

The Savills logo consists of a yellow square above the word "savills" in a lowercase, red, sans-serif font. The background of the entire slide is a photograph of a modern office lobby with large glass windows, orange armchairs, and people walking.

Q1 2024 | OFFICE

# State of the U.S. Office Market

Powered by Savills Research & Data Services

**The office market at the start of 2024 remains sluggish as office space demand continues to be largely expiration-driven and below pre-pandemic levels**

## 01 Hybrid workplace is now the “new normal” overall

Post-pandemic impacts have left the office market strained and availability levels high despite recent data showing improved Return to Office rates. Hybrid workplace is now the “new normal” for most occupiers.

## 02 Leasing activity remains lower than pre-pandemic

Office space demand remains soft and largely expiration-driven at the start of 2024 despite an overall economy that is still growing with a sub-4% unemployment rate.

## 03 Average asking rents have not dropped as expected

Advertised rents have not decreased as much as thought despite lower demand. However, landlord concessions are at a historic high in many markets as many owners have held on their face rents.

## 04 Well-capitalized owners continue to win deals

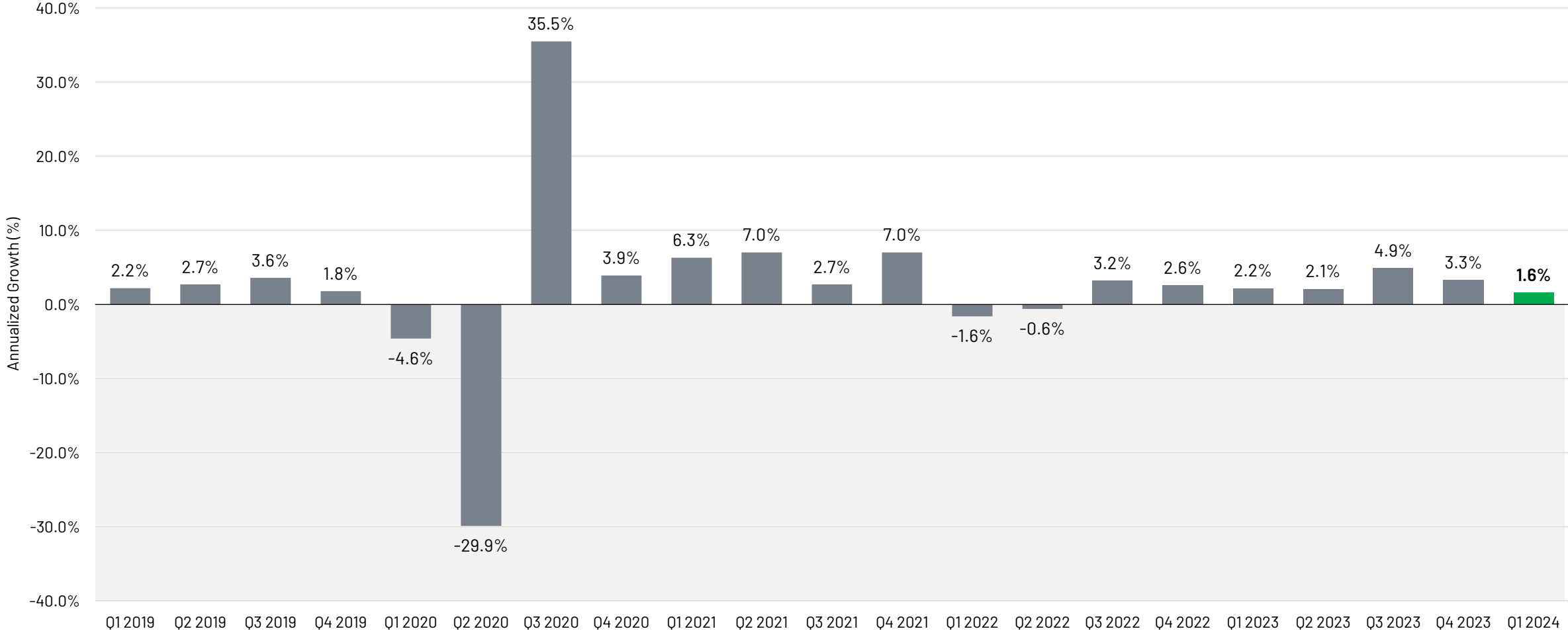
“Flight-to-capital” remain prevalent as office building owners in a stronger financial position and without looming debt maturities have been better able to win deals.

## 05 Purpose of the office continues to evolve

Rather than merely warehousing employees, there is a higher focus on the office as a forum for collaboration, training, mentorship, and reinforcing company culture. However, the long-term effects of the hybrid workplace model remain to be seen.

# Despite Macroeconomic Concerns, Growth was Positive to Begin 2024

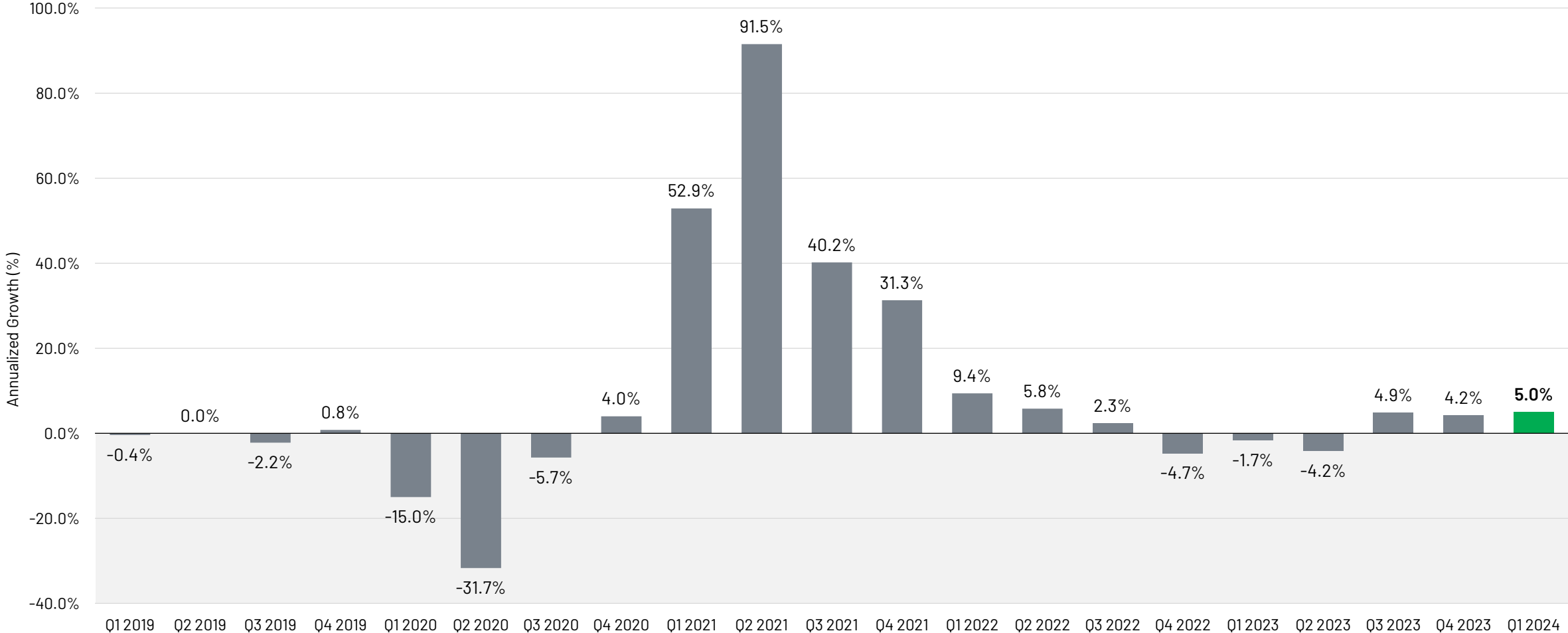
U.S. Gross Domestic Product (Annualized Growth %)



Source: Bureau of Economic Analysis

# Corporate Profits Remain Strong as Economic Expansion Continues

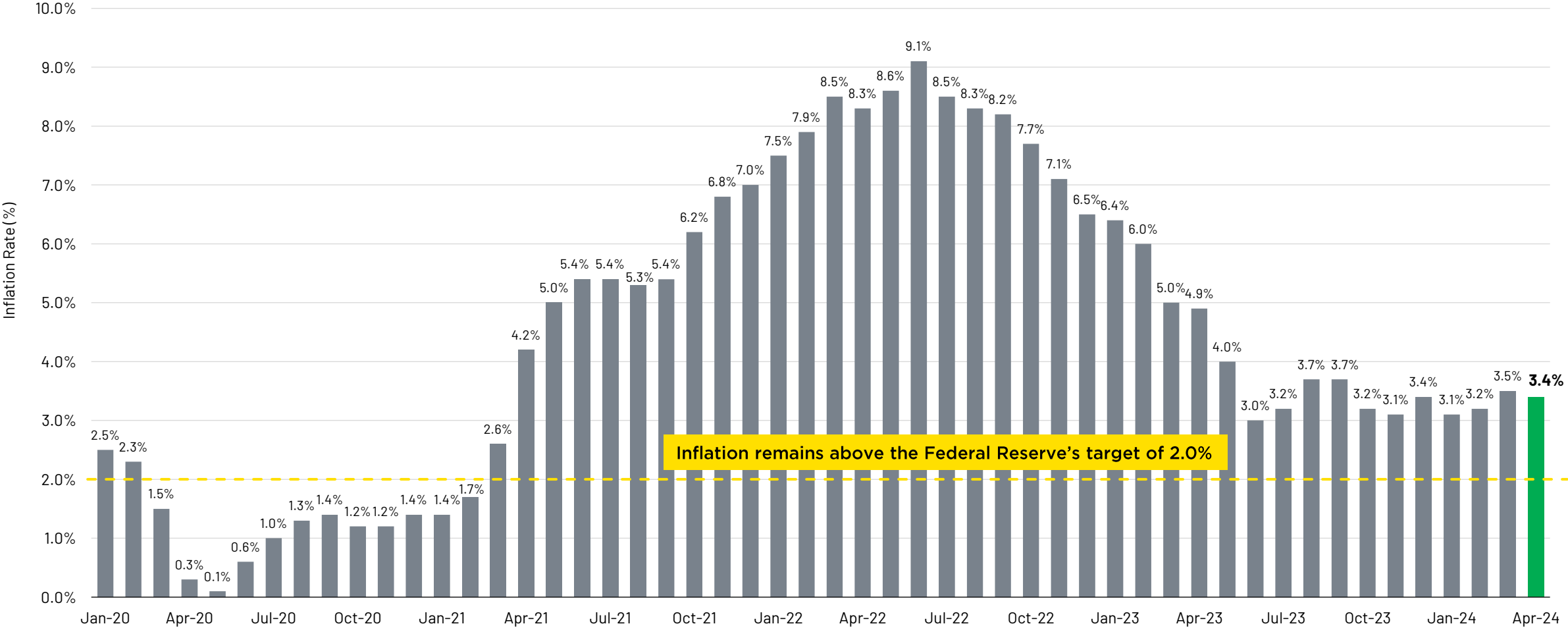
S&P 500 Blended Earnings Per Share (Annualized Growth %)



