

# Savills Studley Report Philadelphia office sector

Q2 2017



## SUMMARY

### Market Highlights

#### LEASING SPIKES

Tenants leased 2.3 msf in the Philadelphia region during the second quarter, an increase of nearly 50.0% from the first quarter, and nearly 15.0% above the market's long-term average. Tenants have leased 7.5 msf in the last four quarters, falling short of the long-term average of 8.0 msf by 7.6%.

#### AVAILABILITY INCHES HIGHER

Center City's overall availability rate posted a modest 20 basis point increase from 13.6% to 13.8% – the second straight quarter with a slight jump. The Class A availability rate dipped from 13.3% to 13.1%, though.

#### RENT PUSHES HIGHER

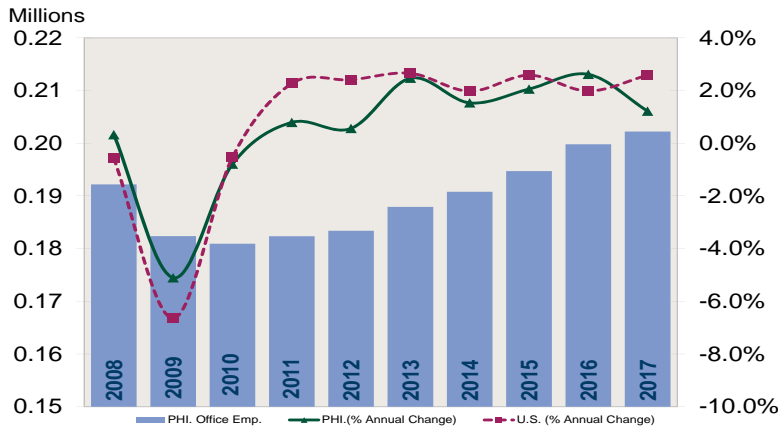
Overall asking rent in Center City rose by 1.9% to \$31.21, and has increased by 5.5% year-on-year. Overall asking rent in Suburban Philadelphia (\$26.89) jumped by 4.5% during the quarter.

#### SALES DECLINE

Year-to-date office property sales totaled \$752 million, a significant decrease of 46.2% from \$1.4 billion that changed hands in the first five months of 2016.

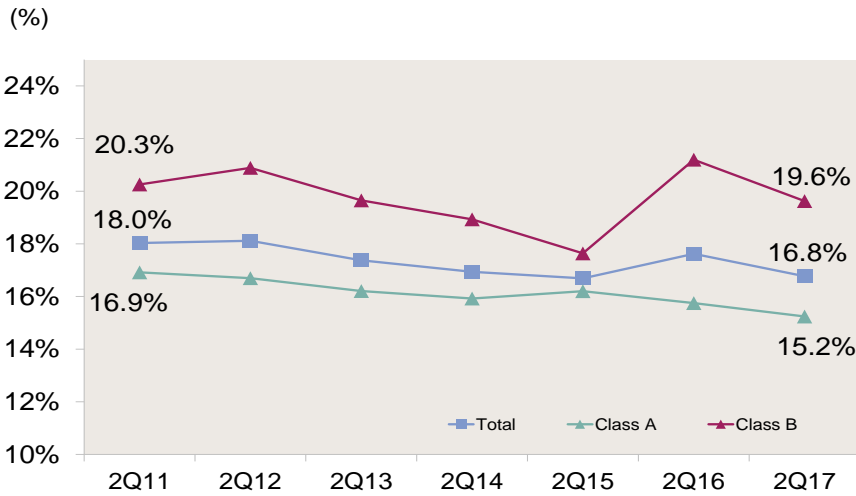
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*"Landlords trying to lease the next set of new projects in Center City are struggling to maintain their initial momentum. Some tenants are displaying a bit of price resistance- by next year tenants may have other options due to potential lease rollovers and a recent flurry of space consolidations."*  
 Greg Soffian,  
 Executive Vice President  
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## Office-Using Employment Trends

