Washington Metro Area Market Overview

Class A Occupancy Expansion Drives Moderation in Vacancy; Investors Frozen by Limited Debt Availability and Economic Uncertainty

Economic indicators in the Washington metro area have begun to wear under the growing pressure of persistent inflation and its impact on potential recessionary conditions. These challenges are not unique to the Washington market, as international central banks are similarly enacting monetary policy measures to curb inflation. Encouragingly, inflation did tip downward in November, potentially softening the Federal Reserve's approach to interest rate hikes in 2023.

The Washington region's labor market grew relative to year-ago levels, but its growth rate has slowed to 1.9%, its lowest rate of the year. Total nonfarm employment grew by 63,900 jobs in the 12 months since November 2021, of which 9,900 were in office-using sectors. The pace of office-using employment growth varies across the region's three substate areas, with the District of Columbia recording rapid cooling during the year and registering annualized job contraction of 0.4% in November 2022. Still, the region boasts encouraging economic drivers, particularly in suburban markets, which are anticipated to support labor markets in the long term. Newmark forecasts annualized employment gains of 83,300 jobs by the end of 2022 and an average of 43,825 net new jobs gained per annum from 2022 to 2025. The region's unemployment rate has decreased 80 basis points over the last year, to 3.1%.

Economy and Labor

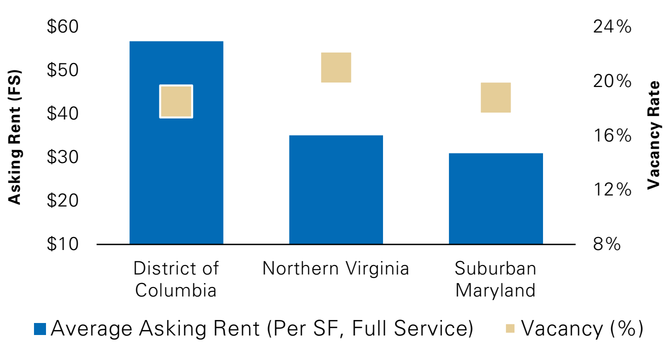
- **Historical Job Change:** 63,900 jobs were gained in the 12 months ending November 2022. The rate of employment growth has slowed throughout in 2022, as recessionary pressures build, and the economy steadies itself for the impacts of a potential downturn.
- **Projected Job Growth:** Newmark forecasts a net gain of 83,300 jobs in 2022 as post-pandemic employment recovery moderates and economic pressures slow momentum. Job gains are expected to average 43,825 per annum from 2022 through 2025.
- **Unemployment Rate:** The regional unemployment rate measured 3.1% in November 2022, a decrease of 80 basis points from November 2021 and a decreased of 20 basis points from October 2022.

Market Summary

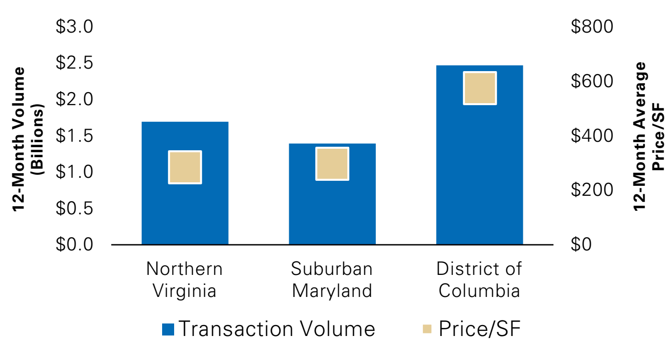
	District of Columbia	Northern Virginia	Suburban Maryland	Metro Area
Total Inventory (SF)	130.2 M	166.3 M	75.8 M	372.3 M
Vacancy Rate	18.5%	21.0%	18.8%	19.6%
Quarterly Net Absorption (SF)	200,465	312,851	-9,042	504,274
Average Asking Rent/SF	$56.65	$35.08	$30.96	$42.07
Under Construction (SF)	514,613	1.1 M	491,746	2.1 M
Deliveries YTD (SF)	1.3 M	1.8 M	826,000	3.9 M

Market Analysis

ASKING RENT AND VACANCY RATE



OFFICE INVESTMENT SALES VOLUME AND PRICING



Source: Newmark Research

NEWMARK

Fundamentals Exhibit Modest Tightening; Market Exceptionally Soft Ahead of Recessionary Concerns

Quarterly net absorption measured 504,274 square feet in the fourth quarter of 2022, representing the largest quarterly occupancy gain since before the pandemic. While this gain is a welcome sight for a challenged market, year-end net absorption highlighted the region's softness, measuring negative 984,465 square feet. Net occupancy gains were strongest in Northern Virginia, which measured 312,851 square feet, followed by the District of Columbia, measuring 200,465 square feet. Suburban Maryland's net absorption was closer to net neutral, at negative 9,042 square feet. While all three markets showed noteworthy improvement from the third quarter of 2022, context is important. For much of the pandemic, net absorption was mostly accounting for occupancy losses as firms allowed leases to expire and offices shifted to remote working. As pent-up demand loosens among these tenants, occupancy gains are expected to represent a larger share of the net absorption equation. This is encouraging for the region, but it should be noted that despite this, office market fundamentals remain exceptionally soft.

The region's construction pipeline continues to slow, measuring 2.1 million square feet in the fourth quarter. Although demand for top-quality product is relatively strong, developers are apprehensive to undertake new projects due to low leasing activity and high construction costs. Just over 500,000 square feet of net-new office space delivered in the quarter. Year-end deliveries totaled 3.9 million square feet, mostly concentrated in the District of Columbia and Northern Virginia.

Contraction in the region's construction pipeline and limited net-new deliveries will aid in slowing vacancy growth. Overall vacancy fell by 10 basis points since the prior quarter, to 19.6% in the fourth quarter of 2022. Driven by positive occupancy and net inventory contraction, this is a positive development for the region's office market, but it should also be noted that regional vacancy was at an all-time high last quarter. Consistently large gains would be required in the period ahead to tighten the market to the levels measured before the onset of the pandemic.

