
2Q23

Greater Philadelphia Office Market Overview



NEWMARK

Market Observations

Economy

- The region’s labor market remained historically strong amid shifting macroeconomic conditions. May’s 3.6% unemployment rate was significantly lower than the 5.6% 10-year historical average.
- Year-over-year, job gains have been most pronounced in the services industry, which now employs more people than it did pre-pandemic. Leisure/hospitality led all sectors in job gains during the past 12 months.
- Some cracks are beginning to show as the Federal Reserve continues its tightening policies. Philadelphia-area employers like David’s Bridal and Forman Mills announced large-scale layoffs and store closures.

Major Transactions

- UGI Corp. announced it was moving its headquarters from 460 N. Gulph Road to 500 N. Gulph Road. The energy company explained it was moving for better amenities and more efficient workspaces. 500 N. Gulph Road was renovated in 2019.
- AmeriHealth Caritas preleased the 106,000 SF Mass Timber building at Ellis Preserve in Newtown Square. The building is slated for completion in 2024. AmeriHealth already leases 378,000 SF at Ellis Preserve.
- Independence Health Group announced it was attempting to sublease its 224,000-square-foot office at 1900 Market Street. The health insurance giant will relocate the operations of its former office to its main headquarters at 1901 Market Street.

Leasing Market Fundamentals

- Absorption in the second quarter of 2023 totaled negative 602,411 SF, almost identical to the previous quarter. Year-to-date absorption totals negative 1.2M SF, with 73% of space givebacks concentrated in the West Market and King of Prussia submarkets. Large occupiers like IBX, Effectv, and Comcast have consolidated their footprints and have left large blocks of space available.
- Class B rents in Greater Philadelphia have peaked and are beginning to decline. Weak demand for vintage product cannot support current asking rates. In the second quarter of 2023, less than 15% of leasing activity was concentrated to Class B offices.
- Sublease availabilities now total 6.3M SF, 5.8% of the market’s inventory. Many of these additions carry significant term left and ask on average 9.0% less than direct asking rates. The combination of affordability, office condition and term have made sublease space a serious competitor to landlords attempting to lease existing availabilities.

Outlook

- Vacancy in Philadelphia will increase further as the year progresses. Around 500,000 SF of leases throughout the city are slated to expire in 2023, providing tenants the opportunity to rework their footprints or go fully remote.
- In the suburbs, leasing activity and deal velocity will be concentrated in major submarkets like King of Prussia, Conshohocken and Radnor/Main Line. At the end of the second quarter of 2023, over 500,000 SF of space requirements were concentrated in those three areas.
- The completion of the 308,000-square-foot Morgan Lewis office is expected sometime in the late summer. This is the first new office constructed in the Central Business District since the Comcast Technology Center at 1800 Arch Street.

1. Economy
2. Leasing Market Fundamentals

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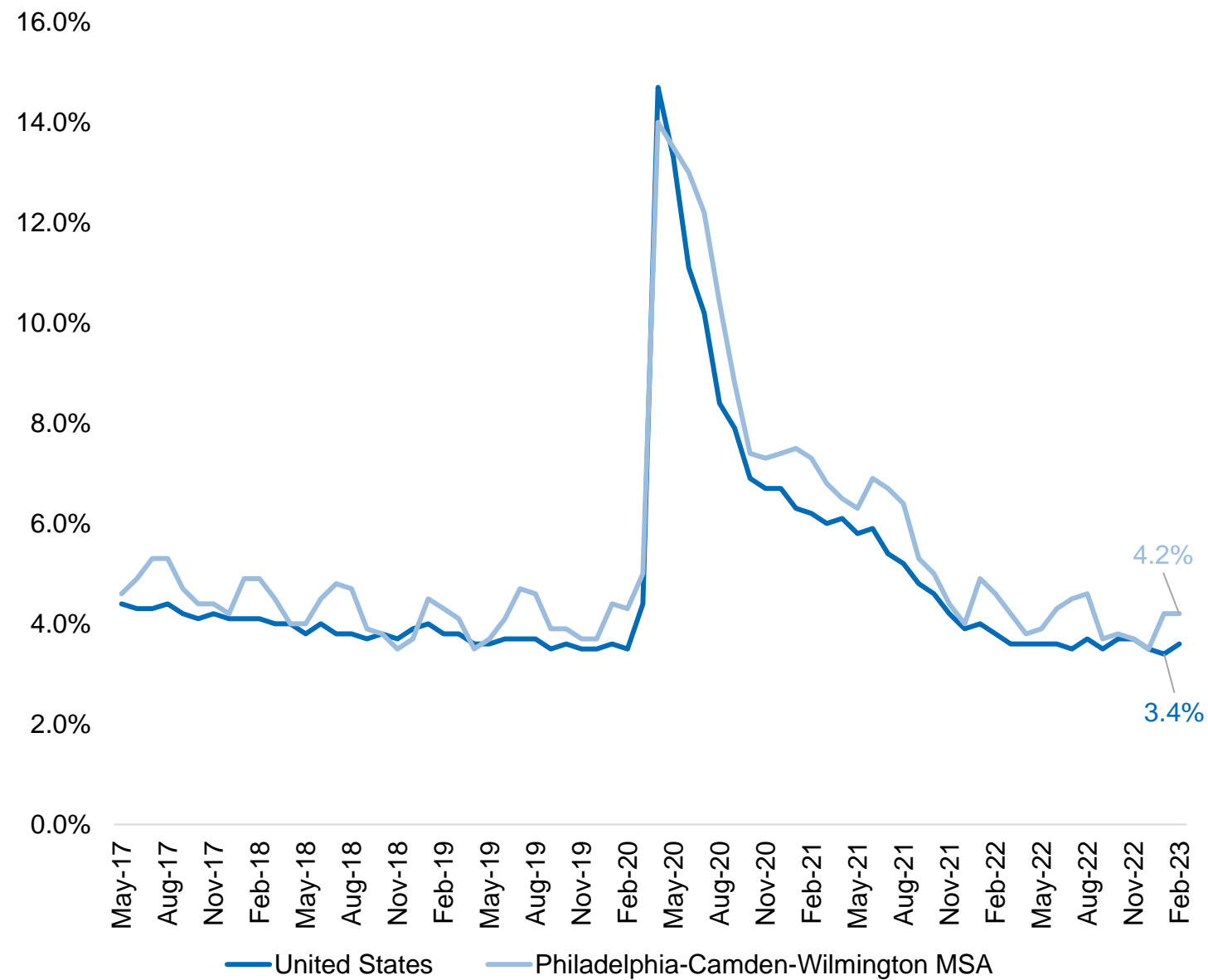
Economy



