1Q24

District of Columbia Office Market Overview

Market Observations

Economy

– The region's labor market remains strong amid shifting macroeconomic conditions. February's 2.7% unemployment rate remains significantly lower than the region's ten-year historical average of 4.1%. 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 Education & Health and Government sectors, posting gains of 2.8% and 2.6%, respectively. The office-occupying industries of Information, 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 decline in employment over the past year, jobs in the office-using sectors remain at a level that is 1.1% higher than four years ago—just prior to the pandemic—and 5.3% higher than the pandemic-induced employment trough in April 2020.

Major Transactions

– Office investment sales continue to lag in pricing per square foot as well as total transaction volume. However, owner-user sales and conversion opportunities are propping up a lot of demand in Washington, D.C. capital markets.

– The largest sale of the quarter was the portfolio sale of Market Square within the East End, sold by a joint venture between Blackstone Inc and PIMCO to a partnership between PRP Real Estate Investment and Morning Calm Management. The two office buildings, totaling 707,000 SF, sold for $323 million, or $456.55 PSF. The East Tower, located at 701 Pennsylvania Avenue, totals 348,000 SF, while the West Tower, located at 801 Pennsylvania Avenue, totals 359,000 SF. The overall occupancy was 79% at the time of sale.

Leasing Market Fundamentals

– The District of Columbia experienced 81,000 SF of negative net absorption during Q1 2024. This led to the vacancy rate increasing slightly, ending Q1 2024 at 20.3%, up 10 basis points quarter-over-quarter and 140 basis points year-over-year.

– The District of Columbia's development pipeline remains historically low, with no deliveries during Q1 2024 and only two properties under construction totaling 736,000 SF. 17XM is a 336,000-square-foot office building under construction in the CBD and 600 Fifth is a 400,000-square-foot office building under construction in the East End.

– Overall, asking rents dipped slightly to begin 2024. Class A rents were the cause of this, as they decreased 3.4% quarter-over-quarter, while Class B rents increased 0.4% quarter-over-quarter. The longer-term trend, however, shows that both Class A and Class B rents have remained relatively flat since 2019.

Outlook

– A strong and resilient labor market, coupled with persistent inflationary concerns, is contributing to an uncertain macroeconomic outlook in the near-term.

– Rents continue to experience modest decline, having seen consistent downward pressure since 2021. Lack of supply-side pressure may ease this pressure going forward and keep rents elevated.

– Fewer landlords have capital for concessions, which have been a major driver in attracting tenants and capturing net positive absorption over the past several years. The pool of landlords that can perform, or pay for tenant improvement, is shrinking. There are fewer owners offering trophy office supply, fostering an unusual landlord-favorable environment for the most quality space. Meanwhile, conditions continue to soften in class B and C assets.

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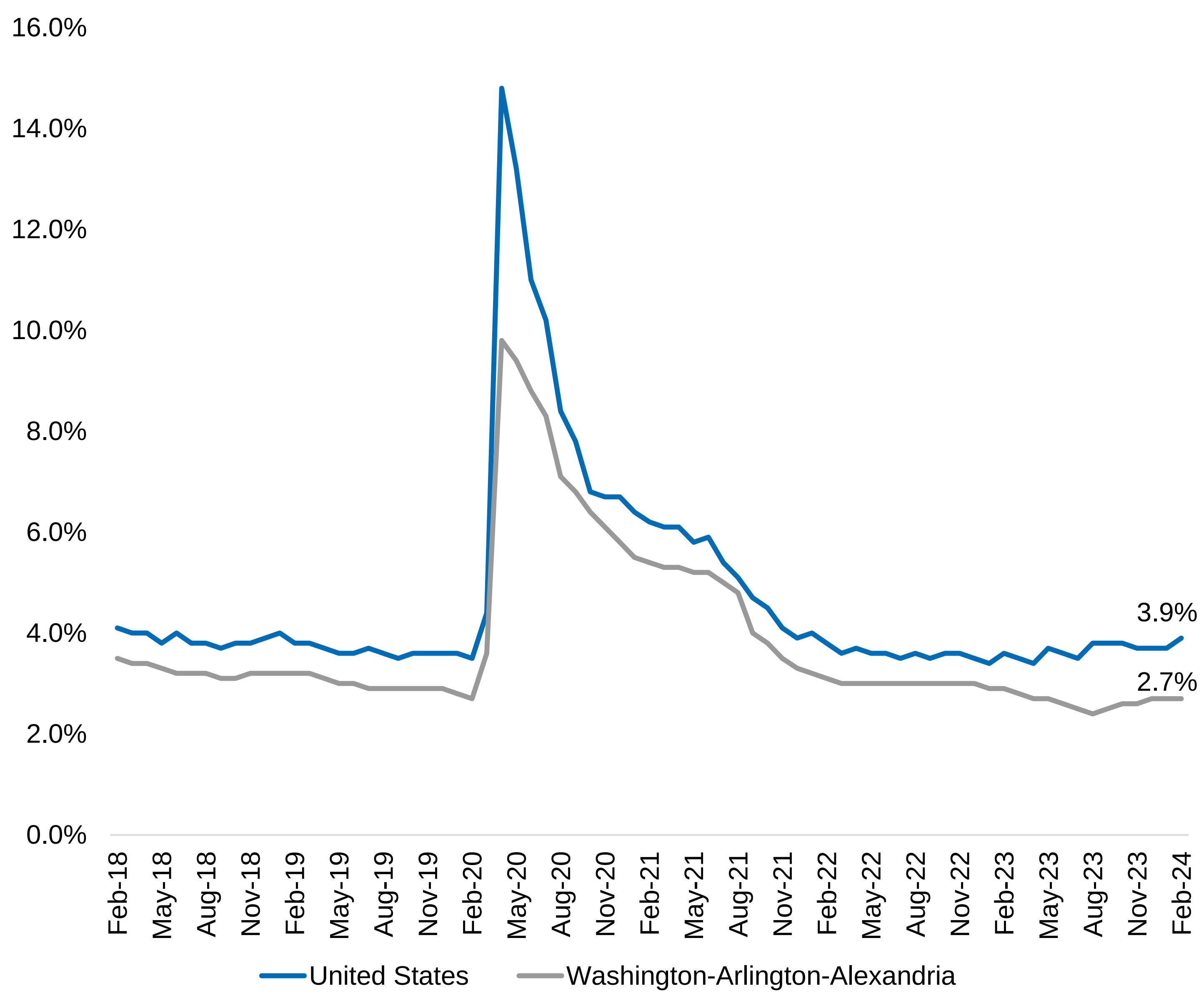
Economy

