1Q24

Washington Metro Office Market Overview

Market Observations

Economy

- The region's labor market remains strong amid shifting macroeconomic conditions. February's 2.7% unemployment rate remains significantly lower than the region's ten-year historical average of 4.1%. Furthermore, the Washington DC metro's unemployment rate is 120 basis points lower than the national rate.
- Year-over-year, job gains have been most pronounced in the Education & Health and Government sectors, posting gains of 2.8% and 2.6%, respectively. The office-occupying industries of Information, Financial Activities, and Professional and Business Services experienced job losses over the past year, helping to account for continued limited demand for office space.
- While some office-using sectors experienced a decline in employment over the past year, jobs in the office-using sectors remain at a level that is 1.1% higher than four years ago—just prior to the pandemic—and 5.3% higher than the pandemic-induced employment trough in April 2020.

Major Transactions

- Office investment sales continue to lag in pricing per square foot as well as total transaction volume. However, owner-user sales, flex facilities, and data centers are propping up a lot of demand in Washington, D.C. capital markets.
- The largest sale of the quarter was Central Place Tower located within the Rosslyn submarket of Northern Virginia. CoStar Group purchased the 552,000-square-foot office building from a joint venture between JBG SMITH Properties and PGIM, Inc for $325 million, or $588.47 PSF. CoStar Group acquired the 31-story office building to use as their national headquarters and will occupy approximately 150,000 square feet of the building.

Leasing Market Fundamentals

- Net absorption for the region totaled negative 1.2 million square feet during Q1 2024, with all three metro area markets experiencing net negative demand.
- Overall vacancy expanded to 21.0%, up 40 basis points over the quarter and 140 basis points year-over-year. Availability also expanded, ending Q1 2024 at 25.4%, an increase of 40 basis points quarter-over-quarter and 170 basis points year-over-year.
- Major first-quarter transactions were comprised entirely of lease renewals, with the top three transactions occurring within the District, while the next two transactions occurred in Northern Virginia.
- After one delivery during the quarter, the office construction pipeline ended Q1 2024 at 2.0 million square feet. The building that delivered was 915 Meeting Street in North Bethesda, which was 45% preleased at the time of delivery.

Outlook

- A strong and resilient labor market, coupled with persistent inflationary concerns, is contributing to an uncertain macroeconomic outlook in the near-term.
- For the first time since 2015, the market demonstrated a decline in rents during the first quarter of 2024. Annual rent increases averaged 1.6% over the last decade, with much of that growth slowing since 2020.
- Fewer landlords have capital for concessions, which have been a major driver in attracting tenants and capturing net positive absorption over the past several years. The pool of landlords that can perform, or pay for tenant improvement, is shrinking. There are fewer owners offering trophy office supply, fostering an unusual landlord-favorable environment for the most quality space. Meanwhile, conditions continue to soften in class B and C assets.

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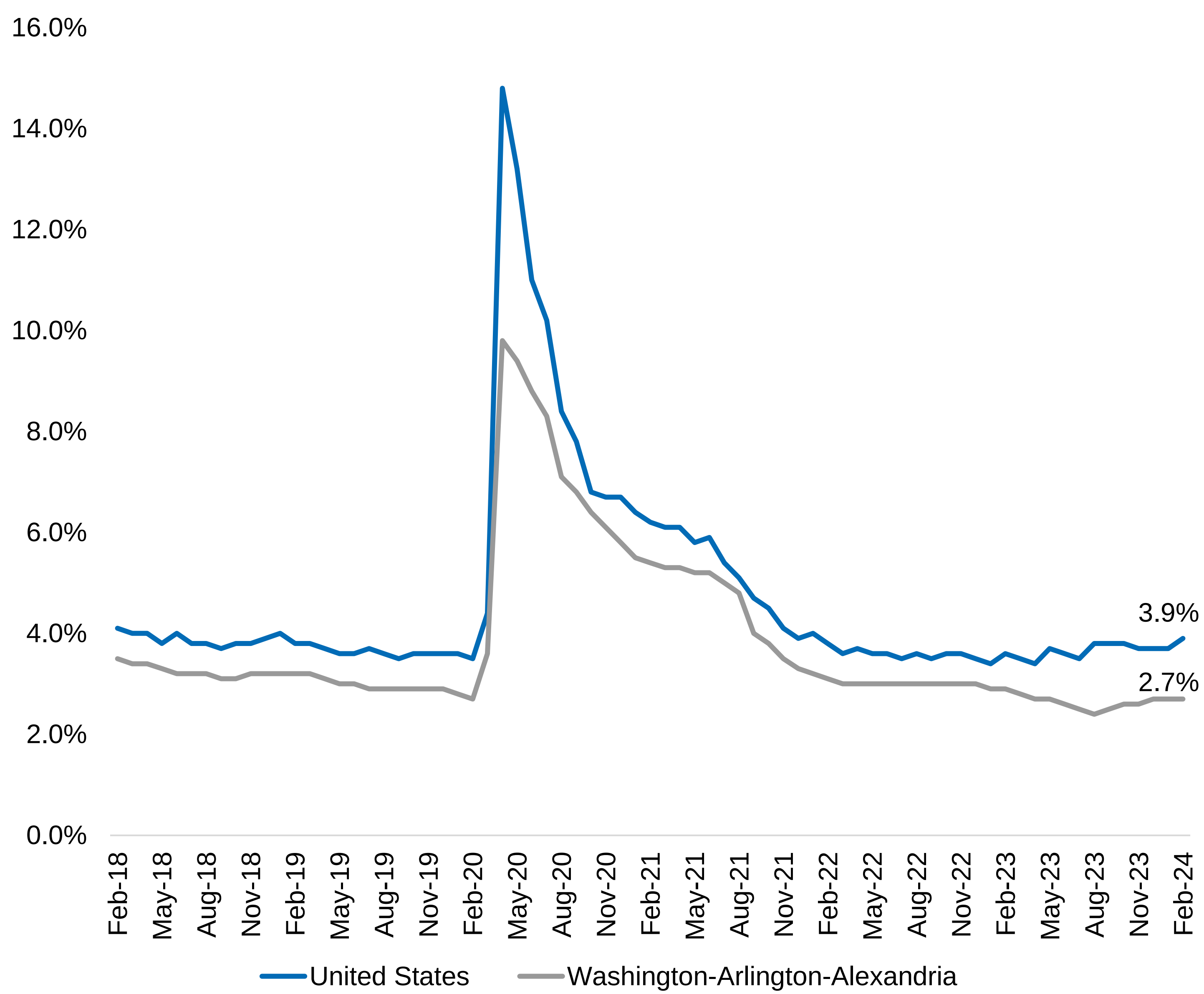
Economy

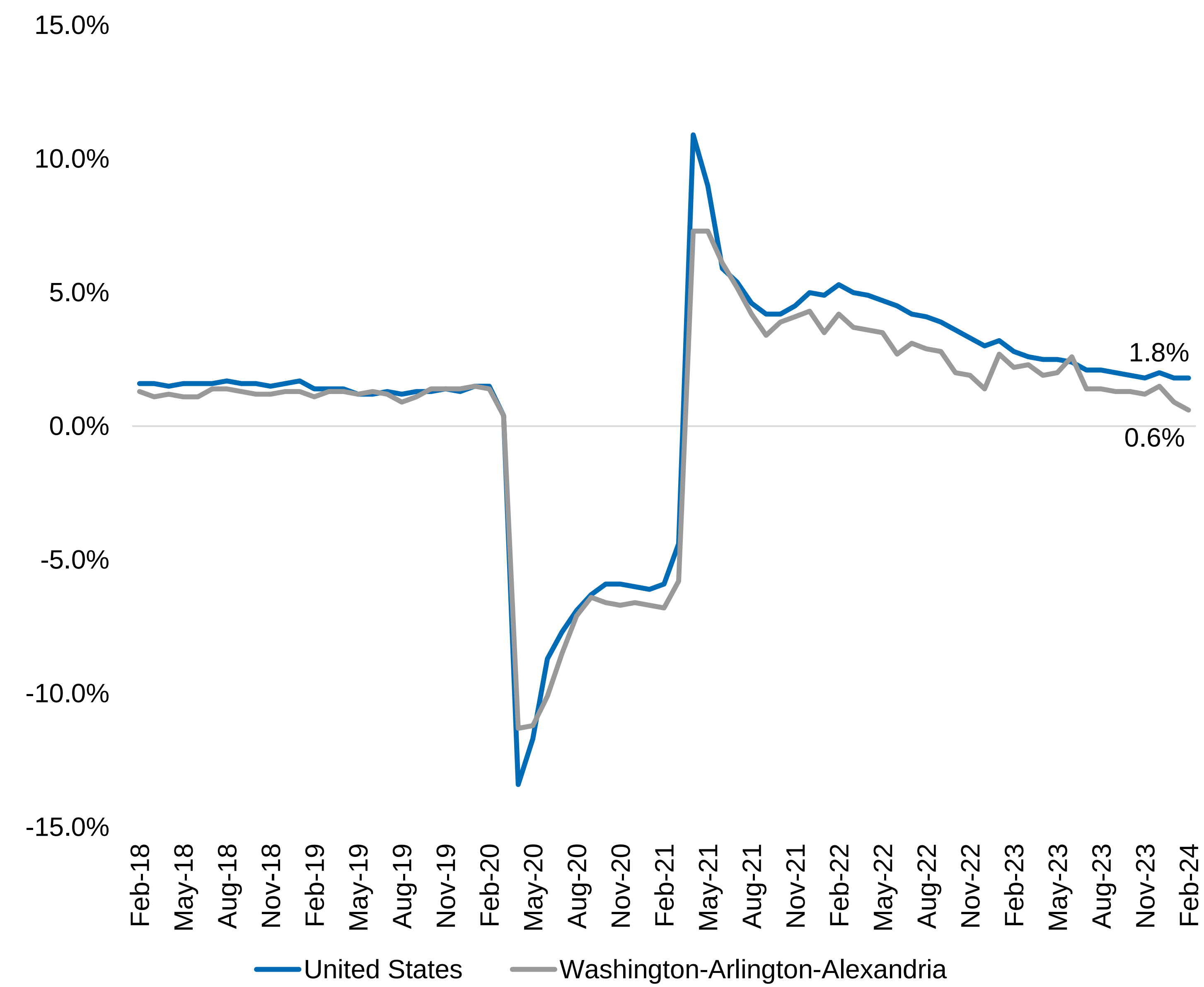
Metro Employment Job Growth Remains Positive Despite Slowing