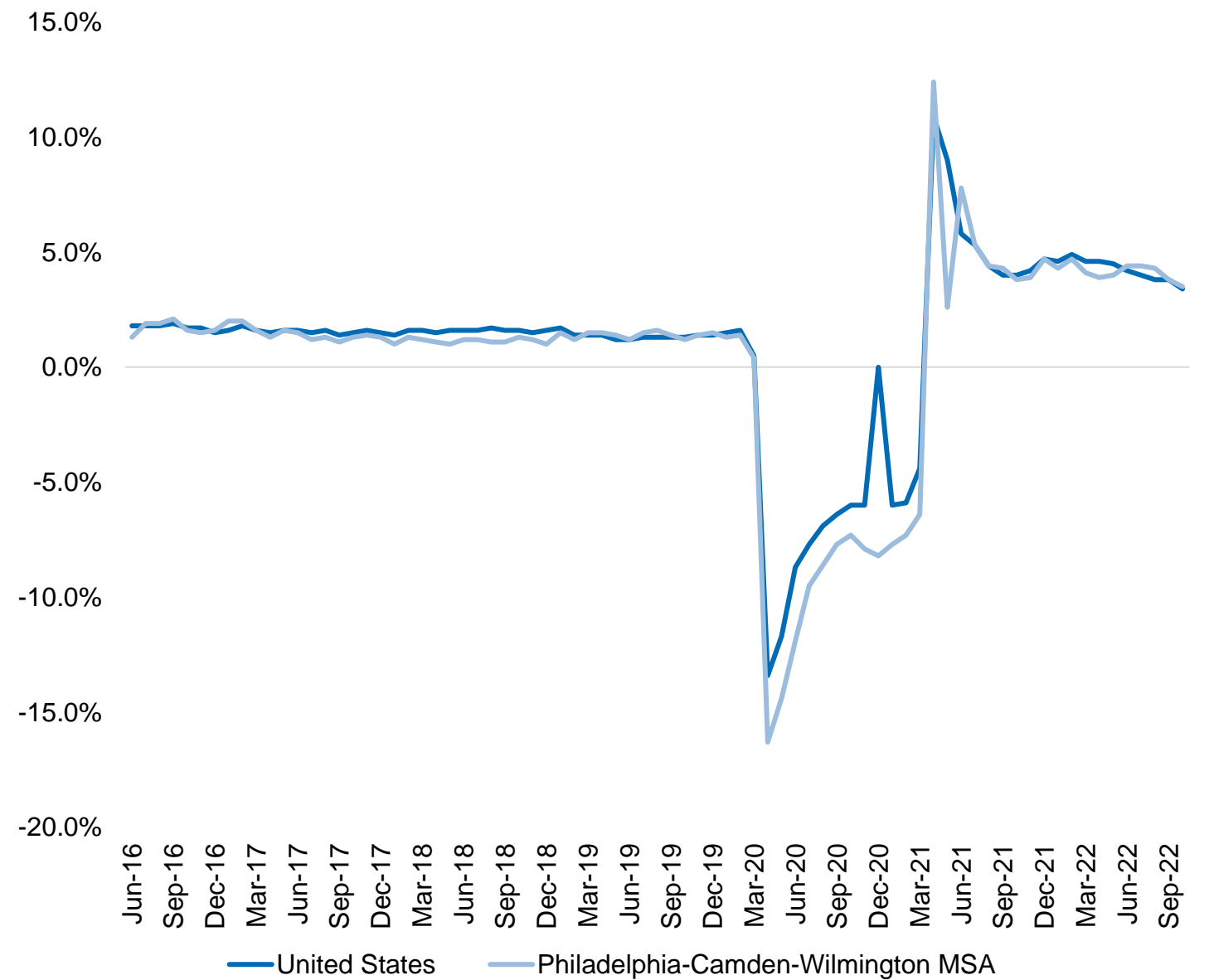
Metro Employment Trends Signal a Slowing Economy

Many economic measurements indicate that Philadelphia Metro's labor market is outperforming national averages; however, employment growth is expected to slow in the quarters ahead due to the Federal Reserve's expected rate hikes in the second half of the year and other macroeconomic headwinds.

