

4Q24

# San Diego Office Market Overview



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# Market Observations

## Economy

- The region’s unemployment rate was 4.6% as of November 2024, up from 4.3% the previous year.
- Total nonfarm jobs grew by 8,900 over the past year, not enough to keep up with the growth of the labor force. Office-using jobs fell by 1,400 during this period and have declined 5.1% since their peak in October of 2022.
- The consumer price index for all urban customers in the San Diego metropolitan area was up 2.6% year-over-year in November 2024, down from an annual rate of 5.2% in November 2023 and 6.7% in November 2022.
- In April 2024, the 12-month median sale price for a single-family home in San Diego County surpassed \$1,000,000 for the first time and continued to climb from there, reaching \$1,050,000 by December.

## Major Transactions

- A joint venture between Harbor Associates and F&F Capital purchased the five-building Highlands Corporate Center in Del Mar Heights from EQ Office for \$77.0M.
- SACA Development purchased 101 W Broadway in Downtown from the Irvine Company for \$43.9M.
- A new film studio called Chula Vista Entertainment Complex leased two buildings totaling 165,000 SF in the mixed-use, master planned Millenia project. The first phase is already under construction and will consist of coworking space, audio and film studios and post-production facilities. The second phase is scheduled to be built over the next three years and will include virtual production facilities for film and television.

## Leasing Market Fundamentals

- The average monthly asking rate was \$3.45/SF in the fourth quarter, up 2.6% over the past year. This rent growth matched the rate of inflation in the region, meaning rents have remained essentially flat.
- Net absorption was positive this quarter, posting 336,407 SF, bringing the annual total to 588,521 SF in net occupancy gains.
- Total vacancy ticked down slightly to 16.8%, down 30 basis points from the previous quarter but up 150 basis points over the past year.
- No new projects delivered during the quarter, leaving 5.3 MSF of projects under construction, down from the all-time high of 6.7 MSF at the start of the year.
- Sublease availability fell to 3.2%, although this decline was driven mainly by sublease listings that were withdrawn from the market rather than being leased.

## Outlook

- Vacancy will continue to climb until the high level of speculative construction subsides towards the end of 2025.
- The high-end office market will face increased competition from new developments originally intended for life science use that failed to secure biotech tenants during their construction.
- Underperforming office buildings will continue to sell for conversion to multifamily, particularly in Downtown where demand for apartments is much higher than for office.
- The Federal Reserve has signaled two more interest cuts are likely in 2025, which should spur more investment activity after two years of high interest rates and low sales activity.

