

**OVERVIEW.** 3Q was the second consecutive quarter without negative net absorption in the San Diego office market since the start of 2020, indeed, the office market has moved into positive net absorption for the year. Leasing activity reached pre-pandemic levels for the first time in 3Q. Average asking rental rates have not gone down on the top line, but net effective rental rates are certainly depressed as leasing concessions have increased across the board. The market appears to have begun its recovery, but it was a rapid descent in 2020. Much like (and not unrelated to) the employment levels, the climb back to where things were is not happening as quickly as the decline.

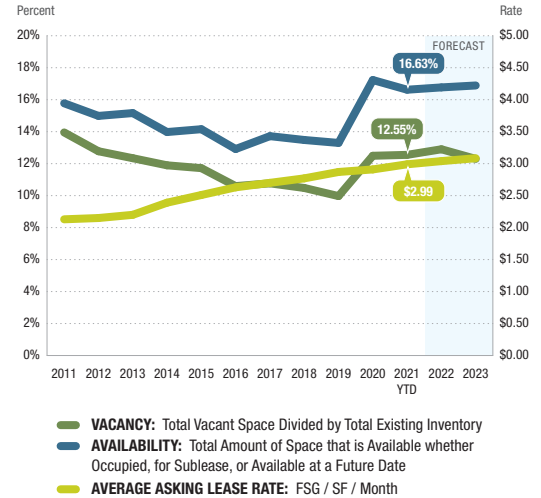
**VACANCY & AVAILABILITY.** Direct/sublease space (unoccupied) finished the quarter at 12.55%, a massive 4.4 percentage-point increase from the prior year's total. The post-pandemic office market saw the past seven years' worth of occupancy gains wiped out in 2020. Vacancy peaked at 12.9% in 1Q and has since inched down by 35 basis points over the past two quarters. Among the county's major submarkets (minimum of 4 MSF of inventory), Sorrento Mesa is now the only submarket with a vacancy rate below 10%, another indicator of the growth of the biotech sector. Meanwhile the vacancy rate in Downtown is now greater than 20% and the availability rate there is greater than 30%. Available office space being marketed (regardless of occupancy status) was 16.63% of the county's inventory at the end of the 3Q. Sublease availability averaged 1.62 MSF per quarter in the two years leading up to COVID. In 4Q 2020 sublease availability peaked at 2.39 MSF and has since receded to 1.81 MSF at the end of 3Q.

**LEASE RATES.** The average asking full-service-gross (FSG) lease rate per square foot per month in San Diego County was \$2.99 at the end of 3Q, which is a 2.31% increase from 3Q 2020'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. The surge in new construction also increases the proportion of high-end office space, pushing up the county's average asking rental rate. The concessions being given by landlords are much more indicative of office tenants' leverage in the market than the stated rental rates.

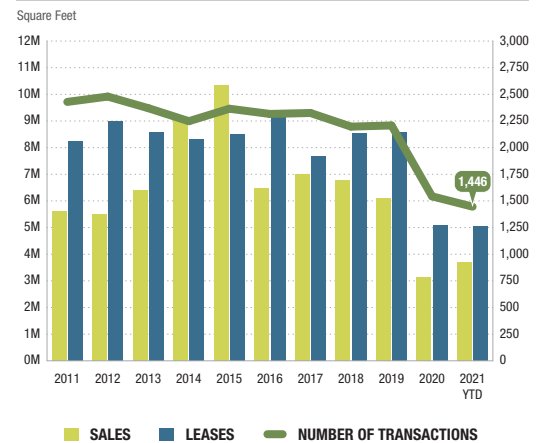
**TRANSACTION ACTIVITY.** Sale and lease transactions totaled 3.6 MSF in 3Q, with a leasing activity of 1.96 MSF. This was the largest quarterly total since mid-2019 and is in line with pre-pandemic activity levels. This is a positive sign that office users are getting more comfortable their plans. Last year many of the office tenants with expiring leases opted for short-term extensions, so many of those leases are coming back up. The majority of the largest sales and leases of the past quarter involved biotech or medical uses. Not to be left out, high-tech companies accounted for three of the top five leases in 3Q.

