DALLAS

AVISON YOUNG

EXECUTIVE SUMMARY

- Dallas will continue to be one of the most active construction markets in the country, with more than 50 million sf (msf) of commercial product delivering in 2020, along with an additional 50 msf in expected construction starts scheduled to take place.
- Multi-Family will likely remain the investor darling as major population growth and limited single-family availability continue to push area residents towards renting, thus maintaining strong demand.
- Office will continue to see a flight-to-quality, where newer and renovated space witness the majority of absorption, putting more pressure on dated product to refresh or get left behind.
- Industrial will maintain the strong leasing velocity it has experienced for the last two years, keeping vacancy around 5% despite record-setting construction activity.

Dallas fundamentals remain solid. While no longer performing at the breakneck pace of 2016 and 2017, the market as a whole is still witnessing near-record levels in regards to construction, absorption and sales. Underlying threats that will need to be addressed include flight-to-quality patterns that are putting large supplies of 1970s and 1980s product at risk of being obsolete if not renovated, along with notable cost-of-living increases that threaten to make corporate relocations less appealing. In the near term, however, Dallas is likely remain one of the strongest performing metros in the U.S.

Dallas-Fort Worth (DFW) will continue to be a hotbed of activity in 2020. The metro has consistently been a top performer in key metrics such as construction, net absorption, sales volume, population growth and job growth. These performance indicators are set to maintain their positive trajectories, even in the face of slowing global growth and economic uncertainty. DFW has added roughly 100,000 jobs per year for the last several years. Also of note, DFW has added more than 1 million people since April 2010 when the area's economic recovery began post-Great Recession. This explosive growth, coupled with DFW's welcoming business climate and strong labor pool, will likely keep the metro positioned for another impressive performance in 2020.

Within the commercial property markets, Avison Young expects DFW to see moderate rent growth across all asset types, with industrial assets likely seeing the highest percentage of growth at roughly 4% year-over-year.

DFW's construction pipeline remains impressive, with more than 50 msf of commercial product set to deliver during 2020. The vast majority of these assets are "premium class" buildings, which will fuel an ongoing flight to quality as more tenants move to occupy newer, more high-end product. This trend poses a moderate threat across multiple fronts. Office absorption has significantly favored new and renovated product in recent years. This trend is putting pressure on older buildings, which DFW has in abundance, and could create a unique sort of bubble in which the market isn't overbuilt per se, but there could soon be a glut of older, non-stabilized properties.

Within the multi-family sector, luxury apartments are essentially the only class being built in the area, which is putting price pressures on all DFW apartments as the metro struggles to provide housing for a rapidly growing population. This has essentially created the beginnings of an affordability crisis in the metro, which has the potential to make corporate relocations less desirable if the area's cost of living becomes less competitive. A lack of affordable workforce housing will drive a large segment of DFW's population farther away from the metro's urban centers, a trend that could shift demographic profiles for recruiting in certain economic sectors, potentially impacting the ability of businesses to find talent, and in turn changing where they choose to locate.

On the sales side, Dallas will likely continue to be a premier investment market, with the liquidity and transaction volume of a gateway market, but with product at a significantly lower cost than can be found in major coastal cities. With recently reduced interest rates likely to remain low through 2020, investors will continue to be drawn to area real estate assets as they search for yield. If momentum continues as it has in recent years, DFW should see at least $15 billion in commercial property sales in 2020.

Looking ahead at larger trends across the metro, certain broad patterns should emerge not just for 2020, but for the years to come, and will potentially shape new ways in which the DFW market performs. Tenants are increasingly demanding flexibility related to office space and leasing terms, as evidenced by the rapid rise of coworking concepts and shorter lease options. Expect this trend to continue, with more landlords seeking to integrate flexible options

KEY MARKET METRICS – 2020 EXPECTATIONS

Annual growth rates, estimated for year-end 2020 vs year-end 2019.

	OFFICE	RETAIL	INDUSTRIAL
Rental Growth	↑	↑	↑↑
Vacant Space	↓	→	→
Construction Levels	→	↓	↑
Leasing Volume	↓	→	↑
Investment Volume	→	→	→

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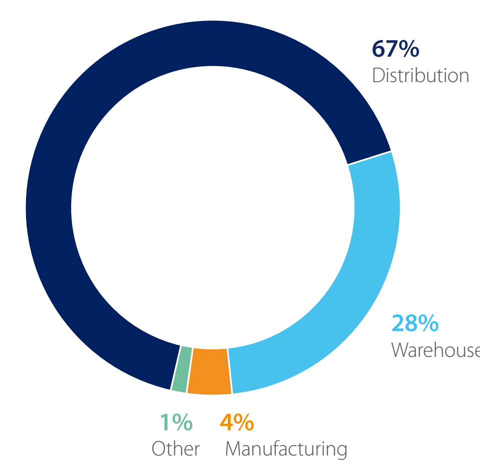
INDUSTRIAL UNDER CONSTRUCTION



