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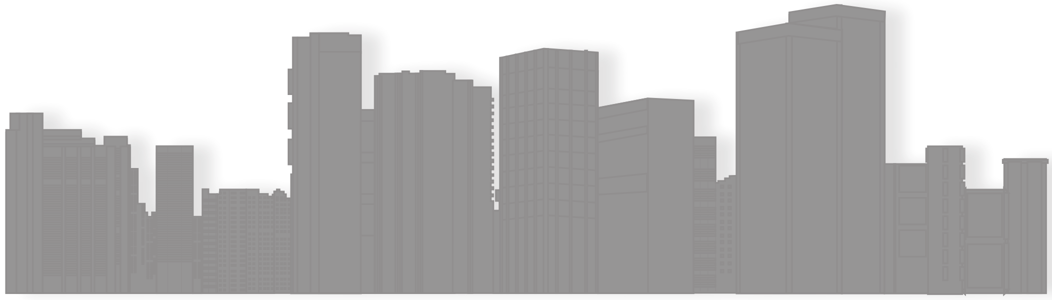

Allen Matkins | UCLA Anderson Forecast

COMMERCIAL REAL ESTATE SURVEY

LOS ANGELES | ORANGE COUNTY | SAN DIEGO | SAN FRANCISCO
EAST BAY | SILICON VALLEY | INLAND EMPIRE

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More detail on the construction and methodology behind this survey can be found in the Allen Matkins/UCLA Anderson Forecast California Commercial Real Estate Survey Support Document available at www.uclaforecast.com.

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 is designed to provide more accurate information on future office, industrial and multifamily space in major California geographical markets. This fourteenth survey covers the major Southern California and Bay Area markets for office, industrial and multifamily space.

The Allen Matkins and UCLA Anderson Forecast Partnership

At Allen Matkins, the top-ranked California-based law firm servicing the real estate industry according to Chambers & Partners, 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 60 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.

John M. Tipton
Partner, Real Estate Department
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California Commercial Real Estate Survey: The Return of the Cranes

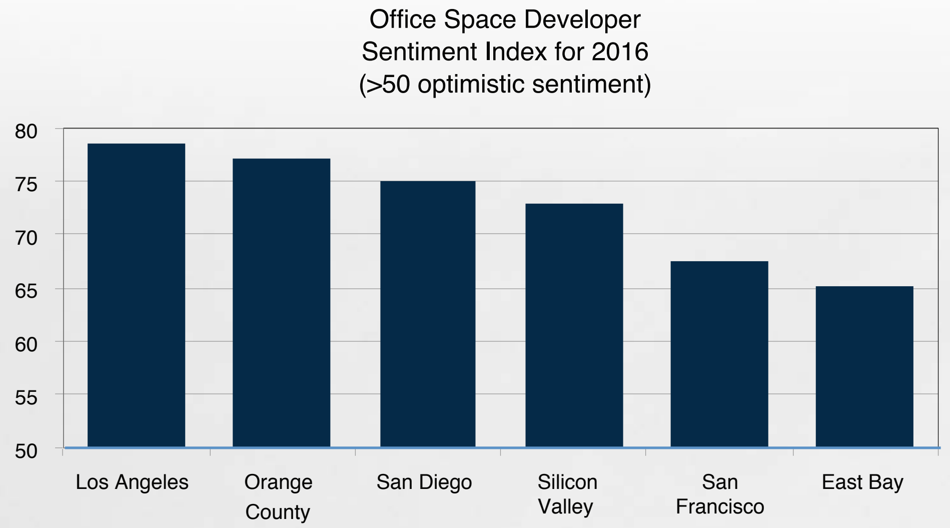
Jerry Nickelsburg
Adjunct Professor of Economics, UCLA Anderson School
Senior Economist, UCLA Anderson Forecast

In the June 2013 Allen Matkins UCLA Anderson Forecast Survey we observed that the cooling in developer optimism with regard to vacancy rates signaled a sense that demand and supply in the markets we surveyed were coming into balance. With gridlock in Washington subsiding, or at least becoming a normal state of affairs, developers are now viewing 2016 as a year in which commercial real estate markets in California tighten and opportunities for profitable new investments increase. In all but the Bay Area Industrial Markets, our developer panels indicated they would accelerate their current development activity and in all markets developer sentiment improved.

The Allen Matkins UCLA Anderson Forecast Survey and Index project compiles the views of commercial real estate developers 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 environmental issues often take much longer). The panel's view on occupancy and rental rates are key ingredients to their own business plans for new projects, and as such, the survey provides insight to 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 the office market in Silicon Valley in 2016, then the initial work for a new project with an expected ready for occupancy date of 2016--a business plan, preliminary architecture, and a search for financial backing--would have to begin no later than 2013. However the converse is not true. A developer could be optimistic about 2016 and still not find the case compelling enough to begin a new development.

