

FURTHER STRENGTHENING. Stimulated by a broad base of demand, the Orange County office market continues to grow. Net absorption year to date is robust, the vacancy rate is declining, and we see cumulative rent growth. By the end of the third quarter of 2016, the vacancy rate had declined to 10.09% which is 66 basis points better than last year. Mortgage, insurance, and education tenants were most active during the quarter, particularly in the Airport Area.

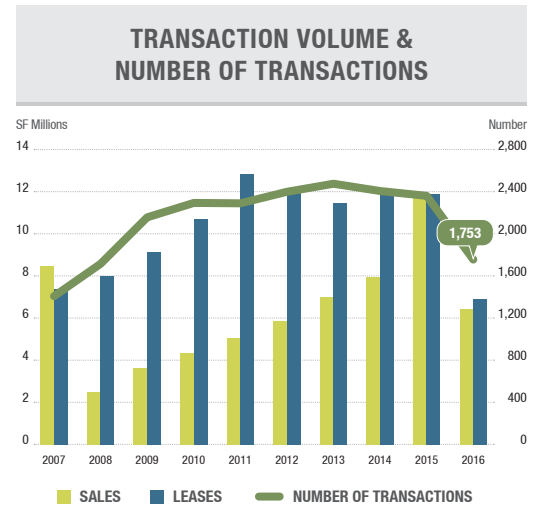
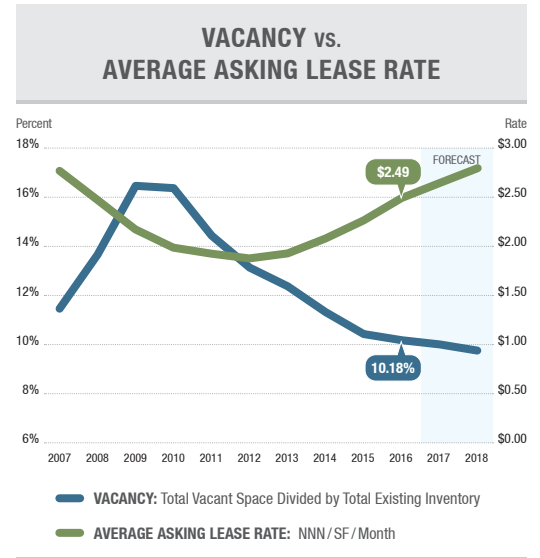
VACANCY. Vacancy rates in Orange County office buildings fell to 10.18% at the end of third quarter 2016. Vacancy rates in the county have been steadily declining since highs of 16.96% were posted in the second quarter of 2010. Local companies are expanding and account for much of the positive vacancy helping to fill up many of the buildings in the Airport and South County markets.

LEASE RATES. Orange County average asking rental rates continue to rise at a double digit clip year over year. The Orange County office average asking rent of \$2.49 per square foot was up 2.05% from the second quarter 2016 rate of \$2.44, and up from last year's third quarter rate of \$2.20.

TRANSACTION ACTIVITY. Leasing activity for the third quarter totaled 1.68 million square feet in 469 separate transactions, which was only 50% of the lease activity from the third quarter of 2015, (total leasing activity in the third quarter of 2015 was 3.29 million square feet). Notable activity this quarter included Nationstar Mortgage's 130,000 square foot lease in Santa Ana, Crown Castle's 44,300 square foot lease in Irvine Spectrum, and UCI's 31,720 square foot deal in Irvine.

EMPLOYMENT. The unemployment rate in Orange County was 4.4% in August 2016, down from a revised 4.6% in July 2016, and below the year-ago estimate of 4.6%. This compares with an unadjusted unemployment rate of 5.6% for California and 5.0% for the nation during the same period.

OVERALL. The office market sector posted strong gains, with higher rents and lower vacancies helping to fuel the construction of new office buildings. It's certainly tilted toward more of a landlord's market, but Orange County rents are still a relative bargain compared to its neighbors to the north.



Market Statistics

	Change Over Last Quarter	3Q 2016	2Q 2016	3Q 2015	% Change Over Last Year
Vacancy Rate	▼ DOWN	10.18%	10.53%	10.51%	-3.14%
Availability Rate	▲ UP	15.16%	14.59%	14.55%	4.19%
Average Asking Lease Rate	▲ UP	\$2.49	\$2.44	\$2.20	13.18%
Sale & Lease Transactions	▲ UP	4,492,406	4,350,606	5,590,676	-19.64%
Gross Absorption	▲ UP	2,719,085	2,284,155	2,987,777	-8.99%
Net Absorption	▲ POSITIVE	407,774	592,672	(26,918)	N/A

LEASE RATES. Expect the average asking lease rates to increase by 2% to 3% over the next three quarters.

