

Phoenix

Medical Market Report Second Quarter 2019

Quick Stats

\$41.2 M

Increase in investment sales
from first quarter 2019.

\$24.02

Full service average asking
rental rate per square foot for
second quarter 2019.

-91.2 K

Square foot absorption for
second quarter 2019.

431.9 K

Square foot of medical office
space under construction
during second quarter 2019.

12.3%

Vacancy rate in the second
quarter, up 0.1% from first
quarter 2019.

Valley's MOB Market Remains Attractive to Investors

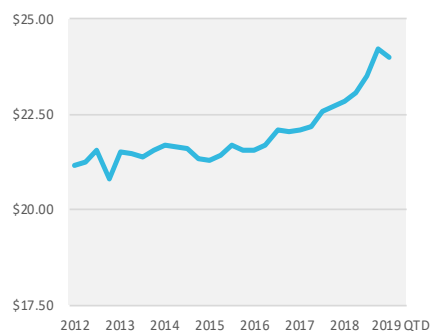
Investment sales of \$148.5 million and the disposition of two large portfolios were Q2 2019 evidence that Metro Phoenix remains a major player in the healthcare real estate market. Two assets in the Piestewa Peak Corridor were part of a 55-property portfolio that sold in May for \$1.25 billion, or \$380.47 per square foot (psf). In June, an entire portfolio of five office properties in Scottsdale sold for \$25.93 million, commanding \$184.64 psf. The positive news was mildly tempered on the leasing side, however, as the quarter witnessed a negative net absorption and a small rent pull-back. But with Phoenix leading the Nation in both job creation and population growth, the fundamentals are strong, and the medical office market is on solid ground.

Employment

Phoenix continued its expansion in jobs and office space in Q2 2019 matching

a strong Q1 2019. Bolstered by strong economic development, large employers are choosing to put more people in Phoenix due to the climate, affordability and a business-friendly environment. Metro Phoenix added 68,000 new jobs for the year ending April 30. That's up 3.2 percent more than in 2018. The Metro Phoenix unemployment rate dropped from 4.1 percent to 3.7 percent. April's Phoenix job hike was higher than hiring in 21 other states including Colorado, Massachusetts, Oregon, Nevada and Utah. In Metro Phoenix, healthcare and education services hiring was up 14,400 in year-over-year data, putting the sector workforce at 277,600. Healthcare hiring never slowed during the Great Recession. In the peak employment month before the downturn, October 2007, there were 179,900 healthcare workers in the Valley. At the trough, or low point in employment, the healthcare workforce increased to 197,700, a gain of 17,800 jobs.

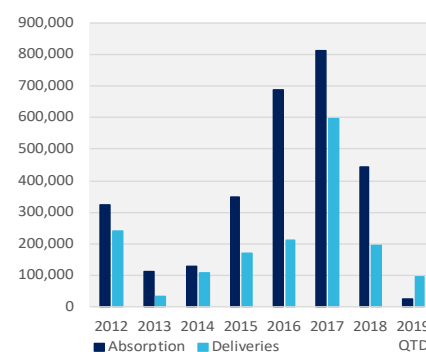
Rental Rates



Vacancy Rates



Absorption & Deliveries



Top Leases

Tenant	Building	Submarket	Square Feet	Type
Phoenix Children's Hospital	3370 S. Mercy Road	Gateway Airport/Loop 202	40,000	Direct
Rehabilitation Center	108 E. 2nd Avenue	Mesa Downtown	13,095	Direct
Hopebridge Autism Therapy Centers	5859 W. Talavi Blvd	Deer Valley/Airport	11,021	Direct
Family Clinic	1201 S. 7th Avenue	Downtown	10,409	Direct
Northwest Vascular	13128 N. 94th Drive	Arrowhead	10,000	Direct
Symbius	20333 N. 19th Avenue	Deer Valley/Airport	8,234	Direct

