

# MARKET TRENDS | SEATTLE

# OFFICE

3RD QUARTER  
2020

▼ ABSORPTION | ▲ VACANCY | ◀▶ RENTAL RATE | ▼ CONSTRUCTION DELIVERIES

Year-over-year change

Now, at the end of the 3rd quarter, we are starting to see some signs of the economic impact on the regional office from the pandemic which has yet to be contained. The initial impact was a skyrocketing of the unemployment rate to 16.6% due to the loss of 318,000 jobs during the shutdown of "non-essential" businesses. As some businesses began to re-open, the region started to see improvement in May.

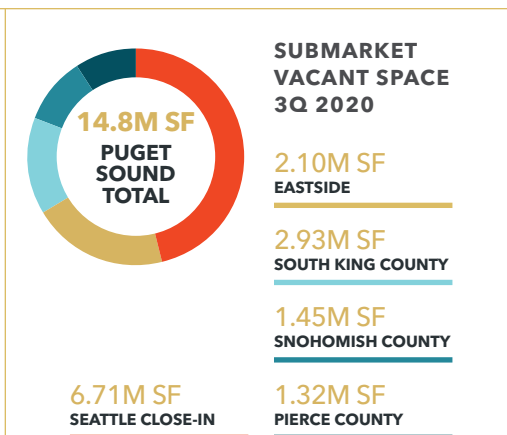
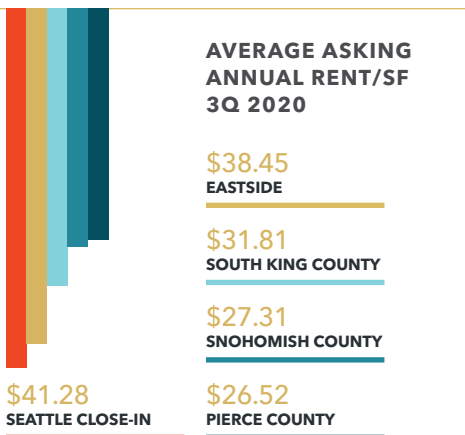
As of the end of August, the region has gained back 176,500 of the lost jobs, but the regional office market is seeing some of the trickle-down impacts from COVID-19. The 3Q 2020 data shows a spike in regional vacancy from 6.20% last quarter to 6.91% along with negative net regional absorption (-256,063 s.f.) for the first time since the 4th quarter of 2017. Sublet vacancy has jumped to 18% of total vacancy from 13% last quarter. Investment sales also remain depressed and leasing volumes are at levels below their typical mark. Fortunately, however, there are some positives with essentially all major office construction projects moving forward with a solid 60% of that space pre committed. Furthermore, the coronavirus has yet to trip up demand from the tech giants with Amazon committing to about 2M s.f. of Eastside office space and Facebook purchasing a newly delivered 400k s.f. surplus office building from REI at their HQ campus in the Spring District.

Moving forward, two important factors to consider for the regional office market long-term are the statewide economic implications related to both job loss and job growth and the long-term positioning of companies to embrace the work-from-home trend, which has been put into fast forward mode over the last six months. The regional unemployment rate in March stood at 5.4%, then nearly tripled to 16.1% in April before declining back

down to its current rate of 7.9%. The Puget Sound Economic Forecaster's most recent employment projection for 2020 is a year-end net loss of -6.1% followed by a positive job growth forecast of 3.0% for 2021. This indicates the economic metrics suggest that the employment picture should continue to improve near-term. As businesses and the economy continue to open back up and gain some momentum, we will be able to better measure how the normally fast paced and diverse Puget Sound market will rebound from the pandemic.

Real estate investors and real estate capital are mostly patient and focus on longer views that would likely bridge the effects of the current disruptions. So far, the data shows the economic impact of COVID-19 is negative, but the impact felt to the regional office market thus far has been relatively moderate. It is also important to note that the downturn could have been worse if not for stimulus money that went toward employees that lost jobs and businesses that were shut down. While we are clearly in a time of uncertainty with many questions remaining to be answered, the blow to the Seattle office market has been vetted by several factors thus far including a reasonable inventory of new regional construction with strong levels of pre-leasing, the rebound in local

continued on page 4



**3Q 2020 MARKET HIGHLIGHTS**

- REGIONAL OFFICE VACANCY** increased from 6.20% last quarter to 6.91%
- 5.4M SF** of new office under construction, primarily in Seattle and the Eastside
- 60% OF OFFICE SPACE** currently under construction is pre-committed
- AVG RENT QUOTES** in four of the five market areas decreased over the quarter
- CONTINUED TRICKLE** of sales activity

## SEATTLE CLOSE-IN REVIEW

### 10 MAJOR CONSTRUCTION PROJECTS

are ongoing that collectively total just over 2.7M+ s.f. with three projects expected to be delivered by the end of 2020; 23% pre-committed.

