3Q24

District of Columbia Office Market Overview

NEWMARK

Market Observations

Economy

- The region's labor market remains strong amid shifting macroeconomic conditions. August's 3.7% unemployment rate remains lower than the region's ten-year historical average of 3.9%, although it has risen 100 basis points quarter-over-quarter and year-over-year. Furthermore, the Washington DC metro's unemployment rate is 50 basis points lower than the national rate.
- Year-over-year, job gains were most pronounced in Education & Health, posting a gain of 2.2%. Furthermore, the Government sector also experienced notable job gains, increasing 0.4% year-over-year. The office-occupying industries of Information, Financial Activities, and Professional and Business Services experienced job losses over the past year, however, helping to account for continued limited demand for office space.
- While some office-using sectors experienced a decline in employment over the past year, jobs in the office-using sectors remain at a level that is 2.6% higher than five years ago—just prior to the pandemic—and 6.2% higher than the pandemic-induced employment trough in May 2020.

Major Transactions

- Office investment sales continue to lag in pricing per square foot as well as total transaction volume with the average PSF of $407 down from the recent peak of $645 PSF in 1Q23 and total transaction volume of $2.0 billion, down from the recent peak of $3.8 billion in 1Q22. However, owner-user sales and conversion opportunities are propping up a lot of demand in Washington, D.C. capital markets.
- The most notable sale of the quarter was 2000 K Street. The 233,000-square-foot, 12-story office building was sold by Tishman Speyer to Spear Street Capital for $140.2 M, or $600.96 PSF. The Class A building was originally built in 1986 and went through an extensive renovation in 2017. It was 91.1% leased at the time of sale, with notable tenants including AECOM, Ankura Consulting Group, DCI Group, and Transwestern among others.

Leasing Market Fundamentals

- The District of Columbia experienced 107,571 SF of negative net absorption during Q3 2024. The vacancy rate declined 10 basis points quarter-over-quarter at 20.2%, although increased 100 basis points year-over-year.
- The District of Columbia's development pipeline remains historically low, with no deliveries during the quarter. The sole property under construction in the district is 600 Fifth, a 400,000-square-foot office building in the East End.
- Overall, asking rents have decreased slightly during 2024. Class A rents were the cause of this, as they have declined 2.4% year-to-date, while Class B rents have increased 1.6%. The longer-term trend, however, shows that both Class A and Class B rents have remained relatively flat since 2019. The rent spread between direct and sublet deals has settled around $10, after having spiked in 2020 and 2021 when it hovered around $12 to $14.

Outlook

- 2024 year-to-date has seen a stark uptick in institutional investors coming back to the DC office market, while unconventional investors have begun to show interest as well. This coincides with an increase in transaction volume of distressed assets selling at an average of 43% of their last sale price in 2024. This presents new owners with the opportunity to acquire poor-performing assets significantly lower than replacement cost with the intention of renovation or conversion.
- Colleges and Universities continue to be a bright spot in the market as they are major participants in both leasing and purchasing office space in the District.
- DC has one of the lowest sublease availability rates among all the gateway markets, helping to temper the risk of oversupply.

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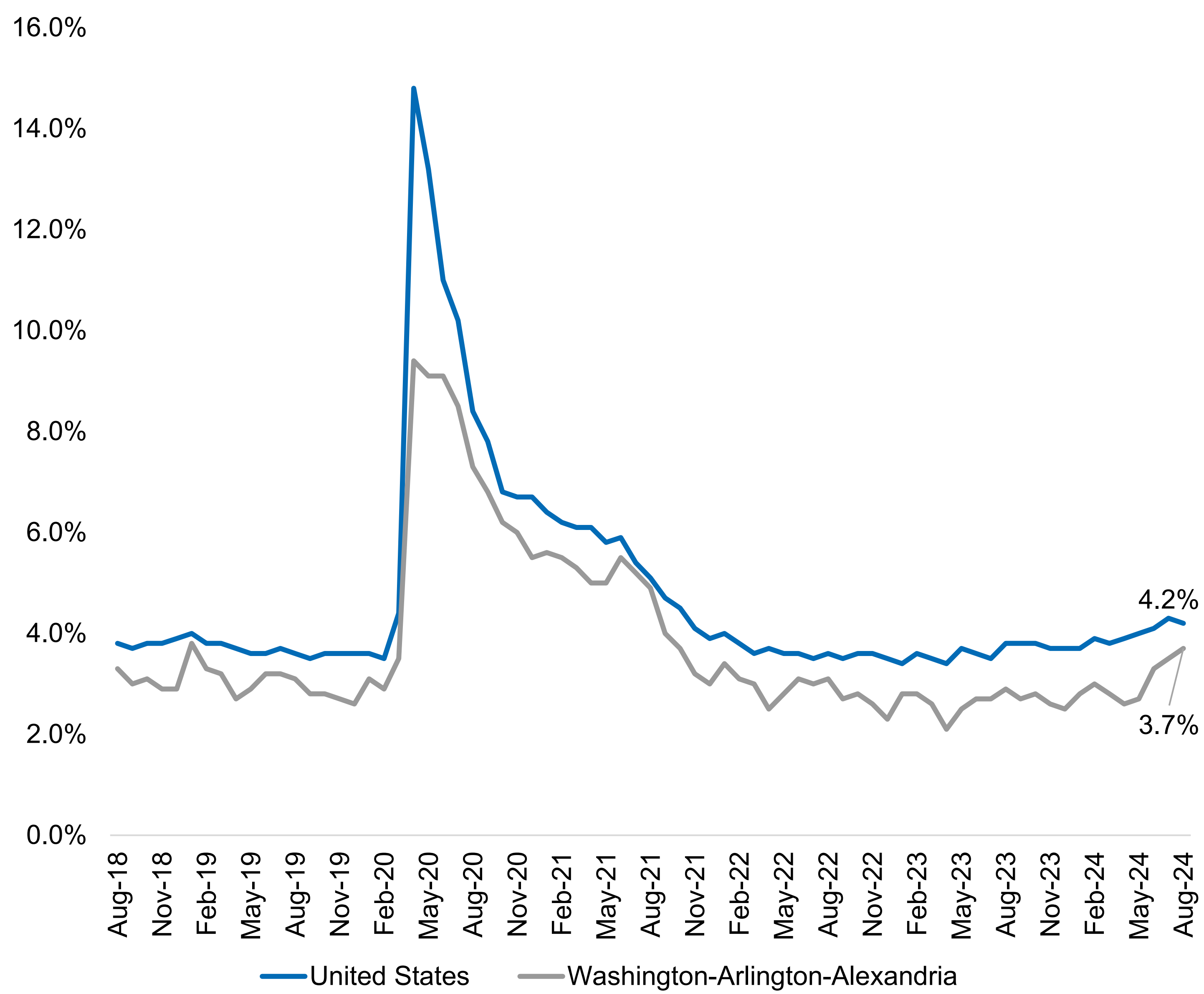
Economy

