

LOS ANGELES OFFICE MARKET

THIRD QUARTER 2016

Office rental rates increase again in the second half of 2016

Overall fundamentals remain positive, but caution has returned to the market

In the third quarter, the Los Angeles office market reported increased average rental rates for the fourteenth consecutive quarter. Despite concerns of weaker growth overseas, the Los Angeles regional economy continues to grow. As a result, office market fundamentals remain positive with positive net absorption, elevated levels of new construction, and solid investment sales activity. Looking into year-end, expect several blockbuster transactions as well as a few long-awaited large occupier move-ins as the Los Angeles office market remains a bright spot nationally despite a local vacancy rate in the mid-teens.

ECONOMY




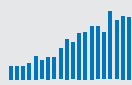


Year-over-year office-using employment growth continues to outpace the nation

The seasonally adjusted unemployment rate for Los Angeles County remained at 4.9% in August, which continues to be the lowest unemployment rate seen in the region since early 2007. However, total year-over-year nonfarm employment increased by just 73,900 (1.7%) while office-using employment increased by 31,000 (2.6%), respectively. Although the area unemployment remains lower than the overall California unemployment rate of 5.6% in August, it appears that lower corporate earnings growth, weak overseas growth and, probably most importantly, the combined high cost of housing and doing business have increasingly acted as a drag on local hiring.

SUPPLY AND DEVELOPMENT

Over 3.7 million square feet now underway across the region

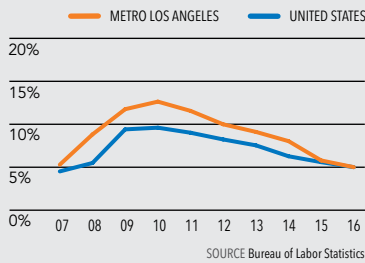
A total of 311,486 square feet was delivered in the third quarter, which brought year-to-date new deliveries to 944,572 square feet. As for office space now under construction, a total of 3.7 million square feet is currently underway, which constitutes 2.0% of the existing Los Angeles office base. In terms of pre-leasing, just 11% of the total office space currently under construction has been pre-leased, which could cause vacancy levels to rise if leasing activity and net absorption slow over the next 12 months.

| TRENDLINES | |
|--------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------|
| 5-YEAR TREND | CURRENT QUARTER |
| VACANCY  | 15.3% Vacancy rate down 10 basis points |
| ABSORPTION  | 357,206 SF 14 straight quarters of positive absorption |
| RENTAL RATE  | \$3.17 PSF Rates up 7.1% year over year |
| UNDER CONSTRUCTION  | 3,726,773 SF Just 11% of office space is pre-leased |
| CAP RATES  | 5.5% Cap rates tick up 10 basis points |
| JOB GROWTH  | 73,900 jobs Growth of just 1.7% year over year |

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UNEMPLOYMENT RATE

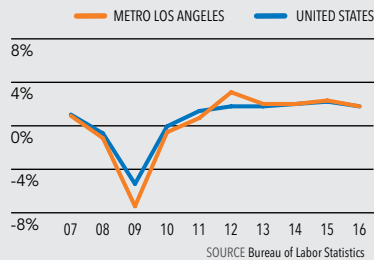


DEMAND

Net absorption positive for the fourteenth consecutive quarter

Demand for office space in the third quarter was 357,206 square feet, which brought total year-to-date net absorption to 974,909 square feet. Compared to net absorption reported in the first nine months of 2015 of over 1.9 million square feet, 2016 net absorption has decreased by almost 50%. This has been due to rising average rental rates all over the region, as well as local companies becoming more cautious about expanding and leasing space for future growth amid mixed economic data.

PAYROLL JOB GROWTH

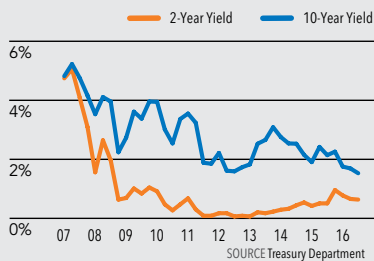


VACANCY

Total vacancy rate ticks down 10 basis points to 15.3%

The total vacancy rate of 15.3% was an additional 10 basis point decrease from a revised total vacancy of 15.4% in the second quarter. While nearly eight million square feet of vacant office space has been absorbed over the past two years, vacancy levels have not decreased by a higher amount due to the large amount of office space that has been completed and delivered to the market. In addition, the long-term industry trend of most office occupiers now utilizing their spaces more efficiently continues to keep vacancy levels stubbornly high region-wide.

TREASURY RATES



RENTAL RATES

Direct weighted average asking rental rate up 7.1% year over year

The direct weighted average asking rental rate increased to \$3.17 per square foot per month (up 7.1% year over year), which remains higher than when the office market last peaked at \$2.92 per square foot in the third quarter 2008. Office landlords all over the region have raised asking rents while still offering aggressive landlord concessions such as free rent and tenant improvement allowances on new leases in order to capture new tenants at the top of the market. Expect office rental rate growth to continue to grow through the end of 2016, although this growth is expected to slow moving into 2017.

