Q2 2025 Houston Market Outlook

Prepared for: Crown & Oak Workspace
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Geography: Greater Houston MSA
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Executive Summary

- **Rents +4% YoY** across the market on average, driven by resilient demand in growth corridors and limited quality supply in select submarkets.
- **Cap rates are compressing in secondary markets**, reflecting renewed risk appetite and strong capital inflows targeting yield relative to primaries.
- **Leasing momentum** concentrated in tenant-favored, upgraded space; landlords that executed capex/amenities captured outsized absorption.
- **Debt markets** remained selective but stable; spreads tightened modestly for stabilized, cash-flowing assets, with more creativity required for transitional business plans.
- **Outlook (H2 2025):** Expect continued bifurcation by asset quality and micro-location; pricing discovery is ongoing but trending firmer where NOI growth visibility is highest.

Key call-outs for Crown & Oak: prioritize high-growth nodes with improving household formation and logistics connectivity; underwrite to today's debt costs with conservative exit caps, but recognize targeted compression where rent growth is durable.

Table of Contents

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1) Market Backdrop & Macro Context

Houston's growth profile continues to benefit from: - **Population & employment in-migration:** diversified beyond energy into healthcare, life sciences, logistics, and tech-enabled services. - **Affordability vs. coastal**

peers: sustaining household formation even amid higher rates. - **Logistics advantage:** port, interstate, and air cargo connectivity supports industrial take-up.

Theme: 2025 demand has been quality-biased: assets with modern specs, ESG-forward upgrades, and amenity packages outperform vintage stock.

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2) Capital Markets Overview

Pricing & Cap Rates

- **Secondary market compression:** Investor competition increased for well-located assets in suburban nodes and emerging corridors, leading to **cap rate compression** versus late-2024 levels (user-provided directional input).
- **Bid-ask:** Narrowing for stabilized product; still wider for transitional/repositioning deals pending lease-up proof.

Debt & Structures

- Stabilized assets: conventional bank and life-co appetite improved; modestly tighter spreads; preference for lower leverage and robust DSCR.
- Transitional assets: more **structured solutions** (A/B notes, earn-outs, partial recourse, mezz/preferred).
- Interest-rate hedging remains standard for floating exposure; sponsors increasingly extend caps to cover the full business plan.

Takeaway: Where NOI growth is credible, pricing is firming; exit underwriting should reflect **measured** cap compression only where supported by submarket rent growth and liquidity depth.

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3) Operating Fundamentals

Rents

- **Market headline: Rents are up ~4% YoY** (user-provided).
- Growth strongest in supply-constrained microlocations and in assets with recent capex/amenity upgrades.
- Concessions persist in older/vintage stock, particularly where competitive new deliveries cluster.

Vacancy & Absorption (Qualitative)

- Vacancy mixed by asset quality: newer product closer to full; older product elevated without upgrades.
- Absorption skewed to upgraded and well-located properties; flight-to-quality remains a dominant theme.

Operating Expenses & NOI

- Insurance and taxes remain the biggest wildcards; energy efficiency retrofits and proactive tax appeals continue to protect margins.

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4) Supply Pipeline & Deliveries (Directional)

- **Pipeline moderation:** Starts down vs. peak years; deliveries scheduled through late-2025 are increasingly pre-leased in top nodes.
- **Spec development:** More selective, focused on best-in-class product and infill parcels.
- **Renovation wave:** Value-add and adaptive reuse targeting repositioning to higher spec.

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5) Submarket Spotlights (Qualitative Themes)

Downtown & Midtown

- Repositionings and amenity upgrades drawing tenants seeking modernized space with transit access.
- Hospitality and lifestyle activations support evening/weekend foot traffic.

Galleria / Uptown

- Retail-amenitized, mixed-use environment supports premium rents for modern product; older stock competes via incentives and spec suites.

Energy Corridor & Westchase

- Corporate consolidations into higher-efficiency footprints; proximity to executive housing remains a draw.
- Buildings with high parking ratios and wellness-forward amenities outperform.

The Woodlands & North Houston

- Family-oriented amenities and master-planned environments maintain strong absorption; logistics nodes benefit from beltway connectivity.

Sugar Land / Southwest

- Demographic growth and improving retail mix underpin rent resilience; selective new supply.

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6) Asset Class Deep-Dive

> **Note:** The following narratives are directional and align with the overall **+4% YoY rent** trend provided. Replace placeholders with internal KPIs as needed.

Multifamily

- Steady leasing velocity with **amenity-rich, newer assets** capturing the most demand.
- Concessions focused on lease-up assets or submarkets with recent deliveries; renewal spreads positive in stabilized, well-managed properties.
- **Capex ROI:** in-unit upgrades (appliances, flooring), package/parcel management, and energy efficiency deliver tangible rent premiums.

