DOWNTOWN DALLAS

State of the Market

Downtown Dallas
& COVID-19

To our Downtown Stakeholders,

The livelihood and success of Downtown Dallas, as well as downtowns across the country, is critical for the economic health of our city and country. The top priority for Downtown Dallas, Inc. (DDI) is the health and well-being of Downtown's employees, residents, and visitors in light of the national outbreak of COVID-19, as well as doing our part to help stop the spread of the virus and end the pandemic. Since the beginning of the outbreak, we have been working closely with our local partners and following recommendations from the Centers for Disease Control and Prevention (CDC), Dallas County Health, and the City of Dallas.

Furthermore, supporting business continuity and positioning Downtown Dallas to be an international model for recovery is top of mind. **We MUST protect the last 25 years of investment in the heart of our city, support business continuity in this "new normal," and position Downtown Dallas as an international model for recovery.**

As the economy advances phased reopening efforts, DDI continues to work diligently to support the Downtown marketplace with tools and information to support rapid recovery. In that spirit, our Economic Development and Research teams have put together this updated State of the Market resource with valuable insights on the Downtown market pre-COVID, with additional information on current market impact, challenges, and signs of strength.

Kourtny Garrett
President & CEO
Downtown Dallas, Inc.

Downtown's unprecedented growth has led to robust market sectors spanning multifamily, commercial office, hospitality, retail, and restaurants.

Taken individually, the analysis of each sector builds an overall market snapshot to inform both the current state of the Downtown market, as well as opportunities to enhance and sustain Downtown's terrific success.

Currently, in Downtown Dallas, over 12,000 people are residing in 50 residential properties that include apartment towers, condominiums, and townhome developments. Additionally, we are watching the performance of 139 commercial office buildings and 26 hotels in Downtown, while monitoring the status of retail, restaurants, and over 100 active construction and development projects within the immediate area.

The analysis and insights within this State of the Market Report will break down each of these crucial market sectors to provide up-to-the-minute data to aid in continued realization of the great vision that is Downtown.

As of the publication date, the State of Texas is implementing a staged reopening. We will continue to monitor and update on how this phased approach is impacting our Downtown businesses.

12k+
Residents

50
Residential Properties

139
Commercial Office Buildings

26
Hotels

100+
Active Construction & Development Projects

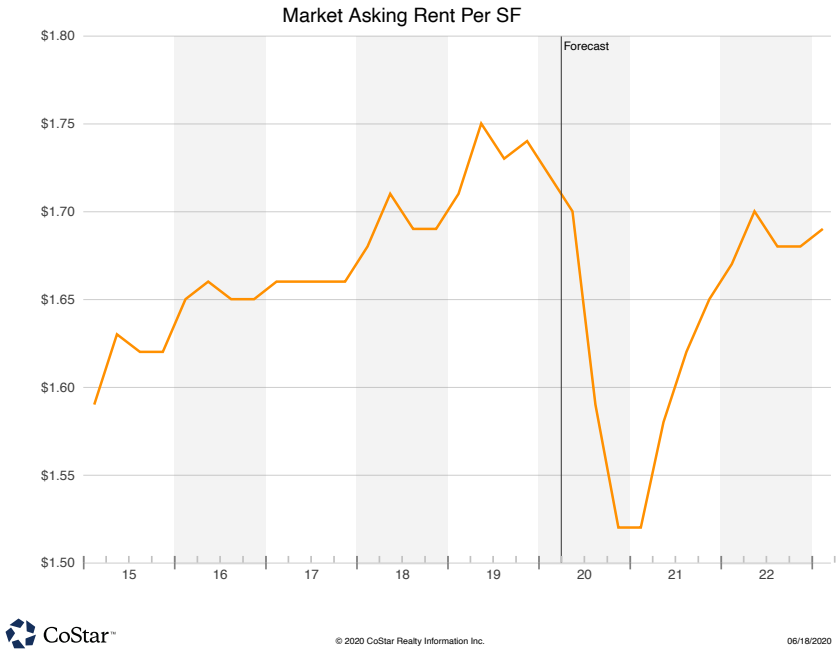
MULTIFAMILY

Over the past 20 years, Downtown has seen incredible growth in multifamily development, growing from just 200 residents to over 12,000.

Available products include a variety of rental, condominium, and attached single family products. Downtown has been fortunate to lie within the center of a top-performing multifamily market, consistently setting the bar for multifamily starts nationally.

