

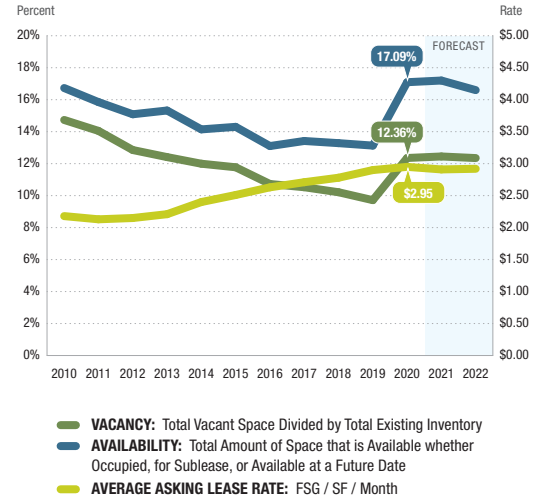
OVERVIEW. The San Diego office market posted substantial negative net absorption in 2020, and the development pipeline has ramped up at a very inopportune time. The total office square feet leased in 2020 was less than half the amount leased in 2019. The office market is in a decline and will continue on that path at least until the vaccine distribution ramps up. The office market will continue to remain hampered while restrictions from government, and the resulting defensive posture from tenants, remain in place.

VACANCY & AVAILABILITY. Direct/sublease space (unoccupied) finished the quarter at 12.36%, a 50-basis-point increase. The post-pandemic office market saw the past seven years' worth of occupancy gains wiped out in 2020. Among the county's major submarkets (minimum of four MSF of inventory), UTC is now the only submarket with a vacancy rate below 10%, while the vacancy rate in Downtown now sits just below 20%. Available office space being marketed (regardless of occupancy status) was 17.09% at the end of the 2020, a 4 percentage point increase in over 4Q 2019's rate, and a substantial 4.7 percentage points higher than the vacancy rate. Sublease availability increased by 603,580 SF in 2020, finishing the year at a 2.3% availability rate, the highest sublease availability rate since 2009. More than 100 office suites across San Diego County came onto the market for sublease in 4Q alone.

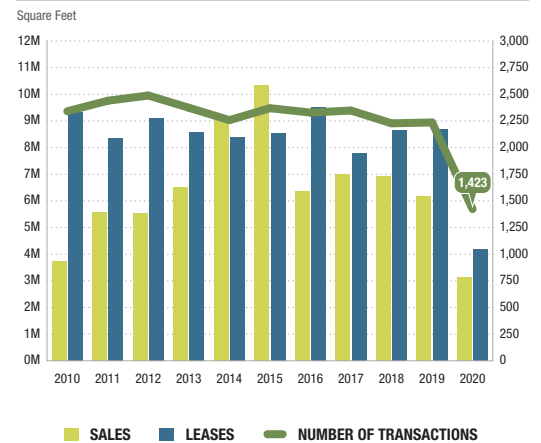
LEASE RATES. The average asking full-service gross (FSG) lease rate per square foot per month in San Diego County was \$2.95 at the end of 4Q, which is a one-cent increase over the prior quarter, and an annual increase of 1.8% from 4Q 2019's rate of \$2.90. Asking rates do not tell the whole story, as landlords are offering more lease concessions which lowers the effective rental rates without affecting the asking rates. The surge in new construction also increases the proportion of high-end office space, pushing up the county's average asking rental rate higher.

TRANSACTION ACTIVITY. Sale and lease transactions totaled 1.9 MSF in 4Q, a major increase from last quarter's 1.0 MSF leased and sold, and a major decline from the 3.6 MSF which transacted in pre-pandemic 4Q 2019. Alexandria Real Estate Equities was the buyer in the largest transaction of the quarter for the second consecutive quarter. This highlights one of the strongest sectors in the San Diego economy: biotechnology. In past times of economic contraction, the large local defense industry often acted as the primary counter-cyclical growth engine. In the current pandemic-ravaged economy, the local biotech concentration is one of the only sectors with increasing office demand. In fact, the top four sales in 4Q were acquired by companies with ties to biotechnology or healthcare. Despite this one bright spot, transaction activity remains depressed. 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 recorded 4.2 MSF of office space leased, and 3.1 MSF of offices sold.