Unemployment Rate, Seasonally Adjusted



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

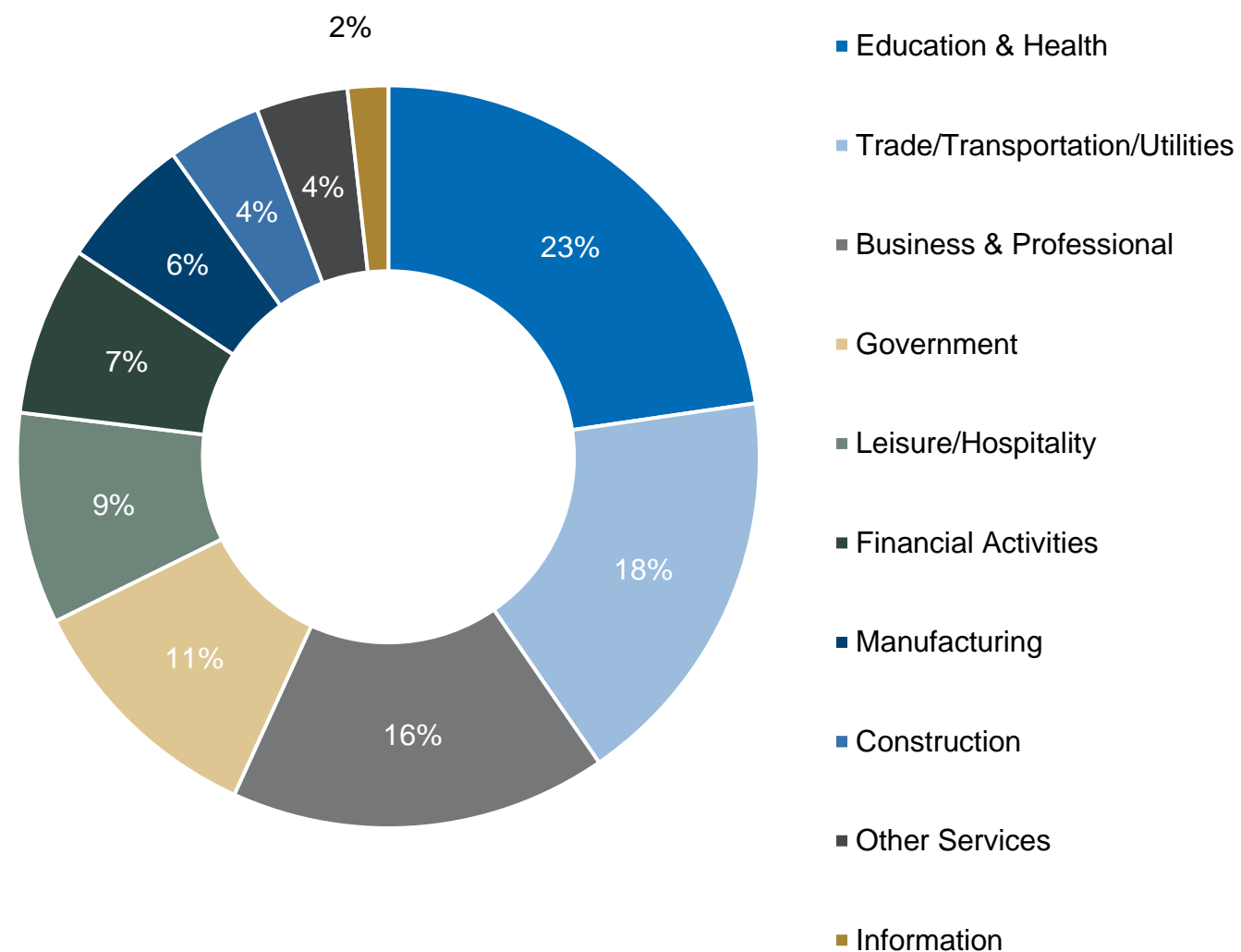


Source: U.S. Bureau of Labor Statistics, Philadelphia-Camden-Wilmington MSA

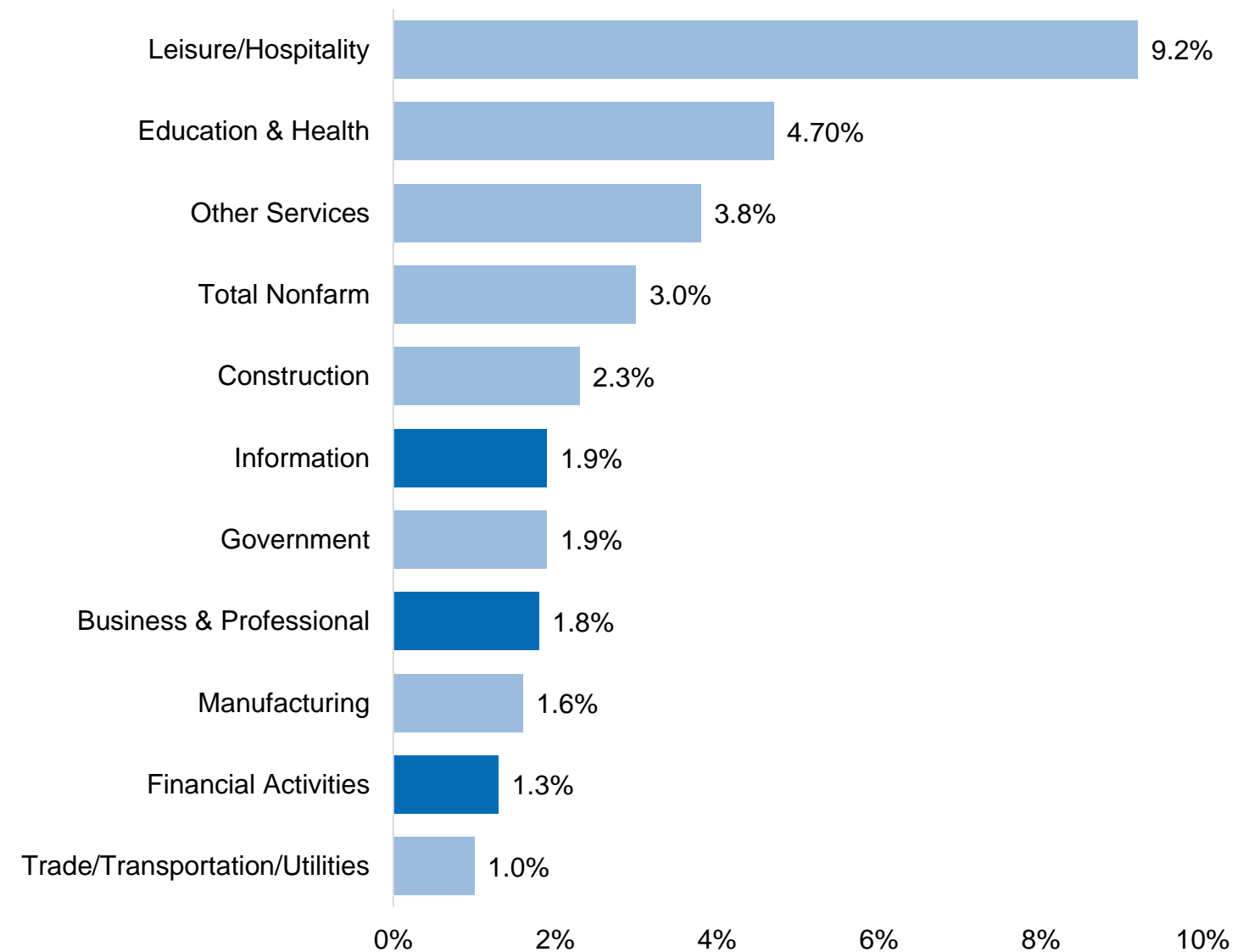
Job Growth Driven in Large Part by Services Still Making up for Pandemic Losses

The leisure and hospitality industry has led the region's post-pandemic recovery. Since the end of the first quarter of 2023, this sector has added over 23,600 jobs. Employment growth in office-using employment has been healthy; however, year-over-year growth has declined compared with figures from the first quarter of 2023.

