

Office Market Report

Compared to the Previous Quarter:

Vacancy

DOWN

Net Absorption

POSITIVE

Lease Rates

UP

Transactions

UP

Deliveries

UP

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Market Highlights

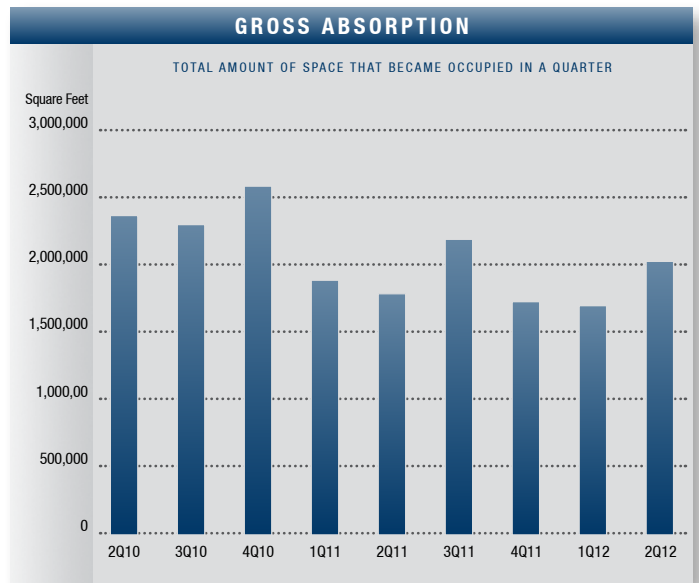
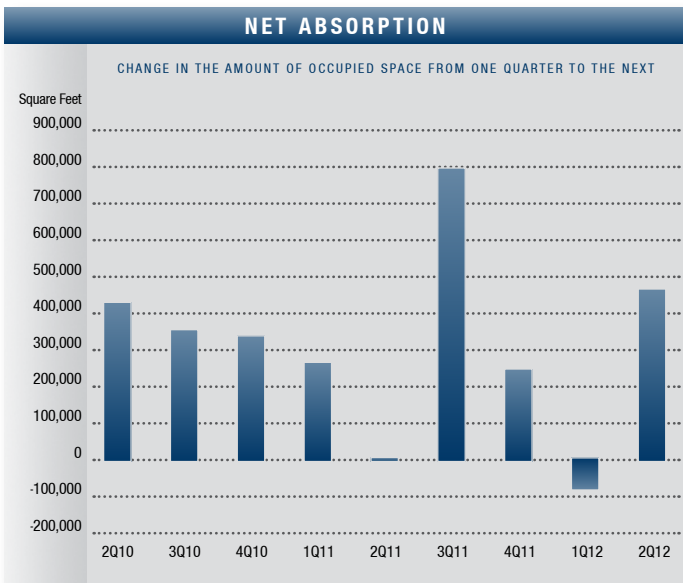
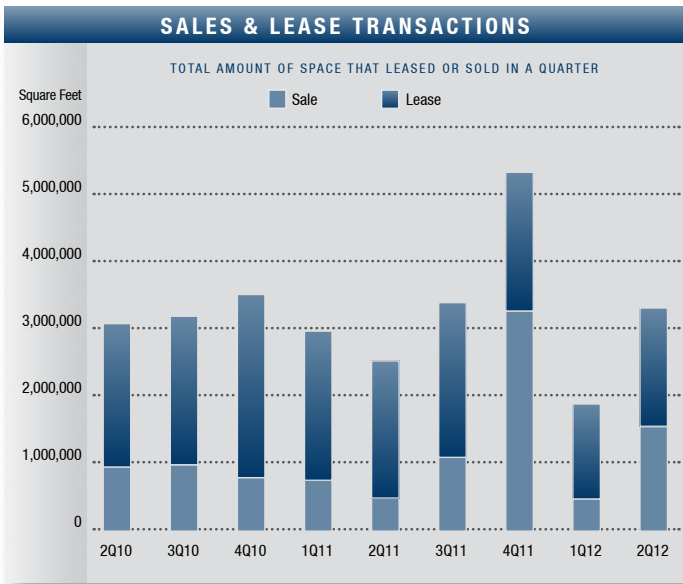
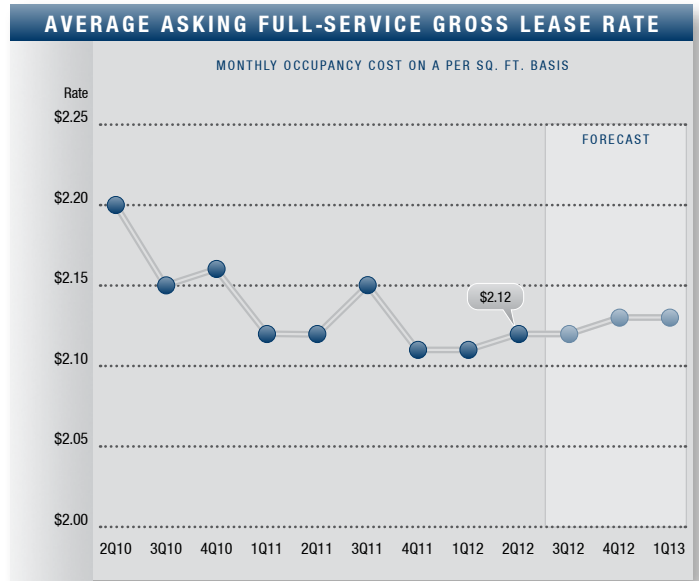
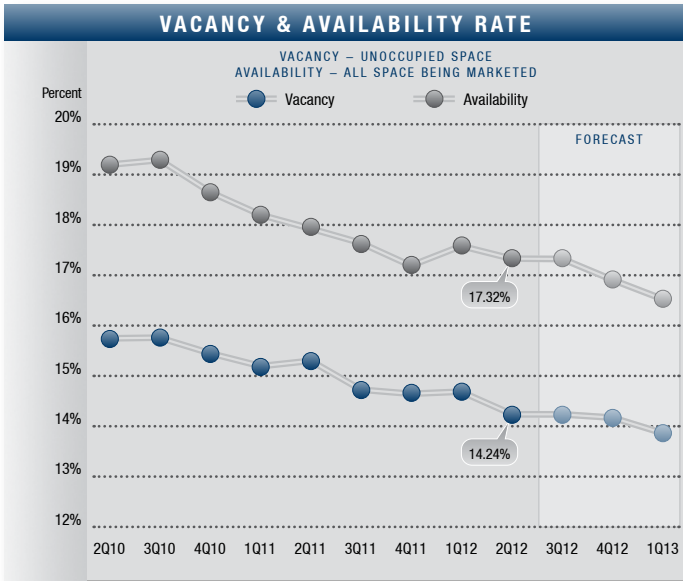
- Bounce Back Quarter** - After a slight step back for the San Diego office market in the first quarter of 2012, the second quarter posted positive numbers, with a decrease in vacancy, solid positive net absorption, and a gain in transaction volume. The average asking rate for office space was up compared to the previous quarter, an indication that lease rates may be stabilizing. While net absorption was slightly negative in the first quarter, over the past nine quarters, the market accumulated over 2.8 million square feet of positive absorption. While these are positive indications, stability will need to be sustained in coming quarters to be considered recovery.
- Construction** - Over the past five years over 7.7 million square feet of new construction was completed in San Diego County. The record year for new development was 2001, when 3.7 million square feet of new space was added. Total space under construction checked in at 1.8 million square feet in the second quarter of 2012.
- Vacancy** - Direct/sublease space (unoccupied) finished the quarter at 14.24%, a decrease from the previous quarter's figure of 14.7% and the lowest rate seen since mid-2008. The Central Suburban market posted the lowest rate in the county, at 10.7%.
- Availability** - Direct/sublease space being marketed was 17.32% at the end of the second quarter, a decrease of 1.5% when compared to the 17.58% availability rate of first quarter 2012.
- Lease Rates** - The average asking full-service gross (FSG) lease rate per square foot per month in San Diego County was \$2.12 for the quarter, up one cent from the previous quarter. The record high rate of \$2.76 was established in the first and second quarters of 2008. The highest rates for the county were in the North County Coastal area, where the average asking lease rate was \$2.74 FSG. Class A rates for the county averaged \$2.51 FSG.
- Absorption** - The San Diego office market posted 463,997 square feet of positive net absorption this quarter, the ninth

quarter of positive net absorption of the last ten quarters. Look for professional and business services, leisure and hospitality, defense, medical and alternative energy companies to lead the charge of positive absorption over the next few years.

