

Dallas/Fort Worth

Office Market Research Report 2Q 2018

Market Overview

The Dallas-Fort Worth metro continues its healthy evolution into the next stage of the economic cycle. Payroll employment expanded at its fastest rate in a year and a half and unemployment dropped from 3.6% to 3.4% year over year, still below the national average which rose slightly back to 4.0%. Office leasing activity moderated in the year's first two quarters, no longer reaching the nation-leading demand, likely due to the tapering of corporate migrations that characterized the past few years.

Overall, the market remains healthy and much more durable than it has been in previous cycles. A combination of sustained job growth, reasonable construction, and single-tenant build-to-suit projects for large corporate users have kept vacancies at stable levels, still below the last cycle's low. Dallas is traditionally known for being over-built, but discretion has helped this period of growth set itself up to avoid many of the past cycle's pitfalls. Even as supply levels begin to crest, with a number of major spec projects delivering or set to deliver in the coming quarters, occupancies have barely taken a hit.

Looking ahead, the best years of the cycle are in the rear view mirror, but Dallas's cost of doing business and strong talent pool will position it to remain one of the most in-demand office markets in the country.

Market Facts



122,000

Jobs added in the last year, a 2.8% increase in employment.



3.4%

Unemployment in Dallas.



2.0%

12 Mo. Rent Growth



\$25.61

Average Gross Direct Rental rate

Dallas/Fort Worth Market Facts



318,618,783
Square Feet

16.4%
VACANCY

4,433,138 SF
12 MONTH ABSORPTION



Average Gross Asking Rents

\$29.28
CLASS A

\$21.32
CLASS B



8.7 MSF
UNDER CONSTRUCTION

3.6 MSF
YTD DELIVERIES

- Sustained job growth in office-using sectors has translated into some of the strongest demand in the country over the past three years, keeping vacancies below the last cycle's low.
- Dallas-Fort Worth's affordability, location, and quality of labor continue to draw major employers to the metro.

Parameters: Office | 20,000 sf+ | Existing

Bragging Rights/**In The News**

"#1 Best city for jobs 2 years in a row"
- ***Forbes***

"#1 Most business friendly city in America"
- ***Market Watch***

"#1 City for investing"
- ***PwC Emerging Trends***

"#1 City for starting a business"
- ***Kiplinger***

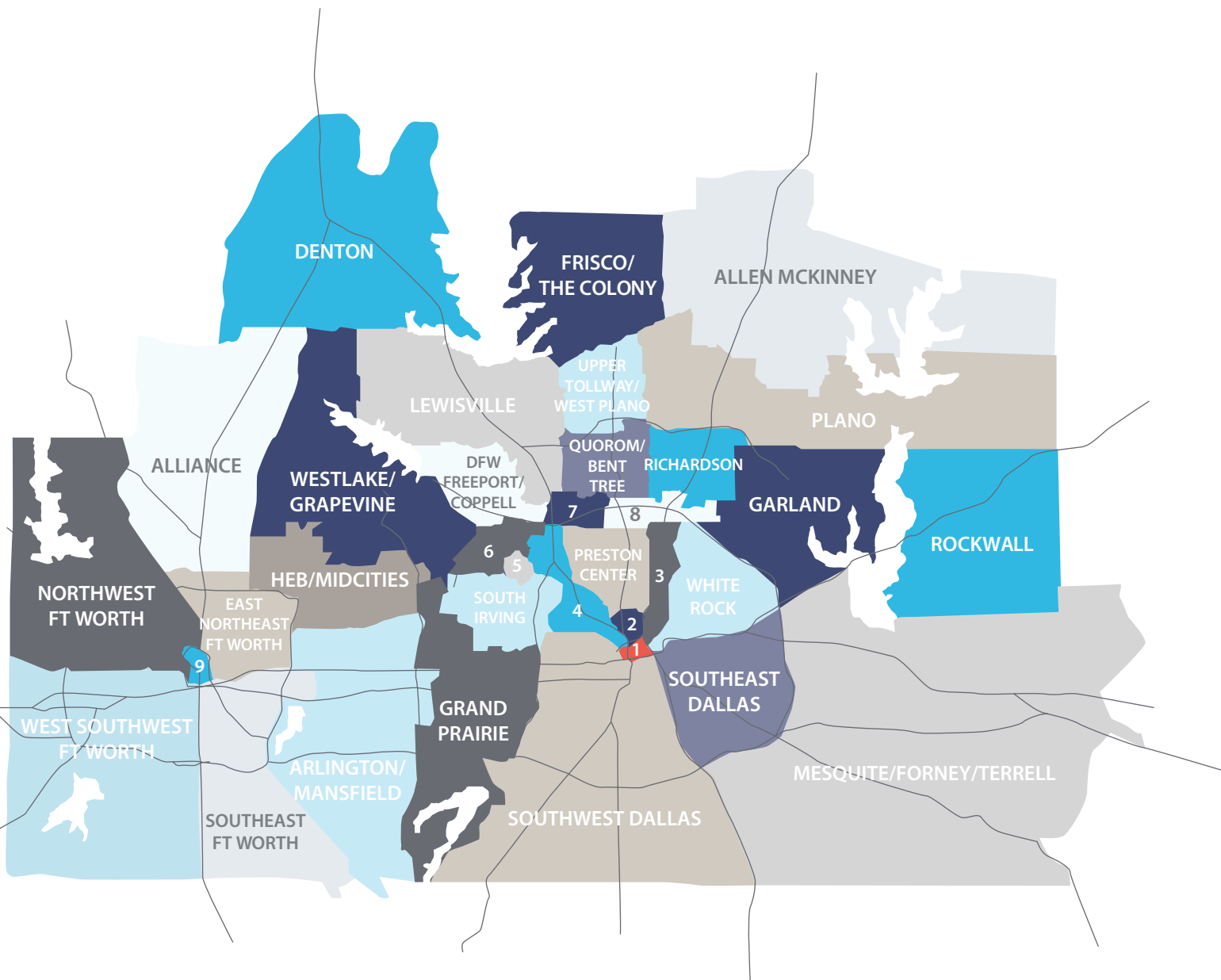
"#1 Pick for Amazon HQ2"
- ***Wall Street Journal***

"#1 Most family-friendly city in the US"
- ***Homes.com***

"#4 US's best economic powerhouses of 2018"
- ***Goldman Sachs***

"#1 Largest growing metro in US"
- ***Census Bureau***

The Market: Submarket Map



- 1 DALLAS CBD
- 2 UPTOWN/TURTLE CREEK
- 3 CENTRAL EXPRESSWAY
- 4 STEMMONS FREEWAY
- 5 URBAN CENTER/WINGREN
- 6 OFFICE CTR/WEST LBJ EXT
- 7 WEST LBJ FREEWAY
- 8 EAST LBJ FREEWAY
- 9 FT WORTH CBD

