

The background of the cover is a photograph of a city skyline, likely San Diego, with several tall buildings and a construction crane. In the foreground, a white speedboat is moving across the water, leaving a white wake. The sky is clear and blue.

**Yardi® Matrix**

**OFFICE MARKET REPORT**

# San Diego Investment Powers Ahead

Winter 2020

**Vacancy Rate  
Tightens**

**Construction Activity  
Moderates**

**Investment Stays  
Promising**

# SAN DIEGO OFFICE MARKET

Yardi® Matrix

## Vacancy Levels Decline

San Diego's office market fundamentals remained constant through the end of 2019. The total sales volume neared \$1.9 billion last year, surpassing 2018's number by roughly \$60 million. While most buyers were local and regional institutional investors, the metro also attracted out-of-state capital, particularly from companies based on the East Coast. Office and lab space in the University City, Kearny Mesa and Sorrento Valley submarkets comprised the bulk of transactions.

Office-using employment was strong throughout 2019, with the unemployment rate remaining at record lows. The professional and business services sector added 8,200 jobs year-over-year through November. Despite contracting by 200 jobs, the metro's information sector remains one of the best in the nation.

The office vacancy rate shrank to 11.5% as of December, making the competition for premier office space even tighter. The availability of modern assets featuring lab spaces remains one of San Diego's challenges, especially since more than half of the office inventory consists of Class B assets. Construction activity was moderate throughout 2019, with only 510,000 square feet delivered, the lowest total in the past five years. Projections remain positive as almost 1.3 million square feet was underway at the end of 2019, while nearly 10 million square feet was in the planning and permitting stages.

## Market Analysis

First Quarter 2020

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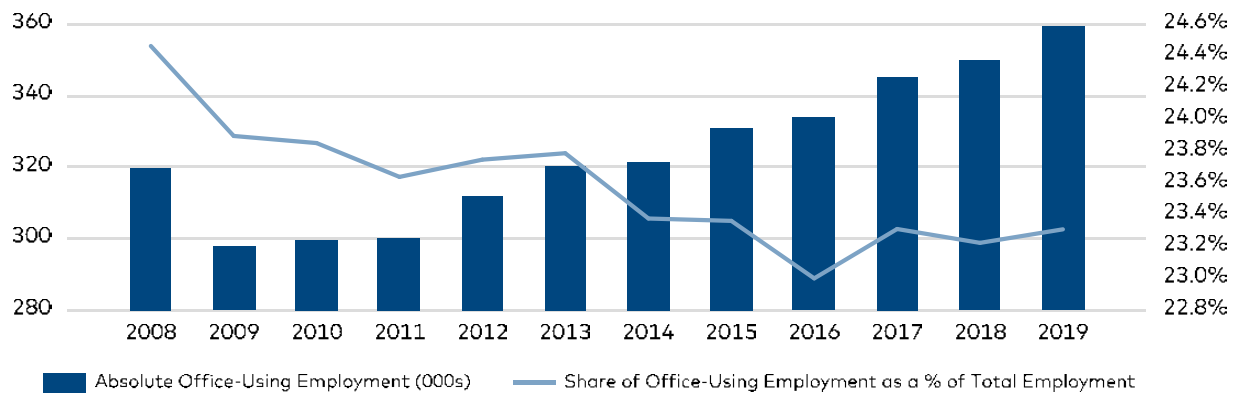
**Roxana Baiceanu**

*Associate Editor*

## ECONOMIC SNAPSHOT

- ▶ Office-using employment in San Diego grew by 7,200 jobs over the 12 months ending in November, for a 2.9% year-over-year increase. This brought the office-using segment to 23.4% of total employment or 180 basis points above the national average.
- ▶ Professional and business services led gains across all employment sectors, with 8,200 jobs gained in the 12 months ending in November, up 3.2% year-over-year. The only two sectors that recorded higher growth rates were mining, logging and construction (up 7.9%) and manufacturing (up 3.3%).
- ▶ The information and financial activities sectors continued to contract through the end of 2019. Financial activities slid by 800 jobs, while information lost 200 positions. Meanwhile, the massive hiring event announced by Apple is expected to continue this year. Teradata, which moved its headquarters from Ohio to San Diego in 2018, cut 80 positions in November.

