STRONG FUNDAMENTALS, INNOVATIVE ECONOMY FUEL TRIANGLE OFFICE MARKET

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The Raleigh metro has consistently placed nationally as a top place to live, work and play, and in 2017 that continues to be the case. The thriving central business districts (CBD) of Raleigh and Durham, as well as the world renowned Research Triangle Park, have fostered success and corporate growth in the life science/biotech, IT and pharma industries. Being home to three neighboring Tier 1 research universities (unmatched anywhere else in the country) makes Raleigh and the Triangle as a whole a hub for innovation, employee growth and office expansion.

The Triangle office market has continued strong fundamentals from 2016 into the first quarter of 2017. Average rental rates in the first quarter of 2017 increased $0.51 from first-quarter 2016, with downtown submarkets averaging bumps of over $2.75 from 2016. Class A office rents currently run at $25.62 per square foot for the Triangle region, with CBD districts demanding higher averages of $28.81 per square foot. Rental rates will continue to push up as the average Triangle vacancy rates continue their steady decline from 2008. Vacancy rates in the first quarter of 2017 remained in single digits at 7.9 percent, a drop of almost 200 basis points from 2016.

Employment numbers remain favorable, with unemployment rates reporting as low as 4.2 percent in March 2017. The Triangle also added over 3,200 jobs in 54 new and expanding companies, creating a total company investment of over $91 million in the first quarter of the year.

Large Developments

The Triangle is experiencing a boom of development activity as 2016 ended one of the hottest years of office construction in the Triangle, with over 2 million square feet of space under construction. It's the most Raleigh-Durham has had in its development pipeline in 10 years. Spread out over 15 projects, the new developments continue to focus in the strongest Triangle submarkets of CBD districts and the Research Triangle Park.

Owing to the live-work-play atmosphere and tenants' abilities to have denser footprints, the Downtown Raleigh, Downtown Durham and North Hills submarkets continue to attract marquee, Class A projects. Kane Realty's new Midtown Plaza in the upscale North Hills submarket delivered 329,213 square feet in the first quarter of 2017.

Kane is also under construction for 267,000 square feet of high-rise office space at the Dillon warehouse in Downtown Raleigh, with close to 1 million additional square feet proposed in the Raleigh CBD by rival developers. Durham's downtown currently has over 400,000 square feet under construction through a mixture of high-rise office and redeveloped warehouse spaces, a welcome sign in a submarket that has reported only 2 percent vacancy for the past six quarters.

Leasing Activity

While average runway time to negotiate a lease has methodically increased to over eight months in some scenarios, there has been no shortage of demand of tenants floating in the market for additional space. Through organic growth or relocations to Raleigh, leasing activity has kept developers busy. Delivery numbers support this with over 450,000 square feet completed in the first quarter. The Triangle offers companies more than just location, location, location. It offers the culture and lifestyle that attract and retain talent necessary for the TAMI (technology, advertising, media and information) and innovative cluster companies expanding in Raleigh and Durham.

Preleasing continues to be the name of the game in new Triangle developments with almost 50 percent of space under development already accounted for. Demand for big blocks of space is of particular concern. Notable deals such as INC Research signing a lease for 214,450 square feet and Align Technologies taking 60,000 square feet in RTP, as well as Allscripts and SunTrust Bank taking 270,000 square feet at North Hills, add to the general tenant anxiety and fear that competition is intense for large blocks. The heavily preleased new construction and limited large options in the market have not only push rental rates and absorption numbers up (overall absorption reached over 441,000 square feet for Class A space in the first quarter), but also demand for shadow spaces.

Increase in sublease activity, attributed mainly to growth that was unforeseen by many companies, has taken an unusual form in the Triangle. Backfill of sublease spaces that used to take half a year or longer has now been shortened to a few months. Rent concessions that halved asking rates are now close to face value in desirable sublease locations. The short time on the market and lack of concessions in the sublease market all point to what Triangle tenant's already know — rates are going up, space is in tight demand and the office market is admirably healthy in Raleigh and the Research Triangle.