



Philadelphia Office Market

Philadelphia Mask Mandate Lifted; Return-to-Office Issues Linger

The Philadelphia regional office market, while showing signs of improvement, continues to struggle with return to office concerns. The recent variant of COVID-19, Omicron, has waned since January and February, yet a forceful back to the office push by employers has not materialized. According to the Kastle Systems' March 2022 occupancy barometer, the Philadelphia Metropolitan area has seen 37.4% of its workforce return to the office. This remains below the current major metro average of 40.0%. Also, compared to the fourth quarter of 2021, the return to office average for Philadelphia only increased by 20 basis points, up from 37.2%.

The Philadelphia Central Business District (CBD) office market continues to absorb the brunt of the impact from the ongoing pandemic especially when compared to the Suburban Philadelphia office market. The workforce of sizable Downtown tenants, such as Comcast and Independence Blue Cross, remain largely remote. On the plus side, Philadelphia's indoor mask mandate, which had been in effect since June of 2020, was lifted during the first week of March 2022. With this encouraging news, and barring any unforeseen COVID flareup, we may now witness some larger employers press harder for a return to office during the spring and summer months. One significant downtown employer, Morgan Lewis & Bockius, is expected to implement a return policy for their employees in the month of April.

Current Conditions

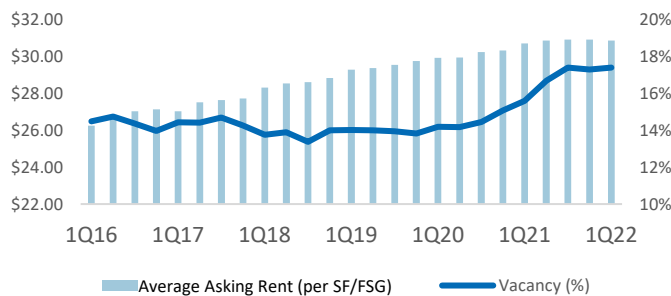
- Absorption was negative in the first quarter at -218,623 square feet.
- Available sublease space increased quarter-over-quarter by 0.8%.
- Overall vacancy rate increased slightly to 17.4% in the first quarter of 2022.

Market Summary

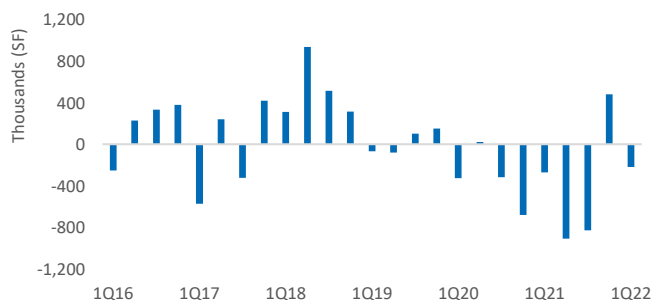
	Current Quarter	Prior Quarter	Year Ago Period	12-Month Forecast
Total Inventory (SF)	109.8M	109.7M	109.0M	↑
Vacancy Rate	17.4%	17.3%	15.6%	↑
Quarterly Net Absorption (SF)	-218K	482K	-269K	↑
Average Asking Rent/SF	\$30.87	\$30.93	\$30.71	↑
Under Construction (SF)	1.6M	1.6M	2.5M	↑

Market Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION



RESEARCH Q1 2022

According to Center City District's March 2022 Economic Recovery report, SEPTA ridership climbed to a pandemic high of 3.1 million per week in October 2021, but the Omicron variant reversed the momentum and the number of users declined to 2.2 million in January 2022. This utilization pales in comparison with January of 2020, when there were 5.4 million riders per week.

Kicking off 2022, overall absorption for the region was negative 218,623 square feet. The occupancy losses were mostly due to some large sublease vacancies recently added in the King of Prussia submarket. As a result, overall vacancy increased by 10 basis points from 17.3% in the fourth quarter to 17.4% in the first quarter. Asking rental rates for all classes declined marginally quarter-over-quarter from an average of \$30.93/SF in the fourth quarter to \$30.87/SF, a 0.2% drop. More positively, Class A asking rental rates increased since last quarter to \$34.61/SF, up from \$34.56/SF in the previous quarter.

