3Q24

Houston Office Market Overview

NEWMARK

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Market Observations

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- The Houston market's unemployment rate rose 19 basis points year over year to 4.4% but remains below the five-year average of 5.5%.
- Job growth fell by 77 basis points year over year to 2.3%, trending toward pre-pandemic levels, with August 2019 growth at 2.2%.
- All sectors, except information, reported employment growth, with other services leading job gains at 8.0% over the past 12 months.
- Office-using jobs in the market totaled 784,172 in August 2024, reflecting 10.0% growth since 2019.

Leasing Market Fundamentals

- Average annual full-service asking rental rates dropped to $30.05/SF, reflecting a 1.3% decrease year over year. The current average asking rent is a 1.93% decrease from the all-time high of $30.64/SF reported in the fourth quarter of 2023.
- Overall vacancy rates fell slightly to 25.2% in the third quarter of 2024, down 10 basis points quarter over quarter, but increasing by 30 basis points year over year. Vacancy is trending toward stabilization as the construction pipeline empties and new deliveries slow.
- Positive absorption in the second and third quarters of 2024 has counteracted the 991,864 SF negative absorption in the first quarter. Year to date, absorption totals -3,751 SF, with positive absorption of 466,840 SF in the third quarter.
- Total leasing activity closed the quarter at 2.5 MSF, well below the long-term third-quarter average of 4.4 MSF. The average lease size was 3,542 SF, a decrease of 4.4% quarter over quarter and a decrease of 4.1% year over year. Deal volume is down 18.7% year over year as occupiers hold out for a more favorable financing environment and await election results.

Major Transactions

- Jackson Walker signed the quarter's largest deal, a renewal and expansion for 88,214 SF at 5 Houston Center in the CBD.
- Coworking operator, IWG/Spaces signed a 65,909 SF lease at The Jones on Main for the second largest transaction of the quarter.
- Tenants are showing renewed interest in the CBD, with four of the six-largest deals of the quarter occurring in the submarket.
- Notable transactions during the quarter came from a broad mix of tenants, indicating a healthy appetite for space among occupiers.

Outlook

- The Houston office market will likely continue to see subdued growth for the remainder of 2024. Office investment activity could start to pickup due to the recent 50 basis point reduction in interest rates along with the results of the upcoming elections.
- Strong demand for premier office product has continued to keep rents elevated in top tier buildings, increasing the rent spread between Class A and Class B assets, with flight-to-quality expected to remain a trend in the market.
- The office market is expected to remain tenant friendly with continued muted demand. As a result, overall asking rents in non-premier buildings are projected to remain flat in the near term.

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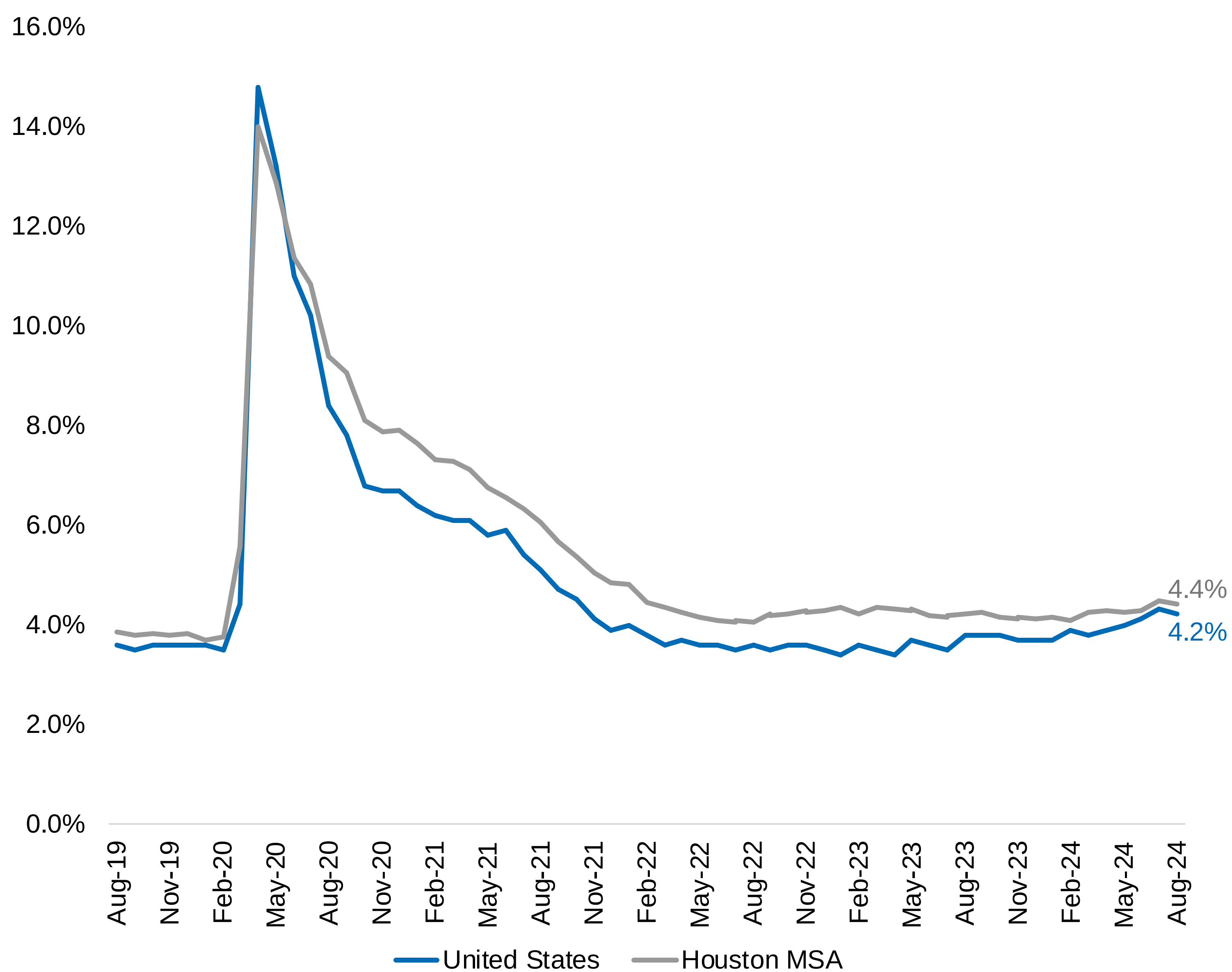
Economy