Employment by Industry, May 2023



Employment Growth by Industry, 12-Month % Change, May 2023

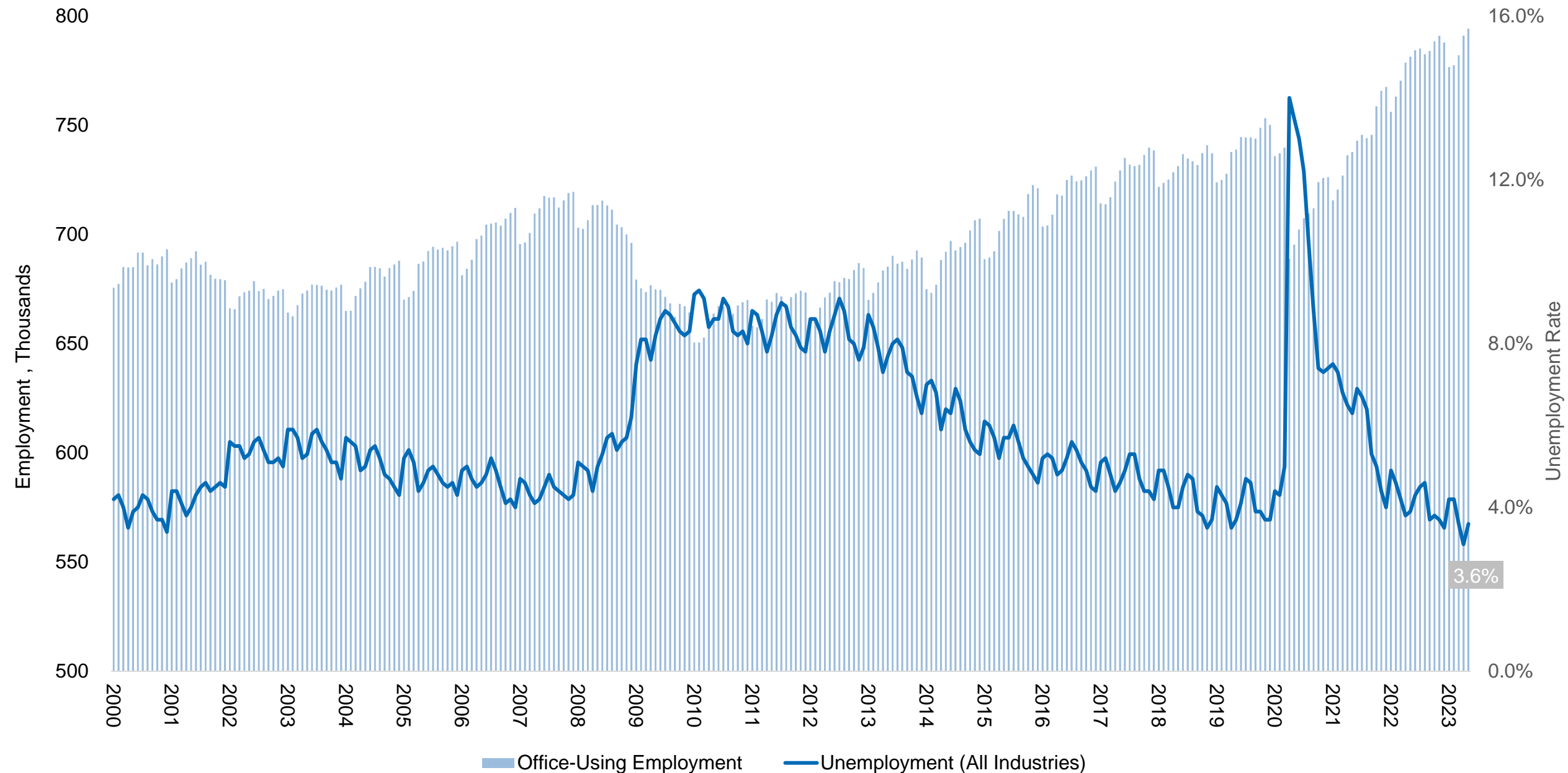


Source: U.S. Bureau of Labor Statistics, Philadelphia-Camden-Wilmington MSA

Overall Office-Using Employment Has Rebounded

The number of office jobs has exceeded pre-pandemic levels since the end of 2021, but office occupancy has not been in step. A historically tight labor market has given workers more leverage over employers, and they have been adamant about maintaining the option of remote work.

Office-Using Employment* and Unemployment Across All Industries



Source: U.S. Bureau of Labor Statistics, Philadelphia-Camden-Wilmington MSA

Note: May 2023 data is preliminary.

*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.

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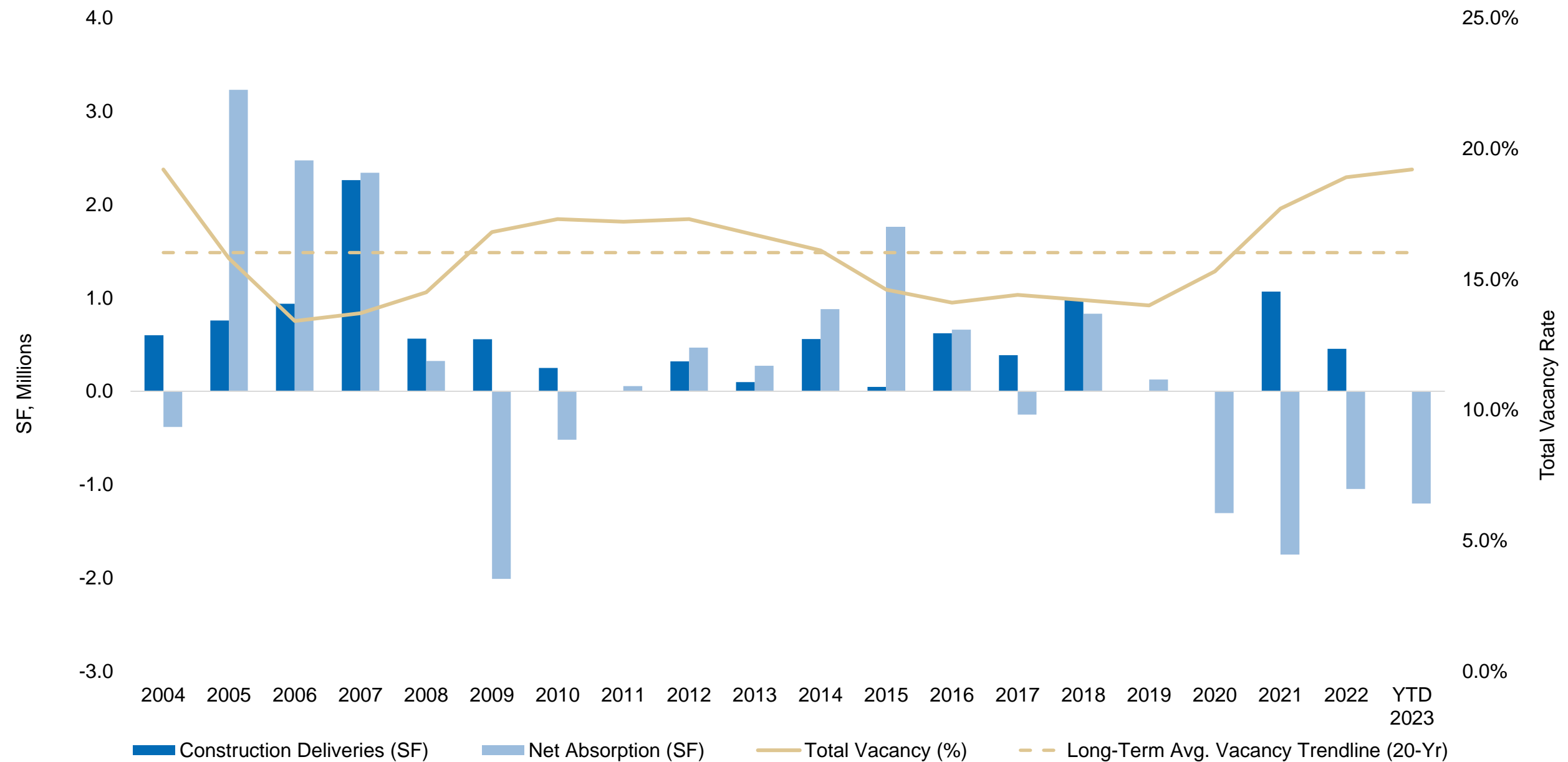
Leasing Market Fundamentals



Vacancy Rises as Tenants Downsize

The suburban and city markets continue to struggle with vacancy additions as previously large office occupiers like IBX, Effectv and Digitas gave up significant amounts of space in the second quarter of 2023. Current vacancy matches the 20-year high but is expected to increase further as multiple large leases are set to expire in the coming years.

