

4Q23

Phoenix Office Market Overview



Market Observations

Economy

- Phoenix’s labor market remains strong, with a 3.5% unemployment rate in November, even with the national average.
- Education and health services led local job gains over the past 12 months, with information and other services seeing the biggest losses.
- Overall office-occupying employment is up 7.8% compared to pre-pandemic levels. The big question for the Metro, like other similar large markets, is to what degree global layoffs at large tech firms, such as Google, Meta and Amazon, impact local jobs going into 2024.

Major Transactions

- Larger tenants such as Peckham and Northrup Grumman signed new leases during the fourth quarter.
- Quarterly leasing volume was strong, up 18.4% comparing fourth-quarter 2023 to fourth-quarter 2022. Annual leasing met predictions and surpassed totals from 2020 to 2022. While leasing activity is down compared to pre-pandemic totals, it is more stable relative to other metros in the Southwest region.
- Sales activity was up 50.0% quarter-over-quarter. Both investors and occupiers made big moves throughout the region. Private buyers were the main players in acquisitions, making up over 80% of transactions.

Market Fundamentals

- Office occupancy in the fourth quarter of 2023 contracted by 515,666 SF. Overall net absorption losses for the year totaled 1.7 million SF. Absorption losses are expected to slow but continue into 2024.
- Under-construction activity has trended down sharply since 2020. Hybrid work models and rising sublet availability are deterring developers from breaking ground.
- Vacancy and asking rents both increased year-over-year. Total vacancy grew to 23.3%, with under 500,000 SF of new product coming online during 2023.
- Sublease space entering the market has slowed down, with the transition from sublease availability to direct escalating. More direct-transitions are expected since most of today’s sublet offerings come to term in 2024 and 2025.

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 sales activity.
- Market vacancy will increase further as lease expirations occur and tenants continue the trend of renewing and/or leasing at smaller footprints.
- Phoenix remains an attractive locale for both local and out-of-state office users due to its strong economic fundamentals in population growth, diversified economic sectors and a highly educated workforce.

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2. Market Fundamentals
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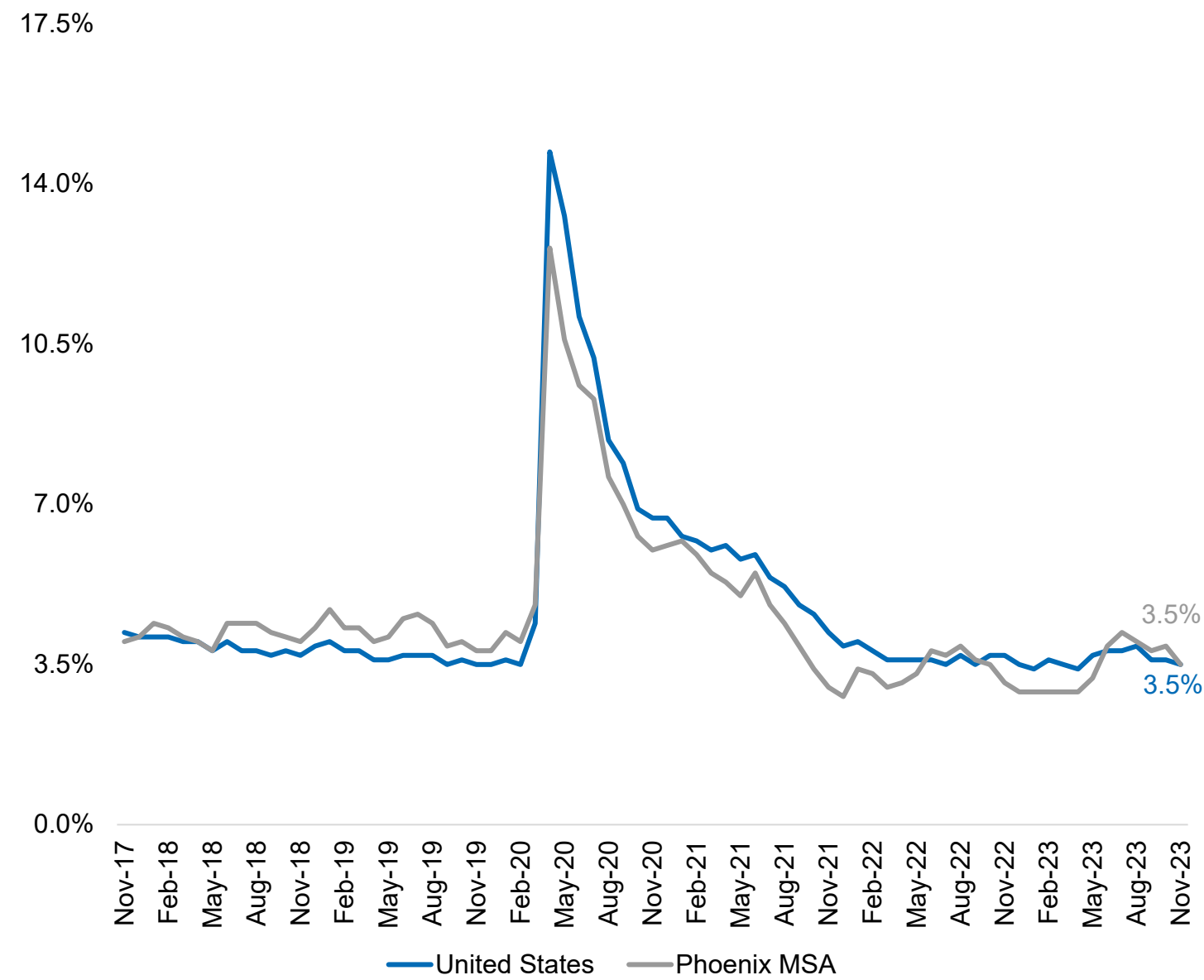
Economy



