

Houston



Quick Stats

72,600

Jobs created during the 12 months ending February 2019

4.2%

February unemployment rate in Houston, down from 4.7% in February 2018

7.2

Msf of sublease space now listed on the sublease market, down from a high of 11 msf in 2016

15.9%

Direct vacancy in Houston's office market

2.5

Msf under construction

Positive absorption and lower vacancy rates recorded in the first quarter are encouraging signs of progress in Houston's office market. Direct net absorption remained positive for the third consecutive quarter, with the most recent 12-month total a positive 790,000 sf. This positive momentum builds confidence for Houston's office market recovery.

Vacancy rates have shown consistent improvement during the last two years. The first-quarter direct vacancy rate of 15.9% represents the lowest recorded since first-quarter 2017's 15.6% rate.

Local employment growth has been steady, with the unemployment rate dropping to 4.2% in February from January's 4.5% and last February's 4.7%. For the 12 months ending February 2019, the Houston metro area created 72,600 jobs, a 1.9% increase year-over-year, according to Texas Workforce Commission statistics. The leading job growth sector was durable goods manufacturing with 15,200 new jobs.

Overall rental rates are also trending higher each quarter with the current asking rate at \$30.73 per square foot (psf) overall and

\$36.63 psf for class A. Concessions are available, especially in submarkets with large amounts of available space.

Newer, modern buildings are driving many older class A properties to invest in major upgrades with amenities to attract and retain quality tenants. Downtown's Houston Center and Allen Center are working on significant improvements, which has already resulted in increased leasing activity for Houston Center. The flight-to-quality factor – firms opting for office efficiency in newer properties – is keeping availability high as firms leave larger, vacant office spaces behind.

Absorption and Demand

Direct positive net absorption returned to the office market for a third consecutive quarter, with 386,929 sf recorded during the first quarter. Overall class A and C properties reported direct net gains during the first quarter, with class A properties recording the highest absorption of 470,931 sf. Suburban properties led in class A absorption, recording a positive 520,704 sf compared to the Central Business District's (CBD) class A negative absorption of 49,773 sf.

Broken down by submarkets, the Woodlands submarket recorded the highest positive absorption of 408,796 sf during the first quarter, primarily due to American Bureau of Shipping's occupancy of the company's new 303,137-sf offices in CityPlace 2. This is the second consecutive quarter the Woodlands submarket recorded the largest gains due to occupancies in Springwoods Village; during fourth quarter, HP moved into its two new buildings totaling 378,402 sf.

Other large movement in class A properties during the first quarter included Asurion's occupancy of 129,966 sf in Legacy at Fallbrook in the West Belt submarket and WeWork's 55,400 sf at 1725 Hughes Landing in The Woodlands. For class B, the Houston Forensic Science Center moved into 83,800 sf at 500 Jefferson downtown.

The solid leasing activity in the newest buildings in the CBD indicates that the flight-to-quality trend continues to dominate the market. Capitol Tower, scheduled for delivery in June, is almost 80% preleased. 609 Main, the newest 1.1-msf tower started in the downturn and completed in 2017, steadily signs up tenants. Developed by Hines, 609 Main was 49% preleased when it delivered to the market and is currently 86% leased with more deals reportedly underway.

Vacancy & Availability

The direct vacancy rate decreased 40 basis points to 15.9% during the first quarter from 16.3% last quarter. Vacancy improved overall during the last 12 months, decreasing from 2018's first quarter rate of 16.7%. Vacancy rates

decreased slightly this quarter for class A properties to 17.6% from 17.9%, and for class C, which is now 7.7% vacant. Class B properties maintained the same 17.9% vacancy rate of the previous quarter.

Comparing submarkets, the Northeast Near submarket (defined as being inside Beltway 8) boasts the lowest vacancy rate at 4% and the Greenspoint submarket came in with the highest rate at 44.8%. However, Greenspoint is making some headway recuperating from several large moveouts during the last few years including Exxon Mobil, Noble Energy and most recently, the American Bureau of Shipping. Vacancy rates in all other submarkets range from 5.2% to 21.9%.