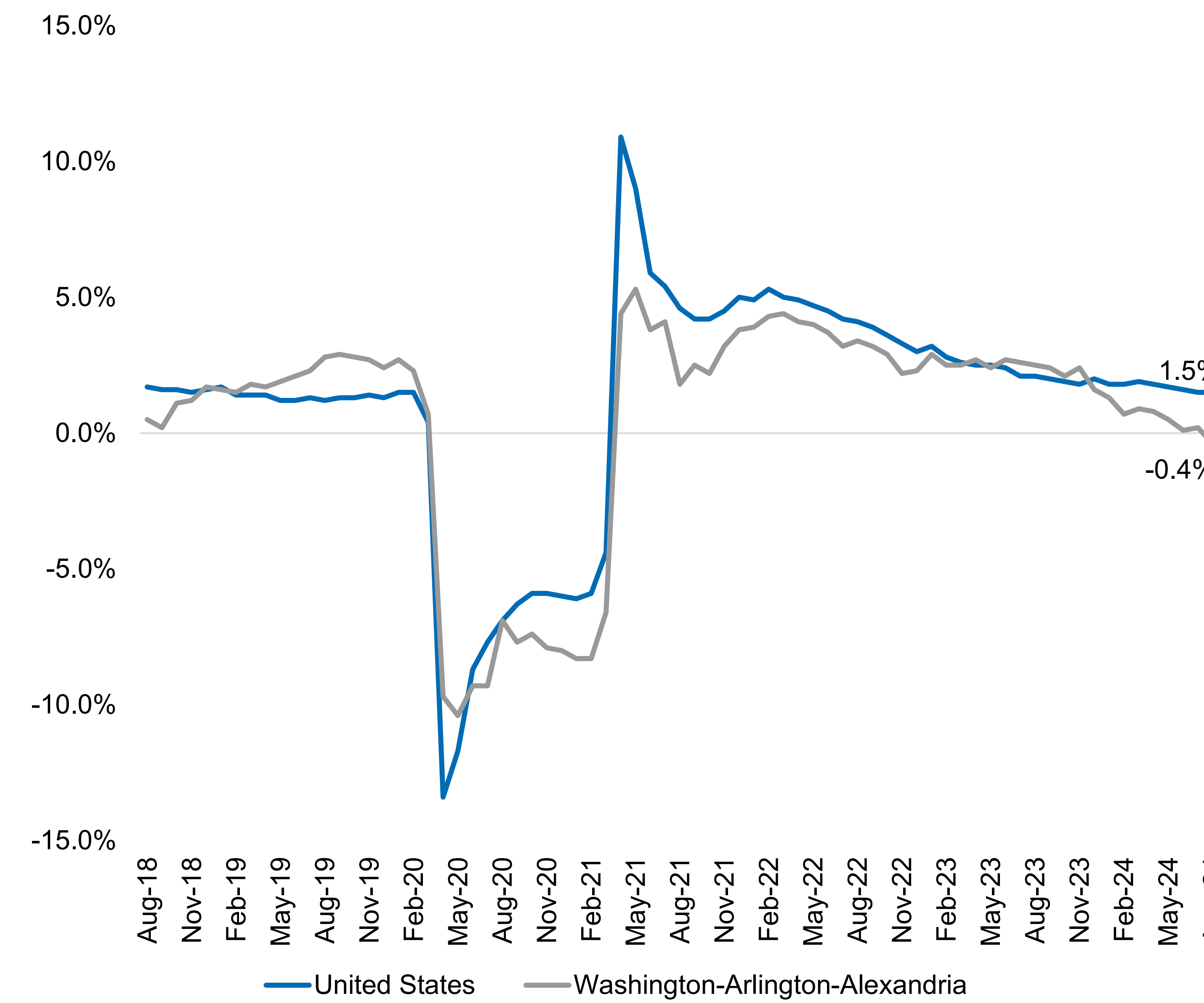
Metro Employment Job Growth Enters Negative Territory

The region's labor market is very tight, with unemployment 50 basis points below the national average. However, it is showing signs of loosening as the spread between the regional and national labor market decreased 70 basis points quarter-over-quarter. National job growth has begun to slow, but nonetheless remains positive. Regional job growth has dipped to -0.4% year-over-year.

Unemployment Rate, Seasonally Adjusted



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

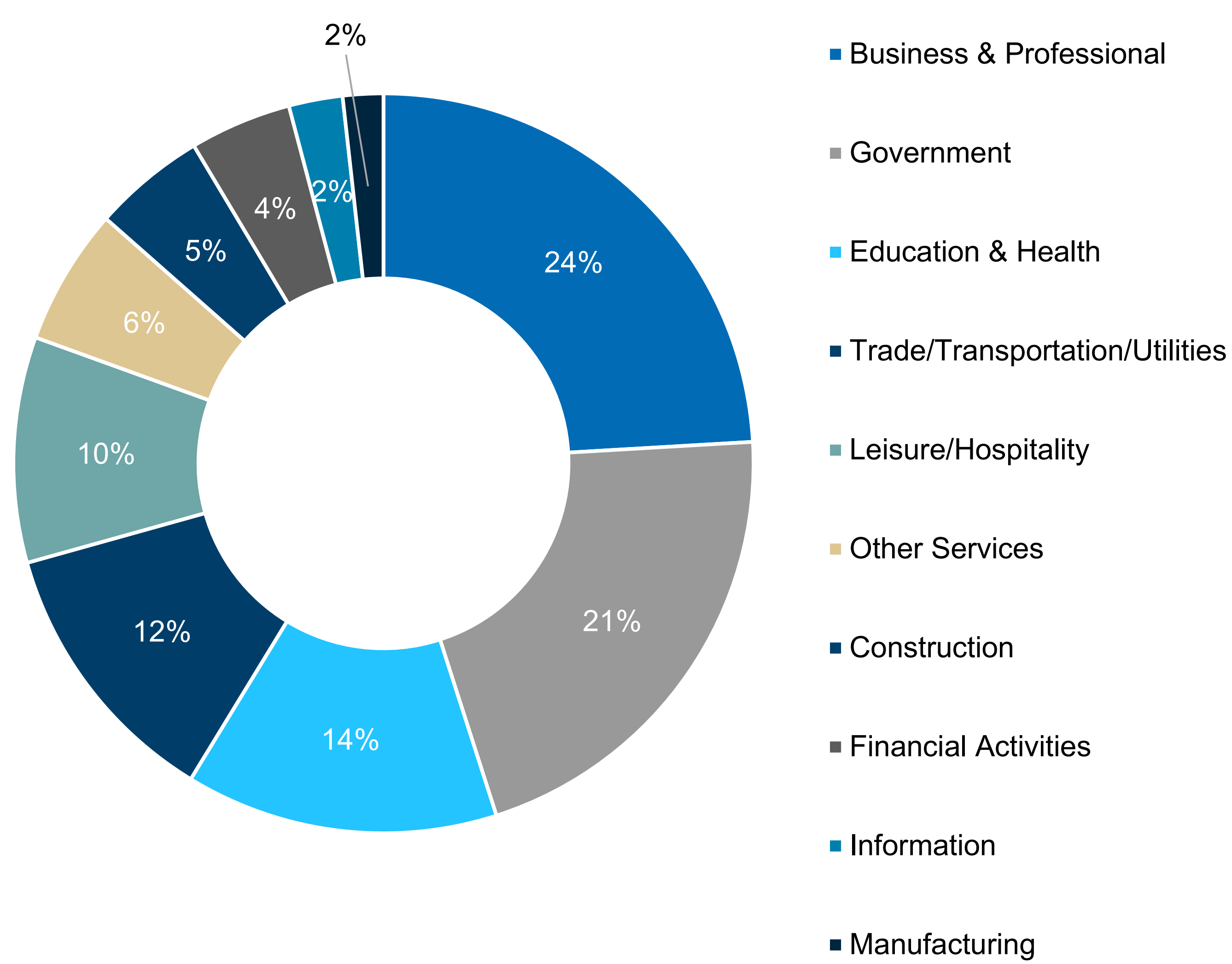


Source: U.S. Bureau of Labor Statistics, Washington-Arlington-Alexandria

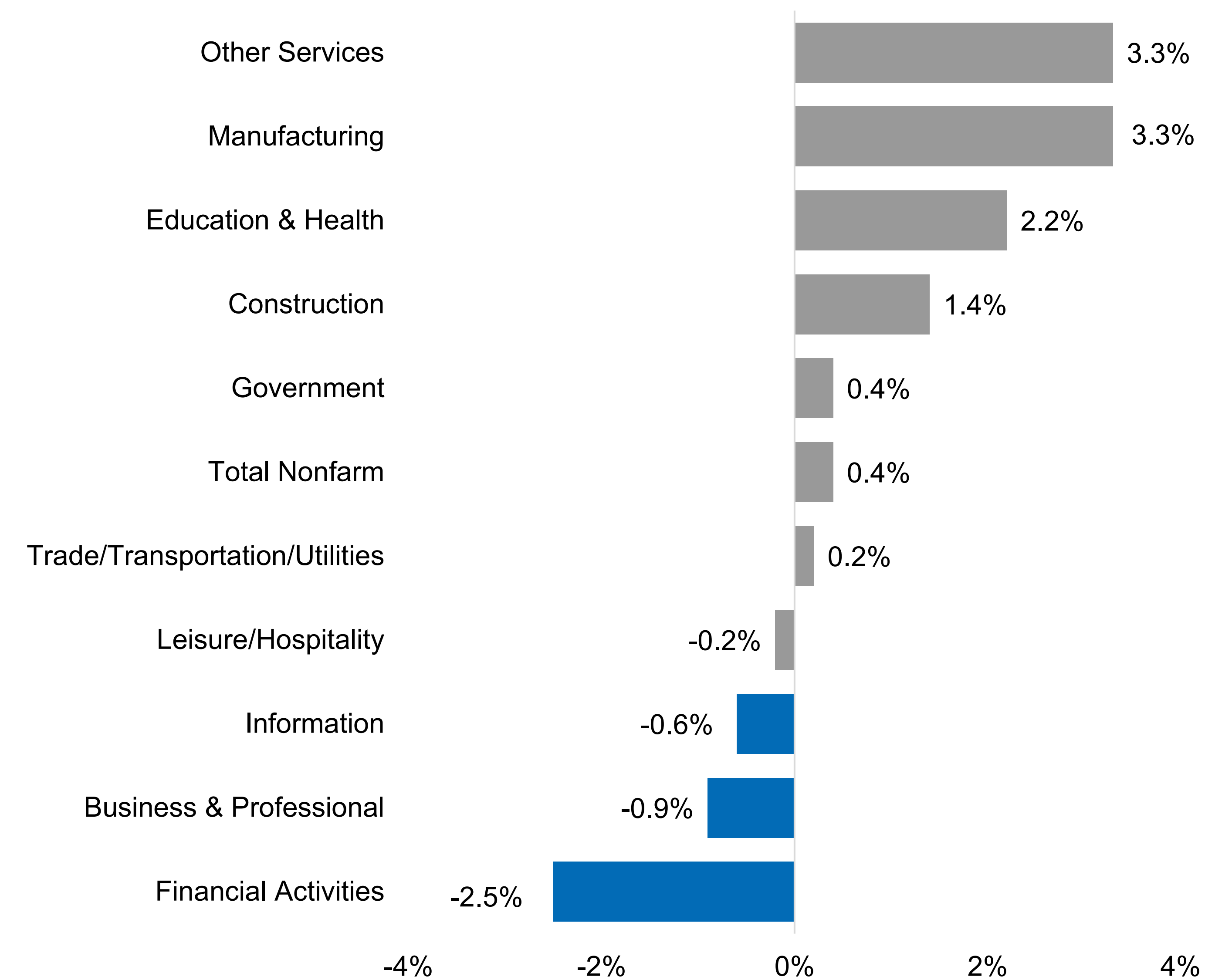
Job Growth Driven in Large Part by Education, Health, and Government

