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Casden Real Estate Economics Forecast

Casden Forecast 2012 Industrial & Office Forecast Report

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Contents

The Casden Real Estate Economics Forecast is pleased to present its 2012 report on the Southern California office and industrial real estate markets. The Casden Real Estate Economics Forecast analyzes fundamentals and forecasts real estate market indicators in the Southern California region. The Forecast issues two annual reports, one covering the region's office and industrial markets and the other covering its apartment markets.

We begin with overviews of the United States and regional economies, which serve as the foundation for the analysis of the Southern California real estate markets. A comprehensive summary of the fundamental trends in the industrial and office markets for Los Angeles County, Orange County, and the Inland Empire as well as individual submarkets make up the main body of the report. The statistical snapshots provide concise summaries of recent movements in quarterly rents, vacancy rates, and net absorption for each county as well as the submarkets. At the end of the report, we present our two-year forecast for rents and vacancy rates in each of the four metro markets. This year, for the second time, we are including statistical confidence bounds on all of our predictions.

A report of this magnitude is only possible through the contributions from many individuals. We thank J.C. Casillas of Newmark Grubb Knight Frank for providing the fundamental market data. We also thank Skye Tirsbier for her outstanding research assistance and Marilyn Ellis for her help with the graphic production of the report. We are also grateful to the Lusk Center staff for their assistance, especially Jennifer Frappier and Sonia Savoulian. Finally, we gratefully acknowledge our sponsor Newmark Grubb Knight Frank.

Richard K. Green, Director
Lusk Center for Real Estate

Tracey Seslen, Senior Research Associate
USC Casden Real Estate Economics Forecast

Executive Summary

Like the Southern California economy overall, from Q3 2011 to Q3 2012, the office and industrial markets of the region remained on a path of improvement. For the industrial market, improvement meant a continued rise in occupancy and mostly rising rents, while for the office market, it meant a continued rise in occupancy and smaller rent declines. On the industrial side, all but two of 14 submarkets experienced positive net absorption of space. Ten of 14 submarkets saw a rise in rents, up from eight in the prior four quarters. On the office side, 13 out of 17 submarkets recorded a rise in occupancy, and five of 17 a rise in rents.

We predict office market rents to stabilize in as little as 6 months, but a sustained recovery could be many years off. Office demand should continue to improve, but vacancy rates in some submarkets remain so far above their "natural" levels that the trend could continue without any accompanying stabilization in rents.

On the industrial side, we should continue to see declining vacancy and rising rents in all metro markets, but the magnitude of the changes will be dependent upon manufacturing output, port activity and completion of new stock. A building boom has begun once again in the Inland Empire, and could temper the improvements in rents and vacancy rates that otherwise would have occurred.

The top performers across all metro markets and both property types were the Los Angeles and Inland Empire industrial markets, which both recorded rent gains of more than 6 percent and positive net absorption of over 9 million square feet. Already one of the nation's tightest industrial markets, the Los Angeles vacancy rate fell from 3.1 to 2.1 percent. For the Inland Empire, although demand was off from the 20 million square feet of positive net absorption logged between Q3 2010 and Q3 2011, the rent performance was a dramatic improvement over the 5.7 percent loss experienced in the prior year. The weakest performer, for the second year in a row, was the Inland Empire office market, which posted a 3.6 percent decline in rents. Although the area witnessed an increase in demand for office space, the vacancy rate sits at a region-worst 21.1 percent as of Q3 2012.

The Southern California industrial market appears to be on a clear path to recovery, although geopolitical turmoil and economic challenges continue to pose a risk to the health of the sector. On the other hand, the office market is still struggling, and could continue to struggle for years to come. A paradigm shift in the way tenant firms use office space will force landlords and developers to re-think their investment strategies even as the economy improves. We may never see office vacancy rates at pre-crisis levels until we see some natural retirement of the capital stock and a reduction in the region's office supply.

Los Angeles County

Office:

Four out of seven submarkets recorded positive net absorption through Q3 2012, leading to 402,000 square feet of net move-ins for the county as a whole. Los Angeles still has a long way to go, however, in erasing the nearly 6 million square feet of net move-outs that occurred between Q1 2009 and Q3 2010. The strongest performance, in relative terms, came from LA North, which posted 343,000 square feet of positive net absorption and a decline in vacancy of 1.0 percentage point. The Mid-Wilshire area was the worst performer relative to market size, recording 146,000 square feet of net move-outs and a 1.7 percentage-point increase in its vacancy rate. Mid-Wilshire overtook the South Bay submarket for the highest vacancy rate, ending Q3 2012 at 21.1 percent. For the third year in a row, San Gabriel Valley had the lowest vacancy rate by a 6 percentage-point margin.

As of Q3 2012, average Class A asking rents for Los Angeles County stood at $2.93 per square foot, down 0.4 percent for the year. Class B asking rents rose for the second year in a row to $2.19, an improvement of 0.8 percent.

San Gabriel Valley experienced the largest drop in Class A rents among submarkets at 4.7 percent year-over-year. The Downtown submarket – the second most expensive in Los Angeles county – was the strongest performer, with a year-over-year increase of 4.0 percent. In spite of a 3.2 percent decline in average asking rents, West Los Angeles remained the most expensive among Los Angeles county submarkets, at $3.50 per square foot.

The period Q3 2011 to Q3 2012 brought the delivery of 102,000 square feet of Class A space. As of Q3 2012, 522,000 square feet of new office space is under construction, all of which is located in West Los Angeles.

Year-to-date sales volume for 2012, which stands at $1.5 billion, is up nearly 15 percent from the whole of 2011. Still, sales volume is down more than 80 percent from the peak achieved in 2006. The average cap rate for 2012 deals stands at 6.0 percent, down from 7.3 percent in 2011.

Industrial:

Over the last year, the Los Angeles industrial market experienced a substantial increase in demand, with positive net absorption of 9.05 million square feet. The vacancy rate currently sits at 2.1 percent, down 1 percentage point from Q3 2011 and only 0.6 percentage points off its market-peak level. Los Angeles remains the tightest industrial market in the United States.

The Mid-Cities submarket experienced the largest relative increase in demand, logging nearly 2 million square feet of net absorption on a stock of about 111 million square feet. Consequently, the vacancy rate fell 1.9 percentage points to 2.2 percent.

Owner-user purchases and overall leasing activity stand at 36.9 million square feet for 2012. If the YTD pace of sales and leasing activity hold up through Q4 2012, the annual totals will be on par with 2011 levels.

Countywide average asking rents were up 6.3 percent to $0.53 per square foot. And for the first time in the post-crisis era, all five submarkets logged year-over-year increases. For the second year in a row, Central Los Angeles was the clear winner, recording a 14.2 percent increase in average asking rents. San Gabriel Valley was the weakest performer, registering a 0.3 percent rise in rents. North Los Angeles remains the most expensive industrial submarket, with average asking rents of $0.64 per square foot.

Warehouse and distribution rents rose 3.9 percent in the last four quarters to settle at $0.49 per square foot. General industrial space experienced a strong turnaround over the last year after three straight years of decline. Average asking rents rose 7.4 percent to $0.55 per square foot.

From Q3 2011 to Q3 2012, around 1.1 million square feet of new industrial space came online across six properties. Completions were divided between the South Bay (62.6 percent), San Gabriel Valley (27.6 percent), and Mid-Cities submarkets (9.8 percent). About 1.13 million square feet of new industrial space are currently under construction across the Central, Mid-Cities, and South Bay submarkets.

Sales volume through Q3 2012 stood at $614 million. If the average pace of transactions continues through the end of the year, total sales will finish slightly ahead of the 2011 level. The average cap rate for 2012 stood at 6.8 percent, down 0.5 percentage points from 2011.

Orange County

Office:

From Q3 2011 to Q3 2012, Orange County saw continued improvement in its office market, although demand was not as strong as during the prior four quarters. The county overall experienced 1.65 million square feet of net move-ins, down from 1.9 million square feet. The vacancy rate subsequently fell 1.7 percentage points to 16.6 percent. Although the Orange County office market is by no means in good shape, it has made great strides toward recovery during the last eight quarters.

The North County submarket recorded the highest level of net move-ins relative to market size and ended Q3 2012 with the lowest vacancy rate in the county; vacancy fell 3.7 percentage points to 12.2 percent. The West County submarket was the only one to experience negative net absorption over the last four quarters, with 170,000 square feet of net move-outs. The vacancy rate subsequently rose 5.5 percentage points to 18 percent, which is the highest level among Orange County submarkets.

Average asking rents continued to fall in Orange County; however, the declines have been decreasing over time. Between Q3 2011 and Q3 2012, Class A and Class B rents fell by 2.9 percent and 0.9 percent, respectively. Class A rents ended Q3 2012 at $2.11 per square foot, while Class B rents ended the quarter at $1.73 per square foot. Central County posted the strongest Class A rent performance among submarkets and was the only one to see a year-over-year rent increase. Average asking rents rose 3.9 percent to $2.06 per square foot. South County took the greatest hit in Class A rents, posting a decline of 7.7 percent to $1.90 per square foot. South County now stands as the least expensive office submarket in Orange County.

For the second year in a row, no new office space was completed in Orange County. Eight hundred forty-nine thousand square feet of office space are currently under construction, divided between the Airport and West County submarkets. Year-to-date sales volume stood at $467 million, which is only 5 percent off the total for 2011. Since witnessing an astonishing $4.7 billion in office transactions in 2007, Orange County has not seen more than $1 billion per year in office sales. The average cap rate stands at 5.6 percent, up a tick from 2011.

Industrial:

As with the Orange County office market, the Orange County industrial market experienced an increase in demand over the last four quarters, but not as large an increase as in the prior year. The County logged about 1.6 million square feet of net move-ins, down from 2.5 million. The vacancy rate subsequently fell half a percentage point to 4.8 percent.

At the end of Q3, owner-user purchases and overall leasing activity for 2012 stood at 15.7 million square feet. If the average pace of contracting holds steady through the end of the year, the 2012 total will exceed the 2011 amount by about 7.3 percent.

South County, which is the smallest of the Orange County industrial submarkets, experienced the largest relative increase in demand, logging 414,000 square feet of net move-ins. The vacancy rate, which remains the highest in the county, fell 0.9 percentage points to 7.2 percent. The West County submarket was the only submarket to experience a decline in demand over the last four quarters, recording 326,000 net move-outs. The vacancy rate for the area rose 0.9 percentage points to 5.2 percent.

After rising 10.2 percent between Q3 2010 and Q3 2011, average asking rents in Orange County experienced a correction during the last four quarters: rents fell 4.3 percent to end Q3 2012 at $0.71 per square foot. Among the Southern California metro markets discussed in this report, Orange County was the worst performer in industrial rents by a wide margin, but it remains the most expensive by $0.18 per square foot.

The Airport submarket was the only submarket to experience an increase in asking rents, but its performance was way off the 10.2 percent increase recorded between Q3 2010 and Q3 2011. Rents rose 1.6 percent to end Q3 2012 at $0.86 per square foot. North County was the weakest performer, logging a 7.0 percent decline in average asking rents.

Warehouse properties saw a 5.3 percent increase in rents over the last four quarters, ending Q3 2012 at $0.54 per square foot. General Industrial properties, on the other hand, lost nearly all of the ground it gained from Q3 2010 to Q3 2011, logging a 9.4 percent decline in average asking rents. R&D/Flex properties, which make up about 30 percent of the total industrial stock, ended in-between, posting a 4.6 percent decline in average asking rents. The R&D/Flex category is the most expensive industrial sub-type in the county at $0.94 per square foot, and carries the highest vacancy rate at 6.6 percent.

For the second year in a row, no new industrial space came online. One hundred thirty-two thousand square feet are currently under construction, divided between the North County and South County submarkets. Year-to-date sales volume is off nearly two-thirds from the 2011 annual total and currently stands at $84 million. Not surprisingly, average going-in cap rates have risen from 5.8 to 7.3 percent.

Inland Empire

Office:

Although demand rose in all five Inland Empire submarkets, the market-wide vacancy rate remains the highest in Southern California at 21.1 percent. Between Q3 2010 and Q3 2011, the region reported 721,000 square feet of net move-ins, and a decline in the vacancy rate of 2.7 percentage points. The Temecula/South submarket experienced the largest relative increase in demand. The area's 145,000 square feet of net move-ins led to a decline in the vacancy rate of 6.3 percentage points. At the end of Q3, the vacancy rate stood at 19.0 percent.

After logging a 6.3 percent decline in rents from Q3 2010 to Q3 2011, the Inland Empire office market witnessed a slightly-less-dismal 3.6 percent decline from Q3 2011 to Q3 2012. At the end of Q3 2012, rents stood at $1.85 per square foot. The Class B market, which makes up the majority of Inland Empire office space, held steady at $1.47 per square foot. The Temecula/South submarket was the top performer in the Class A category, and the only submarket to experience a year-over-year rent increase. Average asking rents rose 6.4 percent to end Q3 2012 at $1.83 per square foot. Interestingly, in the Class B category, the Temecula/South submarket was the worst performer, recording a year-over-year rent decline of just over 5 percent. The Riverside submarket was the worst performer in the Class A category, logging an 8.3 percent year-over-year decline.

The period Q3 2011 to Q3 2012 brought the completion of one new office property: a 140,000 square foot Class A building in the Riverside submarket. No new space is currently under construction. Year-to-date sales volume stood at $64.6 million, 15.5 percent below the 2011 calendar-year total. The average going-in cap rate rose from 8.3 to 8.7 percent.

Industrial:

For the third year in a row, the Inland Empire industrial market showed significant improvement in demand. From Q3 2011 to Q3 2012, the area logged 9.4 million square feet of positive net absorption, bringing the total net absorption since Q1 2009 to nearly 40 million square feet. The vacancy rate subsequently fell another 1.7 percentage points to 4.9 percent. Year-to-date owner-user purchases and leasing activity stand at 21.6 million square feet. If the pace of transactions is maintained through Q4 2012, the annual total will fall just short of 2011 volume.

With the exception of West County, all Inland Empire submarkets experienced sharp declines in vacancy.

The Riverside submarket experienced the strongest absolute and relative increase in demand from Q3 2011 to Q3 2011, logging 3.5 million square feet of net move-ins and a decline in the vacancy rate of 2.1 percentage points. The vacancy rate stood at 6.4 percent as of Q3 2012, the highest among Inland Empire submarkets.

Area-wide average asking rents rose for the second year in a row, climbing 6.1 percent to $0.35 per square foot. San Bernardino performed the best among submarkets, posting 10.7 percent gain in average asking rents. For the second year in a row, the South County submarket performed the weakest, with rents slipping a staggering 33.3 percent to $0.30 per square foot.

As was the case from Q3 2010 and Q3 2011, the vast majority of industrial completions in Southern California occurred in the Inland Empire during the last four quarters. Another 1.7 million square feet of space was added to the area stock across four properties. An additional 7.2 million square feet are currently under construction.

Year-to-date transaction volume sits at $319 million, which is down significantly from previous years. Even if the average pace of transactions is maintained through the end of 2012, annual totals will fall short of 2011 numbers by about 12 percent and will fall short of 2010 totals by 68 percent. Average going-in cap rates held steady at 6.2 percent

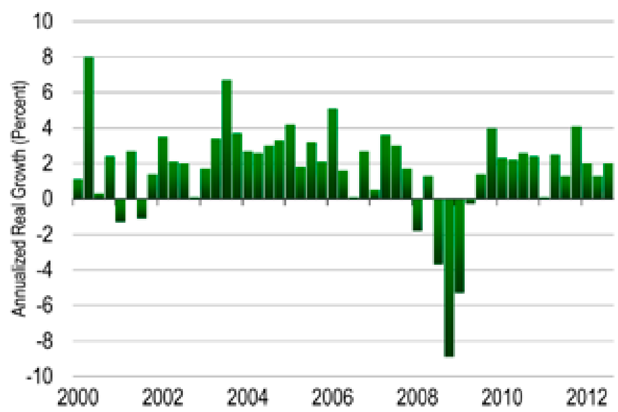
Current View of the Economy

The US economy has continued to improve through the first three quarters of 2012. As we reported back in April, most of the major economic indicators – including GDP, unemployment, and consumer sentiment – showed signs of recovery. But the incremental gains have been relatively small and the country is still a long way off from pre-recession levels of economic health.

The third quarter of 2012 marked the 13th straight quarter of positive annualized growth in Gross Domestic Product, but not since 2007 has the country seen two straight quarters of 3 percent growth or more. Quarterly annualized growth has hit 4 percent twice since the end of the recession, but has generally bounced around between 1.0 and 2.5 percent. These numbers have to improve if sub-5-percent unemployment is ever to become reality again.

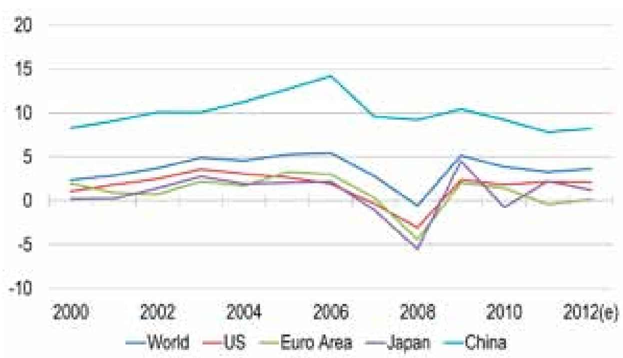
After a roaring start to 2012, job creation slowed considerably. California exceeded the nation as a whole in job creation relative to its share of population, but Southern California trailed the rest of the state. With more than 60 percent of the total California population, Southern California created only 42.6 percent of the jobs. The national unemployment rate, as of this writing, stands at 7.9 percent, down 1.0 percentage point from a year earlier and 0.4 percent from February. Still, the US economy has about 4.3 million fewer jobs since employment peaked in early 2008. The state unemployment rate, at 10.2 percent, fell from second-highest to third-highest in the nation (behind Nevada and Rhode Island). Among the

GDP Growth



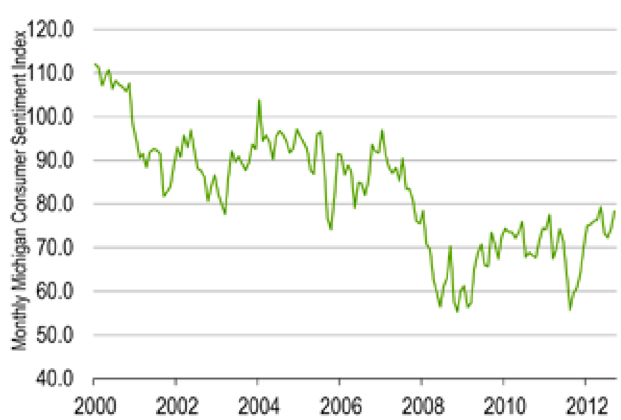
Source | Bureau of Economic Analysis, US Dept of Commerce

GDP Comparision



Source | Internatinoal Montary Fund

Consumer Sentiment



Source | Michigan Survey of Consumer Sentiment four Southern California counties discussed in this report, only Orange County has a lower unemployment rate than either the state or the nation as a whole.

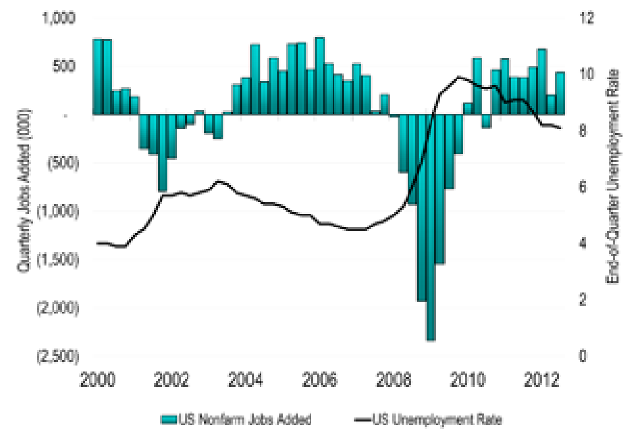
In early November, the Philadelphia Federal Reserve Bank Survey of Professional Forecasters released its latest macroeconomic outlook, which projected more pessimistic GDP and employment growth for 2013 than in its prior 2012 forecasts. The survey predicts average annualized GDP growth of 2.1 percent and an average unemployment rate of 7.8 percent nationally for 2013. The survey also projects average employment growth of about 148,000 jobs per month over the next four quarters. As in previous forecast reports, headline inflation is expected to remain at or below 2.2 percent. This should keep pressure off of interest rates, but it will mean that the real value of debt carried by real estate will remain high.

Adding to the sentiments of recovery has been the performance of the US stock market. Although the S&P 500 was not able to maintain its outstanding first-quarter showing throughout the rest of the year, the stock index is up 8.54 percent year-over-year and 11.82 percent year-to-date as of this writing.

Finally, credit markets continued to loosen during the first half of 2012. US-chartered commercial banks, credit unions, and foreign banking offices in the US combined for $630 billion in net lending, after reporting only $200 billion in net lending for the entirety of 2011 and $183 billion in net borrowing in 2010.

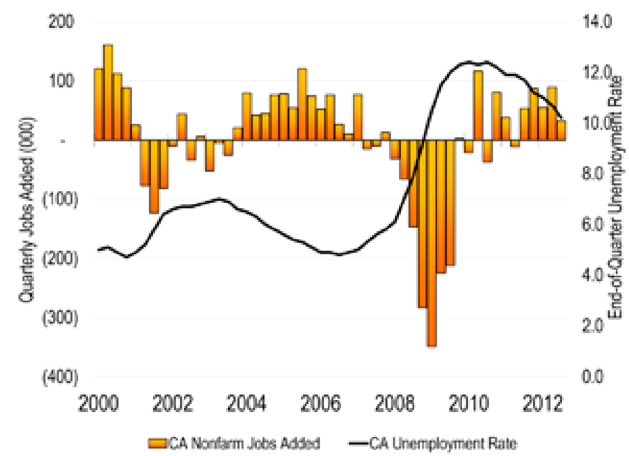
Looking to the future, the following six factors are likely to have the greatest impact on the stability of the US economy, and in turn, the commercial real estate markets:

U.S. Unemployment



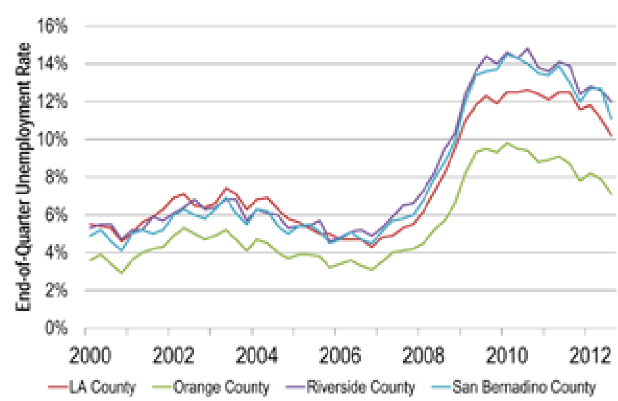
Source | Bureau of Labor Statistics

California Unemployment



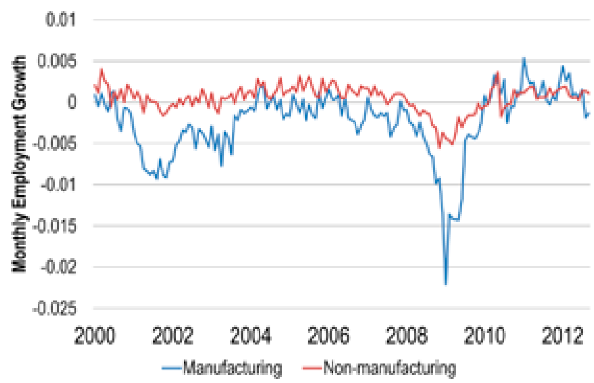
Source | Bureau of Labor Statistics

County-Level Unemployment



Source | Bureau of Labor Statistics

Service and Manufacturing Employment Growth

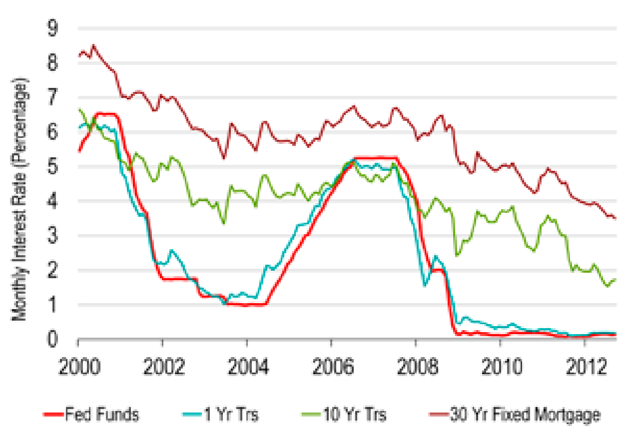


Source | Bureau of Labor Statistics

Capcitiy Utilization

Source | Bureau of Economic Analysis, US Dept of Commerce

Interest Rates



Source | Board of Governors of the Federal Reserve System

Manufacturing output, both in the US and China. Although US factory output and capacity utilization remain below their long-run averages, they increased by 1.6 and 1.5 percent, respectively, on a year-over-year basis, China, on the other hand, has witnessed a steady decline in manufacturing output over the last two years. For the US, higher manufacturing output and capacity utilization will directly result in higher demand for general industrial and warehousing/distribution space. For China, fewer exports to the US will mean fewer dollars to invest in US Treasuries, which could drive down Treasury prices and raise yields.

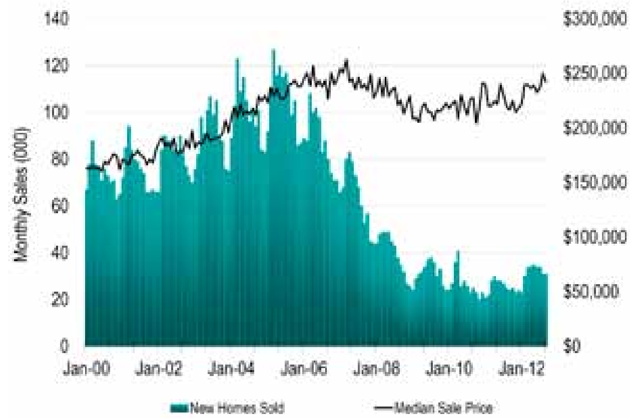
Oil Price Movements. The price of Brent Crude currently stands at $110 per barrel -- about the same as one year ago. Ongoing turmoil in the Middle East and severely constrained refining capacity in the US suggest that the price of petroleum-based products will remain high for the foreseeable future. The elevated price of oil will no doubt impact the real estate industry, keeping construction costs high and reducing the attractiveness of properties in the outlying areas of major metro markets. More broadly, economists believe that every 25 cents of increase in gasoline prices will lead to a reduction in economic growth of roughly 0.2 percentage points.

Sovereign Risk in Europe. Although the worst of the uncertainty appears to have passed, instability in Europe still threatens world financial markets. Greece has avoided default (so far) and the Eurozone has remained intact, but the bailout package's required austerity measures have worsened Greece's recession and led to violent social unrest. Overall unemployment hit 25 percent in July of 2012 and youth unemployment surpassed 50 percent. Spain, which has so far avoided a full-scale bailout, has seen interest rates rise even in the wake of the European Central Bank (ECB) announcing a new pledge to buy the sovereign bonds of struggling European countries. We could be in for a bumpy 2013 if the ECB's promises are no longer sufficient to quiet European financial markets.

US Monetary Policy. With growth remaining sluggish, the Fed continues to tinker with the money supply. Operation Twist, which was an effort to flatten the yield curve by rebalancing the Fed's Treasury portfolio in favor of longer-term securities, was extended so that the Fed could purchase an additional $267 billion in bonds. Then, on September 13, 2012, the Federal Reserve followed up with the announcement of a third round of direct quantitative easing. QE3 will be open-ended and allow up to $40 billion per month in purchases of agency mortgage-backed securities. The stimulus is expected to continue until the country falls into a pattern of steady, strong labor market growth. Currently, the 10-year Treasury rate sits at 1.75 percent, up from a low of 1.5 percent reached in July of 2012, but down about 40 basis points from a year ago. Keeping interest rates low via measures like QE3 will make the dollar less attractive to other assets, because returns to dollar denominated assets will be lower than returns to the Chinese RMB and the Euro. Should the dollar depreciate, American goods will be more competitive abroad and foreign firms will find it less expensive to carry out business operations in the US. From a real estate ownership standpoint, lower interest rates will lead to lower cap rates (or investment return hurdles), which will push transaction prices higher.

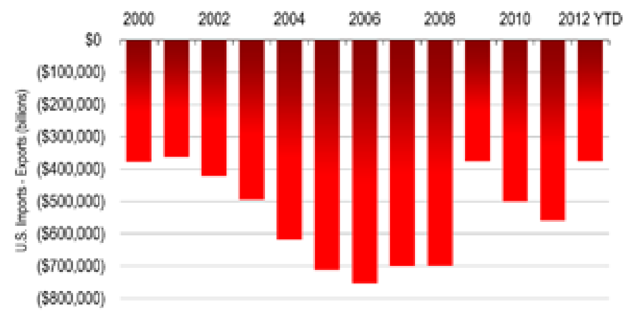
The Health of the US Housing Market. On the housing front, prices are finally on the rise again. The most recent Case-Shiller news release reported a 2.1 percent year-over-year increase in its "Composite 10" index and a 3 percent year-over-year increase in its "Composite 20" sample. Los Angeles recorded a 4 percent increase from September 2011 to September 2012. The

New Home Sales



Source | www.census.gov

Trade Deficit

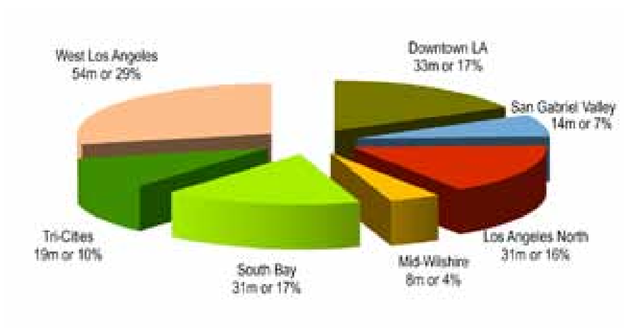


Source | Bureau of Economic Analysis, US Dept of Commerce median single-family house price for California as a whole stood at $341,370 as of October 2012, up a staggering 23 percent from a year earlier. At the national level, new home sales are up 27.1 percent from a year earlier. Existing home sales are up 10.9 percent nationally and 10.2 percent statewide. According to the California Association of Realtors, the inventory of homes selling for less than $750,000 stands at about 3.1 months, down from 5.5 months in October 2011. Just as the housing market brought down the economy in 2007-2008, we believe that a healthy housing market will bring the economy back in the coming year. We believe that GDP growth will be greater than what was predicted by the Survey of Professional Forecasters – about 2.7 percent – on account of improvements in the housing market.

