AVISON YOUNG

Los Angeles office market report

Q3 2021

AVANT by AVISON YOUNG

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10:22 pm
LA Live
Friday, October 8

5:37 pm
Staples Center
Friday, October 8

12:40 pm
Abbot Kinney
Wednesday, October 6

5:30 pm
LA Live
Friday, October 8

8:56 am
Financial District
Tuesday, October 12

12:57 pm
Westwood
Tuesday, October 12

Key takeaways

Los Angeles office market

- Overall vacancy in the 348.8 msf Los Angeles office market has risen to all-time highs, totaling **18.2 percent**.
- Q3 2021 net absorption was **-1.2 msf,** down from 2.0 msf in Q1 2021.
- Leasing activity rebounded in Q2 and Q3 after a slow start to the year. Closed deals totaled **3.9 msf** in Q3 2021, up from 3.1 msf in Q1 2021.
- The "flight to quality" trend persists, with the Class A and Trophy segment accounting for **79.4 percent** share of post-COVID leasing activity.

Sublease Space

- The sublease market continues to drag aggregate fundamentals down, accounting for **9.1 msf** of available space. However, available sublease space has decreased that last 6 months since its peak in Q1 2021 due to an increase in sublease volume and potential sublandlords pulling their space off the sublease market to reoccupy their space.
- Many companies have capitalized on discounted class A sublease space as sublease deals totaled nearly **600,000 sf** in Q3 2021, more than double sublease volume in Q1 2021.

Rental pricing trends

- Net effective rents decreased by **17.3 percent** from pre-pandemic levels as landlords induced tenant commitments through record-setting concession packages and favorable lease provisions, while keeping face rents relatively steady.
- Concessions packages have become more generous in recent months, the latest indication of tenant-favorable market conditions. Tenant improvement allowances for class A space average **$102.21 per square foot**, representing an increase of **14 percent** since 2019.

Key takeaways

Capital markets

- Money is chasing core and core+ properties but sellers are not apt to sell because it is hard for them to recycle capital. Thus, year-to-date investment volume is **$1.1B**, which is the weakest office investment activity reported since the credit crisis in 2009 when $1.3B was recorded.
- Asset pricing has dipped by **10 percent** since 2019, reflecting investors' conservative underwriting assumptions given prevailing occupier market conditions. However, creative office that caters to the entertainment industry is in high demand in target submarkets, demanding a premium.

Economic conditions

- The Los Angeles MSA's unemployment rate of **9.3 percent** nearly equals the average unemployment rate for the five-year period following the Great Recession

Post-COVID recovery rate

- There is a significant dichotomy between Los Angeles return-to-work efforts and other representative areas of interest. Office visitor volumes are **-59.4 percent** while healthcare and education have returned to pre-COVID levels compared with the same period in 2019.
- In the U.S. life sciences, real estate, and law firms have adopted hybrid work models, though tech firms struggled to return to pre-COVID visitor volumes (**-76.9 percent**).

01.

Office occupier conditions

Leasing activity has started to rebound, though heightened concessions have caused net effective rents to continue to soften.

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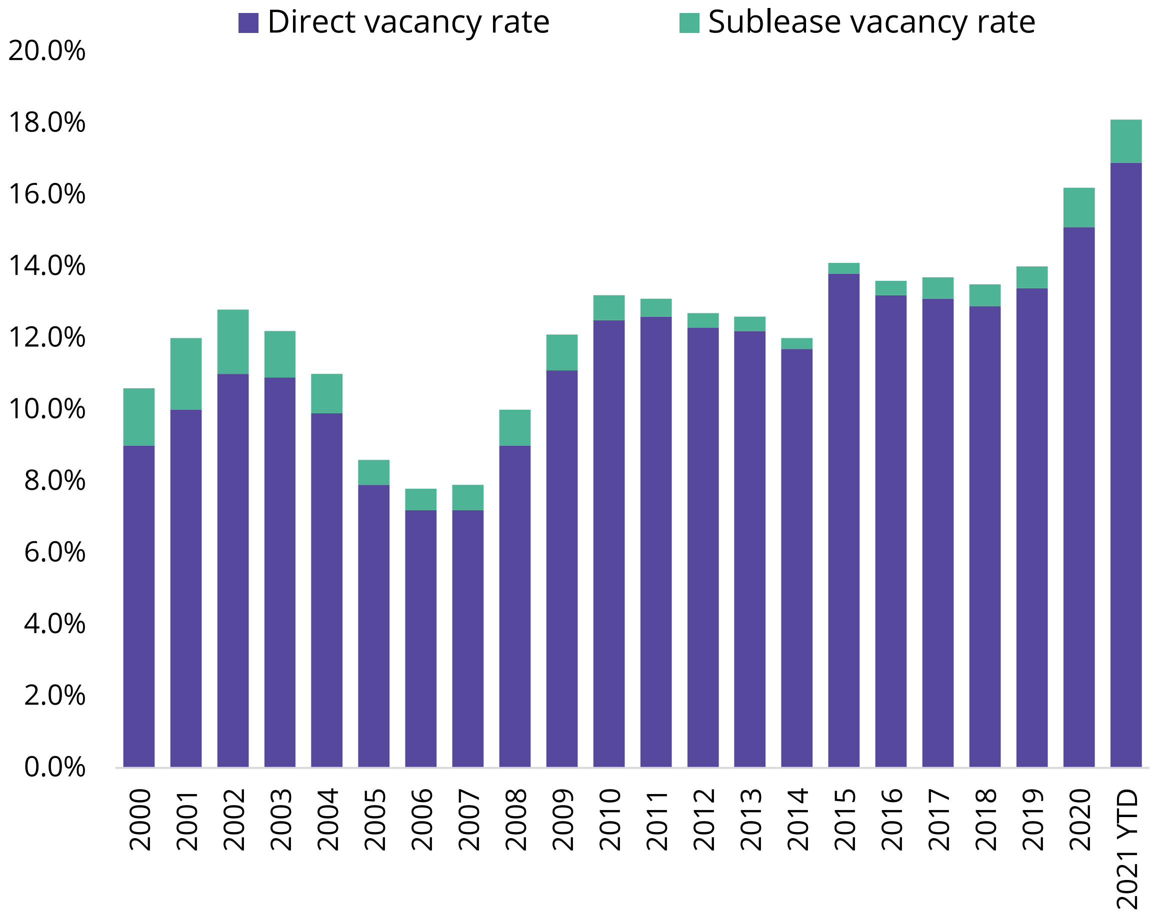
Vacancy rates have reached a record high

18.2%

Post-2000 high Los Angeles vacancy as of Q3 2021

The direct vacancy rate of 16.9% in Q3 2021 remained at a post-2000 peak, though sublease absorption—through subleases and withdrawals—enabled the sublease vacancy rate to dip to 1.2%, below the levels reported from 2001 to 2003. The ratio of sublease-to-total vacant space is comparatively lower than in other gateway markets such as San Francisco, New York, and Boston.



Source: Avison Young

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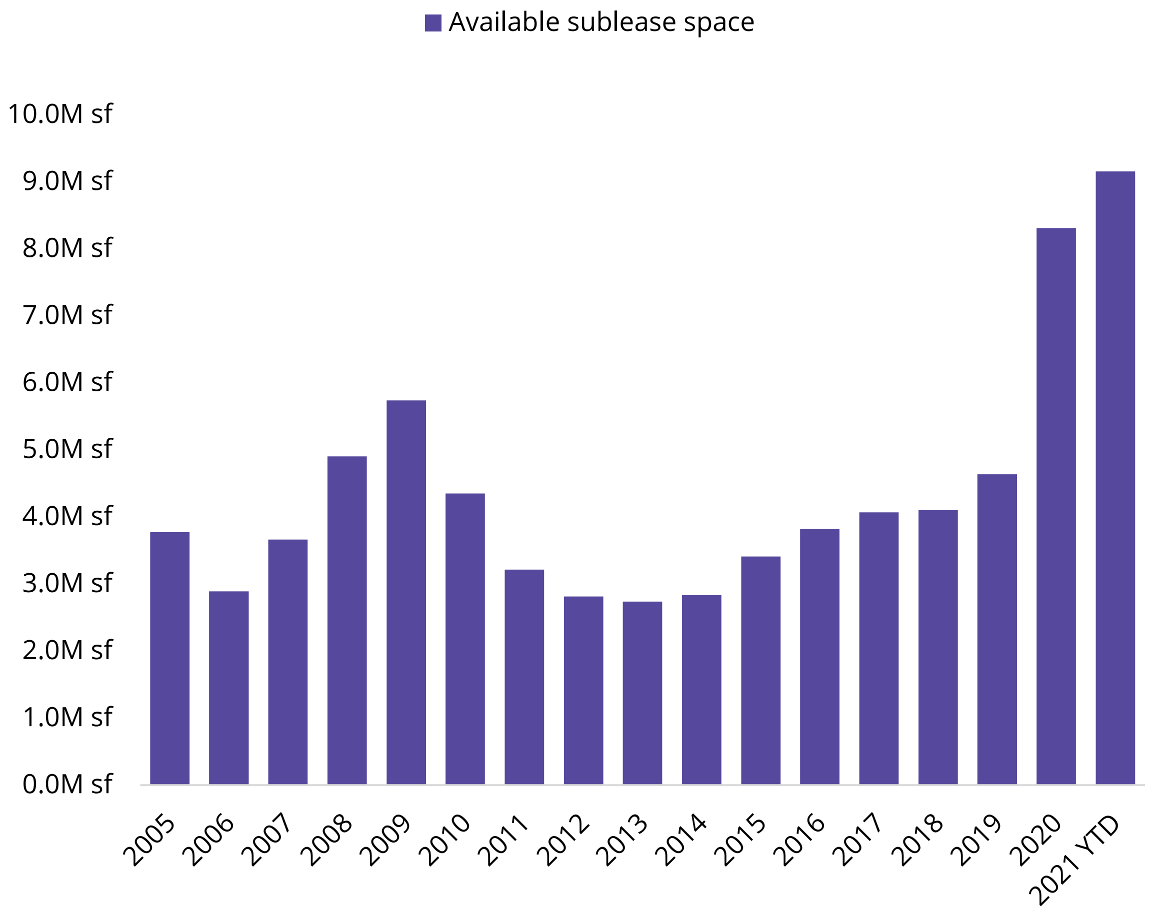
Available sublease space has decreased in Q3

9.1 msf

Available sublease space as of Q3 2021

Tenants have more sublease optionality in the current environment compared with the Global Financial Crisis. The scale of sublease availabilities of 9.1 million sf has no modern precedent.



