

FIGURES | TUCSON OFFICE MARKET | Q1 2023

Tucson Office Market Experiences Leasing Slowdown in Q1 2023

▲14.7%

Vacancy Rate

▼-79,963

SF Net Absorption

►0

SF Construction

▼\$22.74

FSG / Lease Rate

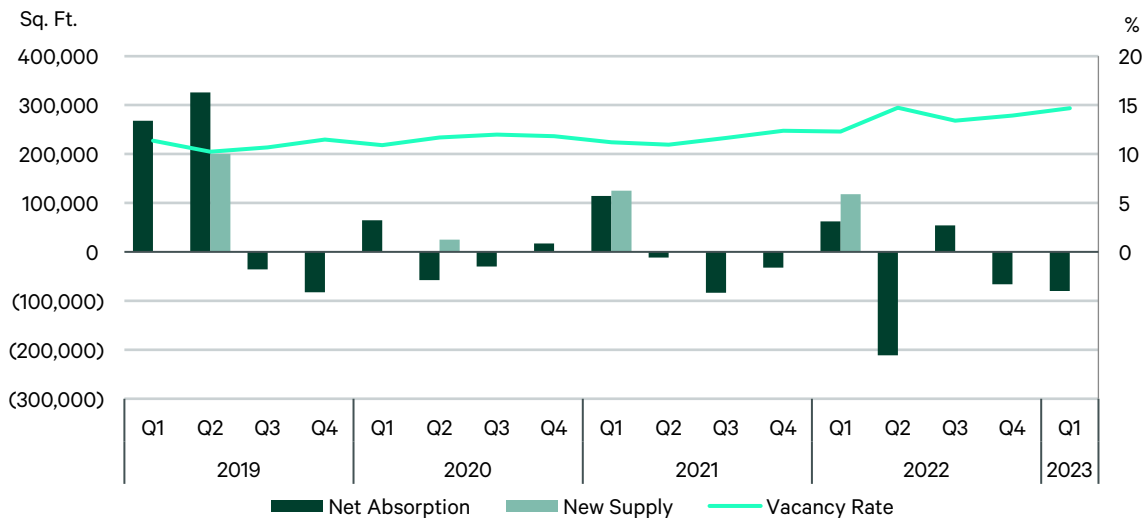
Note: Arrows indicate change from previous quarter.

KEY TAKEAWAYS

- The direct average asking full-service gross (FSG) lease rate declined to \$22.74 in Q1 2023, a 1.9% quarter-over-quarter change.
- The market experienced 40,055 sq. ft. of leasing activity but 79,963 sq. ft. of negative net absorption in Q1 2023, primarily due to East Central submarket move-outs.
- Vacancy increased 80 basis points (bps) and remained 380 bps higher than pre-pandemic levels.

The Tucson office market had a leasing slowdown in Q1 2023. The overall negative net absorption was driven primarily by multiple large tenant move-outs which negated the gross absorption of several smaller new leases. This had a notable impact on vacancy, which rose to 14.7%, a year-over-year increase of 240 bps. The average asking FSG lease rate decreased nearly 2.0% from the prior quarter, with Class A and C remaining virtually unchanged. Lastly, no new developments broke ground within the quarter.

FIGURE 1: Supply and Demand



Source: CBRE Research, Q1 2023.

Availability and Vacancy

Office space availability in Tucson increased by 20 bps, reaching 16.0%. The most significant change occurred in the East Central submarket, which had an 80 bps increase in availability, furthering its position as the most available submarket at 25.3%. Other submarkets experienced smaller shifts in availability. The least available submarkets in Q1 2023 were the Downtown and North Central submarkets which finished Q1 2023 at 8.2% and 7.4%, respectively.

Vacancy saw significant growth of 80 bps market-wide, ending Q1 2023 with a vacancy rate of 14.7%. Much of the rise in vacancy in the first quarter is attributed to already available space being newly vacant. Class A Office space experienced the most substantial shift in vacancy, increasing 160 bps from the previous quarter. Class C recorded a modest increase of 20 bps while Class B remained practically unchanged from Q4 2022. The North Central submarket remained one of the most stable and attractive submarkets with 6.6% vacancy.

