

Suburban Maryland Office Market

Demand Softens, but Modest Construction Pipeline Will Aid Market's Rebound

Demand for office space in Suburban Maryland softened during the second quarter of 2021. Net absorption totaled -277,919 square feet. As an ongoing result of disruption related to COVID-19, leasing activity was limited. The overall vacancy rate was 16.0% at the end of the second quarter, an increase of 30 basis points from the previous quarter and an increase of 200 basis points from a year ago. Vacancy will likely continue to increase in the latter part of 2021, as 380,000 square feet is scheduled to deliver in the third quarter with 0.0% preleased. The average asking rental rate ended the second quarter at \$29.23/SF, an increase of 2.0% from \$28.67/SF in the second quarter of 2020. While it may seem counterintuitive that asking rents continued to increase despite occupancy losses, the construction pipeline and recently delivered product includes high-quality space with asking rates that match the quality, which boosts the average asking rent. By contrast, effective rents are under downward pressure as concessions remain high to lure tenants in an environment of tepid demand.

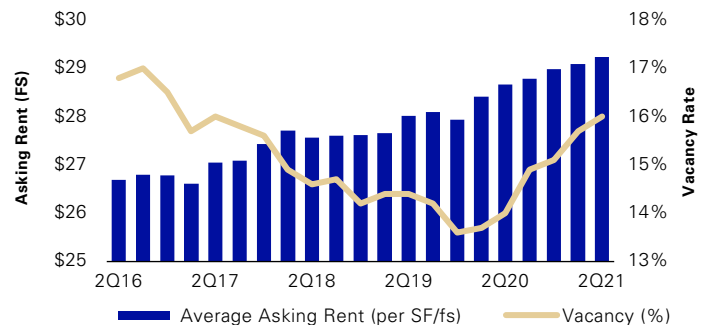
As of second-quarter 2021, 1.3 million square feet of office space is under construction in Suburban Maryland in four projects, excluding renovations and owner-occupied buildings. The pipeline is approximately 63.4% preleased. There were no office deliveries in the second quarter of 2021. The most notable projects currently under construction will deliver in the third quarter of 2021 and the third quarter of 2022, respectively. The first, Avocet Tower at 7373 Wisconsin Avenue, is 380,000 square feet and 0.0% preleased, although the first through sixth floors will be Marriott Autograph Collection property, with office space above. A second notable project under construction is Marriott International's new Bethesda headquarters at 7750 Wisconsin Avenue. It will be 726,000 square feet and is fully preleased by Marriott. Marriott is an example of how office tenants are adapting space to the new normal of work and the shifting power dynamic between employers and employees. Marriott and many other tenants are evolving both their corporate footprint and their employees' schedules to maximize the value of office space while providing the flexibility top talent is demanding.

Current Conditions

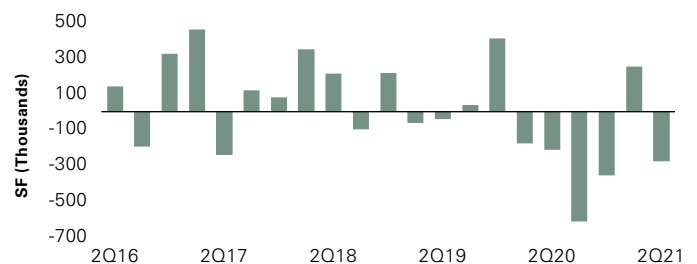
- Suburban Maryland registered -277,919 square feet of absorption during the second quarter.
- The vacancy rate is up 30 basis points from last quarter and up 200 basis points from one year ago, to 16.0%. Demand slowed materially in 2020 and is likely to remain modest during the rest of 2021 before accelerating in 2022.
- 1.3 million square feet is under construction; groundbreakings are limited given the easing demand for office space.

Market Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION



Market Summary

	Current Quarter	Prior Quarter	Year Ago Period	24-Month Forecast
Total Inventory (SF)	75.0 M	75.4 M	74.5 M	↑
Vacancy Rate	16.0%	15.7%	14.0%	↑
Quarterly Net Absorption (SF)	-277,919	252,357	-213,181	↓
Average Asking Rent/SF	\$29.23	\$29.09	\$28.67	↑
Under Construction (SF)	1.3 M	1.3 M	2.3 M	↓
Deliveries (SF)	0	932,767	0	↑

Class A Demand Negative but Slowly Rebounding

Demand in Suburban Maryland's Class A office market was negative during the second quarter of 2021, registering -73,604 square feet of net absorption. Class A vacancy, which registered 16.2% at the end of the second quarter, increased 200 basis points over the past year. Class A asking rents averaged \$31.60/SF, up 2.9% from \$30.70/SF measured one year ago. Suburban Maryland's construction pipeline is 1.3 million square feet, which will expand the supply of Class A inventory. Demand should follow suit as the effects of the pandemic wind down, although some tenant requirements will shrink compared with pre-pandemic needs as office design evolves.

