

COMMERCIAL SALES

	YTD 2019	vs 2018*	vs 5-yr Avg
Sales Transactions	60	- 23%	- 15%
Volume (excl. hotels)	\$319 M	+ 40%	+ 37%

* Annualized

Through three quarters of 2019, South Coast sales continue to reflect a more selective posture from investors, while owner-users have assumed a prominent role, enabled by favorable financing. Dollar volume for sales of office property has been unprecedented, while retail and industrial property have generated below-average activity.

With 60 sales to date on the South Coast, transaction volume is trending about 15% below the prior 5-year average. However, transaction momentum stepped up in Q3 to produce a robust 25 sales. Thanks to the boom in office sales, dollar volume for all property types combined is 24% above the prior 5-year average.

Office volume to date has already reached \$245 million, which is \$100 million beyond the previous high for a full year. The historic dollar volume stems from a handful of high-value sales, including 6300 Hollister Ave in Goleta, 4050 Calle Real in Santa Barbara, and 6410 Via Real in Carpinteria, all three of which traded above \$30 million. The motivations leading the owners of high-value properties to sell in 2019 appear to be varied, meaning the current spike in volume is largely a coincidental aligning of the stars, rather than indicative of a new trend. However, it's safe to say that market timing—10 years into the current economic expansion—was always a factor under consideration.

In contrast to the rally in the office sector, retail and industrial sales as of Q3 were down 45% and 10%, respectively, compared to prior 5-year averages. Lagging industrial sales can be attributed to lack of supply, given that the number of industrial properties for sale has been in the single-digits

throughout 2019. The most notable industrial sale to date was 6155 Carpinteria Ave in Carpinteria, purchased by an owner-user for \$8 million. Meanwhile, retail property is in record supply, with 22 properties on the market. The dip in retail sales appears to correlate with pervasive concern over trends in brick-and-mortar retail. (Though in truth, aside from State Street in downtown Santa Barbara, retail vacancy on the South Coast has remained very stable and would be envied in most markets.) There also seems to be a gap in price expectations between retail owners and potential buyers. Nevertheless, two properties on State Street's downtown retail corridor sold in Q3, including the 58,762 sf multi-tenant retail and office building at 827-831 State St, purchased by an investor for \$23.5 million. There are still 10 properties for sale downtown on State Street.

Owner-users have represented 53% of buyers and the same percentage of dollar volume. Two of the \$30-plus million sales mentioned above—4050 Calle Real in Santa Barbara, and 6410 Via Real in Carpinteria—were purchased by owner-users. The latter was a Q3 sale in which LinkedIn acquired the 87,000 sf office park that it has leased for many years. In Goleta, 420 S Fairview Ave (\$22.8 million) and 454 S Patterson Ave (\$14.8 million) were both off-market purchases by owner-users. Clearly, it's not just small mom-and-pop businesses that are deciding to buy real estate for their own use.

Looking ahead, the Fed has cut interest rates for a third time this year, which should help stoke demand and encourage more buyers to enter the market. On paper, with 69 properties for sale on the South Coast there is ample inventory to sustain strong sales activity. However, investors have become more choosy since the beginning of 2018. Investor demand is strong for high-quality property in good locations. Premium assets routinely receive off-market inquiries from interested buyers and are generating multiple offers when brought to market, provided the price meets market expectation. Fortunately, the remarkable rise in owner-user demand and sales activity has served to fill some of the void left by investors. Provided the deceleration in the broader

economy continues to be gradual, market conditions—and strong sales velocity—are likely to continue into early 2020.

Q3 SALES OF NOTE:

- 6300 Hollister Ave, Goleta. \$33.1 million 106,309 sf office/R&D facility on 6.9 acres purchased by an investor
- 6410-6460 Via Real, Carpinteria. Off-market \$30.4 million 87,138 sf 6-building office park on 9.1 acres purchased by an owner-user
- 827-831 State St, Santa Barbara. \$23.5 million 58,762 sf retail/office building purchased by an investor
- 1486 East Valley Rd, Montecito. \$13 million 6,357 sf office/retail building purchased by an investor
- 2323 Oak Park Ln, Santa Barbara \$6.2 million 7,625 sf medical office building purchased by an investor
- 3793 State St, Santa Barbara. \$4.2 million 4,477 sf office/retail building leased to Fidelity Investments purchased by an investor

- Only two leases larger than 10,000 sf have been signed to date, both by tech firms: Sonos renewed 27,217 sf at 614 Chapala St, and Honey Science subleased 18,792 sf at 530 Chapala St.
- There are 51 properties for lease downtown—the largest inventory on record—totaling more than 220,000 sf and including five spaces larger than 10,000 sf.
- 20% of current inventory came to the market in Q3, including 4,298 sf of warehouse space at 727 Bond Ave and 1,204 sf of light industrial at 12 Ashley Ave.
- There has been a surprising lack of medical leasing. Other than a 1,000 sf renewal at 215 Nogales Ave by Montecito Geriatric Medical Group, there have been no leases of traditional medical space to date. The subdued level of activity is not for a lack of supply: 14 properties are for lease totaling 44,000 sf of medical space.
- Achieved rental rates have continued to rise in 2019—increasing 5% compared to 2018 and 13% compared to 2017. The average rate for leases to date is \$3.00 gross per square foot, a new high mark.

