

SUBURBAN MARYLAND OFFICE MARKET

Q4 2023

TRENDLINES

	Q4 2023	Q4 2022	ONE-YEAR TREND	FIVE-YEAR AVERAGE	12-MONTH FORECAST
UNEMPLOYMENT RATE	2.1	4.2	↓	5.0	↓
NET ABSORPTION (Thousands SF)	(275.0)	(79.0)	↓	25.3	↔
DIRECT VACANCY RATE	17.0%	15.4%	↑	15.0%	↔
DIRECT VACANT SF (MSF)	16.3	14.7	↑	14.2	↔
UNDER CONSTRUCTION (MSF)	0.2	2.0	↓	2.2	↓
ASKING RENT, FULL SERVICE (PSF)	\$29.78	\$29.49	↑	\$29.25	↔
SALES VOLUME (Millions)	\$33.7	\$408.3	↓	\$192.4	↔

Source: Bureau of Labor Statistics, CoStar, Real Capital Analytics, Transwestern

OFFICE CONDITIONS DECLINED IN Q4 2023

The office market diminished during the fourth quarter of 2023, with negative 275,000 SF of net absorption. This was mostly driven by multiple mid-sized move outs and a lack of new leases during the past three months. The direct vacancy increased 70 basis points from last quarter, landing at 17.0%. Asking rents inched upward by 20 basis points, settling at \$29.78 PSF.

We expect office market conditions to remain soft in Suburban Maryland through 2024, as future move-outs and rightsizing, coupled with limited leasing activity, will drag the overall market. Top tier space will remain in demand, with most of the pressure on Class B product. Although demolitions and conversions of obsolete office product to alternative property types will help, it will not be the entire solution. The recent news of the FBI HQ relocation to Prince George's County could boost demand in the area. However, this is to be determined as the decision is under investigation.

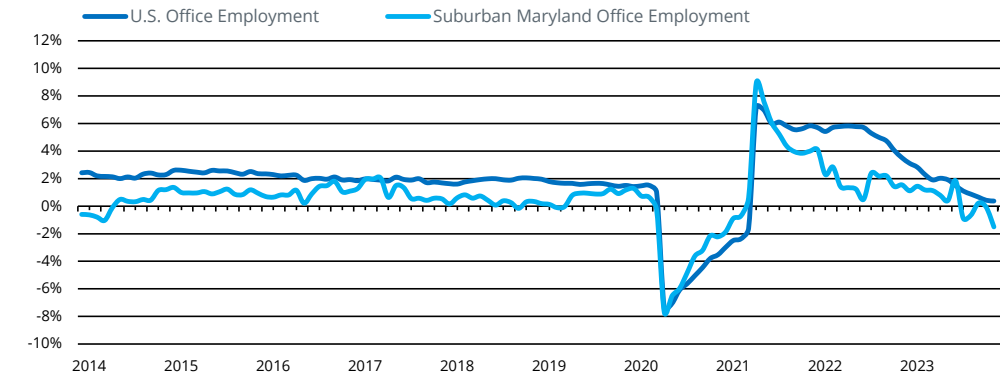


ECONOMY

Overall Job Growth Remains Healthy, but Office-Using Struggling

- 7,200 new jobs were added to the Suburban Maryland economy during the 12-months ending November 2023, which is below the pre-pandemic 5-year average of 9,900. This was driven by health care, educational services, and state/local government sectors.
- Office-using jobs lost 6,000 positions over the year. This was due to job cuts in the admin support sector primarily located in Montgomery/Frederick Counties. However, Prince George's/Calvert/Charles Counties added 2,600 new jobs over this period most of which was concentrated in the professional/business services sector which added 1,800 positions.
- The unemployment rate in Suburban Maryland is currently at 2.2% in October 2023 which is slightly above the average over the past three months. The rate has improved significantly from the peak of 10.4% in July 2020. Montgomery County continues to have the lowest unemployment rate at 1.9%.
- We expect office-using job growth in Suburban Maryland to be steady over the next five years, adding just over 2,500 new jobs per year on average. We expect most of the growth to occur within the federal government, state and local government, and tech sectors.

