Current and Future Market Conditions Q4 2013

At the conclusions of Q 3 the Philadelphia Central Business District (CBD) was looking optimistic with 192,000 SF being absorbed YTD. The total vacancy in the CBD declined to 5.2 M SF and the overall vacancy rate decreased to13%. All signs indicated that the CBD would close the year on a very positive note and officially put an end to the down cycle that has prohibited the CBD from significant growth. Then two announcements shattered these hopes. First; FMC Corporation announced they would relocate 250,000 SF from Mellon Bank Center and join The University of Pennsylvania and kick off of Brandywines much anticipated Cira South project in University City. Weeks later, Sun Oil (Sunoco) announced they would exercise an early termination option and relocate 200,000 SF from Mellon Bank Center and relocate to the Pennsylvania suburbs. Dare we discuss the CBD's tax burdens? By some, this is not considered vacancy, because the vacancy will not occur until 2016 but the space is considered available today. Therefore, it is only prudent to report. The Philadelphia Central Business District ended 2013 on a very low note with 5.7 M SF available, and the vacancy rate in the CBD was driven to 14.2%

Transaction highlights in the Fourth Quarter were limited to Price Water House Cooper's decision to consolidate within Two Commerce Square and lease 190,000 SF well into the next decade.

No tenants with sizable leases (100,000+ SF) exist.

Statistically, rental rates remained flat with Trophy Class Buildings at $35 SF, $27.00 SF for Class A space, $23.00 SF for Class B space, and $19.00 SF for Class C space. The asking rates are the weighted average of the published rate, from all vacant spaces per building class.

Market Street West has some very large vacancy to fill. Low vacancy was one of three components (reduction of inventory, strong inbound demand) driving rental rates. Reit Management & Research (formerly HRPT) will aggressively peruse tenants of all sizes, especially Class A Tenants looking to upgrade their space. Until Mellon Bank Center stabilizes, other Class A Landlords will have to be very careful in how much of a premium they place on renewals and inevitably continue to aggressively pursue new transactions.

Chestnut/Walnut Street remains a very tight submarket. As such, existing tenants can expect to renew at a premium (20%) and concessions will be limited to minimal capital investments to existing suites. New tenants will not find the historically lower base rents that they once enjoyed, but can still extract enough capital to fund their build outs.

South Broad Street continues to enjoy healthy occupancy levels. Existing tenants can expect less concessions (free rent and landlord capital), and higher rental rates. New transactions to this submarket still command high concessions and aggressive base rental rates. The reason is simple; East Market Street is only a few blocks away and an upgrade to West Market Street is even closer.

Market Street East remains a ghost town. Tenants looking to relocate or remain East of Broad Street will enjoy Class B product with high vacancy and low rental rates. Landlords will continue to entice both existing and new tenants with plenty of concessions.

In summary, 2014 should be an interesting year. Absorption will be steady but minimal. On West Market Street most, if not all, of the corporate downsizing has occurred. The CBD's inventory has been stabilized with all of the condo conversions being accounted for. The CBD will pick up where it left off at the end of Q3, and slowly nurse its way back to healthy levels (10% vacancy) in 2014 and beyond.

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Ken Clyman Realty

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1650 Market Street 36th Floor Philadelphia, PA 19103 215.640.8800