

MARKET CHANGE

Compared to Previous Quarter:

Vacancy



UP

Net Absorption

NEGATIVE



Lease Rates



UP

Transactions



UP

Deliveries



UP

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Prepared by:

Jerry J. Holdner, Jr.
Vice President of Market Research
e-mail: jholdner@voitco.com

Joshua Brant
Market Research Analyst
e-mail: jbrant@voitco.com
VOIT Real Estate Services

HIGHLIGHTS

- **Maturing Recovery** - The San Diego office market saw rental rates increase significantly, along with new class A office product delivered in the third quarter. Vacancy rates ticked up slightly, but transaction volume was strong.
- **Construction** - Office deliveries have consistently been around 500,000-800,000 square feet a year over the past five years. This rate of construction is below the historical average and has helped to push vacancy down, and this year should fall within that range as well. In addition to the new construction, there has been a significant level of properties being extensively renovated or even converted to office use, such as the 230,000 square foot Atlas project in Carlsbad currently being converted from industrial to office.
- **Vacancy** - Direct/sublease space (unoccupied) finished the quarter at 12.12%, an increase the previous quarter, but close to the mark of the third quarter 2014. Mission Valley posted the lowest vacancy rate of any submarket with at least five million square feet of inventory at 9.54%.
- **Availability** - Direct/sublease space being marketed was 15.25% at the end of the quarter, an increase from the 15.02% 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 \$2.77 at the end of the second quarter, a new record high for the market. The renovated offices and new offices are really pushing the average asking rates. In the third quarter, Irvine Company's 300,000 square foot One La Jolla Center in UTC came online and their asking rates are in the \$4.25-\$4.65 range.
- **Absorption** - The San Diego office market posted 283,975 square feet of negative net absorption in the third quarter. Class B office was the only segment of the market posting negative net absorption for the quarter, while Class A and C office posted positive net absorption.
- **Transaction Activity** - Sale and lease transactions totaled 5.4 million square feet in the third quarter, an increase from the previous quarter's 4.2 million square feet, and the largest amount of square feet transacted in a quarter in the past three years. 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 5.1% in August 2015, down from a revised 5.4% in August 2015 and below the year-ago estimate of 6.6%. This compares with an unadjusted unemployment rate of 6.1% 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 42,400 payroll jobs from August 2014 and August 2015, including 11,500 from professional and business services, and 8,000 from education and health services, 5,600 from both transportation and utilities, and leisure and hospitality. Only two minor sectors recorded year-over job losses totaling 900 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 market's rental rates continue to rise and are now at an all time high. Rising rents may become a headwind to the rate of vacancy compression. 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. As job creation continues and consumer confidence stabilizes, the office market recovery will continue.

FORECAST

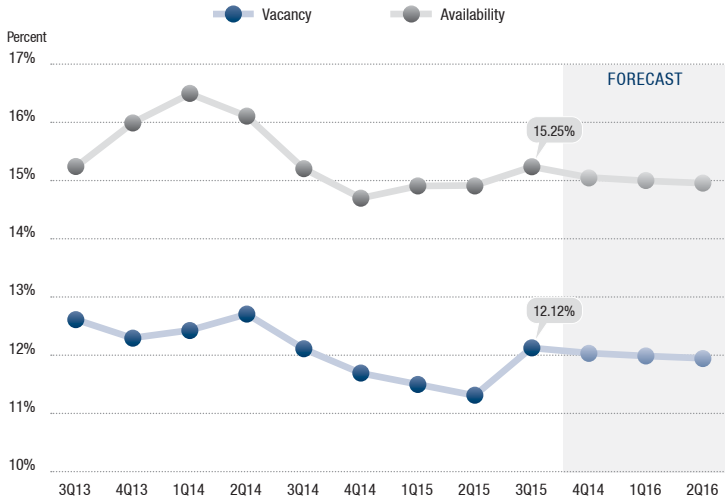
- **Construction** - The recovery of the San Diego office market has now matured to the point that we have multiple speculative office developments under construction. Local office development looks to remain lower than the levels seen during 2005-2008.
- **Employment** - We anticipate job growth of around 1.9%, or 24,600, jobs in San Diego County over the year. Look for sectors like construction, administrative & support, and transportation & utilities to lead the way for employment gains in 2015.
- **Lease Rates** - Expect the average asking lease rate to increase by 4% to 7% percent over the next four quarters.
- **Vacancy** - We anticipate vacancy to descend at a moderate pace in coming quarters, dropping to approximately 11.95%, by the end of the second quarter of 2016.