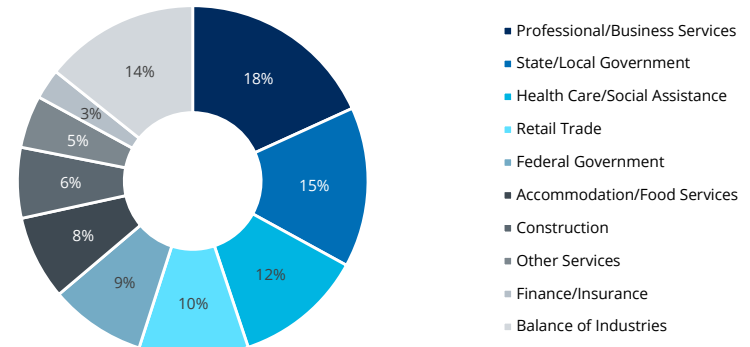
Y-O-Y CHANGE IN OFFICE JOBS



Source: Bureau of Labor Statistics, Transwestern

SHARE OF EMPLOYEES BY INDUSTRY

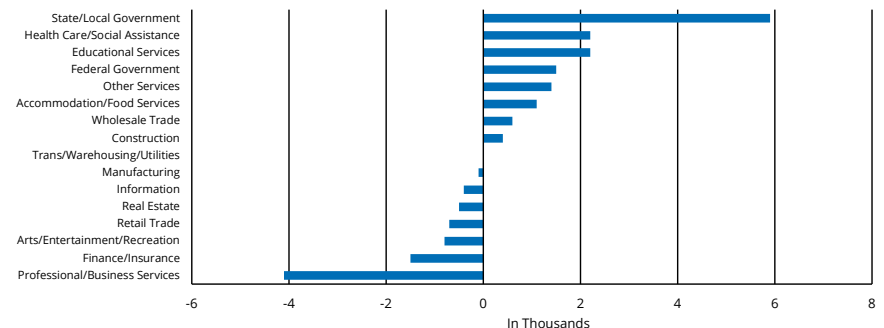
Suburban Maryland | November 2023



Source: Bureau of Labor Statistics, Transwestern

Y-O-Y CHANGE IN JOBS BY INDUSTRY

Suburban Maryland



Source: Bureau of Labor Statistics, Transwestern

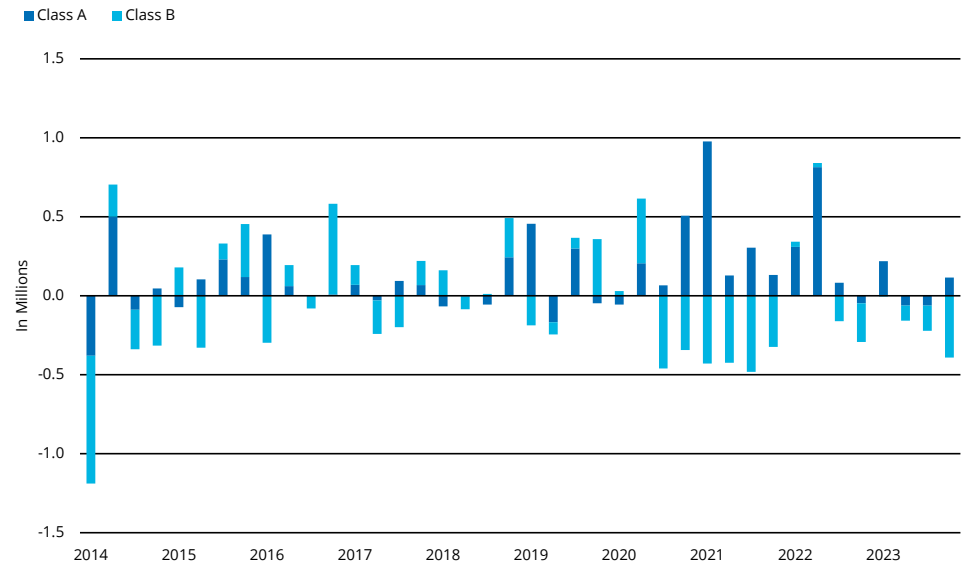


NET ABSORPTION

Class A Improves While Class B Struggles in Q4

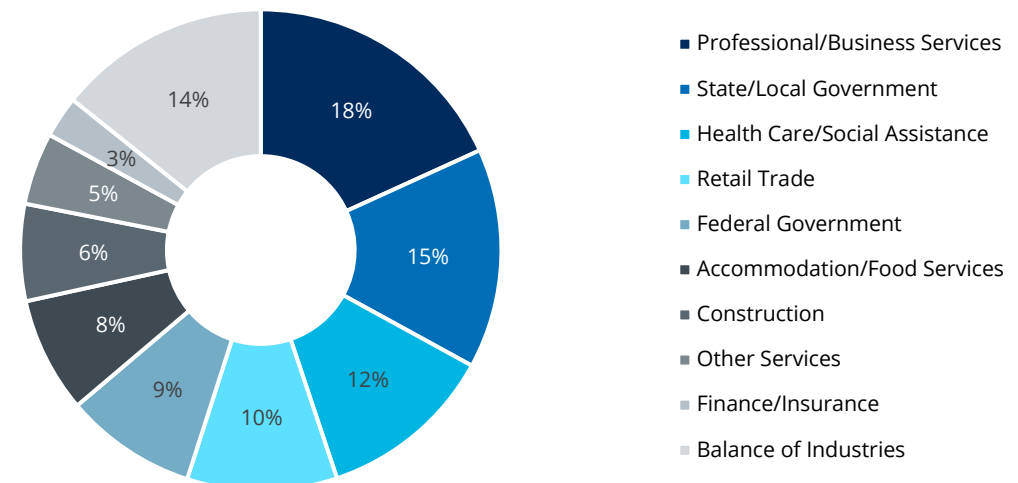
- Net absorption totaled negative 275,000 SF during the fourth quarter of 2023, after negative 213,000 SF during the third quarter of 2023. This compares to negative 292,000 SF of net absorption during the fourth quarter of last year.
- Class A net absorption totaled positive 116,000 SF, while Class B closed the quarter with negative 391,000 SF.
- The most notable deals of the quarter were Choice Hotel International and Sodexo leasing a total of 157,000 SF at the newly delivered 915 Meeting Street in North Bethesda. Other notable deals include Immunocore signing for 19,242 SF at 9801 Washingtonian Boulevard in North Rockville as well as University of Maryland Institute for Health Computing signing for 27,491 SF at 6116 Executive Boulevard in North Bethesda at the end of last quarter.
- Offsetting this gain were mid-sized move outs. Child Trends vacated the top two floors for a total of 31,585 SF at 7315 Wisconsin Avenue in Bethesda/Chevy Chase as they have embraced remote work. The U.S. FDA gave back a floor for a total of 28,438 SF at 5630 Fishers Lane in Rockville.
- We anticipate demand will continue to face challenges through 2024, as economic strains lead certain tenants to delay leasing decisions or renegotiate their current leases in response to new hybrid work policies.

