

# Greater Philadelphia Office, Q3 2017

## Suburban Market Booms, "Wait and See" in the CBD

▲ Net Absorption  
726,722 sq. ft.

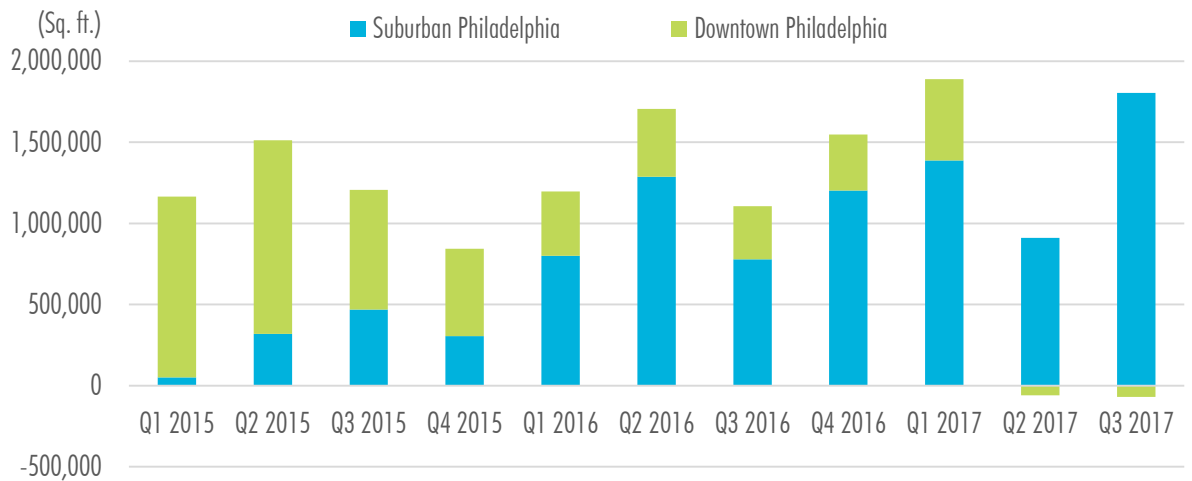
▼ Vacancy Rate  
14.4%

▼ Asking Lease Rate (FS)  
\$25.42

▲ Development  
2.93 Million sq. ft.

Figure 1: Net Absorption (4-quarter rolling sum)

\*Arrows indicate change from previous quarter



Source: CBRE Research, Q3 2017

**Downtown:** Minimal leasing activity in the downtown Philadelphia market led to very little change in vacancy figures. The largest transaction of the quarter was Morgan Lewis' 95,000 sq. ft. renewal at 10 Penn Center.

**Suburbs:** Occupancy within the Philadelphia suburbs grew by 935,538 sq. ft. in Q3 2017, the highest quarterly absorption total seen since 2008.

**Northern Delaware:** Downtown Wilmington continued its strong performance. Vacancy in the Class A market sat at 17% - a year-over-year decrease of more than 400 bps.

**Southern New Jersey:** Southern New Jersey cooled in Q3 2017 with -155,627 sq. ft. of net absorption, which was the first instance of occupancy losses tallied during the previous 5 quarters. Much of this was attributed to Lockheed Martin, who vacated 123,823 sq. ft. in Q3 2017 in Mount Laurel.

The Suburban Philadelphia office market posted its strongest quarter of demand in 12 years during Q3 2017. The 935,538 sq. ft. of net absorption builds on a pattern of strengthening demand in the suburbs, which began to form in 2014 and now eclipses the softening market fundamentals in Downtown Philadelphia.

The demand was broadly distributed across suburban office submarkets with only 2 out of 15 recording negative net absorption. The industries driving the bulk of higher office occupancy included Financial Activities Education and Health Services.

With the suburban office vacancy rate dropping 250 basis points over the last year from 17.6% in Q3 2016 to 15.1% in Q3 2017, the vacancy rate is now only 20 basis points above the low reached in the last cycle (14.9% in Q1 2008). As the economy continues to grow, and very little new supply in sight, we can expect this market to get tighter from here.