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# Economy

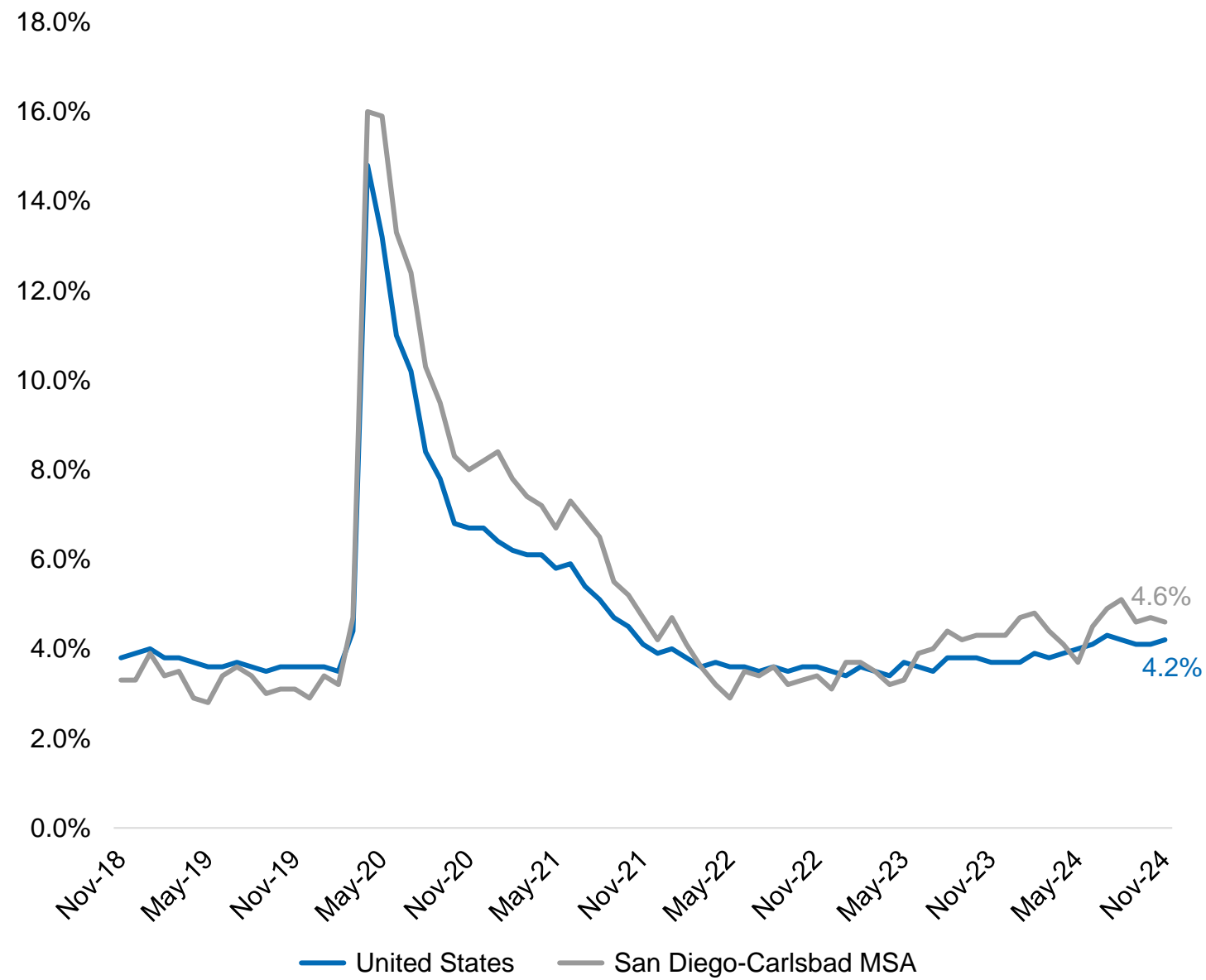




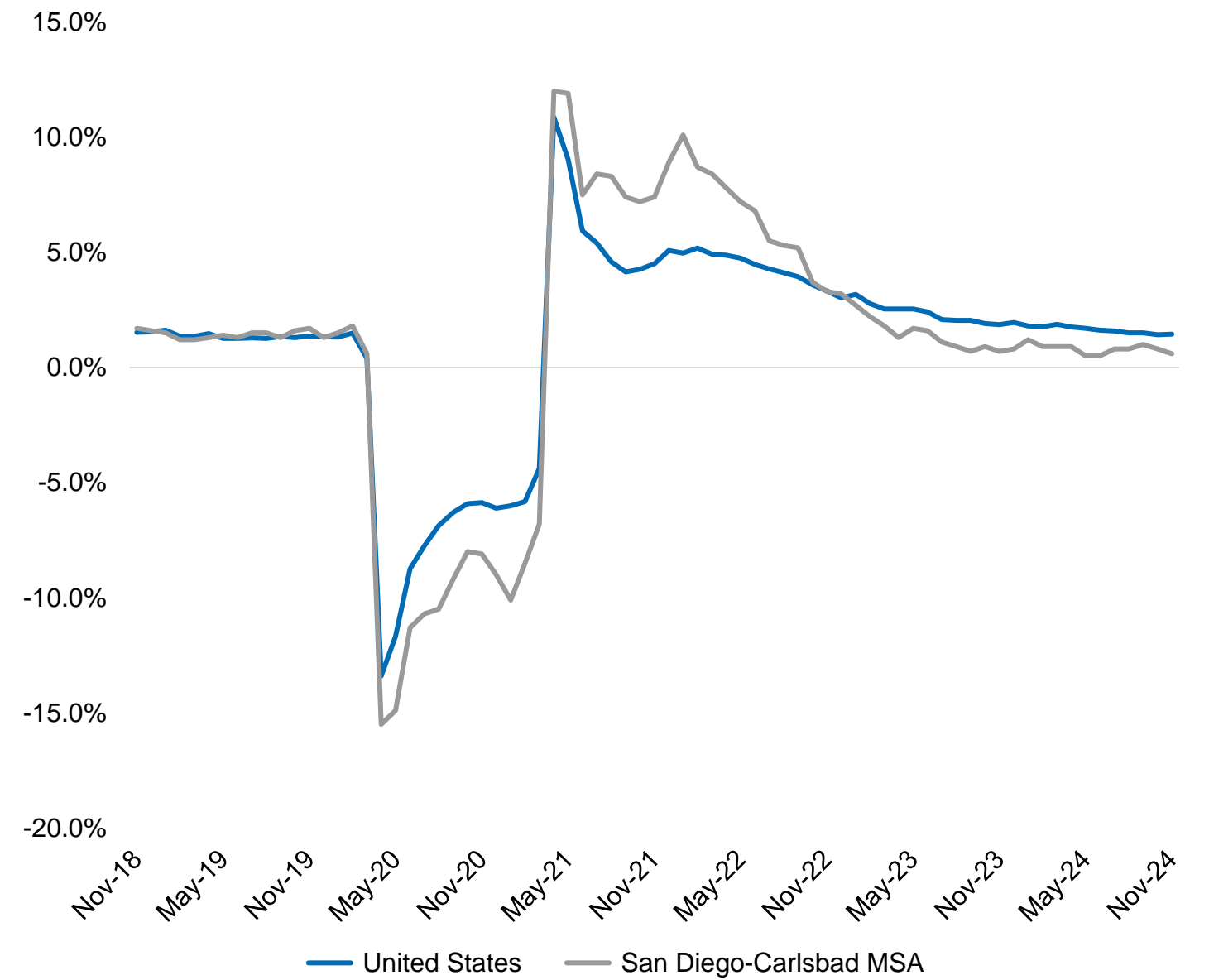
# Unemployment Ticks Up to a Three-Year High

The local unemployment rate was 4.6% in November 2024, up 30 basis points over the past year. During this time nonfarm employment has continued to post modest but positive gains: employers reported an additional 8,900 jobs over the past year, representing growth of 0.6%, trailing the national average of 1.4%. A rising unemployment rate despite overall job gains shows that the labor force is growing faster than new jobs are being created.

Unemployment Rate, Seasonally Adjusted



Nonfarm Payroll Employment, Non-Seasonally Adjusted, 12-Month % Change



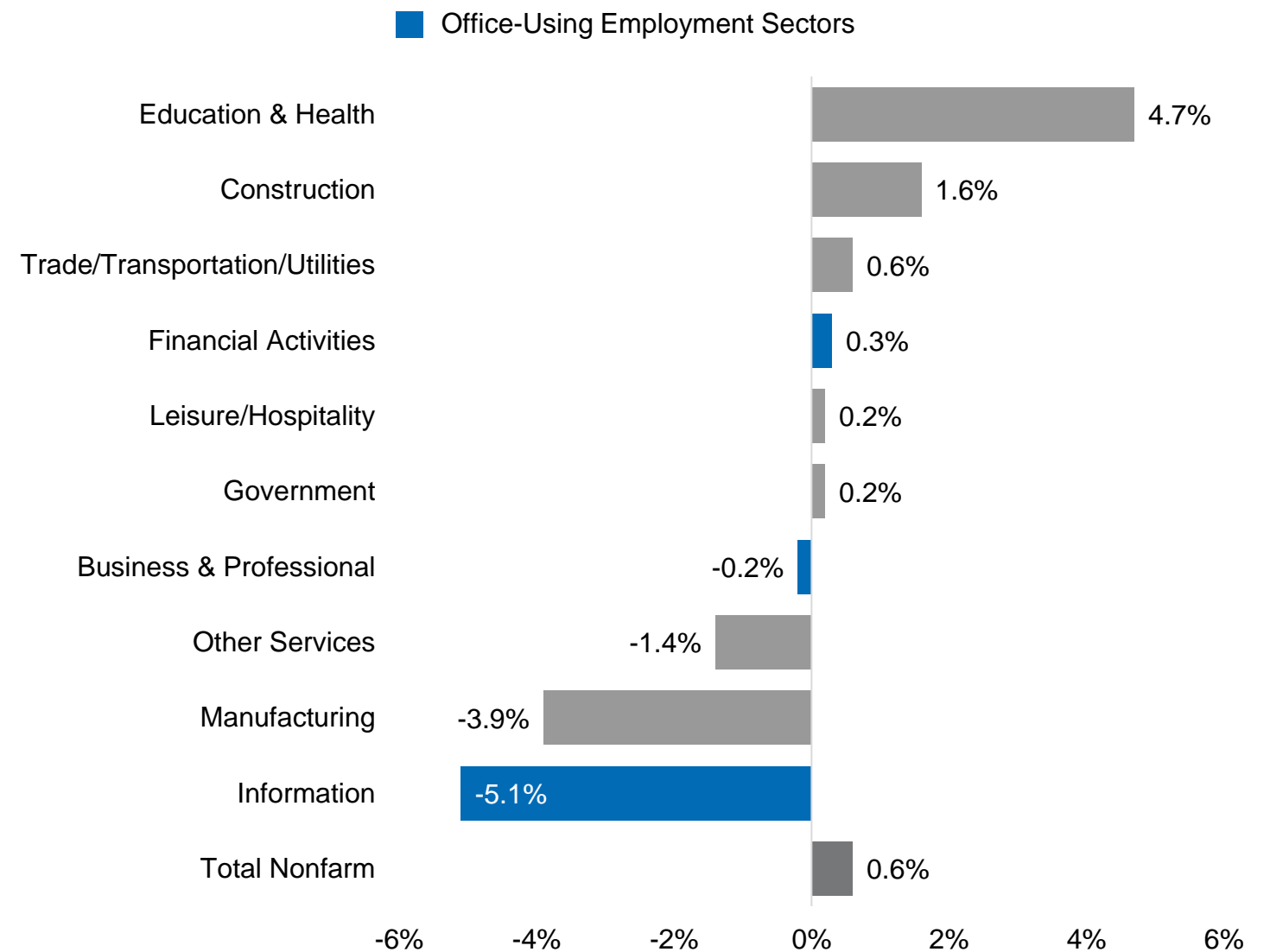
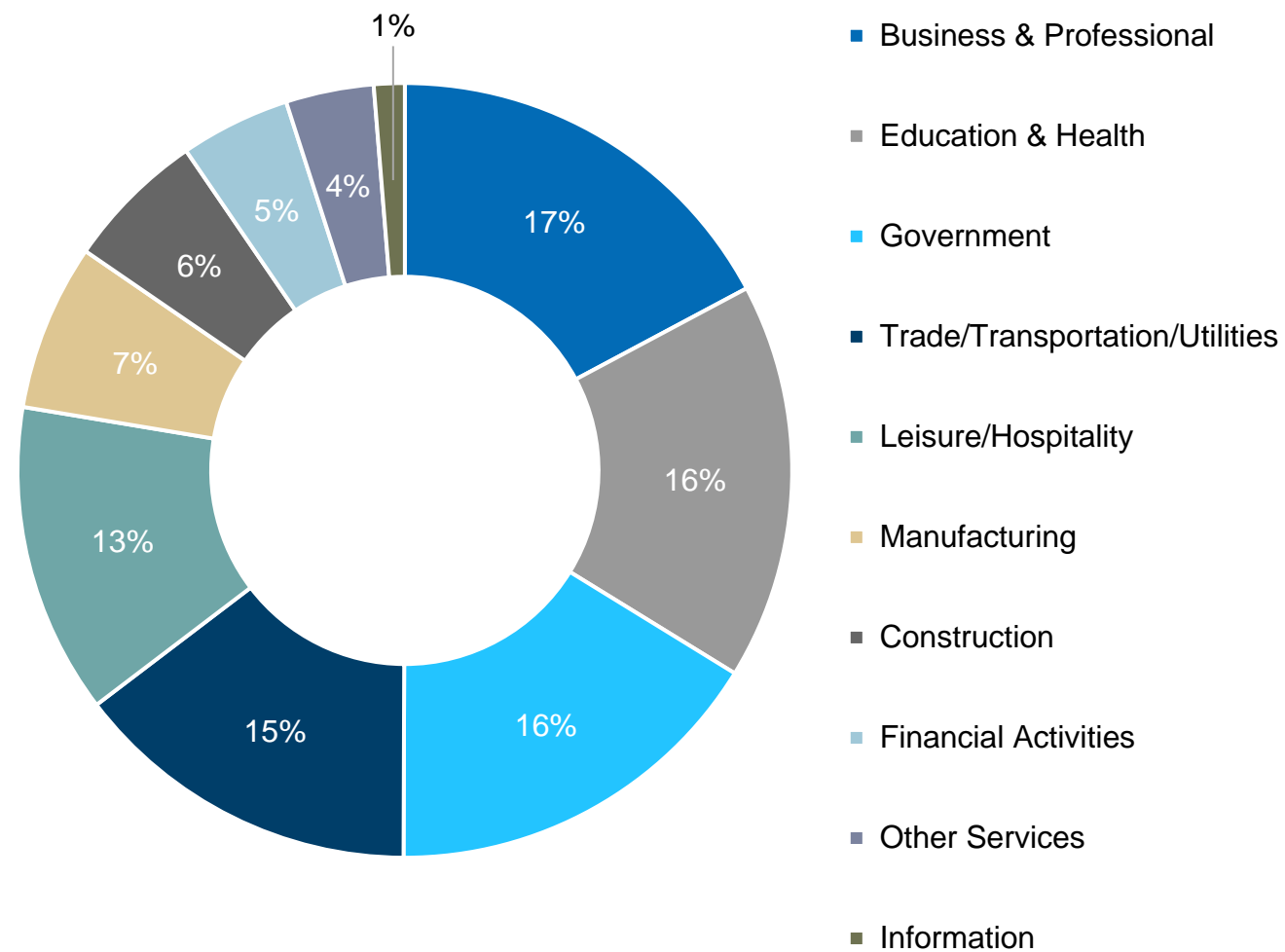
Source: U.S. Bureau of Labor Statistics, San Diego-Carlsbad MSA

