INVESTMENT FORECAST

OFFICE

Philadelphia Metro Area

IPA | INSTITUTIONAL PROPERTY ADVISORS

2020

Tenants Search Outward for Large Footprints; Investors Seeking Deals in High-Vacancy Suburbs

Strong pre-leasing, constrained core development keep vacancy on downward trend. Fundamentals are sturdy in Philadelphia heading into the new decade. In 2020, delivery volume will fall below 1.5 million square feet, just two years after peaking at nearly double that volume in 2018. Of the space coming to market, over 85 percent is pre-leased, and economic drivers are on solid footing with healthcare and life science firms rapidly expanding and absorbing office space. This will support a drop in the vacancy rate to a cycle-low level in 2020. The majority of this year's deliverables will be in the suburbs, with Conshohocken receiving nearly two-thirds of the total space. The largest building under construction here is the 427,000-square-foot Sora West project, which is fully pre-leased. Amerisource Bergen Corporation will anchor the building and take on 93 percent of the rentable space to house its new headquarters. Less than one mile away, the 260,000-sqaure-foot Seven Tower Bridge development is in the final stages. Financial firm Hamilton Lane has pre-leased roughly half of the building's rentable space. Organizations pursuing larger footprints will continue to spill out into suburbs as availability in Center City and University City remains tight, with little relief coming in the pipeline.

Investors seek suburban assets for spillover demand, find mid-tier assets with potential to outperform. The average cap rate is nearing the mid-8 percent range after trending upward every year since 2016. Buyers favoring lower-entry-cost suburban assets over CBD spaces and their preference toward low- to mid-quality space with value-add potential skewed this average. In Blue Bell, Class B assets traded twice as often in 2019 as in the previous year. Risk-taking investors focused here as the region's vacancy rate is hovering 400 basis points above the metro average, making entry-costs obtainable at an average of $80 per square foot. Similarly, Class B assets in Mount Laurel are frequently trading for under $10 million, as the vacancy rate hovers near 18 percent for the locale.

2020 Market Forecast

Employment up 0.7% — Organizations will create 20,000 roles in 2020 after adding 23,200 jobs last year. Nearly 40 percent of the positions are expected to be office-using.

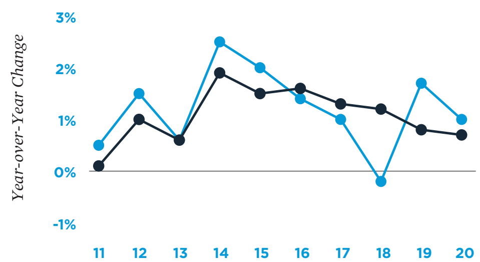
Construction 1.4 million sq. ft. — Development activity will slow down, as the pipeline contains roughly 400,000 square feet less space than last year.

Vacancy down 30 bps — The wane in development in concordance with noteworthy pre-leasing activity allows vacancy to drop to 12.8 percent. In 2019, a 70-basis-point ease was logged.

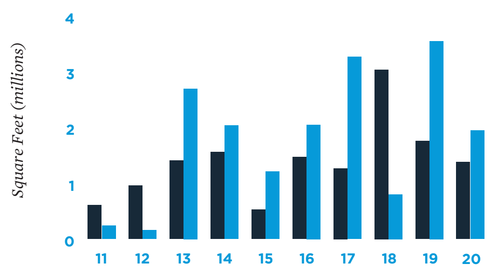
Rent up 2.7% — Rental gains nearly match the previous year's 2.8 percent hike, as the average asking rent moves up to $26.73 per square foot.

Investment — Suburbs along major thoroughfares north of the core will be at the forefront for investors. Properties near urban amenities such as dining and shopping will command aggressive offers.

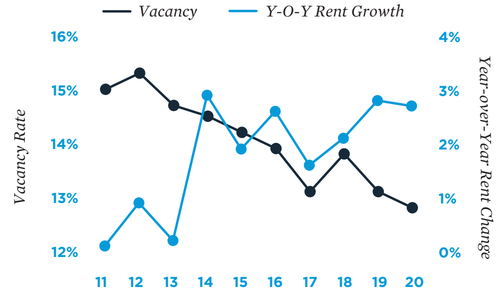
Employment Trends



Office Supply and Demand



Vacancy and Rent Trends



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

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