CommercialEdge

National Office Report

February 2023

Distressed Activity to Pick Up in 2023

- In the years since the pandemic unsettled the office market, many have been anticipating a wave of distressed offices. While distressed activity has been few and far between to this point, conditions may lead to a significant uptick in 2023.

- Some of the factors that have kept distressed activity muted are no longer applicable. Long lease terms for office space mean firms that embraced remote and hybrid work have allowed offices to sit empty while waiting for their leases to expire. Cheap money allowed many owners to kick the can down the road, hoping that pre-pandemic office utilization would return, but it seems increasingly unlikely that will happen.

- The converging forces of a higher cost of debt, weak demand, falling prices and a potential recession could lead to an increase in distressed activity this year. Higher interest rates have already put pressure on owners with floating-rate debt and will provide a substantial challenge for loans that need to be refinanced in 2023. Remote and hybrid work have become entrenched, and the tech industry that drove much of the leasing of office space in recent years is now in a contraction. Weak demand is leading to falling prices for office. The national average sale price of an office property fell from $269 per square foot in the first quarter of 2022 to $214 per foot in the fourth quarter. A flood of distressed office activity could trigger a downward price spiral for offices.

- Properties with low occupancy, expiring leases and maturing loans will be most likely to face distress. A tenant flight-to-quality has been taking place since the pandemic, with firms decreasing the size of their footprints but increasing the quality of the space they lease. This puts older assets, especially those that are not well located and have not been well maintained, at high risk of distress, as well. Yet even trophy towers are not exempt, with Brookfield defaulting on $784 million in loans for two office towers in downtown Los Angeles.

- We anticipate that distressed activity will increase in frequency this year, but it is too early to say it will be a large wave. With demand for office space continuing to be soft, we expect that many of the distressed properties that are sold may be targeted for conversions into life sciences or multifamily, with some razed and entirely redeveloped.

Listing Rates and Vacancy: Remote Work Drives Up Vacancies in Denver

- The average full-service equivalent listing rate was $38.04 in January, an increase of 1.1% over the previous 12 months.
- The national vacancy rate was 16.6%, up 80 basis points over January 2022.
- Vacancy rates continue to climb in most markets, but some places have seen rates rise more rapidly than others since the pandemic upended the office market. Denver's vacancy rate in January sat at 18.3%, up 200 basis points over the previous 12 months and 370 bps over the previous two years. The main driver of increasing vacancy rates in the Mile High City is remote work. According to the Census Bureau's American Community Survey, 28% of respondents in the market reported working from home, one of the highest shares in the country. Additionally, Denver had benefited from robust growth in the tech sector in recent years, and the layoffs currently hitting that industry will hamper the market. Denver's sublease rate is 1.8%, a figure that could move upward in the future.

Listings by Metro

Market	Jan-23 Listing Rate	12-Month Change	Total Vacancy	12-Month Change	Top Listing	Price Per Square Foot
National	$38.04	1.1%	16.6%	80 bps		
Orlando	$24.74	12.2%	16.0%	-120 bps	Celebration Medical Center	$42.40
Seattle	$38.49	10.4%	18.5%	150 bps	1208 Eastlake Avenue East	$89.50
Philadelphia	$31.42	8.1%	14.1%	-40 bps	Two Liberty Place	$53.50
San Diego	$43.83	8.0%	14.1%	30 bps	One La Jolla Center	$69.00
San Francisco	$67.43	8.0%	18.8%	290 bps	Sand Hill Collection - The Quad	$171.60
Charlotte	$34.05	6.9%	13.2%	-150 bps	Rotunda Building, The	$44.42
Miami	$47.24	5.7%	11.7%	-180 bps	830 Brickell	$137.50
Atlanta	$30.38	4.4%	20.0%	-170 bps	Star Metals Offices	$58.00
Nashville	$31.68	4.3%	18.0%	-70 bps	Three Thirty Three	$44.38
Chicago	$27.80	3.8%	19.4%	0 bps	300 North LaSalle Drive	$59.46
Portland	$30.91	3.5%	17.3%	320 bps	M Financial Plaza	$47.40
Phoenix	$27.63	2.8%	17.0%	210 bps	Camelback Collective	$52.50
Bay Area	$57.06	2.4%	17.9%	150 bps	325 Lytton Avenue	$160.20
Manhattan	$75.74	0.9%	15.4%	260 bps	550 Madison Avenue	$210.00
Los Angeles	$42.65	0.8%	14.7%	100 bps	1999 Avenue of the Stars	$96.90
Twin Cities	$25.85	-0.5%	15.1%	50 bps	Tractor Works Building, The	$39.71
Denver	$29.87	-1.1%	18.3%	200 bps	1144 Fifteenth Street	$62.08
Houston	$29.54	-1.1%	26.0%	160 bps	Texas Tower	$58.40
New Jersey	$32.63	-1.4%	17.1%	-10 bps	Newport Tower	$54.80
Washington DC	$40.53	-1.7%	13.8%	-280 bps	601 Pennsylvania Ave NW - North Building	$79.00
Tampa	$28.11	-2.5%	16.3%	-50 bps	Water Street Tampa - Thousand & One	$58.00
Dallas	$28.18	-2.8%	17.9%	40 bps	Rosewood Court	$60.43
Austin	$41.33	-4.4%	19.1%	280 bps	Indeed Tower	$76.67
Boston	$36.34	-4.9%	9.5%	-120 bps	Kendall Square at MIT - 314 Main Street	$121.60
Brooklyn	$40.76	-17.9%	19.7%	210 bps	200 Kent Avenue	$75.00

