

# MARKET REPORT

Office  
Houston Metro Area

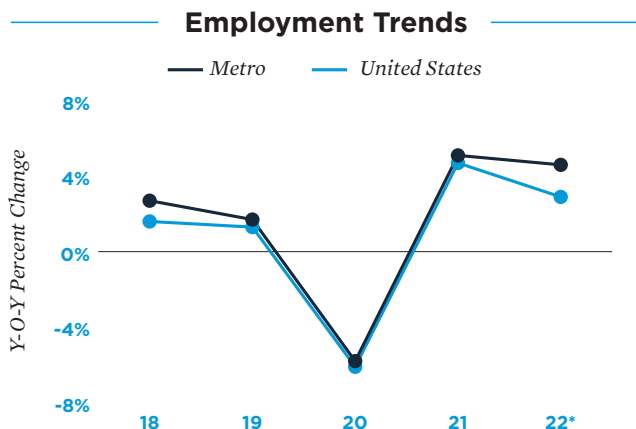
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4Q/22

## Energy Corridor-Adjacent Areas and North Suburbs Are a Beacon of Optimism During Market Pressure

**Katy Freeway and Interstate 45 areas emerge as bright spots.** Of the 29 Houston office submarkets with at least 1 million square feet of inventory, vacancy declines were recorded in 11 over the past year ending in June. This grouping included several submarkets on the west and far north portions of the metro, as firms continue to covet space beyond the Beltway. The Katy Freeway area encompassing the Energy Corridor, as well as the neighboring Katy-Grand Parkway West and FM 1960 submarkets, all recorded annual vacancy drops over the past four quarters. A resurgence in oil prices aided these locales, with new leases signed in the area by Baker Hughes, BW Energy and Enbridge Inc. so far in 2022. Fast-growing northern suburbs along I-45, including Conroe and the Woodlands, also registered lower office availability relative to one year ago. Construction and engineering firms are most active in the leasing market here, aligning with the slew of commercial projects underway in these areas.

**Nation's most vacant metro yet to initiate downward trend.** Office availability stood at 23.4 percent in the second quarter, the highest among major U.S. markets by 200 basis points. Vacancy is expected to drift up slightly in the second half, with economic headwinds mounting as the Federal Reserve attempts to slow inflation by raising interest rates and lifting joblessness. This clouds the office sector outlook in a market that had pre-existing headwinds, with Houston's availability increasing in every year going back to 2013. On a positive note, asking rents appear to be stabilizing in recent periods.




\* Forecast  
Sources: BLS; CoStar Group, Inc.

## Office 2022 Outlook

  
**145,000**  
**JOBS**  
*will be created*


### EMPLOYMENT:

Employment gains were robust through the first eight months of 2022, adding nearly 135,000 jobs during that span, about 15 percent of which were in traditional office-using fields. Hiring activity is anticipated to drop sharply in the latter part of 2022.

  
**2,400,000**  
**SQ. FT.**  
*will be completed*

### CONSTRUCTION:

Annual delivery volume in 2022 falls below the prior year's total by almost 1.3 million square feet, which is a positive trend amid historically high vacancy. Nonetheless, this year's new supply expands metrowide inventory by 0.7 percent.

  
**50**  
**BASIS POINT**  
*increase in vacancy*

### VACANCY:

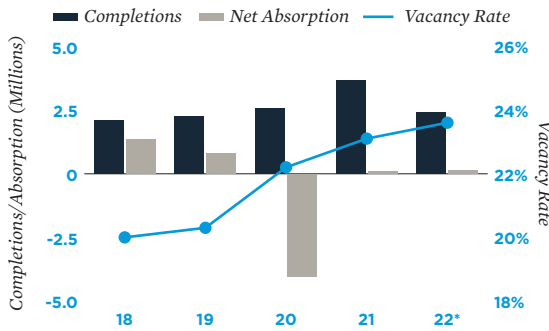
Net absorption is expected to be the strongest since 2019; however, completions and moveouts will exceed the amount of space taken up. This will push up vacancy for a 10th consecutive year to 23.6 percent.