Since the end of the Great Recession we have seen developer optimism spread to all markets and types of commercial space we survey. Today's nascent recovery in new non-residential building predicted by the Survey in 2010 and subsequent Surveys is evident. The current Survey, completed in December 2013, is stronger than the previous one and indicates markets that are not normalizing but are experiencing a shortage of supply. The increased optimism is consistent with job growth in California. From Sonoma to Santa Clara, Ventura, Orange and San Diego Counties and West LA, coastal California is generating jobs at a faster rate than the U.S. This clear economic improvement is now resulting in the requisite developer confidence for initiating new projects. As with the Survey Panels, The Anderson Forecast released in December projects the current expansion of employment to continue through the 2016.

Figure 1.
Office Space Developer Sentiment Index



CALIFORNIA OFFICE SPACE MARKETS

Two panels, one for the Bay Area and one for Southern California, were asked questions about the evolution of Office Markets three years hence. The highest numerical Sentiment Indexes are in Orange County, Los Angeles and San Diego. This is followed by Silicon Valley, San Francisco, and The East Bay. Although each index in the survey is solidly in the optimistic zone, they no longer correlate strictly with job growth in office using employment over the past three years.[1] The surge in sentiment in Southern California is likely due to the increased rate of job growth in the region. In the Bay Area, job growth is still sizzling compared to the U.S. but at a slightly slower rate than previously experienced.

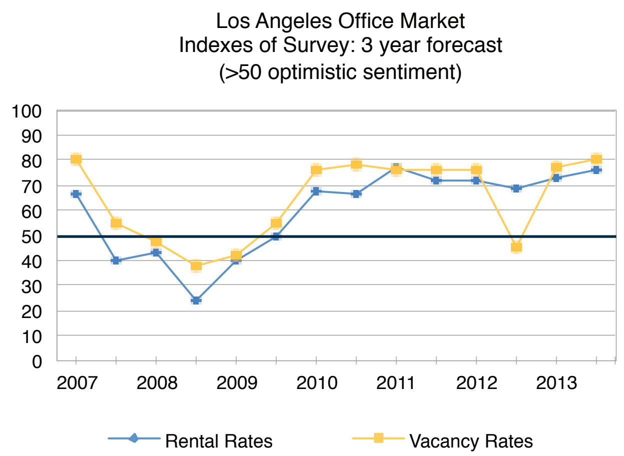
In The Bay Area worries about the Fiscal Cliff and national economic policy on the demand side and a sense that sufficient building was taking place to keep vacancy rates at or above current levels in 2016 persisted through last summer. In the latest survey these concerns have subsided and the sentiment with respect to vacancy rates moved solidly into the optimistic range. This indicates a new view of 2016, one in which both rental rates and occupancy rates are increasing.

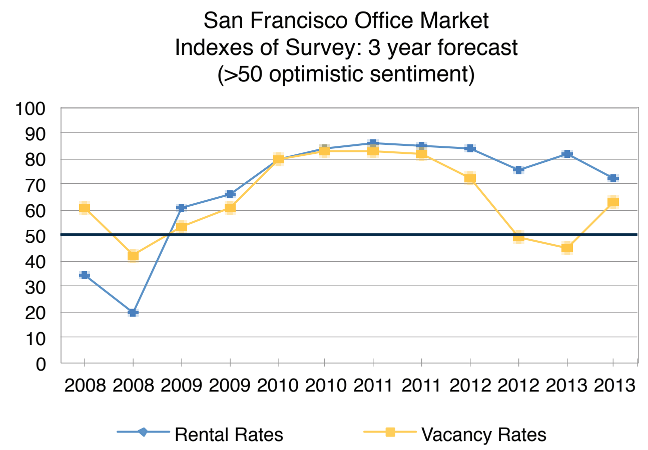
The Anderson Forecast for Bay Area Employment is for the number of non-farm payroll jobs in 2016 to finally reach and subsequently exceed the peak previously achieved in the days before the 2001 dot-com bust. This solid job growth will generate an increasing demand for office space. Notable in this equation is the fact that even though job growth in the East Bay has slowed of late, the panel remains optimistic for that sub-market as well.