Source: FactSet

# Inflation Still Above the Federal Reserve's 2% Target to Begin the Year

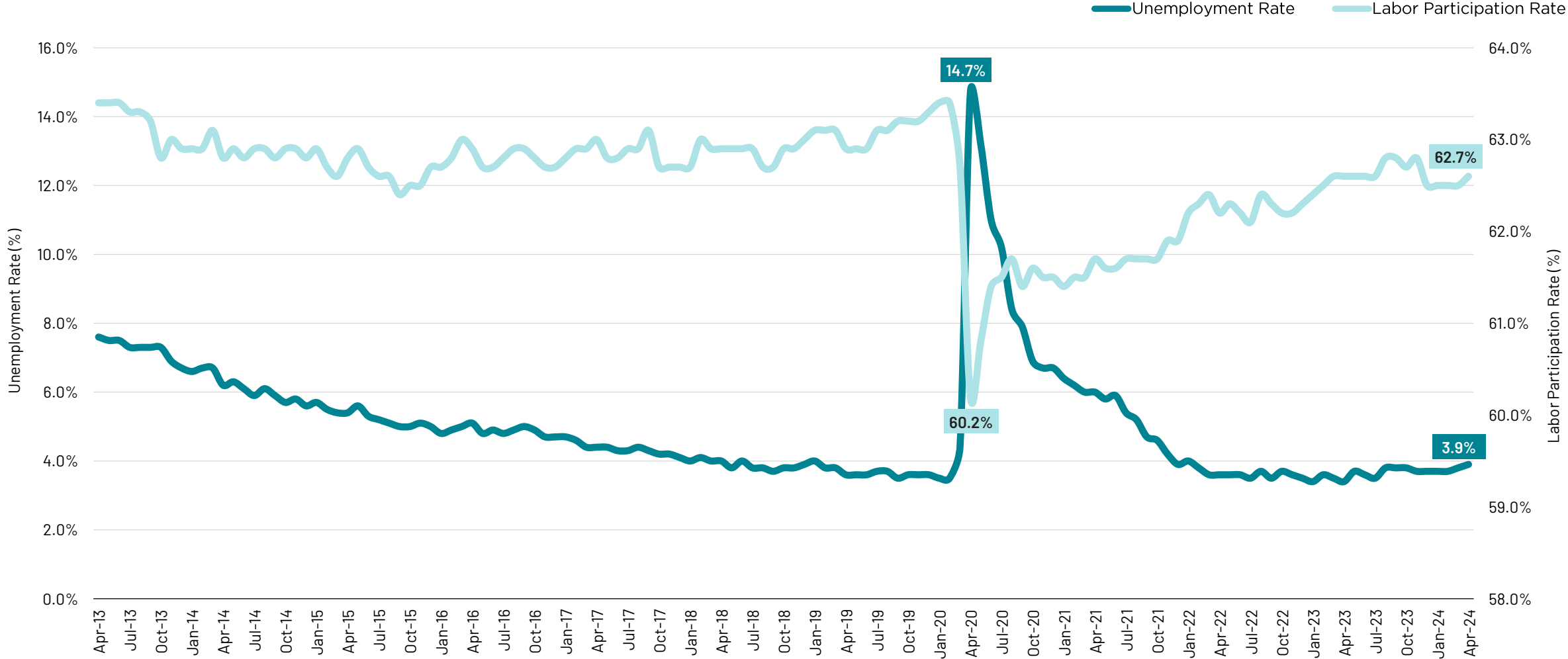
U.S. Consumer Price Index (Annualized Growth %)



Source: Bureau of Labor Statistics

# U.S. Unemployment Rate Seeing Small Uptick But Still Below 4%

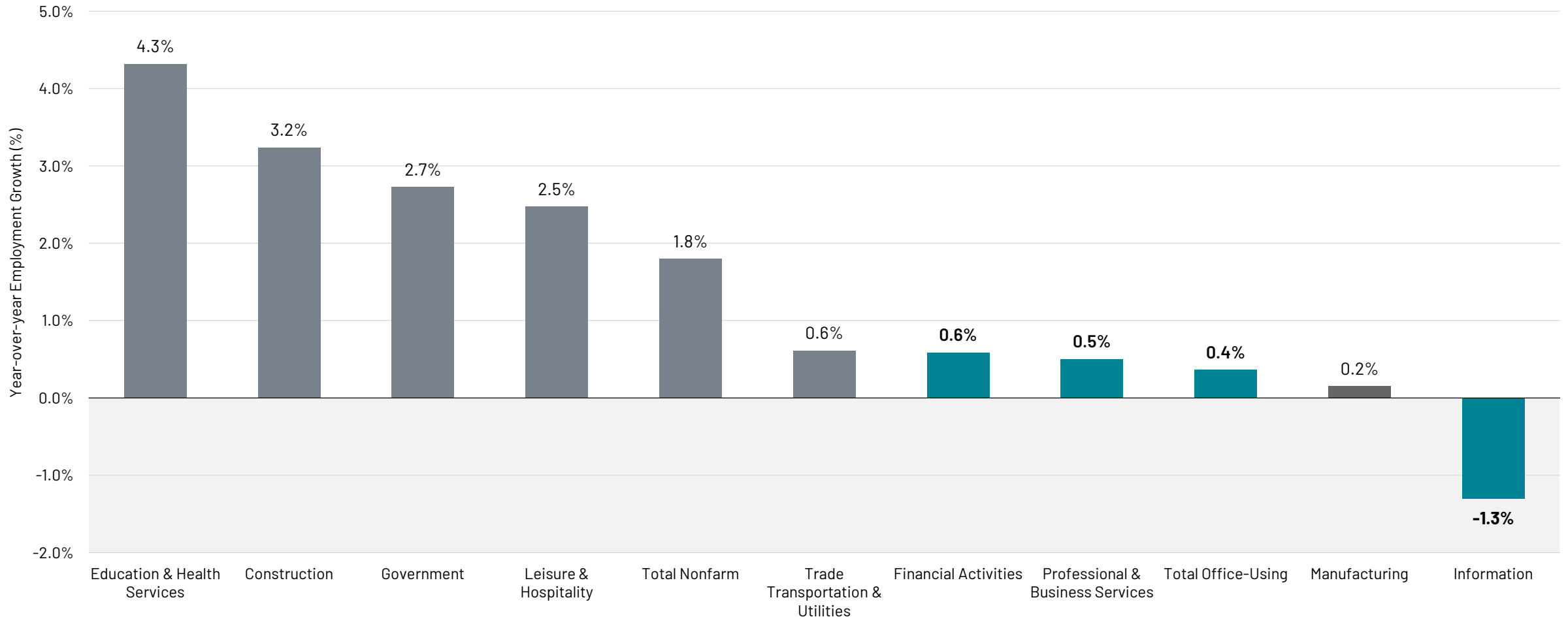
U.S. Monthly Unemployment Rate vs U.S. Monthly Labor Force Participation Rate (%)



Source: Bureau of Labor Statistics

# However, Growth in the Office-Using Employment Sectors has Slowed

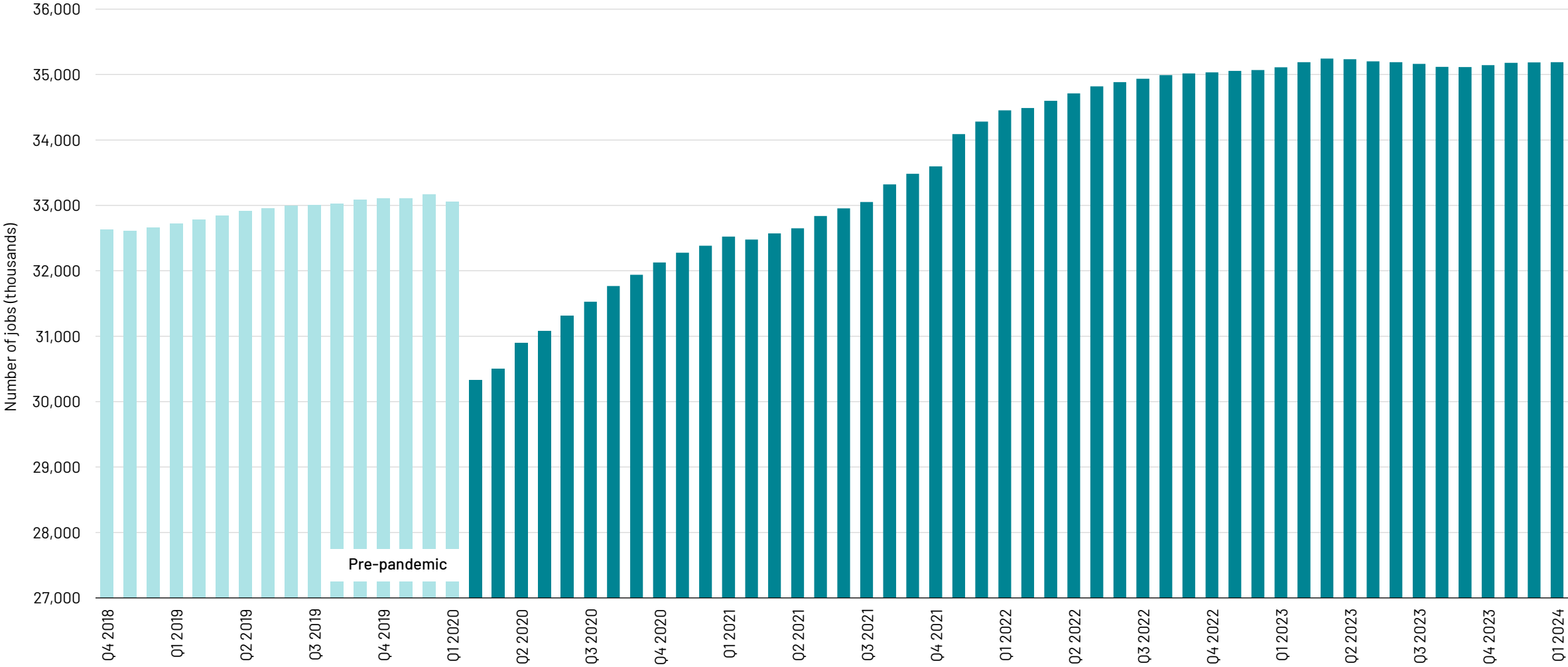
Year over year Employment Growth by Major Sector (%) – April 2024



Source: Bureau of Labor Statistics



# Total Office-Using Employment Has Been Higher Than Pre-Pandemic



Source: Bureau of Labor Statistics

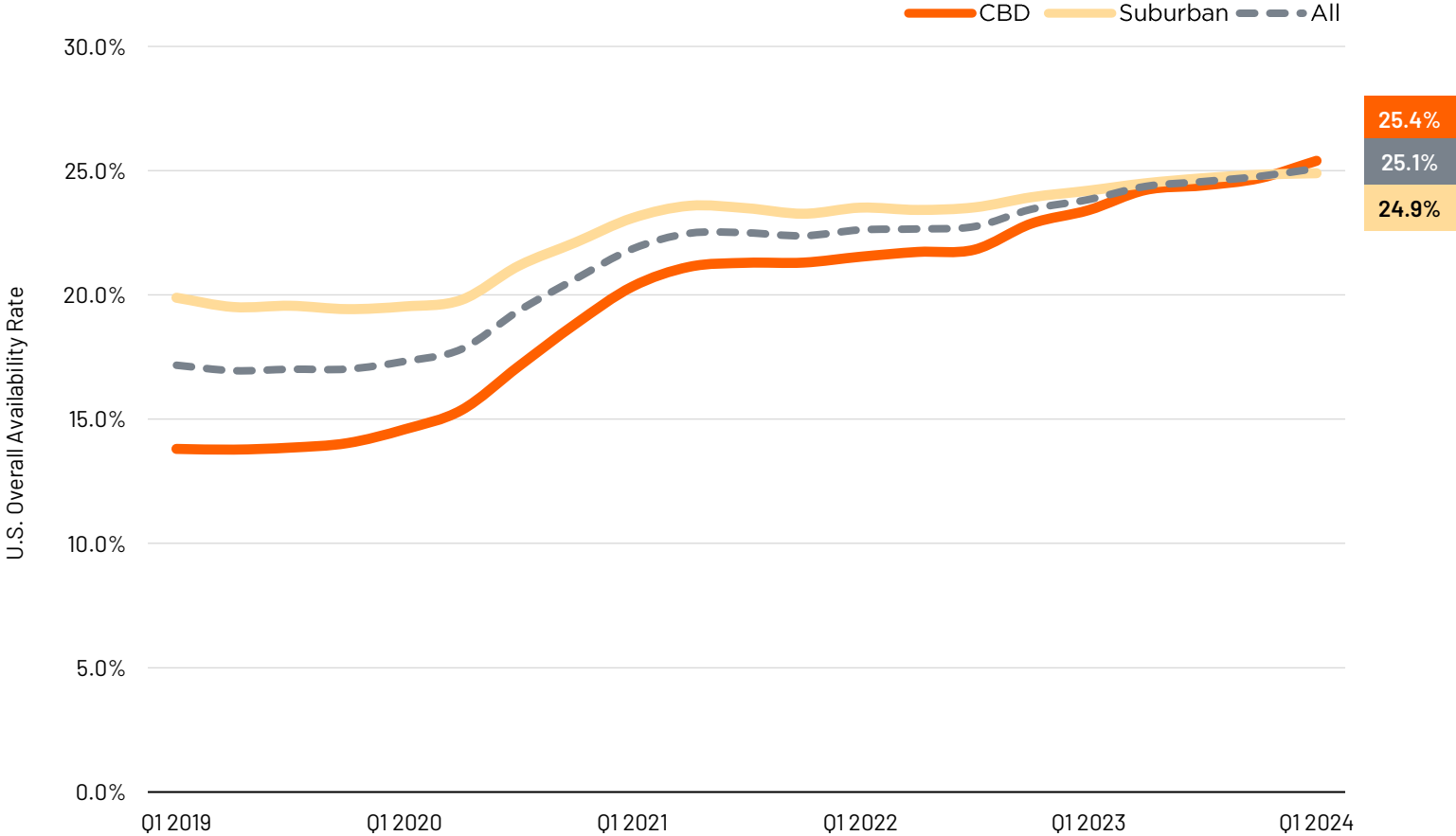
# But Office Availability Still Remains at an All-Time High

