Washington, DC office market insights

Q4 2021

AVISON YOUNG

Key office takeaways

Economic conditions

- Essential and government workers accounted for 2.8% of total jobs gained since February 2021 which helped push **unemployment figures down to 5.2% for the city.**
- The large international presence in DC has been mitigated as COVID-19 variants and return-to-work policies are delayed, **resulting in a -68.7% decline,** measured using extrapolated mobility data.

Recovery rate

- Washington DC metropolitan return-to-work rates slightly lag the **national average, down 68.7%.**
- Despite slow return to office metrics, companies are adding jobs remotely with the total **workforce growing by 0.8%** since the beginning of the pandemic.

Office demand

- Overall leasing activity has been suppressed throughout the pandemic, currently sitting at **-28.3% of the long-term annual average** from the last 20 years.
- **DC's average lease size is down 3.16%** when compared to the five years prior to COVID, flight to quality has persisted, and tenants have often opted to take less space in higher class buildings.

Key office takeaways

Office supply

- The overall vacancy rate for the DC office market has **reached record highs rising to 14.7%**, an increase of 70 bp from the previous quarter.
- The **total availability rate is 28.6% higher** for 2021 when compared to the average over the prior five-year period, 22.96 msf - an indication vacancies are not close to their peak.

Pricing trends

- **Base rents have remained stagnant** since the start of the pandemic, although net effective rents have averaged $61.03 due to higher concession packages, an 11.3% increase from Q3 2021.
- Tenant-friendly market conditions are supported by record free rent and tenant improvements with escalations for **total allowances rising 7.1%** since the beginning of 2021.

Capital markets

- DC Office **investment activity retreats to $2.68B, the lowest since 2017,** as investors are attracted to the sector fundamentals outside of DC - largely in emerging markets outside the region.
- Office investors are **shifting to less risky asset types** including multifamily, lab, and industrial opportunities south of the DC-region.
- Large trophy assets in DC sold in 2021, returning total office asset pricing to **pre-Covid levels at $593 psf**, although investors still face additional headwinds in the sector.

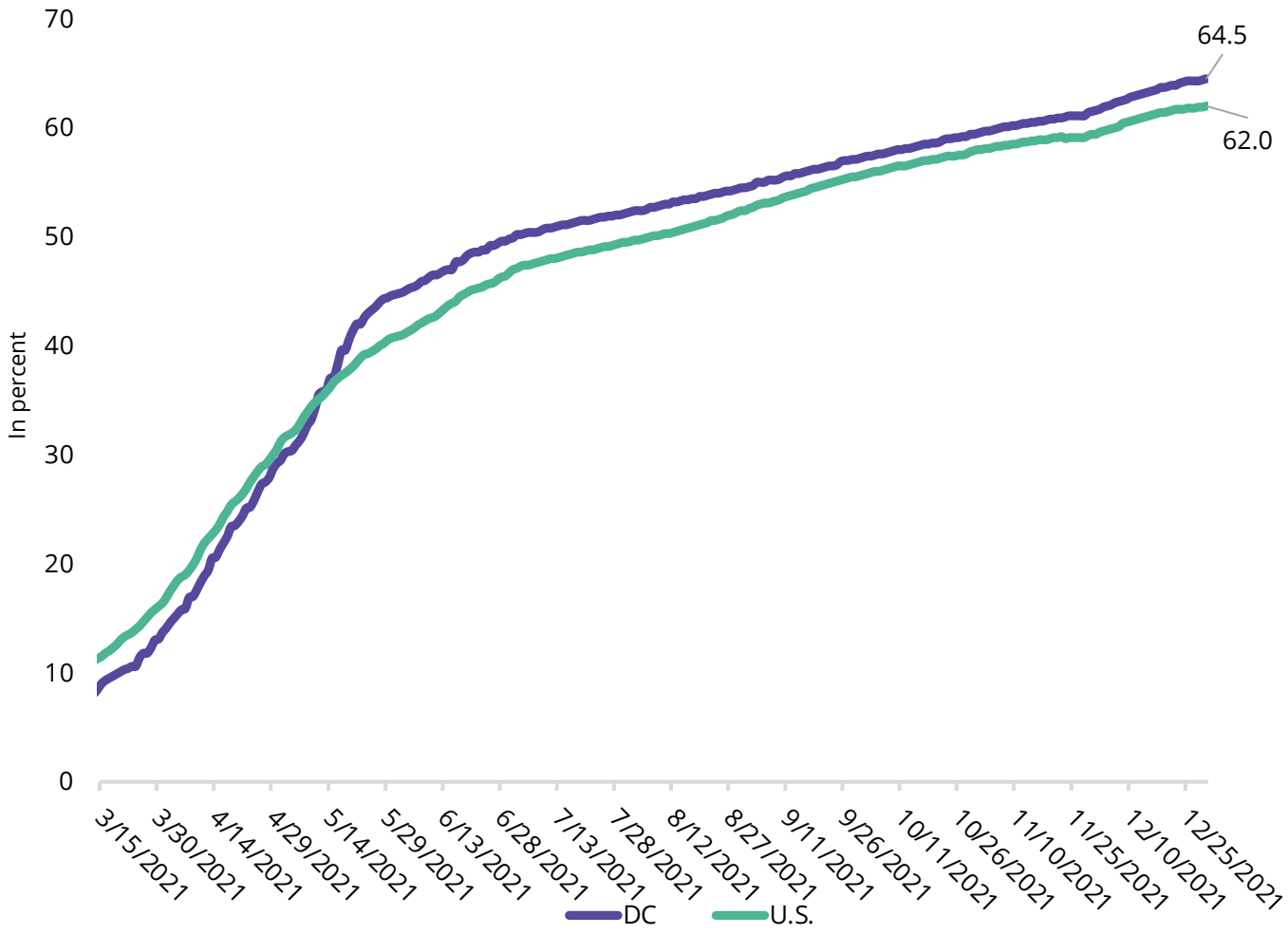
Let's review some key economic and demographic trends

Vaccination rates across population

64.5%

Share of total District of Columbia population that is fully vaccinated.

Through year-end 2021, DC proportionate vaccination rates have mildly surpassed the U.S. average of 62%, an important metric that has allowed the city to determine reopening efforts.



Source: Center for Disease Control

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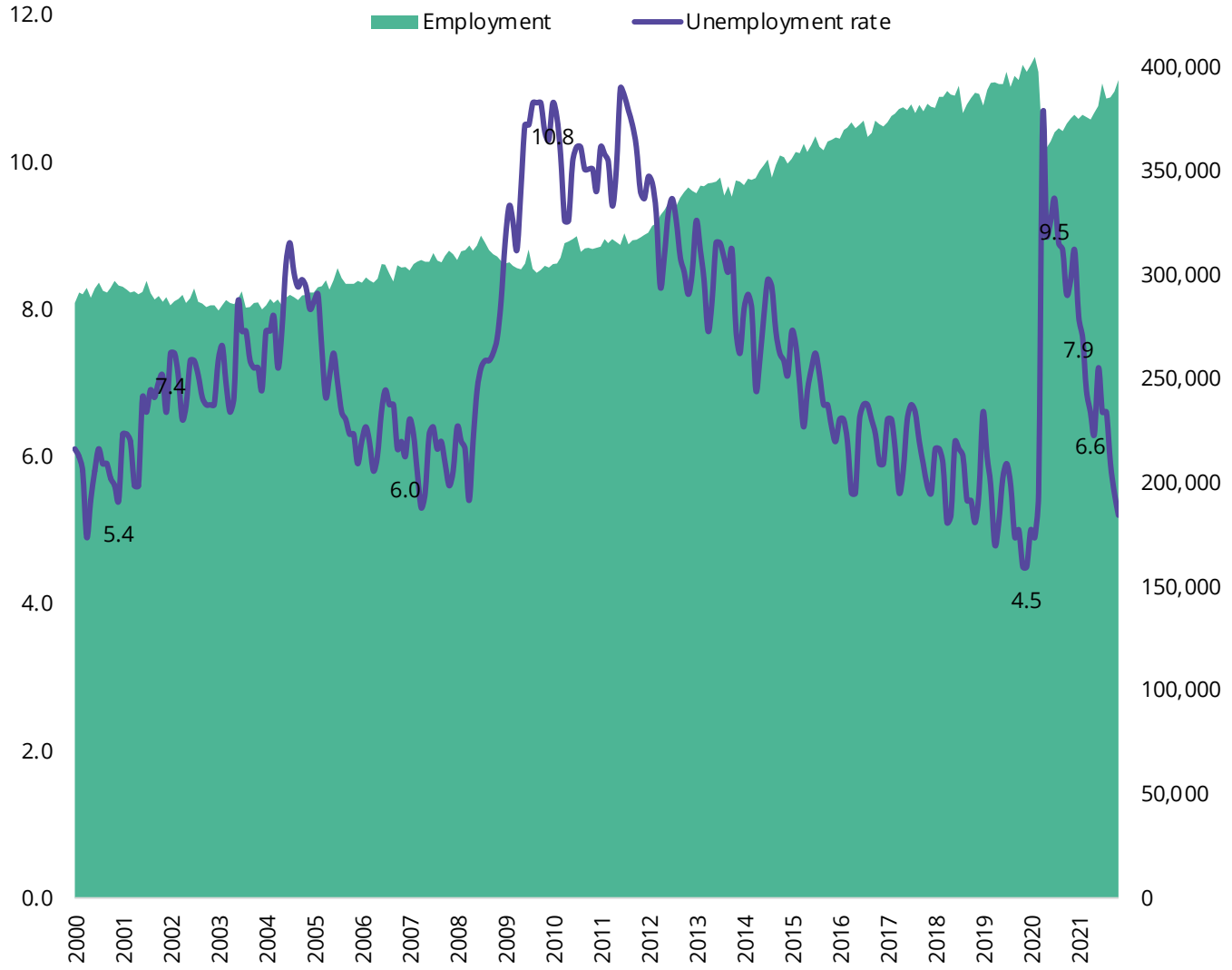
Employment and unemployment rate

5.2%

District of Columbia unemployment rate as of November 2021.

DC's labor market outperformed others due to its large federal presence that led to net job gains during the pandemic. This is largely attributed to large amounts of government-backed spending including emergency expenditures.



Source: Bureau of Labor Statistics

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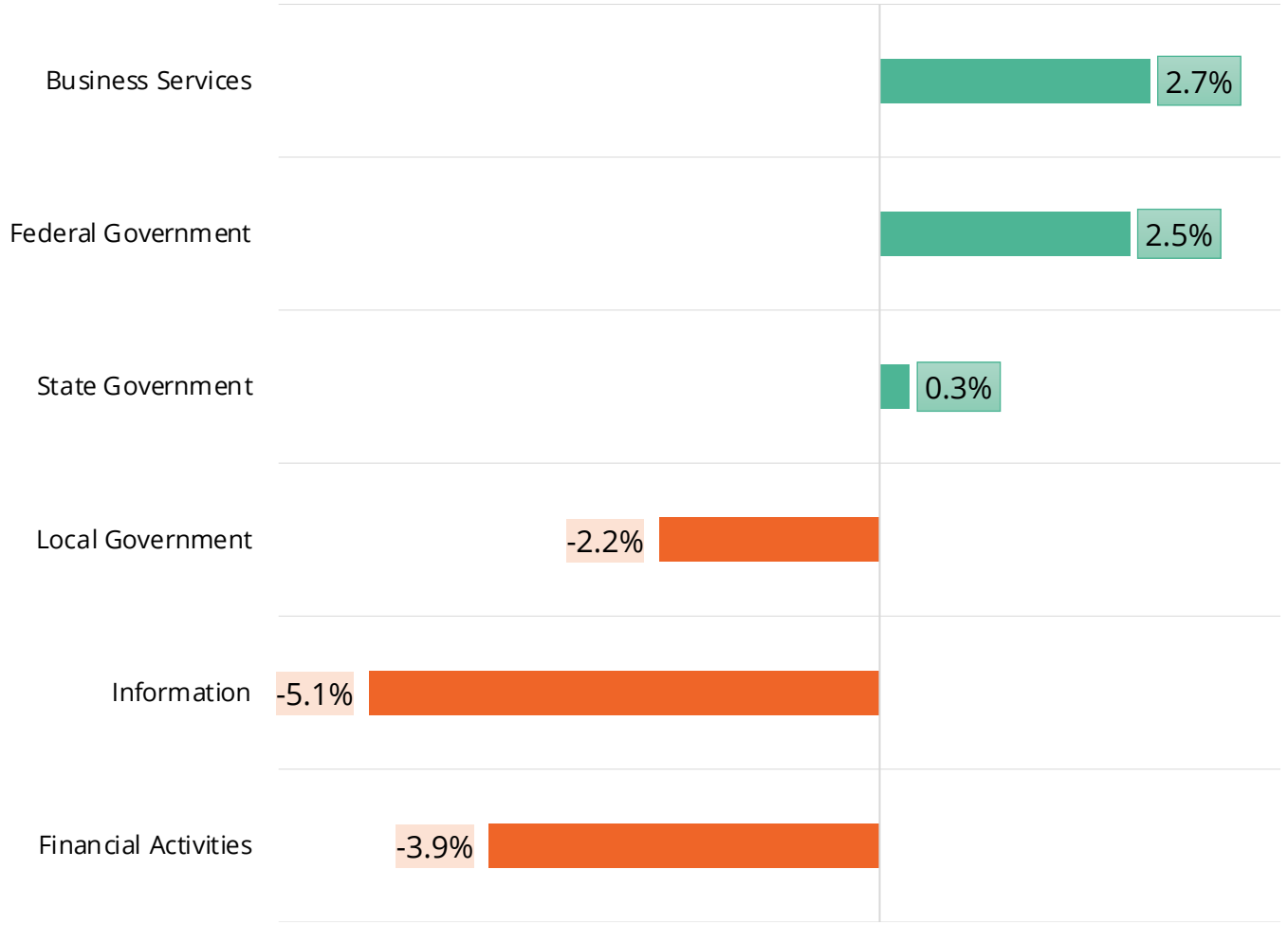
Office-using job gains and losses

+3.9%

Change in office-using employment over the past 12-months.

