

	YoY Chg	12-Mo. Forecast
<b>13.3%</b> Vacancy Rate	▼	▼
<b>22K</b> Net Absorption, SF	▼	▲
<b>\$3.62</b> Asking Rent, PSF	▲	▲

(Overall, All Property Classes)

## ECONOMIC INDICATORS Q4 2022

	YoY Chg	12-Mo. Forecast
<b>1.5M</b> San Diego Employment	▲	▲
<b>3.2%</b> San Diego Unemployment Rate	▼	▲
<b>3.7%</b> U.S. Unemployment Rate	▼	▲

Source: BLS

## ECONOMIC OVERVIEW

The total nonfarm employment in San Diego grew by 48,400 or +3.2% year-over-year (YOY) between November 2021 through November 2022, with the leisure and hospitality sector accounting for the most significant gains or 19,900 jobs added (+10.9% YOY), followed by professional and business services adding 12,700 jobs (+4.6% YOY). During the same time, the monthly unemployment rate decreased from 4.5% last year to 3.3% and is currently 10 basis points (bps) above the quarterly average of 3.2%.<sup>1</sup> All employment sectors are expected to grow at a combined rate of 0.8% (+12,340 jobs) in 2023, while office employment is forecasted to contract by 1.5% (-5,610 jobs) and return to growth of 0.2% in 2024 (+670 jobs). The annual unemployment rate is forecasted to decrease from 3.6% in 2022 and 3.5% in 2023. San Diego's economy of \$260.0 billion as measured by 2022 gross regional product is forecasted to grow 1.2% in 2023.<sup>2</sup>

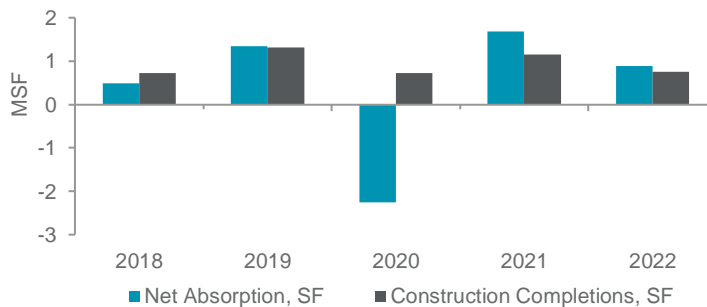
## SUPPLY AND DEMAND

San Diego's overall office vacancy rate increased 20 bps quarter-over-quarter (QOQ) and decreased 70 bps YOY to 13.3% in Q4 2022. Sublease vacancy increased by 40 bps QOQ and 100 bps YOY to 1.8% while direct vacancy decreased by 30 bps QOQ and 160 bps YOY to 11.5%. Year-to-date, occupancy gains totaled 887,746 square feet (sf), with Class A gains accounting for nearly two-thirds of the total gains. Excluding sublease, tenants absorbed 427,168 sf on a direct basis in Q4 2022, marking the eighth consecutive quarter of occupancy gains since the beginning of the COVID-19 pandemic. Direct net absorption was positive among Class A buildings (+320,218 sf) and class B (+137,241 sf), while space was returned in class C (-30,291 sf) inventory. Sorrento Mesa recorded the most positive direct net absorption in Q4 2022 (+157,565 sf) thanks to life sciences occupancies, followed by Torrey Pines (+140,644 sf) with the delivery of the fully leased Spectrum III and Kearny Mesa (+78,735 sf) where the State of California occupied two floors and Sunroad Centrum and multiple properties were purchased by owner/users. Few submarkets experienced negative direct absorption this quarter, with the largest decrease in occupancy in Mission Valley (-67,147 sf).

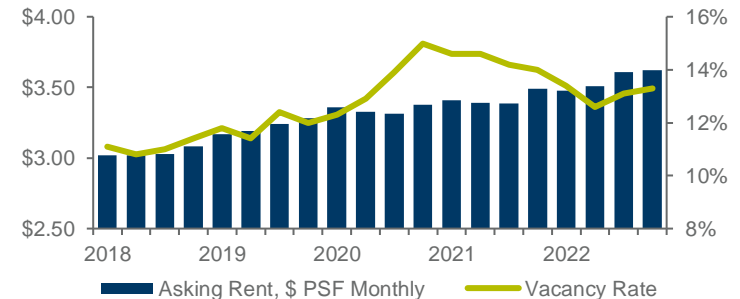
## TENANT TRENDS

Leasing activity tempered significantly in Q4 2022 at 607,000 across 75 deals, excluding renewals, compared to 1.1 million square feet (msf) across 103 deals in Q3 2022 and 2.1 msf (136 deals) in Q4 2021. Kearny Mesa was the most active market, accounting for 23% of new deals, followed by Downtown (22%) and Mission Valley (10%). Kearny Mesa was bolstered by the Veteran Benefits Administration accounting for the bulk of new leasing, while Downtown saw positive activity from new tenants taking space, including the second life sciences tenant at 1155 Island Ave. and the first office tenant at Kilroy Realty's 2100 Kettner project.

