



Houston office market report

Q4 2023

**AVISON
YOUNG**

Houston office market trends

671k sf

Net absorption concentrated mostly in high quality product

Despite a 362k square foot (sf) uptick in Q4, Houston's office market closed 2023 with a net loss of 410k sf. The Trophy and class A assets thrived, recording a robust 671k sf of positive absorption, driven by companies seeking high-quality, sustainable spaces in prime locations. Meanwhile, class B properties continued to struggle, shedding 1.1 msf as tenants downsized or relocated to newer buildings. This uneven performance reflects a widening gap between premium and lower-tier properties. As a result, investing in renovations and building amenities remain a key trend among landlords looking to attract and retain new tenants.

12.2%

Vacancy in product built since 2010 continues to outperform

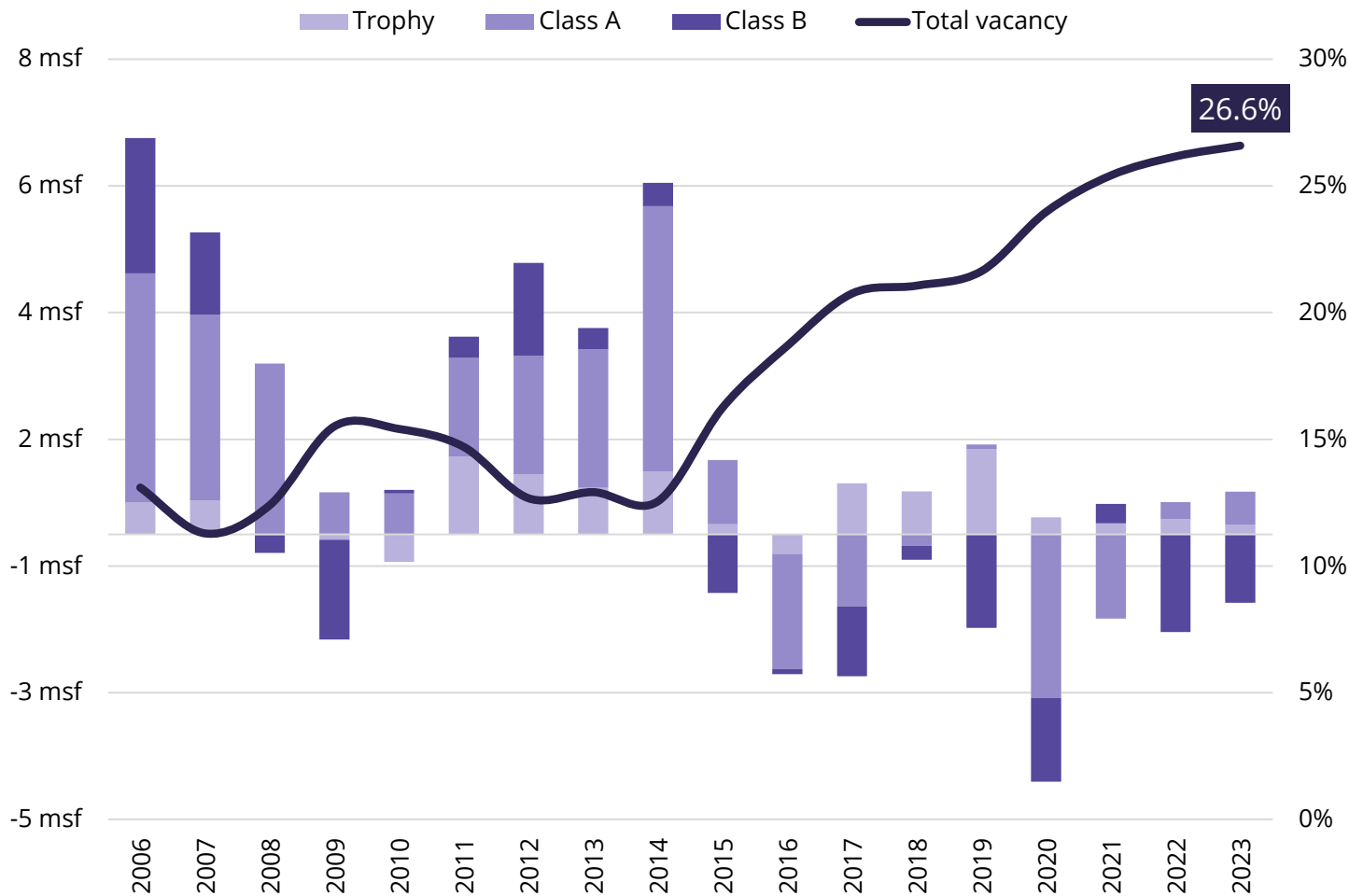
The office sector continues to grapple with ongoing challenges characterized by elevated vacancy rates but is showing signs of edging closer to recovery. Nearly 79% of the citywide vacancy is concentrated in buildings constructed 20 to 50 years ago, while office product built since 2010 is only 12.2% vacant. As the flight to quality trend persists, some older, less-desirable office buildings may face obsolescence. Once interest rates begin to fall and inflation eases, the conversion of vacant office buildings to other uses could become more attractive and financially viable, especially if there are any incentives offered by state and local government entities.

-28.9%

Leasing velocity during second-half slows down

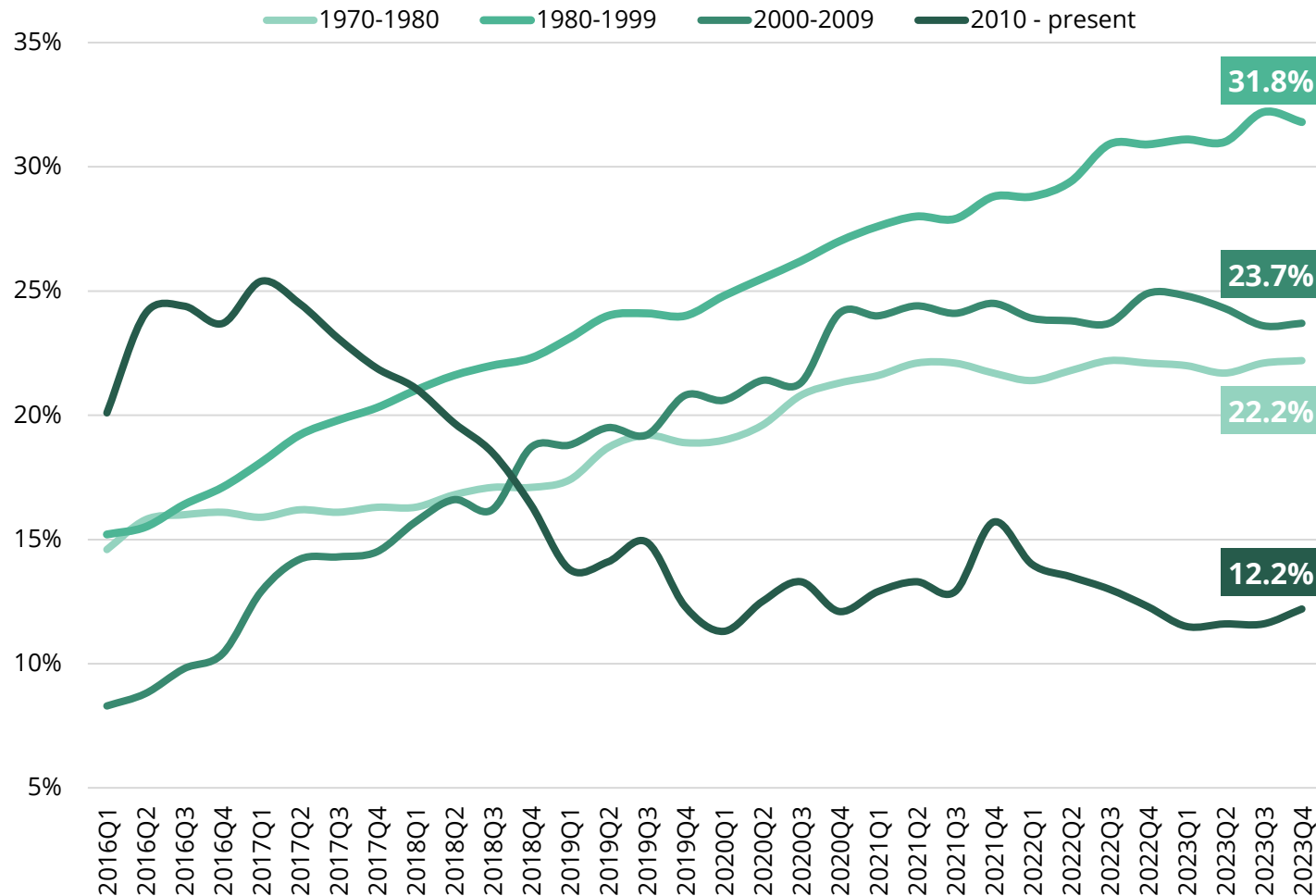
Leasing velocity, which started off strong in the first half of 2023, has cooled significantly due to the tightening financial conditions and economic slowdown. This has led to a 28.9% decline in annual leasing volume compared to the prior year, and a 38% decline compared to the five-year pre-pandemic average. Some companies, preferring short-term solutions due to capital constraints, are contributing to this decline. However, the presence of several large tenants in the market, some with already-negotiated agreements nearing completion, could lead to a substantial shift in leasing activity in the coming quarters.

