

3Q24

# Orange County Industrial Market Overview



**NEWMARK**

# Market Observations

## Economy

- U.S. retail sales are healthy but remain below the 20-year average; local industrial leasing activity will remain subdued.
- Orange County’s median household income is the highest in Southern California. Its affluent population of 3.2 million is appealing to warehouse occupiers.
- The International Longshoremen’s Association (ILA) reached a tentative deal with the United States Maritime Alliance (USMX) on October 3, ending a three-day strike at the Gulf and East Coast ports that made national headlines and threatened global supply chains. Gulf and East Coast distributors will continue to shift cargo to other ports of entry until a new contract is signed. Import traffic at Southern California’s ports will remain elevated.

## Major Transactions

- The largest lease of the quarter was a renewal at 3030 Red Hill Ave in Santa Ana for 315,000 SF. The tenant, Astech Engineered Products, has been at the location for over two decades.
- The City of Irvine got approval from City Council to acquire 17300 Red Hill Avenue, an office-to-industrial conversion site in Irvine, for \$96.5 million. The transaction, once completed, will be one of the priciest in Orange County history on a per-square-foot basis (\$880/PSF). The City plans to convert the site into a municipal gym project.
- A Korean cosmetics company, Silicon2, purchased a pair of office and industrial buildings in Buena Park for a total of \$53.3M in an owner-user sale. The 149,000-SF industrial property will serve as a distribution stop for the tenant.

## Leasing Market Fundamentals

- Current leasing activity is slow relative to 2021-2022.
- Net absorption losses persisted for the seventh-straight quarter, with -178,536 SF.
- Vacancy (4.1%) is the highest it has been in over nine years but remains well below the peak of 6.8% from the Financial Crisis in 2008 and one of the lowest across the Southwest region.
- Under-construction activity dropped to 1.9 MSF after three projects totaling 411,711 SF delivered. Two of the three projects are fully leased, which brought pre-leasing levels down to 4.8% of overall construction.
- Office-to-industrial covered land plays are still ongoing. This quarter, the city of Santa Ana approved plans for C.J. Segerstrom & Sons to convert a dated office complex into a Class A industrial park that spans across 313,000 SF.

## Outlook

- Rent declines will be lower than neighboring markets, due to Orange County’s smaller inventory set, and its high-earning consumer base that is appealing to all final-mile distributors. These factors also appeal to developers and investors.
- Sales activity is expected to hold steady, especially within the small-box market where smaller price-tags drive all-cash transactions.
- California Assembly Bill 98, a new bill which regulates warehouse developments in California via guidelines related to building setbacks, facility design features and truck routing plans, was signed into law. Construction and occupancy costs will rise.
- Vacancy will rise in the quarters ahead as some tenants enact cost-cutting measures and new speculative construction delivers vacant.



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1. Economy
  2. Leasing Market Fundamentals
  3. Sales Activity
  4. Appendix

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# Economy

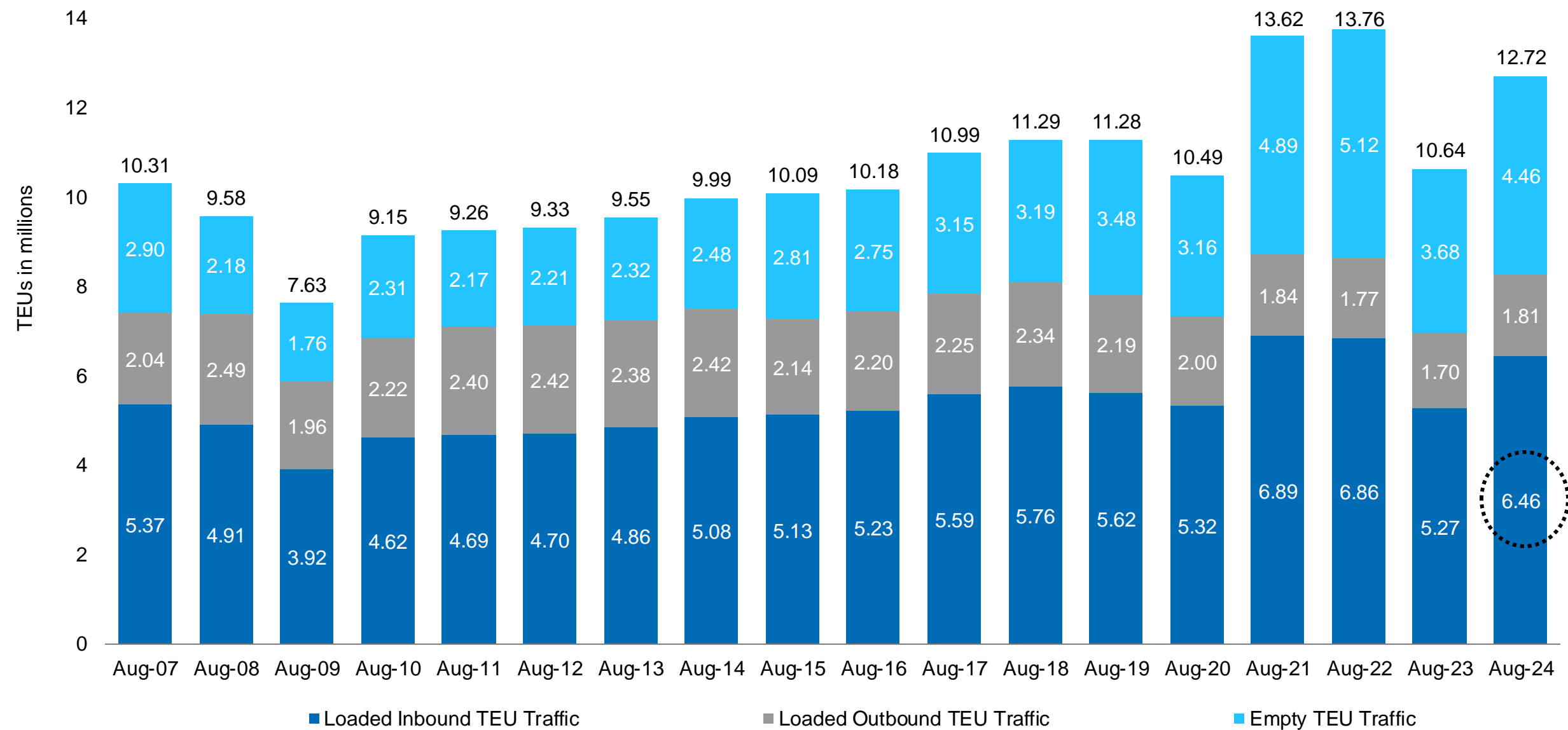




# Loaded Imports in the First Eight Months of 2024 Third Busiest Compared to Same Period of Prior Years

The exceptional (but inflated and unsustainable) growth of 2021-2022 due to COVID-19-related stay-at-home measures, government stimulus, strong retail sales and domestic warehouse occupiers stockpiling goods to mitigate against global supply chain disruptions at the time may have passed, but Southern California's ports are now contending with an influx of imports due to labor issues at Gulf and East Coast ports.

The Ports of Los Angeles and Long Beach: Combined TEU Volume | Loaded Imports, Loaded Exports and Empty Containers | First Eight Months of a Given Year



Source: Newmark Research, The Port of Long Beach and Los Angeles

Note: TEUs are a standard measure for the steel cargo containers commonly used interchangeably on ships, trucks and trains. A TEU or 20-foot equivalent unit is the industry measure used to tally cargo containers, whether the containers are 20-foot long, 40-foot long or some other size.

# West Coast Dockworkers Signed a New Contract in 2023; Their Eastern Counterparts are Next Up...

The ILWU and PMA signed a new labor contract in September 2023, restoring a sense of much-needed stability at U.S. West Coast seaports through late 2029. Longshoremen at Gulf and East Coast ports went on strike for three days in early October after their demands with the United Maritime Alliance were unmet. Now, both sides have a tentative deal in place. Import volume will continue to be rerouted to other North American ports (e.g., Los Angeles-Long Beach) until a master contract is finalized between the ILA and USMX.

## West Coast Ports Agreement Reached; New Contract Good Through Mid-2028

- The International Longshore Warehouse Union (ILWU) represents dockworkers at 29 ports from Washington State to California. The Pacific Maritime Association (PMA) represents ocean carriers and terminal operators.
- The prior contract expired on July 1, 2022.
- The ILWU has a history of work disruptions in prior negotiation periods, ranging from strikes, to deliberate work slowdowns to under-staffing shifts.
- These disruptions have cost major retailers billions of dollars in the past.
- A tentative agreement was reached on June 15, 2023 for what became a new six-year contract. Longshore workers secured a 32% salary increase.
- Many Asian importers pushed inbound goods to East and Gulf Coast ports as talks dragged on. Some of this traffic is returning since stability is now less of a concern.



## East and Gulf Coast Ports Are Up Next

- The International Longshoremen's Association (ILA) represents dockworkers at 36 ports from Maine to Texas. The United States Maritime Alliance (USMX) represents ocean carriers and terminal operators.
- Their contract expired on September 30, 2024.
- Harold Daggett, International President of the ILA, initiated a strike on October 1, 2024 that ended two days later.
- A tentative deal with USMX is now in place, and both sides have until January 15, 2025 to finalize an agreement.
- Job protection from automation and higher pay (a 62% wage increase over six years) for longshore workers are part of the current deal.





