

Job Creation Expected to Digest Supply Overhang As Developers Ease Pace of Construction

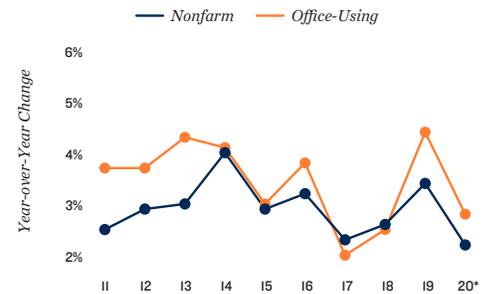
Texas' reputation for scale is exemplified in the Metroplex's office market. Dallas/Fort Worth added the most jobs in the country last year, a performance anticipated to be duplicated again in 2020. Office-using payroll growth has been particularly impressive, expanding by more than 4 percent. Unemployment, meanwhile, begins the year in the mid-3 percent range, representing the lowest level in nearly 20 years. Despite favorable demand-side momentum, vacancy remains stubbornly in the high teens as builders move in lockstep with expanding employers. That trend should begin to fade this year as supply additions fall to the lowest level in five years. Nonetheless, several quarters of strong demand and weakening construction will be necessary before rent gains eclipse 3 percent. As expected, much of the space under construction is speculative and pre-leasing is hovering near 40 percent for office properties scheduled for delivery in 2020. Following this year, however, greater relief from supply-side pressure should emerge as space commitments increase and the construction pipeline abates.

Buyers targeting smaller assets to achieve investment targets. Deal flow dipped last year as investors remained focused on a consistent set of conditions when considering deals. At the top of their wish list are well-located Class B properties with a significant vacancy factor. That trend has been persistent for the past two years and should continue into 2020. To achieve that end, investors are scouring the metro and finding smaller properties. Across all property classes, the average size of transactions has dipped 25 percent in the last 12 months, indicative of buyers' willingness to accept less square footage in return for properties near major thoroughfares that can be renovated and retenanted at better lease terms. The office districts north of Dallas and Fort Worth's city centers, along with the Mid-Cities, have consistently shown the highest investor demand.

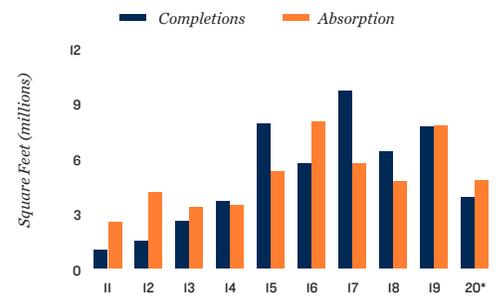
2020 Market Forecast

- Employment** up 2.2%  Approximately 85,000 new jobs are expected to be created this year, including 30,000 office-using positions.
- Construction** 3.9 million sq. ft.  Builders are on pace to expand inventory by 1.1 percent in 2020, down from 2.2 percent growth in 2019.
- Vacancy** down 50 bps  Vacancy tightens to 17.9 percent this year, surpassing the 40-basis-point decline in 2019.
- Rent** up 2.9%  Speculative office construction limits rent gains as the average asking rent inches up 2.9 percent in Dallas/Fort Worth to \$26.83 per square foot.
- Investment**  Value-add opportunities will encourage investors to broaden their search areas to find assets with a vacancy component. Overall, the average cap rate enters the year close to 7 percent.

Employment Trends



Office Supply and Demand



Vacancy and Rent Trends



* Forecast
Sources: CoStar Group, Inc.; Real Capital Analytics

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Metro-level employment, vacancy and asking rents are year-end figures and are based on the most up-to-date information available as of December 2018. Asking rent is based on the full-service marketed rental rate. Average prices and cap rates are a function of the age, class and geographic area of the properties trading and therefore may not be representative of the market as a whole. Sales data includes transactions valued at \$1,000,000 and greater unless otherwise noted. Forecasts for employment and office data are made during the fourth quarter and represent estimates of future performance. No representation, warranty or guaranty, express or implied may be made as to the accuracy or reliability of the information contained herein. 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.