Savills Studley Report
Austin office sector

Q3 2017

SUMMARY

Market Highlights

LEASING TAKES OFF

Tenants have leased 2.2 msf in the most recent quarter, well above the long-term quarterly leasing average of 1.7 msf.

DECLINE IN AVAILABILITY RATES

Austin's overall availability rate dropped by 80 basis points from 12.2% to 11.4% in the third quarter. The rate has fallen by 170 basis points from a year ago. Tenants continue to target higher-quality space – the region's Class A availability rate decreased by 110 basis points to 13.5% in the quarter.

RENTS INCH UP

The market's average Class A asking rent increased by 0.5% to $40.84, and has jumped by 12.4% year-on-year. Class B and C asking rent averaged $29.12, up by 14.9% year-on-year.

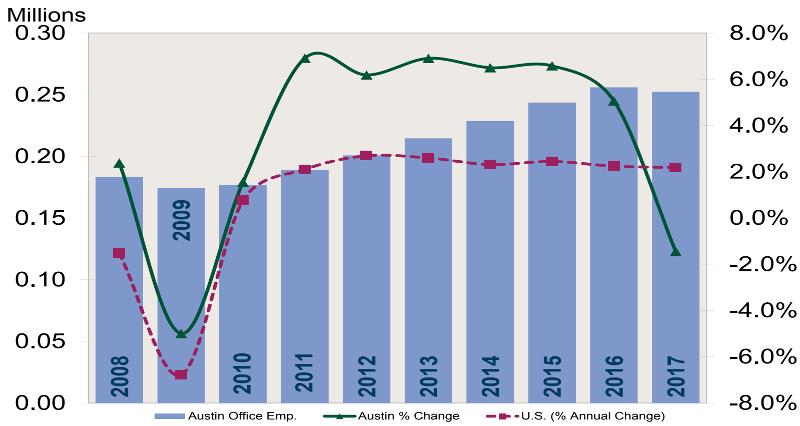
SALES DECLINE

Investors are having a tougher time finding assets to acquire in Austin. Sales volume decreased from $2.5 billion in 2016 to $1.3 billion in the first nine months of 2017.

"In a market nearing the top of the cycle, a few major mega-deals demonstrated that demand has not dwindled for Austin office space."

