U.S. office market report

Q4 2022

AVISON YOUNG

U.S. office market trends

42.1%

return-to-office rates, 2022 relative to 2019

Office employers continue to embrace hybrid work schedules as they navigate their future workplace strategies and competitive labor market conditions.

Our take on this trend...

Low return-to-office rates through mid-December 2022 have not meaningfully changed since Labor Day, inhibiting office demand. Weakening economic conditions could incentivize stronger office returns, incrementally increasing demand in 2023.

-58.8%

change in office job postings, November to December 2022

Greater prospects of a financial economic recession caused a severe and sudden pullback in office job postings, a leading indicator of office demand.

Our take on this trend...

Banking, law, media and tech companies significantly reduced their number of job openings in recent months, while layoffs in the tech sector spiked in November 2022. Workforce reductions would negatively impact office demand in the coming months.

2.0%

unemployment rate for bachelor's degree holders

Backward-looking economic indicators, namely unemployment rates and total jobs, remained strong by historical measures.

Our take on this trend...

The office economy had been on strong footing, though terminations in November and December are expected to weaken those indicators. The at-risk tech sector accounts for 9.4% of total office employment, limiting those disruptions on the broader office market.

U.S. office market trends

27.9%

total availability rate for 1980s Class A assets

These assets do not compete with older properties on pricing and newer properties on sustainability, amenities or efficiencies, causing heightened availability rates.

Our take on this trend...

Landlords holding these weaker-performing assets should investigate opportunities to inject capital to make them more competitive or convert them to alternative uses.

+41.7%

rent premium for offices with tenant lounges

Tenant lounges and conference centers are in demand, with occupiers vying to incentivize their workforce to return to the office and decrease their real estate overhead costs.

Our take on this trend...

Installing high-value office amenities can reinvigorate the leasing momentum for properties with vacancy risk, a necessary proposition for landlords overseeing older office portfolios.

+109bp

quarter-over-quarter change in office cap rates

Spiking risk-free rates, +215bp year-to-date, expectantly applied upward pressure on office cap rates in Q4 2022.

Our take on this trend...

Office fundamental headwinds are also expected to continue to apply downward pressure on values. Patient investors can capitalize on these conditions, especially if spreads widen to more attractive levels.

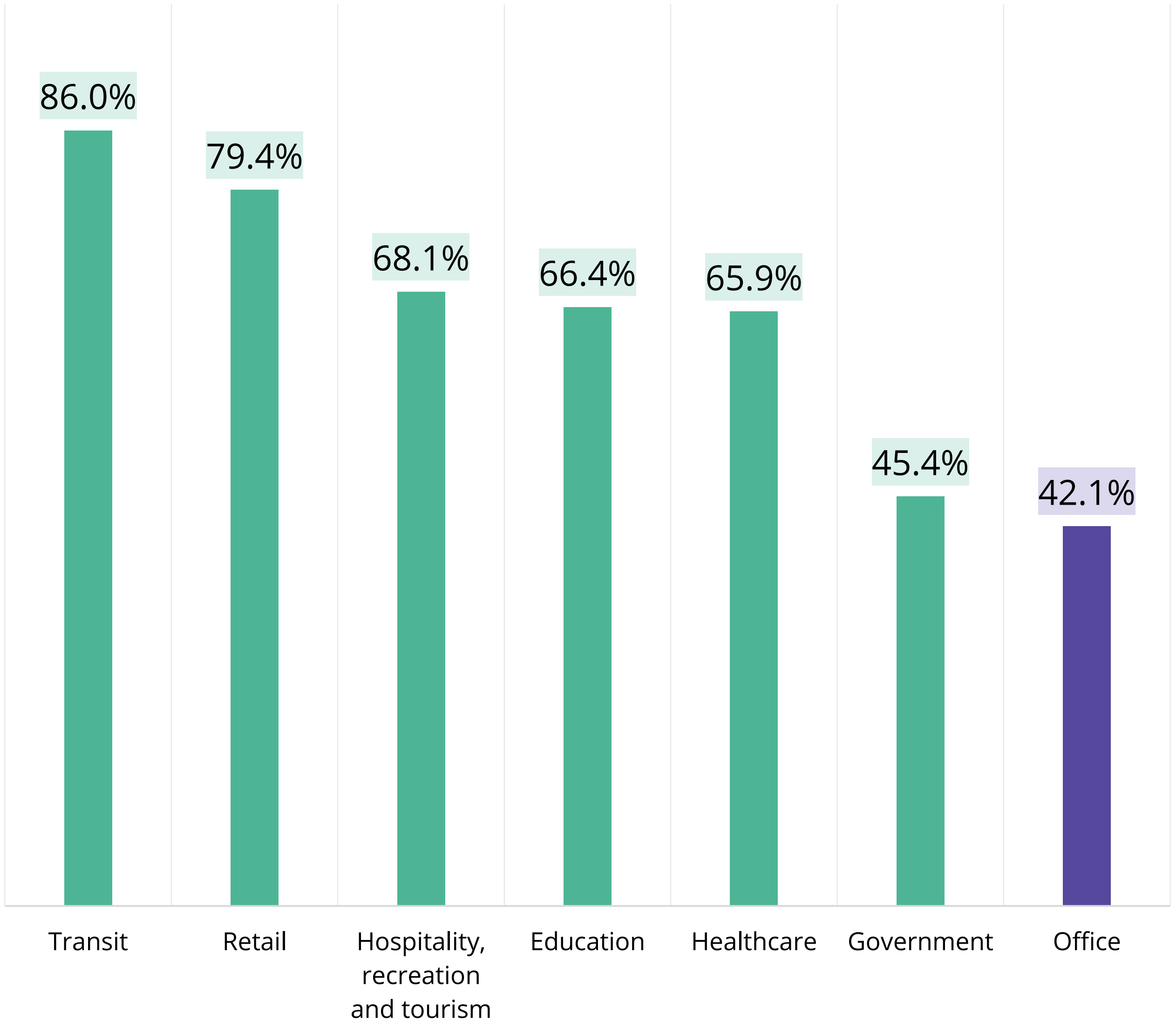
Visitor volumes by property type

42.1%

office visitor volumes, week of December 12, 2022 relative to week of December 9, 2019.

People have returned to mass transit stations—airports are back to normal with visitation at 92.5% of pre-pandemic levels—retail and other areas of interest, though public and private offices remain sparsely populated.

The Vitality Index



Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

Office visitor volumes relative to 2019

Return-to-office efforts remained considerably lower than pre-COVID levels as long-term workplace strategies continued to evolve. Office visitation is up just 3.1% since the week after Labor Day 2022.

19.5%

2020 relative to 2019, when governmental regulations partly prohibited return-to-office efforts.

35.4%

2021 relative to 2019, when return-to-office rates were inhibited by the onset of the Delta variant.

42.1%

2022 relative to 2019, with companies continuing to navigate workplace solutions during the next normal.

Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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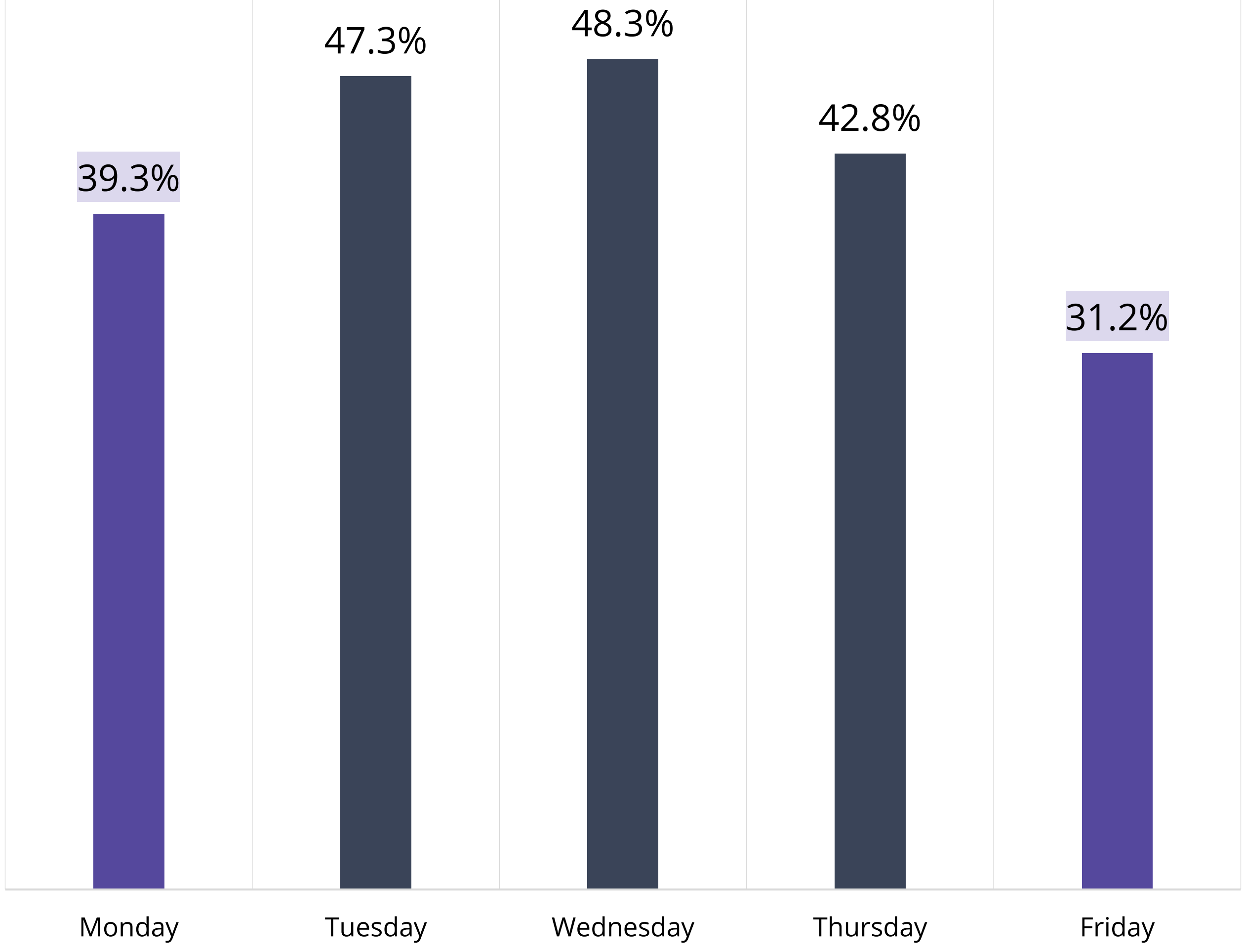
Office visitor volumes by weekday

35.4%

Mondays/Fridays visitation, week of December 12, 2022 relative to week of December 9, 2019.

Hybrid work remains prevalent, with most office workers working from home on Mondays and Fridays. Office visitation at representative tech corporations is 28.1% of 2019 levels on Mondays and 23.8% of 2019 levels on Fridays.

