

# OFFICE MARKET TRENDS

## Orange County

SECOND QUARTER 2008

### Class-A Vacancies Nearly Double As Pain Spreads

More Orange County office space continues to come on the market as the flagging economy – triggered by the troubled real estate and financial sector and exacerbated by sharp increases in energy costs – is producing a ripple effect on employment, particularly in the manufacturing, information and professional business services, retail, leisure and hospitality industries.

This has served to push the overall vacancy rate at the end of the first half of 2008 up to almost 13%, with 19% for Class A and 13% for Class B office space. A total of approximately 4 million square feet came on the market from newly completed projects and give-back space from downsizing tenants. This represents a major swing from the same period last year when the overall vacancy rate was 8.4%, 9.8% for Class A and 8.8% for Class B.

Orange County economists at Chapman University and California State University at Fullerton are split on whether the county's economy has slipped into a recession. They are projecting a loss of 18,000 to 24,000 jobs respectively this year and are forecasting a mild recovery in 2009.

Nevertheless, in this type of moribund economy in which there is business contraction, every landlord is affected. The only movement occurs when companies

consolidate, shut down their operations or a tenant relocates from one space to another.

So far, building owners have been dealing with rising vacancies by offering free rent and generous tenant improvement allowances that in many cases are so large that they serve to dramatically reduce the effective rent. This way, landlords are able to show higher rents that still meet their pro formas.

*"...with more job losses expected in the second half of the year and an economy growing weaker, competition for tenants will intensify."*

But with more job losses expected in the second half of the year and an economy growing weaker, competition for tenants will intensify. Even though the quoted lease

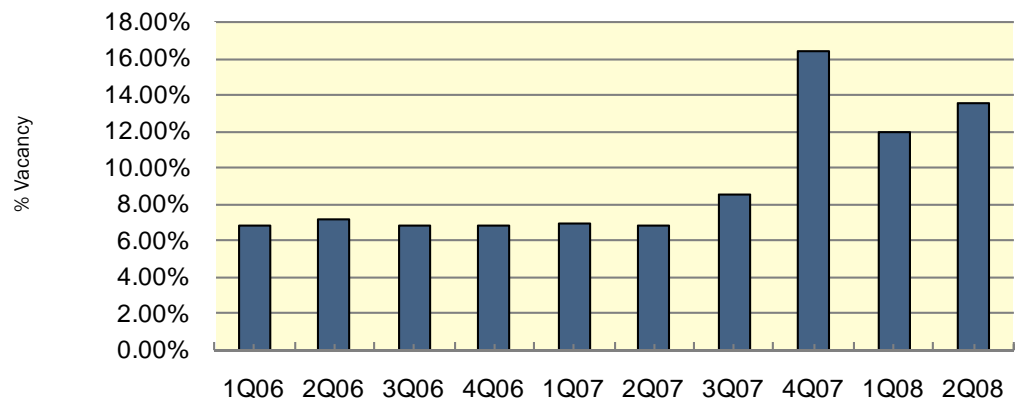
rates on Class A space only have fallen countywide about 2% since the first quarter, some landlords in the Airport, Central and South Orange County – markets with the highest vacancies – are severely reducing effective rents by as much as 25%. Additionally, they are signing short-term leases in efforts to capture tenants now while looking ahead to higher lease rates at renewal time. Quoted and effective rents still have not fallen to the extent they did in the recession of the early 1990s or the recession of 2002.

The one bright spot for building owners is that after this year there is no new office inventory in the construction pipeline. More than half of the 1.7 million square feet of new office construction slated for this year already has been delivered.

#### 2ND QUARTER INDICATORS

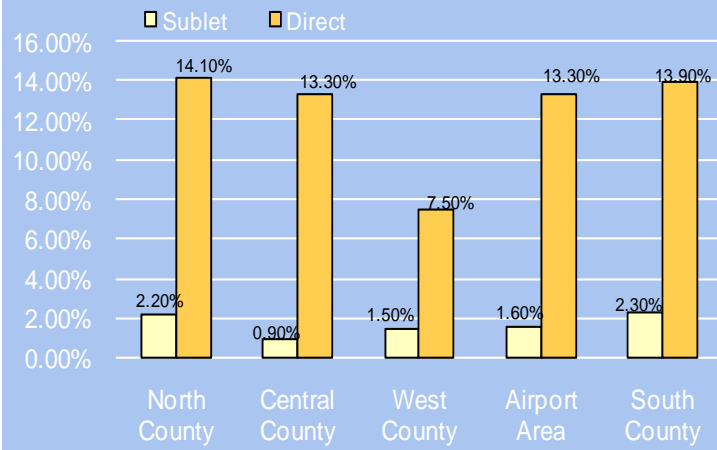
Orange County	2nd Qtr.	Change from last Qtr.
Vacancy	12.68%	↑
Net Absorption	-474,425 SF	↑
Avg. Lease Rate	\$2.53 FSG	↔

