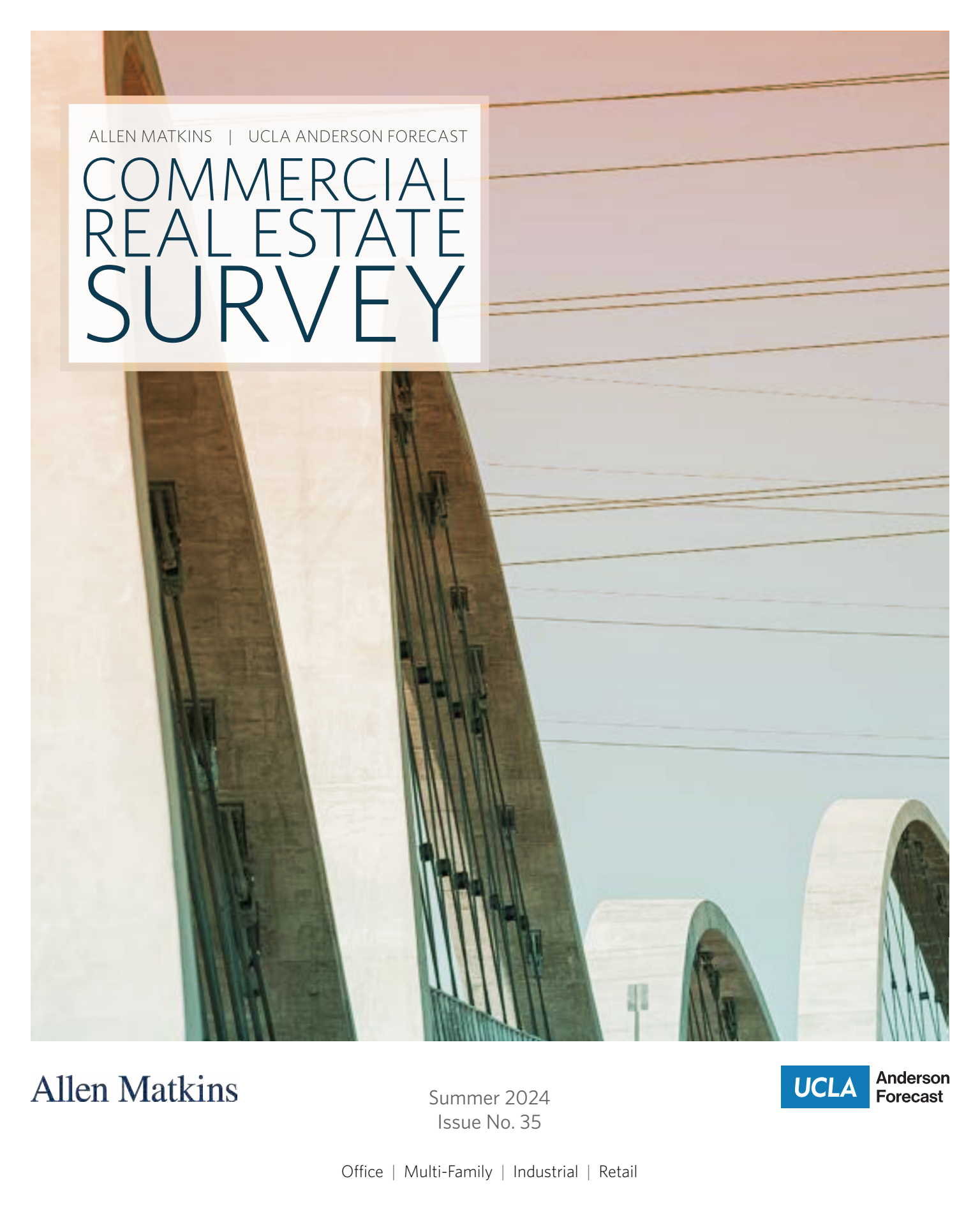




ALLEN MATKINS | UCLA ANDERSON FORECAST

COMMERCIAL REAL ESTATE SURVEY

Allen Matkins

Summer 2024
Issue No. 35

UCLA

Anderson
Forecast

Office | Multi-Family | Industrial | Retail

Allen Markin FORECAST

1. Increase faster than the rate of inflation
2. Increase slower than the rate of inflation
3. Stay the same
4. Decrease
5. Not

6. If you moved to office space in Los Angeles, do you expect the rental rate to:

1. Increase
2. Decrease
3. Stay the same
4. Not

7. If you moved to office space in San Diego, do you expect the rental rate to:

1. Increase
2. Decrease
3. Stay the same
4. Not

8. If you moved to office space in Chicago, do you expect the rental rate to:

1. Increase
2. Decrease
3. Stay the same
4. Not

9. If you moved to office space in New York City, do you expect the rental rate to:

1. Increase
2. Decrease
3. Stay the same
4. Not

10. If you moved to office space in London, do you expect the rental rate to:

1. Increase
2. Decrease
3. Stay the same
4. Not

11. If you moved to office space in Tokyo, do you expect the rental rate to:

1. Increase
2. Decrease
3. Stay the same
4. Not

12. If you moved to office space in Hong Kong, do you expect the rental rate to:

1. Increase
2. Decrease
3. Stay the same
4. Not

13. If you moved to office space in Singapore, do you expect the rental rate to:

1. Increase
2. Decrease
3. Stay the same
4. Not



Welcome to the latest edition of the Allen Matkins/UCLA Anderson Forecast California Commercial Real Estate Survey and Index

Allen Matkins and UCLA Anderson Forecast have partnered to create a Commercial Real Estate Survey and Index to better predict future California commercial rental and vacancy rates. This tool surveys supply-side participants – commercial developers and financiers of commercial development – for insights into their markets. The Survey and the resulting Index provide a measure of the commercial real estate supply-side participants' view of current and future conditions. Since participants make investment actions based upon these views, it provides a leading indicator of changing supply conditions.

