4Q23

Northern Virginia Office Market Overview

Market Observations

Economy

- The region's labor market remains strong amid shifting macroeconomic conditions. October's 2.7% unemployment rate remains significantly lower than the region's10-year historical average of 4.2%. 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 leisure & hospitality and other services sectors, which both grew 3.9%, followed by education & health with 3.5% growth. The office-occupying industries of 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 slight decline in employment over the past year, jobs in the office-using sectors remain at a level that is 1.3% higher than three years ago—just prior to the pandemic—and 6.3% higher than the pandemic-induced employment trough in April 2020.

Major Transactions

- Office investment sales continue to lag, with sales volume near historic lows as buyers and sellers grapple with high interest rates and limited access to debt.
- The largest sale transaction of the quarter was Rosslyn Gateway at 1901 and 1911 N Fort Myer Drive, which traded from JBG Smith to Penzance for $52.0 million. The buyer plans to demolish the office properties and redevelop to mixed-use.
- Another major fourth-quarter transaction was the sale of 8609 Westwood Center Drive within the Tysons Corner submarket. Bernstein Management Group purchased the 158,000-square-foot building from a joint venture between Atlantic Realty Companies and TPG Angelo, Gordon, & Co for $18.52 million, or $117.43 per square foot.

Leasing Market Fundamentals

- Northern Virginia's net absorption totaled negative 474,998 square feet during the fourth quarter to bring 2023's annual absorption total to a negative 1.7 million square feet.
- The office construction pipeline has remained at 1.0 million square feet for the past five quarters, with no new deliveries or groundbreakings during all of 2023.
- Overall vacancy increased to 21.7%, up 20 basis points over the quarter and 80 basis points from 12 months ago. Average asking rents for the area increased 1.1% over the past year with the rate of rent growth decelerating over the past three years.
- Northern Virginia was home to a majority of the metro area's major fourth-quarter lease transactions, with a handful of larger new leases signed during the quarter, signaling tenants' confidence in long-term real estate decisions.

Outlook

- Uncertainty reigns in the macroeconomic outlook. Occupiers and investors alike will approach deals with greater caution as a result, which will impact leasing and investment activity.
- While the rate of rent growth in Northern Virginia has decelerated over the past three years, rents increased 1.1% over the past 12 months. This rate of growth is likely to continue due to a lack of supply-side pressure with a limited office development pipeline.
- Fewer landlords appear to have capital for the concessions that have been a major driver in attracting tenants over the past several years, contributing to the recent slowdown in deal volume. This trend is likely to continue in the near-term.