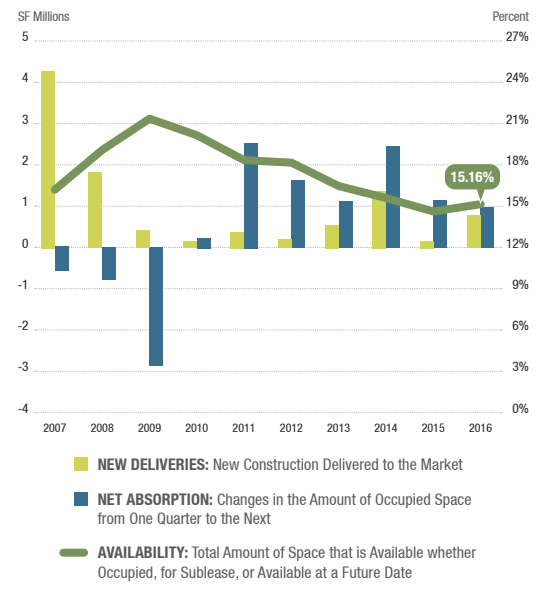
VACANCY. We anticipate vacancy will continue to decrease slightly in the coming two quarters, and then slightly popping up with the new developments coming on line.

CONSTRUCTION. A diverse tenant base coupled with population growth has fueled new construction in O.C. Total space under construction was roughly 2.4 million square feet for the quarter, which was more than triple the 767,909 square feet under construction this time last year. Three large developments are located in Irvine: The Broadway, Broadcom campus, and 400 Spectrum.

AVAILABILITY. Available direct/sublease space came in at 15.16% at the close of the third quarter, which was slightly up from 2015's third quarter rate of 14.55% and from 2016's second quarter rate of 14.59%. The popularity of retrofitting and repurposing older industrial buildings has helped to bolster the supply ahead of new development. For example, the former Los Angeles Times property in Costa Mesa at 1375 Sunflower Avenue is transforming 700,000 square feet into modern product, including "creative" office space

ABSORPTION. The Orange County office market posted 407,774 square feet of positive net absorption in the third quarter, totaling 974,748 square feet of absorption year to date. The strong absorption is mainly due to the positive job growth throughout the county over the past year. In addition, favorable financing has helped many existing companies to invest and expand.

NEW DELIVERIES & NET ABSORPTION vs. AVAILABILITY RATE



Significant Transactions

Sales

Property Address	Submarket	Class	Square Feet	Sale Price	Buyer	Seller
500 City Pkwy. W. – 3 Properties	Orange	A	442,521	\$107,365,000	Greenlaw Partners, LLC	Walton Street Capital
1733–1833 Alton Pkwy. – 2 Properties	Irvine	B	209,351	\$64,000,000	GI Partners	Hines
26732 Crown Valley Pkwy.	Mission Viejo	A	120,172	\$56,397,012	Healthcare Trust of America	St. Joseph Health System
23807–23811 Aliso Creek Rd.	Laguna Niguel	B	233,996	\$53,693,000	Dunhill Partners, Inc.	The Colton Company
24422 Avenida de la Carlota	Laguna Hills	A	119,559	\$30,000,000	Angelo, Gordon & Co.	Lincoln Property Company

Leases

* Voit Real Estate Services Deal

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
1600 E. Saint Andrew Pl.	Santa Ana	B	130,000	Jul-2016	Nationstar Mortgage *	The Brookhollow Group
200 Spectrum Center Dr.	Irvine Spectrum	A	44,239	Jul-2016	Crown Castle	The Irvine Company
3390 Harbor Blvd. – Renewal	Costa Mesa	C	40,091	Sep-2016	John F. Kennedy	Harbor Associates
2010 Main St. – Renewal	Irvine	A	25,137	Jul-2016	Wunderman West	Shorenstein Realty Services
3 Ada St.	Irvine Spectrum	B	24,360	Sep-2016	Montage Hotels	The Irvine Company

