

Absorption Slows, but Investment Activity Surges

Key Takeaways

- Following a strong first three months of 2017, the momentum in the Greater Phoenix retail market cooled in the second quarter, with vacancy flat and net absorption cooling.
- Net absorption was more than 175,000 square feet in the second quarter, the lowest quarterly total in more than two years. Net absorption for the first half of this year was approximately 858,000 square feet, down 7 percent from the first half of 2016.
- Asking rents in Greater Phoenix are on the rise, increasing 4.3 percent in the past year to \$14.56 per square foot. This marks the strongest annual rent growth in nearly a decade, even as current rents are still down approximately 25 percent from the pre-recession peak.
- The investment market strengthened in the second quarter, with sales of shopping centers accelerating, prices rising and cap rates compressing. Year to date, the median price is \$118 per square foot, and cap rates have averaged approximately 7.5 percent.

Greater Phoenix Retail Market

After a period of strong tenant move-ins to start the year, the pace of improvement in the Greater Phoenix retail market stalled in the second quarter. Net absorption totaled nearly 700,000 square feet in the first quarter, but dropped off to less than 180,000 square feet in the second quarter. Net absorption has averaged approximately 2 million square feet per year since 2012, and a similar figure is forecast for 2017. The East Valley submarket has the largest concentration of retail space in Greater Phoenix, accounting for more than 30 percent of the total inventory. Conditions have been improving in the East Valley for the past several quarters, and the vacancy rate in the submarket dipped into the single digits during the second quarter.

Market Indicators Relative to prior period	Market Q2 2017	Market Q2 2016
Vacancy	↔	↔
Net Absorption	↓	↓
Construction	↓	↑
Rental Rate	↑	↑

Second Quarter Employment Trends*

Total Nonfarm Phoenix Metro	↑	↓
Retail Phoenix Metro	↑	↑
Total Nonfarm United States	↓	↓
Retail United States	↑	↓

*Source: Bureau of Labor Statistics

Summary Statistics	Phoenix Market
Vacancy Rate	9.3%
Change from Q2 2016 (bps)	-10
Net Absorption (thousands SF)	177
New Construction (thousands SF)	246
Under Construction (thousands SF)	669
Asking Rents Per Square Foot Per Year	\$14.56
Change from Q2 2016	4.3%

Greater Phoenix Retail Market (continued)

While absorption slowed, investment activity accelerated in the second quarter, reversing the trend from the first few months of the year. Sales picked up across the Valley, with significant transactions taking place in Scottsdale, Goodyear, Peoria and Glendale. Prices

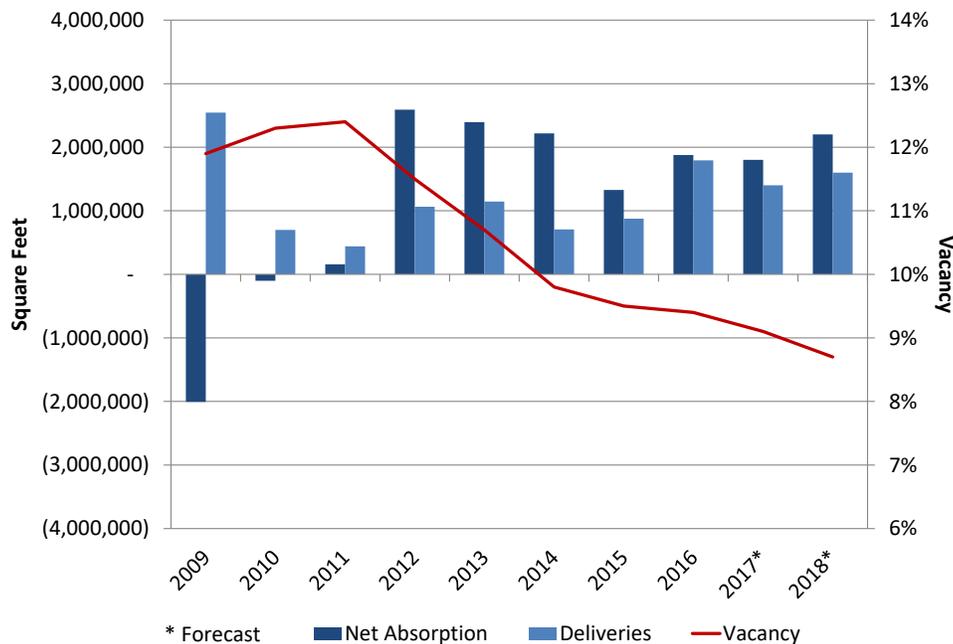
rose and cap rates compressed, signaling the overall strengthening of investor sentiment. With operating fundamentals forecast to improve in the second half of this year, the local investment market is likely to remain healthy.