Figure 2: Philadelphia Metro Office Market Statistics

SUBMARKET	Number of Buildings	Inventory (Sq. ft.)	Total Vacancy Rate (%)	Total Availability Rate (%)	Under Construction (Sq. ft.)	2017 YTD Total Net Absorption (Sq. ft.)	Avg. Asking Lease Rate (\$Fsg/Psf/Yr)	Avg. Class A Asking Lease Rate (\$Fsg/Psf/Yr)
Market West	26	26,291,604	11.3%	14.4%	1,854,000	55,657	\$29.63	\$30.85
Market East	19	6,789,819	11.3%	16.4%	0	-93,541	\$27.58	\$28.14
Independence Hall	16	5,820,454	15.1%	21.7%	0	2,212	\$26.58	\$28.74
University City	23	4,565,028	7.4%	10.8%	340,000	-149,349	\$41.48	\$42.11
<b>Downtown Philadelphia Subtotal</b>	<b>109</b>	<b>43,466,905</b>	<b>11.4%</b>	<b>15.3%</b>	<b>2,194,000</b>	<b>-185,021</b>	<b>\$29.56</b>	<b>\$31.22</b>
Bala Cynwyd	29	2,873,673	11.3%	15.2%	0	48,401	\$30.18	\$31.70
Blue Bell	79	3,975,000	19.2%	23.3%	0	166,532	\$22.34	\$28.69
Central Bucks County	59	2,000,920	15.9%	25.2%	0	307,333	\$20.46	\$27.94
Conshohocken	26	3,394,001	10.7%	15.1%	0	-2,980	\$36.07	\$38.94
Delaware County	84	5,200,168	11.9%	17.2%	0	41,115	\$25.40	\$27.01
Exton/West Chester	91	4,120,931	13.8%	15.7%	0	78,960	\$24.31	\$26.60
Fort Washington	45	3,314,763	20.0%	25.8%	69,000	-66,920	\$24.02	\$27.55
Horsham/Willow Grove	84	5,138,706	16.6%	21.0%	0	152,727	\$23.06	\$25.20
Jenkintown	21	1,352,695	15.4%	16.4%	0	49,061	\$23.56	\$24.93
King of Prussia/Valley Forge	232	16,837,424	13.0%	17.2%	0	541,994	\$26.21	\$30.65
Lower Bucks County	111	5,256,034	21.2%	24.5%	0	115,989	\$23.70	\$26.13
Main Line	46	2,770,882	9.3%	12.0%	0	-102,058	\$35.78	\$37.68
North Penn	14	936,098	37.3%	38.5%	0	88,613	\$19.48	\$19.97
Plymouth Meeting	37	2,352,075	16.0%	23.1%	0	4,837	\$29.61	\$31.58
Upper Main Line	41	1,231,589	17.2%	20.1%	0	64,675	\$26.41	\$28.79
<b>Suburban Philadelphia Subtotal</b>	<b>999</b>	<b>60,754,959</b>	<b>15.1%</b>	<b>19.3%</b>	<b>69,000</b>	<b>1,488,279</b>	<b>\$25.17</b>	<b>\$29.09</b>

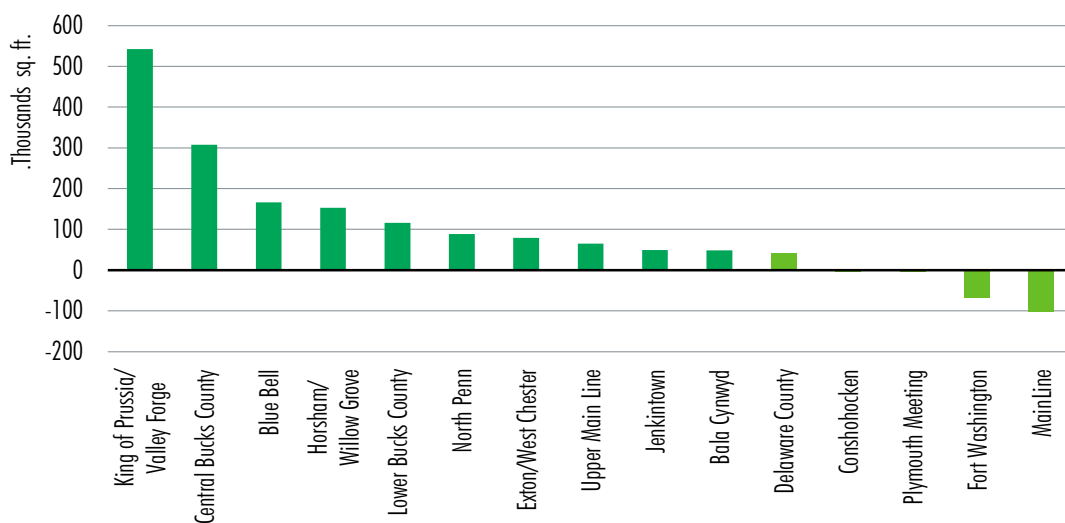
Source: CBRE Research, Q3 2017.

