

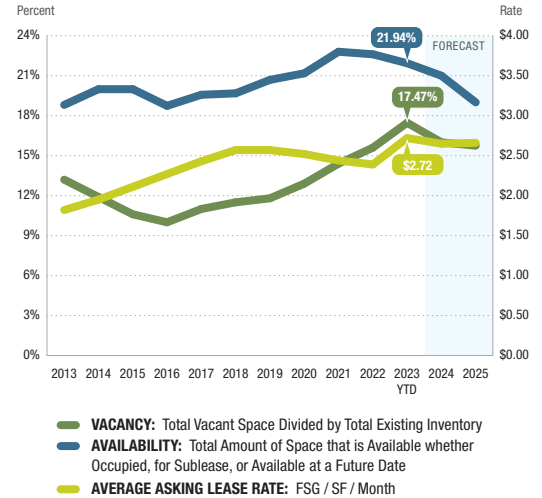
OVERVIEW. The Orange County office market continued to struggle in Q3, but the rate of decline in major metrics slowed. The shift in workplace dynamics has hit the office sector hard and employers are still having trouble implementing orders for their workers to return to the office on a part-time to full-time basis. That has resulted in downsizing, more short-term renewals and indecision in C-suites and boardrooms regarding how to plan for new facilities. Vacancy moved higher again in Q3, but the availability rate declined. Average asking lease rates inched up. Net absorption remained firmly in negative territory, but the net loss declined for the third straight quarter. Lease and sale activity was flat in terms of square footage, but the number of sales increased. Elevated mortgage interest rates continue to pose a problem for those owners with maturing debt.

VACANCY & AVAILABILITY. The overall vacancy rate increased to 17.47% in Q3, up from 17.04% in Q2 and 15.60% in Q1. Year over year, overall vacancy has increased by 12%, but, as we reported last period, the real story is revealed when vacancy is broken down by building class. Class A vacancy has risen to 22.84% and availability, which includes sublease space and available direct space that is still occupied, has increased to 28.36%. On a positive note for building owners, Class A availability in the Airport Area fell to 28.57% from 30.47% in Q2, and that submarket has 26 MSF of Class A space, more than all other submarkets combined. West County Class A availability remained the highest in the County at 34.19%. Class B and C buildings are faring much better with availability rates of 9.86% and 4.54%, respectively.

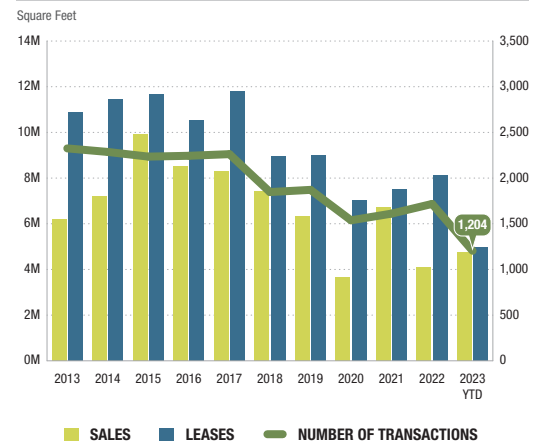
LEASE RATES. The average asking lease rate for all office space across the county increased by \$0.08 in Q3 to \$2.72 PSF, after falling by 2 pennies in Q2. However, as we have been reporting, effective rents are falling, as landlords tend to hold the line on asking rates and offer larger concessions such as free rent and more generous tenant improvement allowances to attract and retain tenants. Consequently, year-over-year asking rates are flat. South County now has the highest asking rate of \$2.91, surpassing the Airport Area by 7 cents. South County includes the Irvine Spectrum submarket where the Irvine Company's signature high-rise buildings are located. Central County still has the lowest overall asking rate at \$2.37 PSF, followed by West County at \$2.40 PSF and North County at \$2.43 PSF.

TRANSACTION ACTIVITY. Lease and sale activity moved slightly higher in Q3, rising from 3,477,010 SF in Q2 to 3,596,260 SF. 355 lease transactions were completed in Q3, down from 440 in Q2. Total square footage leased fell to 1,490,000 SF from 2,233,000 SF in Q2. However, sale transaction activity bounced back to 23 from just 7 in Q2. Total square footage sold nearly doubled to 2,105,000 SF. The impetus for the increase is likely that some owners with maturing debt are choosing to sell in lieu of facing the difficult task of refinancing their loans at high rates with strict underwriting. The largest sale of the quarter was a 553,530 SF Class A project on Bristol Street in Costa Mesa to MGR Real Estate from EQ Office. The largest new lease deal of the quarter was a 116,261 SF lease from Alteryx to Boot Barn at 17100 Laguna Canyon Road in Irvine Spectrum.

