



Philadelphia Office Market

Positive Absorption in 4Q21; Omicron Variant Poses Problems for Early 2022

As of the fourth quarter of 2021, the Philadelphia office market continues to face return-to-office issues related to the COVID-19 pandemic. After struggling with the Delta variant in the late summer and fall of 2021, the threat of a new variant known as Omicron has once again forced businesses to reassess the reboarding plans many had for after the new year. According to Kastle Systems recent occupancy data, 37.2% of Philadelphia’s workforce has made a return to the office which is below the major metro average of 39.8%. More positively, this occupancy data is 300 basis points better than the 34.2% reported by Kastle Systems in the third quarter of 2021, so people are returning to the office, albeit slowly.

The Philadelphia Central Business District (CBD) office market is feeling the effects of the ongoing pandemic more deeply than adjacent suburban markets. According to Center City District’s Philadelphia December 2021 report, as of October, the CBD has only recovered 46.0% of the jobs lost from February 2020 to April of 2020. The average weekly SEPTA ridership also remains down significantly from pre-pandemic levels; 5.8 million riders per week in February of 2020 compared with 3.1 million in October 2021. The bright spot in the CBD is the University City submarket, where the life sciences sector is undergoing a period of dynamic growth.

Current Conditions

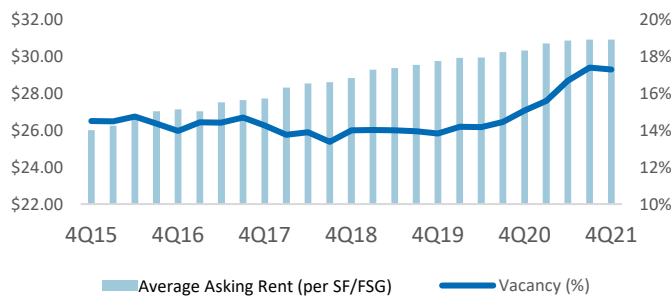
- Absorption was positive in the fourth quarter of 2021 totaling 481,861 square feet.
- Available sublease space rose to 4.3 million square feet market-wide.
- Overall vacancy rate declined to 17.3% in the fourth quarter.

Market Summary

	Current Quarter	Prior Quarter	Year Ago Period	12-Month Forecast
Total Inventory (SF)	109.7M	109.3M	109.3M	↑
Vacancy Rate	17.3%	17.4%	15.1%	↓
Quarterly Net Absorption (SF)	482K	-827K	-686K	↑
Average Asking Rent/SF	\$30.93	\$30.93	\$30.36	↑
Under Construction (SF)	1.6M	2.0M	2.2M	↑

Market Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION



RESEARCH Q4 2021

While the Suburban office market faces issues of its own related to COVID-19, it appears to have weathered the storm better than the Philadelphia CBD. Although some submarkets continue to struggle with occupancy, Conshohocken, Radnor/Main Line, King of Prussia and Bala Cynwyd have been performing well, particularly during the second half of 2021, and all of them except for Radnor/Main Line reported positive absorption in the fourth quarter.

Both the suburbs and Downtown markets had solid performances in the fourth quarter of 2021. However, the combined office sectors finished the year with 1.5 million square feet of negative absorption, the majority of which was realized in the CBD. As a result, the overall vacancy rate increased to 17.3% year-end 2021, a 220-basis point increase over the past year. Asking rental rates for all Classes increased by 1.8% year-over-year to \$30.93/SF. Class A asking rates also escalated over the past year to \$34.56/SF, a 1.5% hike.

Philadelphia Central Business District

The overall vacancy rate in the Philadelphia CBD declined by 20 basis points in the fourth quarter of 2021, dropping from 17.7% in the third quarter to 17.5%. While deal velocity remains slow, fourth-quarter numbers indicate a slight improvement in office market conditions. There was a 3.9% increase in available sublease space during the quarter, but these additions came at the slowest pace since the start of the pandemic. Less positive is the fact that most of the sublease space added over the past 18 months remains available. Year-end 2021 absorption totaled negative 1.2 million square feet; however, the fourth quarter metric was positive at 101,278 square feet.