Availability remains elevated across U.S. markets as sublease space has swelled

Central Business District (CBD) availability currently at 25.4%, up 1,140 basis points from pre-pandemic as dense urban centers remain heavily impacted

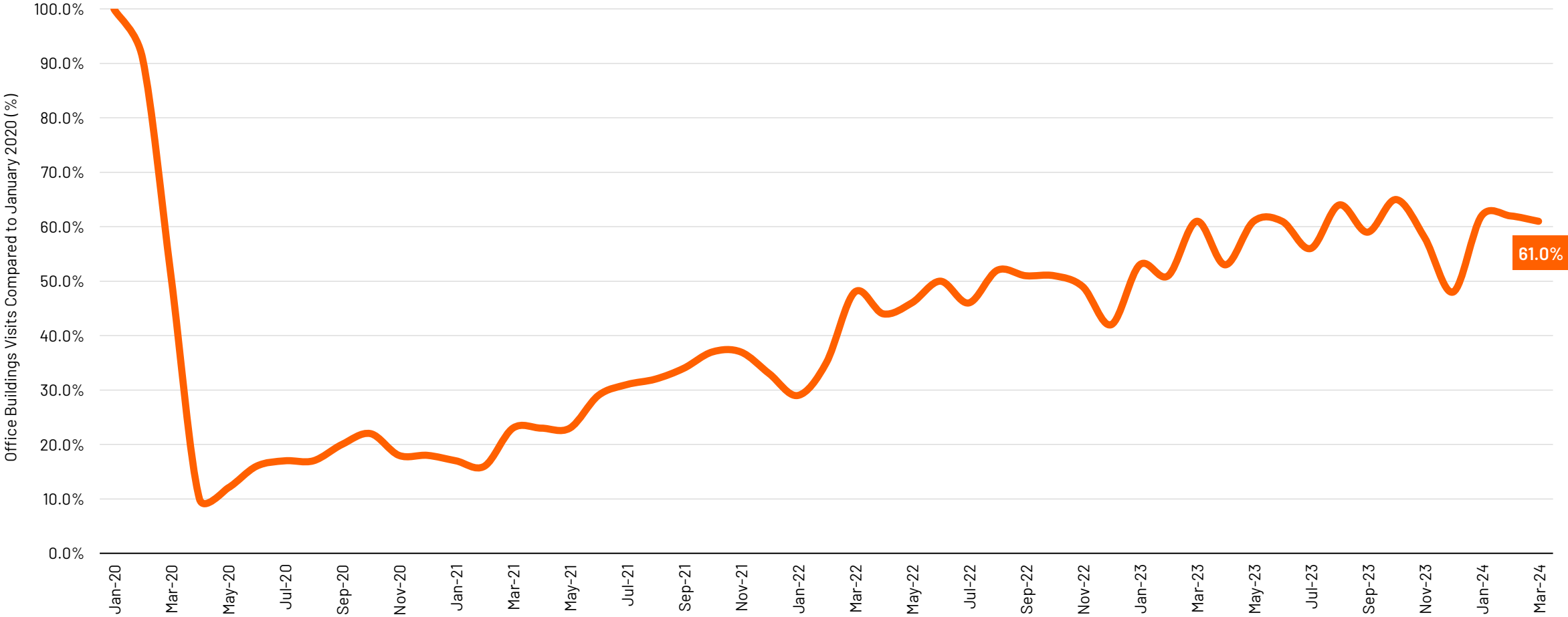
Suburban availability has increased at a slower pace, now at 24.9%, up 550 basis points from pre-pandemic levels

It will take time and sustained leasing activity to substantially offset the amount of space returned to the market since the onset of the pandemic



# Return to Office Rates Recover as Most Occupiers Shift to Hybrid Work

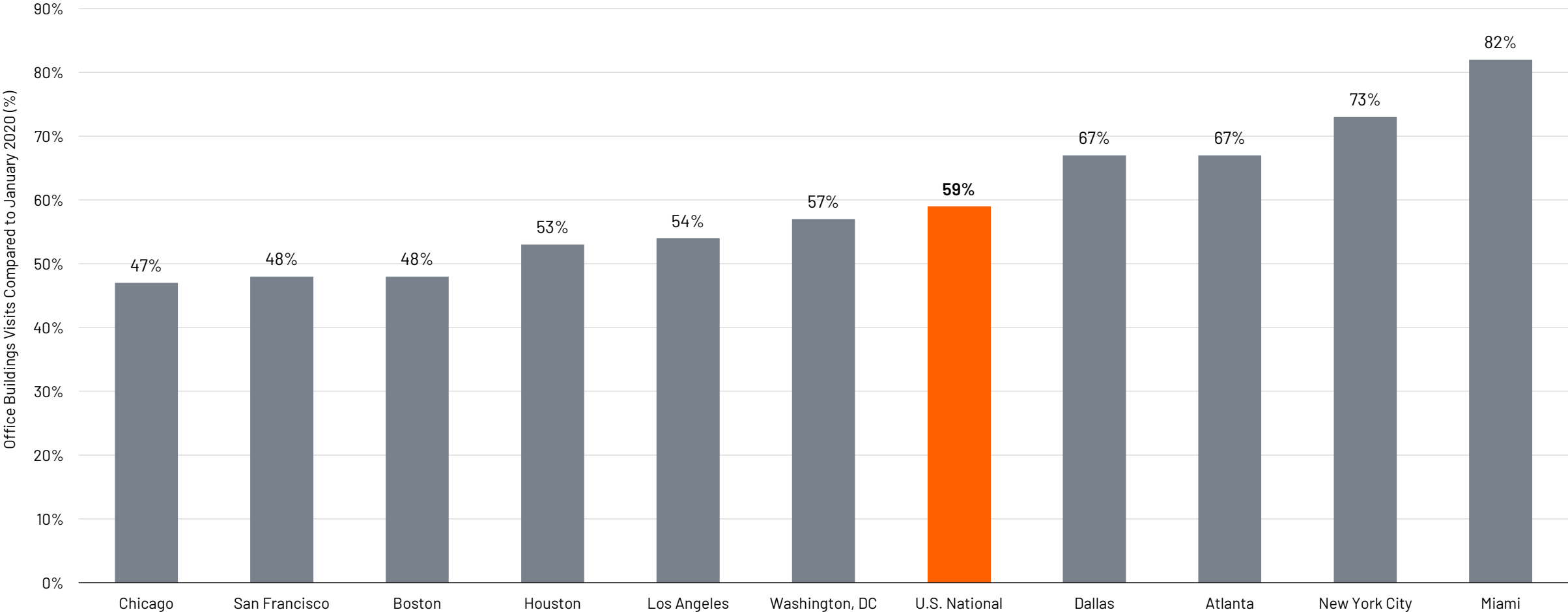
Nationwide Office Building Visits Compared to January 2020 Baseline - All Office Building Types