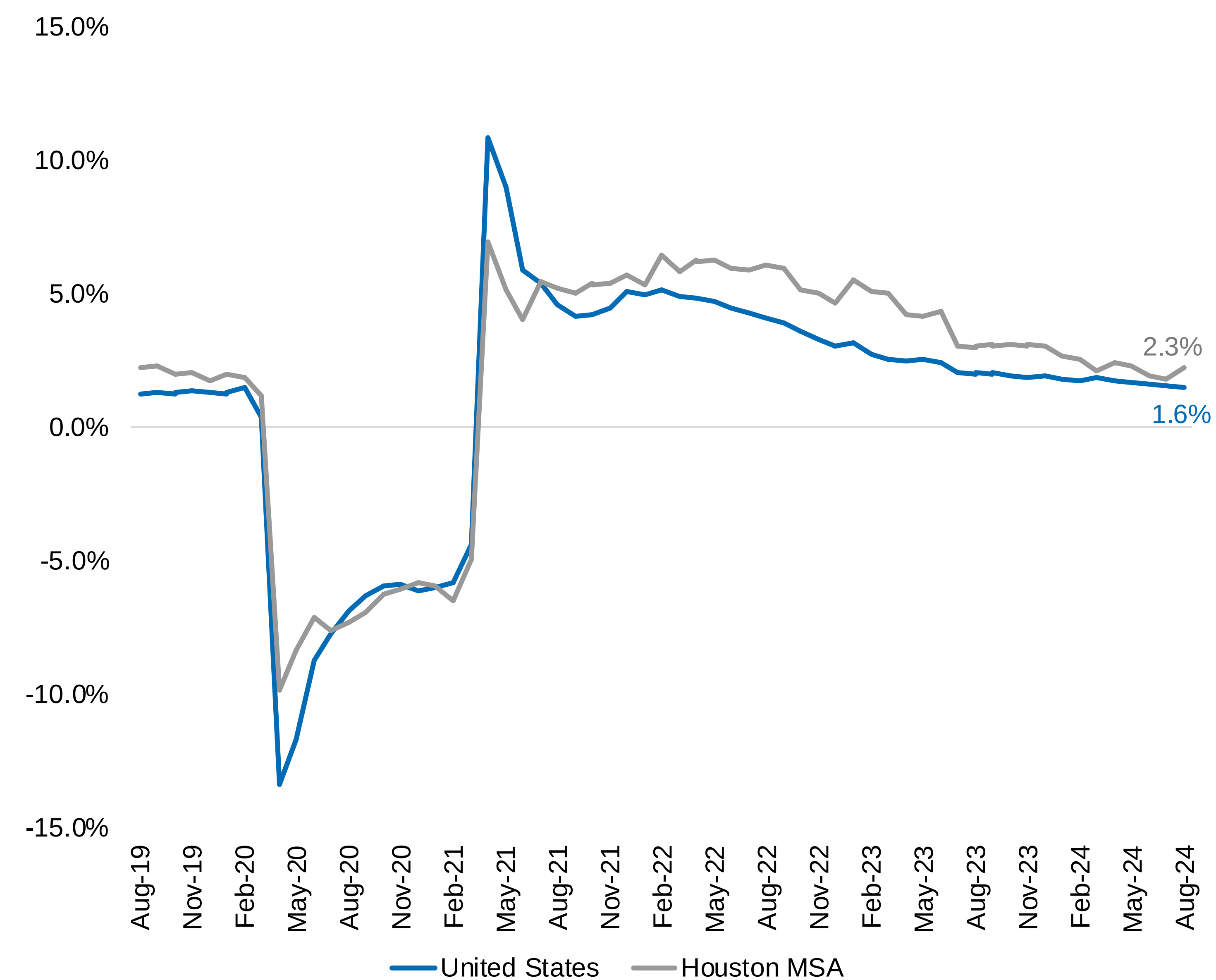
Metro Employment Trends Continue Slow Growth

The Houston market has generally reported slightly higher unemployment rates compared with the national average, while outperforming in employment growth. Recent national economic headwinds have pushed the market's unemployment rate and the national average to converge, at 4.4% and 4.2%, respectively. Houston's unemployment rate increased by 19 basis points year over year, while the employment year-over-year growth rate slowed by 77 basis points compared with the previous year.

