ALEXANDRIA
STATE OF
THE MARKET

2024
Mid-Year
Report

Development Trends

An aerial view of the forthcoming WestEnd Alexandria at the former Landmark Mall site.

PROJECTS UNDER CONSTRUCTION

NAME	CATEGORY	NEIGHBORHOOD
Virginia Tech Innovation Campus	Education	Potomac Yard
Silverstone Phase II	Residential, Senior Living	Potomac Yard
Inova Oakville Healthplex	Health Care and Residential	Potomac Yard
Avanti 550	Residential	Braddock
Aspire Alexandria	Residential, Senior Living	Braddock
Sansé and Naja	Residential, Affordable Housing	Arlandria
901 N. Pitt Street	Residential, Converted from Office	Old Town
TideLock	Residential, Converted from Office	Old Town
802-808 N. Washington Street	Residential	Old Town
1101 King Street	Residential, Converted from Office	Old Town
The Heritage at Old Town	Residential, Affordable Housing	Old Town
Inova Alexandria Hospital	Hospital, Convert-ed from Shopping Mall	West End

Northern Virginia's office development pipeline remains historically low, with no deliveries and no new office projects breaking ground in all of 2023. In fact, the office pipeline for new development in the Greater Washington area is at its lowest level in 30 years, according to CoStar, with only 0.5% of existing inventory under construction.

In Alexandria, previously approved development plans for offices are being revisited, with the City encouraging alternative commercial uses or a mix of uses that would also be valuable to the City's tax base.

The rising cost of construction, combined with a shift to hybrid work, has affected numerous projects. Construction spending has been affected by inflation and increased labor costs, materials costs, and insurance rates. In addition, interest rate increases over the past two years significantly raised the cost of borrowing money.

These challenges—along with pipeline delays of construction materials—have forced developers to look for creative financing solutions. Developers are brainstorming how to assemble the right model to leverage lower financing and more-flexible capital.

1940 Duke Street

OFFICE UPDATE

Office Trends

Office leasing growth continues to decline post-pandemic as employees demand remote or hybrid work. Some companies are fully committed to this new workplace shift, while others are still testing options. Nevertheless, many companies are placing some or all of their office suites on the sublease market as an option to removing an office lease obligation from its bottom line.

To entice tenants to lease space, landlords are renovating lobbies to become hospitality/community spaces and adding meeting and large-format conference spaces that are free to tenants. They are also rolling the dice with construction of multiple speculative suites—to capture users who require quick occupancy—and flexible floorplans to accommodate expansion, as well as the option to downsize the lease mid-term.

Vacancy Rate: 15.5%
Net absorption: -294,700 SF
Inventory: 20.8 Million SF

Alexandria's office vacancy continues to trend upward to 15.5% from 14.6% last year, with Class A vacancy at 18.5%. This overall vacancy is still far below the Northern Virginia rate of 20.2%, but the higher Class A vacancy rates point to continued market compression and challenges to come.

The significant negative absorption was foreshadowed earlier this year after the U.S. Patent and Trademark Office (USPTO) reduced its office footprint by one-third—an 800,000 SF reduction of its 2.5 million SF campus in the Carlyle neighborhood. The USPTO now occupies only three of the five buildings built for them in 2001.

Other notable tenants are also shrinking their footprint. Oblon, patent attorneys at 1940 Duke Street, continue to give back space in a building that was originally built for them. Oblon now only leases a fraction of its original 200,000 SF lease from 2003.

Overall, office leasing activity remains slower than historic norms and Alexandria businesses are right-sizing in place and/or trading up in quality. Some are moving to newer buildings—but leasing a smaller footprint—with modern hospitality-like amenities and in desirable locations that they hope help draw workers back to the office.

Deal transactions continue to be highly incentivized for larger deals, with improvement packages in the triple digits per square foot and rent concessions close to an average of one to two months free per the lease term.

However, very few deals in the Alexandria market are greater than 10,000 SF. This is discouraging for some of the larger more significant blocks of office building vacancies, but the size bodes well for smaller office buildings.

Despite negative absorption, leasing activity continues, albeit at a slower pace. As net new leasing absorption remains stalled, brokers are bringing tenants out earlier than usual to capture concessions from existing and new landlords. And landlords are actively buying deals by paying lease termination penalties to entice tenants to their buildings.

