

# AUSTIN OFFICE MARKET

## AUSTIN OFFICE DEALING WITH COVID IMPACT

The Austin office market saw a second quarter marked by a myriad of COVID related impacts as the global pandemic impacted much of the nation. Within the Austin market, while rental rates crept slowly upwards to \$36.37 across all building classes, the quarter saw over 300,000 square feet of negative absorption take place. This marks three out of the last four quarters that the once robust Austin office market has seen more giving back of space than taking. As a result, the overall vacancy rate has risen in the market to 12.3% at the close of the second quarter.

The market's vacancy rate has gained roughly 230 basis points year-over-year, indicating a potential imbalance towards more supply than demand. Overall, six submarkets tracked by Newmark Knight Frank have a vacancy rate of greater than 10%. Two submarkets, the East and Northwest had vacancy rates for the quarter surpassing 18%. Additionally, there has been almost 600,000 square feet of additional sublease space that has come to the market during the second quarter as companies begin to grapple with the new COVID normal for office space needs. As companies continue with a work from home policy, it is expected that the amount of sublease space on the market will continue to rise. %.

The first quarter absorption was positive 16,674 square feet. By comparison, the second quarter saw 304,869 square feet of space given back. Some submarkets performed stronger than others, as both the Northwest and Cedar Park submarkets had positive absorption greater than 30,000 square feet for the quarter. By comparison, the CBD had 330,000 square feet of negative absorption due to demand dropping for Class A space..

Overall rental rates rose nearly \$1.00/SF to \$36.37/SF in the quarter due to the rise in direct rates being correlated with a rise in sublet rates. However, the price discount between direct and sublet space has shrunk to \$0.19/SF. While several submarkets saw marginal rental rate growth, rates in the market have flattened, highlighting a lower demand through the first half of the year combined with the COVID 19 pandemic uncertainty within the market.

### CURRENT CONDITIONS

COVID 19 impact felt throughout market, but less drastic than other major Texas office markets

Just over 300,000 square feet of negative absorption across all building classes for the quarter

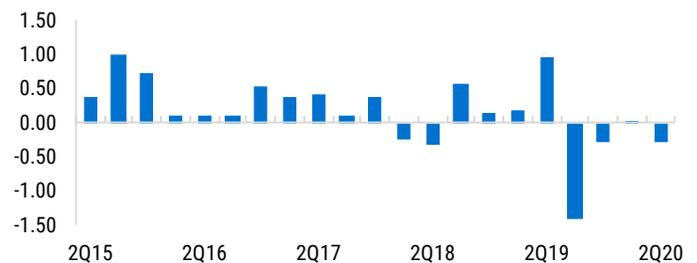
Leasing activity less than 500K SF; 1/4<sup>th</sup> the pre-pandemic mark

### MARKET ANALYSIS

#### Asking Rent and Vacancy



#### Net Absorption (SF, Millions)



### MARKET SUMMARY

	Current Quarter	Prior Quarter	Year Ago Period	12 Month Forecast
Total Inventory	70.0 MSF	69.4 MSF	69.2 MSF	↑
Vacancy Rate	12.3%	11.6%	9.2%	↑
Quarterly Net Absorption	-304,869	16,674	959,131	↑
Average Asking Rent	\$36.37	\$35.45	\$35.32	↓
Under Construction	7.1 MSF	6.6 MSF	4. MSF	↓
Deliveries	1	1	3	↑

Leasing activity in the CBD continues to lag behind the levels seen in 2018 and early 2019. Leasing activity in the first quarter dropped to 112,532 square feet, a negative 18.31% change from the previous quarter, and a decrease of 31.76% year-over-year. This trend continued into the second quarter, as only 92,558 square feet of leasing took place. The average asking rental rate in the CBD is \$48.99/SF, a decrease of just over \$2.00/SF from the previous quarter. Direct rates fell to \$51.21/SF while sublet rates dropped by \$2.00/SF, down to \$46.66/SF. Currently 3.67 million square feet of space is under construction in the CBD submarket, having added 600,000 square feet to the pipeline since last quarter.

The vacancy rate in the North submarket continues to be the lowest in the market, even with a rise to 5.4%. Rental rates fell significantly this quarter, rising to \$31.03/SF. The price discount between direct and sublease space is now at \$4.16/SF as direct asking rates decreased to \$30.22/SF for the quarter. Currently only Domain Tower 2 is actively under construction and will add 320,500 square feet to the submarket when it completes in August 2021, a drastic change from information reported in the fourth quarter of 2019.

