

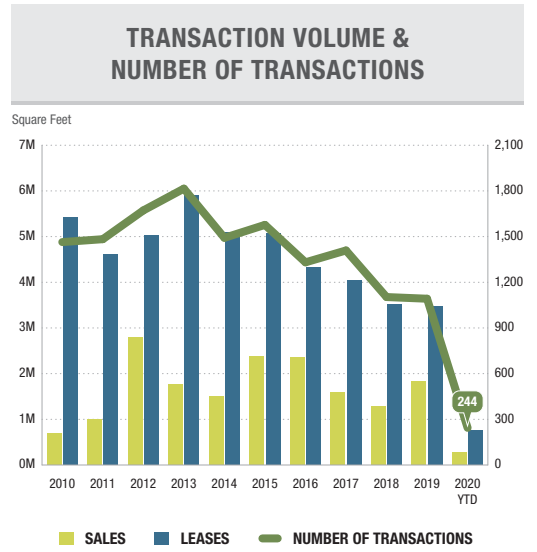
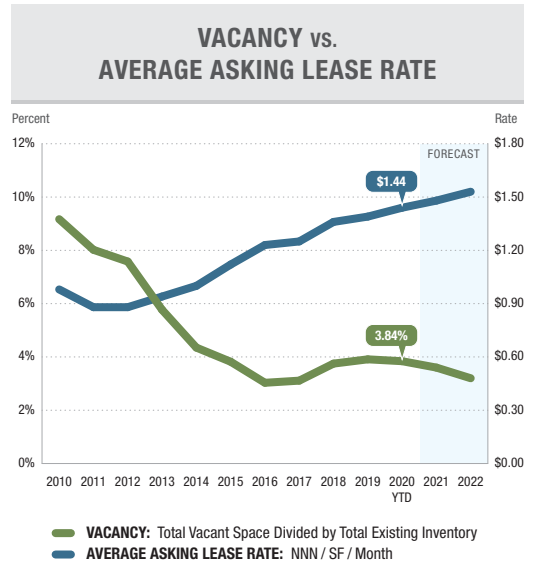
**OVERVIEW.** In our report for the final quarter of 2019, we signaled a possible slowdown in the R&D/flex market. Vacancy rose, net absorption turned negative and rent growth was flat. The first quarter's performance confirmed our suspicions, as the market showed further signs of a loss in momentum. Transaction velocity slowed substantially and net absorption remained in negative territory. The Airport and South County submarkets are seeing the bulk of the activity and rent growth, as has been the case throughout the recovery period. That came to an abrupt halt in mid-March due to Governor Newsom's stay-at-home order precipitated by the COVID-19 virus outbreak. Our prediction that rent growth and leasing activity would pick back up in the first half of 2020 is no longer likely. Fortunately, there is very little new construction and the market is not overbuilt. So, as long as the general economy starts back up in earnest heading into the third quarter, the R&D/flex market may not sustain significant damage.

**VACANCY.** The overall vacancy rate actually fell by 7 basis points in the first quarter, but that was mainly due to a few transactions concentrated in the City of Irvine. Small shifts in the rate are to be expected due to the timing of move-ins and move-outs. Going forward we are looking for vacancy to move higher, though there is not enough data to forecast just how much more we will see. In the final few weeks of the period, tenants and buyers tapped the brakes on new commitments to give themselves time to assess the higher market risk associated with the economic slowdown. Fortunately, just 3.84% of the base inventory is vacant. So, starting from a position of tight supply will help insulate the R&D market from significant damage.

**LEASE RATES.** The average asking lease rate moved higher during the first quarter to \$1.44 but relying on averages in this product type can be unreliable, because there is such a big gap from one submarket to the next. In the Airport area, asking rates range from a high of \$1.62 in Costa Mesa to a low of just \$.98 in Santa Ana. However, in the South County market, rents city-by-city are more homogenous, ranging from a high of \$1.57 in the Irvine Spectrum to a low of \$1.30 in Lake Forest.