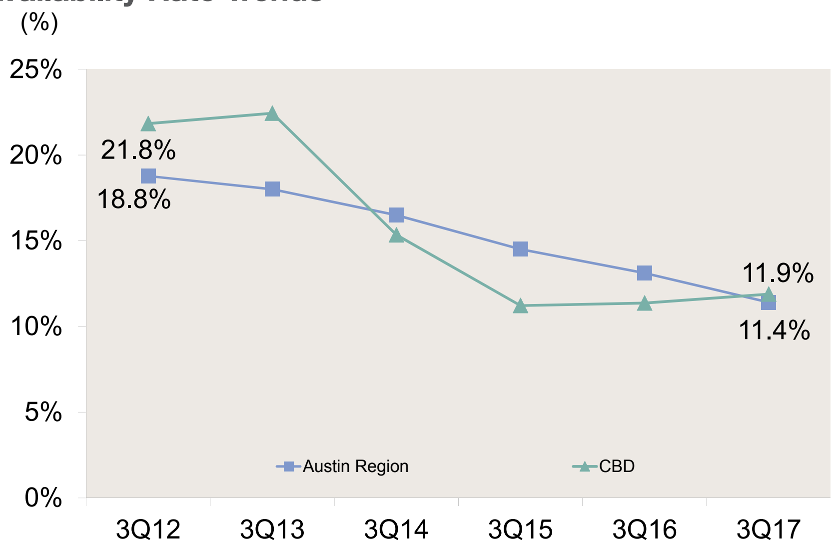
Tim Wingfield,
Savills Studley Research

Office-Using Employment Trends

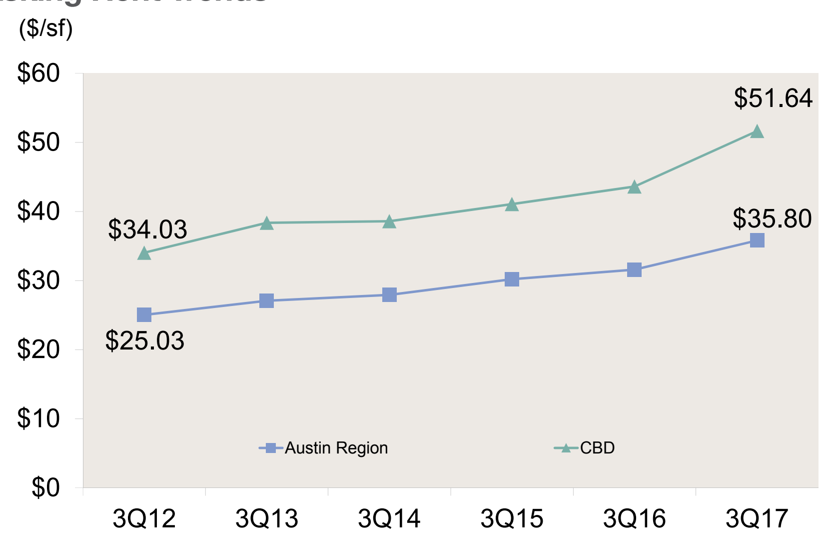


Source: Bureau of Labor Statistics

Availability Rate Trends



Asking Rent Trends



More Growth in an Expensive Market

The Austin office market, and particularly its CBD, still presents tenants with challenging conditions. Availability remains tight, and asking rents remain near all-time highs. Despite that, a fair number of tech companies are actively looking for big blocks of space to accommodate planned payroll expansion. Facebook recently inked ten floors of premium downtown Class A space in Third + Shoal, a 29-story building scheduled to deliver in July 2018. The office development from Austin-based Cielo Property Group, TIER REIT and Invesco will add another 347,072 sf to downtown inventory next year. The terms of Facebook's lease gives the tech giant the option to purchase the building outright at a future date. Facebook has been very proactive with building out new space for its employees in the Central Business District. This past year, the company renovated and expanded its existing space on floors nine through twelve in 300 West Sixth, including the addition of a new 23,000-sf cafeteria, internal stairwell, two outdoor terraces while also signing leases for the 14th and 21st floors.

In another mega-deal, 3M will relocate to Parmer 3.3, a 272,000-sf development in Northeast Austin by Trammell Crow and Los Angeles-based Karlin Real Estate. 3M, known for Scotch Tape and Post-it notes, will find itself in good company with other high-profile multinational corporations along Parmer Lane, such as General Motors' innovation center, Dell and Samsung Semiconductors. 3M will vacate its 156-acre Northwest Austin campus in a sale of an undisclosed price to the contentious Austin-based real estate investment firm World Class Capital Group.

Developers have been a bit more aggressive in recent quarters, reflected in a handful of speculative projects being constructed. Although the level of new construction is relatively controlled, plenty of potential new projects wait on the horizon. San Antonio-based Lynd Development Partners and Dallas-based Lincoln Property Company's unveiling of 600 Guadalupe is significant because Austin, unlike many major metros across the U.S., has not seen much significant growth of major mixed-use developments in its urban core. While the Domain headlines Austin suburban mixed-use development, the proposed 62-story building would deliver 500,000 sf of office, 300 luxury apartments and ground-floor retail space to the CBD. The developers currently plan to kick off construction of 600

Guadalupe beginning September 2018. Landlords with big blocks of available quality space – and there aren't many of them – are in a position to be picky in terms of who they lease space to. Credit worthiness is always an important consideration. This is particularly true for owners planning to sell their asset as soon as they approach or reach full occupancy. These owners are eager to boost face rents and may be willing to offset rent rate hikes with some increased tenant improvement allowances. Of note, elevated construction costs (up 16.7% over the past five years) are diminishing the impact of the higher allowances. Construction costs are likely to spike in the near term thanks in part to the "Harvey affect" as subcontractors shift their attention to the recovery efforts in Houston and Texas' Gulf Coast region.

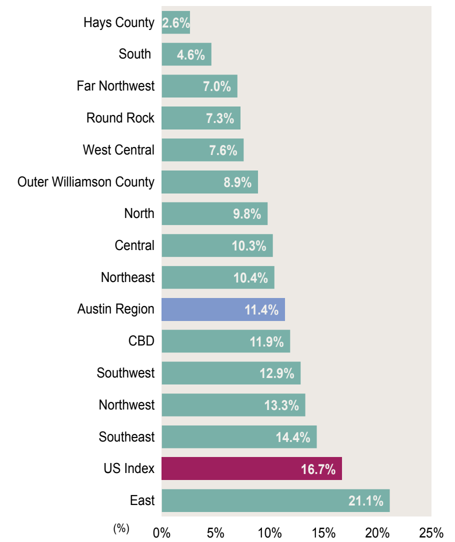
Tenants are still showing a willingness to pay a premium for newly constructed space with average CBD Class A rent approaching $55.00/sf. More cost-conscious tenants could perhaps take a closer look at the Southwest submarket. Just a few miles away from the urban core, the Southwest submarket has significantly slower average asking rent growth despite similar availability. Over the past year, CBD rents grew 18.4% while Southwest rents grew just 3.0%. AMD's campus and the development of Yeti's campus may also demonstrate the attractiveness of the area. However, the area's lack of affordable housing and traffic issues may hinder the appeal of this historically affluent submarket.

