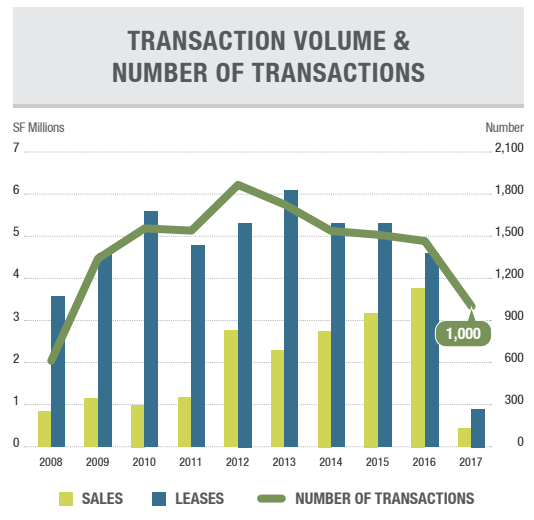
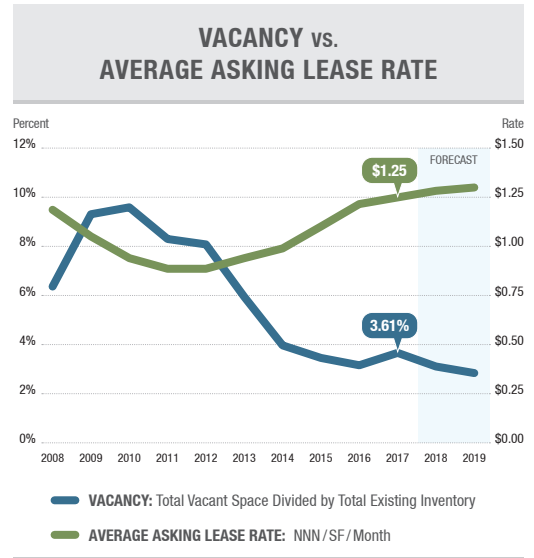


RENTS INCREASING BUT SO IS VACANCY. The thriving Orange County economy has kept the market for R&D/Flex space stable. The market has been exposed to somewhat unique circumstances — stagnant to negative net absorption but a slight increase in rental rates over the past quarter and versus the same time last year. One of the main reasons rents haven't gone down in response to the rise in vacancies is that an increasing portion of the market is made up of conversions of an aging R&D/Flex building/project into campus style or creative office space.

VACANCY. In the second quarter, the Orange County R&D/Flex market saw vacancy levels increase slightly as the overall vacancy rate market-wide reported was 3.61%, up from the 3.54% we saw in the first quarter of 2017, showing an increase of 6.49% when compared with the same quarter last year (3.39%). The lack of available/functional industrial R&D/Flex space is the main driver of leasing activity sluggishness.

LEASE RATES. The average asking lease rate in the R&D/Flex sector for all Orange County was \$1.25 NNN per square foot per month, a four cent (\$0.04) per square foot increase from last quarter and a nine cent (\$0.09) per square foot increase from a year ago (7.76% annual increase). Tenant demand remains consistent and with interest rates on the rise, purchasing is becoming less attractive to many business owners, so we can expect even more upward pressure on lease rates throughout the balance of 2017.

TRANSACTION ACTIVITY. Activity volume continued to be slow-moving, much like the previous quarter. The overall lack of available inventory has continued to take its toll on transaction volume (sales and leases) as gross activity dropped in the second quarter to 941,870 square feet, down from 1.88 million square feet in the previous quarter. Highlights include The Irvine Company's lease of 59,199 square foot lease to Blockage Medical at 29 Parker in Irvine Spectrum, Sparton Corporation leasing 32,933 square feet of at 2802 Kelvin Avenue in Irvine from The Irvine Company, and MBW, Inc. leasing 24,016 square feet at 1732 Reynolds Avenue in Irvine from Ray Taylor Trust.



Market Statistics

	Change Over Last Quarter	2Q 2017	1Q 2017	2Q 2016	% Change Over Last Year
Vacancy Rate	▲ UP	3.61%	3.54%	3.39%	6.49%
Availability Rate	▲ UP	5.27%	5.12%	4.46%	18.16%
Average Asking Lease Rate	▲ UP	\$1.25	\$1.21	\$1.16	7.76%
Sale & Lease Transactions	▼ DOWN	941,870	1,886,980	1,879,838	-49.90%
Gross Absorption	▲ UP	1,012,268	717,549	1,422,944	-28.86%
Net Absorption	▼ NEGATIVE	(46,037)	(230,871)	372,976	N/A

LEASE RATES. Anticipate asking rents to modestly increase by 1–2% to reach a level of \$1.27 per square foot by the end of 2017.