NET ABSORPTION BY CLASS



Source: CoStar, Transwestern

SHARE OF LEASING ACTIVITY BY INDUSTRY YTD 2023



Source: CoStar, Transwestern

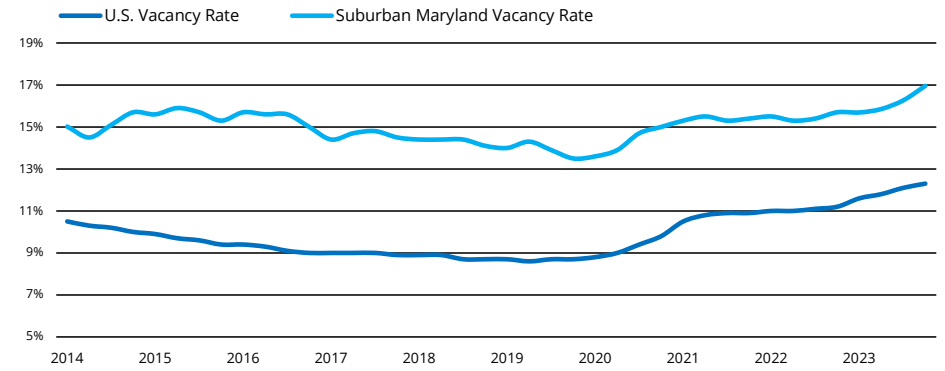


VACANCY

Vacancy Rate Continues to Rise in Q4

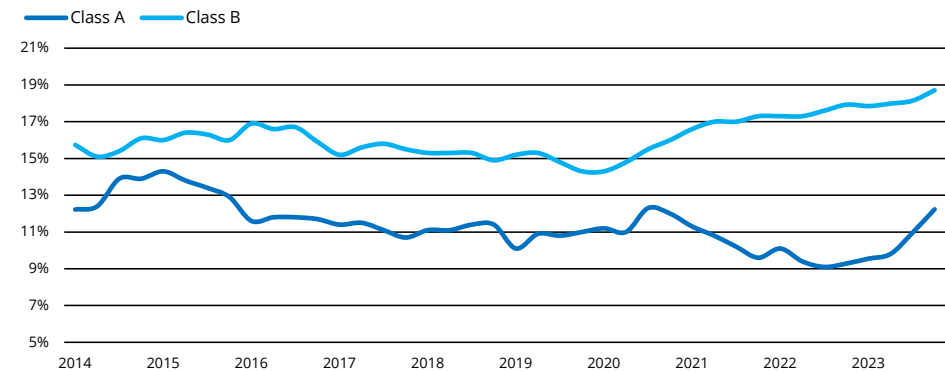
- The direct vacancy rate continued to rise from the third quarter of 2023 finishing the quarter at 17.0% and is up 130-basis points from one year ago.
- The Class A vacancy rate increased 120-basis points to 12.2% in the quarter, while the Class B/C vacancy rate increased 60 basis points to 18.7%. The Class A rate rose despite positive absorption because a medical office building at 950 Harry S Truman Drive delivered 125,000 SF of which only 6% was pre-leased.
- The vacancy rate is expected to face ongoing challenges through 2024. The rate for newer product will likely stabilize due to flight to quality, while older product will continue to struggle.

