

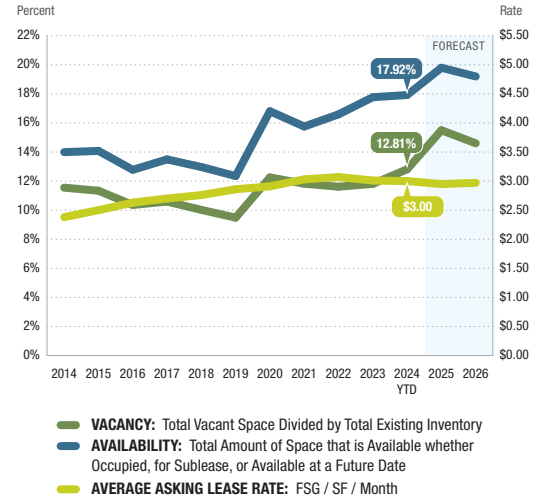
**OVERVIEW.** Leasing and sales volumes remained at low levels compared with historical norms in Q2. The market saw a modest amount of positive absorption in Q2, but the 2024 total remained in the negative. Sublease availability in the market stubbornly held its inflated position. The average asking rental rate for the county was flat in Q2, and office construction is historically elevated. The shift in workplace dynamics continues to unfold across the office market, and the uncertainty it causes is not expected to dramatically change any time soon.

**VACANCY & AVAILABILITY.** Direct/sublease space (unoccupied) finished Q2 at 12.81%, a 92-basis point increase from the level of a year ago. Available office space being marketed (regardless of occupancy status) was 17.92% of the county's inventory at the end of Q2, an increase of 21 basis points over the prior year. Among the county's major submarkets (minimum of 5 MSF of inventory), Sorrento Mesa had the lowest availability, at 11.86%. Meanwhile, the availability rate in Downtown is at 37.59% and the vacancy rate there is greater than 30%. The relatively large amount of new office space that will be completed over the next couple of years will push the vacancy rate higher. Sublease availability has increased by 1.45 MSF since Q3 2021, effectively doubling over that span. There were 2.89 MSF of available sublease space at the end of Q2.

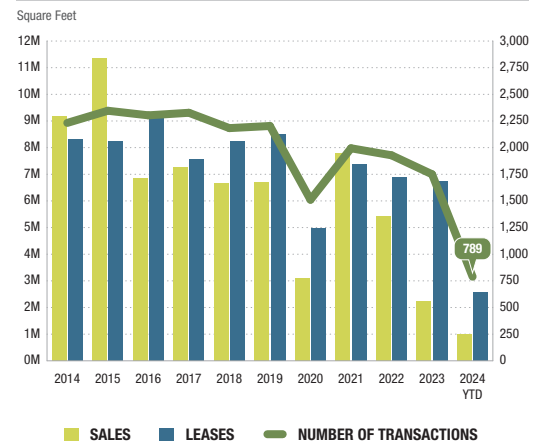
**LEASE RATES.** The average asking full-service-gross (FSG) lease rate per square foot per month in San Diego County was \$3.00 at the end of Q2, no change from the prior quarter's rate, and a 2% decrease from Q2 2023's rate of \$3.06. This decrease in asking rental rates is an indicator of the weakness of the office market, especially in light of the substantial construction pipeline currently underway. Typically, a large amount of new office space coming to the market pushes the average rental rate higher. The average asking rental rate is finally seeing the effects of decreased leasing activity, increased availability, and competition from sublease office space. Average asking lease rates have now been decreasing for over a year, as landlords with less-desirable office buildings, or in lower-demand submarkets, are realizing they need to be more aggressive in the way they position their vacancies. But the balance of leverage varies across the county.

**TRANSACTION ACTIVITY.** Through the first half of 2024, there have been 2.6 MSF of leases recorded. This puts the market on a pace for 5.2 MSF of leasing activity for 2024, while each of the prior three calendar years recorded more than 6.7 MSF of leasing activity. The number of office leases recorded in Q2 was 392. This was below the quarterly average of 447 transactions recorded between 2021 and 2023. Office sales volume remained constrained in the first half of 2024, with less than \$200 million in sales occurring. This puts the market on pace for less than \$500 million for the full year, and prior to 2023, the last time less than \$1 billion in office sold in a calendar year was in 2010. High interest rates, tight lending standards, and concerns about future demand are acting as major headwinds in the current office sales market.