Through an analysis of the Index and the incorporation of the Index into other economic forecasting models, the Survey, now in its 35th issue, is designed to provide more accurate information on future office, industrial, retail, and multi-family space in major California geographical markets.

The Allen Matkins and UCLA Anderson Forecast partnership

At Allen Matkins, a premier real estate and business law firm consistently ranked among the leading firms in California according to *Chambers USA*, we have been fortunate to work with and assist leading institutions, developers, and lenders in the real estate industry. We have prospered, along with our clients, in this vital sector of the California economy. We sponsor this Survey to provide value to the industry. We have partnered with UCLA Anderson Forecast, the leading independent economic forecast of both the U.S. and California economies for over 70 years, and have tapped the knowledge of the leading developers and financiers of real estate development in California to provide what we believe is the best, clear-sighted forecast of the California commercial real estate industry.

We hope you will find this Survey and Index to be helpful.

A handwritten signature in black ink that reads "John M. Tipton". The signature is written in a cursive, flowing style.

John M. Tipton
Partner, Real Estate Department
Allen Matkins

DECELERATION AS A PRELUDE TO GROWTH



"As retail tenants change, they want flexibility to pivot to different trends, such as entertainment-focused retail, or experience-based retail. We're seeing a lot of flexibility not only in permitted uses, but also in a lack of prohibited uses that we used to see, especially from big box tenants."

- Brian W. Michel
Partner,
Allen Matkins

Results of the Allen Matkins/UCLA Anderson Forecast California Commercial Real Estate Survey for 2024-2027

S. Sayantani
Jerry Nickelsburg
UCLA Anderson Forecast

Although widespread job growth is slowing in California this year, this has more to do with running out of people than running out of jobs. In the construction sector labor supply constraints and a wet 2023-2024 winter have both contributed to a slowing of growth. The Summer 2024 Allen Matkins/UCLA Anderson Forecast California Commercial Real Estate Survey reflects this overall slowdown in new projects started as well as the basis for continued growth in industrial, retail and multi-family sectors. Not surprisingly, developers of office space are facing a more challenging environment, and the Survey is indicating a multi-year process of contraction before a new building cycle begins.

The Allen Matkins/UCLA Anderson Forecast California Commercial Real Estate Survey compiles the views of commercial real estate developers, owners, and investors with respect to markets three years hence. The three-year time horizon was chosen to approximate the average time a new commercial project requires for completion (though projects with significant entitlement and/or environmental issues often take much longer). The panelists' views on vacancy and rental rates are key ingredients to their own business plans for new projects, and as such, the Survey provides insights into new, not yet on the radar, building projects and is a leading indicator of future commercial construction. For example, if a developer were optimistic about economic conditions in Silicon Valley's office market in 2027, then initial work for a new project with an expected ready-for-occupancy date of 2027 — a business plan, preliminary architecture, and a search for financial backing — would have to begin no later than the latter part of 2024. Although optimism does not always translate into new construction projects, this sentiment is usually a prerequisite for it.

Statistical forecast analysis has as its basis the proposition that past statistical relationships hold into the future. A knowledge of those correlations, current data and perhaps some assumptions about data not yet known, lead to the forecast. In addition to the summary measures of developer sentiment reported here, the Survey has a rich set of questions such that, with past trends in the Survey's indexes, we can now infer a more nuanced turn in commercial real estate markets.

RETAIL SPACE MARKETS

About 65% of the 2024 Summer Survey panelists are forecasting that the demand for retail space in southern California will grow more than supply. The panelists' three-year-forecast for vacancy rates are for them to fall in the Los Angeles, Inland Empire, Orange County and San Diego retail markets and for rental rates in these four markets to rise faster than inflation. Approximately half of the panelists have new projects planned for the next 12 months, and slightly less than half began new projects in the previous 12 months (Chart 1). The upward trend in sentiment, including in San Francisco, has been historically associated with a turn in the market. Throughout the state, the forecast for retail that it is now poised for an expansion of development in the coming several years.

In Northern California there is no significant change from the Winter 2024 Survey in the share of respondents having plans for beginning new projects over the next year. However, the share has significantly increased since last summer's survey. The financing of retail development is expected to become

more stringent with a forecast of a higher percentages of equity and higher IRR thresholds being required. In each of the Northern California sub-regions, vacancy rates are forecasted to be lower over the next few years, and increases in rental rates will not keep up with inflation. With the exception of San Francisco, the panelists are optimistic overall about the future of retail space markets.

In the Southern California retail space markets, there is less concern with equity participation in new projects, but the

panels share the view with the Northern California panels that the required IRR hurdle rate will be increasing. Overall, the panels for the Southern California sub-regions expressed an optimistic view of both the rental and vacancy rates outlook through 2027. Relative to the previous survey, the Summer 2024 Survey shows noted improvement in the composite sentiment index in every region other than the Inland Empire. It should be noted that sentiment by the Inland Empire panelists has been optimistic for the past year and remains so (Chart 2).

