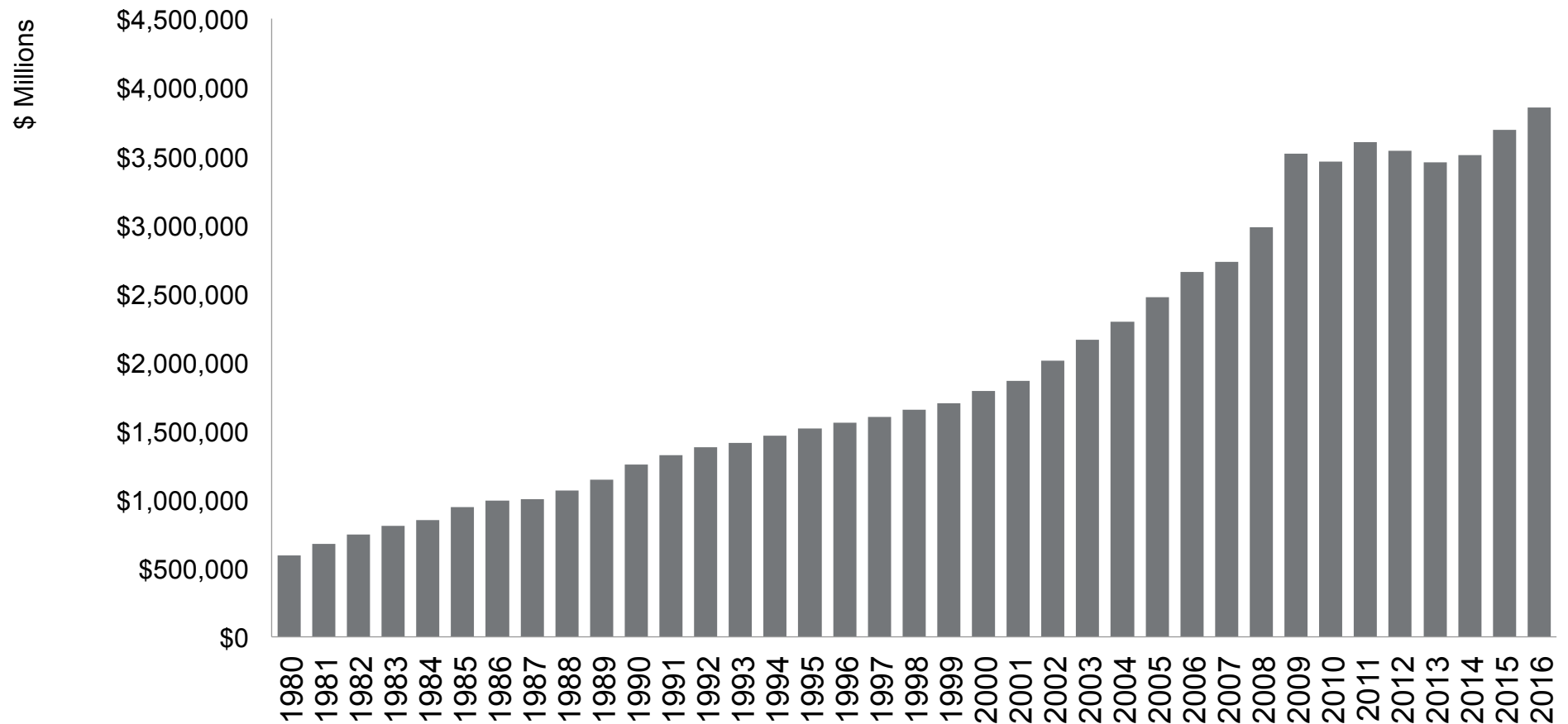
- Agencies have never experienced such drastic cuts in a fiscal year. The changes will affect all industries. Any change, especially large change, usually ushers in a new wave of lobbyists, lawyers and government affairs entities, which will benefit the Trophy / A+ segments of the East End, Capitol Hill and The Wharf.
- The administration also calls for re-organizing the executive-level branch over the next 12 months, which lobbyists and government affairs outfits will want to shape, benefitting Trophy and A+ segments downtown.
- The administration will propose substantial tax reform over the next 12 months. Any changes in corporate tax will shrink the IRS, but require a lot of lawyers to help navigate corporates through amendments, benefitting Trophy and A+ segments downtown.

