MARKET REPORT

Office

Washington, D.C. Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

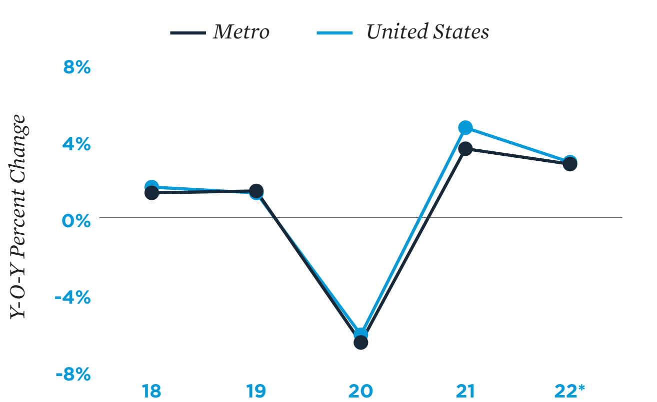
2Q/22

Net Absorption Emerges Out of the Red, Paving a Road Toward an Office Recovery

Reasons for optimism arise. Recent activity indicates the worst may be in the rear view for D.C.'s office market. Indoor mask mandates for the District were lifted in March, which will likely provide additional momentum toward the sector's recovery moving forward. During the trailing 12-month period ending in March, firms absorbed over 700,000 square feet on a net basis, the largest four-quarter total since the onset of the health crisis. Notable leases during this span included the SEC committing to more than 1.2 million square feet of space in NoMa, marking the largest agreement in over 15 years. Looking ahead, President Joe Biden recently expressed in his State of the Union address the vast majority of federal workers will be phased back to in-person work, which may encourage other local firms to begin returning employees to the office as well.

High-profile firms show confidence in D.C. Boeing recently announced it will relocate its headquarters from Chicago to Arlington and establish a major research and technology hub in the city. Additionally, Raytheon Technologies will also be moving its global headquarters from Waltham to Arlington in the third quarter of this year. Both firms noted the region's close proximity to their consumer base and deep talent pool as reasons for the move, and plan to utilize office space they already lease in the area. These two aerospace giants will join firms like Lockheed Martin, General Dynamics and Northrop Grumman, making the Washington, D.C. metro home to the five largest defense contractors in the nation.

Employment Trends



** Forecast*

Sources: BLS; CoStar Group, Inc.

Office 2022 Outlook

93,000 JOBS *will be created*

EMPLOYMENT:

As of May, headcounts in traditionally office-using segments were within 1,000 positions of the pre-pandemic peak and are expected to surpass that level by year-end. Total employment across all sectors is projected to increase by 2.8 percent in 2022.

4,650,000 SQ. FT. *will be completed*

CONSTRUCTION:

Annual delivery volume doubles last year's pace, as developers increase Washington, D.C.'s office inventory by 1 percent. The majority of space slated for near-term completion will complete inside of the District in the Capitol Hill Area and Downtown.

0 BASIS POINT *change in vacancy*

VACANCY:

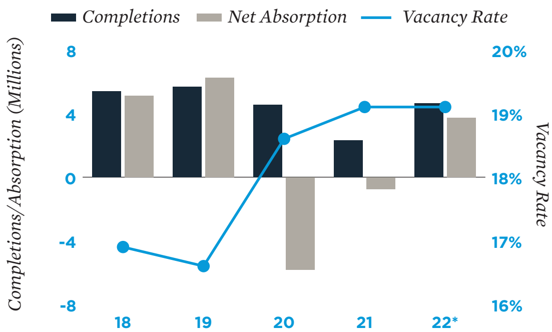
Following two consecutive years of annual vacancy expansion, availability will stay relatively flat in 2022. Annual positive net absorption is projected for the first time since 2019, and the figure is expected to surpass the 3.5 million-square-foot threshold this year.

1.8% INCREASE *in asking rent*

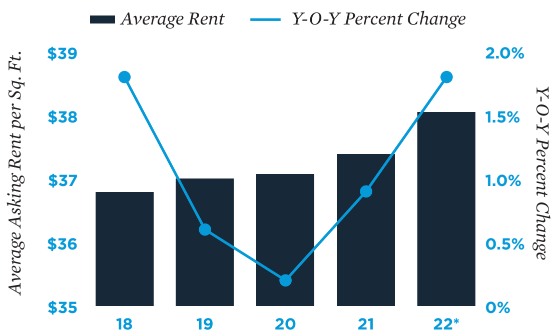
RENT:

Rent growth nears 2.0 percent in 2022, following three consecutive years of sub-1.0 percent gains. The average asking rate will rise to $38.05 per square foot, marking an all-time high for the metro.

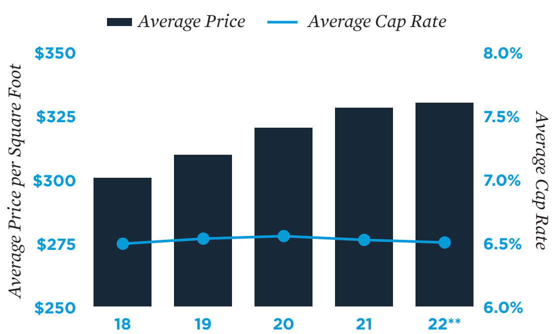
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 1Q*

Sources: CoStar Group, Inc.; Real Capital Analytics

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Price: $250

1Q 2022 - 12-Month Period

CONSTRUCTION

3,054,000 sq. ft. completed

- Developers increased office inventory by 0.6 percent over the past four quarters ending in March, as supply additions tapered by nearly 1 million square feet relative to the previous 12-month period.
- Completions were widespread over this span with Virginia, Maryland and the District each adding over 800,000 square feet.

VACANCY

30 basis point increase in vacancy Y-O-Y

- Over the past 12 months, metrowide vacancy rose 30 basis points to 19.3 percent, the second-highest rate in over two decades. Availability is most elevated in Suburban Virginia, sitting at 20.6 percent as of April.
- Vacancy in Suburban Maryland fell 10 basis points during this span to 16.9 percent, driven by over 750,000 square feet of net absorption.

RENT

0.8% increase in the average asking rent Y-O-Y

- Despite the continual rise in vacancy, asking rents are making strides, rising slightly over the past year to an average of $37.39 per square foot.
- Rent growth in Suburban Maryland is outpacing the metro, recording a year-over-year gain of 1.8 percent, while asking rates in the District and Suburban Virginia improved by 0.7 percent and 0.4 percent, respectively.

Investment Highlights

- Washington, D.C. is an attractive metro for office investors, as the presence of the federal government and a high concentration of Fortune 500 companies provide buyers a sense of stability during periods of uncertainty. Transaction velocity has ramped up over the past year ending in March, outpacing the previous 12-month span by nearly 60 percent. The average sale price rose nearly 3 percent during this time frame to $330 per square foot, with the mean cap rate holding steady in the mid-6 percent range.
- Suburban Virginia noted the most sales activity over the past four quarters, accounting for over half of all transactions in the region. Investors were most active in the Dulles Corridor and Fairfax County, where pricing generally falls below the metro average. Assets in the Alexandria-I-395 Area are highly sought after as well, with properties in the $10 million to $50 million price tranche changing hands most often.
- The I-270 Corridor represents the most liquid submarket in Suburban Maryland, with first-year returns averaging in the low-5 percent span. In the urban core, buyers are targeting offices in Downtown and Uptown D.C., with properties comprising over 100,000 square feet pursued frequently. Here, entry costs often exceed $400 per square foot.