# Primary Office-Using Job Sectors Decline

Business and professional services is the single largest employment sector in the region, fueling white-collar jobs and office demand, but the industry has contracted by 0.2% over the past year. The government and education and health sectors, meanwhile, have grown to be nearly as large in terms of their numbers of jobs. Office-using jobs in the smaller financial activities industry grew slightly by 0.3% and the information industry contracted by 5.1% over the past year.

Employment by Industry, November 2024

Employment Growth by Industry, 12-Month % Change, November 2024

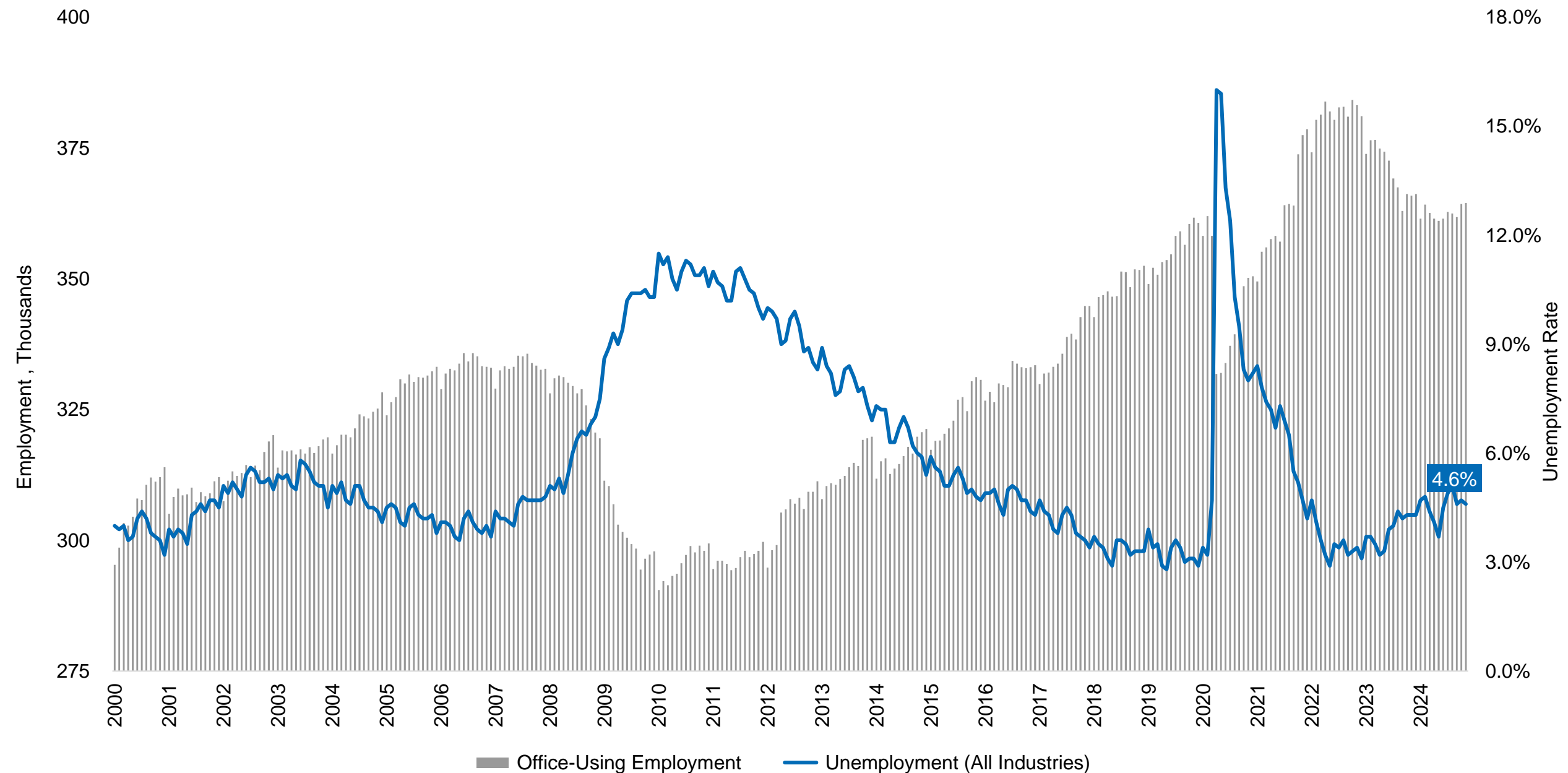


Source: U.S. Bureau of Labor Statistics, San Diego-Carlsbad MSA

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

In 2022 San Diego reached a 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 1,100 jobs over the past year and professional and business services cut 500 jobs. By contrast, the education and health services sector had the best performance over the past year, adding 11,800 jobs.

