

COMMERCIAL REAL ESTATE

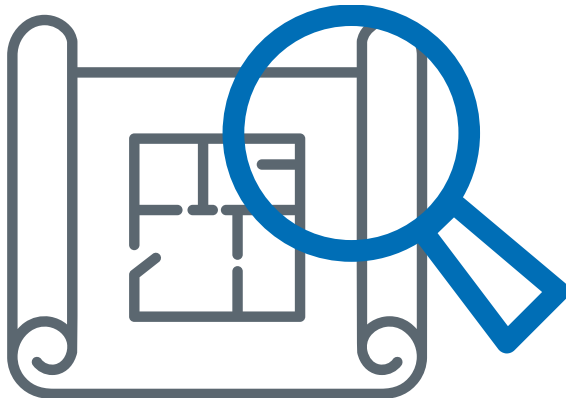
# U.S. MARKET | Office



# THE VIEW FROM HERE



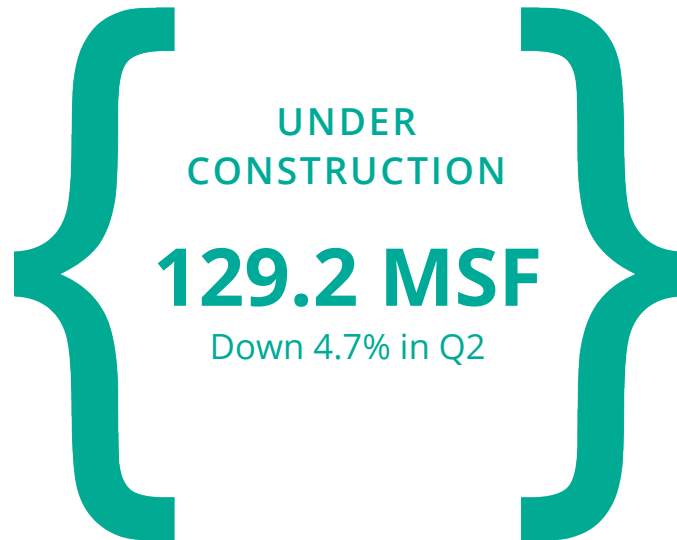
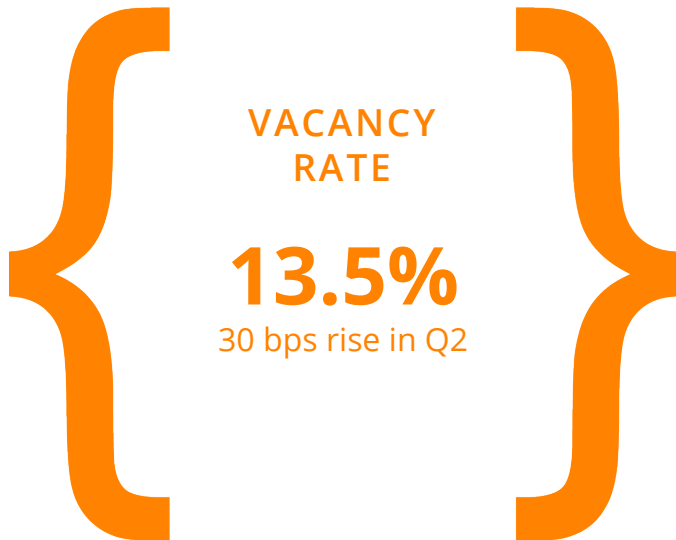
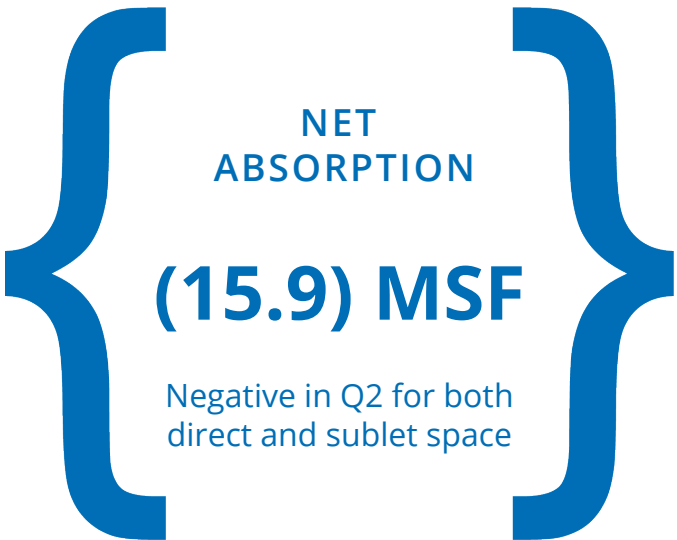

Cyclical, secular and capital market challenges have solidified a new reality for the office sector.



Leasing volumes continue to slow, putting pressure on all constituents to explore creative solutions.