OVERVIEW

	3Q15	2Q15	3Q14	% of Change vs. 3Q14
Total Vacancy Rate	12.12%	11.26%	12.07%	0.41%
Availability Rate	15.25%	15.02%	15.44%	(1.23%)
Average Asking Lease Rate	\$2.77	\$2.46	\$2.35	17.87%
Sale & Lease Transactions	5,414,907	4,229,012	4,207,156	28.71%
Gross Absorption	1,982,232	1,566,757	2,074,528	(4.45%)
Net Absorption	(283,975)	386,563	670,239	N/A

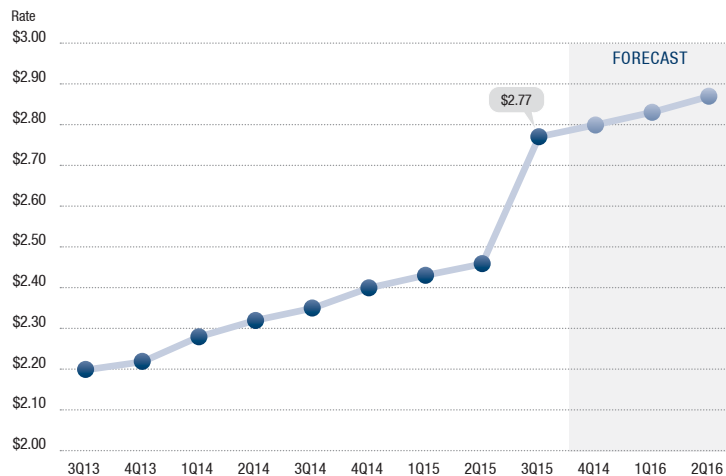
VACANCY & AVAILABILITY RATE

VACANCY – UNOCCUPIED SPACE | AVAILABILITY – ALL SPACE BEING MARKETED



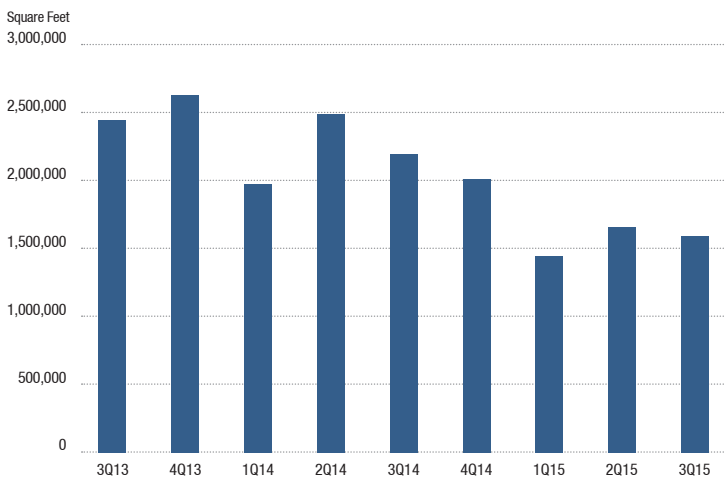
AVERAGE ASKING FULL-SERVICE LEASE RATE

MONTHLY OCCUPANCY COST ON A PER SQ. FT. BASIS



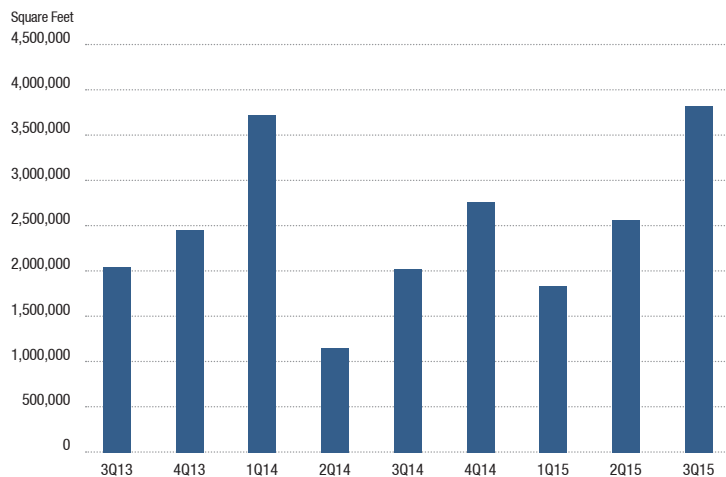
LEASE TRANSACTIONS

TOTAL AMOUNT OF SPACE THAT LEASED IN A QUARTER



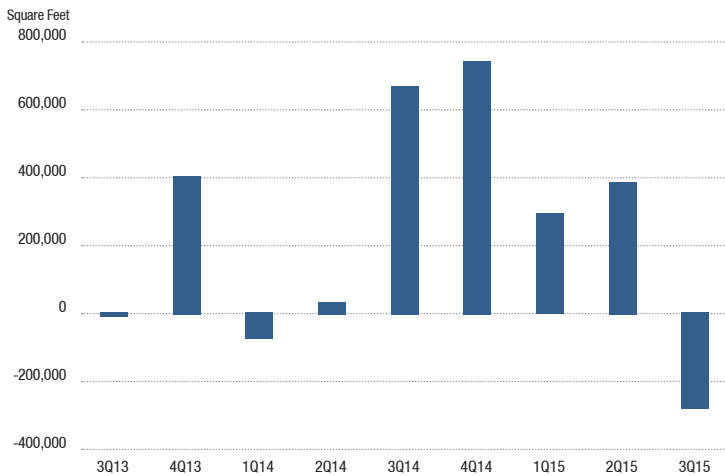
SALES TRANSACTIONS

TOTAL AMOUNT OF SPACE THAT SOLD IN A QUARTER



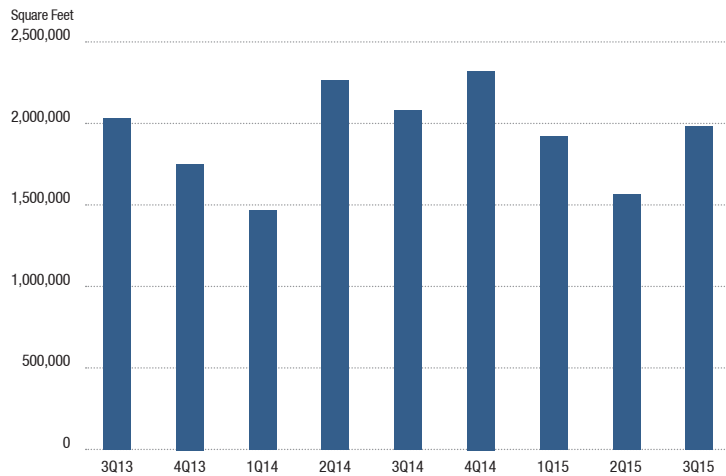
NET ABSORPTION

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 3Q2015	Square Feet Available	Availability Rate 3Q2015	Average Asking Lease Rate	Net Absorption 3Q2015	Net Absorption 2015	Gross Absorption 3Q2015	Gross Absorption 2015
Downtown													
Downtown	136	12,945,481	0	2,369,160	2,050,441	15.84%	2,615,125	20.20%	\$2.39	(37,364)	116,196	536,531	972,664
Downtown Total	136	12,945,481	0	2,369,160	2,050,441	15.84%	2,615,125	20.20%	\$2.39	(37,364)	116,196	536,531	972,664
Central													
City Heights / University	28	1,032,587	25,000	0	62,312	6.03%	74,182	7.18%	\$0.00	1,196	29,552	7,422	45,324
Coronado	6	125,233	0	0	1,091	0.87%	1,091	0.87%	\$0.00	0	(1,091)	0	1,986
Kearny Mesa	237	10,530,362	0	297,000	1,228,564	11.67%	1,376,955	13.08%	\$1.97	(96,639)	(179,546)	171,250	404,308
Mission Gorge	25	582,823	0	0	28,244	4.85%	32,069	5.50%	\$1.16	7,743	10,482	13,522	21,641
Mission Valley	125	6,975,211	0	90,000	665,237	9.54%	1,057,692	15.16%	\$2.37	(51,969)	28,676	257,997	565,195
Old Town / Point Loma	72	2,357,936	0	0	225,574	9.57%	194,211	8.24%	\$1.75	(2,400)	11,865	28,254	94,115
