INVESTMENT MARKET REPORT

Greater Phoenix
Q1 2018 Snapshot
Office & Retail

Presented to you by:

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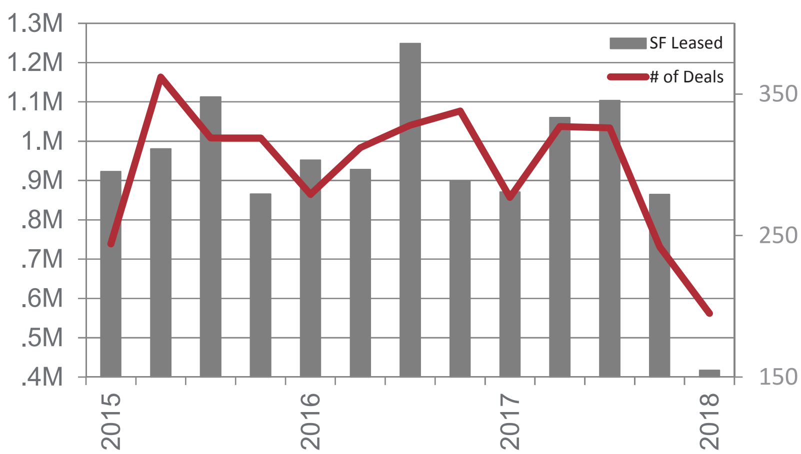
Q1 2018 Office Overview

The Phoenix office investment market ended the first quarter of 2018 in a steady fashion. Although the leasing efforts of investment grade office properties in the first quarter was much slower than years past, sales activity remained strong. Both January and February finished just under $200 million and $250 million in sales volume, respectively, while March held just $42 million in sales volume. Class A and Class B investment office properties are holding their value as it relates to Class C product. Looking at the Sales Activity chart, Class C product shows little to no sales until March thus far in 2018. On another note, vacancy decreased 0.1% since the end of 2017, leaving average rental rates steady in almost all classes of product. The current vacancy rate is 17.1% in all investment office properties with a current average asking rental rate at $24.55, up $0.39 from the end of 2017. The story remains consistent that most activity is in Class A or Class B value-add product. As for Class C (and some Class B) product owners, they must re-invest in their current properties to remain competitive in the current market.

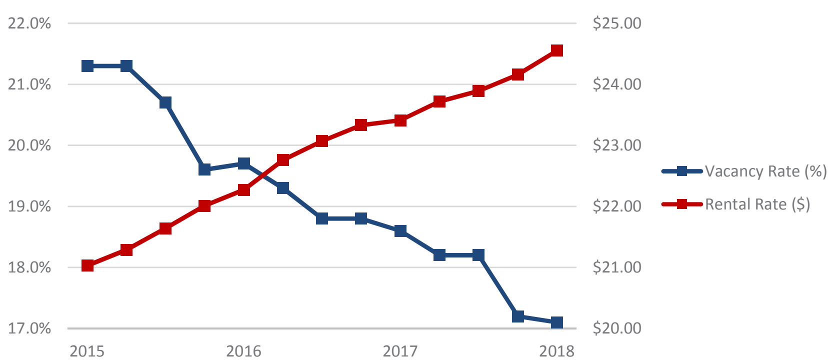
	Current
Vacancy Rate	17.1%
Net Absoprtion	228K SF
Average Asking Rates	$24.55/SF

Leasing Activity

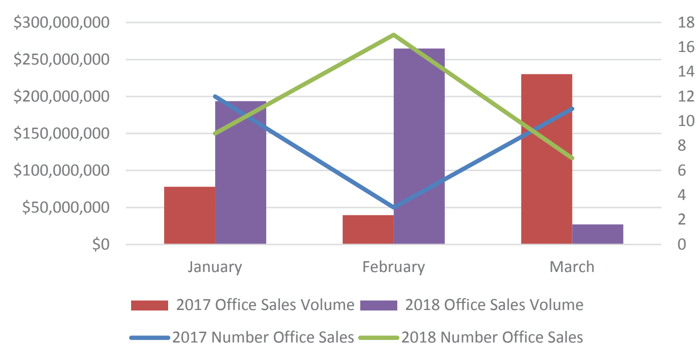


	From Q1 2017	From Q4 2017
Vacancy Rate	18.6%	17.2%
Net Absoprtion	251K SF	1.2MSF
Average Asking Rates	$24.55/SF	$24.16/SF

