

## MARKET CHANGE

*Compared to Previous Quarter:*

**Vacancy**

**DOWN**

**Net Absorption**

**POSITIVE**

**Lease Rates**

**DOWN**

**Transactions**

**DOWN**

**Deliveries**

**DOWN**

## HIGHLIGHTS

- **Steady Growth** - The San Diego office market had a solid start to the year, posting positive net absorption and strong transaction volume. Although the market saw rental rates decrease slightly, vacancy and availability rates also continue to decrease. New deliveries are coming off of their best annual total of the past three years and demand remains strong.
- **Construction** - Office deliveries have averaged 750,000 square feet a year over the past five years. In the first quarter of 2016, approximately 72,766 square feet of new product was delivered. This rate of construction is below the historical average and has helped to keep vacancy at its current level. In addition to the new construction, there has been a significant trend towards property being extensively renovated or outright converted to office use, e.g., the 230,000 square foot Atlas project in Carlsbad, currently being converted from industrial to office, estimated to complete July 2016.
- **Vacancy** - Direct/sublease space (unoccupied) finished the quarter at 11.69%, a 46 basis point decrease from the previous quarter, and a 29 basis point decrease from first quarter 2015. Rancho Bernardo posted the lowest vacancy rate of any submarket (minimum of five million square feet of inventory) at 8.07%.
- **Availability** - Direct/sublease space being marketed was 14.92% at the end of the quarter, a decrease from the 15.26% availability rate of the previous quarter.
- **Lease Rates** - The average asking full-service gross (FSG) lease rate per square foot per month in San Diego County was \$2.64 at the end of the quarter, down from last quarter's record high rate of \$2.81 but still a solid twenty one-cent increase over 2015's first quarter rate of \$2.43. In the third quarter of 2015, The Irvine Company's 300,000 square foot One La Jolla Center in UTC came online and their asking rates are in the \$4.35-\$4.55 range.
- **Absorption** - The San Diego office market posted 532,307 square feet of positive net absorption in the first quarter,

giving the market a total of 7.7 million square feet of positive absorption since 2010. Class B office contributed the highest positive net absorption with 287,430 square feet absorbed in the first quarter, while Class A and Class C both had positive net absorption of 213,172 and 31,705 square feet, respectively.

- **Transaction Activity** - Sale and lease transactions totaled 4.7 million square feet in the first quarter, a decrease from the previous quarter's 5.2 million square feet. This statistic can have some lag time in being reported, so look for figures to end up somewhat higher in the next report. Details of the largest transactions can be found on the back page of this report.
- **Employment** - The unemployment rate in San Diego County was 4.7% in February 2016, unchanged from a revised 4.7% in January 2016 and below the year-ago estimate of 5.5%. This compares with an unadjusted unemployment rate of 5.7% for California and 5.2% for the nation during the same period. According to the State of California Employment Development Department, San Diego County gained 39,100 payroll jobs from February 2015 and February 2016, including 8,500 from education and health services, which reported the largest overall gain. Leisure and hospitality reported a growth of up to 7,000 jobs, followed by professional and business services that reported up to 6,400 jobs.
- **Overall** - Construction levels of new office product are still lower than 2005-2008, but the San Diego office market has now recorded four consecutive year-over-year increases in office square feet delivered. The office market is steady but not explosive, and Class A office product has fared the best through this recovery thus far. Unemployment rates have continued to trend downward since the peak in January 2010. An increase in jobs and less building have set the San Diego office market on firmer footing, and accelerating growth in office-dependent sectors will help continue to further improve the office market.

## FORECAST

- **Construction** - The recovery of the San Diego office market has now matured to the point that we have multiple speculative office developments under construction. Local office development looks to remain lower than the levels seen during 2005-2008.
- **Employment** - We anticipate job growth of around 2.5%, or 35,000 jobs, in San Diego County over the year. Look for sectors like professional, scientific, & technical services, health care & social services, and leisure & hospitality to lead the way for employment gains in 2016.
- **Lease Rates** - Expect the average asking lease rate to increase by 3% to 4% percent over the next four quarters.
- **Vacancy** - We anticipate vacancy to descend at a moderate pace in coming quarters, dropping to approximately 11.35%, by the end of the fourth quarter of 2016.