The Market: Core Submarket Overviews

Allen/McKinney



6,278,021
Square Feet



\$30.93
CLASS A

\$23.84
CLASS B

271,208 12 Mo. Net Absorption

10.5%
Vacancy

CBD



33,181,689
Square Feet



\$27.24
CLASS A

\$20.99
CLASS B

103,966 12 Mo. Net Absorption

22.8%
Vacancy

Central Expy



13,718,245
Square Feet



\$31.24
CLASS A

\$26.12
CLASS B

-57,259 12 Mo. Net Absorption

14.0%
Vacancy

Frisco/The Colony



5,990,932
Square Feet



\$34.64
CLASS A

\$26.84
CLASS B

203,773 12 Mo. Net Absorption

16.5%
Vacancy

Las Colinas



39,633,313
Square Feet



\$30.22
CLASS A

\$21.61
CLASS B

-264,567 12 Mo. Net Absorption

16.1%
Vacancy

LBJ Fwy



22,143,119
Square Feet



\$25.92
CLASS A

\$19.41
CLASS B

341,035 12 Mo. Net Absorption

20.7%
Vacancy

The Market: Core Submarket Overviews

Preston Center



5,578,676
Square Feet



\$40.49
CLASS A

\$29.14
CLASS B

68,991 12 Mo. Net Absorption

10.9%
Vacancy

Quorum/Bent Tree



22,293,809
Square Feet



\$29.40
CLASS A

\$20.79
CLASS B

-955,266 12 Mo. Net Absorption

22.4%
Vacancy

Richardson/Plano



28,943,498
Square Feet



\$27.67
CLASS A

\$19.92
CLASS B

426,611 12 Mo. Net Absorption

18.2%
Vacancy

Stemmons Fwy



14,891,729
Square Feet



\$18.57
CLASS A

\$16.44
CLASS B

424,221 12 Mo. Net Absorption

22.1%
Vacancy

Upper Tollway



30,796,114
Square Feet



\$34.60
CLASS A

\$25.28
CLASS B

3,170,725 12 Mo. Net Absorption

11.7%
Vacancy

Uptown



13,548,241
Square Feet



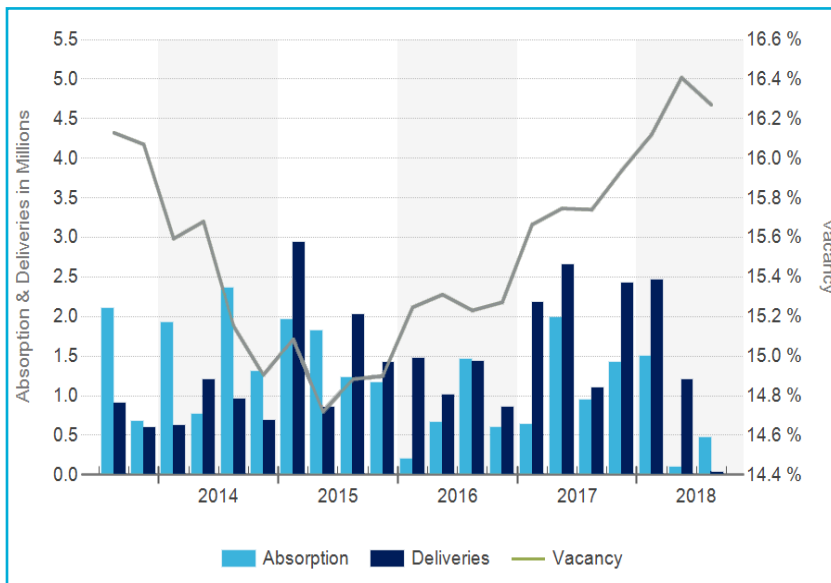
\$41.01
CLASS A

\$34.28
CLASS B

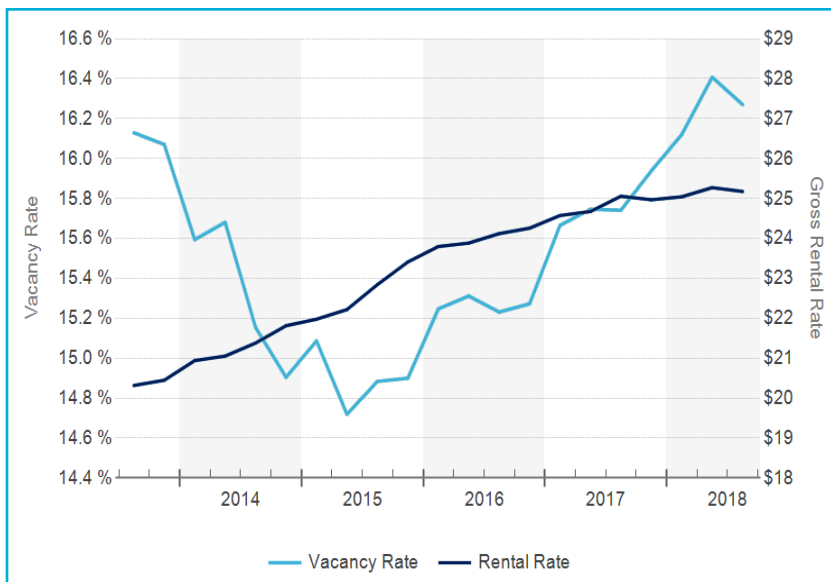
117,051 12 Mo. Net Absorption

11.1%
Vacancy

Vacancy Rate vs Sublease Vacancy Rate



Gross Asking Rent Per SF



Vacancy

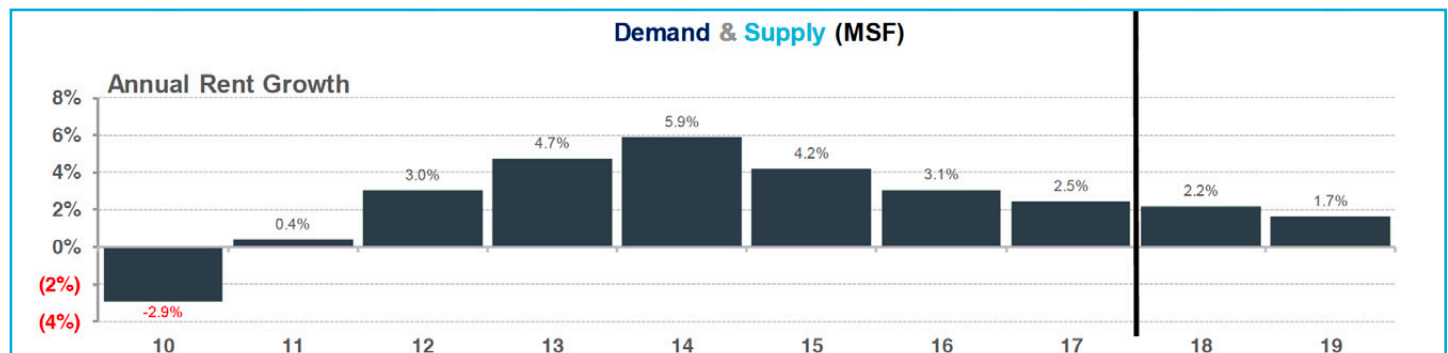
The Dallas/Ft. Worth Office market ended the first half of 2018 with a vacancy rate of 16.4%. In all, there was 52 msf vacant. The vacancy rate was up for Q1 and Q2, with year-to-date net absorption totaling positive 1,803,433 sf when single-tenant build-to-suits are included.

