

Orange County

Office Market Outlook Q2 2023

MARKET OVERVIEW

During the second quarter of 2023, the rate of office space being vacated within Orange County's office market witnessed a slowdown, with a lower 0.9% quarter-over-quarter increase in vacant space, contrasting the higher 16.9% year-over-year rise, resulting in a total of 20.9 million vacant square feet of office space. This trend was driven by the tug and pull between work from home and returning to the office. Similarly, the growth rate of available sublease space also experienced a slower pace down 0.4% quarter over quarter, compared to a 22.7% year-over-year increase, reaching 4.5 million square feet. However, the available sublease space remained considerably higher than the peak during the Great Recession. Overall, Orange County's office market had 26.9 million square feet of available office space during Q2. The challenge of encouraging workers to return to the office since the pandemic has impacted office building owners, leading to rising vacancy rates, although the rate of increase in vacant space appears to be slowing down.

The availability of office space stabilized as the market experienced only a slight uptick of 1 cent in the average rent compared to the previous quarter. However, year over year, the rent slid by 1.8%, leading to an average rent of \$2.68 per square foot on a full-service gross basis. The weak rent growth, coupled with low demand for office space, had a significant impact on the amount of space under construction. With no new construction taking place, the year-over-year construction experienced a sharp drop of 79.1%, remaining at 265,361 square feet in the second quarter.

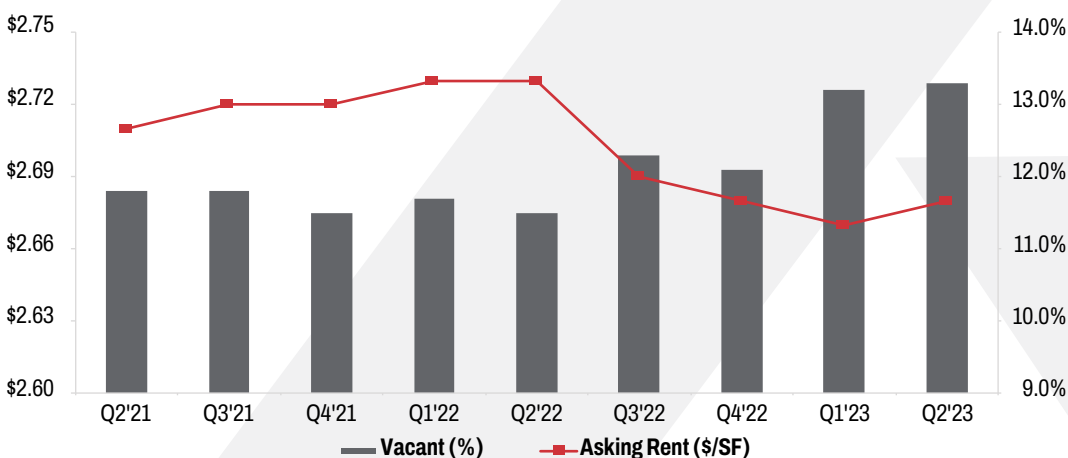
TRENDS TO WATCH

In Q2, the vacancy rate for newly constructed office buildings in Orange County experienced a notable decrease since the pandemic shutdown in 2020, declining by 6.2% quarter over quarter and reaching 24.9%. These new buildings, with an average of 2 stories and none exceeding four, witnessed this improvement. Despite the level of vacant space remaining more than double compared to a year ago, there is an expectation of gradual improvement in occupancy due to a preference for low-rise quality office space. The average asking rent for new construction remained unchanged for the previous three quarters but declined by 24.5% compared to Q2 2020, reaching \$3.94 per square foot.

Furthermore, the vacancy rate for buildings under 6 stories experienced a marginal decline of 0.1%, bringing it to 11.5%, resulting in a total of 14 million square feet of vacant space. Conversely, buildings 7 stories or higher witnessed a 4.1% increase in the vacancy rate, reaching a higher rate of 20.1%, totaling 6.7 million square feet of vacant space. Rent for buildings under 6 stories remained stable at \$2.63 per square foot, while buildings 7 stories or higher experienced a 3.4% increase, reaching \$3.04 per square foot.

The demand for office space will continue to be influenced by work-from-home trends, building preferences, and asking rent. With this, the office market is displaying signs of stabilization compared to the previous rapid increase in vacancy rates. Nevertheless, both landlords and tenants will face difficulties during the challenging recovery period, ultimately impacting real estate values.