**TRANSACTION ACTIVITY.** Overall sale and lease activity took a step back in the first quarter, ending the period at 1,023,119 square feet as compared with 1,251,331 square feet in the previous quarter. 2019 was a very strong year for sale transactions, but just one transaction larger than 40,000 square feet closed escrow in the 1st quarter, a 169,000-square-foot investment sale in Anaheim to Meadow Creek Group, LLC, who acquired the property for \$33.5 million. We can expect sale activity to be light in the second quarter due to pricing uncertainty resulting from the recent economic shock. A bright spot for the quarter was the 186,741-square-foot lease signed by up-and-coming electric truck maker Rivian. The property on Myford Road in Irvine is owned by Meggit PLC.

**EMPLOYMENT.** In February, the nation had 5.79 million jobless and a 3.5% unemployment rate. The national jobless claims recently filed totaled 9.96 million (compared with 11.31 million filings overall in the previous 52 weeks), and if every new claimant was added to the jobless count, then the unemployment rate soars to 9.5%. The second quarter should see more increases, as the economic impact of the response to the virus is in the early stages. Most sectors are being hit very hard. We know the impact of job losses will move the needle on all R&D/Flex market metrics, but it's just too early to tell how much. Fortunately, many of the users who occupy R&D/Flex space are focused on technology or financial services, which allows many workers the opportunity to remain productive working from home.

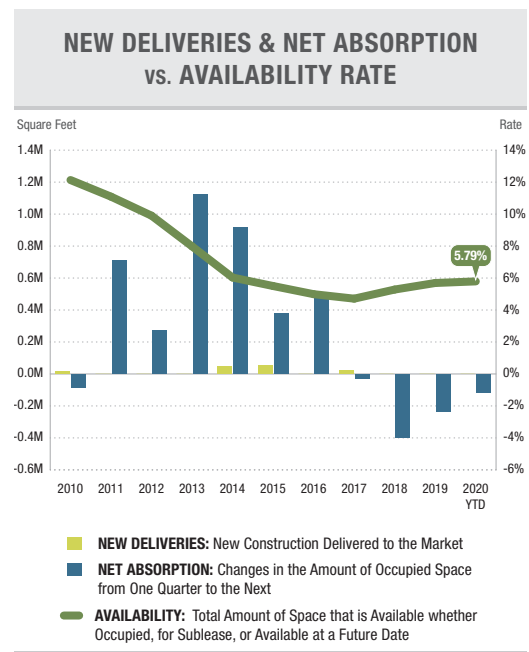


Market Statistics

	Change Over Last Quarter	1Q 2020	4Q 2019	1Q 2019	% Change Over Last Year
Vacancy Rate	▼ DOWN	3.84%	3.91%	3.66%	4.92%
Availability Rate	▲ UP	5.79%	5.69%	5.47%	5.85%
Average Asking Lease Rate	▲ UP	\$1.44	\$1.39	\$1.36	5.88%
Sale & Lease Transactions	▼ DOWN	1,023,119	1,251,331	1,210,577	(15.49%)
Gross Absorption	▼ DOWN	844,094	956,016	1,091,983	(22.70%)
Net Absorption	▼ NEGATIVE	(118,184)	(289,607)	(138,344)	N/A

**CONSTRUCTION.** At the end of the first quarter of 2020, only two projects remained under construction in the Orange County R&D/Flex market, totaling 335,942 square feet. The first is the initial phase of the Los Patrones Business Park located in unincorporated Rancho Mission Viejo, composed of three new multi-tenant buildings, totaling 99,200 square feet on 9.36 acres. Scheduled for completion in June, suites ranging from 1,800 to over 3,000 square feet are available. Flexible zoning and building design, along with a generous 4/1,000 parking ratio allow for a wide variety of use types in the project, which has immediate 241 tollway access and is surrounded by more than 4,500 homes. The second project in the construction queue, located in Irvine, is a 235,000-square foot building being built as part of Edwards Life Sciences’ plan to nearly double the size of its Irvine headquarters. According to city records, the project will eventually total approximately 471,000 square feet once all three phases are completed over the next several years. The new facilities will include office, lab, manufacturing, warehouse and other space, bringing the company’s total footprint up to 660,475 square feet on 26 acres.

