

MARKET TRENDS | SEATTLE

OFFICE

2ND QUARTER
2022

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

Quarter-over-quarter change

Through the 1st half of 2022, the office data shows another quarterly spike in regional vacancy going from 9.94% last quarter to 10.19% currently. Since the pandemic hit, the regional office market has seen a rise in vacancy 8 out of the last 10 quarters.

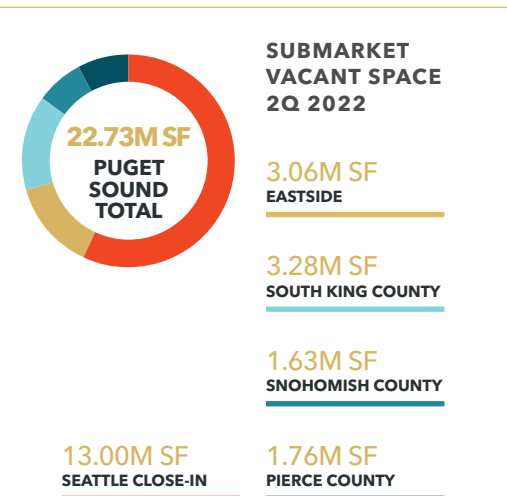
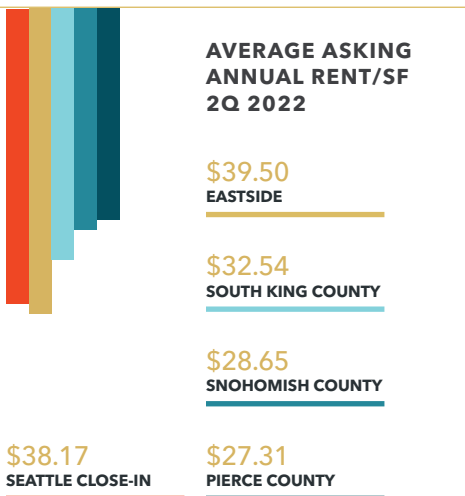
The change in vacancy over the past two and half years indicates a 432 bp increase from the 4th quarter 2019 vacancy mark of 5.87%. The office market also continues the ongoing trend of negative net office absorption after posting -1.235M+ s.f. in negative net absorption through the 1st half 2022 on the heels of -1.534M+ s.f. of negative net absorption in 2021. The percentage of sublet vacancy also continues to be historically high at 15% currently, but has declined from the peak about a year ago when it topped out at 22%. The largest office market (Seattle) in the region continues to see rising vacancy levels with a 61 bp increase over the quarter bringing the current vacancy to 12.94%. Conversely, the second largest market (Eastside) continues to post the lowest regional vacancy at a healthy 5.47%. Investment sale volumes slowed over the 2nd quarter 2022 and the amount of new construction totals 17 major regional office projects which are collectively 76% pre-committed.

While there has been improvement in the job market, the regional office market remains highly volatile. Looking ahead into the 2nd half of 2022, eyes will continue to be on job growth, but also the occupancy positioning of companies as offices repopulate which at this point has been at lower levels than pre-Covid with many employees continuing to work from home or adopt hybrid models. Inflation also remains a significant concern with

the June 2022 seasonally adjusted annual Seattle CPI forecast at 7.2%, compared to 7.3% nationally. The region has also recovered many of the lost jobs from the pandemic, but staffing shortages remain a significant challenge for the region. Puget Sound Economic Forecaster's June 2022 report forecasts total employment growth for 2022 at 4.0% compared to the national average forecast of 3.8%.

While the regional office market clearly remains unsettled particularly in Seattle, businesses have been operating without mandated masking requirements for several months. Vacancy has continued to rise and net absorption remains lackluster as regional office market trends continue to be volatile. Looking forward through 2022 will be telling as to how the regional office market transitions out of the pandemic. Indices to monitor will include vacancy levels (including percentage sublease vacancy), net office absorption, inflation and pre-commitment levels of new construction (currently at 76% region wide).