Education, Health, and Government propped up job growth in the region, leading to total nonfarm employment growth of 0.4%. Despite this, office-occupying industries of Information, Financial Activities, and Professional and Business Services experienced some job losses over the past year, contributing to declining demand for office space.

Employment by Industry, August 2024



Employment Growth by Industry, 12-Month % Change, August 2024

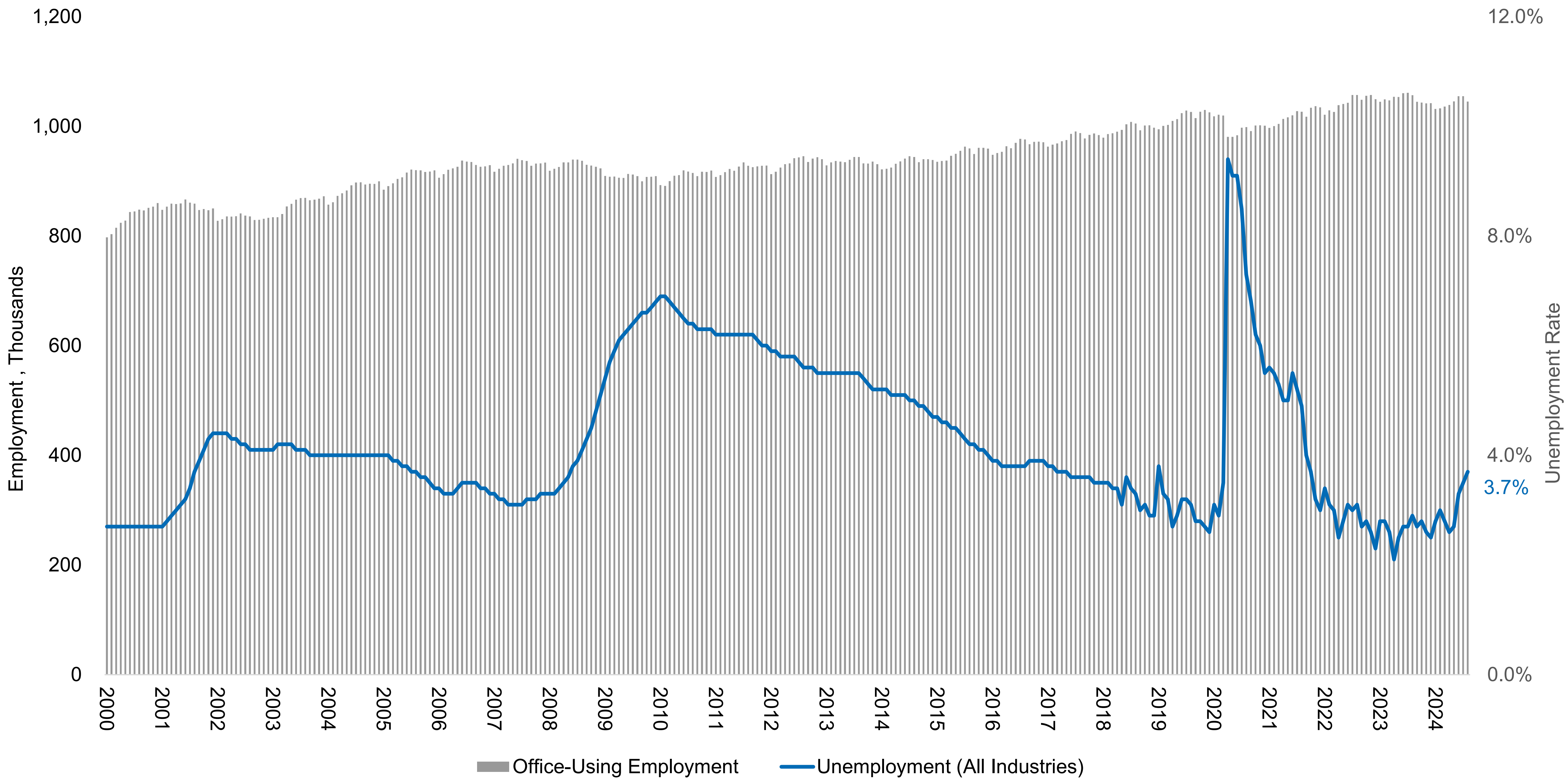


Source: U.S. Bureau of Labor Statistics, Washington-Arlington-Alexandria
Note: August 2024 data is preliminary.
*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.

Overall Office-Using Employment Has Rebounded

The number of office jobs has rebounded and now exceeds pre-pandemic levels. Office-using jobs in the region are currently 2.6% higher than four years ago—just before the pandemic—and 6.2% higher than the pandemic-induced employment trough in May 2020.

Office-Using Employment* and Unemployment Across All Industries



Source: U.S. Bureau of Labor Statistics, Washington-Alexandria-Arlington
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*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.

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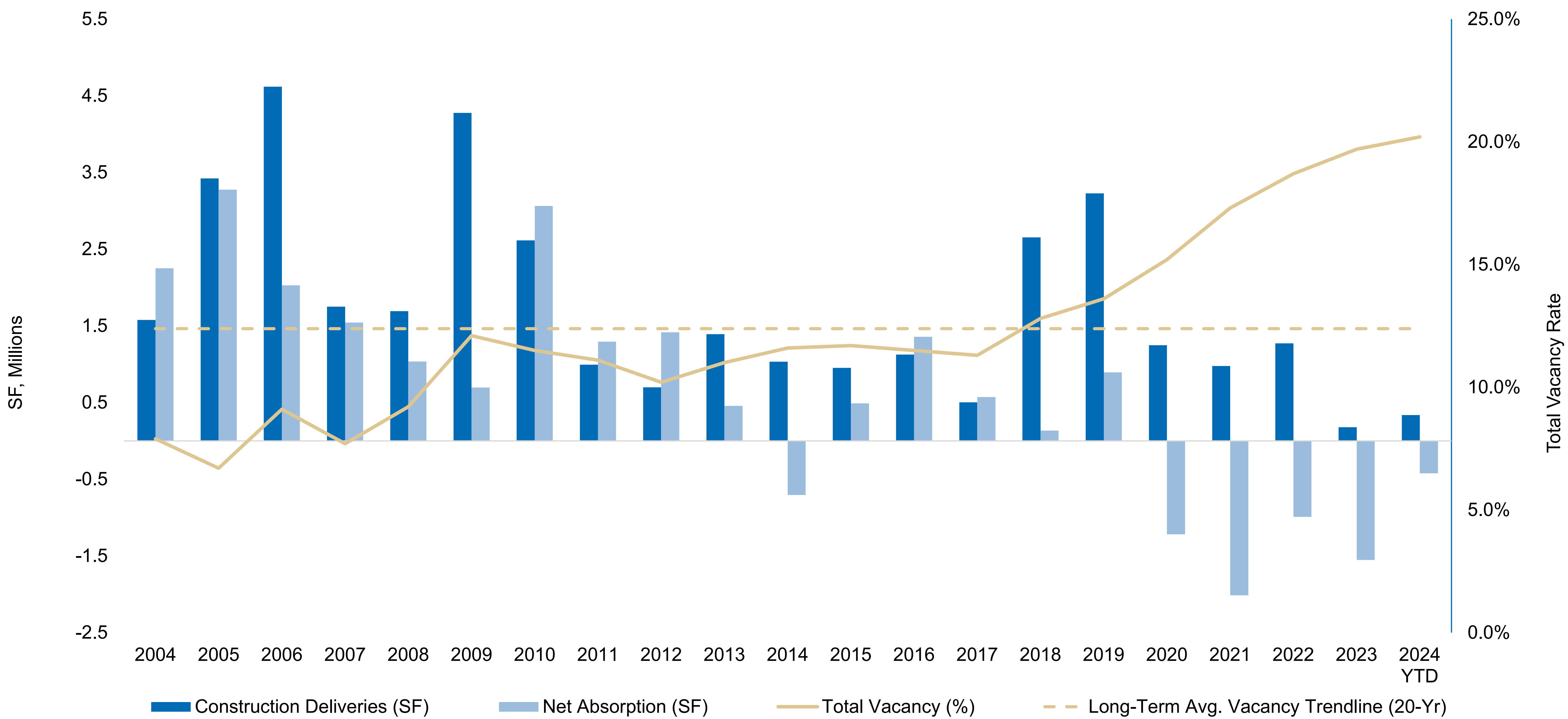
Leasing Market Fundamentals