When those owner occupied build-to-suits are subtracted, the number drops to 401,630 sf for the year-to-date.

Vacant sublease space increased as well, ending the quarter at 3,762,623 sf. Once again, the majority of this is space vacated by large users moving to newer and/or owned spaces, but it is still worth noting as this is the largest amount of available sublease space in 15 years.

Rental Rates

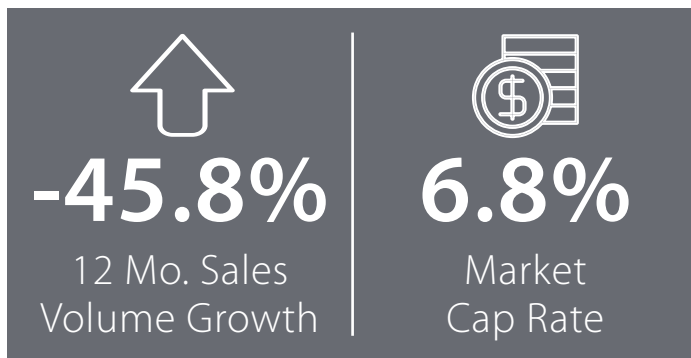
Rent growth slowed with the delivery of more speculative supply and a drop in leasing activity, causing more unleased space to arrive than in previous quarters, thus giving tenants more bargaining power. Rents remain about 15% higher than prerecession peaks. Premier submarkets such as Uptown/Turtle Creek, Frisco/The Colony, and Upper Tollway/West Plano saw the strongest growth, with rents now 20% greater than prerecession peaks.



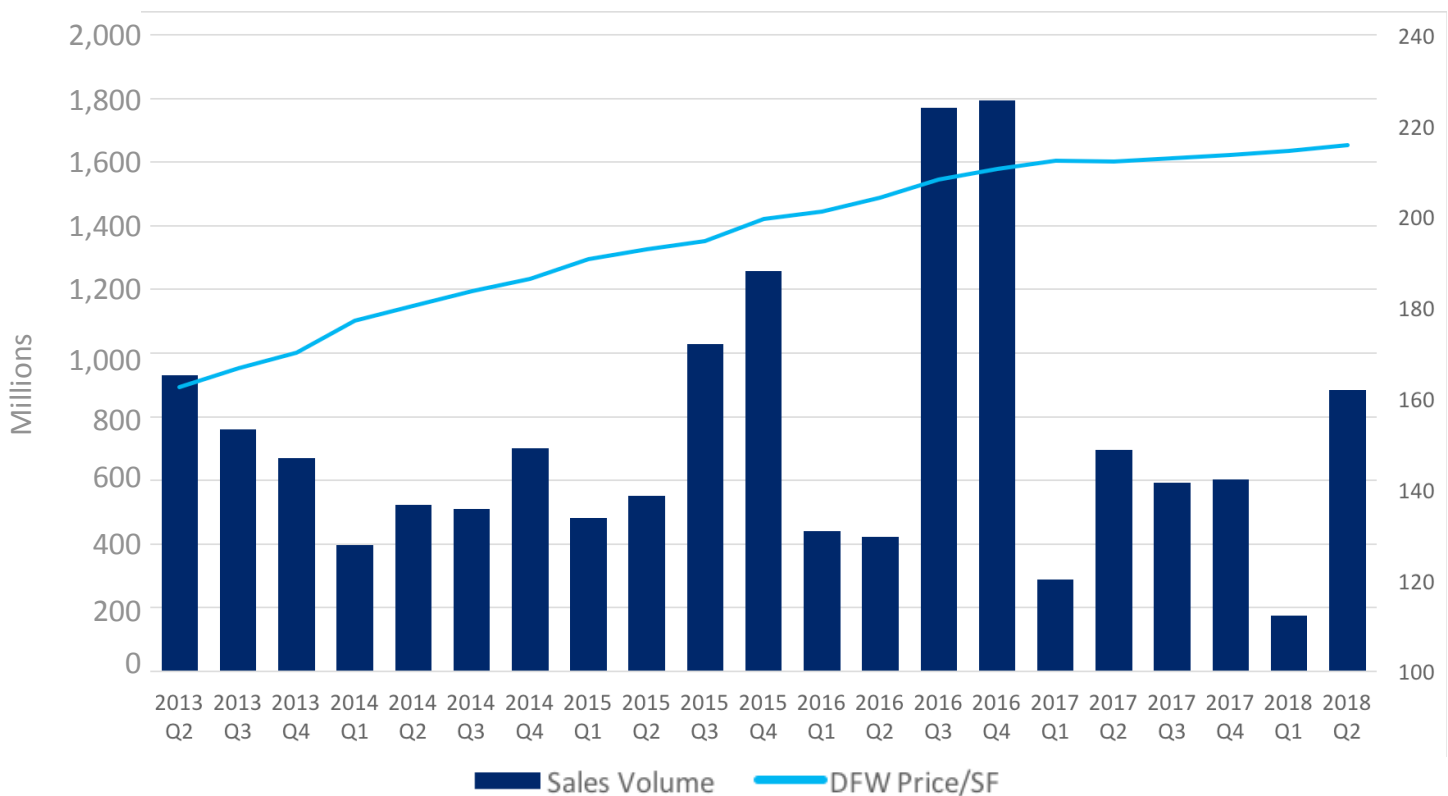
Investment Sales

Sales volume picked up for Q2 2018, with the average price per sf also gaining slightly to continue its historic climb. Dallas continues to draw capital attention from coastal markets such as Boston, New York, and San Francisco, which is coupling with continued demand for space by users, therefore driving prices up across the metroplex.