DIRECT VACANCY RATE



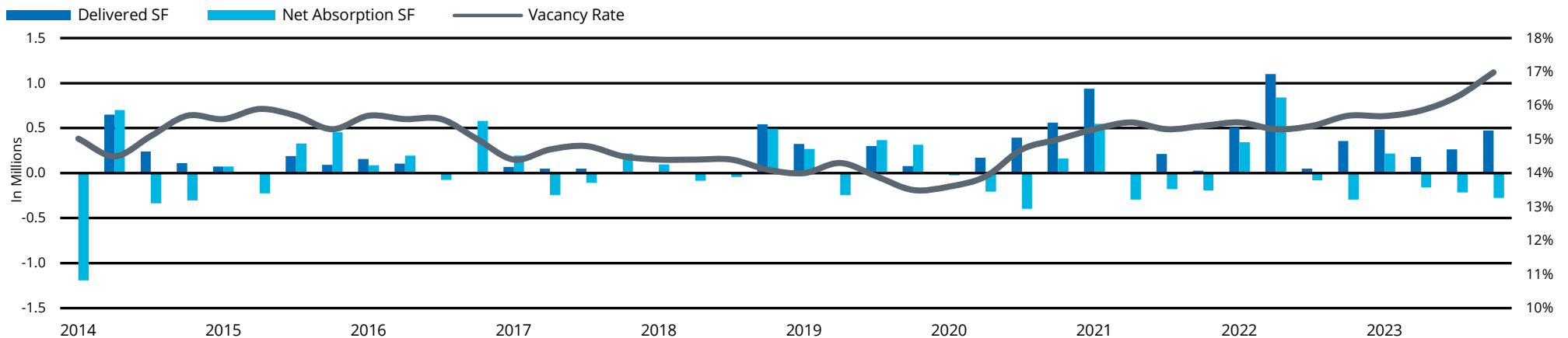
Source: CoStar, Transwestern

DIRECT VACANCY RATE BY CLASS



Source: CoStar, Transwestern

DELIVERY IMPACT ON KEY INDICATORS



Source: CoStar, Transwestern

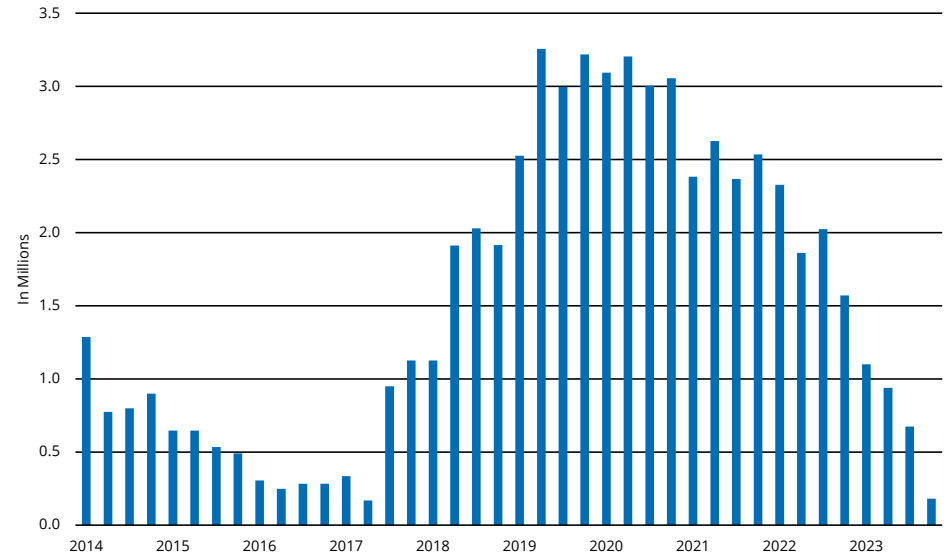


UNDER CONSTRUCTION

915 Meeting Street Delivers in Q4 2023

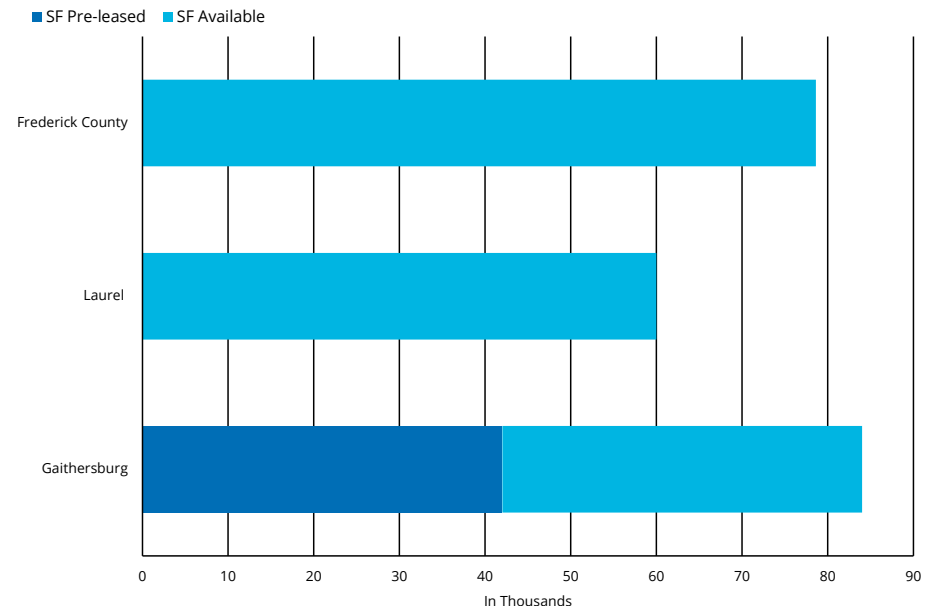
- Three projects delivered over the quarter for a total of 474,000 SF at 39% pre-leased. One project to highlight was Federal Realty Investment Trust delivering 276,000 SF at 915 Meeting Street with Choice Hotels International as the anchor tenant.
- There is 180,600 SF of office construction currently underway in Suburban Maryland, of which 23% is pre-leased. This is the below the 10-year average of 1.6 million SF which is the same amount as one year ago. Most of the pipeline is slated to deliver in 2024.
- Frederick County has the most under construction due to the construction at 112 Thomas Johnson Drive. The 53,138 SF medical office building is expected to deliver in the beginning of next year. In total, the Frederick County submarket will bring 78,600 SF of new space to market when projects deliver next year.
- With office valuation decreasing we expect limited new groundbreakings for the office asset type. The construction pipeline will decelerate as developers pause breaking ground due to the inability to acquire financing and depressed office values. Select owners will remain optimistic and find distressed properties at a lower value with well-funded tenants in place and hope to hold for the long term.

