Kidder Mathews

MARKET TRENDS | OFFICE

LOS ANGELES

2ND QUARTER
2019

▼ **ABSORPTION** | ◀▶ **VACANCY** | ▲ **RENTAL RATE** | ▼ **CONSTRUCTION DELIVERIES**

The Los Angeles office market continued to remain stable in 2Q19, amidst the slow delivery of new supply. Overall employment growth in LA County has aided office market stability and remains positive. The unemployment rate in Los Angeles sits at 4.5%, and is higher than the national average of 3.6%. According to the State of California's Employment Development Department, a total of 46,200 jobs were added this year. Professional, business, education, health, government, and information companies added 25,400 jobs since May. Vacancies are higher in traditional office neighborhoods like Miracle Mile, Mid-Wilshire, Park Mile and CBD Los Angeles. Leasing activity has increased in sprawling, artsy and bohemian areas such as West Hollywood, Beach Cities and Southeast Los Angeles, where vacancies are the lowest. It is no surprise, asking rents continue to climb to post-recession highs, although vacancy rates have remained leveled at 9.8%. Demand is healthy, as over 7.4 million SF in supply is underway mostly in DTLA, Culver City and Hollywood. With healthy job growth, tighter vacancies and tenant demand fundamentals are in place to keep the office market strong in LA.

More notable deals include 101 Continental Blvd in El Segundo, which traded for $400/s.f. or $138.5 million. The buyer has confidence in El Segundo's office market. 5800 Bristol Parkway traded for $260 million or $836/SF. The asset was sold for recapitalization. Another notable sale took place in May and traded at $58 million. The property is located at 11611 San Vicente Blvd. The buyer feels West LA is supply constrained and plans to reposition and reimage the asset. Prices this quarter continue to push skyrocket premiums. Quality assets are still highly sought after by most investor types and pricing is expected to grow in line with inflation. For example, Santa Monica, Beverly Hills, Marina del Rey, Century City, and Downtown have recorded sales exceeding $1,000/s.f. this year. Competition for production, tech, and media space is evident. Furthermore, this lack of product has pushed some companies to build out their own space. Lin Pictures (It, The Lego Movie) is developing a 1.7-acre lot in Westlake, while Amazon Studios is working with developer Hackman Capital to customize large portions of their floor plans. Volume is on track this year to post another all-time high.

This quarter vacancies reached the lowest they have ever been at 9.8% this quarter. Absorption rebounded from Q1 2019's losses of 1.1 million s.f into Q2 with a positive 660,431 s. f. Eyes and interest are upon Culver City as Apple, Amazon and Google have yet to officially move into their spaces. Office spaces are approaching record leasing rates. This quarter, office spaces in LA were on the market at an average of 10 months, the lowest ever in the past 10 years. El Segundo remains a hotbed for rent growth alongside 190th Street corridor. Culver City, DTLA, and Marina Del Ray experienced the strongest absorption this quarter.Santa Clarita and San Gabriel saw favorable occupancy gains as well.

Availabilities are the highest in the LAX area. 25% of inventory remains vacant, with under 20,000 s.f. being delivered since 2000. Typically, cities in or near the South Bay region are drivers of rent growth. For example, El Segundo which has the highest rent growth ($3.98 s.f. FS), fell 3% from Q4 2018, yet close to 3% more growth than Los Angeles. This growth is expected to slow down as this cycle returns to normal ranges previously seen in 2013. The allure of Silicon Beach is undeniable, so a small slowdown is not expected to disrupt the market.

SUBMARKET LEASING ACTIVITY 2Q 2019

1.5M SF
WEST LOS ANGELES

1.0M SF
DOWNTOWN LA

821K SF
TRI-CITIES

658K SF
SOUTH BAY

476K SF
MID-WILSHIRE

SUBMARKET LEASING ACTIVITY YTD 2019

3.36M SF
WEST LOS ANGELES

1.59M SF
DOWNTOWN LA

1.73M SF
TRI-CITIES

1.39M SF
SOUTH BAY

886K SF
MID-WILSHIRE

2Q 2019 MARKET HIGHLIGHTS

VACANCY hits the lowest it has been in the past 10 years

RENTAL RATES are up 18% from the last all time high in 2008 and have outpaced the nation since 2013

