Los Angeles West 2022 Year-End Report

Though the volume of layoffs seems significant, the tech industry is the sector contracting the most. Employees in Tech, however, make up roughly 2% of the labor force, so losses thus far have not had a meaningful economic impact. Otherwise, the job market is still strong with the most growth in healthcare, hotel and leisure, and personal services, but the sector of office-users (finance, insurance, real estate, and legal) is increasing as well.

Tech companies that grew headcount significantly in the last two years are scaling back and evaluating office space needs. Traditional office-using companies are still building on the strategy that the office is a crucial part of the collaborative environment and focusing on creating intentional workplaces. The customized, hybrid workplace encourages employees to use the space in a meaningful and productive way. Additionally, coworking has become a cornerstone for many companies looking for maximum flexibility and growth opportunities.

RAISE

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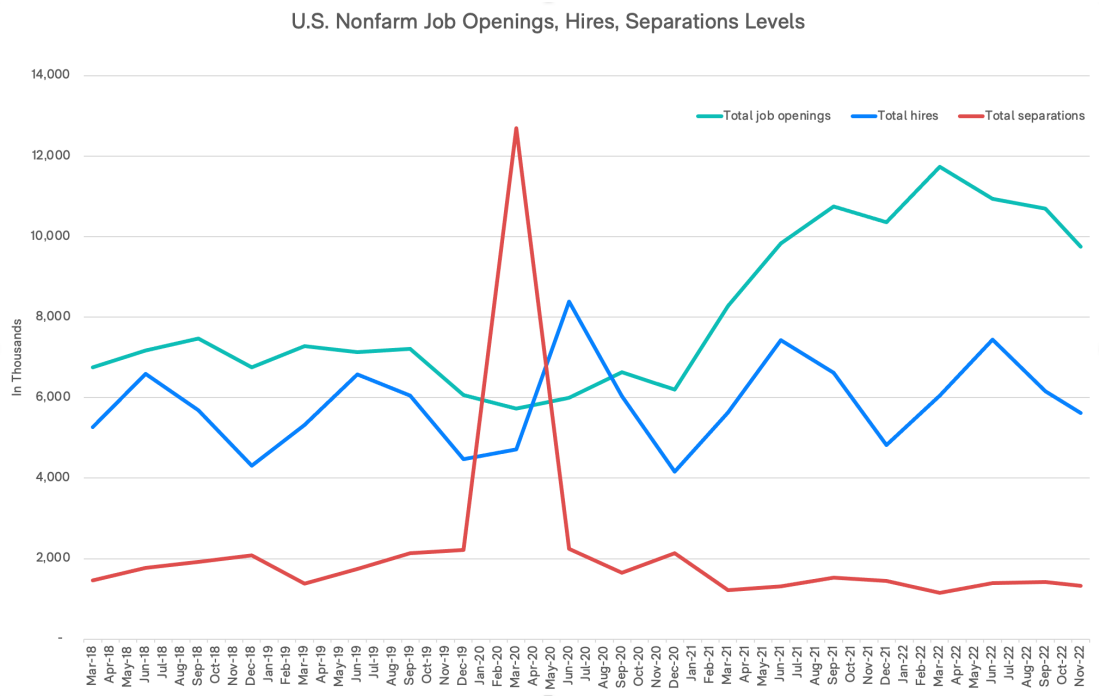
Five Fast Facts

- As of December 2022 Los Angeles had recovered all of the jobs lost during the 2020 lockdowns.
- Q4 2022 VC funding of $4.84B in Los Angeles retracted 56.3% year over year (YoY).
- The impacts of supply-chain disruptions have been the steady increase in construction materials and labor costs. As of November 2022, U.S. construction materials pricing increased 9.7% YoY.
- Asking rents in LA West have slowly started correcting based on the abundant space on the market. Direct asking rents in LA West decreased 1.7% YoY while sublease asking rents decreased by 2.2% in 2022.
- Rightsizing and flight to quality have been the overarching trend for most tech and media companies in LA West, which have been the driving force behind activity in the market over the past decade. The slowdown in momentum of tech and media leasing in LA West resulted in an 11.5% decrease from 2021 to 7.7 msf leased in 2022.

U.S. Employment

Since the dramatic spike in separations (layoffs, quits, discharges) in March 2020, levels returned to normal and November 2022 totals were 29% and 33% below the ten-year and five-year averages, respectively. Job openings peaked in April 2022, but as of November 2022, were still 50% above the ten-year average. Hires have recurrently fluctuated, with a higher-than-usual spike in September 2020, and ended 2022 just 3% above the ten-year average.