Uncertainty over tax rates and broader fiscal policy. On January 1, 2013 the US will reach the so-called "fiscal cliff", which will trigger the elimination of the Bush tax cuts and enact drastic, across-the-board spending cuts. Most policymakers agree that the triggered changes are not the ideal path to deficit reduction, but there has been little consensus on the alternatives (and none of the proposed policies address the even bigger problem of the debt ceiling). Whatever the ultimate fiscal policies turn out to be, the longer the period of uncertainty, the bigger the damage will be to the economy as a whole – investment decisions rely on knowledge of tax rates, and individuals will not invest as long as they are unable to calculate the present value of a future set of cash flows. In California, some of the uncertainty over the state's fiscal situation was reduced recently as a result of the passage of Proposition 30, which raises the income tax on individuals making over $250,000 per year. Some analysts believe that the passage of Prop 30, combined with other economic improvements, will give the state a one billion dollar budget surplus by 2014.

In summary, most of the macroeconomic indicators of greatest concern previously have taken a sustained turn for the better over the last year. The biggest danger to recovery is, without question, the ongoing uncertainty about the nation's fiscal policy. As we've witnessed with Europe, enacting fiscal austerity measures before an economy has fully emerged from a recession will often have devastating effects. If Congress is able to come to an agreement on fiscal reform by the end of the year, we remain optimistic that the next 12 to 24 months will bring further economic improvement. If it cannot, the outlook is far more murky.

Size of Office Submarkets in Los Angeles County



Source | Newmark Grubb Knight Frank

Class A Rents and Vacancy Rates for LA County

Source | Newmark Grubb Knight Frank

Class B Rents and Vacancy Rates for LA County

Source | Newmark Grubb Knight Frank

Los Angeles County Office Market Trends

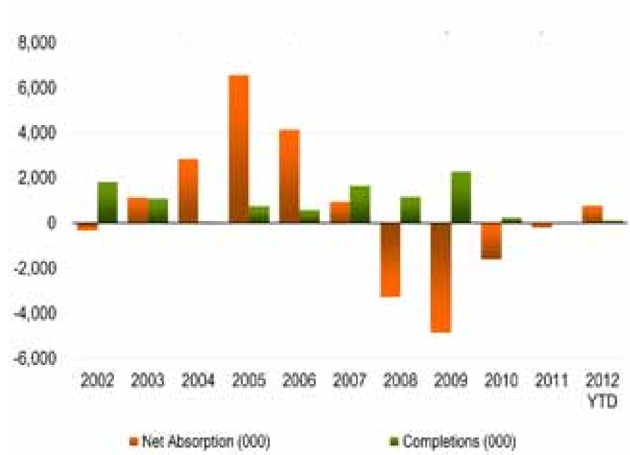
For the second year in a row, Los Angeles County is showing year-over-year improvements in employment. Total nonfarm employment between September 2011 and September 2012 rose by 66,100 jobs, while the unemployment rate fell 2.3 percentage points to 10.2 percent. The greatest gains in employment occurred in the professional and business services sector, leisure and hospitality, and financial activities. The largest job losses occurred in the manufacturing sector. Given that higher employment in office-oriented sectors tends to spur demand for office space, it's not surprising that Los Angeles County, overall, showed continued improvement from September 2011 to September 2012.

Four out of seven submarkets recorded positive net absorption through Q3 2012, leading to 402,000 square feet of net move-ins for the county as a whole. Los Angeles still has a long way to go, however, in erasing the nearly 6 million square feet of net move-outs that occurred between Q1 2009 and Q3 2010. The strongest performance, in relative terms, came from LA North, which posted 343,000 square feet of positive net absorption and a decline in vacancy of 1.0 percentage point. The Mid-Wilshire area was the worst performer relative to market size, recording 146,000 square feet of net move-outs and a 1.7 percentage-point increase in its vacancy rate. Mid-Wilshire overtook the South Bay submarket for the highest vacancy rate, ending Q3 2012 at 21.1 percent. For the third year in a row, San Gabriel Valley had the lowest vacancy rate by a 6 percentage-point margin.

As of Q3 2012, average Class A asking rents for Los Angeles County stood at $2.93 per square foot, down 0.4 percent for the year. Class B asking rents rose for the second year in a row to $2.19, an improvement of 0.8 percent.

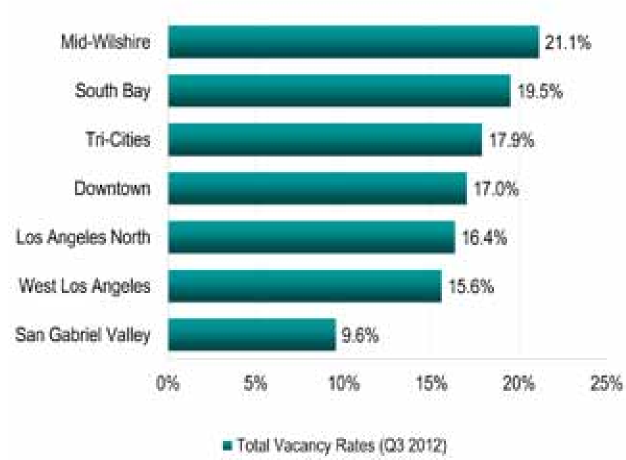
San Gabriel Valley experienced the largest drop in Class A rents among submarkets at 4.7 percent year-over-year. The Downtown submarket – the second most expensive in Los Angeles county – was the strongest performer, with a year-over-year increase of 4.0 percent. In spite of a 3.2 percent decline in average asking rents, West Los Angeles remained the most expensive among Los Angeles county submarkets, at $3.50 per square foot.

Net Absorption and Completions for LA County



Source | Newmark Grubb Knight Frank

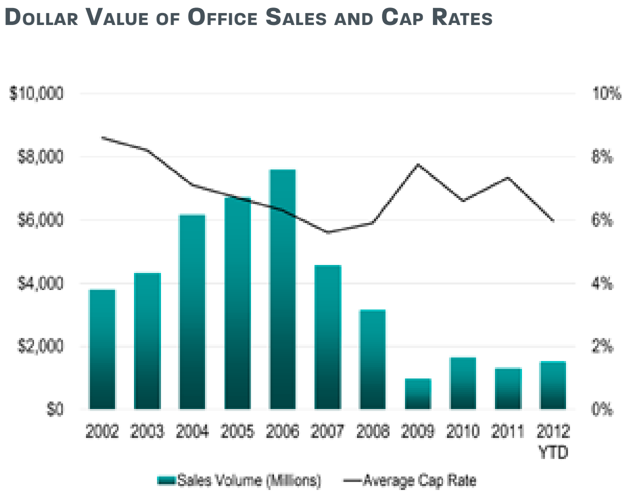
Office Vacancy Rates for LA County Submarkets



Source | Newmark Grubb Knight Frank

2012 Year-over-year Class A Rent Increases

Source | Newmark Grubb Knight Frank



Source | Newmark Grubb Knight Frank

Construction and Investment Activity

The period Q3 2011 to Q3 2012 brought the completion of one new office property, a 102,113 square foot Class A building in the LA North submarket. Sinanian Development's property was the first new office property delivered in Los Angeles since 2010. As of Q3 2012, 522,000 square feet of new office space is under construction, all of which is located in West Los Angeles.

Over the last couple of years, the financial markets have remained stable and lending standards have eased. Between low interest rates and lower levels of equity required to do deals, more investors have had the opportunity to enter the market. Nevertheless, a lot of capital still remains on the sidelines. Year-to-date sales volume for 2012, which stands at $1.5 billion, is up nearly 15 percent from the whole of 2011. But sales volume is down more than 80 percent from the peak achieved in 2006. Cap rates have bounced around considerably since 2009 and are largely dependent on the property classes and submarkets in which transactions are taking place. The average cap rate for 2012 deals stands at 6.0 percent, down from 7.3 percent in 2011. Even though Los Angeles is still considered a "gateway" market by institutional capital, investing has become hyper-local and less favored submarkets could face as much of a struggle to recover as secondary and tertiary metro areas around the rest of the US.

West Los Angeles

West Los Angeles is the largest and most expensive submarket in Los Angeles County, with 28.4 percent of the total office stock and just over 54 million square feet of space. Class A rents fell 3.2 percent from Q3 2011 to Q3 2012 after holding steady in the prior four quarters. West Los Angeles has taken the largest hit in rents among submarkets since the market peaked in Q1 2008, falling nearly 26 percent. Average asking rents stood at $3.50 per square foot as of Q3 2012.

Class B rents, on the other hand, made up most of the ground lost between Q3 2010 and Q3 2011. During the last four quarters, average asking rents rose 5.3 percent to $2.79 per square foot.

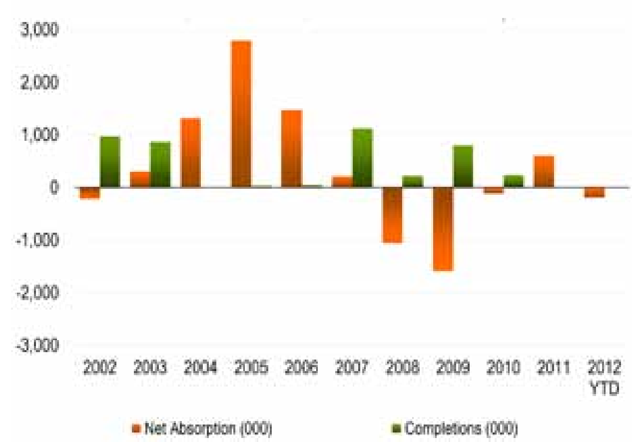
Demand for office space fell over the past year, resulting in over 290,000 square feet of net move-outs. Vacancy subsequently rose 0.8 percent, bringing the overall rate to 15.6 percent. In spite of this increase, West Los Angeles still has the second-lowest vacancy rate in the county.

No new office space came online over the last four quarters, but 522,000 square feet are currently under construction. Almost 95 percent of this construction is Class A space.

Rents and Vacancy Rates for West Los Angeles

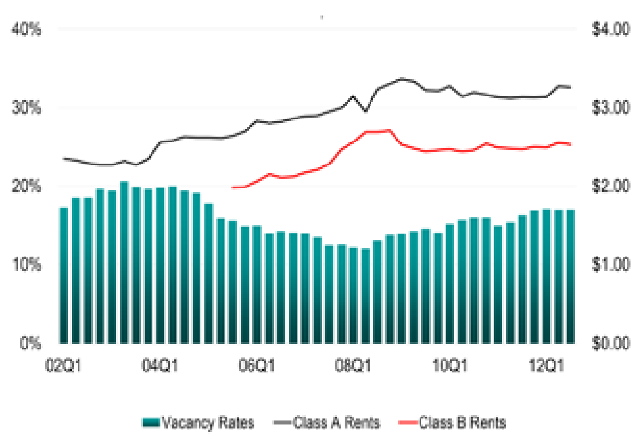
Source | Newmark Grubb Knight Frank

Net Absorption and Completions for West Los Angeles



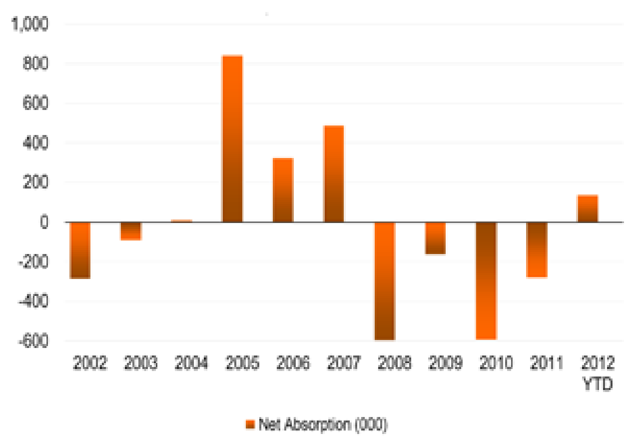
Source | Newmark Grubb Knight Frank

Rents and Vacancy Rates for Downtown LA



Source | Newmark Grubb Knight Frank

Net Absorption for Downtown LA



Source | Newmark Grubb Knight Frank

Rents and Vacancy Rates for South Bay

Source | Newmark Grubb Knight Frank

Downtown

For the third year in a row, the Downtown submarket experienced falling demand, recording 72,000 square feet of net move-outs. The vacancy rate subsequently rose 0.7 percentage points to 17.0 percent.

Average Class A asking rents also rebounded, rising 4 percent to $3.26 per square foot. Class B rents rose a nickel (2.5 percent) to $2.53 per square foot. The downtown submarket remains the second largest and second most expensive office market in the county after West Los Angeles.

South Bay

After a dismal period of falling demand from Q1 2010 to Q3 2011, in which it recorded around 2.2 million square feet of net move-outs, the South Bay submarket began to inch its way back in 2012. The area recorded nearly 460,000 square feet of net move-ins and saw vacancy decline 0.7 percentage points to 19.5 percent. The area surpassed the Mid-Wilshire submarket to have the second-highest vacancy rate in the county.

Class A rents continued to remain stable at $2.28 per square foot. Class B rents, meanwhile, rose 2.3 percent to $2.05 per square foot.

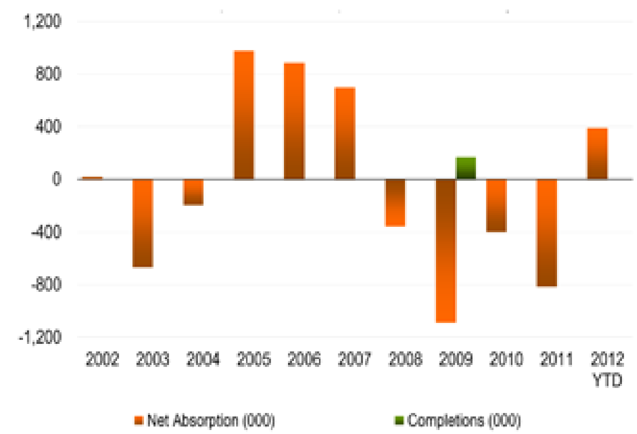
Los Angeles North

For the third year in a row, Los Angeles North posted a significant increase in demand, logging 343,000 square feet of positive net absorption and a decline in vacancy of 1 percentage point. The submarket ended Q3 2012 with a vacancy rate of 16.4 percent. The area's performance was the strongest among Los Angeles submarkets relative to market size. The increase in demand may have been aided by the addition of another 10,000 new jobs to the motion picture industry, a heavy user of office space in the North submarket.

Class A rents continued to decline, but the decline over the last four quarters was smaller than in previous years. Class A rents fell 1.4 percent to $2.29 per square foot. Class B rents fared worse from Q3 2011 to Q3 2012 than in the prior year, falling 5.4 percent to $2.01 per square foot.

The Los Angeles North submarket was the only submarket to receive any new stock between Q3 2011 and Q3 2012. In August 2012, Sinanian Development finished the 102,000 square foot Santa Clarita Professional Center.

Net Absorption and Completions for South Bay

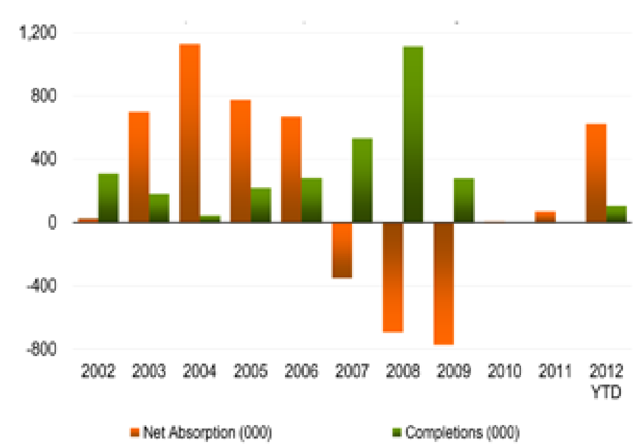


Source | Newmark Grubb Knight Frank

Rents and Vacancy Rates for Los Angeles North

Source | Newmark Grubb Knight Frank

Net Absorption and Completions for Los Angeles North



Source | Newmark Grubb Knight Frank

Tri-Cities

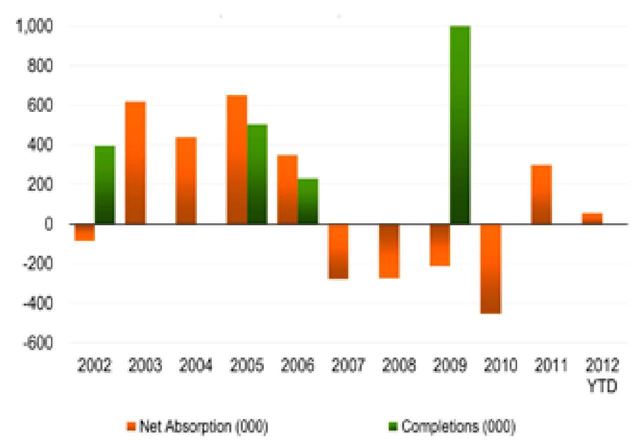
Following a strong increase in demand from Q3 2010 to Q3 2011, the Tri-Cities submarket saw little change in occupancy from Q3 2011 to Q3 2012: the area recorded 9,500 square feet of net move-ins and saw vacancy fall by 0.1 percent

Average Class A asking rents fell a penny to $2.80 per square foot, an improvement over the 2.1 and 4.3 percent declines witnessed over the prior two years. The Tri-Cities area boasts the third-highest rents among Los Angeles submarkets. Class B asking rents rose 2.7 percent to $2.29 per square foot.

Rents and Vacancy Rates for Tri-Cities

Source | Newmark Grubb Knight Frank

Net Absorption and Completions for Tri-Cities



Source | Newmark Grubb Knight Frank

San Gabriel Valley

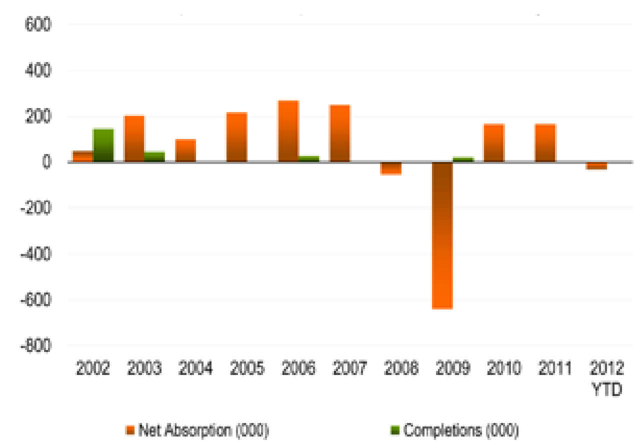
Between Q3 2011 and Q3 2012, San Gabriel Valley more than doubled the occupancy gains made in the prior four quarters, recording 100,000 square feet of net move-ins. The submarket continued to carry the lowest vacancy rate in the county by a significant margin at 9.6 percent. West Los Angeles remained in second place at 15.6 percent vacancy.

Average Class A asking rents fell another 4.7 percent to $2.29 per square foot, bringing the overall decline from the market peak to 16.5 percent. Class B rents fell 1.8 percent to $1.88 per square foot, erasing the gains made from Q3 2010 to Q3 2011.

Rents and Vacancy Rates for San Gabriel Valley

Source | Newmark Grubb Knight Frank

Net Absorption and Completions for San Gabriel Valley

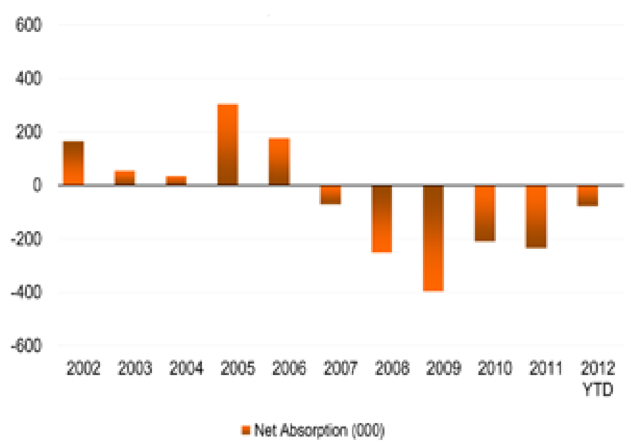


Source | Newmark Grubb Knight Frank

Rents and Vacancy Rates for Mid-Wilshire

Source | Newmark Grubb Knight Frank

Net Absorption and Completions for Mid-Wilshire



Source | Newmark Grubb Knight Frank

Mid-Wilshire

For the third year in a row, the Mid-Wilshire submarket experienced a significant decline in demand, posting negative net absorption of 146,000 square feet. Mid-Wilshire is the smallest of the Los Angeles submarkets with only 8.2 million square feet of office space. Vacancy rose 1.7 percentage points to 21.1 percent – the highest vacancy rate among submarkets. With ample sublease space available at reduced rents in the West Los Angeles and Downtown submarkets, the Mid-Wilshire area has lost some of its attraction as a low-cost alternative.

Class A asking rents rose two cents over the past year to $2.02 per square foot, while Class B asking rents fell two cents to $1.65. These are the lowest asking rents for Class A and B among the Los Angeles submarkets by more than $0.20 per square foot.

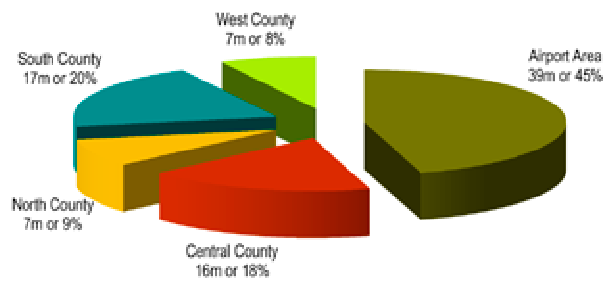
Due to space constraints, there has been very little office construction in the Mid-Wilshire submarket over the last decade and none is expected in the foreseeable future.

Orange County Office Market Trends

For the third year in a row, Orange County has experienced overall economic improvement; the unemployment rate fell to 7.1 percent in September 2012, which is the lowest among the counties discussed in the report. Orange County gained 24,300 nonfarm jobs between September 2011 and September 2012, 9,500 of which came in September 2012 itself. Leisure and hospitality, professional and business services, and financial activities posted the largest gains, while government posted the largest losses. As in Los Angeles, the strong performance of the professional and business services sector was a likely driver of the improved performance of the Orange County office market over the last year.

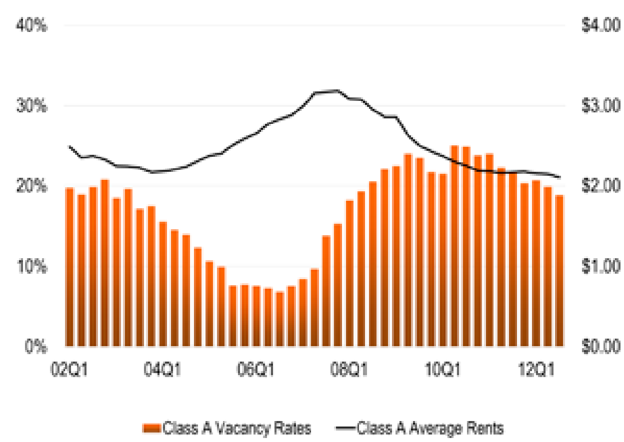
From Q3 2011 to Q3 2012, Orange County saw continued improvement in its office market, although demand was not as strong as during the prior four quarters. The county overall experienced 1.65 million square feet of net move-ins, down from 1.9 million square feet. The vacancy rate subsequently fell 1.7 percentage points to 16.6 percent. Although the Orange County office market is by no means in good shape, it has made great strides toward recovery during the last eight quarters.

Size of Office Submarkets in Orange County



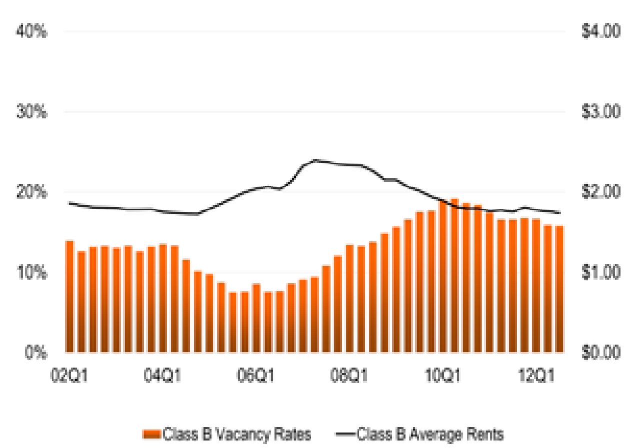
Source | Newmark Grubb Knight Frank

Class A Rents and Vacancy Rates for Orange County



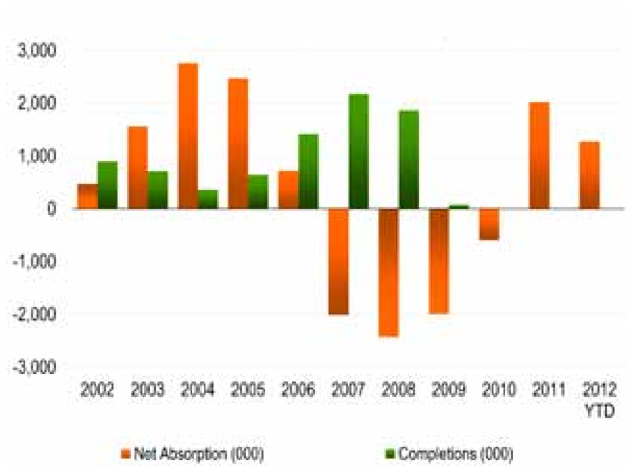
Source | Newmark Grubb Knight Frank

Class B Rents and Vacancy Rates for Orange County



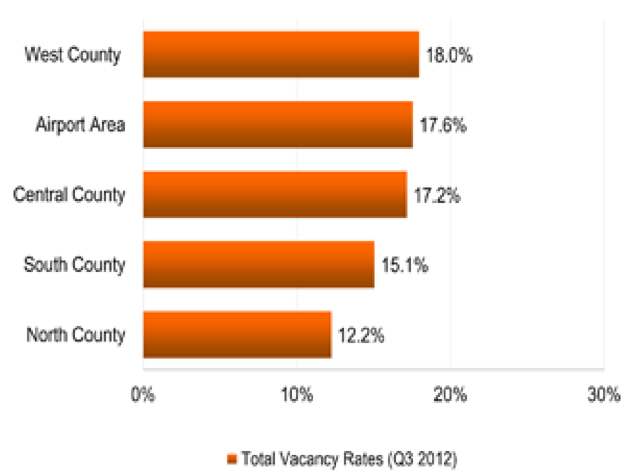
Source | Newmark Grubb Knight Frank

Net Absorption and Completions for Orange County



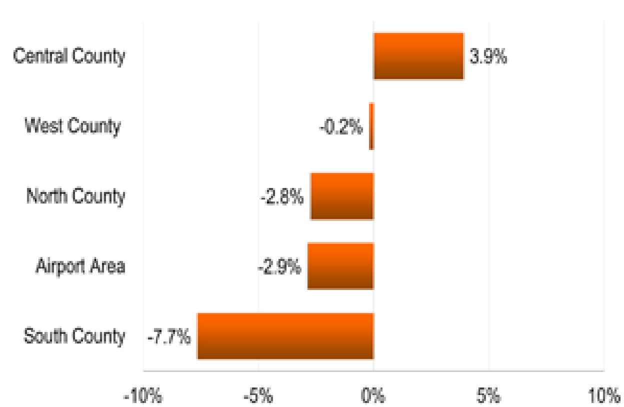
Source | Newmark Grubb Knight Frank

Office Vacancy Rates for Orange County Submarkets



Source | Newmark Grubb Knight Frank

2012 Year-over-year Class A Rent Changes



Source | Newmark Grubb Knight Frank

The Airport area logged the highest absolute level of net move-ins, at 1.15 million square feet, while the North County submarket recorded the highest level of net move-ins relative to market size. The North County submarket ended Q3 2012 with the lowest vacancy rate in the county; vacancy fell 3.7 percentage points to 12.2 percent. The West County submarket was the only one to experience negative net absorption over the last four quarters, with 170,000 square feet of net move-outs. The vacancy rate subsequently rose 5.5 percentage points to 18 percent, which is the highest level among Orange County submarkets.

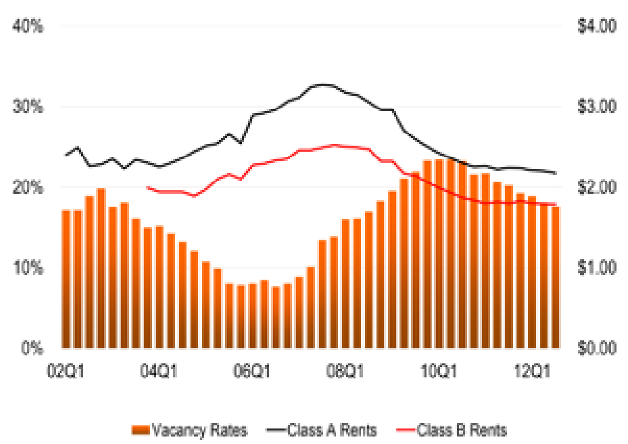
Average asking rents continued to fall in Orange County, however, the declines have been decreasing over time. Between Q3 2011 and Q3 2012, Class A and Class B rents fell by 2.9 percent and 0.9 percent, respectively. Class A rents ended Q3 2012 at $2.11 per square foot, while Class B rents ended the quarter at $1.73 per square foot. Central County posted the strongest Class A rent performance among submarkets and was the only one to see a year-over-year rent increase. Average asking rents rose 3.9 percent to $2.06 per square foot. South County took the greatest hit in Class A rents, posting a decline of 7.7 percent to $1.90 per square foot. South County now stands as the least expensive office submarket in Orange County.