As of today, the DFW market has over 20,000 units of multifamily on the cusp of being delivered and approximately 1,800 of those units are under construction within Downtown, specifically defined as the geography located within the surrounding freeway loop.

Historically, new multi-family deliveries in the City Center* have enjoyed a steady rise in market asking rent per square foot, from $2.85 in 2015, and closing at $3.15 for units delivered in 2019. Rents in the area had begun to flatten as almost 3,000 units were delivered in 2019.



Courtesy of CoStar, Downtown Core Geography

The local economy in Dallas, and in particular Downtown, has shown an unusual resilience to larger economic shocks, such as the 2008 financial crisis. While there was a notable slowing in rent growth and new starts, Downtown performed significantly stronger than its national competitors, partly due to the sheer diversity of employment sectors that make up our corporate environment. Downtown has continued to see steady rent collections and slowed but continued leasing activity. As more employers continue to expand re-openings, Downtown leasing activity is also expected to continue to increase.

The Drakestone

Defined as The 360 Plan geography, or approximately 2.5 miles from the center of Downtown.

As we continue to monitor the current economic impacts associated with COVID-19, we look to our national CRE research institutions for insight and modeling.

Current conservative modeling from CoStar is forecasting a potential $.09 cent per square foot drop in asking rent, though to date we have only seen a flattening, rather than a decrease to overall rent growth. By the end of the second quarter, as new units come online, a rise toward recovery continues to be expected by the end of 2020.

The largest multifamily sector impact to date has been seen in reported investment transactions. Reporting shows an approximate 80% decrease when compared to the same period in 2019. While this may be a cause for caution, this ultimately presents an opportunity for parked capital to flood the market as certainty continues to improve.

As a particular bright spot, construction within Downtown continues to proceed. The construction throughout the City Center* consists of primarily market rate and above, consisting of class A and units with asking rents for one- bedroom units averaging over $2,000. Within Downtown, projects already under construction are maintaining their projected openings this year, including 300 Pearl, AMLI Fountain Place, The National, and Atelier Flora Lofts.

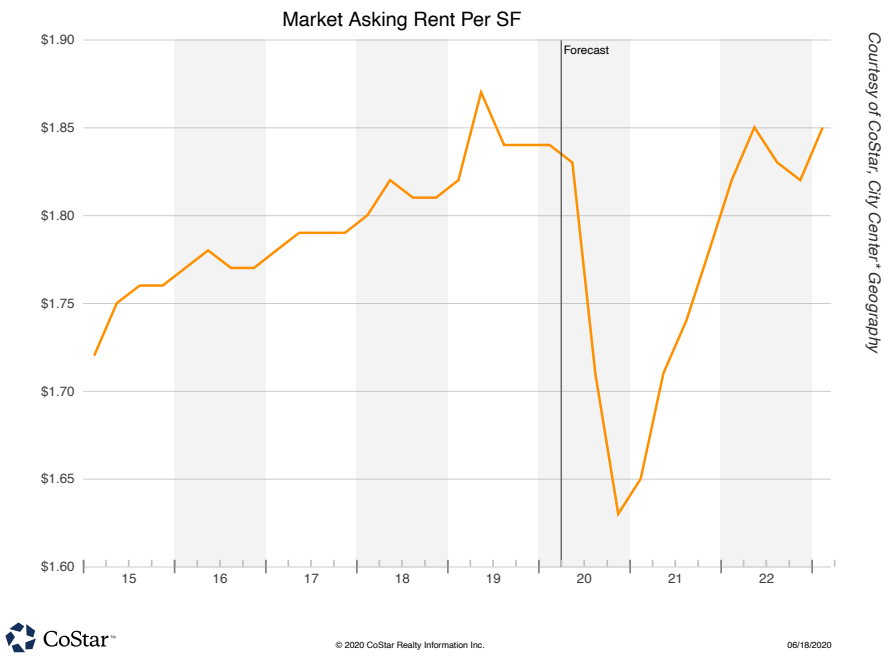
Downtown has also benefited from surgically implemented workforce housing development such as The Galbraith at 2400 Bryan, delivering 217 units across a range of income levels helping to support a diverse market with a variety of housing options across multiple income levels.

Atelier Flora

AMLI Fountain Place

*Defined as The 360 Plan geography, or approximately 2.5 miles from the center of Downtown.

With our finger on the pulse of the specific Downtown Dallas market, we see Downtown's multifamily stock performing with considerable success. According to CoStar, the City Center's* existing residential properties are still performing solidly at 91.4% occupancy with over 57,000 units being tracked.