AVG SALES PRICE for the quarter was $420/sf with cap rates at 5.4% and over $7.4 billion worth of transactions over past year

ECONOMICS median household income is $69,000, 30% of residents hold bachelors degree, 10% lower than major metros, unemployment rate 4.5%. Computer/Math jobs most in demand

The average asking rental rate was $3.21 per square foot on a full-service gross basis per month, a 4.9% increase from a year prior when rates averaged $3.06 per square foot. Class A office space averaged $3.50 s.f. while rental rates for Class B office space averaged $2.89 s.f. and Class C averaged $2.72, all post-recession records. In other words rental rates have grown 13% since 2009. Santa Monica continually commands the highest average direct rents at $4.51 s.f. On the other hand, Hawthorne and Gardena have the lowest average rents at $1.84 s.f. As, conversions continue to become the norm in this area, followed by high demand of quality office space, we can expect rental rates to increase or hold firm. Santa Monica's sales volume is unmatched this quarter as sales have exceeded $1.27 billion in transactional volume. Average sales in this submarket have eclipsed $752 per s.f. In addition, rent growth dropped sharply from last quarter's 3.16%. As one of the priciest submarkets, the slowing growth may hint at affordability concerns. The last time growth was this slow was in Q2 2011.

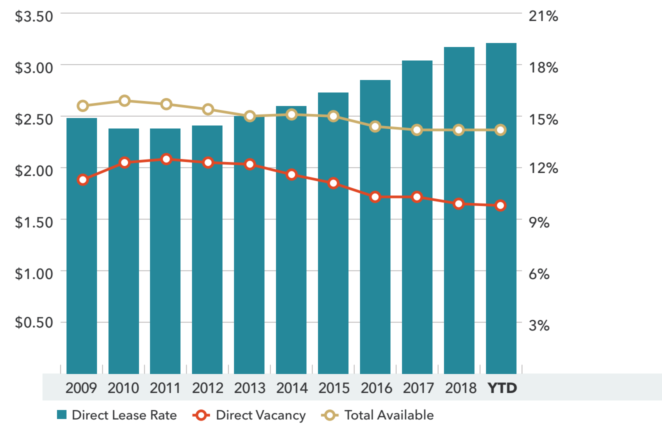
The office market continues to see impressive volume in For Sale listings. A large majority of these are medical tenants. A popular consensus is that medical tenants are selling their condos and offices because doctors are entering retirement or smaller providers joining larger providers to cut costs. Traditionally, doctors have leased small medical office space to serve the needs of their private practices. However, over the past few years, the medical field has seen much consolidation of private practices with lots of smaller spaces being integrated with larger health care providers. According to a study by the Association of American Medical Colleges during Q3 2018, by 2030 we will see a shortage of 49K physicians.

There's a new wave of shared workspace that's serving the needs of medical practitioners and their patients. Doctors operating their own offices are selling their practices to the larger providers in order to reap the benefits that result from the overall efficiency of more doctors sharing the same medical space. Physicians who prefer not to share may end up having a tough time competing with the large providers. Companies like Viva MedSuites are providing a new option to the smaller providers. There are still challenges to get the larger providers into this space. Getting approvals to incorporate behavioral health components is time consuming along with zoning and increasing construction costs. According to a new study by the 2019 National Employer Survey on Mental Health. According to the Affordable Health Care Act (AHCA), insurance companies are now required to provide physical proof that all health providers are providing care in high quality locations just as primary care providers. This mandate has increased the demand from health and quasi-health tenants. If these providers desire to continue receiving insurance payments, they have to move into new and high quality spaces. Patients and providers are also willing to travel further for work and care. To retain or attract the larger tenants, developers may consider constructing new buildings with coworking aspects but containin a look and feel like college campuses. These facilities will often offer yoga, supportive houses, small lab rooms, open courtyards, food courts, dog parks, outdoor grills and gyms in one place.

