

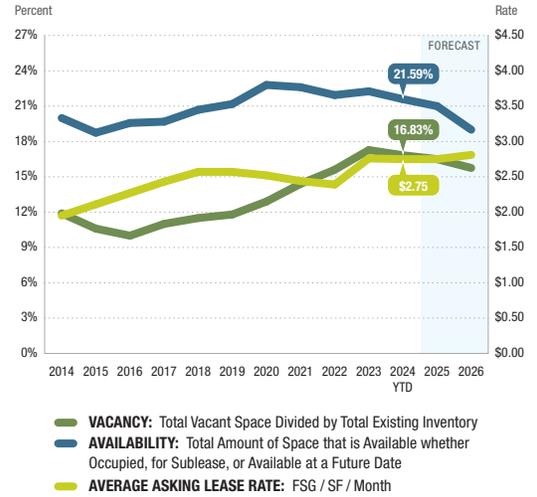
**OVERVIEW.** Despite major challenges, the Orange County office market held its own in Q1 for the second straight quarter, though significant headwinds remain in the forecast. 2023 marked the fourth consecutive year of negative net absorption and that trend continued in the opening quarter of 2024. Vacancy fell slightly again, settling to where it was a year ago, and availability also ticked lower. Lease and sale activity fell again, but gross absorption was up slightly. Average asking lease rates were down, but the true picture in the leasing market only becomes clear after generous tenant concessions are figured in. The shift in workplace dynamics has really taken the office market off course and the uncertainty it caused is not expected to change any time soon. Business owners are still battling with their employees over return-to-work rules and that makes it even more difficult to assess space needs looking ahead. Downsizing is another challenge for landlords, as their renewing tenants are looking to shrink their space footprints. Amenity-rich buildings are getting more attention from business owners looking to secure space that will be more attractive to employees reluctant to return to the office.

**VACANCY & AVAILABILITY.** The overall vacancy rate decreased to 16.83% in Q1 from 17.27% in Q4. Year over year, vacancy has actually decreased by two basis points but the extent of the challenge to landlords becomes more apparent when the market is analyzed by building class. Class A vacancy is up to 22.70%, while availability is up to 28.40%, although both of those metrics moved slightly lower in Q1. Class A vacancy is over 22% in all significant Orange County submarkets. The Airport Area has the largest inventory of Class A space at 25.7 MSF, and 22.08% of that total sat vacant at the end of the quarter. Another 7% is available but still occupied, much of which is large blocks of space offered for sublease, which tends to move more slowly than the smaller size ranges. Vacancy in Class B countywide is just 12.91% and the availability rate is 17.17%. Class B buildings represent roughly half of the county’s 104.3 MSF inventory. Class C vacancy fell under 6% in the quarter, but it represents just 4% of total inventory.

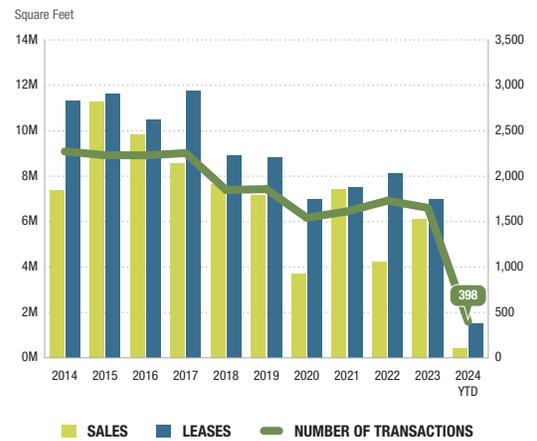
**LEASE RATES.** The average asking lease rate across all building classes countywide moved down a penny to \$2.75 in Q1, but asking rents do not accurately reflect true market conditions. The effective rate, which accounts for concessions offered to tenants, continued to fall because of increases in free rent, tenant improvement allowances and other concessions. Landlords make every effort to maintain their coupon or face rate in their lease documentation, as they believe it better positions their properties for refinancing and eventual disposition.

