Fourth Quarter 2019 / Office Research Report

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# MARKETInsights


## Population

Net migration across the United States has increased over recent years, with higher priced coastal markets like San Francisco, Los Angeles and New York City seeing a large exodus of people and jobs to other parts of the country. Texas and Dallas/Fort Worth, in particular, have been one of the primary beneficiaries of this trend. Companies like State Farm, Toyota, McKesson, Charles Schwab, JP Morgan Chase and Liberty Mutual have all either relocated or significantly expanded operations in DFW over the past few years.

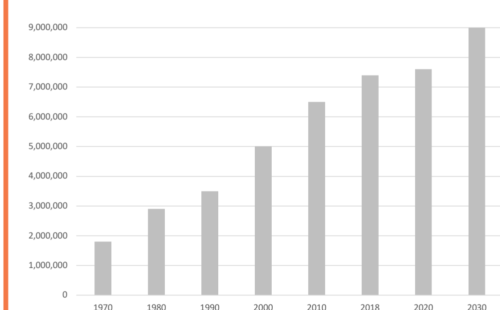
According to the U.S. Census Bureau, the Metroplex is the fourth largest metropolitan statistical area ("MSA") in the United States, with an estimated population of 7.4 million. Since the last census in 2010, the Census Bureau estimates the population of the Dallas-Fort Worth MSA grew by 900,000 or an average of 130,000 people per year. That's a gain of 356 people per day.

The Dallas-Fort Worth-Arlington metropolitan area's 146,000-resident increase over the past year was the most of any metro area in the United States.

The Dallas-Fort Worth-Arlington metropolitan area continued to produce new jobs, creating an estimated 98,700 net new jobs in the 12 months ending October 2019 (the most recent figure available) according to the Bureau of Labor Statistics. This was the highest in the nation, followed by 84,600 for New York City and 80,700 for Los Angeles.

### POPULATION GROWTH

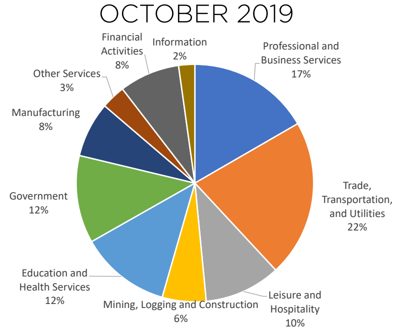
Dallas-Fort Worth-Arlington




Source: North Texas Council of Governments; US Census

### EMPLOYMENT BY INDUSTRY SECTOR

OCTOBER 2019

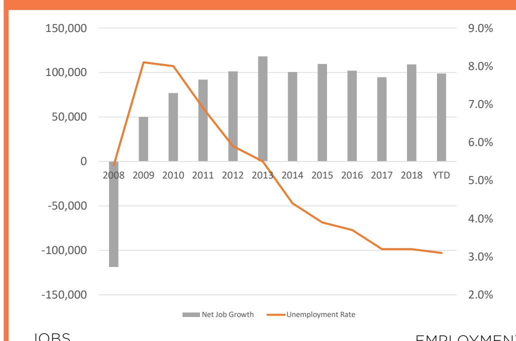



## Employment

For office space demand, employment – especially employment in the "office-using" industry sectors – is a key driver.

According to the Bureau of Labor Statistics, Dallas-Fort Worth was the fourth largest employment market in the nation with total non-farm employment of 4 million as of September 2019. Of this total, almost 27% or 1.1 million jobs were in the office-using sectors of Professional and Business Services, Financial Activities, and Information.

