

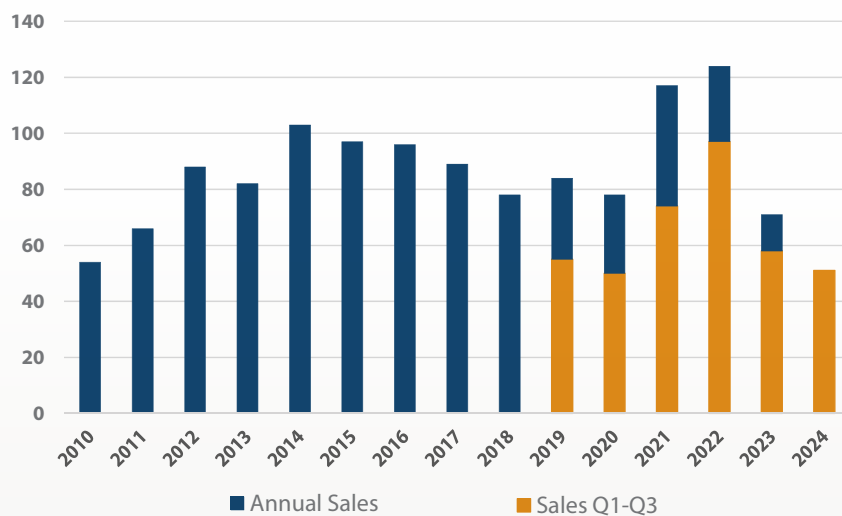
COMMERCIAL SALES: The Darkness Before the Dawn?

Commercial sales have seen a profound lull since the end of 2022, the year that brought steep interest rate increases and ended an era of historically cheap financing. Since then, sellers have not budged much on price, while most buyers have seen their purchasing power undercut by higher interest rates. As a result, sales transactions during 2023 and so far in 2024 are down 63% compared to the prior five-year average. In Q3 there were 14 commercial sales completed totaling \$43 million, a very slow quarter by recent standards. All told, 2024 is on pace for the lowest annual dollar volume since 2009.

Investors appear to have withdrawn from the market even further, possibly holding out for interest rate cuts in coming months. Uncertainty surrounding the Presidential election has also had a cooling effect on real estate investment. There were only four investor purchases in Q3, most notably the "Bottle Shop" retail property at 1200 Coast Village Rd in Montecito by a 1031 Exchange buyer. Another investor acquisition was the 9,800 SF industrial building at 5387 Overpass Rd. By comparison, there were 10 owner-user purchases in Q3, including the 11-acre St. Anthony's Seminary property at 2300 Garden St, auctioned for \$16.7 million in July.

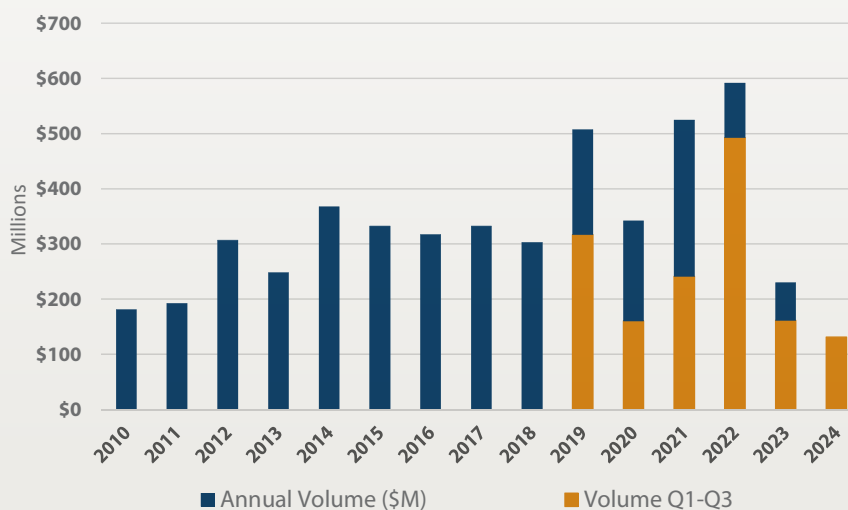
The impact of higher interest rates on sales activity hits hardest in the upper price ranges, as fewer buyers have been willing or able to secure big loans to finance a purchase. The dollar volume of sales priced over \$5 million has dipped nearly 80%, compared to the prior 5-year average. The first three quarters of 2024 yielded only seven transactions over \$5 million, two of which were hotels, and a third was the education property