Chart 1

Retail Space Developer Sentiment
(>50 = optimistic, June '16 to June '24)

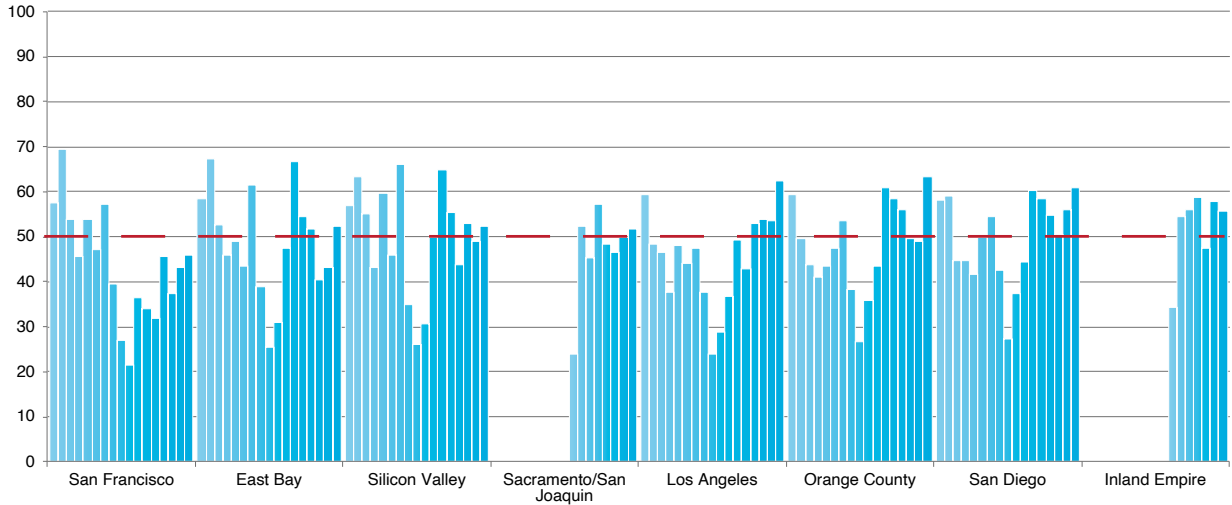
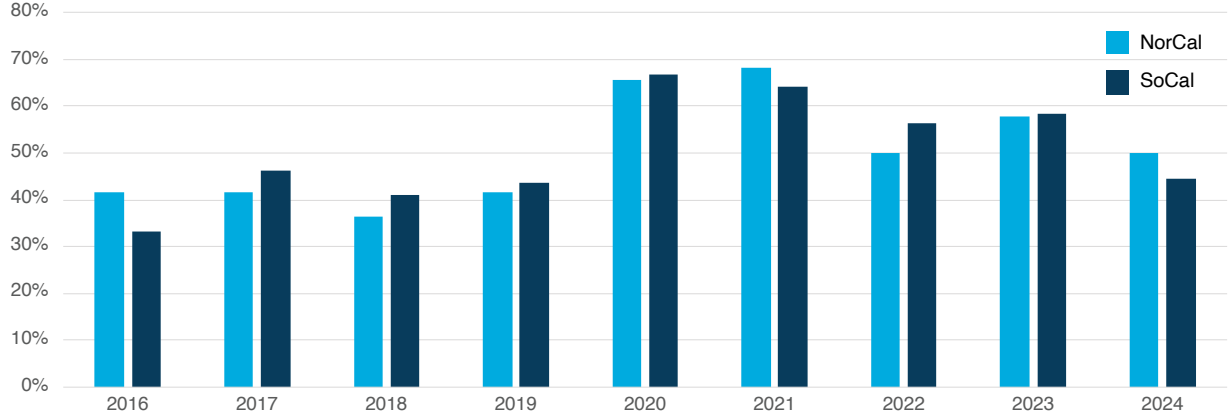


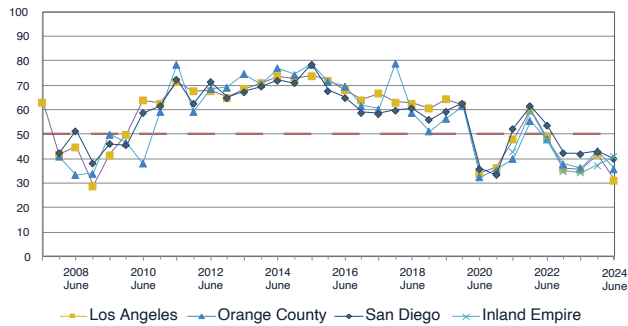
Chart 2

Retail Space
Percent Without New Development Plans
Summer Survey



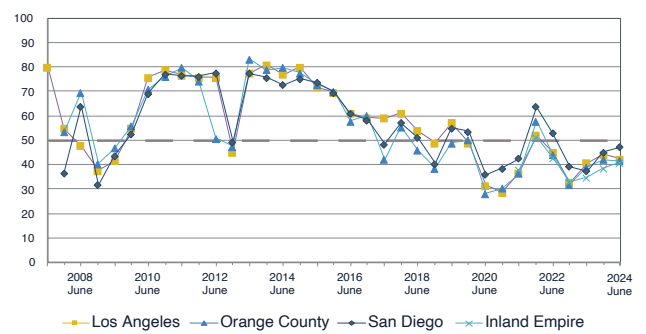
Southern California Office Rental Rates

Indexes of Survey: 3 year forecast
(<50 market weakening, >50 market tightening)



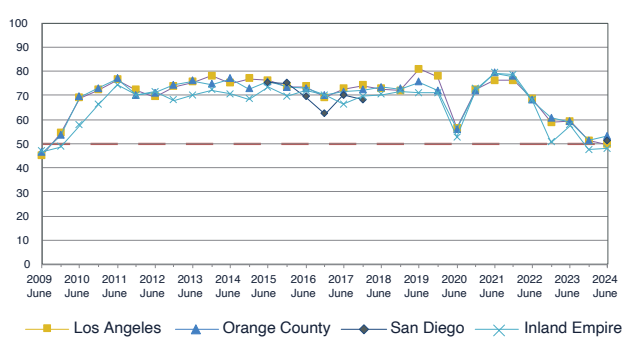
Southern California Office Vacancy Rates

Indexes of Survey: 3 year forecast
(<50 market weakening, >50 market tightening)