Philadelphia Central Business District

The overall vacancy rate in the Philadelphia CBD declined by 20 basis points in the first quarter, going from 17.5% at the end of last year to 17.3% presently. The improvement is small, but it hopefully represents an inflection point, as declines in this metric have now been noted in back-to-back quarters. Absorption also kicked off the year in positive territory, totaling 52,841 square feet.

Many of the trends experienced over the past several quarters continue to be apparent. However, along with the dwindling number of Omicron cases reported during the month of March, there appears to be a corresponding uptick in tenant activity. Short-term leases and renewals continue to be most prevalent as tenants are still generally taking a wait-and-see approach to their real estate needs. Interestingly, short-term leases inked early in the pandemic are reaching their expiration dates, so decisions for these users concerning the length of lease term commitments will have to be made yet again. Also, some tenants are exercising early termination clauses as a means of aligning the size of their space envelope with current needs.

To help combat declining occupancy rates, building conversions continue to be explored by landlords, particularly from office to life science.

Philadelphia's life science market remains extraordinarily strong as more tenants of this type continue to consider Philadelphia as a potential location. Another appealing option for landlords that has arisen recently are office-to-school building conversions. Each of these conversions serves to remove inventory from the competitive market and reduce the overall vacancy rate.

We are also seeing larger tenants turn to coworking space to accommodate current hybrid work models. This gives users the ability to sign flexible, short-term leases and take the time to accurately gauge what their space requirements will be as people return to the office.

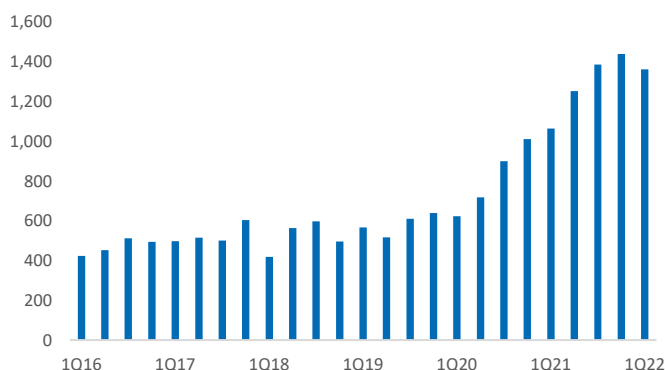
The asking rental rate for all classes in the Philadelphia CBD remained flat quarter-over-quarter at an average of \$34.51/SF. Class A asking rates declined slightly since the fourth quarter going from \$38.05/SF to \$37.90/SF in the first quarter. Concessions offered by landlords continue to be strong. For example, some seven-year leases now include concessions typically associated with a 10-year deal.

Significant leases signed during the first quarter include Drexel committing to 60,000 square feet at a newly proposed life science building, which will be located at 3201 Cuthbert Street. The planned development will total 500,000 square feet, making it the largest life science building currently in the Downtown market. The project is expected to break ground during the second half of 2022 and will deliver in the fourth quarter of 2024. This new building galvanizes University City as the bright spot in the Downtown market where demand for life science space remains robust.

Additional leases inked in the CBD this quarter included: Cash App leasing 35,000 square feet at 1100 Ludlow Street; GLG taking 13,833 square feet in the Bourse Building located at 111 S. Independence Mall E.; and Red Tettermer O'Connell + Partners committing to 11,300 square feet at 2400 Market Street.