Construction and Investment Activity

For the second year in a row, no new office space was completed in Orange County. Eight hundred forty-nine thousand square feet of office space are currently under construction, divided between the Airport and West County submarkets. Year-to-date sales volume stood at $467 million, which is only 5 percent off the total for 2011. Since witnessing an astonishing $4.7 billion in office transactions in 2007, Orange County has not seen more than $1 billion per year in office sales. The average cap rate stands at 5.6 percent, up a tick from 2011.

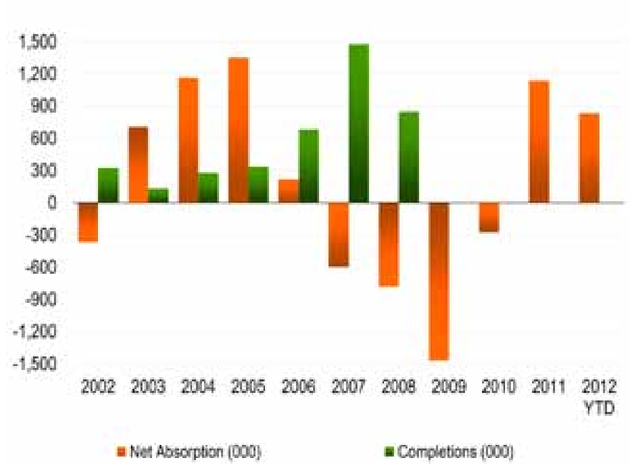
Dollar Value of Office Sales and Cap Rates

Rents and Vacancy Rates for Orange County Airport Area



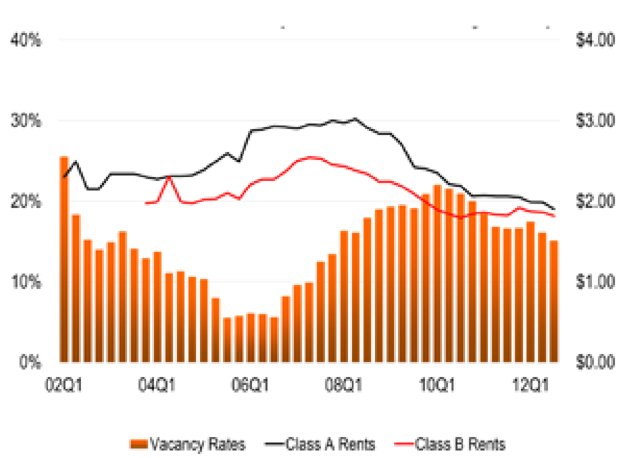
Source | Newmark Grubb Knight Frank

Net Absorption and Completions for Orange County Airport Area



Source | Newmark Grubb Knight Frank

Rents and Vacancy Rates for South Orange County



Source | Newmark Grubb Knight Frank

Airport

The Airport area is the central hub for the Orange County office market. With 39 million square feet, it is the largest submarket and is home to many of the region's most prominent Class A buildings. From Q3 2011 to Q3 2012, the area recorded 1.15 million square feet of positive net absorption, bringing the total move-ins over the last eight quarters to 2.25 million square feet. The vacancy rate fell another 2.6 percentage points to 17.6 percent. Despite the strong increases in demand over the last two years, the area's vacancy rate is the second-highest in the county.

Major companies continued to take advantage of their relative size and strength as renters to lock in lower rates in the Airport area. Average Class A asking rents declined another 2.9 percent to $2.18 per square foot, bringing the total decline since the market peak to 33.5 percent. Class B asking rents fell 0.5 percent to $1.79 per square foot.

Three hundred eighty thousand square feet of new, Class A office space are currently under construction in the Airport submarket.

South County

The South County submarket accounts for 20 percent of the overall office space in Orange County, or about 17 million square feet. Like the Airport submarket, South County experienced a second straight year of strong demand. The 226,000 square feet of net move-ins brought the total net absorption over the last two years to 1.14 million square feet. The vacancy rate subsequently fell 1.4 percentage points to 15.1 percent.

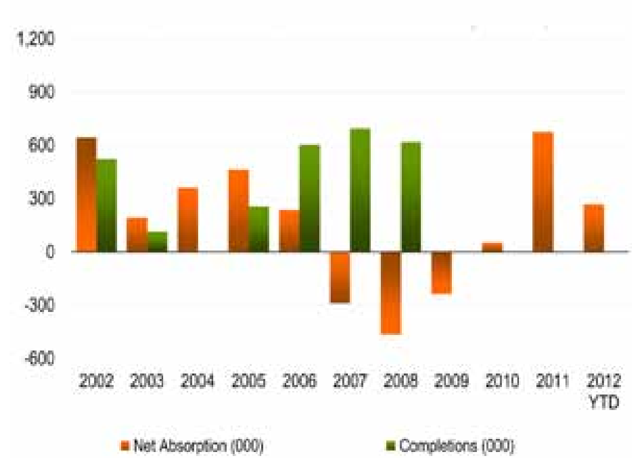
For the fourth consecutive year, Class A rents declined. Average asking rents fell another 7.7 percent over the last four quarters to bring the total decline since the market peak to 36.6 percent. At $1.90 per square foot, South County has the lowest rents in the county and is the only submarket with Class A rents below $2.00 per square foot. Average Class B asking rents held steady at $1.82 per square foot, the highest level in the county.

North County

After posting a small decline in vacancy from Q3 2010 to Q3 2011, North County bounced back with 302,000 square feet of positive net absorption and a 3.7 percentage-point decline in the vacancy rate. As of Q3 2012, the vacancy rate stood at 12.2 percent, which is the lowest level in the county by almost 3 percentage points.

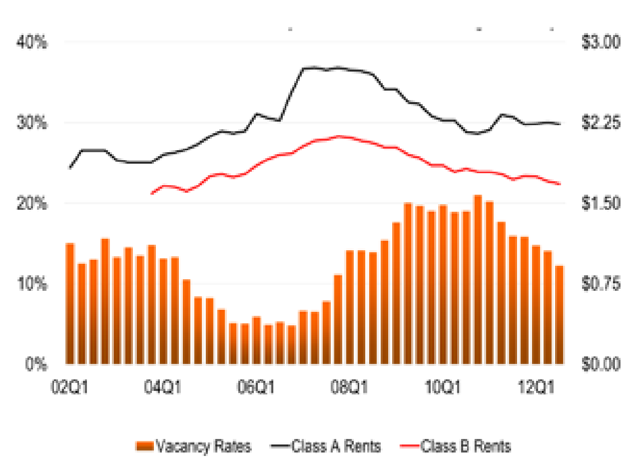
Although average Class A asking rents fell 2.8 percent to $2.24 per square foot, the area has experienced the smallest overall peak-to-trough decline at 19 percent and remains the most expensive submarket in the county in the Class A sector. Class B rents were down 2.3 percent to $1.68 per square foot, an improvement over the 5-plus percent declines experienced in each of the prior two years.

Net Absorption and Completions for South Orange County



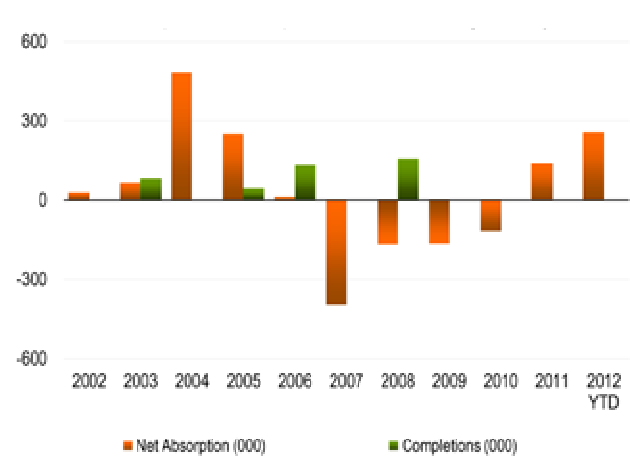
Source | Newmark Grubb Knight Frank

Rents and Vacancy Rates for North Orange County



Source | Newmark Grubb Knight Frank

Net Absorption and Completions for North Orange County



Source | Newmark Grubb Knight Frank

Rents and Vacancy Rates for Central Orange County

Source | Newmark Grubb Knight Frank

Net Absorption and Completions for Central Orange County

Source | Newmark Grubb Knight Frank

Central County

Demand for office space improved from Q3 2011 to Q3 2012: the submarket posted 138,000 square feet of net move-ins and logged a 1.5 percentage-point decline in the vacancy rate. As of Q3 2012, the vacancy rate stood in the middle of the pack at 17.2 percent.

After experiencing the poorest performance in asking rents among Orange County submarkets from Q3 2010 to Q3 2011, the Central County area came out on top over the last four quarters and was the only submarket to record a year-over-year rent increase. Average Class A asking rents rose 3.9 percent to $2.06 per square foot. Class B rents fell a penny to $1.64 per square foot. Central County has the second-lowest rents among both Class A and Class B properties.

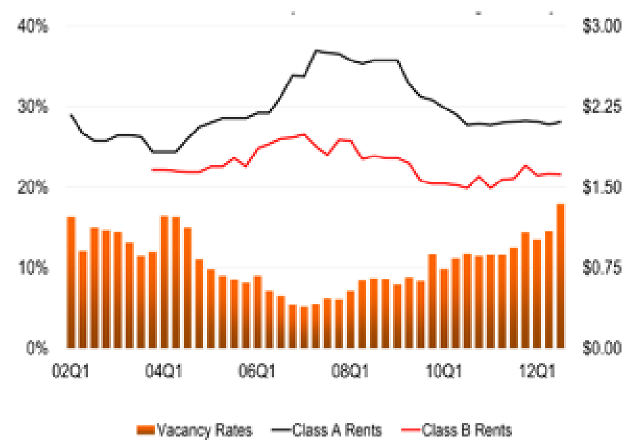
West County

Although rents remained stable over the last year, demand took quite a tumble: the West County area witnessed 170,000 square feet of net move-outs and a subsequent 5.5 percentage-point rise in the vacancy rate. The vacancy rate moved from a county low of 12.5 percent to a county high of 18 percent.

Average Class A asking rents held steady at $2.11 per square foot. Class B asking rents rose 2.4 percent to $1.62 per square foot and remained the lowest among Orange County submarkets.

About 470,000 square feet of Class B office space is currently under construction.

Rents and Vacancy Rates for West Orange County

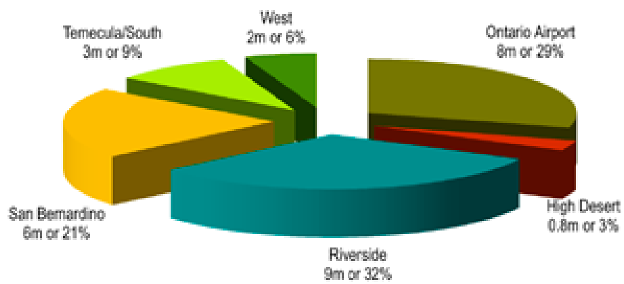


Source | Newmark Grubb Knight Frank

Net Absorption and Completions for West Orange County

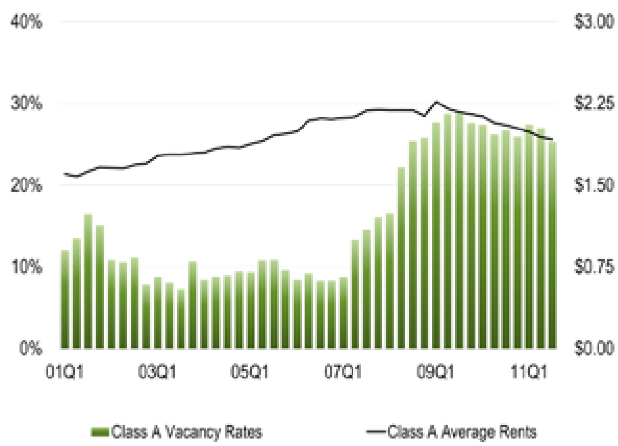
Source | Newmark Grubb Knight Frank

Size of Office Submarkets in the Inland Empire



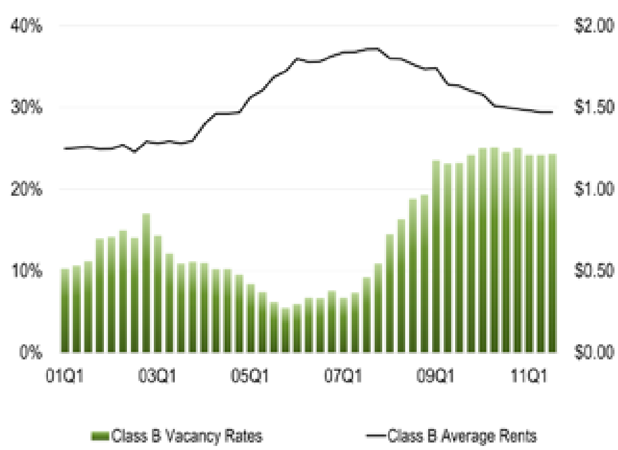
Source | Newmark Grubb Knight Frank

Class A Rents and Vacancy Rates for Inland Empire



Source | Newmark Grubb Knight Frank

Class B Rents and Vacancy Rates for Inland Empire



Source | Newmark Grubb Knight Frank

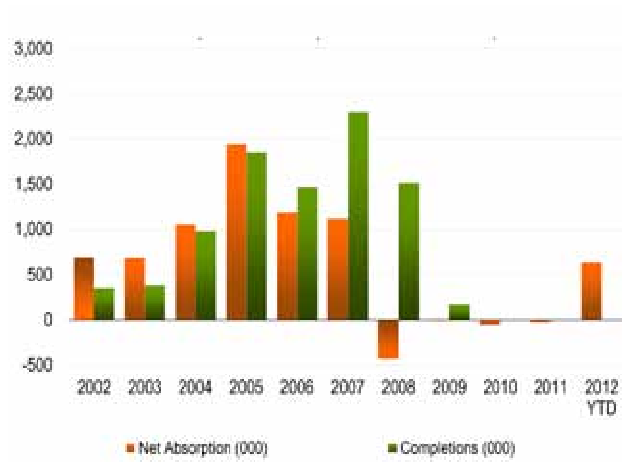
Inland Empire Office Market Trends

Among the Southern California markets discussed in this report, Riverside and San Bernardino Counties have struggled the most as a result of the subprime crisis and overall economic downturn. But like the other metro markets, the Inland Empire has begun to show signs of recovery over the last eight quarters. As of September 2012, unemployment in the region stood at 11.6 percent, down 1.9 percentage points from a year earlier. Total non-farm employment rose by 16,400 jobs. The greatest gains came in the sectors of professional and business services, trade, transportation and utilities, and leisure and hospitality. As with Orange County, the greatest job losses occurred in the government sector.

Although demand rose in all five Inland Empire submarkets, the market-wide vacancy rate remains the highest in Southern California at 21.1 percent. Between Q3 2010 and Q3 2011, the region reported 721,000 square feet of net move-ins, and a decline in the vacancy rate of 2.7 percentage points. The Riverside submarket experienced the largest absolute increase in demand with 350,000 square feet of positive net absorption, while the Temecula/South submarket experienced the largest relative increase in demand. The area's 145,000 square feet of net move-ins led to a decline in the vacancy rate of 6.3 percentage points. At the end of Q3, the vacancy rate stood at 19.0 percent. The Ontario Airport submarket currently has the highest vacancy rate, at 23.3 percent, while the tiny West submarket boasts the lowest vacancy rate at 17.4 percent.

After logging a 6.3 percent decline in rents from Q3 2010 to Q3 2011, the Inland Empire office market witnessed a slightly-less-dismal 3.6 percent decline from Q3 2011 to Q3 2012. At the end of Q3 2012, rents stood at $1.85 per square foot. The Class B market, which makes up the majority of Inland Empire office space, held steady at $1.47 per square foot. The Temecula/South submarket was the top performer in the Class A category, and the only submarket to experience a year-over-year rent increase. Average asking rents rose 6.4 percent to end Q3 2012 at $1.83 per square foot. Interestingly, in the Class B category, the Temecula/South submarket was the worst performer, recording a year-over-year rent decline of just over 5 percent. The Riverside submarket was the worst performer in the Class A category, logging an 8.3 percent year-over-year decline.

Net Absorption and Completions for Inland Empire

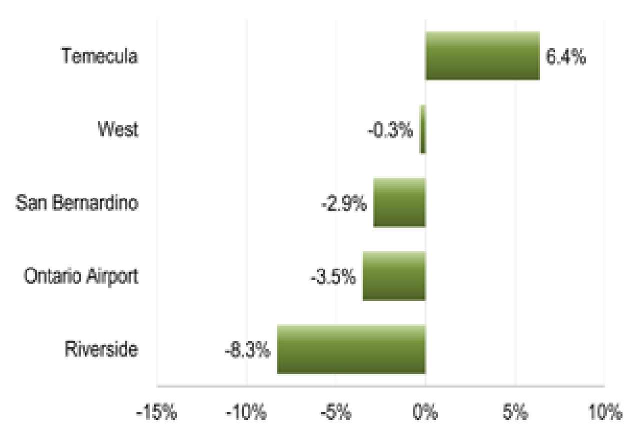


Source | Newmark Grubb Knight Frank

Office Vacancy Rates for Inland Empire Submarkets

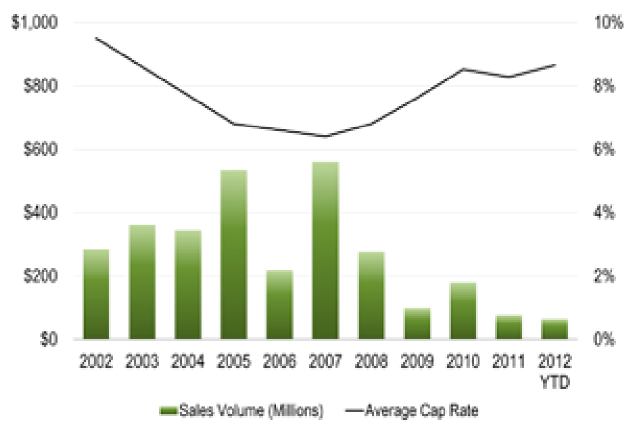
Source | Newmark Grubb Knight Frank

2012 Year-over-year Class A Rent Changes



Source | Newmark Grubb Knight Frank

Dollar Value of Office Sales and Cap Rates



Construction and Investment Activity

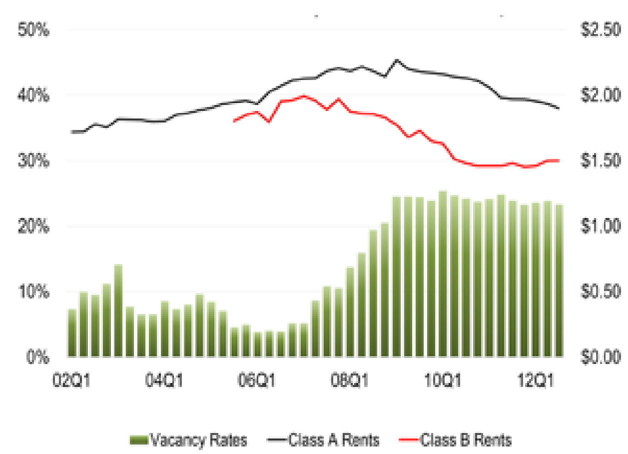
The period Q3 2011 to Q3 2012 brought the completion of one new office property, a 141,133 square foot Class A building in the Riverside submarket. Regional Properties' 6-story Citrus Tower was the first office completion of 20,000 square feet or more in the Inland Empire since 2010. No new space is currently under construction. Year-to-date sales volume stood at $64.6 million, 15.5 percent below the 2011 calendar-year total. The average going-in cap rate rose from 8.3 to 8.7 percent.

Ontario Airport Region

At around 8.5 million square feet, the Ontario Airport submarket comprises 29 percent of the Inland Empire office market and is the second largest submarket after Riverside. The data collection area includes Ontario, Fontana, Mira Loma, and Rancho Cucamonga. The submarket witnessed an increase in demand for the fourth year in a row, with 59,000 square feet of net move-ins.

Class A asking rents fell 3.5 percent to $1.90 per square foot, while class B asking rents rose two cents to $1.50 per square foot.

Rents and Vacancy Rates for Ontario Airport

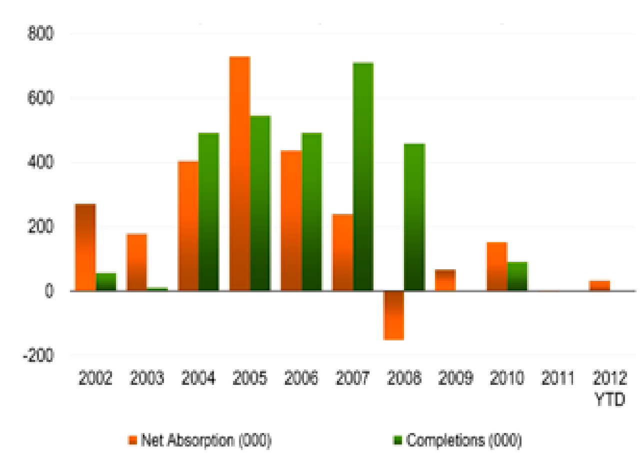


Source | Newmark Grubb Knight Frank

Riverside

The Riverside area is the largest office submarket in the Inland Empire, with 8.85 million square feet of space. From Q3 2011 to Q3 2012, the area logged 350,000 square feet of net absorption, a five-fold increase from the prior four quarters. The vacancy rate subsequently fell 4.8 percentage points to 20.4 percent.

Net Absorption and Completions for Ontario Airport

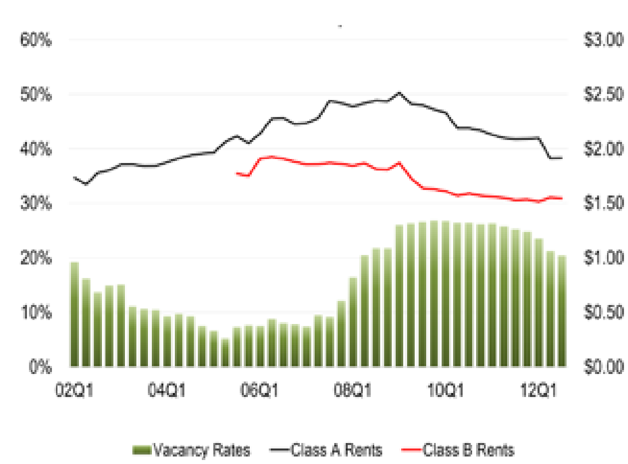


Source | Newmark Grubb Knight Frank

Although unemployment in Riverside County is the highest among the four counties discussed in the report, the area has seen some significant improvement in the last year. The unemployment rate fell 1.9 percentage points between Q3 2011 and Q3 2012, and currently sits at 12 percent. We should expect to see further improvement in the Riverside office market if the employment picture continues to improve.

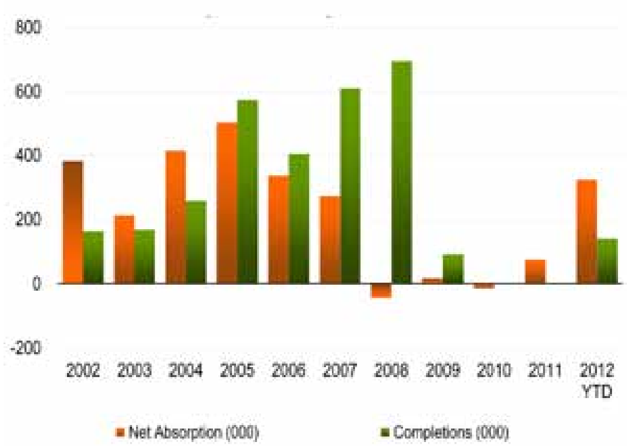
From Q3 2011 to Q3 2012, average Class A asking rents fell 8.3 percent to $1.92 per square foot, bringing the total rent decline from the Q1 2009 peak to around 23.8 percent. Class B rents rose 1 percent to $1.55 per square foot. The Riverside area has the highest average Class B asking rents among Inland Empire submarkets.

Rents and Vacancy Rates for Riverside



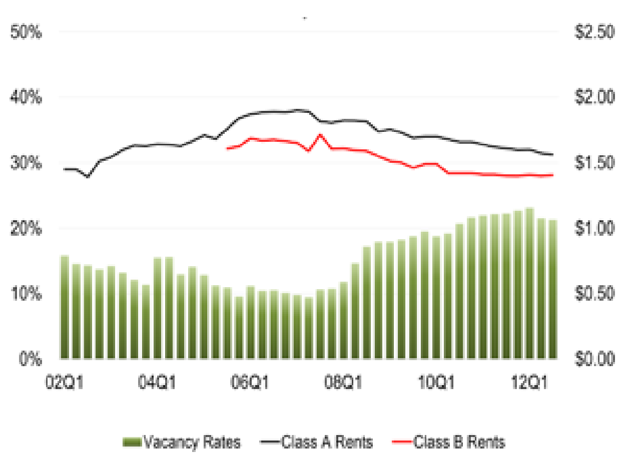
Source | Newmark Grubb Knight Frank

Net Absorption and Completions for Riverside



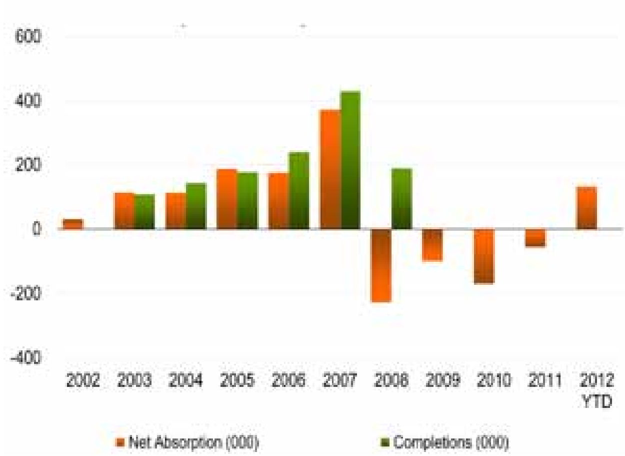
Source | Newmark Grubb Knight Frank

Rents and Vacancy Rates for San Bernardino



Source | Newmark Grubb Knight Frank

Net Absorption and Completions for San Bernardino



Source | Newmark Grubb Knight Frank

San Bernardino

The San Bernardino submarket accounts for 21 percent of the Inland Empire office stock, or 6 million square feet. The data collection area includes the city of San Bernardino, Colton, Loma Linda, Redlands, and Rialto. It is the lowest priced submarket and carries the second-highest vacancy rate at 21.3 percent.

From Q3 2011 to Q3 2012, San Bernardino erased the net move-outs incurred during the prior four quarters with 136,000 square feet of positive net absorption. This performance led to a decline in the vacancy rate of 0.9 percentage points.

Class A asking rents declined 2.9 percent to $1.56 per square foot, while Class B rents rose a penny to $1.41 per square foot. San Bernardino claims the lowest Class A asking rents in the Inland Empire by more than $0.25 per square foot.

Temecula/South

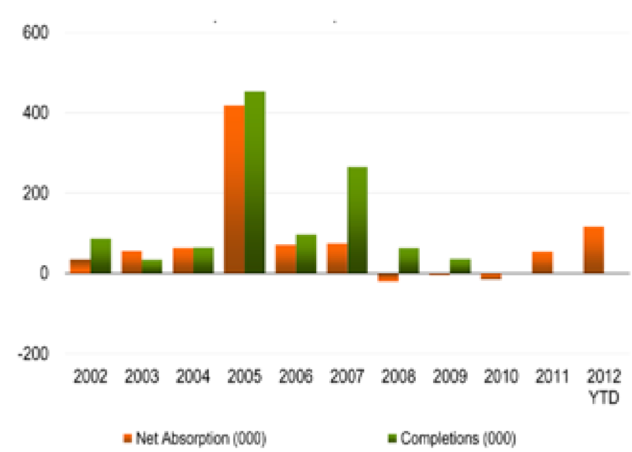
The Temecula/South area accounts for around 9 percent of the office space in the Inland Empire, or 2.5 million square feet, and includes the city of Temecula, Lake Elsinore, Murrieta, and Wildomar. The area witnessed a significant improvement in demand from Q3 2011 to Q3 2012, recording 145,000 square feet of net move-ins and a decline in the vacancy rate of 6.3 percentage points. The vacancy rate stood at 19 percent at the end of Q3 2012. The Temecula/South submarket, which previously carried the highest vacancy rate in the county, now carries the second lowest.

Class A asking rents rose 6.4 percent from Q3 2011 to Q3 2012, after declining sharply in the prior three years. Class B rents fell 5.1 percent, adding to the 6.6 percent decline recorded in the prior four quarters. Class A and Class B rents stand at $1.83 and $1.33 per square foot, respectively. The Temecula/South submarket has the lowest Class B asking rents in the Inland Empire, and has posted the largest overall peak-to-trough decline in Class B asking rents at 36 percent. Industrial Trends

Rents and Vacancy Rates for Temecula

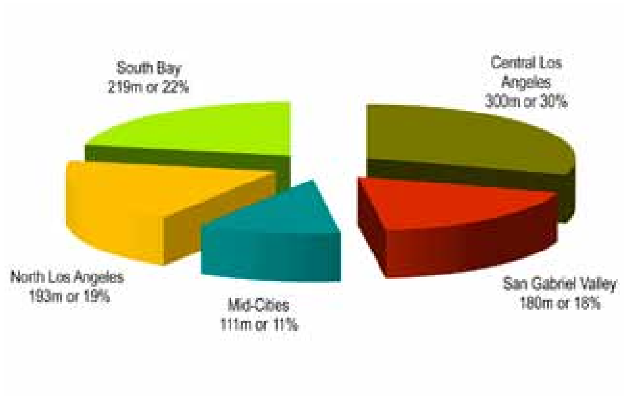
Source | Newmark Grubb Knight Frank

Net Absorption and Completions for Temecula



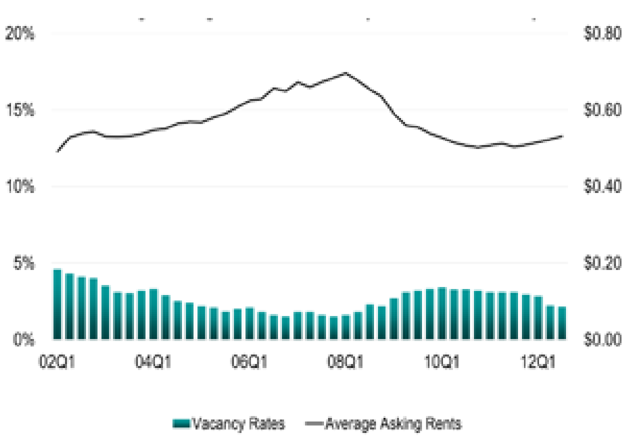
Source | Newmark Grubb Knight Frank

Size of Industrial Submarkets in Los Angeles County



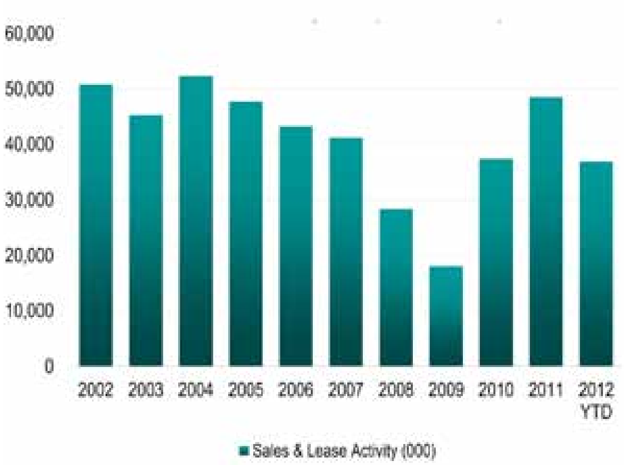
Source | Newmark Grubb Knight Frank

Average Asking Rents and Vacancy Rates for LA County



Source | Newmark Grubb Knight Frank

Sales & Leasing for LA County



Source | Newmark Grubb Knight Frank

Los Angeles County Industrial Market Trends

Over the last year, the Los Angeles industrial market experienced a substantial increase in demand, with positive net absorption of 9.05 million square feet. The vacancy rate currently sits at 2.1 percent, down 1 percentage point from Q3 2011 and only 0.6 percentage points off its market-peak level. Los Angeles remains the tightest industrial market in the United States.