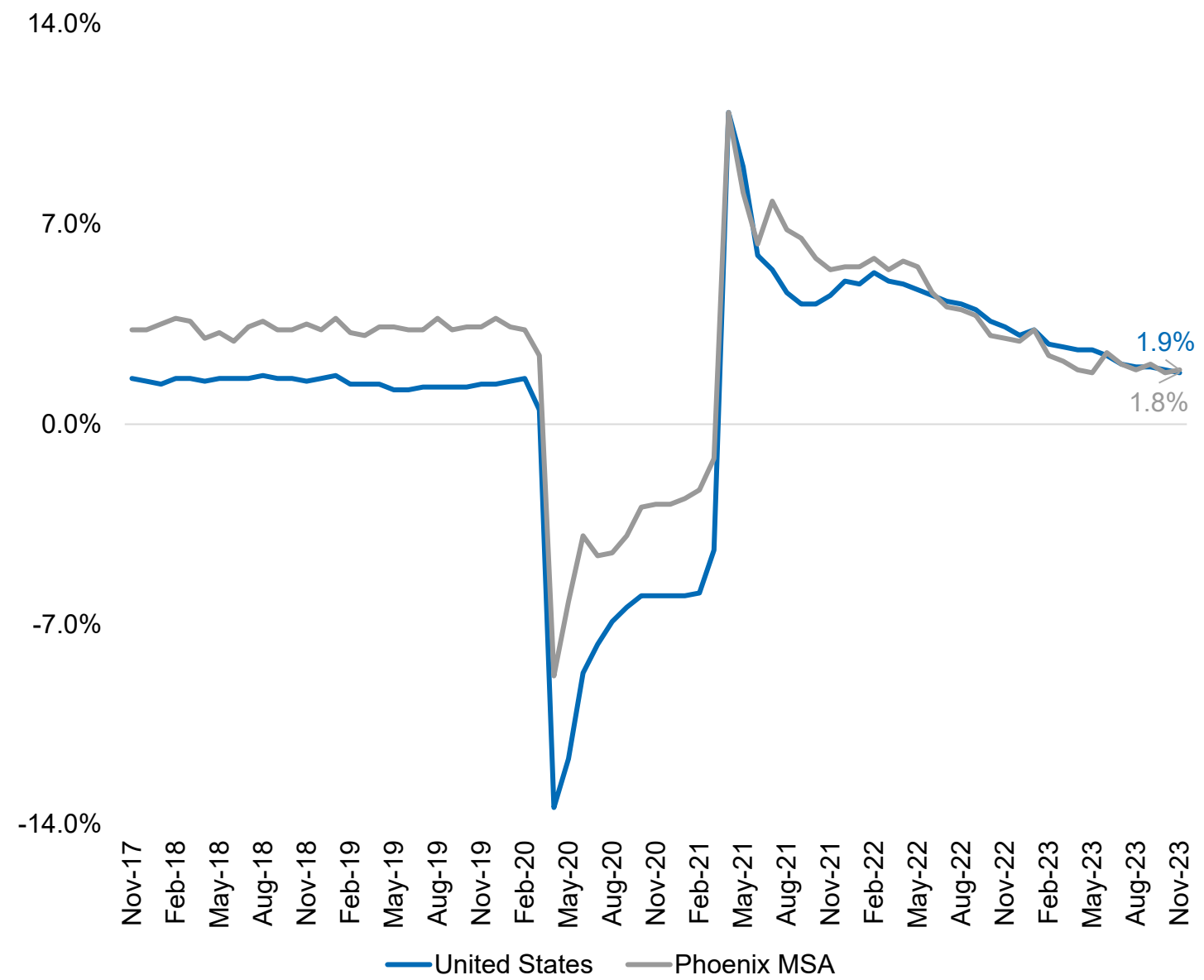
Phoenix’s Labor Market Mirrors National Averages at Year-End

Local unemployment is reminiscent of pre-pandemic averages and matched the national rate in November. Overall local job growth has slowed but remains in the positive for now as companies adapt to softening economic conditions.

Unemployment Rate, Not Seasonally Adjusted



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



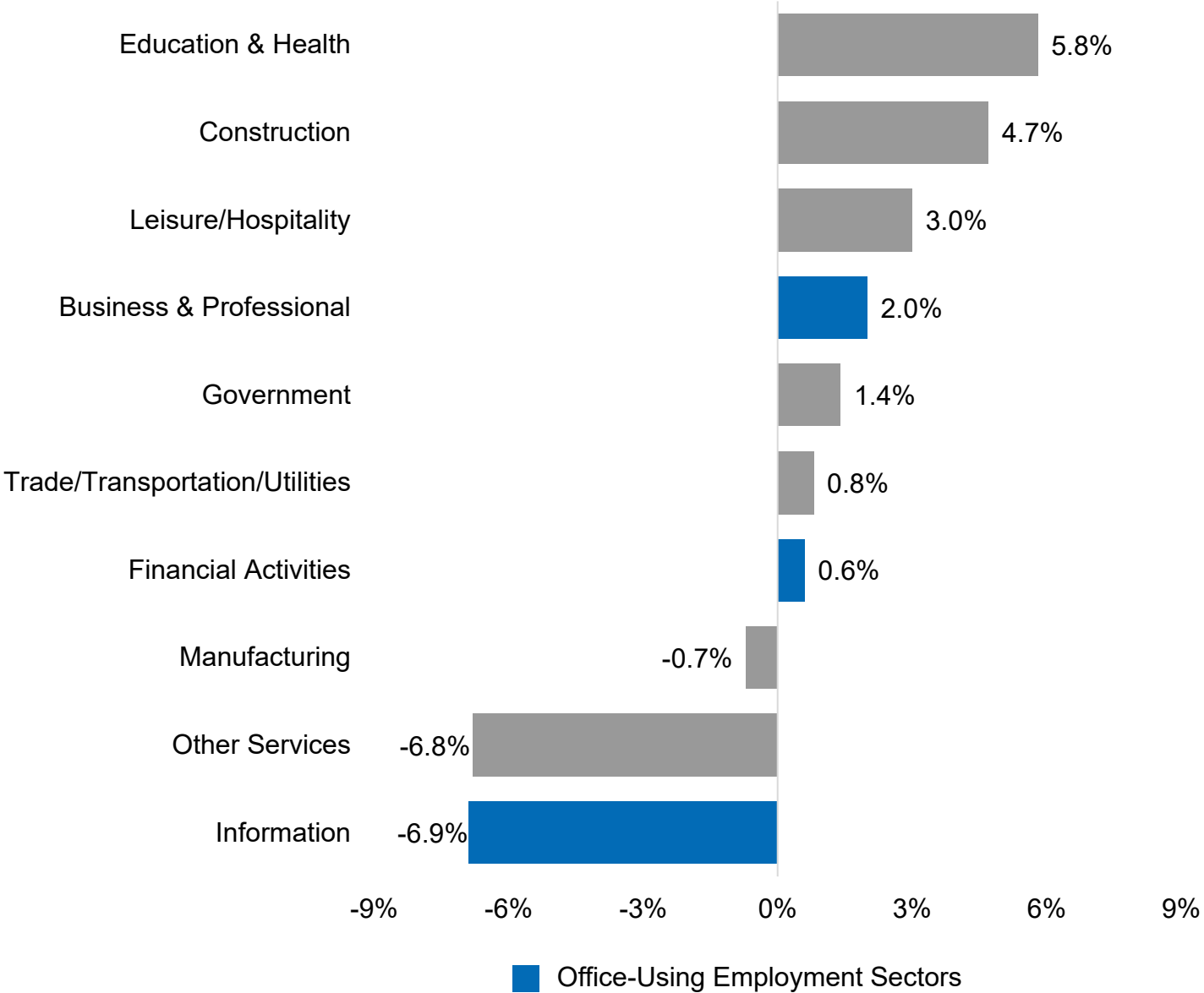
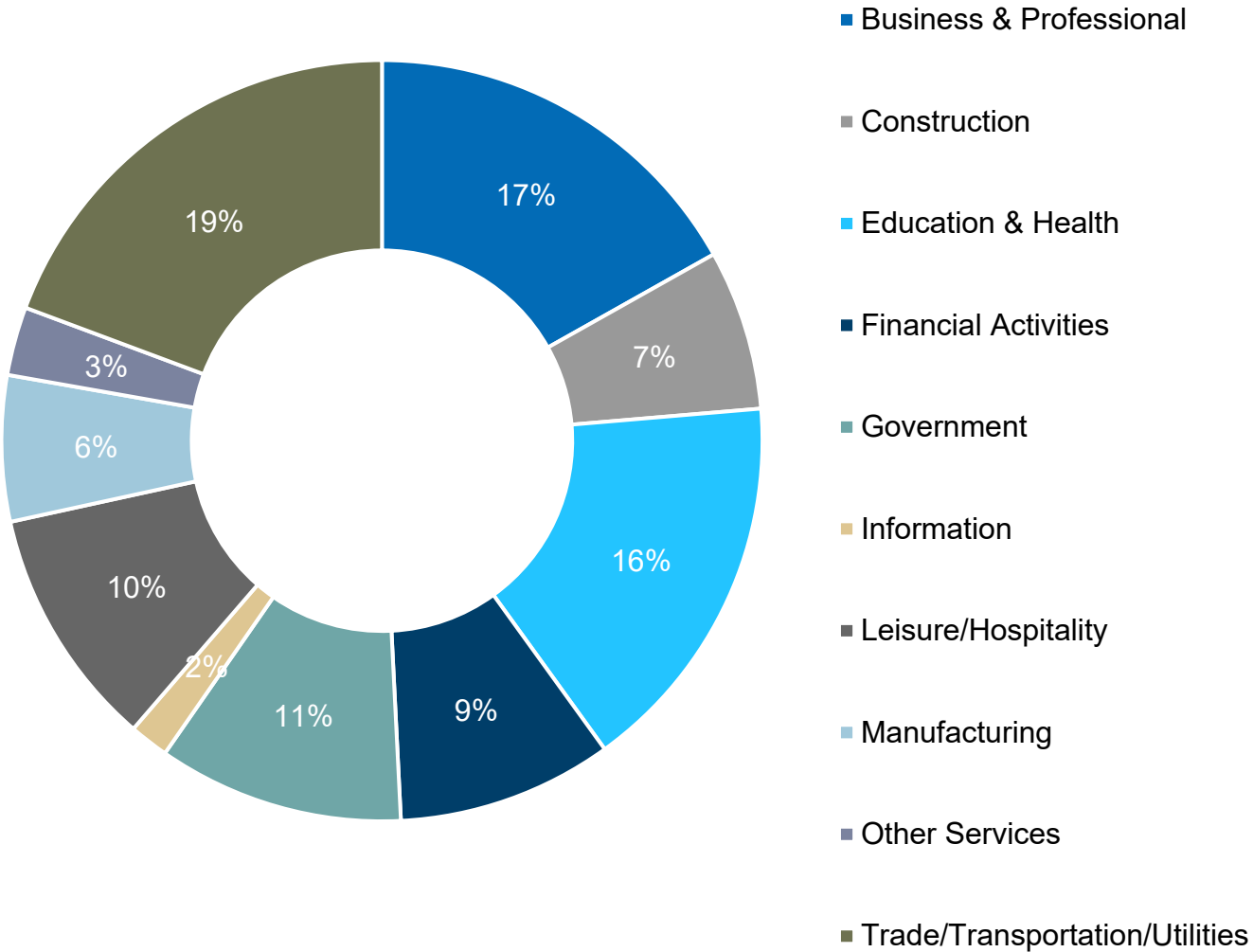
Source: U.S. Bureau of Labor Statistics, Phoenix MSA
Note: November 2023 data is preliminary.

