

**TIGHT MARKET.** The San Diego Flex R&D market fundamentals displayed continued signs of tight supply at the finish of the second quarter of 2017, with low availability, continued low transaction volume, and little supply in the construction pipeline for the immediate future. However, with the steady pace of job growth in the biotech and life sciences industries that drive the Flex/R&D market in San Diego, the market should continue to grow at a slow but steady pace.

**VACANCY.** Direct/sublease space (unoccupied) finished the second quarter at 7.81%, a decrease of 10.23% when compared with the same time last year, and a decrease of more than 50% from 2010's recession low of 16.12%.

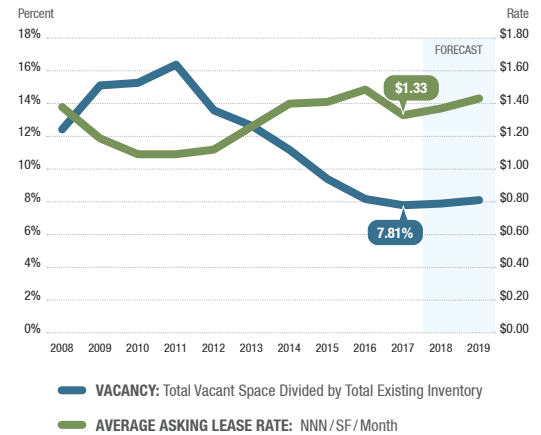
**LEASE RATES.** The average asking triple net lease rate per square foot per month in San Diego County was \$1.33 at the end of the second quarter, which decreased from last quarter's rate of \$1.36. Although a dip in price occurred this quarter, the average asking lease rates have risen a full forty cents (\$0.40) since the recession lows seen in the first and second quarters of 2011, and are still continuing the upward long-term trend.

**TRANSACTION ACTIVITY.** The combined amount of square feet leased or sold in the second quarter totaled 1.22 million square feet, which is up slightly from last quarter's 1.21 million square feet. This statistic can have some lag time in being reported, so look for this quarter's figures to end up somewhat higher in the next report.

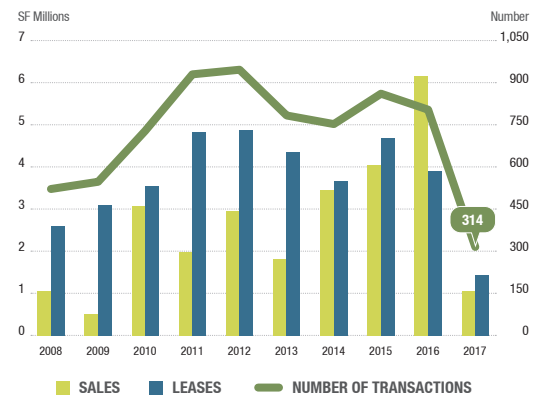
**EMPLOYMENT.** The unemployment rate in San Diego County was 3.6% in May 2017, down from a revised 3.8% in April 2016 and below the year-ago estimate of 4.3%. This compares with an unadjusted unemployment rate of 4.2% for California and 4.1% for the nation during the same period. According to the State of California Employment Development Department, San Diego County gained 20,300 payroll jobs between May 2016 and May 2017, including 6,000 from government services, which reported the largest overall gain. The construction sector reported a growth of 5,000 jobs, and the educational and health services reported an increase of 3,900 jobs.

**OVERALL.** The San Diego Flex R&D market remains tight at the midpoint of 2017, but as the life science and biotech sectors continue to drive San Diego's economy, the market will continue to grow at a steady pace. Because this booming industry targets space in San Diego specifically, there will be ongoing construction and new deliveries in response to the demand, and this will contribute to the slow uptick in availability in the coming future.