Historical Construction Deliveries, Net Absorption, and Vacancy

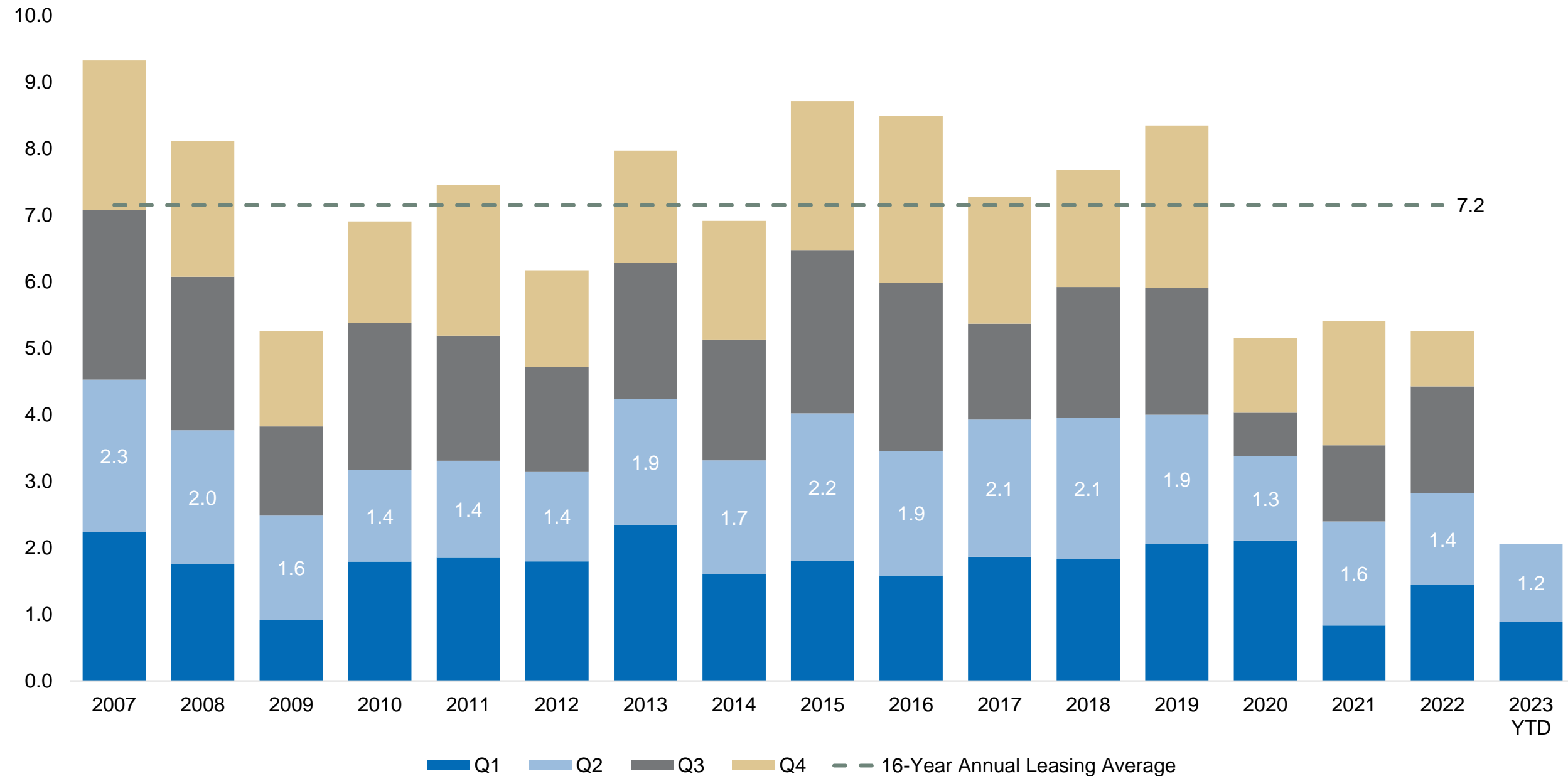


Source: Newmark Research

Leasing Activity Pace Increased Compared with 1Q23

The pace of leasing activity in the first half of 2023 is around 20% less than in the first half of 2021 and 2022; however, large leases signed by UGI, AmeriHealth Caritas, and Glenmede Trust caused leasing activity to rise 31.2% quarter over quarter.

Total Leasing Activity (MSF)

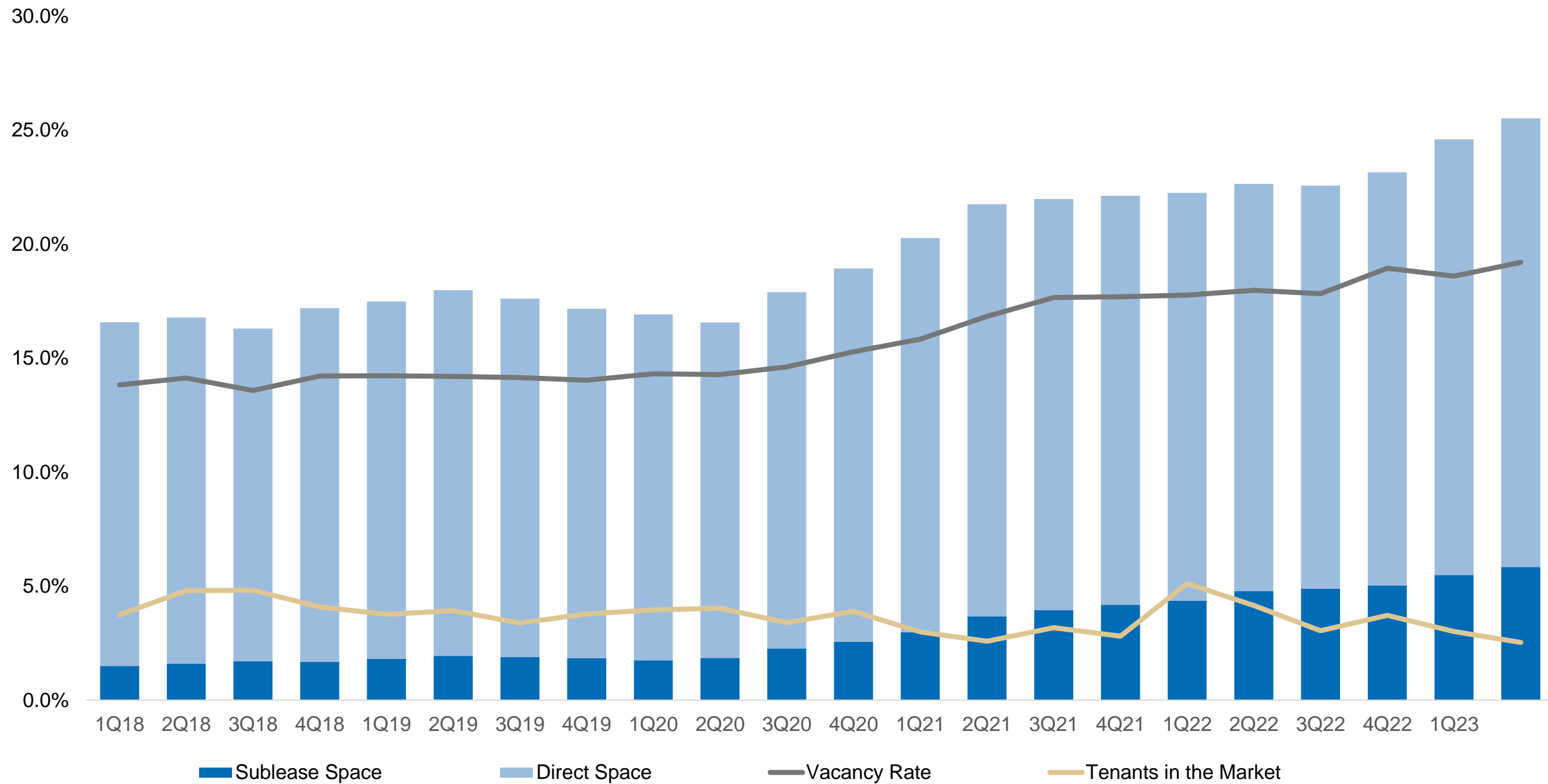


Source: Newmark Research, CoStar

Availability Continues to Increase While Tenant Demand Drops

Space requirements in the market have declined over the past few quarters as many users have decided to downsize from their current footprints. A declining need for space due to hybrid work arrangements and cost savings benefits in a volatile economy are some reasons for contraction.