### FOLLOWING STRONG NET

**ABSORPTION** in the first half of the 2020 with 1,676,098 s.f. and 339K+ s.f. absorbed in the 1st and 2nd quarters, the Seattle market experienced negative net absorption of -581,207 s.f. for the 3rd quarter.

**OFFICE VACANCY** in Seattle currently stands at 7.03%, up 103 bps from last quarter's mark of 6.00% and up 190 bps from the 5.13% vacancy rate one year ago.

**AVAILABILITY RATE** increased over the quarter from 10.8% at the end of last quarter, to 12.2% currently.

**LEASING ACTIVITY** over the quarter was lackluster with CoStar reporting 78 total deals at 325K+ s.f. The CBD accounted for about one third of the total

lease volume at 19 deals totaling 114K+ s.f.

**ASKING RATES** in the Seattle CBD decreased to \$45.96/s.f./yr, from \$47.01/s.f./yr last quarter.

**VACANCY** in the Seattle CBD ended the quarter at 8.9%, up from 7.7% last quarter. The CBD availability rate also increased from 13.5% last quarter to 14.9% currently.

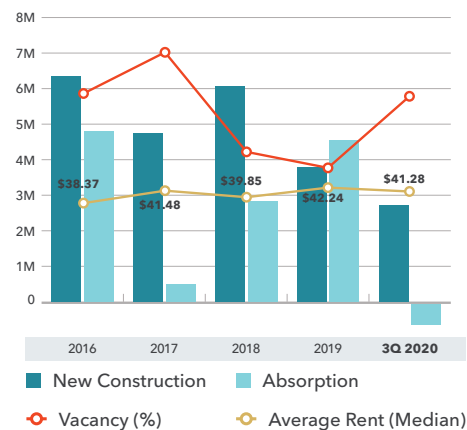
### PERIPHERAL SEATTLE SUBMARKETS

exhibit 3rd quarter vacancy rates of 5.0% in Ballard/U District, 2.9% for Lake Union and 4.3% in N Seattle/Northgate. Vacancy in Queen Anne/Magnolia sets the high mark at 12.1%.

**23% OF NEW CONSTRUCTION** (2.7M+ s.f.) in Seattle is pre-leased with lease negotiations stalled on most projects.

**CURRENT AVAILABLE NEW CONSTRUCTION** still appears manageable at 2.0M+ s.f. considering the Seattle market has historically absorbed about 2.3M s.f. annually.

## SEATTLE CBD / SURROUNDING AREA



### AFTER TWO CONSECUTIVE QUARTERS

with no significant office investment sales in Seattle, there were three investment sales above \$10M including First & Eagle (\$50.7M), Northlake Plaza (\$13.7M) and 830 4th Ave S (\$19.7M+) in 3Q 2020.

**AVERAGE RENT** for Seattle is \$41.28/s.f./yr, down \$0.16/s.f./year from \$41.44/s.f./yr last quarter.

## EASTSIDE REVIEW

**EASTSIDE OFFICE INVENTORY** currently stands at 52,741,909 s.f., comprising 25% of the regional office supply.

**OFFICE VACANCY** at the end of 3Q 2020 is the lowest of all market areas at 4.56%, up from 4.02% last quarter.

**THE AVAILABILITY RATE** has spiked to 6.40% from 5.00% last quarter.

**NET ABSORPTION** for the quarter was a healthy 605,460 s.f. bringing the YTD total for 2020 to for the Eastside to 956K+ s.f.

**OTHER OFFICE LEASING ACTIVITY** was nominal at 264K+ s.f. in total volume, aside from Amazon's pre-commitment to lease two Vulcan projects (555 Tower & West Main) at a combined 1.98M+ s.f.

