

# District of Columbia

## Office Market Cools After 18 Months of Strong Expansion



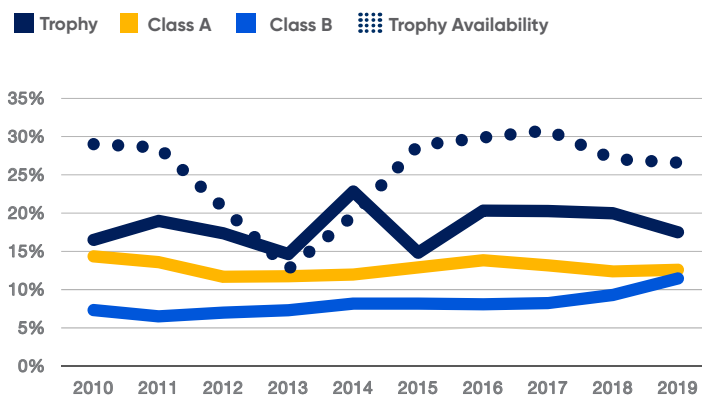
### Executive Summary

The District of Columbia's (DC) office market exhibited stability in the third quarter (Q3) of 2019. Though quarterly occupancy gains were muted, DC's office market has been active in 2019. Net absorption was 22,812 SF in Q3, bringing the year-to-date total to 1,062,203 SF. Occupancy growth has been partly supported by a robust construction pipeline, which has triggered several large-footprint relocations. New construction deliveries are also a contributing factor to DC's rising vacancy, which increased 60 basis points over the last three-months to 13.7%.

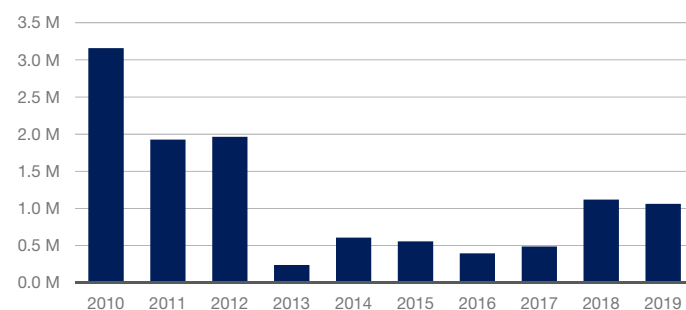
Public sector entities continue to drive much of the leasing activity in DC. Some of the largest public sector lease signings include: the U.S. Attorneys Office/US Marshals Service at 601 D Street, NW (309K SF), DC Department of Parks and Recreation at 1275 1st St, NE (103K SF), and the Department of Homeland Security at 650 Massachusetts Avenue, NW (64K SF).

Job growth rebounded marginally in the early summer, adding 6,000 new jobs over the last 12 months (+0.75%). While office-using job growth has been contracting recently, DC recorded 3,200 new office-using jobs over the last year, marking the largest gain since 2017. Private sector office employment is chiefly responsible for this expansion, as the federal government shed 1,200 DC-based office jobs over the same period.

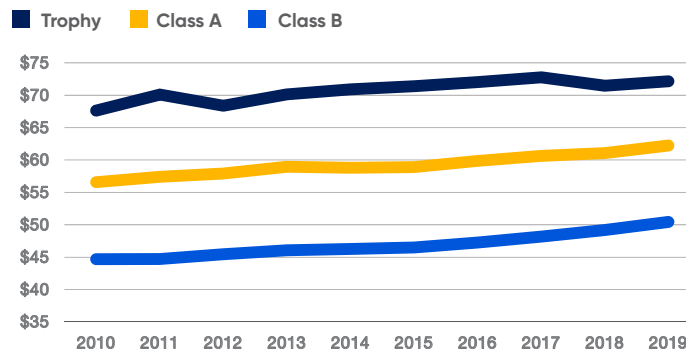
### Average Vacancy Rate



### Net Absorption



### Average Asking Rent



### Q3 Key Market Indicators

Total Vacancy	▲ 13.7%
Net Absorption	22,812 SF
Rental Rate	▲ \$57.99/SF
New Deliveries (YTD)	2,770,204 (2,044,759 SF net new)

## Rental Rates and Vacancy

Average asking rents continue to trend upward in 2019. Full-service direct rents rose by \$1.21 year-over-year (YoY) to \$57.99/SF. Trophy rents are accelerating at the fastest pace, appreciating by 3.9% over the last year to \$73.96/SF. Class A and B rates increased to \$62.05/SF (+\$0.90 YoY) and \$50.53/SF (+\$0.99 YoY), respectively. While most Class A space is concentrated in downtown, newly-developing submarkets, such as NoMa, Southwest, and Capitol Riverfront, boast average Class A asking rates below \$55/SF.

