

COVID-19 puts a damper on Phoenix office market as growth cycle is interrupted

Although Arizona's stay-at-home order was lifted in mid-May, the Phoenix area increasingly struggled with growing cases of COVID-19 as the second quarter progressed. State leaders were forced to tighten restrictions on many businesses at the close of June to stem the outbreak. Pandemic uncertainty and business disruption ultimately caused a jarring impact on Phoenix office market fundamentals. Leasing activity fell by 46.0% from the first quarter and marked its lowest level in more than a decade. Decision makers were forced to re-evaluate strategic priorities, including office space requirements, causing many real estate decisions to be put on hold.

Availability increases due to influx of sublease space; landlords hold off on repricing

Availability across the Phoenix office market was up 80 basis points (bps) from last quarter to 19.0%. Likewise, Class A availability lurched up to 18.6%, jumping 90 bps. Much of the increase was due to sublease space that has flooded the market to date in 2020. Phoenix has witnessed sublease inventories rise by nearly 50% since January. Without a rapid economic resurgence and improvement in containing COVID-19 spread in Arizona, it is expected that both direct and sublease availability will tick upward throughout the remainder of the year. Despite the jump in availability, landlords have not yet been compelled to reprice. Overall asking rates across Phoenix have risen 2.7% year over year to \$28.06 per square foot (psf). Class A rates pushed up to \$31.97 psf, increasing 2.1% from a year ago.

Transaction volume dips sharply as occupiers digest uncertainty

While the market saw transaction volume nearly halved this quarter, several of the popular East Valley submarkets including Tempe, Airport Area and Chandler each witnessed deal activity fall by over 80 percent as measured by rentable square feet transacted. Among deals able to be completed, Sodexo, Inc. signed the largest deal of the quarter, renewing for 59,802 square feet (sf) at 9440 N 25th Drive in the Northwest Phoenix submarket. In Tempe, Morgan Stanley leased 43,975 sf at the new Phase V development of Rio2100. While a rebound in office leasing activity is expected to follow, the timing and magnitude of this boost remains unknown.

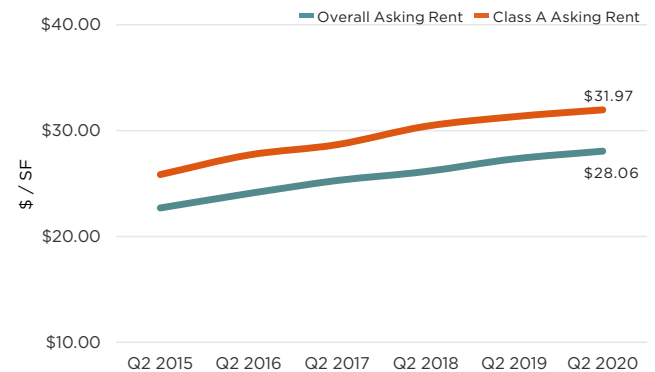
Outlook

- Despite the current uncertainty, Phoenix will remain an attractive option for occupiers in a post-COVID environment due to its low population density and affordable cost of doing business, among other reasons
- Moribund deal activity will likely continue in the near term as real estate decisions are put off until the economic disruption caused by COVID-19 clears and businesses can return to the office
- Opportunistic tenants may be able to take advantage of current market conditions to renegotiate and increase efficiencies within their current premises

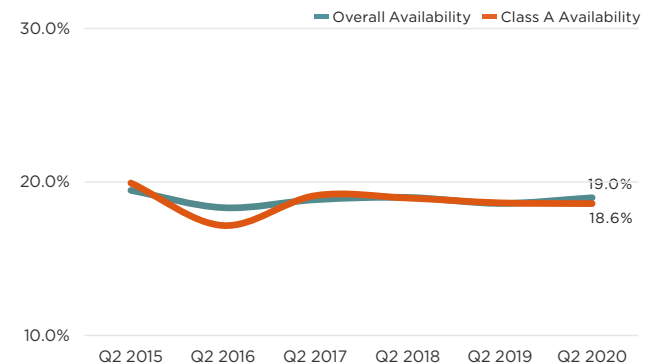
KEY STATISTICS

| | Q2 2019 | Q2 2020 | y-o-y Change |
|----------------------------|-----------|------------------|--------------|
| Inventory | 102.6 MSF | 103.9 MSF | ▲ |
| Availability Rate | 18.6% | 19.0% | ▲ |
| Asking Rental Rate | \$27.33 | \$28.06 | ▲ |
| Class A Asking Rental Rate | \$31.32 | \$31.97 | ▲ |
| Quarterly Leasing Activity | 2.1 MSF | 0.74 MSF | ▼ |

