

Houston Industrial

Q1 2023

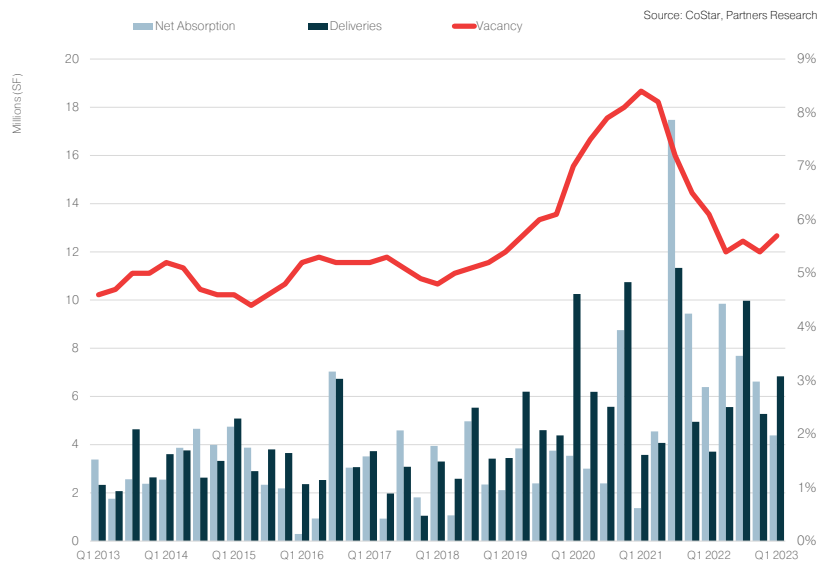
Executive Summary

Houston Industrial remains historically strong, kicking 2023 off with another robust quarter of activity

Houston Industrial Continues Strong Performance into 2023

By the end of Q1 2023, the vacancy rate showed minimal change, rising by 30 basis points quarter-over-quarter from 5.4% to a still-robust 5.7%. This was due to increased construction outpacing strong demand, indicating a healthy balance in market fundamentals. Developers started the year with 37.3 million sq. ft. in the construction pipeline—a 58% increase from 23.6 million sq. ft. in Q1 2022. Moreover, deliveries surged by 30% quarter-over-quarter and a remarkable 84% year-over-year, reaching 6.8 million sq. ft. by the end of Q1 2023. Industrial rental rates have also kept up with inflation, with a 4% increase from last year, currently standing at \$0.74 per sq. ft. Overall, the Houston industrial market's continued growth and stability seems to be showing no signs of slowing down, with increased construction and deliveries keeping pace with demand, and rental rates continuing to rise.

Supply & Demand



Houston's Economic Landscape: Slow to Minimal Growth in 2023

Several indicators suggest a best-case scenario of a mild recession in the U.S., which may result in minimal growth for Houston's economy in 2023. Although Houston's Purchasing Managers Index has been signaling job growth since August 2020, the February 2023 reading of 52.7 was 13.6% down from its peak in October 2021. Moreover, the HLI (Houston's Leading Index) declined by 2.1% over the three months ending in January, indicating a significant slowdown in job growth for the rest of 2023. Additionally, in mid-March, oil prices fell by over 4% to a three-month low after a U.S. inflation report and recent bank failures raised concerns about a new financial crisis that could reduce future oil demand. Brent futures fell by \$3.32, or 4.1%, to settle at \$77.45 a barrel, while U.S. West Texas Intermediate (WTI) crude fell by \$3.47, or 4.6%, to settle at \$71.33.

Key Market Indicators

	CURRENT Q1 2023	PRIOR QUARTER Q4 2022		PRIOR YEAR Q1 2022	
Vacant Total	5.7%	5.4%	▲	6.1%	▼
Vacant Direct	5.3%	5.2%	▲	5.8%	▼
Available Total	10.3%	10.0%	▲	9.0%	▲
Available Direct	9.3%	9.3%	■	8.4%	▲
Net Absorption (SF)	4,384,173	6,619,115	▼	6,392,157	▼
Leasing Activity (SF)	9,355,393	13,961,942	▼	15,322,834	▼
Construction (SF)	37,311,354	37,378,970	▼	23,678,649	▲
Deliveries (SF)	6,835,894	5,276,853	▲	3,712,029	▲
Avg Asking Rent (NNN/MO)	\$0.74	\$0.72	▲	\$0.67	▲
Inventory (SF)	712,650,015	705,814,121	▲	685,006,894	▲

