4Q24

Houston Office Market Overview

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Market Observations

Economy

- The Houston market's unemployment rate rose 38 basis points year over year to 4.5% but remains below the five-year average of 5.5%.
- Job growth fell by 127 basis points year over year to 1.8%, trending toward pre-pandemic levels, with November 2019 growth at 2.1%.
- All sectors, except business and professional and information, reported employment growth, with mining and construction leading job gains at 5.7% over the past 12 months.
- Office-using jobs in the market totaled 785,675 in November 2024, reflecting 10.2% growth since 2019.

Leasing Market Fundamentals

- Average annual full-service asking rental rates fell to $29.92/SF, reflecting a 1.9% decrease year over year from the all-time high of $30.50/SF reported in the fourth quarter of 2023.
- Overall vacancy rates rose to 25.2% in the fourth quarter of 2024, up 30 basis points quarter over quarter, and increasing by 60 basis points year over year.
- Positive absorption in the second and third quarters of 2024 could not counteract the strong negative absorption that started and ended the year. The fourth quarter of 2024 had negative absorption of 619,397 SF, pushing the annual absorption total to negative 663,806 SF.
- Total leasing activity closed the quarter at 3.0 MSF, well below the long-term fourth-quarter average of 4.5 MSF. The average lease size was 3,854 SF, an increase of 16.5% quarter over quarter and a decrease of 5.4% year over year. Deal volume is down 22.1% year over year as occupiers held out for a more favorable financing environment and awaited recent election results.

Major Transactions

- Plains All American Pipeline's extension at Three Allen Center for 260,000 SF in the CBD was the largest transaction of the fourth quarter of 2024.
- Offshore engineering company Subsea7 renewed its lease at Westgate I for 177,100 SF in the second largest deal of the quarter.
- Renewed tenant interest in the CBD continues, with three of the six-largest deals of the quarter occurring in the submarket.
- Energy-related tenants signed four of the six-largest deals of the quarter, indicating revived activity in the energy sector.

Outlook

- The Houston office market will likely continue to see subdued growth at the start of 2025, as activity generated from recent interest rate reductions begins to trickle into the market. Large transactions in the fourth quarter of 2024 from energy and oil and gas companies, the market's largest sector, points to tenant optimism in the market.
- Strong demand for premier office product has continued to keep rents elevated in top-tier buildings, maintaining 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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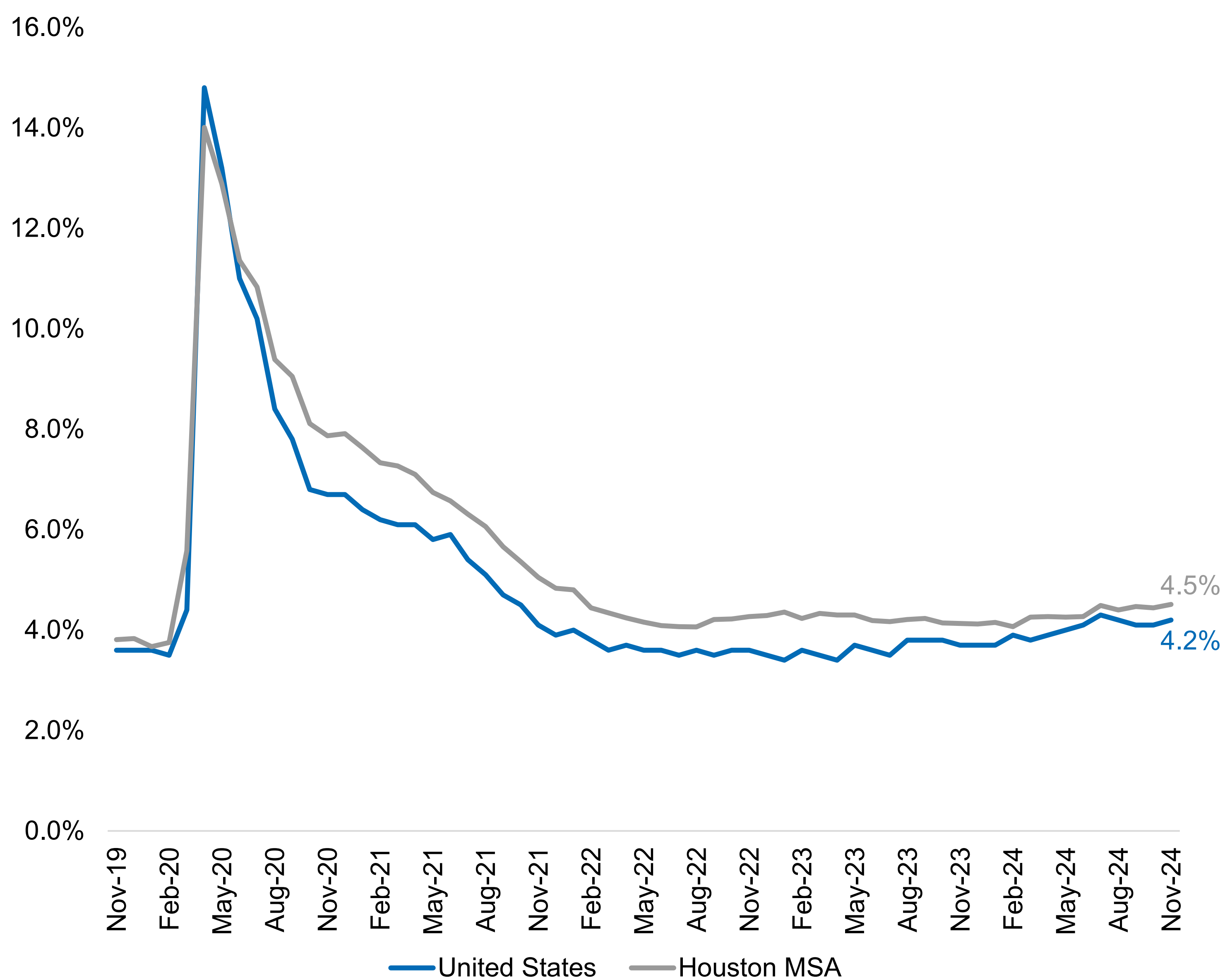
Economy