Much like last quarter, tenants remain reluctant to commit to space long term in the CBD. Short-term leases for both new transactions and renewals remain the prevalent trend. The current hybrid work model is causing larger tenants whose leases are due to expire to shrink the size of their footprint. That same dynamic is responsible for increased demand we see for coworking space. High vacancy and low demand have caused some landlords to consider conversions from office to residential or life science product.

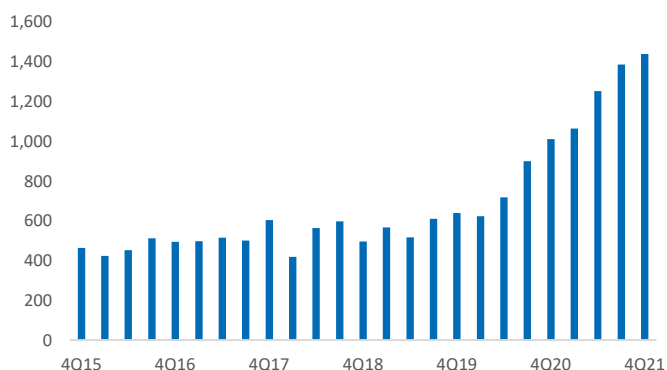
The brightest spot in the picture is the life science industry which remains strong in Philadelphia, particularly in University City where vacancy is presently 9.4%, considerably better than the Downtown office market's 17.5%. The overall success seen in University City and other strong life science submarkets, such as the Navy Yard and areas of the suburbs, explains why many office landlords in other Center City submarkets want to convert their space to accommodate this alternative use. There is a strong demand for additional life science space in University City, which will be fulfilled when the 1.3 million square feet of new construction delivers in 2022 and 2023, most of which is suited for life science tenants.

Asking rental rates for all Classes declined in the fourth quarter of 2021 to \$34.51/SF, a 0.4% drop from the third quarter of 2021. Class A asking rates also decreased by 0.6% to an average of \$38.05/SF this quarter. The drop, and other concessions such as greater amounts of free rent and higher improvement allowances, reflect the aggressive responses landlords have been making to fill space, especially for longer-term leases.

While leasing velocity remains limited, some significant agreements were consummated during the fourth quarter of 2021. At 1234 Market Street, PHDC and the City of Philadelphia renewed for 68,584 square feet and 54,080 square feet, respectively. Plenary Infrastructure Philadelphia leased 59,991 square feet at 10 Penn Center. The Children's Hospital of Philadelphia signed a lease for 54,660 square feet at Cira Centre North. Life science tenant, Imvax, expanded its lease, taking 41,000 square feet of additional space at The Curtis. New to the Philadelphia office market, Harsco Corp. announced it will be relocating its corporate headquarters from Camp Hill, Pennsylvania to Two Logan Square in the Philadelphia CBD. Harsco Corp. leased 22,550 square feet and will relocate during the second quarter of 2022. Naxion also renewed its lease at 1835 Market Street for 22,145 square feet.