DC job losses have been felt most across leisure and hospitality (-13.7%), financial activities (-3.9%), and information industries (-5.1%). Since the onset of the pandemic in Feb 2020, overall employment has declined 2.1% in the District of Columbia, although bolstered by the presence of Federal Government.

Washington, DC Metropolitan Statistical Area
February 2020 to October 2021



Source: Bureau of Labor Statistics

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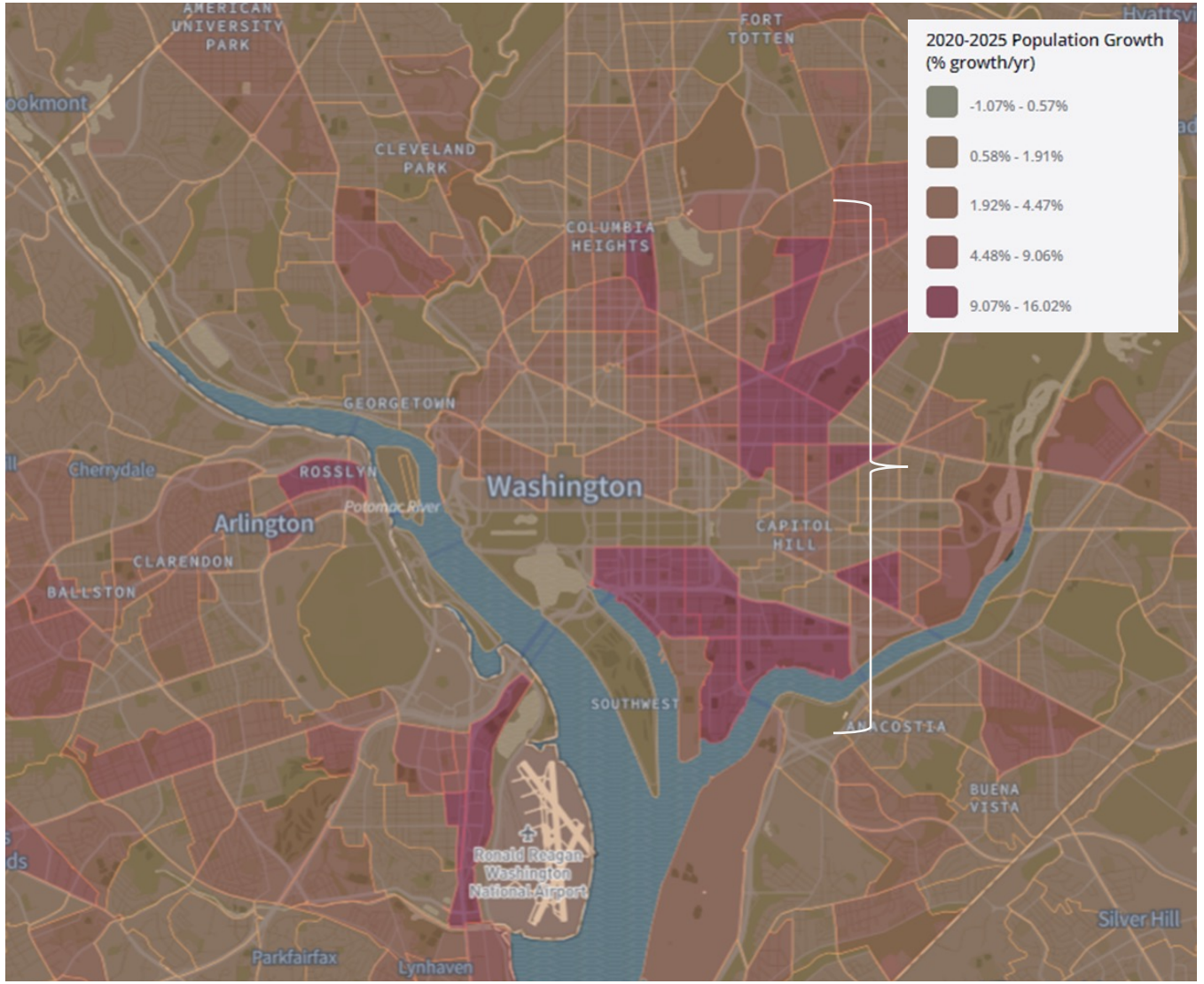
2020-2025 population Growth migrates East

With better affordability options and access to a variety of newly constructed amenities, residents are migrating east of the city center to the Capital Riverfront and Union Market areas in search of recently delivered residential options while working remotely.



Source: AVANT Cities. ESRI 2021.

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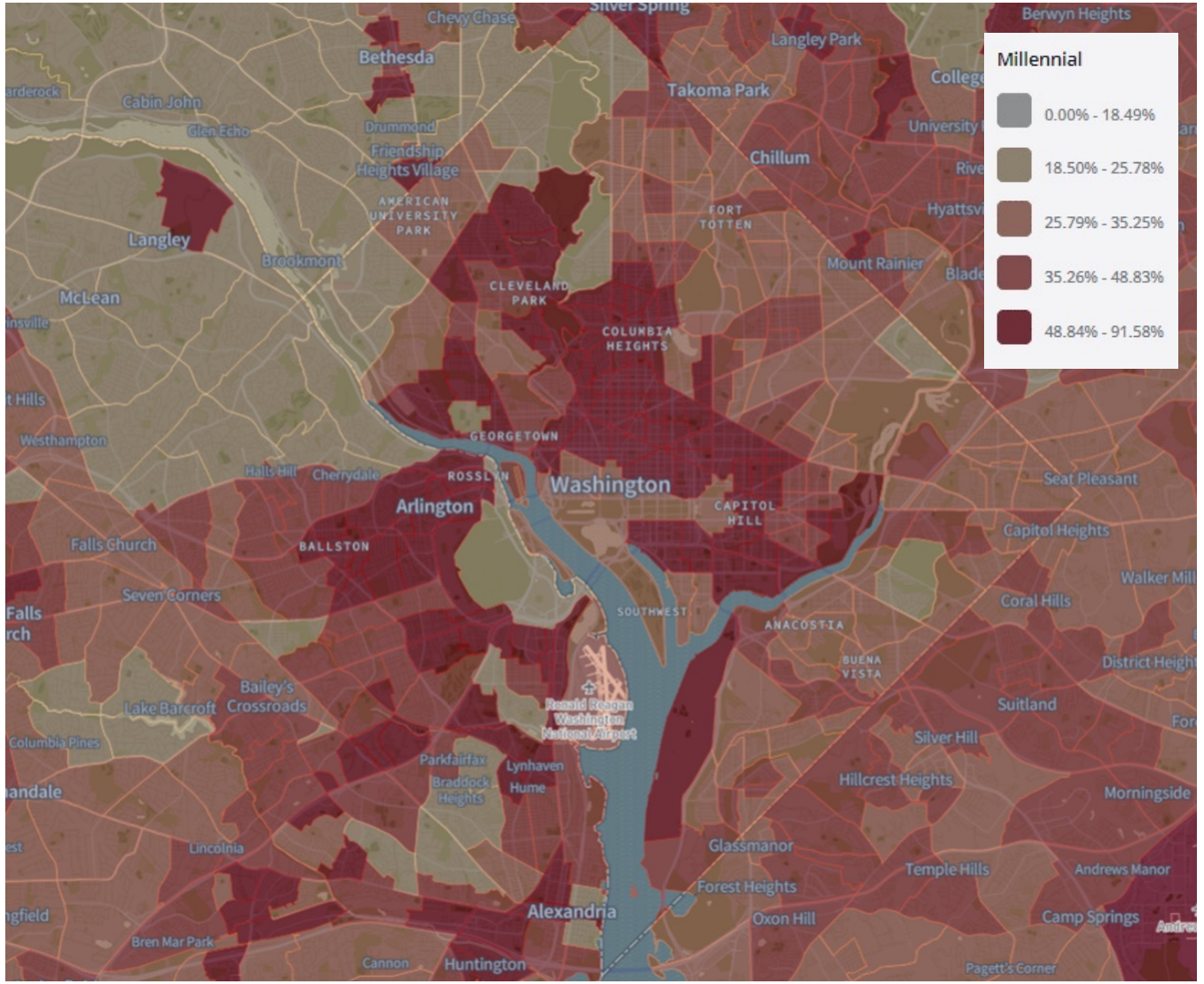
DC has largest concentration of millennials in the region

33.5% of the city's population are millennials, between the ages of 26-41, and account for a large portion of the workforce in the city.

Many companies return-to-work strategies are adapting given investments, partially due to COVID-19 restrictions, into remote-work technologies to recruit from this generation for jobs.



Source: AVANT Cities. ESRI 2021.

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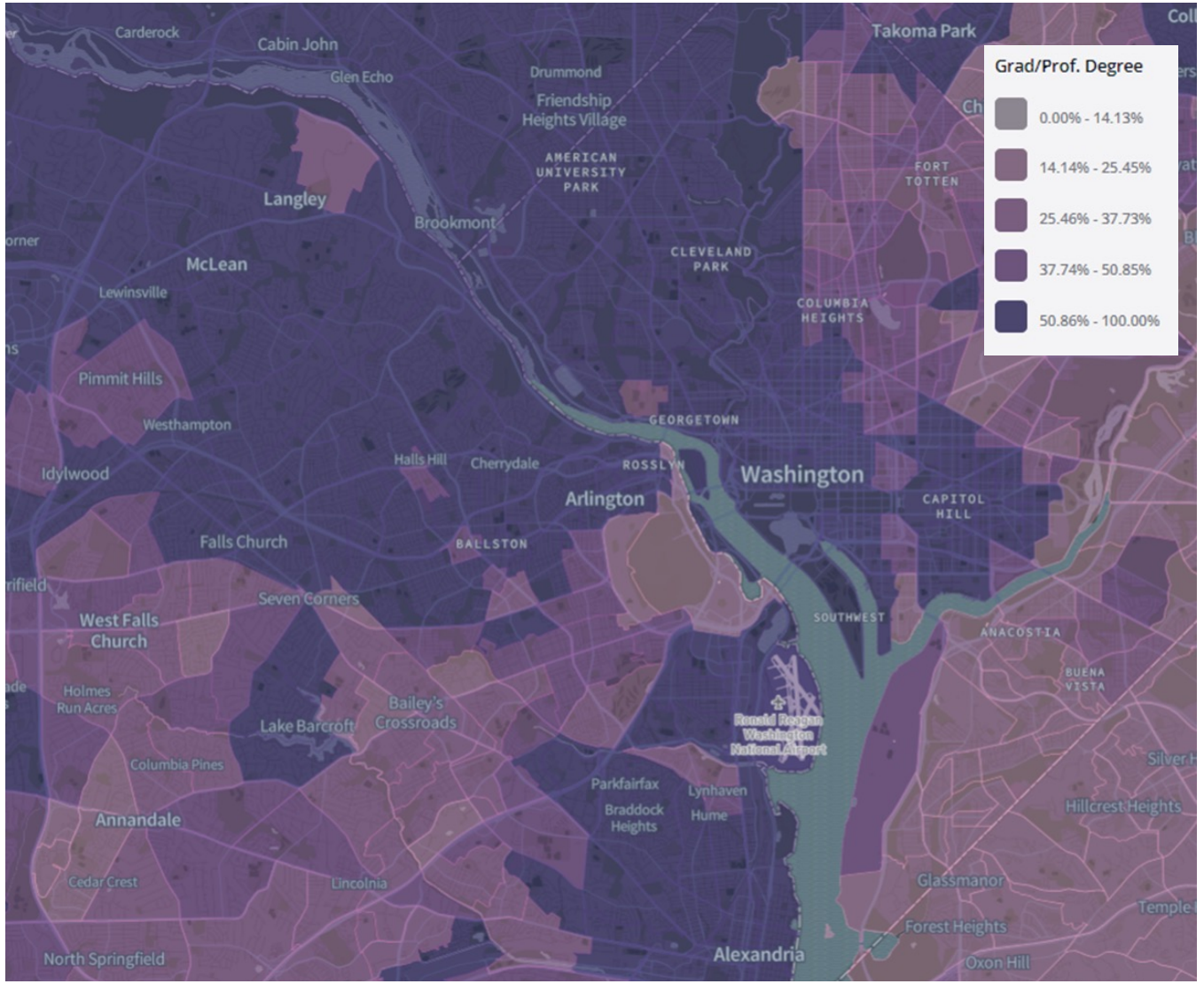
High percentage of Graduate & Professional Degrees

Washington, DC remains an attractive market to do business due to the large per capita of the population that have attained graduate and professional degrees.