The Information sector accounted for just 3% of total nonfarm separations, as of November 2022, and was also 7% and 30% below ten-year and five-year averages, respectively. Job openings peaked in May 2020, but despite the subsequent decline, were still 60% and 29% above ten-year and five-year averages, respectively. Hires levels peaked in both October 2020 and 2021 and remained at higher-than-average levels for 21 of the past 26 months.

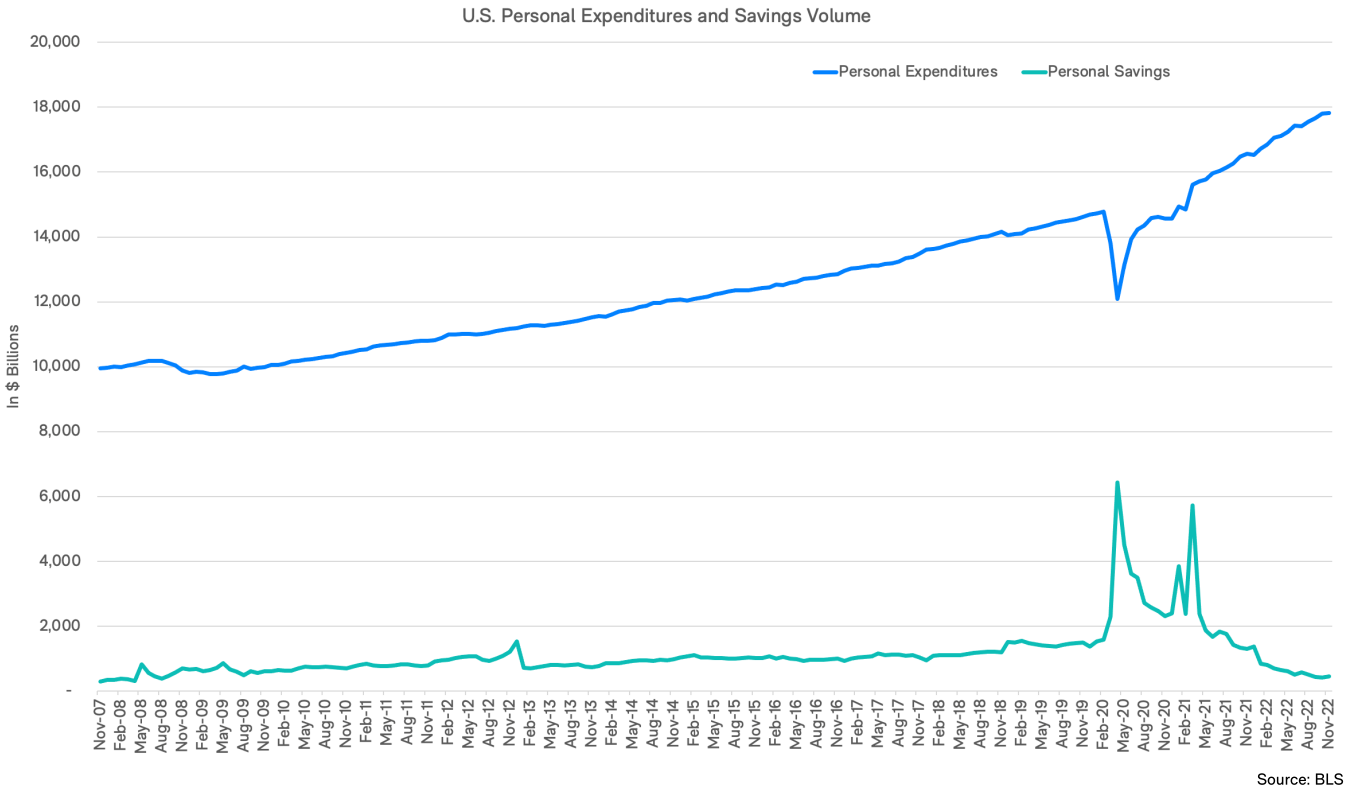


Source: JOLTS

In Los Angeles, Professional and Administrative Services top the charts of industries with the most positions available followed by Healthcare workers, which have been understaffed and overworked since the onset of the pandemic. Additionally as of December 2022 Los Angeles had recovered all of the jobs lost during the 2020 lockdowns.