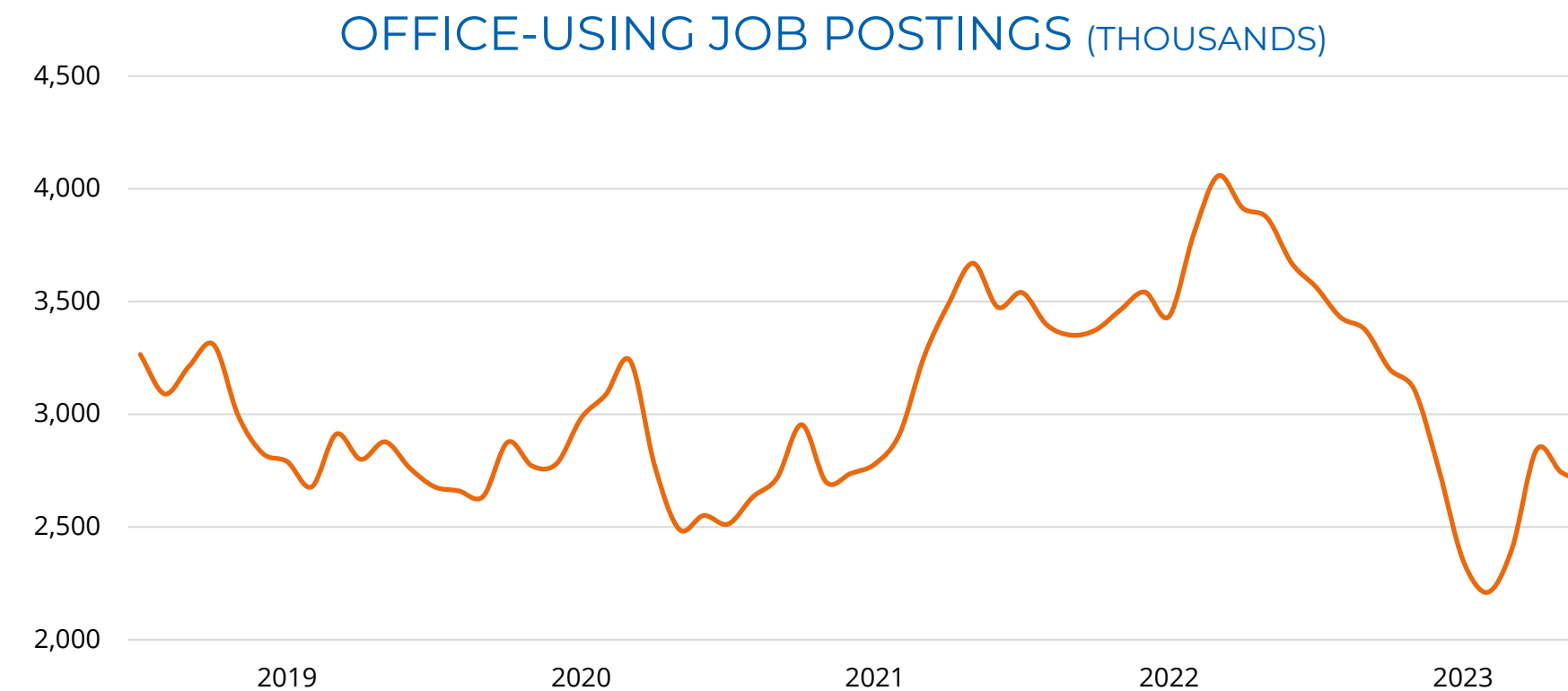
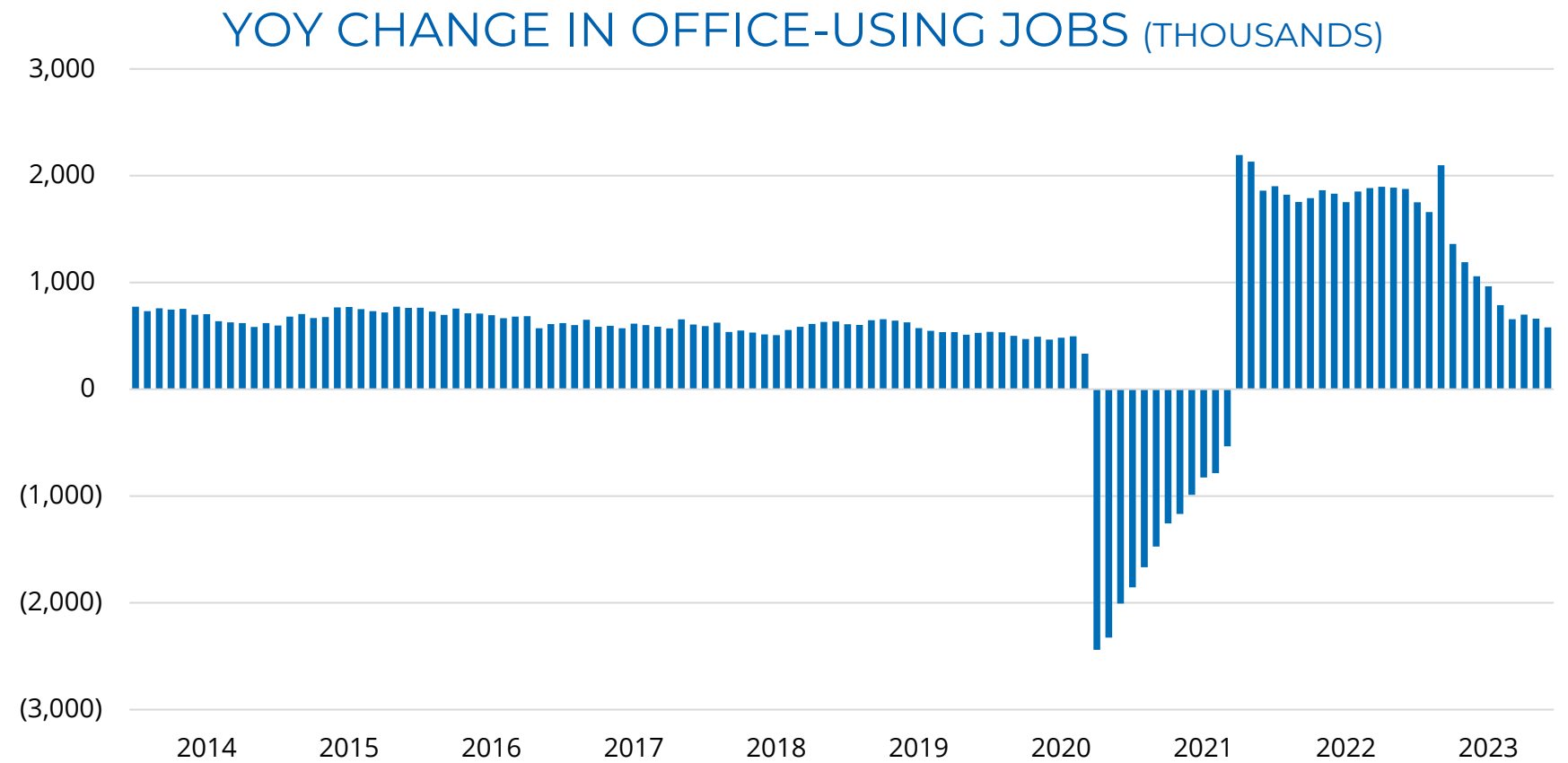
Managers/operators deploying hospitality approaches to make the office more desirable than alternative work options.



## ECONOMIC HIGHLIGHTS

- 579,000 office-using jobs were added to the economy YoY. Growth has decelerated below the pre-pandemic average of 629,000 due to economic headwinds.
- Employers added 170,000 new office-using jobs during Q2, an improvement compared to a revised 63,000 during Q1.
- During the quarter, jobs were cut in the employment services, telecommunications, and broadcasting services industries.
- Hiring grew at a healthy rate for finance, insurance, business consulting, and architecture/engineering.
- Office-using job postings (companies looking to hire) are down 26.5% YoY as companies pulled back on hiring in the face of inflation and higher interest rates.
- Although inflation has subsided at 3.0%, it remains above the 2.0% Fed target. To combat this, the Fed raised the rate in July, after a brief pause, to the highest it has been in 22 years. This rise will likely challenge the already stressed office market.
- The likelihood of a recession in the U.S. continues to be debated.
- According to The Conference Board, 93% of CEOs surveyed said they were preparing for a recession within the next 12 to 18 months. The silver lining is that most, at 87%, believe it will be brief and shallow.
- Regardless, this uncertainty will likely pause or slow hiring efforts, ultimately translating to reduced demand for office space during the balance of 2023 and into 2024.