#### VACANCY RATE



# OFFICE MARKET REPORT

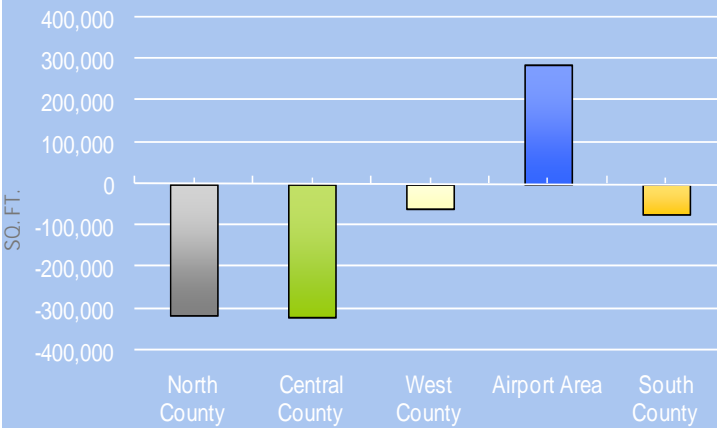
VACANCY BY SUBMARKET  
(DIRECT SPACE VS SUBLET SPACE)



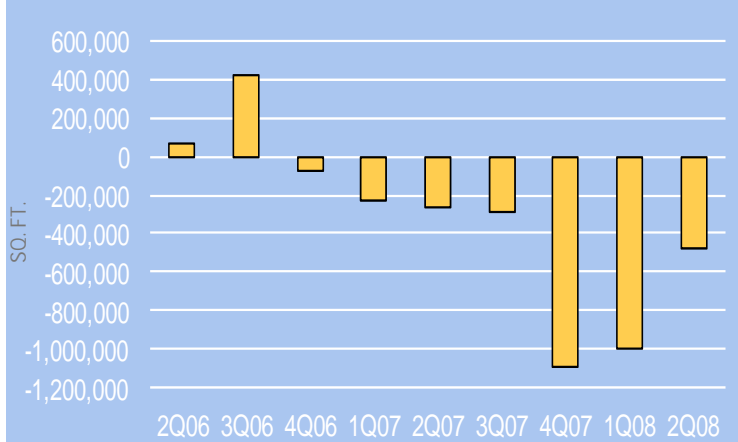
SECOND QUARTER NET ABSORPTION BY  
SUBMARKET & CLASS



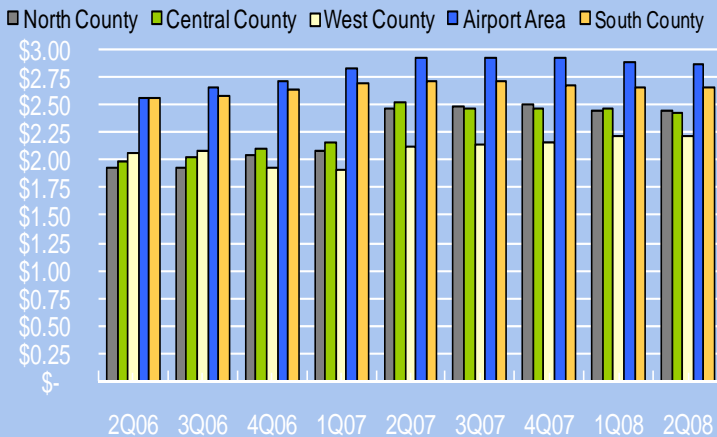
SECOND QUARTER NET ABSORPTION  
(BY SUBMARKET, INCLUDING SUBLET SPACE)