Already Booming Maryland Biotech Industry is Further Bolstered by Foreign Investment

While even before the pandemic Suburban Maryland was a hub for life sciences and biotech companies, that trend has been amplified over the past year. Companies that have been focusing on COVID-19 vaccines are now moving beyond the pandemic and returning to other projects. One result is increased foreign investment into the American, and especially the Maryland, biotech sector. This trend has been led by the arrival of the Australian company Ellume. Ellume has been active in the Maryland area in the past year, having signed a \$232.0 million deal with the Department of Defense to produce at-home COVID tests. The company announced that it will move into 180,000 square feet in Frederick, its first foray into the American commercial real estate market.

Ellume plans to create 1,500 jobs by 2022 as it and other companies refocus on broader disease testing and treatment. Although the London-based biopharmaceutical company Autolus backed out of an 85,000-square-foot lease, its space was immediately taken by another cell therapy company. Autolus specializes in T therapy for treating cancer, an area of research that has helped other companies work to find solutions to COVID-19. TCR² therapeutics is a cell therapy company that will move into the would-be Autolus space, and starting in 2023, the firm will extend Maryland's biotech boom beyond COVID-19 work. This interest from abroad reflects the growing strength of Suburban Maryland's biotech sector, a high-wage industry that will require both lab and traditional office space.

Suburban Maryland Outlook

Soft office fundamentals in Suburban Maryland are likely to slowly tighten over the next two years; leasing activity remains limited for now as tenants still grapple with the effects of COVID-19. Leasing activity is likely to accelerate, though, in the latter part of this year as tenants re-board throughout the summer and fall and make decisions about future office space needs. Marriott has led the way, having changed the office plan for its new headquarters. The hotelier's decision to focus on communal workspace as opposed to smaller individual offices reflects a common change in work preferences; many people no longer want to go into the office for work they can do at home, instead opting to come in most often for meetings and collaborations.

The pipeline of office deliveries in Suburban Maryland over the next two years is higher than last quarter's, at 1.7% of inventory. It is concentrated in Bethesda, with a 63.4% pre-lease rate overall. Newmark Research projects that Suburban Maryland's overall vacancy rate will increase to 17.3% by the end of the second quarter of 2023, a consequence of the long-term workforce changes caused by COVID-19.

As the prioritization of COVID-related research and funding diminishes, cancer and cell research will become more prominent. Maryland is a significant player in these fields, as domestic and international companies flock to it for its proximity to the NIH and other government organizations. President Biden is a major proponent of drastically increasing and improving cancer research; in part because of the death of his son to cancer in 2015, before and during his presidency, Biden has pushed for more funding and attention for cancer and cell research. Also notable for the Suburban Maryland office market is the Maryland Biotechnology Investment Incentive Tax Credit and Montgomery County's local biotech tax credit, both of which benefit existing companies and encourage new domestic and international companies to have space or a headquarters in the area.

For additional information on the Washington metropolitan area economy and office market outlook, please visit the [Mid-Atlantic Market Reports](#) page at nmrk.com.

Notable 2Q 2021 Lease Transactions

Tenant	Building	Submarket	Type	Square Feet
Consumer Product Safety Commission	4330 East-West Highway	Bethesda/Chevy Chase	Lease Renewal	126,266
Maxcyte	9713 Key West Avenue	North Rockville	Direct Lease	67,000
GSA	8490 Progress Drive	Frederick	Direct Lease	27,025
Catalyst Campus	5801 University Research Court	College Park	Direct Lease	27,000
INKY	5825 University Research Court	College Park	Lease Expansion	17,000

Notable Recent Sales Transactions

Building	Submarket	Sale Price	Price/SF	Square Feet
1700 Rockville Pike	Rockville	\$32,800,000	\$201	163,000
Bowie Corporate Center	Bowie	\$24,800,000	\$190	130,650

