

Savills Studley Report Orange County office sector

Q4 2018



SUMMARY

Market Highlights

LEASING SPIKES

Overall quarterly leasing activity nearly doubled, jumping to 2.2 million square feet (msf). Tenants have leased 6.9 msf in the four most recent quarters.

CLASS A AVAILABILITY RISES

Orange County's overall availability rate was unchanged, remaining at 19.5%. The Class A rate rose by 90 basis points to 21.9% and has spiked by 280 basis points from a year ago.

RENT STABLE

The overall average asking rent rose to \$35.71, ticking up by 0.5%. The Class A rate fell from \$39.53 to \$39.45.

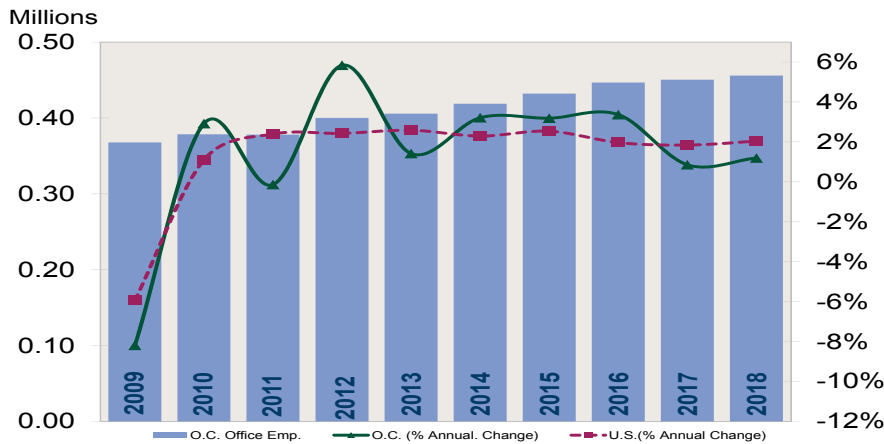
SALES ALMOST UNCHANGED

Office property sales during the first 11 months of 2018 totaled \$2.5 billion, a 5.6% decrease compared to the same period during 2017.

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"Market conditions remain strong, but macroeconomic headwinds could spur market softening in 2019. Rent growth has started to stabilize as sublease options increase, and tenant movement to new buildings opens options in existing properties. Several larger transactions at year's end, including rapid growth from coworking providers, is a sign of confidence in market demand. However, supply increases will create favorable conditions as landlords are forced to boost concessions and cater to tenant demand."