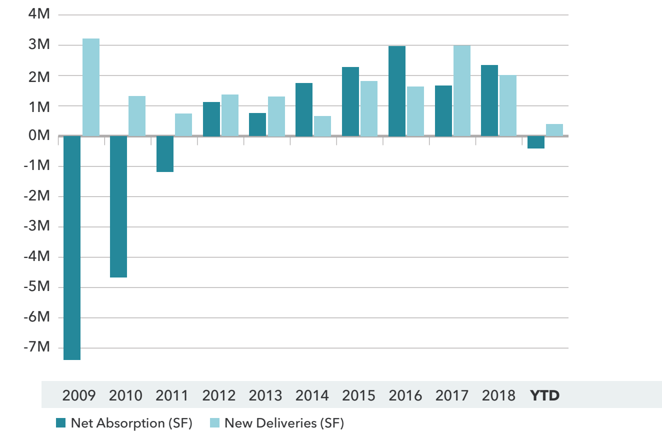
Furthermore, owners are continuing to convert properties into creative office space. For example, some landlords are replacing escalators and elevators to attract tech friendly tenants. For instance, Brookfield is removing 2 escalators out of California Market Center in the Fashion District of downtown Los Angeles. The $170 million makeover will convert into an open-air campus for high profile tech tenants. It is anticipated that more radical makeovers are to come, fueled by shifts in workplace aesthetics among creative and tech tenants. People are desiring to move more freely within an office. Tall towered buildings still attract business services such as lawyers, accountants, and real estate companies. However, shifts in workplace design, large TI allowances and increasing premiums further show the importance of tenant improvements this quarter. Newer buildings offer natural light, outdoor decks and breakout spaces where people can work or socialize away from their desks. Some developers are calling these projects "campuses." The 550,000 s.f. project at 888 Douglas St. is a great example of this trend. Owned by Northrop Grumman, Hackman Capital plans to build an outdoor theater with plush sofa seats, high ceilings lined with glass, and multiple open areas to lounge and work, swinging chairs in the lobby, wooden stairs leading to an open bridge for walking, and an outdoor courtyard reminiscent of a school campus. Finally, abundant parking is not just a luxury. According to a recent Tenant Broker survey, it has proven to be a necessity this quarter.

Source: AHCA, NESMH, Costar, Urbanize LA, California Department of Labor, GlobeSt.com, Allwork.space

