

Phoenix

Healthcare Market Report 3rd Quarter 2018

Quick Stats

37.4 K

Net employment gain from August 2017 to August 2018.

10.3 K

Square feet of negative medical office space absorption.

13.1%

Vacancy increased 1-basis points from second quarter.

847.9 K

Square feet of medical space under construction.

\$22.96 PSF

Gross asking rents increased by 1.2% from second quarter 2018.

Medical Office Space Demand Continues to Grow.

Phoenix has long been known as a medical services hub, due to the large senior population. However, employment opportunities in the Phoenix area have increased in the past decade attracting a younger demographic to the Valley. The number of jobs has increased 1.3% annually in the past ten years, ahead of the population at 1.2%. Demand for medical office space continues to grow due to the influx of new jobs, the affordability of the area, and the favorable weather for retirement.

Rental Rates

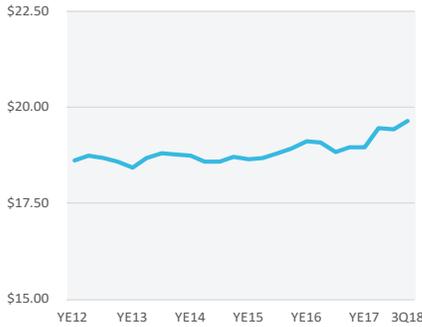
The Phoenix market's average asking rate ended the quarter at \$22.96 per square foot (psf), up 3.5% year-over-year. Rental rates peaked in 2007 at \$26.30, declined to a low of \$20.80 in 2013, and have been slowly recovering. The Southwest Phoenix, Midtown and West I-10 Submarkets have experienced the largest increases since second quarter 2018. Over the past two years asking rates have increased 55.1% in Southwest Phoenix, the fastest growing rate due to available space hitting the market

after a long-term lease. The rate of growth will continue its steady upward trend into mid-2019.

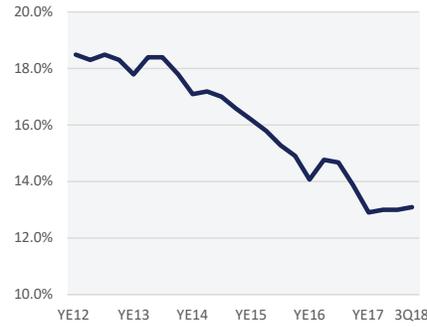
Vacancy

Vacancy increased slightly in the third quarter, but is only 20 bps higher than the nine year low recorded in fourth quarter 2017. Overall, vacancy has remained flat in 2018 despite deliveries. The greatest third quarter improvements were in South Scottsdale with 330 bps, South Tempe with 300 bps and Downtown with 190 bps. 13 of the 29 submarkets, located mostly in suburban areas, saw worsening conditions for vacancy. The largest vacancy increases were the Southwest Phoenix Submarket increasing 570 bps, 44th Street Submarket increasing 400 bps, and Piestewa Peak Corridor Submarket increasing 400 bps. The amount of available sublease space increased 27.5% in the third quarter. Sublease absorption in the Glendale and West I-10 led all submarkets, while a large percentage of negative sublease activity was recorded in Northwest Phoenix and Piestewa Peak Corridor.

Rental Rates



Vacancy Rates



Absorption & Deliveries



Top Leases

Tenant	Building	Submarket	SF	Type
Atlantis Health Systems	Arrowhead Professional Center	Arrowhead	20,000	Direct
United Surgical Partners International	McDowell Medical Center	Central Phoenix	13,418	Direct
Fast Med	Via Linda Corporate Center	Central Scottsdale	12,523	Direct
Abrazo Scottsdale	North Scottsdale Corp Ctr Phase II	Scottsdale Airpark	7,844	Direct
Focused Family Services	McDowell Professional Plaza	Central Phoenix	7,378	Direct

Top Sales

Buyer	Building	Submarket	SF	Sale Price
Medical Properties of America	14520 W Granite Valley Dr.	Loop 303/ Surprise	40,004	\$12,749,400
Medical Properties of America	Lakes Medical Plaza II	Arrowhead	15,208	\$5,250,600
Ryan Spiekerman	Missouri Professional Plaza	Camelback Corridor	25,200	\$3,000,000
John W Colyer	32nd Street Medical Building	Paradise Valley	10,344	\$2,800,000
Denzel Pereira	The Medical Plaza at Spectrum	Gateway Airport/ Loop 202	7,512	\$2,000,000

Under Construction

Property	Submarket	Completion	SF	% Preleased/Owned
Estrella Medical Plaza II	Glendale	1Q19	125,000	78.5%
Credit Union West Corporate Center	Glendale	1Q19	80,000	78.9%
Ortho Arizona	Gateway Airport/ Loop 202	4Q19	49,600	-
Black Mountain Center	Arrowhead	2Q19	25,401	0.0%
Arrowhead Orchards	Arrowhead Orchards	1Q19	22,700	0.0%

Trends to Watch

Education and Health Services employment has increased while the unemployment rate remains the same.