Available Space and Tenant Demand as Percent of Overall Market

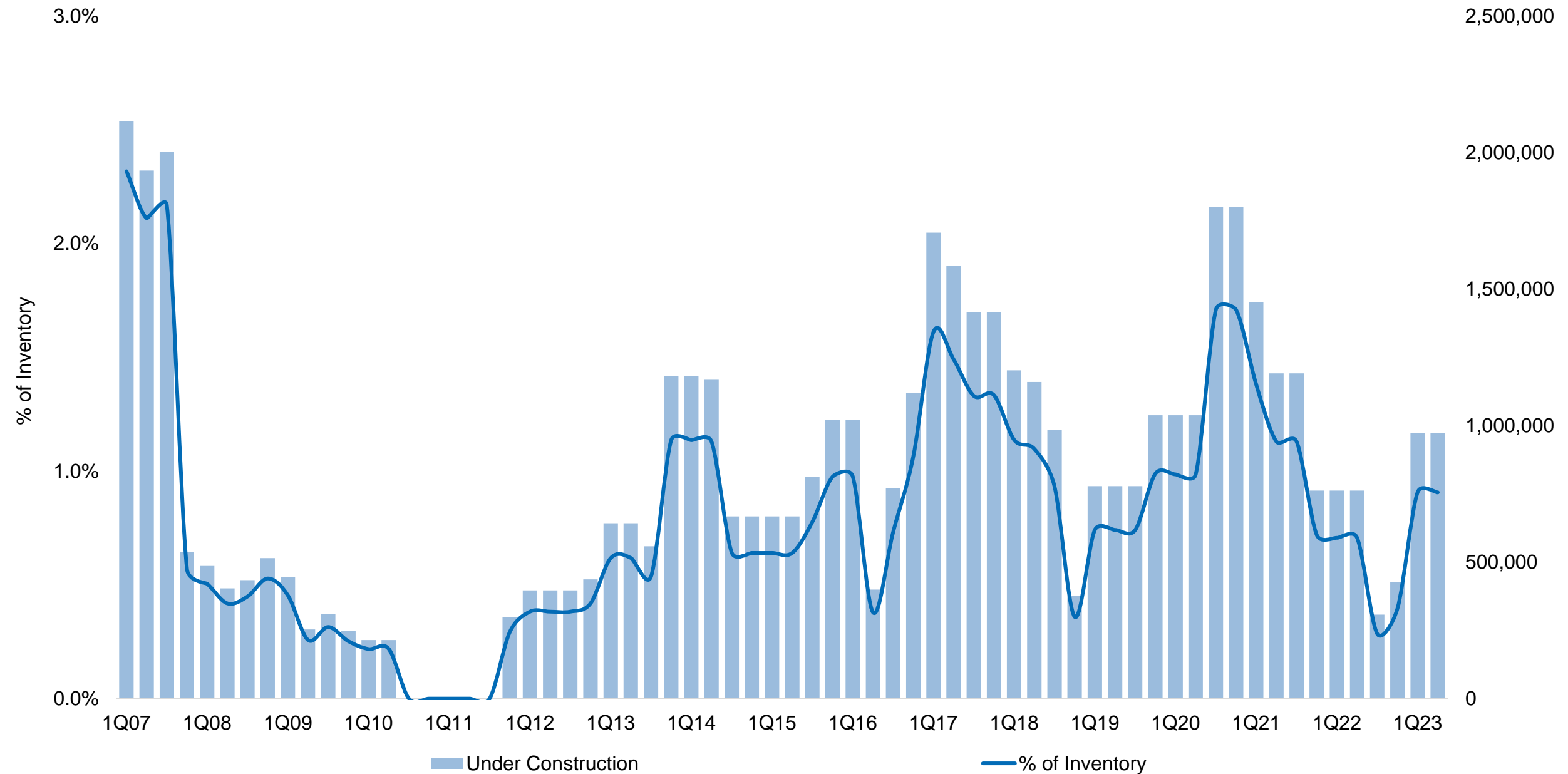


Source: Newmark Research

New Construction is Primarily Build-to-Suit

Around 63.4% of Greater Philadelphia's construction pipeline is built-to-suit. Companies like AmeriHealth Caritas, Morgan Lewis, and Chubb have committed significant resources to their future workplaces. State-of-the-art space is difficult to find in this market; buildings constructed within the past 10 years have a vacancy rate of 2.7%.

