YOUNGER PARTNERS

First Quarter 2020 / Office Research Report

14643 Dallas Parkway, Suite 950,
LB#58 | Dallas, TX 75254
214.294.4400

MARKETInsights

Population

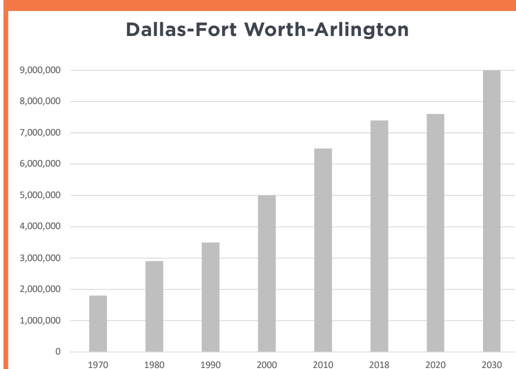
Lower costs of living and tax advantages have played a key role in extremely high net migration to Dallas-Fort Worth-Arlington over the past several years. Companies and individuals from higher priced coastal markets like San Francisco, Los Angeles and New York City have seen a large exodus of people 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 per day.

The Dallas-Fort Worth-Arlington metropolitan area's 130,000-resident increase over the past year was the most of any metro area in the United States.

Prior to the recent spread of the Covid-19, the Dallas-Fort Worth-Arlington metropolitan area continued to produce new jobs, adding 119,300 jobs over the past 12 months. Employment gains were found across all industry sectors, led by professional and business services, adding 21,400 jobs, leisure and hospitality, adding 19,000 jobs, and education and health services, adding 18,000 jobs.

POPULATION GROWTH



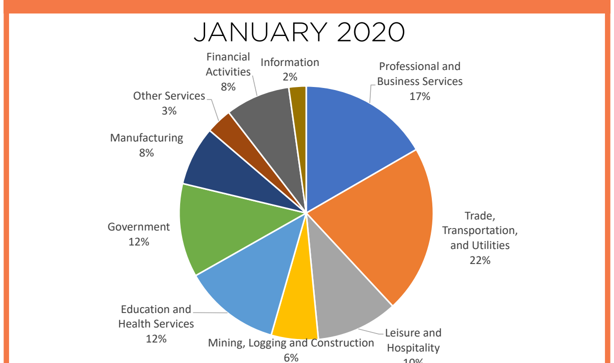
Source: North Texas Council of Governments; US Census

Employment

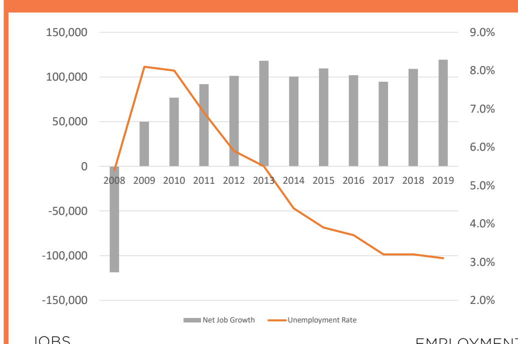
For office space demand, employment– especially employment in the "office-using" industry sectors – is a key driver. Office using sectors are Professional and Business Services, Financial Activities, and Information.

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 over 4 million as of January 2020. Of this total, almost 27% or 1.1 million jobs were in the office-using sectors.

EMPLOYMENT BY INDUSTRY SECTOR



NET JOB GROWTH VS. UNEMPLOYMENT RATE

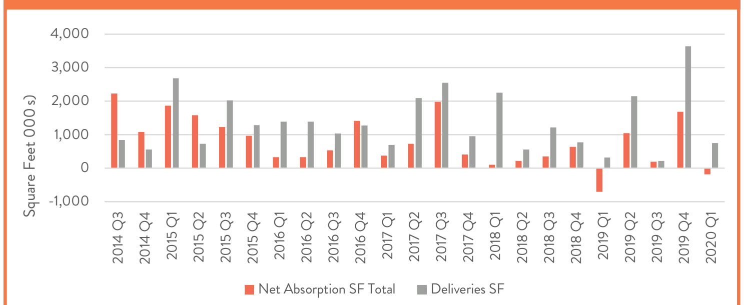


Demand and Supply

Construction deliveries and demand for space were low in the first quarter of 2020, with a negative 182,353 square feet absorbed and 750,834 square feet completed. This slow start to the year was mirrored in 2019, with the remainder of the year picking up in both demand and construction activity. With the recent shutdown of several parts of the world economy due to Covid-19, it is too early to know how severely the slowdown will be ahead, but decreased leasing activity is likely in 2020, for at least the next two quarters.

