RADIUS Insight

RADIUS® Commercial Real Estate

SOUTH COAST MARKET REPORT
Q3 2023

Q3 Commercial Sales Summary

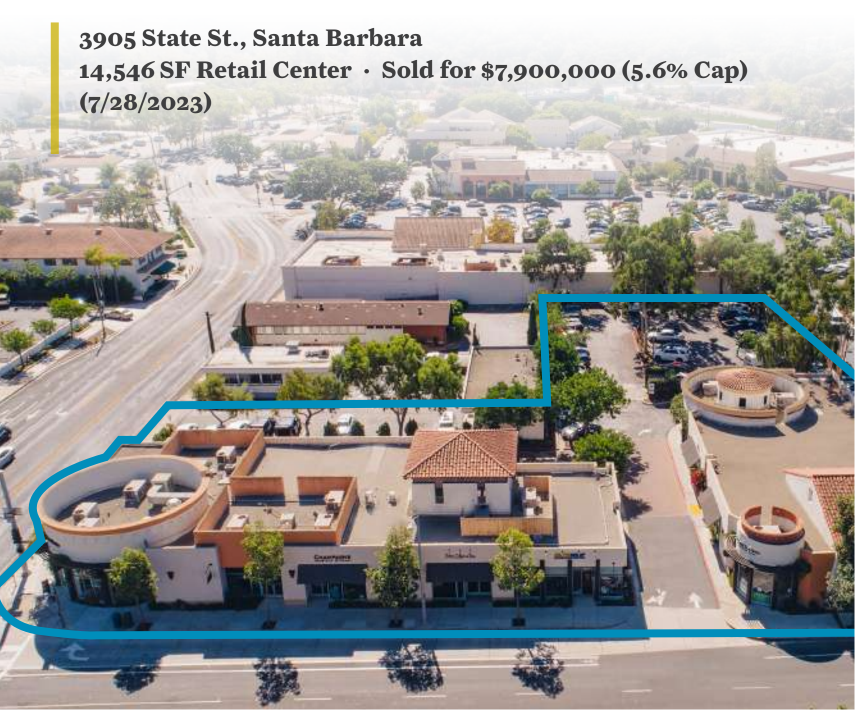
PAINT DRIES ON DECLINING Q3 SALES STATS

South Coast sees lowest number of commercial deals and sales volume since 2020, underscoring negative trends of recent quarters

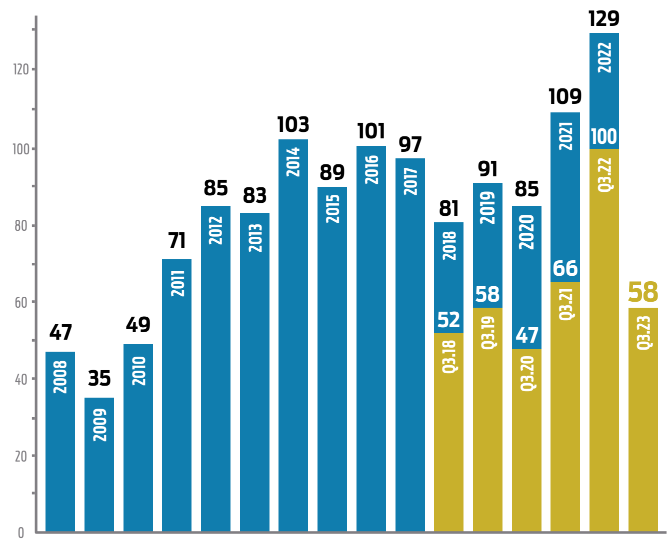
The third quarter of 2023 marked another quarter of declining activity; in fact it was the softest quarter on record since 2020—and the most telling—clearly illustrating many of the trends we've been witnessing during recent quarters and showing the market's true colors.

There were just 14 commercial sales resulting in $33.5MM volume (excluding one $5.2MM hotel sale), the lowest Q3 haul in five years (average Q3 over past five years = 27 sales @ $105MM volume), and down 42% from the second quarter of 2023 (24 sales @ $96MM). By asset type, the quarter saw six retail, four office, two industrial, one land and one hotel deal. investors again purchased the bulk of the product (11 investors vs. 3 owner-users). We attribute this to the backlog of 1031 exchange buyers and lack of available financing for owner-users.

