

Phoenix

Healthcare Market Report 4th Quarter 2018

Quick Stats

103.6 K

Net employment gain from November 2017 to November 2018.

196.6 K

Square feet of positive medical office space absorption. 348.8 K square feet of positive absorption for 2018.

11.9%

Vacancy decreased 120 basis points from third quarter.

300.8 K

Square feet of medical space under construction.

\$23.50 PSF

Gross asking rents increased by 2.4% from third quarter 2018.

The Medical Office Market Ends 2018 Strongly.

As Phoenix's healthy economy attracts more people moving to the area for work, the healthcare sector is expanding to serve the growing population. Healthcare employment in the Phoenix Metropolitan Statistical Area (MSA) increased 4.6% annually since 2013. The Phoenix MSA is still an attractive retirement destination, growing as a hub in the southwest region for advanced healthcare and medical research. Khangura Development secured approval for a \$200 million mixed-use campus that will combine senior living options, medical offices, a hotel, clinic and nursing school on one 20-acre site in Mesa at Crimson Road and Hampton Avenue. The Phoenix branch of the Mayo clinic announced it will add 2,000 jobs, expanding its North Phoenix campus.

Rental Rates

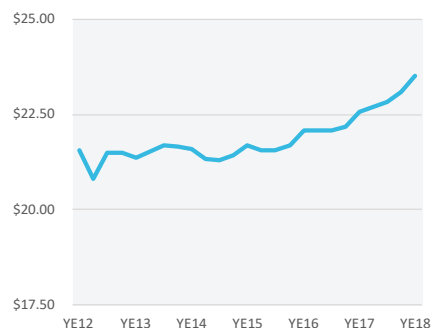
Fourth quarter 2018 rental rates were up 2.4% from third quarter, continuing to recover since 2013. Year-over-year rents increased 4.2%. The largest rent appreciations were in the South Tempe (6.7%), Camelback Corridor (4.7%) and West

I-10 (3.7%) Submarkets. Southwest Phoenix rents spiked in third quarter due to over 20,000 sf returning to the market and fourth quarter rents stabilized with a 2.9% increase. Rents should steadily rise in 2019 due to stable demand.

Vacancy

Vacancy rates dropped to their lowest level since 2007. At 11.9% they are 120 bps lower than third quarter 2018 and 200 bps lower than fourth quarter 2017. Positive or neutral absorption occurred in 21 of the 29 submarkets and occupancy was high in newly delivered inventory. Outside of the small 44th Street Submarket, vacancy rates shrunk the most in the Camelback Corridor (700 bps) and Northwest Phoenix (5.7%) Submarkets. Vacancy increased the most in Southwest Phoenix due to the loss of two tenants at 325 E. Baseline Road totaling 20,186 sf, and North Scottsdale where 45,500 sf was added to the inventory in new construction. Although vacant sublease space declined 29.7% in the fourth quarter, marketed sublease space nearly doubled.

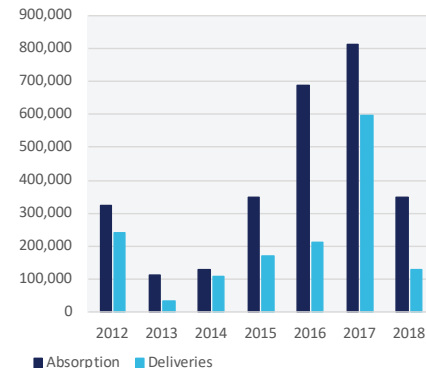
Rental Rates



Vacancy Rates



Absorption & Deliveries



Top Leases

Tenant	Building	Submarket	SF	Type
Cardiovascular Institute	Ironwood Office Square	Central Scottsdale	11,067	Direct
Cancer Treatment Centers of America	Copper Point Business Park	Gateway Airport/Loop 202	7,774	Direct
Recovia	1910 E. Southern Avenue	Tempe	7,150	Direct
Core Institute for Orthopedics	Boswell West Medical Office Building	Arrowhead	5,590	Direct
Vibrant Care	Shalimar Square	Tempe	5,200	Direct

Top Sales

Buyer	Building	Submarket	SF	Sale Price	Price/SF
Inland Real Estate Group of Companies, Inc.	Ironwood Cancer & Research Center - Portfolio	Phoenix	142,585	\$74,250,000	\$521
MB Real Estate Services Inc.	Thunderbird Plaza I	Arrowhead	35,419	\$12,150,000	\$343
Phoenix Venture #1 LLC	Camelback Medical Plaza	Northwest Phoenix	46,697	\$7,300,000	\$156
Robert R Pavese	Virginia Court - 2601 N. Third Street	Midtown	40,000	\$4,150,000	\$104
Chris A Carson	3333 N. Seventh Avenue	Midtown	13,424	\$3,700,000	\$276

Under Construction

Property	Submarket	Completion	SF	% Preleased/Owned
Estrella Medical Plaza II	Glendale	1Q19	125,000	78.5%
Mercy Gilbert Medical Plaza II	Gateway Airport/Loop 202	3Q19	80,000	72.5%
Mercy Medical Commons II	Gateway Airport/Loop 202	3Q19	56,000	39.3%
Ortho Arizona	Gateway Airport/Loop 201	3Q19	49,599	-
Black Mountain Center	Arrowhead	2Q19	25,401	-

Trends to Watch

Professional and business services sector employment began increasing in 2010 and grew through 2018. Sector growth is expected to continue in 2019



3.9%

The unemployment rate decreased 60 bps from January 2018.



