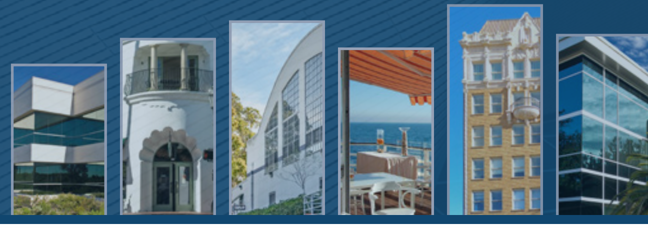
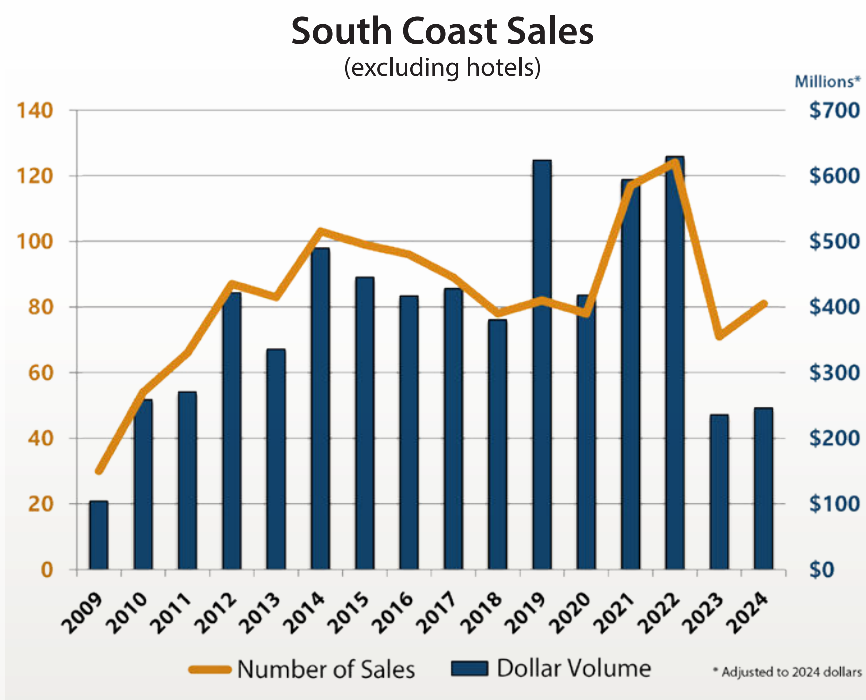


COMMERCIAL SALES: Finishing Strong

The relatively limited commercial sales volume that characterized 2023 continued in 2024, although there was a significant ramping up of transactions in the fourth quarter. Activity remained heavily weighted toward relatively low-price properties, as elevated interest rates impeded buyers in higher price ranges. The non-hotel volume of $245 million was a slight increase over 2023, but otherwise was the lowest total since 2009.

The pronounced upswing in Q4 resulted in 28 transactions valued at $109 million, which was a striking year-over-year rebound from 13 sales totaling $68 million in Q4 of 2023. In fact, it was the highest Q4 result by either measure since 2021. This increased activity may indicate an inflection point in the sales market, potentially marking the first step toward recovery from the stagnancy of the past two years. On the other hand, the fourth quarter of most years features a seasonal bump in sales, which must be taken into consideration. And with interest rate cuts in 2025 expected to be limited, any growth in sales volume is likely to be gradual.



The large gap between transactions (orange curve) and volume (blue bars) indicates that the average sale price was much lower in 2023-2024.

Price Sensitivity

Since early 2023, the sales market has been dominated by lower-price transactions, which we have been defining as up to $5 million. Higher interest rates have had a much greater impact on higher-price property sales by limiting buyers' appetite for (or access to) larger loans. Uncertainty over future revenue from large office and retail properties is another factor that has made investors more cautious about high-dollar acquisitions, especially those without long-term tenants in place.

The South Coast's largest commercial building, 1 N Calle Cesar Chavez, was purchased by a local investor in Q4 for $36.5M.