Unemployment Rate, Seasonally Adjusted



Nonfarm Payroll Employment, Seasonally Adjusted, 12-Month % Change

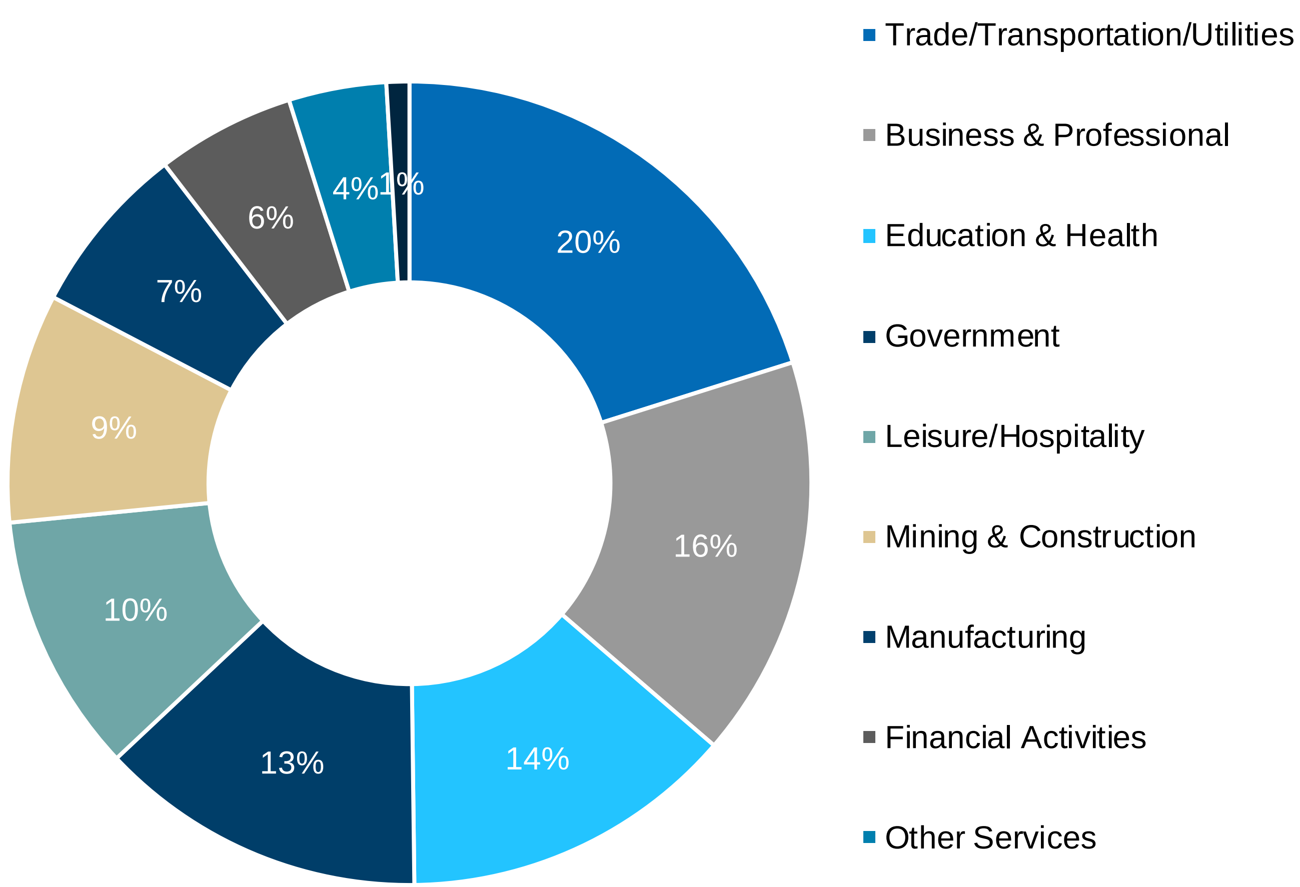


Source: U.S. Bureau of Labor Statistics, Houston MSA

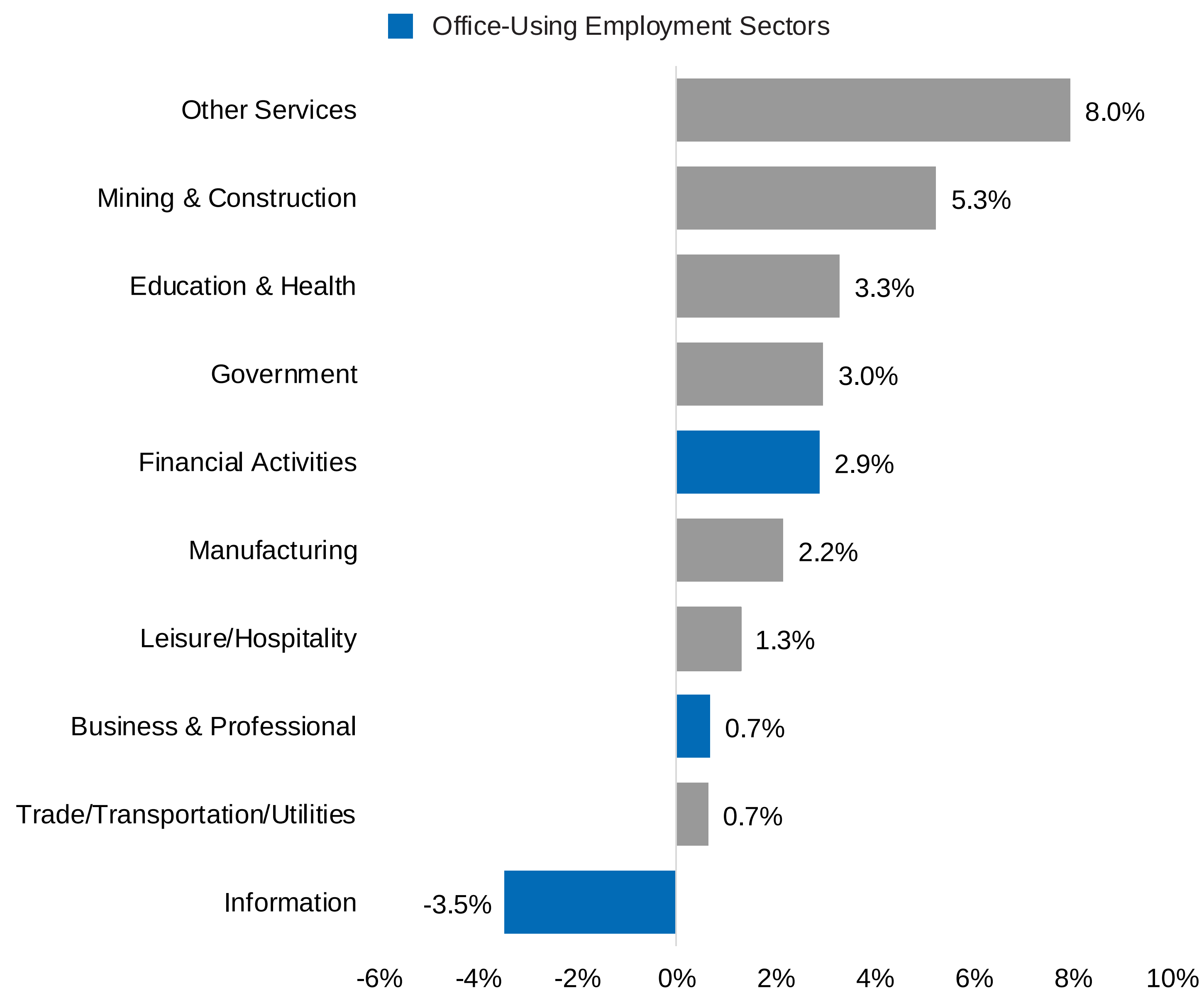
Employment Growth Continues Across Most Office Sectors

Known for its energy sector, the Houston market's top two employment industries account for 36.3% of market share. The office-using employment's business and professional sector is the second-largest industry sector in the metroplex at 16.2%. All industries in the metro, except for information, reported growth with office-using industries reporting year-over-year gains ranging from 0.7% to 2.9% with the information sector reflecting a decline of 3.5%.

