

SD RETAIL DOING FINE. In the face of a changing retail landscape, the San Diego retail market has maintained solid fundamentals with availability at 4.98%, and the vacancy rate is still near a ten-year low. In spite of the rise of e-commerce, the San Diego retail real estate market remains robust with tight supply and high average asking rents.

VACANCY. Direct/sublease space (unoccupied) finished the fourth quarter at 3.83%, a slight increase from 2017's year-end vacancy rate of 3.57%, but at the exact same level as the fourth quarter of 2016, and it is still well below the ten-year average of 4.69% vacancy rate.

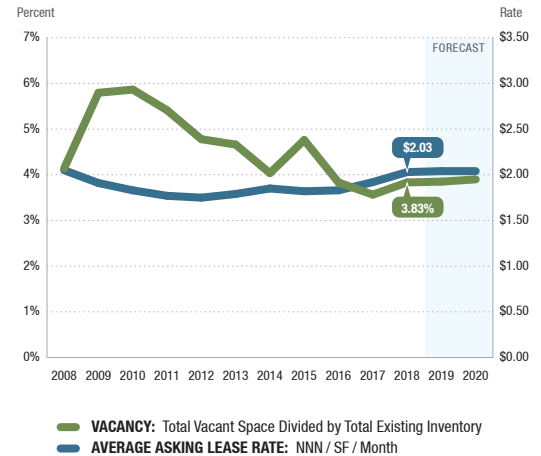
LEASE RATES. The average asking triple-net lease rate per month per square foot in San Diego County was \$2.03, an increase of eleven cents, or 5.73%, over the \$1.92 rate of the fourth quarter of 2017. The highest average asking rate in the market was in the I-15 Corridor, posting \$2.97 per square foot per month, on a triple-net basis.

TRANSACTION ACTIVITY. The combined amount of retail property sold or leased during the fourth quarter was approximately 2.8 million square feet, which was an increase from the 1.7 million square feet transacted in the prior quarter. The 4.3 million square feet sold in 2018 is an increase over the previous year's total of 3.7 million square feet, but below the five year average of 5.2 million square feet. The 3.3 million square feet of leasing volume in 2018 was the lowest level since 2009. The transaction activity 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.

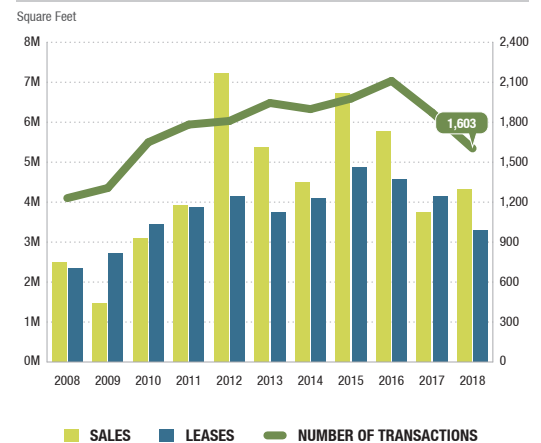
EMPLOYMENT. The unemployment rate in San Diego County was 3.2% in November 2018, down from a revised 3.3% in October 2018, and below the year-ago estimate of 3.5%. This compares with an unadjusted unemployment rate of 3.9% for California and 3.5% for the nation during the same period. According to the State of California Employment Development Department, San Diego County gained 26,400 payroll jobs between November 2017 and November 2018, including 16,500 from professional and business services, which reported the largest overall gain. The manufacturing sector reported a growth of 6,000 jobs the second most among the major employment sectors. The largest year-over-year loss was in trade, transportation, and utilities which reported 3,400 fewer jobs than the prior year.

OVERALL. The San Diego retail market continues to remain on solid footing. The construction pipeline is nearly empty at the moment, and changes in the market such as the planned conversion of Horton Plaza to an office campus keep things tight on the supply side of the equation. While 2018 did see a small amount of negative net absorption, and a decrease in occupancy rate from the previous year, the availability rate remains flat year-over-year. Additionally rental rates continue to rise, demonstrating the stability of the market.

VACANCY vs. AVERAGE ASKING LEASE RATE



TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



Market Statistics

	Change Over Last Quarter	4Q 2018	3Q 2018	4Q 2017	% Change Over Last Year
Vacancy Rate	■ FLAT	3.83%	3.84%	3.57%	7.50%
Availability Rate	▼ DOWN	4.98%	5.12%	4.95%	0.52%
Average Asking Lease Rate	■ FLAT	\$2.03	\$2.03	\$1.92	5.73%
Sale & Lease Transactions	▲ UP	2,823,014	1,749,210	1,533,385	84.10%
Gross Absorption	■ FLAT	1,032,610	1,205,568	1,662,866	(37.90%)
Net Absorption	▲ POSITIVE	62,546	20,891	466,096	N/A

CONSTRUCTION. The completion of the renovation and expansion of Westfield’s UTC Mall closed the books on the driving force behind the majority of the recent construction volume. The market has slowed down, and with only 390,000 square feet under construction, the pipeline of new product looks to be minimal for the near future.