**BELLEVUE CBD OFFICE VACANCY** increased to 4.6% at the end of the 3rd quarter, compared to 4.1% last quarter. The average CBD rent quote is \$52.23/s.f./yr currently, down slightly from \$53.01/s.f./yr last quarter.

**BELLEVUE CBD AVAILABILITY** shot up from 6.0% last quarter to 7.7% currently.

**7 MAJOR EASTSIDE** office projects are under construction (not including expansions at the Microsoft and Costco campuses) which collectively total 2.59M+ s.f.; a healthy 96% of which is committed.

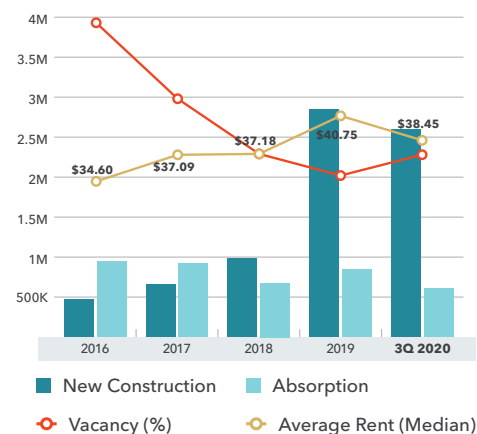
**AMAZON** has pre-leased Vulcan's 555 Tower project at 940k s.f. (under construction) and the West Main project at 1.03M+ s.f. which will contain three 16-17 story towers, further propelling Amazon's overall vision for 15,000 jobs on the Eastside.

**8 PROPOSED MAJOR OFFICE DEVELOPMENT PROJECTS** are currently in design review in Bellevue.

**VACANCY RATES** in peripheral Eastside submarkets remain low at 4.3% and 4.0%, for Kirkland and Redmond respectively.

**NOTEWORTHY SALES** include the transfers of REI's recently delivered HQ building to Facebook for \$367.6M

## EAST KING COUNTY



(\$919/s.f.) and Columbia West Building (Swift) for \$72M (\$516/s.f.).

**AVERAGE RENT QUOTE** for the Eastside is currently \$38.45/s.f./yr, down \$1.58/s.f./year from \$40.03/s.f./yr last quarter.

## SOUTH KING COUNTY REVIEW

**NEGATIVE NET ABSORPTION** of -65K+ s.f. at the end of 3rd quarter 2020 brought the 2020 YTD net absorption to negative -41K+ s.f., compared to 325K+ s.f. for all of 2019.

**OFFICE VACANCY** remains highest by far of the market areas at 13.17%, up slightly from 13.12% last quarter, but below 13.38% at the end of 2019.

**NO MAJOR DELIVERIES** or construction starts occurred this past quarter.

**ALASKA AIRLINES'** headquarters expansion building remains the

only significant office project under construction at 129K, to be delivered next quarter.

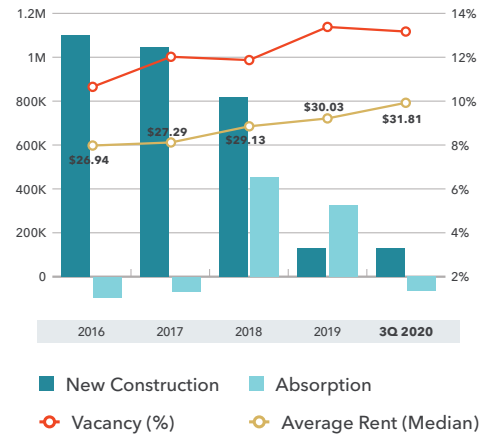
**39 OFFICE LEASE TRANSACTIONS** occurred over the 3rd quarter, totaling 139K+ s.f., or just over 3K s.f. per average deal size.

**SUBMARKET VACANCIES** for Renton/Tukwila and Federal Way/Auburn remain high at 17.9% and 15.3%, respectively.

**NO SIGNIFICANT** sale transactions.

**HIGH VACANCY** is expected to continue in the South King County market through 2020 and into 2021.

### SOUTH KING COUNTY



## SNOHOMISH COUNTY / NORTHEAST REVIEW

**THE NORTHEAST OFFICE MARKET** is third largest in the region, with a current office inventory of just over 22.6M+ s.f.

**VACANCY** increased over the 3rd quarter from 5.56% last quarter to 6.39% currently, a jump of 83 bps.

**AVAILABILITY RATE** also increased to 7.9% in the 3rd quarter 2020, from 6.7% in the previous quarter.

### BOTHELL/KENMORE SUBMARKET

**VACANCY** increased to 10.3% compared to 9.5% last quarter. The Everett CBD reports a current vacancy of 4.0%, down from 4.6% last quarter.