3905 State St., Santa Barbara
14,546 SF Retail Center · Sold for $7,900,000 (5.6% Cap) (7/28/2023)



2023 South Coast Commercial Sales



15-year average = 83.7 sales/year. Excludes apartment sales.

The most eye-opening market statistic, which we saw signs of in Q2, is the margin between original listing prices versus effective sale prices, as well as time on market. According to our data, the average discount from asking prices across the 14 sales was 14%. However, half of Q3's transactions sold at an average price drop of 24%—and in some cases as high as 30–40%—below their original asking prices. As a result, some of these properties spent time on the market in excess of a year. These stats are sobering signs of a turning market and environment in which the gap between sellers' and buyers' expectations is narrowing.

However, it is important to note that these discounts are

Commercial Sales Summary Continued on P.2

Q3 Commercial Sales Summary

Q3.23 Quick Stats

14
SALES (Q3.23) vs. AVG. 27 OVER PAST 5 Q3'S

42%
DECLINE OVER Q2 (24 SALES / $96MM VOLUME)

$33.5MM
SALES VOLUME (Q3.23) VS. $108MM (Q3.22)
(Excludes Hotel Sales Volume)

11
INVESTOR SALES VS. 3 OWNER-USERS

Continued from P.1

asset-specific. The deals with the largest discounts were primarily vacant office or retail properties. Otherwise, industrial assets continued to hold their pricing, a result of very low vacancy and low inventory in this sector.

What the future holds is uncertain. Increasing treasury yields and global turmoil continue to spook the commercial real estate investing market and affect pricing. One change in direction taking place is an uptick in available inventory. As vacancies increase and property loans near maturity, the market has seen more product come available.

While the 15-yr. sales average in the South Coast market is 83.7 sales/year, 2023 is currently pacing to finish below that. That said, fourth quarters have proven to be the boldest over the last few years, and we may see a strong finish as buyers and sellers push to finalize transactions by year-end in conjunction with the 1031 exchange deadlines extending yet again to November 16.

A final word to the wise: if you are a seller, pricing your property correctly at the beginning of the marketing cycle is imperative to avoid chasing down the market. Barring some serious property defect such as environmental issues, poor location or high vacancy, if you don't see some interest within the first 30–45 days on the market, you are likely overpriced.

Notable Q3 deals

3905 State St. – 14,546 SF Retail Strip Center
$7.9MM (5.6% Cap Rate)

1323 De La Vina St. – 8-key Boutique Hotel
$5.2MM ($650,000/Key)

726 State St. – 2,384 SF Retail Property
$2.16MM

1514 Anacapa St. – 3,420 SF Office Property
$1.875MM

1323 De La Vina St., Santa Barbara
8-Key Boutique Hotel
$5,200,000 (7/11/2023)

726 State St., Santa Barbara
2,384 SF Retail Building
$2,155,000 (7/26/2023)

1514 Anacapa St., Santa Barbara
3,420 SF Office Building
$1,875,000 (7/6/2023)

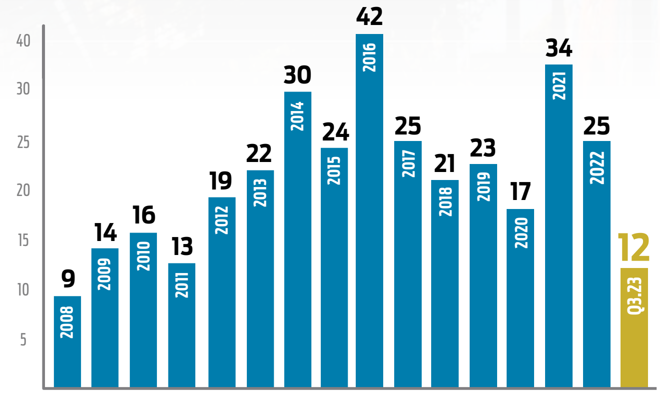
Q3 Multifamily Sales Summary

During the third quarter of 2023, there was a noticeable decrease in activity compared to the previous year. This was anticipated in the multifamily space due to increasing interest rates, specifically the 10-year treasury, which rose 72 points from the beginning of the quarter (7/3/2023: 3.858%) to the end (9/29/2023: 4.579%). Although there is still a substantial pool of buyers, they are now more conservative in their underwriting process, considering the significant debt cost factor currently influencing the market. Additionally, Sellers are beginning to realize that properties with a 3% CAP rate are not as common as they used to be. Though a few hit the market in Q3, typically their profile is a lower price/unit number associated with the lower cap rate as rents are well below market, which has great market rent upside for those units. Investors that are taking into consideration these properties are trying to take advantage of the low price/unit price point, understanding that over time they will be able to adjust rents consistently and most likely will need to invest in upgrades to the property.