Among the property classes, Class A properties recorded a negative 172,945 square feet in the first quarter, while Class B was a positive 47,549 square feet and Class C properties had a negative 56,957 square feet.

NET ABSORPTION & DELIVERIES



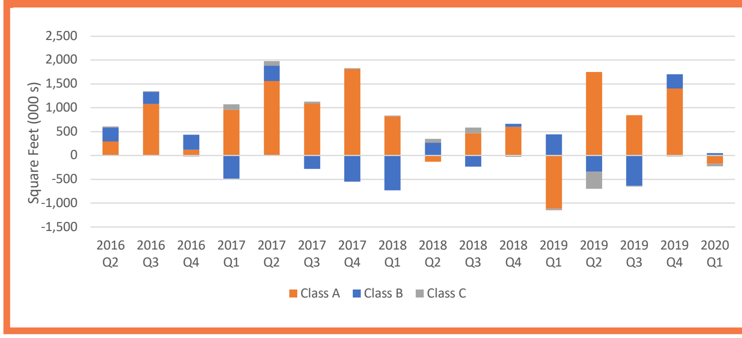
Construction deliveries for the quarter were low in the first quarter, following the end of 2019, which saw the completion of American Airlines new headquarter built-to-suit campus being delivered, along with Pioneer Natural Resources and several mid-sized spec projects, like Redbird One and the Offices at the Realm.

As of March 2020, there was a total of 7,647,415 rentable square feet of office space under construction in Dallas-Fort Worth. Of the 7.6 million square feet of construction currently underway, 3.4 million square feet is scheduled for delivery in 2020.

Of the 7.6 million square feet of space currently under construction, 49% percent has been accounted for through a combination of built-to-suits and pre-leasing.

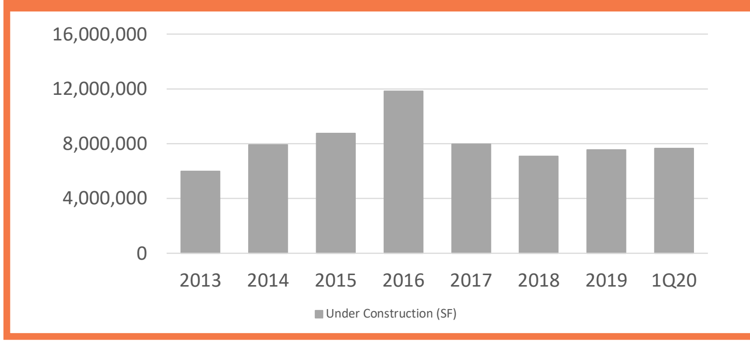
JP Morgan Chase (phase 2), Keurig Dr Pepper new build-to-suit and several spec office construction projects (Headquarters II, Frisco Station, Legacy Town Center) make Far North Dallas currently the most active submarket with 31% of the current under construction pipeline. East Dallas, a traditionally very small and inactive submarket, currently has two large build-to-suit projects

CLASS NET ABSORPTION



for Uber (Epic phase 2) and Baylor Scott and White Health that make up 14% of the submarket's construction pipeline. There have been several recently announced spec projects that have not yet broken ground and are expected to begin construction some time in 2020 (most of these projects are concentrated in Legacy area of Far North Dallas and Uptown).

SF CURRENTLY UNDER CONSTRUCTION



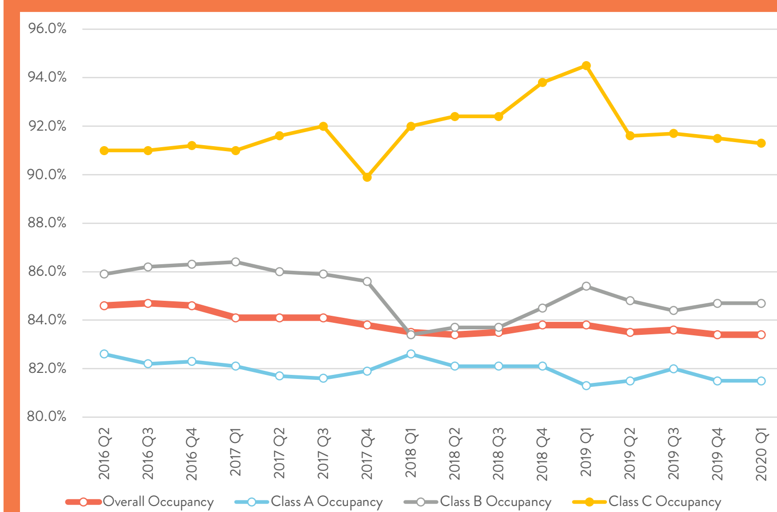
Occupancy Trends

Absorption was slightly negative in the first quarter, but with limited construction deliveries, the overall occupancy rate remained unchanged at 83.4%. Over the past five years, however, 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 construction 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-square-foot 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).

