

QUARTERLY REAL ESTATE OUTLOOK

Real Estate Markets Remain Flat As Job Growth Struggles

Home Sales Dip With End Of Tax Credits; Commercial Sectors See Slight Rise In Small Business

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While local real estate markets have made some progress this year, the shaky economy is still unwilling to show true signs of recovery and continues to flounder in uncertainty.

Although somewhat better than last year, real estate activity has been up and down for the past six months, showing overall flat movement in both Long Beach and the greater South Bay region, according to brokers and economic reports.

California's unemployment rate has remained steady at 12.3 percent, as of July, with Long Beach at 14.6 percent (an increase from 13.5 the prior month), which some say is an indication that local markets are still suffering from a down economy.

Low interest rates, along with state and federal tax incentives temporarily helped bring back the housing market in the second quarter, but reports have already shown a drop in home sales and buyer confidence across the state and nation.

Gary Painter, director of research for the USC Lusk Center for Real Estate, said the decline in home purchases was expected but continues to accelerate due to struggling job growth that has yet to rebound at the same rate as the significant losses earlier in the recession. Overall, he said a trend in real estate hasn't been identified.

"I think the question is, 'where is the trend line?' And from what I can see, the trend is pretty flat," he said. "It's not clear things are getting better or worse. It's been choppy for a good year or two. Right now, it all comes down to the job market . . . and the job market is not coming back at a speed we'd all like it to."

For the commercial sectors of retail, office and industrial, this year's second quarter, ending June 30, brought more activity from small businesses attracted to lower rental rates over the last year. But most companies remain hesitant to expand, which some say overshadows any positive gains.

"I would say [the economy is] not necessarily recovering at this point," said Becky Blair, president of Blair Commercial Real Estate, who mostly deals in office and retail building space. "We handle a lot of small business so there's certainly activity, but 'recovering' means to me that job growth would be enhanced . . . and until that happens you're not going to see a lot of movement in our marketplace."

Commercial: Office, Retail Leases Pick Up

Despite some economic despondency, the commercial sectors have seen a slight rise in startups and small businesses signing leases this quarter, showing improvements as landlords offer lower rents and concession packages to attract tenants.

Hoyt Hochman, a real estate broker in charge of about 150,000 square feet in two Class C buildings for Blair Commercial, said, "The leasing market in Long Beach has begun to pick up." The property management firm brought rates down to starting rents of 99 cents per square foot for those buildings, which once ran at \$1.34.

The lower asking rents have attracted new small businesses to the market, with the firm closing on at least 50,000 square feet of overall commercial space. Although companies aren't necessarily downsizing, many have moved to the less expensive Class C buildings because of market conditions.

Meanwhile, brokerage firm Cushman & Wakefield's second quarter report also shows significant lease transactions this quarter, such as Aero Technologies, which signed on to 12,700 square feet of office space at 3333 E. Spring St., near the Long Beach Airport. Apollo Enterprises and Coffey Environments, Inc. also both signed on to different locations for about 6,900 square feet each.

The only notable purchase during the quarter was Park Tower, located at 5150 E. Pacific Coast Hwy. The previous owner, Ocean Beach Investors, sold the property for \$11.2 million to a private investor, bringing the building under new ownership. Lipscomb Chemical Company signed on as a new tenant, with 6,446 square feet.

Robert Alperin, a senior director for Cushman & Wakefield, said the market has been pretty steady and doesn't appear to show any dramatic improvements one way or the other. "There were leases that were done, there were some renewals that were done; some people left and some people came in. But at the end of the day it kept us pretty much treading water," he said of the second quarter. "We didn't really have a lot of leasing activity up or down on an overall basis."

Although rates have gone down to historic levels, Alperin noted that the market has made for a larger spread in the balance between asking rents and actual closing deals, adding that for the rest of the year, further downward pressure is expected on rental rates and lenders catering to tenants with the most credit.



Patrick O'Healy, owner of O'Healy Commercial Real Estate Services, serving the Long Beach and Signal Hill area, said the leasing market has started to see slight movement this year. Seen here, his office is located at 1240 E. 29th St. in Signal Hill. He served for 8 years on the American Industrial Real Estate Association's Board and was the president in 1992. (Photograph by the Business Journal's Thomas McConville)

Kevin Jones, a real estate office broker for Lee & Associates, said the Long Beach market has remained pretty much steady compared to areas in Orange County and Los Angeles County that were hit much harder by the mortgage crisis. He added that there has been a slight increase in "owner/user products," or tenants that bought property for their own use instead of subleasing, during the second quarter.

