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Pittsburgh's office vacancy rates continue to languish

Summary: In April 2020, *Policy Brief Vol. 20, No. 11* looked at the downtown Pittsburgh office vacancy rate for pre-pandemic 2019's fourth quarter. The conclusion of that *Brief*—the virus could be another impediment to a turnaround in the office market—turned out to be correct. The data for 2021's fourth quarter shows scant improvement in the city's office market as the pandemic continues its grip.

A recent newspaper article on the sale of three office buildings in the city's central business district (CBD) comments on how difficult the pandemic has been on the office market. A New York developer had purchased three older office buildings in 2016 with the goal of refurbishing them. One, the Allegheny Building, was sold to another property group. Two others, the Lawyer's Building (now the Pittsburgher) and Centre City Tower, will head to sheriff's sale.

While a spokesperson noted there were some tenant concerns regarding problems with construction at the former, for the latter the pandemic was the biggest problem as the building lost rental income and the developer couldn't pay the mortgage. According to the developer's spokesperson, "COVID was the nail in the coffin."

As has been well documented in past *Briefs*, the pandemic crushed the local economy. Job losses in the Pittsburgh region from nearly two years ago have yet to reach pre-pandemic levels, not to mention any lost growth that would have occurred. Certainly, that had to have an impact on the downtown office market as jobs were certainly shed. But the pandemic also brought about the work-from-home culture that seems here to stay. It is very likely that firms looked to lower office footprints, specifically rental costs, as the number of people physically in the office declined.

According to another recent article, BNYMellon is requiring employees to return to the office in early March 2022 after nearly two years of working from home, but on a hybrid schedule, a mix of days worked at home and in the office—perhaps a sign that a new office culture is taking root. It remains to be seen what the long-term effect on office space demand such an innovation will have.

Class A office space in the CBD

Office space is divided into two classes, A and B. Class A is considered premium space and the rest of the office space is rated as class B. In 2013 the vacancy rate for class A office space in Pittsburgh's CBD had its best showing with a rate of just 5.2 percent, the second-lowest rate of 53 major cities in national real estate firm Jones Lang LaSalle's office outlook survey (all real estate data in this *Brief* comes from JLL.com).

By the end of 2019, Pittsburgh's class A vacancy had risen to 15.9 percent. In each of the first two quarters of 2021, the rate rose even further—to 18.1 percent. In the fourth quarter, vacancies had improved slightly to 17.6 percent. Keep in mind, the vacancy rate is a measure of space not currently under lease, not necessarily that the space is simply unoccupied.

The *Policy Brief* from 2020 compared Pittsburgh to nine other cities: Austin; Boston; Charlotte; Cincinnati; Columbus; Dallas; Denver; Los Angeles and Seattle. Pittsburgh's CBD class A vacancy rate in late 2019 was better only than Dallas' (26.4 percent). The same cities are examined in this *Brief.*

At the end of 2021, Pittsburgh's CBD vacancy rate (17.6 percent) for class A buildings ranks better than Columbus (17.8 percent); Los Angeles (19.9 percent); Seattle (20.0 percent); Austin (20.8 percent); Denver (21.9 percent) and Dallas (34.1 percent). Boston (13.3 percent), Charlotte (16.1 percent) and Cincinnati (16.7 percent) had the best vacancy rates among the sample.

The class A market in Pittsburgh's CBD is also only one of four in this sample to have a "positive absorption" rate, although negligible. Positive absorption occurs when unleased square footage becomes leased as a percentage of total inventory. Negative absorption means that leased space becomes unleased.

In the Pittsburgh CBD, there are 13,512,018 square feet of class A office space. 39,538 square feet were leased, on net, year-to-date, for a year-to-date absorption rate of 0.30 percent. Only Charlotte (6.1 percent), Columbus (4.7 percent) and Austin (3.0 percent) had year-to-date positive absorption rates. The year-to-date absorption rate is calculated by taking the net absorption for the year and dividing it by the total inventory.

Note, too, that Pittsburgh is one of only four markets without any class A square footage under development (Seattle, Los Angeles and Dallas) within the CBD in 2021. Although a new office building is being constructed, with taxpayer money, on the site of the former Civic Arena and this will undoubtedly put more pressure on CBD vacancy rates.

Total office space in the CBD

The total vacancy rate for Pittsburgh's CBD (class A and B combined) reached 16.9 percent in the fourth quarter of 2019. It climbed to 19.6 percent in 2021's first quarter and then to 20.9 percent by the fourth quarter. This is the fourth best rate among this small sample behind only Boston (14.6 percent); Charlotte (16.0 percent) and Austin (19.7 percent). Of all the cities in this group, only Dallas' first quarter total CBD vacancy rate improved from first quarter 2021 to the fourth quarter (31.1 percent to 29.8 percent).

The Pittsburgh CBD has a total of 18,972,607 square feet of office space with 5,460,589 square feet designated as class B space. Pittsburgh's class B space saw 388,161 square feet be negatively absorbed (went from being leased to unleased)—a rate of negative 7.1 percent.

In this sample, only four had positive absorption rates for the total office space in the CBD, Charlotte (4.9 percent); Seattle (4.3 percent); Austin (2.7 percent) and Columbus (1.1 percent).

In this sample only three cities had no new square footage (either class) under development at the end of 2021's fourth quarter—Pittsburgh, Los Angeles and Seattle.

Conclusions

The pandemic continues to have a grip on the economy. Jobs have yet to climb back to their pre-pandemic levels, let alone pre-pandemic plus lost growth. Firms within Pittsburgh's central business district are slowly welcoming employees back to the workplace. However, the work-from-home culture may be here to stay as employees in a labor-slanted market may demand more flexibility to work from home, even if just a day or two per week.

This recovery of the office market in Pittsburgh's CBD may be slower than usual due to this new work-from-home culture. But more importantly, as we have documented many times, Pittsburgh's ability to draw new firms or businesses into its borders has long been hampered by burdensome regulations, high taxes and a fealty to unions—strictures that existed, and persisted, before the pandemic hit.

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