Courtesy of CoStar, City Center Geography*

As multiple projects continue to deliver throughout the City Center* geography, we expect to see market rents respond within an approximately $.03 range reacting to the sheer number of new deliveries. CoStar continues to project declining rent growth in Q3 of this year followed by a slight increase into Q1 of 2021 then exponential increases to full recovery by 2022.

Due to the projected delivery of significant class A units, the average asking rent for Downtown Core apartments show a continued steady increase in per/ft asking rents over the next two years. Significant projects contributing to this gain are AMLI Fountain Place with 350 units, Atelier in the Arts District with 419 units, 300 Pearl in the Dallas Farmers Market with 336 units, and The National at 1401 Elm with 324 units.

According to surveyed property managers and landlords, Downtown properties have enjoyed a strong year with little residential turnover, which continues to support a strong market health. Owner and manager feedback indicates a strong trend to date of stable occupancy, and a lesser need for rent concessions to attract tenants. With new buildings coming on-line this year at AMLI and The National, followed by Atelier, and more multifamily construction starts in the East Quarter, Farmers Market, and nearby West Dallas, we anticipate a standard supply related adjustment to rent growth in our current properties for the near term, beginning to rise as properties stabilize and demand for urban product continues to grow.

**Defined as The 360 Plan geography, or approximately 2.5 miles from the center of Downtown.*

Though the economic impacts of COVID-19 have proven to be a source of uncertainty for both multifamily owners and tenants, the sector as a whole has already begun to see steady performance due to generally stable rent collections and tenant retention programs throughout this crisis.

Sheraton Parking Garage

COMMERCIAL OFFICE

The Downtown Core is the largest concentration of office space in North Texas; with over 33.6 million square feet of space and another quarter of a million square feet under construction in a relatively compact 1.1 square mile geography.

Recent reporting periods have shown incredible commercial office performance in Downtown, exhibiting the advantage of the sheer available RSF within the overall geography in comparison to the limited space in surrounding markets. 2018 and 2019 led the entire North Texas region with over 650K square feet of positive net absorption.

Taken in context, Downtown is the historic commercial center of the region. Due to this factor, Downtown also has by far the largest density of commercial office availability anywhere in the region.

View from Pacific Plaza

As surrounding submarkets have matured over the last 30 years, Downtown has historically seen past periods of increased vacancy in step with overall national trends, particularly in the late 80s and early 90s.

This fact continues to be both a source of challenge and opportunity seen throughout similar national markets. Among our historic commercial office stock lies a significant amount of existing available space.

Within this current vacancy, though, lies a unique opportunity distinct from surrounding markets. Among those advantages is great opportunity for contiguous square footage in buildings that have recently gone through transformational redos, like Fountain Place.

As was projected, deals already in the pipeline have continued to move forward. A significant indicator of the overall health of the Downtown market is among CoStar's "3 star" properties – **Downtown continues to outperform surrounding markets by 9.4%.**

Overall impacts of COVID-19 on the commercial office sector have been seen nationally, but we have continued to see activity within themarketplace. Many deals that were already in the pipeline have continued to close. CoStar has reported approximately 67 leases signed in Downtown since January 2020, which is while slightly lower than the prior year, remains only moderately slowed We've seen more expansions in 2020 than in prior years and more varying terms on new leases. As the market begins to settle into a wait and see, we have seen modest slowing, anticipating a readjustment to normal as conditions become clearer.

Given the Downtown commercial market's continual persistence, Downtown remains a key relocation focus for national tenants in highly impacted markets.

In Q1 and Q2 of 2019, CoStar reported a total of 102 office deals totaling just over 700,000 square feet with a gross average asking rent of $28.74 p/ft and an average square footage of 7,307. This included large leases of Kane Russell Coleman of 44K square feet at Bank of America Plaza, Scheefer & Stone of 25K at Ross Tower, and both TripAction and ReelFX for 25K at 717 Harwood.

In the same period this year, we have seen 67 deals reported totaling 401,059 square feet with a gross average asking rent of $30.14 p/sf and an average square footage of 6,046. This included large deals of Sheppard Mullin Richter & Hampton for 52K at Chase Tower, Vision2 Systems for 25K at Factory Six03, and a 10K expansion from Orix as well as another 10K taken by Goldman Sachs, both at Trammell Crow Center.

