

Q3 2021

DALLAS-FORT WORTH

OFFICE MARKET REPORT

DFW OFFICE MARKET SEES
POSITIVE DEMAND
SINCE ALMOST TWO YEARS AGO

TABLE OF CONTENTS

ECONOMIC CONDITIONS

- 4** Population
- 8** Employment

OFFICE MARKET CONDITIONS

- 10** Demand and Supply
- 14** Occupancy Trends
- 17** Rental Rate Trends
- 22** Submarkets

OUR APPROACH

- 24** Younger Partners

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

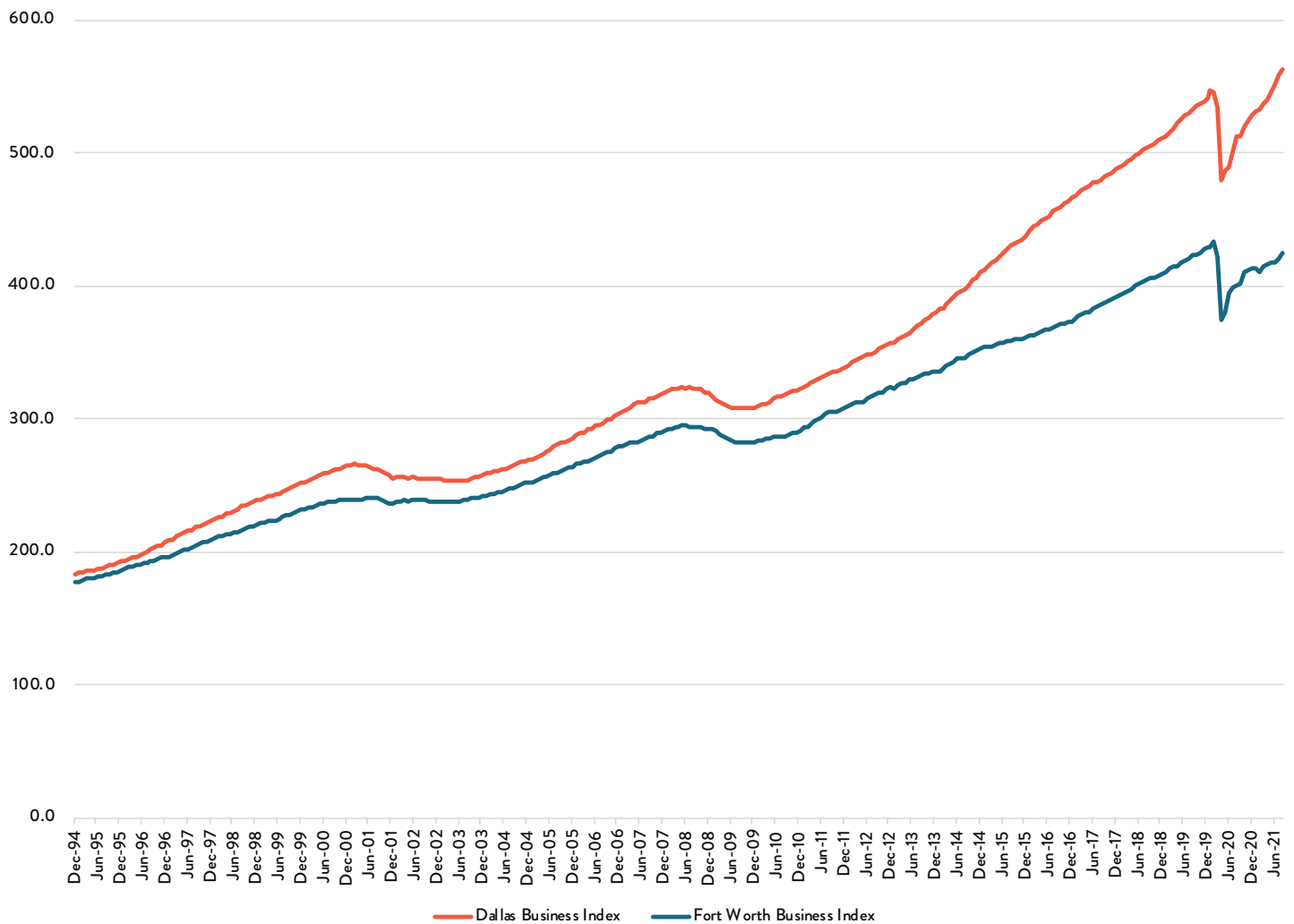
POPULATION

The 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.

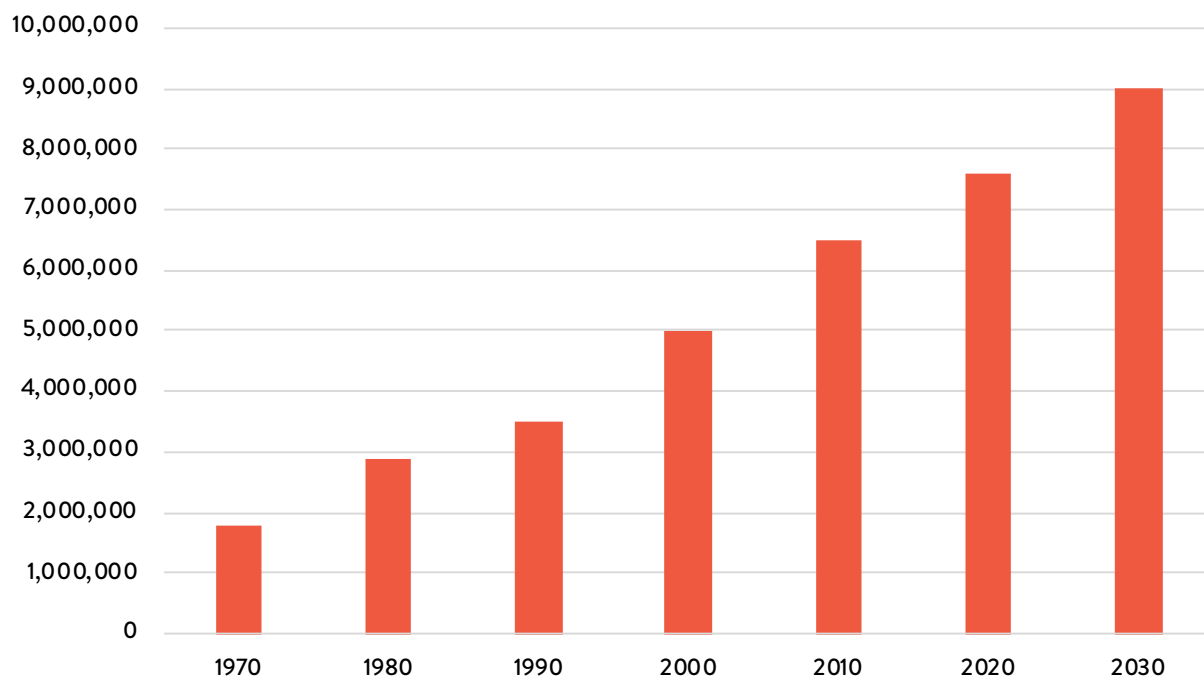
According to the Federal Reserve Bank of Dallas, the Dallas and Fort Worth business-cycle indexes (broad measures of economic activity) continued to expand in July, buoyed by recent job gains and unemployment rate declines. The Dallas index rose an annualized 14.3%, eclipsing its pre-pandemic peak and 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)



