MARKET REPORT

Office

Los Angeles Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

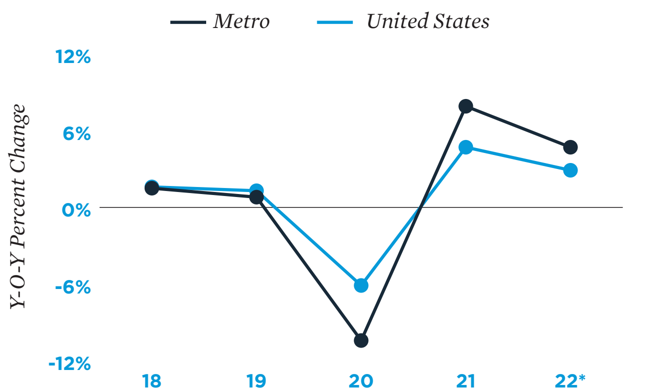
2Q/22

Tides Shift Positively in Silicon Beach, Yet Outlook for Office Sector Remains Foggy

Market recovery hits some roadblocks. After recording positive net absorption in each of the last three quarters of 2021, Los Angeles County's office market encountered a setback during the initial months of this year. Signaling an extended transitional period, vacant stock expanded by nearly 2.6 million square feet during the first quarter of 2022. This increase placed vacancy at a record mark, with availability historically high across property tiers. Additional upward pressure is expected in the near term as tenants continue to evaluate their space requirements amid longer-term adoption of hybrid and remote work models. Nevertheless, a positive has emerged for most locales. Apart from West Los Angeles, submarkets are slated to add an average of just 200,000 square feet this year, a boon for properties with vacant floor plans and available sublease space.

Tech hub outperforms. Housing one-fifth of the county's office inventory, West Los Angeles was the only submarket with more than 40 million square feet of stock to record vacancy compression over the past year ended in March. During the stretch, a tenant mix that included tech and entertainment-centric firms absorbed a net of roughly 1.5 million square feet, most of which was Class A space. User demand for mid- and larger- sized floor plans is apparent as the submarket accounted for more than half the 50,000-square-foot-plus executions inked countywide over the past year. Still, potential near-term headwinds loom. As of May, three-fourths of the 2.5 million square feet slated for 2022 finalization here was available.

Employment Trends



* Forecast

Sources: BLS; CoStar Group, Inc.

Office 2022 Outlook

210,000 JOBS *will be created*

EMPLOYMENT:

Hiring by traditionally office-using firms accounted for one-fourth of all positions added during the first four months of 2022. Continued hiring by these companies will play a role in the metro recording a 4.7 percent annual rate of employment growth.

3,630,000 SQ. FT. *will be completed*

CONSTRUCTION:

Developers finalize more than 3.5 million square feet for a second consecutive year. Still, the county's office inventory expands by less than 1.0 percent, with nearly two-thirds of the space slated for completion unaccounted for as of May.

100 BASIS POINT *increase in vacancy*

VACANCY:

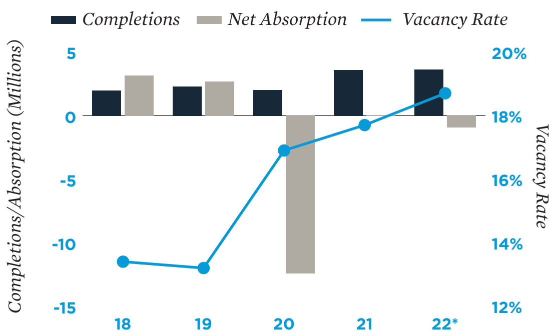
Metro vacancy reaches 18.7 percent this year as supply-side pressure and companies reevaluating their long-term space needs increase the metro's vacant stock. Availability is likely to hover above the metro average in Greater Downtown Los Angeles.

2.0% INCREASE *in asking rent*

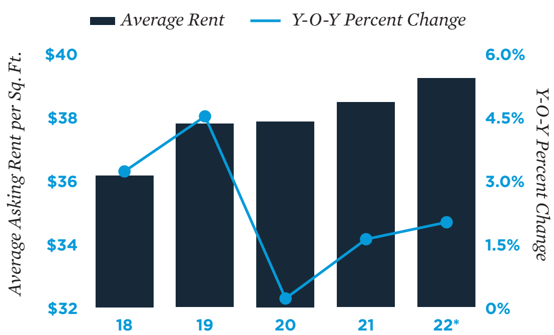
RENT:

The county's marketed rent rises for an 11th straight year to a mean of $39.20 per square foot. A record-high asking rent is established in 2022, despite vacancy reaching a level more than 400 basis points above the long-term average.

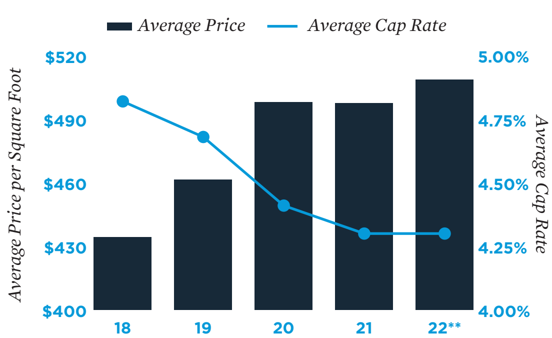
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 1Q*

Sources: CoStar Group, Inc.; Real Capital Analytics

1Q 2022 - 12-Month Period

CONSTRUCTION

4,124,000 sq. ft. completed

- Driven by completions in West Los Angeles and Mid-Wilshire, the county's office stock grew by 1.1 percent over the 12-month period ended in March.
- As of May, ongoing projects in West Los Angeles and Burbank-Glendale-Pasadena accounted for nearly 75 percent of the metro's active pipeline, which comprised more than 4.1 million square feet.

VACANCY

70 basis point increase in vacancy Y-O-Y

- Supply additions outpaced positive absorption during the past four quarters, lifting the county's vacancy rate to 18.3 percent. The Class A sector noted the largest increase in availability at 110 basis points.
- Apart from West Los Angeles, vacancy increased by 70 to 170 basis points in all submarkets with at least 40 million square feet of space.

RENT

1.9% increase in the average asking rent Y-O-Y

- The Class A and Class B/C segments each registered rent growth of roughly 2.0 percent during the recent yearlong span, elevating Los Angeles' overall marketed rate to an average of $38.79 per square foot.
- Home to the lowest vacancy among locales with at least 20 million square feet of stock, the San Gabriel Valley noted a 6.9 percent rise in asking rents.

Investment Highlights

- Trading outside of Greater Downtown Los Angeles accounted for the bulk of sales velocity during the 12-month span ended in March, a period that notched a 45 percent improvement in yearlong deal flow. Sales activity notably increased across price tranches, reflecting diverse buyer demand for available listings. Following pricing adjustments during the initial quarters of the health crisis, the county's average sales price rose 2 percent to $509 per square foot, with the mean cap rate falling slightly to 4.3 percent.
- West Los Angeles and office-heavy locales of South Bay are target destinations for buyers seeking creative spaces. First-year returns typically fall in the 4 percent range in both locales. However, pricing varies greatly, with most Class B assets trading above $800 per square foot in Silicon Beach.
- Medical office transactions have been equally dispersed throughout the metro, with yields rarely exceeding the low-5 percent band. In South Bay and San Gabriel Valley, sub-$400 per square foot pricing remains common.
- Private buyers seeking 5 percent to high-6 percent returns are pursuing traditional office assets in suburban hubs. Burbank-Glendale-Pasadena is gaining in appeal, following recent local Class B/C vacancy compression.

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Price: $250