

Office Market Report

Compared to the Previous Quarter:

Vacancy

DOWN

Net Absorption

POSITIVE

Lease Rates

FLAT

Transactions

DOWN

Deliveries

UP

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Prepared by:

Jerry J. Holdner, Jr. — Lic.#01145748
Vice President of Market Research
e-mail: jholdner@voitco.com

Joshua Brant
Market Research Analyst
e-mail: jbrant@voitco.com

VOIT Real Estate Services — Lic.#01333376

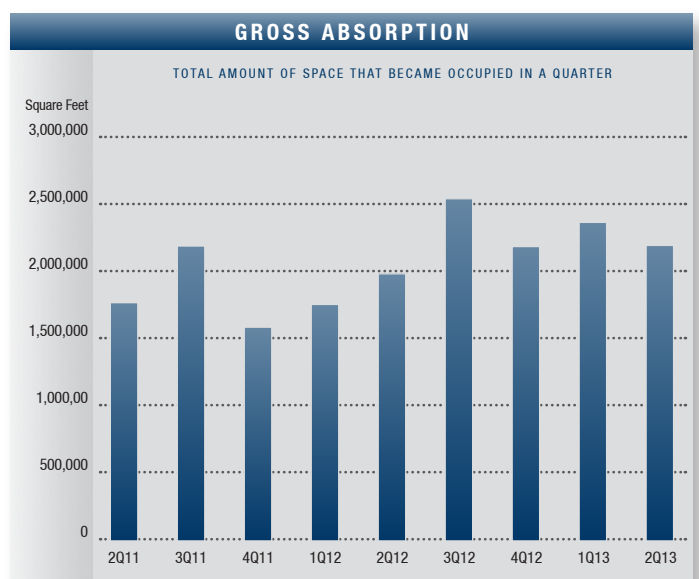
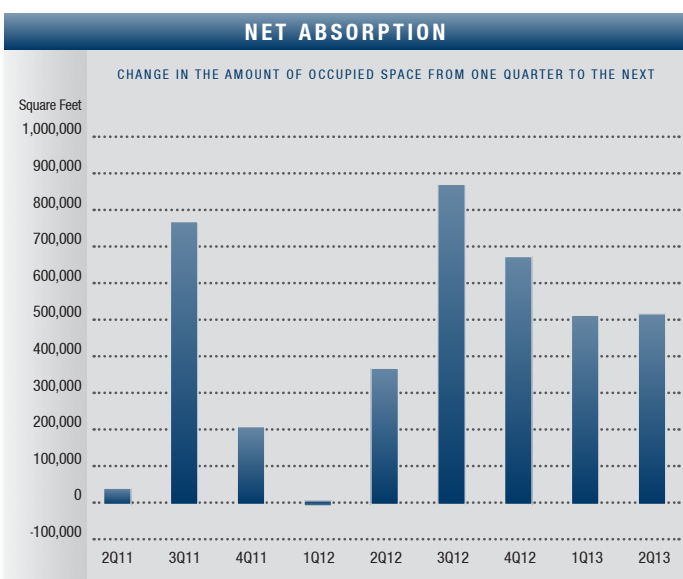
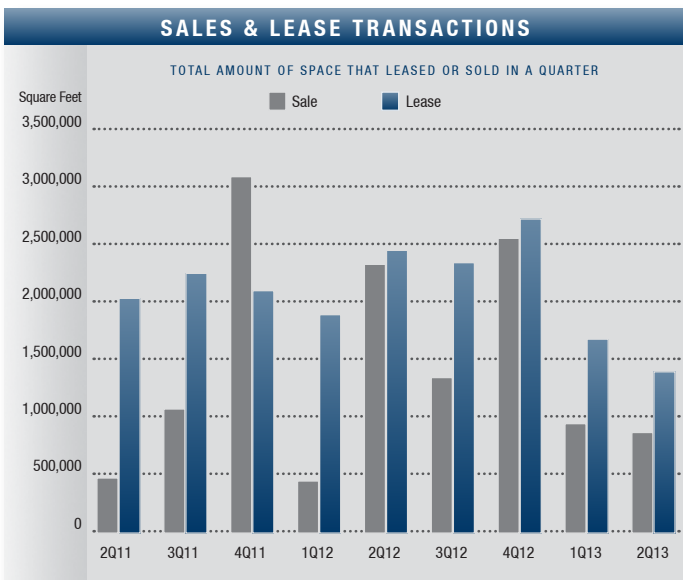
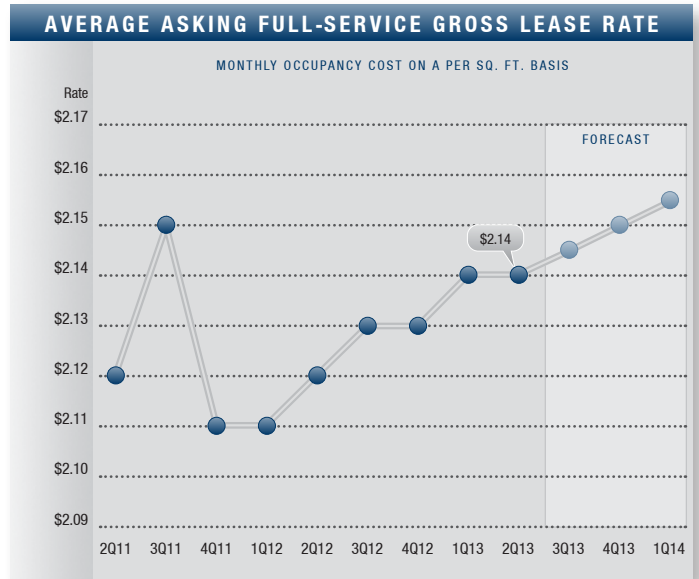
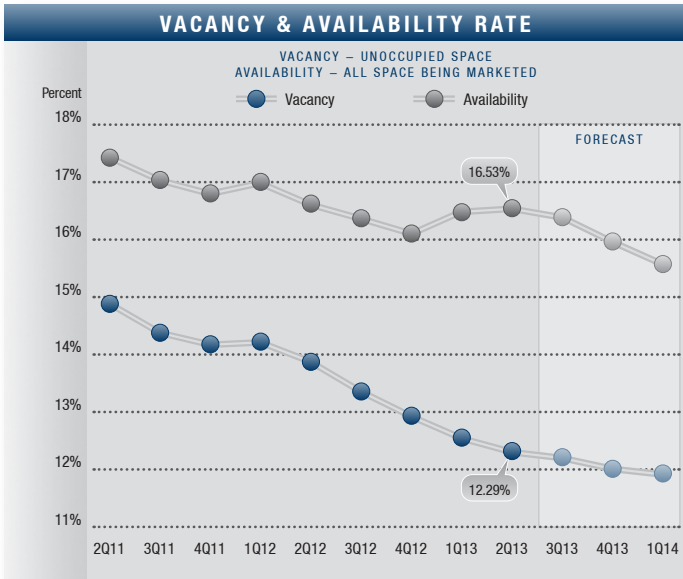
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Market Highlights

