Hudson Pacific Properties, Inc.
Q2 2025 Earnings Conference Call
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Corporate Participants:
Laura Campbell *Executive Vice President – Investor Relations & Marketing*

Victor Coleman *Chairman & Chief Executive Officer*

Harout Diramerian *Chief Financial Officer*

Mark Lammas *President*

Arthur Suazo *Executive Vice President – Leasing*

Other Participants:
Thomas Catherwood *Analyst, BTIG*

John Kim *Analyst, BMO*

Seth Eugene Bergey *Analyst, Citigroup*

Caitlin Burrows *Analyst, Goldman Sachs*

Dylan Robert Burzinski *Analyst, Green Street*

Peter Abramowitz *Analyst, Jefferies*

Vikram Malhotra *Analyst, Mizuho*

Ronald Kamdem *Analyst, Morgan Stanley*

Alexander Goldfarb *Analyst, Piper Sandler*

Blaine Heck *Analyst, Wells Fargo*

Laura Campbell, EVP, Investor Relations & Marketing
Good afternoon, everyone. Thanks for joining us. With me on the call today are Victor Coleman, CEO and Chairman; Mark Lammas, President; Harout Diramerian, CFO; and Art Suazo, EVP of Leasing.

This afternoon, we filed our earnings release and supplemental on an 8-K with the SEC, and both are now available on our website. An audio webcast of this call will also be available for replay on our website.

Some of the information we'll share on the call today is forward-looking in nature. Please reference our earnings release and supplemental for statements regarding forward-looking information, as well as the reconciliation of non-GAAP financial measures used on this call.

Today, Victor will discuss industry and market trends. Mark will provide an update on our office and studio operations and development, and Harout will review our financial results and 2025 outlook. Thereafter, we'll be happy to take your questions. Victor?

Victor Coleman, Chairman & CEO

Thank you, Laura. Good afternoon, everyone, and welcome to our second quarter call. We are energized by the progress year-to-date on our strategic objectives as well as the positive trends across our portfolio, sectors and markets. Importantly, leasing, which is one of our top priorities, resulted in a 1.2 million square feet of office leases signed year-to-date. And we're on pace for our strongest office leasing year since 2019 and poised to grow occupancy with among the sector's lowest expirations over the next two years. Our studio occupancy is also improving, and California's significantly expanded film and television tax credit is finally in effect.

Since the start of the year, we have also executed on operational enhancements, asset sales and capital transactions, all of which are contributing to the rebuilding of our foundation to drive future cash flow growth. Following our successful CMBS financing and follow-on capital raise, we have over $1 billion of liquidity, and the refinancing of our only 2025 maturity is well underway. We are also starting to realize positive results from our ongoing efforts to enhance the company's cost profile. Specifically, we have meaningfully improved G&A and further streamlined our studio business to achieve profitability.

Moving to the state of our markets, the West Coast office recovery is taking hold, led by emerging AI and tech companies. Tech and leasing in San Francisco drove the single largest quarter occupancy increase in seven years and a third consecutive quarter of positive net absorption. Given year-to-date leasing activity and demand in the market, the city is also on track to have the highest annual gross leasing since 2019. In Silicon Valley, occupancy also improved for the third consecutive quarter. Over 1 million square feet of positive net absorption was driven by the tech sector, new leasing and, for the first time in a long time, deals of 100,000-plus square feet.

AI and AI-enabled businesses are the next wave of economic growth on the West Coast, and billions of venture capital dollars once again flowed into the sector in the second quarter, with no signs of stopping despite tariff uncertainty. AI job postings trended further upwards, and the war for the best talent is on. For AI start-ups especially, proximity to the broader ecosystem is the key. And this explains the reason that 60% of AI's current footprint is located in the Bay Area and why we anticipate West Coast Gateway markets, which have always had a unique mix of talent networks, funding and research, will be the primary beneficiaries.

Today, core AI tenants, that is companies creating, selling and licensing AI models, platforms, infrastructure or chips, represent only 10% of our ABR and are located exclusively throughout the Bay Area. Given the funding available to these companies, their office cultures and the current offerings within our portfolio, we see a considerable runway to expand both core AI and AI-enabled companies with our tenant mix.

On the studio side, there are multiple reasons we are gaining confidence in the business despite weaker overall production activity in the second quarter. Pilot shoot days were up 11% year-to-date and 48% on a trailing 12-month basis. There were 134 productions in active development or prep in California during the second quarter, the most in any quarter since the 2023 strikes.

In the first half of 2025, $375 million was allocated under the previous California Film & Television Tax Credit Program, nearly exceeding total dollars allocated during the entirety of 2024. And of the 110 allocations made so far this year, 51 of them occurred in June alone. Productions are only just beginning to apply for the more than doubled $750 million California tax credit, which, among other new features, provides for larger allocations to more types of productions. And we expect to see increased allocation activity in the near term, with the potential for show counts to begin to benefit as early as the fourth quarter of this year.

Finally, turning to asset sales, we continue to strategically pursue the disposition of noncore assets. We completed the sale of 625 Second for $28 million during the second quarter and we're in various stages on a handful of other potential dispositions. We evaluate each transaction within the framework of our broader capital allocations priorities, seizing the opportunities to increase liquidity while optimizing our portfolio to create longterm shareholder value.

And now, I'm going to turn the call over to Mark.