Park East	9	176,637	0	0	4,766	2.70%	4,766	2.70%	\$0.00	0	1,025	0	1,025
Rose Canyon / Morena	55	1,261,530	0	0	45,462	3.60%	89,044	7.06%	\$2.22	7,628	19,757	13,572	51,406
Uptown / Hillcrest	104	2,652,791	0	0	134,167	5.06%	225,760	8.51%	\$2.20	(3,863)	53,272	14,238	110,182
Central Total	661	25,695,110	25,000	387,000	2,395,417	9.32%	3,055,770	11.89%	\$2.09	(138,304)	(26,008)	506,255	1,295,182
I-15 Corridor													
Escondido	90	1,888,179	0	37,000	211,325	11.19%	273,312	14.47%	\$1.82	23,544	63,835	33,159	93,738
Poway	29	1,304,758	0	675,000	99,851	7.65%	109,071	8.36%	\$0.00	1,120	(14,731)	11,662	35,542
Rancho Bernardo	109	6,639,430	100,000	1,010,002	689,561	10.39%	875,188	13.18%	\$1.80	(139,106)	(130,749)	70,472	206,193
Scripps Ranch	50	2,674,259	0	846,200	347,503	12.99%	364,676	13.64%	\$2.15	11,598	127,524	42,051	176,790
I-15 Corridor Total	278	12,506,626	100,000	2,568,202	1,348,240	10.78%	1,622,247	12.97%	\$2.08	(102,844)	45,879	157,344	512,263
North County Coastal													
Carlsbad	152	6,017,270	232,609	601,158	1,207,543	20.07%	1,397,151	23.22%	\$2.33	(3,031)	(119,982)	97,046	320,934
Del Mar Heights / Carmel Valley	71	4,556,000	168,760	875,059	485,894	10.66%	780,481	17.13%	\$3.99	5,019	145,013	92,433	347,802
North Beach Cities	111	2,538,834	20,100	55,000	159,081	6.27%	229,009	9.02%	\$2.94	14,540	51,336	50,046	171,282
North County Total	334	13,112,104	421,469	1,531,217	1,852,518	14.13%	2,406,641	18.35%	\$2.72	16,528	76,367	239,525	840,018
North City													
Governor Park	19	856,764	0	0	123,036	14.36%	178,824	20.87%	\$2.75	21,219	25,930	43,184	95,637
La Jolla	54	1,630,086	14,750	0	174,906	10.73%	237,390	14.56%	\$4.00	28,585	66,927	46,855	145,115
Miramar	37	1,711,077	0	0	217,395	12.71%	309,079	18.06%	\$2.12	17,889	67,708	29,295	118,372
Sorrento Mesa	119	9,556,668	0	2,169,063	1,181,358	12.36%	1,587,143	16.61%	\$2.74	(198,660)	(259,408)	75,604	263,405
