

OVERVIEW. The Flex/R&D market in San Diego is driven by the biotech subset which remains strong. Vacancy and availability continue trending downward, and rental rates remain elevated from a long-term perspective. Leasing activity remains steady, while sales volume and pricing are at all-time highs. Construction is trending upwards after a lull the last two years. Net absorption was positive for the sixth consecutive quarter.

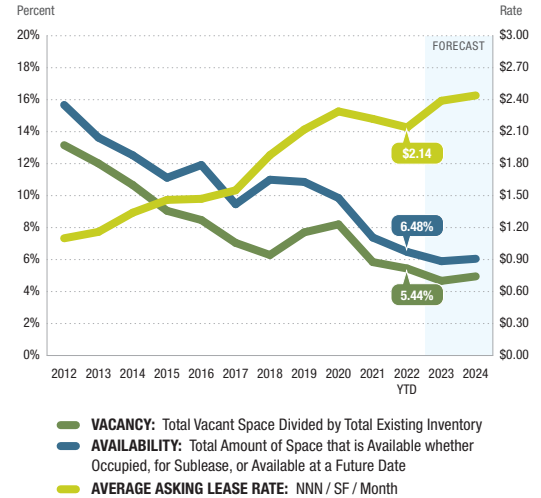
VACANCY & AVAILABILITY. Direct/sublease space (unoccupied) finished 1Q 2022 at 5.4%, a decrease of 2 percentage points from 1Q 2021's vacancy rate of 7.4%. This is an extremely low vacancy rate compared with a decade ago when the countywide vacancy rate finished 2011 above 16%. On top of that, the gap between vacancy and availability has narrowed to 1.0 percentage points, compared with a 4.8 percentage point difference at the end of 2018. Vacancy measures the amount of space which is unoccupied regardless of whether it is being marketed for sale or lease. Availability measures the amount of space which is on the market, regardless of whether it is occupied. Direct/sublease space being marketed was 6.5% at the end of 1Q. All but one of the properties under construction is preleased. This reduces the amount of space which is on the market for lease, but not physically unoccupied.

LEASE RATES. The average asking triple net lease rate per square foot per month in San Diego County was \$2.14 at the end of 1Q 2022, which is a 5.7% decrease from 1Q 2021. The average asking lease rate has been on a long-term trend of increases, but dramatic changes in the average in recent history are likely due to a change in the composition of available space. Over the past five years the countywide asking rental rate has increased an average of 8.9% per year, as more space gets built out with expensive biotech laboratories. The Flex R&D market is relatively small in comparison to the office or industrial markets, and additionally the difference between the rental rates for biotech properties and other Flex/R&D properties is vast. This causes the overall average market statistics to fluctuate periodically.

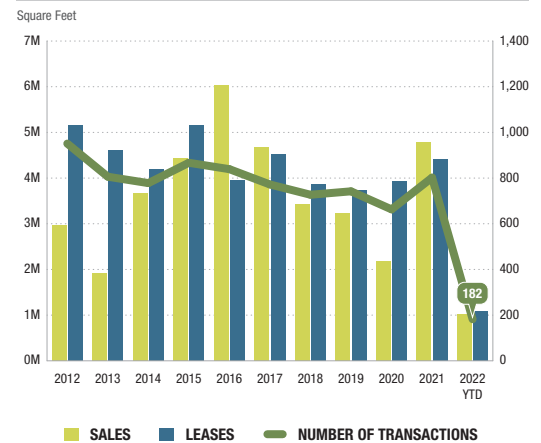
TRANSACTION ACTIVITY. The combined amount of square feet leased or sold in 1Q totaled 2.1 MSF, a 11.7% increase from the 1.9 MSF transacted in 1Q 2021. There were 1,077,468 SF of Flex/R&D space leased in 158 transactions recorded in 1Q. This is almost exactly in line with the averages of the past five years, which were 1,022,506 SF, and 157 lease transactions per quarter. The largest sale of the quarter was BioMed Realty's disposition of 643,000 SF of their local portfolio, which was acquired by Oxford Properties. This sale was a rarity because the large institutional owners of biotech real estate almost never sell. Oxford properties is the latest in a string of ownership groups entering the San Diego biotech market. There were 24 Flex R&D buildings sold in 1Q with a median price per square foot of \$507 per square foot. This was the highest quarterly median price per square foot ever recorded. The 1Q 2022 sales volume totaled \$546 million, the second highest quarterly total since 2016.

