

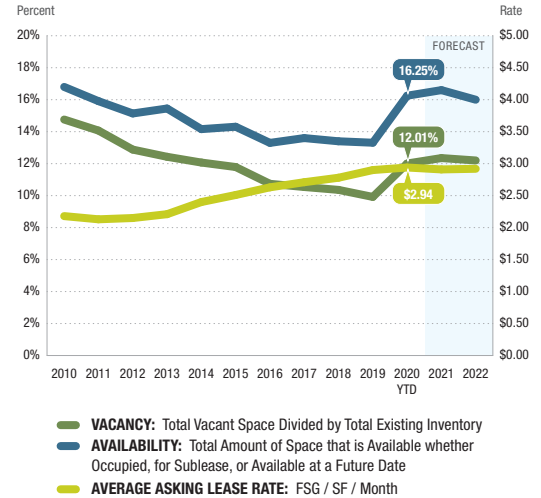
OVERVIEW. This is a difficult time for the San Diego office market. The market has seen more than a million square feet of negative net absorption so far this year, and that has been dispersed through the whole county, not limited to certain areas. Asking lease rates decreased in 3Q, and availability increased. The office market will continue to remain hampered while restrictions from government, and individual companies, remain in place.

VACANCY & AVAILABILITY. Direct/sublease space (unoccupied) finished the quarter at 12.01%, a 133-basis-point increase. In the first three quarters of 2020 the overall occupancy has retreated back to levels last seen in 2015. Among the county's major submarkets (minimum of four million square feet of inventory), UTC is now the only submarket with a vacancy rate below 10%, while the vacancy rate in Downtown now exceeds 20%. Available office space being marketed (regardless of occupancy status) was 16.25% at the end of the 3Q, a 2.8 percentage point increase in over 3Q 2019's rate, and a substantial 4.2 percentage points higher than the vacancy rate. Headlines about a flood of sublease space continue to come out of the tech-heavy San Francisco Bay Area office market. Fortunately, the same has not happened in San Diego. Since the start of the year the sublease office space available has increased by 455,000 SF, and direct office space for lease has increased by 2.7 MSF. The largest sublease space which has come to market since March is approximately 200,000 SF from American Specialty Health in Sorrento Mesa.

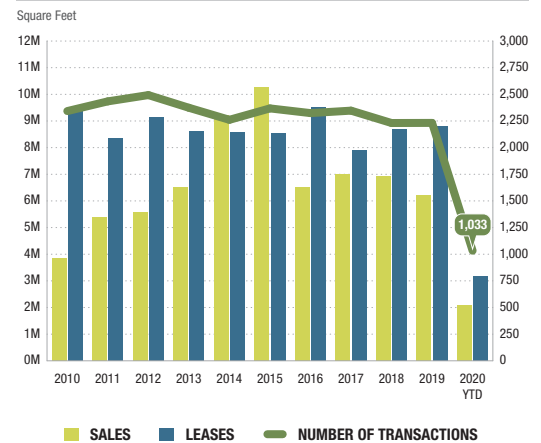
LEASE RATES. The average asking full-service gross (FSG) lease rate per square foot per month in San Diego County was \$2.94 at the end of 3Q, which is a two-cent decrease over the prior quarter, yet an annual increase of 2.8% from 3Q 2019's rate of \$2.86. Asking rates do not tell the whole story as landlords typically budge on effective rental rates before moving the asking rental rates. As always, every lease negotiation depends on the specific tenant's alternative options, and the specific landlord's position and posture. With that said, on the average, tenants are gaining the upper hand in lease negotiations as they see rising vacancy rates as an opportunity to take a stronger negotiating stance. In practice, a majority of office tenants would prefer not to negotiate in the current environment until they have more clarity on their own situation.

