

Inland Empire

Office Market Outlook 2Q 2017

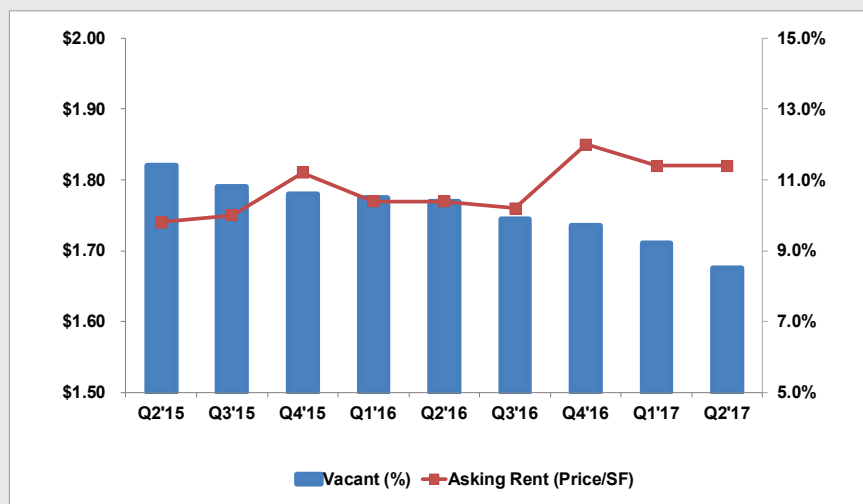
MARKET OVERVIEW

In the second quarter of 2017, the Inland Empire office market has continued to remain strong. The vacancy rate closed the quarter at 8.5%, down 70 basis points from last quarter and 190 basis points below this time last year. This is the lowest vacancy rate since 2007, indicating strong underlying market demand. Average asking rents remained steady at \$1.82/SF over the quarter, but have increased 2.8% from this time last year. Two projects are under construction totaling 39,080 square feet, both of which are medical office. Both of these projects are expected to deliver by the end of Summer 2017. The largest project is 31775 De Portola Road, a medical office building fully leased by Radnet Management, delivering in July. Employment growth continues to be a primary driver of demand for office space. Overall, the unemployment rate for the Inland Empire has fallen from 5.4% to 4.5% from May 2016 to May 2017, with more than 41,000 jobs created. The medical industry continues to be a primary driver of demand for office space in the Inland Empire, with the Education & Health Services sector growing 2.1% from last year and adding 4,400 new jobs.

TRENDS TO WATCH

As occupancy and employment rates continue to increase, developers are becoming more confident in the Inland Empire office market and are moving ahead with several new construction projects. Currently, there are five major projects totaling 661,324 square feet that are expected to break ground later this year, with an additional 1.6 million square feet in the planning or proposal stages of development. The Creekside Corporate Center in Murrieta is the largest project scheduled to begin construction this year. The project is being developed by The Truax Group, Inc. and is expected to deliver 240,966 square feet when complete. As these trends continue, developers will see opportunity in the Inland Empire and be encouraged to move ahead with new projects.