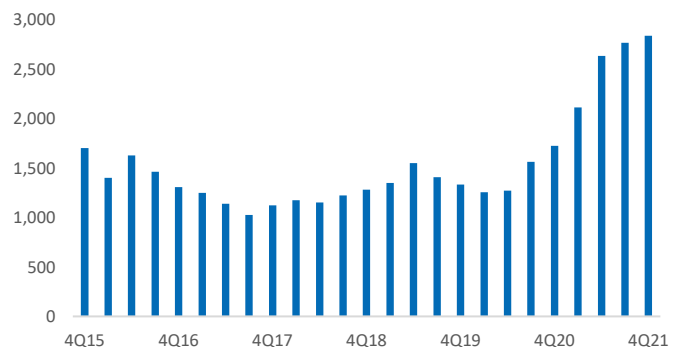
Sublease Volume: Philadelphia CBD

TOTAL SF, THOUSANDS



Sublease Volume: Philadelphia Suburbs

TOTAL SF, THOUSANDS



Philadelphia Suburbs

The Suburban Philadelphia office market experienced a decline in vacancy quarter-over-quarter, from 17.2% to 17.1% currently. However, there was an increase in the vacancy metric over the course of the year equal to 180 basis points. Several submarkets had strong fourth quarters and overall absorption during this period totaled 580,583 square feet. Despite the noted improvements year-end absorption totaled negative 385,677 square feet. Like the Philadelphia CBD, sublease space additions slowed during the fourth quarter of 2021 although there was still an increase of 2.6% compared with last quarter.

While the size of deals increased during Q421, short-term leases on both renewals and new transactions continued as the norm throughout the suburbs. Some submarkets, such as Bucks County and Horsham/Willow Grove, are struggling with occupancy and negative absorption, while traditionally stable markets, like Conshohocken, King of Prussia, Bala Cynwyd, and Radnor/Main Line, have had solid leasing velocity and are performing well. Larger deals in the market are few and far between; however, a number of medium-sized transactions landed in the fourth quarter and there is a notable amount of ongoing activity in this same size range.

Deal signings and other activity was robust during the fourth quarter of 2021: Conshohocken saw 383,176 square feet of positive absorption, due mostly to the construction completion of the 429,000-square-foot SORA

West building at 3 Fayette Street. The new building will serve as AmerisourceBergen's new global headquarters. The King of Prussia submarket had multiple notable deals inked this quarter, including IQVIA leasing 54,427 square feet at 650 East Swedesford Road and Infinite Blue taking 36,793 square feet of space at 2500 Monroe Boulevard in Norristown. In the Central/South Delaware County submarket, the largest lease of the quarter and year was signed by Vanguard at 3801 West Chester Pike in the Ellis Preserve in Newtown Square. In Fort Washington, Nutrisystem leased 53,026 square feet at 1100 Virginia Drive in the Fort Washington Technology Center.

On the investment sales side, the largest building to trade during the fourth quarter was 45 Liberty Boulevard in Malvern's Great Valley Corporate Center. The 137,000-square-foot building was purchased by Equus Capital Partners from FLD Group for \$36.3 million or \$265/SF.

In conclusion, leasing activity in the suburbs is expected to increase further in 2022. Traditionally stable submarkets will continue to outperform others. Interest in Class A trophy assets will increase and exceed that of other types of office product. Expect certain industries, such as eds and meds and private equity companies, to also continue to be active in the market in 2022.

Philadelphia CBD Lease/User Transactions

Tenant	Submarket	Building	Type	Square Feet
PHDC	East Market	1234 Market Street	Renewal	68,584
Plenary Infrastructure Philadelphia	West Market	10 Penn Center	New Lease	59,991
Children's Hospital of Philadelphia	University City	Cira Centre North	New Lease	54,660
City of Philadelphia	East Market	1234 Market Street	Renewal	54,080
Imvax	Independence Square	The Curtis	Expansion	41,000
Harsco Corp.	West Market	Two Logan Square	New Lease	22,550

Philadelphia Suburbs Lease/User Transactions

Tenant	Market	Building	Type	Square Feet
Vanguard	Central/S Delaware County	3801 West Chester Pike	New Lease	240,000
IQVIA	King of Prussia	650 East Swedesford Road	New Lease	54,427
Nutrisystem	Fort Washington	1100 Virginia Drive	New Lease	53,026
Infinite Blue	King of Prussia	2500 Monroe Boulevard	New Lease	36,793

