

The office sector's outlook is brightening

Recent performance trends could signal a broader recovery, but risks remain



New York's office market, the world's largest, drove a shift in office occupancy in 2024 that could signal a broader recovery ahead. (Joseph DiBlasi/CoStar)

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Demand for office space turned meaningfully positive at the end of 2024 for the first time since 2021. Meanwhile, the U.S. office market has entered a period of historically low supply of completions that is expected to last for years.

The combination of those two trends could mark the beginning of the end of a protracted period of difficulty and underperformance for the office sector — but it is not out of the woods yet.

The recent change in momentum is one reason for a more optimistic forecast. The latest base case forecast from CoStar now calls for the national office vacancy rate to peak near 14.5% in late 2026. This is about 70 basis points lower than earlier versions of the forecast and occurs four to six quarters earlier than previously projected. Rent growth, which was previously forecast to turn negative in 2025, is now expected to stay above water, albeit at an anemic growth rate of about 1%.

Two primary factors have driven this change in the forecast. First, economic and job growth were stronger than anticipated in 2024. This, along with expectations for stimulative fiscal policy from the new administration, has led economists to raise their forecasts for GDP growth and office-using employment through 2025 and into 2026.

Second, move-outs by office tenants substantially slowed in the latter part of 2024, suggesting that occupiers are closer to the end of adjusting their footprints to post-pandemic workplace arrangements than they once appeared.

Reasons for optimism

Expectations for more frequent office attendance are a likely factor in the decision by office tenants to hold onto more space. Multiple indicators, including transit ridership and mobile location data, showed a rise in office attendance in 2024. Several large organizations, including tech giant Amazon, big bank JPMorgan Chase and even the Federal Government, have recently announced requirements for more in-office work.

If more employers follow suit this year, the attendance recovery could accelerate. This could lead some occupiers to add more space to accommodate their workers even if their headcounts do not grow appreciably.

The rapid drawdown of the supply pipeline is another positive sign for higher occupancy prospects. With less space available in well-located premium buildings, office occupiers who may once have let go of existing space in favor of smaller, more efficient layouts may now choose instead to stay in place.

Finally, stronger economic growth in the near term could lead to a reacceleration of hiring in knowledge-oriented sectors of the economy. This, in turn, could spur demand for space, especially in the professional service industries that have continued to use offices in more traditional ways.

On the other hand

There are also reasons for caution. So far, the recovery in office demand has been very limited in geographic scope. Occupancy may have risen by 2.7 million square feet in the final quarter of 2024, but almost all of that increased occupancy was in [New York](#), which, according to mobility data provider Placer.ai, led all major markets in December office attendance.

Other gateway office markets, including Boston, Chicago, Los Angeles and Washington, DC, were still losing occupancy at the end of 2024. More broadly, occupancy decreased in about half of the 50 largest office markets in the United States despite the net national gain.

The lack of breadth in the nascent recovery is not the only downside risk to the forecast. The experience of the last two years has demonstrated that office-using job losses are possible even absent a general recession. Job growth in professional services and ambulatory healthcare have fueled demand in the past year, but other office stalwarts, such as the technology sector, have seen employment stagnate.

Moreover, the specter of downsizing looms at several large employers, including the Federal Government. The Department of Government Efficiency purportedly seeks to reduce the Federal Government's headcount and work with the U.S. General Services Administration to cancel lease commitments and sell many Federally owned buildings.

While the effects of these actions would be concentrated in and around the [District of Columbia](#), they may nevertheless indicate a broader risk. Some private-sector organizations, such as Amazon, have also hinted at layoffs, which would mitigate the need for office space.

Despite these risks, the overall outlook for the office sector is for a slow return to fundamental balance. Slow, steady employment growth should support mediocre demand recovery, resulting in a structurally higher vacancy rate.

Even so, limited supply additions and the concentration of vacancy in older, noncompetitive buildings should support overall rent growth in office properties, especially at premium buildings. As this plays out, there will likely be wide variability in performance trends across markets.