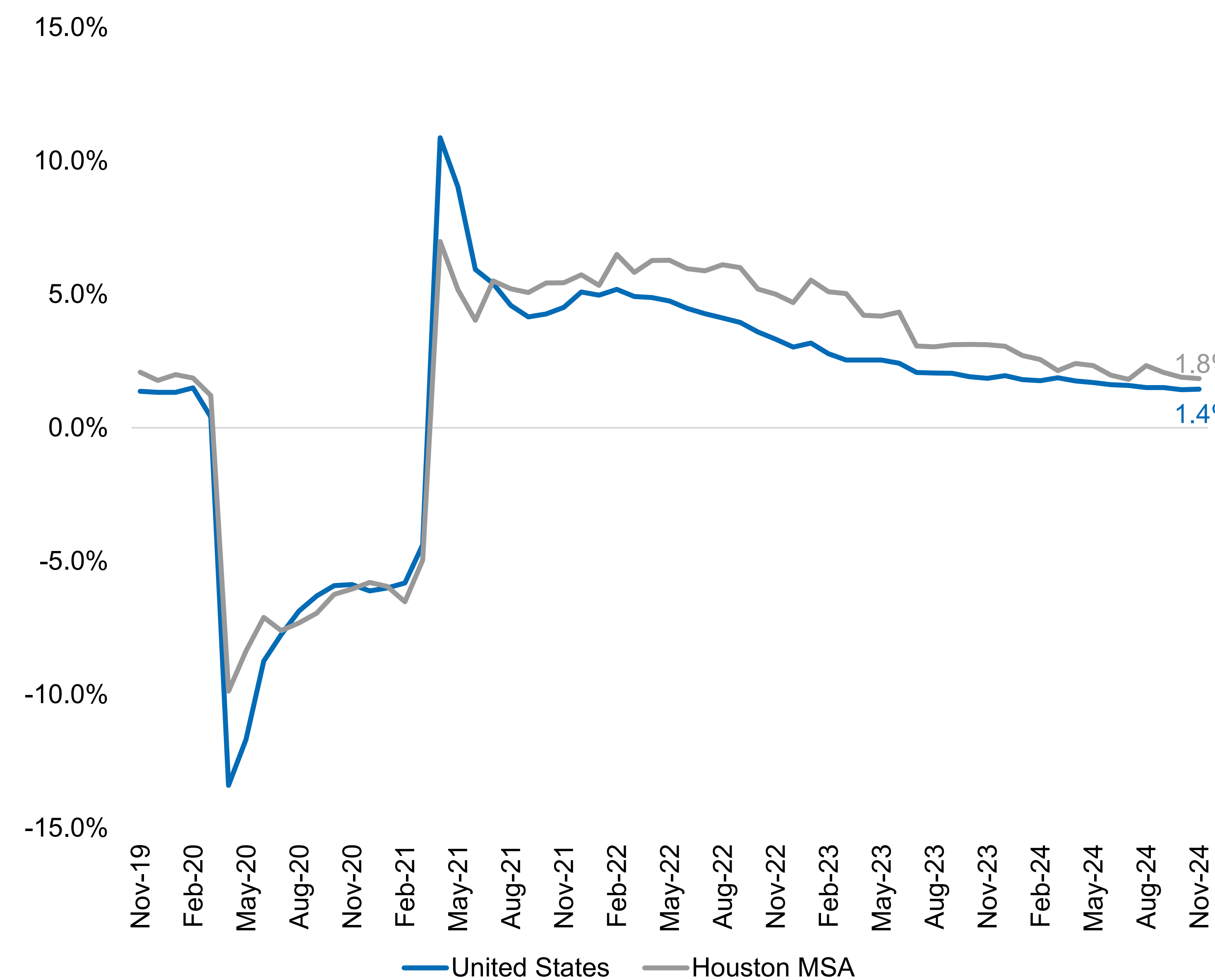
Metro Employment Trends Continue Slow Growth

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 4.5% and 4.2%, respectively. Houston's unemployment rate increased by 38 basis points year over year, while the employment year-over-year growth rate slowed by 127 basis points compared with the previous year.

