

# Greater Philadelphia Office MarketView

Q3 2014

CBRE Global Research and Consulting

MSA UNEMPLOYMENT  
6.7%

MSA OFFICE-USING EMPLOYMENT  
+4,180 jobs Y-o-Y

10-YEAR U.S. TREASURY  
2.54%

BLOOMBERG PHILADELPHIA STOCK INDEX  
13.91% Y-o-Y

## SURGING CENTER CITY SALES ACTIVITY TO PRESAGE BROADER OFFICE MARKET RECOVERY?

\*Arrows indicate change from previous period.

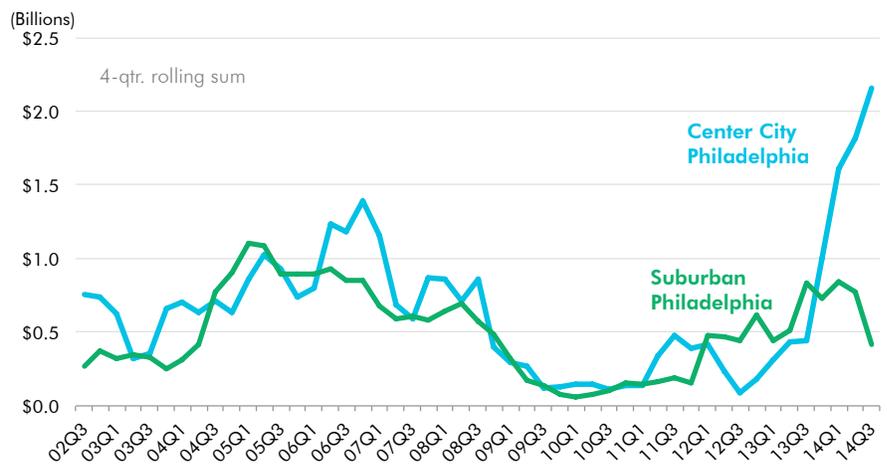
### Quick Stats

Q3 2014	Q-o-Q	Y-o-Y
Total Net Absorption: 1.1 MSF	↑	↑
Total Vacancy Rate: 18.0%	↓	↓
Avg. Asking Lease Rate: \$23.93 FSG	↓	↑
Development Pipeline: 2.3 MSF	↑	↑

### Hot Topics

- Liberty Property Trust officially broke ground on the 1.33 million sq. ft. Comcast Innovation & Technology Center at 18th & Arch Streets in Philadelphia.
- E-Money Advisors leased 69,986 sq. ft. at 100 Matsonford Road in Radnor, PA.
- Hill International Group will relocate its corporate headquarters from Marlton, NJ to a 60,000 sq. ft. space at One Commerce Square in Philadelphia, PA.
- Frontline Technologies has agreed to sublease 60,000 sq. ft. from Endo Pharmaceutical at 1400 Atwater Drive in Malvern, PA with plans to expand by an additional 30,000 sq. ft. in 2017.

Figure 1: Office Sales Volume



Sources: Real Capital Analytics, CBRE Research.

Investors are scooping up Center City Philadelphia office buildings at the fastest rate in years. With billions of dollars of capital searching nationwide for real estate assets with attractive income yield, record pricing has already occurred in major gateway cities such as New York and San Francisco. Center City Philadelphia office buildings, offering higher income yields and stable but improving fundamentals, have caught the eye of investors, leading to soaring sales activity. The abundance of capital indicates that not only will Center City become an increasing target for institutional investors in the future, but also that the outlook for market fundamentals remains positive.

The data tells a compelling story: the largest sales volume (in dollars) of office buildings ever recorded in Center City Philadelphia transpired over the 12 month period ending Q3 2014, according to CBRE estimates. The \$2.16 billion in office building sales between October 1, 2013 and September 30, 2014 represents a jump of 385% compared to the previous year. While this number is

particularly high due to Comcast's estimated \$640 million buyout of Commerzbank's share of Comcast Tower, the statistics without this significant trade still establish an all-time record of approximately \$1.53 billion. Notable trades over the past year include One and Two Commerce Square, 1818 Market, and 1500 Spring Garden.

