MARKET REPORT

Office

Washington, D.C. Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

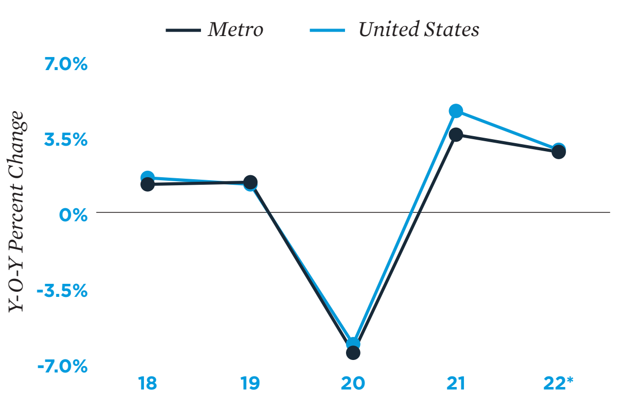
4Q/22

Developers Remain Confident in D.C.'s Office Market as Demand for Class A Space Surfaces

Flight-to-quality is evident. Firms absorbed a net of nearly 2.4 million square feet of office space during the past year ended in June. This recent activity indicates tenants are prioritizing higher-quality space, with Class A leasing accounting for more than 95 percent of net move-ins during this span. Both private and public sector organizations leased large blocks of space during the first half of 2022. The Department of Justice committed to 331,000 square feet at the Judiciary Center in the East End. Additionally, T-Mobile signed a lease totaling just over 200,000 square feet in Herndon, and Hughes Network Systems committed to occupying 140,000 square feet in Germantown. Looking ahead, investments from various local universities to bolster the technology talent pipeline should further increase demand for upper-tier space, as this may draw even more new or expanding tech tenants to the metro.

Moveouts and new supply weigh on fundamentals. Firms consolidating their office space contributed to the rise in vacancy observed in the DMV; however, recent market conditions have also driven development. More than 3.8 million square feet of new supply delivered in the past year ending in June. Robust deliveries, coupled with declining space demand, spurred a 20-basis-point rise in availability during this span. An additional 1.5 million square feet is set to come online during the second half. Fortunately, these deliveries may not have as adverse an impact on overall vacancy, as they collectively boasted a pre-leasing rate above 80 percent as of August.

Employment Trends



* Forecast

Sources: BLS; CoStar Group, Inc.

Office 2022 Outlook

93,000 JOBS *will be created*

EMPLOYMENT:

Following the addition of more than 51,000 new jobs through the first eight months of 2022, firms are on pace to expand total employment by 2.8 percent by year-end. Roughly 18,000 of the new jobs added will be in fields that traditionally used offices.

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

CONSTRUCTION:

Supply additions total at least 4 million square feet for the fifth time in the past six years, as developers increase office inventory by 1 percent in 2022. Amazon's HQ2 project is the largest development in the metro's active pipeline as of September.

60 BASIS POINT *increase in vacancy*

VACANCY:

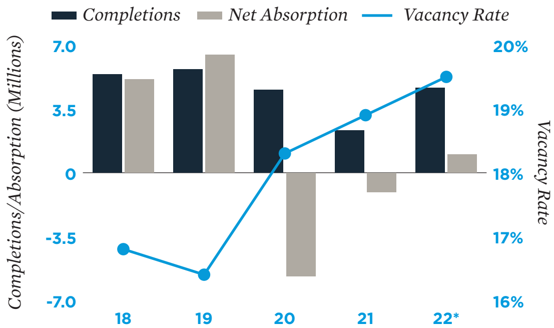
Tenant relocations and consolidations are likely to place upward pressure on availability this year. Washington, D.C.'s vacancy will reach its highest level in more than 15 years in 2022, rising to 19.5 percent.

