Correction Incoming for Class A Office, Says Moody's

For most of 2022, there was a little bit of light for the beleaguered office sector in the form of Class A offices. Where Class B and C buildings struggled, Class A showed a steady uptick through the year. This was largely due to the ongoing efforts to provide best-in-class amenities, designed to tempt occupiers and workers alike back into office.

According to a recent Moody's Analytics article, however, that may be about to change.

Slipping Numbers

In their analysis of Q4 data, Moody's points out that for the first time in over a year, Class A office occupations in Central Business Districts (CBDs) have taken a downturn, finally matching the flagging performance of their Class B and C counterparts.

Moody's notes: "We still tend to agree that a "flight to quality" is a real phenomenon, but the net leasing activity is beginning to turn south even within those higher quality, urban assets."

They add that the current trajectory suggests Class A vacancies will continue to rise through 2024 and that they could "unfortunately tempt the historic high of 19.3% last hit during the Savings and Loan Crisis."

Urban and Suburban

The data shows that the trend outside of CBDs is a little steadier, however, even showing a small uptick for Class A after a slowdown period earlier in the year.

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Given these figures, Moody's says, suburban office properties in "lifestyle" communities or "urbanesque" areas "may end up being a decent safe haven."

It's a trend we've seen in general throughout the pandemic, with suburban offices showing a smaller change in vacancy rates compared to their CBD counterparts.

Cause and Effect?

Naturally, the current spate of high-profile loan defaults in the office sector has shaken up the space and, combined with rising vacancies, Class A office does seem to be headed for a rough time.

With that said, Moody's is quick to point out that we must consider the context of defaults by big players. For example, Columbia, which recently defaulted on $1.7 billion of office loans, is "in discussions with their lenders about restructuring the loan."

They add that part of the problem for Columbia in particular is the fact that one of the properties is partly rented out by Twitter, which famously stopped paying rent last year.

Moving Ahead

The conclusion? There's still a lot that remains to be seen about how the long-term situation plays out for Class A offices and there's certainly nothing set in stone for the sector. For now, however, we should expect to see some ongoing turbulence as the market adjusts to changing conditions.