ABSORPTION. The San Diego Flex R&D market recorded 271,902 SF of positive net absorption in 1Q 2022. In 2021 there was 1.3 MSF of positive net absorption, the largest growth of the market's total tenant footprint since 2012. This is a swing back to growth in the tenant base following two

VACANCY, AVAILABILITY & AVERAGE ASKING LEASE RATES



TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



Market Statistics

	Change Over Last Quarter	1Q 2022	4Q 2021	1Q 2021	% Change Over Last Year
Vacancy Rate	▼ DOWN	5.44%	5.84%	7.40%	(26.41%)
Availability Rate	▼ DOWN	6.48%	7.38%	9.07%	(28.51%)
Average Asking Lease Rate	▼ DOWN	\$2.14	\$2.22	\$2.27	(5.73%)
Sale & Lease Transactions	▼ DOWN	2,095,837	2,856,345	1,876,626	11.68%
Gross Absorption	▼ DOWN	899,176	1,245,124	944,034	(4.75%)
Net Absorption	▲ POSITIVE	271,903	704,675	380,487	N/A

years of negative net absorption. The non-biotech segment of the Flex R&D market had been a source of negative net absorption in the market over the past two years. Many of these buildings, which lost their tenants and were acquired for biotech conversion, have now been occupied by new tenants as conversions are completed. Every submarket cluster in the county recorded positive net absorption in 1Q. The largest total of positive net absorption in any submarket came from Sorrento Mesa, which is the epicenter of the biotech conversions.

CONSTRUCTION. Last year 188,641 SF of new construction was delivered which marks the lowest annual total since 2015. At the end of 1Q 2022 the construction pipeline has picked back up with over 1 MSF currently under construction. The lack of available building sites, specifically in the primary biotech submarkets, has led to a steady stream of property conversions and repositioning over the years. These conversions do not show up in the new construction totals. The dividing line between office properties and flex properties is becoming less defined, especially in Sorrento Mesa and Sorrento Valley where there is more capital than ever chasing properties than can be converted for lab space.

EMPLOYMENT. The unemployment rate in San Diego County was 4.0% in February 2022, down from a revised 4.7% in January 2022, and below the year-ago estimate of 7.9%. This compares with an unadjusted unemployment rate of 4.8% for California and 4.1% for the nation during the same period. Over the 12-month period between February 2021 and February 2022, San Diego County employment increased by 104,300 jobs, an increase of 7.5%. With the normal delay in reporting from the California EDD, employment figures from March were unavailable at the time of publishing this report. The total employment figures for San Diego County and the U.S. are now within 1% of their pre-pandemic levels. The U.S. added an average of 562,000 jobs per month in the first quarter of 2022.

Forecast

Leasing and sales activity in 1Q was strong which should lead to positive net absorption and decreased vacancy in the coming quarters. Going forward, the competition on the sales side looks to remain fierce across the board for stabilized investment assets, as well as for user sales or biotech conversions in the submarkets surrounding UCSD. Sales prices are increasing rapidly, which will place upward pressure on rental rates, as owners strive to maintain yield levels.