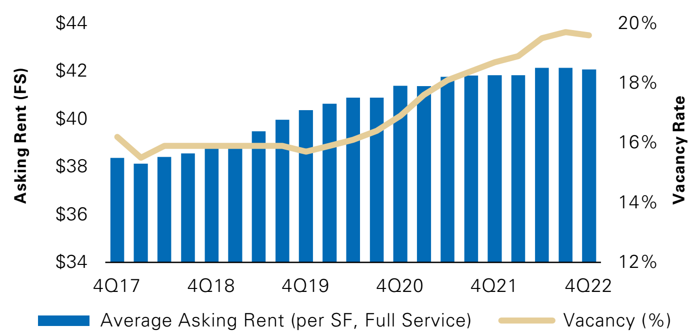
Flight to quality remains a significant factor in driving office market fundamentals. Tenants' preference for quality not only supports stronger leasing and occupancy but is also driving owners of lower quality assets to reconsider their competitive positions. This has accelerated momentum in office conversion and demolition activity, causing inventory contraction, as obsolete office assets are removed from the market. While this activity is not a significant share of the market, it is large enough to create noticeable contraction in inventory. Conversely, tenant demand for quality space is tightening market conditions for the most elite product. Although developers remain hesitant to break ground on new projects, strong preleasing activity could encourage a ground break, despite economic and leasing market headwinds.

Current Conditions

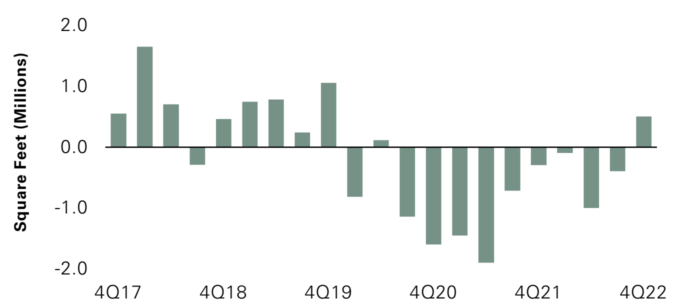
- The region registered 504,274 square feet of net absorption during the fourth quarter of 2022; however, year-end absorption remained contractionary at negative 984,465 square feet. Occupancy losses in 2022 have been less severe than in 2021 but are significant relative to historical levels.
- Vacancy decreased 10 basis points in the fourth quarter of 2022, to 19.6%. Most vacancy growth over the last year is concentrated in the region's Class B market, which rose 200 basis points to 22.2%.
- Average asking rents in the urban core as well as suburban markets are beginning to wear under the extended pressure of low demand. Average asking rents measured $42.07/SF, up 0.6% from last year, but down 0.1% from the third quarter.

Market Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION



Market Summary

	Current Quarter	Prior Quarter	Year Ago Period	24-Month Forecast
Total Inventory (SF)	372.3 M	373.3 M	371.3 M	↑
Vacancy Rate	19.6%	19.7%	18.7%	→
Quarterly Net Absorption (SF)	504,274	-393,130	-293,466	↓
Average Asking Rent/SF	$42.07	$42.13	$41.83	→
Under Construction (SF)	2.1 M	2.3 M	4.3 M	↓
Deliveries YTD (SF)	3.9 M	3.3 M	3.2 M	↓

The extended duration of the pandemic appears to be wearing on asking rents, which had been at least holding value for much of the last two years. Average asking rents contracted by 0.1% from the prior quarter, measuring $42.07/SF in the fourth quarter. Despite flight-to-quality, rent compression in the suburbs and among commodity-grade assets has resulted in Class A rents falling by 0.3% from the prior quarter, measuring $45.74/SF. Class B assets have shown more stability; however, landlords of low-quality buildings have been more consistently challenged by low leasing conditions since 2020.

Effective rents, which account for generous concession packages, remain under downward pressure. However, as high vacancy and low leasing damage the financial condition of some assets, certain ownership groups may not be able to finance excessive tenant improvement allowances. Low concession leases, which boast lower base rents, could be advantageous for some tenants in the market, but inflationary pressure on construction materials has significantly elevated the cost to build and furnish new office spaces. While supply chains are loosening and the consumer price index is pointing downward, month-over-month producer price index, a measure of prices received by producers of inputs, has been consistent through November. Pricing among some construction inputs may be moderating, but in aggregate, inflation will continue to challenge construction pricing into 2023.

Flight to Quality Drives Activity to Class A Market

The top-end of the Class A market continues to attract most of the market activity. The quarter's strong occupancy gains were heavily supported by the Class A market, measuring 572,542 square feet, compared to Class B/C markets' negative 68,268 square feet. As anticipated based on leasing activity over the last year, flight to quality is bringing some relief to Class A fundamentals. The unbalanced preference for top-quality assets is leading to further softening among commodity-grade Class A and low-quality Class B/C assets. The financial burdens of the prolonged underperformance is presenting distinct challenges for some owners and lenders. Office conversions still present exit opportunities for well-positioned buildings, though the pipeline for proposed conversions is already large, at 7.5 million square feet. To read more about the region's office conversion market, please download Newmark Research's recent report: [Office Conversion Activity Accelerates in the Washington Metro Area].

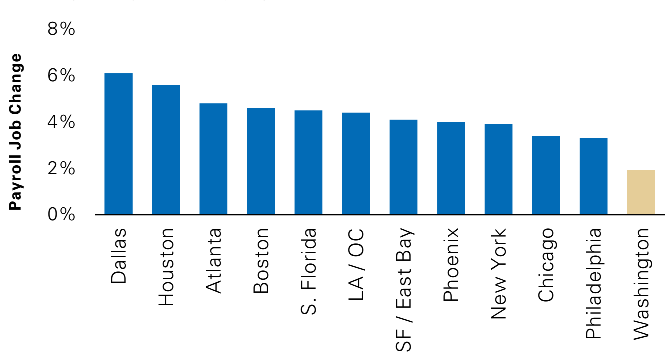
Return to Office Momentum Mixed

Employees' return-to-office momentum was less dynamic than anticipated following strong rhetoric from corporations ahead of Labor Day. Local in-office occupancy has slowly risen in 2022, as hybrid schedules have become increasingly common for many office occupiers. According to survey results from WFH Research, the percentage of paid remote working days notably declined in the Washington region over the last year, measuring 31.8% of days as of November 2022.[1] According to this study, among the 10 largest US markets, the Washington metro area recorded the third fastest decline in the number of remote days worked over the last year, behind only the Bay Area and Houston. Considering other return-to-office data points, the story is less clear. Kastle Systems key fob swipe data and Metrorail ridership depict an environment of less aggressive in-office occupancy recovery.