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## Import Traffic Has Jumped Since Late 2023 at Los Angeles/Long Beach

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## Truck Dwell Times are Lower Than Rail Dwell Times

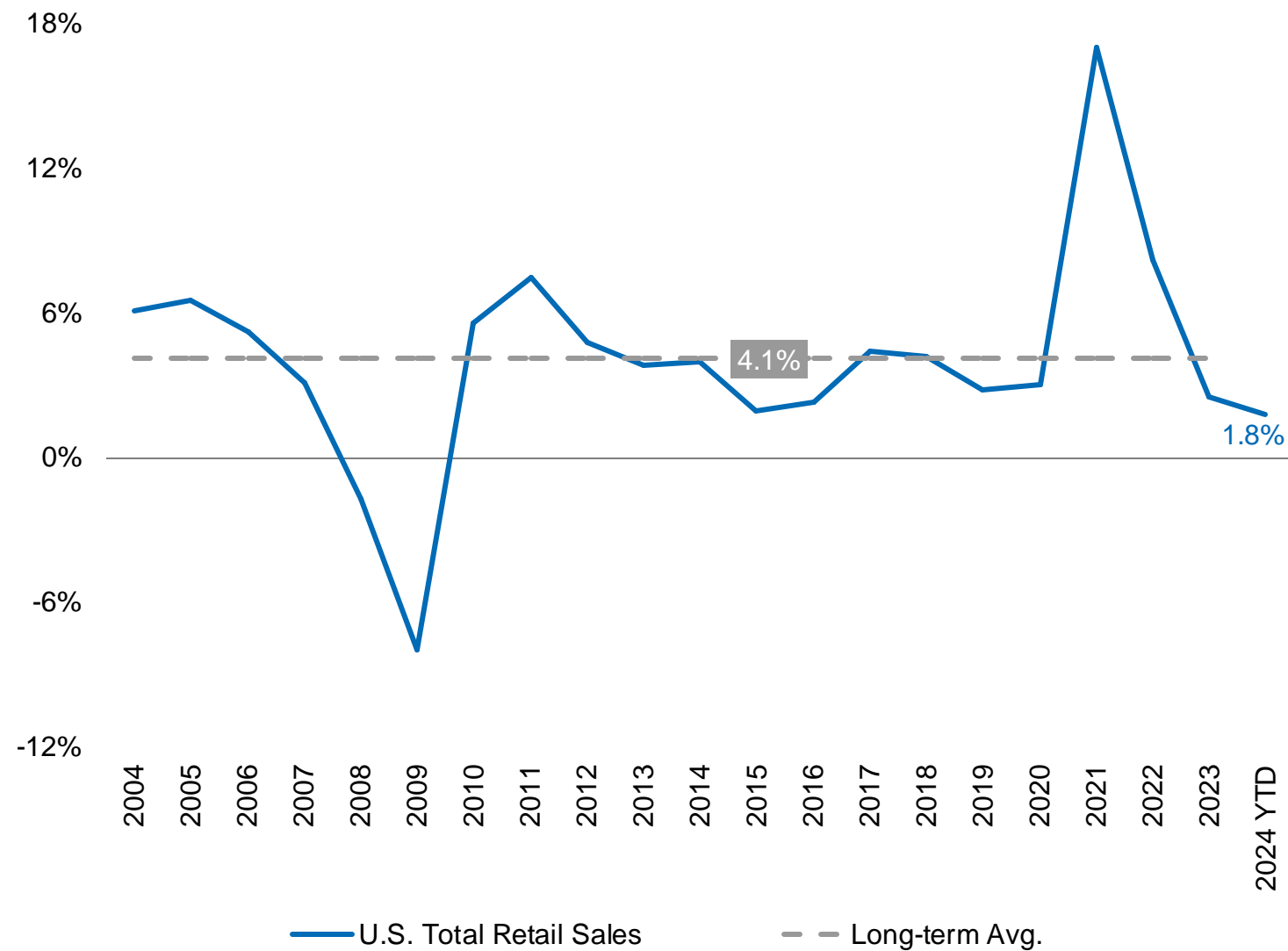
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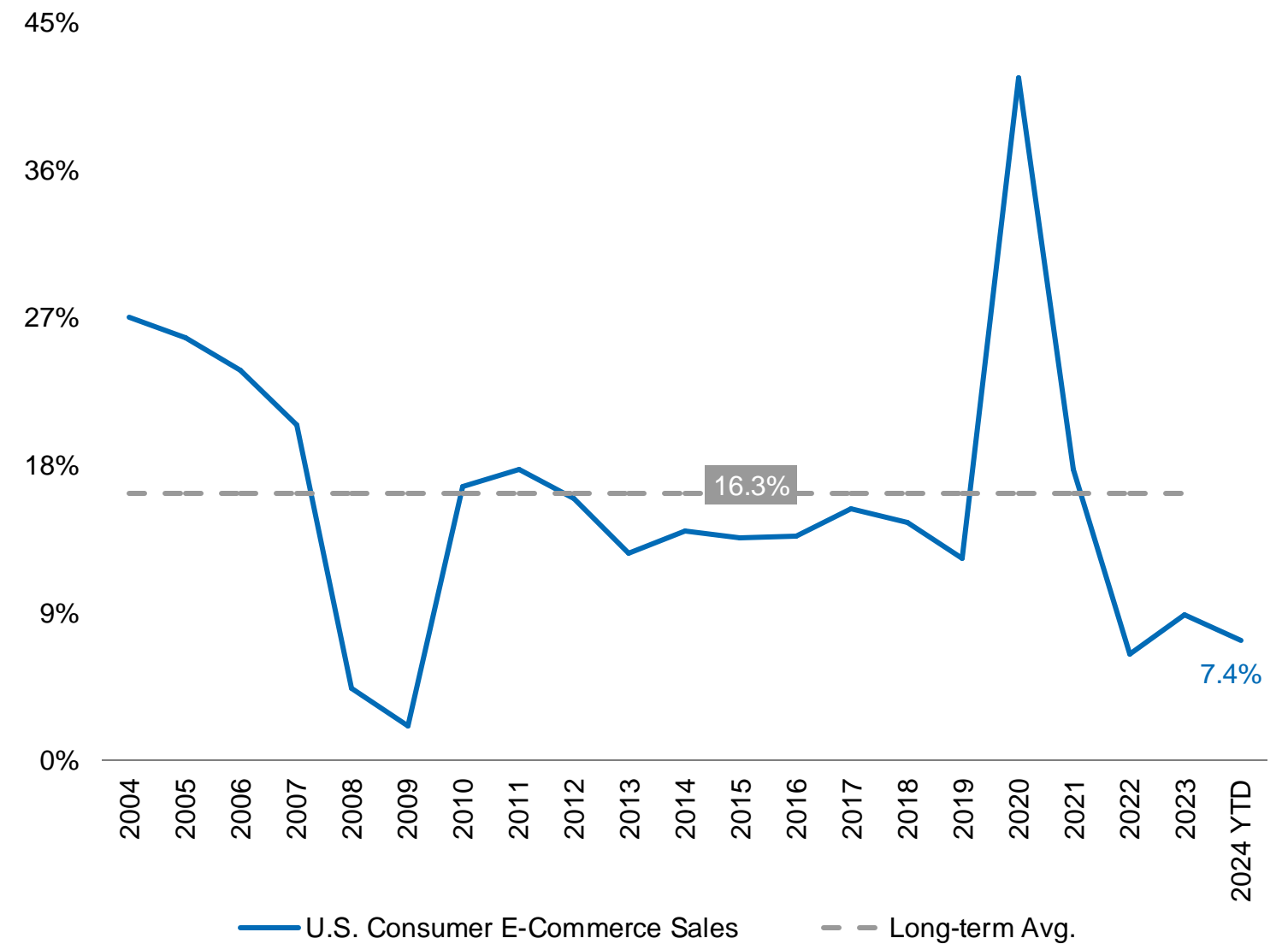
# Retail Sales (an Indicator of Warehouse Demand) Continue to Moderate

Consumer e-commerce sales were up 7.4% in the first half of 2024 compared with the same period in 2023. Although e-commerce sales growth exceeded total retail sales (+1.8% over the same period), the decline from 2021 onward is noticeable as consumer spending registers slower gains.

## U.S. Overall Retail Sales Annual Growth



## U.S. Consumer E-Commerce Sales Annual Growth



Source: US Census Bureau (consumer adjusted retail sales); most current data available  
 Note: 2024 YTD annual growth represents the change in sales from the first six months of 2023 to the same period in 2024.