EMPLOYMENT. The labor market in San Diego County will continue to improve, although we anticipate job growth to slow. In 2017 there was a 1.2% increase in total employment, and a 1.0–1.2% increase is projected for 2018. With the local stalwarts of defense and biotech remaining strong, look for these sectors to lead the way for employment gains, followed by healthcare.

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

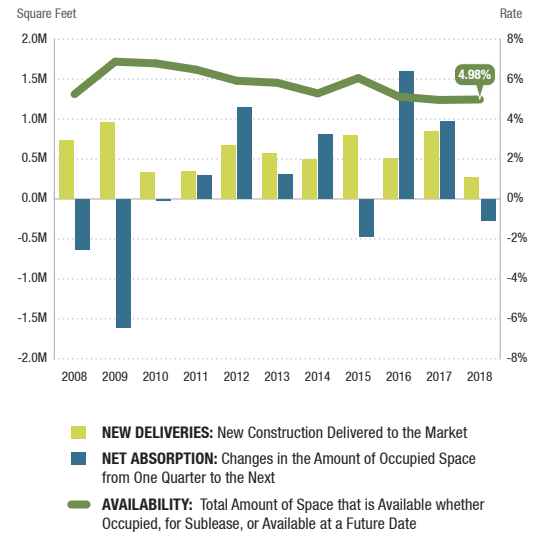
VACANCY. We anticipate the vacancy rate to remain stable and low, with much of the occupancy gains already captured. Availability has remained steady over the past four quarters, and with no buildup in availability, and minimal construction under way, we do not anticipate significant increases in vacancy.

CONSTRUCTION. Following the 967,992 square feet of new retail projects completed in 2017 (the highest annual total since 2009), there were only 275,103 square feet of new construction deliveries in 2018, which is the lowest level in a decade.

AVAILABILITY. Direct/sublease space being marketed was 4.98% at the end of the fourth quarter. This was a slight decrease from the third quarter’s availability rate of 5.12%. The Central South area of the county posted the lowest availability rate in the county, at 3.93%.

ABSORPTION. The San Diego retail market saw a modest 62,546 square feet of positive net absorption in the fourth quarter, but was solidly in the red for the year, with a final tally of 268,738 square feet of negative net absorption in 2018. This was just the second year of negative net absorption since the end of the last recession.

NEW DELIVERIES & NET ABSORPTION vs. AVAILABILITY RATE



Significant Transactions

Sales

Property Address	Submarket	Square Feet	Sale Price	Buyer	Seller
Liberty Station (Leasehold)	Point Loma	321,208	\$158,980,000	Seligman Western	The Corky McMillin Companies
110–194 N. El Camino Real	Encinitas	124,411	\$43,000,000	Encinitas Marketplace, LLC	Kimco Realty Corporation
16351–16495 Bernardo Center Dr.	Rancho Bernardo	27,511	\$9,000,000	Pacifica Companies	Equity Real Estate Services
1306 Broadway	El Cajon	14,490	\$6,600,000	St Paul’s Episcopal Home	1665 White Bear, Inc.
110 Fletcher Pkwy.	El Cajon	7,600	\$6,143,000	4860 Hazeltine Avenue, LLC	Brixton Fletcher, LLC

Leases

Property Address	Square Feet	Square Feet	Transaction Date	Tenant	Owner
8181 Mira Mesa Blvd.	Mira Mesa	48,000	Oct-2018	Undisclosed	Mesa Centers
935 Sweetwater Rd.	Spring Valley	48,000	Dec-2018	Target	Jamacha Sweetwater, LLC
2880 Roosevelt Rd.	Point Loma	41,000	Nov-2018	Undisclosed	NTC Foundation
8120 Mira Mesa Blvd.	Mira Mesa	21,300	Dec-2018	Michaels	Brixmor Property Group
13439 Camino Canada	El Cajon	16,203	Nov-2018	Dollar Tree	Spirit Realty Capital

