What's Ahead for 2015

HOUSTON COMMERCIAL REAL ESTATE MARKETS

BOYAR MILLER
ATTORNEYS AT LAW

Introduction: *Chairman's Letter*

In order to deliver counsel beyond expectations, we want to be as knowledgeable in your industry as we are about law.

As part of our commitment to knowing our real estate clients' business, we collect insights from some of the best minds in the industry. This understanding contributes to how we deliver counsel that exceeds our clients' expectations and our ability to help them make strategic decisions about their business.

Looking ahead to 2015, there is a lot of uncertainty, and we want to be certain that you are well equipped to make the best possible decisions for your company. The information in this ebook has been invaluable to us and our clients, and we hope that it will benefit you as well.

Read some of the insights and trends gathered from industry-leading clients and our own real estate team. If you find value in it and would like to hear more, join us for our next BoyarMiller Breakfast Forum, or give me a call.

Best regards,

Chris Hanslik

Chris Hanslik, *Chairman*

TABLE OF CONTENTS

THE EYES OF THE WORLD ARE ON HOUSTON

DON'T FEAR THE LOW OIL PRICE.

$50–$60
PER BARREL

Although dropping oil prices have many companies on alert, real estate developers are confident that Houston's markets can weather the challenges caused by continued low prices. Demand continues to grow in residential, retail and industrial sectors – even if office development slows in the energy corridor as a result of oil prices, developers are confident that growth elsewhere will continue.

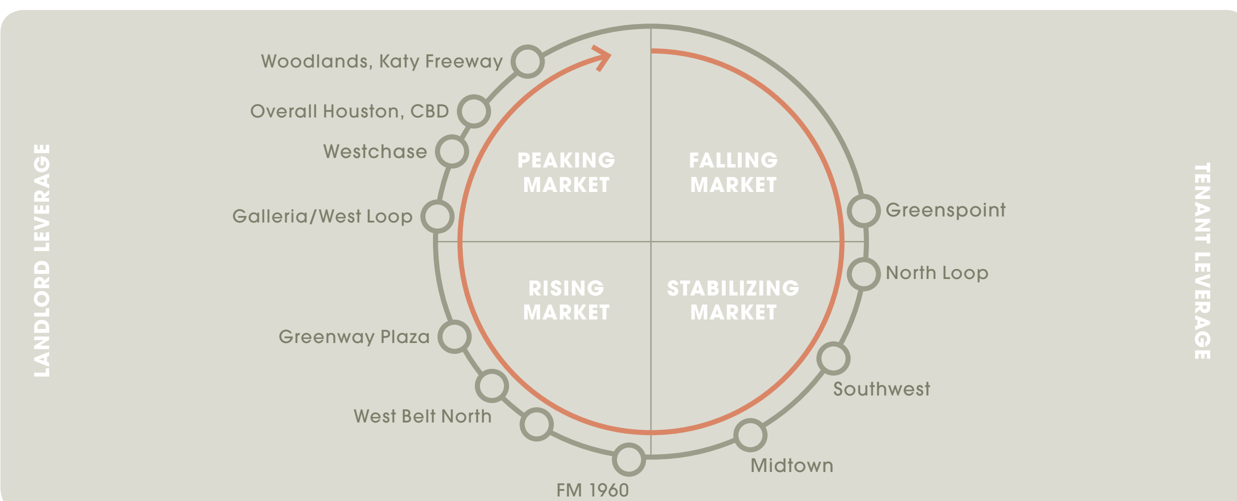
HOUSTON JOB & POPULATION GROWTH CONTINUES.

119,400
JOBS ADDED BY SEPT. 2014

The Houston-Sugar Land-Baytown market saw the second-highest job growth numbers in the nation, behind only New York City. In addition, the city has the largest growth in square footage built of any metropolitan area in the country. This is good news for the real estate industry, which will continue to see demand for homes, shopping centers and offices as the city expands.

HOUSTON'S NORTH AND WEST NEIGHBORHOODS ARE GROWING.

While markets like Greenway Plaza and FM 1960 are rising in Houston, five key areas are at their peak activity and growth level: the Galleria/West Loop, Westchase, Houston CBD, The Woodlands and the Katy Freeway.



EXPERT INSIGHT

Land Development, Homebuilding & Multi-Family Market

"The number one driver of homebuilding and communities is going to be jobs – and from where we sit right now, growth will still continue, but at a slower pace."

