

SUMMARY

Market Change

Compared to 2017

Sales Transactions	▼	DOWN
Sales \$ Volume	▼	DOWN
Lease Transactions	▲	UP
Lease \$ Volume	▲	UP
Lease Rates	▼	DOWN
Net Absorption	▼	NEGATIVE
Vacancy	▲	UP

Change values are for all commercial property types since 1/1/2018.

Highlights

- Commercial sales volume picked up momentum in Q2; however, inventory has expanded to its highest level since 2012.
- Goleta to date has seen 10 leases for spaces larger than 10,000 sf, well above the recent trend.
- Retail vacancies are peaking on Santa Barbara's State Street corridor, and the blocks near Paseo Nuevo are seeing the fastest expansion of available space.
- Industrial vacancy continues to be concentrated in Goleta where the rate is above 5%.

COMMERCIAL SALES

At the midpoint of 2018, South Coast sales activity has slowed compared to prior years. Both the number of commercial transactions and dollar volume (excluding hotels) have decreased nearly 30% compared to the prior 5-year averages. Transaction momentum did pick up in the second quarter, suggesting that the activity during the first quarter was indeed diminished by the Thomas Fire and Montecito mudslide. Additionally, properties currently under contract have the potential to produce a substantial bump in volume in the second half of the year.

Santa Barbara has been the focus of most of the action to date. Two medical properties sold in the second quarter, including the 18,200 sf building at 3045 De La Vina St, which traded for \$9.5 million. The mixed-use property at 2801 De La Vina St (home to Nick Rail Music) was purchased by a local investor for \$3.4 million in June.

One unheralded area of recent sales activity is the Lagoon District/Lower Eastside area of Santa Barbara. With Haley and Gutierrez Streets as its artery and vein, the neighborhood has been evolving gradually into a sprawling variation on the Funk Zone concept, dotted with "adaptive" repurposing of industrial property for beer and wine, artisan retail, and office use. The area from Cota Street to US 101 and from Milpas

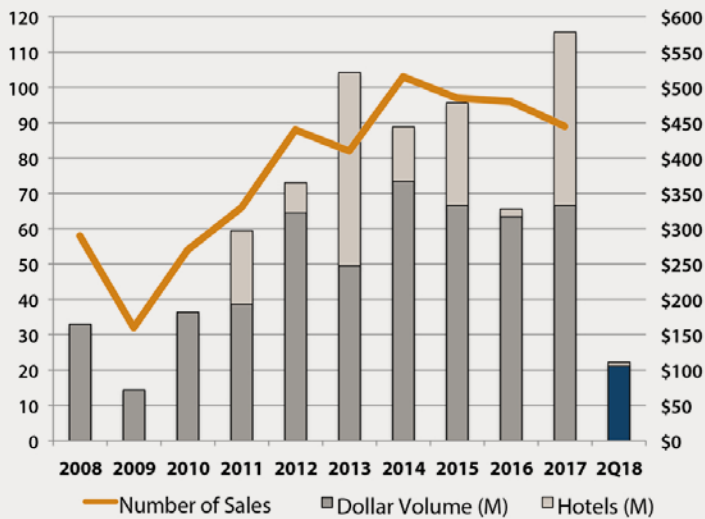
Street to Anacapa Street has produced 21 sales valued at \$47.3 million over the past 18 months. Almost all of those properties had either industrial improvements or undeveloped land. Most recently, 519 Garden St, 100-102 E Haley St, 719 Bond Ave, and 314 Edison Ave all sold in the second quarter.

Activity in Goleta and Carpinteria was subdued in the first two quarters, with just three commercial sales in each city. In the second quarter, the City of Goleta purchased the warehouse property at 27 S La Patera Ln from Direct Relief International for an undisclosed sum. The Cantwell's Market building at 2580 Lillie Ave in Summerland was purchased by an owner-user for \$5.4 million.