The region's labor market is very tight, with unemployment 120 basis points below the national average. Job growth has begun to slow, but nonetheless remains positive.

Unemployment Rate, Seasonally Adjusted



Nonfarm Payroll Employment, Non-Seasonally Adjusted, 12-Month % Change

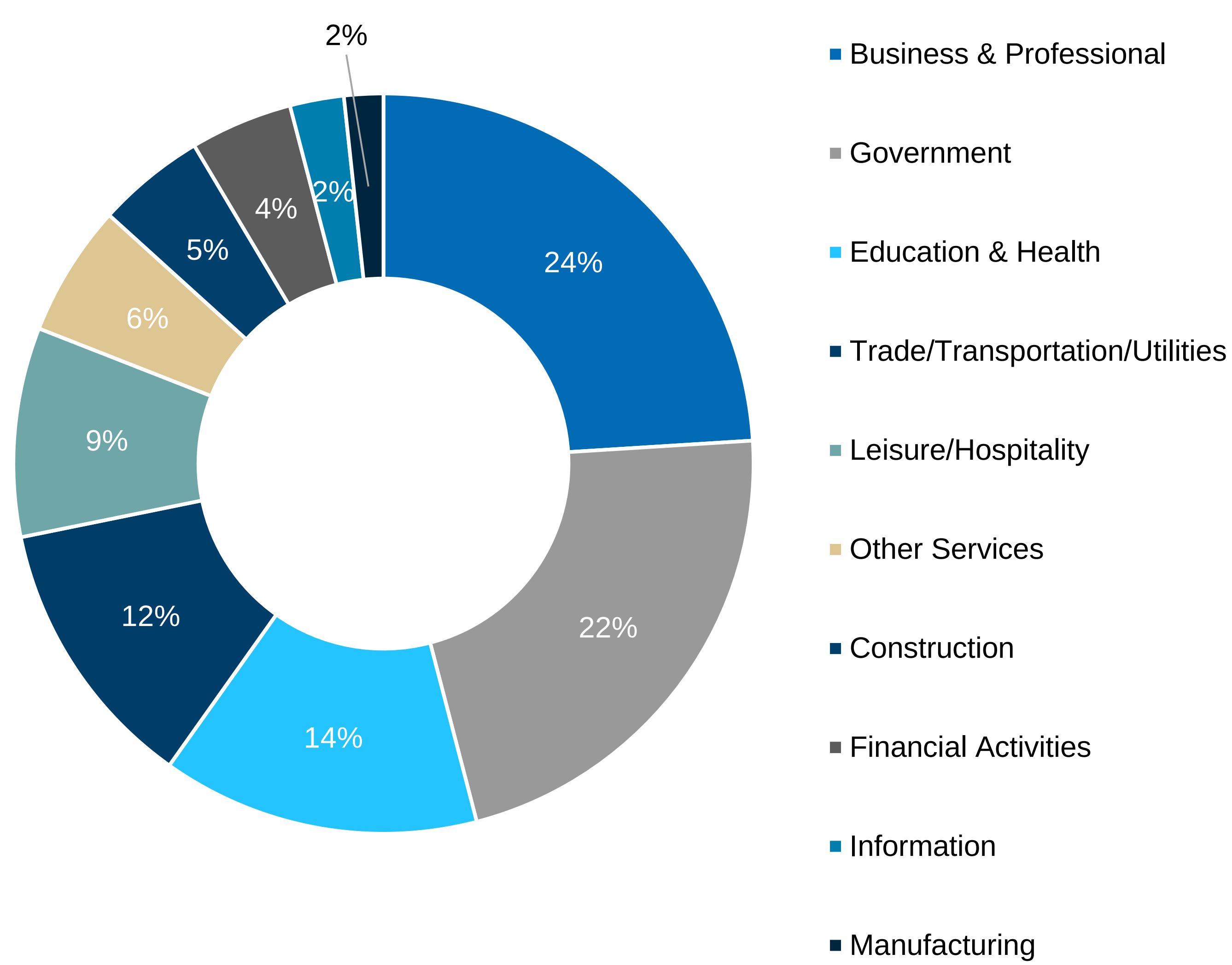


Source: U.S. Bureau of Labor Statistics, Washington-Arlington-Alexandria

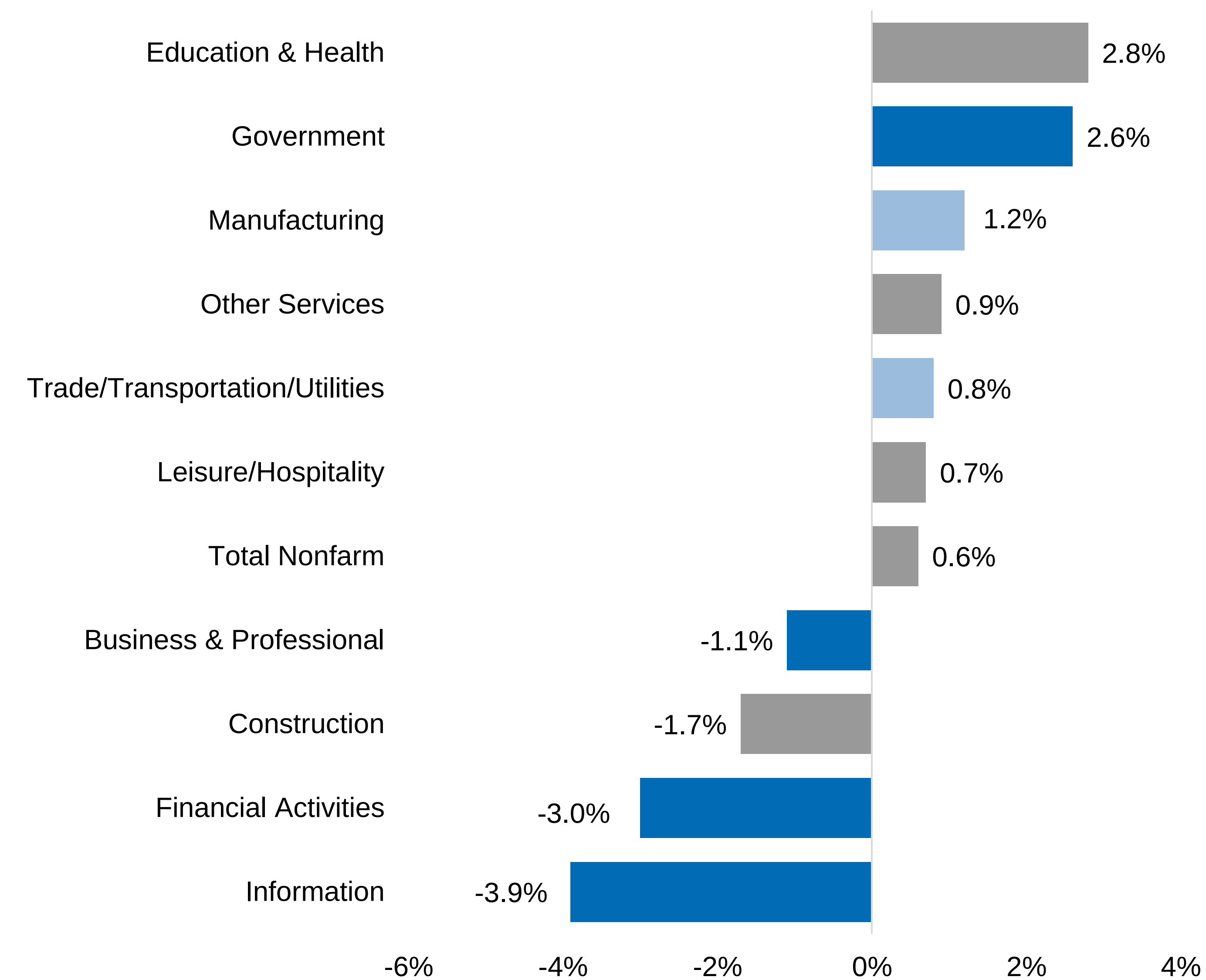
Job Growth Driven in Large Part by Education, Health, and Government

Education, Health, and Government propped up job growth in the region, leading to total nonfarm employment growth of 0.6%. Despite this, office-occupying industries of Information, Financial Activities, and Professional and Business Services experienced some job losses over the past year, contributing to declining demand for office space.