The Vitality Index



Note: Representative office locations
Source: Orbital Insight, AVANT by Avison Young

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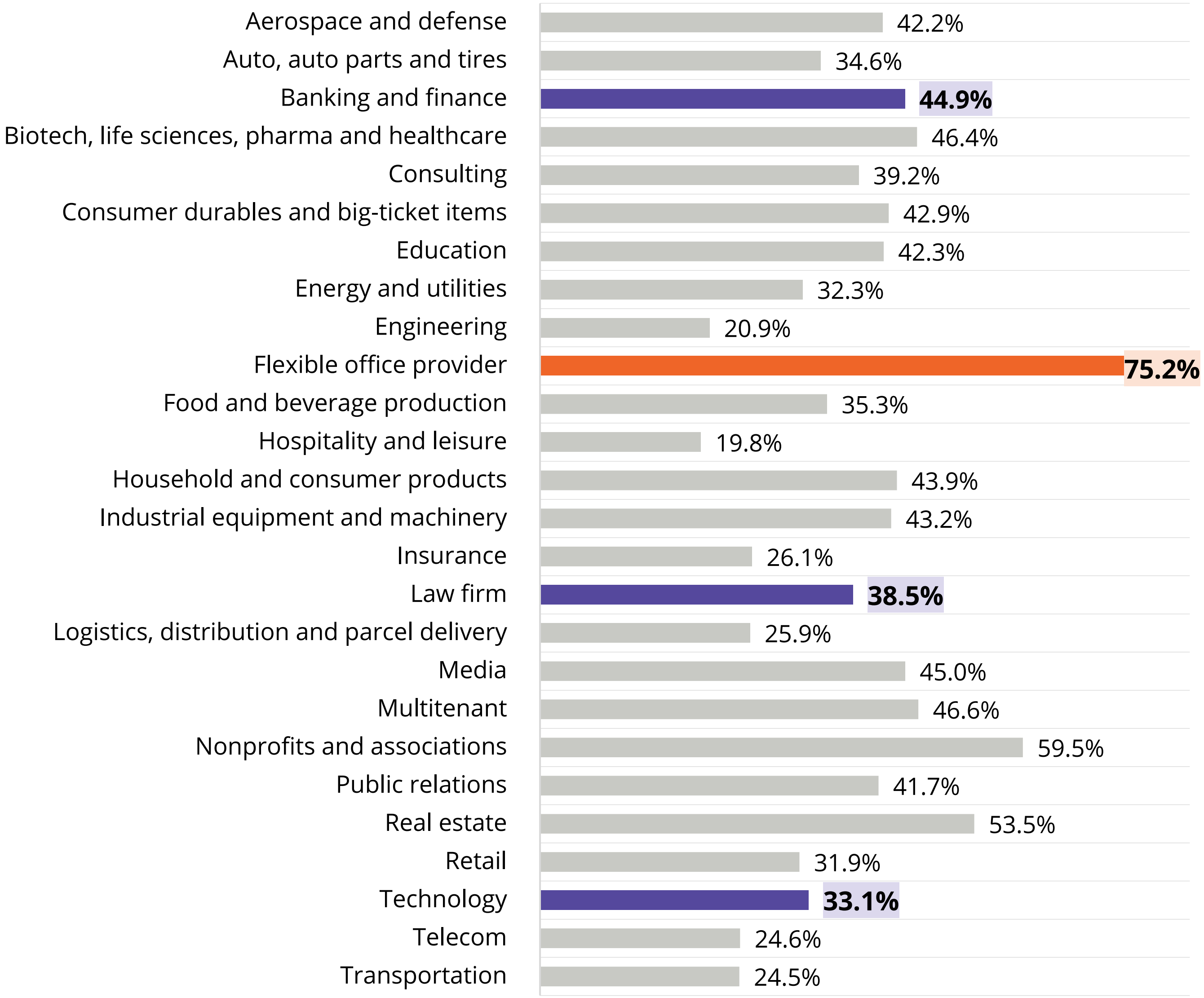
Return-to-work rates by office industry

75.2%

visitation at flexible offices, week of December 12, 2022 relative to week of December 15, 2019.

Flexible office providers have provided a placemaking outlet for office occupiers that are still navigating their workplace strategies, enabling these locations to post consistently superior office visitor volumes throughout the pandemic.

The Vitality Index



Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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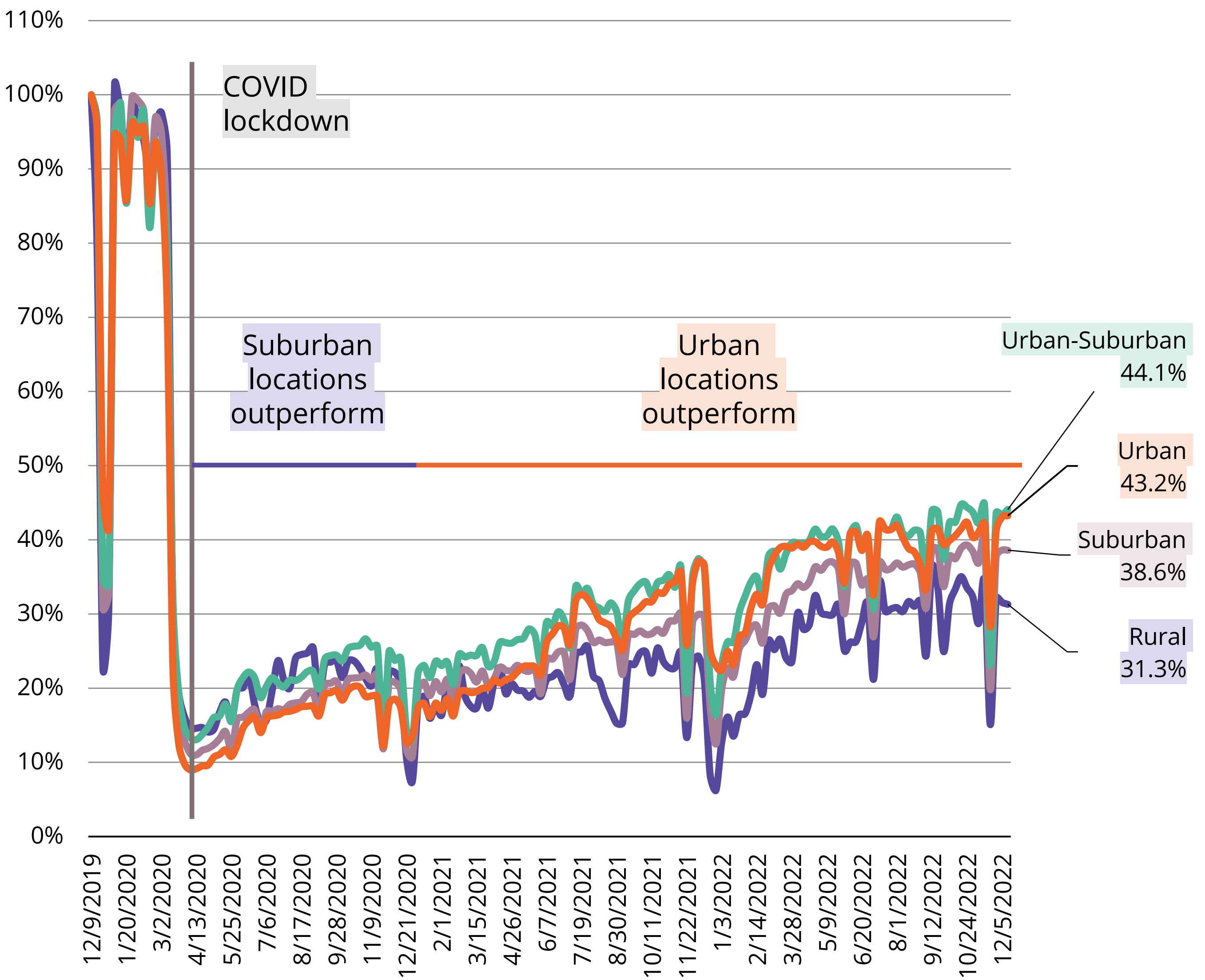
Office visitation by type of location

43.3%

office visitation at urban and urban-suburban locations, 2022 relative to 2019.

Suburban offices reported stronger visitation relative to urban offices in the immediate aftermath of the pandemic, with office workers dispersed and virus-related concerns elevated. However, offices located in cities have reported consistently superior visitor volumes since 2021.

View dashboard



Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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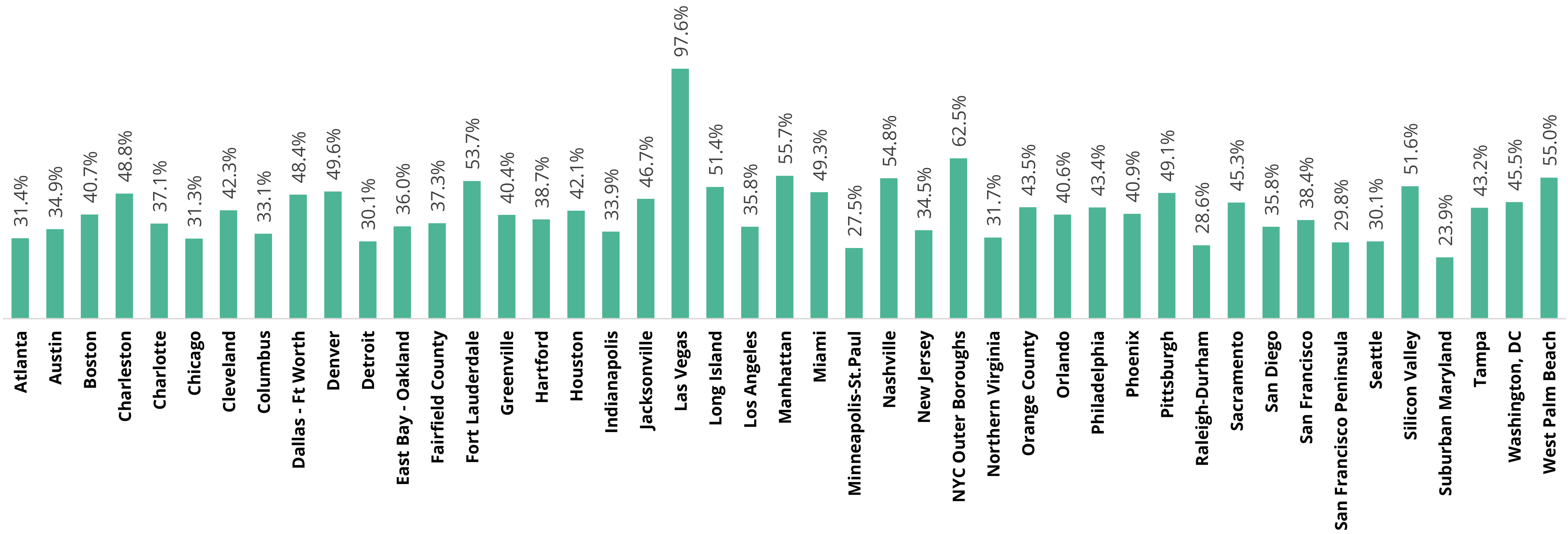
Return-to-office by market

42.1% U.S. week of December 12, 2022 relative to week of December 9, 2019.