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2Q 2022 MARKET HIGHLIGHTS

REGIONAL OFFICE VACANCY increased from 9.94% last quarter to 10.19%

NEGATIVE net office absorption for the 2nd quarter 2022 is -343.4K+ for the region

7.29M+ SF of new office space under construction among 17 regional projects

76% OF THE OFFICE SPACE under construction is pre-committed

FOUR OFFICE SALES above \$20M over the quarter

SEATTLE CLOSE-IN

THERE ARE 6 MAJOR speculative office construction projects underway in Seattle containing 1.15M+ s.f. with two projects scheduled for 3rd quarter 2022 delivery; minimally pre-committed.

SEATTLE OFFICE VACANCY is currently 12.94%, up 61 bps from last quarter's mark of 12.33% and up 199 bps from 10.95% one year ago.

ONE MAJOR OFFICE DELIVERY over the 2nd quarter, the Google leased 520 Westlake project at 347.5K s.f.

THE AVAILABILITY RATE increased over the quarter to 17.2% from 16.8% indicating vacancy will likely remain at or above its current level near-term.

NET OFFICE ABSORPTION over the quarter was negative totaling -360,837 s.f. bringing the mid-year 2022 total to -1.08M+ s.f., compared to negative net absorption of -1.51M+ s.f. in 2021.

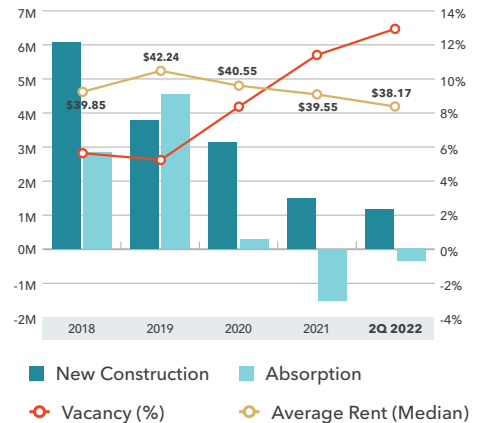
LEASING ACTIVITY was steady over the quarter with CoStar reporting 135 total deals at a total volume of 664K+ s.f. The CBD accounted for 54% of the total lease volume with 52 deals totaling 361.3K+ s.f.

AVERAGE RENT QUOTES in the Seattle CBD decreased to \$44.23/s.f./yr, from \$44.52/s.f./yr last quarter.

SEATTLE CBD VACANCY ended the 2nd quarter 2022 up sharply from 16.2% last quarter to 18.6% currently. The CBD availability rate also increased from 22.8% last quarter to 23.4% currently.

PERIPHERAL SEATTLE SUBMARKETS exhibited 2nd quarter vacancy rates of 5.3% in Ballard/U District, 6.9% for Lake Union, 7.5% in S Seattle and 3.7% in N Seattle/Northgate showing mostly downward vacancy trends. Queen Anne/Magnolia remains the high mark at 16.4%.

SEATTLE CBD / SURROUNDING AREA



THERE WERE 3 NOTABLE office sales over the quarter including the Lake Union Building at \$67M, Madison Centre at \$730M and Facebook leased Eleven 01 Westlake at \$151.5M.

AVERAGE RENT FOR SEATTLE is \$38.17/s.f./yr at the 2nd quarter 2022, down from \$38.85/s.f./yr last quarter.

EASTSIDE REVIEW

EASTSIDE OFFICE VACANCY is 5.47% currently, down 3 bps from 5.50% last quarter and down 60 bps from 6.07% a year ago. Eastside office inventory currently stands at 55.8M+ s.f.

THERE ARE 11 MAJOR Eastside office projects under construction (not including the 2.5M+ s.f. Microsoft campus expansion) collectively totaling 6.13M+ s.f.; which are 90% pre-committed.

THE EASTSIDE AVAILABILITY RATE has increased to 9.20% from 8.60% last quarter.

NET EASTSIDE OFFICE ABSORPTION during the quarter was a lackluster 9,145 s.f., although second highest in the region. Midyear 2022 net absorption totals 31.3K+ s.f. compared to 842K+ s.f. for yearend 2021 and negative absorption of -155K+ s.f. in 2020.

THE CURRENT AMOUNT of available new office construction to absorb is 586K+ s.f., which is manageable from a historic absorption perspective (541K+ s.f. annually-10 yr avg.).