**TRANSACTION ACTIVITY.** Combined lease and sale activity declined to 1,949,884 SF in Q1 from 2,705,650 SF in Q4 of last year. 393 lease transactions were completed compared to 378 in Q4, but total square leased fell by 150,000 SF. This reflects the concentration of deal-making in the smaller size ranges and a rising number of larger spaces sitting vacant longer.

**VACANCY, AVAILABILITY & AVERAGE ASKING LEASE RATES**



**TRANSACTION VOLUME & NUMBER OF TRANSACTIONS**



Market Statistics

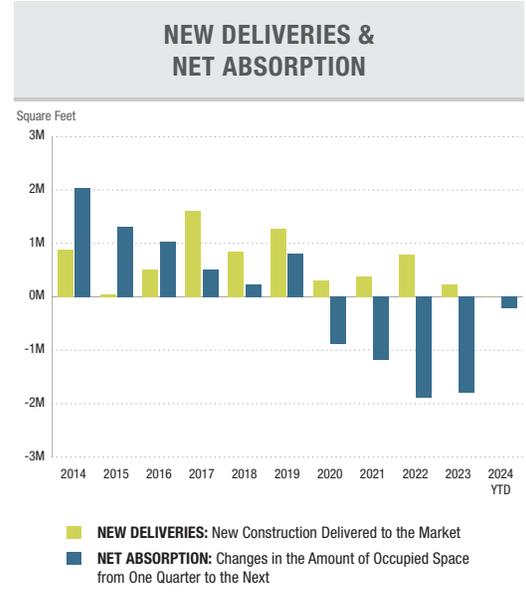
	Change Over Last Quarter	Q1 2024	Q4 2023	Q1 2023	% Change Over Last Year
Vacancy Rate	▼ DOWN	16.83%	17.27%	16.85%	(0.10%)
Availability Rate	▼ DOWN	21.59%	22.26%	22.80%	(5.31%)
Average Asking Lease Rate	▼ DOWN	\$2.75	\$2.76	\$2.66	3.38%
Sale & Lease Transactions	▼ DOWN	1,949,884	2,705,650	2,711,823	(28.10%)
Gross Absorption	▲ UP	2,467,193	2,405,733	1,990,437	23.95%
Net Absorption	▼ NEGATIVE	(207,467)	366,886	(1,262,288)	N/A

Sale transaction count fell from 12 to 5 and total square footage sold declined to 437,597 SF from 1,042,515 SF in the final quarter of 2023.

**ABSORPTION.** Countywide net absorption turned negative again in Q1 after a brief return to positive territory in Q4 of 2023. The office sector is now entering its fifth year of net occupancy loss, which accelerated during the pandemic shutdowns and continue today as workplace dynamics have been slow to return across most office-sector employers. In Q1, a decline in occupancy of 207,467 SF was reported, the bulk of which was in Class B space in the Airport and North County submarkets. South and West County submarkets posted modest gains, while Central County was relatively flat. Projects with the best amenities are faring best across all building classes, as business owners are trying to make in-office work more attractive after years of work-from-home or hybrid engagement.

**CONSTRUCTION.** As we reported in the final quarter of 2023, not a single square foot of office space is under construction in Orange County. With current low levels of leasing activity, this is welcome news for the owners of existing projects in all building classes. The lack of new inventory being added to the speculative base will help keep net absorption from falling further into negative territory and lease rates from declining. However, buildings with functional obsolescence and a lack of amenities are still struggling. Anything in the planning queue will probably stay there, as soft market metrics and the high cost of capital persist.

**EMPLOYMENT.** Orange County’s unemployment rate held steady at 4.2% in February 2024, unchanged from January but higher than 3.4% a year earlier. Information (-1,500 jobs), manufacturing (-1,000), and professional services (-200) were the few sectors contracting year over year.