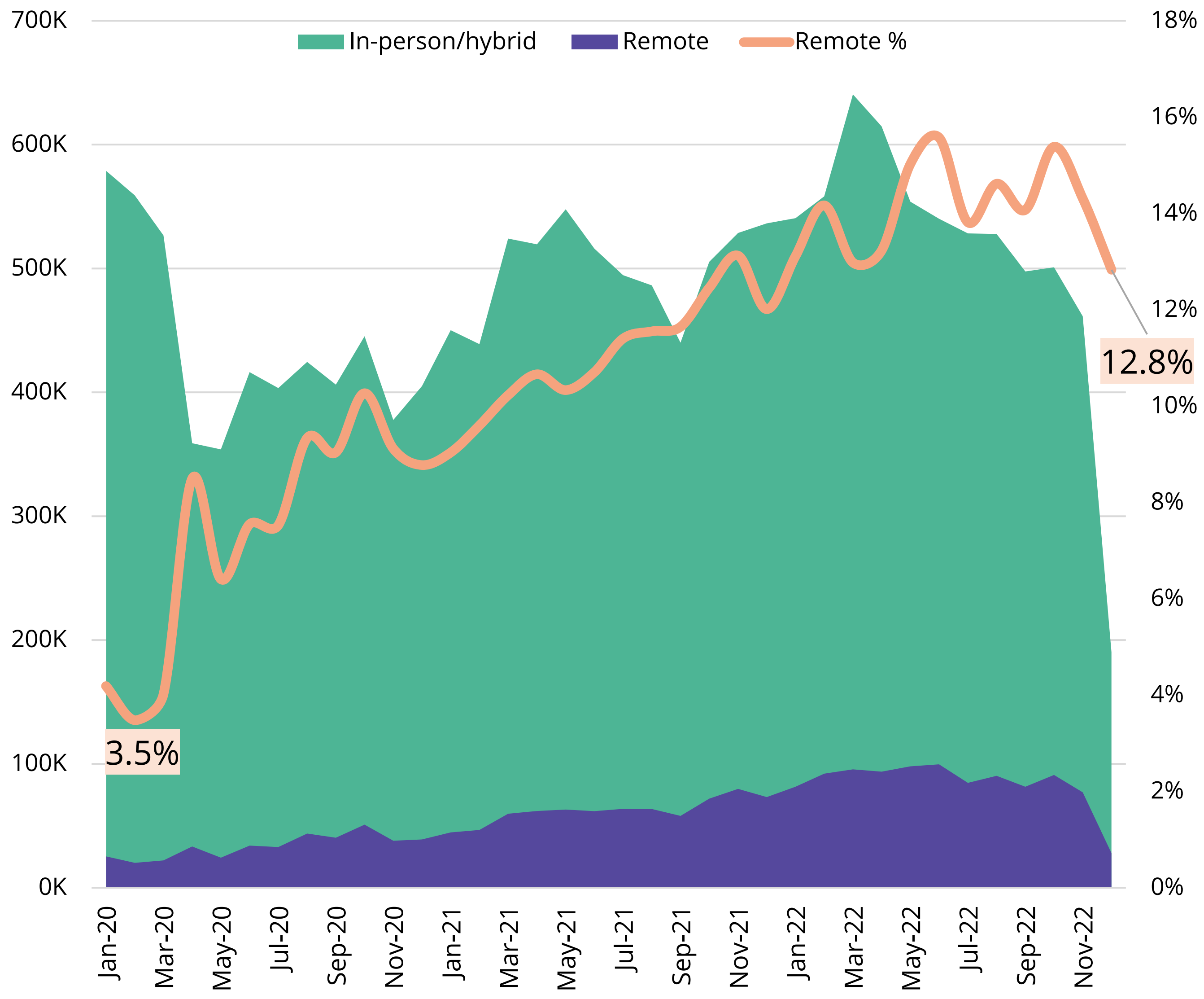
Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

In-person and remote job postings

-58.8%

November to December 2022 change in in-person/hybrid office job postings.

The greater prospects of a financial economic recession caused a severe pullback in office job postings. The decline in job postings is a leading indicator of continued office fundamental distress, accentuated by the still-heightened proportionate share of remote job postings of 12.8%.



Note: Includes administrative, finance and insurance, information, management, professional scientific and technical services and real estate industries
Source: Emsi, AVANT by Avison Young

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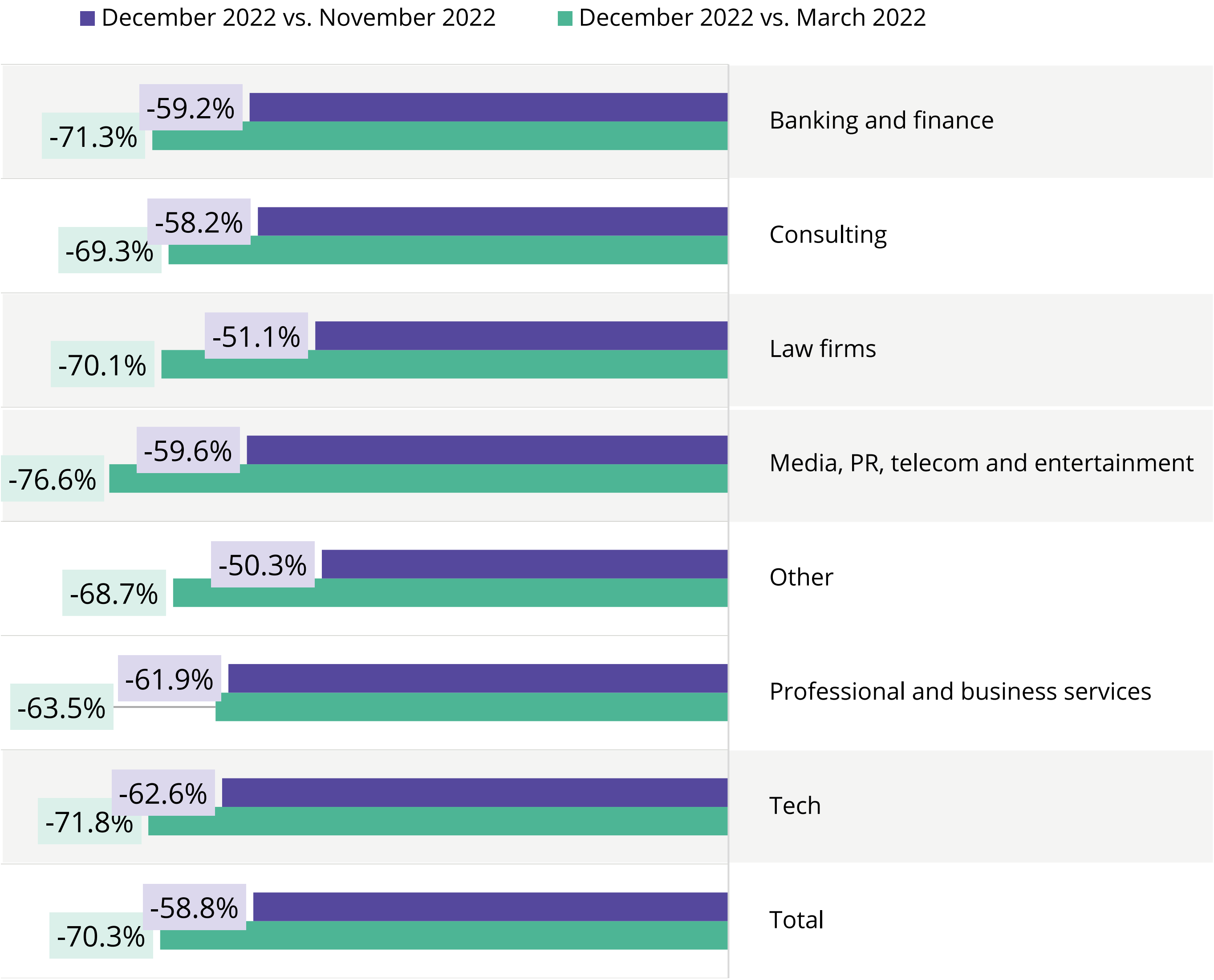
In-person/hybrid office job postings by sector

-71.8%

change in tech job postings, December 2022 vs. March 2022.

All major office-using job sectors have been affected by mounting economic headwinds, though the tech sector has been especially impacted. Tech job postings declined by 62.6% from November 2022 to December 2022 and by 71.8% from the post-COVID job postings peak in March 2022 to December 2022.



Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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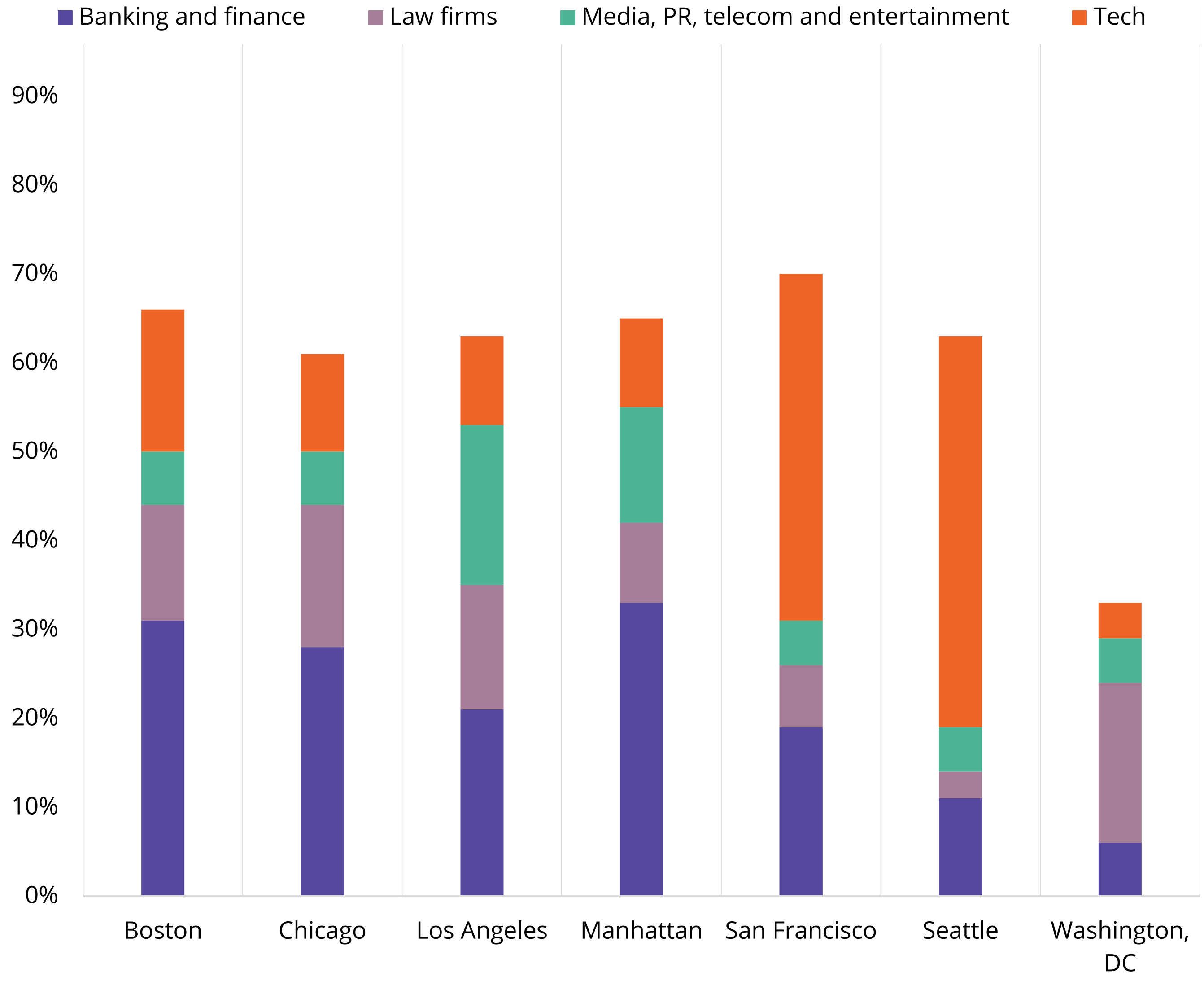
Exposure to at-risk industries

60.0%

average gateway market exposure to industries with greatest month-over-month job postings declines.

