



Phoenix

Q3 2017 / Quarterly Healthcare Market Report

Market Facts


 **13.1%**
Class A Vacancy

 **14.4%**
Class B Vacancy

 **\$28.76**
Class A Average Asking Rate

 **\$22.82**
Class B Average Asking Rate

 **\$170**
Average Sales
Price/Square Foot

 **8.0%**
Medical Office
Average CAP Rate

Market Overview

The Phoenix medical office market grew to 24.7 million square feet (msf) and the third quarter overall vacancy rate dropped to 14.3%, 40 basis points lower than first quarter 2017. Average rental rates declined slightly to \$22.11 per square foot (psf) in the third quarter, down from \$22.31 psf in the first quarter. Year-to-date absorption continues to be positive, with 55,000 square feet (sf) absorbed, of which, 97,657 sf was in the third quarter. Quarterly absorption was positive in 2015 and 2016, but negative 113,699 sf in first quarter 2017. These strong market fundamentals are unsurprising, Phoenix's growing population and the increasing demands of an aging population for medical services continues to bode well for the local medical office market. According to the Arizona Office of Economic Opportunity's medium series, between 2015 and 2020 the total population of Maricopa County is projected to grow 1.9% annually, and the number of individuals over 65 will increase 4.4%.

Top Leases

Tenant	Building	Address	Submarket	Square Feet	Type
Banner Health	Ironwood Medical Plaza	37100 N Gantzel Rd	Gateway Airport/Loop 202	7,023	New
Integrated Medical Services	Physicians Medical Plaza of Scottsdale	3815 E Bell Rd	Paradise Valley	5,690	New
Bayless Integrated Healthcare	Dobson Medical	2204 S Dobson Rd	Superstition Corridor	5,520	New
IASIS Healthcare	St. Luke's Medical Center	555 N 18th St	Midtown	5,421	New
NovaSpine Pain Institute	Mercy Gilbert Medical Center	3645 S Rome St	Gateway Airport/Loop 202	4,808	New

Top Sales

Buyer	Building	Address	Submarket	Square Feet	Sale Price	Price/SF
Avison Young Sold Woodside Health	Foothills Health Center	4510 & 4530 E Ray Rd	South Tempe/Ahwatukee	53,310	\$12,087,675	\$227
Woodside Health	Shea Medical Plaza	7425 E Shea Blvd	Central Scottsdale	42,439	\$11,653,110	\$275
MCR Companies	Arizona Heart Foundation	1910 E Thomas Rd	Central Phoenix	30,017	\$5,000,000	\$167
Avison Young Sold Meridian Property Company	Grunow Memorial Medical Center	926 E McDowell Rd	Central Phoenix	51,150	\$4,900,000	\$96
Gregg Graines	Banner Sun City	10541 W Thunderbird Blvd	Arrowhead	13,900	\$3,700,000	\$266

According to the Arizona Commerce Authority, healthcare is the leading industry in the state. Healthcare employers in Arizona are adding more jobs than those nationwide (3.2%) and more than other industries in the state (2.5%). In 2015 that translated into 320,028 jobs statewide, worth a total \$21.4 billion in annual earnings. In the Phoenix Metropolitan Statistical Area (MSA), in September 2017 there were 255,700 healthcare employees, and the sector grew 3.8% annually since 2012. Several factors contribute to the region's continued popularity with retirees, prime consumers of healthcare services. Year-round dry and hot weather ensure continual outdoor recreation, and appeal to those relocating from cold and wet winters in the Midwest and Northeast. Housing costs remain low compared to other major MSAs. Social Security income and public service pensions are tax exempt, and there is no inheritance or estate tax. As unemployment continues to fall in the Phoenix MSA and the economy improves, young families with children are also relocating, further pushing demand for healthcare services.

Due to favorable demographic trends and public funding for services, healthcare real estate and development is increasingly viewed as a safe investment by fiduciaries and private equity groups. Stable rental and vacancy trends also provide investor assurance. Through the third quarter, 41% of 2017 purchase volume was by

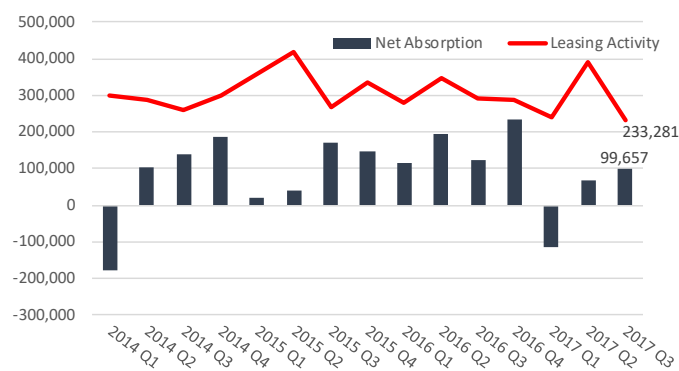
REITs or other public groups, and 44% was by private non-user investors. Healthcare Trust of America was the most active purchaser by dollar volume. Median cap rates dipped from 7.3% in first quarter 2017 to 7.0% in second quarter, before rebounding strongly to 8.0% in third quarter.