Job Growth Was Pronounced in Already Strong Employment Sectors

Education and health led all industries in annual job growth, followed closely by construction and leisure/hospitality. Sizeable population growth in recent years supports the first two segments, while construction remains elevated on account of record high industrial development in the region. For office-occupying sectors: information contracted by 6.9%; financial activities and business and professional both saw modest gains.

Employment by Industry, November 2023

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

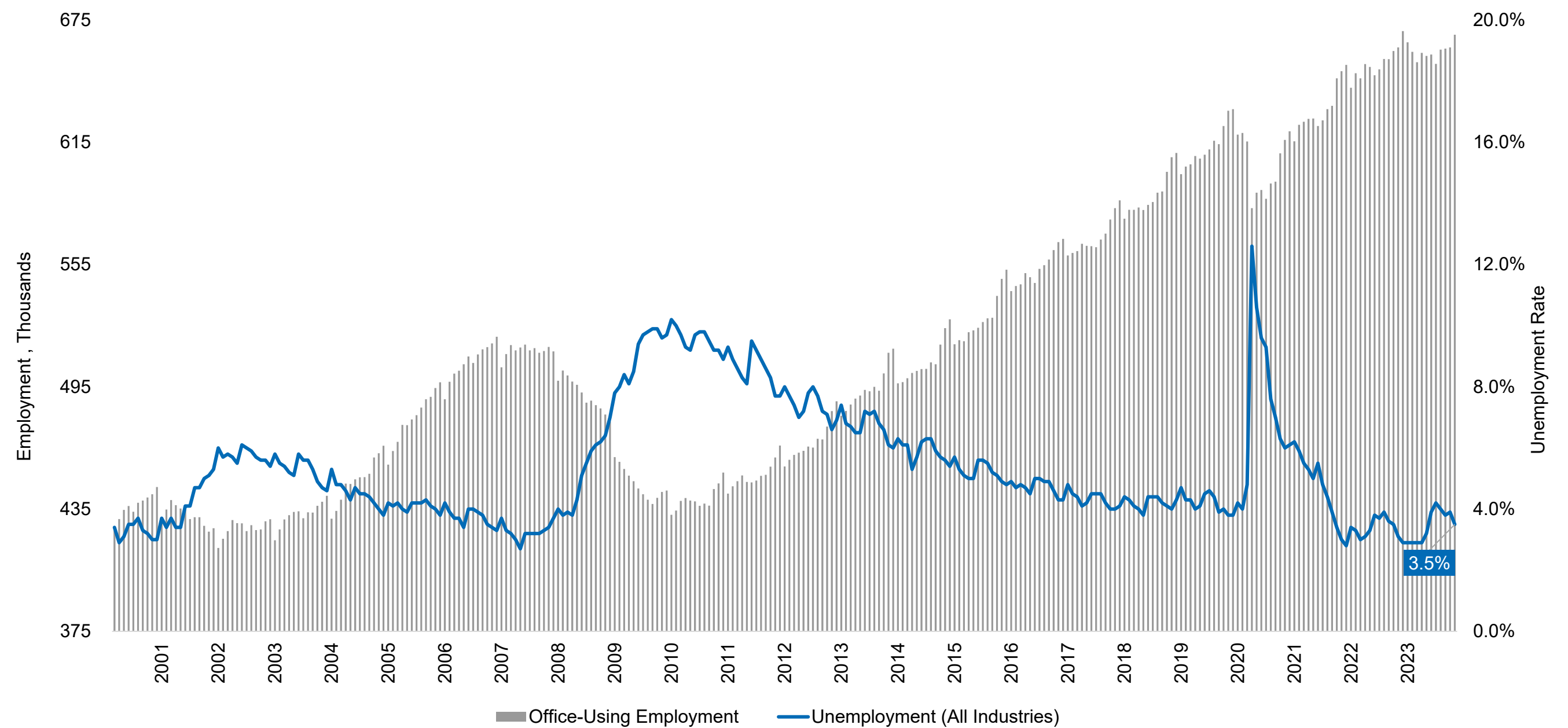


Source: U.S. Bureau of Labor Statistics, Phoenix MSA
Note: November 2023 data is preliminary.

Office-Using Employment Reaching Stabilization

Office-using employment totaled 667,800 jobs in November 2023, 7.8% higher than the market’s pre-pandemic total from February 2020. Although white-collar employment remains healthy, there have been modest inclines and declines since December 2022 due to fluctuations in the financial activities and information sectors since the start of 2023.