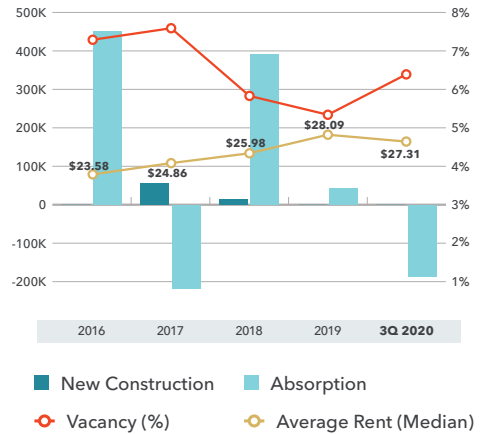
**THE NORTHEAST MARKET** continues to attract office tenants looking for affordable housing proximity with future light rail connectivity.

**AT AN AVERAGE RENT QUOTE** of \$27.31/s.f./yr, it is \$13.97/s.f./yr more affordable than the current average rent quote in Seattle at \$41.28/s.f./yr.

**NO SIGNIFICANT** sale transactions or new construction projects.

**THE NORTHEAST OFFICE MARKET** should see long-term improvement as businesses get squeezed out of close-in office space.

### SNOHOMISH COUNTY



## PIERCE COUNTY REVIEW

**OFFICE VACANCY** in Pierce County is 6.21%, above last quarter's mark of 5.90%.

**AVAILABILITY RATE** increased by 120 bps from 6.0% in 2Q to 7.2% currently.

**ONE THIRD** of the Pierce County office supply is in the Tacoma CBD which has a current 3rd quarter vacancy rate of 7.1%, down from 8.7% last quarter. The CBD availability rate increased to 9.3%, from 7.7% last quarter.

**LEASING ACTIVITY** remains sluggish at 33 deals averaging approximately 2,200 s.f. in size.

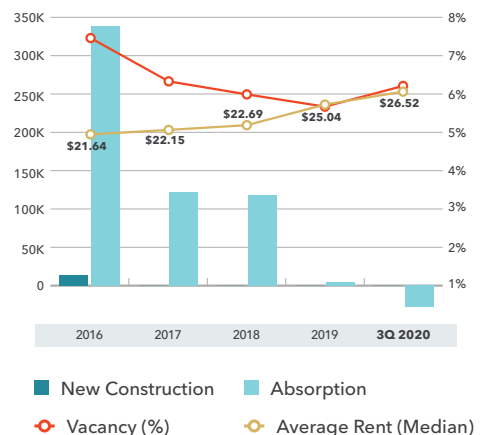
**NEGATIVE NET ABSORPTION** of -28K+ s.f. in the 3rd quarter, compared to -71K last quarter and positive 70K+ s.f. in the 1st quarter 2020. 2020 YTD net absorption totals -21K s.f. compared to 5K+ s.f. for all of 2019.

**SUBMARKET VACANCY** for Puyallup is high at 11.0% while the Spanaway submarket currently has 3.9% office vacancy.

**AVERAGE RENT** increased modestly to \$26.52/s.f./yr from \$26.14/s.f./yr last quarter.

**NO OFFICE PROJECTS** are currently under construction.

### PIERCE COUNTY



unemployment and the continued appetite for office space in the region by the tech giants. While sales activity will be slow to recover and the fundamentals of the regional office market are expected to be volatile, the region appears to be positioned to ride out the storm, but time will tell.