Source: Placer.ai

# In Top Tier Office Buildings, Miami and New York City Lead

Nationwide Office Building Visits Compared to January 2020 Baseline – March 2024

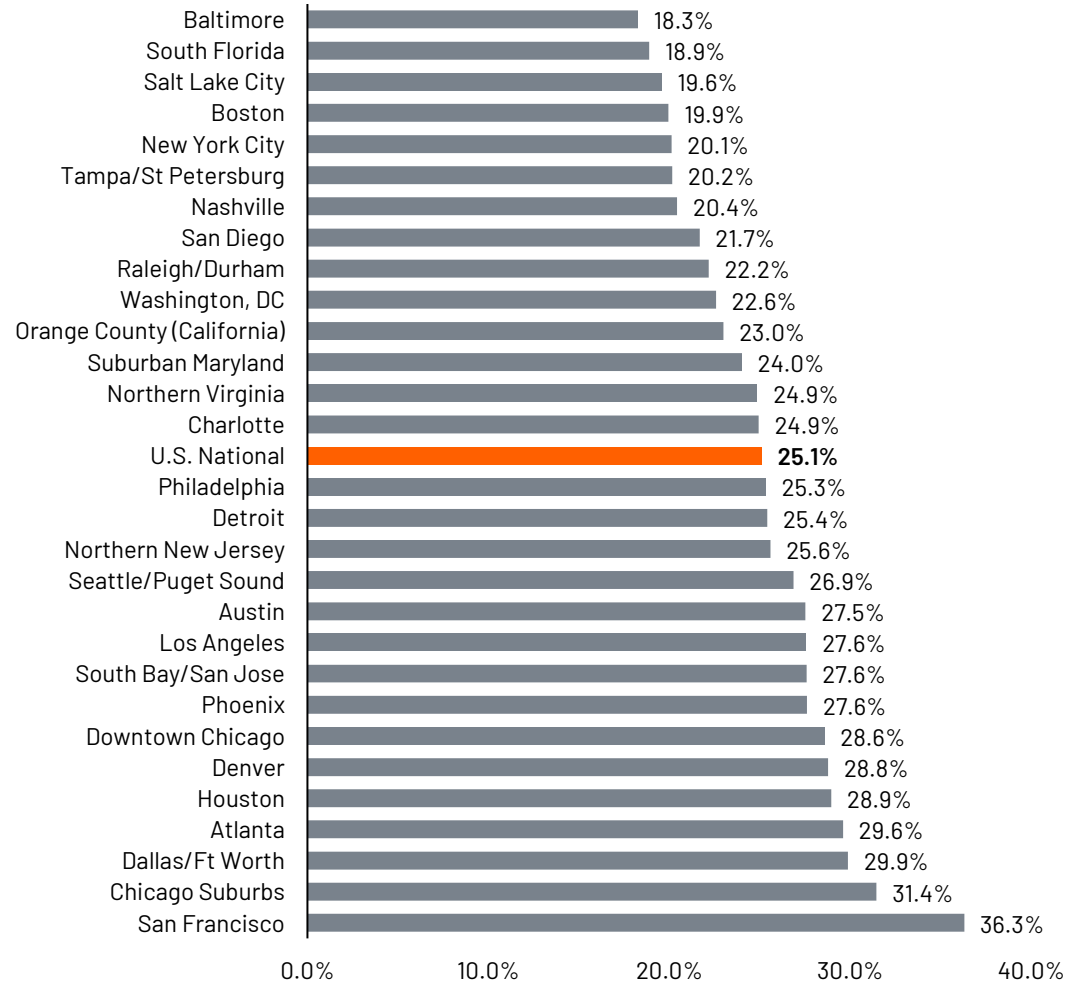


Source: Placer.ai

# Tech-Centric Office Markets Observing Largest Increase in Availability

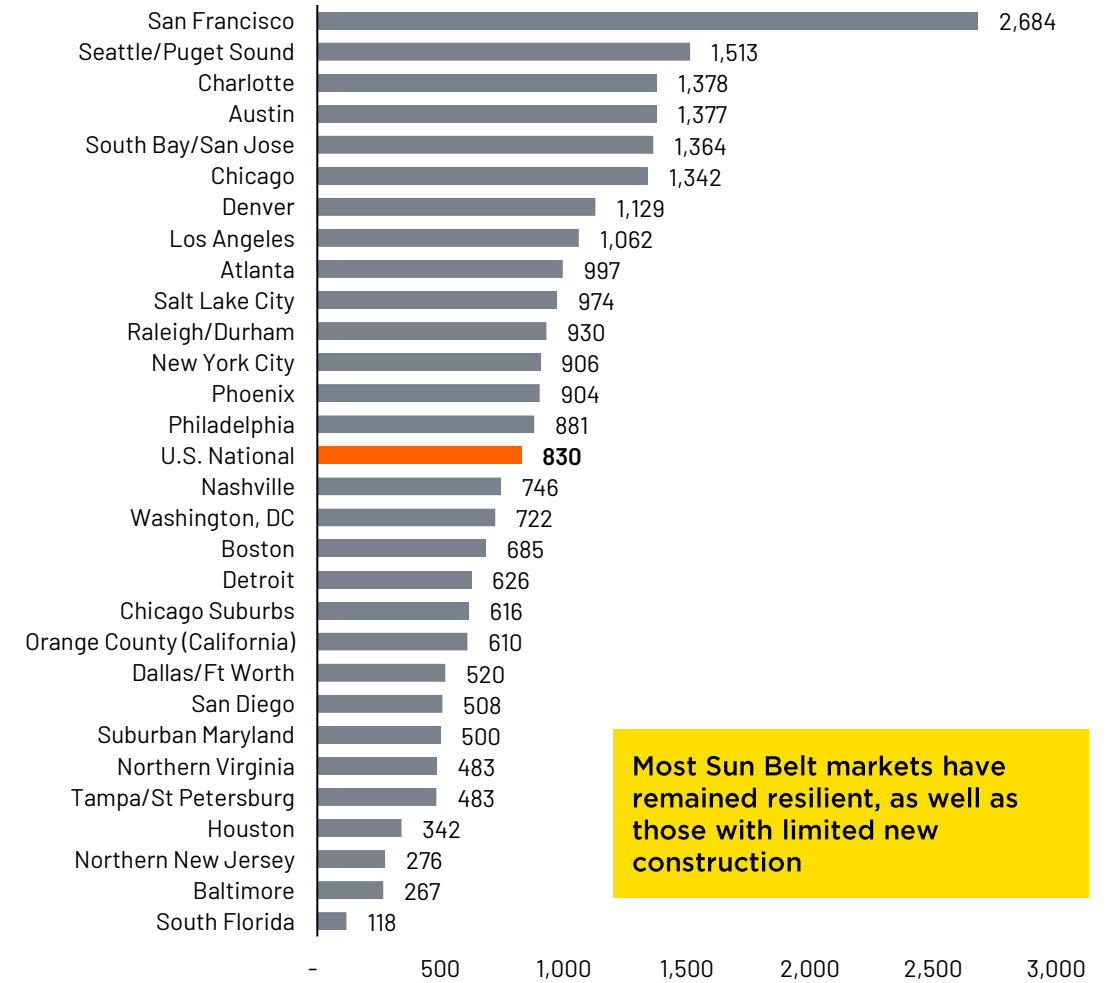
## Total Availability Rate (%)

Q1 2024



## Total Availability Rate (bps)

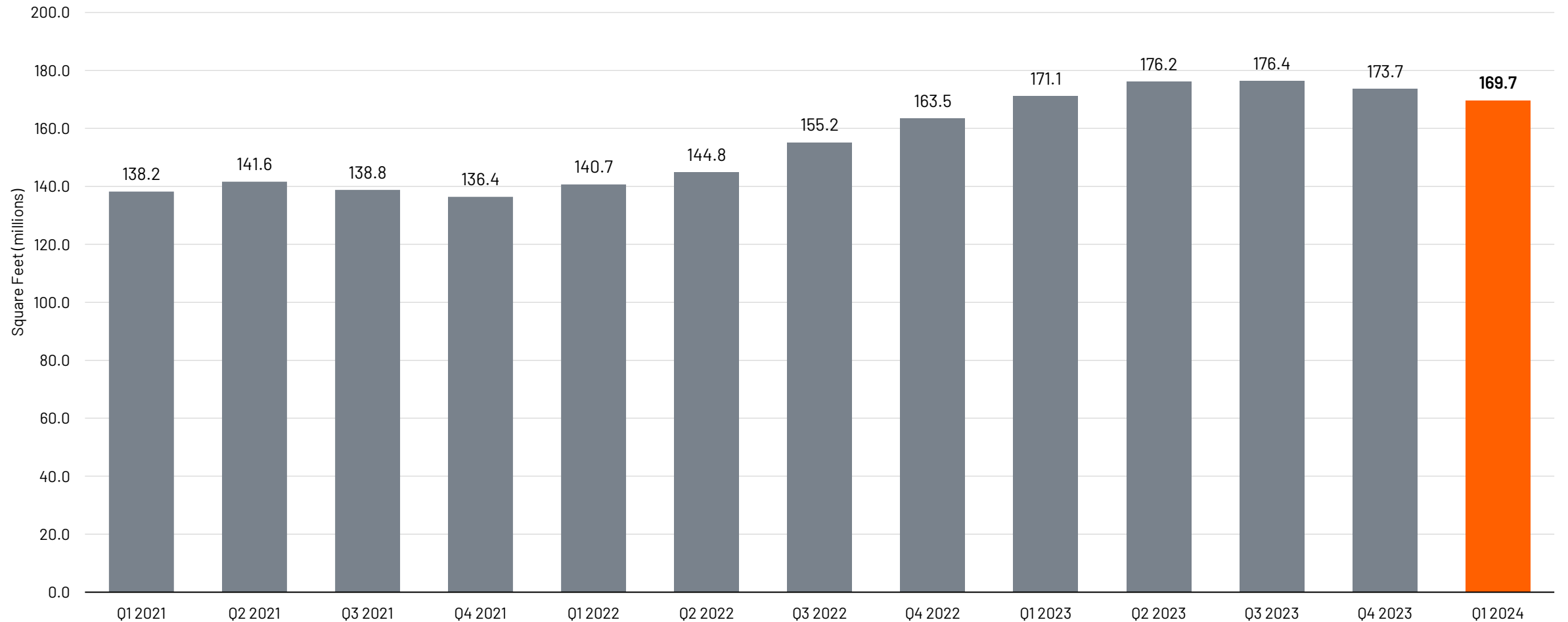
PANDEMIC CHANGE COMPARED TO Q4 2019



**Most Sun Belt markets have remained resilient, as well as those with limited new construction**

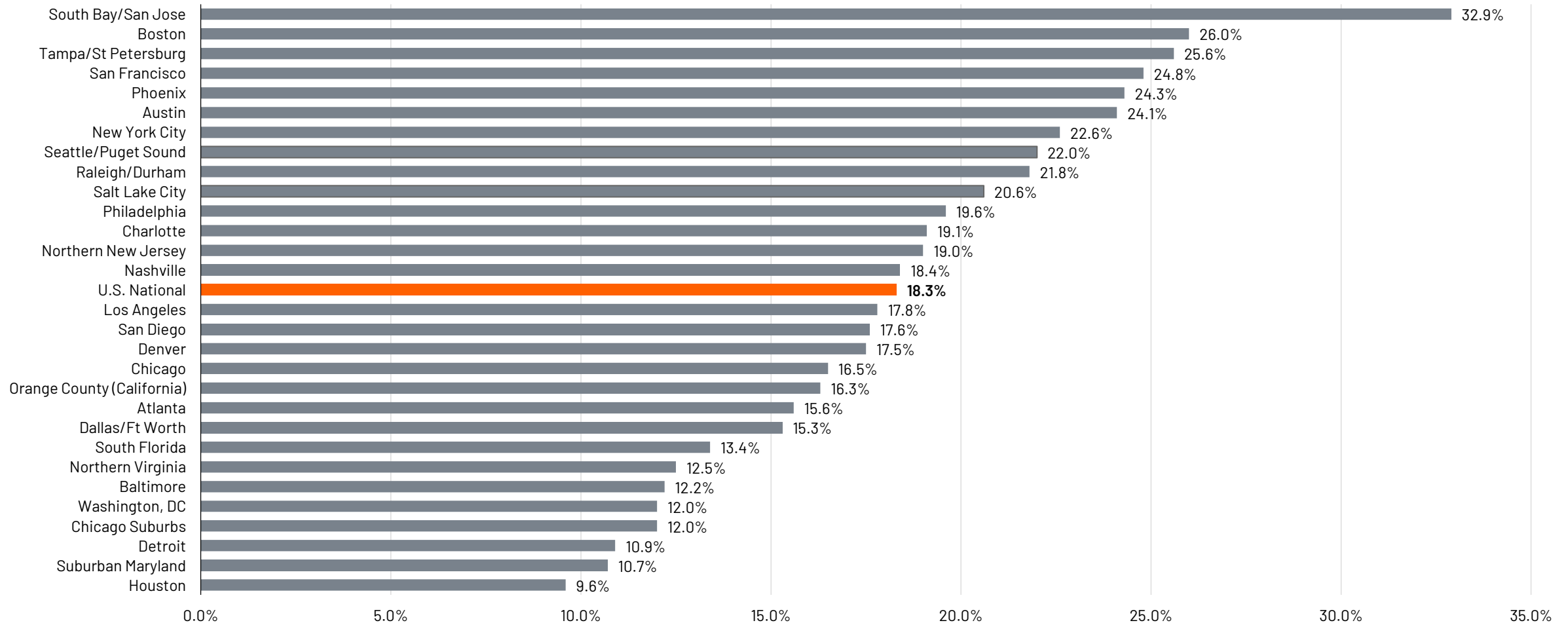
# Sublease Space Has Decreased Over the Past Two Quarters

Total Available Sublease Space (msf)



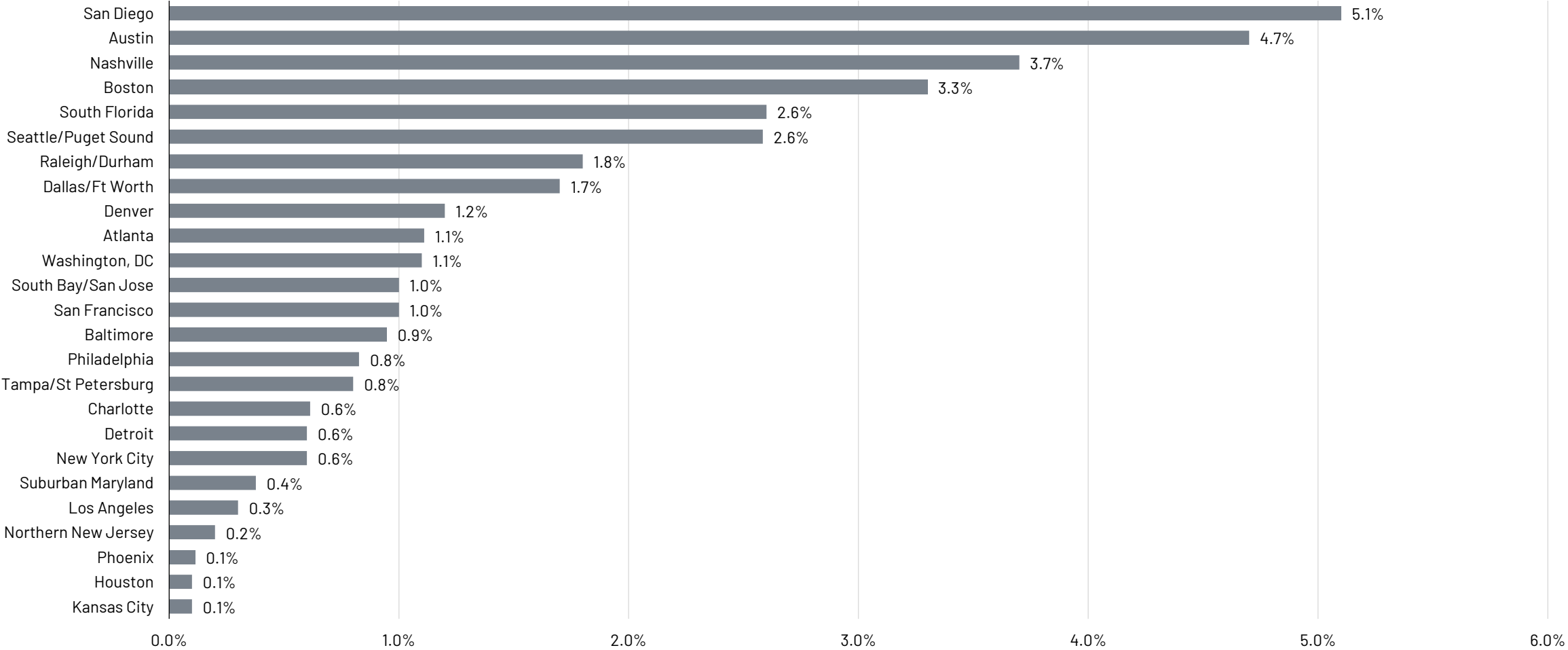
# Sublease Space Glut Remains Most Pronounced in Tech-Centric Markets