TABLE OF CONTENTS

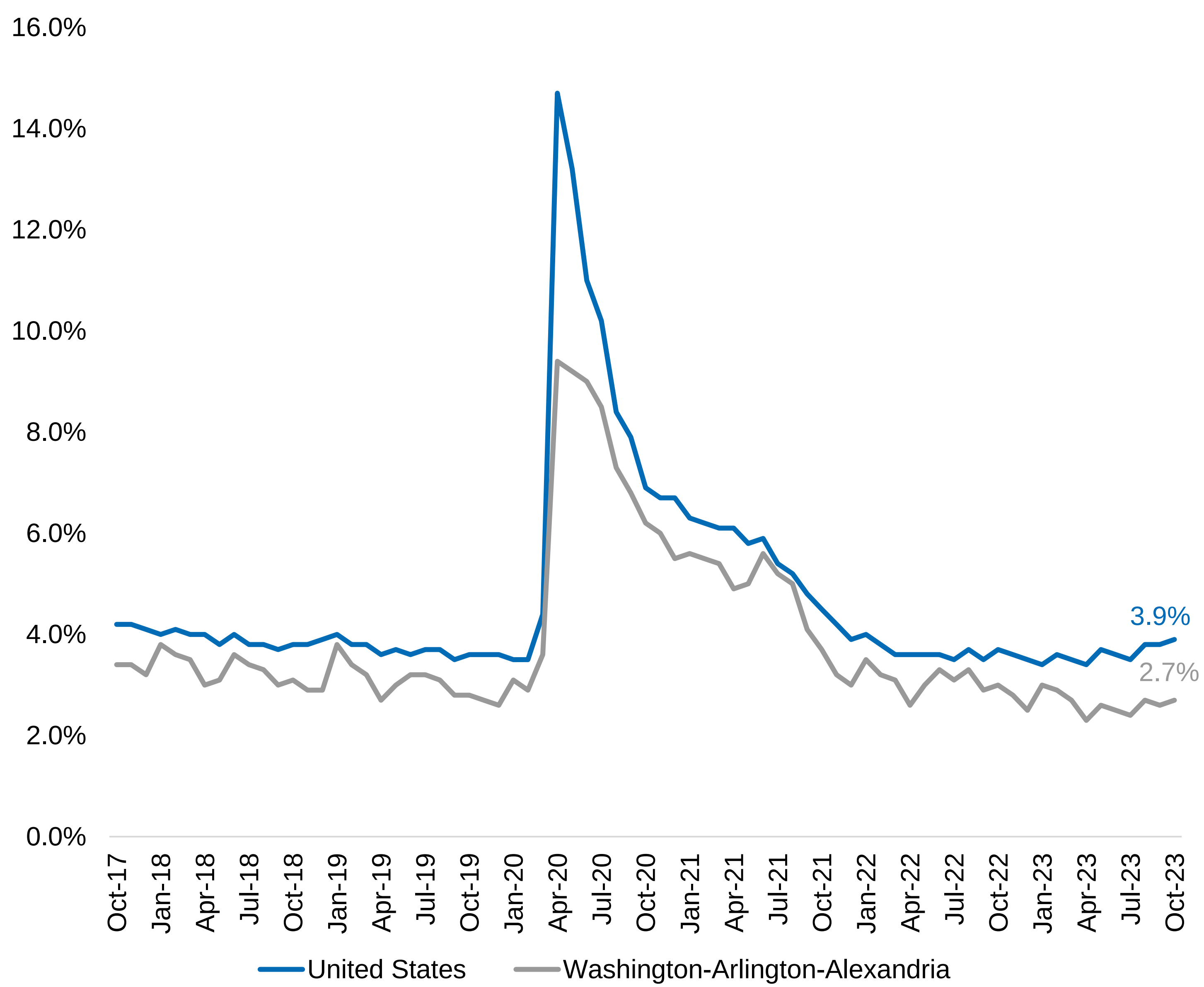
4Q23

Economy

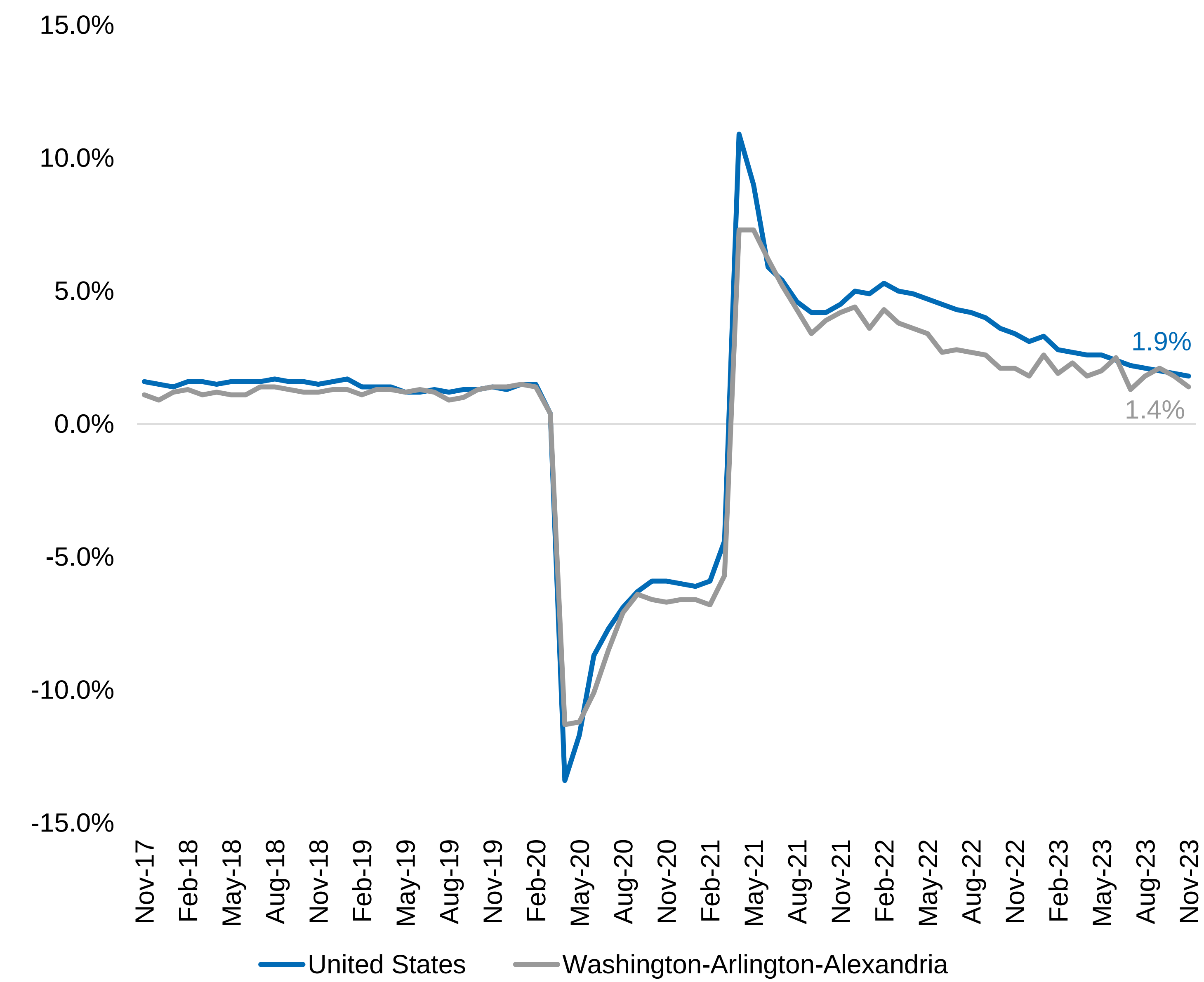
Metro Employment Trends Offer Mixed Signals

While the region's labor market remains on relatively solid footing with unemployment 120 basis points below the national average, job growth has begun to slow amid persistently high inflation and increasing interest rates.