## SPACE DEMAND / DELIVERIES



## OVERALL VACANCY / ASKING RENT



Most of the expected future absorption from previously signed leases will come from the life sciences sector, including tenants like Native Microbials and Neurocrine Biosciences. Though Apple comprises much of the tenant activity for large blocks of traditional space, other office users, Gomez Trial Attorneys and Turner Construction, committed to leases and are expected to occupy in the upcoming quarters.

### PRICING

The countywide average direct asking rent across all classes increased 5.7% from \$3.52 per square foot (psf) to \$3.72 psf on a monthly full-service basis from a year ago, while the overall average asking rent, including sublease space, increased 3.7% from \$3.49 psf to \$3.62 psf. Over the past 12 months, Class A direct average rent has increased by 2.2% to \$4.21 psf, while Class B average rent has increased by 13.4% to \$3.46 psf. New speculative (SPEC) construction and life sciences conversions of older buildings are expected to push rents higher over the next 12 months. While submarkets directly impacted by life sciences development and conversion are growing rents fastest, Del Mar Heights is benefitting the most among traditional office products, with direct asking rents rising 9.7% YOY.

### FUTURE INVENTORY

Of the 34 properties, totaling over 5.9 msf, currently under construction countywide, 33% are pre-leased and 3.7 msf are expected to be delivered by the end of 2023. The majority or 69% of inventory, totaling 4.1 msf across 22 buildings, is speculative with the remaining 31%, totaling 1.9 msf across 12 buildings, build-to-suit. Approximately 43% or 2.6 msf of inventory currently under construction is in the Downtown submarket. Additionally, there are 83 proposed projects, totaling 26.4 msf, across all classes.

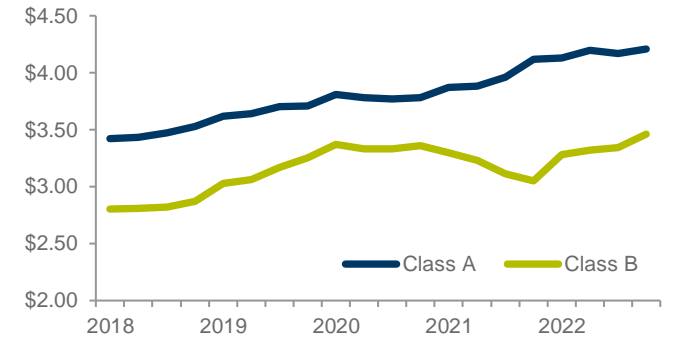
Developers continue to acquire projects for potential conversion and redevelopment, such as Breakthrough Properties' acquisitions of Governor Pointe in Governor and the industrial multi-tenant project Environmental Plaza in Sorrento Valley. Life sciences represent most of the new development as developers look at existing office sites for opportunities, pushing existing tenancy to other submarkets, which is anticipated to increase tenant activity throughout the next 12-15 months. The traditional office represents just a quarter of new development, including La Jolla Commons III in UTC, 16707 Via Del Campo in Rancho Bernardo and the Sandbox in Solana Beach.

Sources: <sup>1</sup>[www.bls.gov](http://www.bls.gov) <sup>2</sup>Moody's Analytics economy.com 12/2022.

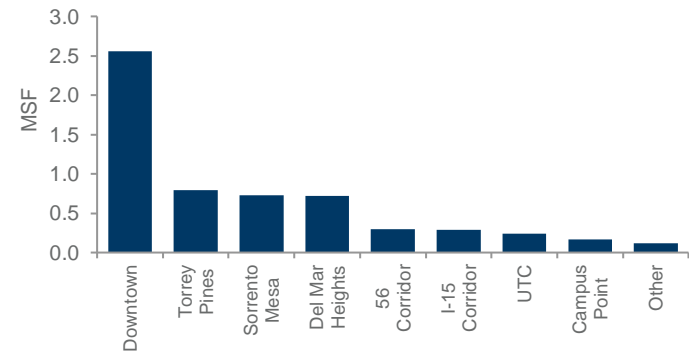
### OUTLOOK

- Tenants are reassessing their real estate footprint based on work-from-home policies as well as assessing both short and long-term needs 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 39% of total sf in lease obligations set to expire 12 to 24 months from the end of the quarter.
- Active tenant requirements of all sizes remain robust at 3.0 msf over the next 24 months countywide. While many of these tenants paused their plans due to COVID-19, a majority have reactivated their requirements or begun exploring the market. While not all current tenants in the market will transact in the short term, these levels provide a barometer for leasing activity in subsequent quarters.