UNDER CONSTRUCTION



Source: CoStar, Transwestern

UNDER CONSTRUCTION BY SUBMARKET



Source: CoStar, Transwestern

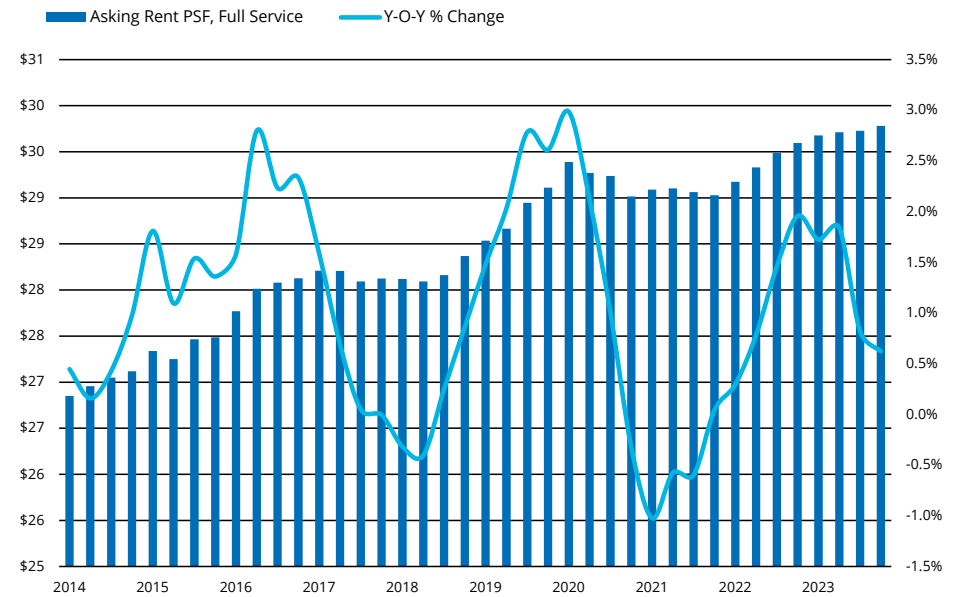


RENTAL RATES

Class A Asking Rents Inch Upward in Q4

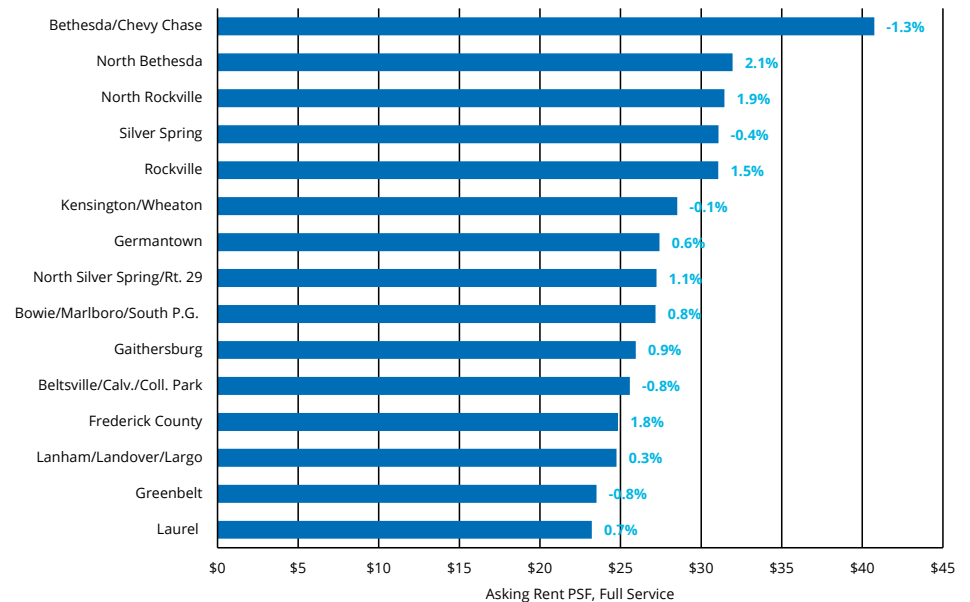
- Asking rents inched upwards 20 basis points during the fourth quarter of 2023, landing at \$29.78 PSF. The rate increased 60 basis points year-over-year which has been on an incline throughout 2022 and into 2023. Landlords have kept asking rents relatively steady, while offering competitive concessions which reduces the effective rate.
- Class A asking rents inched upward slightly by 10 basis point to \$34.90 PSF, while Class B/C averaged \$26.76 PSF, after a 30-basis point increase during the quarter.
- Concession packages will remain elevated through 2024, which will put downward pressure on effective rates. For a typical 10-year or greater term for a new lease signed during 2023, tenant improvement allowances averaged around \$115 PSF with 11.8 months of free rent. This compares to \$101 PSF and 12.9 months during 2022.
- We anticipate limited asking rent growth over next year. Newer space should achieve greater rent gains due to continued demand and quality product coming on-line. In addition, landlords will continue to provide competitive concession packages in order to attract tenants in a difficult market.