Available Sublease Space as a % of Total Available Space by Market



# New Supply Concerns Now Limited to Only a Few Markets

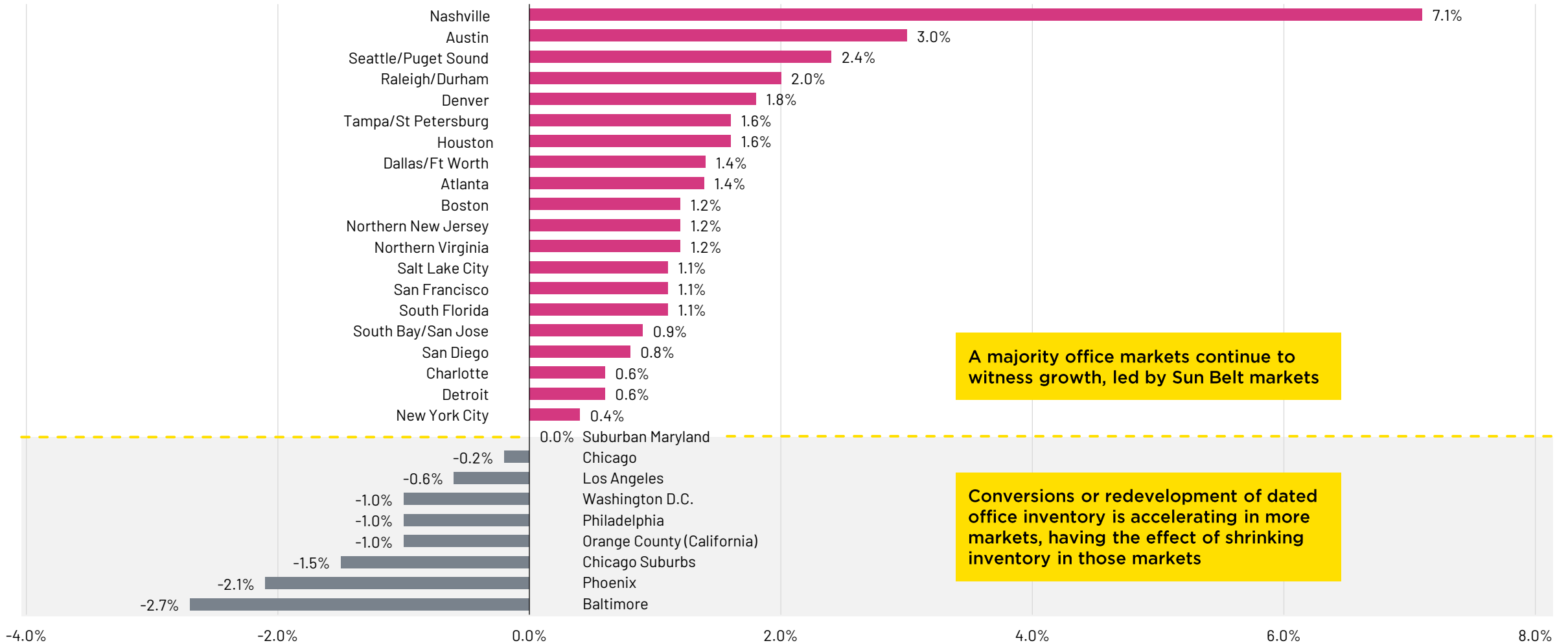
Office Square Footage Currently Under Construction as % of Inventory (100,000+ sf projects)





# Office Inventory is Now Shrinking in Some Markets

% Inventory Change From Q1 2023 to Q1 2024

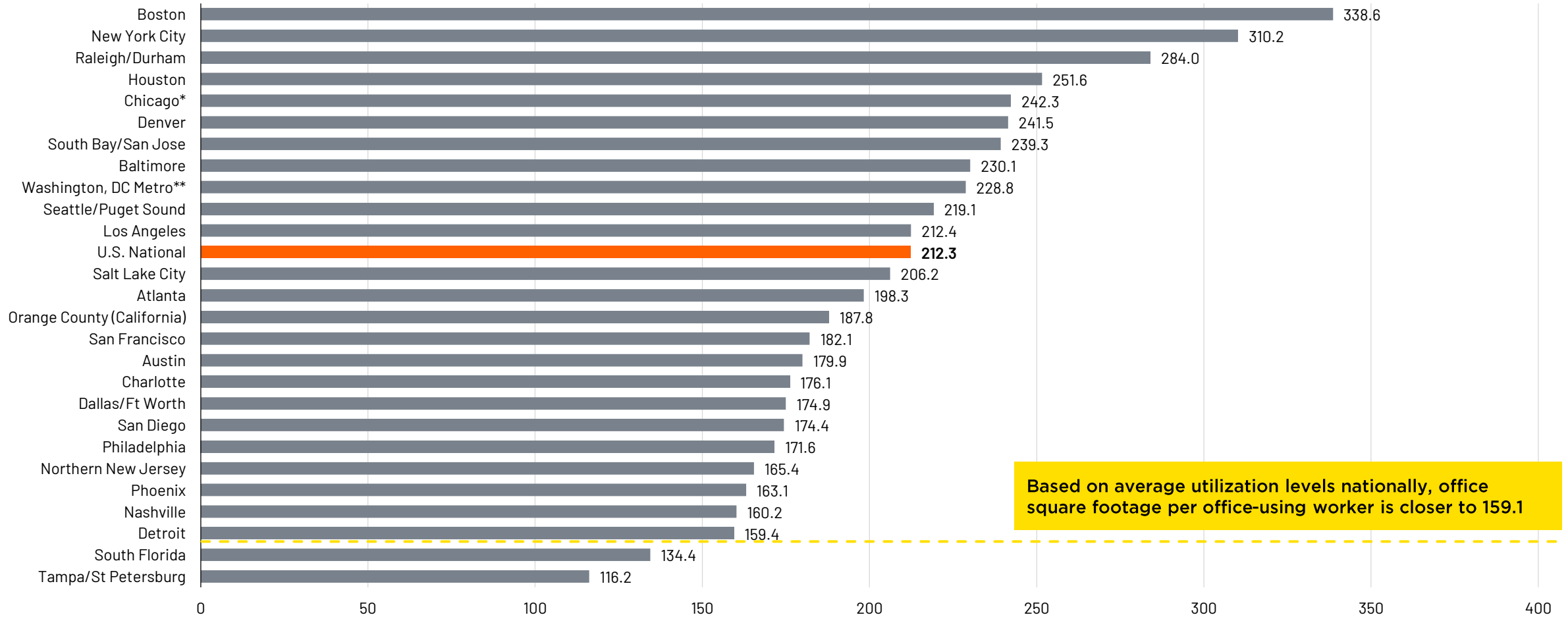


A majority office markets continue to witness growth, led by Sun Belt markets

Conversions or redevelopment of dated office inventory is accelerating in more markets, having the effect of shrinking inventory in those markets

# Office Markets are Now Mostly Oversupplied Compared to Demand

Office Square Footage Per Office-Using Worker by Market (sf)



\*Downtown Chicago and Chicago Suburbs combined.

\*\*Washington DC, Northern Virginia and Suburban Maryland Combined.

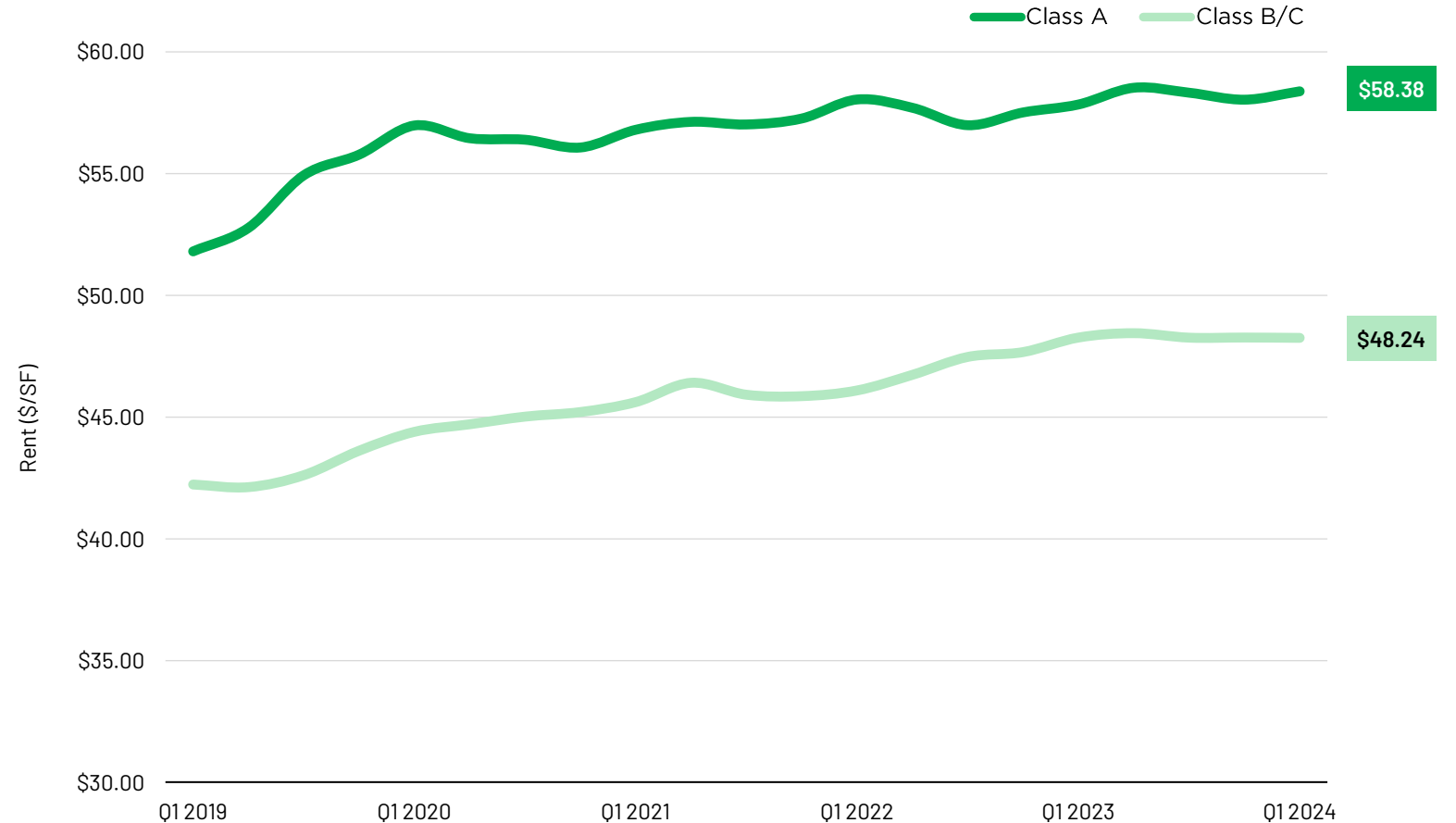
# Little Change to Asking Rents as Owners Offer High Concessions

CBD Average Asking Rents – Class A vs Class B/C (\$/sf)

Central Business Districts (CBDs) have not yet seen drastic repricing of asking rents with many owners **continuing to offer high concessions rather than dropping their face rents**

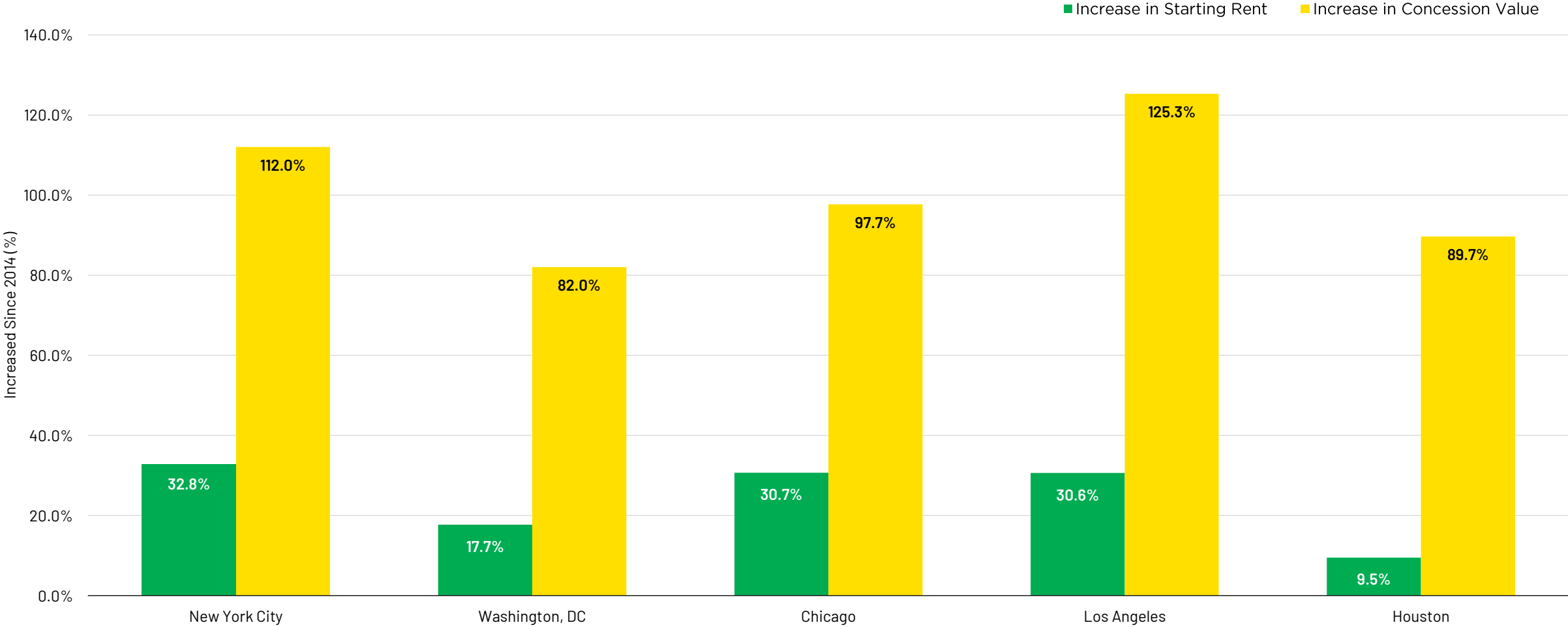
Flight-to-quality and active construction pipelines have contributed to stabilization of Class A rents – and **increasing at the very top of the market**