## OVERVIEW

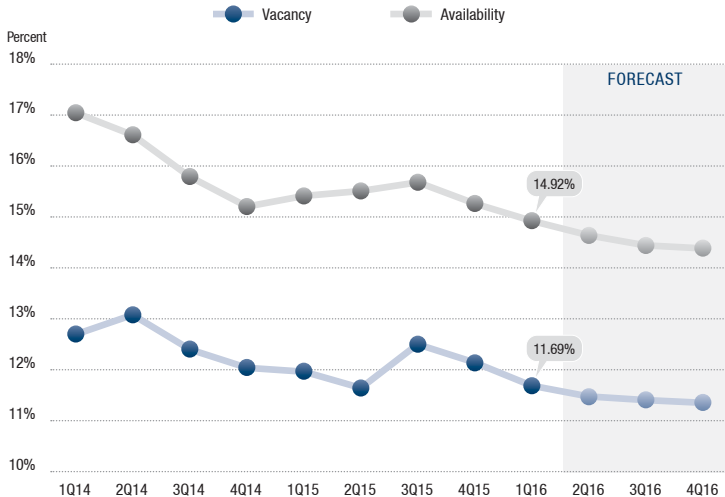
	1Q16	4Q15	1Q15	% of Change vs. 1Q15
Total Vacancy Rate	11.69%	12.15%	11.98%	(2.42%)
Availability Rate	14.92%	15.26%	15.66%	(4.73%)
Average Asking Lease Rate	\$2.64	\$2.81	\$2.43	8.64%
Sale & Lease Transactions	4,749,239	5,159,734	3,944,879	20.39%
Gross Absorption	1,887,313	2,025,103	1,986,392	(4.99%)
Net Absorption	532,307	446,565	192,247	N/A

*To view available properties or electronic versions of current or past market reports, please visit:*

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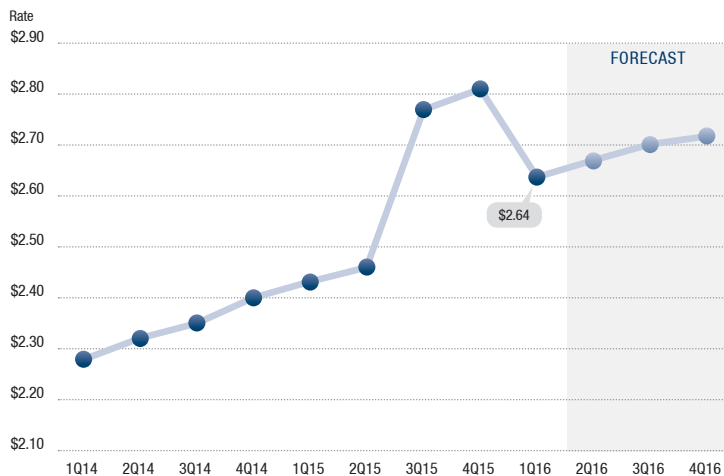
VACANCY & AVAILABILITY RATE