VACANCY RATE AND AVERAGE ASKING RENT



MARKET OUTLOOK

**Asking
Rental Rates**



**Sale
Prices**



**Availability
Vacancy Rates**



**Landlord
Concessions**



**Sales/Leasing
Volume**



**New
Construction**



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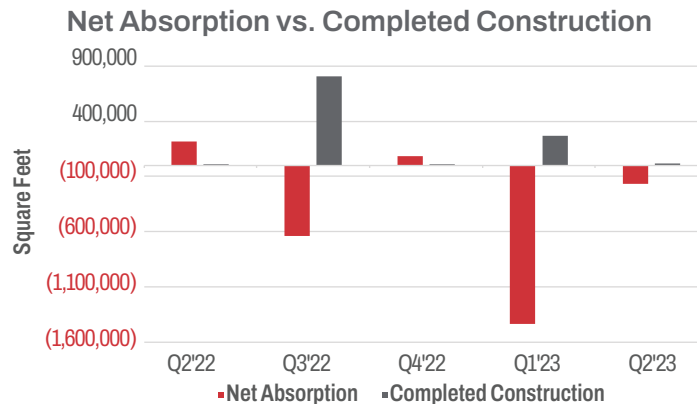
MARKET STATISTICS*

Submarket	Existing Total RBA (SF)	Under Construction (SF)	Total Available (%)	Total Vacancy (%)	Leasing Volume (SF)	YTD Leasing Volume (SF)	Sales Volume (SF)	YTD Sales Volume (SF)	Average Asking Rent \$/SF NNN	Average Sale Price \$/SF
Airport	73,972,956	7,072	20.1%	15.6%	1,369,940	2,193,158	661,827	1,702,267	\$2.75	\$167
Central	14,979,582	155,200	16.1%	12.5%	138,864	251,763	166,193	188,492	\$2.50	\$175
North	19,247,570	0	11.3%	8.4%	201,919	411,623	0	29,036	\$2.47	-
South	35,000,919	97,893	17.3%	13.6%	513,677	1,027,354	136,026	521,538	\$2.72	\$315
West	13,962,659	5,196	10.7%	8.0%	54,937	109,874	45,292	99,796	\$2.49	\$285
Orange County	157,163,686	265,361	17.2%	13.3%	2,279,337	3,993,772	1,009,338	2,541,129	\$2.68	\$192

* RBA includes industrial buildings of all sizes. Rents reflect buildings of at least 10,000 square feet.

LEASING TRENDS

The market's supply and demand shift is highlighted by the last five quarters, with completed construction adding a total of 1,094,070 square feet to the market. However, the net absorption during the same period has been well under that, totaling a negative 1,942,210 square feet as of Q2 2023. This indicates a significant disparity between the demand and supply of newly constructed office.



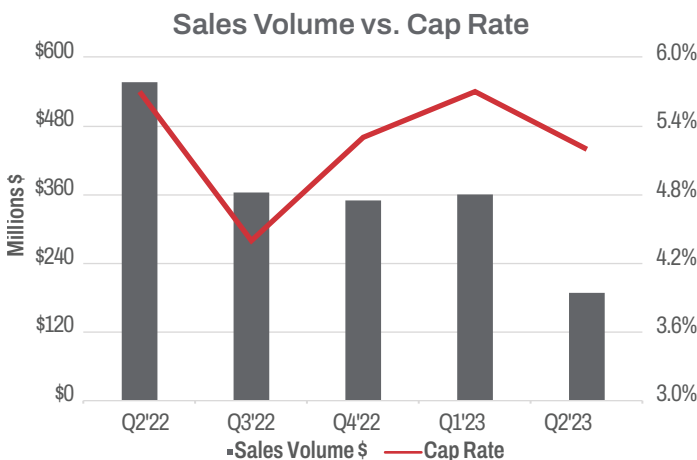
Select Lease Transactions

Address	City	Submarket	Square Feet
15515 Sand Canyon Ave	Irvine	Airport	119,115
10600 Valley View St	Cypress	West	91,506*
200 W Santa Ana Blvd	Santa Ana	Central	81,882*
17800 Laguna Canyon Rd	Irvine	Airport	55,667
3 MacArthur Pl	Santa Ana	Central	43,306

*Renewal

SALES TRENDS

The last five quarters highlight the downward trend in sales volume as the impact of rising interest rates was felt. By midyear 2023, the sales volume ended approximately 33.9% percent below Q2 2022, amounting to approximately \$549 million year to date. Additionally, the average cap rate on investment sales decreased by 50 basis points from the first quarter of 2023, reaching 5.2 percent.



Select Sales Transactions

Address	City	Submarket	Square Feet
5 Hutton Centre Dr (Portfolio of 2 Office Properties)	Santa Ana	Central	560,163
201 E Sandpointe Ave (Portfolio of 3 Office Properties)	Santa Ana	Central	417,061
625 The City Dr S	Orange	North	150,161
17900 Von Karman Ave	Irvine	Airport	70,964
23041 Avenida de la Carlota	Laguna Hills	South	67,587