

Current and Future Market Conditions Q4 2016

Transaction velocity across the CBD accelerated during Q 4. 90,000 SF of positive absorption was recorded bringing the year to date net absorption to 240,000 SF. This is a far cry from 2015's historic year of 800,000 SF of positive absorption. The CBD's vacancy rate ended the year at 8.5% with 3.3 million SF available.

New Leases:

- Montgomery McCracken will significantly decrease their footprint from 150,000 SF at 123 South Broad Street to 67,000 SF on floors 19-21 at Mellon Bank Center. The law firm recently committed to a new 16-year lease.
- Mellon Bank Center remains active luring Hogan Lovells from 1835 Market Street, where they leased the 23rd floor and half of the 22nd floor for 33,000 SF. The law firm entered a new 11-year lease.
- Braskem renewed 44,000 SF in Mellon Bank Center for 10 years.
- Pennoni & Associates will relocate to 1900 Market Street from 3001 Market Street, thereby committing to a 12-year lease of 55,000 SF.
- Flaster Greenberg inked a new short term commitment at 1835 Market Street for 5 years. The firm will downsize from 30,000 SF at their present location, 4 Penn Center, to 11,000 SF on the 10th floor at 1835 Market Street.
- WeWork, the shared office company, continues to increase their presence in the Philadelphia market with a new lease of 56,000 SF on the top floor of 1900 Market Street. This lease, coupled with prior leases in 2015 at 1601 Market Street (40,000 SF), 1430 Walnut Street (20,000 SF) and 1010 North Hancock Street (10,000 SF) in Northern Liberties, pushes their net absorption to more than 120,000 SF.
- Nasdaq, formerly The Philadelphia Stock Exchange, will relocate from their long-time headquarters at 1900 Market Street to take advantage of the new FMC Tower's Keystone Opportunity Zone, leasing 75,000 SF for 12 years.
- SCA North America renewed 100,000 SF in the Cira Center well into the next decade.
- Merrill Lynch, the corporate banking division of Bank of America, will consolidate 60,000 SF that it currently occupies at 1818 Market Street, One Liberty Place and 4 Penn Center. A new 10-year lease was signed for 70,000 SF on floors 11 & 12 in Four Penn Center.

In the Market:

- Environmental Protection Agency is seeking 225,000 SF, a significant reduction from its current footprint of 310,000 SF at 1650 Arch Street.
- Jacobs Engineering is looking to relocate 50,000 SF from 2301 Chestnut Street.
- Brandywine Global has peaked its head out of Cira Center, searching for 90,000 SF.
- Jenkins Law Library continues its search for 35,000 SF.
- Relx, formerly Elsevier, located in Four Penn Center is seeking 80,000 SF.
- Spark Therapeutics, a spinoff of Children's Hospital that is new to the market, is seeking 175,000 SF.



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- Comcast is again rumored to be looking for a significant block of space with a new requirement of 100,000 SF.

Noteworthy Points:

- ***Statistically, rental rates remained flat:*** i) Trophy Class space priced at \$39.00/SF, ii) Class A space inched upward to \$29.00/SF, iii) Class B space priced at \$25.00/SF, and iv) Class C space priced at \$22.50/SF.

Obviously, with vacancy continuing to shrink, rentals rates will continue to climb. Simultaneously, landlords are decreasing concessions, specifically abated rent.

Also of note on the supply side is the continuing office construction boom in Center City. Developers are currently building at a feverish pace. As such, the biggest story of 2016 was the dramatic increase in the cost of construction. This trend is clearly making the construction of new office space a major decision parameter and may lead more firms to decide in favor of renewal.

We are seeing rate escalations throughout the CBD, in all submarkets and in all building classes (defined below). The future pace of this escalation will depend on several factors, but the trend will clearly remain for the foreseeable future. During the current cycle, rates have increased 25%-30% over a 3-year period.

In Summary, presuming the national economy continues to grow and expand, Philadelphia's CBD will absorb the new supply and continue to strengthen in the next few years. Further, any new supply will be constrained and positive absorption will continue to shrink the remaining vacancy.