### VACANCY, AVAILABILITY & AVERAGE ASKING LEASE RATES



### TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



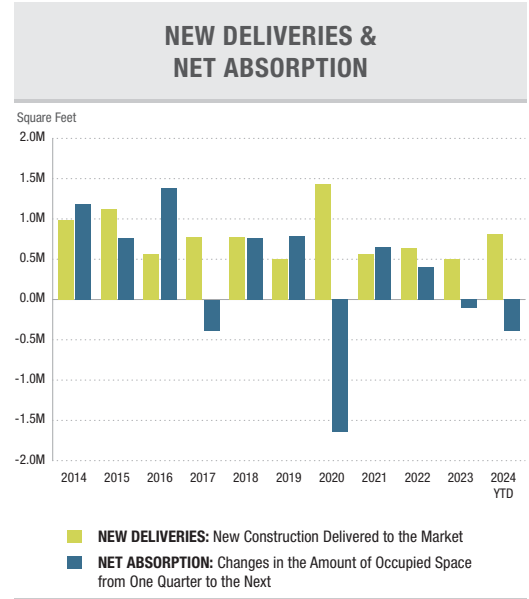
### Market Statistics

	Change Over Last Quarter	Q2 2024	Q1 2024	Q2 2023	% Change Over Last Year
Vacancy Rate	▲ UP	12.81%	12.33%	11.89%	7.78%
Availability Rate	▬ FLAT	17.92%	17.84%	17.71%	1.21%
Average Asking Lease Rate	▬ FLAT	\$3.00	\$3.00	\$3.06	(1.96%)
Sale & Lease Transactions	▲ UP	1,868,244	1,726,343	2,199,109	(15.05%)
Gross Absorption	▲ UP	1,728,035	1,269,478	1,478,951	16.84%
Net Absorption	▲ POSITIVE	157,206	(547,024)	(313,744)	N/A

**ABSORPTION.** There were 157,206 SF of positive net absorption in Q2, just the second quarter of positive net absorption over the past eight quarters. Despite this small respite, the market remains firmly in the red with a net total of negative 389,818 SF for the first half of 2024. The Del Mar Heights/ Carmel Valley submarket registered the greatest amount of positive net absorption, with over 300,000 SF of office tenant footprint expansion in the first half of 2024. Much of the growth in that submarket has come in offices completed in 2024.

**CONSTRUCTION.** Through the first six months of 2024, there have been 810,000 SF of new office deliveries, exceeding the annual totals of each of the previous three years. The 520,000 SF Torrey View development in Carmel Valley is the largest office development to come to fruition thus far in 2024. The three-building project owned by Breakthrough Properties commenced construction in 2021, and came to completion in 2024, fully occupied. Pfizer and BD each leased over 200,000 SF in the project. As for offices under construction at the midpoint of 2024, IQHQ and Stockbridge are each still searching for an anchor tenant for their office developments under construction in Downtown San Diego. IQHW has over 1.5 MSF of available office space under construction, and Stockbridge has more than half a million square feet of available office space under construction. Construction projects that recently completed, or are nearing completion, were begun during a period of rapid growth in the technology and life sciences sectors. Those sectors have pulled back, along with their demand for office space, leaving owners of new office buildings jockeying to capture their piece of a smaller pie.

**EMPLOYMENT.** The unemployment rate in San Diego County was 3.6% in May 2024, down from a revised 4.1% in April 2024, and above the year-ago estimate of 3.3%. This compares with an unadjusted unemployment rate of 4.5% for California and 3.7% for the nation during the same period. Over the 12-month period between May 2023 and May 2024, San Diego County employment increased by 6,900 jobs, an increase of 0.4%. With the normal delay in reporting from the California EDD, employment figures from June were unavailable at the time of publishing this report. For the nation as a whole, the unemployment rate rose to 4.1% in June, matching the highest level since October 2021.