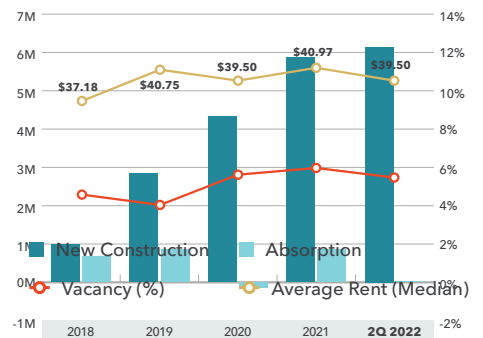
MODEST Eastside office leasing over the quarter with CoStar reporting 109 deals totaling 384K+ s.f. in total volume.

BELLEVUE'S CBD office vacancy increased slightly to 5.8% from 5.7% last quarter. The average CBD rent quote is \$53.68/s.f./yr currently, down 2.7% from \$55.15/s.f./yr last quarter.

THERE WAS ONE notable office delivery over the 2nd quarter, the Google leased 503 6th St. project at 136K s.f.

VACANCY RATES in key peripheral Eastside office submarkets remain very low at 1.8% and 5.0%, for Redmond and Kirkland, respectively compared to 1.8% and 6.4% last quarter, respectively.

EAST KING COUNTY



NO NOTEWORTHY 2Q 2022 office sales on the Eastside, although several office projects have sold for redevelopment.

THE AVERAGE RENT QUOTE for the Eastside is currently \$39.50/s.f./yr, down \$0.28/s.f./yr from \$39.78/s.f./yr last quarter.

SOUTH KING COUNTY REVIEW

OFFICE VACANCY in South King County remains highest in the region at 14.47%, down from 14.78% last quarter and the market peak of 15.32% one year ago in the 2nd quarter 2021.

THE SOUTHEND posted positive net absorption of 60,650 s.f. during the 2nd quarter 2021. This brings the mid-year 2022 total net absorption to -163.6K+ s.f., compared to year-end 2021 net absorption of 84.2K+ s.f.

CURRENT SUBMARKET VACANCIES for Federal Way/Auburn and Renton/Tukwila remain high at 12.5% and 20.2%.

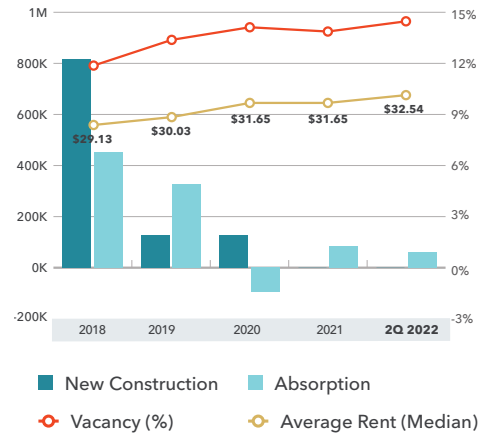
THERE ARE NO major office projects currently under construction.

47 OFFICE lease transactions reported in the 2nd quarter 2022 totaling 107.7K+ s.f., averaging just under 2,300 s.f. per deal. The average rent quote increased slightly over the quarter to \$32.54/s.f./yr.

DVA FEDERAL WAY BUILDING sold for \$93.5M (\$583/s.f.) at a reported cap rate of 4.0%.

WITH 15.1% availability, Southend vacancy is expected to remain high through the second half of 2022.

SOUTH KING COUNTY



SNOHOMISH COUNTY / NORTHEND REVIEW

THE NORTHEND office market has a current office inventory of 22.9M+ s.f. among 1,702 surveyed office buildings, an average size of 13.5K+ s.f.

NORTHEND OFFICE VACANCY decreased from 7.23% last quarter to 7.11% currently, a change of 12 bps.

66 OFFICE LEASE TRANSACTIONS over the quarter, totaling 244K s.f., or 3,700 s.f. average size.

THE AVAILABILITY RATE decreased from 8.5% last quarter to 7.6% currently at the 2nd quarter 2022.

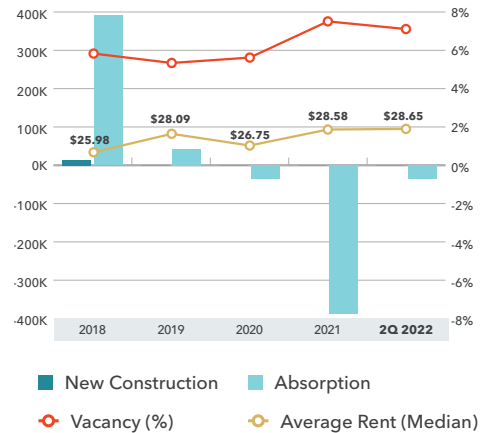
AT AN AVERAGE current rent quote of \$28.65/s.f./yr, this market is \$10.85/s.f./yr

more affordable than the current average Eastside rent quote of \$39.50/s.f./yr.