Top Sales

Buyer	Building	Submarket	Square Feet	Sale Price	Price/SF
Hammes Partners	Spectrum Medical Commons	Gateway Airport/Loop 202	43,355	\$17,750,000	\$409
Millice Group, Ltd.	Clarendon Place	Midtown	91,353	\$13,650,000	\$149
Welltower, Inc.	Lincoln Medical Center I	Piestewa Peak Corridor	29,319	\$10,583,256	\$361
MB Real Estate Services	Scottsdale at Mescal	Central Scottsdale	48,181	\$8,716,982	\$181
MBRE Healthcare	Thunderbird Wellness Centre	Arrowhead	20,160	\$7,181,935	\$356
Welltower, Inc.	North Mountain Medical Plaza	Piestewa Peak Corridor	27,072	\$7,000,000	\$259

Top Projects Under Construction

Building	Submarket	Completion	Total SF	% Preleased/Owned
Maricopa Integrated Health System	Glendale	Q2 2020	127,000	100.0%
Mercy Gilbert II	Gateway Airport/Loop 202	Q3 2019	80,000	75.6%
AKOS Medical Campus	Glendale	Q3 2019	68,000	41.2%
Mercy Medical Commons II	Gateway Airport/Loop 202	Q3 2019	56,000	39.3%
Ortho Arizona	Gateway Airport/Loop 202	Q4 2019	49,600	100.0%

Trends to Watch

Small scale urgent care and retail clinics continue popping up in urban and suburban areas.



Constant Change
By 2024, there will be fewer independent hospitals and health systems.



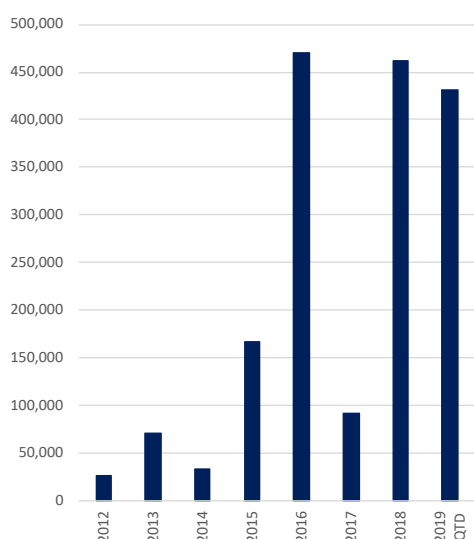
Value-Based
15% of global health care spending will be tied to value-based models in 2019.



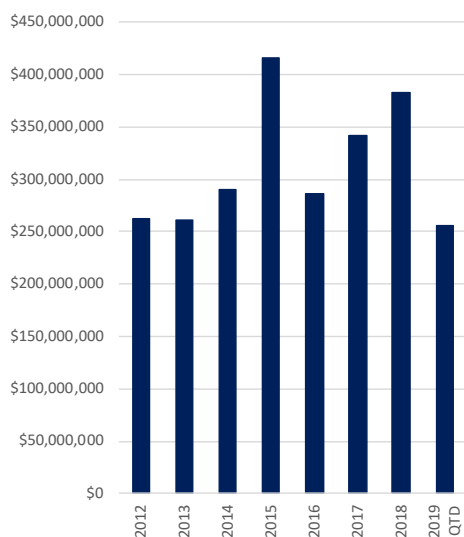
New Leasing Rules
Within 3 years, providers will have less flexibility on how they classify their leases.

**Metro Phoenix
added 68,000 new
jobs for the year
ending April 30.
That's up 3.2%
more than 2018.**

Under Construction



Investment Sales



Employment (Cont.)

The sector has never lost momentum; the number of jobs by April 2019 were 55 percent higher than 2007. In early Q2, most new jobs were created in construction, an industry facing strong service demand even as contractors struggle to find workers. The workforce increased 16,600 jobs to 138,100. That number is equal to employment in the sector in May 2004. Before the Great Recession, construction jobs peaked at 174,200 in Metro Phoenix in July 2007. The bulk of construction hiring was in the specialty trade.

