

## Phoenix

## Office Market Report Third Quarter 2019

### Quick Stats

**66.5 K**

New employment gains in Metro  
Phoenix from August 2018 to  
August 2019

**14.3%**

Office space vacancy in  
third quarter 2019

**\$30.89**

Per square foot class A office  
space average asking rental rate

**1.4 M**

Square feet net  
deliveries for 2019 YTD

**\$1.3 B**

Total sales volume for 2019 YTD

### Shifting to the Right Gear

As Phoenix continues to make impressive marks nationally, the specter of the last crash still hovers over the Valley. Great strides have been made to diversify the economy, invest in business & technology incubators, and reconsider the terrain to prepare for another inevitable downturn. Yet the sting of the Great Recession has created conditions in which under-supply may now be an issue as the city's profile rises and its investment reputation attracts expanding enterprises particularly from expensive West Coast markets. The Valley's office market vacancy is now fairly low and demand has been stronger than supply for the past eight years.

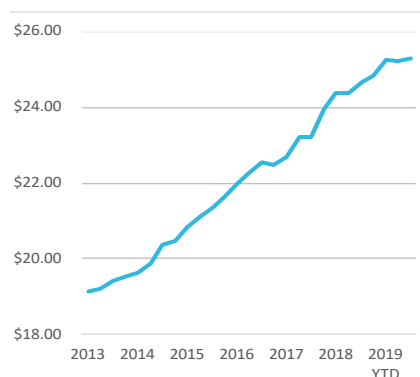
#### Employment

Phoenix continues to absorb new arrivals although Maricopa County's unemployment rate at 4.6% remains above the national average of 3.8%. The city added 66,500 non-farm jobs in the past year, a 2.3% year-over-year increase with the biggest

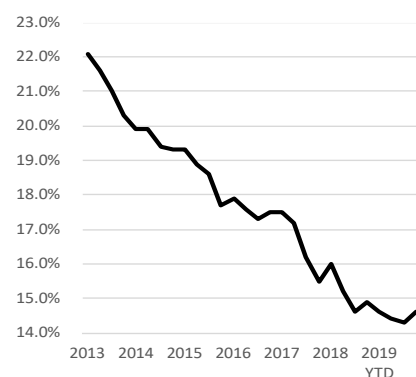
gains in construction and manufacturing. Upward wage pressures, particularly in the labor-constricted construction sector, are bumping up costs for employers and while the region is still an attractive option for workers, rising rents and housing prices are beginning to challenge the area's reputation for affordability.

Despite trade headwinds and a sense that the long economic expansion has run its course, accelerating household formation has helped buoy consumer confidence. Employment growth is also adjusting to demographic changes. The flow of baby boomers exiting the workforce is opening up opportunities for the even larger cohort of millennials held back by turbulence in the Great Recession during a time when they should have made significant career strides. Boomers, however, are retiring at a slower rate than previous generations and 45% have no retirement savings, keeping them at work longer than expected.

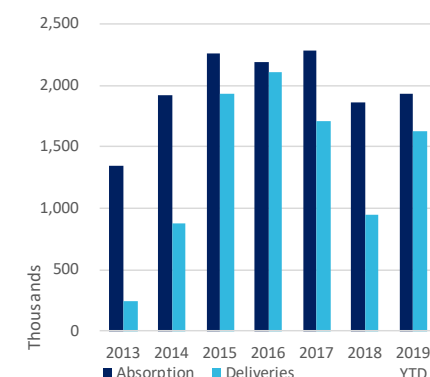
## Rental Rates



## Vacancy Rates



## Absorption & Deliveries



## Top Leases

Tenant	Building	Submarket	Square Feet	Type
WageWorks	Union at Riverview	Tempe	150,000	Direct
Deloitte	The Commons at Rivulon	Chandler	102,434	Direct
Grand Canyon University	3100 W. Camelback Road	Camelback Corridor	56,722	Direct
Confidential	1333 S. Spectrum Boulevard	Chandler	34,143	Direct

## Top Sales

Buyer	Building	Submarket	Square Feet	Sale Price	Price/SF
SKB - Scanlan Kemper Bard	US Bank Center + Parking Structure	Downtown	373,013	\$92,750,000	\$178
NGP V Fund	FBI Regional Headquarters	I-17/Deer Valley Airport	210,202	\$92,250,000	\$439
Transwestern	Camelback Esplanade III	Camelback Corridor	218,387	\$60,250,000	\$276
CIM Group	Northsight Corporate Center	Scottsdale Airpark	136,862	\$51,476,000	\$376
Innovatus Capital Partners	Waypoint 4	Tempe	153,134	\$44,565,228	\$291