## Forecast

The current surge in office construction will push the vacancy rate up, and that will have the strongest direct impact on the market for larger tenants. For the county as a whole, we project increased vacancy in the coming quarters. The office sales market has been hit by high interest rates, tight lending standards, and paltry demand for offices as the asset category's fundamentals are currently working through a paradigm shift. We do not foresee a significant change to these underlying factors in the coming quarters. Office loan distress is mounting, and this may place downward pressure on office sale pricing.

## Significant Transactions

Sales							* Voit Real Estate Services Deal
Property Address	Submarket	Class	Square Feet	Sale Price	Buyer	Seller	
9275 & 9325 Sky Park Ct.	Kearny Mesa	A	205,000	\$18,968,000	Orum Capital	TPG Angelo Gordon & Co., LP	
3702 & 3790 Via de la Valle	North Beach Cities	B	63,629	\$18,500,000	Brixton Capital	Lincoln Property Company & ASB Capital Management	
6719 Alvarado Rd.	College Area	B	53,781	\$16,350,000	Sharp HealthCare	TDA Investment Group	
3990 Ruffin Rd.	Kearny Mesa	B	45,940	\$12,248,350	VEBA*	CONAM Management Corp.	
9265 Sky Park Ct.	Kearny Mesa	B	44,020	\$11,500,000	Pacific Coast Properties, LLC*	Omninet Capital	

Leases						
Property Address	Submarket	Class	Square Feet	Transaction Date	Tenant	Owner
16464 Via Esprillo	Rancho Bernardo	B	82,999	May-2024	Daylight Solutions (Renewal)	Drawbridge Realty
7650 Mission Valley Rd.	Mission Valley	B	74,000	Jun-2024	City of San Diego	(Sublease)
13520 Evening Creek Dr. N.	Rancho Bernardo	A	23,973	Jun-2024	Lennar Homes	Kilroy Realty Corp.
10620 Treena St.	Scripps Ranch	A	23,388	Jun-2024	Engineering Partners	Treena Properties, LP
12400 High Bluff Dr.	Del Mar Heights	A	18,415	Apr-2024	Undisclosed	Kilroy Realty Corp.