### VACANCY vs. AVERAGE ASKING LEASE RATE



### TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



### Market Statistics

	Change Over Last Quarter	2Q 2017	1Q 2017	2Q 2016	% Change Over Last Year
Vacancy Rate	▼ DOWN	7.81%	8.39%	8.70%	(10.23%)
Availability Rate	▲ UP	12.41%	12.23%	13.42%	(7.53%)
Average Asking Lease Rate	▼ DOWN	\$1.33	\$1.36	\$1.47	(9.52%)
Sale & Lease Transactions	▲ UP	1,220,668	1,212,310	2,198,226	(44.47%)
Gross Absorption	▼ DOWN	1,119,960	1,157,718	903,312	23.98%
Net Absorption	▲ POSITIVE	250,743	244,448	38,435	N/A

**EMPLOYMENT.** The labor market in San Diego County will continue to improve, although we anticipate job growth to slow to 1.8%, or 25,000 jobs, over the year. With an expected growth in tourism and the local economy in general, look for sectors like leisure and hospitality to lead the way for employment gains, followed by health care and biotech, and government employment.

**CONSTRUCTION.** Construction in the Flex/R&D sector has been largely concentrated in the biotech subset of properties. For the remainder of the Flex/R&D market, there has been remarkably little new construction. We expect this to change with the “creative industrial” trend migrating into the Flex/R&D market.

**LEASE RATES.** Expect average asking rates to increase by approximately 2–3% over the next four quarters.

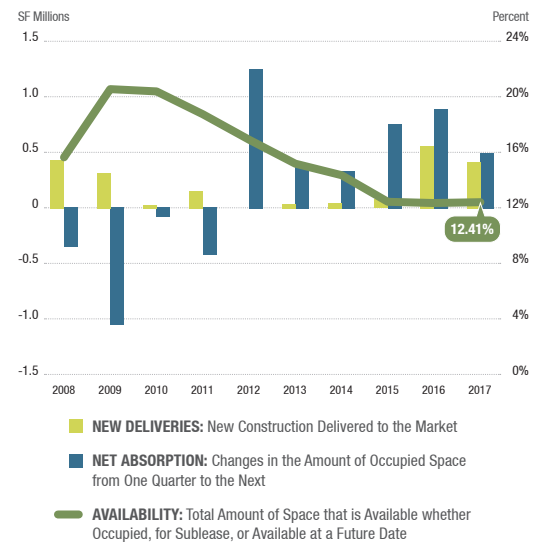
**VACANCY.** With new deliveries hitting the market this year, we anticipate vacancy rates to tick up slightly in the coming quarter, to around 8.1% by the end of the year.

**CONSTRUCTION.** At the end of the second quarter, there were 1,109,492 square feet under construction in San Diego County’s flex market. Approximately 367,000 square feet were delivered in the first two quarters of the year, and a majority of the buildings currently under construction are due to complete this year. Notable projects underway, for two prominent biotech companies, include Vertex Pharmaceuticals build-to-suit property in Torrey Pines, and Illumina’s 316,000 square foot expansion at i3 Campus in UTC. Illumina is slated to take occupancy this year, and Vertex is projecting occupancy in 2018.

**AVAILABILITY.** Direct/sublease space being marketed was 12.41% at the end of the quarter, a 7.53% decrease from the previous year’s rate of 13.42%.

**ABSORPTION.** The San Diego Flex R&D market posted 250,743 square feet of positive net absorption in the second quarter, giving the market a total of more than four million square feet of positive absorption over the past six and a half years.

NEW DELIVERIES & NET ABSORPTION vs. AVAILABILITY RATE



Significant Transactions

Sales

\* Voit Real Estate Services Deal

Property Address	Submarket	Square Feet	Sale Price	Buyer	Seller
Scripps Ranch Business Park	Scripps Ranch	186,157	\$31,400,000	Hill Properties	RREEF Management
Ponderosa Technology Park	Kearny Mesa	155,691	\$28,525,000	BKM Capital Partners, LP	Granite Peak Partners
Trade Center	Miramar	118,457	\$21,250,000	Double Eagle Jet LLC	Colony Northstar
14145 Danielson St.	Poway	117,354	\$20,000,000	General Atomics	Poway Danielson, LLC
3205 Lionshead Ave.	Carlsbad	47,850	\$11,150,000	Landwin Management	Aethercomm, Inc.