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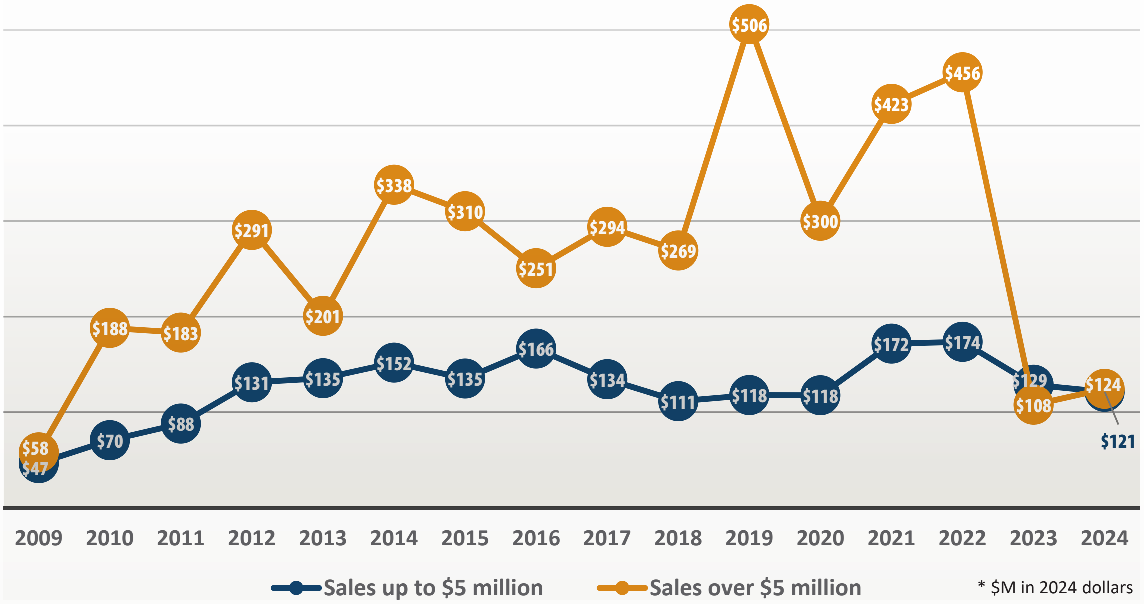
Dollar Value of Sales Below and Above $5 Million

(excluding hotels)



Splitting sales into two buckets based on price illustrates the dramatic impact of the rapid rise of interest rates on sales over $5 million, shown in orange. By comparison, sales up to $5 million have held relatively steady.

The ten years prior to 2023 averaged 26 sales above $5 million annually. By contrast, the average for 2023 and 2024 tumbled to 13 sales, or half the prior 10-year level. For dollar volume, the drop-off was even steeper, as shown in the graph above. The average for the last two years was $116 million, a 65% decrease from the prior 10-year average of $335 million. Evidently, the current lending environment is far less of a hinderance in the lower price tier. For sales less than $5 million, transactions and dollar volume decreased only 9% and 12% respectively, compared to 10-year averages.

The retail/office buildings at 250-270 Storke Rd in Goleta were purchased by a local investor in Q4 for $10.5M.