Source: Avison Young

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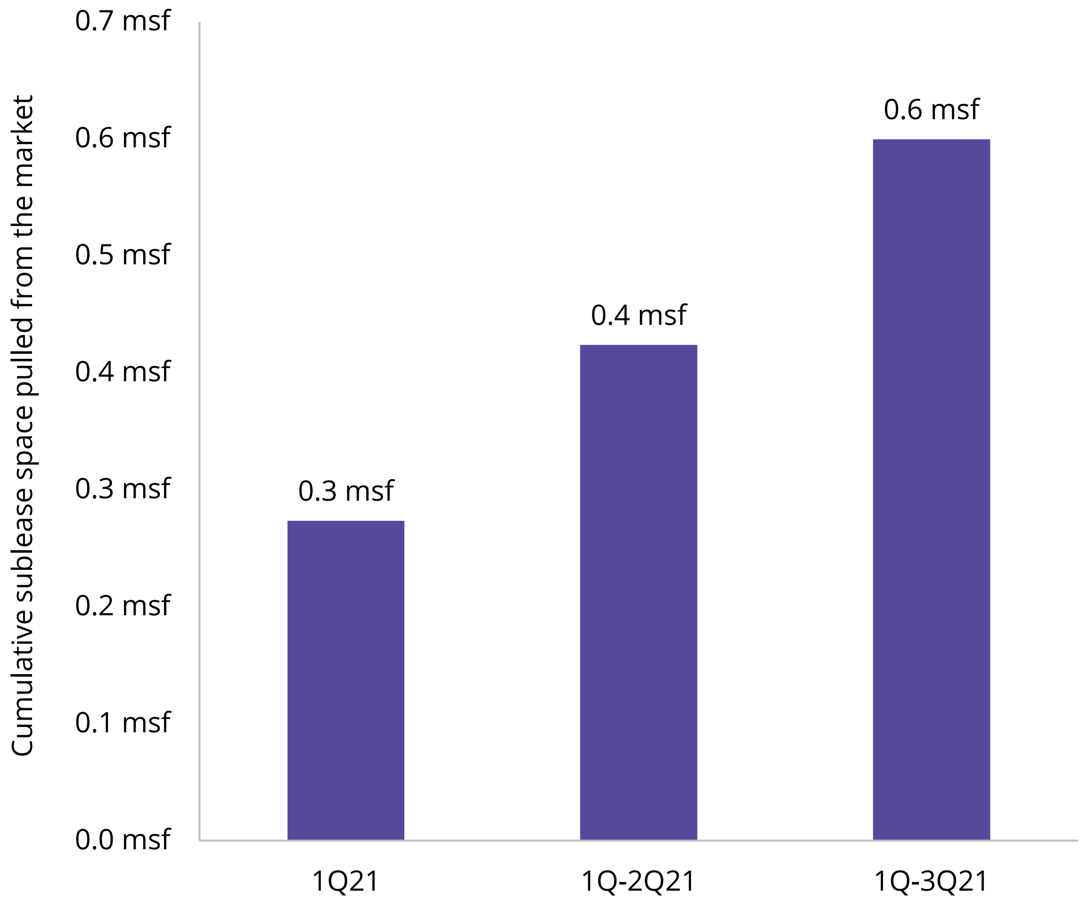
Sublease deal volume has increased

599,721 sf

Q3 sublease deals

Sublease deal volume has incrementally increased every quarter in 2021 as companies seek to capitalize on discounted space, particularly in the class A market. This trend combined with some prospective sublandlords pulling their availabilities from the market has allowed sublease availabilities to decrease since Q1 2021.



Source: AVANT by Avison Young

Office leasing activity has weakened

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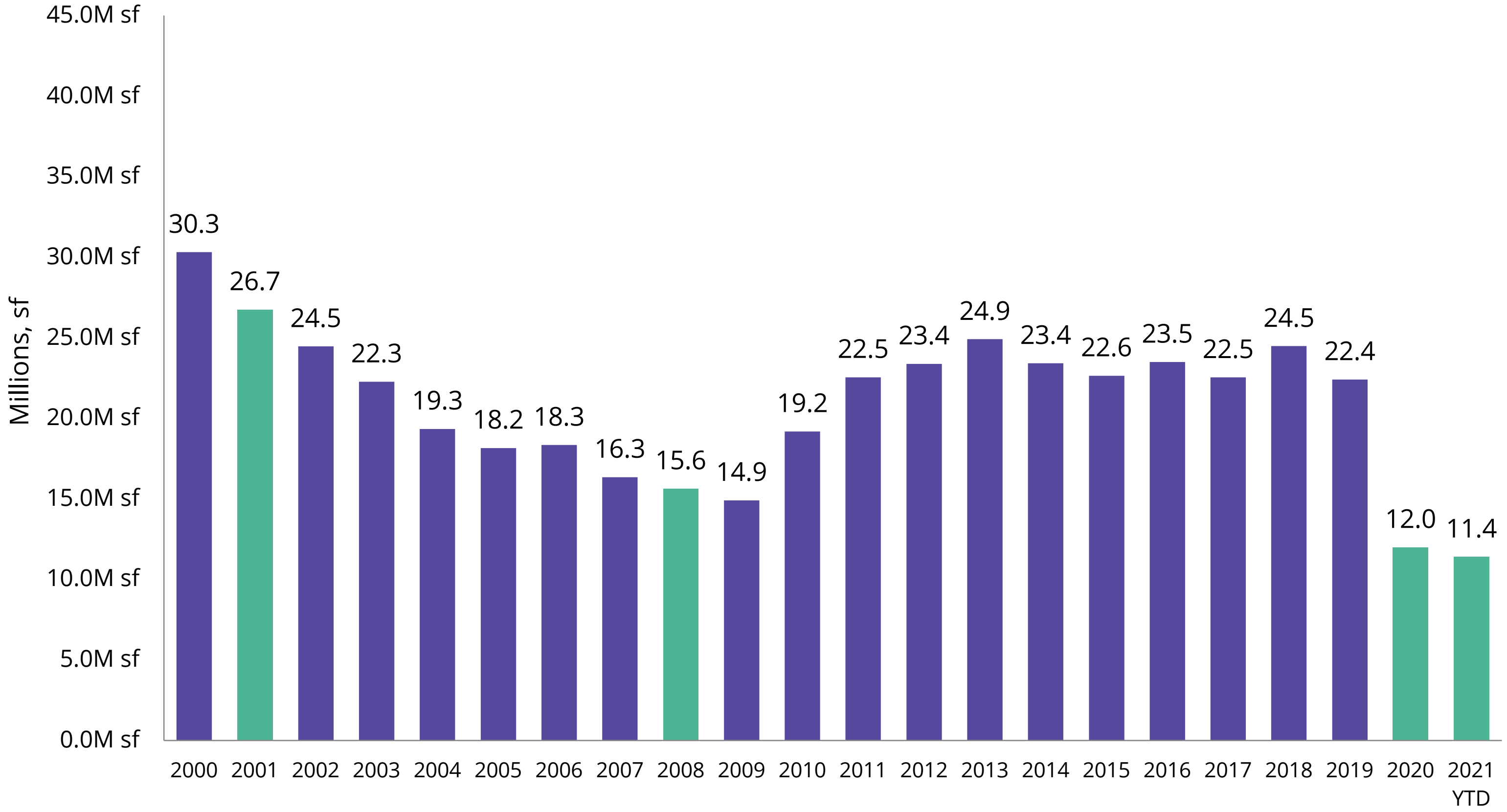
-28.7%

2021-pro-rated vs. prior 20-year annual average leasing activity

Leasing activity in 2021 is poised to outpace 2020 total although the annualized pace of closed deals remains the weakest reported since at least 2001.



