



AVISON
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Northern Virginia Office Insight Report

Q3 2021

AVANT
by AVISON YOUNG

Key takeaways



Economic conditions

- Unemployment in Northern Virginia is now at **3.7 percent**, essentially unchanged since last quarter, after recovering from a pandemic high of 10.2 percent.
- Office-using employment is down **2.2 percent** since before the pandemic, but most of this drop is due to recent layoffs in local government. Most other office-using sectors have seen employment recover past their pre-pandemic level.



Recovery rate

- Activity across the DC Metro region at workplaces, shopping centers, universities, and other areas of interest is **64.8 percent** of pre-COVID levels, as measured by extrapolated mobility data.
- Looking at office locations specifically, visitor traffic is only **36.0 percent** of pre-COVID levels. Stagnant office recovery in the face of a relatively strong overall recovery suggests that employees are not fearful of COVID-19, but simply prefer working remotely.



Office demand

- Q3 leasing activity rose **14.4 percent** in comparison to the same quarter in 2020. YTD activity remains on pace to finish below 2020 levels.
- Renewals are accounting for an elevated share of leasing activity, at **45.9 percent**.
- The average lease term for a **new** lease has risen **8.1 percent** since its pandemic low. The average renewal lease term continues to fall as tenants use short-term renewals to postpone their long-term leasing decisions.

Key takeaways



Office supply

- Direct and sublease vacancy have achieved all-time highs, totaling **18.2 percent**.
- Sublease vacancy did not substantially grow in Q3 and remains elevated by **124 percent** in comparison to the end of 2019.
- The construction pipeline has thinned, which should help curb vacancy increases, and most active projects are either substantially preleased or are owner-occupied buildings like Amazon's HQ2.



Pricing trends

- Concessions continue to rise, but at a slower rate than in 2020. In 2021, the average TI allowance and free rent period have increased by **1.2 percent** and **5.5 percent**, respectively.
- Average asking rents have risen by a modest **1.5 percent** in 2021, though rising concessions balance this increase on a net effective basis.



Capital markets

- After a slow first half, Northern Virginia saw **\$1.2 billion** in investment sales in Q3, putting volume back on pace to match or exceed 2020 levels.
- Pricing for value-add investments has risen **24.1 percent** in 2021, while stabilized pricing has fallen due to a high proportion of activity taking place in lower-priced submarkets outside the Beltway.
- Value-add sales have continued to account for an increasing share of Northern Virginia's sale activity and have made up **45.0 percent** of dollar volume in 2020-2021.



01.

Economic and demographic trends

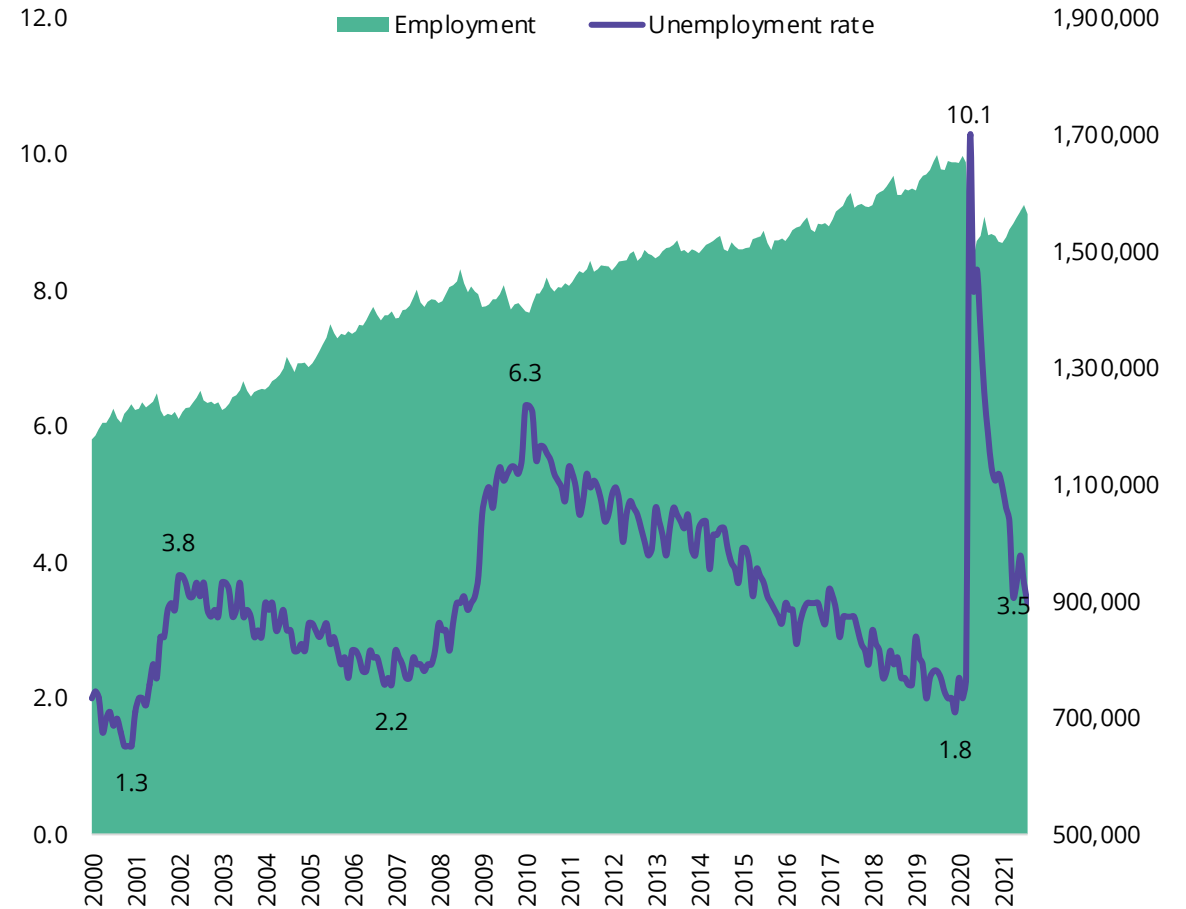
The pandemic caused a sharper disruption to the Northern Virginia economy than past recessions did, but the region fared well by national standards and office employment proved resilient.

Employment and unemployment rate

3.4%

Northern Virginia unemployment rate as of July 2021

After rapidly spiking and then falling, unemployment has hovered between 3.5% and 4.1% for the past several months.



Note: Not seasonally adjusted data.
Source: Bureau of Labor Statistics

Office-using job gains and losses

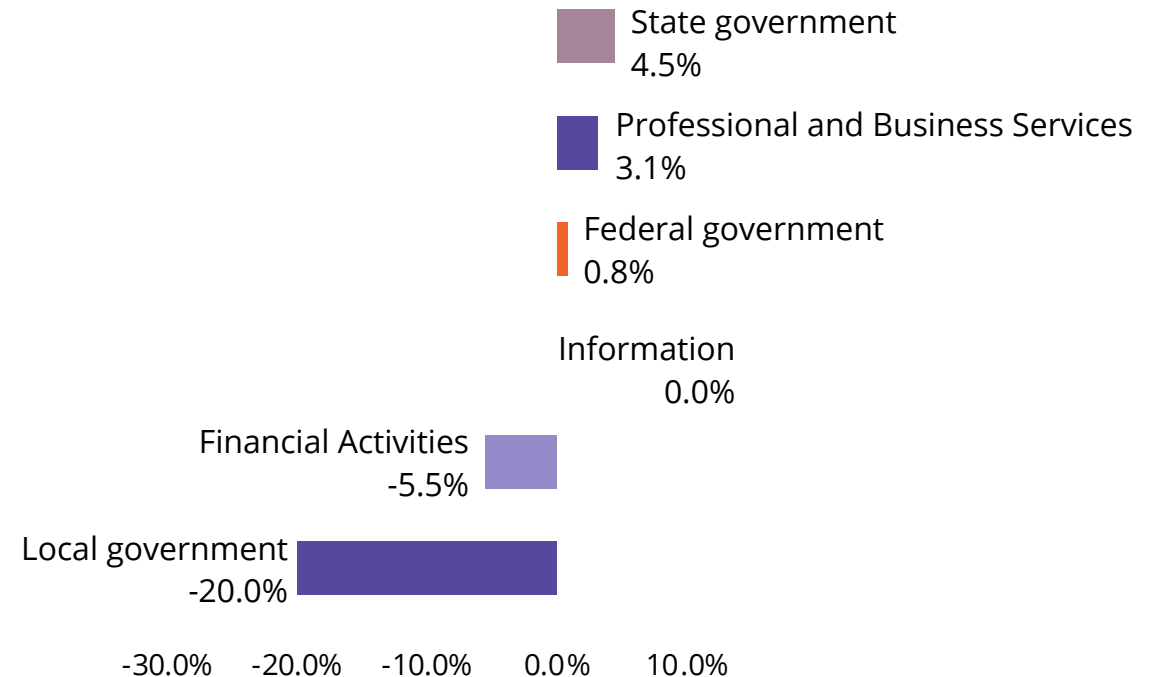
-2.2%

Change in office-using employment since February 2020

Office-using employment in Northern Virginia is now down 2.2% compared to before the pandemic. Most office-using sectors have fared well and the losses are almost entirely due to a recent decline in local government employment.

Total change in Northern Virginia job gains/(losses)

February 2020 to April 2021



Note: Not seasonally adjusted data. Northern Virginia subset of Metro DC metropolitan statistical area.
Source: Bureau of Labor Statistics

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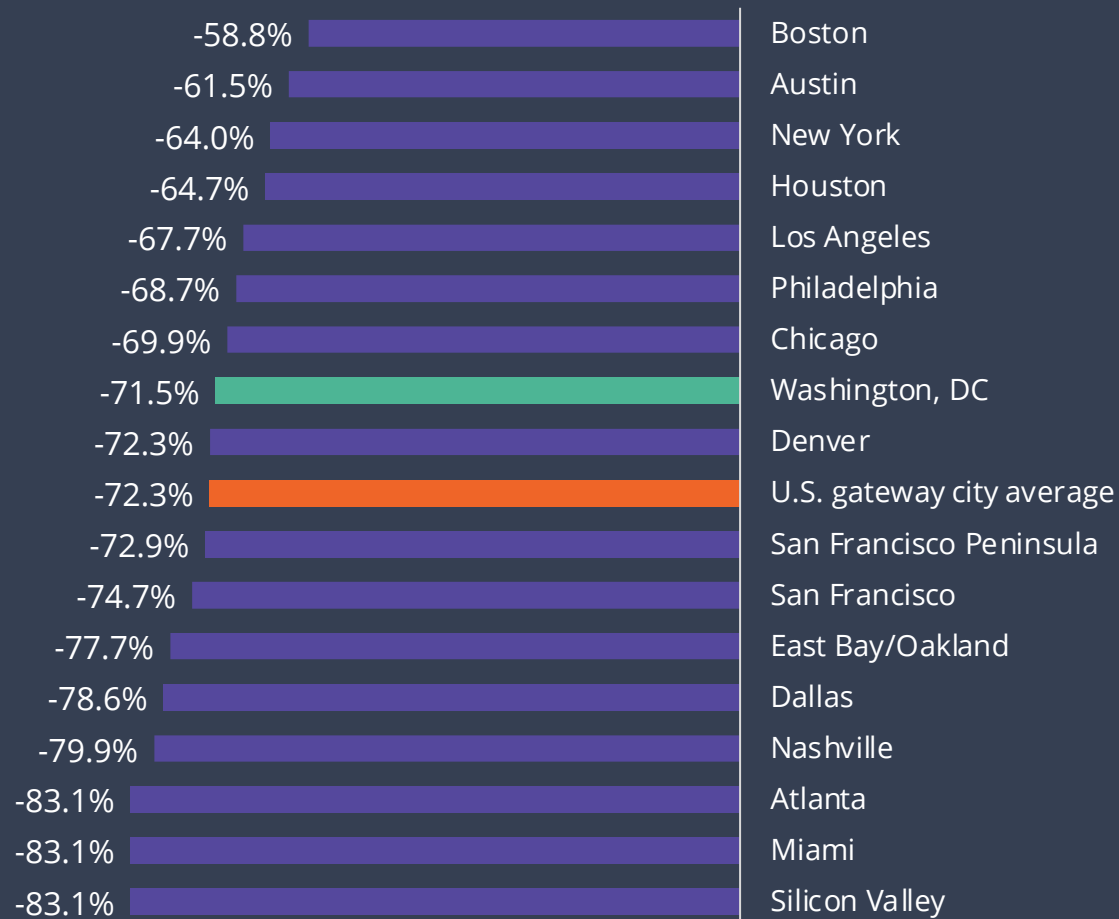
U.S. return-to-work rates since start of COVID

-72.3%

Average office visitor volumes across U.S. gateway cities, March 2, 2020 vs. September 20, 2021

Return-to-work efforts across cities have been influenced by governmental regulations (informed by infection and vaccination rates), office-using industry composition and employees' reliance on mass transit.