One notable sale, he said, was the purchase of a building at the Traffic Circle at 4300 Pacific Coast Hwy., which sold in July of this year to Farmers Insurance for \$2.1 million. In this economy, having any sale, Jones added, makes for a more optimistic view of the market.

In addition, Patrick O'Healy, owner of O'Healy Commercial Real Estate Services, said his 20-year career in the commercial real estate markets of Long Beach, Signal Hill and other regions has taught him that small business always picks up first during recessions. "Having gone through three other downturns, the harbinger is that small businesses start to pick up again," he said. "We're not doing a huge amount of activity, but we're doing deals in small buildings, so there's movement. I've had eight lease renewals in the last 10 months. Last year, I didn't have a single tenant renew a lease."

He also said the leases that are taking place are for a much shorter term. Tenants that once would sign on to three-year contracts are only looking for one to two-year deals. Due to the economy, much of the drop off is more psychological than really reflective of supply and demand, he said. For instance, vacancies have held steady while lease rates continue to fall. "It indicates (tenants) need the space, and we see those tenants expanding. But they don't have so much confidence where they're going to make a longer commitment," he said. "This is the only time in my career where I've watched rents go down and vacancies unchanged."

On the flip side, some businesses have announced or initiated the process of vacating building space all together, which continues to give back to the market. Cushman & Wakefield's report

indicates the Downtown Long Beach market saw 11,819 square feet of negative net absorption, which is the margin of available space leftover after more losses than gains. The suburban Long Beach market saw negative absorption of 27,079 square feet. Long Beach's office vacancy rate overall has increased slightly to over 20 percent, according recent reports.

Alperin said there have been slightly more losses than gains in office lease transactions for the second quarter, which could turn into a trend, but remains insignificant, given the entire square feet of office space on the market. For instance, there was a loss of 12,775 square feet of Class A building space, or buildings of higher quality, rents and standards, in the downtown submarket during the quarter. However, that's just a fraction of the particular submarket, which occupies a total of 1.8 million square feet and is roughly 80 to 90 percent occupied.

The most losses in Long Beach came from the Bixby Knolls submarket with 41,247 square feet put back on the market mainly due to "the addition of multiple spaces totaling 30,908 square feet at the 3711 Long Beach Boulevard Building," according to the Cushman & Wakefield report.

Additionally, Douglas Park, west of Lakewood Boulevard and south of Carson Street, has been left in a bit of a quandary after the real estate markets have turned this year following the new development of industrial and office buildings there. DeVry University was planning to move into 98,000 square feet of office space there, touted as the first transaction on the 54-acre site, however, it has apparently pulled out. Instead, it will stay at Kilroy Airport Center, its home since 1995, with only half of its current square footage.

Dan Dement, DeVry spokesman would say nothing more than the plan to stay was a corporate decision that would better fit its local enrolled students. "Plans are to stay put at the airport," he told the Business Journal. "We just determined that at this time a move would not be the best interest of our Long Beach campus students . . . and until we consider another option maybe further down the road."

Michael Soto, a real estate research analyst for Collier's International's South Bay regional office, agrees there has been more activity in the office side, noting that Long Beach has remained solvent compared with surrounding markets, while most of the activity in Los Angeles County continues in Torrance and El Segundo.

But, Soto added that large vacancies have also evened out the South Bay market. For instance, while leasing activity increased 15 percent over last quarter, the growth rate remains at a relatively low level with Boeing and Northrop Grumman consolidating large chunks of office space by the year's end. If Boeing didn't move out of four floors, amounting to about 100,000 square feet in El Segundo at 400 North Continental Blvd. in June, net absorption would have been positive, he added.

"It's actually just more of the same, especially when the market's

really down,” Soto said. “Cities really need to think of ways to attract companies. You are seeing companies moving . . . to those cities that can really attract and attain companies they already have. These tenants aren’t just looking at the rents, they’re looking at what is going to make these businesses successful.”

Residential:

Home Sales Down, Still Affordable

Both federal and state tax incentives for first time homebuyers have buoyed the housing market across the state and nation during the second quarter. But, after the federal program expired, some reports show home sales have already begun to decline much more than anticipated.

Consumers eligible for the federal tax credit had until April 30 to open escrow to qualify and had to close initially by June 30. The closing deadline, however, was extended to September 30.

A number of people raced to get their home deal consummated in time for the original deadline, and a drop in sales was expected once those tax credits ran their course. The state tax credit deadline, on the other hand, allows qualifying homebuyers to sign a deal by January 1, 2011.

July statistics released August 24 by the National Association of Realtors shows existing home sales across the nation as “sharply lower” than the previous month, falling 27.2 percent – and 25.5 percent from the same month last year. This is the largest percent change in sales during the 15 years the association has been tracking the bulk of transactions.