Office-Using Employment* and Unemployment Across All Industries



Source: U.S. Bureau of Labor Statistics, Phoenix MSA
Note: November 2023 data is preliminary.
*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.

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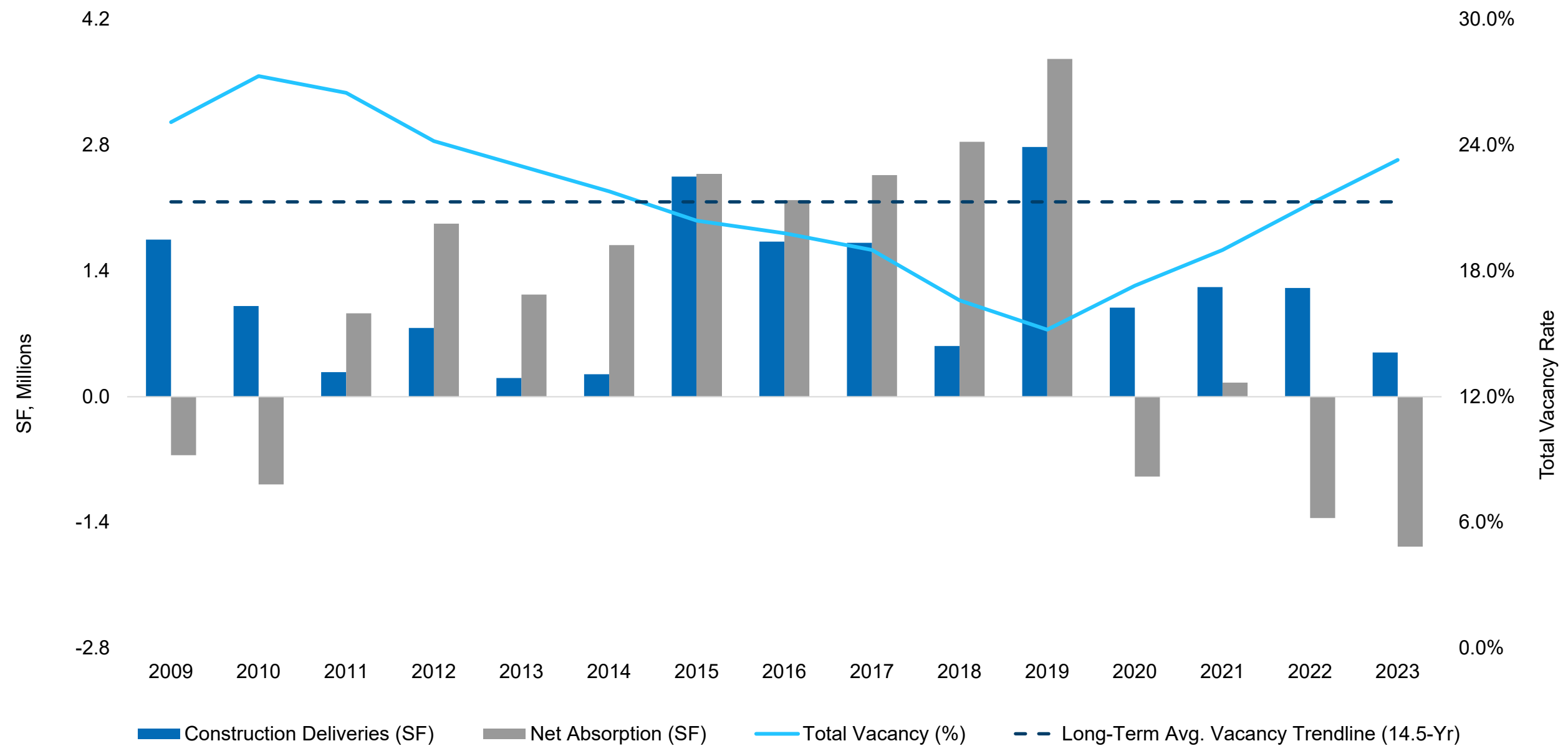
Market Fundamentals



Rising Vacancy and Absorption Losses Outpace Office Deliveries for Another Year

Total vacancy was 23.3% at the end of the fourth quarter of 2023, higher than the 14.5-year average (21.3%) for the first time since 2014. Space givebacks throughout 2023 continue as office users contract footprints in both renewals and new leases. Overall vacancy will progressively level out as office construction slows.

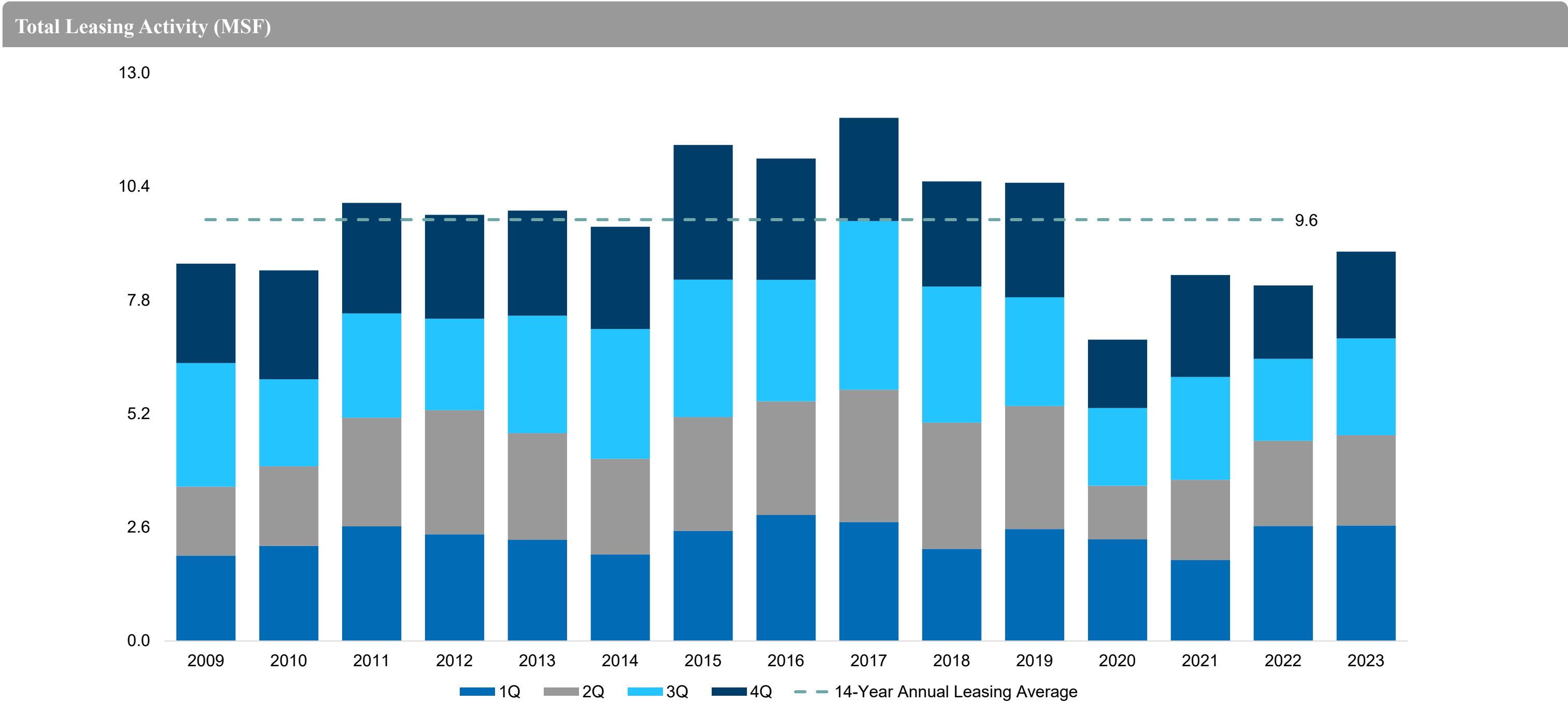
Historical Construction Deliveries, Net Absorption, and Vacancy



Source: Newmark Research

2023 Leasing Activity Surpassed 2020, 2021 and 2022

While this is encouraging, 2023 leasing activity fell short of the 14-year annual leasing average (9.6 MSF) SF by 7.6%. Leasing in the fourth quarter of 2023 was up 18.4% compared to the same period in 2022; a standout trend compared with other Southwest markets and their slowing leasing activity.

