

# Orange County

Office Q3 2023



	YoY Chg	12-Mo. Forecast
<b>19.7%</b> Vacancy Rate	▲	▲
<b>-822.6K</b> Net Absorption, SF	▼	▲
<b>\$2.85</b> Asking Rent, PSF	▼	▼

(Overall, All Property Classes)

## ECONOMIC INDICATORS Q3 2023

	YoY Chg	12-Mo. Forecast
<b>1.7M</b> Orange County Employment	▲	▲
<b>3.3%</b> Orange County Unemployment Rate	▲	▬
<b>3.7%</b> U.S. Unemployment Rate	▲	▲

Source: BLS

## ECONOMIC OVERVIEW

Total nonfarm employment in Orange County (OC) grew by 42,700 or +2.6% year-over-year (YOY) between August 2022 and August 2023. The private education and health services sector accounted for the most gains, or 11,200 jobs added (+4.5% YOY), followed by the leisure and hospitality sector, adding 10,200 jobs (+4.6% YOY) and professional and business services adding 6,200 jobs (+1.9% YOY). During the same time, the monthly unemployment rate increased from 3.2% last year to 3.9% and is currently 60 basis points (bps) above the quarterly average of 3.3%.<sup>1</sup> The recovery from the 272,300 nonfarm job losses experienced between March and May 2020 has been completed, with 296,300 jobs fully recovered between June 2020 and August 2023. All employment sectors are projected to grow at a combined growth rate of 1.9% in 2023 and 1.5% in 2024 compared to the 5-year historical average of 0.5%.<sup>2</sup>

## SUPPLY AND DEMAND

The OC office market continues to face headwinds even three years after the onset of the COVID-19 pandemic. The overall vacancy rate has increased significantly by 930 bps since Q1 2020, reaching 19.7% in Q3 2023. This represents a 110-bps increase quarter-over-quarter (QOQ) and a 450-bps increase YOY. In Q3 2023, tenants vacated slightly under 823,000 square feet (sf), indicating that many tenants are still not fully committed to being “back in the office”. The Irvine Spectrum submarket within South County led occupancy losses at -401,636 sf, largely due to Verizon (-119,115 sf) and Accurate Background (-63,412 sf) vacating, followed by Irvine (-188,815 sf) in the Greater Airport Area. However, two submarkets posted positive absorption in Q3 2023: Costa Mesa (+143,580 sf) in the Greater Airport Area and Civic Center Area (+47,105 sf) in Central County. This positive absorption largely resulted from Anduril Industries moving into the second building of ‘The Press’, and IWG/Regus taking occupancy at 901 W. Civic Center Dr. respectively. Tenants have been actively reassessing their real estate needs over the last three years, although this quarter had the first decrease in available sublease space in the previous six quarters. Overall available sublease space decreased to 3.9 million square feet (msf) this quarter, down 0.1% QOQ but still up 24.2% YOY. When combined with direct available space, 21.7 msf or 23.5% of the entire office inventory in OC is on the market and available for lease. This figure is elevated (+1.8% QOQ and +19.2% YOY) and well above the five-year quarterly average of 14.8 msf of overall availability at 16.4%. Leasing activity in Q3 2023 decreased slightly, with 1.5 msf leased across 337 deals, excluding renewals. This compares to 1.7 msf (390 deals) in Q2 2023 and 1.8 msf (326 deals) in Q3 2022. The Greater Airport Area was the most active major market, accounting for 47.1% or 691,197 sf of leasing activity in Q3 2023 followed by South County (28.6% or 419,624 sf). The three most active submarkets were Irvine (30.1%), Irvine Spectrum (17.1%) and Newport Beach (9.9%). Combined, these submarkets accounted for 57.1% or 837,910 sf of new leases signed in Q3 2023. Class A properties were in high demand, representing 54.3% or 796,398 sf of all new lease deals signed in the quarter. Boot Barn signed the quarter’s largest deal by subleasing 116,261 sf of Alteryx and Kajabi’s vacated space at Spectrum Terrace in South County.

## SPACE DEMAND / DELIVERIES



## OVERALL VACANCY / ASKING RENT



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## PRICING: Asking Rates Hold Tight Despite Heightened Vacancies

Despite increased market vacancies, the average asking rate across all classes has remained stable over the past four years. Landlords have not significantly lowered rental rates but are offering extended free rent periods and higher tenant improvement allowances to stay competitive. The average asking rent fell 0.3% QOQ and 1.0% YOY to \$2.85 per square foot (psf) on a monthly full-service basis. Over the past 12 months, the average Class A asking rent increased by 0.3% to \$3.15 psf, while Class B rent decreased by 2.0% to \$2.44 psf. The minor increase in Class A rent is mainly due to newly vacant spaces listed at higher asking rents. Newly developed Class A projects with modern design and amenities command higher asking rates, ranging from \$4.65 to \$5.65 psf, and are near full occupancy.