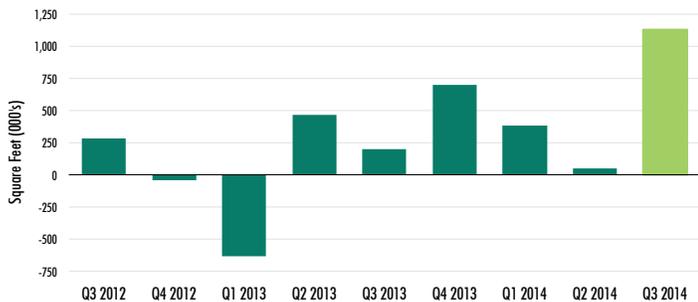
The question remains: does all this transaction activity reflect shifting market fundamentals, or is it just a capital markets play by institutional investors? The answer is both. The outlook for fundamentals is positive: vacancy is forecast to decline and demand to strengthen, supporting rents. Certainly investors recognize the favorable market fundamentals behind their purchases. At the same time, there is abundant equity, supported by increasingly accessible debt, that needs to be placed. Regardless of the reason, the surging investment activity can be considered a sign of favorable office market trends where fundamentals will improve throughout the region in the near-term.

Figure 2: Market Statistics

SUBMARKET	# BUILDINGS	INVENTORY	TOTAL VACANCY RATE	TOTAL AVAILABILITY RATE	COMPLETIONS	UNDER CONSTRUCTION	2014 YTD TOTAL NET ABSORPTION (SQ. FT.)	AVG. ASKING LEASE RATE (\$FSG/PSF/YR)	AVG. CLASS A ASKING LEASE RATE (\$FSG/PSF/YR)
Market West	52	26,897,266	14.2%	16.2%	0	1,285,000	555,987	\$27.85	\$29.17
Market East	19	6,789,819	12.4%	15.6%	0	0	(61,300)	\$23.40	\$24.46
Independence Hall	16	5,969,454	18.4%	18.5%	0	0	(138,952)	\$25.10	\$27.10
University City	23	3,975,620	6.6%	6.6%	340,000	547,700	335,409	\$29.19	\$39.69
<b>DOWNTOWN PHILADELPHIA SUBTOTAL</b>	<b>110</b>	<b>43,632,159</b>	<b>13.8%</b>	<b>15.6%</b>	<b>340,000</b>	<b>1,832,700</b>	<b>691,144</b>	<b>\$26.55</b>	<b>\$28.31</b>
Bala Cynwyd	28	2,859,714	13.7%	15.4%	0	0	34,975	\$29.39	\$30.68
Conshohocken	25	3,363,918	15.0%	19.6%	0	0	120,371	\$31.21	\$32.70
Delaware County	85	5,186,750	16.7%	17.5%	0	0	75,430	\$24.47	\$26.12
Exton/West Chester	89	3,811,618	24.4%	26.6%	0	0	(41,269)	\$22.83	\$22.30
Fort Washington	44	3,382,132	20.5%	21.6%	0	0	93,271	\$23.03	\$25.62
Horsham/Willow Grove	89	5,358,371	21.5%	22.9%	0	0	(12,698)	\$22.36	\$23.56