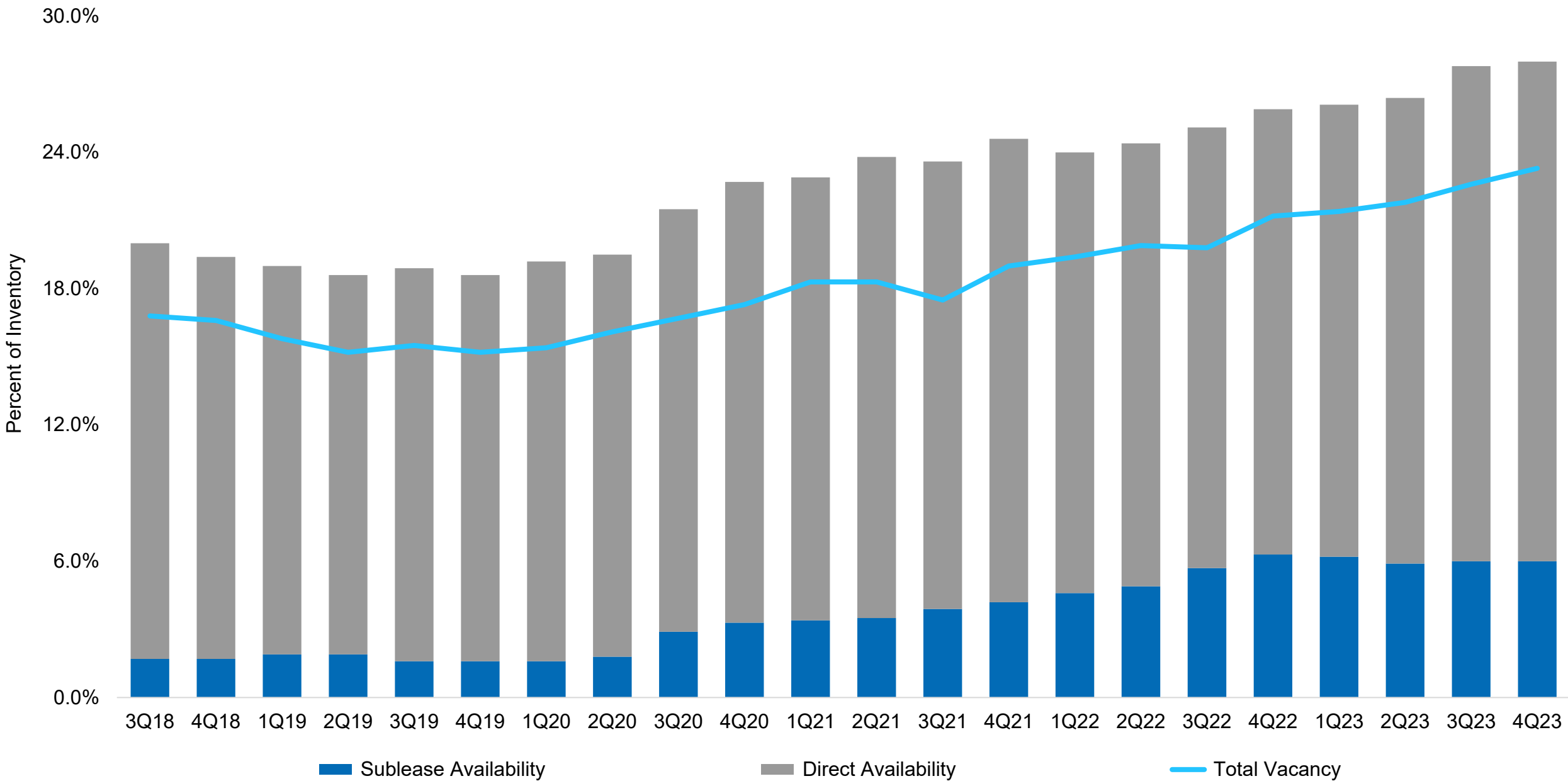


Source: Newmark Research

Availability Increases Slow; Spaces Moving Vacant Pushes Vacancy Upwards

From the onset of the pandemic until the end of 2022, sublease availability saw steady increases as tenants reduced footprints for a multitude of reasons, including hybrid work models and general cost-saving measures. Sublease space has held steady at around 6.0% since the beginning of 2023 with overall availability also finding stabilization in the second half of 2023. Sublease spaces are staying on market longer and are contributing to increased vacancy as tenants officially vacate.