Macro budget detail

Historical U.S. federal spending



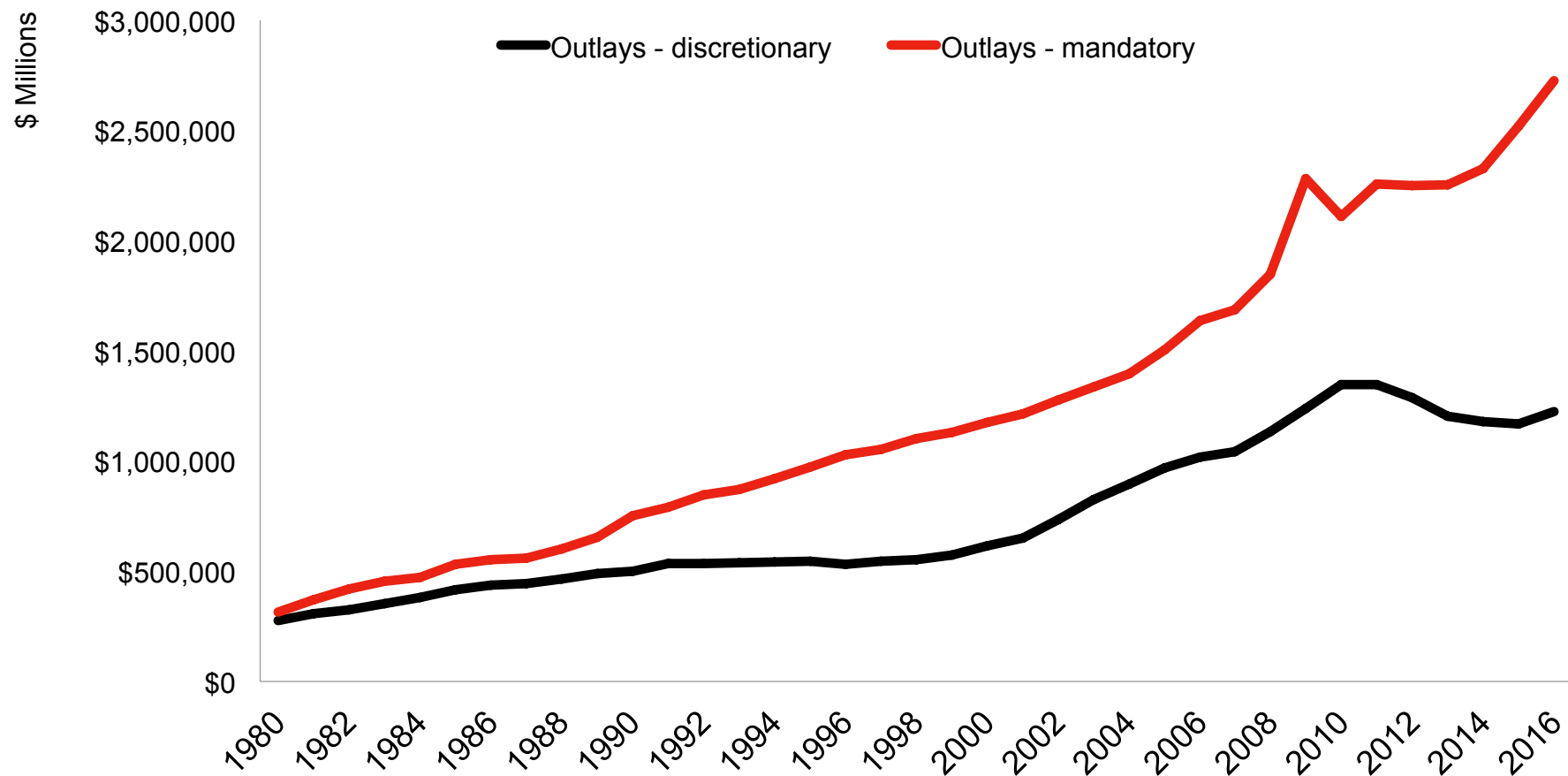
After consistent levels of growth, almost forever, will federal spending take a sharp turn?



Historical U.S. budget authority



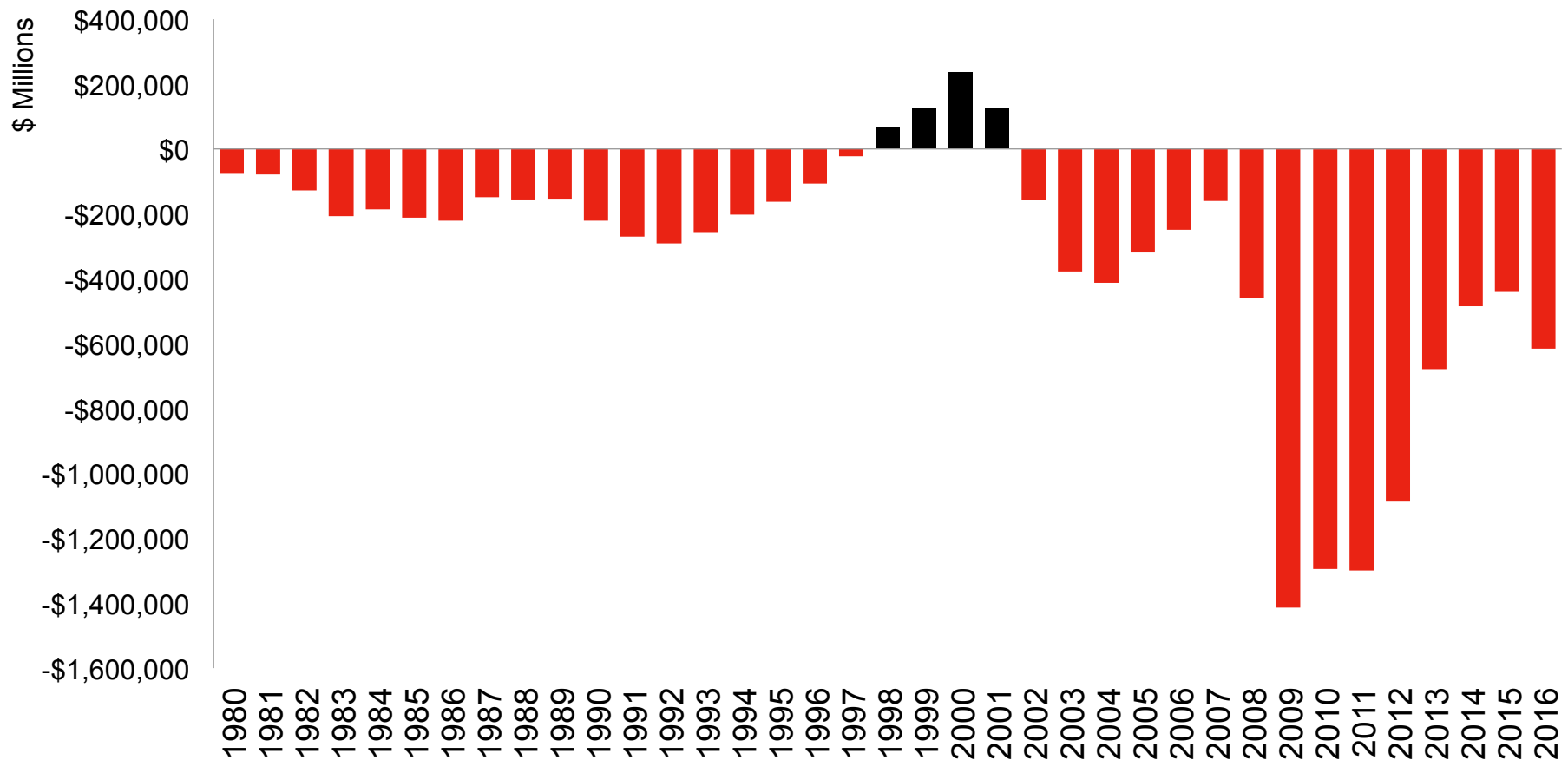
Entitlements (Social Security, Medicaid and Medicare) have eaten into discretionary investments over past few decades



