



NEWMARK

San Diego:
Office Market Overview

1Q26



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San Diego Office Market Observations



Economy

- Local unemployment was 4.4% in December 2025, up 20 basis points year-over-year. The release of more recent labor market data was delayed due to a partial federal government shutdown in January.
- Total nonfarm employment increased by only 2,400 jobs over the past year, and office-using employment continued its yearslong retreat. Over the past year business and professional services lost 6,200 jobs, financial activities lost 2,300, and information lost 900 jobs.
- The consumer price index for all urban consumers in the San Diego metro was up 2.6% annually as of January 2026, down from the 3.8% annual rate at the start of 2025.
- The Federal Reserve was expected to enact another 25-basis-point cut in 2026, but the war with Iran has created uncertainty over oil prices and inflation, leaving any potential cuts in doubt.



Leasing Market Fundamentals

- The average monthly asking rate rose to \$3.56/SF FSG, up 1.6% over the past year and a new all-time high. Over 3.0M SF of new speculative developments delivered in 2025 have helped asking rents continue to rise despite high vacancy.
- Net absorption was negative for the quarter, posting 79,972 SF of losses. Leasing activity totaled only 812,000 SF, well below the five-year quarterly average of 1.5M SF.
- Total vacancy fell 10 bps from the previous quarter to 20.1%, up from 18.6% a year ago.
- No new projects delivered during the first quarter, and current construction levels have fallen to 800K SF after record deliveries last year and developers' discomfort with high vacancy.
- Sublease availability fell to 1.7M SF while direct availability climbed to 17.1M SF, a new record.



Major Transactions

- The largest lease deal of the first quarter was defense contractor Northrop Grumman's renewal of a 168,000-SF, two-building project in Rancho Bernardo.
- Biotech firm Neomorph signed the largest new lease of the quarter, leasing 84,000 SF in two buildings in Mira Mesa from Alexandria Real Estate Equities.
- Axos Bank executed the largest acquisition of the quarter, purchasing three buildings in Rancho Bernardo from Kilroy Realty for \$124.5M.
- San Diego companies raised \$3.2B in venture capital funding during the first quarter, thanks in large part to defense contractor Shield AI's \$2.0B series, the largest venture capital round in San Diego's history.



Outlook

- Subdued leasing activity from the past two years will become the new baseline as office-using jobs have shrunk and many occupiers elect to renew in place rather than expand.
- High vacancy rates Downtown have put pressure on owners, leading to several underperforming projects to sell at a discount to new operators. A further 825K SF of office space has been removed from the inventory for conversion to apartments. Further basis – and rent – resets and conversions will occur until the market reaches equilibrium.
- The current construction pipeline is 100% preleased. Developers will only begin construction on projects that are preleased until the supply/demand imbalance subsides.
- Del Mar Heights and UTC have positioned themselves as the primary office core among premier office tenants, maintaining high asking rates and stable vacancy as Downtown has struggled.