### Office-Using Employment



Source: Bureau of Labor Statistics (BLS). Data as of December 2019

### Employment Growth by Sector as of December 2019 (Year-Over-Year)

Code	Employment Sector	Current Employment		Year Change	
		(000)	% Share	Employment	%
<b>60</b>	<b>Professional and Business Services</b>	<b>259</b>	<b>16.8%</b>	<b>9,500</b>	<b>3.8%</b>
15	Mining, Logging and Construction	92	6.0%	8,700	10.4%
90	Government	259	16.8%	6,800	2.7%
65	Education and Health Services	222	14.4%	6,400	3.0%
30	Manufacturing	119	7.7%	4,500	3.9%
80	Other Services	57	3.7%	1,200	2.1%
<b>55</b>	<b>Financial Activities</b>	<b>76</b>	<b>4.9%</b>	<b>200</b>	<b>0.3%</b>
<b>50</b>	<b>Information</b>	<b>24</b>	<b>1.5%</b>	<b>-300</b>	<b>-1.3%</b>
70	Leisure and Hospitality	200	13.0%	-1,100	-0.5%
40	Trade, Transportation and Utilities	232	15.1%	-1,100	-0.5%

Source: Bureau of Labor Statistics (BLS). Data as of December 2019

## LEASING | VACANCY

- ▶ The office vacancy rate in San Diego was 11.5% as of December. Steady absorption, paired with delays in new projects, continued to drive the vacancy rate down. Class B assets held steady at 12%, while demand for Class A space pushed its rate to 11.1%.
- ▶ Emerging coastal submarket Carlsbad continued to attract life science companies, compressing the area's average vacancy to 17.6% as of December.

### Vacancy by Submarket

Top Submarkets	Vacancy Rate (%)
University City	6.1%
West San Diego	6.8%
Poway	6.9%
Escondido-San Marcos	7.5%
East San Diego	8.8%

Source: Yardi® Matrix. Data as of January 2020  
Note: Vacancy including sublease

## LEASING | LISTINGS

- ▶ Some 8.2 million square feet of office space was available across San Diego; more than two-thirds of this space was located in suburban quadrants. Space in Class A assets was listed at \$43.67 per square foot. In the Torrey Pines submarket, per-square-foot rental rates in Class A assets reached \$63.75.
- ▶ With Apple expanding in University City by more than 200,000 square feet, absorption is set to remain strong in upcoming quarters.

### Available Properties

Top Submarkets	Square Feet Available	Properties Available
Downtown	1,423,640	35
Sorrento Valley	1,402,640	117
Carlsbad	1,092,610	86
University City	653,263	92
Kearny Mesa	652,300	73
<b>Total Market</b>	<b>8,389,580</b>	<b>774</b>

Source: Yardi® Matrix. Data as of January 2020

## COWORKING

- ▶ The expansion of the coworking sector slowed toward the end of 2019, with the total amount of space occupied by providers reaching 1.2 million square feet as of December. Half of the space is clustered in the Downtown, Carlsbad and University City submarkets.
- ▶ Regus remains the dominant provider of shared space in the market, with 18 locations across the metro. Premier Workspaces surpassed WeWork as the second most-active player, with eight offices and 144,000 square feet of coworking space.

### Top Coworking Tenants (Square Feet)

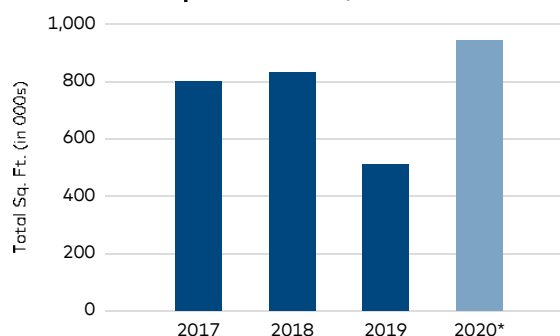
Coworking Tenant/ Operators	No. of Locations	Square Feet Leased
Regus	18	272,238
Premier Workspaces	8	144,150
WeWork	2	140,644
Spaces	3	99,970
Barrister Executive Suites	4	84,962

Source: Yardi® Matrix. Data as of January 2020

## SUPPLY

- ▶ Nine projects were underway in San Diego as of December, totaling 1.3 million square feet of office space or 1.5% of total stock. Due to labor shortages and rising construction costs, several upcoming developments had completion dates pushed back. Downtown had some 650,000 square feet underway—6.2% of office inventory—while Carmel Valley and University City had 285,000 square feet each.
- ▶ Construction activity in San Diego was moderate in 2019, with only 515,000 square feet delivered. This marked the lowest delivery in the past five years. Another 10 million square feet of space was in the planning and permitting stages.
- ▶ The largest project under construction in San Diego remains the U.S. Navy Headquarters, part of Doug Manchester's multibillion-dollar waterfront development, Manchester Pacific Gateway. Delivery for the 373,000-square-foot project, initially scheduled for mid-2020, has been pushed to late October.
- ▶ Another large project under construction is the two-building One Paseo, a 23-acre mixed-use development in the Carmel Valley submarket. While the first apartments opened in fall 2019, the office component is slated for delivery in March 2021. The project is expected to easily attract tenants, due to its close proximity to Sorrento Valley's cluster of tech and biotech communities.