Historical U.S. annual budget deficit / surplus



Deficits have ruled the most recent fiscal landscapes



Agency budget detail

(ranked by winners to losers)

“Provides one of the largest increases in defense spending without raising the debt”

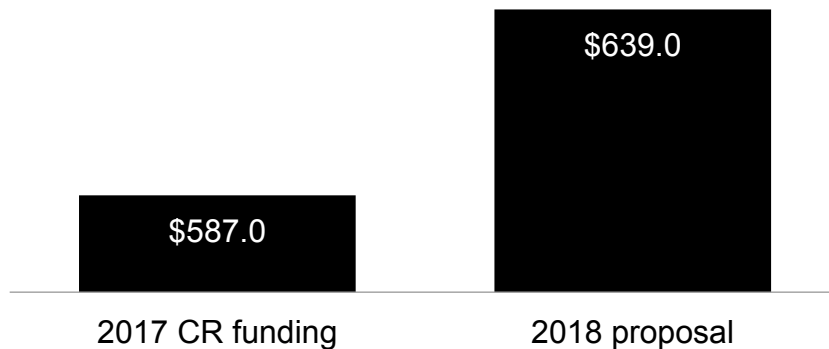
“Offsets defense investment with \$54 billion in cuts elsewhere”

Defense



Proposed budget calls for 9% increase

Funding in billions



Investing in

- Overall training, equipment and infrastructure, including for campaign to defeat ISIS
- Increased Army headcount
- Increased Navy ship fleet
- Air Force maintenance capacity, training, and additional F-35 Joint Strike Fighters

Metro DC office impact

Benefits: Crystal City, RB Corridor, Route 28 South, Toll Road, Ballpark, Columbia, Harford County, Aberdeen Proving Ground, Hampton Roads

Challenges: No regional submarkets

Indirect: Reinvigorates mission-critical and R&D-focused government contractors regionally.

Cutting

- No specific cuts referenced

“Significantly increases the budget for immigration enforcement at the Department of Justice and Homeland Security by expanding US Attorneys, U.S. Immigration & Customs Enforcement and Border Patrol”

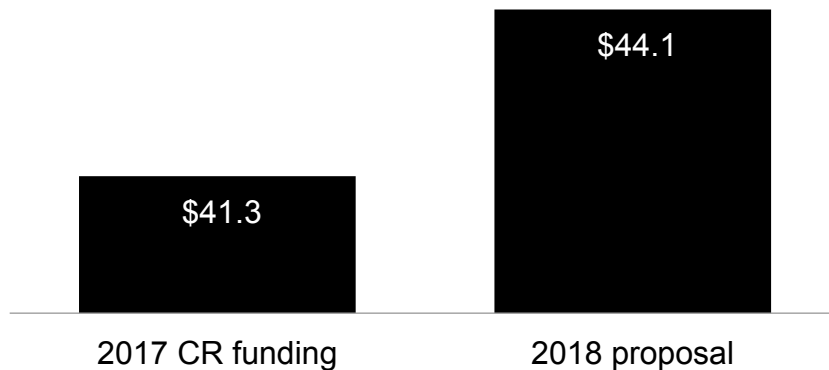
“Build a wall and increase funding to address violent crime and opioid abuse

Homeland Security



Proposed budget calls for 7% increase

Funding in billions



Investing in

- \$2.6B in infrastructure and border security technology, including to design and construct southern border wall
- \$314M for recruitment, hiring and training of 500 new Border Patrol Agents and 1,000 new Customs Enforcement personnel
- Additional \$1.5B for expanded detention, transportation, and removal of illegal immigrants
- \$15M to implement mandatory E-Verify Program for determining employee eligibility
- \$1.5B for cybersecurity

Metro DC office impact

Benefits: Crystal City, Route 28 South, Loudoun, Southwest, NoMa, Prince George's

Challenges: Pentagon City (TSA), Southwest (FEMA)

Indirect: This administration's focus on mission-critical could delay or altogether eliminate St. Elizabeth's funding. Investment in cyber will benefit Westfield / Dulles area.

Cutting

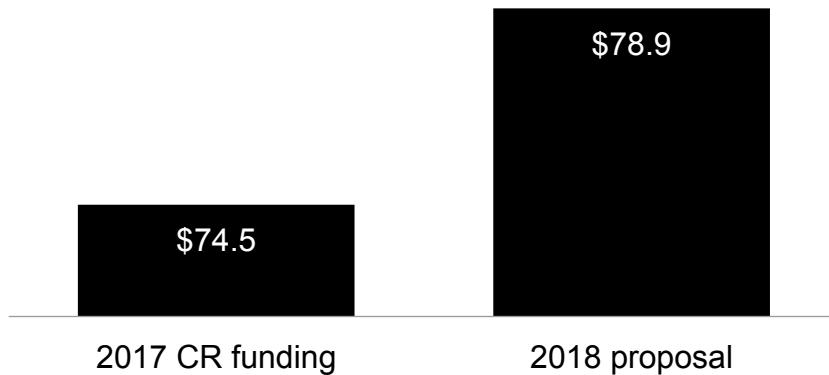
- \$667M in state and local grant funding for FEMA, including Pre-Disaster Mitigation Grant Program
- \$80M in unauthorized and underperforming programs administered by TSA, including Visible Intermodal Prevention and Response program and state and local grants
- \$190M for National Flood Insurance Program's Hazard Mapping Program

Veterans Affairs



Proposed budget calls for 6% increase

Funding in billions



Metro DC office impact

Benefits: NoMa, East End

Challenges: No regional submarkets

Indirect: Funding for new, modern and consolidated VA facilities nationally will be more readily available

Investing in

- Increasing efficiency and breadth of care offered to veterans
- Extending the Veterans Choice Program
- Revamping the VA claims process

Cutting

- **No initiatives specified**

“In 12 months, the OMB through Congress, will deliver comprehensive plan for reorganization of executive branch proposals”

“Agencies will devoting greater percentage of tax dollars to mission achievement rather than compliance activities”