Source: Avison Young

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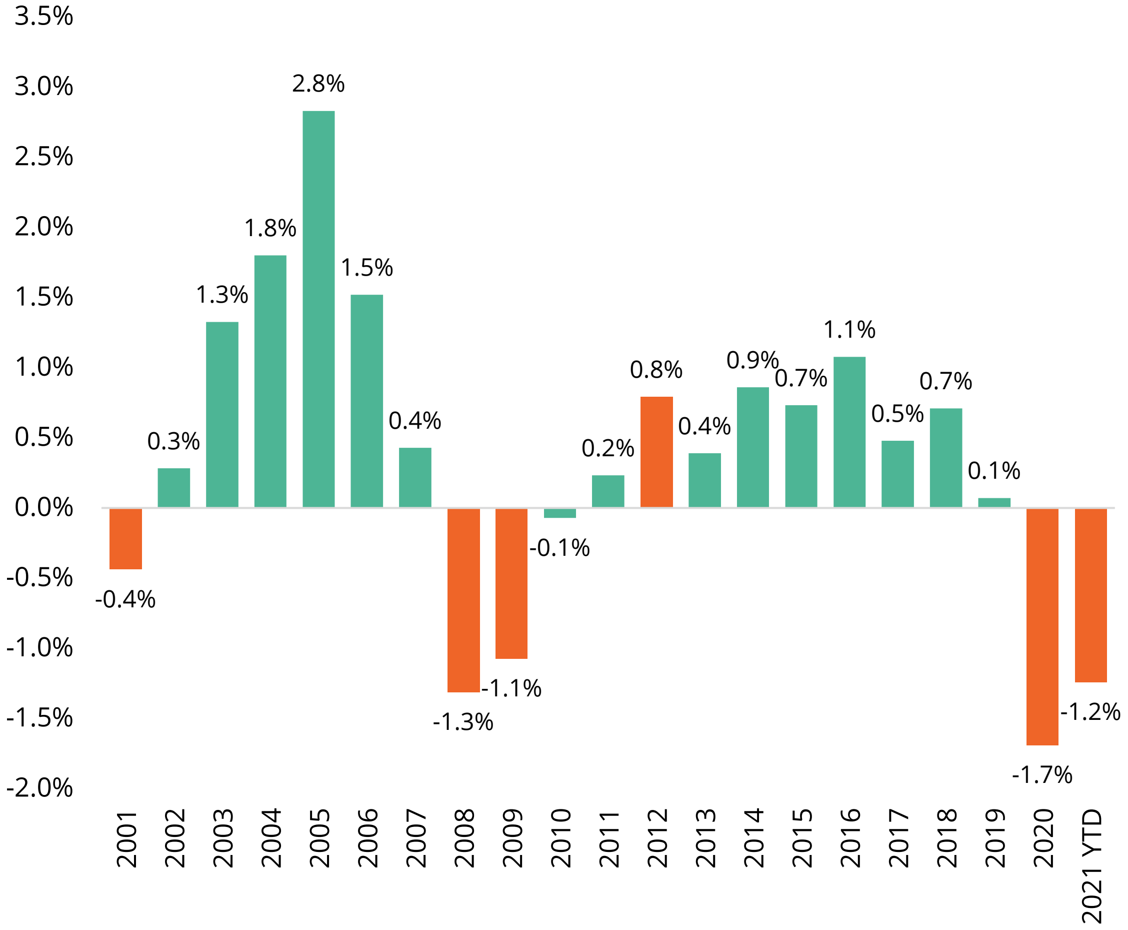
Net absorption is improving

-1.7 to -1.2%

Net absorption as a percentage of inventory in 2020 and 2021 YTD

Occupancy losses from 2020 to Q3 2021 have totaled 10.2 million sf. These losses surpass the losses of the early 2000's recession (-0.4%) and global financial crisis (-1.1% and -1.3%).



Source: Avison Young

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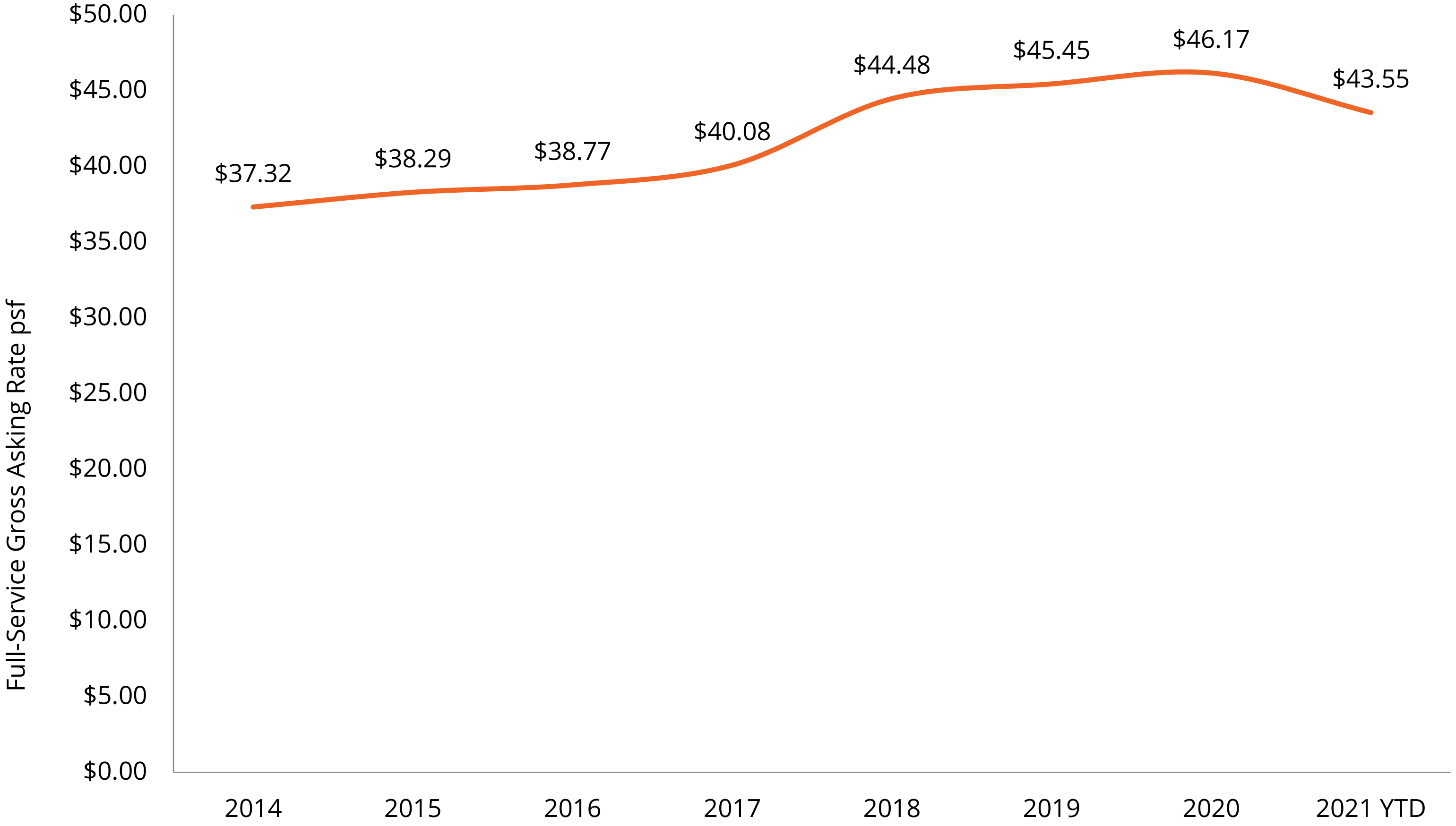
Gross rents are beginning to stabalize

-4.2%

Change in base rents, 2019 to 2021

Base rents have begun to stabilize in Q2 and Q3 2021. Despite a slight drag in gross rents from 2019 to 2021, Trophy Assets held by institutional landlords have held rents at pre-COVID rates given the disproportionate demand at the top of the market.



Source: Avison Young

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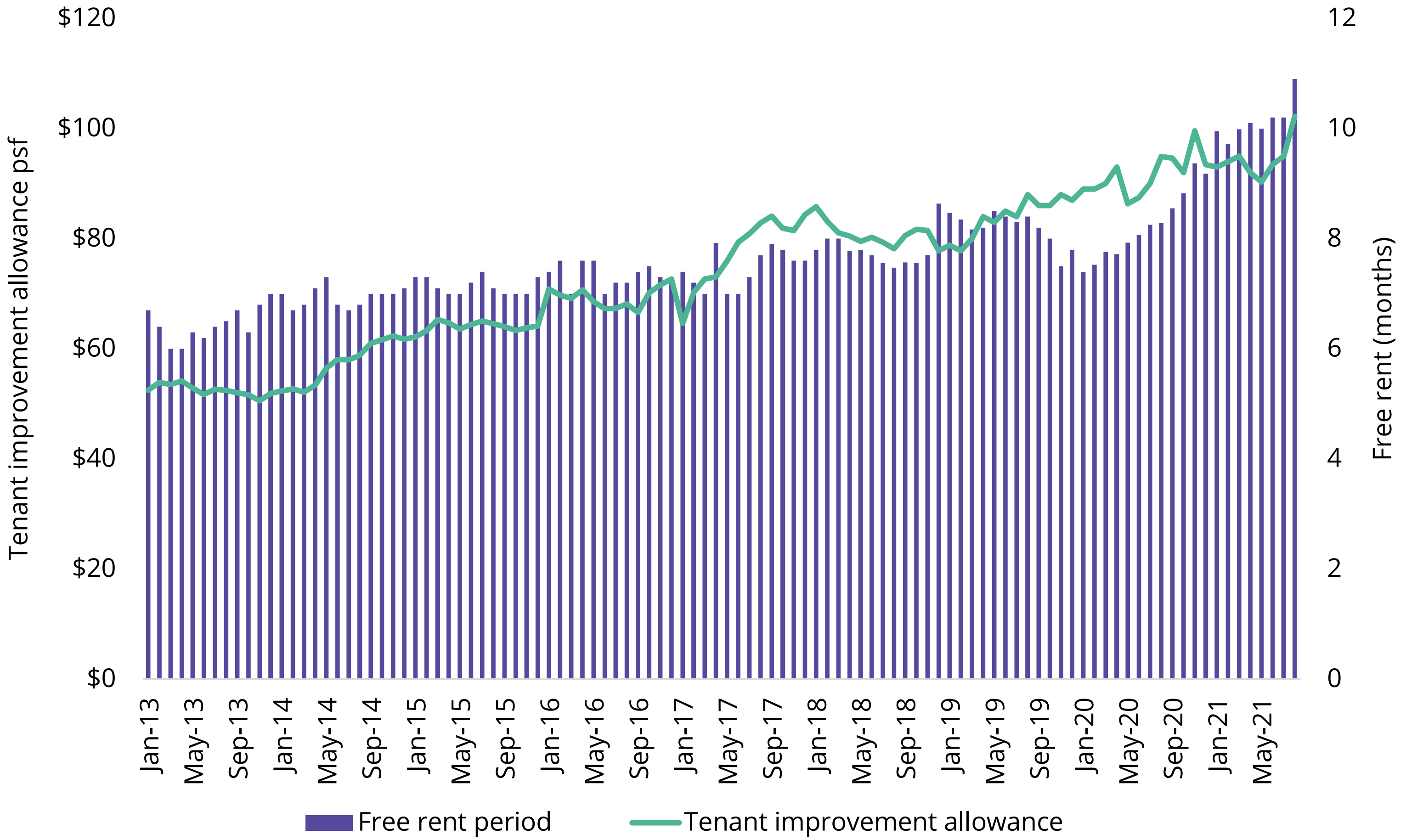
Concessions are still rising

