MARKET REPORT

Industrial

Houston Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

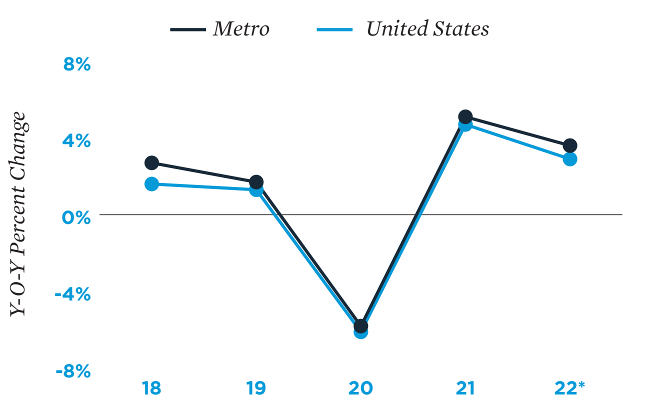
Midyear 2022

Monumental Port Expansion, Leasing Surge Epitomize Near- and Long-Term Tailwinds

Billion dollar ship channel initiative enhances future prospects. In early June it was announced that Project 11, an improvement to the Port of Houston more than a decade in planning, would officially get underway, with a completion target set for 2025. An estimated $1 billion will be injected into the project, with a goal of widening and deepening the port to facilitate efficient two-way traffic flow. At a time when port congestion has plagued supply chains across the globe, this will likely intrigue shippers and distributors, potentially elevating the number of vessels coming in and out of Houston. This will translate to increased storage needs near the port, serving as a tailwind for industrial space demand in adjacent areas. Locations that stand to benefit most include Chambers and Galveston counties as well as the Interstate 10 corridor on the east side of the metro.

Southeast Houston is the epicenter of leasing. Across the first six months, Pasadena, Baytown and La Porte were responsible for about one-third of the 100,000-square-feet-plus commitments signed metrowide. Baytown alone inked at least five tenants for 250,000-square-foot-plus spots, predominantly logistics providers, such as FedEx, NFI Industries and Supply Chain Warehouses. Still, the Southeast Corridor had the highest vacancy rate among major submarkets in Houston, entering the second quarter at 7.5 percent. New speculative supply is counterbalancing strong demand here. Approximately 3.4 million square feet of space with no commitment as of June will deliver in the Southeast Corridor in the second half.

Employment Trends



** Forecast*

Sources: BLS; CoStar Group, Inc.

Industrial 2022 Outlook

112,000 JOBS *will be created*

EMPLOYMENT:

Houston's transportation and warehousing segment grew by more than 15,000 roles from the end of 2019 through May of this year, one of the largest gains across sectors. Sustained expansion in this industry helps lift the total job count by 3.6 percent.

16,500,000 SQ. FT. *will be completed*

CONSTRUCTION:

After an active stretch of construction during which roughly 53 million square feet finalized from 2020-2021, development cools off this year. The slower pace of building will allow demand to outpace supply additions, pushing down on vacancy.

40 BASIS POINT *decrease in vacancy*

VACANCY:

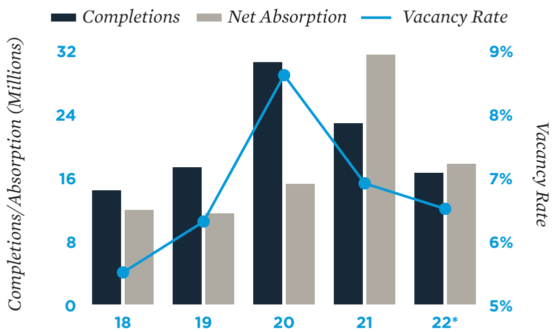
A bevy of 100,000-square-foot-plus lease signings in the first half of this year, and many more anticipated in the second half, propel net absorption above 17 million square feet annually in 2022. This depletes vacancy for a second straight year to 6.5 percent.

