Suburban Maryland Office Market

Market Remains Soft Despite Steady Vacancy and Inventory Growth

Suburban Maryland's office market recovery remained relatively soft in the fourth quarter of 2022. Net absorption totaled negative 9,042 square feet on the quarter. Instances of large occupancy losses were limited in the quarter, which enabled the market to see improvements, resulting in net-neutral quarterly absorption. Yet, the overall vacancy rate held steady at 18.8%. Concurrently, in the last year, vacancy has increased by 200 basis points. The average asking rental rate measured $30.96/SF, an increase of 2.0% from fourth-quarter 2021, but only 0.7% from last quarter.

Suburban Maryland's construction pipeline measured 491,746 square feet in the fourth quarter of 2022. The pipeline is approximately 6.1% preleased, indicating the potential for net new vacancy when future projects deliver. There was one delivery in the quarter at 9179 Central Avenue. Named Kingdom Square, this project delivered 100,000 square feet fully preleased by the Family Services and Veterans Affairs Department of the Prince George's County HHS. There are two expected deliveries for the first quarter of 2023, though one is WMATA's new facility at New Carrollton Station, which does not factor into Newmark's market statistics, as it is owner-occupied. The other expected delivery is the Alexandria Center at Shady Grove Life Sciences Center at 9808 Medical Center Drive. This 97,000 square-foot building is just over 20% preleased, which could increase vacancy, against the fully leased Kingdom Square delivery. Breaking ground in the quarter was 1600 Rockville Pike, which measures 237,000 square feet and is fully available for lease.

Current Conditions

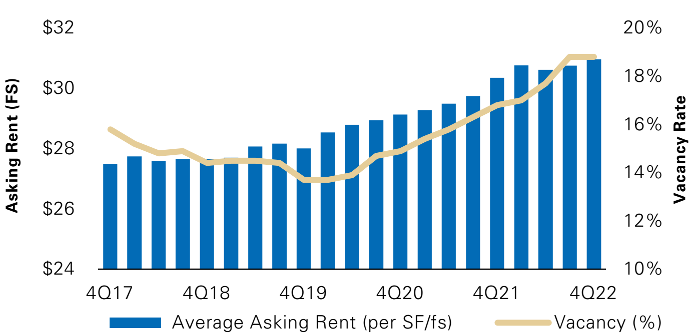
- Suburban Maryland recorded negative 9,042 square feet of net absorption in the fourth quarter, a significant improvement from the third quarter. However, year-to-date net absorption has been negative for the past seven consecutive quarters.
- Vacancy has increased 200 basis points from last year, to 18.8%.
- 491,746 square feet is under construction; groundbreakings remain limited given low demand, economic uncertainty, and cost of resources.
- Asking rents increased 2.0% over the last year and 0.7% since the third quarter, to $30.96/SF.

Market Summary

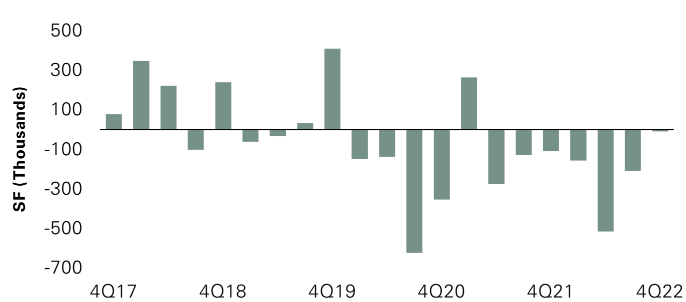
	Current Quarter	Prior Quarter	Year Ago Period	24-Month Forecast
Total Inventory (SF)	75.8 M	75.6 M	75.2 M	↑
Vacancy Rate	18.8%	18.8%	16.8%	↑
Quarterly Net Absorption (SF)	-9,042	-208,978	-109,569	→
Average Asking Rent/SF	$30.96	$30.75	$30.35	↑
Under Construction (SF)	491,746	354,746	923,196	↓
Deliveries YTD (SF)	826,000	726,000	1.3 M	↑

