RESEARCH Q3 2022

San Diego Office Market Report

Market Fundamentals Remain Positive but Flatten Out

- The average asking rent hovered near its all-time high, falling slightly to $3.33/SF from the previous quarter's record of $3.34/SF. The average was up 2.6% over the past year, decelerating from the average of 4.4% annual rent growth over the past three years.
- Total vacancy remaining unchanged at 14.4% as direct vacancy ticked down 10 basis points but sublet vacancy increased by an equal amount.
- Net absorption posted 262,692 square feet of gains for the quarter, with particularly strong absorption of 112,875 square feet in the Sorrento Mesa submarket. This brought the year-to-date total to 806,682 square feet of positive net absorption.
- Sublease availability continued to increase, reaching nearly 2.3 million square feet.
- Two new projects delivered 380,428 square feet of new inventory, with another 4.0 million square feet under construction.

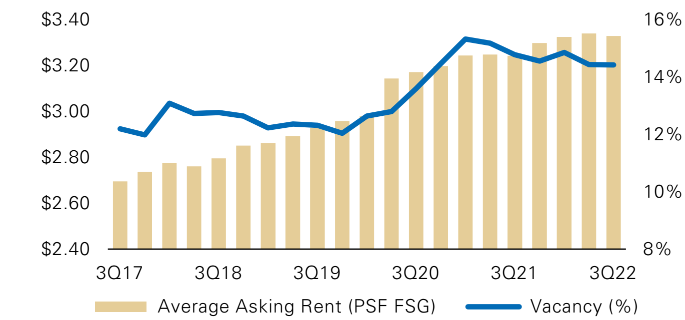
Large Sale Transactions Shrug Off Headwinds

Sales volume for the quarter totaled $557.2 million, down 6.1% compared to a year ago and totaling $2.2 billion over the past year. The running four-quarter sales volume peaked back in the first quarter of 2022 when it reached an all-time high of nearly $2.9 billion and has trended down since that time as rising interest rates have cooled the pace of capital markets activity. Despite this relative slowdown, some groups continue to make large acquisition plays.

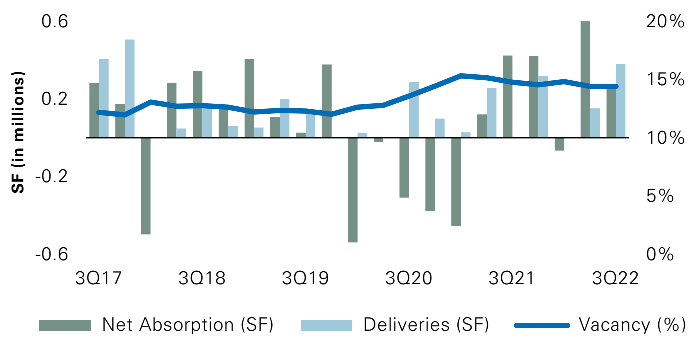
In Rancho Bernardo, Apple purchased the eight-building Rancho Vista Corporate Center from Swift Real Estate Partners for $445.0 million. The campus contains a mixture of office and flex buildings and has long housed technology companies, including Hewlett Packard and Intel. The purchase will eventually more than double Apple's footprint in Rancho Bernardo as the current tenants move

Market Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION, CONSTRUCTION DELIVERIES AND VACANCY



Market Summary

	Current Quarter	Prior Quarter	Year Ago	12-Month Forecast
Total Inventory (SF)	72.9M	72.8M	72.2M	↑
Total Vacancy Rate	14.4%	14.4%	14.8%	↑
Quarterly Net Absorption (SF)	263K	607K	-425K	→
Average Asking Rent/SF/Month	$3.33 FSG	$3.34 FSG	$3.24 FSG	→
Deliveries (SF)	380K	152K	0	↑
Under Construction (SF)	4.0M	4.4M	3.5M	↓

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out, adding 809,000 square feet to the 622,000 square feet Apple leases in the submarket.