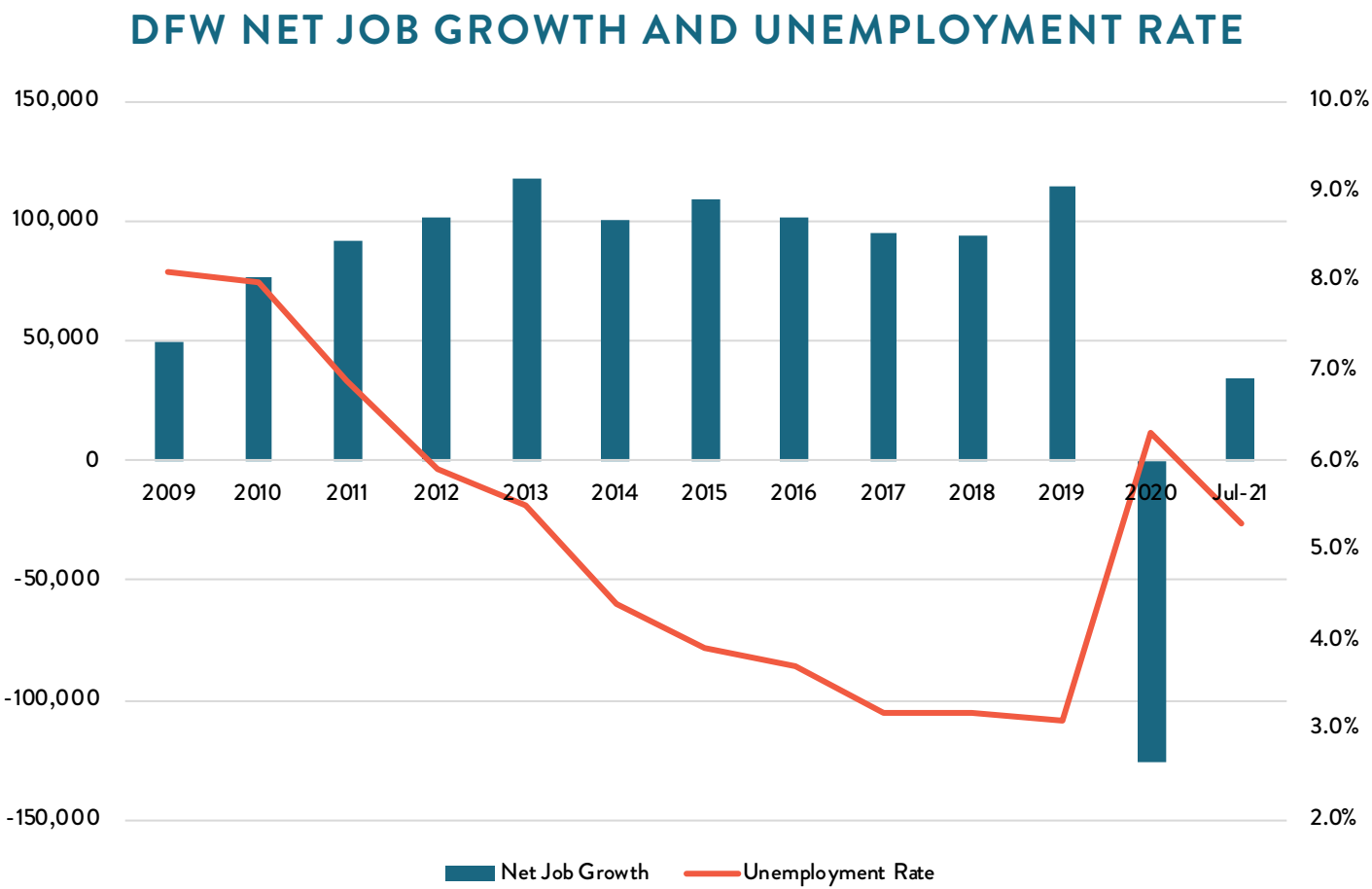
Longer term as more workers return to their workplaces, DFW's more affordable home prices, lower costs of living and tax advantages are expected to play a key role in high net migration to Dallas-Fort Worth. Companies and individuals from higher priced coastal markets like San Francisco, Los Angeles 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.