2015 PREDICTIONS

Will Holder, *President, Trendmaker Homes*

- **EXISTING HOMES CANNOT KEEP UP WITH DEMAND.** Currently, Houston has the most spec homes under construction than the city has had in more than four years. Last summer saw more than 80,000 closings, with only 20,000 listings for sale – so clearly there is room to build.

80,000
CLOSINGS

- **LOT SHORTAGES PERSIST.** Persistent lot shortages are creating a bit of havoc in the home-building market. Because we have fully deployed the current lots, we have to buy them years in advance. New lot deliveries lag demand significantly, driving up the price of land.

- **CAPACITY CONSTRAINTS ARE DRIVING PRICES HIGHER.** We're testing how the market will support higher home prices, though home prices still fall within the median for now. Raw materials, licensed mechanical contractors, framers, carpenters, factory-fabricated components, professional service providers and equipment heavy contractors are all in high demand and available only at a premium, so expect prices to increase.

HIGHER
HOME PRICES

Practice Leaders, continued

- HOUSING MARKET IS RESILIENT AND FLEXIBLE. While high costs are creating challenges, the demand exists and we can expect Houston's supply-rich environment to self-correct. Plus, all this competition keeps our market creative and fresh!

Will Holder has worked in the homebuilding and residential land development industry for over 30 years in Houston and in several other U.S. metro markets. He started his homebuilding career with David Weekley Homes. Later, he built apartments and townhomes in a dozen cities across the U.S. for 6 years with Lokey Properties. Will returned to Houston to work for 5 years for Village Builders. Ultimately, he joined Trendmaker Homes in 1993 where he has led the company to become the leader in luxury production homebuilding and MPC development. Founded in 1971, Trendmaker Homes is a subsidiary of Weyerhaeuser Real Estate Company operating across Texas under three brands: Trendmaker Homes, Avanti Custom Homes and Texas Casual Cottages. Trendmaker is known for its awarding winning home designs and its commitment to customer satisfaction.

Retail Market

"The homebuilders are performing well, and that's good for the whole real estate industry. That's the barometer we use to measure our success in the real estate business."

2015 PREDICTIONS

Allen H. Crosswell, *Managing Principal, NewQuest Crosswell*

450,000+
NEW RESIDENTS

- **HOUSTON'S RETAIL MARKET IS GOING NORTH AND WEST.** Following Houston's major areas of population growth, Houston's retail market is going north and west. Since 2011, Houston has grown by more than 450,000 people, and the shopping center business will continue to follow the growing population centers in the north and west of Houston.

- **GROCERY IS DRIVING RETAIL DEVELOPMENT.** The primary drivers of retail development in Houston are grocery chains, including Kroger, Walmart, HEB and Whole Foods. For example, Kroger is doing very well, with a great market share in Houston. They achieved their 44th consecutive quarter of 5.6% supermarket sales growth.

- **HIGHER RENT AND HIGH LAND COSTS BALANCE.** We have very limited space for retail and high demand: as a result, rent is up nearly 35% for the first time in a very long time. However, the tremendous rise in land costs are beginning to balance out this increase in returns for retail developers.

- **NEW ACCESS DUE TO GRAND PARKWAY HAS OPENED UP SPECULATION.** The opening of the west Grand Parkway has opened up so much speculation in retail development because of new access. It will continue to increase speculation as more sections of the road become available. Any developer with money, capacity and abilities is looking at the Grand Parkway – that's where it's all happening.

Allen H. Crosswell is Managing Principal of NewQuest Crosswell. NewQuest Crosswell leverages the full-service support and resources of NewQuest Properties with Allen's knowledge, experience and relationships within the industry to develop retail centers throughout Texas. Previously co-founder of TGB Crosswell, as well as founder of its predecessor Crosswell Development, Allen has a significant track record of identifying and executing successful raw land investment and development opportunities. His ability to pinpoint the key issues in a deal and to work through those issues in a way that is agreeable and even beneficial to all parties involved is a recurring theme in the transactions Allen has completed.

Office Market & Mixed-Use Development

"The office market is where we'll feel the low oil price first. There's a lot of sensitivity around that $60 mark."