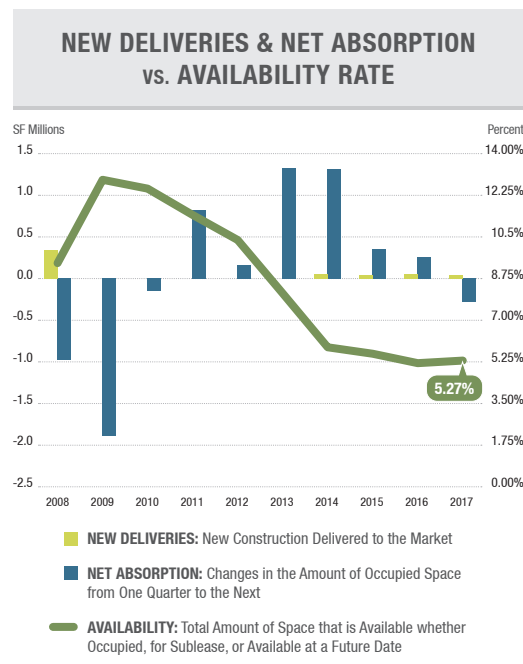
VACANCY. With limited new product coming online and tenants electing to recommit or to renew in larger blocks of space, expect vacancy rates to remain at approximately 3% into 2018.

OVERALL. With an improving economic and employment picture slowly stimulating the market, the Orange County area created 3,800 jobs between May 2016 and May 2017, an annual increase of 0.2%. With no new deliveries in the pipeline to apply upward pressure on vacancy, the market should continue to be relatively stable. We should also see a slight increase in leasing activity as many short-term deals come up for renewal in 2017 and some of these companies have a need to expand. As long as unemployment rates continue to drop and consumer confidence remains relatively stable, the R&D market will move forward steadily.

CONSTRUCTION. With the price of land now above previous record highs in most markets, expect developers to be conservative and to build more alternative (lucrative) uses in the short term. There was no R&D/Flex space under construction in Orange County in the second quarter of 2017. The shrinking availability of land, limited opportunities for financing and rising construction costs have led to a lack of projects being developed. With (limited) infill parcels now approaching \$50 per square foot in some cases, we do not expect any significant R&D/Flex construction in the coming quarters.

ABSORPTION. The Orange County R&D/Flex market continued to experience an absorption slowdown in the second quarter, as deal velocity was stagnant relative to previous quarters. The Orange County submarket reported negative absorption of approximately 46,037 square feet. It hit hardest in the West County (negative 47,159 square feet) and Airport Area (negative 28,128 square feet). As mentioned, the big hurdle in the market is a lack of viable choices to fuel activity, so many companies are opting for traditional industrial space or “making do” with what they currently have.

AVAILABILITY. Direct/sublease space being marketed came in at 5.27% for the second quarter of 2017, a 15 basis point increase from the previous quarter and an increase of 18.16% from second quarter 2016’s rate of 4.46%. Quality available space is difficult to find in some size ranges creating a flight to alternative type space for many tenants.



Significant Transactions

Sales

Property Address	Submarket	Square Feet	Sale Price	Buyer	Seller
9950 Jeronimo Rd.	Irvine Spectrum	262,463	\$56,167,082	Karma Automotive, LLC	Bixby Land Company
1250 N. Tustin Ave.	Anaheim	84,928	\$19,808,500	Doyle Properties, LLC	The Blackstone Group, LP
5037 E. Hunter Ave.	Anaheim	81,836	\$12,215,000	Glen F. & Barbara A. Ceiley Tr	Makena Hunter, Inc.
1620 Sunflower Ave.	Costa Mesa	37,477	\$8,435,000	Meridian Link, Inc.	TKBL, LLC
991 Calle Amanecer	San Clemente	28,075	\$5,699,225	Del Boca Vista Phase II Invest	Teemu, LLC