U.S. Expenditures and Savings

Historic personal savings levels in April 2020 and February 2021 were related to COVID-19 and the Omicron outbreaks, followed by sharp decreases as expenditures (goods, services, household) increased due to rising prices. Used vehicle prices, which had been a major contributor to the initial inflation burst, have steadily dropped over the past year. Food prices dropped for the first time after increasing at a constant rate of 0.9% the past few months. Gasoline prices have also dropped after steady increases in 2021. If prices of goods and services keep falling as higher interest rates curb demand, the target rate can be attainable in the latter half of 2023.



Source: BLS

Softening In Tech

The tech industry was able to weather much of the economic downturn throughout 2020 and 2021 due to increased demand for content; however, in 2022 even Big Tech succumbed to the slowdown. The popularization of hybrid work schedules and the regression of demand for content meant that firms were bloated in terms of footprint and headcounts in the middle of economic stagnation/inflation/stag-flation. Signs of instability at the largest firms highlighted the overvaluations and funding of tech companies based on growth. As a result Q4 2022 VC funding of $5.69B in Los Angeles retracted 51.3% year over year (YoY). Despite the tightening in funding, 40.2% of invested capital in Q4 went to information companies indicating that tech still dominates investment volume during the softening in the tech industry.

Big Tech Companies

Facebook/Meta announced in November that it cut 11,000 employees or 12.6% of their staff. They are also one of the first Big Tech companies to shrink their office footprint, paying to terminate leases on 476,000 sf of office space in Silicon Valley.

Apple - Since laying off 100 employees in early August, it has been more deliberate in hiring processes. Despite the slight downsize in staff, Apple is still looking to move forward with their developments in Culver City and leased a further 98k square feet (sf) in Playa Vista with plans to hire 3,000 employees by 2026.

Amazon - Amazon announced it would cut 10,000 jobs and effectively shutter its Alexa division in 2022. In early 2023 they announced the single largest cut of employees in company history laying off 18,000 additional people.

Netflix - Netflix announced a second round of layoffs of 300 employees in July 2022 compounding the 150 employees already laid off earlier in the year. Additionally, they put 180,000 sf of space up for sublease at their Burbank, CA media hub.

Google/Alphabet is one of the only Big Tech companies that didn't lay off any employees in 2022. Google hired around 12,000 new employees in the third quarter this year, expanding the company 24% over third quarter last year. Since this round of hires Google tightened its performance review standards, which could impact roughly 10,000 people.

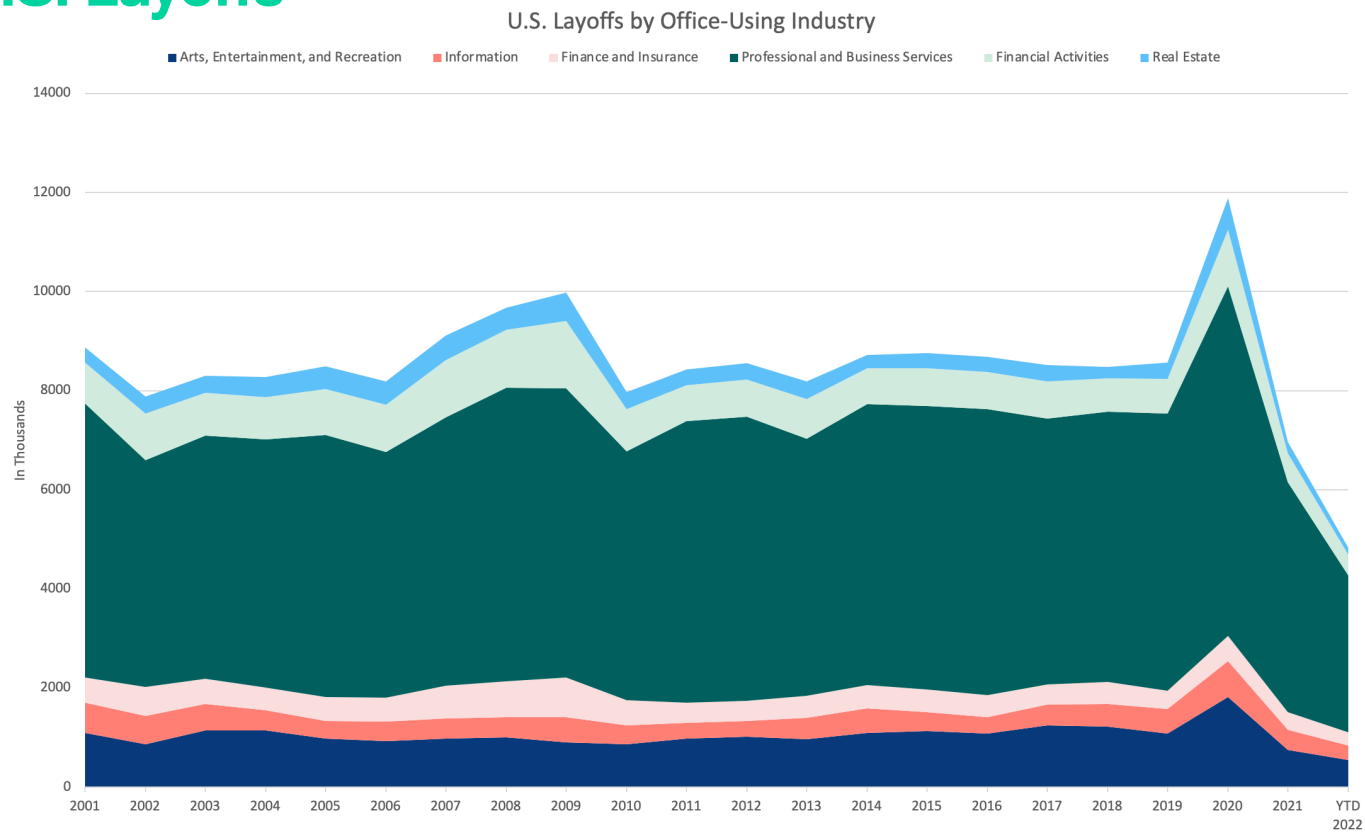
Hulu/Disney - The Walt Disney Company will be instituting cost-cutting measures, which will likely include layoffs in the near future. Though exact numbers weren't reported, Disney will look at operations and labor to find savings.