Unemployment Rate, Seasonally Adjusted



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

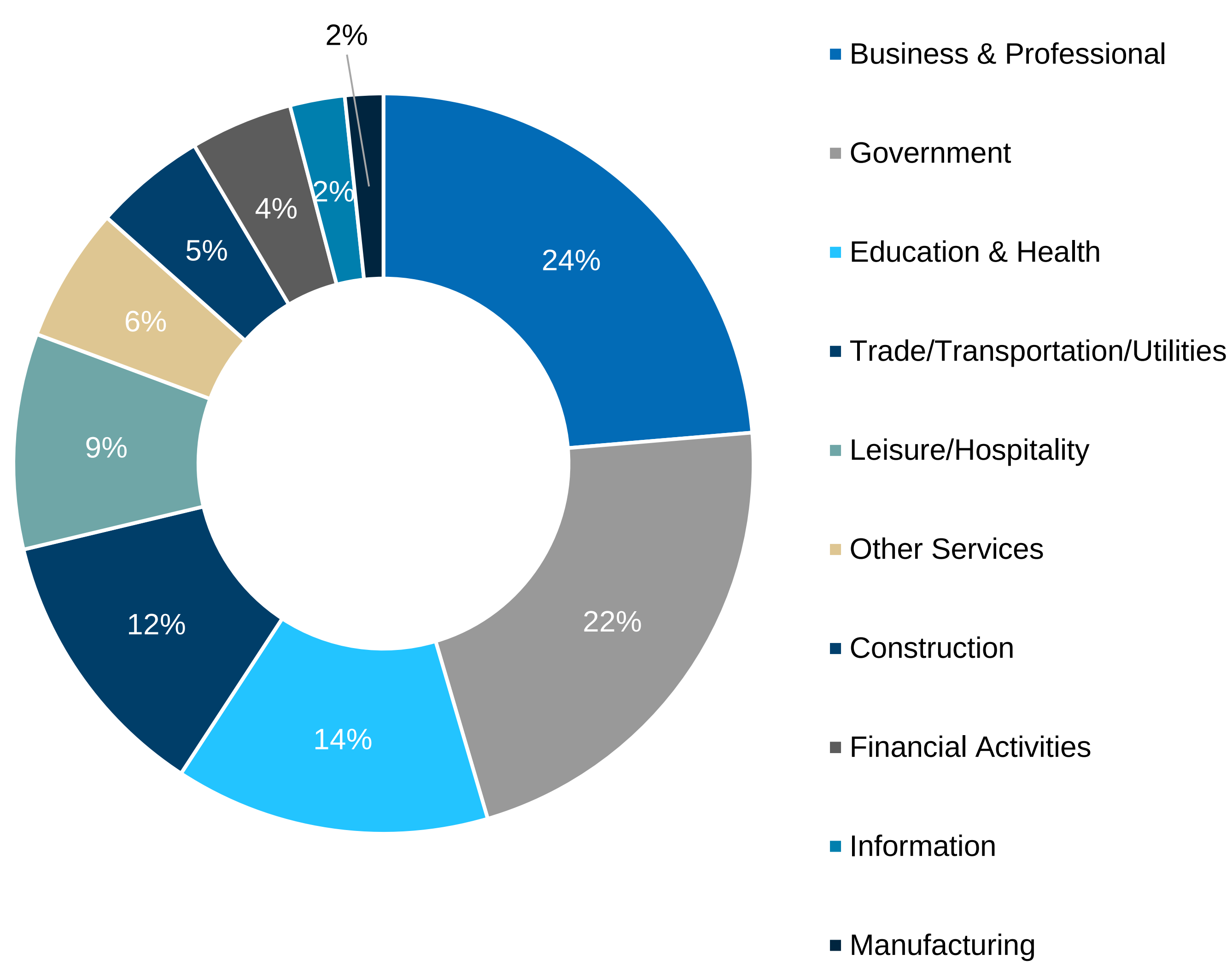


Source: U.S. Bureau of Labor Statistics, Washington-Arlington-Alexandria

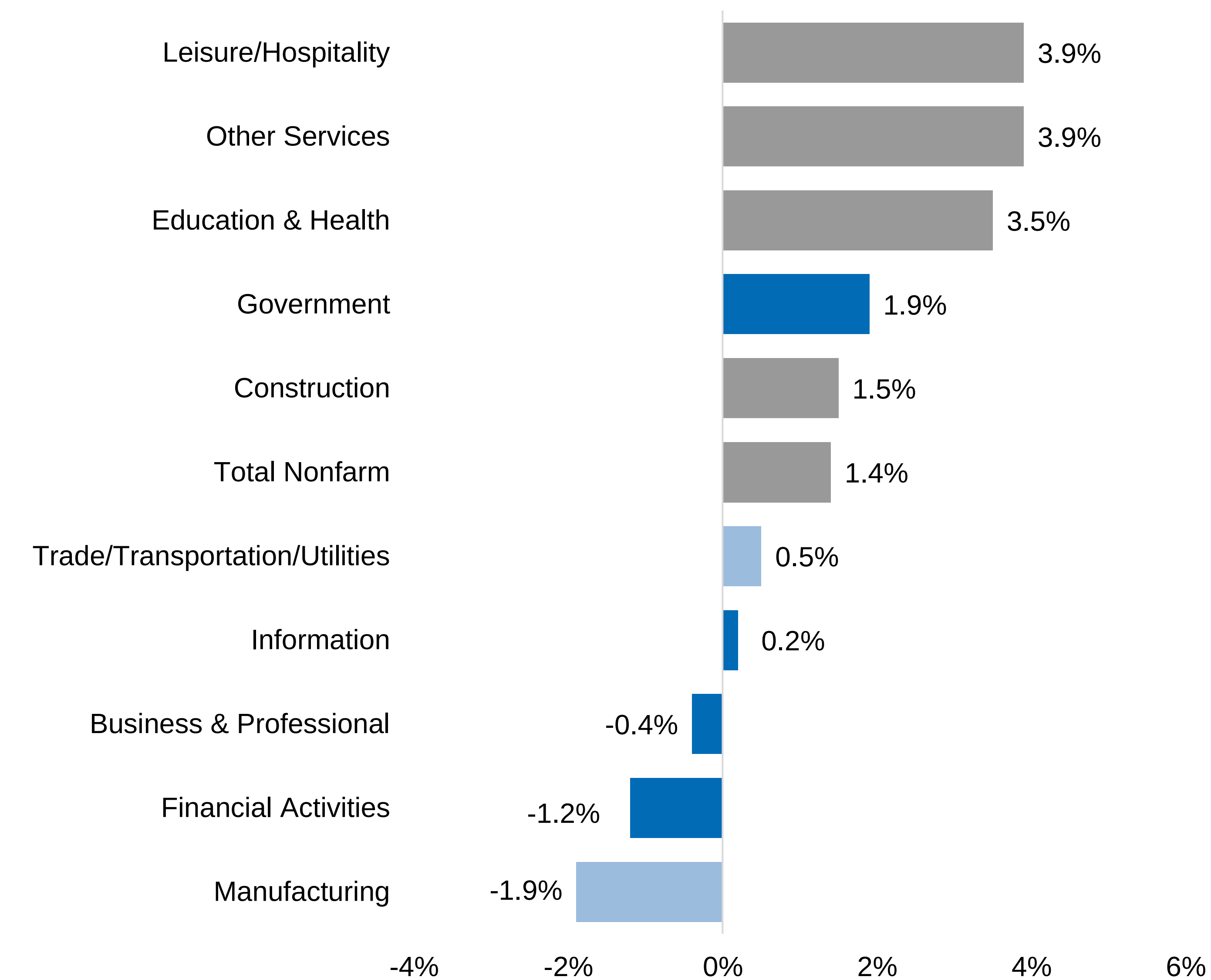
Job Growth Driven in Large Part by Services Still Making Up for Pandemic Losses

The Leisure/Hospitality and Other Services sectors led all industries in regional annual job growth amid a greater shift in spending from goods in favor of services. The office-occupying industries of Financial Activities and Professional and Business Services experienced job losses over the past year, helping to account for continued limited demand for office space.