Employment by Industry, August 2024



Employment Growth by Industry, 12-Month % Change, August 2024

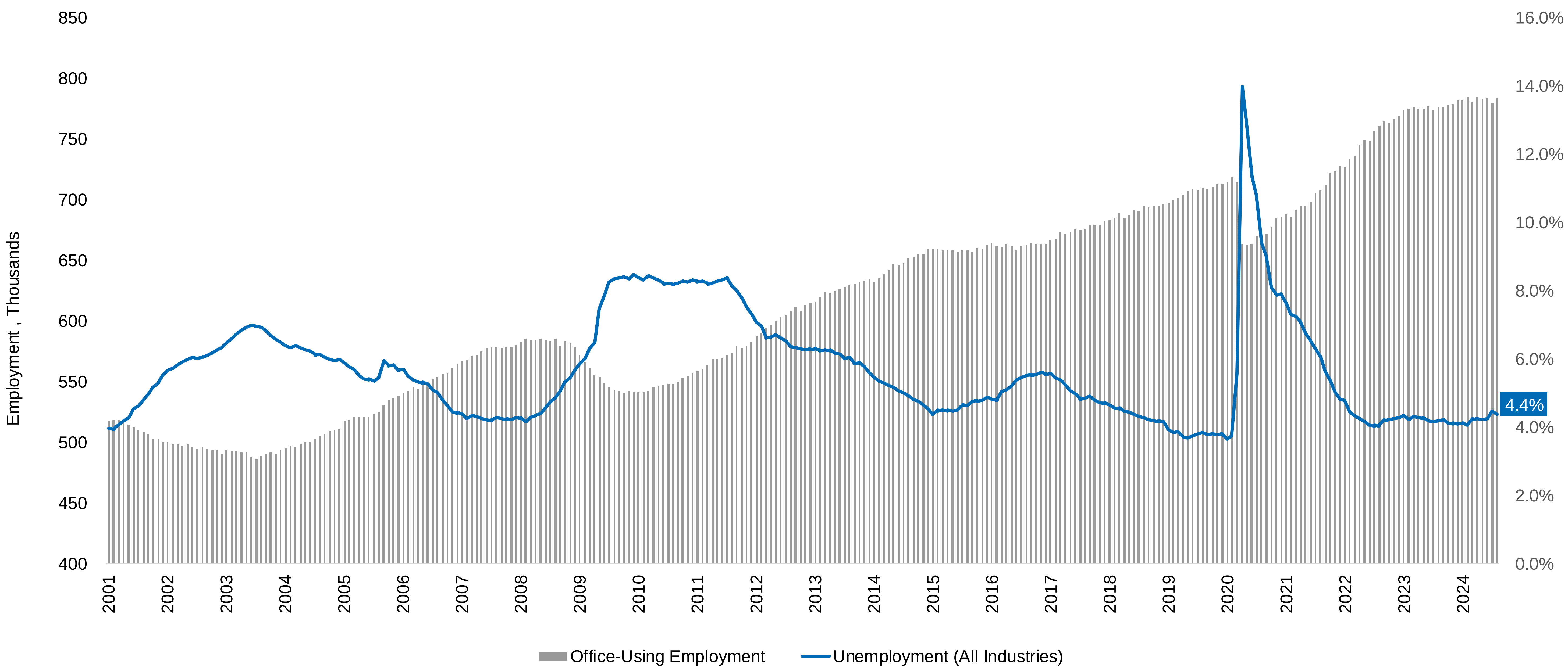


Source: U.S. Bureau of Labor Statistics, Houston MSA

Overall Office-Using Employment Eases from Historical High

Office-using employment in the Houston market as of the end of August 2024 is at 784,172 employees, falling by 1,226 from the all-time high in April 2024. Currently, the unemployment rate is at 4.4%, above the 3.8% average levels reported in 2019. The office-using information sector was the only employment sector to report negative annual growth, while the business and professional services sector posted marginal gains. The stagnating information sector is a contributing factor to Houston's unemployment rate and decreased office-using employment numbers.

Office-Using Employment* and Unemployment Across All Industries



Source: U.S. Bureau of Labor Statistics, Houston MSA

*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.

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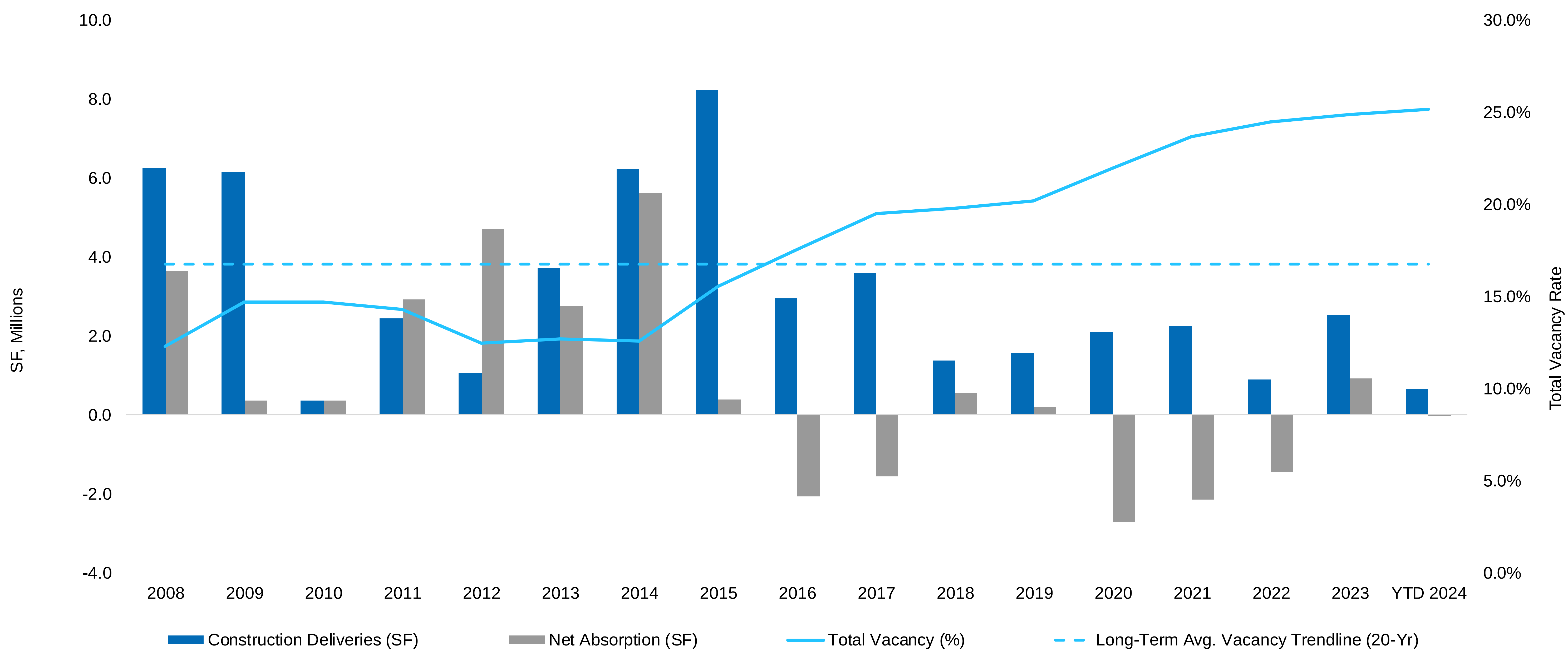
Leasing Market Fundamentals

Vacancy Continues to Flatten as Net Absorption Outpaces Deliveries

The Houston office vacancy rate increased by 30 basis points year over year to 25.2% in the third quarter of 2024, well above the long-term average of 16.8%. Quarter over quarter, vacancy rates fell 10 basis points as absorption outpaced deliveries. Since the oil crash in 2015-2016, vacancy rates have steadily increased in the market as new deliveries outpaced annual absorption. However, construction pipeline empties, vacancy in the market is expected to stabilize in the near-term.