Quarterly vacancy rose to 13.7% in Q3, which marks a 150 basis point (bps) rise over year-ago levels. While occupancy gains have been strong over the last 18 months, new construction has added a substantial amount of new inventory to the market, effectively offsetting occupancy gains. Trophy, Class A and Class B vacancy was recorded at 17.5% (-650 bps), 13.4% (+80 bps), and 13.5% (+290 bps), respectively. Of the five office developments to deliver in the East End in 2019, roughly 475,000 SF remain vacant in Q3. These five projects have added 100 bps to East End's vacancy and 36 bps to DC's overall vacancy.

## Supply and Demand

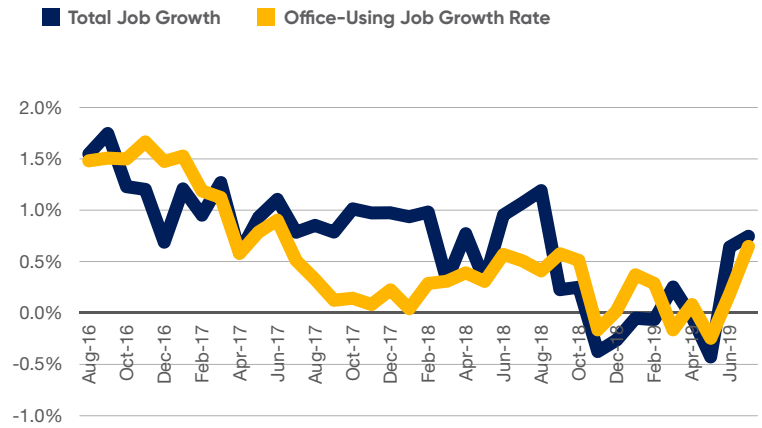
Quarterly net absorption was recorded at 22,812 SF, which brings the year-to-date total to 1,062,203 SF. DC has registered meaningfully positive occupancy gains for the last two years, partly supported by large-footprint relocation to newly-constructed buildings. Total leasing activity has been down in 2019, and has fallen short of 2 million SF in every quarter this year. From 2013 to 2018, DC failed to reach 2 million SF of quarterly leasing activity only three times. Slow tenant demand cannot be attributed to one particular industry, however DC's largest tenant groups (federal government and law firms) are exhibiting exceptionally low leasing activity. If weak demand continues into 2020, DC's office market will further soften, causing greater concern among landlords. With 1.5 million SF still in the construction pipeline however, the opportunity for a leasing rebound is present.

Although the District is in a period of steady occupancy expansion, DC still possesses a significant oversupply of office space relative to demand. Total office availability is at an all-time high (27.3 million SF) and concerns are exacerbated by below-average leasing activity, construction deliveries and the threat of federal consolidations.

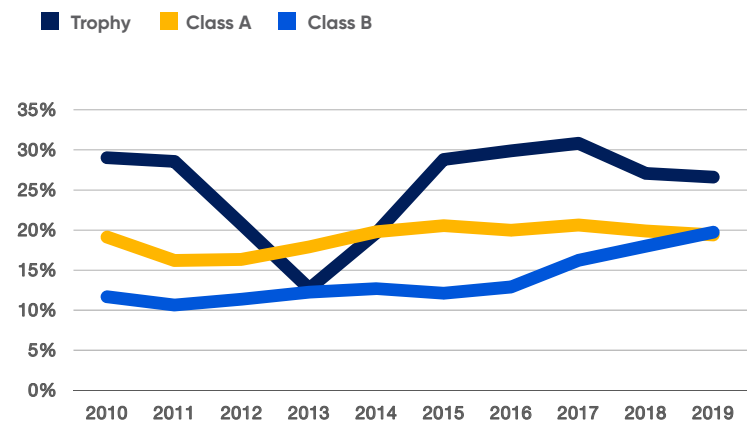
## Market Outlook

Despite the recent boost in occupancy, Cresa expects the District of Columbia to remain tenant-favorable through 2021. There is a considerable amount of optimism regarding the economic impacts of Amazon's HQ2, however the magnitude and timing of this economic driver will remain unknown in the near-term. Aggressive construction activity through 2020 will add to DC's existing inventory and further exacerbate its supply/demand imbalance. Though DC boasts upward-trending rents, landlord concession packages remain generous, resulting in significantly reduced effective rents. Average landlord concessions for new leases are expected to include tenant improvement allowances of at least \$100/SF and around 1.2 months of free rent per year of term.