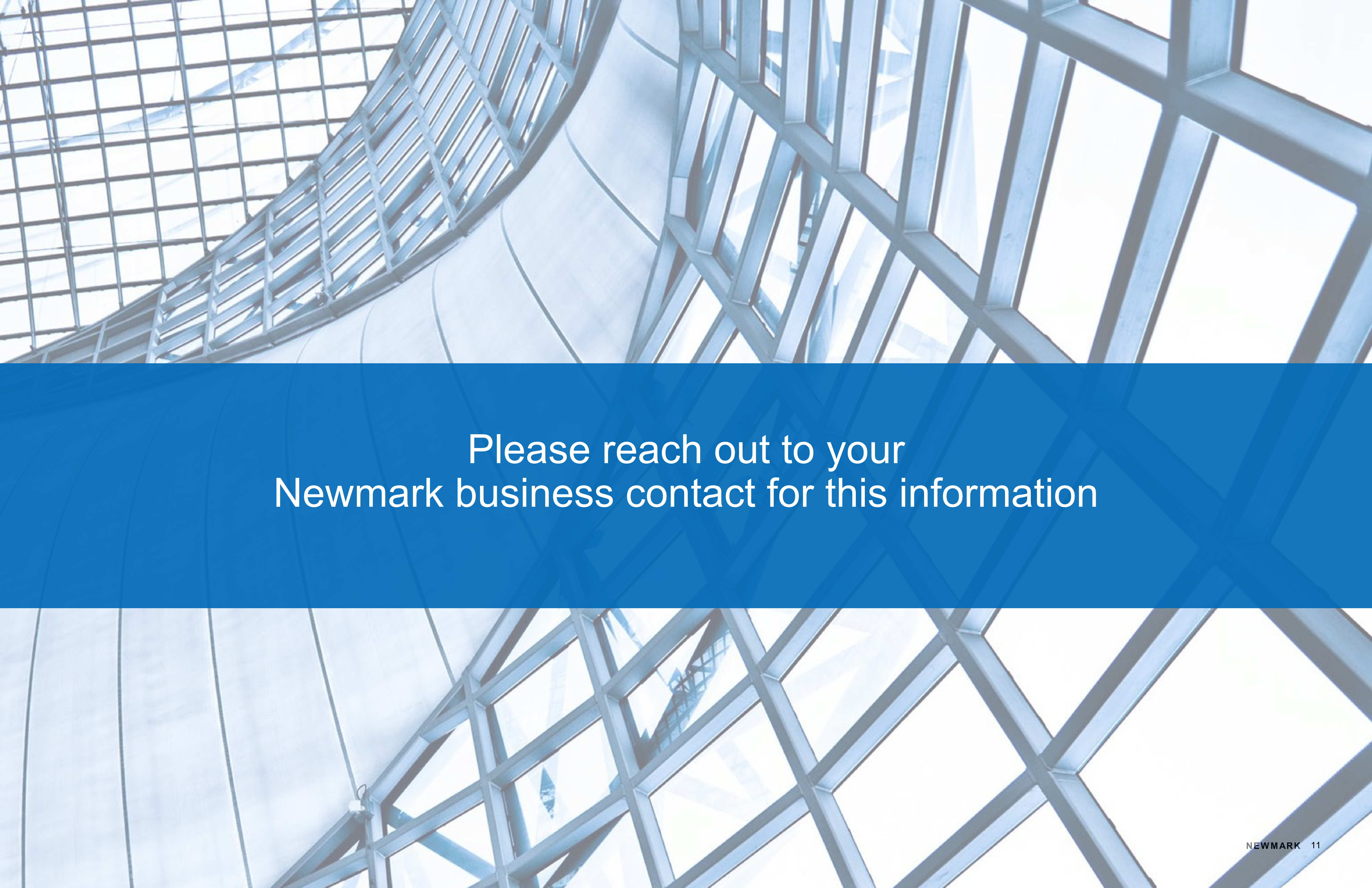
Vacancy Continues to Expand at a Decelerating Rate during 2024

The District of Columbia's vacancy rate ended Q3 2024 at 20.2%, a slight expansion of 10 bps quarter-over-quarter and 100 bps year-over-year. After the vacancy rate expanded at its fastest rate of 210 bps during 2021, the market has experienced a deceleration of expansion each year since. The market has seen a slowdown in deliveries during 2024, experiencing only 336,000 SF of deliveries so far during the year. This is much less than the market's average of 1.8 million square feet of annual deliveries over the past 20 years.

Historical Construction Deliveries, Net Absorption, and Vacancy



Source: Newmark Research



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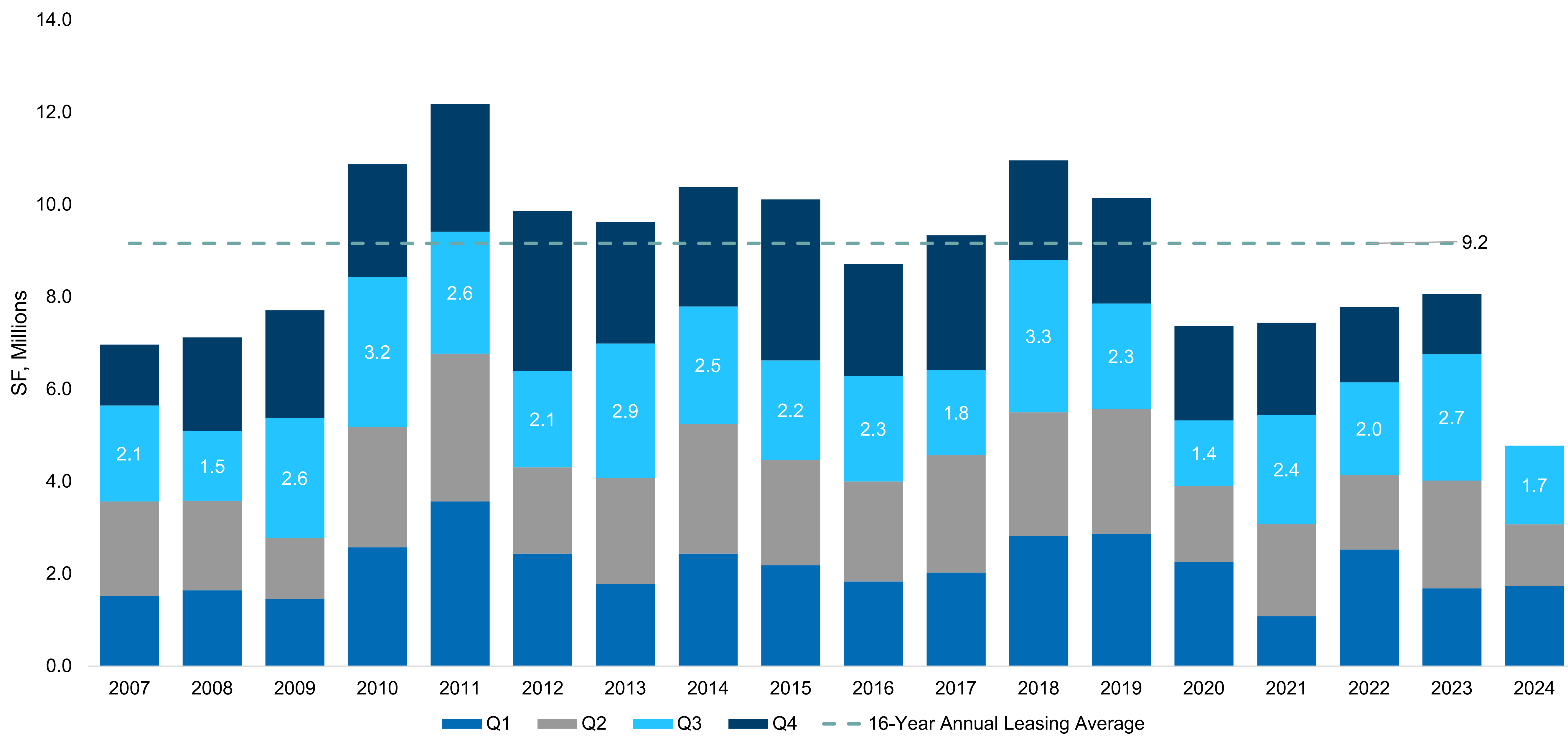
Leasing Activity Has Slowed