South Coast Commercial Sales Transactions



Through Q3 there were 51 sales, compared to the 5-year avg of 67 sales. Non-hotel volume was \$131 million versus the 5-year avg of \$274 million.

Commercial Dollar Volume (excluding hotel property)



at 2300 Garden St noted above. The remaining sales over \$5 million were two industrial and two retail properties. There were no office sales above that price threshold.

On the other hand, sales below \$5 million have followed a gentler decline, trending about 15% below the 5-year trends for both transactions and dollar volume. Properties in this price tier are obviously easier to finance and/or purchase with cash, making the barriers to ownership less imposing.

Office property typically generates more dollar volume than other commercial types, but there haven't been any sizeable office sales, and dollar volume to date is only \$17 million. Meanwhile, retail and industrial sales have produced \$55 million and \$32 million, respectively, which are both about 22% below their 5-year averages. Most of the retail sales have been in the Funk Zone and downtown Santa Barbara, including four buildings on the State Street corridor.

Looking ahead, there is a willing and growing supply of sellers in the market. The number of properties for sale expanded by 33% during the past 6 months to reach the highest level in two years. In fact, 35% of the current inventory came to market during the third quarter. As for demand, the Federal Reserve's recent interest rate cuts—the first in more than four years—have given buyers cause for optimism. With potential for lower interest rates ahead and the election in the rearview mirror, commercial sales may be poised to regain momentum during 2025.



Prime real estate in the heart of Coast Village Road, the Bottle Shop property at 1200 Coast Village Rd was purchased by an investor.

OFFICE LEASING

Adapting to the widespread embrace of hybrid and remote work by employees, office tenants are tending to choose smaller suites, especially in the South Coast's robust tech sector. Gross absorption of square footage to date through Q3 was down about 40% compared to pre-pandemic levels, while the average office space leased was about 15% smaller in Santa Barbara, and about 35% smaller in Goleta. Not surprisingly, South Coast office vacancy is relatively high, but is still less than half the national average of 20%.

Santa Barbara

Gross absorption of Santa Barbara office space has decreased 12% compared to the 5-year average, and vacancy has crept up, but achieved rents have held steady.

- Setting aside the 111,800 SF shell space offered on the upper floors of the former Nordstrom building, Santa Barbara office vacancy is 8.7%, the highest rate in three years.
- Sonos's move to Goleta has contributed substantially to Santa Barbara's vacancy. More than 100,000 SF of the available space was held by Sonos, including 25 E Mason St, 600-614 Chapala St, 25 W Cota St, and 530 Chapala St. The latter two are adjacent buildings that Sonos leased but never occupied, and then subleased to Honey/Paypal for the rest of the lease term. Now the buildings are available for sale or lease.
- The average achieved rent held steady at around \$3.15 gross per SF. Rates appear to be rising for office space in Montecito's Coast Village, though, where achieved rents to date ranged from \$4.80 to over \$8.50 gross per SF.

Q3 leases of note:

- In one of the largest Santa Barbara office leases in recent years, a law firm leased the 17,100 SF building at 1020 State St on a 10-year term.
- Merrill Lynch renewed 9,400 SF at 1424 State St.



The 82,000 SF office building at 5383 Hollister Ave near Goleta Cottage Hospital is fully leased thanks to a 29,800 SF lease in Q3.

- PathPoint leased 7,000 SF at 901 Olive St on a 10-year term. They will only need to move about a block from 902 Laguna St, where they have been for over 10 years.