Growing bifurcation in many markets where pricing is high (and space limited) for top-tier buildings, while **older, more dated space is sitting on the market longer**



# Growth in Concession Values Have Outpaced Growth in Starting Rents

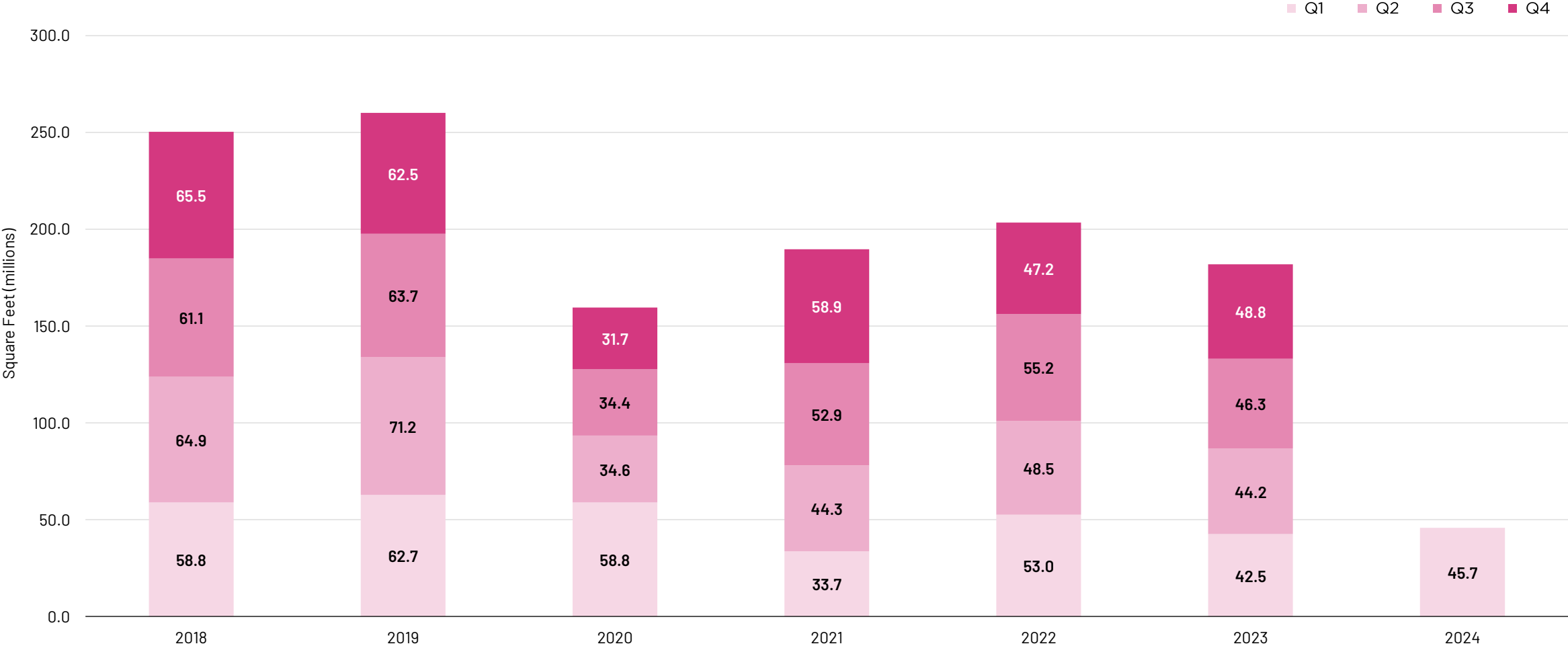
Class A New Long-Term Leases in Select Markets (2014-2024)



Source: CompStak Analytics

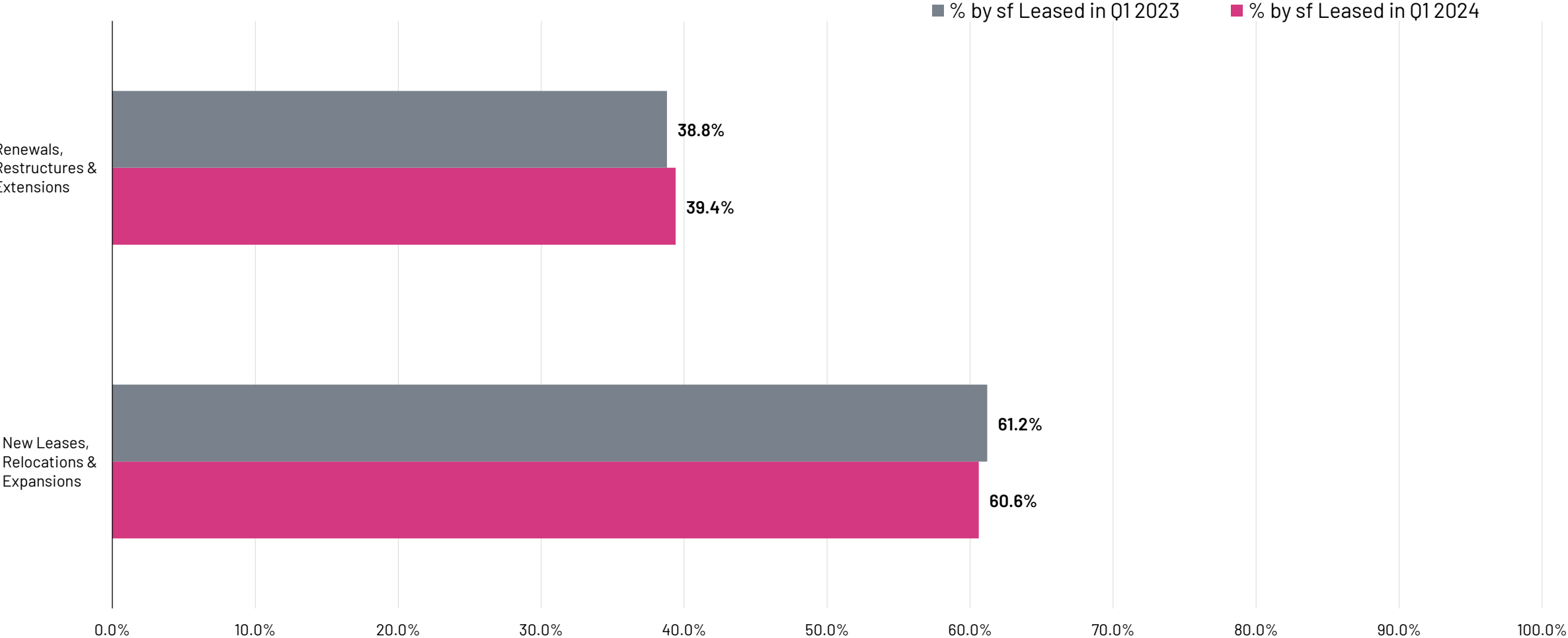
# Q1 Leasing Activity Up From a Year Ago But Lower than Pre-Pandemic

Total Leasing Activity (msf)














# New Office Space Demand Has Slightly Cooled From a Year Ago

Lease Transactions 20,000+ sf



# Largest Office Leases in Q1 2024 Largely Consist of Renewals

TENANT	INDUSTRY	MARKET	BUILDING	SIZE (SF)	LEASE TYPE	QUARTER LEASED
Snap	 TAMI*	Los Angeles	Santa Monica Business Park	466,733	Renewal	Q1 2024
Booz Allen	 Business, Professional and Consulting Services	Northern Virginia	8283 & 8285 Greensboro Drive	431,208	Renewal	Q1 2024
The Pokémon Company	 TAMI	Seattle/Puget Sound	10660 NE 8th Street	374,286	New Location	Q1 2024
The Washington Post	 TAMI	Washington, DC	1301 K Street NW	297,176	Renewal	Q1 2024
D.C. Dept. of General Services	 Government	Washington, DC	1101 4th Street SW	274,122	Early Restructure	Q1 2024
Maryland Dept of the Environment	 Government	Baltimore	1800 Washington Boulevard	263,473	New Location	Q1 2024
Endeavor Group	 Business, Professional and Consulting Services	Los Angeles	9601 Wilshire Boulevard	250,530	Extension	Q1 2024
Republic Services	 Transportation	Phoenix	NWC 56th Street & Loop 101	250,000	New Location	Q1 2024
Pfizer	 Pharmaceuticals	San Diego	11202 & 11208 El Camino Real	239,133	New Location	Q1 2024
Finnegan, Henderson, Farabow, Garrett & Dunner	 Legal Services	Washington, DC	901 New York Avenue NW	214,408	Renewal	Q1 2024
Manhattan Associates	 Business, Professional and Consulting Services	Atlanta	2300 Windy Ridge Parkway SE	210,000	Renewal	Q1 2024

\*Technology, Advertising, Media and Information

# Office Leasing Activity by Market

Total Leasing Activity Q1 2023 vs Q1 2024

## Savills Leasing Momentum Meter

BY BUBBLE COLOR

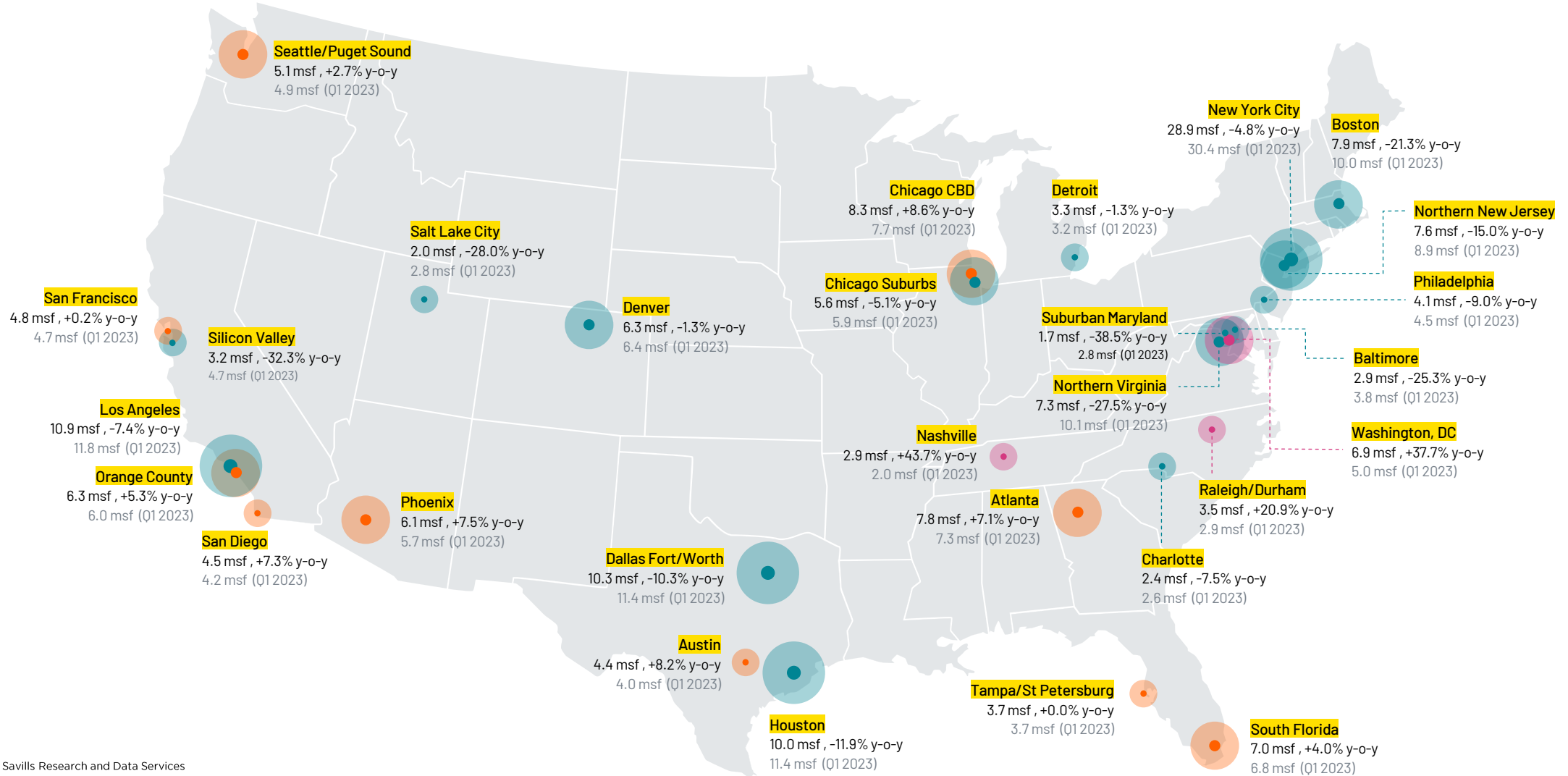
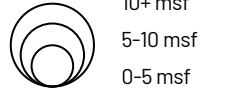