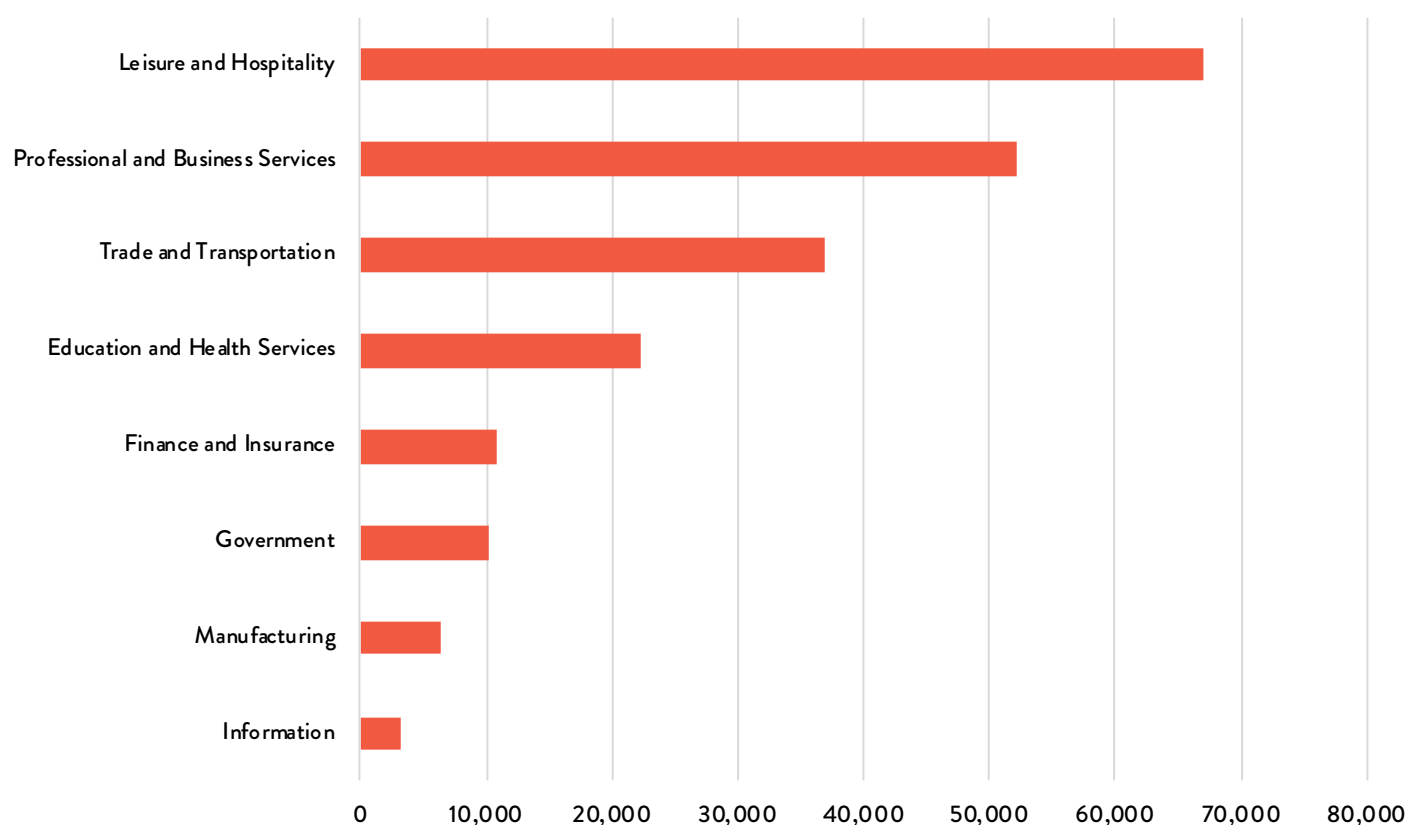


The unemployment rate in Dallas-Fort Worth, as of July 2021, stands at 5.3% and job growth has turned positive with 35,000 jobs through July 2021.

EMPLOYMENT

For 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

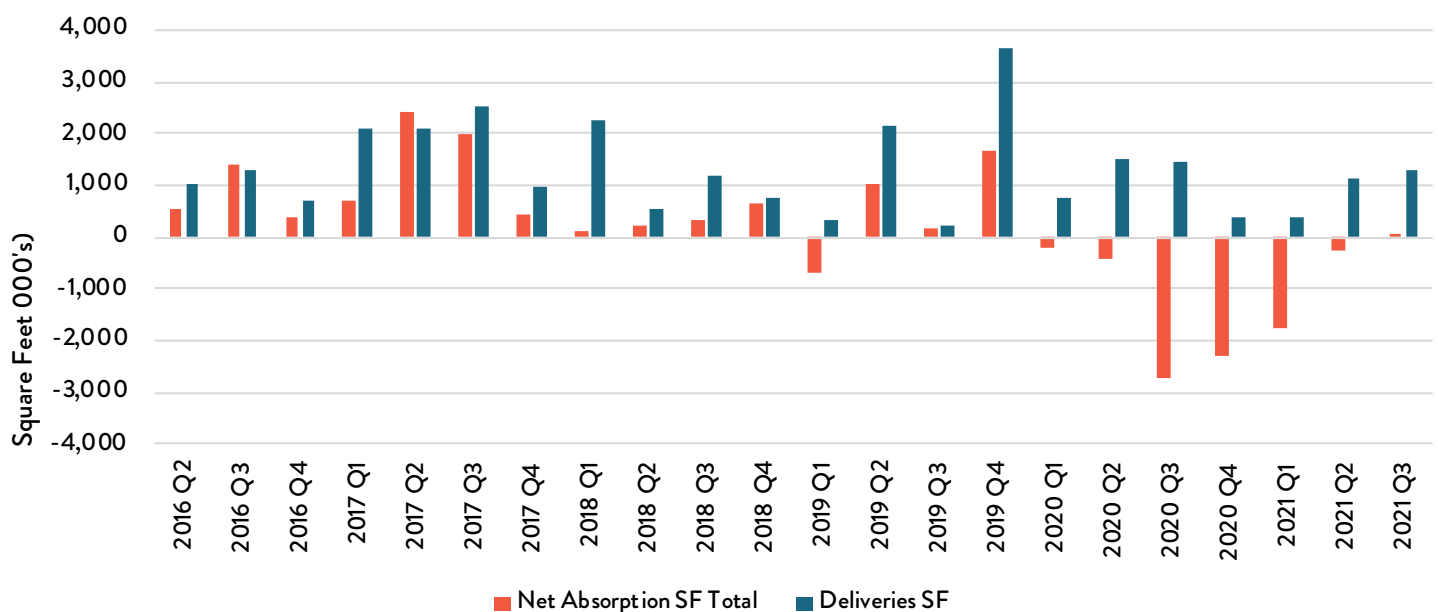


DEMAND & SUPPLY

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).

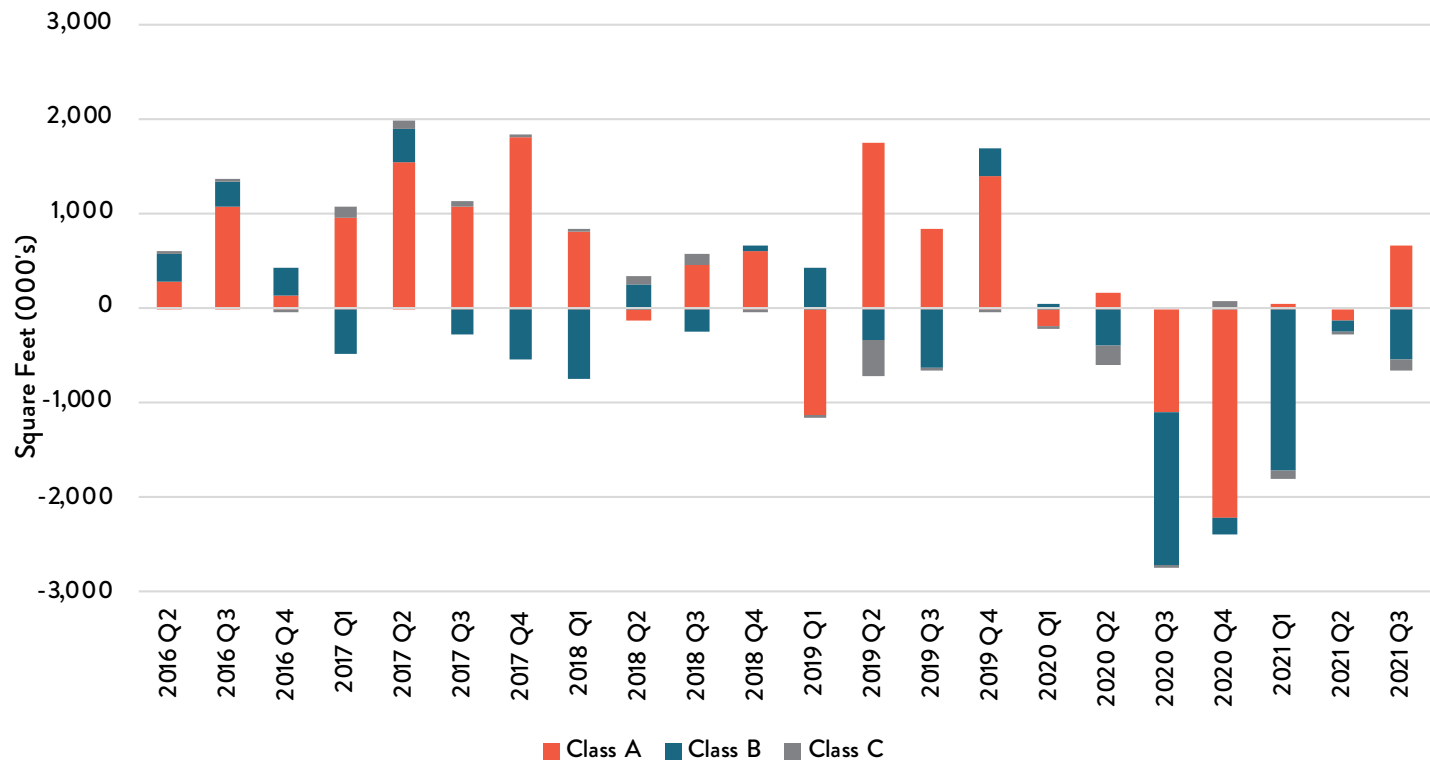
Overall, with 1.3 million square feet of new deliveries and limited positive net absorption, the total vacancy rate remained unchanged at 20.0%. The total vacancy rate is expected to increase slightly before the end of 2021. This is primarily due to 2 million square feet being delivered during Q4. A total of 5.8 million square feet is currently under construction.