Unemployment Rate, Seasonally Adjusted



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

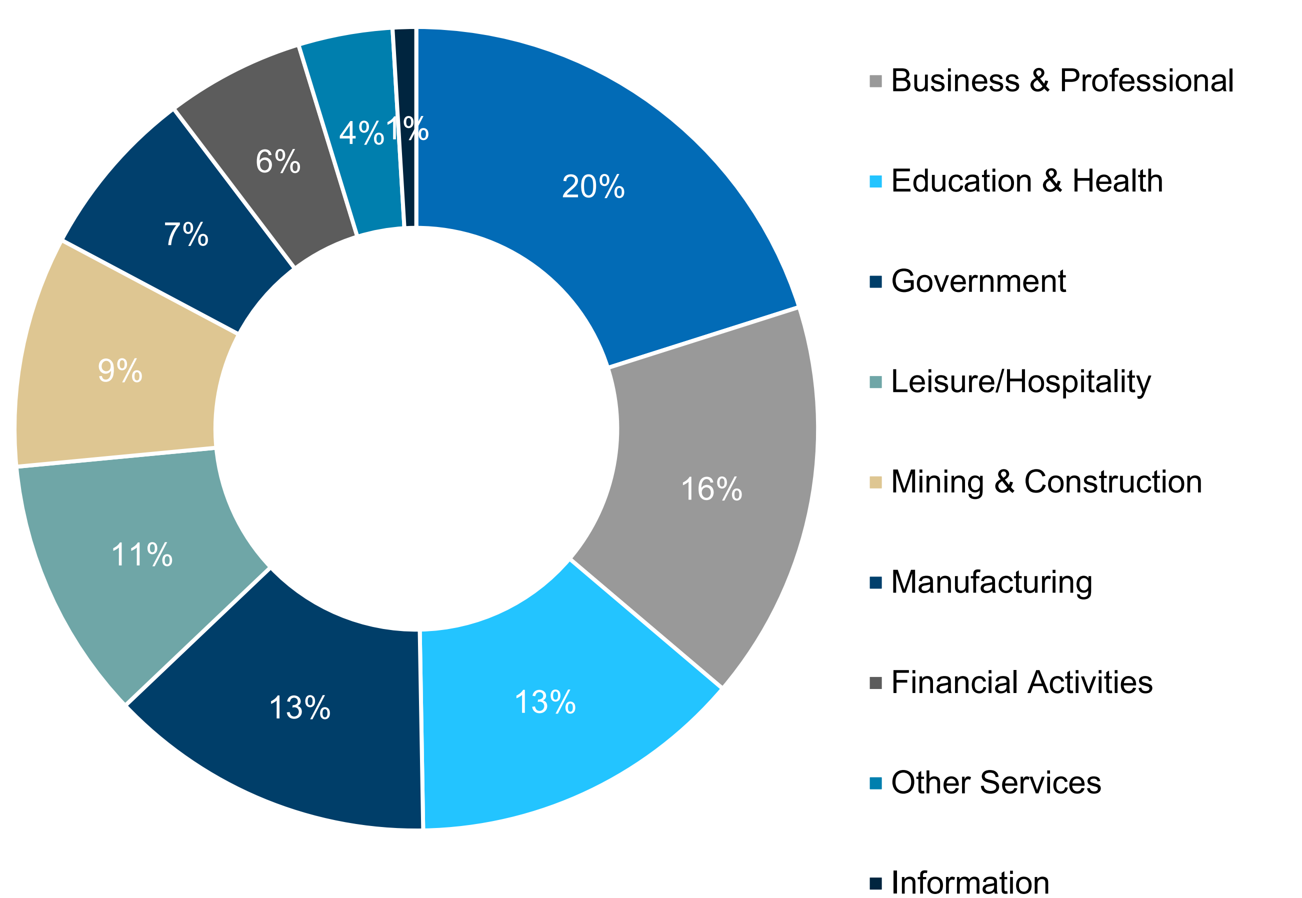


Source: U.S. Bureau of Labor Statistics, Houston MSA

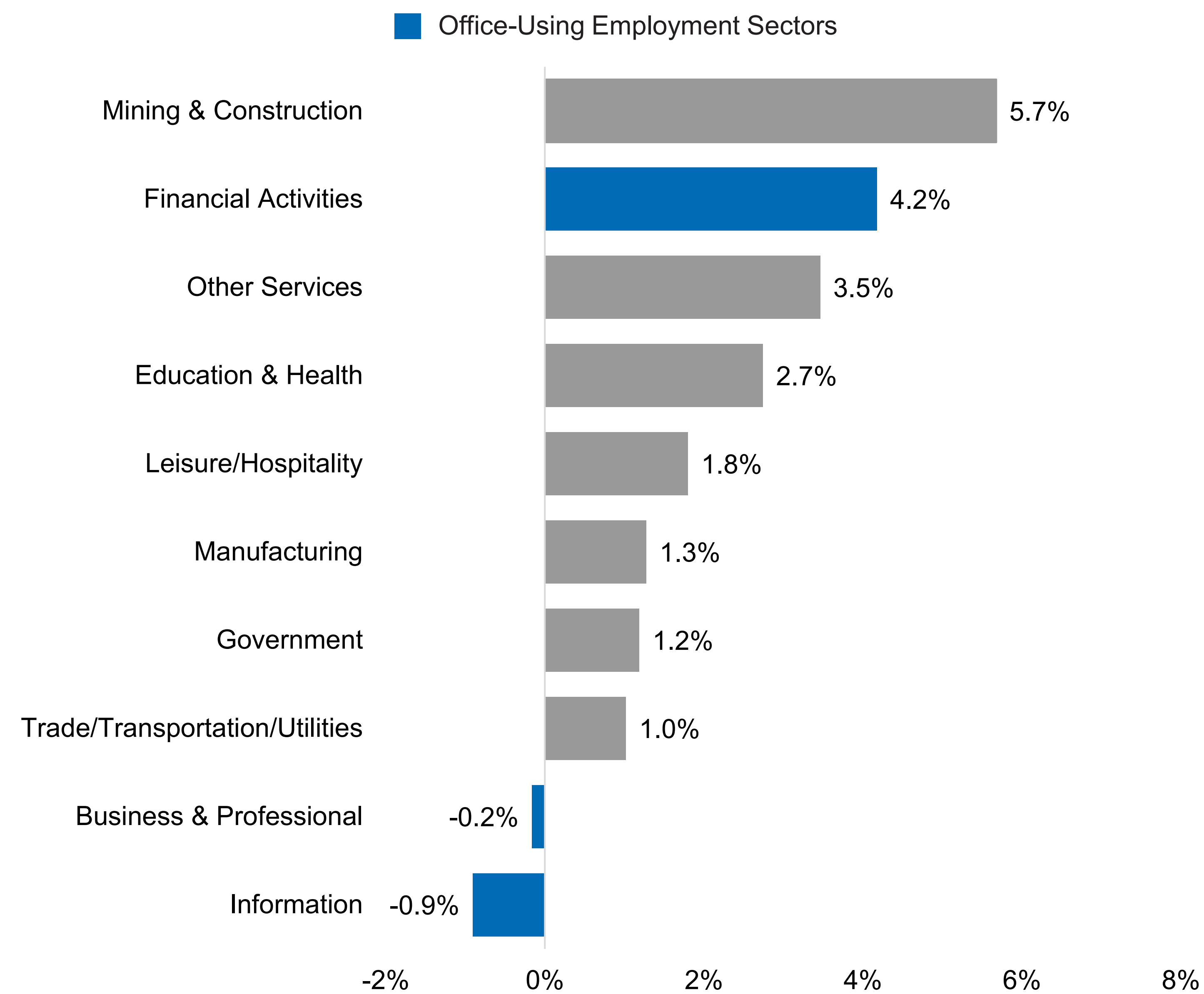
Employment Growth Slows Across Most Office Sectors

Known for its energy sector, the Houston market's top two employment industries account for 36.2% of market share. The office-using employment's business and professional sector is the second-largest industry sector in the metroplex at 16.1%. While most industries in the metro continued reporting growth, two office-using sectors contracted, with the business and professional sector and information sector declining by 0.2% and 0.9% year over year, respectively. Meanwhile, financial activities grew by 4.2%.

