

Office Market Report

Compared to 2009:

Vacancy

DOWN

Net Absorption

POSITIVE

Lease Rates

DOWN

Transactions

DOWN

Construction

DOWN

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Market Highlights

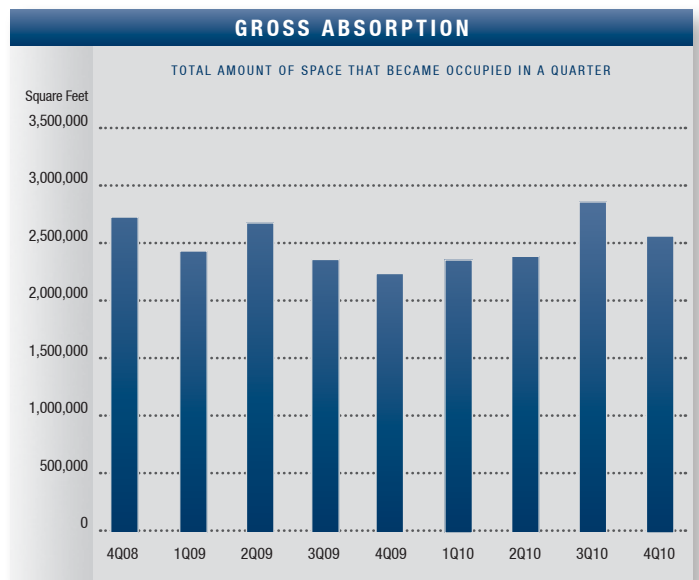
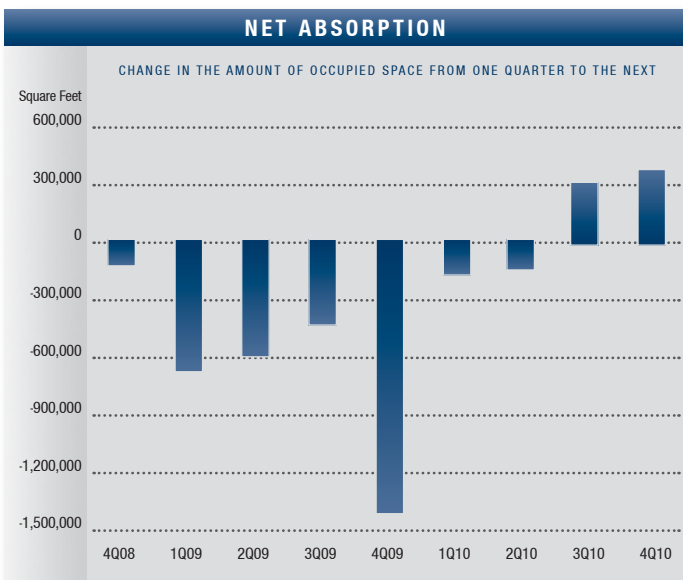
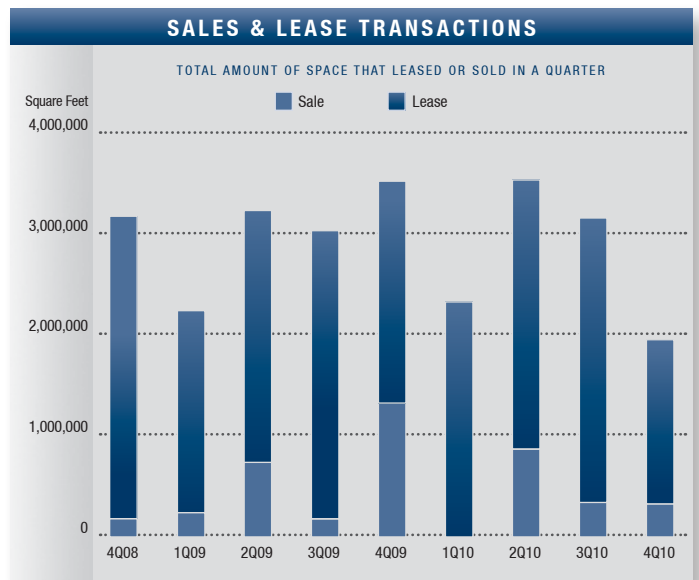
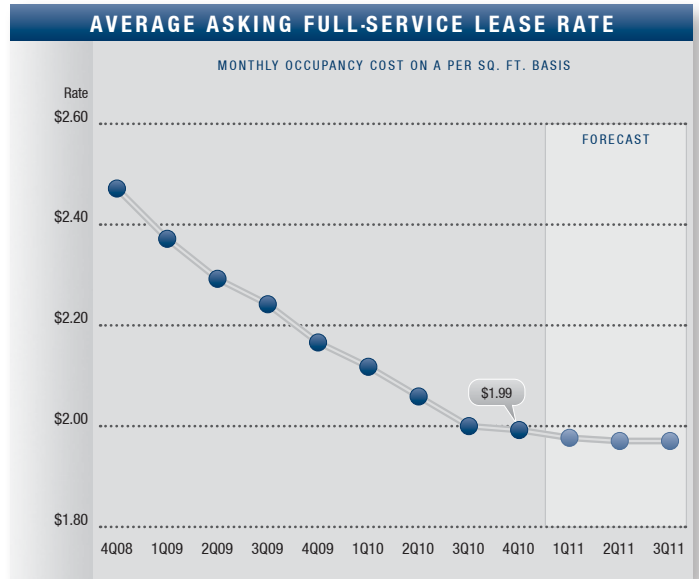
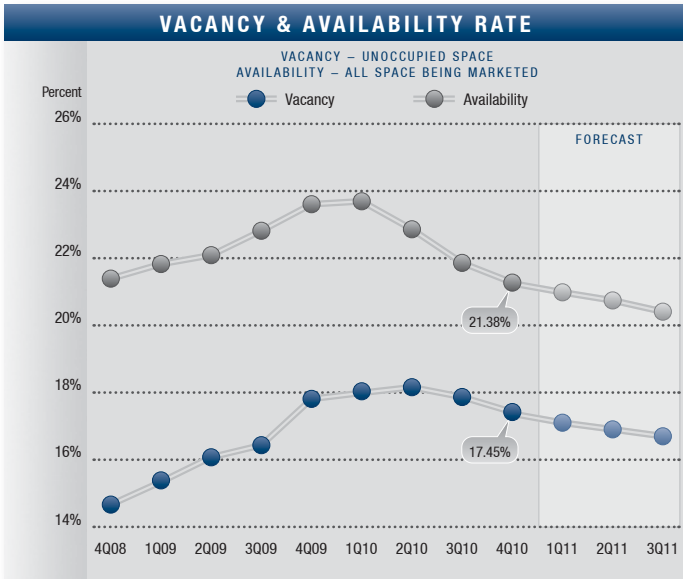
- **Are we there yet?** – The Orange County Office displayed more signs of stabilization this quarter. Both vacancy and availability were down from the previous quarter, and net absorption was positive for two consecutive quarters, displaying overall positive absorption for 2010. Although demand is still weak by historical standards, Labor Day marked the beginning of a renewed interest in sales transactions. While these are positive indications, stability will need to be sustained in coming quarters to be considered recovery.
- **Construction** – The record year for new development was 1988, when 5.7 million square feet of new space was added and vacancy rates were approximately 24%. Total space under construction came in at 337,000 square feet for the fourth quarter of 2010. The slowdown in construction has and will ease the upward pressure on vacancy and the downward pressure on lease rates.
- **Vacancy** – Direct/sublease space (unoccupied) finished the quarter at 17.45%, a decrease over the third quarter's rate of 17.86%. This is also down from the Great Recession peak of 18.13% we saw in the second quarter of 2010 and significantly less than the 23% vacancy rate recorded in 1990.
- **Availability** – Direct/sublease space being marketed was at 21.38% this last quarter — a noticeable decrease of over 9% when compared to 2009's rate of 23.58% and a noticeable decrease from last quarter's rate of 21.89%. We are finally beginning to see a decrease in the velocity of new available space being added to the market.
- **Lease Rates** – The average asking Full-Service Gross (FSG) lease rate per month per square foot in Orange County was \$1.99 for the fourth quarter of 2010 — an 8.29% decrease over 2009's rate of \$2.17 and one cent lower than the third quarter's rate. The record high rate of \$2.77 was established in the fourth quarter of 2008. Class A asking rates for the county averaged \$2.16 FSG — the highest being in the Airport market where they are averaged \$2.28 FSG.
- **Absorption** – Net absorption for the county posted a positive 392,539 square feet for the fourth quarter of 2010, giving the office market a total of 398,692 square feet of positive absorption for 2010, correcting the negative