Goleta

Available office space in Goleta has contracted by one third since the beginning of the year, and the vacancy rate of 5.3% is near the lowest on record. At the same time, there were only four Q3 leases, and lack of demand remains a concern for landlords.

- Second-floor office suites have been slower to lease in Goleta during the past four years, as remote work has undercut demand. Countering this trend, 29,800 SF at 5383 Hollister Ave was leased by an unnamed tenant on a 10-year basis, with 18,200 SF of the leased area being on the second floor. It was the largest South Coast lease of the year to date. The 82,000 SF building is fully leased for the first time in over five years.
- The vacant 46,400 SF office building at 6750 Navigator Way was for lease for many years but was recently pulled from the market because a pending sale.
- Majestic has completed 12 lease transactions totaling 80,400 SF, which represents half of the

office leasing to date in Goleta. Nine of the 12 transactions were renewals.

Carpinteria

Carpinteria's office market continues to be in stasis, with an excess of available space—currently 19.7% vacancy—being met by almost invisible demand.

- No transactions were signed in Q3, following only two small leases in the first half of the year (one in Carpinteria and one in Summerland).
- Procore's 79,500 SF for sublease across two buildings on the bluffs constitutes the bulk of the vacancy. Agilent has 10,100 SF for sublease as well, at 6398 Cindy Ln. Those sublease offerings comprise 69% of Carpinteria's available space.

RETAIL LEASING

South Coast retail leasing transactions year-to-date are up 16% compared to the 5-year average, as the sector continues to recover from the pandemic. However, deal velocity waned during Q3, with only 16 transactions completed.

Retailers are thinking smaller, and leases of large retail spaces have become rare. In fact, no leases over 5,000 SF have been signed to date in 2024, and the average leased space was a record-low 1,825 SF. As a result, gross absorption of space through Q3 was down 28% from the 5-year average. Nevertheless, South Coast vacancy remains tight at 2.8%, and demand—for modest-sized spaces at least—appears stable.

For State Street, the big news of the past quarter was Cost Plus World Market's 24,000 SF "big box" space at 610 State St coming to market for lease in the heart of downtown. There is no evidence the store will be closing any time soon, but the move indicates a likely change down the road for one of downtown's larger buildings.

The State Street corridor saw five Q3 deals signed, and each of those tenants has moved quickly to open for

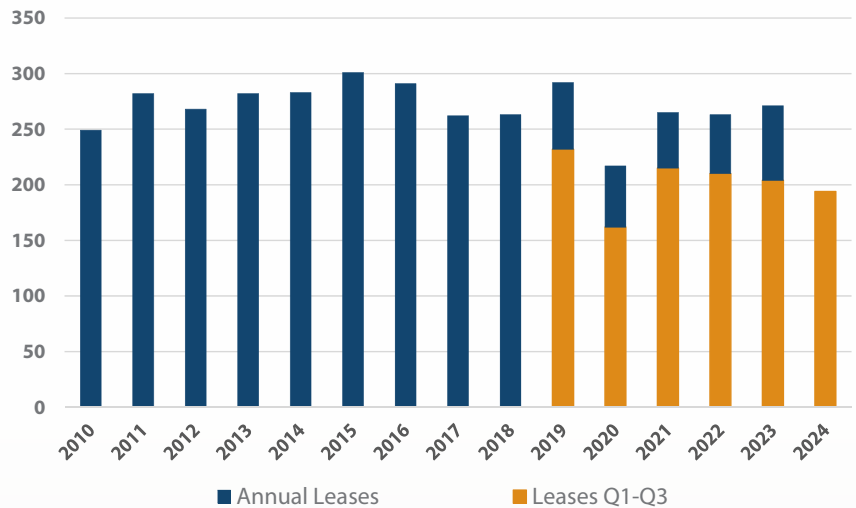
business. Casa Agria Ale is planning a November launch after leasing the former Modern Times space in the Kim's Service Department project at 418 State St. Two soft goods retail stores, Courtney Burke at 931 State St and Canvas Boutique at 1307 State St, signed leases and opened for business in short order. Next door to Canvas, Tamsen Gallery subleased 1309 State St, and has already moved there from the 900 block. Finally, Namaste Indian Cuisine subleased 1218 State St and opened in a curry (pardon the pun). Storefront vacancy ticked up slightly to 12.9%, but the "perceived" vacancy of dark storefronts is less bleak at 8.0%.

