RADIUS® Commercial Real Estate

Insight

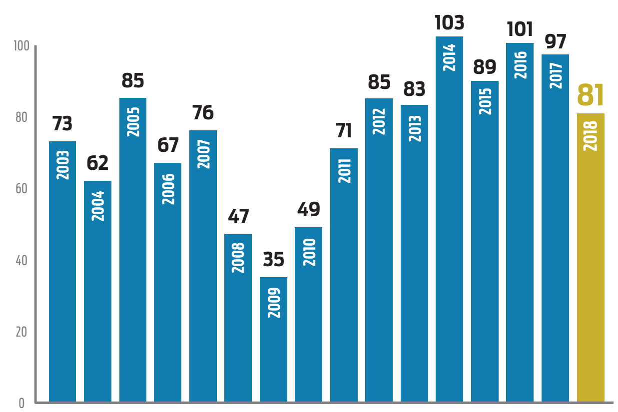
Q4 | 2018 SOUTH COAST MARKET REPORT

Commercial Sales Summary

Sales numbers down. Market sees some adjustments, remains steady.

As we predicted in our reporting during the year, the total number of commercial sales for 2018 came in well under the all-time highs we've seen during the past five years. In the 4th Quarter there were 24 sales including one agricultural (read: cannabis) property. While this was two more transactions than Q4 2017, total deals in 2018 amounted to only 81 versus 97 in 2017, a 16.5% decrease. Part of this decline can be attributed to the catastrophic December and January events on the South Coast which resulted in lower sales during the first and second quarters. However, it should be noted that we still surpassed the prior-15-year average of 75 sales per year. We also should not rush to speculate that this softening in sales activity portends anything ominous. As noted in our Q3 report, in actuality we may simply be witnessing a balancing of the market.

2018 SOUTH COAST COMMERCIAL SALES



Excluding sales of apartments. Prior 15-year average = 74.9 sales/year.

Breaking down these 24 fourth quarter sales by category, three were land, five industrial, 11 office (including five office condos in one complex), three retail and two hospitality (hotels). One interesting observation is that half (12) of Q4 sales could be considered owner-user transactions (i.e. the buildings or land will ultimately be occupied by the buyer) while only 20% of the traded properties were purchased as leased investments. As interest rates increase and DCR's thin, continue to look for owner-users to make up a larger portion of buyers than in years past.

Total sales volume for all of 2018 was $350MM (not including the $87.5MM sale of the Hyatt Centric Santa Barbara Hotel, as such large hospitality sales can skew the data) compared to $354MM sales volume in 2017. That translates to roughly $3.65MM per sales transaction for 2017 versus $4.3MM per deal for 2018. Clearly there were some larger deals in 2018, especially in the fourth quarter. Q4 notable sales include the $27MM multi-tenant industrial/office property at 75 Robin Hill Rd.; the 5-parcel subdivided land/development deal in the Cabrillo Business Park slated for flex/R&D buildings (listed at more than $26MM); the $11.6MM sale of the National Guard Armory to Santa Barbara Unified School District, and the $27MM sale of the soon-to-open Target store in the former Galleria building at the corner of State and La Cumbre (purchased at $794/SF and a 4.79% cap rate). Since we typically don't see this many large properties come to market over the year, that's probably a high water mark for a single quarter's sales.

Sold | 5 Land Parcels, 6700 Block of Hollister Avenue, Goleta (Cabrillo Business Park) | 11.36 Acres | Listed at $26 Million

So, along with our nose to the ground, what does all this tell us about the future? First, there is still a lot of cash available for the right deals, but investors are more skeptical about projected returns since rents have recovered and may not have much upside

Commercial Sales Summary Continued on P.2

Commercial Sales Summary

Continued from P.1

Sold | 3891 State St., Santa Barbara
Retail | 34,000 Sf | $27 Million (Target)

in the immediate future. Consequently most of these acquisitions are for the long term and are more strategically designed for future value due to location, utility or development value down the line. Even though many of the deals are cash heavy on the front end, interest rates continue to become more of a factor when determining what a market capitalization rate should be. While we really haven't seen a lot of examples yet, cap rates are expected to trend upward for occupied investments.