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	1,602,000	17.5%	101,278	-1,156,589	\$38.05	\$30.34	\$34.51
East Market	6,331,084	-	18.9%	-22,773	1,683	\$36.39	\$27.38	\$32.15
Independence Square	5,380,384	-	17.9%	117,992	-46,672	\$30.21	\$32.75	\$31.30
University City	4,688,776	1,294,000	9.7%	23,580	-58,752	\$42.27	\$44.18	\$42.24
Walnut/South Broad	3,977,064	-	20.8%	13,145	-58,752	\$35.12	\$32.92	\$30.70
West Market	24,796,953	308,000	17.8%	-15,648	-783,653	\$38.59	\$28.58	\$35.83
Suburban Total	64,553,586		17.1%	380,583	-385,677	\$31.98	\$26.87	\$28.91
Bala Cynwyd	2,944,026	-	14.1%	3,994	-78,246	\$38.64	\$35.13	\$36.07
Blue Bell/Plymouth Meeting	8,531,020	-	18.7%	-16,724	5,653	\$29.76	\$23.95	\$26.25
Bucks County	7,984,833	-	20.8%	708	-150,609	\$28.44	\$23.26	\$24.85
Central/S Delaware County	5,304,227	-	17.0%	-62,921	151,500	\$29.15	\$26.00	\$27.31
Conshohocken	3,999,915	-	21.1%	393,176	238,086	\$44.99	\$36.49	\$42.13
Exton/Malvern	7,873,948	-	14.9%	28,424	-238,741	\$29.83	\$27.67	\$28.79
Fort Washington	3,561,466	-	13.3%	-36	106,879	\$27.61	\$25.93	\$26.89
Horsham/Willow Grove	4,382,604	-	28.9%	-160,441	-206,501	\$27.91	\$24.94	\$25.26
Jenkintown	1,081,401	-	21.2%	-2,713	46,764	\$25.60	\$22.33	\$24.62
King of Prussia	13,417,944	-	14.7%	132,971	-147,320	\$33.98	\$28.76	\$30.52
Radnor/Main Line	2,666,360	-	5.5%	-197	-39,459	\$45.44	\$32.52	\$42.07
Southern 202 Corridor	2,805,842	-	14.5%	64,342	-73,686	\$28.70	\$25.94	\$27.36
Market Totals	109,727,847	1,602,000	17.3%	481,861	-1,542,266	\$34.56	\$27.89	\$30.93

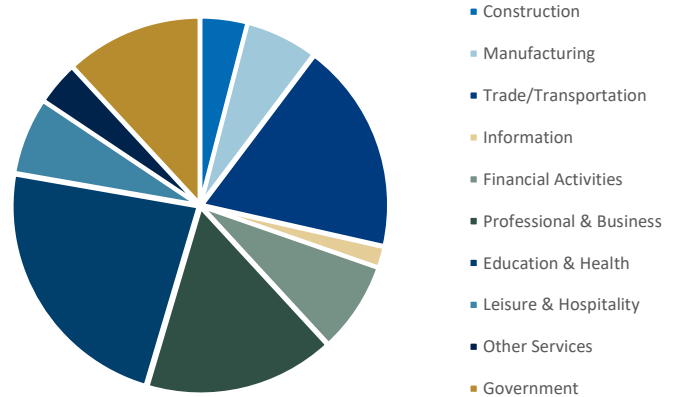
Economic Overview

The unemployment rate in the Philadelphia metropolitan statistical area (MSA) declined to 5.1% in the month of October, a significant drop from the 6.9% rate in July of 2021. All of the Philadelphia MSA's tracked industries have exhibited growth over the past 12 months. The leisure and hospitality (+16.3%), information (+6.5%), and construction (+5.4%) sectors demonstrated the most positive growth over that period.

While there will be some uncertainty heading into 2022 with the rising cases of the Omicron variant, both the Downtown and Suburban Philadelphia office markets are in a better place than they were a year ago at this time. Nearly 61.0% of Pennsylvania's population is fully vaccinated. People are slowly returning to the office and even with the hybrid model, companies have been successful over the past year. The return to the office matching something more like normal may be delayed throughout the winter but expect a notable increase in office occupancy by the summer of 2022.