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01

Economy

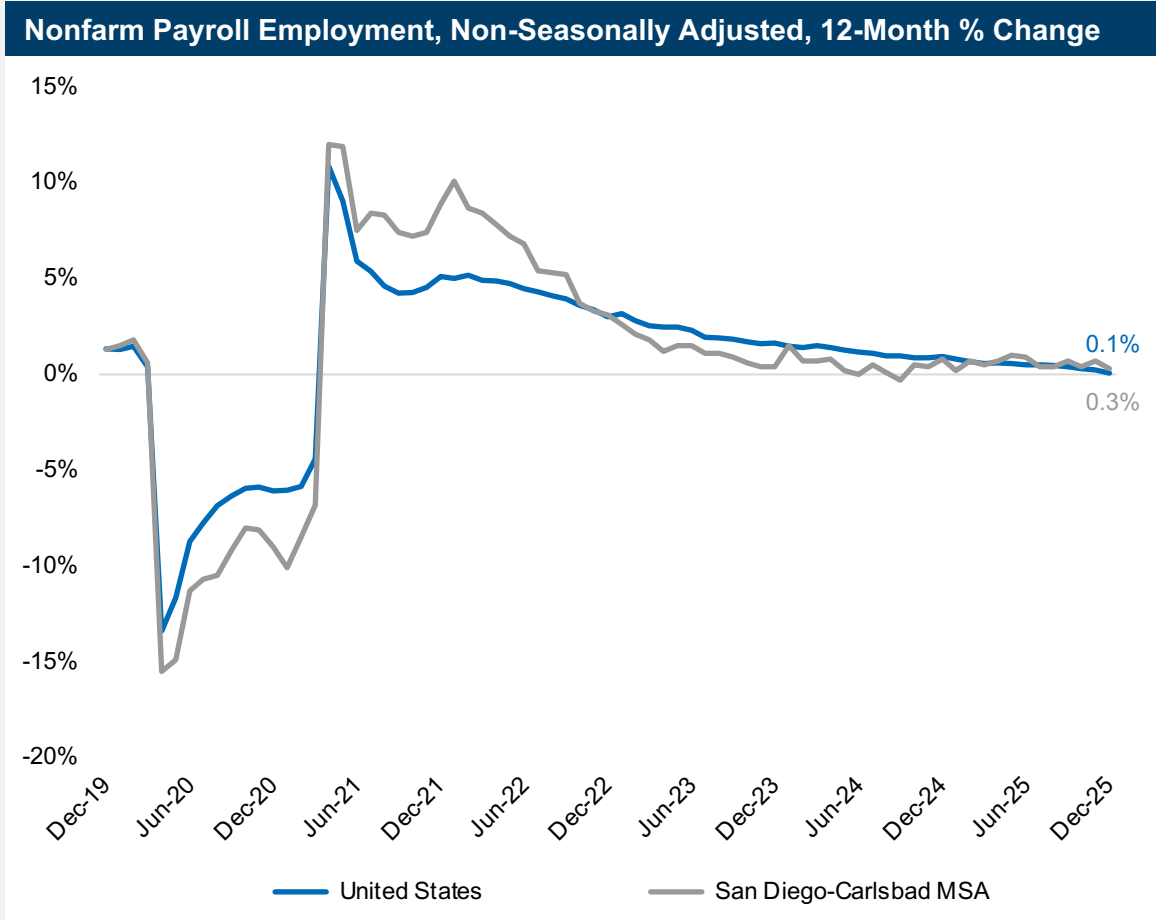
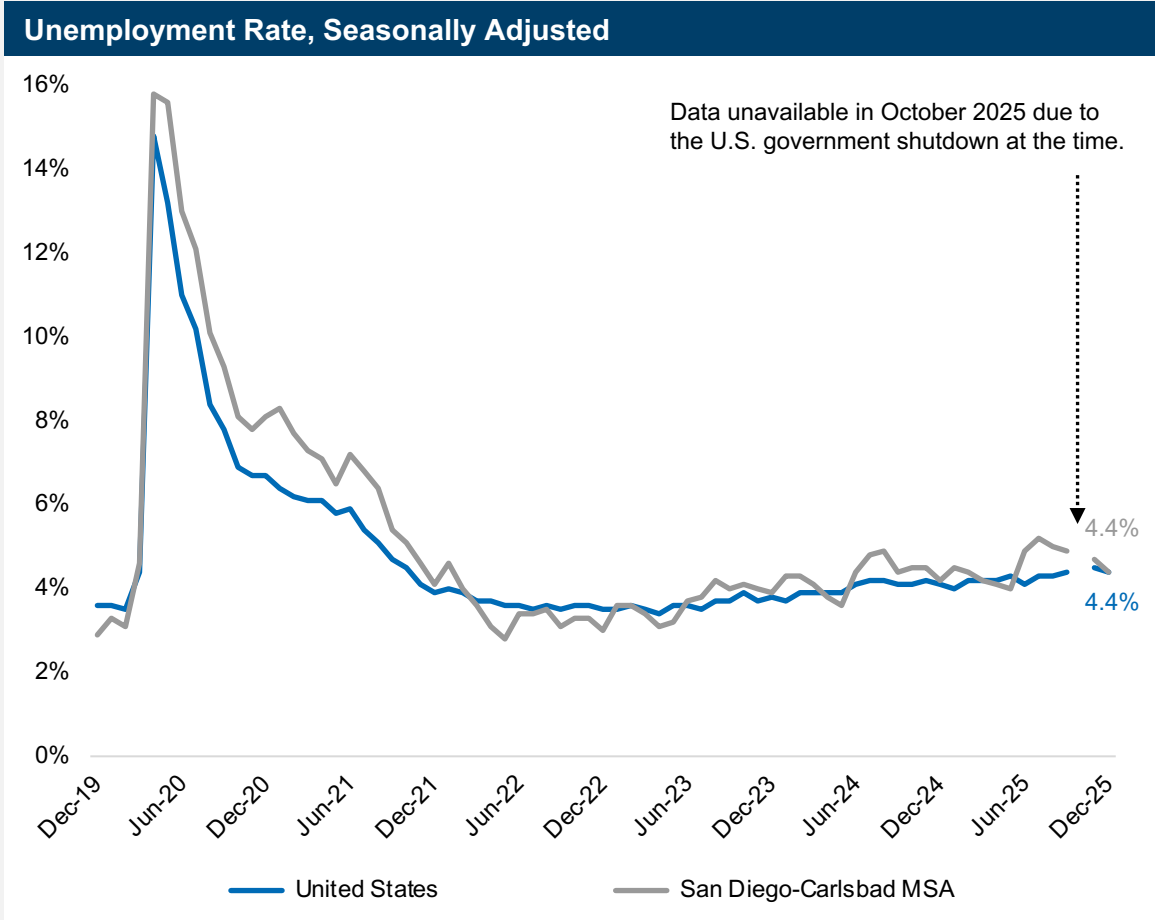
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Unemployment Trends Higher as Job Growth Has Slowed

Federal government shutdowns in recent months are affecting the release of timely labor market data. The local unemployment rate was 4.4% in December 2025, up 20 basis points over the past year. The local and national unemployment rates have risen gradually since 2021. During the past year total nonfarm employment posted minimal gains: employers reported an additional 2,400 jobs, representing annual growth of 0.3%.

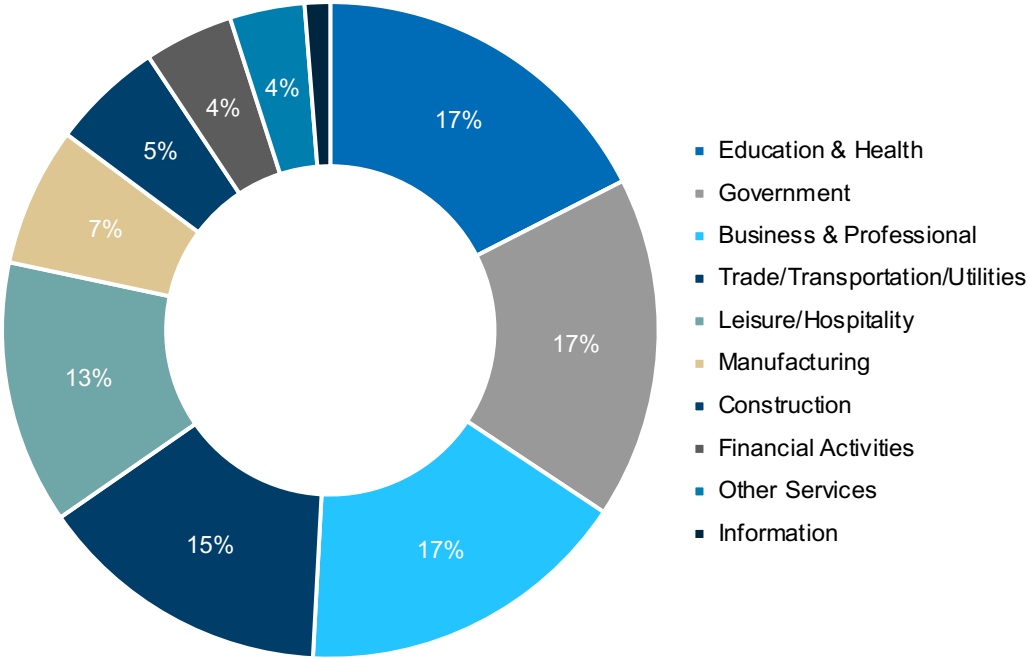


Source: U.S. Bureau of Labor Statistics, San Diego-Carlsbad MSA
 Note: Local employment statistics for October 2025 were unavailable due to the federal government shutdown. Early 2026 employment data was unavailable at the time of writing.