0.6% INCREASE *in asking rent*

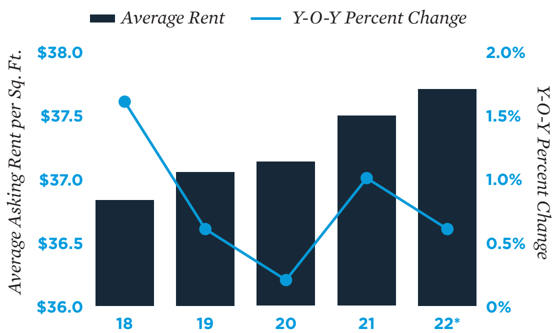
RENT:

Annual rent growth remains positive this year; however, the pace of increase will slow from the 1 percent gain recorded in 2021. The average asking rate will rise to $37.70 per square foot, marking a record high for the Washington, D.C. metro.

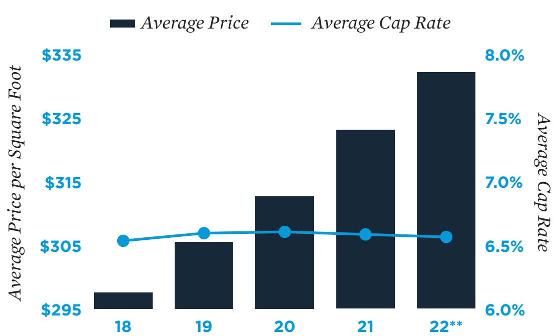
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 2Q*

Sources: CoStar Group, Inc.; Real Capital Analytics

Washington, D.C. Office:

Brian Hosey *First Vice President, Division Manager*

7200 Wisconsin Ave, Suite 1101

Bethesda, MD 20814

Tel: (202) 536-3700 | brian.hosey@marcusmillichap.com

Prepared and edited by:

Carlos Pietri

Research Analyst | Research Services

For information on national office trends, contact:

John Chang

Senior Vice President, Director | Research & Advisory Services

Tel: (602) 707-9700 | john.chang@ipausa.com

2Q 2022 - 12-Month Period

CONSTRUCTION

3,861,000 **sq. ft. completed**

- Builders increased office inventory by 0.8 percent over the past year ending in June, with nearly 80 percent of all supply additions occurring inside of D.C. proper and Suburban Virginia.
- There is nearly 10 million square feet of office space underway metrowide, with roughly 78 percent of the pipeline pre-leased as of August.

VACANCY

20 **basis point increase in vacancy Y-O-Y**

- During the trailing 12-month period ending in June, availability inside the District rose 40 basis points to 19.7 percent. Meanwhile, the Suburban Virginia vacancy rate advanced 10 basis points to 20.2 percent.
- In Suburban Maryland, local vacancy remained relatively steady during this time frame at 17.7 percent.

RENT

0.5% **increase in the average asking rent Y-O-Y**

- Despite softening space demand, the average asking rent continued to climb upward, reaching $37.48 per square foot in June.
- Suburban Maryland and the District recorded rent gains of 1.9 percent and 0.7 percent, respectively, year-over-year ending in June. Meanwhile, the mean marketed rate in Suburban Virginia fell 0.5 percent during this span.

Investment Highlights

- Washington, D.C. remains one of the most liquid office transaction markets in the nation. The presence of the federal government and ongoing growth of the cloud software and biotechnology sectors is bolstering investor confidence in the future performance of assets in the metro. As such, transaction velocity returned to pre-pandemic levels during the past year ending in June, outpacing the previous yearlong span by more than 50 percent. The average sale price rose to $332 per square foot over the past year, while the mean first-year return held firm in the mid-6 percent span.
- Recently robust population growth and the Silver Line Metrorail extension are generating buyer interest in the Dulles Corridor-area office assets. Pricing here often falls below the market mean, with first-year returns that can climb to the mid-8 percent range. Investors are also finding similar opportunities in other areas, such as Alexandria-I-395, Downtown D.C., I-270 Corridor and Greater Fairfax County.
- Medical office trading reached a record high in the past year. Buyers are finding opportunities for these properties in emerging residential submarkets, such as Southeast Montgomery County, South Prince George's County, Frederick and the Dulles Corridor.

Price: $250