Still, multifamily performance continues to hold up well, as rents and occupancy were relatively flat this quarter. We did not see a large change in market rents over the past quarter, as we still see strong rental demand in Santa Barbara, Ventura and SLO counties. Economic growth continues to be stronger than expected, supporting consistent multifamily demand.

After several years of stellar income growth, multifamily faces headwinds that include not only decelerating rent gains but also a rapid uptick in expenses led by massive growth in insurance costs. Insurance is rising because of the growing number of significant weather-related events: extreme temperatures and wildfires have created large insurer payouts, particularly in the Southeast, Texas and California. This has become a major variable for buyers when underwriting properties and will be a concern for the foreseeable future.

2023 South County Multi-Family Sales



Properties 5+ Units in Size

We are seeing more products on the market right now than we have in past years. As of 10/20/2023, in the City of Santa Barbara alone, there are 10 multifamily properties for sale ranging in size from 6 – 75 units with current CAP rates ranging from 3.20% – 5.29%, and price per unit ranges from $306,818 – $510,000 per unit. Typically, we do not see this much inventory on the market at one time.

215 Bath St., Santa Barbara
52 Units · $16,800,000 ($323,077/Unit · 3.39% CAP Rate)
8/31/2023

South Santa Barbara County

South Santa Barbara County saw just three transactions in Q3 involving properties greater than 5 units. The largest transaction was 215 Bath St., a 52-unit asset in the highly desirable West Beach area. This property, which was listed at $19,000,000 and sold for $16,800,000 ($323,077/unit) at a 3.39% CAP rate, included 23 studio units, 27 one-bed units and two (2) two-bed units, with rents well below market.

A 12-unit property located at 280 Mathilda Dr. in Goleta sold for $4,000,000 ($333,000/unit) at a 4.42% current CAP rate. Goleta remains a highly desirable rental market.

The third sale of the quarter was located in Carpinteria at 4956 5th St. This 7-unit building sits in

Multifamily Sales Summary Continued on P.4

Q3 Multifamily Sales Summary

Continued from P.3

a very attractive location just blocks from the beach. Priced at $4,395,000, the asset was on the market for three months and sold under asking at $4,000,000 ($571,428/ unit). The unit mix for this property was (5) 3-bed / 2 bath units and (2) 2 bed / 1 bath units. The property included below market rents in place and a number of deferred maintenance items.

Isla Vista

In Isla Vista, despite multiple properties coming to market, there was very limited sales activity in Q3. One property that did close during the quarter was at 6697 Del Playa Dr., a 2-unit oceanfront student housing asset that had been renovated and set back over 30 feet from the bluff which is a great feature in the eyes of the Coastal Commission as well as buyers. This property sold for $2,650,000 at a 5%+ CAP rate on current rent with additional upside in rent for the 2024–2025 school year.

There is still a strong demand for housing in Isla Vista as student housing continues to get top-of-market rents. Investors are exercising a cautious approach and careful consideration in their decision-making process in this current high-interest rate environment and with high insurance costs when looking at the currently available properties.

North Santa Barbara County

North County saw just one transaction in Q3: an 18-unit designated affordable housing property located at 733 N. E St. in Lompoc. The property was on market for 85 days with an asking price of $2,295,000. The building sold for $2,145,000 ($119,167/unit).

San Luis Obispo County

In SLO County, five (5) properties traded in the segment of 5+ Multifamily units. 3505 Spring St., Paso Robles, was an 8-unit building that sold for $1,510,000 ($188,750/ unit). Also, 318 4th St. Paso Robles sold for $2,700,000 ($385,714) and was a 7-unit building. Another 7-unit building at 175 Stimson Ave, Pismo Beach, sold for $4,150,000 ($592,857/ unit). The third property was located at 3150 Rockview Place, SLO, this was a 9-unit building that sold for $2,430,000 ($270,000/ unit), this property was sold at a 4.5% CAP rate based on the current income, the property was delivered with one unit vacant as well. The final 2 sales in SLO county were 2005 Binns Ct., San Luis Obispo which sold for $1,800,000 ($360,000/unit), this property was on the market for over 60 days and was initially listed at $2,350,000.