Mark Lammas, President

Thanks, Victor. We signed up 558,000 square feet of office leases in the quarter, 60% of which were new leases and 60% of which were in the Bay Area. We improved occupancy across all our major markets but for Seattle, where, as expected, a single tenant at Hill7 vacated approximately 100,000 square feet. Quarter-over-quarter, our in-service occupancy was stable at 75.1% and our lease percentage dipped only 30 basis points to 76.2%.

Our rent spreads trended upward, increasing 4.9% on a GAAP basis and decreasing 1.8% on a cash basis. Our trailing 12-month net effective rents were 2% lower compared to the prior year and 11% lower versus pre-pandemic. Our tour activity increased 8% compared to the first quarter to 1.8 million square feet, the highest level in more than two years, driven by additional tours at our San Francisco, Peninsula and Silicon Valley assets.

Tech as a percentage of our tours grew from 35% to 53%, and core AI tenants as a component of tech demand increased from 7% to 61%. Our leasing pipeline is healthy at 2.1 million square feet, including over 0.5 million square feet of later stage deals.

Average requirement size continues to grow, approaching 20,000 square feet, both for tours and our pipeline. We have approximately 50% coverage, including deals and leases, LOIs, proposals or in discussions on our 547,000 square feet of remaining 2025 expirations, including 100% coverage on our only remaining expiration greater than 50,000 square feet. Most of our 2025 expirations are smaller tenants averaging around 5,000 square feet, and thus, decision-making typically occurs within the quarter of lease expiration.

As we have noted, from this point forward, due to both increased office demand and significantly lower expirations, we anticipate our in-service office occupancy should remain stable and should begin to grow as we move through the coming quarters. We have on average 270,000 square feet expiring per quarter through 2029, which is only about half the roughly 500,000 square feet of leases we've signed per quarter over the last two years.

Turning to studios, on a trailing 12-month basis, our in-service studios were 63% leased, with related stages 63.6% leased. The quarter-over-quarter change for these metrics was driven by the inclusion of our Sunset Glenoaks development for the first time. But for Sunset Glenoaks, our trailing 12-month in-service total and stage lease percentages would have increased to 74.3% and 80% respectively due to improved occupancy at Sunset Las Palmas, where 9 of 11 stages are leased.

Our Quixote Studios total in-stage trailing 12-month lease percentages also improved quarter-over-quarter, up 340 basis points to 40.2% and up 410 basis points to 47.4% respectively. Quarter-over-quarter, our studio revenue increased 3% to $34.2 million, primarily due to additional studio occupancy and transportation utilization at Quixote, even without an improvement in show counts. Studio expenses decreased by 11% to $36.6 million quarter-over-quarter, mostly due to elevated expenses in the first quarter associated with various onetime cost reduction initiatives at Quixote. As a result, our studio NOI improved by $5.4 million quarter-over-quarter.

Turning to development, construction at Pier 94 Studios in Manhattan is on time and on budget for delivery by year-end. We are in discussions with tenants regarding longer-term leases and expect show-by-show demand to pick up in the fourth quarter of this year as productions typically book two to three months out. Regarding Washington 1000 in Seattle, discussions with various potential tenants are ongoing and we have tours scheduled for several new mid to large size requirements. This project's exceptional quality positions it favorably in that market, especially given a diminishing pool of truly competitive supply.

And with that, I'll turn the call over to Harout.

Harout Diramerian, CFO

Thanks, Mark. Our second quarter 2025 revenue was $190 million, compared to $218 million in the second quarter of last year, the change primarily due to asset sales and lower office occupancy. Excluding $14.3 million of onetime expenses associated with the forfeiture of executive noncash compensation, our second quarter G&A expense improved to $13.5 million, compared to $20.7 million in the second quarter last year and $18.5 million in the first quarter this year, or nearly a 35% and 27% improvement, respectively, in alignment with our ongoing efforts to reduce costs.

Our second quarter FFO, excluding specified items, of $8 million or $0.04 per diluted share compared to $24.5 million or $0.17 per diluted share in the second quarter of last year. Specified items for the second quarter totaled $19.2 million or $0.09 per diluted share, including onetime expenses associated with forfeited noncash compensation agreements, debt repayment, Quixote cost cutting and transactions. By comparison, specified items for the second quarter of last year totaled $1.2 million or $0.01 per diluted share, including income related to transactions and a one-time derivative fair value adjustments.

Excluding specified items, the year-over-year change in FFO was mostly attributable to factors affecting revenue. Our second quarter same-store cash NOI was $87.1 million, compared to $104.1 million in the second quarter last year, mostly due to lower office occupancy.

Turning to the balance sheet. We continue to execute on a multipronged approach to enhance our maturity profile, increase liquidity and strengthen key debt metrics. In the second quarter, we repaid all of our private placement notes, Series B, C and D totaling $465 million, addressing significant maturities in 2025, 2026 and 2027. We also raised $690 million of gross proceeds through a common equity offering and used net proceeds to fully repay our credit facility and for general corporate purposes. In connection with this offering, we secured commitments to increase capacity under our credit facility by $20 million through the end of 2026, including extensions, and to extend $462 million of capacity through year-end 2029, including extensions.

At the end of the second quarter, we had $1 billion of total liquidity comprised of $236 million of unrestricted cash and cash equivalents and $775 million of undrawn capacity under our credit facility. We had another $22.3 million of HPP's share of undrawn capacity under the Sunset Pier 94 construction loan. Regarding our only remaining 2025 maturity, the loan secured by 1918 Eighth, we expect to successfully refinanced the loan. We will pursue the most cost-effective structure with closing anticipated this quarter.

