

Santa Maria Commercial Real Estate Update

Fourth Quarter 2016

Pacifica Commercial Realty

My name is Jerry Schmidt. I am one of the Principals of Pacifica Commercial Realty. My Company was founded (by others) in 1968 in Santa Barbara. Pacifica Commercial Realty is the Central Coast's largest, full-service commercial real estate company. We offer a wide variety of commercial real estate services including mainly commercial property management and brokerage for commercial properties throughout the Central Coast. We have six commercial brokers and/or agents in our Santa Maria headquarters, five commercial brokers/agents in our Santa Barbara Office, and four brokers/agents in our Paso Robles office.

I opened the Santa Maria office for Pacifica in 1989. I attended Cal Poly and played some football (real football), and in 1987 I got my start in commercial real estate working in the Silicon Valley as an Industrial/R&D specialist. I am the Senior Industrial Real Estate specialist in our office. I also serve the City of Santa Maria as a Reserve Police Officer, and had served on a number of Nonprofit Boards, currently on the Santa Maria Police Council Board.

The focus on my presentation today is going to be Industrial Real Estate (vs. Retail or Office), although I will brush on those two as well. Generally, the 'Commercial' Real Estate Market is comprised of 3 distinctly different Segments: Industrial/Office/Retail. Most of my work over the past nearly 30-years has been done in the Industrial Sector with some some work in the Office Segment related to R&D Office, Corporate Office or larger Medical Office. However, some recent significant Retail projects that my company has taken on, have required me to work on larger Retail sites as well. I am going to touch base on the Office and Retail segments of the market as well as briefly mention several new Developments that will affect the Santa Maria Valley.

Commercial vs. Residential Real Estate

In case you haven't noticed, there is quite a bit of activity in the Residential Real Estate Sector. However, there's not really a direct tie-in between Commercial real estate and Residential real estate. So the effect of market variables (Supply, Demand, Rising Prices/Decreasing Prices) in residential real estate are not automatically mirrored in the commercial real estate market. There are 'common trends' that affect both areas of the real estate market, but there isn't necessarily a direct correlation between the two segments of the real estate market. There are even further differences in between the various segments of the Commercial Market.

Santa Maria Industrial Real Estate: Historical Growth

The past four or five years have been pretty significant for Industrial Segment of the Santa Maria Valley Commercial Real Estate Market. Historically, Santa Maria has had an overall Industrial Vacancy Factor (Vacant Buildings) of about 4 to 8% Citywide. That number generally represented +/-300,000 to 800,000 square feet of vacant space using a total Industrial Base (vacant & occupied buildings) of +/-5 to 7 million square feet (depending upon the time period being evaluated). In addition to the vacant buildings, there are always projects 'under construction' or in the development pipeline. However, for the purpose of our tracking, those were never included in our Vacancy Surveys until the buildings were available for occupancy. We have been tracking the Vacancy Factor of Industrial RE since the early 90's.

Nothing before 2011 really matters in the RE market because 'life changed' during "The Great Recession". When we first pulled our collective heads out from under the water in about 2011, Santa Maria had the highest Vacancy Factor we had ever seen in Santa Maria. At that time our Industrial Base was +/-7.5 million square feet and our Vacancy Factor was about 10%. However, we weren't hit anywhere

near as hard as other areas around the Country. The Central Coast really didn't experience outrageous inflationary pricing and associated overbuilding that other areas experienced. So, our 'fall to the bottom' wasn't that bad. Conversely, we didn't have too far to 'climb out of the pit'. At that time, we were even a bit bullish. We predicted that the lure of the Central Coast would continue to attract investors and users, so our absorption rates would likely be fairly high.

Here's the good news: Of the +/- 750,000 square feet of vacant industrial and/or R&D Office buildings we had at that time, pretty much all of those buildings have been leased or sold since 2012. In addition, Santa Maria has added another +/-1.5 million square feet to its Industrial Base (and most of THOSE buildings have been either leased or sold). We have the largest Industrial Base and the lowest Vacany Factor IN RECORDED HISTORY. We currently have over 8.5 million square feet of Industrial Buildings and **our overall Vacancy Factor is +/- 1.91%**

Here are some of what we believe are significant Transactions that took place in a relatively short period from 2012 to 2015 (Sales, Leases, or Build-to-Suits):

