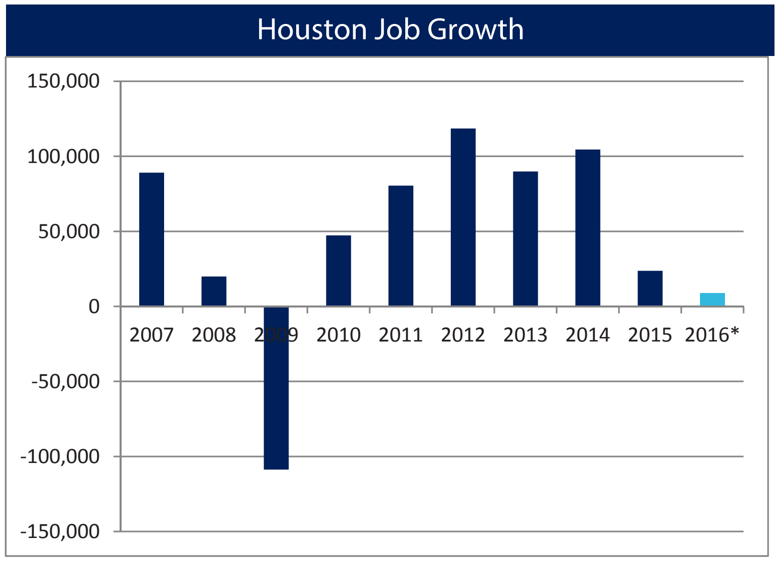
AVISON YOUNG

HOUSTON INDUSTRIAL MARKET MONITOR
FIRST QUARTER 2016

Quarterly industrial activity increases despite downturn

The Houston industrial market recorded over 1.2 msf in absorption in the first quarter. Vacancy rose slightly due to new product deliveries. Asking rates remained stable.

Economic Overview



*Feb'15-Feb'16

Energy analysts predicted that falling energy prices would equate to falling oil production, thereby stabilizing the price of oil in the near term. The U.S. rig count fell to 450 at the beginning of April, the lowest rig count to be recorded in the 29 years that Baker Hughes has kept track. However, advances in technology have made drilling more productive. Crude oil inventory is at an all-time high, recording 534,834 barrels at the end of March. To put this in perspective, crude inventories went above 400,000 barrels for the first time at the beginning of 2015 and have since increased by 34%. Low oil prices have not led to a cut in production, and an even more volatile energy market is predicted going forward as over-supply concerns continue. Energy companies, particularly those that are over-leveraged, are targets for either bankruptcy or merger and acquisition activity. These companies continue to make cuts in both jobs and budgets. The Mining & Logging sector has shed 22,700 Houston jobs since peaking in December 2014. The Houston Manufacturing sector has shed 28,200 in this time. However, health care, education, and the petrochemical industry have slightly offset contraction in the struggling upstream and midstream energy industry and manufacturing sector. Houston's population growth has also benefitted the overall health of the city. According to the latest Census data, the Houston metro area added 159,000 residents in 2015, adding more people to its overall population than any other metro.

Houston gained 9,000 jobs in the last 12 months ending in February, a 0.3% increase in employment. The GHP forecasts that Houston will add 20,000-30,000 jobs in 2016. The unemployment rate registered 4.7% in February, still below the national unemployment rate of 5.0%. The Houston Purchasing Managers Index (PMI) fell to 44.5 in February. Readings below 50 indicate contraction in regional production in the short term. This is the 14th consecutive month to report contraction. Health care and Financial & Professional Services were reported to be the only sectors of the economy showing significant strength, while wholesale trade, durable goods manufacturing, and oil and gas exploration were causing the greatest concerns.

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The median price for a single-family home was up 5.3% year-over-year in January to $200,000. This is an all-time high for January in Houston.

The U.S. Baker Hughes rig count fell to 450 at the beginning of April, although crude oil inventories remain at historic-highs.

The price of oil averaged $33.38/bbl. in the first quarter.