Available Space and Total Vacancy as Percent of Overall Market

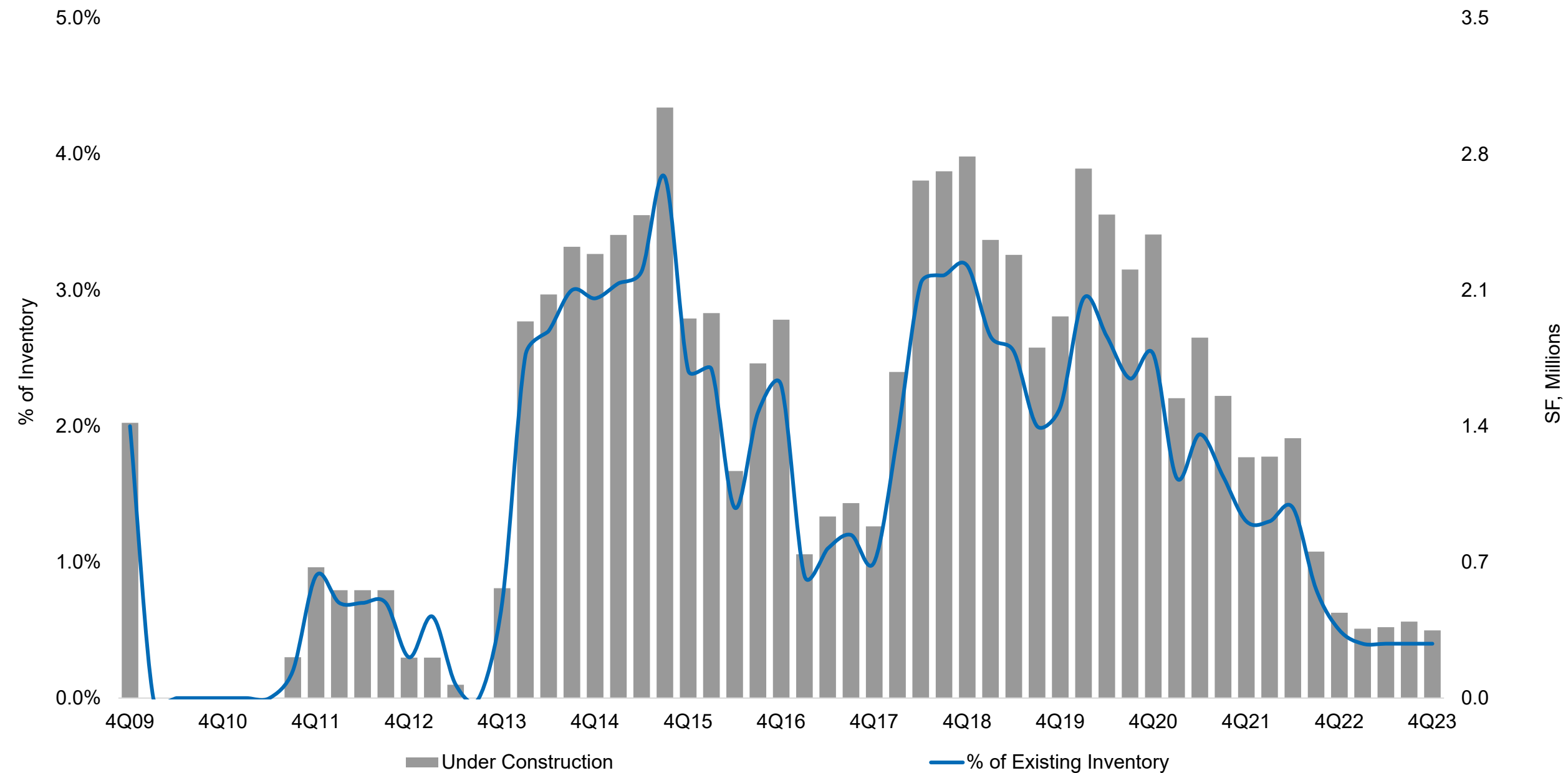


Source: Newmark Research

Under-Construction Activity Dwindles

Hybrid work models, sublet availability and measured tenant demand relative to pre-pandemic averages caused a sharp reduction in office under-construction activity since 2020. With only 492,714 SF of traditional office space delivered in 2023 and less than 400,000 SF presently underway, the office development pipeline is at a 10-year low.