Office Under Construction and % of Inventory

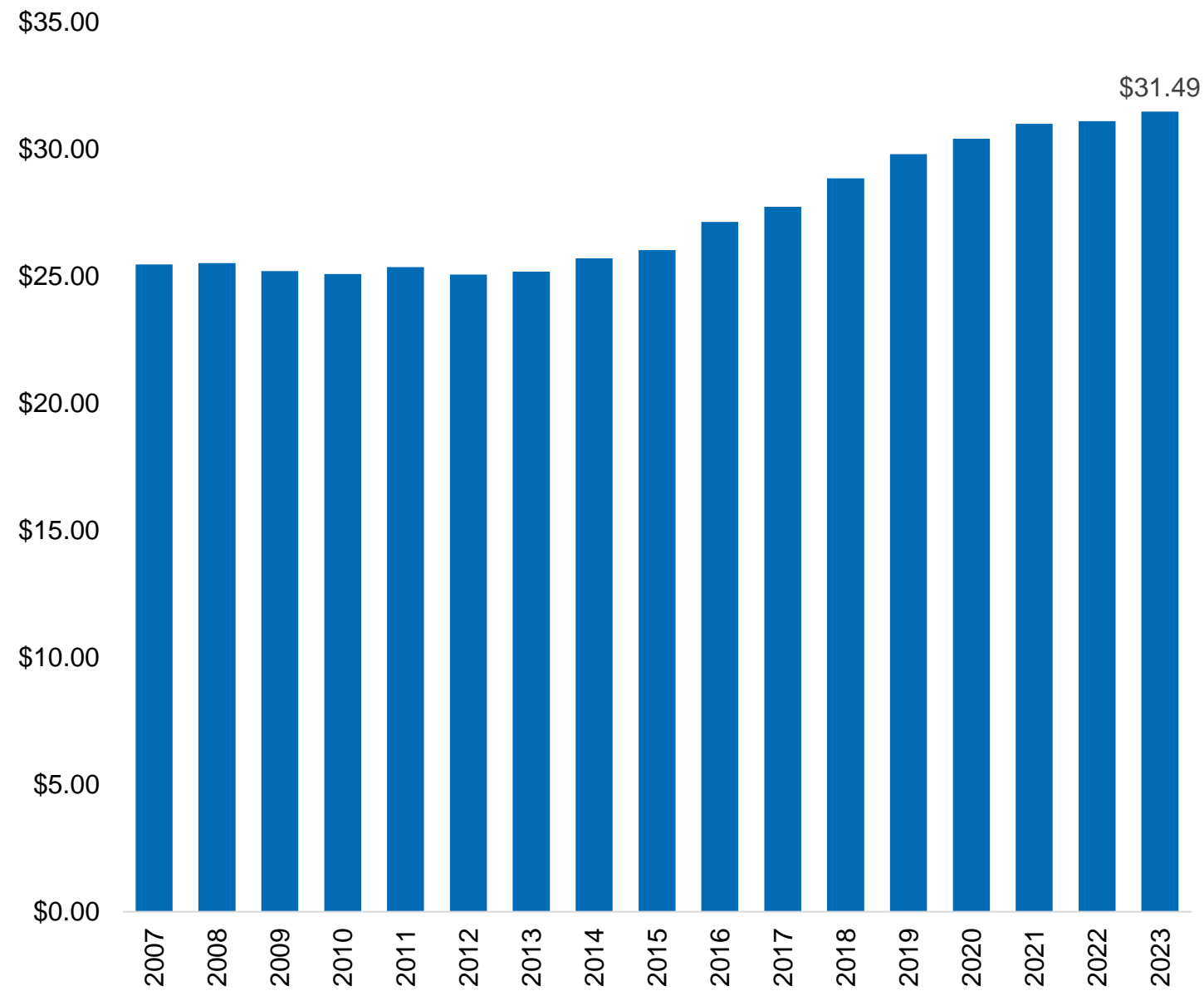


Source: Newmark Research

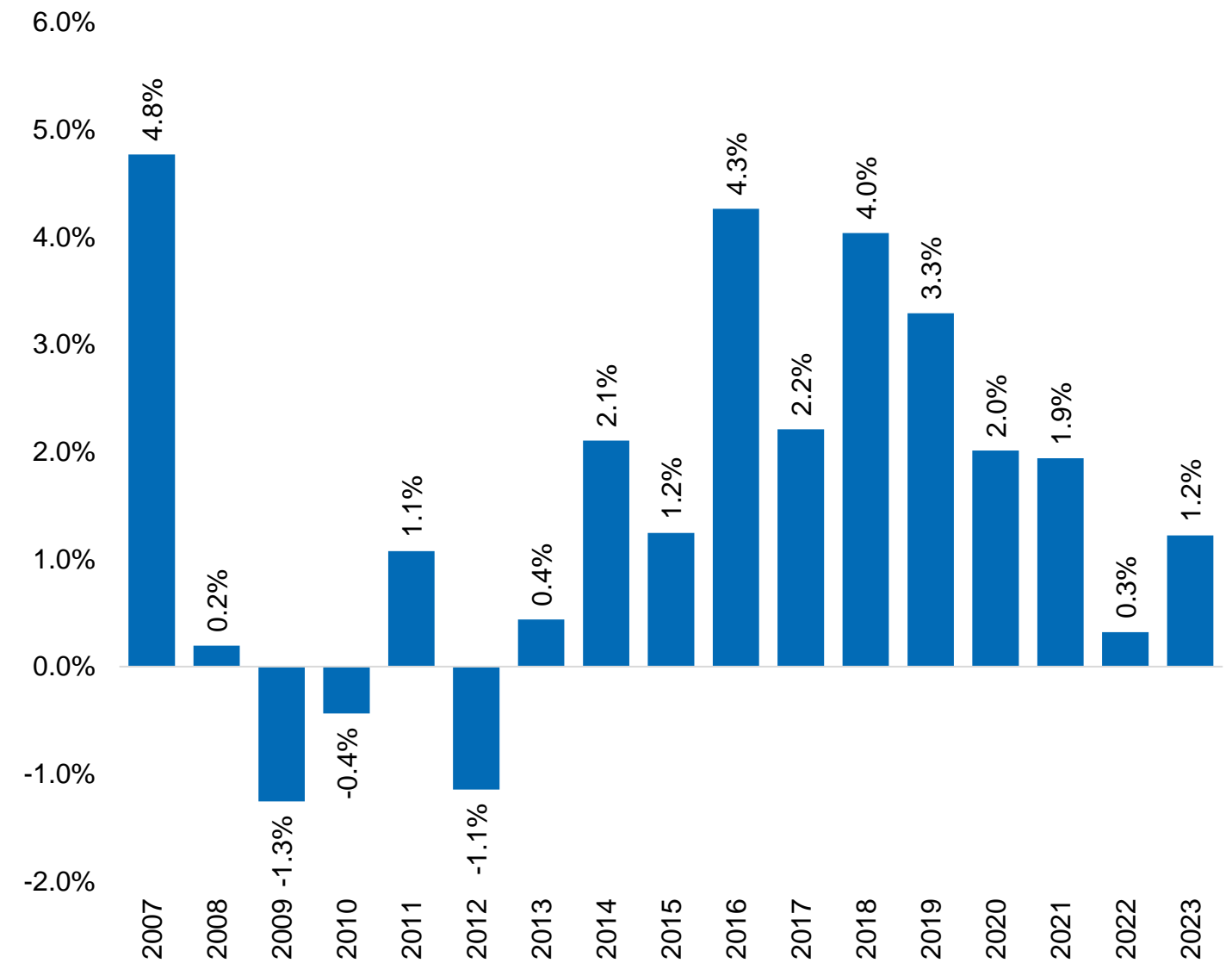
Rents Are Stabilizing

Asking rents have plateaued and began to decline in some submarkets in the second quarter of 2023. Face rents are near all-time highs; however, effective rents are falling faster due to the aggressive concession packages offered by landlords.

