

Q3 2021

# DALLAS-FORT WORTH

## OFFICE MARKET REPORT

DFW OFFICE MARKET SEES  
**POSITIVE DEMAND**  
SINCE ALMOST TWO YEARS AGO

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An aerial photograph of a city skyline at dusk. The sky is a deep blue. Several skyscrapers are visible, with their windows glowing with warm yellow light. The most prominent building on the right is a tall, dark glass skyscraper with a sharp, triangular top. To its left is another tall building with a similar glass facade. In the center, a smaller, more traditional skyscraper with a pointed top is visible. The foreground shows a mix of urban landscape, including trees, streets, and lower-rise buildings. The text "ECONOMIC CONDITIONS" is overlaid in large, white, sans-serif capital letters across the middle of the image.

# ECONOMIC CONDITIONS



# POPULATION

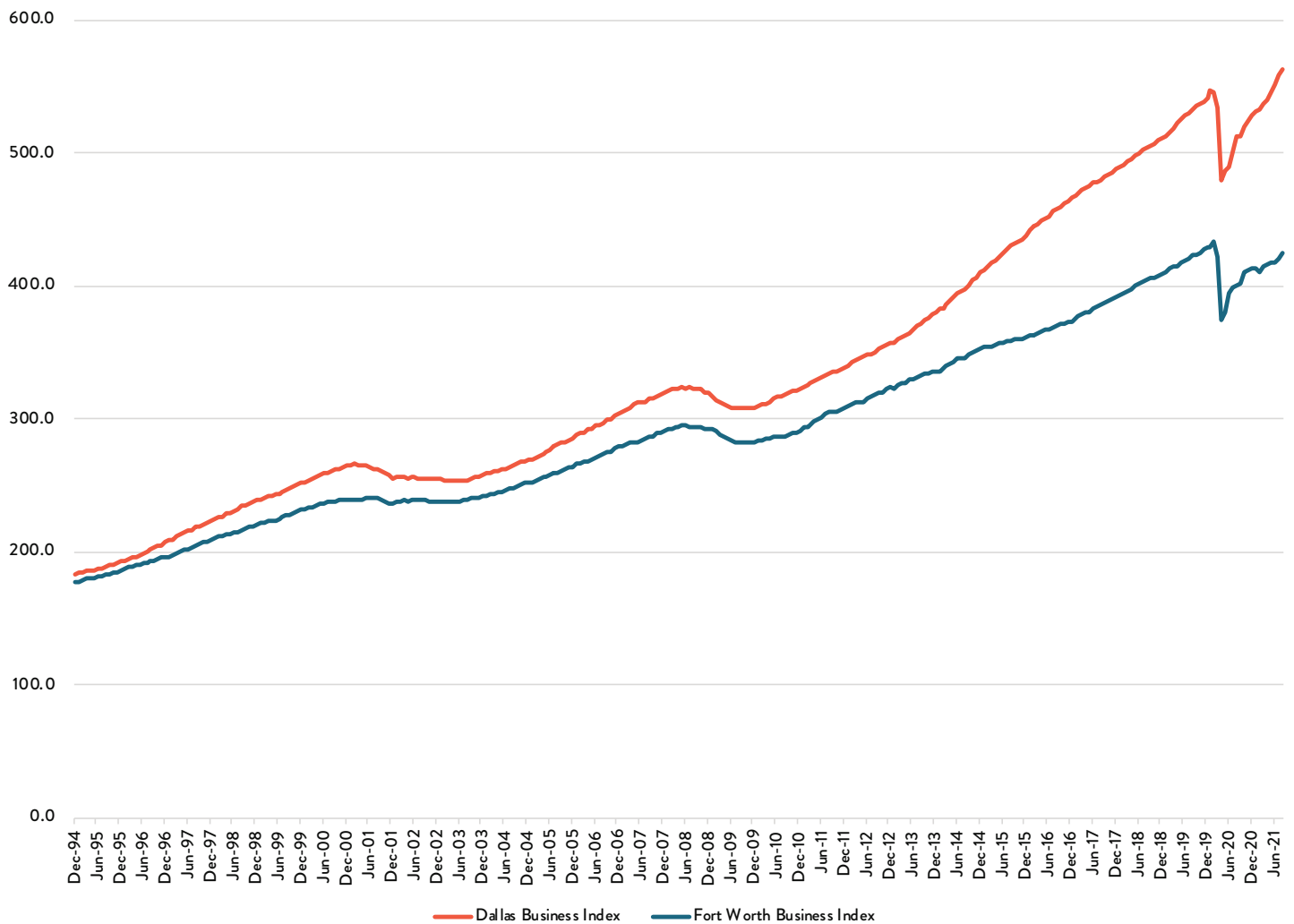
**T**he unemployment rate in Dallas-Fort Worth (DFW) dipped below 6.0% for the first time since the onset of the pandemic in March 2020. In the latest data available (July of 2021), the unemployment rate fell further for DFW to 5.3%. Since peaking in early April 2020, the headline unemployment rate in DFW has generally been on a downward trend.

DFW employment continued to recover at a solid clip through the summer months. DFW added nearly 23,000 jobs, or an annualized 7.5% increase in July after expanding 8.5% in June. That brought DFW payrolls to a 91.0% recovery of the jobs lost in March and April of 2020. The Dallas–Plano–Irving metro division had nearly recouped all its lost jobs by July, while the employment recovery in Fort Worth–Arlington trailed with only 72.4% of its lost jobs recovered.

According to the Federal Reserve Bank of Dallas, the Dallas and Fort Worth business-cycle indexes (broad measures of economic activity) continued to expand in July, buoyed by recent job gains and unemployment rate declines. The Dallas index rose an annualized 14.3%, eclipsing its pre-pandemic peak and marking the fifteenth successive month of growth. The Fort Worth index increased 7.7% in July, its fifth straight month of expansion; it remains down 2.8% from February 2020 levels.

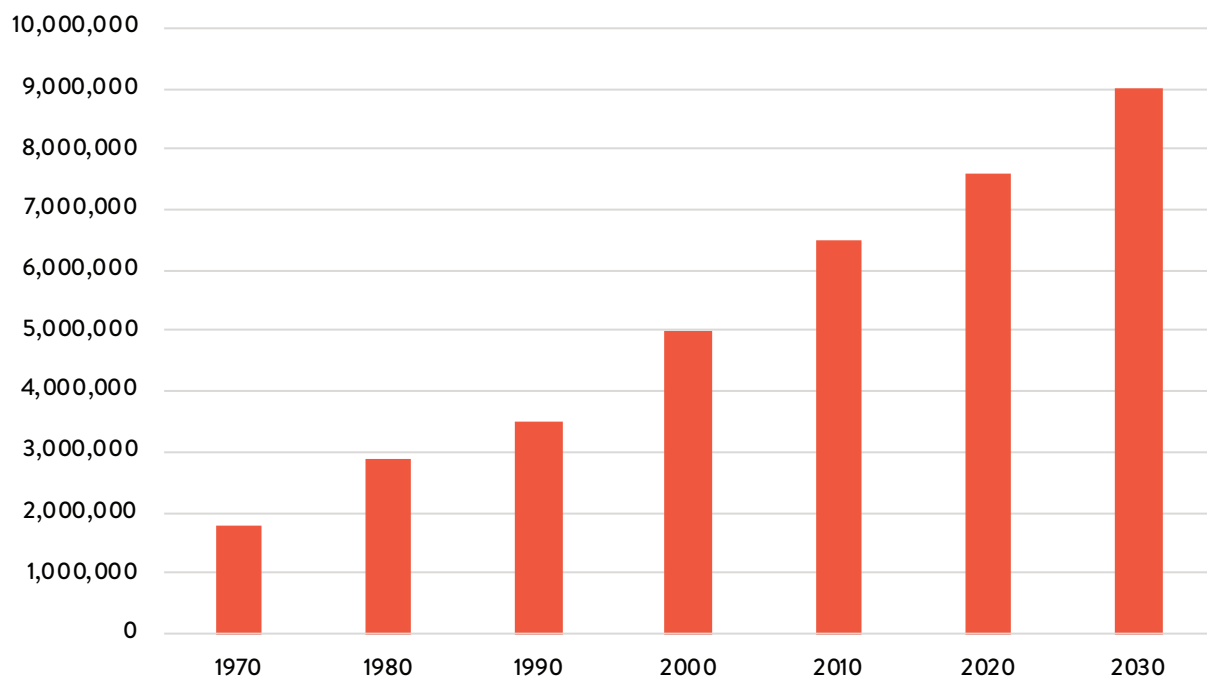


# DALLAS FED BUSINESS INDEX DALLAS AND FORT WORTH (BROAD MEASURES OF ECONOMIC ACTIVITY)



Longer term as more workers return to their workplaces, DFW's more affordable home prices, lower costs of living and tax advantages are expected to play a key role in high net migration to Dallas-Fort Worth for the foreseeable future. Companies and individuals from higher priced coastal markets like San Francisco, Los Angeles and New York City have opted to "flee" to other parts of the country. Texas and Dallas-Fort Worth, in particular, have been one of the primary beneficiaries of this trend. Over 20 companies have either relocated or significantly expanded operations in DFW this year.