14.0%

Change in tenant improvement allowance amounts, 2019 vs. 2021

Landlords have offered record levels of concessions packages to induce tenants to make long-term commitments, regardless of building location and quality.



Note: Class A office properties.
Trailing 12-month unweighted averages. Excludes subleases, renewals and expansions.
Normalized to 10-year lease terms. Source: Avison Young

Class A economics after the pandemic

Period	Average full service gross rent	Average free rent period	Average tenant improvement allowance	Average net effective rent
2018 to 03/2020	$48 psf	7 months	$78 psf	$40 psf
04/2020 to today	$47 psf	11 months	$102 psf	$35 psf

Note: Class A direct relocations only normalized for 10-year lease terms. Source: Avison Young

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Class B and C economics after the pandemic

Period	Average full service gross rent	Average free rent period	Average tenant improvement allowance	Average net effective rent
2018 to 03/2020	$36 psf	6 months	$55 psf	$30 psf
04/2020 to today	$32 psf	11 months	$91 psf	$23 psf

Note: Class B and C direct relocations only normalized for 10-year lease terms. Source: Avison Young

Los Angeles office construction and development pipeline

142 properties

proposed or under construction

23.6 msf

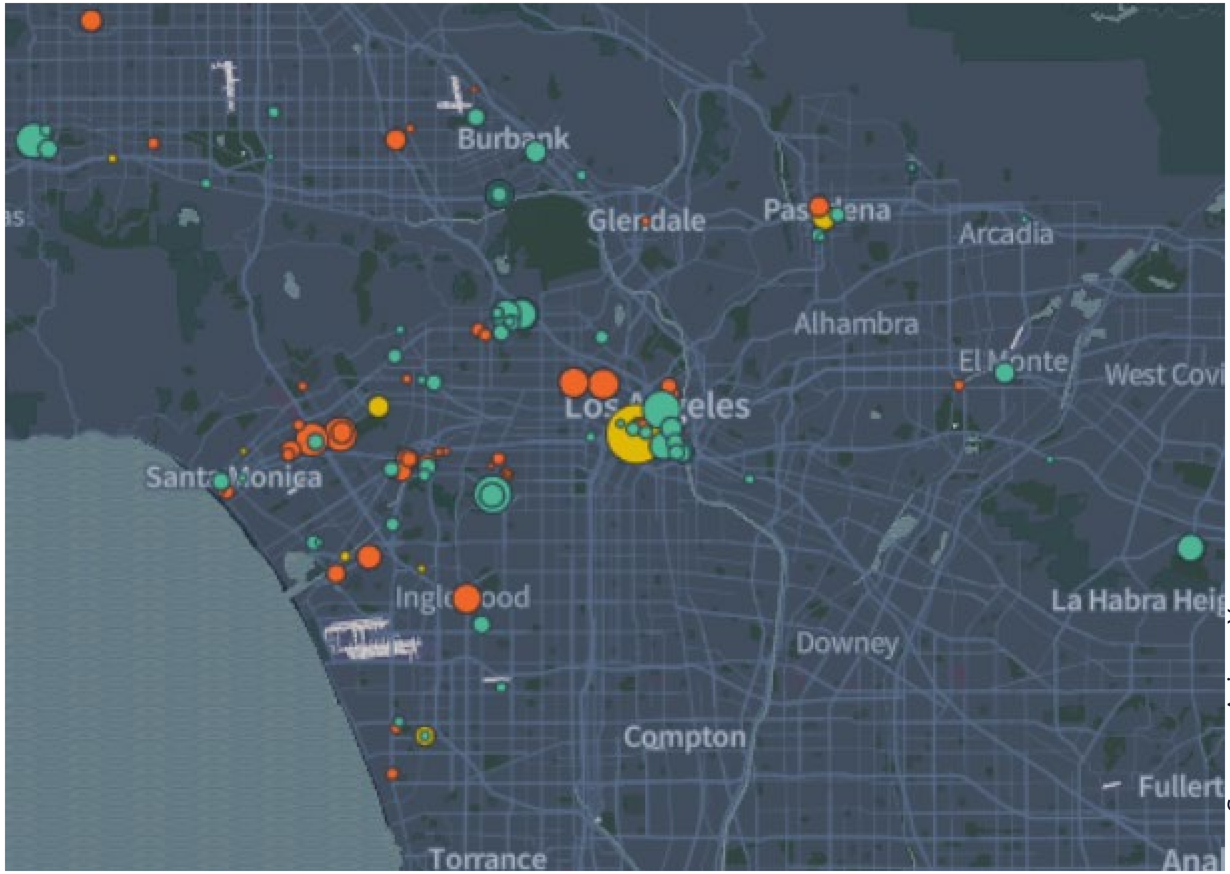
proposed or under construction

7.3%

share of current office inventory

1976

average vintage of existing Los Angeles offices



Source: Avison Young

Under Construction
Under Renovation
Proposed

02.

Capital market conditions

Pricing trended downward and investment activity continued to lag amidst challenging occupier market conditions.

Office investment dollar volume is still well below average

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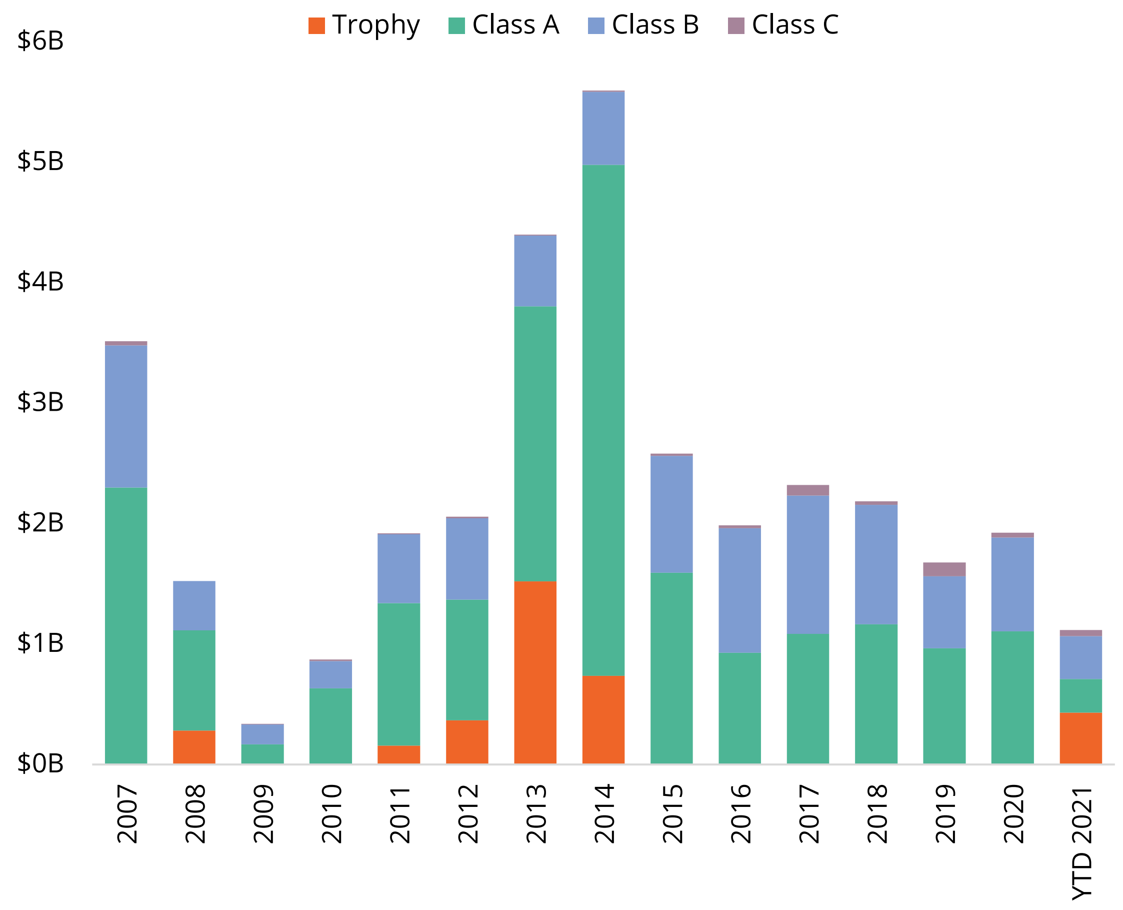
$3.1B

Los Angeles office dollar volume over the past 18 months

Office sales activity has declined during the pandemic due to owners resisting "panic selling," decreasing by 30% compared to the prior five-year average dollar volume.