Houston office net absorption by class



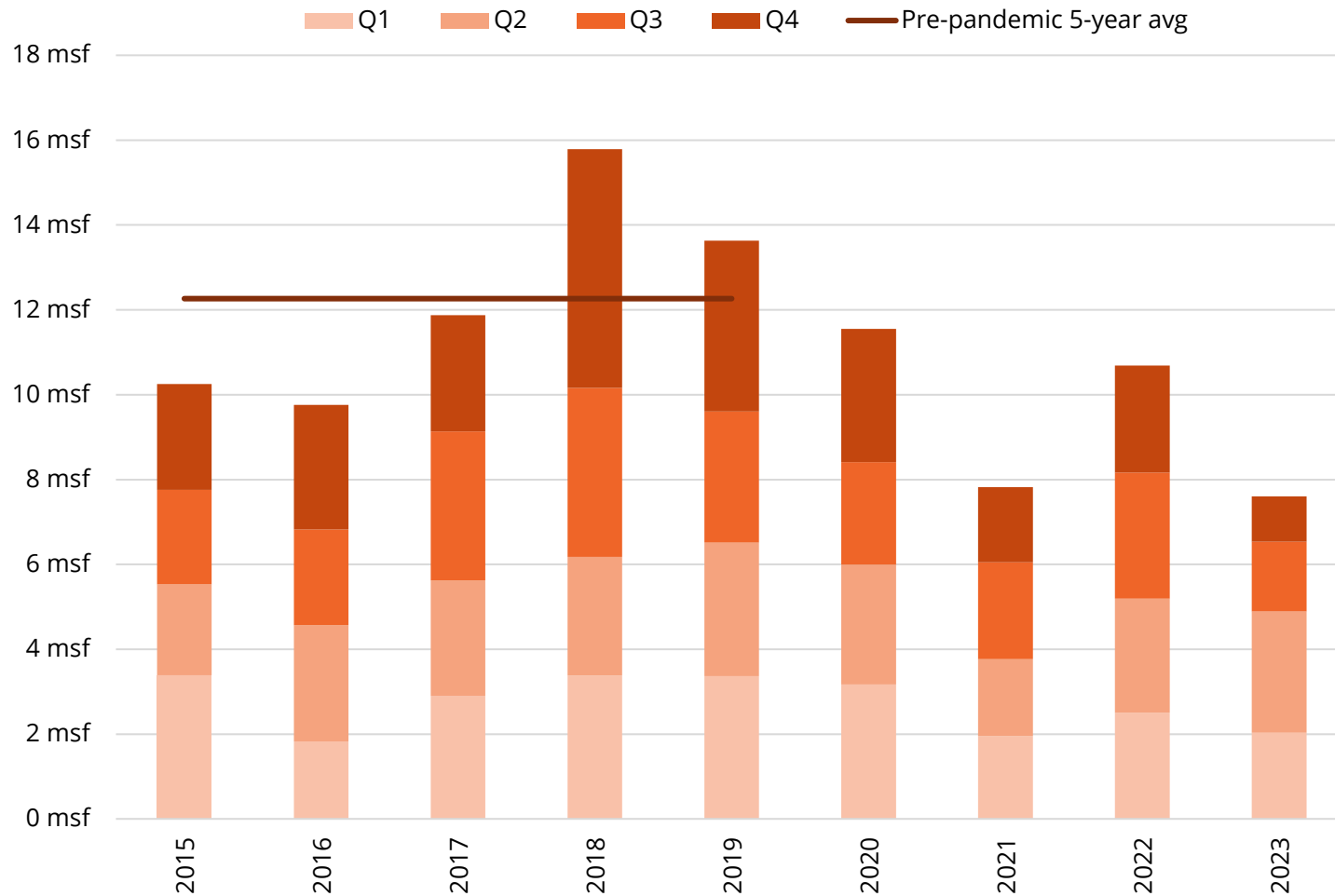
Houston's office vacancy rate has climbed to record highs with most of the occupancy losses taking place in older vintage assets while trophy and class A product continues to lead in the recovery.

Total vacancy by vintage year



A persistent flight-to-quality trend is driving a significant disparity in vacancy rates with trophy and new product built since 2010 outperforming older vintage assets.

Historical office leasing activity



Leasing activity volume declined by 28.9% below the prior year and remains 38% below the 5-year pre-pandemic average, reflecting the broader slowdown in economic growth.

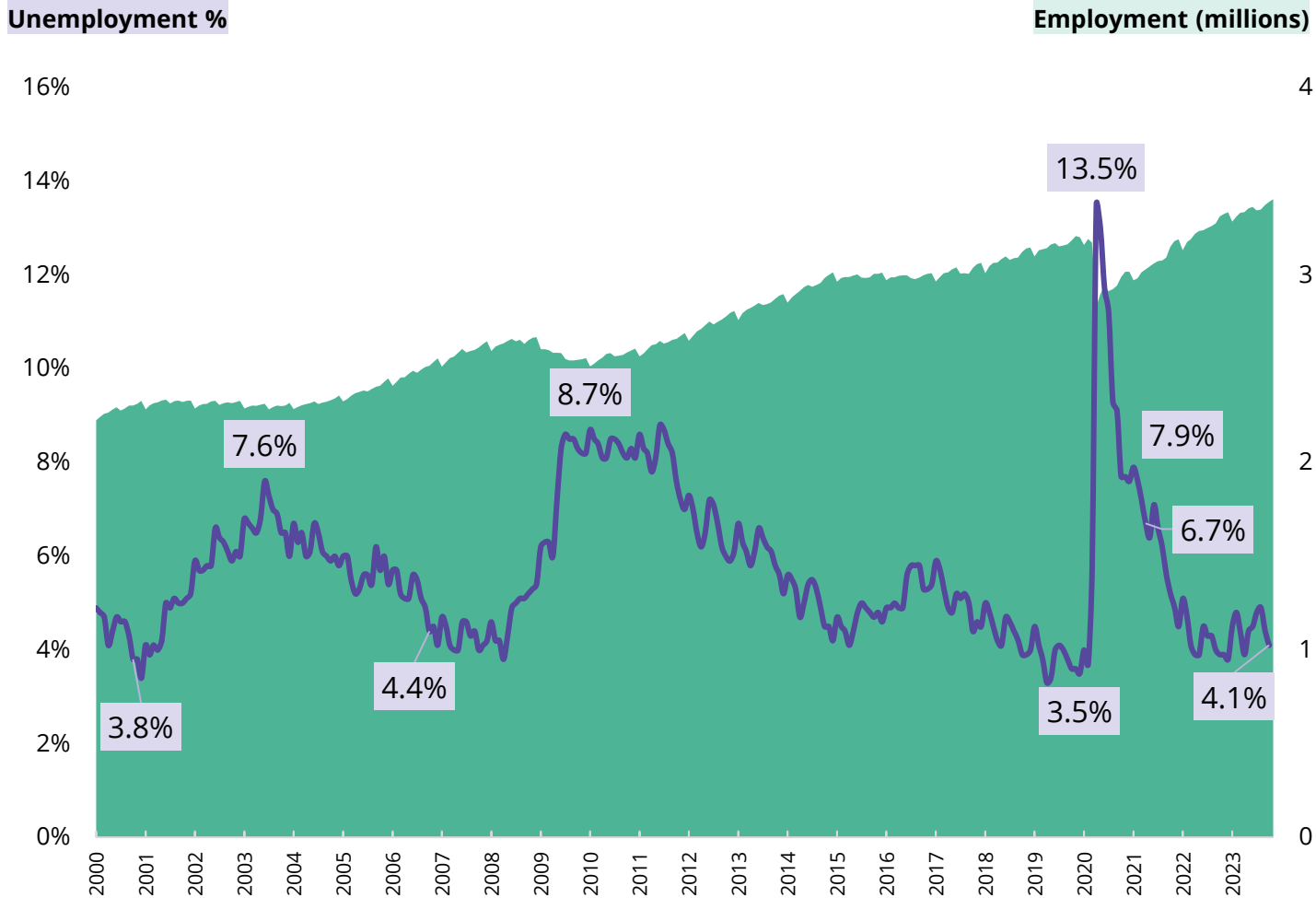
Source: AVANT by Avison Young, CoStar
Note: Limited to deals 10k sf or greater, which includes relocation, renewals, expansions and subleases