9.0% INCREASE *in asking rent*

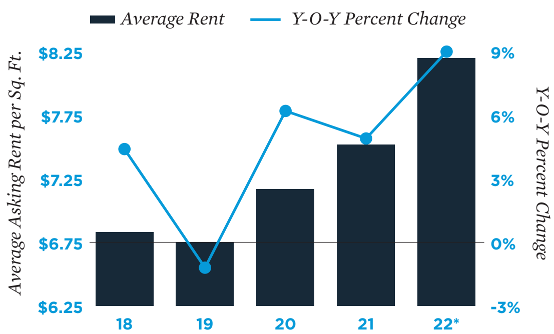
RENT:

Vacant stock descends to the lowest level since 2019 as demand outpaces new supply. These dynamics support a very strong year for rent growth, as the average marketed rate increases at its fastest pace in 15 years to $8.20 per square foot.

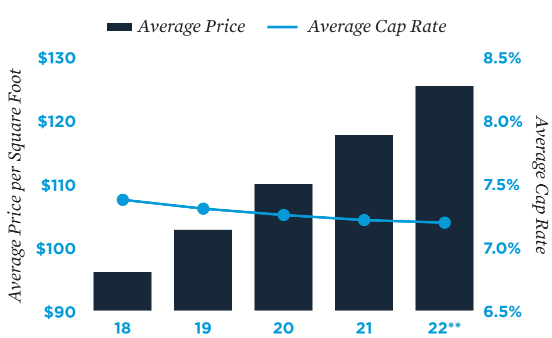
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 1Q*

Sources: CoStar Group, Inc.; Real Capital Analytics

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Price: $250

1Q 2022 - 12-Month Period

CONSTRUCTION

21,726,000 sq. ft. completed

- Deliveries in the first period of 2022 totaled 2.4 million square feet, the smallest quarterly addition since 2017. This comes after a 10.8 million-square-foot influx in the third quarter of 2021, the largest tally on record.
- Ground was broken on 16.4 million square feet of industrial space as of June, hinting that the supply wave of 2020 and 2021 has subsided.

VACANCY

240 basis point decrease in vacancy Y-O-Y

- Entering 2021, the North Corridor had the highest vacancy in Houston at 10.7 percent. Now in the first quarter of 2022, the rate here is down to 6.6 percent, which is lower than at least two comparably sized submarkets.
- Inventory in the CBD rose by just 0.5 percent since 2010, helping suppress availability. The rate here has never exceeded 6.0 percent during that span.

RENT

10.6% increase in the average asking rent Y-O-Y

- The Northwest Corridor, Houston's largest submarket with over one-fourth of the metro's total stock, posted double-digit rent growth annually. Robust gains here and in the CBD buoyed the marketwide improvement.
- One of the lowest cost areas — the Southern Corridor — had a vacancy rate under 4 percent in March, which is powering a surge in asking rents here.

Investment Highlights

- From April 2021 through March 2022, about 80 percent more industrial trades were recorded than the annual average between 2015 and 2019. Buyer fervor is evident and fundamental strength, paired with a promising outlook, should keep the transaction market healthy and liquid, even as higher interest rates could alter investor decisions in the coming quarters.
- Industrial assets in Houston commanded an average sale price of $125 per square foot during the yearlong span ended in the first quarter, rising 12 percent relative to the prior interval. Despite this increase, it has the lowest entry cost among major Texas markets and also the majority of similarily-sized metros in the Sun Belt. Likewise, the mean cap rate of 7.2 percent in Houston is the highest in the state by at least 50 basis points.
- Deal flow during the yearlong stretch ended in May more than doubled annually in both the North and Northwest Corridors. Warehouse assets were the overwhelming buyer favorite, often trading with first-year returns in the low-4 to mid-7 percent range. Larger warehouses in prominent business parks land on the lower side of that cap rate range. Conversely, smaller facilities in outlying suburbs adjacent to major interstates, like Conroe, Spring and Humble, have initial yields at the top of that band.