Figure 2 (cont.)

SUBMARKET	Number of Buildings	Inventory (Sq. ft.)	Total Vacancy Rate (%)	Total Availability Rate (%)	Under Construction (Sq. ft.)	2017 YTD Total Net Absorption (Sq. ft.)	Avg. Asking Lease Rate (\$Fsg/Psf/Yr)	Avg. Class A Asking Lease Rate (\$Fsg/Psf/Yr)
Burlington County	192	9,542,244	15.7%	18.6%	0	-130,445	\$19.71	\$23.38
Camden County	120	6,970,634	18.5%	20.6%	472,376	183,979	\$20.29	\$24.72
Gloucester County	24	467,492	18.3%	21.9%	0	-10,442	\$21.70	N/A
<b>Southern New Jersey Subtotal</b>	<b>336</b>	<b>16,980,370</b>	<b>16.9%</b>	<b>19.5%</b>	<b>472,376</b>	<b>43,091</b>	<b>\$20.02</b>	<b>\$23.85</b>
Wilmington CBD	37	6,824,639	19.4%	21.4%	0	262,961	\$24.45	\$26.29
New Castle Co. Suburbs	168	8,867,034	15.6%	18.0%	0	-78,364	\$22.76	\$23.79
<b>Northern Delaware Subtotal</b>	<b>205</b>	<b>15,691,673</b>	<b>17.3%</b>	<b>19.5%</b>	<b>0</b>	<b>184,597</b>	<b>\$23.75</b>	<b>\$25.33</b>
Lehigh Valley East	55	3,013,188	20.7%	21.9%	99,263	61,886	\$20.42	\$21.66
Lehigh Valley West	103	6,694,165	12.5%	16.1%	142,000	75,057	\$18.50	\$21.02
<b>Lehigh Valley Totals</b>	<b>158</b>	<b>9,707,353</b>	<b>15.0%</b>	<b>17.9%</b>	<b>241,263</b>	<b>136,943</b>	<b>\$19.88</b>	<b>\$21.11</b>
<b>TOTAL</b>	<b>1,807</b>	<b>146,601,260</b>	<b>14.4%</b>	<b>18.1%</b>	<b>2,931,639</b>	<b>1,667,889</b>	<b>\$25.42</b>	<b>\$28.68</b>

Source: CBRE Research, Q3 2017.

Figure 3: Suburban Philadelphia Office Year-to-Date Absorption



Source: CBRE Research, Q3 2017.

**OFFICE ABSORPTION**

New occupancy rose in Q3 by 726,722 sq. ft., bringing the YTD total up to 1,667,889 sq. ft. of positive net absorption. Downtown, occupancy continued to shrink on the heels of office densification trends, however the Suburbs saw consistent demand growth with the highest amount of space absorbed since 2005 at 935,538 sq. ft.. Recent reports, specifically by Bloomberg View, noted that millennials are starting to return to the suburbs because of better economic conditions along with development barriers in urban areas created by “not in my backyard” policies. YTD absorption totals in the suburbs of 1.5 million sq. ft. are already higher than 2016 totals, and comprise 89% of 2017 YTD totals within the region.