The overall average rental rate on Austin's east side remains one of the biggest movers as the second quarter saw it close at \$35.43/SF, up significantly from the prior quarter. Direct rates increased by almost \$4.00/SF and are now at \$37.20/SF. Class A sublet space in the submarket saw a significant decrease \$30.05/SF, an decrease of over \$4.00/SF from the previous quarter.

Vacancy in the East Northeast submarket has been steadily increasing over the past quarter to 22.5%, up from 19.7% in the first quarter and the submarket maintains the highest vacancy rate market wide.

## LEASING ACTIVITY

Leasing activity plummeted 435,000 square feet of space, after stalling around 1.0 million for three consecutive quarters. Transactions totaled 102 for the quarter and the average lease size increased to 4,350 square feet. The largest leases reported during the quarter was Husch Blackwell taking 50,000 square feet at 111 Congress in the CBD and AMD taking roughly 35,000 square feet in the southwest submarket during the quarter.

## CRANE WATCH

Austin has maintained its robust development pipeline in to the new year, with at least fourteen office properties proposed across the market. The market currently has 7.0 million square feet of space under construction, with the bulk of construction taking place in the CBD. Construction has started on 6 X Guadalupe, Austin's tallest tower. The project is being developed by Lincoln Property Co. and will include 589,661 square feet of office space, 349 apartments and 11,675 square feet of retail space once complete. Block 185, at the corner of Cesar Chavez and Nueces streets, is also underway. The 723,000 square foot building is already 100% pre-leased by Google and features a prominent sail-like design. Google expects to move in sometime in 2023.

## AVERAGE ASKING RENT BY SUBMARKET

Average Asking Rent (\$/SF)			
	Current Quarter	2Q19	12 Month Change
CBD	\$48.99/SF	\$49.76/SF	↓
Southwest	\$38.70/SF	\$38.81/SF	↓
North	\$29.48/SF	\$32.07/SF	↓
Suburban	\$33.50/SF	\$33.32/SF	↑
Northwest	\$33.51/SF	\$32.99/SF	↑

## VACANCY BY SUBMARKET

Vacancy Rate (%)			
	Current Quarter	2Q19	12 Month Change
East/ Northeast	22.5%	18.2%	↑
South/Southeast	11.1%	10.3%	↑
Southwest	8.7%	10.8%	↓
Suburban	13.0%	11.1%	↑
Northwest	18.1%	11.3%	↑

Expected to deliver in April 2021, Indeed Tower is already pre-leased to tenants including Brown Advisory, Teacher Retirement System of Texas and Indeed. However, TRS is expected to sublease its 100,000 square feet of space and Indeed is the buildings largest tenant, taking up the top ten floors. 405 Colorado is expected to deliver in early 2021 and between DLA Piper and AB Private Investors, is already 45% pre-leased. Once complete, the building will contain 25 stories of office space.

WeWork Towers, a massive mixed-use project at Cesar Chavez and Red River was in the planning stages prior to the company's financial issues in 2019. The status of the project is currently unknown and could be impacted further by the company's recent credit downgrade to CCC+ from B- and subsequent placement on the watch list by S&P. This is a project to watch as it would be one of Austin's largest projects should planning proceed.

Additionally, while lowered interest rates typically make it easier to borrow, according to Brookings, despite the Federal Reserve's decision to slash interest rates, firms may still have difficulty borrowing due to the overall uncertainty surrounding COVID-19's economic impact. So while it may be a good time for firms to look in to purchasing debt and assets, the process could still prove difficult for buyers and developers.

## ECONOMY

The unemployment rate in Austin was 2.6% in January, a slight uptick but still well below both the state and national unemployment rates, each at 3.5%. Prior to the U.S. outbreak of the coronavirus (COVID-19), data from earlier in the first quarter pointed to a robust economy in Austin.