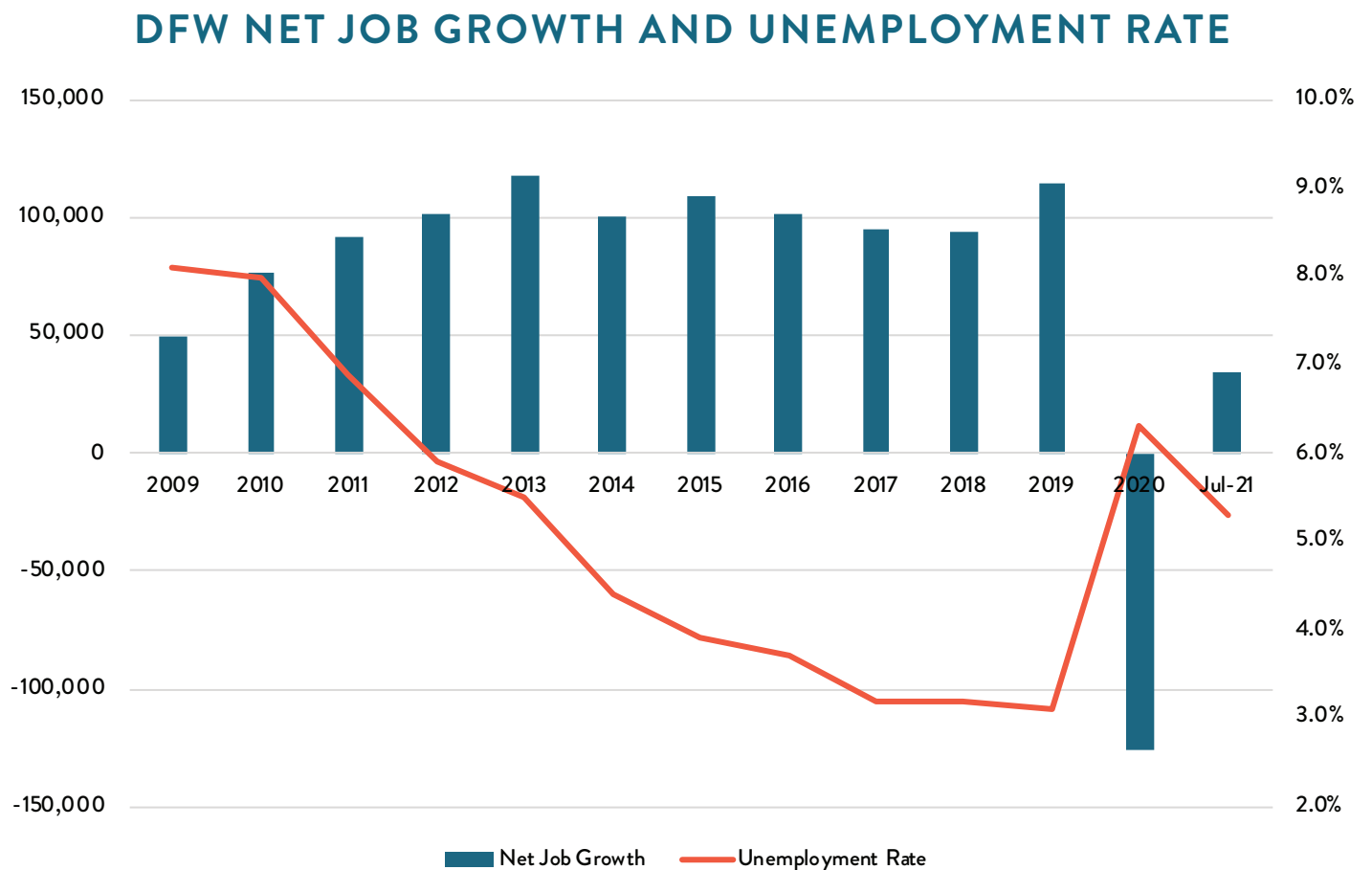
## DALLAS/FORT WORTH POPULATION GROWTH



Source: North Texas Council of Governments; US Census



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 7.6 million. Since the 2010 census, the Census Bureau estimates the population of the Dallas-Fort Worth MSA grew by 23.1%. This was the most of any metropolitan area in the country for the same time period.

