HOUSTON

OFFICE MARKET REPORT

Second Quarter 2020

BELVOIR

REAL ESTATE GROUP, LLC

Going Places

BROKERAGE / DEVELOPMENT / MANAGEMENT / INVESTMENT

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A Message from Matthew Goldsby, Belvoir Managing Director

The office market has been significantly impacted by low oil prices brought on by a combination of low oil demand from the coronavirus pandemic and OPEC production policies that remain less concerned with supporting prices. Houston's overall office vacancy rate is currently 17.3% with a trailing twelve-month negative net absorption rate of 1.1 million SF and flat rent growth.

This year, most of the new leasing activity took place in a handful of buildings located in the CBD, Katy West, Westchase, Greenway Plaza and The Woodlands. In the first quarter, leasing activity (both new leases and renewals) totaled 912,670 SF, with an additional 390,394 SF transacting in the second quarter. This statistic does not include Anadarko's 808,000 SF 13-year renewal which was required for the sale of the property to the Hughes organization, as well as OXY's 876,961 SF 10-year renewal/expansion in Greenway Plaza.

New construction has slowed, although the construction pipeline remains steady at around 5.7 million SF, representing 1.7% of Houston's total office inventory and 60.7% preleased. Only five relatively minor projects broke ground in the second quarter of 2020, totaling an additional 417,661 SF underway.

Over the last 12 months, there have been 664 comparable sales at an average price of $256 per SF on a 7.7% cap. The average vacancy at the time of sale was 16.1%. In 2020, there have been only two sales of 318,529 SF in March. Anadarko's sale-leaseback of their office towers and campus was recorded in the fourth quarter of 2019.

Through the second quarter, most major occupiers guided their staff to work from home if possible, and smaller employers have also followed suit. As an example, Greenway Plaza, where many major tenants are energy companies, is still in "lockdown" mode. Employees can access the building with their security cards, but the campus is otherwise closed to external visitors. In the Galleria, many buildings are open as the tenant base is more diverse, and visitors are permitted access. With the spike in coronavirus cases, the work from home orders from employers are expected to continue into 2021. Optimistic jobs reports indicate that an employment recovery is already underway, although full capacity is not expected to return until mid-2021.

OFFICE MARKET SNAPSHOT

LEASING

The recent oil price crash and coronavirus pandemic pose serious downside risks to Houston's office market. Net absorption amounted to about -990,000 SF last quarter and -1.1 million SF over the past year. Still, leasing activity was relatively robust, as deals in the pipeline closed well into the middle of 2020. Houston already had the highest office vacancy rate in the country, coming out of the 2015 to 2017 oil downturn. In this tenants' market, landlords must offer significant amenities and compete in terms of price.

RENT

Houston office may experience declining rent growth in the coming months, as the market deals with the economic and social fallout stemming from the coronavirus pandemic. Asking rents recently began to recover after a multi-year decline, although that appears to be short-lived considering recent events. Rent growth over the past year was strongest inside the Loop, the area that has seen the most new development and absorption activity. West Houston submarkets located in and near the Energy Corridor recently trailed just slightly behind, a result of resurgent leasing activity in the area in 2019.

CONSTRUCTION

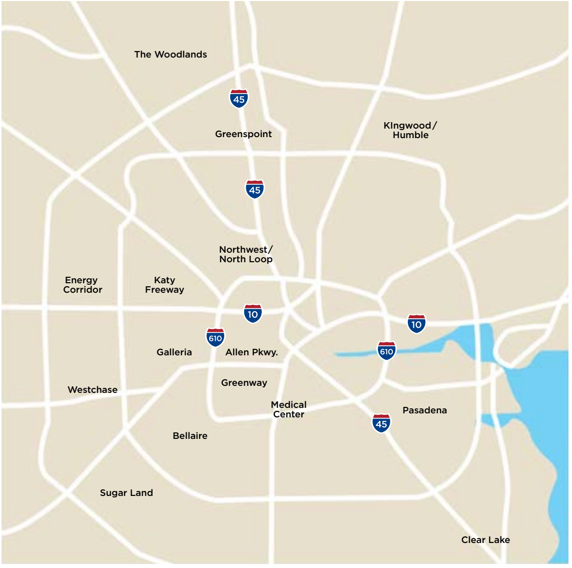
Houston's office supply pipeline was already down significantly since the oil downturn of 2015-2017, as the market worked through significant oversupply, prior to the coronavirus pandemic and recent oil price crash. However, there are still a few new projects underway. Among the largest, Hines is under construction with its 1.1 million SF Texas Tower in downtown Houston, which is set to deliver in 2021. Hines is also developing Marathon Oil's new 440,000 SF headquarters in City Centre, which is expected to deliver by the end of 2021. Property owner Rice University is expected to spend a reported $100 million on the redevelopment of the 270,000 SF former midtown Sears building. Upon completion, it is expected to eventually serve as the de facto innovation tech hub for Houston.