Now that the economy has had a chance to fully be impacted by the COVID pandemic (and to a smaller extent in Austin, the oil price uncertainty), it can be seen that the robust economy of the 1<sup>st</sup> quarter in Austin is no more. Unemployment rates have risen drastically from sub 4.0% pre-COVID to now nearly 11% within the city. Additionally, across a multitude of employment sectors, 12 month growth percentages have shifted negative as the city and economy continue to shed jobs while adjusting to the pandemic. While the full impacts of COVID-19 on the Austin economy are yet to be seen, it is important to pay attention to unemployment levels, which were at 10-year lows in the months before the outbreak. Unemployment filings surged to an all-time high in the third week of March with 3.28 million people filing for relief. Industries such as Leisure and Hospitality, which have already shed jobs in recent months, are most at risk for additional job loss but may have a quick recovery period.

Given the tech industry's impact on in-migration and population growth, layoffs and lack of funding for startups could put a strain on secondary industries, such as construction and home building. As Moody's Analytics notes, the volatility of the tech industry has been a risk for the Austin metro all along, but how the industry responds to COVID-19 will be certain to impact Austin's economy in both the short and long-term

## LEASE/USER TRANSACTIONS

Tenant	Building	Submarket	Type	Square Feet
Husch Blackwell	111 Congress	CBD	Renewal	46,000
AMD	7000 William Cannon Dr W	Southwest	Direct/New	34,995
Unknown Tenant	504 Lavaca St	CBD	Direct/New	19,231

## SELECT SALE TRANSACTIONS YTD 2020

Buyer/Seller	Building	Submarket	Sale Price	\$/SF
PRP Real Estate Investment Management/ Karlin Real Estate	13011 McCallen Pass (2 Property Portfolio Sale)	Northeast	\$102,157,297	\$499.79
TBD	1507 Nueces St	CBD	\$2,450,000	\$408

## SUBMARKET STATISTICS

	Total Inventory (SF)	Under Construction (SF)	Total Vacancy Rate	Qtr Absorption (SF)	YTD Absorption (SF)	Direct Asking Rent (Price/SF)	Sublet Asking Rent (Price/SF)	Average Asking Rent (Price/SF)
<b>CBD Total</b>	<b>11,859,752</b>	<b>3,678,781</b>	<b>8.7%</b>	<b>-339,870</b>	<b>-293,944</b>	<b>\$51.21</b>	<b>\$46.68</b>	<b>\$48.99</b>
Class A	8,190,239	3,678,781	10.1%	-330,500	-299,841	\$52.99	\$46.91	\$49.76
Class B	3,037,553	0	6.0%	-8,448	7,995	\$49.44	\$45.94	\$48.16
<b>Cedar Park / Georgetown Round Rock Total</b>	<b>3,624,013</b>	<b>0</b>	<b>12.7%</b>	<b>42,708</b>	<b>85,301</b>	<b>\$30.50</b>	<b>\$32.25</b>	<b>\$30.60</b>
Class A	1,843,183	0	16.9%	17,394	82,993	\$33.30	\$35.87	\$33.46
Class B	1,530,371	0	9.5%	25,134	2,588	\$27.54	\$28.50	\$27.63
<b>Central West Central Total</b>	<b>5,104,701</b>	<b>518,228</b>	<b>7.1%</b>	<b>-1,868</b>	<b>18,485</b>	<b>\$34.10</b>	<b>\$35.75</b>	<b>\$34.37</b>
Class A	1,230,738	384,114	6.6%	2,475	45,365	\$45.27	\$38.59	\$42.27
Class B	2,832,851	134,114	8.9%	1,428	-18,393	\$33.37	\$32.31	\$33.27
<b>East Northeast Total</b>	<b>6,510,491</b>	<b>449,533</b>	<b>22.5%</b>	<b>-45,465</b>	<b>32,208</b>	<b>\$37.20</b>	<b>\$30.05</b>	<b>\$35.43</b>
Class A	1,784,298	199,436	25.4%	-29,986	-91,503	\$46.35	\$36.00	\$44.19
Class B	4,137,584	237,097	23.2%	-2,312	19,231	\$26.60	\$17.82	\$21.77
<b>North Total</b>	<b>7,888,246</b>	<b>330,000</b>	<b>5.4%</b>	<b>-20,087</b>	<b>2,105</b>	<b>\$30.22</b>	<b>\$36.38</b>	<b>\$31.03</b>
Class A	3,583,997	330,000	2.6%	-19,808	-13,502	\$34.80	-	\$34.80
Class B	4,218,236	0	7.8%	-279	15,607	\$28.39	\$36.38	\$29.80
<b>Northwest Total</b>	<b>17,759,028</b>	<b>0</b>	<b>18.1%</b>	<b>30,799</b>	<b>61,009</b>	<b>\$34.38</b>	<b>\$29.80</b>	<b>\$33.59</b>
Class A	10,616,049	0	23.5%	68,282	41,701	\$37.08	\$32.90	\$36.01
Class B	6,949,710	0	10.3%	-37,582	105,033	\$31.45	\$24.65	\$30.10
<b>South Southeast Total</b>	<b>6,266,656</b>	<b>1,193,310</b>	<b>11.1%</b>	<b>12,532</b>	<b>-1,405</b>	<b>\$37.70</b>	<b>\$43.97</b>	<b>\$37.89</b>
Class A	1,347,543	1,193,310	11.2%	45,507	42,094	\$36.24	-	\$36.24
Class B	4,090,789	0	10.1%	-34,015	38,004	\$37.08	\$21.33	\$34.86
<b>Southwest Total</b>	<b>11,003,910</b>	<b>407,962</b>	<b>8.7%</b>	<b>16,382</b>	<b>-128,410</b>	<b>\$37.27</b>	<b>\$35.41</b>	<b>\$36.88</b>
Class A	7,767,759	407,962	8.4%	47,856	-93,503	\$40.99	\$36.62	\$39.67
Class B	3,143,013	0	9.9%	-37,752	-39,540	\$33.32	\$28.21	\$32.83
<b>Suburban Total</b>	<b>58,157,045</b>	<b>3,551,235</b>	<b>13.0%</b>	<b>35,001</b>	<b>56,059</b>	<b>\$34.92</b>	<b>\$31.79</b>	<b>\$34.34</b>
Class A	28,173,567	3,047,304	15.0%	131,720	-71,036	\$38.78	\$34.63	\$37.85
Class B	26,902,554	503,931	11.6%	-85,198	125,095	\$31.97	\$27.66	\$31.28
<b>Austin Total</b>	<b>70,016,097</b>	<b>7,138,016</b>	<b>12.3%</b>	<b>-304,869</b>	<b>-288,222</b>	<b>\$36.42</b>	<b>\$36.23</b>	<b>\$36.37</b>
Class A	36,363,806	6,626,085	13.9%	-198,780	-371,754	\$40.69	\$39.31	\$40.30
Class B	29,940,087	503,931	11.0%	-93,646	129,818	\$32.87	\$30.23	\$32.41