Turnover slowed in 2017, dropping from an average of roughly 35 million sf trading annually from 2012-2016, down to 26 million sf for 2017. Turnover picked up slightly in early 2018 though as nearly 2% of inventory traded in 18Q1. Infomart's sale in April is the major driver of 2Q, selling for \$800,000,000 at 1,600,000 sf for an average price per sf of \$500/sf.



| Period | Sales Volume | DFW Price/SF |
|---------|-----------------|--------------|
| 2018 Q2 | \$883,572,474 | \$215.81 |
| 2018 Q1 | \$174,463,236 | \$214.54 |
| 2017 Q4 | \$601,946,746 | \$213.56 |
| 2017 Q3 | \$592,203,825 | \$212.91 |
| 2017 Q2 | \$695,621,533 | \$212.13 |
| 2017 Q1 | \$289,186,684 | \$212.23 |
| 2016 Q4 | \$1,794,938,659 | \$210.50 |
| 2016 Q3 | \$1,771,741,674 | \$208.24 |
| 2016 Q2 | \$422,895,084 | \$204.11 |
| 2016 Q1 | \$440,189,965 | \$201.07 |
| 2015 Q4 | \$1,258,172,883 | \$199.43 |
| 2015 Q3 | \$1,028,055,182 | \$194.55 |
| 2015 Q2 | \$552,227,628 | \$192.76 |
| 2015 Q1 | \$482,418,414 | \$190.67 |
| 2014 Q4 | \$701,822,680 | \$186.34 |
| 2014 Q3 | \$510,181,647 | \$183.55 |
| 2014 Q2 | \$522,667,048 | \$180.38 |
| 2014 Q1 | \$395,490,762 | \$177.10 |
| 2013 Q4 | \$669,279,347 | \$170.11 |
| 2013 Q3 | \$760,650,333 | \$166.72 |
| 2013 Q2 | \$930,596,843 | \$162.47 |



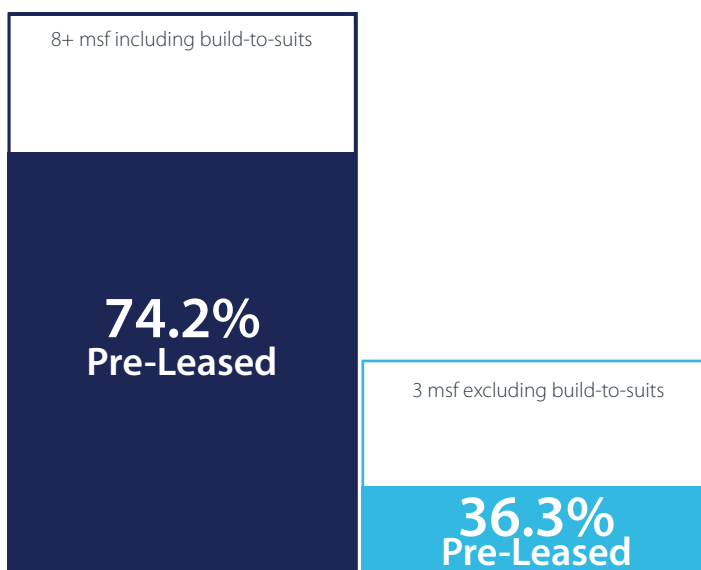
Absorption & Demand

While absorption slowed in 2016, it rebounded in 2017. However, most of that demand came in the form of build-to-suits: Absorption in multi-tenant office buildings in 2017 was less than half of what it was in 2016. Also, nearly all of the net absorption in 2017 came in upper B and A class assets, signifying a strong flight-to-quality effect. This is coupled with the "Aging-out" effect that dated properties are seeing as more tenants are focusing on new built spaces instead of 70's and 80's era product.

Regardless, the demand outlook looks bright. Moody's Analytics projects that D-FW will generate some of the strongest office-using employment growth in the country, and spec projects in high-demand areas like Frisco and Legacy, Las Colinas, and Uptown should give marquee tenants plenty of options.

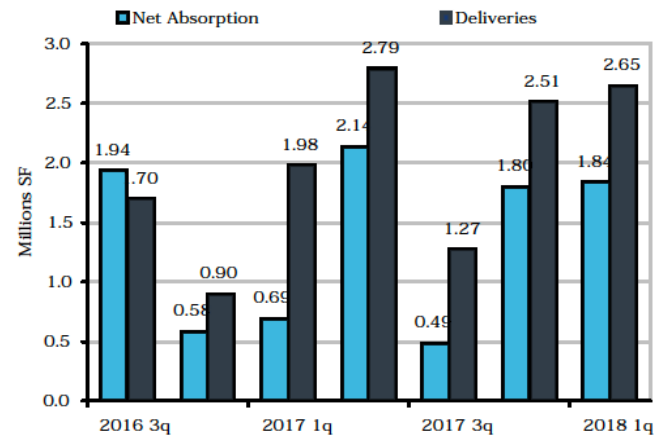
Of the 8+ msf currently under construction, including single tenant build-to-suits, the availability rate stands at 25.8%.

When those owner-occupied build-to-suits are removed, this number jumps to 63.7% availability for the roughly 3 msf underway. Also, as of Q2 2018, there is 4 msf of multi-tenant office space available that either was built since the beginning of 2017 or is under construction. Therefore, some additional softness in the market could be expected over the next few quarters.



Absorption & Deliveries

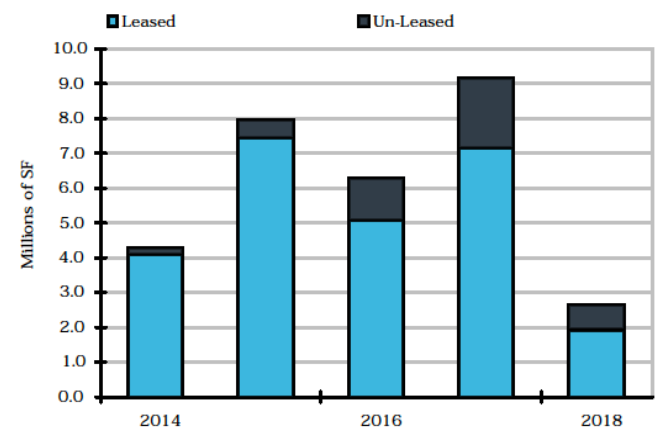
Past 7 Quarters



Source: CoStar Property®

Recent Deliveries

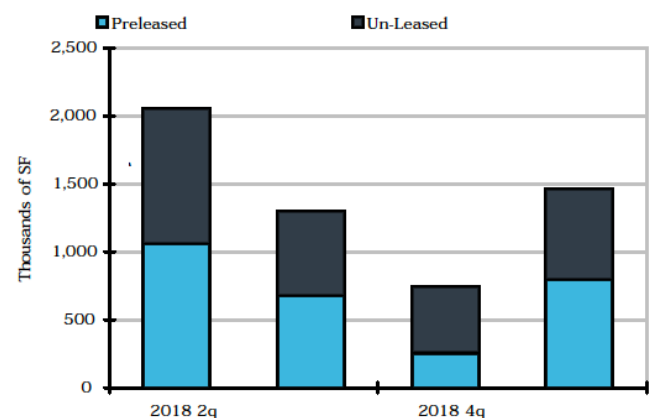
Leased & Un-Leased SF in Deliveries Since 2014