The District has a highly educated workforce with over 173,300, or 24.6% of the population, having attained secondary level education.



Source: AVANT Cities. ESRI 2021.

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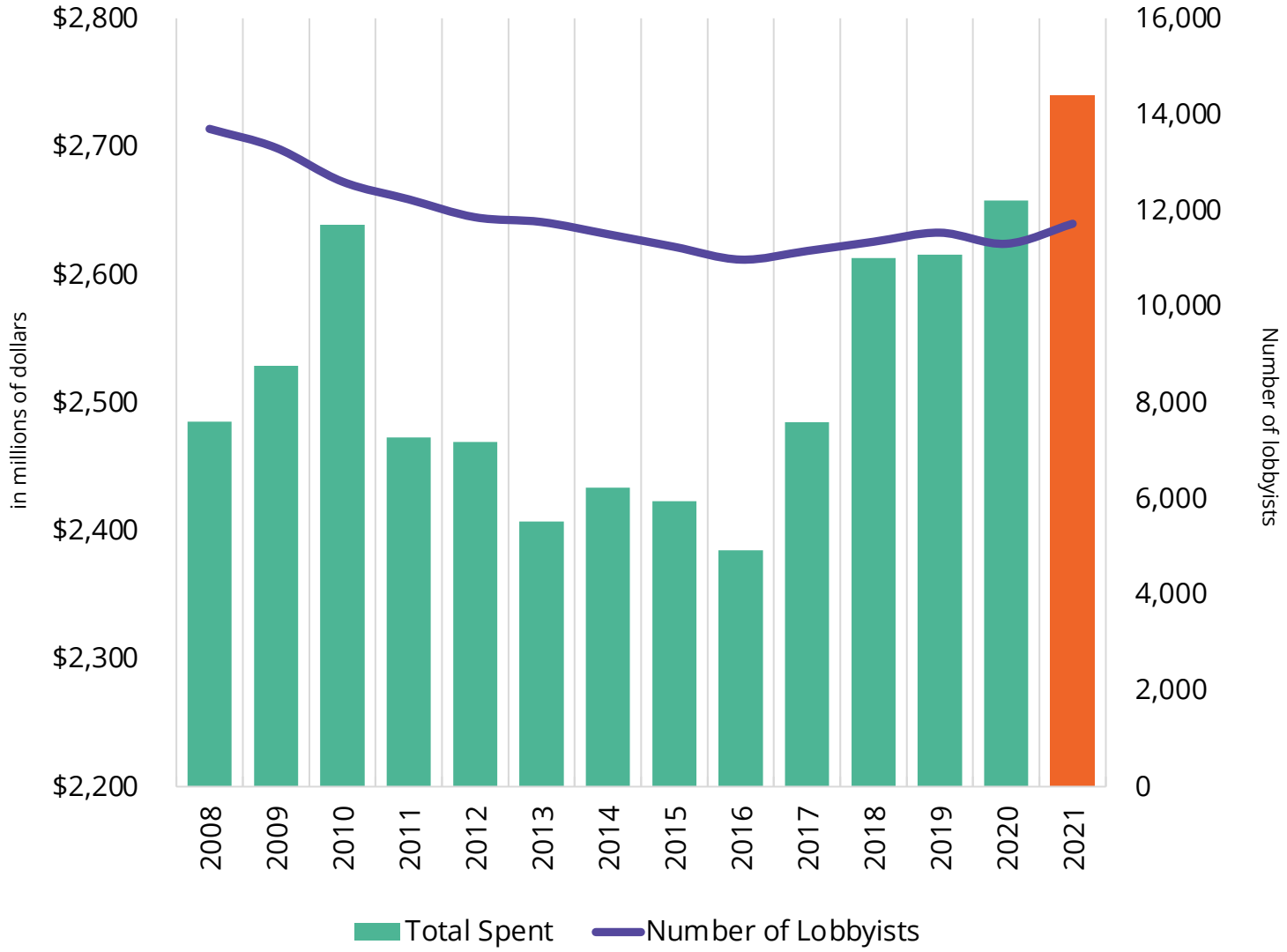
Lobbying dollars increases to all-time high

Total 2021 lobbying dollars spent was **$2.49 billion and is the largest sum** on an annual basis going back to 2008.

The total number of **registered lobbyists has risen slightly to 11,722** from last year and has helped stimulate demand in the office market in the DC region.



Source: AVANT by Avison Young. Open Secrets.

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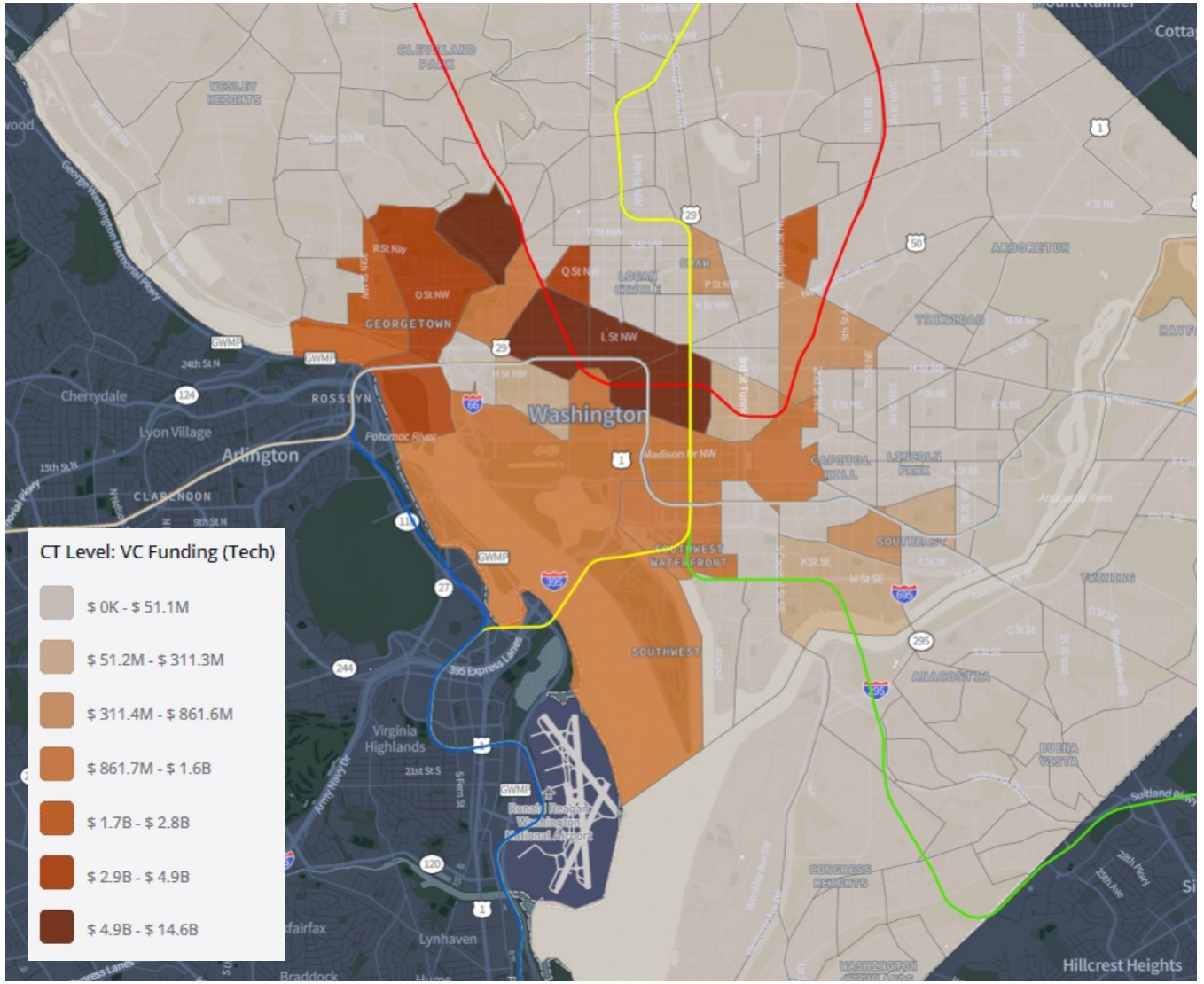
DC core concentrations of venture capital funding in technology

Venture Capital funding in technology companies is highest in the Central Business District and northwest towards Georgetown.

The concentration of investments follows a trend along major metro lines, showing the benefits of a transit-oriented office and residential opportunities.



Source: AVANT Cities. ESRI 2021. WMATA.

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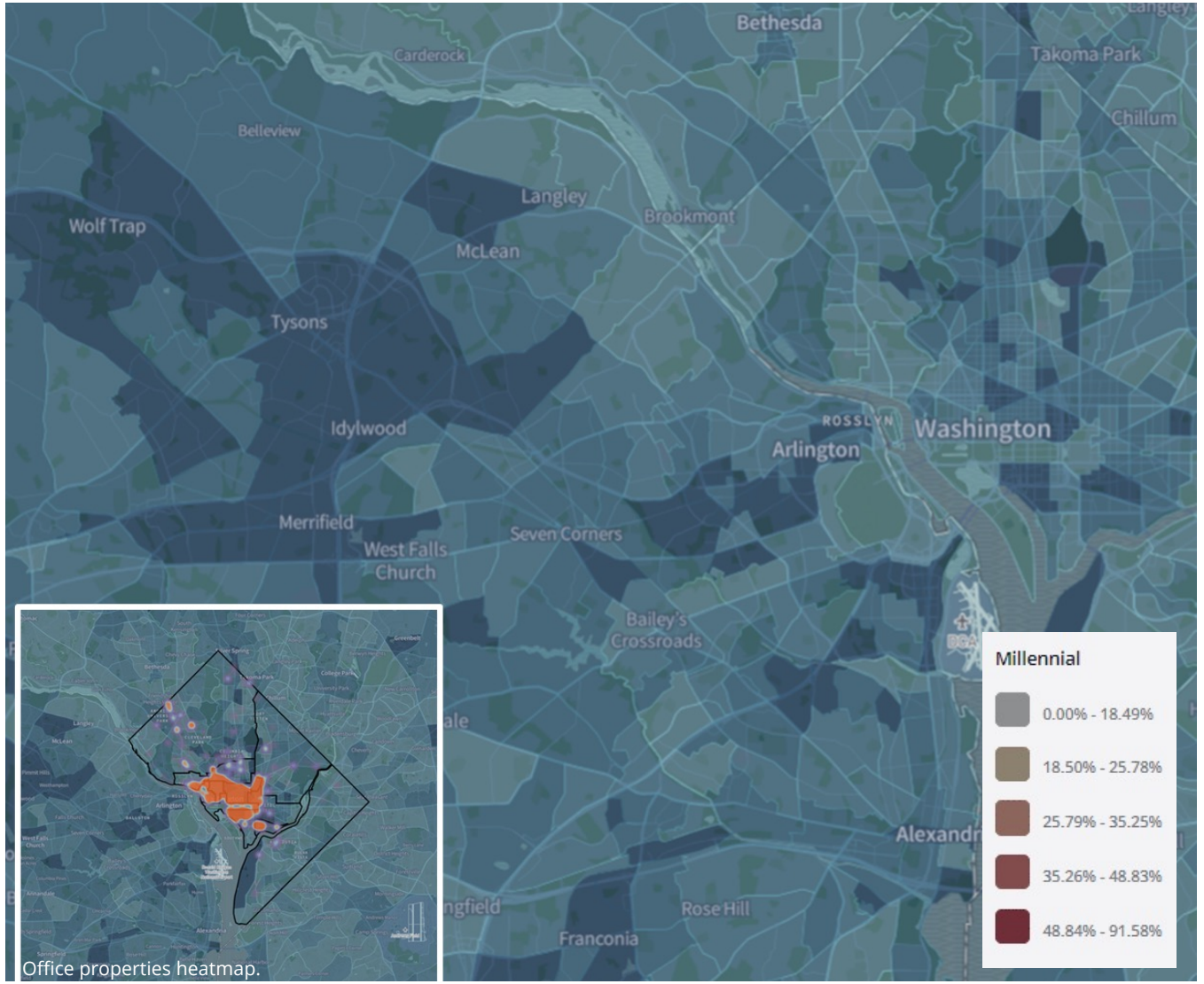
Technology workforce in the DC-metro

With the emergence of technology companies in the region, and the battle for talent, the highest concentration of technology jobs cluster around the DC-metro region.