Employment by Industry, February 2024



Employment Growth by Industry, 12-Month % Change, February 2024

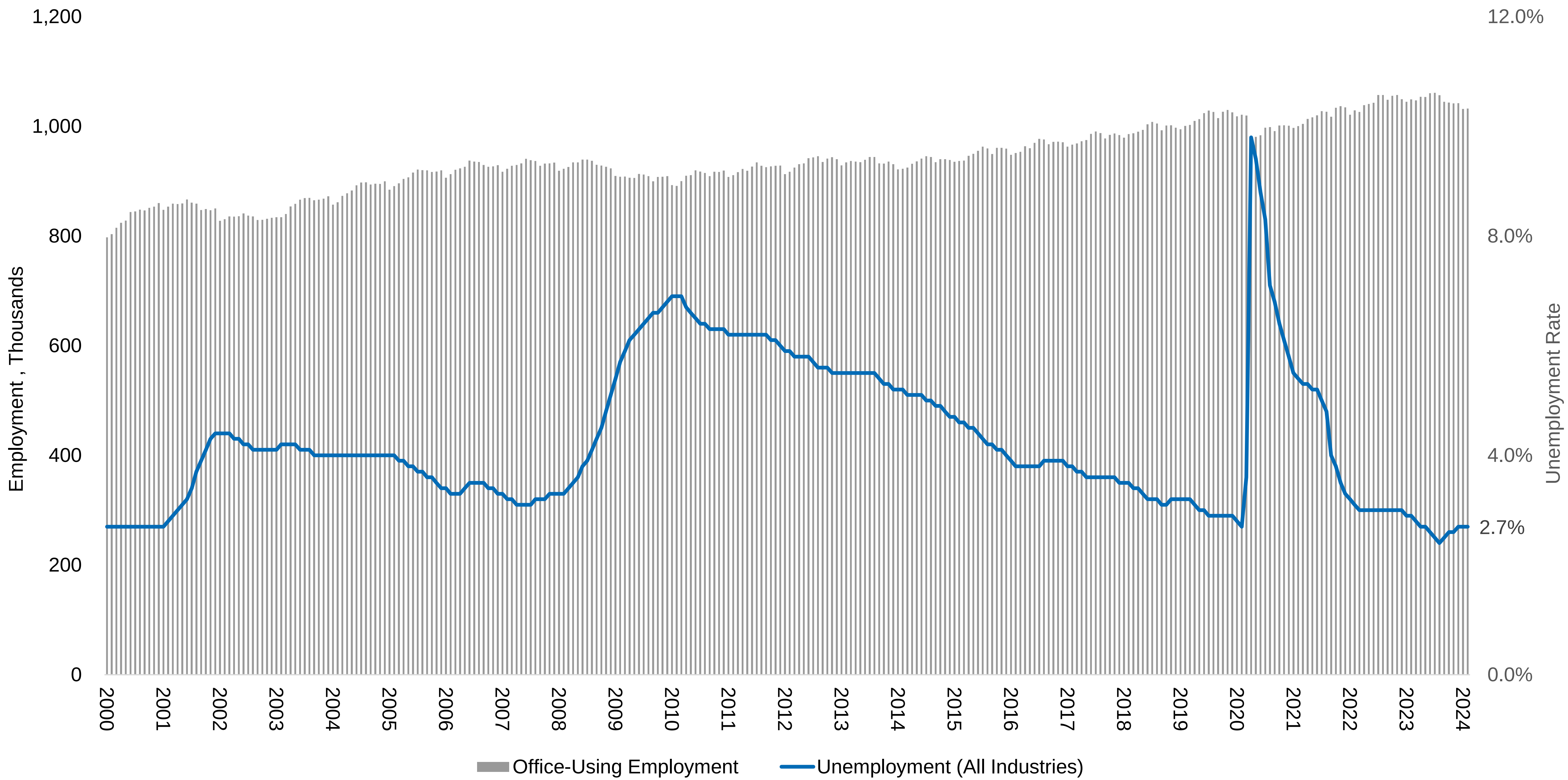


Source: U.S. Bureau of Labor Statistics, Washington-Arlington-Alexandria

Overall Office-Using Employment Has Rebounded

The number of office jobs has rebounded and now exceeds pre-pandemic levels. Office-using jobs in the region are currently 1.1% higher than four years ago—just before the pandemic—and 5.3% higher than the pandemic-induced employment trough in April 2020.

Office-Using Employment* and Unemployment Across All Industries

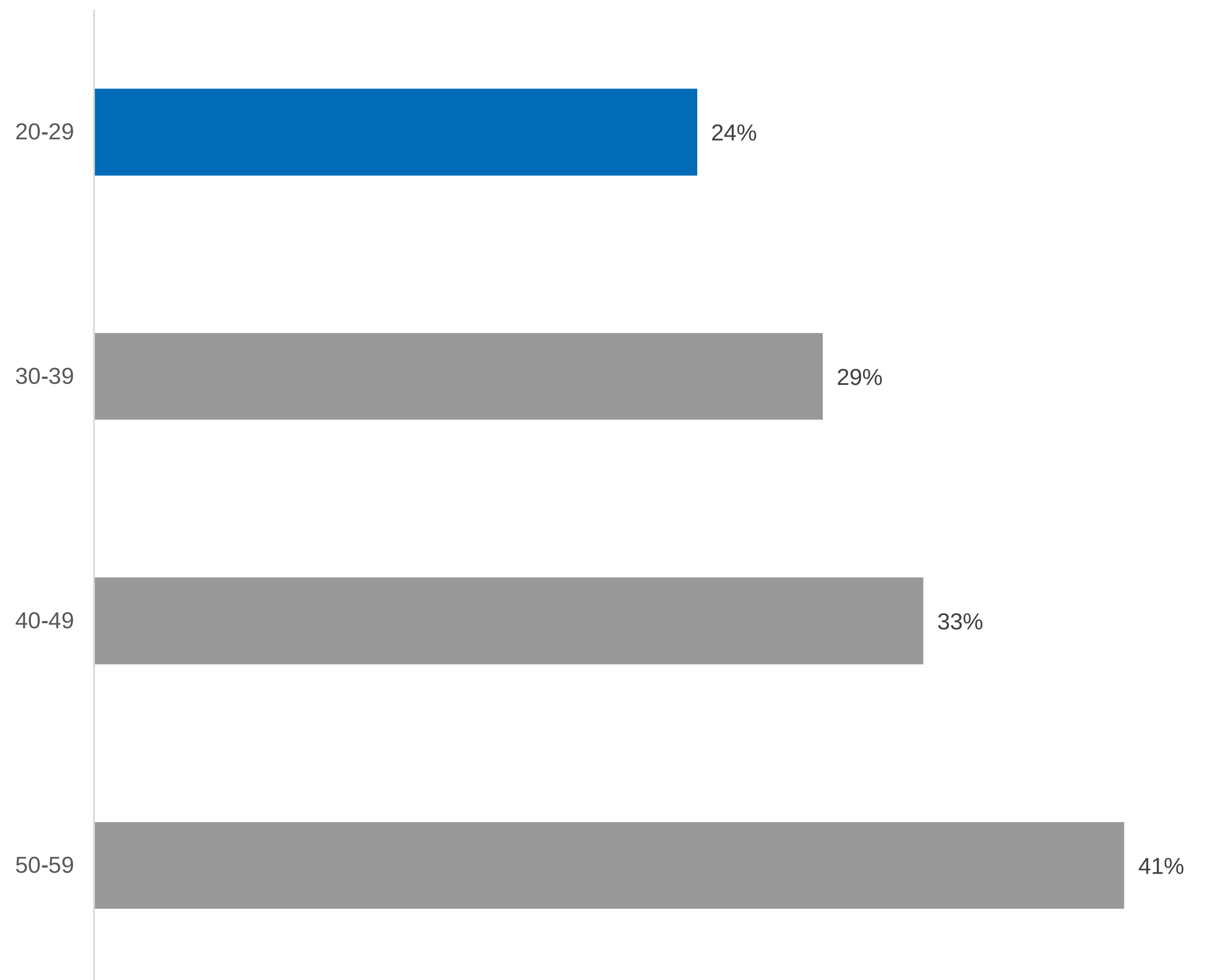


Source: U.S. Bureau of Labor Statistics, Washington-Alexandria-Arlington
Note: February 2024 data is preliminary.
*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.