Metro Los Angeles Office Market Indicators

| PROPERTY CLASS | INVENTORY | UNDER CONSTRUCTION | Q3 NET ABSORPTION | YTD NET ABSORPTION | DIRECT VACANCY | SUBLEASE SPACE | TOTAL VACANCY | AVERAGE RATE PSF |
|-----------------------|--------------------|--------------------|-------------------|--------------------|----------------|----------------|---------------|------------------|
| Class A | 123,619,633 | 2,358,697 | 477,661 | 1,542,486 | 14.0% | 0.7% | 14.7% | \$3.52 |
| Class B | 65,841,790 | 1,368,076 | -120,455 | -567,577 | 16.1% | 0.4% | 16.5% | \$2.58 |
| LA Metro Total | 189,461,423 | 3,726,773 | 357,206 | 974,909 | 14.7% | 0.6% | 15.3% | \$3.17 |



INVESTMENT MARKET

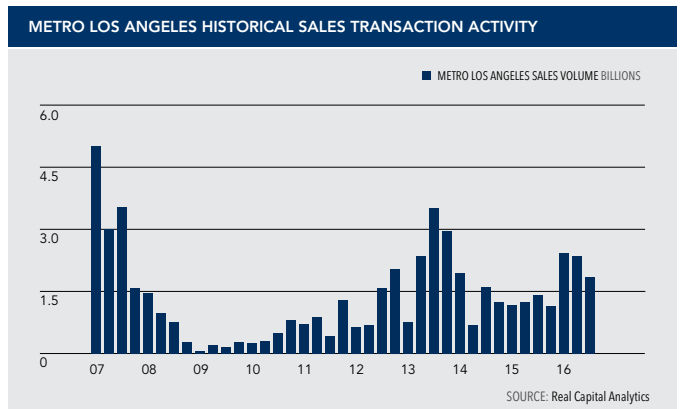
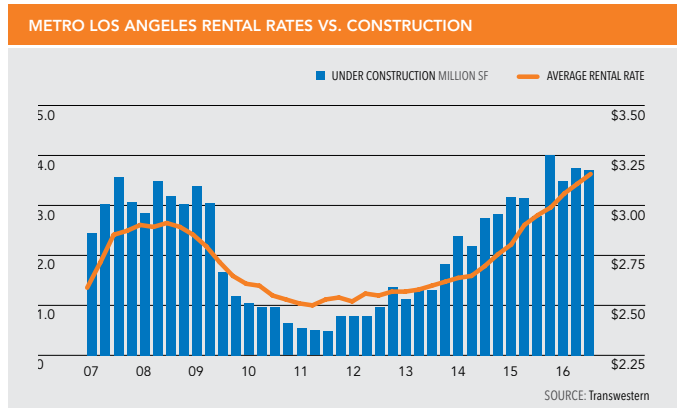
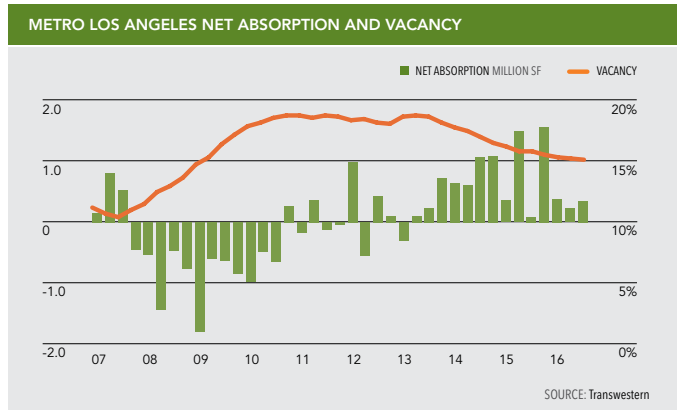
Investment sales market takes a breather before surge in trades before year-end

A total of \$1.9 billion worth of office buildings traded in the third quarter, which brought the 2016 year-to-date total up to \$6.7 billion (up 77% compared to the first nine months of 2015). As mentioned in previous reports, the office sales market in Los Angeles remains red-hot this late in the cycle as regional, national and increasingly international buyers continue to seek high quality trophy assets in high-barrier-to-entry submarkets. At the same time, local value-add investors remain focused on finding well-located properties that can be repositioned to creative office for the region’s growing entertainment, media and technology sector. While the third quarter has definitely seen a slowdown in sales volume compared to the previous two quarters, expect the fourth quarter 2016 and the first quarter 2017 to see several blockbuster trades around the region at historically high pricing as buyers still need to deploy capital and interest rates remain historically low.