Source: Avison Young

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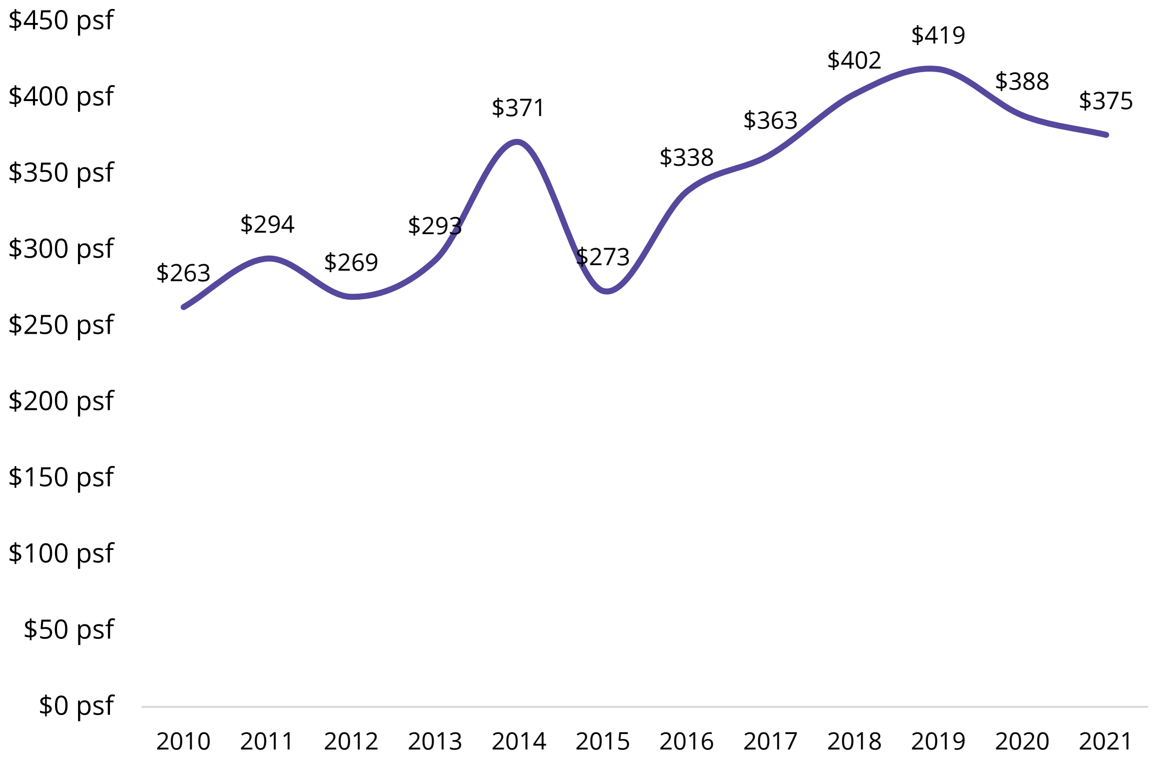
Office asset pricing has softened

-10.0%

Los Angeles office pricing from 2019 to September 2021

Los Angeles office asset pricing continued to slightly trend downward in Q3 2021, reflecting investors' more conservative underwriting approaches given prevailing office occupier conditions. Creative offices have held pre-pandemic prices unlike traditional office properties.



Source: Avison Young

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03.

Economic and demographic trends

Office visitor volumes have lagged those of other representative areas of interest, despite steady underlying employment fundamentals.

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Vaccination rates are increasing but slowing

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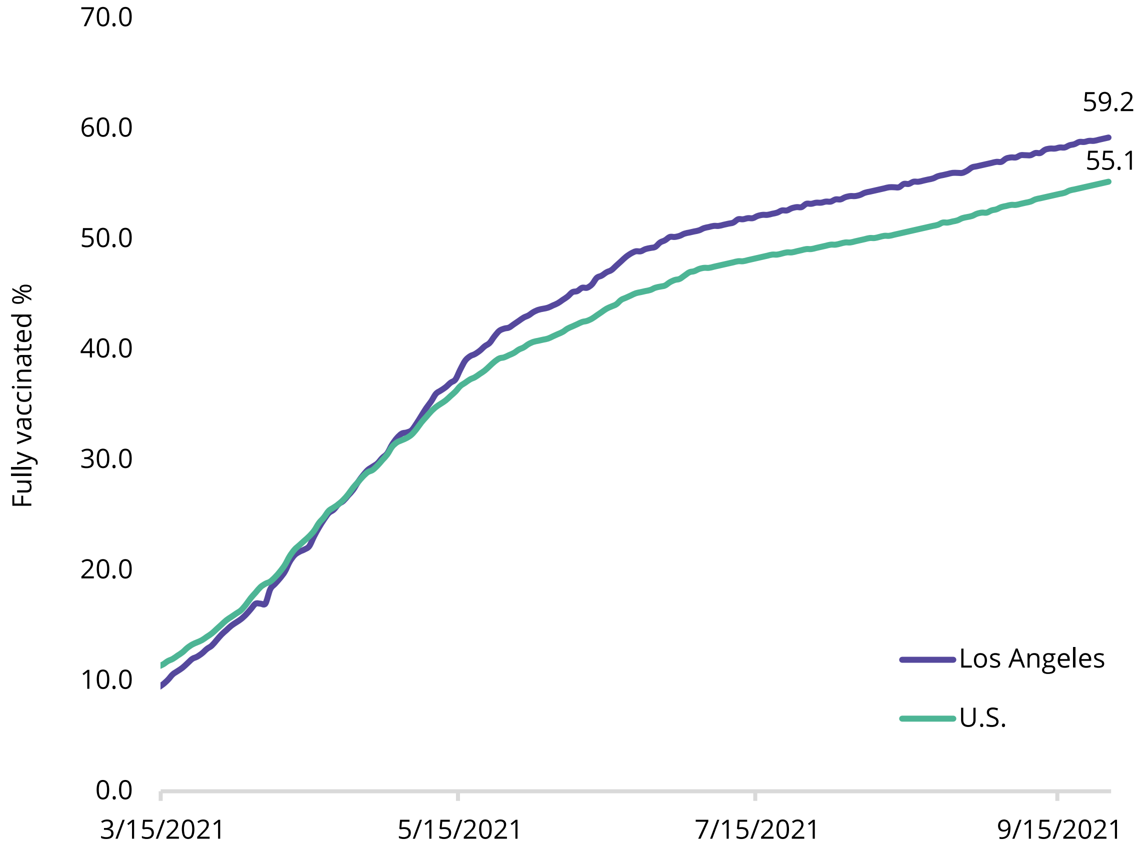
59.2%

Share of total Los Angeles County population that is fully vaccinated

Los Angeles proportionate vaccination rates have slightly surpassed U.S. averages.



Source: CDC

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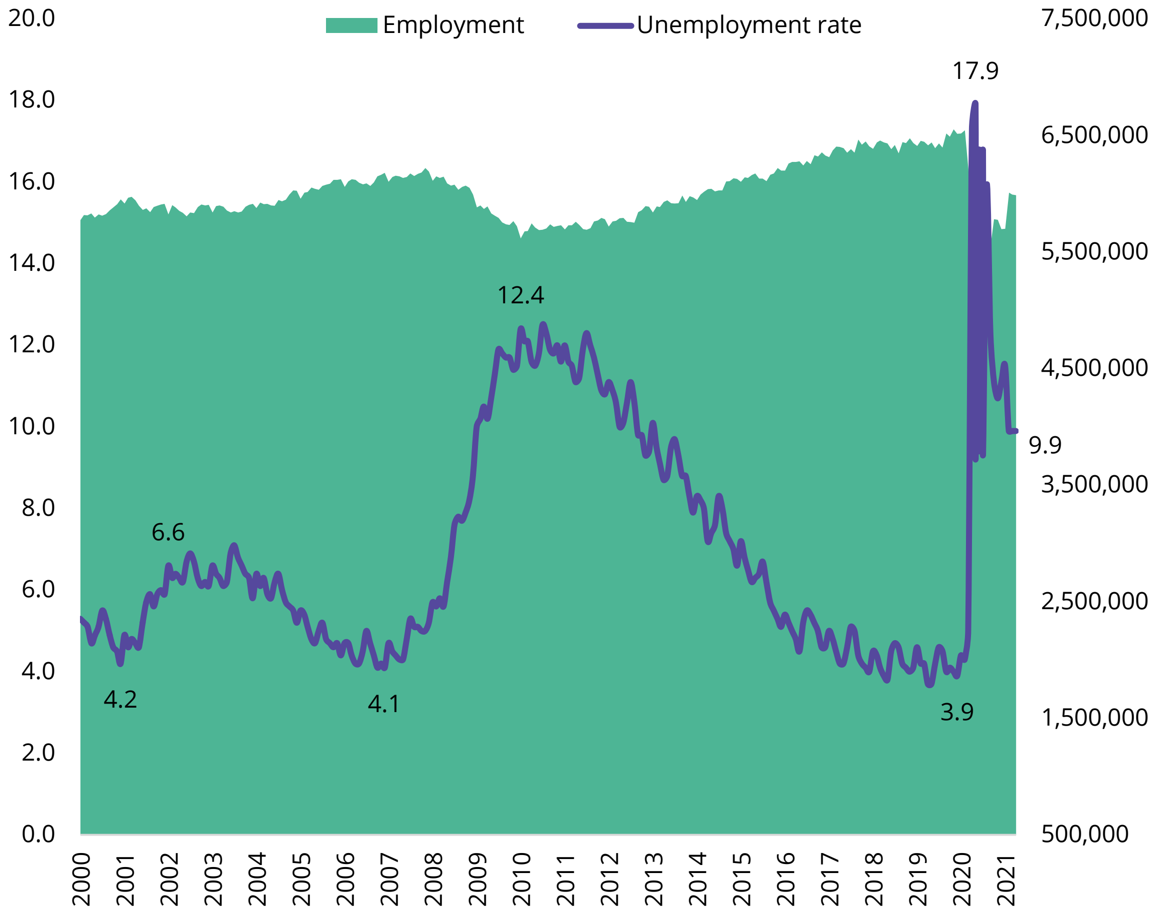
Unemployment rate is still falling