Leasing

The second quarter recorded a negative net absorption of -91,243 sf with a delivery of just 10,135 sf. Three submarkets kept things “positive” with net absorption of 14,383 sf, Scottsdale South; Arrowhead, 11,868 sf; and Chandler, 10,513 sf. The top lease in Q2 2019 went to Phoenix Children's Hospital, which will occupy 40,000 sf at 3370 S. Mercy Road, in Gilbert.



Phoenix Children's Hospital

The Rehabilitation Center took 13,095 sf at 108 E. 2nd Avenue., in the Mesa Downtown submarket. Three additional leases of more than 10,000 sf were also recorded: Hopebridge Autism Therapy Centers, 11,021sf; Family Clinic, 10,409 sf; and Arrowhead, Northwest Vascular, 10,000 sf.

Investment Sales

Investment sales in Q2 2019 totaled a whopping \$148.5 million after the

market witnessed a robust \$107.3 million in Q1 2019. Investment sales YTD total \$256.6 million on 156 transactions, with a median cap rate of 7.0. Two large portfolio sales buoyed investment for the quarter. Lincoln Medical Center I (\$10.583 million, 29,319 sf) and North Mountain Medical Plaza (\$7 million, 27,072 sf) in the Piestewa Peak Corridor were part of a portfolio of 55 properties sold in May for \$1.25 billion. Welltower, Inc. purchased the portfolio that totaled 3.285 msf.



Lincoln Medical Center I

An entire portfolio of five office properties in Scottsdale sold in June for \$25.93 million (140,448 sf). Included were Scottsdale at Mescal in Central Scottsdale and Thunderbird Wellness Center in the Arrowhead submarket. MB Real Estate Services/MBRE Healthcare was the buyer.



Spectrum Medical Commons

The top non-portfolio sale was to Hammes Partners, a Wisconsin-based private equity firm, who acquired Spectrum Medical Commons in Gilbert for \$17.75 million. The price commanded \$409 psf, making it one of the highest psf rates for a multi-tenant medical office building in the Valley.

Rental Rates

Average asking rental rate for the quarter was \$24.02 psf, full service (FS). The rate represents a slight dip from Q1 2019's \$24.20 psf. Of three submarkets with net absorption of more than 10,000 sf, the average asking rate was \$22.33 psf, Scottsdale South; \$24.78 psf, Arrowhead; and \$18.16 psf, Chandler. Rates are expected to modestly rise throughout the remainder of 2019.

\$24.02

AVERAGE ASKING
RENTAL RATE (FS)

Vacancy

Medical office building vacancy for the quarter was 12.3%. It was a slight increase from Q1 2019 (12.2%). This trend is expected for the remainder of 2019 as the construction pipeline is delivered to the market. Vacant direct space for the quarter was 3.216 million square feet, with an additional 145,386 sf available via sublease.

Construction

The Metro Phoenix medical office building market has projects totaling 431,888 sf under construction.

431.9 K

SF UNDER
CONSTRUCTION

The Gateway Airport/Loop 202 submarket boasts three of the top five construction projects. The Glendale submarket features the other two, including the No. 1 project for the Maricopa Integrated Health System. The new West Valley Healthcare Clinic will total 127,000 sf at Grand Avenue and Cotton Crossing in Peoria. The AKOS Medical Campus in Avondale is looking at a Q3 2019 opening.



AKOS Medical Campus

Gateway Airport/Loop 202 Project Overview

The three major projects under construction in the Gateway Airport/Loop 202 submarket include Mercy Gilbert II (80,000 sf), the second largest project under construction during the second quarter, and Mercy Medical Commons II (56,000 sf) which are both scheduled for Q3 2019 completion. Ortho Arizona (49,600 sf) is set to open in Q4 2019.



Mercy Medical Commons II



Deer Valley

Markets on the Rise

Northwest Phoenix saw the largest increase in investment sales for the second quarter with a \$145,873 increase from first quarter 2019.

