



10.6%

Vacancy Rate

YoY
Chg12-Mo.
Forecast

-910k

Net Absorption, SF



\$2.73

Asking Rent, PSF



Overall, Net Asking Rent

ECONOMIC INDICATORS
Q2 2020

1.02M

San Jose MSA
EmploymentYoY
Chg12-Mo.
Forecast

11.8%

San Jose MSA
Unemployment Rate

13.0%

U.S.
Unemployment RateSource: BLS, Moody's Analytics
2020Q2 data are based on latest available data

ECONOMY: Unemployment Grows

The COVID-19 pandemic struck the U.S. in March 2020, late in the quarter but with enough time to have a significant impact on first quarter market fundamentals. In the second quarter of 2020, the U.S. economy felt its effects more fully, as government-mandated shutdowns along with shelter-in-place (SIP) ordinances pushed the country deeper into recession. The situation remains very fluid. Access the most recent information specific to COVID-19 [here](#). Job growth in the San Jose metropolitan statistical area (MSA) decreased by 131,800 jobs year-over-year (YOY). This brings regional employment to 1.0 million. This decrease was expected due to the SIP, though jobs are slowly coming back as the economy reopens. The San Jose MSA unemployment rate increased during the quarter, closing at 11.8% which compares to the higher national figure of 13.0%.

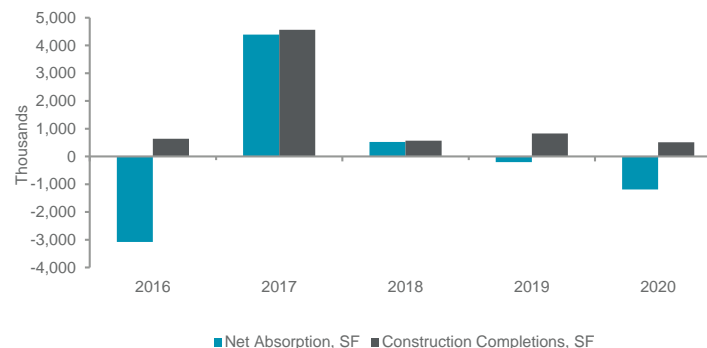
SUPPLY: Vacancy On The Rise

After dropping below 9.0% last year for the first time in three years, Silicon Valley's R&D vacancy rate has been increasing for the last three quarters, finishing the second quarter at 10.6%. However, sublease space as a component of vacancy has stayed fairly consistent recently, ending the quarter at 22.4%, from 22.7% in the first quarter. This sublease number is, however, substantially higher than the ten-year average of 14.1%. Large subleases on the market include Boston Scientific (226,000 sf), Cavium Networks/Marvel (224,000 sf) and HPE (164,000 sf), all in North San Jose. Total vacancy is currently 17.8 million square feet (msf), up from 16.6 msf in the first quarter.

PRICING: Asking Rents Increase Slightly

The average asking rent for R&D space in Silicon Valley increased slightly from \$2.69 per square foot (psf) in the first quarter to \$2.73 psf on a monthly triple net basis. This is a 5.0% increase from one year ago when the asking rent was \$2.60 psf. The northern Silicon Valley cities continue to outperform the market averages posting the highest rents, with Palo Alto at \$7.01 psf, Mountain View at \$4.43 psf, and Menlo Park at \$4.38 psf.

SPACE DEMAND / DELIVERIES



OVERALL VACANCY & ASKING RENT





Silicon Valley

R&D Q2 2020

Occupancy Losses Continue

Net absorption has been in the red since the fourth quarter of 2019. The occupancy loss in the second quarter amounted to a negative 910,000 square feet (sf). This combined with the first quarter number brings the first half 2020 to a negative 1.1 msf. This compares to the full 2019 total of negative 203,000 sf.

Leasing activity also dropped in the second quarter, coming in at 1.8 msf. This is approximate 1.0 msf less than the number recorded in the first quarter. The first half of 2020 gross absorption totaled 4.6 msf. This compares to the record low annual number of 11.4 msf in 2019. The ten-year average gross absorption is 15.1 msf.