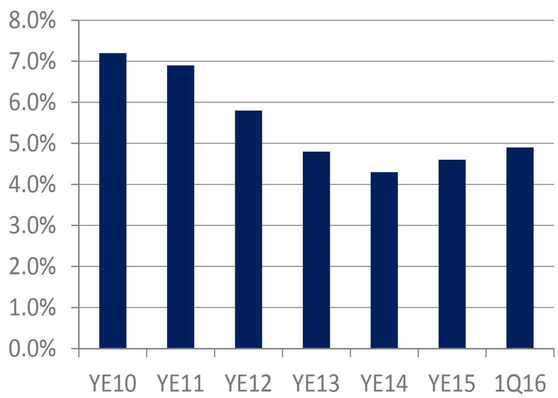
Economic sectors reporting growth in the last 12 months include Leisure & Hospitality (7.2%), Health Care (4.5%), Construction (3.3%), Government (2.6%), Finance (1.1%), and Trade, Transportation & Utilities (0.9%).

The Houston PMI registered 44.5 in February, indicating contraction in regional production in the short term.

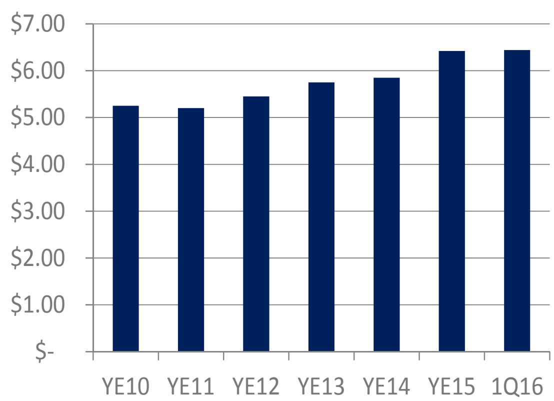
Industrial Market Overview

The Houston industrial market saw an uptick in activity in the first quarter despite the energy downturn. Quarterly absorption once again registered over one million square feet. Leasing activity improved compared with 2015, but it is still down when compared to the historic average. Vacancy increased slightly in the first quarter, although it remains near historically-low levels. The industrial market experienced years of supply struggling to meet demand, resulting in an incredibly tight market with sound fundamentals. Vacancy still ranks among some of the lowest in the U.S. Overall average asking rates have remained stable for the past six months, a trend that is expected to continue throughout 2016 in the midst of the energy downturn. Construction activity increased in the first quarter with many large projects breaking ground. New projects have remained very well preleased, particularly in the Southeast submarket near the Port of Houston.

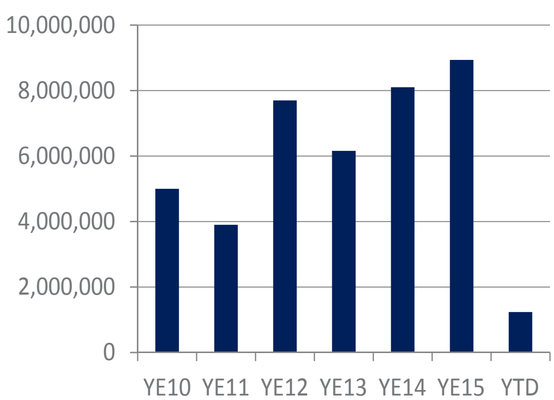
Vacancy Rates



Asking Rents



Net Absorption



ABSORPTION & DEMAND

4Q15 marked the first time since 2011 that the Houston industrial market recorded less than one million square feet of quarterly net absorption. Recorded absorption slowly declined throughout 2015 as the benefit of coming off of a boom year dissipated and industrial users pushed off making real estate decisions amidst the economic uncertainty. However, the Houston industrial market reversed this trend in the first quarter, recording over 1.2 msf in absorption, as well as an uptick in leasing activity in both existing and new product. This marks the 21st consecutive quarter of positive net absorption. Growth in the first quarter was mainly attributed to two factors- industrial users expanding due to Houston's significant population gains and the petrochemical boom. Although these gains bode well, the industrial market is still driven by the energy industry. Manufacturing, warehouse, and distribution properties that serve Houston's upstream, midstream, and service companies remain particularly vulnerable. Submarkets that recorded negative net absorption in the first quarter include the Southeast (-274,365 sf), CBD Inner Loop (-211,164 sf), and the South (-151,420 sf). The Southwest submarket led Houston in absorption in the first quarter with 620,337 sf. The Northeast submarket has gained traction in recent years. FMC Technologies took occupancy of the first phase of its campus in the Northeast submarket. The company is consolidating its operations on 173 acres in Generation Park. The first phase consists of 640,000 sf of industrial space and 369,000 sf of office space. Future development of the campus will be dependent on the market, but the campus could total up to 1.7 msf.