Leases

* Voit Real Estate Services Deal

Property Address	Submarket	Square Feet	Transaction Date	Tenant	Owner
29 Parker	Irvine Spectrum	59,199	Apr-2017	Blockage Medical	The Irvine Company
2802 Kelvin Ave.	Irvine	32,933	May-2017	Sparton Corporation	The Irvine Company
1732 Reynolds Ave.	Irvine	24,016	Apr-2017	MBW, Inc.	Ray Taylor Trust
23811 Via Fabricante	Mission Viejo	18,783	May-2017	O'Reilly Auto Parts	RREEF
8850–8900 Research Dr.	Irvine Spectrum	14,773	May-2017	Hibino, Inc.	525 Trust*

	INVENTORY				VACANCY & LEASE RATES				ABSORPTION				
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U/C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 2Q2017	Square Feet Available	Availability Rate 2Q2017	Average Asking Lease Rate	Net Absorption 2Q2017	Net Absorption 2017	Gross Absorption 2Q2017	Gross Absorption 2017
Airport Area													
Costa Mesa	177	4,291,404	0	0	146,291	3.41%	354,601	8.26%	\$1.06	(15,644)	10,784	63,214	152,853
Fountain Valley	50	1,426,073	0	0	9,593	0.67%	8,983	0.63%	\$0.95	3,730	(914)	15,560	27,112
Irvine	249	6,220,428	0	0	158,507	2.55%	381,532	6.13%	\$1.24	52,507	(20,055)	122,863	201,210
Newport Beach	24	618,441	0	0	13,982	2.26%	13,982	2.26%	\$1.23	(3,552)	1,591	3,358	15,101
Santa Ana	194	5,068,141	0	0	261,535	5.16%	448,775	8.85%	\$1.19	(72,788)	(103,375)	69,030	117,939
Tustin	92	3,126,539	0	0	232,166	7.43%	273,613	8.75%	\$1.27	7,619	(14,844)	46,282	85,513
Airport Area Total	786	20,751,026	0	0	822,074	3.96%	1,481,486	7.14%	\$1.19	(28,128)	(126,813)	320,307	599,728
North County													
Anaheim	191	5,419,107	0	0	235,307	4.34%	195,689	3.61%	\$1.06	(3,259)	(47,826)	71,644	115,916
Brea	52	1,506,420	0	0	124,063	8.24%	163,386	10.85%	\$1.26	10,528	7,050	23,863	43,658
Buena Park	31	983,704	0	0	16,980	1.73%	16,980	1.73%	\$0.00	5,580	20,978	9,870	23,119
Fullerton	47	1,811,683	0	0	34,449	1.90%	37,309	2.06%	\$0.00	756	(11,095)	22,297	30,857
La Habra	10	187,013	0	0	2,108	1.13%	1,000	0.53%	\$0.00	(1,000)	(1,000)	1,108	1,108
Orange	104	2,323,790	0	0	16,763	0.72%	66,732	2.87%	\$1.50	6,858	6,664	15,050	34,904
Placentia	27	676,082	0	0	44,740	6.62%	39,887	5.90%	\$0.76	(15,427)	(15,692)	6,060	11,700
Yorba Linda	53	1,397,044	0	0	58,285	4.17%	59,629	4.27%	\$0.80	(9,570)	(8,693)	41,289	80,257
North County Total	515	14,304,843	0	0	532,695	3.72%	580,612	4.06%	\$1.01	(5,534)	(49,614)	191,181	341,519
South County													
Aliso Viejo	45	1,104,753	0	0	17,382	1.57%	20,557	1.86%	\$1.30	2,828	6,570	5,075	12,960
Foothill Ranch	7	162,895	0	0	0	0.00%	1,718	1.05%	\$0.00	0	0	0	0
Irvine Spectrum	302	10,403,856	0	0	477,010	4.58%	698,477	6.71%	\$1.41	990	(53,269)	180,507	265,017
Laguna Hills	55	1,279,039	0	0	37,375	2.92%	67,065	5.24%	\$1.33	(10,207)	(22,570)	24,438	38,550
Laguna Niguel	21	498,678	0	0	1,717	0.34%	3,706	0.74%	\$1.55	12,000	12,340	12,000	12,340
Lake Forest	62	1,401,310	0	0	50,485	3.60%	49,317	3.52%	\$1.21	18,859	(10,239)	47,364	66,443
Mission Viejo	36	919,124	0	0	34,821	3.79%	16,038	1.74%	\$1.14	(9,803)	(11,082)	23,897	31,677
Rancho Santa Margarita	44	1,495,300	0	0	5,484	0.37%	22,904	1.53%	\$1.22	5,247	6,742	5,247	18,758
San Clemente	57	1,363,669	0	0	7,018	0.51%	78,072	5.73%	\$1.22	18,024	50,562	51,010	110,338