Turning to our outlook. For our third quarter, we expect FFO per diluted share to range from $0.01 per share to $0.05 per share. Comparing our second quarter FFO of $0.04 per diluted share to our third quarter outlook, we expect gross FFO to increase, largely due to full quarter impact of deleveraging following the recent equity offering. This increase will be partially diluted by the higher weighted average share count of approximately 456,750,000 shares for the third quarter.

Regarding our full-year assumptions, we anticipate both improved interest expense range of $168 million to $178 million and G&A expense ranging from $57.5 million to $63.5 million as we continue to execute on previously announced cost-saving measures. Estimated weighted average share counts now range from 319 million and 321 million for the full year.

Finally, please note that consistent with this quarter's filing, our full-year same-store cash NOI now reflects the inclusion of our Metro Center office property, resulting in a range of negative 11.5% to 12.5%, which would have been identical to last quarter's range of negative 12.5% to negative 13.5%, but for that adjustment. As always, our outlook excludes the impact of any potential dispositions, acquisitions, financings and/or capital markets activity.

Now, we'll be happy to take your questions. Operator?

Q&A Section

Operator

Our first question for today comes from Seth Bergey of Citigroup. Your line is now open. Please go ahead.

Blaine Heck, Wells Fargo

Hi. Thanks. Good afternoon. So it seems as though the building blocks are in place for office occupancy growth now that you're effectively past the large known move-outs. But just wanted to make sure that there were no incremental concerns that came up this quarter around significant move-outs in future years or tenant credit situations that could make it a more bumpy recovery.

Victor Coleman, Chairman & Chief Executive Officer

Not at all. Blaine?

Blaine Heck, Wells Fargo

Okay. Yeah, go ahead.

Victor Coleman, Chairman & Chief Executive Officer

No, not at all. There aren't any significant issues with any tenant in the portfolio on any level that would change the dynamic around what we've announced and what we have going forward with leasing.

Blaine Heck, Wells Fargo

Okay. No, that's helpful. I guess, following up on that, Victor, I guess, how do you think about the pace of which you can recover this occupancy? Is this – it certainly seems like a multiyear rebuilding effort, but maybe give us a little bit of color around how we should be thinking about this.

Victor Coleman, Chairman & Chief Executive Officer

I mean, listen, Blaine, I think you heard in the prepared remarks specifically around Mark with we have had quarter-over-quarter sequential increase in leasing. We've had quarter-over-quarter, more importantly, tours and activity and pipeline has been stable. We've gotten – I shouldn't say we, Mark got in trouble one time for sort of projecting where leasing was going. I think we feel very comfortable given the activity, the deals we have in the pipeline that we're shooting for somewhere around a low-8, high-7 handle year-end and then 2026 a mid-8 handle given everything we're working on right now. And it was indicative of sort of the playbook that we laid out with the tenant occupancy and leased differential, I'm referring to a lease number there.

Blaine Heck, Wells Fargo

Yeah. Okay. That's really helpful. Clearly, you guys accomplished a lot with respect to the balance sheet this quarter. So do you feel as though you've completely kind of shifted your focus to leasing and occupancy growth in both office and studios, kind of driving at an improvement in your overall cost of capital as that comes through? Or is there anything substantial that you're working on with respect to the balance sheet in the near term that we should be aware of, obviously, outside of 1918, which Harout touched on?

Victor Coleman, Chairman & Chief Executive Officer

Yeah. I mean, indicative around 1918, I think as Harout said in his prepared remarks, we're very close to finalizing that deal. On a balance sheet standpoint, we have excess liquidity that we've not had access to in some time. And there really isn't any next major step on the balance sheet/liquidity basis for us to accomplish, everything we need to accomplish on the office and studio side over the next 36 months probably, with the exception of us renewing the media loan at a little over a year from now.

I think that it does put us in a much stronger position to work on the execution, which is clearly around leasing and ops. And that's where we see the upside here. And that's why I think we're very confident. And we've clearly bottomed out in

every market we're in. And more than just bottomed in some of the markets. It's really made a dramatic turn, as you can see, by the activity not just within our portfolio, but also in our peers' portfolios in the similar markets.

Blaine Heck, Wells Fargo
Okay, great. That's helpful. Last one for me with respect to Quixote. It seemed as though there were some lease terminations and sales of the fleet. I guess, can you talk about the drivers behind those lease terminations and just give us an update on maybe how much more you can cut on the cost side and your ultimate plans for that business?

Mark Lammas, President
Yeah. So, Blaine, it's the downsize of the fleet, the lease terminations, all part of that cost-cutting efforts that we've been underway on. Last quarter, the update on that front was that we had cut about $14 million of expenses on a pro forma basis. We thought relative to, say, 2024 actual results, that $14 million of cost cutting translates into about $10 million of improved NOI pro forma to 2024.

That effort continues. In the latest quarter, we cut another $10 million. That was largely downsizing of the fleet, including the location services part of that fleet. So we're at the current annualized expense cutting efforts coming in at around $24 million. The update on the NOI side, again, pro forma to 2024 results, is $14 million of NOI improvement – cash NOI improvement.

I think importantly, when we last updated you, we thought that breakeven based on those cost-cutting efforts were like mid to upper 90 show count levels. Based on the latest cost cutting, we think that's now down into the low-90s, gets us closer to breakeven. And I think last but not least, we still think we're in that $30 million to $40 million cash NOI range if we can see show counts get somewhere back to the 110 to 120 level.