Source: CoStar Property®

Future Deliveries

Preleased & Un-Leased SF in Properties Scheduled to Deliver



Source: CoStar Property®

Making Cents Of It All

Averages of 1,000+ SF Leases for Q2 2018

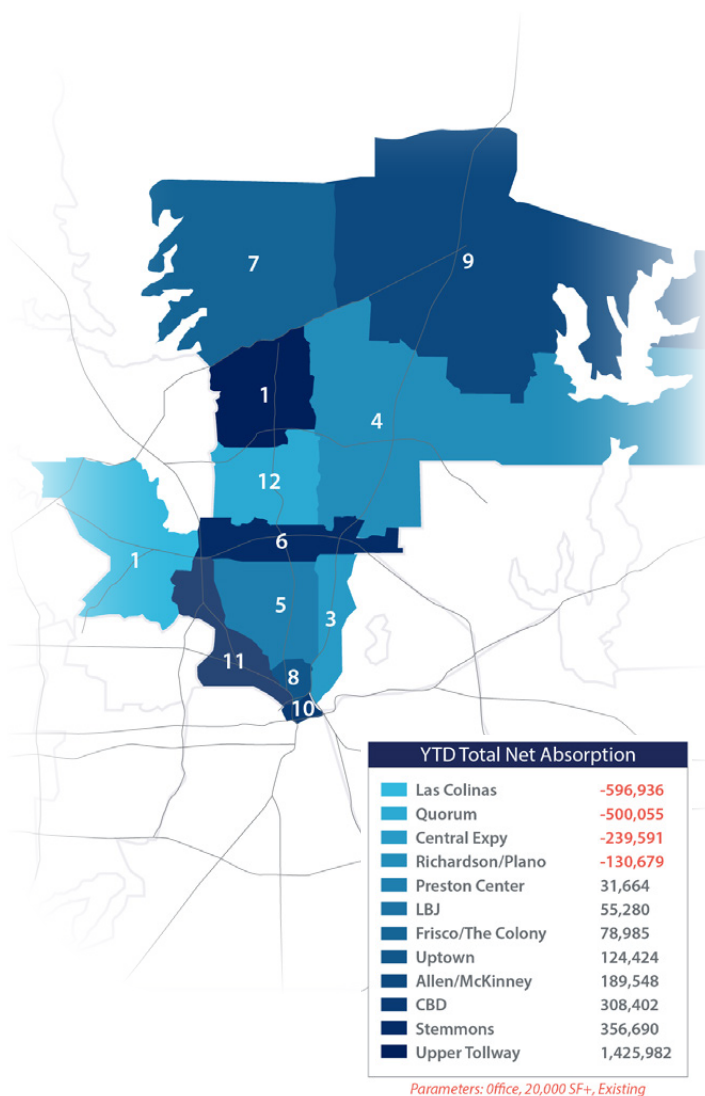
| Rents Per SF | Survey | Low | High |
|----------------------|---------|--------|---------|
| Gross Asking Rent | \$25.36 | \$4.75 | \$60.49 |
| Gross Starting Rent | \$20.78 | \$6.00 | \$50.09 |
| Gross Effective Rent | \$19.36 | \$6.00 | \$37.80 |

| Concessions | Survey | Low | High |
|----------------------|--------|--------|---------|
| Months Free Rent | 0.1 | 0.0 | 2.0 |
| TI Allowance Per SF | \$3.34 | \$0.00 | \$40.00 |
| Concessions | - | - | - |
| Asking Rent Discount | 1.6% | -61.5% | 50.6% |
| Annual Rent Increase | 2.0% | 2.0% | 2.0% |

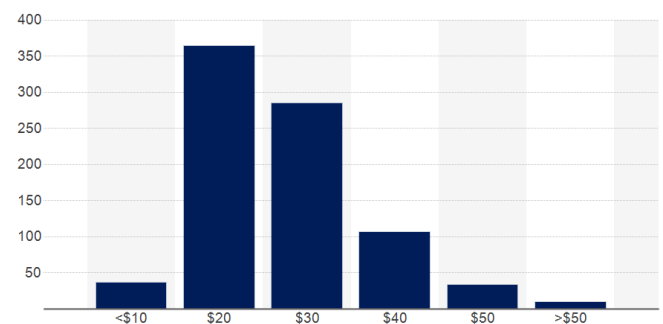
| Volume | Survey | Low | High |
|-----------------|------------|-------|-----------|
| Deals | 932 | - | - |
| SF Leased | 4,751,123 | 1,000 | 250,000 |
| Average Deal SF | 5,097 | 1,000 | 250,000 |
| Buildings | 659 | - | - |
| Building SF | 73,514,423 | 1,150 | 1,849,729 |

| Time on Market | Survey | Low | High |
|-----------------------|--------|-----|-------|
| Months on Market | 10.5 | 0.0 | 217.3 |
| Months Vacant | 10.0 | 0.0 | 219.6 |
| Average Term in Years | 0.7 | 0.1 | 10.2 |

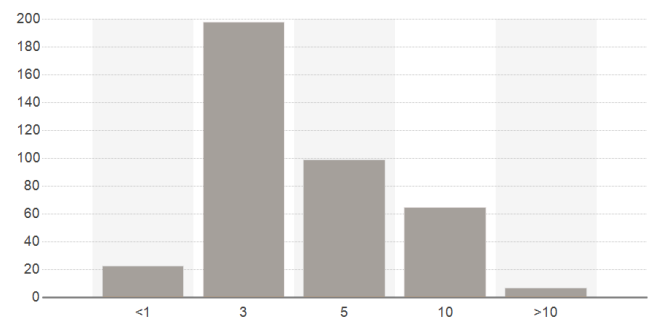
YTD Net Absorption for Core Dallas Submarkets