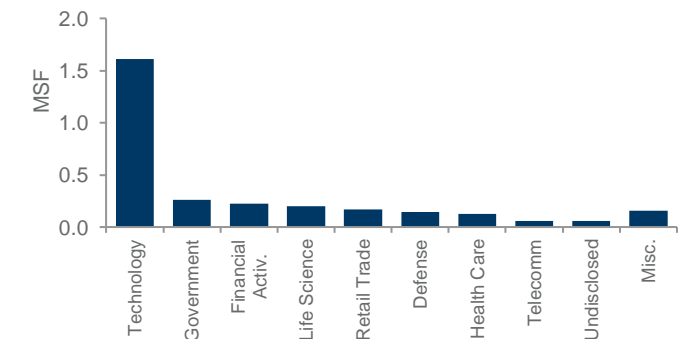
### AVERAGE DIRECT ASKING RENT \$PSF MONTHLY



### UNDER CONSTRUCTION INVENTORY BY SUBMARKET



### TENANT DEMAND BY INDUSTRY SECTOR



## MARKET STATISTICS

SUBMARKET	INVENTORY (SF)	DIRECT VACANT (SF)	SUBLET VACANT (SF)	OVERALL VACANCY RATE	CURRENT QTR OVERALL ABSORPTION (SF)	YTD OVERALL ABSORPTION (SF)	YTD LEASING ACTIVITY** (SF)	YTD CONSTR COMPLETIONS (SF)	UNDER CNSTR (SF)	OVERALL AVG ASKING RENT (ALL CLASSES)*	OVERALL AVG ASKING RENT (CLASS A)*
North County	11,703,802	1,361,264	132,463	12.8%	-32,732	151,371	442,270	20,177	50,000	\$2.89	\$3.25
Central County	54,767,687	5,016,696	1,227,262	11.4%	38,044	842,909	4,536,747	737,596	3,321,428	\$3.85	\$4.46
South County	17,966,664	3,330,212	195,411	19.6%	16,247	-106,534	346,548	0	2,558,500	\$3.55	\$4.02
Class A	39,130,947	5,226,020	952,062	15.8%	112,117	576,512	3,722,516	757,773	5,929,928	\$4.12	
Class B	35,781,519	3,504,578	586,626	11.4%	-62,566	219,323	1,515,973	0	0	\$3.30	
Class C	9,525,687	977,574	16,448	10.4%	-27,992	91,911	87,076	0	0	\$2.18	
<b>SAN DIEGO TOTALS</b>	<b>84,438,153</b>	<b>9,708,172</b>	<b>1,555,136</b>	<b>13.3%</b>	<b>21,559</b>	<b>887,746</b>	<b>5,325,565</b>	<b>757,773</b>	<b>5,929,928</b>	<b>\$3.62</b>	

\*Rental rates reflect full service asking, psf monthly. \*\*Renewals not included in leasing statistics.

## KEY LEASE TRANSACTIONS Q4 2022

PROPERTY	SUBMARKET	TENANT	SF	TYPE
8620 Spectrum Center Blvd.	Kearny Mesa	Veteran Benefits Administration	120,209	New
1155 Island Ave.	Downtown	Excellos	36,000	New
300 Rancheros Dr.	San Marcos	Welk Resort Group	30,308	Renewal**
5880 Oberlin Dr.	Sorrento Mesa	Innoflight	30,192	New
2100 Kettner Blvd.	Downtown	Boston Consulting Group	27,945	New

## KEY SALES TRANSACTIONS Q4 2022

PROPERTY	SUBMARKET	SELLER / BUYER	SF	PRICE / \$ PSF
Carlsbad Executive Plaza & The Plaza VIII	Carlsbad	Brookwood Financial Partners / MC Strauss Company	222,005	\$48.6M / \$219
3838 Camino Del Rio N.	Mission Valley	HighBrook Investors / Bitwise at State Center LLC	94,612	\$21.6M / \$228
9370 Sky Park Ct. & 4180 Ruffin Rd.	Kearny Mesa	Gleich Family Trust	71,070	\$18.5M / \$260
1959 Palomar Oaks Way & 1800 Thibodo Rd.	Carlsbad / Vista	Labyrinth / MJL Properties	70,963	\$13.9M / \$196
9210 Sky Park Ct.	Kearny Mesa	Omninet Capital / Bill Howe Plumbing	39,583	\$10.5M / \$264