Employment by Industry

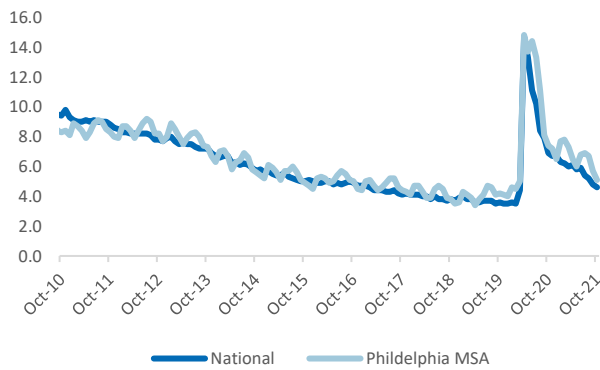
PHILADELPHIA MSA, 2021 ANNUAL AVERAGE



Source: U.S. Bureau of Labor Statistics, October 2021.

Unemployment Rate

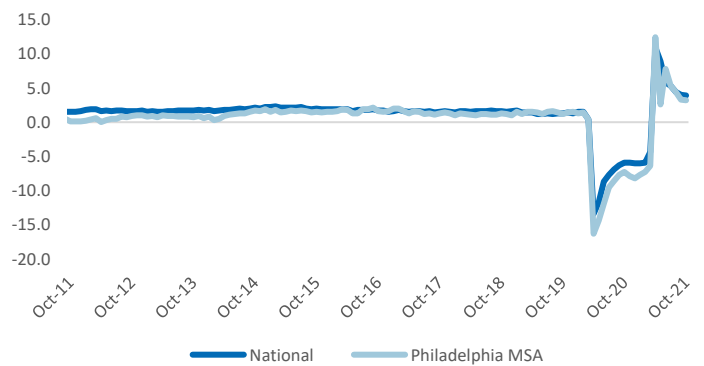
NOT SEASONALLY ADJUSTED



Source: U.S. Bureau of Labor Statistics, October 2021.

Payroll Employment (Total Nonfarm)

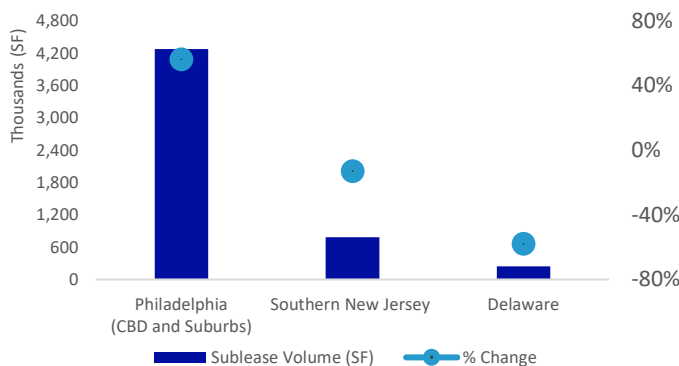
NOT SEASONALLY ADJUSTED, 12-MONTH % CHANGE



Source: U.S. Bureau of Labor Statistics, October 2021.

Greater Philadelphia Markets Sublease Analysis

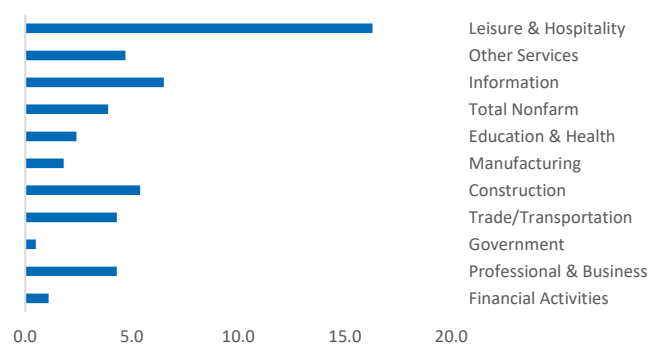
SQUARE FEET AND 12-MONTH % CHANGE, 3Q21



Source: Newmark Research, December 2021.

Employment Growth by Industry, October 2021

PHILADELPHIA MSA, 12-MONTH % CHANGE



Source: U.S. Bureau of Labor Statistics, October 2021.

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