Significant Transactions

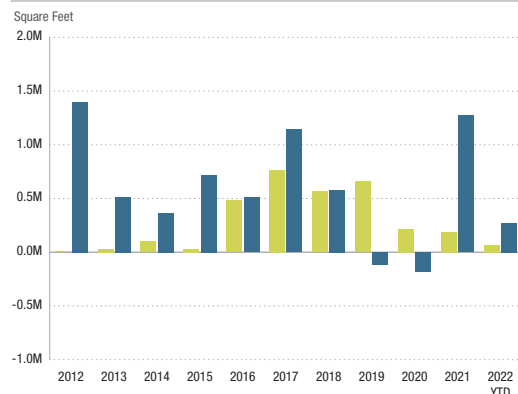
Sales

Property Address	Submarket	Square Feet	Sale Price	Buyer	Seller
5870-5880 Pacific Center Blvd., 11388-11408 Sorrento Valley Rd., 9535 Waples St., 4215 Sorrento Valley Blvd., 6114-6838 Nancy Ridge Dr., 3030 Bunker Hill St.	Sorrento Mesa / Sorrento Valley / Miramar / Pacific Beach	642,886	\$464,300,000	Oxford Properties Group	BioMed Realty
6138-6150 Nancy Ridge Dr.	Miramar	59,478	\$34,000,000	Sorrento Ridge Research Pk, LLC	Prandium, Inc.
2290 Cosmos Ct.	Carlsbad	37,328	\$9,530,000	Luminous Capital Mgmt.	Excelsior Partners, LLC
4851 Paramount Dr.	Kearny Mesa	24,614	\$9,000,000	Adamick Trust	The American Council on Exercise
11487-11491 Woodside Ave.	Santee	41,450	\$8,164,800	Woodside Investment, LLC	West Coast Cabling

Leases

Property Address	Submarket	Square Feet	Transaction Date	Tenant	Owner
Carmel Valley Rd.	Del Mar Heights / Carmel Valley	535,000	Feb-2022	Neurocrine Biosciences	Alexandria RE Equities
Campus Point Dr.	UTC	427,000	Mar-2022	Bristol Myers Squibb	Alexandria RE Equities
10931 & 10933 N. Torrey Pines Rd.	Torrey Pines	205,667	Jan-2022	Singular Genomics Systems	Alexandria RE Equities
16868 Via Del Campo Ct.	Rancho Bernardo	86,952	Feb-2022	RF Industries	Sorrento West Properties
1395 Aspen Way	Vista	81,928	Mar-2022	Undisclosed	(Sublease)

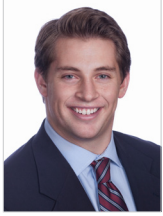
NEW DELIVERIES & NET ABSORPTION



■ NEW DELIVERIES: New Construction Delivered to the Market
 ■ NET ABSORPTION: Changes in the Amount of Occupied Space from One Quarter to the Next