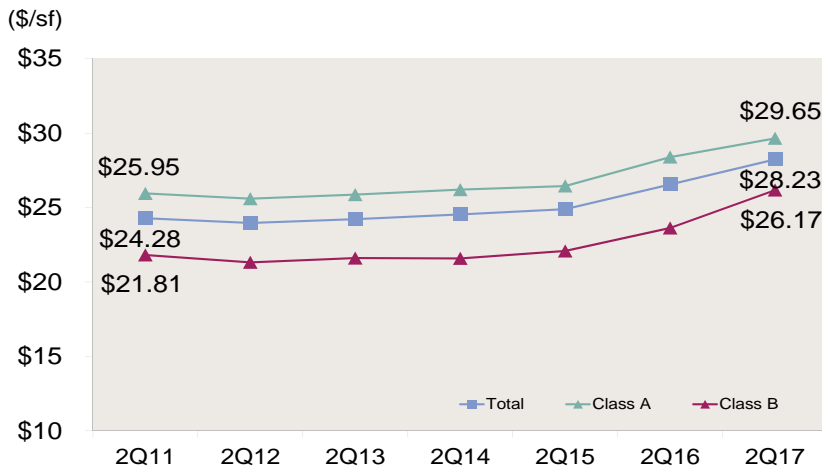


Source: Bureau of Labor Statistics

## Availability Rate Trends



## Asking Rent Trends



## State of the Market

Philadelphia's office market has maintained a relatively steady pace in the last couple of years. Tenant demand has been strong enough to sustain activity in both Center City and prime suburban locations such as Main Line/Conshohocken. A bit of a standoff is emerging, though – between landlords trying to pre-lease costly space in the next set of new projects planned for 2018 and beyond – and tenants who are displaying price resistance. The clock is ticking for some of these owners – a flurry of significant lease expirations and recent rash of substantial space consolidations will create additional and more affordable opportunities for tenants by 2018.

Leasing volume rebounded in the second quarter, due largely to a handful of significant leases concentrated in West Market and Wilmington. In West Market, Duane Morris completed a 257,021sf lease at 30 S 17th Street. Also, Brandywine Global took 66,501 sf at 1735 Market Street and Jazz Pharma leased 46,000 sf at nearby 2005 Market Street. Wilmington had an active quarter, as Chemours leased 256,000 sf at 1007 N Orange Street. Capital One also inked a 88,797 sf deal at 802 Delaware Avenue. These leases pushed quarterly deal volume to 2.3 msf, its highest mark since 2015.

### Consolidation Providing Some Relief

The last few months brought news of significant consolidations among banks, as well as the movement of back office operations to lower-cost markets. PNC, for example, recently signed a lease extension at 1600 Market Street, but they will shrink from 360,000 sf to 230,000 sf. They are also subletting just under 115,000 sf of the 441,000 sf they lease at 8800 Tincum Boulevard. A few months ago Wells Fargo moved 120 employees to Charlotte, North Carolina. In Delaware, HSBC announced that it will move 400 jobs from 90 Christian Road to Chicago and Buffalo. Banks are not the only sector shedding space. Pennsylvania Lumberman's is rumored to be cutting its occupancy at Commerce Square in half to about 15,000 sf. Deloitte which leases 120,000 sf at 1700 Market Street is slimming down to about 75,000 sf.

Several significant lease rollovers in Downtown Philadelphia will provide additional alleviation of the space crunch in 2018 and 2019. United Health and several Comcast Corp lease expirations are looming. The EPA, which occupies

307,847 sf at 1650 Arch St and has a lease expiration in 2018, is considering its options. Other office users throughout the city are contracting space via densification, not necessarily reducing headcounts. A game of musical chairs still prevails in Philly's CBD - people would rather move across the street to a comparable building with a substantial concession package than live through construction to renovate their existing space. While eds and meds are still expanding, University City has seen a slowdown in activity with CHOP vacating 3535 Market St and limited expansion from the typical University City tenants.