Leasing activity has slowed since 2020, although it picked up the pace slightly during 2023. During Q3 2024, the market saw 1.7 MSF of leasing activity, significantly lower than the same period in 2023 and on track to be well below the annual average of 9.2 MSF. Lease Renewals are the primary drivers for leasing activity for larger spaces, while smaller spec suites are the primary drivers for new leases.

Total Leasing Activity (msf)

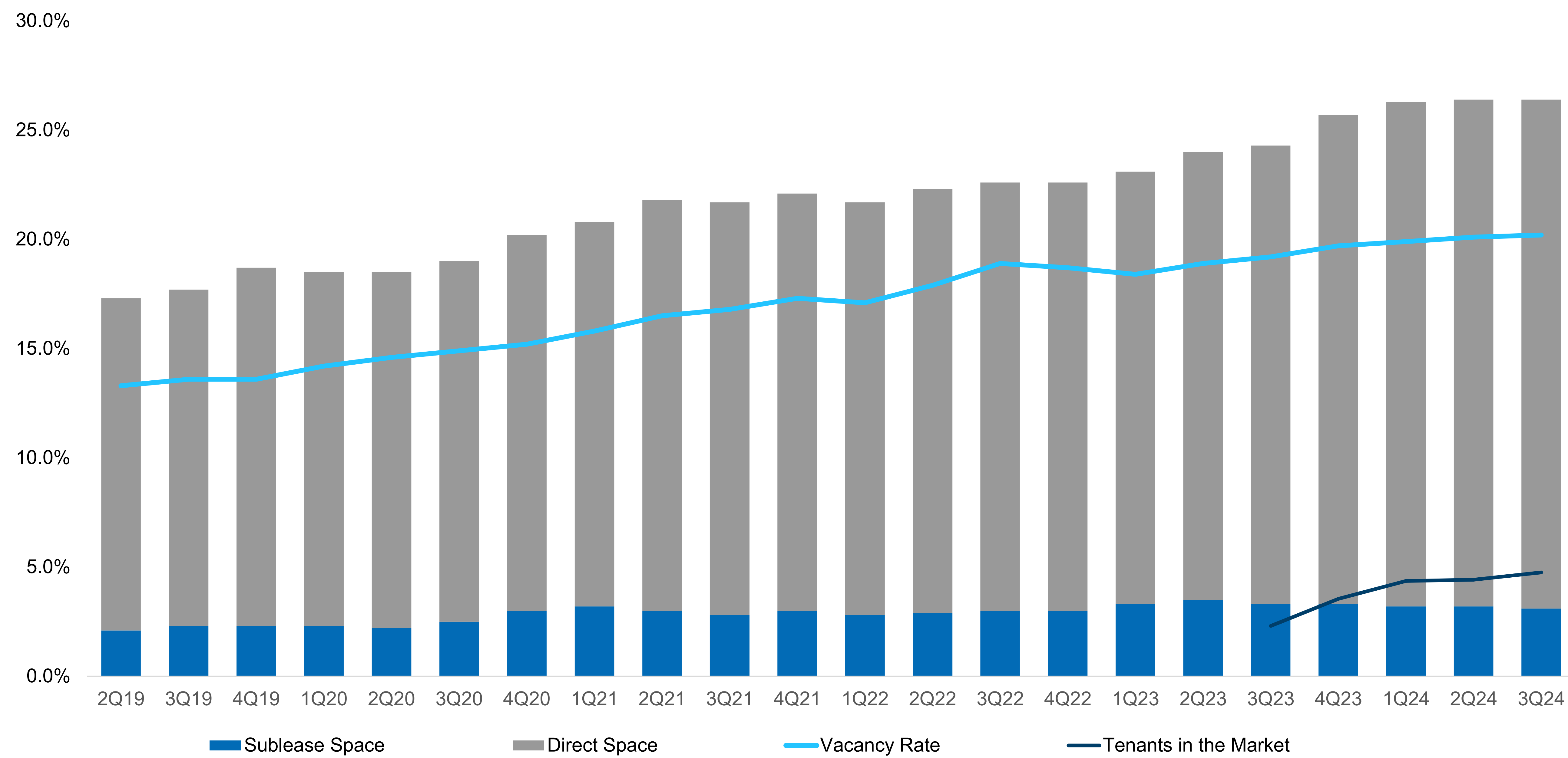


Source: Newmark Research, CoStar

Availability Continues to Increase Slightly, Although Tenant Demand Has Picked Up

Available office space sits near historical highs, both in terms of direct and sublease space. Over the past five years, the direct availability rate has averaged 19.4% while the sublease availability rate has averaged 2.8%. The Q3 2024 availability rates of 23.3% for direct space and 3.1% for sublease space are well above the long-term average.