During the same day, the California Association of Realtors (CAR) released similar findings for July, showing home sales across the state having decreased 20.8 percent compared with the same month in 2009 and 11 percent from the prior month. “The national markets had a bigger decline than the California market, and I think both were a bit larger decline than we had originally anticipated,” said Robert Kleinhenz, CAR’s senior chief economist.

However, during the second quarter, as a whole, statewide home sales were down 3.5 percent from a year ago. In Long Beach, home sales were 7.1 percent lower, or about 473 homes on the market rather than 509, from the same quarter in 2009. He added it’s not uncommon for there to be fewer sales in the second quarter than the first.

In addition, the California housing market saw home prices adjust early on in the housing downturn, which changed the affordability calculation for the state’s housing, Kleinhenz said. California had a larger median price shift than the nation, with a 59 percent correction from the peak in 2007 to the trough in early 2009. “I think that probably buoyed or pushed sales in California more so than what happened in the national picture,” he said. “As we have tracked this, it appears as though, while it was difficult to deal with that price decline, California has been able to have a little bit better sales volume.”

Home prices for single-family residences have continued to edge upwards since the beginning of the year in Long Beach and throughout the state, which Kleinhenz said has been primarily driven by the amount of distressed properties on the market. The more distressed properties at lower end prices, the more sales activity.

While still maintaining a lower inventory of homes for sale, Long



The Aubry at Alamitos Ridge residential development is quickly taking form at View Ridge Drive and Redondo Avenue. It’s the newest residential construction currently in Long Beach with 14 acres of 85 new homes or detached condos. Construction is expected to be completed by September. There are four designs of the two-story homes as part of Lennar Home’s PowerSmart Solar Home system design, which comes with solar panels, tankless water heaters and other energy efficient functions for residents to save money on energy costs. The above models are available for viewing. (Photograph by the Business Journal’s Thomas McConville)

Beach, for instance, saw an 8.4 percent increase in the median home price from January’s \$350,500 price to the most recent median price in July of \$375,000.

Kleinhenz said home sales are expected to be weaker during the second half of the year and into 2011.

He added that there has been a mix of sales in the market for Real Estate Owned (REO) properties – those which have fallen back onto banks or mortgage lenders after an unsuccessful auction – and short sales, which allow distressed properties to go through the foreclosure process. Since short sales are at somewhat higher prices, there have been more sales of REOs in California. Overall, for the past year, at least 60 percent of the state’s market has consisted of some type of distressed sale, he said.

As far as financing, he added that availability to qualify for loans has improved compared to the beginning of last year. Jumbo loans, or loan values around \$750,000, have now returned to the market, which could suggest that financial lending is slightly recovering after lenders held back during the worst of the financial crisis. But the jumbo loans that are available come with higher down payments and more stringent underwriting standards than a few years ago.

Kleinhenz said that if government entities didn’t step into financially assist banks, then the real estate downturn would have been much worse. “We would really just have a trickle of activity in the housing market rather than what we have today,” he said. “We have low mortgage rates, home prices are significantly below peak and affordability in California is quite high. I think there’s an opportunity to become a homeowner.”

On the other hand, Jeremy Colonna, a broker and partner for Colonna and Co. Realty in Long Beach, said the tax credits have only compounded the housing market by basing consumer confidence on opportunities from the federal government rather than a general belief the market is getting better. “It’s a lot of what got us into this problem in the first place,” he said. “The second quarter numbers were really solid, but . . . the reasoning behind it wasn’t grounded in economics. [Tax credits were] a primary drive behind

the second quarter numbers, and . . . consumer confidence numbers speak volumes about how people perceive our market right now.”

In addition, Colonna said it's been a limited year for higher-end homes in Long Beach as most people purchasing in that income bracket have more uncertainty about the economy than lower end buyers who might be more willing to make a move.

Colonna said Long Beach home prices are already down 6 percent this year and could dip further. “Since the expiration of the tax credit, we are already seeing marked differences in the market, he said. “I’ve been telling my clients for the last year that I really see the market bottoming back out to the prices we were looking at first quarter 2008 and 2009.”

Mike Domino, a realtor for Main Street Realty, said the tax incentives succeeded at spurring interest from buyers and that the primary problem is in fact that the inventory of homes on the market has declined. “There just aren’t that many quality homes for sale,” he said. “Even for the short sales that are out there, there’s a very low amount of homes to choose from. The tax incentives are a big motivator and the hardest thing right now is there are buyers that are interested.” He added that some of the buyers have dropped out.

Domino said the main factors driving sales are price and location and that buyers care far more about the particular neighborhood than what’s going on at the national level or even state level. Long Beach is such a diverse area with a mixture of low-end and high-end neighborhoods that a median price doesn’t really reflect the city’s true housing market, he added.

