

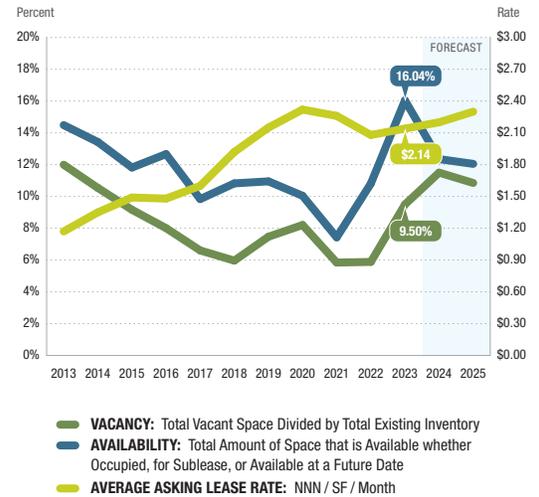
OVERVIEW. Following two consecutive years of positive net absorption, the Flex/R&D market registered an dramatic 1.4 MSF of negative net absorption in 2023, and a corresponding increase in the vacancy and availability rates. The Flex/R&D market in San Diego is driven by the biotech sector which is showing signs of slowing. Rental rates remain elevated from a long-term perspective. Leasing and sales volume were both far below historic norms in 2023.

VACANCY & AVAILABILITY. Direct/sublease space (unoccupied) finished Q4 2023 at 9.5%, a 61% increase from Q4 2022's vacancy rate of 5.9%. From a historical perspective, this is still well below the vacancy rate from more than ten years ago when the countywide vacancy rate finished 2011 above 16%. Direct/sublease space being marketed was 16% at the end of Q4. The availability rate saw a 48% increase from the prior year. 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. The segments of the county with the least amount of lab space, East County, the I-15 Corridor, and South County, all have availability rates in the single digits. Since the start of 2022, the sublease vacancy across the county has increased more than fourfold, finishing Q4 2023 at 3.8%.

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 2023, which is an increase of 2.9% from Q4 2022. 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 ten years the countywide asking rental rate has increased an average of 6.5% 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 Q4 totaled 877,050 SF, just over half of the 1.6 MSF transacted in Q4 2022. There were 558,544 SF of Flex/R&D space leased in 104 transactions recorded in Q4. These figures were far below the five-year averages of 134 transactions and 944,078 SF leased per quarter. On the sales side, 75 Flex/R&D buildings totaling 1.9 MSF traded in 2023. The prior two years averaged 130 buildings, and 4.5 MSF of transactions per year. The Flex/R&D sales market is facing headwinds from both increasing costs of capital and weaker leasing-market conditions. Prior to 2020, it was rare to see an institutional biotech landlord part ways with any of their local holdings. Alexandria showed up on the seller side in one of

VACANCY, AVAILABILITY & AVERAGE ASKING LEASE RATES



TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



Market Statistics

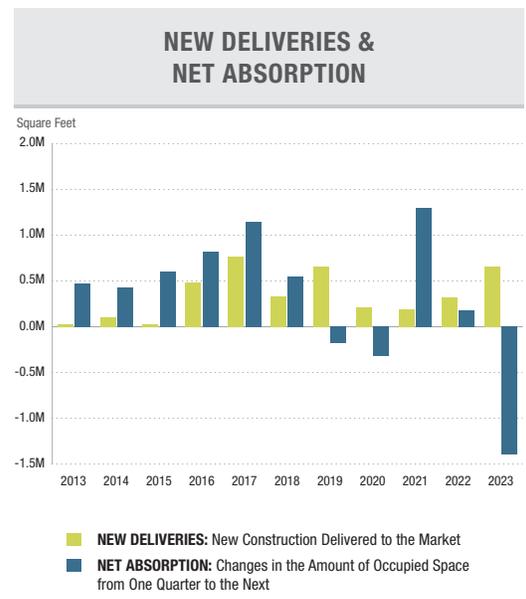
	Change Over Last Quarter	Q4 2023	Q3 2023	Q4 2022	% Change Over Last Year
Vacancy Rate	▲ UP	9.50%	9.14%	5.88%	61.44%
Availability Rate	▼ DOWN	16.04%	16.32%	10.81%	48.43%
Average Asking Lease Rate	▼ DOWN	\$2.14	\$2.22	\$2.08	2.88%
Sale & Lease Transactions	▲ UP	877,050	532,511	1,618,222	(45.80%)
Gross Absorption	▲ UP	718,751	579,501	845,174	(14.96%)
Net Absorption	▼ NEGATIVE	(43,576)	(409,869)	(18,377)	N/A