Lease Rates

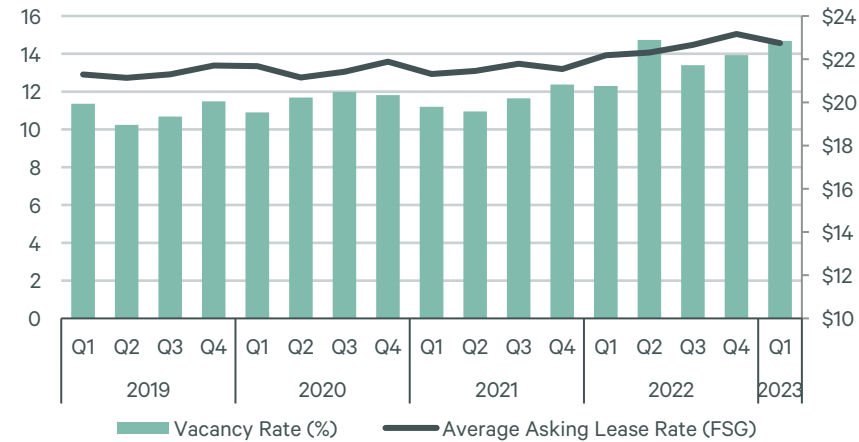
The Q1 2023 average asking FSG rate was \$22.74 per sq. ft., which represented year-over-year growth of 2.5%. Quarter-over-quarter changes amongst class types were minor, where Class A average asking lease rates slightly declined while other building classes increased. Downtown remained a premier office location with asking rates at \$23.64 per sq. ft., followed closely by the North Central submarket with asking rates of \$23.64 per sq. ft. On the contrary, the Northeast submarket recorded an asking lease rate of \$18.90 per sq. ft., a slight decrease from the quarter prior.

Net Absorption and Leasing Activity

The Tucson office market experienced 79,963 sq. ft. of negative net absorption in Q1 2023. Although the region saw several tenants occupy smaller spaces, these gains were negated by a handful of 10,000+ sq. ft. move-outs. Class A product had 84,618 sq. ft. of negative net absorption which greatly impacted the overall market. Class B recorded positive net absorption of 6,400 sq. ft.

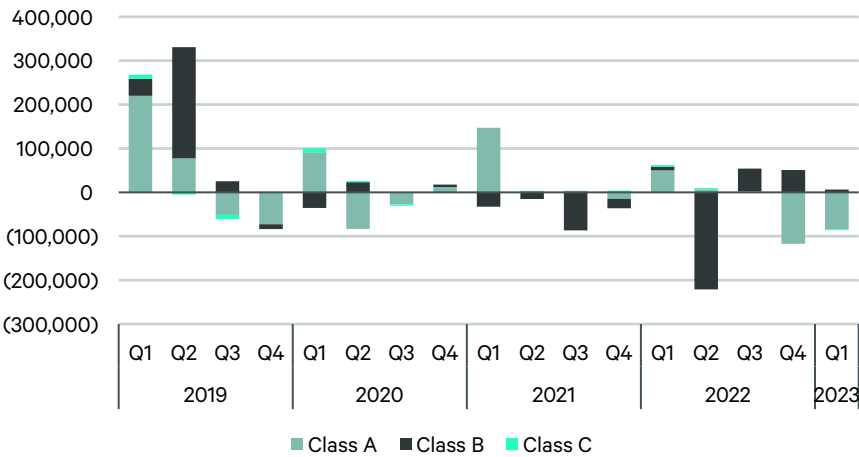
Nearly all submarkets recorded negative net absorption, but East Central made up the majority with -47,913 sq. ft. due to multiple large tenant move-outs at the Williams Centre II and 4801 E Broadway buildings. North Central experienced moderate leasing activity, with 23,595 sq. ft. of space leased within the quarter, making space even more limited in the submarket.

FIGURE 2: Overall Vacancy and Lease Rate



Source: CBRE Research, Q1 2023.

FIGURE 3: Net Absorption by Class (Sq. Ft.)



Source: CBRE Research, Q1 2023.

