

Phoenix

Overall market activity remains muted, single sublessor drives negative absorption

- The Phoenix office market remains bifurcated, with 10% of buildings accounting for 56% of office vacancy, while 60% of buildings have no vacant space at all.
- Positive direct absorption was offset by an increase in sublease vacancy, making Q2 2023 the seventh consecutive quarter with negative net absorption.
- The pace of occupancy loss, however, decelerated by 60% from last quarter's net absorption of -704,275, showing signs of a nearing inflection point.
- Sublease space remains concentrated, with the top 10 sublessors accounting for 37% of total sublease availability.

The cloudy macroeconomic landscape persists, as the Fed held interest rates in June but has signaled for more hikes throughout the rest of the year. While investment inactivity has resulted in a stagnation in sales volume, proactive investors are making capital improvements to their assets in order to attract and retain tenants with quality space. On the other hand, office occupiers are opting to right-size and re-evaluate their office needs. While some are beginning to issue return-to-office mandates, others are introducing their unutilized spaces to the sublease market.

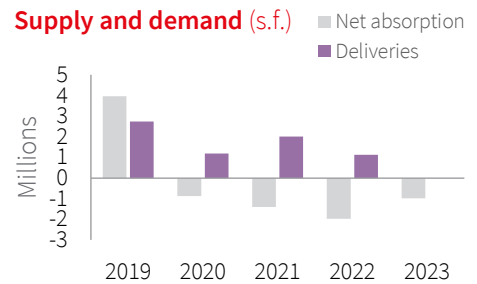
Carvana was the biggest driver of negative absorption this quarter, with the addition of 292,119 s.f. of plug & play sublease space at Marina Heights, a premium office business park located in Tempe. The online car retailer originally subleased the space from State Farm but has shrunk its office footprint considerably after a series of layoffs. With over 600,000 s.f. of sublease space on the market, Carvana alone makes up nearly 10% of total sublease availability.

CBD submarkets that have been hit hard since the onset of the pandemic experienced positive absorption this quarter, potentially an early indicator of recovery in the urban core. With an appealing location surrounded by amenities and a strong labor profile, the premiere South Scottsdale submarket saw the greatest increase in occupancy growth, with 198,509 s.f. of quarterly net absorption. Average direct asking rents have stabilized over recent quarters but are 3.5% higher year-over-year across the valley.

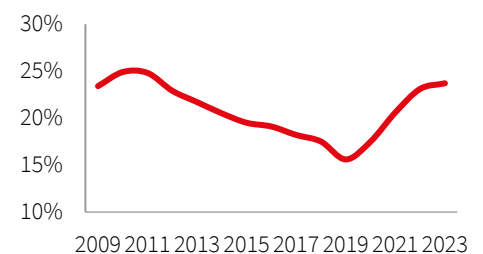
Outlook

While return-to-office mandates are gaining traction amongst large employers across the nation, the future of office remains murky as the elevated interest rate environment can create more distress for troubled landlords and occupiers. Despite the overarching uncertainty, the Phoenix market has maintained composure amidst economic pressures.

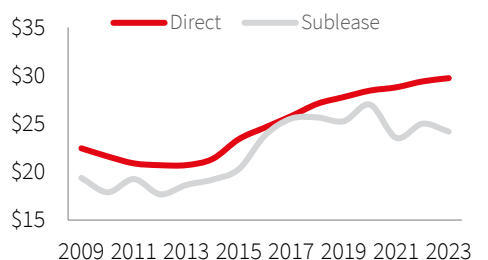
| Fundamentals | Forecast |
|----------------------|------------------|
| YTD net absorption | -978,323 s.f. ▼ |
| Under construction | 150,000 s.f. ▼ |
| Total vacancy | 23.7% ▲ |
| Sublease vacancy | 5,368,453 s.f. ▲ |
| Direct asking rent | \$29.73 p.s.f. ► |
| Sublease asking rent | \$24.18 p.s.f. ► |
| Concessions | Rising ▲ |



Total vacancy (%)



Average asking rent (\$ p.s.f.)



As part of a continuous process of data quality improvement, JLL Research has expanded its tracked inventory to include corporate owner-occupied properties. Buildings owned by government, educational and medical entities remain outside of statistical inventory.