## Forecast

Problems for the office market will persist. Until business owners figure out how to get all their people back into the office full time, leasing activity will languish. While the COVID-induced spike in vacancy moderated in the last half of 2023, it may continue to increase in 2024 as leases on larger spaces expire and are not renewed. For that reason, we believe vacancy will creep higher throughout the year, which will keep average asking lease rates in the range they are now. However, effective rates will go lower, as more free rent and other concessions will be offered. Property values for office buildings have already taken a big hit and that trend will continue. Several Class A projects in Orange County have already traded at under \$150 per square foot, which is just a fraction of replacement cost. That trend will make it even more difficult for owners facing loan maturity to refinance their properties. Unless their lenders are willing to extend call dates, we could see a significant uptick in loan defaults in 2024.

## Significant Transactions

### Sales

Property Address	City	Class	Square Feet	Total Price	Buyer	Seller
1 MacArthur Pl.	Santa Ana	A	208,257	\$31,050,000	One Macarthur Place, LLC	TPG Angelo Gordon & Co, L.P.
2700 Main St.	Santa Ana	A	120,560	\$18,600,000	Core Development Group	PRES Companies
1835–1915 W. Orangewood Ave - 3 Properties	Orange	B	108,780	\$11,500,000	Orangewood Office Center LLC	Providence Capital Group, Inc.