Hybrid work arrangements are becoming normalized for most office occupiers. However, the pace of adoption could be catalyzed by more cohesive efforts by the region's largest employer, the federal government, to enact and enforce its verbally mandated return-to-office policies. Various members of the local real estate community have lobbied the government to lead the region in recalling employees to offices, but agencies are fractured in enacting the requirement. While some federal agencies are returning employees to offices, the pace is slow. Some experts view a potential recession in 2023 as an inflection point for office occupiers, both private and public, to recall employees to offices, but the exceptionally tight labor market may alternatively encourage firms to prioritize retaining quality workers over managing real estate occupancy. Locally, the impact of the federal government's in-office employee requirement would be a much stronger and tangible driver for regional occupancy gains. Political pressure is building for the federal government to enact a change, but little clarity on a timeline exists entering 2023.

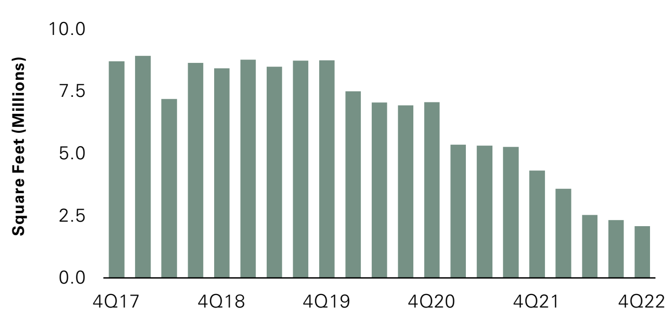
Payroll Job Change – Largest Metro Areas

12 MONTHS ENDING NOVEMBER 2022



Office Market Construction Pipeline

WASHINGTON METRO AREA | SQ. FT. UNDER CONSTRUCTION



Source: U.S. Bureau of Labor Statistics, Newmark Research

[1] Barrero, Jose Maria, Nicholas Bloom, and Steven J. Davis, 2021. "Why working from home will stick," National Bureau of Economic Research Working Paper 28731.

Washington Area Economic Outlook

Economic headwinds are strengthening and slowing growth in the Washington metro area. Labor markets largely remain in expansion, but the growth rate has precipitously slowed in 2022 among both total nonfarm and office-using jobs. This slowing pace is expected to continue, as the Federal Reserve's efforts to curb inflation and slow economic output begin to work through labor markets. This is a point of concern for Washington's office demand recovery, particularly given that its labor markets are decelerating faster than comparable major metro markets. The threat of a recession is changing business' priorities, but leading experts are not in concert regarding the inevitability of a recession in 2023. Regardless, increased economic uncertainty is resulting in slight revisions to anticipated employment gains in coming years. Still, Newmark projects net labor growth from 2022 to 2025, averaging 43,825 jobs per annum regionally.

One of Washington's greatest competitive strengths regardless of the economic market conditions is the high quality and size of its labor force. Additionally, local academic institutions are actively investing in programs and facilities, particularly in technical fields, which will benefit the region's ability to domestically produce well-trained workers to satisfy the demands of current employers in the region and serve as a magnet for other firms seeking a steady supply of high-quality labor.

Washington's increasingly diversified economy will create green chutes for growth in the period ahead. Noteworthy developments in the region's technology sector, led by both public and private sector growth, has been a boon for the region's reputation as an emerging tech hub. However, technology workers have generally been able to adapt to remote-compatible roles more readily than many other office-using sectors, which could damage office demand potential. Encouragingly, some major tech firms have begun publicly announcing plans to require in-office occupancy among its workers, which could serve as validation for other firms to follow suit, at least in a hybrid capacity.

Office Market Outlook

The Washington metro area's office market showed signs of modest tightening and leveling off at the close of the year. While return-to-office momentum was not particularly robust this fall, it is ticking upward, and pent-up demand has been loosening among tenants that had foregone office space in the preceding years. The modest return of tenants to offices is driving greater net-positive occupancy in the market, despite uncertainty around long-term real estate needs. Although the fourth quarter's absorption gains marked an inflection point in regional net occupancy, steady growth is not necessarily expected. As occupiers react to greater economic uncertainty in 2023, oscillations in net demand are likely and consolidations may weigh more strongly against loosening pent-up demand.

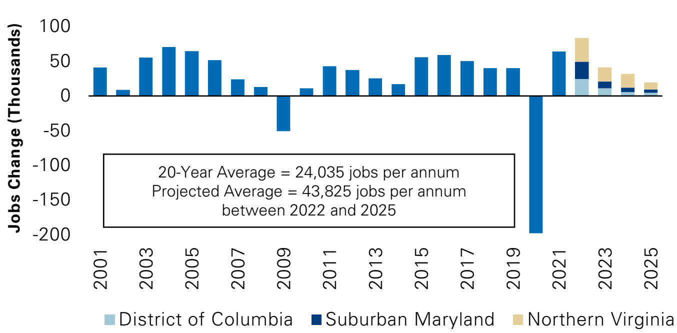
Over the next two years, total regional net demand is anticipated to measure just under 400,000 square feet. Most of this expansion is expected to be concentrated in Northern Virginia, at over 800,000 square feet. Net demand in Suburban Maryland is expected to be closer to net-neutral, and the District and urban core is likely to continue to record consolidations among its government-heavy tenant base, measuring net occupancy of negative 400,000 square feet. Vacancy rate moderation could be additionally aided by inventory contraction through office conversions. In concert, these factors are expected to apply downward pressure on the market's near record-high vacancy, which is expected to settle to 19.2% by year-end 2024.

Although the contractionary standard set by the pandemic is beginning to subside, office market fundamentals will remain generally soft due to oversupply and elevated vacancy. Tenant preference for quality will benefit the highest-quality assets, tightening fundamentals for some segments of the market. Lower-quality and commodity-grade asset owners will remain more challenged, even as demand returns to the market.