Houston employment trends

Let's examine the economic trends impacting the office sector



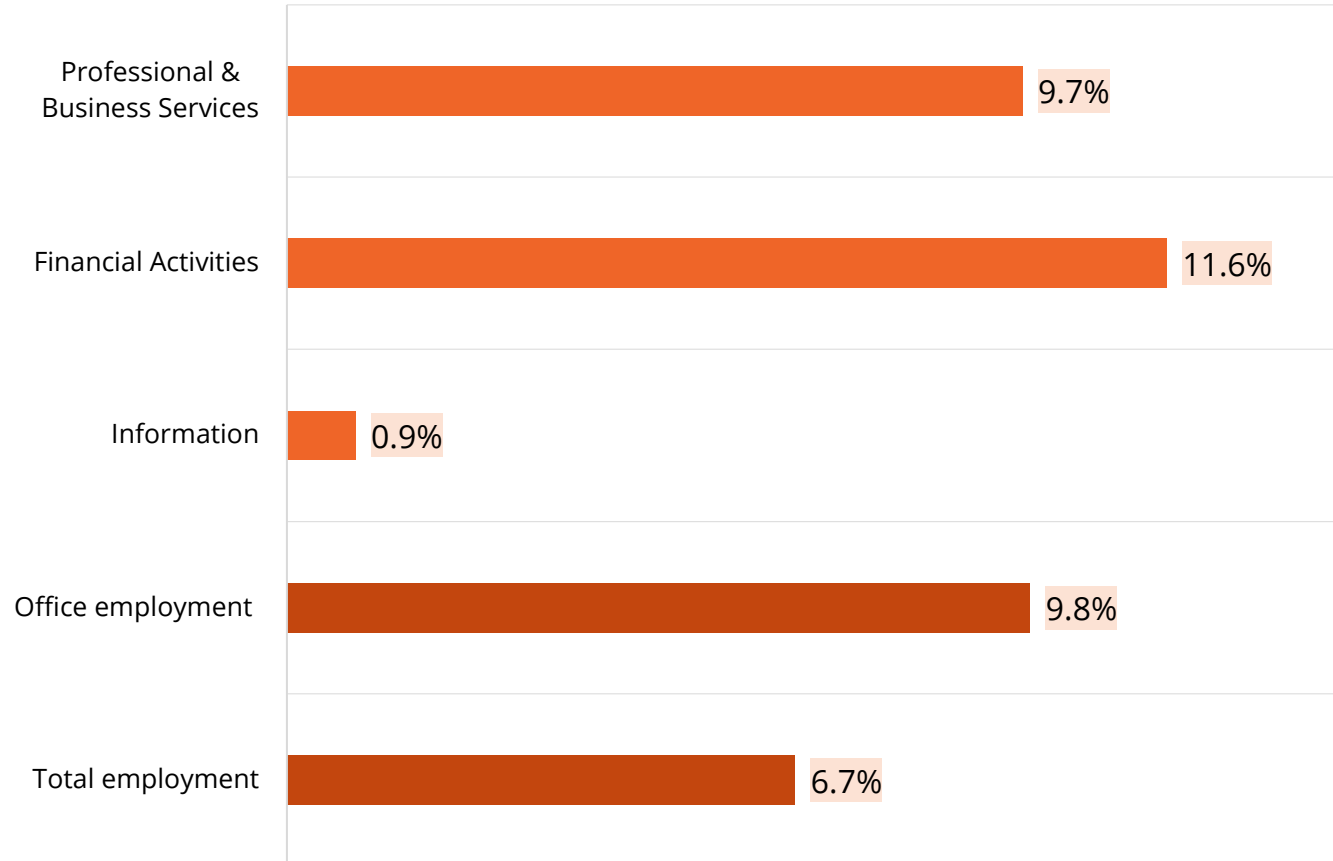
Employment and unemployment rate



Houston's employment base has expanded by nearly 78k jobs in the past 12 months, while unemployment remains relatively low at 4.1%.

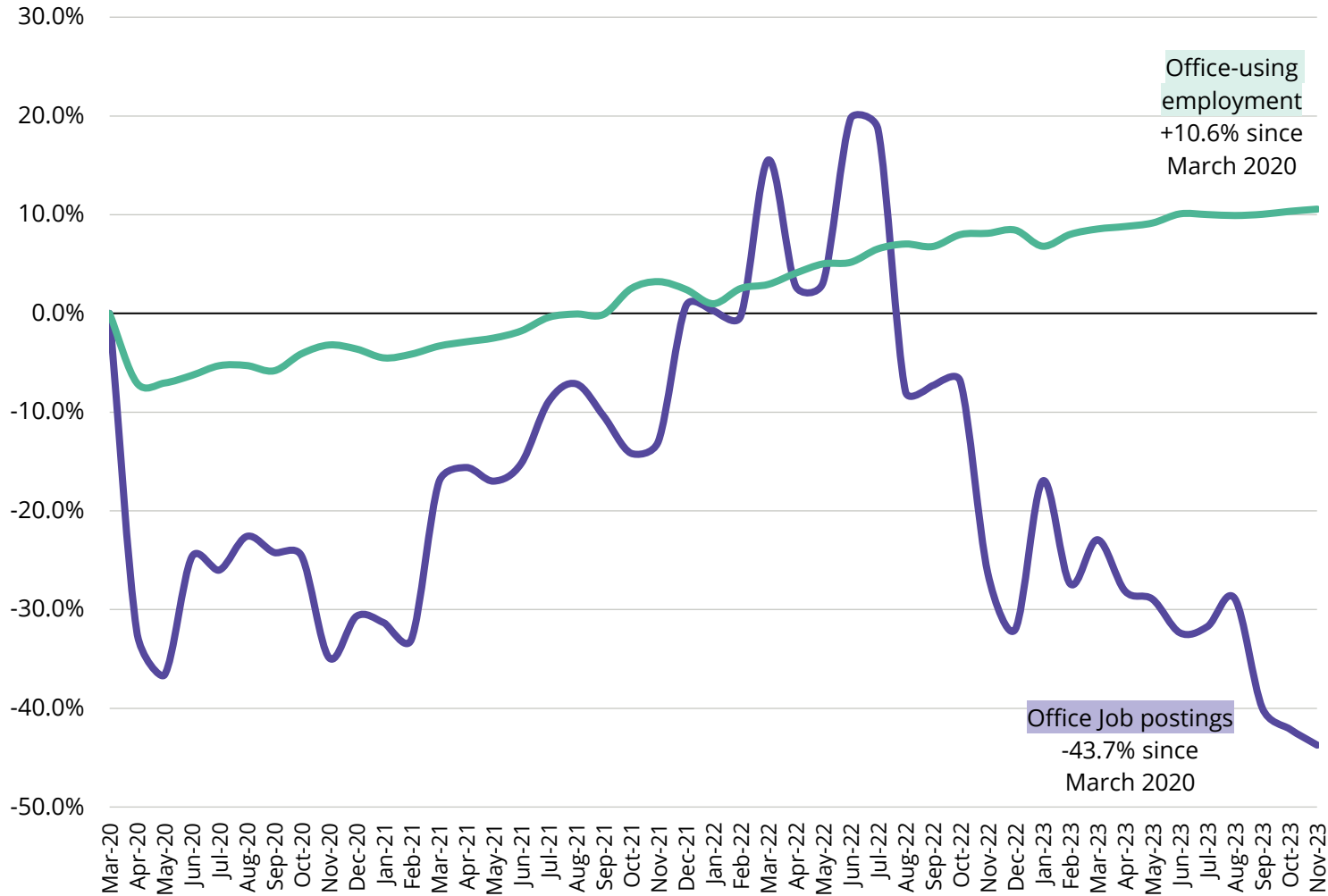
Houston office-using job gains

Houston Metropolitan statistical area
February 2020 to November 2023



Strong office job growth has helped buoy the market, with 70k jobs gained since its pre-pandemic peak, but a disconnect has emerged between office job growth and office demand.

Office-using employment up, postings down



Office-using employment has rebounded, reaching a historic peak with a 10.6% surge since March 2020. In contrast, office job postings have significantly declined by 43.7% over the same period.

Source: AVANT by Avison Young

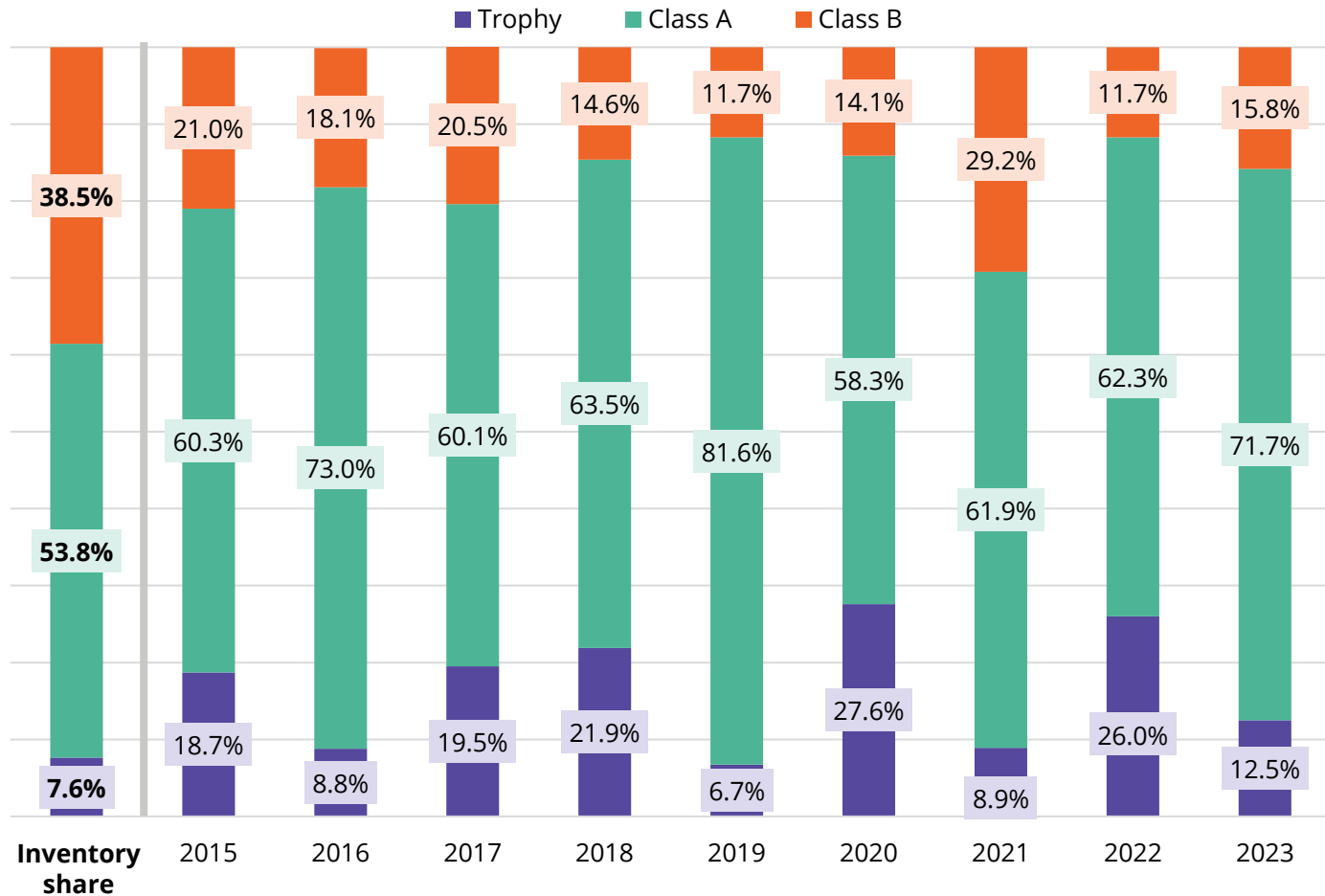
Note: information, financial, and profession business sectors are included in office-using employment and job postings