BELOW $60
SENSITIVITY

2015 PREDICTIONS

Jonathan Brinsden, *President & CEO, Midway*

- **HOUSTON IS A GREAT PLACE TO WORK AND TO LIVE.** Houston has always been a good place to get a job, but with investment in infrastructure and the increase in mixed-use projects that create communities for people, Houston is becoming a better and better place to live, too.
- **TRANSPORTATION WILL BE AN ISSUE WITH CONTINUED DENSIFICATION.** From the energy corridor to downtown, significant densification is coming. Traffic and transportation will be an issue: as continue to build more office, how we get people to that office becomes important. Metro reimagining their bus system to be a more intuitive grid system will help get people where they belong.
- **EXPECT TO SEE VACANCY RATES RISE A BIT IN 2015 AND 2016.** From 2010 to 2013, demand outstripped supply in the office market. 2013 was nearly in perfect equilibrium, and 2014 saw supply start to outweigh demand. Equilibrium is at 12–14% vacancy, and 2014 was at 11%, so expect vacancy rates to rise slightly in the coming years.
- **LOWER OIL PRICE WILL PUT PRESSURE ON THE OFFICE MARKET.** Many expect that oil prices will stay below the $60 mark for long enough to put pressure on the service side and middle market companies of the energy industry, creating a need to renegotiate contracts or consolidate, and potentially impacting the office real estate market.

Jonathan Brinsden serves as Chief Executive Officer of Midway. As one of four members of the Midway Executive Team, he guides the company's overall business strategy and operations. Jonathan joined Midway's development team in 2001 and was named Chief Operating Officer in 2008. Prior to joining Midway, he served as President and COO of Hamm Corporation, a Houston-based development company. Jonathan is an Adjunct Professor in the graduate real estate program at Texas A&M University and the University of Houston. He also serves on the Executive Advisory Board for both programs. He is a member of the Urban Land Institute (ULI) Board of Trustees and the Governance Chair, and immediate past Chair, of ULI Houston. University.

Industrial Market

"Houston is now considered the Best City for Job Growth and one of the Top 10 Cities for Relocation. That sends a great message to out-of-state companies, which is why we're all so busy right now."

2015 PREDICTIONS

Welcome W. Wilson, Jr., *President & CEO, GSL Welcome Group*

- **HOUSTON IS COUNTERBALANCED WHEN IT COMES TO OIL PRICES.** Although the west side of town makes its living on high oil prices – and therefore, we may see a decline in growth there during this dip in oil prices – the east side of town, the refiners, thrive on low prices. Hopefully the east side will boom while oil price is limiting growth on the west side.

- **INDUSTRIAL REAL ESTATE CONTINUES TO GROW.** Houston has 532 million square feet of industrial space and more than 6.3 million square feet under construction. There is a balance of supply and demand in the industrial real estate market. We're in good shape. Huge sales like Cedar Crossing Industrial Park – the largest industrial park on the Gulf Coast – are driving it forward.

532M FT^2
OF INDUSTRIAL SPACE

- **LOST OF OPPORTUNITY FOR HOUSTON: PANAMA CANAL, GRAND PARKWAY, ETC.** The completion of the Panama Canal in 2016 will bring only opportunity for Houston, especially in LNG. In addition, the completion of Section E of the Grand Parkway has brought a lot of new companies to Houston. Overall, Houston is more than just an energy leader – it's a distribution and logistics hub, and its industrial sector looks resilient.

- **HIGH LAND COSTS ARE PUSHING DEMAND FOR EXISTING PROPERTIES.** Land costs for industrial development have doubled as the residential and retail land developers buy it up to accommodate Houston's growing population. That has made our existing properties look really good!

As President & CEO of Welcome Group, Welcome W. Wilson, Jr. oversees the development, leasing, construction and purchase of single tenant office, lab, manufacturing and industrial facilities in Texas. Welcome Group has built over 150 such facilities since 1998 and still owns over 75 containing in excess of 3 ½ million square feet. Welcome has been a real estate developer for more than 35 years with extensive experience in industrial development, residential subdividing, retail centers and office buildings.

HOUSTON HAS FAMILIAR REAL ESTATE OUTLOOK: CAUTIOUS OPTIMISM

Blake Royal & Cassie B. Stinson, *BoyarMiller*

To its residents, the development of Houston has long been a steady train, always churning toward progress despite setbacks and obstacles. Recently, however, the obstacles have been few and the result is a Houston that would be unrecognizable not only to its forefathers, but to any visitor who last set foot here five years ago. The miraculous reemergence of the United States' domestic energy industry has been a boon to all industries in our nation's energy capital, but with the recent drop in oil prices, what is in store for Houston and its surrounding communities? Have we learned our lessons from the past or have the last five years been too good to be true? The outlook is one familiar to all Houstonians regardless of vintage: cautious optimism.