## SELECT TEXAS MARKETS- LARGEST SUBMARKETS

Austin, June 2020

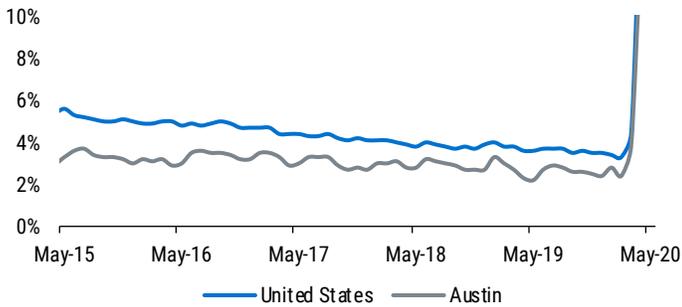
Top 10 Submarkets by Rentable Square Feet

Rank	Submarket	RSF
1	Far North Dallas	61.1 M
2	DFW Las Colinas	41.6 M
3	Houston CBD	39.7 M
4	Richardson/Plano	35.1 M
5	Dallas CBD	31.2 M
6	DFW Mid-Cities	28.0 M
7	HOU Galleria/Uptown	23.4 M
8	HOU Energy Corridor	22.4 M
9	DFW LBJ Freeway	21.7 M
10	Austin Northwest	17.8 M