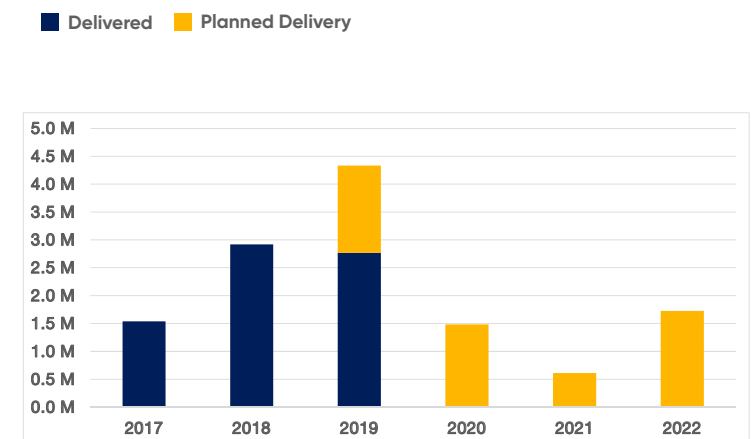
## Annualized Employment Growth by Month



## Availability Rate by Class



## Construction Schedule





### Q3 Top Leases

Tenant	Submarket	Address	Size	Type
GSA - Offices of the US Attorneys and US Marshals	East End	601 D St, NW	309,000 SF	New Lease
EAB	West End	2445 M St, NW	148,338 SF	New Lease
D.C. Department of Parks and Recreation	NoMA	1275 1st St, NE	103,495 SF	New Lease
GSA - Department of Homeland Security	East End	650 Massachusetts Ave, NW	64,976 SF	Renewal

### Q3 Top Sales

Building	Submarket	Size	Price	Price (PSF)	Buyer	Seller
1625 Eye Street, NW	CBD	386,686 SF	\$259,000,000	\$669.79	American Real Estate Partners	EDGE Funds Advisors
815 Connecticut Avenue, NW	CBD	216,786 SF	\$231,250,000	\$1,066.72	Ponte Gadea USA, Inc.	The Blackstone Group
325 7th Street, NW	East End	173,915 SF	\$154,500,000	\$888.37	Artemis Real Estate Partners	Paramount Group
1275 1st Street, NE	NoMA	338,645 SF	\$141,771,984	\$418.64	Boyd Watterson Asset Management	Walton Street Capital/Stonebridge

### Submarket Statistics

Submarket	Total Bldgs	Inventory	Sublet Available	Total Available	Total Vacant	Vacancy Rate	Net Absorption (Q3 2019)	Net Absorption (YTD)	Class A Rent	Class B Rent	Total Direct Rent	Under Constr.	SF Delivered YTD	Net New SF Delivered
CBD	205	35,842,484	1,017,317	7,882,349	4,869,262	▲ 13.6%	(104,935)	(5,002)	\$71.57	\$50.25	▲ \$59.17	1,866,399	357,500	199,706
East End	216	47,200,629	1,176,923	10,643,766	7,537,959	▲ 16.0%	(303,085)	396,942	\$66.19	\$51.53	▲ \$61.20	394,229	1,266,997	664,346
Downtown Core	421	83,043,113	2,194,240	18,526,115	12,407,221	▲ 14.9%	(408,020)	391,940	\$67.75	\$50.76	▲ \$60.34	2,260,628	1,624,497	864,052
Capitol Hill	35	4,898,911	45,974	1,940,303	709,488	▼ 14.5%	(11,949)	(40,394)	\$65.00	\$48.95	▼ \$63.27	1,083,252	408,157	408,157
Capitol Riverfront	12	2,736,635	27,911	688,103	306,509	▼ 11.2%	35,509	(24,069)	\$55.90	N/A	▲ \$55.90	357,948	-	-
Georgetown	38	2,986,915	83,593	636,588	383,551	▲ 12.8%	16,391	(136,712)	\$50.47	\$43.73	▼ \$47.77	-	-	-
NoMa	33	9,974,515	42,311	1,099,891	838,026	▼ 8.4%	40,898	537,522	\$50.29	\$44.38	▼ \$50.52	581,652	522,550	552,550
Southwest	35	12,004,153	54,849	1,832,524	1,133,906	▼ 9.4%	55,741	159,767	\$50.54	\$46.14	▲ \$48.70	729,703	215,000	220,000
Uptown	119	7,073,685	214,464	1,596,068	1,073,572	▲ 15.2%	113,998	194,388	\$52.85	\$46.08	▲ \$47.29	371,606	-	-
West End	23	3,377,500	183,361	789,403	389,484	▲ 11.5%	180,244	(20,239)	\$57.73	\$43.14	▲ \$53.66	-	-	-
District of Columbia	716	126,095,427	2,846,703	27,108,995	17,241,757	▲ 13.7%	22,812	1,062,203	\$63.81	\$50.53	▲ \$57.99	5,384,789	2,770,204	2,044,759

\*Availability refers to all marketed office spaces. In addition to vacant space, availability also includes marketed spaces which are currently occupied and spaces still under construction but are available for pre-leasing.

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