Banking and finance companies had been resilient to pandemic-related economic difficulties, though recent layoff announcements and job postings declines could begin to more meaningfully affect office demand in this sector. Media, PR, telecom, entertainment, law firms and tech sectors have also experienced severe downturns in job postings in recent months.



Note: Central business districts only. Represents active leases.
Source: AVANT by Avison Young

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At-risk industries vs. change in availabilities

+9.8 pp

change in post-COVID availability rates, markets with 60.0%+ exposure to at-risk industries.

The temporary pause in demand due to rising economic headwinds and evolving post-COVID workplace strategies have caused total availability rates, including direct and sublet spaces, to rise in gateway office markets. Supply increases have been especially pronounced in San Francisco, which capitalized on robust expansionary tech demand in the prior growth cycle but has encountered a significant fundamental reversion since 2020.

Note: Central business districts only. Availability rate includes direct and sublet spaces.
Source: AVANT by Avison Young, CoStar

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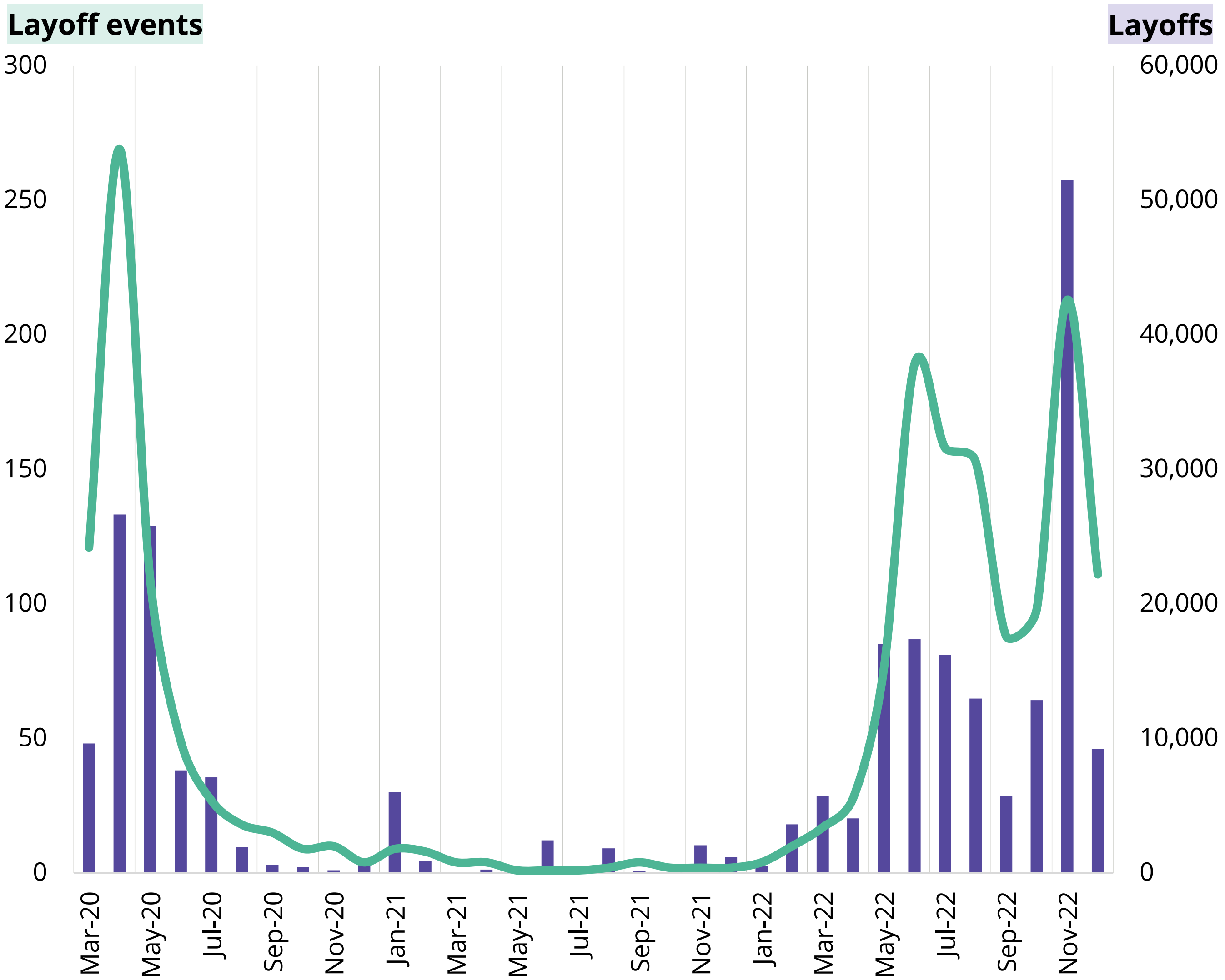
Tech sector layoffs

60.7K

tech layoffs from November to December 2022, accounting for 24.0% of post-COVID terminations.

Layoffs in the tech sector spiked in November 2022, a swift reaction to equity market disruption caused by growing economic strains. Market segments with outsized exposure to tech may encounter new sublet additions and weaker demand attributable to this sector.



Source: Layoffs.fyi

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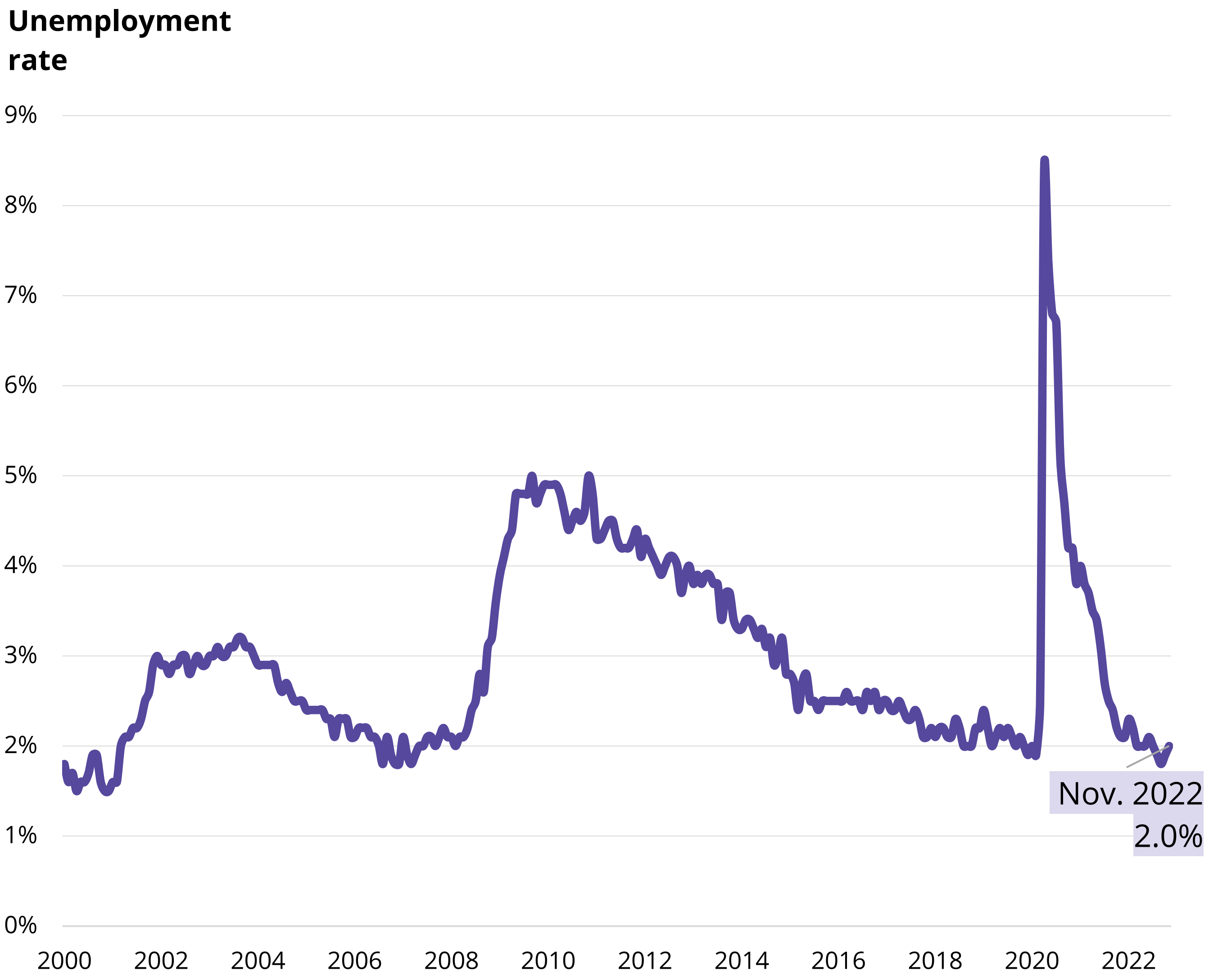
Bachelor's degree unemployment rate

2.0%

unemployment rate for bachelor's degree holders, lower than the 2000-to-present average of 3.0%.

Backward-looking economic measures such as unemployment rates and total jobs, which are strong relative to historical levels, do not reflect the layoffs and job postings disruptions that were reported in November and December. These alternative economic indicators are expected to negatively impact lagging economic datasets—and property markets—in future months. Still, the office economy had been on strong footing before signs of an economic correction became more prevalent.



