

MARKETBEAT SAN DIEGO

Office Q3 2020



13.3%

Vacancy Rate

YoY
Chg



12-Mo.
Forecast



-355K

Net Absorption, SF



\$3.39

Asking Rent, PSF



(Direct, All Property Classes)

ECONOMIC INDICATORS Q3 2020

1.4M

San Diego
Employment

YoY
Chg



12-Mo.
Forecast



11.9%

San Diego
Unemployment Rate



8.8%

U.S.
Unemployment Rate



Source: BLS.

ECONOMIC OVERVIEW: Decreasing Unemployment Shows Signs of Life

The San Diego employment market has been significantly affected by COVID-19 stay-at-home orders, resulting in loss of 135,800 jobs or -9.0% year-over-year (YOY) through August 2020.¹ Of the 135,800 jobs lost, 60,100 (-28.9% YOY) or 44% of losses were in the leisure and hospitality sector. Professional and business services sector lost just 300 jobs (-0.1% YOY). During the same time period, the monthly unemployment rate increased from 3.4% last year to 9.9% and is currently 420 basis points (bps) above the 30-year average of 5.7% and 200 bps below the Q3 2020 quarterly average of 11.9%. All employment sectors are expected to shrink at a combined rate of -7.5% in 2020 and -0.4% in 2021. San Diego's economy of \$244.9 billion as measured by gross regional product is forecasted to shrink by 4.9% in 2020 and return to growth of 3.6% in 2021, above its 10-year average of 3.2%.²

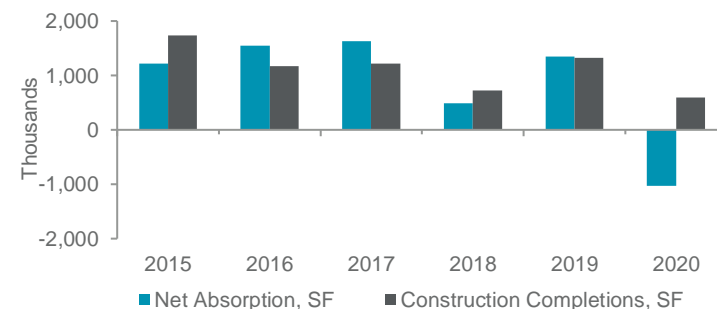
SUPPLY AND DEMAND: Large Vacancies and Limited Occupancies

At the end of Q3 2020, San Diego's direct office vacancy was 13.3%, an increase of 70 bps from the previous quarter and 150 bps from a year ago. Sublease vacancy increased 20 bps from last quarter and 50 bps YOY. Tenants returned 355,000 square feet (sf) in Q3 2020 compared to 495,000 sf in Q2 2020 and 272,000 sf in Q1 2020, marking the third consecutive quarter of negative absorption. Negative net absorption for three consecutive quarters was last seen in 2009. Year-to-date (YTD), tenants have returned over one million sf across all submarkets with Mission Valley recording the most (-108,000 sf), while Rancho Bernardo accounting for the two largest single tenant vacancies with both Renovate America and BioMed Realty vacating over 50,000 sf each. Countywide, Class A space recorded limited positive absorption of 6,000 sf, while Class B experienced the most negative absorption (-258,000 sf) or 73% of total losses. Though overall occupancy growth was negative in Q3 2020, several companies did occupy this quarter, such as SIS Insurance, Apple and Mapp Biopharmaceutical. The delivery of One Paseo contributed significantly to positive absorption with occupancies from ACADIA Pharmaceuticals, Fish & Richardson, Compass and Boxer Capital, with additional pre-leased tenants expected to occupy in the near future. Previously signed deals for large blocks of space by companies such as Apple, Fate Therapeutics, Wawanesa Insurance and Guild Mortgage will contribute positively to occupancy growth in upcoming quarters.