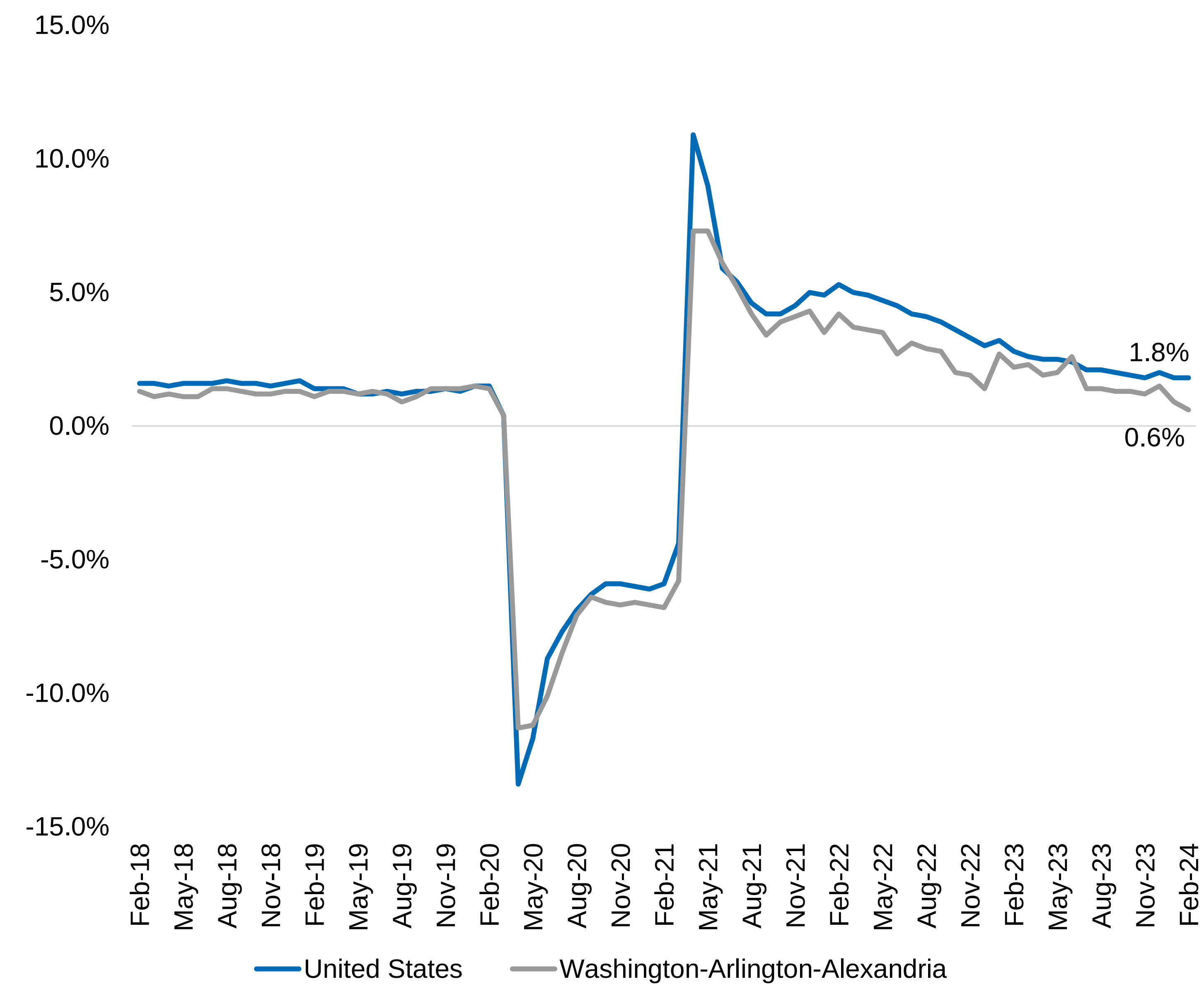
Metro Employment Job Growth Remains Positive Despite Slowing

The region's labor market is very tight, with unemployment 120 basis points below the national average. Job growth has begun to slow, but nonetheless remains positive.

Unemployment Rate, Seasonally Adjusted



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

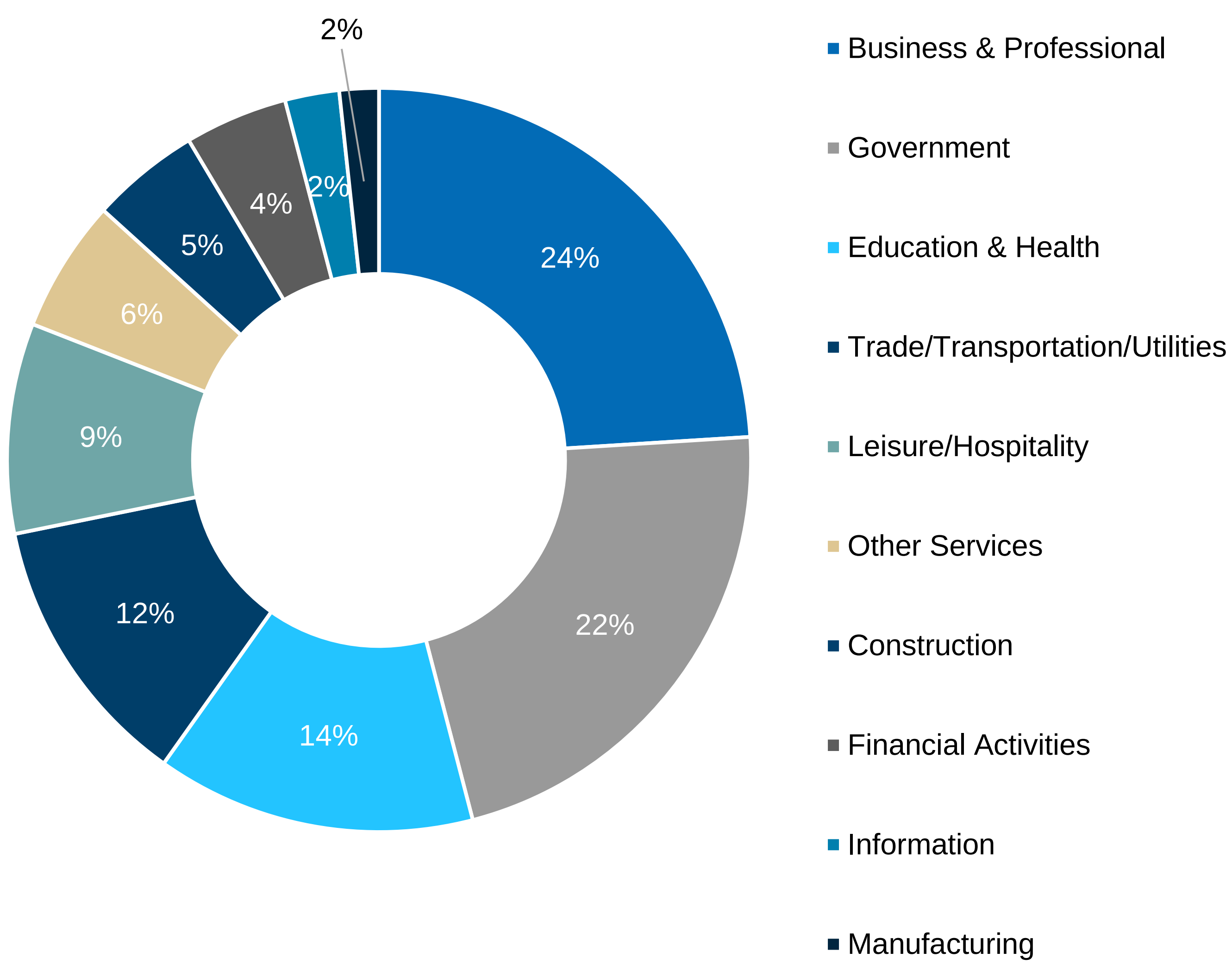


Source: U.S. Bureau of Labor Statistics, Washington-Arlington-Alexandria

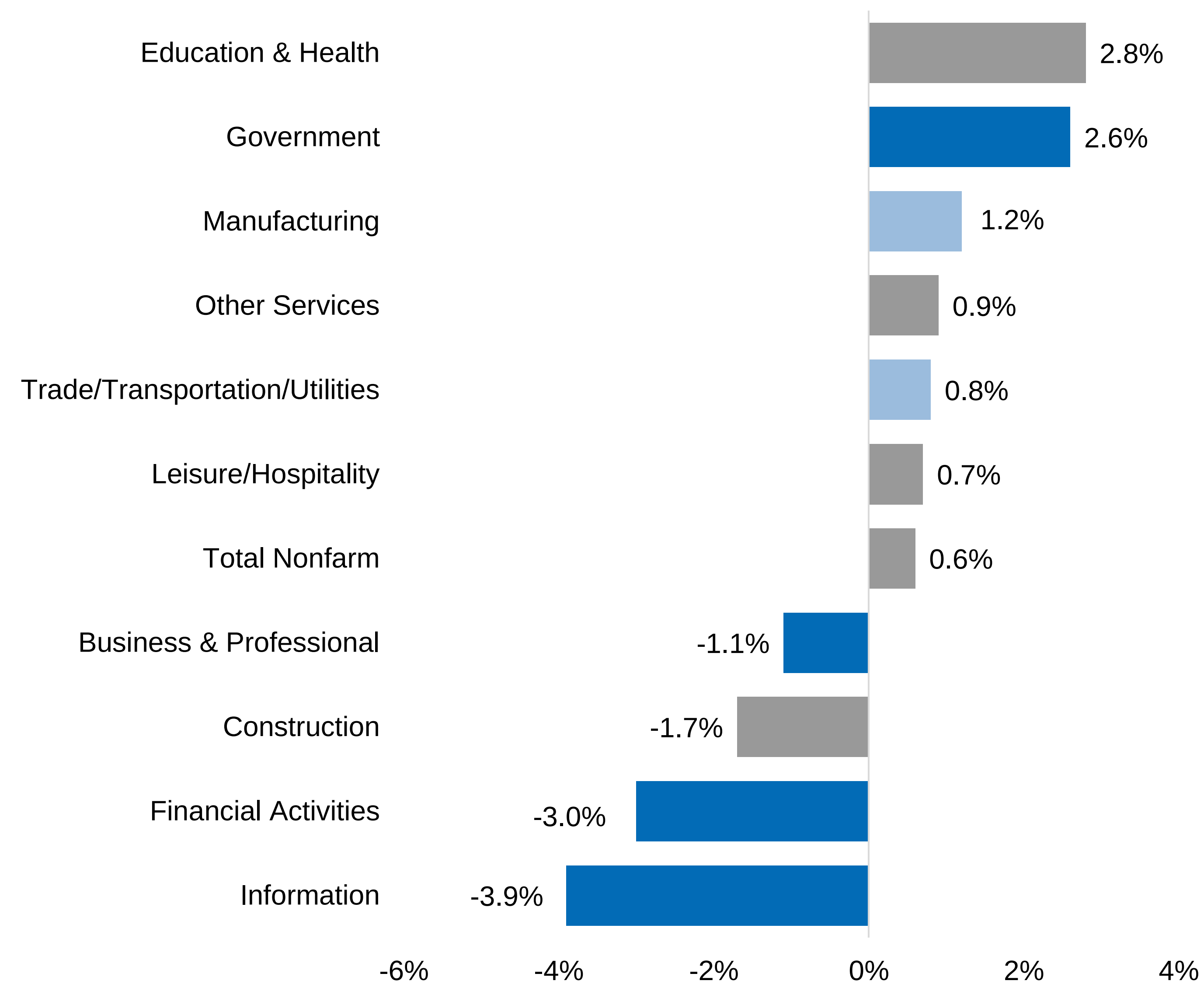
Job Growth Driven in Large Part by Education, Health, and Government