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# The Pandemic Accelerated E-Commerce Sales Growth and Adoption Rates

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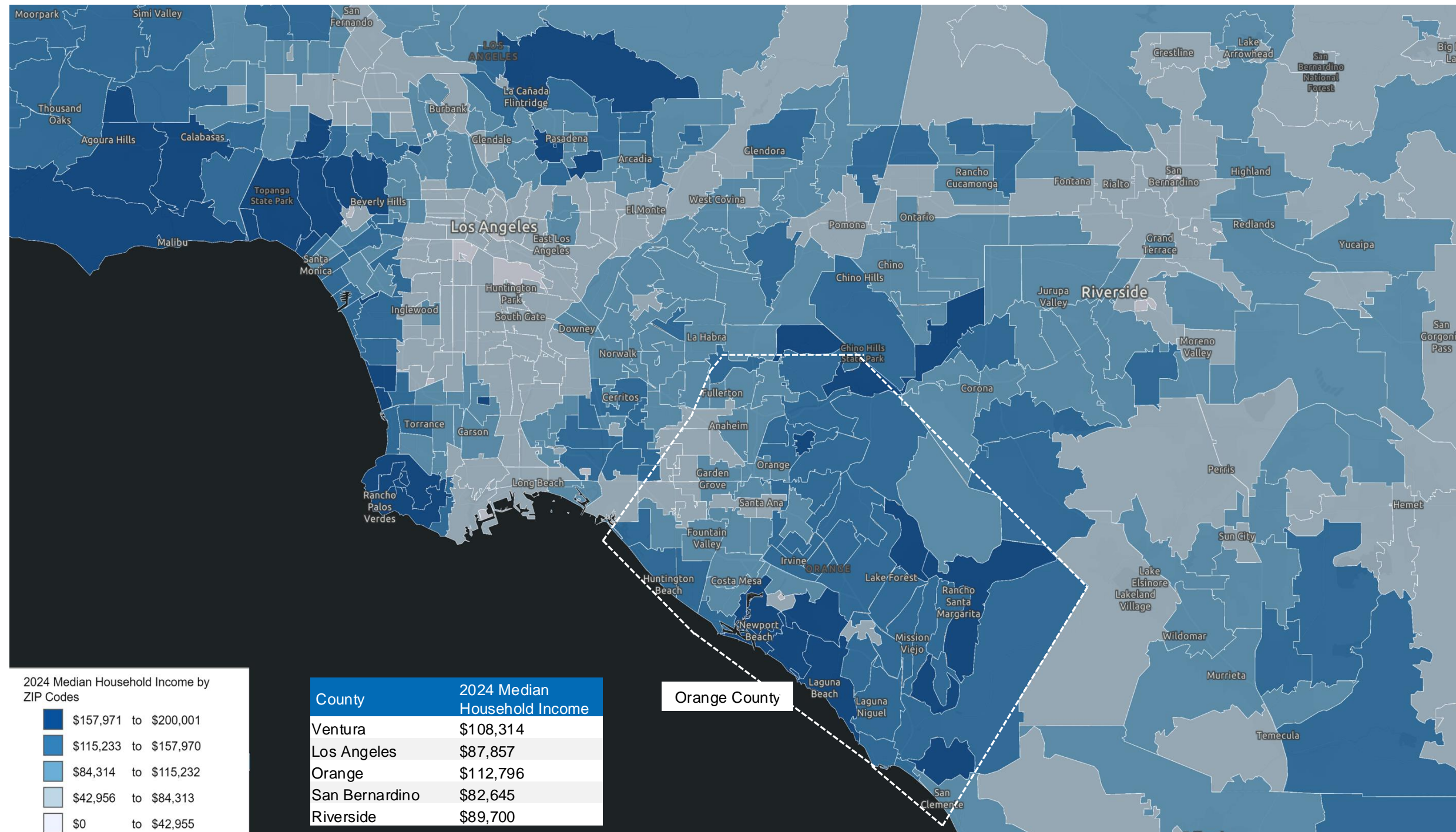
# Orange County Median Household Income Highest In Southern California

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# Orange County is the Most Affluent County in Southern California

Across the greater map: median household incomes are generally higher in coastal and foothill communities.



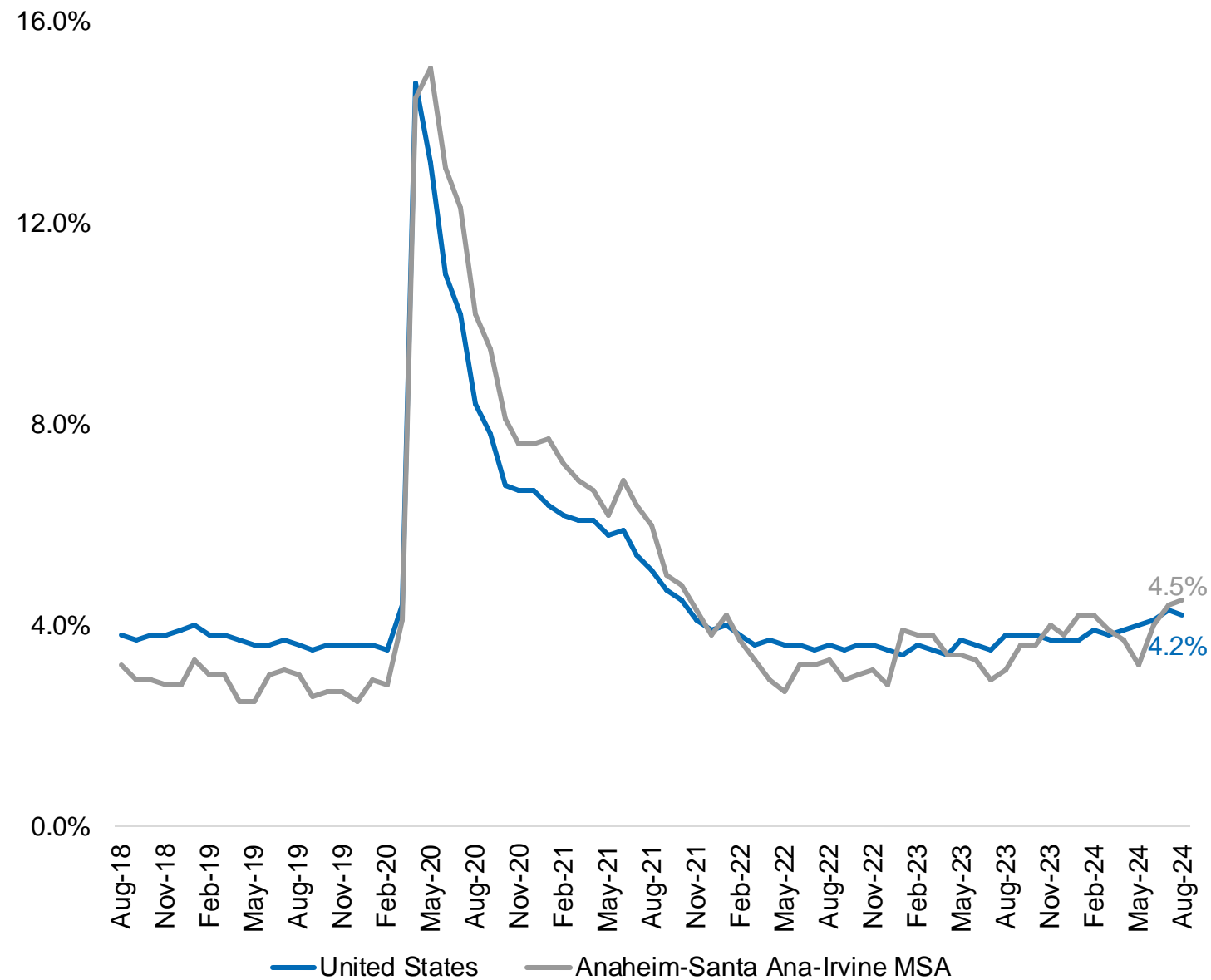
Source: Newmark Research, ESRI



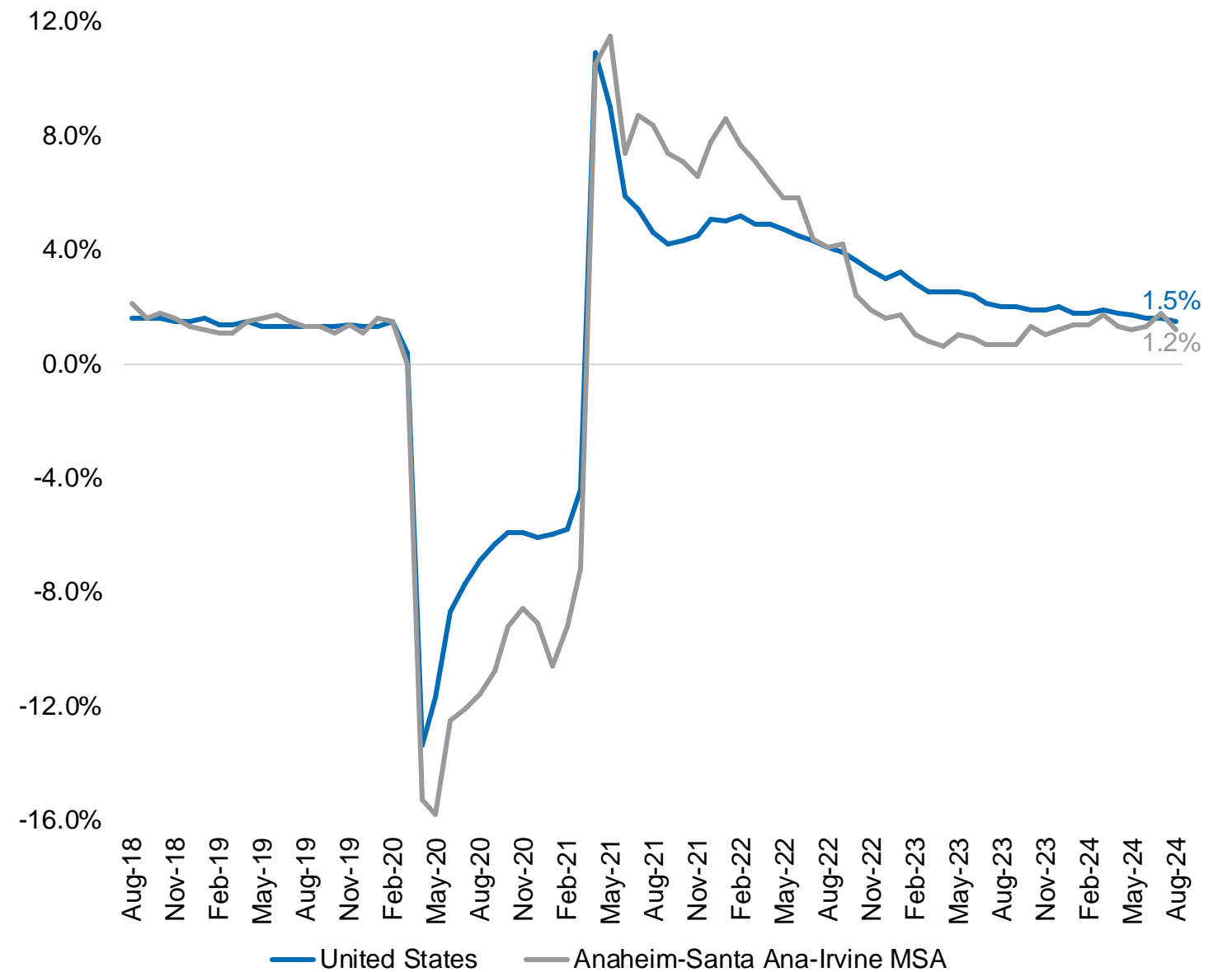
# Local Unemployment Reaches Its Highest Level Since 2021