Microsoft - Microsoft recently announced layoffs on Monday for nearly 1,000 employees worldwide in 2022 and followed it up with an additional 10,000 employees in first weeks of 2023.

Oracle - Oracle is looking to sell its 320,000-s) complex at 2600 Colorado Avenue in Santa Monica. Oracle only occupies about 90,000 sf there despite owning the property. Lionsgate is the largest tenant occupying 192,000 sf, though the movie studio plans to sublease 40,000 sf of its space. Since announcing the company was moving its HQ to Texas, Oracle has subleased an 86,000-sf office in San Francisco, a 230,000-sf building in Belmont, a 186,000-sf building in Pleasanton, and sold a 17-story office tower in San Francisco.

Though traditional office-using industries will likely stabilize the market, Tech, Media, and Entertainment are likely the industries that will push the market out of stagnation. In the face of layoffs and space givebacks from Tech giants, there is still belief in the industry. Of the 15 largest deals in LA West, 10 were by Tech, Media, and Entertainment companies, demonstrating the resilience even during downturns.

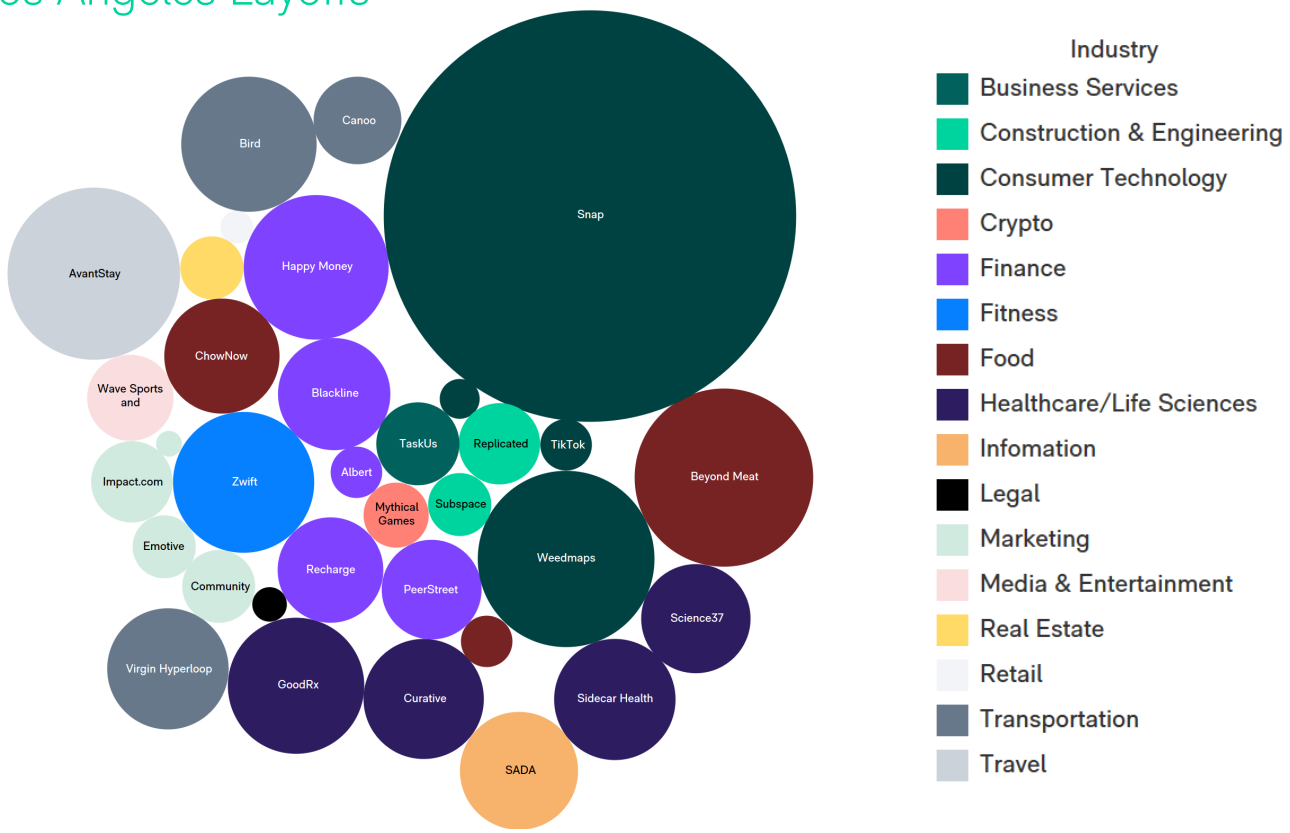
U.S. Layoffs



Source: BLS

The volume of layoffs in the office-using sector decreased sharply since 2020 and is now below even 2008 levels. Professional and Business Services typically bear the brunt of layoffs when moving into a recession and are the slowest to recover from that cycle.