**ABSORPTION.** Both gross and net absorption pulled back in the first quarter, as we expected, even without the impact of the COVID-19 situation. Gross absorption, which measures the total amount of move-ins, fell to 844,000 square feet compared with 956,000 square feet in the fourth quarter and 1,091,000 on a year-over-year basis. Expect that to decline again in the second quarter as the top five leases signed in the first period added up to just 336,038 square feet, including the Rivian deal. This quarter’s activity becomes absorption in the next two or three quarters. So, we are heading into a slow period without good momentum and an uncertain economy. Net absorption recorded negative 118,184 square feet in the first quarter due to the low vacancy rate and lack of supply of functional product.



Forecast

**OVERALL.** Last quarter we were most concerned about warnings of a global slowdown, concerns over US GDP growth and trade relations between the US and China. But, in the last three months the world has changed, and we are finally able to identify the Black Swan economists have been warning about for years. The COVID-19 virus, first identified in China, has circled the planet in a matter of weeks, causing leaders around the world to take draconian steps to stop it. Entire countries are on lockdown and our own federal and state governments have taken steps similar to our neighbors in Asia and Europe. It’s too early to tell what the exact impact the reaction to the virus will have on the Orange County R&D/Flex market, but we do predict at least a near-term slowdown in sale and lease activity. We should see the statistical evidence of that in the second quarter and third quarter numbers.

**LEASE RATES.** After rents averaged more than 5.2% annual growth over the past five years, that pace has decelerated in the past year. Given that vacancies remain extremely low, this is likely an indication that years of outsized rent gains have pushed costs about as high as the market will bear, especially for product with functional obsolescence or deferred maintenance.

**VACANCY.** Low vacancy will persist throughout the year, though there is a chance it could move up slightly as a result of the COVID-19 disruption. But, with vacancy at just 3.84%, the county could withstand a substantial rise in that rate without significantly disrupting the supply-demand balance. We look for the county’s overall rate to range between 3.50% and 3.75% for the balance of the year.

Significant Transactions

Sales					
Property Address	Submarket	Square Feet	Sale Price	Buyer	Seller
100-396 Cerritos Ave.	Anaheim	168,992	\$33,500,999	Meadow Creek Group, LLC	Anaheim Business Campus, LLC
15 Whatney	Irvine Spectrum	39,696	\$14,800,000	Bernicia Capital	Ampronix
1375 Logan Ave.	Costa Mesa	25,282	\$6,146,000	Gdc Logan, LLC	Young Family Trust
2511 W. 5th St.	Santa Ana	18,288	\$4,969,500	Red Hook Capital Partners, LLC	Templo Calvario, Inc.
1641 McGaw Ave.	Irvine	14,040	\$6,050,000	Golden Triangle Group, LLC	McGaw, LLC

Leases					
Property Address	Submarket	Square Feet	Transaction Date	Tenant	Owner
14600 Myford Rd.	Irvine	186,741	Jan-2020	Rivian	Meggitt PLC
15350 Barrance Pkwy.	Irvine Spectrum	53,392	Jan-2020	Rep 1 Football, LLC	The Irvine Company
20321 Valencia Cir.	Lake Forest	40,934	Jan-2020	Matter Hackers	Valencia Circle, LLC
15 Whatney	Irvine Spectrum	39,696	Jan-2020	Ampronix	Bernicia Capital
9671-9701 Irvine Center Dr.	Irvine Spectrum	15,277	Jan-2020	University Medical Pharmaceuticals Corp.	Winchester Equity Group, LLC





## Battling Target Fixation

by **Seth Davenport**

EXECUTIVE VICE PRESIDENT / PARTNER, IRVINE  
714.935.2376 · sdavenport@voitco.com · Lic. #01413387

The concept of target fixation is well known in racing circles. It's based on the fact that we go where our eyes take us. Car racers are trained to use this instinctive phenomenon to their advantage. They are always looking up the track or through a turn rather than right over the hood. This is what allows them to go so much faster than the rest of us ever could. It's also why us non-racers see debris in our lane and then inexplicably run right over it instead of going around it as we would if we focused on the area to either side of it.