OFFICE LEASING

	Santa Barbara	Goleta	Carpinteria	All
Vacancy	6.4%	6.3%	3.9%	6.2%
Available Space	+9%	-26%	+112%	-9%
Transactions	+13%	+16%	-73%	+8%
Achieved Rents	+6%	+3%	-26%	+2%
Gross Absorption	-6%	+17%	-88%	+3%

Change percentages are compared to 2019, annualized where appropriate.

South Coast office leasing has been robust in 2019, especially in Goleta where momentum from record volume in 2018 has carried forward to the present. Achieved rents have also ascended to new heights. The remarkable inversion of vacancy curves still shows Goleta with a lower rate than Santa Barbara—a reversal that would have seemed impossible a few years ago—and the gap is likely to widen.

SANTA BARBARA

- Transaction volume and gross absorption are on par with the prior 5-year averages. The vacancy rate contracted slightly in Q3 but at 6.4% is still very high by historical standards.

GOLETA

- As in Santa Barbara, achieved rental rates in Goleta are breaching a new threshold: the average rate for leases to date is \$2.00 gross per square foot. This reflects both healthy demand by tenants as well as increased landlord investment in improvements during the current economic cycle.
- The largest available space is the 82,132 sf building at 125 Cremona Dr, which is being vacated by Medtronic.
- Leasing activity coasted in Q3, compared to heavy volume in the first half of the year. Gross absorption and transactions to date are still in step with the record levels posted in 2018.
- Demand continues to be very strong, and activity is expected to rebound significantly in Q4. In fact, early Q4 leases and deals in negotiation could bring the vacancy rate to 5% or even lower by year end.

CARPINTERIA

- The office market in Carpinteria and Summerland has been quiet, with just two transactions to date and no known tenants actively looking in the area.
- The first half of the year saw record-low vacancy around 1.5%. However, three spaces became available in Q3 in Carpinteria and one more in Summerland, which notched the vacancy rate up to 3.9%.

Q3 OFFICE LEASES OF NOTE:

- 57,385 sf renewed at 7402 & 7406 Hollister Ave in Goleta by InTouch Health
- 17,177 sf leased at 7410 Hollister Ave in Goleta by InTouch Health
- 6,147 sf leased at 111 W Micheltorena St in Santa Barbara by Bragg Live Foods

RETAIL LEASING

	Santa Barbara	Goleta	Carpinteria	All
Vacancy	3.8%	1.9%	5.7%	3.3%
Available Space	+ 12%	- 13%	- 24%	+ 5%
Transactions	+ 48%	- 25%	- 33%	+ 27%
Achieved Rents	- 3%	+ 9%	+ 44%	+ 15%
Gross Absorption	+ 75%	- 71%	- 35%	- 22%

Change percentages are compared to 2018, annualized where appropriate.

Santa Barbara is in the midst of a high-volume year for retail leasing. Transaction volume is trending 35% higher than the prior 5-year average. In contrast, leasing activity in Goleta has proceeded below recent levels, primarily due to limited inventory. Achieved lease rates have softened in both cities, with average gross rents decreasing nearly 20% since the recent peak in 2016.

In Santa Barbara’s downtown retail core, there have been 15 lease transactions totaling 42,500 sf on State Street to date, which is consistent with the prior five-year average volume. Keeping with the recent trend, the large majority of the lease transactions were signed by local or regional businesses. The only new tenant with a national profile is Insomnia Cookies, which leased 430 State St in Q3. Although Forever 21 filed for bankruptcy in September,

the Santa Barbara store at 901 State St has not yet been named for closure. Along the 400 to 1300 blocks of State, the storefront vacancy rate remains elevated at 12%. For the lower stretch of that corridor—between Gutierrez and Carrillo—vacancy has remained above 15% for six consecutive quarters. The former Staples building, 17,000 sf at 410 State St, is back on the market for lease.

To help address the challenges facing downtown Santa Barbara, the City has committed to hiring an economic development director, as prescribed by the report delivered by a Los Angeles-based consultant in July. Local interests seem to agree this a positive step, if not a bold one.

