

Landlords Ease Rent Demands And Flight To Quality Ensues

Reacting to falling leasing activity and weakened demand, landlords of premium buildings eased their rent requirements in 2018 and leased up the most Class A space in three years.

The flight to quality came at the expense of Class B buildings, which account for about half the county's total office inventory. Absorption was negative 896,630 SF in 2018 in this class with three quarters of contraction.

Countywide, demand for space closed the year in the red by 102,307 SF, the first annual net loss since 2009. That follows a 580,000 SF net absorption gain in 2017 and increases averaging nearly 1.4 million SF over the previous four years.

Net absorption for Class A space ended the fourth quarter at 172,929 SF, boosting the total for the year to 808,411 SF. Virtually all of the growth was in the South County market.

Adding to the strain on landlords, 842,816 SF of space was completed this year and about 2.3 million SF - largely creative open-concept campus designs - have been added to inventory since 2016, most of which was developed by the Irvine Co.

But the delivery of the new space has come late in the economic cycle amid signs of slowing expansion and periodical surveys lately showing recent reduced business optimism. This is forcing anxious landlords to cut rent demands and make other concessions.

For example, Class A asking rents increased an average 4.5% over the last 24 months compared to the average 8.5% in rent growth for each of the previous three years. Owners of Class B space, meanwhile, were pushing rents in 2018. Asking lease rates gained an average 9.8% in 2018 after growing at an average 6.6% annually since 2014.

Weakened demand in 2018 in the Airport and Central County markets combined for 972,000 SF of negative absorption. Growth was nearly flat in the West County and North County markets.

South County posted an 835,930-SF gain in 2018 with the Irvine Co. landing much of that tenant growth in its vast and expanding portfolio of premium properties. The company completed two buildings totaling 211,000 SF in the Sand Canyon Business Center earlier in the year. In the fourth quarter the company delivered The Quad, four mid-rise buildings totaling 370,000 SF about 65% pre-leased in the Irvine Spectrum.

Despite posting a strong fourth quarter with 499,321 SF of net absorption, the Airport market, which makes up 38% of the county's inventory, was 613,707 SF in the red for the year.

There were 1,593 lease transactions countywide in 2018, down 27% from 2017 and 25% from the average of the previous five years.

FORECAST

Executives polled in Cal State Fullerton's Q4 business expectations survey expressed reduced optimism with 47% forecasting a healthy profit picture, down from 64% at the end of Q3.

ORANGE COUNTY OFFICE

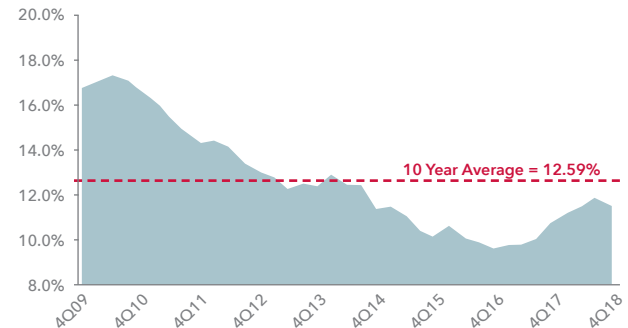
ECONOMIC INDICATORS

	Current Quarter	Prior Quarter
OC Unemployment	2.8%	2.8%
California Unemployment	3.9%	3.9%
US Unemployment	3.9%	3.7%

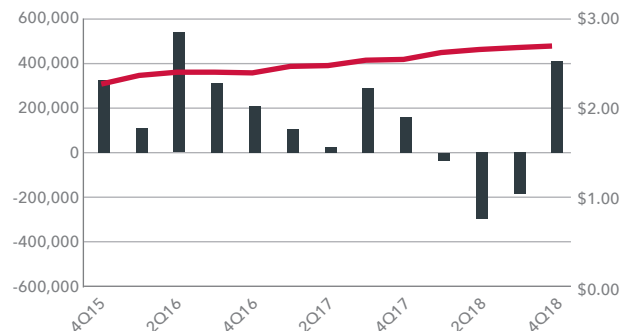
MARKET INDICATORS

	Current Quarter	Prior Quarter
Total Inventory (SF)	114,935,455	114,897,142
Vacancy Rate (%)	11.46%	11.79%
Net Absorption (SF)	413,204	(185,800)
Average Asking Rent (\$/SF)	\$2.70	\$2.66
Under Construction (SF)	1,215,520	1,174,633