NET ABSORPTION & DELIVERIES

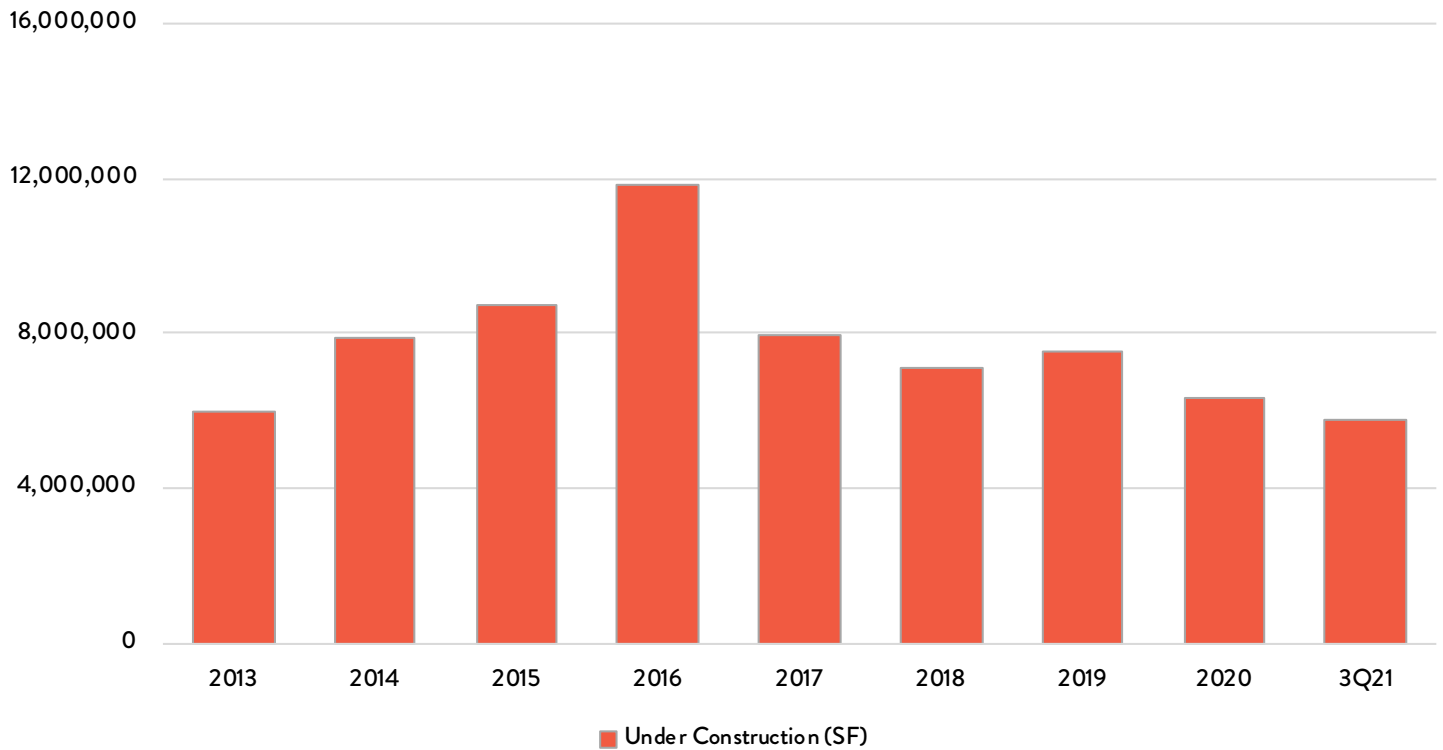


Absorption figures varied among the property classes in the third quarter of 2021. Class A properties recorded a positive 660,940 square feet, while Class B properties recorded a negative 538,753 square feet and Class C properties had a negative 107,048 square feet.