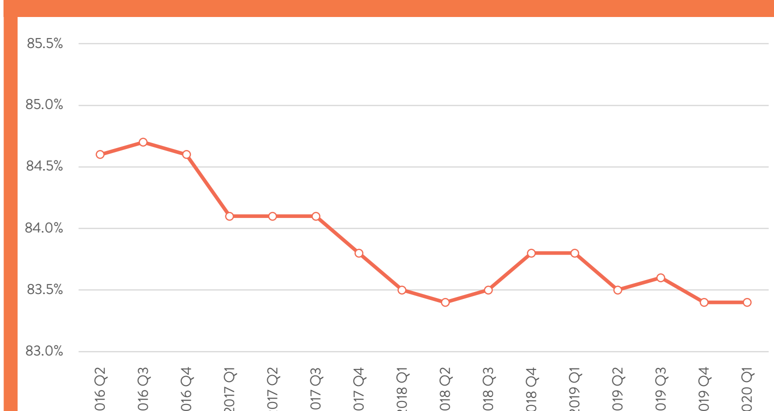
With elevated construction this past year and a robust construction pipeline, the overall occupancy decline is expected to continue for the foreseeable future. This is mainly due to new construction, but also because several office using industries have been squeezing more employees into less space than in the past. A trend that is likely to change as "social distancing" influences design. With the construction pipeline at 7.6 million square feet and rates far above previous cycles, occupancy is expected to decline 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 amount of large blocks of second-generation spaces that will need to be backfilled (many of which were recently vacated for the large built-to-suit projects).

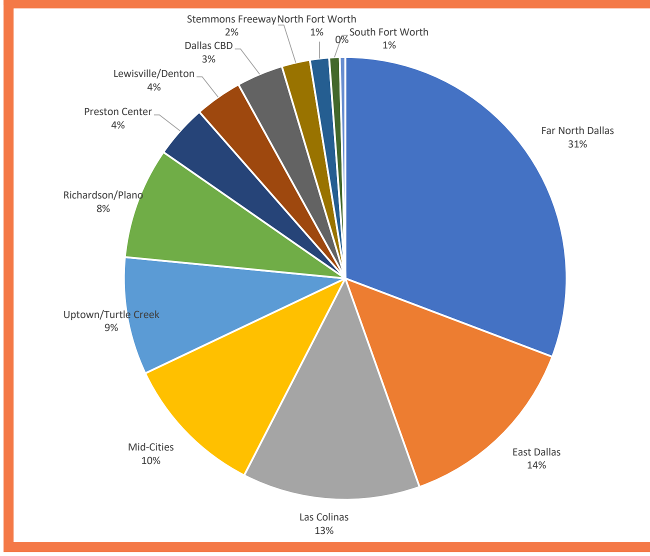
CLASS OCCUPANCY



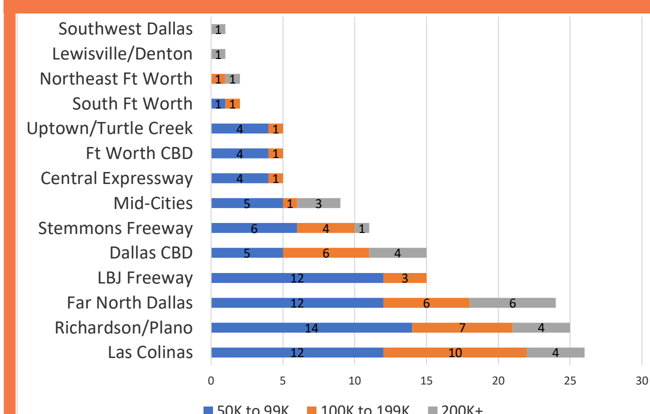
OCCUPANCY TRENDS



SUBMARKET NEW CONSTRUCTION



BIG BLOCKS OF SPACE



*Includes Sublease Space

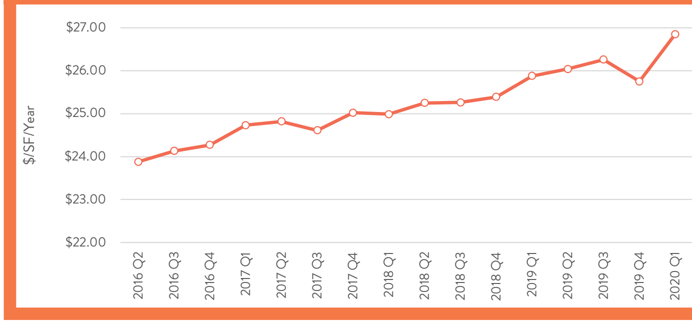
Rental Rates

Rates saw a spike over the past quarter, but changes to the methology of quoted rates were a factor (quoted rental ranges were taken out, only a single rate is now used). Overall, the total weighted average asking rate is $26.85 (FSG), which is up 97 cents year over year.