Orange County unemployment increased by 140 basis points from August 2023 to August 2024 primarily due to businesses implementing workforce reductions as a cost-cutting measure, especially in the manufacturing and information technology sectors. Total nonfarm employment reached record-high levels at the end of 2023 and has remained elevated since.

Unemployment Rate, Seasonally Adjusted



Nonfarm Payroll Employment, Non-Seasonally Adjusted, 12-Month% Change



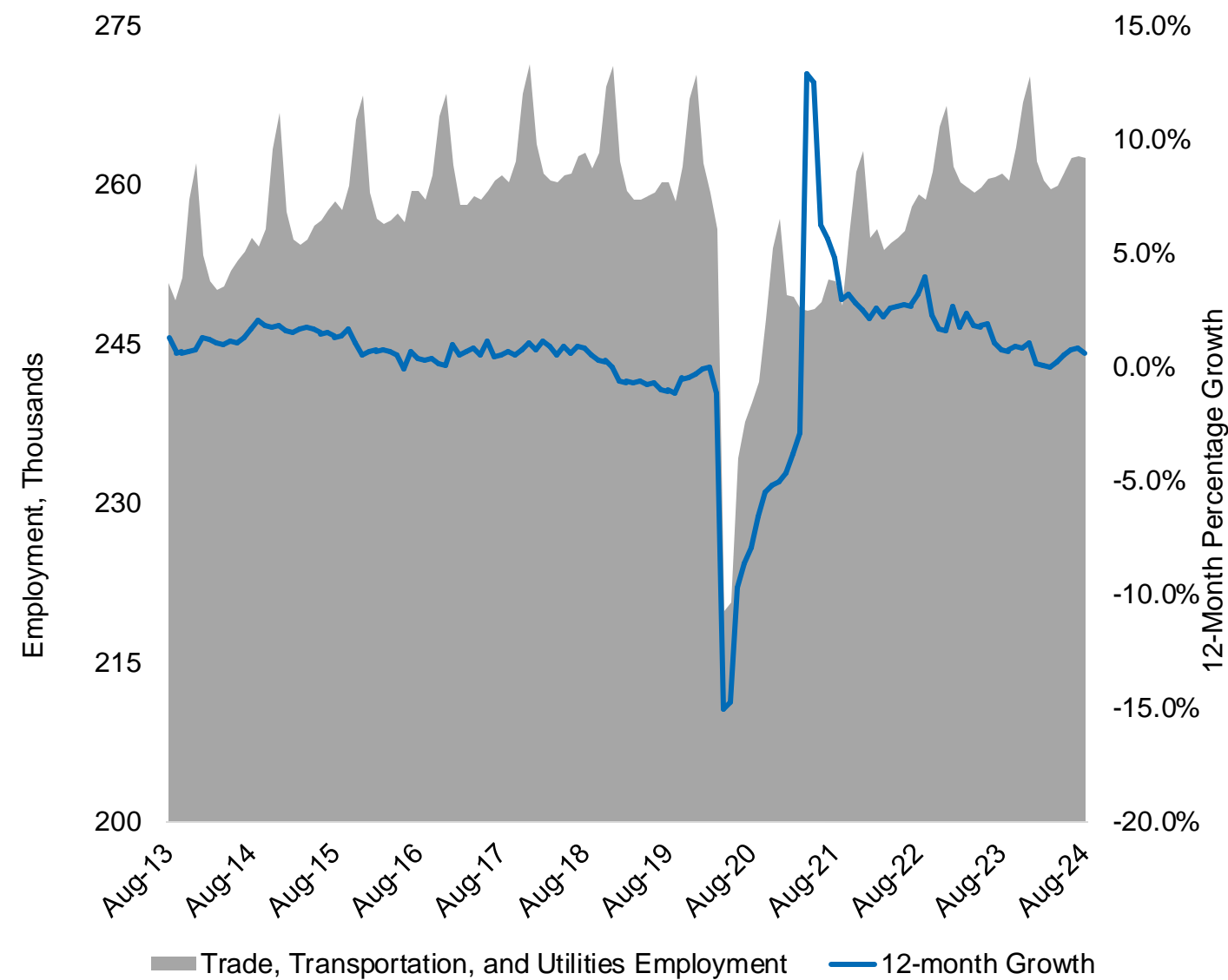
Source: U.S. Bureau of Labor Statistics, Anaheim-Santa Ana-Irvine, CA  
 Note: August 2024 data is preliminary.



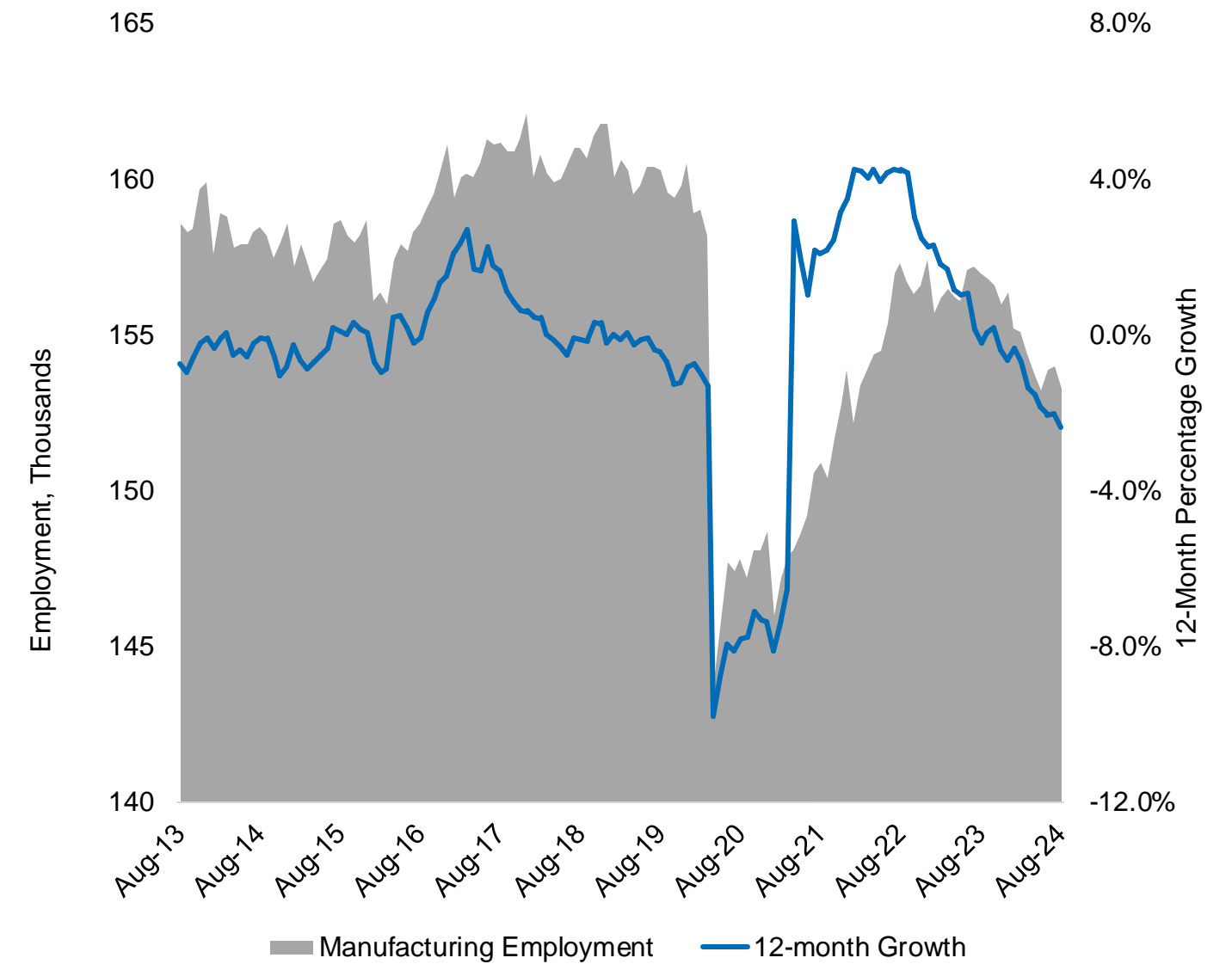
# Manufacturing Sector Driving Down Industrial Employment

The trade/transportation/utilities sector continues to follow a cyclical pattern where local employment peaks in December following the holiday season and drops gradually in the first half of the year. A spate of plant closures has contributed to a continued decline in manufacturing employment over the last year. Given the regionally disadvantageous costs of doing business in California, it is unlikely that the county will recoup these job losses anytime soon.