## Office-Using Employment\* and Unemployment Across All Industries



Source: U.S. Bureau of Labor Statistics, San Diego-Carlsbad MSA

Note: November 2024 data is preliminary.

\*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.



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# Leasing Market Fundamentals

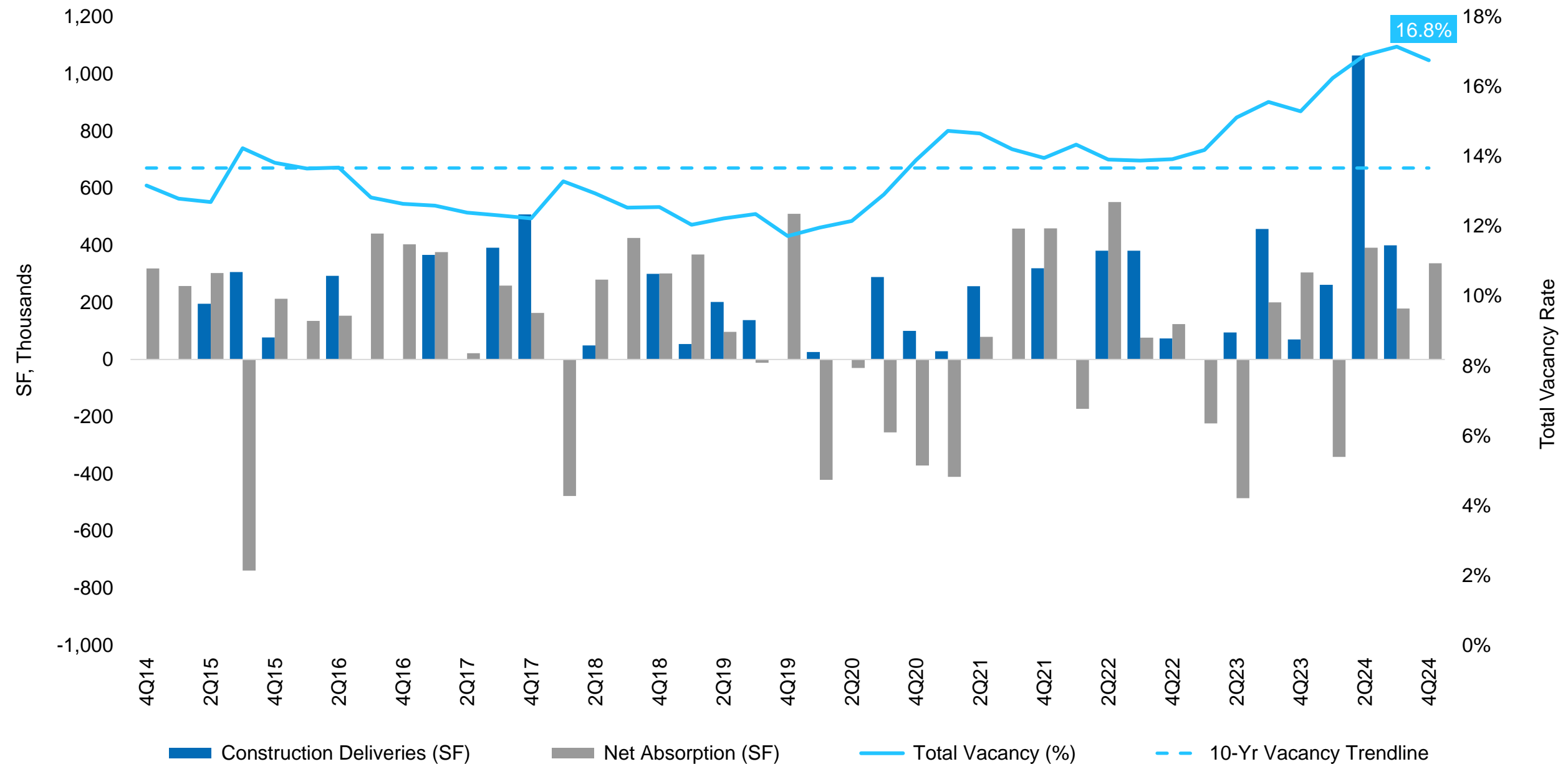




# Vacancy Levels Out After Climbing From High Deliveries

2024 saw 1.7 MSF of new inventory due to construction deliveries, the largest amount of new space in over a decade. Although the market posted 588,521 SF of positive net absorption for the year, the large volume of new product has still caused total vacancy to climb to the highest levels in a decade, currently at 16.8%. Vacancy will climb over the short-term as the 5.3 MSF in current construction projects continue to deliver over the next year or two.