VACANCY, AVAILABILITY & AVERAGE ASKING LEASE RATES



TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



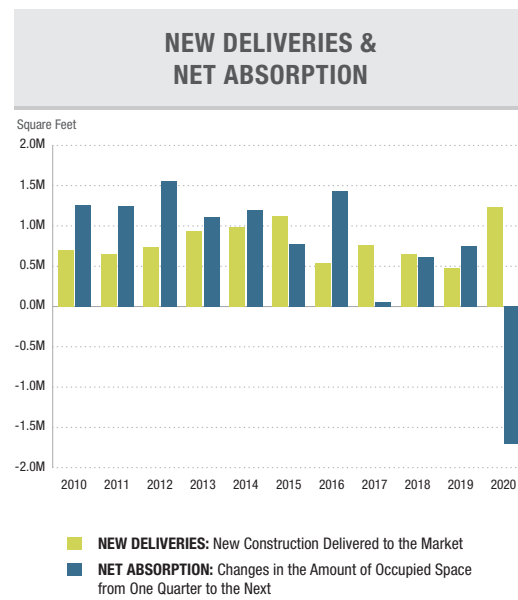
Market Statistics

	Change Over Last Quarter	4Q 2020	3Q 2020	4Q 2019	% Change Over Last Year
Vacancy Rate	▲ UP	12.36%	11.86%	9.72%	27.14%
Availability Rate	▲ UP	17.09%	16.10%	13.13%	30.19%
Average Asking Lease Rate	▲ UP	\$2.95	\$2.94	\$2.90	1.72%
Sale & Lease Transactions	▲ UP	1,926,158	993,706	3,534,185	(45.50%)
Gross Absorption	▲ UP	1,989,429	1,278,785	1,570,916	26.64%
Net Absorption	▼ NEGATIVE	(234,379)	(654,677)	386,371	N/A

ABSORPTION. The San Diego office market recorded 234,379 SF of negative net absorption in 4Q, and a total of 1,704,323 SF of negative net absorption in 2020. This was the first calendar year of negative absorption since 2008. The only major office submarket to see positive net absorption in 2020 was Del Mar Heights / Carmel Valley which increased its office tenant base by a quarter MSF. This positive net absorption in the submarket can entirely be attributed to Kilroy Realty's new "One Paseo" development which delivered in 2020 and was 92% leased at year-end.

CONSTRUCTION. The office market has 1.9 MSF under construction at the end of Q4, which marks the largest year-end tally since 2007. Only one third of the office space currently under construction has been pre-leased. Apple accounts for 369,000 SF of the pre-leased office space via two UTC offices being developed separately by BioMed Realty and Kilroy Realty. The largest speculative office projects under construction include Kilroy Realty's 234,000 square foot "2100 Kettner" project in Little Italy, and Lincoln Property Company's 217,000 square foot phase one of "Aperture Del Mar" on the Highway-56 Corridor. Conversely, the new offices constructed in 2020 are 93% leased at year end. There were 1.2 MSF of new offices delivered in 2020, the largest annual total in a decade.

EMPLOYMENT. The unemployment rate in San Diego County was 6.6% in November 2020, down from a revised 7.5% in October 2020, and substantially greater than the year-ago estimate of 2.9%. This compares with an unadjusted unemployment rate of 7.9% for California and 6.5% for the nation during the same period. According to the State of California Employment Development Department, San Diego County gained 14,300 jobs between October 2020 and November 2020. With the normal delay in reporting from the California EDD, employment figures from December were unavailable at the time of publishing this report. In December, the employment data for the United States as a whole came in with 140,000 jobs lost, which was the first month of net job losses for the nation since April 2020.