Trade/Transportation/Utilities Employment and 12-Month Growth Rate



Manufacturing Employment and 12-Month Growth Rate



Source: U.S. Bureau of Labor Statistics, Anaheim-Santa Ana-Irvine MSA  
 Note: August 2024 data is preliminary.



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# Leasing Market Fundamentals





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## Contract Rents Continue to Adjust

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Term Lengths are Moderately Up After Declines in 2022 and 2023

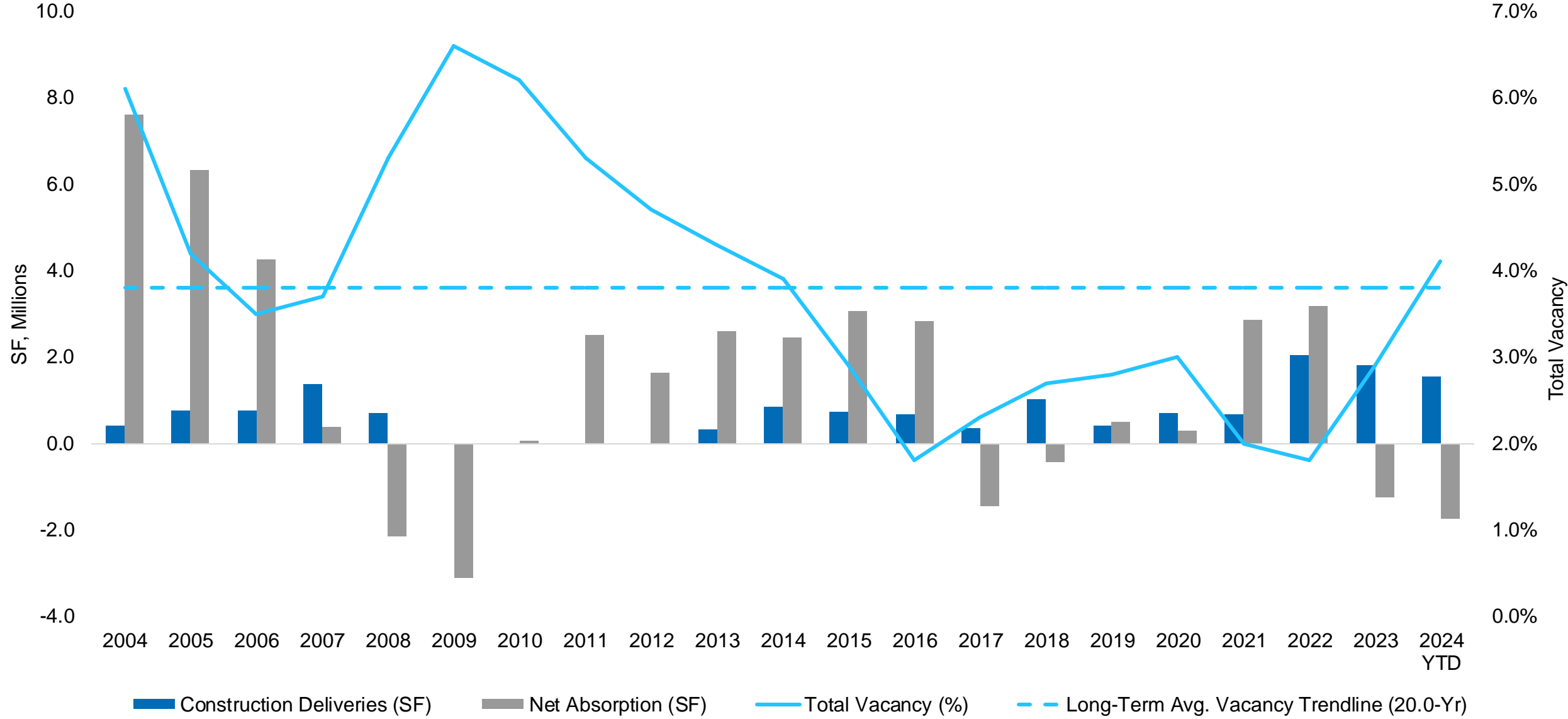
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# Vacancy Reaches Its Highest Level In Nine Years

Net absorption has incurred seven consecutive quarters of net losses, with -178,536 SF this quarter. On a year-to-date basis, nearly 1.7 MSF in net absorption losses was met with 1.5 MSF in construction deliveries, causing vacancy to rise to 4.1%. Current vacancy is higher than the 20-year average.

Historical Construction Deliveries, Net Absorption, and Vacancy



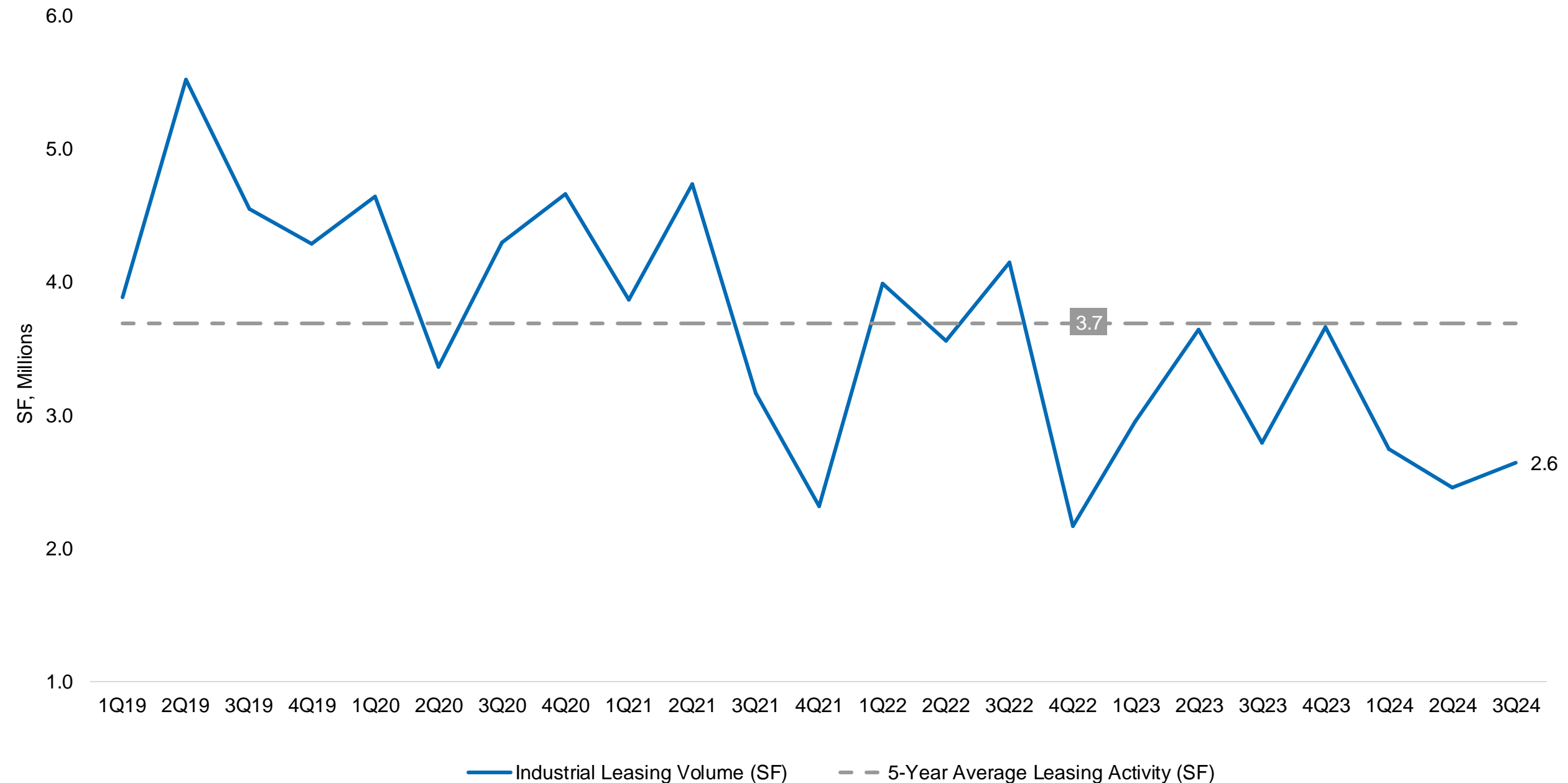
Source: Newmark Research



# Leasing Activity Levels Remain Below Five-Year Average

A few large-block deals marginally improved activity from last quarter, but as a whole leasing volume is still subdued compared to two years ago. Cooling demand and a slowing economy is prompting tenants to downsize, which will lead to lower leasing figures in the quarters ahead. The current economic climate is keeping retail sales in check, while most occupiers are trying to shed overcapacity in their networks to reduce costs. Both have implications for future leasing activity.