Looking at supply, a growing number of South Coast owners have concluded it is time to sell. The number of properties for sale has rocketed upward 54% from a historic low at the end of 2017. Properties for sale have increased in all three cities, with the biggest jumps in office and retail. Some of the increase in inventory stems from the slow sales activity toward the beginning of the year. However, 46 of the 63 available properties have come to market since the beginning of the year.

Retail property for sale in Santa Barbara is at the highest level on record with 19 listings available. This mirrors the national trend, according to a report by the Boulder Group, in which retail owners seeking to sell ahead of rising cap

South Coast Sales



rates are expanding inventory in major markets. In Santa Barbara, owners on State Street may also be aiming to sell ahead of rising vacancy. There are nine properties for sale along the downtown State Street corridor. That retail stretch has already seen five transactions to date this year: the sales of the Macy's (701 State St) and Saks (1001 State St) buildings in the first quarter, followed by three sales on the 1200 block in the second quarter.

Will the South Coast's largest inventory since 2012 lead to rebounding sales volume in the coming quarters? Our brokers report that solid investor demand persists for real estate with a clear path to a competitive return, especially given uncertainty in other investment classes, such as stocks and commodities. However, properties that are more of an unknown quantity will face greater pricing headwind in conditions of expanded supply. Interest rates are still low in the long view, but their gradual rise is squeezing the margin for risk that has enabled much of the sales activity during the past five years.

OFFICE LEASING

Available office space has increased in all three market cities since year end, pushing the combined South Coast vacancy rate to 9.2%, the highest level on record. However, some of that rise is due to a few very large

spaces becoming available, rather than a dramatic shift in trend.

In Goleta, the largest new availability is the 105,257 sf building at 71 S Los Carneros Rd in Goleta, which is occupied by Apeel Technology for another 18 months, under sublease from Allergan. Despite this single large space coming back on the market, the underlying trend in Goleta is toward contraction. In fact, there were 10 leases signed to date for spaces larger than 10,000 sf, far exceeding the pattern of recent years. Only one of these leases was a renewal: Raytheon exercised its option on 121,131 sf at 75 Coromar Dr. The second quarter saw large leases by Seek Thermal, Resonant, EmployBridge, and Toyon Research. We stand by our characterization two quarters ago that Goleta's office market is "resurgent."

In contrast to Goleta, the trend in Santa Barbara points toward higher vacancy, which at midyear stands at a historically high rate of 6.2%. Both square feet and the number of spaces available in Santa Barbara have expanded more than 60% over the past three years. The UCSB Economic Forecast Project's May report for Santa Barbara County cites a 12% decrease in professional and business services sector employment during the past three years. Since much of Santa Barbara's office property is used by professional and business services, this shift in employment may be sapping demand for office space. To date in 2018, absorption has decreased 18% compared to last year. In the second quarter, the 19,738 sf building at 3820 State St came to the market, which was the final straw that pushed the vacancy rate to an unprecedented level.

Increased vacancy is evidently pressing Santa Barbara landlords to greater pricing concessions. Since the beginning of 2017, the average discount that landlords conceded to secure a new tenant increased 230 basis points, compared to

OFFICE

Vacancy	7.7%
Available Space	▲ UP
Gross Absorption	▲ UP
Asking Rates	▲ UP
Achieved Rates	▼ DOWN

Summary for the entire South Coast.
Change indicators are since 1/1/2018.

leases completed from 2013 to 2016. On the other hand, Santa Barbara's high vacancy has not affected deal volume; the first half of 2018 produced 56 lease transactions, which is right on par with the past five years.

In Carpinteria, five of the six leases to date were completed in the second quarter, including Starr Indemnity & Liability's lease of 10,395 sf at 1001 Mark Ave. Vacancy has rebounded significantly since Procore's leasing spree ended in 2016, but the current rate of 5.2% is still relatively low by historical standards.