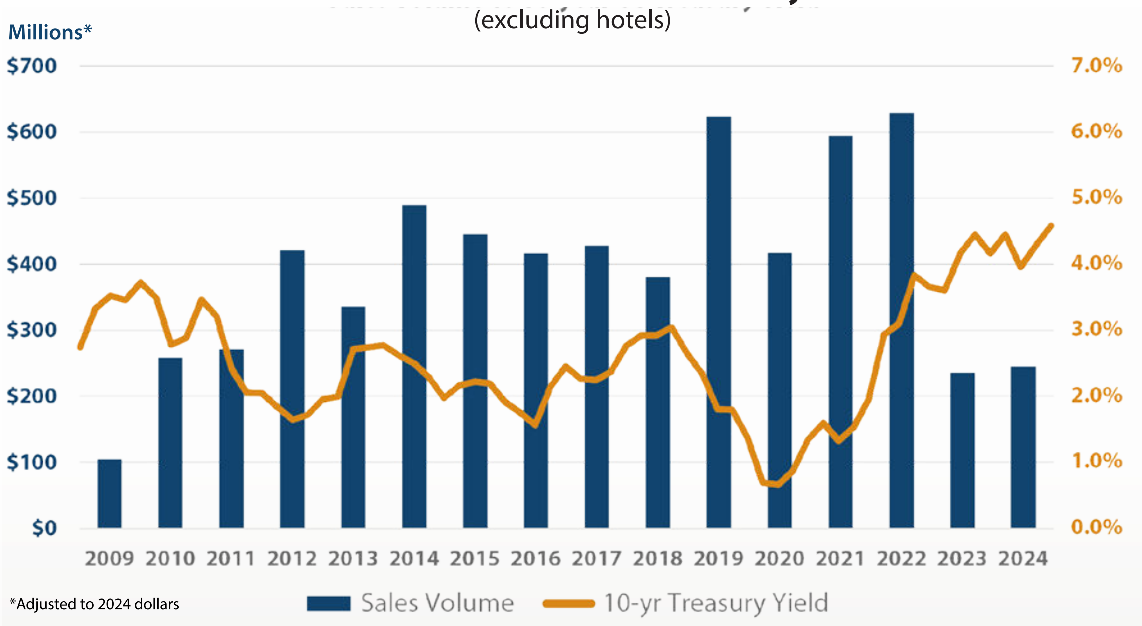
Interest Rates

While tempting to view the growth in sales at the end of the year as a response to the Fed's 2024 interest rate cuts, the reality isn't so simple. Real estate interest rates did come down briefly after the Fed's September cut, but rates drifted back up after that. And surprisingly, the subsequent cuts by the Fed in November and December did not induce a corresponding decrease in real estate interest rates (more on that later). However, seeing the Fed cut rates for the first time in several years did appear to have a psychological effect on some commercial buyers, bringing more active demand to the market.

To visualize the relationship between interest rates and commercial sales, the graph on the next page shows South Coast dollar volume over time, overlayed with the 10-year Treasury Bond yield curve. The 10-year Treasury yield closely resembles changes in interest rates for real estate loans over time, and is a useful proxy for this comparison. The graph indicates the correlation, in which changes in the yield (interest rates) have an inverse effect on sales volume. The impact is most pronounced during the last five years, when the prolonged period of sub-2% yields coincided with record high sales volume, followed by

Sales Volume vs 10-Year Treasury Yield

(excluding hotels)



*Adjusted to 2024 dollars

The 10-year Treasury Yield curve in orange is a useful stand-in for real estate interest rates. While interest rates aren't the only factor affecting commercial sales volume, the correlation is evident in this comparison.

the major drop in sales volume after the 10-year Treasury yield climbed steeply and toward 4% in 2022.

The graph also shows that the 10-year Treasury yield did not come down at the end of 2024 in tandem with the Federal Funds Rate. Real estate loan rates, like the treasury yields, are in an unusual phase of divergence from the Fed's benchmark rate. This "inversion" creates a layer of uncertainty and tension in the market, but more importantly means that debt continues to be relatively expensive for buyers.

Who's Buying

All told, investors were largely on the sidelines in 2024, making only 38 acquisitions, the lowest count since pandemic-stricken 2020. However, all 10 transactions over $5 million were investment sales, and half of those closed in Q4. The most substantial of the Q4 deals were the 208,000 SF Vercal building at 1 N Calle Cesar Chavez, purchased for $36 million, and 250-270 Storke Rd purchased for $10.5 million. High-value sales have been sparse for nearly two years, so this cluster of sales in Q4 indicates a shift in posture among investors. Of the year's 10 sales over $5 million, four were purchased with cash, and the average estimated interest rate to finance the other six was 6.5%.

Owner-user buyers played a larger role in 2024 than the previous year, completing 43 sales, which is on par with the 5-year average. Three of the more notable sales occurred in Q4: a Valvoline franchisee purchased the automotive property at 932 De La Vina St; members of the Karpeles family purchased 21 W Anapamu St, the longtime home of the Karpeles Manuscript Museum; and Allen Associates construction purchased 201 N Milpas St,

The office building at 411 E Canon Perdido St was purchsed for $6.7M by an investor/developer with plans to repurpose the property.

where its offices have been located for many years. Not surprisingly given higher interest rates, owner-user sales continued to favor the lower price ranges. All of the owner-user sales were under $5 million, and more than 80% were under $2.5 million. Among those owner-user sales over $2.5 million, half were all-cash buyers.