### Leases

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
3351 Michelson Dr.	Irvine	A	51,629	Jan-2024	Symple Lending LLC	LBA Realty
5 Park Plaza - Sublease	Irvine	A	45,960	Jan-2024	Clear Start Tax	Better Mortgage Corporation
19900 MacArthur Blvd.	Irvine	A	38,717	Feb-2024	Tax Rise, Inc.	Newport Gateway Office LLC
3161 Michelson Dr.	Irvine	A	31,196	Jan-2024	Hyundai Capital America	Manulife Financial Corporation
18300 Von Karman Ave.	Irvine	A	30,289	Jan-2024	The New Home Company, Inc.	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 Q1 2024	Square Feet Available	Availability Rate Q1 2024	Average Asking Lease Rate	Net Absorption Q1 2024	Net Absorption 2024	Gross Absorption Q1 2024	Gross Absorption 2024
<b>Airport Area</b>													
Costa Mesa	60	6,809,973	0	0	1,516,267	22.27%	1,973,598	28.98%	\$3.14	36,527	36,527	160,971	160,971
Irvine	243	24,107,217	0	420,980	4,265,147	17.69%	5,923,929	24.57%	\$2.79	(97,945)	(97,945)	544,303	544,303
Newport Beach	104	9,174,665	0	0	1,269,789	13.84%	1,762,212	19.21%	\$3.08	(96,896)	(96,896)	149,411	149,411
Santa Ana	9	1,980,930	0	0	588,380	29.70%	631,787	31.89%	\$2.61	(20,688)	(20,688)	18,200	18,200
Tustin	4	418,585	0	0	49,979	11.94%	70,043	16.73%	\$4.70	39,502	39,502	26,141	26,141
<b>Airport Area Total</b>	<b>420</b>	<b>42,491,370</b>	<b>0</b>	<b>420,980</b>	<b>7,689,562</b>	<b>18.10%</b>	<b>10,361,569</b>	<b>24.39%</b>	<b>\$2.91</b>	<b>(139,500)</b>	<b>(139,500)</b>	<b>899,026</b>	<b>899,026</b>
<b>Central County</b>													
Anaheim	21	1,964,515	0	150,000	460,850	23.46%	469,389	23.89%	\$2.47	9,532	9,532	51,346	51,346
Orange	64	6,211,976	0	0	1,079,185	17.37%	1,536,408	24.73%	\$2.02	(18,059)	(18,059)	56,221	56,221
Santa Ana	130	9,469,914	0	0	1,772,476	18.72%	2,159,201	22.80%	\$2.35	36,423	36,423	258,943	258,943
Tustin	38	1,965,050	0	0	199,556	10.16%	209,629	10.67%	\$2.00	(36,647)	(36,647)	40,408	40,408
<b>Central County Total</b>	<b>253</b>	<b>19,611,455</b>	<b>0</b>	<b>150,000</b>	<b>3,512,067</b>	<b>17.91%</b>	<b>4,374,627</b>	<b>22.31%</b>	<b>\$2.27</b>	<b>(8,751)</b>	<b>(8,751)</b>	<b>406,918</b>	<b>406,918</b>
<b>North County</b>													
Anaheim Hills	64	4,288,625	0	0	494,765	11.54%	578,025	13.48%	\$2.40	(51,972)	(51,972)	25,653	25,653
Brea	37	3,756,649	0	0	459,186	12.22%	754,489	20.08%	\$2.60	(37,960)	(37,960)	209,553	209,553
Buena Park	18	1,204,984	0	0	75,960	6.30%	92,138	7.65%	\$2.13	(43,145)	(43,145)	3,845	3,845
Fullerton	16	867,909	0	0	54,909	6.33%	137,370	15.83%	\$2.22	9,321	9,321	31,134	31,134
La Habra	3	115,103	0	0	4,844	4.21%	4,844	4.21%	\$1.75	(750)	(750)	0	0
La Palma	7	542,913	0	0	106,934	19.70%	165,218	30.43%	\$0.00	(11,839)	(11,839)	13,966	13,966
Placentia	6	197,762	0	0	44,063	22.28%	46,283	23.40%	\$2.00	(2,426)	(2,426)	1,451	1,451
Yorba Linda	5	289,383	0	0	21,160	7.31%	22,997	7.95%	\$2.25	200	200	200	200
<b>North County Total</b>	<b>156</b>	<b>11,263,328</b>	<b>0</b>	<b>0</b>	<b>1,261,821</b>	<b>11.20%</b>	<b>1,801,364</b>	<b>15.99%</b>	<b>\$2.42</b>	<b>(138,571)</b>	<b>(138,571)</b>	<b>285,802</b>	<b>285,802</b>
<b>South County</b>													
Aliso Viejo	37	2,918,688	0	0	1,062,686	36.41%	1,219,399	41.78%	\$2.77	(31,081)	(31,081)	183,035	183,035
Dana Point	3	127,999	0	0	0	0.00%	0	0.00%	\$0.00	1,200	1,200	1,200	1,200
Foothill Ranch	7	639,436	0	0	268,317	41.96%	262,824	41.10%	\$2.50	4,557	4,557	40,895	40,895
Irvine Spectrum	170	13,329,871	0	0	2,017,877	15.14%	2,560,250	19.21%	\$3.14	(9,892)	(9,892)	334,166	334,166
Laguna Beach	4	124,004	0	0	4,944	3.99%	4,944	3.99%	\$0.00	0	0	0	0
Laguna Hills	28	1,341,232	0	465,000	239,305	17.84%	279,342	20.83%	\$2.65	24,271	24,271	68,280	68,280
Laguna Niguel	7	395,699	0	0	72,871	18.42%	81,445	20.58%	\$2.37	5,010	5,010	10,272	10,272
Lake Forest	40	2,172,465	0	0	349,779	16.10%	369,102	16.99%	\$2.13	52,748	52,748	113,342	113,342