VACANCY, AVAILABILITY & AVERAGE ASKING LEASE RATES



TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



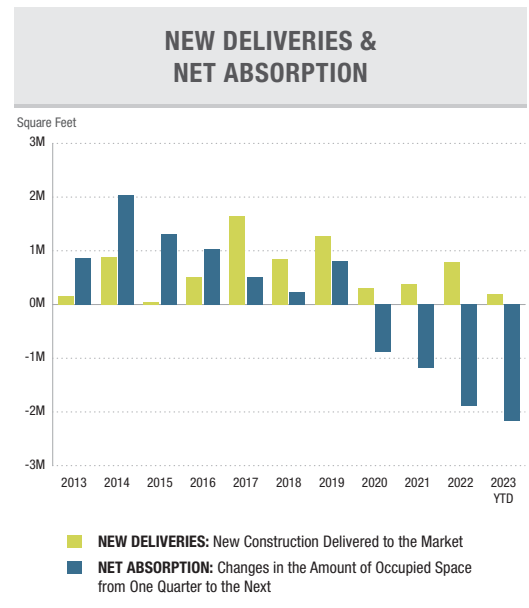
Market Statistics

	Change Over Last Quarter	Q3 2023	Q2 2023	Q3 2022	% Change Over Last Year
Vacancy Rate	▲ UP	17.47%	17.04%	15.60%	11.99%
Availability Rate	▬ FLAT	21.94%	22.61%	20.69%	6.03%
Average Asking Lease Rate	▲ UP	\$2.72	\$2.64	\$2.71	0.37%
Sale & Lease Transactions	▲ UP	3,596,260	3,477,010	2,516,249	42.92%
Gross Absorption	▲ UP	2,159,730	1,805,694	1,989,293	8.57%
Net Absorption	▼ NEGATIVE	(403,741)	(499,618)	(448,508)	N/A

ABSORPTION. Countywide net absorption remained firmly in negative territory, but moderated to 403,741 SF from 499,618 SF in Q2. Year to date, negative net absorption stands at 2,165,647 SF. The Airport Area was the only major submarket to report a net gain for the period, which came in at 232,102 SF. South County posted the biggest loss in occupancy in Q3 at 448,791 SF. West and Central County both posted modest losses, while all cities in North County, except Fullerton, registered lower occupancy as the quarter ended. Persistent negative absorption is putting heavy pressure on landlords to fight to retain existing tenants whose leases are expiring soon. Their problem is compounded by the fact that many tenants are downsizing as they renew leases and are inclined to avoid long-term commitments.

CONSTRUCTION. Thankfully, construction activity has completely stopped and no new projects are scheduled to get underway any time soon. Higher capital costs and soft market conditions make new projects impossible for developers to pencil with the possible exception of The Irvine Company, which has a low land basis and is able to build with cash. The absence of new construction is a bright spot for existing building owners who are struggling with the ongoing challenges associated with hybrid and work-from-home employment models.

EMPLOYMENT. In August 2023, the unemployment rate in Orange County rose to 3.9%, marking an increase from the revised rate of 3.6% in July 2023 and exceeding the year-ago estimate of 3.2%. The government sector added 1,700 jobs, while manufacturing saw an increase of 1,000 jobs. Trade, transportation, and utilities also showed growth, adding 300 jobs, and professional and business services expanded by an additional 200 jobs.



Forecast

The office market will continue to be under stress on several fronts for the foreseeable future. Loan maturity is a looming problem, as any owner who needs to refinance in this environment is faced with much higher debt-service costs. We expect more sales at discounted prices for properties in all building classes that are facing a refinancing event. Uncertainty over how much space is needed and how it should be configured will remain a huge problem for tenants and landlords well into 2024. We are nowhere near a resolution to this problem that was forced on business owners by the pandemic. Expect more downward pressure on lease rates and an increase in concessions to attract and retain tenants.

Significant Transactions

Sales

Property Address	City	Class	Square Feet	Total Price	Buyer	Seller
3090–3150 Bristol St.	Costa Mesa	A	553,530	\$91,500,000	MGR Real Estate	EQ Office
85–101 Enterprise	Aliso Viejo	A	477,451	\$70,000,000	Acore Capital	Old Republic International Corporation
1801 Hughes Dr.	Fullerton	B	405,180	\$76,500,000	Diamond Development Group	Oaktree Capitol Management, L.P.
7711–7777 Center Ave.	Huntington Beach	A	401,820	\$42,000,000	Joe C Wen	Pendulum Property Partners
2050 Main St.	Irvine	A	314,074	\$57,500,000	Greenlaw Partners	Angelo Gordon & Co., L.P.