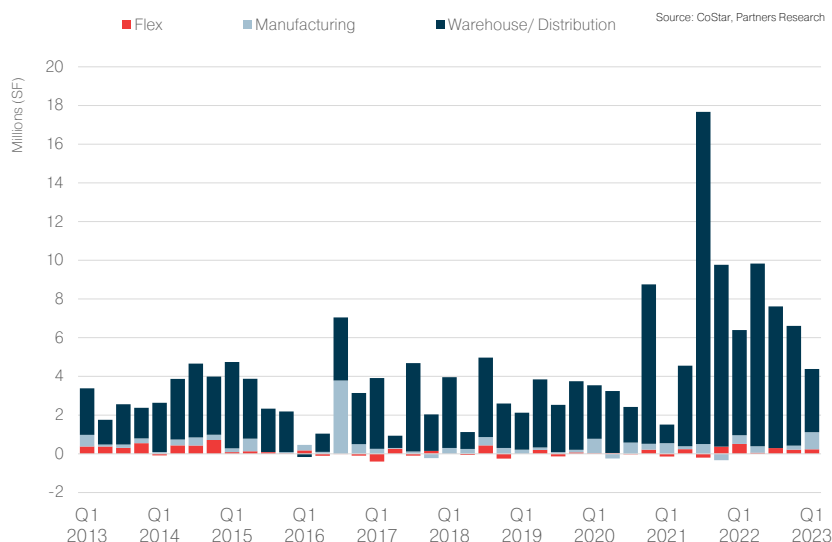
Market Overview

01

Fourteen Years of Positive Net Absorption

The industrial market's momentum continued into Q1 2023, with the first quarter marking 55 straight quarters—equal to over 14 years—that Houston recorded overall positive net absorption. Net absorption (4.3 million sq. ft.) remained positive, primarily due to 3.2 million sq. ft. in warehouse/distribution space and 596,000 sq. ft. in manufacturing space. Moreover, the market has yet to experience negative net absorption on the scale of Q2 2009, when it plummeted to negative 234,000 sq. ft.

Net Absorption

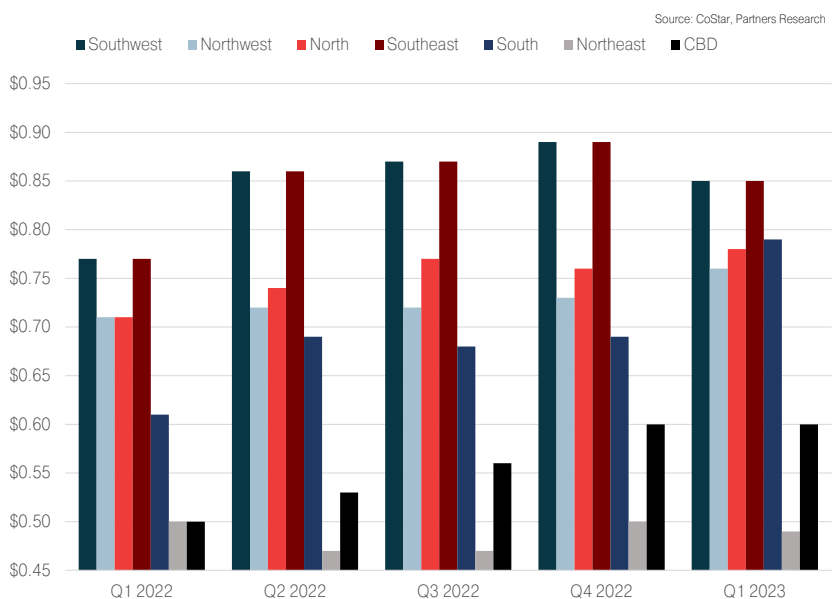


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Rental Rates Continue to Trend Upward

The average monthly rental rate for the Houston market was \$0.74 per sq. ft. as of the end of Q1 2023, up quarter-over-quarter at \$0.72 per sq. ft. and up from \$0.67 per sq. ft. year-over-year. The average monthly rate per square foot for Flex space stood at \$0.91, while the rates for manufacturing space and warehouse/distribution space were \$0.72 and \$0.69, respectively. The Southwest and Southeast submarkets currently have the highest monthly overall average rate at \$0.85 per sq. ft., followed by the South at \$0.79 per sq. ft. Overall, the Houston rental market continues to see an upward trend in rental rates, with Flex space commanding the highest rates.