In the Funk Zone, there are changes and leases taking shape on the city block that local developer Brian Kelly's group purchased earlier this year. In addition to food truck-style operators already up and running along Yanonali and Gray Streets, there are rumored deals for two brick-and-mortar restaurant concepts, Dart Coffee, and soft goods retailers. Aside from this project, the only other retail lease to date was the Tendrel men's clothing store at 223 Anacapa St.

Golf simulators are an emerging niche within the "experiential retail" trend, and two operators made deals in Q3 to join the club. Downtown Santa Barbara's first golf simulator business, SwingPath Golf Club, opened in a small industrial space at 417 Santa Barbara St. Meanwhile, The Golf Lounge will open in December at 2840 De La Vina St in collaboration with Validation Ale's new uptown location next door.

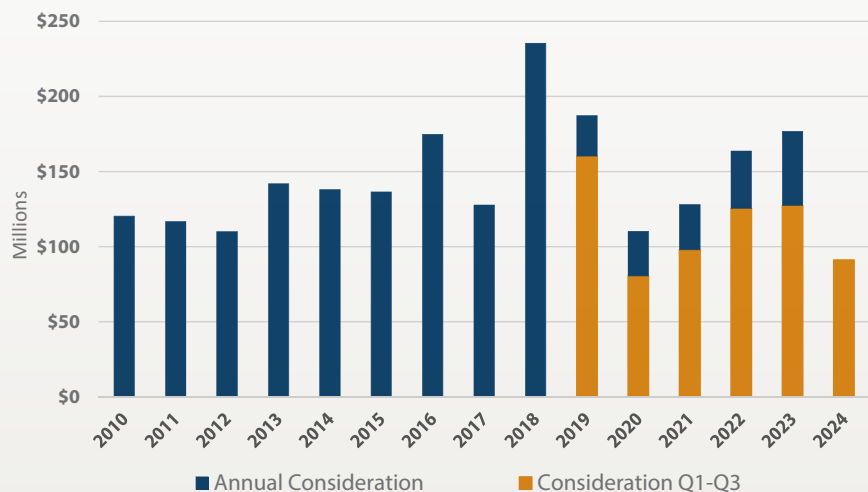
Montecito gained two tenants in Q3, as Belrose Jewelers secured the former Baske space at 1268 Coast Village Rd, and Wunderkind leased the former optometry space at 1147 Coast Village Rd for its second Montecito location. Prime Coast Village storefronts are increasingly garnering double-digit rent per square foot, as these two did. The three Coast Village Road shop spaces leased to date have averaged about \$11.50 gross per SF.

South Coast Lease Transactions (all property types)



Through Q3 there were 194 leases, compared to the 5-year avg of 205 leases. Dollar consideration was \$91 million versus the 5-year avg of \$118 million.

Sout Coast Lease Consideration (all property types)



In Carpinteria, the adaptive reuse project at 700 Linden Ave (newly dubbed "Linden Square") is expected to open in January, and the ground floor is fully leased thanks to recent signings by two retailers: Macher and The Shopkeepers. The upstairs bar/restaurant area is the only remaining retail vacancy in the project (there is some



610 State St, the 24,000 SF building occupied by Cost Plus World Market recently hit the market for lease in downtown Santa Barbara.

office space on the second floor as well). Across the street from Linden Square, the 7,300 SF former Rite Aid building at 801 Linden Ave, was recently brought to market for sale or lease, and (as of this writing) is already under contract with a buyer.