Education, Health, and Government propped up job growth in the region, leading to total nonfarm employment growth of 0.6%. Despite this, office-occupying industries of Information, Financial Activities, and Professional and Business Services experienced some job losses over the past year, contributing to declining demand for office space.

Employment by Industry, February 2024



Employment Growth by Industry, 12-Month % Change, February 2024

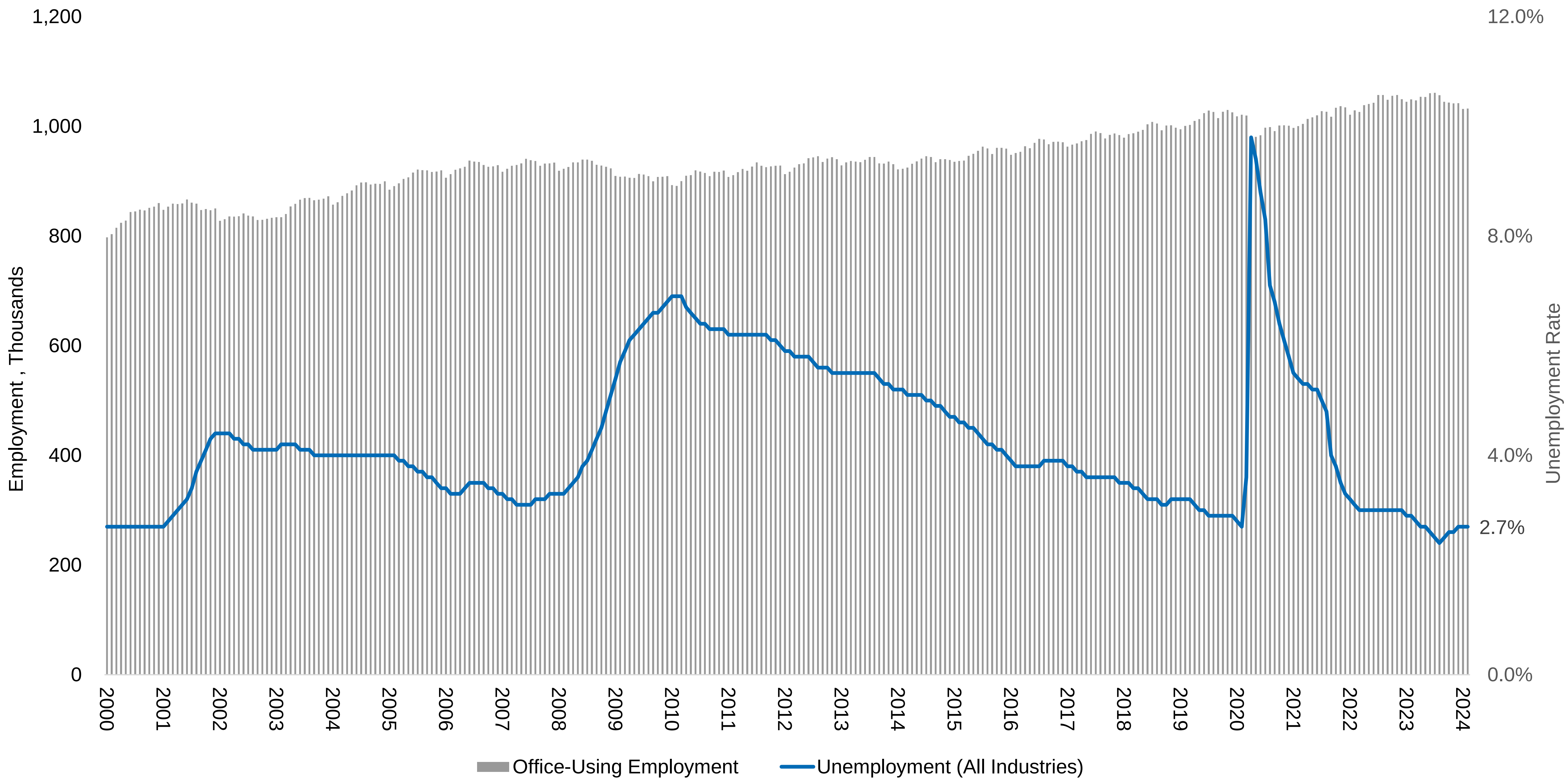


Source: U.S. Bureau of Labor Statistics, Washington-Arlington-Alexandria

Overall Office-Using Employment Has Rebounded

The number of office jobs has rebounded and now exceeds pre-pandemic levels. Office-using jobs in the region are currently 1.1% higher than four years ago—just before the pandemic—and 5.3% 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: February 2024 data is preliminary.
*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.

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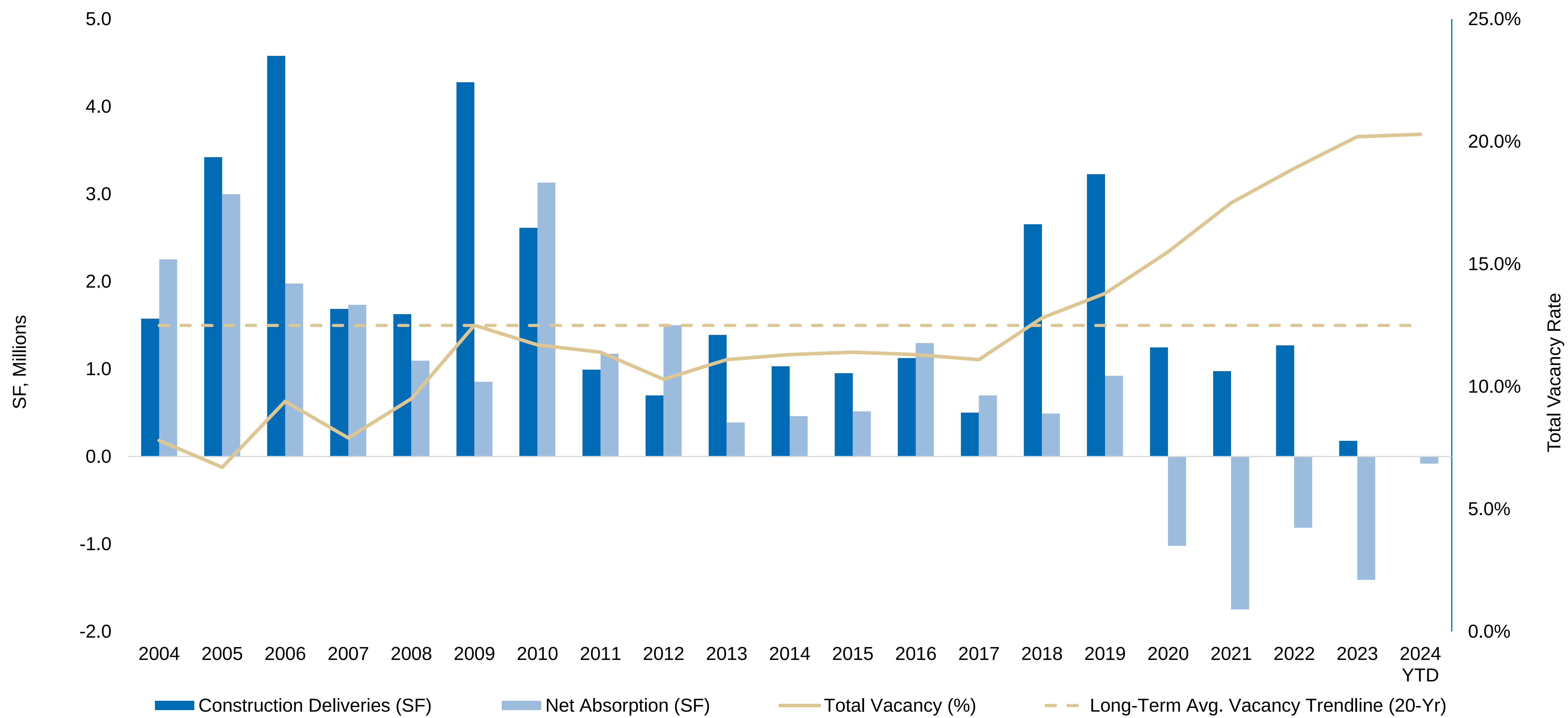
Leasing Market Fundamentals