## HISTORICAL

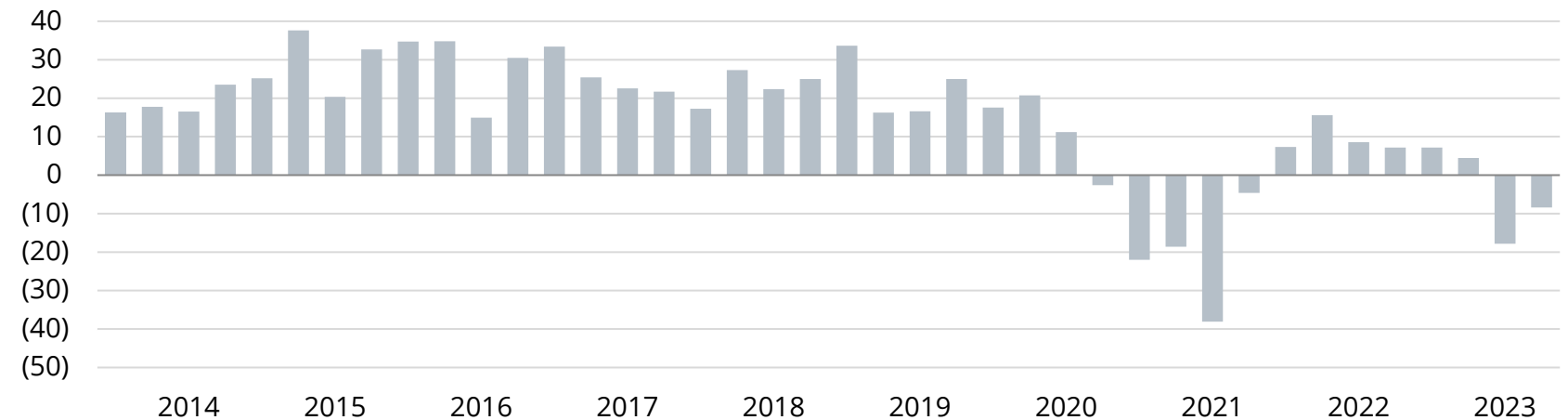


## MARKET HIGHLIGHTS

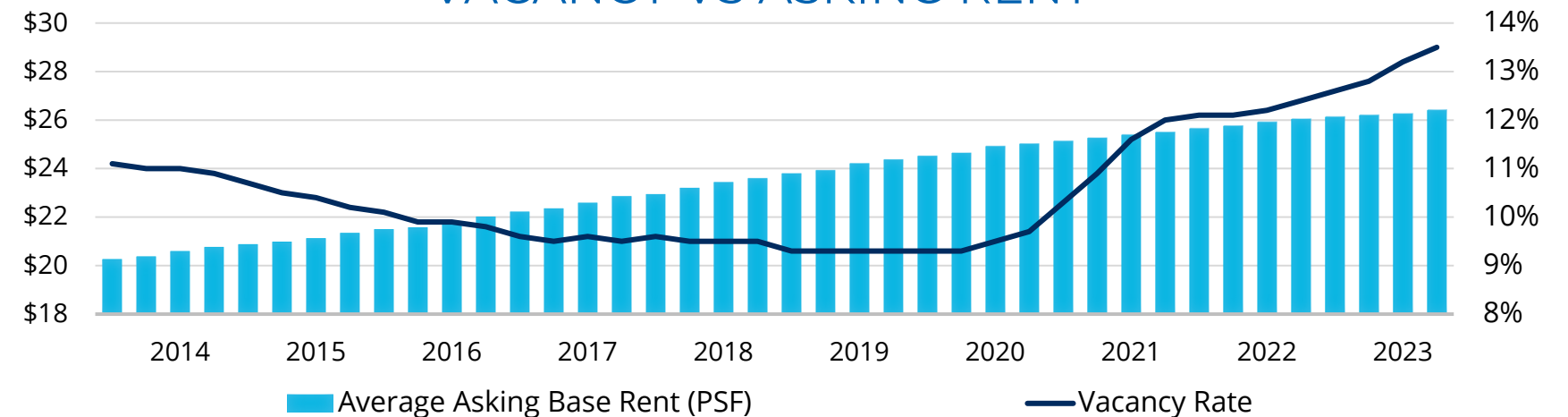
- The office market retracted with negative 15.9 MSF in net absorption in Q2, which accounts for both direct and sublet space.
- Only 19 of 51 tracked markets registered positive net absorption, led mostly by smaller metros. Northern Virginia far outpaced other markets in positive absorption due to the fully pre-leased delivery of Amazon HQ2. However, if you remove this delivery, absorption would be negative for the quarter.
- The overall vacancy rate rose 30 basis points to 13.5% and is up 400 basis points since the start of the pandemic. It will likely take until 2024 for the vacancy rate to stabilize. Flight to quality has tightened the rate for newer product, with buildings built in the last 10 years at 10.2%.
- Asking rents rose 1.4% YoY, a deceleration compared to the average growth rate of 3.2% pre-COVID.
- Asking rents continue to rise as landlords offer above-average concessions in most major markets, which in turn puts downward pressure on the effective rent.
- Demand has and will continue to be concentrated in newer product. With construction levels down 4.7% YoY, this has limited options for tenants and prompted them to explore 2<sup>nd</sup> gen Class A space.
- Recovery will be long and uneven. We expect tenants will right size on average 20%. Tenants in the market are asking for more detail about the loan health of prospective office buildings, which will challenge select landlords. Demolitions and conversions of obsolete office stock should help alleviate some of this pressure but is not a silver bullet solution to recovery.

## HISTORICAL

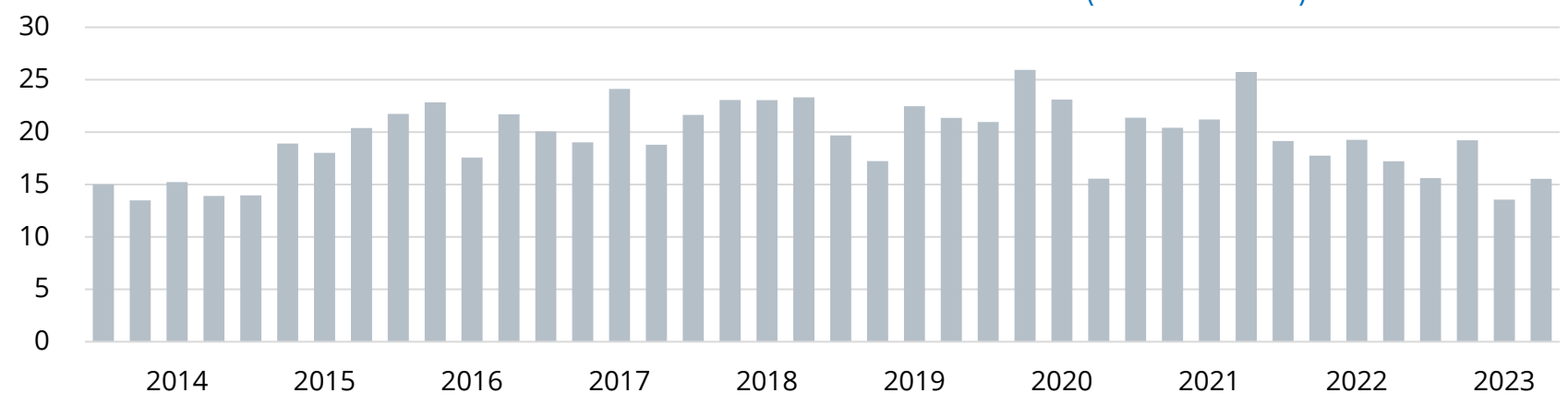
### NET ABSORPTION (MILLION SF)