## FUTURE INVENTORY: Projects Waiting for Tenants to Commit to Continue

The completion of the second building of 'The Press' in Costa Mesa this quarter marked the end of all current office construction countywide. This project delivered 190,000 sf of Class A space that Anduril Industries occupied, in addition to the 449,206-sf building that was delivered in Q1 2023. The development pipeline has three notable proposed projects: Flight @ Tustin Legacy Phase II in Tustin, Innovation Office Park Phase III in Irvine and Five Lagunas in Laguna Hills. However, due to the state of the market, it is unlikely that these projects will break ground anytime soon without securing tenant commitments first.

Lastly, The Irvine Company announced a proposed 512,000 sf "Lab-Ready Campus" called Academy Point in the latter half of 2022. This development would be the largest life sciences office campus in Orange County, featuring four buildings with 32,000-sf floor plates tailored to accommodate mid-to-large-sized tenants. Currently, there is yet to be a timeline for the project, leading to intense speculation that The Irvine Company is waiting for a tenant commitment before commencing construction.

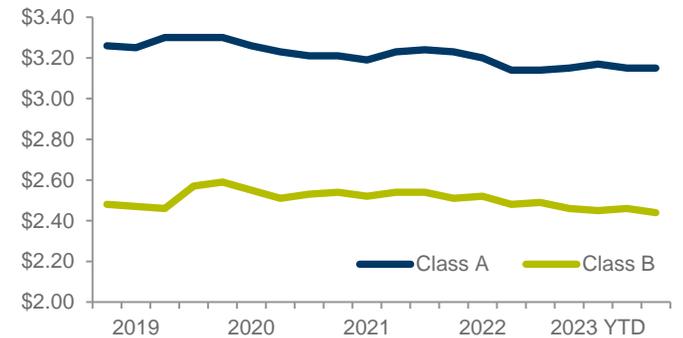
## SALES ACTIVITY: Private Buyers Dominate

The OC office market recorded \$314 million (M) in sales volume (8 properties) in Q3 2023, compared to \$253M (10 properties) in Q2 2023 and \$146M (9 properties) in Q3 2022.<sup>3</sup> This represents an increase of 24.0% QOQ in volume and 115% YOY. The average price psf was \$252 in Q3 2023, increasing 0.4% QOQ yet down 23% YOY. The leading buyers as of Q3 2023 were private investors at 86% (vs. 78% in 2022), followed by institutional at 7% (vs. 15% in 2022) and REITs at 7% (vs. 8% in 2022). Private investors accounted for 52% of sales activity as of Q3 2023 (vs. 68% in 2022), followed by institutional investors at 31% (vs. 28% in 2022) and REITs at 17% (vs. 5% in 2022). Two notable transactions during Q3 2023 were the CANVAS sale in Costa Mesa for \$92M and the Raytheon Campus in Fullerton for \$77M. Private investors acquired both assets.

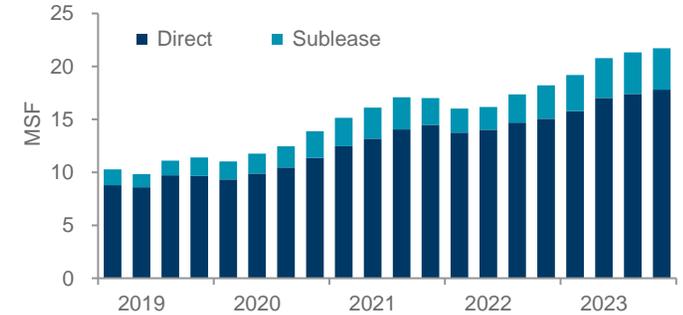
## OUTLOOK

- Landlords will remain firm on asking rents while offering increased concession packages in the form of more months of free rent and higher tenant improvement allowances due to their existing debt commitments.
- Active tenant requirements of all sizes remain robust at 2.4 msf countywide over the next 24 months, led by Blizzard's search for a consolidated campus. While not all current tenants in the market will lease space in the short term, these active requirements indicate future leasing activity in the coming quarters.

