

Phoenix

Office Market Report Second Quarter 2019

Quick Stats

3.7%

Current Metro Phoenix
unemployment rate dropped

15.1%

Office space vacancy in
second quarter 2019

\$31.39

Per square foot Class A office
space average asking rental rate

1.9 M

Square feet net
absorption for 2019 YTD

\$272 M

Total sales volume in
second quarter 2019

Tempe Office Market Remains Talk of the Town

It was a stellar Q2 2019 for office properties as Metro Phoenix experienced its 24th straight quarter of positive absorption. This positive news also spurred interest from out-of-state office investors. Tempe seized bragging rights as the tightest office market in Metro Phoenix with an overall vacancy rate of 6%, and an even more impressive vacancy rate of 3% for high-quality properties. Tempe also boasts four of the top five construction projects in the Valley as well as the top two investment sales. For the second straight quarter, the demand for office space was spurred by gains in construction, education, health services and manufacturing.

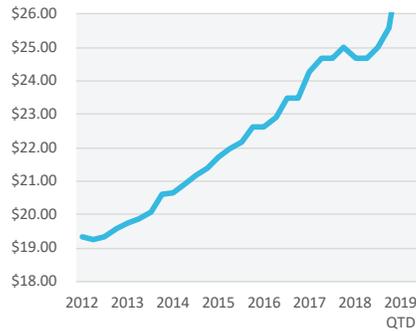
Employment

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

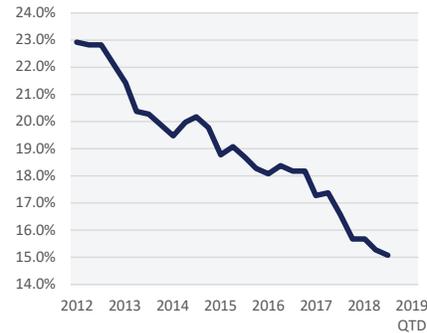
environment. Metro Phoenix added 68,000 new jobs for the year ending April 30. That's up 3.2 percent more than in 2018. The Metro Phoenix unemployment rate dropped from 4.1 percent to 3.7 percent. April's Phoenix job hike was higher than hiring in 21 other states including Colorado, Massachusetts, Oregon, 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. The sector has never lost momentum; the number of jobs by April 2019 were 55 percent higher than 2007.

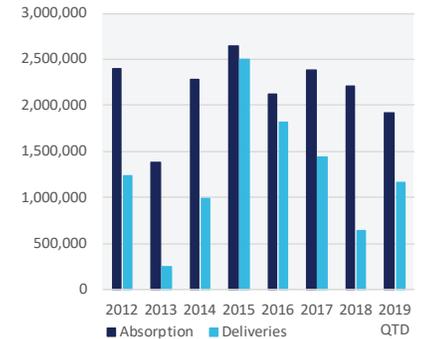
Rental Rates



Vacancy Rates



Absorption & Deliveries



Top Leases

Tenant	Building	Submarket	Square Feet	Type
Bridgepoint Education	Ascend at Chandler Airport Center	Chandler	130,642	Direct
WeWork Downtown	101 E. Washington Street	Downtown	90,576	Direct
Arizona State University	Skysong Innovation	Scottsdale South	50,000	Direct
Ascend Learning	The Reserve at San Tan	Chandler	40,440	Direct

Top Sales

Buyer	Building	Submarket	Square Feet	Sale Price	Price/SF
Menlo Equities	Wells Fargo Office Building	Tempe	214,303	\$52,400,000	\$245
Strategic Office Properties	The Circuit	Tempe	185,000	\$46,000,000	\$249
DRA Advisors	Camelback Lakes Corporate Center	Camelback Corridor	136,540	\$27,602,261	\$202
Gramercy Capital Corp	One Chandler Corporate Center	South Tempe/Ahwatukee	117,394	\$25,210,000	\$215
BH Properties, LLC	Northsight Financial Center	Scottsdale Airpark	120,040	\$23,800,000	\$198

Top Projects Under Construction

Property	Submarket	Completion	Total SF	% Preleased/Owned
The Grand at Papago Park Phase II	Tempe	Q3 2019	345,795	0.0%
Block 23 At Cityscape	Downtown	Q3 2019	280,399	59.0%
The Watermark Phase I	Tempe	Q3 2019	265,000	26.1%
I.D.E.A. Tempe Phase I	Tempe	Q1 2020	185,833	64.6%
777 Tower at Novus Innovation Corridor	Tempe	Q2 2020	169,500	0.9%

Trends to Watch

The Phoenix market sees continued growth in population, inventory and coworking space for yet another quarter. However, vacancy continues to decrease.



Population Growth

Phoenix is reportedly the fourth largest growing state in 2019 YTD, with the state's population at 7.27 million, an increase of 1.7%.



Vacancy Decrease Continues

Despite continued office inventory additions, vacancy dropped to its lowest rate in the second quarter since second quarter 2008.