OUTLOOK

Office market fundamentals steady but caution has come back to the market

As mentioned in previous reports, the Los Angeles office market continues to report healthy underlying fundamentals that have led to record average rental rates and sales prices. Overall, the market remains healthy, but caution has slowly crept back this year as occupiers are mostly leasing space they need while buyers and lenders have taken a much closer look at their acquisition underwriting assumptions considering where we are at in the current business cycle. While nobody is forecasting a recession over the immediate horizon, continued concern over a hard landing in China’s economy, post-Brexit uncertainty in Europe and the normal anxiety over the upcoming US presidential election will continue to feed caution as market players re-adjust to a leasing and investment market very different from a year ago. ■



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Metro Los Angeles Office Market Indicators

| MARKET | INVENTORY | UNDER CONSTRUCTION | Q3 NET ABSORPTION | YTD NET ABSORPTION | DIRECT VACANCY | SUBLEASE SPACE | TOTAL VACANCY | AVERAGE RATE PSF |
|-------------------------------|--------------------|--------------------|-------------------|--------------------|----------------|----------------|---------------|------------------|
| Downtown Los Angeles | 32,136,841 | 1,334,248 | -13,102 | 52,359 | 17.9% | 0.5% | 18.4% | \$3.16 |
| Wilshire Corridor/Hollywood | 17,315,760 | 668,300 | 44,992 | 241,537 | 17.8% | 0.2% | 18.0% | \$3.04 |
| West Los Angeles | 50,466,349 | 1,236,101 | -149,424 | 35,614 | 11.0% | 1.1% | 12.1% | \$4.63 |
| Tri-Cities | 19,861,024 | - | 58,112 | 299,305 | 13.6% | 0.2% | 13.7% | \$3.25 |
| San Fernando Valley | 18,392,374 | - | 100,087 | 159,167 | 14.7% | 0.1% | 14.8% | \$2.50 |
| South Bay | 27,681,874 | 410,874 | 259,615 | 310,707 | 17.1% | 0.6% | 17.7% | \$2.31 |
| San Gabriel Valley | 9,282,447 | 77,250 | 61,351 | 175,810 | 14.3% | 0.2% | 14.5% | \$2.12 |
| Conejo Valley | 7,950,345 | - | 22,257 | -271,283 | 16.8% | 0.6% | 17.3% | \$2.49 |
| Santa Clarita Valley | 1,999,139 | - | -3,115 | 14,258 | 12.4% | 0.6% | 13.0% | \$2.34 |
| Mid-Cities/Southeast LA | 4,375,270 | - | -23,567 | -42,565 | 9.9% | 1.3% | 11.2% | \$2.14 |
| LA Office Market Total | 189,461,423 | 3,726,773 | 357,206 | 974,909 | 14.7% | 0.6% | 15.3% | \$3.17 |

MAJOR LEASE ACTIVITY

| PROPERTY | TENANT | SF | TYPE | MARKET | SUBMARKET |
|-----------------------------|----------------------------------|--------|-------------------|--------------------|--------------|
| 1620 26th St | Oracle | 92,350 | Class A Expansion | West Los Angeles | Santa Monica |
| 12851 Crossroads Pkwy South | County of LA | 77,250 | Class B New Lease | San Gabriel Valley | Eastern SGV |
| 3100 W Lomita Ave | Torrance Memorial Medical Center | 60,146 | Class B Renewal | South Bay | Torrance |
| 2383 Utah Ave | Kite Pharma | 60,000 | Class B New Lease | South Bay | El Segundo |

MAJOR SALES ACTIVITY

| PROPERTY | PRICE | PRICE PSF | BUYER | MARKET | SUBMARKET |
|-----------------------------------------|---------------|-----------|---------------------------|------------------|----------------------------|
| Colorado Center (6 bldgs) - 49.8% stake | \$511,100,000 | \$866 | Boston Properties | West Los Angeles | Santa Monica |
| 11601 Wilshire Blvd | \$311,000,000 | \$621 | Hudson Pacific Properties | West Los Angeles | Brentwood |
| 12100 Wilshire Blvd | \$225,000,000 | \$616 | Douglas Emmett & QIA | West Los Angeles | Brentwood |
| 12777 W Jefferson Blvd | \$165,000,000 | \$843 | Rockwood Capital | West Los Angeles | Marina Del Rey/Playa Vista |

DEVELOPMENT ACTIVITY

| PROPERTY | SF | TYPE | DEVELOPER | MARKET | SUBMARKET |
|------------------------------------------------|---------|---------|---------------------------|-----------------------------|----------------------------|
| Icon & CUE at Sunset Bronson Studios (2 bldgs) | 419,326 | Class A | Hudson Pacific Properties | Wilshire Corridor/Hollywood | Hollywood |
| 12105 & 12126 W Waterfront Dr (2 bldgs) | 415,987 | Class A | Tishman Speyer | West Los Angeles | Marina Del Rey/Playa Vista |
| Wilshire Grand Tower (Office component) | 356,141 | Class A | Korean Air (Hanjin Group) | Downtown Los Angeles | Financial Core |
| 5800 Bristol Pkwy | 281,400 | Class A | IDS Real Estate Group | West Los Angeles | Culver City |

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METHODOLOGY

The information in this report is the result of a compilation of information on office properties located in the Los Angeles metropolitan area. This report includes single-tenant and multi-tenant office properties 10,000 SF and larger, excluding condo and medical office facilities and those properties owned and occupied by a government agency.



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