9.3%

Los Angeles unemployment rate as of October 2021, dipping below the height of the financial crisis

Although the unemployment rate is still falling, the pace at which it is falling is slowing. Unemployment dropped 600 basis points quarter-over-quarter, compared to 160 basis points the previous quarter.



Note: Not seasonally adjusted data.
Source: Bureau of Labor Statistics

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Office-using job losses are less severe

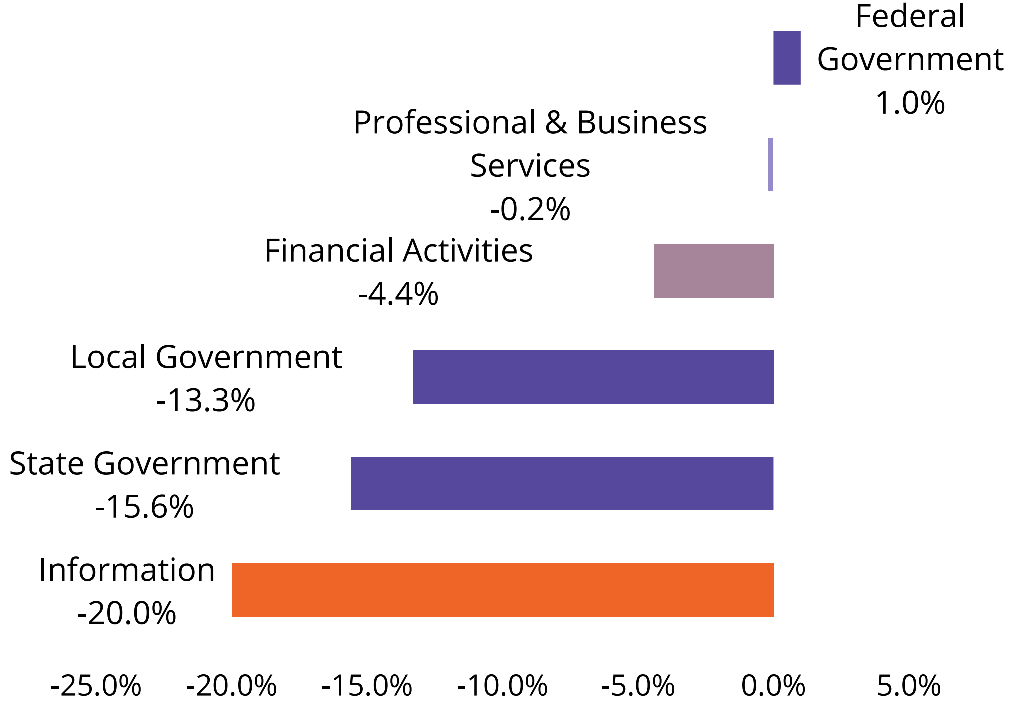
-7.1%

Change in office-using employment during the pandemic

Los Angeles MSA total job losses have declined by 9.1% since the start of the pandemic while office-using jobs contracted by just 7.1%.

Total change in Los Angeles MSA* job gains/(losses)

February 2020 to September 2021



Note: Not seasonally adjusted data. Metropolitan statistical area.
Source: Bureau of Labor Statistics

VIEW DASHBOARD

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U.S. return-to-work rates since start of COVID

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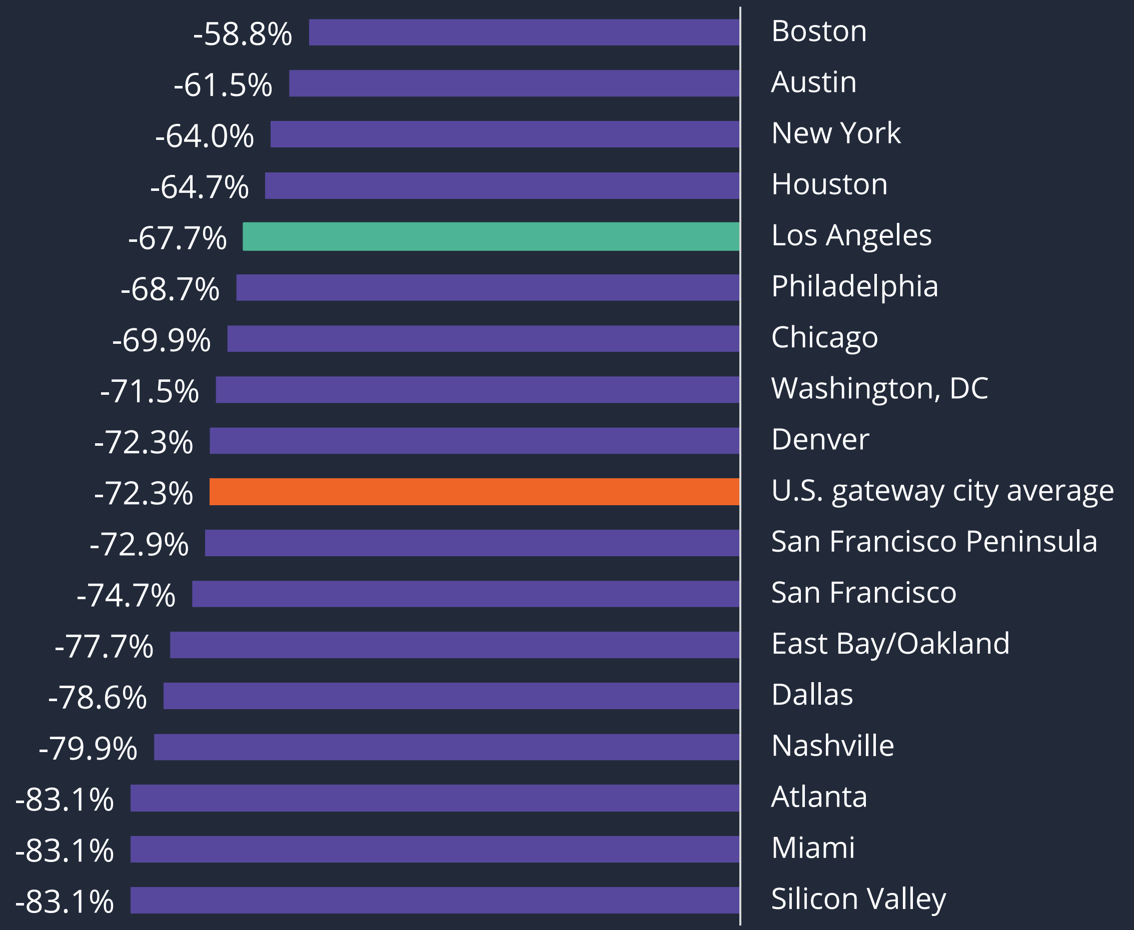
-72.3%

Average office visitor volumes across U.S. gateway cities, March 2, 2020 vs. September 20, 2021

Return-to-work efforts across cities have been influenced by governmental regulations (informed by infection and vaccination rates), office-using industry composition and employees' reliance on mass transit.