Office Under Construction and % of Existing Inventory

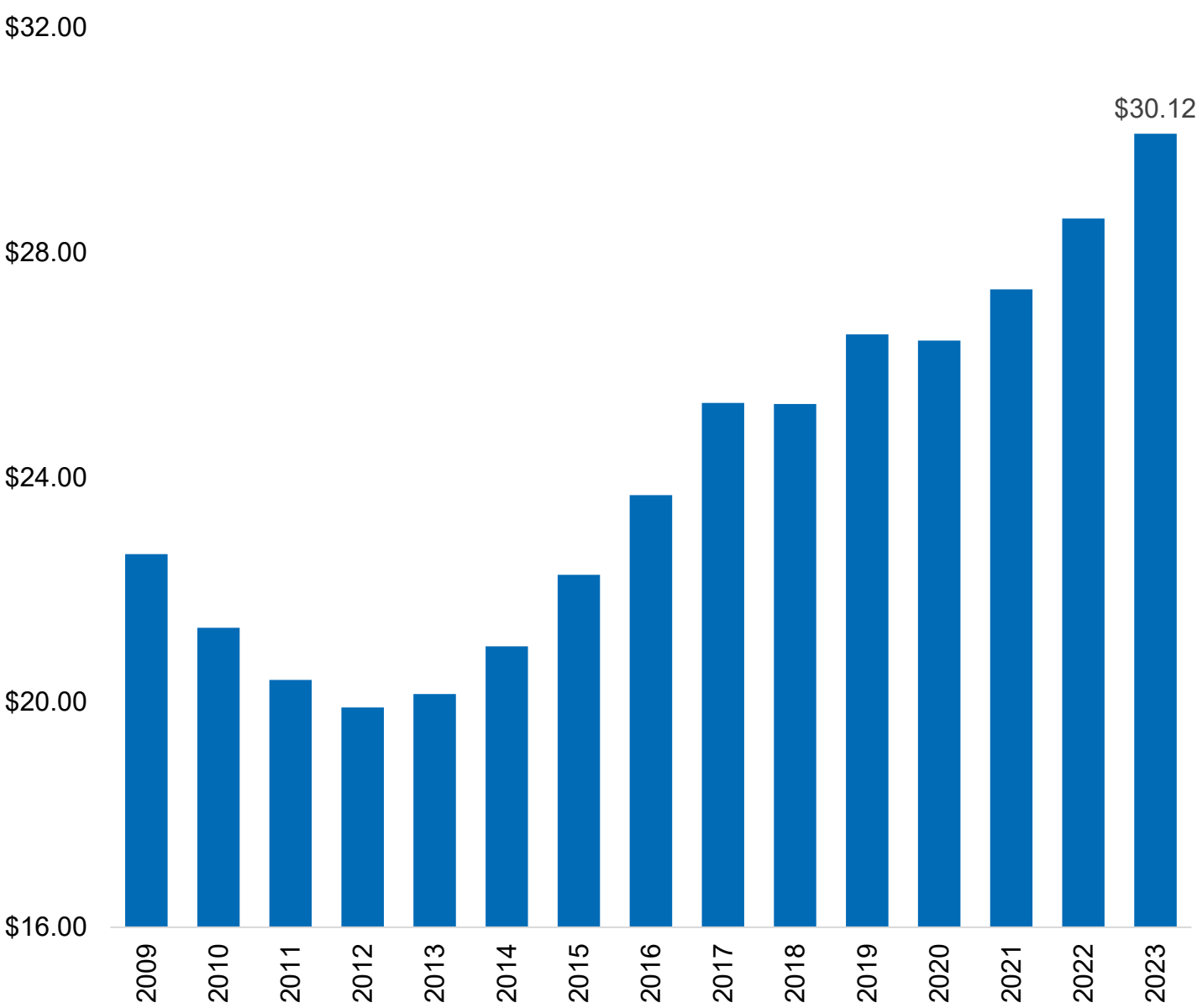


Source: Newmark Research

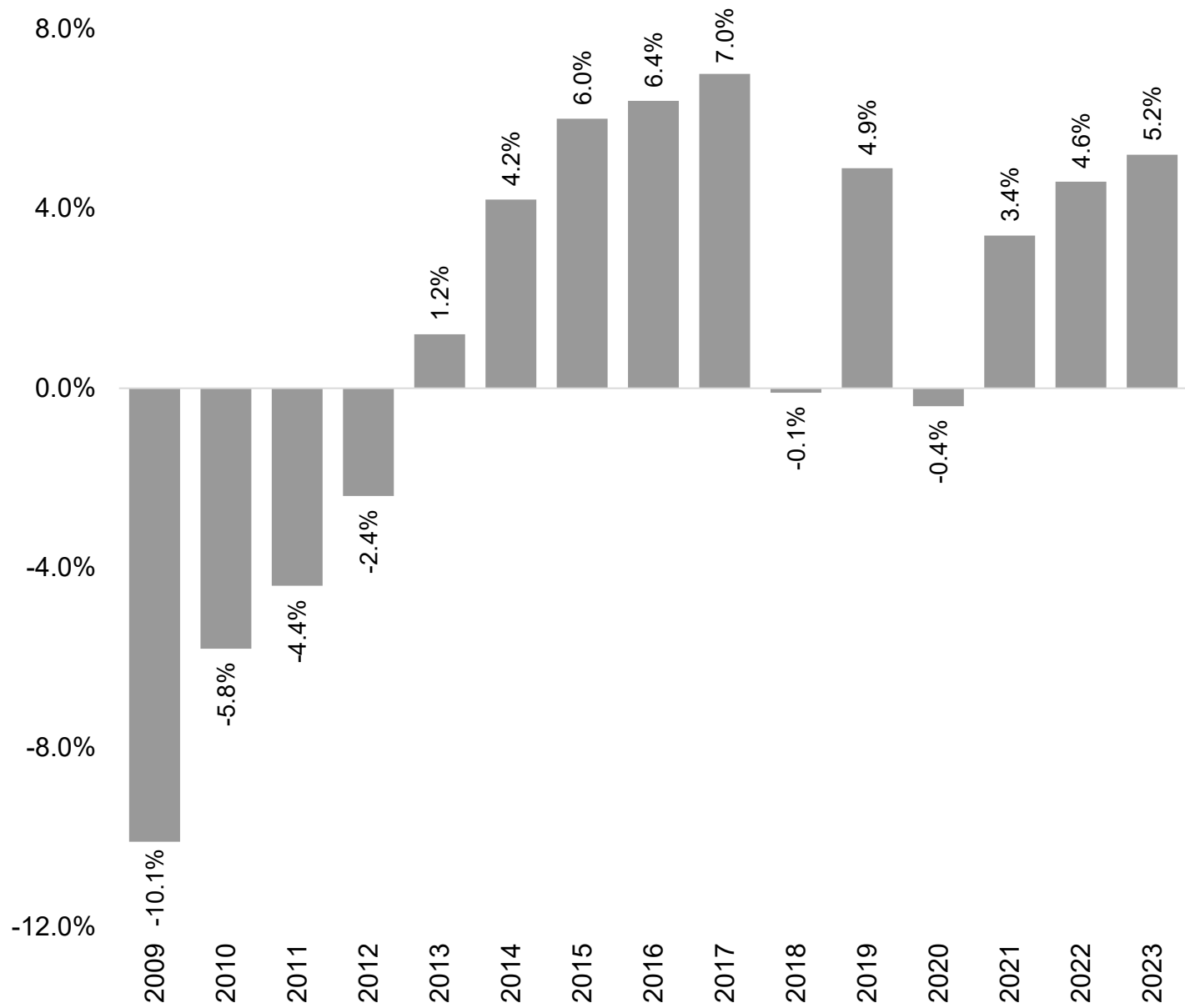
Asking Rents Continue to Climb for Now

Despite rising vacancy, overall asking rates increased this quarter and hit a new record of \$30.12/SF. Landlords are holding rates for direct space, preferring to offer more in way of concessions and tenant improvement allowances to attract and retain tenants. Rent growth in 2023 averaged 5.2%, with Class B and C rents seeing the highest annual increases.

Office Average Asking Rent, \$/SF/Year, FS



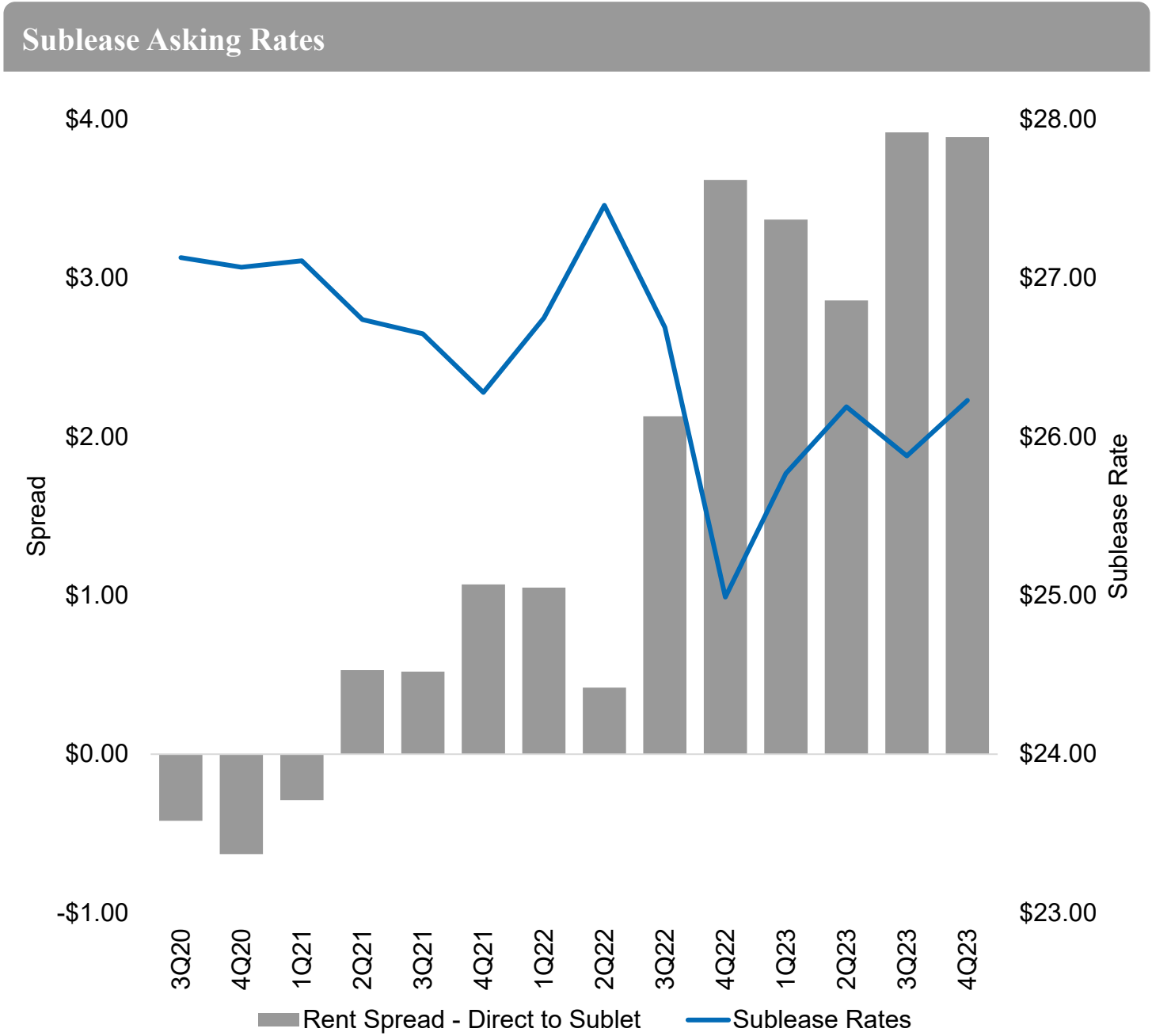
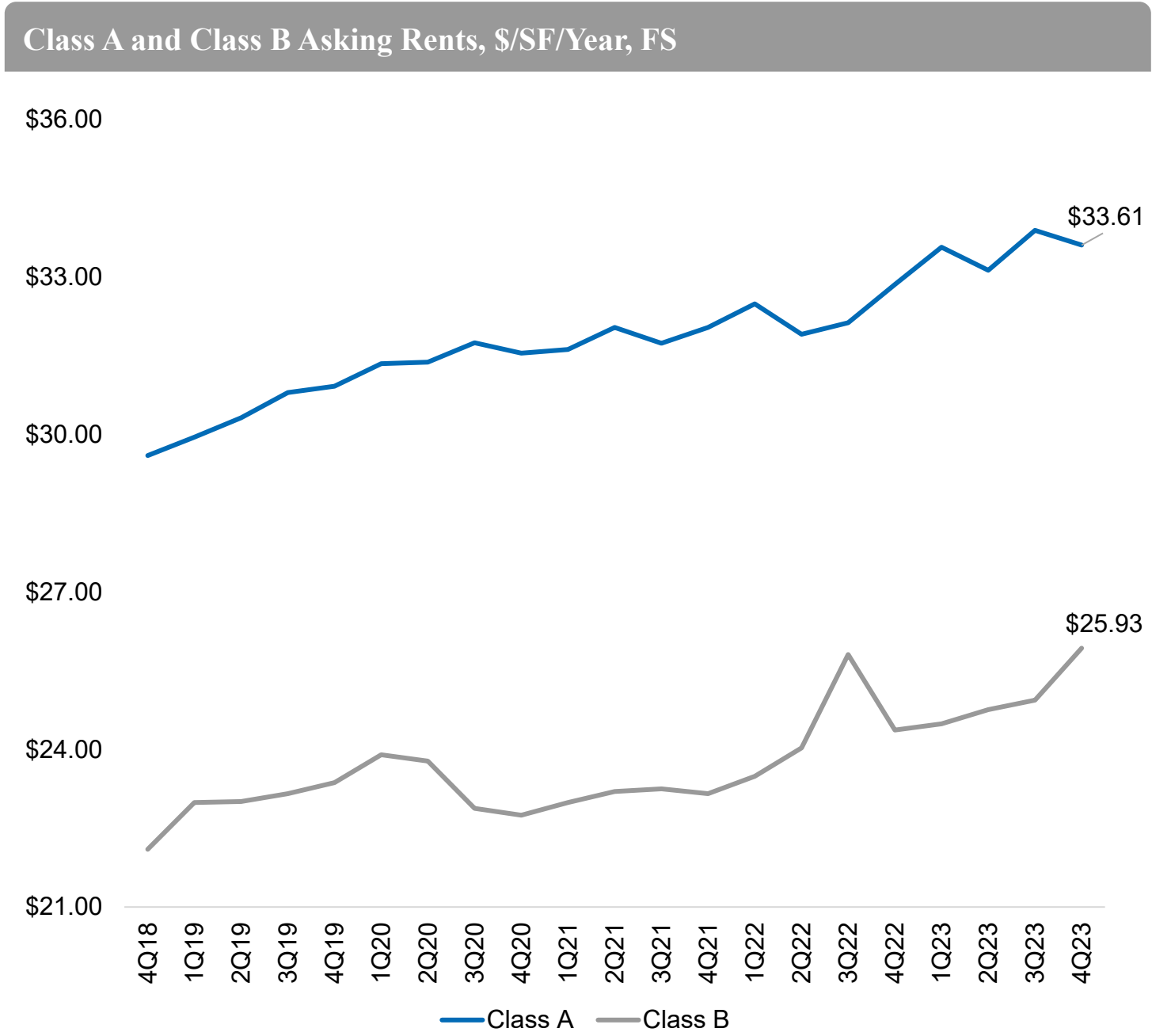
Year-over-Year Asking Rent Growth Rate



