

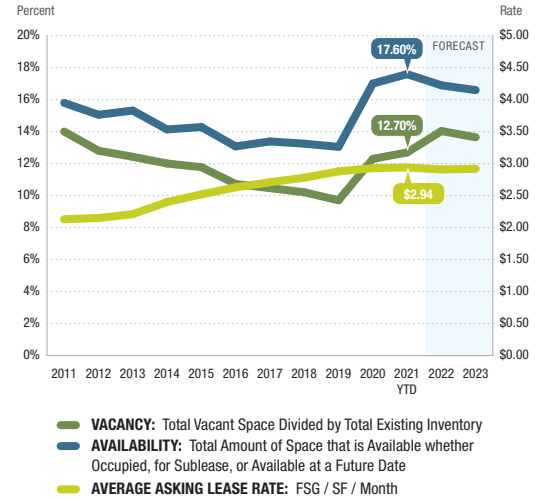
OVERVIEW. The San Diego office market has posted negative net absorption in every quarter since the end of 2019, and the development pipeline has ramped up at a very inopportune time. The total office square feet leased in 2020 was less than half the amount leased in 2019, and 1Q leasing activity was not much better, while negative absorption is on pace to exceed last year. The office market is not anywhere near the activity levels that would be considered normal just 18 months ago. The work-from-home strategy, which office users were forced to adopt, has worked better than expected, and that success has slowed progress towards a return to traditional work patterns.

VACANCY & AVAILABILITY. Direct/sublease space (unoccupied) finished the quarter at 12.70%, a 40-basis-point increase from 4Q. 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 4 MSF of inventory), UTC is now the only submarket with a vacancy rate below 10%, while the vacancy rate in Downtown is greater than 20% and the availability rate is greater than 30%. Available office space being marketed (regardless of occupancy status) was 17.09% of the county's inventory at the end of the 1Q, a four-percentage-point increase over 1Q 2020's rate, and a substantial 4.9 percentage points higher than the vacancy rate. Sublease availability has increased by 734,505 SF since 1Q 2020. The sublease availability rate is currently 2.3%, the highest rate since 2009. One point for optimism was the change in sublease space in 1Q — the total square feet of sublease space available decreased by 35,000 SF. On the flip side, more than 100 new office sublease availabilities came onto the market in 1Q.

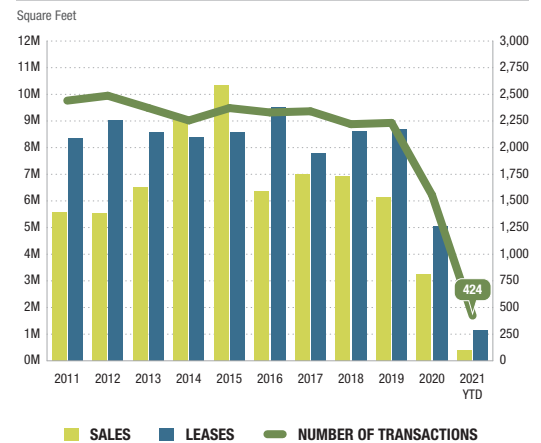
LEASE RATES. The average asking full-service-gross (FSG) lease rate per square foot per month in San Diego County was \$2.94 at the end of 1Q, which is a one-cent increase over the prior quarter, and an annual increase of 0.34% from 1Q 2020's rate of \$2.93. Asking rates do not tell the whole story, 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. Landlords face the daunting prospect of operating in an environment of decreased demand for office space, while also competing with sublease availability. This is a very competitive environment, and effective rates are reflecting that.

TRANSACTION ACTIVITY. Sale and lease transactions totaled 1.6 MSF in 1Q, a decrease from last quarter's 2.4 MSF leased and sold, and a major decline from the 3.2 MSF which transacted in 1Q 2020. Near-term uncertainty has caused a rise in short-term renewals. Speculation over how office space will be used in the future is in the headlines every day and that has business owners confused and uncertain about how they should adapt their operations to reflect what could be long-term changes in the way they do business. Until that becomes clearer, transaction activity will be negatively impacted.