RETAIL LEASING

State Street has seen a disconcerting sequence of departing tenants in the past six months, including Aaron Brothers, Verizon, Chipotle, Pinkberry, Staples, and Peet's Coffee. The plight and future of State Street continues to be a prominent topic of attention and concern, and in an effort to inform the discussion, Hayes Commercial recently completed our most thorough survey to date of the State Street corridor from the waterfront to Sola Street. In a nutshell, our research confirms that there are more spaces available now

than during the peak of the last recession. The vacancy rate on State has been on an upward trend since a low point of 3.0% in Q1 2015, while the US retail sector and retail elsewhere in Santa Barbara have produced relatively stable vacancy over the same period.

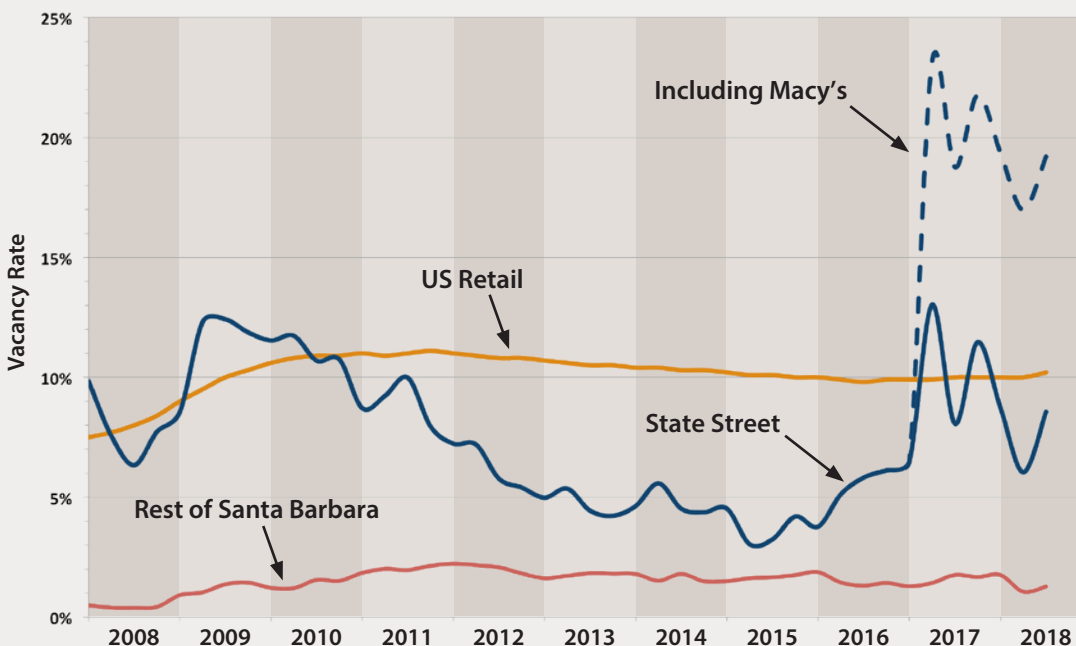
In our analysis, we divided the corridor into four segments and found that the Paseo Nuevo area (600 to 900 blocks) has been disproportionately impacted by the rise in vacancy. Since Q1 2015, this four-block stretch has added available spaces at twice the rate of the adjacent segments on either side. Obviously, as home to the Macy's building this segment also bears the vast majority of State Street's available square footage. Yet, even excluding the Macy's building, the vacancy rate for these blocks is 11% and has risen at double the rate of the neighboring segments over the past three years. It's not clear what has happened during the past three years that would explain this

RETAIL

Vacancy	3.0%
Available Space	▼ DOWN
Gross Absorption	▲ UP
Asking Rates	▼ DOWN
Achieved Rates	▼ DOWN

Summary for the entire South Coast.
Change indicators are since 1/1/2018.

