

OVERVIEW. The San Diego industrial market tightened further in the first half of 2022 with a million square feet of positive net absorption pushing vacancy and availability rates lower. The surge in construction over the past five years has not been able to keep up with the level of demand in the market. As a result, average asking lease rates continued their ascent, rising to another record high in Q2.

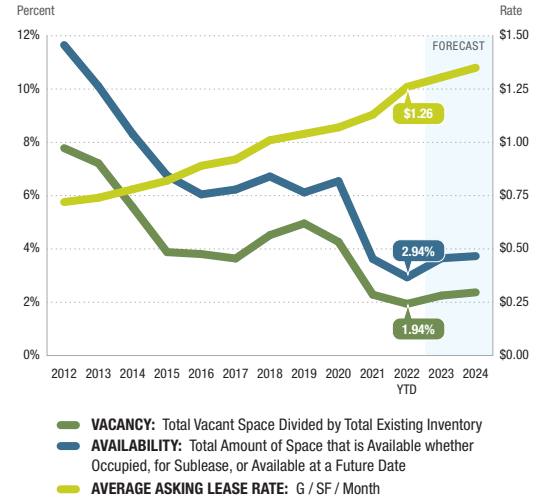
VACANCY & AVAILABILITY. Direct/sublease space (unoccupied) finished 2Q at 1.9%, a decrease of more than half from the previous year's vacancy rate of 4.0%. A large portion of this decrease can be attributed to the delivery of Amazon's build-to-suit facility in Otay Mesa in 2021. This added 3.4 MSF of occupied space to the countywide total. The availability rate decreased at an equal measure and finished 2Q 2022 at 2.9%. Ten years ago, the vacancy rate for the county as a whole was 9%. Today the vacancy rate for every submarket in the county is below 3%.

LEASE RATES. The average asking lease rate checked in at \$1.26 per square foot per month, which is an increase of nine cents per square foot over the previous quarter. Compared with 2Q last year, we see a 16.7% annual increase. By and large, negotiating leverage in the industrial market remains in the hands of the landlords, and rental rates remain elevated. Over the past decade, the average asking rental rate in San Diego has increased a total of 75%, and over the past five years the rental rates have increased at an average of 6.5% per year. In many cases, tenants with expiring leases have no alternatives in their submarket, placing the negotiating leverage squarely in the hands of landlords. In the most competitive areas, landlords are increasingly able to backfill new availabilities before the existing tenant vacates. Fixed annual rental increases are also moving up. It is now common to see landlords insist on increases of 4% per year, rather than 3%, which had been the standard for many years.

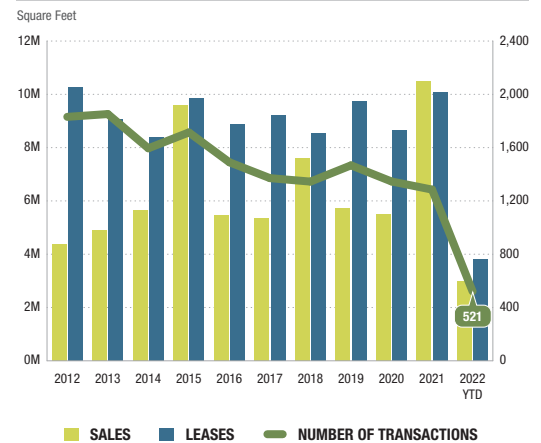
TRANSACTION ACTIVITY. The total space leased and sold in 2Q was approximately 3.8 MSF, a 34% decrease from the 5.7 MSF of transactions in 2Q 2021. There were 195 lease transactions recorded in 2Q bringing the average number of leases recorded per quarter over the last year down to 205. The preceding five years had a quarterly average of 290 lease transactions. The market is so tight there are many tenants deciding to stay in their current location rather than move to a new facility because of the lack of available options. Three of the five largest leases in 2Q were in Otay Mesa buildings. This is a direct result of Otay Mesa leading the entire county in new construction the past couple of years. Sales activity picked up in 2Q with 68 industrial buildings trading for a total of \$583.8M dollars in consideration. Record-low vacancy and record-high lease rate levels have fueled demand for investment in industrial real estate, especially as retail and office market fundamentals took a hit from COVID-19. These factors have driven the average price per square foot in industrial real estate above \$300, more than doubling over the past five years.