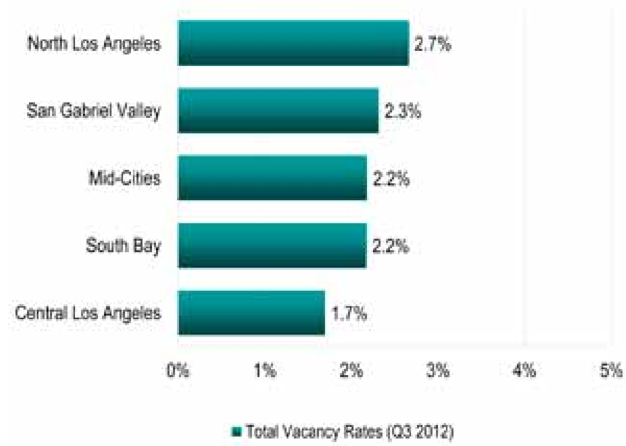
The Mid-Cities submarket experienced the largest relative increase in demand, logging nearly 2 million square feet of net absorption on a stock of about 111 million square feet. Consequently, the vacancy rate fell 1.9 percentage points. The San Gabriel Valley submarket recorded the highest absolute increase in demand, with 2.5 million square feet of net move-ins on a stock of 180 million square feet. Mid-Cities and San Gabriel Valley, which are the two smallest of the Los Angeles County submarkets, stand at 2.2 and 2.3 percent vacancy, respectively.

Owner-user purchases and overall leasing activity stand at 36.9 million square feet for 2012. If the YTD pace of sales and leasing activity hold up through Q4 2012, the annual totals will be on par with 2011 levels.

Countywide average asking rents were up 6.3 percent to $0.53 per square foot. And for the first time in the post-crisis era, all five submarkets logged year-over-year increases. For the second year in a row, Central Los Angeles was the clear winner, recording a 14.2 percent increase in average asking rents. San Gabriel Valley was the weakest performer, registering a 0.3 percent rise in rents. North Los Angeles remains the most expensive industrial submarket, with average asking rents of $0.64 per square foot.

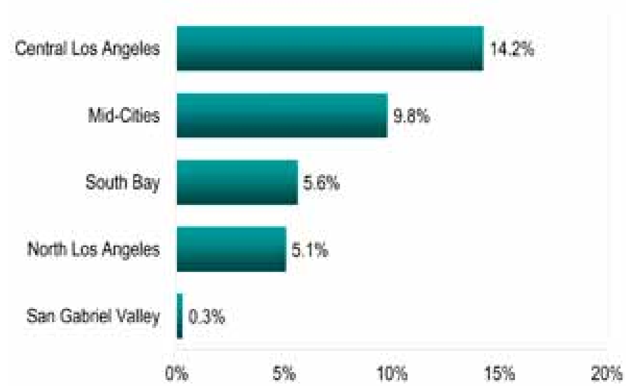
After rising 4.4 percent from Q3 2010 to Q3 2011, warehouse and distribution rents rose another 3.9 percent in the last four quarters to settle at $0.49 per square foot. General industrial space experienced a strong turnaround over the last year after three straight years of decline. Average asking rents rose 7.4 percent to $0.55 per square foot. The Los Angeles industrial market is divided nearly 50-50 between these two property sub-types. R&D/Flex space experienced the largest increases in rents (and remains the most expensive of industrial sub-types) but makes up a miniscule share of the overall industrial stock.

Industrial Vacancy Rates for LA Submarkets



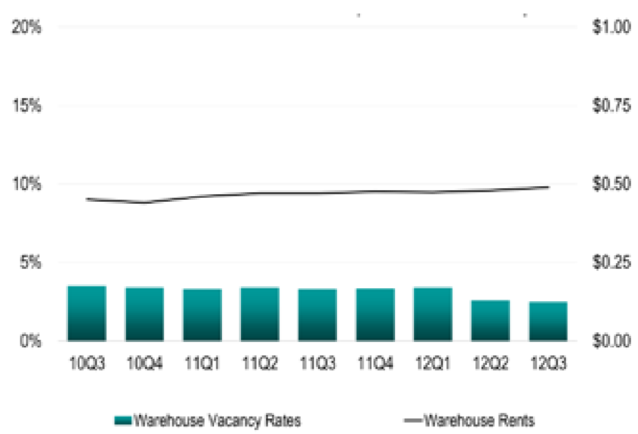
Source | Newmark Grubb Knight Frank

2012 Year-over-year Average Rent Changes



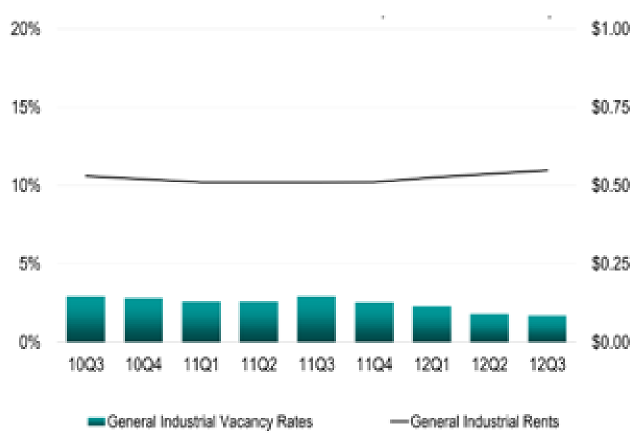
Source | Newmark Grubb Knight Frank

Warehouse Rents and Vacancy Rates for LA County



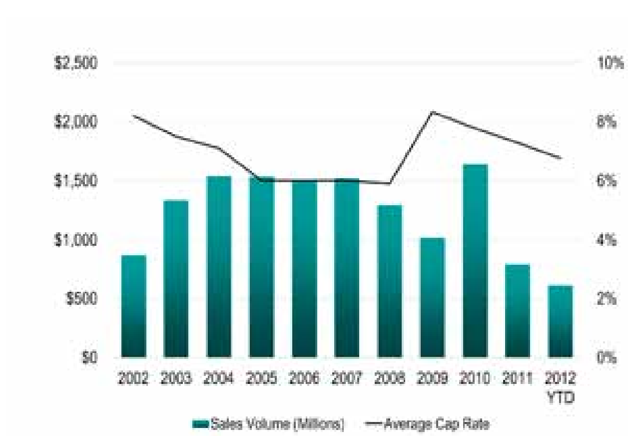
Source | Newmark Grubb Knight Frank

General Industrial Rents and Vacancy Rates for LA County



Source | Newmark Grubb Knight Frank

Dollar Value of Industrial Sales and Cap Rates



Source | Newmark Grubb Knight Frank

Construction and Investment Activity

From Q3 2011 to Q3 2012, around 1.1 million square feet of new industrial space came online across six properties. Completions were divided between the South Bay (62.6 percent), San Gabriel Valley (27.6 percent), and Mid-Cities submarkets (9.8 percent). About 1.13 million square feet of new industrial space are currently under construction across the Central, Mid-Cities, and South Bay submarkets

Sales volume through Q3 2012 stood at $614 million. If the average pace of transactions continues through the end of the year, total sales will finish slightly ahead of the 2011 level. The average cap rate for 2012 stood at 6.8 percent, down half a percentage point from 2011.

Central Los Angeles

The Central Los Angeles submarket experienced a surge in demand from Q3 2011 to Q3 2012. The area experienced 1.86 million square feet of positive net absorption and saw a drop in vacancy of 0.8 percentage points. Central Los Angeles continues to be the tightest submarket in the Los Angeles County industrial market with a vacancy rate of 1.7 percent. With just over 300 million square feet of industrial space, Central Los Angeles is the largest industrial submarket in Los Angeles County and among the densest industrial zones in the nation.

As the industrial market has tightened, average asking rents have subsequently increased. Average asking rents rose a tremendous 14.2 percent year-over-year to rest at $0.47 per square foot. Still, average asking rents are down 22.3 percent from the Q1 2007 peak.

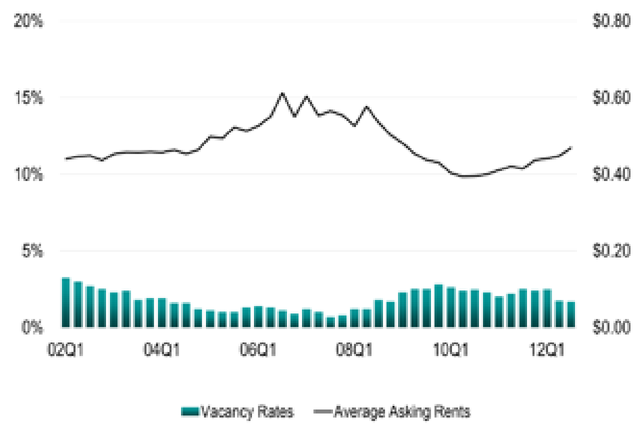
About 100,000 square feet of general industrial space is currently under construction in the area.

North Los Angeles

From Q3 2011 to Q3 2012, demand for industrial space increased in North Los Angeles submarket. The area recorded 441,000 square feet of net move-ins and saw vacancy fall half a percentage point. At 2.7 percent, the vacancy rate stands less than one percentage point above its Q4 2006 low.

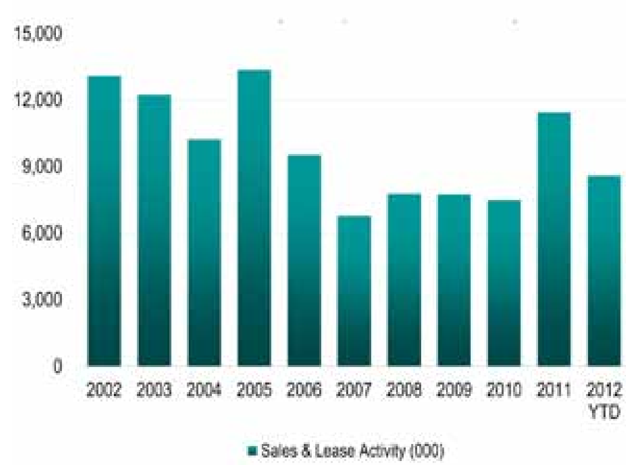
After two years of significant rent declines, the North Los Angeles submarket rebounded from Q3 2011 to Q3 2012 with a rent increase of 5.1 percent. Average asking rents stand at $0.64 per square foot, the highest level among Los Angeles submarkets. Average asking rents are down about 28 percent from the Q1 2008 peak.

Average Asking Rents and Vacancy Rates for Central Los Angeles



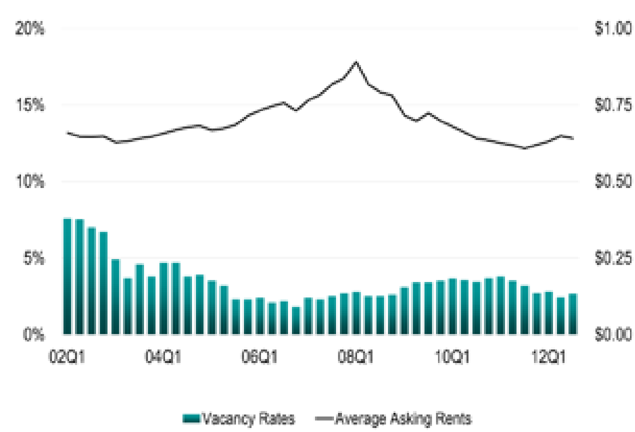
Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for Central Los Angeles



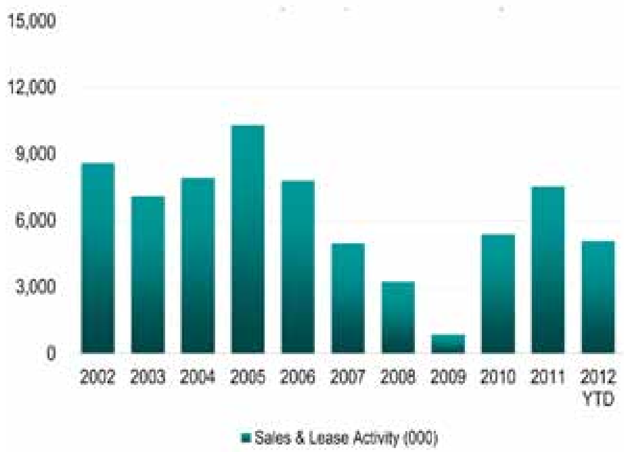
Source | Newmark Grubb Knight Frank

Average Asking Rents and Vacancy Rates for North Los Angeles



Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for North Los Angeles

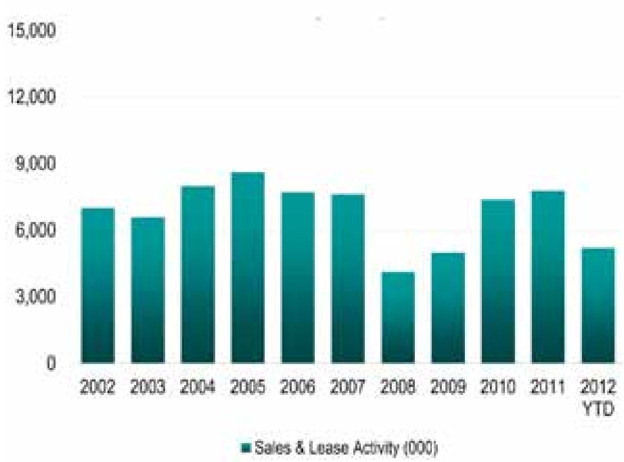


Source | Newmark Grubb Knight Frank

Average Asking Rents and Vacancy Rates for Mid-Cities

Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for Mid-Cities



Source | Newmark Grubb Knight Frank

No space was added to the North Los Angeles industrial stock between Q3 2011 and Q3 2012, and no new space is currently under construction.

Demand for industrial space in the North Los Angeles submarket has been aided over time by the fact that the buildings tend to be newer and provide more attractive amenities than in other parts of the county.

Mid-Cities

Mid-Cities, which is the smallest of the Los Angeles County industrial submarkets at 111 million square feet, witnessed a significant increase in demand from Q3 2011 to Q3 2012. The area logged almost 2 million square feet of positive net absorption, bringing the vacancy rate down 1.9 percentage points to 2.2 percent. As with North Los Angeles, the vacancy rate sits less than one percentage point from its Q2 2008 low. The increase in demand is somewhat surprising given the recent decline in activity at the Port of Long Beach and its relative proximity thereto.

Rents rose a healthy 9.8 percent to $0.49 per square foot. As of Q3 2012, rents stood about 22 percent below the Q3 2007 peak.

In Q4 2011, El Greco Development completed a 106,000 square foot warehouse and distribution facility near the intersection of Burke St. and Norwalk Boulevard in Whittier. Just under 330,000 square feet of warehouse and distribution space is currently under construction in the Santa Fe Springs area.

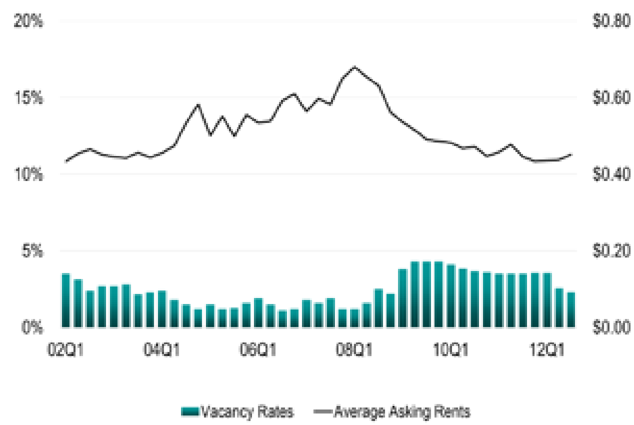
San Gabriel Valley

From Q3 2011 to Q3 2012, San Gabriel Valley experienced the largest absolute increase in demand among Los Angeles industrial submarkets. The area logged over 2.5 million square feet of positive net absorption, leading to a decline in the vacancy rate of 1.2 percentage points. As of Q3 2012, the vacancy rate stood at 2.2 percent, 1.1 percentage points from its pre-recession low.

Average asking rents remained stable at $0.45 per square foot, after experiencing an area-worst decline between Q3 2010 and Q3 2011. Rents have declined more than 34 percent from peak-to-trough, which is the largest decline among Los Angeles industrial submarkets.

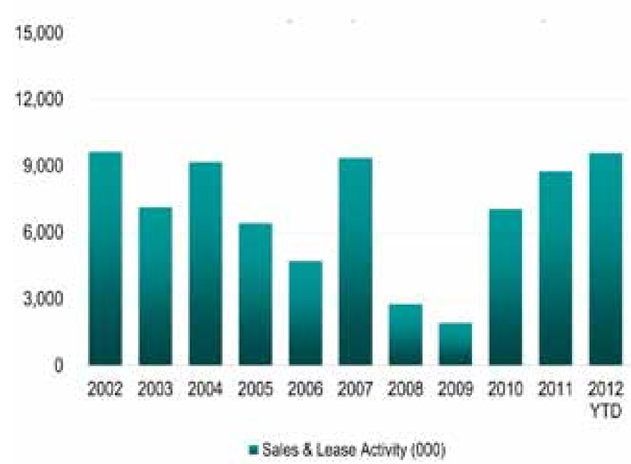
In January of 2012, Majestic Realty completed a 300,000 square foot warehouse and distribution facility on the 100 block of Grand Avenue in the City of Industry. No new space is currently under construction.

Average Asking Rents and Vacancy Rates for San Gabriel Valley



Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for San Gabriel Valley



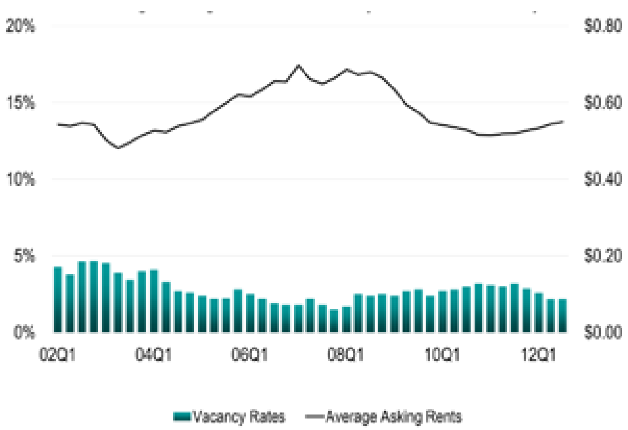
Source | Newmark Grubb Knight Frank

South Bay

The South Bay is the second largest submarket in the county with 219 million square feet of industrial space and enjoys its position as the home of the busiest port in the United States. With the post-recession drop in retail commerce and manufacturing, the industrial market as a whole has suffered. South Bay has been somewhat insulated from these effects due to its role in providing immediate warehousing space for the hundreds of thousands of shipping containers passing through the port each year. The future of this area may be in question with the opening of the Panama Canal in 2014 to the world's largest container ships, but for now, it remains one of the stronger submarkets of Los Angeles County and one of the tightest industrial markets in the nation.

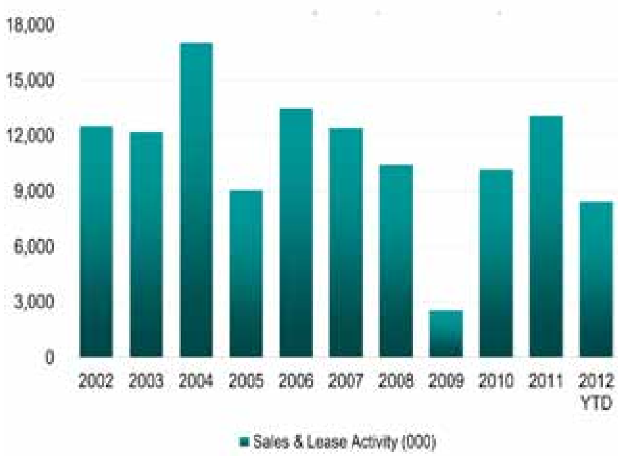
From Q3 2011 to Q3 2012, the area recorded just over 2.2 million square feet of net move-ins, a turnaround from the 346,000 square feet of net move-outs logged in the prior four quarters. Vacancy subsequently fell 1 percentage point

Average Asking Rents and Vacancy Rates for South Bay



Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for South Bay



Source | Newmark Grubb Knight Frank

to 2.2 percent. Rents rose 5.6 percent year-over-year to $0.55 per square foot, which is the second-highest level among submarkets.

Although the South Bay is the second most expensive industrial submarket in the county, continued volatility in energy prices and immediate access to the port may lead firms engaged in importing and exporting to prefer warehousing and distribution space in this submarket to the much cheaper but less accessible Inland Empire.

Between Q3 2011 and Q3 2012, the South Bay submarket received 680,000 square feet of new industrial stock. In October 2011, Millie & Severson completed the construction of a 135,000 square foot build-to-suit for Rubbercraft, which provides engineering and manufacturing solutions for the aerospace and marine sectors. The property is located within Douglas Park, a 260-acre master-planned, mixed-use development adjacent to the Long Beach Airport. In early 2012, Watson Land Company finished the construction of a 225,000 square foot warehouse in the Watson Corporate Center. Located in the City of Carson and adjacent to the 405 freeway, the Watson Corporate Center is a 113-acre master-planned business center featuring light manufacturing, warehousing, and distribution buildings. In Q3 2012, GLJ Holding completed a 48,000 square foot industrial building on the 1500 block of Francisco Street in Torrance. Finally, in September of 2012, ProLogis completed the 272,000 square foot Capelin Distribution Center on the 20000 block of Western Avenue in Torrance. The 14-acre site previously housed an obsolete steel plant which the company transformed into a Class A, LEED-certified logistics center.

Just over 700,000 square feet of new industrial space is under construction across three properties. The largest of these properties is a 438,000 square foot warehouse and distribution center in the Torrance area.

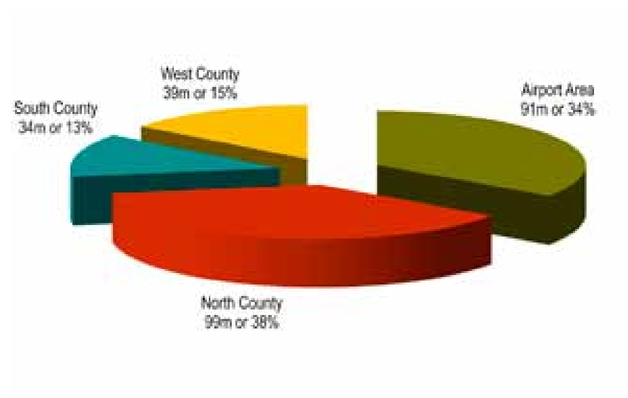
Orange County Industrial Market Trends

As with the Orange County office market, the Orange County industrial market experienced an increase in demand over the last four quarters, but not as large an increase as in the prior year. The County logged about 1.6 million square feet of net move-ins, down from 2.5 million. The vacancy rate subsequently fell half a percentage point to 4.8 percent.

At the end of Q3, owner-user purchases and overall leasing activity for 2012 stood at 15.7 million square feet. If the average pace of contracting holds steady through the end of the year, the 2012 total will exceed the 2011 amount by about 7.3 percent.

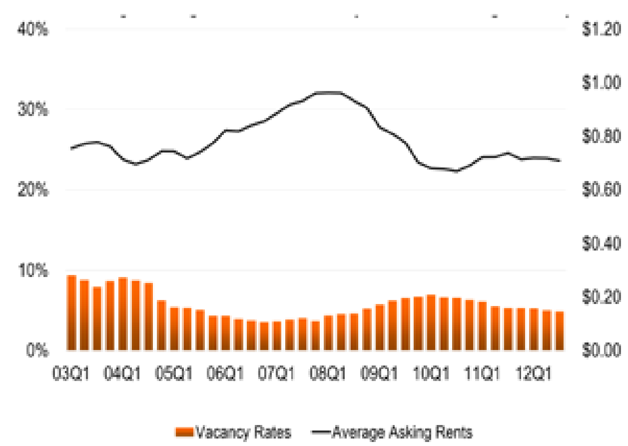
The North County area, once again, experienced the largest absolute increase in demand among submarkets, with positive net absorption of 980,000 square feet. The vacancy rate stood at 3.3 percent at the end of Q3 2012, down 0.7 percentage points from a year earlier. South County, which is the smallest of the Orange County industrial submarkets, experienced the largest relative increase in demand, logging 414,000 square feet of net move-ins. The vacancy rate, which remains the highest in the county, fell 0.9 percentage points to 7.2 percent. The West County submarket was the only submarket to experience a decline in demand over the last four quarters, recording 326,000 net move-outs. The vacancy rate for the area rose 0.9 percentage points to 5.2 percent.

Size of Industrial Submarkets in Orange County



Source | Newmark Grubb Knight Frank

Average Asking Rents and Vacancy Rates for Orange County



Source | Newmark Grubb Knight Frank

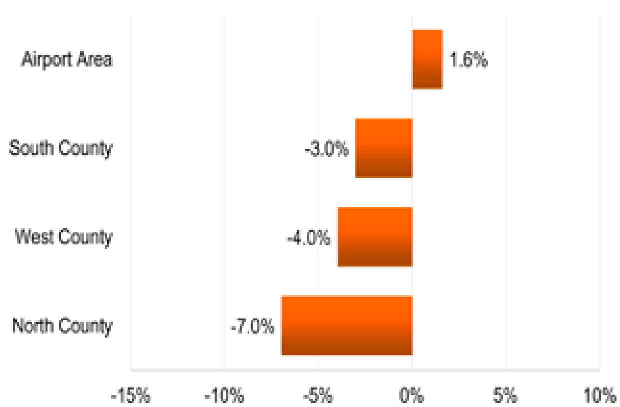
Sales & Lease Activity for Orange County

Source | Newmark Grubb Knight Frank

Industrial Vacancy Rates for OC Submarkets

Source | Newmark Grubb Knight Frank

2012 Year-over-year Average Rent Changes



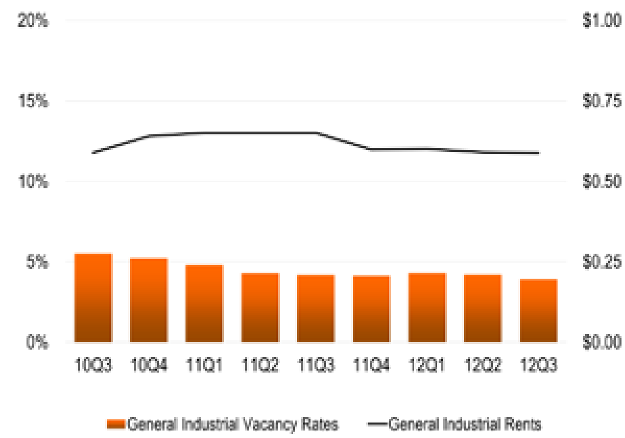
Source | Newmark Grubb Knight Frank

After rising 10.2 percent between Q3 2010 and Q3 2011, average asking rents in Orange County experienced a correction during the last four quarters: rents fell 4.3 percent to end Q3 2012 at $0.71 per square foot. Among the Southern California metro markets discussed in this report, Orange County was the worst performer in industrial rents by a wide margin, but it remains the most expensive by $0.18 per square foot.

The Airport submarket was the only submarket to experience an increase in asking rents, but its performance was way off the 14.9 percent increase recorded between Q3 2010 and Q3 2011. Rents rose 1.6 percent to end Q3 2012 at $0.86 per square foot. North County was the weakest performer, logging a 7.0 percent decline in average asking rents.

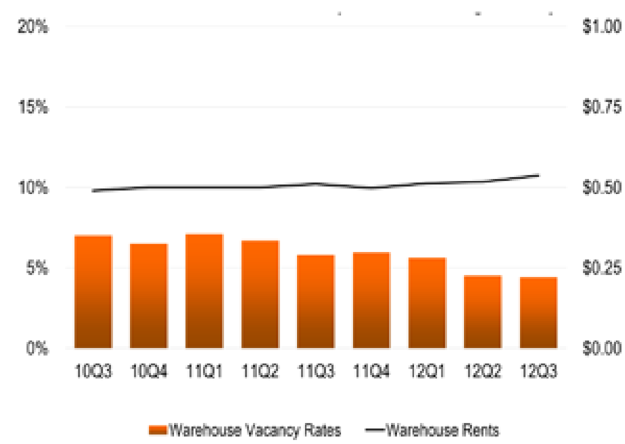
Warehouse properties saw a 5.3 percent increase in rents over the last four quarters, ending Q3 2012 at $0.54 per square foot. General Industrial properties, on the other hand, lost nearly all of the ground it gained from Q3 2010 to Q3 2011, logging a 9.4 percent decline in average asking rents. R&D/Flex properties, which make up about 30 percent of the total industrial stock, ended in-between, posting a 4.6 percent decline in average asking rents. The R&D/Flex category is the most expensive industrial sub-type in the county at $0.94 per square foot, and carries the highest vacancy rate at 6.6 percent.