## Top Projects Under Construction

Property	Submarket	Completion	Total SF	% Preleased/Owned
Block 23 at CityScape	Downtown	Q4 2019	280,399	59.0%
The Watermark Phase I	Tempe	Q4 2019	265,000	64.1%
Wexford Science & Technology	Downtown	Q4 2020	227,000	54.4%
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	0.4%

## Trends to Watch

Population growth, especially incoming younger workers priced out of superstar cities, is causing shifts in office space planning. Limited class A supply is driving rent growth while demographic changes, emerging flex space & productivity trends are reconfiguring the workplace.



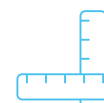
### Arrivals

The Phoenix Metro added approximately 200 new residents per day over the past year.



### Rent Growth

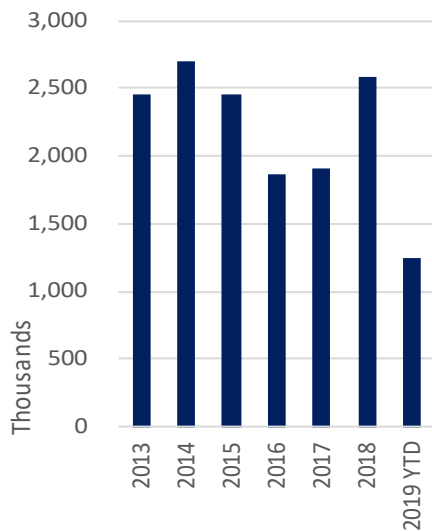
Rent growth is down from 2016 peaks, however relatively limited class A office supply is expected to keep it above historical averages.



### Space Adjustment

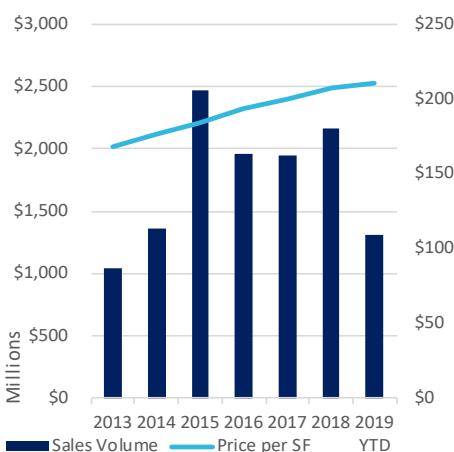
While square footage per employee fell in recent years, a partial reversal is now happening as flexible space offers new growth options.

## Under Construction



The risk now is an undersupplied market for contemporary offices just as demand switches into an even higher gear.

## Investment Sales



## Absorption & Vacancy

While new deliveries arrive at a steady clip in prime submarkets, the disconnect between supply and demand remains a challenging equation. Abundant caution from the last great downturn and its devastating aftermath tempered the market. The risk now is an undersupplied market for contemporary offices just as demand switches into an even higher gear.



**I.D.E.A. Campus at Tempe**

Several projects underway have preleased significant space to be delivered in the next 12 to 18 months including Deloitte, doubling its presence in the Valley with an additional 102,434 sf at the Commons at Rivulon – Building B in Gilbert and the medical technology giant, Becton Dickinson's Peripheral Intervention business set to occupy 120,000 sf at the I.D.E.A. Tempe campus scheduled for delivery in January 2020.

## Rental Rates

Rent growth in popular submarkets continues an upward trajectory, however in weaker submarkets like Northwest Phoenix and Downtown gains remain sluggish.

All eyes are on WeWork as it stumbled spectacularly in the run-up to a now-pulled IPO. As landlords examine leases and consider contingency plans, the Phoenix Office Market can count the co-working giant's late entry here as a blessing. That said, the bloom fell off

WeWork just as high-profile locations debuted including 47,737 sf at The Esplanade I for \$41.50 psf in September and 53,093 sf at \$28 psf on a 3-year lease that commenced October 1st in the US Bank Center. Two more sites are set to open in November – The Watermark Phase I, 68,968 sf at \$42 psf & Block 23 at CityScape downtown, 90,576 sf at \$38.50 psf – both in major new buildings. Expect intense local scrutiny as well as headline-grabbing news from WeWork's national C-Suite.