Recent Transactions in the Market

RETAIL SALE ACTIVITY					
Property Address/Intersection	Submarket	Sale Date	Sale Price	Size SF	Sale Price SF
13802-14046 N Scottsdale Rd., Scottsdale	North Scottsdale	4/27	\$31,000,000	162,259	\$191
14175 W Indian School Rd., Goodyear	West Valley	5/31	\$22,450,000	107,633	\$209

RETAIL LEASE ACTIVITY			
Property Address/Intersection	Submarket	Tenant	Size SF
4609-4735 E Ray Rd., Phoenix	South Mountain	Burlington	41,752
NWC Recker Rd. & Longbow Pky., Mesa	East Valley	Sprouts	29,972

Historical Absorption, Deliveries and Vacancy Rates



Vacancy:

- › Retail vacancy in Greater Phoenix held steady in the second quarter, remaining at 9.3 percent. The rate is 10 basis points lower than one year ago and vacancy has remained below 10 percent since the end of 2014.
- › Following a strong start to the year, the pace of net absorption cooled in the second quarter. Net absorption was approximately 177,000 square feet in the second quarter, bringing the total for the first half of the year to 858,000 square feet. During the past 12 months, net absorption has totaled more than 1.8 million square feet.
- › Vacancy in the East Valley dipped below 10 percent for the first time in nearly a decade during the second quarter. The rate is now down to 9.8 percent, 60 basis points lower than one year ago. Year to date, net absorption in the East Valley has totaled more than 470,000 square feet, compared to only 171,000 square feet of new construction.

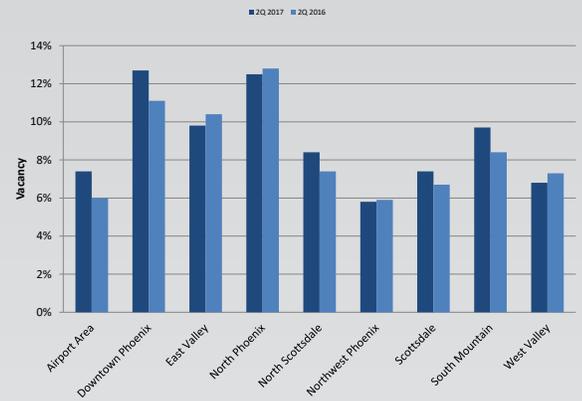
Rents:

- › Rent growth accelerated in the second quarter, with asking rents reaching \$14.56 per square foot. Asking rents are now up 4.3 percent from one year ago.
- › Rents in North Scottsdale are on the rise, increasing by 6.6 percent year over year to \$19.42 per square foot. Asking rents in North Scottsdale inched lower in both 2015 and 2016, but changed course in the first half of this year.
- › In the East Valley, rents have increased in four of the past five quarters. In the second quarter, asking rents in the East Valley reached \$13.95 per square foot, 3.4 percent higher than one year ago. With vacancy now below 10 percent, further rent increases are likely.

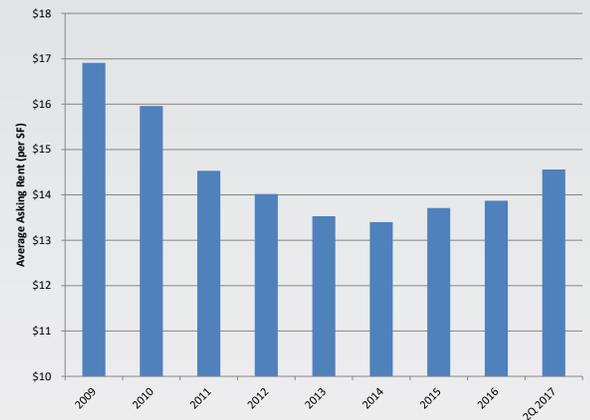
Investment Trends:

