

MARKET OVERVIEW. The office market had a strong year with more than half a million square feet of positive net absorption, and the vacancy rate is edging towards single digits for the first time in this period of economic expansion. Rental rates continue to increase, and Kilroy Realty has been leading a venture into speculative office buildings which have seen strong demand. That along with Apple's local expansion have been a shot in the arm to the office market, and optimism is up heading into 2020.

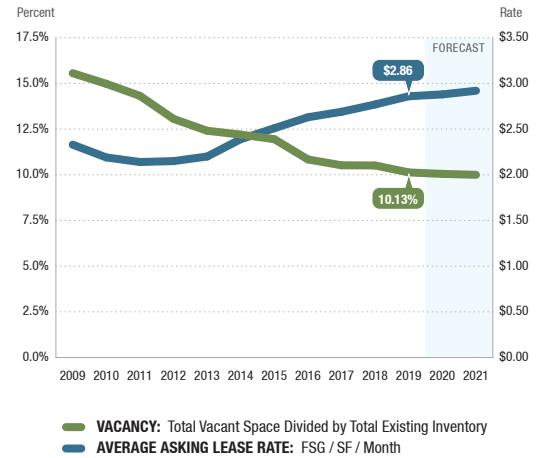
VACANCY. Direct/sublease space (unoccupied) finished the quarter at 10.13%, a moderate 38 basis point decrease from the rate of a year ago. Among the county's major submarkets (minimum of four million square feet of inventory), UTC ended the year with the lowest vacancy rate. UTC has come down 14 percentage points since the middle of 2016 and was at 4.6% vacancy at the end of 2019.

LEASE RATES. The average asking full-service gross (FSG) lease rate per square foot per month in San Diego County was \$2.86 at the end of the fourth quarter, which is a four-cent increase over the prior quarter, and an annual increase of 3.25% from the fourth quarter of 2018's rate of \$2.77. The overall San Diego office market average asking rate is now at an all-time high, surpassing the previous peak of \$2.74 from 2007.

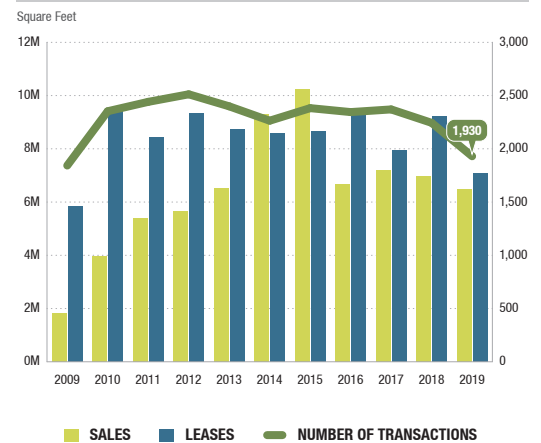
TRANSACTION ACTIVITY. Sale and lease transactions totaled 3.5 MSF in the fourth quarter, a slight decrease from the 3.7 MSF which transacted in the third quarter. Apple's local expansion is making major waves in San Diego County, as they recorded the top two lease transactions of the fourth quarter. The transaction activity statistic can have some lag time in being reported, so look for figures to end up even higher in the next report.

EMPLOYMENT. The unemployment rate in San Diego County was 2.9% in November 2019, unchanged from a revised 2.9% in October 2019, and below the year-ago estimate of 3.1%. This compares with an unadjusted unemployment rate of 3.7% for California and 3.3% for the nation during the same period. According to the State of California Employment Development Department, San Diego County gained 34,300 payroll jobs between November 2018 and November 2019, including 8,200 from the professional and business sector, which reported the largest overall gain. The government sector reported a growth of 7,800 jobs, the second most among the major employment sectors. The largest year-over-year loss was in trade, transportation, and utilities which reported 1,000 fewer jobs than the prior year.

VACANCY vs. AVERAGE ASKING LEASE RATE



TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



Market Statistics

	Change Over Last Quarter	4Q 2019	3Q 2019	4Q 2018	% Change Over Last Year
Vacancy Rate	▼ DOWN	10.13%	10.50%	10.51%	(3.66%)
Availability Rate	▼ DOWN	13.55%	13.63%	13.67%	(0.88%)
Average Asking Lease Rate	▲ UP	\$2.86	\$2.82	\$2.77	3.25%
Sale & Lease Transactions	▼ DOWN	3,517,802	3,685,564	4,520,191	(22.18%)
Gross Absorption	▼ DOWN	1,729,132	1,901,139	2,415,276	(28.41%)
Net Absorption	▲ POSITIVE	461,826	(91,800)	369,159	N/A

EMPLOYMENT. The labor market in San Diego County will continue to improve, although we anticipate job growth to slow. In 2018 there was a 1.7% increase in total employment, and a 1.0–1.2% increase is projected for 2019, and closer to 1% growth is projected in 2020. With the local stalwarts of Defense and Biotech remaining strong, look for these sectors to lead the way for employment gains, along with Technology.

