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Office rents in parts of Phoenix top \$40/sq. foot

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Some office buildings at the corner of Camelback and 24th Street are commanding rents of more than \$40 per square foot, rivaling the going rates of better-known office addresses in Chicago and Newport Beach, Calif.

New tenants are finding those top-tier rents at the Camelback Esplanade, at 2425 and 2525 E. Camelback Road, and the 11-story Hines office project under development just west of the upscale corner.

Meanwhile, the Phoenix market average for Class A space, which is in buildings with the most up-to-date amenities, was \$26.75 per square foot during the fourth quarter of 2006, according to Cushman & Wakefield of Arizona. Competitor CB Richard Ellis listed the Valley's Class A space at \$29.21.

Across the metropolitan area, the average asking rates for leases climbed between 15 percent and 20 percent in the past year, according to broker reports.

"The tenants have not resisted these increased prices," said Larry Downey, Cushman's executive director of office properties. "They understand the market is tightening . . . and that the Esplanade is the place to be."

Mike Coover of Grubb & Ellis/BRE Commercial LLC said, "Camelback Corridor currently has the highest rates. We are not seeing the threshold of \$40 for traditional space being broken for other submarkets yet."

Pat Devine of CB Richard Ellis said part of the price pressure in the Camelback Corridor stems from record prices paid for the Esplanade buildings in 2005.

"You saw huge rent pressure from investors needing to achieve certain returns," he said. So rents climbed from the high \$20s to low \$30s, to the high \$30 to low \$40s in just over a year. The climb is more dramatic when compared with two years ago when rents per square foot generally were in the mid-\$20s.

No reining in rates

Even the construction of 24th at Camelback II, west of the original Hines building on that intersection's southwest corner, isn't expected to rein in rents, brokers said.

Grubb & Ellis is already preleasing the 300,000-square-foot building. Construction is expected to start in the second quarter of this year.

Construction will take at least 18 months, Downey said. He added, "I think they are building that building on rates they can achieve, knowing that the rates will be north of \$40."

The project's Web site lists rents of \$40 to \$44 a square foot, based on size and location.

Those Esplanade rents are also pushing up rent nearby along Camelback and south along Central Avenue.

Overall rents climbed 15.2 percent last year, according to Cushman's estimates. In some parts, rates climbed 20 to 30 percent, Coover of Grubb & Ellis said. And rents are expected to keep growing this year.

Coover, who wrote the 2007 Real Estate Forecast released by Grubb & Ellis, expects this to be a catch-up year for landlords unaware of rental growth.

Absorption of office space hit a new record, as nearly 3.5 million square feet were snapped up by new and growing companies. The previous high was 3.3 million square feet, according to Cushman.

"Every submarket got a healthy shot in the arm" from strong job creation in 2006, Downey said.

That job creation has many commercial real estate experts predicting another good year for landlords in 2007.

Scottsdale Airpark showed the most job creation, followed by midtown Phoenix, according to the Cushman report.

Office vacancies across the metropolitan area also dropped to 11.1 percent during the fourth quarter, from 13.5 percent at the end of 2005, according to Cushman. CB Richard Ellis listed an 11.1 percent vacancy rate, down from 14.6 percent last year.

An optimum vacancy rate, so that the Valley doesn't lose out to other markets for lack of available space, is 12 to 15 percent, Downey said. Anything lower means the market is tight, and prospective tenants face a hard time finding space to occupy immediately.

West Valley growth

New office inventory in the Valley doubled last year to 2.5 million square feet, much of it at the Scottsdale Airpark and in the West Valley, according to Cushman.

"The West Valley will be the submarket to watch in the next two to five years," Downey said. "Recent residential growth in the area and the addition of amenities like the University of Phoenix Stadium have helped position this submarket for future commercial growth."

Grubb & Ellis, meanwhile, is projecting that north Scottsdale and the southeast Valley along Loop 202, known as the Santan Freeway, will see the most construction.

Developers, meanwhile, are focused on adding offices, with nearly 4.9 million square feet now under construction around the Valley, according to the Cushman report.

CB Richard Ellis expects 3.7 million square feet of space to become available in 2007.

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