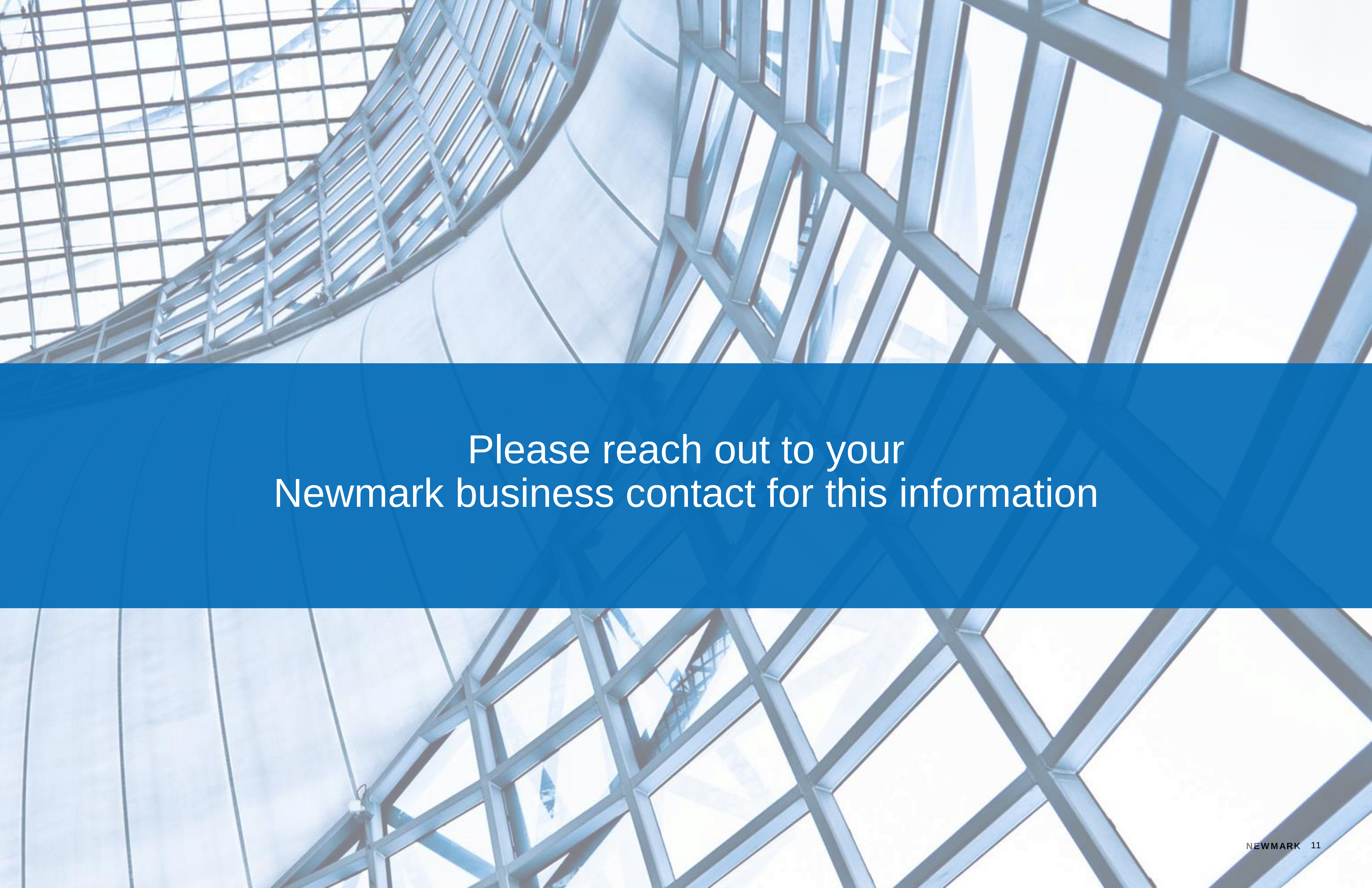
Vacancy Remains Relatively Flat to Begin 2024

The District of Columbia's vacancy rate rose 10 basis points over the quarter to end Q1 2024 at 20.3%. The market did not have a delivery during the quarter, a market that has averaged 1.8 million square feet of annual deliveries over the past 20 years. This slowdown in office deliveries and 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



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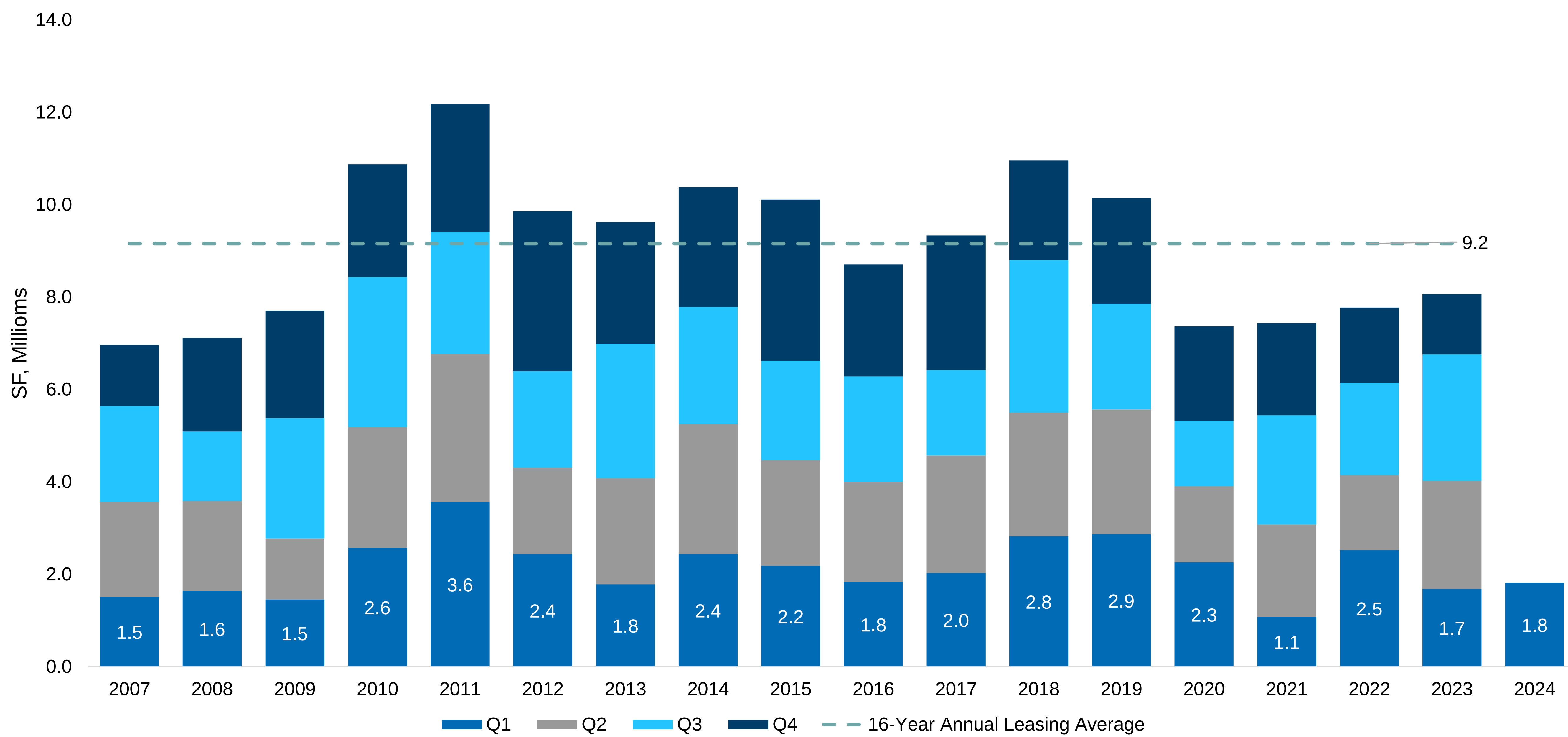
Leasing Activity Has Slowed