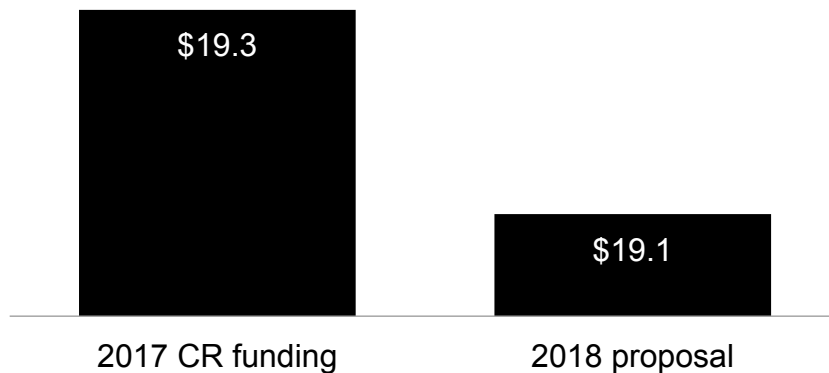
“Control cost and eliminate unnecessary regulation: requires agencies to eliminate at least two existing regulations for each new regulation issued”

National Aeronautics and Space Administration



Proposed budget calls for 1% reduction

Funding in billions



Metro DC office impact

Benefits: Tysons and Toll Road

Challenges: Southwest, Prince George's

Indirect: While NASA direct occupancy will likely not grow, there appears to be room for growth in contracts to the private sector, benefitting the Toll Road and Tysons.

Investing in

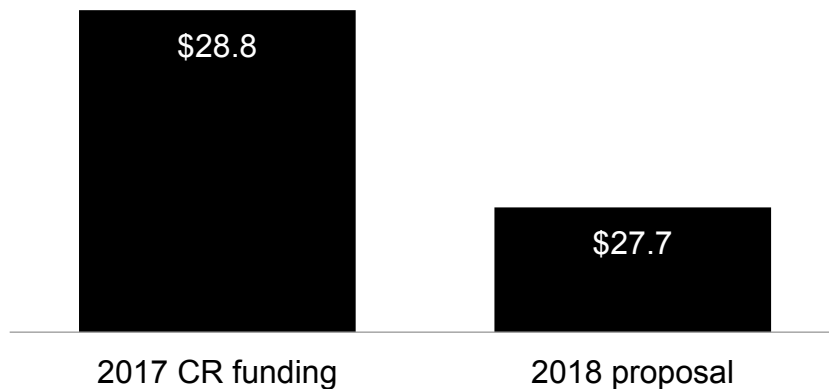
- Public-private partnerships that support research for deep-space habitation and develop new space technologies
- Aeronautics research for over-land commercial supersonic flights
- Planetary Science program for missions to Mars and Europa
- Cybersecurity capabilities

Cutting

- Cancels the Asteroid Redirect Mission
- Reduces the Earth science portfolio by \$102M cutting four earth science missions and reducing funding for earth science research grants
- Eliminates the \$115M Office of Education
- Restructures a robotic satellite refueling demonstration mission reducing funding by \$88M

Proposed budget calls for 4% reduction

Funding in billions



Investing in

- Public safety
- Law enforcement
- National security
- Confronting terrorism
- Reducing violent crime
- Tackling the Nation's opioid epidemic
- Combating illegal immigration

Metro DC office impact

Benefits: NoMa, East End

Challenges: Price George's if FBI deal is delayed or cut

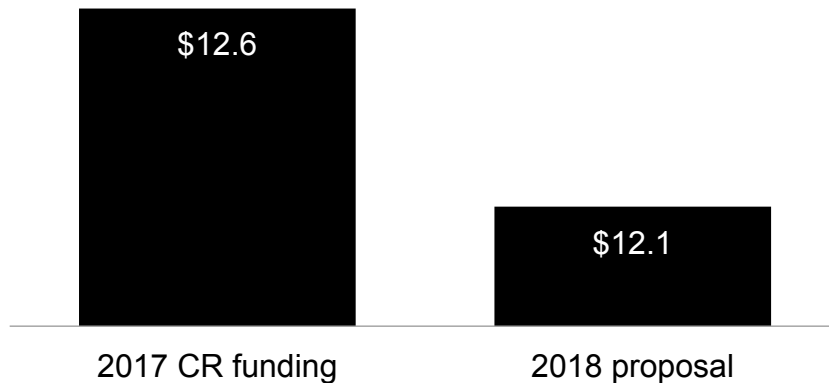
Indirect: With no mention of the FBI relocation in budget, does a new, secure HQ facility qualify as mission critical? In past administrations, it did. However, in this administration, maybe not, or maybe not with the current real estate deals.

Cutting

- Unnecessary spending on outdated programs that either have met their goal or have exceed their usefulness such as the State Criminal Alien Assistance Program
- Federal prison construction spending

Proposed budget calls for 4% reduction

Funding in billions



Investing in

- Cybersecurity
- Protecting the financial system from threats
- Combating financial crime and terrorism financing

Metro DC office impact

Benefits: Northern Virginia ((Route 28 South, Loudoun (cyber)); Capitol Hill, East End The Wharf Trophy product

Challenges: No regional submarkets

Indirect: If tax reform is proposed, lobbyists will shape it and expand. If tax reform is enacted, law firms will navigate new code for corporations.

Cutting

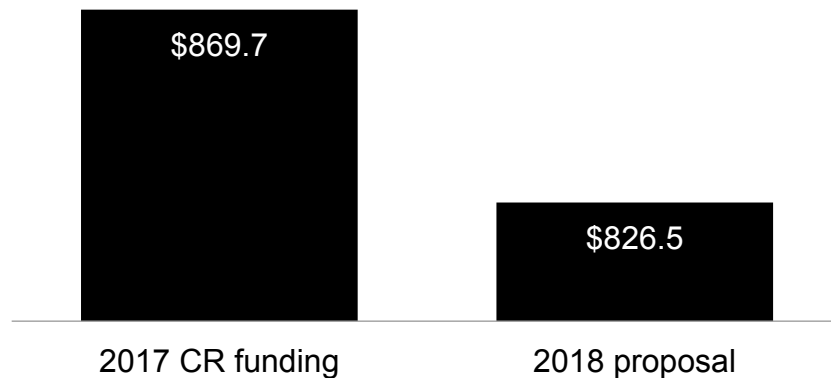
- Federal workforce; redirecting resources away from duplicative policy offices
- Community Development Financial Institutions Fund grants
- Antiquated operations that are reliant on paper-based review

Small Business Administration



Proposed budget calls for 5% reduction

Funding in millions



Metro DC office impact

Benefits: No regional submarkets

Challenges: No regional submarkets

Indirect: A small reduction in funding will not dramatically impact anything regionally in Washington.