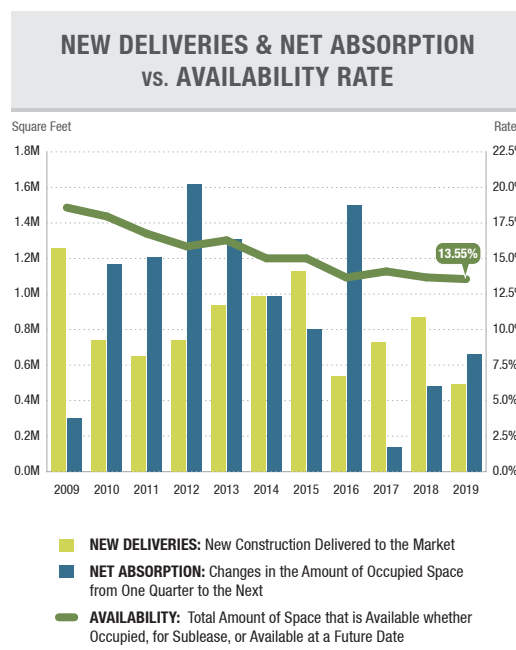
LEASE RATES. Expect the average asking lease rate to increase by a modest 2.5–3.0% over the next four quarters.

VACANCY. Vacancy has been very stable since dropping below 11% in 2016, remaining in the 10–11% range. In the next 4–6 quarters we expect vacancy to dip into the single digit range, moving under 10% for the first time since 2006.

CONSTRUCTION. Speculative construction remains modest overall, and preleasing has been strong. Following good preleasing demand for Kilroy’s One Paseo project in Del Mar Heights, Kilroy has now begun construction on the 223,000 square foot 2300 Kettner office building in the Little Italy corner of Downtown, with more than a quarter of the building leased already.

ABSORPTION. The San Diego office market recorded 461,826 square feet of positive net absorption in the fourth quarter, and the 2019 total was 659,495 square feet of positive net absorption. This total surpasses the annual totals from both 2017 and 2018. There are hundreds of thousands of square feet of preleased office space under construction, so this will add significant levels of positive net absorption in the coming quarters, as these new construction projects come online.

AVAILABILITY. Direct/sublease space being marketed was 13.55% at the end of the fourth quarter, a small decrease of 8 basis points from the third quarter, and an overall decrease of 0.9% from the previous year.



Significant Transactions

Sales

Property Address	Submarket	Class	Square Feet	Sale Price	Buyer	Seller
9605–9855 Scranton Rd.	Sorrento Mesa	A&B	689,925	\$229,927,500	Alexandria RE Equities	CalSTRS
5887 Copley Dr.	Kearny Mesa	A	205,725	\$90,363,636	CIM Group, LP	Sudberry Properties
450 B St.	Downtown	A	283,786	\$71,000,000	LeBeau Realty & Associates	Sumitomo Corp. of Americas
12626 & 12636 High Bluff Dr.	Del Mar Heights	B	119,504	\$59,000,000	Swift Real Estate Partners	The Blacstone Group, LP
9040 & 9050 Friars Rd.	Mission Valley	B	152,944	\$33,919,115	Westbrook Partners	Wawanesa General Insurance

Leases

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
9775 Towne Centre Dr.	UTC	A	204,000	Oct-2019	Apple	BioMed Realty
9455 Towne Centre Dr.	UTC	A	165,000	Dec-2019	Apple	Kilroy Realty
1950 Camino Vida Roble	Carlsbad	A	121,541	Dec-2019	Alpatec Spine	RAF Pacifica Group
550 W. C St.	Downtown	A	36,704	Nov-2019	Undisclosed	Alaska Permanent Fund
11455 El Camino Real	Del Mar Heights	A	32,775	Dec-2019	Undisclosed	American Assets Trust