San Juan Capistrano	45	917,665	0	0	28,990	3.16%	36,046	3.93%	\$1.29	(3,154)	(2,708)	19,787	24,268
South County Total	674	19,546,289	0	0	660,282	3.38%	993,900	5.08%	\$1.37	34,784	(23,654)	369,325	580,351
West County													
Cypress	56	2,646,864	0	0	89,943	3.40%	106,601	4.03%	\$1.00	30,256	(5,192)	48,917	58,442
Garden Grove	71	1,824,277	0	0	42,344	2.32%	37,191	2.04%	\$0.85	8,996	(4,734)	41,508	62,908
Huntington Beach	132	3,055,908	0	0	123,638	4.05%	125,791	4.12%	\$0.78	(90,029)	(70,036)	31,678	71,267
La Palma	1	85,000	0	0	0	0.00%	0	0.00%	\$0.00	0	0	0	0
Los Alamitos	41	913,587	0	0	12,355	1.35%	15,896	1.74%	\$1.20	5,678	8,113	8,532	29,847
Stanton	6	122,189	0	0	0	0.00%	3,264	2.67%	\$0.00	0	0	0	0
Westminster	19	502,745	0	0	15,480	3.08%	17,480	3.48%	\$0.00	(2,060)	(4,978)	820	820
West County Total	326	9,150,570	0	0	283,760	3.10%	306,223	3.35%	\$0.89	(47,159)	(76,827)	131,455	223,284
Orange County Total	2,301	63,752,728	0	0	2,298,811	3.61%	3,362,221	5.27%	\$1.25	(46,037)	(276,908)	1,012,268	1,744,882
Airport Area													
10,000-24,999	528	8,476,388	0	0	309,390	3.65%	481,379	5.68%	\$1.23	(4,752)	(62,068)	176,546	353,222
25,000-49,999	190	6,382,150	0	0	328,940	5.15%	443,990	6.96%	\$1.37	17,590	(8,025)	119,847	204,744
50,000-99,999	52	3,481,385	0	0	183,744	5.28%	381,537	10.96%	\$0.99	(40,966)	(56,720)	23,914	41,762
100,000 Plus	16	2,411,103	0	0	0	0.00%	174,580	7.24%	\$0.00	0	0	0	0
North County													
10,000-24,999	334	5,357,517	0	0	131,109	2.45%	220,785	4.12%	\$1.09	10,944	32,561	97,246	192,777
25,000-49,999	136	4,515,566	0	0	151,422	3.35%	235,596	5.22%	\$0.83	(13,166)	(41,507)	81,295	108,370
50,000-99,999	30	1,976,214	0	0	136,328	6.90%	22,810	1.15%	\$1.10	(9,287)	(28,252)	6,664	34,396
100,000 Plus	15	2,455,546	0	0	113,836	4.64%	101,421	4.13%	\$0.00	5,975	(12,416)	5,976	5,976
South County													
10,000-24,999	413	6,905,780	0	0	267,367	3.87%	369,843	5.36%	\$1.36	62,444	(33,261)	187,854	267,881
25,000-49,999	193	6,477,284	0	0	308,085	4.76%	486,778	7.52%	\$1.41	(67,531)	(27,698)	135,034	257,518
50,000-99,999	55	3,663,590	0	0	84,830	2.32%	137,279	3.75%	\$1.20	39,871	37,305	46,437	54,952
100,000 Plus	13	2,499,635	0	0	0	0.00%	0	0.00%	\$0.00	0	0	0	0
West County													
10,000-24,999	223	3,568,141	0	0	114,982	3.22%	125,849	3.53%	\$0.96	(15,021)	(5,356)	55,545	116,721
25,000-49,999	68	2,325,217	0	0	80,730	3.47%	92,326	3.97%	\$1.02	19,776	(14,367)	63,616	92,669
50,000-99,999	30	2,068,376	0	0	61,048	2.95%	61,048	2.95%	\$0.80	(51,914)	(57,104)	12,294	13,894
100,000 Plus	5	1,188,836	0	0	27,000	2.27%	27,000	2.27%	\$0.00	0	0	0	0
Orange County													
10,000-24,999	1,498	24,307,826	0	0	822,848	3.39%	1,197,856	4.93%	\$1.28	53,615	(68,124)	517,191	930,601
25,000-49,999	587	19,700,217	0	0	869,177	4.41%	1,258,690	6.39%	\$1.32	(43,331)	(91,597)	399,792	663,301
50,000-99,999	167	11,189,565	0	0	465,950	4.16%	602,674	5.39%	\$1.02	(62,296)	(104,771)	89,309	145,004
100,000 Plus	49	8,555,120	0	0	140,836	1.65%	303,001	3.54%	\$0.00	5,975	(12,416)	5,976	5,976
Orange County Total	2,301	63,752,728	0	0	2,298,811	3.61%	3,362,221	5.27%	\$1.25	(46,037)	(276,908)	1,012,268	1,744,882