- Transaction Activity** - Sale and lease transactions totaled 3.3 million square feet in the first quarter, nearly doubling the 1.8 million square feet in the first quarter of 2012. A large portion of sale volume in the second quarter was the sale of the ±642,000-square-foot San Diego Tech Center. Details of the largest transactions can be found on the back page of this report.
- Employment** - The unemployment rate in the San Diego County was 8.8% in May 2012, unchanged from a revised 8.8% in April 2012 and below the year-ago estimate of 9.8%. This compares with an unadjusted unemployment rate of 10.4% for California and 7.9% for the nation during the same period. According to the State of California Employment Development Department, San Diego County gained 13,400 payroll jobs from May 2011 to May 2012 — 5,400 in educational and health services and 5,300 in professional and business services. Manufacturing posted the greatest year-over-year decline — a loss of 2,300 jobs.
- Overall** - The recovery has not been overwhelming to this point, but overall, the office market has been steadily improving over the last two years. With few new deliveries in the pipeline to apply upward pressure on vacancy, and the market has begun to stabilize. We foresee a continued increase in investment activity in the coming quarters as lenders dispose of distressed assets. Lease rates are expected to continue to firm up and possibly increase in the fourth quarter of 2012. We should also see an increase in leasing activity as many short-term deals come up for renewal. Unemployment rates have continued to drop since the peak in January 2010. As job creation continues and consumer confidence stabilizes, the office market will continue to recover.

OFFICE MARKET OVERVIEW

	2Q12	1Q12	2Q11	% of Change vs. 2Q11
Total Vacancy Rate	14.24%	14.70%	15.26%	(6.68%)
Availability Rate	17.32%	17.58%	17.99%	(3.72%)
Average Asking Lease Rate	\$2.12	\$2.11	\$2.12	0.00%
Sale & Lease Transactions	3,281,289	1,841,836	2,496,084	31.46%
Gross Absorption	2,000,348	1,692,849	1,780,705	12.33%
Net Absorption	463,997	(77,383)	7	N/A