Off-market sales are on the rise. For the year, 43% of transactions and 55% of dollar volume were off-market deals. Both ratios represent increases of roughly 5% compared to 2023, and provide another indication that buyer demand and owners' willingness to sell appear to be gradually converging.

Property Types

With 26 office sales, 2024 was on par with the 5-year average transaction count. However, just one office property above $5 million changed ownership, and dollar volume for the year was only $40.5 million, the lowest total since 2009. There were an unusually high number of office condos sold, including six sales averaging $200,000 each at the 5290 Overpass Rd complex. The year's largest office sale was the 17,200 SF building on an acre at 411 E Canon Perdido St, which traded in Q4 for $6.7 million. Reportedly, the buyer plans to convert the property to a non-office use. One positive note is that there were 10 office sales in Q4, and hopefully that momentum will carry into 2025.

Annual dollar volume of industrial sales was 34% over the 5-year average, thanks primarily to the Q4 sale of 1 N Calle Cesar Chavez, the largest commercial building on the South Coast. Earlier in the year, 6338 Lindmar Dr in Goleta sold for $11.1 million. Industrial is a favored asset class among investors, but opportunities to buy are rare on the South Coast. Despite the boost in dollar value, the modest number of sales (13) was 29% below the 5-year trend.

Retail sales for the year numbered 27 transactions, a 19% increase over the 5-year average. A trio of substantial Q4 sales helped bring the dollar volume for retail property to $93 million, which is in line with the recent historical average. Largest of these was the previously noted $10.5 million sale of 250-270 Storke Rd, two buildings totaling 32,500 SF next to Target in Goleta. The other two, 330 State St and 3890 La Cumbre Plaza Ln in Santa Barbara, both traded above $6 million.

Looking Ahead

The closing of five relatively high-priced sales in Q4 hints at renewed demand from investors, and after about two years of a pricing impasse, more sellers may also be more willing to accept the current conditions and make a deal. Properties that are priced accurately are attracting offers. On the other hand, interest rates for real estate loans so far have not come down as hoped, and given ongoing uncertainty about inflation, tariffs, and other economic factors, the projections for interest rates during 2025 are tenuous. The increase in activity at the end of 2024 does indeed justify cautious optimism for improved sales momentum in 2025, but realistically the growth in sales (if any) will likely be modest.

COMMERCIAL SALES OVER $5 MILLION

Address	City	Property Type	Quarter	Sold Price	Bldg SF	Land SF	Buyer Type	Market Status
1 N Calle Cesar Chavez	Santa Barbara	Industrial	4	$36,500,000	208,228	324,086	Investor	Off-Market
121 E Mason St, etc	Santa Barbara	Retail/Industrial	1	$19,000,000	36,000	90,165	Investor	Off-Market
6338 Lindmar Dr	Goleta	Industrial	2	$11,100,000	66,178	199,069	Investor	Market
250-270 Storke Rd	Goleta	Retail/Office	4	$10,500,000	32,532	98,010	Investor	Market
411 E Canon Perdido St	Santa Barbara	Office	4	$6,700,000	17,265	46,174	Investor	Market
330 State St	Santa Barbara	Retail	4	$6,700,000	13,791	28,314	Investor	Market
3890 La Cumbre Plaza Ln	Santa Barbara	Retail/Office	4	$6,375,000	11,451	13,504	Investor	Off-Market
1200 Coast Village Rd	Santa Barbara	Retail	3	$5,600,000	2,250	15,246	Investor	Market
5387 Overpass Rd	Goleta	Industrial	3	$5,172,500	9,871	29,621	Investor	Market

OFFICE LEASING

Combined South Coast office vacancy changed little during 2024, as contraction of inventory in Goleta was offset by expansion in Santa Barbara and Carpinteria. Total dollar consideration was $60.7 million, a decrease of 27% from the 5-year average. Rents continue to hold relatively steady, but demand for large spaces is weak, which is the main cause of the drop in consideration.

