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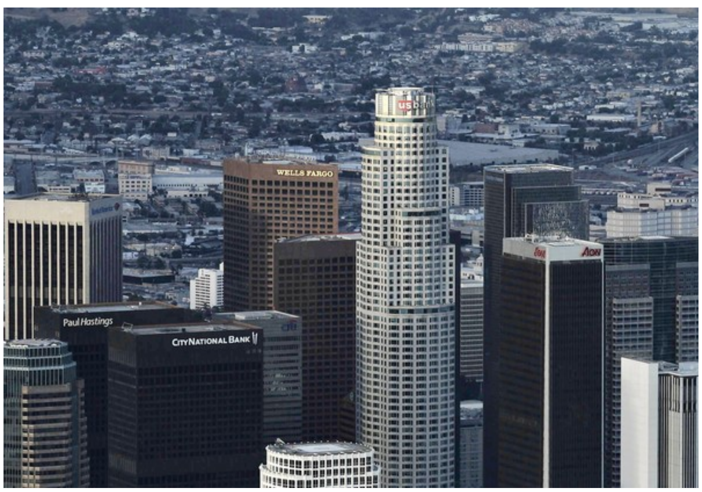
Office market will stabilize soon, brokers predict

Rents and occupancy fell in Southern California's office buildings last quarter. But, brokers say, the pace of lease transactions picked up as new tenants took advantage of the prices.

By Roger Vincent, Los Angeles Times January 23, 2011



Is this what the bottom looks like?

Challenging times persisted for landlords in the fourth quarter as rents and occupancy fell in Southern California's office buildings. But at the same time, the pace of lease transactions picked up as business owners moved to take advantage of comparatively low rental rates, bolstered by growing confidence that their firms have weathered the worst of the economic downturn, real estate brokers said.

"We are definitely flattening out," said Joe Vargas, area manager of Cushman & Wakefield.

The real estate brokerage reported that 19.6% of offices in Los Angeles, Orange, Riverside and San Bernardino counties were empty in the fourth quarter, up from 18.5% a year earlier. The overall average rent sought by landlords was $2.34 per square foot per month, down 7 cents.

Occupancy and rents will continue to fall slightly over the next quarter or two and then stabilize, Vargas predicted: "We are essentially bumping along the bottom right now." That counts as upbeat news in a market that has been in decline for 12 straight quarters.

This year, a slight recovery for the office leasing business is in store, broker Bob Safai of Madison Partners said. "Now it becomes a matter of going through the process of healing." The process will be slow, he said, and it will be 2013 before landlords can expect "a huge upswing" in occupancy and rents.

The Southern California market has shown sparks for the last few months as new leases were signed and some companies even expanded their offices, but the overall market has been stubbornly disappointing to landlords who would like to fill their buildings and charge higher rents. While some firms were ready to make commitments to stay put or expand, others gave up space or moved someplace else.

"Every time we think we are going to get ahead in a certain submarket, someone bails out," said Jonathan Larsen, an executive managing director at Transwestern real estate brokerage.

In Century City, for example, legendary studio Metro-Goldwyn-Mayer Inc., aviation giant Northrop Grumman Corp. and law firm Goodwin Procter have all announced plans to leave. Century City is considered one of the region's premier office markets, but it had a net reduction of more than 200,000 square feet of rented space last year, more than it lost in 2009.

West Hollywood landlord Charles Steven Cohen, though, is upbeat. Tenants in his family's Green Building at the Pacific Design Center have recently opened lease renewal negotiations years early in hopes of locking in current rates.

"We have been along the bottom for a while," he said. "Rents are not going down any more."

Cohen is one of the few owners building new office space in the region. His $160-million Red Building on San Vicente Boulevard will be finished this summer and he is asking for $5 per square foot per month, well above the West Hollywood average of $3.60.

The sleek, bright red building designed by architect Cesar Pelli "will see a flight to its unusually artistic, monument-type architecture," he said. "We want to pick the very best tenants."

Owners of more typical buildings, however, are waiting for corporate America to start hiring again. Nearly 110,000 office-using jobs have been lost in Los Angeles County since the economy tanked, according to brokerage Jones Lang LaSalle.

Companies are slow to hire during the early stages of recovery, the brokerage said, and many tenants are saddled with excess, unused space for which they are paying rent. Such "shadow" space must be absorbed before companies start renting larger offices.