Annual rental rates in San Luis Obispo County have seen modest growth of about 2.3%. The top employers in SLO County are still Cal Poly, the County of San Luis Obispo and Atascadero State Hospital with Amazon growing its presence in the region as well.

Ventura County

Ventura County saw a total of 4 transactions in Q3 of 2023. Two of which occurred in Oxnard at 5200 Wooley Rd. & 1719 S Oxnard Blvd. Wooley Rd., was a 7-unit property that sold at a 4.28% CAP rate and a price point of $2,838,000. 1719 S Oxnard Blvd, this was an off-market transaction with limited additional information. 1719 S Oxnard Blvd. is a 105-unit property that was built in 2000.

The other transactions in Ventura County that were completed in Q3 were located at 330-332 Fillmore St. Fillmore, as well as 1313 Buena Vista St in Ventura. 330 Filmore St. was a 10-unit building that sold for $2,443,00 ($244,300/unit), and 1313 Buena Vista St was a 12-unit property that had recently been updated and sold for $5,930,000 ($494,167/ unit) at a 4.45% CAP rate. This was a well-located property close to downtown Ventura.

Multifamily Sales Summary Continued on P.5

Q3 Multifamily Sales Summary

Continued from P.4

Summary

There is still strong demand for multi-family housing in San Luis Obispo, Santa Barbara, and Ventura County. Though there is strong interest, we are seeing investors exercising caution and taking more time than in past quarters before making decisions due to the unique combination of high-interest rates and low asking CAP rates where properties are currently being priced. With this buyer sentiment, we are seeing several properties sit on the market longer than we have seen in past years. Interestingly enough, we are seeing more inventory on the market currently in Santa Barbara and Ventura County at one time than we have in the past year as well. If you are in the market for multifamily housing, there are several options available to you. However, these properties are running into the same challenge as buyers are still working to make sense of the price points, taking into consideration increased expenses as well as low asking cap rates. This dynamic has resulted in several properties trading below the asking price point in Q3. We have seen this trend for the past couple of quarters. When properties are coming to market, we still have higher CAP rates than in past years, but they are trending well below the current interest rates.

We expect to see more transactions in Q4 than we did in Q3, as several of the properties on the market in Q4 have gone under contract and are expected to close in late November and early December. We anticipate a spike in the sales activity of 10+ unit assets in the Santa Barbara County. We are seeing evidence of this based on the current pending transactions. South County recently saw two properties go pending, both boasting 16+ units as well as a 12 unit North County property which went under contract in 24 days. These are all positive signs that the market is picking back up within the larger multi-family category.

We are anticipating more of the same for the remainder of the year with regard to rental rates. In Q3, like in Q1 & Q2 of 2023, rents have plateaued and slightly decreased from the highs of 2022. Owners are still achieving much higher rates than we have seen over the past couple of years in the area but the are not increasing at the same rate as rents have been in 2021 & 2022.

Q3 South Coast Leasing Summary

2023 So. Coast Leasing Quick Stats

VACANCY

		Q2.23	Q3.23
OFFICE	Santa Barbara	12.6%	13.3%
	Goleta	9.8%	9.5%
	Carpinteria	31.3%	30.1%
INDUSTRIAL	Santa Barbara	0.8%	0.9%
	Goleta	4.4%	3.1%
	Carpinteria	3.3%	3.0%
RETAIL	Santa Barbara	2.0%	2.1%

GROSS ABSORPTION (SF)

		Q2.23	Q3.23
OFFICE	Santa Barbara	60,400	69,000
	Goleta	13,400	72,600
	Carpinteria	2,400	5,400
INDUSTRIAL	Santa Barbara	16,500	28,800
	Goleta	27,000	115,600
	Carpinteria	0	0
RETAIL	Santa Barbara	16,400	46,700

AVG. GROSS ASKING RATES ($/SF)

		Q2.23	Q3.23
OFFICE	Santa Barbara	$3.27	$3.27
	Goleta	$2.21	$2.14
	Carpinteria	$2.69	$2.66
INDUSTRIAL	Santa Barbara	$2.12	$2.47
	Goleta	$1.95	$1.93
	Carpinteria	$1.90	$1.76
RETAIL	Santa Barbara	$4.25	$4.11