Overall, the greatest impact to commercial leasing garnered by existing economic conditions is on short-term leases which have less of an ability to adapt their overall lease structures to absorb current hardships.

Long-term leases, though, continue to prove to be resilient as they have the ability to provide short-term flexibility that can be reabsorbed over the term of the lease.

Office rents in Downtown still exhibit significant values among competing submarkets, while also being located in the highest density of employers, residential options, and industries in the region, averaging $26.85 p/ft compared to the DFW market average of $27.38.

Skyline at Night

HOSPITALITY

Downtown has enjoyed strong hotel growth over the past five years, fueled by a strong economy, a high-performing convention center, and significant growth of business travel and tourism.

Due to these strong market factors, Downtown hosts some of the highest hotel room densities in the region with just under 9,000 rooms in 24 hotels currently within the Downtown Core. Furthermore, there are 445 additional hotel rooms under construction with a comparable amount planned or proposed in planned or announced developments.

The hospitality sector is linked strongly to the restaurant and retail sector performance within Downtown and has undoubtedly been one of the most significantly impacted industries in the COVID-19 crisis. While operators have seen significant impacts as very short-term, longer impacts to the industry at large will be influenced by the speed of the overall market rebound fueled by a rapid stabilization in public health.

The Statler

Shelter-in-place orders led to temporary hotel closures nationwide. While many properties have now begun to reopen to business, approximately 50% of Downtown hotels temporarily ceased operations. While many have resumed operation, occupancy levels still continue to hover at roughly 20%. While this is a daunting figure, original impacts saw occupancy as low as 5-7% average in February and March. The currently observed increase in Downtown occupancy rates is projected to continue a steady increase as a return to limited leisure and business travel becomes more common.

All factors taken together the combination of partial travel bans, canceled conventions, and self-quarantine has significantly impacted the industry globally. Swift action to preserve public health and shorten shelter in place orders will greatly accelerate the recovery throughout the industry.

According to VisitDallas, the high degree of hotel demand losses may result in an estimated 20-25% of hotels temporarily closing this year. As the tourism industry begins a recovery in 2021, we are expecting hotels to slowly reopen and recover to pre-crisis levels during 2022. While it is expected that occupancy rates will rebound to near pre-crisis levels within the next two years, hotel revenue recovery is expected to lag until 2024, due to a slow recapture of average room rates. This will likely mirror the same trend experienced after both 9/11 and the 2008 financial crisis, with both average room rates and hotel revenues taking between 4-5 years to recover to pre-crisis levels.

Among regional markets, Downtown hospitality properties have been able to leverage unique opportunities afforded by an urban location. Due to the proximity to both public institutions and services, a number of properties have partnered with the public sector to provide temporary housing for both first responders and vulnerable populations. These strategies ultimately allowed for continued operation, needed cash infusions, and the ability to keep staff working. Fortunately, these conditions continue to improve as more hotels reopen for business.

Overall, announced projects continue to move forward, while existing properties are utilizing methods to maintain solvency as the public sector considers additional methods and programs to aid in a strong rebound.

All of these indications are encouraging signals that, given the right tools, the hospitality market sees a strong opportunity for recovery as the market stabilizes.

RETAIL

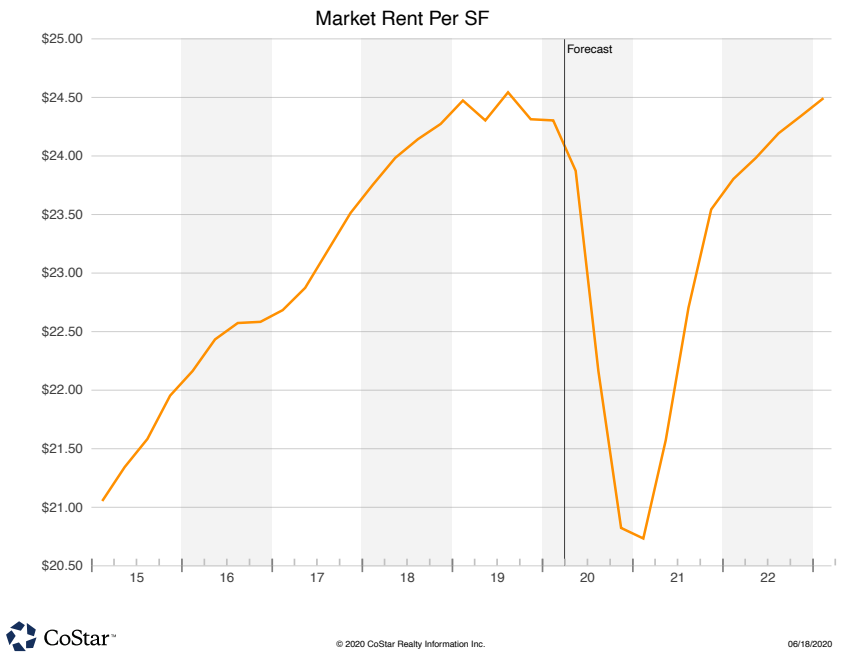
Alongside the strong rise in Downtown residential production, retail uses have seen solid growth throughout the geography. The City Center* at large boasts over 200 places to shop.