In contrast to the State Street corridor, available space in Montecito’s lower village has contracted to five spaces totaling 7,429 sf for lease. In Q3, MLG Retail leased 2,783 sf at 1155 Coast Village Rd, while Mesa Burger claimed the former Coffee Bean & Tea Leaf space at 1209 Coast Village Rd.

In Goleta, disparities between the eastern part of the city and western part have come back into stark relief. The area east of the airport is shouldering 89% of the city’s vacant retail space, including about 16,000 sf available at Magnolia Shopping Center. Meanwhile, in the western part of the city, availability is scarce, which is putting upward pressure on rental rates. In addition, Target’s long-anticipated opening in Storke Plaza has further established the Storke and Hollister intersection as the South Coast’s “big box retail” destination, thereby emboldening nearby landlords to increase rents. As a result, the average gross asking rent in the western part of Goleta is 85% higher than in the eastern part.

Q3 RETAIL LEASES OF NOTE:

- A Board and Brush franchisee leased 1,002 sf at 19-31 E Canon Perdido St
- Rejuvenation Spa & Nails leased the former Just Play Music space at 802 State St
- Insomnia Cookies leased 1,654 SF at 430 State St
- An unnamed local apparel tenant leased 1,917 SF at 714 State St, formerly Lole
- A specialty retailer plans to open a store called Aromas de Jabon at 907 State St, formerly Happy Feet

- Mesa Burger leased the Coffee Bean & Tea Leaf space at 1209 Coast Village Rd
- Mercado El Rey leased 3,167 SF at 305 W Montecito St
- La Cumbre Animal Hospital leased 4,324 SF at 3910 State St

INDUSTRIAL LEASING

	Santa Barbara	Goleta	Carpinteria	All
Vacancy	1.1%	4.8%	0%	2.5%
Available Space	-2%	-17%	-100%	-25%
Transactions	-68%	+115%	-3%	+12%
Achieved Rents	-12%	-1%	+4%	-4%
Gross Absorption	-68%	+43%	+27%	+17%

Change percentages are compared to 2018, annualized where appropriate.

South Coast available industrial space has contracted 25% year-to-date. Goleta and Carpinteria have generated gross absorption far above their 5-year trend lines, while Santa Barbara has seen below-average deal flow.

GOLETA

- Heavy demand for Goleta industrial space has produced record leasing volume, with 29 transactions to date, more than any annual count on record. Gross absorption is also on pace for a new annual high mark and is trending 40% above the prior 5-year average.
- All the activity has helped the vacancy rate to dip back below 5%. However, large vacancies remain at 80 Coromar Dr (57,600 sf vacated by Curvature), 149-151 Castilian Dr (29,465 sf in Santa Barbara Research Park), and 6338 Lindmar Dr (25,940 sf).
- Renewals have represented only 20% of lease transactions, a far smaller proportion than usual, and another indicator of strong demand. The largest of the renewals was 20,337 sf retained by Freedom Photonics at 41 Aero Camino.
- The largest Q3 lease was 12,252 sf leased by Deployable Space Systems at 165 Castilian Dr, vacated by Tencate.

CARPINTERIA

- Carpinteria's only lease in Q3 was a significant one, as Procure secured the 24,030 sf building at 6384 Via Real. In addition to the size, the lease is notable because the rent is in the range normally seen for pure class A office. The property, previously occupied by Northrop Grumman, was purchased earlier this year by Montana Ave, which also owns Procure's headquarters across the freeway at 6303-6309 Carpinteria Ave.
- There are no industrial spaces available for lease. There have been no more than three spaces on the market at any given time for the past four and a half years. The spaces that become available are typically leasing before they come to market.

SANTA BARBARA

- With just five transactions completed through Q3, Santa Barbara is on track for the lowest annual gross absorption on record.
- Eight of the ten available spaces have been on the market for at least four months.
- Industrial space in Santa Barbara has become more diverse over the past decade, ranging from simple warehouses to spaces improved for fitness, creative office, R&D, and tasting rooms. While this variety—and the corresponding range of asking rents—might seem to offer something for every tenant, it actually limits the choice for the tenant with a specific requirement, especially when vacancy is only 1.0%.

Q3 INDUSTRIAL LEASES OF NOTE:

- 24,030 sf leased at 6384 Via Real in Carpinteria by Procure
- 12,252 sf leased at 165 Castilian Dr in Goleta by Deployable Space Systems
- 5,400 sf leased at 6485 Calle Real in Goleta by Deckers Outdoor
- 5,119 sf leased at 650 Ward Dr in Goleta by Above All CNC, Inc

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