INVESTMENT FORECAST

OFFICE

Washington, D.C. Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

2020

Technology Sector Driving New Leasing; Vacancy Falls To Multiyear Low Despite Increased Construction

Diversifying economy supports office leasing, pushing vacancy closer to cycle low. Washington, D.C.'s economy has long been centered around the federal government, but that focus is beginning to shift. More public agencies are scaling back on space and consolidating offices, while new private organizations are entering the metro, including technology companies such as Amazon. The e-commerce giant is building a campus in National Landing while its Web Services division is expanding its presence in the Dulles Corridor. Consultancies, law firms, and government contractors are also prominent office lessors, supporting an overall improvement in absorption activity this year compared with 2019. The added demand will help tighten the metrowide vacancy rate to 17.1 percent, its lowest level since 2012, despite the largest annual construction pipeline since 2009. More than 2 million square feet will open within the District and in Northern Virginia, especially in Capitol Hill, Reston and along State Route 28.

Growing employment hubs entice new transactions. Multiple well-established sources of office tenant demand continue to foster investment into the property type. A growing technology presence in Crystal and Pentagon cities as well as the planned Virginia Tech satellite campus in Potomac Yard are likely fueling increases in sales velocity in nearby Alexandria. A plethora of government agencies and professional service firms seeking the highest-quality space encourage institutions targeting trophy assets to look in the core District neighborhoods surrounding the National Mall and Capitol. Cap rates on these trades often fall below 6 percent, with sales prices sometimes exceeding $1,000 per square foot. Investors looking for higher first-year returns or lower entry costs have found opportunities in suburban Maryland. Overall, 2019 was one of the more active years in this business cycle for office transactions, and sentiment continues to be positive for 2020.

2020 Market Forecast

Employment up 1.4%: Employers will add about 47,100 jobs this year, about 18,300 of which will be in traditionally office-using roles.

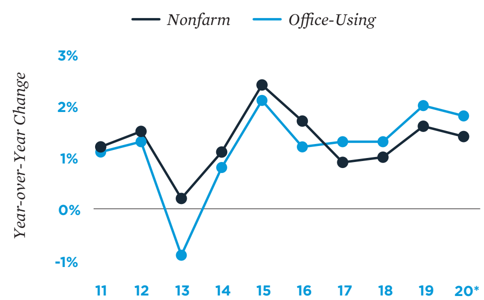
Construction 5.7 million sq. ft.: Approximately 1 million more square feet will be delivered in 2020 than completed last year, surpassing total openings from 2018 to mark a new cycle-high level of arrivals.

Vacancy down 20 bps: Vacancy will decline for the third consecutive year to 17.1 percent in 2020, bolstered by triple-digit vacancy contractions in parts of suburban Virginia and Maryland.

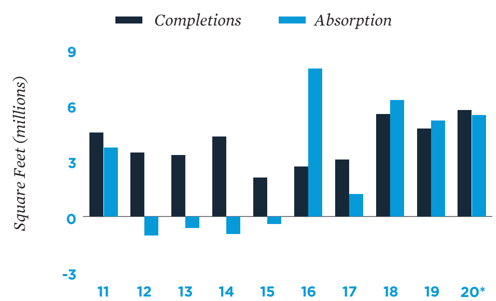
Rent up 1.6%: The average asking rent will advance to $38.61 per square foot following a tepid 0.3 percent growth rate in 2019.

Investment: Foreign investment in office assets continues to represent a notable portion of overall trading activity. Buyers from Switzerland and Singapore stepped up their acquisitions in 2019.

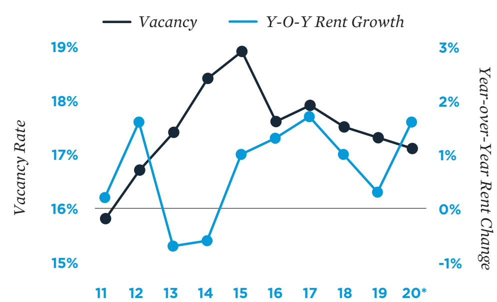
Employment Trends



Office Supply and Demand



Vacancy and Rent Trends



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

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Metro-level employment, vacancy and asking rents are year-end figures and are based on the most up-to-date information available as of December 2020. Asking rent is based on the full-service marketed rental rate. Average prices and cap rates are a function of the age, class and geographic area of the properties trading and therefore may not be representative of the market as a whole. Sales data includes transactions valued at $1,000,000 and greater unless otherwise noted. Forecasts for employment and office data are made during the fourth quarter and represent estimates of future performance. No representation, warranty or guaranty, express or implied may be made as to the accuracy or reliability of the information contained herein. This is not intended to be a forecast of future events and this is not a guaranty regarding a future event. This is not intended to provide specific investment advice and should not be considered as investment advice.