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Note: Representative full-building office occupiers only. Weekdays only. Data as of September 20, 2021. Source: Orbital Insight, AVANT by Avison Young

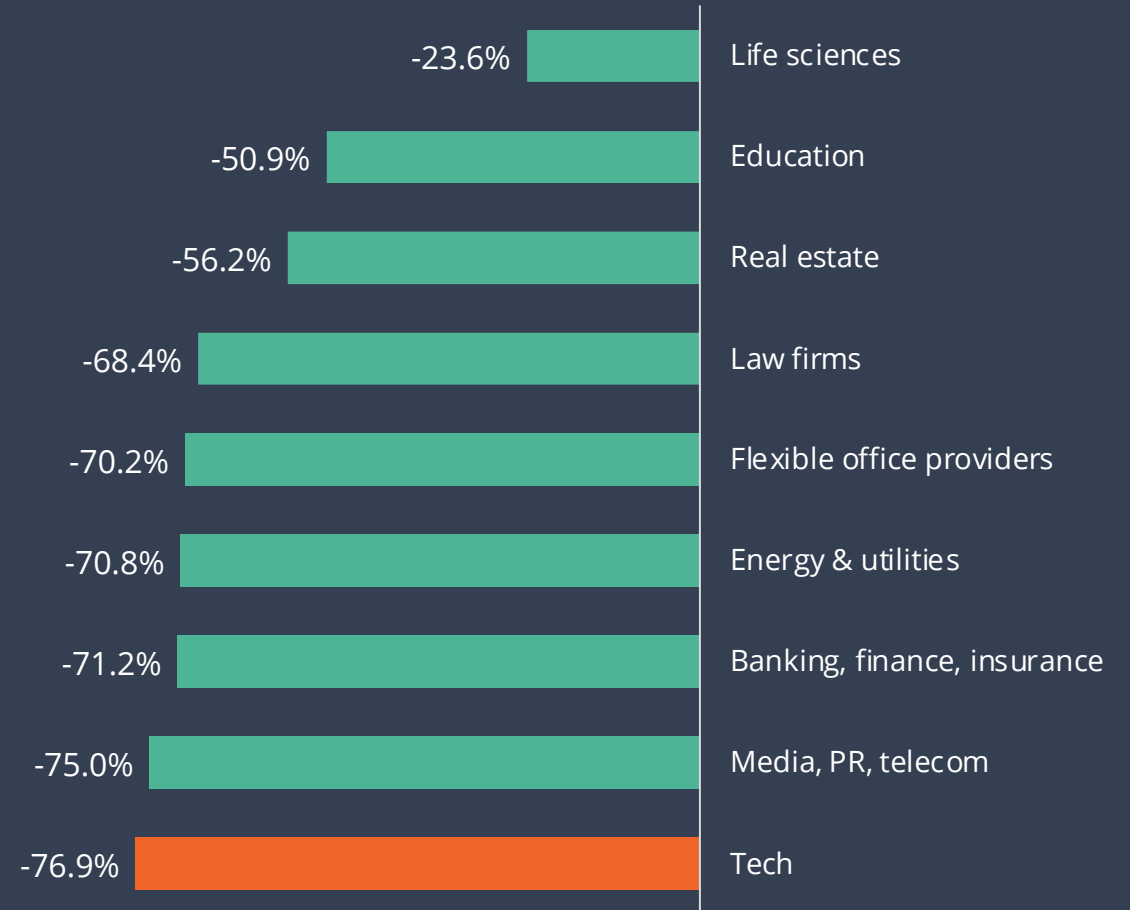
U.S. return-to-work rates since start of COVID

-76.9%

Average tech office visitor volumes across U.S. gateway cities, March 2, 2020 vs. September 20, 2021

Tech companies have adopted remote work strategies more than most major office-occupying industries, while life sciences and real estate companies have embraced flexible in-office and remote working arrangements.

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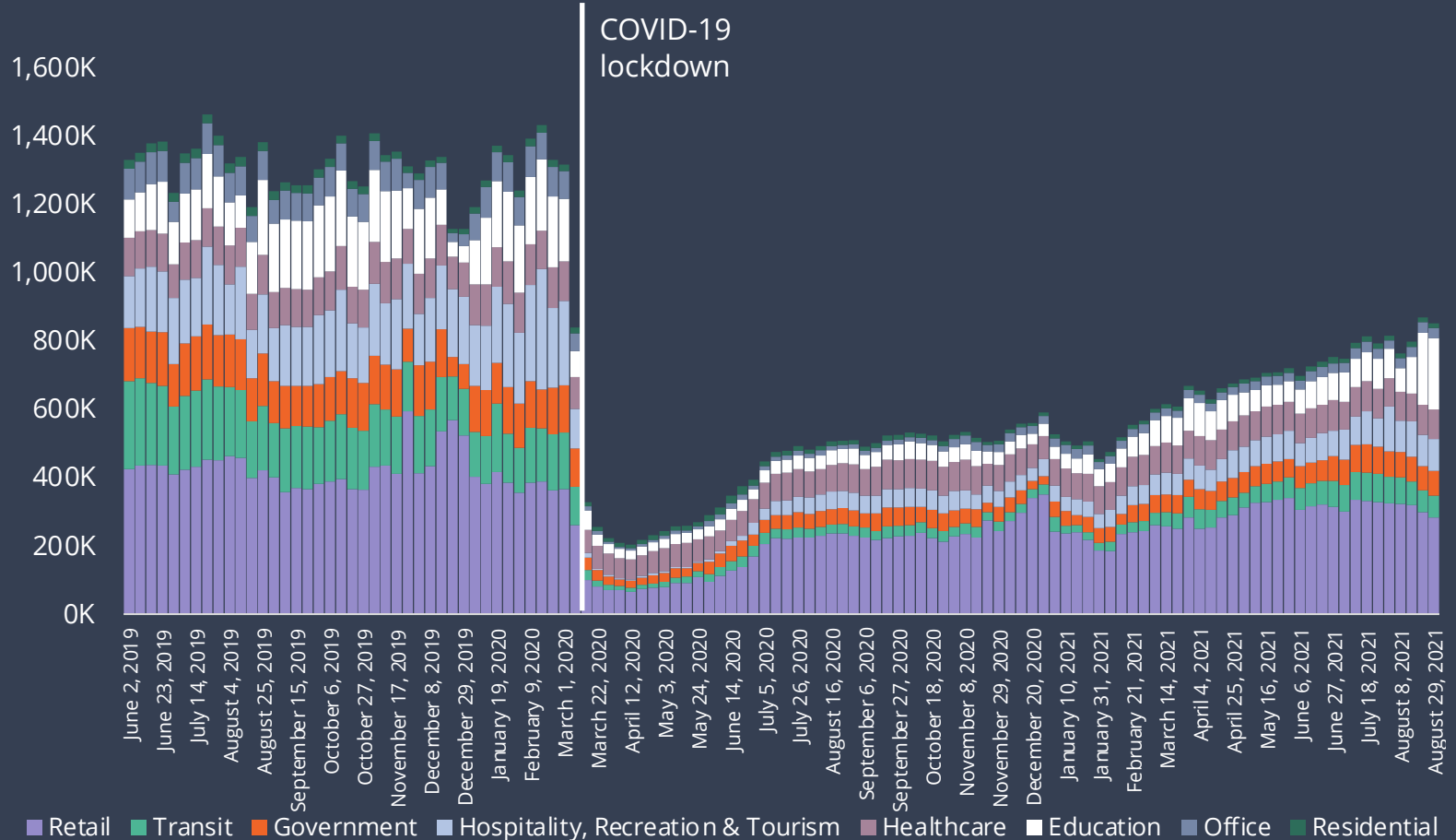
Note: Representative full-building office occupiers only. Weekdays only. Data as of September 20, 2021. Source: Orbital Insight, AVANT by Avison Young

Recovery index

64.8%

Regional activity in past six weeks compared to the six weeks before lockdown

Although the fall has created an uptick at schools (white area on the chart), regional activity in other sectors has started to decline.