Occupier market conditions

Let's examine more prevailing office trends

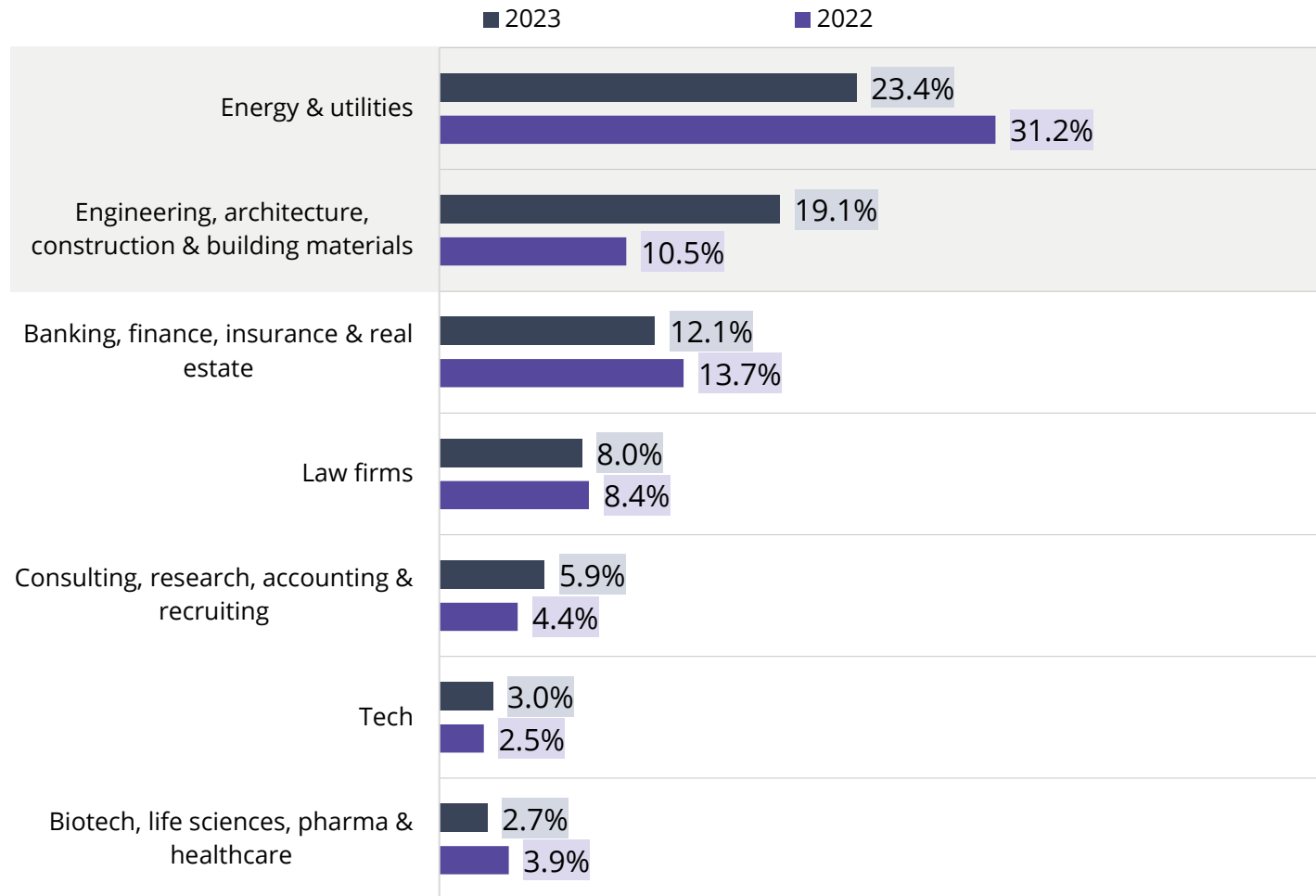


Leasing activity by asset class



Trophy and class A assets continue to outperform the broader market, accounting for 83% of leasing activity since 2015 while making up 62% of the inventory.

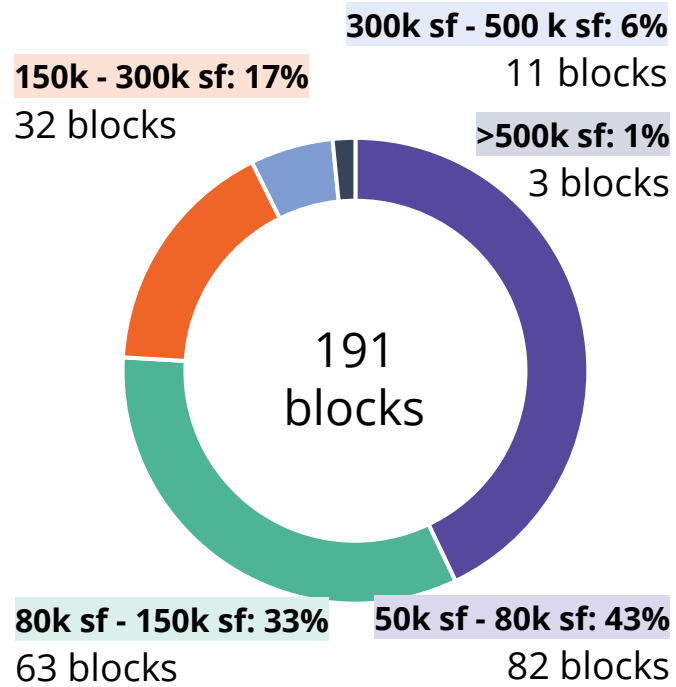
Leasing activity by industry sector



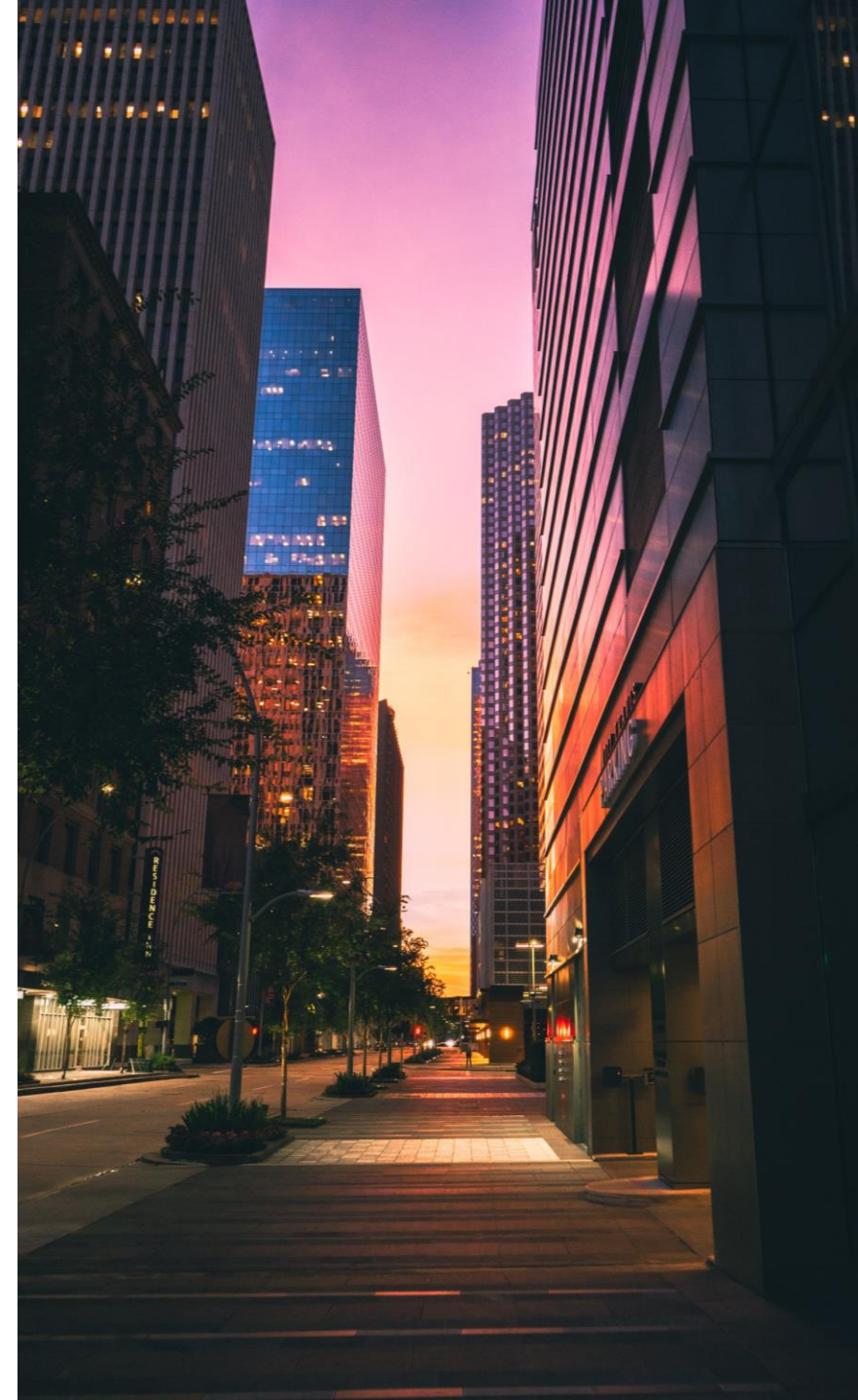
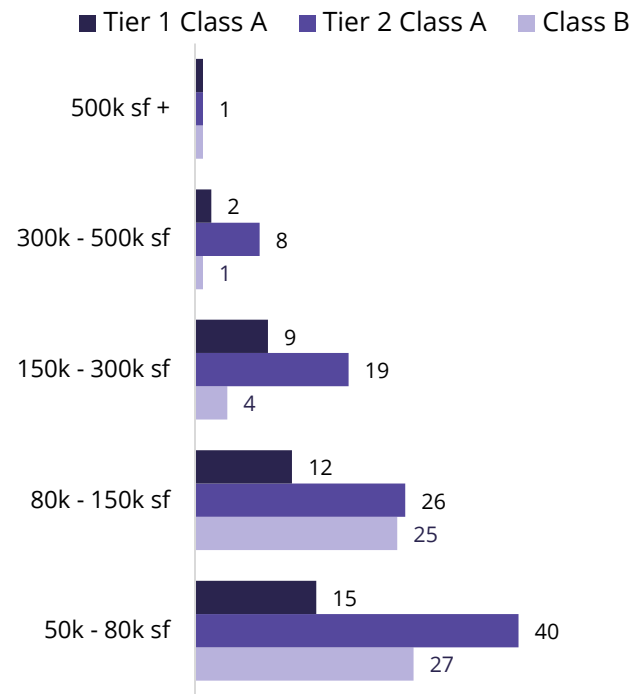
Engineering and energy-related firms have remained active primarily in West Houston with numerous large leases signed over the past two years.

