

Houston, Texas

Tenant's Guide ■ North American Markets ■ Second Quarter 2010

Overview

The Houston office market continued to send mixed signals during the second quarter. While citywide vacancy increased to 19.8%, and the metropolitan area reported negative absorption of 42,509 SF, asking rental rates held steady in the most popular submarkets. Downtown class A office rents ended the quarter at \$36.01/SF, compared to \$36.40/SF one year ago. In suburban markets, class A asking rents increased slightly from a year ago, ending the second quarter at an average of \$27.60/SF, compared to \$27.15/SF at the end of the second quarter 2009. Several recently completed buildings, hampered with high rent benchmarks, are struggling to find large anchor tenants, but existing properties in close-in submarkets like Greenway and the Galleria are well leased.

While a handful of building sales occurred during the quarter, most notably the sale of Energy Center I to Wells REIT, opportunistic office buyers are still waiting in the wings. Houston's sublease inventory fell slightly during the second quarter, ending at 4,127,820 SF.

The capital market shows little sign of recovering, and lenders are cautious to approve any lease transactions that could be a future risk, demanding corporate guarantees on large leases with heavy up-front lease costs.

Market Trends

- The impact of any job loss as the result of the Gulf oil spill has yet to play out in the office market.
- Expect more ownership changes as debt matures over the next 12 months.
- Increased rental rates in class A space reflects the move of tenants into quality space at competitive rates, raising occupancy rates and decreasing the number of choices of second generation class A space.
- Job growth is starting to pick up in the hospitality and health care areas, but is slow to pick up in the industries that impact office occupancy.
- Buildings impacted by the CMBS loans are diminishing the number of options for tenants in the market.

Tenant's Perspective

Should the economic forecast continue to be bleak, its impact could drive the market further away from recovery. Tenants in the market will be the beneficiaries of concessions from savvy landlords adjusting to slow summer month leasing activity or proactively responding to a possible slowdown in energy, the metropolitan area's major industry.

Major Transactions

Tenant/Buyer	Size	Type	Lease/Sale
Energy Center I	332,000	Office	Sale
16225 Park 10 Place	163,000	Office	Sale
U S Attorney's Office	132,000	Office	Lease
GDF Suez	127,673	Office	Lease
5850 San Felipe	102,000	Office	Sale
Merrill Lynch	100,000	Office	Lease
MMI	87,000	Office	Lease
AON	46,797	Office	Lease
Sutherland Asbill & Brennan	42,000	Office	Lease
Multiphase Solutions	27,306	Office	Lease

Vacancy Rate



Average Rental Rates

CBD	Q4 2009	Q1 2010	Q2 2010
Class A Office	\$35.63	\$36.45	\$36.01
Class B Office	\$22.99	\$22.99	\$24.54
Suburban	Q4 2009	Q1 2010	Q2 2010
Class A Office	\$27.30	\$27.30	\$27.60
Class B Office	\$18.30	\$18.30	\$18.34
R&D	\$9-\$15	\$9-15	\$9-13

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