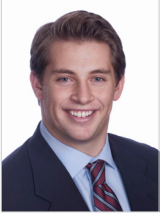
Leases

\* Voit Real Estate Services Deal

Property Address	Submarket	Square Feet	Transaction Date	Tenant	Owner
9625 Towne Centre Dr.	UTC	150,000	Jun-2017	Takeda	Alexandria Real Estate
13112 Evening Creek Drive – Renewal	Rancho Bernardo	109,780	Apr-2017	LabCorp	Alexandria Real Estate
6122–6126 Nancy Ridge Dr.	Miramar	49,294	Jun-2017	Undisclosed	Sublease
1891 Rutherford Rd.	Carlsbad	25,776	Jun-2017	Undisclosed	Diversified Properties
10070 Barnes Canyon Rd.	Sorrento Mesa	24,000	Jun-2017	Undisclosed	BLT Enterprises

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 2Q2017	Square Feet Available	Availability Rate 2Q2017	Average Asking Lease Rate	Net Absorption 2Q2017	Net Absorption 2017	Gross Absorption 2Q2017	Gross Absorption 2017
<b>Central</b>													
Central City	15	175,224	0	0	9,442	5.39%	11,840	6.76%	\$0.00	466	466	6,613	6,613
East City	3	31,892	0	0	0	0.00%	0	0.00%	\$0.00	0	1,000	0	1,000
Southeast City	17	197,755	0	0	5,000	2.53%	0	0.00%	\$0.00	0	0	0	0
Kearny Mesa	204	5,509,650	156,000	0	350,329	6.36%	736,106	13.36%	\$1.43	(32,808)	(93,606)	85,481	144,480
Mission Gorge	29	287,556	0	0	14,966	5.20%	32,393	11.26%	\$1.60	8,739	5,959	15,150	17,110
Rose Canyon/Morena	38	609,335	0	0	22,626	3.71%	26,742	4.39%	\$0.00	(589)	10,908	3,446	34,603
Sports Arena/Airport	30	380,720	0	0	0	0.00%	0	0.00%	\$0.00	1,350	1,350	1,350	1,350
Miramar	219	4,741,828	0	11,760	404,803	8.54%	582,817	12.29%	\$1.29	1,041	(31,180)	120,632	163,057
Sorrento Mesa	160	5,950,902	0	618,000	578,464	9.72%	802,851	13.49%	\$1.51	34,082	124,151	121,729	267,322
Sorrento Valley	102	2,353,949	0	0	219,208	9.31%	430,889	18.30%	\$1.70	(51,188)	(43,034)	42,309	89,856
Torrey Pines/UTC	71	5,906,074	782,394	620,600	732,793	12.41%	1,051,104	17.80%	\$2.44	33,943	334,604	53,754	400,947
<b>Central County Total</b>	<b>888</b>	<b>26,144,885</b>	<b>938,394</b>	<b>1,250,360</b>	<b>2,337,631</b>	<b>8.94%</b>	<b>3,674,742</b>	<b>14.06%</b>	<b>\$1.47</b>	<b>(4,964)</b>	<b>310,618</b>	<b>450,464</b>	<b>1,126,338</b>
<b>East County</b>													
El Cajon	77	851,324	0	0	1,670	0.20%	1,670	0.20%	\$0.00	14,666	16,719	16,266	32,255
La Mesa/Spring Valley	42	319,852	0	0	17,689	5.53%	17,689	5.53%	\$0.00	(1,264)	(6,264)	957	5,118
Santee/Lakeside	54	564,061	0	0	3,308	0.59%	13,524	2.40%	\$0.00	0	0	0	0
<b>East County Total</b>	<b>173</b>	<b>1,735,237</b>	<b>0</b>	<b>0</b>	<b>22,667</b>	<b>1.31%</b>	<b>32,883</b>	<b>1.90%</b>	<b>\$0.00</b>	<b>13,402</b>	<b>10,455</b>	<b>17,223</b>	<b>37,373</b>
<b>North County</b>													
Escondido	80	752,671	0	0	15,872	2.11%	14,129	1.88%	\$0.00	(628)	38,543	3,600	45,920
Oceanside	33	985,977	0	0	34,043	3.45%	44,549	4.52%	\$0.00	1,081	(16,099)	4,097	9,220