Historical Construction Deliveries, Net Absorption and Vacancy



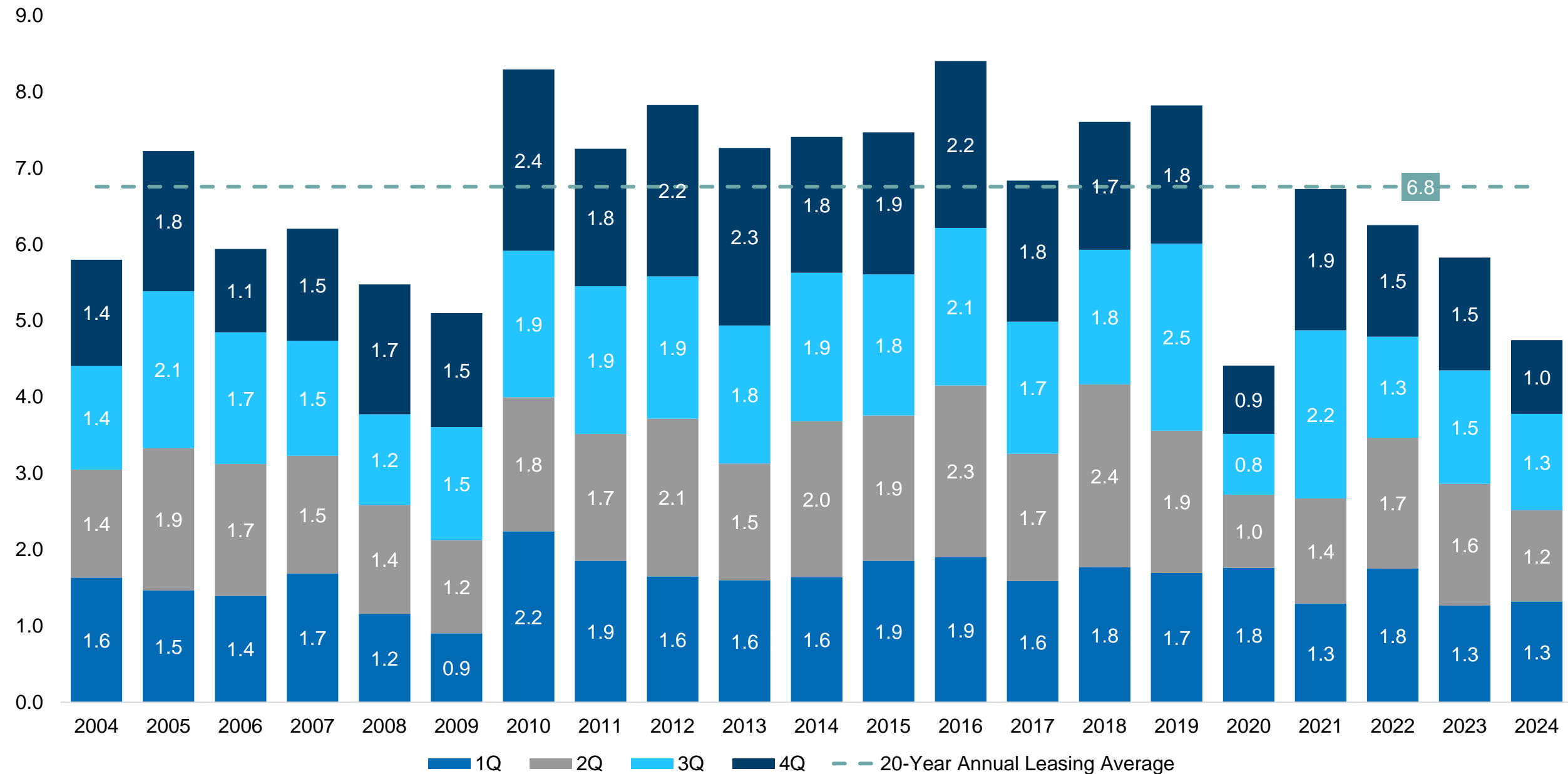
Source: Newmark Research



# Leasing Activity Continues to Slow

Leasing activity has lagged the historical annual average of 6.8 MSF every year since 2019 and has steadily decreased every year since 2021. 2024 recorded only 4.7 MSF in annual leasing activity, the second lowest total in 20 years, second only to 2009 in the wake of the Global Financial Crisis. Demand has softened amid office-using job declines and economic shifts to other employment sectors.

Total Leasing Activity (MSF)



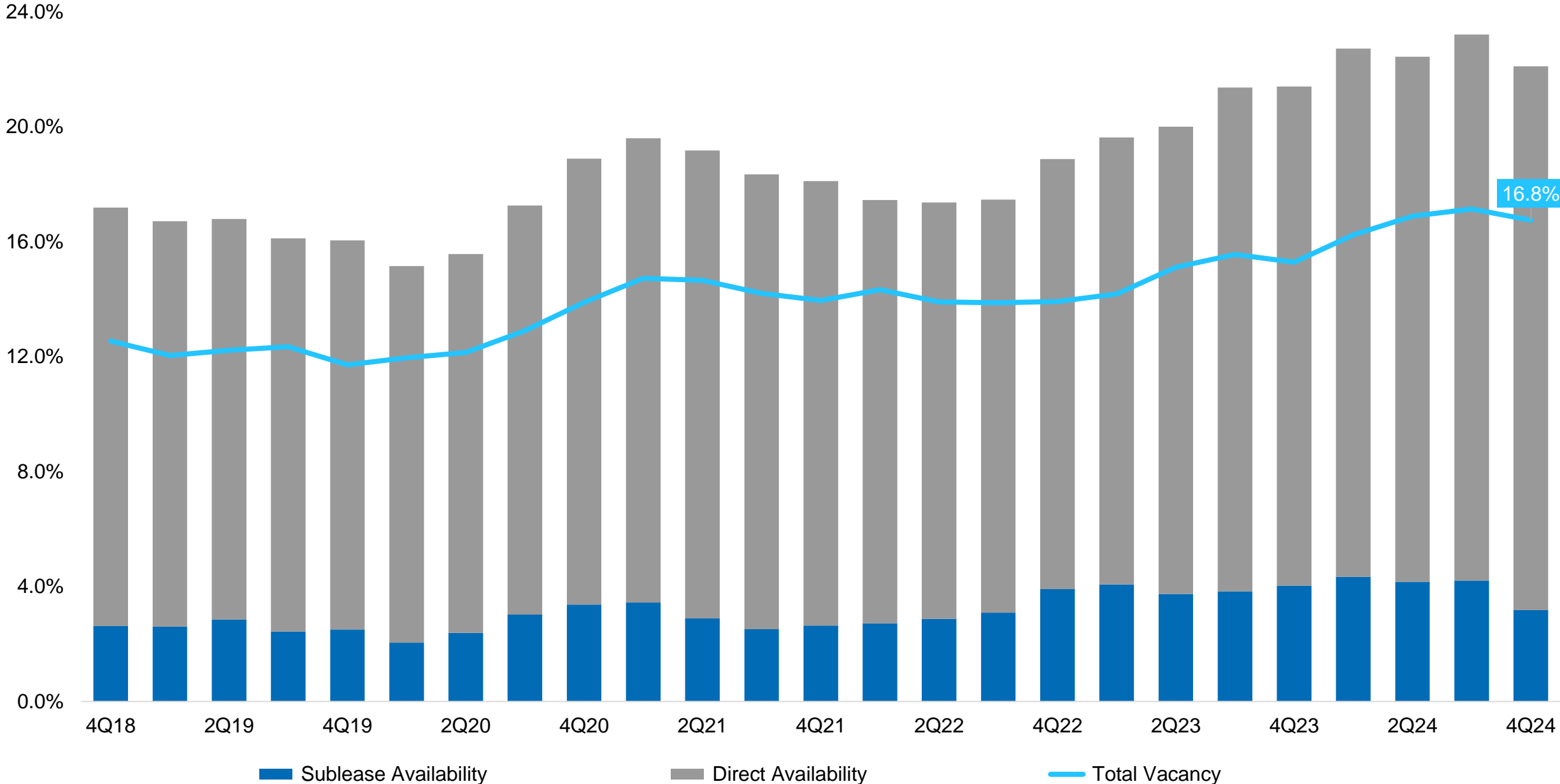
Source: Newmark Research, CoStar



# Vacancy and Availability Remain Elevated

Vacancy has climbed from 14.9% two years ago to 16.8% by the end of 2024 as supply has consistently outstripped demand for new space. Sublease availability dipped to close out the year, although this decline was mostly due to sublease offerings being withdrawn from the market rather than leasing activity.