19.1% to 15.7%

Vacancy decreased 340 bps and has generally trended downward since first quarter 2016.

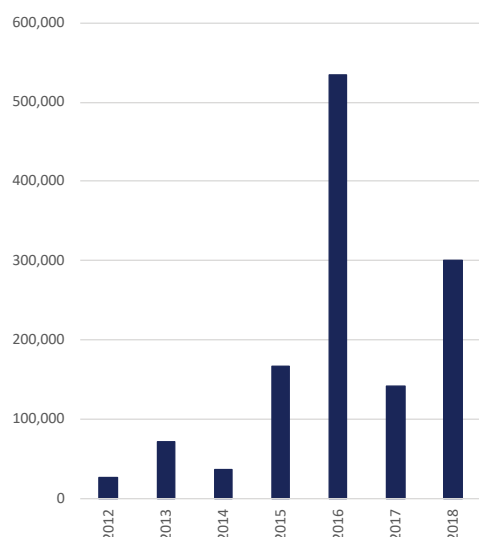


5.6%

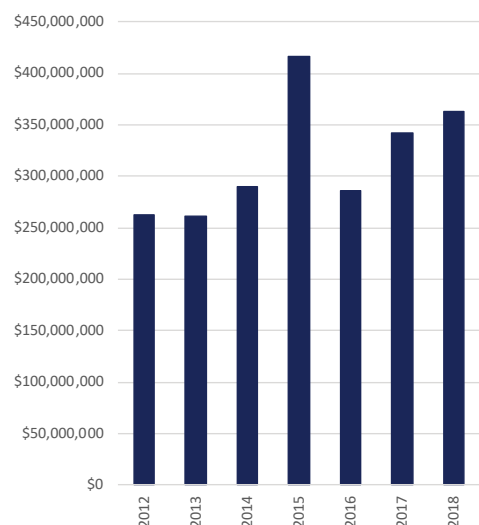
Professional and business services employment increased year-over-year.

The Phoenix economy continues to expand as financial services, software and technology companies take advantage of low business costs and a quality workforce.

Under Construction



Investment Sales



Leasing

Fourth quarter leasing activity turned absorption positive in the fourth quarter, resulting in positive 196,551 sf in the quarter and 348,796 sf in the year. Northwest Phoenix and the Camelback Corridor recorded the highest quarterly absorption, with 43,715 sf and 34,357 sf respectively.



Ironwood Office Square

Cardiovascular Institute signed the largest lease of the quarter, taking 11,067 sf in Ironwood Office Suites. 14.0% of leased RBA was in Chandler with half of the leases in Chandler occurring in the Bellagio Executive Center office condominium development.

Construction

2018 closed with 300,836 sf of medical office space under construction. The largest project is Estrella Medical Plaza II in Glendale, projected to finish in early 2019, adding 125,000 sf with 78.5% preleased.



Estrella Medical Plaza II

Preleasing is also strong in Mercy Gilbert II (72.5%), which will add 80,000 sf in third quarter 2019. Mercy Medical Commons II is also underway in the Mercy campus, adding 56,000 sf in third quarter 2019 with 39.3% preleased.

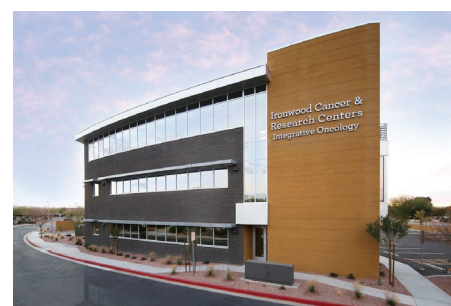
Glendale and Gateway Airport/ Loop 202 contain the four largest medical office construction projects: 9306 W. Thomas Road, Mercy Gilbert II, Mercy Medical Commons II and Ortho Arizona. The Arrowhead Submarket has two major projects. Black Mountain Center will add 25,401 sf in second quarter 2019, and a pad site at 6320 W. Union Hills Road should be completed by the end of the first quarter 2019, with 22,700 sf. Neither site has preleased space.

Investment Sales

Fourth quarter investment sales increased to \$107 million.

2018 sales volume increased by \$16.2 million from annual sales in 2017.