- Recovering** - The second quarter continued the trends of stabilized lease rates, positive absorption, and a decreasing vacancy rate for the San Diego office market. These indicators have been generally moving in this direction since the beginning of 2010, despite a couple bumps along the way. This sustained improvement points to a market making strides towards recovery.
- Absorption** - The San Diego office market posted 510,192 square feet of positive net absorption in the first quarter — the fifth consecutive quarter of positive net absorption.
- Transaction Activity** - Sale and lease transactions totaled 2.2 million square feet in the second quarter, not far off from the 2.6 million square feet transacted in the first quarter. 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 6.7% in May 2013, down from a revised 7.0% in April 2013 and below the year-ago estimate of 8.8%. This compares with an unadjusted unemployment rate of 8.1% for California and 7.3% for the nation during the same period. According to the State of California Employment Development Department, San Diego County gained 20,300 payroll jobs from May 2012 to May 2013 — including 5,600 in professional and business services and 4,800 each from educational and health services and leisure and hospitality. Construction and manufacturing were the only employment sectors to post year-over year job losses, at 400 and 100 net jobs lost, respectively.
- Overall** - The economic recovery has not been overwhelming to this point, but overall, the office market has been steadily improving over the last three years. With few new deliveries in the pipeline to apply upward pressure on vacancy, the market is stabilizing. Lease rates have begun rising for Class A property in some central areas. We should see an increase in leasing activity as many short-term deals come up for renewal. Unemployment rates have continued to trend downward since the peak in January 2010. As job creation continues and consumer confidence stabilizes, the office market will continue to recover.
- Vacancy** - Direct/sublease space (unoccupied) finished the first quarter at 12.29%, a decrease from the previous quarter's figure of 12.53%, which was the first drop in office vacancy below 13% since mid-2008, and down nearly 11.5% compared to the same quarter of 2012.
- Construction** - Office deliveries have consistently been around 400,000–700,000 square feet a year over the past three years. This rate of construction is below the historical average and has helped to push vacancy down. The bulk of the current inventory under construction is in the UTC, Sorrento Mesa, and Del Mar Heights submarkets.
- Availability** - Direct/sublease space being marketed was 16.53% at the end of the first quarter, a very slight increase over the 16.49% availability rate of the previous quarter but down compared to 2012's second quarter rate of 16.68%.
- Lease Rates** - The average asking full-service gross (FSG) lease rate per square foot per month in San Diego County was \$2.14 for the second quarter, unchanged from the first quarter, and up one cent from the fourth quarter of 2012. The record high rate of \$2.76 was established in the first and second quarters of 2008. Class A rates for the county averaged \$2.52 FSG.