INVENTORY

VACANCY & LEASE RATES

ABSORPTION

	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 3Q2016	Square Feet Available	Availability Rate 3Q2016	Average Asking Lease Rate	Net Absorption 3Q2016	Net Absorption 2016	Gross Absorption 3Q2016	Gross Absorption 2016
Airport Area													
Costa Mesa	71	7,294,628	0	442,476	897,862	12.31%	1,303,457	17.87%	\$2.49	43,092	158,385	204,698	524,679
Irvine	256	23,995,292	537,224	782,000	2,211,085	9.21%	4,781,364	19.93%	\$2.83	49,592	(258,119)	586,184	1,434,433
Newport Beach	120	9,945,353	44,000	68,346	797,042	8.01%	1,168,666	11.75%	\$3.53	(40,626)	167,846	155,508	737,357
Santa Ana	15	2,448,402	0	0	408,047	16.67%	489,486	19.99%	\$2.40	81,564	51,661	275,298	414,706
Airport Area Total	462	43,683,675	581,224	1,292,822	4,314,036	9.88%	7,742,973	17.73%	\$2.98	133,622	119,773	1,221,688	3,111,175
Central County													
Anaheim	17	1,949,215	0	300,000	343,446	17.62%	394,214	20.22%	\$2.52	(6,213)	34,068	34,360	130,280
Orange	83	7,154,500	0	0	582,358	8.14%	764,501	10.69%	\$2.09	(68,006)	(59,972)	62,654	286,944
Santa Ana	167	12,420,638	0	702,325	1,825,057	14.69%	1,883,305	15.16%	\$1.88	181,252	124,856	360,999	732,391
Tustin	43	2,268,702	0	1,179,124	494,705	21.81%	589,986	26.01%	\$2.16	18,971	(135,382)	53,379	141,667
Central County Total	310	23,793,055	0	2,181,449	3,245,566	13.64%	3,632,006	15.26%	\$1.97	126,004	(36,430)	511,392	1,291,282
North County													
Anaheim Hills	82	5,923,268	0	0	621,502	10.49%	890,529	15.03%	\$2.02	45,312	49,595	78,813	189,539
Brea	42	4,053,071	0	120,000	406,749	10.04%	596,045	14.71%	\$2.15	(19,279)	38,602	57,078	215,575
Buena Park	17	1,115,193	0	0	105,138	9.43%	254,123	22.79%	\$1.74	(16,162)	31,525	1,465	117,313
Fullerton	30	2,432,708	0	0	176,473	7.25%	374,136	15.38%	\$1.80	10,247	37,196	27,715	80,511
La Habra	4	142,069	0	0	0	0.00%	0	0.00%	\$0.00	0	0	0	0
La Palma	10	712,038	0	0	93,266	13.10%	59,679	8.38%	\$0.00	32,647	26,420	36,762	88,543
Placentia	8	267,589	0	0	33,419	12.49%	39,308	14.69%	\$1.59	(3,168)	2,718	3,906	11,334
Yorba Linda	5	288,094	0	0	42,809	14.86%	42,809	14.86%	\$1.86	(8,257)	(8,830)	0	929
North County Total	198	14,934,030	0	120,000	1,479,356	9.91%	2,256,629	15.11%	\$1.97	41,340	177,226	205,739	703,744
South County													
Aliso Viejo	43	3,124,343	205,000	0	275,094	8.80%	514,836	16.48%	\$3.18	(20,497)	(44,937)	41,746	96,967
Dana Point	2	91,876	0	0	0	0.00%	0	0.00%	\$0.00	0	0	0	0
Foothill Ranch	10	798,721	0	0	86,780	10.86%	146,475	18.34%	\$2.51	(8,665)	(13,672)	88,162	100,397
Irvine Spectrum	157	10,793,155	1,558,796	414,332	709,916	6.58%	962,860	8.92%	\$3.17	51,575	553,489	292,855	1,153,695
Laguna Beach	5	192,434	0	0	20,834	10.83%	22,414	11.65%	\$0.00	3,763	8,061	3,763	15,953
Laguna Hills	32	1,816,327	0	0	276,336	15.21%	327,056	18.01%	\$2.43	18,637	17,726	50,305	190,514
Laguna Niguel	10	1,750,428	0	0	48,915	2.79%	58,733	3.36%	\$0.00	5,522	5,653	7,679	22,367
Lake Forest	40	2,100,640	0	0	137,290	6.54%	341,776	16.27%	\$2.12	(16,671)	91,086	29,465	200,681
Mission Viejo	36	1,925,414	0	110,000	211,883	11.00%	279,153	14.50%	\$2.19	(31,534)	7,785	40,544	121,059
Rancho Santa Margarita	6	250,472	0	0	17,923	7.16%	21,996	8.78%	\$2.11	496	2,810	4,360	8,422
San Clemente	12	502,157	0	0	31,466	6.27%	39,568	7.88%	\$2.30	6,397	(13,094)	9,832	25,276