### VACANCY VS ASKING RENT

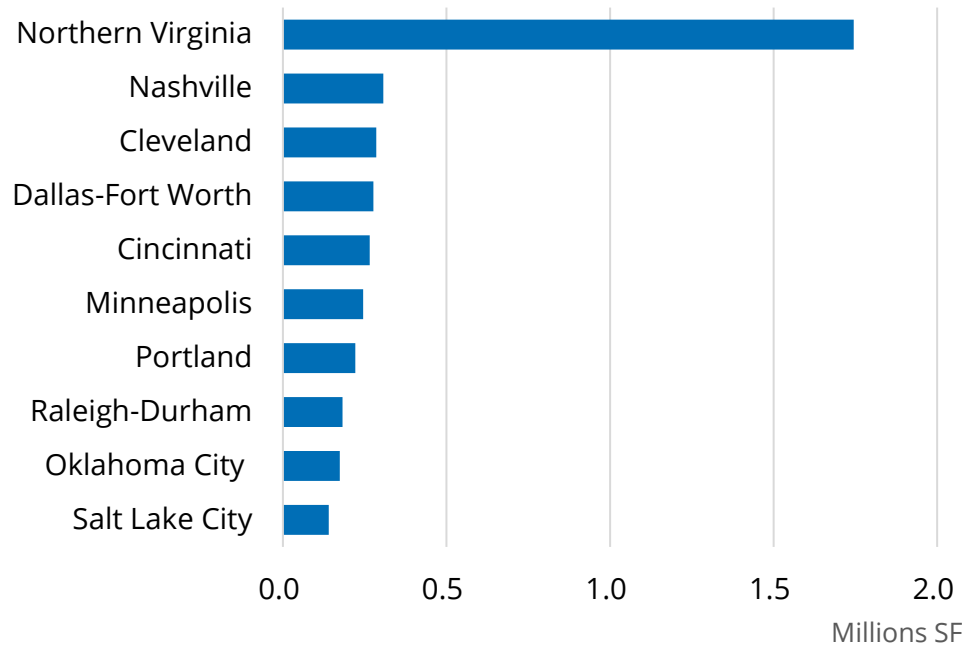


### CONSTRUCTION – DELIVERED (MILLION SF)



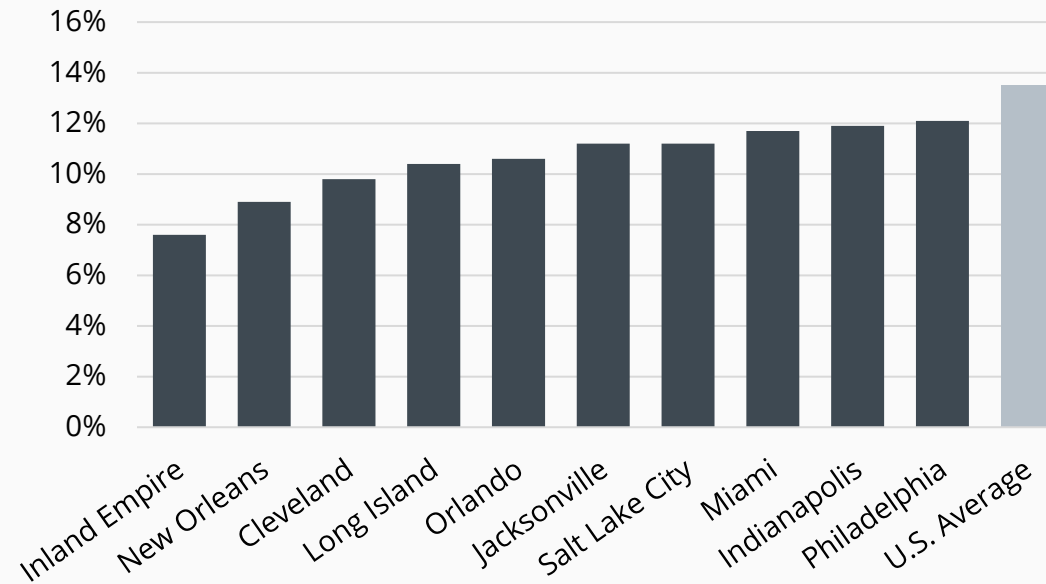
### NET ABSORPTION

Q2 2023 Net Absorption



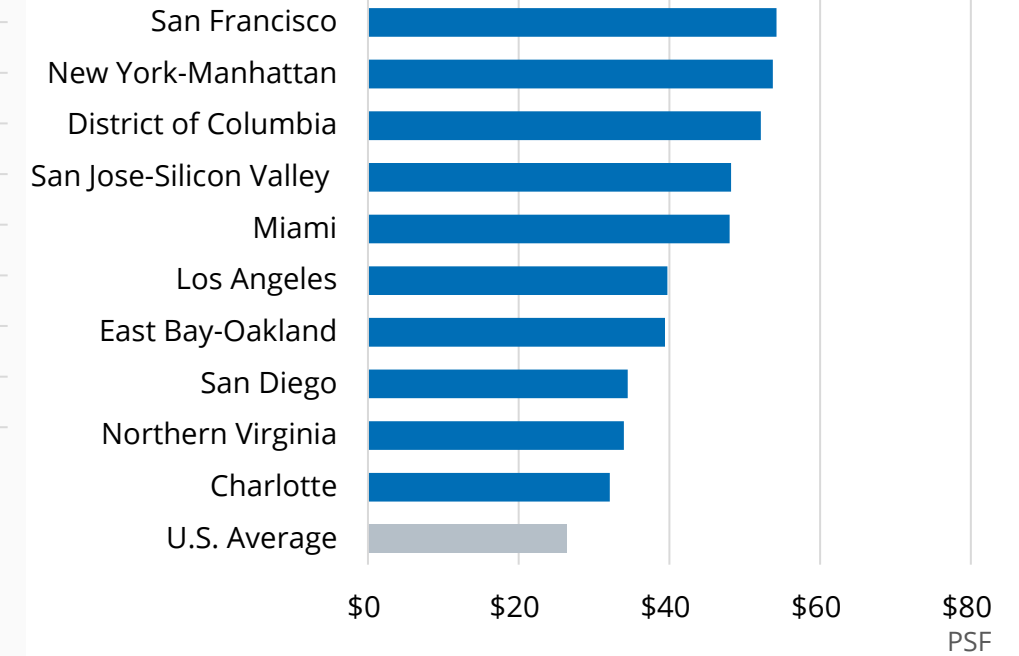
### VACANCY/CONSTRUCTION

Q2 2023 Overall Vacancy Rate

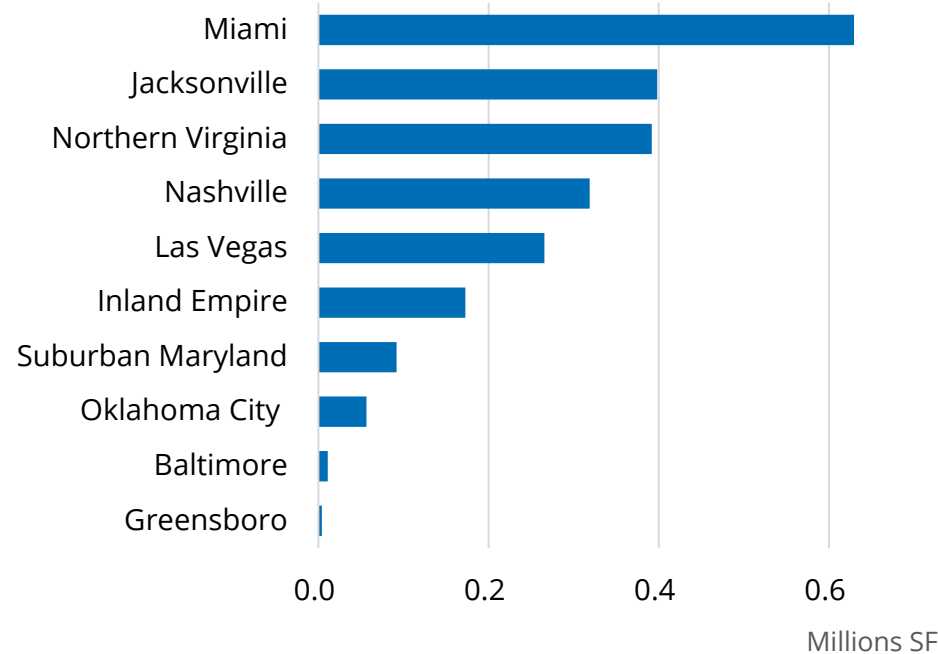


### ASKING RENTS

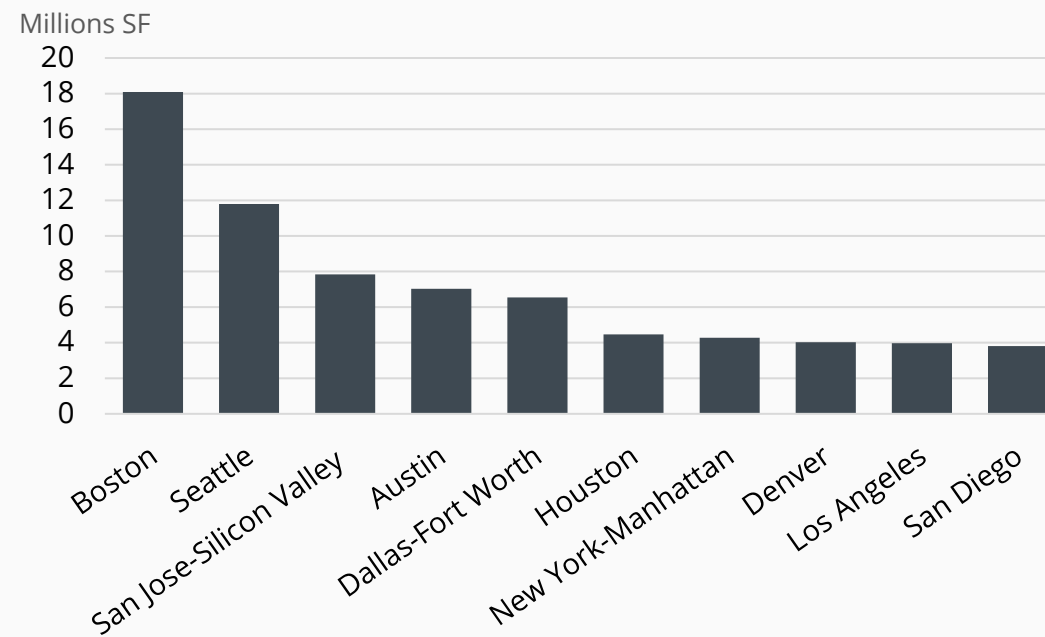
Q2 2023 Asking Rate (Base)