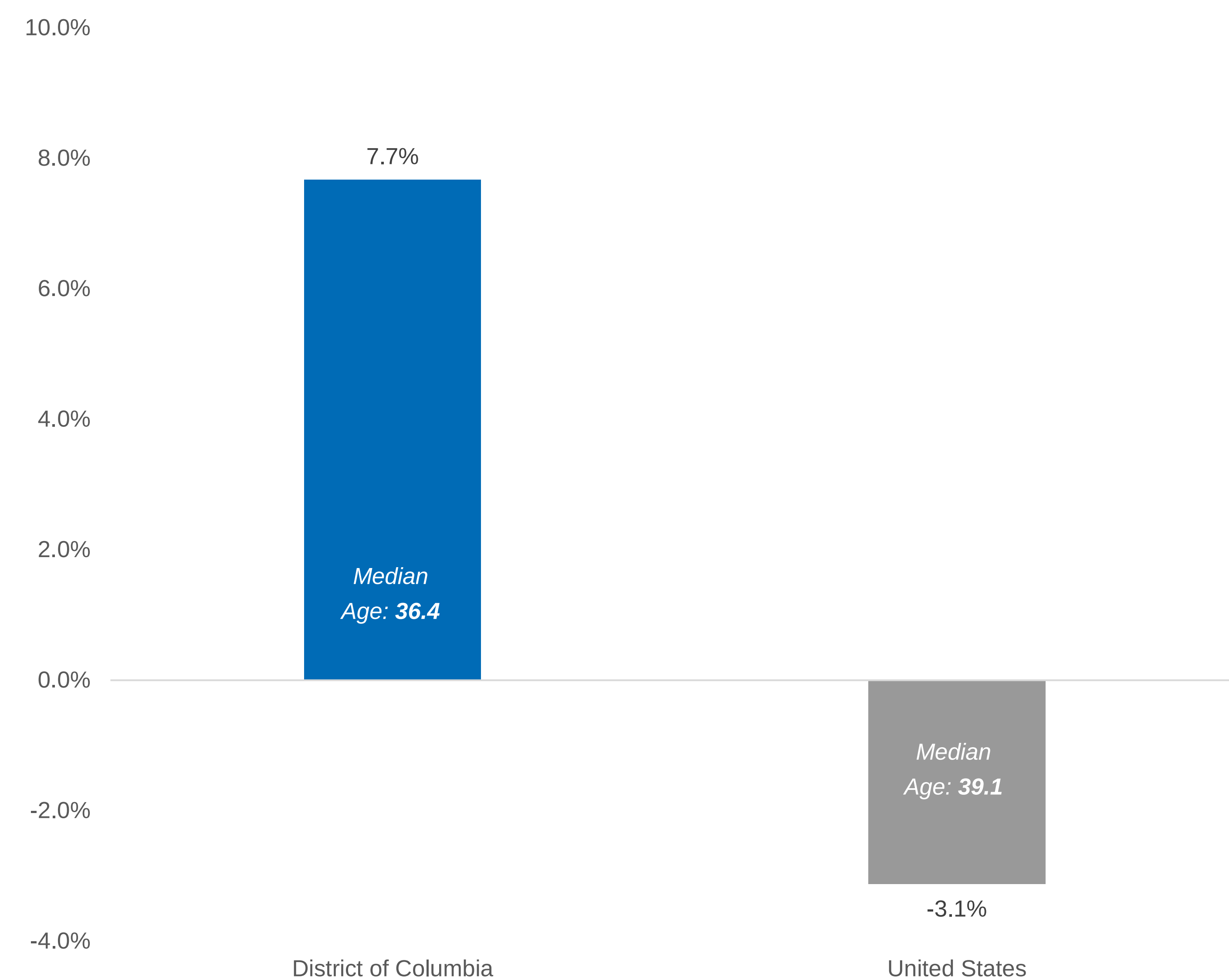
Younger Workers Prefer Office Time, And D.C.'s Workforce Is Getting Younger

Less than a quarter of workers in their 20s want to work from home full-time. In general, the older the employee, the more likely they are to prefer fully remote work. In the District of Columbia, the median age (36.4 years) is significantly lower than the U.S. average of 39.1 years. This bodes well for office demand, as it will be younger generations that desire designated office space.

Percent of Employees Who Prefer To Work From Home Full-Time



Five-Year Population Growth, 20-29 Year Olds (2023-2028)



Source: Business Insider, ESRI

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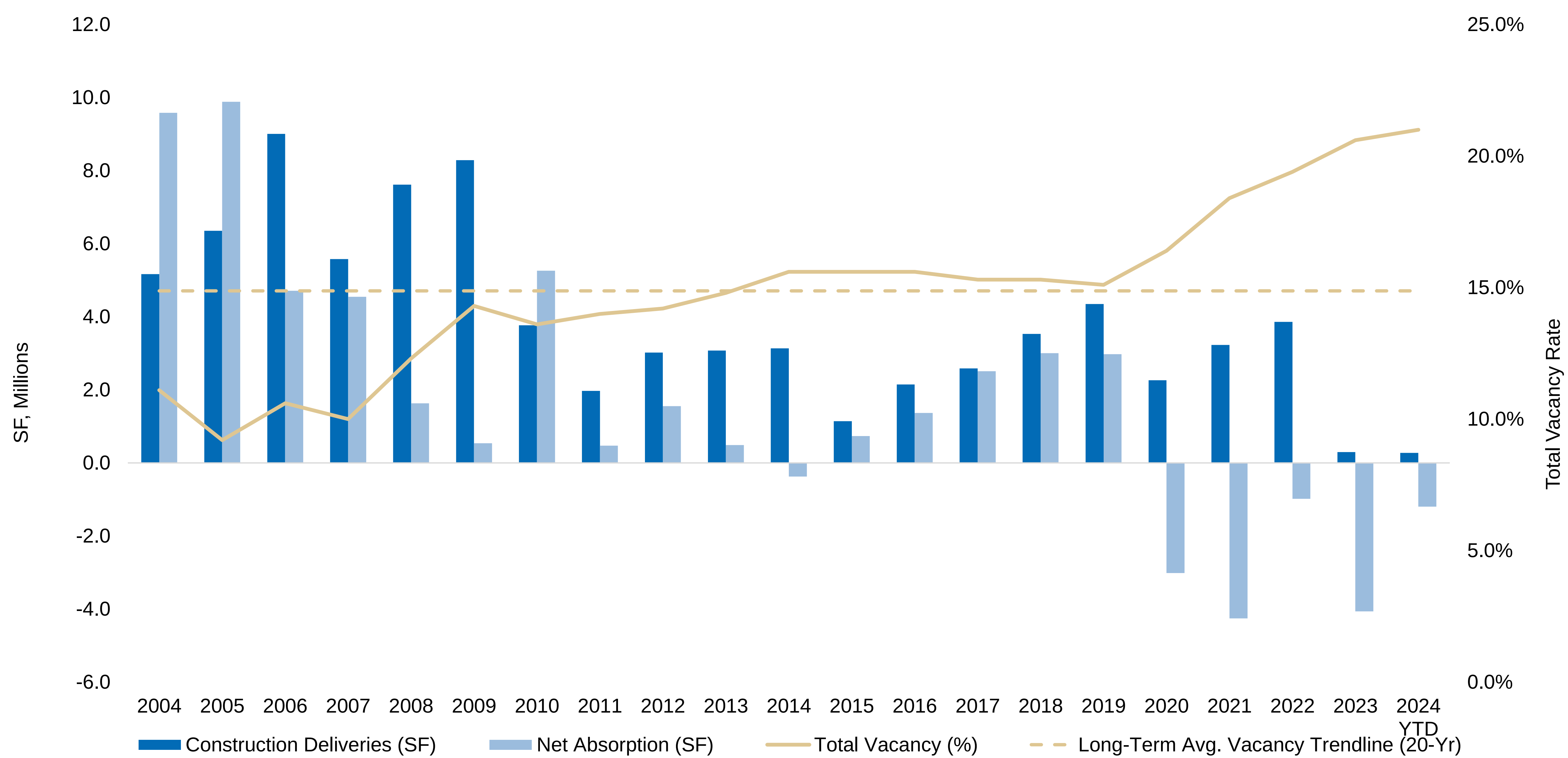
Leasing Market Fundamentals

Vacancy Rises but Construction Deliveries Slow Down

The metro area vacancy rate rose 40 basis points over the quarter to end Q1 2024 at 21.0%. This occurred after the market experienced over 1.2 MSF of negative net absorption during the quarter. Approximately 276,000 square feet delivered in Q1 2024, well below the 20-year average of almost 1.0 MSF delivered per quarter. A slowdown in office deliveries and lack of new speculative office construction will be advantageous in helping to balance supply with waning demand.