Investing in

- Training and support services for transitioning service members and veterans
- Support to loan guarantees, microloan financing and technical assistance for small business businesses

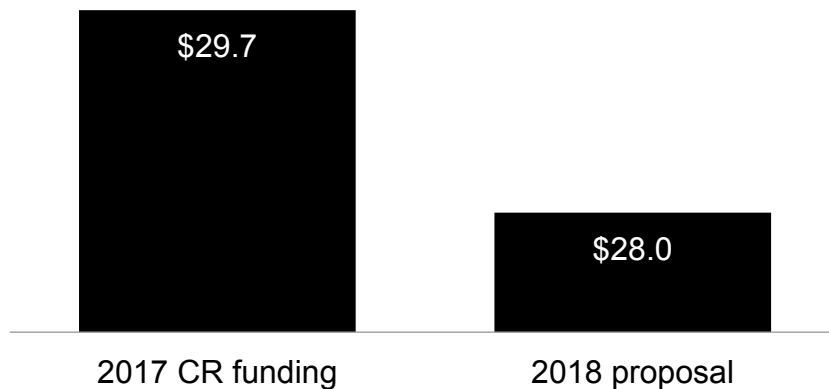
Cutting

- SBA programs including PRIME technical assistance grants, Regional Innovation Clusters, and Growth Accelerators (\$12M savings)
- Duplicative services offered by outreach center programs

Energy

Proposed budget calls for 6% reduction

Funding in billions



Investing in

- National Nuclear Security Administration received a \$1.4 billion increase above the 2017 CR level
- Office of Electricity Delivery and Energy Reliability's capacity to carry out cybersecurity and grid resiliency activities
- Environmental Management to clean up the legacy of waste and contamination from nuclear weapons production

Metro DC office impact

Benefits: Rockville Pike, Anne Arundel

Challenges: Southwest

Indirect: Mission-critical elements such as investment in Nuclear and cyber investment will likely benefit Montgomery County; HQ reduction will negatively impact Southwest.

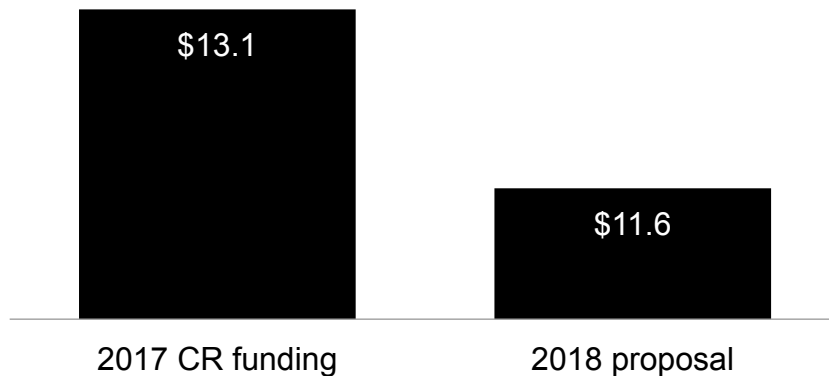
Cutting

- Reduces the Office of Science allocation by \$900 million
- Eliminates the Advanced Research Projects Agency-Energy, the Title 17 Innovative Technology Loan Guarantee Program, and the Advanced Technology Vehicle Manufacturing Program which will allow the private sector to finance the energy research and development
- Eliminates the Weatherization Assistance Program and the State Energy Program in order to reduce Federal intervention in State-level energy policy

Interior

Proposed budget calls for 12% reduction

Funding in billions



Investing in

- Programs that strengthen the Nation's energy security on public land and offshore waters
- The National Park Service by increasing investment in deferred maintenance projects
- U.S. Geological Survey for research in sustainable energy development and resource management
- More than \$1 billion of funding for water resource management in western U.S.

Metro DC office impact

Benefits: Reston, East End

Challenges: Ballpark (Bureau of Land Management)

Indirect: Interior, more than any other executive-level branch agency, is the likeliest to be relocated outside of Washington, should momentum in Congress build to focus on that. Franklin Square transformation could be realized downtown.

Cutting

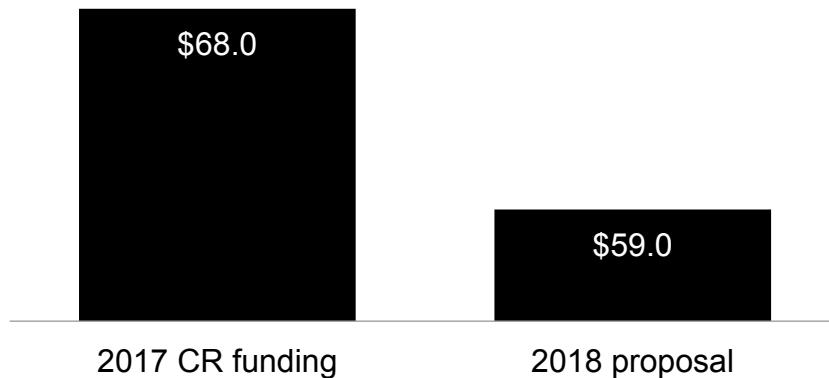
- Abandoned Mine Land grants
- Funding to National Heritage Areas
- National Wildlife Refuge fund payments to local governments
- Reduces land acquisition funding by \$120M
- Reduces funding for recent demonstrations projects that serve only a few Indian Tribes

Education



Proposed budget calls for 13% reduction

Funding in billions



Investing in

- \$20B annually for public and private school choice programs, an increase of \$1.4 billion
- \$168M funding increase for charter schools
- \$250M for a new private school choice program
- \$1B spending increase for school choice system
- Maintains funding for IDEA program
- Maintains funding for programs serving high percentages of minority students
- Level funds Pell Grant program

Metro DC office impact

Benefits: No regional submarkets

Challenges: Southwest, NoMa

Indirect: Across Metro DC, from Tysons to Downtown to Montgomery County, Charter Schools have taken down land and traditional office space. This will only continue under this administration, diversifying office uses.