BOTHELL/KENMORE submarket vacancy decreased slightly to 13.5% in the 2nd quarter from 13.8% last quarter. The Everett CBD continues to report tight vacancy of 3.7% currently, down slightly from 4.0% last quarter.

THE NORTHEND office market should see long-term growth as businesses get squeezed out of pricier close-in markets and consider its appeal to local office tenants looking for affordability, housing proximity and future light rail connectivity.

SNOHOMISH COUNTY



PIERCE COUNTY REVIEW

OFFICE VACANCY in Pierce County currently stands at 8.31%, down from 7.82% last quarter and below the vacancy mark of 8.58% from one year ago.

THE OVERALL Pierce County availability rate increased over the 2nd quarter from 8.7% to 9.2% currently.

ABOUT ONE THIRD of the Pierce County office supply is in the Tacoma CBD which has a current 2nd quarter 2022 vacancy rate of 10.8%, up from 10.3% last quarter. The CBD availability rate increased to 12.2%, from 11.8% last quarter.

NET ABSORPTION for the 2nd quarter 2022 was negative at -18.5K+ s.f., bringing the first half 2022 net

absorption total to 33.3K+ s.f. This compares to year-end 2021 negative net absorption of -561K+ s.f..

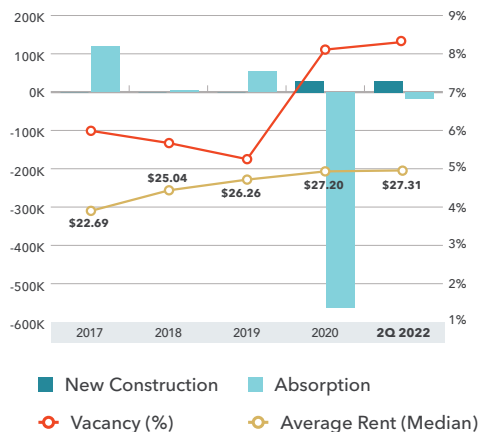
LEASING ACTIVITY over the 2nd quarter 2022 included 37 deals totaling 71.5K+ s.f. in total volume.

THE AVERAGE Pierce County rent quote increased by a modicum to \$27.31/s.f./yr in the 2nd quarter from \$27.27/s.f./yr last quarter.

NO MAJOR office sales or construction starts in the Tacoma market over the 2nd quarter.

SUBMARKET VACANCY for Suburban Tacoma is low at 3.1% compared to 2.9% last quarter while office vacancy in Gig Harbor increased over the quarter to 5.9% from 5.6% last quarter.

PIERCE COUNTY



VACANT SPACE/VACANCY RATE

Midway through 2022, the Puget Sound region has a total office supply of 223.1M+ s.f. After two quarters of declining vacancy at the end of 2021, regional office vacancy increased over the past two quarters to 10.19% currently. This is up from 9.94% last quarter and 9.60% at the end of 2021. This is the first-time regional vacancy has exceeded the 10% mark since the end of 2013. Furthermore, current vacancy is 440 bps higher than the ten-year low vacancy mark of 5.79% set three years ago in the 2nd quarter 2019. Of the current vacant inventory, 15% is from sublease space which is a reduction from 16% last quarter and 18% at year-end 2021. Three of the five regional market areas saw a decline in vacancy over the 2nd quarter. Seattle vacancy shot up sharply for the second consecutive quarter by 61 bps from 12.33% last quarter to 12.94% currently. The Southend continues to post the highest vacancy in the region at 14.47%, although decreased by 31 bps from 14.78% last quarter. Eastside remains the lowest regional vacancy decreasing slightly over the quarter to 5.47% from 5.50% last quarter. Tacoma vacancy jumped to 8.31% from 7.82% last quarter and Northend vacancy is 7.11%, declining from 7.23% last quarter. The increase in regional vacancy over the quarter is the result of negative net regional absorption of -1.23K+ s.f. at the halfway point for 2022, following negative regional net absorption of -1.53M+ s.f. in 2021 and continued historical high sublet vacancy levels (3.36M+ s.f.). Over the quarter, Seattle posted the largest negative net absorption of -360K+ s.f. followed by the Northend at -34K+ s.f. The regional availability rate ended the 2nd quarter at 13.24%, up from 13.00% last quarter and well above 8.96% from two years ago.