Source: Newmark Knight Frank

## UNEMPLOYMENT RATE

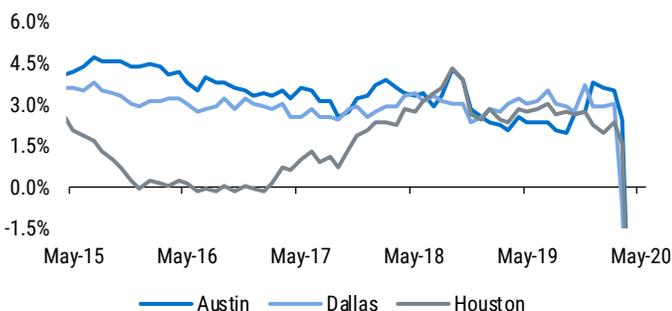
Not Seasonally Adjusted



Source: U.S. Bureau of Labor Statistics

## PAYROLL EMPLOYMENT—SELECT TEXAS MARKETS

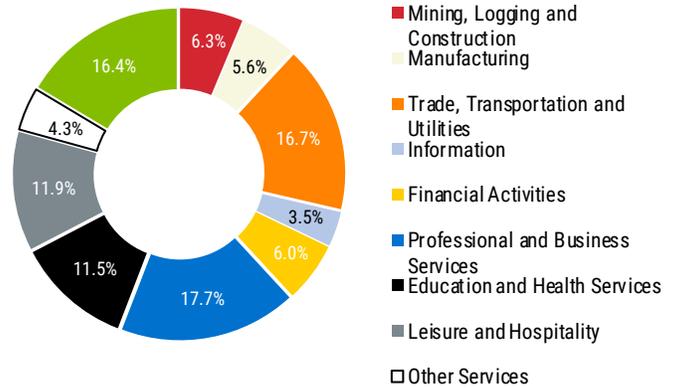
All Items, 12-Month % Change, Not Seasonally Adjusted



Source: U.S. Bureau of Labor Statistics

## EMPLOYMENT BY INDUSTRY

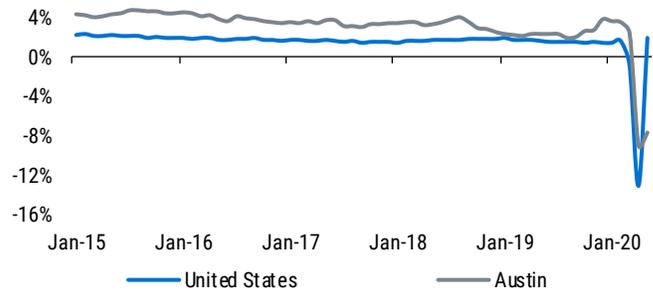
Austin, May 2020



Source: U.S. Bureau of Labor Statistics

## PAYROLL EMPLOYMENT

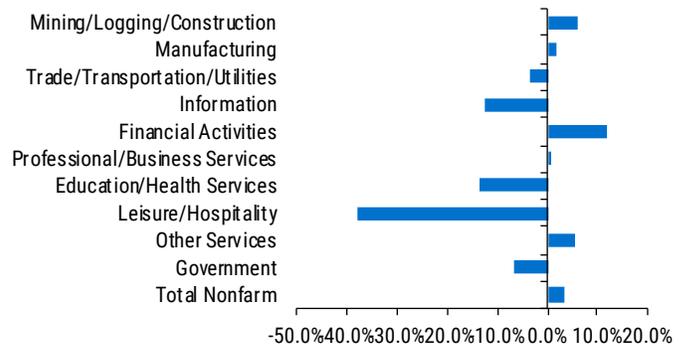
Total Nonfarm, Not Seasonally Adjusted, 12-Month % Change