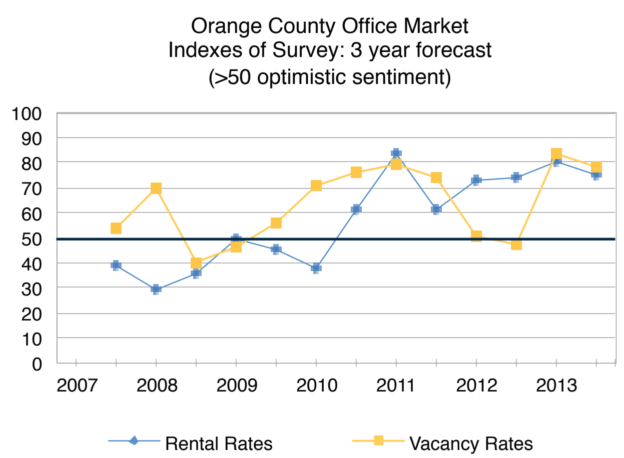
By contrast, the Southern California Office Space Indexes were unchanged over the last six months. The Southland seems to have sloughed off the jitters about the impact of gridlock in Washington earlier than the Bay Area on the demand side and is now experiencing a tightening on the supply side. A key difference between the two regions on the supply side stems from the Bay Area leading in this economic recovery and therefore generating the basis for the development of new supply of office space earlier than Southern California.

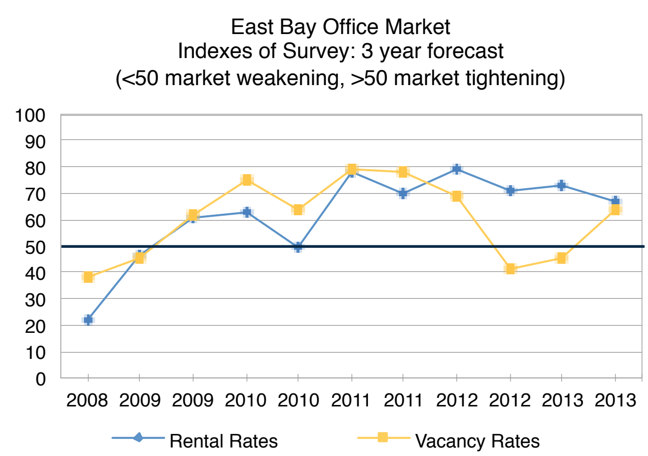
The differential in the view of the two panels is reflected in the fact that 70% of the Southern California Panel members stated that their companies would be starting one or more new projects in the next twelve months while 52% of the Bay Area Panel are intending to do so. Though these may seem to be different, they are in fact much the same were one to factor in the percentages of the previous surveys. Further evidence is found in a surge in the value of office building construction permitted in California of 27% over the past year.

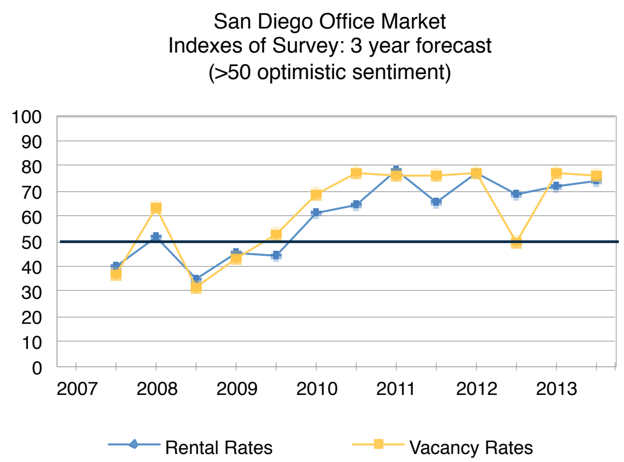
Figure 2-7.
Office Space Developer Sentiment Indices

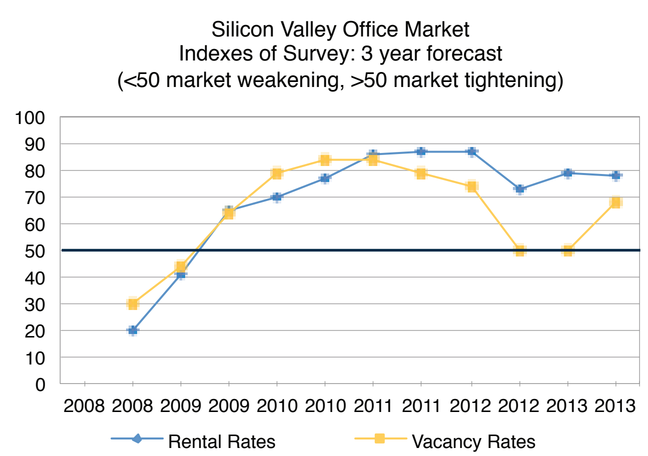












CALIFORNIA INDUSTRIAL SPACE MARKETS

Industrial Space is comprised of two distinct markets, manufacturing and warehousing. Although each geography is a mixture of both, San Francisco, Silicon Valley and Orange County can be broadly characterized as being more heavily manufacturing, the East Bay, and Los Angeles a mix of the two, and the Inland Empire by warehousing. The basic underlying economic forces in industrial markets are California manufacturing, the export of goods to Asia and Mexico, and consumer goods from the manufacturing centers of Asia brought into the U.S. through the California's ports.