Source: CommercialEdge. Data as of January 2023. Listing rates are full-service or "full-service equivalent" rates for spaces available as of report period. National listing rate is an average of the top 50 markets.

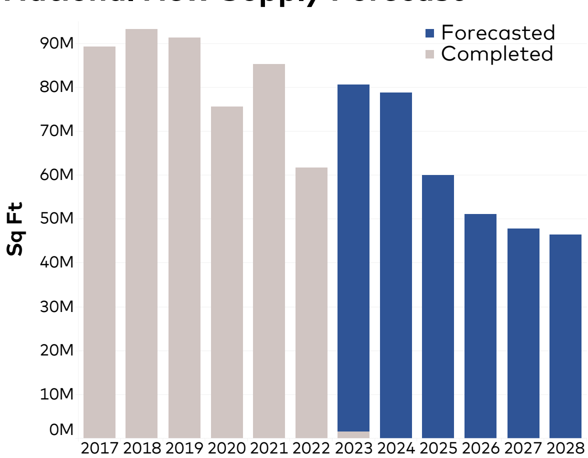
Supply:
Dallas Growth Fuels Office Development

- Nationally, there are 123.6 million square feet of office space currently under construction.

- The top five markets by total square footage—Boston, Manhattan, Dallas, Austin and San Francisco—account for more than a quarter of all new supply being built.

- An influx of people have moved into Texas in recent years, helping prop up office markets that have been hit by remote work. In Dallas, vacancy rates have been resilient, only increasing 40 basis points over the last year despite the many headwinds the office sector faces. The steadiness of the office market in Dallas has let developers remain active in the market, with 4.1 million square feet started last year and more on the way. The Fields—a 180-acre, $2 billion mixed-use project in Frisco—will eventually include 4 million square feet of office space to go alongside retail, restaurants, apartments and hotels. Large, master-planned mixed-use projects are popular in the market. Dallas Cowboys owner Jerry Jones' firm Blue Star Land is adding three properties, including the 15-story TIAA Tower in The Star, a mixed-use development that also houses the Cowboys' headquarters and training facilities.

National New Supply Forecast



Source: Yardi Matrix. Data as of January 2023
Data in this chart includes owner-occupied properties

Supply Pipeline (by metro)

Market	Under Construction	Under Construction % Stock	Plus Planned % Stock
National	123,622,986	1.9%	6.2%
Austin	6,697,054	7.6%	25.2%
Boston	12,920,197	5.4%	11.1%
Nashville	3,010,813	5.3%	14.7%
Charlotte	3,878,122	5.2%	15.1%
San Diego	4,620,289	5.0%	9.4%
Seattle	6,458,919	4.7%	20.1%
Brooklyn	1,533,841	4.3%	7.4%
San Francisco	6,503,662	4.2%	12.7%
Miami	2,211,526	3.1%	8.1%
Bay Area	5,803,088	2.9%	16.6%
Dallas	7,390,945	2.7%	9.5%
Orlando	1,471,104	2.7%	6.7%
Atlanta	4,474,488	2.3%	5.9%
Manhattan	9,919,815	2.2%	4.5%
Denver	2,949,092	1.9%	4.9%
Houston	3,910,276	1.7%	3.3%
Philadelphia	2,481,066	1.4%	5.3%
Washington DC	5,020,174	1.3%	3.6%
Portland	681,714	1.2%	6.5%
Chicago	2,699,779	0.9%	6.5%
Los Angeles	2,556,369	0.9%	3.7%
New Jersey	1,502,870	0.8%	2.2%
Phoenix	834,356	0.6%	5.3%
Twin Cities	676,369	0.6%	2.6%
Tampa	382,099	0.6%	4.3%