Direct availability citywide increased from 20.4% last quarter to 21.0% this quarter. Fluctuating in the 20% range during the last 12 months, availability overall including sublease space is now at 24.0%. Leasing activity slowed during the first quarter to 3.1 msf, and no building completions took place during the first quarter.

Total available sublease space dipped to 7.2 msf from fourth quarter's 7.4 msf, representing a 31% decrease of sublease space recorded in 2017. Total sublease space represents about 13% of the 54.9 msf available, and five submarkets represent 79% of all sublease space available.

Construction

The construction pipeline remains limited, with eight buildings totaling 2.5 msf under construction and 39.6% preleased. The CBD represents about 75% of the total square footage.

Although no buildings were completed during first quarter, one new property, Park Place River Oaks, broke ground. The 207,202-sf property in the West Loop submarket is reported 21% preleased with completion in March 2020.



Three properties are scheduled for completion during the second quarter: CityPlace 1 and City Place in Springwoods Village located in the Woodlands submarket and Capitol Tower in the CBD.

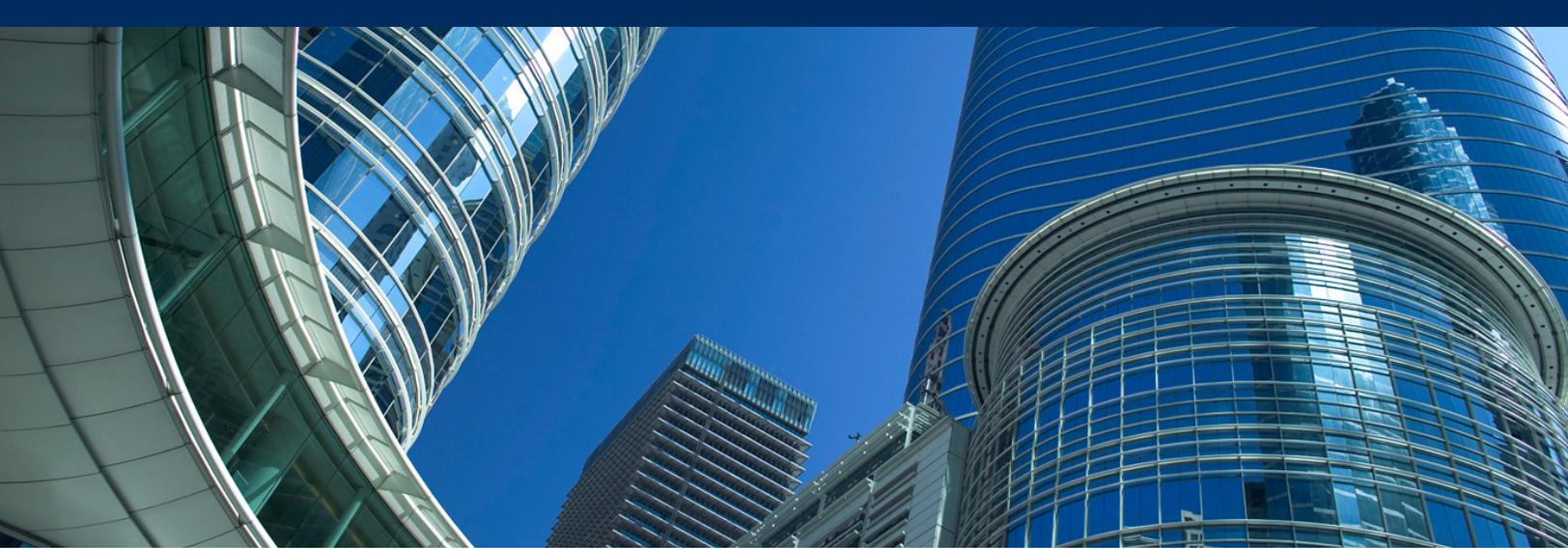
Asking Rates

Overall average asking rates have increased slightly to \$30.73 psf gross from the previous quarter's \$30.42 psf and 3.9% from the \$29.59 recorded year-over-year. Asking rates have been relatively stable and reported in the \$29-\$30 psf range during the last five years. Throughout the downturn, landlords have offered various concessions ranging as high as year-long rent abatements and allowances covering the full cost of tenant improvement construction.