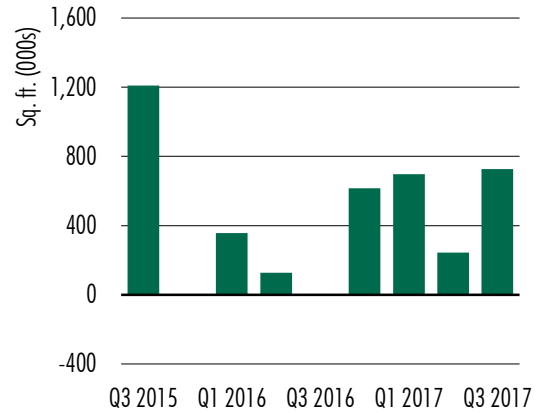
**OFFICE VACANCY**

The total vacancy rate in the region persisted downward 90 basis points to 14.4%. Vacancy within the CBD and Suburban markets combined was 13.6%, which is the lowest total vacancy rate seen since pre-recession levels in 2008. Corporate right-sizing and consolidations in the CBD was a continuing trend throughout the second half of 2017, as tenants found efficient use of space leading to lower real estate costs. Expect a drop in vacancy in the Suburban submarket in the short term, inversely related to a short-term rise in CBD rates. This should be a short-term trend as pricing should temper toward an equilibrium state.

**OFFICE DEVELOPMENT PIPELINE**

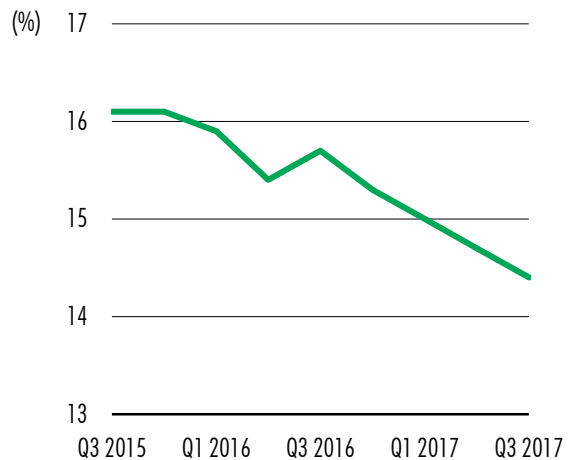
With the delivery of Highway to Health’s 110,550 sq. ft. build-to-suit in King of Prussia, along with Franklin Mint’s 71,000 sq. ft. project in Delaware County, new speculative developments in the Lehigh Valley and Fort Washington maintained a relatively stable construction total of 2.9 million sq. ft. Spring House Tech Park is a notable 69,000 sq. ft. office building in Fort Washington on a large expandable campus. This broke ground due to a limited supply of contiguous large blocks of Class A space within the Suburban submarket, and the persistent demand displayed in occupancy gains throughout the past year in traditionally “secondary” submarkets.

**Figure 4: Net Absorption**



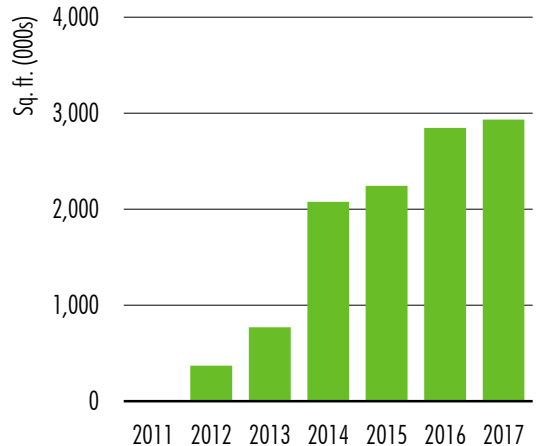
Source: CBRE Research, Q3 2017.

**Figure 5: Vacancy Rate**



Source: CBRE Research, Q3 2017.

**Figure 6: Development Pipeline**



Source: CBRE Research, Q3 2017.

**OFFICE LEASE RATES**

While rents in the greater Philadelphia area tempered during the third quarter, rents in the PA portion of the market continued their upward trend. At third quarter’s end, the average asking lease rate for that segment of the market sat at \$27.00. With vacancy sitting at its lowest point since 2008, lack of supply continued to push lease rates higher. Suburban Philadelphia saw a drop in lease rates for the first time this year as a result of demand taking down a significant amount of available Class A space, leaving lower-priced space on the market. Only 5 of the 15 suburban submarkets saw increases in lease rates. Downtown lease rates continued to climb. However, as vacancy climbs in the downtown market, lease rates are expected to fall from their record highs.