OFFICE MARKET OVERVIEW

	2Q13	1Q13	2Q12	% of Change vs. 2Q12
Total Vacancy Rate	12.29%	12.53%	13.88%	(11.46%)
Availability Rate	16.53%	16.49%	16.68%	(0.90%)
Average Asking Lease Rate	\$2.14	\$2.14	\$2.12	0.94%
Sale & Lease Transactions	2,231,754	2,595,830	4,752,578	(53.04%)
Gross Absorption	2,187,305	2,354,356	1,971,331	10.96%
Net Absorption	510,192	509,474	365,852	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 2Q2013	Square Feet Available	Availability Rate 2Q2013	Average Asking Lease Rate	Net Absorption 2Q2013	Net Absorption 2013	Gross Absorption 2Q2013	Gross Absorption 2013
Central													
Downtown	137	12,981,506	0	976,354	1,990,785	15.34%	2,761,817	21.28%	\$2.17	90,671	146,659	210,576	440,507
Central Total	137	12,981,506	0	976,354	1,990,785	15.34%	2,761,817	21.28%	\$2.17	90,671	146,659	210,576	440,507
Central Suburban													
City Heights/University	28	1,024,375	0	0	108,072	10.55%	126,649	12.36%	\$1.72	2,505	924	31,147	38,701
Coronado	6	124,741	0	0	0	0.00%	5,636	4.52%	\$0.00	0	3,100	0	3,100
Kearny Mesa	238	10,641,648	0	193,000	1,194,381	11.22%	1,720,798	16.17%	\$1.75	(94,409)	(149,940)	181,823	338,206
Mission Gorge	26	603,823	0	0	53,626	8.88%	53,626	8.88%	\$1.13	(2,562)	1,916	4,387	11,332
Mission Valley	126	6,963,313	0	285,830	824,548	11.84%	883,165	12.68%	\$1.86	61,190	63,228	235,484	395,026
Old Town/Point Loma	77	2,458,500	0	0	201,194	8.18%	340,135	13.84%	\$0.00	(18,449)	(12,234)	23,824	63,460
Park East	9	176,637	0	0	7,562	4.28%	7,562	4.28%	\$0.00	5,196	11,456	5,196	11,456
Rose Canyon/Morena	57	1,283,014	0	11,160	85,968	6.70%	97,854	7.63%	\$1.56	(8,011)	30,531	29,460	72,830
Uptown/Hillcrest	105	2,666,176	0	72,514	209,850	7.87%	238,478	8.94%	\$2.40	(11,793)	(20,326)	18,495	36,226
Central Suburban Total	672	25,942,227	0	562,504	2,685,201	10.35%	3,473,903	13.39%	\$1.75	(66,333)	(71,345)	529,816	970,337
Highway 78 Corridor													
Oceanside	57	1,270,426	0	309,832	203,739	16.04%	229,128	18.04%	\$1.81	61,575	64,714	82,288	100,014
San Marcos	38	1,357,058	0	1,487,970	225,606	16.62%	224,429	16.54%	\$0.00	13,415	3,895	18,578	38,650
Vista	49	1,167,954	0	212,350	191,345	16.38%	252,588	21.63%	\$1.47	(1,412)	5,276	9,001	19,521
Highway 78 Corridor Total	144	3,795,438	0	2,010,152	620,690	16.35%	706,145	18.61%	\$1.47	73,578	73,885	109,867	158,185
I-15 Corridor													
Escondido	91	1,913,330	0	43,107	337,887	17.66%	315,304	16.48%	\$1.69	(12,077)	(12,164)	48,844	74,159
Poway	28	1,256,659	0	650,570	86,424	6.88%	91,253	7.26%	\$1.42	1,435	4,356	10,214	27,486
Rancho Bernardo	108	6,573,462	0	1,136,675	647,920	9.86%	830,575	12.64%	\$2.33	27,677	60,207	71,684	204,543
