

HOUSTON
**OFFICE MARKET
REPORT**

First Quarter 2019



BELVOIR

REAL ESTATE GROUP, LLC

Going Places

BROKERAGE / DEVELOPMENT / MANAGEMENT / INVESTMENT

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A Message from Matthew Goldsby, Belvoir Managing Director

Based on the data for Q1 2019, we expect to see Houston's market to continue to improve during 2019. The recent trend of positive net absorption continued, and the vacancy rate fell again. While rents were flat, they remain improved over the period during Houston's oil slump. CRE activity highlights included the announcements of TransOcean's leasing 300K SF at Enclave Place; OXY's pending move to its new corporate headquarters (the 1.4 Mil SF campus purchased from ConocoPhillips); and McDermott taking the entirety of the 524,323 SF Energy Five building, all positive signs for the Energy Corridor/Katy West submarket.

EXECUTIVE SUMMARY

The Houston Office market ended the first quarter 2019 with a vacancy rate of 16.3%. The vacancy rate was down over the previous quarter, with net absorption totaling positive 2,637,493 square feet in the first quarter. Rental rates ended the first quarter at \$28.00, which represents flat rent growth over the past 12 months. 62 properties totaling 3,448,637 square feet were under construction at the end of the quarter, with 45.4% of that pre-leased.



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OFFICE MARKET SNAPSHOT

LEASING

Houston's office vacancy rate of 16% was the highest among large metros as of 19Q1. However, the booming Dallas-Fort Worth metro was not far behind, with 15% vacancy as of 19Q1. This suggests a high rate of structural obsolescence in both markets. A significant amount of new inventory delivered in both metros during the early 1980s, right into the oil bust and savings and loan crisis of that decade. As much as one-third of Houston's office stock was built during these years. Even though both economies have diversified substantially since that time, tenants last cycle indicated a strong preference for 4 & 5 Star product, often at the expense of 1980s product unable to compete.

RENT

Houston's average rental rate of \$28.00/SF is similar to that of Chicago's, narrowly placing in the top 25 most expensive U.S. metros as of 19Q1. The local office market experienced flat rent growth over the past 12 months, while tenants continued to work through the recent supply wave. A significant sublease space overhang and a persistently high vacancy rate continue to place pressure on landlords to offer free rent and concessions. However, even flat rent growth is a welcome change from -6% rent growth experienced at the bottom of the oil downturn in 2016.

CONSTRUCTION

The pipeline of new construction is down significantly, to 3,400,000 SF from a peak of nearly 20 million SF in 14Q2. The development cycle looks like it may be nearing bottom, although Houston could see a slight uptick in new projects announced in the near future as firms continue to seek flight-to-quality and space efficiencies.

INVENTORY

Total office inventory in the Houston market area amounted to 328,175,609 square feet in 9,462 buildings as of the end of the fourth quarter 2018. The Class-A office sector consisted of 146,022,400 square feet in 529 projects. There were 4,080 Class-B buildings totaling 138,687,596 square feet, and the Class-C sector consisted of 43,465,613 square feet in 4,853 buildings. Within the Office market there were 671 owner-occupied buildings accounting for 43,785,663 square feet of office space.

SALES

Houston's office transaction volume in 2018 was down nearly 42% from the prior year, although it amounted to a strong \$1.8 billion in trades. This is not surprising, given the number of large portfolio trades that occurred in 2017, including Parkway's recapitalization of Greenway Plaza, CPPIB's acquisition of Parkway, and Brookfield's acquisition of Houston Center.

Among notable trades, Chicago-based LaSalle Investment Management acquired the 5 Star, 30-story, 510,300-SF Memorial Hermann Medical Plaza in the Texas Medical Center from locally based Mischer Investments in July 2018. The building sold at a 4.67% cap rate for approximately \$405 million (\$794/SF), making it the most expensive medical office sale in U.S. history.