Jenkintown	21	1,346,850	12.8%	12.8%	0	0	47,820	\$22.87	\$23.86
King of Prussia/Valley Forge	207	15,941,714	20.0%	23.0%	0	0	368,196	\$25.42	\$26.52
Lansdale/Montgomeryville	70	2,659,483	23.2%	24.9%	0	0	34,363	\$22.27	\$23.00
Lower Bucks County	113	5,311,427	24.4%	25.6%	0	0	(8,772)	\$25.58	\$26.63
Main Line	43	2,796,474	5.1%	6.2%	0	0	18,100	\$33.15	\$34.98
Plymouth Meeting/Blue Bell	117	6,020,691	26.8%	29.6%	0	0	(138)	\$23.47	\$24.79
Upper Main Line	42	1,263,153	19.5%	19.5%	0	0	49,067	\$24.61	\$26.58
<b>SUBURBAN PHILADELPHIA SUBTOTAL</b>	<b>973</b>	<b>59,302,295</b>	<b>19.9%</b>	<b>22.0%</b>	<b>0</b>	<b>0</b>	<b>778,716</b>	<b>\$24.76</b>	<b>\$26.16</b>
Burlington County	190	9,763,417	14.8%	15.3%	0	0	228,611	\$18.99	\$21.38
Camden County	118	7,418,495	27.0%	27.0%	0	0	(7,883)	\$20.42	\$21.60
Gloucester County	26	530,626	17.5%	21.8%	0	0	7,065	\$22.75	\$24.38
<b>SOUTHERN NEW JERSEY SUBTOTAL</b>	<b>334</b>	<b>17,712,538</b>	<b>20.0%</b>	<b>20.4%</b>	<b>0</b>	<b>0</b>	<b>227,793</b>	<b>\$19.93</b>	<b>\$21.69</b>
Wilmington CBD	40	7,112,044	23.1%	23.1%	0	0	(37,464)	\$23.15	\$26.52
New Castle Co. Suburbs	176	9,233,700	18.8%	18.8%	0	0	(70,639)	\$21.43	\$22.30
<b>NORTHERN DELAWARE SUBTOTAL</b>	<b>216</b>	<b>16,345,744</b>	<b>20.7%</b>	<b>20.7%</b>	<b>0</b>	<b>0</b>	<b>(108,103)</b>	<b>\$22.39</b>	<b>\$24.67</b>
Lehigh Valley East	53	2,581,449	16.2%	16.9%	0	0	31,759	\$18.39	\$19.78
Lehigh Valley West	100	6,061,814	17.5%	17.5%	0	473,000	(69,526)	\$18.05	\$19.29
<b>LEHIGH VALLEY SUBTOTAL</b>	<b>153</b>	<b>8,643,263</b>	<b>17.1%</b>	<b>17.3%</b>	<b>0</b>	<b>473,000</b>	<b>(37,767)</b>	<b>\$18.14</b>	<b>\$19.39</b>
<b>TOTAL</b>	<b>1,786</b>	<b>145,635,999</b>	<b>18.0%</b>	<b>19.4%</b>	<b>340,000</b>	<b>2,305,700</b>	<b>1,558,586</b>	<b>\$23.93</b>	<b>\$26.00</b>

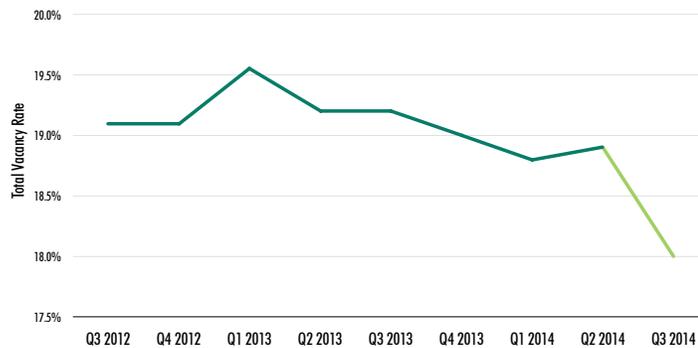
Source: CBRE Research, Q3 2014.