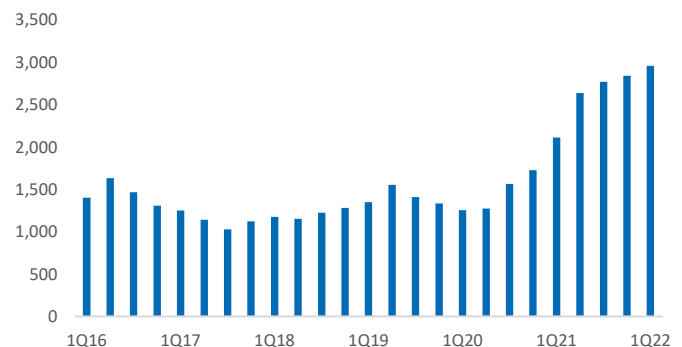
Sublease Volume: Philadelphia CBD

TOTAL SF, THOUSANDS



Sublease Volume: Philadelphia Suburbs

TOTAL SF, THOUSANDS



Philadelphia Suburbs

The Suburban office market experienced an increase in vacancy from 17.1% in the fourth quarter to 17.4% in the first quarter. This is attributed to two large tenants in the King of Prussia submarket opting to put their buildings on the market for sublease. CSL Behring announced it would offer its 100,820-square-foot building at 500 N. Gulph Road to the market for sublease as did Vertex, which is located at 2301 Renaissance Boulevard in 189,000 square feet. Both tenants are shedding space in response to current hybrid work conditions created by COVID-19.

Despite the noted increase in sublease space this quarter, conditions remain more promising in the suburbs than in the Downtown market. Deal velocity is strong, and many tenants are looking for space. While short-term transactions and renewals remain prevalent, longer-term leases are being signed. Landlords continue to offer generous concessions to entice tenants into longer-term commitments. Despite healthy overall leasing activity in the suburbs, some submarkets continue to struggle with occupancy. The amount of sublease space that could potentially be introduced to the market over the next several quarters will be worth monitoring.

Asking rental rates in the suburbs for all classes declined by 0.4% quarter-over-quarter to a current average of \$28.79/SF. Class A rates remained relatively flat, increasing only slightly from \$31.98/SF to \$32.00/SF quarter-over-quarter.

Significant leases signed this quarter included Janssen Supply Group subleasing nearly 60,000 square feet of space at 700 Dresher Road in Horsham. This transaction helped offset some of the negative absorption caused by users dumping space onto the sublease market over the past several quarters in the Horsham/Willow Grove submarket. In the same submarket, Grundy Insurance took 25,000 square feet at 410 Horsham Road. Additional notable leases inked this quarter included Customers Bank taking 40,368 square feet at 40 General Warren Boulevard in Malvern and Pep Boys leasing 35,950 square feet at 1 Presidential Boulevard in Bala Cynwyd.

The largest investment sale in the suburban Philadelphia office market this quarter was the purchase of 980 Jolly Road in Blue Bell. The 150,000-square-foot asset was purchased by Jack Lingo Asset Management from Artemis Real Estate Partners for \$36.5 million, or \$243/SF.

Philadelphia CBD Lease/User Transactions

Tenant	Submarket	Building	Type	Square Feet
Drexel	University City	3201 Cuthbert Street	New Lease	60,000
Cash App	East Market	1100 Ludlow Street	New Lease	35,000
GLG	Independence Square	111 S Independence Mall E	New Lease	13,833
Red Tetterer O'Connell + Partners	West Market	2400 Market Street	New Lease	11,300

Philadelphia Suburbs Lease/User Transactions

Tenant	Market	Building	Type	Square Feet
Janssen Supply Group	Horsham/Willow Grove	700 Dresher Road	Sublease	58,155
Customers Bank	Exton/Malvern	40 General Warren Boulevard	New Lease	40,368
Pep Boys	Bala Cynwyd	1 Presidential Boulevard	New Lease	35,950
Grundy Insurance	Horsham/Willow Grove	410 Horsham Road	New Lease	25,000