	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 2Q2012	Square Feet Available	Availability Rate 2Q2012	Average Asking Lease Rate	Net Absorption 2Q2012	Net Absorption 2012	Gross Absorption 2Q2012	Gross Absorption 2012
Central													
Downtown	142	12,950,126	0	0	2,235,965	17.27%	2,881,517	22.25%	\$2.16	(6,555)	43,659	134,887	328,537
Central Total	142	12,950,126	0	0	2,235,965	17.27%	2,881,517	22.25%	\$2.16	(6,555)	43,659	134,887	328,537
Central Suburban													
City Heights/University	28	1,024,375	0	0	67,389	6.58%	103,918	10.14%	\$1.63	794	47,680	12,945	73,162
Coronado	6	124,741	0	0	7,361	5.90%	1,725	1.38%	\$0.00	(2,898)	(3,939)	1,041	1,041
Kearny Mesa	236	10,288,215	573,353	193,000	1,088,837	10.58%	1,279,869	12.44%	\$1.62	80,646	69,121	182,564	322,559
Mission Gorge	26	603,823	0	0	53,295	8.83%	55,035	9.11%	\$1.15	1,995	1,995	3,737	3,737
Mission Valley	126	7,020,335	0	55,000	928,796	13.23%	1,068,233	15.22%	\$1.93	51,490	(31,431)	203,767	356,558
Old Town/Point Loma	83	2,561,809	0	0	245,713	9.59%	347,292	13.56%	\$1.59	(5,241)	4,757	16,974	45,535
Park East	8	161,365	0	0	11,063	6.86%	28,360	17.58%	\$2.10	(540)	(2,411)	1,519	3,742
Rose Canyon/Morena	58	1,302,584	0	11,160	132,594	10.18%	145,884	11.20%	\$1.85	(2,844)	(497)	20,487	52,843
Uptown/Hillcrest	106	2,640,467	66,365	72,514	215,350	8.16%	251,915	9.54%	\$2.13	(14,324)	(15,066)	15,962	25,061
Central Suburban Total	677	25,727,714	639,718	331,674	2,750,398	10.69%	3,282,231	12.76%	\$1.72	109,078	70,209	458,996	884,238
Highway 78 Corridor													
Oceanside	56	1,212,291	57,476	352,946	239,126	19.73%	229,655	18.94%	\$1.60	13,781	(1,428)	18,131	25,008
San Marcos	37	1,278,270	71,200	818,000	247,587	19.37%	260,705	20.40%	\$2.25	(15,035)	(13,802)	19,741	42,833
Vista	49	1,156,987	0	215,350	175,674	15.18%	212,523	18.37%	\$1.43	229	(5,380)	6,606	11,994
Highway 78 Corridor Total	142	3,647,548	128,676	1,386,296	662,387	18.16%	702,883	19.27%	\$1.42	(1,025)	(20,610)	44,478	79,835
I-15 Corridor													
Escondido	90	1,894,574	0	43,107	313,619	16.55%	341,906	18.05%	\$1.61	(2,591)	345	27,162	51,773
Poway	27	1,315,857	0	790,570	84,946	6.46%	87,808	6.67%	\$0.00	6,026	10,653	6,026	24,000
Rancho Bernardo	104	6,425,841	40,398	1,136,675	748,342	11.65%	807,952	12.57%	\$1.92	(1,255)	18,763	129,734	241,040
Scripps Ranch	51	2,720,608	0	377,000	865,991	31.83%	770,179	28.31%	\$2.15	63,631	105,380	82,732	141,377
I-15 Corridor Total	272	12,356,880	40,398	2,347,352	2,012,898	16.29%	2,007,845	16.25%	\$1.96	65,811	135,141	245,654	458,190
North City													
Governor Park	19	866,467	0	0	73,328	8.46%	171,815	19.83%	\$2.10	(6,868)	3,894	26,002	53,247
La Jolla	56	1,703,614	0	0	169,575	9.95%	300,791	17.66%	\$2.70	(4,415)	(2,064)	35,801	69,236
Miramar	37	1,606,962	0	0	265,398	16.52%	294,028	18.30%	\$1.68	(2,229)	(28,595)	31,761	36,755
Sorrento Mesa	115	8,524,728	350,882	1,440,712	1,068,944	12.54%	1,120,119	13.14%	\$2.67	(24,502)	(30,557)	66,356	155,009
Sorrento Valley	27	834,350	0	0	88,664	10.63%	115,876	13.89%	\$1.61	14,229	(8,093)	20,716	27,824
Torrey Pines	47	3,291,494	0	0	248,517	7.55%	570,212	17.32%	\$3.75	5,647	23,781	17,671	58,784
UTC Center	83	7,575,244	538,004	175,000	1,045,311	13.80%	1,559,276	20.58%	\$2.74	294,431	301,861	341,575	607,563
North City Total	384	24,402,859	888,886	1,615,712	2,959,737	12.13%	4,132,117	16.93%	\$2.59	276,293	260,227	539,882	1,008,418
North County													
Carlsbad	152	5,960,868	0	492,000	1,384,218	23.22%	1,641,527	27.54%	\$2.18	10,734	(15,476)	157,887	321,865
Del Mar Heights/Carmel Valley	67	4,398,506	0	682,136	821,584	18.68%	1,089,631	24.77%	\$3.18	13,237	(27,610)	257,117	341,774
North Beach Cities	110	2,419,293	63,941	48,708	220,796	9.13%	316,728	13.09%	\$2.67	3,363	(24,715)	56,245	93,229
North County Total	329	12,778,667	63,941	1,222,844	2,426,598	18.99%	3,047,886	23.85%	\$2.74	27,334	(67,801)	471,249	756,868
South/Southeast Corridor													
Chula Vista	90	2,757,852	45,000	273,122	456,640	16.56%	474,615	17.21%	\$1.55	(41,370)	(59,150)	43,366	73,010
East County	160	3,845,871	0	552,200	334,898	8.71%	371,560	9.66%	\$1.55	12,080	11,935	36,624	70,633
National City	15	533,398	0	20,000	225,592	42.29%	239,619	44.92%	\$0.00	14,692	4,651	15,438	21,458
Otay Mesa	13	328,316	0	0	32,810	9.99%	34,074	10.38%	\$0.00	7,659	8,353	9,774	12,060
Southeast San Diego	10	426,932	0	0	102,580	24.03%	102,580	24.03%	\$1.25	0	0	0	0
South/Southeast Total	288	7,892,369	45,000	845,322	1,152,520	14.60%	1,222,448	15.49%	\$1.56	(6,939)	(34,211)	105,202	177,161
Class A	251	31,549,890	1,007,361	5,026,894	4,317,909	13.69%	5,272,236	16.71%	\$2.51	356,066	537,226	838,938	1,494,018
Class B	1,204	51,134,337	799,258	2,722,306	8,067,597	15.78%	9,844,809	19.25%	\$1.86	133,185	(60,169)	954,491	1,818,146
Class C	779	17,071,936	0	0	1,814,997	10.63%	2,159,882	12.65%	\$1.49	(25,254)	(90,443)	206,919	381,083
San Diego County Total	2,234	99,756,163	1,806,619	7,749,200	14,200,503	14.24%	17,276,927	17.32%	\$2.12	463,997	386,614	2,000,348	3,693,247

