

Current and Future Market Conditions Q3 2017

Philadelphia's office market resumed its growth trend in the third quarter as absorption turned positive at 50,000 SF. This minimal growth is significant because the market absorbed 80,000 SF of contraction from Independence Blue Cross at 1500 Spring Garden Street. Absorption for the year is barely positive after two relatively stagnant quarters to begin the year. 3.25 million SF is still available and the vacancy rate is 8.6%.

New Leases:

- Morgan Lewis renewed 100,000 SF in 10 PC for ten years.
- Klehr, Harrison, Harvey, Branzurg & Ellers renewed 65,000 SF at 1835 Market St. The law firm secured today's rental rates and added 5 years of term onto their existing lease that previously expired in 2020.
- The Office of the Attorney General entered a new 10-year lease at The Phoenix Building leasing 35,000 SF.
- American Heart Association renewed 17,000 SF in Suburban Station for 10 years.
- Magee Rehab leased 18,000 SF at Suburban Station for 12 years.
- Bond Station House, based in New York City, leased the entire 20th floor (20,000 SF) at Suburban Station for 15 years.

In the Market:

- Willis Towers Watson is seeking to considerably reduce its existing footprint from 275,000 SF to 125,000 SF.
- Deloitte plans to downsize from 125,000 SF in 1700 Market St to 75,000 SF.
- Post & Shell, located at 4 PC, is considering relocation options for 60,000 SF.
- Willig, Williams & Davidson hopes to leverage an early termination option on 40,000 SF located at 1845 Walnut St.
- Gordon & Rees is exploring alternatives outside of One Commerce Square for 25,000 SF.
- Jefferson Health System plans to consolidate numerous office spaces into one centralized location with 300,000 SF at 1101 Market St rumored to be the location.
- Wells Fargo is exploring alternatives other than 123 S Broad Street for 125,000 SF.
- Macquarie Investment Management, the successor to Delaware Investments, presently located at One Commerce Square, is seeking 125,000 SF.
- The Department of Labor is searching for 100,000 SF on both East and West Market Street.
- The Engineering firm McCormick Taylor & Associates, Inc., located at Two Commerce Square is proactively approaching their 2020 lease while exploring alternatives for 60,000 SF.
- Simon & Simon has outgrown their existing space at 1515 Market Street and is searching for 30,000 SF.
- Market Resource Partners is rumored to be eager to vacate 1650 Arch Street, seeking 30,000 SF on West Market Street.

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Noteworthy Points:

The largest percentage increase in asking rents occurred in the Class B market where rates moved 4% (or \$1.00 SF) during Q 3. Trophy and Class A asking rates remained flat; however, I expect this to change when existing and new landlords react to a tightening and healthy Class B market. Additionally, with buildings being sold at record high water marks, landlords are renovating aging assets with a plethora of tenant amenities. My take home message: I don't see the rental market going anywhere but up.

- **Statistically, rental rates remain healthy on the surface:** i) Trophy Class space priced at \$39.00/SF, ii) Class A space inched upwards to \$29.00/SF, iii) Class B space priced at \$26.00/SF, and iv) Class C space priced at \$23.00/SF.

Finally, although absorption has slowed from 2016's historic pace, I continue to project minimal positive absorption for the balance of the year with vacancy hovering around current levels. Philadelphia is a city booming with people of all ages flocking to it to live, work, and to play. I believe basic market fundamentals, such as a strong, growing healthcare and education sectors, will offset "shadow space" (discussed last quarter) that is projected for 2018. Landlords should continue to see the market move in their favor for the foreseeable future.

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