State Street Retail Vacancy (00 to 1300 Blocks)



Source: Hayes Commercial Group, US Retail data from REIS, Inc

phenomenon, but these blocks have the highest concentration of national retailers and the highest rents along the corridor. Whatever the reason, it certainly exacerbates the image of State Street's decline when prime blocks adjacent to a regional mall have the steepest vacancy growth.

Not all of the news is grim, though. Leases are being signed, and State Street continues to avoid stagnation despite high vacancy. Along the

downtown corridor, 10 leases have been completed to date, including the renewal by Apple at 928 State St. Montecito restaurateurs are bringing variations on existing concepts to State Street as the operators of Tre Lune will launch Due Lune in 3,660 sf at 1 State St, and Trattorie Mollie's sister restaurant is already open at 1218 State St. The beleaguered 6,750 sf corner space at 400 State St was leased by Habitat Home and Garden.

In Goleta, the big story is Kmart's closing in October, to be replaced by Target following upgrades to the center. This change will further establish the Hollister and Storke area as the center of gravity for Goleta retail. The effects on the rest of Goleta are already evident. There is four times more retail space available east of the airport than west of the airport toward Storke Road. For example, Calle Real Center has been struggling to attract and retain tenants; despite two leases completed this year, there remain seven spaces currently available comprising 18% of the property. The difference in pricing is also telling: landlords are asking a 42% premium per square foot west of the airport compared to the eastern part of the city. This echoes the phenomenon in most American suburbs in which strip malls and grocery-anchored centers located near "big box" centers have a harder time retaining customer traffic. To keep this in perspective, though, Goleta's vacancy rate is still remarkably low at 1.9%, compared to the national average of 10.2%.

INDUSTRIAL LEASING

On the industrial scene, Santa Barbara and Carpinteria are continuing the trajectory of very low vacancy, while Goleta's vacancy is on the rise due to emerging large availabilities. There is ample demand from smaller tenants, but larger spaces are proving harder to lease. Based on tenant requirements currently in the market, we expect this bifurcation of demand to continue in the near future.

Goleta's industrial vacancy has nearly doubled since a year ago and currently stands at a rate of 5.2%, the highest level since 2012. Aside from Curvature's short-term renewal of 57,600 sf at 70 Cremona Dr, there were only five industrial leases by midyear, all smaller spaces totaling 10,871 sf. Vacancies created by Channel Technologies, Direct Relief International, FLIR, and others have resulted in an unusual number of large industrial spaces on the market. Smaller spaces are leasing, but tenants looking for large spaces are few.

In Santa Barbara the number of lease transactions to date is trending 30% above the prior 5-year average. However, most of the leases have been for smaller spaces. Standing desk accessory company FluidStance leased 3,277 sf at 121 E Mason St in the Funk Zone. There were two renewals of approximately 12,000 sf each at 1 N Calle Cesar Chavez by Town & Country Event Rentals and US Air Conditioning Distributors. There are only six spaces available, comprising a wispy vacancy rate of 0.35%. Asking rates vary substantially depending on location; not surprisingly, the Funk Zone is the high-rent area of town, where landlords are asking a premium of about 50 cents per square foot per month.

In Carpinteria, there are only three spaces available, all with asking rates comparable to what is being asked for office space in that city. The 24,030 sf building at 6384 Via Real was brought to the market in the second quarter, as Northrop Grumman plans to vacate by the end of the year. There were no leases signed in the second quarter and just two in the first, one of which was a renewal.

INDUSTRIAL

Vacancy	2.7%
Available Space	▲ UP
Gross Absorption	▼ DOWN
Asking Rates	▲ UP
Achieved Rates	▲ UP

Summary for the entire South Coast.
Change indicators are since 1/1/2018.

To receive future Hayes Commercial Group reports electronically, please visit HayesCommercial.com and subscribe.