Industrial

- Demand led by e-commerce, 3PLs, construction suppliers, and energy-adjacent manufacturing.
- **Spec vs. BTS:** Spec remains measured; BTS for specialized users continues.
- Rents holding firm; **yard and trailer parking** and proximity to major arterials command pricing power.

Retail

- Neighborhood/service-oriented centers outperform; grocer-anchored centers strongest.
- **Small-bay** availability tight in growth corridors; rent growth supported by local services and medical/fitness users.

Office

- **Flight-to-quality:** Tenants trade up to efficient, amenitized Class A; Class B/C requires creative leasing and capital plans.
- Sublease supply stable to declining in select micromarkets; ESG features and wellness certifications support absorption in newer product.

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7) Investment Strategy Implications (Crown & Oak)

1. **Target high-growth suburban nodes** with improving schools, retail, and last-mile access; lean into assets where **light-to-moderate capex** can unlock rent premiums.
2. **Underwrite rent growth at ~4% YoY** baseline where supported, with scenario analysis ±200 bps by submarket and asset condition.
3. **Exit cap guidance:** reflect selective compression in secondary markets **only** where liquidity is deep; maintain conservative caps elsewhere.
4. **Capital stack:** favor fixed-rate or hedged floating structures; evaluate mezz/pref to right-size leverage within DSCR guardrails.
5. **Asset management:** prioritize energy efficiency, amenity enhancements, and tax/insurance risk management to protect NOI.

Illustrative Underwriting Guardrails
- Leverage: 50–60% stabilized; 60–65% transitional with de-risking milestones.
- DSCR: ≥1.35x stabilized (underwritten at stressed rate).
- Reserves: insurance/taxes and capex fully funded at close.
- Exit cap: purchase cap +25–75 bps unless submarket/asset quality supports tighter outcome.

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8) Risks & Watchlist

- **Insurance & tax volatility** affecting operating expenses and valuations.
- **Interest-rate path** and credit availability for transitional assets.
- **Supply pockets** creating localized concessions until absorption normalizes.
- **Construction costs** and timelines for repositioning/adaptive reuse.
- **Regulatory & permitting** timelines impacting project delivery.

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9) Methodology, Definitions & Notes

- This report synthesizes market-level trends using Crown & Oak's vantage point and user-provided directives: **cap rate compression in secondary markets** and **~4% YoY rent growth**.
- Replace directional placeholders with internal datasets: leasing pipeline, traffic/lead analytics, renewal spreads, comp sales, and lender term sheets.
- **Definitions:**
- *Cap rate compression:* decline in going-in yield implied by market pricing.
- *Secondary market:* submarkets outside the core CBD/prime districts.
- *Flight-to-quality:* tenant preference for newer, amenitized, efficient assets.

Appendix A — Illustrative Tables (Replace with Actuals)

A1. Sample Rent & Vacancy Snapshot (Illustrative)

Submarket	Avg Asking Rent (YoY)	Vacancy (Dir.)	Notes
Downtown/ Midtown	+3.5%	↘	Amenity-led leasing in renovated assets
Galleria/Uptown	+4.2%	→	Mixed-use amenity base supports pricing
Energy Corridor	+3.8%	↘	Corporate consolidations; spec suites help
The Woodlands	+4.6%	↘	Master-planned advantages, family amenities
Sugar Land/SW	+4.1%	→	Selective new supply; services-led demand

Arrows: ↘ improving (declining vacancy), → stable, ↗ rising

A2. Capital Markets — Illustrative Cap Rate Ranges

Asset Class	Core	Core-Plus	Value-Add
Multifamily	4.75–5.25%	5.25–5.75%	5.75–6.50%
Industrial	4.50–5.00%	5.00–5.50%	5.50–6.25%
Retail (Grocery-anchored)	5.25–5.75%	5.75–6.25%	6.25–7.00%
Office (Class A)	6.25–7.00%	7.00–7.75%	7.75%+

Illustrative only. Insert observed ranges from current comps and term sheets.

A3. Illustrative Debt Terms

Product	Stabilized	Transitional
Senior loan	5–7 year, partial IO, fixed/hedged	3–4 year, floating w/ cap, extension options
Proceeds	50–60% LTV	55–65% LTC with earn-outs
Covenants	DSCR ≥1.35x	Milestone-based funding, DSCR cash sweeps

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Appendix B — Analyst Checklist (For Deal Screens)

• Submarket rent & vacancy trend vs. MSA
• Competitive set (age, specs, parking, amenities)
• Capex plan and ROI metrics
• Insurance quotes and historic loss runs
• Tax assessment appeal strategy
• Debt quotes (2–3 sources) and hedging plan
• Exit liquidity depth and recent comp activity

Disclaimer

This document is a market narrative built around user-provided direction for **Q2 2025 Houston**. Figures flagged as *illustrative* are placeholders; replace with verified internal and third-party data prior to investment decisions.