4.5%
The unemployment rate has remained flat from January 2018.



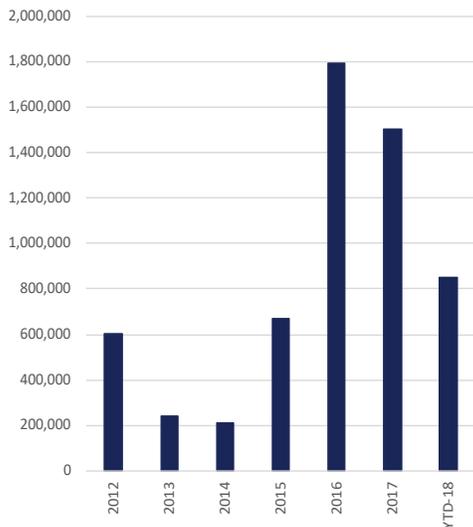
13.9% to 13.1%
The vacancy rate has continued to drop year-over-year since third quarter 2017.



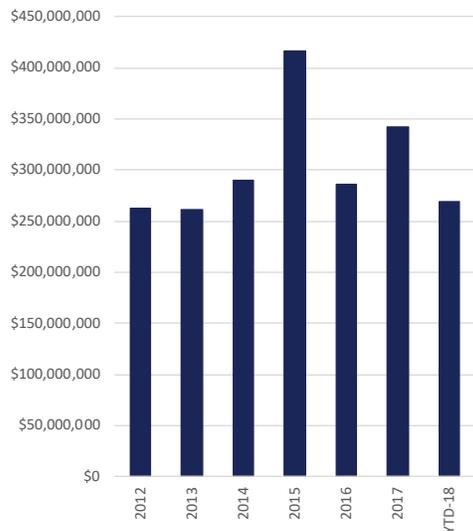
3.5%
Education and Health Services employment have increased year-over-year since third quarter 2017.

Demand for medical office space continues to grow due in part to the favorable weather for retirement.

Under Construction



Investment Sales



Leasing

Absorption in the third quarter was recorded at -10,328 sf, bringing the year-to-date total to -11,319 sf. The submarkets with the largest positive absorption figures were South Scottsdale at 28,270 sf and Gateway/Airport/Loop 302 at 19,789 sf.



Arrowhead Professional Center

The largest lease of the quarter was in the Arrowhead Professional Center where Atlantis Health Systems acquired 20,000 sf, half of the square footage in Building A.

Leasing activity has shown a growing demand for family services.

An indication of this growing demand is Desert West Obstetrics & Gynecology's lease of 16,000 sf under construction at N. 67th Avenue and W. Thunderbird Road.

Construction

At the end of third quarter, the medical office market had nearly 848,000 sf under construction. The Glendale Submarket accounts for 24.8% of the square footage under construction, including Estrella Medical Plaza II, the largest building under development in the third quarter. It is projected to deliver 125,000 sf in early 2019 and is already 78.5% preleased.



Estrella Medical Plaza II

Strong preleasing is evident in the Glendale Submarket. Credit Union West Corporate Center, the second largest project in development, is an 80,000 sf Class A medical and professional office building located in Glendale. The project is due to be delivered in late fourth quarter of 2018. 78% of the building will be occupied by the Owner and the remainder is in the preleasing stage.

Investment Sales

Office sales totaled \$59.4 million in the third quarter, bringing year-to-date volume to \$269.5 million.



14520 W. Granite Valley Drive

In the largest sale of the quarter, the 100% leased 14520 W. Granite Valley Drive 40,000 sf medical office development, located in the Loop 303/ Surprise Submarket, was purchased by Medical Properties of America for \$12.7 million (\$319 psf). Medical Properties of America also had the second largest transaction, purchasing Lakes Medical Plaza II at 10494 W. Thunderbird Road for \$5.3 million (\$345 psf), which is situated on a ground lease. Both of these properties were bought from The Core Institute, no brokers were involved.

