

# Industrial Market Trends Orange County

Grubb & Ellis Research

Fourth Quarter 2005



## Orange County Industrial Market Remains Hot

### Executive Summary

As 2005 drew to a close, the Orange County industrial market illustrated the economic law of supply and demand, with demand far outweighing supply. This was true for both the leasing and sale sides. Tenants seeking space and investors seeking purchases are finding their side of the bargaining table more difficult. Leasing activity continues to rise and is expected to increase progressively into next year. Asking rents have increased slightly due to the lack of quality space available on the market as well as the fact that there is limited new construction on the horizon for the lease product. The overall vacancy rate in Orange County dropped 70 basis points to 4.4 percent from 5.1 percent the previous quarter. Net absorption in Orange County during the fourth quarter increased by over 640,000 square feet compared to the previous quarter. Sale activity remains strong with no signs of slowing. The declining vacancy rate gives landlords the leverage to stay firm on their high asking rental rates and reduce concessions to the tenant.

The three largest lease transactions completed during the fourth quarter all occurred in the North Orange County submarket. Advanced Image Direct leased 135,571 square feet and Eleganza Tile leased 91,116 square feet lease in Fullerton, while OC RV Storage secured 90,664 square feet in the city of Anaheim. Investors' demand for industrial space is vigorous, fueled by low interest rates and lack of product. The short-term forecast for the Orange County industrial market is one of continued strength and steady growth. Limited land, low vacancies and a large supply of investors will support the market expansion in 2006.

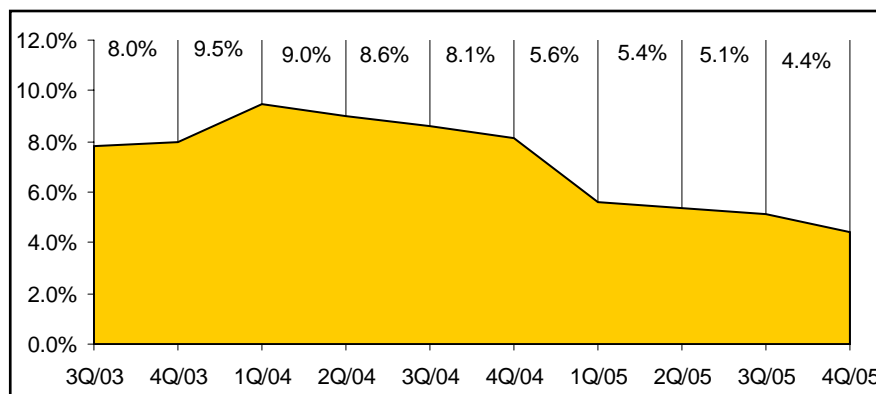
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Industrial Vacancy Rate\*

\* All Product Types

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*“There was over 1.8 million square feet of leasing activity during the fourth quarter.”*

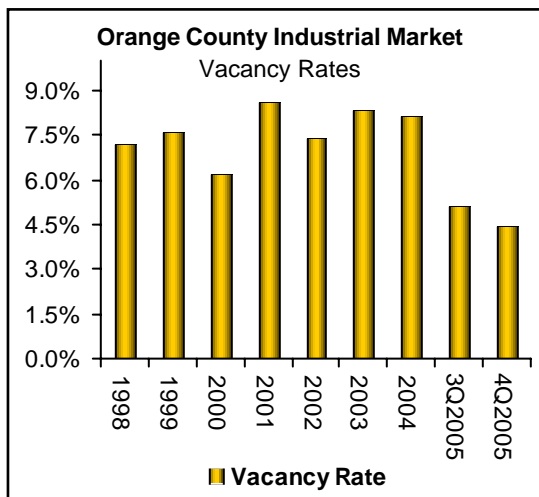
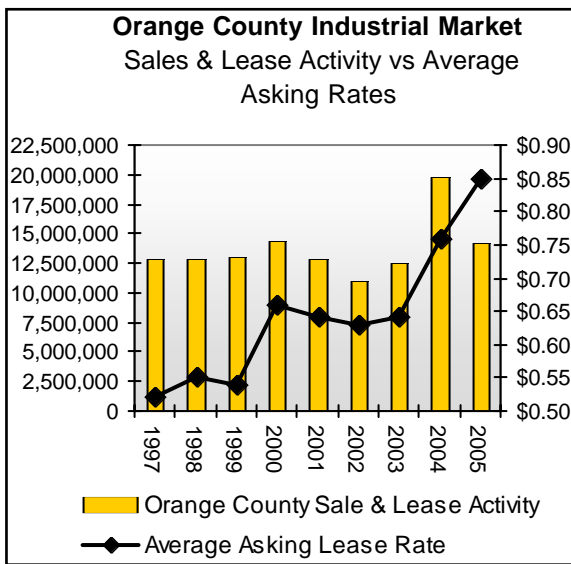
## Market Assessment