Blaine Heck, Wells Fargo
Great. Very helpful. Thanks, everyone.

Victor Coleman, Chairman & Chief Executive Officer
Thanks, Blaine.

Operator
Thank you. Our next question comes from Alexander Goldfarb of Piper Sandler. Your line is now open. Please go ahead.

Alexander Goldfarb, Wells Fargo
Hey. Good afternoon out there. So, Mark, maybe just sticking with Blaine's question on Quixote and the studios, I think if memory serves, it was about $100 million of EBITDA that went away when the studio shut down a few years ago. Obviously, you've retooled the business and it's great, Victor, to hear about the increasing show counts and the tax credits.

Where should we think about – I don't know if it's $100 million that you guys will get back to, but where should we think about that revenue or that EBITDA and recovery? And if we think about the length of time, is it two years, three years? Do you think it'd be quicker? Just trying to get a sense of how much we'll get back and a timing of when you think it will get back based on how productions are coming back?

Mark Lammas, President
Yeah. So the last point I was making, Alex, really points to where we think it could trend to at that 110, 120-ish level. 120 was average show counts in 2022. In 2021 and 2019, we shot show counts above 130, even in certain months 140. But I don't think we're thinking that that's peak television is necessarily in the cards. But with the tax credit now more than doubled to the $750 million level and officially in the budget, hopeful that we could see show counts get above, say, the 110 level, which should get us somewhere in the neighborhood of about $30 million of NOI.

I don't know that it makes sense to revisit the initial pro forma back when we purchased the company starting in 2021, which is that $100 million or so that you're pointing to. For now, I think the key is getting closer to breakeven, which I mentioned is around that 90-ish show count level and trying to get back into positive EBITDA territory, like that $30 million, $40 million range that I think we could potentially get to.

Alexander Goldfarb, Piper Sandler
Okay. And then the second question is, Victor, I think you mentioned that you guys, obviously nice job on the capital raise, that you have the capital that you need for the next 36 months. But just want to make sure I understand, as you think about the leasing CapEx, the free rent and everything that you need to do to get the portfolio back into, I guess, sort of the low-90s on the office front, is that correct that you don't need any additional capital or – I just want to make sure I understand that correctly.

Victor Coleman, Chairman & Chief Executive Officer
I mean, I think what we're referring to is, is that we've got a plan in place that can access additional capital if need be, and the balance sheet will shape up that way. I'm not saying we're not selling any more assets because that's not the case, because you heard in my prepared remarks, we have a few assets that we are working on. I think the expediency of selling a couple of quarters ago was ramped up and now we're taking more of a moderate time line on that because we don't need the capital today. Doesn't mean we're not going to be pruning the portfolio as we typically do.

Alexander Goldfarb, Piper Sandler
And then as part of that, the line of credit which I think Harout said is $775 million undrawn, is your view to use like maybe a little bit of that? Or as you think – or as we think about this plan, the line of credit would form a meaningful part of the capital spend?

Victor Coleman, Chairman & Chief Executive Officer
I mean, typically we use a line of credit on a need be basis. Right now, there's no need because we have cash on the balance sheet in excess of almost $200 million. So we're in good shape there. And we've always used the credit facility when we need it. If there are opportunities that we have to access it, we will. There's no set game plan as to when we're going to draw down on it.

Alexander Goldfarb, Piper Sandler
Okay. Perfect. Listen, thank you.

Victor Coleman, Chairman & Chief Executive Officer
Thank you, Alex.

Operator
Thank you. Our next question comes from Caitlin Burrows of Goldman Sachs. Your line is now open. Please go ahead.

Caitlin Burrows, Goldman Sachs
Hi, everyone. I guess, I was wondering if you could just comment on the leasing environment. It seems like you guys have been maintaining this kind of average quarterly pace in that 500,000-square-foot range for a while now. I feel like also in line with what you guys were saying, that there's a lot of commentary about West Coast picking up. So I guess, I was wondering if you could just comment on are you seeing a pickup? Are you seeing what you've been seeing sustaining? Just how those volumes are going?

Arthur Suazo, Executive Vice President – Leasing
Hi, Caitlin. This is Art. Yeah. So that pace, that 500 – that magical 500,000 square feet, we well surpassed. If you look at the last two quarters, I think we're averaging about 590,000 square feet. So, yes, to answer your question, it is picking up. Not only is it picking up, but we're starting to see the front end of that engine, which is tours pick up as well. We're up 10% quarter-over-quarter in just tours, up to 1.8 million square feet, which is really the highest we've had in probably about six

years. So that's the good news behind what's in our pipeline and what we're executing on. And additionally, the tour activity, the average deal size is increasing. That's telling us, that's informing us that the midsized deals are really back into the market and we're availing ourselves of them.

Caitlin Burrows, Goldman Sachs
Got it. And then, I guess, maybe could you just differentiate by some of the markets? I know you were talking before about the strength in tech and AI mostly in the Bay Area. Would you say that's driving the strength? Or would you say the kind of pickup that you were just talking about is across markets?