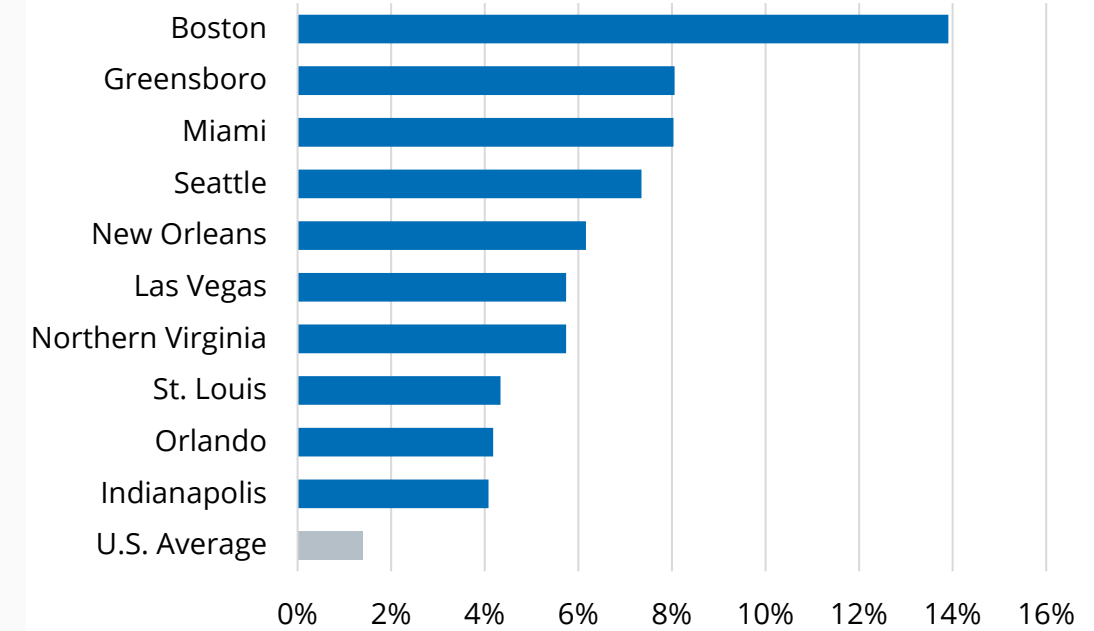
### Trailing 4-Qtr Net Absorption



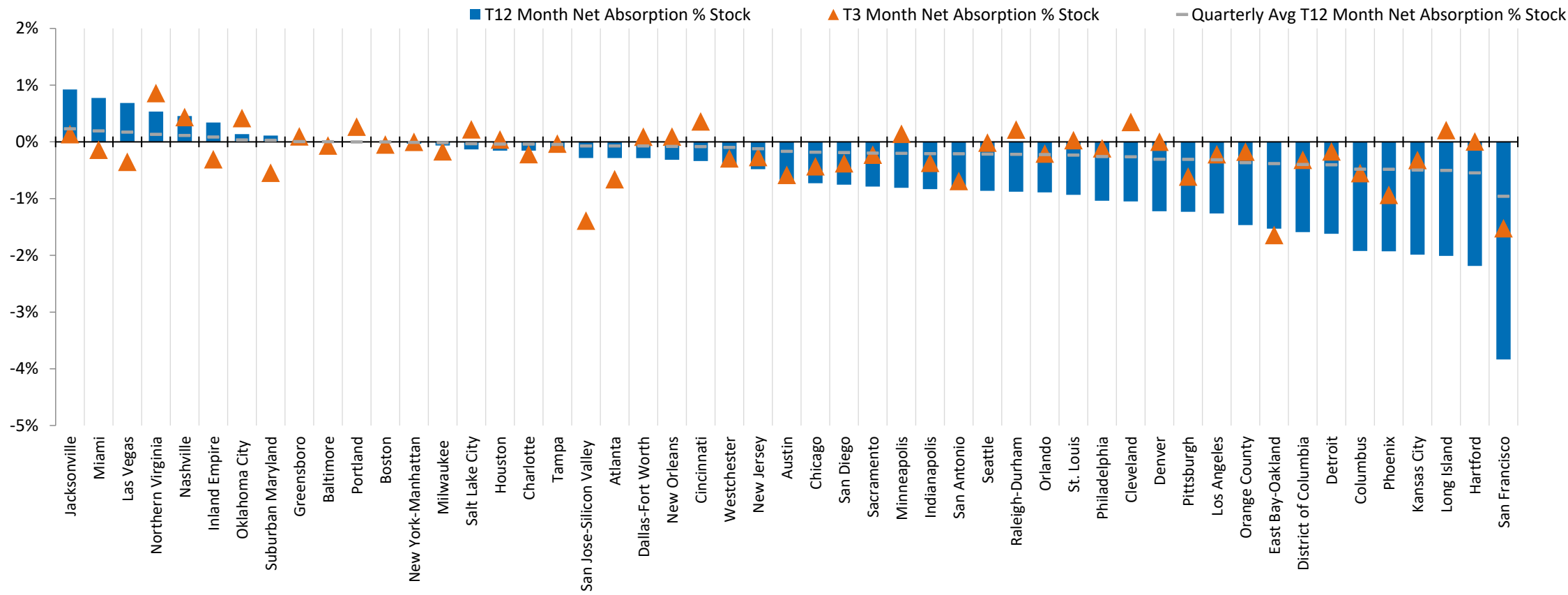
### Q2 2023 Under Construction



### Year-Over-Year Rent Growth

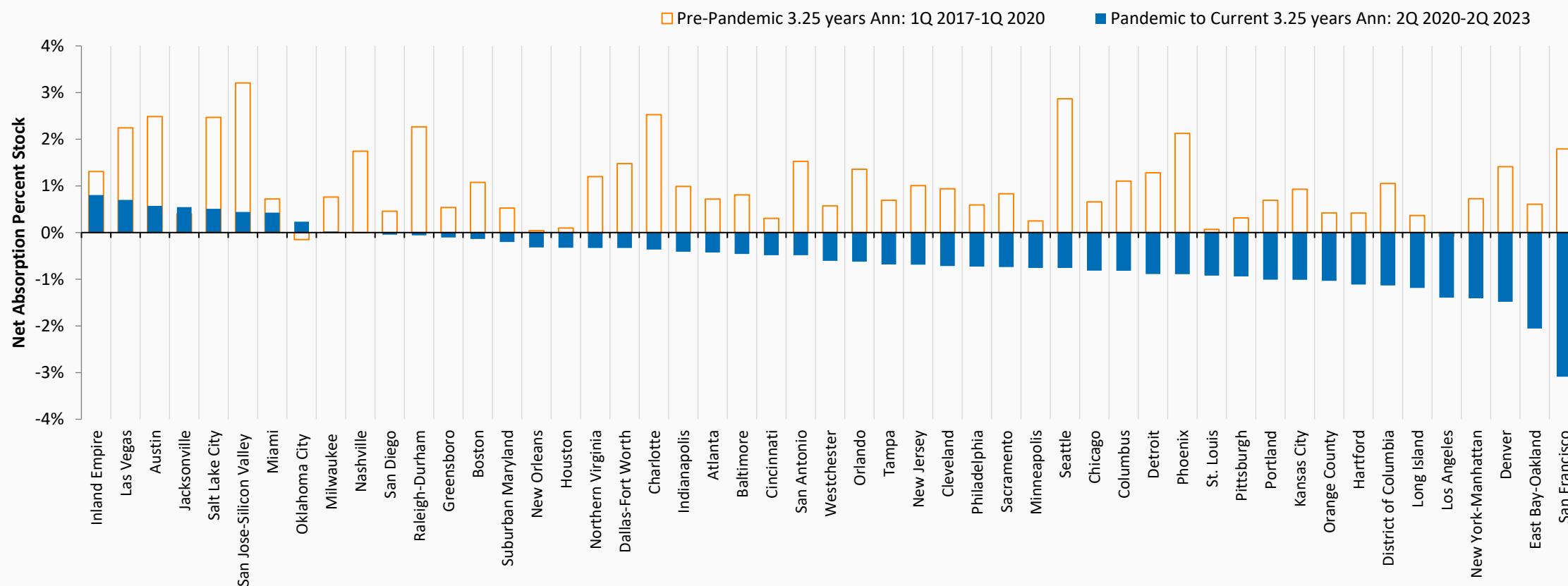


### NET ABSORPTION % STOCK



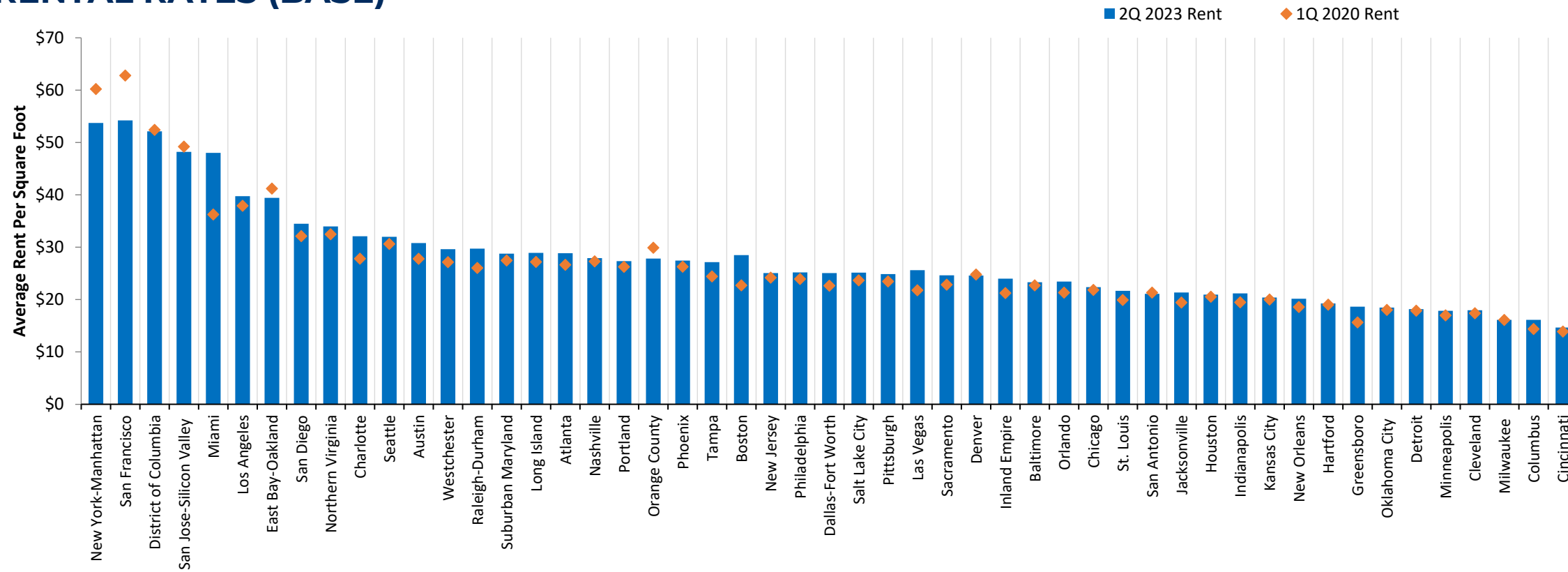
- Demand for office space remains muted with less than 10% of markets managing positive net absorption for both the quarter and the trailing 12-months.
- Top markets for trailing 12-month net absorption that also saw positive net absorption for the quarter include Jacksonville, Northern Virginia, Nashville, Oklahoma City, and Greensboro.