Loop 303/Surprise was the most active submarket in the third quarter of 2017, recording nearly 31,000 sf of positive absorption, 32% of the market's positive absorption. The Airport Area had the highest average asking rent at \$28.86 psf, while Downtown Mesa and Southwest Phoenix reported the lowest vacancy rates, both were nearly 100% occupied. Of the 12 submarkets with over 1.0 msf, the Gateway/Airport/Loop 302 submarket is the healthiest, with Class B vacancy at 10.4%, Class A vacancy at 10.3%, and the highest average rental rate of \$26.07 psf. The largest lease of the third quarter occurred in Pinal County, with Sun Life Family Health Center acquiring 12,182 sf at 174 W. Highway 287.

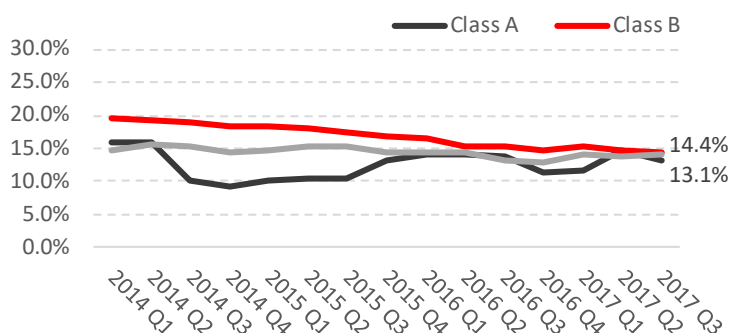
100,400 sf of new medical office product was delivered in the Phoenix market through third quarter 2017, with 70.8% leased, and nearly 195,000 sf is currently under construction in the region, with 38.1% being preleased. There are three projects under construction with over 15,000 sf: the four-story expansion of Banner Estrella Hospital

Market Snapshot

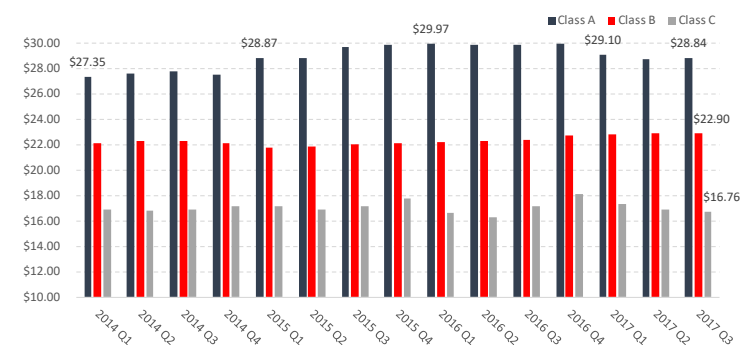
Historical Net Absorption & Leasing Activity



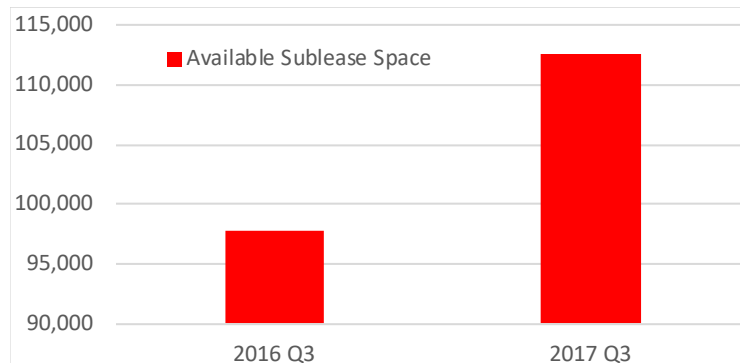
Historical Vacancy



Historical Asking Rental Rate (FSG)



Total Available Sublease Space in the Market



Campus is located at 9305 W Thomas Road and will add 125,000 sf of medical office space to the market in mid-2018; Laveen Medical Plaza is under construction at 51st Avenue and Baseline Road, scheduled for completion in May 2018, with none of its 44,000 sf preleased; and Noah Palomino Clinic's new 16,000 sf office at 16251 N Cave Creek Road will be completed in December 2017.

Sales activity slowed in the third quarter. It appears that most value-add office deals have already been sold, the remaining sellers are aggressive with pricing, feeding into the market slowdown. The largest sale was 4510 and 4530 E. Ray Road, a 45,000-sf medical office building which sold for \$12.0 million, or approximately \$227 psf, in an Avison Young brokered transaction. Total square footage volume was down 21.6% from second quarter and dollar volume dipped 50.3%, while the median price psf declined 8.6%.