Office Average Asking Rent, \$/SF, FS



Year-Over-Year Asking Rent Growth Rate

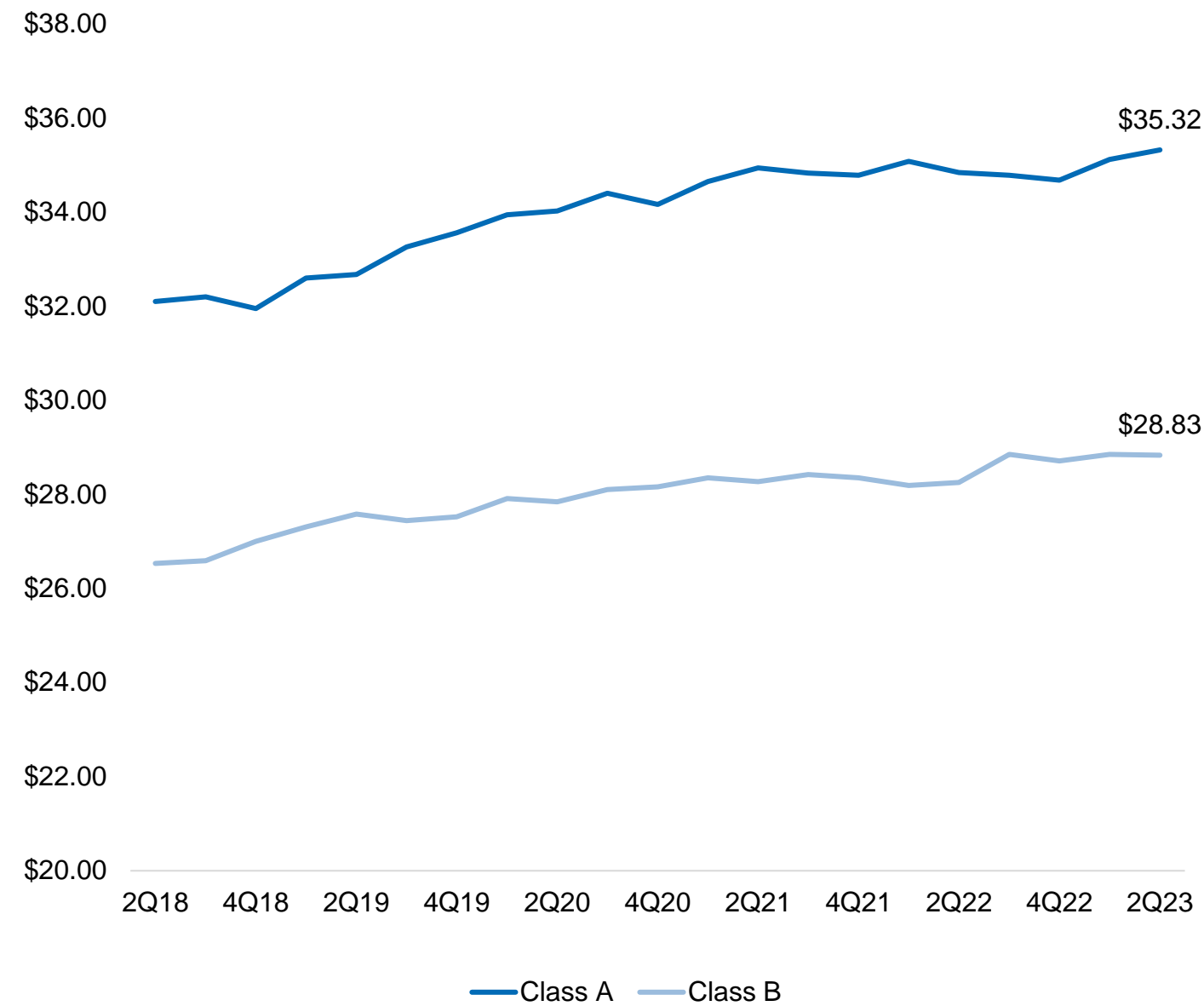


Source: Newmark Research

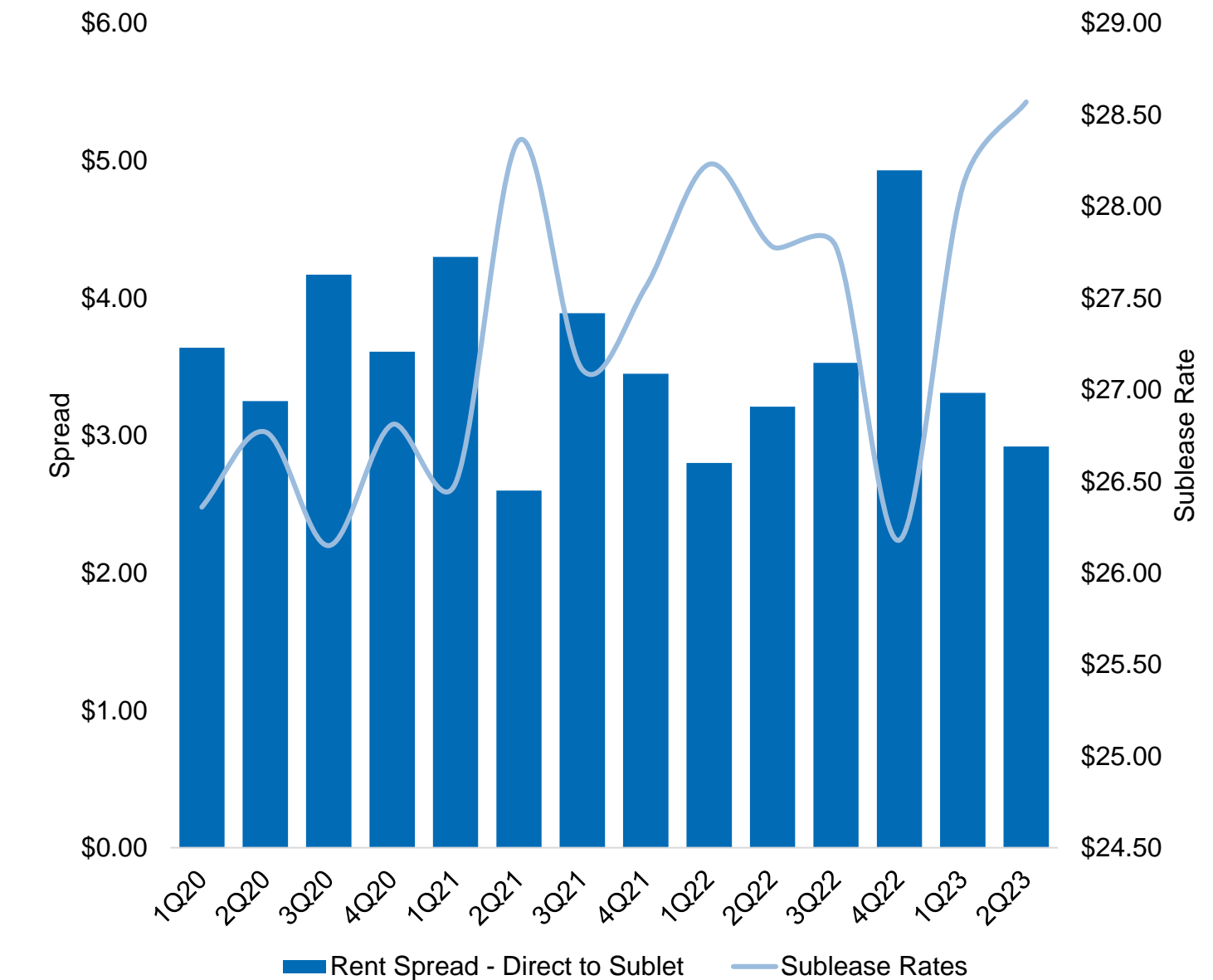
Asking Rents March on for Class A Space

Class A rents have grown by \$0.48/SF year-over-year as space demand remains focused on high-end and trophy assets. The average asking rate for vintage properties peaked last year and is beginning to decline in suburban markets. Rent spread between direct and sublet space has compressed in the past couple of quarters, as many of the new availabilities were large blocks in great condition and located in trophy buildings in the CBD.

Class A and Class B Asking Rents



Sublease Rates



Source: Newmark Research, CoStar

Leasing Activity: Green Shoots in the Suburbs, Crab Grass in the City

New leasing activity in the suburbs is anticipated to net new absorption gains as UGI is expected to occupy 500 N. Gulph Road in the third quarter of 2023. Inversely, many of the city's largest deals will deteriorate the CBD's occupancy as three major lease transactions occurred, which reduced each tenant's previous footprint. The average percentage of space reduction for these tenants was 38.7%.

Notable 2Q23 Lease Transactions

Tenant	Building(s)	Submarket	Type	Square Feet
AmeriHealth Caritas	203 Squire Drive	Central/Southern Delaware County	Prelease	106,000
<i>The lease is part of AmeriHealth's plan to add 1,000 employees in the years ahead</i>				
UGI Corporation	500 N. Gulph Road	King of Prussia	Sublease	100,820
<i>Desire for modern floorplans and better amenities drove UGI to the recently renovated building</i>				
Glenmede Trust Co.	1650 Market Street	CBD – West Market	Lease Renewal/Downsizing	74,000
<i>Glenmede previously occupied 111,000 SF in building. Will occupy new 74,000 SF office in 4Q 2024.</i>				
Digitas, Inc.	111 S Independence Mall E	CBD – East Market	Direct Lease	60,000
<i>Formerly occupied 108,619 SF at the Wanamaker Building</i>				
ZS Associates	1650 Market Street	CBD – West Market	Lease Extension	23,715
BDO USA, LLP	1801 Market Street	CBD – West Market	Downsizing	18,522
<i>BDO USA, LLP formerly occupied 25,824 SF in the building, which represents a 28.3% decrease in footprint</i>				

Source: Newmark Research

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