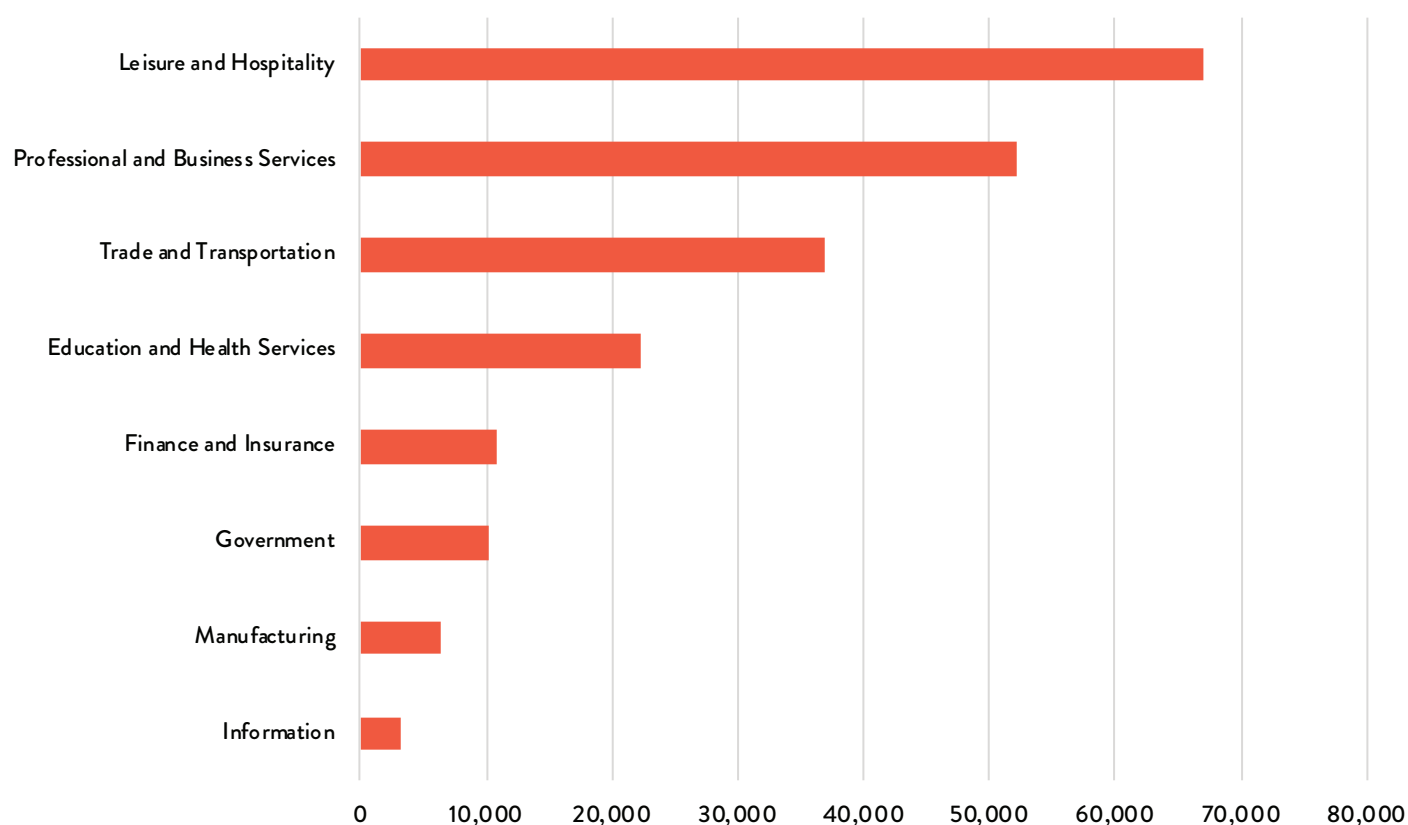


The unemployment rate in Dallas-Fort Worth, as of July 2021, stands at 5.3% and job growth has turned positive with 35,000 jobs through July 2021.

# EMPLOYMENT

**F**or office space demand, employment – especially employment in the “office-using” industry sectors – is a key driver.

## JOB GROWTH BY INDUSTRY (JULY 2020 TO JULY 2021)



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 3.8 million as of July 2021. Of this total, 29% or over 1 million jobs were in the office-using sectors of Professional and Business Services, Financial Activities and Information.



# OFFICE MARKET CONDITIONS

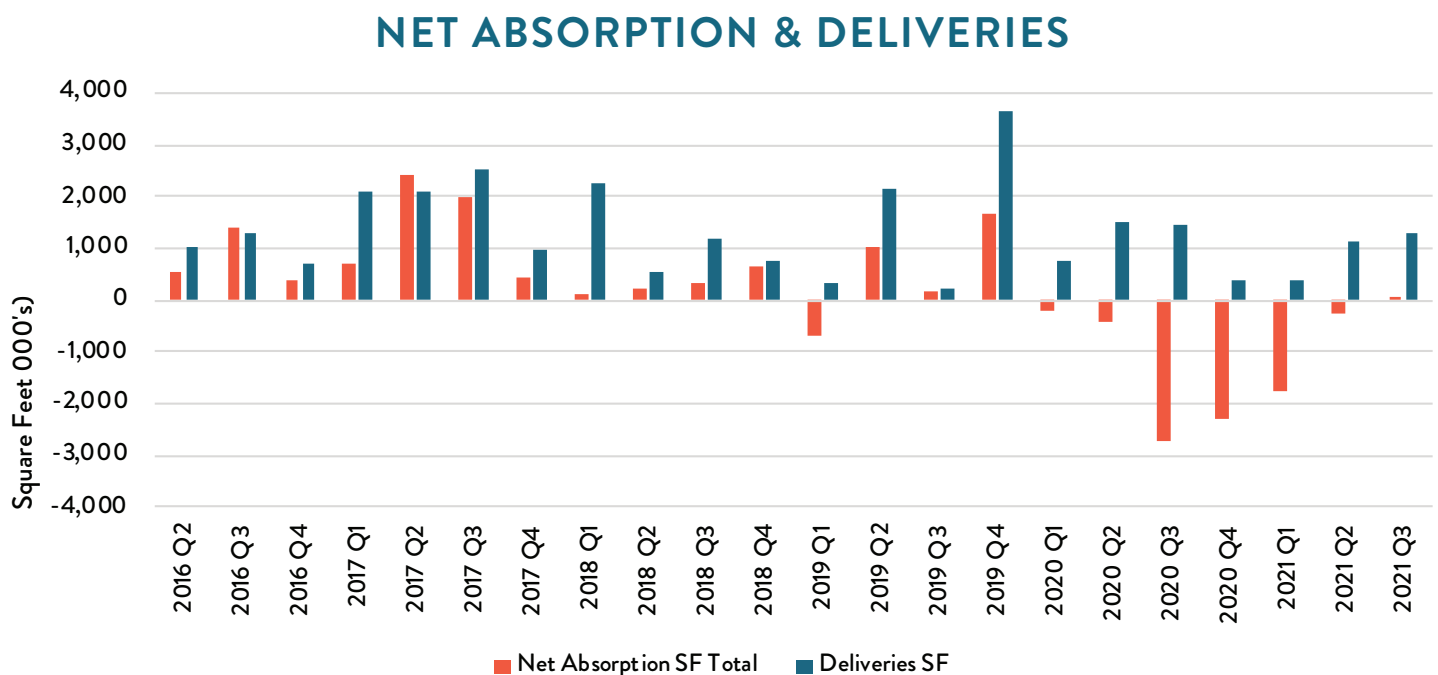




# DEMAND & SUPPLY

Overall total net absorption moved into positive territory for the first time since 2019, as two large built-to-suits by JPMorgan Chase (phase 2) and Keurig Dr Pepper delivered in third quarter of 2021 in the Far North Dallas submarket. Both of these deals were the predominant contributor to the overall direct net absorption (over 330,000 square feet), however, an increase in vacant sublease space (315,000 square feet) kept the total net absorption number just positive for the quarter (15,139 square feet).

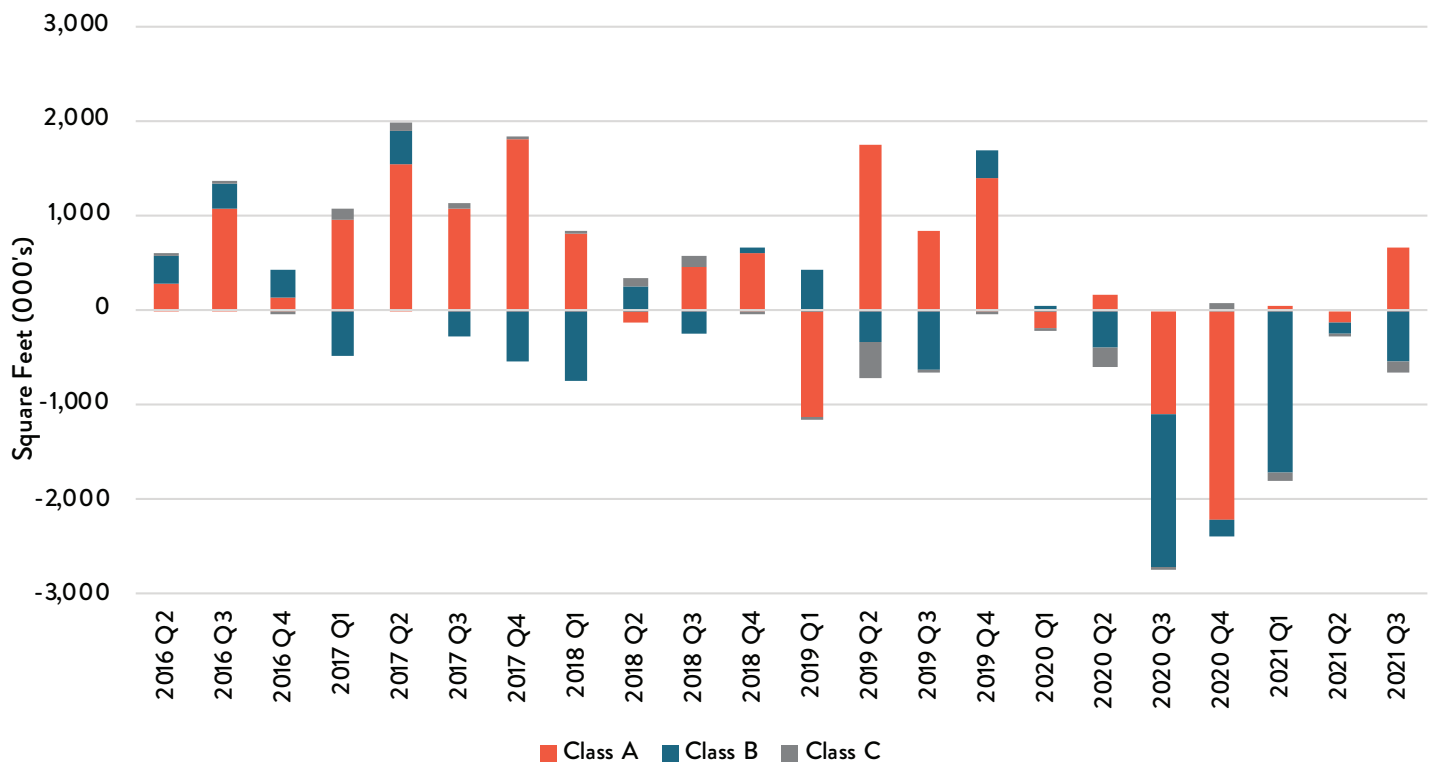
Overall, with 1.3 million square feet of new deliveries and limited positive net absorption, the total vacancy rate remained unchanged at 20.0%. The total vacancy rate is expected to increase slightly before the end of 2021, due to another 5.8 million square feet underway (2 million of which is scheduled for delivery in the fourth of 2021).