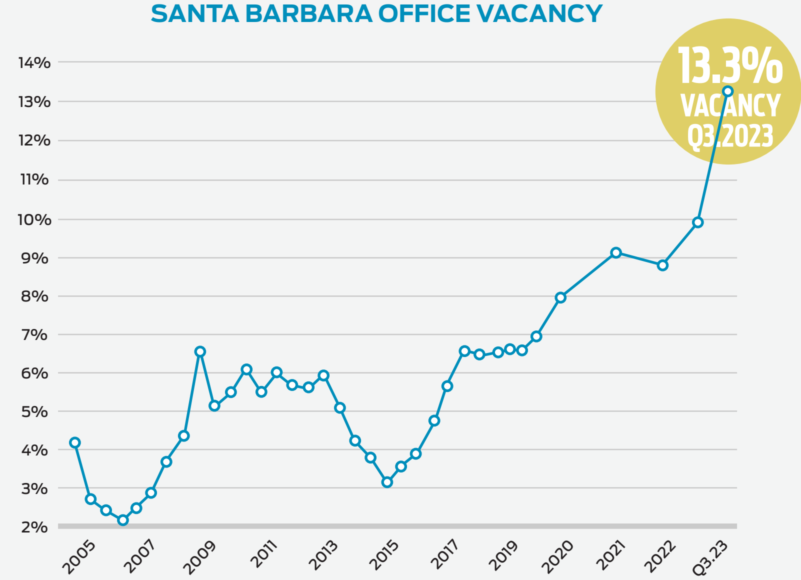
AVG. GROSS ACHIEVED RATES ($/SF)

		Q2.23	Q3.23
OFFICE	Santa Barbara	$3.03	$2.99
	Goleta	$1.99	$2.22
	Carpinteria	$2.00	$1.70
INDUSTRIAL	Santa Barbara	$1.96	$1.92
	Goleta	$2.08	$1.94
	Carpinteria	N/A	N/A
RETAIL	Santa Barbara	$3.16	$4.23

Office

Goleta office vacancy currently sits at 9.5%. During the 3rd quarter we saw AppFolio sublease 35,297 SF of their campus. Inogen subleased their 50,000 SF R&D building and then leased 17,928 SF of space at 859 Ward Dr. Bell-Everman also leased 8,145 SF at 759 Ward Dr. There remains 43,655 SF of space available for sublease from AppFolio on Castilian Drive and 29,372 SF available at 6500 Hollister Ave. However, there seems to be more tenant activity in Goleta currently than we have seen over the last 12 months. We would guess the vacancy rate will tick down further.

SANTA BARBARA OFFICE VACANCY



Meanwhile in Santa Barbara, the office vacancy rate ticked up to 13.3% in the third quarter. The largest spaces remain the vacant former Macy's and Nordstrom buildings that anchor Paseo Nuevo Mall, both of which are being marketed as tech office. Together this represents just under a whopping 300,000 SF. However, recently it was announced that the owners of the Macy's building are trying to bring housing to the site. Should they demolish the building that would remove 132,500 SF of vacancy. There is also 28,000 SF of available office space at 25 E. Mason St. in the Funk Zone (former Sonos building).

The biggest lease of the quarter was Umbra Labs subleasing the 27,773 SF space at 419 State St. This large tech office lease probably didn't get enough attention as this was a big win for State Street and downtown considering the many challenges this area continues to face. The next biggest lease of the quarter was Zoom subleasing their 7,758 SF space at 420 E. Carrillo St., which feels a bit ironic.

Finally down in Carpinteria the office vacancy rate remained above 30% in Q3, finishing the quarter at 30.1%. As mentioned many times before this is a very small-inventory submarket and a few larger vacancies can have a major impact on the vacancy figures. The largest vacancies remain ProCore's 50,000 SF at 6267 Carpinteria Ave., as well as the company's 28,493 SF at 6307-B Carpinteria Ave. There were just two new lease

Leasing Summary Continued on P.7

Q3 South Coast Leasing Summary

Continued from P.6

transactions during the quarter, the largest being 4,770 SF at 1180 Eugenia Pl. taken by Realty Carpinteria for office use.