Although, submarkets including the Rosslyn-Ballston Corridor, and along the Dulles Toll Road, offer more attractive real estate options for employees due to lower apartment rents and cost of living.



Office properties heatmap.

Source: AVANT Cities. ESRI 2021.

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

-69.6%

Office visitor volumes, week of December 13, 2021 vs. week of December 15, 2019.

Office visitor volumes have generally risen in recent months, particularly after Memorial Day and after Labor Day, but remain considerably lower than pre-pandemic levels. The next major litmus test for return-to-office efforts will be January 2022.

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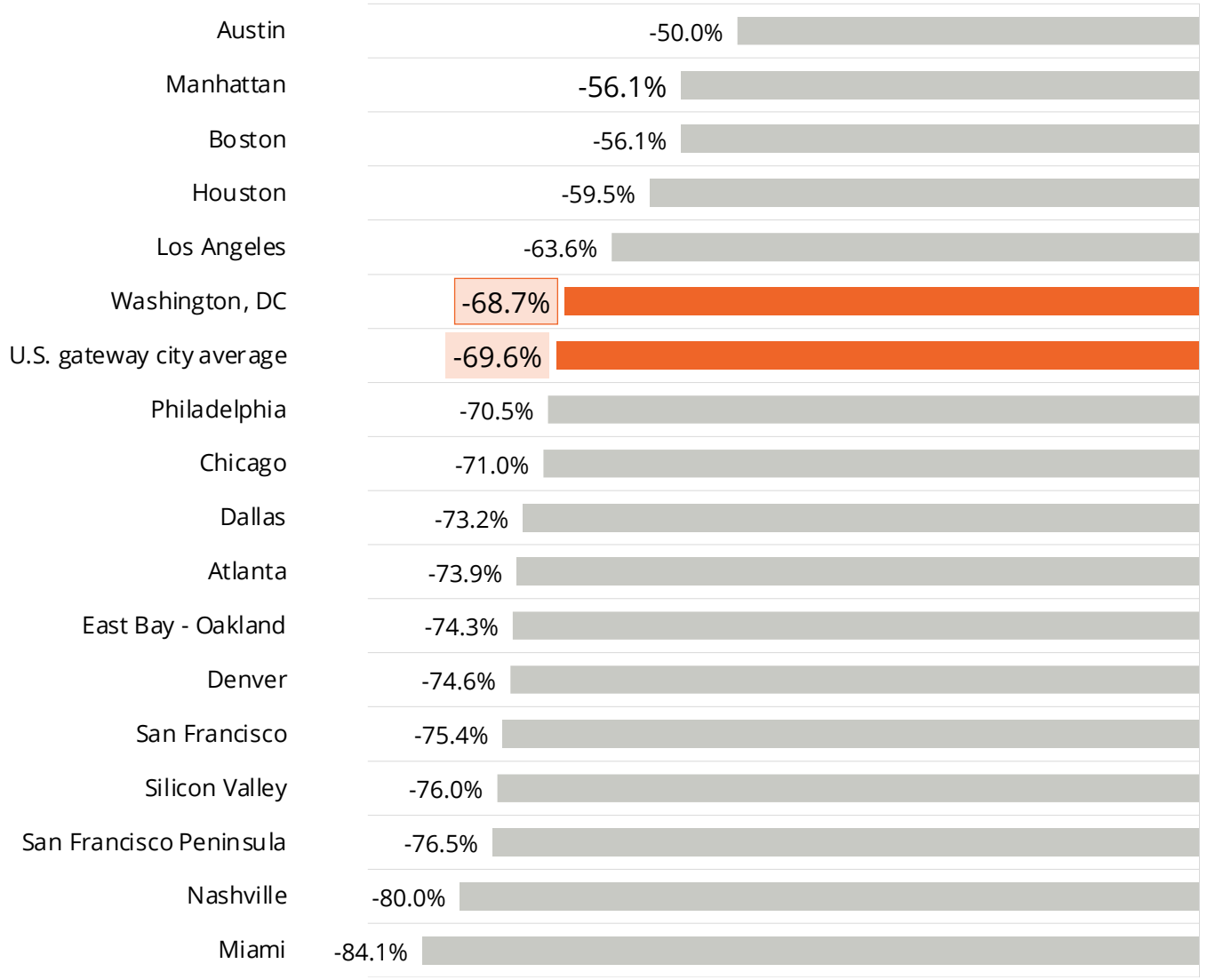

Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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

-71.1%

Tech office visitor volumes, week of December 13, 2021 vs. week of December 15, 2019.

Competitive labor market conditions and some employees' productivity outside of the office have caused many tech companies to adopt hybrid or remote work strategies.

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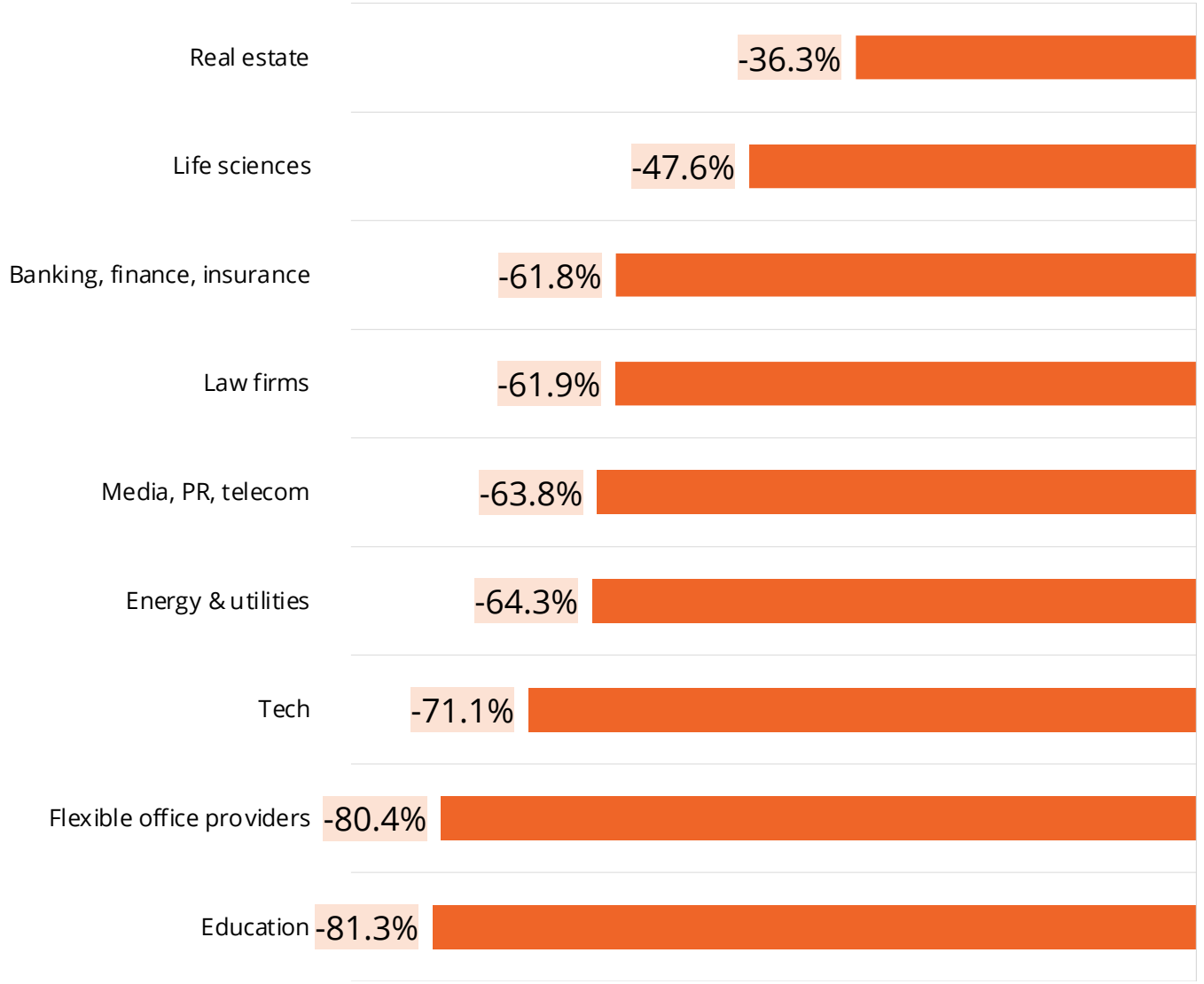

Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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Local return to work efforts by industry

-59%

Law Firm office visitor volume vs. December 11, 2019

Law firms have reinforced hybrid remote/in-person work schedules, though creative companies have adopted remote work strategies.

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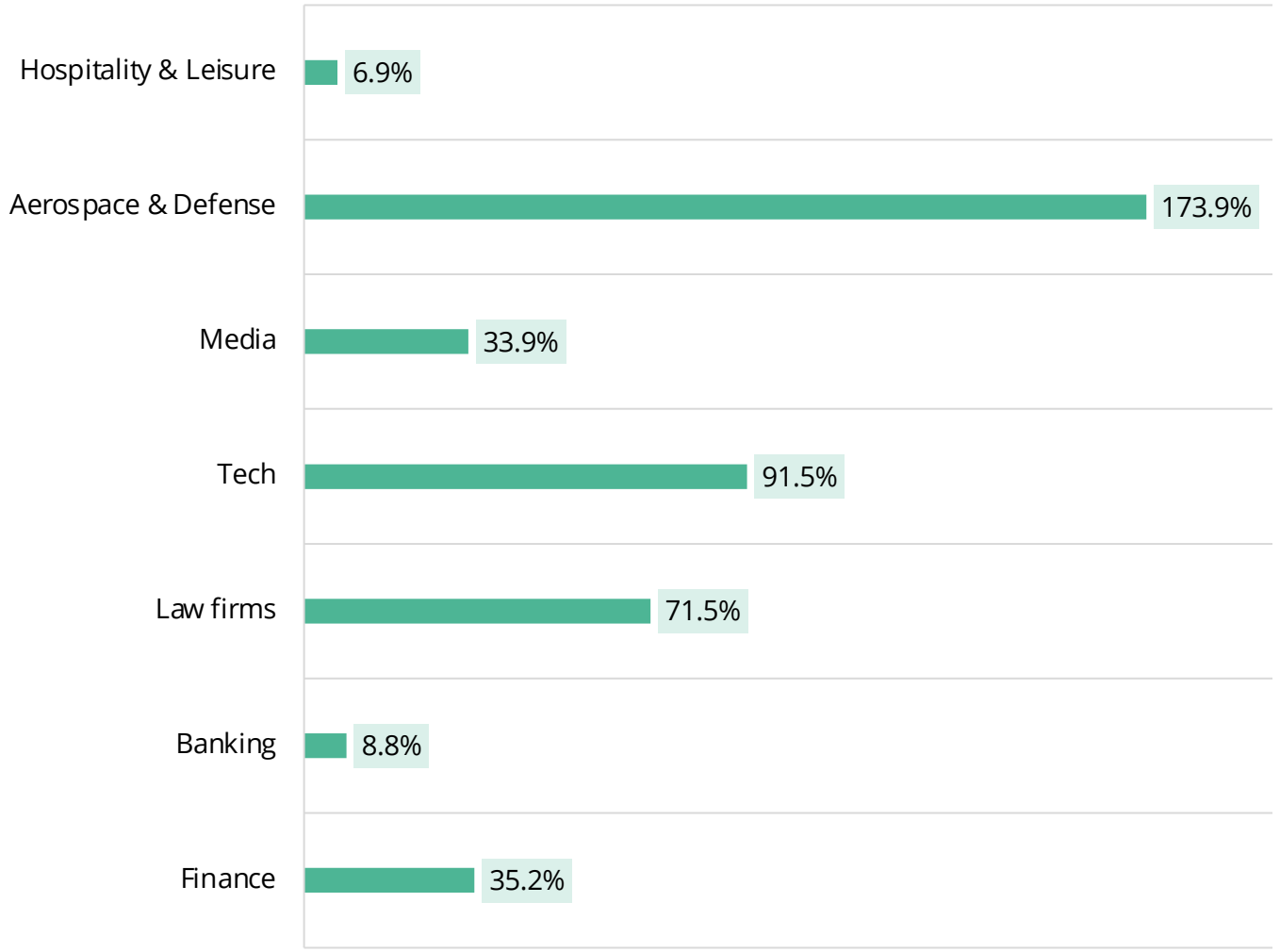

Note: Representative office locations. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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Local historical visitor volumes

-41.5%

Total visitor volume since March 2, 2020

Retail (+23.8%) returns to pre-covid activity levels while education (-79.1%) and office (-63%) sectors have lagged all other property types. Companies have been slower to return to the office due to investments in remote technologies and mitigating exposure to variants.