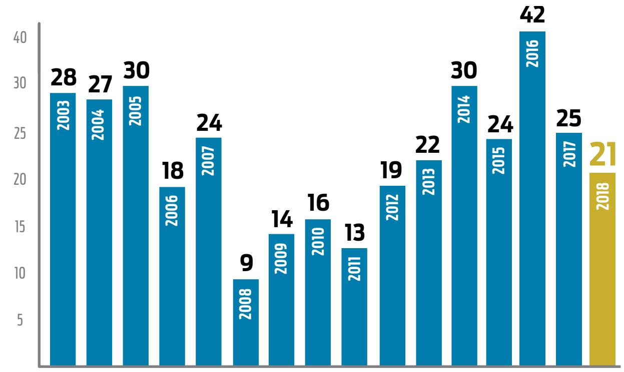
Ultimately, we believe we are starting to see more of a buyer's market evidenced in part by an increase in the number of price reductions for both commercial and multifamily property. Investors and banks may no longer be satisfied with values based on higher future projected rents, so the market seems to have plateaued and rising interest rates are making it more challenging to meet banks' required DCR's. This translates to more money down or lower sale prices. Perceived risky investments like vacant buildings or land may also be driving some sale prices downward, no doubt a result of higher construction prices. We are beginning to see the trend of an overall market adjustment. Such shifts in the market are by no means catastrophic and are not uncommon, particularly after an extended economic expansion and the boom in sales activity we've seen over the past several years.

Multifamily Sales Summary

Santa Barbara South County

No doubt 2018 was a relatively slow year for multifamily investment sales in the South County. The effects of the twin natural disasters from last December and January certainly impacted all commercial real estate sectors at the beginning of the year. That coupled with the continued trend of low inventory, we tallied just 21 total sales of multifamily properties 5+ units in size during 2018, four fewer than 2017 and well below 2016's record 42 sales. Still, the year did end on a positive note with seven (7) sales of properties 5+ units in size during Q4. All said, the multifamily investment market throughout the Central Coast has held steady and looks to stay that way in 2019.

2018 SOUTH COUNTY MULTIFAMILY SALES



Sales of Multifamily properties 5+ Units in size

Sold | The Marc, 3885 State St., Santa Barbara
89 Units | $56.2MM (Off Market)

Even though interest rates are the highest they have been in some time, they are still relatively low and lenders are poised to compete for business. Apartments remain an extremely attractive category for real estate investors on the Central Coast, especially in South Santa Barbara County where the appealing California coastal lifestyle is a huge draw for renters who may not be able to (or choose not to) afford the area's pricey real estate.

Nationally, the apartment vacancy rate was flat during 2018, with Q4 finishing at 4.8%, unchanged from Q3. This time last year it was 4.6% and at year-end 2016 it was 4.2% (*Reis Dec. 21, 2018). Robust demand for apartments remained strong throughout 2018, helped by limited construction and high home prices. Job growth should remain healthy in 2019 and apartment demand should also remain consistent.

Multifamily Sales Summary Continued on P.3

Multifamily Sales Summary

Continued from P.2

The South County apartment vacancy rate continues to come in well lower than the national average, hovering around 2%, where it has been for some time. Locally, rents continue to remain level with a one-bed apartment going for $1,700–$1,925, depending on location.

While Isla Vista continues to be a blue chip area for investors, buoyed by UCSB's perennial drawing power and a near-zero apartment vacancy rate for this popular college community, during Q4 we saw just two (2) sales of 5+ unit properties.

Q4 Highlight Sales

Off Market — The Marc, 3885 State St., Santa Barbara, 89 Units, $56,212,500 ($631,601 PPU), 12/14/18

1315 Bath St., Santa Barbara, 12 units, $4,650,000 ($387,500 PPU), 11/6/18

7388 Calle Real, Goleta, 10 units, $4,000,000 (Under Construction), 12/11/18

6517 El Greco Rd., Isla Vista, 8 units, $3,400,000 ($425,000 PPU), 11/30/18

114–120 Natoma Ave., Santa Barbara (West Beach), 8 units, $3,145,000 ($393,125 PPU), 12/19/18

North County

With the lack of inventory in South County, investors continue to look to Santa Maria and the surrounding communities for opportunities. There were a total of two (2) sales of 5+ unit properties during Q4. As more businesses continue to move into North County, the rental market will continue to tighten.

Q4 Highlight Sales

127 Agnes Ave., Santa Maria, 13 units, $ 1,860,000 ($143,077 PPU), 11/9/18

215 N. Miller St., Santa Maria, 7 units, $1,262,000 ($180,286 PPU), 10/19/18

Ventura County

The trend continues in Ventura's West County market with high demand and very little inventory, and investors with a strong appetite.

Ventura City apartment vacancy rates will continue to remain low at or below 3.1% countywide. More than 520 homes were destroyed in the city and many homeowners are eager to rebuild. Just one year after the Thomas Fire the Woolsey Fire broke out. Many folks are now renting as they wait to build, creating a very tight rental market.