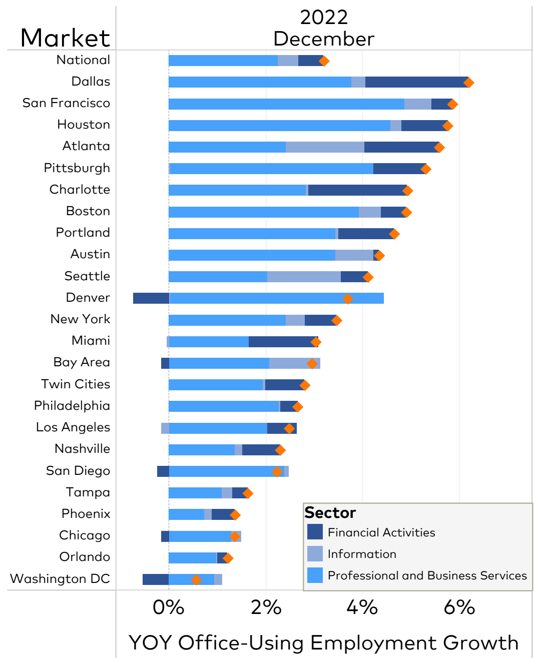
Source: CommercialEdge. Data as of January 2023

Office-Using Employment:
Washington, DC, Struggles to Add Jobs

- Office-using sectors of the labor market grew 3.1% year-over-year in January, with professional and business services adding 82,000 workers in the month, financial activities adding 6,000 and information losing 5,000, according to the Bureau of Labor Statistics.,

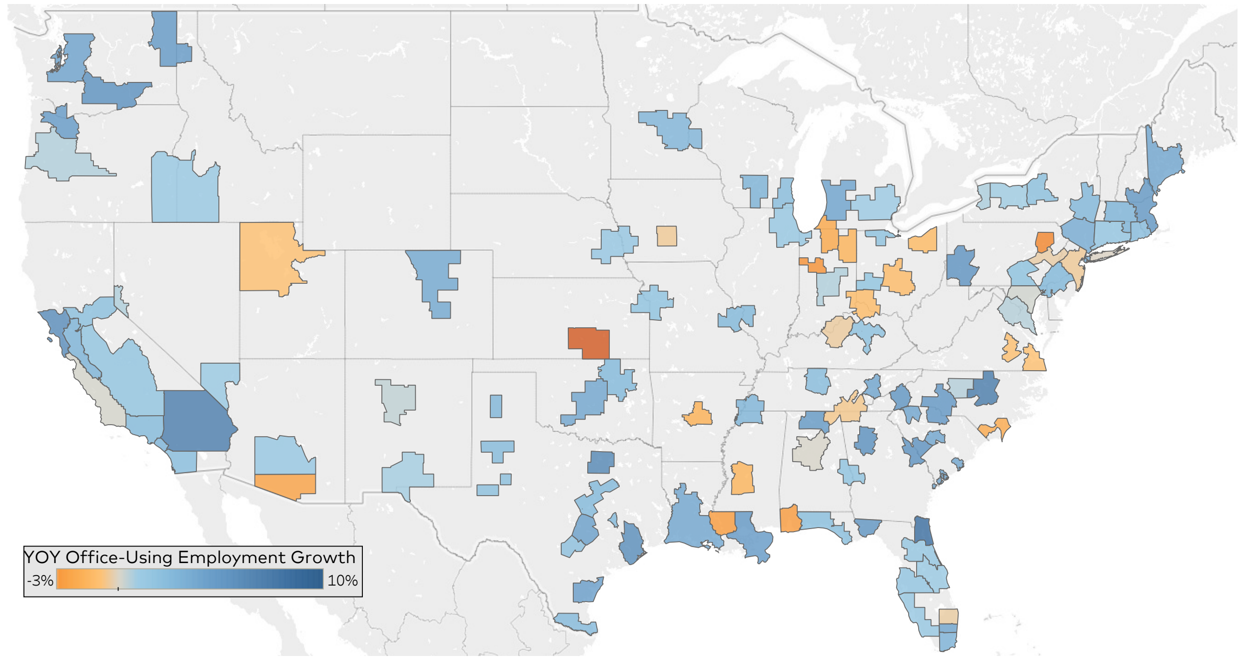
- In the nation's capital, office-using employment growth is sluggish. Metro employment data for December, which trails the national release, showed Washington, D.C., growing at just 0.4% year-over-year, the lowest rate of growth among the top 25 markets covered by CommercialEdge. Yet slow growth in the traditional office-using sectors only paints a partial picture of the struggles in D.C.'s office market. Unlike other markets, in D.C. much of the office employment is government workers, and BLS data shows employment in the federal government sector falling by 3.5% in 2022. Further compounding issues for the market, the federal government has embraced remote and hybrid work, seeing it as a competitive advantage in a tight labor market.

