MARKET REPORT

Retail

Philadelphia Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

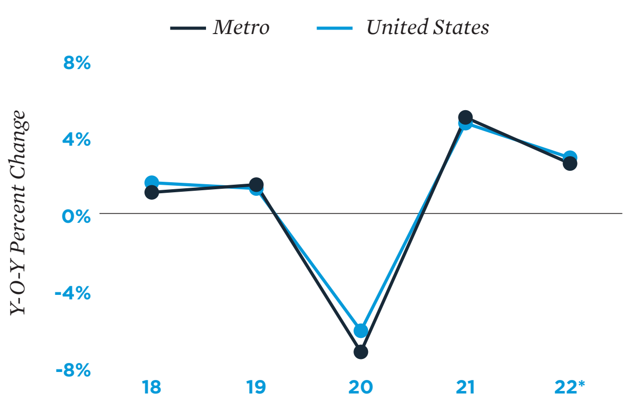
3Q/22

Availability Shrinks Across Greater Philadelphia, Center City Retail Outlook Improves

Urban zones tighten, Center City foot traffic on the rise. Retail leasing reached its most fervent pace since the onset of the health crisis during the past 12 months ended in June. During this span, nearly 2.7 million square feet were absorbed on a net basis, highlighted by retailers committing to space in outlying residential neighborhoods of Philadelphia proper, where foot traffic has been consistent since 2020. In University City and Philadelphia's outermost urban submarkets, availability was tighter than pre-pandemic norms at the onset of July. Recovery is also proceeding in the core and adjacent zones. Comcast, one of the city's largest employers, called 8,000 workers back to Center City offices in September, aiding restaurants and shops dependent on weekday patrons. Additionally, foot traffic from neighborhood residents is 17 percent above 2019 levels, helping to close the gap as office usage continues to improve.

Value brands targeting suburban leases. Moving farther from the urban core, demand for space is more frenetic. North New Castle County, the submarket most acutely impacted by rising availability in the wake of the health crisis, saw a 640-basis-point vacancy compression during the trailing year ended in June. Furthermore, of the 13 submarkets located in Southern New Jersey or Delaware, just two reported increasing vacancy during the same period. Discount retailers constitute a noticeable proportion of recent leases in these locales, a response to consumers seeking out low-cost retailers amid continued inflation.

Employment Trends



* Forecast

Sources: BLS; CoStar Group, Inc.

Retail 2022 Outlook

75,000 JOBS *will be created*

EMPLOYMENT:

Despite increasing economic uncertainty, job gains have accelerated as the year has progressed. Philadelphia's employment base will end the year within striking distance of the pre-pandemic level, as it expands by roughly 2.6 percent.

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

CONSTRUCTION:

Developers finalize less than 1 million square feet for a third consecutive year, expanding inventory by just 0.2 percent. The volume of space delivered will represent the lowest annual total in more than 15 years.

40 BASIS POINT *decrease in vacancy*

VACANCY:

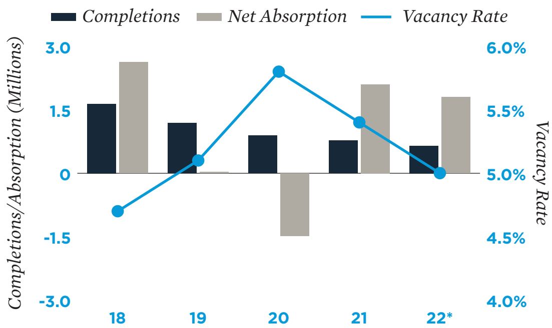
Availability will tighten to 5.0 percent, dropping below the 2019 level as the market posts the second-lowest year-end vacancy rate since at least 2007. So far this year, the multi-tenant segment has led compression in this metric.

3.1% INCREASE *in asking rent*

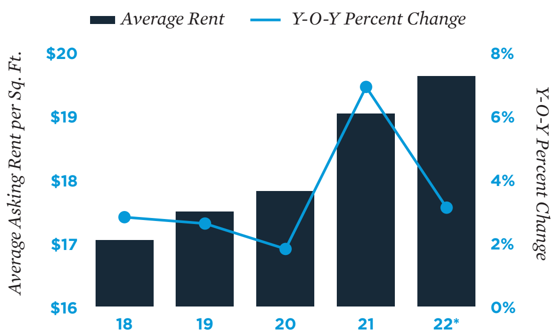
RENT:

Vacancy reaching the 5.0 percent threshold for the first time in four years will facilitate solid rent gains, even as the pace abates, following last year's 6.9 percent surge. The average marketed rent closes out 2022 at $19.62 per square foot.

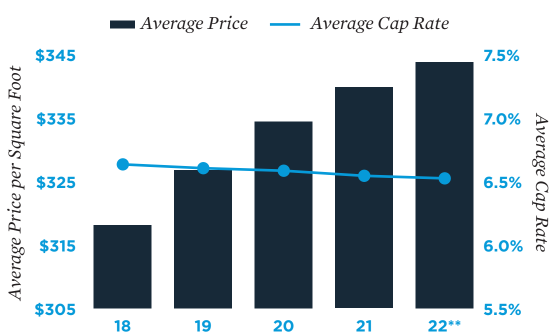
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 2Q*

Sources: CoStar Group, Inc.; Real Capital Analytics

2Q 2022 - 12-Month Period

CONSTRUCTION

567,000 sq. ft. completed

- Builders finalized the lowest amount of space in multiple decades over the 12-month period ending in June. During the trailing decade preceding the pandemic, an average of 1.6 million square feet was completed annually.
- The first two quarters of 2022 set consecutive record lows for deliveries in a three-month span, with less than 60,000 square feet added each period.

VACANCY

70 basis point decrease in vacancy Y-O-Y

- Standout absorption over the past year compressed availability to 5.0 percent entering July, the lowest rate since the onset of the health crisis.
- Multiple suburban zones notched commendable vacancy compression this period. This translated to a 130-basis-point decline in multi-tenant availability, as a notable share of these centers are in these low-density areas.

RENT

4.0% increase in the average asking rent Y-O-Y

- Marketed rents have recorded consistent quarterly gains since late 2020, closing out June at $19.30 per square foot.
- Significant multi-tenant tightening fueled higher rent gains, with asking rents advancing 10.3 percent to an average of $18.93 per square foot. Single-tenant rents grew just 2.2 percent in the same span.

Investment Highlights

- The metro observed record transaction velocity during the 12-month period ended in June, with deal flow exceeding the pre-pandemic high by nearly 40 percent. However, trading began to slow during the second quarter of 2022, as the cost of capital began to rise and evolving economic concerns began to affect the underwriting process. Nevertheless, investor activity remained well above the pre-pandemic norm at the onset of the second half, though rising interest rates will intensify financing headwinds.
- Cap rates held steady during the 12-month period ended in June in both the single- and multi-tenant sectors, averaging in the low-6 and 7 percent band, respectively. A slight dip in the overall cap rate this period stems from an increasing proportion of single-tenant properties changing hands, as buyers pursue assets in more densely-developed zones.
- The greater Philadelphia region is home to a number of vintage multi-tenant assets in the sub-$10 million range. Strip and community centers in this price tranche are typically seen trading in Southern New Jersey or outlying regions of Montgomery and Chester counties. These locales are home to the metro's affluent suburbs, many of which grew as remote working options became prevalent.

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