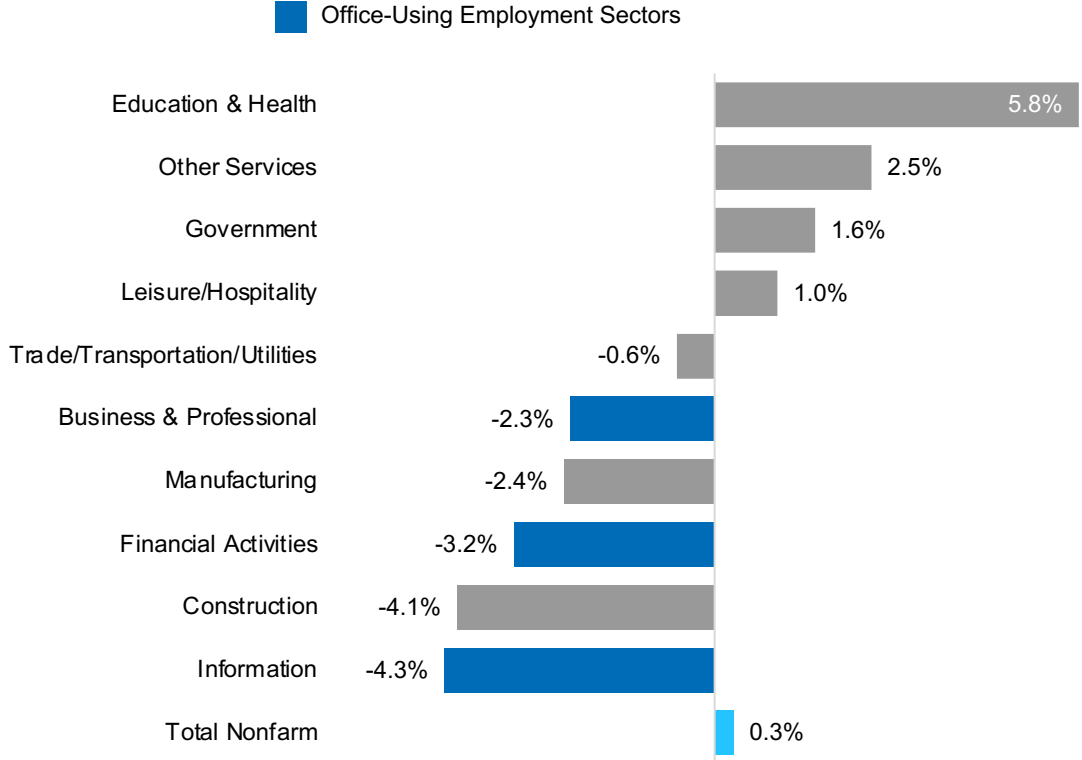
Business & Professional Services is No Longer the Largest Employment Sector

For most of the past five years business and professional services was the largest employment sector in the region, fueling white-collar jobs and office demand. However, this sector has been shrinking since 2022, while the education and health and government sectors have been growing rapidly - in March 2025, education and health surpassed business and professional to become the region's largest employment sector and in September 2025 government jobs became the second-largest employment sector. Office-using jobs in the smaller financial activities and information sectors have also been shrinking.

Employment by Industry, December 2025



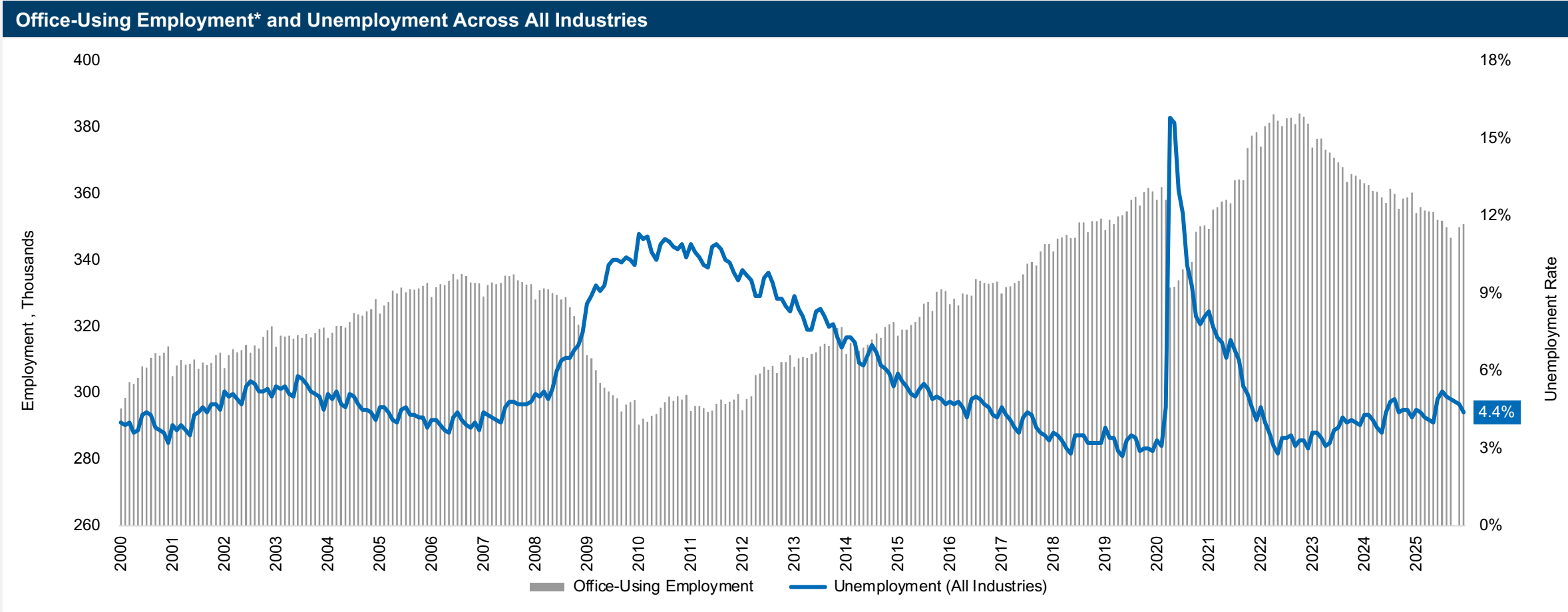
Employment Growth by Industry, 12-Month % Change, December 2025



Source: U.S. Bureau of Labor Statistics, San Diego-Carlsbad MSA
 Note: Local employment statistics for October 2025 were unavailable due to the federal government shutdown. Early 2026 employment data was unavailable at the time of writing.