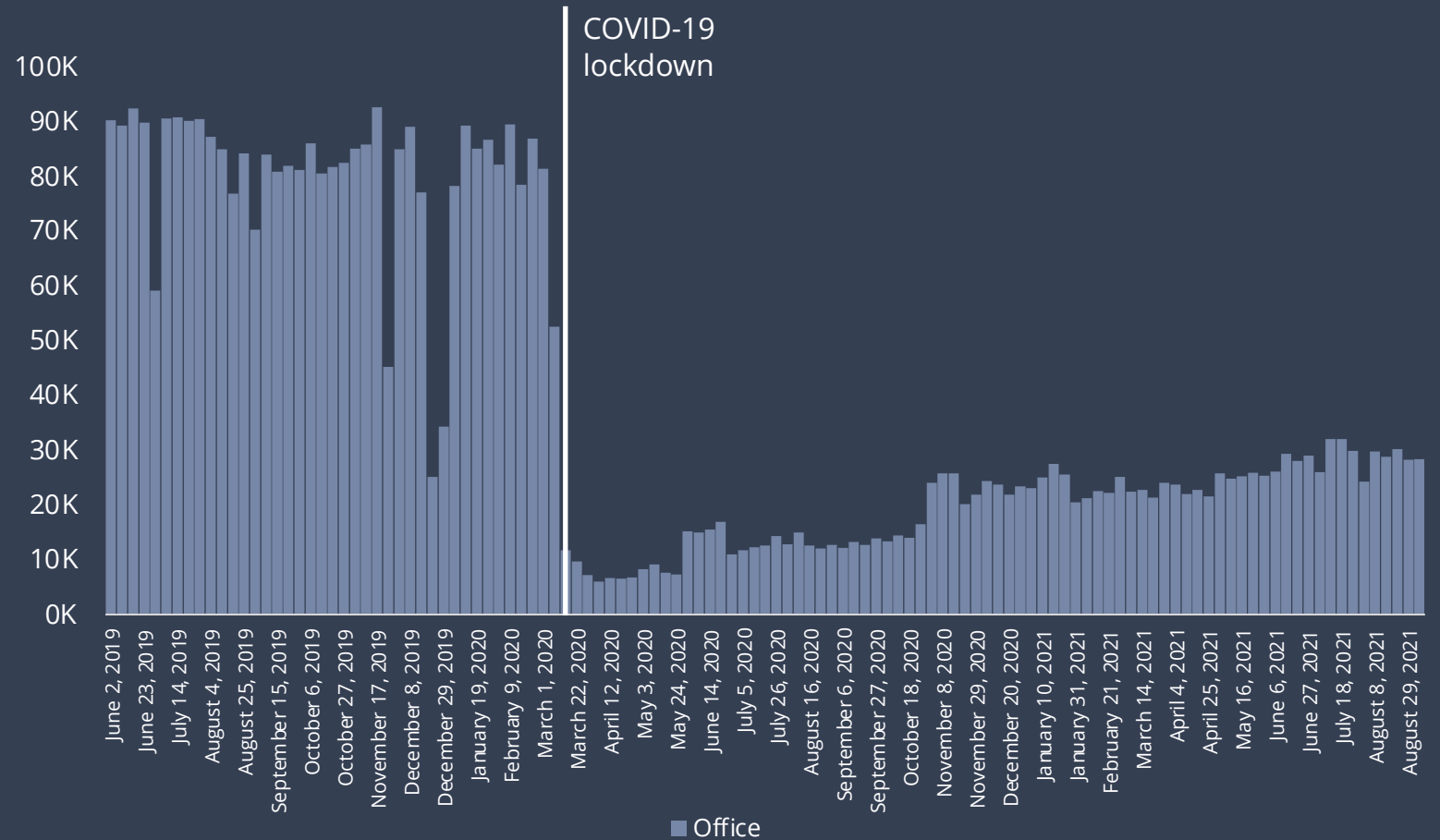
Note: Representative areas of interest. Weekdays only.
Source: Orbital Insights, AVANT by Avison Young

Recovery index

36.0%

Regional office activity in past 6 weeks compared to the 6 weeks before lockdown

Traffic to office buildings hasn't recovered nearly as much as the region overall and has once again begun to decline, likely a response to new strains of COVID-19.



Note: Representative areas of interest. Weekdays only.
Source: Orbital Insights, AVANT by Avison Young

Change in local activity levels, 2019 vs. 2021

-80.0%

Office

-34.5%

Retail

-67.2%

Transit

-23.3%

Healthcare

-0.6%

Education

-40.4%

Government

-47.6%

Residential

-42.0%

Hospitality & Tourism

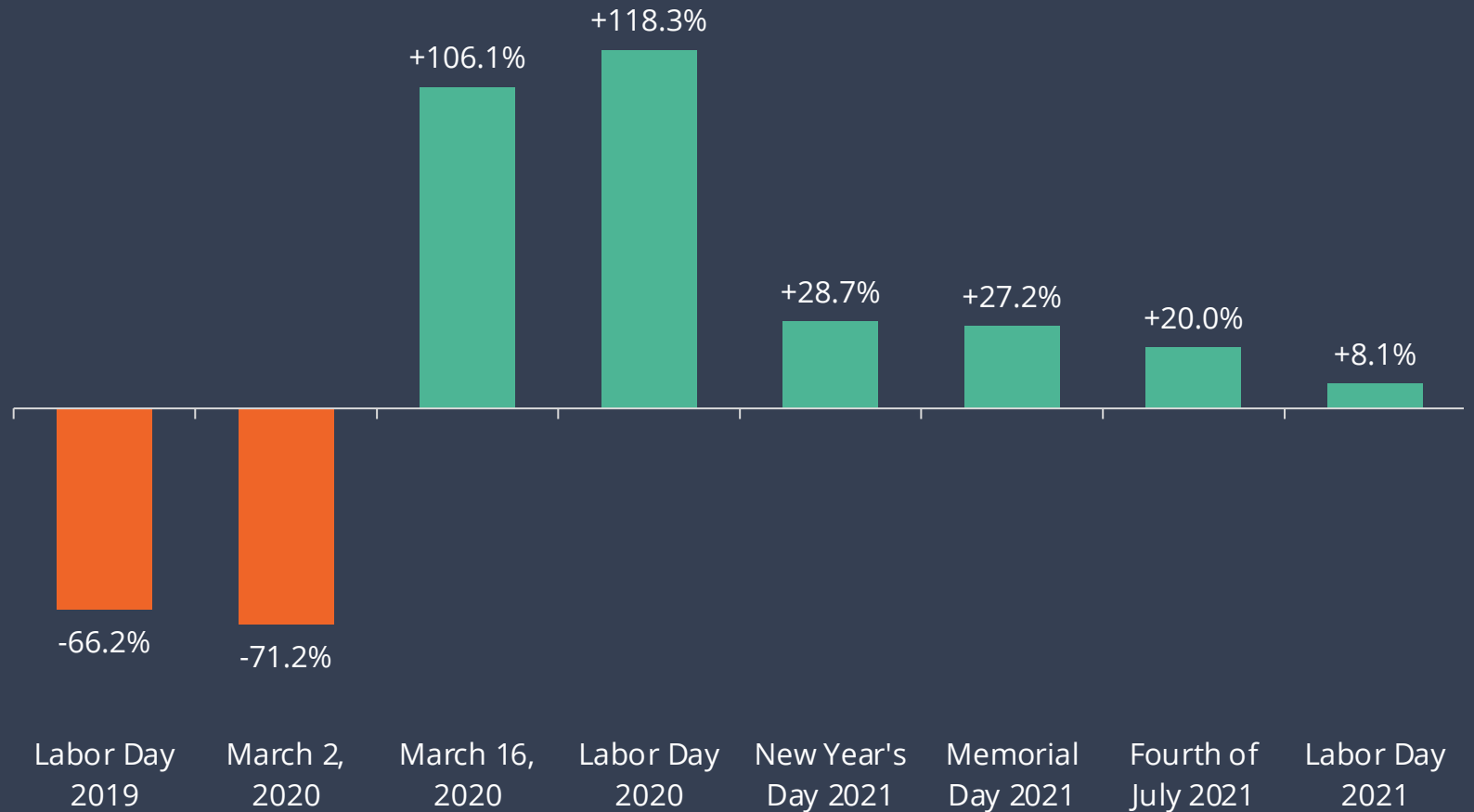
Note: Select, representative areas of interest only. Weekdays only.
Week of September 16, 2019 vs. week of September 20, 2021.
Source: Orbital Insight, AVANT by Avison Young

Evolution of local return-to-work efforts

+20.0%

Metro DC office visitor volume since the Fourth of July 2021

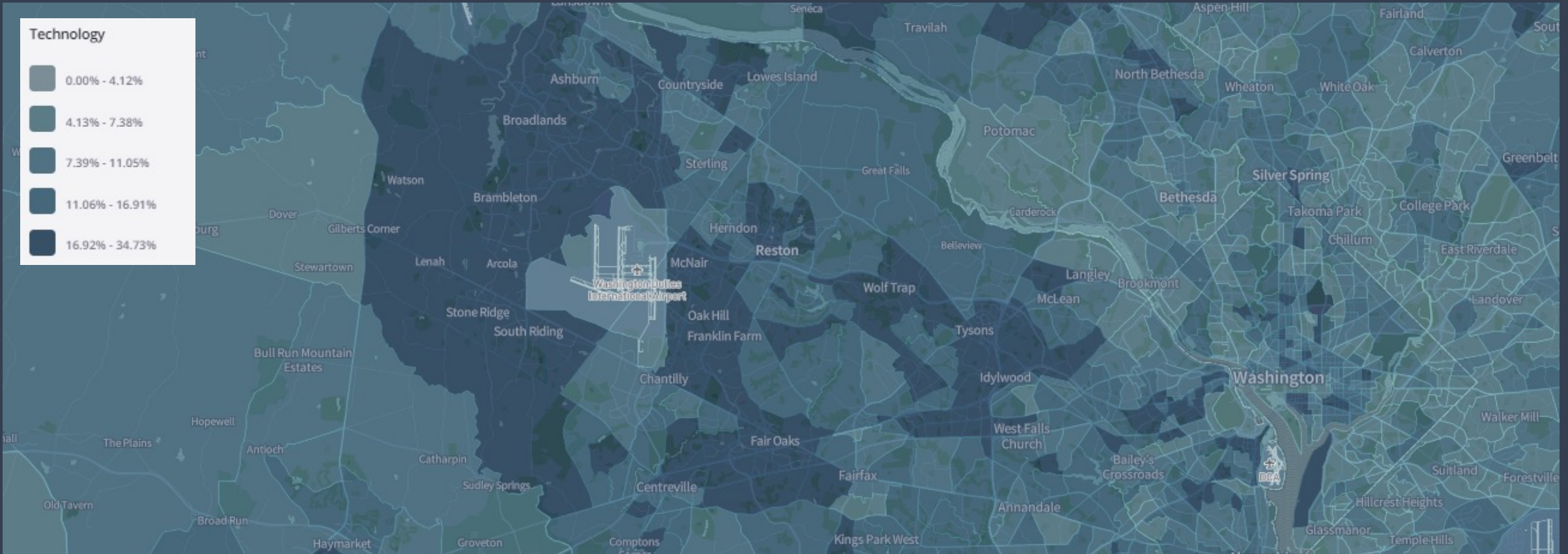
While office activity remains dramatically below the levels of traffic seen before the pandemic, it has recovered substantially from the low point of the COVID-19 lockdowns.



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Note: Select, representative occupiers only. Weekdays only.
Data as of September 20, 2021.
Source: Orbital Insight, AVANT by Avison Young

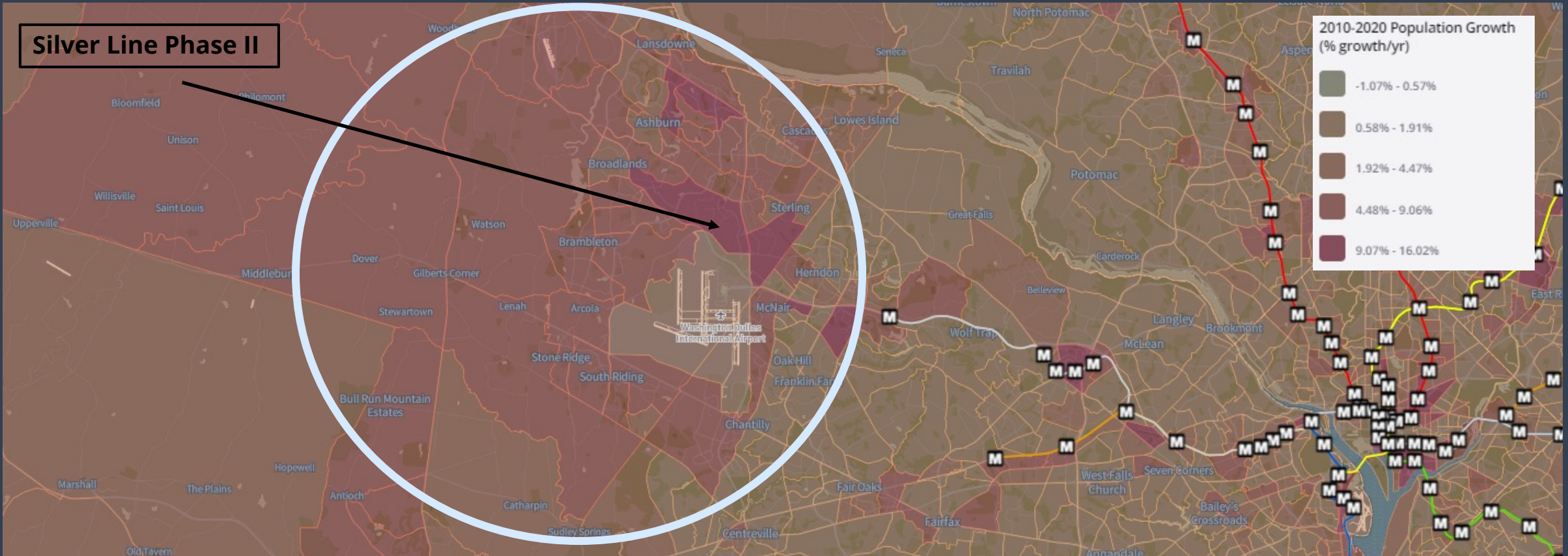
Regional High-Tech Employment



Toll Road and Route 28 are poised to attract high tech leasing due to the proximity to top talent and a diverse workforce.