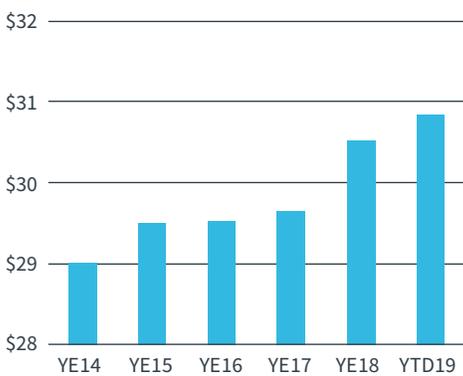
Asking rates for the different submarkets range from \$16.39 psf in the Southwest to \$43.67 in the CBD. The suburban submarkets with the highest rates include the West Loop, Greenway Plaza and the Woodlands.

Class A rates overall are up to \$36.63 psf and gaining ground over first quarter 2018's \$35.02 psf. CBD properties are currently quoting the highest class A rates on record at \$43.67 psf, while average CBD sublease rates are about half the direct rate at \$21.87 psf. Average suburban class A rates are currently \$32.22 psf.

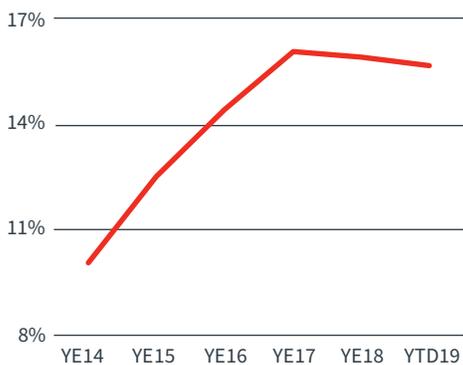




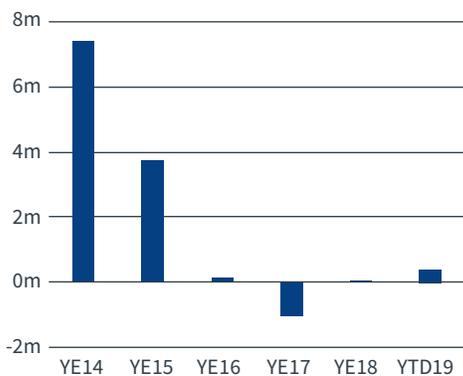
Asking Rates



Vacancy Rate



Net Absorption



First-Quarter Highlights

- **Deloitte US** renewed its 204,210-sf lease in Heritage Plaza and will be renovating the space.
- Three tenants are taking over about 65% of the former CB&I space in Lake Front North in Hughes Landing in The Woodlands. **Arena Energy** has leased 87,231 sf in Building 1 at 2103 Research Forest. **Energy** and **Exxon Mobil** have leased 54,000 sf and 26,000 sf, respectively, in Building 2 at 2107 Research Forest. CB&I sold the two buildings totaling 257,025 sf last year after being acquired by McDermott International.
- **Asurion** occupied 129,966 sf in Legacy at Fallbrook, 10720 W. Sam Houston Parkway in the West Belt submarket.
- **American Bureau of Shipping** moved into its 303,127-sf space in CityPlace 2, 1701 City Plaza Drive, in the Woodlands submarket, representing the largest absorption during the first quarter.
- One office building, **Park Place River Oaks**, broke ground during first quarter. The new building will add 207,200 sf to the West Loop submarket in March 2020.