**ABSORPTION.** There were 369,340 SF of positive net absorption in 3Q which was enough to move the 2021 year-to-date total into positive territory. The San Diego County office occupier base has grown by a net total of 153,242 SF through the first three quarters. This is a positive

### VACANCY, AVAILABILITY & AVERAGE ASKING LEASE RATES



### TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



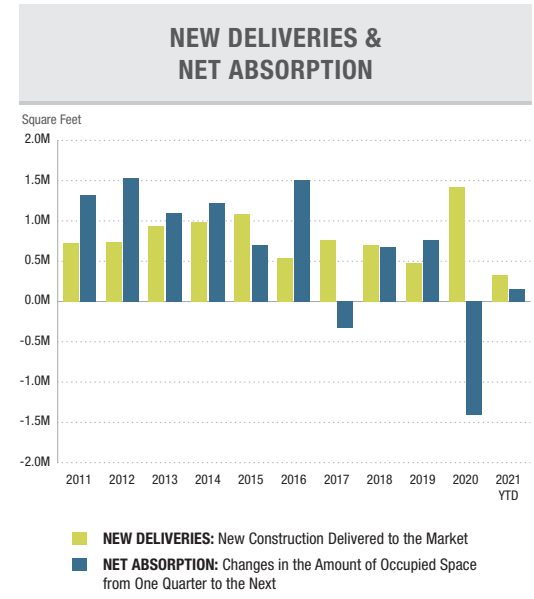
### Market Statistics

	Change Over Last Quarter	3Q 2021	2Q 2021	3Q 2020	% Change Over Last Year
Vacancy Rate	▼ DOWN	12.55%	12.83%	12.02%	4.39%
Availability Rate	▼ DOWN	16.63%	17.13%	16.25%	2.31%
Average Asking Lease Rate	▲ UP	\$2.99	\$2.98	\$2.90	3.10%
Sale & Lease Transactions	▼ DOWN	3,547,659	4,972,224	1,174,708	202.00%
Gross Absorption	▲ UP	1,970,744	1,791,078	1,260,822	56.31%
Net Absorption	▲ POSITIVE	369,340	234,570	(668,768)	N/A

sign but does not put the market on pace to recover from the 1.4 MSF of negative net absorption in 2021. The Class A office market is driving all of the positive net absorption, with Class B and Class C offices accounting for 301,783 SF of negative net absorption through three quarters.

**CONSTRUCTION.** The office market has 2.4 MSF under construction at the end of 3Q. Approximately two thirds of the office space under construction is located in Downtown. The current office vacancy rate in Downtown of 24% hasn't dampened the long-term optimism for the submarket. Kilroy Realty, IQHQ, and Stockbridge, who have large projects underway in Downtown, have all stated that they are looking to attract high-tech or biotech tenants, which have not historically been a significant driver of demand in Downtown. Holland Partners is also taking an untraditional approach with their current downtown development Courthouse Commons. This project at the site of the former San Diego County Courthouse will be a unique mixed-use project with ground-floor retail, office on floors 2-8, amenities on floor 9, and apartments on floors 10-37.

**EMPLOYMENT.** The unemployment rate in San Diego County was 6.6% in August 2021, down from a revised 6.9% in July 2021, and below the year-ago estimate of 10.8%. This compares with an unadjusted unemployment rate of 7.5% for California and 5.3% for the nation during the same period. Over the 12-month period between August 2020 and August 2021, San Diego County employment increased by 59,200 jobs, or 4.4%. With the normal delay in reporting from the California EDD, employment figures from September were unavailable at the time of publishing this report. At the end of September, the 4-week average of initial unemployment claims in the U.S. dropped to 336,000, the lowest figure since the start of the pandemic. The total employment for the U.S. is still 5.3 million jobs fewer than the pre-pandemic level.