TRANSACTION ACTIVITY. Sale and lease transactions totaled 0.9 MSF in 3Q, below last quarter's 1.3 MSF leased and sold, and a fraction of the 4.5 MSF which transacted in 3Q 2019. The largest sale of the quarter was Alexandria's \$97.5 million acquisition of the 139,000 SF National University headquarters. This one transaction represented about 15% of the total amount of office space leased and sold in the quarter; and this was really more of a long-term redevelopment play to acquire 11.4 acres in Torrey Pines. Over the last decade, the office market has averaged more than 550 lease transactions per quarter. In 2Q 2020 there were about 250 lease transactions, and in 3Q there were fewer than 350 lease transactions. Beyond the headline statistics which point towards the decline of office tenant demand in the current environment, even in the leases that are happening, tenants are pushing for shorter term leases where they can. The annual averages over the last four years are 8.7 MSF leased, and 6.7 MSF sold. For the full year 2020, the San Diego Office market is currently on pace for 4.2 MSF of office space leased, and 2.8 MSF of offices sold.

VACANCY, AVAILABILITY & AVERAGE ASKING LEASE RATES



TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



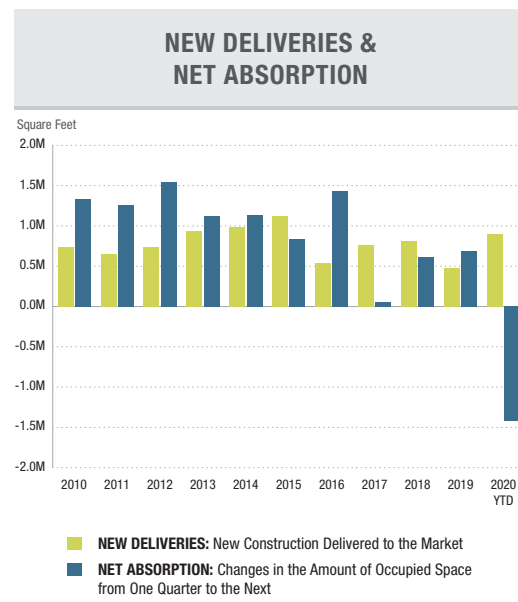
Market Statistics

	Change Over Last Quarter	3Q 2020	2Q 2020	3Q 2019	% Change Over Last Year
Vacancy Rate	▲ UP	12.01%	10.68%	10.27%	16.98%
Availability Rate	▲ UP	16.25%	14.99%	13.42%	21.07%
Average Asking Lease Rate	▼ DOWN	\$2.94	\$2.96	\$2.86	2.80%
Sale & Lease Transactions	▼ DOWN	926,520	1,260,883	4,485,730	(79.35%)
Gross Absorption	▲ UP	1,264,075	1,138,786	1,773,726	(28.73%)
Net Absorption	▼ NEGATIVE	(667,158)	(301,530)	(107,236)	N/A

ABSORPTION. The San Diego office market recorded 667,158 SF of negative net absorption in 3Q. There have not been any calendar years of negative absorption since 2008, and the market is approaching 1.5 MSF of negative net absorption through the first three quarters of 2020.

CONSTRUCTION. The office market has 2.1 MSF under construction at present. Prior to last quarter, the construction pipeline had not surpassed 2 MSF since 2008. In the years following the Great Recession, one of the primary stabilizing factors in the local office market was the very modest supply of new offices being built. The relatively light supply of new office paired well with the slow and steady nature of the office market recovery. Developers were praised for their disciplined approach, not overbuilding beyond the appetite of market demand. The office development pipeline appears to have ramped up at a very inopportune time, with downtown as a focal point. Between the Paladion revamp, the conversion of the former Thomas Jefferson Law School building, Kilroy’s speculative 2100 Kettner project, The Campus at Horton Plaza, and 450 B Street, there are more than 1.3 MSF of recently repositioned, or currently under-construction office space available in Downtown.

EMPLOYMENT. The unemployment rate in San Diego County was 9.9% in August 2020, down from a revised 12.4% in July 2020, and substantially greater than the year-ago estimate of 3.4%. This compares with an unadjusted unemployment rate of 11.6% for California and 8.5% for the nation during the same period. According to the State of California Employment Development Department, San Diego County gained 20,500 jobs between July 2020 and August 2020. With the normal delay in reporting from the California EDD, employment figures from September were unavailable at the time of publishing this report. In September, the employment data for the United States as a whole came in with 661,000 jobs added which was the fifth straight month of net job gains.