San Marcos	60	1,080,003	0	219,477	83,168	7.70%	127,633	11.82%	\$0.88	(9,390)	(4,465)	13,405	29,780
Vista	61	1,383,860	0	0	70,491	5.09%	115,203	8.32%	\$1.09	(2,668)	(7,932)	9,235	53,612
Carlsbad	250	6,166,315	171,098	146,108	590,362	9.57%	899,100	14.58%	\$1.37	(28,836)	31,605	67,818	293,220
North Beach Cities	18	155,333	0	0	915	0.59%	915	0.59%	\$0.00	0	(35)	0	1,480
Outlying SD County North	18	139,412	0	0	500	0.36%	2,550	1.83%	\$0.00	0	1,296	0	1,296
<b>North County Total</b>	<b>520</b>	<b>10,663,571</b>	<b>171,098</b>	<b>365,585</b>	<b>795,351</b>	<b>7.46%</b>	<b>1,204,079</b>	<b>11.29%</b>	<b>\$1.32</b>	<b>(40,441)</b>	<b>42,913</b>	<b>98,155</b>	<b>434,528</b>
<b>I-15 Corridor</b>													
Poway	61	1,522,333	0	0	55,099	3.62%	77,636	5.10%	\$1.17	41,274	62,719	88,304	130,469
Rancho Bernardo	93	4,570,959	0	0	362,562	7.93%	578,826	12.66%	\$1.40	211,994	28,759	406,359	472,017
Scripps Ranch	27	713,377	0	233,741	10,214	1.43%	35,836	5.02%	\$1.40	4,000	11,794	4,000	22,008
<b>I-15 Corridor Total</b>	<b>181</b>	<b>6,806,669</b>	<b>0</b>	<b>233,741</b>	<b>427,875</b>	<b>6.29%</b>	<b>692,298</b>	<b>10.17%</b>	<b>\$1.39</b>	<b>257,268</b>	<b>103,272</b>	<b>498,663</b>	<b>624,494</b>
<b>South Bay</b>													
Chula Vista	83	1,504,445	0	0	80,667	5.36%	83,598	5.56%	\$1.30	(16,312)	(16,457)	5,617	26,683
National City	23	303,615	0	0	10,888	3.59%	15,781	5.20%	\$0.00	(6,163)	(1,963)	925	5,125
Otay Mesa	9	215,354	0	256,022	37,594	17.46%	141,443	65.68%	\$0.65	47,313	47,313	47,313	47,313
San Ysidro/Imperial Beach	4	81,972	0	0	960	1.17%	55,960	68.27%	\$0.00	(960)	(960)	0	0
Outlying SD County South	20	78,080	0	0	0	0.00%	0	0.00%	\$0.00	1,600	0	1,600	1,600
<b>South Bay Total</b>	<b>139</b>	<b>2,183,466</b>	<b>0</b>	<b>256,022</b>	<b>130,109</b>	<b>5.96%</b>	<b>296,782</b>	<b>13.59%</b>	<b>\$0.72</b>	<b>25,478</b>	<b>27,933</b>	<b>55,455</b>	<b>80,721</b>
<b>San Diego County Total</b>	<b>1,901</b>	<b>47,533,828</b>	<b>1,109,492</b>	<b>2,105,708</b>	<b>3,713,633</b>	<b>7.81%</b>	<b>5,900,784</b>	<b>12.41%</b>	<b>\$1.33</b>	<b>250,743</b>	<b>495,191</b>	<b>1,119,960</b>	<b>2,303,454</b>

Lease rates are on a triple-net basis.



by **Greg Marx**  
ASSOCIATE, SAN DIEGO

Building values continue to reach record levels, vacancy rates remain extremely low, and rents continue to increase across San Diego County. To recap, in the first quarter of 2017, we saw a bit of a pause in the market. Transaction volume had slowed, net absorption had declined, and the country was holding their breath in the aftermath of the 2016 Presidential Election. Since the end of the first quarter, we've seen a slight resurgence, and while the level of growth is nothing compared with what we saw in 2015 and early 2016, the market is continuing to strengthen.