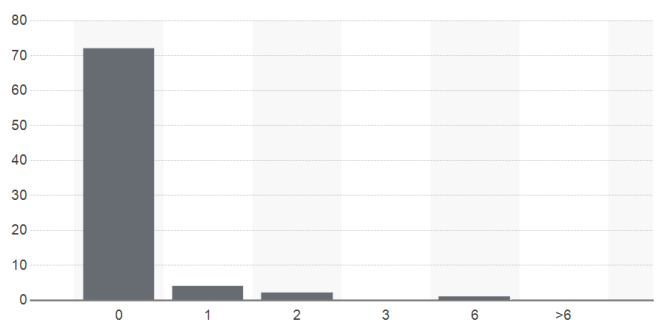
Deals by Gross Direct Rent



Deals by Lease Term in Years

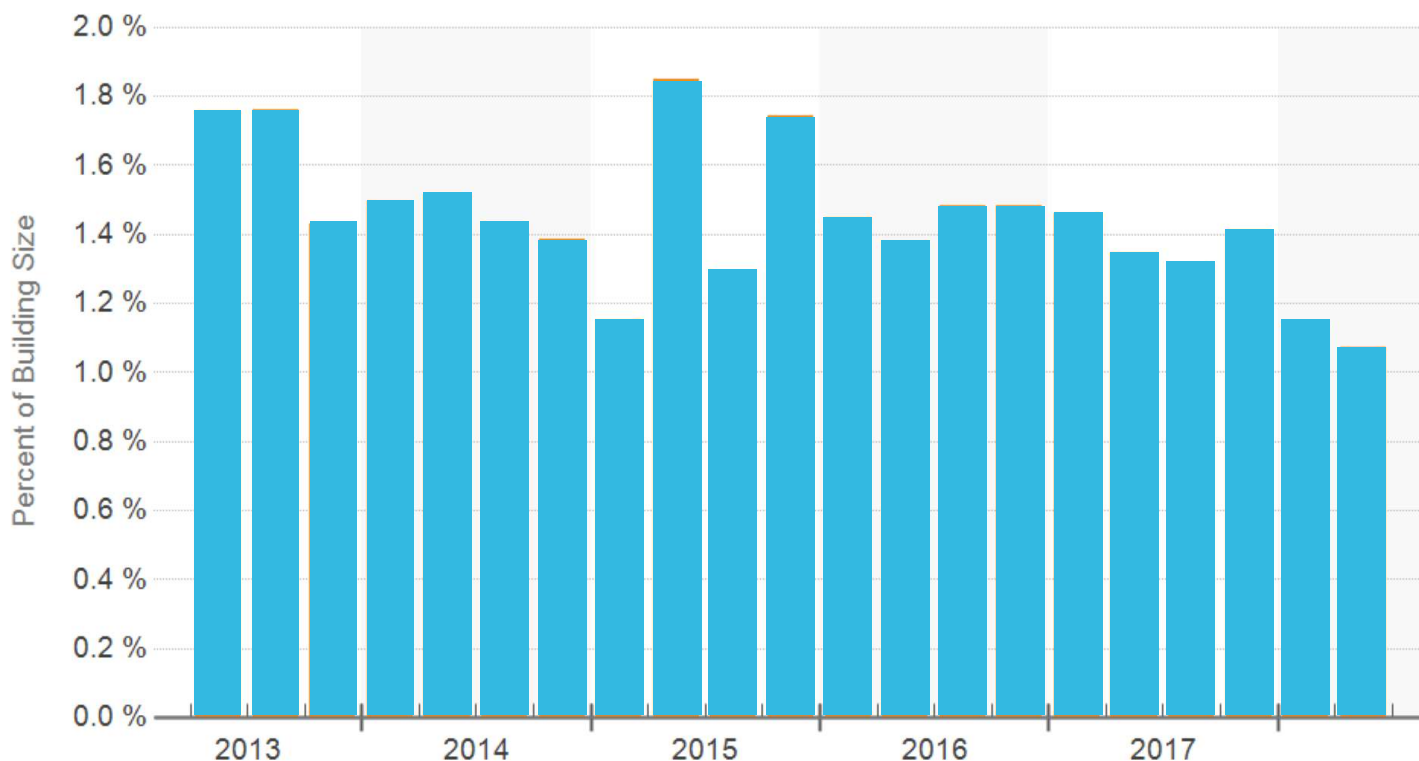


Deals by Months of Free Rent (Reported)



Leasing Activity

Leasing activity remains active though slightly lower than previous years for 2Q 2018. Activity has averaged around 1.4% of total building size over the past five years, with both 2018 quarters so far performing lower than previous quarters. In all, 2018 has seen 4,152,857 SF of year to date leasing.



Top Leases

| Address/Complex | Tenant | Size (sf) | Deal Type |
|-----------------|----------------------|------------|-----------|
| Cypress Waters | Nokia | 350,000 sf | New |
| Legacy Central | Samsung | 216,000 sf | New |
| One Arts Plaza | Thompson & Knight | 180,000 sf | New |
| Galatyn Commons | Steward Health Care | 165,300 sf | New |
| Pinnacle Tower | Guidestone Financial | 112,825 sf | New |

Trends to Watch



Workplace Strategies

Smaller, more thoughtful spaces will reduce space requirements and deal sizes.



Coworking

Flexible alternatives such as coworking continue to grow in demand.



Supply Drop

Tariffs, rising borrowing costs, and concerns of a looming slowdown may cause the cycle's pipeline to pump the breaks.

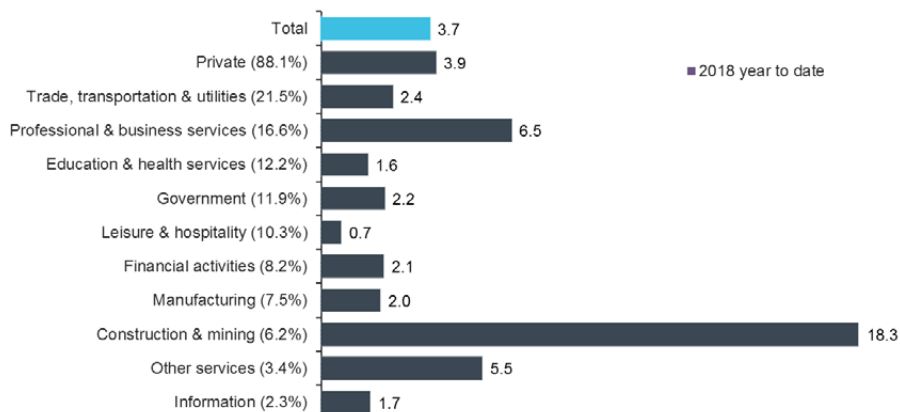
Economic Outlook

According to the Federal Reserve Bank of Dallas, the Dallas/Fort Worth metro continued its strong expansion. Job growth stands at a 3.5% annualized rate versus the US average of 1.6%, with the metroplex already adding over 60,000 net new jobs. Unemployment remains near record lows, pushing the area closer to peak employment. Wage growth is steady at 3.2% and home price increases continue to climb but have slowed to 6.6% year over year growth.