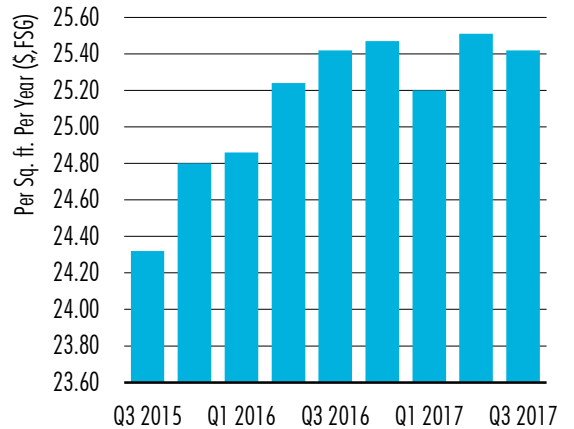
**OFFICE CAPITAL MARKETS**

Investment sales remained higher than historical 10-year averages on the heels of robust activity tallied during 2015 and 2016. In the third quarter, Centre Square traded to The Nightingale Group – following a lengthy sale process. This sale represented the largest asset to trade in Philadelphia history at over 1.7 million sq. ft. The suburban markets saw most of the market’s activity, as suburban office product continued to be popular among various investors as the suburbs are becoming less taboo in terms of demographic shifts. CBRE Research is tracking 26 assets that are currently for sale. Of those 26 assets – 21 are in suburban markets.

**PHILADELPHIA TROPHY OFFICE VACANCY**

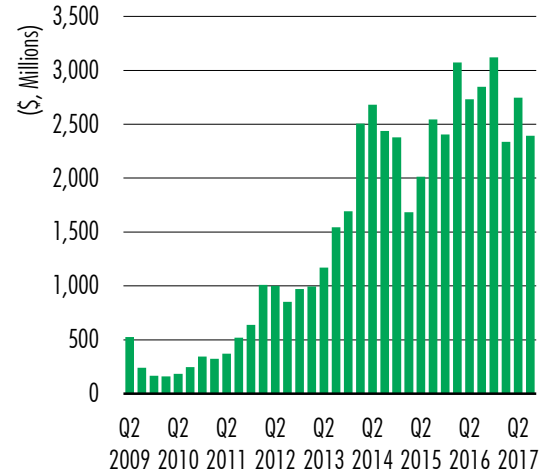
Trophy product across the Philadelphia region continued to outperform its class A competition. Trophy vacancy across the region sat at an ultra-low 6.3% - the third lowest figure on record. Trophy lease rates carry a premium of more than 18% above other Class A space, yet this has not proven to be a deterrent to users looking for high quality space. But, with trophy vacancy levels at historic lows, Class A, non-trophy product is expected to benefit by the lack of trophy options. Tenants looking for large blocks of high-end space may be hard pressed to find choices that meets their needs.

Figure 7: Office Lease Rates



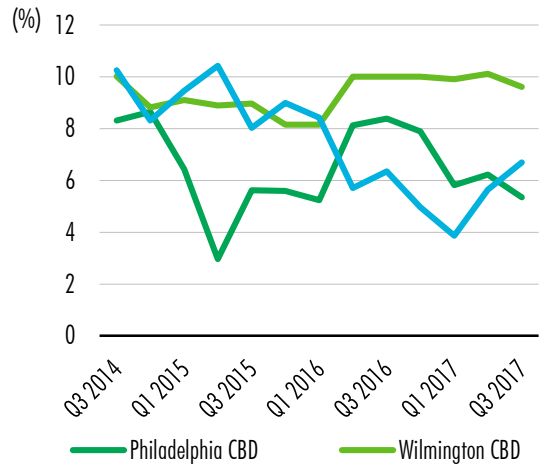
Source: CBRE Research, Q3 2017.