Cutting

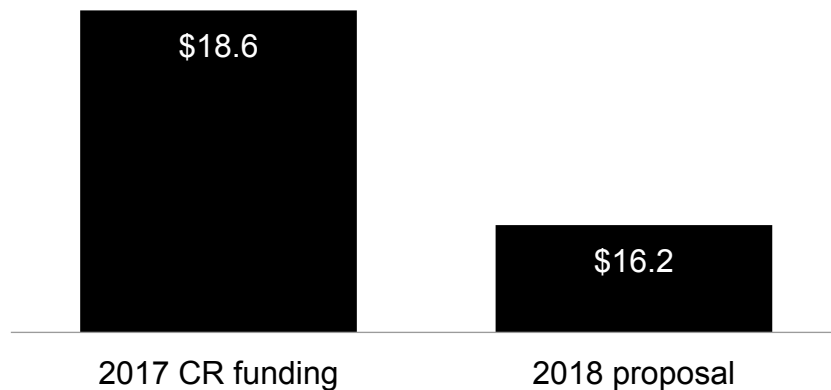
- Eliminates Supporting Effective Instruction State Grants program
- Eliminates 21st Century Community Learning Centers program
- Eliminates Federal Supplemental Educational Opportunity Grant program
- Reduces Federal Work-Study, Gear Up and TRIO Programs funding
- Eliminates or reduces over 20 categorical programs

Transportation



Proposed budget calls for 13% reduction

Funding in billions



Metro DC office impact

Benefits: No regional submarkets

Challenges: Ballpark, Capitol Hill (Amtrak)

Indirect: Based on administration's mission-critical focus, HQ functions of the DOT will likely decline with money going to local infrastructure projects. Will Metro DC and WMATA, which voted all blue, miss out from infrastructure list?

Investing in

- Nationally and regionally significant transportation infrastructure projects
- Privatization of Federal Aviation Administration's air traffic control function
- Authorizes \$900M annually for Nationally Significant Freight and Highway Projects grant program through 2020

Cutting

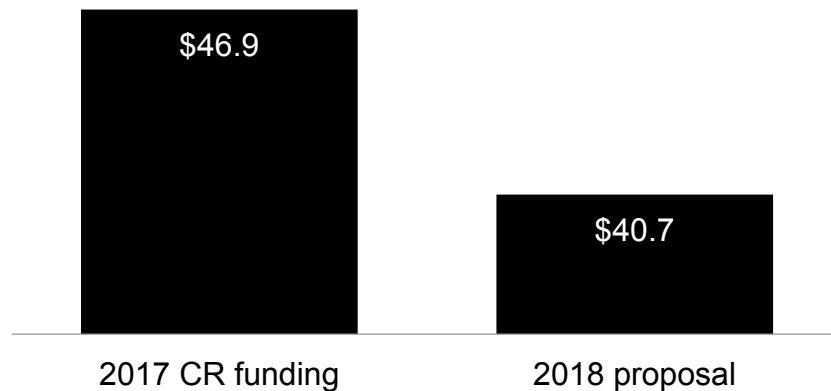
- Restructures and reduces Federal subsidies for Amtrak to focus resources on regional operations
- Terminates Federal subsidies for Amtrak's long distance train services
- Limits Federal Transit Administration's Capital Investment Program (New Starts) funding
- Eliminates Essential Air Service program funding
- Eliminates TIGER discretionary grant program funding

Housing and Urban Development



Proposed budget calls for 13% reduction

Funding in billions



Metro DC office impact

Benefits: No regional submarkets

Challenges: Southwest DC

Indirect: The administration, like past ones, will likely explore the privatization of both Fannie and Freddie, which combined, occupy more than 2 million s.f. throughout the region.

Investing in

- \$35B for rental assistance programs
- \$130M for lead-paint and other home hazard mitigation in low-income homes
- Federal Housing Administration mortgage insurance programs

Cutting

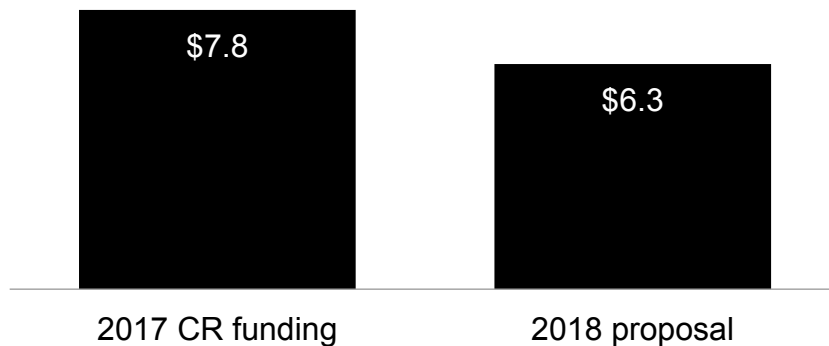
- Eliminates Community Development Block Grant Program funding
- Eliminates HOME Investment Partnerships Program funding
- Eliminates Choice Neighborhoods funding
- Eliminates Self-help Homeownership Opportunity Program funding
- Eliminates Section 4 Capacity Building for Community Development and Affordable Housing funding

Commerce



Proposed budget calls for 16% reduction

Funding in billions



Investing in

- International Trade Administration's trade enforcement and compliance functions
- \$1.5B funding for 2020 Decennial Census, an increase of more than \$100M
- Maintains National Weather Service capabilities by investing \$1B
- Maintains development of NOAA polar orbiting and geostationary weather satellites

Metro DC office impact

Benefits: Silver Spring, (NOAA), Southwest (HQ)

Challenges: Prince George's (Census and analysis)

Indirect: Commerce has many agencies under it and with massive consolidation potentially, primary functions around Census and data, a lot of which are focused in Prince George's, could benefit.