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate Q2 2024	Square Feet Available	Availability Rate Q2 2024	Average Asking Lease Rate	Net Absorption Q2 2024	Net Absorption 2024	Gross Absorption Q2 2024	Gross Absorption 2024
<b>Downtown</b>													
Downtown	128	14,223,994	2,426,312	550,000	4,273,931	30.05%	6,258,694	37.59%	\$2.67	(122,454)	(237,639)	138,735	263,397
Downtown Total	128	14,223,994	2,426,312	550,000	4,273,931	30.05%	6,258,694	37.59%	\$2.67	(122,454)	(237,639)	138,735	263,397
<b>Central</b>													
City Heights / University	32	1,251,082	0	0	47,388	3.79%	71,084	5.68%	\$2.52	2,560	(112)	7,901	9,401
Coronado	4	84,540	0	0	0	0.00%	0	0.00%	\$3.25	0	0	0	0
Kearny Mesa	240	11,403,125	0	354,087	898,862	7.88%	1,563,409	13.71%	\$2.97	(14,333)	7,113	77,492	220,051
Mission Gorge	19	586,866	0	0	5,025	0.86%	6,405	1.09%	\$2.11	(1,245)	(2,723)	4,070	4,070
Mission Valley	129	7,499,505	0	1,130,925	1,323,151	17.64%	1,477,694	19.70%	\$2.94	(53,452)	9,645	152,120	384,560
Old Town / Point Loma	75	2,306,052	0	230,000	211,016	9.15%	268,231	11.63%	\$2.64	23,497	(8,290)	32,852	56,500
Park East	15	221,094	0	0	0	0.00%	0	0.00%	\$1.98	1,385	985	8,098	8,098
Rose Canyon / Morena	50	1,188,527	0	0	72,312	6.08%	110,090	9.26%	\$2.37	10,353	(31,369)	25,022	38,589
Uptown / Hillcrest	78	2,179,768	0	0	132,222	6.07%	186,709	8.57%	\$2.92	(6,117)	13,013	15,773	51,344
Central Total	642	26,720,559	0	1,715,012	2,689,976	10.07%	3,683,622	13.79%	\$2.88	(37,352)	(11,738)	323,328	772,613
<b>I-15 Corridor</b>													
Escondido	73	1,740,262	0	36,614	229,087	13.16%	372,318	21.39%	\$2.32	18,670	(17,395)	45,424	67,989
Poway	30	1,246,715	0	0	99,319	7.97%	102,371	8.21%	\$1.84	(9,658)	333	3,668	20,455
Rancho Bernardo	101	6,454,144	0	165,747	847,505	13.13%	953,846	14.78%	\$3.20	36,427	(17,708)	65,367	154,753
Scripps Ranch	49	2,742,662	0	356,000	465,285	16.96%	398,916	14.54%	\$3.00	(22,301)	(37,632)	2,588	13,390
I-15 Corridor Total	253	12,183,783	0	558,361	1,641,196	13.47%	1,827,451	15.00%	\$2.97	23,138	(72,402)	117,047	256,587
<b>North County Coastal</b>													
Carlsbad	165	7,063,991	0	50,000	1,025,675	14.52%	1,735,001	24.56%	\$2.72	(63,745)	(154,659)	57,577	127,490
Del Mar Heights / Carmel Valley	85	6,232,218	442,534	1,635,627	823,265	13.21%	1,156,395	17.32%	\$4.58	455,929	330,307	659,302	711,318
North Beach Cities	112	2,757,474	0	25,456	271,333	9.84%	312,482	11.33%	\$4.10	(13,581)	(42,993)	36,030	74,373
North County Total	362	16,053,683	442,534	1,711,083	2,120,273	13.21%	3,203,878	19.42%	\$3.36	378,603	132,655	752,909	913,181
<b>North City</b>													
Governor Park	19	768,582	0	0	80,304	10.45%	102,698	13.36%	\$2.96	(2,089)	(2,245)	18,305	26,974
La Jolla	44	1,350,248	0	0	199,525	14.78%	253,068	18.74%	\$3.55	(15,106)	(863)	14,263	48,158
Miramar	33	1,508,065	0	0	86,825	5.76%	607,163	40.26%	\$2.33	9,994	(12,406)	25,029	47,336
Sorrento Mesa	104	8,486,289	0	1,232,000	615,699	7.26%	1,006,086	11.86%	\$2.92	(36,441)	(88,624)	59,024	86,979
Sorrento Valley	21	610,215	0	0	140,491	23.02%	84,760	13.89%	\$2.71	(8,753)	(37,145)	0	0
Torrey Pines	40	3,020,942	0	309,094	42,751	1.42%	60,658	2.01%	-	(2,246)	(5,680)	9,221	11,487
UTC	90	9,161,301	558,183	400,000	925,747	10.10%	1,617,610	16.64%	\$3.91	42,994	(10,644)	153,547	311,542
North City Total	351	24,905,642	558,183	1,941,094	2,091,342	8.40%	3,732,043	14.66%	\$3.47	(11,647)	(157,607)	279,389	532,476
<b>Southern &amp; Eastern Areas</b>													
Chula Vista	92	2,972,610	228,000	1,925,884	133,366	4.49%	247,353	7.73%	\$2.49	(6,389)	(13,319)	48,153	69,811
National City	16	583,906	0	0	12,932	2.21%	62,706	10.74%	\$2.47	(7,925)	(5,777)	0	4,884
South San Diego	14	350,710	0	0	55,219	15.74%	52,888	15.08%	\$4.40	(137)	983	783	6,141
Southeast San Diego	13	481,066	0	0	2,235	0.46%	2,235	0.46%	\$2.33	0	18,226	0	18,226
East County	153	3,826,289	0	0	162,684	4.25%	239,090	6.25%	\$2.42	(62,852)	(35,804)	19,498	67,870
Southern & Eastern Areas Total	288	8,214,581	228,000	1,925,884	366,436	4.46%	604,272	7.16%	\$2.46	(77,303)	(35,691)	68,434	166,932
<b>Highway 78 Corridor</b>													
Oceanside	62	1,491,916	0	218,235	155,040	10.39%	166,468	11.16%	\$2.63	13,382	(3,264)	31,717	46,585
San Marcos	38	1,482,054	0	1,488,285	66,998	4.52%	115,321	7.78%	\$2.33	1,711	(67)	6,447	19,888
Vista	51	1,255,156	0	0	243,343	19.39%	155,912	12.42%	\$2.42	(10,872)	(4,065)	10,029	25,854
Highway 78 Corridor Total	151	4,229,126	0	1,706,520	465,381	11.00%	437,701	10.35%	\$2.46	4,221	(7,396)	48,193	92,327
Class A	302	40,753,130	3,595,029	7,531,779	6,838,773	16.78%	10,797,242	24.35%	\$3.34	353,053	51,120	1,024,323	1,540,708
Class B	1,253	51,893,047	60,000	2,576,175	5,893,119	11.36%	7,778,209	14.97%	\$2.80	(173,565)	(403,079)	573,493	1,183,849
Class C	620	13,885,191	0	0	916,643	6.60%	1,172,210	8.44%	\$2.28	(22,282)	(37,859)	130,219	272,956
<b>San Diego County Total</b>	<b>2,175</b>	<b>106,531,368</b>	<b>3,655,029</b>	<b>10,107,954</b>	<b>13,648,535</b>	<b>12.81%</b>	<b>19,747,661</b>	<b>17.92%</b>	<b>\$3.00</b>	<b>157,206</b>	<b>(389,818)</b>	<b>1,728,035</b>	<b>2,997,513</b>