In short, we see that there are just simply not enough new units to accommodate the new household formation that is happening.

There were just three (3) sales of 5+ unit properties during the quarter in Ventura West, and a total of 20 for the year.

Sold | 86 S. Bryn Mawr St., Ventura
10 Units | $2,650,000

Q4 Highlight Sales

86 S Bryn Mawr St., Ventura, 10 units, $2,650,000 ($265,000 PPU), 12/20/18

1267 Meta St., Ventura, 7 Units, $2,010,000 ($287,142 PPU), 11/21/18

164 S. Laurel St., Ventura, 6 Units, $1,345,000 ($224,166 PPU), 11/7/18

South Coast Leasing Summary

2018 SO. COAST LEASING QUICK STATS

Vacancy

		Q3	Q4
OFFICE	Santa Barbara	6.1%	6.6%
	Goleta	8.3%	9.3%
	Carpinteria	5.3%	2.5%
INDUSTRIAL	Santa Barbara	0.6%	0.6%
	Goleta	5.2%	6.0%
	Carpinteria	3.8%	3.4%
RETAIL	Santa Barbara	3.6%	3.2%

Quarterly Absorption (SF)

		Q4 Available Space	Absorption
OFFICE	Santa Barbara	338,200	*-25,000*
	Goleta	396,700	*-44,200*
	Carpinteria	11,600	13,000
INDUSTRIAL	Santa Barbara	28,700	*-500*
	Goleta	252,900	*-32,300*
	Carpinteria	44,000	5,900
RETAIL	Santa Barbara	337,100	43,300

Avg. Gross Asking Rates ($/SF)

		Q3	Q4
OFFICE	Santa Barbara	$3.10	$3.05
	Goleta	$1.92	$1.98
	Carpinteria	$1.74	$1.63
INDUSTRIAL	Santa Barbara	$2.45	$2.63
	Goleta	$1.69	$1.62
	Carpinteria	$1.62	$1.75
RETAIL	Santa Barbara	$4.37	$4.46

Avg. Gross Achieved Rates ($/SF)

		Q3	Q4
OFFICE	Santa Barbara	$2.77	$3.16
	Goleta	$1.96	$1.85
	Carpinteria	$1.92	$2.15
INDUSTRIAL	Santa Barbara	$1.85	$1.95
	Goleta	$1.84	$1.56
	Carpinteria	$1.50	$1.37
RETAIL	Santa Barbara	$3.99	$3.16

Office

The office vacancy rate in Santa Barbara has been relatively steady over the last three quarters, ending the year at 6.6%. Smaller spaces continue to make up the majority of vacancies in this market, with 83 of the 112 vacant spaces at the end of Q4 being under 3,000 SF in size, representing approx. 135,000 SF or about 40% of total vacant square footage.

The trend continues of startups and general office users seeking creative space that isn't stifled by traditional office layouts. In fact the largest office lease in Q4 involved Invoca taking over the 27,773 SF Sonos space at 419 State St., formerly a retail property before Sonos transformed it. Some smaller office tenants are also utilizing short-term solutions in co-working spaces to avoid often lengthy and expensive tenant improvement processes.

Goleta's office vacancy rate increased from 8.3% to 9.3% during Q4 2018, largely due to the 52,118 SF coming to market at 6500 Hollister as Curvature downsizes locally. The largest lease of the quarter was CenCal Health taking 22,392 SF at 5540 Ekwill Dr. Google leased an additional 8,591 SF at 301 Mentor Dr. giving them a total of 54,649 SF. The strength in the Goleta leasing market was also evidenced by developer RAF Pacifica purchasing five lots at the Cabrillo Business Park including entitlements to build an additional 145,000 SF of premium flex/R&D space in five separate buildings.

Down in Carpinteria, we saw another dramatic shift in office vacancy, not uncommon given the very limited inventory in this submarket. Four active listings total 11,649 SF, yielding a vacancy rate of 2.5% in Q4, far below Q4 2017's 6.9%. Two leases were signed in Q4 totaling just 12,782 SF which absorbed over half the available space at the time. Businesses seeking reprieve from higher rates in Santa Barbara continue to look to Carpinteria for an office location that encourages skilled employees to commute from Santa Barbara and Ventura Counties. As we look ahead, we expect slight increases in lease rates due to low supply.

One noteworthy sale could significantly impact vacancy in the market, as 6384 Via Real was purchased by an investor who may add 24,000 SF to the market. The property housed Northrop Grumman for many years, and the new owner plans significant upgrades for the traditionally industrial building. The nature of tech growth in this market is one factor impacting the transition of some spaces to office, and more owners may decide that is the highest and best use for their buildings.