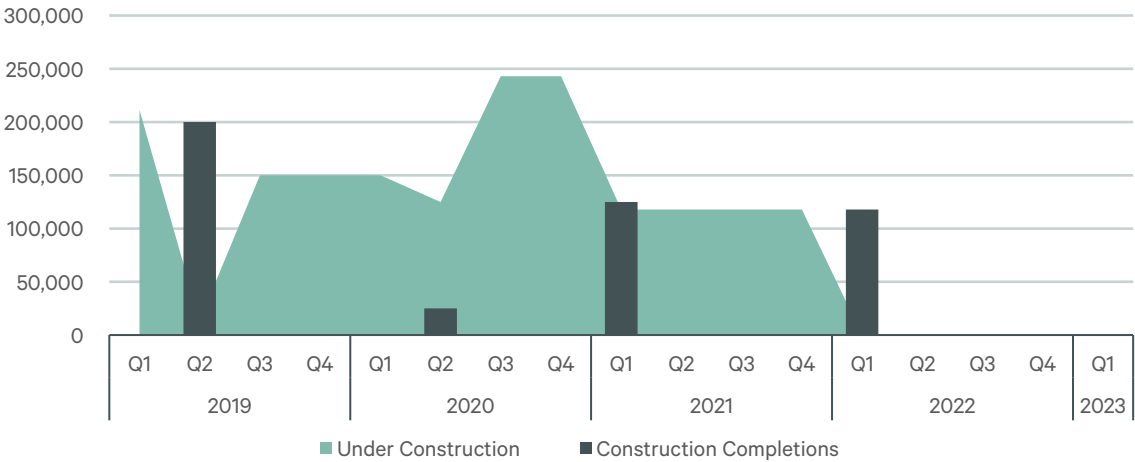
Development Activity

Tucson office development continues the trend of no projects breaking ground or delivering continued in Q1 2023. Rising vacancy and construction costs continue to deter office development. This trend is likely to continue as space remains abundantly available with a lack of tenant demand, along side interest rates which are expected to remain elevated into 2024. As CBD submarkets continue to struggle post-pandemic, high-value suburban submarkets like North Central are likely candidates for future planned developments.

Outlook

The Tucson office market continues to show several positive indicators of an opportunistic future ahead. Tucson remains a headquarter-friendly location due to ample Class A office space available and affordable asking lease rates. The market continues to capture value as a rising technology and life science market bolstered by a strong talent pipeline and favorable operating costs.

FIGURE 4: Under Construction and New Supply (Sq. Ft.)