Arthur Suazo, Executive Vice President – Leasing
No, it's 100% driving the strength across the Bay Area, San Francisco in particular. It's the tech – it's the relationship to the tech into the pipeline itself. It's up in the Valley, it's up to about 68%. In the city, it's up very close to 60%. And AI is roughly about 25% of that and growing, by the way. In Seattle, a little bit more modest increases, but increases nevertheless. We've seen year-over-year probably 25% increase in demand and gross leasing. And the tech pipeline though, again, a little bit more muted in San Francisco, we're starting to see migration. We're starting to see the front end of some of the top name tech companies, AI companies, getting a foothold in Seattle, availing themselves of the talent pool in Seattle, for example, OpenAI, Anthropic, NVIDIA, Databricks, to name a few. And so we're seeing these tenants take 8,000, 10,000, 15,000 feet, and then grow. So if you paid attention to the last cycle, that's precisely what happened and drove the engine in Seattle.

Caitlin Burrows, Goldman Sachs
Got it. Thanks.

Operator
Thank you. Our next question comes from Seth Bergey of Citi. Your line is now open. Please go ahead.

Seth Bergey, Citigroup
Hi. Thanks for taking my question. I just wanted to touch on third quarter guidance. What kind of at this point, and where we sit in August, with July kind of already in the books, kind of gets you towards the lower end or the higher end of guidance?

Harout Diramerian, Chief Financial Officer
Yeah. Thanks for the question. I think a lot of this stems from the studio business. I think if we get surprised and the activity increases more than we expect, we can get in the higher end of the guidance. And I think if the studio business is slower than we expect, it may go to the lower end of the business. Obviously, if we get some different type of leasing, if we execute on leases that give us more benefit to occupancy, that can also help on the higher end of the range. But as it relates to other costs and interest, I think those things are pretty well known as we fix our interest, and our G&A costs are pretty known at this point.

Seth Bergey, Citigroup
Okay. Great. And then I think in your prepared remarks, you said that there's around 500,000 square feet of – the leasing pipeline is kind of in later stages. Any of that at Washington 1000?

Arthur Suazo, Executive Vice President – Leasing
Yeah. So I think it was – the number is actually closer to 600,000 square feet. I think we said 500,000 square feet, but it's moved up. Not at Washington 1000, no later stage deals. The deals that we have at Washington 1000 is based upon the market information I shared with Caitlin just a second ago. We're starting to see more multitenant deals in the market of which we are touring. So, tours are up significantly quarter-over-quarter. And then we have – there's three 100,000-square-foot deals in the market right now that we're engaged with. So, not later stage lease or LOI yet.

Seth Bergey, Citigroup
Okay. Great. Thank you.

Operator
Thank you. Our next question comes from Tom Catherwood of BTIG. Your line is now open. Please go ahead.

Thomas Catherwood, BTIG
Thank you and good afternoon, everybody. Following up on Alex's leasing CapEx question. With the incremental capital on your balance sheet right now, can you get more aggressive pursuing new leases and kind of capturing more of the 2 million-plus square foot pipeline that you have? Or is the plan to hold more cash for other uses in the next 12 to 18 months?

Victor Coleman, Chairman & Chief Executive Officer
Thanks, Tom. Good question. Listen, we've never detracted our business plan around spending capital if the quality and size and quantity of leasing is available to ourselves. So it's not about whether we have capital or not. We've never constrained ourselves from not doing deals because of capital at the end of the day.

So we're trying to expedite the process. We're not losing deals because we're being aggressive or not being aggressive. We're losing deals to competitors who may have space that's readily accessible, and that marketplace has been drying up dramatically, specifically in Seattle. I mean, the deals that we've lost in Seattle have been to move-in ready space. So the majority of that sublease space in the marketplace is now gone.

In the Bay Area, both in the Peninsula and San Francisco, we're at a massive level playing field there right now. The activity, as Art mentioned and Mark in his prepared remarks, has never been higher. So we're comfortable in the ability for us to execute. It's really just a timing situation. And I do think that the comment about we're a month into the quarter, remember, it's also the quietest quarter being summer. We've already seen great activity for this quarter in leasing, and we expect September to be a pretty strong month for us.

Thomas Catherwood, BTIG
Got it. Appreciate that, Victor. Then kind of when we think of institutional investor interest in West Coast, CRE but especially office, seems like that's ramped recently, whether they're owner users, whether they're financial investors. What have you seen in terms of valuation improvements across your markets? And is that changing how you're approaching asset sales? Are you moving certain assets in or out just depending on the change in values recently?

Victor Coleman, Chairman & Chief Executive Officer
That's an excellent question. I think you've got to look at a couple of factors right now. They're sort of lean towards the valuation and institutional capital coming into specific office. But in general into CRE, overall on the West Coast, the venture capital drive has put the capital forefront into the Bay Area specifically and then Seattle secondarily. I mean, the Bay Area is – 60% of the AI is going in the Bay Area and the VCs are funding companies that are putting their companies and corporations and headquarters in the Bay Area. And so, that has taken a very positive shift in terms of valuations and increased price per foot.

The number of transactions has picked up in terms of sales and dispositions or sales, whichever side of the table you're at. But it's not materially changed quarter-over-quarter to a point where you're seeing massive decrease in cap rates and evaluation shift. We think that's coming. Clearly, those who ventured into the marketplace in the Bay Area, both in the Peninsula and the city 12 to 18 months back, all the way through till the beginning of this year, have made really, really solid buys for the most part. And so we're seeing those valuations increase. But I think it's still a little too early to sort of capture, well, this is where cap rates have gone from to. But that is coming.

In terms of your latter part of your question, right now we have really looked at only one asset in the Bay Area that could be a disposition candidate left in our portfolio that would make some sense and be priced out at a good number. So we're not reevaluating that and I don't see us doing so. I'd rather see the leasing pick up and then maybe look down the road of a more stabilized asset.