Employment by Industry, November 2023



Employment Growth by Industry, 12-Month % Change, November 2023

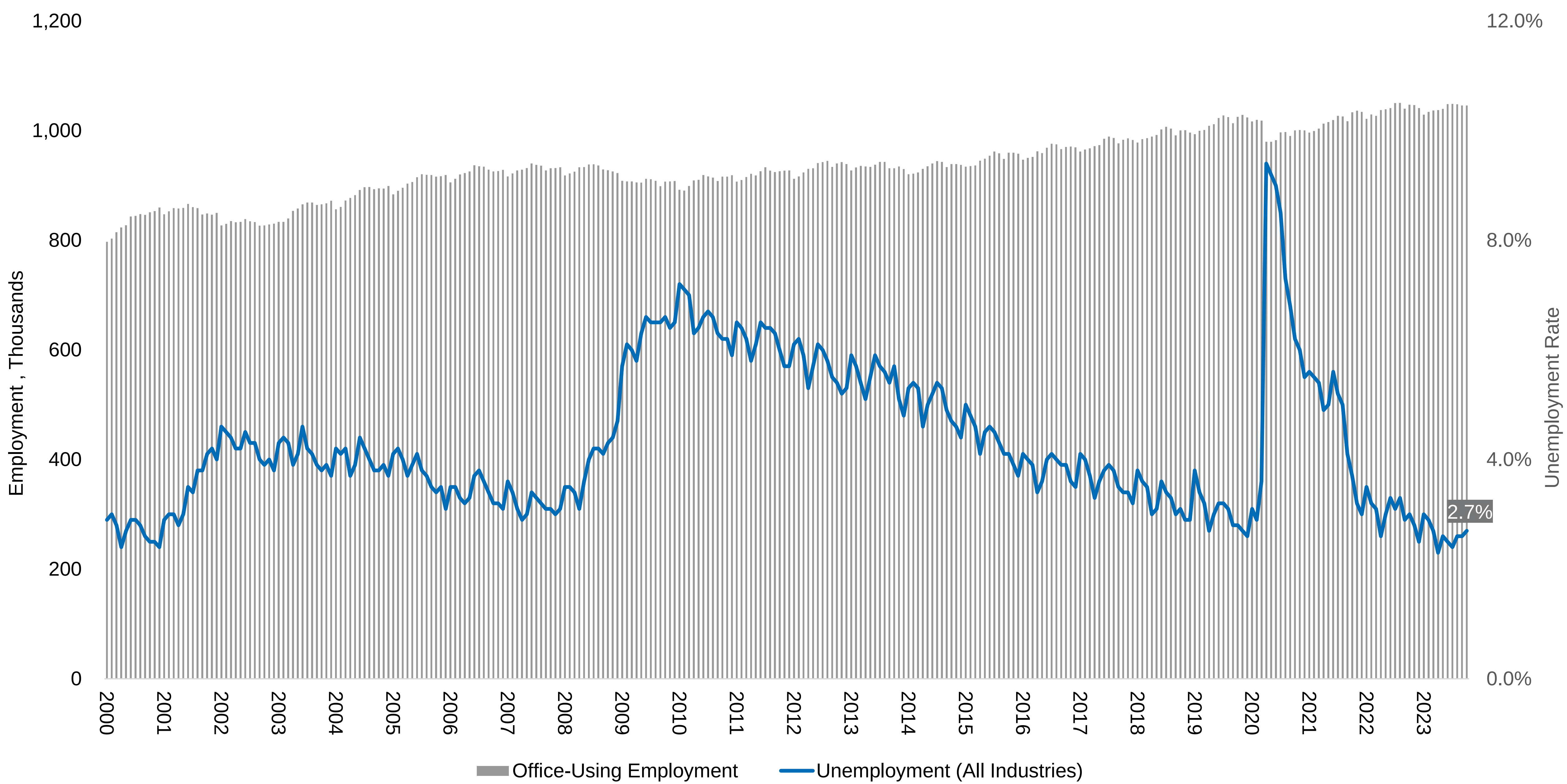


Source: U.S. Bureau of Labor Statistics, Washington-Arlington-Alexandria

Overall Office-Using Employment Has Rebounded

The number of office jobs has rebounded and exceeded pre-pandemic levels. Office-using jobs in the region are currently 1.3% higher than three years ago—just prior to the pandemic—and 6.3% 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: November 2023 data is preliminary.
*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.

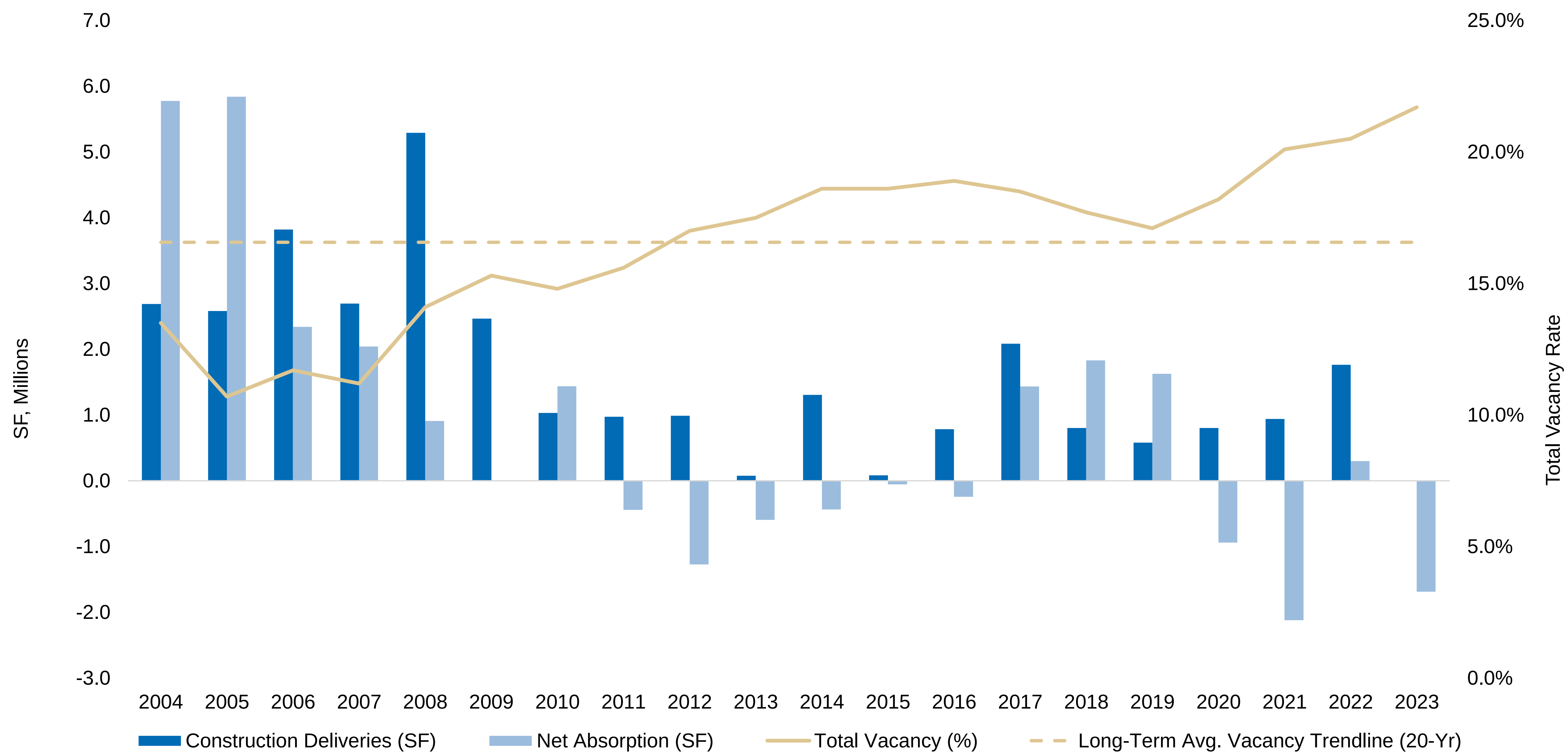
4Q23

Leasing Market Fundamentals

Vacancy Rises but Construction Deliveries Slow Down

Northern Virginia's vacancy rate rose 20 basis points over the quarter to end 2023 at 21.7%. However, 2023 saw no office deliveries in Northern Virginia, a market that has averaged 1.6 million square feet of deliveries over the past 20 years. A slowdown in office deliveries and the lack of new speculative office construction will be advantageous in helping to balance supply with waning demand.