RESIDENTIAL LAND DEVELOPMENT AND HOME BUILDING

The Houston residential market is making up for lost time. The local economy has made a full recovery from the recession of 2008-2010, and homebuilders are working at full capacity to meet the pent-up demand. Builders cannot build homes fast enough for the thousands of new residents taking advantage of Houston's unparalleled job growth. Home inventory is low – 2.5 to 3 months – and while the number of spec homes under construction is at its highest level in four years, the inventory of completed spec homes is at its lowest level during the same period.

What is preventing builders from meeting the demand at a higher pace? The first issue is that land development is still catching up. There have been more home starts than finished lots in every quarter since the fourth quarter of 2008. While this deficit is rapidly diminishing, the greatest factor is time: it takes 18 months on average to fully develop a neighborhood of lots. As more lots are completed, the number of new starts will increase dramatically.

The second issue is capacity constraints. The acceleration of demand has outpaced supply, resulting in higher costs for raw materials and fabricated components and a tighter market for skilled contractors and professional service providers. Finally, the resale market has tightened, which has placed greater demand on new product. Current residents are finding it increasingly harder to justify a move within Houston. Many owners find that the value of their homes has increased beyond what they are willing to spend on a new home, and any move would be a lateral one at best. Other owners recognize the location cannot be replaced and opt to remodel their existing home.

At the very least, the current demand for homes should steady despite the recent uncertainty in the energy industry. In fact, it may give builders some breathing room to create the inventory reflective of a healthy residential market.

RETAIL

The growth in retail developments – particularly grocery-anchored retail developments – follows the growth in residential construction: retail tenants want to be where their customers live. As the economy in Houston has grown, so have new neighborhoods and new retail centers.

In Houston, the growth has largely been in the northern and western regions of the metropolitan area. The majority of new retail developments have followed the growth and anticipated growth of residents and residential developments in these areas. As the new transportation corridors in these areas – namely the northwest portion of the Grand Parkway – are completed, there will be additional projects brought to the market. In addition to the suburban developments, there have also been some recent redeveloped centers in the city proper, as older properties have been reclaimed for new uses. Again, this is driven by the growth in the number of consumers. As the urban population grows, so will retail development.

Houston's growth has also attracted retail brands that are new to the market. This competition for space, coupled with the slow-but-steady growth in new developments, has created a market in which demand has outpaced supply to the extent that retail rental rates have increased slightly after several years of stagnation. From a resale perspective, the market has stabilized after the uncertainty of the recession, with newer properties with creditworthy tenants fetching several bids and healthy cap rates.

OFFICE MARKET AND MIXED USE DEVELOPMENTS

While all market sectors have benefitted from Houston's economic surge, the office sector has seen the fastest growth. But the rapid ascension is balanced by the potential for a rapid decline: the office market is also the sector that will feel the first effects of a fall in the price of oil. Approximately 40% of recent new developments are located in the Energy Corridor, with many buildings being leased in large blocks by the largest energy production and services companies in the region. So far, developers have managed to maintain a healthy balance in the market, with a majority of space being owner-occupied or pre-leased prior to construction. It remains to be seen, however, if recently announced projects will be able to continue this trajectory.

Houston has long had a reputation as a city of opportunity, where hard work is appreciated and jobs are available for those who want them. In recent years, however, it has earned a reputation for not only being a great place to work, but also a great place to live. Increased investment in parks and local infrastructure has increased the appeal of urban living, and Houston has proven that it is not immune to recent national development trends, such as increased density – despite its fame for a lack of zoning laws and regulations – and the rise of mixed-use developments. These developments, which integrate at least three separate revenue-generating uses, appeal to a new generation of office workers who seek lifestyle amenities close to the workplace. Houston has already seen the development of several successful projects, and with more in the midst of construction, the city will continue to be a national leader in this product type.

INDUSTRIAL

The industrial market in Houston has been a constant through turbulent times. Never feeling the full brunt of the recession, it has also recovered at a slower, but always steady, pace.

This is due in large part to the balanced nature of Houston's energy industry. Exploration and production companies may feel the squeeze of the low price of oil, but the downstream refining and processing companies reap the benefits. Luckily, Houston is home to all facets of the industry, and while one may slow, the others pick up the slack. In addition, Houston has become an increasingly important distribution and logistics hub, with access to all major modes of transportation: road, rail, air and sea.