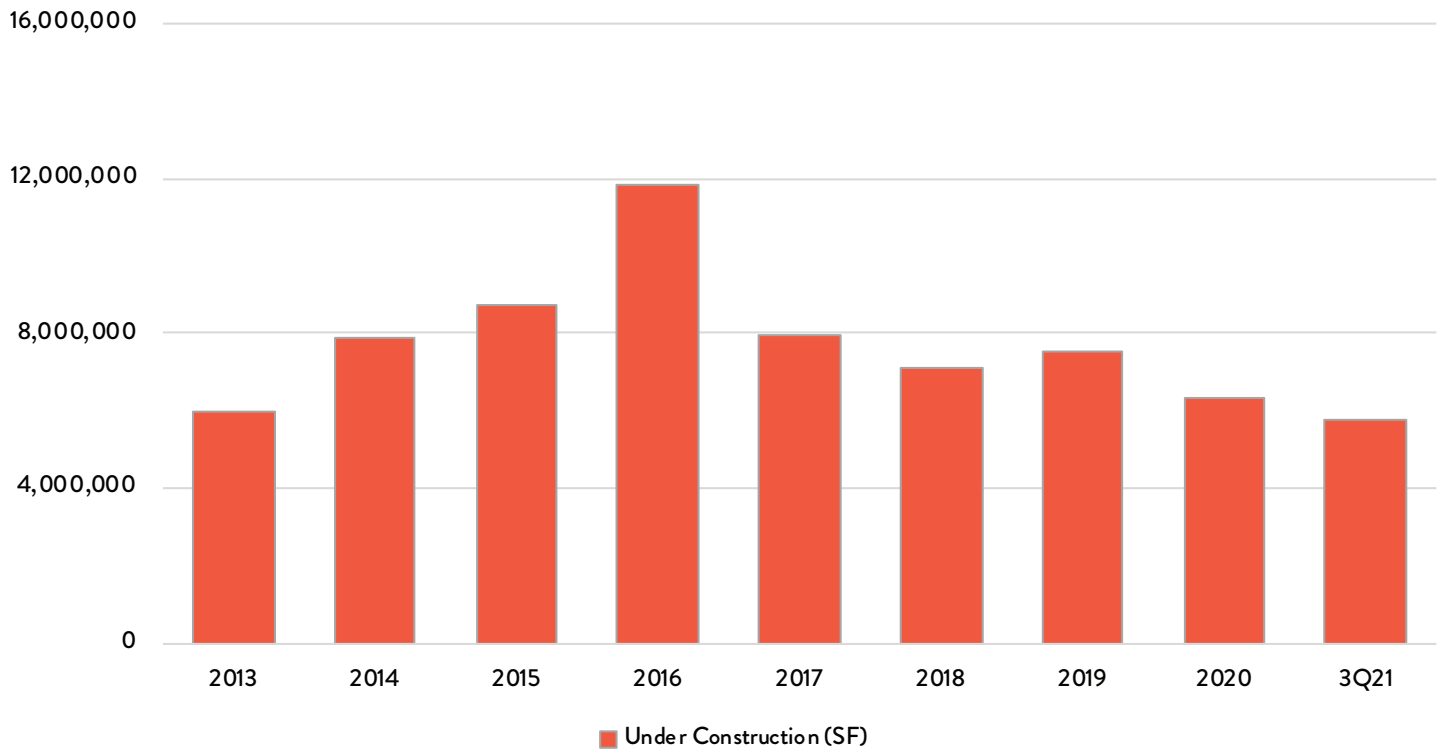
Absorption figures varied among the property classes in the third quarter of 2021. Class A properties recorded a positive 660,940 square feet, while Class B properties recorded a negative 538,753 square feet and Class C properties had a negative 107,048 square feet.

### CLASS NET ABSORPTION



As of September 2021, there was a total of 5,780,900 rentable square feet of office space under construction in Dallas-Fort Worth. Of the 5.8 million square feet of construction currently underway, 2 million square feet is scheduled for delivery in the fourth quarter of 2021.

## DFW NEW CONSTRUCTION

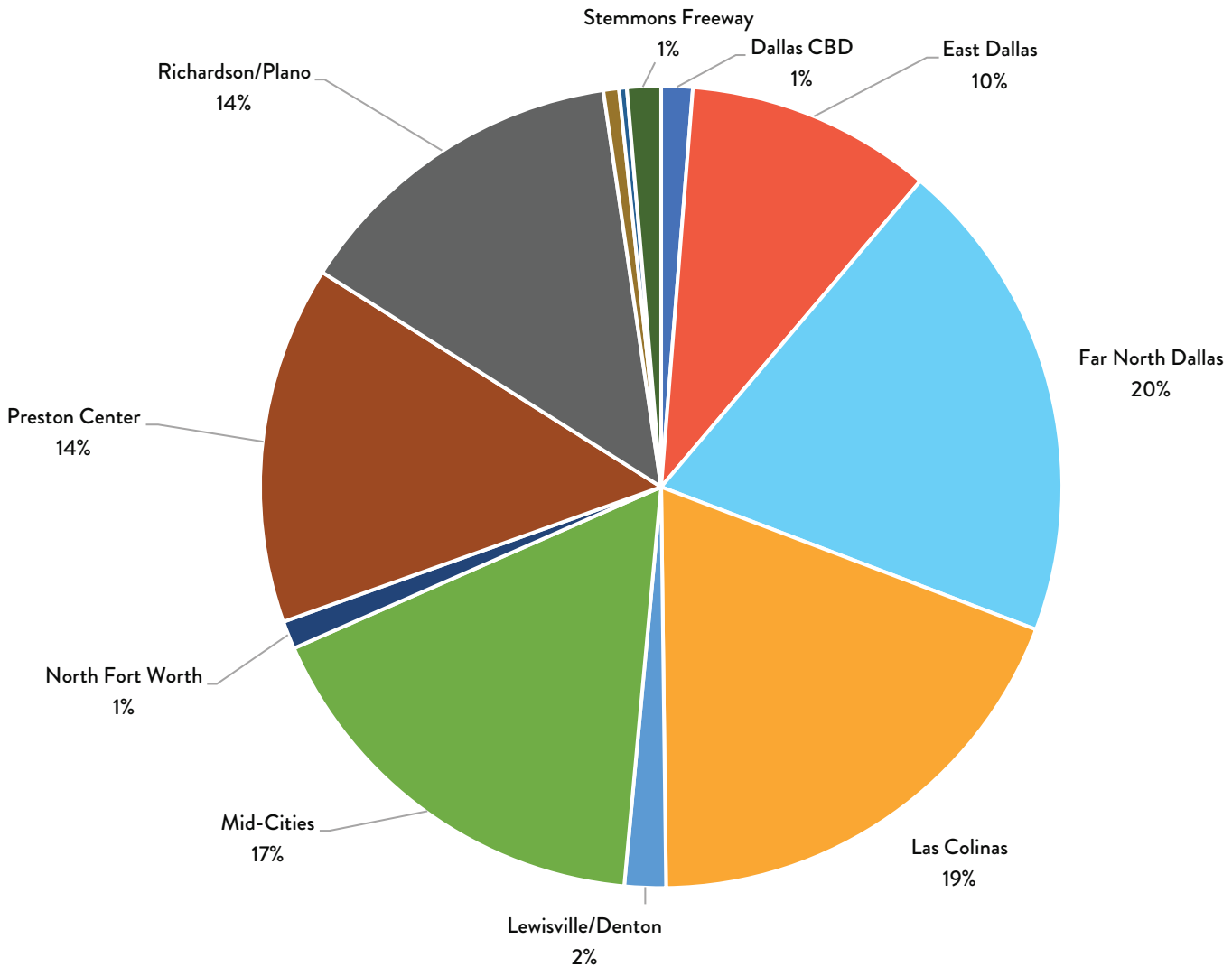


Of the 5.8 million square feet of space currently under construction, 48 percent has been accounted for through a combination of built-to-suits and pre-leasing.