Office-Using Employment Has Steadily Declined Since the Peak in 2022

In 2022 San Diego reached its peak of office-using jobs, but employment in these sectors has since fallen even as the number of total jobs in the region has grown. The information sector shed 900 jobs over the past year, financial activities lost 2,300 jobs, and business and professional shed 6,200 jobs. By comparison, education and health had the best performance over the past year, experiencing 5.8% job growth while government jobs saw 1.6% growth.



Source: U.S. Bureau of Labor Statistics, San Diego-Carlsbad MSA
 Note: December 2025 data is preliminary. *Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.
 Local employment statistics for October 2025 were unavailable due to the federal government shutdown. Early 2026 employment data was unavailable at the time of writing.

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Market Fundamentals

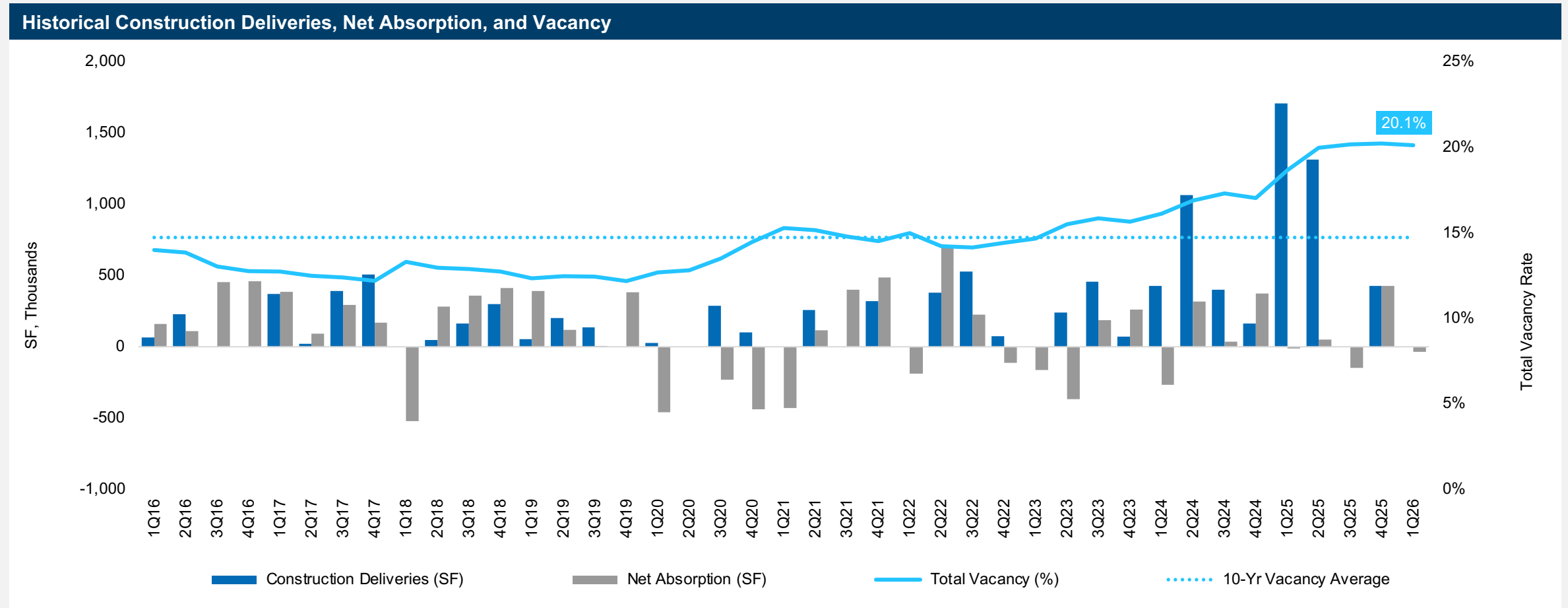
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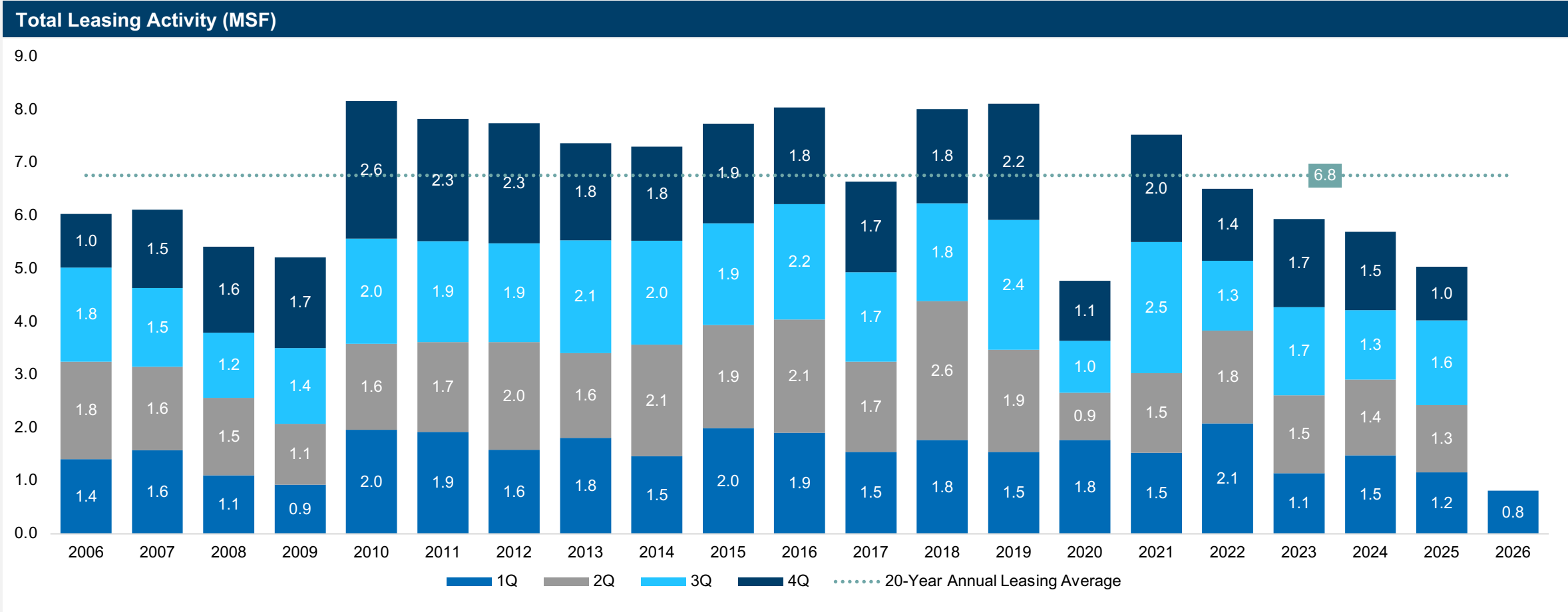
Vacancy Levels Out as New Speculative Deliveries Cease