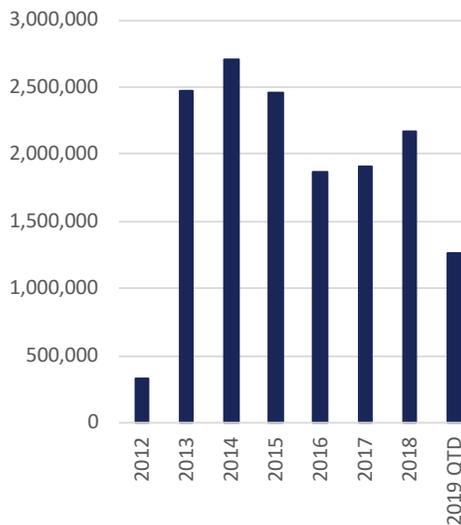


Coworking Growth Continues

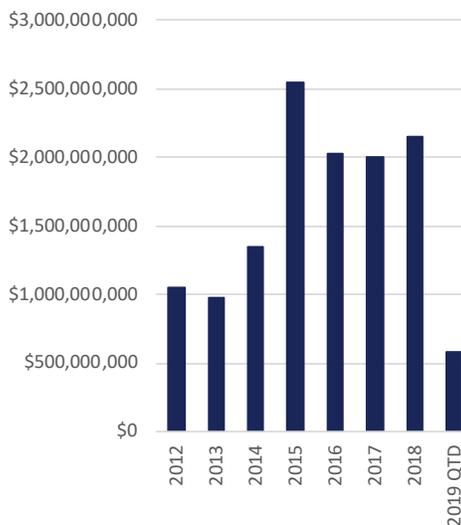
Coworking spaces double Phoenix footprint in only two years with WeWork, Industrious and Novel Coworking dominating the market.

The Metro Phoenix office market remains strong as businesses continue bringing their operations to the Valley, driving demand while increasing employment opportunities.

Under Construction



Investment Sales



Absorption & Vacancy

The Valley's 24th consecutive quarter of positive net absorption helped lower the vacancy rate to 15.1%, down from 15.3% in Q1 and 15.8% a year ago. Gross leasing activity through the first two quarters of 2019 exceeded 3 million square feet while net new absorption topped one million square feet bringing the year to date total to more than 1.9 MSF.

Submarket vacancy is not the best measure of desirability in a rapidly expanding economy. A better judge is the amount of space that is under construction and planned. However, in submarkets with more than 1 MSF of space, Tempe is the low vacancy leader at 6.2% followed by Glendale at 7.8% and Superstition Corridor at 8.6%.

Rental Rates

Average Class A rental rates kept rising in Q2 2019 and now average \$31.39, up by 7.5% from Q1 and 8% from a year ago. Class B rental rates stayed stable at an average of \$23.32 from Q1 and up slightly year over year. The most expensive submarkets typically match the most desired submarkets (those with the lowest vacancy as denoted above).



Camelback Corridor

Tempe leads the way with an average Class A rental rate of \$39.18 followed by the Camelback Corridor at \$36.95 and Scottsdale South at \$32.99.

The lowest Class A average rental rate is \$23.09 in the Northwest Phoenix submarket. However, the top lease of Q2 2019 was in Chandler with Bridgepoint Education at Ascend at Chandler Airport with 163,142 SF.



Bridgepoint Education at Ascend

Followed by the Downtown Phoenix submarket, WeWork took 90,576 SF at 101 E. Washington; Arizona State University took 50,000 at SkySong in the Scottsdale South submarket, and Ascend Learning took 40,440 SF in Chandler.



WeWork at 101 E. Washington Street

New Construction

In the office development arena, suburban markets in the Southeast Valley continue to dominate. When considering top tier Class A space only in Tempe, the vacancy is a paltry 2.9%. Since 2016, Tempe office inventory has increased by 22% but has still fallen short of demand. Several developers are scrambling to finish product there, but it won't deliver until 2020, leaving large tenants with immediate needs to consider other areas.



New Construction (cont.)

The largest construction project, The Grand at Papago Park Phase II in Tempe, is scheduled to deliver 345,795 SF in Q3 2019.



The Grand at Papago Park Phase II

Developers delivered more than 500,000 SF of new space in Q2, more than half of which was pre-leased. More than two thirds of the office space under construction currently is in the Southeast Valley (Tempe, Chandler and Gilbert). The market is scheduled to deliver 3.5 MSF of new space before the end of 2019. With almost 4 MSF of potential demand coming from 62 companies, new construction is still not keeping pace which will keep Phoenix running for the foreseeable future.



Watermark Phase I

Besides The Grand at Papago Park, Tempe is on pace to deliver Watermark Phase I in Q3 2019 (265,000 SF); I.D.E.A. Tempe Phase I in Q1 2020 (185,833); and 777 Tower at Novus Innovation Corridor in Q2 2020 (169,500 SF).