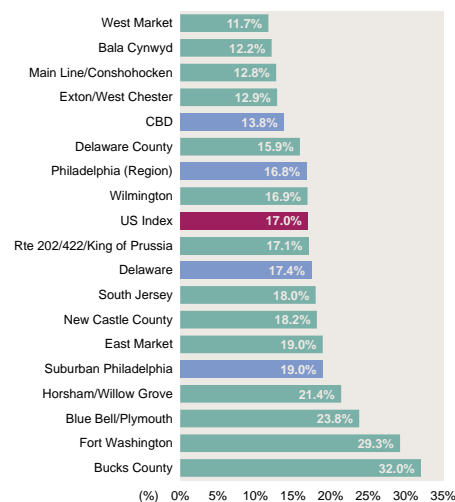
### Price Resistance Slows Pre-Leasing Efforts

Center City's existing building stock is a bit picked over, particularly in terms of bigger blocks of quality space. Tenants could tap into the next set of proposed high-rises, but so far there have been few takers for these projects. The differential in rent between existing Class A buildings (\$40/sf range) and new proposed properties (\$50/sf or higher) appears too wide. Meanwhile, new projects in Camden NJ offer incentives that significantly lower occupancy costs. This is piquing the interest of some large tenants that may have normally restricted their search to Center City. Downtown Philadelphia's ample retail, nightlife and residential product is a key advantage that Camden can not match, but cost-conscious firms are taking a close look.

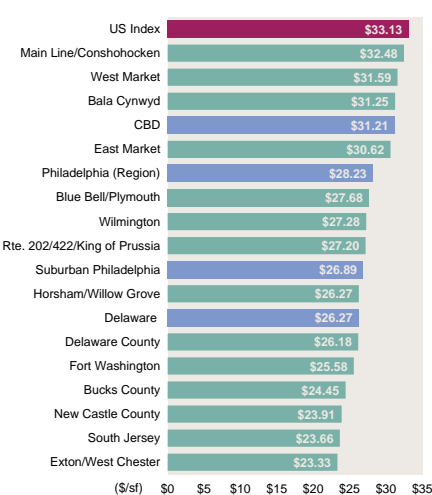
### Widespread Renovations

Rising construction costs give tenants added cause to be as efficient as possible in their leases. Space efficiency can be best achieved in newer buildings, but the elevated rent that offsets the value of downsizing is still a big hurdle for many firms to overcome. Another alternative is to find space in recently renovated buildings. With the very top of the market separating from the rest of the pack it creates space for landlords in older A/B+ building to modernize their assets and then raise rent, but still remain affordable. We have seen this as buildings have traded hands over the past few years. Owners are adding amenities and renovating lobbies. Some landlords are converting class B buildings to creative space to attract new tenant types. Between new construction in Camden, and renovated buildings, some suburban office product - particularly the most isolated buildings without the cash to fund major capital improvements - are struggling to compete.

### Availability Rate Comparison



### Rental Rate Comparison



### Major Transactions

Tenant	Sq Feet	Address	Market Area
Duane Morris	257,021	30 S 17th St	West Market
Chemours	256,000	1007 N Orange St	Wilmington
Capital One	88,797	802 Delaware Ave	Wilmington
JG Wentworth	83,500	1200 Morris Dr	Route 202/422/King of Prussia
Brandywine Global	66,501	1735 Market St	West Market
Jazz Pharmaceutical	46,000	2005 Market St	West Market
RSM McGladrey	42,450	518 Township Line Rd	Plymouth Meeting
Cenlar	35,000	780 Township Line Rd	Bucks County
BTG	33,538	300 Conshohocken State Rd	Main Line/Conshohocken
Liberty Property Trust	31,479	650 E Swedesford Rd	Route 202/422/King of Prussia
<b>Sum of Leases</b>	<b>940,286</b>	<b>Sum of 2nd Quarter Leasing Activity</b>	<b>2.3 MSF</b>

There are always exceptions to the rule. The last few years have brought many stories about the demise of the suburban campus, but some companies are bucking the trend. SEI has been adding about 200 people a year for the last five years. They are now planning a major expansion at their campus in Montgomery County, but have short term solutions in existing office buildings. SEI plans to add more than 400,000 sf of new office space on 90 acres adjacent to its current campus.