VACANCY, AVAILABILITY & AVERAGE ASKING LEASE RATES



TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



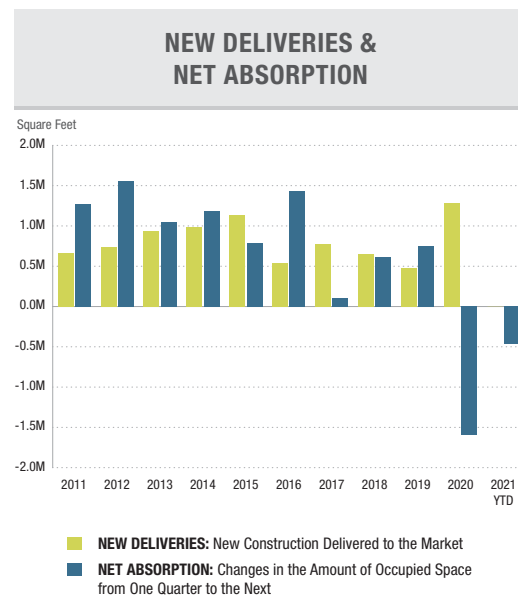
Market Statistics

	Change Over Last Quarter	1Q 2021	4Q 2020	1Q 2020	% Change Over Last Year
Vacancy Rate	▲ UP	12.70%	12.30%	10.12%	25.56%
Availability Rate	▲ UP	17.60%	17.01%	13.14%	33.96%
Average Asking Lease Rate	▲ UP	\$2.94	\$2.93	\$2.93	0.34%
Sale & Lease Transactions	▼ DOWN	1,551,384	2,364,409	3,234,707	(52.04%)
Gross Absorption	▼ DOWN	1,122,368	1,988,101	1,388,107	(19.14%)
Net Absorption	▼ NEGATIVE	(465,143)	(263,927)	-384,671	N/A

ABSORPTION. The San Diego office market recorded 465,143 SF of negative net absorption in 1Q, following a total of 1,602,660 SF of negative net absorption in 2020, which was the first calendar year of negative absorption since 2008. Downtown recorded the most negative absorption in 1Q with a net total of 167,953 SF of occupier contraction.

CONSTRUCTION. The office market has 2.1 MSF under construction at the end of 1Q. Prior to 2020, the San Diego office market had not had more than 2 MSF under construction since 2008. The largest ground-up speculative office projects under construction include Kilroy Realty's 234,000 SF "2100 Kettner" project in Little Italy, and Lincoln Property Company's 217,000 SF phase one of "Aperture Del Mar" on the Highway 56 Corridor.

EMPLOYMENT. The unemployment rate in San Diego County was 7.2% in February 2021, down from a revised 8.0% in January 2021, and substantially greater than the year-ago estimate of 3.2%. This compares with an unadjusted unemployment rate of 8.4% for California and 6.6% for the nation during the same period. According to the State of California Employment Development Department, San Diego County gained 31,900 jobs between January 2021 and February 2021. Over the 12-month period between February 2020 and February 2021, San Diego County employment fell by 131,700 jobs, or 8.7%. With the normal delay in reporting from the California EDD, employment figures from March were unavailable at the time of publishing this report. The jobs report for the U.S. overall showed a gain of 916,000 jobs in March, the largest monthly increase of jobs since August.



Forecast

Within less than a month of this report being published all California adults will be eligible to get a COVID-19 vaccine, and the Governor has announced the intention to have the California economy "fully reopen" before the end of 2Q. U.S. Treasury Secretary Janet Yellen recently predicted a return to full employment in 2022. Based upon these and other predictions from prominent analysts, the economy is projected to have a period of strong growth for at least the upcoming 12-18 months. As conditions improve, the office sector will experience some bounce-back as companies feel more comfortable making real estate commitments. However, the landscape for the office sector has been reshaped this past year, and we do anticipate some portion of office employees will continue to work remotely even as everything opens back up. This will likely lead to less demand for office space and some continued negative net absorption, at least in the short run. The local office market will remain a tenant's market even as restrictions are lifted. 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 2021.

Significant Transactions

Sales * Voit Real Estate Services Deal

Property Address	Submarket	Class	Square Feet	Sale Price	Buyer	Seller
2130 W. Citracado Pkwy.	Escondido	A	80,064	\$53,600,000	Harrison Street Capital	JRMC Real Estate
11440 W Bernardo Ct.*	Rancho Bernardo	A	98,249	\$33,000,000	Peregrine Realty Partners	Carleton Management*
5889-5897 Oberlin Dr.	Sorrento Mesa	B	62,424	\$25,750,000	Longfellow Real Estate Partners	Crown Realty and Development
330 Lewis St.	Uptown / Hillcrest	B	22,461	\$17,150,000	Healthcare Realty Trust, Inc.	Coast Income Properties
765 3rd Ave.	Chula Vista	A	42,290	\$8,500,000	Aroga Real Estate, LLC	Olvera Plaza, LLC

Leases

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
4810 Eastgate Mall	UTC	B	48,293	Mar-2021	Undisclosed	(Sublease)
7825 Fay Ave.	La Jolla	A	23,729	Feb-2021	Prospect Home Finance	PERA 7825 Fay Avenue, Inc.
9255 Towne Centre Dr.	UTC	A	16,737	Jan-2021	Undisclosed	The Irvine Company
9640 Towne Centre Dr.	UTC	B	16,607	Jan-2021	Bionano Genomics	The Irvine Company
1800 Aston Ave.	Carlsbad	A	16,162	Mar-2021	Undisclosed	Burke Aston Partners, LLC