Market Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION



NEWMARK

Southern Maryland Steady Since the Pandemic

Since the beginning of the pandemic, southern Suburban Maryland's office market has fared better and exhibited steadier fundamentals than the northern portion of the region. With the southern border of Silver Spring as a dividing line, southern Maryland has experienced a relatively steadier office market during a challenging period, despite that area's inventory measuring just 18.3 million square feet, compared to the 57.5 million square feet of northern Maryland. Both areas have experienced measurable market softening since 2020; however, northern Maryland has recorded significantly more vacancy growth. Since the second quarter of 2020, southern Maryland's vacancy rate has increased 140 basis points, to 16.5%, while northern Maryland's vacancy has ballooned by 620 basis points, to 19.7%. Southern Maryland has also measured modestly negative absorption in 6 out of the last 11 quarters, but northern Maryland has not measured positive net absorption since the fourth quarter of 2019.

Possibly contributing to the relative stability of fundamentals in southern Maryland could be the presence of several long-term leases by the General Services Administration (GSA) on behalf of the government. The GSA has been consolidating its real estate footprint for over a decade, yet most of its Suburban Maryland leases are not scheduled to expire for at least several more years.

Northern Suburban Maryland is an anchor for the region's fast-growing life sciences industry, however the success of this economic driver has had relatively muted impacts on office market fundamentals, as biotech and pharmaceutical occupiers typically require industrial or flex space, as opposed to traditional office. Nonetheless, northern Maryland's office market conditions seem to be stabilizing as office-occupying tenants become more comfortable committing to long term real estate plans.

Montgomery County Looks to Densify Metro Ends

After years of focus on the development and densification of Bethesda from both work and play perspectives, Montgomery County looks to extend that momentum to the ends of the Metrorail line. The County's Council recently unanimously approved Thrive 2050, a plan aimed at densifying the ends of the Metro near Glenmont and Shady Grove. If implemented, more duplexes and triplexes will more efficiently densify areas of Suburban Maryland, especially around transportation centers like Silver Spring, Wheaton, and Glenmont. The plans are controversial because, although they aim to limit sprawl and encourage the use of public transportation, especially with the eventual support of the Purple Line, there are concerns about the ability of office demand in far-suburban, transit-oriented development hubs to support pricing of new construction. Low office demand in these markets could limit the diversification of new development nearby Metro stations. There is still optimism, though, that the plan, if implemented thoughtfully, will enable expanded use of public transportation, greater diversity, and more density along Metrorail's most suburban stations.

Suburban Maryland Outlook

Soft, but relatively steady market fundamentals in Suburban Maryland should persist in the coming quarters, resulting in net neutral demand. Recessionary pressures may slightly soften market conditions in early 2023 as tenants brace for near-term uncertainty. Suburban Maryland's construction pipeline increased from last quarter, measuring about 6.0% of inventory, yet 2023 is unlikely to see many deliveries. For a change, future new deliveries will be concentrated in submarkets outside of Bethesda, although the pipeline will decrease considerably over the next year unless new projects break ground. At the same time, though, new ground breakings are few and far between for the moment, as recessionary pressures, challenging interest rates, and high cost of construction and materials increase caution throughout the industry. Newmark Research projects that Suburban Maryland's overall vacancy rate will decrease to 18.6% by the end of the fourth quarter of 2024.

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 4Q 2022 Lease Transactions

Tenant	Building	Submarket	Type	Square Feet
Sodexo	915 Meeting Street	North Bethesda	Direct Lease	52,000
Gilbert Employment	8403 Colesville Road	Silver Spring	Direct Lease	16,972
Optimal Beginnings	6010 Executive Boulevard	North Bethesda	Direct Lease	13,011

Notable Recent Sales Transactions

Building	Submarket	Sale Price	Price/SF	Square Feet
6901-6905 Rockledge Drive	Bethesda	$69,500,000	$101	688,493
9601 Blackwell Road	Rockville	$48,000,000	$397	120,999
100 Lakeforest Boulevard	Gaithersburg	$14,500,000	$113	128,655

