

Phoenix

Medical Office Market Report Fourth Quarter 2019

Quick Stats

\$24.05

Full service average asking rental rate per square foot for 4Q 2019

13.5 %

Class A vacancy rate in the fourth quarter, down 40 bps from 3Q 2019

\$200

Average price per square foot for medical office real estate in 4Q 2019

800 k

Square feet of medical office space under construction

\$110.8 M

Total investment sales fourth quarter 2019

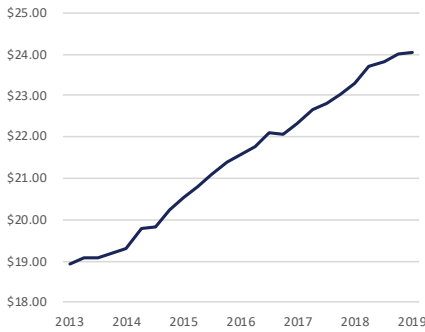
Retrofitting for the Future

The medical office real estate sector is highly responsive to consumer changes and new technology that presents great opportunities and challenges for patients, practitioners and real estate developers. Adaptive reuse of retail space has transformed healthcare delivery, de-emphasizing centralized campuses and bringing services closer to consumers. The sector begins the decade with strong momentum but challenges persist: a shortage of skilled staff, the high cost of upgrading technology, medical record data security, and the need to retrofit obsolete properties among them.

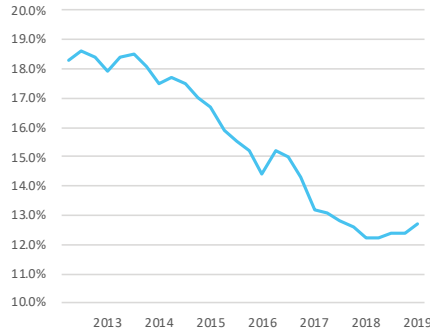
Historically, Phoenix billed itself as a healthcare mecca. Before a cure for tuberculosis was developed at the end of WWII, the region was known for its therapeutic climate and numerous facilities for both the affluent and indigent. Scottsdale earned the nickname "White City," a reference to the white tents where

patients lived under the desert sun. The less well-off gathered in an area known as The Colony, which later became Sunnyslope, a North Phoenix working class district. Today, the Valley has several medical hubs including the Mayo Clinic campus, Phoenix Children's Hospital and Banner University Medical Center near downtown, Ironwood Square and the HonorHealth facilities in Scottsdale. A number of established hospital networks are expanding in the Valley, including most notably the Mayo Clinic undertaking a \$648 million expansion through 2023. Chandler Regional Medical Center has committed \$194.8 million to its Dignity Health project, a new 5-story tower. A new \$170 million, 210 ksf hospital at HonorHealth's Sonoran Medical Center Campus will deliver in 3Q 2020, and in Sun City, Banner Boswell Medical Center is building a \$106 million 6-story patient tower.

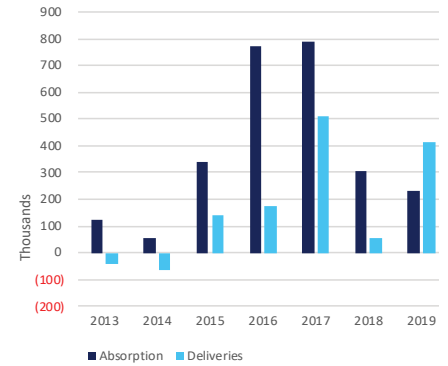
Average Rental Rates



Average Vacancy Rates



Absorption & Deliveries



Top Leases

Tenant	Name	Submarket	Square Feet	Type
Stockbridge	555 N 18th Street	Midtown/Central Phoenix	27,858	Direct
Unknown	5757 W Thunderbird Road	Deer Valley/Airport	10,623	Direct
Unknown	1112 E McDowell Road	Midtown/Central Phoenix	5,100	Direct
Unknown	14040 N Cave Creek Road	Paradise Valley	4,300	Direct
America's Health Center	9300 E Raintree Drive	Scottsdale Airpark	4,297	Direct

Top Sales

Buyer	Name	Submarket	Square Feet	Sale Price	Price/SF
Camelback Services	The Centre - South Building	Midtown/Central Phoenix	37,500	\$8,278,429	\$221
Camelback Services	The Centre - North Building	Midtown/Central Phoenix	37,500	\$7,371,571	\$197
Harrison Street Capital	Sandstone East	Mesa East	11,308	\$4,880,000	\$432
DAVCO Realty Advisors	Ranch Medical & Dental Center	Superstition Corridor	9,000	\$3,300,000	\$367
AMERCO Real Estate Company	2620 N 3rd Street	Midtown	18,425	\$3,057,912	\$166

Top Projects Under Construction

Property	Submarket	Completion	Total SF	% Preleased/Owned
Wexford	Downtown	4Q 2020	227,000	54.4%
Maricopa Integrated Health System	Glendale	2Q 2020	127,000	100.0%
90th Street Medical Campus	Central Scottsdale	4Q 2020	90,000	0.0%
AKIOS Medical Campus	Glendale	1Q 2020	68,000	41.2%
17300 North Perimeter Drive	Scottsdale Airpark	1Q 2020	48,514	49.6%

Trends to Watch

Tech advances in medicine, while exciting, are also overwhelming. The public expects healthcare to be on the cutting edge. However, change has consequences.