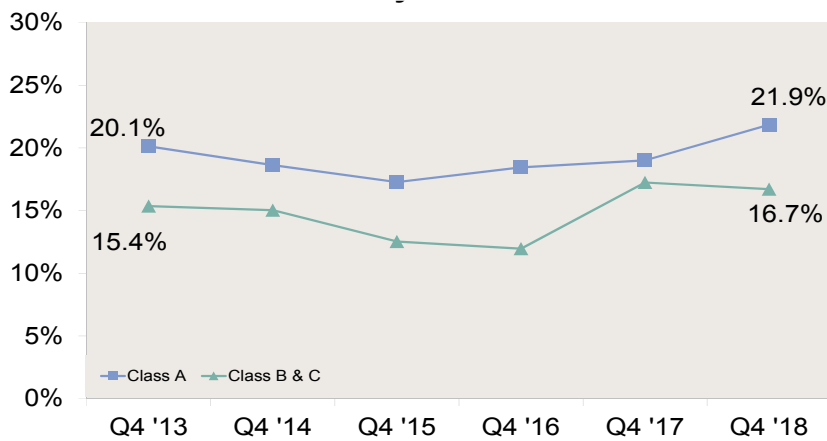
Royce Sharf,
Executive Vice President

Office-Using Employment Trends

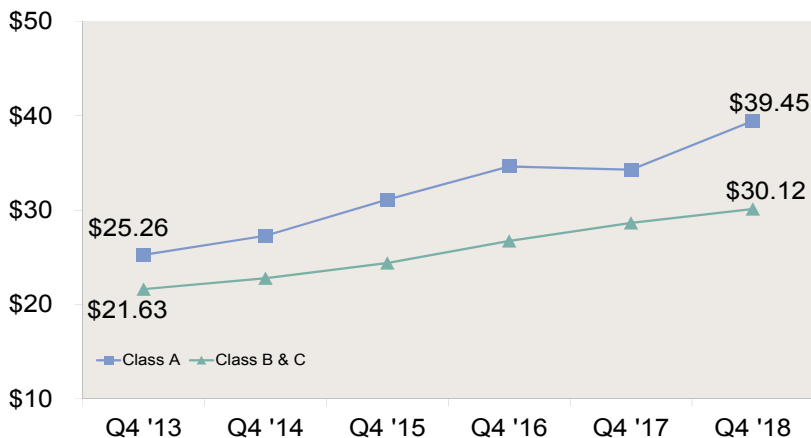


Source: Bureau of Labor Statistics^

Availability Rate Trends



Asking Rent Trends



Economy Holds Strong, Despite Some Rising Headwinds

Orange County's office market remains healthy as tenants in the tech, media, and marketing industries continue to grow. Orange County's office market expanded further in the final quarter of the year, and as of year-end had a Class A availability rate of 21.9%, rising by 100 basis points. Larger tenants seeking the highest-quality blocks of space in prime locations such as The Airport Area and Irvine Spectrum have new options to consider. Space has expanded as buildings underway are set to deliver early in 2019 and more sublease options come to market. Asking rent continues to push higher and ended 2018 averaging just under \$40/sf for Class A buildings, with much higher rent in the newest properties underway in Irvine Spectrum.

Orange County's labor market has gone from one of the worst, to one of the best. The unemployment rate has plummeted from 9.0% in December of 2010, to only 3.0% at the close of this year. The region has regained the 77,000 jobs lost in the recession (hitting the break even point in late 2018) and has since added 13,000 more jobs. From the perspective of growing businesses, the low unemployment rate presents a high hurdle to scaling up rapidly. Tight labor markets and a lack of the most qualified workers adds to the challenges that companies face as they try to scale up.

Coworking Providers Continue Expansion

Sustained startup activity continues to fuel demand among smaller and mid-sized businesses. Coworking providers are targeting Orange County in the hopes of landing fast-growing tenants that are unsure of their future space needs. The top fractional office space providers had roughly 1.2 msf of coworking space, as of early September. That represents an increase of about 20% from the prior year.

WeWork is leading the charge. The New York City-based coworking provider accounted for a couple of the top leases during the fourth quarter. The coworking trailblazer leased 44,520 SF at Irvine Company's 400 Spectrum Center after reaching capacity at its neighboring 200 Spectrum Center location, just over two years from its initial opening. In addition, Wework leased 63,816 SF at Trammel Crow's The Boardwalk in the Airport Area. These two new leases, in two core Orange County submarkets and in two

of the newest developments commanding top market rents, underscore WeWork's confidence in this segment of the market.

Industrious and Spaces – as well as some smaller firms (TechSpace, LiquidSpace, PeopleSpace) – are jumping into the fray as well. Landlords are also seizing on the flexibility that shared office providers give. HQ by WeWork, which focuses on short term space for established mid-sized corporations is the most direct threat to landlords and brokers.

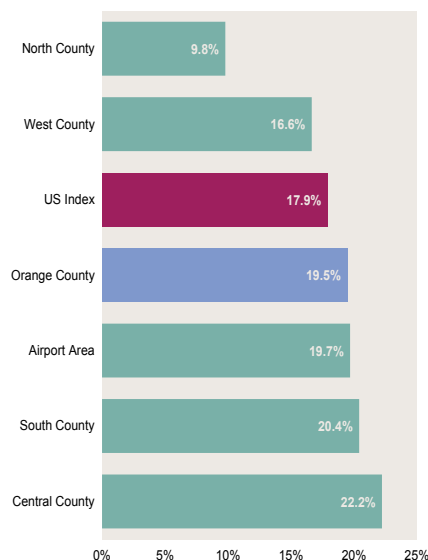
Following this leasing activity, 400 Spectrum is now 70% leased. The 466,696-sf building delivered roughly a year ago. Womble Bond & Dickinson LLP was another internationally recognized tenant to recently take space in the tower this quarter, leasing a total of 17,700 SF. The CEO announced the move as part of a goal to recruit Orange County's top legal professionals and to signal the firm's commitment to Orange County and Southern California.