This survey consists of buildings greater than 10,000 square feet. Lease rates are on a full-service gross basis.

RECENT TRANSACTIONS

Sales Transactions

Property Address	Submarket	Class	Square Feet	Price Per SF	Buyer	Seller
9605-9855 Scranton Rd & 10055-10075 Barnes Canyon Rd.	Sorrento Mesa	B	641,693	\$237.65	Beacon Capital Partners, LLC	MPG Office Trust, Inc.
5780 Fleet St.	Carlsbad	A	121,380	\$238.92	Coast Income Properties, Inc.	Brandywine Realty Trust
855 & 865 3rd Ave.	Chula Vista	B	74,894	\$328.46	Griffin-American Healthcare REIT II	Grasela Investments, LLC
401 Mile of Cars Way	National City	B	198,198	\$83.75	Walton Street Capital, LLC	Textron Financial Corporation
5770 Armada Dr.	Carlsbad	B	81,712	\$190.91	LBA Realty	Carlsbad Ranch, LP

Lease Transactions

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
6965 Lusk Blvd.	Sorrento Mesa	B	74,558	June-12	Qualcomm	Colony Realty Partners
5770 Armada Dr.	Carlsbad	B	70,052	April-12	SkinMedica	LBA Realty
10670 Wexford St. – Renewal	Scripps Ranch	B	50,916	April-12	Sharp Rees-Stealy	Lankford & Associates
4875 Eastgate Mall	UTC	B	48,000	May-12	L-3 Communications	The Irvine Company
9890 Towne Centre Dr.	UTC	B	31,706	April-12	N/A	The Irvine Company

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.

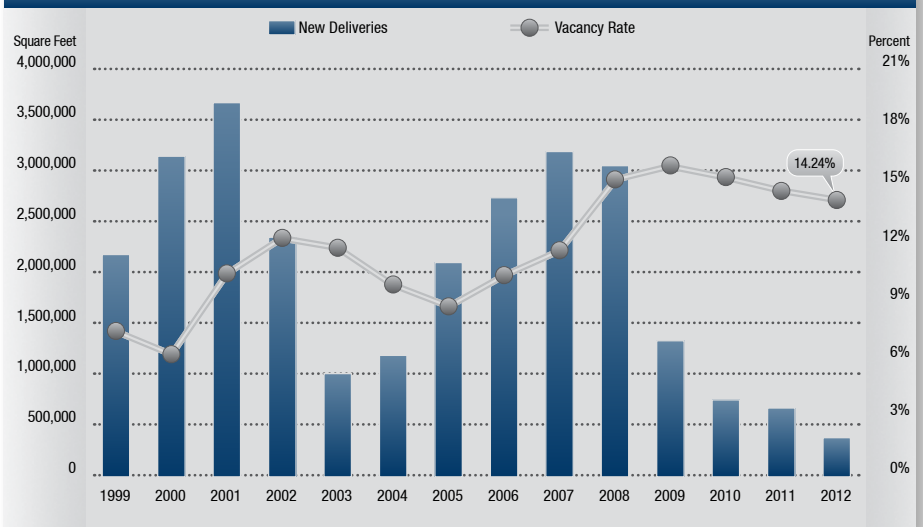
CLASS B

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.

ANNUAL OFFICE NEW DELIVERIES VS. VACANCY RATE



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