VIEW VITALITY INDEX



Note: Representative full-building office occupiers only.
Weekdays only. Data as of September 20, 2021.
Source: Orbital Insight, AVANT by Avison Young

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U.S. return-to-work rates since start of COVID

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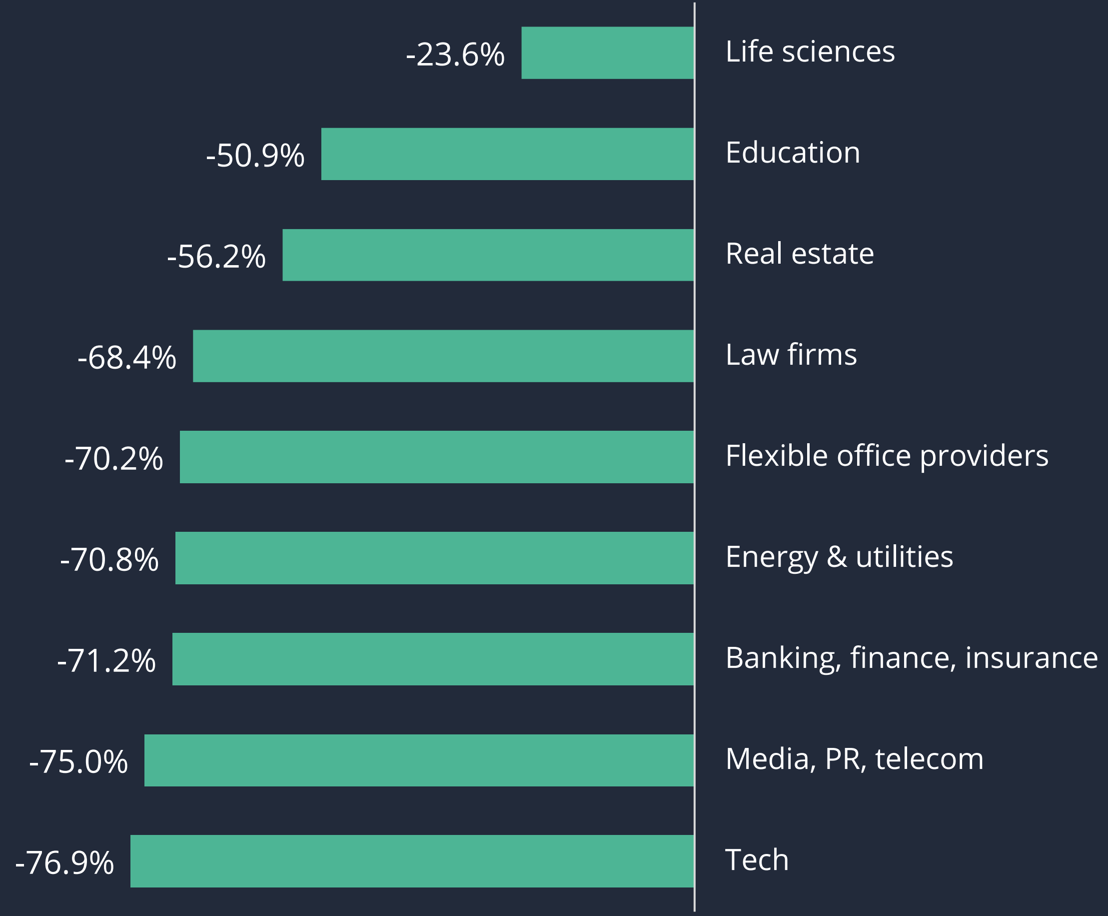
-76.9%

Average tech office visitor volumes across U.S. gateway cities, March 2, 2020 vs. September 20, 2021

Tech companies have adopted remote work strategies more than most major office-occupying industries, while life sciences and real estate companies have embraced flexible in-office and remote working arrangements.

VIEW VITALITY INDEX



Note: Representative full-building office occupiers only. Weekdays only. Data as of September 20, 2021.
Source: Orbital Insight, AVANT by Avison Young

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Local historical visitor volumes

-25.3%

Total visitor volume, September 2, 2019 vs. September 20, 2021

Education (+19.1%) and Healthcare (+2.2%) have returned to pre-COVID activity levels, though office (-59.4%) has lagged all other property types.

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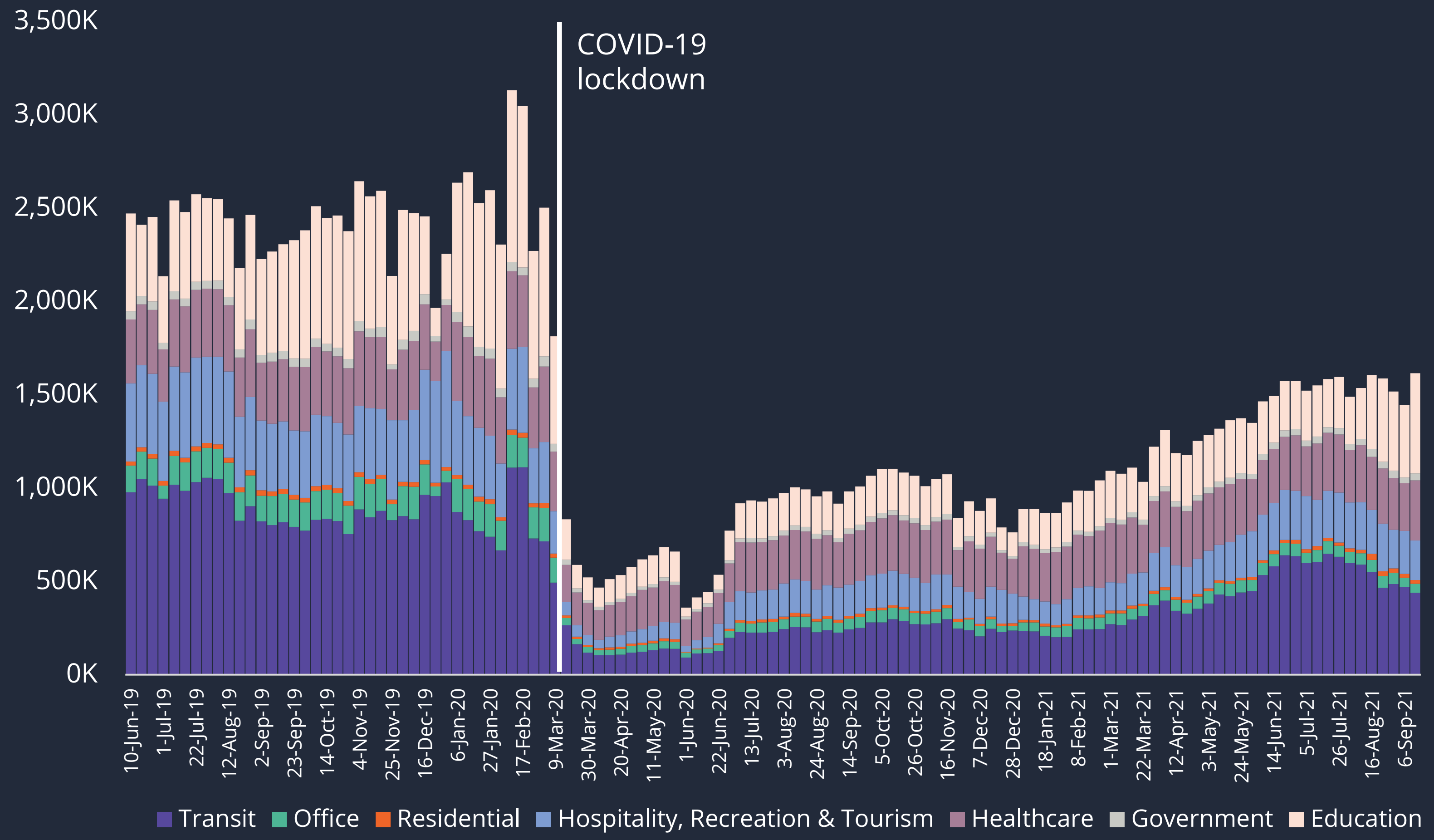

Note: Representative areas of interest. Weekdays only.
Weekly visitor volumes referenced above.
Source: Orbital Insight, AVANT by Avison Young

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Change in local activity levels, 2019 vs. 2021

-69.1% Office	**-42.1%** Retail	**-39.7%** Transit	**-21.6%** Healthcare
-23.2% Education	**-38.2%** Government	**-16.3%** Residential	**-34.0%** Hospitality & Tourism

Note: Select, representative areas of interest only. Weekdays only.
Week of September 16, 2019 vs. week of September 20, 2021.
Source: Orbital Insight, AVANT by Avison Young

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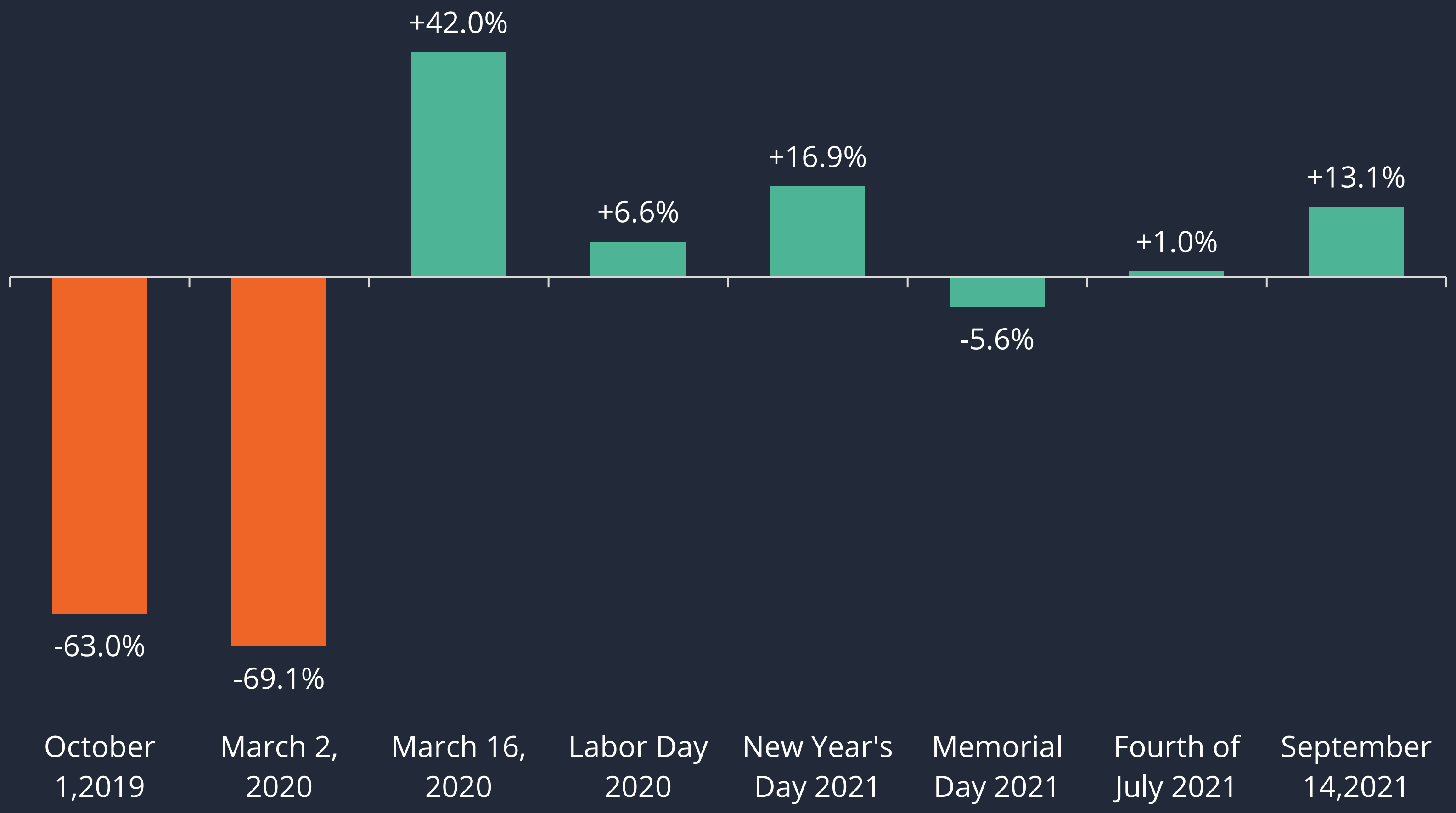
Evolution of local return-to-work efforts