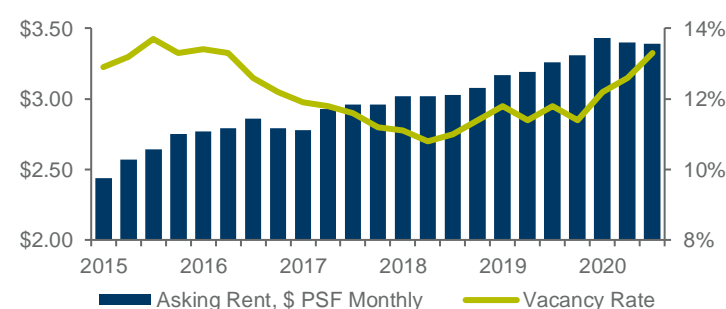
PRICING: Rents Remain Flat

Countywide average asking rent for all classes combined dipped to \$3.39 per square foot (psf) on a monthly full-service basis. This metric decreased by just \$0.01 over the last three months but increased 4.0% from where it stood a year ago. Over the past 12 months, Class A average rent has increased by 1.9% to \$3.77 psf, while the Class B rate has increased by 5.0% to \$3.33 psf, largely as a result of significant acquisitions and conversions of older product to lab space.

SPACE DEMAND / DELIVERIES



DIRECT VACANCY / ASKING RENT





TENANT TRENDS: Apple, Biotech Lead New Leasing

Leasing activity was slower in Q3 2020 at 930,500 sf, including renewals, compared to Q2 2020 at 1.3 million square feet (msf). YTD leasing stands at 4.2 msf of which 2.7 msf are new leases and 1.5 msf are renewals. Apple contributed to two of the largest new leases in Q3 2020, signing for 78,000 sf and 44,000 sf in Eastgate. The rest of large new leasing came from the life sciences sector, including Guardant Health, Organogenesis and Helix. Life sciences sector also comprises several expected occupancies in future quarters, including Fate Therapeutics, Alphatec Spine and AnaptysBio. Other companies, including Guild Mortgage, Fairfield Properties and Wawanesa Insurance are also expected to occupy as the county reopens and COVID-19 restrictions are lifted. Apple has nearly 600,000 sf of leases for existing and under construction product that the company is expected to occupy over the next 12 months, with further plans for a major San Diego campus.

FUTURE INVENTORY: Developers Seek Out Life Sciences

Of the 20 properties currently under construction countywide, totaling over 2.8 msf, 30% are pre-leased and 197,000 sf are expected to be delivered by the end of the year. Nearly 44% or 1.2 msf of inventory under construction is in the Downtown submarket with 0% pre-leased. These projects are expected to add significantly to the Downtown vacancy in a near future until they are absorbed. IQHQ plans to add to the Downtown development pipeline after acquiring the former Manchester Pacific Gateway site. IQHQ plans to develop Downtown San Diego's first life sciences campus. Phase one of the development is expected to begin soon.

Since the beginning of the year, over 622,000 sf of speculative biotech product has broken ground. Cooley leased 73,800 sf, an entire building at The Boardwalk, Healthpeak Properties' newest Class A life sciences development located in Torrey Pines. Element Biosciences leased 104,200 sf for a new Building at Alexandria Tech Center which broke ground this quarter. Organogenesis took 23,000 sf at Muse Torrey Pines.

Much of future absorption will come from leases signed for projects currently under construction. In Eastgate, Apple leased two buildings for over 364,000 sf due for occupancy in early 2021. In Oceanside, a 100,000-sf built-to-suit project for the County of San Diego Health & Human Services department is estimated to be completed in 2020.

Sources: www.bls.gov ² GDP as of 2019. Moody's Analytics economy.com 9/2020.

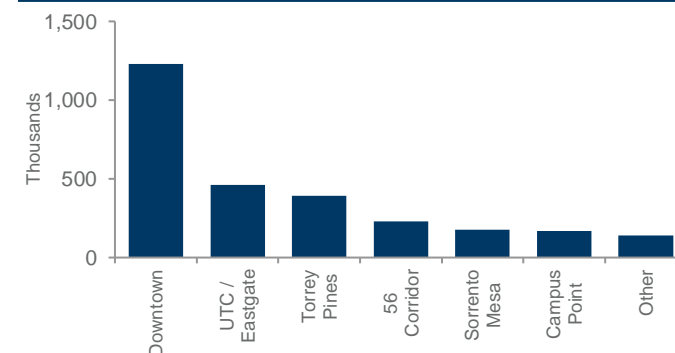
OUTLOOK

- Rising positivity rates for COVID-19 delayed reopening plans in California, resulting in a slower leasing activity through the summer. Tenants are reassessing their footprint based on work-from-home policies of their employees as well as both short and long-term needs of working through and after the pandemic. Leasing within the 10,000 to 50,000 sf range will continue to be the main driver of activity, accounting for 43% of total sf in lease obligations set to expire over the next 18 months.
- Active tenant requirements of all sizes remain at 4.3 msf over the next 24 months countywide, led by life sciences tenants. While many of these tenants paused their plans due to COVID-19, most of them have returned to exploring the market, have sent out proposals and are in the intermediate stages of their search. While not all of the current tenants in the market will transact in the short term, these levels provide a barometer to leasing activity in quarters to follow.