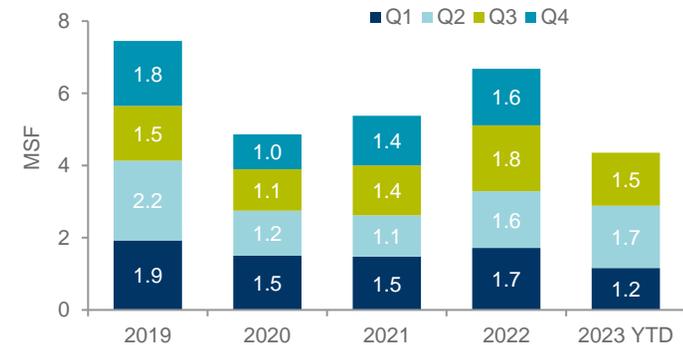
## AVERAGE ASKING RENT \$PSF MONTHLY FULL SERVICE



## DIRECT VS. SUBLEASE AVAILABLE SPACE



## NEW LEASING ACTIVITY



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## MARKET STATISTICS

SUBMARKET	INVENTORY (SF)	DIRECT VACANT (SF)	SUBLET VACANT (SF)	OVERALL VACANCY RATE	CURRENT QTR OVERALL NET ABSORPTION (SF)	YTD OVERALL NET ABSORPTION (SF)	YTD LEASING ACTIVITY ** (SF)	YTD CONSTR COMPLETIONS (SF)	UNDER CNSTR (SF)	OVERALL AVG ASKING RENT (ALL CLASSES)*	OVERALL AVG ASKING RENT (CLASS A)*
Greater Airport Area	40,200,969	7,041,124	945,173	19.9%	-120,732	-509,118	2,130,272	190,000	0	\$3.03	\$3.16
South County	22,315,397	3,689,142	815,496	20.2%	-546,805	-878,952	1,122,428	258,046	0	\$2.91	\$3.31
West County	4,780,422	892,429	49,368	19.7%	-27,143	-231,477	179,074	0	0	\$2.55	\$3.14
Central County	19,293,029	3,639,142	288,176	20.4%	-100,518	-664,990	691,197	0	0	\$2.62	\$2.95
North County	5,719,136	759,056	81,601	14.7%	-27,444	-2,767	229,250	0	0	\$2.33	\$2.69
<b>Class A</b>	<b>44,832,011</b>	<b>9,215,836</b>	<b>1,390,680</b>	<b>23.7%</b>	<b>-299,601</b>	<b>-671,881</b>	<b>2,161,513</b>	<b>448,046</b>	<b>0</b>	<b>\$3.15</b>	
<b>Class B</b>	<b>45,750,976</b>	<b>6,638,643</b>	<b>769,754</b>	<b>16.2%</b>	<b>-523,313</b>	<b>-1,548,606</b>	<b>2,137,489</b>	<b>0</b>	<b>0</b>	<b>\$2.44</b>	
<b>Class C</b>	<b>1,725,966</b>	<b>166,414</b>	<b>19,380</b>	<b>10.8%</b>	<b>272</b>	<b>-66,817</b>	<b>53,219</b>	<b>0</b>	<b>0</b>	<b>\$1.93</b>	
<b>OC TOTALS</b>	<b>92,308,953</b>	<b>16,020,893</b>	<b>2,179,814</b>	<b>19.7%</b>	<b>-822,642</b>	<b>-2,287,304</b>	<b>4,352,221</b>	<b>448,046</b>	<b>0</b>	<b>\$2.85</b>	

\*Rental rates reflect full service asking. \*\*Renewals not included in leasing statistics.

## KEY LEASE TRANSACTIONS Q3 2023

PROPERTY	SUBMARKET	TENANT	SF	TYPE
17100 Laguna Canyon Rd.	Irvine Spectrum	Boot Barn	116,261	Sublease
140 S. State College Blvd.	Brea / La Habra	Burns & McDonnell	50,582	Renewal**
1900 Main St.	Irvine	Zion Bancorporation dba California Bank & Trust	47,228	Renewal**
25510 Commercentre Dr.	Lake Forest / R.S. Margarita	Staar Surgical Company	36,291	New
701 S. Parker St.	Main Place Area	The Word & Brown Insurance Administrators, Inc.	36,060	Renewal**

## KEY SALES TRANSACTIONS Q3 2023

PROPERTY	SUBMARKET	SELLER / BUYER	SF	PRICE / \$ PSF
CANVAS (3070, 3080, 3090, 3100, 3150 Bristol St.)	Costa Mesa	EQ Office (Blackstone) / MGR Real Estate	550,959	\$91.5M / \$166
Raytheon Portfolio (1801 Hughes Dr. – Bldg's 1 & 2)	Fullerton	Hines c/o Oaktree Capital Management / Prime Enterprises	405,130	\$76.5M / \$188
One Pacific Plaza (7711, 7755, 7777 Center Ave.)	Huntington Beach	Pendulum Property Partners / Joe Wen	401,820	\$42.0M / \$105