SALES

The current outlook for transaction activity in 2020 was deteriorating rapidly due to the coronavirus pandemic and recent oil price war. And as noted, Houston is in the midst of its second oil downturn in just five years — with oil prices in the $30s/barrel — and the U.S. is in a recession for the first time since 2008, quite possibly the worst since the Great Depression. This is likely to negatively impact transaction activity and the demand for Houston office properties. And this is important because roughly half of Houston's economy is based on the health of the energy sector and the other half on the health of the global and national economies. As with the rest of the country, the coronavirus pandemic has rattled the financial markets and added ambiguity when pricing active transactions.

The most trophy deal to occur so far in 2020 involved Midway Companies' sale of the 250,000 SF office tower at Kirby Grove for $115 million, or $464/SF, to Chicago-based DWS. The sale included a ground lease, which is owned by the Upper Kirby Redevelopment Authority of the City of Houston. The 5-star, LEED-certified building within Midway's Kirby Grove mixed-use development delivered in 2015 and was 96% occupied at the time of sale.

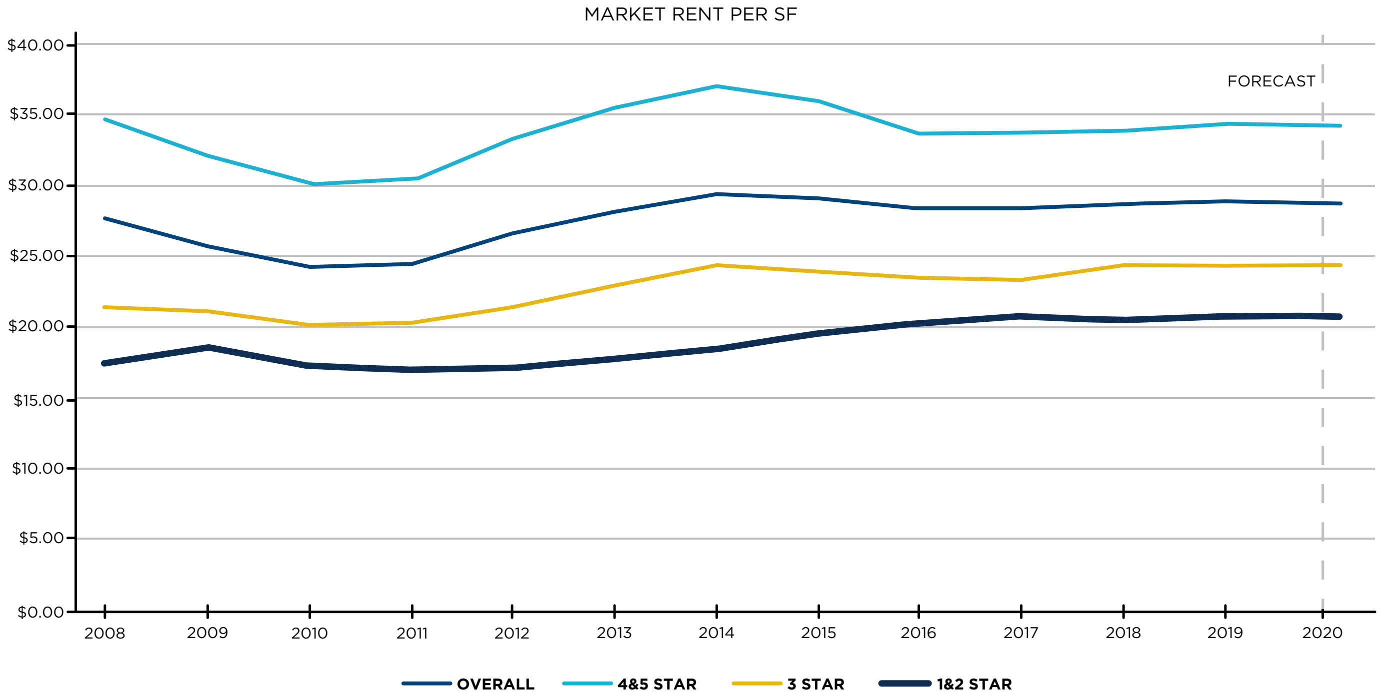
Source: CoStar Property©



Market	Existing Inventory		Vacancy		YTD Net Absorption	YTD Deliveries	Under Const SF (000)	Rent Per SF
	Bldgs	SF (000)	SF	Percent				
Bellaire	92	5,230	785,063	15.0%	(17,797)	1	53	$25.47
CBD	161	51,370	10,431,393	20.3%	(211,026)	1	1,252	$37.26
E Fort Bend Co/Sugar Land	439	10,240	1,212,733	11.8%	36,216	25	109	$26.96
