

Westside office highlights Q3 2009

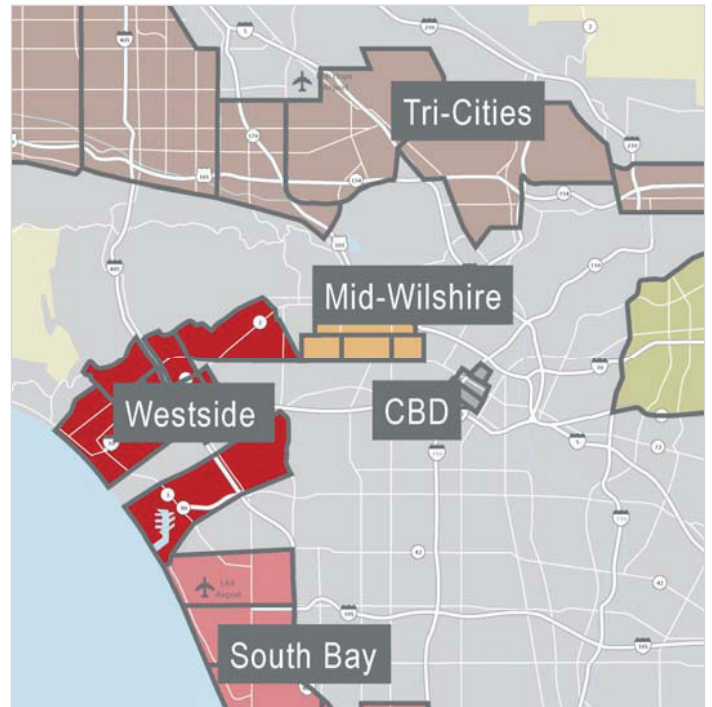
Quarter in review

The rate of deceleration in the West Los Angeles office market slowed substantially during third quarter, with overall vacancy rates increasing by only one percent from 14.4 to 15.4 percent. The Marina Del Rey / Culver City submarket posted the highest vacancy rates of the quarter, due mostly in part to the 418,551 square foot sublease that Fox Interactive is marketing in this submarket. However, over the last four quarters, the volume of new sublease space coming to market has decreased by nearly 50 percent. Over half of the sublease space currently available belongs to entertainment and media companies who are highly susceptible to swings in consumer spending and thus were swift to layoff employees at the first hint of changing market conditions. Leasing activity has remained relatively slow and consistent throughout the year, fluctuating between roughly 850,000 – 900,000 square feet per quarter. Despite the sharp economic downturn this year, leasing activity is only off by 20 percent year-to-date as a result of several large tenants opting to renew their leases early. The early renewals will potentially impact absorption figures in a negative manner between 2010-2011 as space that would have leased during those years, creating positive absorption, will no longer occur.

The three largest leases this quarter were in fact, all renewals. In Santa Monica, Lions Gate Entertainment signed a six-year renewal for 127,000 square feet of space that it occupies at 2600 Colorado Avenue. At the Howard Hughes Center, Sony Connect downsized from three floors to two floors and renewed 50,000 square feet of its premises for five years and in Beverly Hills Live Nation also chose to stay in its 39,000 square feet on Civic Center Drive for another ten years. Similar to a previous trend we saw back during the first quarter of 2009, strong credit tenants that have taken a long term approach to their business plans are locking in favorable rental rates for five to ten years.

On average, rental rates have declined by 20 percent over the last year. Marina Del Rey / Culver City, Miracle Mile and West Los Angeles / Olympic Corridor posted the lowest direct average asking rental rates this quarter at \$2.80 - \$2.95 per square foot. Century City maintained the highest asking rental rates in the market at just over \$4.00 per square foot. The concentration of Class A product and institutional ownership tends to keep Century City consistently at the higher end of the asking rate spectrum compared to the steep declines in asking rates that submarkets like Santa Monica and Westwood have experienced.

Submarket boundaries map



Key market indicators

Stock	↑	49,924,157 s.f.
YTD net absorption	↓	-2,007,350 s.f.
Overall vacancy rate	↑	15.38%
Average direct asking rent	→	\$3.95 FSG / p.s.f.
Under construction	→	890,000 s.f.

Market Outlook

From an economic standpoint, the West Los Angeles market will be challenged over the coming years and remain a tenants' market through 2012. Unemployment figures in Los Angeles County have more than doubled from the 2007 average of 5.1%, with forecasts showing continued upward pressure on unemployment rates in 2010. Based on previous recession data, the lag between employment figures turning positive and actual demand for office space increasing could take up to 30 months from third quarter 2009. In addition, there is an unknown amount of "shadow space" in the market where firms have downsized in terms of physical headcounts but not actually returned sublease or direct space to market yet. As leases begin to expire over the next three years, the impact of this shadow space on vacancy rates could very well be negative and postpone any organic growth in the market.

On the capital markets side, sale activity came to a virtual standstill with no major asset trades occurring during third quarter. As of October, Los Angeles County had \$4 billion in outstanding CMBS loans with only \$100 million in default. The majority of near-term US CMBS loans mature between 2011 and 2013, although many are expected to default prior to maturity. Distressed assets will be monitored closely going forward because of the impact that they have on market rents. Should a building go into foreclosure, the lender or servicer will likely have a lower basis and the capability to lease up the building at lower market rates. Less expensive lease comparables will drag down the overall average rental rate in that particular submarket and the cycle will continue with distress essentially begetting more distress.

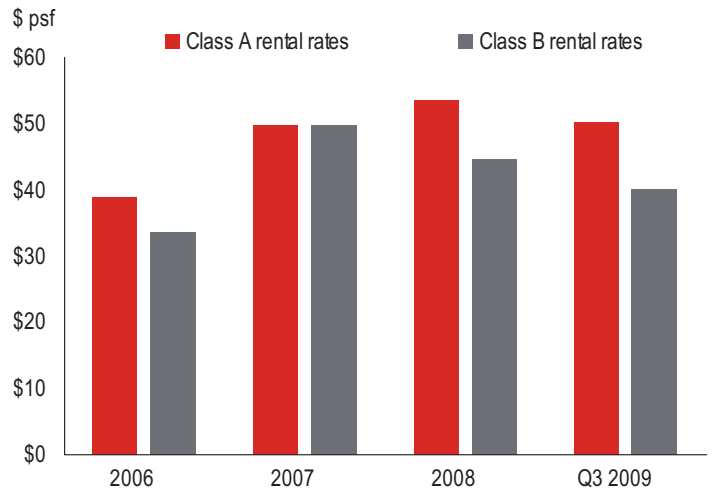
Significant lease transactions

Lions Gate Entertainment 2600 Colorado Avenue	127,000 s.f.
Sony Connect 6080 Center Drive	50,000 s.f.
Live Nation 9348 Civic Center Drive	39,000 s.f.
McKinsey & Company 2000 Avenue of the Stars	22,000 s.f.

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Average rental rates (Class A vs. Class B)



Sublease additions per quarter



Sublease tenant type