TRANSACTIONS OF INTEREST

- 1) ***Linneage Logistics***: a large-scale Freezer/Cold Storage facility of +/-225,000 square feet on La Brea Drive.
- 2) ***Gold Coast Packing***: +/-67,000 square feet of cooling and packing facility.
- 3) ***2100 South Blosser***: 58,000 of R&D Office sold to Rabobank in 2015 and transformed into their Regional Banking Center.
- 4) ***2240 A Street***: This was a former Cabinet Shop that unfortunately did not survive the blood-letting of 2011. We sold the site to Red Dog Management, an Ag related Labor Contractor. An interesting note: Almost all of the *A Street Business Center* has been leased or sold. Most of the buildings on both sides of A

Street from Betteravia to McCoy have been sold, at some of the highest prices found in the market...well north of \$125 per square foot; and most of those sales were to owner/users.

5) 2811-2815 Airpark Drive: This 36,300 square foot R&D Building was built in the late 80s, was home to Comtel/Spar, Gary Player Golf, Rhino Marketing, Computer Sciences Corporation, UPS Teleservices, and Fusion Marketing Systems. Then we sold it to Café FX, and then again to Santa Maria Energy, and finally to a Developer in 2015. Last year, ½ of the space was leased to DCCA (Data Computer Corporation of America...a VAFB related Computer firm out of the East Coast), and most of the other ½ was leased to MindBody, a software company headquartered in SLO. There are currently +/-125 new, high-tech jobs once again in that building, and there is room to add more buildings on that site.

6) Fairway Industrial Center: Two beautiful new 50,000 sf Distribution/Warehouse buildings built on 'spec' and completed at year-end 2015. Only one remains available. In 2015 we leased one of the buildings on a long-term basis to Wine Direct, a wine fulfillment company based out of Napa. The second of the two buildings is currently available, but we are working on two offers that will require splitting the building into two 25,000 sf spaces.

7) 2615 Skyway Drive: This site is a +/-10,000 sf Industrial Condominium within Fairway Technology Park. It was sold to Monaero Engineering in 2015. Monaero tried to purchase 2811 Airpark but came to the dance late (it was in escrow). Currently, FTP is almost full. We have one 6,000 sf space available there.

8) Zodiac Aerospace: in 2012, we leased the former 82,000 sf Den-Mat facility located at 2850 Skyway Drive to Zodiac Cabin Interiors and the site went through a considerable remodel. Then in 2014, we leased the 75,000 sf former Den Mat Headquarters across the street at 2727 Skyway Drive to Zodiac Seat Shells. For reference, there are two Zodiac Divisions in Santa Maria, one is very busy (Cabin Interiors) and one (Seat Shells) has undergone some layoffs and will likely have

one more round before they stabilize. The good news is: as Seat Shells slows down, Cabin Interiors' growth is increasing (at a higher rate).

9) 807 West Main Street: For any of the old-timers here, this 40,000 square feet of older metal buildings was originally home to M&S Pipe and Supply. We sold the site to a partnership of Red Dog Management and Maxco in 2015. The site is now an ag-related manufacturing operation.

10) Skyway Business Park: These 12 buildings across from the Airport, built in two phases from 1979-1983 retained a very high occupancy during the downturn. Even though they experience a 25% vacancy in 2010, SBP is once again near 100% occupancy.

11) Airport Plaza: This site is approximately 75% complete. Originally +/-40,000 square feet of Auto Sales and Service, it is being transformed into Retail, Restaurant, and Office space.

There are also several exciting new projects on the board:

New Developments:

•**Fed Ex:** +/-160,000 square foot Ground Transportation facility under construction where the former Sunset Ridge Golf Course was located on Fairway Drive.

•**Aerostar Commerce Center:** This will be a new, +/- 12 building complex new to the new Fed Ex site. If all things go according to plan, we will have several privately owned Hangar Buildings available for sale. The remaining buildings will be 5,000 sf to 25,000 square feet and available 'For Sale' or 'For Lease'. This is a very exciting and promising Project.

•**Betteravia Plaza:** This site used to be part of the Santa Barbara Research Facility/Hughes Aircraft Company site on Betteravia. The remaining land, +/-57 acres was rezoned into Retail, Office, and Multi-Family. Hopefully, ground-breaking will occur in mid-2017.