The bottom line for industrial space in California is one of strongly positive developer sentiment. Though The Bay Area Indexes declined slightly, it was not a significant decline, and Southern California Indexes firmed slightly. The difference can be attributed to the emergence of Eurozone and Japan from recessions and the strengthening of economic growth in China. With an increased volume of trade through the Southern California ports comes an increased demand for warehouse space. In the Bay Area, the demand for industrial space is increasing, but without the added external demand push found in the Southland.

It is important to note that the fall-off in the value of new permits issued for industrial space in 2013 is not indicative of a pull back or turning point in the market, but an adjustment of the rush to begin new projects in 2012. Our June Bay Area Panel stated that 67% of them would be beginning one or more new industrial space developments in the next twelve months. Some of those have begun and the decline to 25% is reflective of that. In Southern California the percentage stating plans to initiate one or more new developments increased to 72%.

Figure 8.
Volume of Goods Movement Through Ports

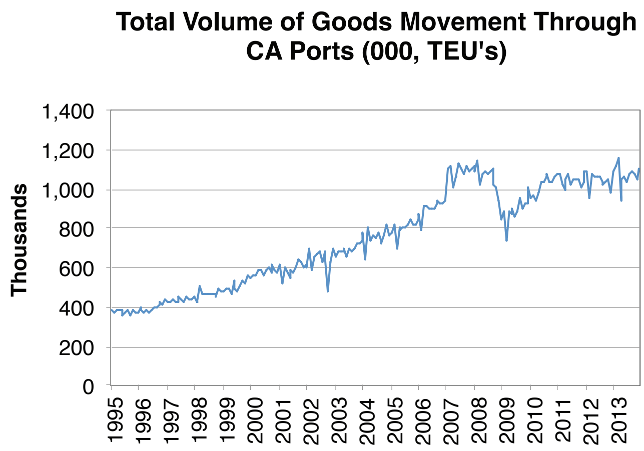
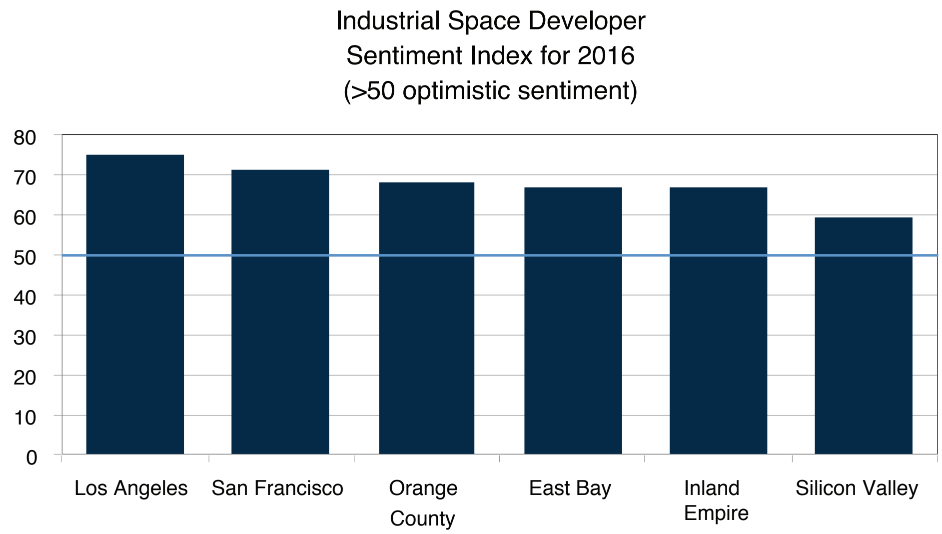