For additional information on the District of Columbia, Northern Virginia, and Suburban Maryland office markets, please visit Newmark's website: Mid-Atlantic Market Reports.

Payroll Job Growth Forecast

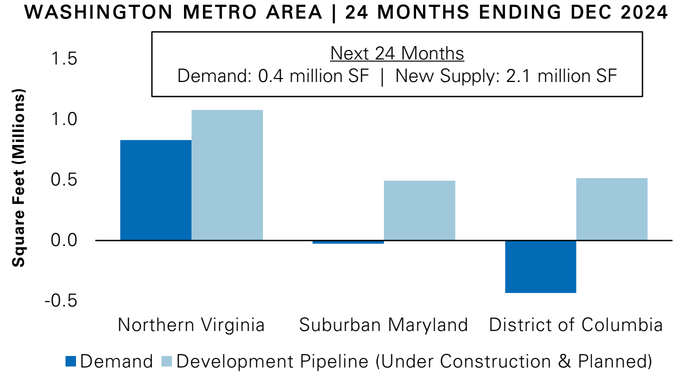
WASHINGTON METRO AREA | 2001 - 2025



Source: U.S. Bureau of Labor Statistics; Forecast by Newmark Research, Stephen S. Fuller Institute and Moody's Analytics

Supply/Demand Forecast

WASHINGTON METRO AREA | 24 MONTHS ENDING DEC 2024



District of Columbia Office Market

The District of Columbia's office market exhibited modest tightening in the fourth quarter of 2022, noted by positive net absorption and a leveling of overall vacancy. This marks the District's largest quarterly net occupancy gain in three years. Leasing activity has increased modestly over the last six months. Although leasing remains low relative to historical expectations, pent-up demand is loosening, and the slow but steady return of workers to offices is encouraging companies to reengage in real estate planning. Average asking rents have been trending downward over the last six months and are currently tied with the lowest average rates recorded since 2019. Rent compression has been experienced in all building classes but has been most pronounced in the Class B market. In addition to relatively low demand, high availability and landlord competition are applying downward pressure on both asking and effective rents.

Net absorption measured 200,465 square feet in the fourth quarter of 2022, nearly offsetting the negative 241,901 square feet measured in the prior quarter. Year-end 2022 net absorption measured negative 302,767 square feet, as early-year occupancy losses weighed on the market. Quarterly vacancy measured 18.5%, down 10 basis points from the third quarter and up 100 basis points in the last year. Class A vacancy, aided by positive net absorption, decreased by 10 basis points on the quarter, measuring 16.5%. Average asking rents measured $56.65/SF, a $0.21/SF decrease from both last quarter and last year. Asking rents have been oscillating around $56/SF over the last year but have decreased each of the last two quarters. Asking rent compression has been experienced market-wide but slightly less in the Class A market, falling by 0.4% over the last year. In comparison, Class B rates have fallen by 0.6%.

District of Columbia Outlook

Over the next 24 months, Newmark projects modest tightening, resulting in the vacancy rate decreasing to 18.1% by December 2024. The top of market has been performing well, but the commodity-grade and Class B markets will struggle to attract tenancy. Stable but low leasing activity should temper expectations for strong occupancy gains in early 2023. Asking rents may modestly appreciate in high-quality assets, but low demand will ensure generous concessions remain common.

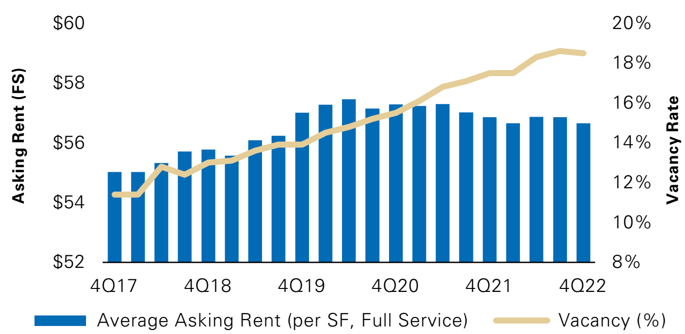
The financial burdens of the prolonged underperformance of certain assets will present distinct challenges for some owners and lenders. Office conversions still present exit opportunities for well-positioned buildings, though the pipeline for proposed conversions is already large, at 3.5 million square feet. Conversion-focused investment activity is relatively low, and only three office assets sold with intent of conversion in the second half of 2022. If proposed projects begin breaking ground, office conversion activity could moderate Class B market fundamentals.

Current Conditions

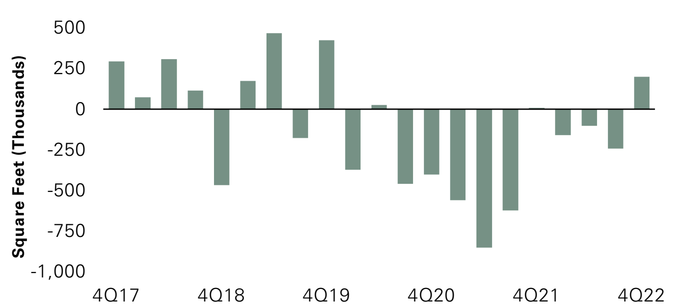
- The District of Columbia recorded 200,465 square feet of net absorption in the fourth quarter of 2022. Year-end net absorption measured negative 302,767 square feet. Despite positive absorption on the quarter, low leasing activity for much of the last year should limit quarterly occupancy in the period ahead.
- The vacancy rate rose 100 basis points over the last year to 18.5% but is down 10 basis points from the third quarter of 2022. Positive quarterly occupancy has helped to slow vacancy growth, but a moderating construction pipeline and inventory contraction by way of office conversions are stabilizing supply.
- Average asking rents measured $56.65/SF in the fourth quarter. Modest quarter-over-quarter rent contraction was measured, signaling further softening in the market.

Market Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION



Market Summary

	Current Quarter	Prior Quarter	Year Ago Period	24-Month Forecast
Total Inventory (SF)	130.2 M	131.1 M	131.4 M	→
Vacancy Rate	18.5%	18.6%	17.5%	→
Quarterly Net Absorption (SF)	200,465	-241,901	8,322	↓
Average Asking Rent/SF	$56.65	$56.86	$56.86	→
Under Construction (SF)	514,613	580,083	1.4 M	→
Deliveries YTD (SF)	1.3 M	1.2 M	976,215	↑

Northern Virginia Office Market

Northern Virginia's office market exhibited modest tightening in the fourth quarter of 2022 and ended the year with a second consecutive quarter of occupancy growth. Despite increased economic headwinds fueled by inflation, in conjunction with recessionary pressures, the office market displayed continued resistance to significant softening.