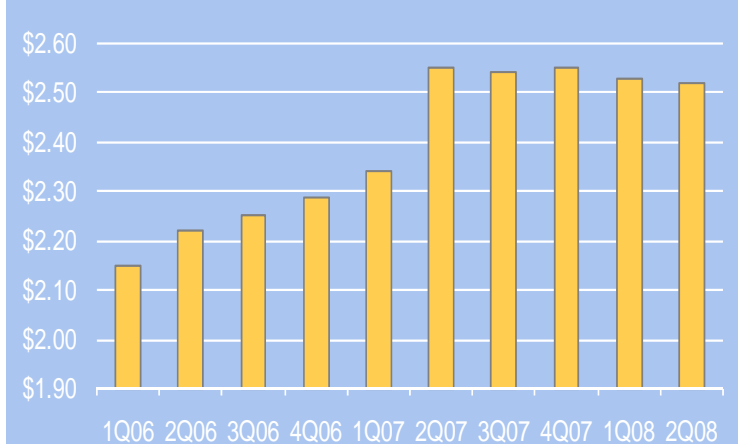
COUNTY-WIDE NET ABSORPTION  
(BY QUARTER, INCLUDING SUBLET SPACE)



YTD LEASE RATES FOR SUBMARKETS  
(NOT INCLUDING SUBLET SPACE)



AVERAGE OC QUARTERLY LEASE RATES  
(NOT INCLUDING SUBLET SPACE)



# M ARKET FORECAST

The increasingly competitive Orange County office market offers tenants with expiring leases major opportunities to relocate and cut costs. Additionally, companies in Class B space should be able to secure suites in many of the county's premium amenity-rich buildings at slight increases over what they're currently paying without long-term commitments.

## RECENT LEE TRANSACTIONS

2001 E. 4th Street



20,840 SF | Sale | Santa Ana  
P. Fridd | J. Hatzis | C. Latta

1507 Yale



17,544 SF | Sale | Orange  
J. Fabiano

2929 Imperial Hwy.



18,906 SF | Lease | Brea  
M. Hintergardt

24532 Del Prado



4,316 SF | Sale | Dana Point  
D. Romero

222 South Harbor



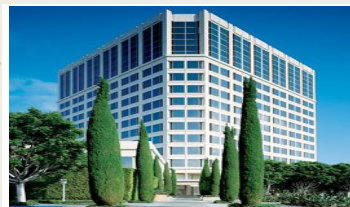
5,756 SF | Lease | Anaheim  
C. Clark

2211 Michelson



8,744 SF | Lease | Irvine  
D. Whitney

8105 Irvine Center Dr., #200



36,519 SF | Lease | Irvine Spectrum  
P. Cohen

1507 W. Yale Street



17,544 SF | Sale | Orange  
K. Johnson

3 Park Plaza, Suite 770



19,913 SF | Lease | Irvine Spectrum  
R. Mason

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As a group of independently owned and operated companies, Lee & Associates currently has more than 33 offices in California, Arizona, Nevada, Michigan, Missouri, Idaho, Illinois, Texas and Wisconsin.

With a broad array of regional, national and international clients—ranging from individual investors and small businesses, to large corporations and institutions—Lee & Associates has successfully completed transactions with a total value of nearly \$4 billion last year, alone.

**Office Brokerage Services**

The firm’s office brokers negotiate various transactions, including mid- and high-rise properties, business and office parks, mixed-used projects, office land for development, multi-tenant buildings and commercial investments. Our brokers analyze the financial arrangements to streamline transactions, and use innovative marketing efforts and unique transaction structuring to provide creative solutions to meet the client’s needs.

Our comprehensive service line includes owner and tenant leasing, acquisition and sales, along with marketing and consulting capabilities. We focus on strategic counseling, rather than merely the transaction, in order to execute the best possible real estate strategies for our clients. This includes building strong relationships within the brokerage community overall. As a result, our clients are assured of the broadest exposure possible.

**MARKET DEFINITIONS**

**Average Asking Lease Rate:** The rate determined by multiplying the lease rate for each building in the summary by its associated available space, summing the products then dividing by the sum of the available spaces with gross lease rates for all buildings in the summary. Direct leases only; excludes sublease space and parking charges.

**Full Service Gross (FSG):** Lease type whereby the landlord assumes responsibility for all the operating expenses and taxes for the property.

**Inventory:** Office inventory includes all multi-tenant and single tenant buildings at least 20,000 square feet. Owner-occupied, government, medical buildings are not included.

**Occupied Square Feet:** NRA not considered vacant.

**Vacancy Rate:** The percentage of the total amount of physically vacant space divided by the total amount of existing inventory.

**Gross Absorption:** The total amount of space leased or sold in a specified period of time.

**Net Absorption:** The change in total occupied square feet from one period to the next. Positive absorption is reflected when a lease is signed, which may not coincide with the date of occupancy.

**Net Rentable Area (NRA):** The gross building square footage minus the elevator core, pipe shafts, vertical ducts, balconies and stairwell areas.

**Vacancy Rate:** Vacant square feet divided by the NRA.

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