NEW CONSTRUCTION ACTIVITY

At the end of the 1st half 2022, there are 17 major office projects under construction in the region, all within the Seattle and Eastside markets. There were two notable deliveries over the quarter. In Seattle, 520 Westlake (Google) was completed adding 347K+ s.f. of new office inventory. The Eastside saw delivery of another Google leased office project, the 136K s.f. 503 6th St. building in Kirkland. There was one new construction start in Seattle (Latona at North Lake Union) at 157K+ s.f., excluding several large life sciences projects that also commenced over the quarter. Of the regional office projects under construction, 6 are in Seattle totaling 1.16M+ s.f. (0% pre-committed) and 11 are on the Eastside at 6.13M+ s.f. (90% pre-committed). The three largest regional projects are all Amazon committed towers in Bellevue including Vulcan's 555 Tower (940K s.f.), West Main (1.02M+ s.f.) and Bellevue 600 (999K+ s.f.). It is also noted that Microsoft is also well underway with their 2.5M s.f. campus office expansion which is not shown in the regional construction stats. Other proposed office projects are planned for both the Eastside and Seattle, but many Seattle developers are waiting to see how market conditions play out. Collectively for the region, of the 17 projects underway, 76% of the space is pre-committed.

RENT FORECAST

Three of the five market areas saw decreases in the average rent quotes for the 2nd quarter 2022. Seattle, the Eastside and Northend all posted lower average rent quotes. Seattle dropped from \$38.85/s.f./yr last quarter to \$38.17/s.f./yr currently, a 1.8% decline. The Eastside, which has the highest average rent in the region at \$39.50/s.f./yr, saw the average quote decrease from \$39.78/s.f./yr last quarter, a change of 28 bps. The Northend dropped nominally to \$28.65/s.f./yr. Both the Southend and Tacoma increased by a few pennies over the 2nd quarter. The Southend average rent quote went from \$32.51/s.f./yr last quarter

to \$32.54/s.f./yr while Tacoma improved nominally from \$27.27/s.f./yr last quarter to \$27.31/s.f./yr. Rent quotes are reported on a gross expense basis. The rent floor is currently set by Pierce County (\$27.31/s.f./yr). At the end of the first half 2022, the Bellevue CBD continues to have highest quoted average rent of any submarket at \$53.68/s.f./yr. Comparatively, the average rent quote for the Seattle CBD is \$44.23/s.f./yr. The Tacoma CBD is at \$27.49/s.f./yr, nearly half the Bellevue CBD rate.

INVESTMENT MARKET

2021 saw improving regional office investment sale activity which carried through the 1st quarter 2022 despite lasting impacts of the 2020 REET increase and lingering pandemic uncertainties among certain investors. For the 2nd quarter of 2022, investment sale activity slowed. Although trophy office assets remain in high demand, there is reluctance on the part of sellers and many buyers have taken a wait and see approach to evaluate the market over the next few quarters. That said, there has been a flurry of office building purchases for redevelopment and a continued steady flow of smaller investment and owner-user office transactions. During the 2nd quarter, the region saw 4 office sales closing above the \$20 million mark. Three of these significant transactions occurred in Seattle and one in the Southend. Seattle sales included the transfer of the Lake Union Building at \$67M+ (\$739/s.f.), Madison Centre at \$730M (\$959/s.f. & 4.3% cap rate) and Eleven 01 Westlake at \$151.5M (\$986/s.f.). For the Southend, the significant sale was the DVA Federal Way Building in Federal Way for \$93.5M+ (\$583/s.f. & 4.0% cap rate). Overall, cap rates remain low but are likely to push upward with the rise in interest rates. Total office sales volume for the quarter was \$1,183M+ (among 89 transactions) compared to \$1,667M+ last quarter and \$1,443M+ the quarter prior.



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