General Industrial Rents and Vacancy Rates for Orange County



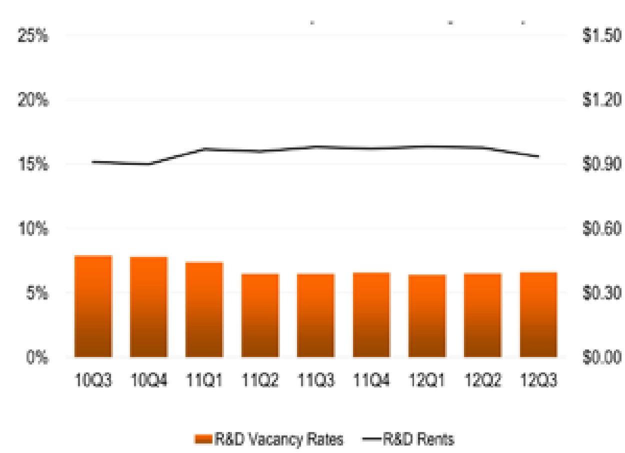
Source | Newmark Grubb Knight Frank

Warehouse Rents and Vacancy Rates for Orange County



Source | Newmark Grubb Knight Frank

R&D Rents and Vacancy Rates for Orange County



Source | Newmark Grubb Knight Frank

Dollar Value of Industrial Sales and Cap Rates

Source | Newmark Grubb Knight Frank

Construction and Investment Activity

For the second year in a row, no new industrial space came online. One hundred thirty-two thousand square feet are currently under construction, divided between the North County and South County submarkets. Year-to-date sales volume is off nearly two-thirds from the 2011 annual total and currently stands at $84 million. Not surprisingly, average going-in cap rates have risen from 5.8 to 7.3 percent.

Airport

The Airport area is the second largest industrial submarket in Orange County with 91 million square feet of space. The area recorded about 490,000 square feet of positive net absorption over the last four quarters. Although net move-ins were down about a third from the prior four quarters, vacancy declined for the third year in a row, falling 0.5 percentage points to 5.5 percent.

From Q3 2011 to Q3 2012, the Airport area was the only Orange County submarket to post a year-over-year rent increase, although the performance fell far short of the prior year's 14.9 percent rise. This year's increase of 1.6 percent brought average asking rents to $0.86 per square foot.

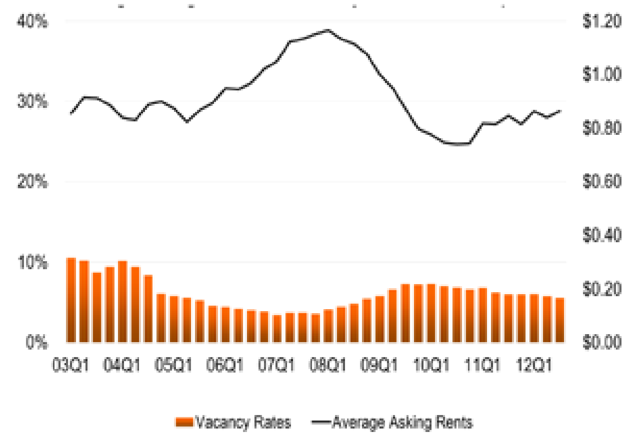
North

Over the last four quarters, demand for industrial space continued to improve; although, like the Airport area, net move-ins were down about 28 percent from a year earlier. The North submarket recorded 980,000 square feet of positive net absorption and a 0.7 percentage point decline in the vacancy rate. As of Q3 2012, the vacancy rate stood at 3.3 percent, which was the lowest level in the county.

On the rent side, all of the gains made from Q3 2010 to Q3 2011 were erased during the last four quarters. Average asking rents fell 7 percent to $0.53 per square foot. The North County area suffered the largest year-over-year rent decline and remains the least expensive submarket in Orange County. Average asking rents in North County are down almost 33 percent from their Q2 2008 peak.

No new space was completed between Q3 2011 and Q3 2012, but 84,350 square feet of warehouse and distribution space is currently under construction.

Average Asking Rents and Vacancy Rates for Orange County Airport Area

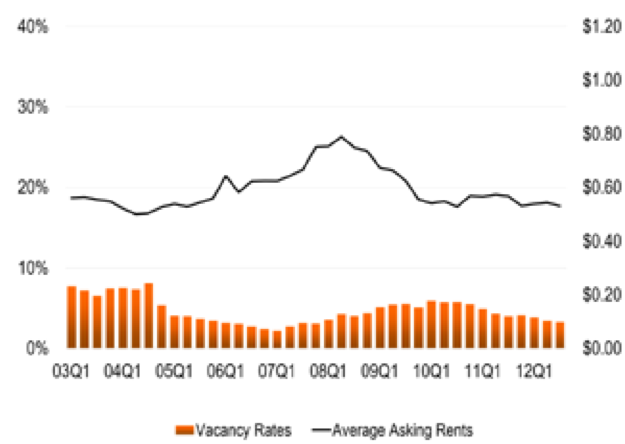


Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for Orange County Airport Area

Source | Newmark Grubb Knight Frank

Average Asking Rents and Vacancy Rates for North Orange County

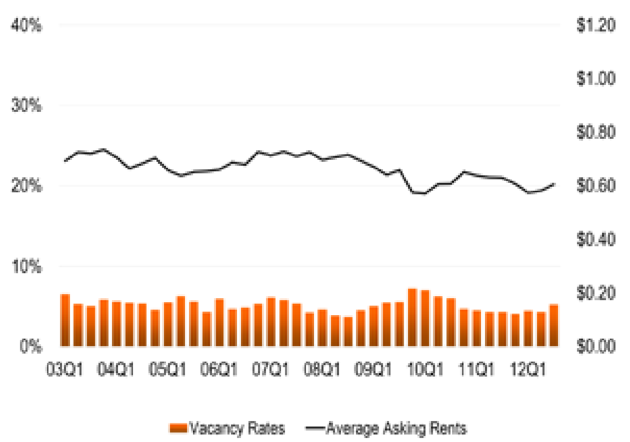


Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for North Orange County

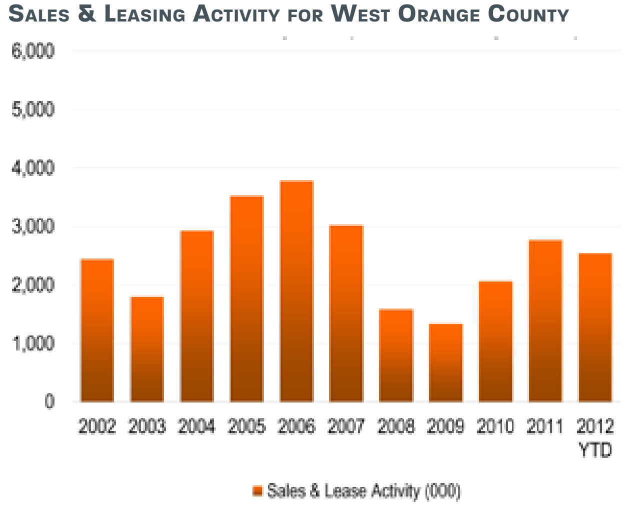
Source | Newmark Grubb Knight Frank

Average Asking Rents and Vacancy Rates for West Orange County



Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for West Orange County



Source | Newmark Grubb Knight Frank

West

The West County submarket was the only Orange County submarket to witness a drop in demand from Q3 2011 to Q3 2012. The 326,000 square feet of net move-outs all but erased the 345,000 square feet of positive net absorption recorded in the prior four quarters. The vacancy rate subsequently rose 0.9 percentage points to 5.2 percent.

At the same time, average asking rents fell 4 percent. Like North County, the West area erased all of the rent gains that occurred from Q3 2010 to Q3 2011. At the end of Q3 2012, average asking rents stood at $0.60 per square foot. In spite of this year's decline, the West area appears to have weathered the economic crisis slightly better than the other industrial submarkets of Orange County; average asking rents fell a total of 19.7 percent peak-to-trough and are currently off 16.6 percent from their peak in Q3 2008. The area's greater stability in rents and vacancy may be due to its relative proximity to the Ports of Los Angeles and Long Beach.

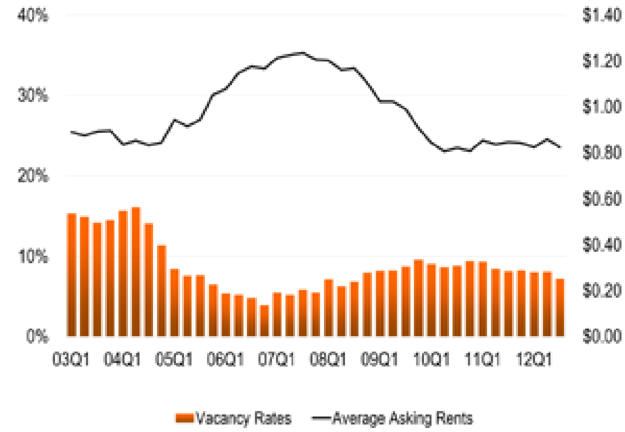
South

The South area, with 34 million square feet of space, is the smallest industrial submarket in Orange County. From Q3 2011 to Q3 2012, the area witnessed 414,000 square feet of net move-ins and saw vacancy subsequently fall 0.9 percentage points to 7.2 percent. The submarket has historically carried the highest vacancy rate in the county and continues to do so as of Q3 2012.

Average asking rents fell 3 percent to $0.82 per square foot. Like the North County submarket, average asking rents in the South County area are down almost 33 percent from their pre-crisis peak.

No new space was delivered during the last four quarters, but 48,000 square feet are currently under construction across two properties.

Average Asking Rents and Vacancy Rates for South Orange County

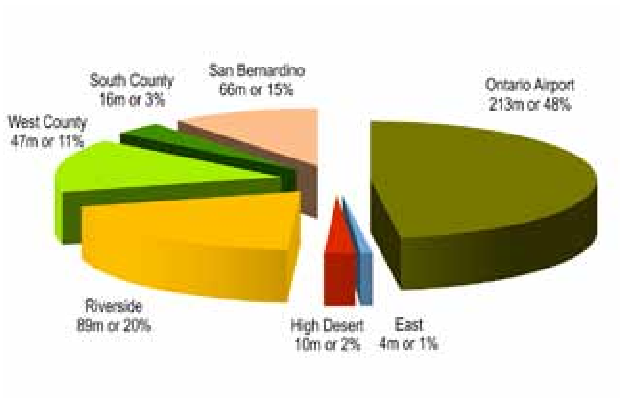


Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for South Orange County

Source | Newmark Grubb Knight Frank

Size of Industrial Submarkets in Inland Empire

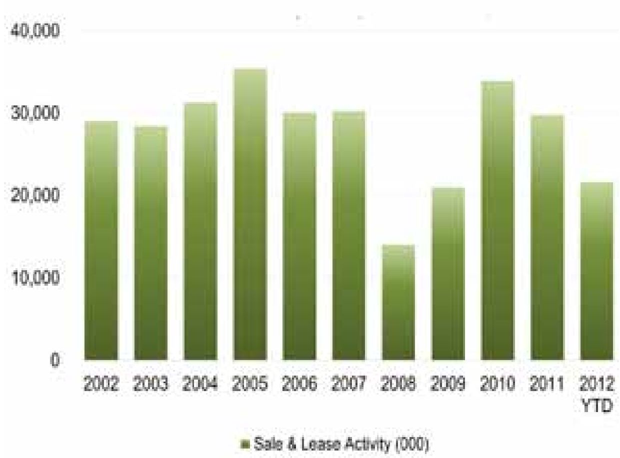


Source | Newmark Grubb Knight Frank

Average Asking Rents and Vacancy Rates for Inland Empire

Source | Newmark Grubb Knight Frank

Sales & Lease Activity for Inland Empire



Source | Newmark Grubb Knight Frank

Inland Empire Industrial Market Trends

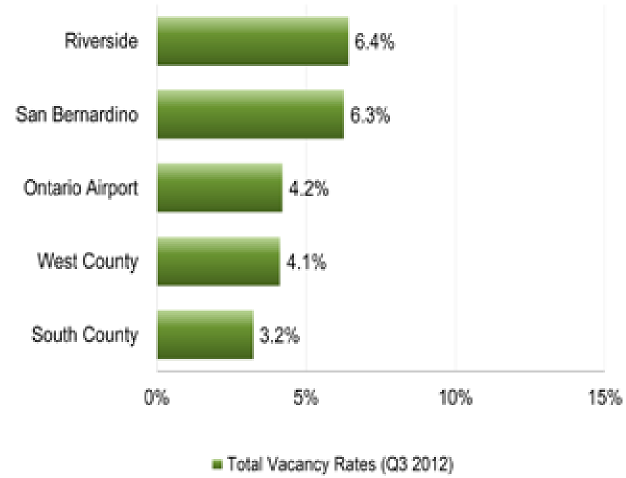
For the third year in a row, the Inland Empire industrial market showed significant improvement in demand. From Q3 2011 to Q3 2012, the area logged 9.4 million square feet of positive net absorption, bringing the total net absorption since Q1 2009 to nearly 40 million square feet. The vacancy rate subsequently fell another 1.7 percentage points to 4.9 percent. Year-to-date owner-user purchases and leasing activity stand at 21.6 million square feet. If the pace of transactions is maintained through Q4 2012, the annual total will fall just short of 2011 volume.

With the exception of West County, all Inland Empire submarkets experienced sharp declines in vacancy.

The Riverside submarket experienced the strongest absolute and relative increase in demand from Q3 2011 to Q3 2011, logging 3.5 million square feet of net move-ins and a decline in the vacancy rate of 2.1 percentage points. The vacancy rate stood at 6.4 percent as of Q3 2012, the highest among Inland Empire submarkets. San Bernardino recorded the second largest relative increase in demand, with 2.4 million square feet of net move-ins and a decline in vacancy of 2.4 percentage points. The vacancy rate in the submarket stood at 6.3 percent as of Q3 2012, down nearly 20 percentage points since Q3 2009.

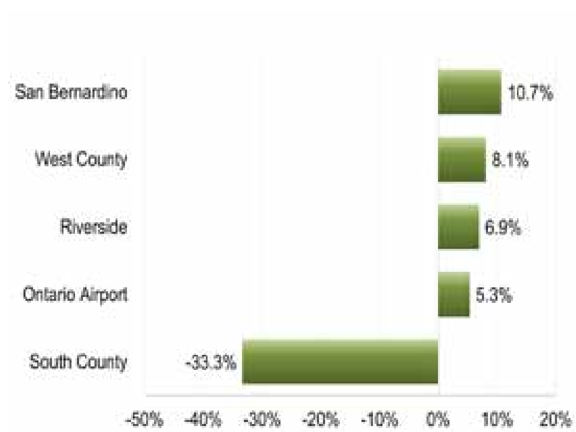
Area-wide average asking rents rose for the second year in a row, climbing 6.1 percent to $0.35 per square foot. These rents are largely driven by changes in demand for warehouse space, which accounts for 86 percent of the industrial stock. San Bernardino performed the best among submarkets, posting 10.7 percent gain in average asking rents. For the second year in a row, the South County submarket performed the weakest, with rents slipping a staggering 33.3 percent to $0.30 per square foot. In one year, the South County submarket went from being the most expensive to the least expensive submarket in the Inland Empire. The West County submarket now sits as the most expensive industrial submarket, with rents of $0.40 per square foot.

Industrial Vacancy Rates for IE Submarkets



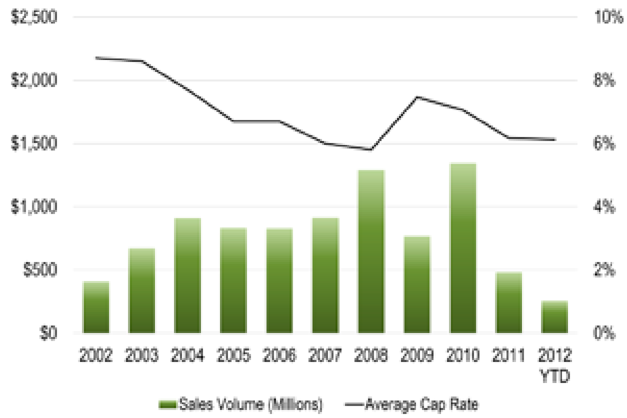
Source | Newmark Grubb Knight Frank

2012 Year-over-year Average Rent Changes



Source | Newmark Grubb Knight Frank

Dollar Value of Industrial Sales and Cap Rates



Source | Newmark Grubb Knight Frank

Construction and Investment Activity

As was the case from Q3 2010 to Q3 2011, the vast majority of industrial completions in Southern California occurred in the Inland Empire during the last four quarters. Another 1.7 million square feet of space was added to the area stock across four properties. The majority of the space came from three warehouse and distribution centers: a 414,000 square foot property in the Ontario submarket, a 692,000 square foot property in the Riverside submarket, and a 617,000 square foot property in the San Bernardino submarket. An additional 7.2 million square feet are currently under construction. Without question, when a developer needs to build big, they go to the Inland Empire to do so.

Year-to-date transaction volume sits at $319 million, which is down significantly from previous years. Even if the average pace of transactions is maintained through the end of 2012, annual totals will fall short of 2011 numbers by about 12 percent and will fall short of 2010 totals by 68 percent. Average going-in cap rates held steady at 6.2 percent

Airport

With 213 million square feet of space totaling 48.9 percent of the total market, the Ontario Airport area is the largest industrial submarket in the Inland Empire. Demand increased for the third year in a row, resulting in 3.2 million square feet of positive net absorption and a decline in the vacancy rate of 1.5 percentage points. Rents rose 5.3 percent from Q3 2011 to Q3 2012, just surpassing the 5.2 percent increase that occurred in the prior four quarters. Average asking rents ended Q3 2012 at $0.36 per square foot.

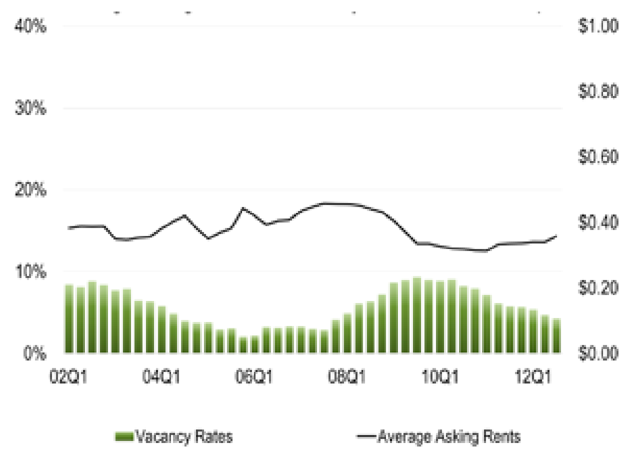
Three new properties were added to the Ontario Airport market between Q3 2011 and Q3 2012: a pair of 8,000 square foot general industrial buildings and a 414,000 square foot distribution facility. In April of 2012, ProLogis finished construction on the Terra Francesco Distribution Center on the 1800 block of Carlos Avenue in Ontario. The single-tenant property is LEED Certified Silver. Almost 1.7 million square feet of new industrial space is currently under construction.

Riverside

At almost 88.5 million square feet of industrial space, the Riverside area is the second largest submarket in the Inland Empire. Like the Airport submarket, demand is up for the third year in a row. The area recorded 3.5 million square feet of net move-ins, bringing the two-year total to almost 10 million square feet of positive net absorption. At the end of Q3 2012, the vacancy rate stood at 6.4 percent -- the highest level among Inland Empire submarkets. This represented a 2.1 percentage-point decline from a year earlier.

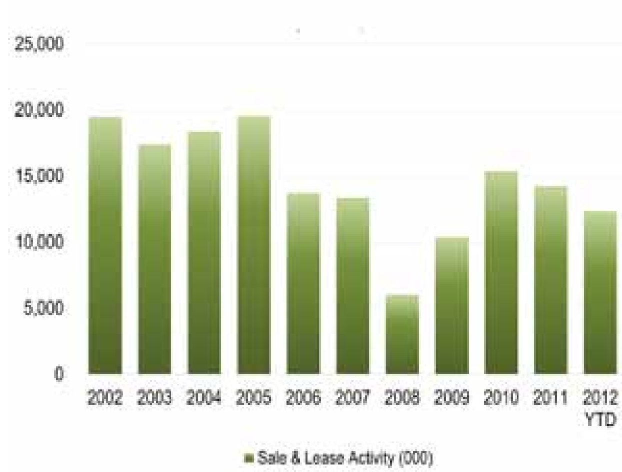
Asking rents rose 6.9 percent to $0.34 per square foot.

Average Asking Rents and Vacancy Rates for Ontario Airport



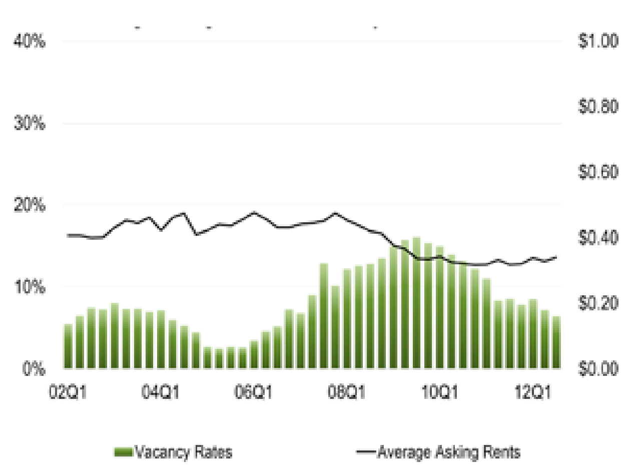
Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for Ontario Airport



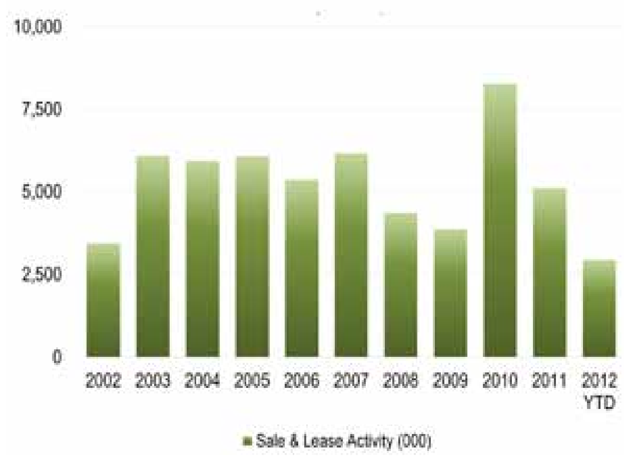
Source | Newmark Grubb Knight Frank

Average Asking Rents and Vacancy Rates for Riverside



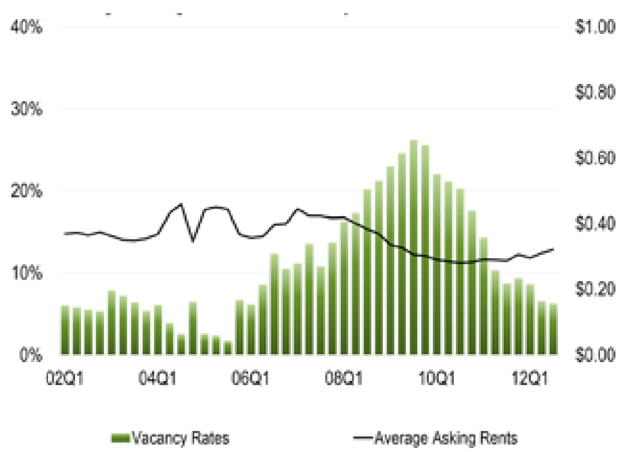
Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for Riverside



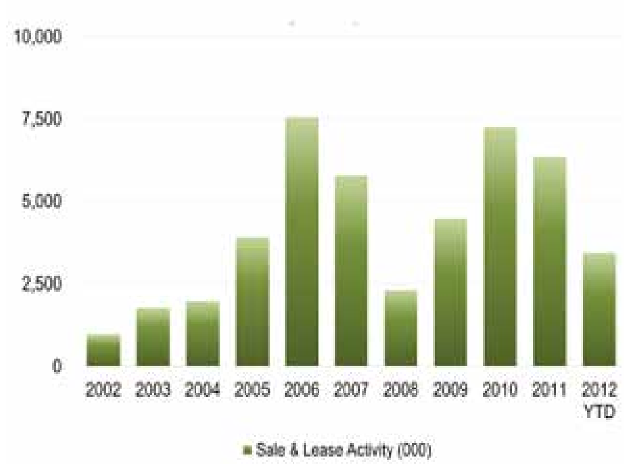
Source | Newmark Grubb Knight Frank

Average Asking Rents and Vacancy Rates for San Bernardino



Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for San Bernardino



Source | Newmark Grubb Knight Frank

One new industrial building of 692,000 square feet was added to the existing stock in the Riverside submarket between Q3 2011 and Q3 2012. In January 2012, First Industrial Realty Trust finished construction on the San Michele Logistics Center on the 24000 block of Nandina Avenue in Moreno Valley. This property represents the first speculative industrial development in Moreno Valley since 2009. Another 5 million square feet of industrial space is currently under construction.

San Bernardino

The submarket of San Bernardino suffered the most as a result of the economic downturn, but has since roared back the strongest. After witnessing an increase in the vacancy rate from 1.7 percent to 26.2 percent between Q3 2005 and Q3 2009, the submarket reached a vacancy rate of 6.3 percent as of Q3 2012, down 2.4 percentage points from a year earlier. The decline in vacancy came as a result of 2.4 million square feet of net move-ins.

From Q3 2011 to Q3 2012, the San Bernardino area logged the largest year-over-year rent increase among Inland Empire submarkets. As of Q3 2012, average asking rents stood at $0.32 per square foot, up 10.7 percent from a year earlier. San Bernardino is the second-most-affordable submarket in the region, down 27.7 percent from its pre-crisis peak.

In October 2011, Watson Land Company completed construction on a 616,000 square-foot single-tenant warehouse and distribution facility on the 26000 block of Pioneer Avenue in Redlands. The building is part of the Watson Commerce Center, a 100-acre master-planned development containing 2.1 million square feet of industrial space. All four buildings in the Watson Commerce Center are LEED Certified. No new space is currently under construction.

South County

The South (Riverside) County area, at 15.9 million square feet, is the smallest industrial submarket included in this report by a significant margin. Although demand was positive, the area saw a decline in rents for the second straight year. The submarket logged 293,000 square feet of positive net absorption, which led to a decline in the vacancy rate of 1.7 percentage points. At 3.2 percent, the South County area carries the smallest vacancy rate among Inland Empire submarkets.

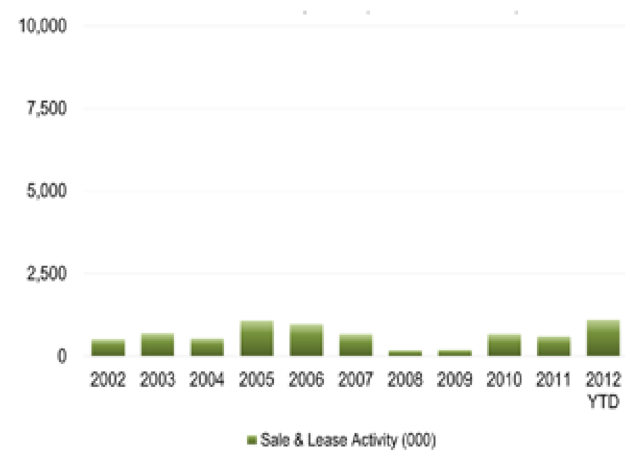
From Q3 2011 to Q3 2012, average asking rents fell a staggering 33.3 percent to $0.30 per square foot. This decline moved the South County submarket from the position of least-affordable to most-affordable in the Inland Empire.

No new industrial space was completed in the South County area over the last year, and no new space is currently under construction.

Average Asking Rents and Vacancy Rates for South County

Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for South County

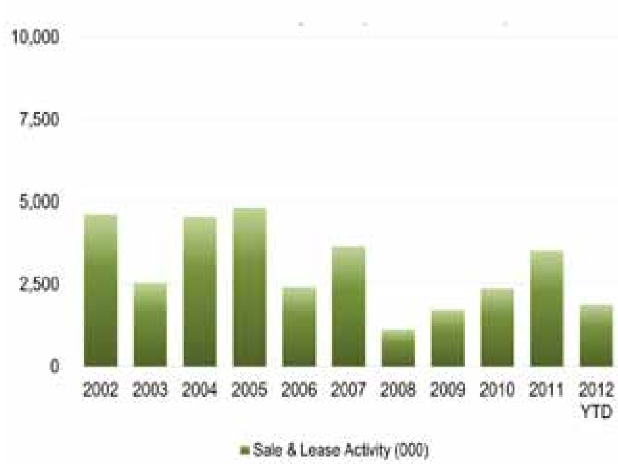


Source | Newmark Grubb Knight Frank

Average Asking Rents and Vacancy Rates for West

Source | Newmark Grubb Knight Frank

Sales & Leasing Activity for West



Source | Newmark Grubb Knight Frank

West

After witnessing a strong increase in demand from Q3 2010 to Q3 2011, the area experienced a reversal in performance during the last four quarters. The area logged 30,500 square feet of net move-outs, which led to a 0.7 percentage-point increase in the vacancy rate. The increase in the vacancy rate to 4.1 percent moves the West submarket from the position of tightest submarket in the Inland Empire to the middle of the pack.

Asking rents rose 8.1 percent to $0.40 per square foot, making the West County submarket the most expensive in the Inland Empire.

The West area, at 47.3 million square feet, represents about 11 percent of the total Inland Empire industrial market. No new space was added in the last year, but 527,000 square feet of new warehouse and distribution space is currently under construction.

Office Market Forecast

For the fourth straight year, Southern California office markets have experienced negative rent growth, although the speed of decline has slowed. Rents could begin to stabilize in as little as 6 months, but sustained growth may be a long way off. Demand continued to improve in most submarkets over the last year, but vacancy rates are still so far above "natural" levels that they may continue to fall for many months to come without any accompanying growth in rents.