Historical Construction Deliveries, Net Absorption, and Vacancy

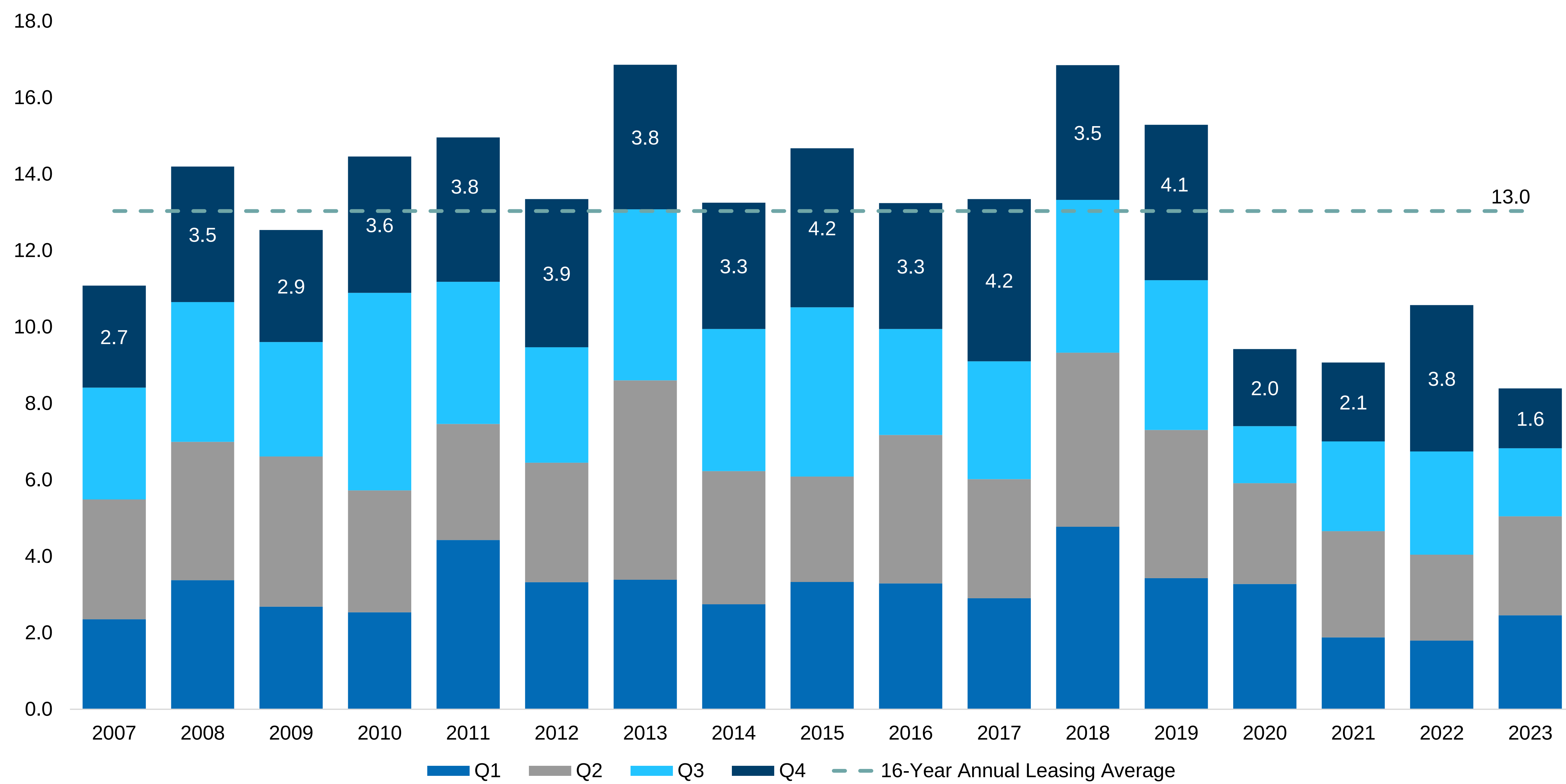


Source: Newmark Research

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. Annual leasing volume for 2023 is slightly lower than over the past three years, driven partly by a slower fourth quarter of leasing activity.

Total Leasing Activity (msf)

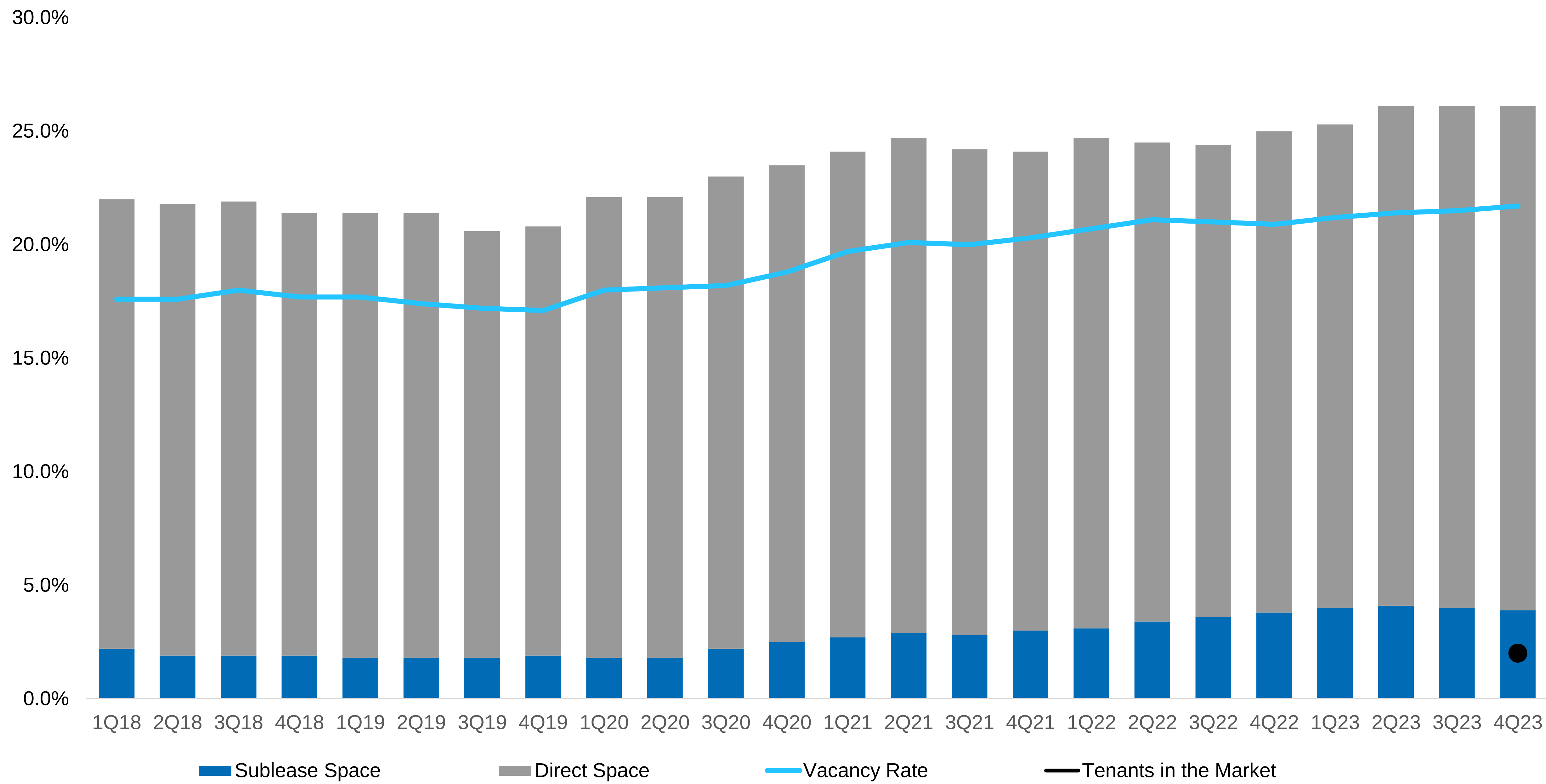


Source: Newmark Research, CoStar

Availability Continues to Increase While Tenant Demand Drops

Available office space sits at a historical high, both in terms of direct and sublease space. Over the past eight years, the direct availability rate has averaged 18.8% while the sublease availability rate has averaged 2.6%. The 4Q23 availability rates of 21.5% for direct space and 3.4% for sublease space are well above the long-term average. 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