Net absorption measured 312,851 square feet in the fourth quarter of 2022, offsetting the occupancy losses incurred earlier in the year. Year-to-date absorption measured 209,689 square feet, marking the first time since the start of the pandemic that Northern Virginia ended the year with positive absorption. Positive quarterly occupancy resulted in a slight reduction in vacancy, which decreased 10 basis points from the last quarter, to 21.0%. However, overall vacancy remained steady during 2022, increasing only 50 basis points over the last 12 months. Average asking rates appreciated 1.7% over the last 12 months, reaching a record high of $35.08/SF. Leasing activity remained relatively strong during the fourth quarter, but there is a continued lack of equitable distribution of this activity across all Northern Virginia's submarkets.

Northern Virginia Outlook

Northern Virginia's office market showed modest signs of recovery in the fourth quarter. Vacancy has been relatively stable over the past year but continues to climb nominally year over year. Sublease availability rose in the quarter, signaling that occupiers are not finished rightsizing their real estate needs. However, economic engines are boosting office-using labor and office inventory contraction could moderate the impact of occupancy losses on vacancy. Newmark Research projects that Northern Virginia's vacancy will decrease from 21.0% to 20.4% by the end of 2024. Northern Virginia's development pipeline measures 1.1 million square feet, with a prelease rate of 28.9%. At less than 1% of the existing inventory, the pipeline remains modest. The market is unlikely to see a significant increase in groundbreakings within the next 12 months, considering the high cost of construction and recessionary pressures.

While rent growth is promising given low demand, concessions remain relevant regionally, causing downward pressure on effective rents. Tenants continue to seize leverage created by increased availability throughout most submarkets. Tenants can generally expect concessions to last through at least mid-2023.

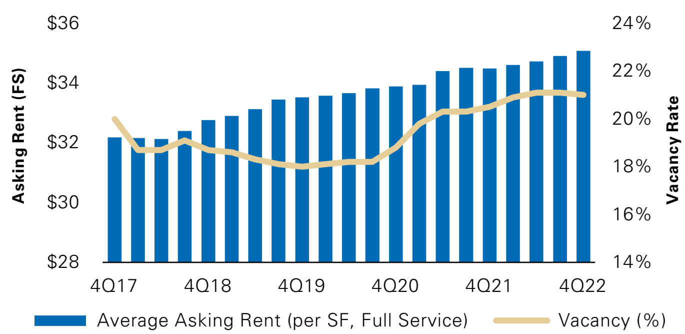
Despite anticipated recessionary safeguarding among potential tenants, and the increased construction costs seen in Northern Virginia this year, the area remains a beacon for growth in several sectors, including technology, government, and cybersecurity firms. As tenants strive to balance the changing landscape of worker needs, they remain bullish on leasing in the Northern Virginia area.

Current Conditions

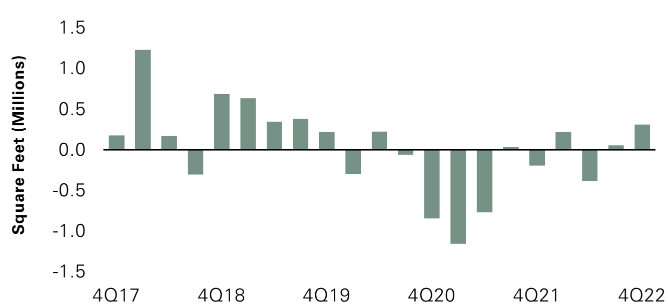
- Quarterly net absorption measured 312,851 square feet in the fourth quarter. This offsets some of the occupancy lost during the year, resulting in year-to-date net absorption of 209,689 square feet.
- The overall vacancy rate was 21.0% at the end of the fourth quarter, up 50 basis points from one year ago.
- Office space under construction, excluding renovations and owner-occupied buildings, totaled 1.1 million square feet at the end of the fourth quarter.
- Asking rents rose to $35.08/SF on the quarter and are up 1.7% from one year ago.

Market Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION



Market Summary

	Current Quarter	Prior Quarter	Year Ago Period	24-Month Forecast
Total Inventory (SF)	166.3 M	165.7M	164.6 M	↓
Vacancy Rate	21.0%	21.1%	20.5%	↓
Quarterly Net Absorption (SF)	312,851	57,749	-192,219	↓
Average Asking Rent/SF	$35.08	$34.90	$34.49	↑
Under Construction (SF)	1.1 M	1.4 M	2.0 M	↓
Deliveries YTD (SF)	1.8 M	1.4 M	939,000	↑

Suburban Maryland Office Market

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. The pipeline is 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.

Suburban Maryland Outlook

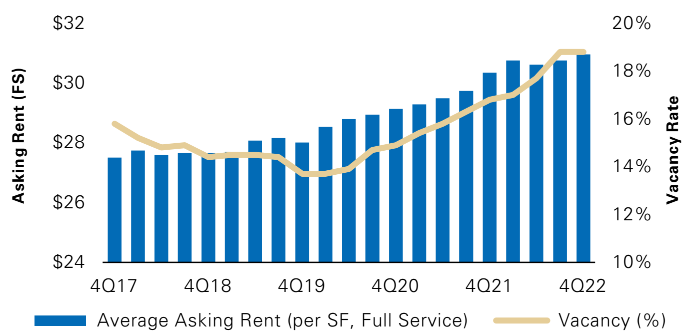
Soft, but relatively steady market fundamentals in Suburban Maryland should persist in the coming quarters, resulting in net neutral demand. Recessionary pressures may slightly soften market conditions in early 2023 as tenants brace for near-term uncertainty. Suburban Maryland's construction pipeline 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.