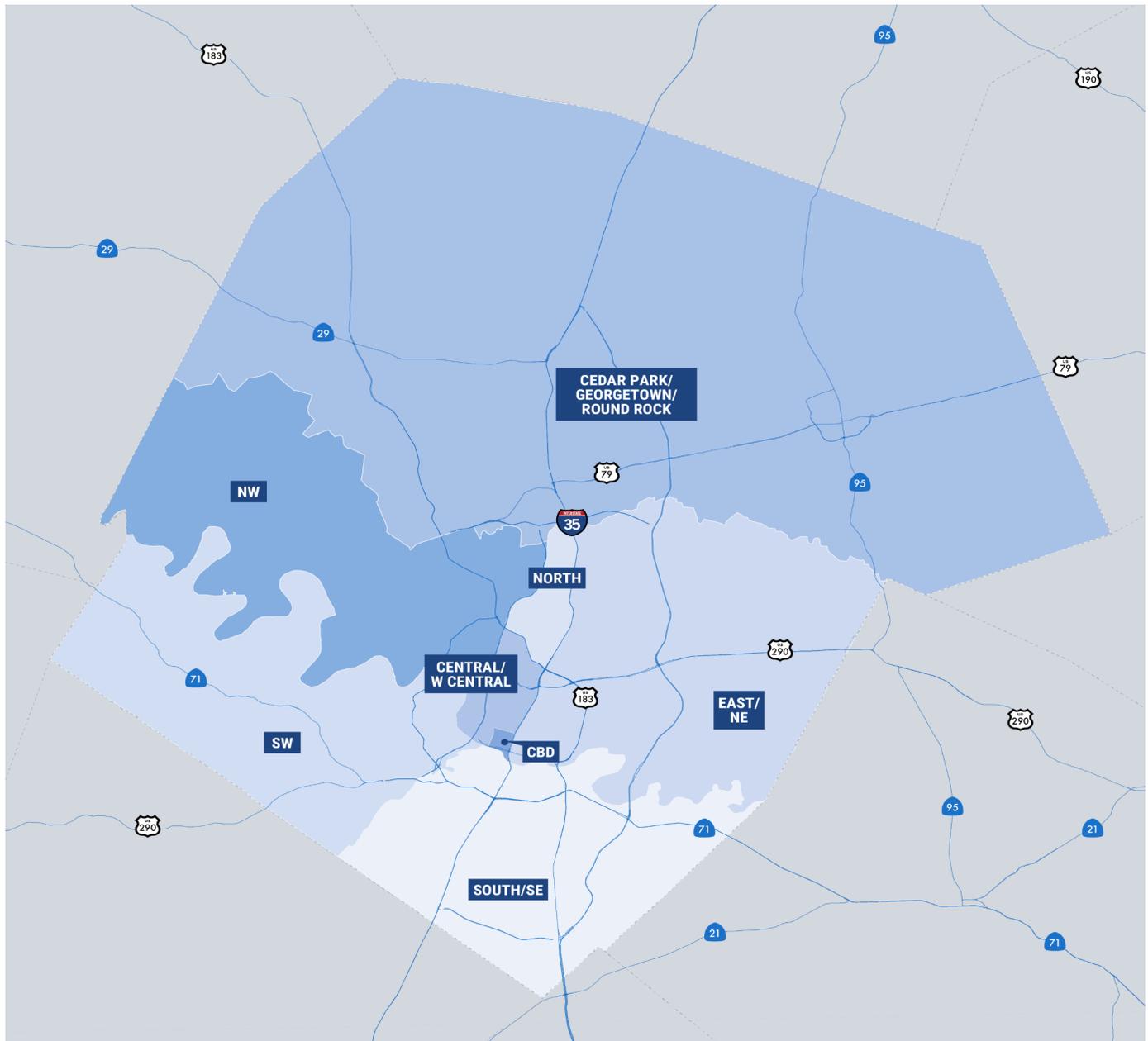
Source: U.S. Bureau of Labor Statistics

## EMPLOYMENT GROWTH BY INDUSTRY

Austin, May 2020, 12-Month % Change, Not Seasonally Adjusted



Source: U.S. Bureau of Labor Statistics



## GRAHAM HILDEBRAND

Director – Texas Research  
713.599.5151  
Graham.hildebrand@ngkf.com

## WALTER BRUTON

Coordinator – Texas Research  
469.467.2042  
Walter.bruton@ngkf.com

Newmark Knight Frank has implemented a proprietary database and our tracking methodology has been revised. With this expansion and refinement in our data, there may be adjustments in historical statistics including availability, asking rents, absorption and effective rents. Newmark Knight Frank Research Reports are available at [www.ngkf.com/research](http://www.ngkf.com/research)

All information contained in this publication is derived from sources that are deemed to be reliable. However, Newmark Knight Frank (NKF) has not verified any such information, and the same constitutes the statements and representations only of the source thereof, and not of NKF. Any recipient of this publication should independently verify such information and all other information that may be material to any decision that recipient may make in response to this publication, and should consult with professionals of the recipient's choice with regard to all aspects of that decision, including its legal, financial, and tax aspects and implications. Any recipient of this publication may not, without the prior written approval of NGKF, distribute, disseminate, publish, transmit, copy, broadcast, upload, download, or in any other way reproduce this publication or any of the information it contains.