Harnessing target fixation is one of the first skills taught at any driving school. Without it, students drive in a stop-and-go, point-to-point fashion, which makes them reset their target at every entry, apex and exit point. A tracing of their laps looks like one of those connect-the-dots pictures we drew as kids waiting at the dentist's office. A good racer is looking at the apex of the turn before reaching the entry point and then picks up the exit before hitting the apex. This reduces steering inputs and allows the driver to move through the turn faster.

We think the concept of target fixation carries over into business decision-making, as well, and the current virus scare is one heck of a target to fix on. It is debris that, for the moment, lies across our path of travel and most of us have applied the brakes to avoid the unknown danger it presents. That reaction has sent the world's economy into a tizzy and shifted the psychology of decision-making into a defensive posture. Understandable? Of course. The virus crisis is an exogenous shock that no one anticipated and it has become the road hazard we just can't take our eyes off of.

That said, when it comes to commercial real estate, it's probably better to have a racer's eye for the track. Real estate is a long-term investment whether you buy it or lease it. It represents the whole track, whereas market conditions at any instant in time represent a specific point on the track. In this case the corner workers are waving yellow flags, so it only makes sense to roll off the gas and survey the danger.

As you evaluate the implications of this unexpected road hazard, we encourage you to heed the yellow flags, but to keep moving forward. In all likelihood, the virus will run its course and the medical community will develop protection from future outbreaks. Could that mean we run a couple of laps under the yellow caution flag? Yes, but the track will eventually go green again and you don't want to be parked in the pit when it is cleared to go.

We realize that many of you, depending on your industry, will be impacted more than others, but it still makes sense to stay on track in anticipation of a return to full race pace on the next lap. If you were looking to buy, sell or lease real estate before this latest market anomaly, the reasons for that decision will come back around soon. In the meantime, respect the yellow flag and hope you see the green one soon.

### Please Contact Us for Further Information

**Tony Tran**  
Regional Director of Research  
ttran@voitco.com

Anaheim, CA 714.978.7880	Carlsbad, CA 760.517.4000	Inland Empire, CA 909.545.8000	Irvine, CA 949.851.5100	Los Angeles, CA 424.329.7500	San Diego, CA 858.453.0505
-----------------------------	------------------------------	-----------------------------------	----------------------------	---------------------------------	-------------------------------

This survey consists of properties representing both single tenant and multi-tenant buildings. The lease rates are based on a triple-net basis. The information contained in this report is gathered from sources that are deemed reliable, but no guarantees are made as to its accuracy. This information is for Voit Real Estate Services' use only and cannot legally be reproduced without prior written consent from the management of Voit Real Estate Services. ©2020 Voit Real Estate Services, Inc. DRE License #01991785.

Represented in 150 Markets  
Nationally & Internationally.



## Product Type

### R&D OR MID-TECH

30% to 74.9% improved with drop ceiling,  
minimum parking ratio of 3 to 1, minimum  
50% of exterior glassline, dock and/or ground  
level loading.

## Submarkets



### NORTH

Anaheim,  
Brea, Buena Park,  
Fullerton, La Habra,  
Orange, Placentia,  
Yorba Linda

### WEST

Cypress, Garden Grove, Huntington Beach,  
La Palma, Los Alamitos, Stanton, Westminster

### AIRPORT

Costa Mesa, Fountain Valley, Irvine, Newport  
Beach, Santa Ana, Tustin

### SOUTH

Aliso Viejo, Foothill Ranch, Irvine Spectrum,  
Laguna Hills, Laguna Niguel, Lake Forest,  
Mission Viejo, Rancho Santa Margarita,  
San Clemente, San Juan Capistrano