Forecast

Given the fact that the year ended with additional pandemic restrictions on business, current market trends are expected to continue well into 2021. We expect negative absorption to continue, as expansion plans are put on hold and business owners take a hard look at how much space they will need when their current leases expire. The construction pipeline will add additional vacant space to the market in 2021 which will place increased pressure on the occupancy rate. Landlords will continue to offer incentives to increase occupancy in the current real estate environment. Technology was already reshaping the workplace before the pandemic hit, and the pandemic ensures that change will continue throughout the coming year.

Significant Transactions

Sales † Plus Excess Land

Property Address	Submarket	Class	Square Feet	Sale Price	Buyer	Seller
6420 & 6450 Sequence Dr.	Sorrento Mesa	A	321,471	\$185,000,000	Alexandria Real Estate Equities	Cruzan Invesco Advisers
9276 & 9330 Scranton Rd.	Sorrento Mesa	A	280,631	\$130,000,000 †	Longfellow Real Estate Partners	Shorenstein Properties, LLC
1155 Island Ave.	Downtown	A	185,000	\$43,500,000	Bain Capital Real Estate, LP	Barings Miller Global Properties, LLC
4765 Carmel Mountain Rd.	Del Mar Heights/ Carmel Valley	A	47,596	\$37,911,500	Healthcare Realty Trust, Inc.	Coast Income Properties
5959 Cornerstone Ct. W.	Sorrento Mesa	B	47,345	\$14,203,500	AYA Healthcare	Buchanan Street Partners

Leases

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
4810 Eastgate Mall	UTC	B	94,542	Nov-2020	Service Now	The Irvine Company
9808 Scranton Rd.	Sorrento Mesa	A	34,295	Oct-2020	Plaza Home Mortgage	Alexandria Real Estate
4181 Ruffin Rd.	Kearny Mesa	B	29,503	Dec-2020	AIMLoan	IDS Real Estate
13500 Evening Creek Dr. N.	Rancho Bernardo	A	26,143	Oct-2020	Daybreak	(Sublease)
240 S. Cedros Ave.	North Beach Cities	B	20,162	Oct-2020	Undisclosed	American Brewing Company