Leasing activity has slowed since 2020, although it picked up the pace slightly during 2023. During Q1 2024, the market saw 1.8 MSF of leasing activity, slightly higher than the same period in 2023. The market will look to accelerate leasing activity throughout 2024 with hopes of returning to normalcy and ending the year closer to the historical annual average of 9.2 MSF of annual leasing activity.

Total Leasing Activity (msf)

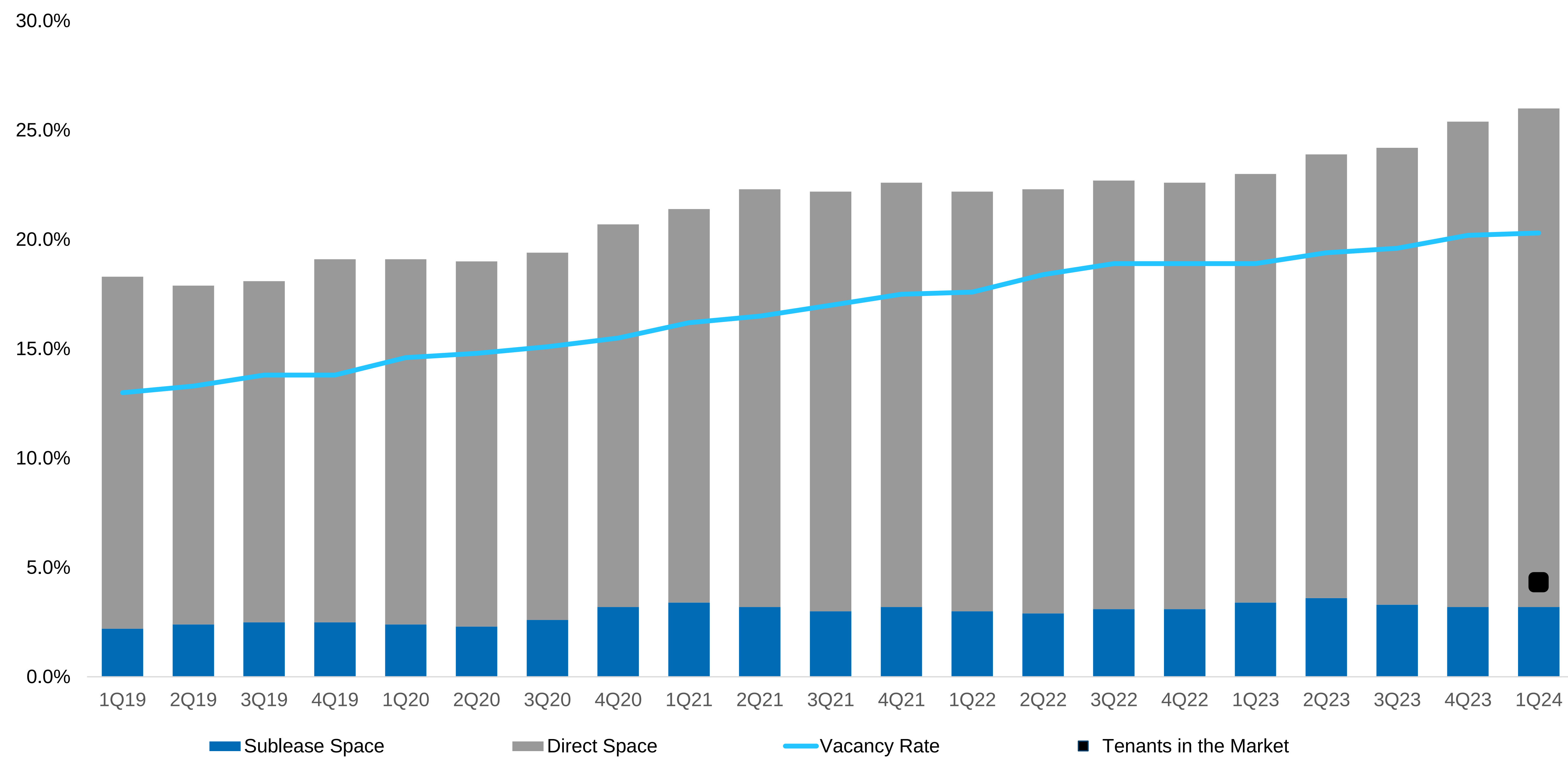


Source: Newmark Research, CoStar

Availability Continues to Increase While Tenant Demand Drops

Available office space sits near historical highs, both in terms of direct and sublease space. Over the past five years, the direct availability rate has averaged 18.6% while the sublease availability rate has averaged 2.9%. The Q1 2024 availability rates of 22.8% for direct space and 3.2% for sublease space are well above the long-term average.