Growth by Sector



Sources: Bureau of Labor Statistics and Moody's Analytics

Office-Using Employment Growth



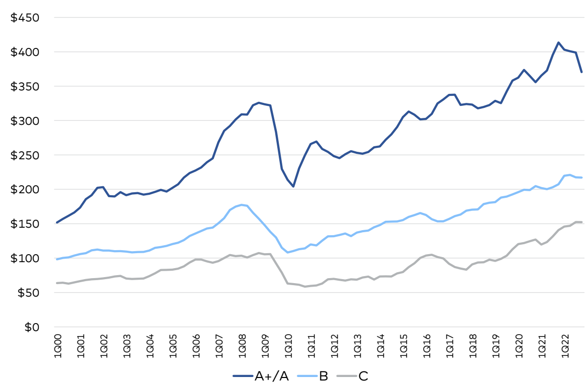
Sources: Bureau of Labor Statistics and Moody's Analytics

Transactions:
Muted Sales Volume This Year

- CommercialEdge has recorded $1.9 billion of office transactions so far this year, with properties trading at $202 per square foot.

- Due to the interest rate environment, economic uncertainty and remote work, we anticipate that there will not be much capital for office transactions this year. Investors may still be able to find loans for well-located buildings with strong occupancy and cash-flow, but for the most part deals for office buildings will fail to materialize. We expect that office transaction volume in 2023 will be at its lowest level since the years following the Great Financial Crisis.

Asset Class (price per sq. ft.)



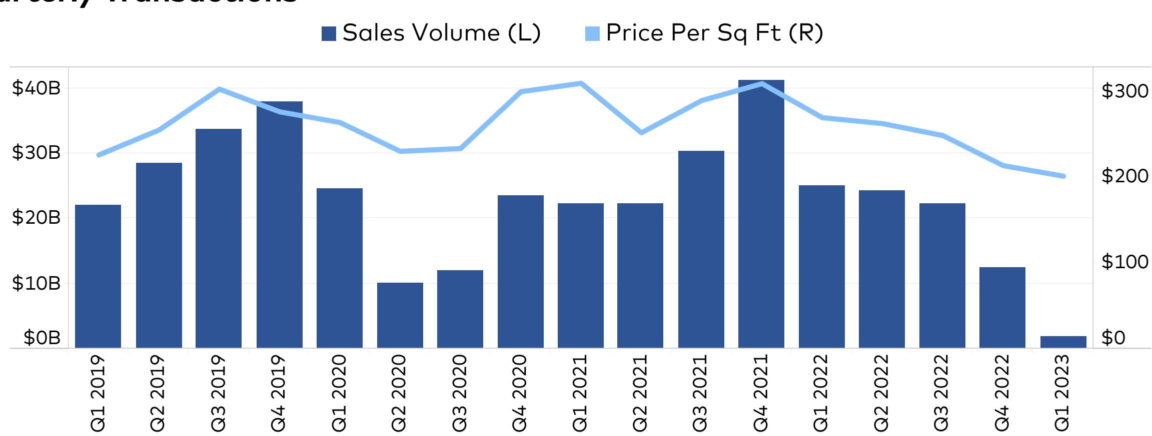
Source: CommercialEdge; 12-month moving average.
Does not include unpublished and portfolio transactions.

Sales Activity

Market	YTD Sales Price PSF	YTD Sales (Mil, as of 1/31)
National	$202	$1,928
Houston	$184	$324
Miami	$549	$316
Atlanta	$197	$248
New Jersey	$128	$96
Los Angeles	$264	$86
Washington DC	$489	$78
San Francisco	$843	$73
Philadelphia	$108	$69
Phoenix	$207	$57
Boston	$1,054	$56
Dallas	$162	$54
Tampa	$90	$40
Chicago	$28	$22
Twin Cities	$203	$22
Bay Area	$538	$17
Seattle	$234	$11
Charlotte	$109	$6
Austin	$328	$4
San Diego	$0	$0
Denver	$0	$0
Orlando	$0	$0
Portland	$0	$0
Manhattan	$0	$0
Brooklyn	$0	$0
Nashville	$0	$0

Source: CommercialEdge. Data as of January 2023. Sales data for unpublished and portfolio transactions are estimated using sales comps.