## Forecast

During 2Q all California adults became eligible to get a COVID-19 vaccine, and California lifted most COVID-19 restrictions two weeks before the end of July. Coming into 3Q, optimism was at the highest level it had been since the onset of COVID-19. Then the Delta variant came in and put a damper on the recovery. Many of the largest office occupiers in the U.S. postponed their return to office plans once the Delta variant sent case counts back up. These large companies tend to be among the most conservative in their human resources plans. One sign of long-term optimism was while Apple announced a delay in their return to office plans, they simultaneously continued to lease large office blocks in San Diego. The freefall in the office market is over, and the road forward has begun. The speed of the office recovery will be dependent upon how effectively COVID-19 can be curtailed.

## Significant Transactions

### Sales

\* Voit Real Estate Services Deal

Property Address	Submarket	Class	Square Feet	Sale Price	Buyer	Seller
5355 & 5375 Mira Sorrento Pl.	Sorrento Mesa	A	296,327	\$146,000,000	Prime US REIT	Shorenstein Properties
5717 Pacific Center Blvd.	Sorrento Mesa	B	67,832	\$46,650,000	BioMed Realty	Montana Avenue Capital Partners
12250 El Camino Real	Del Mar Heights	A	74,620	\$34,825,000	Phase 3 RE Partners	Meissner Jacquet
2067 W Vista Way	Vista	B	54,703	\$26,750,000	Anchor Health Properties/The Carlyle Group	AmeriCare Medical Properties
3444 Kearny Villa Rd.	Kearny Mesa	B	38,665	\$22,970,000	Remedy Medical Properties	Kayne Anderson Real Estate

Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
12400 High Bluff Dr.	Del Mar Heights	A	181,949	Sept-2021	Tandem Diabetes	Kilroy Realty Corp.
12340 El Camino Real	Del Mar Heights	A	95,997	Jul-2021	DermTech	Kilroy Realty Corp.
4401 Eastgate Mall	UTC	A	92,446	Aug-2021	Apple	The Irvine Company
5759 Fleet St.	Carlsbad	B	82,163	Sept-2021	Rockstar Games	Drawbridge Realty
4747 Executive Dr.	UTC	A	73,176	Sept-2021	Apple	(Sublease)