**Figure 3: Total Net Absorption ('000's sq. ft.)**



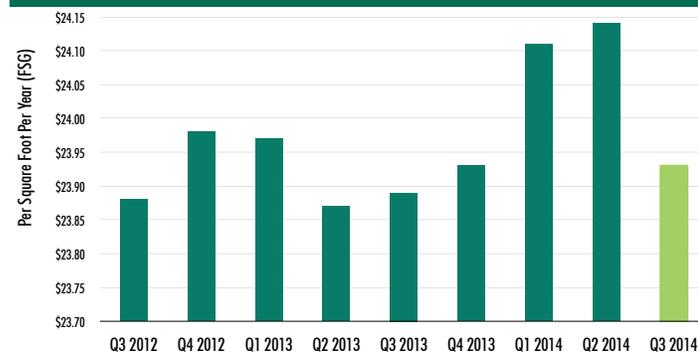
Source: CBRE Research, Q3 2014.

**Figure 4: Total Vacancy (%)**



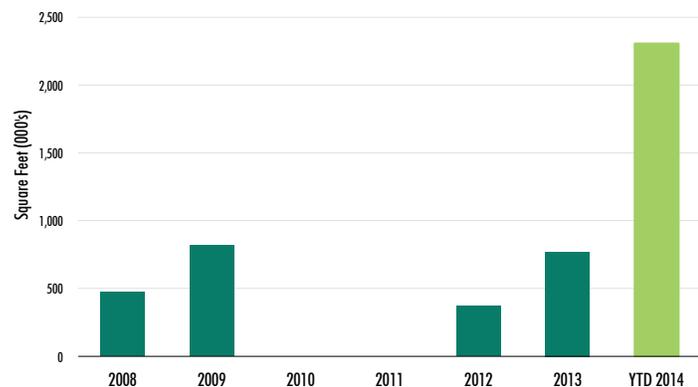
Source: CBRE Research, Q3 2014.

**Figure 5: Average Direct Asking Lease Rate (FSG)**



Source: CBRE Research, Q3 2014.

**Figure 6: Development Pipeline ('000's sq. ft.)**



Source: CBRE Research, Q3 2014.

**OFFICE ABSORPTION**

The region experienced a strong third quarter with 1,129,346 sq. ft. of positive net absorption. This is a rebound after a slightly weak second quarter of 48,000 sq. ft. of absorption. Market West led Downtown Philadelphia with 366,401 sq. ft. of positive absorption with several professional services firms taking full floors. King of Prussia led Suburban Philadelphia with 180,762 sq. ft. of positive absorption, a figure made up mostly of smaller to mid-size tenants. Burlington County experienced 170,334 sq. ft. of positive absorption in New Jersey. The New Castle County submarket in northern Delaware also performed well with 124,005 sq. ft. of positive absorption. Thirteen of the 24 submarkets experienced positive absorption this quarter, creating favorable momentum throughout the region.