The vacancy rate appears to have peaked in all three metro markets for both Class A and Class B properties. In Los Angeles County the vacancy rate has bounced around between 16.4 percent and 17.4 percent over the last 11 quarters and is expected to remain near the upper end of that range for the next two years. In Orange County and the Inland Empire, vacancy rates are expected to continue a steady decline across both classes of properties. Important to note is that Orange County and the Inland Empire suffered far worse levels of vacancy over the last three years than during the previous market bust, whereas Los Angeles did not. In Orange County, the differences between the peak levels of vacancy across the two busts were 5.4 percentage points for Class A and 5.9 percentage points for Class B. The Inland Empire fared even worse: the peak vacancies were 12.6 percentage points and 8.9 percentage points higher in the recent bust for Class A and Class B properties, respectively. In short, it's hard to imagine things in Orange County and the Inland Empire getting any worse.

2000-2004 Peak Office Vacancy

	Orange County	Inland Empire	Los Angeles
Class A	19.7%	16.4%	16.2%
Class B	13.3%	16.2%	17.4%

2008-2012 Peak Office Vacancy

	Orange County	Inland Empire	Los Angeles
Class A	25.1%	29.0%	17.4%
Class B	19.2%	25.1%	17.3%

Overall, the future health of the office market will be dependent on several factors:

The employment picture. Office space is made to be filled with workers. The fewer the number of workers that are needed in office-based industries, the more the office market will suffer. Over the last year, employment has continued to grow slowly in all three metro markets, with the highest levels of job creation coming in office-focused industries such as professional and business services and financial activities. If this trend continues, we should expect to see further improvement in vacancy and possible improvement in rents.

Construction (or lack thereof). Over the last eight quarters, only two office buildings of more than 20,000 square feet have been added to the Southern California office stock: one 102,000 square foot property in the Los Angeles metro area and one 141,000 square foot property in the Inland Empire. The lack of new construction will undoubtedly help stabilize the office market. Hopefully this trend will continue and development-minded individuals will focus on renovations and "green" retrofits of existing buildings rather than ground-up construction.

Changes in corporate use of office space. In order to cut losses in these difficult times, companies have become more efficient in their use of office space. Although many changes in the use of office space began prior to the crisis, the concern for cutting costs in the post-crisis world has led to greater adoption of space-saving ideas and technologies. Open floor-plans filled with cubicles have replaced the structurally partitioned offices of the past; temporary, hotel-based workspaces for executive road-warriors have replaced permanent, dedicated office space; and telecommuting from a home-based office has become increasingly commonplace. Widespread digitization of documents has largely eliminated the need for filing cabinets; flat screen monitors, laptops, and networked printers have reduced the desk space needed for job productivity; and inexpensive video-conferencing tools have reduced the need for centralized workspaces and face-to-face meetings. With less office space required per worker, greater job creation than what has been lost over the last three years will be required to bring the office market back to health.

"Green" considerations. In recent years, there has been increased interest among tenants in making their companies more "green" – for instance, leasing office space in LEED Certified buildings or locating in transit-oriented districts which allow employees to commute to work easily by rail, bus, or bicycle. Although LEED certification may not automatically lead to higher rents, in buildings with triple-net leases, greater energy efficiency will be passed on to the tenant in the form of lower expenses, which will make the LEED-certified building more attractive to tenants with a choice of whether to go "green" or not. As a result in coming years, the better-performing submarkets of Southern California are likely to be the ones that conform to this desire for "greenification". Submarkets with a higher share of LEED-certified buildings (or buildings that can be inexpensively retrofitted) and submarkets with more green transportation options may recover sooner than ones with higher shares of older, energy-inefficient buildings in more automobile-dominated locations.

In summary, the interplay of these four factors will help guide the future path of rents and vacancy in the office market. Southern California will not see increases in rents until the greater economic health of the area improves and some of the slackness in the market disappears. Currently, the three markets covered in this report remain approximately 4 to 11 percentage points above the vacancy rate at which rents will begin to rise.

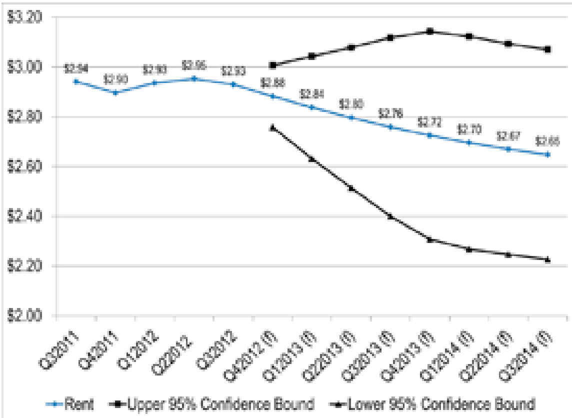
On the Class A front, Orange County is expected to fare the best, followed by the Inland Empire. Both metro areas are expected to see modest rent increases over the next two years. Los Angeles, on the other hand, is expected to see a further rent decline. Among Class B properties, only Orange County is expected to see a rent increase over the next two years. Los Angeles is expected to see a further rent decline, but smaller than what has been predicted for the Class A market.

On the vacancy side, both Orange County and the Inland Empire are expected to see a decline in the vacancy rate. Our models predict a similar performance on the Class A side, and a stronger performance from Orange County on the Class B side. The vacancy rate is expected to remain virtually unchanged in Los Angeles County over the next two years.

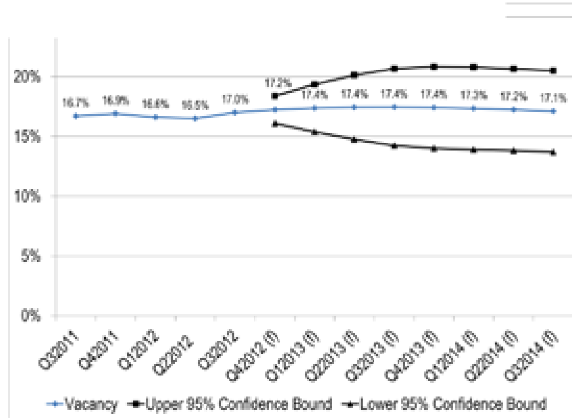
A Note on Confidence Intervals

This year, for the second time, the Casden Forecast is reporting 95 percent confidence intervals on our forecast estimates. These intervals, depicted in the forecast graphs by black lines, represent the upper and lower bounds between which the "true" rent or vacancy rate is likely to fall with 95 percent probability. As the reader will observe, the confidence intervals are relatively narrow for Q4 2012 and Q1 2013 and get wider as we move further into the future. In other words, accurately predicting the next quarter or two of rent is relatively easy; predicting beyond that with much precision is difficult. So even though we can rank the three metro areas in terms of the trends in the actual forecast estimates, the true realization may paint a very different picture.

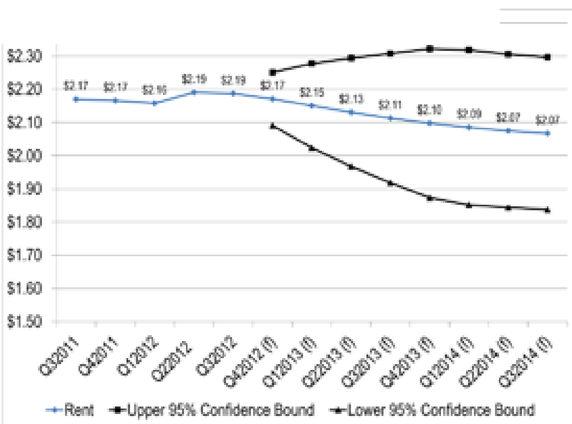
Los Angeles Class A Rent Forecast



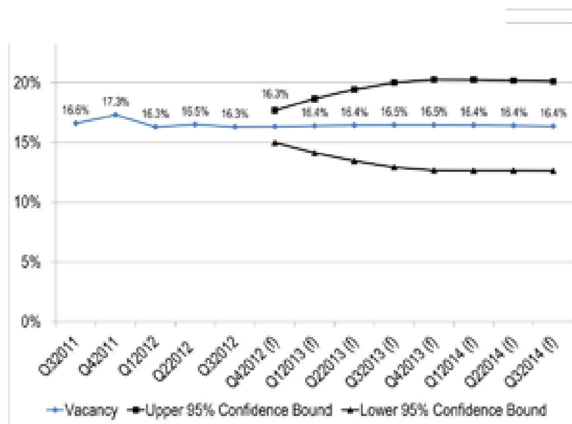
Los Angeles Class A Vacancy Forecast



Los Angeles Class B Rent Forecast



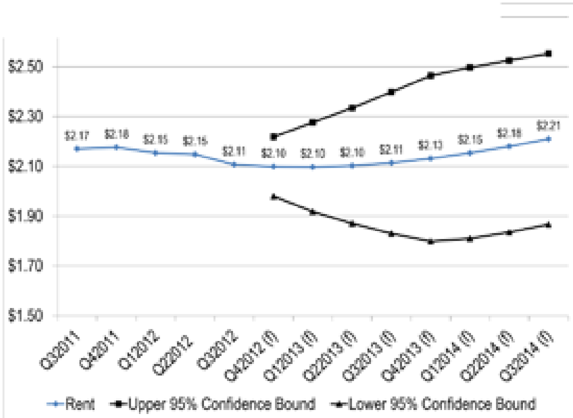
Los Angeles Class B Vacancy Forecast



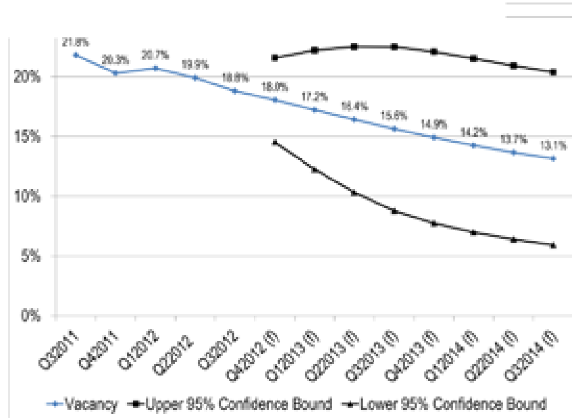
Los Angeles Forecast

Similar to the forecast of the last two years, we expect vacancy rates in Los Angeles County to remain stable across both property classes, while rents continue to decrease. Class A rents are expected to decline an additional 5.8 percent over the next four quarters and 9.6 percent total over the next two years. Class B rents are expected to decline 3.4 percent over the next four quarters and 5.5 percent total over the next two years.

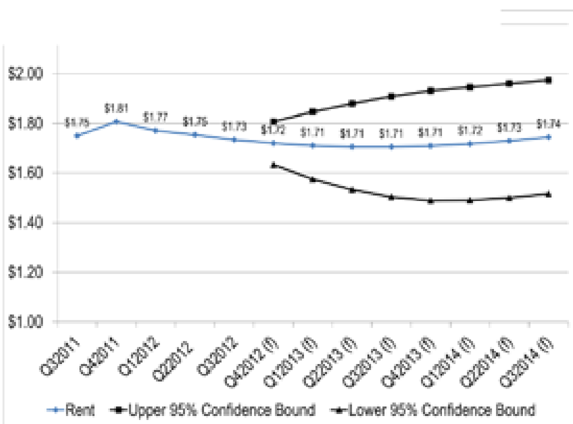
Orange County Class A Rent Forecast



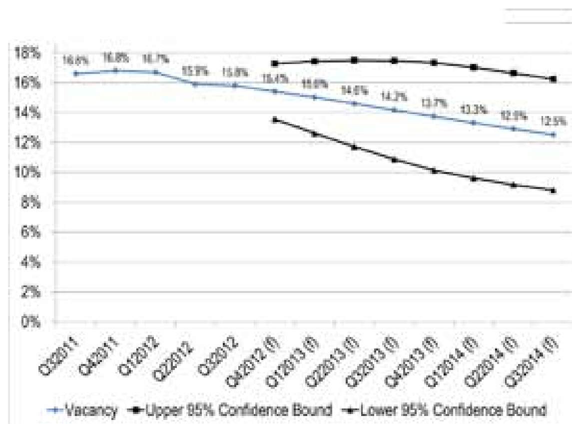
Orange County Class A Vacancy Forecast



Orange County Class B Rent Forecast



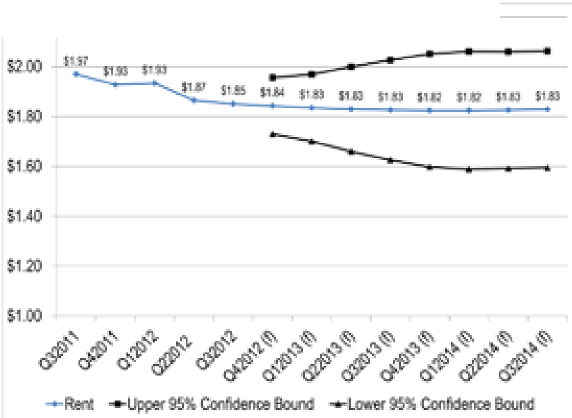
Orange County Class B Vacancy Forecast



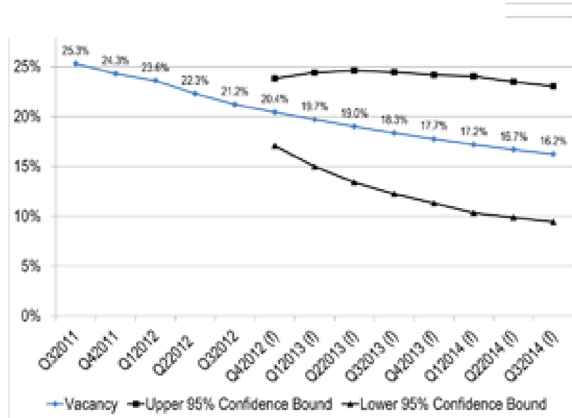
Orange County Forecast

Our model predicts a significant decline in vacancy over the next two years and modestly rising rents through the end of 2013. Class A rents are expected to rise 0.3 percent over the next four quarters and 4.8 percent total over the next two years. Class B rents are expected to decline 1.7 percent over the next four quarters but end Q3 2014 up a total of 0.6 percent. The vacancy rate in Class A properties, which currently sits at 18.8 percent, is expected to decline 3.2 percentage points over the next four quarters and 5.6 percentage points over the next two years. The vacancy rate in Class B properties is expected to decline 1.6 percentage points over the next four quarters and 3.3 percentage points over the next two years from its current level of 15.8 percent.

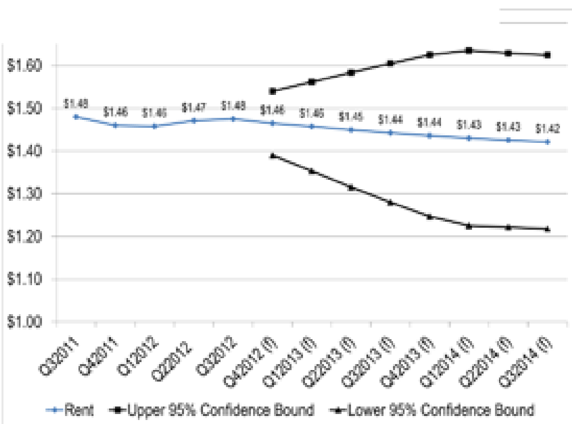
Inland Empire Class A Rent Forecast



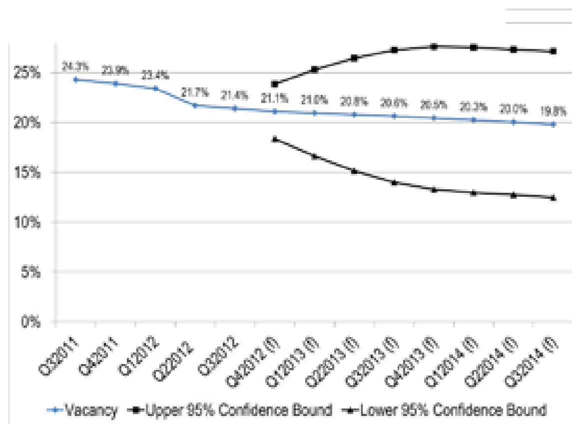
Inland Empire Class A Vacancy Forecast



Inland Empire Class B Rent Forecast



Inland Empire Class B Vacancy Forecast



Inland Empire Forecast

We anticipate modest decreases in both Class A and Class B rents over the next two years. Class B properties, which make up the majority of the office stock, are expected to see a decline in rents of 2.2 percent over the next four quarters and a total decline of 3.6 percent over the next two years. The vacancy rate is expected to fall 1.6 percentage points over the next two years from its current level of 21.4 percent. Class A properties, which make up 35 percent of the office stock in the region, are expected to see a 1.3 percent decrease over the next four quarters and then hold steady through Q3 2014. The vacancy rate is expected to decline 2.9 percentage points over the next four quarters and a total of 5 percentage points over the next two years from its current level of 21.2 percent.

Industrial Market Forecast

The period Q3 2010 to Q3 2011 was one of great turnaround for the Southern California industrial market. Over the last four quarters, the momentum continued in Los Angeles and the Inland Empire, but petered out somewhat in Orange County. All three metro areas witnessed positive net absorption of industrial space, but the net move-ins were not as high as in the previous four quarters. And while Los Angeles and the Inland Empire continued to see strong rent growth, Orange County saw average asking rents slide more than 4 percent. Our models predict that the Orange County performance was a temporary hiccup and that all three metro areas will experience double-digit rent growth over the next two years. Vacancy rates are expected to remain stable or decline in all three metro markets as well.

The future path of rents and vacancy in the industrial sector will be largely determined by the following five factors:

Trade activity. Los Angeles is the second largest industrial market in the nation and one of the tightest due to its position as the home of the nation's largest port. Industrial space in the vicinity of the port is used as temporary storage for both inbound and outbound containers. As port traffic changes, so will demand for industrial space. Areas in close proximity to the port will likely be more sensitive to changes in port activity than those further off the main arteries from the port area, all else equal. For the third year in a row, traffic at the Port of Los Angeles has increased; total container traffic is up 2.4 percent October to October and up 4.7 percent year-to-date relative to 2011. Traffic at the Port of Long Beach is up year-over-year as well, but the port is still recovering from last year's 20 percent decline due to the departure of California United Terminals. Year-to-date totals are down 3.2 percent from 2011.

Another concern for the Ports of Los Angeles and Long Beach (and nearby industrial property) is the completion of the Panama Canal expansion project, which is slated for 2014. The project will ultimately double the canal's traffic capacity and allow for longer and wider ships to pass through. Ships from Asia will be able to reach the east coast of the US more cheaply, but the trip will take about five days longer than it would if it unloaded in Los Angeles and the cargo were shipped to the east coast by truck or rail. There is no doubt that some traffic bound for Los Angeles/Long Beach will be lost, but how much remains to be seen. Despite the reduction in shipping costs from using the Panama Canal, many U.S. firms refuse to use it due to security considerations, so the impact of the expansion could end up being minimal.

Manufacturing output. With the post-crisis rise in unemployment and the de-leveraging of the American household, demand for consumer goods declined, and along with it, manufacturing activity. This led to a decline in general industrial space used for manufacturing processes as well as warehousing space used to store raw materials as well as finished products. As employment levels have increased and consumer spending has picked up (perhaps due to lower interest rates and, in turn, lower debt service-to-income ratios), demand for industrial space has increased and rents have risen once again. For the nation as a whole, manufacturing output is up 1.6 percent year-over-year. Given that Los Angeles is the largest manufacturing center in the United States, this statistic bodes well for the performance of the industrial real estate market going forward.

Gasoline prices. If the cost of trucking goods to and from the port area drops, firms engaged in importing and exporting may prefer warehousing and distribution space in the cheaper Inland Empire to the more expensive (but more accessible) Los Angeles County. Particularly high or volatile gasoline prices will favor the areas closest to the port in Los Angeles and Orange Counties.

Speculative Development. With land so plentiful and entitling so easy, the Inland Empire has long attracted developers with an "If you build it, they will come" mentality. Over-exuberance of developers could derail a recovery if too many projects begin construction before a sustained pattern of rent increases has been established. Until recently, developers appear to have exercised restraint in pursuing speculative development, and total absorption has far exceeded the amount of new space being brought to market. But 7 million square feet of space are currently under construction, and only one 420,000 square foot project was committed to a particular tenant as of Q3 2012.

Land Scarcity (or lack thereof). Rents will tend to be lower and rise slower in the Inland Empire relative to the other metro markets because of the abundance of land and a higher share of larger tenants. But the area's downfall is also its advantage. When a firm needs a 750,000 square foot or larger facility, the Inland Empire is the go-to location. (A 750,000 square foot building has a footprint of 17.2 acres and would require several additional acres of circulation and setback space) So as firms attempt to lower operating costs by consolidating multiple warehouse and distribution centers into fewer larger ones, we ought to see lower vacancy and higher rents in areas, like the Inland Empire, that can easily accommodate the largest corporate operations.

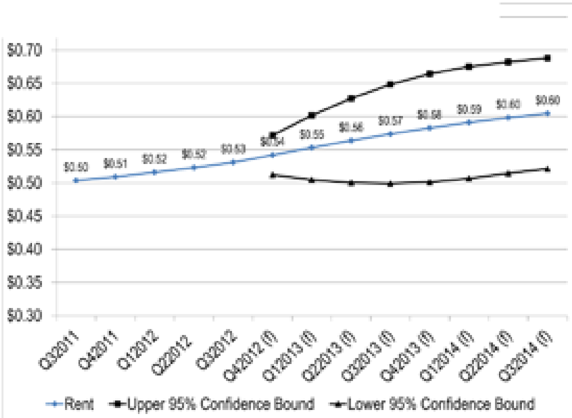
Submarket Forecasts

For the second time in its history, the Casden Forecast is including rent and vacancy forecasts for individual industrial submarkets. Relative submarket performance is most likely to be influenced by:

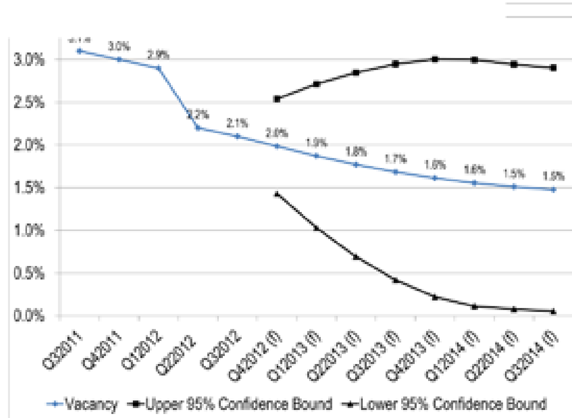
- Relative proximity to the Ports of Los Angeles and Long Beach and transportation corridors
- Relative changes in supply as a percentage of total submarket supply, due to completion of new construction.

Expected best- and worst-performing submarkets in rents and vacancies are listed in the appropriate metro-level sections below.

Los Angeles Industrial Rent Forecast



Los Angeles Industrial Vacancy Forecast



Los Angeles County

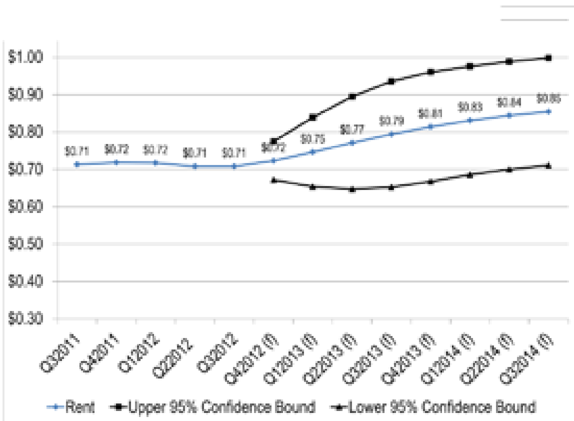
We expect rents to increase 8 percent over the next four quarters and 13.8 percent total over the next two years to around $0.60 per square foot. The vacancy rate is expected to decrease by 0.6 percentage points over the next two years to reach a level of 1.5 percent. Because the market is so tight, small changes in vacancy will have an immediate impact on rents. If trade activity and manufacturing output continue to grow, we could easily witness the predicted rent gains, but new additions to the industrial stock could slow the momentum. Currently, more than 1.1 million square feet of new industrial space is under construction in the Central, Mid-Cities, and South Bay submarkets.

Submarket Notes:

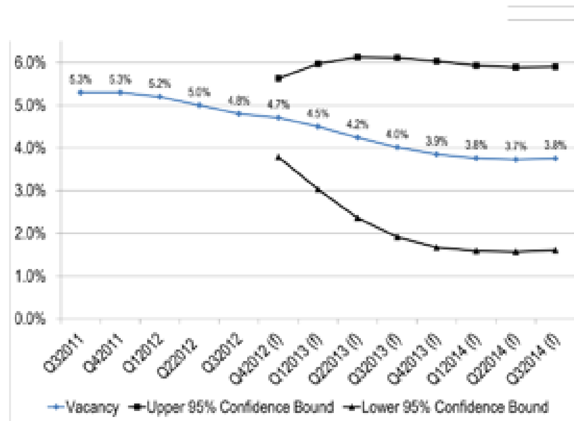
Our models predict gains in rents and stable or slightly declining vacancy in all five submarkets. The San Gabriel Valley is predicted to see the largest rent growth over the next two years, with an increase of 12.1 percent over the next four quarters and up to 20 percent total over the next two years. The Central Los Angeles submarket is predicted to see the smallest rise in rents, with growth of 2.1 percent over the next four quarters and 3.3 percent total over the next two years.

On the demand side, the San Gabriel Valley is also expected to post the largest decline in vacancy – about 0.6 percentage points over the next two years. As of late, the San Gabriel Valley has been benefitting from a higher-than-average number of larger transactions, and our predictions are taking this trend heavily into account. (The most recent rent and vacancy data weigh the most heavily in our econometric models). A return to more typical patterns of demand will temper some of the rent and occupancy growth. In general, given the overall tightness of the Los Angeles industrial market, there isn't much room for downward movement in vacancy and very small changes in vacancy can lead to considerable changes in rents.

Orange County Industrial Rent Forecast



Orange County Industrial Vacancy Forecast



Orange County

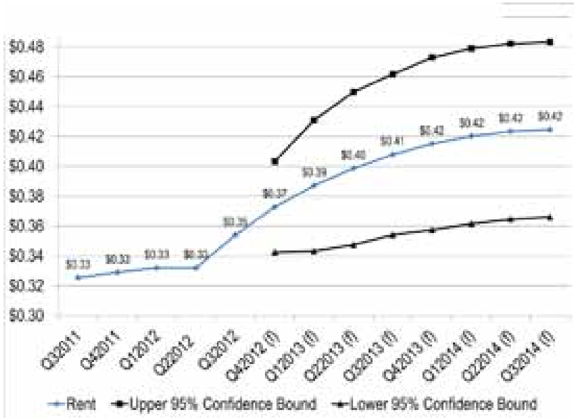
Our model predicts rents to increase 12.1 percent during the next year and 20 percent total over the next two years to reach $0.85 per square foot. The vacancy rate is predicted to fall from 4.8 to 3.8 percent. Although increased trade activity will most directly benefit the Los Angeles industrial market, the West County submarket of Orange County is less than ten miles away from the Port of Long Beach and could provide a boost to the overall Orange County industrial market if the increase in trade activity continues. An additional boost could come from increased demand for R&D/Flex space, which rents for much higher rates than warehouse or manufacturing space and represents a much larger fraction of the industrial market in Orange County (30 percent) than in Los Angeles or the Inland Empire (5 and 3 percent, respectively). As Southern California has progressed through the early stages of economic recovery, we have witnessed particular growth in sectors such as professional and business services, various subsets of which make significant use of R&D/Flex space. If this trend continues, the industrial market of Orange County could receive an extra boost in rents and occupancy. New deliveries are expected to remain low in the coming year; only 132,300 square feet of space are currently under construction.

Submarket Notes:

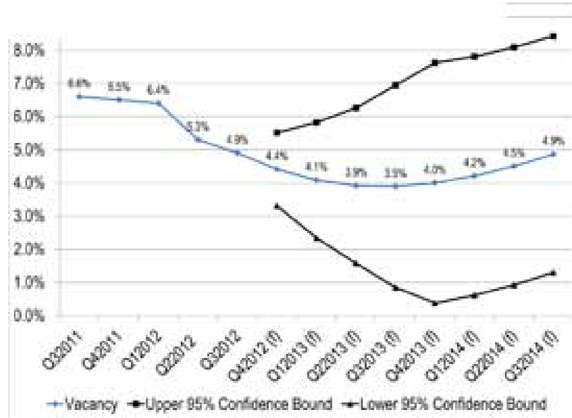
Our models predict rising rents and stable or declining vacancy in all four submarkets. We expect the North submarket to log the greatest rent growth, with rents increasing 15.4 percent over the next four quarters and 24.1 percent total over the next two years. The West submarket is expected to experience the weakest performance, with rent growth of 2.2 percent over the next four quarters and 5.6 percent total over the next two years.

The South area is expected to witness the largest decline in vacancy; our models predict a drop of 0.8 percentage points over the next four quarters and 1.3 percentage points total over the next two years. Our models predict the vacancy rate to remain virtually unchanged in the West County submarket. The West County area, which is the closest submarket to the Port of Long Beach, is most likely to feel a continuing impact of California United Terminals' departure from the port.

Inland Empire Industrial Rent Forecast



Inland Empire Industrial Vacancy Forecast



Inland Empire

The Inland Empire is expected to experience a 15.2 percent increase in rents during the next four quarters and a 20 percent total increase in rents over the next two years to reach $0.42 per square foot. Our model predicts the vacancy rate to decline 1 percentage point over the next year and remain stable for the subsequent four quarters. These rent and vacancy levels were last seen around the beginning of 2007, and will likely be tempered by the addition of new space: 7.2 million square feet are currently under construction, including 5 million in the Riverside submarket alone.