Figure 9.
Industrial Space Developer Sentiment Index



CALIFORNIA MULTI-FAMILY HOUSING SPACE MARKETS

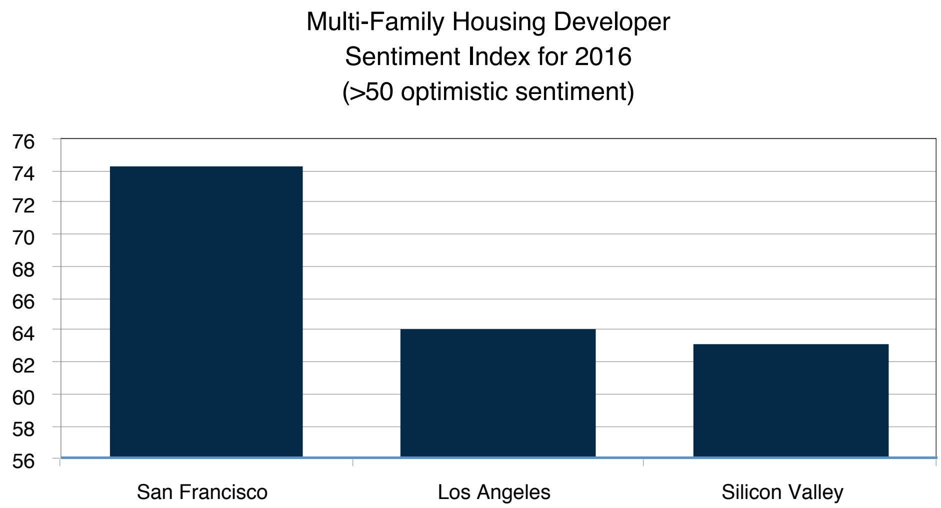
The current survey marks the fourth Allen Matkins UCLA Anderson Forecast survey of multi-family housing developers. In each of the three markets surveyed, Los Angeles, San Francisco, and Silicon Valley, the panel continued to be optimistic about the prospects for returns on multi-family housing investments in the coming three years.

The survey indicates that the market outlook is sufficiently bright for all of our Bay Area panelists and 65% of our Los Angeles panelists to state that they would be beginning one or more new developments in the coming 12 months. This corresponds to a white-hot market in San Francisco and Silicon Valley with occupancy rates above 97% and rental rate growth among the highest in the nation. In Los Angeles, it is all about location. There are similar occupancy and rental rate growth on the Westside to San Francisco and Silicon Valley and less so in the inland parts of the County.

The boom in multi-family home construction is also evident in the permitting numbers. The cumulative percentage increase in permits through the November 2013 (the date of the survey) are 19.6% in the City of Los Angeles, 18.2% in San Francisco and 44.2% in San Jose. The smaller jurisdictions in the survey regions were mixed. For example, Santa Monica and Pasadena had a decrease in multi-family permits this year after the approval of several large projects in 2012 and Sunnyvale went from 0 to over 300 new home permits. Overall each of the regions permitted a significantly larger number of multi-family units than in the previous year.

The Survey Panel's optimism in each market is a reflection both of the strength of demand and a sense that even with building permits increasing at a rapid clip, there will not be enough multi-family housing in late 2016 to stem the rise in rental and occupancy rates. Demographics, limited land and continued growth in payroll jobs in these markets are driving the demand for multi-family housing and our Survey Panels view this as a longer-term trend.

Figure 10.
Multi-Family Housing Developer Sentiment Index



SUMMARY

The Allen Matkins / UCLA Anderson Forecast survey was designed to improve forecasting the evolution of commercial real estate markets. Although the survey is still relatively new and there is as yet not enough data for rigorous statistical analysis, interpretation of the snapshots provided by each survey provides insight into our statistically based forecasts. The optimism about 2016 in the Survey is an important indicator of both the probability of new additions to stock being started over the next two years and of opportunities for new investment in office and industrial space. Importantly, the Indexes provide a window into the evolution of commercial real estate markets in California. In the previous survey developer optimism was consistent with all markets normalizing in early 2016. The current survey projects that the normalization will be short lived and markets will tighten once again as 2016 rolls to a close.

1. http://www.edd.gov

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UCLA Anderson
FORECAST

Allen Matkins

Founded in 1952, the UCLA Anderson Forecast is one of the most widely watched and often-cited economic outlooks for California and the nation. Award-winning for its accuracy, the UCLA Anderson Forecast has a long tradition of breaking with the consensus forecast to be among the first to spot turning points in the economy.

The forecasting team is credited as the first major U.S. economic forecasting group to predict the recession in 2001. The team was also ahead of the pack in predicting both the seriousness of the early-1990s downturn in California, and the strength of the state's rebound since 1993. In 2002, the UCLA Anderson Forecast was among the first to identify the growing imbalances in the housing sector and correctly predicted sharply declining sales volumes and weak prices when rates returned to normal.

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Allen Matkins is located on the Web at www.allenmatkins.com.

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