**OFFICE VACANCY**

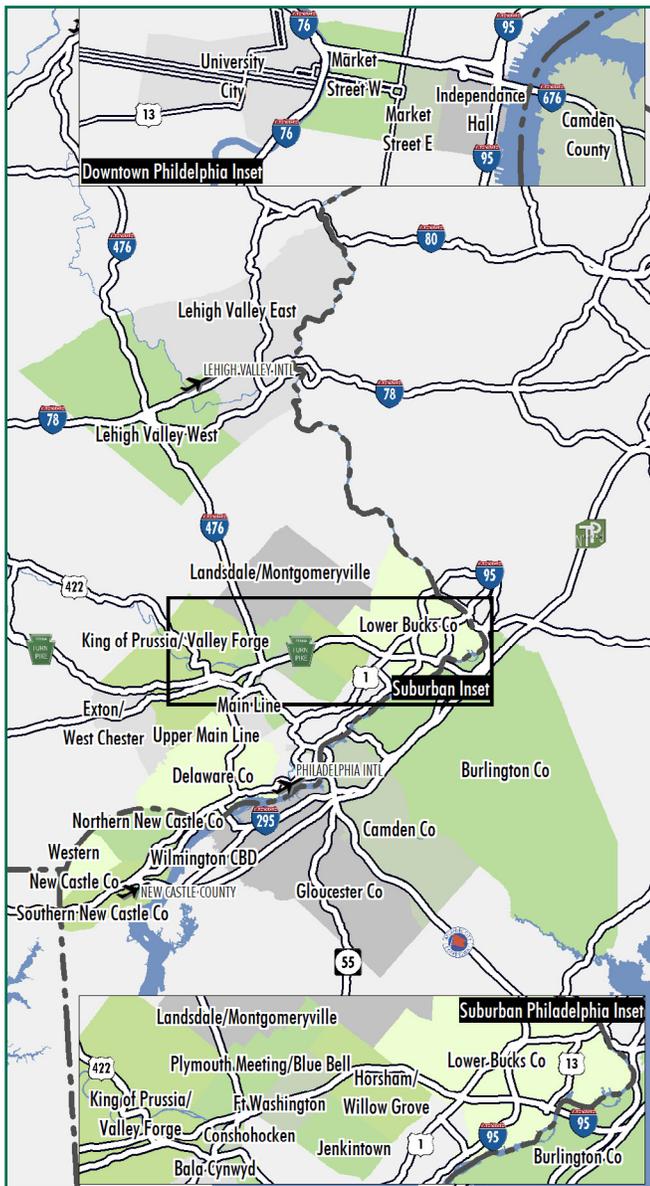
The total vacancy rate across all submarkets decreased by 90 basis points quarter-over-quarter to 18.0%. Notable improvement occurred downtown in Market West as the total vacancy rate decreased by 130 basis points quarter over quarter to 14.2%, and in the Suburban markets where Delaware County decreased by 580 basis points quarter over quarter to 16.7%. The two tightest submarkets in the region continue to be the Main Line and University City, with direct vacancy rates of 3.8% and 5.4% respectively. The 80 basis point total vacancy increase in the Lehigh Valley contrasted with strong performances in Southern New Jersey, where rates dropped to 20.0%, and in Northern Delaware, where they stand at 20.7%. Moving forward, we expect lower vacancy rates to continue to be tied to submarkets in which ownership groups invest in their buildings to offer a more modern workspace.

**OFFICE LEASE RATES**

The overall average asking lease rate for the region decreased from \$24.14 to \$23.93 per sq. ft. quarter over quarter. This breaks the streak of four consecutive quarters of rental rate growth for the region. However, when compared year over year, the regional average has appreciated by \$.04 per sq. ft. Submarkets that have a higher quality inventory and access to public transit saw their rates continue to increase. Conshohocken saw average asking rates increase by \$0.45 to \$31.38 per sq. ft., while the Main Line submarket continues to be the high water mark in Suburban Philadelphia as rates increased by \$0.94 to \$33.15 per sq. ft. The flight to quality was also evident in Southern New Jersey, as Class A average asking rates increased by \$0.45 to \$21.69 per sq. ft. The Burlington County submarket led this notable increase, with a rate increase of \$0.87 quarter over quarter. Moving forward, we expect the pricing gap between Class A and Class B to widen, as more modern space comes on the market.

**OFFICE DEVELOPMENT PIPELINE**

With construction underway at the Comcast Innovation and Technology Center, the office development pipeline has increased to 2.3 million sq. ft. This marks the third consecutive quarter of increasing pipeline figures, a strong sign of improving economic fundamentals in the region. The University City Science Center at 3737 Market Street completed work and opens its doors with 82% of the space occupied. Suburban development figures may increase over the next year, as Conshohocken continues to outpace most of the Philadelphia suburban submarkets. Equus Capital Partners, Oliver Tyrone Pulver Corporation, Keystone Property Group, E-Kahn Development, and O'Neil Property Group each have secured land in the popular submarket. Moving forward, we anticipate any new developments in the suburban submarkets to be oriented around access to public transit.



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