Data Security

Consumers want convenience but also security when it comes to healthcare records & how data is shared. Breaches are frequent and troubling.



Predictive Patients

As more people have more access to information, patients are increasingly pro-active. Advances in genetic testing alert patients often before physicians have examined them.

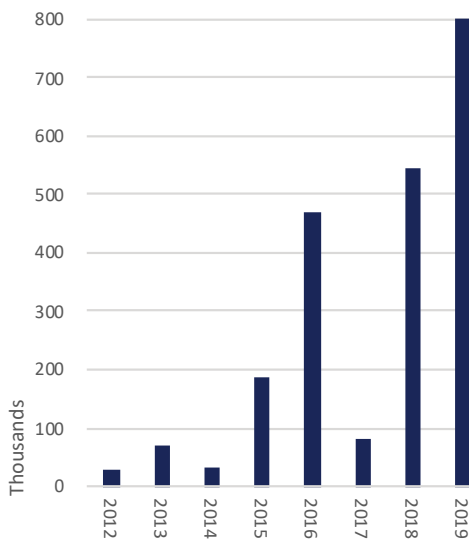


Physician Tech

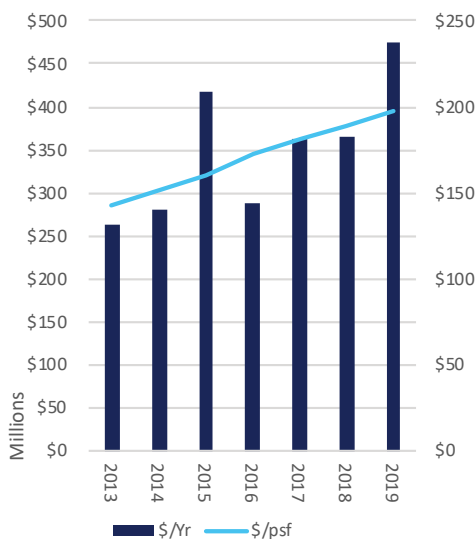
Medicine on the cutting edge requires highly-skilled physicians to use technology & interpret results. An ecosystem of support has sprung up to assist providers..

Price per square foot is right at the \$200 mark, surpassing the pre-recession high of \$198 in 3Q 2007.

Under Construction



Investment Sales



Rental Rates

Rent growth peaked in 3Q 2006 at 9.6% before plummeting to -12.6% in 4Q 2009. Growth came back into positive territory at the beginning of 2013 and has averaged around 3.8% growth in the subsequent seven years. However, according to experts, actual rent is expected to flatten in the next few years. The growth rate may fall below 2% by 2021.

Vacancy

Overall vacancy rate began to trend slightly upwards in throughout 2019. Class A medical office has the highest rate at 13.5%, down 40 basis points from the previous quarter, however both class B & C product vacancies inched upwards by 60 and 120 basis points respectively. A building surge will likely mean that vacancies levels will rise somewhat in the near term. Availability varies significantly by submarket. Northwest Phoenix with its substantial inventory reported the highest submarket vacancy at 24.3%. In submarkets with over a million square feet of inventory, the lowest vacancy rate at 4.9% is West I-10 which includes the booming suburb of Goodyear.

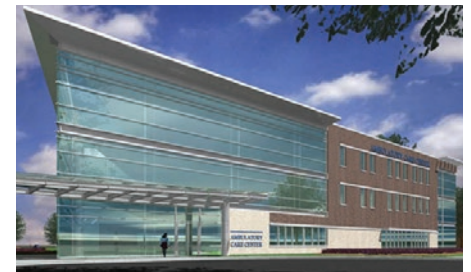
Leasing

Leasing activity remained constant, if not particularly robust, in the past year. Tenants leased 390 thousand square feet (ksf) of medical office space during the quarter. The annual total of 1.5 million square feet (msf) leased in 2019 ticked up 8% over the previous year. While months on the market fell slightly to 12.2 months, the figure is half the time registered at the sector's nadir in 1Q 2016. The largest signing occurred in October at the now-defunct St. Luke's Medical Center, when Stockbridge Capital Group took 27,858

sf in the medical office building at the site as it transitions from a traditional hospital campus to largely private medical office spaces.

Construction

The pace of construction activity picked up in the past two years after a decade of minimal building. 800 ksf of medical office space is currently under construction, down considerably from the sector's peak building boom in 2006, when 2.2 msf were delivered. Current project deliveries are expected to peak in 4Q 2020 before tapering. The Wexford at the downtown biomedical campus is still the top project by size currently under construction in Metro Phoenix. The 90th Street Medical Campus, a 90 ksf project, broke ground in Central Scottsdale near Loop 101 and is expected to deliver in December 2020.