Available Space and Tenant Demand as Percent of Overall Market

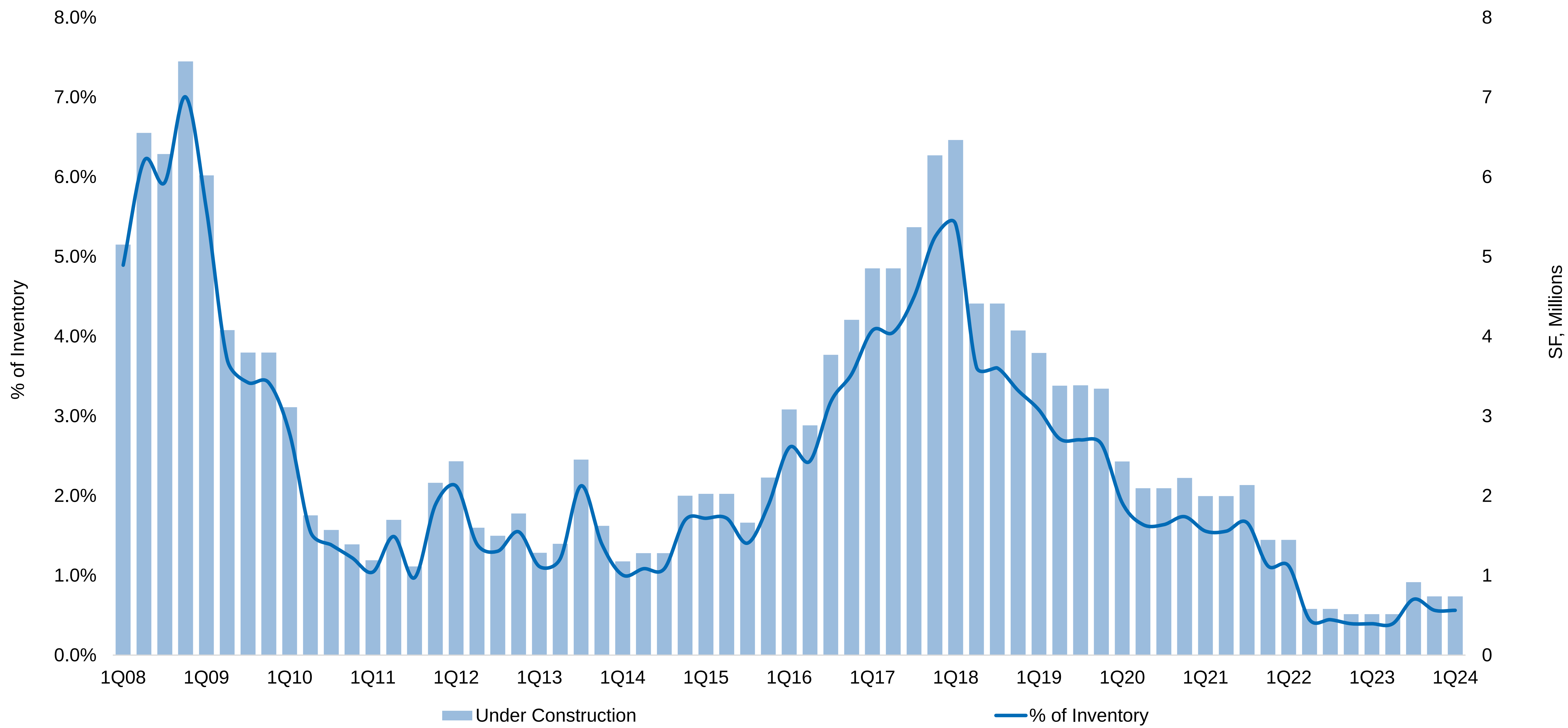


Source: Newmark Research

Slowing Office Construction Pipeline Will Help Ease Rising Vacancy

The District of Columbia's development pipeline remains historically low, with no deliveries in Q1 2024. There are two projects under construction totaling 736,000 SF. 17XM is a 336,000-square-foot office building located in the CBD. It has an expected delivery of Q2 2024 and is 57% preleased. 600 Fifth is a 400,000-square-foot office building located in the East End. It has an expected delivery of Q1 2026 and is 54% preleased. With demand continuing to moderate, limited new supply and strong preleasing will help ease rising vacancy.

Office Under Construction and % of Inventory

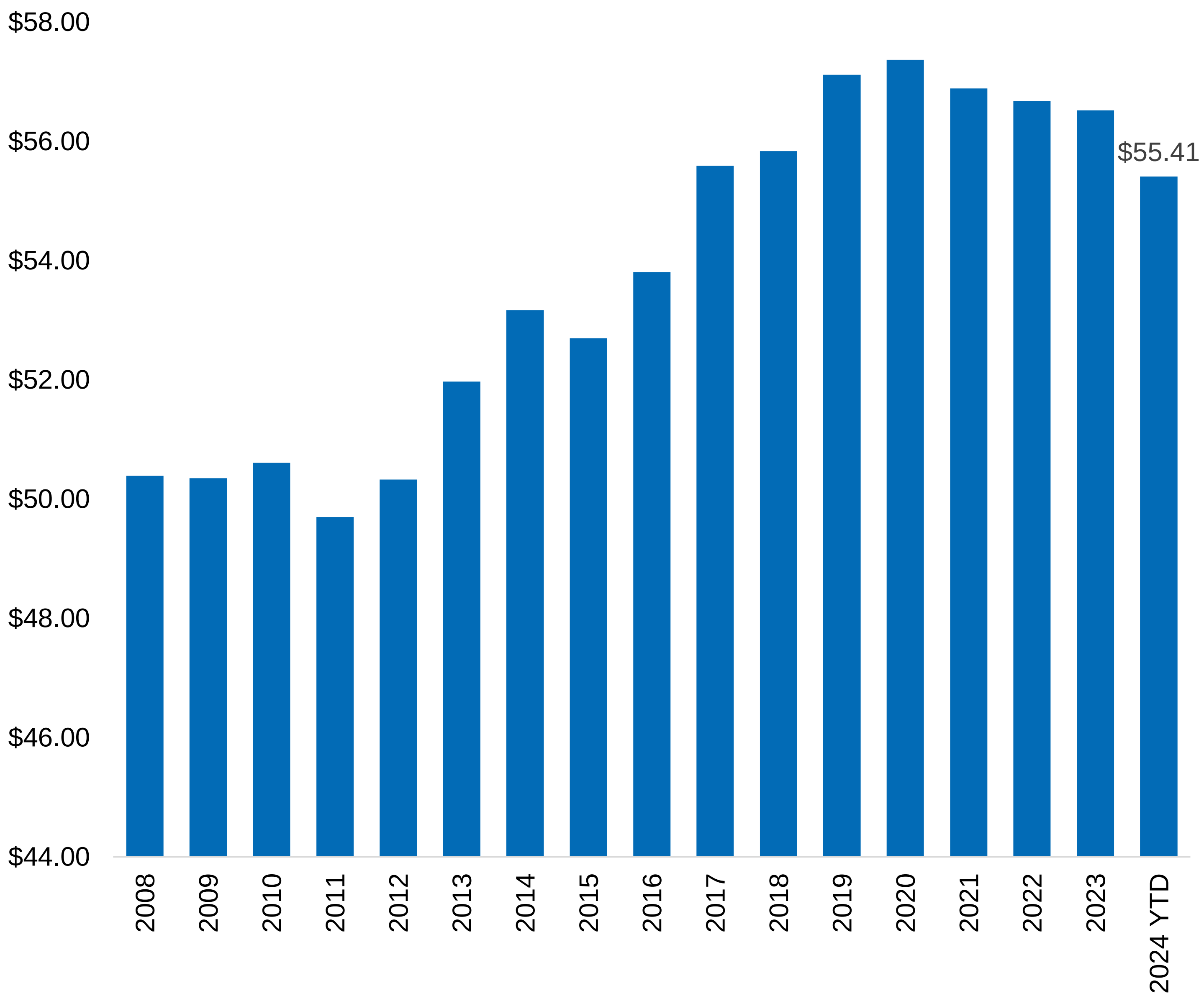


Source: Newmark Research, CoStar

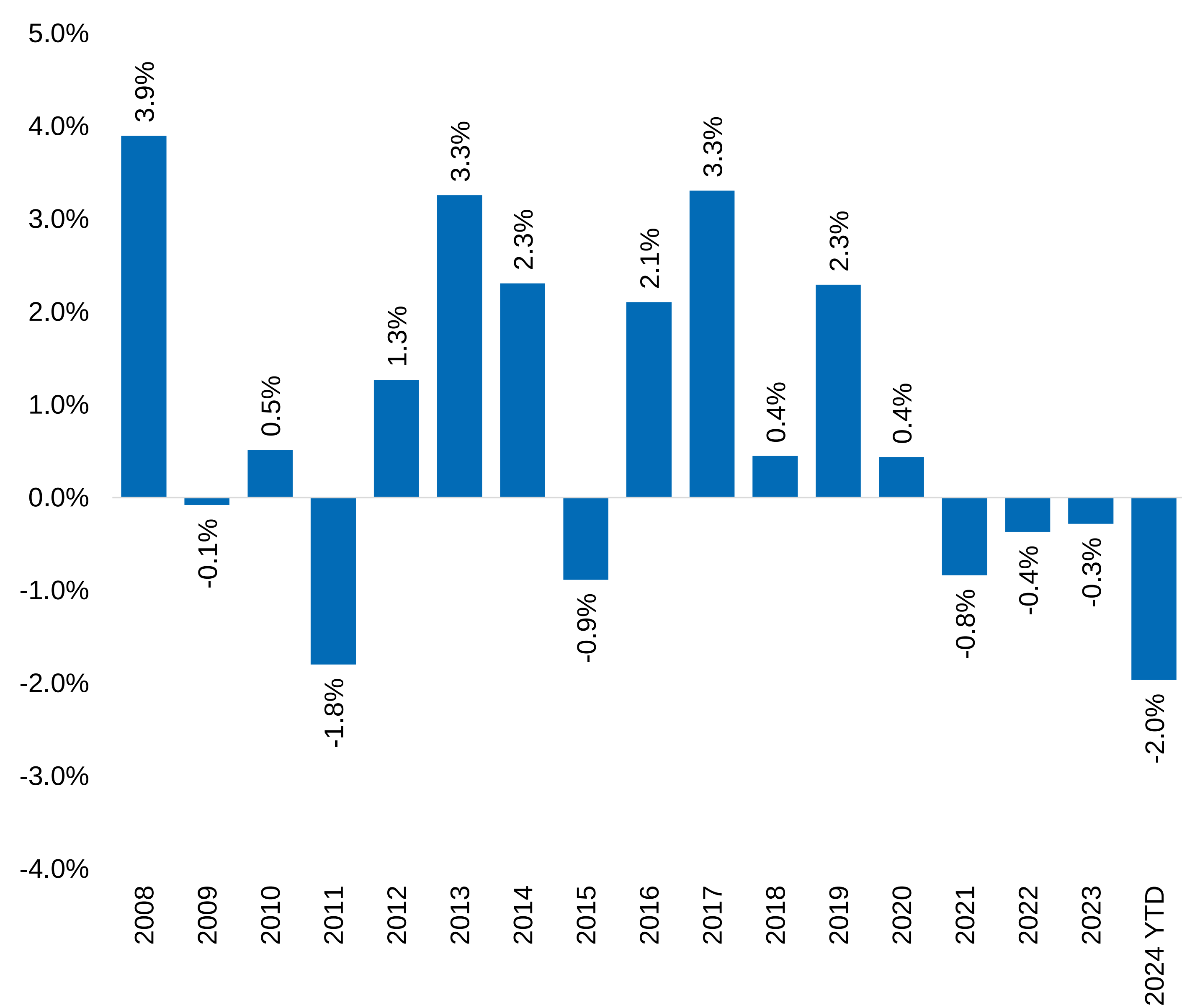
District of Columbia Asking Rents Experiencing Modest Decline