VACANCY – UNOCCUPIED SPACE | AVAILABILITY – ALL SPACE BEING MARKETED



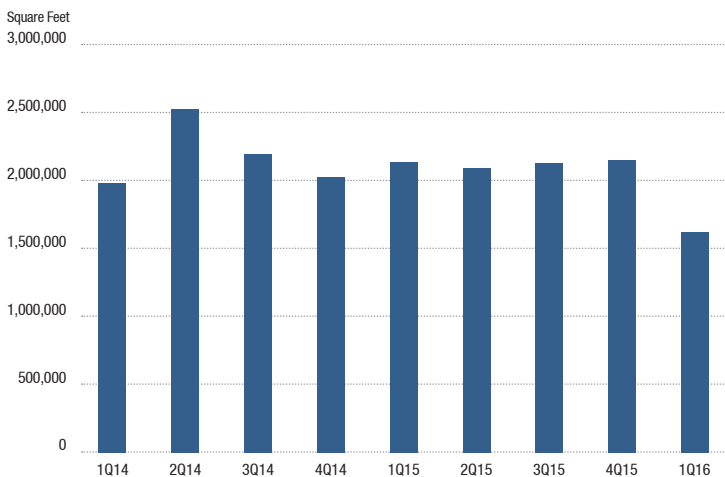
AVERAGE ASKING FULL-SERVICE LEASE RATE

MONTHLY OCCUPANCY COST ON A PER SQ. FT. BASIS



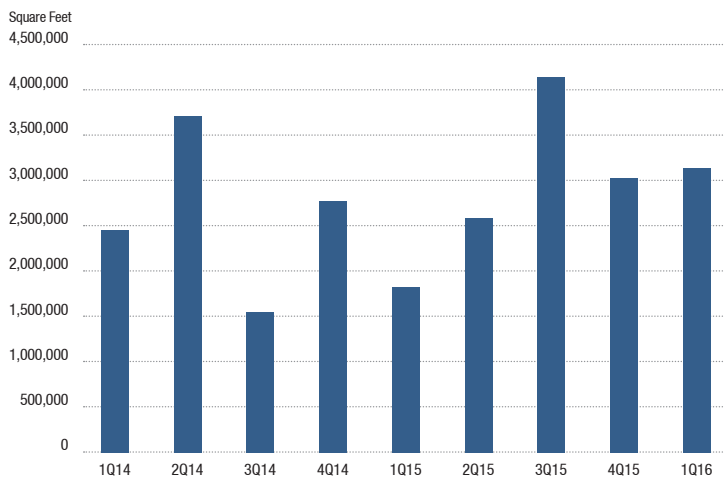
LEASE TRANSACTIONS

TOTAL AMOUNT OF SPACE THAT LEASED IN A QUARTER



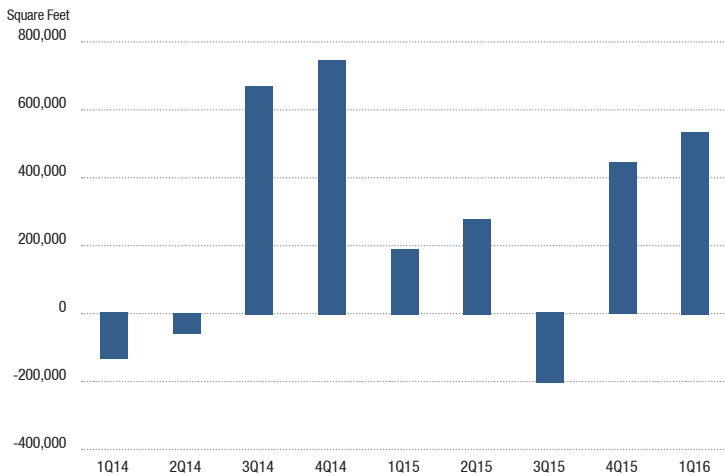
SALES TRANSACTIONS

TOTAL AMOUNT OF SPACE THAT SOLD IN A QUARTER



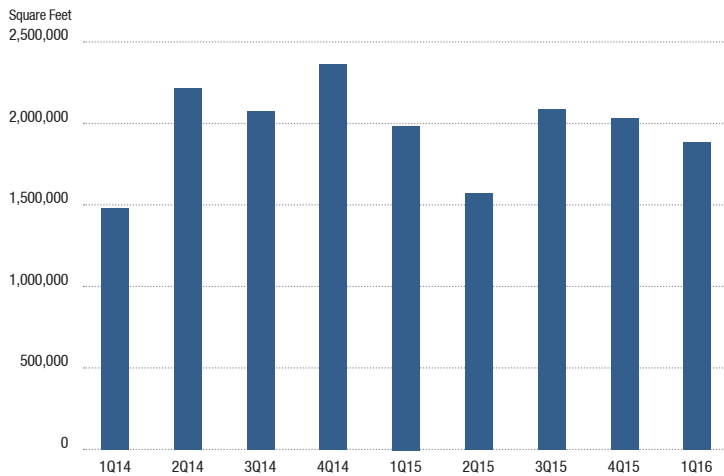
NET ABSORPTION

CHANGE IN THE AMOUNT OF OCCUPIED SPACE FROM ONE QUARTER TO THE NEXT



GROSS ABSORPTION

TOTAL AMOUNT OF SPACE THAT BECAME OCCUPIED IN A QUARTER



	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 1Q2016	Square Feet Available	Availability Rate 1Q2016	Average Asking Lease Rate	Net Absorption 1Q2016	Net Absorption 2015	Gross Absorption 1Q2016	Gross Absorption 2015
<b>Downtown</b>													
Downtown	136	13,037,308	0	2,724,744	2,055,798	15.77%	2,522,540	19.35%	\$2.46	50,162	60,677	208,616	1,127,459
Downtown Total	136	13,037,308	0	2,724,744	2,055,798	15.77%	2,522,540	19.35%	\$2.46	50,162	60,677	208,616	1,127,459
<b>Central</b>													
City Heights / University	29	1,058,511	0	0	59,418	5.61%	61,180	5.78%	\$0.00	(6,634)	39,080	1,656	54,852
Coronado	6	125,233	0	0	0	0.00%	11,254	8.99%	\$0.00	930	(930)	930	2,147
Kearny Mesa	238	10,592,278	0	297,000	1,145,111	10.81%	1,250,010	11.80%	\$2.03	85,270	(96,980)	190,758	564,970
Mission Gorge	26	592,926	0	0	39,023	6.58%	42,341	7.14%	\$1.07	(11,904)	11,607	826	27,309
Mission Valley	125	6,975,211	0	0	648,185	9.29%	1,071,518	15.36%	\$2.34	(21,946)	71,997	100,536	782,369
Old Town / Point Loma	68	2,199,276	0	0	168,951	7.68%	210,280	9.56%	\$1.75	44,466	23,287	67,201	116,113
Park East	8	155,884	0	0	5,745	3.69%	5,745	3.69%	\$2.35	0	(20,707)	2,560	1,025
Rose Canyon / Morena	55	1,261,530	0	0	62,463	4.95%	72,248	5.73%	\$1.74	(10,079)	12,835	11,513	65,387