A view of the Carlyle neighborhood

OFFICE UPDATE

Future Trends

The outlook for the market seems uncertain as businesses and investors will approach deals with greater scrutiny and consider more variables. This closer analysis will affect leasing and investment activity.

Office vacancy should eventually stabilize in the Alexandria area over the coming year with the continual removal of obsolete offices, especially if 5001 Eisenhower Avenue, formerly known as the Victory Center, redevelops into residential. This 600,000 SF building—which had long been earmarked for future federal office space—stands empty, accounting for almost 2.5% of the City's office vacancy.

Owners of other empty or near-empty buildings are keeping their options open. They have received approvals to convert to residential but haven't yet started construction and continue to advertise available office space. This includes the 95,000 SF office building at 1201 E. Abingdon Drive—the former home of Harris Corporation and Housing Alexandria—and the 301 N. Fairfax Street office building, whose owners plan to replace the 1970s building with a four-story multifamily apartment building.

However, these conversions give a false sense of an improving market. Not all buildings will be saved from foreclosure. In fact, the volatility in the office market will soon bear witness as loan maturities come due over the next year, forcing many notable Class A buildings to go back to banks and/or to auction.

More buildings are expected to face financial trouble and owners will not wait for foreclosure—they will voluntarily give back buildings to banks for auction. This happened with the approximately 165,000 SF office building at 2000 Duke Street. The Motley Fool previously occupied the majority of the building, which was handed back to the bank. At auction this past summer, the building sold for $3.5 million, a fraction of the $75 million it traded for in 2019.

This trend of banks recapturing and offloading office inventory at values far below market will continue. This could be viewed as an opportunity for Alexandria to capitalize on a changing landscape to meet the community's needs through conversion to other uses such as schools, medical offices, hotels, and affordable housing.

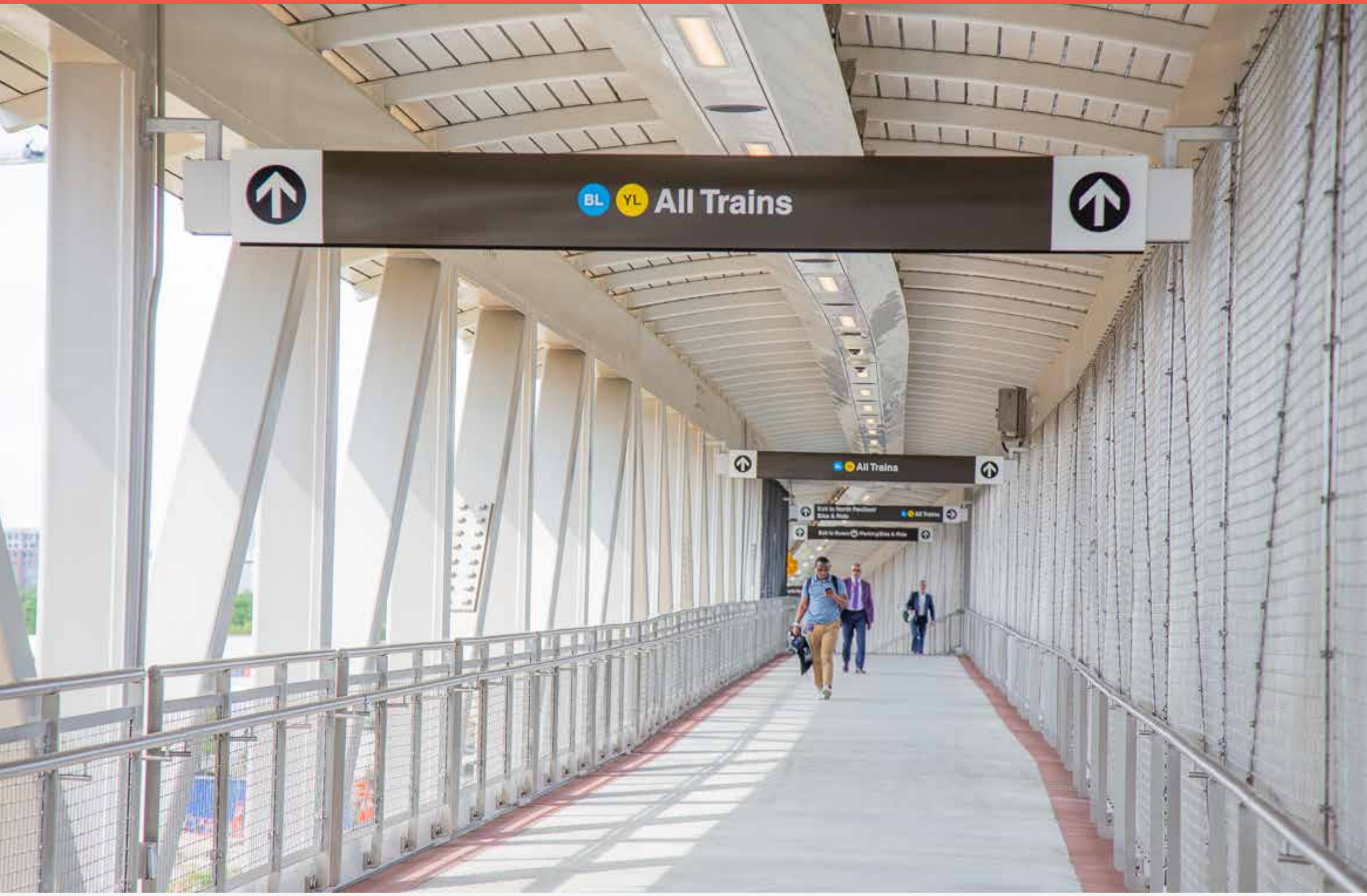
Without further interest rate reductions though, the market will remain stagnant. The pace of rent growth in Northern Virginia will plateau over the next three years until supply depletes and/or is converted to other uses.