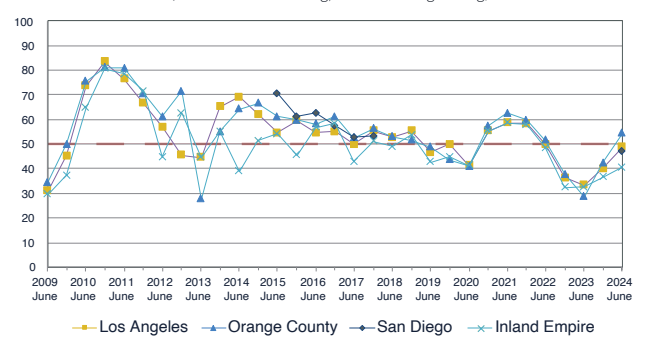
Southern California Industrial Rental Rates

Indexes of Survey Responses
(<50 market weakening, >50 market tightening)



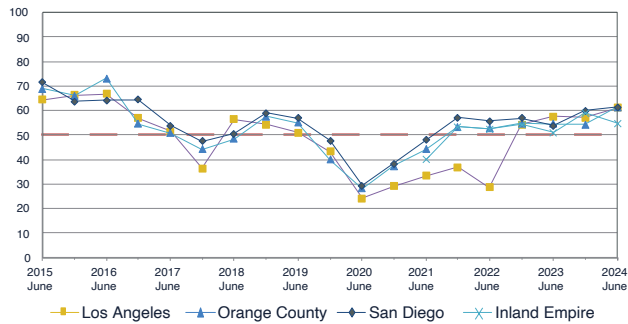
Southern California Industrial Vacancy Rates

Indexes of Survey Responses
(<50 market weakening, >50 market tightening)



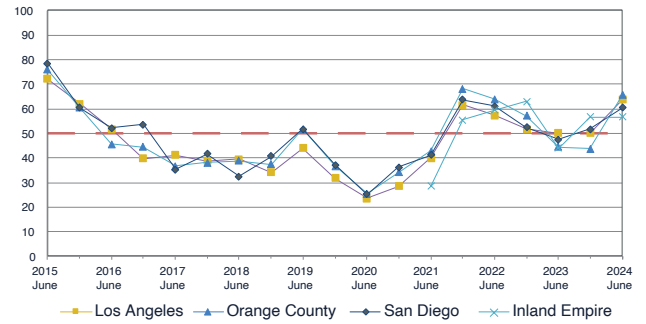
Southern California Retail Rental Rates

Indexes of Survey: 3 year forecast
(<50 market weakening, >50 market tightening)



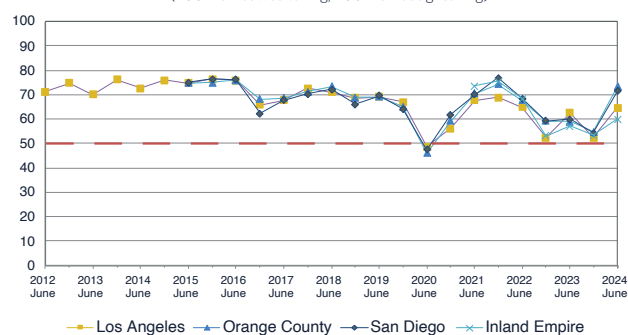
Southern California Retail Vacancy Rates

Indexes of Survey: 3 year forecast
(<50 market weakening, >50 market tightening)



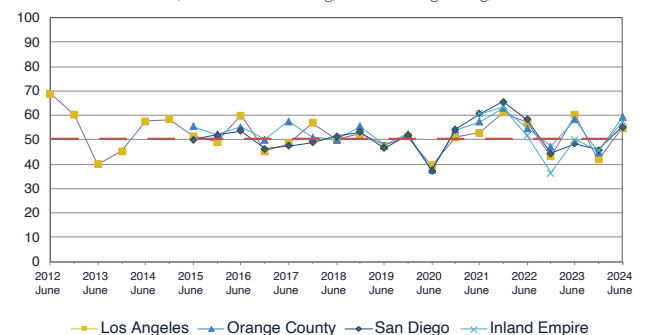
Southern California Multifamily Rental Rates

Indexes of Survey Responses
(<50 market weakening, >50 market tightening)



Southern California Multifamily Vacancy Rates

Indexes of Survey Responses
(<50 market weakening, >50 market tightening)



In Southern California, the share of panelists having started new projects in the previous 12 months declined by about eight percentage points. The non-labor building cost index for Southern California rose as well, although not as fast as in Northern California. The three-year-forecasts for rental rate changes and for vacancy rates are pessimistic everywhere in Southern California. Also in Southern California, 62% of the respondents in the current survey expect to be required to hold more equity in their projects over the next three years.

Office Space Developer Sentiment Index
(>50 optimistic sentiment, June '16 to June '24)