South Coast office leases have claimed about 20% less square footage, on average, since 2020 than during the years before the pandemic, and our assumption is that remote work caused most of that decrease. Nationally, several high-profile corporations (and even the federal government) are requiring employees to work at the office, or at least work most days at the office. From what we hear, many local employers have been experimenting with similar policies since the end of the pandemic, and the renewed national attention to this trend will likely ripple through the South Coast as well. However, one key factor complicating return-to-office requirements in our area is the relatively high cost of living, especially housing, which can make it more difficult to recruit employees to move here, and also to remain here over time as their housing needs evolve.

Goleta

Following very active leasing in 2023, Goleta's office market was quiet through Q3 and then picked up momentum in Q4 with 13 transactions covering 89,000 SF. In spite of the late surge, gross absorption of space for the year was 30% below the 5-year average. Nevertheless, vacancy remains relatively low at 6.2%, and deals in progress so far in Q1 of 2025 are likely to bring vacancy down in the near term. The South Coast's largest 2024 office lease was 29,800 SF at 5383 Hollister Ave signed by Sutter/Sansum for 10 years. The deal is also notable because most of the space is on the second floor, and demand for second-floor space in Goleta has been scarce in recent years.

Renewals were prominent and comprised 56% of the gross leased area in 2024. Four of the five largest transactions were renewals by Raytheon, Resonant, CACI, and Tecolote Research, which retained 20,400 SF at 420 S Fairview Ave in Q4. Google continued to grow its presence in Goleta, signing a Q4 deal adding 12,600 SF to existing space it holds at 6868 Cortona Dr. Bardex also increased its footprint in Goleta, signing 11,100 SF at 130 Robin Hill Rd, which proved to be the largest new lease of Q4.

Tecolote Research renewed 20,400 SF at 420 S Fairview Ave in Goleta, one of several large renewals signed in Q4.

About 40% of Goleta's available inventory is sublease space, including the three largest current offerings: 43,600 SF at 50 Castilian Dr, 29,300 SF at 6500 Hollister Ave, and 22,900 SF at 425 Pine Ave. Another 16,900 SF is still for sublease at 71 S Los Carneros Rd. Average asking rates are the highest we have seen, and the average achieved rate continues to rise, showing 5-year growth of 18%.

Santa Barbara

In Santa Barbara, the 96 office transactions in 2024 was on par with the 5-year average, though gross absorption decreased 12%. Available office space has expanded 36% since two years ago. This is primarily due to the move by Sonos to Goleta, which accounts for nearly 88,000 SF of available space downtown. The vacancy rate of 10.3% is near the historic high.

While Sonos' departure didn't help, the current phase of oversupply began during the pandemic. Specifically, demand for large spaces plummeted during the pandemic and still has not recovered. Comparing the current Santa Barbara inventory to five years ago (year-end 2019), the number of available spaces under 5,000 SF is almost the same (56 vs 57). However, for spaces over 5,000 SF the current inventory is nearly double the 2019 level (30 vs 16). With many employees still working remotely at least part of the time, companies are leasing less space. The median Santa Barbara office lease in 2024 was 1,912 SF, which was 19% smaller than the 2019 median.

The shift in demand has also affected rents. The average achieved rent for spaces over 5,000 SF has decreased 20% since 2019. Of course, rent is still very dependent on the quality of the space. Larger spaces can still command high rents if they have a desirable location, amenities, and a modern buildout, but the trick is finding a tenant seeking that size space.

A recent case in point is the 14,000 SF third floor of the former Sonos building at 25 E Mason St in the Funk Zone, which was signed by a local company in Q4. The space offers a trendy location, recent creative/tech buildout, and ocean views. As a result, the rent per SF was 39% higher than average for spaces over 5,000 SF. On the other hand, the space was on the market for 16 months because tenants looking for large spaces are rare in the current market. The second floor of the building, which is very similar space, is still available.

Another notable Q4 signing was the 12,000 SF renewal at 1 N Calle Cesar Chavez by HG Insights. The software company has saved a lot of money since moving to the industrial/flex Vercal Building over a decade ago, paying substantially less rent than it would in just about any office building in the city (and, by the way, less than half the rent just signed at the third floor of 25 E Mason St). In another Q4 renewal, Compass Realty secured its 5,000 SF space at 801 Chapala St for another five years.