Other large sales in the third quarter included: 7425 E. Shea Boulevard, which was purchased for \$11.7 million (\$275/psf); 1910 E. Thomas Road, a 30,017 sf office building that sold for \$5.0 million (\$167/psf); and the 51,150 sf 926 E. McDowell Road property, which was bought for \$4.9 million (\$96/psf).

Market By The Numbers

Submarket	Total RBA (SF)	Vacant Space		Vacancy Rate			Available Space		Net Absorption (SF)	Avg. Ask Total (FS)	Avg. Ask Class A (FS)
		Direct	Sublease	Class A	Class B	Class C	Direct	Sublease			
44th St	157,541	29,774	3,870	-	27.7%	6.4%	26,789	3,870	-2,003	\$25.58	-
Airport Area	207,679	1,875	0	-	1.2%	0.0%	0	0	0	\$28.86	-
Arrowhead	2,232,643	327,729	15,008	30.4%	11.9%	34.5%	305,013	15,008	-1,293	\$24.57	\$27.99
Camelback Corridor	449,943	63,768	0	9.9%	20.5%	9.5%	63,768	0	-1,072	\$23.75	\$27.95
Central Phoenix	1,271,777	223,051	0	-	21.0%	9.4%	220,864	0	4,268	\$20.75	-
Central Scottsdale	1,449,140	203,824	0	8.5%	15.6%	0.0%	192,608	0	12,128	\$24.08	\$27.50
Chandler	1,562,759	169,304	20,795	-	12.9%	1.1%	155,829	20,795	-3,506	\$23.37	-
Deer Valley/Airport	1,310,100	223,104	9,012	13.7%	19.3%	10.3%	220,919	9,012	15,247	\$24.67	\$28.28
Downtown	654,757	38,111	0	0.0%	7.0%	10.0%	38,111	0	0	\$24.33	-
Downtown Mesa	129,543	24,049	1,100	-	0.0%	24.4%	24,049	1,100	-700	\$12.56	-
East Mesa	1,124,462	162,057	0	-	13.2%	16.4%	159,909	0	3,993	\$17.87	-
Gateway/Airport/Loop 302	1,284,622	127,750	4,819	10.3%	10.4%	0.0%	113,547	4,819	23,707	\$26.07	\$29.66
Glendale	730,354	86,117	17,106	14.6%	15.7%	8.7%	86,117	17,106	4,304	\$27.45	\$30.93
Loop 303/ Surprise	1,183,428	201,915	0	-	17.8%	5.0%	201,915	0	30,870	\$22.52	-
Midtown	1,186,325	60,104	0	-	4.8%	5.8%	60,104	0	-1,428	\$20.61	-
North Interstate-17	177,486	34,401	2,018	-	20.5%	-	34,401	2,018	-6,031	\$24.11	-
North Phoenix	61,149	8,835	0	-	14.4%	-	8,835	0	4,026	\$21.05	-
North Scottsdale	325,228	26,775	0	-	7.9%	10.3%	26,775	0	6,472	\$21.59	-
NW Phoenix	1,532,369	463,005	0	-	31.8%	27.9%	456,044	0	-13,999	\$16.61	-
Paradise Valley	1,201,154	181,862	12,286	22.9%	16.0%	5.9%	173,818	12,286	-3,617	\$22.55	\$26.92
Piestewa Peak Corridor	294,234	26,764	20,189	16.6%	18.8%	9.9%	26,764	20,189	5,263	\$27.16	\$25.50
Pinal County	652,018	67,216	0	-	12.7%	0.0%	67,216	0	10,688	\$21.09	-
Scottsdale Airport	730,351	30,339	2,018	5.8%	4.4%	-	30,339	0	9,098	\$27.44	\$30.00
South Scottsdale	856,936	128,471	4,631	-	20.9%	10.2%	126,948	4,631	4,140	\$23.37	-
South Tempe	513,788	85,136	0	-	17.5%	0.0%	85,136	0	-7,575	\$23.67	-
Southwest Phoenix	171,662	5,864	0	-	0.0%	6.8%	5,864	0	6,112	\$14.46	-
Superstition Corridor	1,557,841	142,265	0	0.0%	9.0%	14.4%	142,265	0	-14,422	\$20.59	-
Tempe	948,146	220,009	0	15.3%	29.4%	17.0%	218,951	0	1,336	\$22.53	\$34.06
West I-10	709,836	52,423	1,657	-	7.4%	39.4%	52,423	1,657	11,651	\$23.93	-
Total	24,667,271	3,415,897	114,509	13.1%	14.4%	14.2%	3,325,321	112,491	97,657	\$22.11	\$28.84



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