Source: BLS

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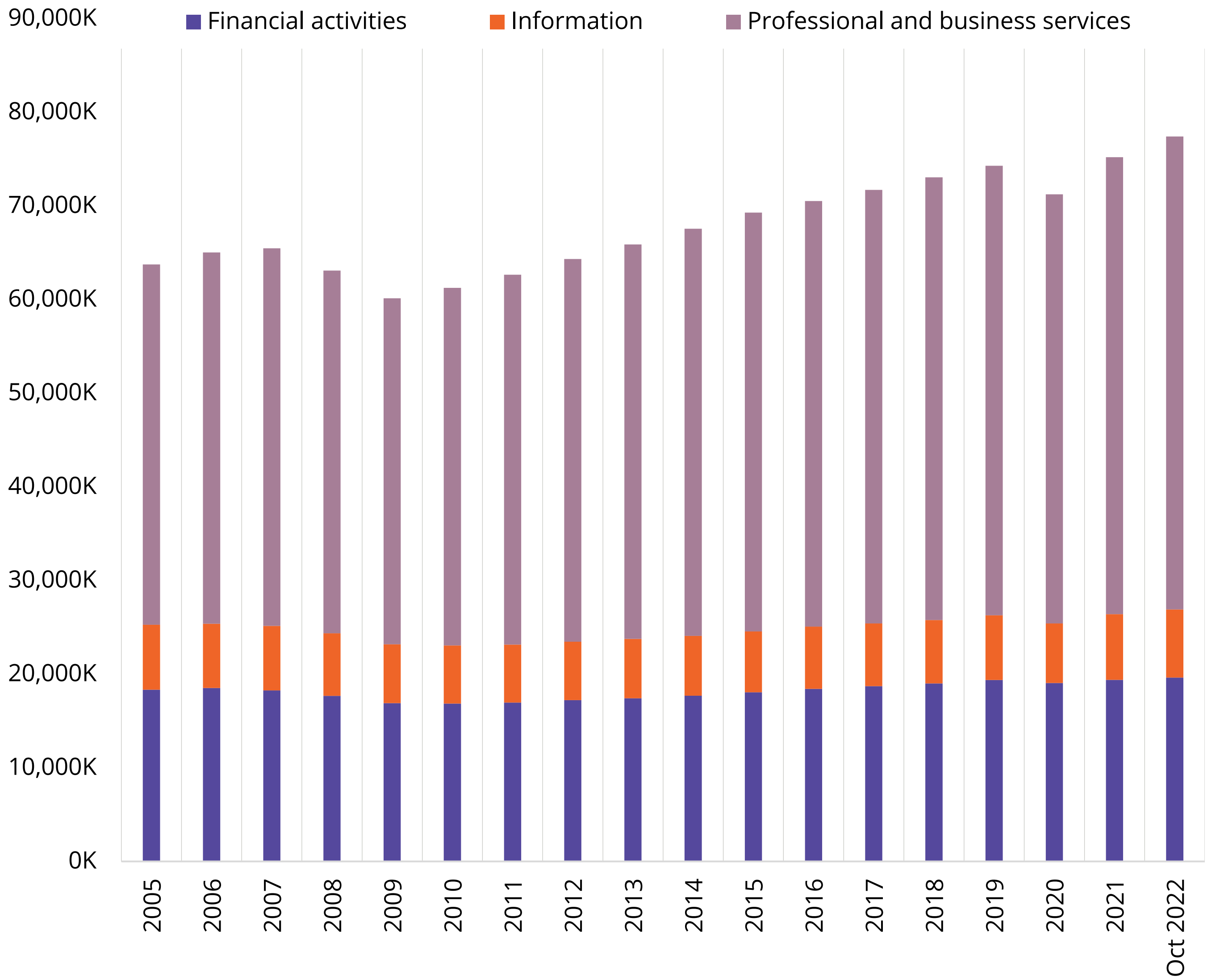
Office employment by industry

9.4%

information, including tech, share of total U.S. office-using employment.

Tech comprises less than 10.0% of total office-using employment in the U.S., emphasizing that future disruptions to this industry should only impact select market segments.

This backward-looking data had trended favorably through October 2022—up 2.9% since year-end 2021 and 4.2% since year-end 2019—though office employment is poised to decline in future months when updated data becomes available.



Source: BLS

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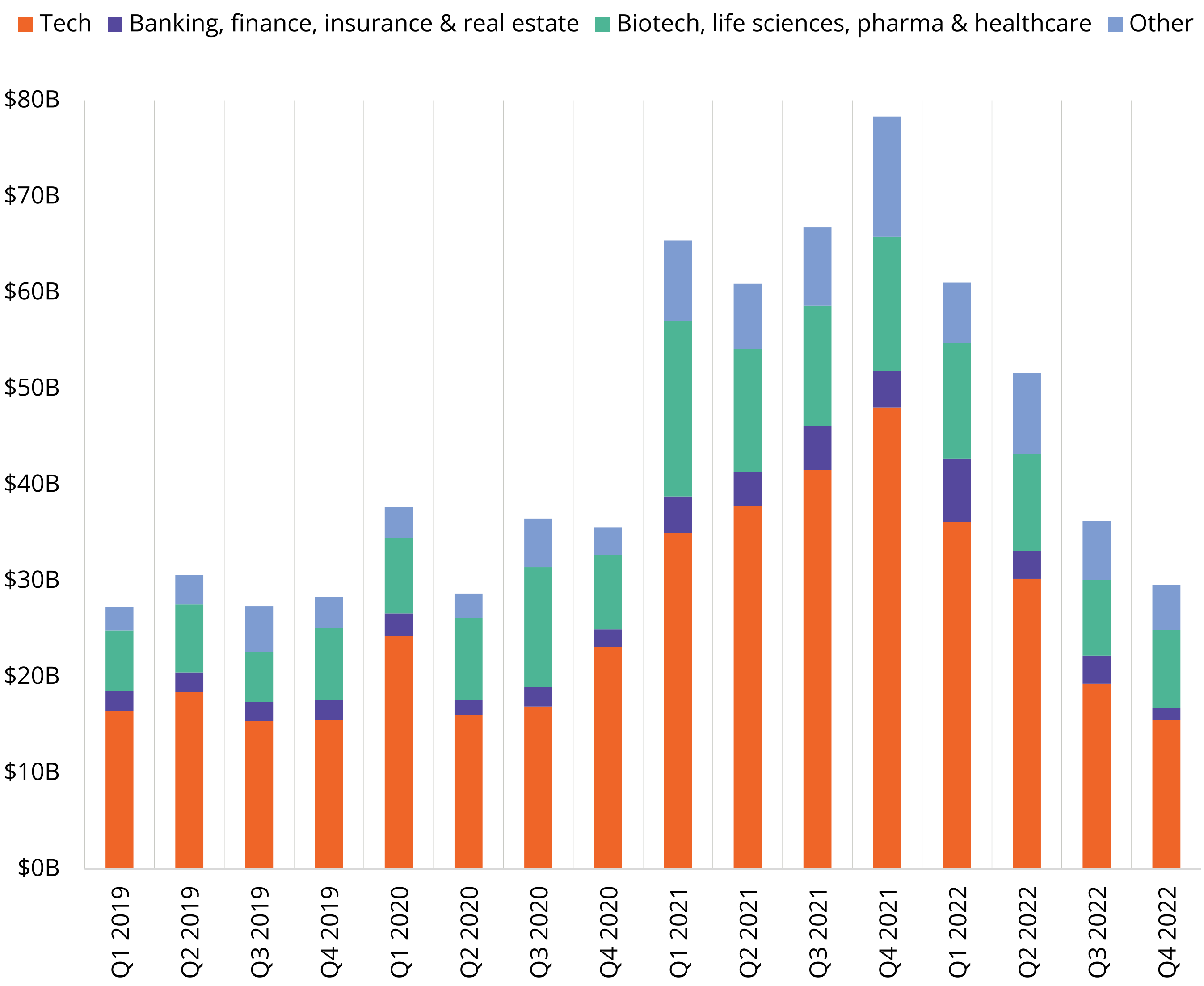
Venture capital funding

-62.2%

year-over-year change in total quarterly venture capital funding.

Venture capital dealmaking dipped to $29.6B in Q4 2020, roughly equating the Q1 2019 to Q2 2020 levels of $30.0B. Investors have been refocusing on profitability during the higher interest rate environment; according to a Q3 2022 Pitchbook report, median equity multiples declined from 17.3x to 5.6x in the past year. Emerging tech companies have been especially impacted, with funding in that sector declining by 67.7% year-over-year to Q3 2019 levels.



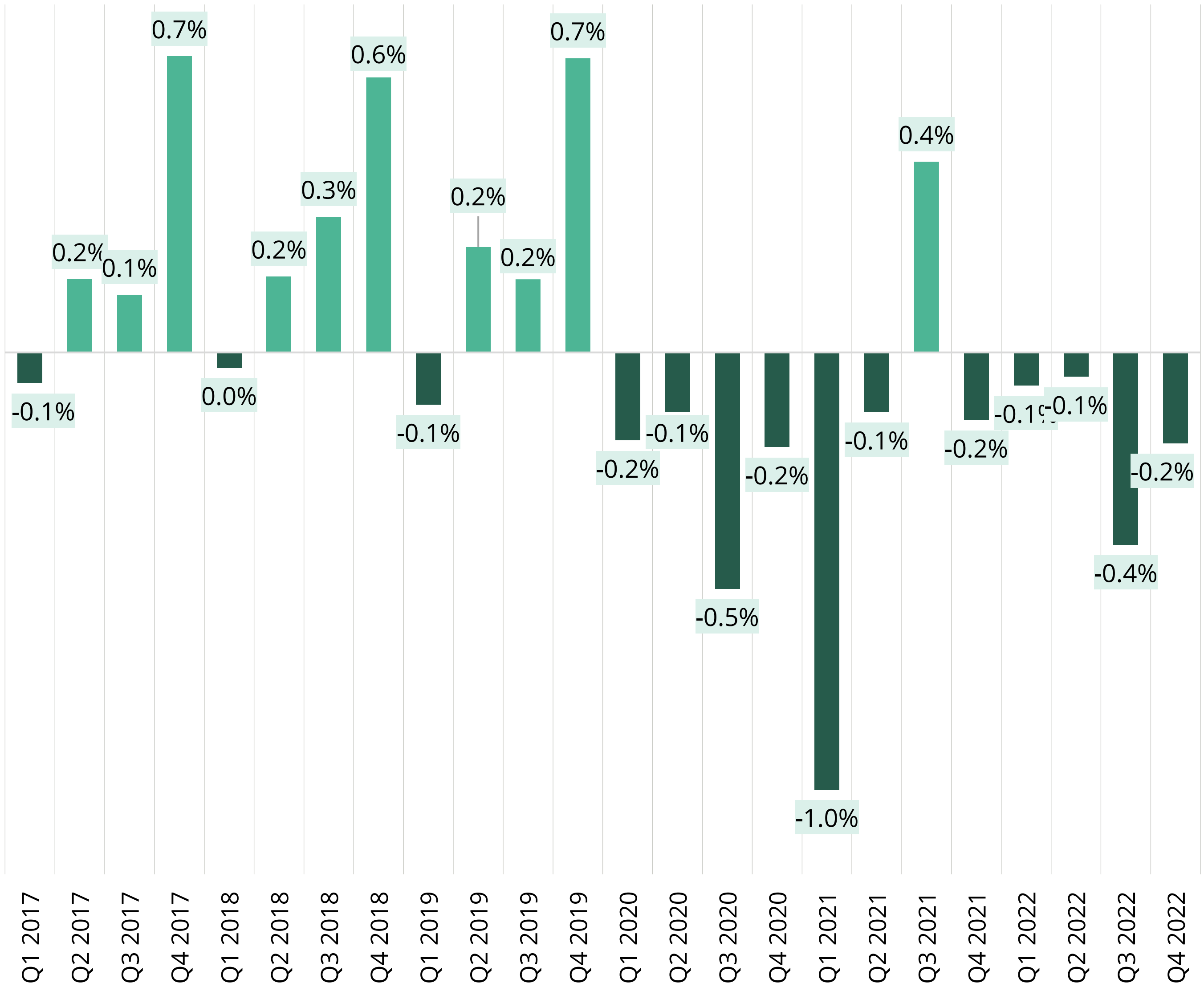
Source: AVANT by Avison Young, Pitchbook

U.S. net absorption as a share of inventory

-2.5%

cumulative net absorption as a percentage of inventory, Q2 2020 to Q4 2022.