In August, life science REIT IQHQ made the unusual move of purchasing the Hyatt Regency hotel for $227.3 million, assuming full control of the mixed-use Aventine property in UTC, the office and retail components of which it acquired last year. Although the new owner is expected to continue to operate the hotel as-is for the foreseeable future, ownership of this last piece will give IQHQ complete control over the planning process as it seeks to redevelop the rest of the 11.2-acre site as a life science campus.

Employment and Economic Outlook

San Diego's unemployment rate was 3.4% in August, down 310 basis points over the past year as the region added 59,600 jobs to its total nonfarm employment, including 12,400 office-using jobs. As the economy shifted from recovery to expansion mode in mid-2022, the unemployment rate has bounced around the low 3% range with a smaller pool of unemployed labor to recruit from.

Now, a period of uncertainty lies ahead as companies try to gauge the impact of a variety of rapidly changing macroeconomic factors, including rising interest rates, inflation, economic issues abroad and continued repercussions from the war in Ukraine.

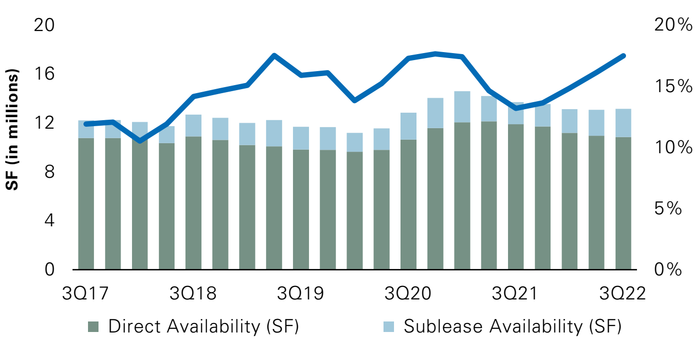
Sublease offerings are likely to continue to increase as employers take advantage of the willingness of employees to work from home to shed nonessential office space and cut real estate expenses.

The technology sector has been propping up the office market with large leases and developments over the past several years. If the tech giants were to halt these expansion pushes, it would take the wind out of the sails of leasing activity and likely push absorption into the red.

A large pipeline of modern office space is set to deliver soon, especially in Downtown, where the submarket is already more than a quarter vacant. This surge of new space may finally tip rents over the peak and lead landlords to start reducing asking rates.

Sublease vs. Direct Availability (SF)

AND SUBLEASE AS A % OF OVERALL AVAILABLE SF



Office-Using Employment

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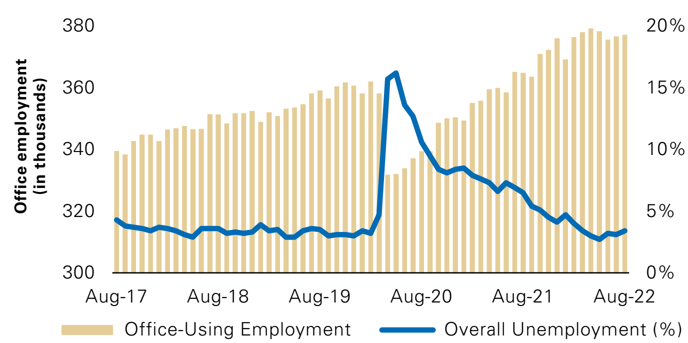

Source: U.S. Bureau of Labor Statistics (Preliminary data, not seasonally adjusted). Includes information, financial activities and professional and business services jobs.

Lease Transactions

Tenant	Building	Market Area	Lease Type	Square Feet
DLA Piper	4365 Executive Drive	UTC	Renewal	59,462
Maravai LifeSciences	5717 Pacific Center Boulevard	Sorrento Mesa	Sublease	54,232
National Funding	4380 La Jolla Village Drive	UTC	New	35,713

Sale Transactions

Buyer	Building(s)	Market Area	Sale Price (PSF)	Square Feet
Apple	16399-16409 W Bernardo Drive	Rancho Bernardo	$445,000,000 ($550/SF)	809,769
Tritower Financial Group	5909 & 5919 Sea Otter Place	Carlsbad	$88,750,000 ($394/SF)	230,907
Welltower	4180 La Jolla Village Drive	UTC	$57,000,000 ($570/SF)	100,000