Local innovators continue to grow. Karma Automotive added about 40 local employees this year, including additions to its high voltage battery and electrical engineering teams. Other companies seek to draw from Orange County's pool of executive and C-suite level talent. Chipotle recently added Chief Legal and Development officers locally, and Cloudevirga also recruited their Chief Product officer Tim Von Kaenel, previously with LoanDepot.

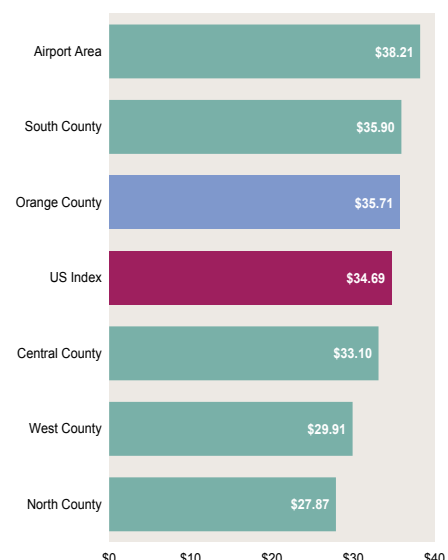
Top Deal to End the Year

In addition to activity from smaller tenants, Orange County's top employers are also active, further depleting the supply of big blocks of space. Glaukos recently announced that it will move its headquarters to Aliso Viejo in the largest lease transaction of 2018. The healthcare company will occupy the three-building, 165,000-sf campus in mid-2019. In addition, Glaukos is in discussions to purchase an adjacent 2.5 acres of land entitled for another 46,000 sf of office space. Glaukos employed 387 people at the end of last year. The new space will hold 550 employees comfortably, and provides great branding as the company looks to attract and hire new talent. Investment companies Stillwater and CrossHarbor paid \$36 million for the campus in 2017. It was previously owned and occupied by networking products maker QLogic Corp. One of the city's largest tech companies, QLogic downsized into smaller space in Irvine last year.

Availability Rate Comparison



Overall Rental Rate Comparison



Major Transactions

Tenant	Sq Feet	Address	Market Area
Taco Bell	181,000	1 Glen Bell Way	South County
Glaukos	165,000	26600-26700 Aliso Viejo Pky	South County
AltaMed	90,533	1325 N Anaheim Blvd	North County
AECOM	73,908	999 W Town and Country Rd	Central County
WeWork	63,816	18565-18575 Jamboree Rd	Airport Area
Advantage Sales & Marketing	62,876	1610 E Saint Andrew Pl	Central County
Google	43,720	19520 Jamboree Rd	Airport Area
Anaheim Ducks	31,938	1500 S Douglas Rd	Central County
Medterra	29,000	9801 Research Dr	South County
Allied Bank	26,312	535 Anton Blvd	Airport Area
Sum of Leases	768,103		

Despite a stronger dollar and some pullback among foreign investors, capital markets activity remains strong. Of note, the owners of the Element expanded their local holdings, paying \$18.6 million for 2100 and 2200 Orangewood Avenue which have a combined total of about 107,000 sf. The offices were sold by Glendale-based PS Business Parks Inc., a real estate investment trust that has sold three Orange County properties this year.