90th Street Medical Campus

Investment Sales

Sales volume has risen steadily over the past three years with 2019 finishing at \$475.7 million in medical office transactions. Price per square foot is right at the \$200 mark, surpassing the pre-recession high of \$198 in 3Q 2007. In November, two buildings at The Centre (4400 N 32nd Street), traded for a total of \$15.7 million (\$209 psf). The biggest non-portfolio sale achieved more than twice figure per square foot when Sandstone East in Mesa sold for \$4.9 million (\$432 psf) in October.

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	Avg. Ask Total (FS)
44th St Corridor	101,929	16,923	0	-	21.5%	7.0%	15,723	0	0	-
Airport Area	155,399	220	0	-	0.0%	0.0%	0	0	0	-
Arrowhead	2,424,881	309,690	4,742	29.1%	9.9%	13.0%	278,952	4,742	7,357	\$24.58
Camelback Corridor	492,957	38,848	9,928	2.6%	12.7%	14.4%	38,848	9,928	(4,621)	\$26.95
Central Scottsdale	1,481,647	15	3,762	8.1%	10.0%	0.0%	135,195	3,762	60,581	\$25.82
Chandler	1,747,639	156,128	8,908	0.0%	9.6%	2.9%	152,740	8,908	(984)	\$18.22
Deer Valley/Airport	1,447,572	203,099	4,574	2.7%	15.0%	11.8%	184,020	4,574	(26,064)	\$26.80
Downtown	676,931	34,611	0	0.0%	9.3%	0.0%	34,611	0	0	-
Gateway/Airport/Loop 302	1,556,428	139,795	1,973	19.7%	5.6%	0.0%	106,140	1,973	26,702	\$27.42
Glendale	1,104,932	132,765	5,997	22.2%	10.7%	6.7%	132,795	5,997	41,234	\$25.67
Loop 303/Surprise	1,234,052	161,229	8,330	0.0%	14.5%	0.0%	161,229	8,330	(9,058)	\$26.10
Mesa Downtown	117,931	17,540	0	-	-	19.2%	17,540	0	(6,669)	\$12.00
Mesa East	1,257,977	141,421	2,995	-	11.6%	10.5%	138,541	2,995	14,023	\$16.96
Midtown	1,774,047	165,051	1,356	0.0%	9.8%	10.1%	166,051	1,356	(22,001)	\$20.63
Midtown/Central Phoenix	1,360,256	174,066	0	0.0%	11.5%	2.7%	177,738	0	4,242	\$20.27
North Phoenix/Cave Creek	61,319	0	3,000	-	4.9%	-	0	3,000	0	\$18.48
North Scottsdale/Carefree	461,853	44,670	300	-	8.8%	15.3%	44,670	300	1,578	\$21.14
North I-17	206,906	37,046	0	-	17.9%	-	37,046	0	(9,585)	\$17.19
Northwest Outlying	40,277	1,015	0	-	4.7%	0.0%	1,015	0	0	\$16.20
NW Phoenix	1,803,542	437,165	7,336	-	32.7%	8.3%	431,165	7,336	(26,369)	\$16.64
Paradise Valley	1,349,076	208,583	0	25.6%	14.7%	7.1%	204,174	0	20,730	\$20.39
Piestewa Peak Corridor	376,333	80,352	1,200	28.0%	23.9%	5.2%	80,352	1,200	3,955	\$18.27
Pinal County	699,354	85,587	0	-	14.5%	3.2%	85,587	0	0	\$14.19
Scottsdale Airpark	895,189	84,357	14,073	7.0%	11.6%	-	84,357	14,073	(5,935)	\$25.07
Scottsdale South	860,851	137,451	12,564	-	19.0%	15.2%	135,449	12,564	(10,209)	\$20.97
South Tempe/Ahwatukee	535,926	97,550	15,810	-	20.7%	0.0%	89,050	15,810	(17,311)	\$17.21
Southwest Outlying	27,486	0	0	-	0.0%	0.0%	0	0	0	\$24.00
Southwest Phoenix	184,577	0	0	-	0.0%	0.0%	0	0	0	\$23.25
Superstition Corridor	1,719,601	216,917	5,000	0.0%	12.8%	8.7%	208,477	5,000	(51,037)	\$18.43
Tempe	1,055,782	188,223	0	-	13.0%	16.4%	155,523	0	8,954	\$21.58
West I-10	1,223,219	46,875	2,356	-	4.0%	0.0%	46,875	2,356	641	\$22.63
Total	28,436,459	3,282,833	114,204	13.5%	12.4%	9.2%	4,376,338	202,553	154	\$24.05

*The data contained in this market report is obtained from The CoStar Group, Inc., and Revista, and is used under licensed permission. The report is based on all Metro Phoenix markets for medical 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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