MARKET REPORT

OFFICE

Washington, D.C., Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

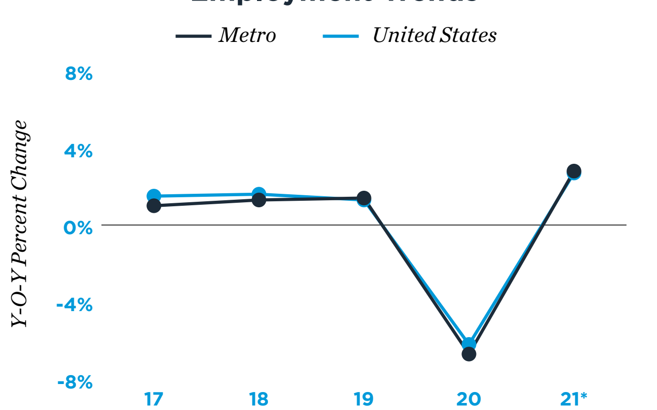
2Q/21

Technology, Public Sectors a Guiding Hand Amid Near-Term Leasing and Supply Concerns

Traditionally strong office hubs face longer road to recovery. A year of ample uncertainty placed the market's offices on softer footing entering 2021. Vacancy in major hubs such as Bethesda-Chevy Chase, Downtown D.C., and the Dulles Corridor all shot above 20 percent. Total available sublease space also increased over 30 percent from 2019. Moving forward, filling these floor plans will take time as the full extent and duration of remote working remains unclear. Many of the lower occupancy areas will also be compounded with new supply. Over 900,000 square feet will open around Capitol Hill in 2021, the most of any submarket. While several of these properties have leases in place, others are still in the process of securing tenants.

Tech and public sectors bolster future office needs. Despite notable health crisis challenges, several long-term demand tailwinds lift the metro's outlook. The new administration has renewed efforts toward restaffing federal agencies that lost personnel during the previous leadership. That may temper plans to relocate some agencies to other markets, as previously these actions have prompted significant talent attrition. Other revived endeavors include a new headquarters for the FBI. Such plans pave the way for older government buildings in central locations to be redeveloped. At the same time, Amazon has continued to develop its second headquarters in National Landing, with the firm intending to bring staff members back to offices nationally in the fall.

Employment Trends



* Forecast

Sources: BLS; CoStar Group, Inc.

Office 2021 Outlook

87,500 JOBS
will be created

EMPLOYMENT:

An anticipated vaccine-driven economic improvement in the second half of the year will help restore about 40 percent of the jobs lost in 2020. Hiring in the traditional office-using sectors will stabilize at a 1.7 percent growth rate following disruptions last year.

3,638,000 SQ. FT.
will be completed

CONSTRUCTION:

Moderately fewer square feet will be delivered this year compared with 2020 as metro inventory is expected to grow by 0.8 percent. Office supply in Maryland is poised to expand the most as several projects over 300,000 square feet in size open.

80 BASIS POINT
increase in vacancy

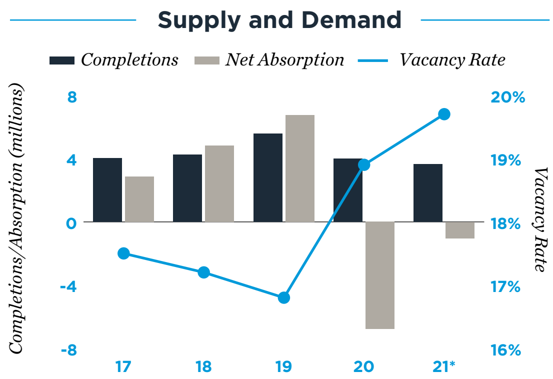
VACANCY:

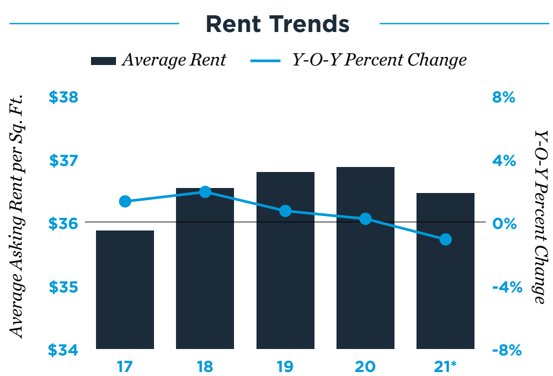
After a large shock last year, a clearer health and economic outlook will enable more companies to finalize leasing decisions. Stabilizing demand will temper the upward momentum in vacancy as the rate climbs by a smaller annual margin in 2021 to 19.7 percent.

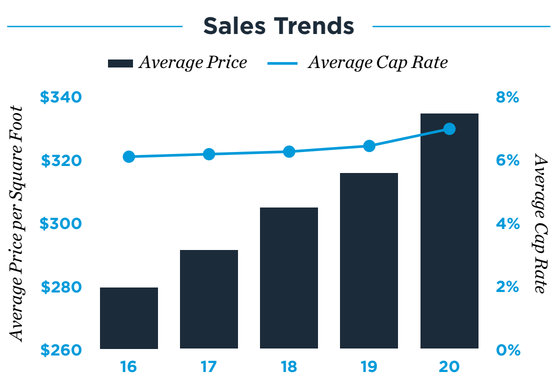
1.1% DECREASE
in asking rent

RENT:

A second year of negative net absorption and a large amount of space available for sublease will place downward pressure on asking rates. The metro's average rent will decrease to $36.46 per square foot, roughly on par with the 2018 measure.







* Forecast

Sources: CoStar Group, Inc.; Real Capital Analytics

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2020

CONSTRUCTION

3,990,000 square feet completed

- After completions reached a decade high in 2019, the delivery pipeline shrank by nearly 30 percent in 2020.
- Four new buildings south of Dupont Circle drove Downtown D.C. openings to 893,000 square feet. A trio of deliveries in Reston contributed to most of the 774,000 square feet deposited in the Dulles Corridor.

VACANCY

210 basis point increase in vacancy Y-O-Y

- Numerous completions led to vacancy jumps of over 200 basis points in Capitol Hill, Downtown D.C., and the Dulles Corridor, contributing to the metrowide rise to 18.9 percent, the highest rate in at least 14 years.
- The market's Class A vacancy rate climbed 230 basis points to 21.4 percent, while the Class B/C rate increased 190 basis points to 15.8 percent.

RENT

0.2% increase in the average asking rent Y-O-Y

- General uncertainty about tenants' space needs led to a minimal rise in the average asking rent to $36.87 per square feet last year.
- The average marketed rent in the central business district inched up by 0.2 percent to $49.98 per square foot, while the average asking rate for suburban space increased by 0.6 percent to $28.72 per square foot.

Investment Highlights

- The number of properties that changed hands in 2020 was down about 30 percent from the year before as the health crisis made long-term space needs less clear. Preliminary data from the first quarter of this year shows that sales activity continues to be dampened.
- A higher proportion of Class A transactions reflected a flight to safety among investors last year that supported a 6 percent increase in the average sale price to $334 per square foot. The growth was also supported by numerous Class B trades, which were on average of a higher quality than what was exchanged in 2019. Nevertheless, fewer sales priced above $100 million translated into an average cap rate for all of 2020 of 6.9 percent, up 50 basis points from the year prior.
- While investment activity was tempered across the market, northern Virginia remained the most actively traded area. Buyer focus shifted from the Dulles Corridor to the Greater Fairfax County submarket as lower-entry cost suburban offices gained attention. At the same time, more Class A buildings also changed hands within the District than in 2019, signaling demand for trophy urban assets.