### NET JOB GROWTH VS. UNEMPLOYMENT RATE

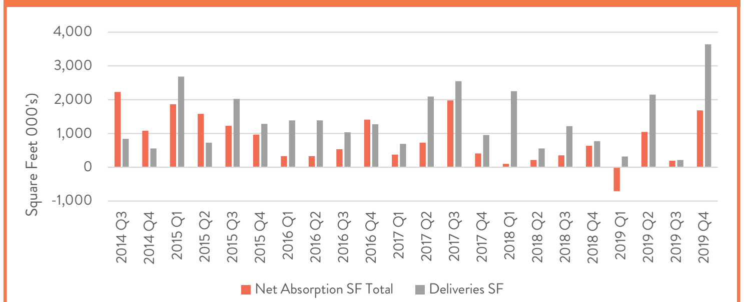



## Demand and Supply

Construction deliveries and demand for space were both high in the fourth quarter of 2019, with about 1.7 million square feet absorbed and 3.6 million square feet completed. For the year as a whole, 2.2 million was absorbed, while 6.3 million square feet was delivered (for the new construction completed in 2019, the total occupancy was an impressive 88%). Notable new construction for the year includes: American Airlines, Pioneer Natural Resources, Charles Schwab, Nokia, USAA, Brinker International and Independent Bank. Also, co-working companies continued to expand rapidly in DFW during the first three quarters of the year, but activity slowed for that sector in the fourth quarter.

Among the property classes, Class A properties absorbed a very strong 1.4 million square feet in the fourth quarter, while Class B was a positive 304,155 square feet and Class C properties lost 19,262 square feet of users.

### NET ABSORPTION & DELIVERIES



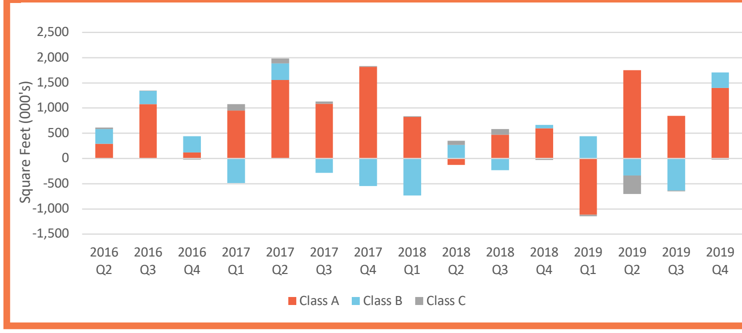

Construction deliveries were very high in the fourth quarter, with American Airlines new headquarter built-to-suit campus being delivered, along with Pioneer Natural Resources and several mid-sized spec projects, like Redbird One and the Offices at the Realm. For the quarter and year as a whole, 3.6 million and 6.3 million square feet were completed, respectively. This level of construction is slightly higher than the most recent five year average of 5.8 million square feet.

As of December 2019, there was a total of 7,561,462 rentable square feet of office space under construction in Dallas-Fort Worth. Of the 7.6 million square feet of construction currently underway, 4.6 million square feet is scheduled for delivery in 2020.

Of the 7.6 million square feet of space currently under construction, 48% percent has been accounted for through a combination of built-to-suits and pre-leasing.

JP Morgan Chase (phase 2), Keurig Dr Pepper new build-to-suit and several spec office construction projects (Headquarters II, Frisco Station, Legacy Town Center) make Far North Dallas currently the most active submarket, with 29% of the construction pipeline. Between multiple Cypress Waters' projects, the USCIS building and Paycom, Las Colinas has the second highest concentration of new construction underway and accounts for 16% of the construction pipeline. There have been several recently announced spec projects that have not yet broken ground but are expected to begin construction some time in 2020 (most of these projects are concentrated in the Legacy area of Far North Dallas and Uptown).