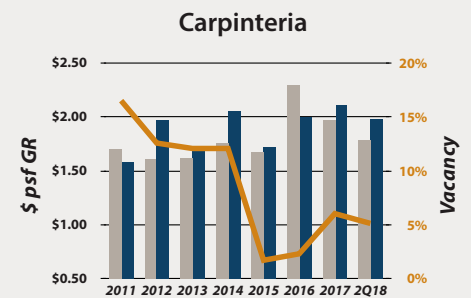
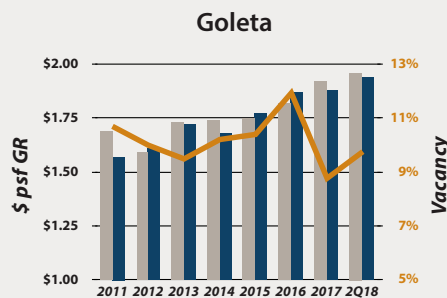
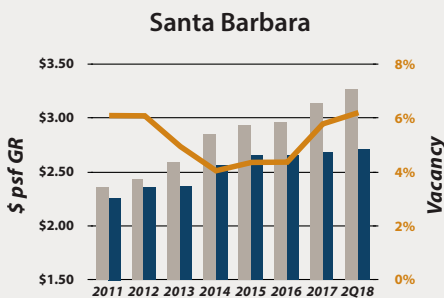
OFFICE LEASING

Market	Available	Change*	Gross Absorption	Change*	Asking Rate	Change*	Achieved Rate	Change*
Santa Barbara	312,775	7.2%	151,358	-20.2%	\$3.27	4.2%	\$2.71	1.3%
Goleta	443,578	11.3%	361,835	114.4%	\$1.96	1.8%	\$1.94	2.8%
Carpinteria	32,702	-14.9%	16,926	26.8%	\$1.78	-10.0%	\$1.98	-\$0.06
Totals	789,055	8.3%	530,119	42.6%	\$2.47	2.4%	\$2.16	-6.0%

* Since 1/1/2018. Average rate totals are weighted by square footage.