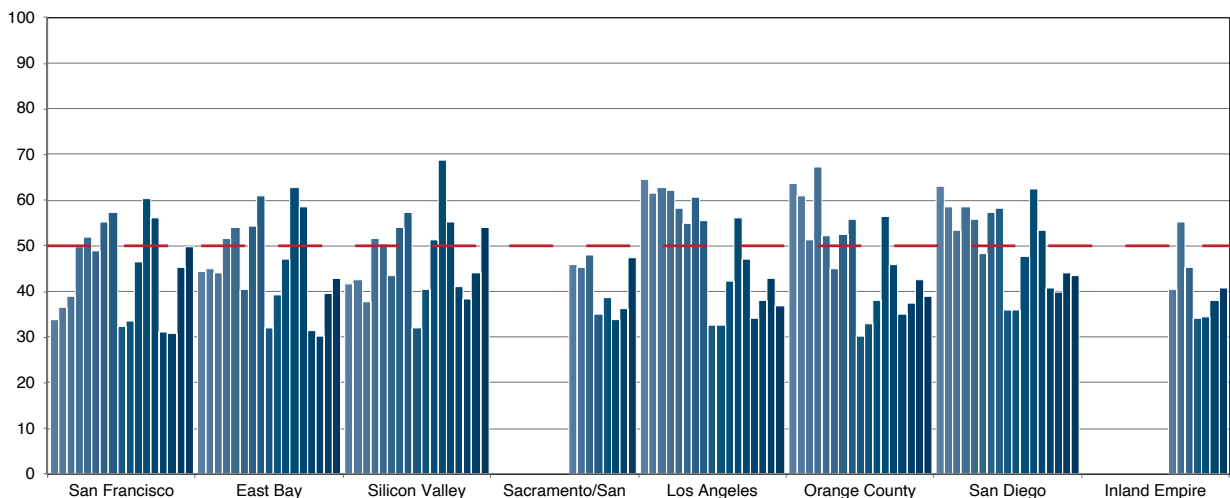
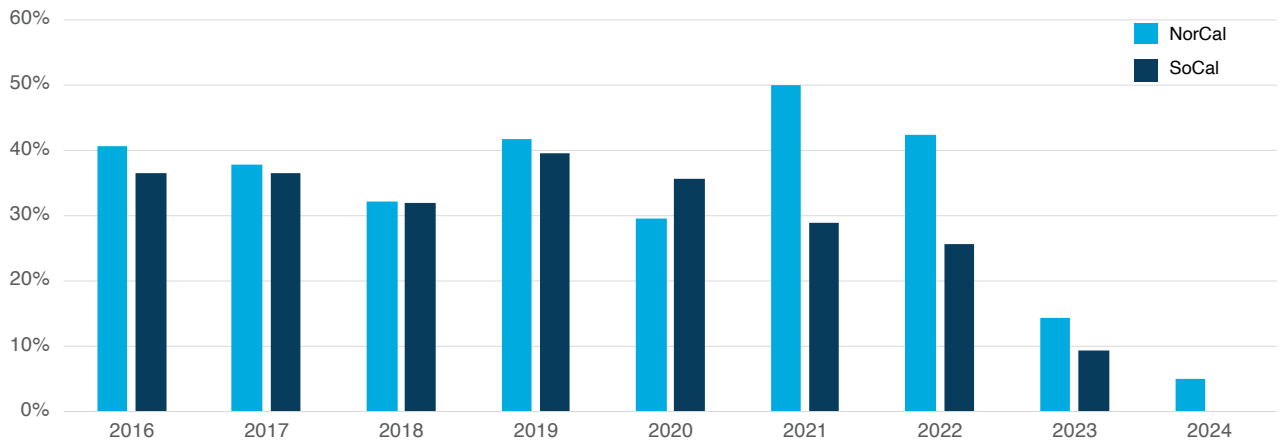


Chart 4

Percent of Panelists Planning New Office Development
(Next 12 Months, 8 Markets, Summer Survey)



"One of the trends we're seeing in office space is that tenants are investing in smaller, better space, and there are a few ways we're seeing this. One is a flight to quality where tenants are moving to smaller space in markets that have more amenities."

- Erin L. Murphy
Partner,
Allen Matkins



INDUSTRIAL SPACE MARKETS

In the Winter 2024 Survey, the panels indicated a cooling of the red-hot industrial sector, though they were not predicting a contraction. The return of traffic at California's seaports and the holding up of consumption have contributed to a more positive sentiment in the current survey. Three out of the five markets surveyed: the East Bay, Sacramento/San Joaquin and Orange County had a composite sentiment index greater than 50, implying optimism about improved market conditions over the next three years (Chart 5). The Los Angeles panel is forecasting markets to remain as robust as today, and the Inland Empire panel is forecasting a slight cooling of the market. Nevertheless, one should keep in mind that pessimism only means that rental rates and vacancy rates will be no better

than today. In a perennially hot market this is not pessimism in the usual sense. Over the three-year-horizon, the Summer 2024 Survey reports growth in demand surpassing supply and the differential has increased from that expected in 2023 in both Northern and Southern California (Chart 6).

In both the East Bay and the Sacramento/San Joaquin regions the expectation is for rental-rate growth to exceed inflation and for vacancy rates to decline over the next three years. The percentage of panelists starting new projects during the last 12 months and the percentage planning to begin new projects over the next 12 months has declined, though this is only a reflection of a normalization of developer activity.

"In the industrial space, we're seeing a lot of growth nationwide, but it's moving towards geographic locations that have strong workforces, as well as low-cost construction, low-cost regulatory compliance, and in the data center space, availability of power."

- Alykhan Shivji
Partner,
Allen Matkins



"There is a major skilled labor shortage, and I think that's driving where the hubs for industrial and distribution are really growing the most."

- Evan Kantor
Head of U.S. Commercial
Investment Group,
Kennedy Wilson



While a majority of the respondents expect vacancy rates to grow over the next three years in the Los Angeles, the Inland Empire and San Diego regions, the opposite is the case for the Orange County panel. In the Los Angeles and Inland Empire regions, rental rates are not expected to increase fast enough to keep up with inflation, and in Orange County and San Diego the panel expectations are for greater than the rate of inflation rental-rate increases. About 65% of the

respondents expect to be required to hold more equity to achieve a higher investment IRR threshold over the next three years than today. Forty-four percent of the panelists started new projects over the last 12 months and 50% reported plans to start new projects in the coming 12 months. In addition, the panelists are expecting demand to grow more than supply over the next three years.