the top Q4 deals, as the institutional biotech owners have shown increasing willingness to dispose of non-core assets.

ABSORPTION. The San Diego Flex/R&D market recorded 43,576 SF of negative net absorption in Q4, the sixth consecutive quarter of negative net absorption. The negative net absorption was concentrated in the suburban core of the county where the bulk of the biotech properties is located. In total, the Flex/R&D market's tenant footprint shrunk by 1.4 MSF in 2023, the most negative net absorption in a calendar year in over a decade. The biotech segment of the Flex/R&D market has a very boom-bust nature dominated by a high percentage of large tenants, and this can move the market statistics rapidly in one direction or the other.

CONSTRUCTION. At the end of 2023 there were 2 MSF under construction or lab conversion, with 84% of this space still available for lease. 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. All of the properties under construction at the end of 2023 were in the submarkets surrounding UCSD. These conversions do not show up in the new construction totals. The dividing line between office properties and flex properties is becoming less distinct, especially in Sorrento Mesa and Sorrento Valley which have been the epicenter of recent lab conversions. Additionally, many ground-up developments are positioned towards attracting both office and lab users to fill their new buildings.

EMPLOYMENT. The unemployment rate in San Diego County was 4.2% in November 2023, unchanged from a revised 4.2% in October 2023, and above the year-ago estimate of 3.3%. This compares with an unadjusted unemployment rate of 4.9% for California and 3.5% for the nation during the same period. Over the 12-month period between November 2022 and November 2023, San Diego County employment increased by 21,900 jobs, an increase of 1.4%. With the normal delay in reporting from the California EDD, employment figures from December were unavailable at the time of publishing this report. For the nation as a whole, 216,000 jobs were added in December, and weekly new jobless benefit claims finished the year at their lowest level in two months.



Forecast

It is evident that the supply of biotech conversions has outpaced the tenant demand currently in the market. Growth in the biotech sector is heavily reliant upon large capital infusions, and not only will this capital be more difficult to source during a macroeconomic malaise, but also it will demand higher yields in response to rising interest rates. We anticipate a continued increase in vacancy as the surge of life-science conversions centered around Sorrento Mesa reaches completion.

Significant Transactions

Sales						* Voit Real Estate Services Deal
Property Address	Submarket	Square Feet	Sale Price	Buyer	Seller	
11501 Rancho Bernardo Rd. & 16981 Via Tazon	Rancho Bernardo	87,516	\$30,800,000	Dollinger Properties	Montana Avenue Capital Partners	
15330 Avenue of Science	Rancho Bernardo	73,756	\$26,350,000	Helix Electric	Montana Avenue Capital Partners	
11075 & 11065 Roselle St.	Sorrento Valley	43,530	\$14,900,000	W.P. Carey, Inc.	Alexandria Real Estate Equities	
9180 Brown Deer Rd.	Miramar	13,509	\$5,850,000	9180 Brown Deer, LLC*	Pacific Science & Engineering Group	
2440 Grand Ave.	Vista	14,973	\$4,239,000	2440 Grand Avenue, LLC	Spence Industries, LLC	