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 4Q2018	Square Feet Available	Availability Rate 4Q2018	Average Asking Lease Rate	Net Absorption 4Q2018	Net Absorption 2018	Gross Absorption 4Q2018	Gross Absorption 2018
Central South													
General Retail	3,703	19,878,096	2,640	929,725	507,551	2.55%	739,156	3.72%	\$2.39	91,741	14,161	212,299	690,963
Malls	42	4,696,527	0	0	199,380	4.25%	158,380	3.37%	–	0	(5,724)	0	1,608
Power Centers	98	3,570,236	0	6,000	56,321	1.58%	58,657	1.64%	\$3.85	1,066	(1,244)	25,073	34,198
Shopping Centers	729	11,154,560	0	34,635	375,859	3.37%	580,824	5.21%	\$2.09	59,771	68,772	147,319	449,247
Specialty Centers	7	294,915	0	0	18,609	6.31%	18,609	6.31%	\$5.83	0	2,179	0	8,934
Central South Total	4,579	39,594,334	2,640	970,360	1,157,720	2.92%	1,555,626	3.93%	\$2.29	152,578	78,144	384,691	1,184,950
East County													
General Retail	1,454	7,374,870	0	51,970	178,715	2.42%	262,295	3.56%	\$1.43	(8,880)	(30,063)	44,903	163,791
Malls	14	2,816,104	0	0	48,258	1.71%	85,002	3.02%	–	(41,085)	(45,763)	0	9,965
Power Centers	60	1,702,163	0	4,800	22,203	1.30%	33,044	1.94%	–	3,161	(4,953)	4,361	15,641
Shopping Centers	563	8,295,410	15,834	246,731	471,124	5.68%	463,071	5.58%	\$1.71	(97,656)	(82,331)	70,206	333,315
Specialty Centers	2	34,558	0	0	0	0.00%	0	0.00%	–	0	0	0	0
East County Total	2,093	20,223,105	15,834	303,501	720,300	3.56%	843,412	4.17%	\$1.63	(144,460)	(163,110)	119,470	522,712
I-15 Corridor													
General Retail	172	1,648,380	0	62,925	17,759	1.08%	53,020	3.22%	\$2.63	(5,383)	(6,201)	6,276	16,534
Malls	0	0	0	0	0	0.00%	0	0.00%	–	0	0	0	0
Power Centers	24	566,418	0	0	4,914	0.87%	112,173	19.80%	–	0	0	0	0
Shopping Centers	288	4,287,899	0	233,138	181,340	4.23%	206,765	4.82%	\$3.01	(7,862)	34,749	27,425	131,601
Specialty Centers	0	0	0	0	0	0.00%	0	0.00%	–	0	0	0	0
I-15 Corridor Total	484	6,502,697	0	296,063	204,013	3.14%	371,958	5.72%	\$2.97	(13,245)	28,548	33,701	148,135
North County													
General Retail	1,691	11,439,889	78,696	501,155	471,715	4.12%	555,429	4.86%	\$2.13	52,496	(146,185)	100,706	262,979
Malls	24	3,176,626	0	50,340	13,303	0.42%	10,973	0.35%	–	(4,601)	(6,385)	2,330	4,392
Power Centers	109	3,101,378	0	18,312	107,064	3.45%	125,107	4.03%	–	(12,255)	(9,857)	11,965	109,111
Shopping Centers	964	15,148,957	132,094	358,511	988,735	6.53%	1,147,472	7.57%	\$1.59	(8,701)	77,911	106,957	693,386
Specialty Centers	5	363,588	0	0	1,210	0.33%	1,210	0.33%	–	0	(1,210)	0	1,710
North County Total	2,793	33,230,438	210,790	928,318	1,582,027	4.76%	1,840,191	5.54%	\$1.72	26,939	(85,726)	221,958	1,071,578
Central North													
General Retail	869	7,096,865	11,409	85,308	250,483	3.53%	276,683	3.90%	\$3.23	43,393	(46,539)	92,092	256,531
Malls	21	1,454,387	0	40,000	331,711	22.81%	331,711	22.81%	–	(4,367)	(149,211)	0	0
Power Centers	66	2,094,287	21,300	101,235	13,529	0.65%	39,877	1.90%	–	2,675	103,791	6,163	128,580
Shopping Centers	422	6,567,197	11,849	442,529	285,366	4.35%	347,337	5.29%	\$2.71	(2,932)	(85,663)	50,388	211,164
Specialty Centers	9	232,667	0	0	67,054	28.82%	70,054	30.11%	\$1.75	(4,900)	(18,974)	0	4,104
Central North Total	1,387	17,445,403	44,558	669,072	948,143	5.43%	1,065,662	6.11%	\$2.84	33,869	(196,596)	148,643	600,379
South County													
General Retail	1,116	5,874,893	12,377	427,757	126,451	2.15%	208,363	3.55%	\$1.80	19,640	3,806	31,821	170,206
Malls	42	2,746,513	0	0	3,591	0.13%	119,318	4.34%	–	0	21,860	0	30,684
Power Centers	27	1,025,479	0	79,900	7,400	0.72%	24,714	2.41%	–	4,575	0	4,575	11,975
Shopping Centers	537	9,181,948	104,493	159,357	536,445	5.84%	781,190	8.51%	\$2.01	(47,227)	25,376	46,041	317,982
Specialty Centers	26	780,784	0	0	4,357	0.56%	15,946	2.04%	\$3.02	17,598	(1,167)	18,545	21,735
South County Total	1,748	19,609,617	116,870	667,014	678,244	3.46%	1,149,531	5.86%	\$1.99	(5,414)	49,875	100,982	552,582
Outlying Areas													
General Retail	515	2,067,915	0	13,248	50,079	2.42%	82,840	4.01%	\$1.82	2,755	(4,265)	12,589	36,090
Malls	11	145,890	0	0	3,930	2.69%	3,930	2.69%	–	7,070	7,070	7,070	7,070
Power Centers	0	0	0	0	0	0.00%	0	0.00%	–	0	0	0	0
Shopping Centers	92	1,273,377	0	12,766	35,268	2.77%	76,306	5.99%	\$1.71	2,454	17,322	3,506	47,409
Specialty Centers	1	255,000	0	0	0	0.00%	0	0.00%	–	0	0	0	0
Outlying Areas Total	619	3,742,182	0	26,014	89,277	2.39%	163,076	4.36%	\$1.76	12,279	20,127	23,165	90,569
San Diego Total	13,703	140,347,776	390,692	3,860,342	5,379,724	3.83%	6,989,456	4.98%	\$2.03	62,546	(268,738)	1,032,610	4,170,905
General Retail	9,520	55,380,908	105,122	2,072,088	1,602,753	2.89%	2,177,786	3.93%	\$2.21	195,762	(215,286)	500,686	1,597,094
Malls	154	15,036,047	0	90,340	600,173	3.99%	709,314	4.72%	\$2.53	(42,983)	(178,153)	9,400	53,719
Power Centers	384	12,059,961	21,300	210,247	211,431	1.75%	393,572	3.26%	\$3.85	(778)	87,737	52,137	299,505
Shopping Centers	3,595	55,909,348	264,270	1,487,667	2,874,137	5.14%	3,602,965	6.44%	\$1.91	(102,153)	56,136	451,842	2,184,104
Specialty Centers	50	1,961,512	0	0	91,230	4.65%	105,819	5.39%	\$2.34	12,698	(19,172)	18,545	36,483
San Diego Total	13,703	140,347,776	390,692	3,860,342	5,379,724	3.83%	6,989,456	4.98%	\$2.03	62,546	(268,738)	1,032,610	4,170,905

