

Current and Future Market Conditions Q2 2016

Philadelphia's office market continues to sizzle. The CBD witnessed the rise of the new and exciting FMC Tower. The 600,000 SF trophy asset preleased 425,000 SF. The addition of FMC to the CBD inventory and the vacancy left by Center City tenants offset the flurry of new activity in the CBD. Second Quarter absorption was flat. The CBD's vacancy rate remained at 8.5%, with 3.4 million SF available.

New Leases:

- Duane Morris, LLP agreed to extend their lease for 6 ½ years beyond the current lease expiration date. The Law firm occupies 257,000 square feet at 30 South 17th Street.
- Comcast was at it again expanding in Two Logan Square by leasing an additional 45,000 square feet on floors 15-16. The cable giant now leases 180,000 square feet in Two Logan square and a staggering 300,000 square feet in Three Logan Square.
- Magna Legal Services leased an additional 14,000 square feet in 1635 Market Street bringing their total occupancy to 28,000 square feet. They inked a new lease for 10 1/2 years.
- Carpenter Technology announced it would make Philadelphia their new corporate headquarters by leasing 20,000 square feet in Mellon Bank Center. The company will relocate 100 employees from Wyomissing, PA later this year.
- Nasdaq, formerly The Philadelphia Stock Exchange, will relocate 75,000 SF to FMC Tower from 1900 Market Street to take full advantage of the state and local tax benefits of being in a Keystone Opportunity Zone. They along with Cozen O Conner were original anchor tenants since the building's completion in 1981.

In the Market:

- Aramark Towers is rumored to be relocating to 2401 Market Street to occupy 225,000 SF, leaving a gaping hole of 350,000 SF in their longtime headquarters located at 1101 Market Street.
- Environmental Protection Agency is seeking 225,000 SF, a significant reduction from its current footprint of 310,000 SF at 1650 Arch Street.
- Five Below is rumored to be leaving 1818 Market Street (50,000 SF) in search of 125,000 SF.
- Montgomery McCracken is seeking 100,000 SF. The law firm is presently located at 123 S. Broad Street.
- The CBD continues to attract tenants from suburban markets with Enclara Pharmacia from South Jersey seeking 40,000 SF.
- Relx, formerly Elsevier, is evaluating 100,000 SF of relocation options outside of their longtime home at 4 Penn Center.
- Pennoni & Associates, located at 3001 Market Street are evaluating opportunities to meet 50,000 SF.
- Jacobs Engineering is looking to relocate 50,000 SF from 2301 Chestnut Street.



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- Merrill Lynch, the corporate banking division of Bank of America, is looking to consolidate 60,000 SF that it currently occupies at 1818 Market Street, One Liberty Place and 4 Penn Center.
- Brandywine Global has peaked its head out of Cira Center and is searching for 90,000 SF.
- Jenkins Law Library is looking to keep up with today's trends and head west of broad street in search of 35,000 SF. The Library presently resides at 833 Chestnut, which is owned by a medical REIT and occupied predominantly by Jefferson Hospital.

Noteworthy Points:

- West Market Street continues to be the preferred submarket in the city. A unprecedented flurry of activity involving 10,000 SF - 50,000 SF exists with tenants exploring the market.
- **Statistically, rental rates have surged \$2.00-\$3.00 per SF in the past 24 months.** Q 2 is no different: i) Trophy Class space priced at \$39.00 SF, ii) Class A space priced at \$28.50 SF, iii) Class B space priced at \$25.00 SF, and iv) Class C space priced at \$22.50 SF.
- Keystone Property Group added One Washington Sq. to their already impressive Center City Portfolio consisting of Curtis Center and 100 S Independence Mall. Meanwhile, MRP Realty acquired 325 Chestnut Street, 400 Market Street, and The Bourse Building from the sale of the Kaiserman Company's portfolio. MRP and Keystone now control the vast majority of this submarket. As such, this once "low cost alternative" for office space has turned the corner. East Market street is well positioned with single digit vacancy. Rents have risen in this submarket 20%-30% over the previous 12 months.

With retail, residential and office construction booming throughout the city, landlords will continue to push rents and decrease tenant concessions while generally feeling confident they will renew existing tenants at a premium. Simultaneously, they likely will be bullish about attracting new tenants to available space. The scarcity of quality large blocks of office space in the existing inventory has fueled rental rate growth to new all-time highs.

With rental rate reform upon us for the foreseeable future, the traditional Center City office market will be pushed to the fringes. Using Broad Street as an example, tenants looking for lower cost alternatives (\$21.00-\$23.00 per SF) will need to search south and east of Locust Street, north and east of Callowhill Street and even north and west of Spring Garden Street. These areas are becoming hotbeds for conversion of older industrial buildings to chic office spaces. Buildings featuring exposed ceilings and ducts are now popular and desired by millennials seeking office space. Lastly, tenants with leases expiring in the next 12-18 months must be careful. By delaying a decision regarding renewing or relocating, tenants risk losing out on an opportunity in this fast changing market.