Historical Construction Deliveries, Net Absorption, and Vacancy

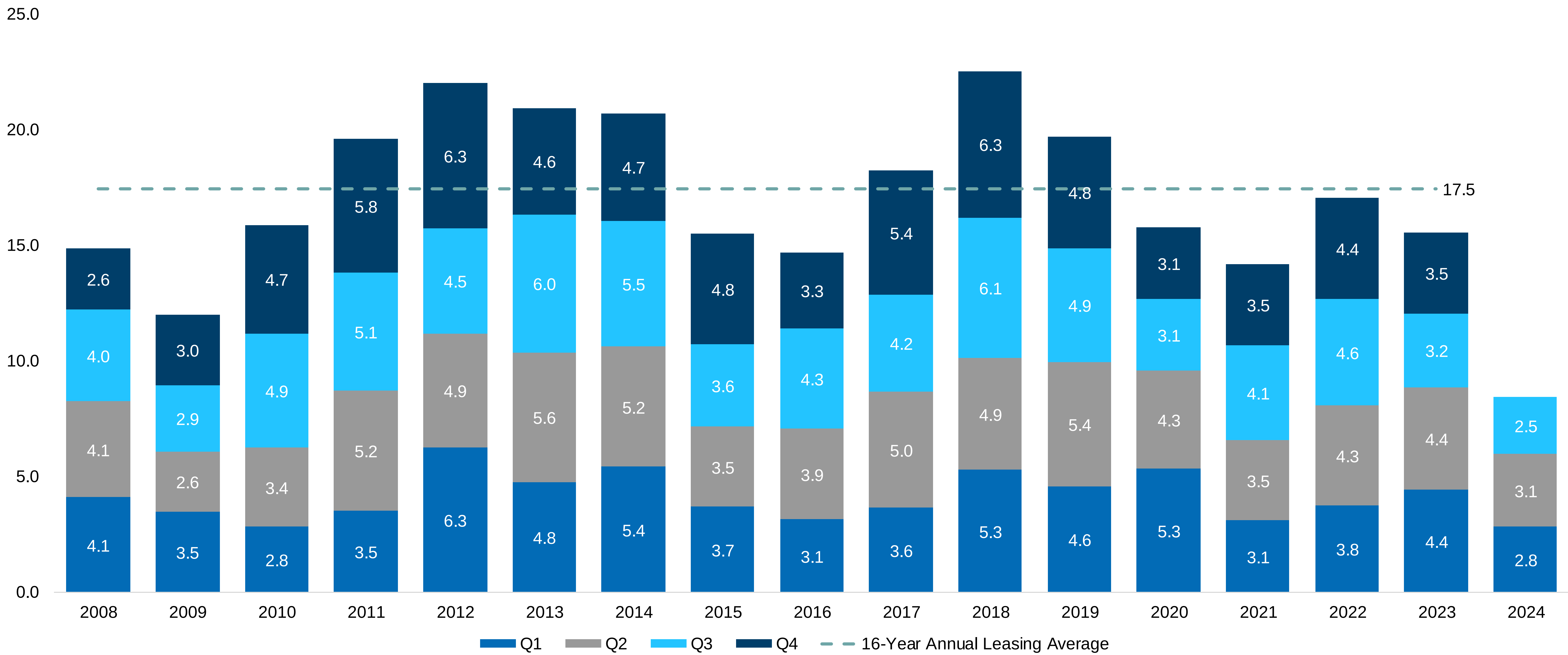


Source: Newmark Research, CoStar

Deal Activity Continues to Decline in Third Quarter

Leasing activity in the market remains slower, with leasing activity in the third quarter of 2024 totaling 2.5 MSF. Since 2008, third-quarter leasing activity averaged 4.4 MSF, with the third quarter of 2024 roughly 57% lower than the historical average. Deal size averaged 3,542 SF in the third quarter of 2024, down 153 SF from a year ago. The slowing leasing activity pace, down 18.7% in number of deals year over year, is largely attributed to occupiers waiting out the challenging debt environment and upcoming elections.

Total Leasing Activity (msf)

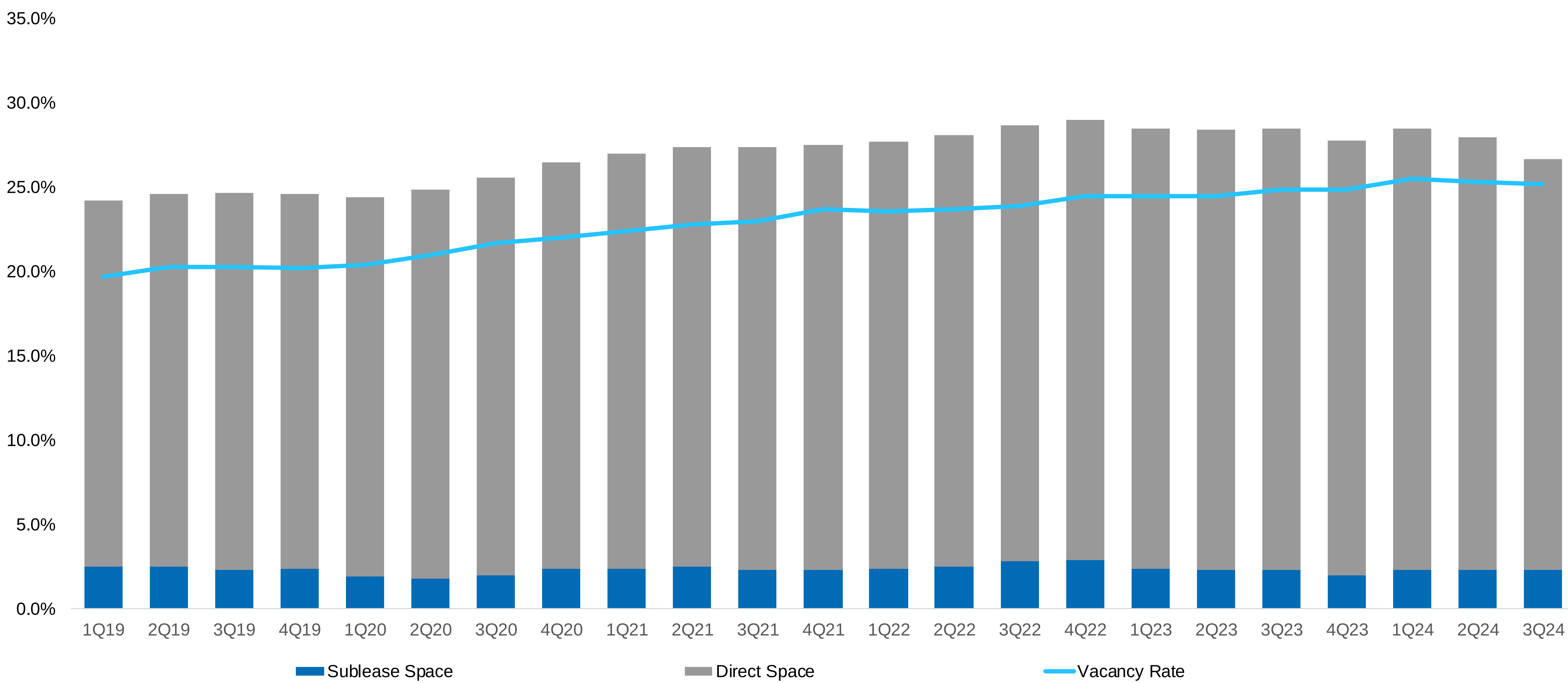


Source: Newmark Research, CoStar

Availability Continues to Fall but Remains Elevated

Sublease availabilities in the Houston market have declined since the oil crash in 2015-2016, remaining at a relatively steady level since 2019. As of the end of the third quarter of 2024, sublease availability in the market was at 2.3%, with no change quarter over quarter. Direct availabilities have generally increased since the pandemic, reaching an all-time high of 26.2% in the third quarter of 2023 and again in the first quarter of 2024, with the current direct availability rate at 24.4%. Vacancies remain elevated alongside availabilities, at 25.2%.