Lease rates are on a triple-net basis.



The Sun Shines in San Diego

by **Mark Caston**

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The San Diego Retail market ended 2018 with a strong finish.

The fourth quarter vacancy rate overall was 3.83%, with some specific retail product types and areas dipping below 3%. In the fourth quarter, we experienced negotiations for new leases before the space or site was even vacated.

Retail lease rates and vacancy rates remained flat in comparison with the third quarter, which was a very good quarter. However, rental rates are a bit deceiving. Operating expenses (NNN's) have been increasing overall. This trend will put pressure on base rent increases moving forward in 2019. Landlords must manage these expense increases, as tenants will be comparing aggregate rent.

Employment in San Diego County is still very strong. Low unemployment, increasing wages and new employers moving into San Diego County will continue to drive positive results in the San Diego retail market.

Two additional factors influencing the local retail market are the lack of new retail development and the change of use of existing retail properties. For example, there are several sites in San Diego County currently being converted to medical uses and most notably, the planned conversion of the 900,000 square foot Horton Plaza mall into an office campus use is underway. These changes will further increase demand and lower vacancy rates.

Investment in San Diego retail product continues to be strong. There remains very little supply and cap rates remain low. There were about 363 sale transactions in 2018 versus 394 sales in 2017. Increasing interest rates are starting to affect buyer valuations. However, seller expectations have not moved much. Going forward into 2019, look for lower transaction volume.

We believe the San Diego retail market to be highly stabilized and very insulated.

The sun continues to shine on the San Diego retail market.

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Submarkets

CENTRAL SOUTH

Central San Diego, Clairemont, Coronado, Downtown, Mission Gorge, Mid City/Southeast San Diego, Mission Valley, Pacific Beach/Morena, Point Loma/Sports Arena

EAST COUNTY

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

I-15 CORRIDOR

Carmel Mountain Ranch, Poway, Rancho Bernardo, Rancho Penasquitos

CENTRAL NORTH

Cardiff/Encinitas, Del Mar Heights, La Jolla/Torrey Pines, Miramar, UTC

NORTH COUNTY

Carlsbad, Escondido, Oceanside, San Marcos, Vista

OUTLYING AREAS

Outlying SD County North, Outlying SD County South

SOUTH COUNTY

Chula Vista, Eastlake, Imperial Beach/South San Diego, National City