Submarket Statistics—All Classes

	Total Inventory (SF)	Direct Vacancy Rate	Overall Vacancy Rate	2018 Absorption (SF)	2019 Absorption (SF)	2020 Absorption (SF)	2Q 2021 Absorption (SF)	YTD 2021 Absorption (SF)
Suburban Maryland	75,053,978	15.0%	16.0%	680,170	345,945	-1,356,741	-277,919	-25,562
Beltsville	1,457,852	28.1%	28.5%	77,319	-1,062	-19,452	3,506	-884
Bethesda	10,963,039	15.9%	18.6%	-152,116	187,647	-459,758	19,426	-39,247
Bowie	1,229,062	15.5%	15.8%	45,968	4,239	-30,591	-15,903	-6,588
College Park	3,729,450	11.3%	11.3%	66,443	197,669	-152,144	16,765	27,686
Gaithersburg	3,526,178	10.0%	10.3%	30,598	-226	-83,535	-6,538	-22,655
Germantown	2,308,113	22.7%	23.6%	-68,967	-42,624	-104,609	17,887	-12,512
Greenbelt	2,869,682	22.1%	22.5%	43,056	130,707	-49,391	14,422	-3,010
Landover/Lanham/Largo	4,597,337	14.3%	14.4%	166,268	5,221	21,612	-28,012	-15,077
Laurel	1,842,894	23.3%	23.8%	26,511	-95,067	-15,004	-19,353	-82,019
North Rockville	11,693,189	15.7%	16.8%	243,161	296,245	-381,707	-98,244	-170,941
North Bethesda	9,836,014	14.2%	15.6%	221,345	131,710	22,231	-99,461	-95,126
Rockville	8,334,684	13.0%	14.0%	-113,513	94,590	-78,405	-46,676	-193,073
Silver Spring	9,756,065	13.6%	14.3%	128,883	-639,090	-1,496	-29,525	-5,674
Southern Prince George's	2,910,419	8.7%	8.8%	-34,786	75,986	-24,492	-6,213	593,558

Market Statistics By Class

	Total Inventory (SF)	Direct Vacancy Rate	Overall Vacancy Rate	2018 Absorption (SF)	2019 Absorption (SF)	2020 Absorption (SF)	2Q 2021 Absorption (SF)	YTD 2021 Absorption (SF)
Suburban Maryland	75,053,978	15.0%	16.0%	680,170	345,945	-1,356,741	-277,919	-25,562
Class A	41,537,836	14.7%	16.2%	533,517	342,676	-827,373	-73,604	368,318
Class B	23,166,110	15.6%	16.3%	171,921	115,306	-344,451	-185,424	-314,499
Class C	10,350,032	14.7%	14.8%	-25,268	-112,037	-184,917	-18,891	-79,381

Submarket Statistics—All Classes

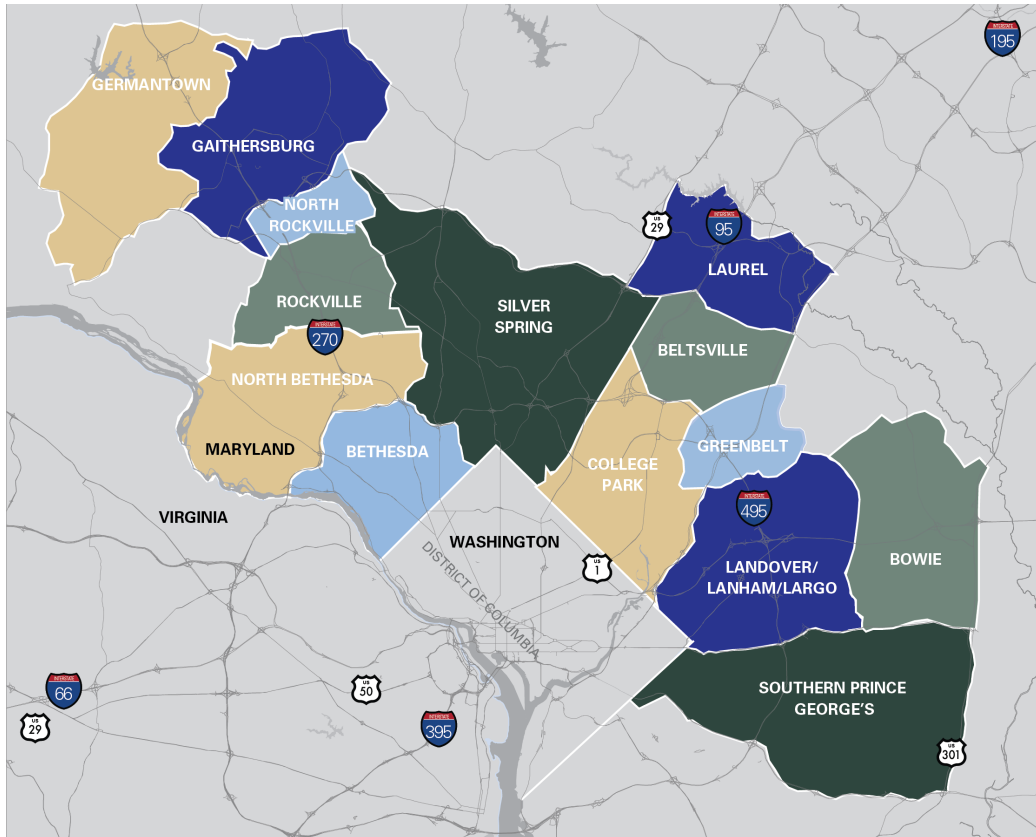
	Total Inventory (SF)	Class A Asking Rent (Price/SF)	Class B Asking Rent (Price/SF)	Overall Asking Rent (Price/SF)	2Q 2021 Deliveries (SF)	YTD 2021 Deliveries (SF)	Under Construction (SF)
Suburban Maryland	75,053,978	\$31.60	\$27.48	\$29.23	0	932,767	1,305,860
Beltsville	1,457,852	\$22.68	\$17.51	\$22.29	0	0	0
Bethesda	10,963,039	\$46.30	\$38.78	\$41.15	0	358,000	1,108,664
Bowie	1,229,062	\$26.09	\$16.44	\$25.06	0	0	0
College Park	3,729,450	\$25.77	\$24.00	\$24.02	0	0	0
Gaithersburg	3,526,178	\$33.21	\$16.76	\$28.87	0	0	0
Germantown	2,308,113	\$26.88	\$23.14	\$24.74	0	0	0
Greenbelt	2,869,682	\$23.10	\$21.72	\$22.45	0	0	0
Landover/Lanham/Largo	4,597,337	\$21.96	\$21.54	\$21.61	0	0	100,000
Laurel	1,842,894	\$22.50	\$20.68	\$20.99	0	0	0
North Rockville	11,693,189	\$30.35	\$24.82	\$28.25	0	0	97,196
North Bethesda	9,836,014	\$29.15	\$28.38	\$28.03	0	0	0
Rockville	8,334,684	\$33.32	\$28.13	\$31.22	0	0	0
Silver Spring	9,756,065	\$32.30	\$25.77	\$28.11	0	0	0
Southern Prince George's	2,910,419	\$32.00	\$23.96	\$23.28	0	574,767	0