Rental & Vacancy Rates



Sales Activity



Q1 2018

12-Month Consumer Price Index ↑ 2.1%

30-Year Fixed Mortgage ↑ 4.4%

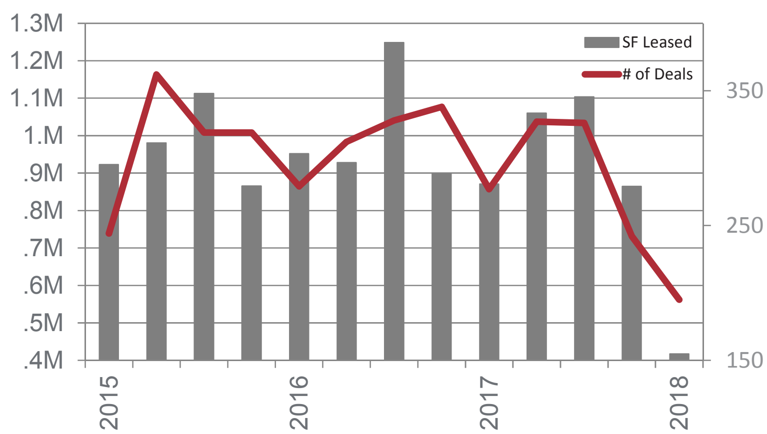
Phoenix Metro Unemployment ↑ 4.4%

Retail

The Phoenix Retail market remained strong through the first quarter of 2018. Vacancy rates in investment retail properties dropped .2% since the end of 2017 and 1.5% since Q1 2017. Average rental rates remained constant from Q1 2017 but did take a bit of a dip, seeing a $0.14 decrease from Q4 2017. Fear of the big box segment of the market seemed to slow the amount of sales in the shopping center and neighborhood center markets. With large retailers continually closing excess stores and Toys R Us filing for bankruptcy, skepticism is high in the larger retail markets. Because of the small amounts of sales for the investment side of retail sector, prices have continued to increase and cap rates have seemed to settle anywhere between the high 6 and low 7 mark. Although, net absorption remained strong in Q1 2018 from Q1 2017, almost 100K square feet more absorption at the year mark. The continued strong retail market can be attributed to the increasingly healthy economy and steady housing market we have been observing nationally and locally.

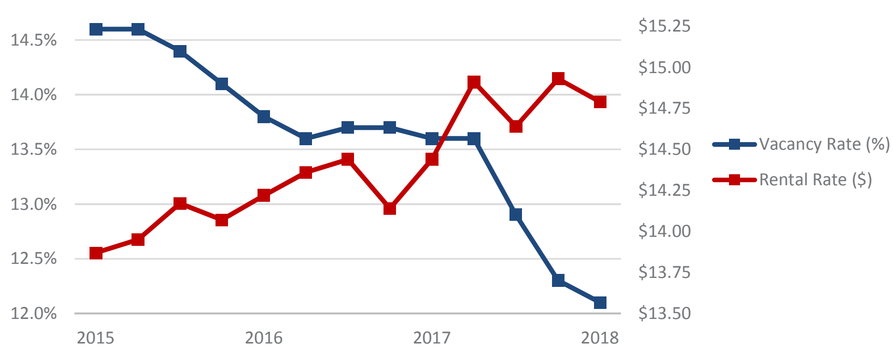
	Current
Vacancy Rate	12.1%
Net Absorption	188K SF
Average Asking Rates	$14.79/SF

Leasing Activity

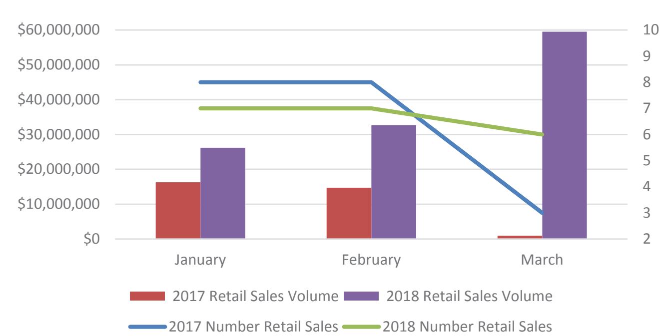


	From Q1 2017	From Q4 2017
Vacancy Rate	↓ 13.6%	↓ 12.3%
Net Absorption	↑ 87K SF	↓ 521K SF
Average Asking Rates	↑ $14.79/SF	↓ $14.93/SF

Rental & Vacancy Rates



Sales Activity



Phoenix Overview - Investment Market

As we all know in the investment industry the economy is the fuel that propels the real estate engine…and right now as we look at the fuel gauge, the tank is sufficiently full. The two most critical elements of the economy are job growth and population growth, in that order. As jobs are created the people have come to fill them during 2017 and continuing into the first quarter of 2018. In 2017 alone Maricopa County led the nation in population growth with a 1.7% increase or nearly 74,000 people.

As far as job growth goes, from March 2017 through March 2018 the Phoenix MSA added 65,000 new jobs to the civilian labor force (in calendar year 2017 it was 53, 500). Much of the growth is organic as companies already here continue to expand; however, much of the growth is from California companies relocating to Arizona primarily because it is a less expensive business environment. On another note, Phoenix has become a bastion of the technology scene. Through the first quarter of 2018 Phoenix has seen a large amount of job growth in the tech sector, to the extent we are now sometimes referred to as the “Silicon Desert.” Though, unemployment now stands at 4.1%, for Phoenix’s economy this extremely low unemployment will make it harder to fill new jobs. In fact the shortage of construction workers is currently being felt with higher tenant improvement costs across the Valley in all product types. This in turn is leading to longer lease terms in order to reduce the impact of these higher TI charges.

Let’s now take a look at the trend of rising interest rates. A few years ago many investors were extremely concerned about this trend, now that fear has greatly subsided. The Fed Funds rate was lowered to .25% after the beginning of the recession, where it stayed for 7 years. There were then 5 increases including the one in March of this year raising it to 1.75%, and it is forecasted that there will be two more ¼ point increases before year end. Investors were concerned these rate increases would translate to increases in cap rates and reductions in property values. Historically this has not proven to be the case, and many feel the same will be true now since interest rate increases normally occur during strong economic times. These conditions cause investors to be more aggressive in their underwriting and pricing with cap rate spreads absorbing the interest rate change.

In conclusion, looking at the transactional velocity, the number of transactions and the dollar volume in the first quarter of 2018 continued to be below the recent peak reached in 2015. The lack of “for sale” investment inventory was one reason for the decline in velocity, and this scarcity along with continued rental rate increases have pushed the average price per square foot to ever increasing highs.

Realizing Potential,

Delivering Results.

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