Figure 8: Office Sales Transactions

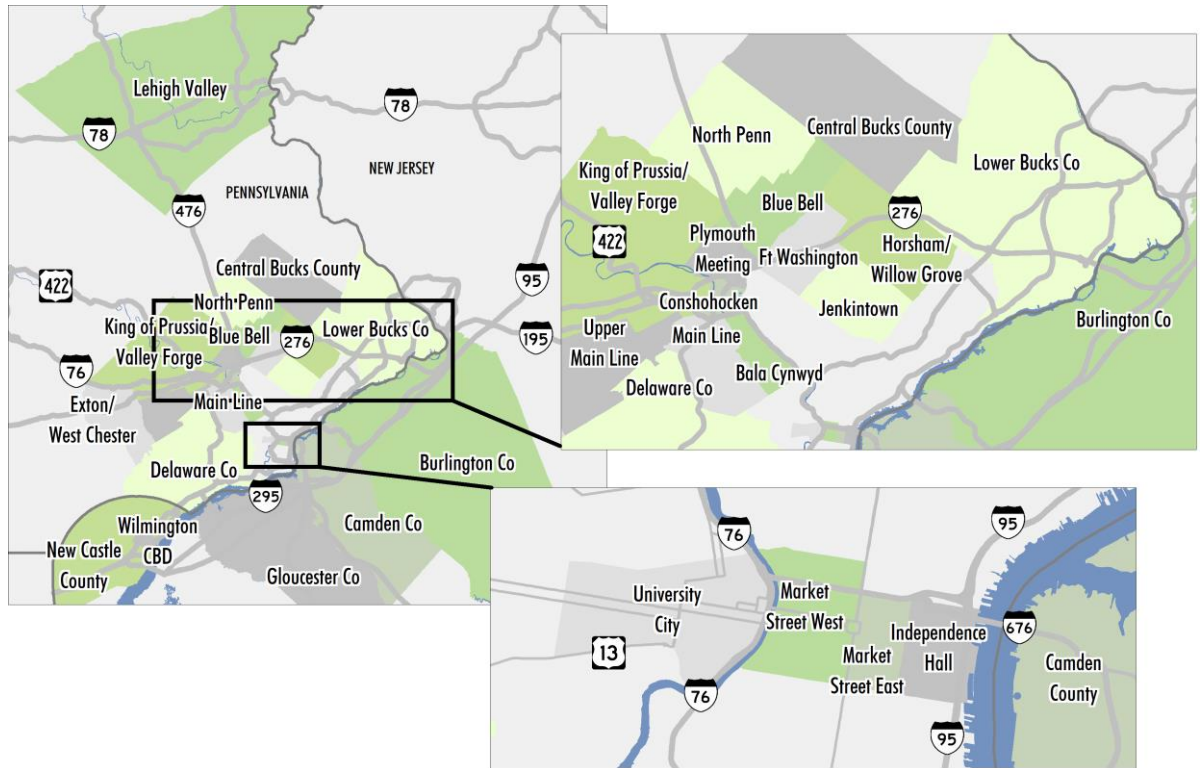


Source: Real Capital Analytics (4-qtr. Aggregate) Q2 2017.

Figure 9: Philadelphia Office Trophy Vacancy Rates



Source: CBRE Research, Q3 2017.



**CONTACTS**

**Ian Anderson**  
*Director of Research and Analysis*  
 +1 215 561 8997  
 ian.anderson2@cbre.com

**Joseph Gibson**  
*Research Operations Manager*  
 +1 610 727 5922  
 joseph.gibson@cbre.com

**Greg Dagit**  
*Researcher*  
 +1 610 251 5182  
 gregory.dagit@cbre.com

**Liam Fahey**  
*Researcher*  
 +1 215 561 8740  
 liam.fahey2@cbre.com

**LOCAL OFFICES**

**Center City Philadelphia**  
*Two Liberty Place*  
 +1 215 561 8900

**Allentown, PA**  
 +1 610 398 6900  
**Harrisburg, PA**  
 +1 717 540 2700

*Cira Center*  
 +1 215 921 7400

**Mt. Laurel, NJ**  
 +1 856 359 9500

**Wayne, PA**  
 +1 610 251 0820

**Wilmington, DE**  
 +1 302 661 6700

**Conshohocken, PA**  
 +1 610 834 8000

To learn more about CBRE Research, or to access additional research reports, please visit the Global Research Gateway at [www.cbre.com/researchgateway](http://www.cbre.com/researchgateway).