Available Space as Percent of Overall Market

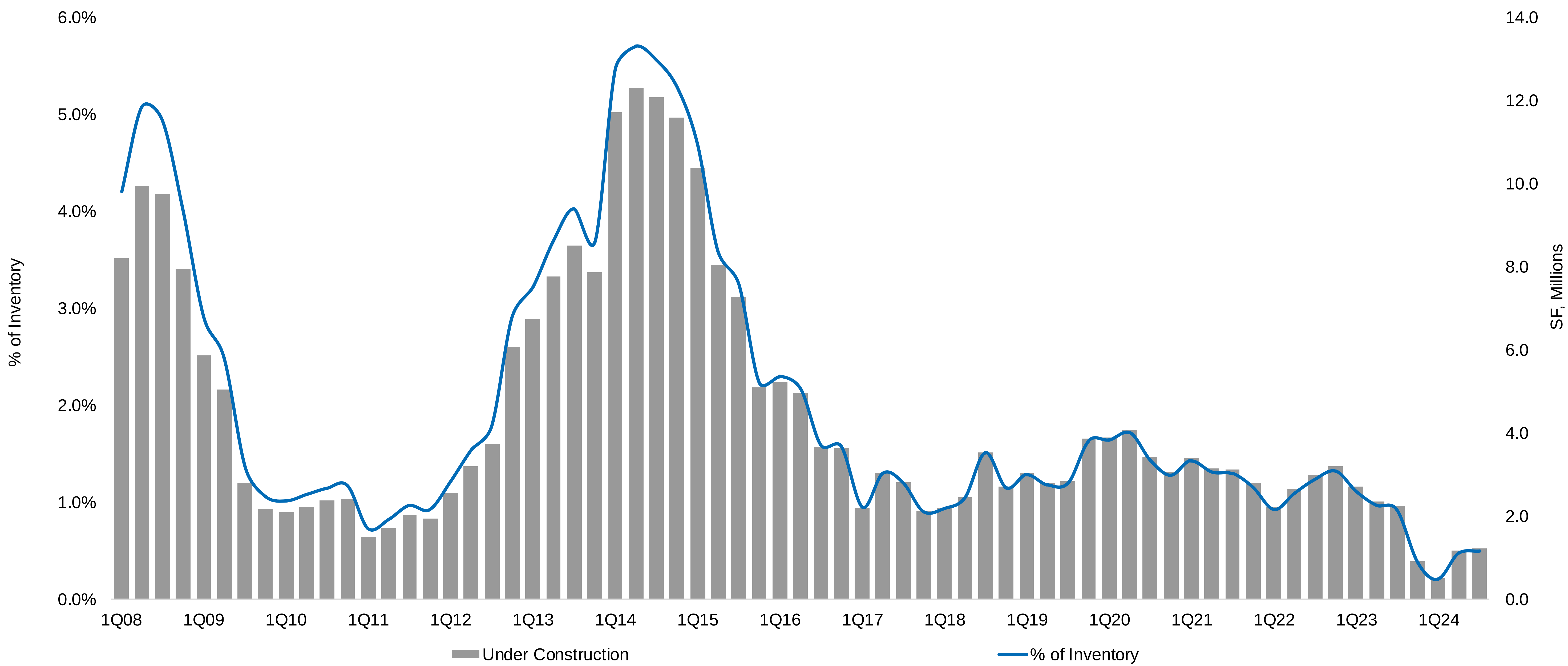


Source: Newmark Research, CoStar

Construction Activity Rose but at Substantially Subdued Level

Construction activity has remained relatively muted in the market since 2016. As of the third quarter of 2024, the market had 1.2 MSF under construction*, nearly double the amount of space in the pipeline in the first quarter. Under construction space accounts for 0.5% of the market's inventory, indicating there is less risk of overbuilding.

Office Under Construction and % of Inventory



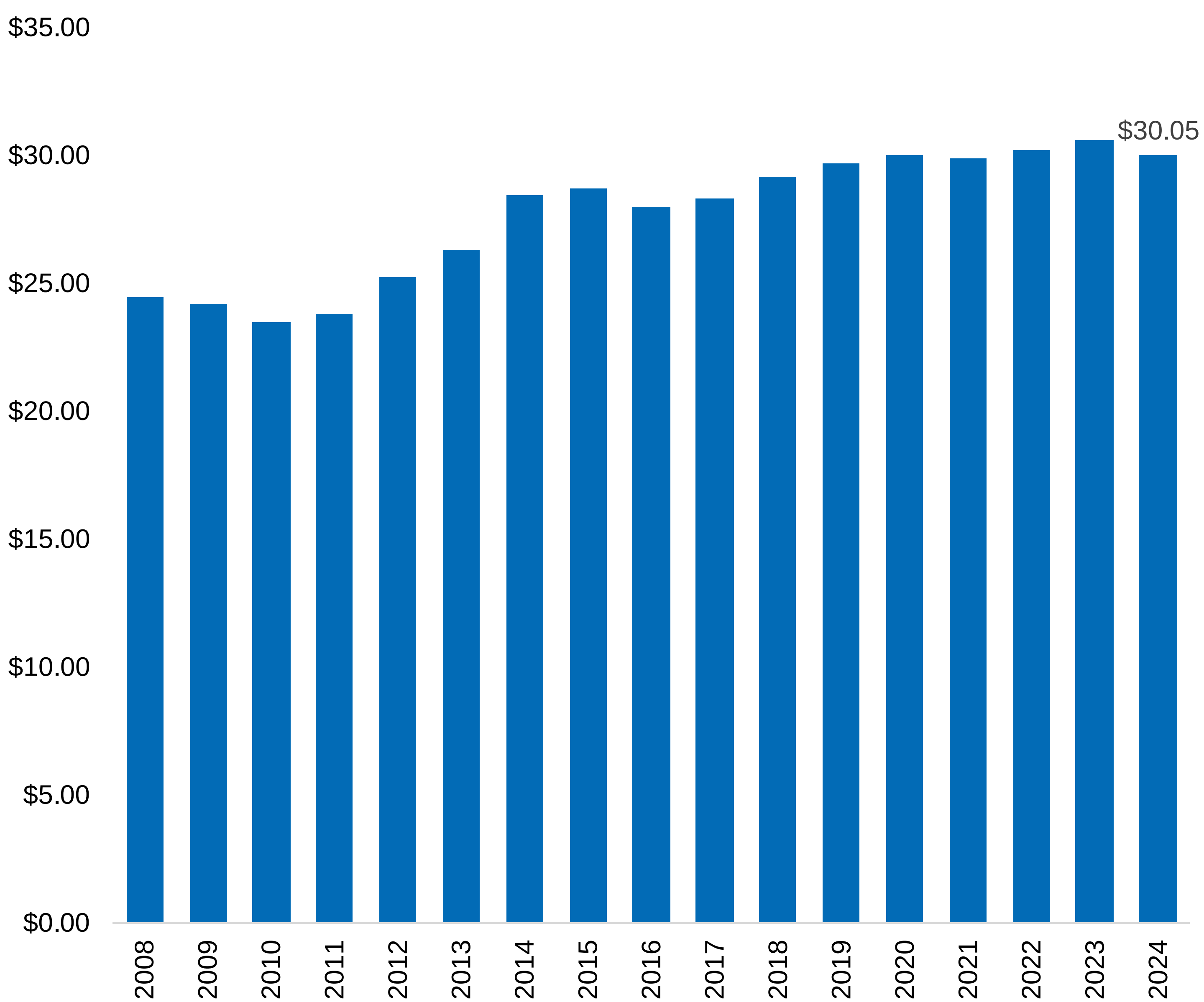
Source: Newmark Research, CoStar

* The bulk of space under construction in 2Q24 is medical office

Rents Begin Trending Downward from All-Time High

In the third quarter of 2024, rents fell by 1.3% year over year to $30.05/SF and remain below the all-time high of $30.64/SF reported in the fourth quarter of 2023. Generally, asking rents are likely to remain elevated in a market impacted by inflation, higher interest rates, and increasing operating costs.