Asking rental rates have been decreasing year-over-year since 2021. The District of Columbia has not experienced sustained annual losses in asking rents since the Global Financial Crisis, but even then, it took two years for rates to noticeably drop in 2011. Continued limited demand—and in some cases, a lack of capital for concessions—has placed downward pressure on asking rents in the District.

Office Average Asking Rent, $/SF, FS



Year-over-Year Asking Rent Growth Rate

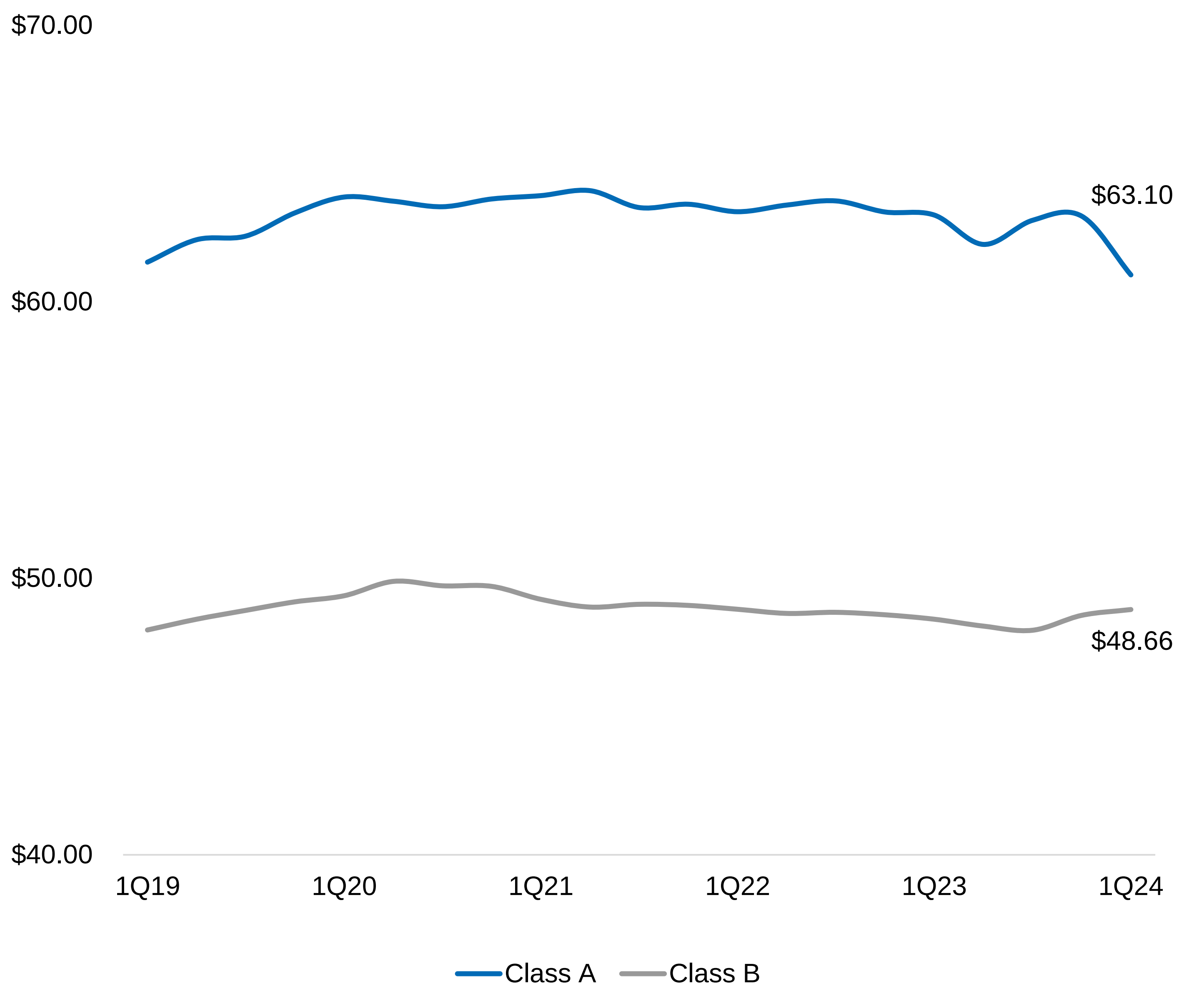


Source: Newmark Research, CoStar

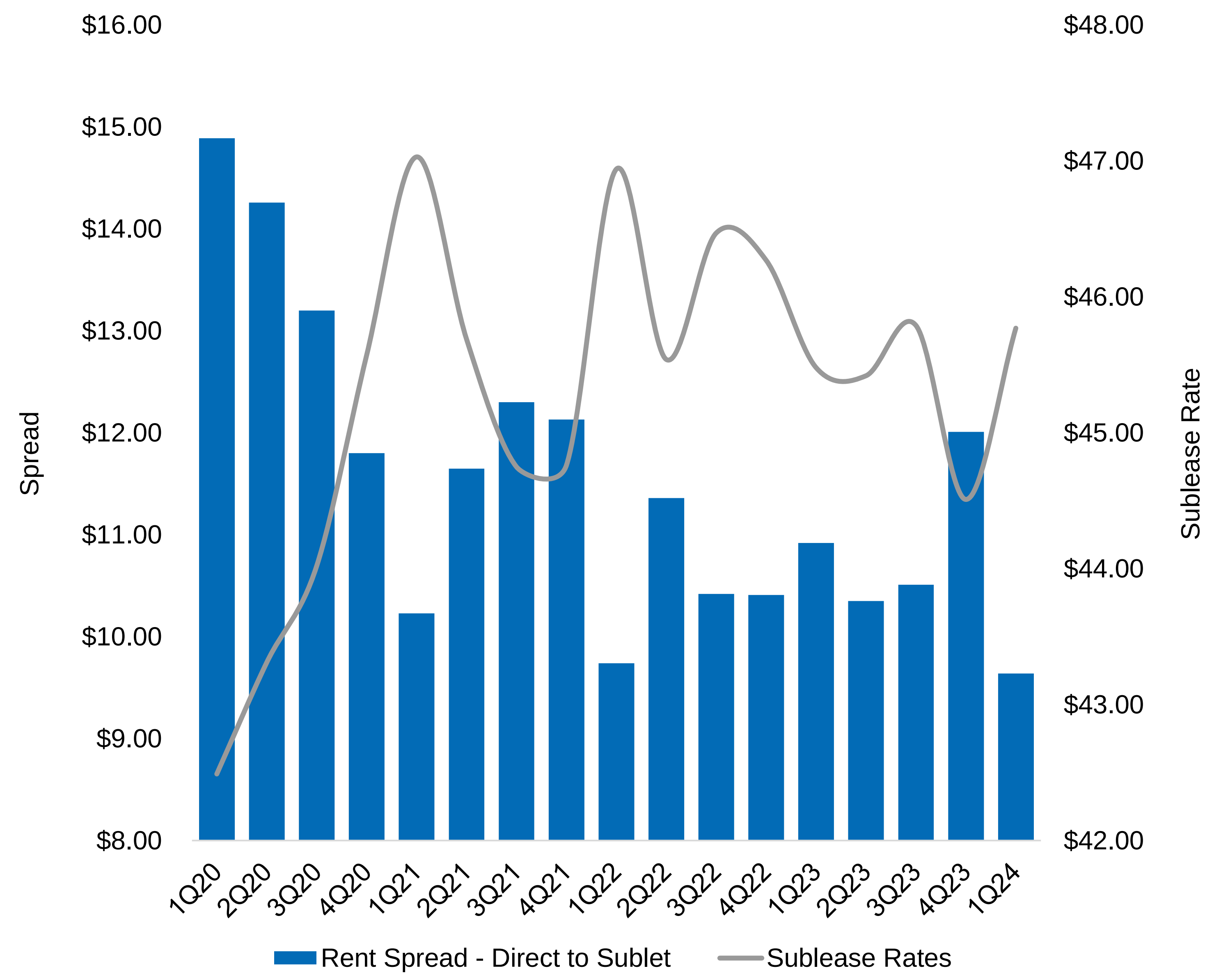
Asking Rents Dip Slightly to Begin 2024

Overall, asking rents dipped slightly to begin 2024. Class A rents were the cause of this, as they decreased 3.4% quarter-over-quarter, while Class B rents increased 0.4% quarter-over-quarter. The longer-term trend, however, shows that both Class A and Class B rents have remained relatively flat since 2019.

Class A and Class B Asking Rents



Sublease Rates

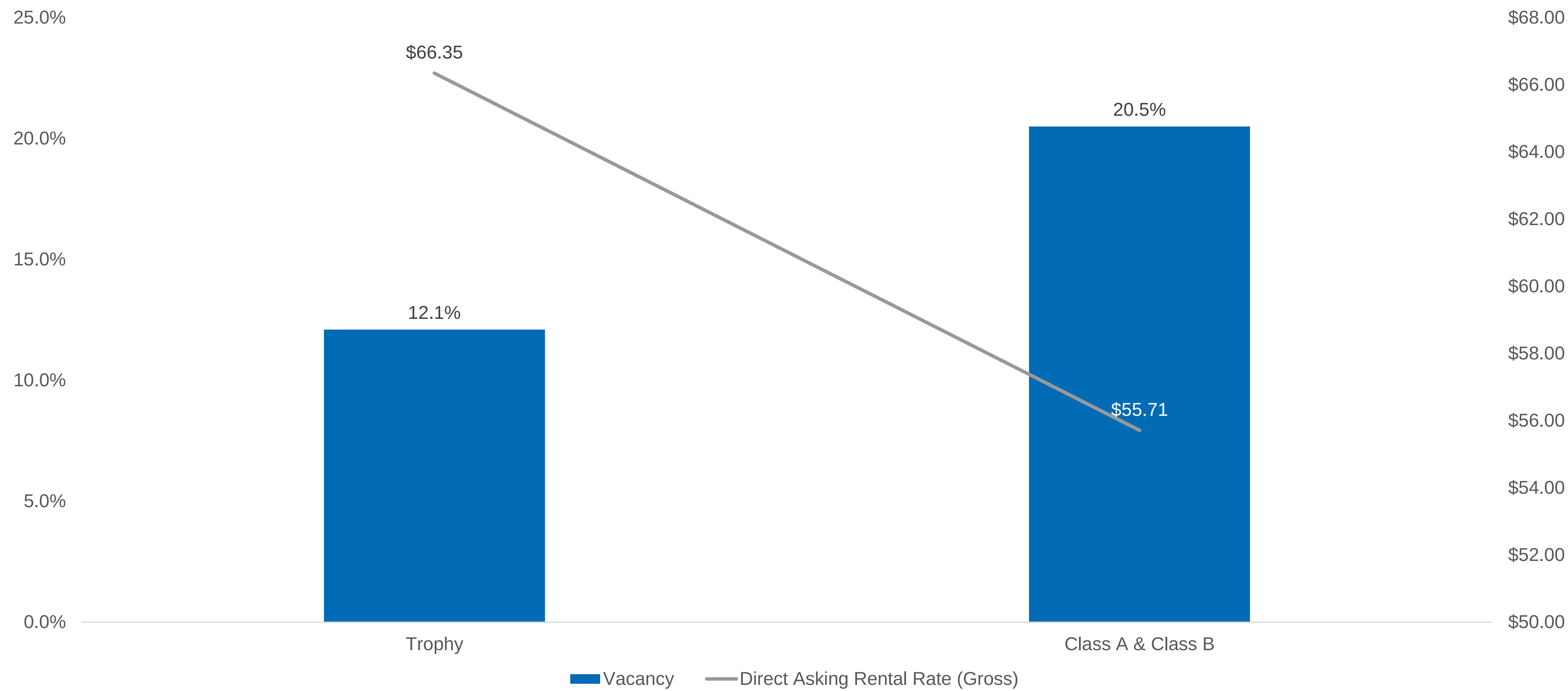


Source: Newmark Research, CoStar

District of Columbia Trophy Office Outperforms Class A & Class B

The District of Columbia, like many other office markets, is experiencing a bifurcation of performance across classes. “Flight to quality” is a pervasive trend and is especially observed among Trophy assets.

Vacancy and Rental Rates By Office Class, Q1 2024



Source: Newmark Research.

Leasing Activity Dominated by Renewals

Despite negative absorption, leasing activity continues, albeit at a slower pace. Major first-quarter transactions were comprised entirely of lease renewals, with the most activity occurring within the East End submarket, which contained three of the top five transactions.

Notable 1Q24 Lease Transactions

Tenant	Building(s)	Submarket	Type	Square Feet
The Washington Post	1301 K Street, NW	East End	Lease Renewal	299,873