Uptown / Hillcrest	103	2,641,274	0	0	210,603	7.97%	210,595	7.97%	\$2.29	(5,737)	(26,590)	33,082	129,642
Central Total	658	25,602,123	0	297,000	2,339,499	9.14%	2,935,171	11.46%	\$2.11	74,366	13,599	409,062	1,743,814
<b>I-15 Corridor</b>													
Escondido	91	1,890,494	0	60,000	230,308	12.18%	255,751	13.53%	\$1.42	(795)	46,647	15,025	115,133
Poway	29	1,304,758	0	630,000	79,977	6.13%	86,810	6.65%	\$1.80	8,875	(3,732)	20,823	50,321
Rancho Bernardo	108	6,763,053	100,000	1,010,002	545,961	8.07%	887,797	13.13%	\$0.00	59,899	(34,048)	118,884	355,989
Scripps Ranch	50	2,676,246	0	903,000	304,355	11.37%	286,188	10.69%	\$2.35	15,570	141,964	57,392	210,344
I-15 Corridor Total	278	12,634,551	100,000	2,603,002	1,160,601	9.19%	1,516,546	12.00%	\$2.20	83,549	150,831	212,124	731,787
<b>North County Coastal</b>													
Carlsbad	153	6,090,660	232,609	345,112	1,050,939	17.25%	1,512,515	24.83%	\$2.17	32,160	13,670	126,499	616,851
Del Mar Heights / Carmel Valley	74	4,670,118	92,000	895,059	572,363	12.26%	1,004,289	21.50%	\$3.37	(2,185)	158,897	64,561	441,595
North Beach Cities	111	2,538,834	20,461	55,000	121,903	4.80%	210,712	8.30%	\$2.55	8,514	81,753	56,635	224,283
North County Total	338	13,299,612	345,070	1,295,171	1,745,205	13.12%	2,727,516	20.51%	\$2.62	38,489	254,320	247,695	1,282,729
<b>North City</b>													
Governor Park	19	860,055	0	0	150,009	17.44%	82,468	9.59%	\$2.95	(26,196)	(8,701)	13,495	104,028
La Jolla	53	1,616,486	14,750	0	142,415	8.81%	184,808	11.43%	\$4.12	15,409	66,604	33,323	178,563
Miramar	37	1,710,317	0	0	267,823	15.66%	421,097	24.62%	\$2.25	2,079	15,201	28,947	192,190
Sorrento Mesa	122	9,662,922	0	2,169,063	1,287,447	13.32%	1,495,184	15.47%	\$2.69	179,846	(412,606)	269,049	420,563
Sorrento Valley	27	785,003	0	0	73,191	9.32%	112,696	14.36%	\$1.50	39,875	33,066	50,202	109,735
Torrey Pines	42	2,683,753	0	0	183,323	6.83%	166,046	6.19%	\$4.05	(17,812)	(34,600)	4,553	220,694
UTC	86	8,507,572	64,832	436,119	1,389,027	16.33%	1,773,051	20.84%	\$3.62	(75,616)	347,824	103,148	940,226