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 1Q2021	Square Feet Available	Availability Rate 1Q2021	Average Asking Lease Rate	Net Absorption 1Q2021	Net Absorption 2021	Gross Absorption 1Q2021	Gross Absorption 2021
Downtown													
Downtown	128	13,537,563	1,069,492	2,402,000	2,774,158	20.49%	4,588,449	33.89%	\$2.88	(167,953)	(167,953)	78,599	78,599
Downtown Total	128	13,537,563	1,069,492	2,402,000	2,774,158	20.49%	4,588,449	33.89%	\$2.88	(167,953)	(167,953)	78,599	78,599
Central													
City Heights / University	30	1,202,320	0	0	67,263	5.59%	107,939	8.98%	\$2.21	2,165	2,165	8,725	8,725
Coronado	6	133,926	0	0	4,942	3.69%	4,642	3.47%	\$3.89	(2,210)	(2,210)	0	0
Kearny Mesa	242	11,401,308	0	60,186	1,428,031	12.53%	1,549,509	13.59%	\$2.52	(51,868)	(51,868)	104,569	104,569
Mission Gorge	19	581,130	0	0	1,793	0.31%	9,251	1.59%	\$1.62	2,628	2,628	2,628	2,628
Mission Valley	126	7,267,887	0	1,130,925	1,110,957	15.29%	1,296,574	17.84%	\$2.73	(8,112)	(8,112)	124,535	124,535
Old Town / Point Loma	77	2,394,771	0	230,000	153,319	6.40%	333,411	13.92%	\$2.83	(36,481)	(36,481)	17,548	17,548
Park East	16	234,322	0	0	7,001	2.99%	23,653	10.09%	\$2.38	6,939	6,939	8,484	8,484
Rose Canyon / Morena	56	1,297,671	0	0	86,616	6.67%	141,481	10.90%	\$1.94	(9,278)	(9,278)	8,538	8,538
Uptown / Hillcrest	79	2,242,003	0	0	197,669	8.82%	291,650	13.01%	\$2.66	(3,237)	(3,237)	13,889	13,889
Central Total	651	26,755,338	0	1,421,111	3,057,591	11.43%	3,758,110	14.05%	\$2.58	(99,454)	(99,454)	288,916	288,916
I-15 Corridor													
Escondido	75	1,761,051	0	46,614	210,666	11.96%	247,760	14.07%	\$2.03	(7,049)	(7,049)	68,139	68,139
Poway	31	1,384,913	0	0	50,147	3.62%	102,960	7.43%	\$2.21	722	722	21,314	21,314
Rancho Bernardo	103	6,784,806	0	2,835,094	881,315	12.99%	1,228,520	18.11%	\$2.83	(1,076)	(1,076)	75,539	75,539
Scripps Ranch	53	2,915,214	0	356,000	559,761	19.20%	508,747	17.45%	\$2.87	(25,540)	(25,540)	7,396	7,396
I-15 Corridor Total	262	12,845,984	0	3,237,708	1,701,889	13.25%	2,087,987	16.25%	\$2.72	(32,943)	(32,943)	172,388	172,388
North County Coastal													
Carlsbad	164	6,907,548	0	50,000	1,081,759	15.66%	1,413,121	20.46%	\$2.67	(30,196)	(30,196)	57,737	57,737
Del Mar Heights / Carmel Valley	79	5,103,366	228,662	418,833	822,581	16.12%	1,440,066	28.22%	\$4.28	(118,987)	(118,987)	61,253	61,253
North Beach Cities	113	2,720,562	62,177	25,456	235,946	8.67%	389,777	14.33%	\$3.62	(8,600)	(8,600)	50,156	50,156
North County Total	356	14,731,476	290,839	494,289	2,140,286	14.53%	3,242,964	22.01%	\$3.37	(157,783)	(157,783)	169,146	169,146
North City													
Governor Park	20	899,234	0	0	149,983	16.68%	178,639	19.87%	\$2.66	(4,995)	(4,995)	15,654	15,654
La Jolla	45	1,328,629	0	0	240,601	18.11%	239,662	18.04%	\$3.30	20,502	20,502	56,414	56,414
Miramar	32	1,451,242	0	0	101,077	6.96%	200,564	13.82%	\$2.06	(22,546)	(22,546)	6,745	6,745
Sorrento Mesa	116	9,361,751	194,910	1,325,000	1,013,137	10.82%	1,440,700	15.39%	\$2.96	49,279	49,279	128,643	128,643
Sorrento Valley	25	658,534	0	0	158,076	24.00%	135,509	20.58%	\$2.09	(8,567)	(8,567)	2,500	2,500
Torrey Pines	44	3,194,830	74,000	0	234,258	7.33%	152,641	4.78%	\$4.42	25,202	25,202	25,281	25,281
UTC	91	8,750,913	369,000	705,975	818,682	9.36%	1,249,473	14.28%	\$3.84	(87,547)	(87,547)	47,311	47,311
North City Total	373	25,645,133	637,910	2,030,975	2,715,814	10.59%	3,597,188	14.03%	\$3.20	(28,672)	(28,672)	282,548	282,548
Southern & Eastern Areas													
Chula Vista	91	2,852,717	0	1,203,000	196,365	6.88%	308,193	10.80%	\$2.39	(3,277)	(3,277)	27,733	27,733
National City	15	528,493	0	0	10,177	1.93%	5,160	0.98%	\$2.00	736	736	736	736
South San Diego	13	319,824	0	0	10,975	3.43%	10,975	3.43%	\$2.03	0	0	0	0
Southeast San Diego	13	460,835	0	290,000	63,266	13.73%	63,266	13.73%	\$2.03	4,901	4,901	4,901	4,901
East County	152	3,767,329	0	300,300	151,593	4.02%	197,877	5.25%	\$2.21	21,682	21,682	34,340	34,340
Southern & Eastern Areas Total	284	7,929,198	0	1,793,300	432,376	5.45%	585,471	7.38%	\$2.29	24,042	24,042	67,710	67,710
Highway 78 Corridor													
Oceanside	63	1,349,672	100,000	277,749	142,279	10.54%	184,472	13.67%	\$2.16	(4,090)	(4,090)	11,155	11,155
San Marcos	38	1,465,135	0	1,447,462	117,498	8.02%	177,140	12.09%	\$2.53	6,429	6,429	28,637	28,637
Vista	53	1,309,540	0	0	327,487	25.01%	354,270	27.05%	\$2.21	(4,719)	(4,719)	23,269	23,269
Highway 78 Corridor Total	154	4,124,347	100,000	1,725,211	587,264	14.24%	715,882	17.36%	\$2.29	(2,380)	(2,380)	63,061	63,061
Class A	305	39,608,856	1,658,064	9,255,921	6,460,396	16.31%	9,549,994	24.11%	\$3.45	(193,712)	(193,712)	352,788	352,788
Class B	1,263	51,846,061	440,177	3,848,673	6,000,692	11.57%	7,838,767	15.12%	\$2.67	(293,947)	(293,947)	623,039	623,039
Class C	640	14,114,122	0	0	948,290	6.72%	1,187,290	8.41%	\$2.10	22,516	22,516	146,541	146,541
San Diego County Total	2,208	105,569,039	2,098,241	13,104,594	13,409,378	12.70%	18,576,051	17.60%	\$2.94	(465,143)	(465,143)	1,122,368	1,122,368