District Office of Chief Financial Affairs	1101 4th Street, SW	Southwest	Lease Renewal	263,097
Finnegan	901 New York Avenue, NW	East End	Lease Renewal	214,258
The International Bank for Reconstruction and Development	1899 Pennsylvania Avenue, NW	CBD	Lease Renewal	56,796
Caplin & Drysdale	1 Thomas Circle, NW	East End	Lease Renewal	54,487

Source: Newmark Research

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Submarket Stats

District of Columbia Market Overview

Market Statistics By Class

	Total Inventory (SF)	Overall Vacancy	Overall Availability	1Q 2024 Absorption (SF)	YTD Absorption (SF)	Quarter Deliveries (SF)	YTD Deliveries (SF)	Under Construction (SF)	Asking Rent (Price/SF)
Washington D.C.	**130,892,045**	**20.3%**	**26.1%**	**-80,594**	**-80,594**	**0**	**0**	**735,906**	**$55.41**
Class A	81,139,426	17.4%	24.5%	115,627	115,627	0	0	735,906	$60.98
Class B	45,648,880	26.1%	29.3%	-199,107	-199,107	0	0	0	$48.87
Class C	4,103,739	11.7%	20.7%	2,886	2,886	0	0	0	$41.75

Submarket Statistics – All Classes

	Total Inventory (SF)	Overall Vacancy	Overall Availability	1Q 2024 Absorption (SF)	YTD Absorption (SF)	Quarter Deliveries (SF)	YTD Deliveries (SF)	Under Construction (SF)	Asking Rent (Price/SF)
Capitol Hill	5,393,778	22.6%	28.6%	36,391	36,391	0	0	0	$59.28
Capitol Riverfront	4,978,946	16.5%	18.7%	14,259	14,259	0	0	0	$58.38
CBD	40,545,429	21.1%	28.6%	155,955	155,955	0	0	336,289	$55.70
East End	42,670,430	23.1%	31.1%	-217,574	-217,574	0	0	399,617	$57.87
Georgetown	2,810,774	26.8%	33.1%	-27,815	-27,815	0	0	0	$53.27
NoMa	11,717,348	12.9%	17.8%	39,457	39,457	0	0	0	$46.59
Southwest	13,000,831	14.4%	14.7%	-27,988	-27,988	0	0	0	$51.28
Uptown	5,774,175	20.5%	18.5%	-35,222	-35,222	0	0	0	$44.90
West End	4,000,334	18.8%	19.9%	-18,057	-18,057	0	0	0	$54.93

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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