Houston office large block availability

Number of blocks by size



Blocks by quality of building



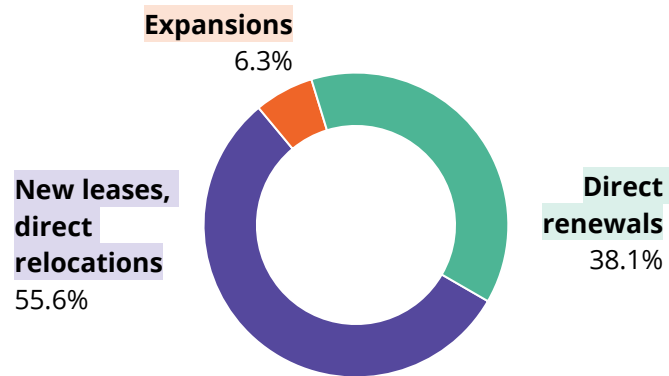
Transaction activity by lease type

31.8%

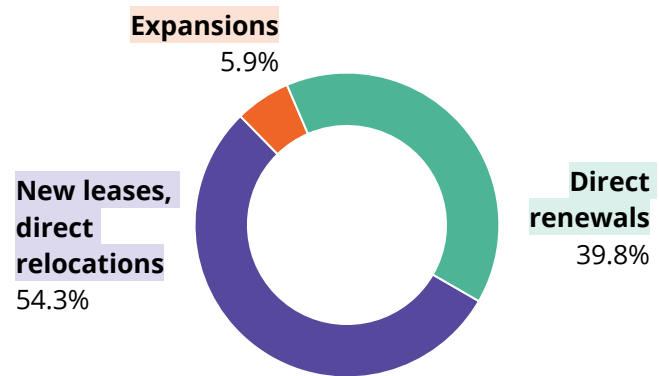
Percent increase in new deals as a share of total leasing activity, 2023 vs. pre-COVID

The distribution of transaction activity has shifted, with new deals and direct relocations accounting for 73.3% of the annual transactions above 10,000 sf compared to 55.6% from 2018 to March 2020.