Submarket Statistics—All Classes

	Total Inventory (SF)	Direct Vacancy Rate	Overall Vacancy Rate	2019 Absorption (SF)	2020 Absorption (SF)	2021 Absorption (SF)	4Q 2022 Absorption (SF)	YTD 2022 Absorption (SF)
Suburban Maryland	**75,806,653**	**17.3%**	**18.80%**	**347,519**	**-1,266,230**	**-253,457**	**-9,042**	**-891,387**
Beltsville	1,520,332	21.3%	21.7%	-1,062	-19,452	49,657	26,341	35,604
Bethesda	12,145,588	18.5%	21.4%	187,647	-459,758	8,870	-39,429	574,089
Bowie	1,229,062	13.3%	13.5%	4,239	-30,591	-13,250	13,973	34,712
College Park	3,344,450	13.2%	13.2%	197,669	-152,144	37,062	10,685	-27,744
Gaithersburg	3,096,979	11.3%	11.5%	-226	-83,535	-3,712	2,119	-29,161
Germantown	2,111,498	23.1%	26.9%	-42,533	-28,957	-56,005	-7,828	-101,205
Greenbelt	2,869,682	22.3%	23.1%	130,707	-49,391	-30,366	-9,799	10,021
Landover/Lanham/Largo	4,700,350	18.4%	20.7%	5,221	21,612	-6,165	-45,208	-313,048
Laurel	1,842,894	18.8%	18.8%	-95,067	-15,004	-34,012	7,618	45,193
North Rockville	11,089,084	16.9%	18.5%	292,813	-375,820	-298,002	3,457	-10,891
North Bethesda	10,309,664	25.4%	27.0%	131,710	22,231	-102,870	51,025	-994,137
Rockville	8,928,235	14.1%	15.3%	99,505	-67,235	-316,790	-17,602	-107,168
Silver Spring	9,834,916	14.3%	15.2%	-639,090	-3,694	-85,973	-11,487	-15,395
Southern Prince George's	2,783,919	3.8%	3.8%	75,986	-24,492	598,099	7,093	7,743

Market Statistics By Class

	Total Inventory (SF)	Direct Vacancy Rate	Overall Vacancy Rate	2019 Absorption (SF)	2020 Absorption (SF)	2021 Absorption (SF)	4Q 2022 Absorption (SF)	YTD 2022 Absorption (SF)
Suburban Maryland	**75,806,653**	**17.3%**	**18.8%**	**347,519**	**-1,266,230**	**-253,457**	**-9,042**	**-891,387**
Class A	42,892,882	18.1%	19.9%	342,811	-797,822	330,386	29,803	-367,736
Class B	23,184,528	17.7%	19.1%	116,745	-283,491	-551,532	-63,069	-492,048
Class C	9,729,243	12.7%	13.0%	-112,037	-184,917	-32,311	24,224	-31,603