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 1Q2022	Square Feet Available	Availability Rate 1Q2022	Average Asking Lease Rate	Net Absorption 1Q2022	Net Absorption 2022	Gross Absorption 1Q2022	Gross Absorption 2022
Central													
Central City	12	170,791	0	0	20,064	11.75%	31,904	18.68%	\$2.19	(2,827)	(2,827)	0	0
East City	2	26,892	346,128	0	0	0.00%	0	0.00%	-	0	0	0	0
Southeast City	22	240,994	0	0	0	0.00%	16,310	6.77%	\$1.61	5,000	5,000	5,000	5,000
Kearny Mesa	204	5,570,137	0	0	353,617	6.35%	294,853	5.29%	\$1.70	(63,211)	(63,211)	40,994	40,994
Mission Gorge	27	279,685	0	0	23,790	8.51%	31,560	11.28%	\$1.86	(6,480)	(6,480)	3,240	3,240
Rose Canyon/Morena	39	636,045	0	0	15,264	2.40%	23,361	3.67%	\$1.45	(3,698)	(3,698)	11,566	11,566
Sports Arena/Airport	32	418,986	0	0	64,939	15.50%	68,889	16.44%	\$2.17	0	0	0	0
Miramar	223	4,916,849	0	118,750	189,536	3.85%	305,499	6.21%	\$2.52	(5,730)	(5,730)	65,089	65,089
Sorrento Mesa	168	7,478,884	163,205	1,025,463	604,171	8.08%	622,108	8.14%	\$3.04	100,808	100,808	152,273	152,273
Sorrento Valley	108	2,564,534	0	0	236,854	9.24%	213,483	8.32%	\$3.39	78,898	78,898	118,478	118,478
Torrey Pines/UTC	75	6,586,401	331,368	545,666	143,643	2.18%	285,012	4.12%	\$6.79	58,435	58,435	88,290	88,290
Central County Total	912	28,890,198	840,701	1,689,879	1,651,878	5.72%	1,892,979	6.37%	\$2.64	161,195	161,195	484,930	484,930
East County													
El Cajon	78	871,152	47,878	0	27,227	3.13%	37,812	4.11%	\$1.23	1,701	1,701	10,972	10,972
La Mesa/Spring Valley	40	291,356	0	60,000	676	0.23%	676	0.23%	-	(676)	(676)	0	0
Santee/Lakeside	55	586,728	0	0	5,360	0.91%	5,360	0.91%	\$1.34	148	148	5,788	5,788
Rural East County	22	95,520	0	0	0	0.00%	0	0.00%	\$1.36	0	0	0	0
East County Total	195	1,844,756	47,878	60,000	33,263	1.80%	43,848	2.32%	\$1.26	1,173	1,173	16,760	16,760
North County													
Escondido	81	766,902	0	0	11,379	1.48%	27,151	3.54%	\$1.19	45,909	45,909	49,874	49,874
Oceanside	33	990,106	0	0	864	0.09%	77,903	7.87%	\$1.24	16,386	16,386	17,250	17,250
San Marcos	57	1,086,139	0	0	39,177	3.61%	66,390	6.11%	\$1.21	5,102	5,102	7,285	7,285
Vista	64	1,424,284	0	0	357,199	25.08%	355,264	24.94%	\$1.20	(94,612)	(94,612)	2,229	2,229
Carlsbad	262	7,158,491	0	0	375,656	5.25%	448,584	6.27%	\$1.45	57,195	57,195	156,458	156,458
North Beach Cities	20	168,171	0	0	4,032	2.40%	7,643	4.54%	\$3.50	0	0	0	0
Rural North County	19	139,572	0	0	4,600	3.30%	4,600	3.30%	\$1.00	(2,950)	(2,950)	0	0
North County Total	536	11,733,665	0	0	792,907	6.76%	987,535	8.42%	\$1.42	27,030	27,030	233,096	233,096
I-15 Corridor													
Poway	62	2,111,814	0	0	36,926	1.75%	35,063	1.66%	\$1.37	(1,690)	(1,690)	0	0
Rancho Bernardo	99	4,685,970	0	0	230,811	4.93%	280,959	6.00%	\$1.66	25,334	25,334	40,955	40,955
Scripps Ranch	29	794,196	145,000	100,000	6,253	0.79%	101,371	10.79%	\$1.89	20,380	20,380	20,380	20,380
I-15 Corridor Total	190	7,591,980	145,000	100,000	273,990	3.61%	417,393	5.39%	\$1.65	44,024	44,024	61,335	61,335
South County													
Chula Vista	82	1,454,654	0	0	80,304	5.52%	96,175	6.61%	\$1.52	18,432	18,432	78,809	78,809
National City	25	354,668	0	0	1,046	0.29%	3,296	0.93%	\$1.73	(1,046)	(1,046)	0	0
Otay Mesa	7	156,362	0	0	3,151	2.02%	3,151	2.02%	\$0.77	21,095	21,095	24,246	24,246
South San Diego	5	86,361	0	0	0	0.00%	0	0.00%	-	0	0	0	0
South County Total	119	2,052,045	0	0	84,501	4.12%	102,622	5.00%	\$1.29	38,481	38,481	103,055	103,055
San Diego County Total	1,952	52,112,644	1,033,579	1,849,879	2,836,539	5.44%	3,444,377	6.48%	\$2.14	271,903	271,903	899,176	899,176

Lease rates are on a triple-net basis.