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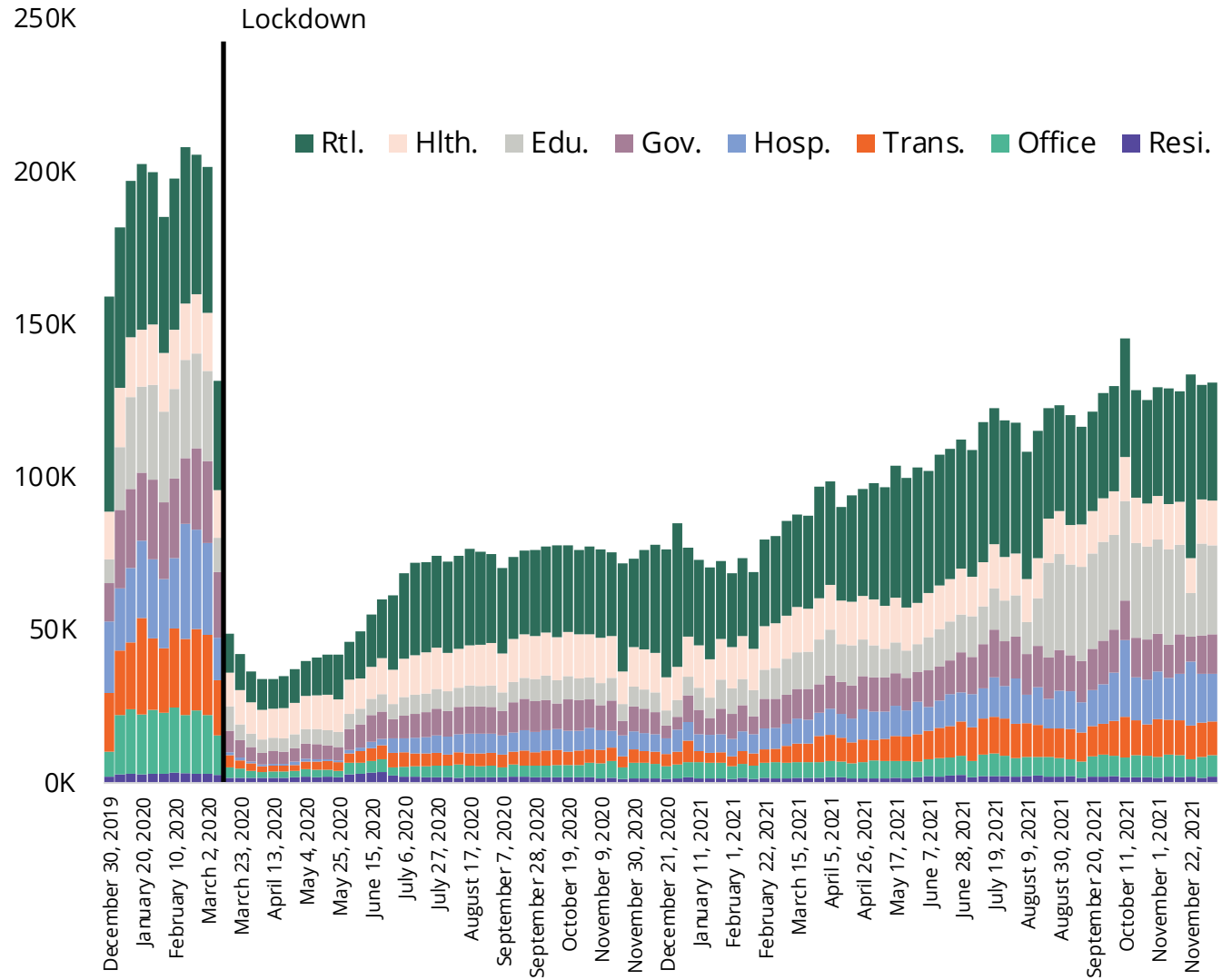

Note: Representative areas of interest. Weekdays only.
Source: Orbital Insight, AVANT by Avison Young

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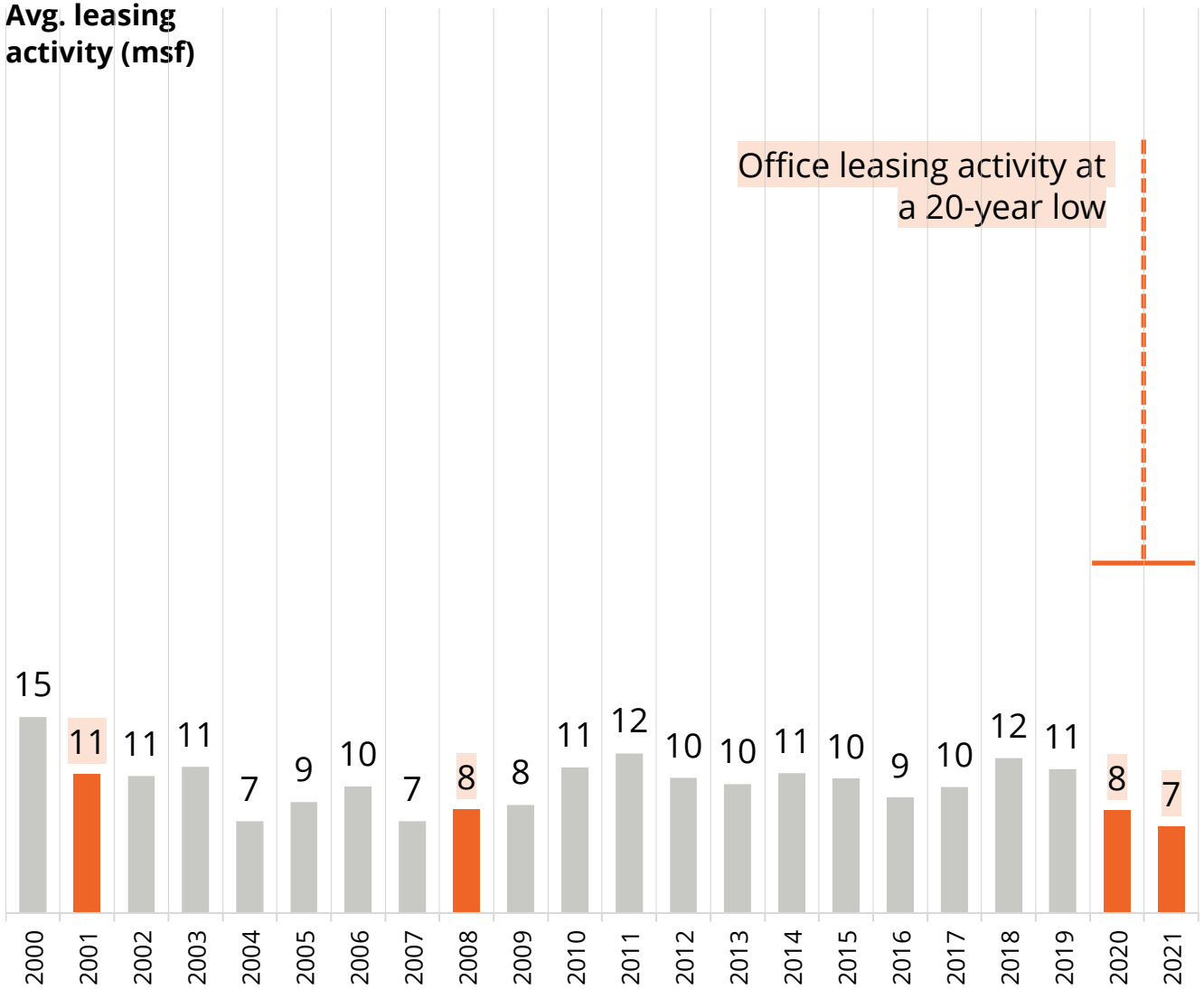
Let’s look at office occupier market conditions

Office leasing activity

-28.3%

2020 & 2021 Average leasing volume vs. prior 20-year annual average leasing volume

There is no modern precedent for the post-COVID slowdown in leasing activity including both 2001 & 2008 downturns. The lack of activity can be attributed to the sudden change in office occupier's workplace strategies and the 2020 recession.



Source: CoStar

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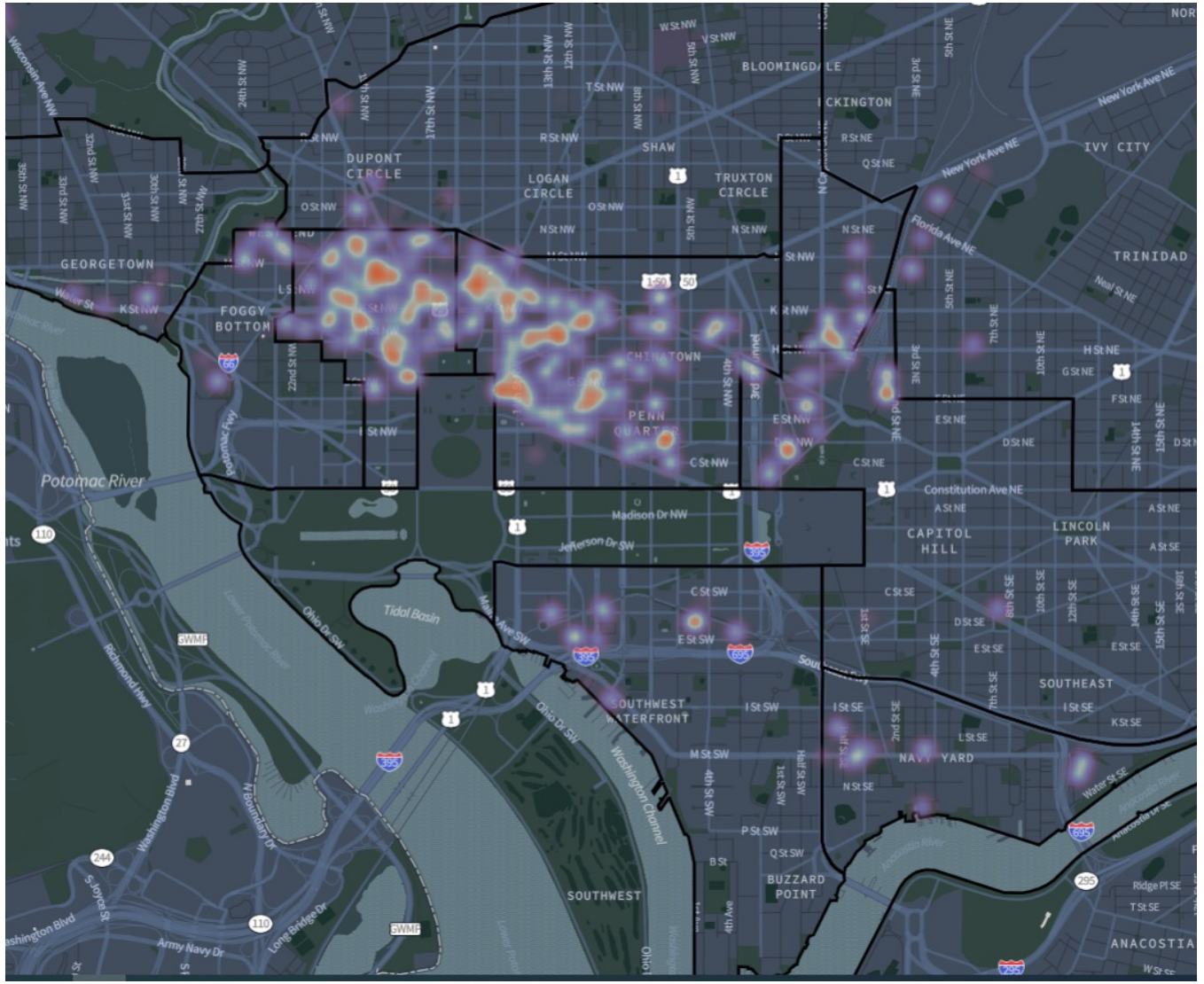
Office leasing activity: velocity across the downtown

DC has experienced the most leasing activity for deals over 10k square feet in the central business district that includes DowntownDC and Golden Triangle.