### CLASS NET ABSORPTION




### SF CURRENTLY UNDER CONSTRUCTION

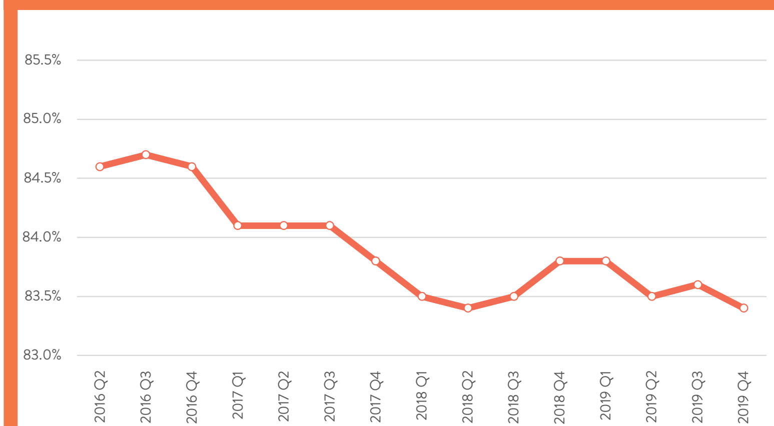

## Occupancy Trends

Absorption was strong in the fourth quarter, but was greatly outpaced by new construction deliveries, pushing down the overall occupancy rate to 83.4%. This has been part of a longer term trend. Over the past five years, 15.3 million square feet has been absorbed while new office construction for that same time period has been almost double that amount at 29.2 million square feet. This dynamic has been in place for a couple of reasons, but one of the primary reasons is developers have not had too much difficulty leasing up new projects. Tenants have a strong preference for newer space, so new construction has been leasing well, with the lower occupancy being felt most acutely in older Class A- and Class B properties. There are several older large office projects that are currently vacant, including the 1.6 million-square-foot former HP headquarters at 5400 Legacy, American Airlines' recently vacated 1.3 million former headquarters campus and Pegasus Place (a 518,656-square-foot property formerly owned and occupied by Exxon Mobile that has been completely vacant since late 2006).

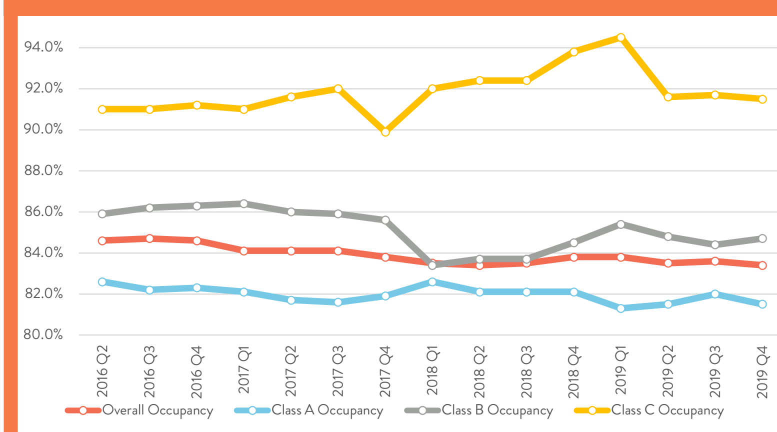

With elevated construction this past year and a robust construction pipeline, the overall occupancy decline is expected to continue for the foreseeable future. This is mainly due to new construction, but also because several office using industries have been squeezing more employees into less space than in the past. With the construction pipeline near 7.6 million square feet and asking rates far above previous cycles, this trend is expected to continue for at least the next two years.

Despite the elevated levels of new construction over the past five years, one of the highest risks in the market is the amount of large blocks of second-generation spaces that will need to be backfilled (many of which were recently vacated for large built-to-suit projects).