2025 saw 3.6 MSF in construction deliveries, well above the 2.1 MSF delivered in 2024 and the largest annual total on record. This mostly unleased new inventory caused total vacancy to climb to an all-time high, before falling slightly to 20.1% in the first quarter of 2026. Deliveries have now abated as developers have paused further speculative developments as the wait for leasing demand to catch up to current supply.



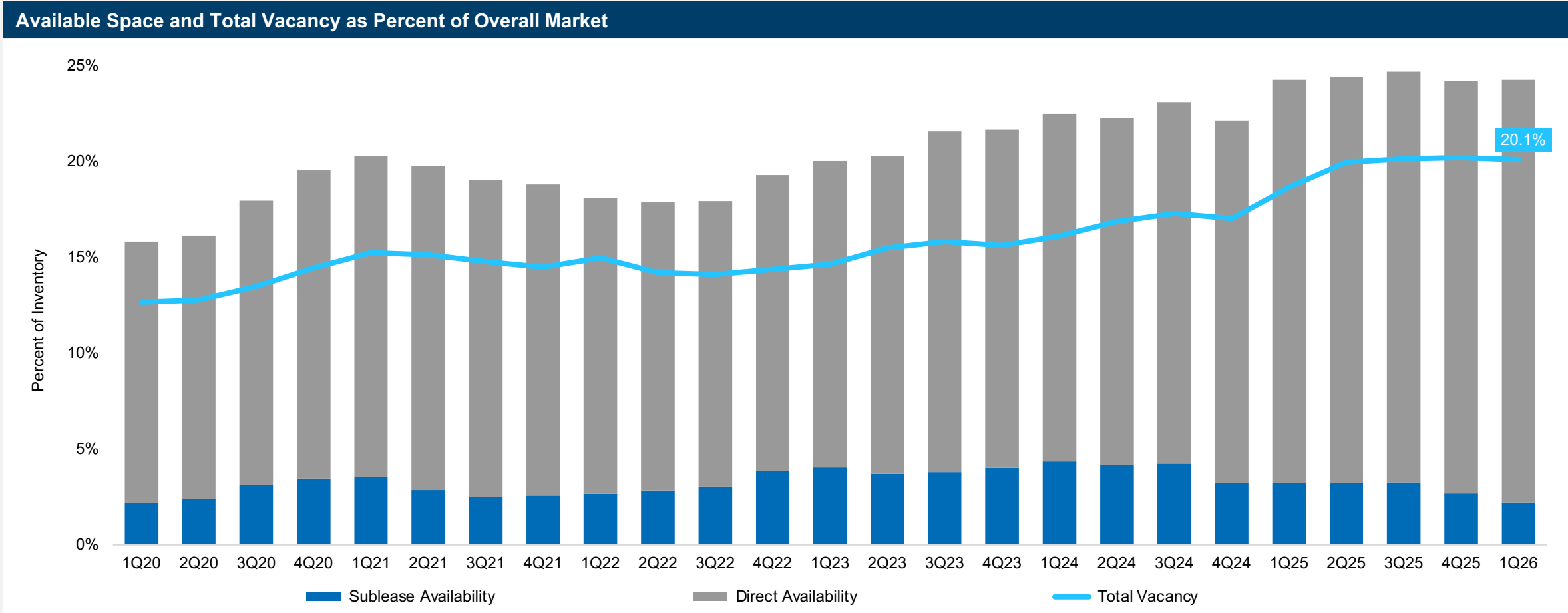
Leasing Activity Continues to Lag Historical Average

Leasing activity has lagged the historical annual average of 6.8 MSF since 2021 and has steadily decreased each year. 2025 saw only 4.7 MSF in leasing activity, lower than even 2009, during the Global Financial Crisis, largely due to slow activity during the fourth quarter. The first quarter of 2026 logged only 812,000 SF of leasing activity.