Photo courtesy Radius Group

25 E Mason St in Santa Barbara is a former Sonos building in the Funk Zone. The top floor was leased in Q4 by a undisclosed tenant.

Carpinteria

Q4 brought little change to Carpinteria's office market, which is carrying excess supply and minimal leasing activity. There were only two small transactions in 2024, both signed by midyear. The 19.3% vacancy rate is the highest year-end rate we have seen. There is still over 80,000 SF of sublease space offered by Procore and Agilent, which makes up nearly two thirds of the availability.
As the buzz increases around upcoming opening of Linden Square in downtown Carpinteria, it's worth noting that the project includes about 4,900 SF of office on the second floor, which is marketed as small executive offices. The space is adjacent to the planned terrace bar, meaning happy hour will be just a few steps away.

RETAIL LEASING

After a very strong start, South Coast retail leasing lost momentum in the second half of 2024, and only 15 deals were signed in Q4. Nevertheless, the tally for the year was a robust 86 transactions, 15% higher than the 5-year average. Vacancy remains relatively low at 3.2%

True to the recent trend, there were few leases of large spaces, as there continues to be a shortage of tenants to fill larger vacancies in the area's shopping malls and on State Street. At the other end of the size spectrum, smaller spaces are seeing both high demand and high turnover, as many (mainly) local and regional businesses claim small stores or restaurant spaces to try or expand their concepts. Even with above average transactions, the focus on smaller spaces resulted in less leased area, and gross absorption ended up 15% below the 5-year average.

In the year's only "big box" transaction, Cost Plus World Market signed an extension on its 24,000 SF space at 610

State St in Santa Barbara. However, it may not remain a fixture of downtown retail for long because the landlord has the right to terminate the lease, and the space is on the market. Speaking of downtown fixtures, the 31,400 SF 24 Hour Fitness space at 820 State St was also recently brought to market.

State Street leasing kicked into a higher gear in 2024 with 22 transactions on the retail corridor, the highest count in five years. On top of that, five State Street retail properties (330, 532, 636, 922 and 1305) were purchased in 2024. The Q4 leases along the State Street retail corridor included Art & Soul Gallery at 1323, Art Essentials at 1207, Lighthouse Skate Shop at 907, and Rolld Ice Cream at 819-A (facing the Pavilion). In addition, Sephora leased the 6,100 SF former Athleta space at 733 State St, where it will relocate from the interior of Paseo Nuevo.

Despite all the leasing activity, State Street's storefront vacancy rate only decreased slightly from 13.7% to 12.9%. Meanwhile the perceived vacancy of dark storefronts ticked up a bit to 9.2%. Recent departures and announced closings include long-time tenants like 24 Hour Fitness previously mentioned, CVS at 1109 State St, Billabong at 631 State St, and Volcom at 625 State St. Pascucci restaurant will soon close at 509 State St after more than three decades on State Street. While many of these businesses will be missed by locals, the arrival of fresh storefronts, combined with the new Community Benefit Improvement District (CBID), will hopefully contribute to the rejuvenation of downtown.

Montecito is also seeing some turnover, with a number of recent retail closings on Coast Village Road. Demand there is strong though, and new tenants are on the way following Q4 signings by Healing Arts Spa at 1236, Everything But Water bathing suits at 1253, and The Agency Realty at 1046. The only currently marketed space is 900 SF next to Ca' Dario at 1187 Coast Village Rd.

In Goleta, only four leases totaling 10,000 SF were signed during the past two quarters, and gross absorption for the year was 42% below trend. The vacancy rate notched up as a result, but is still only 2.7%, and rents have not suffered. The Target center at Hollister and Storke is getting some attention as the in-line building near Hollister Avenue is getting a new façade, a new address (now 6865 Hollister), and the landlord is marketing over 17,000 SF there in an effort to bring in new tenants. So far Giovanni's Pizza is the only new lessee announced. Across the parking lot, as mentioned in the sales summary, the buildings at 250 & 270 Storke Rd, which include Ca' Dario, Dune Coffee, Chipotle, Rusty's Pizza, and others, changed ownership in Q4. Speaking of Rusty's, in Q4 they leased the 3,500 SF restaurant building at 6583 Pardall Rd in Isla Vista (formerly Giovanni's Pizza).