Office Vacancy vs. Achieved & Asking Rates

— Vacancy Rate ■ Asking Rate ■ Achieved Rate



2018 Office Leases of Note



6300 Hollister Ave, Goleta
30,863 sf – Seek Thermal



175 Cremona Dr, Goleta
27,037 sf – Resonant



3660 State St, Santa Barbara
11,930 sf – Wells Fargo Advisors



1001 Mark Ave, Carpinteria
10,395 sf – Starr Indemnity & Liability

Largest Available Spaces

71 S Los Carneros Rd, Goleta
112,480 sf Allergan building

70 Castilian Dr, Goleta
86,246 sf in Castilian Tech Ctr

650 Ward Dr, Goleta
30,000 sf Office/R&D

5385 Hollister Ave, Goleta
21,504 sf Pacific Tech Center

5540 Ekwil St, Goleta
20,829 sf in Santa Barbara Tech Center

3820 State St, Santa Barbara
19,738 sf in EmployBridge building

6398 Cindy Ln, Carpinteria
19,063 sf in Office & Warehouse

1020 State St, Santa Barbara
19,000 sf in Brownstein building

530 Chapala St, Santa Barbara
18,792 sf Sonos sublease

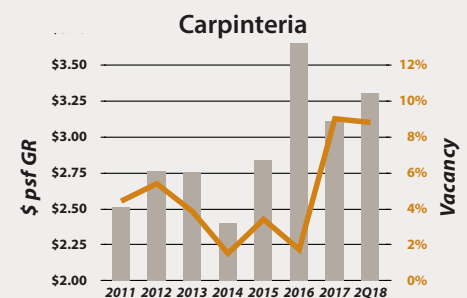
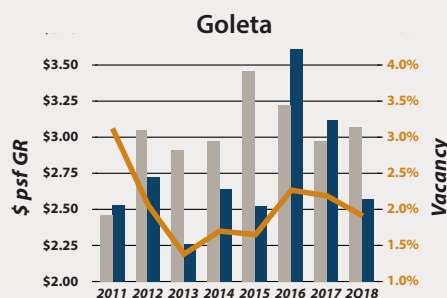
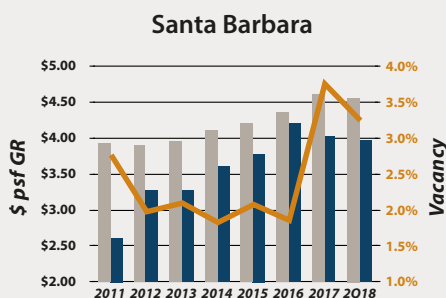
RETAIL LEASING

Market	Available	Change*	Gross Absorption	Change*	Asking Rate	Change*	Achieved Rate	Change*
Santa Barbara	341,817	-13.4%	65,878	9.6%	\$4.56	-1.3%	\$3.97	-1.2%
Goleta	76,869	-12.6%	53,943	285.9%	\$3.07	3.2%	\$2.57	-17.7%
Carpinteria	32,302	-2.3%	2,193	-19.7%	\$3.30	5.9%	\$1.75	-32.3%
Totals	450,988	-12.6%	122,014	58.8%	\$4.21	-0.6%	\$3.31	-13.0%

* Since 1/1/2018. Average rate totals are weighted by square footage.

Retail Vacancy vs. Achieved & Asking Rates

— Vacancy Rate ■ Asking Rate ■ Achieved Rate



2017 Retail Leases of Note



7035 Marketplace Dr, Goleta
30,147 sf – HomeGoods



928 State St, Santa Barbara
18,743 sf – Apple, Inc



400 State St, Santa Barbara
6,750 sf – Habitat Home and Garden



1 State St, Santa Barbara
3,660 sf – Due Lune

Notable Available Spaces

- 701 State St, Santa Barbara**
135,000 sf former Macy's
- La Cumbre Plaza, Santa Barbara**
29,738 sf various spaces
- Calle Real Center, Goleta**
21,137 sf various spaces
- 187 S Turnpike Rd, Santa Barbara**
19,739 sf in Turnpike Shopping Center
- 410 State St, Santa Barbara**
17,000 sf former Staples
- 32 W Carrillo St**
10,026 sf former Greyhound site
- 29 N Milpas St, Santa Barbara**
10,008 sf former Trader Joe's
- 185 S Patterson Ave, Goleta**
9,548 sf in Patterson Center
- 11 Anacapa St, Santa Barbara**
7,500 sf in Funk Zone

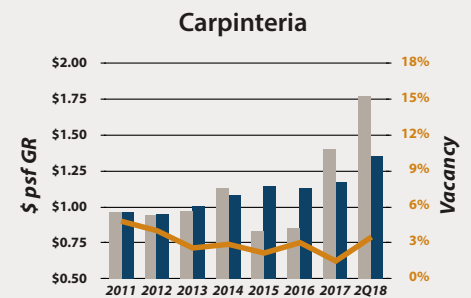
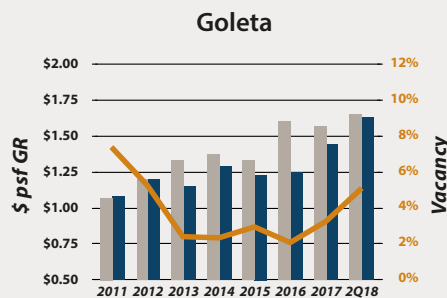
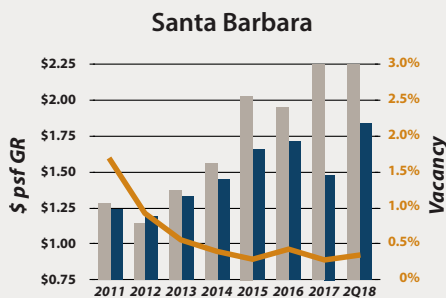
INDUSTRIAL LEASING