ABSORPTION. There were 291,044 SF of positive net absorption in 2Q 2021. The San Diego market is on track for its twelfth consecutive year of growth to the total tenant footprint. The

VACANCY, AVAILABILITY & AVERAGE ASKING LEASE RATES



TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



Market Statistics

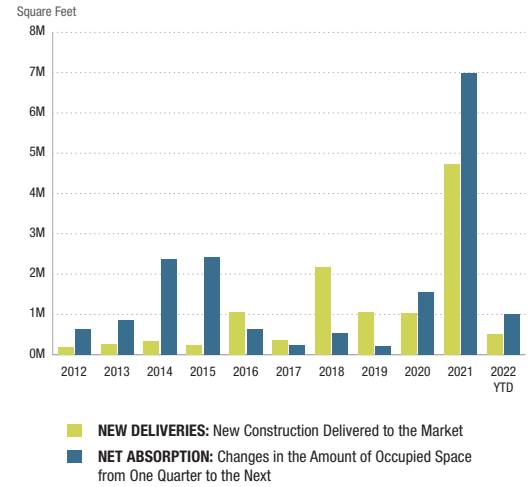
	Change Over Last Quarter	2Q 2022	1Q 2022	2Q 2021	% Change Over Last Year
Vacancy Rate	▼ DOWN	1.94%	2.08%	3.98%	(51.24%)
Availability Rate	▼ DOWN	2.94%	3.21%	4.70%	(37.51%)
Average Asking Lease Rate	▲ UP	\$1.26	\$1.17	\$1.08	16.67%
Sale & Lease Transactions	▲ UP	3,791,116	2,990,795	5,703,536	(33.53%)
Gross Absorption	▬ FLAT	1,653,832	1,677,691	2,684,554	(38.39%)
Net Absorption	▲ POSITIVE	291,044	705,287	897,492	N/A

South County and North County areas each saw over 400,000 SF of positive absorption in the first half of 2022. These areas have seen the majority of new construction over the past decade, and this growth of industrial inventory accommodates the growth of industrial tenants.

CONSTRUCTION. 4.7 MSF of new industrial projects were delivered in 2021, which was the fifth year out of the past six with more than 1 MSF of new construction completed. 1 MSF has been delivered in the first half of 2022 alone, with 1.8M more currently under construction. This is in stark contrast to the 360,000 feet per year of new construction which was the annual average from 2008 through 2015. With very little land in the central county area available for development, most new construction in the county is happening around the edges. Over the past six years there have been more than 1 MSF of new industrial development in each of South County, North County, and the I-15 Corridor, while Central County and East County combined have seen only a half a million total square feet of new development during that span. More recently, construction has been especially concentrated in Otay Mesa which accounts for 92% of the construction completions over the past 18 months, and 83% of the industrial real estate currently under construction.

EMPLOYMENT. The unemployment rate in San Diego County was 2.7% in May 2022, down from a revised 3.0% in April 2022, and below the year-ago estimate of 6.6%. This compares with an unadjusted unemployment rate of 3.4% for California and 3.4% for the nation during the same period. Over the 12-month period between May 2021 and May 2022, San Diego County employment increased by 83,900 jobs, an increase of 5.9%. With the normal delay in reporting from the California EDD, employment figures from June were unavailable at the time of publishing this report. After 27 months, the total employment figure for San Diego County finally exceeded the pre-pandemic level in 2Q.

NEW DELIVERIES & NET ABSORPTION



Forecast

The brief, but drastic, recession we saw with COVID-19 was not able to slow the growth in industrial real estate. In fact, it had the opposite effect. Going into the second half of 2022 we find ourselves in a high-inflation environment, entering a cycle of increasing interest rates. An increasing number of economic analysts are predicting recession by next year. In the short term, demand in the industrial market continues to remain strong. Over the longer horizon, a slowdown of the broader economy could have a cooling effect on the industrial market. On the sales side, rising interest rates will apply upward pressure on cap rates going forward.

Significant Transactions

Sales

Property Address	Submarket	Square Feet	Sale Price	Buyer	Seller
1205-1225 Park Center Dr., 2281 Las Palmas Dr., 120 Mata Way, Et Al	Vista Carlsbad San Marcos	614,020	\$205,500,000	BentallGreenOak	Link Logistics RE
1695 Continental St. & 7255 Otay Mesa Rd.	Otay Mesa	229,680	\$77,100,000	Hines	Murphy Development Co.
10111 Riverford Rd.	Lakeside	72,783	\$30,000,000	Costco	Southland Envelope Co.
1695 Faraday Ave.	Carlsbad	63,062	\$19,000,000	Lincoln Property Co./Angelo, Gordon & Co.	SMAC
2655 Melksee St.	Otay Mesa	66,243	\$18,298,000	Dalfen Industrial	Royal Flavor, LLC