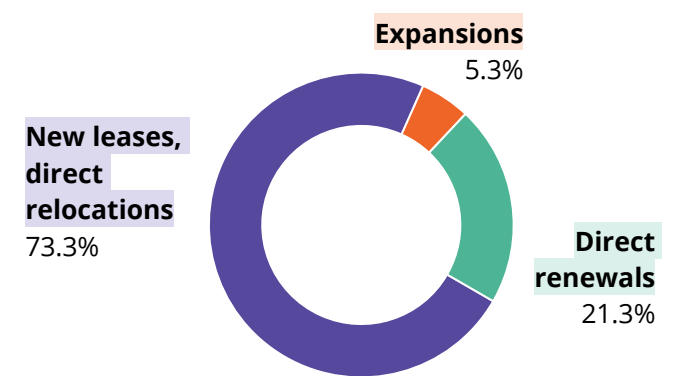
Pre-COVID From 2018 to March 2020



Post COVID April 2020 to Present



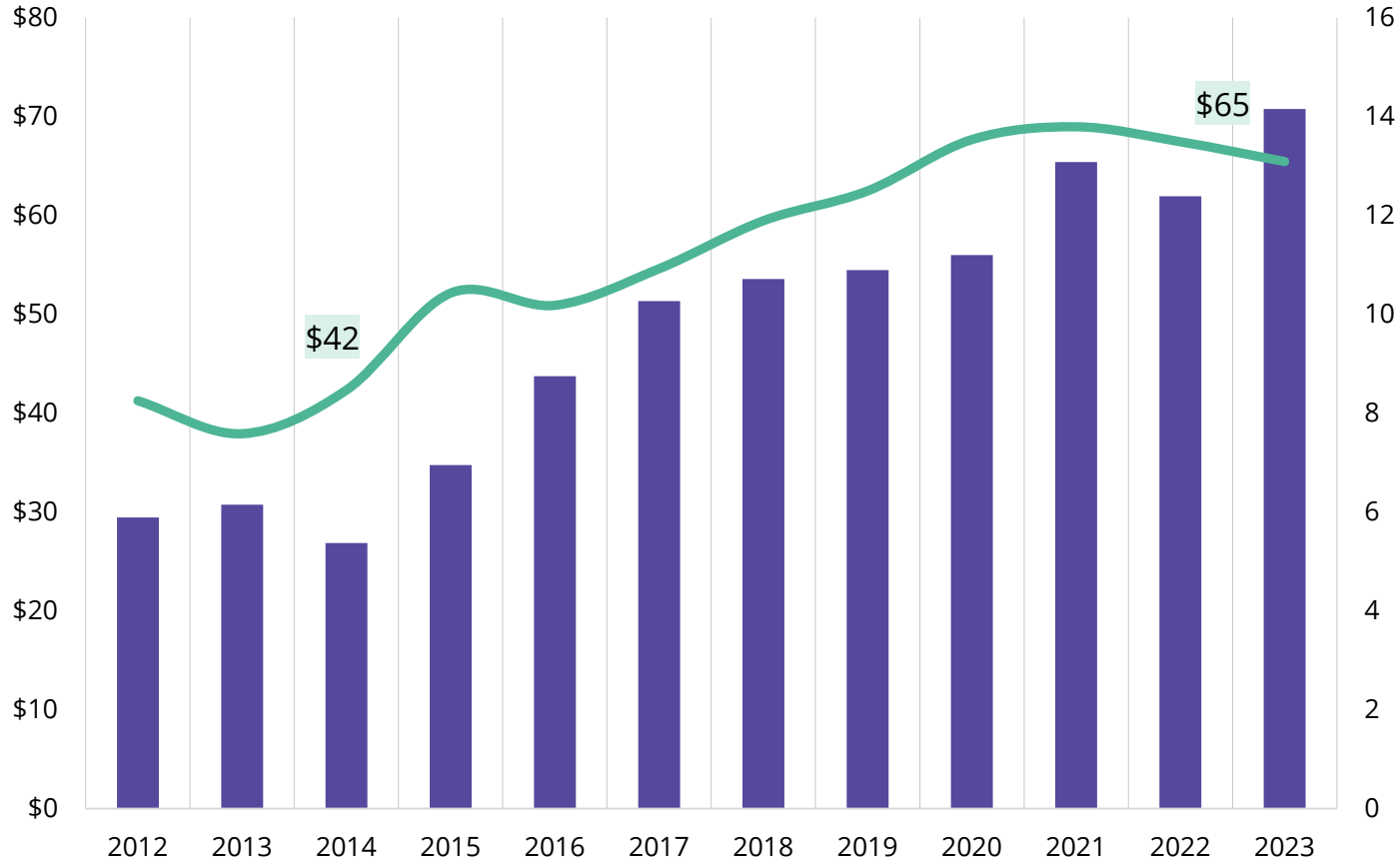
2023



Class A office concessionary trends

Tenant allowance psf

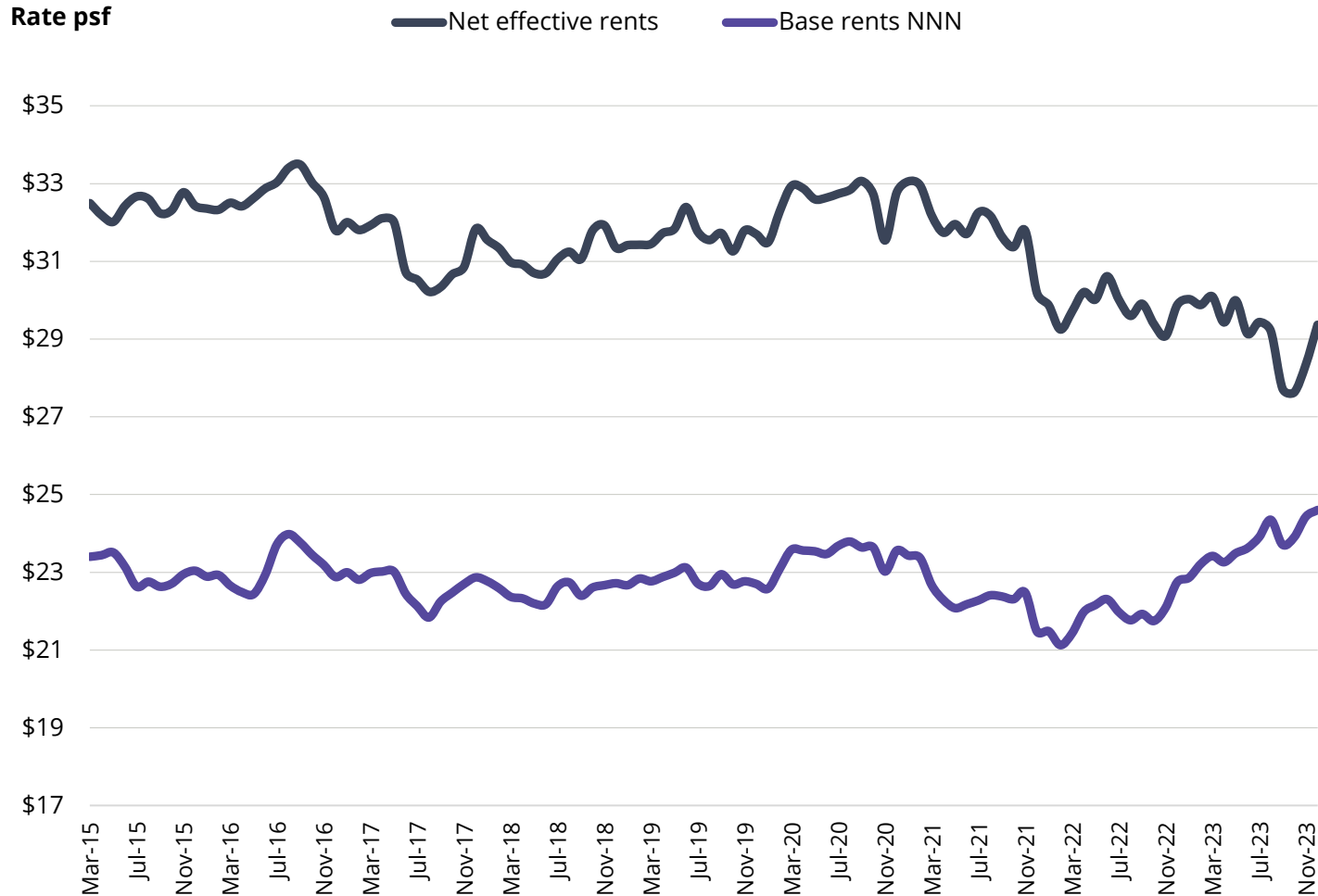
of months rent free



Class A tenant improvement allowances and average free rent reached record highs following the 2015-16 oil bust and COVID pandemic and remain elevated to entice tenants.

Source: AVANT by Avison Young
Note: Concessions inclusive of only new direct leases & expansions greater than 10k sf, concessions normalized for a 10-year term

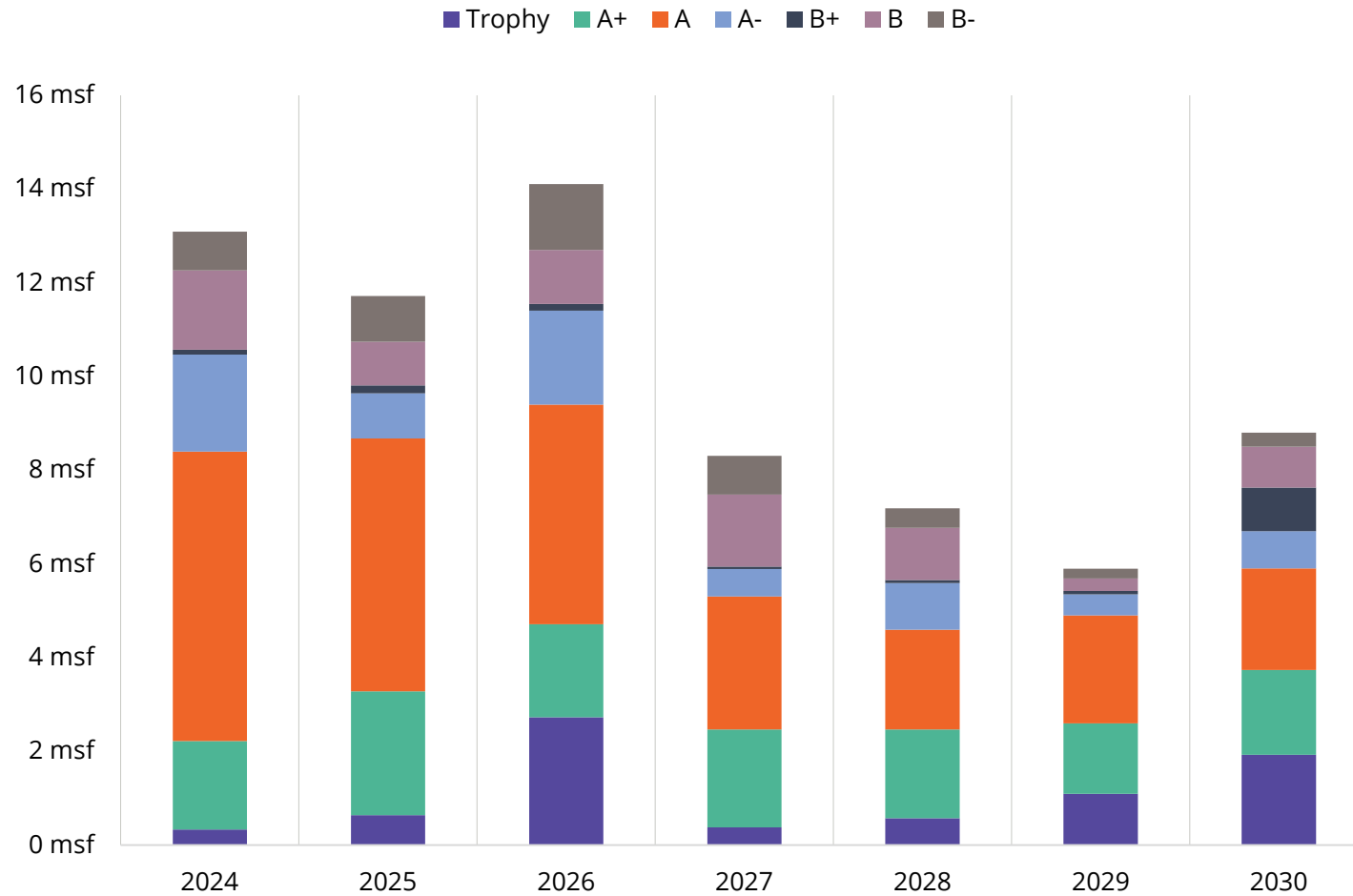
Trophy & Class A net effective vs. base rents



Highly competitive concession packages with generous rental abatement and TI allowances have resulted in lower net effective rents.

Source: AVANT by Avison Young
Note: Concessions inclusive of only new direct leases & expansions greater than 10k sf, concessions normalized for a 10-year term