Cutting

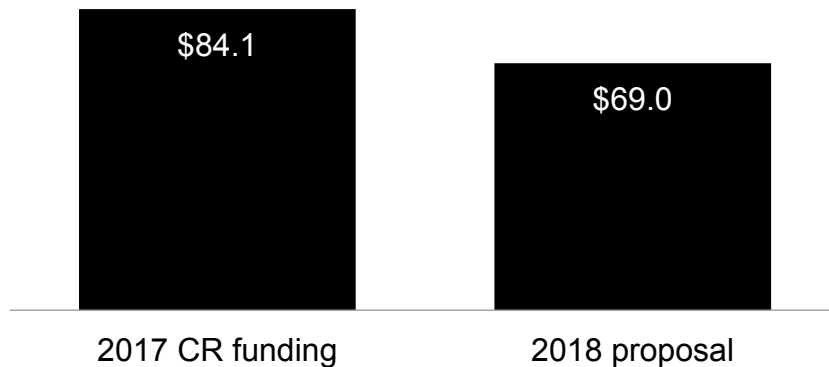
- Consolidates Economics and Statistics Administration
- Eliminates Economic Development Administration
- Eliminates Minority Business Agency
- Discontinues Manufacturing Extension Partnership
- Zeroes out \$250 million in targeted NOAA grants
- Cuts part of NOAA's Polar Follow On satellite

Health & Human Services



Proposed budget calls for 18% reduction

Funding in billions



Investing in

- HCFAC to help prevent fraud in Medicare and Medicaid
- SAMHSA with an emphasis on opioid abuse
- FDA as it relates to regulatory efficiency and speed the development of medical products
- CDC as it creates a new Federal Emergency Response Fund
- Highest priorities: community health centers, Ryan White HIV/AIDS providers, IHS

Metro DC office impact

Benefits: North Silver Spring, Prince George's, Rockville Pike

Challenges: I-270 Corridor

Indirect: Life sciences has made a comeback recently in Suburban Maryland. A significant funding reduction could return the lab market to stagnant conditions that were present from 2004-2014.

Cutting

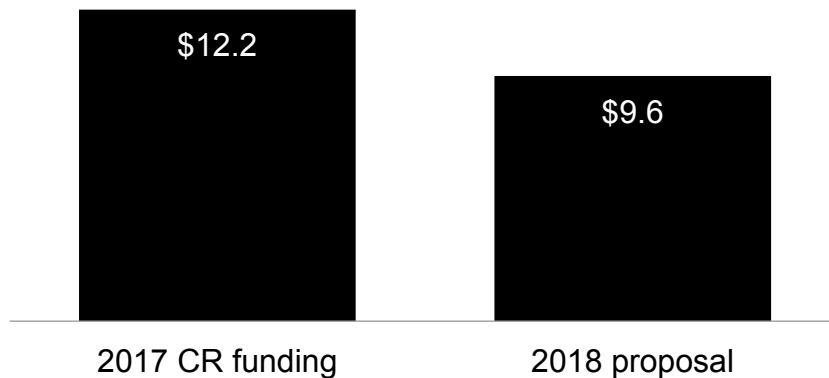
- Reduces NIH spending relative to the 2017 annualized CR level by \$5.8B (major reorganization is planned)
- Eliminates \$403M in health professions and nursing training programs
- Eliminates the discretionary programs within the Office of Community Services, including LIHEAP and CSBG

Labor



Proposed budget calls for 21% reduction

Funding in billions



Metro DC office impact

Benefits: NoMa, Southwest or East of the River (potential HQ relocation sites), Capitol Hill

Challenges: No regional submarkets

Indirect: Reduced focus on Labor could lead to HQ downsize and relocation, leading to new construction and redevelopment of Perkins building on Hill into another use.

Investing in

- Reemployment and Eligibility Assessments
- Apprenticeship programs

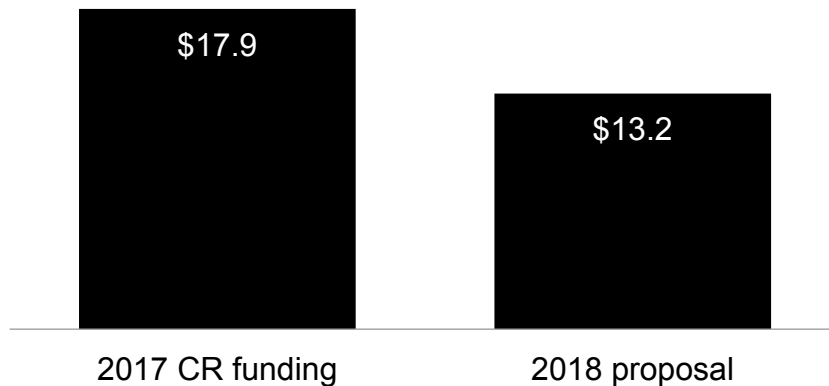
Cutting

- Senior Community Service Employment Program (\$434M savings)
- Grant funding for Bureau of International Labor Affairs (\$60M savings)
- Federal support for job training and employment service formula grants
- Occupational Safety and Health Administration training grants (\$11M savings)

Agriculture

Proposed budget calls for 21% reduction

Funding in billions



Metro DC office impact

Benefits: No regional submarkets

Challenges: Southwest DC

Indirect: After Interior, Agriculture is one of the likeliest executive-level agencies to be relocated outside of Washington, should momentum in Congress build to focus on that.