Available Space and Total Vacancy as Percent of Overall Market



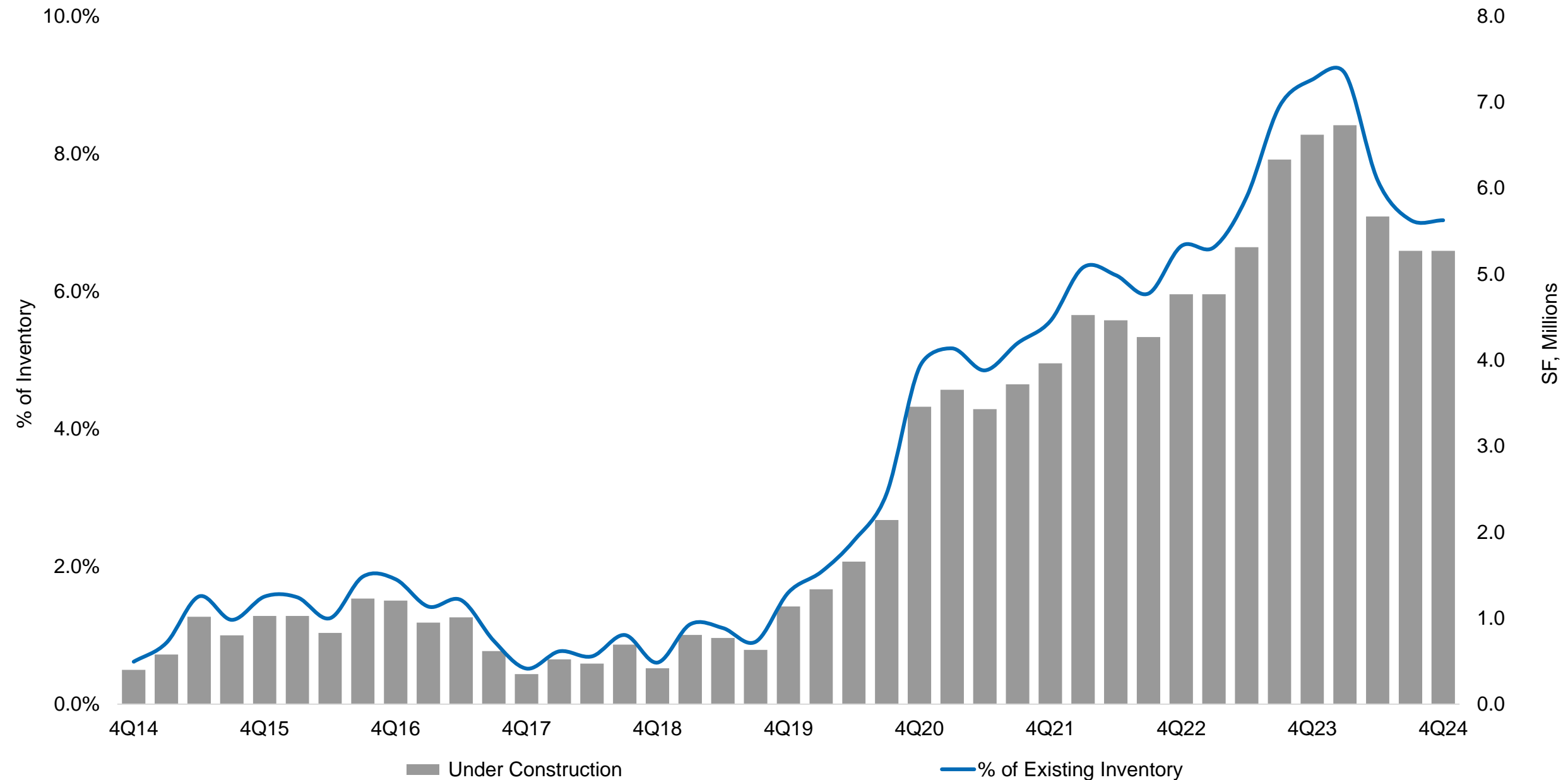
Source: Newmark Research



# Construction Starts to Decline from Record High

Office construction boomed during the recovery and is now tapering off as market conditions soften. There is currently 5.3 MSF in projects under construction, down from the all-time high of 6.7 MSF set in the first quarter of 2024. Downtown has the most construction activity, including IQHQ's Research and Development District (a ground-up, 1.7-MSF life science and office campus) and Stockdale Capital's Horton Plaza (a 700,000-SF creative-office conversion of an obsolete shopping mall).