Leases

Property Address	Submarket	Square Feet	Transaction Date	Tenant	Owner
7757 Saint Andrews Ave.	Otay Mesa	199,359	May-2022	Mad Engine	Hamann Companies
2340 Cousteau Ct.	Vista	134,299	Apr-2022	Aptera Motors	Elion
1695 Continental St.	Otay Mesa	124,223	May-2022	Home Depot	Murphy Development
8151 Airway Rd.	Otay Mesa	123,748	May-2022	Ontrac	Badiee Development
1 Viper Way	Vista	100,500	Apr-2022	Cymer	RAF Pacifica 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 2Q2022	Square Feet Available	Availability Rate 2Q2022	Average Asking Lease Rate	Net Absorption 2Q2022	Net Absorption 2022	Gross Absorption 2Q2022	Gross Absorption 2022
Central County													
Central City	87	1,384,255	0	0	10,000	0.72%	12,100	0.87%	\$1.05	26,000	26,000	36,000	36,000
East City	60	613,379	0	0	4,778	0.78%	4,778	0.78%	\$0.95	0	(4,778)	0	0
Southeast City	365	4,252,563	0	0	55,082	1.30%	102,100	2.40%	\$1.25	(7,500)	(7,989)	21,693	57,693
Kearny Mesa	418	9,545,932	315,000	202,251	153,785	1.61%	220,551	2.24%	\$1.62	28,725	37,195	86,633	157,567
Mission Gorge	106	1,745,285	0	0	6,246	0.36%	18,135	1.04%	\$1.79	12,220	(6,246)	18,466	18,466
Rose Canyon / Morena	128	1,993,572	0	0	10,040	0.50%	29,929	1.50%	\$1.31	(10,040)	52,479	0	62,519
Sports Arena / Airport	138	1,583,219	0	0	64,949	4.10%	81,479	5.15%	\$1.62	6,350	12,350	12,350	18,350
Miramar	585	13,446,049	0	0	120,087	0.89%	310,538	2.31%	\$1.47	40,691	5,492	115,374	213,276
Sorrento Mesa	70	3,282,738	0	0	47,452	1.45%	137,401	4.19%	\$1.80	(16,180)	(15,026)	15,922	23,997
Sorrento Valley/UTC	41	993,145	0	0	0	0.00%	0	0.00%	\$1.39	0	8,000	0	8,000
Central County Total	1,998	38,840,137	315,000	202,251	472,419	1.22%	917,011	2.34%	\$1.49	80,266	107,477	306,438	595,868
East County													
El Cajon	447	9,131,646	0	381,240	67,414	0.74%	101,206	1.11%	\$1.10	22,763	111,824	25,345	142,481
La Mesa / Spring Valley	314	2,695,379	0	3,000	96,232	3.57%	99,827	3.70%	\$1.14	17,326	(38,164)	53,308	69,568
Santee / Lakeside	285	3,938,163	0	0	114,094	2.90%	128,183	3.25%	\$1.37	659	18,587	19,905	56,393
Rural East County	82	822,289	0	0	1,800	0.22%	1,800	0.22%	-	(1,800)	(1,800)	0	0
East County Total	1,128	16,587,477	0	384,240	279,540	1.69%	331,016	2.00%	\$1.17	38,948	90,447	98,558	268,442
North County													
Escondido	633	7,564,861	0	62,000	153,086	2.02%	193,257	2.55%	\$1.25	(22,531)	(51,428)	69,243	103,217
Oceanside	399	9,314,087	0	400,000	97,246	1.04%	97,144	1.04%	\$1.16	18,657	19,140	96,325	185,124
San Marcos	475	8,101,572	0	223,175	293,539	3.62%	164,069	2.03%	\$1.24	26,378	146,293	70,636	212,232
Vista	527	12,989,870	0	30,165	388,499	2.99%	396,166	3.05%	\$1.18	131,264	284,023	197,338	468,548
Carlsbad	226	8,607,253	0	0	160,039	1.86%	463,078	5.38%	\$1.32	(82,042)	24,350	44,191	182,899
North Beach Cities	40	234,183	0	0	0	0.00%	0	0.00%	-	0	0	0	0
Rural North County	116	995,399	0	0	2,896	0.29%	9,296	0.93%	\$2.96	(1,016)	6,688	0	7,704
North County Total	2,416	47,807,225	0	715,340	1,095,305	2.29%	1,323,010	2.77%	\$1.23	70,710	429,066	477,733	1,159,724
I-15 Corridor													
Poway	186	7,615,028	0	0	50,471	0.66%	123,492	1.62%	\$1.35	(1,897)	(32,676)	4,279	4,279
Rancho Bernardo	41	3,238,502	0	0	20,635	0.64%	102,541	3.17%	\$1.75	(20,635)	(20,635)	0	0
Scripps Ranch	28	711,985	0	0	3,013	0.42%	31,093	4.37%	\$1.70	4,362	(3,013)	10,385	10,385
I-15 Corridor Total	255	11,565,515	0	0	74,119	0.64%	257,126	2.22%	\$1.52	-18,170	-56,324	14,664	14,664
South County													
Chula Vista	325	8,817,059	0	599,588	509,640	5.78%	496,868	5.64%	\$1.19	(325,745)	(393,443)	60,377	112,269
National City	252	3,644,115	0	80,970	33,640	0.92%	44,004	1.21%	\$1.40	14,074	65,429	14,074	79,643
Otay Mesa	357	21,172,186	1,528,524	3,614,017	435,630	2.06%	1,050,143	4.63%	\$0.95	430,161	751,959	681,188	1,098,393
South San Diego	63	1,318,244	0	24,121	4,688	0.36%	30,195	2.29%	\$0.97	800	1,720	800	2,520
South County Total	997	34,951,604	1,528,524	4,318,696	983,598	2.81%	1,621,210	4.44%	\$1.01	119,290	425,665	756,439	1,292,825
San Diego County Total	6,794	149,751,958	1,843,524	5,620,527	2,904,981	1.94%	4,449,373	2.94%	\$1.26	291,044	996,331	1,653,832	3,331,523
0-9,999	3,062	15,566,849	0	3,000	179,045	1.15%	258,256	1.66%	\$1.52	(15,106)	(25,788)	73,399	150,350
10,000-19,999	1,773	25,092,118	0	16,000	312,071	1.24%	417,665	1.66%	\$1.38	74,204	(11,923)	302,664	466,032
20,000-34,999	970	24,958,228	0	82,006	539,906	2.16%	770,912	3.09%	\$1.34	2,105	79,746	227,941	515,684
35,000-49,999	369	15,236,828	0	222,100	235,894	1.55%	389,902	2.56%	\$1.28	38,525	116,401	198,298	378,560
50,000-99,999	390	26,894,988	128,491	519,501	687,002	2.55%	1,005,652	3.72%	\$1.18	125,259	114,167	288,370	566,536
100,000 Plus	230	42,002,947	1,715,033	4,777,920	951,063	2.26%	1,606,986	3.68%	\$0.97	66,057	723,728	563,160	1,254,361
San Diego County Total	6,794	149,751,958	1,843,524	5,620,527	2,904,981	1.94%	4,449,373	2.94%	\$1.26	291,044	996,331	1,653,832	3,331,523