Source: AVANT by Avison Young

2010 -2020 Population Growth



Northern Virginia population growth is largely concentrated around current, and future, transit hubs located in western **Fairfax** and eastern **Loudon** counties.

02.

Office occupier conditions

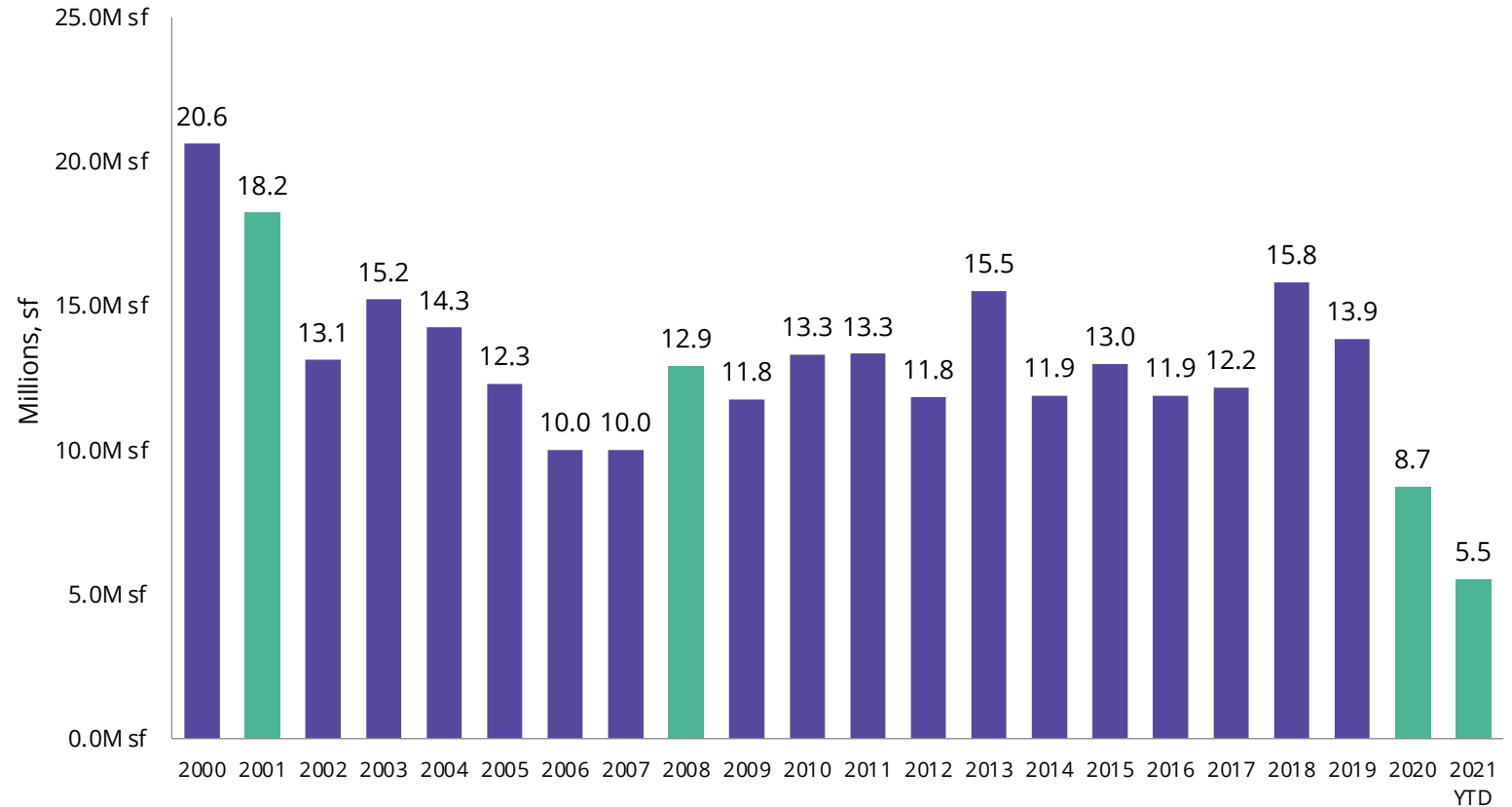
With demand dramatically hampered by the pandemic, vacancy has hit record highs and concessions have followed suit.

Office leasing activity

+14.4%

Q3 2021 leasing activity compared to same quarter in 2020.

Q3 leasing activity showed an increase compared to Q3 2020, but YTD leasing remains 19.9% lower than the same three quarters in 2020.

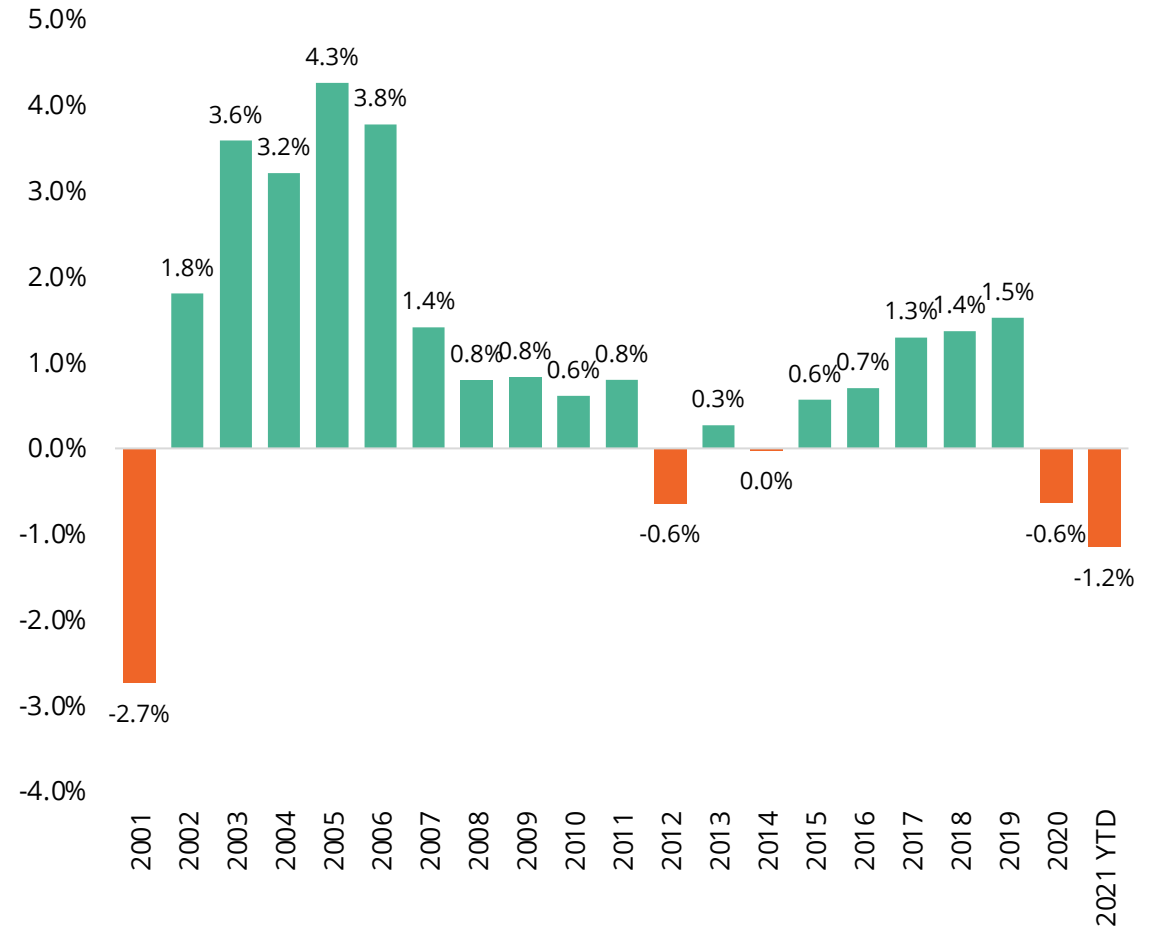


Source: AVANT by Avison Young

-1.2%

YTD Net absorption as a percentage of inventory

While Northern Virginia is typically resilient in downturns and weathered the Global Financial Crisis while continuing to gain occupancy, the dramatic shift in office use patterns due to COVID-19 has continued to weigh on the market throughout 2021.