Historical Construction Deliveries, Net Absorption, and Vacancy

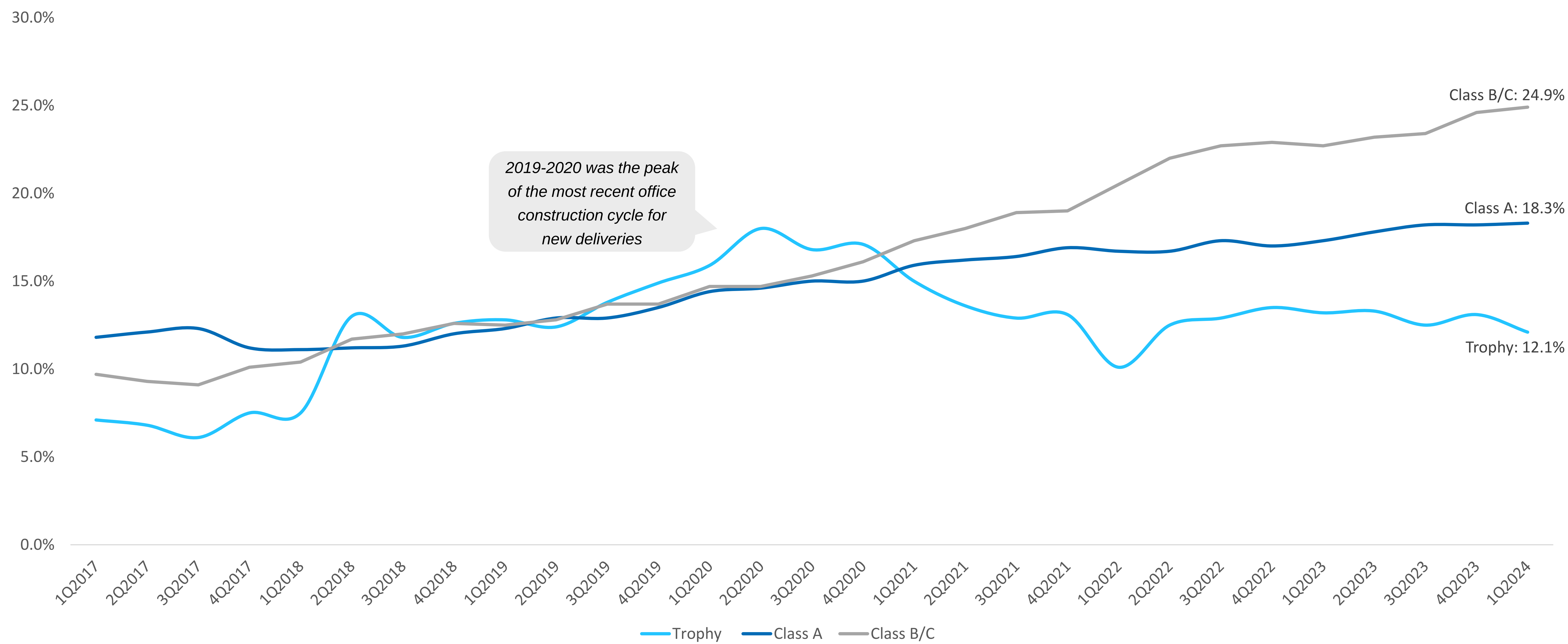


Source: Newmark Research

D.C. Trophy Office Continues to Outperform Lower-Quality Product

Trophy product saw a peak in vacancies at 18.0% in Q2 2020, which was partly attributable to new deliveries in lease-up. Since that point, trophy product has outperformed all other asset classes by tightening 590 bps and ending 2023 at 12.1%. In contrast, Class A and Class B/C product saw vacancy expansions during the same period, highlighting the desirability of trophy product in the market, even during economic downturns.

Washington, D.C. Office Total Vacancy: Trophy Vs. Class A Vs. Class B/C

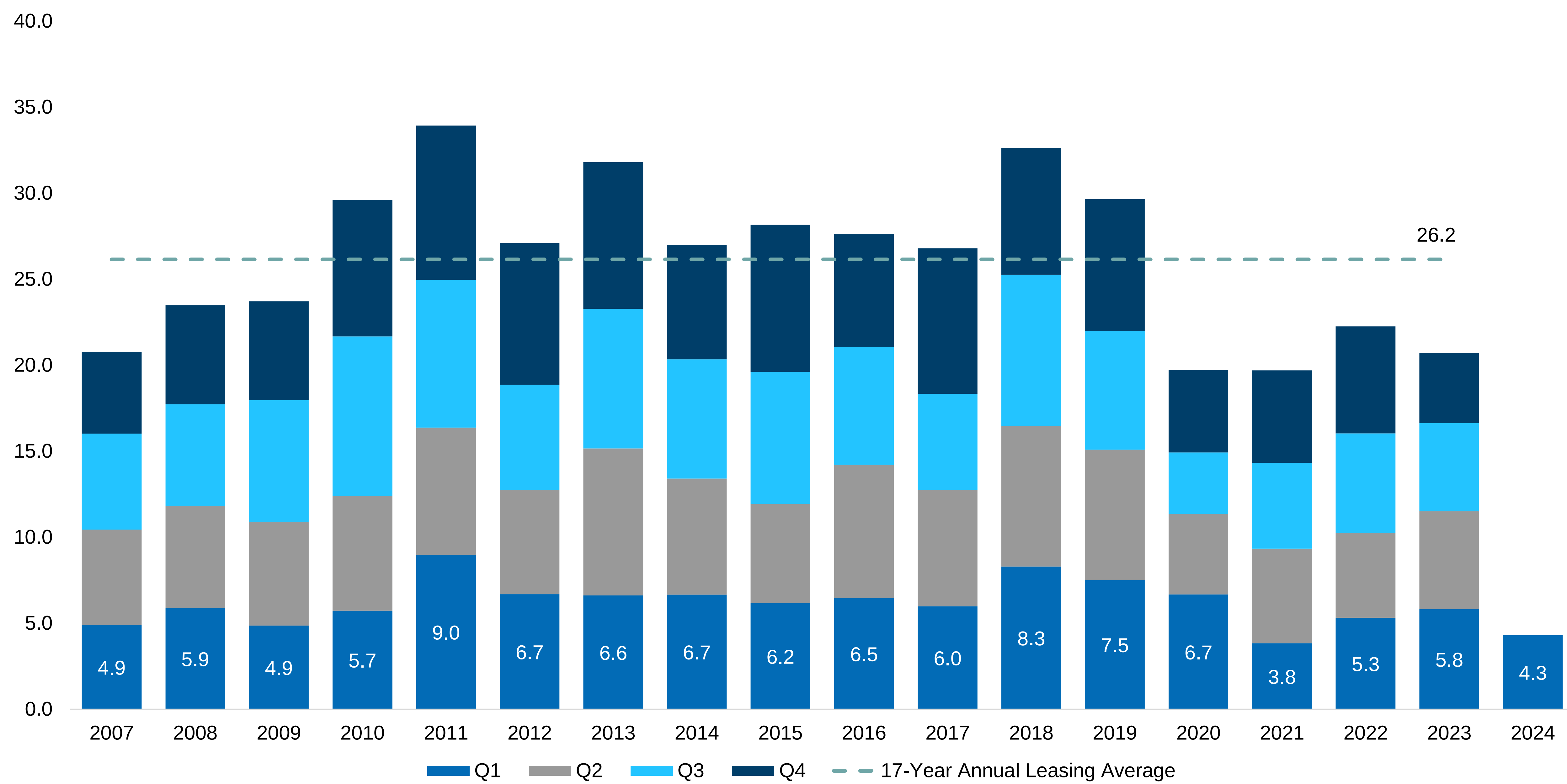


Source: Newmark Research

Leasing Activity Has Slowed

A cloudy economic outlook and the higher cost of capital has prompted many companies to pause, assess current conditions and enact cost-cutting measures where applicable. This is highlighted by the market's leasing activity, as the market saw only 4.3 MSF of leasing activity during Q1 2024, lower than the long-term average of 6.2 MSF of leasing activity during Q1.