Mission Viejo	24	1,276,103	0	0	247,001	19.36%	289,055	22.65%	\$2.31	(3,825)	(3,825)	15,169	15,169
Rancho Santa Margarita	5	212,716	0	0	23,359	10.98%	28,759	13.52%	\$2.40	0	0	0	0
San Clemente	8	411,212	0	0	31,509	7.66%	33,943	8.25%	\$2.60	(6,328)	(6,328)	9,347	9,347
San Juan Capistrano	19	944,993	0	0	35,397	3.75%	48,542	5.14%	\$2.79	15,527	15,527	21,792	21,792
<b>South County Total</b>	<b>352</b>	<b>23,894,328</b>	<b>0</b>	<b>465,000</b>	<b>4,353,045</b>	<b>18.22%</b>	<b>5,177,605</b>	<b>21.67%</b>	<b>\$2.90</b>	<b>52,187</b>	<b>52,187</b>	<b>797,498</b>	<b>797,498</b>
<b>West County</b>													
Cypress	27	1,819,947	0	0	173,463	9.53%	214,937	11.81%	\$2.43	1,309	1,309	18,539	18,539
Fountain Valley	26	1,180,227	0	0	41,201	3.49%	43,247	3.66%	\$2.01	(2,791)	(2,791)	0	0
Garden Grove	14	710,092	0	0	62,634	8.82%	59,843	8.43%	\$2.12	6,987	6,987	9,292	9,292
Huntington Beach	32	1,805,421	0	0	312,958	17.33%	330,370	18.30%	\$2.08	7,502	7,502	28,994	28,994
Los Alamitos	8	441,664	0	0	6,276	1.42%	7,424	1.68%	\$2.35	(3,492)	(3,492)	1,520	1,520
Seal Beach	6	452,518	0	0	51,856	11.46%	59,373	13.12%	\$3.45	8,997	8,997	9,948	9,948
Stanton	4	143,361	0	0	25,894	18.06%	18,261	12.74%	\$1.43	5,906	5,906	5,906	5,906
Westminster	11	445,789	0	0	56,786	12.74%	62,306	13.98%	\$2.40	2,750	2,750	3,750	3,750
<b>West County Total</b>	<b>128</b>	<b>6,999,019</b>	<b>0</b>	<b>0</b>	<b>731,068</b>	<b>10.45%</b>	<b>795,761</b>	<b>11.37%</b>	<b>\$2.46</b>	<b>27,168</b>	<b>27,168</b>	<b>77,949</b>	<b>77,949</b>
<b>Orange County Total</b>	<b>1,309</b>	<b>104,259,500</b>	<b>0</b>	<b>1,035,980</b>	<b>17,547,563</b>	<b>16.83%</b>	<b>22,510,926</b>	<b>21.59%</b>	<b>\$2.75</b>	<b>(207,467)</b>	<b>(207,467)</b>	<b>2,467,193</b>	<b>2,467,193</b>
<b>Airport Area</b>													
Class A	122	25,731,847	0	420,980	5,682,369	22.08%	7,499,600	29.15%	\$3.09	(5,536)	(5,536)	585,392	585,392
Class B	280	15,742,922	0	0	1,941,491	12.33%	2,751,052	17.47%	\$2.63	(116,769)	(116,769)	295,609	295,609
Class C	18	1,016,601	0	0	65,702	6.46%	110,917	10.91%	\$2.67	(17,195)	(17,195)	18,025	18,025
<b>Central County</b>													
Class A	36	6,525,248	0	150,000	1,611,602	24.70%	2,026,489	31.06%	\$2.66	13,592	13,592	88,712	88,712
Class B	176	11,340,165	0	0	1,715,412	15.13%	2,127,344	18.76%	\$2.16	(9,686)	(9,686)	308,218	308,218
Class C	41	1,746,042	0	0	185,053	10.60%	220,794	12.65%	\$1.70	(12,657)	(12,657)	9,988	9,988
<b>North County</b>													
Class A	20	2,428,817	0	0	606,587	24.97%	708,986	29.19%	\$2.72	(29,559)	(29,559)	47,307	47,307
Class B	117	7,976,435	0	0	645,604	8.09%	1,082,748	13.57%	\$2.31	(108,773)	(108,773)	236,997	236,997
Class C	19	858,076	0	0	9,630	1.12%	9,630	1.12%	\$2.29	(239)	(239)	1,498	1,498
<b>South County</b>													
Class A	68	9,298,863	0	465,000	2,108,695	22.68%	2,343,435	25.20%	\$3.29	(29,525)	(29,525)	365,180	365,180
Class B	267	13,748,411	0	0	2,212,983	16.10%	2,798,792	20.36%	\$2.76	84,016	84,016	430,906	430,906
Class C	17	847,054	0	0	31,367	3.70%	35,378	4.18%	\$2.53	(2,304)	(2,304)	1,412	1,412
<b>West County</b>													
Class A	12	1,309,359	0	0	271,089	20.70%	283,593	21.66%	\$2.59	20,612	20,612	20,612	20,612
Class B	101	5,166,242	0	0	453,523	8.78%	505,712	9.79%	\$2.41	1,012	1,012	51,793	51,793
Class C	15	523,418	0	0	6,456	1.23%	6,456	1.23%	\$1.87	5,544	5,544	5,544	5,544
<b>Orange County</b>													
Class A	258	45,294,134	0	1,035,980	10,280,342	22.70%	12,862,103	28.40%	\$3.05	(30,416)	(30,416)	1,107,203	1,107,203
Class B	941	53,974,175	0	0	6,969,013	12.91%	9,265,648	17.17%	\$2.57	(150,200)	(150,200)	1,323,523	1,323,523
Class C	110	4,991,191	0	0	298,208	5.97%	383,175	7.68%	\$1.94	(26,851)	(26,851)	36,467	36,467
<b>Orange County Total</b>	<b>1,309</b>	<b>104,259,500</b>	<b>0</b>	<b>1,035,980</b>	<b>17,547,563</b>	<b>16.83%</b>	<b>22,510,926</b>	<b>21.59%</b>	<b>\$2.75</b>	<b>(207,467)</b>	<b>(207,467)</b>	<b>2,467,193</b>	<b>2,467,193</b>