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 4Q2019	Square Feet Available	Availability Rate 4Q2019	Average Asking Lease Rate	Net Absorption 4Q2019	Net Absorption 2019	Gross Absorption 4Q2019	Gross Absorption 2019
Downtown													
Downtown	128	13,024,935	595,357	3,388,248	2,204,915	16.93%	2,743,160	21.06%	\$2.83	42,136	(104,214)	212,984	867,313
Downtown Total	128	13,024,935	595,357	3,388,248	2,204,915	16.93%	2,743,160	21.06%	\$2.83	42,136	(104,214)	212,984	867,313
Central													
City Heights/University	31	1,216,139	0	0	54,725	4.50%	93,806	7.71%	\$2.31	(4,123)	(14,027)	3,936	18,391
Coronado	6	124,831	0	0	1,232	0.99%	2,763	2.21%	\$4.22	6,295	5,081	7,640	7,640
Kearny Mesa	238	11,007,875	215,000	229,000	720,486	6.55%	1,212,379	11.01%	\$2.27	71,588	83,627	126,067	564,867
Mission Gorge	19	567,430	0	0	6,008	1.06%	10,116	1.78%	\$1.97	4,689	3,921	7,121	27,181
Mission Valley	127	7,220,560	0	0	773,736	10.72%	1,133,958	15.70%	\$2.75	32,884	(75,542)	109,086	646,180
Old Town/Point Loma	79	2,408,771	0	230,000	79,936	3.32%	120,140	4.99%	\$2.84	19,898	48,426	38,654	126,983
Park East	17	273,122	0	0	22,821	8.36%	22,821	8.36%	\$2.37	(120)	(16,058)	180	7,834
Rose Canyon/Morena	54	1,233,791	0	0	66,567	5.40%	100,270	8.13%	\$1.95	(19,249)	(2,706)	7,614	86,961
Uptown/Hillcrest	78	2,211,113	0	0	115,510	5.22%	184,877	8.36%	\$2.71	2,823	6,318	15,168	90,555
Central Total	649	26,263,632	215,000	459,000	1,841,021	7.01%	2,881,130	10.97%	\$2.48	114,685	39,040	315,466	1,576,592
I-15 Corridor													
Escondido	74	1,686,007	75,000	46,614	156,569	9.29%	230,727	13.68%	\$2.39	(17,352)	20,123	5,811	114,638
Poway	30	1,325,923	0	160,000	18,430	1.39%	62,128	4.69%	\$2.33	4,901	16,628	7,203	39,205
Rancho Bernardo	105	6,800,918	0	2,595,747	659,493	9.70%	1,068,382	15.71%	\$3.11	66,101	81,635	111,641	402,735
Scripps Ranch	52	2,897,182	0	137,000	480,048	16.57%	583,975	20.16%	\$2.64	(34,762)	169,192	28,708	415,192
I-15 Corridor Total	261	12,710,030	75,000	2,939,361	1,314,540	10.34%	1,945,212	15.30%	\$2.87	18,888	287,578	153,363	971,770
North County Coastal													
Carlsbad	162	6,807,825	0	10,000	1,072,370	15.75%	1,136,192	16.69%	\$2.62	10,116	339,770	144,009	854,472
Del Mar Heights/Carmel Valley	76	4,765,280	288,484	634,192	678,971	14.25%	883,863	18.55%	\$4.36	(33,368)	120,351	83,629	540,531
North Beach Cities	112	2,636,582	97,525	140,389	130,997	4.97%	248,790	9.44%	\$3.64	110,245	166,058	143,068	313,550
North County Total	350	14,209,687	386,009	784,581	1,882,338	13.25%	2,268,845	15.97%	\$3.35	86,993	626,179	370,706	1,708,553
North City													
Governor Park	20	897,461	0	0	80,102	8.93%	132,830	14.80%	\$2.73	7,181	2,233	15,942	64,109
La Jolla	45	1,342,740	0	0	185,162	13.79%	239,679	17.85%	\$3.44	(30,635)	(112,662)	3,287	99,134
Miramar	33	1,487,988	0	0	108,215	7.27%	159,606	10.73%	\$1.73	(8,488)	(12,873)	21,157	87,779
Sorrento Mesa	123	9,783,325	0	1,476,500	1,191,685	12.18%	1,444,281	14.76%	\$2.90	31,111	(115,747)	175,203	692,578
Sorrento Valley	28	772,789	0	0	121,559	15.73%	156,153	20.21%	\$2.83	(24,312)	(46,354)	1,097	29,126
Torrey Pines	44	3,192,191	0	0	237,909	7.45%	321,878	10.08%	\$4.40	(4,602)	(149,579)	3,100	46,964
UTC	91	8,797,386	165,000	447,124	492,478	5.60%	674,525	7.67%	\$3.56	220,815	256,826	356,358	975,872
North City Total	384	26,273,880	165,000	1,923,624	2,417,110	9.20%	3,128,952	11.91%	\$3.01	191,070	(178,156)	576,144	1,995,562
Southern & Eastern Areas													
Chula Vista	90	2,840,906	0	1,428,151	187,896	6.61%	266,514	9.38%	\$2.52	(385)	38,036	17,725	156,000
National City	15	528,472	0	0	994	0.19%	9,035	1.71%	\$1.62	6,480	0	6,480	8,286
Otay Mesa	13	319,824	0	0	15,861	4.96%	50,241	15.71%	\$2.30	(3,064)	(11,571)	0	1,002
Southeast San Diego	13	460,835	0	290,000	78,409	17.01%	78,409	17.01%	\$2.00	(25,409)	(18,211)	0	7,698
East County	149	3,620,718	86,000	86,800	115,865	3.20%	151,053	4.17%	\$1.99	18,473	20,398	34,748	159,477
Southern & Eastern Areas Total	280	7,770,755	86,000	1,804,951	399,025	5.13%	555,252	7.15%	\$2.35	(3,905)	28,652	58,953	332,463
Highway 78 Corridor													
Oceanside	63	1,349,020	100,000	302,749	124,142	9.20%	176,917	13.11%	\$2.07	14,928	21,778	23,784	103,689
San Marcos	38	1,407,116	0	2,041,538	91,505	6.50%	109,042	7.75%	\$2.45	653	13,377	17,032	66,383
Vista	51	1,254,343	0	0	284,965	22.72%	316,348	25.22%	\$1.75	(3,622)	(74,739)	700	92,894
Highway 78 Corridor Total	152	4,010,479	100,000	2,344,287	500,612	12.48%	602,307	15.02%	\$2.02	11,959	(39,584)	41,516	262,966
Class A	294	37,330,653	1,248,841	9,471,172	4,207,166	11.27%	5,849,382	15.67%	\$3.43	346,562	998,079	720,163	3,692,933
Class B	1,260	52,735,327	373,525	4,172,880	5,519,321	10.47%	7,192,895	13.64%	\$2.60	138,087	(378,955)	854,707	3,307,302
Class C	650	14,197,418	0	0	833,074	5.87%	1,082,581	7.63%	\$2.04	(22,823)	40,371	154,262	714,984
San Diego County Total	2,204	104,263,398	1,622,366	13,644,052	10,559,561	10.13%	14,124,858	13.55%	\$2.86	461,826	659,495	1,729,132	7,715,219

