

MARKET REPORT

OFFICE

Washington, D.C., Metro Area

IPA INSTITUTIONAL
PROPERTY
ADVISORS

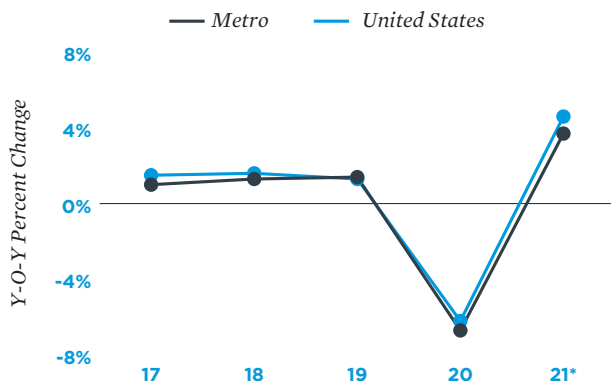
4Q/21

Office Return Yet to Take Widespread Hold in D.C.; Suburban Assets First to Report Improving Metrics

Slow return to workplaces weighs on operations. Despite the availability of vaccines and testing, the office sector had yet to make substantial progress by June of this year. Since the first quarter of 2020, approximately 9.7 million square feet of office space has been returned to the market, driving vacancy up 270 basis points to its highest level since at least 2007. The path through the rest of the year is mixed. Rising infections from coronavirus variants have delayed some planned office returns. A vaccine mandate for employees of federal agencies and large companies nevertheless aims to facilitate that process, which should help lift foot traffic in still-quiet commercial districts. Ridership across the metro's many public transit options continued to trail normal levels by around 60 percent in September.

Suburban offices more resilient. While several short-term challenges remain, many firms are committed to offices in the long run. Large companies such as Microsoft, PWC and JPMorgan all moved into floor plans of at least 150,000 square feet this year. The federal government also intends to hold onto offices, especially at facilities it owns. The amount of space they lease from other organizations may be consolidated in the coming years however. So far in 2021, offices in lower rent, less central, and more car accessible areas have performed best. Vacancies are contracting in parts of Prince George's, Frederick and Montgomery counties, as well as along some key interstates.

Employment Trends



* Forecast

Sources: BLS; CoStar Group, Inc.

Office 2021 Outlook



115,000

JOBS

will be created

EMPLOYMENT:

Metro employers are on track to expand headcounts by 3.7 percent in 2021 following a 6.7 percent contraction last year. About 17,500 of the roles added this year will be in traditionally office-using sectors, representing a 1.8 percent growth rate.



2,000,000

SQ. FT.

will be completed

CONSTRUCTION:

Office arrivals in 2021 will fall to the lowest level in six years with a 0.4 percent expansion to inventory. The highest concentration of new space will be in South Prince George's County as well as around Capitol Hill and in Bethesda-Chevy Chase.



110

BASIS POINT

increase in vacancy

VACANCY:

Vacancy will climb by about half the pace of last year to 19.7 percent as the rate of office move-outs moderately tempers. Availability will rise the most within the District and across northern Virginia, which comprise 78 percent of the market's inventory.



0.1%

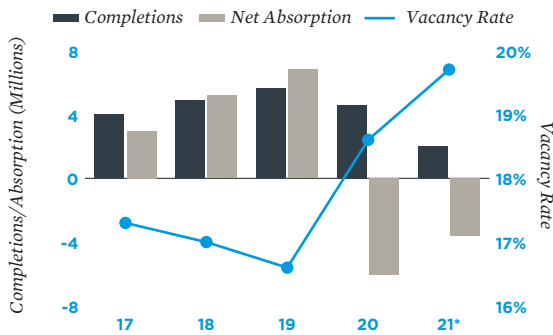
DECREASE

in asking rent

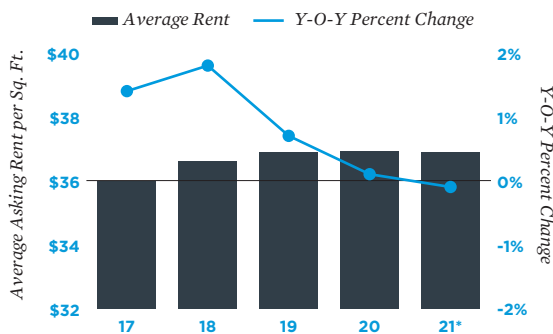
RENT:

The average asking rent will hold about flat at \$36.91 per square foot for the second year in a row as many companies continue to contemplate their office needs. Through the first half of 2021, market rates dipped the most in northern Virginia.

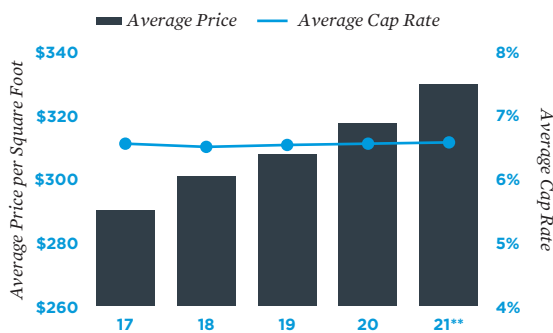
Supply and Demand



Rent Trends



Sales Trends



* Forecast ** Through 2Q
Sources: CoStar Group, Inc.; Real Capital Analytics

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2Q21 – 12-Month Period

CONSTRUCTION

3,214,000 sq. ft. completed

- Developers finalized approximately 1.4 million fewer square feet over the 12-month span ended in June relative to the prior annual period.
- The most space came online in suburban Maryland at more than 2 million square feet. About 880,000 square feet was delivered in northern Virginia followed by 295,000 square feet in D.C. proper.

VACANCY

240 basis point increase in vacancy Y-O-Y

- Nearly 9 million square feet of office space was vacated on a net basis over the past four quarters, lifting marketwide vacancy to 19.5 percent. Between 2007 and 2020, the rate had never surpassed 18.6 percent.
- Over the past year Class A vacancy jumped 270 basis points to 22.1 percent, while the Class B/C rate rose 190 basis points to 16.2 percent.

RENT

0.3% decrease in the average asking rent Y-O-Y

- Despite notable negative net absorption, the average asking rent remained relatively flat over the past year, inching down to \$36.96 per square foot. The measure is 0.6 percent below the pre-recession high.
- Rents shifted the most in parts of Maryland, down 3.0 percent in Frederick and up 2.9 percent in North Prince George's County.

Investment Highlights

- Transaction activity over the past 12 months ending in June fell by about 20 percent year over year. A similar number of Class A properties changed hands, while sales velocity slowed for Class B/C assets.
- A flight to quality among investors over the past four quarters contributed to a higher average sale price of \$329 per square foot, a 6 percent annual gain. The mean cap rate inched up 10 basis points to 6.6 percent over the same span. Some properties changed hands with yields under 6 percent, including in central parts of the District.
- More properties continued to change hands in northern Virginia relative to other areas, with deal velocity slowing the most inside the District. Submarkets that drew more investor interest relative to recent years included North Prince George's County and Southeast Fairfax County, where entry costs dropped below \$200 per square foot.
- The sales velocity for medical offices picked up slightly over the past year, with an average entry cost over \$300 per square foot.