- › Sales of shopping centers accelerated in the second quarter, spiking by more than 50 percent from the first quarter. Sales velocity in the first half of 2017 is down 11 percent from the first half of last year. After minimal activity in the first quarter, transaction activity in properties selling for \$10 million and higher returned to normal levels during the second quarter.
- › The median price rose 20 percent from the first quarter to the second quarter. The median price reached \$122 per square foot in the second quarter, bringing the median price to \$118 per square foot for year-to-date transactions.
- › After ticking higher to start 2017, cap rates compressed in the second quarter. The average cap rate in properties sold during the second quarter dipped below 7 percent. Year to date, the average cap rate in all shopping center transactions is approximately 7.5 percent.

Vacancy by Submarket Cluster



Asking Rents Trends



Investment Trends



Outlook:

The Greater Phoenix retail market is off to a healthy start to 2017, setting the stage for a second half that should bring additional improvement. While the market should continue to strengthen between now and the end of the year, the robust absorption activity recorded in the first few months of the year was not sustained in the second quarter, highlighting the uneven nature of the recovery in retail real estate. The current Greater Phoenix retail forecast calls for net absorption of approximately 1.8 million square feet in 2017, similar to levels recorded during the past three years. Employment growth has been steady in recent years, but significant gains are being posted in the leisure and hospitality and construction sectors, which are historical indicators of the overall health of the local economy.

Total leasing volume has been fairly consistent in recent years, but there are some signs of larger spaces being leased after several high-profile big-box closures. Some of these spaces are being backfilled, including Target opening a new 50,000-square foot concept in a former Sports Authority at 16th Street and Camelback Road. Additional re-tenanting of larger spaces will likely continue in the years ahead, although some blocks may need to be reconfigured into smaller spaces to keep pace with the evolving retail real estate trends. The strongest source of optimism in the market is the ongoing strengthening in the local economy. Employers are on pace to add about 50,000 new jobs in 2017, while homebuilders are forecast to pull more than 20,000 single-family housing permits.

Submarket Statistics

		TOTAL VACANCY			NET ABSORPTION-SF		NEW SUPPLY			ASKING RENTS
Submarket	Inventory	Vacant SF	Q2-17	Q2-16	Q2-17	YTD	Q2-17	YTD	Under Construction	Rate
Airport Area	3,280,648	242,614	7.4%	6.0%	(10,924)	(64,839)	-	-	-	\$14.44
Downtown Phoenix	4,499,102	570,212	12.7%	11.1%	(11,482)	(19,119)	11,372	11,372	73,294	\$14.00
East Valley	61,625,102	6,042,746	9.8%	10.4%	73,797	470,413	74,105	171,035	168,132	\$13.95
North Phoenix	32,121,009	4,014,160	12.5%	12.8%	78,263	62,894	-	-	148,000	\$12.93
North Scottsdale	14,813,276	1,251,238	8.4%	7.4%	(29,428)	89,602	87,969	99,630	44,124	\$19.42
Northwest Phoenix	16,906,004	988,239	5.8%	5.9%	107,617	327,088	12,000	263,056	10,000	\$14.52
Scottsdale	15,800,004	1,175,006	7.4%	6.7%	45,892	20,608	13,855	25,855	116,974	\$23.79
South Mountain	5,704,394	555,683	9.7%	8.4%	(62,655)	(49,740)	-	-	10,000	\$14.46
West Valley	19,200,225	1,311,930	6.8%	7.3%	(14,382)	20,979	46,940	98,195	79,620	\$13.99
Metro Phoenix	173,949,764	16,151,828	9.3%	9.4%	176,698	857,886	246,241	669,143	650,144	\$14.56

FOR MORE INFORMATION

Bob Mulhern

Senior Managing Director | Greater Phoenix
+1 602 222 5038
Bob.Mulhern@colliers.com

Jim Keeley SIOR

Founding Partner | Scottsdale Office
+1 480 655 3300
Jim.Keeley@colliers.com

Pete O'Neil

Research Director | Greater Phoenix
+1 602 222 5029
Pete.ONeil@colliers.com