## Total Leasing Activity (SF)



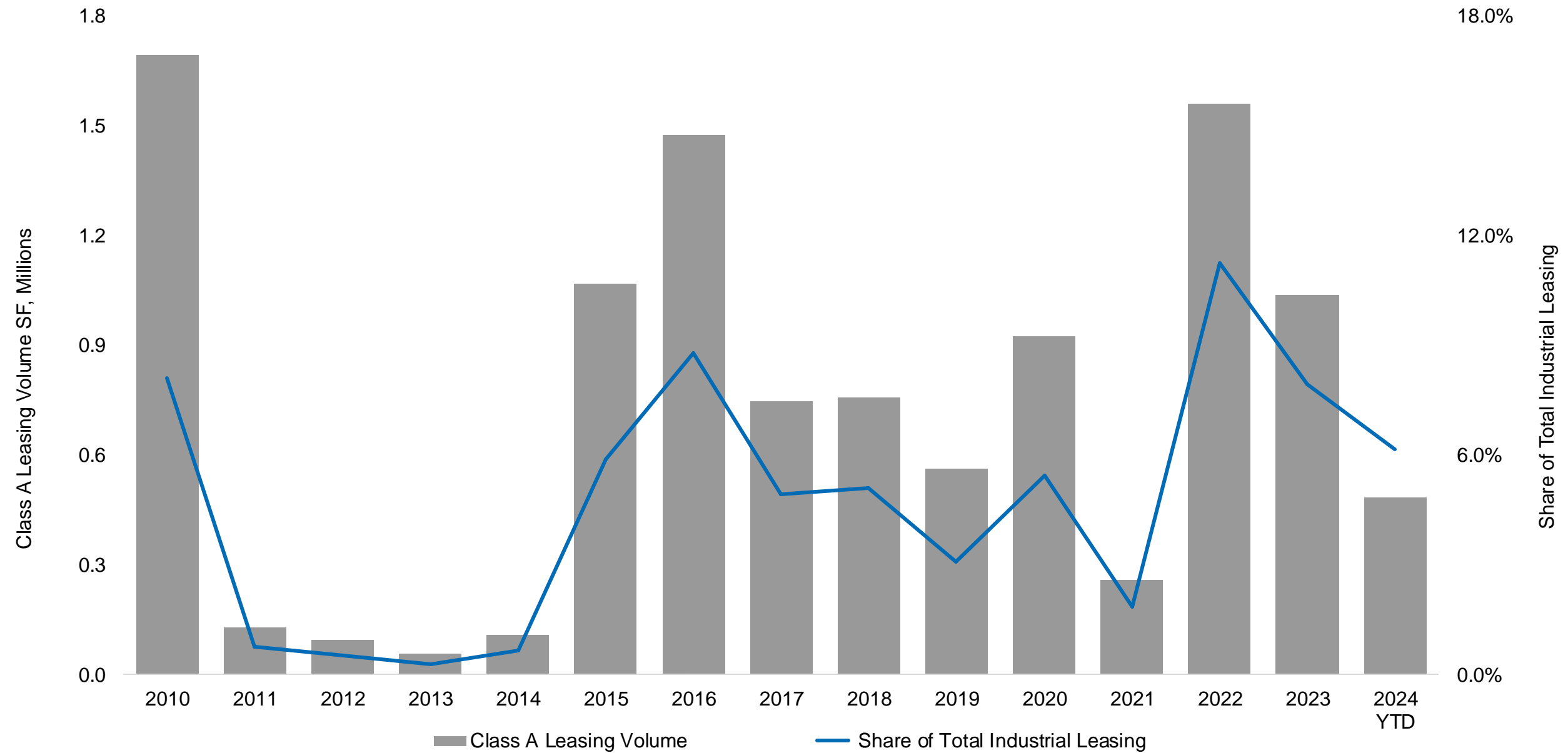
Source: Newmark Research, CoStar



# Slowed Class A Leasing Activity This Quarter

The momentum of Class A leasing activity from the first half of the year has slowed, with year-to-date leasing activity accounting for less than half of 2023 totals. Yes4All's sublease at 3170 Nasa Street for 104,316 SF was the sole contributor for this quarter.

## Industrial Class A Leasing Volume and Percentage of Total Industrial Leasing Volume



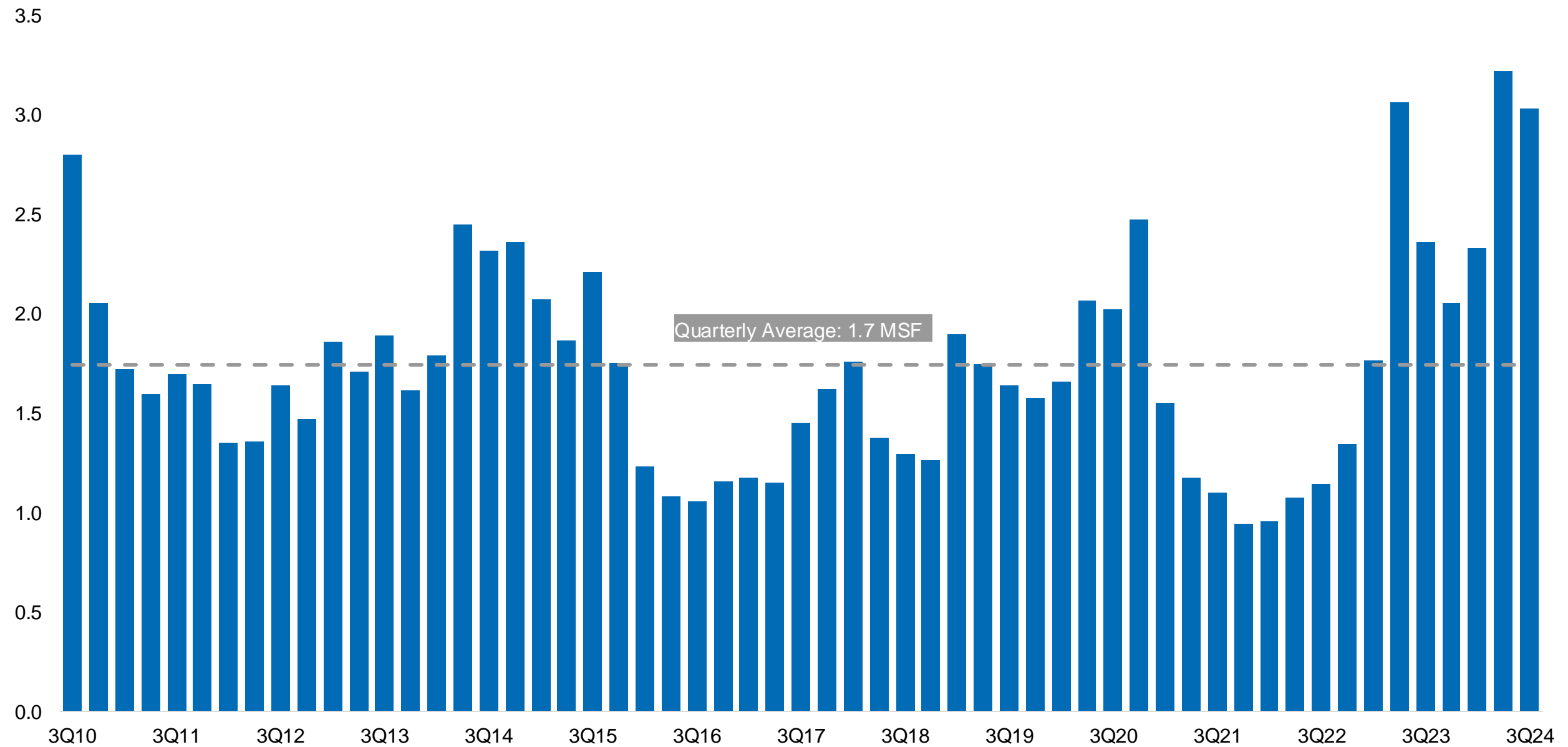
Source: Newmark Research, CoStar



# Sublease Availability Remains Elevated Following Surge From Previous Quarter

Last quarter's sublease offerings from Quicksilver and TYP Sport (328,084 SF at 5600 Argosy Ave in Huntington Beach), McKesson (147,950 SF at 1930 Malvern Ave in Fullerton) and Syco Enterprise (134,716 SF at 500 W Warner Ave in Santa Ana) are still active and keeping sublet availability elevated. Some tenants are downsizing to mitigate the high costs of doing business amid a slowed economy.