Source: CoStar Property®

SUBMARKET STATISTICS

Q1 2019

Market	Existing Inventory		Vacancy		YTD Net Absorption	YTD Deliveries	Under Const SF	Rent Per SF
	Bldgs	SF (000)	SF	Percent				
Austin County	44	263	7,414	2.8%	566	0	-	\$23.66
Baytown	138	1,659	104,841	6.3%	15,066	5	-	\$20.74
Bellaire	91	5,108	774,633	15.2%	(34,037)	0	5	\$25.16
CBD	160	50,642	9,301,141	18.4%	454,508	0	1,887	\$35.97
Conroe	261	2,696	274,977	10.2%	66,397	66	3	\$22.52
E Fort Bend Co/Sugar Land	412	10,054	1,086,601	10.8%	120,543	131	110	\$26.73
FM 1960/Champions	255	4,362	575,126	13.2%	62,512	30	-	\$19.05
FM 1960/Hwy 249	423	8,570	942,214	11.0%	(42,829)	73	290	\$25.26
FM 1960/I-45 North	111	2,538	553,536	21.8%	100,202	0	-	\$20.52
Galleria/Uptown	66	16,856	2,591,546	15.4%	258,244	0	-	\$31.92
Greenspoint/IAH	56	3,138	730,728	23.3%	(31,045)	0	-	\$19.46
Greenspoint/N Belt W.	119	11,061	4,955,138	44.8%	(223,479)	0	-	\$18.56
Greenway Plaza	279	13,115	1,816,756	13.9%	27,153	0	-	\$30.07
Gulf Freeway/Pasadena	641	8,112	779,471	9.6%	204,539	101	-	\$21.80
I-10 East	133	1,368	86,830	6.3%	61,105	1	-	\$20.61
Katy Freeway East	260	11,603	1,245,076	10.7%	136,027	0	102	\$30.42
Katy Freeway West	261	28,455	6,958,689	24.5%	342,083	6	124	\$30.18
Katy/Grand Parkway W.	440	6,238	646,214	10.4%	242,664	124	-	\$27.99
Kingwood/Humble	229	3,517	379,154	10.8%	24,941	108	17	\$23.87
Liberty County	71	349	13,349	3.8%	(5,551)	0	-	\$22.22
Midtown	561	9,603	905,838	9.4%	(15,371)	26	165	\$29.25
NASA/Clear Lake	527	10,335	1,543,702	14.9%	508	47	52	\$23.87
North Loop West	350	6,233	1,072,725	17.2%	(99,958)	45	-	\$23.04
Northeast Near	150	2,264	120,449	5.3%	11,539	0	-	\$24.17
Northeast Outlier	86	937	43,786	4.7%	19,455	8	-	\$24.19
Northwest Far	130	4,399	853,396	19.4%	58,204	0	-	\$19.67
Northwest Near	54	1,454	168,426	11.6%	(64,437)	0	-	\$19.67
Northwest Outlier	259	1,813	246,917	13.6%	52,759	53	36	\$25.19
Outlying Chambers Co.	21	73	-	-	60	0	7	\$23.53
Outlying Montgomery Co.	201	1,422	180,277	12.7%	30,838	45	5	\$22.65
Outlying Waller Co.	23	120	2,200	1.8%	262	0	-	\$22.37
Post Oak Park	43	4,681	1,122,534	24.0%	8,072	0	207	\$31.02
Richmond/Fountainview	118	2,248	179,545	8.0%	17,851	0	5	\$20.76
Riverway	24	3,091	546,910	17.7%	31,235	0	-	\$28.01
San Felipe/Voss	50	5,343	1,096,560	20.5%	(39,951)	0	-	\$26.60
South	267	3,255	308,855	9.5%	(15,199)	63	103	\$26.73