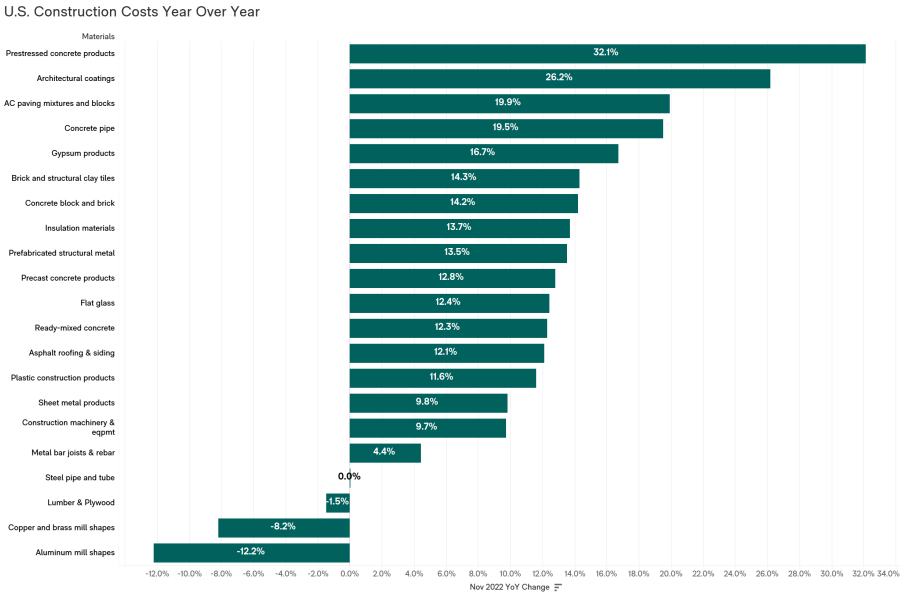
Los Angeles Layoffs



Source: Layoffs.fyi, trueup.io

U.S. Construction Costs

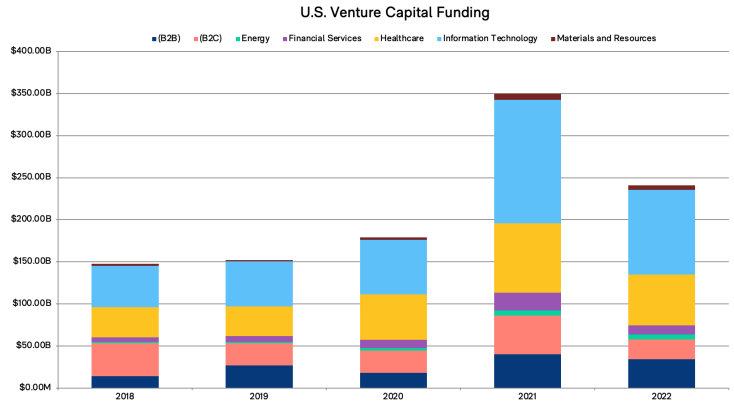
The impacts of supply-chain disruptions have been the steady increase in construction materials and labor costs. As of November 2022, U.S. construction materials pricing increased 9.7% YoY but dipped 0.4% from the previous month. Pricing on construction materials downstream from petroleum production such as concrete and asphalt increased sharply in 2022 driven by inflation, supply-chain disruptions, and lower oil production. As supply-chain issues are corrected pricing on construction materials should begin retracting in 2023.



Source: BLS

U.S. VC Funding

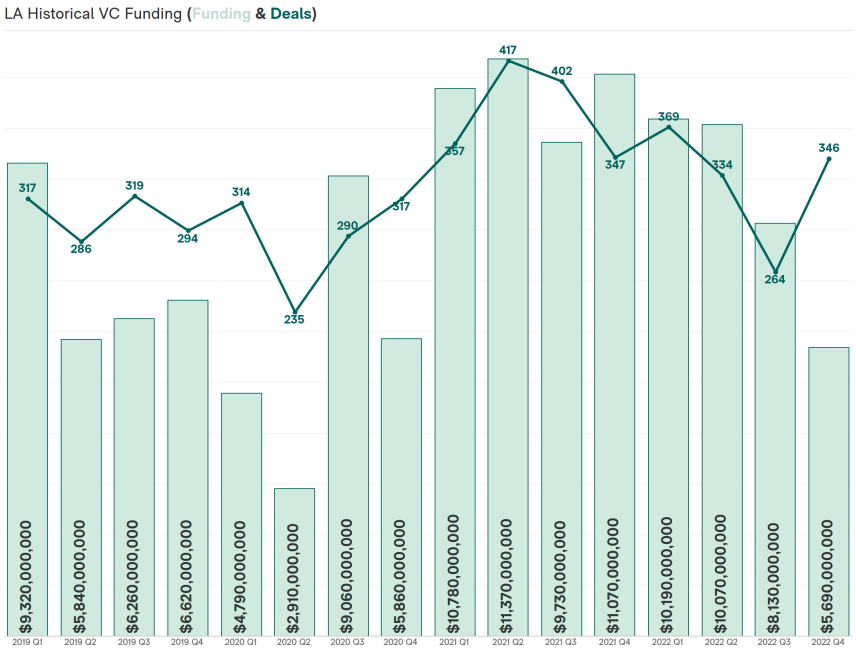
The Information Technology sector received a higher percentage of funding across the U.S. over the past five years totaling $414B, followed by Healthcare.