Average Asking Monthly NNN Rent

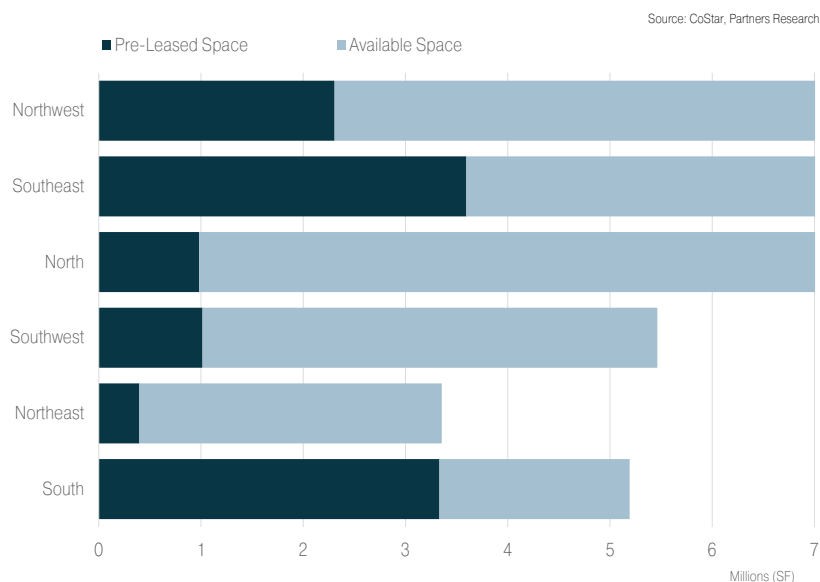


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Robust Construction Pipeline and Deliveries in 2023

Houston's industrial construction pipeline remains strong with a total volume of 37.3 million sq. ft., consisting of 36.6 million sq. ft. in warehouse/distribution space and 626,000 sq. ft. in flex space. The Southeast submarket leads in construction, with 8.9 million sq. ft.—or 24%—of all space under development, followed by the Northwest market with 19.3 million sq. ft. (or 19%). Meanwhile, Houston's deliveries totaled 6.8 million sq. ft., with the Southwest and Southeast submarkets accounting for 45% and 25%, respectively. Noteworthy projects set to debut in early 2023 include a 1.2 million-sq.-ft. spec distribution building at TGS Cedar Port DC4 in Baytown and a 3.1 million-sq.-ft., 240-acre business park offering industrial and warehouse space in Baytown.

Construction

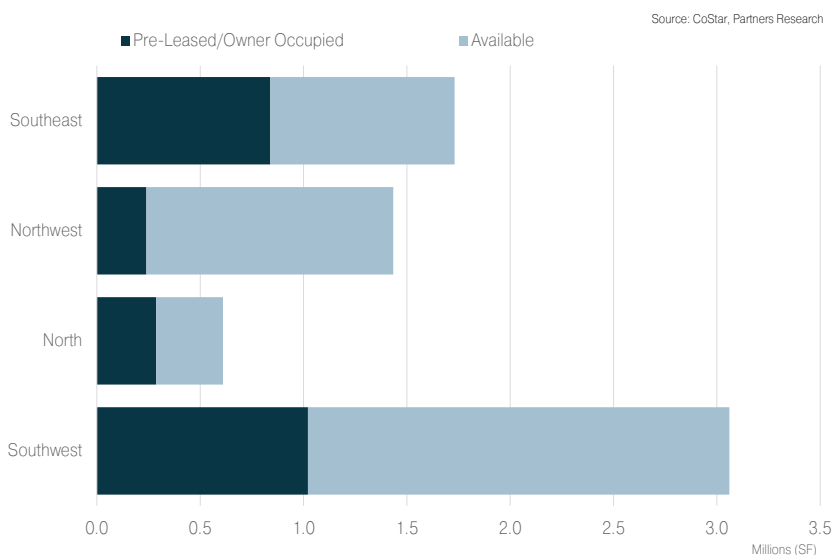


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Vacancy Rate Edges Up Slightly to 5.7%

The completion of industrial projects that began during the pandemic surge in warehouse demand combined with the slowing economy has contributed to a small rise in vacancy in the first quarter of 2023. The vacancy rate rose 30 basis points quarter-over-quarter to 5.7% during Q1 2023. It is worth noting that this percentage is still a fraction of the vacancy rates recorded in the 9%-10% range in the aftermath of the Great Recession and early 2000s recession, respectively. This could be a sign that the current economic downturn may not have as severe an impact on the industrial sector as previous recessions. Despite current challenges, the vacancy rate is not expected to exceed 6% even into 2024. This suggests that the industrial sector will remain relatively stable in the coming years.