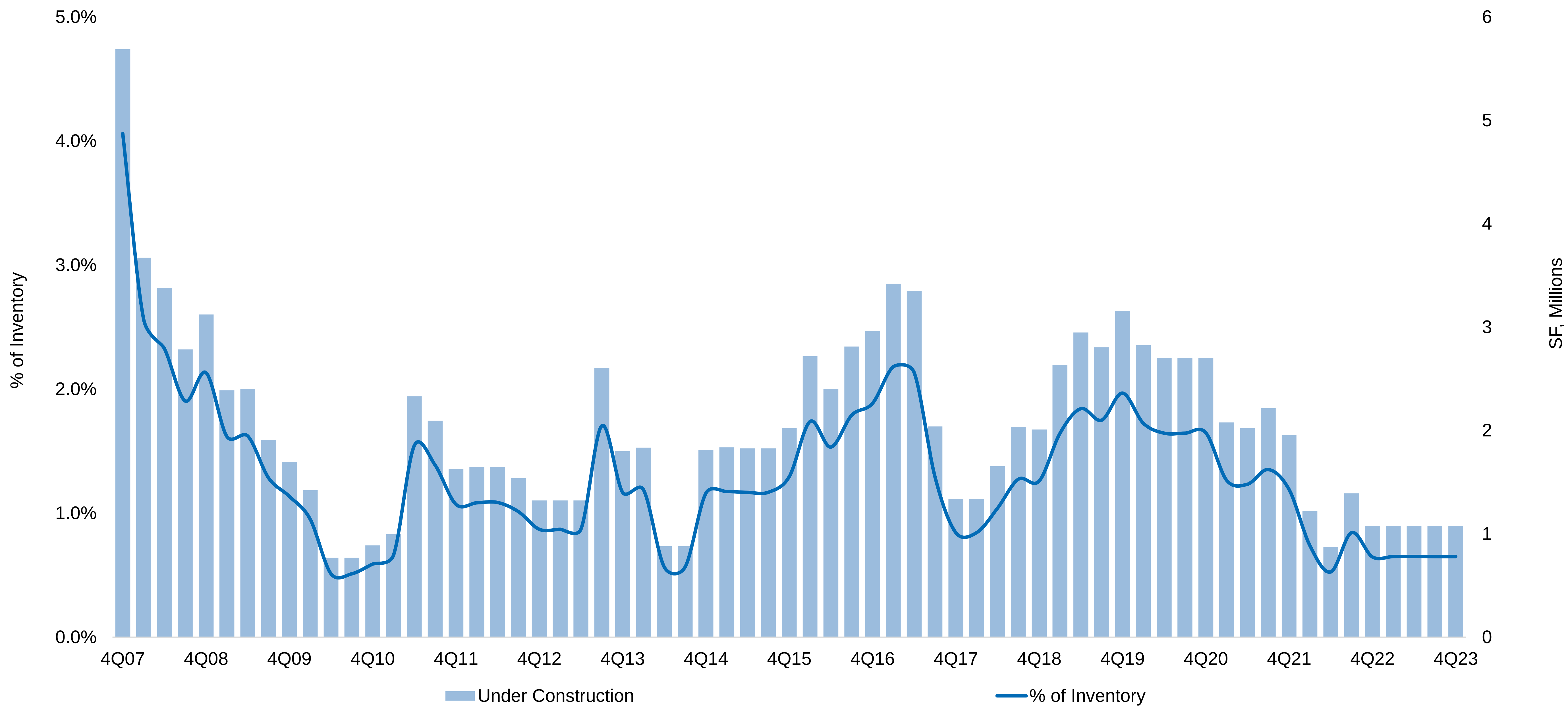


Source: Newmark Research

Deliveries Slow as Office Construction Pipeline Tapers

Northern Virginia's development pipeline remains historically low, with no deliveries and no new projects breaking ground in all of 2023. There are currently five office properties under construction in Northern Virginia, totaling 1.0 million square feet. With demand continuing to be limited as companies adjust to the post-COVID office environment, a lack of new supply will help ease rising vacancy.