Submarket Statistics								
	Total Inventory (SF)	Under Construction (SF)	Total Vacancy Rate	Qtr Absorption (SF)	YTD Absorption (SF)	Class A Asking Rent (Price/SF)	Class B Asking Rent (Price/SF)	Total Asking Rent (Price/SF)
CBD Total	45,174,261	1,610,000	17.3%	52,841	52,841	\$37.90	\$30.34	\$34.51
East Market	6,331,084	-	19.5%	262	262	\$36.39	\$27.39	\$32.21
Independence Square	5,380,384	-	17.8%	5,417	5,417	\$30.21	\$32.75	\$31.30
University City	4,688,776	1,302,000	9.7%	-1,000	-1,000	\$43.34	\$44.18	\$43.15
Walnut/South Broad	3,977,064	-	20.0%	31,813	31,813	\$35.39	\$32.95	\$30.96
West Market	24,796,953	308,000	17.7%	16,349	16,349	\$38.23	\$28.54	\$35.62
Suburban Total	64,645,064		17.4%	-271,464	-271,464	\$32.00	\$26.72	\$28.79
Bala Cynwyd	2,944,026	-	14.5%	-11,792	-11,792	\$38.64	\$35.10	\$36.06
Blue Bell/Plymouth Meeting	8,452,658	-	17.6%	32,434	32,434	\$29.62	\$23.80	\$26.27
Bucks County	7,984,833	-	21.6%	-60,670	-60,670	\$27.85	\$23.60	\$24.75
Central/S Delaware County	5,304,227	-	15.7%	73,116	73,116	\$29.32	\$25.90	\$27.32
Conshohocken	3,999,915	-	20.8%	14,722	14,722	\$45.38	\$36.49	\$42.12
Exton/Malvern	7,873,948	-	15.9%	-109,666	-109,666	\$29.55	\$27.38	\$28.51
Fort Washington	3,561,466	-	13.3%	741	741	\$27.79	\$25.83	\$26.95
Horsham/Willow Grove	4,382,604	-	27.3%	67,603	67,603	\$28.00	\$25.04	\$25.44
Jenkintown	1,081,401	-	20.5%	7,654	7,654	\$25.82	\$22.53	\$24.24
King of Prussia	13,417,944	-	16.6%	-257,130	-257,130	\$34.32	\$29.21	\$30.81
Radnor/Main Line	2,836,200	-	6.0%	-24,638	-24,638	\$45.71	\$29.59	\$42.56
Southern 202 Corridor	2,805,842	-	14.6%	-3,838	-3,838	\$28.83	\$25.56	\$27.20
Market Totals	109,819,325	1,610,000	17.4%	-218,623	-218,623	\$34.61	\$27.73	\$30.87

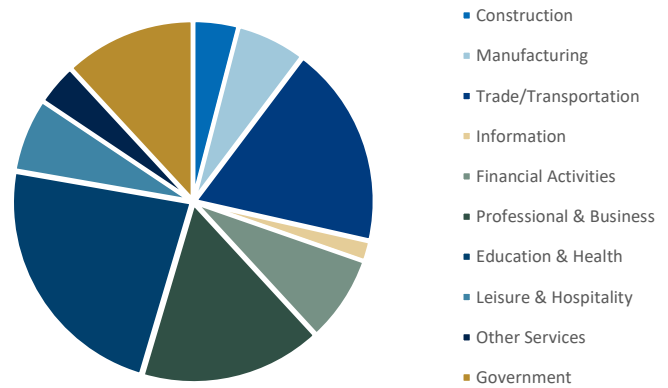
Economic Overview

The unemployment rate in the Philadelphia metropolitan statistical area increased to 5.3% in January 2022, a 110 basis point increase from the 4.2% unemployment rate in December 2021. In comparison, the national unemployment rate currently sits at 3.8%. Despite the increase in unemployment in early 2022, all of the Philadelphia MSA's tracked industries have exhibited growth over the past year. The leisure and hospitality (+24.6%), professional and business services (+5.2%) and construction (+4.6%) sectors demonstrated the highest growth over that period.

As the Philadelphia office market emerges from the winter months and passes beyond the Omicron variant, 2022 is poised to be a better year. Expect more companies to make partial or even full returns to the office, particularly in the Downtown market. However, the hybrid work model many companies have implemented will be a factor, the extent of which we can only speculate about at this juncture.