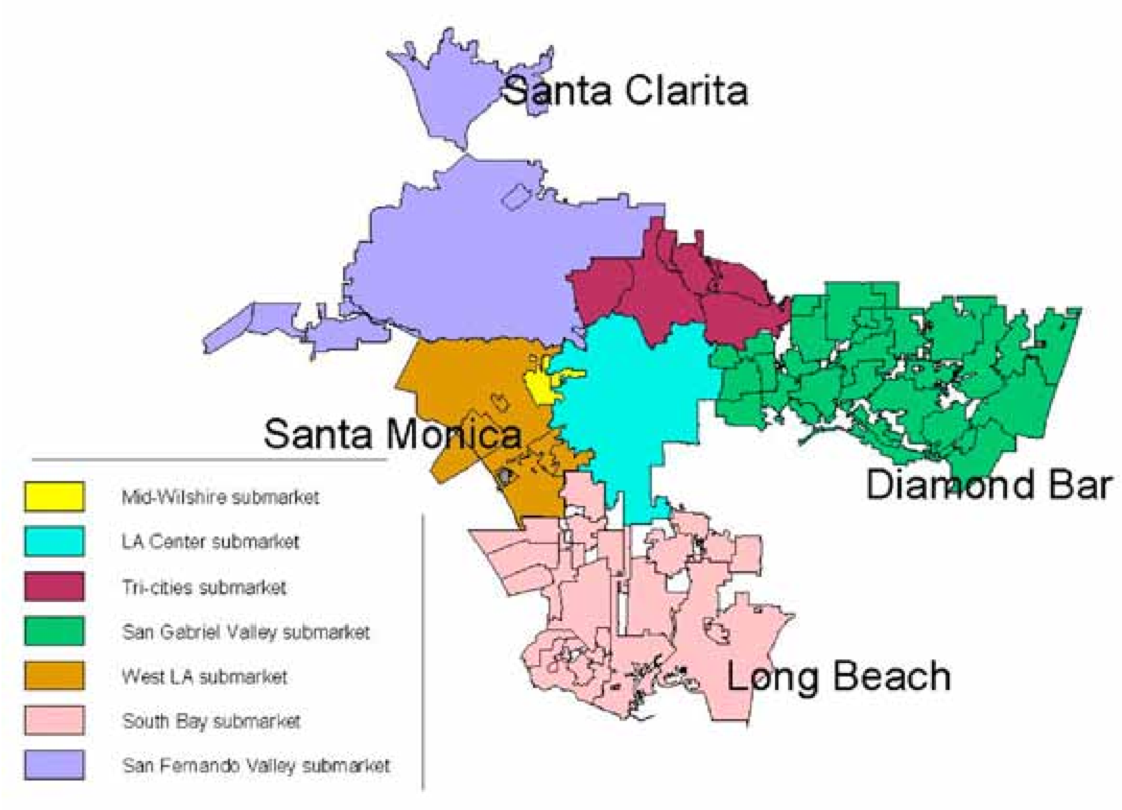
Submarket notes:

Our models, once again, predict large percentage increases in rents and stable or declining vacancy in all five submarkets. The Temecula/South submarket is expected to record the highest rent growth, with increases of 31.1 percent over the next four quarters and 48.2 percent total over the next two years. Given that the Temecula/South submarket witnessed a 33.3 percent decline in rents over the last year and currently carries the lowest average asking rents in Southern California ($0.30 per square foot), the predicted movements are not outside the realm of possibility. The West submarket is expected to be the weakest performer over the next two years, with an increase in rents of only 4.2 percent.

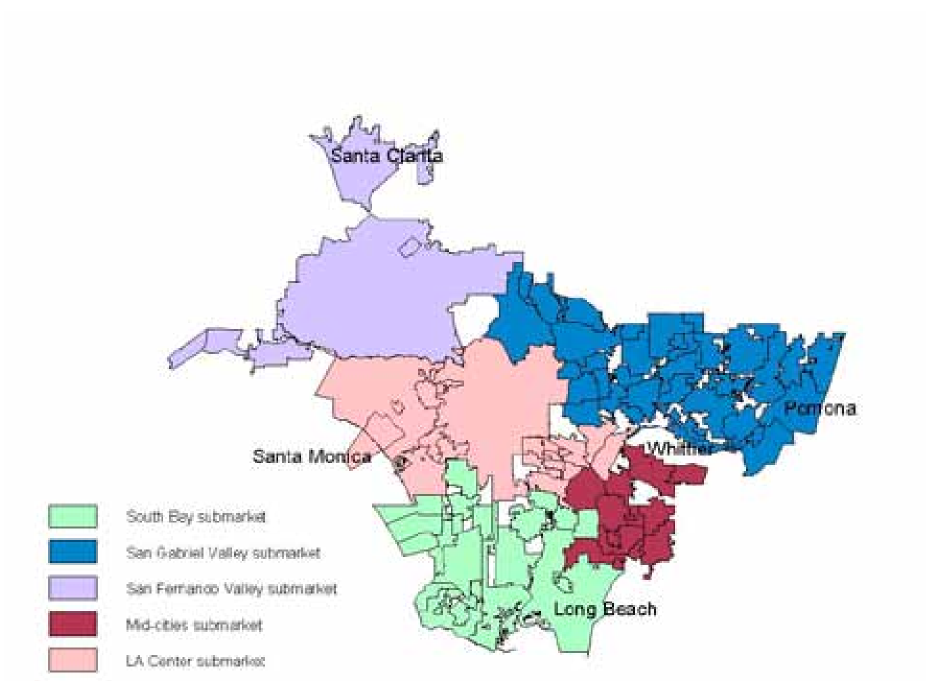
On the demand side, the Riverside submarket is expected to log the greatest decline in vacancy: 2 percentage points over the next four quarters and 2.5 percentage points total over the next two years. Currently, the Riverside submarket has the highest vacancy rate at 6.4 percent and thus, the greatest room for improvement, but the addition of up to 5 million square feet of space over the next two years will likely lessen the decline.

Current Market Snapshots

Office submarket for Los Angeles County



Industrial submarket for Los Angeles County



Los Angeles County Office Snapshot

Average Monthly Rents PSF	Class A	Class B	Total Vacancy Rate
	Q3 2012		Q3 2012
Downtown	$3.26	$2.53	17.0%
Mid-Wilshire	$2.02	$1.65	21.1%
Tri-Cities	$2.80	$2.29	17.9%
South Bay	$2.28	$2.05	19.5%
San Gabriel Valley	$2.29	$1.88	9.6%
Los Angeles North	$2.29	$2.01	16.4%
West Los Angeles	$3.50	$2.79	15.6%
Los Angeles County	$2.93	$2.19	16.6%

Los angeles County Office Quarter Comparison

Class A Average Monthly Rents PSF	Current Quarter		Previous Quarter		1 Year Ago		Net Absorption Q4 2011 to Q3 2012 (000)	Change in Average Rent
Total Vacancy Rate	Q3 2012		Q2 2012		Q3 2011			2011-2012
Downtown	$3.26	17.0%	$3.27	17.0%	$3.13	16.3%	(72)	4.0%
Mid-Wilshire	$2.02	21.1%	$2.02	20.3%	$2.00	19.4%	(146)	1.0%
Tri-Cities	$2.80	17.9%	$2.81	17.4%	$2.81	18.0%	10	-0.3%
South Bay	$2.28	19.5%	$2.29	19.5%	$2.28	20.2%	459	0.2%
San Gabriel Valley	$2.29	9.6%	$2.32	9.3%	$2.40	10.2%	100	-4.7%
LA North	$2.29	16.4%	$2.30	16.4%	$2.32	17.4%	343	-1.4%
West Los Angeles	$3.50	15.6%	$3.58	15.2%	$3.62	14.8%	(291)	-3.2%
Los Angeles County	$2.93	16.6%	$2.95	16.4%	$2.94	16.6%	402	-0.4%

Class A Average Rents for LA County Submarkets

Office Vacancy Rates for LA County Submarkets

2012 Year-over-year Class A Rent Increases

Los Angeles County Industrial Subtype

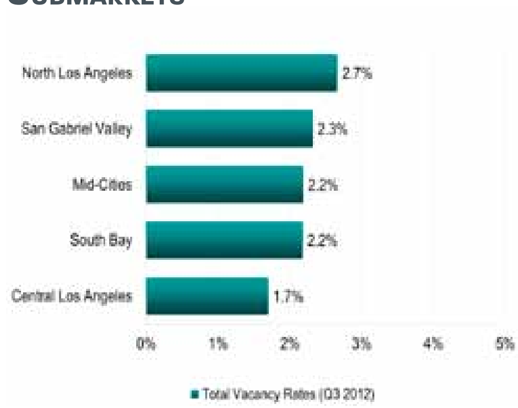
Average Monthly Rents PSF Total Vacancy Rate	Current Quarter Q3 2012		Previous Quarter Q2 2012		1 Year Ago Q3 2011		Change in Average Rent 2011-2012
General Industrial	$0.55	1.7%	$0.54	1.8%	$0.51	2.9%	7.4%
Incubator	$0.62	2.6%	$0.62	2.3%	$0.59	3.0%	4.5%
R&D/Flex	$0.75	3.0%	$0.71	2.7%	$0.69	3.9%	8.8%
Warehouse	$0.49	2.5%	$0.48	2.6%	$0.47	3.3%	3.9%

Los Angeles County Indusrial Quarter Comparison

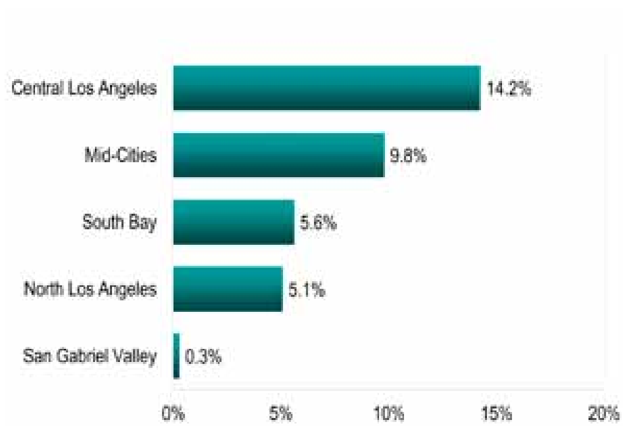
Average Monthly Rents PSF Total Vacancy Rate	Current Quarter Q3 2012		Previous Quarter Q2 2012		1 Year Ago Q3 2011		Net Absorption Q4 2011 to Q3 2012 (000)	Change in Average Rent 2011-2012
Central Los Angeles	$0.47	1.7%	$0.45	1.7%	$0.41	2.5%	1,859	14.2%
Mid-Cities	$0.49	2.2%	$0.48	2.8%	$0.45	4.1%	1,964	9.8%
North Los Angeles	$0.64	2.7%	$0.65	2.4%	$0.61	3.2%	441	5.1%
San Gabriel Valley	$0.45	2.3%	$0.44	2.6%	$0.45	3.5%	2,543	0.3%
South Bay	$0.55	2.2%	$0.54	2.2%	$0.52	3.2%	2,240	5.6%
Los Angeles County	$0.53	2.1%	$0.52	2.2%	$0.50	3.1%	9,047	6.3%

Average Rents for LA County

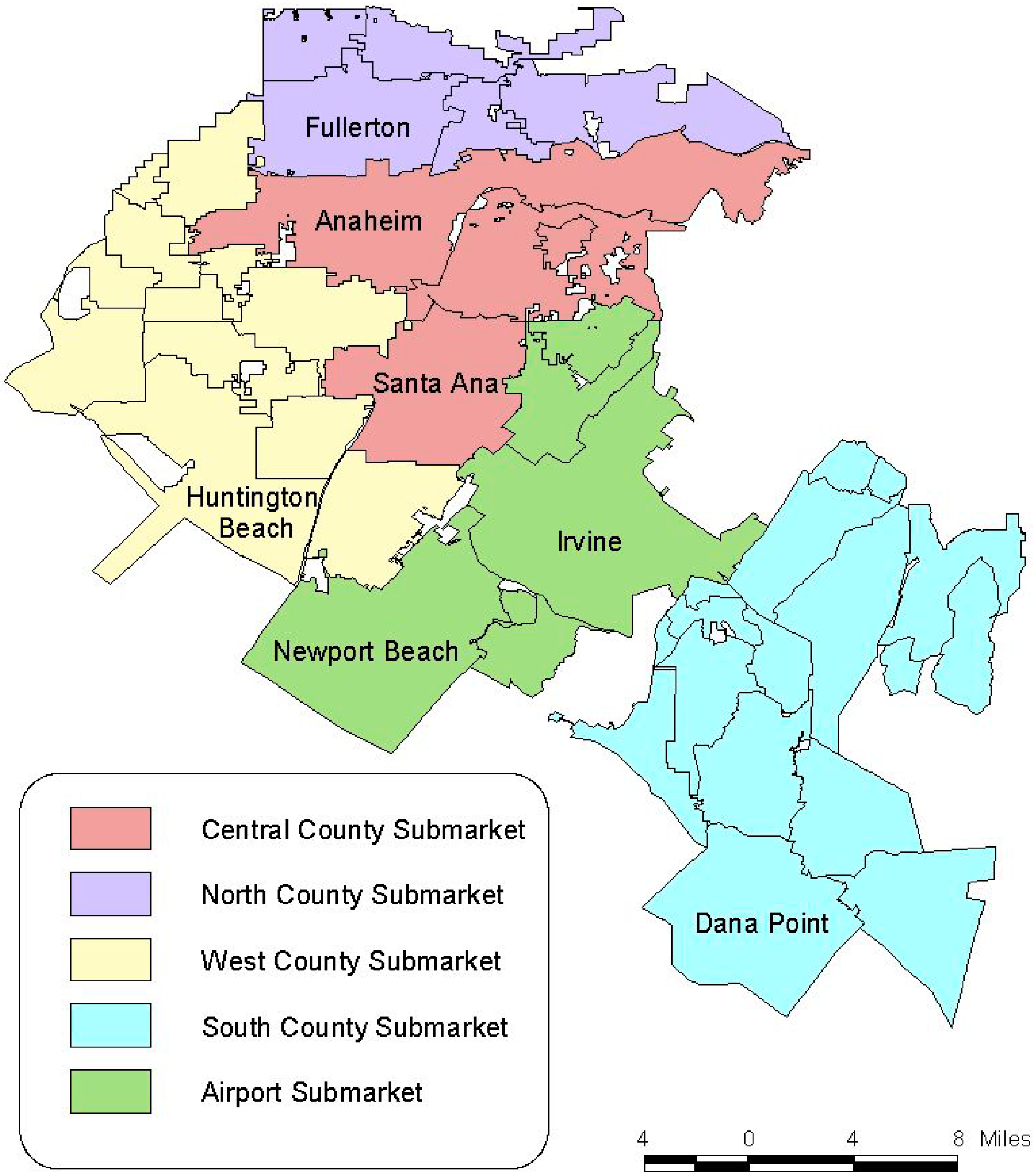
Industrial Vacancy Rates for LA Submarkets



2012 Year-over-year Average Rent Changes



Office and Industrial Submarkets for Orange County



Orange County Office Snapshot

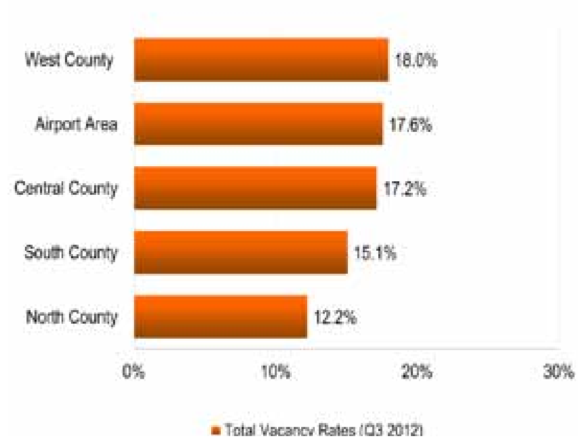
Average Monthly Rents PSF	Class A	Class B	Total Vacancy Rate
	Q3 2012		Q3 2012
Airport Area	$2.18	$1.79	17.6%
Central County	$2.06	$1.64	17.2%
North County	$2.24	$1.68	12.2%
South County	$1.90	$1.82	15.1%
West County	$2.11	$1.62	18.0%
Orange County	$2.11	$1.73	16.6%

Orange County Office Quarter Comparison

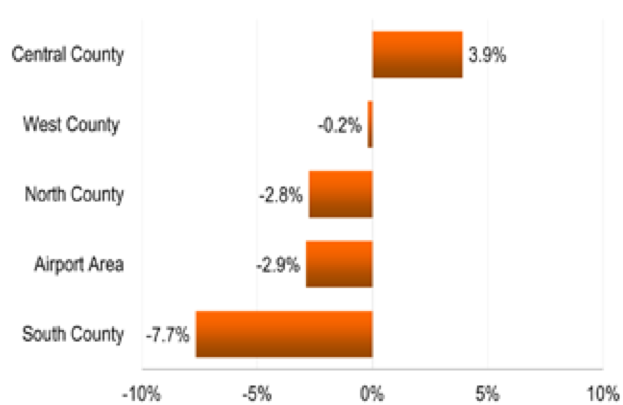
Class A Average Monthly Rents PSF	Current Quarter		Previous Quarter		1 Year Ago		Net Absorption Q4 2011 to Q3 2012 (000)	Change in Average Rent
Total Vacancy Rate	Q3 2012		Q2 2012		Q3 2011			2011-2012
Airport Area	$2.18	17.6%	$2.20	18.1%	$2.24	20.2%	1,152	-2.9%
Central County	$2.06	17.2%	$2.06	17.9%	$1.98	18.7%	138	3.9%
North County	$2.24	12.2%	$2.25	14.0%	$2.30	15.9%	302	-2.8%
South County	$1.90	15.1%	$1.99	16.1%	$2.06	16.6%	226	-7.7%
West County	$2.11	18.0%	$2.08	14.6%	$2.11	12.5%	(170)	-0.2%
Orange County	$2.11	16.6%	$2.15	17.0%	$2.17	18.3%	1,649	-2.9%

Class A Average Rents for Orange County

Office Vacancy Rates for Orange County Submarkets



2012 Year-over-year Class A Rent Changes



Orange County Industrial Subtype

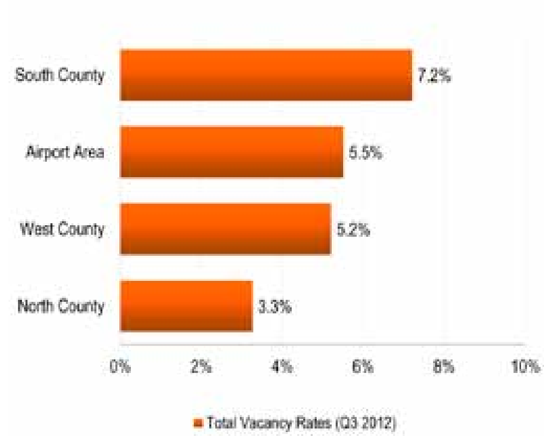
Average Monthly Rents PSF	Current Quarter		Previous Quarter		1 Year Ago		Change in Average Rent
Total Vacancy Rate	Q3 2012		Q2 2012		Q3 2011		2011-2012
General Industrial	$0.59	3.9%	$0.59	4.2%	$0.65	4.2%	-9.4%
R&D/Flex	$0.94	6.6%	$0.98	6.5%	$0.98	6.5%	-4.6%
Warehouse	$0.54	4.4%	$0.52	4.5%	$0.51	5.8%	5.3%

Orange County Indusrial Quarter Comparison

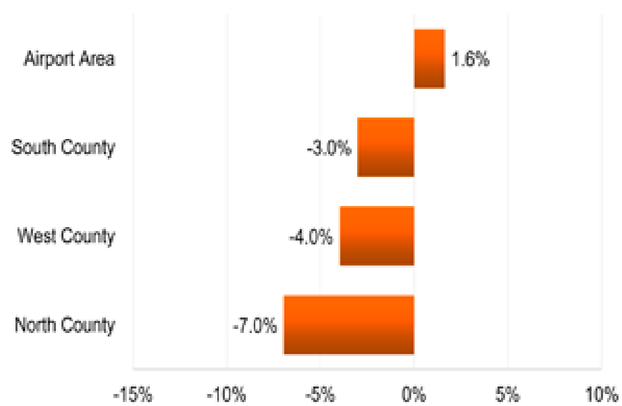
Average Monthly Rents PSF	Current Quarter		Previous Quarter		1 Year Ago		Net Absorption Q4 2011 to Q3 2012 (000)	Change in Average Rent
Total Vacancy Rate	Q3 2012		Q2 2012		Q3 2011			2011-2012
Airport Area	$0.86	5.5%	$0.84	5.8%	$0.85	6.0%	488	1.6%
North County	$0.53	3.3%	$0.54	3.4%	$0.57	4.0%	980	-7.0%
South County	$0.82	7.2%	$0.86	8.1%	$0.85	8.1%	414	-3.0%
West County	$0.60	5.2%	$0.58	4.3%	$0.63	4.3%	(326)	-4.0%
Orange County	$0.71	4.8%	$0.72	5.0%	$0.74	5.3%	1,556	-4.3%

Average Rents for for Orange County

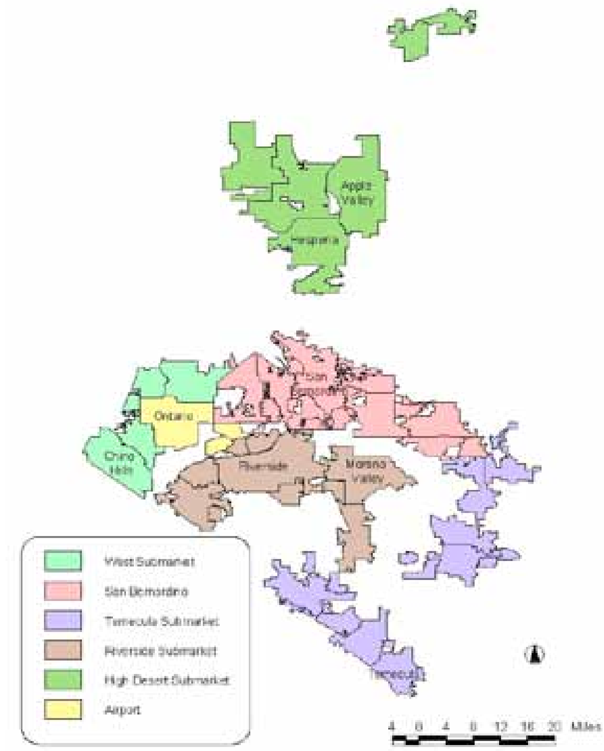
Industrial Vacancy Rates for Orange County Submarkets



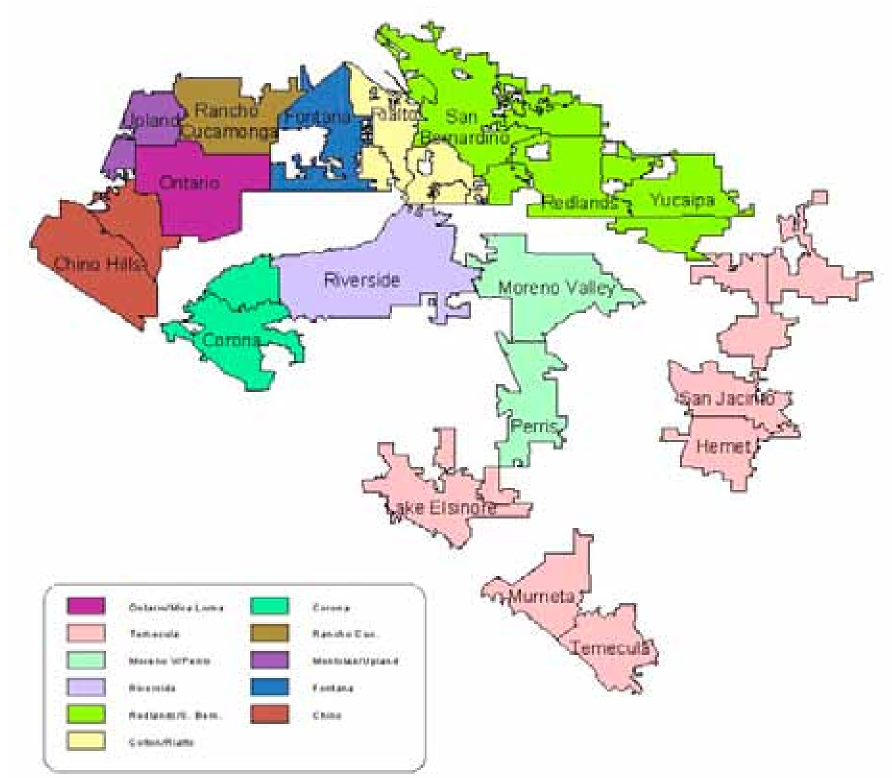
2012 Year-over-year Average Rent Changes



Office Submarkets for Inland Empire



Industrial Submarkets for Inland Empire



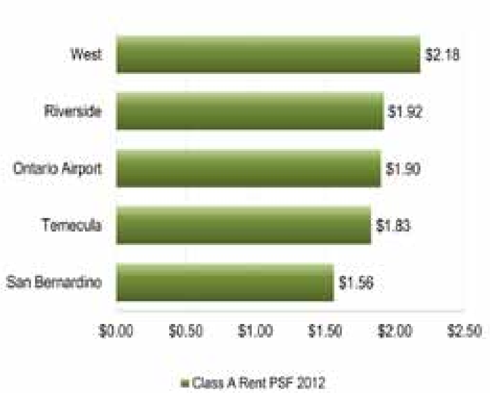
Inland Empire Office Snapshot

Average Monthly Rents PSF	Class A	Class B	Total Vacancy Rate
	Q3 2012		Q3 2012
Ontario Airport	$1.90	$1.50	23.3%
Riverside	$1.92	$1.55	20.4%
San Bernardino	$1.56	$1.41	21.3%
Temecula	$1.83	$1.33	19.0%
West	$2.18	$1.47	17.4%
Inland Empire	$1.85	$1.47	21.1%

Inland Empire Office Quarter Comparison

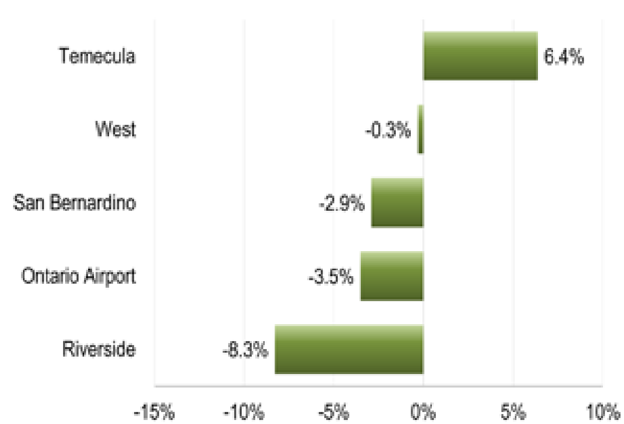
Class A Average Monthly Rents PSF Total Vacancy Rate	Current Quarter Q3 2012		Previous Quarter Q2 2012		1 Year Ago Q3 2011		Net Absorption Q4 2011 to Q3 2012 (000)	Change in Average Rent 2011-2012
Ontario Airport	$1.90	23.3%	$1.94	23.8%	$1.97	23.9%	59	-3.5%
Riverside	$1.92	20.4%	$1.91	21.2%	$2.09	25.2%	350	-8.3%
San Bernardino	$1.56	21.3%	$1.57	21.5%	$1.61	22.2%	136	-2.9%
Temecula	$1.83	19.0%	$1.83	18.8%	$1.72	25.3%	145	6.4%
West	$2.18	17.4%	$2.18	18.3%	$2.19	19.4%	30	-0.3%
Inland Empire	$1.85	21.1%	$1.86	21.6%	$1.92	23.8%	721	-3.6%

Class A Average Rents for Inland Empire



Office Vacancy Rates for Inland Empire Submarkets

2012 Year-over-year Class A Rent Changes



Inland Empire Industrial Subtype

Average Monthly Rents PSF	Current Quarter		Previous Quarter		1 Year Ago		Change in Average Rent
Total Vacancy Rate	Q3 2012		Q2 2012		Q3 2011		2011-2012
General Industrial	$0.31	8.5%	$0.33	8.9%	$0.37	11.7%	-15.8%
R&D/Flex	$0.46	5.0%	$0.51	5.5%	$0.56	7.2%	-17.5%
Warehouse	$0.36	4.6%	$0.33	5.0%	$0.32	6.2%	11.0%

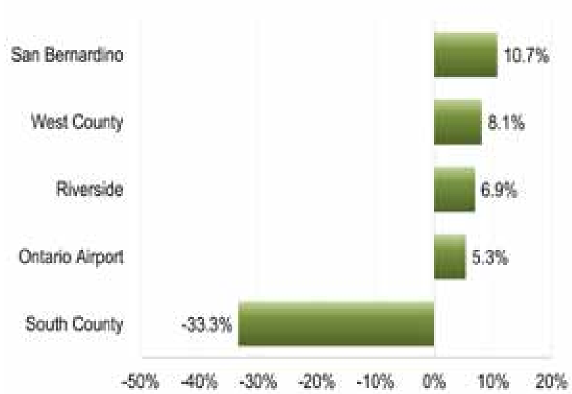
Inland Empire Indusrial Quarter Comparison

Average Monthly Rents PSF	Current Quarter		Previous Quarter		1 Year Ago		Net Absorption Q4 2011 to Q3 2012 (000)	Change in Average Rent
Total Vacancy Rate	Q3 2012		Q2 2012		Q3 2011			2011-2012
Ontario Airport	$0.36	4.2%	$0.34	4.7%	$0.34	5.7%	3,226	5.3%
Riverside	$0.34	6.4%	$0.33	7.1%	$0.32	8.5%	3,518	6.9%
San Bernardino	$0.32	6.3%	$0.31	6.6%	$0.29	8.7%	2,378	10.7%
South County	$0.30	3.2%	$0.38	3.0%	$0.45	4.9%	294	-33.3%
West County	$0.40	4.1%	$0.38	4.5%	$0.37	3.4%	(31)	8.1%
Inland Empire	$0.35	4.9%	$0.33	5.3%	$0.33	6.6%	9,385	6.1%

Average Rents for for Inland Empire

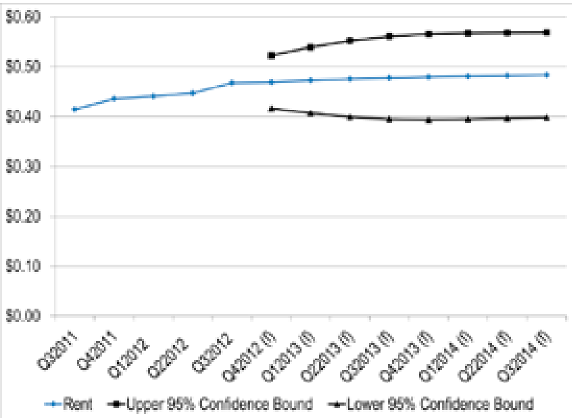
Industrial Vacancy Rates for Inland Empire Submarkets