Submarket Statistics

	Total Inventory (SF)	Under Construction (SF)	Total Vacancy Rate	Qtr Net Absorption (SF)	YTD Net Absorption (SF)	Class A Asking Rent (Price/SF)	Class B Asking Rent (Price/SF)	Total Asking Rent (Price/SF)
Downtown San Diego	**11,739,280**	**2,763,107**	**26.1%**	**-41,693**	**-70,911**	**$3.86**	**$2.94**	**$3.53**
Suburban Total	**61,180,311**	**1,286,954**	**12.2%**	**304,385**	**877,593**	**$3.75**	**$2.81**	**$3.23**
Carlsbad	5,508,413	0	15.6%	-19,224	156,549	$2.92	$2.71	$2.71
Chula Vista/South Bay/ National City	1,432,994	0	2.1%	-1,025	19,404	$2.82	$2.50	$2.75
Del Mar Heights/ Carmel Valley	5,541,571	519,300	17.7%	-6,648	-38,844	$4.79	$4.15	$4.64
East County	1,069,049	0	5.4%	-9,894	-37,095	$2.92	$2.09	$2.47
Escondido	511,722	0	11.4%	2,396	20,239	$2.32	$2.24	$2.31
Governor Park	846,865	0	7.5%	14,631	69,823	$3.12	$2.89	$2.90
Kearny Mesa	7,151,422	0	11.4%	43,149	96,596	$3.46	$2.53	$2.80
La Jolla	1,331,239	0	14.8%	-18,937	-57,612	$3.73	$3.14	$3.48
Mira Mesa/Miramar	795,006	0	7.0%	14,896	76,375	-	$2.31	$2.19
Mission Gorge/College	666,839	0	0.4%	71	5,056	-	$2.46	$2.23
Mission Valley	6,112,745	0	18.0%	-17,520	-116,522	$3.68	$2.90	$3.22
North Beach Cities	1,118,304	55,000	11.2%	-7,307	20,084	$4.13	$3.80	$4.13
Oceanside	524,182	0	6.5%	17,906	-1,739	$2.44	$1.58	$2.01
Old Town/Sports Arena/ Point Loma	1,071,724	0	7.7%	-23,910	7,499	-	$2.79	$2.74
Poway	1,071,188	0	20.5%	10,251	-142,505	$4.06	$2.34	$3.62
Rancho Bernardo	3,881,839	83,482	16.5%	23,311	-66,205	$3.49	$2.76	$2.81
Rose Canyon/Morena	516,097	0	14.4%	-1,765	-27,678	-	$1.93	$1.94
Scripps Ranch	2,116,385	0	12.8%	1,143	38,690	$3.15	$2.69	$2.90
Sorrento Mesa	6,563,419	163,205	11.2%	112,875	232,438	$4.11	$2.86	$3.45
Sorrento Valley	409,035	0	13.3%	-52	29,438	-	$2.91	$2.51
Torrey Pines	1,137,972	183,116	6.5%	-24,378	103,467	$4.43	$3.85	$4.22