With real estate intertwined with the local economy, he said most buyers are still uncertain. But historically low interest rates have been a silver lining, as some consumers have taken a chance in upgrading to larger homes.

Also, Domino predicts more statistics to come out with higher sales in the next few months since many homebuyers, spurred either by the tax incentives or lower interest rates, are still in escrow and haven’t closed yet.

New Developments

Although the recession has stalled most new residential developments, a few new projects are popping up in Long Beach.

After acquiring more than 14 acres of land at View Ridge Drive and Redondo Avenue, Lennar Homes is building a new community of 85 state-of-the-art homes, the most recent residential development in Long Beach. Neil Barnes, the developer’s home consultant, said the gated community, called Aubry at Alamitos Ridge, boasts energy-efficient “solar” homes and detached condominiums, complete with solar panels and tankless water heaters, at the footstep of Signal Hill. There are three different floor plans for the two-story houses, ranging from 2,055 to 2,477 square feet.

Lennar expects its open house to draw hundreds of people. “We’re ready to go full speed ahead,” Barnes said. “We should have people living here in September.”

In the downtown area, Gallery421, a new development of multi-family luxury residential apartments, has been recently completed and is ready for move-in. The apartment community features 291 units on West Broadway, north of Ocean Boulevard. Residents began moving into the upscale complex months ago, marking the third such structure by Lyons Communities in Long Beach.

Industrial: Increased Demand, Vacancy Rates Stagnant

The industrial market, largely dependent on port activity and distribution in the local area, saw some moderate signs of a continued uptrend in the second quarter, according to reports and brokerage firms.

For the most part, the Long Beach and Los Angeles ports have

seen much needed cargo return with an average 15 percent increase in cargo for the year after a significant downturn in trade in 2009.

Colliers International’s second quarter report on industrial space for the South Bay region shows the market saw positive absorption “for the first time in over two years.” The overall vacancy rate appears to be leveling out at about 5.3 percent, but Colliers notes it’s still well above the market’s long-term average of 2.9 percent. Sales and leasing activity, however, totaled 3.8 million square feet, according to the firm – the highest level of activity recorded since the recession began in late 2007.

Many industry experts have said the reduction in lease rates for the industrial market is at or near the bottom, with the average South Bay asking rate at 48 cents per square foot. Meanwhile, different real estate firms have reported different outcomes depending on how they calculate submarkets.

For instance, Lee & Associates actually reports negative absorption in the South Bay region for the second quarter with 486,093 square feet back on the market and vacancy rates climbing to 5.6 percent.

But, regardless, both firms agree that port activity has significantly increased and vacancy rates appear to be stabilizing.

Brandon Carrillo, industrial real estate broker for Lee & Associates, said compared to other markets that have vacancies in the double digits, the industrial sector has remained fairly healthy this year, although it’s hard to predict the future. “We’re in the recovery,” he said. “What’s tough is we really don’t have one thing you can say for sure, but we are certain it’s going to be a bumpy road.”

In addition, some commercial real estate investors have been bullish in the industrial market, gobbling up space for low rents, especially in the Inland Empire, where rates are even cheaper, he added.

Carrillo said Small Business Administration (SBA) loans with near 5 percent interest rates or less have made up about 95 percent of sales, including a deal closed on 6101 Orange Ave. in North Long Beach.

“That’s really been a lot of the volume on a lot of these deals,” he said. “That’s job creation. These are small businesses taking advantage of the low interest rates. It’s a great opportunity to buy real estate and expand your business because the SBA would allow you . . . to pick up capital for more machines for a building twice the size at a low interest rate.”

The largest transaction since the beginning of this year, according to Lee & Associates, is a sale in the LAX/EI Segundo area where over 1 million square feet of industrial development was sold in Hawthorne, which remains a positive sign as ports move into the “peak season.”

However, Ryan McClean, senior Los Angeles regional director for First Industrial Realty Trust, Inc., a Real Estate Investment Trust (REIT), said while there appears to be signs of increased port activity that has translated into more demand for industrial space, it doesn’t appear to be long term. Instead, he said, “I think there were a lot of tenants that already had buildings, and that capacity had to be used up.” He does believe, though, that the industrial market is better positioned than others.

“I don’t really cover other product types but, in general, from what I understand, industrial held up favorable,” he said. “Overall occupancy is still 95 percent, but still not a lot of outlays. Not a capital incentive product type. There are no more new buildings going up.”

During the second quarter, the Chicago-based REIT had announced a new multi-year lease agreement with exporter Advanced Logistics Management Inc. for a 173,000 square-foot distribution facility in Rancho Dominguez. ■