### Lab Space Infusion

Even the very tight lab/R&D market could get a much-needed injection of added space. Lab and R&D space is tighter than the traditional office space market. Vertex's move out of five buildings totaling 130,000 sf at 1041 Old Cassatt Road will enable the owner to make substantial improvements to the facility. In a much bigger impact on the market, GlaxoSmithKline's massive 2.2 msf campus at 709 Swedesford Road has been put up for sale. The availability of existing lab space could be particularly appealing.

### Looking Forward

Philadelphia's office market, much like the broader national economy is expected to be in a holding pattern during the second half of 2017. Camden could see a flurry of activity - its hefty incentives are set to sunset in mid-year 2019 and an upcoming governor elections. Otherwise, more tenants are likely to proceed cautiously. Tenants may take a closer look at suburban growth opportunities, as landlords in office parks do their best to compete with both the Camden and Philadelphia CBDs, by expanding their amenity offerings.

Map	Submarket	Total	Leasing Activity	Available SF		Availability Rate			Asking Rents Per SF			
		SF (1000's)	Last 12 Months	This Quarter	% Change from Last Qtr.	Year Ago	This Quarter	PP Change from Last Qtr. (1)	Year Ago	This Quarter	% Change from Last Qtr.	Year Ago
1	<b>West Market</b>	31,959	2,666	3,747	-2.3%	3,852	11.7%	-0.3%	13.7%	\$31.59	1.6%	\$30.48
	West Market - Class A	23,475	2,078	2,544	0.7%	2,500	10.8%	0.1%	12.2%	\$32.13	0.5%	\$32.78
2	<b>East Market</b>	12,853	797	2,436	7.8%	2,375	19.0%	1.4%	16.8%	\$30.62	2.7%	\$28.36
	East Market - Class A	5,454	162	1,256	-4.0%	1,019	23.0%	-1.0%	17.7%	\$32.58	1.4%	\$31.47
3	<b>Bala Cynwyd</b>	3,232	154	393	3.8%	474	12.2%	0.4%	13.7%	\$31.25	-2.4%	\$29.53
	Bala Cynwyd - Class A	2,258	112	293	1.7%	326	13.0%	0.2%	13.2%	\$32.62	-0.8%	\$32.34
4	<b>Blue Bell/Plymouth Meeting</b>	5,342	403	1,272	-11.2%	1,368	23.8%	-3.1%	21.2%	\$27.68	3.6%	\$24.93
	Blue Bell/Plymouth Meeting - Class A	2,701	69	473	-6.0%	380	17.5%	-1.0%	10.6%	\$27.46	1.9%	\$25.91
5	<b>Fort Washington</b>	2,756	151	806	0.3%	1,198	29.3%	0.1%	24.8%	\$25.58	9.2%	\$24.00
	Fort Washington - Class A	1,665	77	421	3.6%	801	25.3%	0.9%	18.6%	\$26.47	10.5%	\$24.33
6	<b>Horsham/Willow Grove</b>	4,514	132	966	3.9%	1,010	21.4%	0.8%	22.1%	\$26.27	4.3%	\$25.38
	Horsham/Willow Grove - Class A	3,404	56	509	5.8%	398	15.0%	0.8%	11.9%	\$25.84	3.2%	\$25.44
7	<b>Route 202/422/King of Prussia</b>	13,561	1,048	2,317	-1.0%	2,907	17.1%	-0.2%	20.3%	\$27.20	4.1%	\$27.79