It's Hot Out There

by **Greg Marx**

VICE PRESIDENT / PARTNER, SAN DIEGO

858.458.3302 · gmarx@voitco.com · Lic. #01940696

Building values continue to reach record levels, vacancy rates remain extremely low, and rents continue to increase across San Diego County. In the 1st quarter of 2022, we saw a bit of a slowdown in the market: leasing activity pulled back. Many tenants are having a tough time finding new locations to fit their needs. This is no surprise when some of the largest industrial submarkets, like Miramar, El Cajon, Carlsbad, and Poway, have vacancy rates of 1% or less. Not only are tenants finding few options to lease in many instances, but they're experiencing a sticker shock from current rental rates. An industrial tenant coming off of a five-year lease will find today's rates well over 50% higher than the last time they were looking at their options. The market remains a "landlord's market" as we continue to see rents rise to record levels with a reduction of concessions and downtime.

Because rental rates have been increasing to such an extent, and now we see high economy-wide inflation on top of that, gone are the days of across-the-board 3% annual escalations in leases. It's now common to see 3.5% or 4% increases in a growing number of leases. Moreover, this is not limited to the Central County areas. Otay Mesa used to be known as the best location to find a bargain rate in San Diego County, but even this submarket at the Mexican border is seeing leases with escalations above 3% now.

San Diego companies in the market to purchase a building are feeling the squeeze as well. The average price per square foot for industrial buildings was \$274 in the first quarter. Incredibly, the price per square foot has actually doubled in just the last five years. This is the overall county average--prices in some areas are much higher. Kearny Mesa is now seeing industrial sales that exceed \$400 per square foot. And rising interest rates promise to exacerbate the situation.

Despite the dramatic increase in rental rates and sales prices, there is still an imbalance between supply and demand with occupancy rates so high across the county. We anticipate that 2022 will continue to experience upward pressure on rents, with concessions such as free rent and tenant improvement packages all but disappearing because the occupancy levels continue to remain high. San Diego's diverse employment base, its wonderful climate, proximity to Mexico and the Pacific Rim all help support our local economy's continued growth, with only a lack of existing and new industrial inventory standing in the way.

Product Type

MFG./DIST.: Flex/Research and Development (R&D) buildings can be one story, one story with a mezzanine, and two story built-out structures with a high ratio of window wall to floor area with lower ceilings. They generally have over 50% built-out office space or laboratory use, with the remaining space being utilized as light manufacturing or warehousing. In addition, the parking ratio must be at least 3 spaces or greater per 1,000 square feet.

Submarkets

CENTRAL COUNTY

Central City, East City, Southeast City, Kearny Mesa, Mission Gorge, Rose Canyon/Morena, Sports Arena/Airport, Miramar, Sorrento Mesa, Sorrento Valley, Torrey Pines/UTC

EAST COUNTY

El Cajon, La Mesa/Spring Valley, Santee/Lakeside, Rural East County

NORTH COUNTY

Escondido, Oceanside, San Marcos, Vista, Carlsbad, North Beach Cities, Rural North County

I-15 CORRIDOR

Poway, Rancho Bernardo, Scripps Ranch

SOUTH BAY

Chula Vista, National City, Otay Mesa, South San Diego

Please Contact Us for Further Information

Joshua Brant
Regional Director of Research
jbrant@voitco.com

Anaheim, CA
714.978.7880

Carlsbad, CA
760.472.5620

Inland Empire, CA
909.545.8000

Irvine, CA
949.851.5100

Los Angeles, CA
424.329.7500

San Diego, CA
858.453.0505

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