Scripps Ranch	50	2,704,815	0	377,000	595,391	22.01%	712,953	26.36%	\$2.06	89,768	100,323	157,369	183,513
I-15 Corridor Total	277	12,448,266	0	2,207,352	1,667,622	13.40%	1,950,085	15.67%	\$1.97	106,803	152,722	288,111	489,701
North City													
Governor Park	19	867,993	0	0	112,438	12.95%	138,197	15.92%	\$2.25	16,367	(32,080)	17,382	49,702
La Jolla	56	1,709,467	0	0	208,235	12.18%	240,835	14.09%	\$2.71	11,170	6,281	26,287	76,386
Miramar	38	1,635,185	0	0	313,305	19.16%	344,867	21.09%	\$1.53	10,173	(38,090)	15,269	55,505
Sorrento Mesa	121	9,434,901	250,000	1,671,029	728,648	7.72%	1,214,701	12.87%	\$2.74	227,670	372,439	370,792	629,292
Sorrento Valley	26	798,299	0	0	123,648	15.49%	153,900	19.28%	\$1.99	(5,463)	(45,125)	30,481	53,866
Torrey Pines	44	2,868,587	0	0	100,415	3.50%	320,125	11.16%	\$3.75	(9,295)	13,924	493	61,944
UTC Center	83	7,679,280	414,575	428,684	943,231	12.28%	2,036,923	26.52%	\$3.10	(63,094)	12,606	110,446	378,227
North City Total	387	24,993,712	664,575	2,099,713	2,529,920	10.12%	4,449,548	17.80%	\$2.95	187,528	289,955	571,150	1,304,922
North County													
Carlsbad	152	5,927,911	0	492,000	1,140,155	19.23%	1,250,806	21.10%	\$1.46	(7,022)	104,871	143,284	392,153
Del Mar Heights/Carmel Valley	65	4,288,045	70,000	598,611	619,500	14.45%	822,121	19.17%	\$3.90	50,795	108,645	113,376	307,247
North Beach Cities	111	2,477,157	34,000	77,120	180,432	7.28%	232,120	9.37%	\$2.95	11,816	14,657	71,572	120,208
North County Total	328	12,693,113	104,000	1,167,731	1,940,087	15.28%	2,305,047	18.16%	\$3.09	55,589	228,173	328,232	819,608
South/Southeast Corridor													
Chula Vista	90	2,788,340	0	265,002	340,929	12.23%	385,876	13.84%	\$2.12	46,568	98,563	98,278	165,806
East County	157	3,811,387	0	194,200	290,012	7.61%	320,100	8.40%	\$1.55	24,298	47,732	51,275	125,496
National City	15	541,398	0	0	176,692	32.64%	156,692	28.94%	\$0.00	0	56,430	0	60,650
Otay Mesa	14	338,316	0	0	33,932	10.03%	33,932	10.03%	\$1.34	(4,330)	(1,928)	0	3,449
Southeast San Diego	10	426,932	0	0	107,959	25.29%	107,959	25.29%	\$0.00	(4,180)	(1,180)	0	3,000
South/Southeast Total	286	7,906,373	0	459,202	949,524	12.01%	1,004,559	12.71%	\$1.81	62,356	199,617	149,553	358,401
Class A	252	31,550,738	734,575	6,644,358	3,570,705	11.32%	4,953,120	15.70%	\$2.52	277,790	289,683	731,073	1,294,630
Class B	1,214	52,288,528	34,000	2,838,650	7,196,965	13.76%	9,756,130	18.66%	\$1.92	157,972	577,224	1,170,855	2,688,881
Class C	765	16,921,369	0	0	1,616,159	9.55%	1,941,854	11.48%	\$1.54	74,430	152,759	285,377	558,150
San Diego County Total	2,231	100,760,635	768,575	9,483,008	12,383,829	12.29%	16,651,104	16.53%	\$2.14	510,192	1,019,666	2,187,305	4,541,661