CLASS NET ABSORPTION



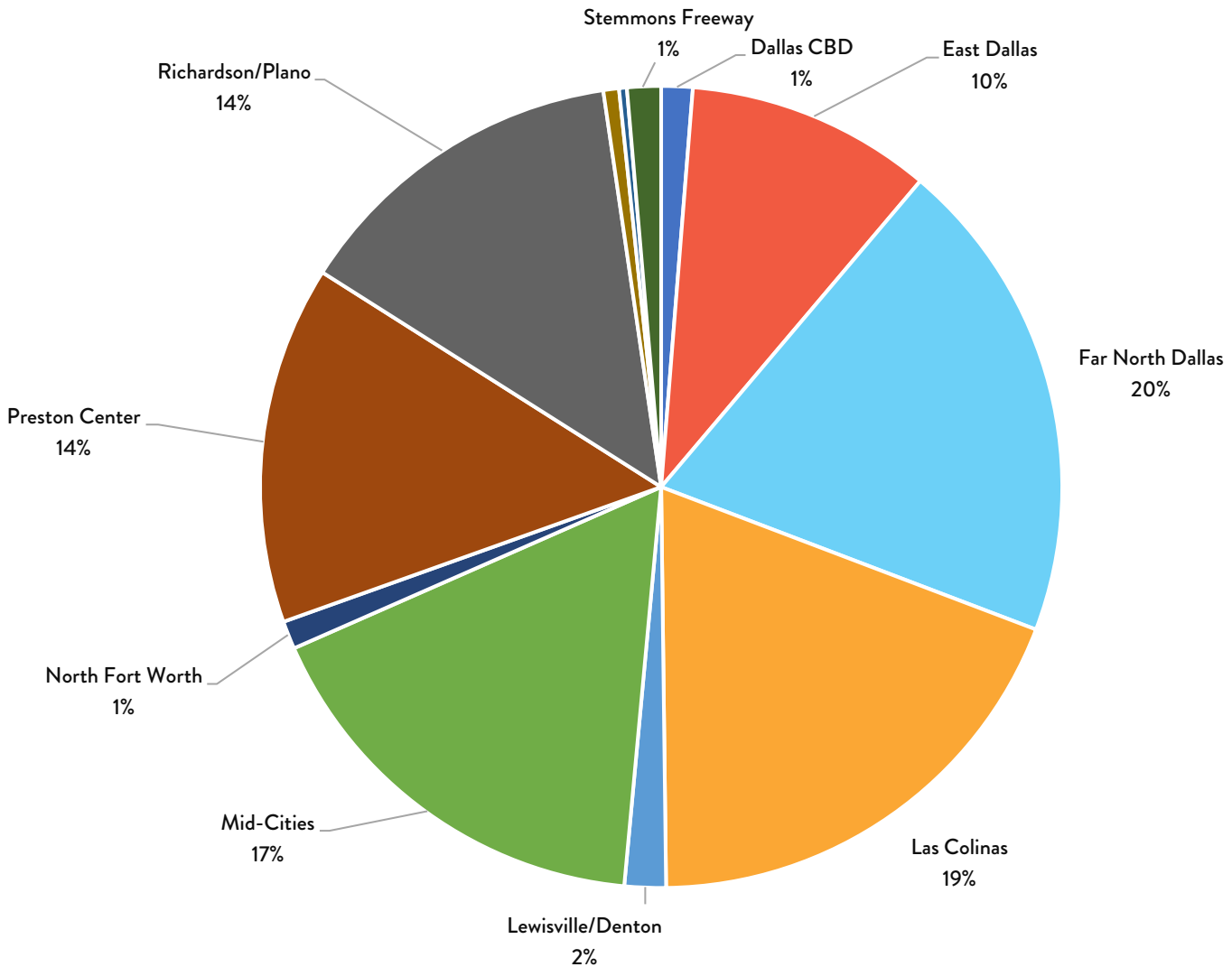
DFW NEW CONSTRUCTION



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)

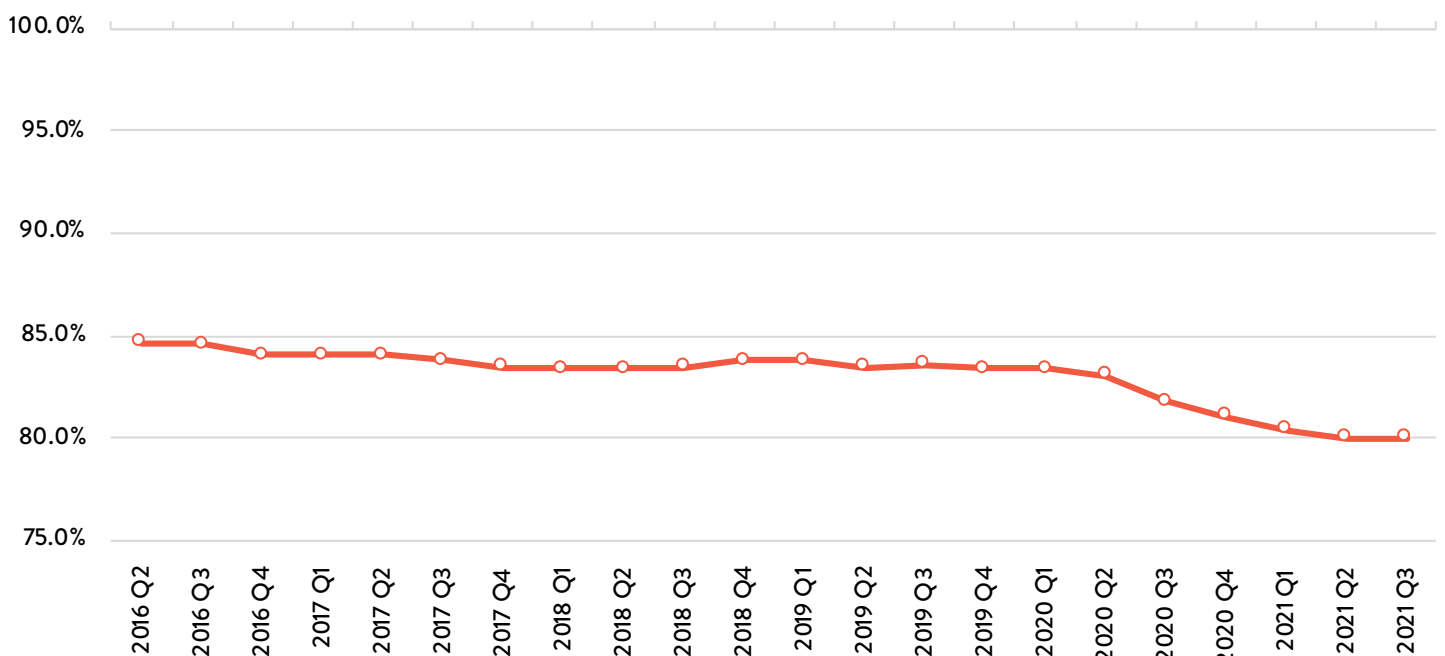


Far North Dallas leads the market in office projects currently underway (Reata Pharmaceuticals, The Star-Phase IV, The Parkwood and PGA Headquarters), followed by Las Colinas (Christus Health, Cypress Waters and Paycom).