Available Space and Tenant Demand as Percent of Overall Market

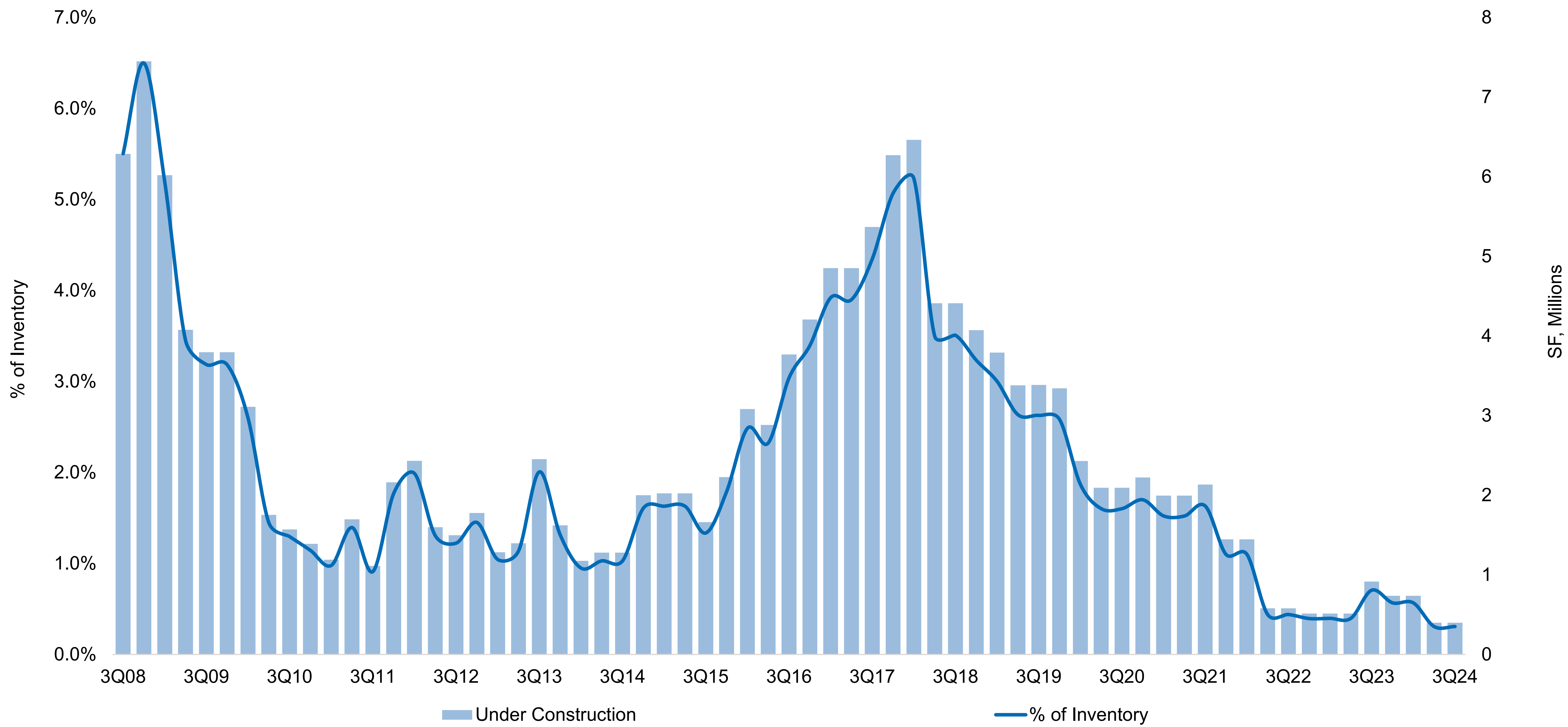


Source: Newmark Research

Slowing Office Construction Pipeline Will Help Ease Rising Vacancy

The District of Columbia's development pipeline remains historically low, with no deliveries in Q3 2024. There is one project under construction totaling 400,000 SF. This development, 600 Fifth, is a 400,000-square-foot office building located in the East End. It has an expected delivery of Q1 2026 and is 54% preleased. With demand continuing to moderate, limited new supply and strong pre-leasing will help ease rising vacancy.

Office Under Construction and % of Inventory

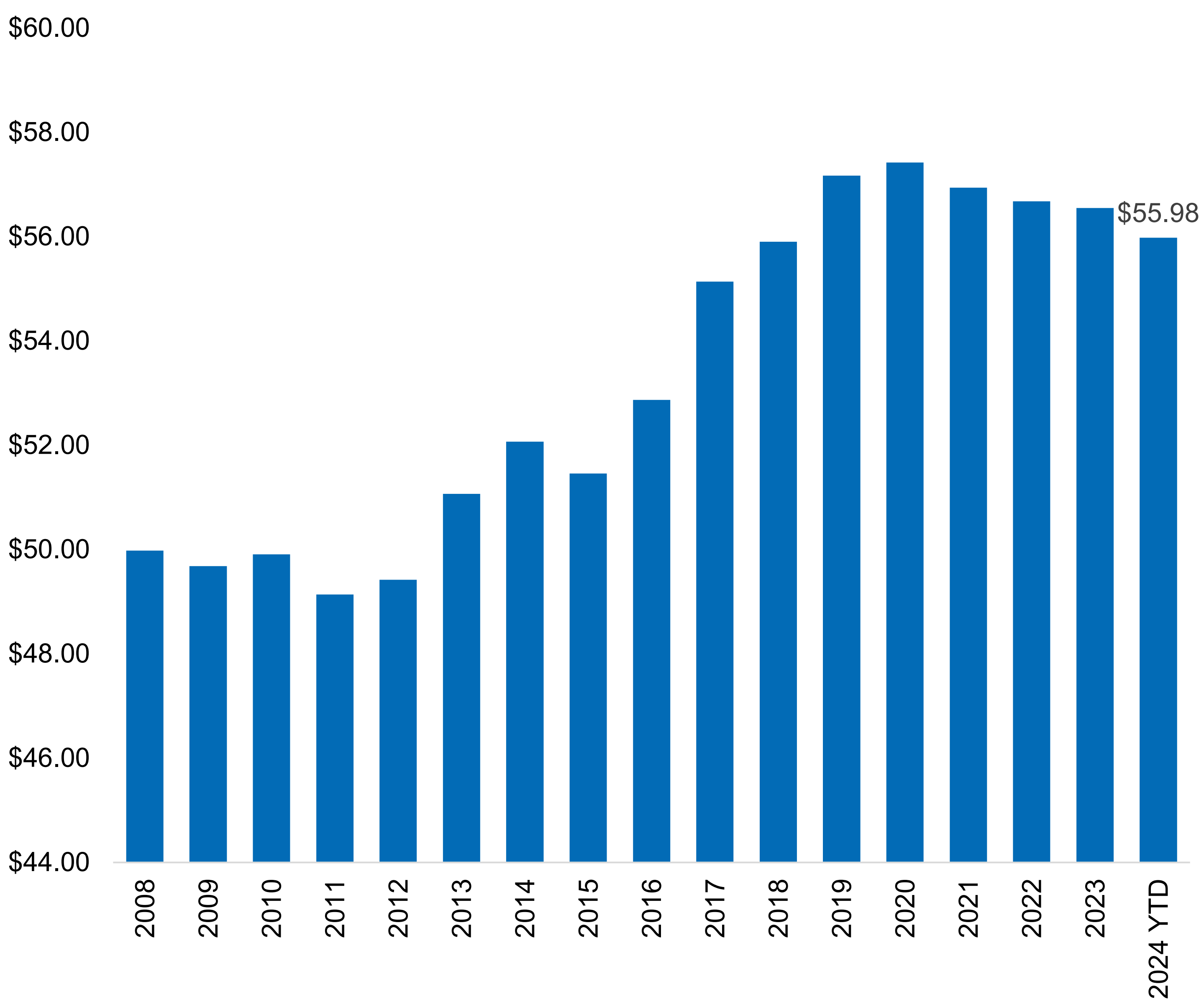


Source: Newmark Research, CoStar

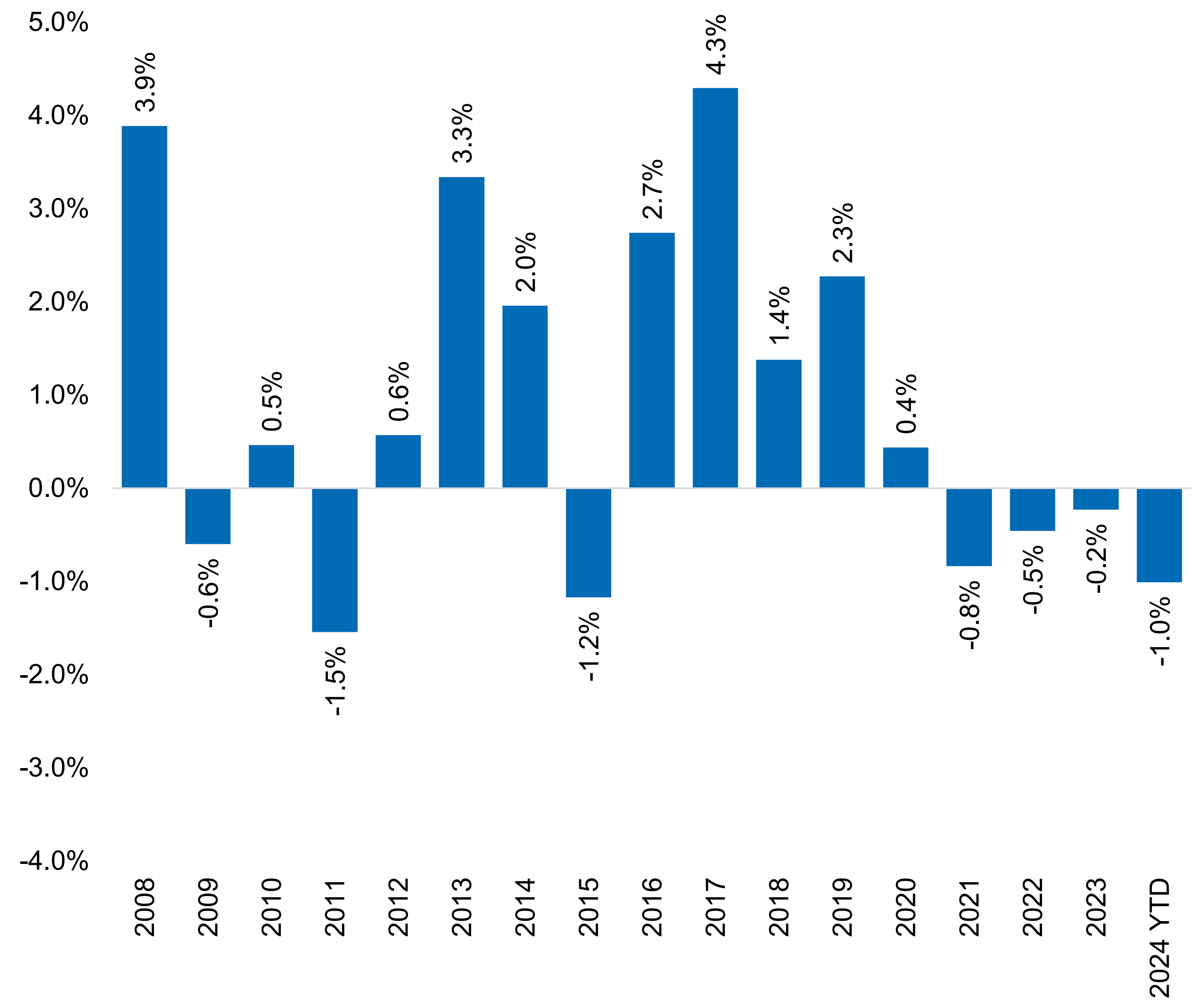
District of Columbia Asking Rents Experiencing Modest Decline