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 3Q2021	Square Feet Available	Availability Rate 3Q2021	Average Asking Lease Rate	Net Absorption 3Q2021	Net Absorption 2021	Gross Absorption 3Q2021	Gross Absorption 2021
<b>Downtown</b>													
Downtown	128	13,671,840	1,591,198	2,065,000	3,231,517	23.64%	5,026,616	36.77%	\$2.90	(59,810)	(270,197)	110,891	432,816
Downtown Total	128	13,671,840	1,591,198	2,065,000	3,231,517	23.64%	5,026,616	36.77%	\$2.90	(59,810)	(270,197)	110,891	432,816
<b>Central</b>													
City Heights / University	31	1,217,320	0	0	50,862	4.18%	71,042	5.84%	\$2.18	19,099	33,566	32,009	66,532
Coronado	6	133,926	0	0	2,542	1.90%	2,542	1.90%	\$3.89	0	190	0	2,400
Kearny Mesa	243	11,424,707	0	60,186	1,483,392	12.98%	1,629,378	14.26%	\$2.58	(27,351)	(95,180)	75,613	281,831
Mission Gorge	19	581,130	0	0	5,561	0.96%	16,913	2.91%	\$2.25	1,793	(1,140)	3,787	6,415
Mission Valley	126	7,274,353	0	1,130,925	1,103,277	15.17%	1,320,383	18.15%	\$2.88	4,569	(2,972)	163,092	435,512
Old Town / Point Loma	76	2,373,866	0	230,000	138,192	5.82%	318,099	13.40%	\$2.69	(5,274)	(23,194)	49,262	101,385
Park East	16	234,322	0	0	4,565	1.95%	4,565	1.95%	\$2.34	0	9,375	0	10,920
Rose Canyon / Morena	56	1,297,671	0	0	77,511	5.97%	131,659	10.15%	\$2.05	16,475	(173)	26,451	41,668
Uptown / Hillcrest	78	2,176,953	0	0	209,484	9.62%	284,613	13.07%	\$2.63	(4,903)	(76,660)	31,344	80,833
Central Total	651	26,714,248	0	1,421,111	3,075,386	11.51%	3,779,194	14.15%	\$2.68	4,408	-156,188	381,558	1,027,496
<b>I-15 Corridor</b>													
Escondido	75	1,759,542	75,000	36,614	253,764	14.42%	289,490	16.45%	\$2.12	(55,944)	(50,147)	1,568	109,787
Poway	31	1,393,621	0	0	58,834	4.22%	93,527	6.71%	\$2.16	(13,080)	(7,965)	5,998	36,407
Rancho Bernardo	104	6,892,802	0	1,835,094	903,841	13.11%	1,125,949	16.34%	\$2.94	121,022	114,651	251,086	361,522
Scripps Ranch	52	2,875,843	0	531,000	389,752	13.55%	487,654	16.96%	\$2.89	(58,792)	143,939	36,326	300,426
I-15 Corridor Total	262	12,921,808	75,000	2,402,708	1,606,191	12.43%	1,996,620	15.45%	\$2.84	(6,794)	200,478	294,978	808,142
<b>North County Coastal</b>													
Carlsbad	165	6,923,014	0	50,000	1,078,424	15.58%	1,258,363	18.18%	\$2.73	(19,921)	(26,861)	117,632	374,782
Del Mar Heights / Carmel Valley	79	5,129,135	228,662	418,833	713,760	13.92%	1,244,530	24.26%	\$4.34	57,677	(10,166)	161,846	352,278
North Beach Cities	113	2,722,929	12,177	101,911	225,414	8.28%	311,595	11.44%	\$3.64	75,221	61,932	123,253	223,091
North County Total	357	14,775,078	240,839	570,744	2,017,598	13.66%	2,814,488	19.05%	\$3.38	112,977	24,905	402,731	950,151
<b>North City</b>													
Governor Park	20	899,234	0	0	152,898	17.00%	284,227	31.61%	\$2.66	9,370	(7,910)	23,736	46,180
La Jolla	45	1,331,621	0	0	189,197	14.21%	224,900	16.89%	\$3.30	44,170	71,906	58,028	140,475
Miramar	31	1,422,598	0	1,007,050	97,197	6.83%	160,294	11.27%	\$2.04	21,650	(21,370)	43,189	63,820
Sorrento Mesa	112	8,886,294	176,910	2,363,000	802,666	9.03%	1,177,458	13.25%	\$3.21	25,748	111,038	122,612	371,001
Sorrento Valley	25	669,752	0	0	153,777	22.96%	115,127	17.19%	\$2.07	12,652	(4,268)	13,830	26,812
Torrey Pines	44	3,253,939	74,000	0	191,412	5.88%	99,617	3.06%	\$4.42	15,887	68,048	33,124	85,364
UTC	92	8,901,406	204,000	682,851	905,406	10.17%	943,852	10.60%	\$3.93	107,085	(16,943)	323,535	525,039
North City Total	369	25,364,844	454,910	4,052,901	2,492,553	9.83%	3,005,475	11.85%	\$3.30	236,562	200,501	618,054	1,258,691
<b>Southern &amp; Eastern Areas</b>													
Chula Vista	91	2,849,947	0	1,035,000	166,792	5.85%	259,725	9.11%	\$2.62	24,541	26,296	34,931	92,969
National City	15	528,493	0	0	2,261	0.43%	4,284	0.81%	\$2.00	2,899	8,652	2,899	10,115
South San Diego	13	319,824	0	0	8,064	2.52%	8,064	2.52%	\$2.35	0	2,911	0	2,911
Southeast San Diego	13	460,835	0	290,000	63,266	13.73%	63,266	13.73%	\$2.06	0	4,901	0	4,901
East County	152	3,767,329	0	300,300	139,897	3.71%	157,876	4.19%	\$2.27	8,628	33,378	42,657	112,453
Southern & Eastern Areas Total	284	7,926,428	0	1,625,300	380,280	4.80%	493,215	6.22%	\$2.47	36,068	76,138	80,487	223,349
<b>Highway 78 Corridor</b>													
Oceanside	65	1,549,560	0	250,749	81,053	5.23%	107,170	6.92%	\$2.20	38,385	57,136	42,922	85,905
San Marcos	38	1,453,297	0	1,447,462	108,272	7.45%	172,635	11.88%	\$2.58	19,286	15,655	29,993	66,573
Vista	52	1,265,121	0	0	266,087	21.03%	168,236	13.30%	\$2.29	(11,742)	4,814	9,130	73,158
Highway 78 Corridor Total	155	4,267,978	0	1,698,211	455,412	10.67%	448,041	10.50%	\$2.37	45,929	77,605	82,045	225,636
Class A	309	39,889,281	2,070,770	9,947,847	5,922,656	14.85%	9,205,000	23.08%	\$3.52	420,754	455,025	1,066,231	2,320,776
Class B	1,267	51,906,190	291,177	3,888,128	6,449,364	12.43%	7,354,268	14.17%	\$2.72	(27,437)	(245,740)	733,469	2,130,973
Class C	630	13,846,753	0	0	886,917	6.41%	1,004,381	7.25%	\$2.11	(23,977)	(56,043)	171,044	474,532
<b>San Diego County Total</b>	<b>2,206</b>	<b>105,642,224</b>	<b>2,361,947</b>	<b>13,835,975</b>	<b>13,258,937</b>	<b>12.55%</b>	<b>17,563,649</b>	<b>16.63%</b>	<b>\$2.99</b>	<b>369,340</b>	<b>153,242</b>	<b>1,970,744</b>	<b>4,926,281</b>