Employment by Industry, November 2024



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

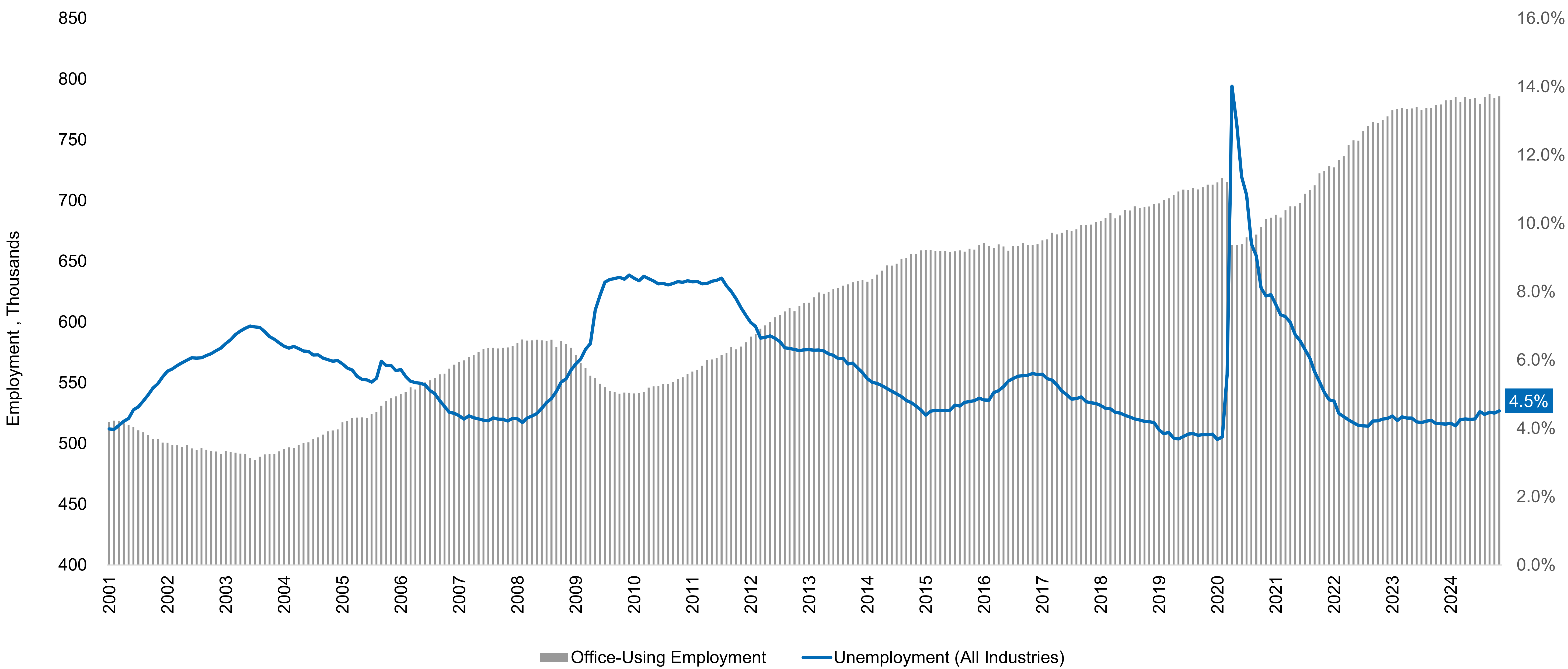


Source: U.S. Bureau of Labor Statistics, Houston MSA

Overall Office-Using Employment Eases From Historical High

Office-using employment in the Houston market as of the end of November 2024 is at 785,675 employees, falling from the all-time high in September 2024 by 2,773 jobs. Currently, the unemployment rate is at 4.5%, above the 3.8% average levels reported in 2019. The office-using business and professional, and information sectors reported negative annual growth, while the financial services sector posted moderate 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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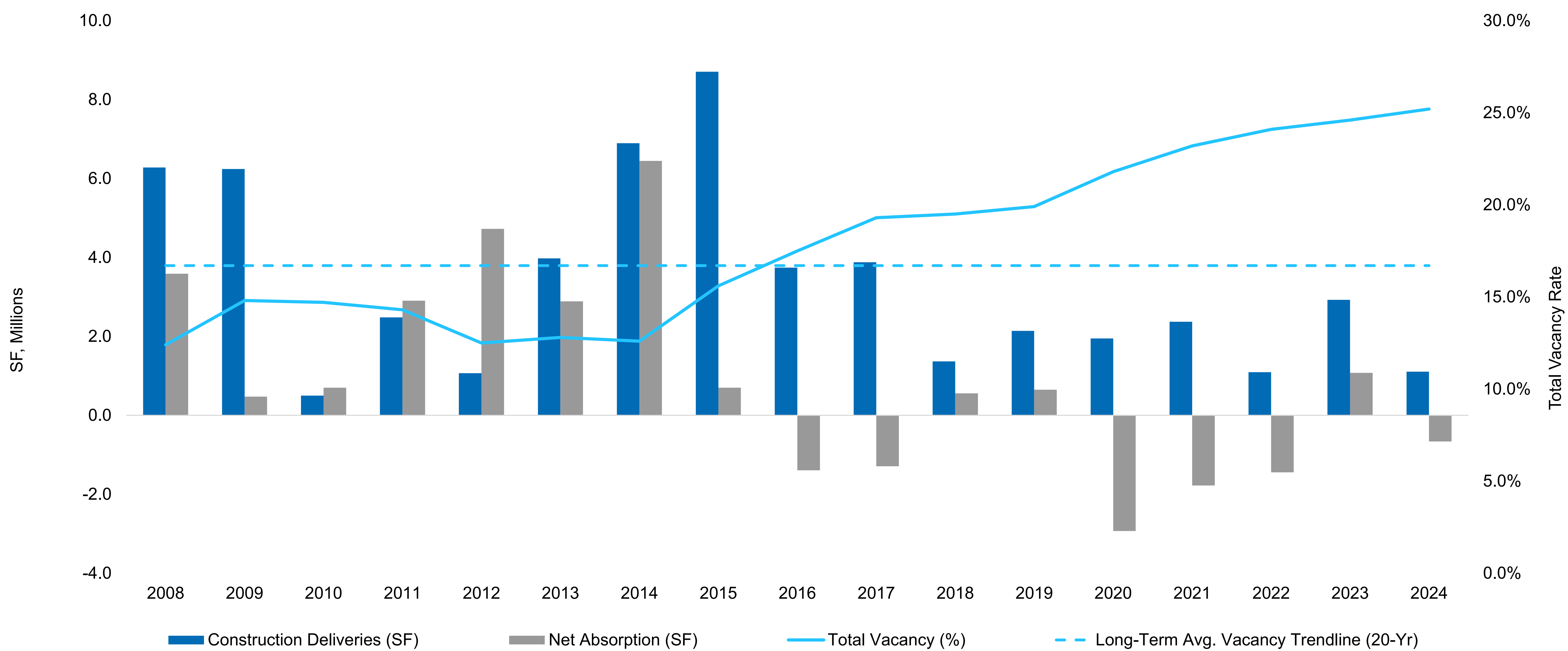
Leasing Market Fundamentals

Year Ends With Slowing Demand and Rise in Vacancy

The Houston office vacancy rate increased by 60 basis points year over year to 25.2% in the fourth quarter of 2024, well above the long-term average of 16.7%. Quarter over quarter, vacancy rates rose 30 basis points as absorption turned negative. Since the oil crash in 2015 to 2016, vacancy rates have steadily increased in the market as new deliveries outpaced annual absorption. However, as the construction pipeline empties, vacancy in the market is expected to stabilize in the near-term.