Source: CoStar Realty Information, Inc.

into their operations. Within coworking specifically, WeWork received the most headlines for 2019 for all the wrong reasons, but their challenges do not represent the industry as a whole. Coworking in DFW will likely continue to expand through varied providers, the vast majority of which are smaller, local operators. WeWork itself only accounts for 17% of DFW's 3.5-msf coworking inventory, with only 11 locations across the metro. If coworking provider expansion continues as it has across DFW, the metro could possibly overtake Boston and Chicago to become the 4th or 3rd largest coworking market in the U.S.

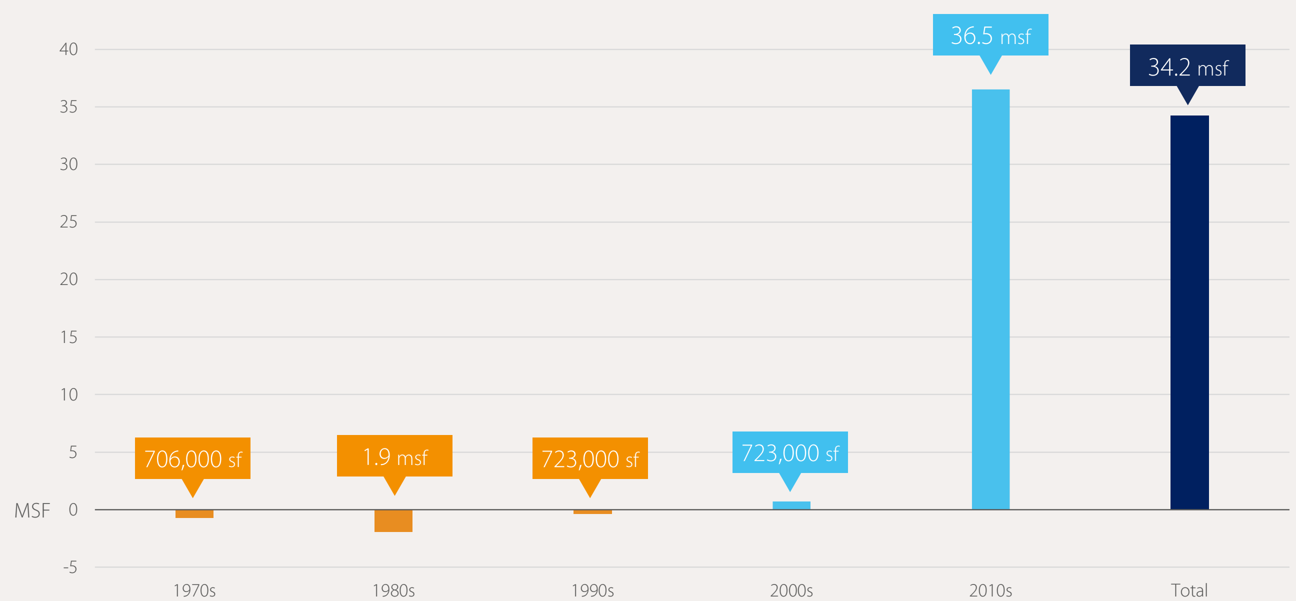
Another trend to watch in 2020 and beyond is the growing demand from office employees to work from home. Companies are increasingly offering personnel the ability to work from home at least once per week, or to have more flexible office hours. Millennials and Gen Z employees are leading the charge in these requests, and with Dallas leading the nation in Millennial relocations, this workforce perk will likely become more common. This trend could sync with workplace strategy decisions for office leases as companies continue to look for ways to reduce their office footprint and overall occupancy expenses. If companies are willing to downsize their office space by moving more workers to rotating hoteling options, the result could be a noticeable decline in absorption as less space gets leased.

Increased demand from tenants for amenities will also impact DFW office, multi-family and retail development moving forward. Recent projects have shown that DFW craves walkable, mixed-use, experiential development with amenities that cater to convenience for the user. As suburbs become more hip through the creation of their own unique "big-city" experience clusters, such as the Legacy district in Plano or the Urban Center in Las Colinas, commercial assets in these areas will be positioned to perform well. If the energy and amenities match the experience one can get in Uptown and Downtown while being located in a more affordable business hub much closer to a user's home, many businesses will happily choose that space to avoid hour-long commutes and other inconveniences.

As for basic amenities, the fight to gain a competitive advantage will likely move to technology, convenience and cost-savings. Things like smart locks, in-building messaging, green tech to reduce energy usage and costs, and storage are the sorts of things that developers will likely need to consider to make their properties stand out.