This growth continues to increase within Downtown with the sheer amount of recently opened, under construction, and announced projects; with the majority including a mix of restaurant and retail uses. As reported from conversations with each of our major development entities within Downtown, each of these projects, representing nearly $4B in total investment, remain on track and set to deliver. The current impacts of COVID-19 have varied between retail and restaurant, both implementing measures to retain staff, sustain cash flow, and position themselves for recovery.

Pink Toes Nail Bar – Opening Soon

**Defined as The 360 Plan geography, or approximately 2.5 miles from the center of Downtown.*

Regionally, there continues to be movement in the retail sector. According to CoStar, over the past 12 months DFW experienced 1.2 million square feet of net positive absorption in the retail sector while delivering 3.4 million square feet with another 4 million in the pipeline. The bulk of deliveries has been in mixed-use developments in urbanized areas. Following these recent deliveries, most retail leases signed in the metroplex have been less than 5,000 square feet; smaller tenants account for nearly half of the RBA leased last year. Pre-leasing has been strong, especially in the mixed-use segment, with over 75% of retail space under contract prior to delivery. Large grocers are still looking to enter submarkets with strong demographics.



Courtesy of CoStar, Downtown Core Geography

Retail has seen significant impacts to operations, though have shown some advantages given programs and strategies already underway to adapt to natural evolution in the marketplace.

Prior to the COVID crisis, brick and mortar retailers were already beginning to reimagine their concepts to compete with e-commerce and adapt to changing consumer demands and expectations. This diversification has both proved to be advantageous and applicable to the current restrictions and mandates imposed on in-person retail activity. The COVID crisis has intensified the need to rethink everyday business, and to-date, there is not a strong projection of what the future holds. In Downtown, our retail anchors such as Forty Five Ten and Neiman Marcus have been forced to furlough in-store sales representatives, but are working to adapt to the market by moving to online sales and virtual personal shopping. This is a trend that we see intensifying, and as continued programs to support the retail economy are implemented by the public sector such as online ordering and curbside pick up, we will continue to see retailers leverage preexisting platforms to maintain operations under current conditions.

Within Downtown specifically, retail rental rates have steadily risen to and stand at a current average of $24.06. Vacancy within new construction has remained low, with the majority of new projects incorporating various forms of retail and grocery such as the Dallas Farmers Market and Royal Blue in Trammell Crow Center.

We have also seen the continued filling of existing space with examples such as Royal Blue Grocery at The Mercantile. With new projects coming online, we expect to see continued supply throughout the Downtown market.

While Downtown has proven strong performance in food and beverage in particular, the overall impacts of COVID-19 have been undeniable, resulting in limited operations and both temporary and permanent closures. While we have witnessed significant impacts to retail and restaurant activity in the short-term, comparable to the larger regional market projections, demand for services driven by residential and employment density point to a stronger recovery than many competing markets.

Commerce at Adolphus Hotel

Royal Blue Grocery

RESTAURANT

The City Center* at large has nearly 500 restaurants and bars which have shown great resilience adapting to challenging conditions.

With the uninterrupted allowance of delivery and pick-up options, phased reopening to 75% allowable occupancy, as well as the state relaxing select laws regarding the sale of carry out alcohol, many restaurants have adapted to modified business models and remained in operation. Additionally, initiatives such as the temporary pop-up patio program, serve as new tools to adapt to changing customer habits and regulations. Essential businesses such as Royal Blue Grocery and the Farmers Market have been meeting the grocery needs of our residents during this time.

Along with the adaptations in operations, public programs provided through the CARES Act, such as the Paycheck Protection Program, have allowed many impacted food establishments to continue to retain staff and modify their operations rather than temporarily limit operation. That said, the overall impacts to restaurants in particular, given total restrictions to in-establishment dining, continue to be significant. The long-term ability to for Downtown businesses to recover will continue to improve as we see continued increases in public health and confidence.