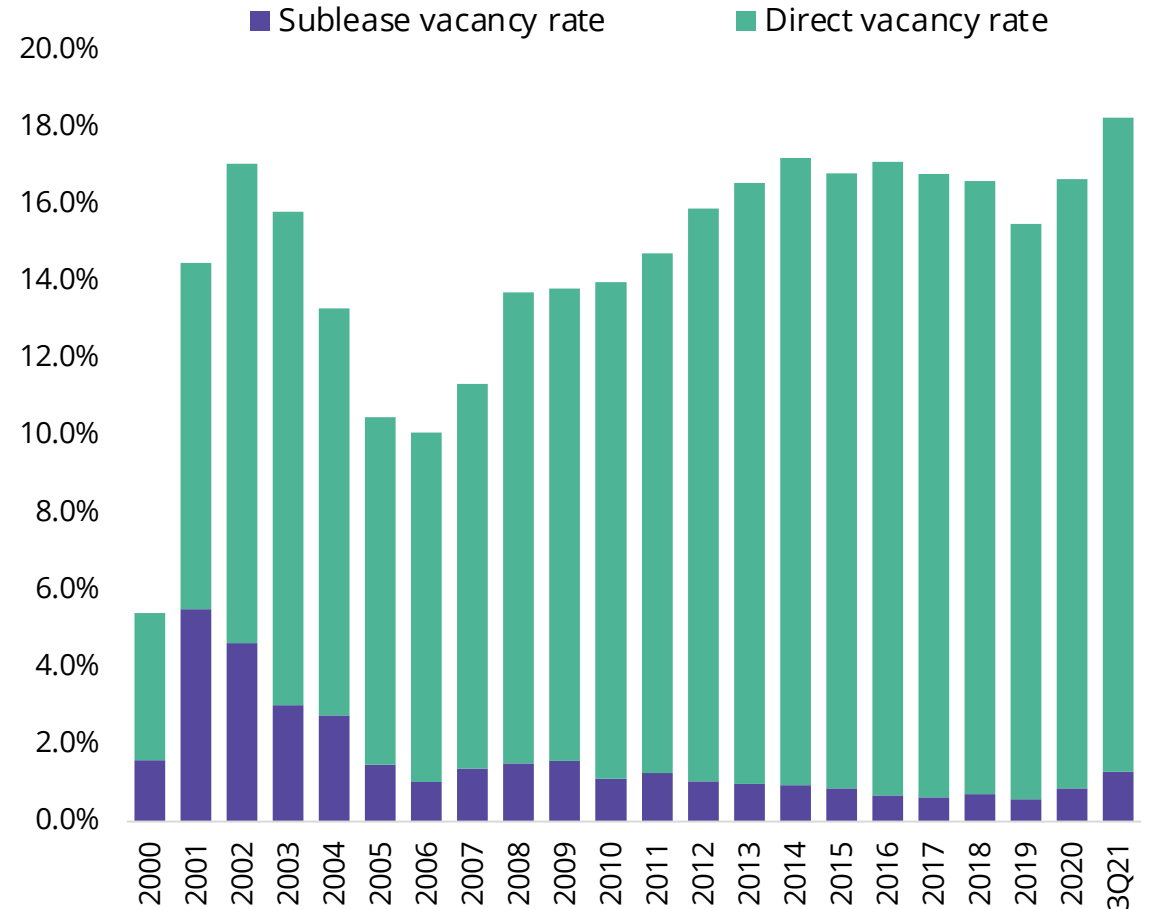
Source: AVANT by Avison Young

Vacancy rate

18.2%

Total vacancy as of Q3 2021

Total vacancy has reached its highest level in at least two decades, though sublease vacancy remains lower than in either of the past two cycles.



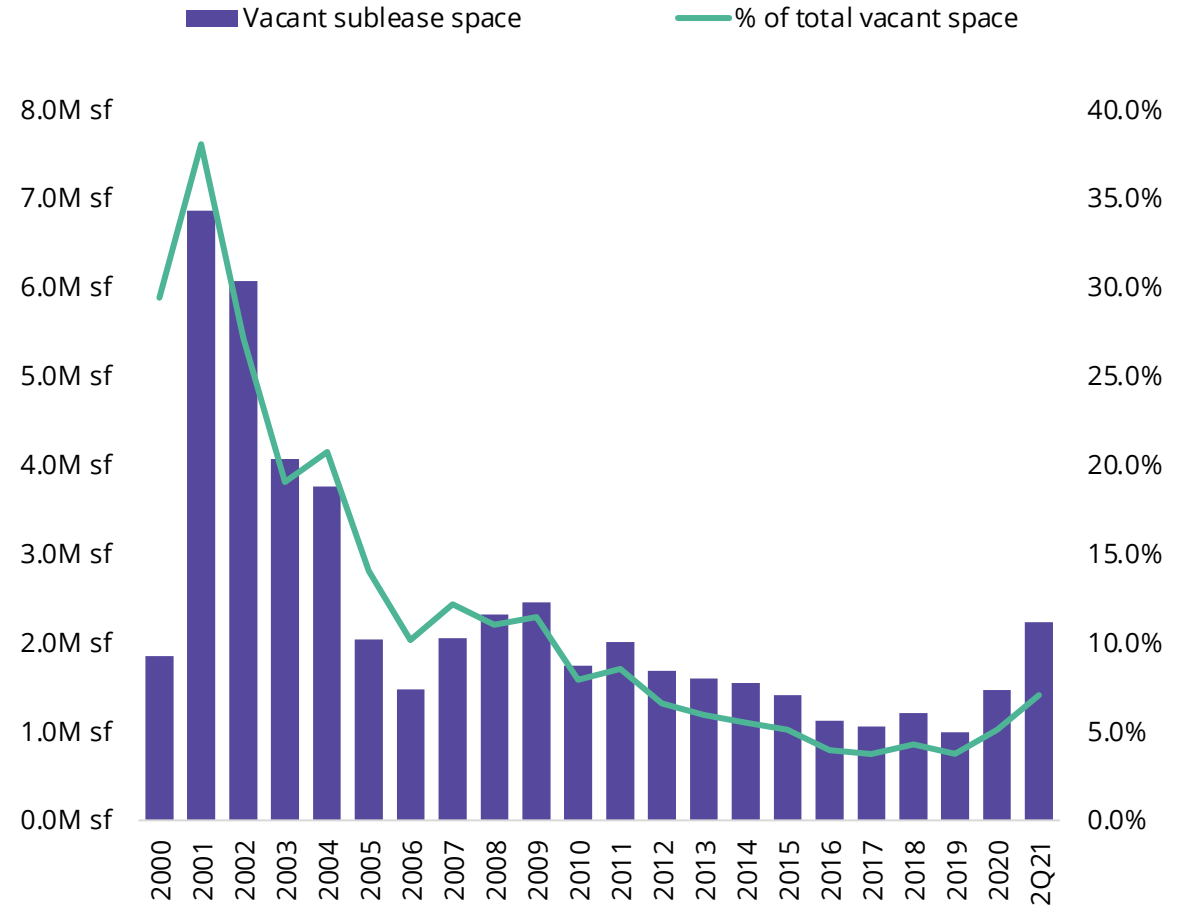
Source: AVANT by Avison Young

Vacant sublease space

52%

Rise in sublease vacant space since end of 2020

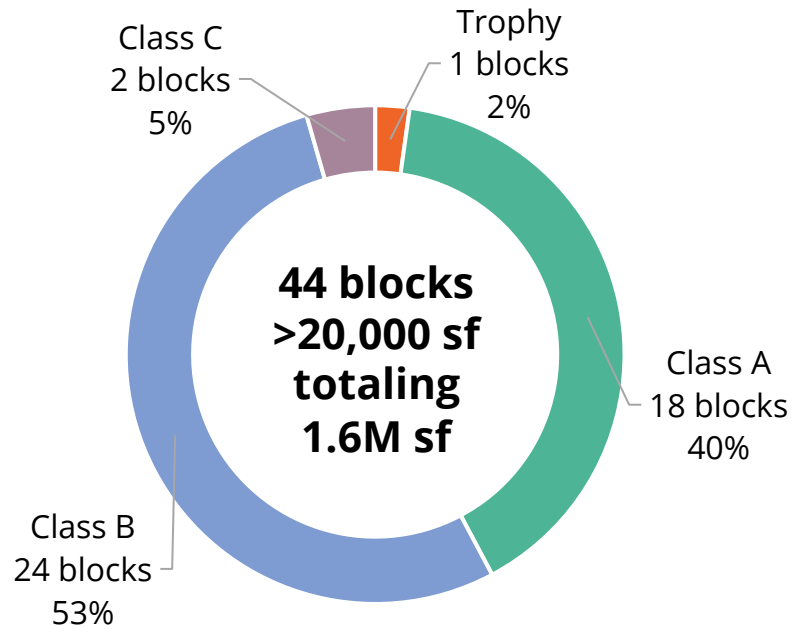
The volume of vacant sublease space continues to rise but remains below the peaks seen in either of the past two market cycles.



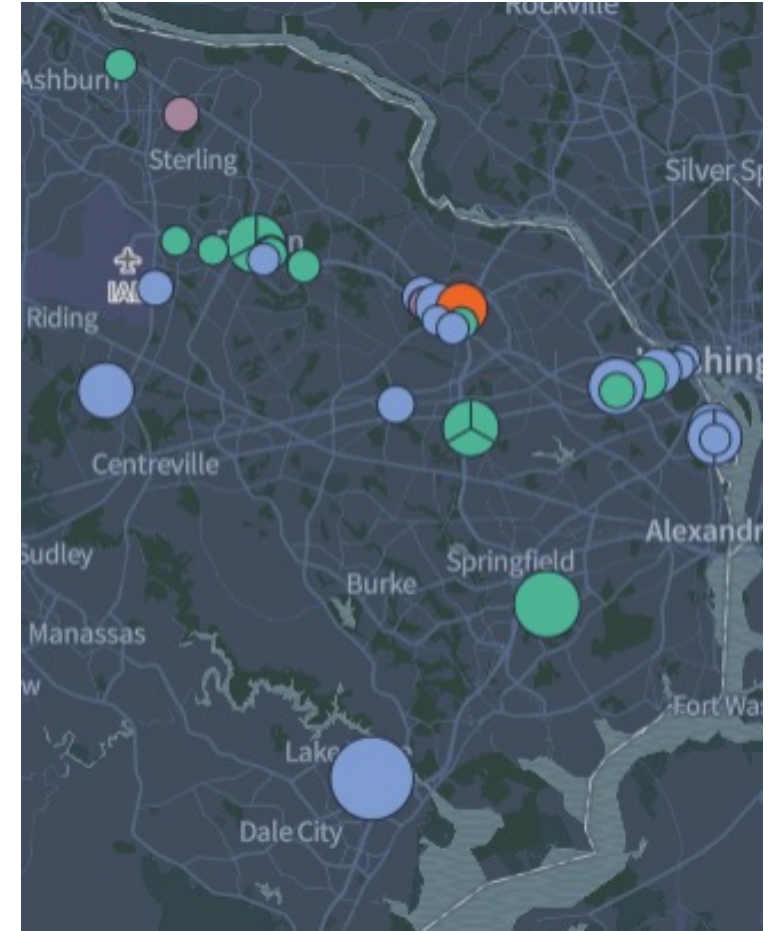
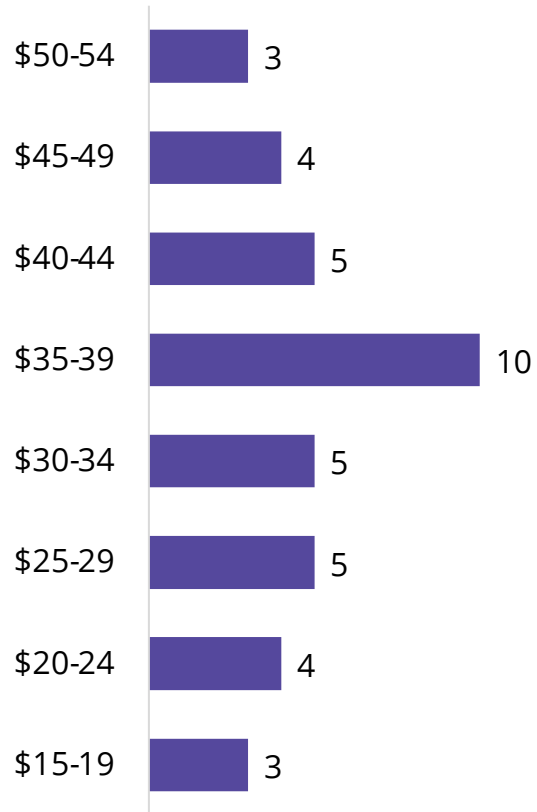
Source: AVANT by Avison Young