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Source: CoStar Property®

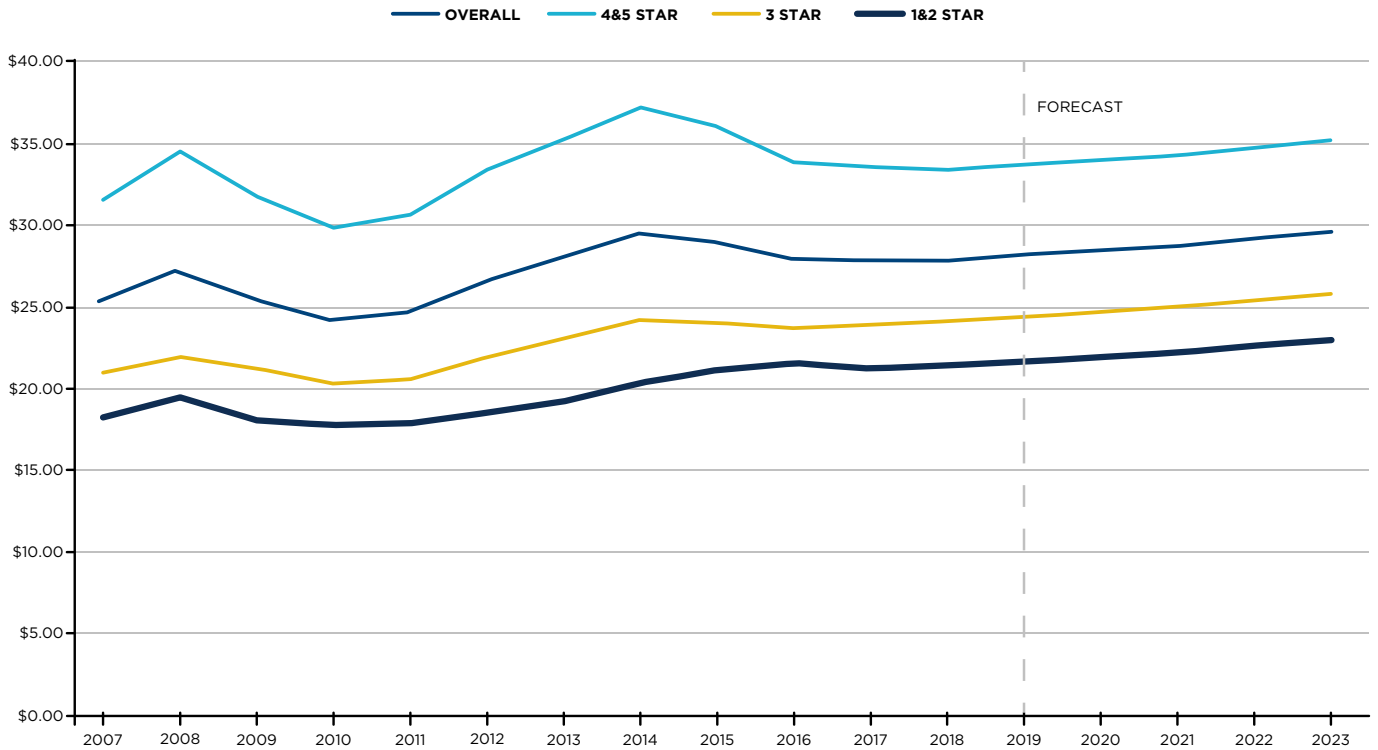
SUBMARKET STATISTICS

Q1 2019

Market	Existing Inventory		Vacancy		YTD Net Absorption	YTD Deliveries	Under Const SF	Rent Per SF
	Bldgs	SF (000)	SF	Percent				
South Hwy 35	155	842	33,294	4.0%	18,511	15	-	\$21.13
South Main/Medical Center	241	13,526	654,607	4.8%	(113,169)	0	-	\$27.28
Southeast Outlier	349	4,095	326,493	8.0%	75,396	0	22	\$22.55
Southwest Beltway 8	190	7,456	1,279,660	17.2%	(90,843)	0	-	\$18.53
Southwest Far	91	1,453	97,861	6.7%	177,580	0	-	\$24.38
Southwest Outlier	210	1,764	223,253	12.7%	7,514	6	30	\$23.34
Southwest/Hillcroft	107	5,274	942,484	17.9%	82,632	0	-	\$17.51
The Woodlands	639	22,579	2,056,935	9.1%	848,250	810	273	\$31.93
West Belt	110	6,269	1,385,645	22.1%	119,319	17	-	\$28.19
Westchase	137	18,892	4,345,162	23.0%	(263,173)	21	-	\$26.40

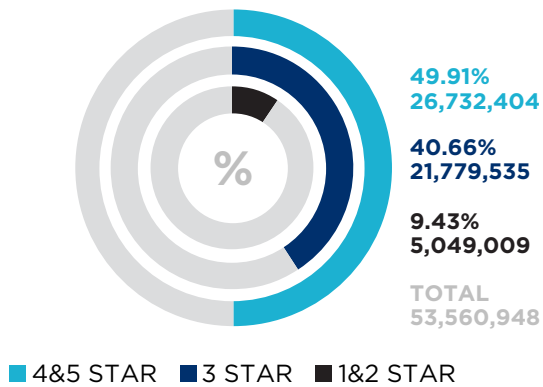
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HISTORICAL AND FORECAST RENTAL RATES BY CLASS



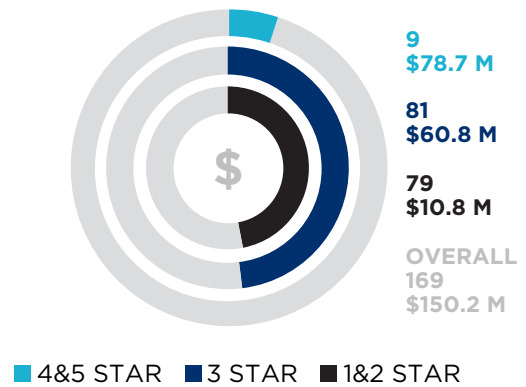
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VACANCY BY CLASS



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SALES BY CLASS



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