Structurally weaker demand has caused net absorption to decline in 11 of the past 12 quarters. Post-COVID losses have nearly offset the gains made from 2017 to Q1 2020 of 2.8% net absorption as a percentage of inventory.



Source: AVANT by Avison Young, CoStar

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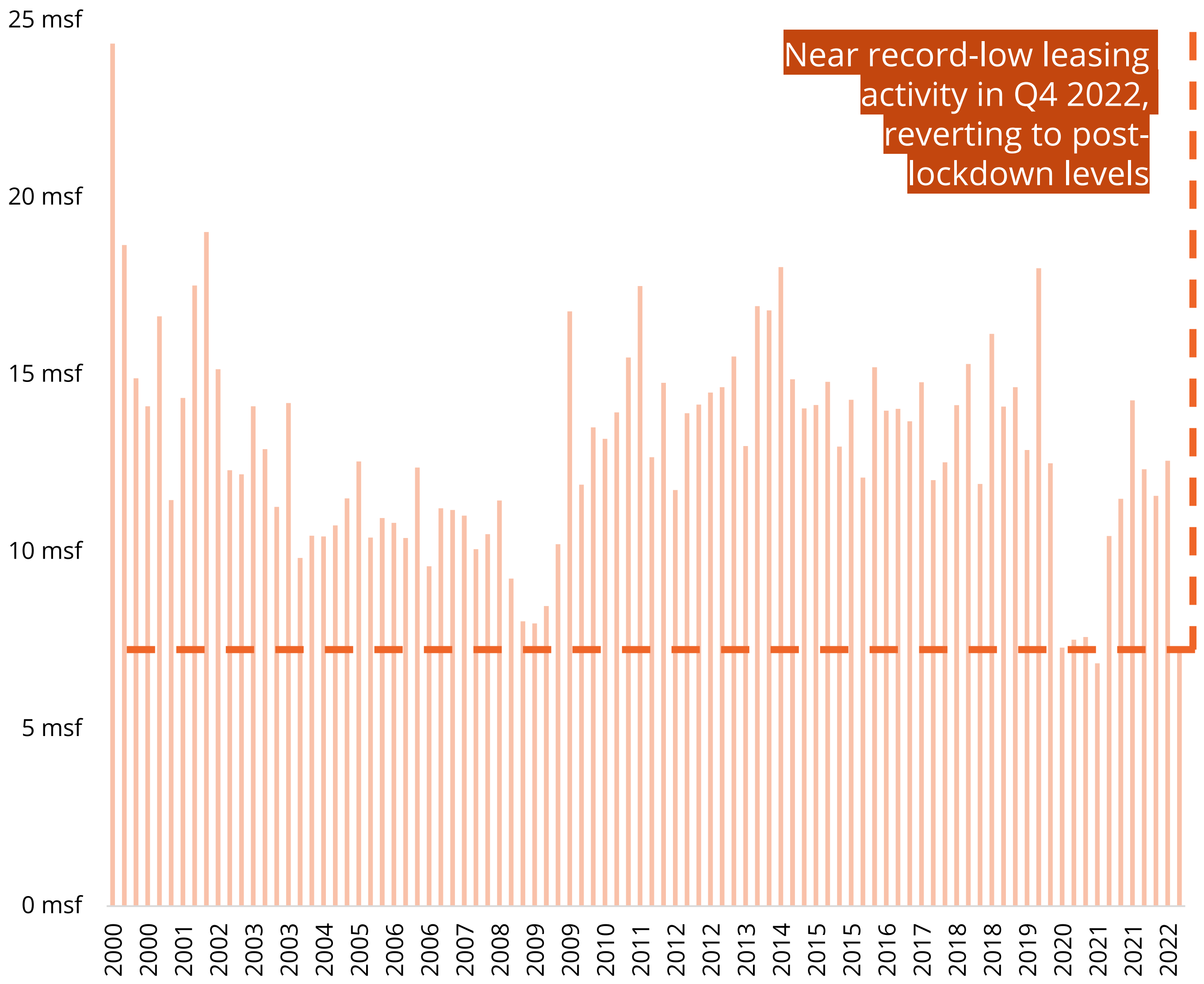
Office market leasing activity

-46.2%

Q4 2022 leasing activity vs. 2000 to 2020 quarterly average, second lowest on record since 2000.

U.S. leasing activity paused in Q4 2022 due to continued workplace strategy uncertainties compounded by mounting economic headwinds. The most recent quarter office deal flow totaled just 7.2 msf, the second weakest activity reported since 2000 and effectually matching the activity of 7.3 msf reported during the immediate aftermath of the pandemic from Q2 2020 to Q1 2021.



Note: All transaction types. Offices that are 20,000 sf or greater.
Source: CoStar

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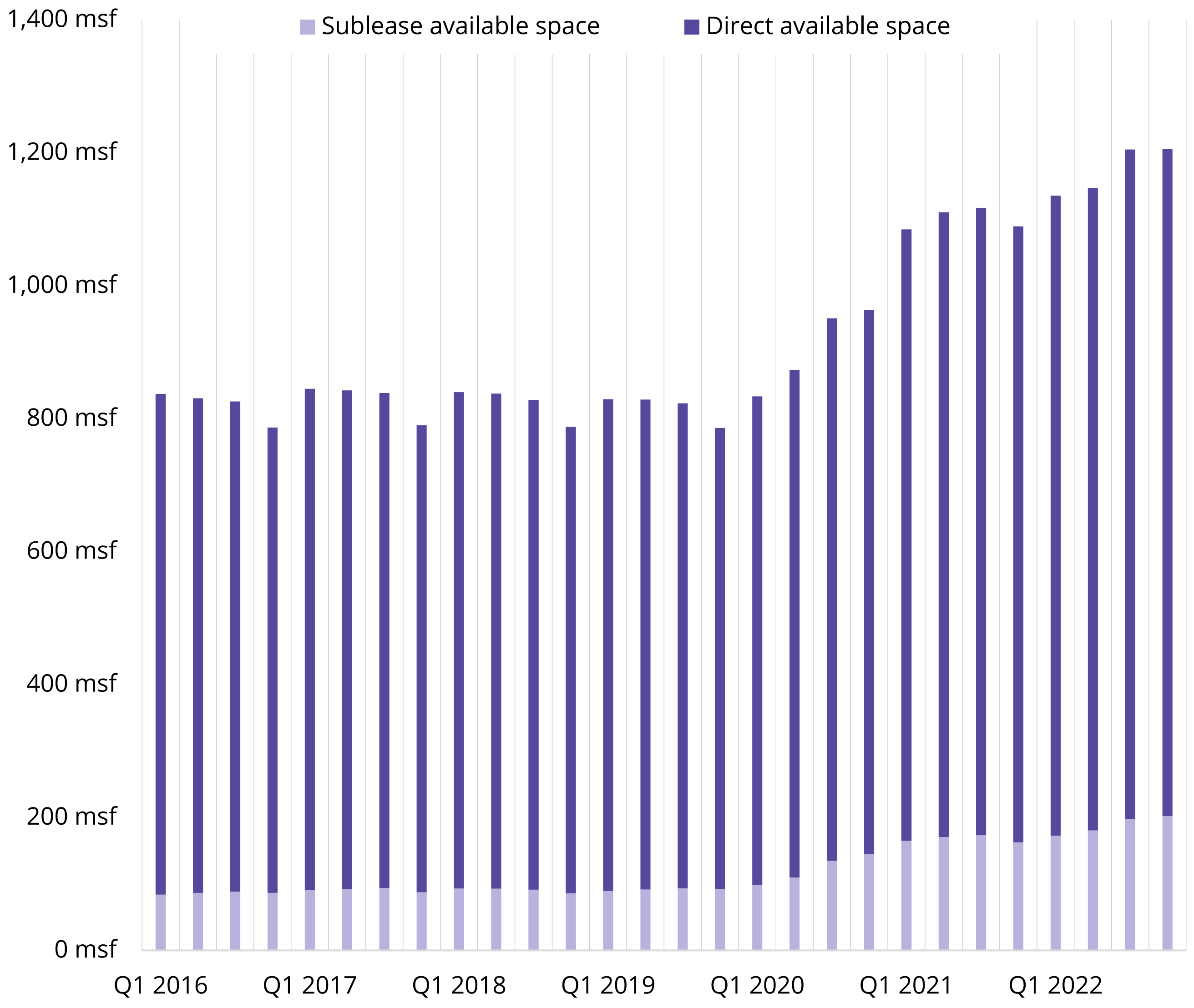
U.S. available space for lease

202.2 msf

total available sublet space, reaching a new post-2016 high.

For reference, the scale of available sublet space in the U.S. is larger than the entirety of the Atlanta (165.3 msf), Chicago CBD (175.1 msf) and Washington, DC (148.7 msf) office markets. Sublease availabilities, particularly from tech companies, are expected to continue to rise as economic conditions are positioned to deteriorate in 2023.



Source: AVANT by Avison Young, CoStar

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Total availability rate by office vintage

27.9%

availability rate for Class A offices developed in the 1980s.

Older vintage assets that cannot compete on pricing, building accommodations nor efficiencies are encountering the greatest challenges in the current environment. Conversely, Trophy offices delivered since 2000 have captured comparatively strong demand as tenants vie to compete for talent and strive to reconfigure and future-proof their workplaces.