The result is a largely even market, with decreasing vacancy rates and a balance of absorption of new construction. Demand for industrial products will continue to increase as tenants seek more specialized spaces. Furthermore, Houston is poised to capitalize on its established infrastructure, with the Port of Houston growing in anticipation of the completion of the expansion of the Panama Canal, which will open additional opportunities for trade with Asia.

Other than the price of oil, the only factor on the horizon that can slow the steady growth of the various real estate markets in Houston is land prices. Industrial, residential, retail and office developers are all fighting for the same pieces of the pie in an increasingly crowded market. But all in all, this is a good problem to have: it show just how appealing Houston has become as a place to live, work and dream.

HEARD IN THE NEWS

REAL ESTATE IN HOUSTON

Houston's growing energy sector has translated to a construction boom for apartments and homes as well as offices and industrial space. However, as crude oil prices have plummeted…commercial and residential developer are worried about how falling oil prices will affect their building projects in the coming years.

Paul Takahashi, *"Houston developers keep wary eye on falling oil prices," Houston Business Journal*

The memory of Houston's boom-and-bust realty cycles, including the horrific crash of the mid-1980s, remains fixed in the minds of many investors, lenders and developers, Brinsden said in remarks late last week at the BoyarMiller real estate forecast breakfast in Houston.

"Houston's Brinsden: Oil price plunge will pinch office market first," Realty News Report

TGS Cedar Port Partners has purchased the 10,897-acre Cedar Crossing Industrial Park in Baytown, the biggest industrial park in the Houston area and one of the world's largest, and is planning a major expansion of its rail capacity… Evercore Partners, Craig Cavalier Attorneys at Law, and BoyarMiller's Bill Boyar and Cassie Stinson advised TGS in the transaction.

The Houston economy is not going to suddenly skid from 100 miles per hour to 10 MPH. Houston's overall economy – and its realty markets have been showing incredible strength in 2014.

Ralph Bivens, *"Houston gains 125,000 jobs – best job growth since 1981," Realty News Report*

Katherine Feser, *"Huge industrial park has new owner," Houston Chronicle*

REAL ESTATE
PRACTICE LEADERS

We're proud to be among the Top 10 Real Estate Firms in Houston, according to the Houston Business Journal. Meet the practice leaders who deliver counsel beyond expectations to our clients.

Bill Boyar

Founding Shareholder, Business Group

Bill represents the various parties involved in the acquisition, disposition, capitalization and financing of assets and businesses on a national and international level. He has served as lead counsel on numerous complex, multi-party acquisitions and project financings, with significant experience in real estate, hospitality, corporate finance, healthcare, and private equity mergers and acquisitions.

Cassie B. Stinson

Shareholder, Business Group

Cassie's practice is focused on commercial real estate and finance, public/private projects, business transactions and public law, with a particular emphasis on complex projects and multi-party transactions. She has significant experience with office, heavy industrial and manufacturing, multi-family, hospitality and restaurants, institutional facilities and governmental infrastructure.

Stephen Johnson

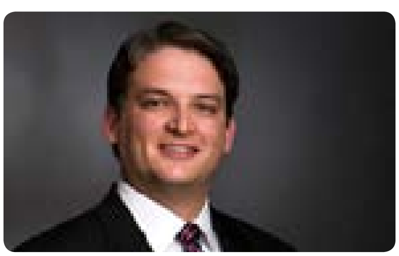
Shareholder, Business Group

Stephen's practice is devoted to commercial real estate law, transactional law, commercial transactions and general corporate representation. His real estate practice includes the financing, acquisition, development and disposition of commercial real estate, with an emphasis on master-planned communities, commercial office and retail, land and hospitality.

Lee A. Collins

Shareholder, Litigation Group

A significant focus of Lee's practice relates to the representation of developers, owners and managers of commercial real estate in state and federal court, including tenant disputes, easement and restrictive covenant enforcement, condemnation, adverse possession, construction litigation, lien enforcement and creditor bankruptcy representation.



Blake Royal

Senior Associate, Business Group

Blake represents developers in all major product types – residential/master-planned communities; commercial/office and retail; and industrial – in capital investment, acquisition, financing and disposition transactions. Deal sizes have ranged from small parcels for low six figures to a multiple tract transaction for nine figures. He has negotiated investment and financing transactions with major institutional investors and lenders (i.e. real estate capital firms, pension funds and life insurance companies) and national, regional and local lenders.

BoyarMiller

4265 San Felipe, Suite 1200
Houston, Texas 77027

TEL 713.850.7766
FAX 713.552.1758

boyarmiller.com