Office Average Asking Rent, $/SF, FS



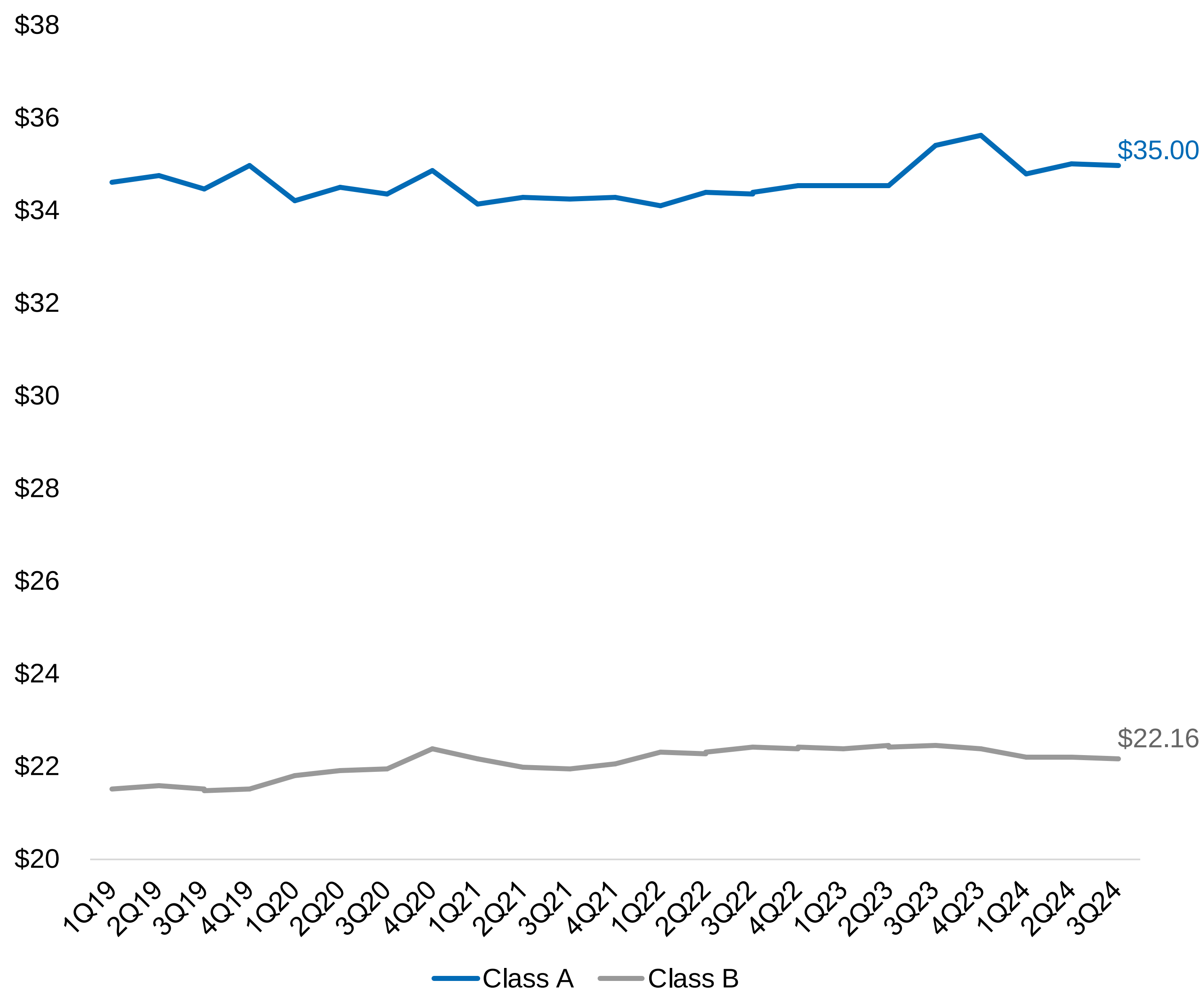
Year-over-Year Asking Rent Growth Rate

Source: Newmark Research, CoStar

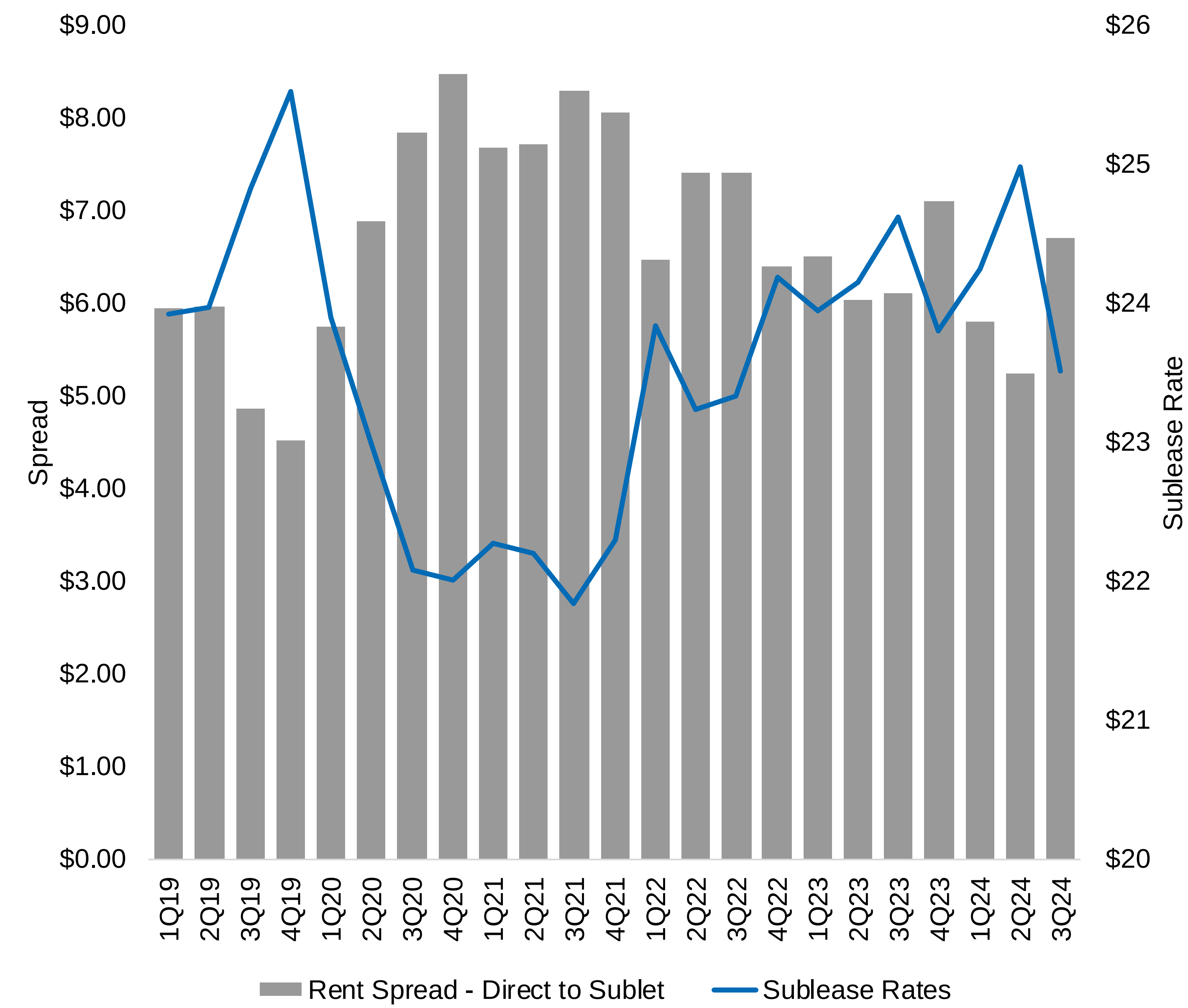
Rent Spread Remains Wide Among Class A Assets

As of the end of the third quarter of 2024, Class A rents ended at $35.00/SF, while Class B reported $22.16/SF. The $12.84/SF spread represents a 1.0% decrease year over year and reflects the greater demand for higher quality assets. Sublease rates decreased from a recent high of $24.98/SF in the second quarter of 2024, dropping 5.9% quarter over quarter to the current $23.51/SF. As companies attempt to entice subtenants, the rent spread between direct and sublease rates continues to widen, growing by 27.8% to $6.71/SF, quarter over quarter.