Office Under Construction and % of Inventory

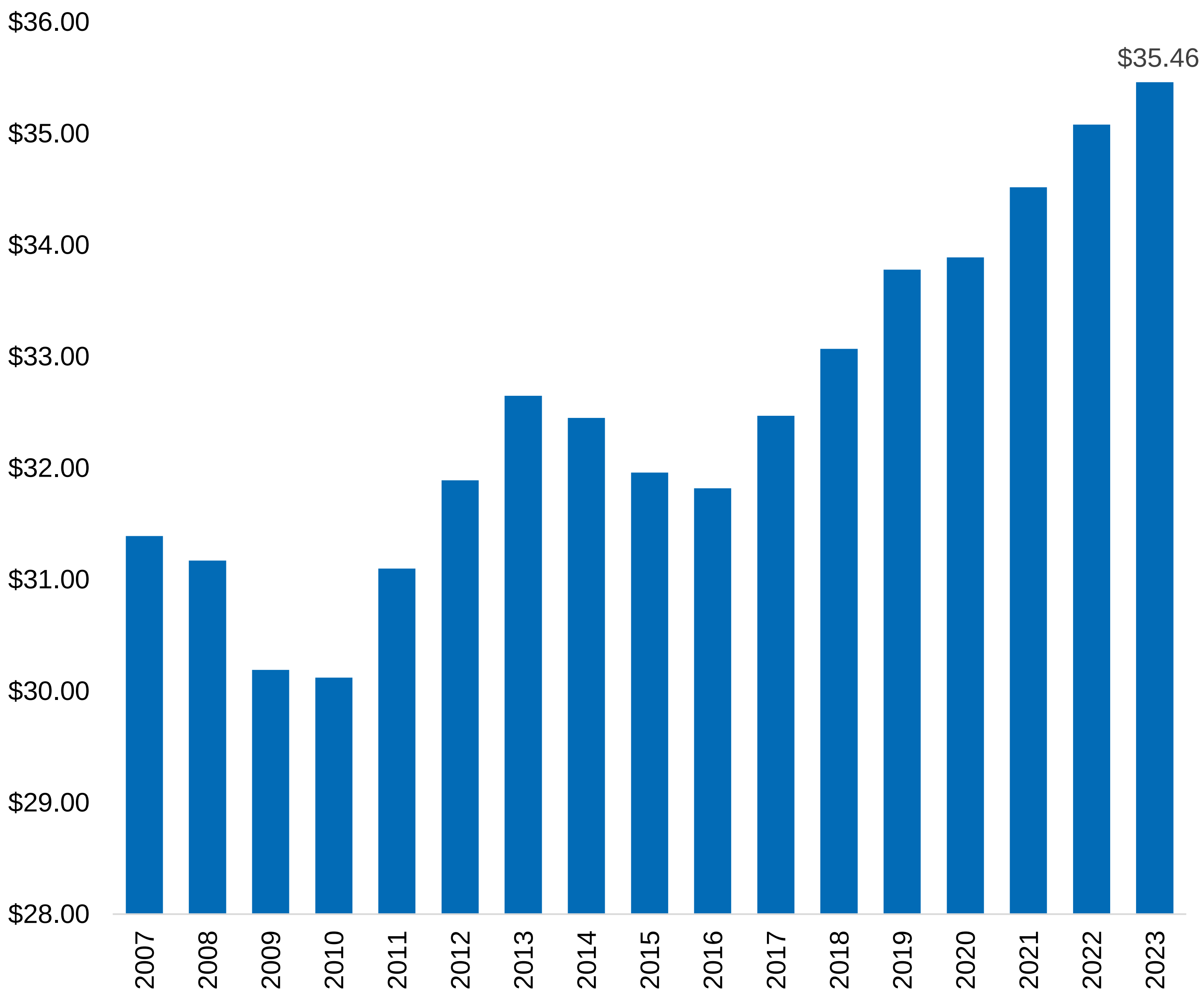


Source: Newmark Research, CoStar

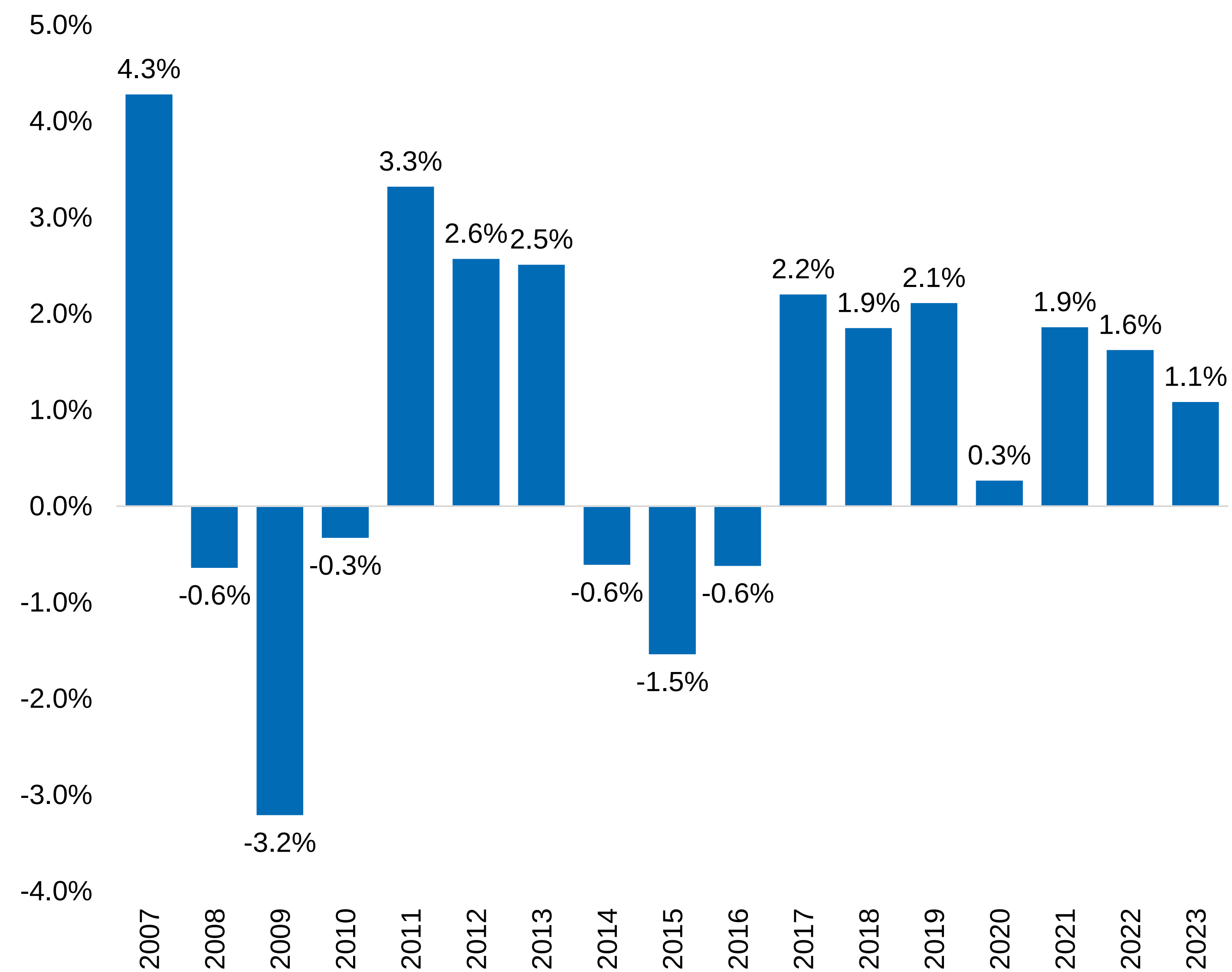
Market Maintains Rent Growth at a Decelerating Rate

In past cycles, asking rents have adjusted downward to account for depressed demand, but it often takes many quarters or even years for rates to fall, as asset owners seek to maintain face rates while increasing concessions to attract tenants. Rent growth has decelerated over the past three years but is still on par with the 1.0% year-over-year average since 2007.