Asking rental rates have been decreasing year-over-year since 2021. The District of Columbia has not experienced sustained annual losses in asking rents since the Global Financial Crisis, but even then, it took two years for rates to noticeably drop in 2011. Continued limited demand—and in some cases, a lack of capital for concessions—has placed downward pressure on asking rents in the District.

Office Average Asking Rent, $/SF, FS



Year-over-Year Asking Rent Growth Rate

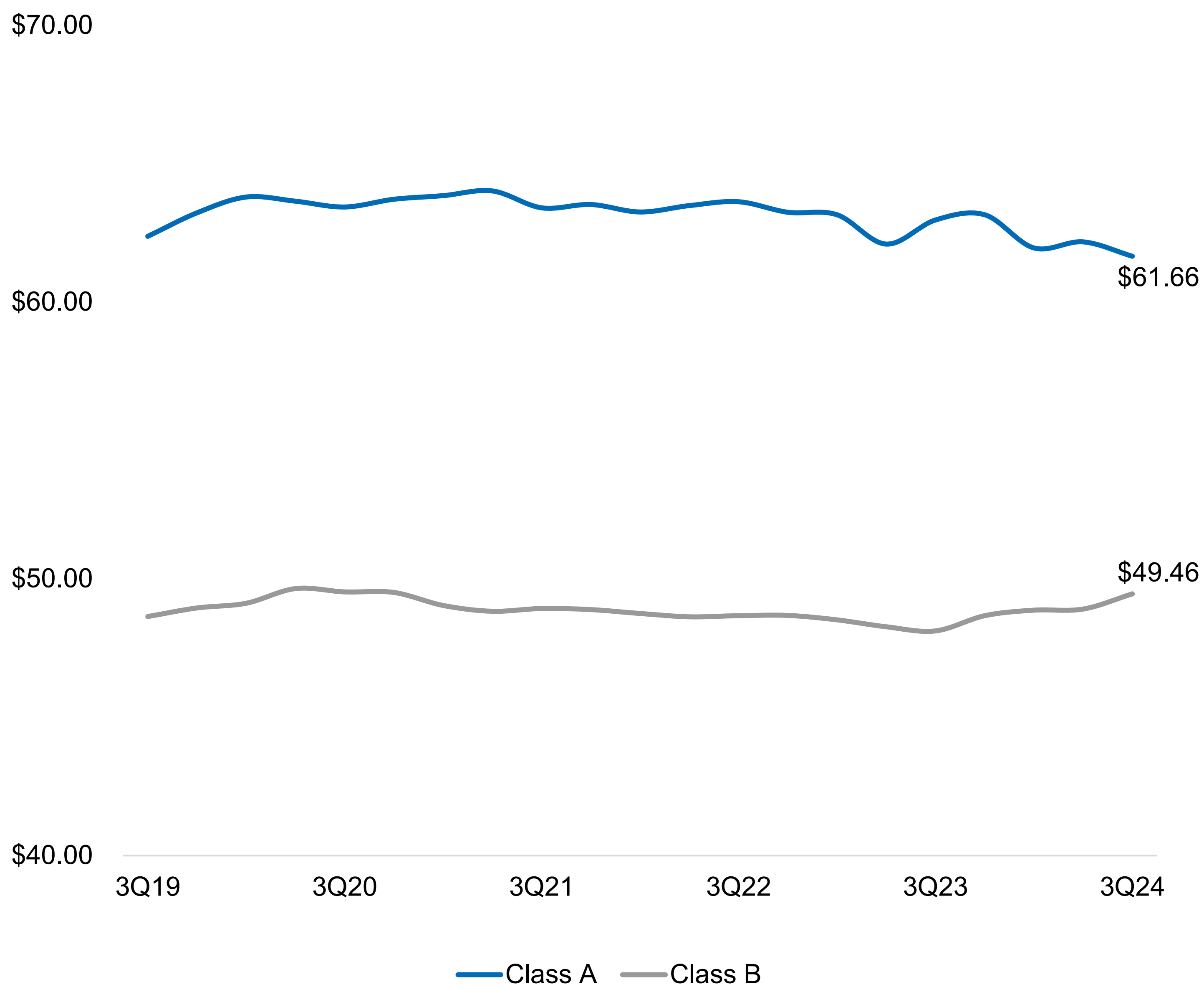


Source: Newmark Research

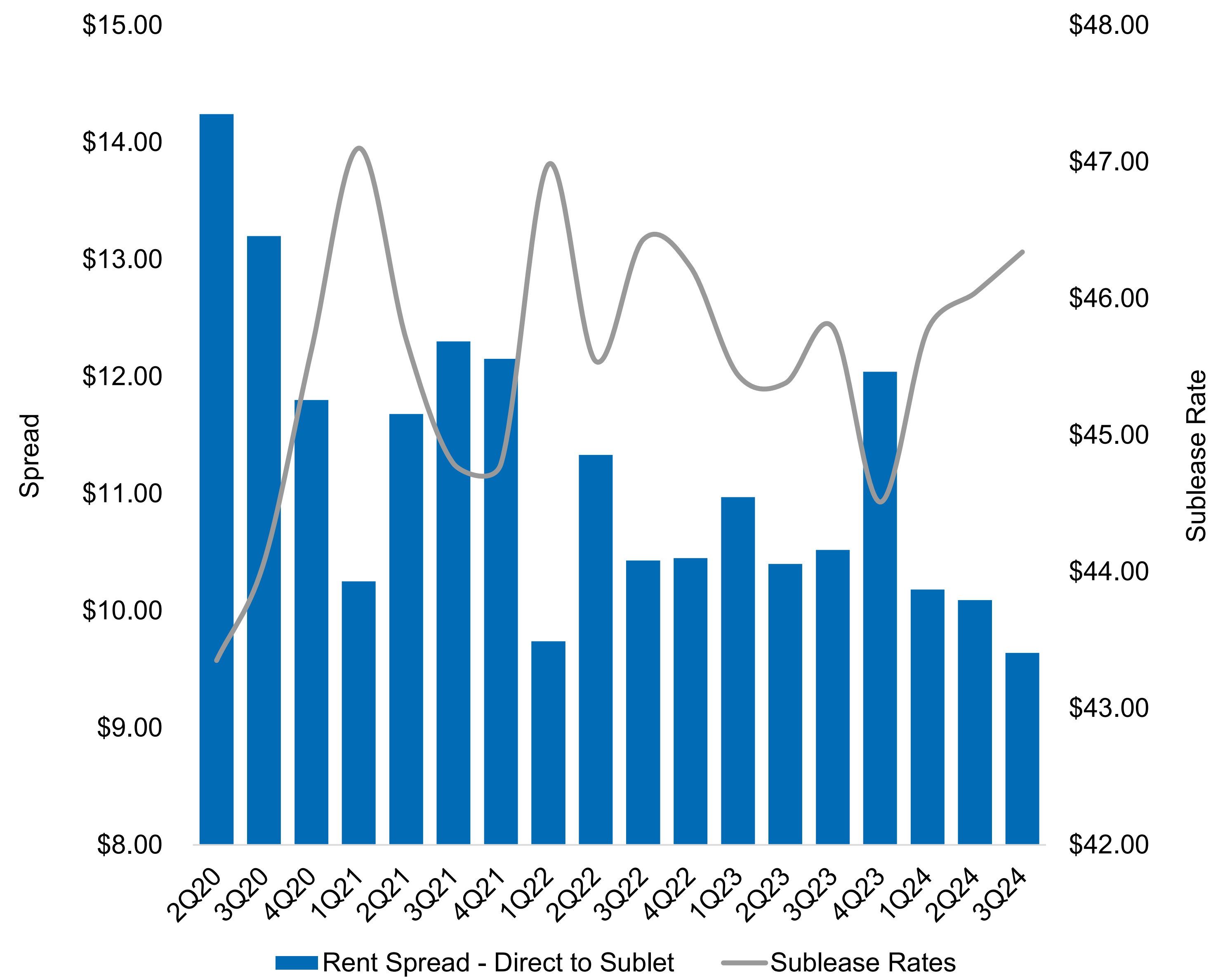
Asking Rents Show Declines So Far in 2024

Overall, asking rents have decreased slightly during 2024. Class A rents were the cause of this, as they have declined 2.4% year-to-date, while Class B rents have increased 1.6%. Over the last five years, both Class A and Class B rents have remained relatively flat since 2019. The rent spread between direct and sublet deals has settled around $10, after having spiked in 2020 and 2021 when it hovered around $12 to $14.