+13.1%

Los Angeles office visitor volume since the Fourth of July 2021

Los Angeles return-to-work efforts to rise throughout 2021, albeit at levels that were lower than previously anticipated earlier the year due to the spread of the delta variant in the summer months.

VIEW VITALITY INDEX



Note: Select, representative occupiers only. Weekdays only.
Data as of September 20, 2021.
Source: Orbital Insight, AVANT by Avison Young

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Submarket Summary

Submarket	Existing Inventory (SF)*	Q3 2021 Vacancy %	Q2 2021 Vacancy %	Q3 2021 Net Absorption (SF)	Q3 2021 Completions (SF)	U/C (SF)	Weighted Avg Asking Lease Rate
Downtown LA	**45,794,522**	**25.1%**	**23.6%**	**(213,891)**	**0**	**1,454,962**	**$3.79**
Bunker Hill	10,119,716	20.9%	19.2%	(77,800)	-	-	$3.96
Financial District	19,536,309	24.4%	22.2%	(181,911)	-	-	$3.68
Greater Downtown	13,682,467	28.8%	28.9%	12,194	-	1,454,962	$3.35
South Park	2,456,030	26.7%	23.5%	33,626	-	-	$3.22
Tri Cities	**30,947,897**	**14.0%**	**14.1%**	**45,309**	**0**	**1,098,373**	**$3.51**
Burbank	10,169,510	5.6%	7.4%	182,250	-	879,373	$3.80
Glendale	8,715,109	18.8%	18.3%	(41,357)	-	-	$3.20
Pasadena	12,063,278	17.5%	16.7%	(95,584)	-	219,000	$3.48

*Inclusive of Class A, B, and C

Submarket Summary

Submarket	Existing Inventory (SF)*	Q3 2021 Vacancy %	Q2 2021 Vacancy %	Q3 2021 Net Absorption (SF)	Q3 2021 Completions (SF)	U/C (SF)	Weighted Avg Asking Lease Rate
West LA	**73,487,552**	**21.2%**	**20.4%**	**(903,407)**	**0**	**2,597,902**	**$4.83**
Beverly Hills	9,905,345	19.1%	18.7%	(41,318)	0	50,146	$5.46
Brentwood	3,994,624	19.4%	18.0%	(58,219)	-	-	$4.39
Century City	10,988,051	14.0%	11.1%	(322,471)	-	-	$5.61
Culver City	7,063,357	18.3%	16.7%	(122,955)	0	389,899	$3.74
Marina Del Rey/Venice	8,993,760	35.3%	34.5%	(351,932)	-	315,000	$5.42
Miracle Mile	4,998,207	27.0%	29.6%	130,361	-	-	$4.02
Olympic Corridor	3,084,110	35.3%	34.3%	(38,514)	-	811,211	$4.51
Santa Monica	12,287,410	18.0%	17.9%	(6,206)	-	73,426	$4.87
West Hollywood	4,967,961	14.4%	13.2%	(60,042)	-	97,742	$4.80
West Los Angeles	1,566,177	25.2%	25.6%	6,628	-	813,208	$3.55
Westwood	5,638,550	20.0%	19.3%	(38,739)	-	47,270	$4.15

*Inclusive of Class A, B, and C

Submarket Summary

Submarket	Existing Inventory (SF)*	Q3 2021 Vacancy %	Q2 2021 Vacancy %	Q3 2021 Net Absorption (SF)	Q3 2021 Completions (SF)	U/C (SF)	Weighted Avg Asking Lease Rate
LA North	**30,511,029**	**16.2%**	**14.7%**	**(457,077)**	**0**	**77,591**	**$2.78**
Calabasas/Westlake	5,629,175	16.0%	13.6%	(132,771)	-	-	$2.53
East SF Valley	3,737,466	9.2%	9.3%	2,613	-	-	$2.62
West SF Valley	5,768,551	13.4%	12.6%	(48,866)	-	-	-
Woodland Hills	10,412,827	16.2%	15.4%	(85,797)	-	77,591	$3.11
Sherman Oaks	3,228,362	22.8%	16.3%	(208,733)	-	-	$2.53
North Hollywood	1,734,648	28.9%	29.8%	16,477	-	-	$2.45
Hollywood/Mid-Wilshire	**27,660,881**	**23.6%**	**23.4%**	**(27,533)**	**61,800**	**850,365**	**$3.24**
Hollywood	7,463,274	25.8%	24.6%	(45,521)	61,800	342,365	$4.69
Mid-Wilshire	20,197,607	22.8%	22.9%	17,988	-	508,000	$2.71

*Inclusive of Class A, B, and C

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Submarket Summary

Submarket	Existing Inventory (SF)*	Q3 2021 Vacancy %	Q2 2021 Vacancy %	Q3 2021 Net Absorption (SF)	Q3 2021 Completions (SF)	U/C (SF)	Weighted Avg Asking Lease Rate
South Bay	**40,436,586**	**22.4%**	**22.6%**	**(40,881)**	**20,000**	**173,878**	**$3.06**
190th Street Corridor	4,551,835	15.3%	14.9%	(20,598)	-	-	$2.47
Torrance	6,225,990	12.9%	13.6%	43,648	-	-	$2.73
Downtown Long Beach	6,202,660	18.7%	18.7%	4,793	-	-	$2.41
Suburban Long Beach	6,418,726	17.3%	16.4%	(77,442)	-	-	$2.56
El Segundo	13,109,807	28.4%	29.4%	17,800	20,000	173,878	$4.18
LAX	3,927,568	39.5%	39.3%	(9,082)	-	-	$2.42
San Gabriel Valley	**18,043,803**	**11.2%**	**11.9%**	**111,438**	**0**	**113,787**	**$2.23**
East San Gabriel Valley	10,407,518	10.8%	11.6%	79,405	-	20,627	$2.23
West San Gabriel Valley	7,636,285	11.8%	12.3%	32,033	-	93,160	$2.24
LA Market Total:	**348,762,347**	**18.2%**	**17.8%**	**(4,316,225)**	**81,800**	**6,366,858**	**$3.62**

*Inclusive of Class A, B, and C

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Looking forward

Here’s what we can expect

- Leasing demand is **unlikely to return to pre-COVID levels** in the near term until office occupiers return to the office en masse through which they can determine their long-term occupancy strategies. Labor Day 2021 was originally the effective return-to-work timeframe, though the spread of the delta variant largely postponed those efforts. These shifts underscore the prevailing uncertainties as space occupiers navigate an unprecedented change in workplace strategies.
- **Tenants are expected to retain leverage** in most lease negotiations, except for top-of-market properties that have benefitted from flight-to-quality and ease-of-accessibility trends.
- **Traditional office asset pricing is poised to continue to soften**; however, the sizable spread between investment yields and benchmark rates and lower pricing could attract new capital sources, especially for cash-flowing properties.

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Get in touch

Christopher Hart

Data Analyst
+1 781 775 6675
chris.hart@avisonyoung.com

Artree Maharajh

Senior Insight Analyst
+1 949 430 0685
arty.maharajh@avisonyoung.com

Carl Caputo

Global Practice Lead, Data Science
+1 202 508 5284
carl.caputo@avisonyoung.com

Christopher Cooper

Principal, Regional Managing Director
+1 213 935 7435
chris.cooper@avisonyoung.com

Jonathan Larsen

Principal, Managing Director – DTLA
U.S. Executive Committee, Los Angeles
+1 213 471 1069
jonathan.larsen@avisonyoung.com

Christopher Bonbright

Principal, Managing Director – LA North & West LA
+1 323 603 5093
chris.bonbright@avisonyoung.com

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Let's talk

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