- Demand momentum remains somewhat flat with around half of markets' quarterly net absorption beating their trailing 12-month quarterly average net absorption.

### NET ABSORPTION % STOCK: PRE-PANDEMIC vs PANDEMIC to CURRENT



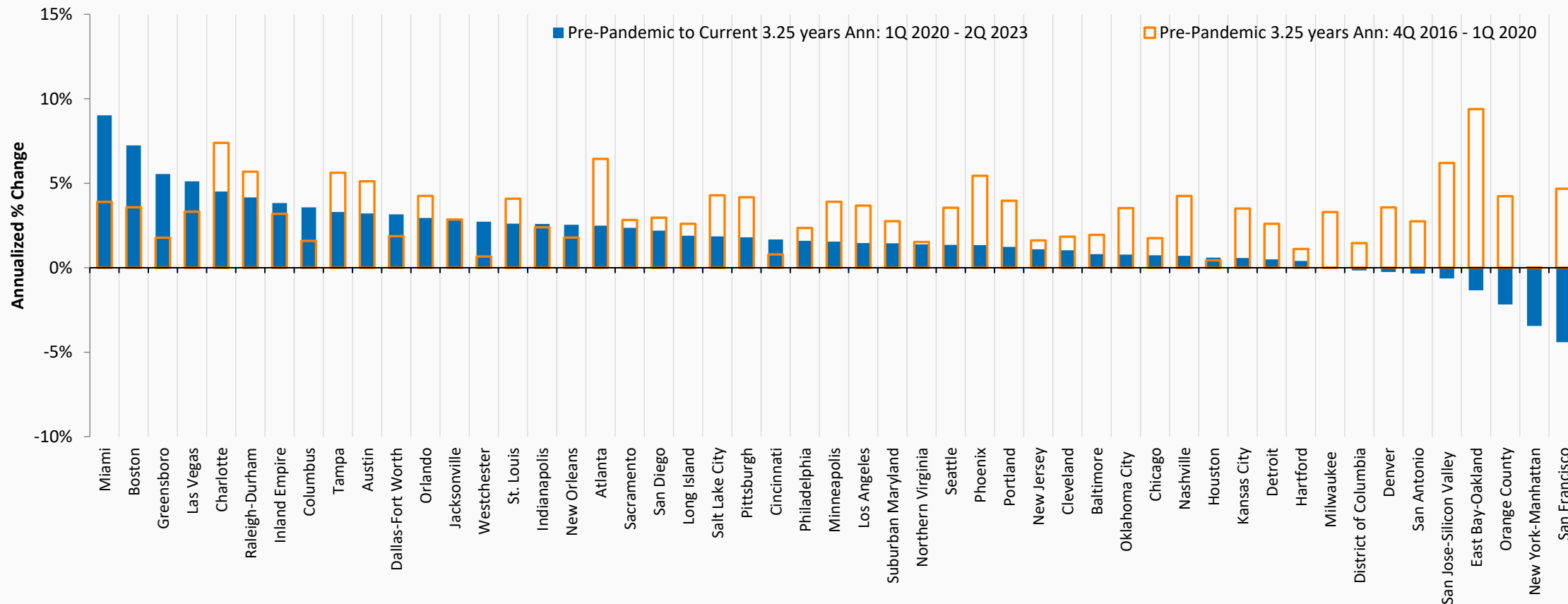
- This graph compares net absorption as a percent of stock annualized for the 3.25 years preceding the start of the pandemic to the 3.25 years since the pandemic began.
- Markets experiencing expansion since the pandemic include Inland Empire, Las Vegas, Austin, Jacksonville, Salt Lake City, San Jose-Silicon Valley, Miami, Oklahoma City, and Milwaukee.

