

Absorption Spikes to Close 2017

Key Takeaways

- > The Greater Phoenix retail market ended 2017 on an upswing, with strong net absorption driving the local vacancy rate lower. With more space leasing up and vacancies tightening, landlords have begun to accelerate the pace of rent increases.
- > Net absorption exceeded 1 million square feet during the fourth quarter, and for the year more than 2.8 million square feet was absorbed. This was the strongest year of retail net absorption in Greater Phoenix since 2007.
- > A rise in demand fueled an increase in rents. Asking rents advanced 4.6 percent in 2017, ending the year at \$14.64 per square foot. Rent gains in 2017 were far steeper than increases recorded in the previous two years.
- > More shopping centers sold during the fourth quarter than in the third quarter, but transaction activity for 2017 still slightly lagged 2016 levels. The median price was also a bit lower in 2017, in part because more high-vacancy properties are selling as lease-up opportunities.

Greater Phoenix Retail Market

The Greater Phoenix retail market closed 2017 with its strongest quarter of net absorption in five years. Tenants moved into a net of more than 1 million square feet of retail space during the fourth quarter, bringing the total for 2017 to more than 2.8 million square feet. Much of this tenant demand is being concentrated in high-income, fast-growing areas of the Southeast Valley. Net absorption in Gilbert reached nearly 290,000 square feet in 2017, while retailers moved into a net of more than 265,000 square feet of space in neighboring Chandler. Combined, these two cities accounted for approximately 20 percent of the total net absorption in Greater Phoenix in 2017, a continuation of a trend that firmly took hold in 2016, when combined net absorption in Chandler and Gilbert represented more than 40 percent of the Greater Phoenix total.

Market Indicators Relative to prior period	Market Q4 2017	Market Q4 2016
Vacancy	↓	↓
Net Absorption	↑	↑
Construction	↓	↓
Rental Rate	↑	↓
Fourth 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	8.4%
Change from Q4 2016 (bps)	-90
Net Absorption (thousands SF)	1,067
New Construction (thousands SF)	213
Under Construction (thousands SF)	715
Asking Rents Per Square Foot Per Year	\$14.64
Change from Q4 2016	4.6%

Greater Phoenix Retail Market (continued)

The local investment market gained momentum during the fourth quarter, although transaction activity in 2017 somewhat lagged totals from the previous year. Prices also retreated a bit in 2017, although there was a wide range in pricing based on occupancy levels and tenant quality. With retail tenants in expansion mode, there could be a rise in the sale of centers with elevated vacancies, as investors

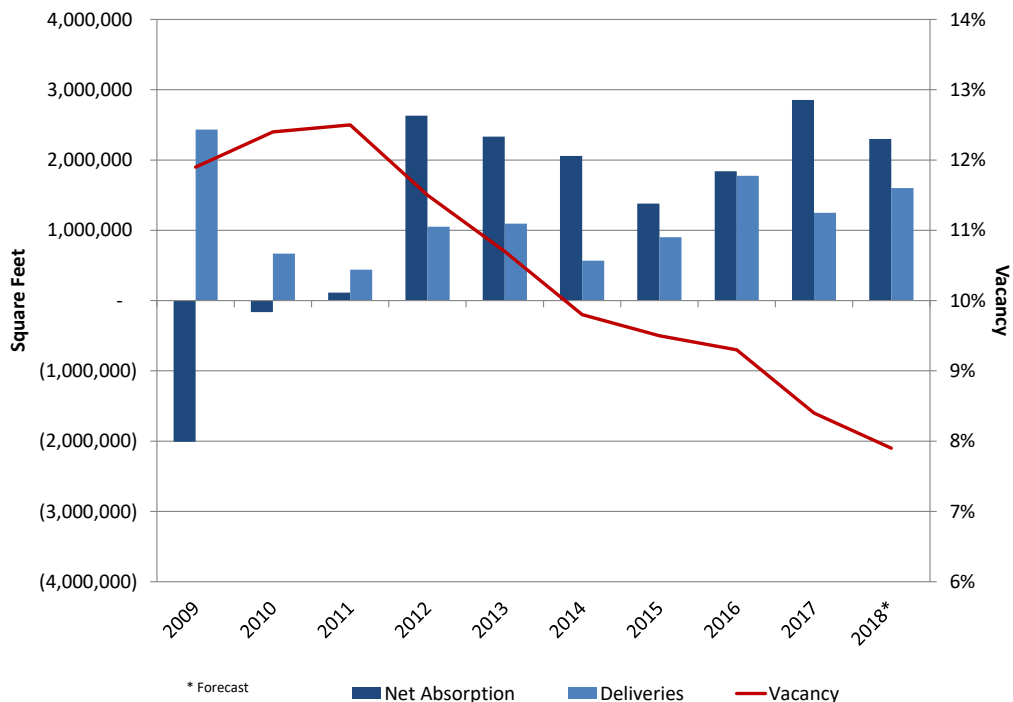
implement lease-up strategies. There was an increase in the number of these high-vacancy properties changing hands during the fourth quarter, which was one factor in the decline of the median sales price. Cap rates are generally averaging in the low- to mid-7 percent range, which seems sustainable in the coming months.