Subleased | 301 Coromar Dr., Goleta
±50,532 SF Industrial
7/13/2023 (Sonos)

Leased | 147-151 Castilian Dr., Goleta
±35,297 SF Industrial
7/27/2023 (Karl Storz Imaging)

Leased | 419 State St., Santa Barbara
±27,773 SF Creative Office
7/21/2023 (Umbra Lab, Inc.)

Leased | 859 Ward Dr., Goleta
±17,928 SF Creative Office
8/2/2023 (Inogen)

Leased | 1200 State St., Santa Barbara
±14,714 SF Retail
8/1/2023 (JPMorgan Chase & Co.)

Leased | 759 Ward Dr., Goleta
±8,145 SF Office/R&D
9/14/2023 (Bell-Everman, Inc.)

Industrial

The industrial sector ended the quarter with continued trends of low vacancy and stable lease rates. Overall there was just about 145,000 SF of new lease activity including some notable company moves, however Carpinteria saw no new activity. Goleta dominated the headlines beginning with Sonos leasing 50,000 SF at 301 Coromar Dr. (formerly occupied by Inogen) and they will transition/consolidate their numerous downtown Santa Barbara facilities into this newer industrial/R&D building that commanded over $2.00/SF NNN. The market continues to demand newer, high-efficiency flex/industrial product.

Karl Storz Imaging also leased 35,000 SF at 147 Castilian Dr. for additional R&D space. While the medical device manufacturer is relinquishing a small industrial space on Aero Camino, the company is increasing its footprint in Goleta with this move. Soilmoisture, another company making moves, signed a new lease at 601 Pine Ave. for 12,800 SF after occupying a building on Kellogg Avenue since the early 60's. Goleta's vacancy rate dropped from 4.4% to 3.1% during Q3, with rates remaining stable.

Santa Barbara industrial activity, on the other hand, was made up largely of lease renewals with a handful of smaller new leases. The city's vacancy rate remains below 1% with continued stable rates.

Notable vacancies in the market include 42,000 SF at 326 Bollay Dr., Goleta; 17,000 SF at 1 N. Calle Cesar Chavez, Santa Barbara; and 24,000 SF at 6384 Via Real, Carpinteria. Additionally, cannabis distributor Herbl, which fell into receivership in June, vacated over 50,000 SF between three buildings located at 839, 759 and 749 Ward Dr. in Goleta.

Looking forward, there are multiple industrial tenants in the market and we expect this sector to remain stable with continued activity. After years of significant rate increases, we do see level rents in the near term.

Retail

Retail leasing improved on the South Coast during the third quarter, a positive sign for local owners of retail property. During Q3 there were 21 new leases totaling about 47,000 SF, representing twice the absorption of the 14 new leases in Q2. Smaller spaces remain the most active with deals ranging from approx. 530-15,000 SF.

The largest retail lease was to JP Morgan Chase at 1200 State St. While the recent shake-up in the banking industry triggered the lease, it was exciting news to see the international bank retain the building formerly occupied by First Republic (RIP), especially given recent large vacancies by US Bank and Bank of the West just a few blocks down State Street. With recent activity favoring retail spaces under 5,000 SF, these larger financial service buildings continue to be tough to fill.

Upper State Street remains active with the sale of 3905 State St., which quickly followed with a Lease to Town & Country Event Rentals. The company pivoted from a showroom/warehouse at 1 N. Calle Cesar Chavez to a retail corner previously occupied by TD Ameritrade. The 3,151 SF retail lease filled a long-term vacancy on the prominent intersection of State Street and La Cumbre Road.

Validation Ale leased a second Santa Barbara location at 2840 De La Vina St., highlighting another example of successful Funk Zone brands expanding into a more localized retail market.

Retail leasing was more active this quarter, but the overall Santa Barbara retail vacancy rate was stable, shifting only slightly from 2.0% to 2.1%. Asking rates for Santa Barbara retail are averaging $4.11/SF Gross Equivalent (Base Rent + NNN) continuing the downward trend for the past year. However, achieved rates increased from $3.16/SF Gross Equivalent to $4.23/SF Gross Equivalent in Q3.

Although JP Morgan Chase constituted the largest lease, the overall retail market on the South Coast continues to be driven by local small businesses. With rising interest rates and SBA financing compressed, the community and regulators will need to be proactive for the success of these retailers.