Average Asking Rent and Vacancy Rate



Source: NAI Capital Research, CoStar

MARKET OUTLOOK

Asking Rental Rates



Sale Prices



Availability/Vacancy Rates



Landlord Concessions



Sales/Leasing Volume



New Construction



NAI Capital Research
www.naicapital.com

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Market Statistics

SUBMARKET	EXISTING TOTAL RBA (SF)	UNDER CONSTRUCTION (SF)	TOTAL AVAILABLE (%)	TOTAL VACANCY (%)	2Q17 LEASING VOLUME (SF)	YTD LEASING VOLUME (SF)	2Q17 SALES VOLUME (SF)	YTD SALES VOLUME (SF)	AVERAGE ASKING RENT \$/PSF FSG	AVERAGE SALE PRICE \$/PSF
Airport	13,177,447	4,000	10.5%	7.3%	106,626	227,067	29,001	613,939	\$1.95	\$209
High Desert	5,596,749	0	6.9%	5.1%	16,733	37,096	91,837	146,026	\$1.63	\$173
Riverside	17,034,241	14,080	11.3%	8.8%	171,337	384,530	774,254	944,794	\$1.94	\$155
San Bernardino	14,707,137	0	14.7%	10.9%	123,225	199,144	226,448	340,254	\$1.58	\$184
South	7,589,691	25,000	14.5%	7.9%	115,003	226,013	26,340	148,053	\$1.87	\$114
West	4,090,980	0	9.3%	7.8%	66,130	140,275	31,341	112,490	\$1.86	\$322
Total	62,196,245	43,080	11.8%	8.5%	599,054	1,214,095	1,179,221	2,305,556	\$1.82	\$159

RBA includes office buildings of all sizes and classes. Rents reflect buildings of at least 20,000 square feet.

Leasing

Leasing activity this quarter totaled just under 600,000 square feet, which was a slight decrease of 2.6% over the quarter, and a decrease of 31% over this time last year. This is a result of high average asking rents and a shortage of vacant office space. The vacancy rate has fallen to its lowest point since 2007, and is only 130 basis points above the lowest point on record in 2005. Rising rents indicate that the Inland Empire has improved to the point where new construction is feasible as rents push upward. In one lease transactions this quarter, Innovated Structural Engineering leased 5,330 square feet in Temecula for \$1.75/SF. Similarly, the County of Riverside took down 5,317 square feet at the same business center in Temecula for \$1.60/SF.

Sales

Sales volume held steady over the quarter in the Inland Empire, totaling nearly 1.2 million square feet. However, this level remains 53% higher than last year at this time. Similarly, average sale prices have increased 2.9% over the year to \$159/SF, while cap rates averaged 7.03%. This increase in both total sales activity and average sale prices over the year has been driven primarily due to increasing investor confidence in the Inland Empire office market. In one of the largest sales transactions this quarter, Stillwater Investment Group purchased the 193,738 square foot Towers at Riverwalk in Riverside for \$197/SF from Long Wharf Capital, LLC. Similarly, Crownsnest Properties, LLC purchased the mixed-use Citrus Park, which contains 148,504 square feet of office space alongside 203,939 square feet of industrial space, for \$104/SF from Proficiency Capital.

Significant Lease Transactions

TENANT	ADDRESS	SUBMARKET	ASKING RENT \$/PSF*	SQUARE FEET
Tenant Not Listed	202 E Airport Dr	San Bernardino	\$1.10	29,840
Innovated Structural Engineering	40810 County Center Dr	South	\$1.75	5,330
County of Riverside	40925 County Center Dr	South	\$1.60	5,317
Foster Services	14174 Green Tree Blvd	High Desert	\$1.30	4,455
Oasis MD	27699 Jefferson Ave	South	\$1.95	3,635