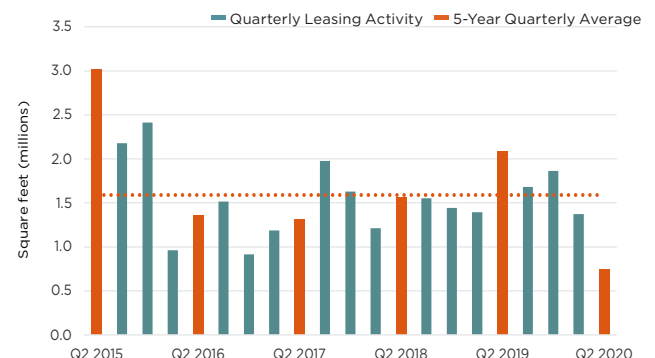
ASKING RENT TRENDS



AVAILABILITY TRENDS



LEASING ACTIVITY



MAJOR TRANSACTIONS

57.0%

major transactions were **renewals** by square footage

22.0%

of major transactions occurred in the **Tempe** submarket by square footage

33.6%

Professional Services sector tenants represented 33.6% of major transactions by square footage

| Tenant | Square feet | Address | Transaction type | Submarket | Industry |
|--|-------------|---------------------------|------------------|-----------------------|-----------------------|
| Sodexo, Inc. | 59,802 | 9440 N 25th Drive | Renewal | Northwest Phoenix | Professional Services |
| District Medical Group | 56,544 | 3141 N 3rd Avenue | Renewal | Midtown | Healthcare |
| Morgan Stanley | 43,975 | 2100 E Rio Salado Parkway | New Location | Tempe | Financial Services |
| Triwest Healthcare Alliance | 30,571 | 16010 N 28th Avenue | Renewal | Deer Valley/Airport | Healthcare |
| Hownd | 20,040 | 1840 E Guadalupe Road | New Location | Tempe | Professional Services |
| Ogletree, Deakins, Nash, Smoak & Stewart, P.C. | 18,801 | 2415 E Camelback Road | Renewal | Camelback Corridor | Legal Services |
| Experience Scottsdale | 17,718 | 4343 N Scottsdale Road | New Location | Scottsdale South | Professional Services |
| Carrington Mortgage | 17,431 | 585 N Juniper Drive | New Location | South Tempe/Ahwatukee | Real Estate |
| Symmetry Software | 13,306 | 14350 N 87th Street | Expansion | Scottsdale/Airpark | TAMI |
| The Federal Savings Bank | 12,445 | 5670 W Chandler Boulevard | New Location | South Tempe/Ahwatukee | Financial Services |

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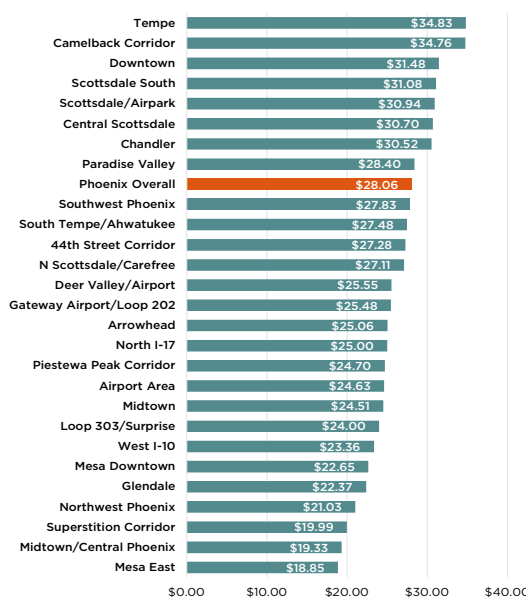
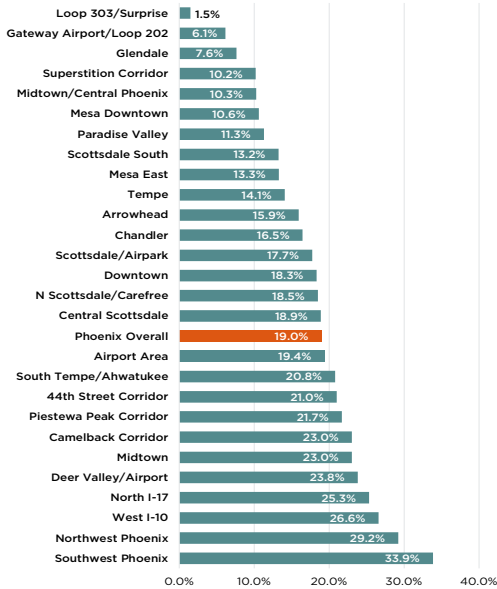
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AVAILABILITY RATE COMPARISON

Phoenix Submarkets

RENTAL RATE COMPARISON (\$/SF)

Phoenix Submarkets



Unless otherwise noted, all rents quoted throughout this report are average asking gross (full service) rents per square foot. Statistics are calculated using both direct and sublease information. Current and historical availability and rent data are subject to change due to changes in inventory.

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