Investing in

- Food Safety & Inspection Service
- Wildland fire preparedness and suppression activities

Cutting

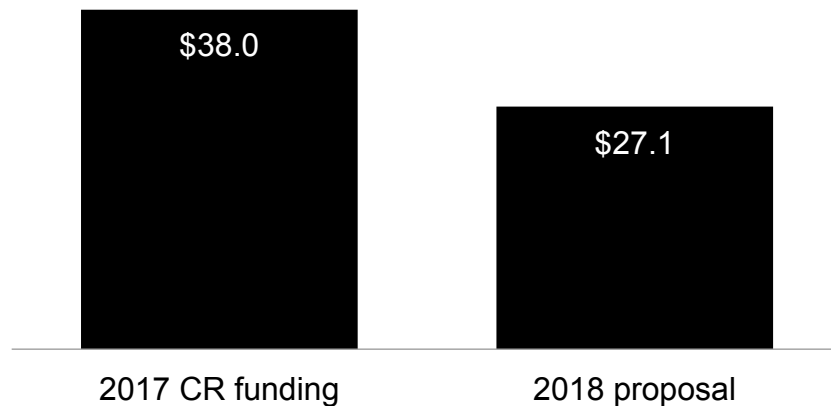
- National Forest System
- USDA's statistical capabilities (HQ)
- Water and Wastewater grant program
- USDA Service Center Agencies (county-level)
- Discretionary activity of Rural Business and Cooperative Service (\$95 million savings)
- McGovern-Dole International Food for Education program

State/USAID (Base Discretionary)



Proposed budget calls for 29% reduction

Funding in billions



Metro DC office impact

Benefits: Dupont Circle (think tank central)

Challenges: East End (USAID) and West End, Rosslyn (State)

Indirect: Should State cuts go through. West End excess space will be gobbled up by GWU. Think tanks could get bigger if State gets smaller, benefitting Dupont Circle

Investing in

- New embassy construction and maintenance
- Security assistance commitment to Israel
- Maintains funding to the Vaccine Alliance
- President's Emergency Plan for AIDS Relief
- Global Fund for AIDS, Tuberculosis, and Malaria

Cutting

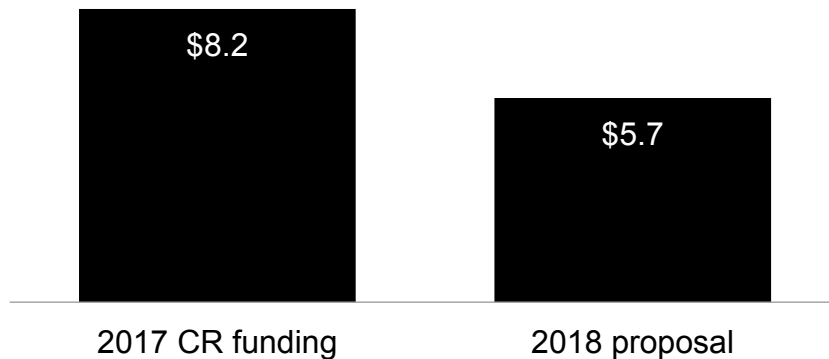
- Global Climate Change Initiative
- Foreign military assistance shifts from grants to loans
- Reduces UN peacekeeping mission funding
- Eliminates Emergency Refugee and Migration Assistance Account
- Educational and Cultural Exchange Programs
- Reduces funding for the World Bank

Environmental Protection Agency



Proposed budget calls for 31% reduction

Funding in billions



Metro DC office impact

Benefits: No regional submarkets

Challenges: Crystal City, East End, Baltimore CBD, Annapolis

Indirect: Superfund cuts and regional cuts (like the Chesapeake Bay Program) may affect the USACE location in the Baltimore CBD.

Investing in

- Wastewater and drinking water infrastructure.
- Slightly increases funding for the State Revolving Funds

Cutting

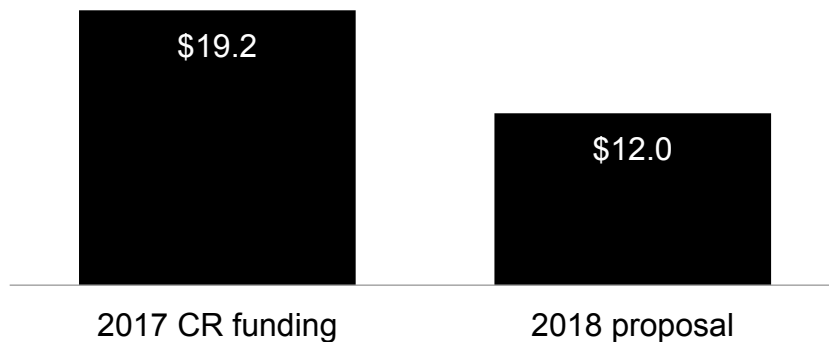
- Eliminates funding for the Clean Power Plan, international climate change programs, and climate change research
- Reduces Hazardous Substance Superfund Account
- Enforcement of environmental protection violations
- Reduces Office of Research and Development funding
- Eliminates funding for Chesapeake Bay cleanup and Great Lakes Restoration Initiative
- Eliminates an additional 50 EPA programs including Energy Star
- Eliminates 3,200 positions

State/USAID (OCO)



Proposed budget calls for 38% reduction

Funding in billions



Metro DC office impact

Benefits: Dupont Circle (think tank central)

Challenges: East End (USAID) and West End, Rosslyn (State)

Indirect: Should State cuts go through. West End excess space will be gobbled up by GWU. Think tanks could get bigger if State gets smaller, benefitting Dupont Circle

Investing in

Cutting

- Reduces Overseas Contingency Operations funding, especially in war areas including Syria, Iraq and Afghanistan

Eliminating funding for independent agencies



- African Development Foundation (East End leased)
- Appalachian Regional Commission (Uptown leased)
- Chemical Safety Board (CBD leased)
- Corporation for National and Community Service (Southwest leased)
- Corporation for Public Broadcasting (East End leased)
- Delta Regional Authority (Capitol Hill leased)
- Denali Commission (Outside of region: Alaska)
- Institute for Museum and Library Services (Southwest leased)
- Inter-American Foundation (East End leased)
- U.S. Trade and Development Agency (Rosslyn leased)
- Legal Services Corporation (Georgetown leased)
- National Endowment for the Arts (Southwest leased)
- National Endowment for the Humanities (Southwest leased)
- Neighborhood Reinvestment Corporation (NoMa leased)
- Northern Border Regional Commission (Outside of region: New Hampshire)
- Overseas Private Investment Corporation (East End leased)
- United States Institute of Peace (West End owned)
- United States Interagency Council on Homelessness (NoMa leased)
- Woodrow Wilson International Center for Scholars (East End owned)



**> 700,000
s.f. of
leased
regional
office
space
impacted**

*“Safety is first priority because
without safety, there is no
prosperity”*

FY 2018 budget observations



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