### RENTAL RATES (BASE)



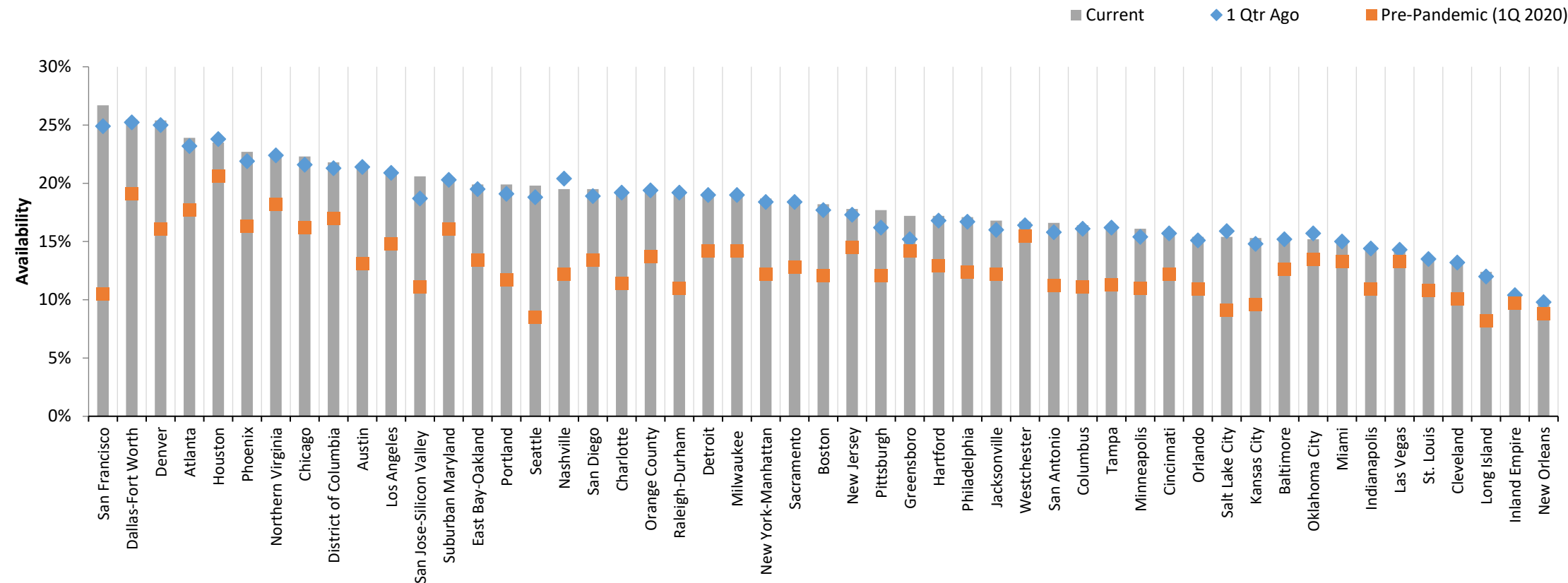
- The largest, densest and most developed markets have historically commanded significantly higher rental rates, yet pandemic-related trends have diminished these markets' lead.
- Since the beginning of the pandemic, the two most expensive markets, San Francisco and New York, have experienced the largest declines in rental rates at 14% and 11%, respectively.
- Miami has experienced the reverse with strong gains in rents, driven by demand in the urban core.

### RENTAL RATE CHANGE: PRE-PANDEMIC vs PRE-PANDEMIC to CURRENT



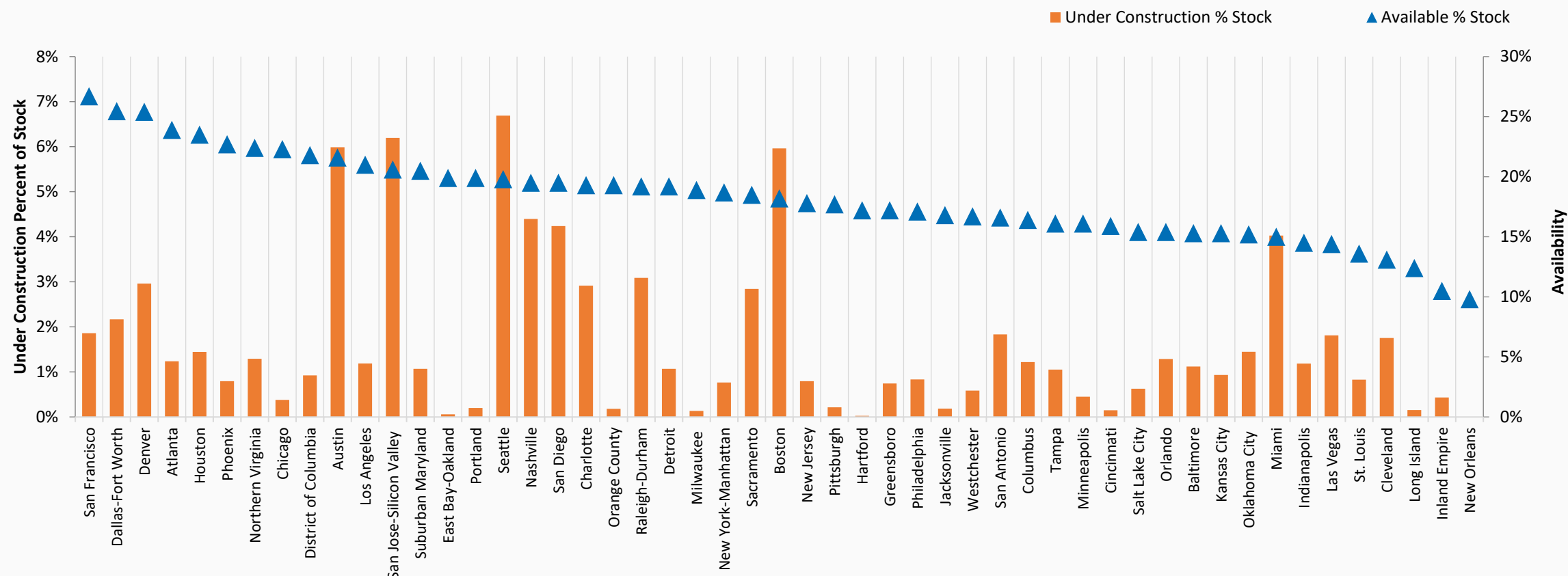
- Demand for space has yet to return to pre-pandemic levels in most market. Concessions remain high and leasing muted obscuring the true cost of rent.
- Some markets have fared relatively better than others:
  - The highest rental rate growth markets since the start of the pandemic are Miami, Boston, Greensboro, Las Vegas, Charlotte, and Raleigh-Durham.
  - Markets experiencing the most relative lift compared to pre-pandemic rental rate growth include Miami, Greensboro, Boston, Westchester, Columbus, Las Vegas, and Dallas-Fort Worth.

### AVAILABLE SQUARE FEET % STOCK



- In this graph, the softening of demand is illustrated by heightened availability rates shown in all tracked markets.
- Markets seeing the least rise in availability since the pandemic began include Inland Empire, New Orleans, Las Vegas, Westchester, Miami, and Oklahoma City.
- Only 23% of markets stayed constant or saw improvement from the previous quarter.