NOTABLE FIRST QUARTER ACTIVITY:

- ***Advance Auto Parts*** leased 441,000 sf at Beltway Crossing NorthWest. The company will take occupancy in August.
- ***Fedex*** broke ground on its new 800,000-sf ground facility in the Northwest submarket, located off of the Grand Parkway expansion. It will be Fedex's largest ground facility in Texas with an estimated completion date of August 2017.
- ***FoxxConn Technology Group,*** the maker of Apple's iPhone, took occupancy of 400,250 sf at 8303 Fallbrook Dr. in the Northwest submarket. The company needed an advanced manufacturing facility located closer to their clients.
- **National Oilwell** Varco took occupancy of 383,750 sf of warehouse space at 8017 Breen Dr. in the North submarket.
- **Plastic Express** preleased 394,489 sf in Phase II at Port 225. The 775,000-sf Phase II is 65% preleased and will deliver in 2Q16.

VACANCY & AVAILABILITY

New deliveries continued to outpace absorption in the first quarter, causing vacancy to increase by 30 basis points from year-end 2015 to 4.9%. This still ranks among some of the lowest vacancies in the U.S. Vacancy registered 4.3% at this point last year. The North submarket continues to have the highest vacancy rate in Houston, although it fell by 10 basis points from the previous quarter to 7.1%. Vacancy in the Southeast is up by 30 basis points from the previous quarter but remains low at 3.6%.

Available sublease space ticked up in the first quarter to over 3.6 msf, representing 0.8% of Houston's industrial market. The majority of this space is located in the North and Northwest submarkets. Sublease space typically accounts for 0.5%-0.6% of Houston's industrial availability. Sublease availability is expected to grow throughout 2016 with the continued downsizing in the energy industry.

ASKING RATES

Average asking rates remained relatively unchanged from the previous quarter, increasing by just $0.02 per square foot (psf) to $6.44 psf NNN. Overall average asking rates have remained stable for the past six months. Year-over-year, asking rates have increased by 8.8%. Asking rate changes were experienced differently across the industrial product types. Flex properties and Warehouse & Distribution space both recorded slight gains from the previous quarter, increasing by 1% and 2%, respectively. However, manufacturing asking rates fell by 8% from the previous quarter. Manufacturing properties have been hardest-hit in the current downturn.