Available Industrial Sublease Volume (MSF)



Source: Newmark Research



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## North County Leads Other Submarkets In Sublet Availability

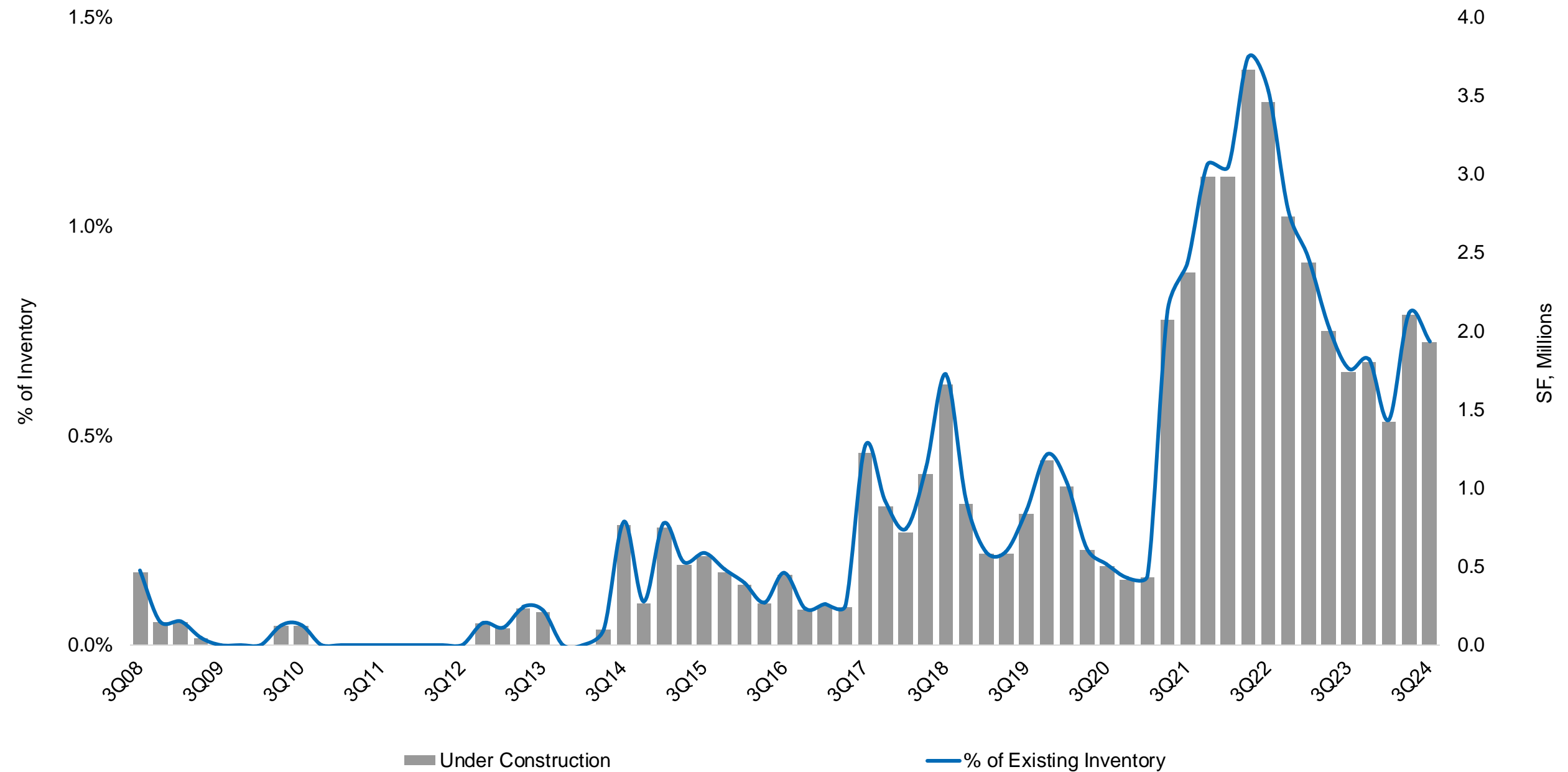
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# Elevated Under-Construction Levels Gradually Normalizing

A total of 1.9 MSF across ten development projects are currently underway, all of which remain available save one. Construction starts are expected to level off in the quarters ahead.

## Industrial Under Construction and % of Existing Inventory



Source: Newmark Research



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## Pre-leasing Activity at a Halt

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# Third Quarter's Top Deals Were All Over 100,000 SF

A mix of renewals, direct leases and a sublease were signed this quarter, all of which were over 100,000 SF. Traditional manufacturing occupiers, specifically in the aerospace sector, are renewing contracts for their large-block spaces as they are harder to come by in the small-box market.

## Select Lease Transactions

Tenant	Building	Submarket	Type	Square Feet
Astech Engineered Products Inc.	3030 Red Hill Ave	Airport Area	Renewal	315,000
<i>This has been the aerospace company's headquarters for over two decades.</i>				
Integral Aerospace LLC	2036-2040 E Dyer Rd	Airport Area	Renewal	278,132
<i>Integral Aerospace has committed to an additional eight years at its manufacturing facility.</i>				
L3 Technologies Inc.	22745 Savi Ranch Pkwy	North County	Direct Lease	141,863
<i>This is the Florida-based defense company's second manufacturing facility in Orange County.</i>				
Orange Courier	2815 Warner Ave	Airport Area	Sublease	120,000
<i>The logistics company took over a sublease in Irvine to support its expanding operations.</i>				
Big D Floor Covering Supplies	12782 - 12802 Monarch St	West County	Direct Lease	108,981
<i>The construction material supplier moved into the brand-new facility to support its retail stores in the area.</i>				



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## New Bill Adds Regulations on Warehouse Development in the State

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# Sales Activity

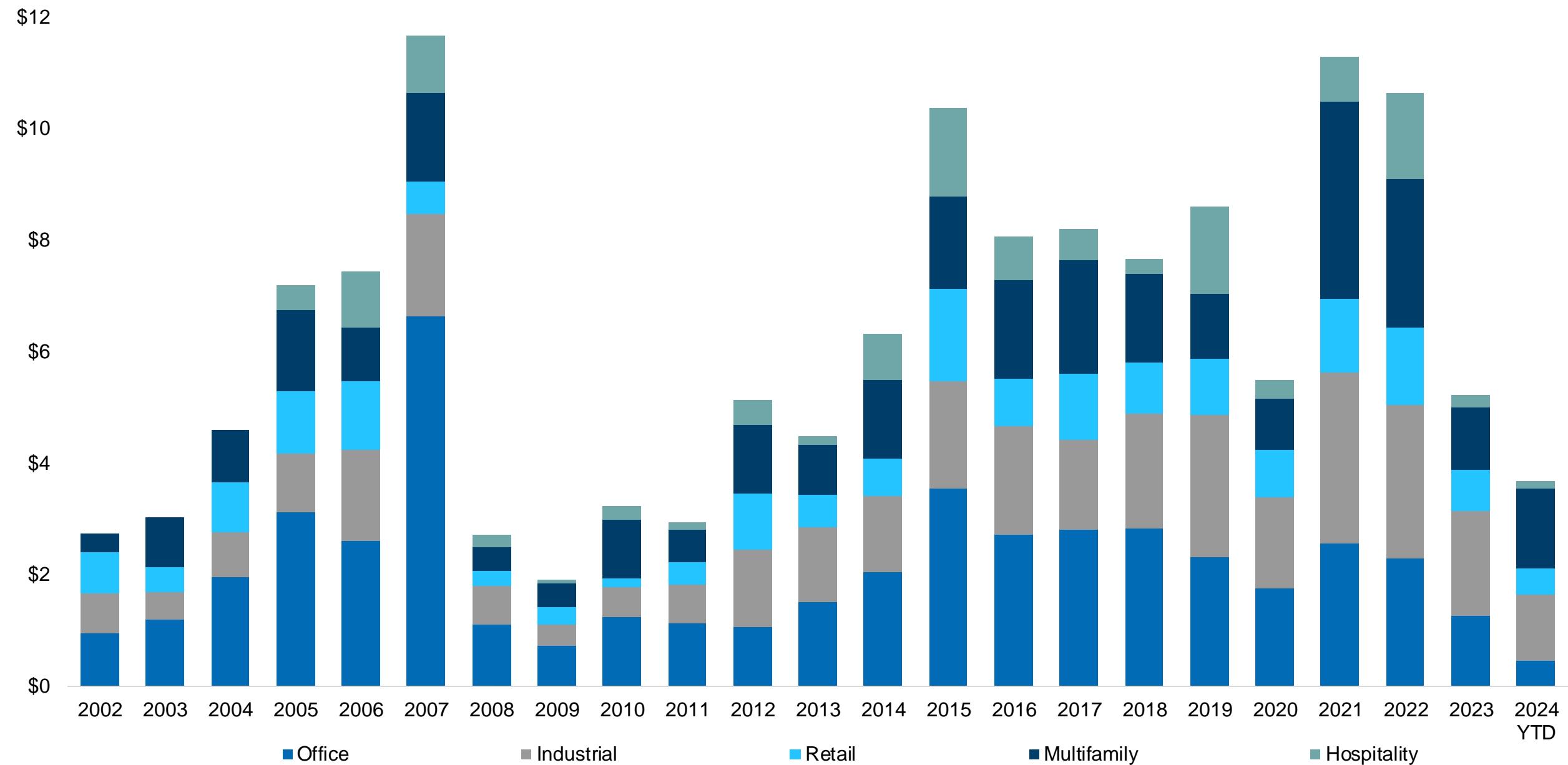




# Industrial Comprised 32.2% of Total Sales Volume Year-To-Date

This figure is significantly higher than the 20-year average (2004 to 2023) of 23.5%. Still-ow vacancy and heated rent growth in recent years favor the segment, with many investors targeting desirable buildings with credit tenants whose leases are up for renewal. What the tenant was paying (\$\$) is different than today's rent averages (\$\$\$\$).