Total Leasing Activity (msf)

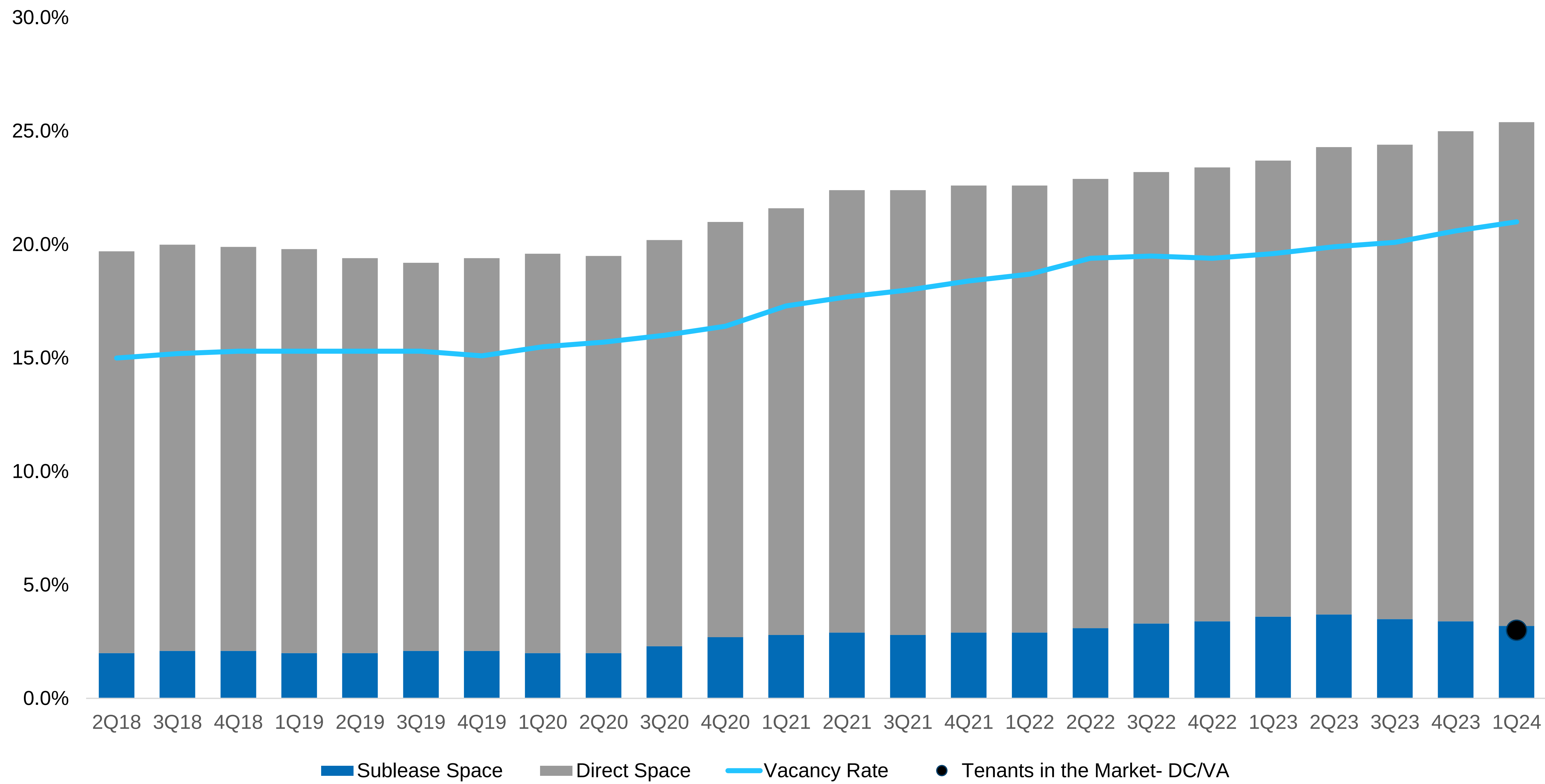


Source: Newmark Research, CoStar

Availability Continues to Increase While Tenant Demand Drops

Available office space sits near historical highs, both in terms of direct and sublease space. Over the past six years, the direct availability rate has averaged 19.0% while the sublease availability rate has averaged 2.7%. The Q1 2024 availability rates of 22.2% for direct space and 3.2% for sublease space are well above the long-term averages. This expansion of available space is likely to continue as companies cautiously plan longer-term office strategies.

Available Space and Tenant Demand as Percent of Overall Market

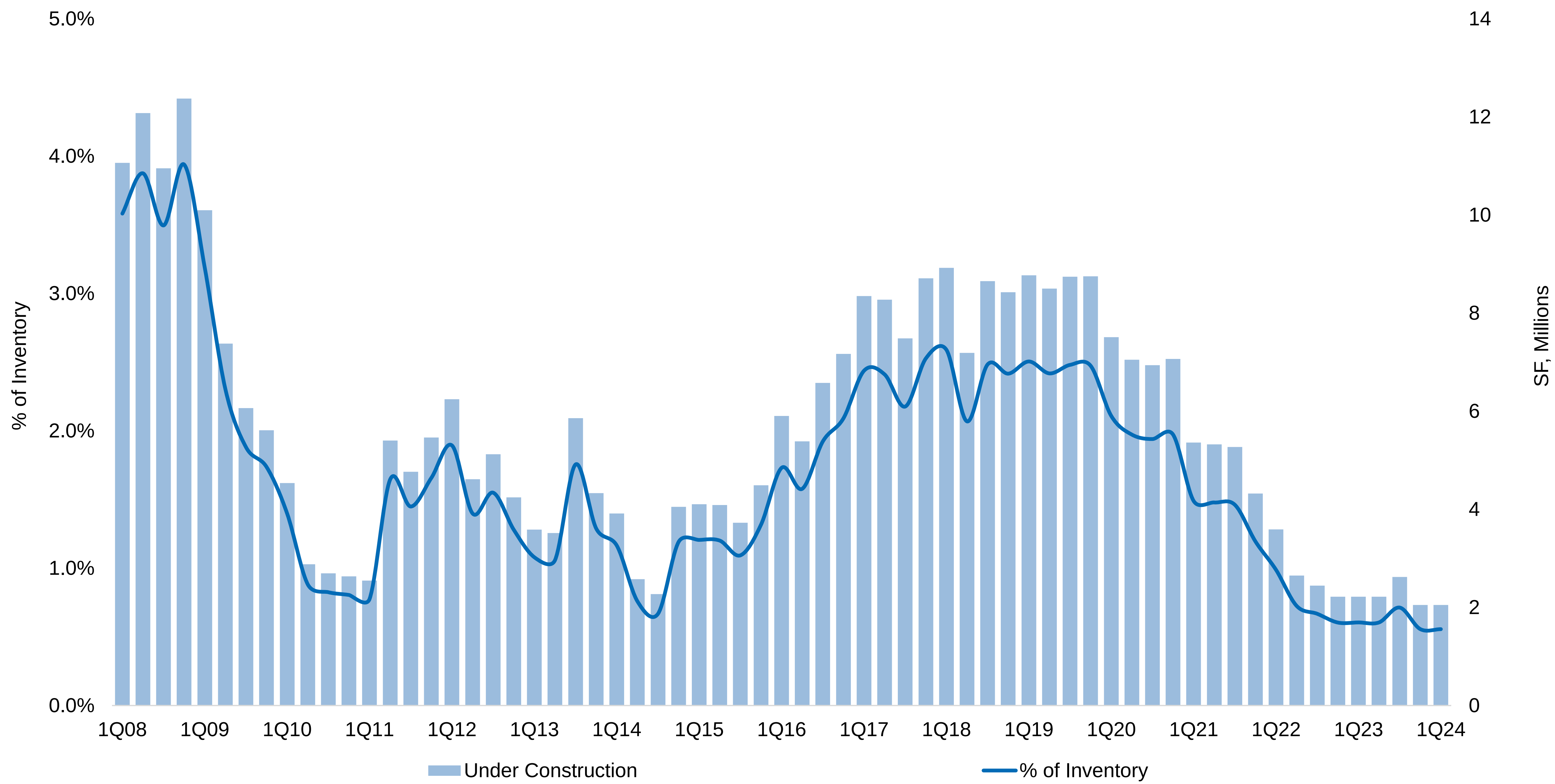


Source: Newmark Research

Deliveries Slow as Office Construction Pipeline Tapers

The Washington Metro area development pipeline remains historically low, with no new projects breaking ground and only one office delivery this quarter. There are currently 8 office properties under construction in the region, well below the historical average of 22 properties under construction.