Note: Includes direct and sublet spaces
Source: AVANT by Avison Young, CoStar

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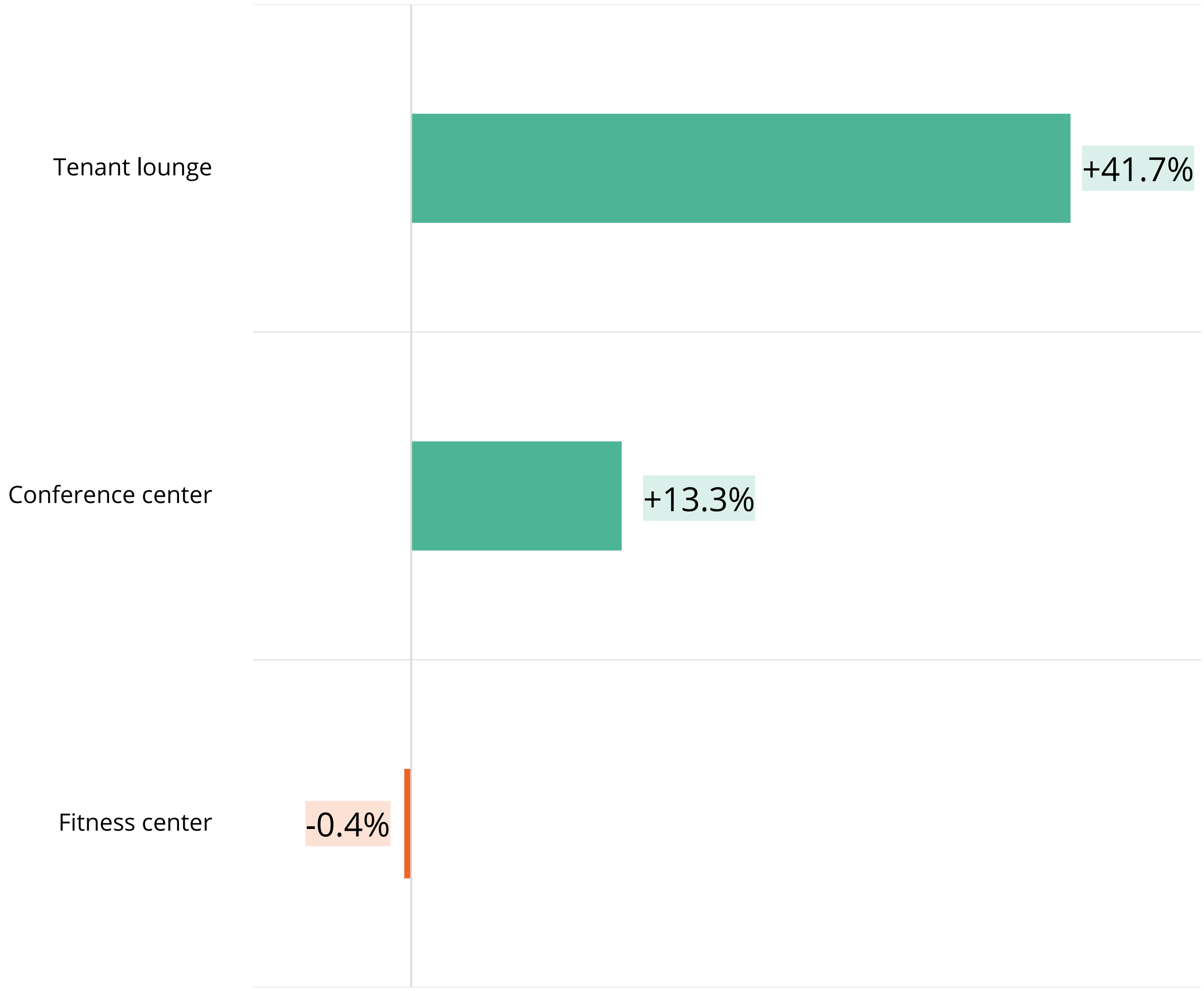
Gateway office rent premium by amenity

+41.7%

base rent premium, offices with tenant lounges vs. offices that do not offer tenant lounges.

Not all office amenities are created equal, with tenants prioritizing office properties that offer tenant lounges and conference centers. Fitness centers, conversely, do not meaningfully influence property rents. (Though this trend may change, depending on peoples' New Year's resolutions.)



Note: Class A and Trophy properties located in Boston, Chicago, Los Angeles, Manhattan, San Francisco and Seattle. Based on executed base rents in the past two years.
Source: Orbital Insight, AVANT by Avison Young

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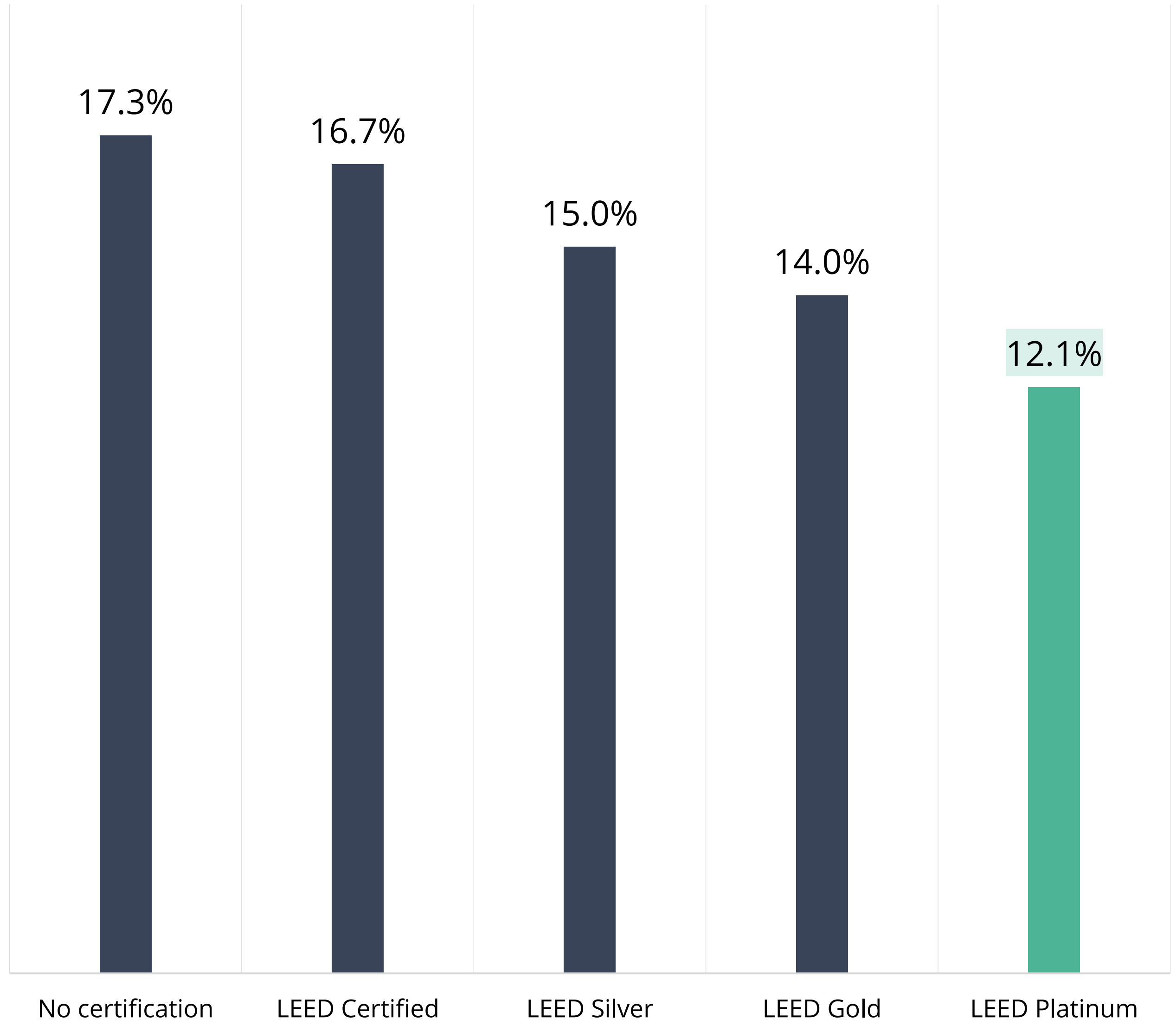
Gateway office vacancy rate by sustainability

12.1%

office vacancy rate for properties with LEED Platinum certification.

Properties that offer better sustainability compliance are capturing stronger tenant interest, as demonstrated by lower vacancy rates for properties offering higher LEED certification levels.



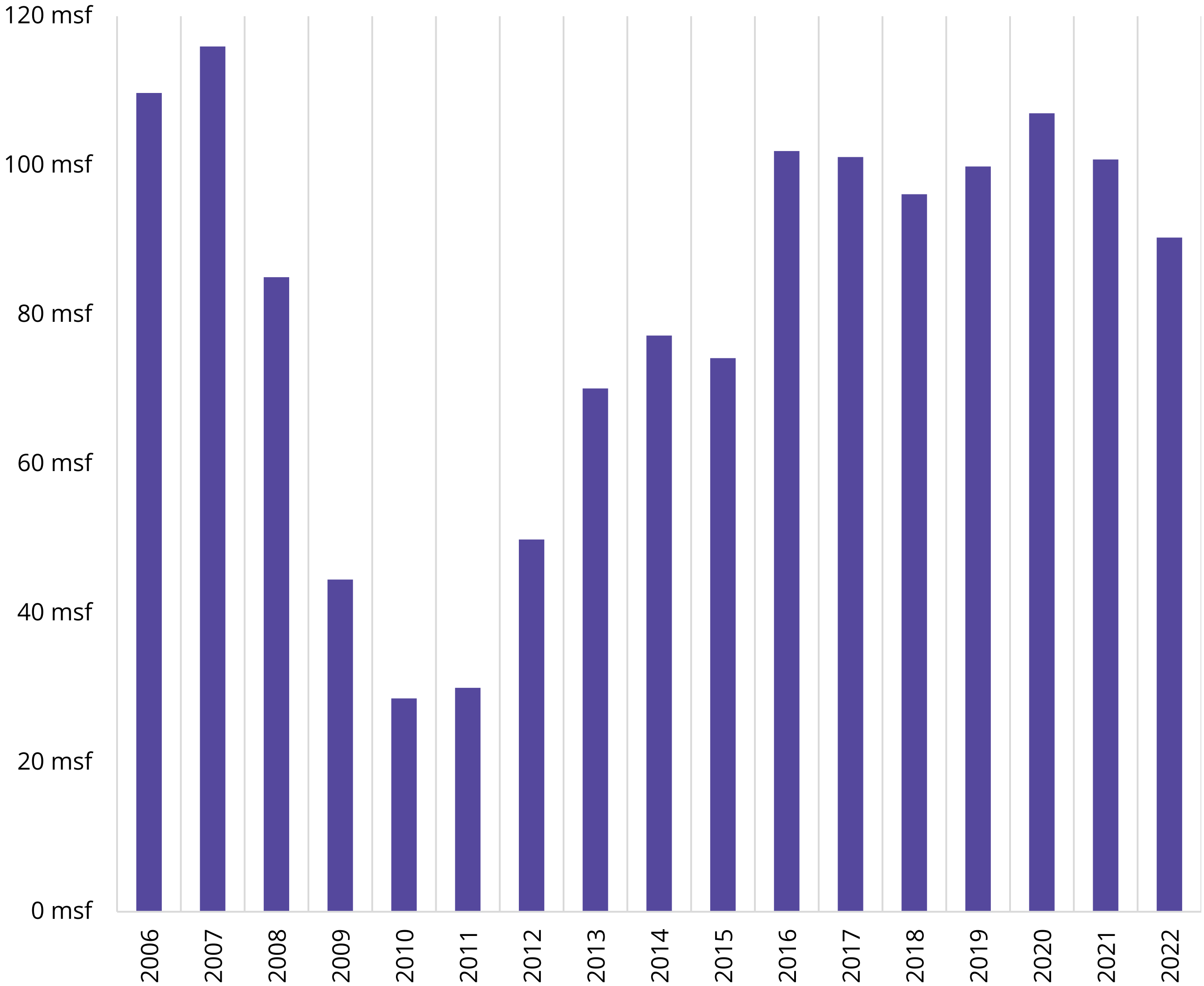
Note: Boston, Chicago, Los Angeles, Manhattan, San Francisco and Seattle. Vacancy rate includes direct and sublet spaces. Source: AVANT by Avison Young, CoStar

Office development activity

90.3 msf

of office properties under construction across the U.S., as of Q4 2022.

Outperformance by amenity-rich, sustainable, new construction offices could usher continued development activity, albeit with mounting financing difficulties. Construction activity in 2022 nearly matched 2016-to-2021 levels of 101.1 msf.