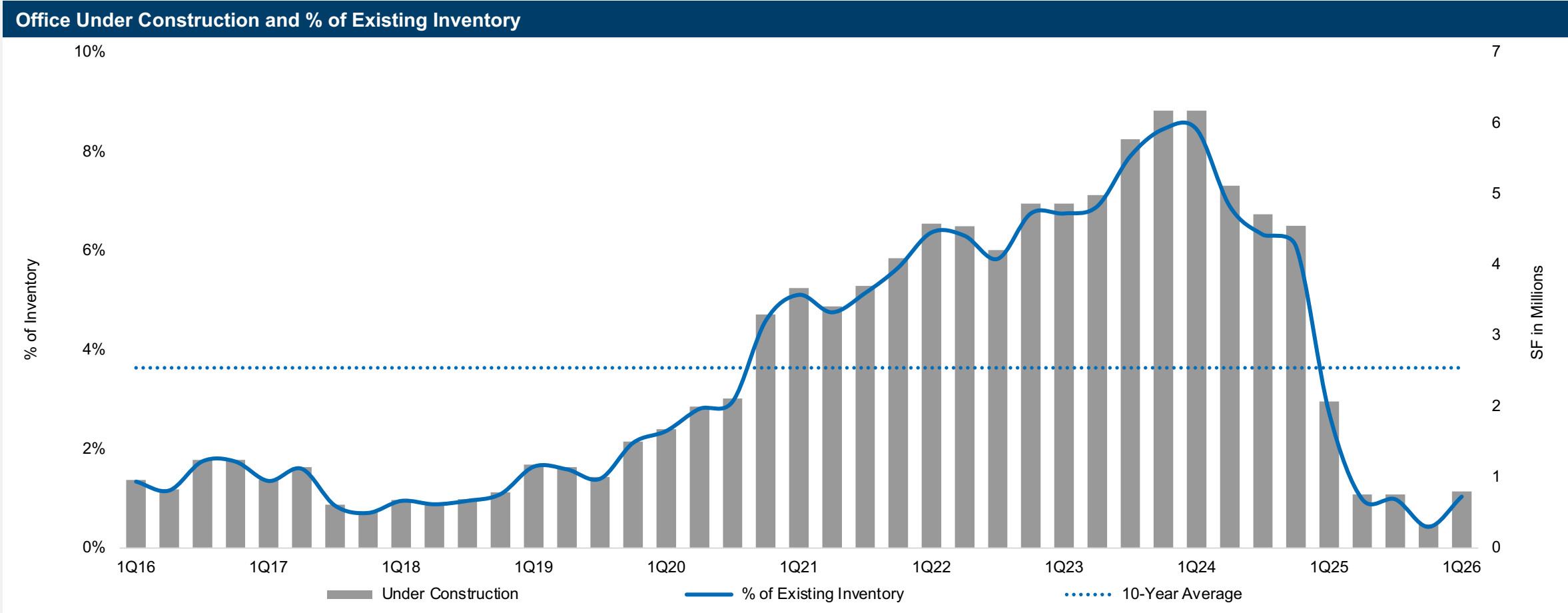
Vacancy and Availability Remain Elevated

Vacancy climbed to 20.1% from 18.6% a year ago as new supply has continued to outstrip demand for space. Sublease availability has fallen by 46.4% since the high in the first quarter of 2024 to 1.7 MSF, as sublease offerings were withdrawn