Market	Available	Change*	Gross Absorption	Change*	Asking Rate	Change*	Achieved Rate	Change*
Santa Barbara	16,741	24.0%	47,899	-39.6%	\$2.28	-10.0%	\$1.84	24.8%
Goleta	217,027	56.9%	68,471	-25.1%	\$1.65	5.1%	\$1.63	13.4%
Carpinteria	46,730	133.7%	14,909	-59.9%	\$1.77	26.2%	\$1.35	14.9%
Totals	280,498	63.2%	131,279	-36.8%	\$1.71	5.0%	\$1.68	19.3%

* Since 1/1/2018. Average rate totals are weighted by square footage.

Industrial Vacancy vs. Achieved & Asking Rates

— Vacancy Rate ■ Asking Rate ■ Achieved Rate



2017 Industrial Leases of Note



80 Coromar Dr, Goleta
57,600 sf – Curvature



525 Maple Ave, Goleta
13,509 sf – DSY Education Corp



1 N Calle Cesar Chavez, Santa Barbara
11,845 sf – US Air Conditioning



6485 Calle Real, Goleta
4,395 sf – Szkutak Wine Ventures

Largest Available Spaces

- 340 Storke Rd, Goleta**
29,300 sf sublease
- 30 S Calle Cesar Chavez, Santa Barbara**
25,570 sf sublease
- 859 Ward Dr, Goleta**
24,412 sf
- 6384 Via Real, Carpinteria**
24,030 sf
- 30 S La Patera Ln, Goleta**
23,000 sf
- 153 Castilian Dr, Goleta**
22,001 sf
- 5756 Thornwood Dr, Goleta**
20,794 sf
- 550 Linden Ave, Carpinteria**
20,000 sf
- 879 Ward Dr, Goleta**
18,253 sf

COMMERCIAL SALES

2017 Commercial Sales of Note



1001 State St, Santa Barbara
\$18,500,000



701 State St, Santa Barbara
\$12,000,000



1001 Coast Village Rd, Montecito
\$7,700,000



2580 Lillie Ave, Summerland
\$5,400,000

Highest Priced Properties For Sale

7414-7418 Hollister Ave
Goleta Office • 162,174 sf
\$33,500,000

600 Pine Ave
Goleta Office/R&D • 83,479 sf
\$22,950,000

Cabrillo Business Park
Goleta Land • 490,050 sf
\$21,508,112

1486 E Valley Rd
Montecito Retail • 6,357 sf
\$18,395,333

900 State St, Santa Barbara
Santa Barbara Retail • 38,015 sf
\$17,700,000

559 San Ysidro Rd, Montecito
Montecito Office • 9,626 sf
\$12,750,000



EXPERIENCE. INTEGRITY. TRUST.
SINCE 1993

Greg Bartholomew
805-898-4395
greg@hayescommercial.com
lic. 01131126

Christos Celmayster
805-898-4388
christos@hayescommercial.com
lic. 01342996

Francois DeJohn
805-898-4365
fran@hayescommercial.com
lic. 01144570

Stephen Hayes
805-898-4370
steve@hayescommercial.com
lic. 00827640

Michael Martz
805-898-4363
michael@hayescommercial.com
lic. 01391838

Caitlin McCahill
805-898-4374
caitlin@hayescommercial.com
lic. 01893341

Dan Moll
805-898-4380
dan@hayescommercial.com
lic. 00885073

Greg Moss
805-898-4382
gmoss@hayescommercial.com
lic. 01069933

Liam Murphy
805-898-4385
liam@hayescommercial.com
lic. 01439777

Kristopher Roth
805-898-4361
kris@hayescommercial.com
lic. 01482732

Dylan Ward
805-898-4392
dylan@hayescommercial.com
lic. 01472452