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	Q2 Net Absorption (SF)	Avg. Ask Total (FS)
44th St Corridor	122,229	15,723	0	-	39.8%	0.0%	44,144	0	0	\$23.50
Airport Area	172,092	1,220	0	-	0.0%	2.2%	1,220	0	0	\$21.90
Arrowhead	2,427,540	326,924	2,500	35.5%	15.1%	19.5%	413,645	9,229	11,868	\$24.78
Camelback Corridor	475,562	25,100	11,797	5.0%	5.6%	17.5%	40,458	11,797	-9,707	\$27.51
Central Scottsdale	1,413,052	162,042	50,149	30.4%	13.0%	0.0%	196,823	17,777	-49,927	\$24.88
Chandler	1,682,578	103,366	8,663	0.0%	6.7%	6.5%	172,745	9,814	10,513	\$18.16
Deer Valley/Airport	1,443,815	191,226	4,574	11.8%	13.8%	6.5%	211,650	5,992	-7,433	\$25.97
Downtown	676,931	49,610	0	0.0%	14.1%	0.0%	39,201	0	0	\$23.48
Gateway/Airport/Loop 302	1,399,354	110,712	0	0.0%	8.9%	0.0%	204,753	0	6,330	\$26.52
Glendale	1,094,500	144,789	27,730	21.8%	15.8%	5.2%	195,853	27,730	-10,876	\$27.21
Loop 303/Surprise	1,181,075	144,334	8,330	-	13.6%	0.0%	154,439	8,330	3,291	\$26.28
Mesa Downtown	123,811	22,804	0	-	0.0%	23.4%	22,804	0	-7,907	\$15.11
Mesa East	1,218,893	153,947	0	-	12.4%	13.1%	162,080	0	-7,698	\$18.76
Midtown	1,305,864	51,264	1,356	-	5.3%	0.0%	86,089	1,356	487	\$20.42
Midtown/Central Phoenix	1,344,340	206,996	0	-	18.4%	7.4%	226,296	0	2,645	\$18.78
North Phoenix/Cave Creek	61,149	0	3,000	-	4.9%	-	1,768	3,000	0	\$20.74
North Scottsdale/Carefree	393,145	43,874	0	-	9.9%	19.7%	56,653	0	2,299	\$21.55
North I-17	200,929	25,988	0	-	12.9%	-	45,988	1,873	-2,743	\$24.61
Northwest Outlying	40,277	1,015	0	-	4.7%	0.0%	1,015	0	0	\$18.54
NW Phoenix	1,815,431	366,420	12,308	-	24.9%	11.0%	444,804	11,113	909	\$19.18
Paradise Valley	1,280,747	238,798	1,572	28.8%	18.0%	12.3%	280,124	3,316	-29,283	\$17.64
Piestewa Peak Corridor	365,170	79,680	6,813	36.7%	19.4%	11.2%	111,242	6,813	-798	\$26.83
Pinal County	689,354	90,479	0	-	14.9%	5.1%	94,264	0	-4,298	\$13.69
Scottsdale Airpark	841,042	56,427	200	7.0%	6.7%	-	102,272	21,264	-8,257	\$26.78
Scottsdale South	869,368	88,701	1,534	-	17.5%	8.7%	112,059	3,534	14,383	\$22.33
South Tempe/Ahwatukee	532,750	91,015	3,310	-	18.7%	0.0%	108,561	3,310	-12,898	\$20.81
Southwest Outlying	23,406	2,450	0	-	32.9%	0.0%	0	0	0	\$31.86
Southwest Phoenix	184,577	0	0	-	0.0%	0.0%	5,000	0	0	\$27.99
Superstition Corridor	1,716,065	174,715	1,550	-	10.6%	7.7%	269,016	5,929	6,652	\$16.01
Tempe	1,021,866	190,840	0	-	22.4%	12.0%	197,125	1,552	-8,255	\$24.90
West I-10	1,255,149	55,955	0	-	4.3%	39.4%	102,824	0	9,460	\$29.85
Total	27,372,061	3,216,414	145,386	18.4%	12.4%	9.3%	4,104,915	153,729	-91,243	\$24.02

*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 medical buildings, regardless of size. It includes sublease space only upon the date of availability, and includes any owner and renter occupied space. Both current and historical data has been adjusted with corrected or updated information, after it was obtained. This may prevent comparison to previously released reports.



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