Forecast

The road forward heavily depends on factors outside of traditional free market considerations, including COVID-19 vaccine development, state and local government restrictions on business operations, and economic stimulus actions. Based upon the current conditions and outlook, we anticipate a decrease in net effective rental rates as concessions will increase in the currently diminished transaction-volume environment. At present, these movements are anticipated to be generally moderate, but will fluctuate significantly based upon the specific submarket within the county. Overall, we expect the current trends in the office market to continue in the short-term outlook. Absorption, both gross and net, are likely to suffer further declines as tenants continue their struggle to return to normal operations. That will cause further increases in vacancy and more tenants will be rethinking how they utilize their space over the long term, which will put a strain on the office market into next year.

Significant Transactions

Sales

Property Address	Submarket	Class	Square Feet	Sale Price	Buyer	Seller
11255 & 11355 N. Torrey Pines Rd.	Torrey Pines	B	139,135	\$97,500,000	Alexandria Real Estate Equities	National University
2176 Salk Ave.	Carlsbad	B	46,199	\$24,750,000	Scripps Health	H.G. Fenton
15706-15708 Pomerado Rd.	Poway	B	46,183	\$17,000,000	Healthcare Realty Trust, Inc.	Milan Capital Management
2160 S. El Camino Real	Oceanside	C	13,500	\$6,650,000	Gemar Santa Fe, LLC	GW Green Properties
5928 Pascal Ct.	Carlsbad	B	38,276	\$6,150,000	Mesa Centers	Sterling Trustees

Leases

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
10150 Meanley Dr.*	Scripps Ranch	B	30,245	Jul-2020	CUSO Financial Services	Double Black Diamond Properties, LLC*
5375 Mira Sorrento Pl.	Sorrento Mesa	A	19,978	Sep-2020	Dexcom	Shorenstein Properties, LLC
3570 Carmel Mountain Rd.	Del Mar Heights/ Carmel Valley	A	19,105	Aug-2020	Zeku	The Irvine Company
2310 Camino Vida Roble	Carlsbad	B	11,583	Sep-2020	Undisclosed	Doumani Trust
7862 El Cajon Blvd.	La Mesa	C	9,367	Sep-2020	Undisclosed	Medicus Property Group