> 10% change y-o-y

< 0% change y-o-y

## Trailing 4-Quarter Leasing

BY BUBBLE SIZE

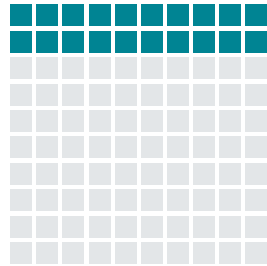


Source: Savills Research and Data Services

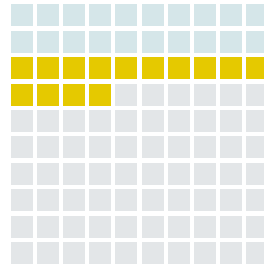


# TAMI Sector Leads Demand Despite Pullback From Large Tech Firms

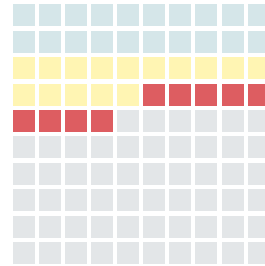
Total Leasing Activity 2023; 20,000+ sf



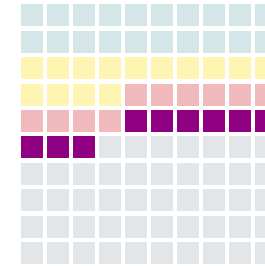
20.2% TAMI



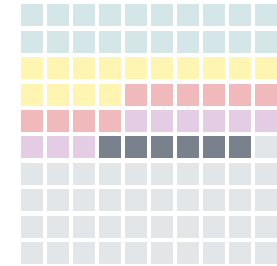
14.2% Financial Services and Insurance



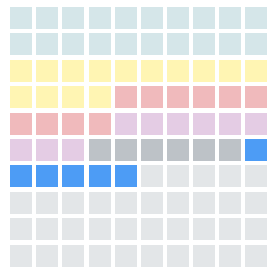
10.8% Professional & Business Services



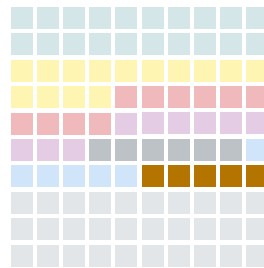
9.4% Legal Services



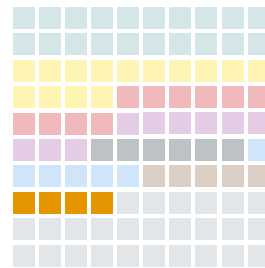
6.8% Retail



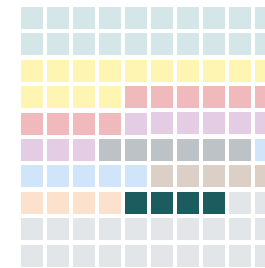
6.2% Government



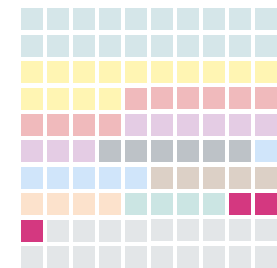
5.4% Manufacturing



4.0% Architecture, Engineering, and Construction



4.0% Energy & Utilities



3.3% Associations & Non-profit Organizations

15.7% Other\*



\*Other includes all remaining industries tracked by Savills Research & Data Services and not represented in the top 10

**Office investment sales market continues to be largely frozen as cost of capital remains high and distressed opportunities have been slower to materialize**

# Investment Sales Activity Has Slowed Significantly in the Office Sector

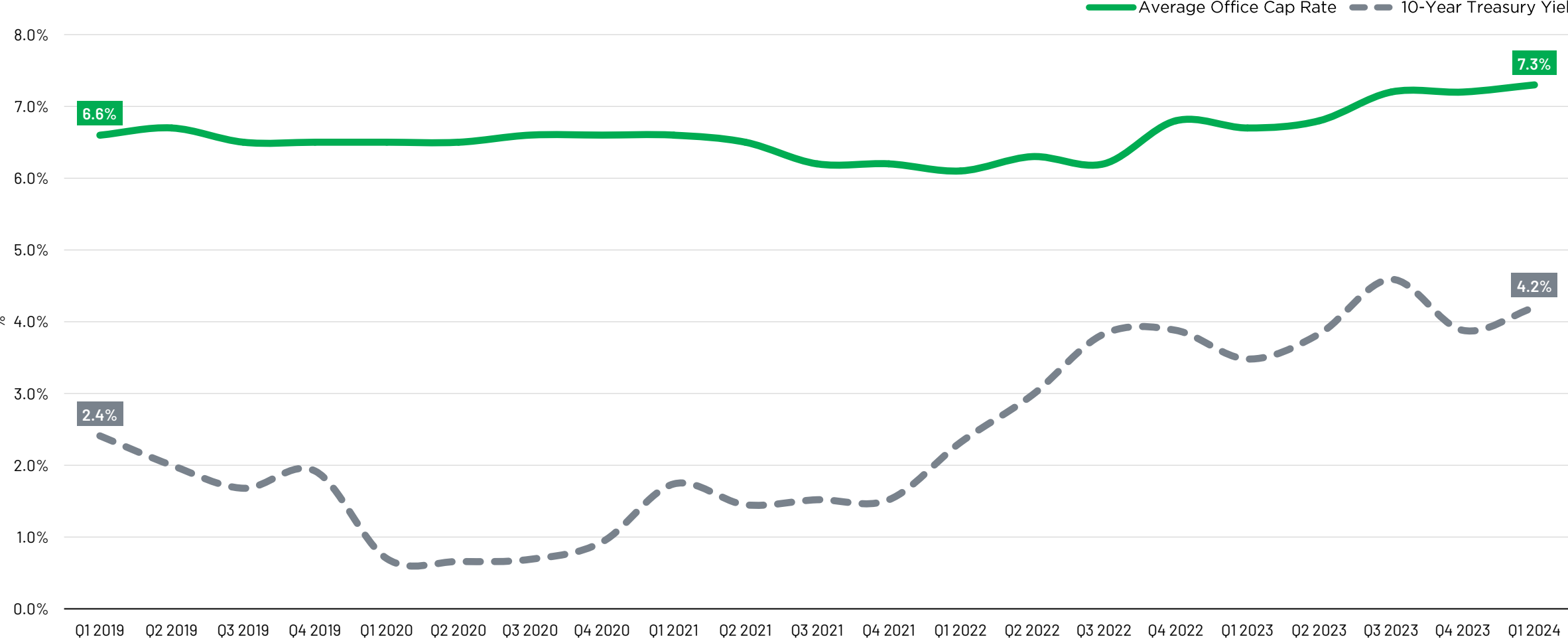
Total Office Property Sales Volume (\$ billions)



Source: MSCI Real Capital Analytics

# Office Cap Rates Have Increased as Interest Rates Have Increased

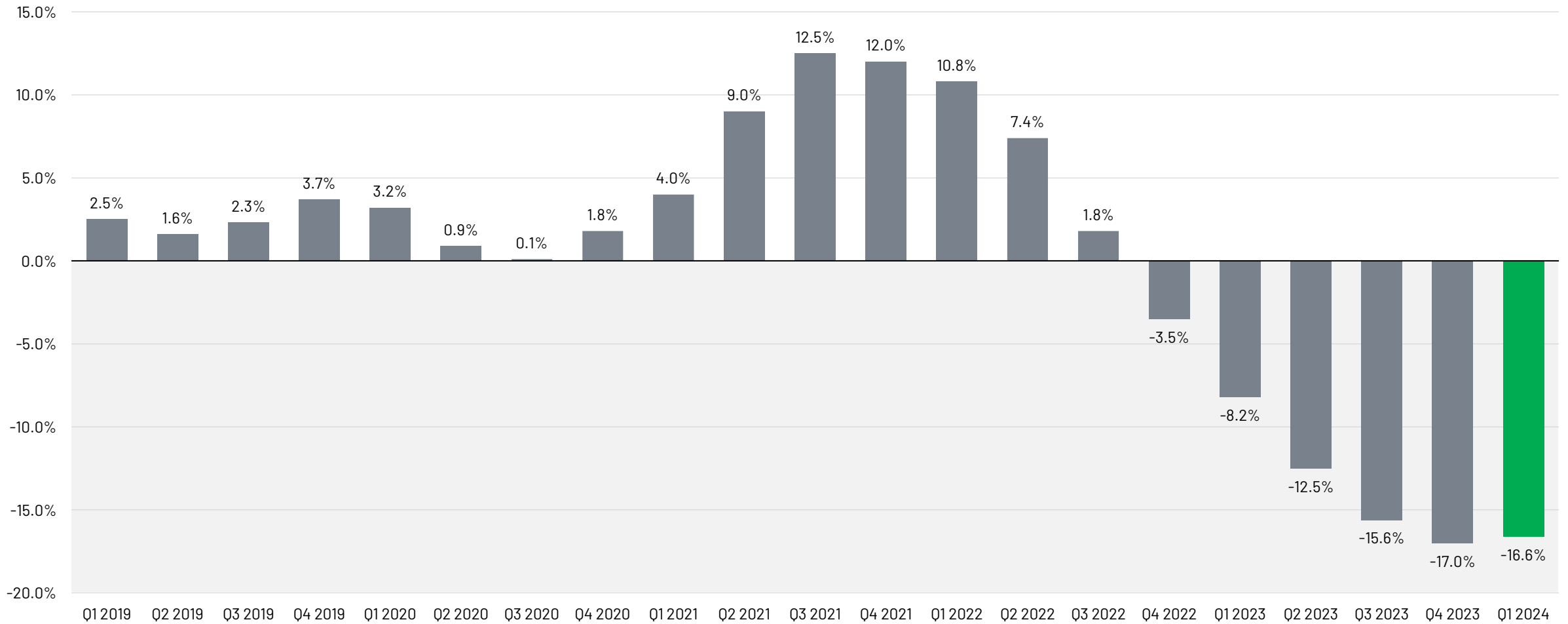
CBD and Suburban Office Average Cap Rate vs 10-Year Treasury Yield (%)



Source: MSCI Real Capital Analytics, Federal Reserve Economic Data (FRED)