Chart 5

Industrial Space Developer Sentiment Index
(>50 optimistic sentiment, June '16 to June '24)

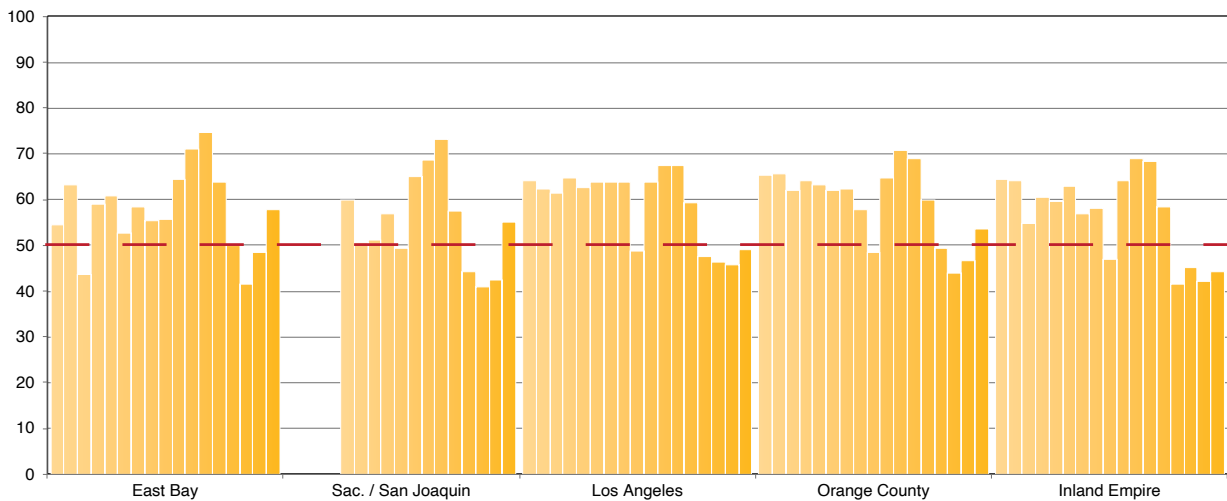
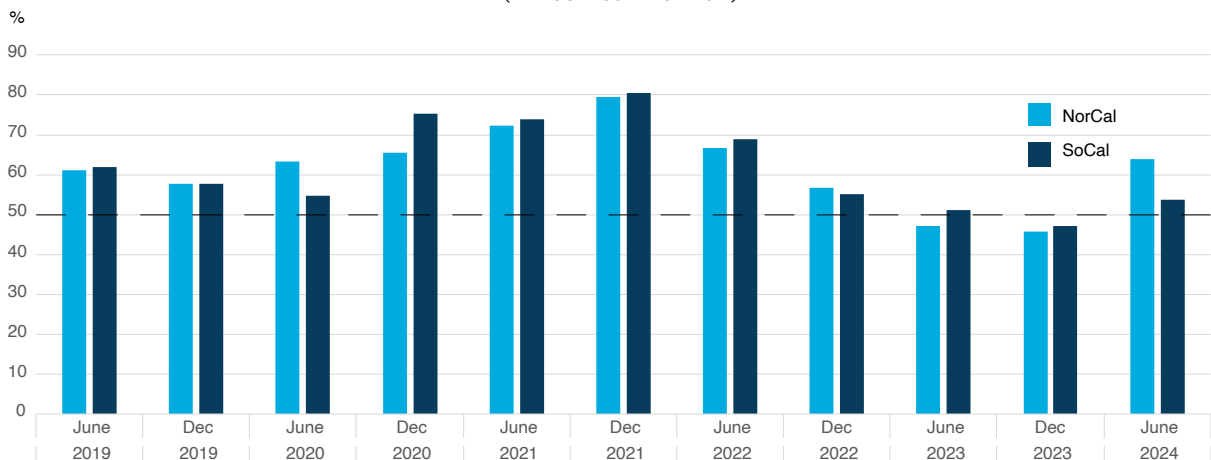


Chart 6

Industrial Space Demand/Supply Growth
(Three Year Horizon)



MULTIFAMILY HOUSING MARKETS

The multifamily housing panel development sentiment indexes are higher than they have been for most of the last two years and the panelists are optimistic with respect to market fundamentals for each of the eight sub-regions surveyed: San Francisco, Silicon Valley, the East Bay, Los Angeles, Orange County, San Diego, Sacramento/San Joaquin and the Inland Empire (Chart 7). Among these, the increase in panelists' sentiment in Los Angeles, Orange County and San Diego moved these markets into the optimistic region from a neutral position. While the share of participants planning new multi-family development is lower than the Summer 2023 Survey,

it is higher than the Winter 2024 Survey (Chart 8). The share of the current survey respondents who expect to be required to have more equity and to face a higher required investment IRR threshold is lower, albeit marginally, from the Winter 2024 Survey.

Rental rates for multifamily units are expected to be higher across California and vacancy rates are expected to fall everywhere over the next three years with the exception of the Sacramento/San Joaquin region where they are expected to be unchanged.

Chart 7
Multifamily Housing Developer Sentiment Index
(>50 optimistic sentiment, June '16 to June '24)