and landlords took these spaces to market direct, although this decline was more than offset by an increase in direct availability and deliveries of new vacant buildings.



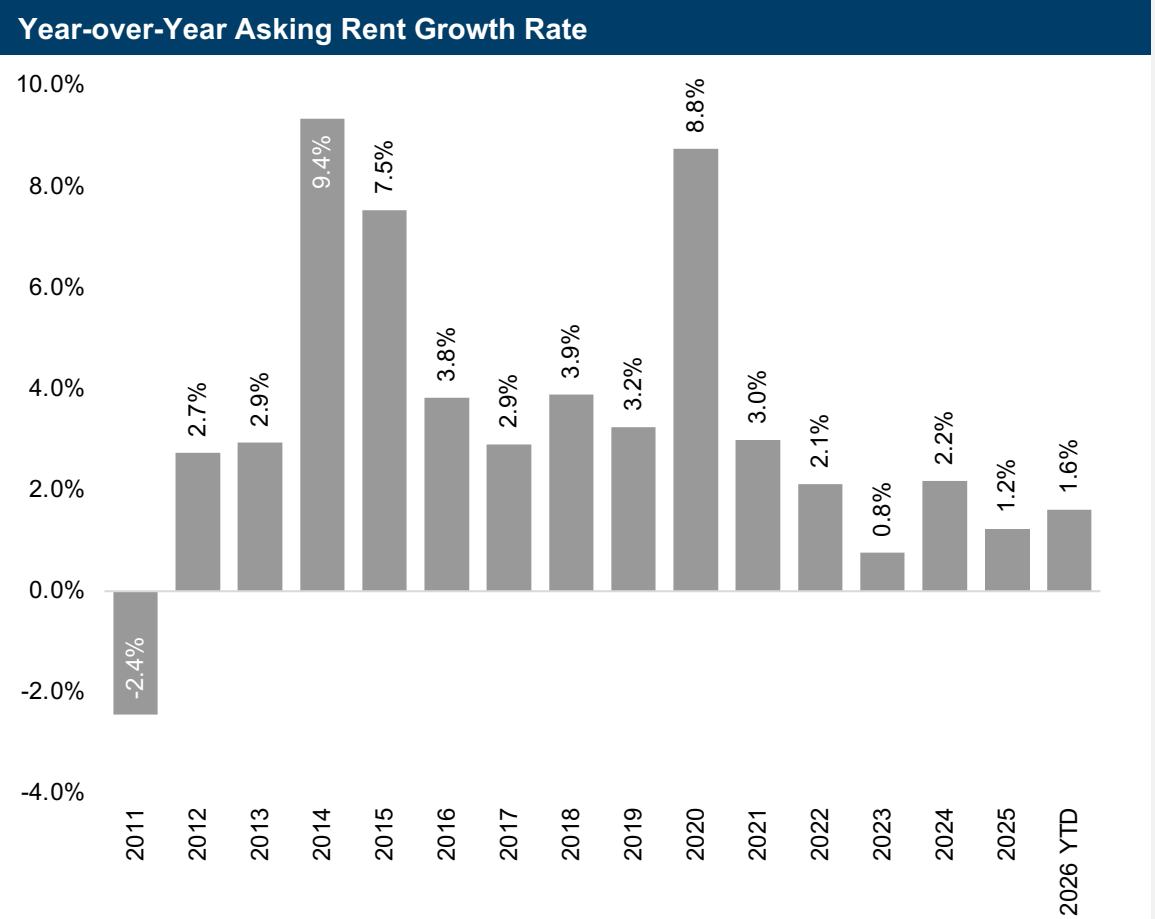
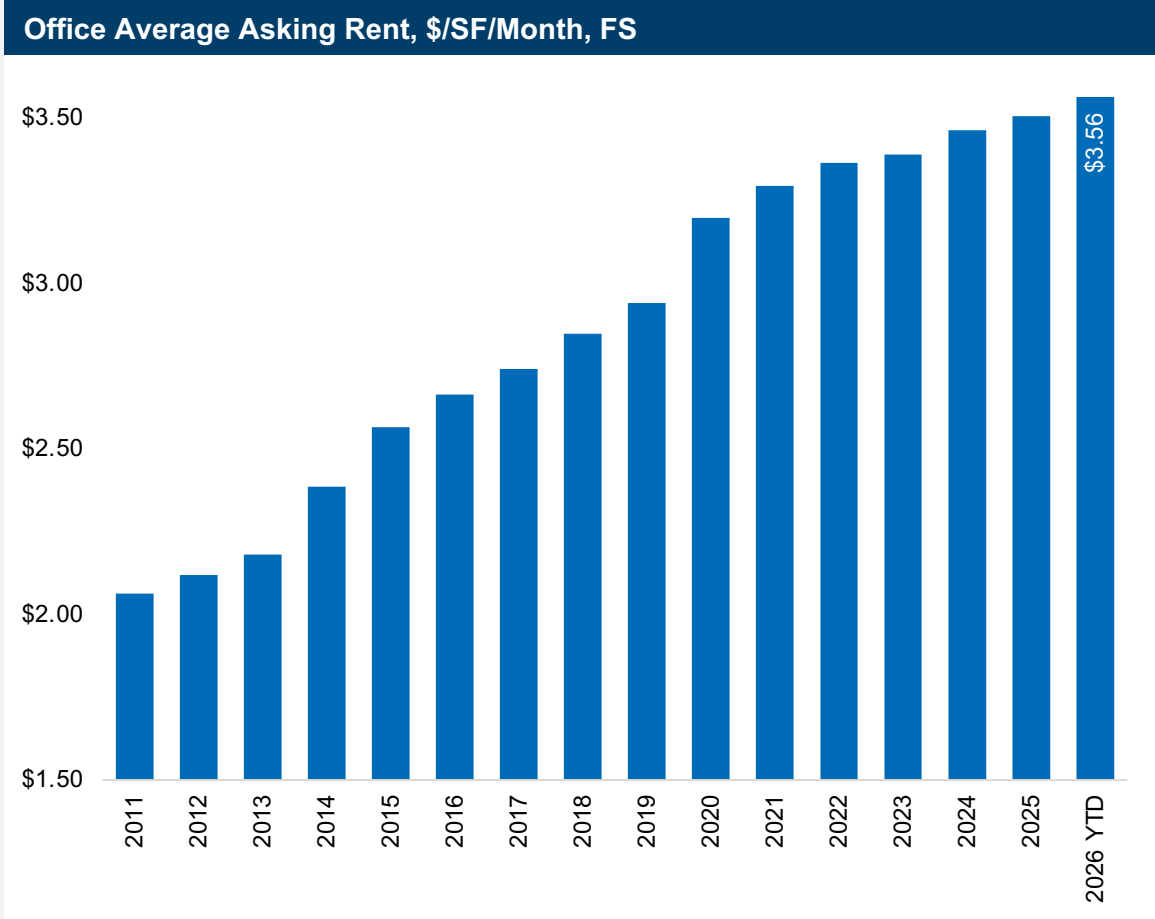
Construction Levels Continue to Retreat from Record High