ASKING RENT



Source: CoStar, Transwestern

ASKING RENTS BY SUBMARKET AND Y-O-Y GROWTH



Source: CoStar, Transwestern

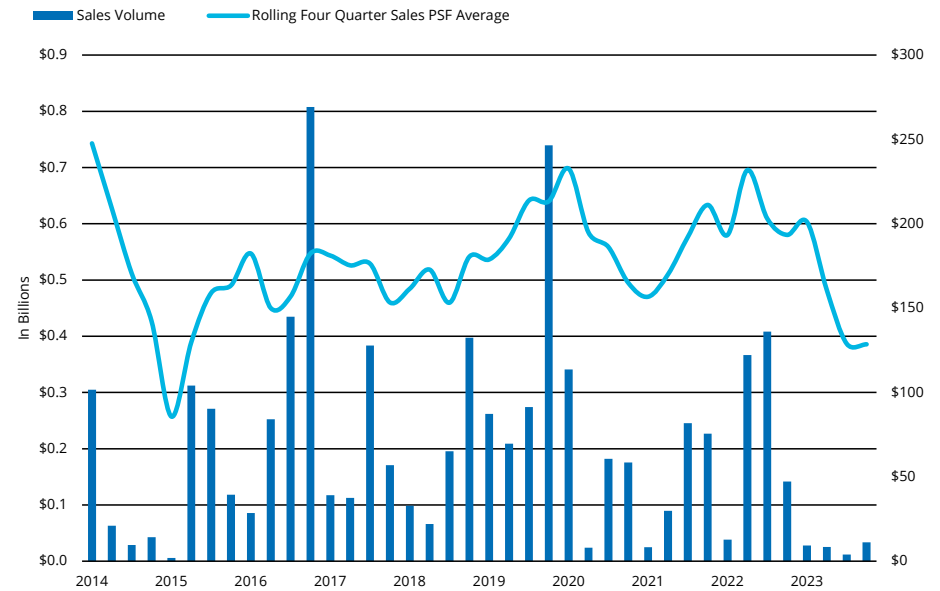


SALES

Sales Volume Remains Limited Through Q4

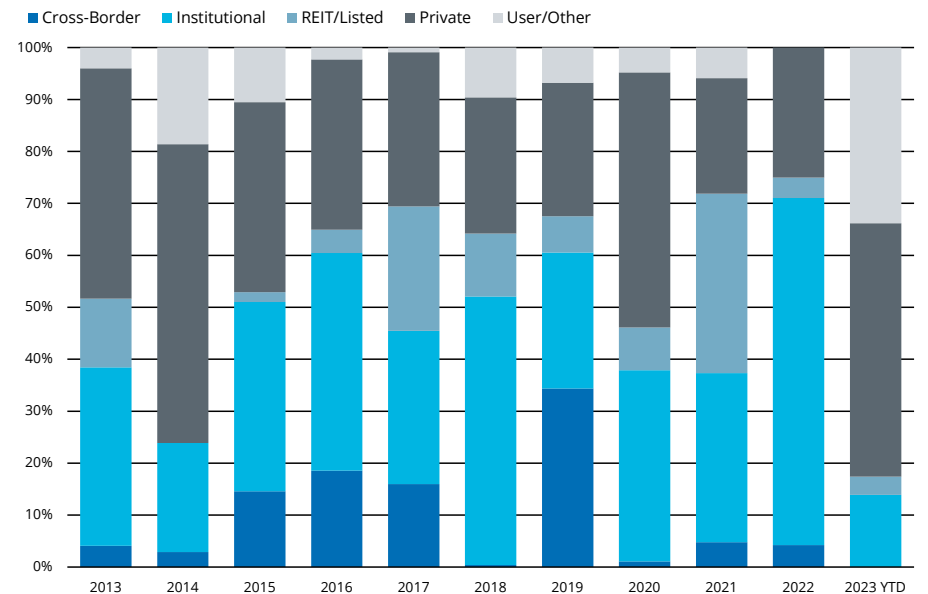
- During the fourth quarter of 2023, investment sales volume totaled \$33.7 million at \$184 PSF on three transactions. This compares to six transactions completed during the third quarter of 2023, totaling \$11.7 million at \$53 PSF. \$33.7 million is the highest quarterly sales volume in 2023 for Suburban Maryland.
- One notable sale of the quarter was 9850 Key West Avenue in North Rockville. Hines purchased the asset for \$25.7 million or \$357 PSF from Harrison Street Capital. The property was 100% leased at the time of sale. This was part of a two-property medical portfolio transaction. The motivation for the acquisition was to gain exposure to an alternative investment such as medical outpatient buildings.
- The news of the FBI’s decision to place their headquarters in Greenbelt could potentially help office values near the project. While the decision remains under investigation, there is opportunity to attract other government tenants to Prince George’s County which could spur economic development thus helping office values in the area.
- Elevated interest rates continue to stifle investment volume across all property sectors as debt remains difficult to acquire. The office market largely remains in a period of price discovery. With office debt maturities still set to occur into 2024, opportunistic capital will be looking for distressed assets that they can purchase at a discounted rate.