Sublease supply pipeline

Building classification



Asking rent per square foot



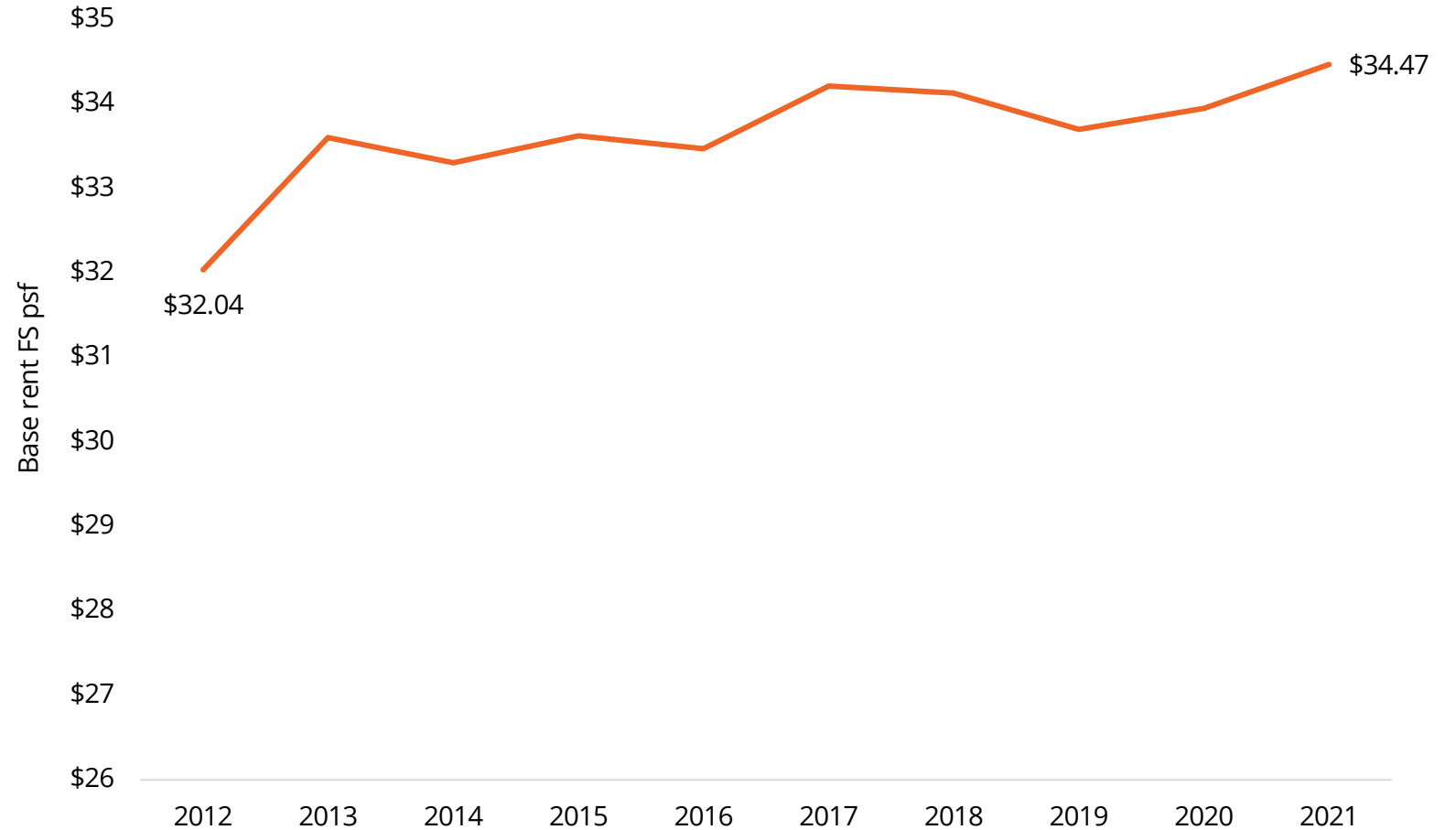
Source: AVANT by Avison Young

Base rents

+ 1.5%

Change in base rents, year-to-date 2021

The average base rent actually rose, though increased concession packages mean that net effective rates are not increasing.

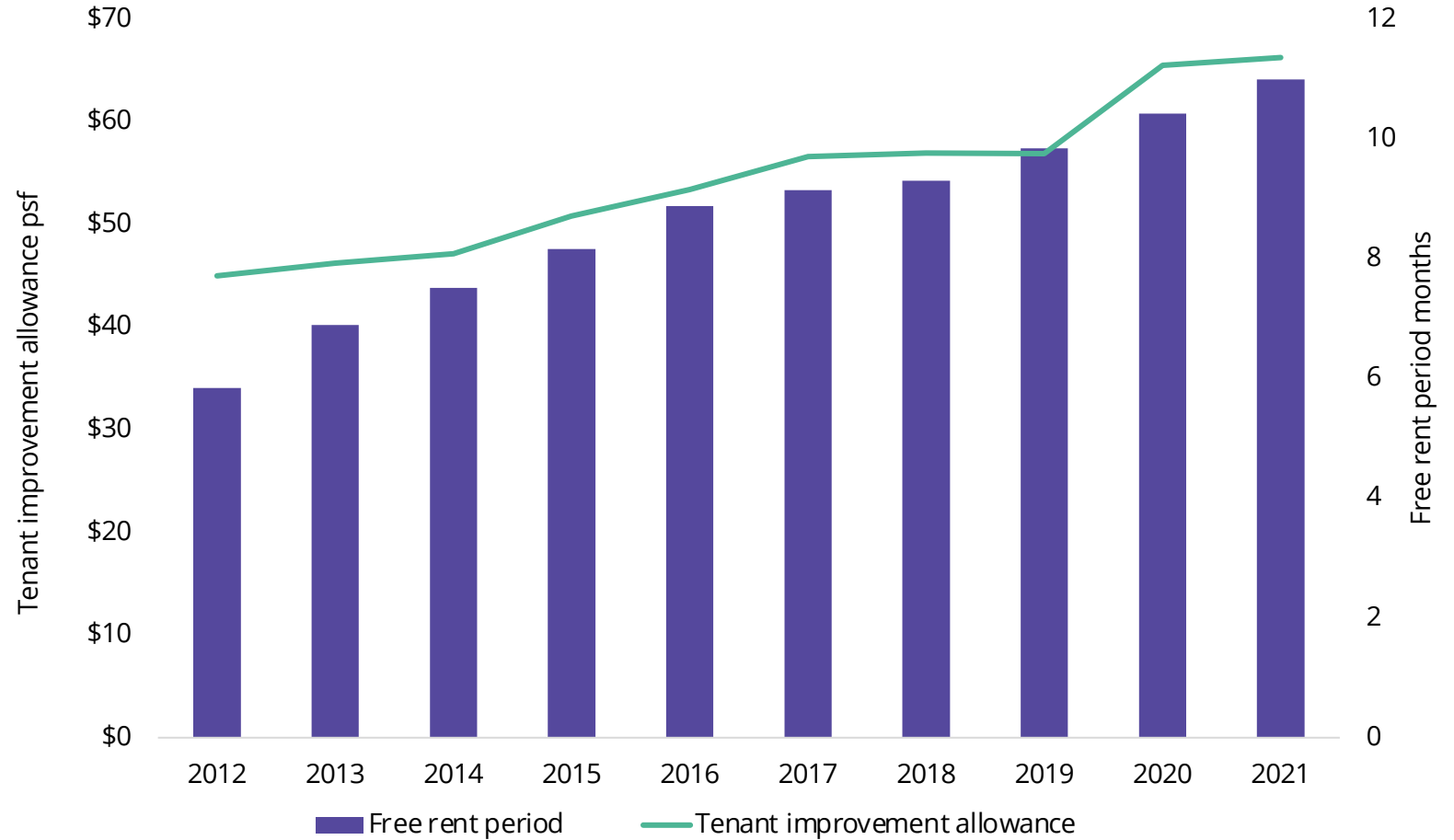


Note: Excludes subleases, expansions and renewals.
Source: AVANT by Avison Young

5.4%

Increase in average free rent period since beginning of 2021

The average TI allowance and free rent period have both increased in 2021, but this increase has levelled out in comparison to the jump seen in 2020.



Note: Excludes subleases, expansions and renewals. Normalized to 10-year lease terms.
Source: AVANT by Avison Young

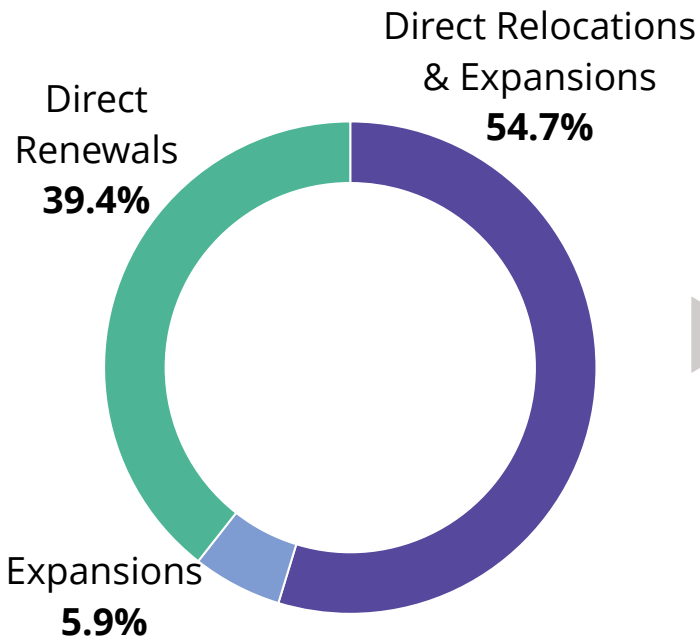
Transaction activity by lease type

45.9%

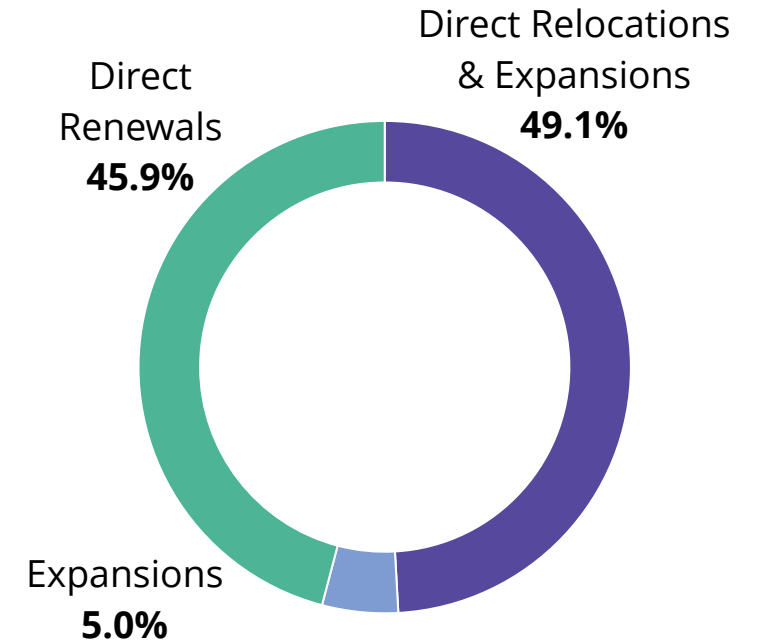
Renewals share of office leasing activity post-COVID

Renewals still account for an elevated share of leasing since the onset of COVID. Despite many tenants considering remote work and a shrunken office footprint, expansion activity is continuing strongly at 5% of all lease volume.