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
5740-5770 Fleet St.	Carlsbad	B	179,194	\$229.76	BBL, Inc.	Regent Properties, Inc.
9710 & 9740 Scranton Rd.	Sorrento Mesa	B	116,825	\$249.95	Cornerstone Real Estate Advisers	Cruzani/Monroe
700-750 Windy Pt.	San Marcos	B	78,643	\$368.76	STORE Capital	Sawtooth Development Group
5575-5675 Ruffin Rd.	Kearny Mesa	B	124,712	\$169.99	Brookwood Four Points Investors, LLC	Menlo Equities
445 Marine View Ave.	North Beach Cities	B	47,543	\$296.57	Hankey Investment Company LP	Jamison Services, Inc.

Lease Transactions

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
9970 Carroll Canyon Rd.	Scripps Ranch	B	81,881	May-13	PETCO	(Sublease)
1615 Murray Canyon Rd.	Mission Valley	A	51,252	May-13	Liberty Mutual	Commonwealth Partners
9620 Towne Centre Dr.	UTC	B	26,897	April-13	N/A	The Irvine Company
9275 Sky Park Ct. – Renewal	Kearny Mesa	A	25,085	June-13	UnionBank	Arden Realty, Inc.
2375 Northside Dr.	Mission Valley	B	23,980	May-13	N/A	Kilroy Realty Corporation

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.

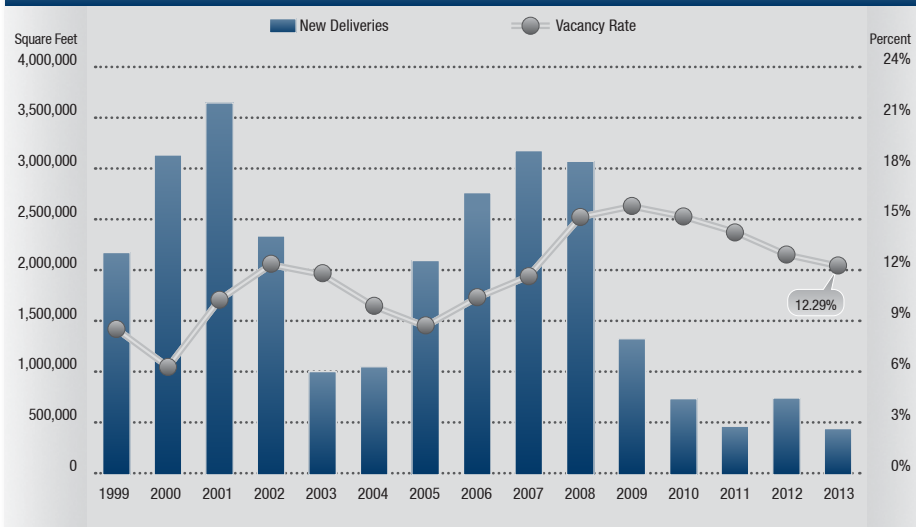
CLASS B

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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