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 3Q2020	Square Feet Available	Availability Rate 3Q2020	Average Asking Lease Rate	Net Absorption 3Q2020	Net Absorption 2020	Gross Absorption 3Q2020	Gross Absorption 2020
Downtown													
Downtown	127	13,502,505	1,072,769	2,334,082	2,871,353	21.27%	4,024,668	29.81%	\$2.84	(125,134)	(295,263)	107,136	428,724
Downtown Total	127	13,502,505	1,072,769	2,334,082	2,871,353	21.27%	4,024,668	29.81%	\$2.84	(125,134)	(295,263)	107,136	428,724
Central													
City Heights / University	31	1,216,139	0	0	65,205	5.36%	105,831	8.70%	\$2.22	(7,766)	(9,252)	330	26,667
Coronado	5	111,541	0	0	2,732	2.45%	4,263	3.82%	\$4.50	0	(1,500)	0	300
Kearny Mesa	238	11,101,127	125,000	185,186	1,129,719	10.18%	1,385,105	12.48%	\$2.51	(200)	(322,311)	167,969	283,625
Mission Gorge	19	581,130	0	0	3,543	0.61%	7,664	1.32%	\$1.67	6,862	2,465	8,612	8,612
Mission Valley	127	7,269,799	0	0	852,339	11.72%	1,222,759	16.82%	\$2.71	(115,307)	(84,636)	101,686	403,793
Old Town / Point Loma	79	2,419,065	0	230,000	86,895	3.59%	218,837	9.05%	\$2.87	(12,443)	(6,959)	11,132	62,130
Park East	16	234,322	0	0	16,444	7.02%	31,742	13.55%	\$2.08	(3,247)	3,864	2,433	17,591
Rose Canyon / Morena	56	1,297,671	0	0	96,166	7.41%	148,910	11.48%	\$2.10	(13,627)	(25,824)	7,090	41,974
Uptown / Hillcrest	79	2,225,121	0	0	184,849	8.31%	252,918	11.37%	\$2.72	(48,481)	(69,339)	9,933	42,415
Central Total	650	26,455,915	125,000	415,186	2,437,892	9.21%	3,378,029	12.77%	\$2.60	(194,209)	(513,492)	309,185	887,107
I-15 Corridor													
Escondido	75	1,766,571	0	46,614	218,239	12.35%	279,889	15.84%	\$1.99	30,102	18,394	50,717	97,351
Poway	29	1,263,220	0	0	26,478	2.10%	79,397	6.29%	\$2.20	386	(13,702)	1,185	9,706
Rancho Bernardo	104	6,846,168	0	2,740,820	870,376	12.71%	1,037,205	15.15%	\$2.99	(187,067)	(215,593)	26,808	213,523
Scipps Ranch	53	2,916,228	0	356,000	471,395	16.16%	456,461	15.65%	\$2.79	(49,251)	8,653	7,815	85,403
I-15 Corridor Total	261	12,792,187	0	3,143,434	1,586,488	12.40%	1,852,952	14.49%	\$2.81	(205,830)	(202,248)	86,525	405,983
North County Coastal													
Carlsbad	164	6,903,300	0	50,000	1,172,838	16.99%	1,321,676	19.15%	\$2.70	(55,732)	(77,220)	143,174	390,702
Del Mar Heights / Carmel Valley	79	5,098,960	217,235	416,955	803,735	15.76%	1,222,972	23.98%	\$4.29	103,969	155,135	198,829	408,561
North Beach Cities	114	2,686,264	72,177	120,456	213,221	7.94%	376,630	14.02%	\$3.73	(24,332)	(53,704)	23,687	103,875
North County Total	357	14,688,524	289,412	587,411	2,189,794	14.91%	2,921,278	19.89%	\$3.35	23,905	24,211	365,690	903,138
North City													
Governor Park	20	899,461	0	0	111,468	12.39%	138,041	15.35%	\$2.70	(9,627)	(31,366)	15,730	33,735
La Jolla	45	1,328,629	0	0	260,983	19.64%	301,669	22.71%	\$3.32	(57,826)	(79,906)	6,386	26,863
Miramar	32	1,451,242	0	0	89,426	6.16%	201,136	13.86%	\$1.98	17,120	(5,852)	21,622	59,658
Sorrento Mesa	120	9,538,997	0	1,481,000	1,115,102	11.69%	1,553,503	16.29%	\$3.17	(29,764)	(63,275)	87,206	401,875
Sorrento Valley	27	742,572	0	0	162,592	21.90%	193,223	26.02%	\$2.27	(23,558)	(70,809)	13,781	19,443
Torrey Pines	44	3,206,337	74,000	0	261,837	8.17%	250,366	7.81%	\$4.43	(31,222)	(55,955)	12,891	33,464
UTC	92	8,858,725	369,000	699,124	615,588	6.95%	990,943	11.19%	\$3.67	(10,522)	(104,572)	142,484	318,000
North City Total	380	26,025,963	443,000	2,180,124	2,616,996	10.06%	3,628,881	13.94%	\$3.19	(145,399)	(411,735)	300,100	893,038
Southern & Eastern Areas													
Chula Vista	90	2,840,782	0	1,203,000	184,357	6.49%	289,827	10.20%	\$2.53	1,820	2,089	28,310	98,957
National City	15	528,493	0	0	11,347	2.15%	10,341	1.96%	\$2.10	(12)	(10,353)	2,000	2,000
South San Diego	13	319,824	0	0	11,663	3.65%	47,210	14.76%	\$2.02	0	4,198	0	4,198
Southeast San Diego	13	460,835	0	290,000	68,167	14.79%	84,917	18.43%	\$2.03	443	10,242	443	17,227
East County	151	3,666,012	86,000	300,300	151,857	4.14%	195,566	5.33%	\$2.13	(12,211)	(3,992)	13,460	48,789
Southern & Eastern Areas Total	282	7,815,946	86,000	1,793,300	427,391	5.47%	627,861	8.03%	\$2.22	(9,960)	2,184	44,213	171,171
Highway 78 Corridor													
Oceanside	63	1,350,466	100,000	277,749	106,317	7.87%	148,351	10.99%	\$1.96	16,358	17,825	38,106	61,872
San Marcos	38	1,464,541	0	1,815,718	114,240	7.80%	181,372	12.38%	\$2.52	(6,428)	(24,521)	9,735	38,759
Vista	51	1,285,312	0	0	309,317	24.07%	362,903	28.23%	\$2.18	(20,461)	(18,233)	3,385	16,038
Highway 78 Corridor Total	152	4,100,319	100,000	2,093,467	529,874	12.92%	692,626	16.89%	\$2.26	(10,531)	(24,929)	51,226	116,669
Class A	305	39,540,181	1,580,004	9,604,051	6,082,321	15.38%	8,376,881	21.19%	\$3.45	(180,430)	(441,524)	520,395	1,612,279
Class B	1,262	51,686,747	536,177	2,942,953	5,599,302	10.83%	7,480,987	14.47%	\$2.73	(400,606)	(796,366)	632,696	1,851,167
Class C	642	14,154,431	0	0	978,165	6.91%	1,268,427	8.96%	\$2.18	(86,122)	(183,382)	110,984	342,384
San Diego County Total	2,209	105,381,359	2,116,181	12,547,004	12,659,788	12.01%	17,126,295	16.25%	\$2.94	(667,158)	(1,421,272)	1,264,075	3,805,830