Fewer landlords will have the capital to build enticing amenities and to offer concessions.

Growing vacancy shows a market continuing to readjust to new office hybrid work environments. However, unlike neighboring jurisdictions, Alexandria remains ahead of the market as the City continues to approve conversions of obsolete office buildings into schools, hotels, senior living, and, of course, residential. This limits office space options for lease to the remaining higher quality, well-positioned buildings and locations.

NOTABLE LEASE TRANSACTIONS

Washington University of Science and Technology	2900 Eisenhower Avenue	59,600 SF
GSA/Department of Defense	4825 Mark Center Drive	45,843 SF
Baker International	1925 Ballenger Avenue	23,600 SF
McEnearney Commercial	510–526 King Street	22,545 SF
Inova Health Care Services	4700 King Street	14,666 SF
Applied Research Services	2760 Eisenhower Avenue	14,548 SF
Amentum	2800 Eisenhower Avenue	12,839 SF
Cowo & Creche	330 John Carlyle Street	12,312 SF
Virginia Passenger Railway Authority	1800 Diagonal Road	11,699 SF



The Potomac Yard Metro Station

NOTABLE OFFICE SALES

2000 Duke Street	$3.5 million ($21.29/SF)	The Shidler Group to OSOOL Holdings Inc.
3601 Eisenhower Avenue	$21.5 million ($148/SF)	Monday Properties to Virginia Hospital Center (for outpatient surgery center)
510–526 King Street at Courthouse Square	$29.5 million ($245/SF)	Brookfield to Melrose Alexandria Holdings
4850 Mark Center Drive	$58.7 million ($225/SF)	Institute for Defense Analysis (IDA) to City of Alexandria (part of the City's lease with IDA was this option to purchase the building)

The Evening Star on Del Ray's Mount Vernon Avenue

RETAIL UPDATE

Regional Retail Trends

Retail real estate is faring better than the commercial market. While office buildings struggle after the shift to a remote and hybrid work environment, the job market and tourism industry continue to do well.

One of the biggest national trends can be seen in the Greater Washington area as well: the rise of the food hall, which benefits both consumers and operators. In 2023, the U.S. had 360 food halls, an increase from 220 in 2019, according to Cushman & Wakefield. Another 127 food halls were expected to open across the country in 2024.

The food hall concept provides smaller and first-time restaurant entrepreneurs opportunities at lower startup and ongoing costs. Food halls previously catered to commuters but are now adapting to provide a more communal experience for locals and tourists. According to Cushman & Wakefield, millennials and Gen Zers prioritize experience over goods and will return again and again to food and beverage destinations they deem to have preferable experiences, such as social interaction, authenticity, and elevated concepts.

The DC area saw three new food halls in 2023: the Michelin award-winning Love Makoto in the East End, The Square in Golden Triangle, and The Heights in Chevy Chase. While this largely benefits retail developers, it also means vacancies in more traditional brick-and-mortar restaurant sites as restauranteurs move into food halls.