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



Change is Coming to the Office

by **Connor Wieck**

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With the effects of the COVID-19 pandemic lingering, the jury is still out on which nascent office market trends will persist in San Diego. Headlines continue to surface of large companies in dense metropolitan areas pulling back on the amount of office space required for their company's operations. However, San Diego seems to be following an alternate narrative.

The life sciences industry is the elephant in the room. Owners of real estate are setting their sights on various opportunities to capture the demand for life science occupiers. The biotech and life science industries in San Diego are growing at a rapid pace and investors are acting quickly with a focus on how they can corner this demand in the market. As this change in emphasis occurs a natural balance will follow as the supply of office is reduced beyond the overall reduction of demand from COVID-19. Capital Markets will continue their adjustments as they monitor the sectors they want to target. As it relates to office in particular, capital will be allocated first to the most stable assets and core markets. As the market begins to stabilize, that capital will begin to reach toward riskier assets with larger upside opportunities.

Tenants are focused on obtaining concessions and ensuring the workplace environment is clean and safe, and maximizes employee well-being. Onsite and walkable amenities will drive tenants to make changes to accommodate the flexibility that is being introduced into the new standard for a working routine. The pandemic has undoubtedly focused attention on the importance of maximizing health and wellness, which can largely be achieved in amenity-rich office buildings.

For landlords, the top priority is occupancy. That means landlords must focus their attention on what it will take to attract new tenants and to retain existing tenants. Properties must be competitive with their offerings, and landlords will need to stretch to win deals. This will help stabilize the asset for the property owner until they get into a better leasing market.

From a macro perspective, San Diego has a tremendous opportunity to outpace the recovery of the other large metropolitan office markets. The pandemic has illustrated that there are alternatives in how businesses function and operate within commercial space. An increase in the efficiency of transit services, companies pushing toward suburban markets and a focus on health and wellness within the workplace will open opportunities that were not present before. The market will continue to adapt, and San Diego will continue to cement its position as a leading performer in the push for a new way of work life.

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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