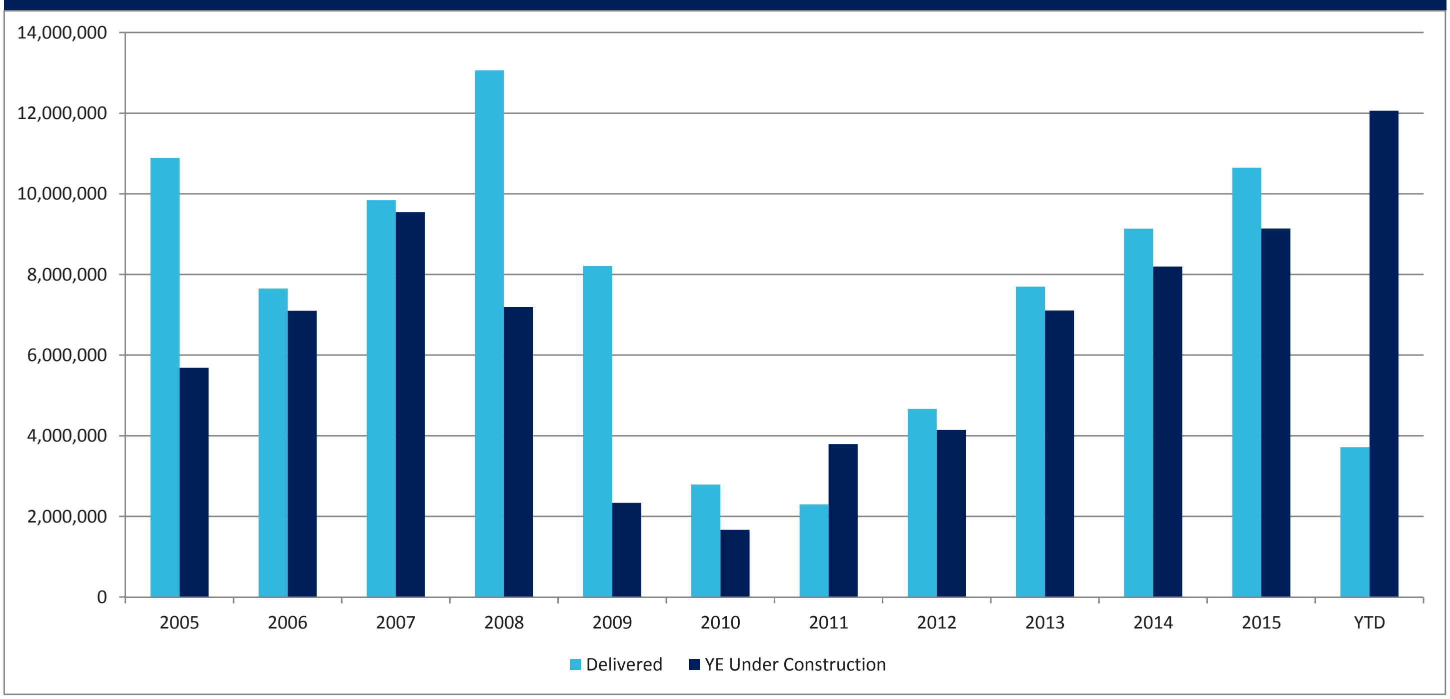
CONSTRUCTION

Construction activity increased in the first quarter with over 12.1 msf underway. The Northwest submarket leads in construction. Although energy service companies and manufacturers (both heavily located in the Northwest) are dampening new development, supply and logistics companies are drawn to the area due to the Grand Parkway, Houston's new third major highway loop. The Grand Parkway section between U.S. 59 South and U.S. 59 North opened in the first quarter, running the full length of the Northwest submarket. Fedex broke ground on its new 800,000-sf facility in Cypress, located off of the Grand Parkway expansion. It will be Fedex's largest ground facility in Texas and will employ 400 people. The new facility has an estimated completion date of August 2017. Daikin Industries, a major HVAC manufacturer, broke ground on its 4-msf campus in the Northwest in 2015. The new development accounts for over 33% of total industrial construction in Houston. The company is consolidating operations at the new location which is set to deliver in mid-2016.

Construction activity in the Southeast submarket increased significantly after years of limited development. Over 1.1 msf delivered in the first quarter, and another 1.7 msf currently underway. Expansion in the plastics and petrochemical industries has led to increasing asking rates, therefore justifying new industrial development. New construction projects have preleased well, particularly those that offer rail-served distribution space near the Port of Houston. Plastic Express preleased 394,489 sf in Phase II at Port 225. The 775,000-sf Phase II is now 65% preleased and is expected to deliver in mid-2016.

The Houston market delivered 3.7 msf of new space in the first quarter. Despite the energy downturn, space in Houston's industrial market remains very tight. The conservative development pipeline will add much needed space to alleviate the tight market and has yet to be overbuilt.

Houston Industrial Development Timeline



NOTABLE BUILDINGS UNDER CONSTRUCTION

- Daikin Manufacturing & Distribution Center (4,000,000 sf). Northwest.
- FedEx Distribution (800,000 sf). Northwest.
- Bay Area Business Park Phase 2 (830,000 sf). Southeast.
- Fallbrook 1 (500,400 sf). North.
- Port Crossing Commerce Center Bldg. B4 (415,272 sf). Southeast.
- Port 225 Building 4 (394,489 sf). Southeast.
- Stafford Grove (351,960 sf). Southwest.
- 233 S Cravens Rd. (303,335 sf). Southwest.
- 14151 E Hillcroft St Phase I (240,000 sf). Southwest.
- FloWorks (225,000 sf). South.
- Prologis Greens Parkway (213,218 sf). North.
- Park 8Ninety (208,907 sf). Southwest.
- Fallbrook 2 (193,000 sf). North.

Largest 1Q16 Transactions

Tenant Name	Building	Submarket	Square Feet
Advance Auto Parts	Beltway Crossing Northwest	Northwest	441,000
Plastic Express	Port 225	Southeast	394,489
United Stationers Supply Co.	Cole Creek Business Park	Northwest	211,680

Trends to Watch

Employment: Houston added 9,000 jobs in the 12 months ending in February

Active Markets: Southeast, Northwest, Southwest

Market Drivers: Petrochemical Industry, Health Care, Population Growth

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CANADA'S BEST MANAGED COMPANIES