Total Net Absorption in square footage across San Diego County was solidly in the black for the second quarter after a significant posting of negative net absorption in the first quarter. This "bounce back" of positive absorption can be partly attributed to an increase in total transaction volume; approximately 270 deals were done in the second quarter compared with 230 deals done in the first quarter. The market remains relatively tight as a whole. The average occupancy across San Diego County increased minimally to 95.7%, which could be due to the increase in total deals done and the lack of newly developed space brought to market during the second quarter.

Similar to the first quarter, there are a number of "spec" buildings currently under construction in San Diego County. A total of 7 buildings are currently under construction encompassing a total of 536,283 square feet. As the market remains as tight as ever, developers are counting on the continuously vigorous and pent-up tenant demand for space. Carlsbad has been at the core of the industrial development, with more than three quarter million square feet of industrial and R&D space delivered since the start of the recovery, and more than half a million square feet currently under construction.

The combination of a lack of available space, high occupancy rates, and limited new building deliveries has driven average lease rates to a high of \$0.85 per square foot on a NNN basis, which is a 1.2% increase since last quarter when the average rent was \$0.84 per square foot. The market remains a "Landlord's Market" as we continue to see rents rise to record levels with a reduction of concessions and downtime.

With very little land inventory on which to build, onerous mitigation requirements, draconian storm water regulations, increasing construction costs and fees, and a general shortage of construction labor, there is a very limited amount of new product being built to meet the growing industrial tenants' demand. We anticipate that 2017 will continue to experience upward pressure on rents, with concessions such as free rent and tenant improvement packages all but disappearing as the occupancy levels approach historical highs. San Diego's diverse employment base, its wonderful climate, and its proximity to Mexico and the Pacific Rim all help support our local economy's continued growth, with only a lack of existing and new industrial inventory standing in the way.

## Please Contact Us for Further Information

**Josh Brant**  
Regional Director of Research  
jbrant@voitco.com

Anaheim, CA  
714.978.7880

Carlsbad, CA  
760.517.4000

Inland Empire, CA  
909.545.8000

Irvine, CA  
949.851.5100

Los Angeles, CA  
424.329.7500

San Diego, CA  
858.453.0505

This survey consists of properties representing both single tenant and multi-tenant buildings. The lease rates are based on a triple-net basis. The information contained in this report is gathered from sources that are deemed reliable, but no guarantees are made as to its accuracy. This information is for Voit Real Estate Services' use only and cannot legally be reproduced without prior written consent from the management of Voit Real Estate Services. ©2017 Voit Real Estate Services, Inc. License #01991785.

Represented in 150 Markets  
Nationally & Internationally.  
**CORFAC**  
International

## Product Type

**MFG./DIST.:** Flex/Research and Development (R&D) buildings can be one story, one story with a mezzanine, and two story built-out structures with a high ratio of window wall to floor area with lower ceilings. They generally have over 50% built-out office space or laboratory use, with the remaining space being utilized as light manufacturing or warehousing. In addition, the parking ratio must be at least 3 spaces or greater per 1,000 square feet.

## Submarkets

### CENTRAL COUNTY

Central City, East City, Southeast City, Kearny Mesa, Mission Gorge, Rose Canyon/Morena, Sports Arena/Airport, Miramar, Sorrento Mesa, Sorrento Valley, Torrey Pines/UTC

### EAST COUNTY

El Cajon, La Mesa/Spring Valley, Santee/Lakeside

### NORTH COUNTY

Escondido, Oceanside, San Marcos, Vista, Carlsbad, North Beach Cities, Outlying SD County North

### I-15 CORRIDOR

Poway, Rancho Bernardo, Scripps Ranch

### SOUTH BAY

Chula Vista, National City, Otay Mesa, San Ysidro/Imperial Beach, Outlying SD County South