Part of the reason for the sudden decrease of deals was that some of the large tech companies have gone on hold with their expansion plans. There were only three transactions over 100,000 sf and one of those was a renewal. The largest deal was the Facebook expansion of 229,000 sf in Fremont. These two buildings are adjacent to the 750,000 sf they leased in Ardenwood in 2018. Another significant deal was Kodiak Sciences' 155,000 sf lease in Palo Alto. Both deals had been negotiating for several months prior to completion. There was also a large renewal in the mix with RMS signing back up for 102,000 sf in Newark.

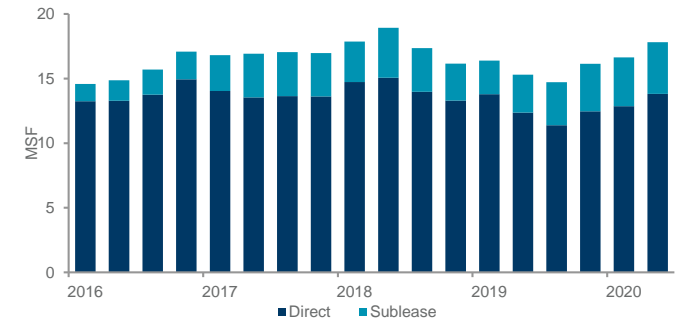
Construction

New product under construction across the region consists of 3.6 msf which breaks down to 2.1 msf of build-to-suits and 1.5 msf of speculative product. Of that 1.5 msf of 'spec', 37.0% has been preleased, leaving 943,000 sf that could enter vacancy once complete. The build-to-suits include Google, Nvidia, and Fortinet who are all building on their own land. Understandably, due to COVID-19, our current tenant tracking has decreased with 4.0 msf of active office/R&D requirements. We believe this to be temporary until the economy opens up and people feel safe to get back to the office. Although the work-from-home model has been successful, surveys are finding many employees miss the culture and collaboration possible within an office environment.

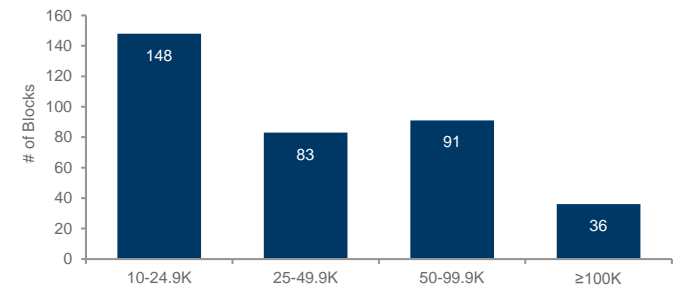
Outlook

- The overall R&D performance in the first half of 2020 was lackluster at best. But even with the increasing vacancy and negative net absorption, rents have thus far held up. As the economy comes back, we expect the Silicon Valley to recover faster than many other markets thanks in part to it being primarily a less-dense low-rise environment.
- Although the demand pipeline has decreased, there are still 4.0 msf of tenants actively looking to expand. We expect this number to grow as tenants get back into their offices.
- Another sign of a reemerging market is the return of NNN leased investments. Right before the end of the quarter several portfolios closed escrow, with two in North San Jose and one in South San Jose.

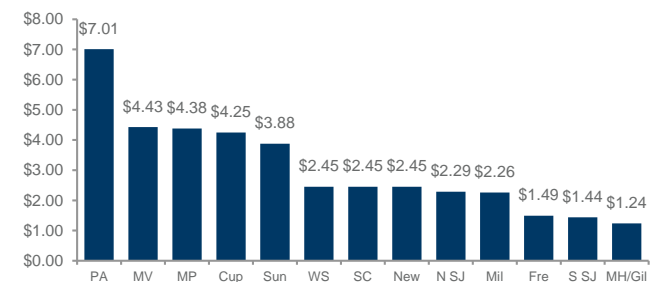
DIRECT VS. SUBLEASE SPACE AVAILABLE COMPARISON