SALES VOLUME



Source: CoStar, Real Capital Analytics, Transwestern

BUYER CAPITAL COMPOSITION



Source: CoStar, Real Capital Analytics, Transwestern



NOTABLE LEASES

TENANT	ADDRESS	SUBMARKET	TYPE	SF LEASED
AGNOVOS HEALTHCARE	7301 Calhoun Pl	North Rockville	Renewal	30,751
LEIDOS	2099 Gaither Rd	North Rockville	Renewal	25,000
AMERICAN INSTITUTE OF PHYSICS	1 Physics Ellipse	Beltsville/Calv./Coll. Park	Sale Lease Back	22,521
IMMUNOCORE	9801 Washingtonian Blvd	North Rockville	New Lease	19,242
COAKLEY & WILLIAMS CONSTRUCTION	4500 East West Hwy	Bethesda/Chevy Chase	New Lease	18,793
RBC WEALTH MANAGEMENT	5425 Wisconsin Ave	Bethesda/Chevy Chase	Renewal	18,408

= Transwestern deal

Source: CoStar, CompStak, Transwestern.

NOTABLE SALES

ADDRESS	SUBMARKET	SALE DATE	SALES PRICE	BUILDING SF	PRICE PSF	BUYER	SELLER
10230-10244 RIVER RD	North Bethesda	Nov-23	\$2,013,450	18,266	\$110	Carrollton Enterprises	Sarofim Realty Advisors
9850 KEY WEST AVE	North Rockville	Oct-23	\$25,723,770	72,000	\$357	Hines	Harrison Street Capital
21 CHURCH ST	Rockville	Oct-23	\$6,000,000	93,450	\$64	Dilan Investments	Hartford Investment Management Co
11820 PARKLAWN DR	North Bethesda	Sep-23	\$1,800,000	62,160	\$29	Polinger Co.	Link Logistics Real Estate
11900 PARKLAWN DR	North Bethesda	Sep-23	\$1,380,000	46,188	\$30	Polinger Co.	Link Logistics Real Estate

= Transwestern deal

Source: CoStar, CompStak, Transwestern.