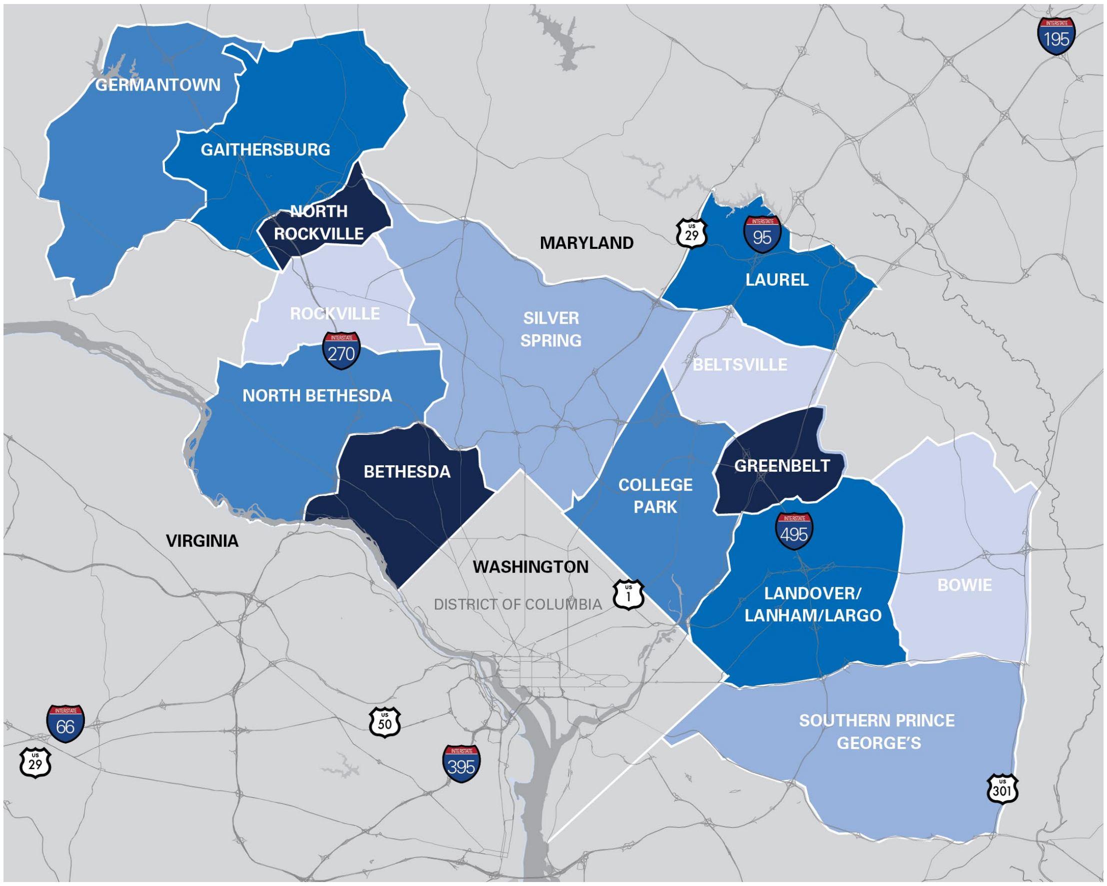
Submarket Statistics—All Classes

	Total Inventory (SF)	Class A Asking Rent (Price/SF)	Class B Asking Rent (Price/SF)	Overall Asking Rent (Price/SF)	4Q 2022 Deliveries (SF)	YTD 2022 Deliveries (SF)	Under Construction (SF)
Suburban Maryland	**75,806,653**	**$33.69**	**$27.82**	**$30.96**	**100,000**	**826,000**	**491,746**
Beltsville	1,520,332	$22.74	$18.00	$21.39	0	0	0
Bethesda	12,145,588	$47.39	$38.53	$43.84	0	726,000	0
Bowie	1,229,062	$25.72	$24.70	$25.60	0	0	0
College Park	3,344,450	$27.21	$23.10	$24.95	0	0	0
Gaithersburg	3,096,979	$30.37	$24.72	$28.24	0	0	0
Germantown	2,111,498	$27.04	$24.33	$25.41	0	0	0
Greenbelt	2,869,682	$23.80	$21.83	$22.79	0	0	0
Landover/Lanham/Largo	4,700,350	$22.35	$22.94	$22.81	100,000	100,000	0
Laurel	1,842,894	$22.50	$20.81	$21.02	0	0	0
North Rockville	11,089,084	$30.32	$25.51	$28.95	0	0	97,196
North Bethesda	10,309,664	$29.45	$30.53	$29.43	0	0	157,550
Rockville	8,928,235	$35.04	$30.91	$33.46	0	0	237,000
Silver Spring	9,834,916	$31.93	$26.21	$28.09	0	0	0
Southern Prince George’s	2,783,919	$31.97	NA	$23.40	0	0	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)	4Q 2022 Deliveries (SF)	YTD 2022 Deliveries (SF)	Under Construction (SF)
Suburban Maryland	**75,806,653**	**$33.69**	**$27.82**	**$30.96**	**100,000**	**826,000**	**491,746**
Class A	42,892,882	$33.69	NA	$33.69	100,000	826,000	491,746
Class B	23,184,528	NA	$27.82	$27.82	0	0	0
Class C	9,729,243	NA	NA	$25.25	0	0	0

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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