24 Hour Fitness is not renewing its lease at 820 State St, which has brought 31,400 SF to the market in downtown Santa Barbara.

INDUSTRIAL LEASING

Goleta had only 16 industrial transactions during 2024, which was well below the recent norm. However, the deals averaged over 15,000 SF, and gross absorption for the year ended up 8% above the 5-year average. There were four leases over 35,000 SF: Mammoth Moving renewed 42,700 SF at 5390 Overpass Rd in Q1; Redwire Space leased 42,600 SF at 326 Bollay Dr in Q2; Karl Storz leased 35,200 SF at 147-151 Castilian Dr in Q3; and Sonatech renewed 39,900 SF at 879 Ward Dr in Q4. The Karl Storz space at 147-151 Castilian Dr is available for sublease, and Restoration Hardware is occupying most of it on a month-to-month basis. Spaces recently added to the market include the 11,700 SF warehouse/R&D building at 6780 Cortona Dr and a 4,500 SF woodworking shop at 87 Santa Felicia Dr. The vacancy rate in Goleta is relatively low at

3.2% and achieved rents were up 15% compared to the 5-year average.

In Santa Barbara, the leasing activity was weighted toward smaller spaces in 2024, with most of the spaces being under 3,000 SF. The two largest spaces were signed in Q4, as a car storage tenant subleased the 12,700 SF "Hangar" building at 201 W Montecito St, and PANOS Brands leased 10,700 SF at 430 E Gutierrez St. Achieved rents for the 18 transactions ranged widely from $1.45 to $4.99 Gross per SF, depending on the location and type of use. As ever, vacancy is very slight at 1.3%, which (believe it or not) is the highest year-end vacancy in four years. Recent arrivals on the market include 14,300 SF at 415 N Salsipuedes St and 6,500 SF at 519 E Gutierrez St.

In Carpinteria, the largest industrial lease of the year came in Q4, as Dakar renewed 19,400 SF at 1015 Cindy Ln. The only other Q4 transaction was a 5,795 SF lease at 5045 6th St. Gigavac is newly offering 40,000 SF for sublease at 6382 Rose Ln, a space it has occupied since 2012. Another substantial recent availability is the 22,000 SF industrial/showroom building at 1120 Mark Ave. These offerings have helped bring the vacancy rate to its highest level in almost 15 years at 7.3%.

Sonatech signed a Q4 renewal for 39,900 SF at 879 Ward Dr in Goleta. They have been in the building for 8 years.

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LEASING MARKET DATA

	Market	Vacancy Rate		Transactions		Gross Absorption (SF)		Achieved Rent (PSF GR)	
OFFICE	Santa Barbara	**10.3%**	+3%	**96**	-5%	**300,062**	-20%	**$3.04**	-9%
OFFICE	Goleta	**6.2%**	-22%	**36**	+9%	**252,222**	-51%	**$2.32**	+4%
OFFICE	Carpinteria	**19.3%**	+150%	**2**	-71%	**4,035**	-87%	**$2.16**	-5%
RETAIL	Santa Barbara	**3.3%**	+4%	**60**	+5%	**137,763**	+1%	**$4.49**	+13%
RETAIL	Goleta	**2.7%**	+15%	**16**	-11%	**33,675**	+5%	**$3.48**	+7%
RETAIL	Carpinteria	**4.6%**	-13%	**10**	+11%	**17,480**	+37%	**$5.09**	+9%
INDUSTRIAL	Santa Barbara	**1.3%**	+59%	**15**	-38%	**57,455**	-68%	**$2.66**	+37%
INDUSTRIAL	Goleta	**3.2%**	+31%	**16**	-20%	**252,508**	+49%	**$1.92**	+9%
INDUSTRIAL	Carpinteria	**4.0%**	+84%	**7**	+250%	**60,536**	+83%	**$1.48**	+31%

Change percentages are compared to 2023 values.

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805.898.4369

Caitlin Hensel
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