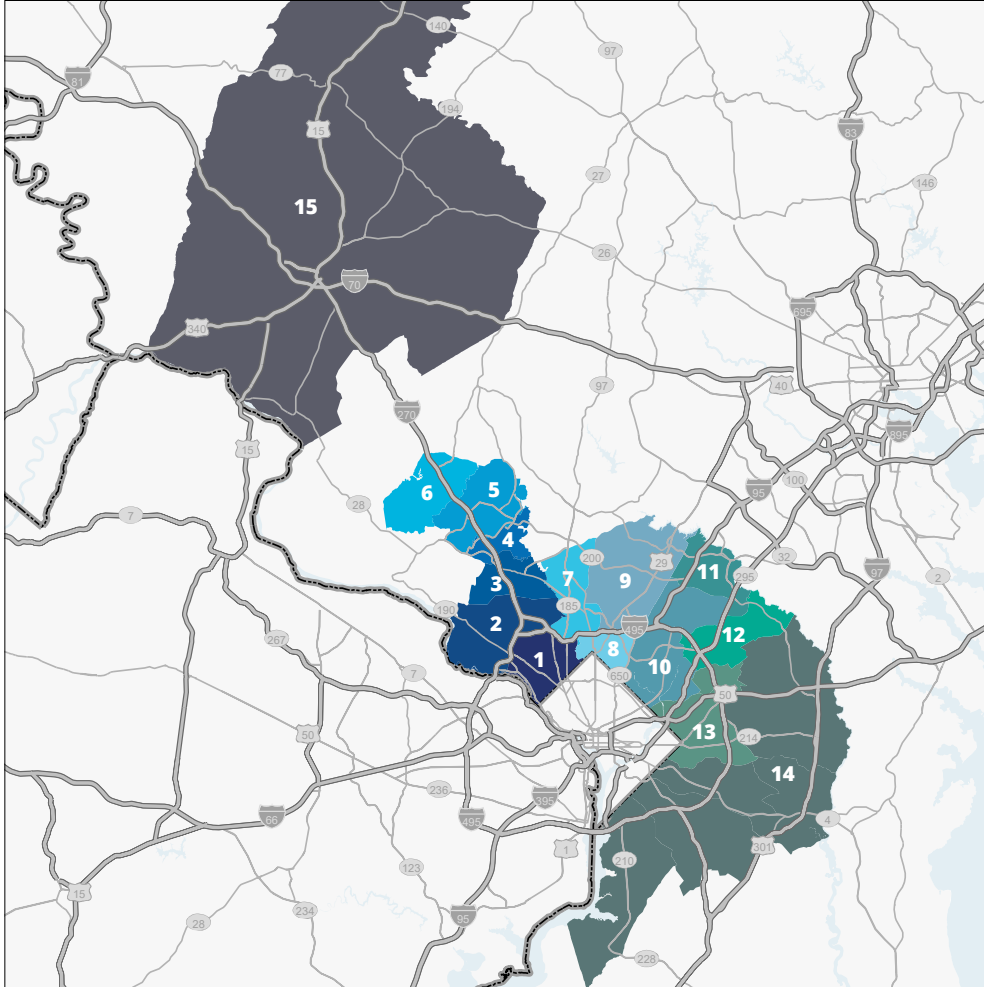


MARKET INDICATORS

All Classes of Space | Q4 2023

SUBMARKET	INVENTORY SF	DIRECT VACANT SF	DIRECT VACANCY RATE	OVERALL VACANCY RATE	UNDER CONSTRUCTION SF	NET ABSORPTION SF	Y-O-Y NET ABSORPTION SF	ASKING RENT PSF, FULL SERVICE
BETHESDA/CHEVY CHASE	13,170,201	2,410,147	18.3%	19.5%	0	(66,000)	(303,000)	\$40.74
NORTH BETHESDA	11,173,353	2,022,377	18.1%	19.2%	0	155,000	161,000	\$31.95
ROCKVILLE	8,436,869	1,645,189	19.5%	19.9%	0	(51,000)	(186,000)	\$31.07
NORTH ROCKVILLE	12,720,546	1,685,472	13.3%	14.4%	0	(76,000)	(92,000)	\$31.44
GAITHERSBURG	6,074,217	698,535	11.5%	15.9%	42,000	(103,000)	(121,000)	\$25.94
GERMANTOWN	2,803,251	709,223	25.3%	27.9%	0	19,000	(60,000)	\$27.41
KENSINGTON/WHEATON	1,641,234	223,826	13.6%	15.3%	0	0	(32,000)	\$28.52
SILVER SPRING	6,973,396	1,042,523	15.0%	15.4%	0	(30,000)	(129,000)	\$31.07
N. SILVER SPRING/RT. 29	3,661,988	371,692	10.2%	11.5%	0	13,000	27,000	\$27.23
MONTGOMERY COUNTY	66,655,055	10,808,983	16.2%	17.6%	42,000	(139,000)	(735,000)	\$32.30
BELTSVILLE/CALV./COLL. PARK	6,082,488	1,021,858	16.8%	17.9%	0	(49,000)	(41,000)	\$25.57
LAUREL	2,579,823	544,343	21.1%	21.2%	60,000	8,000	(39,000)	\$23.21
GREENBELT	3,016,041	871,636	28.9%	29.3%	0	(36,000)	57,000	\$23.52
LANHAM/LANDOVER/LARGO	5,659,867	1,682,112	29.7%	32.9%	0	1,000	360,000	\$24.75
BOWIE/MARLBORO/SOUTH P.G.	5,485,712	447,086	8.2%	8.4%	0	(8,000)	(27,000)	\$27.17
PRINCE GEORGE'S COUNTY	22,823,931	4,567,034	20.0%	21.2%	60,000	(84,000)	310,000	\$25.21
FREDERICK COUNTY	6,880,350	963,249	14.0%	15.2%	78,600	(52,000)	(7,000)	\$24.85
TOTAL	96,359,336	16,339,267	17.0%	18.3%	180,600	(275,000)	(432,000)	\$29.78

Source: CoStar, Transwestern.



Suburban Maryland Office Submarkets

- 1 Bethesda/Chevy Chase
- 2 North Bethesda
- 3 Rockville
- 4 North Rockville
- 5 Gaithersburg
- 6 Germantown
- 7 Kensington/Wheaton
- 8 Silver Spring
- 9 N. Silver Spring/Rt. 29
- 10 Beltsville/Calverton/College Park
- 11 Laurel
- 12 Greenbelt
- 13 Lanham/Landover/Largo
- 14 Bowie/Marlboro/South P.G.
- 15 Frederick County

RESEARCH METHODOLOGY

The information in this report is the result of a compilation of information on office properties located in Suburban Maryland. This report includes single tenant, multi-tenant and owner-user properties 15,000 SF and larger, excluding those properties owned by a government agency.

FOR MORE INFORMATION

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