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.



## Navigating Challenges

by **Doug Killian**

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The Orange County office market, in line with other submarkets in Southern California, is encountering notable challenges driven by declining commercial real estate prices due to rising interest rates and an uptick in vacant spaces. Let's delve deeper into the specifics.

A recent survey by ResumeBuilders gathered insights from more than a thousand corporate decision-makers regarding the Return to Office (RTO) trend, revealing key findings. Companies are showing an optimistic outlook, with a significant 90% planning to reintroduce employees to physical offices by 2024. Minimal resistance is observed, as only 2% of respondents indicated their companies have no plans to mandate a return to physical workplaces. Impressively, 72% of decision makers believe that RTO initiatives have positively influenced their company's revenue. Interestingly, 28% of companies are prepared to enforce RTO policies rigorously, including the possibility of termination for non-compliance.

While the momentum towards RTO is evident, a delicate balance must be struck between employee satisfaction, professional growth, and productivity. The evolving remote-work model is reshaping office space requirements as employees divide their time between home and office. This shift, coupled with economic pressures and cost-saving imperatives, is transforming the market landscape.

With regard to the repurposing of office assets into multifamily properties, stakeholders face several key challenges: High office valuations that do not align with current demand levels, increased project capital expenditure due to recent inflation, and the necessity for alternative funding sources when pivoting from office-specific projects. Additionally, the financial difficulties of repurposing efforts are compounded by high conversion costs, limited differences in returns between office and multifamily assets, technical infrastructure issues, and navigating regulatory hurdles that can significantly increase project expenses. These factors underscore the importance of innovative funding approaches to successfully navigate the complexities associated with conversion.

In response to softening office demand, landlords are offering more free rent and other concessions. Forward-thinking landlords are enhancing common areas with amenities like fitness centers, indoor workspaces, and outdoor retreats to retain current tenants and attract new ones seeking a comprehensive work environment.

### Please Contact Us for Further Information

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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.

## 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