absorption we saw earlier in the year. This is the first time since 2006 that we have seen annual positive absorption. Hopefully, this positive trend will continue, but it will be dependent upon continued job creation.

- **Transaction Activity** – Leasing activity checked in at nearly 9.5 million square feet for 2010, a slight decrease over the previous year's total of 9.58 million square feet. Sales activity showed a decrease, posting 1.5 million square feet of activity compared to the 2.4 million square feet we saw in 2009. Details of the largest transactions for 2010 can be found on the back page of this report.
- **Employment** – The unemployment rate in Orange County was 9.3% in November 2010 — up from a revised 9.1% in October 2010 and below the year-ago estimate of 9.6%. This compares with an unadjusted unemployment rate of 12.4% for California and 9.3% for the nation during the same period. According to the State of California Employment Development Department, Orange County increased by 19,100 payroll jobs from November 2009 to November 2010; the largest gains were 10,100 in professional & business services and 8,400 in leisure and hospitality. However, during that same period, Orange County lost 4,900 jobs in construction. Chapman University is forecasting that 23,000 jobs will be added in Orange County in 2011.
- **Overall** – We are beginning to see a decrease in the amount of available space being added per quarter, as well as an overall increase in investment sales activity. As we enter into 2011, positive absorption has begun, and with few new deliveries in the pipeline that would put more upward pressure on vacancies, the market is beginning to stabilize. We foresee an increase in investment activity in the coming quarters as lenders continue to dispose of distressed assets. Lease rates are expected to remain soft for the near future, and concessions in the forms of free rent, reduced parking fees, relocation funds and tenant improvement allowances should continue to increase to incentivize tenants to act immediately. We should see an increase in leasing activity as many short-term deals come up for renewal. If job creation continues and consumer confidence stabilizes, the office market will continue to recover.