2018-3/2020



Post-COVID



Source: AVANT by Avison Young

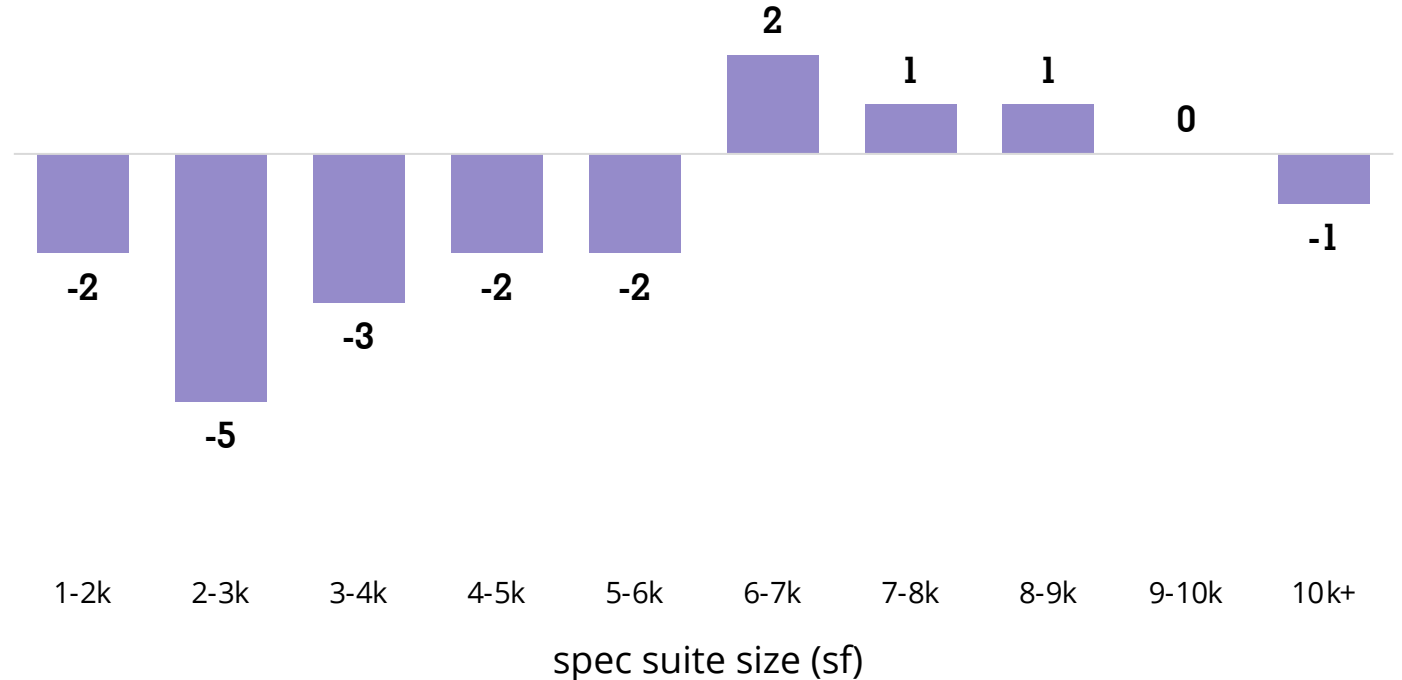
Spec suite leasing

-8.0%

Change in RB Corridor spec suite inventory, past 12 months

Spec suite availability has begun to decline even as overall market vacancy remains elevated. Although smaller suites have seen the most leasing over the past year, tour activity seems to be increasingly focused on suites larger than 5,000 square feet.

Net Change in # Spec Suites by Size Range (sf), 2020-2021

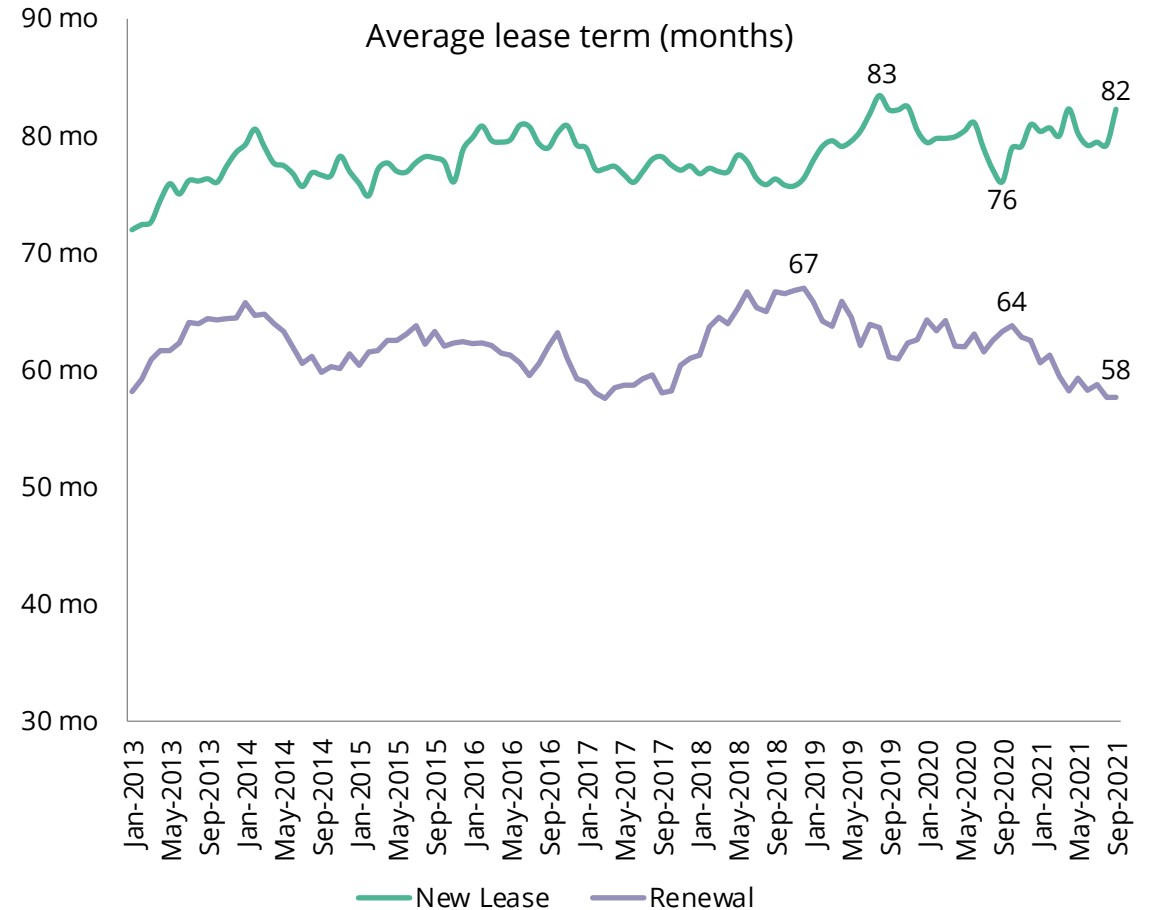


Average lease term

+8.1%

Rise in average *new* lease term since September 2020

The average lease term on new leases has bounced back from its pandemic low, rising 8.1% since bottoming in September 2020. Meanwhile, with many tenants still delaying their long-term real estate decisions, short-term renewals continue to pull down the average renewal term.



Source: AVANT by Avison Young

Development pipeline

9 properties

under construction

4.3 msf

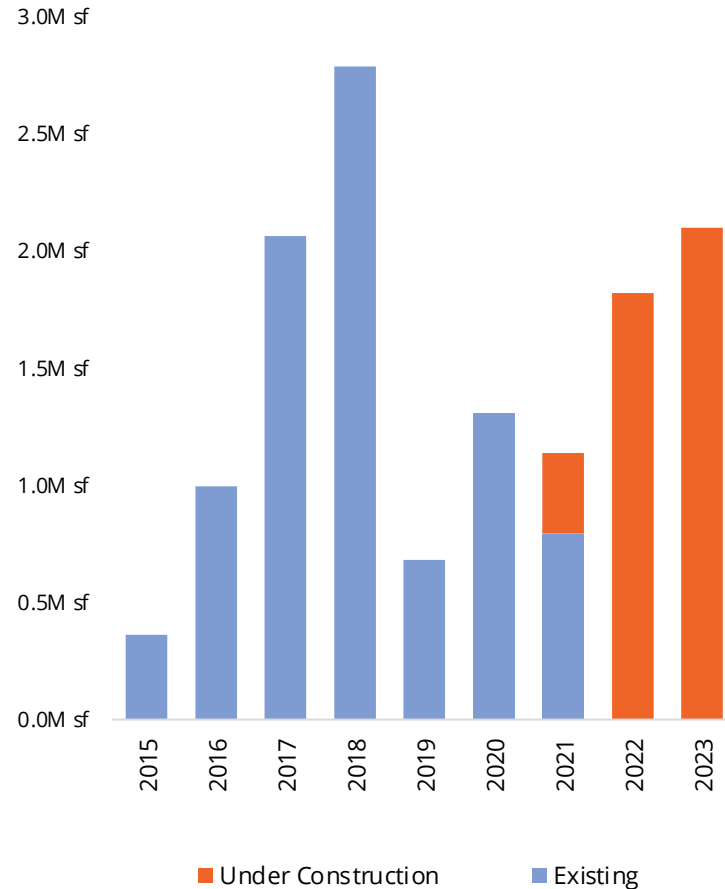
proposed or under construction

2.5%

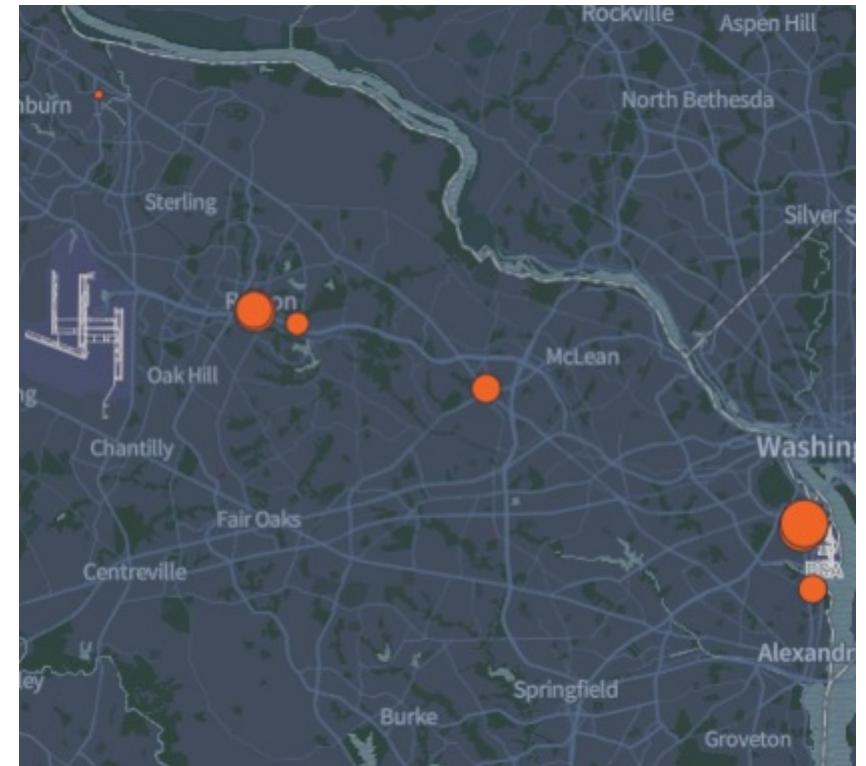
share of office inventory

1991

average delivery date of existing Northern Virginia offices



Source: AVANT by Avison Young



03.