Leases

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
17100 Laguna Canyon Rd.	Irvine Spectrum	A	116,261	Aug-2023	Boot Barn	Alteryx
3345–3353 Michelson Dr.	Irvine	A	25,911	Aug-2023	Panasonic	LBA Realty
600 Anton Blvd.	Costa Mesa	A	22,466	Sep-2023	Ducommun	CJ Segerstrom & Sons
1900 Main St.	Irvine	A	22,464	Sep-2023	Healthpeak Properties, Inc.	Terrace Tower Group U.S.A.
1 Park Plaza	Irvine	A	18,877	Jul-2023	Am Trust	International Vitamin Corp.

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate Q3 2023	Square Feet Available	Availability Rate Q3 2023	Average Asking Lease Rate	Net Absorption Q3 2023	Net Absorption 2023	Gross Absorption Q3 2023	Gross Absorption 2023
Airport Area													
Costa Mesa	60	6,988,809	0	0	1,442,253	20.64%	1,951,147	27.92%	\$3.07	229,744	(69,353)	170,570	376,343
Irvine	243	24,167,282	0	1,051,438	4,623,689	19.13%	5,772,159	23.88%	\$2.75	76,790	(538,656)	820,830	1,951,418
Newport Beach	106	9,149,987	0	0	1,220,765	13.34%	1,780,784	19.46%	\$3.09	(41,486)	(159,807)	153,288	427,552
Santa Ana	9	2,003,987	0	0	578,332	28.86%	682,933	34.08%	\$2.42	847	(141,558)	151,633	295,619
Tustin	4	418,585	0	0	54,227	12.95%	80,368	19.20%	\$4.70	(33,793)	71,587	0	105,380
Airport Area Total	422	42,728,650	0	1,051,438	7,919,266	18.53%	10,267,391	24.03%	\$2.84	232,102	(837,787)	1,296,321	3,156,312
Central County													
Anaheim	21	1,952,808	0	0	495,632	25.38%	462,347	23.68%	\$2.47	(14,111)	(45,578)	66,721	118,017
Orange	64	6,181,828	0	0	1,135,592	18.37%	1,571,718	25.42%	\$2.30	(49,264)	(152,005)	46,748	249,327
Santa Ana	134	9,571,388	0	0	1,882,037	19.66%	2,290,387	23.93%	\$2.47	48,657	(71,102)	168,901	432,077
Tustin	38	1,981,506	0	0	177,512	8.96%	239,249	12.07%	\$1.72	(23,600)	51,651	22,606	138,017
Central County Total	257	19,687,530	0	0	3,690,773	18.75%	4,563,701	23.18%	\$2.37	(38,318)	(217,034)	304,976	937,438
North County													
Anaheim Hills	61	4,088,439	0	0	448,562	10.97%	481,806	11.78%	\$2.52	5,916	(22,512)	19,105	114,219
Brea	39	3,889,565	0	0	631,117	16.23%	925,625	23.80%	\$2.60	(71,154)	36,850	32,972	173,412
Buena Park	17	1,078,748	0	0	45,597	4.23%	80,484	7.46%	\$2.26	(24,953)	(31,261)	5,411	28,980
Fullerton	16	867,909	0	0	76,179	8.78%	125,271	14.43%	\$2.15	11,829	26,312	15,735	50,916
La Habra	3	115,103	0	0	4,254	3.70%	4,094	3.56%	\$1.72	(1,296)	(2,100)	1,765	5,166
La Palma	7	542,913	0	0	111,002	20.45%	138,505	25.51%	\$0.00	(12,025)	(32,226)	8,340	12,536
Placentia	6	199,881	0	0	28,969	14.49%	41,656	20.84%	\$2.07	(8,215)	(12,574)	623	12,212
Yorba Linda	5	289,383	0	0	22,862	7.90%	24,499	8.47%	\$2.26	(3,612)	(16,002)	1,344	4,630
North County Total	154	11,071,941	0	0	1,368,542	12.36%	1,821,940	16.46%	\$2.43	(103,510)	(53,513)	85,295	402,071
South County													
Aliso Viejo	36	2,641,812	0	0	949,472	35.94%	1,014,318	38.39%	\$2.84	(95,223)	(223,140)	40,536	156,874
Dana Point	3	127,999	0	0	0	0.00%	0	0.00%	\$0.00	0	6,000	0	7,200
Foothill Ranch	8	697,717	0	0	289,323	41.47%	281,775	40.39%	\$2.50	(1,784)	(232,953)	9,433	48,574
Irvine Spectrum	170	13,361,229	0	0	2,086,627	15.62%	2,729,033	20.43%	\$3.12	(366,464)	(316,805)	265,968	712,587
Laguna Beach	4	124,004	0	0	5,644	4.55%	5,644	4.55%	\$3.45	(700)	(3,172)	0	675
Laguna Hills	27	1,301,662	0	465,000	275,489	21.16%	299,204	22.99%	\$2.62	5,441	(9,376)	35,354	104,604
Laguna Niguel	7	395,699	0	0	77,933	19.70%	82,783	20.92%	\$2.47	8,066	(21,854)	8,964	15,681
Lake Forest	41	2,202,710	0	0	419,029	19.02%	431,143	19.57%	\$2.09	(3,595)	(48,470)	25,180	96,029