Deliveries

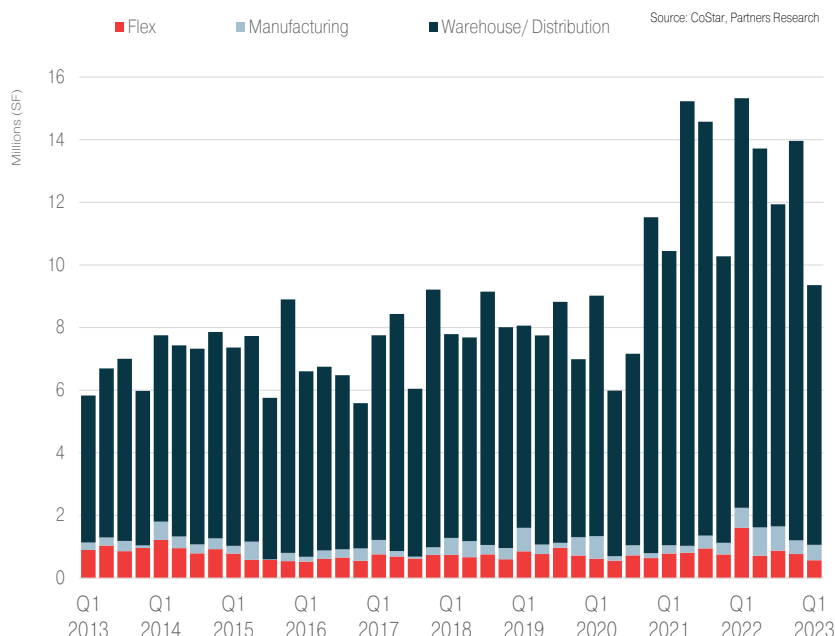


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Houston Industrial Leasing Down 33%

For all of the positivity surrounding the industrial market, one key metric was down during Q1 2023. The volume of signed lease transactions during the first quarter—comprised of new leases and renewals—was 9.3 million sq. ft., compared to the previous quarter's 13.9 million sq. ft. and a year ago at 15.3 million sq. ft. This pullback follows several years of considerable expansion in warehouse leasing as a surge in online shopping driven by the Covid-19 pandemic pushed companies to snatch up space to get goods closer to consumers. Among Q1's notable transactions was Tesla's massive 1 million-sq.-ft. warehouse lease in the Empire West Business Park in Brookshire.