Capital market conditions

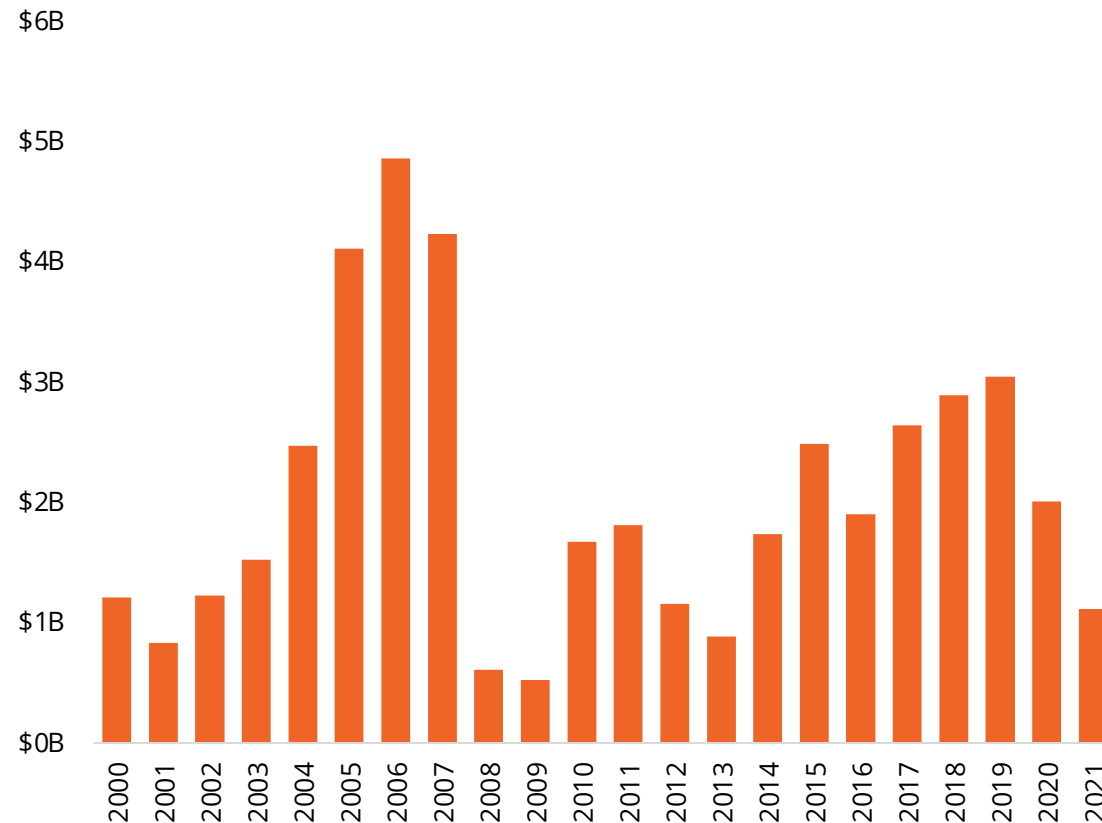
Investment in Northern Virginia has continued to move slowly, with submarkets outside the Beltway driving a majority of activity.

Office investment dollar volume

\$1.1B

Northern Virginia office dollar Volume YTD

Investment volume surged in Q3 after a weak first half of 2021 but remains on pace to finish slightly below 2021.



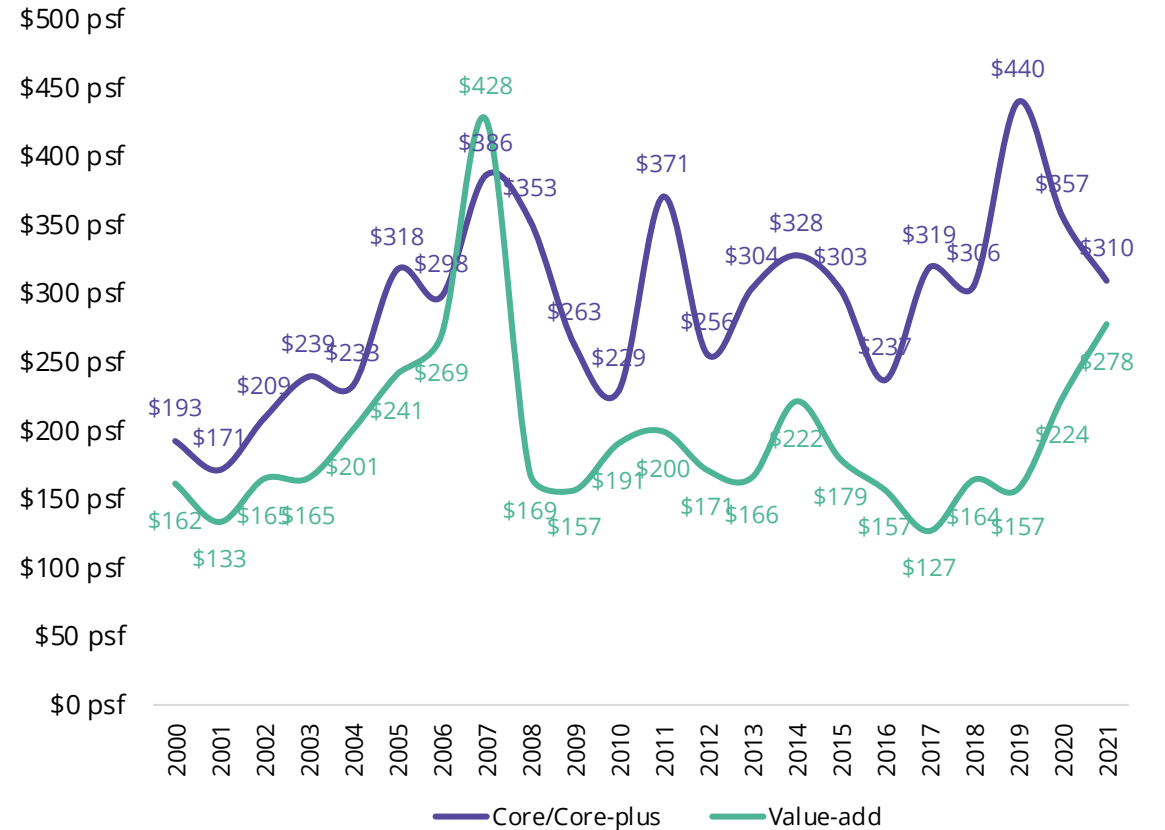
Source: AVANT by Avison Young, RCA
*includes buildings rumored but not yet launched for sale

Office asset pricing

24.1%

Rise in average value-add pricing since end of 2020

Unusually, value-add pricing has continued to rise during the downturn while stabilized core/core-plus pricing has declined. This decline can be at least partially attributed to the large share of activity that took place outside the beltway.



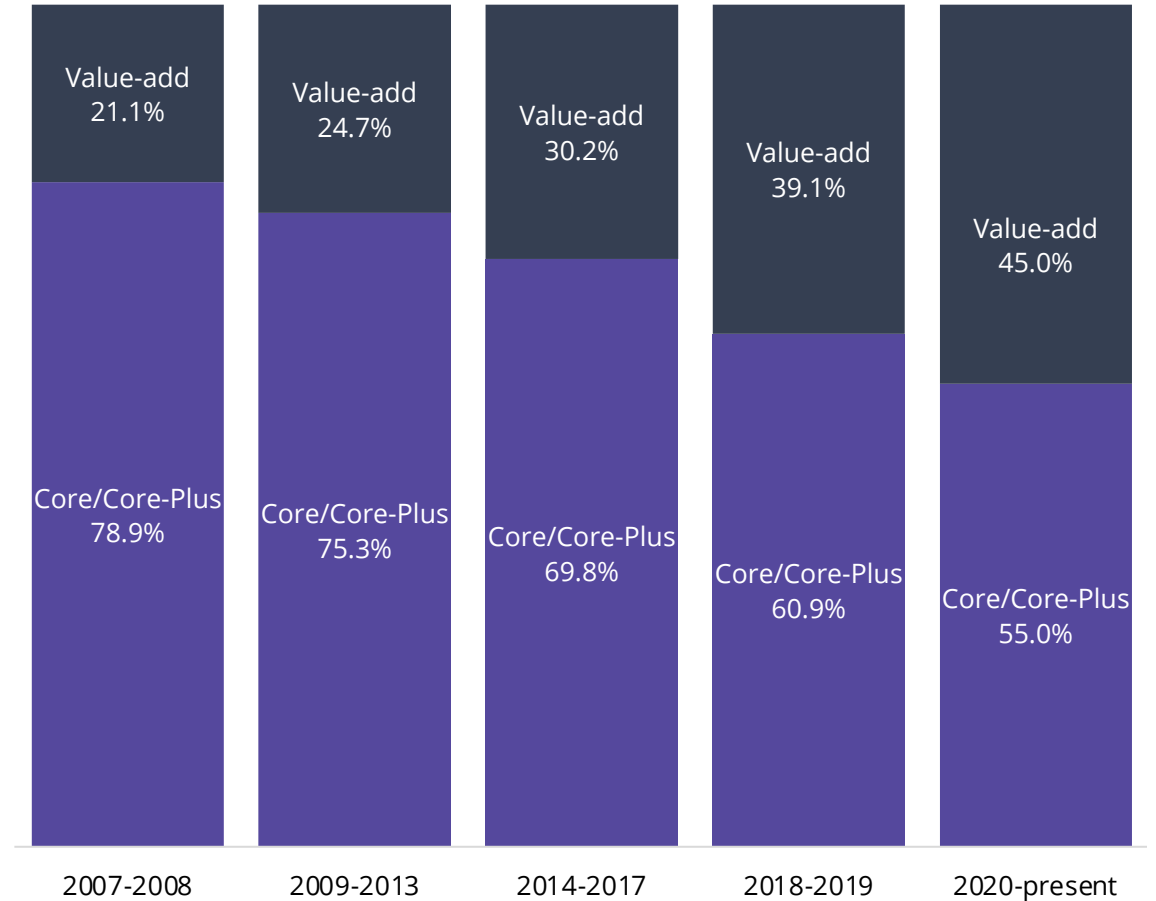
Source: AVANT by Avison Young, RCA

Office investment asset profiles

45.0%

Value-add share of investment sales in the pandemic

Although investors in many markets have targeted safer, stabilized assets during the downturn, value-add investments continue to account for an increasing share of sale volume in Northern Virginia.



Source: AVANT by Avison Young, RCA

Looking forward



Here's what we can expect

- An uptick in **large-tenant tour activity** suggests that leasing could accelerate in Q4. Pandemic-related hesitancy should continue to subside as long as government-mandated restrictions do not tighten.
- The intensity of the **amenity arms race** will continue to grow as landlords seek to attract companies back to the office and compete with one another to secure new leases from a shrinking pool of potential tenants.
- **Spec suites**, particularly on the larger end, will capture an outsized portion of demand as tenants return to the office market seeking quick occupancy. Spec suites offered on short lease terms (1-5 years) will be especially attractive.
- **Investment sales activity** is poised to increase inside the beltway, as several stabilized offerings have come to market in the past month.



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Let's talk

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