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



How to Win

by **Eric Smith**

SENIOR ASSOCIATE, ANAHEIM

Everybody wants to win. Win their co-ed softball game, win in their office, win in life... and win in real estate. So, how do you win in a 2.32% vacant market? Said another way, how do you win in basically the tightest industrial real estate market on record? Not so easy of a win, now is it?

A win may be hard to recognize in this market. As mentioned earlier in this report, a lot of tenants may be faced with an uncomfortable and almost unfathomable new lease rate. For example, a lease rate signed in the early recovery era of 2012 has probably seen a 30–40% increase. For example, a 20,000 square foot industrial lease at \$0.60 NNN per square foot per month most likely has just become a \$0.84 NNN per square foot per month lease in the current market. That is a \$4,800 monthly difference. On any scale, these numbers can be frustrating for tenants and ecstasy for landlords. Hence, let's establish what a win actually is.

Winning is prioritizing, strategizing, starting early and using professionals. Winning is calmly leasing the building that is in the right location, with the right power, right clearance, loading and port access. Winning is buying a building to control your own real estate and capitalizing on still low interest rates. Winning is leasing to a credit tenant with a clean use. Winning may be paying the asking rate...

Here are some winning strategies you should consider using:

Accept Sticker Shock – everyone is facing 30–40% rent increases. Before you tell your landlord where to stuff their lease, look around. Making a sound business decision based on growth numbers, ROI and ROE of being in the right building will probably assuage the increased rent.

Buying vs Leasing – buying is always an option. Even with sales prices increasing as much as 26% from the first quarter of 2016, in many circumstances owning the real estate and taking into consideration after-tax benefits is less expensive than leasing.

Consider Moving East – to the Inland Empire. Perhaps Corona, Ontario, Chino or Inland Empire West. There are only 2 buildings (totaling 387,835 square feet) that are under construction in the entire Orange County industrial market.

Consider Renewing Early – blend and extend to get a sense of certainty now. You can always reach out to your landlord early to see about renewing now and securing your rental rate.

Shoot for a Short-Term Lease – if you are a tenant, aim for a short-term lease of 2–4 years so you can catch a potential market correction.

Remember, the pendulum will swing back some day. Be strategic, be informed and learn how to recognize a win.

**Please Contact Us
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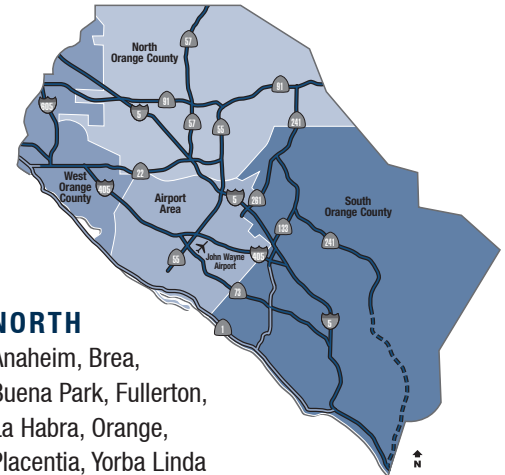
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Product Type

R&D OR MID-TECH

30% to 74.9% improved with drop ceiling, minimum parking ratio of 3 to 1, minimum 50% of exterior glassline, dock and/or ground level loading.

Submarkets



NORTH

Anaheim, Brea, Buena Park, Fullerton, La Habra, Orange, Placentia, Yorba Linda

WEST

Cypress, Garden Grove, Huntington Beach, La Palma, Los Alamitos, Stanton, Westminster

AIRPORT

Costa Mesa, Fountain Valley, Irvine, Newport Beach, Santa Ana, Tustin

SOUTH

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