Current Conditions

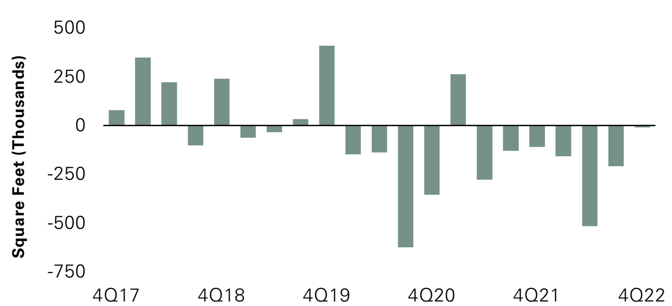
- Suburban Maryland recorded negative 9,042 square feet of net absorption in the fourth quarter, a significant improvement from the third quarter. However, year-to-date net absorption has been negative for the past seven consecutive quarters.
- Vacancy has increased 200 basis points from last year, to 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 Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION



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 Statistics – Vacancy and Absorption

	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)
Washington Metro Area	**372,348,454**	**18.4%**	**19.6%**	**2,796,086**	**-3,440,985**	**-4,360,868**	**504,274**	**-984,465**
District of Columbia	130,221,824	17.1%	18.5%	890,479	-1,204,657	-2,027,247	200,465	-302,767
Suburban Maryland	75,806,653	17.3%	18.8%	347,519	-1,266,230	-253,457	-9,042	-891,387
Northern Virginia	166,319,977	19.8%	21.0%	1,558,088	-970,098	-2,080,164	312,851	209,689

Market Statistics – Vacancy and Absorption 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)
Washington Metro Area	**372,348,454**	**18.4%**	**19.6%**	**2,796,086**	**-3,440,985**	**-4,360,868**	**504,274**	**-984,465**
Class A	227,836,989	17.8%	19.1%	2,856,315	-1,063,249	-1,011,887	572,542	1,464,748
Class B	110,393,493	20.8%	22.2%	162,365	-1,640,762	-3,046,560	-136,955	-2,431,947
Class C	34,117,972	14.8%	15.1%	-222,594	-736,974	-302,421	68,687	-17,266

Market Statistics – Rents and Development

	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)
Washington Metro Area	**372,348,454**	**$45.74**	**$38.43**	**$42.07**	**515,470**	**3,869,223**	**2,081,176**
District of Columbia	130,221,824	$62.98	$48.45	$56.65	65,470	1,270,986	514,613
Suburban Maryland	75,806,653	$33.69	$27.82	$30.96	100,000	826,000	491,746
Northern Virginia	166,319,977	$37.36	$32.33	$35.08	350,000	1,772,237	1,074,817

Market Statistics – Rents and Development 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)
Washington Metro Area	**372,348,454**	**$45.74**	**$38.43**	**$42.07**	**515,470**	**3,869,223**	**2,081,176**
Class A	227,836,989	$45.74	NA	$45.74	515,470	3,869,223	2,081,176
Class B	110,393,493	NA	$38.43	$38.43	0	0	0
Class C	34,117,972	NA	NA	$29.75	0	0	0

Note: Asking rents are quoted on a full service basis

Investment Sales Market

The Washington region registered $5.6 billion in office sales volume for the 12 months ending in the fourth quarter of 2022. Quarterly sales volume measured $705.5 million at production of this report. This marks the region's lowest quarterly sales volume since the first quarter of 2021. Despite relatively robust sales activity in the third quarter of 2022, momentum was not sustained into the close of the year, and the impact of economic headwinds and tighter debt markets are directly suppressing investor activity.

Investors Pause New Investment Activity

Office investors currently face distinct challenges, resulting in tepid investment activity. Most importantly, the Federal Reserve has remained steadfast in raising interest rates to combat inflation and economic expansion. Interest rate increases are anticipated to continue in 2023, as inflation remains stubbornly high. However, inflation decreased in November 2022, signaling that the Fed may consider tempering its stance in mid-2023, allowing investors to better assess when peak interest rates are reached.

High borrowing costs are a headwind for investors, as the availability of debt financing also tightens. For investors looking to capitalize on the down market, equity is a significant barrier to entry, given limited debt financing options. Dry powder is available for real estate investment, but conditions are causing many institutional investors to pause new acquisitions. Among buildings in the market, low office leasing projections in the near term have created a large spread between seller's asking prices and buyer's willingness to pay.

These key drivers of office investment uncertainty are not unique to the Washington metro area. Nationally, office investors have similarly retreated from investment markets, awaiting more financial market stability. The region's forecasted recovery of office investment activity is largely tied to national financial markets, but improvement in local office demand could help to provide some added safety for investors. On balance, the region's forecasted office demand is net-negative, but certain markets are expected to see modest expansion, which in coordination with a potential increase in return-to-office policies in a recession, could provide a bump to investor confidence.

Office Investment Sales Outlook

Office investors are likely to experience a more stabilized investment market in mid-to-late 2023, but conditions will remain challenging. It is anticipated that some new debt funds will create additional financing options for owners and investors, but the threat of upcoming debt maturities, limited access to equity, and depreciating asset values will be a significant strain on segments of the market.

Once investment markets stabilize, Washington's historically strong performance of driving returns during periods of uncertainty will ensure it remains a competitive investment market for both domestic and foreign office investors. Structural challenges to financial markets and office demand dynamics in a hybrid work environment may limit Washington's reputation of safety, but opportunistic investors are likely to see more potential targets as pricing further settles.

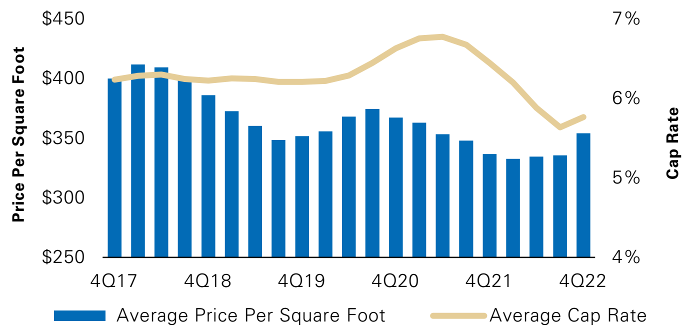
Market Summary

	Washington Metro Area
12-Month Transaction Volume at 4Q 2022	$5.6 B
12-Month Transaction Volume at 4Q 2021	$7.0 B
12-Month Trailing Average Price PSF at 4Q 2022	$354/SF
12-Month Trailing Average Cap Rate at 4Q 2022	5.8%