Larger tech companies are still engaged in a battle for talent. Firms such as Facebook, Apple, Oracle and Google are increasing their presence in Austin. Most tech firms in Austin have already "right sized" and increased density in the "dedicated work place" portion of their space. Increased densification and smaller workstations are being offset by increased amenities such as ping pong and foosball "de-stressing" areas and nourishment zones (food/bistros/cafes). Firms are also building out creative collaborative space as well as breakout and conference areas. Consequently, the amount of parking and building infrastructure (i.e. elevators, bathrooms and fire code) is imposing an upper limit on the amount of density. Density restriction provisions have become more prevalent in the lease agreement identifying "not to exceed" employees per square foot limitation.

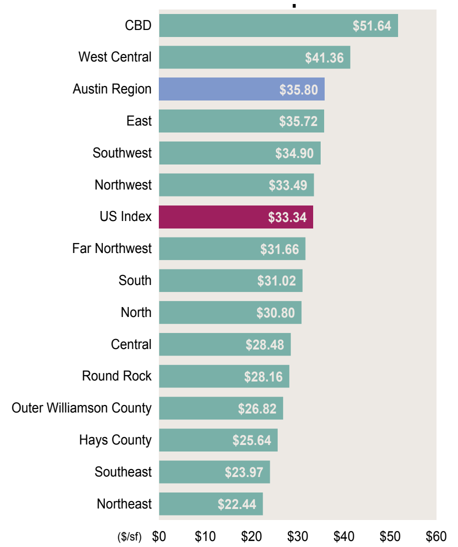
Austin's Robust Absorption

Twelve-month net absorption totaled more than 1.0 msf, thanks in large part to the third quarter's 640,000-sf positive net absorption. The high technology sector signed about 30% of third quarter leases while engineering firms took down about half (15%) of that amount in signed leases. The strong positive net absorption numbers were driven by robust demand from space occupiers. Employment growth presses onward; through mid-year 2017, Austin's unemployment rate fell to a paltry 2.8%, which almost led all the nation's large metropolitan areas. On an annual basis, employment grew at 1.7% while the business-cycle index growth totaled 4.8%, which was 120 basis points below the metro's long-term growth rate of 6.0%, which suggests that Austin is still adjusting to its booming growth experienced over the past five or more years.

Availability Rate Comparison



Rental Rate Comparison



Major Transactions

Tenant	Sq Feet	Address	Market Area
3M	272,000	500 E Parmer Ln	Northeast
Facebook	231,000	601 W 3rd St	CBD
SailPoint Technologies	170,000	11305 Four Points Dr	Far Northwest
LifeSize	72,824	1601 S MoPac Expy	Southwest
City of Austin	60,000	5900 E Ben White Blvd	Southeast
Mood Media	55,025	2100 S Interstate 35 S	South
Opcity	50,000	6800 Burleson Rd	Southeast
Origin Biomedical	42,604	7000 Burleson Rd	Southeast
Parsley Energy	41,469	203 Colorado St	CBD
Kinnser Software	40,000	2500 Bee Caves Rd	Southwest
Sum of Top Leases	**1,034,922**	**Sum of 3rd Quarter Leasing Activity**	**2.2 MSF**

A Record Sale

In September, Lincoln Property Group and Goldman Sachs Group sold its leasehold interest in 5th & Colorado (201 West 5th Street) to Boston-based Intercontinental Real Estate Corporation for $119,000,000. The 5.86% pro forma cap rate proved competitive, but the sales price of $663 per square foot marked a new record high for the Austin market. The office building is anchored by tenants Indeed, Plains Capital Bank, Industrious and USAA. Intercontinental's interest in the property included its high tech tenancy, 94% lease up and perceived below-market in-place rents.

Looking Forward

As suggested earlier, tenants seeking affordable options must, at this point, pursue submarkets other than downtown, The Domain and other attractive live/work/play parts of town. With continued high demand still outpacing supply, there will not be significant rent drops for the foreseeable future.