Sorrento Valley	27	785,003	0	0	121,257	15.45%	119,832	15.27%	\$1.96	(16,402)	24,875	30,061	96,890
Torrey Pines	43	2,703,699	0	0	173,405	6.41%	239,725	8.87%	\$4.05	(10,008)	(53,317)	15,417	82,576
UTC	85	8,367,296	64,832	390,770	1,348,937	16.12%	1,729,308	20.67%	\$3.98	67,235	217,041	165,292	691,083
North City Total	384	25,610,593	79,582	2,559,833	3,340,294	13.04%	4,401,301	17.19%	\$3.80	(90,142)	89,756	405,708	1,493,078
Southern & Eastern Areas													
Chula Vista	89	2,785,062	0	765,002	302,391	10.86%	381,923	13.71%	\$2.08	9,906	29,182	25,932	76,659
East County	152	3,699,615	0	194,200	249,640	6.75%	300,898	8.13%	\$1.24	(4,571)	(36,989)	26,254	84,864
National City	15	531,473	0	0	121,417	22.85%	36,955	6.95%	\$0.00	(2,901)	(10,126)	0	1,000
Otay Mesa	13	326,747	0	0	21,775	6.66%	21,775	6.66%	\$1.30	0	(1,019)	0	536
Southeast San Diego	10	391,848	0	0	62,180	15.87%	66,452	16.96%	\$1.65	5,218	7,610	5,218	8,384
Southern & Eastern Areas Total	279	7,734,745	0	959,202	757,403	9.79%	808,003	10.45%	\$1.70	7,652	(11,342)	57,404	171,443
Highway 78 Corridor													
Oceanside	62	1,345,800	0	337,567	193,466	14.38%	218,630	16.25%	\$1.69	12,189	36,380	23,041	59,095
San Marcos	37	1,352,911	0	1,367,139	161,790	11.96%	179,920	13.30%	\$1.16	37,357	42,630	37,875	75,177
Vista	49	1,214,946	0	0	205,281	16.90%	178,557	14.70%	\$1.53	10,953	26,980	18,549	49,803
Highway 78 Corridor Total	148	3,913,657	0	1,704,706	560,537	14.32%	577,107	14.75%	\$1.53	60,499	105,990	79,465	184,075
Class A	269	34,562,936	188,860	7,873,977	3,954,005	11.44%	5,311,074	15.37%	\$3.42	20,752	370,367	879,232	2,081,744
Class B	1,217	50,843,154	437,191	4,205,343	7,035,234	13.84%	8,541,641	16.80%	\$2.22	(321,139)	(55,911)	888,444	2,792,319
Class C	734	16,112,226	0	0	1,315,611	8.17%	1,633,479	10.14%	\$1.62	16,412	82,382	214,556	594,660
San Diego County Total	2,220	101,518,316	626,051	12,079,320	12,304,850	12.12%	15,486,194	15.25%	\$2.77	(283,975)	396,838	1,982,232	5,468,723