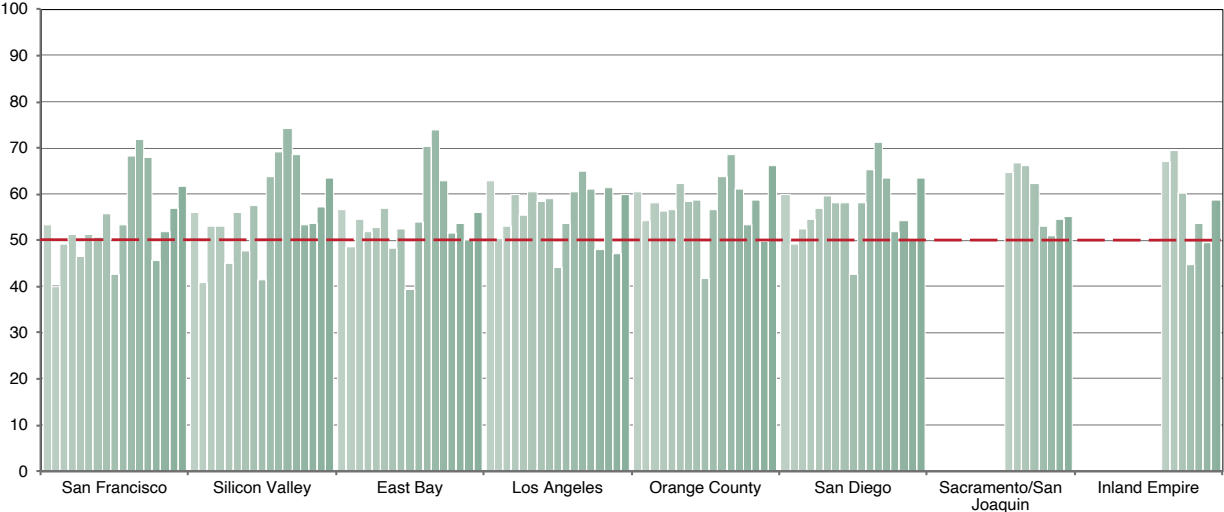
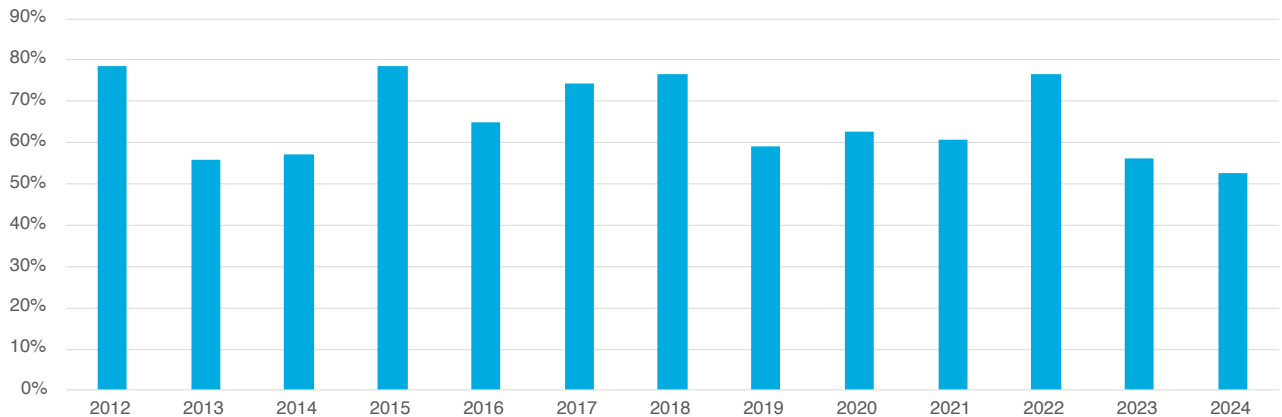


Chart 8

Percent of Panelists Planning New Multifamily Development
(Next 12 months, 8 markets, Summer Survey)



"Many people would like to be in a house with a yard, but with escalated interest rates and elevated housing costs, home ownership is out of reach for most.

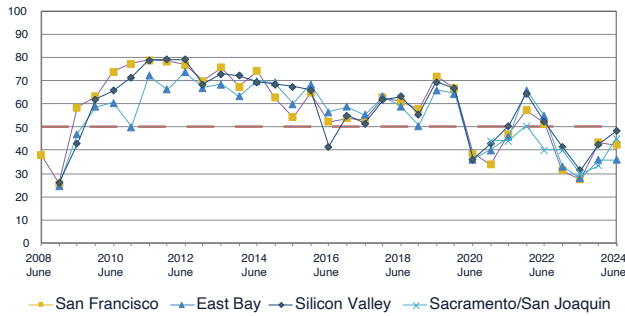
This has led to a tremendous jump in the quantity of developers building to rent, which has served as a boon to renters and developers alike."

- Kitty Wallace
Senior Executive Vice President,
Colliers



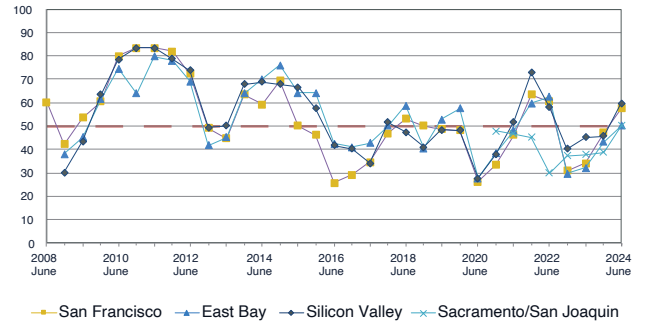
Bay Area Office Rental Rates

Indexes of Survey: 3 year forecast
(<50 market weakening>50 market tightening)



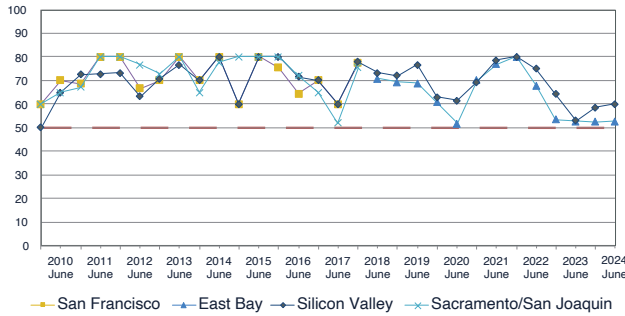
Bay Area Office Vacancy Rates

Indexes of Survey: 3 year forecast
(<50 market weakening>50 market tightening)