OFFICE MARKET OVERVIEW

	2010	2009	2008	% CHANGE vs. 2009
Vacancy Rate	17.45%	17.80%	14.64%	(1.97%)
Availability Rate	21.38%	23.58%	21.45%	(9.33%)
Average Asking Lease Rate	\$1.99	\$2.17	\$2.47	(8.29%)
Sale & Lease Transactions	10,995,690	12,004,324	9,625,274	(8.40%)
Gross Absorption	10,098,962	9,652,447	9,795,338	4.63%
Net Absorption	398,692	(3,086,873)	(1,059,471)	N/A



RECENT TRANSACTIONS

Sales Transactions

Property Address	Submarket	Class	Square Feet	Sale Price per SF	Buyer	Seller
2211 Michelson Avenue	Airport	A	271,556	\$380.03	Kilroy Realty Corporation	Crescent Real Estate Equities
2957-3031 Michelson Drive - 2 Properties	Airport	A	150,480	\$306.73	LBA Realty	Maguire Properties
5 & 6 Hutton Centre Drive - 2 Properties	Airport	A	543,188	\$162.01	Gordon Angelo & Company	Maguire Properties
18301 Von Karman Avenue	Airport	A	224,383	\$183.84	Greenlaw Partners	KBS Real Estate Investment Trust, Inc.
999 W. Town and Country Road	Central	B	98,551	\$225.00	Kilroy Realty Corporation	TA Associates Realty
17600 Gillette Avenue	Airport	B	98,925	\$205.71	Hines Global REIT	AJ Irvine Owner Corporation

Lease Transactions

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
1600 S. Douglass Road - Renewal	Central	A	127,750	Aug-10	Cash Call	New Tower Trust Company
2701 S. Bristol Street - Renewal	Airport	B	115,000	Apr-10	Coastal Communities Hospital	Integrated Healthcare Holdings, Inc.
5 Peters Canyon Road	Airport	A	107,152	May-10	LSI Title	The Realty Associates Fund VIII, LP
4000 MacArthur Boulevard - Renewal	Airport	A	96,829	Mar-10	Mindspeed Technologies, Inc.	Tishman Speyer
3 MacArthur Place	Airport	A	85,340	Aug-10	Edison Mission Energy	Highridge Partners
1525 N. Tustin Avenue	Central	A	81,646	Jan-10	Regional Center of Orange County, Inc.	Thomson Reuters

Product Type

CLASS A

Most prestigious buildings competing for premier office users with rents above average for the area. Buildings have high-quality standard finishes, state-of-the-art systems, exceptional accessibility and a definite market presence.

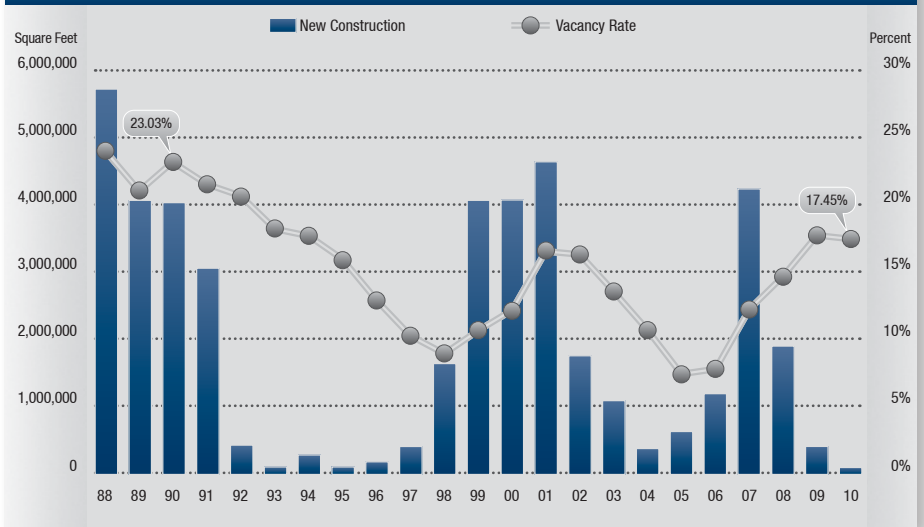
CLASS B

Buildings competing for a wide range of users with rents in the average range for the area. Building finishes are fair to good for the area, and systems are adequate. However, Class B buildings cannot compete with Class A buildings of the same price.

CLASS C

Buildings competing for tenants requiring functional space at rents below the area average.

ANNUAL NEW CONSTRUCTION VS. VACANCY RATE



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