### Office Completions (Square Feet)



Source: Yardi® Matrix. Data as of January 2020  
\*Total Year Projections

### Construction Activity

Top Submarkets	Square Feet Under Construction
Downtown	645,355
Mira Mesa–Rancho Penasquitos	300,000
Carmel Valley	285,550
University City	186,604
Torrey Pines	76,408
<b>Total Market</b>	<b>1,493,917</b>

Source: Yardi® Matrix. Data as of January 2020

### Construction Distribution

Top Submarkets	% of Inventory
Mira Mesa–Rancho Penasquitos	68.4%
Carmel Valley	6.8%
Downtown	6.2%
Torrey Pines	1.8%
University City	1.6%

## INVESTMENT TRANSACTIONS

- ▶ San Diego closed another strong year for office transactions, with the total sales volume nearing \$1.9 billion in 2019. This exceeded 2018's volume by approximately \$60 million, as interest in the metro's office assets, particularly from in-state investors, remained high.
- ▶ Sixty-five properties traded from January to December, with only a quarter of those representing Class A assets. The bulk of transactions remained concentrated in three key submarkets: University City (\$913 million), Kearny Mesa (\$299 million) and Sorrento Valley (\$220 million).
- ▶ The top three transactions in 2019 were all in the University City submarket and included the \$525 million La Jolla Commons Towers portfolio. American Assets Trust purchased the property from Hines Interests in June, becoming the metro's top buyer of the year.
- ▶ For medical office buildings, investors targeted the Escondido–San Marcos and South San Diego submarkets. In Escondido–San Marcos, three assets changed hands for a total of \$75 million, which included the \$46.9 million acquisition of Palomar Health Outpatient Center Phase I. Transaction activity in South San Diego was topped by Welltower's \$24 million purchase of Chula Vista Medical Arts I and II, a Class B portfolio encompassing nearly 100,000 square feet.
- ▶ Investment activity slowed toward the end of 2019, with only 12 properties trading during the last quarter. Half of the assets were located in Kearny Mesa and Carlsbad. The largest deal closed between September and December was CIM Group's \$90.4 million acquisition of The Terraces, a 200,000-square-foot property in Kearny Mesa.

### Transaction Volume

Top Submarkets	Total Transaction Square Feet	Total Transaction Volume (000s)
University City	1,288,238	\$913,225
Sorrento Valley	1,260,432	\$322,285
Kearny Mesa	1,062,334	\$306,256
Carlsbad	643,833	\$91,628
West San Diego	221,387	\$76,801
<b>Total Market</b>	<b>5,367,703</b>	<b>\$1,965,995</b>

Source: Yardi® Matrix. Data as of January 2020

### Average Price

Top Submarkets	Avg. Price Per Square Foot
University City	\$708.89
Carmel Valley	\$497.96
Escondido–San Marcos	\$444.07
West San Diego	\$411.71
Kearny Mesa	\$288.29

Source: Yardi® Matrix. Data as of January 2020

### Investment Activity

Top Buyers	Total Transaction Square Feet	Total Transaction Volume (000s)
American Assets Trust	717,836	\$525,000
Alexandria Real Estate Equities	599,087	\$398,100
IDS Real Estate Group	328,173	\$100,551
LaSalle Investment Management	158,341	\$91,000
CIM Group	201,661	\$90,364

Source: Yardi® Matrix. Data as of January 2020



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Swift Real Estate Lands \$112M Refi For R&D Campus

CBRE Capital Markets secured the floating-rate loan with Annaly Commercial Real Estate Group.



Life Science Campus To Break Ground

Healthpeak Properties is developing the \$164 million, 195,000-square-foot office and lab property.



North San Diego Office Asset Trades For \$24M

At the time of the sale, the 148,488-square-foot building housed four tenants.



Kilroy Realty Inks Major Lease

A large tech firm has agreed to occupy the upcoming 9455 TCD development in the University Towne Centre submarket.