## VACANT SPACE/VACANCY RATE

At the end of the 3rd quarter 2020, the region has a total office inventory of 214.3M s.f. Current regional office vacancy stands at 6.91% with 14.8M s.f. of total vacant space, including sublet vacancy. Of the total vacant space, nearly 18% is from sublease vacancy, up sharply from 13% last quarter. The current regional vacancy rate increased 71 bps over the 6.20% vacancy rate last quarter and is 104 bps higher than the 5.87% vacancy rate at the end of 2019. All five of the region's market areas posted increases in vacancy over the 3rd quarter. Southend vacancy remains the highest in the region at 13.17% with the Eastside setting the low mark at 4.56%. The increase in regional vacancy over the quarter is due in no small part to negative net absorption of -256,063 s.f. for the quarter following very lackluster net absorption last quarter at 301K+ s.f. This compares to net absorption of 2.05M+ s.f. in Q1 2020 and 5.76M+ s.f. in net absorption for all of 2019. The Eastside was the only market to report positive absorption in the 3rd quarter at 605,460 s.f. Seattle posted the largest negative net absorption at -581K s.f. The regional availability rate, tracking space that is marketed but not necessarily completed or physically vacant, ended the quarter at 10.11%, up from 8.94% last quarter, setting the expectation for a near term rise in regional vacancy.

## NEW CONSTRUCTION ACTIVITY

As is stands at quarter end, 17 of the 18 major office projects under construction in the region are in Seattle and Eastside markets. There were three major deliveries over the quarter adding 922K s.f. of new supply including completion of the REI HQ Buildings in Bellevue, one of which just sold to Facebook. With several new office projects looming in the region, there were no new construction starts of note in the 3rd quarter. Among the existing close-in office projects under construction, 10 are in Seattle and collectively total 2.70M+ s.f. (23% pre-leased). Of these, three projects are expected to deliver by the end of 2020 delivering about 1.08M s.f. Comparatively, the Eastside currently has seven office projects totaling 2.59M+ s.f. underway, the largest of which is Vulcan's 555 Tower project at 940k, fully leased to Amazon. The Eastside projects are a very healthy 96% pre-committed. Amazon has also leased all Vulcan's 1.04M s.f. West Main office project, which is undergoing site work. Other proposed office projects in both the Eastside and Seattle are poised to commence construction, but it remains to be seen which projects will push through first. Fortunately for the region, the 18 projects under construction are collectively 60% pre-committed

## RENT FORECAST

Of the five market areas in the region, only the Tacoma market posted a nominal rental rate increase over the quarter while the other four saw average rent quote declines from the 2nd quarter. The rent increase in Pierce County was modest going from \$26.14/s.f./yr last quarter to \$26.52/s.f./yr currently, a bump of \$0.38/s.f./yr. The most notable rent decrease was in the Eastside going from \$40.03/s.f./yr last quarter to \$38.45/s.f./yr currently, a drop of 3.9%. The highest average rent continues to be in Seattle at \$41.28/s.f./yr which is a \$0.16/s.f./yr decline from the \$41.44/s.f./yr average last quarter. Seattle is followed closely by the Eastside (\$38.45/s.f./yr), then the Southend at \$31.81/s.f./yr and Snohomish County at \$27.31/s.f./yr. Tacoma posted the lowest average rent. At the end of the 2nd quarter, Bellevue CBD had the highest quoted average full-service rent of any regional submarket at \$52.23/s.f./yr, due to short supply. The average rent quote for the Seattle CBD is at \$45.96/s.f./yr with Tacoma CBD at \$27.47/s.f./yr, about half the Bellevue CBD rate.

## INVESTMENT MARKET

2020 continues to see very nominal office investment sale activity given the current pandemic and in the wake of the REET increase which took effect January 1, 2020. There remains a significant amount of uncertainty with buyers and sellers waiting on the sidelines to see how market conditions play out. Over the 3rd quarter, there were eight sales above \$10 million that closed (not purchased for land or repurposing), a slight uptick over the first two quarters. The largest transaction was the purchase of the one of the recently completed REI HQ Buildings in Bellevue by Facebook for \$367.6M (\$919/s.f.). Also trading over the quarter was Columbia West in Bellevue for \$72M (\$516/s.f.) and Seattle's First & Eagle Building for \$50.7M (\$669/s.f.). There were five other notable sales ranging in price between \$11M and \$28.5M. Total sales volume for the quarter was \$801.5M (among 67 transactions) compared to \$194.1M last quarter and \$4,683.3M in 4Q 2019. With the REET increase and market uncertainty, the slowing of investment sales is expected to continue through year end.



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