	Route 202/422/King of Prussia - Class A	9,138	864	1,316	-0.2%	2,126	14.4%	0.0%	20.9%	\$28.86	0.7%	\$29.89
8	<b>Exton/West Chester</b>	4,287	153	553	-5.7%	601	12.9%	-0.8%	12.6%	\$23.33	3.1%	\$22.28
	Exton/West Chester - Class A	2,854	129	340	-9.7%	416	11.9%	-1.3%	13.1%	\$25.46	5.8%	\$23.44
9	<b>Main Line/Conshohocken</b>	5,745	356	733	-16.4%	684	12.8%	-2.5%	13.6%	\$32.48	1.0%	\$32.76
	Main Line/Conshohocken - Class A	4,506	332	529	-20.8%	510	11.7%	-3.1%	14.1%	\$35.22	1.4%	\$36.86
10	<b>Delaware County</b>	4,717	186	751	8.5%	779	15.9%	1.2%	16.7%	\$26.18	3.8%	\$25.49
	Delaware County - Class A	3,782	62	579	-1.1%	673	15.3%	-0.2%	16.9%	\$26.76	4.6%	\$25.82
11	<b>Bucks County</b>	4,460	317	1,428	-11.0%	1,662	32.0%	-4.0%	32.0%	\$24.45	5.3%	\$22.35
	Bucks County - Class A	3,109	226	951	-14.9%	1,153	30.6%	-5.4%	31.4%	\$25.20	5.8%	\$22.79
12	<b>Wilmington</b>	7,735	619	1,310	-10.5%	1,474	16.9%	-2.0%	18.6%	\$27.28	3.1%	\$27.13
	Wilmington - Class A	6,182	563	1,042	-11.1%	1,186	16.9%	-2.1%	18.9%	\$28.83	3.1%	\$28.25
13	<b>New Castle County</b>	5,152	100	937	13.9%	860	18.2%	2.2%	17.7%	\$23.91	6.9%	\$21.17
	New Castle County - Class A	3,286	48	460	26.8%	286	14.0%	3.0%	10.2%	\$22.85	-3.0%	\$20.75
14	<b>South Jersey</b>	14,355	398	2,586	22.1%	2,548	18.0%	3.3%	16.0%	\$23.66	11.1%	\$21.05
	South Jersey - Class A	6,721	161	1,256	44.0%	1,062	18.7%	5.7%	13.2%	\$25.67	9.8%	\$22.24
1-2	<b>Philadelphia CBD Total</b>	44,812	3,463	6,184	1.5%	6,228	13.8%	0.2%	13.9%	\$31.21	1.9%	\$29.58
	Philadelphia CBD Total - Class A	28,930	2,239	3,800	-0.9%	3,520	13.1%	-0.1%	12.2%	\$32.28	0.8%	\$32.38
3-11	<b>Suburban Philadelphia Total</b>	48,612	2,902	9,220	-2.8%	10,699	19.0%	-0.6%	21.1%	\$26.89	4.5%	\$25.86
	Suburban Philadelphia Total - Class A	33,417	1,927	5,411	-4.8%	6,795	16.2%	-0.8%	19.3%	\$28.09	4.0%	\$26.93
12-13	<b>Delaware Total</b>	12,887	720	2,247	-1.7%	2,334	17.4%	-0.3%	18.2%	\$26.27	4.2%	\$25.73
	Delaware Total - Class A	9,469	114	1,503	-2.2%	1,472	15.9%	-0.4%	15.9%	\$27.98	2.9%	\$27.53
1-14	<b>Philadelphia Region Total</b>	120,666	7,482	20,237	1.2%	21,808	16.8%	0.2%	17.6%	\$28.23	3.7%	\$26.55
	Philadelphia Region Total - Class A	78,536	4,938	11,970	0.4%	12,847	15.2%	0.1%	15.7%	\$29.65	2.6%	\$28.39

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(1) Percentage point change for availability rates.  
 Unless otherwise noted, all rents quoted throughout this report are average asking gross (full service) rents psf. Statistics are calculated using both direct and sublease information.  
 Short-term sublet spaces (terms under two years) were excluded.

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