Thomas Catherwood, BTIG
Got it. Thanks for that, Victor. And last one for me. Mark, you mentioned Sunset Las Palmas. I think it was 9 out of the 11 studios are leased. But in the supp, it's still sub-50% from a leased percent. Is there a lag when it comes to – when a stage is spoken for to when the actual occupancy is taken and that percentage ramps? How do we think through it with Las Palmas specifically?

Mark Lammas, President
Yeah. Yeah, for all the stages, we track occupancy on a trailing 12-month basis, which is how we've done it historically since 15 years now. Its origin relates to really the period of time of really show-by-show occupancy on the stages. And the trailing 12-month occupancy looks were designed to give more sort of robust look at ongoing occupancy, unaffected by temporary expirations and then backfills across different stages. So what you're seeing there is really just lower occupancy in earlier periods at Sunset Las Palmas.

Thomas Catherwood, BTIG
So then at the end of the quarter, what did the occupancy or the percent leased look like for Las Palmas?

Mark Lammas, President
Well, 9 of the 11 stages were leased. I don't know, it's probably in the neighborhood of about 80% leased right now.

Thomas Catherwood, BTIG
Understood. That's it for me. Thanks, everyone.

Operator
Thank you. Our next question comes from Peter Abramowitz of Jefferies. Your line is now open. Please go ahead.

Peter Abramowitz, Jefferies
Yes. Thank you for taking the question. Just want to go back to Victor's comments around increasing occupancy. And I think you mentioned the target for getting leased occupancy back to the mid-80s by the end of next year. Obviously, the Bay Area, despite the pickup in activity, is still kind of trailing the rest of the portfolio. So, just curious, what's kind of a realistic target for stabilized occupancy in the Bay Area in your view? And how long do you think it can take to get there?

Victor Coleman, Chairman & Chief Executive Officer
So when you're defining the Bay Area, are you defining the entire marketplace from San Francisco all the way down through the Peninsula? Or are you looking at just San Francisco...

Peter Abramowitz, Jefferies
Yeah, yeah, kind of looking at both. Yeah.

Victor Coleman, Chairman & Chief Executive Officer
Yeah. I mean, the lag has really been candidly in the airport area, Santa Clara at the end of the day. I mean, the numbers we're looking at right now, if you look at the entire marketplace, it's right around 70. And if you look at the city, it's – Palo Alto being the highest, its already at like 92%. Redwood is like 73%. And Foster City's like 87% and Santa Clara is like 90%. And then in the low end, you've got North San José, which is bringing everything down in the mid-50s. But the activity in North San José right now has been exceptional. And as Mark made – sorry as Art made the comment, we're seeing – we were doing 7,000 to 20,000 square foot deals. We're now seeing 30,000 and 40,000 square foot deals and even some even higher.

Arthur Suazo, Executive Vice President – Leasing
Yeah, so that's really the average. Peter, this is Art. When you're talking about the Valley, you're talking about an increase in deals that are 100,000 square foot or more. There were eight a year ago. There's 18 today. We're even seeing, mind you, we're talking specifically about the airport with our portfolio. We're seeing that there's four deals over 100,000 square feet

that we're in discussions or negotiations on. And as you know, that's a small tenant market. The average tenant size in our portfolio is roughly 7,000 to 8,000 square feet, right? And we're in discussions and negotiation with four tenants over 100,000 square feet. That's really going to move the needle in a big way.

And as you move north, the two biggest vacancies that we have we're negotiating, one is 80,000 square feet, the other is 50,000 square feet. We're negotiating both spaces with multiple users. So we feel pretty bullish about leasing – that pace of lease-up over the next year-and-a-half. And then, of course, as you get into the city, our largest vacancy is 1455. And we're in discussions right now for a land share of that space. So we're feeling – again, we're feeling good about what's in the pipeline and what's behind it in terms of tours.

Peter Abramowitz, Jefferies
Okay. That's helpful. I appreciate the color. And maybe just a follow-up on the tour activity, I think you mentioned it was up 10% quarter-over-quarter. Could you just specify how is tour activity trending specifically in Los Angeles?

Arthur Suazo, Executive Vice President – Leasing
Yeah. So let me start with the tour. Yes, it is up 10%, but I'll give you numbers. It's up to 1.8 million square feet. At the same time, quarter-over-quarter, the average deal size popped 30%, right? So it's closing in on 20,000 square feet. Those are the tours we're seeing. That's what's going to feed the pipeline, which is going to inform what we close downstream. And actually our hit rate on tours is pretty high, it's about 30%. So we can start to look favorably about what's going to happen in the coming quarters.

In LA, we really only have this 11601 building that we're sitting in right now. We're 96% leased. It's really become a small tenant building. And we're garnering the highest rents in the market. But the LA market in general is really driven by West LA, it always has been, certainly well through the pandemic. The demand drivers are there, right? The demand is probably up 20% year-over-year. More importantly, the gross leasing still remains robust.

So not that concerned about LA and certainly not this building at the moment, because we have a pipeline for this building of about 50,000 square feet, which doesn't sound like much, but we're – again we're closing in on 97% leased.

Peter Abramowitz, Jefferies
All right. That's all for me. Thank you.

Arthur Suazo, Executive Vice President – Leasing
Thank you.

Operator
Thank you. Our next question comes from Vikram Malhotra of Mizuho. Your line is now open. Please go ahead.