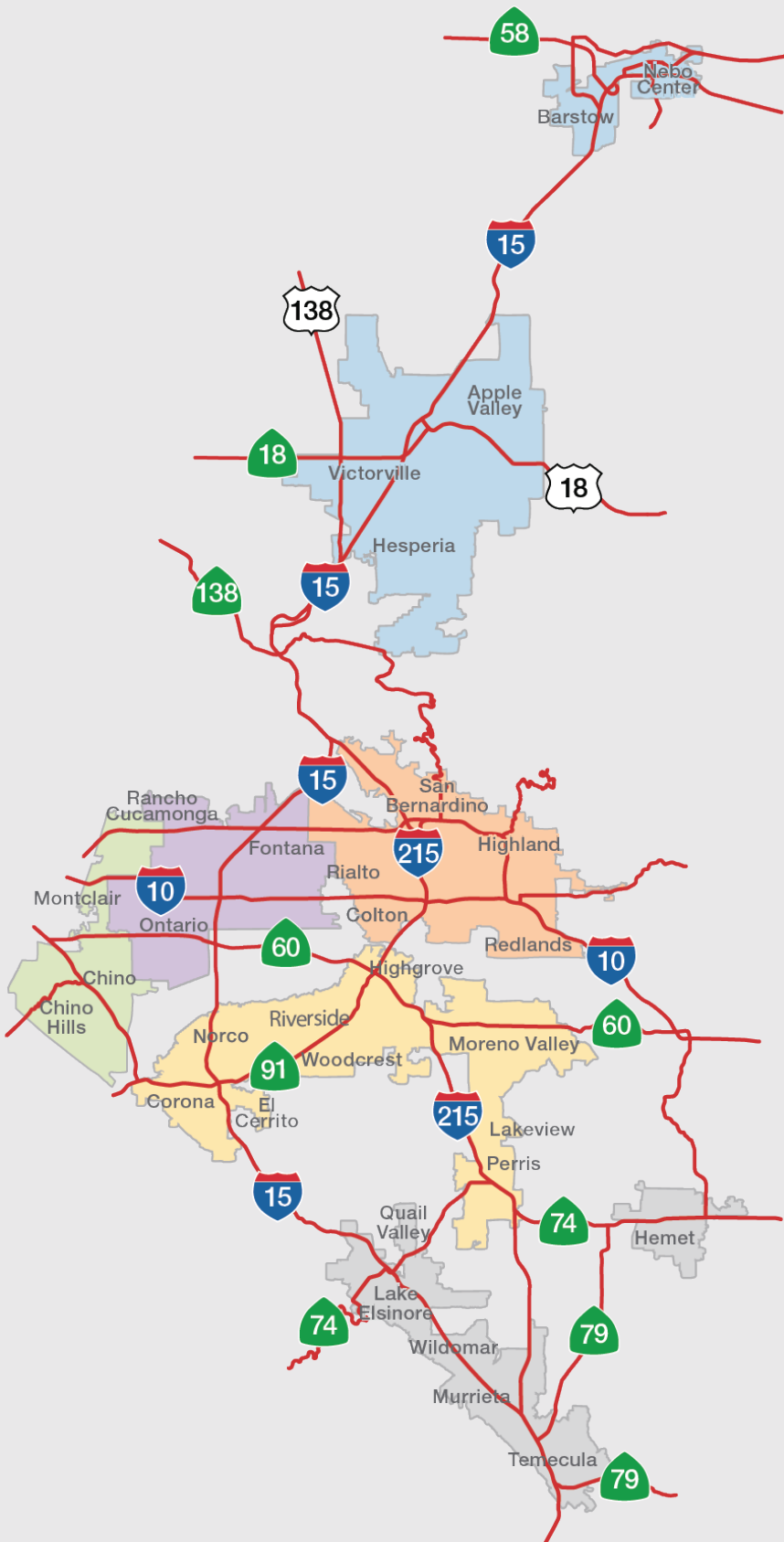
*All rents are FSG unless otherwise stated

Significant Sales Transactions

BUYER	ADDRESS	SUBMARKET	SALE PRICE \$/PSF	SQUARE FEET
Stillwater Investment Group	Towers at Riverwalk	Riverside	\$197	193,738
Crownsnest Properties, LLC	Citrus Park	Riverside	\$104	148,504
American Education Properties, LLC	655 W 2nd St	San Bernardino	\$167	86,606
English Road LLC	15095 Armagosa Rd	High Desert	\$203	34,998
Clouse Spaniac Living Trust	8038 Haven Ave	Airport	\$229	10,715

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- **High Desert**
 - Apple Valley
 - Barstow
 - Hesperia
 - Victorville
- **West**
 - Chino
 - Chino Hills
 - Montclair
 - Upland
- **Airport**
 - Fontana
 - Ontario
 - Rancho Cucamonga
- **San Bernardino**
 - Colton
 - Highland
 - Loma Linda
 - Redlands
 - Rialto
 - San Bernardino
- **Riverside**
 - Corona
 - Moreno Valley
 - Norco
 - Perris
 - Riverside
- **South**
 - Hemet
 - Lake Elsinore
 - Murrieta
 - Temecula
 - Wildomar

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Inland Empire

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