Houston office lease expirations

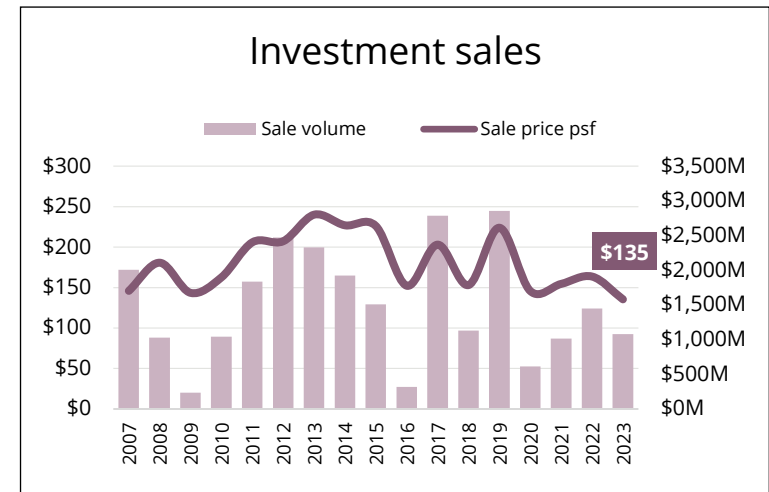
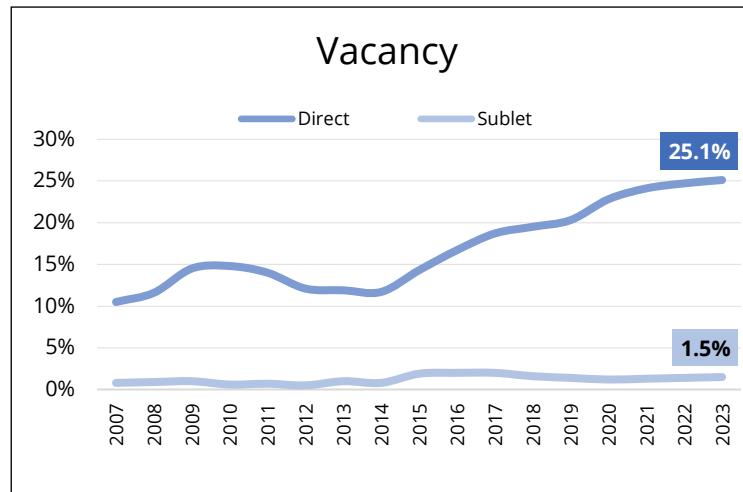
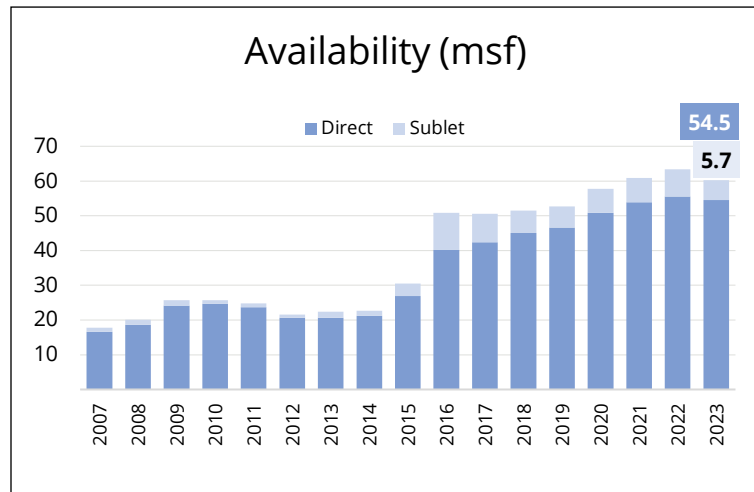
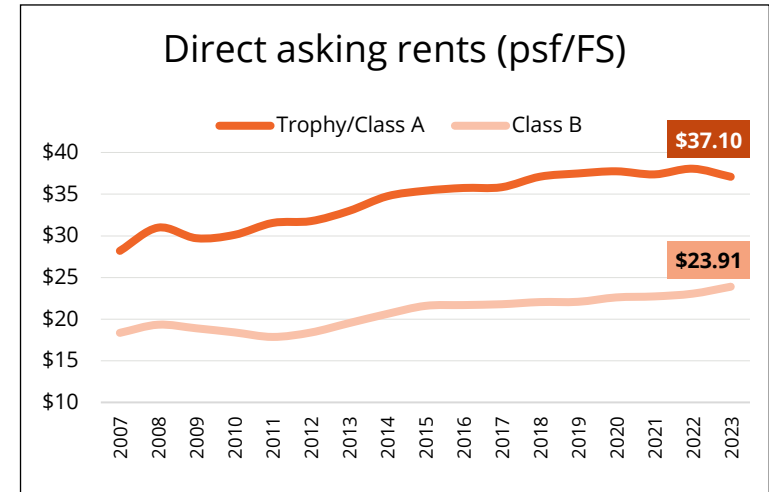
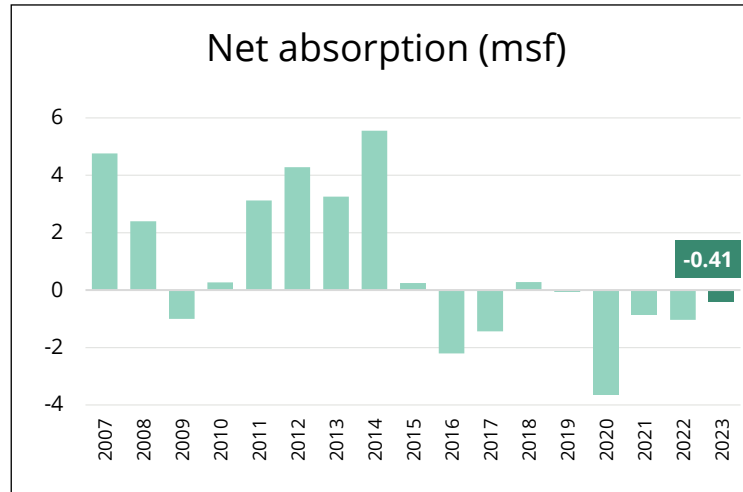
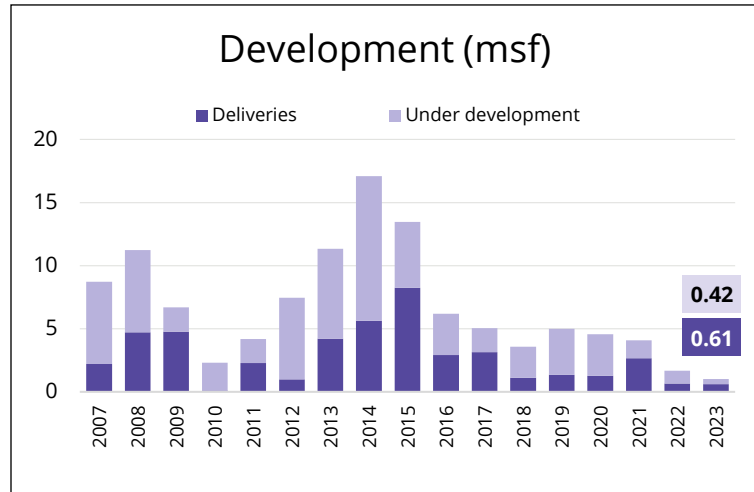


The office sector has over 12 msf of expiring leases per year through 2026, which will likely result in the supply of high-quality space options being constrained if the flight to quality trend continues.

Appendix



Houston office market indicators



Houston office market activity

Recent leasing activity

Tenant	Address	Submarket	Sign date	Size (sf)	Transaction type	Lease type
Seadrill	11025 Equity Drive	West Belt/249	December 2023	57,870	Extension	Direct
CBRE Loan Services	15377 Memorial Drive	Energy Corridor / Katy Freeway West	November 2023	57,200	New	Direct
Lockwood Andrews & Newman	3700 W Sam Houston Pkwy S	Westchase	December 2023	42,098	New	Direct
Southwest Water Company	2150 Town Square Place	E Fort Bend Co/Sugar Land	November 2023	41,114	New	Sublease
Stephens	9 Greenway Plaza	Greenway Plaza	November 2023	35,454	Renewal	Direct
Axens North America	1800 St James Place	Galleria/West Loop	November 2023	32,674	Renewal	Direct
Keystone Holdings	10900 Corporate Centre Drive	West Belt/249	October 2023	31,709	New	Direct
Taylor Morrison	3250 Briarpark Drive	Westchase	October 2023	29,078	New	Direct
Percheron Holdings	1904 Grand Pkwy N	Katy/Grand Parkway West	December 2023	28,597	Renewal	Direct
Pillsbury	609 Main Street	CBD	December 2023	28,337	New	Direct

Top projects under development

Address	Submarket	Delivery date	Building size sf	% Preleased	Developer
1550 Lamar St	CBD	January 2024	386,323	35.0%	Skanska