OCCUPANCY TRENDS

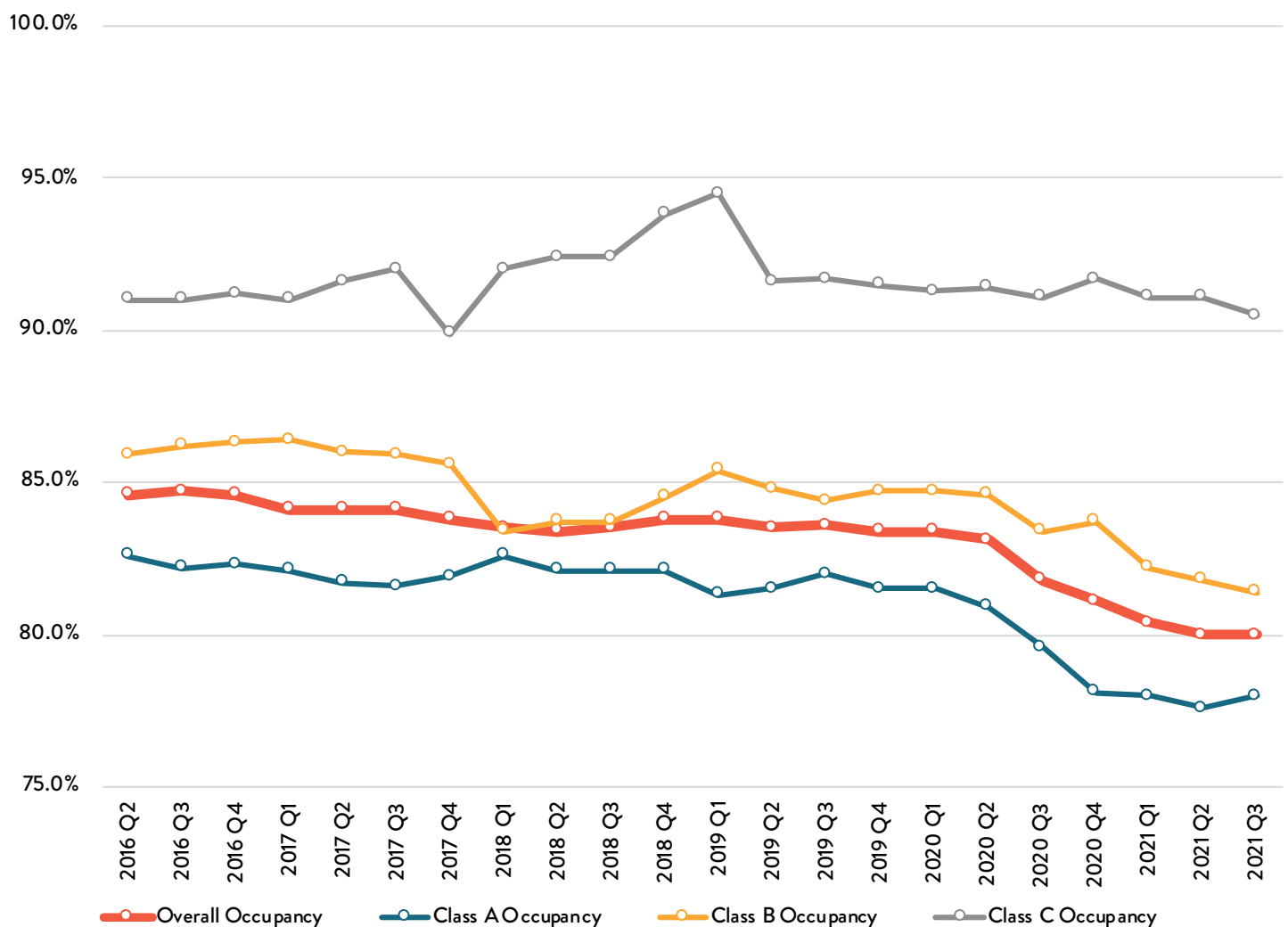
Overall occupancy remained unchanged for the quarter, with positive net absorption balanced by new construction deliveries. Most of the absorption over recent quarters has been in newly constructed properties, while older properties have largely languished. There are several older large office projects 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 foot 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

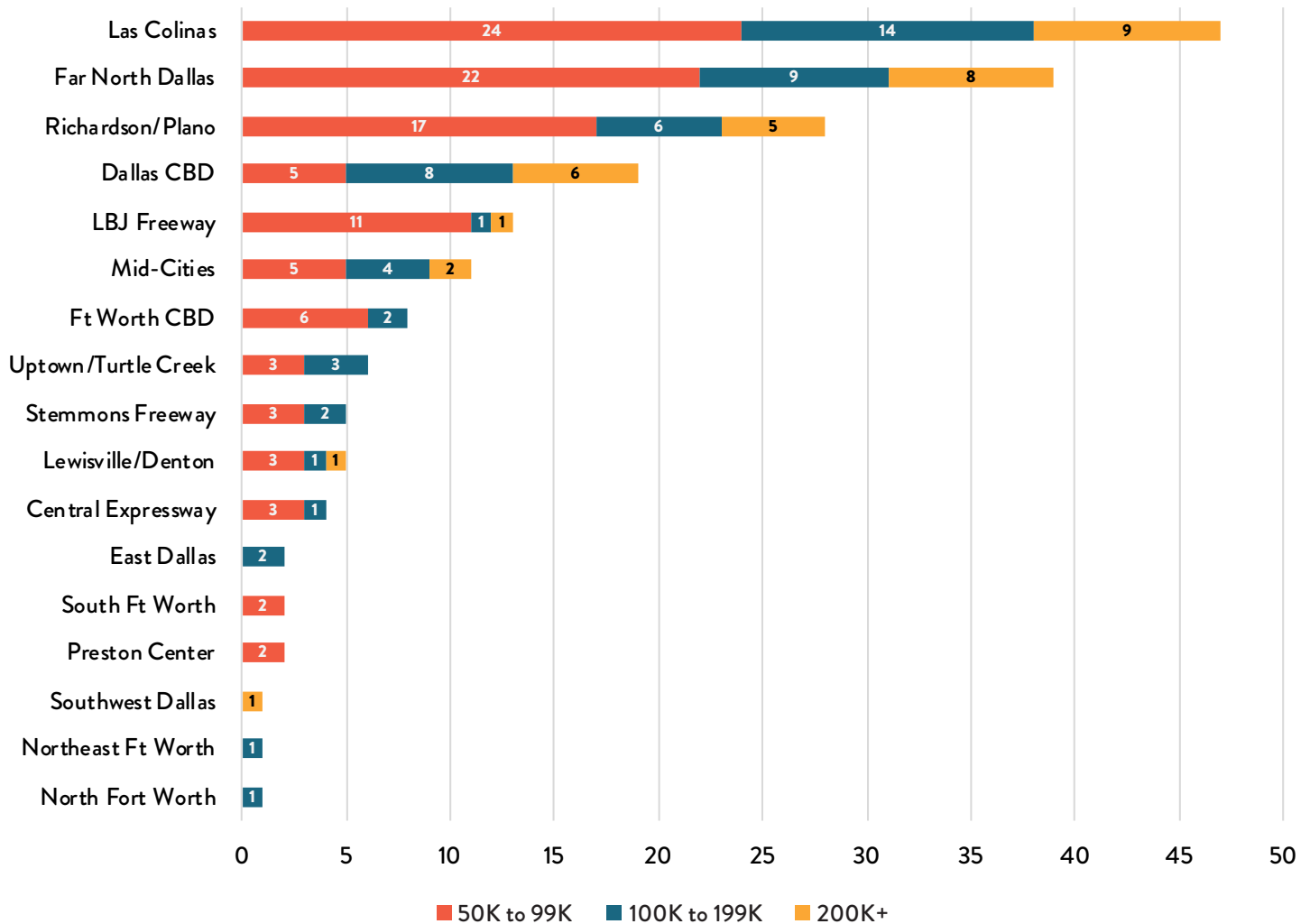


While newer construction should continue to perform well, there will be older properties that lose tenants and will likely have a hard time backfilling. Older second generation space will be challenging to lease. These facts, combined with record high sublease space, will put downward pressure on occupancy over the next few quarters.