FM 1960/Champions	266	4,426	752,070	17.0%	(43,283)	1	-	$18.80
FM 1960/Hwy 249	475	9,692	1,620,671	16.7%	(61,244)	25	155	$25.17
Galleria/Uptown	66	16,850	2,826,137	16.8%	(220,016)	0	70	$31.24
Greenspoint/N Belt W.	117	10,895	4,908,355	45.0%	98,653	0	-	$18.93
Greenway Plaza	274	12,689	1,910,133	15.1%	(85,289)	0	-	$30.61
Gulf Freeway/Pasadena	662	8,499	1,081,301	12.7%	(28,061)	1	64	$22.32
Katy Freeway East	266	11,857	1,263,479	10.7%	167,053	2	1,200	$31.29
Katy Freeway West	263	27,961	5,916,831	21.2%	943,548	3	-	$30.42
Katy/Grand Parkway W.	474	6,386	806,412	12.6%	(100,239)	11	152	$28.43
Midtown	586	10,041	1,064,334	10.6%	(162,702)	1	528	$30.62
NASA/Clear Lake	539	10,279	1,377,154	13.4%	34,805	4	78	$23.80
North Loop West	367	6,230	1,007,174	16.2%	94,585	1	136	$23.23
Post Oak Park	44	4,541	1,439,896	31.7%	(251,767)	1	-	$31.62
San Felipe/Voss	50	5,346	1,143,541	21.4%	(38,938)	0	-	$26.23
South Main/Medical Center	240	13,067	925,957	7.1%	(174,773)	1	277	$28.39
Southwest Beltway 8	194	7,417	1,385,029	18.7%	19,282	0	-	$17.76
Southwest/Hillcroft	111	5,323	863,471	16.2%	21,626	1	-	$17.26
The Woodlands	671	23,621	2,752,908	11.7%	(544,153)	11	751	$32.05
West Belt	113	6,311	1,465,784	23.2%	(361,837)	0	4	$28.41
Westchase	140	18,926	4,553,810	24.1%	(219,794)	0	-	$27.27

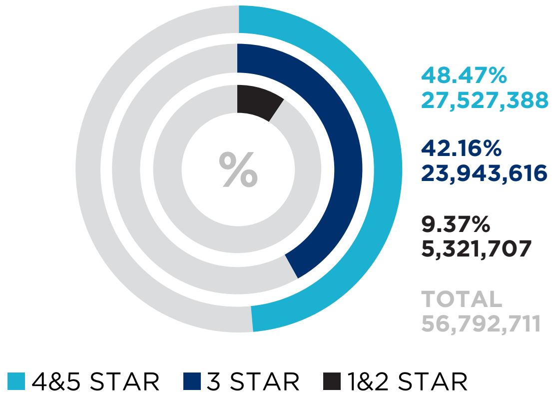
Source: CoStar Property©

HISTORICAL AND FORECAST RENTAL RATES BY CLASS



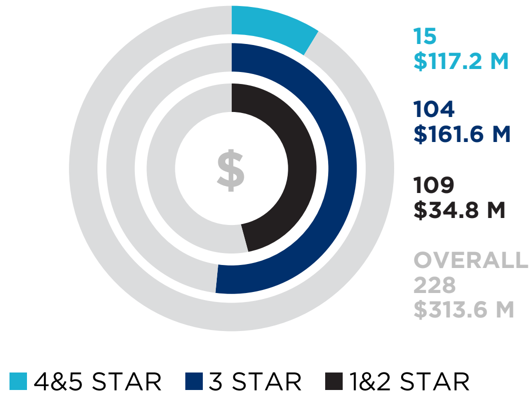
Source: CoStar Property©

VACANCY BY CLASS



Source: CoStar Property©

SALES BY CLASS



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