Mission Viejo	25	1,317,777	0	0	244,008	18.52%	269,622	20.46%	\$2.36	11,035	(5,468)	38,276	65,551
Rancho Santa Margarita	5	212,716	0	0	21,114	9.93%	28,982	13.62%	\$2.40	(1,267)	464	0	8,601
San Clemente	8	411,212	0	0	30,232	7.35%	34,986	8.51%	\$2.00	(4,128)	2,069	0	11,536
San Juan Capistrano	20	971,944	0	0	36,456	3.75%	46,191	4.75%	\$2.73	(172)	(2,484)	8,902	34,898
South County Total	354	23,766,481	0	465,000	4,435,327	18.66%	5,223,681	21.98%	\$2.91	(448,791)	(855,189)	432,613	1,262,810
West County													
Cypress	27	1,904,468	0	0	183,579	9.64%	329,537	17.30%	\$2.43	1,898	(62,098)	7,636	39,281
Fountain Valley	25	1,156,301	0	0	37,959	3.28%	40,005	3.46%	\$2.04	(5,495)	(7,400)	300	16,935
Garden Grove	14	710,490	0	0	74,262	10.45%	71,656	10.09%	\$2.08	(21,039)	(32,095)	15,574	28,892
Huntington Beach	33	1,783,701	0	0	340,289	19.08%	371,983	20.85%	\$1.86	846	(38,372)	9,940	40,379
Los Alamitos	9	472,574	0	0	6,273	1.33%	7,598	1.61%	\$2.28	(1,550)	(488)	0	5,442
Seal Beach	6	452,518	0	0	59,392	13.12%	70,570	15.59%	\$3.44	(1,841)	8,485	780	37,958
Stanton	4	143,361	0	0	38,203	26.65%	34,285	23.92%	\$1.49	92	(34,196)	572	2,757
Westminster	10	414,019	0	0	66,076	15.96%	78,584	18.98%	\$2.32	(18,135)	(35,960)	5,723	25,586
West County Total	128	7,037,432	0	0	806,033	11.45%	1,004,218	14.27%	\$2.40	(45,224)	(202,124)	40,525	197,230
Orange County Total	1,315	104,292,034	0	1,516,438	18,219,941	17.47%	22,880,931	21.94%	\$2.72	(403,741)	(2,165,647)	2,159,730	5,955,861
Airport Area													
Class A	126	25,967,311	0	932,496	5,720,008	22.03%	7,419,373	28.57%	\$3.20	267,923	(475,930)	840,238	2,077,198
Class B	276	15,597,901	0	118,942	2,132,785	13.67%	2,741,781	17.58%	\$2.65	(26,029)	(352,361)	429,835	1,020,943
Class C	20	1,163,438	0	0	66,473	5.71%	106,237	9.13%	\$2.60	(9,792)	(9,496)	26,248	58,171
Central County													
Class A	39	6,843,524	0	0	1,921,474	28.08%	2,241,472	32.75%	\$2.66	(33,505)	(216,136)	122,518	419,098
Class B	177	11,082,264	0	0	1,618,191	14.60%	2,122,273	19.15%	\$2.29	6,998	11,774	161,546	459,621
Class C	41	1,761,742	0	0	151,108	8.58%	199,956	11.35%	\$1.86	(11,811)	(12,672)	20,912	58,719
North County													
Class A	20	2,417,720	0	0	629,119	26.02%	759,847	31.43%	\$2.59	(98,022)	(72,508)	18,361	140,109
Class B	118	8,023,949	0	0	726,984	9.06%	1,049,654	13.08%	\$2.39	(2,805)	27,151	66,009	258,816
Class C	16	630,272	0	0	12,439	1.97%	12,439	1.97%	\$2.04	(2,683)	(8,156)	925	3,146
South County													
Class A	68	8,976,951	0	465,000	1,824,050	20.32%	2,033,760	22.66%	\$3.24	(165,154)	(113,482)	216,897	617,546
Class B	275	14,286,582	0	0	2,576,347	18.03%	3,160,133	22.12%	\$2.77	(280,651)	(725,782)	209,146	631,929
Class C	11	502,948	0	0	34,930	6.95%	29,788	5.92%	\$2.53	(2,986)	(15,925)	6,570	13,335
West County													
Class A	12	1,382,111	0	0	315,829	22.85%	472,568	34.19%	\$2.57	(5,384)	(58,509)	3,096	54,528
Class B	102	5,172,473	0	0	468,304	9.05%	509,750	9.86%	\$2.32	(45,040)	(121,865)	32,229	135,352
Class C	14	482,848	0	0	21,900	4.54%	21,900	4.54%	\$1.56	5,200	(21,750)	5,200	7,350
Orange County													
Class A	265	45,587,617	0	1,397,496	10,410,480	22.84%	12,927,020	28.36%	\$3.02	(34,142)	(936,565)	1,201,110	3,308,479
Class B	948	54,163,169	0	118,942	7,522,611	13.89%	9,583,591	17.69%	\$2.60	(347,527)	(1,161,083)	898,765	2,506,661
Class C	102	4,541,248	0	0	286,850	6.32%	370,320	8.15%	\$2.07	(22,072)	(67,999)	59,855	140,721
Orange County Total	1,315	104,292,034	0	1,516,438	18,219,941	17.47%	22,880,931	21.94%	\$2.72	(403,741)	(2,165,647)	2,159,730	5,955,861