CLASS OCCUPANCY



BIG BLOCKS OF SPACE

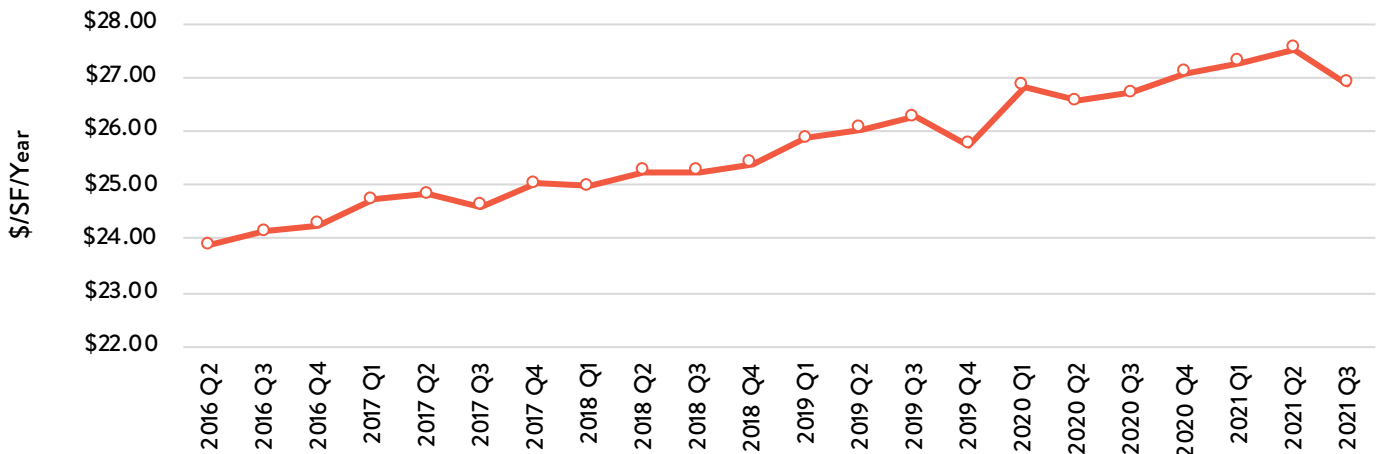


Despite the elevated levels of new construction over the past five years, one of the highest risks in the market is the amount of large blocks of second-generation spaces that will need to be backfilled (many of which were recently vacated for the large built-to-suit projects). As of September 2021,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

RENTAL RATE TRENDS

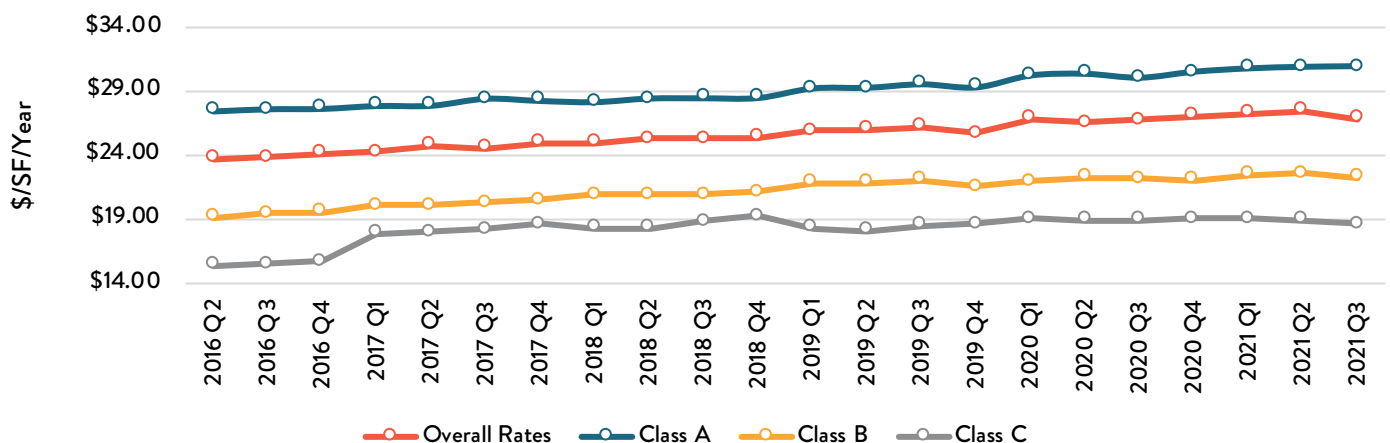
For the first time this cycle, quarterly average asking rates have decreased. Even with the decrease, rates are still up slightly year-over-year. Overall, the total weighted average asking rate is \$26.90 (FSG), which is up \$0.18 from the third quarter of 2020.

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.