North City Total	386	25,826,108	79,582	2,605,182	3,493,235	13.53%	4,235,350	16.40%	\$3.46	117,585	6,788	502,717	2,165,999
<b>Southern &amp; Eastern Areas</b>													
Chula Vista	89	2,786,978	0	765,002	286,558	10.28%	337,424	12.11%	\$1.98	27,131	15,707	61,727	87,846
East County	152	3,692,465	0	194,200	193,385	5.24%	239,323	6.48%	\$1.38	67,129	(38,397)	97,012	140,101
National City	15	531,473	0	0	17,338	3.26%	15,601	2.94%	\$0.00	102,722	(7,380)	104,194	3,746
Otay Mesa	12	285,999	0	0	17,649	6.17%	17,649	6.17%	\$1.30	8,617	(5,510)	8,617	1,154
Southeast San Diego	10	391,848	0	0	60,380	15.41%	64,652	16.50%	\$2.20	1,800	7,610	1,800	20,896
Southern & Eastern Areas Total	278	7,688,763	0	959,202	575,310	7.48%	674,649	8.77%	\$1.60	207,399	(27,970)	273,350	253,743
<b>Highway 78 Corridor</b>													
Oceanside	61	1,335,657	0	310,249	209,063	15.65%	230,763	17.28%	\$1.62	(20,543)	40,032	24,122	64,407
San Marcos	37	1,352,912	0	1,367,139	166,136	12.28%	185,524	13.71%	\$0.00	(5,497)	43,781	5,458	89,114
Vista	50	1,226,436	0	11,800	175,283	14.29%	188,427	15.36%	\$1.52	(13,203)	70,181	4,169	104,812
Highway 78 Corridor Total	148	3,915,005	0	1,689,188	550,482	14.06%	604,714	15.45%	\$1.54	(39,243)	153,994	33,749	258,333
Class A	271	34,747,530	112,461	9,429,450	3,803,105	10.94%	5,379,669	15.48%	\$3.14	213,172	507,149	680,732	2,587,530
Class B	1,223	51,334,722	412,191	2,744,039	6,877,398	13.40%	8,200,744	15.98%	\$2.13	287,430	(4,787)	999,721	4,156,762
Class C	728	15,921,218	0	0	1,239,627	7.79%	1,636,073	10.28%	\$1.62	31,705	109,877	206,860	819,572
<b>San Diego County Total</b>	<b>2,222</b>	<b>102,003,470</b>	<b>524,652</b>	<b>12,173,489</b>	<b>11,920,130</b>	<b>11.69%</b>	<b>15,216,486</b>	<b>14.92%</b>	<b>\$2.64</b>	<b>532,307</b>	<b>612,239</b>	<b>1,887,313</b>	<b>7,563,864</b>

This survey consists of buildings greater than 10,000 square feet. Lease rates are on a full-service gross basis.