BLOCKS OF CONTIGUOUS SPACE



ASKING RENT COMPARISON





MARKET STATISTICS

SUBMARKET	INVENTORY (SF)	SUBLET VACANT (SF)	DIRECT VACANT (SF)	VACANCY RATE	CURRENT NET ABSORPTION (SF)	YTD NET ABSORPTION (SF)	YTD LEASING ACTIVITY (SF)	UNDER CONST (SF)	OVERALL AVG ASKING RENT*
Menlo Park	3,907,913	0	97,363	2.5%	(4,224)	(27,331)	94,859	0	\$4.38
Palo Alto	10,378,934	400,931	896,672	12.5%	(379,190)	(251,940)	392,439	85,420	\$7.01
Mountain View	14,672,797	378,788	447,714	5.6%	10,521	(166,771)	143,273	1,218,372	\$4.43
Cupertino	5,698,336	0	28,125	0.5%	(125)	16,365	413,903	0	\$4.25
Westside	2,284,992	17,125	126,536	6.3%	29,109	15,718	128,933	0	\$2.45
Sunnyvale	23,357,153	254,999	1,038,817	5.5%	(220,572)	38,164	567,198	1,562,361	\$3.88
Santa Clara	21,622,165	639,512	2,115,695	12.7%	39,487	(458,558)	641,969	750,000	\$2.45
North San Jose	36,048,400	1,368,116	3,987,660	14.9%	(72,597)	90,080	1,097,193	0	\$2.29
South San Jose	10,350,861	250,592	783,225	10.0%	19,079	(25,257)	67,555	0	\$1.44
Milpitas	12,724,829	201,280	2,158,048	18.5%	(107,458)	38,884	245,378	0	\$2.26
Fremont	20,685,146	236,960	1,850,601	10.1%	(196,235)	(350,027)	687,447	0	\$1.49
Newark	3,047,685	204,828	120,363	10.7%	1,990	(45,357)	133,171	0	\$2.45
Morgan Hill/Gilroy	3,583,090	40,000	163,969	5.7%	(30,394)	(25,819)	34,821	0	\$1.24
TOTALS	168,362,301	3,993,131	13,814,788	10.6%	(910,609)	(1,187,011)	4,648,139	3,616,153	\$2.73

*Rental rates reflect triple net asking

*Market indicators are not reflective of US MarketBeat tables

KEY LEASE TRANSACTIONS Q2 2020

PROPERTY	SUBMARKET	TENANT	LANDLORD	SF	TYPE
6800-6900 Dumbarton Cir	Fremont	Facebook	Peery Arrillaga	229,530	New Lease
1050 Page Mill Rd	Palo Alto	Kodiak Sciences	Sand Hill Property Company	155,474	New Lease
7777 Gateway Blvd	Newark	RMS	BioMed Realty Trust, Inc.	102,473	Renewal
3301-3521 Leonard Ct	Santa Clara	Thermo Fisher Scientific	PS Business Parks	90,095	Expansion/Renewal
44370 Christy St	Fremont	Bloom Energy	Dermody Properties	88,246	New Deal

KEY SALES TRANSACTIONS Q2 2020

PROPERTY	SUBMARKET	SELLER / BUYER	SF	PRICE / \$ PSF
San Ignacio & Great Oaks portfolio	South San Jose	DRA Advisors / Kennedy Wilson	257,453	\$53.5M / \$207
100 Headquarters & 200 Holger Wy	North San Jose	KBS / Exan Group	142,710	\$95.2M / \$667
2560-2570 Orchard Pkwy	North San Jose	Regency Valley Center, LLC / Takara Bio USA	129,024	\$44.8M / \$347
3041 Orchard Pkwy*	North San Jose	Allied Telesis / Mizuho Corporate Bank	64,466	\$19.8M / \$306
165 Gibraltar Ct	Sunnyvale	Nearon / Google, Inc.	48,666	\$28.5M / \$585