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 4Q2020	Square Feet Available	Availability Rate 4Q2020	Average Asking Lease Rate	Net Absorption 4Q2020	Net Absorption 2020	Gross Absorption 4Q2020	Gross Absorption 2020
Downtown													
Downtown	128	13,518,130	1,069,366	2,407,000	2,606,205	19.28%	4,413,951	32.65%	\$2.91	267,624	(25,715)	528,842	960,325
Downtown Total	128	13,518,130	1,069,366	2,407,000	2,606,205	19.28%	4,413,951	32.65%	\$2.91	267,624	(25,715)	528,842	960,325
Central													
City Heights / University	30	1,205,489	0	0	69,428	5.76%	108,904	9.03%	\$2.18	(4,223)	(24,125)	2,285	28,952
Coronado	5	111,541	0	0	2,732	2.45%	2,732	2.45%	\$4.50	0	(1,500)	0	300
Kearny Mesa	241	11,378,146	0	60,186	1,376,163	12.09%	1,440,012	12.66%	\$2.54	583	(323,159)	342,022	624,216
Mission Gorge	19	581,130	0	0	4,421	0.76%	7,664	1.32%	\$1.62	(878)	1,587	0	8,612
Mission Valley	126	7,267,935	0	0	1,102,845	15.17%	1,234,253	16.98%	\$2.76	(352,910)	(446,142)	35,873	431,070
Old Town / Point Loma	78	2,406,951	0	230,000	116,838	4.85%	254,217	10.56%	\$2.84	(31,482)	(36,902)	23,342	86,680
Park East	16	234,322	0	0	13,940	5.95%	33,782	14.42%	\$2.09	2,504	6,368	5,874	23,465
Rose Canyon / Morena	56	1,297,671	0	0	77,338	5.96%	128,949	9.94%	\$2.06	18,828	(6,996)	30,031	72,005
Uptown / Hillcrest	79	2,242,003	0	0	194,432	8.67%	287,342	12.82%	\$2.62	(8,788)	(78,922)	15,158	57,573
Central Total	650	26,725,188	0	290,186	2,958,137	11.07%	3,497,855	13.09%	\$2.60	(376,366)	(909,791)	454,585	1,332,873
I-15 Corridor													
Escondido	76	1,778,215	0	46,614	203,617	11.45%	301,779	16.97%	\$2.01	14,622	33,016	38,500	137,101
Poway	31	1,384,913	0	0	50,869	3.67%	103,933	7.50%	\$2.23	(16,403)	(32,439)	1,185	10,891
Rancho Bernardo	103	6,778,348	0	2,782,719	880,239	12.99%	1,038,201	15.32%	\$2.98	(17,851)	(231,110)	57,569	275,643
Scripps Ranch	53	2,916,228	0	356,000	535,235	18.35%	470,978	16.15%	\$2.87	(63,840)	(55,187)	13,857	99,260
I-15 Corridor Total	263	12,857,704	0	3,185,333	1,669,960	12.99%	1,914,891	14.89%	\$2.82	(83,472)	(285,720)	111,111	522,895
North County Coastal													
Carlsbad	164	6,904,261	0	50,000	1,051,563	15.23%	1,356,593	19.65%	\$2.69	106,746	45,249	228,806	626,260
Del Mar Heights / Carmel Valley	79	5,103,359	217,235	416,955	703,594	13.79%	1,295,198	25.38%	\$4.23	100,141	255,276	182,989	591,550
North Beach Cities	113	2,677,062	72,177	120,456	229,842	8.59%	366,620	13.69%	\$3.68	(15,908)	(70,325)	40,528	144,855
North County Total	356	14,684,682	289,412	587,411	1,984,999	13.52%	3,018,411	20.55%	\$3.31	190,979	230,200	452,323	1,362,665
North City													
Governor Park	20	899,234	0	0	144,988	16.12%	167,973	18.68%	\$2.64	(33,520)	(64,886)	9,971	43,706
La Jolla	45	1,328,629	0	0	261,103	19.65%	283,354	21.33%	\$3.32	(120)	(80,026)	15,320	42,183
Miramar	32	1,451,242	0	0	78,531	5.41%	157,704	10.87%	\$1.98	10,895	5,043	17,064	76,722
Sorrento Mesa	118	9,467,440	0	1,501,428	1,161,464	12.27%	1,505,503	15.90%	\$3.15	(103,777)	(166,852)	124,541	531,073
Sorrento Valley	25	658,534	0	0	149,509	22.70%	165,154	25.08%	\$2.04	2,374	(68,315)	14,453	33,896
Torrey Pines	44	3,206,337	74,000	0	259,460	8.09%	251,176	7.83%	\$4.35	2,377	(53,578)	2,377	35,841
UTC	91	8,761,870	369,000	699,124	731,135	8.34%	1,362,950	15.56%	\$3.80	(113,174)	(269,473)	81,480	350,126
North City Total	375	25,773,286	443,000	2,200,552	2,786,190	10.81%	3,893,814	15.11%	\$3.25	(234,945)	(698,087)	265,206	1,113,547
Southern & Eastern Areas													
Chula Vista	90	2,840,782	0	1,203,000	193,088	6.80%	289,858	10.20%	\$2.17	(11,287)	(6,642)	13,877	110,278
National City	15	528,493	0	0	10,913	2.06%	10,913	2.06%	\$2.00	(572)	(9,919)	2,300	3,294
South San Diego	13	319,824	0	0	10,975	3.43%	10,975	3.43%	\$2.03	688	4,886	1,328	5,526
Southeast San Diego	13	460,835	0	290,000	68,167	14.79%	68,167	14.79%	\$2.03	0	10,242	0	17,227
East County	152	3,758,885	0	300,300	173,275	4.61%	198,637	5.28%	\$2.15	64,582	60,590	130,319	179,108
Southern & Eastern Areas Total	283	7,908,819	0	1,793,300	456,418	5.77%	578,550	7.32%	\$2.14	53,411	59,157	147,824	315,433
Highway 78 Corridor													
Oceanside	63	1,349,672	100,000	277,749	138,189	10.24%	176,627	13.09%	\$2.14	(34,044)	(14,047)	10,967	75,011
San Marcos	38	1,465,115	0	531,882	123,927	8.46%	184,454	12.59%	\$2.53	(9,687)	(34,208)	7,718	46,477
Vista	52	1,298,540	0	0	320,532	24.68%	370,386	28.52%	\$2.18	(7,879)	(26,112)	10,853	26,891
Highway 78 Corridor Total	153	4,113,327	100,000	809,631	582,648	14.16%	731,467	17.78%	\$2.28	(51,610)	(74,367)	29,538	148,379
Class A	303	39,471,082	1,451,601	8,153,312	6,241,318	15.81%	9,184,597	23.27%	\$3.41	(14,763)	(529,779)	1,039,552	2,626,036
Class B	1,265	51,963,289	450,177	3,120,101	5,832,433	11.22%	7,652,545	14.73%	\$2.72	(215,594)	(978,768)	806,926	2,648,479
Class C	640	14,146,765	0	0	970,806	6.86%	1,211,797	8.57%	\$2.18	(4,022)	(195,776)	142,951	481,602
San Diego County Total	2,208	105,581,136	1,901,778	11,273,413	13,044,557	12.36%	18,048,939	17.09%	\$2.95	(234,379)	(1,704,323)	1,989,429	5,756,117