OVERALL VACANCY



NET ABSORPTION VS ASKING RATES



ORANGE COUNTY

FOURTH QUARTER 2018 OFFICE MARKET REPORT

ORANGE COUNTY MARKET STATISTICS - 4Q 2018

BY AREA

	Bldg Count	SF RBA	Total SF Available	Avail. Rate	Total SF Vacant	Total Vac. Rate	Net Absorption	YTD Net Absorption	Avg Asking Lease Rate	SF Under Construction
North Orange County	170	14,141,010	1,399,753	9.9	1,155,208	8.2%	60,883	23,631	\$2.24	- 0 -
Central Orange County	262	22,665,687	3,949,657	17.1	2,684,813	11.8%	(1,412)	(358,294)	\$2.25	417,609
West Orange County	129	8,985,152	1,054,457	11.7	640,657	7.1	(20,132)	10,133	\$2.33	- 0 -
Greater Airport Area	422	43,370,273	7,696,775	17.5	5,855,759	13.5%	499,321	(613,707)	\$2.99	507,511
South Orange County	352	25,773,333	4,154,512	15.9	2,839,535	11%	(125,456)	835,930	\$2.82	290,400
TOTALS	1,335	114,935,455	18,255,154	15.88%	13,175,972	11.5%	413,204	(102,307)	\$2.70	1,215,520

ORANGE COUNTY MARKET STATISTICS - 4Q 2018

BY SUBMARKET

	Bldg Count	SF RBA	Total SF Available	Avail. Rate	Total SF Vacant	Total Vac. Rate	Net Absorption	YTD Net Absorption	Avg Asking Lease Rate	SF Under Construction
Class A	302	49,001,239	9,930,170	19.8	6,863,461	14%	172,929	808,411	\$2.92	1,060,520
Class B	945	61,447,371	8,028,698	13.0	6,106,898	9.9%	268,224	(896,630)	\$2.56	155,000
Class C	88	4,486,845	296,286	6.6	205,613	4.6%	(27,949)	(14,088)	\$2.05	- 0 -
TOTALS	1,335	114,935,455	18,255,154	15.9%	13,175,972	11.5%	413,204	(102,307)	\$2.70	1,215,520

LEASE TRANSACTIONS 4Q 2018

PROPERTY	SF	TENANT	LANDLORD	REPRESENTING BROKERS
5271 California Avenue, #200 & 300 Irvine, CA	40,835	Ready At Dawn Studios	The Irvine Company	Phil Cohen, Kurt Bruggeman & Ryan Swanson represented the Tenant.
1240 N. Lakeview Avenue #120, Anaheim, CA	10,627	Novo Missions, Inc.	FKC Lakeview, LLC	Craig DeMiranda represented the Tenant.
16755 Von Karman Avenue, Ste 150 Irvine, CA 92606	6,402	Adams Streeter Civil Engineers	BRE CA Office Owner, LLC	Gary McArdell and John Collins represented the Tenant

SALE TRANSACTIONS 4Q 2018

PROPERTY	SF	BUYER	SELLER	REPRESENTING BROKERS
2650 E. Imperial Highway Brea, CA	27,379	Mahn Properties, LLC	Brea Office Portfolio, LLC	John Son represented the Buyer.
17871 Mitchell North Irvine, CA	13,702	3339 Exposition Place	Yocum-Baldwin Development and John & Kathleen Hamilton Family Trust	John Collins represented the Seller.
1900 Quail Newport Beach, CA	10,000	Paul Alteri	Sunshine Ventures, LLC	Allen Basso and Ryan Harman represented the Seller.

LEE & ASSOCIATES - IRVINE

9838 Research Drive
Irvine, California 92618
(949) 727-1200

LEE & ASSOCIATES - NEWPORT BEACH

100 Bayview Circle, Suite 600
Newport Beach, California 92660
(949) 724-1000

LEE & ASSOCIATES - ORANGE

1004 West Taft Avenue, Suite 150
Orange, California 92865
(714) 647-9100

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