Recent Transactions in the Market

RETAIL SALE ACTIVITY					
Property Address/Intersection	Submarket	Sale Date	Sale Price	Size SF	Sale Price SF
13811-13843 N Tatum Blvd., Phoenix	North Scottsdale	11/29	\$11,000,000	55,738	\$197
2235 S Power Rd., Mesa	East Valley	11/2	\$7,850,000	46,035	\$171

RETAIL LEASE ACTIVITY			
Property Address/Intersection	Submarket	Tenant	Size SF
1126 S Gilbert Rd., Mesa	East Valley	Aspire Fitness	36,241
3807 S Gilbert Rd., Gilbert	East Valley	Mor Furniture	25,495

Historical Absorption, Deliveries and Vacancy Rates



Vacancy:

- › Retail vacancy in Greater Phoenix fell 50 basis points during the fourth quarter, ending the year at 8.4 percent. The rate declined by 90 basis points in 2017, following modest dips in both 2015 and 2016.
- › Vacancy was driven lower by strong levels of net absorption, particularly late in the year. Net absorption topped 1 million square feet in the fourth quarter, bringing the total for the full year to more than 2.8 million square feet. Net absorption had averaged approximately 2 million square feet per year from 2012-2016, before spiking during the past 12 months.
- › The economy in the West Valley is gaining traction, supported in part by the extension of the Loop 303 freeway. Retail vacancy in the West Valley dipped 40 basis points in 2017, ending the year at just 6 percent.

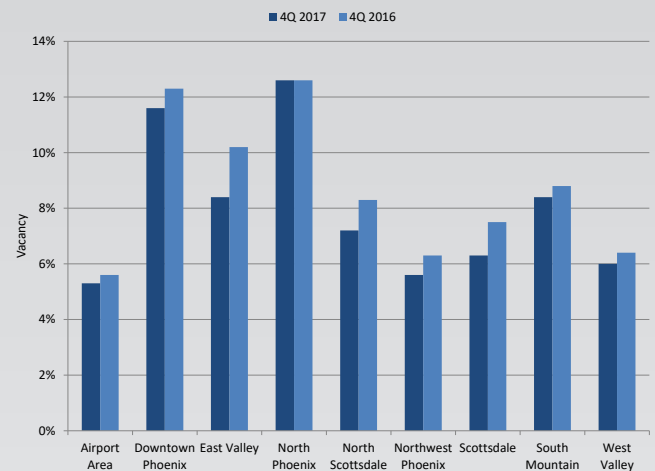
Rents:

- › Rents rose in the fourth quarter, reaching \$14.64 per square foot. Asking rents gained 4.6 percent in 2017, following average gains of just 1.5 percent per year in 2015 and 2016.
- › Rents in the East Valley region gained momentum in the fourth quarter, ticking up to \$14.35 per square foot. Asking rents in the East Valley rose 5.8 percent in 2017, building on a 4.1 percent increase in the preceding year.
- › Elevated vacancy in the North Phoenix region is dragging on rents. Asking rents in North Phoenix dipped 2.2 percent in 2017, ending the year at \$11.94 per square foot. With vacancy in the submarket likely to remain in the double digits in the years ahead, there could be some additional downward pressure on rents.

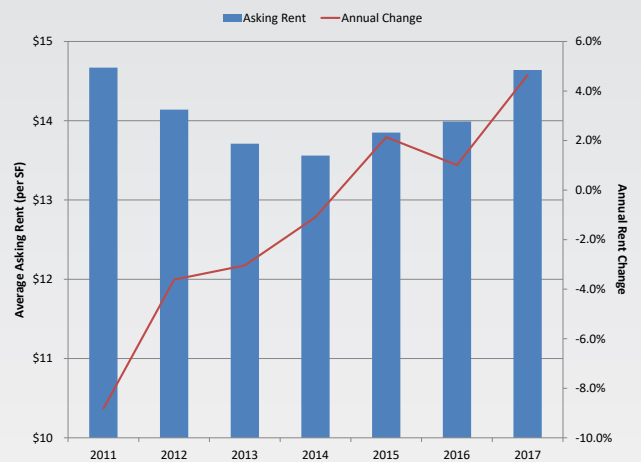
Investment Trends:

- › Sales activity of shopping centers gained momentum in the fourth quarter, spiking by approximately 35 percent from the transaction activity in the third quarter. Despite the late-year surge in activity, sales velocity in 2017 was down 4 percent from the preceding year.
- › After a steep rise in the third quarter, the median price dipped in the last three months of the year. The median price in the fourth quarter was \$109 per square foot, and the median price for all of 2017 was \$114 per square foot. This represents a 6 percent decline in the median price from the 2016 figure.
- › Cap rates inched lower in the fourth quarter, averaging approximately 7 percent. The average cap rate in shopping center transactions in 2017 was approximately 7.4 percent, about 40 basis points higher than the 2016 average.