Another positive for DFW is that its employment base is arguably the most diverse it has ever been. This is shown in its employment gains, with every major sector reporting growth for 2018 year to date.



Employment Growth by Sector



NOTES: Data show seasonally adjusted annualized percentage growth by sector December 2017–May 2018. Numbers in parentheses are shares of total Dallas–Fort Worth nonfarm employment in May 2018 and may not sum to 100 due to rounding.

SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; seasonal and other adjustments by the Dallas Fed.



Dallas has 22 Fortune 500 companies located in the metro, up from 18 in 2014.



All economic sectors reported growth in the last 12 months, with Professional & Business Services (5.2%), and Leisure and Hospitality (4.9%) leading the way.



In the latest population estimates provided by the U.S. Census Bureau, the DFW area was ranked as the second fastest-growing metropolitan area in the U.S.



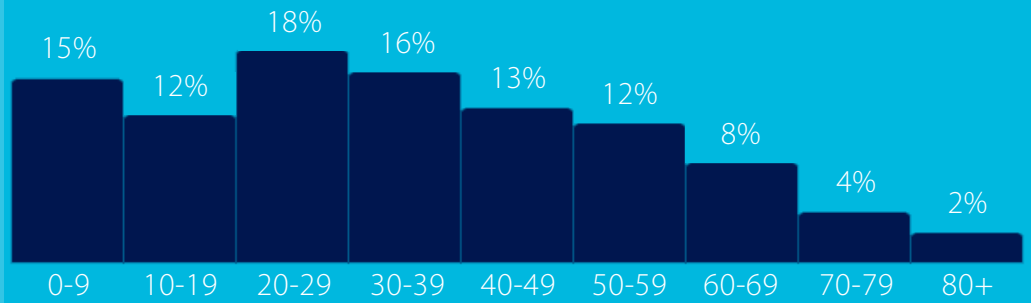
Total nonfarm employment in the Dallas-Fort Worth-Arlington Metropolitan Statistical Area stood at **3,707,500** in May 2018, up **122,000** over the year.