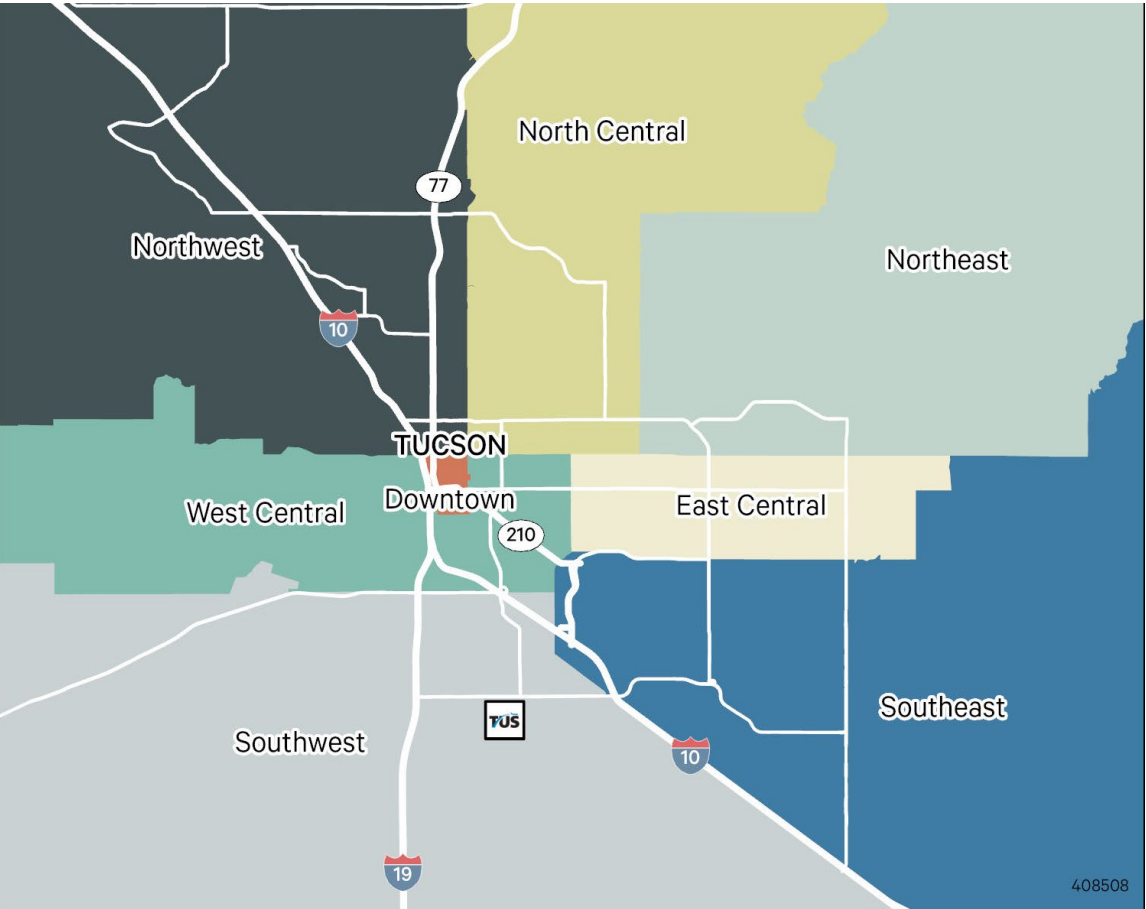


Source: CBRE Research, Q1 2023.

FIGURE 5: Submarket Stats

	Building Count	Net Rentable Area (Sq. Ft.)	Availability (%)	Vacancy (%)	Net Absorption (Sq. Ft.)		Under Construction (Sq. Ft.)	Construction Deliveries (Sq. Ft.)	Avg. Direct Asking Lease Rate (\$PSF/FSG)
					Q1 2023	2023 YTD			
Downtown	19	816,273	8.2%	8.0%	0	0	0	0	\$23.66
East Central	59	2,784,496	25.3%	22.6%	-47,913	-47,913	0	0	\$23.02
North Central	85	2,159,996	7.4%	6.6%	-1,161	-1,161	0	0	\$23.64
Northeast	53	995,019	21.3%	21.0%	1,156	1,156	0	0	\$18.90
Northwest	72	2,440,052	16.4%	15.0%	-31,165	-31,165	0	0	\$21.61
Southeast	2	119,157	12.5%	12.5%	0	0	0	0	\$27.00
Southwest	2	118,273	5.8%	5.8%	0	0	0	0	\$24.96
West Central	23	914,892	10.2%	9.4%	-880	-880	0	0	\$27.01
Tucson Total	315	10,348,158	16.0%	14.7%	-79,963	-79,963	0	0	\$22.74

Source: CBRE Research, Q1 2023.



Definitions

Available Sq. Ft.: Space in a building, ready for occupancy within six months; can be occupied or vacant. Availability Rate: Total Available Sq. Ft. divided by the total building Area. Average Asking Lease Rate: A calculated average that includes net and gross lease rate, weighted by their corresponding available square footage. Building Area: The total floor area sq. ft. of the building, typically taken at the “drip line” of the building. Gross Activity: All sale and lease transactions completed within a specified time period. Excludes investment sale transactions. Gross Lease Rate: Rent typically includes real property taxes, building insurance, and major maintenance. Net Absorption: The change in Occupied Sq. Ft. from one period to the next. Net Lease Rate: Rent excludes one or more of the “net” costs (real property taxes, building insurance, and major maintenance) typically included in a Gross Lease Rate. Occupied Sq. Ft.: Building Area not considered vacant. Vacancy Rate: Total Vacant Sq. Ft. divided by the total Building Area. Vacant Sq. Ft.: Space that can be occupied within 30 days.

Survey Criteria

Includes all office buildings 10,000 sq. ft. in Tucson Metro. Buildings which have begun construction as evidenced by site excavation or foundation work.

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