## KEY CONSTRUCTION COMPLETIONS 2022

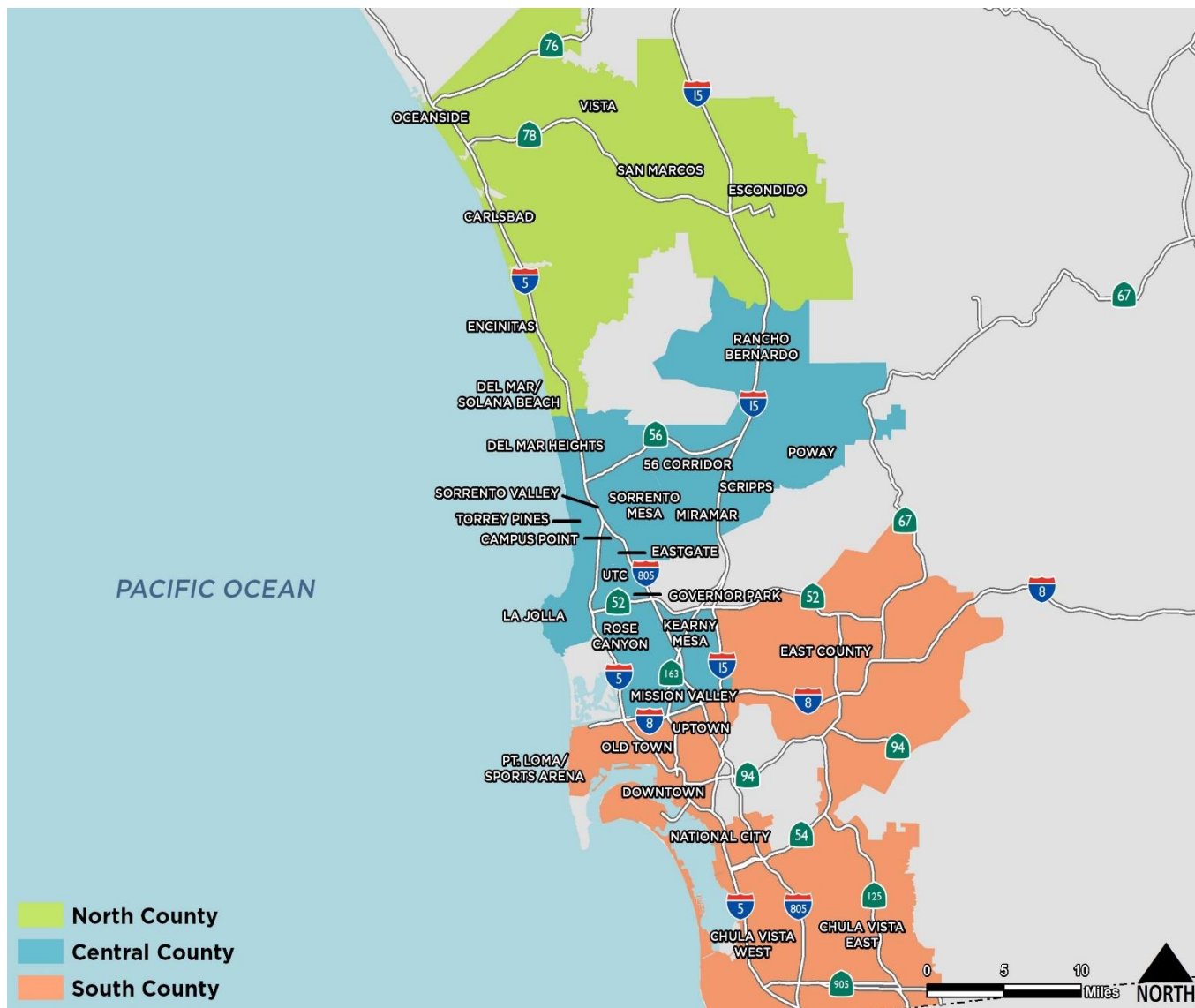
PROPERTY	SUBMARKET	TENANT	SF	OWNER
APEX	Eastgate	Apple	204,000	BioMed Realty
Alexandria Tech Center	Sorrento Mesa	Element Biosciences	195,435	Alexandria Real Estate Equities
The Boardwalk	Torrey Pines	Cooley LLP, Zentalis Pharmaceuticals, Arcturus	191,705	Healthpeak Properties



# SAN DIEGO

Office Q4 2022

OFFICE SUBMARKETS



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