

# INVESTMENT FORECAST

OFFICE  
San Diego Metro Area

IPA  
INSTITUTIONAL  
PROPERTY  
ADVISORS

2020

## Office-User Expansions Trigger Rise in Absorption; New Construction Falls Short of Demand

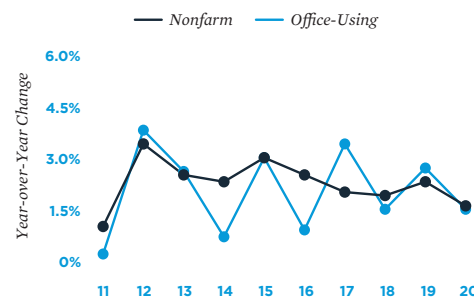
**Vacancy dips below pre-recession levels.** Home to a sizable life science presence and a collection of defense and tech-related companies, San Diego hosts a diverse tenant base that has supported solid demand for office space this cycle. The metro enters 2020 following a year of solid leasing velocity that reduced vacancy to a cycle-low level. Since peaking at 18.7 percent in 2009, vacancy rates have declined steadily, reinforcing the market's appeal to businesses. Despite strong demand, speculative development is restrained as most of more than 1 million square feet slated for delivery this year is pre-leased. A U.S. Navy headquarters in downtown San Diego and Cubic's facility in Kearny Mesa highlight the list of upcoming completions. Additionally, Apple has inked leases for three properties near La Jolla, one of which will be completed this year. A lack of additions of new space coupled with traditional office-user growth will further reduce the volume of available floor plans. As vacancy falls to the low-12 percent band, asking rents climb at a healthy rate, pushing the metro's average roughly \$3 per square foot above the prior cyclical high.

**Buyers focus on extended runway for office assets.** The metro's varied tenant mix coupled with compressing vacancy and improving rent growth continue to attract a mix of capital, equating to widespread deal flow. Sorrento Mesa and Kearny Mesa are top spots for buyers seeking mid- to top-tier properties in life science and defense contractor hubs. In both locales, opportunities to deploy \$10 million to \$20 million-plus remain frequent, as do minimum returns in the 4 percent range. North along Interstate 5, Carlsbad is another target for Class B deals; however, most assets are smaller, warranting investments of \$1 million to \$5 million. Active local buyers pursue Class C buildings in neighborhoods adjacent to downtown San Diego and Balboa Park, where cap rates typically fall in the 5 to 6 percent range and pricing above \$400 per square is common.

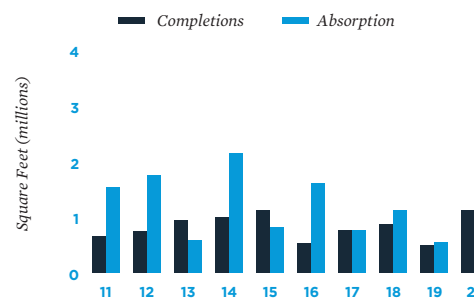
## 2020 Market Forecast

- Employment** up 1.6%  
 San Diego employers add 24,500 positions in 2020 after creating an average of 30,300 jobs during the prior three years.
- Construction** 1.1 million sq. ft.  
 Delivery volume in 2020 surpasses the 1 million-square-foot mark for the first time in five years, with supply additions increasing the metro's office inventory by 1.1 percent.
- Vacancy** down 50 bps  
 Metro vacancy compresses for a fifth straight year, falling to 12.1 percent on net absorption of nearly 1.5 million square feet. In 2019, a decline of 10 basis points was recorded.
- Rent** up 3.2%  
 The average asking rent climbs to \$34.74 per square foot, besting the prior three-year average annual increase of 2.3 percent.
- Investment**  
 Private investors seeking the highest yields available target El Cajon and La Mesa, where smaller Class C assets routinely provide 8 percent-plus first-year returns. In both East County locales, pricing well below the metro's average remains.

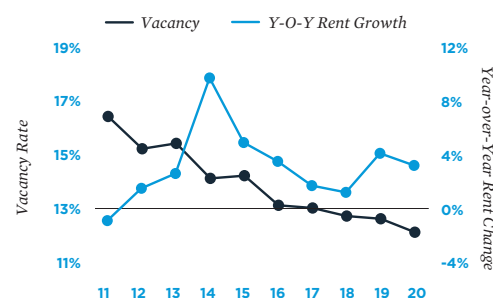
### Employment Trends



### Office Supply and Demand



### Vacancy and Rent Trends



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

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Metro-level employment, vacancy and asking rents are year-end figures and are based on the most up-to-date information available as of December 2020. Asking rent is based on the full-service marketed rental rate. Average prices and cap rates are a function of the age, class and geographic area of the properties trading and therefore may not be representative of the market as a whole. Sales data includes transactions valued at \$1,000,000 and greater unless otherwise noted. Forecasts for employment and office data are made during the fourth quarter and represent estimates of future performance. No representation, warranty or guaranty, express or implied may be made as to the accuracy or reliability of the information contained herein. This is not intended to be a forecast of future events and this is not a guaranty regarding a future event. This is not intended to provide specific investment advice and should not be considered as investment advice.