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



## Market Cycle Perspective

by **Brandon Keith**

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The state of the office market has consistently been the subject of speculation ever since COVID restrictions began to ease in 2021-2022. Will anyone come back to the office? Is the traditional corporate office era over forever? Rapid interest rate hikes beginning in 2022 compounded the dire sentiment surrounding office ownership. Will there be massive loan defaults, short sales, bankruptcies in the office sector? How will these owners refinance as debt comes due?

The answer to these questions midway through 2024 is that the office market is “75%–80% back,” from a daily office occupancy standpoint; and yes, there will be significant loan defaults and short sales over the next two to three years nationwide. The office distress largely resides with older, obsolete office product in city centers, over-leveraged owners (from small individuals to institutional owners), and new development projects that happen to be delivering at an inopportune time. In San Diego’s downtown office market, the RADD development by IQHQ and the Horton Plaza redevelopment from Stockdale Partners are examples of the latter scenario—just plain bad luck on timing.

Despite all the negative news, there is light at end of the office story, as there always is with market cycles and disruptive events. Over the next couple of years, businesses will have largely “right sized” their office spaces to account for remote workers. Obsolete and other distressed office property will be purchased for renovation or conversion (residential or other), resulting in less available office product in certain areas.

The cost of labor and construction materials have continued to increase, and they historically never decline in the long run. Even in the 2008–2010 period of the Great Recession, these costs did not decline. Interest rates, construction costs and overall market forces will result in very little new office development for the next two to five years in most markets across the nation. This will give existing office product an opportunity to heal and office vacancy should stabilize over the next three years.

Meanwhile, one office market segment which has remained surprisingly strong the last couple of years is the owner-user market. Despite SBA loan rates nearly doubling from 2020 through 1st quarter 2022, business owners continued seeking to control their overhead and own their office space. Ongoing demand is concentrated in the 3,000–25,000 SF range, but we are also seeing 40,000–60,000 SF office user purchases as well. This has kept owner-occupier sales prices at or near market highs, despite a drop in values for larger, institutionally owned office assets.

If rates move lower by 50 or more basis points over the next twelve months as many economists predict, then the user market is likely to gain even more strength. Lower interest rates will also help office owners in need of refinancing, and the overall health of the office market will improve. The expectation of lower rates, combined with the market forces detailed above, paint a mixed, but generally more positive, near-term picture of the office market than one might infer based on national headlines.

### Please Contact Us for Further Information

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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.

## 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