Trends to Watch

With its central location within the U.S. and the Americas, Houston is an important office base. The following are regional updates for key economic indicators.



Oil

The price of oil has fluctuated between \$50 to \$65 recently after a high in the \$70s in October 2018.



Employment

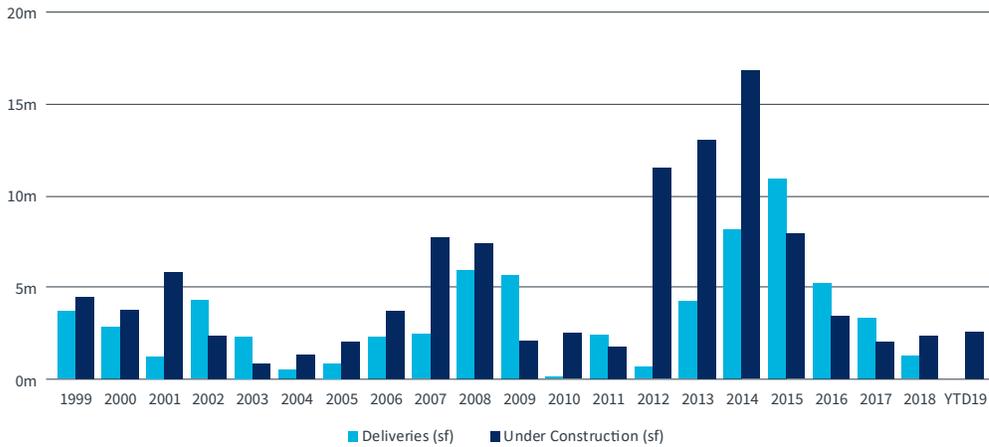
Employment grew 1.9%, creating 72,600 jobs for the 12 months ending February 2019.



Purchasing

The Purchasing Manager's Index (PMI) registered 64 in March 2019, its highest reading in six years, up from 56.1 in February.

Construction Timeline



Select Under Construction

Building Name	Building Address	Rentable Building Area	% Preleased	Projected Delivery	Submarket
Texas Tower	845 Texas Avenue	1,106,581	32.8%	October 2021	CBD
Capitol Tower	800 Capitol Street	780,593	79.6%	June 2019	CBD
Park Place River Oaks*	4200 Westheimer Road	207,202	21.0%	March 2020	West Loop
Chasewood Crossing Three	19350 State Highway 249	156,000	0.0%	August 2019	FM 1960
CityPlace 1	1700 City Plaza Drive	149,500	18.0%	June 2019	Woodlands
City Place	1401 Lake Plaza Drive	48,840	45.2%	May 2019	Woodlands
Buffalo Heights	3663 Washington Avenue	35,363	0.0%	September 2019	Midtown

*Broke ground Q1 2019

Select First-Quarter Lease Transactions

Tenant	Building Name	Building Address	Size (sf)	Submarket
Hunton Andrews Kurth*	JP Morgan Chase Building	600 Travis Street	134,763	CBD
Asurion	Legacy at Fallbrook	10720 W. Sam Houston Parkway	129,966	West Belt
UniveralPegasus International*	Loop Central II	4848 Loop Central Drive	113,764	Bellaire
Forum Energy Technologies Inc.*	Sam Houston Crossing II	10344 Sam Houston Park Drive	108,639	Northwest
Direct Energy	2 Houston Center	909 Fannin Street	105,579	CBD
Constellation (sublease)	Kinder Morgan Building	1001 Louisiana Street	94,000	CBD
Arena Energy	Lake Front Building 1	2103 Research Forest	87,231	Woodlands

*Renewals

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Properties

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For more information, please contact:

Patsy Fretwell
Research Manager
713.993.7151
patsy.fretwell@avisonyoung.com

Jack Penman
Marketing Manager
713.993.7693
jack.penman@avisonyoung.com