San Juan Capistrano	17	876,712	0	0	138,014	15.74%	146,084	16.66%	\$2.44	12,964	16,536	14,656	36,696
South County Total	370	24,222,679	1,763,796	524,332	1,954,451	8.07%	2,860,951	11.81%	\$2.76	21,987	631,443	583,367	1,972,027
West County													
Cypress	29	2,001,637	0	0	391,133	19.54%	552,483	27.60%	\$1.94	(2,726)	(24,683)	17,640	49,342
Fountain Valley	33	1,995,993	0	0	75,313	3.77%	82,379	4.13%	\$1.45	6,044	12,544	6,044	48,175
Garden Grove	20	1,562,070	0	0	65,013	4.16%	67,589	4.33%	\$1.82	(5,985)	(12,772)	22,544	74,414
Huntington Beach	43	2,482,937	44,500	0	158,577	6.39%	257,045	10.35%	\$2.22	86,930	111,406	129,278	256,485
Los Alamitos	12	687,842	0	0	33,655	4.89%	40,440	5.88%	\$0.00	1,392	(1,479)	3,085	18,087
Seal Beach	7	473,787	0	0	50,811	10.72%	53,450	11.28%	\$2.81	(2,853)	1,658	3,844	14,765
Stanton	4	143,361	0	0	10,173	7.10%	18,263	12.74%	\$1.25	825	(1,734)	5,935	7,882
Westminster	12	482,280	0	0	74,026	15.35%	88,543	18.36%	\$2.15	1,194	(2,204)	8,529	15,691
West County Total	160	9,829,907	44,500	0	858,701	8.74%	1,160,192	11.80%	\$2.10	84,821	82,736	196,899	484,841
Orange County Total	1,500	116,463,346	2,389,520	4,118,603	11,852,110	10.18%	17,652,751	15.16%	\$2.49	407,774	974,748	2,719,085	7,563,069
Airport Area													
Class A	128	25,363,713	581,224	847,000	3,083,917	12.16%	4,975,741	19.62%	\$3.30	130,517	45,130	805,938	2,072,255
Class B	308	17,024,628	0	445,822	1,162,510	6.83%	2,642,439	15.52%	\$2.50	7,603	69,524	367,337	967,614
Class C	26	1,295,334	0	0	67,609	5.22%	124,793	9.63%	\$1.89	(4,498)	5,119	48,413	71,306
Central County													
Class A	44	7,335,977	0	1,879,449	930,633	12.69%	1,041,782	14.20%	\$2.22	89,494	3,388	258,061	495,791
Class B	210	14,021,058	0	302,000	2,108,670	15.04%	2,309,966	16.47%	\$1.94	35,651	(24,291)	220,690	705,967
Class C	56	2,436,020	0	0	206,263	8.47%	280,258	11.50%	\$1.49	859	(15,527)	32,641	89,524
North County													
Class A	27	3,181,283	0	120,000	460,362	14.47%	648,472	20.38%	\$2.19	6,360	15,753	89,138	202,121
Class B	147	10,823,415	0	0	966,290	8.93%	1,544,099	14.27%	\$1.90	33,679	160,056	113,812	490,786
Class C	24	929,332	0	0	52,704	5.67%	64,058	6.89%	\$2.10	1,301	1,417	2,789	10,837
South County													
Class A	61	7,373,497	1,763,796	453,332	691,499	9.38%	899,789	12.20%	\$3.14	78,369	225,050	283,355	629,482
Class B	299	16,355,314	0	71,000	1,261,694	7.71%	1,958,670	11.98%	\$2.40	(56,927)	407,120	297,998	1,337,926
Class C	10	493,868	0	0	1,258	0.25%	2,492	0.50%	\$1.59	545	(727)	2,014	4,619
West County													
Class A	23	2,464,991	0	0	256,135	10.39%	437,204	17.74%	\$2.53	(2,677)	20,834	23,345	135,424
Class B	115	6,459,451	44,500	0	565,750	8.76%	678,791	10.51%	\$1.90	88,889	60,376	171,729	329,961
Class C	22	905,465	0	0	36,816	4.07%	44,197	4.88%	\$0.00	(1,391)	1,526	1,825	19,456
Orange County													
Class A	283	45,719,461	2,345,020	3,299,781	5,422,546	11.86%	8,002,988	17.50%	\$2.93	302,063	310,155	1,459,837	3,535,073
Class B	1,079	64,683,866	44,500	818,822	6,064,914	9.38%	9,133,965	14.12%	\$2.14	108,895	672,785	1,171,566	3,832,254
Class C	138	6,060,019	0	0	364,650	6.02%	515,798	8.51%	\$1.61	(3,184)	(8,192)	87,682	195,742
Orange County Total	1,500	116,463,346	2,389,520	4,118,603	11,852,110	10.18%	17,652,751	15.16%	\$2.49	407,774	974,748	2,719,085	7,563,069