Map	Submarket	Inventory	Leasing Activity	Available SF			Availability Rate			Asking Rents Per SF		
		SF (1000's)	Last 12 Months	This Quarter	% Change from Last Qtr.	Year Ago	This Quarter	pp Change from Last Qtr.(1)	Year Ago	This Quarter	% Change from Last Qtr.	Year Ago
1	**CBD**	12,196	950	1,450	3.1%	1,383	11.9%	0.4%	11.4%	$51.64	-0.9%	$43.60
	CBD - Class A	7,735	748	1,128	-1.4%	1,021	14.6%	-0.2%	13.2%	$54.33	-0.2%	$45.19
2	**Central**	4,292	149	441	22.5%	412	10.3%	1.9%	9.6%	$28.48	8.9%	$26.21
	Central - Class A	474	15	85	1021.2%	75	18.0%	16.4%	15.7%	$42.36	20.2%	$23.09
3	**East**	2,362	41	499	-2.3%	570	21.1%	-0.5%	29.7%	$35.72	-4.3%	$20.80
	East - Class A	N/A	14	0	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
4	**Far Northwest**	4,862	462	340	-7.5%	530	7.0%	-0.6%	11.0%	$31.66	2.6%	$31.23
	Far Northwest - Class A	2,685	401	278	-2.3%	463	10.3%	-0.2%	17.2%	$33.05	3.0%	$32.25
5	**Hays County**	553	7	14	-3.5%	35	2.6%	-0.1%	6.3%	$25.64	13.0%	$17.41
	Hays County - Class A	N/A	0	0	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
6	**North**	6,029	705	591	-19.3%	1,107	9.8%	-2.3%	18.4%	$30.80	0.2%	$32.15
	North - Class A	2,292	473	145	-21.3%	599	6.3%	-1.7%	26.1%	$37.22	-0.2%	$35.64
7	**Northeast**	2,968	506	310	-2.4%	0	10.4%	-0.3%	13.9%	$22.44	7.8%	$20.00
	Northeast - Class A	735	295	48	59.9%	126	6.5%	2.4%	17.2%	$24.51	-1.7%	$23.69
8	**Northwest**	13,815	981	1,837	-10.1%	1,925	13.3%	-1.5%	13.9%	$33.49	0.6%	$30.38
	Northwest - Class A	7,225	681	1,174	-10.4%	1,083	16.2%	-1.9%	15.0%	$35.68	0.5%	$32.68
9	**Outer Williamson County**	550	19	49	-16.5%	63	8.9%	-1.8%	12.2%	$26.82	1.6%	$22.64
	Outer Williamson Co - Class A	N/A	0	33	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
10	**Round Rock**	1,957	72	143	-16.5%	132	7.3%	-1.4%	6.8%	$28.16	-4.1%	$26.84
	Round Rock - Class A	442	35	7	0.0%	41	1.5%	-5.7%	9.2%	$35.38	0.5%	$30.72
11	**South**	3,222	232	148	-63.0%	282	4.6%	-7.8%	8.7%	$31.02	-8.8%	$26.45
	South - Class A	515	26	28	-84.9%	45	5.4%	-30.3%	8.8%	$35.07	4.8%	$35.52
12	**Southeast**	2,191	192	314	14.8%	249	14.4%	1.9%	12.2%	$23.97	0.1%	$23.39
	Southeast - Class A	N/A	16	30	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
13	**Southwest**	12,401	1,140	1,595	-3.8%	1,738	12.9%	-0.5%	14.0%	$34.90	0.3%	$33.88
	Southwest - Class A	7,615	842	1,112	-2.7%	1,239	14.6%	-0.4%	16.3%	$36.92	0.1%	$35.31
14	**West Central**	1,066	21	81	16.2%	52	7.6%	1.1%	4.9%	$41.36	-4.4%	$37.06
	West Central - Class A	538	11	43	-11.9%	35	8.0%	-1.1%	6.5%	$44.44	-2.2%	$39.61
1-14	**Austin Region**	**68,465**	**5,478**	**7,812**	**-6.8%**	**8,888**	**11.4%**	**-0.8%**	**13.1%**	**$35.80**	**0.6%**	**$31.59**
	Austin Region - Class A	**30,549**	**3,557**	**4,110**	**-7.5%**	**4,791**	**13.5%**	**-1.1%**	**15.8%**	**$40.84**	**0.5%**	**$36.33**

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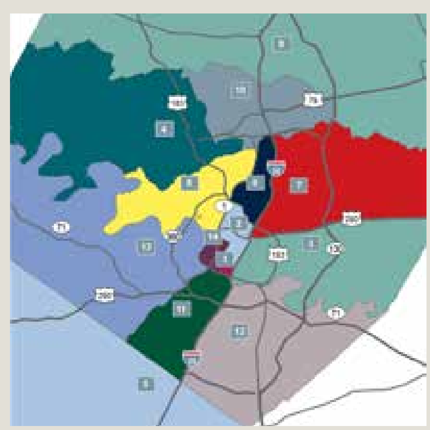

(1) Percentage point change for availability rates.
Unless otherwise noted, all rents quoted throughout this report are average asking gross (full service) rents psf.
Statistics are calculated using both direct and sublease information.
Short-term sublet spaces (terms under two years) were excluded.

The information in this report is obtained from sources deemed reliable, but no representation is made as to the accuracy thereof. Statistics compiled with the support of The CoStar Group.