Orange County: Sales Volume Across Commercial Property Segments (\$ in Billions)



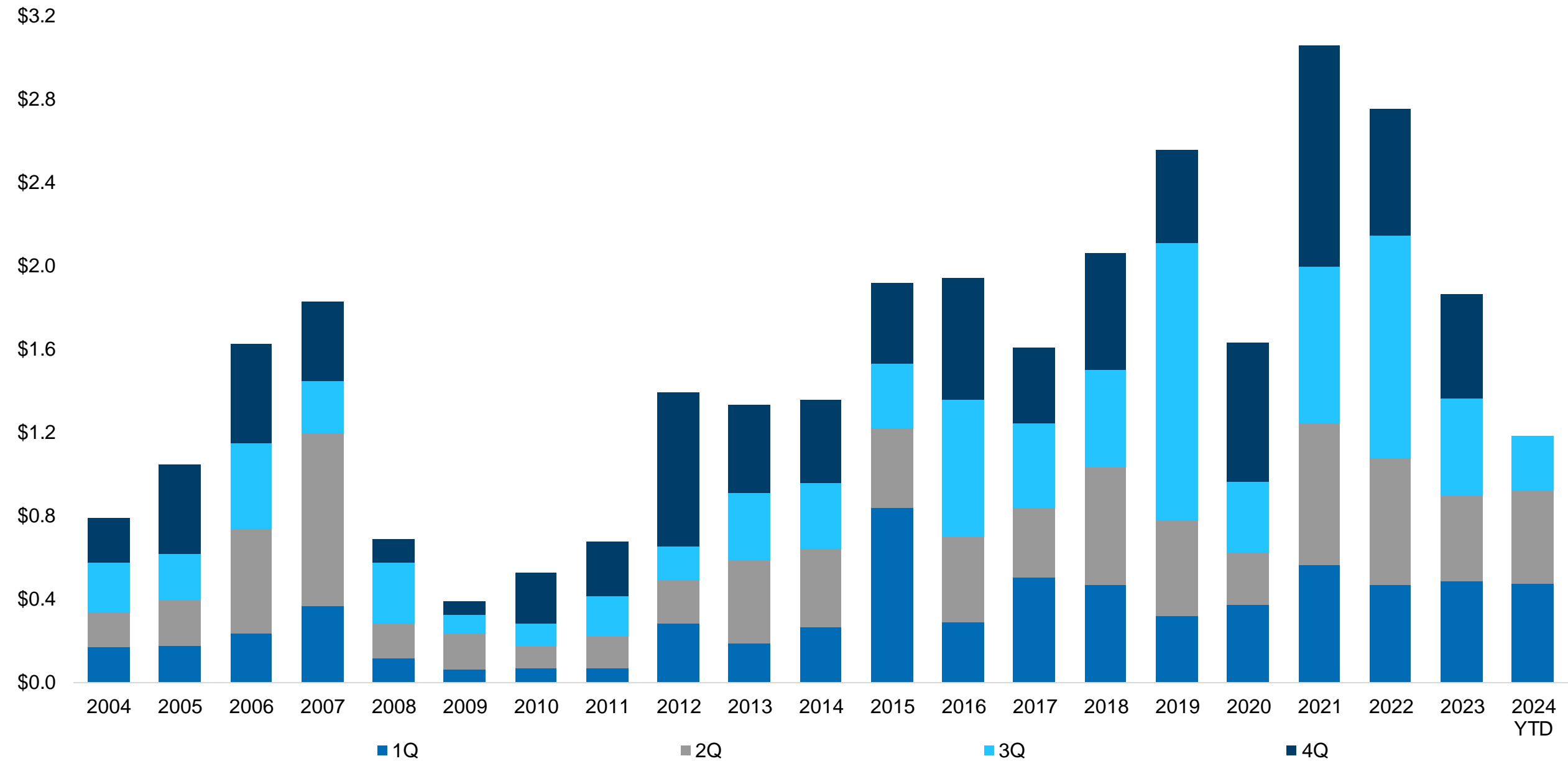
Source: MSCI Real Capital Analytics, Newmark Research  
 Note: Preliminary data is cited for the third quarter of 2024.



# Industrial Sales Activity Cooling

Industrial sales volume totaled \$265.0 million in the third quarter of 2024, down by 43.6% from the same period in 2023. The higher cost of capital following multiple interest rate hikes from March 2022 to July 2023 has crimped momentum, in addition to adjusting leasing fundamentals. Sales activity could increase in 2025 as the Fed imposes successive interest rate cuts, following this quarter's 50 bps reduction.

Orange County: Industrial Sales Volume (\$ in Billions) | By Quarter



Source: Newmark Research, MSCI Real Capital Analytics  
 Note: Preliminary data is cited for the third quarter of 2024.



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## Pricing Hovers Below 2022's Peak, While Cap Rates Are Rising

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## Private and REIT Investors Most Active Industrial Buyers

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# Appendix





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## Orange County Submarket Map and High-Level Statistics | 3Q24

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## Some Underperforming Office Properties Will Find New Life

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## WAIRE: Program Summary and Implications for Industrial

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# The World's Top 20 Containerized Cargo Seaports

Fifteen are in Asia, China leads all other countries with eight and Los Angeles-Long Beach is the only U.S. complex to make the list.

Rank	Seaport	2023 Volume (TEU, in millions)
1	Shanghai, China	49.2
2	Singapore	39.0
3	Ningbo-Zhoushan, China	35.3
4	Qingdao, China	30.0
5	Shenzhen, China	29.9
6	Guangzhou Harbor, China	25.4
7	Busan, South Korea	22.8
8	Tianjin, China	22.2
9	<b>Los Angeles-Long Beach, U.S.</b>	<b>16.6</b>
10	Jebel Ali/Dubai, United Arab Emirates	14.5

Rank	Seaport	2023 Volume (TEUs, in millions)
11	Hong Kong	14.3
12	Port Klang, Malaysia	14.1
13	Rotterdam, The Netherlands	13.4
14	Xiamen, China	12.6
15	Antwerp, Belgium	12.5
16	Tanjung Pelepas, Malaysia	10.5
17	Kaohsiung, Taiwan	8.8
18	Laem Chabang, Thailand	8.7
19	Tanger Med, Morocco	8.6
20	Beibu Gulf, China	8.0

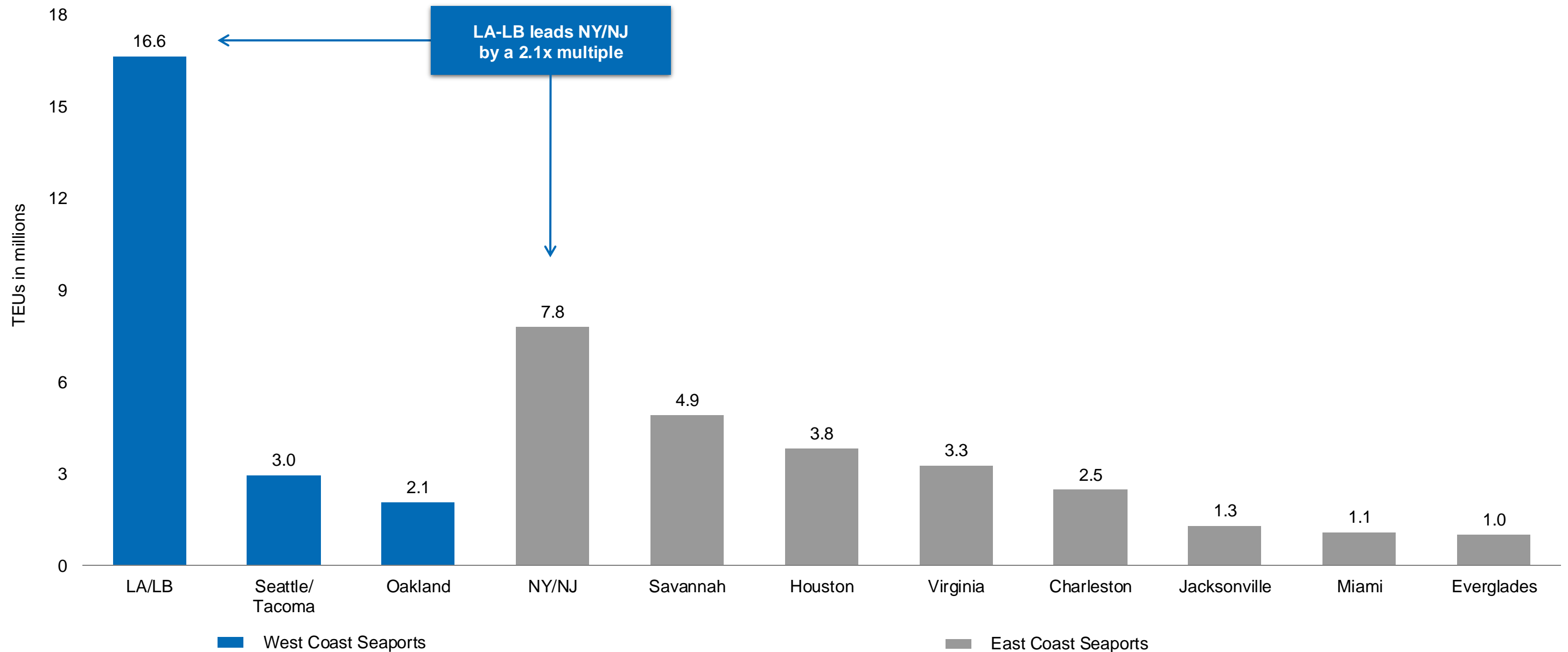
Source: Newmark Research, upply  
 Note: TEU totals includes loaded and empty containers



# Los Angeles-Long Beach is the Nation's Dominant Port System

Los Angeles-Long Beach can accommodate 18,000 TEU vessels, which are too wide to traverse the new Panama Canal. Additionally, both ports have Class 1 freight rail connectivity to the nation's major population centers.

Major U.S. Seaports: 2023 TEU Volume (All Containers: Loaded and Empty)



Source: Newmark Research, Individual Seaports



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## Why Los Angeles-Long Beach?

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# Transport Costs Are the Biggest Expenditure for Most Warehouse Occupiers

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Transport Costs Per TEU Container Increase the Further an Occupier is from the Ports

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