The manufacturing/distribution sector showed a marked improvement during the fourth quarter with 1,440,760 square feet absorbed, an increase from the third quarter. In the standard industrial sector, the West and North County submarkets outperformed other submarkets. The West County topped the rest of the county with 532,188 square feet absorbed, while the North County area absorbed 524,039 square feet. The market was extremely active on the leasing side compared to the same period a year ago. There was over 1.8 million square feet of leasing activity during the fourth quarter. Activity was strongest in the North and Airport submarkets with the North County submarket contributing 33 percent of the total leasing activity. The majority of the fourth quarter's leasing activity was concentrated in the 10,000 to 50,000 square-foot ranges. Asking rental rates in the manufacturing/distribution sector increased from \$0.70 to \$0.75 NNN during the quarter.

The Orange County R&D sector bounced back in the fourth quarter. There was a total of 452,319 square feet absorbed compared to negative 23,320 square feet in the third quarter. This caused overall vacancy rates to decline from 5.5 percent to 4.9 percent. Asking rental rates increased \$0.03 from the previous quarter. Construction of R&D buildings remained modest with 63,000 square feet underway in the West and North County submarkets.

Buildings for sale remained a hot item with the number of user sales increasing substantially. Demand was high for industrial product ranging from 7,500 to 28,000 square feet. There was over 1.8 million square feet of transactions during the fourth quarter. Average asking sale prices reached a staggering \$160 per square foot. Although short-term interest rates have increased, small investors see the value in real estate and continued to take advantage of low long-term interest rates to buy property.

Industrial space under construction in the fourth quarter totaled 790,080 square feet. That was up from the previous quarter's total of 622,627. The West Orange County submarket accounted for the most space under construction with 460,495 square feet, followed by North County with 310,435 square feet. Some of the major projects still under construction in the fourth quarter are the Astronautic Corporate Center in Huntington Beach and the North Anaheim Industrial Park. These projects are expected to complete in the first quarter of 2006 and will add more than 100,000 square feet of manufacturing space to the market.



## Economics

The unemployment rate in Orange County was 3.7 percent in November 2005, down from a revised 3.8 percent in October 2005, and below the

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year-ago estimate of 3.9 percent. This compares with an unadjusted unemployment rate of 5.1 percent for California and 4.8 percent for the nation during the same period. Between October and November 2005, non-farm wage and salary employment in Orange County increased by 6,100, bringing the total number of jobs to 1,499,600. Trade, transportation and utilities reported the largest payroll increase (up 2,100 jobs) as stores hired staff for the holiday shopping season. Nearly 94 percent of the gain was in retail trade, led by advances in general merchandise stores, clothing and clothing accessories stores, miscellaneous store retailers, and electronics and appliance stores. Between September 2004 and September 2005, total non-farm employment was up 27,700 jobs, an increase of 1.9 percent. Professional and business services gained 11,900 jobs with nearly 70 percent of the increase in administrative and support services, which includes temporary help firms.