Office Average Asking Rent, $/SF, FS



Year-over-Year Asking Rent Growth Rate

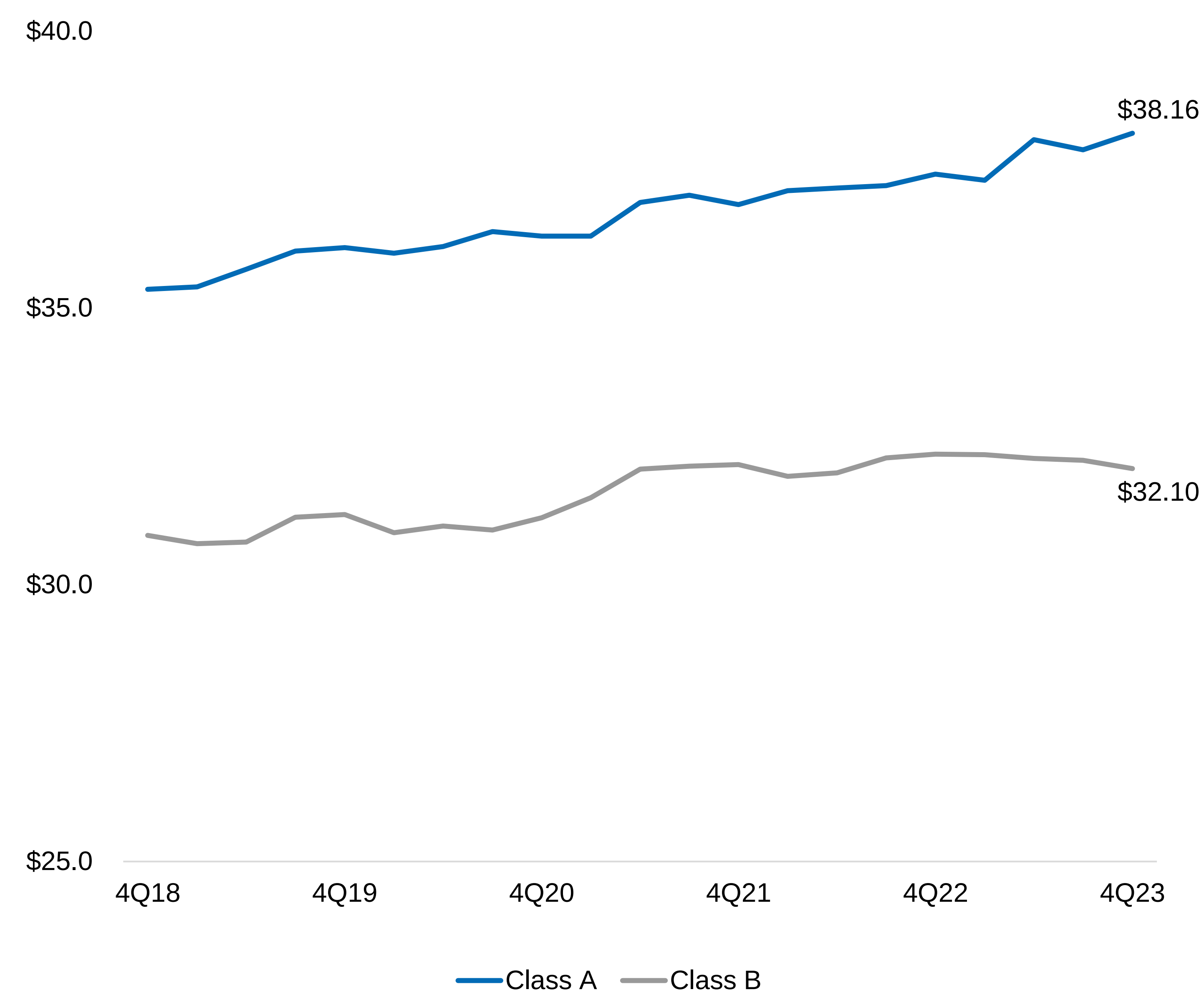


Source: Newmark Research, CoStar

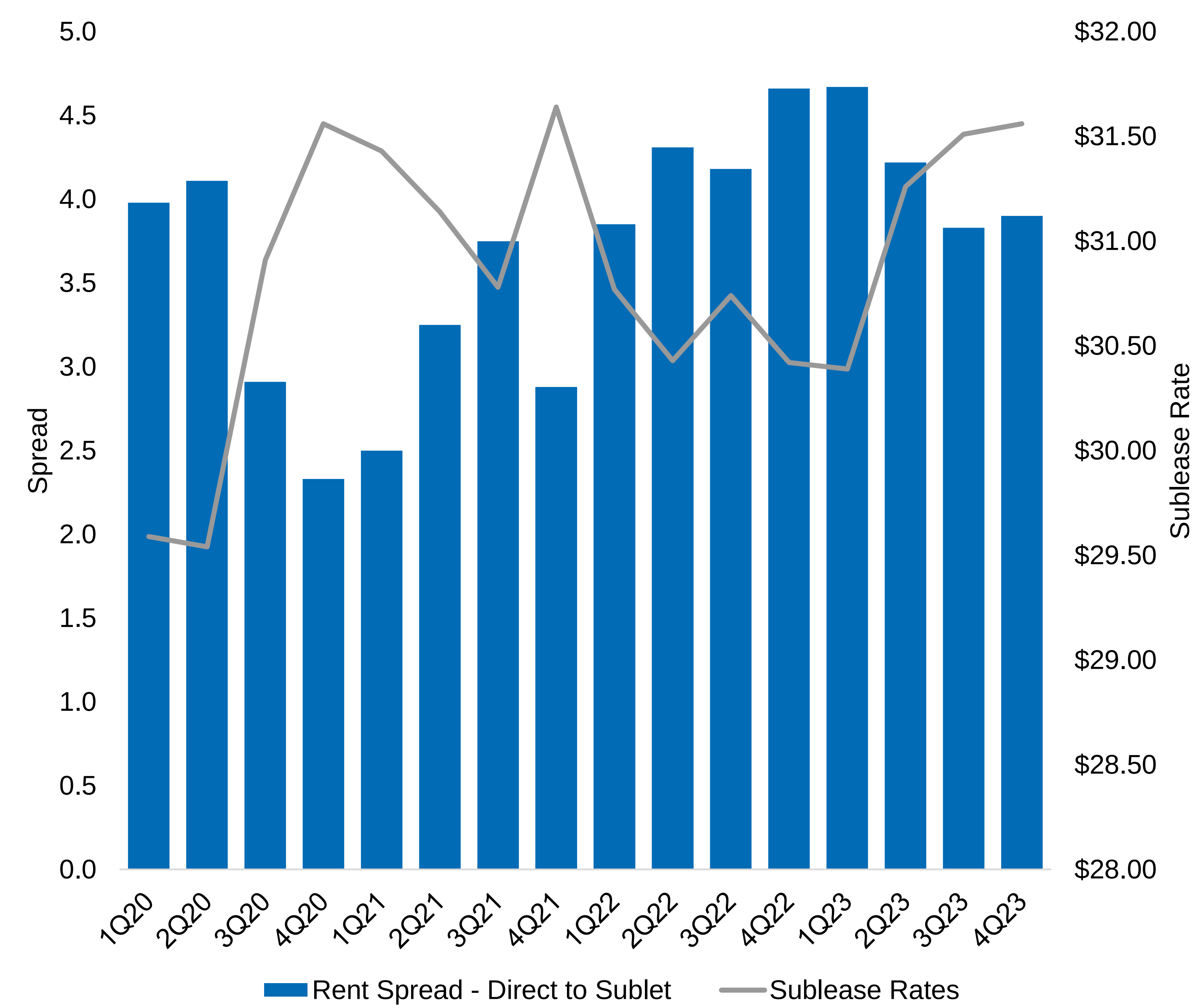
Asking Rents Continue to Rise

While Class B rents saw a slight decline over the past year, Class A rents have seen positive movement, increasing 2.0% year-over-year. This is indicative of the bifurcation of office user demand. Trophy and Class A space is outperforming, while Class B and Class C rates will continue to drop or remain stagnant in the face of limited demand.

Class A and Class B Asking Rents



Sublease Rates



Source: Newmark Research, CoStar

Leasing Activity Remains Limited

Despite negative absorption, leasing activity continues, albeit at a slower pace. The largest fourth quarter transactions were lease renewals, however, a handful of larger new leases were signed during the quarter, signaling tenants' confidence in making long-term real estate decisions while also weighing future space needs and hybrid work models.

Notable 4Q23 Lease Transactions

Tenant	Building(s)	Submarket	Type	Square Feet
Amazon	241 18th Street	Crystal City / Pentagon City	Lease Renewal	88,000
Accenture Federal Services	5155 Parkstone Drive	Rt. 28 South	Lease Renewal	77,245
Washington University of Science and Technology	2900 Eisenhower Avenue	Eisenhower Avenue	New Lease	59,778
Cambridge Associates	950 N Glebe Road	Ballston	New Lease	48,181
Baker Tilly	8270 Greensboro Drive	Tysons Corner	New Lease	44,316

Source: Newmark Research

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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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