This survey consists of office properties 25,000 square feet and larger in size, representing both single tenant and multi-tenant buildings. The lease rates are based on a full-service gross basis.



Market Update

by **Stefan Rogers**

SENIOR VICE PRESIDENT, IRVINE

The Orange County economy and office market showed continued strength in Q3 2016 with more than 850,000 square feet of net absorption (an increase of more than 100,000 compared with Q3 2015) and a 0.41% increase in asking office rents. Over 1.3 million square feet of absorption and 2.95% of rental growth has been recorded in 2016 and office rents are now at or above record highs in core submarkets.

Typically, this data would indicate signs of an anticipated correction or softening in the office market, however strong economic and demographic fundamentals suggest the contrary. While some uncertainty exists over the timing of an interest rate increase and the results of the upcoming general election, we expect the impact to be fairly minimal in Orange County given the diversity of our local economy.

This trend is attributed primarily to continued job growth in the automotive, technology, financial services, medical, and construction sectors. Developers are responding with exciting new projects including 400 Spectrum Center, The Press (the former LA Times site) in Costa Mesa, and The Boardwalk in Irvine. Orange County is increasingly viewed as a highly desirable place to do business due to the educated workforce, attractive Southern California lifestyle and relative affordability of office space compared with many other suburban markets (Los Angeles & San Francisco).

The current landscape presents opportunities for developers/investors, landlords, tenants, buyers and sellers alike. Developers have a unique window to focus on tenant demand and workplace trends while continuing to seek viable, value-add and adaptive reuse opportunities. Landlords have an opportunity to push rents and improve tenant retention by enhancing onsite amenities and services, while consulting closely with tenants to deliver more functional, customized workplaces to help their customers boost their bottom line. Tenants are now looking at longer leases, allowing them to extract maximum economic concessions and control their overall occupancy costs. They are focused on efficiency and intelligent workspace design to maximize recruitment, retention and productivity. Flexibility to expand and contract over time is a key driver for tenants right now as they leverage technology to minimize their real estate footprint.

Buyers, both investors and users, have been taking advantage of the low cost of capital to acquire stabilized long-term investments and we anticipate this trend to continue. Although the capital markets are showing some signs of a correction, sellers are continuing to take advantage of the tremendous flow of capital targeting commercial real estate. Foreign investors, trade buyers and institutional investors continue to compete for a very limited number of quality buildings. While a temporary gap exists in the "bid versus ask" figures on product listed for sale, we expect pricing to hold based on the overall supply/demand imbalance and the strength shown by corporate occupiers as well as local, entrepreneurial firms.

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Product Type

CLASS A: Most prestigious buildings competing for premier office users with rents above average for the area. Buildings have high-quality standard finishes, state-of-the-art systems, exceptional accessibility and a definite market presence.

CLASS B: Buildings competing for a wide range of users with rents in the average range for the area. Building finishes are fair to good for the area, and systems are adequate. However, Class B buildings cannot compete with Class A buildings of the same price.

CLASS C: Buildings competing for tenants requiring functional space at rents below the area average.

Submarkets

AIRPORT AREA

Costa Mesa, Irvine, Newport Beach

CENTRAL COUNTY

Anaheim, Orange, Santa Ana, Tustin

NORTH COUNTY

Anaheim Hills, Brea, Buena Park, Fullerton, La Habra, La Palma, Placentia, Yorba Linda

SOUTH COUNTY

Aliso Viejo, Dana Point, Foothill Ranch, Irvine Spectrum, Laguna Beach, Laguna Hills, Laguna Niguel, Lake Forest, Mission Viejo, Rancho Santa Margarita, San Clemente, San Juan Capistrano

WEST COUNTY

Cypress, Fountain Valley, Garden Grove, Huntington Beach, Los Alamitos, Seal Beach, Stanton, Westminster