FY 2024 RETAIL OPENINGS AND LEASES

Alloy Personal Training	1070 N. Fayette Street
Amazon Fresh	3801 Richmond Highway
Atlas Muay Thai Gym	215 N. Payne Street
Chase Bank	628 King Street
Chase Bank	3625 Richmond Highway
Como en Casa	4112 Mount Vernon Avenue
Continues Arcade	1050 N. Fayette Street
Crème de la Crème	907 King Street
DistrictCryo	113 S. Columbus Street
Enchant Hair Co.	2202 Mount Vernon Avenue
Era Edit Clothing and Accessories	109 N. Fairfax Street
First National Bank	704 King Street
Framebridge	1308 King Street
Happy Place	107 S. Union Street
Lil' Creamery	1014 Madison Street
Little Birdies	103 S. St. Asaph Street
Madame Coco's: The Enchanted Emporium	103 S. St. Asaph Street
Monday's Child	127 S. Fairfax Street
Nothing in Between Studio	1306 King Street
PetMedic Urgent Care	515 King Street
Pippin Toy Company	1310 King Street
Small Door Veterinary	277 S. Washington Street
Spa180 Prestige	2813 Duke Street
VABC	825 S. Washington Street
Veterinary Emergency Group	4525 Duke Street
Yoga Six	2465 Mandeville Lane

FY 2024 RESTAURANT OPENINGS AND LEASES

Atlas Brew Works and Andy's Pizza	2429 Mandeville Lane
Bad Axe Throwing	617 S. Pickett Street
Benny Diforza's Pizza	1504B Mount Vernon Avenue
Ben'Yays	1028 King Street
Bloom Tea	425 S. Washington Street
Call Your Mother Deli	1300 King Street
Capo Italian Deli	109 N. Washington Street
Crazy Mason	716 King Street
Dreampt	2216 Mount Vernon Avenue
Frankies	823 S. Washington Street
Gin Ramen & Asian Tapas	500 John Carlyle Street
Gustave Boulangerie & Brasserie	2213 Mount Vernon Avenue
Josephine	109 S. St. Asaph Street
Kiln	699 Prince Street
La'Baik Del Ray	2309 Mount Vernon Avenue
La Pupusa Loca	4231 Duke Street
Le Petit Ananas Shaved Ice	2307 Mount Vernon Avenue
Lily's Chocolate & Coffee	631 King Street
MacMillan Spirit House	500 Montgomery Street
Midnight Treats	110 S. Payne Street
Mint Condition	122A S. Royal Street
Mystic BBQ & Grill	218 N. Lee Street
Omar's Pitas & Platters	3100 Richmond Highway
Orkney Springs Distillery	3125 Mount Vernon Avenue
Piece Out Del Ray	2419 Mount Vernon Avenue
Pitango Gelato	115 S. Union Street
Pupatella Neapolitan Pizza	700 Slaters Lane
Rosemarino D'Italia	1905 Mount Vernon Avenue
Royal Restaurant	730 N. St. Asaph Street
Tatte	515 King Street
The Greenery	1023 Queen Street

ECONOMIC UPDATE

Trends and a Look to the Future

Looking toward 2025, the economic outlook for the Greater Washington area has shifted from stable to uncertain. While our region is traditionally protected from macroeconomic instability because of the federal government's employment presence, the area's economy underperformed the rest of the country in a few key metrics, particularly employment growth.

A thin labor pool and high demand for skilled workers has limited growth across all sectors. However, Northern Virginia's tech sector (and Maryland's life science sector) position the region well for further economic diversification over the long term. *The Washington Business Journal* and CBRE estimate a total Washington-area net job growth of 21,500 in 2024.

Nevertheless, presidential elections bring uncertainty, and the next 18 months will be telling.

In addition, it remains to be seen whether the Federal Reserve will again lower interest rates. The Fed lowered interest rates by half a point in September and a quarter point in November for the first time in four years, pointing to a low but slight increase in the unemployment rate and a lower, but still elevated, inflation rate. These cuts could boost the real estate transaction market, but it's too early to see if this bears out.

As our report shows, the pandemic will have a long-term effect on the DC Metro area's retail and commercial market. It remains to be seen how all this shakes out, even after four and a half years since lockdown. Consumer behavior may be changed forever, as we shop, eat, and work more from home. What that means for any jurisdictions that have historically collected tax revenues based on physical locations remains to be seen.

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