The market for big blocks of quality space and creative office space is tight in much of the region, but mid-sized tenants have a few more options. Sublease space has continued to pile up as firms relocate early, downsize, and employ space efficiency and workplace strategy. Total sublet space has risen, increasing to 2.7 msf regionally. After signing a 155,000-sf lease earlier this year, defense technology firm Anduril is giving back roughly 45,000 sf of its space prior to having even occupied it. In a market where flexible office solutions are so highly sought

out, these space alternatives can generate interest from both established and emerging modern tech companies. This sublease accounts for only a portion of the 1.3 msf of sublet space available in the Greater Airport Area (Newport Beach, Costa Mesa, Irvine) – 51 of the 133 subleases have come on the market since October.

Overall, the Orange County office market remains strong, with several new developments set to deliver in 2019, including Irvine Company's 'The Quad', and Lincoln Property Company's 'The Flight at Tustin Legacy.' These new developments illustrate landlord confidence in market demand, especially for big block users targeting Class A space. Net absorption and leasing activity both rose from the third to fourth quarter another strong sign of tenant demand heading into the New Year. Rising availability, coupled with a growing amount of sublease spaces commanding lower than market rents should temper rental rate growth in 2019.

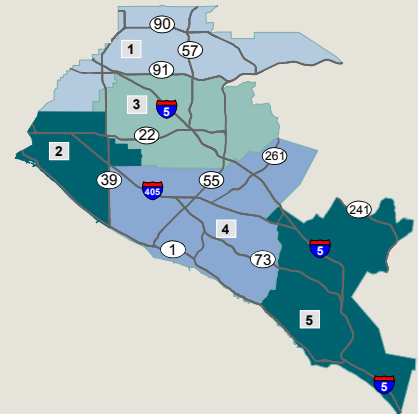
Map	Submarket	Total Inventory	Leasing Activity	Available SF			Availability Rate			Asking Rents Per SF		
		SF (1000's)	Last 12 Months	This Quarter	% Change from Last Qtr.	Year Ago	This Quarter	pp Change from Last Qtr. ⁽¹⁾	Year Ago	This Quarter	% Change from Last Qtr.	Year Ago
1	North County	6,397	363	626	-11.9%	867	9.8%	-1.3%	13.5%	\$27.87	0.8%	\$24.38
	North County - Class A	2,265	62	293	-11.9%	358	12.9%	-1.7%	15.8%	\$29.77	-0.3%	\$27.45
2	West County	4,011	261	668	37.6%	367	16.6%	4.5%	9.2%	\$29.91	6.3%	\$27.32
	West County - Class A	1,385	170	351	62.9%	193	25.3%	9.8%	13.9%	\$33.45	3.1%	\$31.50
3	Central County	16,719	842	3,715	0.9%	2,924	22.2%	0.2%	17.9%	\$33.10	0.7%	\$26.16
	Central County - Class A	7,471	241	1,761	6.5%	982	23.6%	1.4%	13.9%	\$41.17	1.0%	\$28.10
4	Airport Area	35,925	3,910	7,073	-9.1%	8,286	19.7%	-2.0%	23.1%	\$0.00	#DIV/0!	\$0.00
	Airport Area - Class A	23,773	2,639	4,834	-9.8%	5,353	20.3%	-2.2%	22.5%	\$40.07	0.5%	\$35.61
5	South County	19,510	1,570	3,982	18.6%	2,341	20.4%	2.9%	12.5%	\$35.90	1.0%	\$33.50
	South County - Class A	9,127	833	2,384	45.7%	1,261	26.1%	7.7%	15.1%	\$38.99	-2.6%	\$35.86
1-5	Orange County Total	82,562	6,946	16,063	0.3%	14,786	19.5%	0.0%	18.2%	\$35.71	0.5%	\$31.76
	Orange County Total - Class A	44,022	3,946	9,623	4.7%	8,147	21.9%	0.9%	19.0%	\$39.45	-0.2%	\$34.29

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(1) Percentage point change for availability rates.
 Unless otherwise noted, all rents quoted throughout this report are average asking gross (full service) rents psf.
 Statistics are calculated using both direct and sublease information.
 ^Unless otherwise noted, source for data is Savills Studley.,
 The information in this report is obtained from sources deemed reliable, but no representation is made as to the accuracy thereof. Statistics compiled with the support of The CoStar Group.

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