2012 Year-over-year Average Rent Changes

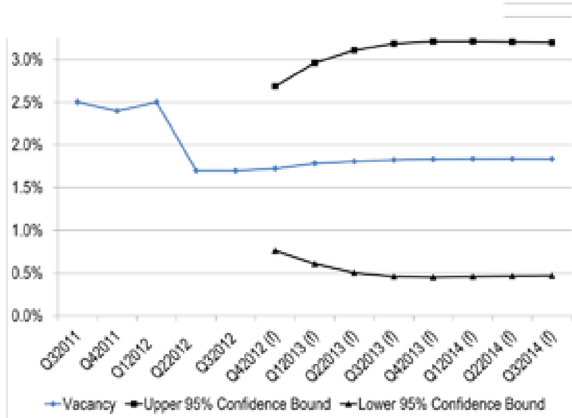


Appendix I Los Angeles County Industrial Forecasted Rents and Vacancy

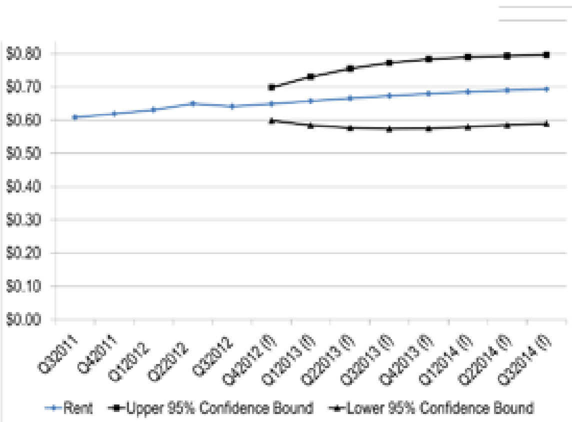
Central Los Angeles Forecasted Rents



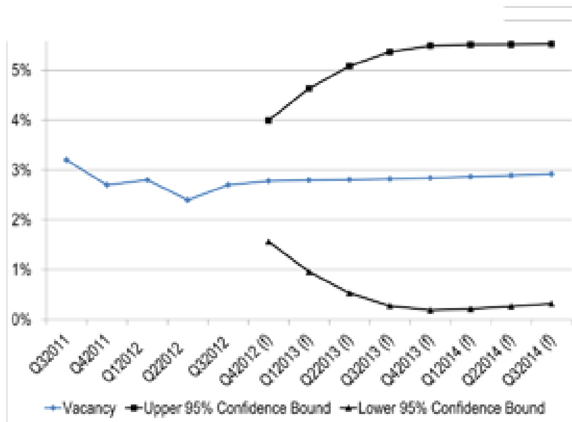
Central Los Angeles Forecasted Vacancy



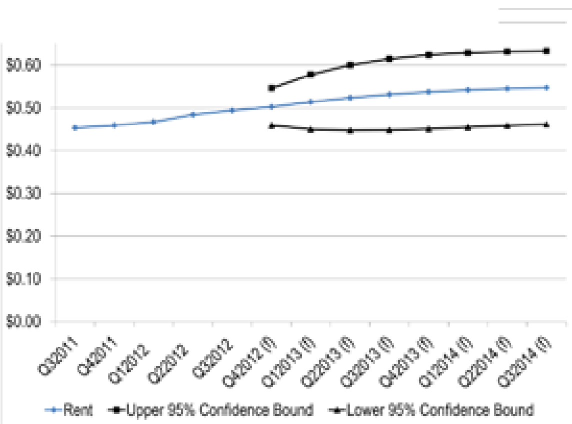
North Los Angeles Forecasted Rents



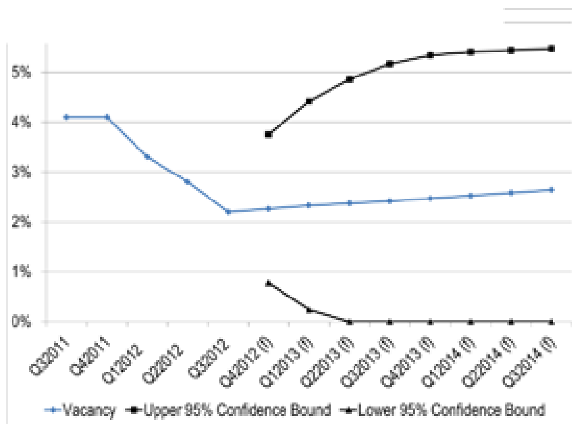
North Los Angeles Forecasted Vacancy



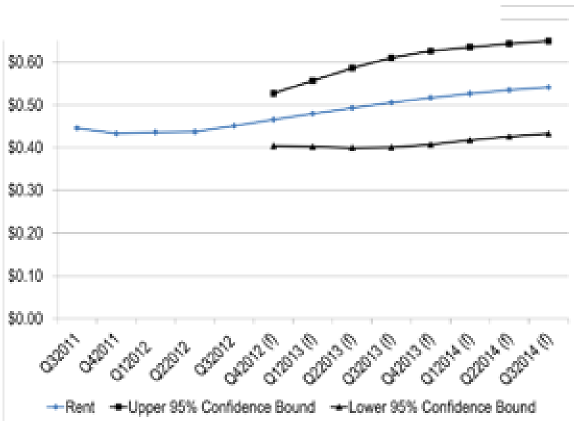
Mid-Cities Forecasted Rents



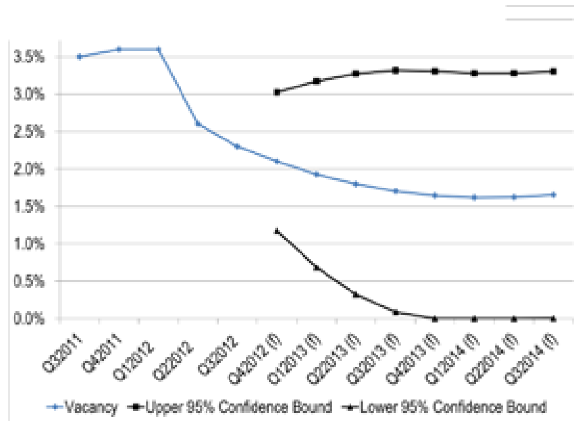
Mid-Cities Forecasted Vacancy



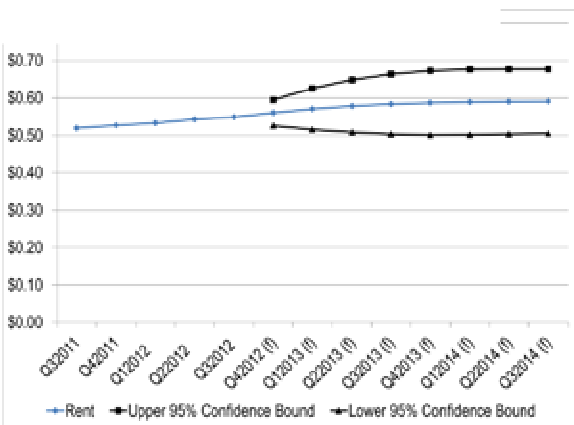
San Gabriel Valley Forecasted Rents



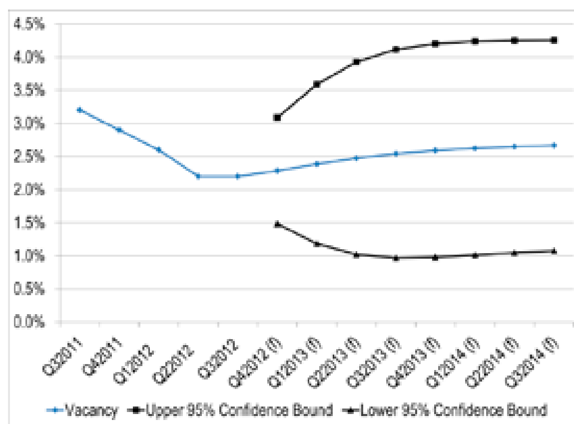
San Gabriel Valley Forecasted Vacancy



South Bay Forecasted Rents

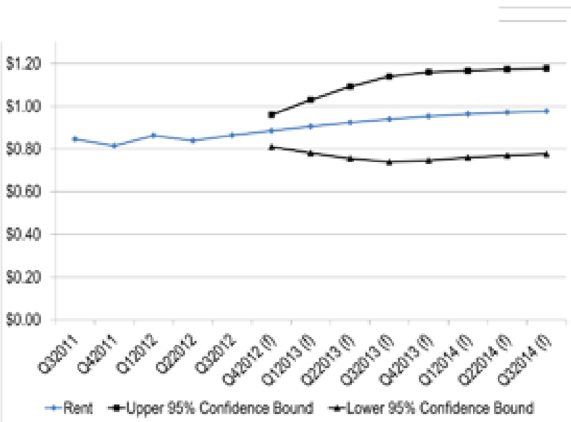


South Bay Forecasted Vacancy

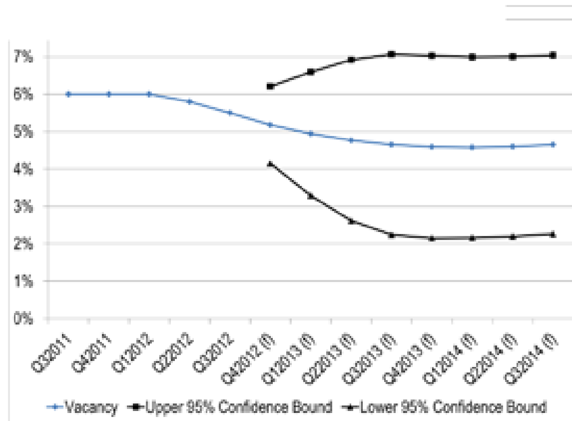


Appendix II Orange County Industrial Forecasted Rents and Vacancy

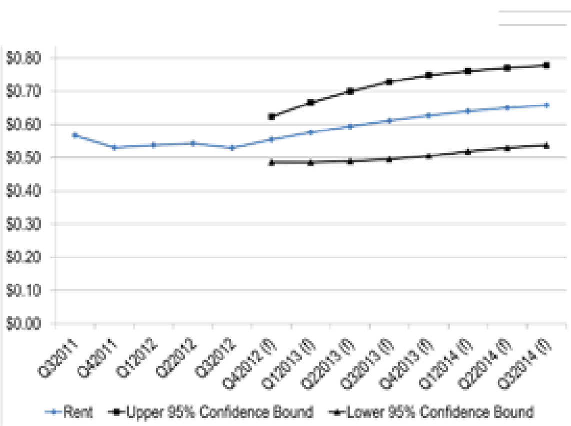
Airport Area Forecasted Rents



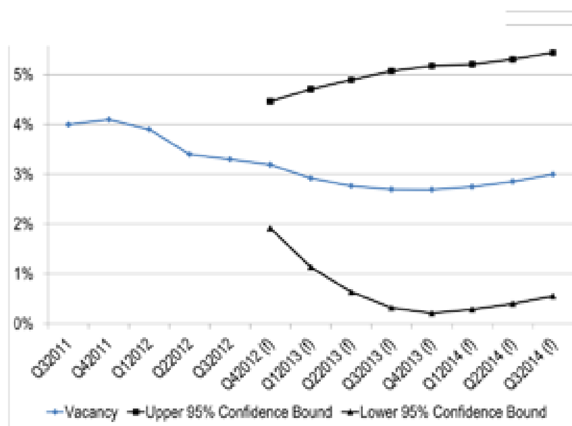
Airport Area Forecasted Vacancy



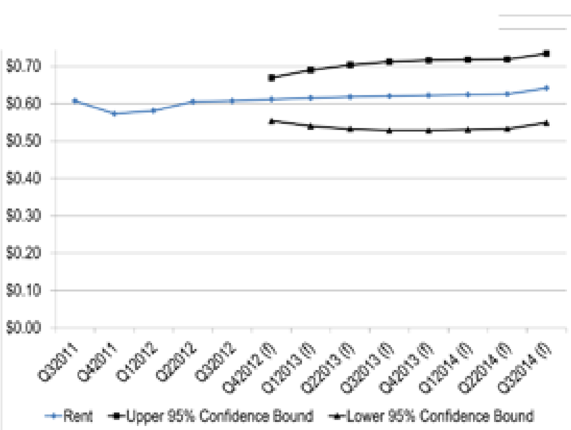
North Orange County Forecasted Rents



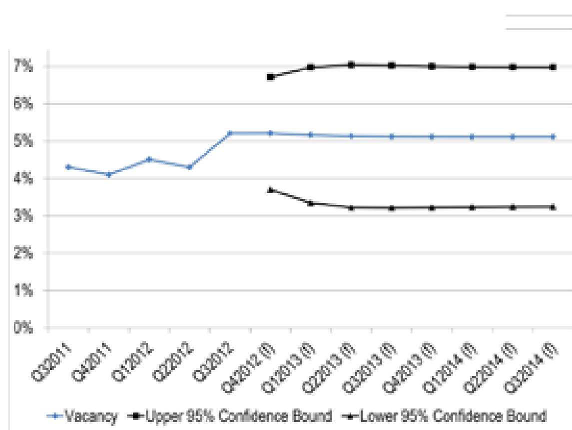
North Orange County Forecasted Vacancy



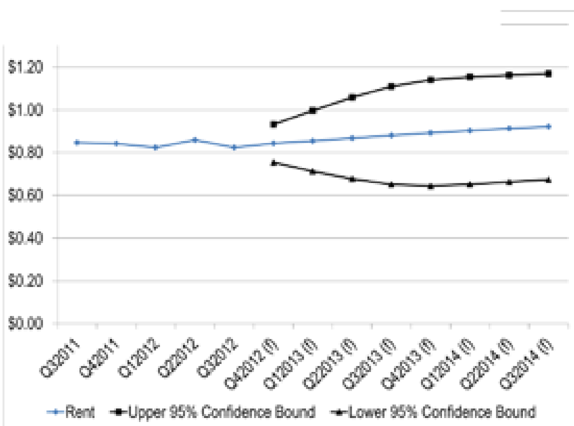
West Orange County Forecasted Rents



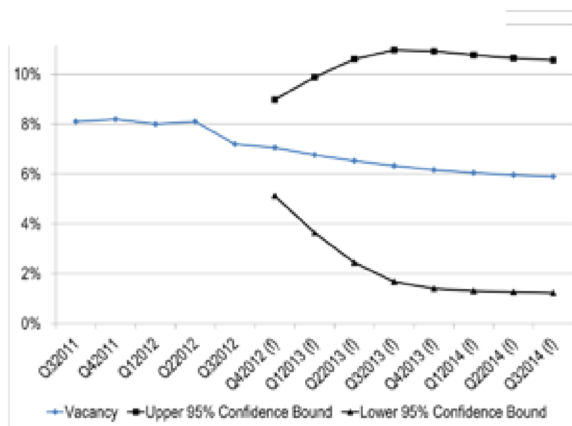
West Orange County Forecasted Vacancy



South Orange County Forecasted Rents

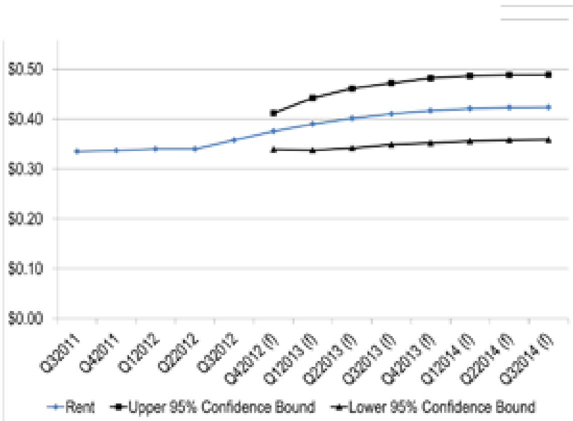


South Orange County Forecasted Vacancy

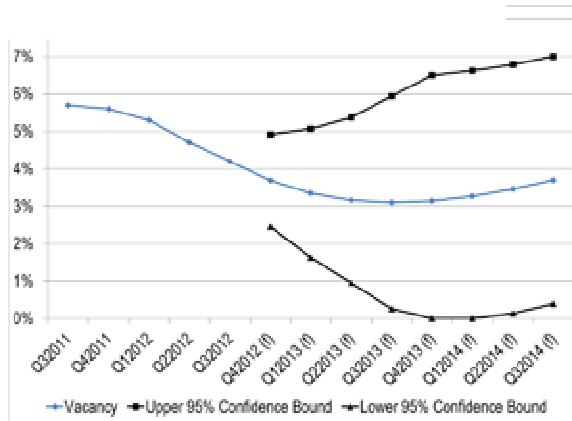


Appendix III Inland Empire Industrial Forecasted Rents and Vacancy

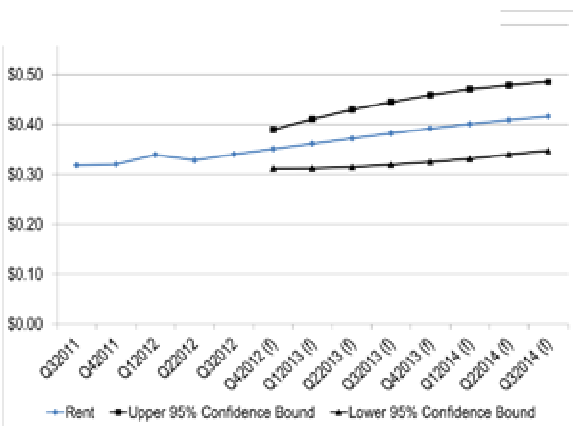
Ontario Airport Forecasted Rents



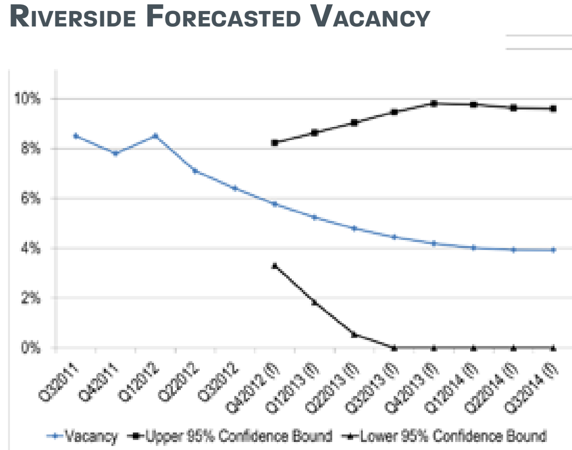
Ontario Airport Forecasted Vacancy



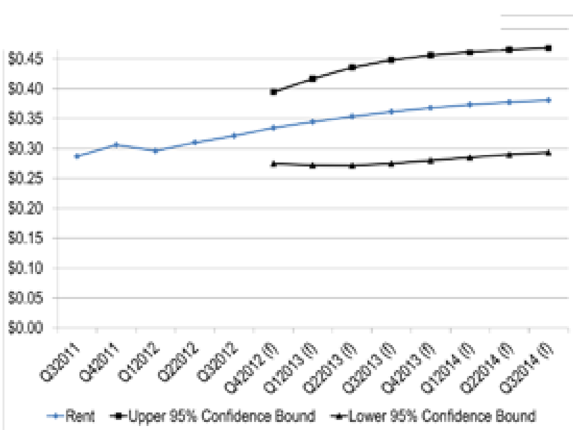
Riverside Forecasted Rents



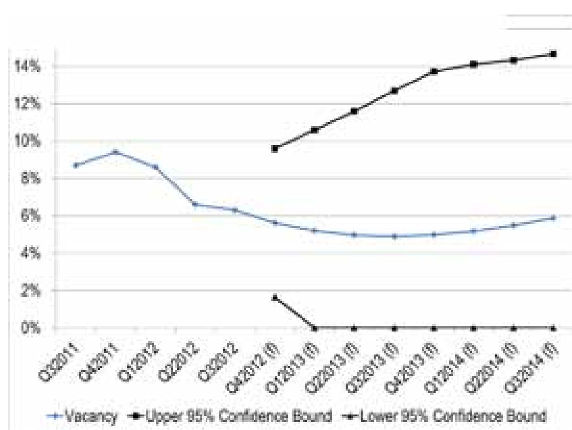
Riverside Forecasted Vacancy



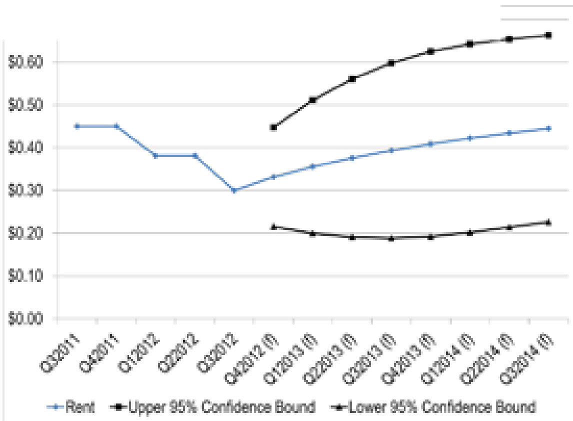
San Bernardino Forecasted Rents



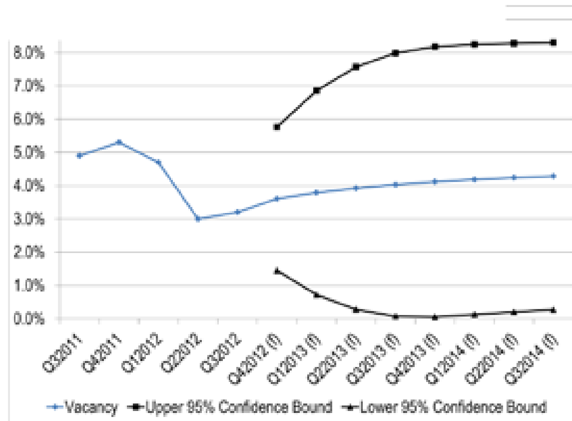
San Bernardino Forecasted Vacancy



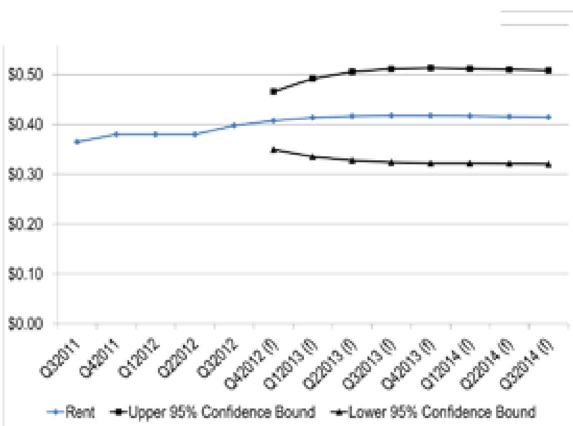
South County Forecasted Rents



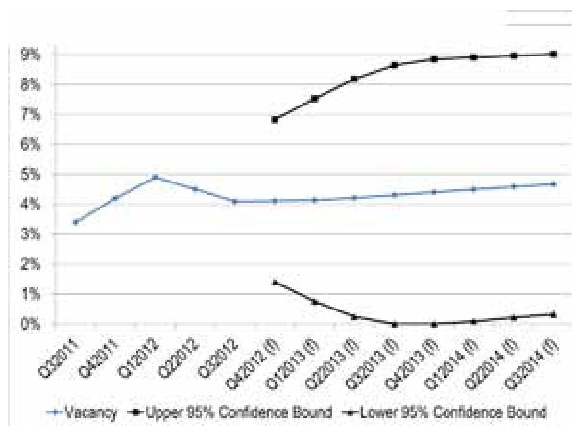
South County Forecasted Vacancy



West Forecasted Rents



West Forecasted Vacancy



Technical Notes

Office Data

Inventory: Office inventory includes all multi-tenant and single tenant buildings with a minimum size threshold of 20,000 square feet. Owner-occupied, government and medical buildings are not included.

Office Building Classifications: Grubb and Ellis adhere to the BOMA guidelines. Class A properties are the most prestigious buildings competing for premier office users with rents above average for the area. Class B properties compete for a wide range of users with rents in the average range for the area… Class C buildings compete for tenants requiring functional space at rents below the area average.

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 month. Office rents are reported as full service where all costs of operation are paid by the landlord up to a base year or expense stop.

Industrial Data

Inventory: Industrial inventory includes all multi-tenant, single tenant and owner-occupied buildings with at least 10,000 square feet and World Ports Industrial Market™ with at least 50,000 square feet.

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.

Space Under Construction: Space under construction that includes speculative, build-to-suit for lease and owner-built projects.

Vacant and Available Space: Vacant space is space that is physically unoccupied. It may or may not be available for lease or sublease. Available space is available for lease and may or may not be vacant.

Asking Rent: The dollar amount asked by landlords for available space expressed in dollars per square foot per month. 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.

Overall Disclaimer

Some of the data in this report has been gathered from third party sources and has not been independently verified. Neither Newmark Grubb Knight Frank nor the Casden Forecast make no warranties or representations as to the completeness or accuracy thereof.

Report Authors | Bios

Richard K. Green

Director of the USC Lusk Center for Real Estate

Richard K. Green, Ph.D., is the Director of the USC Lusk Center for Real Estate. He holds the Lusk Chair in Real Estate and is Professor in the Sol Price School of Public Policy and the Marshall School of Business.

Prior to joining the USC faculty, Dr. Green spent four years as the Oliver T. Carr, Jr., Chair of Real Estate Finance at The George Washington University School of Business. He was Director of the Center for Washington Area Studies and the Center for Real Estate and Urban Studies at that institution. Dr. Green also taught real estate finance and economics courses for 12 years at the University of Wisconsin-Madison, where he was Wangard Faculty Scholar and Chair of Real Estate and Urban Land Economics. He also has been principal economist and director of financial strategy and policy analysis at Freddie Mac. More recently, he was a visiting professor of real estate at the University of Pennsylvania's Wharton School, and he continues to retain an affiliation with Wharton. He is or has been involved with the Lincoln Institute of Land Policy, the Conference of Business Economists, the Center for Urban Land Economics Research, and the National Association of Industrial and Office Properties. Dr. Green also is a Weimer Fellow at the Homer Hoyt Institute, and a member of the faculty of the Selden Institute for Advanced Studies in Real Estate. He was recently President of the American Real Estate and Urban Economics Association.

Dr. Green earned his Ph.D. and M.S. in economics from the University of Wisconsin-Madison. He earned his A.B. in economics from Harvard University.

His research addresses housing markets, housing policy, tax policy, transportation, mortgage finance and urban growth. He is a member of two academic journal editorial boards, and a reviewer for several others. His work is published in a number of journals including the American Economic Review, Journal of Economic Perspectives, Journal of Real Estate Finance and Economics, Journal of Urban Economics, Land Economics, Regional Science and Urban Economics, Real Estate Economics, Housing Policy Debate, Journal of Housing Economics, and Urban Studies. His book with Stephen Malpezzi, A Primer on U.S. Housing Markets and Housing Policy, is used at universities throughout the country. His work has been cited or he has been quoted in the New York Times, The Wall Street Journal, The Washington Post, the Christian Science Monitor, the Los Angeles Times, Newsweek and the Economist, as well as other outlets. He recently gave a presentation at the 31st annual Federal Reserve Bank of Kansas City Economic Symposium, where his work was cited by Federal Reserve Chairman Ben Bernanke. The National Association of REALTORS, the Ford Foundation, and the Lincoln Institute for Land Policy have funded grants to support some of Dr. Green's research. He consults for the World Bank.

In 1995, Dr. Green was honored as "Teacher of the Year" by the University of Wisconsin Graduate Business Association, and soon thereafter was inducted into that University's Teaching Academy.

Tracey Seslen

Senior Research Associate
USC Casden Real Estate Economics Forecast

Tracey Seslen received her Ph.D. in Economics from the Massachusetts Institute of Technology in 2003 and has been an Assistant Professor of Clinical Finance and Business Economics since 2006. Over the last eight years, she has taught Real Estate Finance and Capital Markets in the Marshall School of Business and has been one of the core finance instructors for the Ross Minority Program in Real Estate. Her research has focused on housing cycles, the capitalization of risk and return into housing prices, household mobility behavior, and termination risk in commercial mortgages.

For the past three years, she has been the co-author of the Casden Real Estate Economics Forecast and in that role has developed new models for predicting price and vacancy movements for office, industrial and multi-family markets in Southern California. Her expertise in real estate finance has led to quotes in the LA Times, Wall Street Journal, OC Register, LA Business Journal, Long Beach Business Journal, California Real Estate Journal, SmartMoney.com, Downtown News, and other local and national publications. In addition, she has appeared on the Today Show, Marketplace Radio, and various local network news broadcasts. Recently, she has worked as an expert witness on real estate valuation issues.

When not working in the field of real estate, she is an avid international traveler, photographer, and chef. She lives in Seattle with her husband and two daughters, ages 4 and 3 months.

J.C. Casillas

Assistant Vice President,
Client Services Manager
Newmark Grubb Knight Frank Company

Mr. Casillas has been with Newmark Grubb Knight Frank since 1998. He is responsible for the management of the firm's Southern California research and marketing operations, overseeing extensive data collection, verification, tracking and analysis of the Southern California market. As part of the Southern California management team, Mr. Casillas works extensively with brokers on business development projects, client presentations and special research assignments. Mr. Casillas' market information and analysis are featured every quarter in the Commercial Real Estate update published by the Los Angeles Business Journal. He is recognized by various organizations and universities, including the Los Angeles County Economic Development Corporation (LAEDC), the San Fernando Valley Economic Research Center, and the Real Estate Research Council of Southern California as the "go-to" person for real estate market information. Mr. Casillas received a Bachelor of Science from USC majoring in Public Policy and Management with a minor in Business.

Skye Tirsbier
MBA/MPL
University of Southern California
Skye Tirsbier is a Master of Business Administration/Master of Planning dual degree Graduate of USC. Before attending USC, she worked as a project manager for real estate developer New Urban West in Santa Monica. Skye managed the entitlement process and secured approvals for a large mixed-use community in Southern California. After graduation in 2012, Skye joined SanDisk Corporation in the Bay Area as a Senior Financial Analyst.

www.usc.edu/casden