Market Statistics By Class

	Total Inventory (SF)	Class A Asking Rent (Price/SF)	Class B Asking Rent (Price/SF)	Overall Asking Rent (Price/SF)	2Q 2021 Deliveries (SF)	YTD 2021 Deliveries (SF)	Under Construction (SF)
Suburban Maryland	75,053,978	\$31.60	\$27.48	\$29.23	0	932,767	1,305,860
Class A	41,537,836	\$31.60	NA	\$31.60	0	932,767	1,305,860
Class B	23,166,110	NA	\$27.48	\$27.48	0	0	0
Class C	10,350,032	NA	NA	\$24.82	0	0	0

Note: Asking rents are quoted on a full service basis.

Suburban Maryland Office Submarkets



Methodology

Market statistics are calculated from a base building inventory of office properties 20,000 SF and larger that are deemed to be competitive in the Washington Metro Area office market. Properties that are more than 75% owner-occupied and federally owned buildings are generally excluded from inventory.

Glossary

Asking Rental Rate: The dollar amount asked by landlords for direct available space (not sublease), expressed in dollars per square foot per year. Average asking rents are calculated on a weighted average basis, weighted by the amount of available space. Asking rents are quoted on a full service basis, meaning all costs of operation are paid by the landlord up to a base year or expense stop.

Class A: The most prestigious buildings competing for premier office users with rents above average for the area. Class A buildings have high-quality standard finishes, state-of-the-art systems, exceptional accessibility and a definite market presence.

Class B: Buildings competing for a wide range of users with rents in the average range for the area. Class B building finishes are fair to good for the area and systems are adequate, but the building cannot compete with Class A at the same price.

Class C: Buildings competing for tenants requiring functional space at rents below the area average.

Deliveries: Projects that have completed construction and received a certificate of occupancy.

Net Absorption: The net change in physically occupied space from one quarter to the next. **Year-to-Date (YTD) Net Absorption** is the net change in physically occupied space from the start of the calendar year to the current quarter. Net absorption is counted upon physical occupancy, not upon execution of a lease.

Sublease: Sublease space is offered and marketed as available by the current tenant, rather than directly from the owner.

Under Construction: Properties undergoing ground-up construction in which work has begun on the foundation. Properties that have only undergone grading or other site work are not included as under construction.

Under Renovation: Properties undergoing significant renovations that require all tenants to be out of the building. These properties are removed from inventory during the renovation period and delivered back to inventory upon completion of the renovations. These properties are not included in under construction totals.

Vacancy Rate: The amount of space that is physically vacant, expressed as a percentage of inventory. (Space that is being marketed as available for lease but is largely occupied is not included in the vacancy rate.) The **Overall Vacancy Rate** includes all physically vacant space, both direct and sublease, while the **Direct Vacancy Rate** includes only direct space.

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