

# MARKET REPORT

OFFICE

Northern New Jersey Metro Area

IPA  
INSTITUTIONAL  
PROPERTY  
ADVISORS

2Q/21

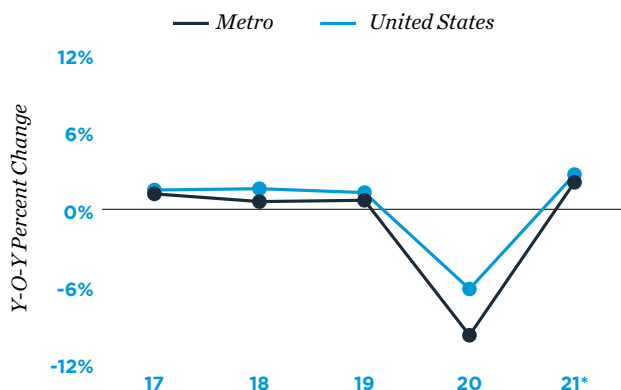
## Suburban Mid-Tier Office Demand Bolsters Market As Some Premium Leases Are Reevaluated

### Class B/C office performance helps stabilize broader sector.

Leasing activity continued at a tempered pace during the first three months of 2021 as some major office tenants looked to sublet space, including PSE&G, Mallinckrodt Pharmaceuticals and ADP. While rapid vaccine deployment is helping to resolve the health crisis, the future of dispersed working is still somewhat unclear, affecting office space needs. Most tenant departures have been in the less affordable Class A segment, where buildings tend to be less accessible in a socially distanced manner. Suburban Class B and C properties, which represent a large portion of local inventory, have been more resilient, posting rent growth amid a smaller hike to vacancy. Less foot traffic congestion and proximity to where many employees live make these offices well suited for firms that adopt a flexible work schedule.

**Construction projects add to hurdles in Hudson County.** An accelerated development pipeline for this year places a new challenge onto an already-hassled office sector. While the overall expansion to inventory is minor, a trio of speculative projects in Hudson County will weigh on fundamentals. Vacancy in the more urbanized submarket was already up 340 basis points annually to 20 percent at the end of the first quarter. As infection rates ease, however, the ability to return to urban high-rises will improve. Elsewhere in the market deliveries are smaller in scope and have some tenants in place, lowering their performance impact.

### Employment Trends



\* Forecast

Sources: BLS; CoStar Group, Inc.

## Office 2021 Outlook



**52,000  
JOBS**

*will be created*

### EMPLOYMENT:

The roughly 14,000 jobs created in the first three months of the year set the stage for a 2.7 percent rate of employment growth in 2021. Last year 213,400 positions were shed. Renewed hiring will bring the total job count to within 8 percent of the pre-pandemic level.



**880,000  
SQ. FT.**

*will be completed*

### CONSTRUCTION:

Office completions will climb to a six-year high in 2021, representing a 0.5 percent expansion to existing inventory. The majority of arrivals will be in Hudson County, growing the local supply by over 2 percent this year.



**90 BASIS  
POINT**

*increase in vacancy*

### VACANCY:

Leasing activity will improve this year, although several speculative deliveries will add to vacant space. Additional available floor plans will translate into a higher vacancy rate of 17.9 percent. Vacancy was last above the 18 percent threshold in early 2015.



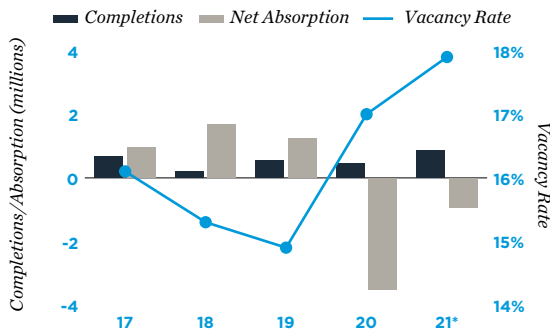
**1.1%  
DECREASE**

*in asking rent*

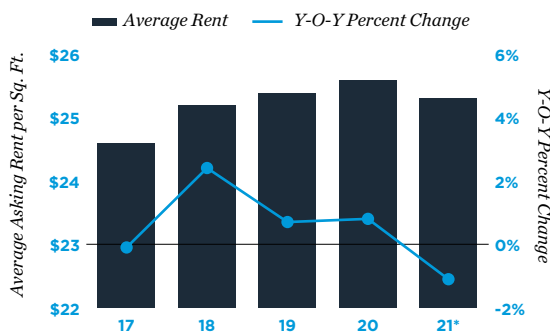
### RENT:

Months of tempered leasing activity will lead to a lower average asking rent of \$25.30 per square foot this year. Prior to 2021, the last time the average marketed rate fell by more than 1 percent on an annual basis was in 2015.

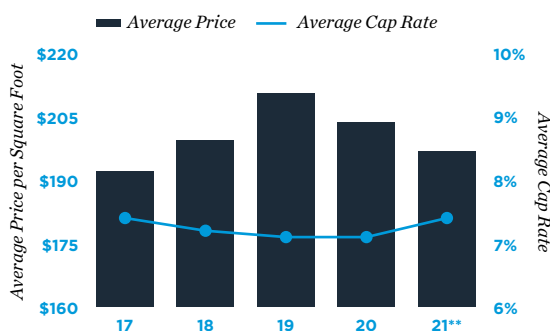
### Supply and Demand



### Rent Trends



### Sales Trends



\* Forecast

\*\* Through 1Q

Sources: CoStar Group, Inc.; Real Capital Analytics

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## 1Q21 – 12-Month Period

### CONSTRUCTION

**498,000 square feet completed**

- The highly anticipated arrival of LG Electronics' 360,000-square-foot North American headquarters in Englewood Cliffs in September contributed the lion's share of completions over the past 12 months.
- Two low-rise buildings, each under 70,000 square feet in size, were the main deliveries of note in the first quarter of 2021.

### VACANCY

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

- About 5.6 million additional vacant square feet of office space pushed the vacancy rate up to 17.7 percent, its highest level since early 2015.
- Higher-rent trophy spaces were more impacted last year as the Class A vacancy rate jumped 550 basis points to 25.8 percent. The Class B/C measure rose 50 basis points to 9.7 percent.

### RENT

**0.9% decrease in the average asking rent Y-O-Y**

- A year of negative net absorption stalled rent growth, with an average asking rent of \$25.46 per square foot at the end of the first quarter.
- When just considering Class A space, the average rent receded 2.1 percent to \$28.31 per square foot. The same metric for Class B/C properties inched up 0.5 percent to \$22.64 per square foot.

### Investment Highlights

- Although improved from a 50 percent year-over-year decrease in the second quarter of 2020, sales velocity in the final months of last year and first three months of 2021 remain below the historical average. About 30 percent fewer properties changed hands over the 12-month period ended in March compared with the prior yearlong span.
- A tempered tenant demand outlook over the past four quarters led to a 6 percent drop in the average sale price to \$197 per square foot, just below the 2018 metric. The average cap rate correspondingly rose, up 30 basis points year over year to 7.4 percent.
- Buyers were most active in the Morris County towns of Morristown and Parsippany over the 12-month period ended in March, followed by Bergen County. Transactions were focused on low-rise Class A and B assets in low-density locations, often built in the 1980s.
- Medical office investment activity increased in 2020 after slowing the year before, as buyers pursued Class B and C assets across the market. So far, sales velocity is on pace to rise further in 2021.