Houston office market stats

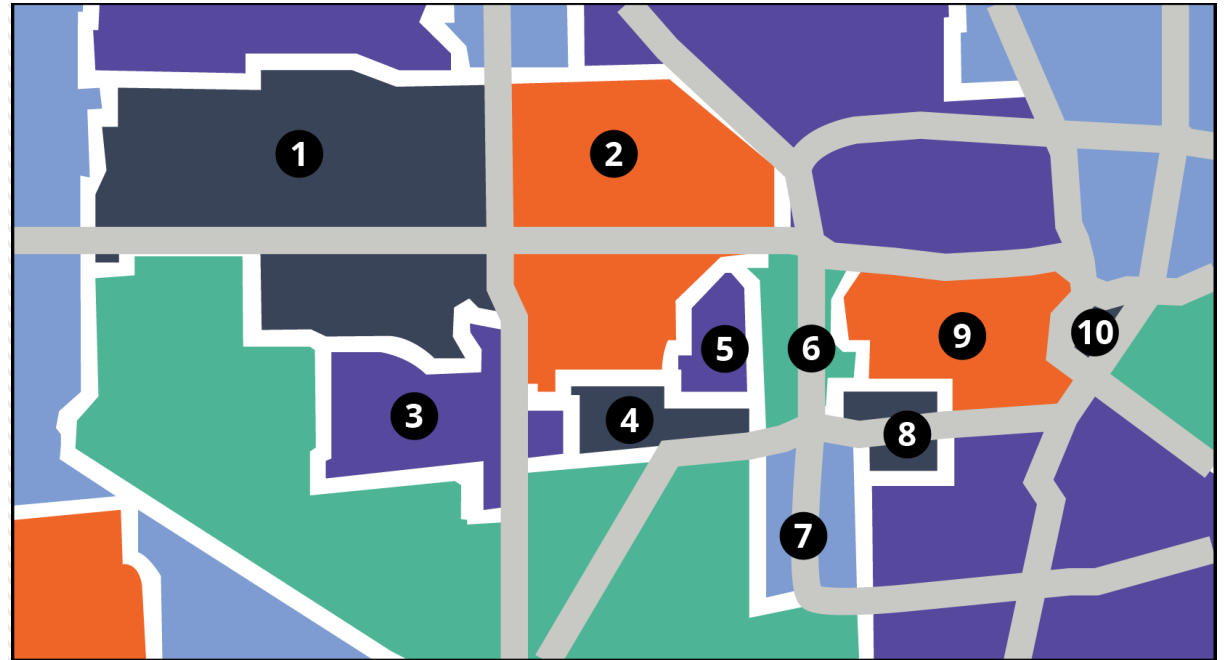
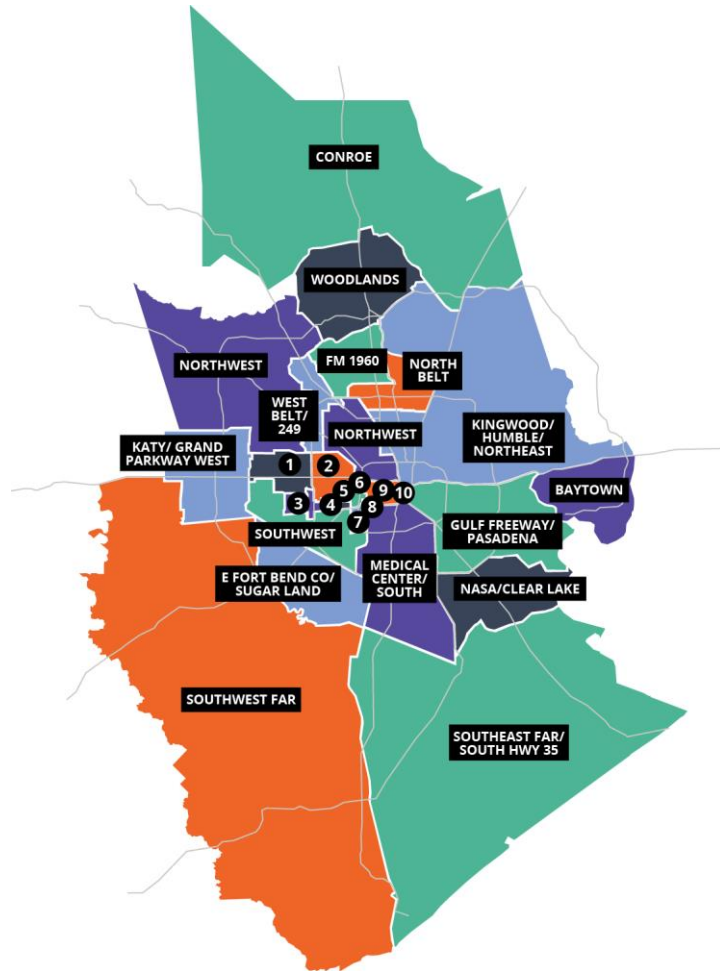
	Existing inventory sf	Deliveries sf (YTD)	Under development sf	Direct vacancy	Sublet vacancy	Total vacancy	Sublet availability sf	Net absorption sf (Q4 2023)	Net absorption sf (YTD)	Annual direct asking rent psf FS
Central Business District	39,873,537	-	386,323	26.4%	1.7%	28.1%	1,329,240	(16,108)	(60,300)	\$42.12
Galleria/West Loop	24,050,998	-	-	28.4%	1.6%	30.0%	567,926	(64,263)	(192,804)	\$35.46
Greenway Plaza	10,717,724	-	-	22.3%	0.3%	22.6%	136,773	35,631	155,026	\$35.81
Energy Corridor/Katy Freeway West	20,558,023	-	-	27.1%	0.8%	27.9%	918,018	336,256	225,328	\$27.87
Katy Freeway East/Memorial City	7,451,044	355,694	-	11.4%	1.2%	12.6%	122,037	20,301	161,117	\$32.88
Westchase	14,903,637	-	-	29.4%	2.9%	32.3%	645,593	383,010	158,718	\$28.76
North Belt	9,816,148	-	-	47.0%	0.4%	47.4%	72,759	76,621	153,480	\$20.52
Northwest	8,208,721	-	-	18.4%	1.2%	19.6%	147,301	(55,099)	(89,765)	\$21.01
NASA/Clear Lake	4,033,309	-	-	11.5%	2.0%	13.6%	131,735	(30,976)	(32,235)	\$26.43
E Fort Bend Co/Sugar Land	5,665,086	-	-	21.1%	1.2%	22.3%	68,134	12,854	24,844	\$30.36
Richmond/Fountainview	1,200,647	-	-	21.9%	0.0%	21.9%	-	(5,629)	(25,387)	\$18.30
San Felipe/Voss	5,284,652	-	-	30.8%	0.3%	31.1%	55,777	2,022	(124,315)	\$30.85
Bellaire	2,686,492	-	-	15.3%	1.2%	16.5%	75,404	(11,209)	(16,411)	\$26.40
Midtown	5,854,342	-	-	15.1%	1.7%	16.8%	138,576	23,857	(56,421)	\$34.15
FM 1960	2,727,240	-	-	27.6%	0.3%	27.8%	9,963	(49,550)	(159,680)	\$17.61
Kingwood/Humble/Northeast	1,170,336	-	-	17.1%	0.0%	17.1%	-	(127)	55,358	\$21.14
Southwest	7,342,935	-	-	23.4%	2.8%	26.2%	202,398	(117,190)	(528,940)	\$21.15
Medical Center/South	1,619,067	-	-	15.5%	0.0%	15.5%	-	(12,879)	(8,541)	\$19.71
The Woodlands	11,829,986	-	-	16.6%	2.7%	19.3%	546,996	(64,001)	122,710	\$36.90
Gulf Freeway/Pasadena	2,426,696	175,000	-	21.9%	1.7%	23.6%	40,676	(14,796)	(30,867)	\$25.69
Katy/Grand Parkway West	2,549,480	-	-	11.0%	2.7%	13.7%	170,138	11,398	26,292	\$33.42
West Belt /249	9,238,540	-	-	34.8%	1.5%	36.4%	338,857	(100,612)	(192,888)	\$23.97
Southwest Far	1,168,910	80,000	32,200	7.7%	0.0%	7.7%	-	4,850	24,230	\$25.09
Southeast Far/South Hwy 35	825,685	-	-	1.4%	0.0%	1.4%	-	(1,069)	(11,318)	-
Conroe	574,150	-	-	21.1%	0.0%	21.1%	-	(1,708)	12,919	\$35.12
Market total	201,777,385	610,694	418,523	25.1%	1.5%	26.6%	5,718,301	361,584	(409,850)	\$32.01

Houston office market stats by class

	Existing inventory sf	Deliveries sf (YTD)	Under development sf	Direct vacancy	Sublet vacancy	Total vacancy	Net absorption sf (Q4 2023)	Net absorption sf (YTD)	Annual direct asking rent psf FS
Trophy	15,383,842	-	386,323	15.2%	3.3%	18.5%	340,035	153,284	\$55.95
Class A	108,643,970	610,694	32,200	26.0%	1.7%	27.7%	73,978	517,687	\$35.79
Class B	77,749,573	-	-	25.8%	0.9%	26.6%	(52,429)	(1,080,821)	\$23.91
Market total	201,777,385	610,694	418,523	25.1%	1.5%	26.6%	361,584	(409,850)	\$32.01



Houston submarket map



Map Key

- | | |
|-------------------------------------|----------------------|
| 1 Energy Corridor/Katy Freeway West | 6 Galleria/West Loop |
| 2 Katy Freeway East/Memorial City | 7 Bellaire |
| 3 Westchase | 8 Greenway Plaza |
| 4 Richmond/Fountainview | 9 Midtown |
| 5 San Felipe/Voss | 10 CBD |

Office insights glossary of terms

Demand

- **Leasing activity:** total square footage of relocations, renewals, expansions and subleases expressed when the leases are signed, not when tenants take physical occupancy of the space
- **Absorption:** period-over-period change in occupied square footage

Supply

- **Direct vacancy rate:** space operated by landlords that is ready for immediate occupancy
- **Sublease vacancy rate:** space operated by sublandlords that is ready for immediate occupancy
- **Total vacancy rate:** sum of direct vacancy rate and sublease vacancy rate
- **Availability rate:** space that is vacant plus space that will become vacant over an indefinite time horizon, including spaces that are occupied by vacating tenants and under-construction properties

Office rents and concessions

- **Asking rents:** pricing guidance provided by landlords to tenants for available space expressed as full service (FS)
- **Base rents:** fair market value of market-level lease pricing based on representative executed leases, expressed as full service (FS)
- **Free rent period:** months of free rent that are typically provided upfront by landlords to tenants as a concession to offset the total cost of a lease and/or the construction timeline of an office suite
- **Tenant improvement allowance:** an allowance expressed in dollars per square foot provided from landlords to tenants to offset build-out, engineering, space planning and related permit costs
- **Net effective rent:** base rents discounted by the dollar values of tenant improvement allowance and free rent concessions expressed as full service (FS)

Capital markets

- **Investment volume:** office sales dollars expressed when the transactions close and based on inventory thresholds; partial-interest sale dollar amounts are not grossed-up to reflect the 100% value of the sale
- **Asset pricing:** unweighted average per-square-foot asset pricing of market-level closed sales
- **Cap rate:** net operating income divided by sale price; this measurement of market-level investment returns is calculated as an unweighted average based on closed investment sales

For more market insights and
information visit **avisonyoung.com**

Wade Bowlin

Principal
Managing Director
wade.bowlin@avisonyoung.com

Anthony Squillante

Principal
Occupier Solutions
anthony.squillante@avisonyoung.com

Darrell L. Betts, CCIM

Principal
Capital Markets
darrell.betts@avisonyoung.com

Ariel Guerrero

Regional Manager, Texas & Denver
Market Intelligence
ariel.guerrero@avisonyoung.com

Carol JeanLouis

Analyst
Market Intelligence
carol.jeanlouis@avisonyoung.com