Historical Construction Deliveries, Net Absorption, and Vacancy

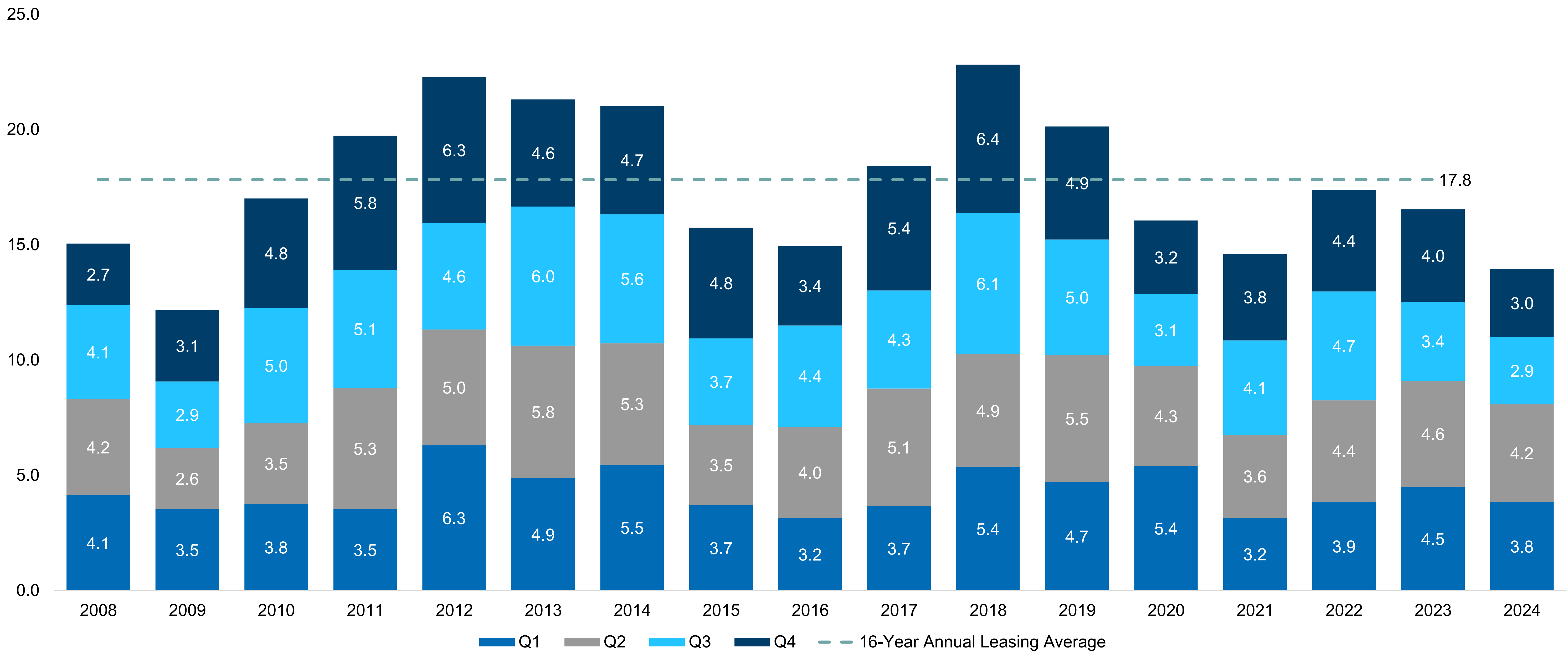


Source: Newmark Research, CoStar

Deal Activity Remains Below Quarterly and Annual Averages

Slowing leasing activity continued in the fourth quarter of 2024, totaling 3.0 MSF. Since 2008, fourth-quarter leasing activity has averaged 4.5 MSF, with the fourth quarter of 2024 roughly 34.7% lower than the historical average. Deal size averaged 3,854 SF in the fourth quarter of 2024, down 222 SF from a year ago. The annual leasing total for 2024 was roughly 14.0 MSF, well below the long-term annual leasing average of 17.8 MSF. The slowing leasing activity pace, down 22.1% in number of deals year over year, is largely attributed to occupiers waiting out the challenging debt environment and recent elections.

Total Leasing Activity (msf)

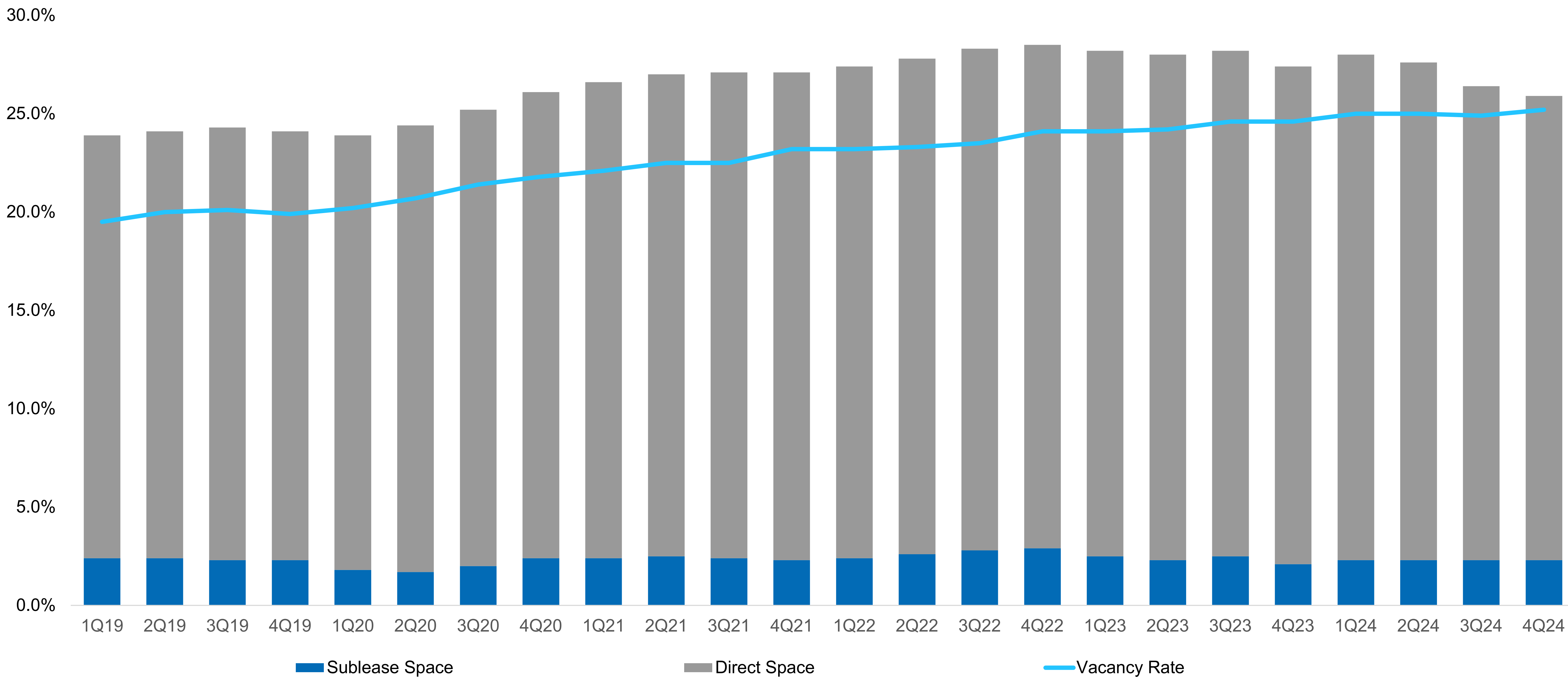


Source: Newmark Research, CoStar

Availability Continues to Fall but Remains Elevated

Sublease availabilities in the Houston market have declined since the oil crash in 2015 to 2016, remaining at a relatively steady level since 2019. Sublease availability in the market was flat throughout 2024, remaining at 2.3% for the fourth consecutive quarter. Direct availabilities have generally increased since the pandemic but have fallen from the recent high of 25.7% in the first quarter of 2024 to the current rate of 23.6%. Vacancies remain elevated alongside availabilities, at 25.2%.