Office Under Construction and % of Inventory

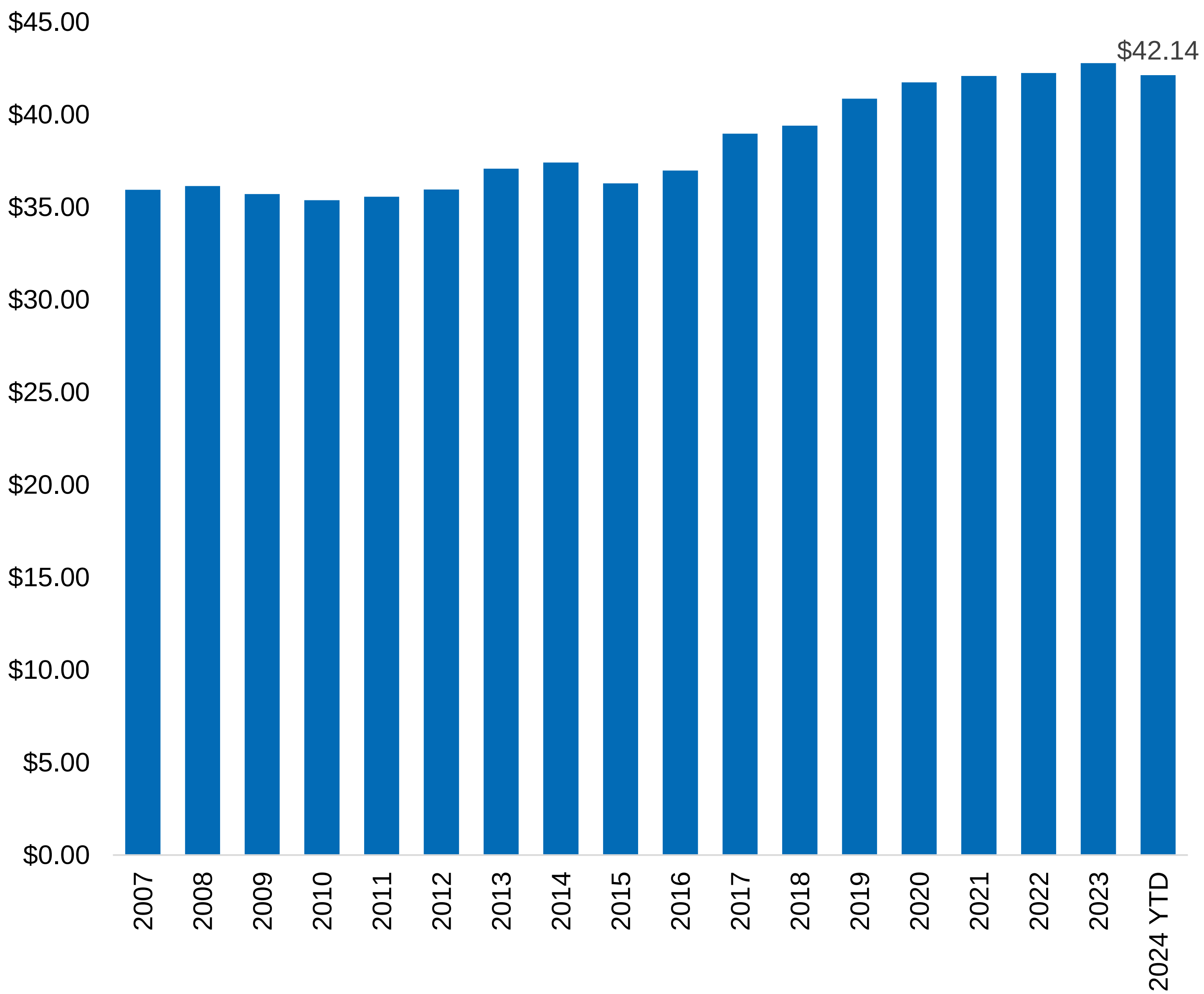


Source: Newmark Research, CoStar

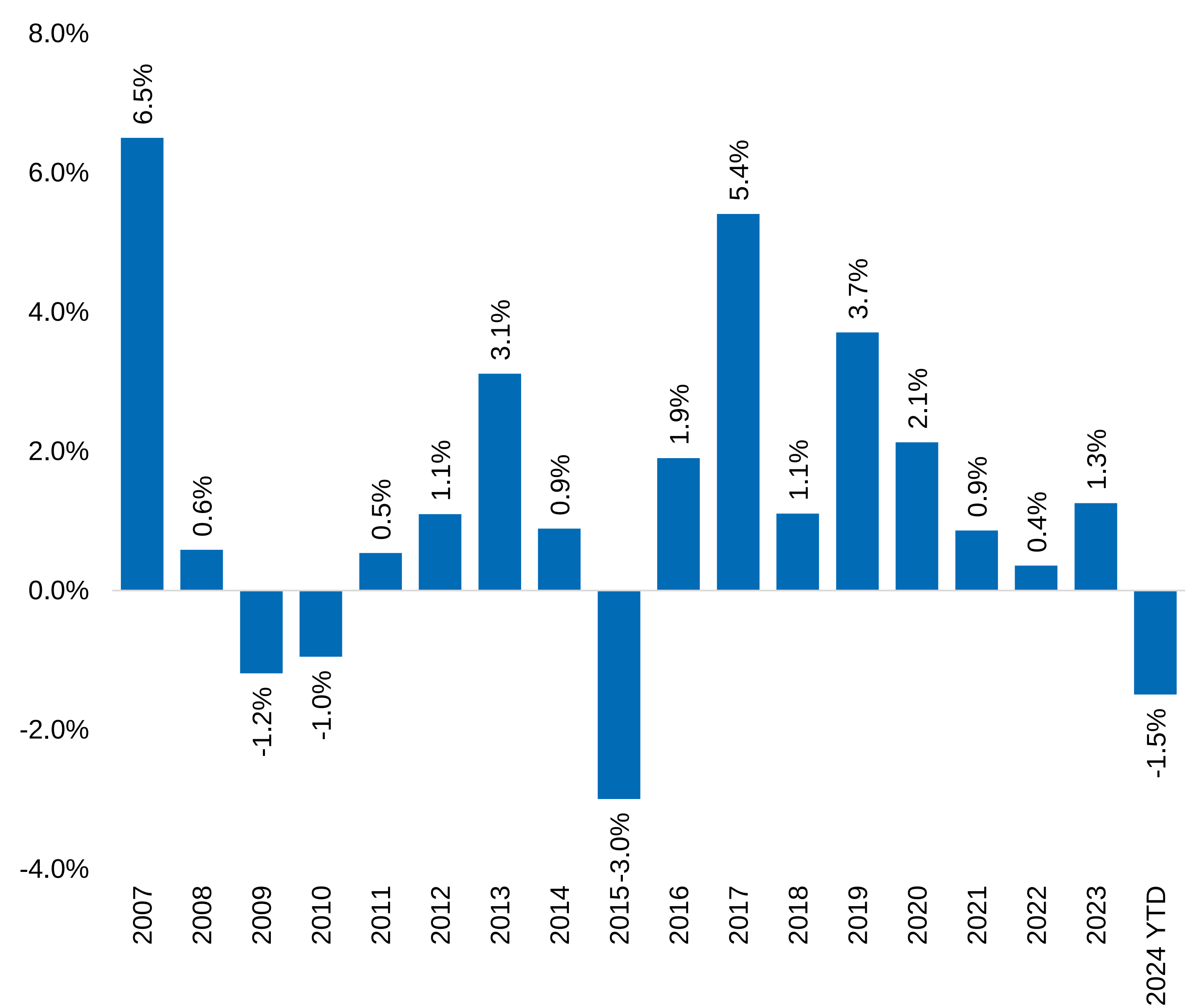
Market Experiences Slight Rent Decline to Begin 2024

For the first time since 2015, the market experienced a decline in rents to begin 2024. Although rents declined 1.5% during Q1 2024, rents were flat year-over-year. The market will look to bounce back during the rest of the year, as the market has experienced annual rent increases of 1.6% over the last decade.