Quarterly Transactions



Source: CommercialEdge. Data as of January 2023

Definitions

This report covers office buildings 25,000 square feet and above. CommercialEdge subscribers have access to more than 14,000,000 property records and 300,000 listings for a continually growing list of markets.

CommercialEdge collects listing rate and occupancy data using proprietary methods.

- *Listing Rates*—Listing Rates are full-service rates or "full-service equivalent" for spaces that were available as of the report period. CommercialEdge uses aggregated and anonymized expense data to create full-service equivalent rates from triple-net and modified gross listings. Expense data is available to CommercialEdge subscribers. National average listing rate is for the top 50 markets covered by CommercialEdge.
- *Vacancy*—The total square feet vacant in a market, including subleases, divided by the total square feet of office space in that market. Owner-occupied buildings are not included in vacancy calculations.

A and A+/Trophy buildings have been combined for reporting purposes.

Stage of the supply pipeline:

- *Planned*—Buildings that are currently in the process of acquiring zoning approval and permits but have not yet begun construction.
- *Under Construction*—Buildings for which construction and excavation has begun.

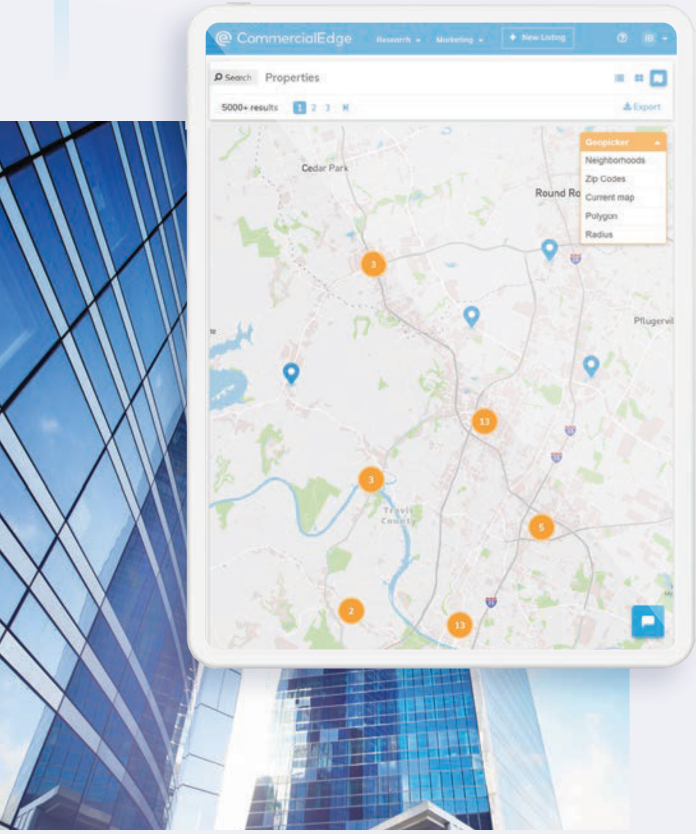
Office-Using Employment is defined by the Bureau of Labor Statistics as including the sectors Information, Financial Activities, and Professional and Business Services. Employment numbers are representative of the Metropolitan Statistical Area and do not necessarily align exactly with CommercialEdge market boundaries.

Sales volume and price-per-square-foot calculations for portfolio transactions or those with unpublished dollar values are estimated using sales comps based on similar sales in the market and submarket, use type, location and asset ratings, sale date and property size.

CommercialEdge

Reliable commercial real estate data, built up over more than a decade of extensive research. Powered by Yardi.

CommercialEdge provides the office segment's most comprehensive market intelligence service and listing management platform, sustaining data-driven decisions.



Key features:

- Continually growing nationwide coverage with 162 markets currently included
- Researched and verified data, powered by a team of 400 experienced property research specialists
- Exhaustive property reports featuring data points such as ownership, leases, sales, debt, taxes and more
- Building and portfolio performance overview with current average rents, vacancy rates and maturing leases
- Extensively researched tenant data with an accuracy rate two to three times higher than the industry average
- Real-time market trends based on actual transactional and leasing data with Yardi Market Insight
- Dedicated tools, including automated competitive building sets, broker tour books and dedicated property webpages
- Access to the CommercialEdge Listing Network — including CommercialCafe, PropertyShark, Point2 and CommercialSearch

Capitalize on comprehensive commercial real estate research
Nationwide property and listing data all in one place, specifically engineered for CRE professionals.

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