Available Space as Percent of Overall Market

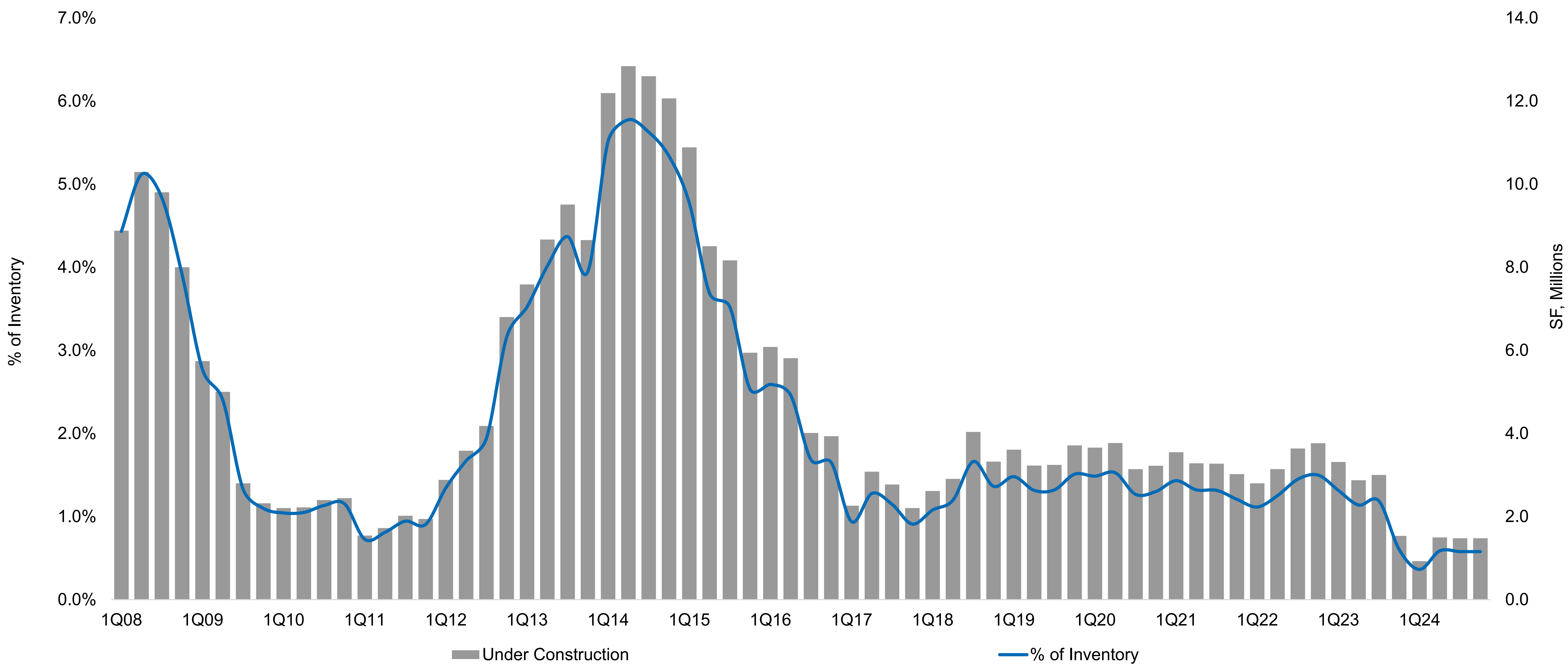


Source: Newmark Research, CoStar

Construction Activity Stationary Since Mid-Year

Construction activity has remained relatively muted in the market since 2016. As of the fourth quarter of 2024, the market had 1.5 MSF under construction*, with no new construction starts occurring since the second quarter of 2024. Under construction space accounts for 0.6% of the market's inventory, indicating there is less risk of overbuilding. Projects currently underway include The Ro (146,003 SF) and CityCentre Six (402,293 SF).