MAJOR TRANSACTIONS

Sales Transactions

Property Address	Submarket	Class	Square Feet	Sale Price Per SF	Buyer	Seller
7525–7555 Torrey Santa Fe Rd. (4 Properties)	Rancho Bernardo	A	465,812	\$563	Intuit, Inc.	Kilroy Realty Corporation
525 B St.	Downtown	A	449,180	\$272	LaSalle Investment Management	Hines
530 B St.	Downtown	B	232,936	\$228	Bosa Development Corporation	Kearny Real Estate Company
5780–5790 Fleet St.	Carlsbad	A	121,380	\$357	Cape Ann Investment Properties, LLC	Washington Capital Management, Inc.
10089 Willow Creek Rd.	Scripps Ranch	B	113,933	\$173	Harbert Management Corporation & Cypress Office Properties	LBA Realty

Lease Transactions

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
6350 Sequence Dr.	Sorrento Mesa	B	132,600	Feb-2016	Dexcom, Inc.	(Sublease)
4655 Executive Dr.	UTC	A	62,625	Jan-2016	Jones Day	The Irvine Company
8911 Balboa Ave.	Kearny Mesa	B	46,707	Mar-2016	County of San Diego	TA Realty
10182 Telesis Ct.	Sorrento Mesa	A	42,773	Jan-2016	Omnitracs	(Sublease)
9210 Sky Park (Renewal/Expansion)	Kearny Mesa	B	26,754	Feb-2016	AMEC Earth & Environmental, Inc.	Ominet Capital

PRODUCT TYPE

**CLASS A**

Most prestigious buildings competing for premier office users with rents above average for the area. Buildings have high-quality standard finishes, state-of-the-art systems, exceptional accessibility and a definite market presence.

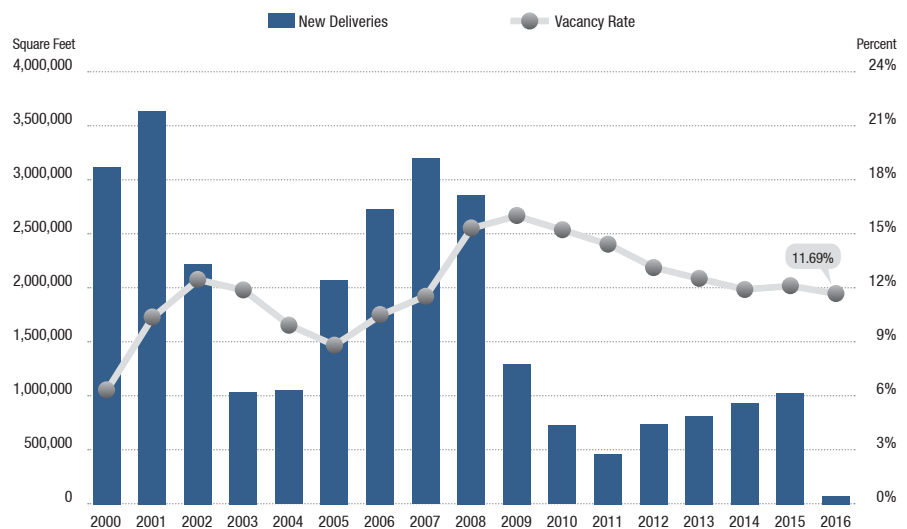
**CLASS B**

Buildings competing for a wide range of users with rents in the average range for the area. Building finishes are fair to good for the area, and systems are adequate. However, Class B buildings cannot compete with Class A buildings of the same price.

**CLASS C**

Buildings competing for tenants requiring functional space at rents below the area average.

ANNUAL NEW DELIVERIES VS. VACANCY RATE



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