Annual 2018 volume was \$362.9 million, up from \$346.6 million in 2017, and the median cap rate declined 30 bps to 7.0%.



Ironwood Cancer and Research Center

The largest transaction was the portfolio sale of Ironwood Cancer and Research Centers' sale/lease back purchased by Inland Real Estate Group, Inc. for \$74.25 million (\$520.74 psf) at a 5.9% cap rate. The eight buildings were 100% leased at the time of sale. The largest non-portfolio transaction was the 49,967 sf Camelback Medical Plaza for \$7.3 million (\$156 psf) by Centum Health Properties to Gold West Investments.

Market By The Numbers

Submarket	Total RBA (SF)	Vacant Space Direct	Vacant Space Sublease	Class A Vacancy Rate	Class B Vacancy Rate	Class C Vacancy Rate	Available Space Direct	Available Space Sublease	Net Absorption (SF)	Avg. Ask Total (FS)
44th St	104,229	16,743	0	-	22.3%	7.0%	16,743	0	0	\$23.50
Airport Area	159,399	2,220	0	-	0.0%	4.1%	1,220	0	-2,220	\$21.90
Arrowhead	2,397,138	307,434	5,872	34.9%	10.6%	18.8%	281,096	5,872	2,961	\$26.68
Camelback Corridor	492,774	27,249	0	3.7%	3.4%	12.2%	22,202	0	34,357	\$26.49
Central Phoenix	1,347,022	221,116	0	-	19.0%	9.7%	221,116	0	16,117	\$22.78
Central Scottsdale	1,434,024	166,902	0	7.7%	12.8%	0.0%	164,021	0	18,385	\$24.64
Chandler	1,683,932	150,194	8,663	-	9.3%	12.1%	8,663	145,569	14,412	\$23.30
Deer Valley/Airport	1,374,674	160,954	4,574	11.8%	12.7%	6.4%	160,954	1,574	17,446	\$26.08
Downtown	654,757	47,421	0	0.0%	9.8%	10.0%	47,421	0	-21,570	\$24.42
Downtown Mesa	121,708	2,000	0	-	0.0%	2.1%	2,000	0	0	\$14.09
East Mesa	1,175,362	111,882	0	-	10.2%	8.2%	111,882	0	-3,435	\$18.79
Gateway/Airport/Loop 302	1,340,344	108,858	0	0.0%	8.8%	0.0%	108,858	0	6,414	\$27.81
Glendale	1,087,567	95,269	1,882	10.2%	8.8%	6.6%	91,089	1,882	-14,559	\$25.91
Loop 303/Surprise	1,153,161	152,285	11,962	-	14.9%	4.6%	151,697	11,962	48	\$24.14
Midtown	1,227,605	55,698	0	-	5.2%	2.5%	55,698	0	23,476	\$21.75
North Interstate-17	183,463	36,070	0	-	19.7%	-	36,070	0	0	\$22.96
North Phoenix	61,149	2,400	0	-	3.9%	-	2,400	0	1,626	\$18.64
North Scottsdale	371,005	52,961	0	-	13.9%	16.6%	51,538	0	-5,025	\$21.02
NW Phoenix	1,631,075	370,273	16,695	-	31.0%	12.0%	368,510	19,695	43,715	\$17.71
Paradise Valley	1,254,637	180,246	2,172	22.6%	14.4%	6.6%	179,629	2,172	14,098	\$23.79
Piestewa Peak Corridor	300,558	82,462	6,813	30.9%	35.8%	17.2%	82,462	6,813	-7,753	\$23.46
Pinal County	680,348	73,620	0	-	12.8%	1.9%	73,620	0	9,420	\$20.31
Scottsdale Airport	727,072	39,423	2,435	8.8%	5.2%	-	37,405	0	10,320	\$28.91
South Scottsdale	853,464	94,410	0	-	15.3%	6.5%	94,410	0	13,919	\$22.37
South Tempe	515,896	80,402	5,060	-	17.3%	3.4%	80,202	5,060	-2,865	\$22.94
Southwest Phoenix	184,577	20,186	0	-	11.2%	10.7%	20,186	0	-9,605	\$25.95
Superstition Corridor	1,820,489	182,367	9,361	0.0%	10.5%	15.5%	178,219	6,550	2,729	\$21.35
Tempe	985,455	191,945	0	-	22.7%	13.2%	191,945	0	15,248	\$21.98
West I-10	1,175,155	38,528	1,657	-	3.2%	39.4%	38,528	1,657	18,892	\$27.70
Total	26,498,039	3,071,518	77,146	12.0%	12.4%	9.7%	2,879,784	208,806	196,551	\$23.50

The data contained in this market report is obtained from The CoStar Group, Inc., and is used under licensed permission. The report is based on all Metro-Phoenix markets for healthcare buildings, regardless of size. It includes sublease space only upon the date of availability, and includes any owner and renter occupied space.


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