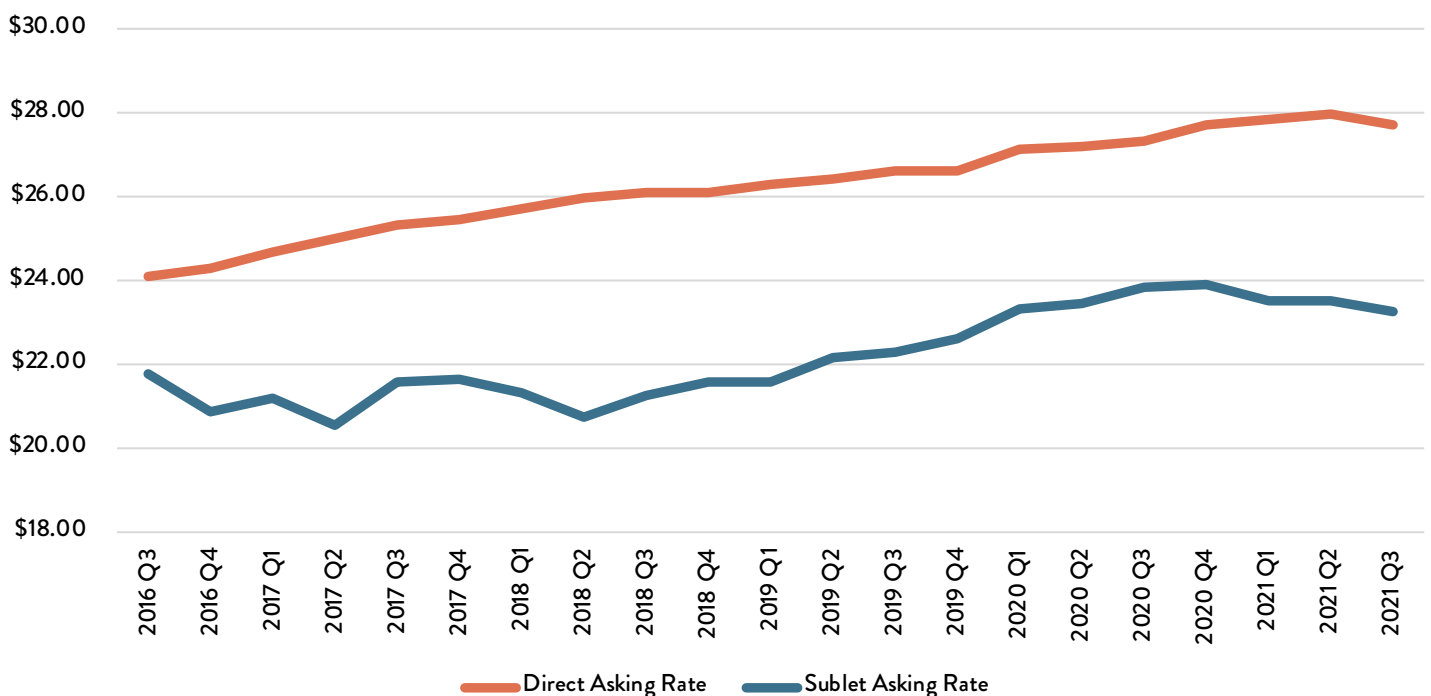
CLASS RENTAL RATES



RENTAL RATE INSIGHTS

A peculiar thing happens to office asking rates when leasing and tour activity grind to a halt, the movement in rental rates stagnates as well. Landlords are hesitant to lower asking rates until they feel like they are being eliminated from consideration by tenants actively touring the market. As a result, rates are a lagging indicator in comparison to other market statistics including 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, Dallas-Fort Worth and similar markets have experienced a muted response on the rental rate front. Overall, asking rates have remained stable while other market fundamentals have weakened due to increased availability and vacancies from tenants downsizing.

DFW OFFICE ASKING RATES (DIRECT AND SUBLEASE, FSG)



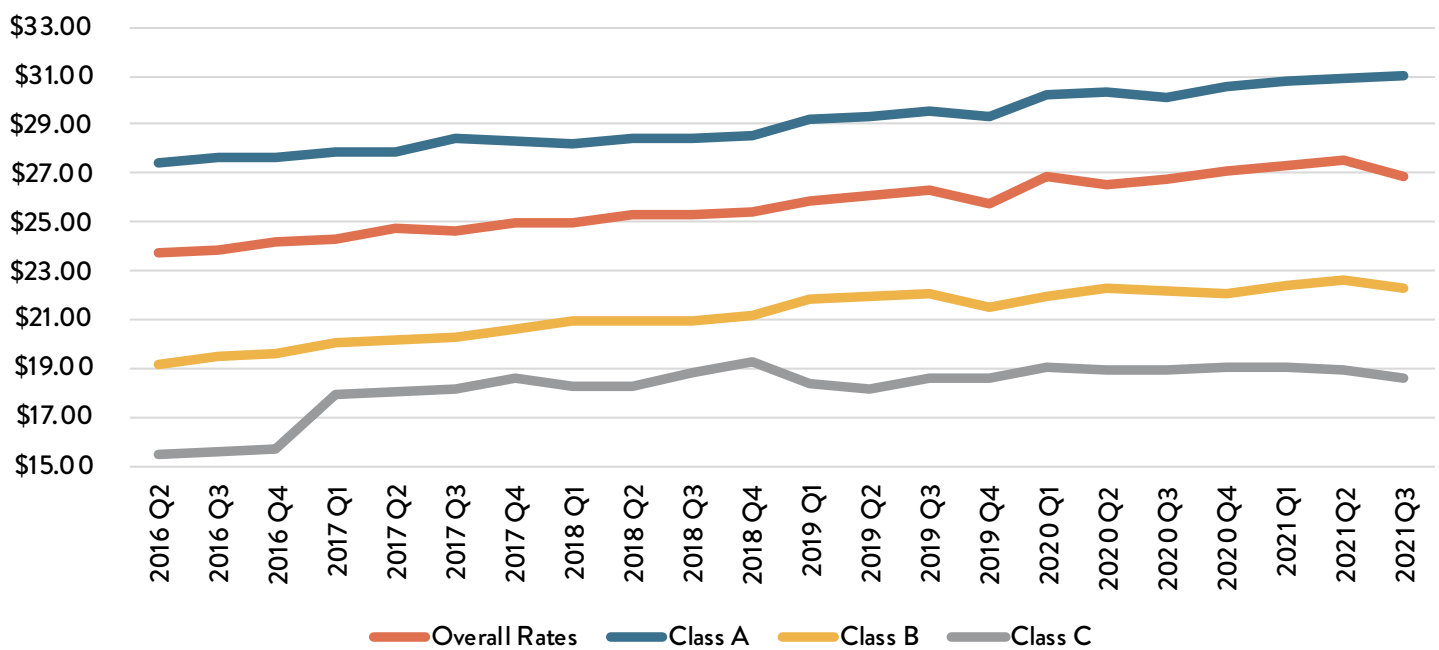
But as many other market experts have touched on in recent articles on the state of the market, the year and a half of sluggish activity and the markets are beginning to thaw. Tour activity has begun to pick up again, and with that, true data on rental rates is emerging.

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 through downsizing and subleases, there has been an elevated amount of new Class A construction deliveries. New office projects delivered over recent quarters have continue to quote top of the market rates (typically in the mid \$40 range, as opposed to \$30 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 decreased rates for older Class A and B properties. Historically, the delta between Class A and Class B properties hovered around \$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 is 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 as well as 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 remaining and others with 10 years or more, tenants looking for space have lots of a plethora of options available. Current sublease rates certainly put downward pressure on rates. However, it is difficult to peg the exact discount beyond the approximate 25% rate reduction because a high percentage of subleases do not 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 reconfigure their size footprints, look for further significant movement ahead on rates. Every cycle is different, but with the past as a guide, we should expect to see somewhere between a 7% to 15% drop in rates as the market adjusts to current market conditions.



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
TOTAL	2,747	294,767,215	58,810,586	20.00%	15,139	-2,014,122	1,270,977	2,740,713	5,780,900	\$26.90
CLASS A	575	161,111,793	35,437,234	22.00%	660,940	586,032	1,114,370	2,350,853	5,395,751	\$30.96
CLASS B	1,684	117,389,183	21,820,637	18.60%	-538,753	-2,369,140	156,607	389,860	385,149	\$22.23
CLASS C	488	16,266,239	1,552,715	9.50%	-107,048	-231,014	0	0	0	\$18.62
TOTAL DFW	2,747	294,767,215	58,810,586	20.00%	15,139	-2,014,122	1,270,977	2,740,713	5,780,900	\$26.90

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



OUR APPROACH

Hilltop Securities

YOUNGER PARTNERS

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. 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.



STEVE TRIOLET, DIRECTOR OF RESEARCH



YOUNGERPARTNERS.COM

214.294.4400

14643 DALLAS PARKWAY, SUITE 950
DALLAS, TX 75254