# Office Property Valuations Have Decreased and Continue to Drop

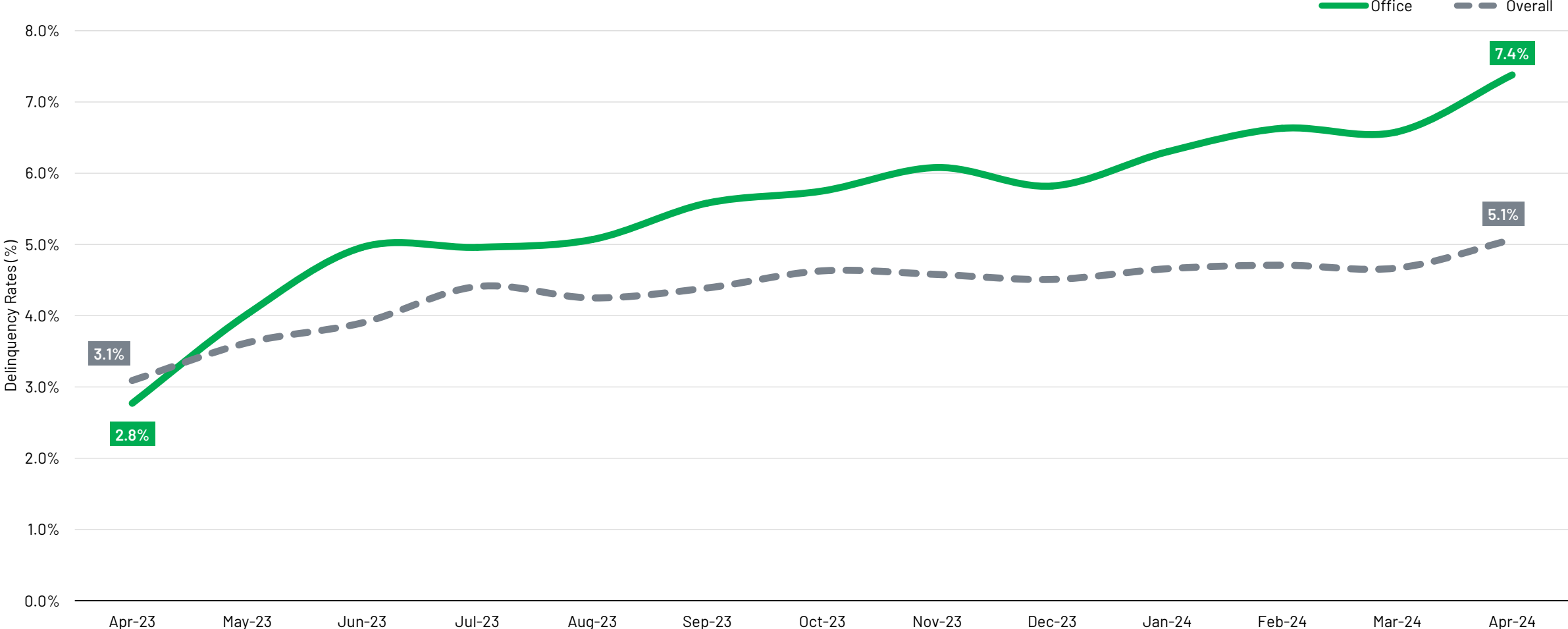
MSCI Real Capital Analytics Commercial Property Price Index (CPPI) – year-over-year Change (%) by Quarter



Source: MSCI Real Capital Analytics

# CMBS Delinquency Rates Have Spiked in the New Year

Overall Loan Delinquency vs Office Loan Delinquency (%)



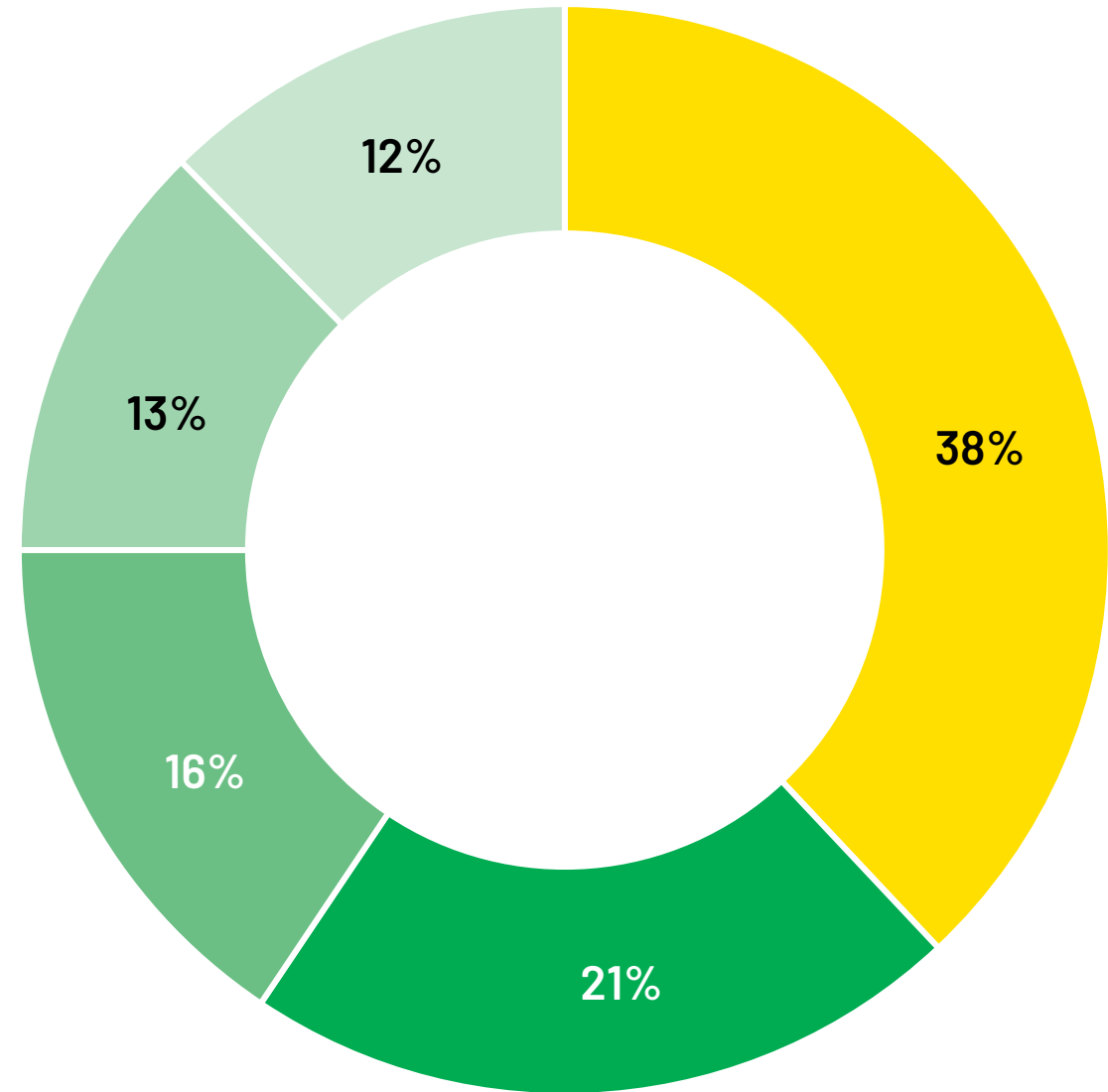
Source: Trepp

# CMBS Remains Only 13% of Total Commercial/Multifamily Debt Outstanding

Est. \$4.69 trillion

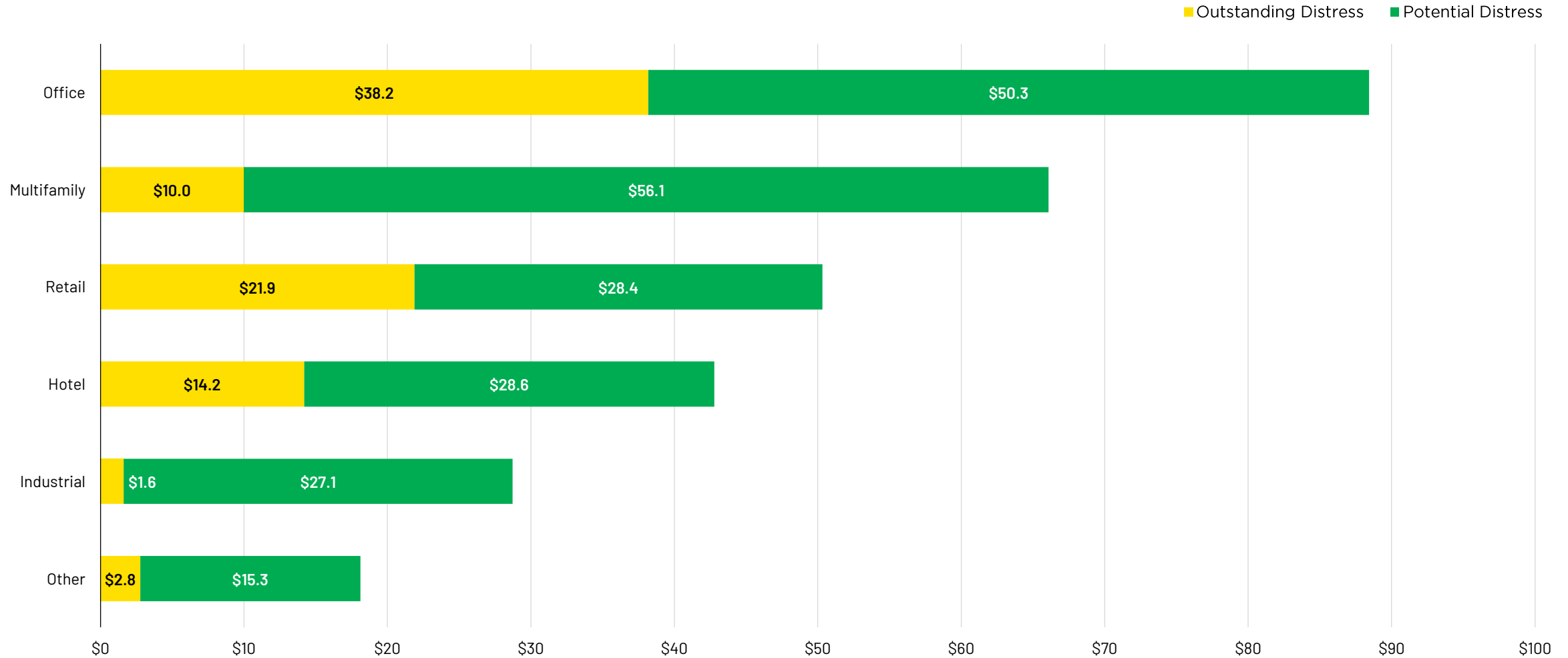
Commercial/Multifamily Debt Outstanding from Mortgage Bankers Association

- Banks & Thrifts
- Agency and GSE Portfolios and MBS
- Life Insurance Companies
- CMBS, CDO and Other ABS Issues
- Others



# Commercial Property Loan Distress Led by Office and Multifamily Sectors

Balance of Distress by Property Type - Cumulative through Q1 2024 (\$ billions)



Source: MSCI Real Capital Analytics



# Occupiers with Superior Credit Continue to be in the Driver's Seat as Property Owners Realize Interest Rates Now Higher-for-Longer

## Higher-for-longer interest rates, falling valuations, soft market fundamentals

- Interest rates remain high as inflation continues to be above the Federal Reserve's 2% target
- Shift from historically low interest rate environment has led to increase in cap rates and decrease in property valuations
- Capital remains available but is expensive, especially as banks have pulled back on new lending
- Office property fundamentals remain soft despite higher Return to Office rates

## Approximately \$959 billion in outstanding CRE loans will mature 2024

- In Q1 2024, \$88.6 billion in commercial real estate loans are now distressed which is the highest level since 2013
- Office property loans comprise \$38.2 billion or 43% of all commercial real estate loans which are currently distressed
- Another \$50.3 billion in office loans have been identified as potentially distressed
- Expect office building owners to work on more lender-facilitated sales or to give back their properties to their lenders in 2024

## What does this mean for office occupiers over the short-term?

- Critical to understand underlying debt situation of ownership, as well as the property's financial situation and capital stack
- Distress does not necessarily mean rents will decline or there will be a substantial increase in concessions as owners might be constrained by their lenders
- Occupiers in a strong financial position with superior credit remain in the driver's seat as landlords aggressively look to preserve occupancy and lock-in cash flow

# Thank you

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## MICHAEL SOTO

Vice President, Research West  
North America

+1 213 553 3833 | [msoto@savills.us](mailto:msoto@savills.us)

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## MARISHA CLINTON

Vice President, Research East  
North America

+1 212 588 3480 | [mclinton@savills.us](mailto:mclinton@savills.us)

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## CAITLIN BARROZO

Research Manager, Southern California  
North America

+1 949 706 6588 | [cbarrozo@savills.us](mailto:cbarrozo@savills.us)

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## SID JAITLY

Data & Technology Manager  
North America

+1 206 773 2276 | [sjaitly@savills.us](mailto:sjaitly@savills.us)

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