Current trends show increased attention and deal flow is occurring in the Union Market and Southwest Waterfront neighborhoods over the past 36 months.



Source: AVANT
Note: Existing office leased in past 36 months >10k sqft.

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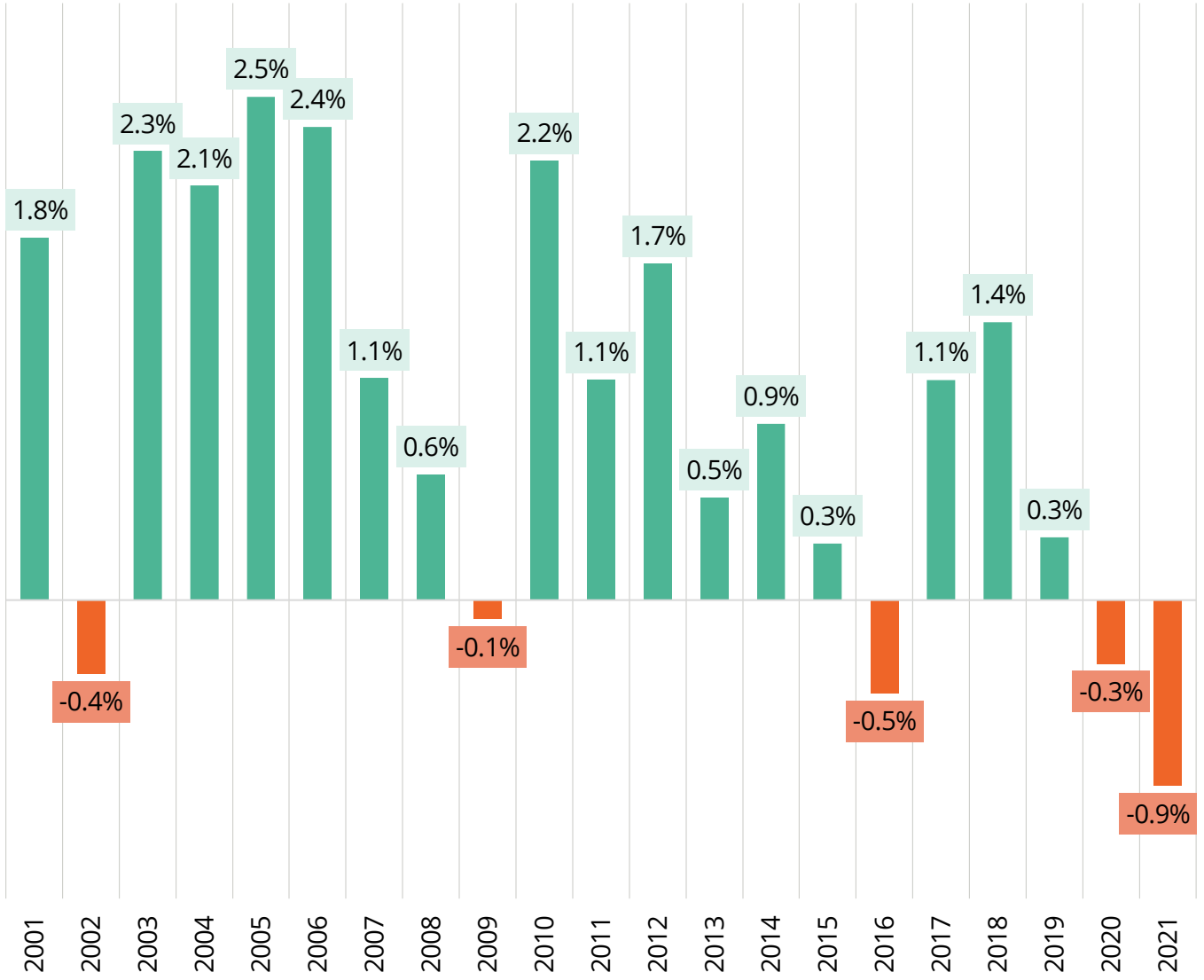
Absorption as a share of inventory

-1.2%

Net absorption as a percentage of inventory, 2020 through 2021.

Negative absorption continued throughout the remainder of 2021 ending with -1.37 msf, which is the most relative to inventory since 2016. While touring and leasing velocity has picked up in Q4 2021, it has not yet converted into deal activity and likely signals an uptick in future demand.



Source: CoStar

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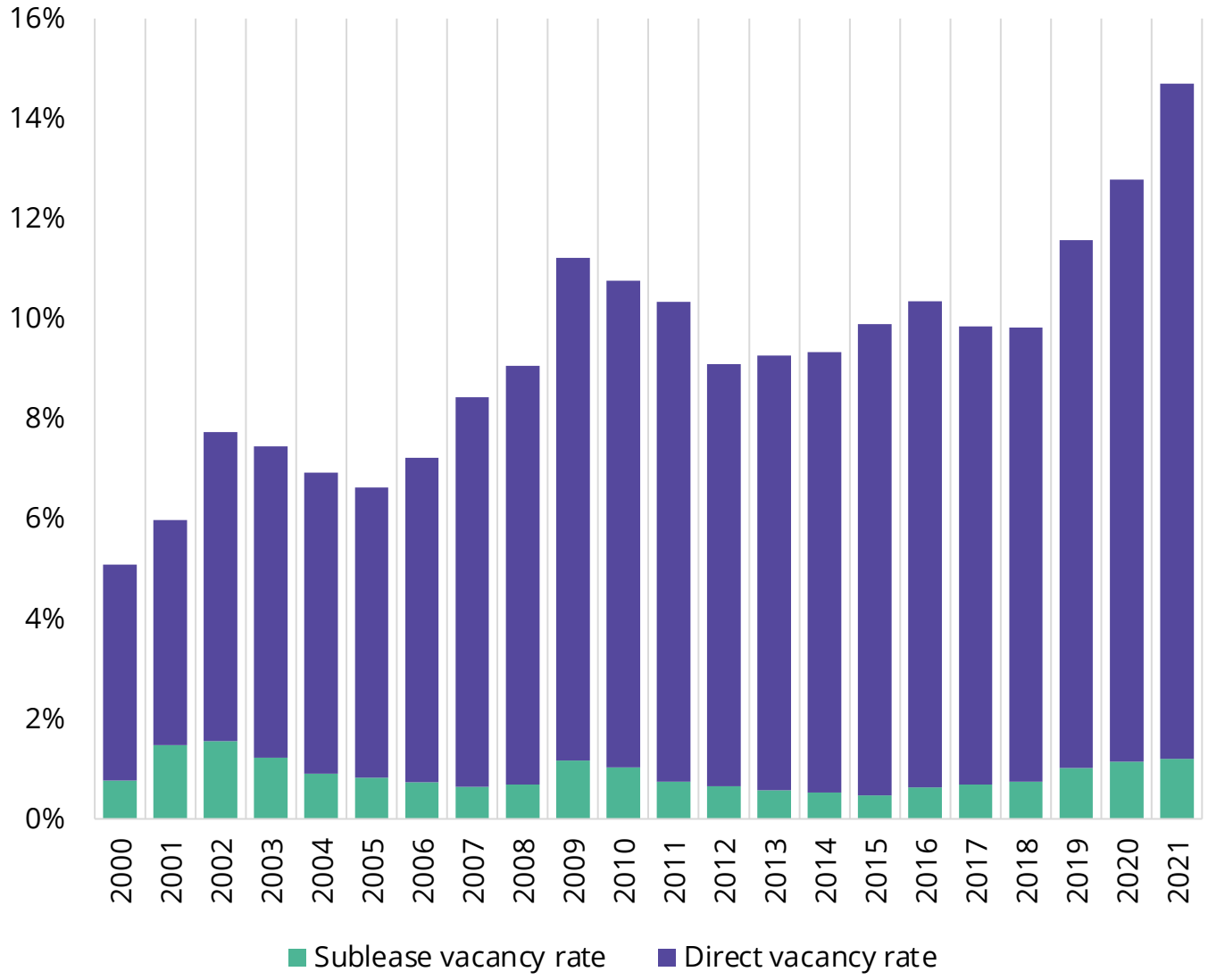
Office market vacancy rate

14.7%

Record high DC office vacancy rate as of Q4 2021.

Direct vacancy rates in the District of Columbia stand at 13.5%, tracing past all-time highs set previously in 2021. With office occupiers taking on less square footage due to investments in remote-work technologies, combined with a flight-to-quality, overall vacancies should continue to rise into next year.



Source: AVANT by Avison Young

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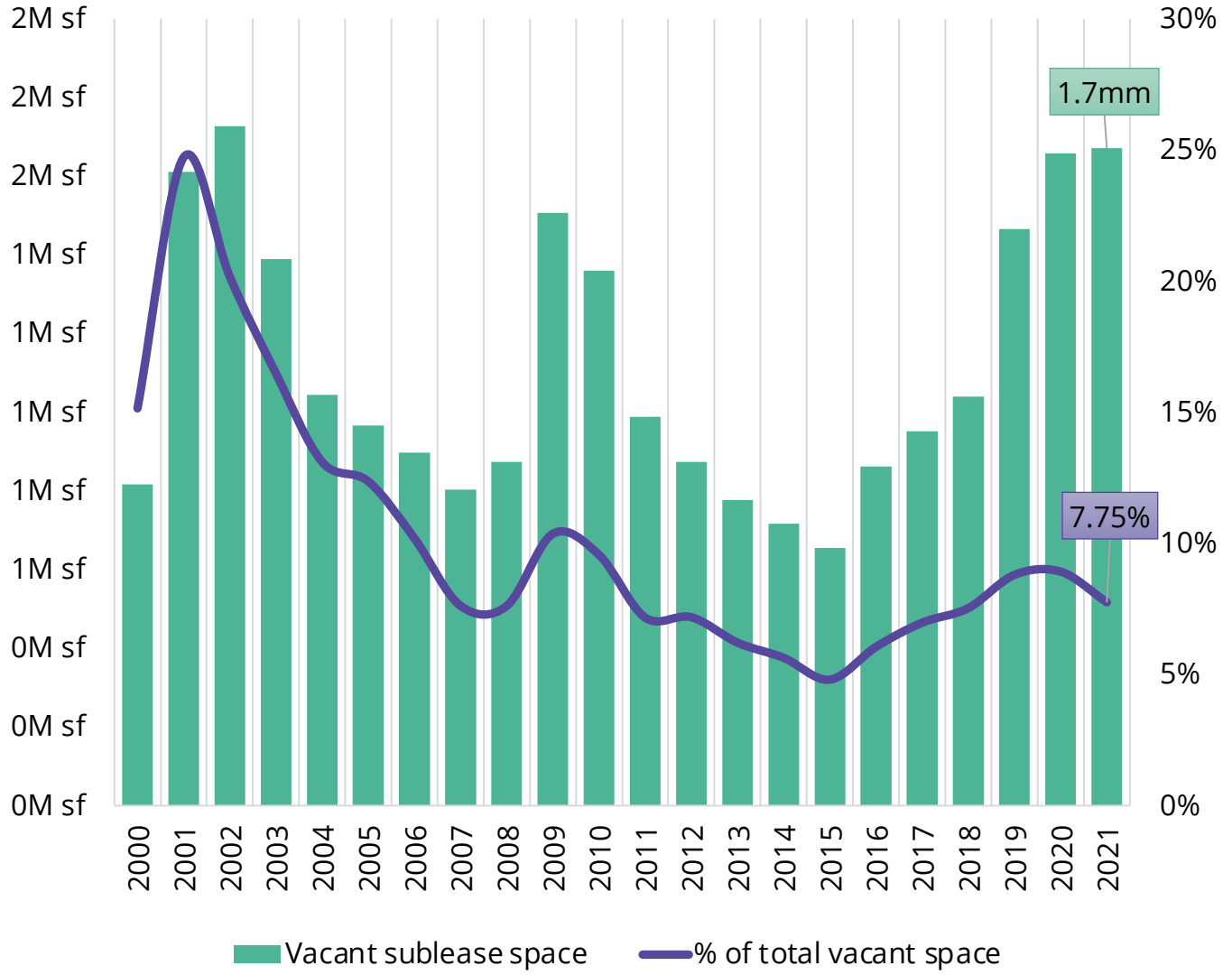
Vacant sublease space

1.7 msf

Declining levels of available sublet space in the District of Columbia.