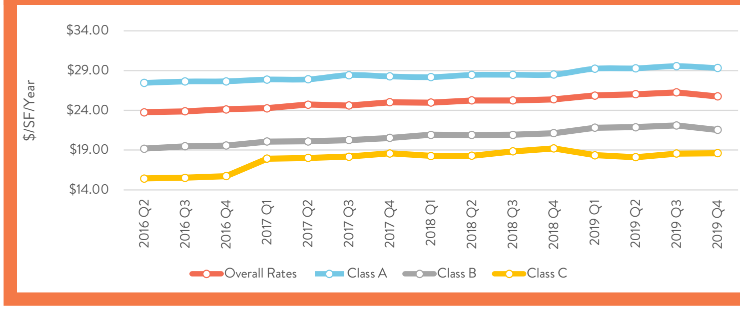
Over the past quarter, Class A annual rental rates increased $0.92 to $30.24 (FSG), Class B rates increased $0.42 to $21.97, while Class C rates increased $0.46 to $19.07.

DALLAS-FORT WORTH

RENTAL RATE TREND



CLASS RENTAL RATES



After a dip in the fourth quarter, rates have trended back upward and are now at all-time historic highs. Beneath this trend, there is an interesting dynamic happening between Class A and Class B rates. Historically, the two move in pretty close tandem with the typical spread between Class A and B rates being a little more than $5 per square foot ($5.24). The delta, however, between the two classes has been widening over the past five years and is currently $8.27. 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.

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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	Wtd. Avg. (FS/G)
Central Expressway	99	12,155,761	1,667,436	13.7%	-74,173	-74,173	0	0	30,252	$30.76
Dallas CBD	94	32,142,495	7,800,080	24.3%	-388,927	-388,927	0	0	259,230	$26.18
East Dallas	141	5,608,430	526,549	9.4%	127,760	127,760	0	0	1,054,893	$26.47
Far North Dallas	439	57,906,197	9,418,561	16.3%	299,673	299,673	260,429	260,429	2,352,411	$29.88
Fort Worth CBD	70	11,394,775	1,533,875	13.5%	35,376	35,376	0	0	0	$28.28
Las Colinas	300	41,419,529	6,243,266	15.1%	-141,764	-141,764	250,000	250,000	993,753	$26.00
LBJ Freeway	149	20,504,264	4,388,596	21.4%	31,272	31,272	0	0	0	$22.87
Lewisville/Denton	129	6,050,320	586,643	9.7%	15,095	15,095	0	0	263,137	$24.14
Mid-Cities	373	27,214,157	4,390,744	16.1%	27,988	27,988	70,000	70,000	795,316	$23.44
North Fort Worth	51	3,750,891	151,981	4.1%	-33,800	-33,800	0	0	106,800	$24.96
Northeast Fort Worth	52	3,923,375	584,327	14.9%	-18,008	-18,008	0	0	0	$22.90
Preston Center	52	5,643,455	571,823	10.1%	-5,063	-5,063	0	0	297,000	$36.88
Richardson/Plano	325	32,686,516	5,781,153	17.7%	110,349	110,349	52,091	52,091	621,323	$24.06
South Fort Worth	178	10,164,800	1,058,546	10.4%	-66,398	-66,398	0	0	58,526	$24.15
Southwest Dallas	75	3,799,552	568,882	15.0%	-24,461	-24,461	28,314	28,314	0	$23.19
Stemmons Freeway	117	10,895,836	2,736,342	25.1%	-146,735	-146,735	0	0	158,000	$17.96
Uptown/Turtle Creek	103	14,788,757	1,863,568	12.6%	69,463	69,463	90,000	90,000	656,774	$40.72
TOTAL	2,747	300,049,110	49,872,372	16.6%	-182,353	-182,353	750,834	750,834	7,647,415	$26.85
CLASS A	575	159,262,216	29,500,474	18.5%	-172,945	-172,945	585,429	585,429	7,051,858	$30.24
CLASS B	1,684	123,521,851	18,870,868	15.3%	47,549	47,549	165,405	165,405	595,557	$21.97
CLASS C	488	17,265,043	1,501,030	8.7%	-56,957	-56,957	0	0	0	$19.07
TOTAL DFW	2.747	300.049.110	49.872.372	16.6%	(182.353)	(182.353)	750.834	750.834	7.647.415	$26.85

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.