## DFW UNDER CONSTRUCTION (5.8 MILLION SQUARE FEET)

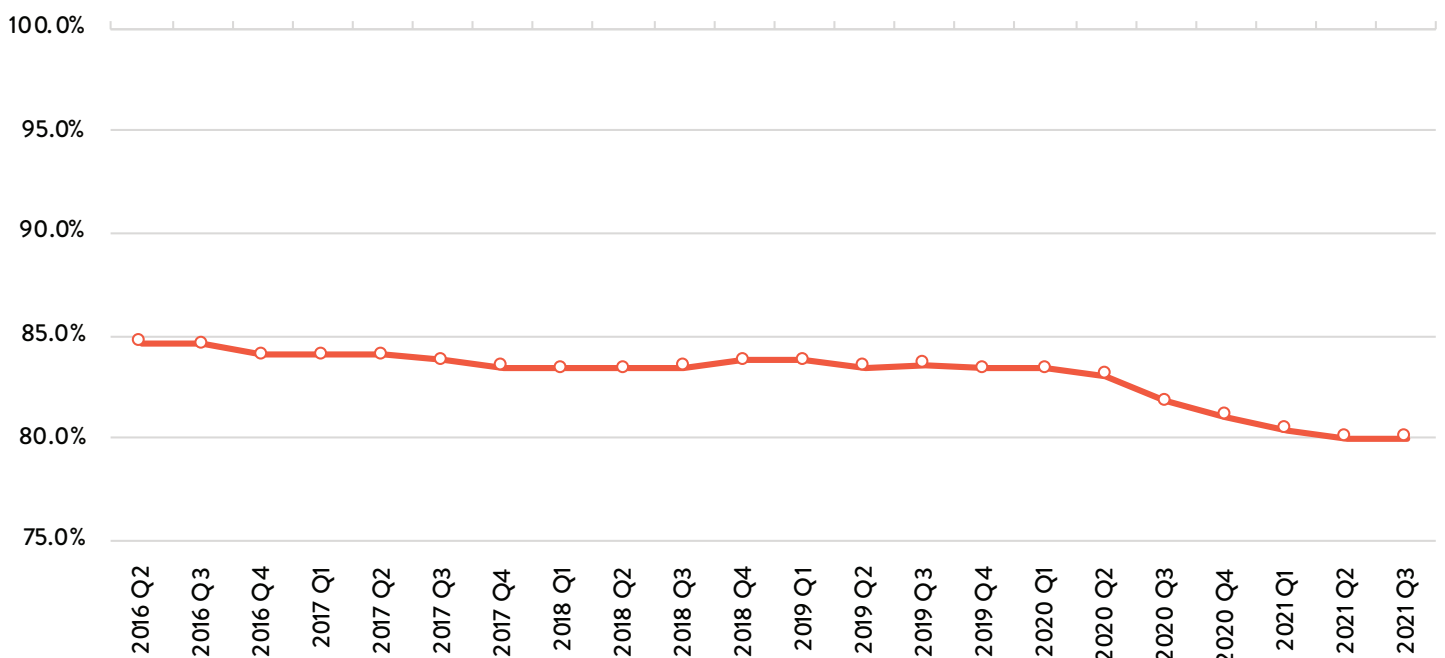


Far North Dallas leads the market in office projects currently underway (Reata Pharmaceuticals, The Star-Phase IV, The Parkwood and PGA Headquarters), followed by Las Colinas (Christus Health, Cypress Waters and Paycom).

# OCCUPANCY TRENDS

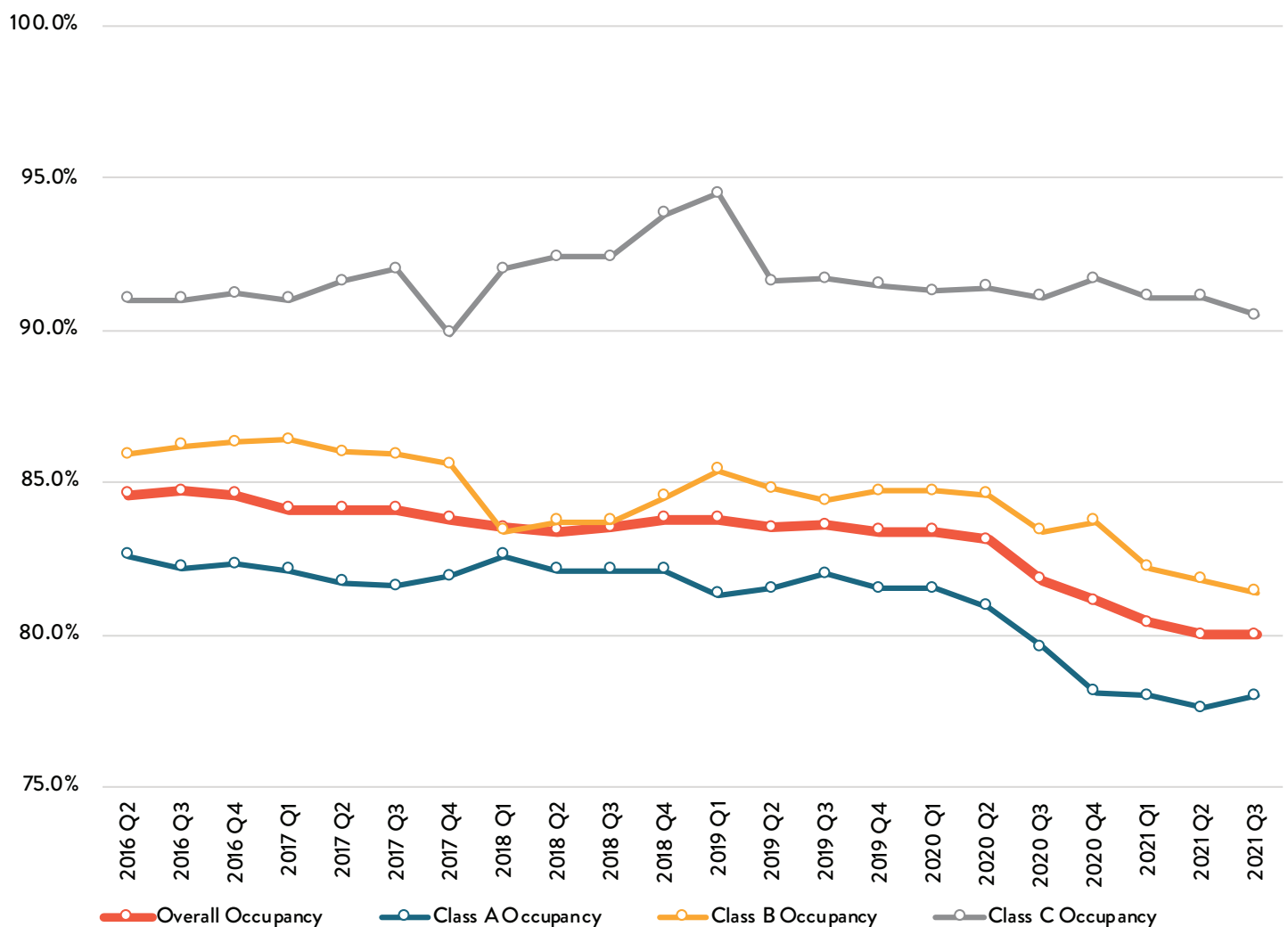
Overall occupancy remained unchanged for the quarter, with positive net absorption was balanced by new construction deliveries. Most of the absorption over recent quarters has been in newly constructed properties, while older properties have largely languished. There are several older large office projects that are currently vacant or have very large blocks of space, 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 in Fort Worth, JCPenney's 1 million square feet at their former headquarters at the Campus at Legacy West and several Dallas CBD skyscrapers (Bryan Tower, Renaissance Tower, 1700 Pacific, Bank of America Plaza, Fountain Place, Comerica Bank Tower and Energy Plaza all have 500,000 square feet or more of available space for lease).