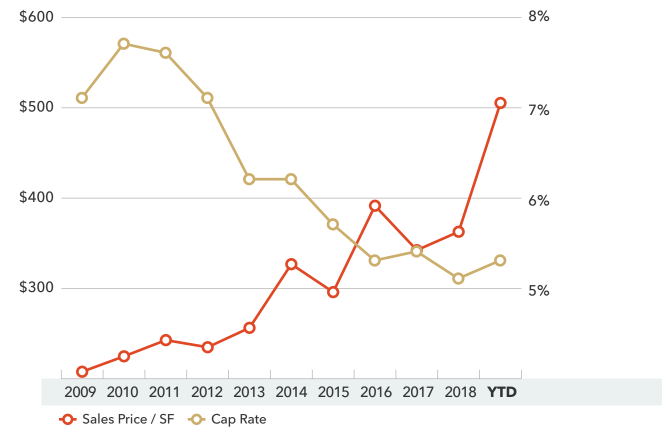
LEASE RATE, VACANCY & AVAILABILITY



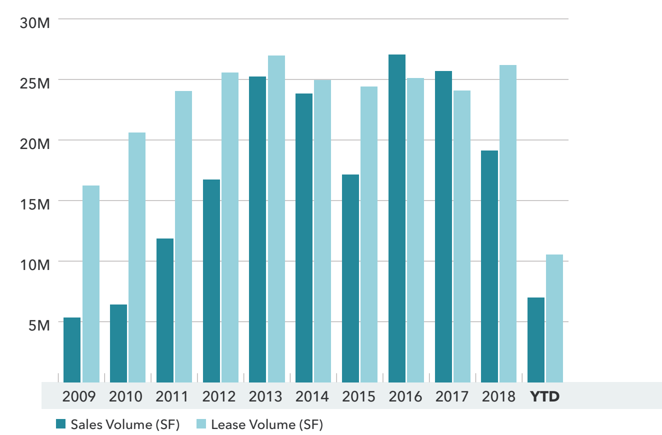
NET ABSORPTION & NEW DELIVERIES



AVERAGE SALE PRICE & CAP RATES



SALES VOLUME VS. LEASE VOLUME



LOS ANGELES SUBMARKET STATISTICS

Submarket	Total Inventory	Direct Vacancy Rate	Sublet Vacancy Rate	Total Vacancy Rate	Total Available Rate	2Q Direct Net Absorption	2019 Direct Net Absorption	2Q Leasing Activity	2019 Leasing Activity	Rental Rate
Burbank	12,937,454	5.7%	1.0%	6.7%	9.8%	135,637	162,938	371,262	554,672	$3.47
Glendale	11,050,955	10.9%	0.7%	11.6%	13.3%	-24,942	-38,276	111,627	415,906	$3.05
North Hollywood	2,297,306	9.7%	0.0%	9.7%	17.8%	47,924	-118,614	24,331	64,702	$3.42
Pasadena/Arcadia/Morovia	19,190,911	8.6%	0.3%	8.9%	15.3%	-64,995	-99,960	267,444	605,314	$2.83
Studio/Universal Cities	3,167,958	4.6%	0.0%	4.6%	6.8%	12,567	31,196	46,572	91,126	$3.18
Tri-Cities	**48,644,584**	**8.1%**	**0.5%**	**8.7%**	**13.0%**	**106,191**	**-62,716**	**821,236**	**1,731,720**	**$3.07**
Downtown Los Angeles	**65,306,752**	**13.1%**	**0.3%**	**13.5%**	**17.9%**	**600,183**	**262,001**	**1,060,850**	**1,595,092**	**$3.07**
Mid-Cities	**9,686,088**	**9.1%**	**0.4%**	**9.4%**	**12.9%**	**-14,310**	**-2,565**	**103,315**	**148,452**	**$2.35**
Hollywood/Silver Lake	10,795,398	7.3%	2.3%	9.6%	12.7%	-108,147	-156,081	242,914	337,527	$4.33
Mid-Wilshire	15,259,745	13.6%	0.4%	14.0%	15.1%	12,879	-42,073	62,110	265,556	$2.41
Miracle Mile	5,592,046	15.5%	1.4%	16.9%	21.3%	-13,774	-20,145	88,311	114,294	$4.21
Park Mile	1,818,647	13.3%	0.7%	14.0%	17.0%	25,558	12,725	16,329	16,329	$3.31
West Hollywood	6,283,004	3.8%	1.1%	4.9%	9.2%	44,050	87,737	66,975	152,621	$4.65
Mid-Wilshire	**39,748,840**	**10.6%**	**1.2%**	**11.8%**	**14.4%**	**-39,434**	**-117,837**	**476,639**	**886,327**	**$3.32**
Eastern SFV	6,979,225	8.2%	0.0%	8.2%	10.0%	-142,751	-179,964	81,720	124,916	$2.46
Encino	4,767,106	9.5%	0.2%	9.7%	14.3%	-19,127	37,997	100,250	180,227	$2.73
Sherman Oaks	3,520,737	8.8%	0.3%	9.0%	11.6%	-6,914	-40,180	68,088	122,504	$2.68
Tarzana	1,596,838	8.5%	0.3%	8.9%	16.1%	-33,489	-34,674	20,728	26,227	$2.86
Western SFV	5,928,928	8.9%	0.1%	9.0%	11.3%	-15,048	-57,304	16,430	45,583	$2.33
Woodland Hills/Warner Cit	9,717,231	9.1%	0.2%	9.3%	11.2%	-13,311	-22,901	116,367	270,255	$2.79
San Fernando Valley	**32,510,065**	**8.8%**	**0.2%**	**9.0%**	**11.7%**	**-230,640**	**-297,026**	**403,583**	**769,712**	**$2.63**
San Gabriel Valley	**25,134,215**	**7.0%**	**0.2%**	**7.1%**	**8.2%**	**22,966**	**138,136**	**175,525**	**458,067**	**$2.23**
Santa Clarita Valley	**4,315,594**	**7.7%**	**0.3%**	**8.0%**	**16.9%**	**74,780**	**33,220**	**42,852**	**123,870**	**$2.62**
190th Street Corridor	5,243,164	17.8%	0.1%	17.9%	29.2%	8,838	31,395	132,097	169,827	$2.34
Beach Cities/Palos Verdes	4,431,888	5.2%	2.6%	7.9%	11.9%	-11,243	-36,757	21,503	50,465	$3.05
El Segundo	17,484,881	10.6%	1.4%	12.0%	17.2%	-260,528	-278,950	259,208	443,473	$3.98
Hawthorne/Gardena	2,596,980	6.3%	0.0%	6.3%	6.9%	-22,499	12,728	5,983	22,993	$1.84
LAX	5,379,546	25.1%	0.0%	25.1%	26.7%	-20,040	-28,963	72,344	154,498	$2.25
Downtown Long Beach	7,051,627	12.7%	0.4%	13.1%	14.5%	9,762	-31,166	76,866	147,100	$2.44
Suburban Long Beach	8,519,837	6.1%	0.0%	6.1%	12.5%	2,948	-54,539	36,143	180,057	$2.34
Torrance	8,099,897	7.3%	0.1%	7.4%	11.7%	72,491	26,008	54,109	224,935	$2.72
South Bay	**58,807,820**	**11.1%**	**0.7%**	**11.8%**	**16.6%**	**-220,271**	**-360,244**	**658,253**	**1,393,348**	**$2.93**
Southeast Los Angeles	**7,721,981**	**5.8%**	**0.4%**	**6.2%**	**7.8%**	**-30,367**	**-62,022**	**39,235**	**82,562**	**$2.13**
West Los Angeles	**79,280,459**	**8.8%**	**1.0%**	**9.7%**	**13.6%**	**391,333**	**63,347**	**1,582,244**	**3,362,801**	**$4.51**
Los Angeles Total	**371,156,398**	**9.8%**	**0.6%**	**10.5%**	**14.2%**	**660,431**	**-405,706**	**5,363,732**	**10,551,951**	**$3.21**
Class A	176,198,257	11.7%	0.8%	12.6%	16.8%	986,869	565,008	3,007,252	6,041,260	$3.50
Class B	148,240,877	9.0%	0.5%	9.5%	13.1%	-164,735	-594,689	1,998,478	3,891,339	$2.89
Class C	46,717,264	5.5%	0.1%	5.7%	7.7%	-161,703	-376,025	358,002	619,352	$2.72