Office Average Asking Rent, $/SF, FS



Year-over-Year Asking Rent Growth Rate

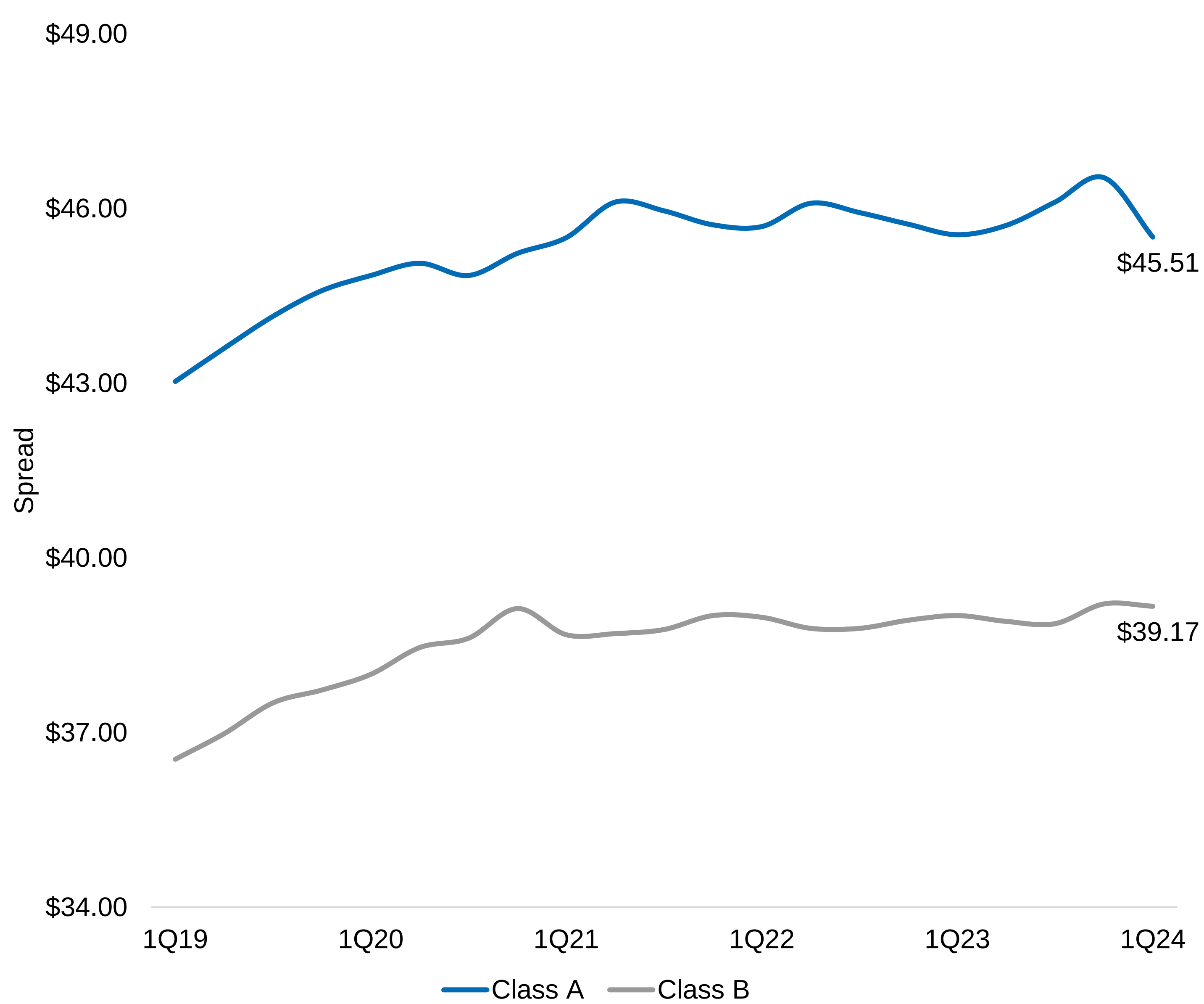


Source: Newmark Research, CoStar

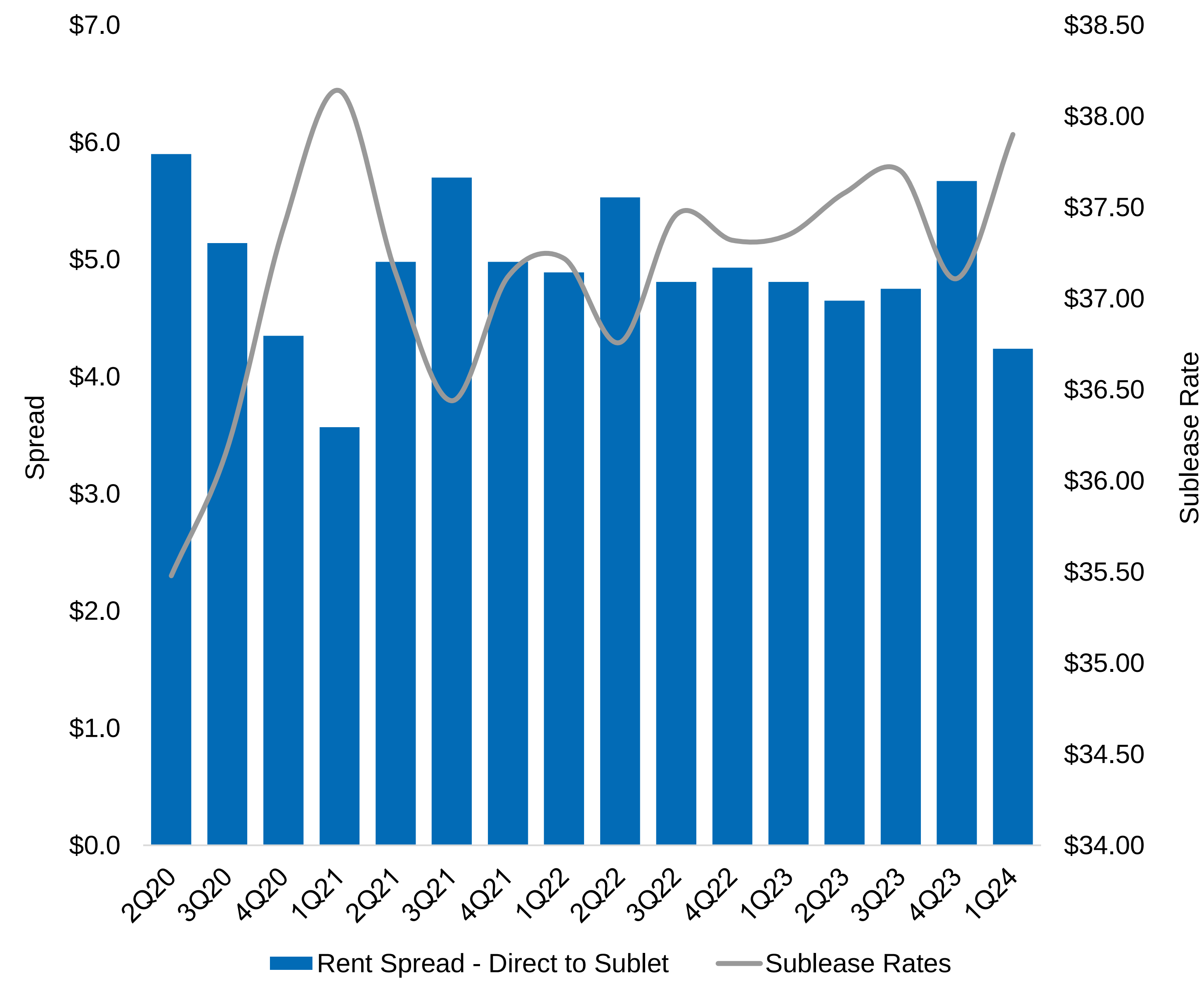
Class A Rents Dip Slightly While Class B Rents Remain Relatively Flat

Class A asking rents dipped slightly during Q1 2024, ending the quarter at $45.51 PSF, while Class B asking rents stayed relatively flat, ending the quarter at $39.17. Despite a soft leasing market, asking rents have remained resilient as asset owners seek to maintain face rates. Trophy and Class A+ space continues to outperform the broader market.

Class A and Class B Asking Rents



Sublease Rates



Source: Newmark Research, CoStar

Leasing Activity Dominated by Renewals

Despite negative absorption, leasing activity continues, albeit at a slower pace. Major first-quarter transactions were comprised entirely of lease renewals, with the top three transactions occurring within the District, while the next two transactions occurred in Northern Virginia.

Notable 1Q24 Lease Transactions

Tenant	Building(s)	Submarket	Type	Square Feet
The Washington Post	1301 K Street, NW	East End	Lease Renewal	299,873
District Office of Chief Financial Affairs	1101 4th Street, SW	Southwest	Lease Renewal	263,097
Finnegan	901 New York Avenue, NW	East End	Lease Renewal	214,258
General Dynamics	7770 Backlick Road	Springfield/Burke	Lease Renewal	114,867
Boeing	14660 Lee Road	Rt. 28 South	Lease Renewal	80,339

Source: Newmark Research

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Market Statistics

Washington Metro Office Market Overview

Market Statistics By Class

	Total Inventory (SF)	Overall Vacancy	Overall Availability	1Q 2024 Absorption (SF)	YTD Absorption (SF)	Quarter Deliveries (SF)	YTD Deliveries (SF)	Under Construction (SF)	Asking Rent (Price/SF)
Washington Metro	**368,222,259**	**21.0%**	**25.4%**	**-1,200,282**	**-1,200,282**	**276,000**	**276,000**	**2,047,723**	**$42.14**
Class A	225,032,050	20.1%	26.1%	-564,575	-564,575	276,000	276,000	2,047,723	$45.51
Class B	110,574,949	24.0%	26.0%	-377,986	-377,986	0	0	0	$39.17
Class C	32,615,260	16.8%	18.7%	-257,721	-257,721	0	0	0	$29.60
Washington D.C.	**130,892,045**	**20.3%**	**26.1%**	**-80,594**	**-80,594**	**0**	**0**	**735,906**	**$55.41**
Class A	81,139,426	17.4%	24.5%	115,627	115,627	0	0	735,906	$60.98
Class B	45,648,880	26.1%	29.3%	-199,107	-199,107	0	0	0	$48.87
Class C	4,103,739	11.7%	20.7%	2,886	2,886	0	0	0	$41.75
Northern Virginia	**163,420,732**	**22.1%**	**25.9%**	**-759,433**	**-759,433**	**0**	**0**	**1,074,817**	**$35.32**
Class A	101,893,835	21.9%	27.7%	-460,930	-460,930	0	0	1,074,817	$38.13
Class B	42,498,784	24.2%	24.3%	-132,692	-132,692	0	0	0	$31.88
Class C	19,028,113	18.5%	19.5%	-165,811	-165,811	0	0	0	$29.43
Suburban Maryland	**73,909,482**	**19.6%**	**23.2%**	**-360,255**	**-360,255**	**276,000**	**276,000**	**237,000**	**$31.76**
Class A	101,893,835	20.6%	25.3%	-219,272	-219,272	276,000	276,000	237,000	$34.36
Class B	42,498,784	19.6%	22.3%	-46,187	-46,187	0	0	0	$28.78
Class C	19,028,113	15.4%	16.2%	-94,796	-94,796	0	0	0	$24.75

Source: Newmark Research, CoStar

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Newmark has implemented a proprietary database and our tracking methodology has been revised. With this expansion and refinement in our data, there may be adjustments in historical statistics including availability, asking rents, absorption and effective rents. Newmark Research Reports are available at nmrk.com/insights.

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