## OCCUPANCY TRENDS



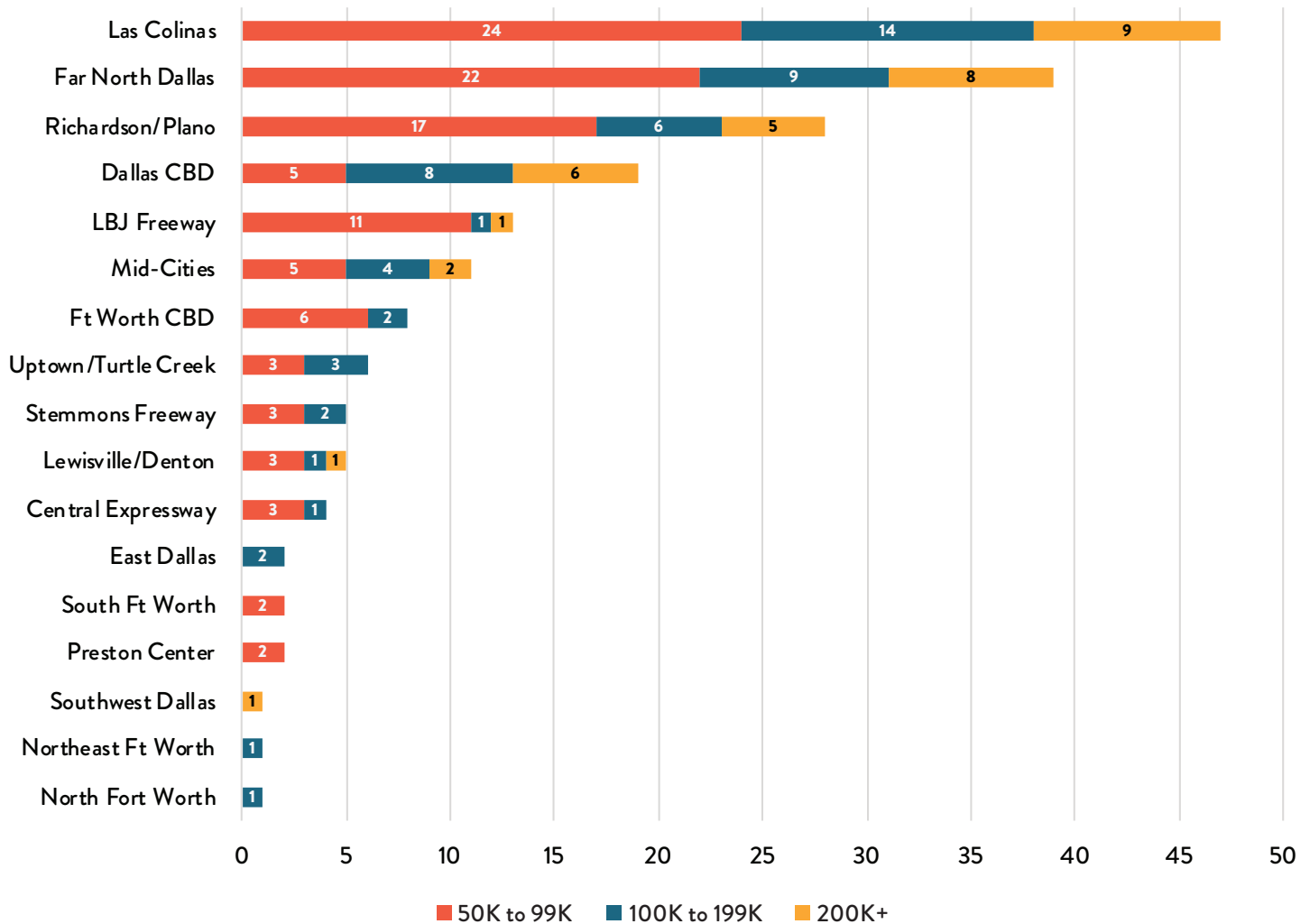
With demand for space currently flat and about half of the construction pipeline accounted for, a moderate decrease in the overall occupancy rate is expected to continue for the foreseeable future. While newer construction should continue to perform well, there will be older properties that lose tenants and will likely have a hard time backfilling older second generation space. This combined with record high sublease space will put downward pressure on occupancy over the next few quarters.

## CLASS OCCUPANCY





## BIG BLOCKS OF SPACE

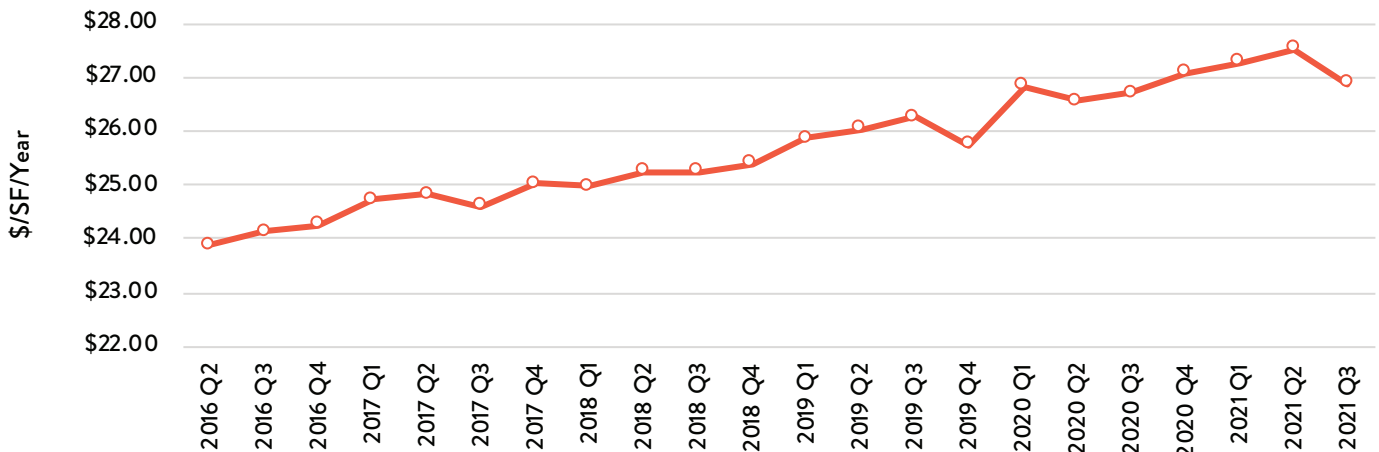


Despite the elevated levels of new construction over the past five years, one of the highest risks in the market is the amount of large blocks of second-generation spaces that will need to be backfilled (many of which were recently vacated for the large built-to-suit projects). As of September 2021, there are 194 big blocks of space over 50,000 square feet (these include both direct and sublease space).