Lease rates are on an industrial-gross basis.

An Unstoppable Force Meets an Immovable Object

by Alex Jize and Chris Moussa



Alex Jize
VICE PRESIDENT / PARTNER
SAN DIEGO
858.458.3361
ajize@voitco.com
Lic. #01947389



Chris Moussa
ASSOCIATE
SAN DIEGO
858.458.3321
cmoussa@voitco.com
Lic. #02111997

What happens when an unstoppable force meets an immovable object? We're about to find out in the San Diego industrial market. Twelve years into the current real estate cycle, we are starting to see market conditions emerge that could begin to slow down the rapid price appreciation that we've seen over the last 18 months. Although the fundamentals are in place to help protect the industrial market from a major correction, the broader economic environment could start to impact the market.

The San Diego County industrial market has been an unstoppable force for several years now. Surging demand combined with a lack of inventory have driven the market. These have led to all-time-high property valuations, with rent growth following suit. Since the start of 2021, industrial property values have appreciated nearly 50% in San Diego County and vacancy rates have reached 2.6% county wide. These statistics illustrate just how strong demand has been. The recent economic factors of record-low interest rates and government stimulus have undoubtedly helped fuel the market.

The immovable object that the market is beginning to run into comes in the form of rising interest rates that are being used to combat decades-high levels of inflation. Wage growth, the increased costs of materials, and record gas prices, among several other factors, are driving inflation numbers not seen since 1981. In response, the Fed is raising interest rates as rapidly as possible while trying to avoid a recession. This has increased the cost of capital for both investors and owner-users.

With GDP growth at -1.6% in the first quarter of this year, it is possible that we will soon enter into a recession, by definition. A recession is defined as two consecutive quarters of negative GDP growth, which we may be on pace for after this quarter's economic data is released. Outside of the negative GDP growth caused by the pandemic in Q2-Q4 of 2020, we have not had any quarters of negative GDP growth since 2008 through 2009.

Going into the second half of the year, we will begin to see if these market dynamics have any impact on the fundamentally solid industrial market in San Diego. Common issues in downturns, such as overdevelopment and excess inventory, will not be a factor as development is currently limited outside of South County. Instead, we will watch to see if the broader economic conditions will be able to slow down the incredible momentum of the San Diego industrial real estate market.

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

This survey consists of properties representing both single tenant and multi-tenant buildings. The lease rates are based on an industrial-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

Product Type

MFG./DIST.

Manufacturing / Distribution / Warehouse facilities with up to 49.9% office space.

Submarkets

CENTRAL COUNTY

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

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