**WeWork at Esplanade I**

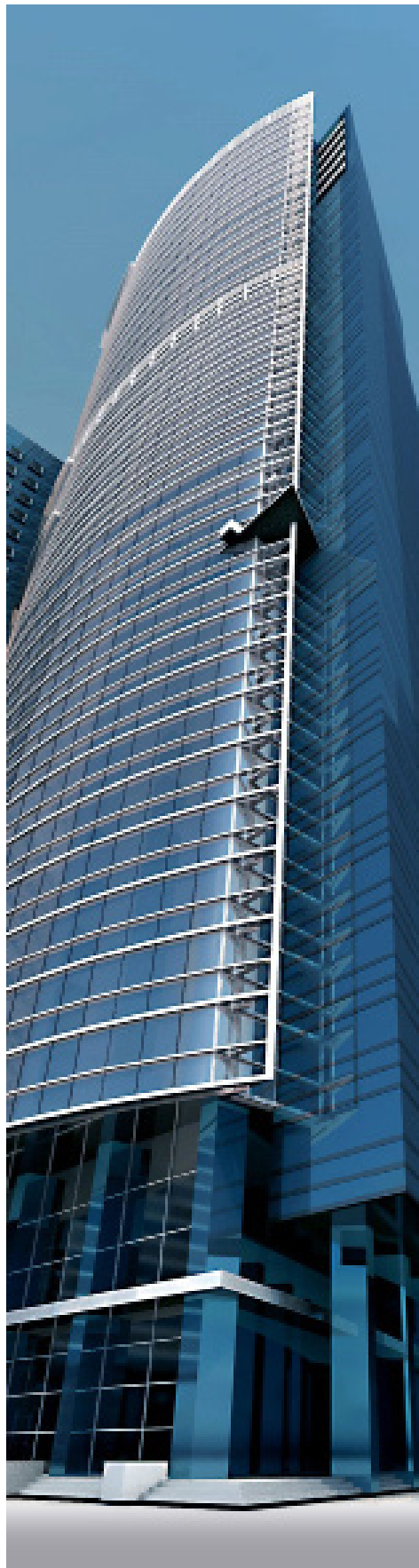
The outlook for the Phoenix Office Market is largely positive for tenants competing for limited space and investors chasing yield should continue to find rewarding targets. However, the long period of national growth following the recovery is slowing. Most economists agree that the next downturn will not be as harsh or prolonged as the previous one, and the local market is not as overbuilt as it was on the eve of the last downturn.

## New Construction

The Tempe submarket remains the star construction activity player, however, Downtown has several very large, competitive projects in the works. The submarket has not ranked as highly in recent years for rent growth, but new product may attract tenants otherwise drawn to the East Valley.

A number of projects delivered in the third quarter are speculative space,





### New Construction (cont.)

including 345,000 sf at The Grand at Papago Park Phase II completed in September. Of the Valley's 32 properties totaling 2.6 msf currently under construction, 49% is preleased.



Wexford Science & Technology

***Universities, tech industries and local governments are collaborating to create innovative business ecosystems.***

ASU continues to grow its presence beyond Tempe. Wexford Science & Technology, the first piece of a 7-acre downtown biomedical campus, will add 227,000 sf. Completion is scheduled for the end of next year. Half of the building will be leased to private firms. The project is an ambitious collaboration with the city that will eventually encompass 30 acres.

### Investment Sales

Class A product attracted most of the quarter's investment dollars, however, class B offices accounted for the majority of transactions as investors chased value-add deals. The Tempe Submarket reaped the largest amount of transaction volume in the third quarter clocking in at \$124.7 billion; although two of the three largest deals occurred in the city's northern sectors.

The iconic US Bank Center plus a nearby parking structure downtown at 101 N. First Avenue traded in August for \$92.8 million. The prior month, NGP V Fund purchased the 210,202 sf GSA Phoenix Professional Office Building near Deer Valley Airport for the FBI Regional Headquarters at an impressive \$439 psf in a deal that registered \$92.3 million making it the largest single building sale, as well as highest dollar per square foot ranking for the quarter.