Note: Values are trailing 12-month averages
Source: Real Capital Analytics, Newmark Research

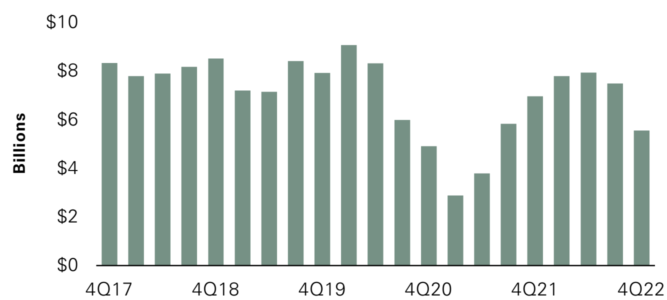
Market Analysis

AVERAGE OFFICE CAP RATE AND PRICE PER SQUARE FOOT



Note: Values are trailing 12-month averages

TRAILING 12-MONTH OFFICE TRANSACTION VOLUME



Notable Recent Office Sales Transactions

Address	Sale Price	Price Per SF	Substate Area
601 Massachusetts Avenue, NW	$531.0 M	$1,033	DC
Commonwealth Tower 1300 Wilson Boulevard	$245.0 M	$714	VA
Key West Corporate Center 9715 Key West Ave	$148.0 M	$523	MD
2235 Monroe Street	$142.0 M	$439	VA
2550 M Street, NW Leasehold	$92.9 M	$449	DC
2115 Wisconsin Avenue	$91.5 M	$495	MD

Source: Real Capital Analytics, Newmark Research

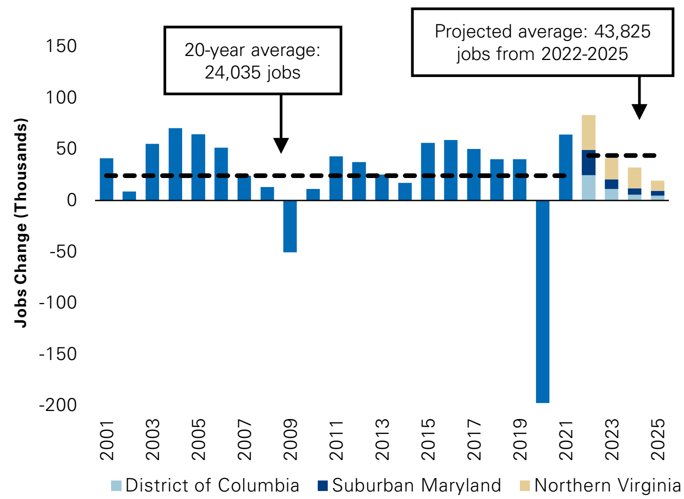
Economic Conditions

The Washington region's unemployment rate registered 3.1% in November 2022. The local unemployment rate is 30 basis points lower than the national rate, but its pace of contraction has notably slowed in 2022 and has oscillated around 3.5% for much of the year. Economic headwinds in the form of persistent inflation and recessionary concerns are slowing labor expansion.

The region gained 63,900 jobs over the last year ending November 2022, of which 9,900 were office-using. The pace of job growth has slowed in 2022 for both the overall market and office-using employment. Despite slowing growth, the Washington region officially recovered all jobs lost since April 2020, reaching a recovery rate of 105.7% of total jobs and 116.7% of office-using jobs, as of November 2022. Office-using employment growth has been most pronounced in Professional & Business Services – the largest regional office-using sector – registering 1.3% annualized growth over the last year and a net gain of 53,800 jobs since April 2020. The metro area is projected to gain 83,300 net new jobs by the close of 2022, but future growth forecasts are likely to be more influenced by the depth and severity of a potential economic downturn.

Employment Forecast

WASHINGTON METRO AREA | PAYROLL JOB CHANGE 2001-2021 AND FORECAST 2022-2025

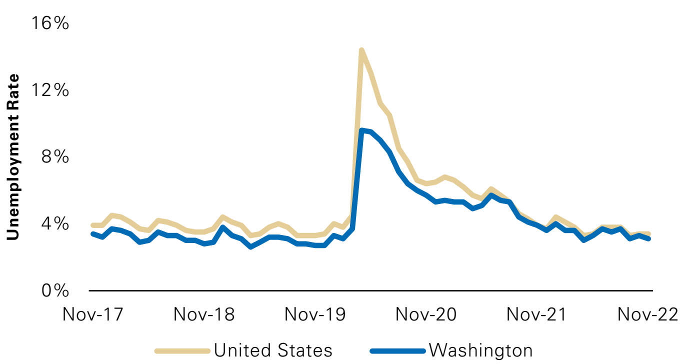


Note: Previous projections have been revised due to COVID-19 and are subject to further revision as conditions change.

Source: U.S. Bureau of Labor Statistics, Moody's Analytics, Newmark Research

Unemployment Rate

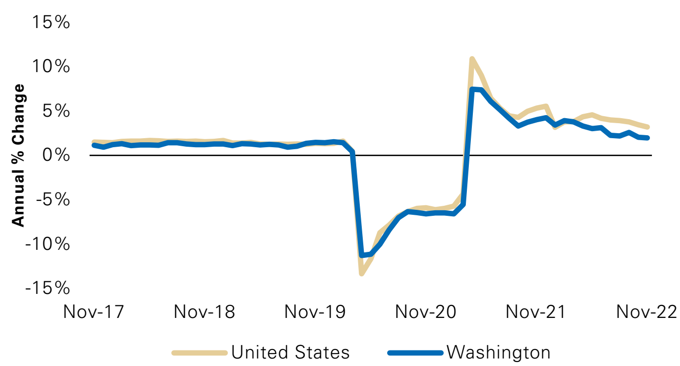
U.S.—SEASONALLY ADJ.
WASHINGTON—NOT SEASONALLY ADJ.