Source: Pitchbook

Los Angeles VC Funding

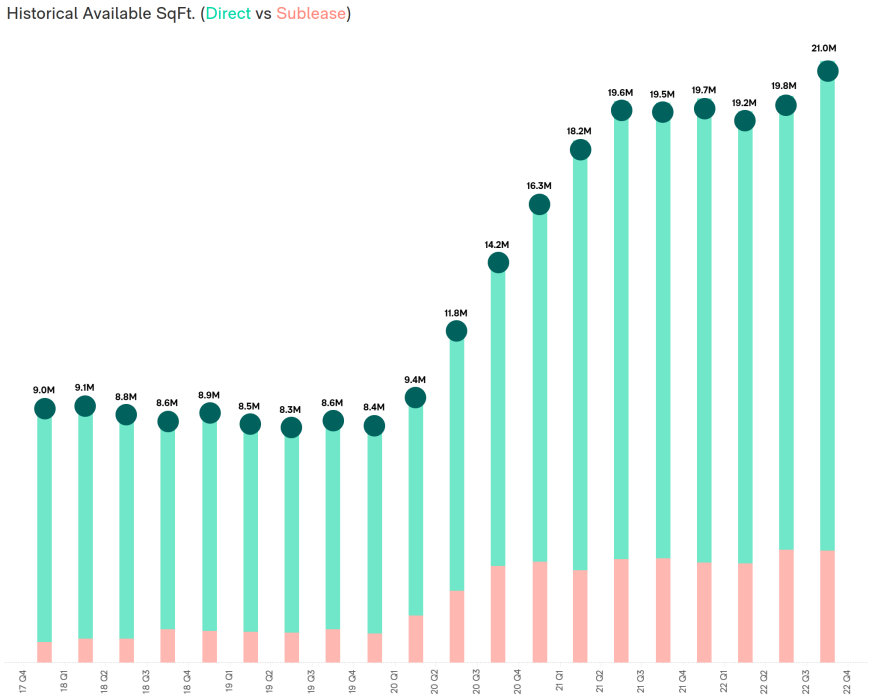
- Q4 VC funding decreased 51.3% YoY
- Despite the dip in investment YoY, the Information Technology sector accounted for 40.2% of all VC funding in 2022.



Source: Pitchbook

Availability Trends

Availability in LA West has hovered above 19 msf since mid-year 2021 but reached new heights in Q4 2022 with 21.0 msf on market.



Source: Raise

Rent Trends

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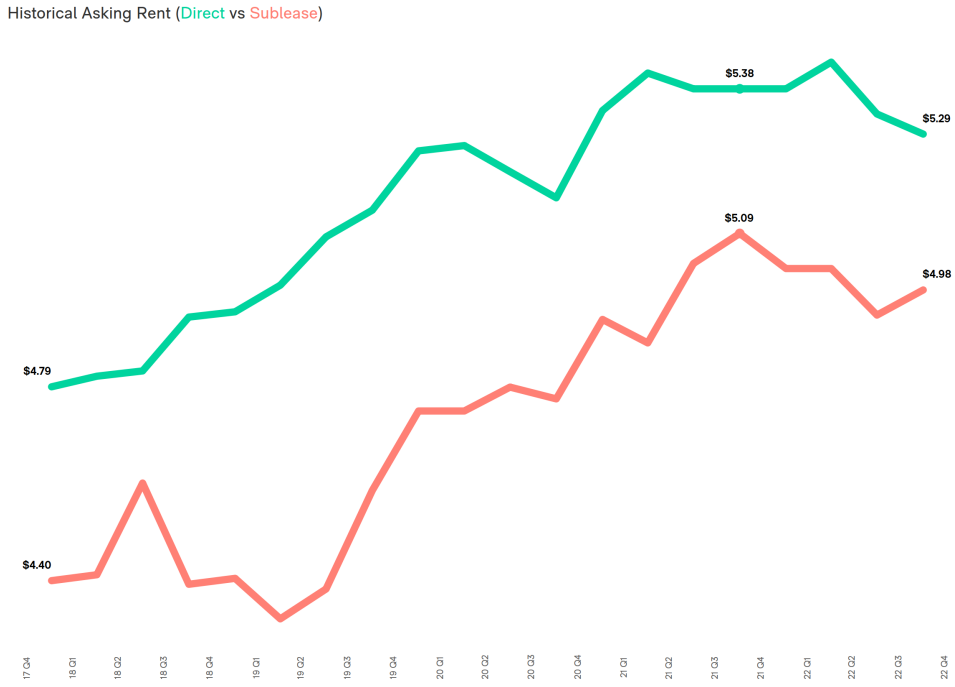
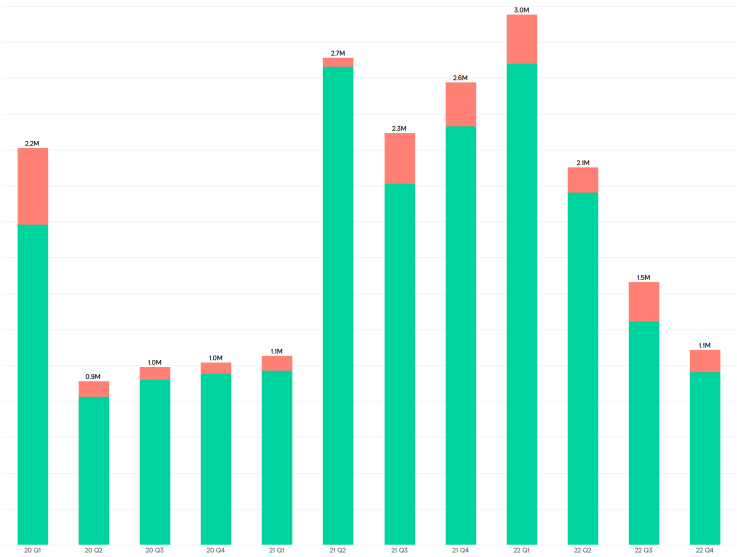