Market Breakdown

	2Q 2019	1Q 2019	2Q 2018	Annual % Change
Vacancy Rate	9.8%	10.1%	10.2%	**-3.92%**
Availability Rate	14.2%	14.2%	14.5%	**-2.07%**
Asking Lease Rate	$3.21	$3.19	$3.06	**4.90%**
Leased SF	5,363,732	5,188,219	6,569,880	**-18.36%**
Sold SF	3,738,500	3,259,285	5,155,764	**-27.49%**
Net Absorption	660,431	-1,066,137	724,867	**N/A**

Notable Sale Transactions

ONNI GROUP 5700 Wilshire Blvd , Los Angeles
586,766 s.f. | $629.9M or $1,073.51/s.f.

OCEAN WEST MANAGEMENT 777 Aviation Blvd, El Segundo
310,985 s.f. | $170M or $836/s.f.

ALLIED COMMERCIAL HOLDINGS 1601 Main St Venice
22,000 s.f. | $22M or $1,000/s.f.

Notable Lease Transactions

L.A. CARE HEALTH PLAN 1200 West 7th St, Los Angeles
212,335 s.f. leased

GHOST MANAGEMENT GROUP 767 S Alameda St, Los Angeles
114,939 s.f. leased

WARNER BROTHERS 777 S Santa Fe Ave, Los Angeles
123,998 s.f. leased

Kidder Mathews

Kidder Mathews is the largest, independent commercial real estate firm on the West Coast, with 800 real estate professionals and staff in 22 offices in Washington, Oregon, California, Nevada, and Arizona. We offer a complete range of brokerage, appraisal, property management, consulting, project and construction management, and debt equity finance services for all property types.

COMMERCIAL BROKERAGE

20M ANNUAL SALES SF

400+ NO. OF BROKERS

$9B ANNUAL TRANSACTION VOLUME

40M ANNUAL LEASING SF

VALUATION ADVISORY

1,600+ APPRAISALS ANNUALLY

36/23 TOTAL NO. APPRAISERS/MAI'S

PROPERTY MANAGEMENT

55M+ MANAGEMENT PORTFOLIO SF

The information in this report was composed by the Kidder Mathews Research Group.

JERRY HOLDNER
Director of Research
949.557.5050
jerry.holdner@kidder.com

ROBERT THORNBURGH, SIOR, CCIM, CPM
Regional President, Brokerage
Southern California
310.807.0880
robert.thornburgh@kidder.com
LIC N° 01324961

KIDDER.COM