Office Under Construction and % of Existing Inventory

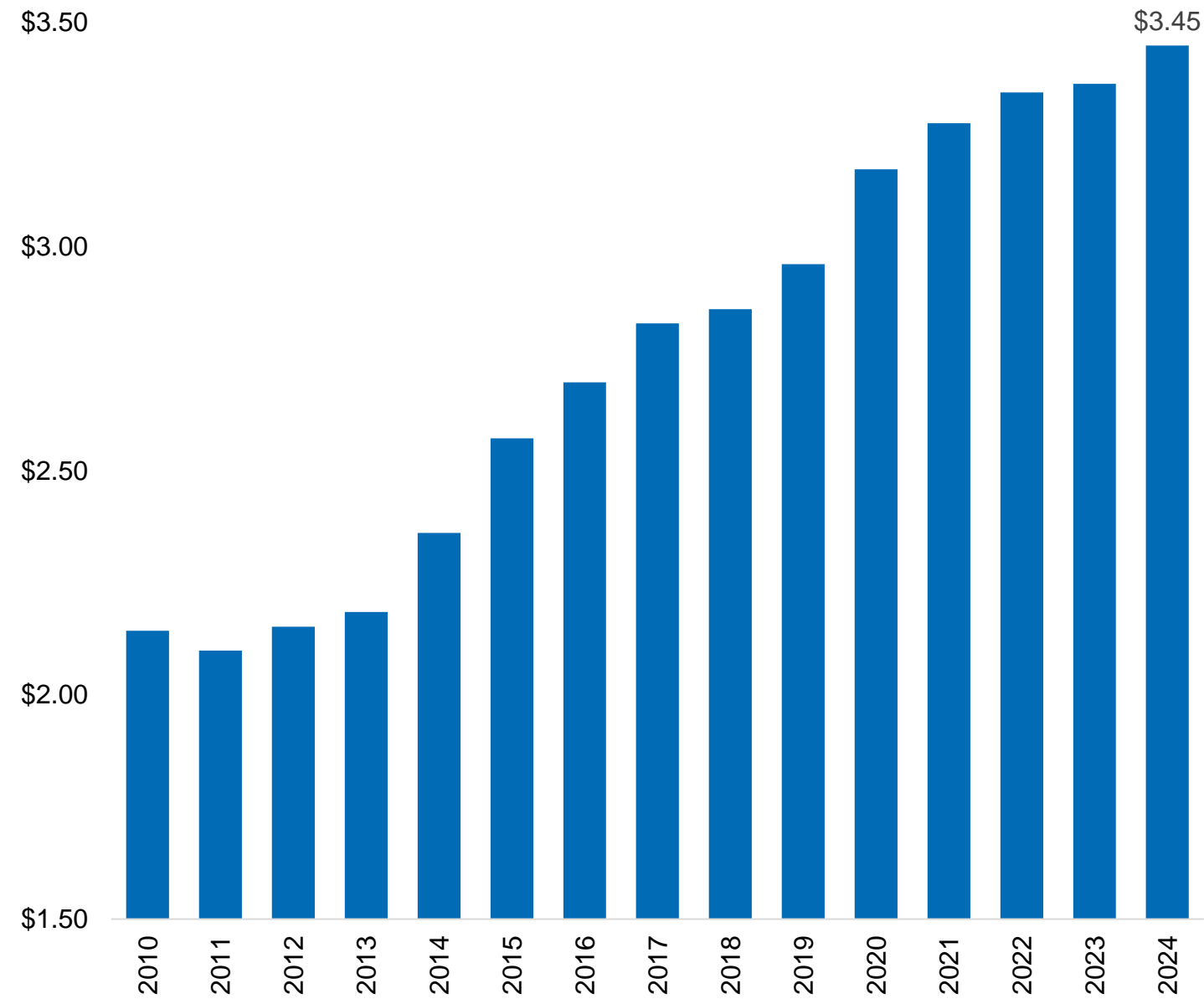


Source: Newmark Research, CoStar

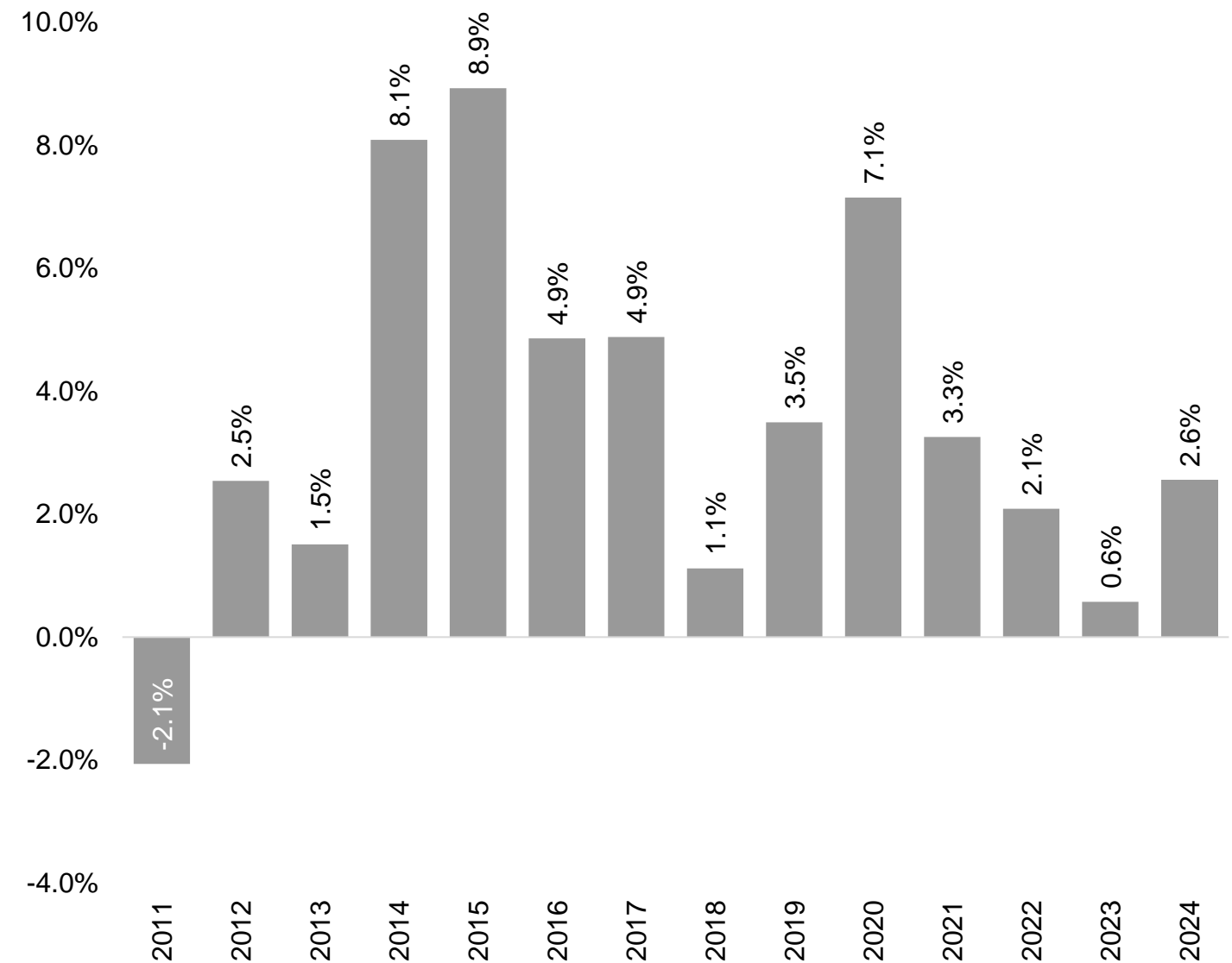
# Rent Growth Driven by High Availability of Newer Spaces

The average asking rate climbed to \$3.45/SF from \$3.36/SF last year, an annual increase of 2.6%. Modest rent growth has continued despite elevated vacancy due to the amount of newer, more expensive space hitting the market. Rent growth has lagged or matched the rate of inflation every year since 2021.