# RENTAL RATE TRENDS

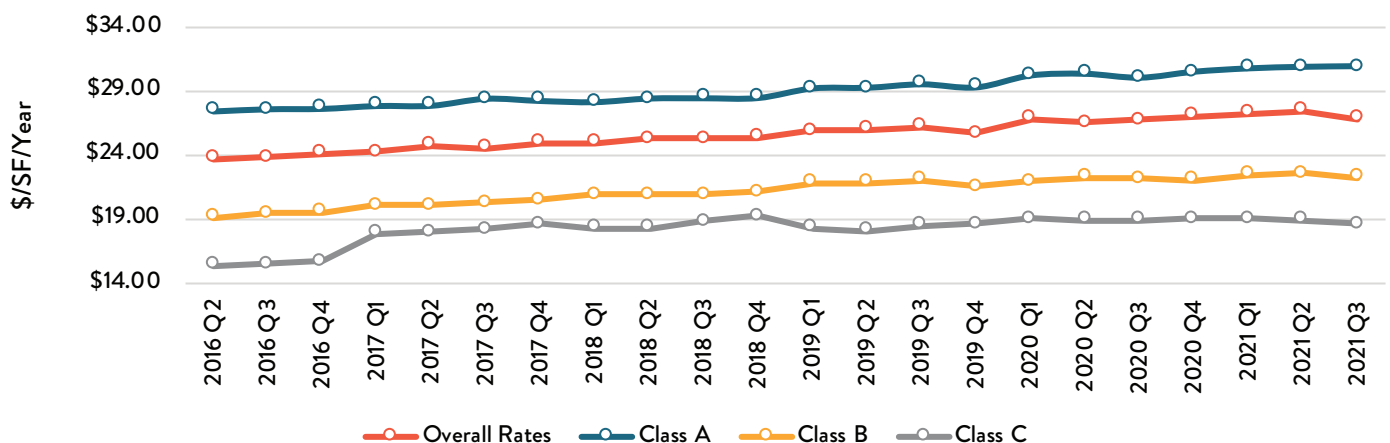
**F**or the first time this cycle, quarterly average asking rates have decreased. Even with the decrease, rates are still up slightly year-over-year. Overall, the total weighted average asking rate is \$26.90 (FSG), which is up \$0.18 from the third quarter of 2020.

## RENTAL RATE TRENDS



Over the past quarter, Class A annual rental rates increased \$0.05 to \$30.96 (FSG), Class B rates decreased \$0.38 to \$22.23, while Class C rates decreased \$0.34 to \$18.62.

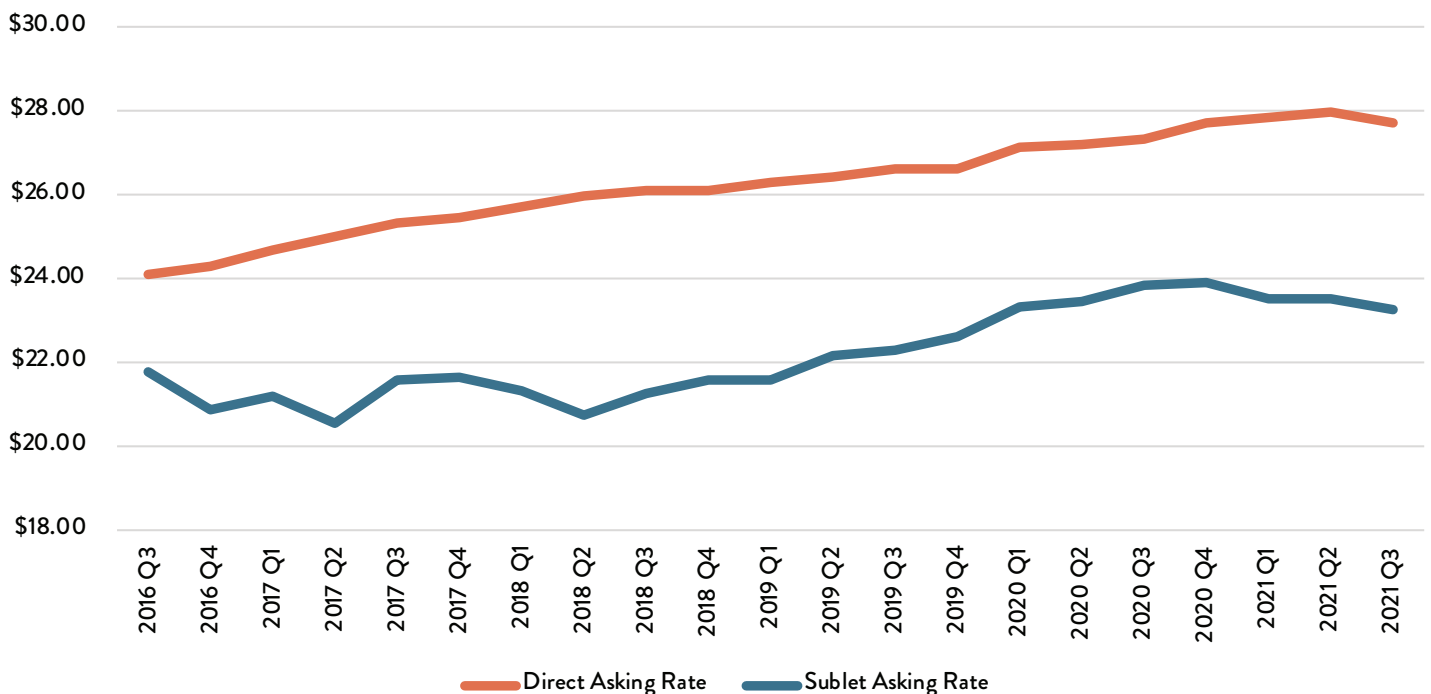
## CLASS RENTAL RATES



# RENTAL RATE INSIGHTS

A peculiar thing happens to office asking rates when leasing and tour activity seize up, the movement in rental rates pretty much stops moving as well. Landlords are hesitant to lower asking rates until they feel like they are being eliminated from consideration by tenants out touring the market for space. That's one of the primary reasons rates are a lagging indicator in comparison to other market statistics like net absorption and vacancy. Even against the backdrop of a global pandemic and widespread work from home measures for all of the office markets across the country, many markets like Dallas-Fort Worth have only seen a muted response on the rental rate front. This is while the other market fundamentals have weakened with higher availability and vacancy increases due to tenant downsizing.

## DFW OFFICE ASKING RATES (DIRECT AND SUBLEASE, FSG)





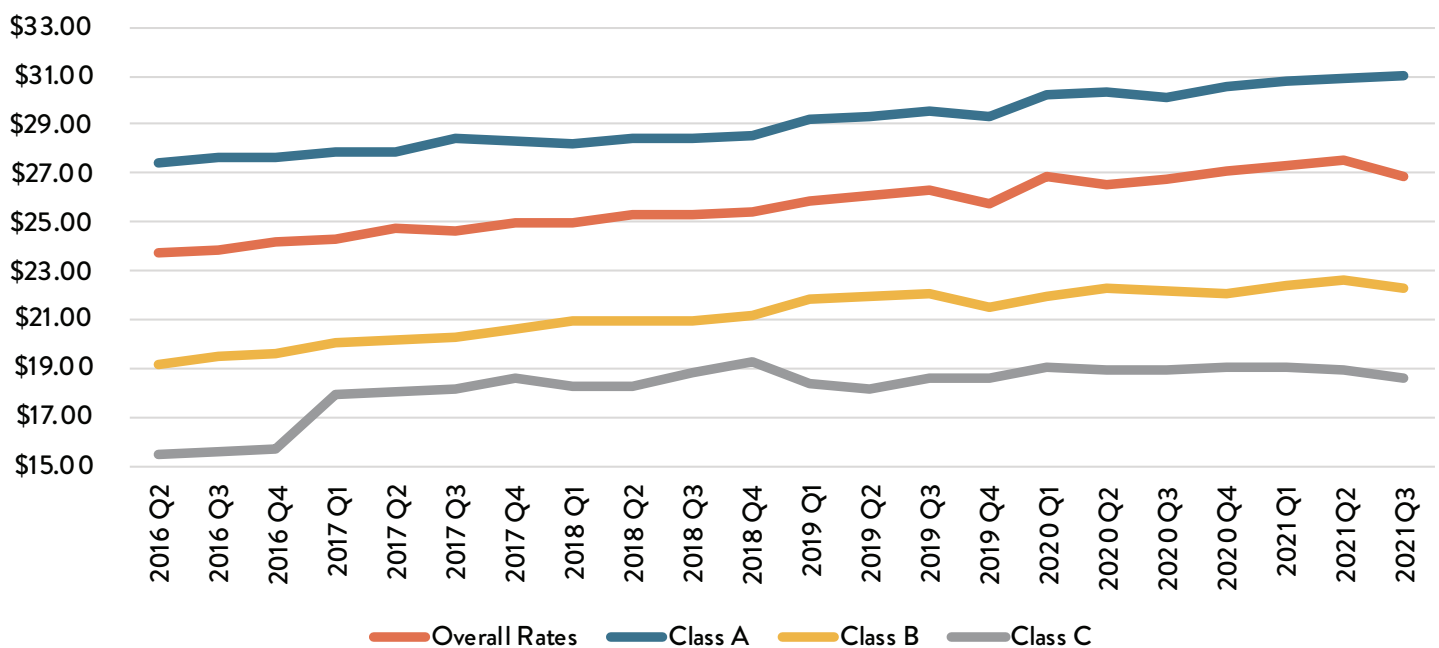
But as many other market experts have touched on in recent articles on the state of the market, the market is beginning to thaw from being frozen over the past year and a half. Tour activity has begun to pick back up again, and with that, rates have begun to move from the increased activity.