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



Rebound Year

by **Jon Boland**

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The San Diego Office market bounced back in 2019, posting a three-year high in positive net absorption. This puts the market on the cusp of single-digit vacancy rates for the first time in 14 years. To the victor go the spoils, and the Class A segment saw a million square feet of positive net absorption for the year, while Class B posted negative net absorption. The technology sector is currently one of the biggest growth engines in San Diego office occupancy. The big hype in 2018 was Amazon opening a new 100,000 square foot location in San Diego, followed by a subsequent 85,000 square foot expansion later that year. In 2019, Apple doubled down, opening a new 100,000 square foot office and inking deals to lease two entire projects under construction in UTC for an additional 369,000 square feet. This level of activity shows they are following through on their intention to ramp up their San Diego presence from virtually nothing to 1,200 employees by 2021.

These recent high-profile expansions are within the UTC submarket which acts as the de facto suburban CBD for San Diego County, and interestingly both Amazon and Apple chose projects that were geared towards biotech companies. While the life science companies in San Diego don't have the household name recognition that the tech companies do, they are one of the true pillars of the San Diego economy. Both sectors are drawn to San Diego due to the high skill level of local workers. San Diego State University is the 9th most applied to university in the country, and UC San Diego is the 2nd most applied to university in the nation. UC San Diego's engineering program is ranked among the top 10 in the country, while its Computer Science program is ranked in the top 10 in the world. Clearly these growing companies are coming here because they know the talent is here and wants to be here.

Another headline across the US office sector was WeWork's IPO fiasco. Clearly the coworking phenomenon has taken root over the past couple years, but as poster child for coworking WeWork did not do its industry any favors in the execution of their growth plan. The San Diego market doesn't share the same level of concern about WeWork's vulnerability as other markets do as it's been reported that WeWork's market share in the county is one of the lowest among major metros.

2019 has increased the optimism for San Diego's economy, and we are looking forward to 2020.

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This survey consists of properties representing both single tenant and multi-tenant buildings. The lease rates are based on a full-service gross 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. ©2020 Voit Real Estate Services, Inc. DRE License #01991785.

Represented in 150 Markets
Nationally & Internationally.



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.

Submarkets

DOWNTOWN: Downtown

CENTRAL: City Heights / University, Coronado, Kearny Mesa, Mission Gorge, Mission Valley, Old Town / Point Loma, Park East, Rose Canyon / Morena, Uptown / Hillcrest

I-15 CORRIDOR: Escondido, Poway, Rancho Bernardo, Scripps Ranch

NORTH COUNTY COASTAL: Carlsbad, Del Mar Heights / Carmel Valley, North Beach Cities

NORTH CITY: Governor Park, La Jolla, Miramar, Sorrento Mesa, Sorrento Valley, Torrey Pines, UTC

SOUTHERN & EASTERN AREAS: Chula Vista, East County, National City, Otay Mesa, Southeast San Diego

HIGHWAY 78 CORRIDOR: Oceanside, San Marcos, Vista