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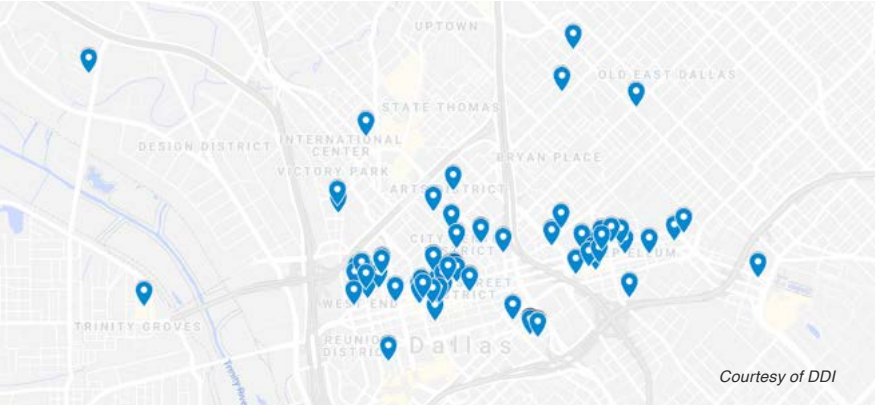
The strain on tenants places significant strain on landlords and property owners as well. Landlords and property managers are handling each tenant on a case-by-case basis reporting rent forgiveness, abatements, and deferments for the time being. Many retailers have received loans under the CARES Act and are hoping that the continued increases in occupancy and normalized will help move toward recovery.



Courtesy of DDI

Downtown Restaurants Offering Delivery/Takeout

Continued support programs to drive customers to Downtown establishments will continue to be essential to enhance short-term performance and long- term success of Downtown's restaurant and retail establishments.

Downtown Dallas, Inc. continues to maintain an updated list of open businesses and modified hours as a resource for customers to goods and services. DDI also continues to partner with Downtown establishments to promote offerings on social media platforms, and to provide up-to-the-minute information to drive business.

Chop House Burger

CONSTRUCTION

Dallas County declared construction activity in commercial and multifamily sectors as essential activities, thus allowing construction and construction-related activities within Downtown to continue.

Downtown continues to see nearly 4 million square feet of active projects advance construction in all categories.


Atelier Flora

Notable projects that continue to move forward include:

The Galbraith (2400 Bryan)	Multifamily	448,500 sf
300 Pearl	Mixed Use	519,000 sf
The National	Mixed Use	1,500,000 sf
AMLI at Fountain Place	Multi-Family	350,000 sf
Atelier / Flora Lofts	Multi-Family	468,000 sf
Hall Arts Residences	Multi-Family	261,475 sf
2000 Ross / JW Marriott Hotel	Hotel	445,000 sf
AT&T Discovery District	Retail/Rest.	40,000 sf
Attiva Farmers Market	Multi-Family	200,853 sf
West End Square	Parks	

Many additional developments continue in planning and pre-construction phases. Examples of significant development efforts include:

Phase one of the Woods Capital and Kaizen Developments Field Street District is in predevelopment wile Charter Holdings is envisioning a mix of hospitality, entertainment, and multifamily at the previous Dallas Morning News Headquarters site. Todd Interests has been busy, continuing to develop the East Quarter with new office, residential, and retail as well as improved multimodal infrastructure, while they have pushed to keep the opening of the National at 1401 Elm on schedule.

300 Pearl

The National

In conclusion, the overall Downtown market has seen extraordinary progress with many notable successes within this economic cycle.

There has been exponential growth in residential development, incredible achievements in commercial office leasing, and the long sought-after achievement of the completion of the last full renovation of the 40+ major existing office towers – an effort underway since the early 2000s. Notably, all of these great accomplishments were achieved while simultaneously navigating a variety of challenges, economic crises, and regional and national pressures.

As we continue to leverage our incredible partners, stakeholders, and neighbors to realize the great vision laid out in the 360 Plan and seen on the very streets we walk each day, we continue forward in the confidence that we will not only weather the current hardships being experienced locally, nationally, and globally, but will once again exhibit the uncommon resilience that has historically insulated Downtown during these times, and will ensure once again a swift recovery and national competitiveness unique to Downtown Dallas and the people committed to its success.

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