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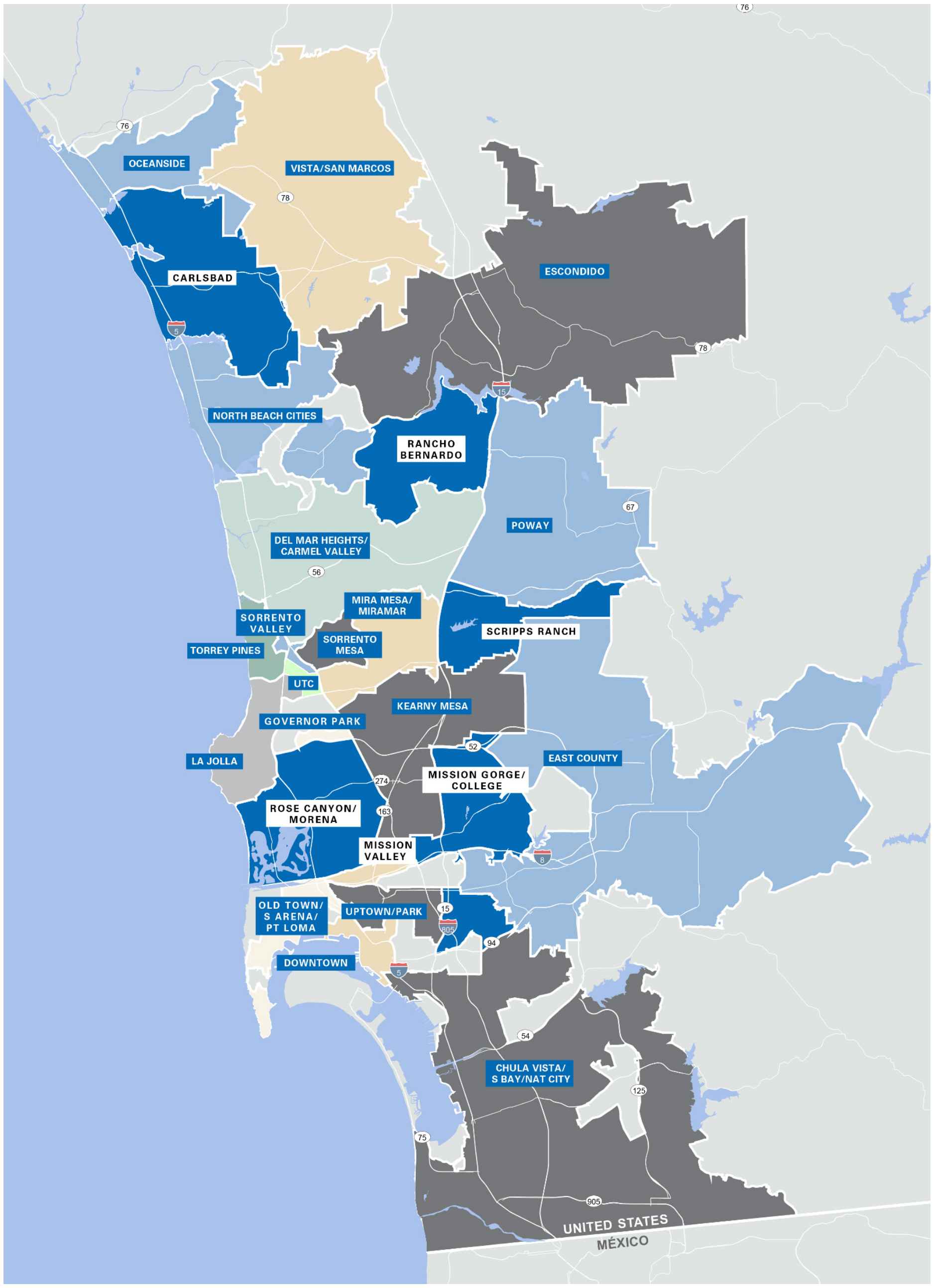
Uptown/Park	926,775	0	5.0%	16,630	74,040	-	$2.87	$2.82
UTC	9,559,308	282,851	6.5%	181,767	427,289	$4.40	$4.10	$4.36
Vista/San Marcos	1,316,218	0	19.6%	-3,981	-11,194	$2.36	$2.15	$2.33
Market	**72,919,591**	**4,050,061**	**14.4%**	**262,692**	**806,682**	**$3.80**	**$2.84**	**$3.33**

Under construction totals include ground-up construction only; under renovation and/or converted product is excluded. The same applies to construction deliveries.

Net absorption is the change in physically occupied space. A hypothetical vacant and available space could lease this quarter with the tenant set to take occupancy six months later; positive absorption is not recorded until this physical move-in occurs. The space will remain vacant, but not available, until occupancy.



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