In DFW specifically, after six quarters of the market turning due to the pandemic induced recession, average asking rates have shown their first significant dip (as of the closing of the third quarter of 2021). Still, it's a single movement over the past quarter and even with the dip average asking rates are still up on a year-over-year basis (average asking rates are up 18 cents from this time last year).

It should be noted that one of the reasons the drop has not been more significant is at the same time that companies are shedding space thru downsizing and subleases, there has been an elevated amount of new Class A construction deliveries. These new office projects delivered over recent quarters have continued to quote top of the market rates (typically in the mid \$40 range, as opposed to about \$30 mark for average Class A properties). Since the beginning of 2020, Class A office deliveries have totaled almost 5 million square feet.

This 5 million square feet of top end new Class A construction has basically been masking the decrease rates for older Class A and B properties. Historically, the delta between Class A and Class B properties has been about \$5 dollars per square foot. Currently, that number has widened to almost \$9 per square foot.

### DFW OFFICE ASKING RATES BY CLASS



Each property Class has its own dynamics, with Class A properties skewed the most, largely due to new construction deliveries. Still, the problem with averages in general is the wide variance individual properties can have from the norm. Even for Class B office properties, it is not uncommon for there to be a 40% variant either above or below the market average. This typically due to submarket dynamics, the age of the property and the property's amenities.

It would be remiss if the near record high amount of sublease space was not mentioned and its impact on average rates. In the past, one could make the argument that sublease space was an outlier, but with the sublease availability being made up of spaces of all shapes and sizes, some with short terms left and others with 10 years or more left, tenants looking for space have lots of viable options right now. These sublease rates certainly put downward pressure on rates. It is hard, however, to peg the exact discount beyond the 25% rate reduction because a high percentage don't quote asking rates.

The irony about asking rates is that even though they are one of the more complicated market measures to make sense of, they are one of, if not, the most important component to both tenants and landlords. As the market changes and companies refigure their size footprints, look for further significant movement ahead on rates. Every cycle is different, but with the past as a guide, we should see somewhere between a 7% to 15% drop-in rates as the market adjusts to current market dynamics.





# SUBMARKETS

SELECT SUBMARKETS	INVENTORY		VACANCY		NET ABSORPTION		COMPLETIONS		UNDER CONSTRUCTION	ASKING RENT
	# of Bldgs.	Total SF	Total SF	Rate	Current Quarter	YTD	Current Quarter	YTD	At End of Current Quarter	Wtd. Avg. (FSG)
Central Expressway	99	11,915,708	2,389,518	20.10%	9,927	-227,687	0	30,000	0	\$31.09
Dallas CBD	94	32,430,714	8,529,981	26.30%	73,755	-401,137	224,370	224,370	60,230	\$26.01
East Dallas	141	5,929,596	793,858	13.40%	24,790	103,306	0	372,741	472,495	\$28.35
Far North Dallas	439	58,656,535	13,891,427	23.70%	603,043	276,595	924,000	1,595,750	933,992	\$31.67
Fort Worth CBD	70	10,020,799	1,783,649	17.80%	-58,690	-143,823	0	0	0	\$27.67
Las Colinas	300	41,858,052	8,755,222	20.90%	-332,995	-765,279	0	261,805	906,000	\$25.82
LBJ Freeway	149	19,372,942	4,515,600	23.30%	-249,112	-442,890	0	0	0	\$23.91
Lewisville/Denton	129	5,650,962	860,708	15.20%	-287,671	-297,420	23,835	23,835	79,412	\$24.33
Mid-Cities	373	25,050,375	3,094,750	12.40%	182,680	256,823	0	32,058	806,998	\$23.28
North Fort Worth	51	3,744,460	119,781	3.20%	7,554	3,648	0	20,000	54,000	\$24.31
Northeast Fort Worth	52	3,809,734	266,243	7.00%	208,600	258,155	0	0	0	\$20.77
Preston Center	52	5,863,423	687,614	11.70%	-30,799	-60,671	0	0	688,368	\$38.17
Richardson/Plano	325	32,255,612	6,434,757	19.90%	-219,894	-208,564	98,772	130,240	652,717	\$23.50
South Fort Worth	178	10,163,311	1,497,661	14.70%	-44,520	-69,929	0	21,600	30,000	\$24.40
Southwest Dallas	75	3,734,134	563,852	15.10%	13,802	8,234	0	28,314	15,000	\$23.06
Stemmons Freeway	117	9,239,143	2,061,657	22.30%	100,039	58,509	0	0	65,000	\$19.93
Uptown/Turtle Creek	103	15,071,715	2,564,308	17.00%	14,630	-361,992	0	0	1,016,688	\$41.11
<b>TOTAL</b>	<b>2,747</b>	<b>294,767,215</b>	<b>58,810,586</b>	<b>20.00%</b>	<b>15,139</b>	<b>-2,014,122</b>	<b>1,270,977</b>	<b>2,740,713</b>	<b>5,780,900</b>	<b>\$26.90</b>
<b>CLASS A</b>	<b>575</b>	<b>161,111,793</b>	<b>35,437,234</b>	<b>22.00%</b>	<b>660,940</b>	<b>586,032</b>	<b>1,114,370</b>	<b>2,350,853</b>	<b>5,395,751</b>	<b>\$30.96</b>
<b>CLASS B</b>	<b>1,684</b>	<b>117,389,183</b>	<b>21,820,637</b>	<b>18.60%</b>	<b>-538,753</b>	<b>-2,369,140</b>	<b>156,607</b>	<b>389,860</b>	<b>385,149</b>	<b>\$22.23</b>
<b>CLASS C</b>	<b>488</b>	<b>16,266,239</b>	<b>1,552,715</b>	<b>9.50%</b>	<b>-107,048</b>	<b>-231,014</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>\$18.62</b>
<b>TOTAL DFW</b>	<b>2,747</b>	<b>294,767,215</b>	<b>58,810,586</b>	<b>20.00%</b>	<b>15,139</b>	<b>-2,014,122</b>	<b>1,270,977</b>	<b>2,740,713</b>	<b>5,780,900</b>	<b>\$26.90</b>

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





# OUR APPROACH

Hilltop Securities



# YOUNGER PARTNERS

**Y**ounger 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. Net absorption is a change in the occupied square feet from one quarter to another. For sublease space, negative absorption is only calculated if the tenant physically vacates the space.

When it comes to analytics, we focus not only on the data, but also the insight behind the data. Information and technology are continuing to progress to a level where data is readily available to everyone. However, conscious interpretation of this data is rare. We specialize in providing an astute understanding into market trends that are often overlooked.



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