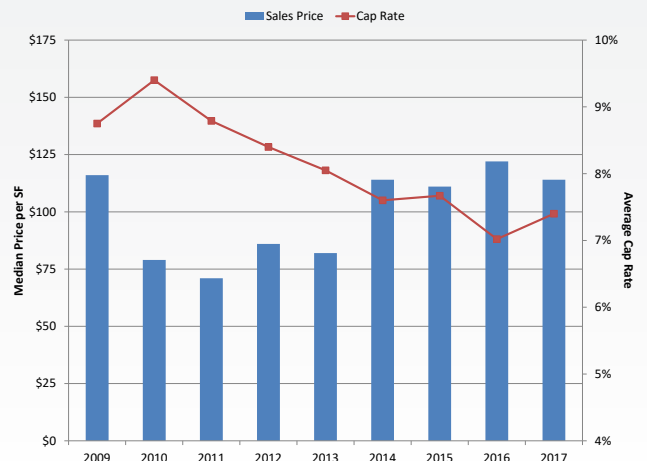
Vacancy by Submarket Cluster



Asking Rents Trends



Investment Trends



Outlook:

The Greater Phoenix retail market will likely have a strong 2018, as tenant demand remains healthy and the economic outlook calls for continued expansion. The local economy has been on an upswing for the past several years, adding more than 300,000 jobs since 2012, including 30,000 positions within the retail sector. Further expansion is likely in the year to come. In addition, the local housing market is bouncing back, with prices pushing higher and housing starts slowly gaining momentum, trends that should continue in 2018 and should support the local retail climate.

Growth in the local retail market is coming from a number of sources. Restaurants have been leading the way, fueled by population expansion, job gains and some recent wage growth that is resulting in more disposable income for consumers. While the outlook for 2018 calls for another wave of restaurant openings, grocery stores could be another source of demand in Greater Phoenix. German grocer Aldi is a potential new entrant into the local grocery market, after the company announced plans to open a regional distribution center in Goodyear.

Submarket Statistics

		TOTAL VACANCY			NET ABSORPTION-SF		NEW SUPPLY			ASKING RENTS
Submarket	Inventory	Vacant SF	Q4-17	Q4-16	Q4-17	YTD	Q4-17	YTD	Under Construction	Rate
Airport Area	3,346,875	177,014	5.3%	5.6%	4,943	11,480	-	-	-	\$15.78
Downtown Phoenix	4,769,898	554,525	11.6%	12.3%	(5,712)	93,740	-	70,772	13,894	\$16.64
East Valley	61,651,736	5,164,105	8.4%	10.2%	498,220	1,426,725	11,590	365,825	398,514	\$14.35
North Phoenix	32,431,857	4,075,736	12.6%	12.6%	168,296	132,610	148,000	148,000	-	\$11.94
North Scottsdale	15,182,006	1,093,363	7.2%	8.3%	172,857	288,878	19,931	129,596	59,728	\$19.74
Northwest Phoenix	17,108,086	960,888	5.6%	6.3%	98,147	377,429	10,000	273,056	-	\$14.56
Scottsdale	15,933,217	1,009,471	6.3%	7.5%	125,552	288,825	-	105,855	99,959	\$22.09
South Mountain	5,763,759	486,115	8.4%	8.8%	(27,201)	29,828	-	10,000	-	\$16.65
West Valley	19,339,574	1,167,003	6.0%	6.4%	31,491	205,266	23,363	146,558	142,570	\$14.12
Metro Phoenix	175,527,008	14,688,220	8.4%	9.3%	1,066,593	2,854,781	212,884	1,249,662	714,665	\$14.64

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

Copyright © 2018 Colliers International.

The information contained herein has been obtained from sources deemed reliable. While every reasonable effort has been made to ensure its accuracy, we cannot guarantee it. No responsibility is assumed for any inaccuracies. Readers are encouraged to consult their professional advisors prior to acting on any of the material contained in this report.

Colliers International | Greater Phoenix
2390 E. Camelback Road, Suite 100
Phoenix, AZ 85016
+1 602 222 5000
colliers.com/greaterphoenix



Accelerating success.