Office construction boomed during the recovery and is now quickly tapering off as market conditions soften. There are 800K SF in projects under construction, down from the all-time high of 6.2 MSF set in the fourth quarter of 2023. In 2025 the lender took control of The Campus at Horton, a troubled 745,000-SF creative-office conversion in Downtown where the developer was not making loan payments and construction had stalled, removing it from the construction pipeline without delivering.



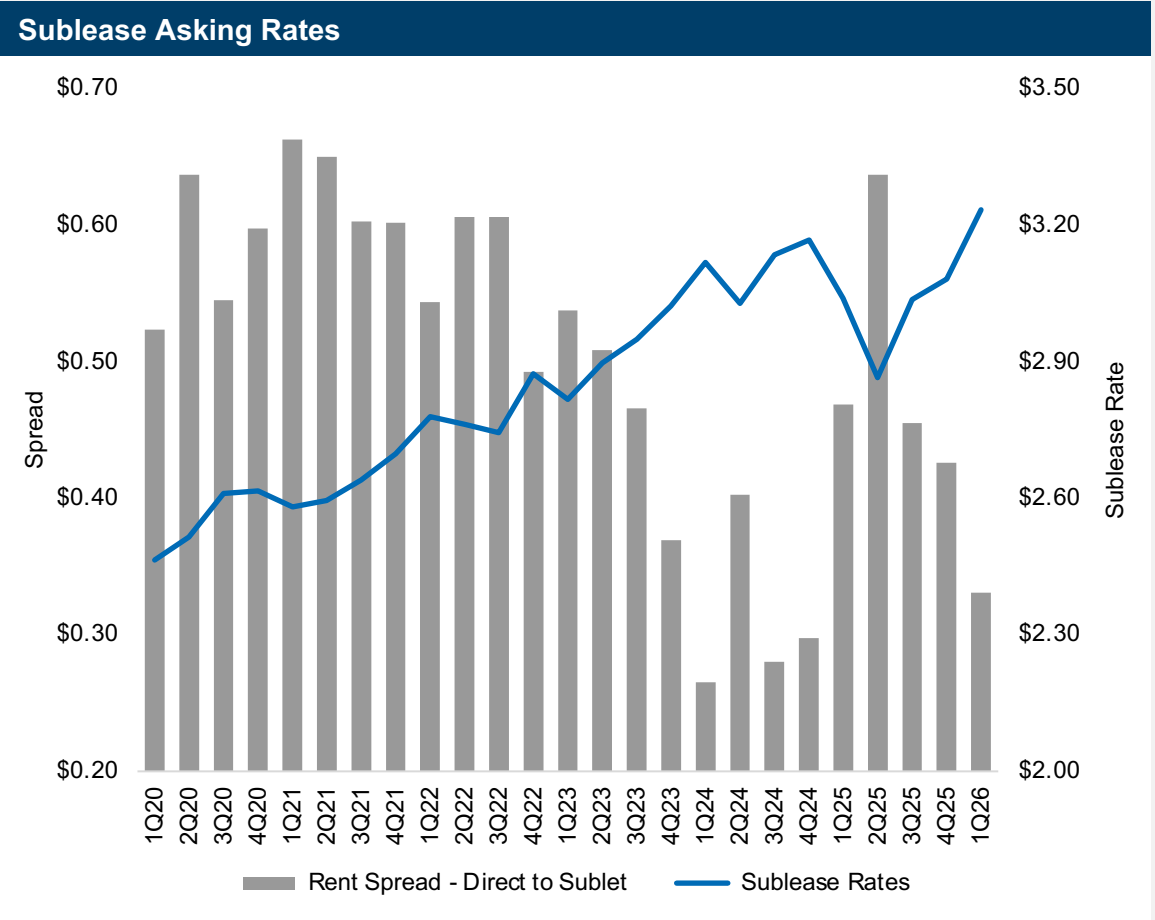
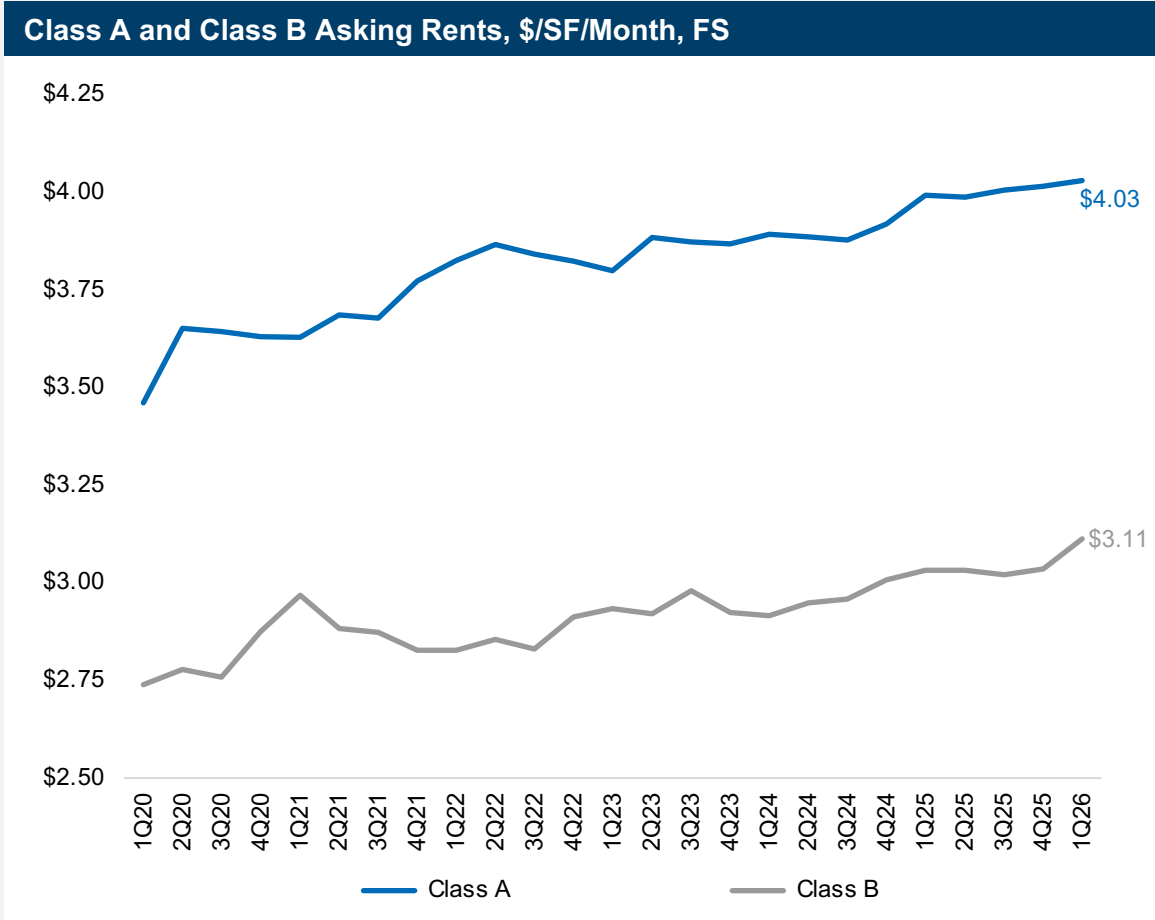
Rent Growth Driven by Newer Spaces But Begins to Stall

In the face of climbing vacancy rates, the average asking rate still managed to climb to an all-time high of \$3.56/SF, although this represented annual rent growth of only 1.6%. While rents have continued to increase modestly, annual rent growth has lagged the rate of inflation every year since 2021.



Class A and B Rents Maintain Spread

Class A rents have maintained a healthy premium to Class B rents with the delivery of new high-end space. Sublease rates fluctuated widely since 2023 as large blocks of modern space hit the market in the post-pandemic reassessment of space needs. The spread between sublease and direct rates currently represents an average discount of \$0.33/SF compared to direct space.



This Quarter's Notable Leases Were Diverse

The largest deal of the quarter was Northrop Grumman's renewal of a two-building project in Rancho Bernardo. In Mira Mesa, small-molecule biotech Neomorph leased a two-building project from Alexandria Real Estate Equities.

Notable 1Q26 Lease Transactions				
Tenant	Building(s)	Submarket	Lease Type	Square Feet
Northrop Grumman	16710-16750 Via Del Campo Ct	Rancho Bernardo	Renewal	168,072
<i>Defense contractor renewed facilities at two buildings in Rancho Bernardo.</i>				
Neomorph	5810-5820 Nancy Ridge Dr	Mira Mesa	New Lease	84,354
<i>Clinical-stage biotech company leased office and lab space at two Alexandria Real Estate Equities buildings.</i>				
State of California	765 3rd Ave	Chula Vista	Renewal	24,289
<i>The state's Department of Corrections renewed its office in Chula Vista.</i>				
SDRE Homebuilders	12777 High Bluff Dr	Del Mar Heights	New Lease	22,511
<i>Middle-income housing developer leased a full floor at Kilroy Realty's One Paseo Junction.</i>				
Clark Construction	2100 Kettner Blvd	Downtown	New Lease	14,187
<i>Building and infrastructure contractor leased new space on the 5th floor at Kilroy Realty Corporation's project in Little Italy.</i>				

Brent Don
Research Manager
San Diego
brent.don@nmrk.com

Dain Fedora
Head of Research
Southwest
dain.fedora@nmrk.com

San Diego
4655 Executive Dr, Suite 800
San Diego, CA 92121
t 858-875-3600

New York Headquarters
125 Park Ave.
New York, NY 10017
t 212-372-2000

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