Leases					
Property Address	Submarket	Square Feet	Transaction Date	Tenant	Owner
4796 Executive Dr.	UTC	61,755	Nov-2023	Lily Gateway Labs	Alexandria Real Estate Equities
10075 Barnes Canyon Rd.	Sorrento Mesa	31,543	Dec-2023	Undisclosed	Alexandria Real Estate Equities
11202 El Camino Real	Carmel Valley	29,734	Oct-2023	Undisclosed	Breakthrough Properties
5764 Pacific Center Blvd.	Sorrento Mesa	29,268	Nov-2023	Undisclosed	Quidel Corporation
3565 General Atomics Ct.	Torrey Pines	22,443	Oct-2023	Undisclosed	Alexandria Real Estate Equities

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate Q4 2023	Square Feet Available	Availability Rate Q4 2023	Average Asking Lease Rate	Net Absorption Q4 2023	Net Absorption 2023	Gross Absorption Q4 2023	Gross Absorption 2023
Central													
Central City	14	188,791	0	0	32,164	17.04%	34,004	18.01%	\$1.80	4,400	(12,100)	6,500	6,500
East City	3	373,020	0	0	0	0.00%	0	0.00%	-	0	346,128	0	0
Southeast City	23	248,050	0	0	6,856	2.76%	6,856	2.76%	\$1.83	0	(3,856)	0	5,500
Kearny Mesa	205	5,460,416	0	5,400	179,189	3.28%	373,086	6.83%	\$1.66	(11,931)	(16,339)	23,600	179,713
Mission Gorge	28	294,807	0	0	16,800	5.70%	0	0.00%	\$2.09	(13,100)	(13,100)	3,700	6,406
Rose Canyon/Morena	41	646,060	0	0	43,684	6.76%	62,046	9.60%	\$1.85	3,131	(36,779)	31,245	75,205
Sports Arena/Airport	33	426,603	0	0	69,988	16.41%	84,660	19.85%	\$1.93	(1,224)	(5,049)	0	0
Miramar	219	4,859,621	0	0	270,424	5.56%	668,607	13.76%	\$1.98	(813)	(124,076)	15,756	140,318
Sorrento Mesa	176	8,118,682	1,464,233	662,196	1,715,324	21.13%	3,437,876	35.88%	\$3.19	(21,517)	(589,000)	88,523	449,824
Sorrento Valley	113	2,725,602	0	0	468,779	17.20%	577,243	21.18%	\$3.14	3,858	(310,809)	64,266	190,135
Torrey Pines/UTC	79	6,861,390	559,966	512,000	698,667	10.18%	1,255,690	16.92%	\$4.26	(54,951)	(397,086)	75,499	205,902
Central County Total	934	30,203,042	2,024,199	1,179,596	3,501,875	11.59%	6,500,068	20.17%	\$2.54	(92,147)	(1,162,066)	309,089	1,259,503
East County													
El Cajon	80	903,480	0	0	22,685	2.51%	26,600	2.94%	\$1.49	(4,729)	(814)	17,956	37,555
La Mesa/Spring Valley	44	310,414	0	0	5,000	1.61%	14,155	4.56%	\$1.60	4,155	(2,000)	9,155	14,755
Santee/Lakeside	54	605,800	0	0	14,812	2.45%	14,812	2.45%	\$1.33	2,468	(9,252)	2,468	17,414
Rural East County	22	95,520	0	0	0	0.00%	0	0.00%	-	0	0	0	0
East County Total	200	1,915,214	0	0	42,497	2.22%	55,567	2.90%	\$1.47	1,894	(12,066)	29,579	69,724
North County													
Escondido	84	787,788	0	0	50,520	6.41%	69,518	8.82%	\$1.42	(30,788)	(25,441)	1,737	13,561
Oceanside	33	966,298	0	217,000	11,094	1.15%	18,509	1.92%	\$1.61	181	(5,876)	4,181	13,190
San Marcos	56	1,054,187	0	0	31,670	3.00%	58,027	5.50%	\$1.34	40,931	22,582	47,308	97,257
Vista	63	1,393,645	0	0	124,166	8.91%	223,578	16.04%	\$1.36	6,407	53,467	34,477	134,848
Carlsbad	264	7,407,613	0	67,714	699,714	9.45%	1,253,008	16.92%	\$1.77	70,703	(55,015)	167,083	508,786
North Beach Cities	19	166,277	0	0	5,240	3.15%	5,240	3.15%	\$2.97	6,201	(5,554)	6,201	10,081
Rural North County	19	139,487	0	0	1,650	1.18%	1,650	1.18%	\$1.00	1,200	1,550	1,200	6,350
North County Total	538	11,915,295	0	284,714	924,054	7.76%	1,629,530	13.68%	\$1.62	94,835	(14,287)	262,187	784,073
I-15 Corridor													
Poway	62	2,113,728	0	0	28,742	1.36%	74,224	3.51%	\$1.82	(8,490)	(15,111)	5,858	18,465
Rancho Bernardo	100	4,711,462	0	0	475,525	10.09%	537,918	11.42%	\$1.99	(39,300)	(297,124)	89,071	155,888
Scripps Ranch	31	1,011,159	0	100,000	99,716	9.86%	99,716	9.86%	\$1.68	5,175	120,403	5,175	150,175
I-15 Corridor Total	193	7,836,349	0	100,000	603,983	7.71%	711,858	9.08%	\$1.95	(42,615)	(191,832)	100,104	324,528
South County													
Chula Vista	80	1,458,880	0	0	34,406	2.36%	59,789	4.10%	\$1.96	(3,124)	(13,655)	13,683	55,948
National City	24	321,727	0	0	7,272	2.26%	10,810	3.36%	\$1.69	1,756	(3,272)	4,109	8,853
Otay Mesa	7	156,362	0	0	0	0.00%	0	0.00%	\$2.88	0	3,130	0	3,130
South San Diego	5	86,876	0	0	4,175	4.81%	4,175	4.81%	-	(4,175)	(4,175)	0	0
South County Total	116	2,023,845	0	0	45,853	2.27%	74,774	3.69%	\$1.90	(5,543)	(17,972)	17,792	67,931
San Diego County Total	1,981	53,893,745	2,024,199	1,564,310	5,118,262	9.50%	8,971,797	16.04%	\$2.14	(43,576)	(1,398,223)	718,751	2,505,759