Investment Sales

Investors from outside Phoenix kept

placing money in office buildings in Q2 2019. Volume is at record levels even though it's starting to moderate in our markets around the U.S. Sales volume for Q2 was \$272 million compared to \$313 million in Q1 and \$470 million a year ago. The largest transaction of the quarter was Menlo Equities purchasing the Wells Fargo Building in Papago Park for \$52.4 million.



Wells Fargo Building in Papago Park

Second was the \$46 million purchase of The Circuit by Strategic Office Properties and DRA Advisors' purchase of Camelback Lakes for \$27.6 million.



The Circuit

Active investors in Phoenix today tend to fall into two categories: those interested in purchasing suburban buildings with credit tenants with long-term leases or those finding value in well-located assets in core submarkets such as Camelback and the Central business district that can be repositioned.

Market By The Numbers*

Submarket	Total RBA (SF)	Vacant Space Direct	Available Space Sublease	Submarket Vacancy	Absorption Class A	Absorption Class B	Q2 Net Absorption (SF)	YTD Net Absorption	Avg. Ask Class A (FS)	Avg. Ask Class B (FS)
44th St Corridor	2,564,918	412,769	6,268	16.3%	-4,837	-1,163	-12,094	-10,614	\$27.68	\$23.48
Airport Area	7,789,817	1,339,231	152,123	19.1%	-27,287	-29,712	-56,999	78,713	\$26.97	\$20.35
Arrowhead/Loop 303/ Surprise	817,743	93,243	3,677	12.9%	1,400	15,016	16,416	-13,457	\$26.00	\$25.53
Camelback Corridor	7,286,568	1,291,646	80,216	18.8%	-71,835	-26,359	-98,194	36,131	\$36.95	\$26.85
Central Scottsdale	5,274,293	566,924	54,248	11.8%	5,352	57,020	62,372	54,404	\$30.02	\$26.14
Chandler/Gilbert	6,306,978	1,282,243	68,667	20.3%	104,587	395,150	499,727	558,013	\$31.34	\$23.81
Downtown	7,701,496	997,928	108,988	13.9%	18,567	-37,092	-18,525	-96,955	\$32.73	\$29.32
Gateway Airport/ Loop 202	267,319	13,176	5,164	6.9%	0	5,672	5,672	-25,148	-	\$24.91
Glendale	1,316,542	103,220	0	7.8%	12,415	11,887	27,402	-21,729	\$26.17	\$24.50
Mesa	819,440	61,850	0	7.5%	-	-17,519	3,197	-26,335	-	\$18.06
Midtown	8,982,878	2,113,777	27,221	23.3%	-9,878	-9,291	-45,836	92,967	\$25.84	\$21.06
Midtown/Central Phoenix	1,450,313	185,244	0	12.8%	-	-13,243	-16,328	-15,457	-	\$19.34
N Scottsdale/Carefree	437,309	86,810	0	19.9%	0	-3,400	-3,400	6,630	-	\$27.64
North I-17/Deer Valley/ Airport	7,067,393	832,711	3,443	13.0%	23,558	-13,568	9,990	1,680	\$23.32	\$23.88
NW Phoenix	5,176,313	1,447,639	31,118	28.6%	19,363	38,927	79,154	-12,768	\$23.09	\$18.76
Paradise Valley	1,947,249	262,574	13,649	14.2%	27,921	-7,488	22,730	79,804	\$28.22	\$21.44
Piestewa Peak Corridor	1,958,134	371,636	6,021	19.3%	4,950	5,689	11,889	47,505	\$26.93	\$23.29
Pinal County	76,810	0	0	0.0%	-	0	0	0	-	-
Scottsdale Airpark	8,978,260	1,317,618	103,344	15.8%	82,736	25,609	108,345	170,706	\$31.23	\$27.67
Scottsdale South	3,878,474	430,223	37,468	12.1%	150,587	86,411	236,998	255,269	\$32.99	\$30.42
South Tempe/Ahwatukee	5,275,967	662,705	40,745	13.3%	0	42,200	59,853	183,388	\$32.49	\$21.83
Southwest Phoenix/ Outlying	812,669	173,512	0	24.1%	-	0	0	0	\$28.87	-
Superstition Corridor	2,538,418	211,020	6,506	8.6%	12,030	52,955	64,985	107,812	\$24.82	\$19.30
Tempe	9,495,681	591,445	8,264	6.2%	37,822	104,827	144,114	465,905	\$39.18	\$22.22
West I-10	430,724	47,264	0	11.0%	8,703	-11,241	-2,538	-2,286	\$27.54	\$25.09
Total	98,651,706	14,896,408	757,130	15.1%	396,154	671,287	1,098,930	1,914,178	\$31.39	\$23.32

*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 office buildings at least 20,000 square feet in size. It includes sublease space only upon the date of availability, and does not include any healthcare space or owner 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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