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



## Office – What is our Future?

### by Ryan King

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As we face our new normal, the future of office space is a widely debated topic. Will “work from home” drastically affect lease rates and kill office values, or will telework and zoom calls merely be molded into a new hybrid office model? One thing is certain: the future of work will look much different as we head into 2022.

### Hybrid Work Model

Students are back in school, the summer is behind us, and more and more workers are returning to their new schedule. So where do employees want to work — do they really want to work from home? “Experts” say employees want and demand hybrid schedules, but what they really want is flexibility and choice. After being at home for the last year, employees feel like they are more productive and efficient and want to be rewarded by having the choice of when and where they will work, but they do want to come back to the office. We expect the physical office will remain the center of the work ecosystem as it reinforces culture and drives collaboration.

### Real Estate Tech & Efficiency

As companies have learned about their capacity to be agile, technology has also proven its enormous importance and value. As the hybrid models evolve, technology advancement will certainly continue to improve the workplace by accommodating flexibility. Software and digital platforms that give organizations visibility into the workforce and their physical occupancy trends will be key for the future. We are seeing tech companies implement apps that allow companies to communicate with employees, to share work schedules and accommodate meetings, and to relay information regarding COVID protocols. Employers are learning that “clocking in” is no longer an important metric but rather efficiency and actually “getting the work done” is the more significant barometer.

### Adaptive Reuse

So, what happens to the value of commercial real estate if the new hybrid model and technological advancements compromise some of the demand for office space? There is ample precedent for adaptive reuse as an engine of urban revitalization across America. Our bold prediction for San Diego is that you will continue to see some transformation of office to lab space, but that the lion’s share of office will continue to be traditional office for the foreseeable future. The San Diego office market is organized as a city of villages spanning from the border to Camp Pendleton with pockets of urban areas and office product. We expect to see lease rates remain flat with landlords able to continue paying their mortgages and make a small profit, while battling with their competition in a competitive leasing environment.

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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