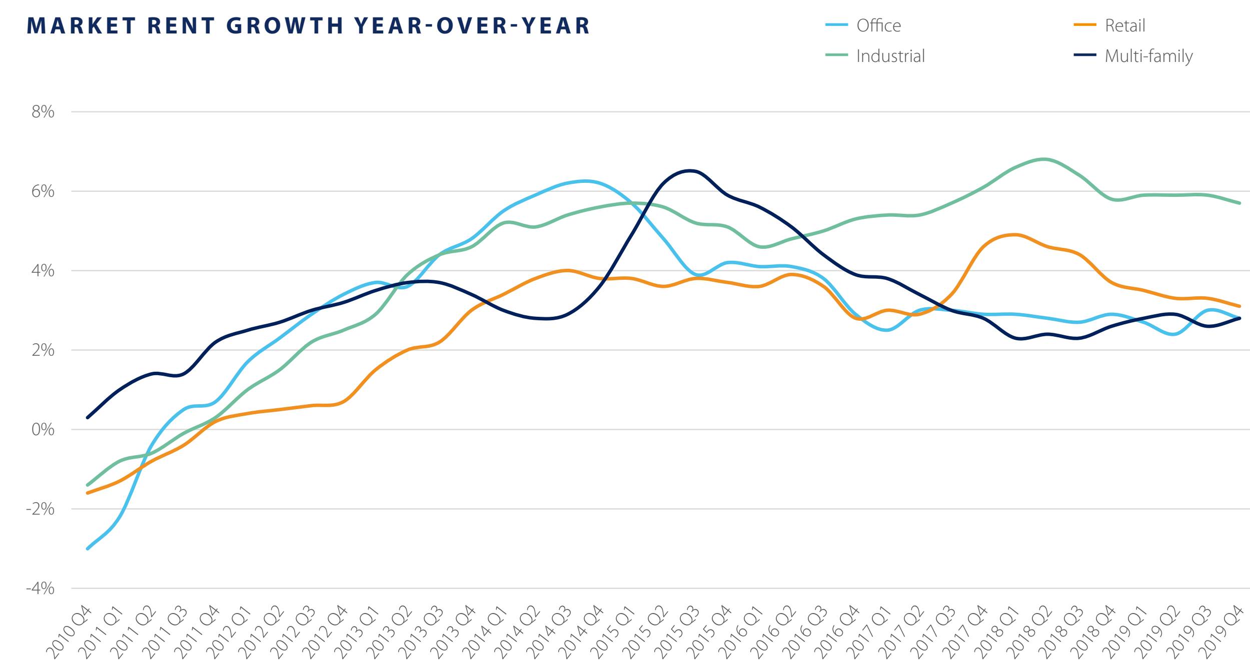
For retail, DFW has the potential to be a strong case study in the reinvention of obsolete assets. Certain major malls across the metro have either undergone or are undergoing drastic renovations. In Plano, Collin Creek Mall is currently being demolished to become a $1 billion mixed-use project. In South Dallas, Red Bird Mall has been revitalized through public-private partnerships and aims to become an economic force for the southern sector like it was in the 1970s. In Dallas, the oft-maligned Valley View Mall has finally been torn down, and plans for the $4 billion mixed-use development called Dallas Midtown are set to see momentum begin in 2020. As these projects take shape and excitement builds, properties around them will likely see a boost in activity and interest, which could shift absorption and construction trends from where they have been in recent years.

ABSORPTION BY THE DECADES



Source: CoStar Realty Information, Inc.

MARKET RENT GROWTH YEAR-OVER-YEAR



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Within the Industrial sector, DFW will continue to see distribution centers be the strongest performers across the market in terms of absorption and construction deliveries. Of the 33 msf of industrial space under construction, roughly two-thirds of that space is contained in distribution centers such as the massive 1.5-msf Home Depot and 1.2-msf Goodyear centers. Nearly all of the remaining industrial buildings currently under construction comprise warehouse space. Key submarket clusters such as Great Southwest/Arlington, North Fort Worth and South Dallas will likely continue to be hotbeds of activity thanks to their prime locations around major thoroughfares and affordable talent pools. DFW's central location, intermodal operations, swaths of open, flat land, and major airport hubs will all continue to push the area to be one of the strongest inland ports in the country.

In conclusion, DFW is positioned to see another strong year in 2020. While the metro's performance will likely cool slightly in tandem with national trends, the area should still see another year of potentially more than 80,000 new residents, and 100,000+ new jobs. These drivers will buoy performance across all asset classes, even as newer product comes online and economic uncertainty continues as a result of the election cycle and volatility in the global financial markets.