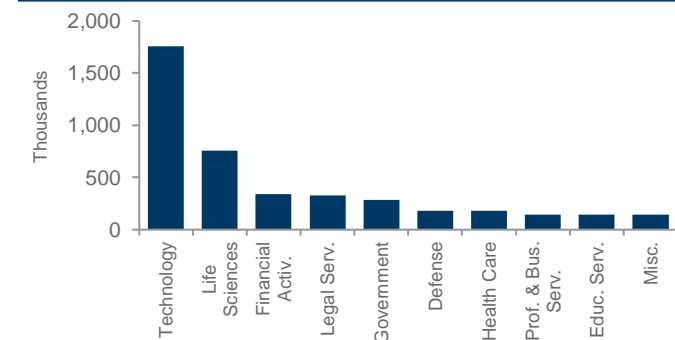
AVERAGE ASKING RENT \$PSF MONTHLY FULL SERVICE



UNDER CONSTRUCTION BY SUBMARKET IN SF



TENANT DEMAND BY INDUSTRY SECTOR IN SF





MARKET STATISTICS

SUBMARKET	INVENTORY (SF)	SUBLET VACANT (SF)	DIRECT VACANT (SF)	DIRECT VACANCY RATE	CURRENT QTR DIRECT NET ABSORPTION (SF)	YTD DIRECT NET ABSORPTION (SF)	YTD LEASING ACTIVITY** (SF)	YTD CONSTR COMPLETIONS (SF)	UNDER CNSTR (SF)	DIRECT AVG ASKING RENT (ALL CLASSES)*	DIRECT AVG ASKING RENT (CLASS A)*
North County	11,494,299	74,295	1,861,188	16.2%	-61,732	-178,413	354,692	20,000	128,000	\$2.73	\$3.07
Central County	52,960,173	651,677	6,404,891	12.1%	-178,952	-576,596	2,132,822	285,550	1,443,292	\$3.60	\$3.96
South County	17,663,871	170,977	2,676,475	15.2%	-113,887	-280,567	166,129	290,260	1,232,767	\$3.27	\$3.74
Class A	36,746,857	400,192	5,122,005	13.9%	5,984	-316,178	1,373,984	575,810	2,664,487	\$3.77	
Class B	35,266,110	451,834	4,703,468	13.3%	-258,192	-519,430	1,207,160	20,000	139,572	\$3.33	
Class C	10,105,376	44,923	1,117,081	11.1%	-102,363	-199,968	72,499	0	0	\$2.07	
SAN DIEGO TOTALS	82,118,343	896,949	10,942,554	13.3%	-354,571	-1,035,576	2,653,643	595,810	2,804,059	\$3.39	

*Rental rates reflect full service asking. **Renewals not included in leasing statistics.