Office Average Asking Rent, \$/SF/Month, FS



Year-over-Year Asking Rent Growth Rate



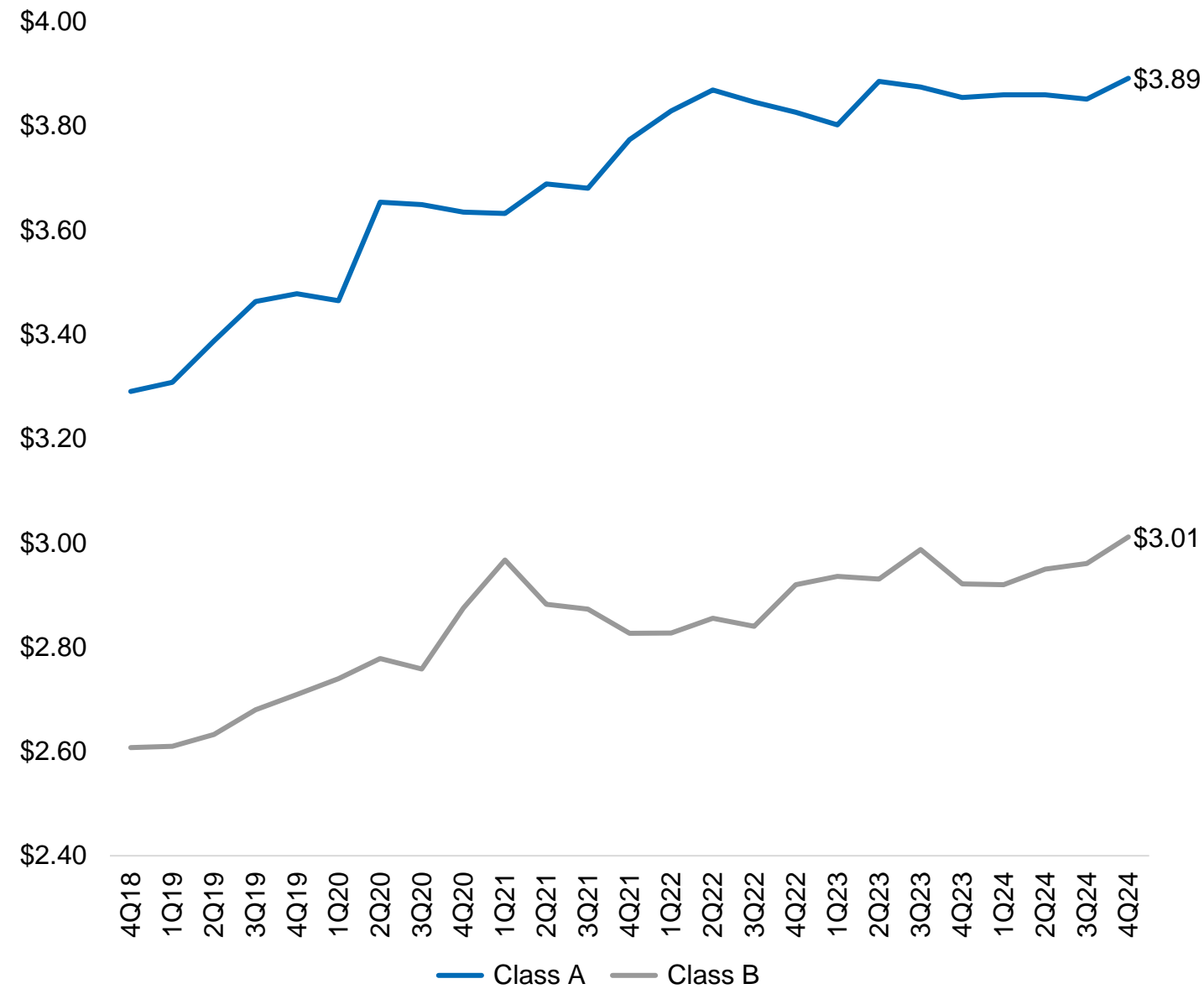
Source: Newmark Research, CoStar



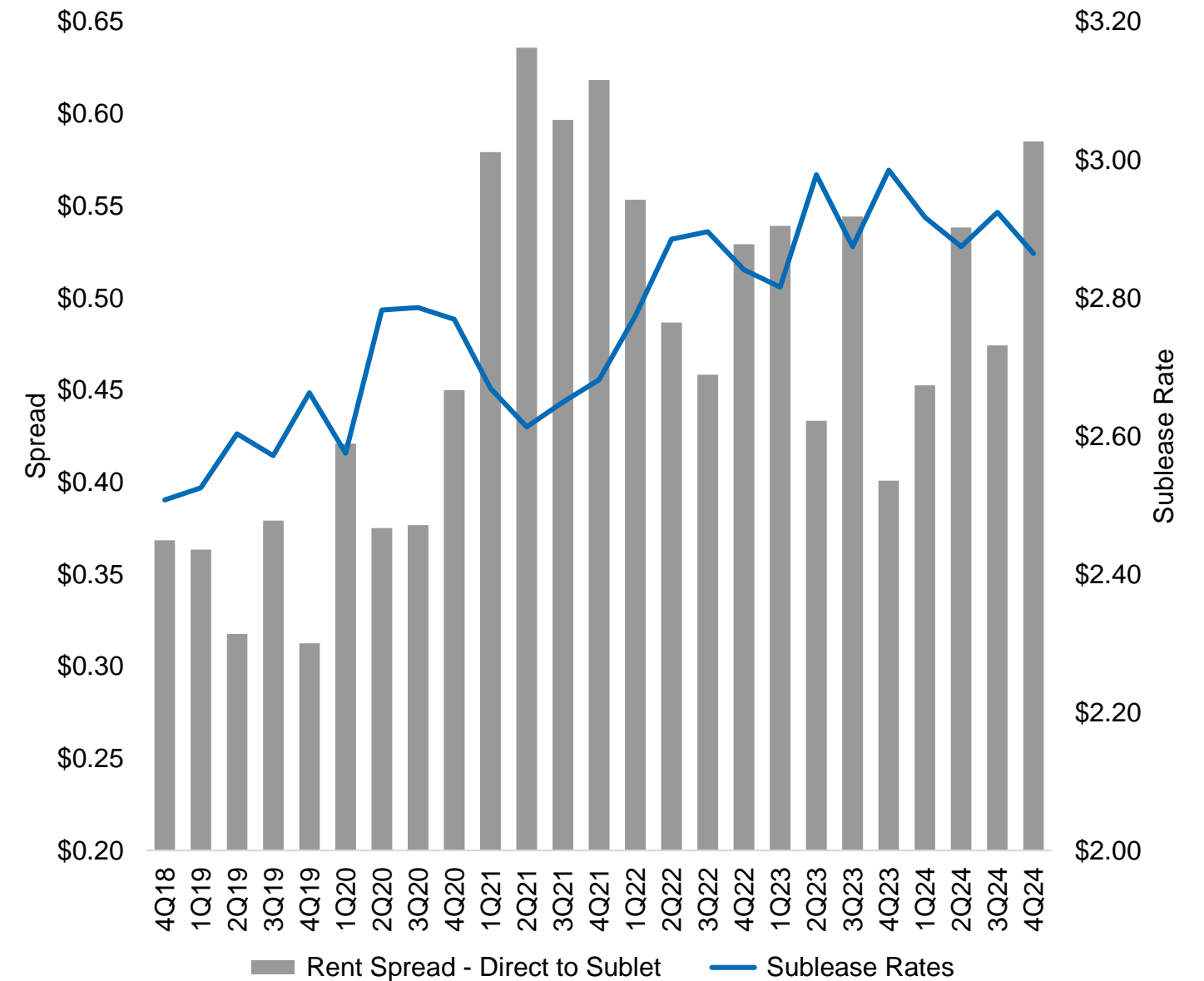
# Class A and B Rents Maintain Spread

Class A and Class B rents have tracked one another closely over the last two years as they have both grown at a moderate pace. Sublease rates have fluctuated more widely as large blocks of modern space have periodically hit the market. The spread between sublease and direct rates has grown since 2019, when it was unusually low at \$0.31/SF, and sublease space currently averages a \$0.59/SF discount to direct space.

Class A and Class B Asking Rents, \$/SF/Month, FS



Sublease Asking Rates



Source: Newmark Research, CoStar

# Notable Lease Transactions

The largest lease of the quarter was for film production studio called Chula Vista Entertainment Complex, which seeks to rekindle a Hollywood-style film and television industry in the mixed-use Millennia development in Chula Vista. The other notable lease transactions were all located in central submarkets.

## Notable 4Q24 Lease Transactions

Tenant	Building(s)	Submarket	Type	Square Feet
Chula Vista Entertainment Complex	1775 Millennia Ave	Chula Vista	New Lease	75,000
<i>Phase 1 of the CVEC film production project will include video-editing bays, sound-effects facilities, audio post-production studios, coworking and office space in the Millenia Library building.</i>				
Chula Vista Entertainment Complex	1785 Millennia Ave	Chula Vista	New Lease	90,000
<i>Phase 2 of the CVEC project, the company plans to develop a virtual production studio campus.</i>				
Kura Oncology	4930 Directors Pl	Sorrento Mesa	New Lease	32,512
<i>Public cancer research company leased a full floor at Directors Science Park.</i>				
Berkley Insurance Company	1615 Murray Canyon Rd	Mission Valley	New Lease	22,505
<i>Commercial insurance business signed a 10-year lease at Pacific Center II.</i>				
Jeff Tabor Group	501 W Broadway	Downtown	New Lease	20,465
<i>Commercial real estate brokerage leased a full floor in Downtown San Diego.</i>				



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## Most Large Spaces are in Newer Construction



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# Submarkets





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## Vacancy Highest in Downtown, Asking Rents Highest in Del Mar Heights

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## Sublease Availability by Submarket

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## Downtown Has the Most Construction, Portending More Vacancy to Come

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## Downtown Also Has a Large Pipeline of Ground-Up Multifamily Projects

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# Capital Markets & Life Science





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## Office Sales Volume Picked Up Modestly in 2024

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## Sales Volume Increases Slightly From Last Year

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# Private and Institutional Buyers Account for the Bulk of Investment

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## Price Per Square Foot Has Fallen as Cap Rates Have Recovered

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# Life Science Continues to Attract Funding

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# Life Science Mergers and Acquisitions Finish the Year Strong

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