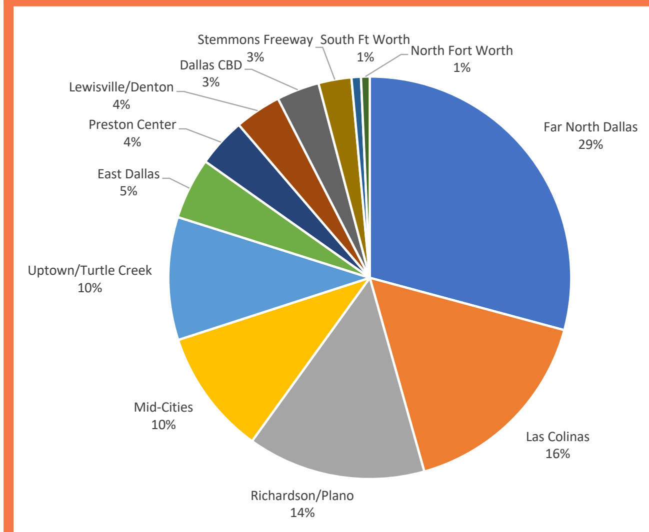
## OCCUPANCY TRENDS



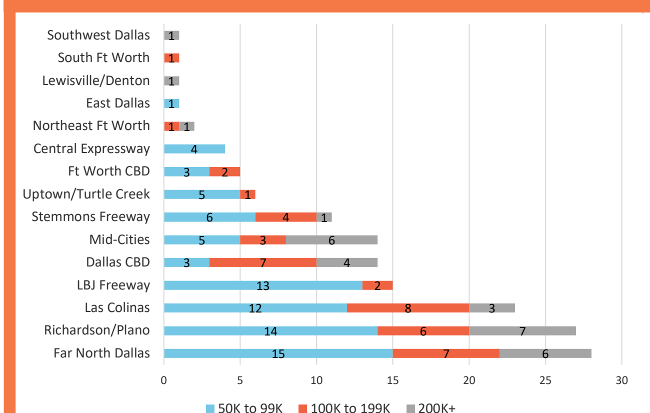

## CLASS OCCUPANCY




## SUBMARKET CONSTRUCTION




## BIG BLOCKS OF SPACE




*Includes Sublease Space

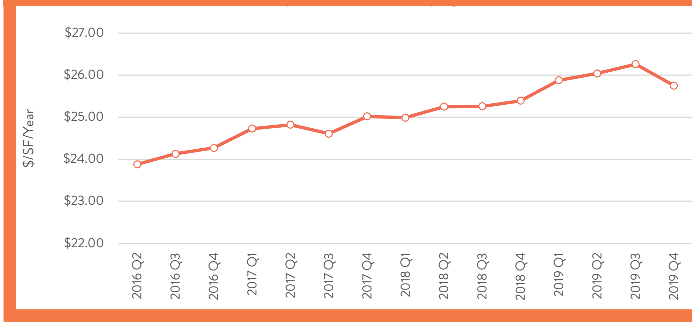
## Rental Rates

While rates are still up year over year, most submarkets (except Far North Dallas and Uptown) saw a moderate dip in rates in the fourth quarter of 2019. This is the first dip the market has seen since the third quarter of 2017, which ended up just being a small blip in an otherwise steady increase of asking rates over the past six years. Overall, the total weighted average asking rate is $25.75 (FSG), which is up 36 cents year over year.

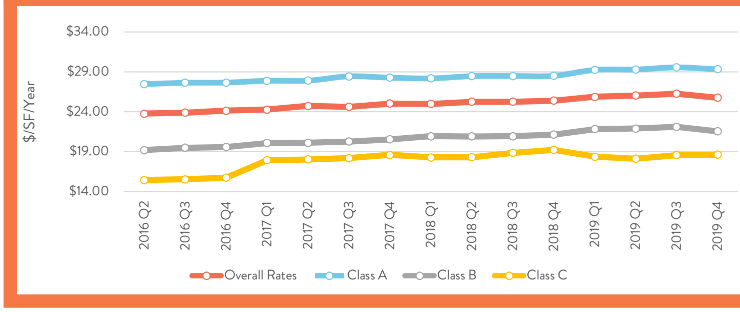
Over the past quarter, Class A annual rental rates decreased $0.24 to $29.32 (FSG), Class B rates decreased $0.56 to $21.55, while Class C rates increased $0.49 to $18.61.

# DALLAS-FORT WORTH

## RENTAL RATE TREND




## CLASS RENTAL RATES




After reaching an all-time high in the third quarter of 2019, overall rates decreased in the fourth quarter. Still, even with the dip, rates are above the overall average for last year. Beneath this trend, there is an interesting dynamic happening between Class A and B rates. Historically, the two moved in pretty close tandem, with the typical spread between Class A and B rates being a little over $5 per SF ($5.24). The delta, however, between the two classes has been widening over the past five years and is currently $7.77. One of the reasons for this expanding delta has been the preponderance of new Class A construction over Class B product. In this construction cycle since 2013, 87% of the new construction completed has been Class A product (30.2 million square feet) as opposed to only 13% for Class B (4.4 million square feet). This is one of the primary reasons why Class A rates have increased much more dramatically than Class B rates, helping to fuel the gap.