For Goleta, the only Q3 transaction was signed by US Marine Corps Recruiting, a renewal and expansion totaling 3,560 SF in the Plaza Shopping Center at 7127 Hollister Ave. Both the number of leases and the average size space are well below trend for Goleta so far this year. However, despite a 39% decrease in gross absorption to date, Goleta's vacancy has shown little change and remains below 2.5%. The average rent in Goleta is up 6% compared to 2023 and 17% higher than the pre-pandemic 5-year average.

INDUSTRIAL LEASING

Goleta

In Goleta, large industrial leases by Redwire Space and Arthrex during Q2 have contributed to over 180,000 SF of gross absorption to date, putting 2024 on par with the prior 5-year trend for square footage leased. Goleta's vacancy rate was 2.7% at the end of Q3, which represents a 12% expansion of available square footage since the beginning of the year.

Goleta industrial was limited to two leases in Q3. One of them was substantial, though, as Karl Storz Imaging (KSI) completed a 10-year lease of 35,300 SF at 147-151 Castilian Dr. However, during a long contingency period before the lease was finalized, KSI decided against occupying the premises and is now trying to sublease the entire space. This sublease offering and the 30,500 SF former Oxford Instruments space at 6310 Hollister Ave comprise more than half of Goleta's available space.

Santa Barbara

Santa Barbara is carrying an unusually large inventory of 11 industrial spaces for lease, and 10 of the spaces have become available during 2024. Despite more spaces than usual being available, the vacancy rate is still just 1.1%. Furthermore, nearly 40% of the available space is for sublease, most notably 11,600 SF at 1 N Calle Cesar Chavez.

The only Santa Barbara industrial lease during Q3 was actually signed by a retail tenant, the golf lounge at 417 Santa Barbara St mentioned previously. That lease, like most of the Santa Barbara industrial leases to date, was less than 1,500 SF. The only lease larger than 5,000 SF was a sublease by Dramatic Choices Inc at 1 N Calle Cesar Chavez back in Q1. The focus on smaller leases has resulted in less gross absorption of space, which is trending 65% below the 5-year average. Another effect of smaller leases is higher rent per square foot. The average achieved rent to date for industrial space is around \$3.00 gross per SF, about a dollar higher than the 5-year average. It should also be noted that leasing of spaces by non-industrial uses, such as retailers, gyms, and wealthy car collectors, has also contributed to the rent growth in Santa Barbara.

Carpinteria

Facing sporadic demand from tenants, Carpinteria has averaged only one industrial transaction per quarter since the end of 2022. Gross absorption to date has surpassed 2023's extremely low total, but nevertheless is down 21% from the 5-year average. The sole Q3 lease was 5,000 SF at 1019 Mark Ave, signed by Advanced Capital Equipment Sales. The recent addition of 22,000 SF at 1120 Mark Ave to the market helped expand vacancy to 4.7%, the highest rate in 12 months.

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LEASING MARKET DATA

	Market	Vacancy Rate		Transactions		Gross Absorption (SF)		Achieved Rent (PSF GR)	
OFFICE	Santa Barbara	10.7%	+7%	73	-4%	226,403	-19%	\$3.16	-5%
	Goleta	5.3%	-33%	23	-7%	163,013	-58%	\$2.34	+5%
	Carpinteria	19.7%	+155%	2	-62%	4,035	-82%	\$2.16	-5%
RETAIL	Santa Barbara	2.9%	-9%	46	+8%	81,818	-20%	\$4.40	+11%
	Goleta	2.4%	+2%	13	-4%	27,189	+13%	\$3.44	+6%
	Carpinteria	4.6%	-22%	10	+48%	17,607	+84%	\$5.20	+11%
INDUSTRIAL	Santa Barbara	1.1%	+33%	9	-50%	23,880	-82%	\$3.03	+56%
	Goleta	2.7%	+12%	13	-13%	181,092	+42%	\$2.20	+25%
	Carpinteria	4.0%	+20%	5	+233%	35,341	+42%	\$1.53	+36%

Change percentages are compared to 2023 values.

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