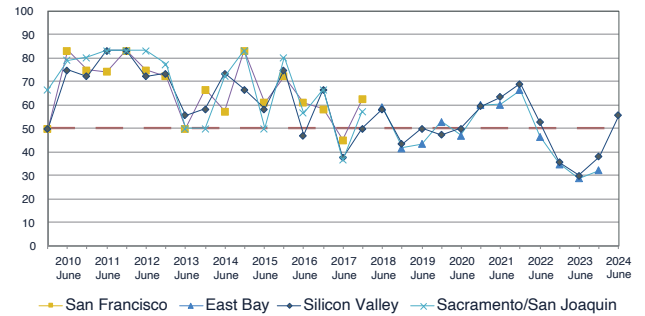
Bay Area Industrial Rental Rates

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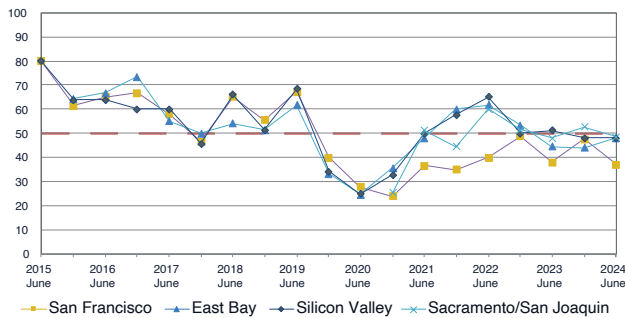
Bay Area Industrial Vacancy Rates

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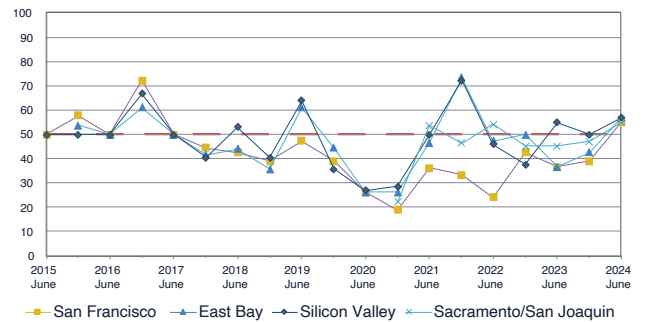
Bay Area Retail Rental Rates

Indexes of Survey: 3 year forecast
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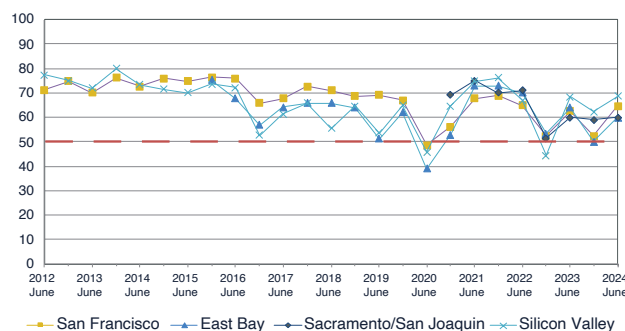
Bay Area Retail Vacancy Rates

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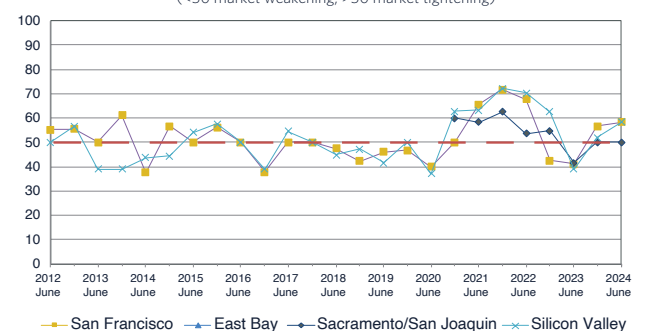
Bay Area Multifamily Rental Rates

Indexes of Survey Responses
(<50 market weakening, >50 market tightening)



Bay Area Multifamily Vacancy Rates

Indexes of Survey Responses
(<50 market weakening, >50 market tightening)



THE SURVEY IN PERSPECTIVE

The Summer 2024 Allen Matkins/UCLA Anderson Forecast California Commercial Real Estate Survey was taken as the economy was coming off a quarter in which GDP growth bounded up to 5.1% and commercial real estate development, in the aggregate, expanded. Our Survey respondents, while generally positive about the coming three years, were concerned with increasing financing costs. Nevertheless, industrial markets, which continue to experience historically low vacancy rates, remain poised for a good run of new building

and superior returns. Multifamily housing sentiment remains positive though significant new development is not expected until 2025 and 2026. The current turn in sentiment for retail will now result in significant new building in the near future. Office markets have a long road ahead as both vacancies and financial overhang require adjusted asset values before a significant increase in new office development will take place. If the recent retail space history is a guide, this process will require time beyond the 2026 horizon of the current Survey.

"We have seen clients, who were waiting for distressed sale opportunities, start to close on those sorts of deals, whether through a note sale or foreclosure, or just trading directly with the existing owner in an off-market transaction. I think those types of transactions are a positive sign, even if they were completed at a lower than anticipated valuation, in that it level sets expectations for the broader market. Our expectation is that this initial activity will lead to a larger wave of transaction volume bringing more potential buyers off the sidelines to start acquiring properties."

- Anthony R. Burney
Partner,
Allen Matkins



"I think the continued improvement to the state's density bonus law has been and will continue to be a real driver for new activity. It presents opportunities for properties that previously didn't pencil because of the added density, and can also be a force for innovation at the local level as some cities improve upon and modify some of the state law language in order to give special benefits within their cities."

- Timothy M. Hutter
Partner,
Allen Matkins



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COMMERCIAL REAL ESTATE SURVEY

Los Angeles
Orange County
Inland Empire
San Diego
Sacramento
San Joaquin County
San Francisco
East Bay
Silicon Valley

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