Vikram Malhotra, Mizuho
Afternoon. Thanks for taking the question. I guess, just going back to the point about target occupancy next year, maybe if you can just step back and give us a sense of, like, over the next two years, let's say you're able to achieve this occupancy, you do have a fair amount of expirations over the next three years. Is it fair to say that once you achieve this occupancy, cash flow growth or AFFO growth will probably still be a probably 27-, 28-time at the earliest?

Victor Coleman, Chairman & Chief Executive Officer
So, Vikram, let me just clarify your comments because they're not accurate, okay? First of all, we're not talking occupancy. The numbers I talked about was leasing, and specifically said leasing versus occupancy. Second of all, we have the lowest amount of expiration in the next three years than we've had in the last eight. We average at around 500,000 to 600,000 square feet a quarter – sorry, yes, 500,000 to 600,000 square feet a quarter. We are sub-250,000 square feet. So, if you look at that and you look at what we talked about earlier and you correlate to leasing, not occupancy, we're very

comfortable that 2026 year-end will be at the range that we're talking about right now, which will correlate to occupancy and cash flow that will increase at a substantial amount from an FFO and an AFFO basis.

Vikram Malhotra, Mizuho
Okay. Yeah. I mean, I was just looking at the expirations as a percent over the next several years, kind of 2025 through 2028.

Victor Coleman, Chairman & Chief Executive Officer
You said three years. So it's – several years could be three. But if you look at three years, it's about $750,000 to $800,000 versus $1.5 million to $2 million.

Vikram Malhotra, Mizuho
Okay. Just going back to the studio business, you talked about reaching hopefully the number of shows and then reaching sort of a run rate breakeven NOI level or rent level. I just want to go back, I guess, it was two quarters ago, part of the plan was maybe looking at it more strategically, it is a challenged business today, but is divesting it still on the cards? And if not, I guess, do you look for more partners? Or do you just – are you still focused on the Quixote – like, having the Quixote business as part of the company? Thanks.

Victor Coleman, Chairman & Chief Executive Officer
Well, I don't recall us ever talking about divesting. What we talked about, which we've executed on, is divesting on certain leases and obligations that are not income producing to lower the overhead and costs, which we've accomplished and we've outlined, and in Mark's prepared remarks, he reiterated again. We have not talked about divesting out of the Quixote business, the Sunset portfolio business or the real property or the OpCos.

Vikram Malhotra, Mizuho
Thanks.

Victor Coleman, Chairman & Chief Executive Officer
Thank you.

Operator
Thank you. Our next question comes from John Kim of BMO Capital Markets. Your line is now open. Please go ahead.

John Kim, BMO
Thank you. I just wanted to clarify your guidance for the year, I guess, for Harout. Same-store NOI is basically unchanged from last quarter. G&A assumption is down, interest expense is down, yet it doesn't look like earnings are moving that much. I know it's a pretty wide range. But what are the offsets to the positive contributors in your guidance? And what would you bring into the low end of guidance, the $0.01 to $0.05 in third quarter?

Harout Diramerian, Chief Financial Officer
Sure. Just to clarify, the annual numbers, obviously, some of which are reflected in the third quarter numbers, right? So there's still the fourth quarter. But I think I touched upon this a second ago. For the third quarter, what the biggest variable numbers would be is the studio business, right? I think if show counts improve, if things are more active and more robust, that'll get us closer to the higher end of the range. And then if things are weaker than we expect, it'll bring us closer to the lower end of the range. That to us is the biggest X factor in our guidance for the next quarter.

John Kim, BMO
Okay. On the studio business, with Sunset Pier 94 looking to get complete or looking for its completion date this quarter, when do you expect occupancy to commence? And if you could break down the stages that you're in negotiation with as far as the longer-term leases versus the show-by-show. And also if there's any services component as part of the NOI of the studio?

Victor Coleman, Chairman & Chief Executive Officer
Well, listen, right now, John, we are in conversations with a couple of shows that are year-to-year, name shows that have come to us. It's still a little early because some are trying to film as of Jan 1, which means they would be in office space prior to that. And so, that's still in limbo. For the most part, though, we've indicated we are going to – the activity is around show-to-show. There's not a lot of long-term leasing that is available in any of the marketplaces throughout the States right now in the three main markets of Atlanta, Los Angeles and New York. But we are seeing some very solid activity around name company shows that will have hopefully repetitive seasons.

The answer to your second part of your question, the economics around that are fully integrated with how we do every one of our deals, which is going to be package deals, which include all services, all amenities, all soundstages, all offices and all of our lighting and grip packages. So that will be a total number at the end of the day. We will have no differentiation between Pier 94 or any of our other studio facilities in terms of how our revenue collections and charges are.

John Kim, BMO
Okay, that's helpful. And then my final question is on the leasing activity. It was pretty healthy this quarter. It looks like your 2026 expirations actually went up this quarter versus last. Were there a lot of short-term leases that you've done or just like short-term renewals that got you there, because it's a little bit of an aberration?

Arthur Suazo, Executive Vice President – Leasing
Yeah, that's generally the case. It went up slightly. Yeah, it went up slightly, but some of the tenants are holding over or in a short-term situation.

John Kim, BMO
Okay. Thank you.

Operator
Thank you. Our next question comes from Ronald Kamdem of Morgan Stanley. Your line is now open. Please go ahead.