Office Under Construction and % of Inventory



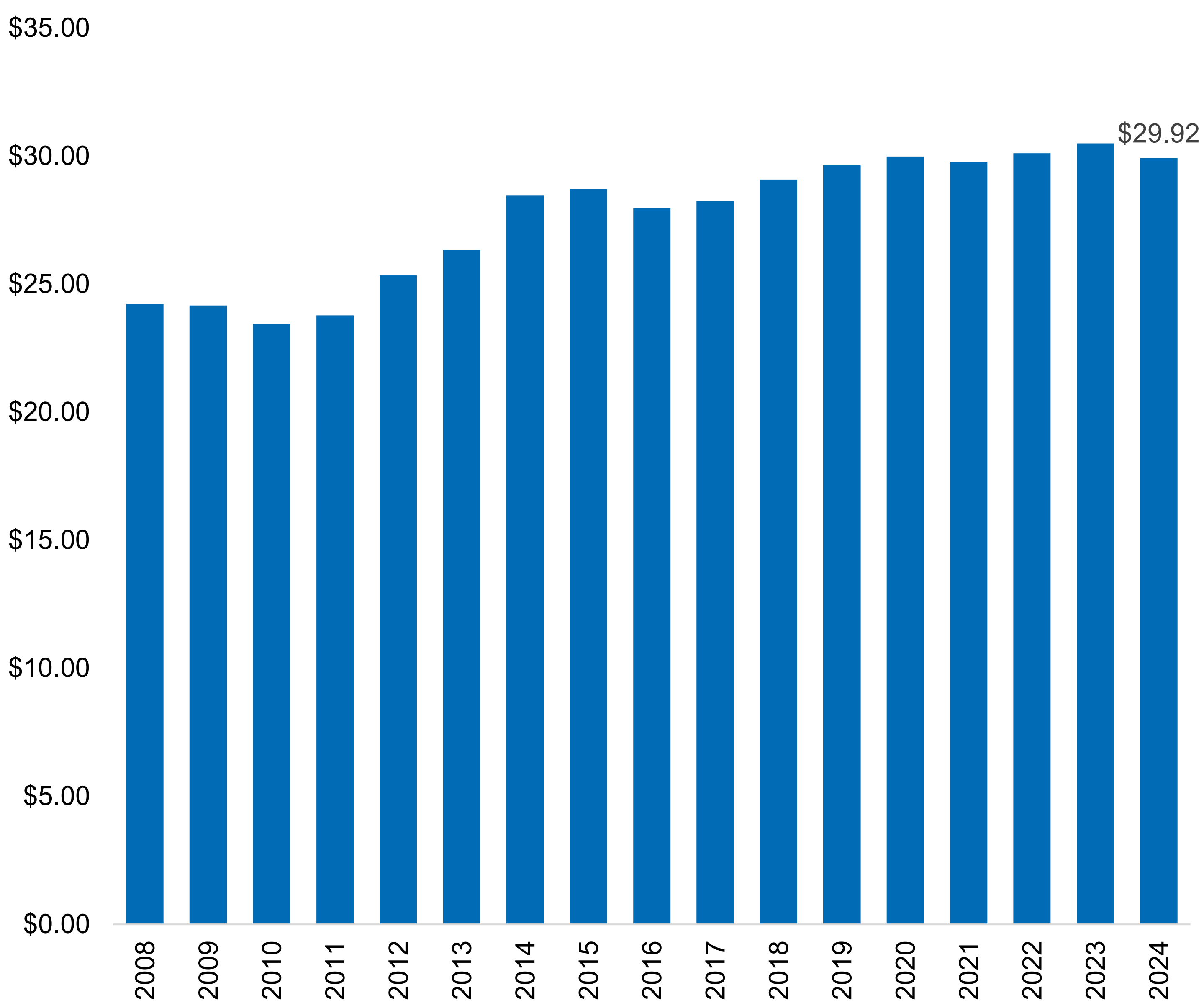
Source: Newmark Research, CoStar

* The bulk of space under construction in 4Q24 is medical office

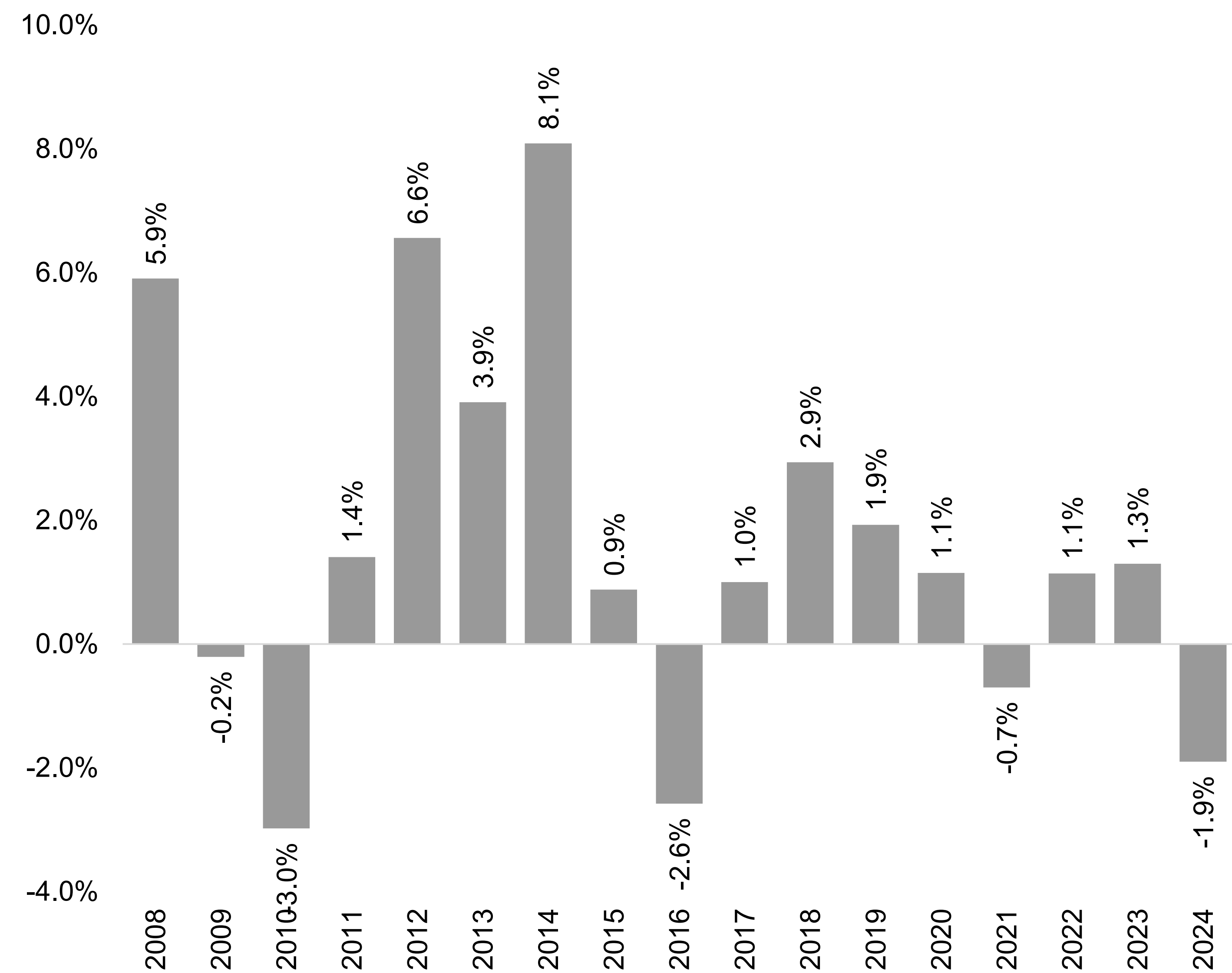
Rents Continue Trending Downward from All-Time High

In the fourth quarter of 2024, rents fell by 1.9% year over year to $29.92/SF and remain below the all-time high of $30.50/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