Lease rates are on a triple-net basis.



A Period of Transition & Complacency

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As 2023 concludes, it has proven to be a year of transition. The frenetic leasing and sale activity of years past is indeed in the rearview mirror.

San Diego Industrial, countywide, has experienced a year of relatively slower activity on both the leasing and building sales fronts, as tenants, owner-user buyers, and institutional investors were taking a more cautious and measured approach to making decisions. This is a return to a moderate tenant and buyer velocity, that is typical in San Diego. We are now in a period of complacency, as the general market remains strong, but tenants, owner-user buyers, and investors are becoming, arguably, complacent in their approach to the market.

It is predicted that building sale prices and asking lease rates will hold steady at these current levels, even in the face of more than two million square feet of industrial currently under construction, most of which is slated for completion this year in Otay Mesa. Multinational corporations continue the “nearshoring” of their manufacturing in Tijuana, and their subsequent need for product distribution on the United States side favors Otay Mesa. This continued demand to locate manufacturing in Tijuana will help with maintaining a healthy absorption rate of new and existing industrial product in Otay Mesa and will help maintain upward pressure on industrial demand throughout San Diego County.

Larger institutional investment sales will remain slow, as this category of investors will remain complacent, as they continue to sit on the sidelines for a few quarters of 2024 to see where interest rates, cap rates, leasing activity, and the general economy go, in this all-important election year.

In summary, the industrial market is healthy, and is predicted to remain strong in San Diego, throughout 2024, countywide. There will be little to no erosion in lease rates, nor in owner-user building sale prices, as San Diego has an extremely balanced economy, with no single, major employer dominating the market. As such San Diego industrial real estate remains in high demand and is favored by institutional investors, who will be back in the market after this short respite.

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

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