Ronald Kamdem, Morgan Stanley
Hey. Just wanted to circle back to the Washington 1000. Just wondering if you could provide just a little bit more commentary on just the activity in the market overall and how that asset is differentiated. And I think it sounded like you're leaning more toward sort of multi-tenant versus maybe a big tenant and so forth. Just would love to dig in there a little bit more. Thanks.

Arthur Suazo, Executive Vice President – Leasing
Yeah, we're exploring all – I mean, at this point, there's an uptick in multi-floor tenants, as I – multi-floor deals as I said. We're touring. The touring has picked up. There are three, there're really five 100,000 square foot tenants in the market, three of which we are in front of for Washington 1000. And the other two are really a Pioneer Square kind of location that we're in negotiations with, which is the good news. So no, we continue with tech of those three 100,000-square-foot tenants, actually two are tech, one is biomed. And we're going to see in the coming quarters, if we can't execute on one of these. But the good news is is behind it, the tours that we have lined up already as we come kind of through the

summer will, I really think it's going to start to pay dividends for us there. But to answer your question on the building, it's one of one. It is if you want new construction, state-of-the-art asset, especially if you need more than 200,000 square feet, we're one of one. So we feel really good about our prospects.

Ronald Kamdem, Morgan Stanley
That's helpful. And then my second one is just going back to the same-store NOI sort of guidance. I guess, when you're thinking about – when we're connecting the dots with the occupancy commentary, what are some of the higher level sort of takeaways in terms of what that does for same store as you're going to 2026 and 2027, right? Because presumably the comp is easier and you're gaining occupancy. So how should we think about just high level what that same store should be doing? Thanks.

Mark Lammas, President
Well, I'll take it. This is Mark. I'll take a crack. Yeah, I mean, they're obviously correlated. You're going to see GAAP same-store NOI begin to improve typically sooner than cash, typically a reflection of the component of the leasing activity that has front-loaded free rent. But hard to pinpoint precisely when you see the turn. But our sequential flat occupancy of 75.1%, I think, sort of reinforces our belief that we've likely hit the bottom on occupancy. We'll see a steady march of positive net absorption that should first materialize in GAAP, like I said, and then you'll start seeing it show up in cash rent.

Ronald Kamdem, Morgan Stanley
Great. That's it for me. Thanks so much.

Operator
Thank you. Our next question comes from Dylan Burzinski of Green Street. Your line is now open. Please go ahead.

Dylan Burzinski, Green Street
Hi, guys. Thanks for taking the question. Just sort of on the sort of lease trajectory, it looks like you guys noted that PayPal has executed a lease termination starting next year. Are there any other larger potential move-outs that we should be aware of as we think about the 2026 ramp?

Victor Coleman, Chairman & Chief Executive Officer
No, no. We already asked—answered that. That was the first question that was asked. No, there's nobody else there.

Dylan Burzinski, Green Street
Great. And then I guess, given the limited amount of near-term lease signings that seem to be expected at Washington 1000, can you kind of talk about how we should expect that to sort of roll into earnings? It seems like that should sort of come off capitalization sometime towards the end of this year. But is that sort of incorrect?

Mark Lammas, President
No, that's right. I mean, it'll – at the end of this year, we'll no longer be capitalizing interest on it. And then you'll see in our supplemental that as we sit today, we're currently anticipating stabilization on it first quarter of 2027, which that's 92-ish percent cash paying occupancy. So you can kind of ramp your way up towards that because we would obviously expect there to be occupancy absorption and cash rent paying rent before that time, but that gives you sort of a timeframe over which we expect to see it stabilized.

Dylan Burzinski, Green Street
Okay. That's actually helpful. Really helpful. Thanks, guys.

Victor Coleman, Chairman & Chief Executive Officer
Thank you, Dylan.

Operator
Thank you. Our final question for today comes from Blaine Heck of Wells Fargo. Your line is now open. Please go ahead.

Blaine Heck, Wells Fargo
Yeah. Thanks for taking the follow-up. We're hearing a lot about the streaming platforms pushing to have more of a foothold in the sports entertainment area. I was wondering if you guys have any view on how that could impact dynamics in the studio space and just overall demand there?

Victor Coleman, Chairman & Chief Executive Officer
Yeah, listen, you're hearing accurately, and what you're finding is live content is been an additional driver of capital for these streaming companies. And so it's in all forms. But, yes, the majority of the capital is going towards sports and sports-related content. It has not, though, taken anything away from the budgetary issues that they've allocated for, for all the other content, whether it's features or shows that are streaming. So it's just – it's in addition to. And Netflix is the biggest contributor. It started with the NFL and now there's follow-ons with Apple and soccer and lots of American football, European football, et cetera. But there's a lot of those examples that are coming to play.

We had commented on this, Blaine, on the last call. Amazon, as an example, which does Thursday Night Football, as everybody knows, has decided to make their sports center here in Los Angeles. So – and as to the tune of Netflix, so their desks that they're going to be reporting from and conducting the live sports commentators are going to be out of LA. Others are in New York. And so that's going to continue. And I think you're going to see more and more capital driven that way. But to date, the capital has not shifted on a budgetary basis away from them creating new content.

Blaine Heck, Wells Fargo
Okay. Great. Thank you.

Operator
Thank you. There are no further questions at this time. I'd like to turn the call back to Victor Coleman, CEO and Chairman, for closing remarks.

Victor Coleman, Chairman & Chief Executive Officer
Thank you so much for participating in our call, and we look forward to speaking to everybody sometime in fall.

Operator
This concludes today's conference call. You may now disconnect your lines.