Leasing Activity

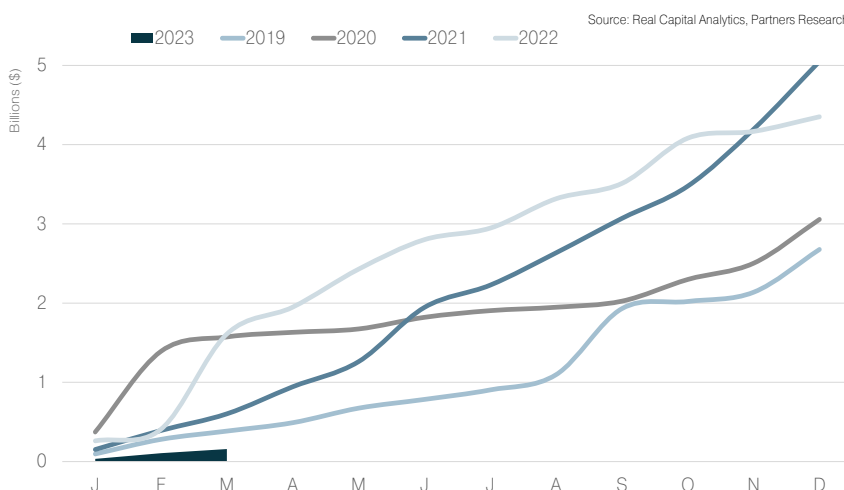


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Investment Sales Trends

Real Capital Analytics data reveals that Q1 2023 industrial sales volume in the Greater Houston region was \$156 million. This indicates a substantial 90% decrease compared to Q1 2022 sales volume of \$1.6 billion. In 2023, the majority of buyers comprised 91% private, 5% cross-border, and 4% institutional, while the majority of sellers included 77% private, 8% institutional, 10% user/other, and 5% user/other. Partners Capital, the investment platform of Partners Real Estate, was responsible for one of the largest industrial acquisitions of the quarter, buying Mitchelldale Business Park, a 12-building industrial flex portfolio covering 377,752 sq. ft. at 5400 Mitchelldale Street. The portfolio has a high occupancy rate of 95% with tenants from the transportation, airline, and textile industries. Despite the decline in Q1 2023 industrial sales volume in Greater Houston compared to the previous year, Partners Capital's acquisition of Mitchelldale Business Park is evidence that there are still promising investment opportunities available in the region's industrial real estate market.