Source: Raise

Leasing Activity

Leasing steadily declined in 2022 coinciding with increasing economic instability pushing companies back into a period of uncertainty. LA West's 7.7 msf of leasing activity in 2022 was a decrease of 11.5% from 2021. Tenants with large footprints have been reassessing their workspace needs in the wake of hybrid work schedules and bloated workforces from over-hiring during periods of growth. Rightsizing and flight to quality have been the overarching trend for most Tech and Media companies in LA West, which have been the driving force behind activity in the market over the past decade. If leasing activity is to return to prior years, it will likely be led by growth of Tech and Media companies.

Historical Leasing (Direct vs Sublease)



Source: Raise

LA West Largest Transactions

TENANT	SQUARE FOOTAGE	LEASE TYPE
Creative Artists Agency	394,580	New Lease
Amazon	207,821	New Lease
Lionsgate	192,584	Renewal
First Republic Bank	156,163	Expansion
Google	97,974	New Lease
Apple	93,949	New Lease
Company3	59,646	Expansion
Ithaca Holdings	58,000	Renewal/Expansion
Google	57,895	Expansion
Kirkland & Ellis	57,000	Expansion
Willkie Farr & Gallagher	56,510	Expansion
Apple	51,234	New Lease
Baker Hostetler	48,234	New Lease
Spotter	44,000	New Lease
HartBeat	38,687	New Lease

Office Demand

Between upcoming expirations through 2025 and known tenants in the market (TIMs) looking for space, LA West has approximately 10.5 msf of demand moving into 2023. Less leasing activity will spur landlords to offer increased flexibility on tenant improvements, lease terms, and free rent to secure tenants.

TIMs - 4.8 msf

Expirations through 2025 - 5.7 msf

Other Trends

Absorption

For the first time since 2019, there was positive net absorption in 2022 totaling 500,000 sf. Despite these gains, the downturn caused by the pandemic resulted in 5.2 msf of negative absorption from Q2 2020 - Q4 2021. The current move-outs were more severe, producing more negative absorption in a shorter period of time than the previous two recessions.

- Dotcom crash 2001 - 4.29 msf of negative absorption (Q4 2000 - Q4 2002)
  - LA tech occupied smaller, older industrial space so the impact on office vacancy was less significant.
- Financial collapse 2008 - 3.125 msf of negative absorption (Q1 2007- Q4 2010)
  - Largely centered around traditional office-using industry sectors.

Notable Properties for Sale

Over the past decade office assets in LA West have been well sought after properties with low vacancy, record levels of demand, and increasing valuations. Declining demand, leasing and general market uncertainty, however, has pushed some owners to reconsider holding major assets in LA West. Two of the most notable are JP Morgan listing the 1.4 msf Water Garden and Oracle listing the 320,000 sf 2600 Colorado.

Occupancy/RTO Indicators

According to Kastle data, Los Angeles' average weekly occupancy stayed above 40% since mid-year 2022 showing steady growth in office use. Aside from expected dips due to holidays, Los Angeles office occupancy has consistently doubled the low point of 21.2% throughout Q4 2022 while the highest occupancy day reached 55.5% in October 2022. Public transit ridership also signals a return to normal activity. As of November 2022 system-wide metro ridership is down 5.2% YoY but up 37.0% since 2020. Despite the significant rebound from 2020, metro ridership still lags 29.7% behind Nov 2019 volume.

Summary

There is little doubt that the signs of a recession are accumulating and the effects of the pandemic recession are still present. On the brighter side, there is still an abundance of cash both on the investment side and personal savings. In order for inflation to stabilize, wage growth will need to level off, which will put downward pressure on demand, and subsequently, pricing on consumer goods.

In order to better weather this downturn and prepare for the next growth cycle, now is the time for companies to consider a financial strategy and review market fundamentals for flight-to-quality and repositioning opportunities. Though all eyes are on large companies to see what workplace strategy they are adopting, the large companies are also looking to the nimble startups that are test fitting hybrid models to which large companies can scale.

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