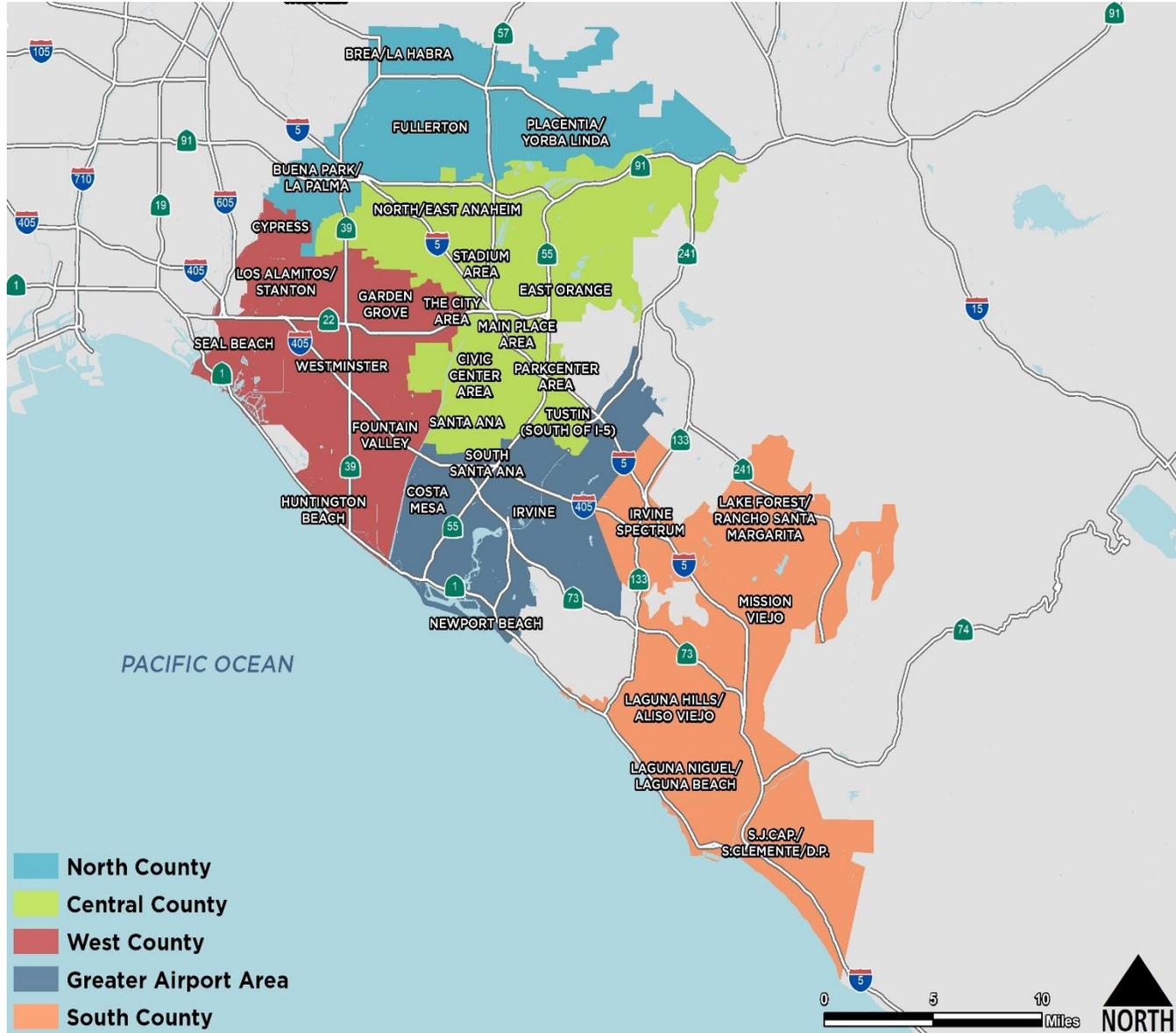
## KEY PROJECTS COMPLETED 2023 YTD

PROPERTY	SUBMARKET	TENANT	SF	OWNER
Innovation Office Park – Ph. II: 200-260 Progress	Irvine Spectrum	N/A	258,194	The Irvine Company
The Press: 1375 Sunflower Dr. – Bldg. 2	Costa Mesa	Anduril Industries	190,000	SteelWave

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OFFICE SUBMARKETS



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