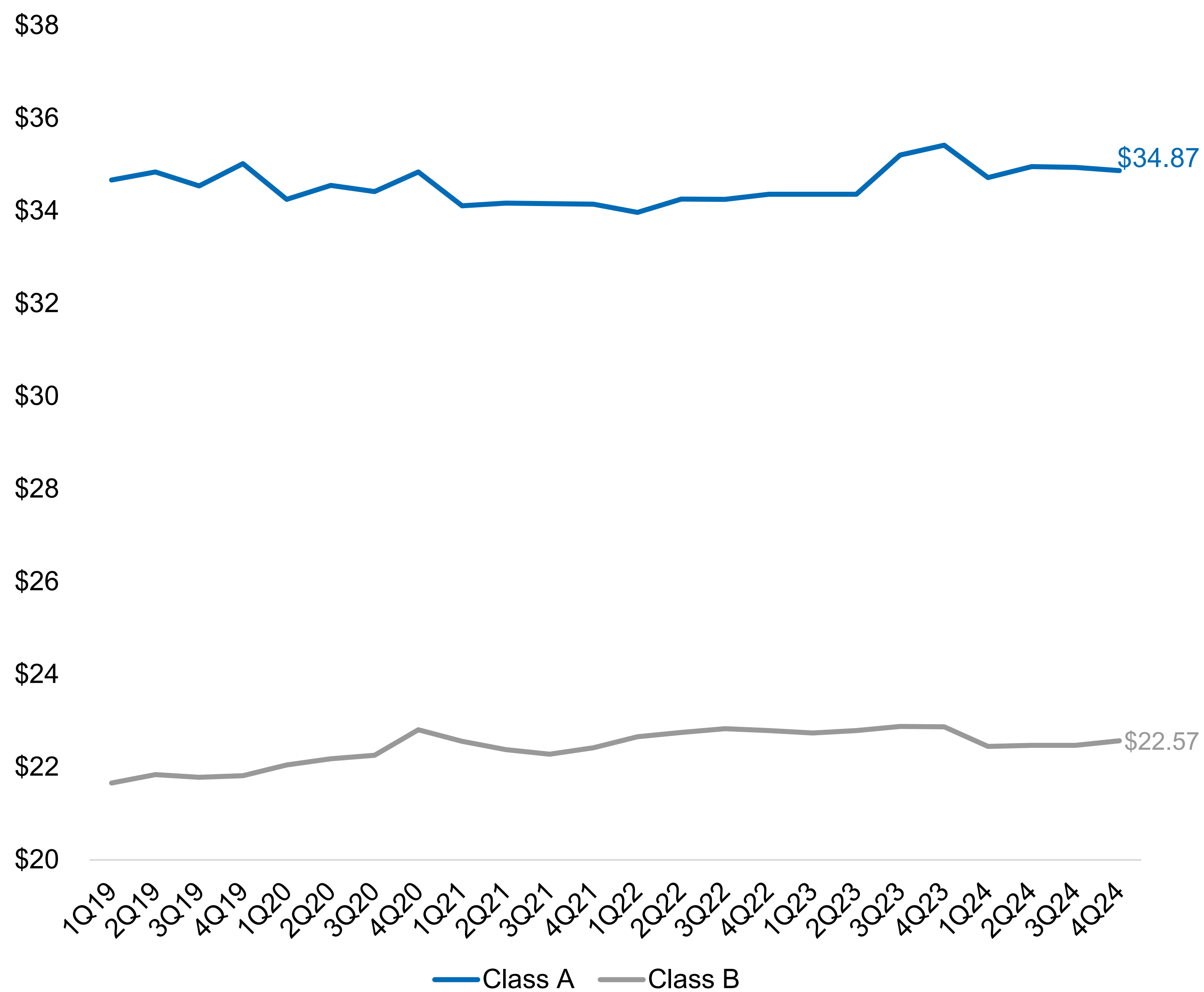


Source: Newmark Research, CoStar

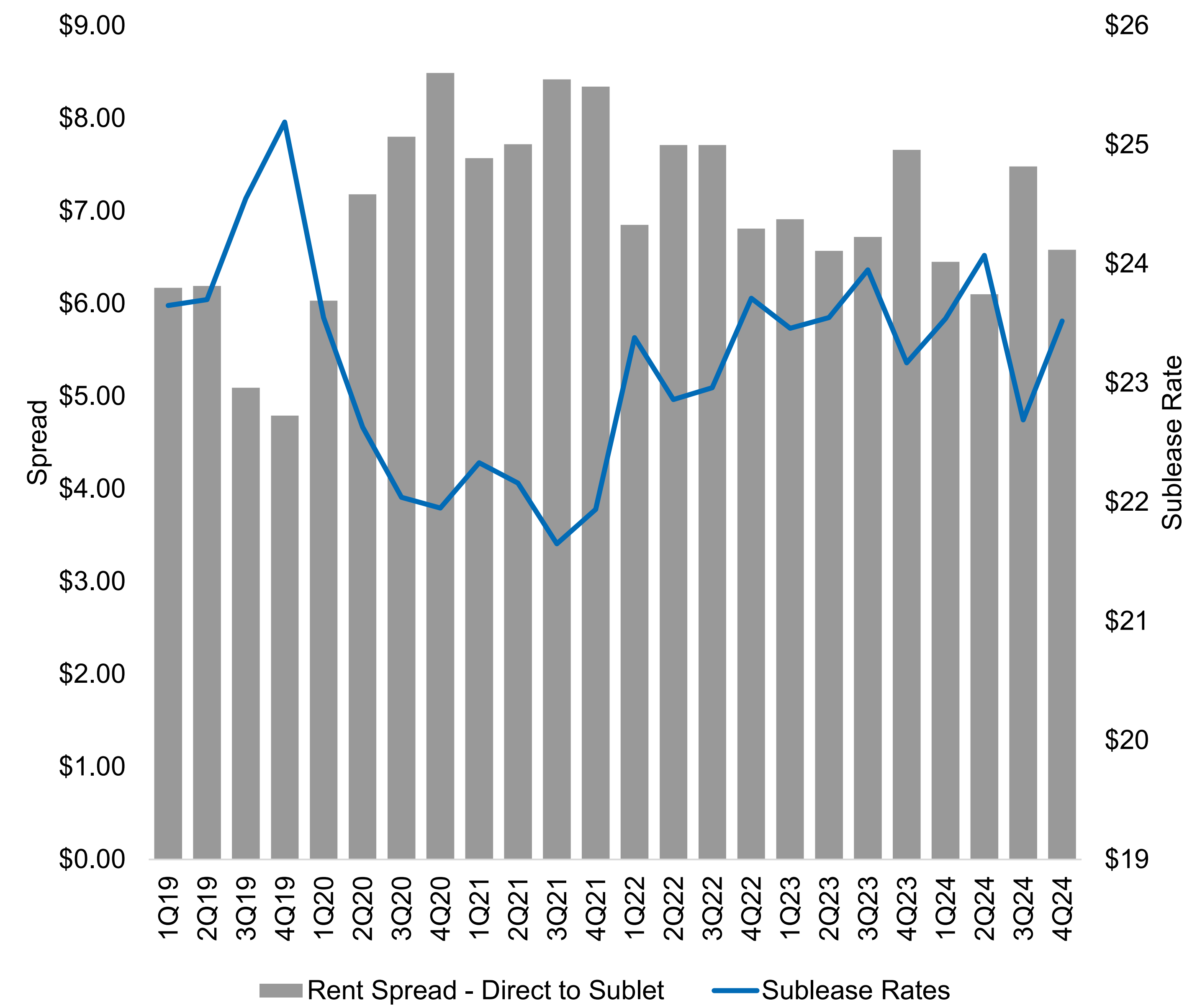
Rent Spread Narrows Slightly Among Class A Assets

Class A rents ended the fourth quarter of 2024 at $34.87/SF, while Class B rents were $22.57/SF. The $12.30/SF spread represents a 2.0% decrease year over year and reflects the greater demand for higher quality assets. Sublease rates increased to $23.52/SF in the fourth quarter of 2024, rising 3.7% quarter over quarter. The rent spread between direct and sublease rates narrowed in the fourth quarter of 2024, decreasing by 12.0% quarter over quarter to $6.58/SF.

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 fourth quarter of 2024, Class A space accounted for 58.9% of the market's leasing activity by SF, but only 34.2% of the market's deal volume. Average leases signed in Class A space were 6,640 SF and continue to remain larger than the average market deal size at 3,854 SF.

Notable 4Q24 Lease Transactions

Tenant	Building(s)	Submarket	Type	Square Feet
Plains All American Pipeline	Three Allen Center	CBD	Renewal/ Extension	260,000
Midstream energy company Plains All American Pipeline extended its 260,000 square foot lease at Three Allen Center through 2036.				
Subsea7	Westgate I	Energy Corridor	Renewal	177,100
Offshore energy engineering and construction company Subsea7 renewed its lease at Westgate I in the Energy Corridor.				
Quest Diagnostics	10900 Equity Drive	West Belt	Direct New	109,000
Medical laboratories company Quest Diagnostics signed a new lease for 109,000 SF at 10900 Equity Drive in the West Belt submarket.				
Ezee Fiber	5959 Corporate Drive	Southwest Fwy	Direct New	94,000
Ezee Fiber, an internet services company, leased 94,000 SF at 5959 Corporate Drive in the Southwest Fwy submarket.				
EDP Renewables	Hess Tower	CBD	Renewal	91,500
Renewable energy firm, EDP Renewables, renewed its 91,500 square foot lease at Hess Tower in the CBD.				
Freeport LNG	Three Allen Center	CBD	Renewal	66,000
Liquefied-natural gas exporter Freeport LNG signed a renewal for 66,000 SF at Three Allen Center.				

Source: Newmark Research, CoStar

Please reach out to your
Newmark business contact for this information

For more information:

Kirsten Kempf
Senior Research Analyst
Kirsten.Kempf@nmrk.com

Ching-Ting Wang
Head of Southeast Research
ChingTing.Wang@nmrk.com

Houston
1700 Post Oak Blvd.
2 Blvd. Place, Suite 250
Houston, TX 77056
t 713-626-8888

New York Headquarters
125 Park Ave.
New York, NY 10017
t 212-372-2000

nmrk.com

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