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.



Office Is Still Struggling, But It's Not As Simple As You Might Think

by **Russ Smith**

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A quick Google search yields plenty of pessimistic content regarding the state of the office market. For Orange County, vacancy rates are on the rise, asking rates are in decline, and net absorption is in negative territory. To be frank, the only conclusion we can draw about the overall office market is that it's poised to be challenging for the foreseeable future. For tenants, determining future space requirements will be a difficult process, with many realizing they need less space than they currently occupy. Meanwhile, landlords may face a protracted struggle to fill vacancies, necessitating creative ways to repurpose space instead of straightforward re-leasing. But now that we've addressed the elephant in the office, let's pivot and discuss the significance of context, particularly in avoiding blanket categorizations of the entire office market as either "bad" or "good." The office market has a substantial gray area in between.

When reading articles, blogs, or watching videos about the state of the office market, it's crucial to remember that much of this content focuses on the macro level, with headlines skewed towards larger buildings and the dynamics of major companies. For instance, the news may highlight Elon Musk's mandate for Tesla employees to return to the office, Meta returning significant space to a landlord, or institutional office landlords facing loan defaults on their downtown LA high-rise buildings. Big companies and large buildings garner attention because they generate clicks and views. However, real estate values, lease rates, cap rates, and more are fundamentally influenced by local dynamics, particularly supply and demand.

In today's landscape, tenants generally expect to find attractive deals regardless of space size, condition, or location. Yet, unless you're seeking spaces exceeding 20,000 SF, you might be surprised to learn that demand for high-quality, amenity-rich space remains strong. With larger companies downsizing but aiming to maintain or enhance their space quality, tenants may discover fewer available options than initially expected. In essence, numerous companies vie for the same smaller, high-quality spaces.

It's a similar situation with the values of office buildings. Most of the vacancy, subleases, and negative absorption can be attributed to larger buildings, particularly in the airport area. This circumstance can strain landlords' ability to service debt and potentially lead to a cycle of increasing vacancies, diminishing income, and defaults, especially as debt on larger office assets typically features shorter terms, typically five to seven years to maturity. In contrast, smaller owner-occupied buildings have managed to maintain their values, primarily because buyers typically employ SBA loans or longer-term conventional financing for their purchases and refinancing. Imagine how different the housing market would appear if homeowners held five-year variable rate loans instead of the standard 30-year fixed-rate mortgages. Context remains pivotal, underscoring the importance of having the right advisor by your side the next time you venture into the office space market.

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This survey consists of properties representing both single tenant and multi-tenant buildings. The lease rates are based on a full-service gross basis. The information contained in this report is gathered from sources that are deemed reliable, but no guarantees are made as to its accuracy. This information is for Voit Real Estate Services' use only and cannot legally be reproduced without prior written consent from the management of Voit Real Estate Services.

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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