The share of sublease-to-total vacant space of 7.75% has begun to decline when compared to 2019-2020 by roughly 100 basis points where it reached all-time highs close to 9%, though still well below highs reached during 9/11.



Source: AVANT by Avison Young

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Office development pipeline

20 properties

Under construction or Renovation

5.2 msf

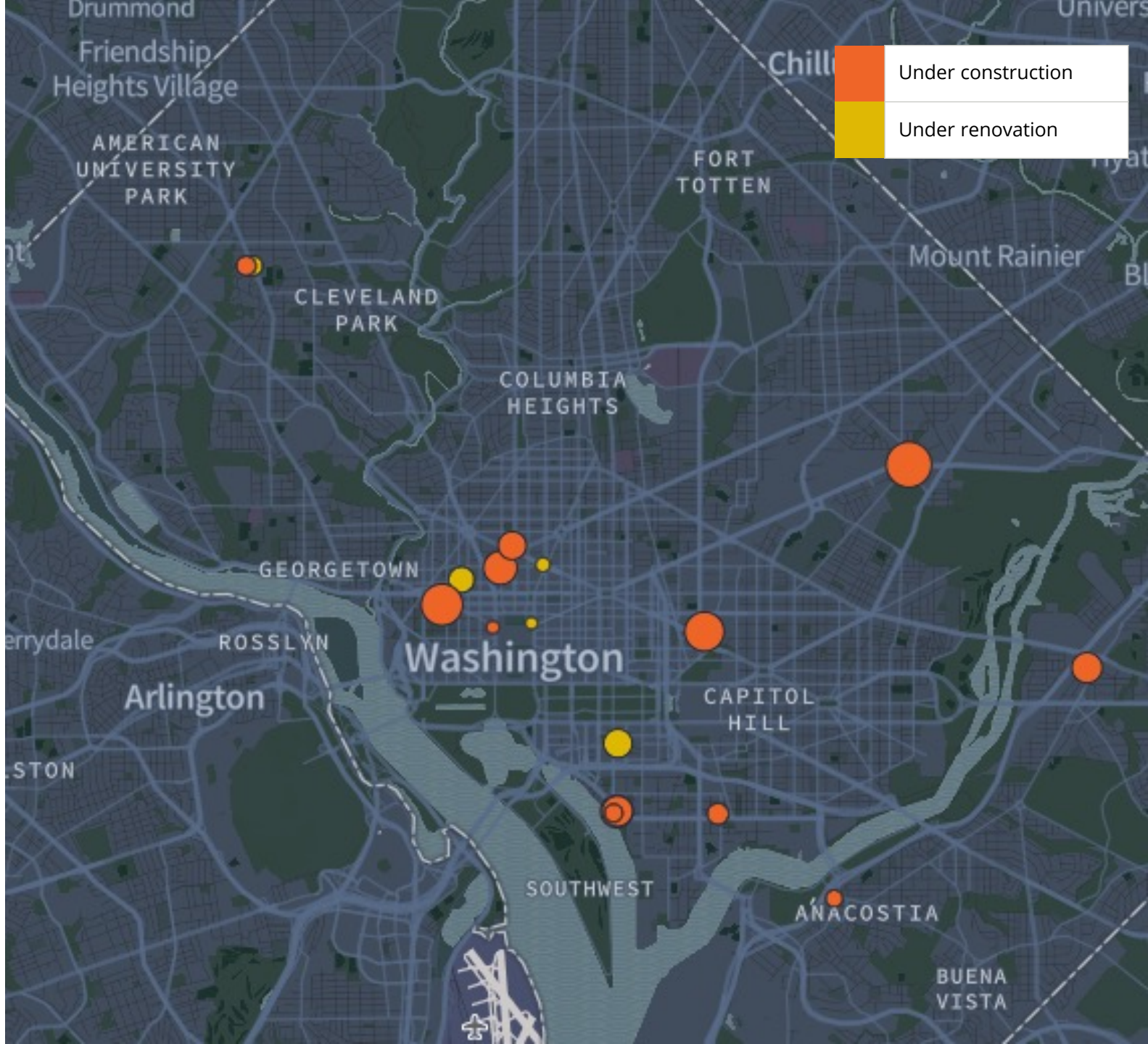
proposed, under construction

2.8%

share of office inventory

1969

average delivery date of DC offices

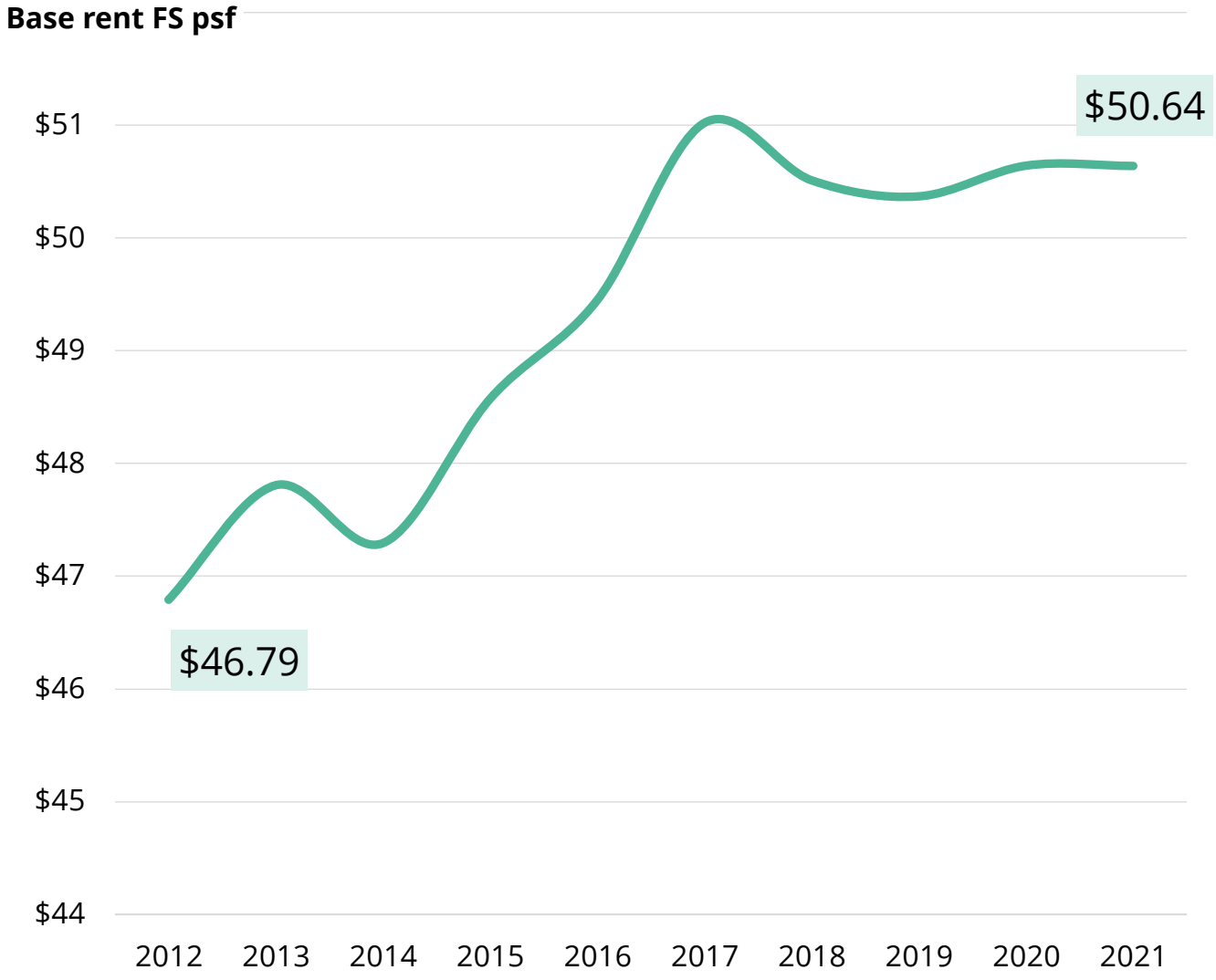


Office base rental rates

Flat

Change in base rental rates, year-to-date 2021.

While Net Effective Rents increased slightly month-over-month in 2021, base rents have remained consistent and landlords have had to be more aggressive with their concession packages to lure tenants due to uncertainties in the market.



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

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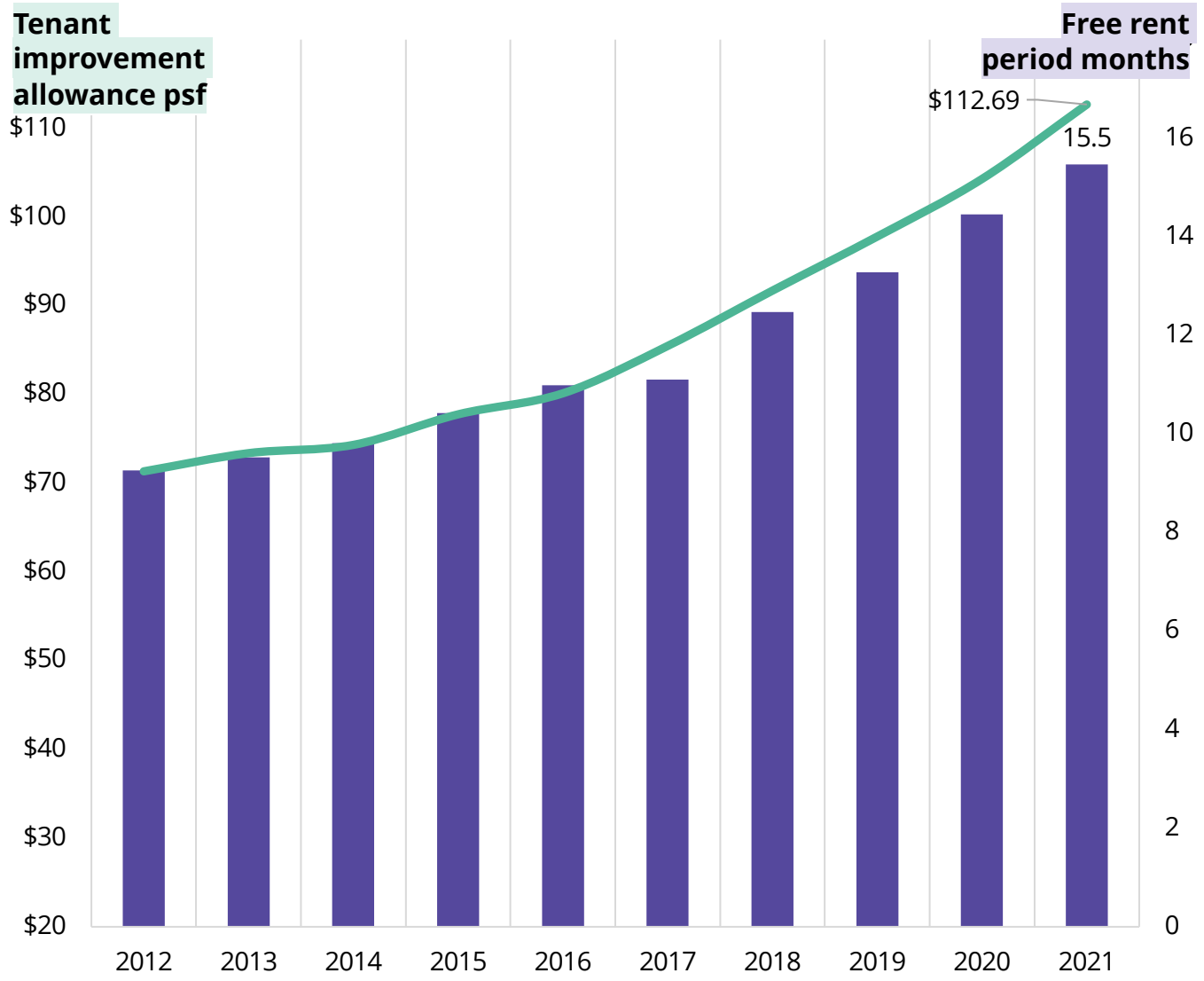
Office tenant concessions

+8.04%

Change in tenant improvement allowance amounts compared to 2020.

Tenant improvement allowances and free rent periods continue to reach all time highs, driven mostly by suppressed leasing velocity due to the ongoing pandemic.