FBI Regional Headquarters

The 4-building Waypoint Campus in Mesa sold as a portfolio to Innovatus Capital Partners in August for \$107.7 million. Situated in the Riverview District, it benefits from a convenient location near the junctions of Loop 101 and 202 Freeways, one of the busiest crossroads in the Valley.



Waypoint Campus

## Market By The Numbers\*

Submarket	Total RBA (SF)	Vacant Space Direct	Available Space Sublease	Submarket Vacancy	Absorption Class A	Absorption Class B	Q3 Net Absorption (SF)	YTD Net Absorption	Avg. Ask Class A (FS)	Avg. Ask Class B (FS)
44th St Corridor	2,563,266	372,048	4,173	15.2%	17,814	3,469	20,461	14,085	\$27.54	\$25.54
Airport Area	7,699,060	1,129,689	148,027	16.6%	92,640	14,451	107,091	291,190	\$26.34	\$21.83
Arrowhead/Loop 303/ Surprise	804,170	104,464	3,677	13.4%	1,950	(19,847)	(17,897)	(29,812)	\$26.00	\$24.79
Camelback Corridor	7,226,815	1,217,205	93,773	18.1%	54,353	(33,565)	20,788	(15,135)	\$37.10	\$26.45
Central Scottsdale	5,299,511	554,726	33,227	11.1%	(50,768)	30,149	(21,765)	31,339	\$30.35	\$26.95
Chandler/Gilbert	6,089,094	1,034,115	10,929	17.2%	153,523	(12,569)	140,854	365,673	\$29.01	\$23.58
Downtown	7,706,546	825,876	110,203	12.1%	(23,273)	(6,363)	(29,636)	(82,740)	\$32.94	\$29.59
Gateway Airport/ Loop 202	267,319	44,445	5,164	18.6%	-	2,731	2,731	(25,146)	-	\$26.46
Glendale	1,316,542	83,569	0	6.3%	0	14,761	14,761	22,025	\$26.09	\$24.50
Mesa	819,440	36,888	0	4.5%	-	(6,767)	(5,695)	(28,461)	-	\$18.33
Midtown	9,036,663	1,826,330	29,109	20.5%	78,435	100,528	236,383	155,781	\$25.92	\$20.99
Midtown/Central Phoenix	1,483,805	172,164	0	11.6%	-	(8,084)	19,007	34,635	-	\$19.48
N Scottsdale/Carefree	412,548	78,464	0	19.0%	-	8,346	8,346	20,741	-	\$26.97
North I-17/Deer Valley/ Airport	6,801,597	735,717	7,578	10.9%	4,328	2,598	6,926	(228,311)	\$26.14	\$23.90
NW Phoenix	5,180,345	1,233,606	31,118	24.4%	71,708	(43,048)	23,995	(105,086)	\$23.37	\$18.99
Paradise Valley	1,969,455	183,293	13,649	10.0%	48,020	(8,668)	48,132	136,094	\$28.83	\$22.73
Piestewa Peak Corridor	1,767,715	333,450	2,378	19.0%	113	(13,932)	(13,819)	26,374	\$26.88	\$24.48
Pinal County	76,810	0	0	0.0%	-	0	0	0	-	-
Scottsdale Airpark	8,972,862	1,129,837	88,929	13.6%	97,561	58,015	154,815	116,905	\$31.09	\$27.58
Scottsdale South	3,901,012	368,294	8,838	9.7%	34,346	5,279	39,547	183,693	\$34.22	\$31.17
South Tempe/Ahwatukee	5,272,744	712,090	16,189	13.8%	4,289	30,435	34,724	199,495	\$32.20	\$23.91
Southwest Phoenix/ Outlying	812,116	173,512	0	21.4%	0	0	0	0	\$28.87	\$26.86
Superstition Corridor	2,580,780	190,502	1,555	7.4%	3,547	4,156	7,703	70,006	\$25.04	\$20.40
Tempe	9,876,558	839,270	13,346	8.6%	66,753	(3,078)	63,475	405,078	\$38.99	\$24.64
West I-10	430,724	44,765	1,787	10.8%	(1,787)	2,499	712	(1,450)	\$26.93	\$25.33
<b>Total</b>	<b>98,367,497</b>	<b>13,424,319</b>	<b>623,649</b>	<b>14.3%</b>	<b>653,552</b>	<b>121,496</b>	<b>861,639</b>	<b>1,556,973</b>	<b>\$30.89</b>	<b>\$23.68</b>

\*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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