INVESTMENT FORECAST

Office

San Francisco Metro Area

2024

Retail-Residential Connection Fueling Market's Stabilization as Local Buyers Find Opportunities

Recovering household count, incomes bolster retail landscape. While certain property types in San Francisco continue to lag the nation in post-pandemic recovery, the metro's retail sector is gathering momentum. A key to this shift is population growth, which resumed in fall 2021, following a year of net out-migration. Many areas of the market are benefiting from this trend, including Downtown, where apartment vacancy in certain neighborhoods has returned to pre-2020 lows. San Francisco also led the country in median household income growth last year, nearing 10 percent. A rising number of households, paired with climbing incomes, bode well for the market's retail outlook. Vacancy in the city, excluding Downtown, continues to hold under 5 percent, with even tighter conditions in South San Mateo County. While high-profile retailer exits in Downtown San Francisco last year pushed vacancy above 10 percent, the greater resident count should encourage improving foot traffic. A rising number of international arrivals at SFO also supports tourism spending both in and outside the metro's core.

Recent challenges clear a path for buyers experienced in the market. Local investors, no strangers to past San Francisco downturns nor the recoveries that follow, were the most active segment of the trading landscape entering this year. A 5 percent decline in the average per-square-foot sale price in 2023, combined with a less competitive sales environment, may be opening repositioning opportunities before the next growth cycle. Trading activity continues to lean west of Van Ness Avenue and south of Golden Gate Park, where vacancy was under 4 percent last year. Restaurants and storefronts near or joined to residential buildings were favored, although some vacant assets also changed hands, revealing some appetite for value-add and redevelopment strategies.

2024 MARKET FORECAST

+0.7% ▲ **EMPLOYMENT:** Hiring continues to slow in San Francisco, with 8,000 new roles in 2024. Job creation will be most prevalent in the education and health services sectors.

160,000 sq. ft. ▲ **CONSTRUCTION:** While completions pick up from last year's negligible additions, a majority of 2024's pipeline stems from the relocating 125,000-square-foot San Francisco Flower Market.

+30 bps ▲ **VACANCY:** Minor completions help keep the metrowide vacancy rate from exceeding 6.8 percent this year, leading to the smallest annual vacancy increase since 2018.
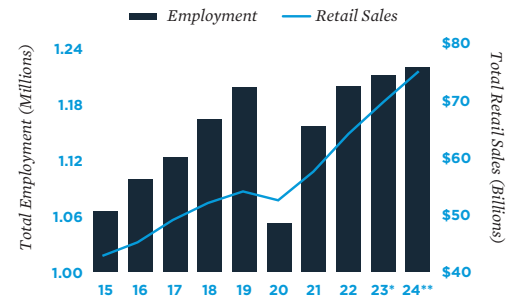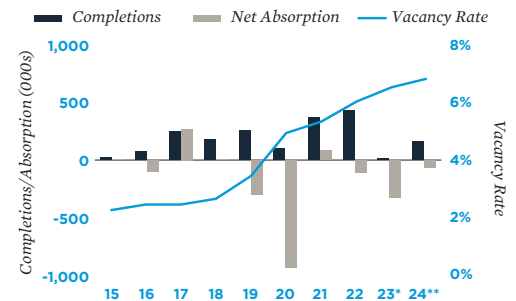
-0.1% ▼ **RENT:** Asking rents continue to improve in the metro's smaller multi-tenant landscape, while declines among downtown single-tenant spaces lead to an overall mean of $35.95 per square foot.

INVESTMENT: *Despite lackluster headlines and higher vacancy downtown, storefronts are changing hands in Chinatown-Van Ness and other areas, likely encouraged by strengthening apartment occupancy nearby.*
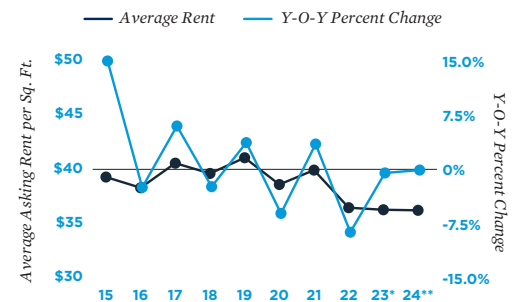
Economic Trends

Legend: Employment (bars), Retail Sales (line)

Left axis: Total Employment (Millions) — 1.00, 1.06, 1.12, 1.18, 1.24
Right axis: Total Retail Sales (Billions) — $40, $50, $60, $70, $80
X-axis: 15, 16, 17, 18, 19, 20, 21, 22, 23*, 24**

Supply and Demand

Legend: Completions (bars), Net Absorption (bars), Vacancy Rate (line)

Left axis: Completions/Absorption (000s) — -1,000, -500, 0, 500, 1,000
Right axis: Vacancy Rate — 0%, 2%, 4%, 6%, 8%
X-axis: 15, 16, 17, 18, 19, 20, 21, 22, 23*, 24**

Rent Trends

Legend: Average Rent (line), Y-O-Y Percent Change (line)

Left axis: Average Asking Rent per Sq. Ft. — $30, $35, $40, $45, $50
Right axis: Y-O-Y Percent Change — -15.0%, -7.5%, 0%, 7.5%, 15.0%
X-axis: 15, 16, 17, 18, 19, 20, 21, 22, 23*, 24**

* Estimate; ** Forecast
Sources: CoStar Group, Inc.; Real Capital Analytics; RealPage, Inc.

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