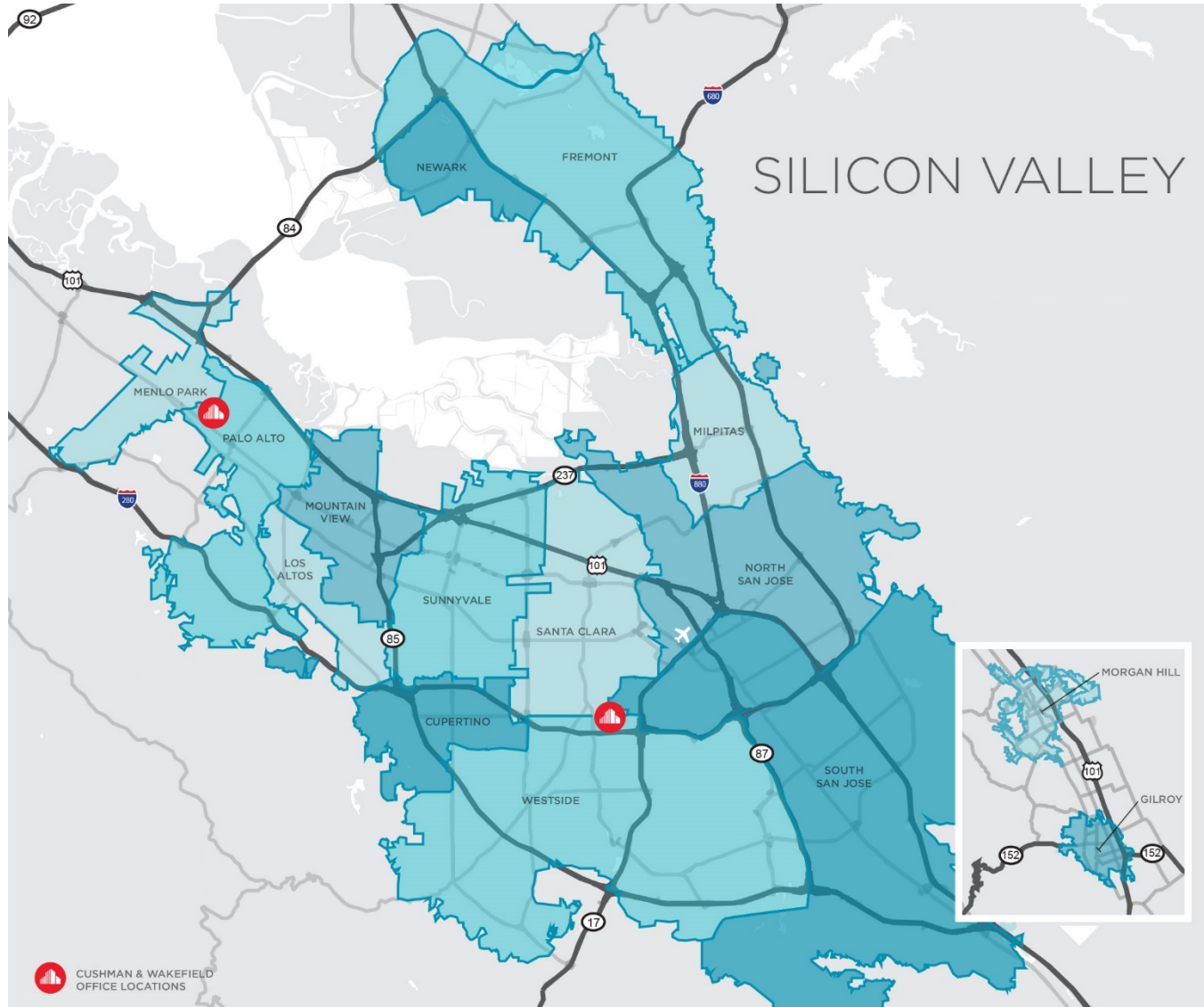
* Sale leaseback

Silicon Valley

R&D Q2 2020

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R&D SUBMARKETS



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