Cumulative Monthly Sales Volume



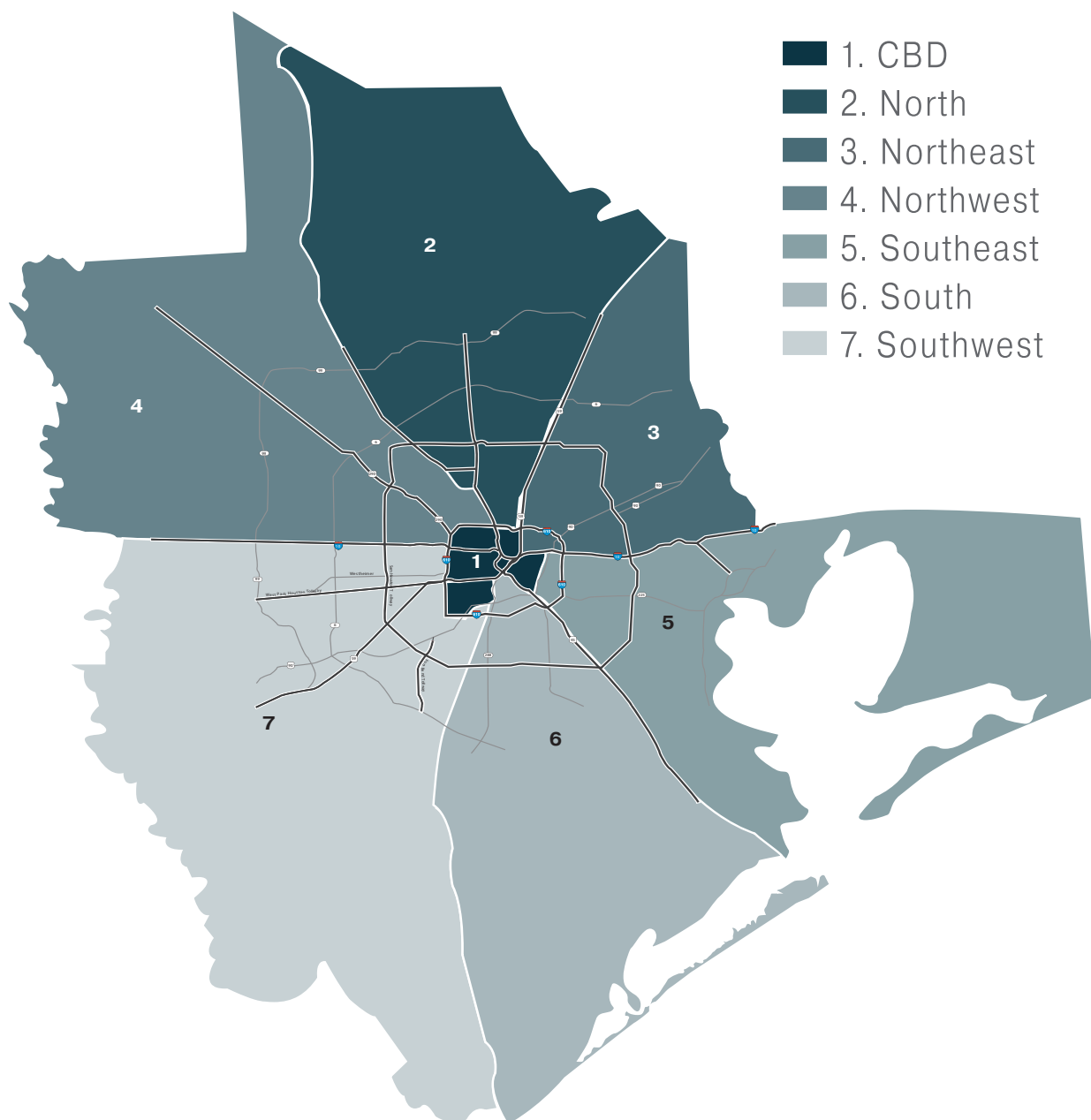
Market Overview

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Submarket Stats

Submarket Statistics (Total reflects Class A/B/C)	Total Inventory (SF)	Total Vacancy (SF)	Total Availability (%)	Q1 2023 Net Absorption (SF)	Q1 2023 YTD Net Absorption (SF)	Q1 2023 Leasing Activity (SF)	Under Construction (SF)	Overall Gross Avg Asking Rent (\$/PSF)
Houston Market Total	712,650,015	5.7	10.3	4,384,173	4,384,173	6,835,894	37,311,354	0.74
Flex	51,041,185	7.9	10.4	232,822	232,822	66,340	625,649	0.99
Manufacturing	94,172,541	1.6	3.4	884,338	884,338	130,000	0	0.72
Warehouse/Distribution	567,436,289	6.2	11.3	3,267,013	3,267,013	6,639,554	36,685,705	0.69
CBD Total	51,601,035	5.2	7.3	-414,374	-414,374	0	0	0.60
Flex	2,985,842	6.3	8.2	-33,231	-33,231	0	0	1.36
Manufacturing	7,979,112	1.0	4.2	-26,590	-26,590	0	0	0.34
Warehouse/Distribution	40,636,081	5.9	7.8	-354,553	-354,553	0	0	0.58
North Total	135,465,981	5.9	11.5	352,271	352,271	610,136	7,161,860	0.78
Flex	12,456,667	7.7	12.8	1,629	1,629	32,400	77,675	0.82
Manufacturing	15,586,830	0.4	2.4	-46,883	-46,883	0	0	0.80
Warehouse/Distribution	107,422,484	6.5	12.7	397,525	397,525	577,736	7,084,185	0.77
Northeast Total	46,599,400	5.5	11.5	119,112	119,112	0	3,335,101	0.49
Flex	644,698	10.6	10.6	-3,861	-3,861	0	0	0.70
Manufacturing	9,282,850	0.0	0.9	0	0	0	0	0.45
Warehouse/Distribution	36,671,852	6.9	14.0	122,973	122,973	0	3,335,101	0.49
Northwest Total	199,074,965	5.6	9.3	2,141,162	2,141,162	1,433,942	7,194,941	0.76
Flex	16,340,894	9.6	11.0	10,274	10,274	33,940	102,052	1.02
Manufacturing	26,241,817	2.8	4.4	381,173	381,173	130,000	0	0.74
Warehouse/Distribution	156,492,254	5.7	9.9	1,749,715	1,749,715	1,270,002	7,092,889	0.71
Southeast Total	129,498,081	5.2	9.6	944,439	944,439	1,731,130	8,963,565	0.74
Flex	3,310,940	8.2	10.4	17,280	17,280	0	39,000	0.98
Manufacturing	18,239,144	0.7	2.8	520,558	520,558	0	0	0.82
Warehouse/Distribution	107,947,997	5.9	10.6	406,601	406,601	1,731,130	8,924,565	0.71
South Total	50,890,443	3.4	8.0	103,891	103,891	0	5,192,863	0.79
Flex	2,561,623	4.9	12.2	18,951	18,951	0	108,364	1.25
Manufacturing	9,471,180	2.1	2.8	188	188	0	0	0.55
Warehouse/Distribution	38,857,640	3.5	8.8	84,752	84,752	0	5,084,499	0.75
Southwest Total	99,520,110	7.7	13.5	1,137,672	1,137,672	3,060,686	5,463,024	0.85
Flex	12,740,521	6.5	7.5	221,780	221,780	0	298,558	1.04
Manufacturing	7,371,608	3.2	5.7	55,892	55,892	0	0	1.03
Warehouse/Distribution	79,407,981	8.3	15.1	860,000	860,000	3,060,686	5,164,466	0.72

Houston Industrial Submarkets



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