Class A and Class B Asking Rents



Sublease Rates



Source: Newmark Research, CoStar

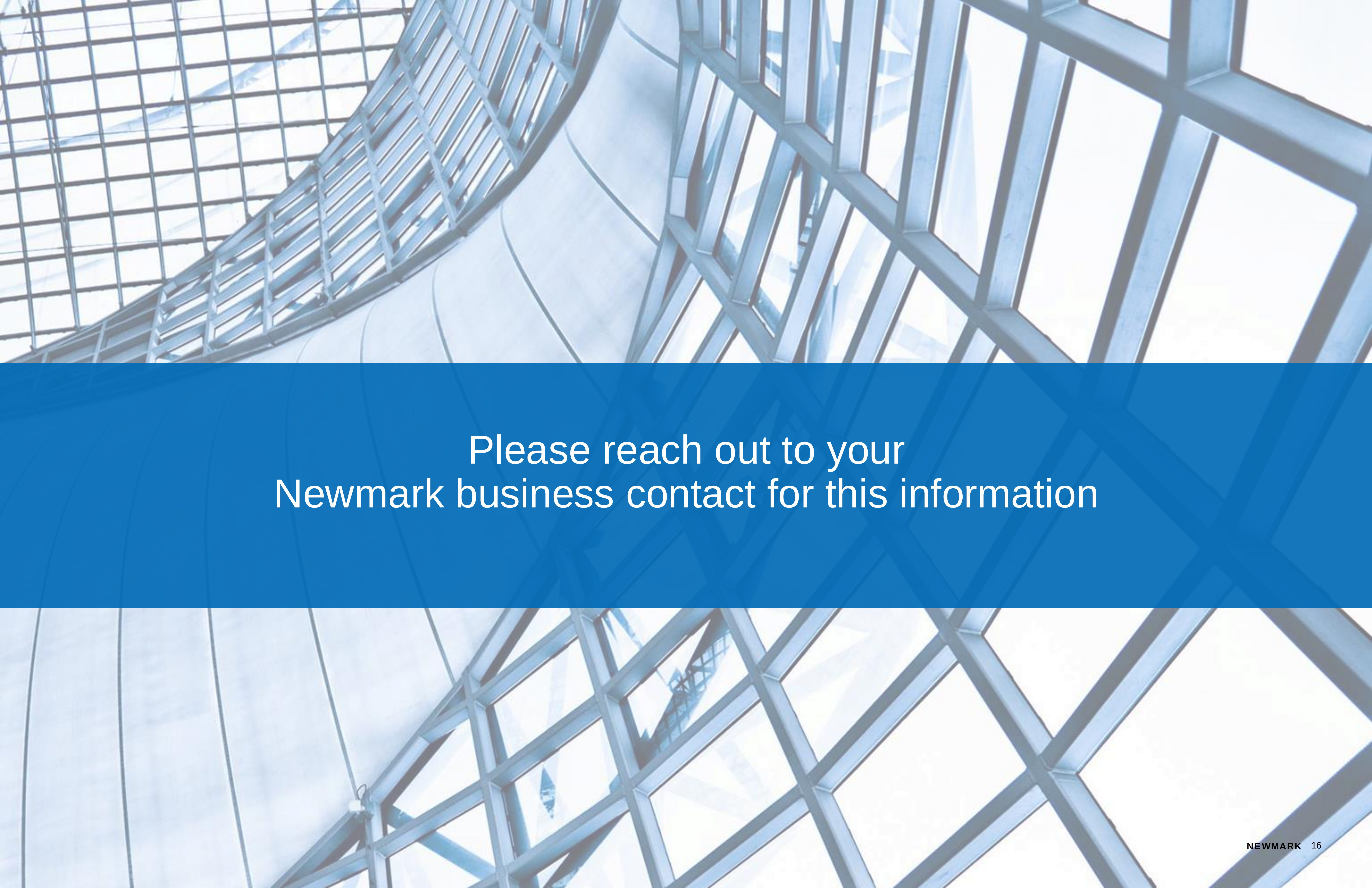
Class A Leasing Continues to Dominate as Flight-to-Quality Persists

Despite slowing leasing activity, flight to quality continues as a trend in the market even as the rent spread in Class A spaces remains elevated. As of the end of the third quarter of 2024, Class A space accounted for 63.5% of the market's leasing activity by SF, but only 33.7% of the market's deal volume. Average leases signed in Class A space were 6,670 SF and continue to remain larger than the average market deal size at 3,542 SF.

Notable 3Q24 Lease Transactions

Tenant	Building(s)	Submarket	Type	Square Feet
Jackson Walker	5 Houston Center	CBD	Renewal/ Expansion	88,214
Law firm Jackson Walker renewed its lease at 5 Houston Center, expanding by 11,199 SF. The firm will occupy 88,214 SF starting in January 2026.				
IWG/Spaces	The Jones on Main	CBD	Direct New	65,909
Swiss coworking company IWG leased 65,909 SF at The Jones on Main for its Spaces brand, taking space previously occupied by WeWork.				
Fayez Sarofim & Co.	Texas Tower	CBD	Direct New	60,764
Global investment manager Fayez Sarofim & Co. leased 60,794 SF at Texas Tower in the CBD.				
Mitsubishi Heavy Industries	3009 Post Oak	Galleria/Uptown	Direct New	50,990
Japanese multinational engineering and electronics equipment company Mitsubishi Heavy Industries signed for 50,990 SF at 3009 Post Oak in the Galleria/Uptown submarket.				
Kiewit	3831 Technology Forest Blvd	The Woodlands	Renewal	50,102
Construction and engineering firm Kiewit renewed its 50,102 SF lease at 3831 Technology Forest Blvd in The Woodlands.				
Sable Offshore	Texas Tower	CBD	Direct New	46,149
Houston-based Sable Offshore, an independent upstream company, signed a new lease for 46,149 SF at Texas Tower in the CBD.				

Source: Newmark Research, CoStar



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Newmark has implemented a proprietary database and our tracking methodology has been revised. With this expansion and refinement in our data, there may be adjustments in historical statistics including availability, asking rents, absorption and effective rents. Newmark Research Reports are available at nmrk.com/insights.

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