Source: AVANT by Avison Young

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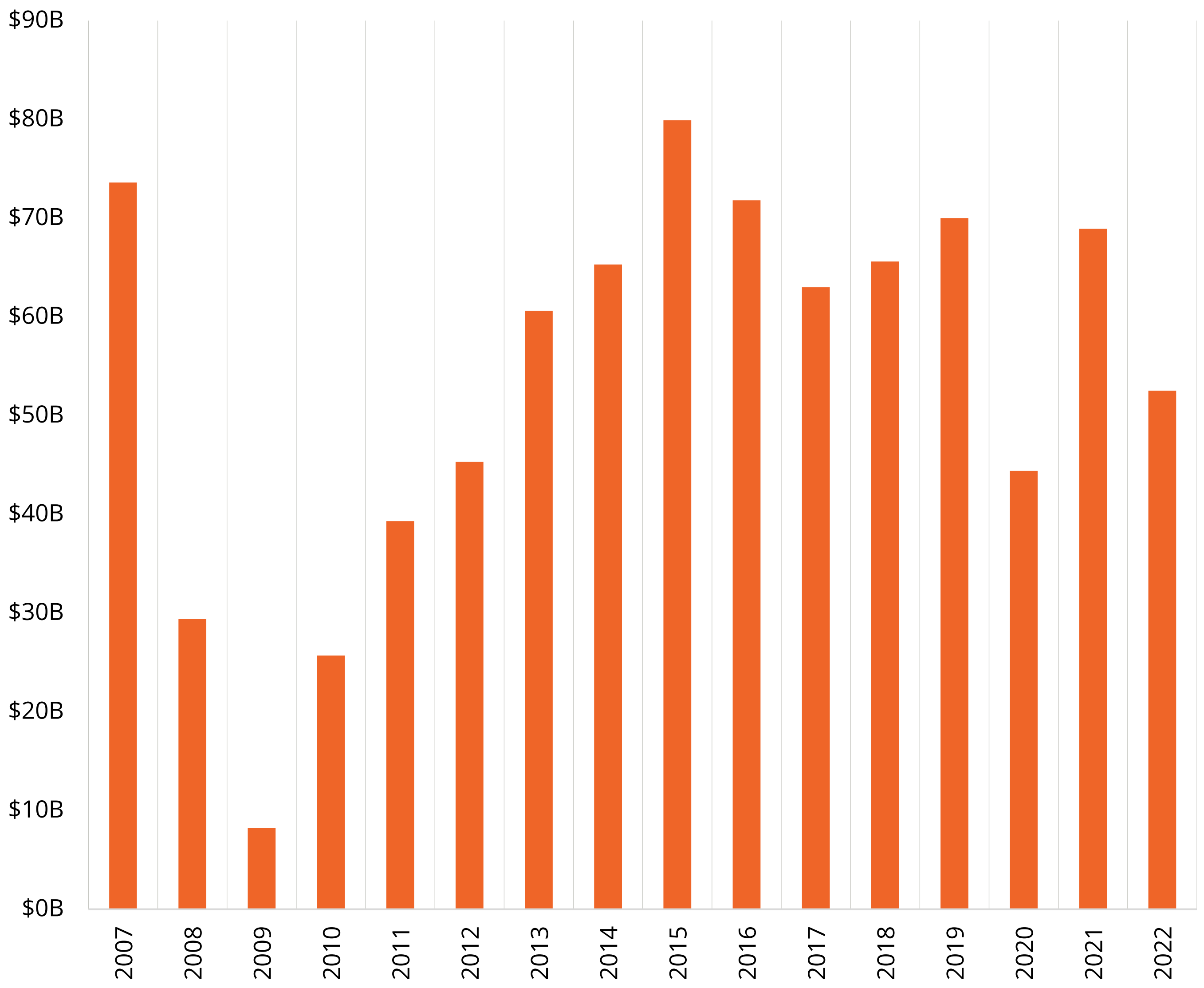
Office investment dollar volume

-23.8%

year-over-year change in U.S. office investment dollar volume.

At $52.5B, 2022 investment activity surpassed 2020 levels of $44.4B but remained below the $63.5B recorded from 2012 to 2021. There is ample uncommitted capital chasing investment opportunities, though investors have increasingly focused on medical office, life sciences and other alternatives due to the prevailing headwinds affecting the office sector. If asset pricing more meaningfully corrects, investors with a long-term view could capitalize and reap attractive risk-adjusted returns.



Source: AVANT by Avison Young, RCA

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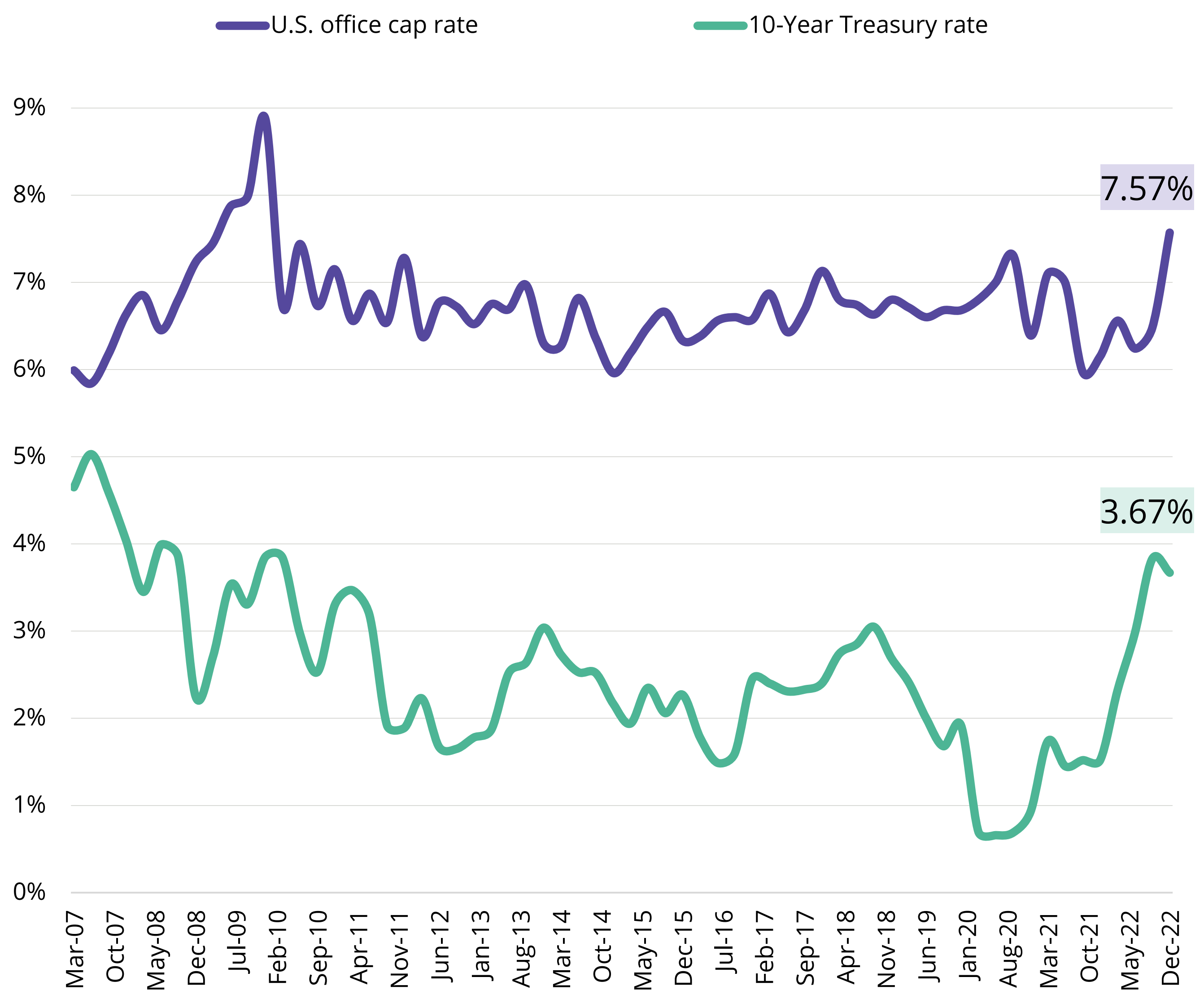
Office cap rates versus benchmark yields

+109bp

quarter-over-quarter change in U.S. office cap rates, reflecting the rise in benchmark yields.

Office yields have caught up to rising benchmark interest rates, with the latter spiking by 215bp year-to-date. The current risk premium—or the difference between cap rates and 10-year Treasury rates—of 390bp is lower than the 448bp spread reported in the past 10 years, which should apply upward pressure to cap rates and therefore depreciate asset valuations in the coming months.



Source: AVANT by Avison Young, RCA, U.S. Department of the Treasury

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Office insights glossary of terms

Demand

- **Leasing activity:** total square footage of relocations, renewals, expansions and subleases expressed when the leases are signed, not when tenants take physical occupancy of the space
- **Absorption:** period-over-period change in occupied square footage

Supply

- **Direct vacancy rate:** space operated by landlords that is ready for immediate occupancy
- **Sublease vacancy rate:** space operated by sublandlords that is ready for immediate occupancy
- **Total vacancy rate:** sum of direct vacancy rate and sublease vacancy rate
- **Availability rate:** space that is vacant plus space that will become vacant over an indefinite time horizon, including spaces that are occupied by vacating tenants and under-construction properties

Office rents and concessions

- **Asking rents:** pricing guidance provided by landlords to tenants for available space expressed as full service (FS)
- **Base rents:** fair market value of market-level lease pricing based on representative executed leases, expressed as full service (FS)
- **Free rent period:** months of free rent that are typically provided upfront by landlords to tenants as a concession to offset the total cost of a lease and/or the construction timeline of an office suite
- **Tenant improvement allowance:** an allowance expressed in dollars per square foot provided from landlords to tenants to offset build-out, engineering, space planning and related permit costs
- **Net effective rent:** base rents discounted by the dollar values of tenant improvement allowance and free rent concessions expressed as full service (FS)

Capital markets

- **Investment volume:** office sales dollars expressed when the transactions close and based on inventory thresholds; partial-interest sale dollar amounts are not grossed-up to reflect the 100% value of the sale
- **Asset pricing:** unweighted average per-square-foot asset pricing of market-level closed sales
- **Cap rate:** net operating income divided by sale price; this measurement of market-level investment returns is calculated as an unweighted average based on closed investment sales

Vitality Index

- **Visitor volumes:** based on extrapolated, anonymized cell phone pings provided by Orbital Insight at custom, geofenced locations, the Vitality Index tracks visitor volumes at representative areas of interest across markets and property types

Explore our latest data and insights

Putting people and the planet first

There is a vital role for our sector to create healthy, productive workplaces for employees, cities that are centers of prosperity for their citizens, and built spaces and places that create a net benefit to the economy, the environment and the community.

Global ESG Report

The return of people and places

Companies across North America continue to grapple with uncertainty. What will the future of work look like? Are downtowns regaining their pre-pandemic vitality? How will societal, cultural and environmental shifts shape the next normal?

The Vitality Index

Tracking U.S. employment trends

Rising layoffs and declining job postings are also indicating that the economy is becoming distressed. Employment data and industries are analyzed across cycles for a real-time and historical look at economic conditions.

U.S. Employment Overview

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For more market insights and information visit **avisonyoung.com**

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