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
6260-6350 Sequence Dr. & 4921 Directors Pl.	Sorrento Mesa	B	537,654	\$303	John Hancock Life Insurance Co.	Kilroy Realty Corporation
10290 Campus Point Dr.	UTC	B	304,326	\$345	Alexandria Real Estate Equities	Qualcomm
5796 Armada Dr.	Carlsbad	A	74,891	\$375	Miller Global Properties	LaSalle Investment Management
128-130 Cedar Rd.	Vista	B	49,303	\$372	American Realty Capital Healthcare	Jayco Vista, LLC
4224 Campus Point Ct.	UTC	B	95,257	\$178	Phase 3 Real Estate Partners	MIG Real Estate

Lease Transactions

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
5770 Armada Dr.	Carlsbad	B	81,712	July-2015	SeaSpine Orthopedics Corp.	(Sublease)
5510 Morehouse Dr.	Sorrento Mesa	B	60,625	July-2015	Undisclosed	Brookfield Asset Management
5887 Copley Dr.	Kearny Mesa	A	59,965	Aug-2015	Cox Communications	Sudberry Properties, Inc.
7947 Mission Center Ct. – Renewal	Mission Valley	C	53,006	Aug-2015	Family Resource Center	TA Realty
9242 Lightwave Ave. – Renewal	Kearny Mesa	A	45,868	July-2015	Epsilon Systems Solutions	Colony Realty Partners

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.

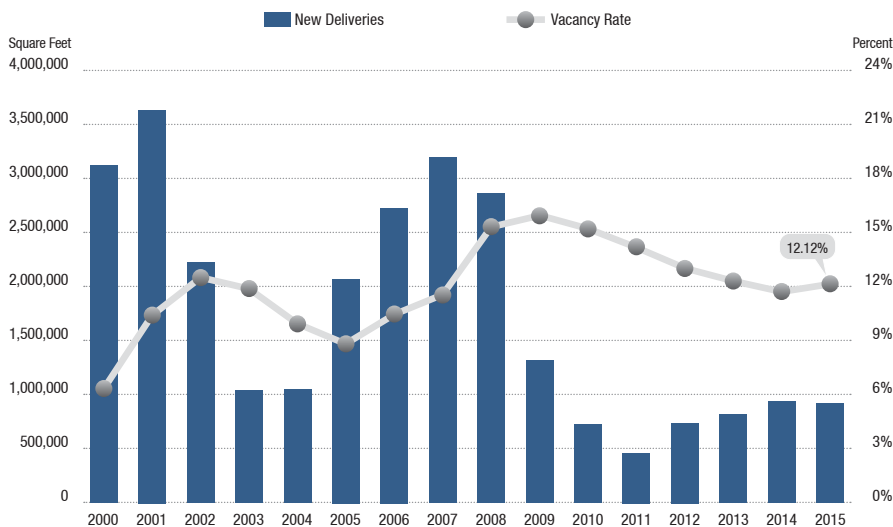
CLASS B

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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Anaheim, CA
714.978.7880

Inland Empire, CA
909.545.8000

Irvine, CA
949.851.5100

Los Angeles, CA
424.329.7500

San Diego, CA
858.453.0505

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