Source: Newmark Research

Delta Between Direct and Sublet Asking Rates in Holding Pattern

Class A direct asking rents were flat compared to three months ago, while Class B rose. This caused the direct average asking rent across all property classes to increase. Sublease asking rents were up as well, with the rent spread between direct space holding steady at \$3.89/SF. Class A direct asking rents in Tempe and Camelback Corridor sit above \$40/SF, new watermark highs.



Source: Newmark Research

New Leases Dominated Lease Transactions in Fourth Quarter of 2023

Tempe and Airport Area submarkets welcomed new, larger tenants during the fourth quarter of 2023. With high population growth, strong economic diversity and a highly educated workforce, Phoenix remains a strong location for many office users to conduct business.

Notable 4Q23 Lease Transactions				
Tenant	Building(s)	Submarket	Type	Square Feet
Peckham	One Compass Center	Airport Area	Direct Lease	136,194
After moving from sublease to direct, Peckham took over the 136,194 SF office block at One Compass Center.				
Northrop Grumman	Gilbert Spectrum	Chandler/Gilbert	Direct Lease/Expansion	119,222
The aerospace and defense company, Northrop Grumman, expanded its Valley footprint at Gilbert Spectrum.				
OfferPad	The Beam	Tempe	Direct Lease	39,985
Based out of Chandler, OfferPad signed a new lease for 41,164 SF in the Tempe Submarket.				
Clin-Path Associates	Workspace Cotton Center	Airport Area	Direct Lease	30,539
Arizona's largest private pathology practice, Clin-Path Associates, entered a new space at Workspace Cotton Center.				
Ports America	Tempe Gateway	Tempe	Direct Lease	27,240
Ports America, the largest U.S. terminal operator and stevedore, signed to occupy 27,240 SF in Tempe.				
Bonneville International	The Summit	Northwest Phoenix	Downsize/Renewal	24,472
Located in the Northwest Phoenix, Bonneville International renewed and downsized its lease, shifting from 30,061 SF to 24,472 SF.				

Sales Activity Remained Robust Throughout the Phoenix Office Market

The Deer Valley Airport submarket attracted investors in the fourth quarter of 2023 with the purchase of Blackhawk Corporate Center and The Corridors. A mix of investors and occupiers sought out product in the Metro with overall transaction activity up by 50.0% quarter-over-quarter.

Notable 4Q23 Sale Transactions				
Building Address	Submarket	Sales Price	Price/SF	Square Feet
Blackhawk Corp. Center I, II, III – 2902 & 3010 W. Agua Fria Fwy.	Deer Valley Airport	\$46,000,000	\$182	252,350
Big Sky Medical acquired the 96% leased, three-building, single story, multi-tenant office and medical office portfolio from ViaWest & Taconic.				
The Corridors – 1925-2095 W. Pinnacle Peak Rd.	Deer Valley Airport	\$32,925,000	\$200	632,427
The Voit Company purchased the freestanding, exterior loaded multi-tenant office portfolio from Libitzky Property Company.				
Discovery Business Campus – 2180-2190 E. Elliot Rd.	Tempe South/Chandler	\$29,170,915	\$200	146,216
Wentworth Property Company acquired the newly constructed, three-story office with two long term leases in place from Northwood Investors.				
Scottsdale Northsight – 14350 N. 87 th St.	Scottsdale North/Airpark	\$26,500,000	\$191	138,693
Purchased by Providence Real Estate Group, this Class A office building was acquired for \$26.5 million.				
200EVB – 200 E. Van Buren St.	Downtown South	\$14,500,000	\$60	240,076
Stenson Tamaddon acquired the 245,513 SF office building in Downtown Phoenix for \$14.5 million with plans to occupy. The detached parking structure was not included in sale.				

Source: Newmark Research

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Appendix



Phoenix Metro Office Submarket Map and High-Level Statistics – 4Q23



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Population Has Increased Four Times Over the Past Five Decades



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