CBRE Names San Diego VP

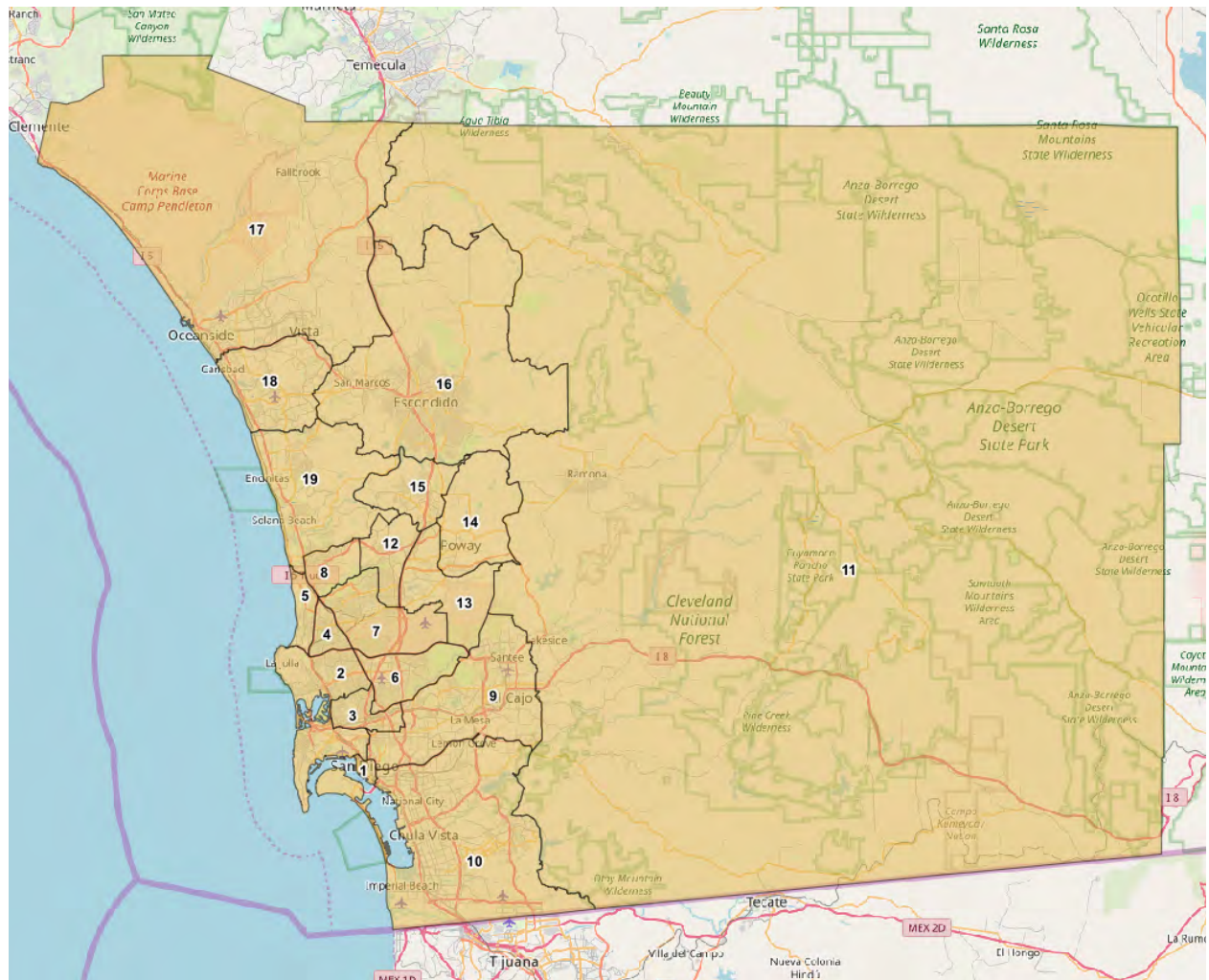
First Vice President Chris Williams brings nearly 13 years of experience to the firm, having previously served as an associate vice president with Colliers.



Irvine Co. Signs 5 Office Tenants

The five leases total approximately 26,000 square feet in a nearly 500,000-square-foot campus in Mission Valley.

# SAN DIEGO OFFICE SUBMARKETS



Area #	Submarket
1	Downtown
2	West San Diego
3	Mission Valley
4	University City
5	Torrey Pines
6	Kearny Mesa
7	Sorrento Valley
8	Carmel Valley
9	East San Diego
10	South San Diego

Area #	Submarket
11	Eastern San Diego County
12	Mira Mesa–Rancho Penasquitos
13	Scripps Ranch
14	Poway
15	Rancho Bernardo
16	Escondido–San Marcos
17	Oceanside–Fallbrook
18	Carlsbad
19	Del Mar–Encinitas



## DEFINITIONS & METHODOLOGY

- ▶ Office using employment is defined as all jobs within the Professional and Business Services, Financial Activities and Information sectors.
- ▶ Rents shown in the listing section are reported on a Full Service (FSG) basis. Yardi Matrix subscribers have access to both listed rents and FSG equivalent rents.
- ▶ Class A and A+/Trophy buildings are combined for reporting purposes.
- ▶ Yardi Matrix tracks properties with 50,000 square feet or more.

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