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



A Tenant's Market, The Move to Amenities

by **Mike Bench**

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The word “uncertainty” was thrown around a lot following the COVID-19 outbreak in 2020, and deservedly so. There are so many things which we cannot know about an economic downturn which was not caused by typical market forces, but rather a virus and stringent government responses all over the world. This was a year that many economic analysts said “broke the charts.” We experienced a crash in the economy unlike any other before, and then in the succeeding months we saw job gains like no other time in U.S. history. At the end of the year, the U.S. is still down roughly 10 million jobs from the pre-pandemic levels, and there is still uncertainty. Let me offer one thing about the San Diego office market that you can be certain of going into 2021: we are in a tenant's market. Landlords do not like to say the words out loud, and there are still some who are in denial — possibly to their detriment. But make no mistake, we are in a tenant's market.

In 2020 the office market saw an incredible and horrific stoppage of nearly all activity. Following the stay-at-home orders, most companies hit pause and took a step back from their real estate plans. The ensuing upheaval in office market fundamentals has not finished, and we have not yet turned the corner. There is farther to fall in 2021. Downturns do not last forever, and I am optimistic about the future. But do not look for office market fundamentals like the occupancy rate to stop falling until well into 2021, or perhaps the start of 2022. We are now seeing sublease space added to the market at a rate that we have not seen in years, and there is more to come.

If you are an office landlord, I advise getting aggressive in retaining your tenants, because demand, at least for the next six months, will be similar to the last six months. When stability returns to the office market, and caution and fear are no longer in the driver's seat, don't expect things to return to normal. The office landscape has changed, and remote work has made the biggest impact. We are going to see more flexible and staggered office schedules than ever before. Companies will need less space, and even among the healthy companies, many will be shrinking their office real estate footprint.

In the last recession we saw the “flight to quality.” Get ready for the sequel, “move to amenities.” In 2021 we will see landlords that have infrastructure like outdoor common areas, touchless technology, good indoor air circulation, and the like will be best positioned to attract and retain office tenants through as long as the specter of COVID-19 lingers, and thereafter.

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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. ©2021 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