  
**0.2%**  
**INCREASE**  
*in asking rent*

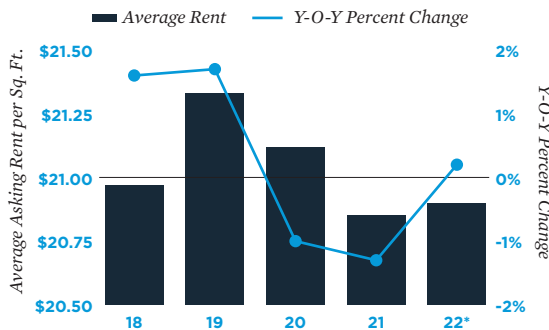
### RENT:

Houston's average asking rent holds relatively firm in 2022 at \$20.90 per square foot, following two straight years of declines. The mean marketed office rent ticked up moderately in the first half of 2022, which was not the case in either 2020 or 2021.

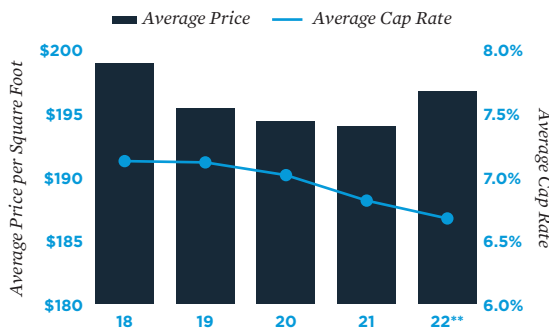
### Supply and Demand



### Rent Trends



### Sales Trends



\* Forecast \*\* Through 2Q

Sources: CoStar Group, Inc.; Real Capital Analytics

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Price: \$250

## 2Q 2022 - 12-Month Period



### CONSTRUCTION

**3,891,000 sq. ft. completed**

- The arrival of over 1.3 million square feet of new Class A space Downtown during the 12-month span had a marginal impact on segment vacancy here, while helping lift the area's average top-tier asking rent by about 4 percent.
- Looking beyond 2022, five major projects larger than 250,000 square feet are underway, headlined by multiple Texas Medical Center expansions.



### VACANCY

**40 basis point increase in vacancy Y-O-Y**

- Houston's Downtown and Katy Freeway areas, which hold nearly one-third of metro inventory, had higher vacancy in June than the 23.4 percent market mean. The rate fell in the latter amid energy sector tailwinds, however.
- Top-performing suburban office markets in terms of vacancy drops during the past year included Kingwood-Humble and Conroe.



### RENT

**0.3% decrease in the average asking rent Y-O-Y**

- As the amount of vacant Class A office space grew by 1.5 million square feet during the past 12 months, the average asking rent in this segment shrunk by almost 2 percent to \$23.34 per square foot at midyear.
- In contrast, the Class B/C average marketed rent ticked up more than 1 percent to \$18.59 per square foot, led by South Main-Medical Center.

## Investment Highlights

- Traditional office assets traded at least 25 percent more frequently from July 2021 through June 2022 as they did in the prior year. However, about two-thirds of those deals took place in the fourth quarter of 2021 or opening frame of 2022. Transactions in the second quarter of this year and preliminary figures since that point show a moderation, as inflation and interest rate hikes came to the forefront. In the most recent months, buyers favored the Katy Freeway and FM 1960 areas, where performance was relatively stronger. Returns in the 6 to 7 percent range are common here.
- Houston's average sale price climbed 1 percent to \$197 per square foot during the 12-month interval ended in June. This comes after the mean price fell in all four years spanning 2018-2021. The average cap rate slid down 20 basis points to 6.7 percent, the highest measure among major Texas markets by 30 to 50 basis points.
- Medical offices have been a bright spot amid headwinds in the traditional space. Robust population growth, including a projected 170,000-person boost to the metro's age 65-plus cohort over the next five years, solidifies buyer enthusiasm. NASA-Clear Lake is a high-focus area for these types of assets, with a handful of investors utilizing 1031 exchanges here.

The information contained in this report was obtained from sources deemed to be reliable. Every effort was made to obtain accurate and complete information; however, no representation, warranty or guarantee, express or implied, may be made as to the accuracy or reliability of the information contained herein. Metro-level employment growth is calculated based on the last month of the quarter/year. Sales data includes transactions sold for \$1 million or greater unless otherwise noted. This is not intended to be a forecast of future events and this is not a guaranty regarding a future event. This is not intended to provide specific investment advice and should not be considered as investment advice. Sources: IPA Research Services; Bureau of Labor Statistics; CoStar Group, Inc.; Real Capital Analytics