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

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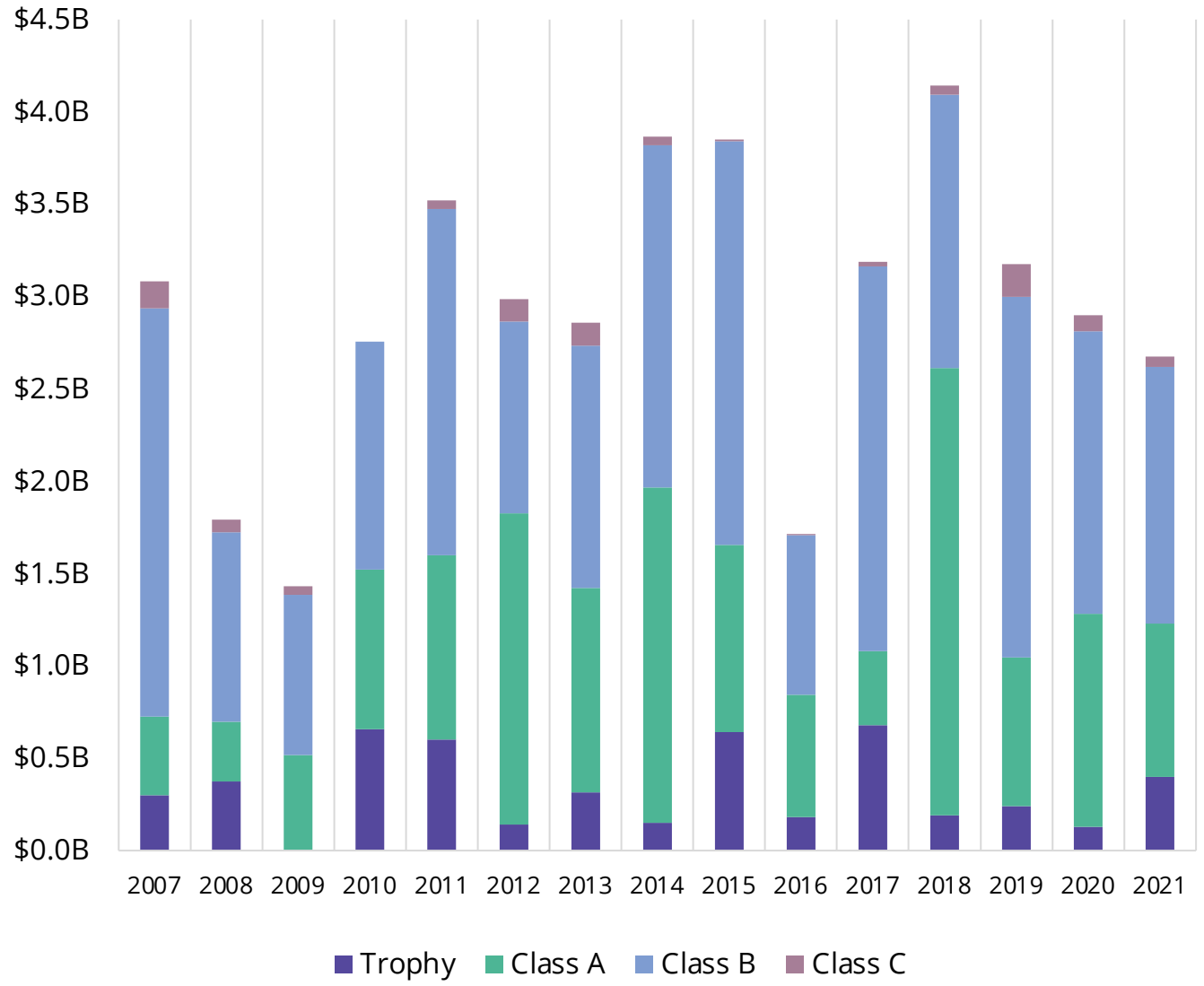
Let’s look at capital markets conditions

Office investment dollar volume

$2.68B

Total DC office investment volume declines in 2021

Office sales activity has temporarily paused during the pandemic, decreasing by a rate of 11.5% when compared to the annualized prior five-year average dollar volume. However, GSA leased assets have continued to draw the interest of investors favoring safer, more stable investments.



Source: AVANT by Avison Young

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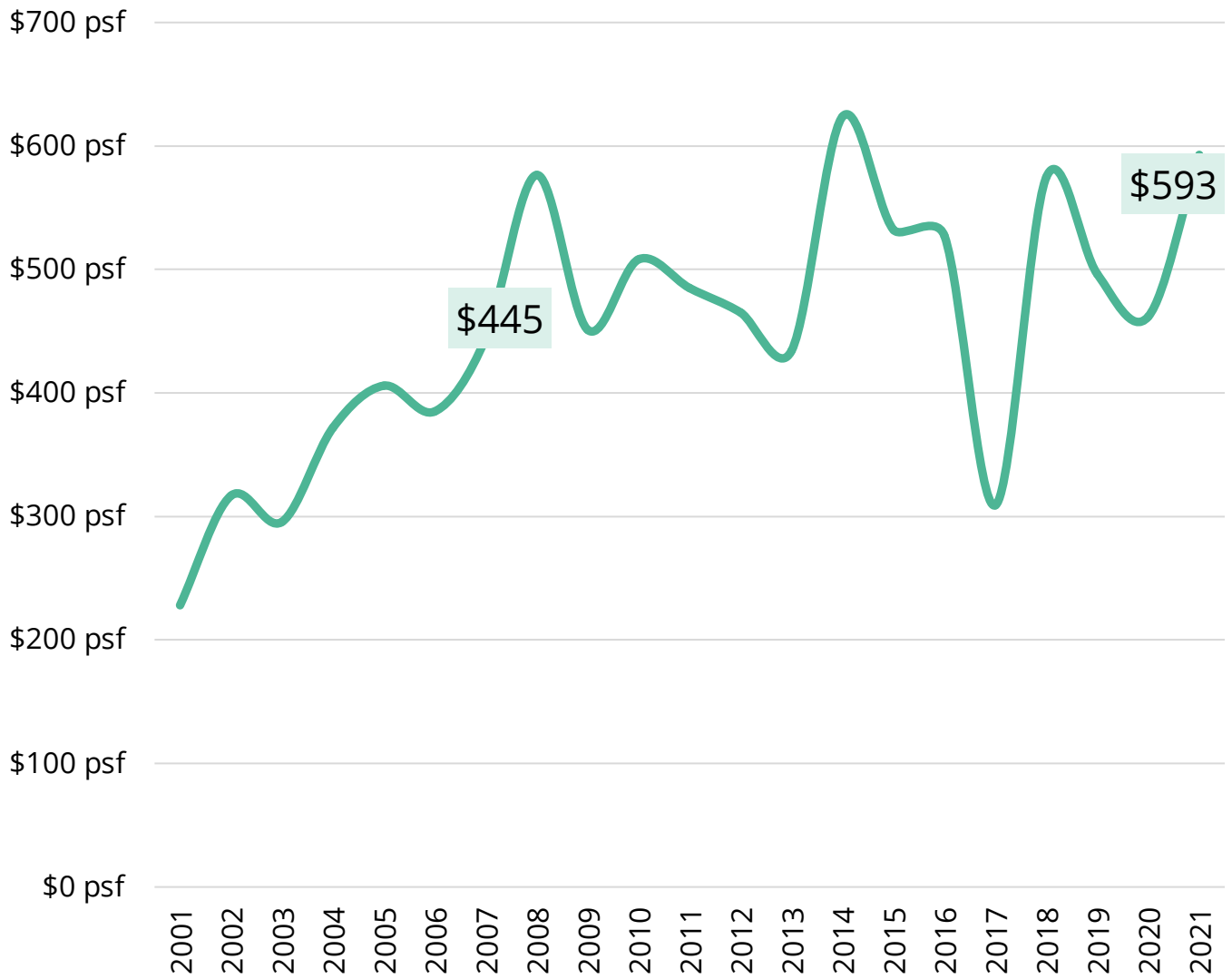
Office asset pricing

+28.4%

Rebound in DC office asset prices when compared to 2020

Even as Investors have adopted more conservative approaches to underwriting, asset pricing has trended incrementally upward in recent months, indicating a potential pathway to additional stabilization.

Pricing has returned from pandemic lows as large trophy assets traded hands in 2021 and are driving higher overall market prices to $593 psf vs. recent years.



Source: AVANT by Avison Young

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Now, let's see what we can expect looking forward

Here's what we can expect looking forward

- **Compressions in base rents** between higher end and commodity office product has accelerated the flight to quality seen throughout 2021. Office users have reduced their space requirements due to investments in remote technologies that have enabled employers to allocate the same budget, or less, for monthly rents.
- **Office investment dollar volume** continues to decline into 2022 as investors flock away from riskier value-add investments in the office sector and incur rising interest rates, This trend will more specifically impact commodity real estate assets in the core business district that are experiencing a rapid rise in vacancy and reductions in rents.
- **Vacancy rates will continue to rise** in the District of Columbia by 200-250 basis points in the next 48 months leaving landlords to determine whether to consider alternative options such as residential conversion or flexible office solutions.
- Due to the uncertainty's surrounding COVID-19 variants and return-to-office, **DC should expect more volatility leading into 2022**.

New construction Class A/Trophy assets that are offering higher end amenities, such as large conference rooms and outdoor common areas, will continue to command record concessions, including 20-25 months in free rent and tenant improvements $140-150 psf, on larger deals.

AVANT by AVISON YOUNG

You have questions. We have answers.

Washington, DC office market report
Q4 2021

Get in touch

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Explore the latest data and insights

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Measuring the pace of our return to downtowns

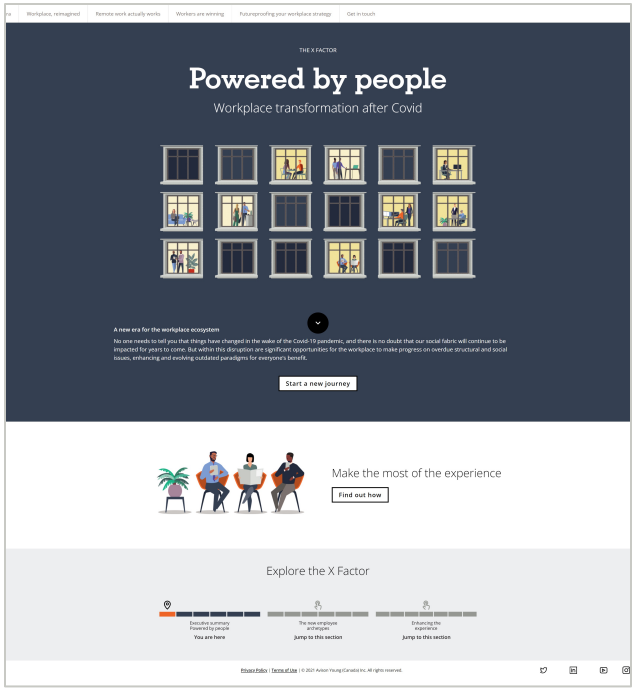
Our team takes a look at real-time movement of people in major cities across North America, and how the volume of foot traffic compares to pre-pandemic levels.

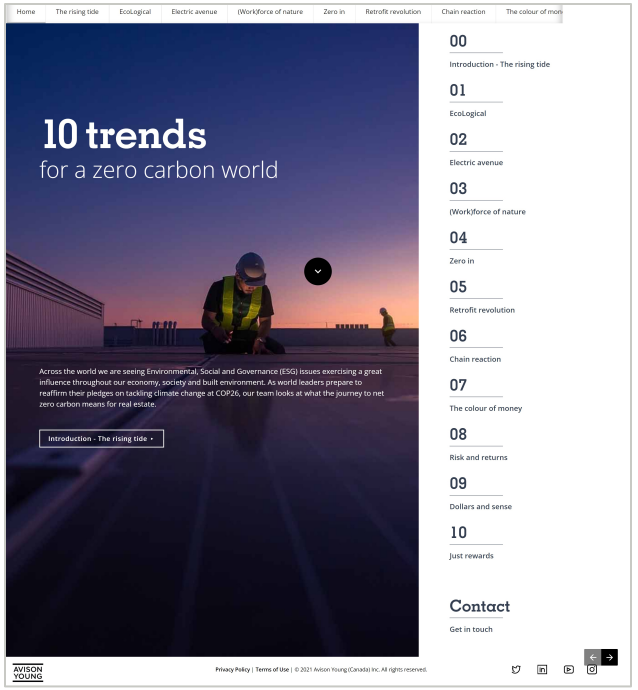
[U.S. employment overview]

Tracking trends in real-time

Our team takes a look at real-time movement of people in major cities across North America, and how the volume of foot traffic compares to pre-pandemic levels.

Deep-dive into the thought capital shaping real estate





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