Industrial Land: ‘Lots’ For Sale (not)

Our current available inventory of industrial land is fairly depleted. There is a 6 acre site on La Brea for sale (zoned M2) that can be bought in the +/--\$6.50/sf range; a couple of 2 acre Lots on West Betteravia that are being priced closer to \$10/sf; one 2-acre site on A Street listed at \$7.75/sf, and a couple of other small in-fill sites in the \$7 to \$10/sf range. There are currently no (zero) privately owned, large sites, ready to develop sites in the 10+ acre size range that are ‘For Sale’ and zoned Industrial. The City of Santa Maria has one large site they are holding out for development to a user who will bring a large number of clean, high paying jobs, who wants to build in an area surrounded by Ag Users.

AREA 9

Some of the larger sites that are ‘close to’ available are the result of Annexation of Area 9. Area 9 was a +/-900 acre Annexation site bordered roughly by Betteravia on the south, Black Road on the west, Stowell Road on the north, and A Street on the east. Area 9 was intended to add to our Industrial inventory. Almost immediately, Windset Farms bought a significant chunk to add to their existing Greenhouse operations. Currently, the biggest stumbling block for Area 9 sites relate to the lack of infrastructure (mainly Fire service). City Utilities for the most part end at Betteravia and A Street. Last year there weren’t too many significant land sales, again because there isn’t much available to be sold.

Santa Maria Public Airport District

There have been discussions at their Board level as to what the SMPAD should do/could do with their developable land since we opened in 1989. In the early 90s they funded an assessment for their proposed Research Park. During a meeting we attended, someone stood up and said, “Santa Maria has enough vacant industrial land to meet our growth needs 50 years, so we don’t need a Research

Park” (this gentleman was obviously not in favor of the project). We refuted that claim and proposed that we would run out of developable land within 20 to 25 years. Based upon our tracking of absorption, without the Research Park Santa Maria would effectively limit their ability for solid growth. Area 9 will help (if a plan to provide infrastructure can be found other than to charge it to the first company to develop). I believe they’ve petitioned the FAA to release certain parcels of land for development purposes. However, there is no public information available as to what is happening with Airport land (other than a ton of real estate signs, and Minutes to their Board Meetings mentioning their petition to the FAA). Santa Maria will certainly benefit if/when the Airport District decides to make their land available for development. The Chamber might suggest a better job of promoting what they have, what they will have (or even hope to have). *Maybe someone might consider a website that prospects could use.*

Current Santa Maria Commercial Real Estate Values

Glenn asked me to provide an idea of where the Commercial Real Estate Market values are currently standing. As a general Summary:

Industrial Building Lease Rates

- **High-end space:**

Over 50,000sf \$.50-\$0.75/sf, NNN

20,000-50,000 \$.50-\$0.75/sf, NNN

Under 20,000sf \$.55-\$0.85/sf, NNN

- **Lower-end space:**

\$.55-\$0.60, Gross

Industrial Building Sale Prices

- **High-end space:**

Over 50,000sf \$80-\$120/sf

20,000-50,000sf \$90-\$130/sf

Under 20,000sf \$100-\$130/sf

- **Lower-end space:**

\$75-\$100/sf

OFFICE (Medical Office not included)

- **Lease Rates: \$1.00-\$2.00/sf, NNN**
- **Sales Prices: Over \$200.00/sf (with some sales at +/- \$300/sf)**
- **Nothing in excess of +/- 9,000 sf currently available**

NEW RETAIL PROJECTS/REDEVELOPMENT

- **Development on North Broadway**
- **Enos Ranch**
- **Betteravia Plaza**
- **Santa Maria Town Center Mall**

SUMMARY

In closing, The last five years has been a very interesting period in the commercial real estate market here in Santa Maria. They were very good years:

- We have a the lowest Vacancy Factor that we have recorded in our nearly 30 years in Santa Maria;
- Most of the large freestanding Industrial Buildings in Santa Maria have been sold or leased.

I was also asked me to provide an Industrial Forecast for 2017:

My forecast can be summed up in four words: “We need more inventory”. Even with what would be described as ‘normal’ demand, we expect the overall vacancy factor in the market to continue to decline (because we have very few buildings available). Furthermore, we expect to see lease rates increase market-wide as the remaining inventory of available buildings and land continues to decrease. Thank you for the opportunity to meet with you today and provide our opinion of conditions in Santa Maria’s Commercial Real Estate Market. I would be happy to entertain any questions you might have.