Class A and Class B Asking Rents



Sublease Rates

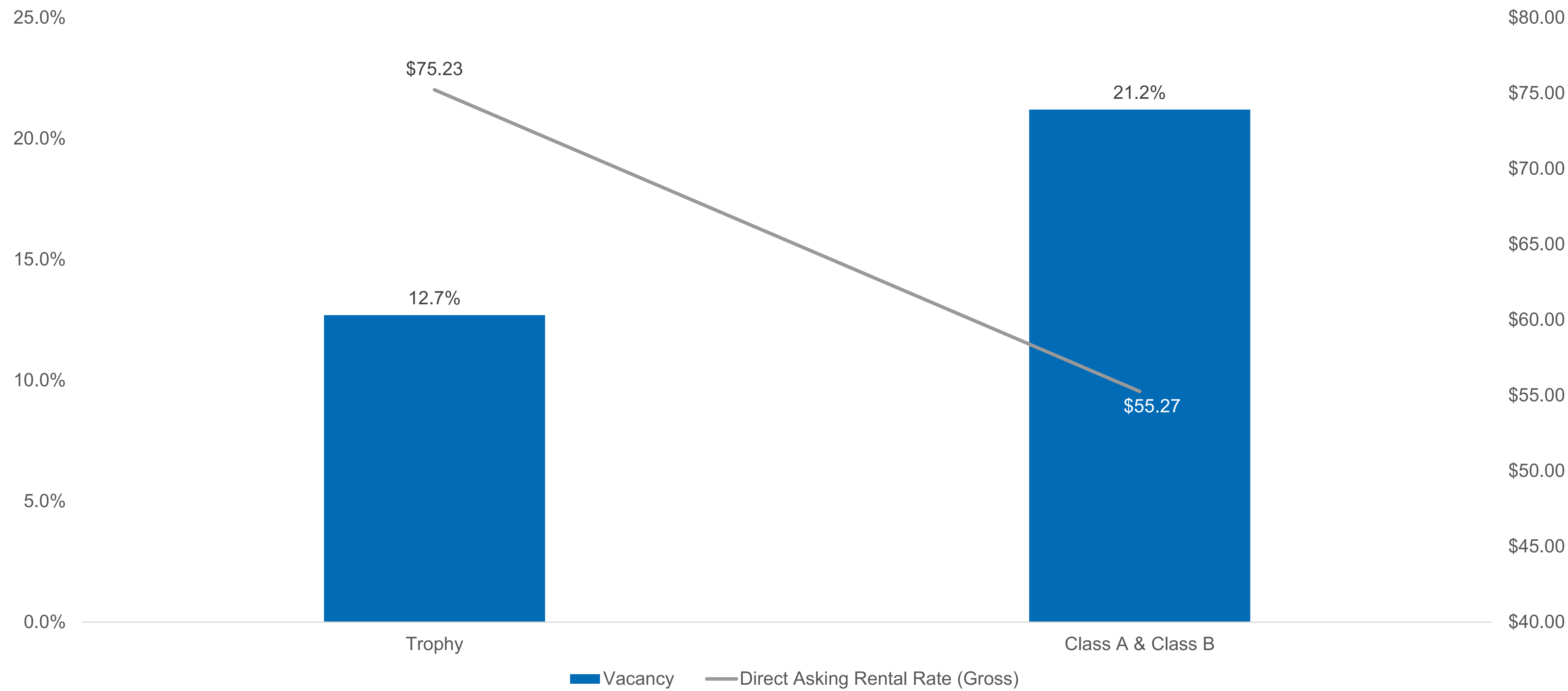


Source: Newmark Research

District of Columbia Trophy Office Outperforms Class A & Class B

The District of Columbia, like many other office markets, is experiencing a bifurcation of performance across classes. “Flight to quality” is a pervasive trend and is especially observed among Trophy assets.

Vacancy and Rental Rates By Office Class, Q3 2024



Source: Newmark Research.

Leasing Activity Dominated by New Deals

Despite negative absorption, leasing activity continues, albeit at a slower pace. Major third-quarter transactions were comprised of mainly new deals, providing much-needed optimism for the DC office market. Furthermore, most of the activity occurred within the CBD submarket, which contained the two top transactions totaling almost 700,000 SF of space.

Notable 3Q24 Lease Transactions

Tenant	Building(s)	Submarket	Type	Square Feet
Voice of America	1875 Pennsylvania Ave, NW	CBD	Direct Lease	350,000
Fannie Mae	1100 15th Street, NW	CBD	Lease Renewal/Contraction	340,000
Court Services & Offender Supervision Agency	501 3rd Street, NW	Capitol Hill	Direct Lease	198,561
D.C. Department of General Services	899 N Capitol Street, NW	NoMa	Direct Lease	169,336
U.S. Department of Treasury	1575 Eye Street, NW	East End	Direct Lease	65,000

Source: Newmark Research

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Submarket Stats

District of Columbia Market Overview

Market Statistics By Class

	Total Inventory (SF)	Overall Vacancy	Overall Availability	3Q 2024 Absorption (SF)	YTD Absorption (SF)	Quarter Deliveries (SF)	YTD Deliveries (SF)	Under Construction (SF)	Asking Rent (Price/SF)
Washington D.C.	**130,095,694**	**20.2%**	**26.3%**	**-107,571**	**-422,917**	**0**	**336,289**	**399,617**	**$55.98**
Class A	81,127,217	18.3%	24.5%	-167,588	-244,396	0	336,289	399,617	$61.66
Class B	44,863,040	24.3%	30.7%	112,981	-79,074	0	0	0	$49.46
Class C	4,105,437	14.2%	15.1%	-52,964	-99,447	0	0	0	$40.17

Submarket Statistics – All Classes

	Total Inventory (SF)	Overall Vacancy	Overall Availability	3Q 2024 Absorption (SF)	YTD Absorption (SF)	Quarter Deliveries (SF)	YTD Deliveries (SF)	Under Construction (SF)	Asking Rent (Price/SF)
Capitol Hill	5,393,778	23.0%	28.4%	-26,099	-55,437	0	0	0	$62.34
Capitol Riverfront	4,978,946	15.6%	22.8%	8,963	16,450	0	0	0	$56.39
CBD	40,535,177	22.3%	27.7%	89,536	-218,055	0	336,289	0	$55.87
East End	42,436,149	22.2%	31.3%	-28,360	-46,135	0	0	399,617	$58.48
Georgetown	2,782,973	23.5%	31.7%	19,787	-27,483	0	0	0	$54.26
NoMa	11,717,348	13.6%	19.4%	-235,464	-195,484	0	0	0	$47.17
Southwest	13,005,941	15.7%	16.0%	63,598	-43,902	0	0	0	$52.09
Uptown	5,245,048	15.3%	18.3%	-5,397	125,555	0	0	0	$44.40
West End	4,000,334	17.9%	22.0%	5,865	21,574	0	0	0	$58.35

Source: Newmark Research

For more information:

Carolyn Bates
Director
Mid-Atlantic Research
carolyn.bates@nmrk.com

Chad Braden
Senior Research Analyst
Mid-Atlantic Research
chad.braden@nmrk.com

Danny Calo
Senior Research Analyst
Mid-Atlantic Research
Danny.Calo@nmrk.com

District of Columbia
1899 Pennsylvania Avenue, NW
Suite 300
Washington, DC 20006
t 202-331-7000

New York Headquarters
125 Park Ave.
New York, NY 10017
t 212-372-2000

nmrk.com

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