KEY LEASE TRANSACTIONS Q3 2020

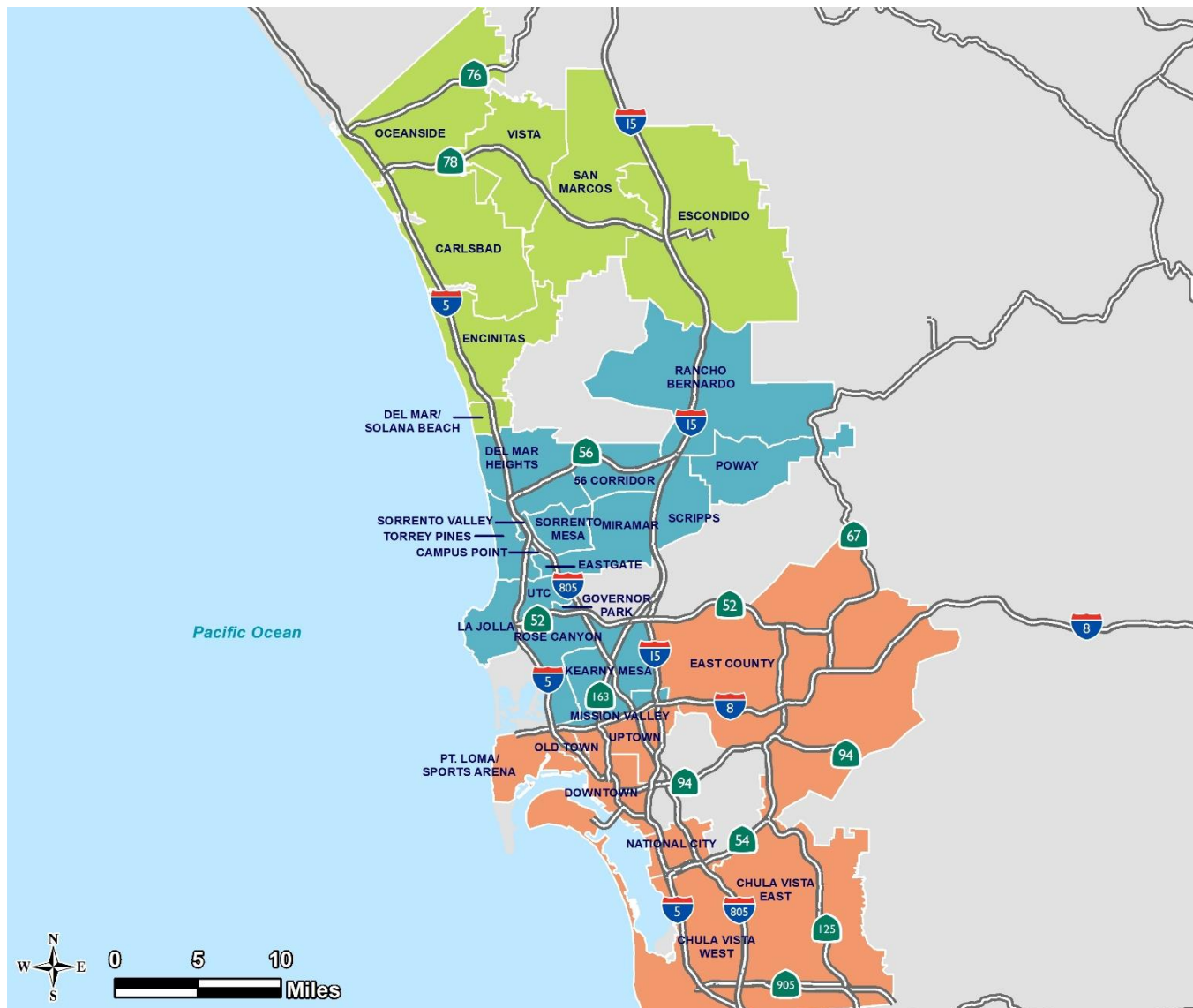
PROPERTY	SUBMARKET	TENANT	SF	TYPE
City Science Park	Sorrento Mesa	Tanvex	136,807	Renewal*
Kilroy Centre Del Mar	Del Mar Heights	Scripps Health	118,912	Renewal*
Axiom	Eastgate	Apple	78,470	New
Hazard Center	Mission Valley	Kimball, Tirey & St. John	36,665	Renewal*
Muse Torrey Pines	Torrey Pines	Organogenesis	22,966	New

KEY SALES TRANSACTIONS Q3 2020

PROPERTY	SUBMARKET	SELLER / BUYER	SF	PRICE / \$ PSF
The Pointe at Torrey Pines	Torrey Pines	National University / Alexandria Real Estate Equities	139,135	\$97.0M / \$701
One Technology Place	Rancho Bernardo	Menlo Equities / Dollinger Properties	137,695	\$39.0M / \$283
Creekside	Sorrento Valley	The Blackstone Group / Longfellow Real Estate Partners	124,473	\$42.8M / \$343
Cornerstone Heights Corporate Center	Sorrento Mesa	Buchanan Street Partners / Timothy James Mullahey	51,690	\$20.6M / \$399
Carlsbad Medical Center	Carlsbad	H.G. Fenton Company / Scripps Health	46,199	\$24.8M / \$536

KEY CONSTRUCTION COMPLETIONS YTD 2020

PROPERTY	SUBMARKET	TENANT	SF	OWNER
One Paseo	Del Mar Heights	ACADIA Pharmaceuticals, Fish & Richardson, Compass California	285,550	Kilroy Realty Corporation
The Paladion	Downtown	N/A	167,181	Bosa Development
Kettner & Ash	Downtown	SPACES	123,079	DivcoWest / Ocean West

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