Source: U.S. Bureau of Labor Statistics, Newmark Research

Payroll Employment

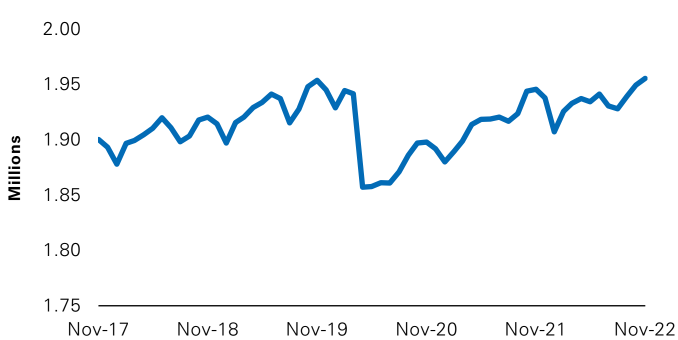
TOTAL NONFARM, U.S.—SEASONALLY ADJ.
WASHINGTON—NOT SEASONALLY ADJ., 12-MO. % CHANGE



Source: U.S. Bureau of Labor Statistics, Newmark Research

Office-Using Employment*

WASHINGTON, OFFICE-USING EMPLOYMENT (000'S), NOT SEASONALLY ADJ.

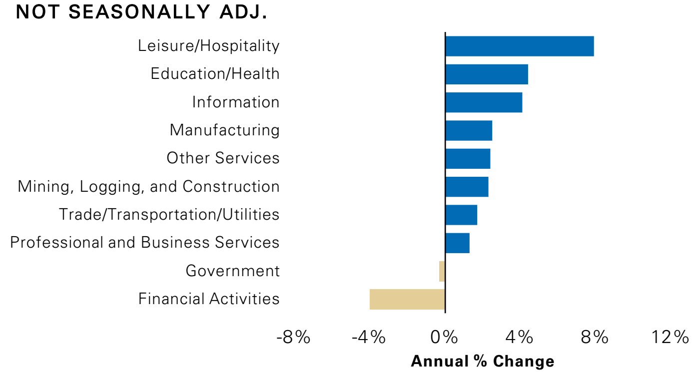


*Identified as Financial Activities, Government, Information, Other Services, and Professional and Business Services

Source: U.S. Bureau of Labor Statistics, Newmark Research

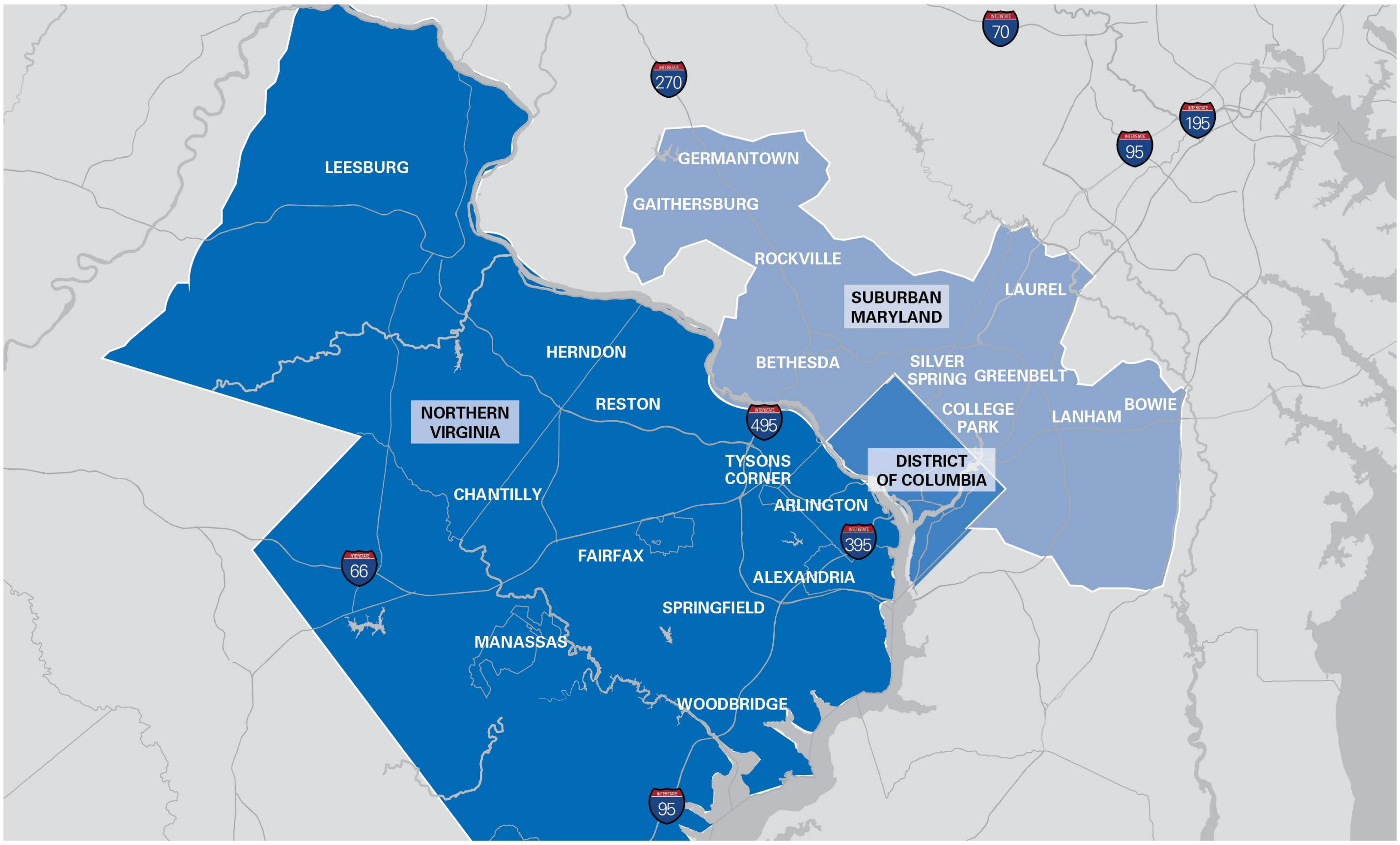
Employment Growth By Industry

WASHINGTON, % CHANGE, 12 MONTHS ENDING NOV 2022, NOT SEASONALLY ADJ.



Source: U.S. Bureau of Labor Statistics, Newmark Research

Washington Metro Office Markets



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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