Industrial

Santa Barbara industrial vacancy fluctuated very little over 2018, with Q4 remaining flat from Q3 at just 0.6%. The average gross lease rate also remained steady, ending 2018 at $1.95/SF. This was a sharp increase over 2017 where the Q4 achieved rate was $1.24/SF. There is very little product at the moment, with just eight (8) vacancies totaling about 28,000 SF. In fact Santa Barbara's industrial market remains the tightest of all asset classes in the South Coast. We feel that rates have stabilized and will remain level throughout 2019.

North to Goleta, the industrial vacancy rate rose steadily over 2018 to end the year at 6.0%. While the average gross achieved rate fluctuated modestly, ending 2018 at $1.56/SF, 2018 consistently saw higher rates than 2017 where the

South Coast Leasing Summary Continued on P.5

South Coast Leasing Summary

Continued from P.4

year ended at $1.36/SF. Smaller, sub 5,000 SF spaces remain scarce while a few larger 20,000+ SF properties account for the majority of the vacancy. Of note, a number of recent above-market rate cannabis leases have taken place, posting over $2.00/SF Gross. These leases may skew the average lease rate for 2019, and the sustainability of that level of rates has yet to be seen. Even with the increase of vacancy we believe that lease rates will remain level over the remainder of this year.

To the south, Carpinteria's industrial market remained strong during 2018 with the vacancy rate at 3.4% to end Q4. Still, vacancy rates were higher than in 2017 when the year ended at 2.5%. This market can fluctuate somewhat throughout the year given limited inventory and just a few larger spaces leasing or coming onto the market, as represented by the current vacancy comprising just two available properties for lease at 44,000 SF total. The average gross lease rate ended at $1.37/SF in Q4, and we believe that lease rates will remain flat through 2019.

Retail

The vacancy rate reduced slightly from 3.6% a year ago to 3.2% at the end of Q4 2018, with available inventory dropping from 375,000 SF to 337,000 SF (80 spaces). Of course a large chunk of this total is the 146,000 SF still-vacant Macy's property in the Paseo Nuevo Mall.

Much of the focus of the retail scene remains the downtown State Street corridor. There were 28 vacant downtown State Street storefronts comprising 216,267 SF at year end 2018. Local landlords are increasingly motivated to fill these vacancies and with fewer retail tenants in the marketplace looking to lease, the average gross achieved lease rate declined dramatically during the year, dropping roughly 28% from $4.36/SF a year ago to $3.16/SF at the end of Q4.

There were 10 leases signed during Q4, comprising 36,436 SF total. The largest lease involved the Fitness 19 gym making their entrance into the South Coast by taking a 19,739 SF space at 187 S. Turnpike Road.

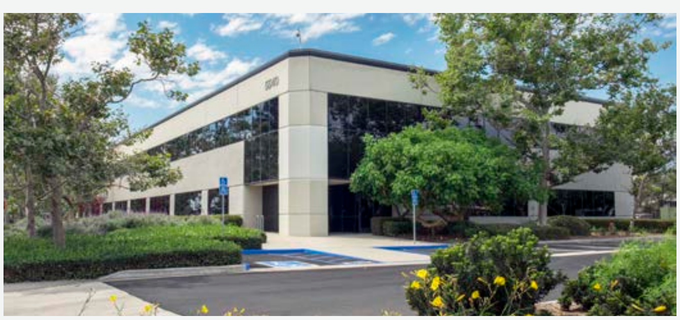
Q4 Leasing Highlights

Leased | 419 State St., Santa Barbara
Office | 27,773 SF

In the largest new lease of the quarter, Invoca, Inc. subleased the former Sonos space, then subsequently signed a direct lease through 2025

Leased | 30 S. La Patera Ln., Goleta
Industrial/Warehouse | 23,000 SF

Leased by Microdyn-Nadir US, Inc. which produces membrane products used in a variety of industries including water processing and water treatment



Leased | 5540 Ekwill St., Goleta
Office/R&D | 22,392 SF

CenCal Health leased the entire second floor at the Santa Barbara Tech Center building in early December

Leased | 6398 Cindy Ln., Carpinteria
Office | 10,167 SF

Agilent Technologies leased this recently improved open office / warehouse space in October

+297

MILLION DOLLARS IN SALES VOLUME

55

COMMERCIAL, MULTIFAMILY & BUSINESS SALES

136

LEASES TOTALING 818,900 SF | +$55 MILLION IN VALUE

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