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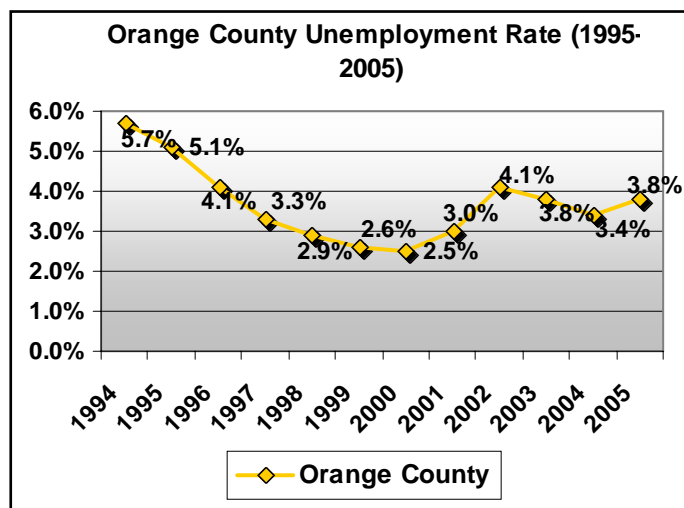
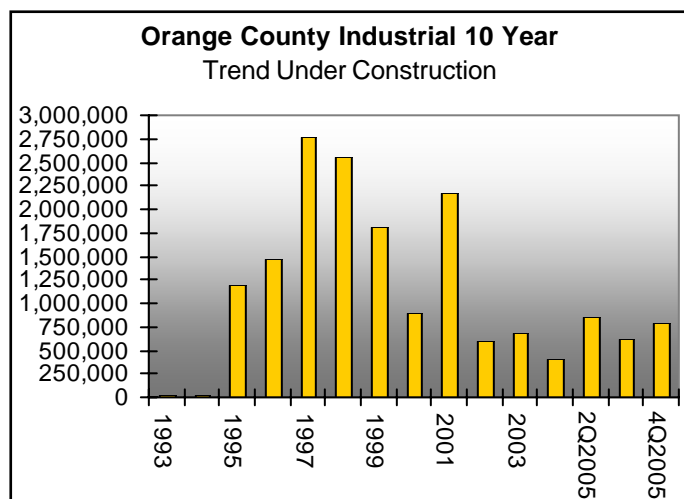
## Opportunities & Challenges

The biggest challenge facing most industrial users is the lack of available space on the market. Demand for industrial space increased significantly in the latter half of 2005 and as result available space continues to be difficult to find. Most industry experts are predicting an increase in rents in the 4 to 7 percent range next year. The highest rents paid now are in the South County, at about \$1.09. As a result, industrial users are heading into the Inland Empire market.

On the sale side, sellers will continue to benefit from rising sale prices as demand outstrips supply. As the supply of quality properties shrinks, lease rates are also expected to rise. Small buildings for sale are the hottest product in Orange County as buyers take advantage of attractive financing. However, the main challenge for investors continues to be sourcing suitable opportunities.

## Forecast

Property values of industrial real estate are predicted to continue upward over the short-term as continued low interest rates fuel both user and investor sale activity. Investor activity will remain high in Orange County despite low cap rates in the 5 to 6 percent range as a result of increasing asking rents. Owner-users will continue to aggressively seek ownership opportunities while interest rates remain low and the overall economy is thriving. New industrial condo development and condo conversions will provide space for much of the owner-user demand. The strength of the Orange County economy is expected to temper the effects of rising interest rates on tenant, user and investor demand for industrial real estate.



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## Major Transactions

Grubb & Ellis is pleased to announce that it represented the following companies in industrial transactions during the fourth quarter of 2005:

**LogoMark, Inc.**  
Lease  
122,260 SF  
Robert Griffith, Sr. Vice President  
Jon Nesbitt, Vice President  
Wade Tift, Vice President  
Tustin

**Vanderbilt Chrysler, LLC**  
Lease  
34,548 SF  
Gary Allen, Sr. Vice President  
Ryan Jett, Associate  
Doug Mathews, Sr. Vice President  
Irvine

**R. Wackeen & Associates, Inc.**  
Lease  
12,280 SF  
Troy Williams, Sr. Vice President

**Graybar Electric Company**  
Lease  
12,000 SF  
Stephen Schaner, Senior Associate  
Anaheim

## Industrial Market Terms and Definitions

**Inventory:** Industrial Inventory includes all multi-tenant, single tenant and owner-occupied buildings at least 10,000 square feet.

**Construction Type:** Speculative ("spec") construction is designed to attract tenants likely to be in the market when the project is leasing. Build-to-suit construction is designed for a specific tenant.

**Industrial Product Types:** Industrial buildings are categorized as warehouse/distribution, general industrial, R&D/flex and incubator based on their physical characteristics including percent office build-out, clear height, typical bay depth, typical suite size, type of loading and typical uses.

**Vacancy and Availability:** The vacancy rate is the amount of physically vacant space divided by the inventory. The availability rate is the amount of space available for lease divided by the inventory.

**Net Absorption:** The net change in physically occupied space over a period of time.

**Asking Rent:** The dollar amount asked by landlords for available space expressed in dollars per square foot per year in most parts of the country and dollars per square foot per month in areas of California and selected other markets. Industrial rents are expressed as triple net where all costs including, but not limited to, real estate taxes, insurance and common area maintenance are borne by the tenant on a pro rata basis.

**Average Weighted Asking Rent:** An average market rent where the asking rent for each building in the market is weighted by the amount of available space in the building.