Metro Area Demographics

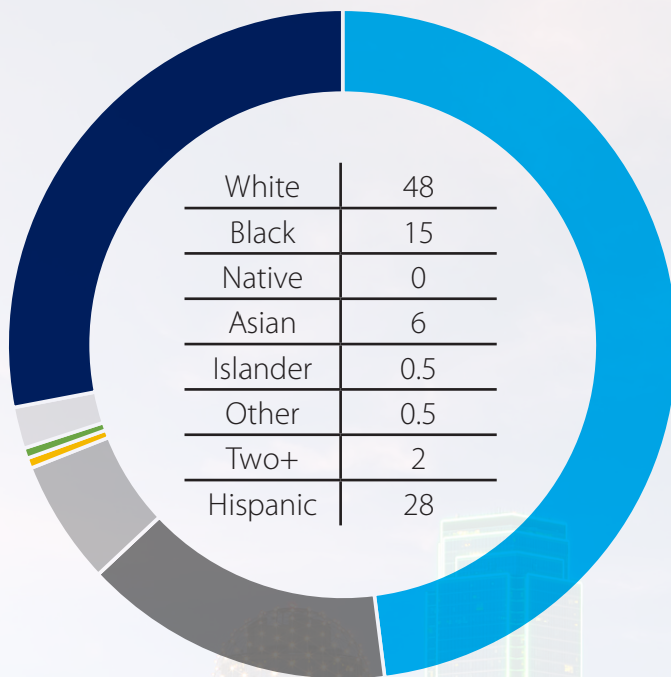


34.8

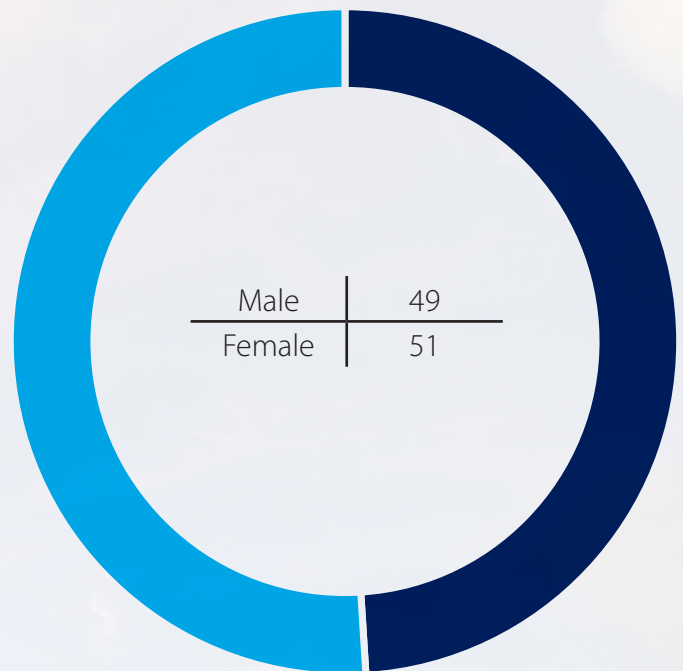
Median Age



Source: Census.gov



■ White ■ Black ■ Native ■ Asian ■ Islander ■ Other ■ Two+ ■ Hispanic



■ Male ■ Female



\$63,812

Median household
income



27.8

Mean travel time
to work in minutes



2,538,547

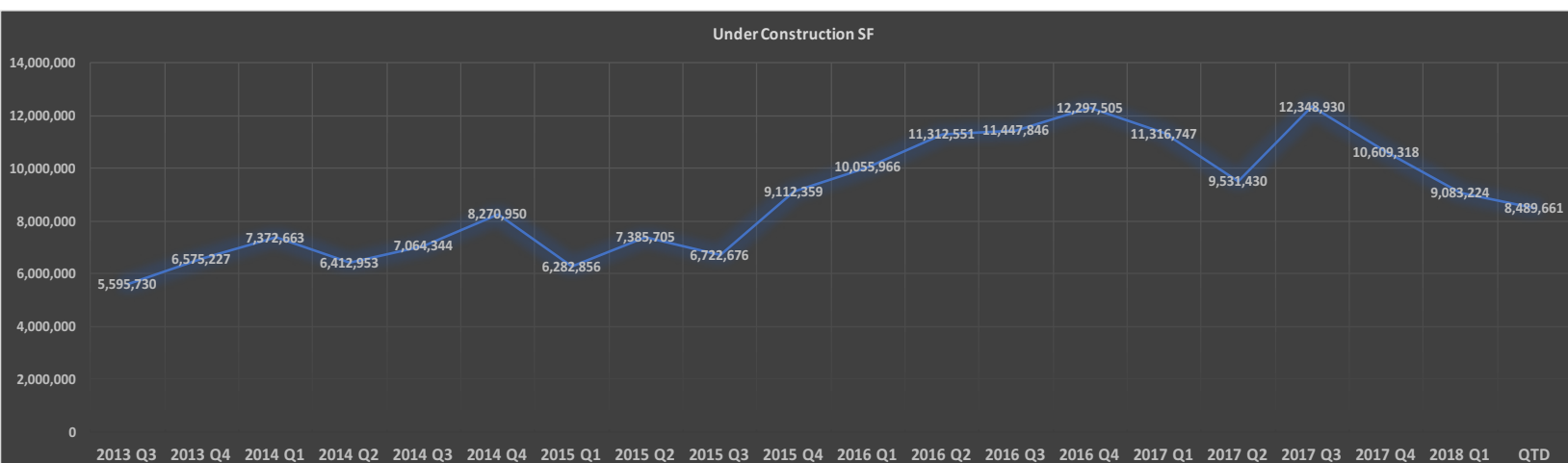
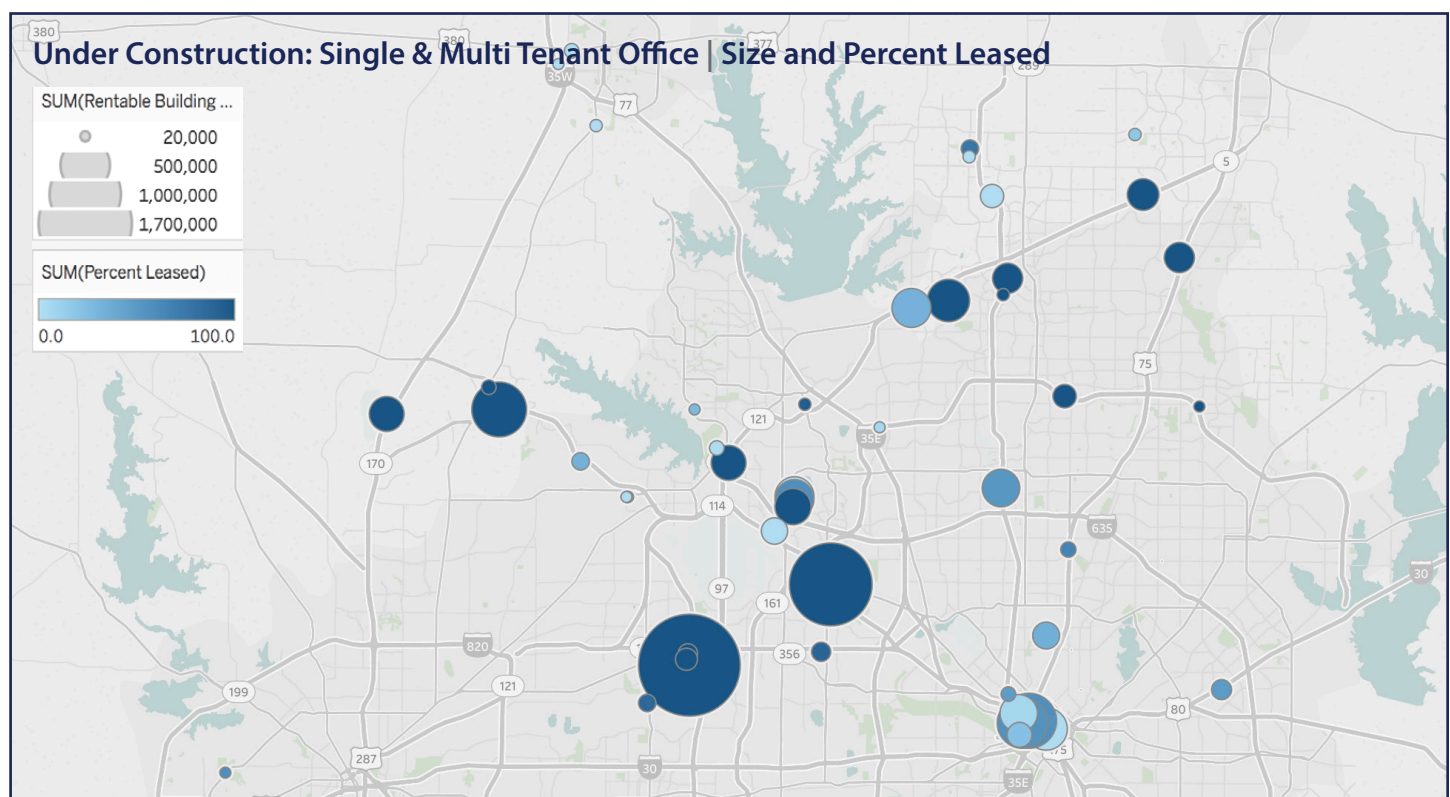
of
Households

Construction Pipeline

Impressive employment gains and corporate relocations have continued to drive construction activity through the cycle. Liberty Mutual delivered its 1,100,000 sf facility in 1Q 2018 and is now fully occupied. Several recent deliveries remain vacant however. Hall Park - T2, a 300,000 sf 1Q delivery, is 100% vacant, as is 3400 CityLine in Richardson, also a 300,000 sf property. Major deliveries for the remainder of 2018 will bring the year's total to roughly 7 msf.

During the first half of 2018, 21 buildings totaling 3,692,091 sf were completed in the Dallas/Ft. Worth market area. This compares evenly with the 56 buildings that completed in 2017 for 8,354,681 sf.

The largest projects underway at the end of first quarter 2018 were American Airlines Corporate Campus, a 1,700,000 sf building with 100% of its space pre-leased, and Pioneer Natural Resources, a 1,125,000 sf facility that is 100% pre-leased.



Noteworthy Projects and Deliveries



American Airlines Corporate Campus

1,700,000 SF
Single Tenant
Delivers Dec. 2019



American Airlines Corporate Campus

1,125,000 SF
Single Tenant
Delivers July 2019



Charles Schwab Corporate Campus

500,000 SF
Single Tenant
Delivers May 2019



PwC Tower

494,300 SF
Multi Tenant
Delivers July 2018



The Union

418,132 SF
Multi Tenant
Delivers Oct. 2018



The Epic

294,820 SF
Multi Tenant
Delivers March 2019



3201 Olympus Blvd

250,000 SF
Multi Tenant
Delivers March 2019



Fourteen55

240,000 SF
Multi Tenant
Delivers Aug. 2018



Harwood No.10

231,098 SF
Multi Tenant
Delivers Dec. 2018

Thank you.

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