Employment by Industry

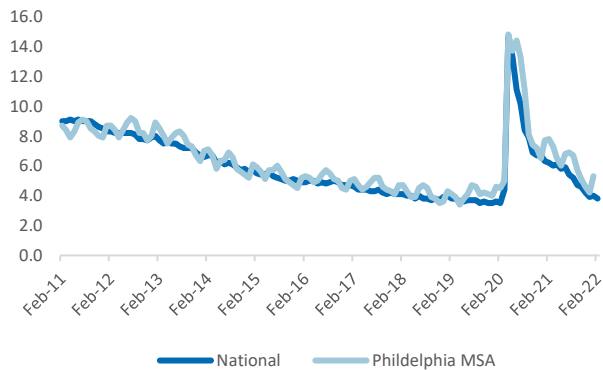
PHILADELPHIA MSA, 2022 ANNUAL AVERAGE



Source: U.S. Bureau of Labor Statistics, February 2022.

Unemployment Rate

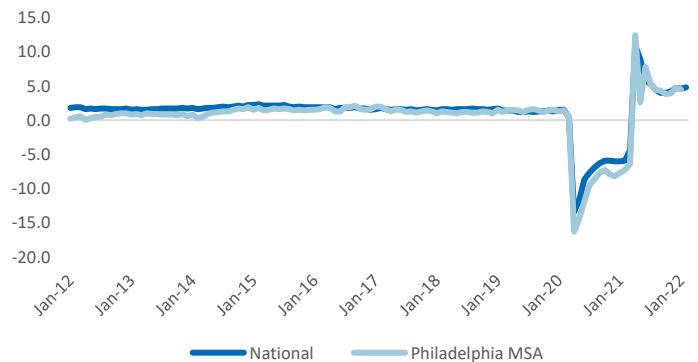
NOT SEASONALLY ADJUSTED



Source: U.S. Bureau of Labor Statistics, February 2022.

Payroll Employment (Total Nonfarm)

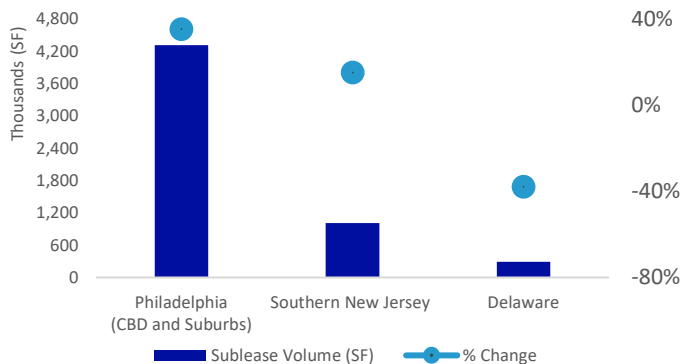
NOT SEASONALLY ADJUSTED, 12-MONTH % CHANGE



Source: U.S. Bureau of Labor Statistics, February 2022.

Greater Philadelphia Markets Sublease Analysis

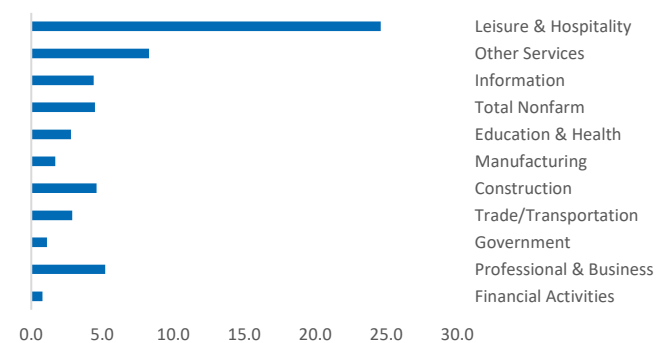
SQUARE FEET AND 12-MONTH % CHANGE, 1Q22



Source: Newmark Research, March 2022.

Employment Growth by Industry, January 2022

PHILADELPHIA MSA, 12-MONTH % CHANGE



Source: U.S. Bureau of Labor Statistics, January 2022.

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