YOUNGER PARTNERS

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## SUBMARKETS

| | INVENTORY | | VACANCY | | NET ABSORPTION | | COMPLETIONS | | UNDER CONSTRUCTION | ASKING RENT |
|---|---|---|---|---|---|---|---|---|---|---|
| SELECT SUBMARKETS | # of Bldgs. | Total SF | Total SF | Rate | Current Quarter | YTD | Current Quarter | YTD | At End of Current Quarter | Ytd. Avg. (FS/G) |
| Central Expressway | 99 | 12,326,935 | 1,587,755 | 12.9% | 17,777 | -189,358 | 0 | 0 | 0 | $29.81 |
| Dallas CBD | 94 | 32,150,825 | 6,964,309 | 21.7% | -151,546 | -361,293 | 0 | 0 | 259,230 | $25.41 |
| East Dallas | 141 | 5,701,609 | 702,585 | 12.3% | -38,090 | 24,447 | 25,000 | 25,000 | 372,582 | $26.56 |
| Far North Dallas | 439 | 57,973,400 | 10,184,058 | 17.6% | 164,745 | -828,100 | 255,421 | 720,821 | 2,206,933 | $28.64 |
| Fort Worth CBD | 70 | 11,394,775 | 1,569,251 | 13.8% | -19,709 | 2,040 | 0 | 0 | 0 | $27.62 |
| Las Colinas | 300 | 41,077,209 | 6,061,889 | 14.8% | 1,168,046 | 1,539,713 | 1,160,000 | 1,906,400 | 1,243,753 | $25.76 |
| LBJ Freeway | 149 | 20,476,719 | 4,419,868 | 21.6% | 119,341 | -46,945 | 0 | 0 | 0 | $22.11 |
| Lewisville/Denton | 129 | 6,084,296 | 612,137 | 10.1% | 3,485 | -254,966 | 0 | 36,875 | 282,497 | $22.71 |
| Mid-Cities | 373 | 27,447,664 | 4,588,004 | 16.7% | 427,460 | 999,940 | 1,805,000 | 2,445,000 | 761,258 | $23.09 |
| North Fort Worth | 51 | 3,833,516 | 119,828 | 3.1% | 9,358 | 189,313 | 0 | 200,000 | 52,800 | $25.12 |
| Northeast Fort Worth | 52 | 3,934,375 | 566,319 | 14.4% | 11,210 | 741,113 | 0 | 0 | 0 | $22.93 |
| Preston Center | 52 | 5,631,300 | 566,760 | 10.1% | -84,620 | -5,179 | 0 | 118,000 | 297,000 | $37.47 |
| Richardson/Plano | 325 | 32,655,227 | 5,839,411 | 17.9% | -80,907 | -245,886 | 0 | 165,000 | 1,081,400 | $23.48 |
| South Fort Worth | 178 | 10,125,787 | 992,148 | 9.8% | 17,024 | -22,345 | 41,353 | 90,203 | 57,235 | $23.82 |
| Southwest Dallas | 75 | 3,771,238 | 516,107 | 13.7% | 41,188 | 85,325 | 315,000 | 315,000 | 0 | $21.49 |
| Stemmons Freeway | 117 | 11,338,398 | 2,667,683 | 23.5% | -1,716 | 61,718 | 45,588 | 45,588 | 200,000 | $17.35 |
| Uptown/Turtle Creek | 103 | 14,747,235 | 1,848,539 | 12.5% | 83,738 | 531,097 | 0 | 265,860 | 746,774 | $40.35 |
| TOTAL | 2,747 | 300,670,508 | 49,806,651 | 16.6% | 1,686,784 | 2,220,634 | 3,647,362 | 6,333,747 | 7,561,462 | $25.75 |
| CLASS A | 575 | 158,190,139 | 29,200,584 | 18.5% | 1,401,891 | 2,879,002 | 3,253,563 | 5,768,823 | 6,925,815 | $29.32 |
| CLASS B | 1,684 | 125,034,516 | 19,119,411 | 15.3% | 304,155 | -229,385 | 393,799 | 564,924 | 635,647 | $21.55 |
| CLASS C | 488 | 17,445,853 | 1,486,656 | 8.5% | -19,262 | -428,983 | 0 | 0 | 0 | $18.61 |
| TOTAL DFW | 2,747 | 300,670,508 | 49,806,651 | 16.6% | 1,686,784 | 2,220,634 | 3,647,362 | 6,333,747 | 7,561,462 | $25.75 |

For additional information on any of the submarkets shown above, please refer to our Market Snapshot reports.

* Younger Partners research is based on the CoStar office building database. Inventory includes office buildings containing at least 15,000 rentable square feet; single tenant, multi-tenant and owner-occupied; Class A, B and C; existing, under construction or under renovation; excludes medical office buildings and data centers.