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



Pressing Through the Darkness

by **Jon Boland**

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When it comes to the San Diego office market right now, it is pretty quiet out there. Tenant demand is down. Leasing volume is down. Sales volume is down. Vacancy is up . . . so where is the action? The most active sector in the San Diego office market right now is an industry typically associated with R&D properties--life sciences and biotechnology. Alexandria has been on a tear. In the second quarter Alexandria acquired the Braille Institute site in the heart of the UTC office market for \$43 million. This quarter Alexandria acquired the headquarters of National University in Torrey Pines for \$98 million for future redevelopment. Just last month Alexandria announced a partnership with Regency Centers that will reportedly cost them hundreds of millions to be able to add office and lab space into the planned redevelopment of the Costa Verde shopping center across the street from the UTC mall. Alexandria isn't the only player making biotech waves in the office market. Stockdale Capital Partners, which is converting Horton Plaza from a shopping mall into a primarily office mixed-use campus, recently announced that they are expanding their vision beyond the technology sector to go after life sciences and biotechnology tenants. That wasn't even the biggest news in this regard that came out of Downtown. A new biotech focused developer, IQHQ, acquired a majority of the waterfront Manchester Pacific Gateway project and expects to spend more than \$1.5 billion developing the site with office and R&D buildings.

Most industries in the office real estate arena are not in this same expansion mode, however. Overall, there is still some sentiment of wait and see. Leases are still expiring, and companies still have to make decisions about their real estate needs, but we are seeing an increase in companies in the market for shorter term leases, in order to bide their time. Of the tenants that are making moves now, both sides of the negotiation are operating with a limited sense of where the market truly is. The activity level is so low that market fundamentals are not particularly clear. This will certainly play out differently across the county. The office market in Downtown San Diego was already relatively soft before COVID-19. The current state of affairs may hit Downtown in a major way. Conversely, areas like UTC came into the year with one of the lowest vacancy rates among the primary office submarkets. Landlords in that area don't have the alarm bells going off in the same way that we hear in Downtown.

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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.

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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, South San Diego, Southeast San Diego

HIGHWAY 78 CORRIDOR: Oceanside, San Marcos, Vista