Market By The Numbers

Submarket	Total RBA (SF)	Vacant Space Direct	Vacant Space Sublease	Class A Vacancy Rate	Class B Vacancy Rate	Class C Vacancy Rate	Available Space Direct	Available Space Sublease	Net Absorption (SF)	Avg. Ask Total (FS)
44th St	180,960	69,745	0	-	48.3%	7.0%	69,745	0	-12,041	\$23.04
Airport Area	193,279	0	0	-	0.0%	0.0%	0	0	0	\$28.86
Arrowhead	2,384,883	311,561	4,706	34.9%	10.3%	21.7%	262,902	4,706	9,562	\$25.85
Camelback Corridor	492,774	40,072	21,534	7.2%	15.5%	13.6%	33,369	17,015	5,197	\$25.30
Central Phoenix	1,338,321	237,233	0	-	20.6%	10.5%	216,009	0	-6,344	\$22.35
Central Scottsdale	1,400,940	180,678	4,202	13.2%	13.6%	4.5%	180,678	4,202	-448	\$24.55
Chandler	1,677,261	152,475	13,486	9.1%	0.8%	9.9%	147,643	13,486	8,833	\$23.32
Deer Valley/Airport	1,375,267	178,400	4,574	9.2%	15.1%	4.6%	171,051	4,574	-16,974	\$26.02
Downtown	654,757	25,851	0	0.0%	3.3%	10.0%	25,851	0	-5,552	\$24.42
Downtown Mesa	127,788	2,000	0	-	0.0%	2.0%	2,000	0	0	\$14.21
East Mesa	1,184,847	108,447	0	-	10.1%	7.5%	108,447	0	9,320	\$18.47
Gateway/Airport/Loop 302	1,337,248	111,195	4,077	0.0%	9.0%	0.0%	107,348	4,077	19,789	\$27.06
Glendale	999,933	78,352	4,240	13.3%	5.6%	8.7%	75,633	4,240	7,372	\$25.67
Loop 303/Surprise	1,196,333	193,716	11,962	-	17.9%	8.1%	190,743	11,962	-4,018	\$24.52
Midtown	1,317,502	82,465	1,356	-	5.6%	8.9%	82,465	1,356	-18,402	\$21.67
North Interstate-17	183,463	36,070	0	-	19.7%	-	36,070	0	-576	\$23.96
North Phoenix	61,149	4,026	0	-	6.6%	0.0%	4,026	0	0	\$18.58
North Scottsdale	325,541	32,709	0	-	9.0%	15.9%	28,784	0	-351	\$20.59
NW Phoenix	1,648,446	467,190	17,637	-	34.0%	20.2%	462,253	17,637	-26,518	\$17.49
Paradise Valley	1,235,573	185,868	600	22.6%	15.8%	0.0%	180,382	600	-18,349	\$23.85
Piestewa Peak Corridor	300,558	75,909	8,613	34.3%	30.4%	8.3%	75,909	5,613	-9,100	\$24.27
Pinal County	680,348	83,040	0	-	14.4%	1.9%	83,040	0	3,049	\$20.77
Scottsdale Airport	738,552	50,245	0	11.4%	6.0%	-	47,398	0	5,302	\$28.46
South Scottsdale	846,288	108,329	0	-	16.1%	9.4%	105,342	0	28,270	\$23.86
South Tempe	508,932	79,287	3,310	-	17.0%	3.4%	79,287	3,310	12,838	\$21.49
Southwest Phoenix	184,577	10,581	0	-	0.0%	10.7%	10,581	0	-10,581	\$25.21
Superstition Corridor	1,813,293	184,961	7,811	0.0%	10.4%	17.3%	184,961	7,811	1,033	\$21.16
Tempe	929,573	207,573	0	12.5%	28.3%	15.7%	207,193	0	-2,360	\$22.72
West I-10	1,168,683	62,420	1,657	-	5.3%	39.4%	62,420	1,657	10,721	\$26.70
Total	26,487,069	3,360,398	109,765	13.5%	13.4%	11.7%	3,241,530	102,246	-10,328	\$22.96

The data contained in this market report is obtained from The CoStar Group, Inc., and is used under licensed permission. The report is based on all Metro-Phoenix markets for healthcare buildings, regardless of size. It includes sublease space only upon the date of availability, and includes any owner and renter occupied space.



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