### CONSTRUCTION AND AVAILABILITY



- Under construction percent of stock is indicative of future market expansion. Combined with availability percent of stock, it can also be a potential determinate of softening or tightening within a market.
- Markets with particularly high under construction and high availability as a percent of stock include Austin, San Jose-Silicon Valley, Seattle, Nashville, San Diego, Charlotte, Raleigh-Durham, Sacramento, and Boston. Future vacancy will depend on how demand matches supply, and at what rate this demand absorbs released space.

Market	Inventory SF	Overall Vacancy Rate	Direct Vacancy Rate	Net Absorption	12-Month Net Absorption	Asking Rent Base	Annual Rent Change	Under Construction
Atlanta	234,402,138	18.5%	17.3%	(1,543,336)	(665,988)	\$28.86	2.7%	2,899,240
Austin	117,430,064	17.4%	14.3%	(683,314)	(784,739)	\$30.79	0.7%	7,030,958
Baltimore	120,388,856	14.2%	13.1%	(76,461)	11,074	\$23.32	-2.0%	1,348,529
Boston	303,464,903	12.1%	9.5%	(139,165)	(23,747)	\$28.50	13.9%	18,089,934
Charlotte	97,736,848	15.8%	12.8%	(210,794)	(151,375)	\$32.10	1.6%	2,849,679
Chicago	445,452,119	17.7%	16.6%	(1,916,023)	(3,244,314)	\$22.38	2.1%	1,685,472
Cincinnati	73,397,803	12.8%	11.6%	265,553	(247,845)	\$14.65	2.2%	110,000
Cleveland	81,225,914	9.8%	9.0%	285,447	(853,020)	\$17.97	1.2%	1,424,846
Columbus	80,884,888	14.0%	11.3%	(445,339)	(1,554,752)	\$16.12	3.1%	986,855
Dallas-Fort Worth	301,755,542	22.0%	19.9%	276,830	(864,310)	\$25.06	2.4%	6,540,166
Denver	136,017,375	18.9%	16.2%	4,520	(1,663,890)	\$24.59	-0.2%	4,028,612
Detroit	138,129,845	14.3%	12.7%	(231,401)	(2,238,206)	\$18.17	0.0%	1,475,909
District of Columbia	151,273,438	17.7%	16.6%	(476,900)	(2,406,232)	\$52.14	-0.4%	1,395,106
East Bay-Oakland	90,591,216	16.8%	14.5%	(1,486,341)	(1,385,188)	\$39.43	-0.2%	53,730
Greensboro	21,555,764	12.1%	11.7%	20,798	4,191	\$18.64	8.1%	160,000
Hartford	48,521,234	12.8%	11.8%	3,167	(1,060,972)	\$19.27	2.0%	12,587
Houston	309,503,502	20.5%	19.3%	133,066	(477,782)	\$20.94	0.6%	4,467,996
Indianapolis	73,686,950	11.9%	10.6%	(271,714)	(614,572)	\$21.17	4.1%	873,357
Inland Empire	50,732,224	7.6%	7.4%	(154,722)	172,735	\$24.00	2.2%	219,471
Jacksonville	43,067,579	11.2%	9.9%	58,446	398,063	\$21.34	2.2%	80,068
Kansas City	97,010,291	12.7%	11.3%	(309,806)	(1,928,938)	\$20.39	3.8%	904,681
Las Vegas	38,760,397	12.3%	11.0%	(135,927)	265,573	\$25.61	5.7%	701,712
Long Island	63,136,939	10.4%	9.3%	130,862	(1,268,838)	\$28.91	3.8%	97,127
Los Angeles	334,450,851	17.6%	15.6%	(729,578)	(4,217,831)	\$39.74	-0.6%	3,967,694
Miami	81,330,590	11.7%	11.1%	(113,543)	629,304	\$48.01	8.0%	3,275,271

Market	Inventory SF	Overall Vacancy Rate	Direct Vacancy Rate	Net Absorption	12-Month Net Absorption	Asking Rent Base	Annual Rent Change	Under Construction
Milwaukee	59,100,291	12.5%	12.2%	(97,999)	(37,828)	\$16.13	1.1%	79,681
Minneapolis	172,629,872	12.3%	10.6%	245,369	(1,398,916)	\$17.86	1.5%	774,616
Nashville	70,131,475	15.4%	12.7%	307,005	318,876	\$27.92	-1.7%	3,083,726
New Jersey	316,442,330	13.6%	11.9%	(842,957)	(1,523,463)	\$25.06	2.0%	2,512,482
New Orleans	35,847,102	8.9%	8.4%	33,428	(113,333)	\$20.16	6.2%	0
New York-Manhattan	557,712,954	14.9%	12.4%	1,568	(181,050)	\$53.73	-2.0%	4,273,680
Northern Virginia	202,551,942	18.2%	17.0%	1,744,636	391,821	\$33.96	5.7%	2,617,375
Oklahoma City	41,502,783	12.3%	11.8%	174,202	56,482	\$18.48	1.5%	600,279
Orange County	130,252,876	15.2%	13.3%	(223,578)	(1,910,175)	\$27.84	-2.8%	234,893
Orlando	66,690,356	10.6%	9.5%	(137,466)	(593,480)	\$23.43	4.2%	858,994
Philadelphia	239,075,181	12.1%	10.4%	(272,309)	(2,480,649)	\$25.18	1.6%	1,990,660
Phoenix	132,252,806	19.7%	15.3%	(1,233,305)	(2,550,304)	\$27.44	2.7%	1,051,740
Pittsburgh	105,060,833	14.0%	12.4%	(642,414)	(1,295,139)	\$24.86	2.8%	224,621
Portland	82,631,241	15.4%	13.5%	221,164	(3,624)	\$27.33	-0.3%	165,000
Raleigh-Durham	83,567,904	12.4%	9.3%	182,169	(733,756)	\$29.72	1.5%	2,580,555
Sacramento	76,806,752	14.2%	13.3%	(173,100)	(604,995)	\$24.64	2.3%	2,183,000
Salt Lake City	63,520,846	11.2%	9.0%	140,076	(84,927)	\$25.14	0.2%	398,144
San Antonio	60,028,986	13.1%	12.1%	(413,365)	(501,350)	\$21.09	-2.5%	1,099,992
San Diego	89,883,004	12.3%	11.2%	(338,397)	(678,736)	\$34.47	1.6%	3,809,652
San Francisco	167,489,346	20.5%	15.9%	(2,548,154)	(6,421,859)	\$54.23	-6.1%	3,116,418
San Jose-Silicon Valley	126,513,030	14.6%	11.5%	(1,754,807)	(358,629)	\$48.20	-1.8%	7,837,207
Seattle	176,321,684	14.5%	11.6%	(23,007)	(1,520,200)	\$31.99	7.3%	11,794,512
St. Louis	109,551,548	13.2%	11.7%	34,163	(1,022,516)	\$21.66	4.3%	906,500
Suburban Maryland	83,047,953	17.0%	15.8%	(451,129)	91,984	\$28.77	1.2%	887,824
Tampa	80,284,883	12.6%	10.0%	(24,324)	(143,902)	\$27.14	0.0%	843,941
Westchester	132,077,991	13.1%	11.6%	(384,383)	(516,589)	\$29.62	-1.0%	773,778



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## ABOUT TRANSWESTERN

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## RESEARCH METHODOLOGY

The information in this report is a compilation of single and multi-tenant office properties located in select U.S. metropolitan areas. Medical offices and government-owned buildings are excluded from analysis. All rents are reported as base, which are rents reflected irrespective of service type (Full Service, Plus Electric, etc.).