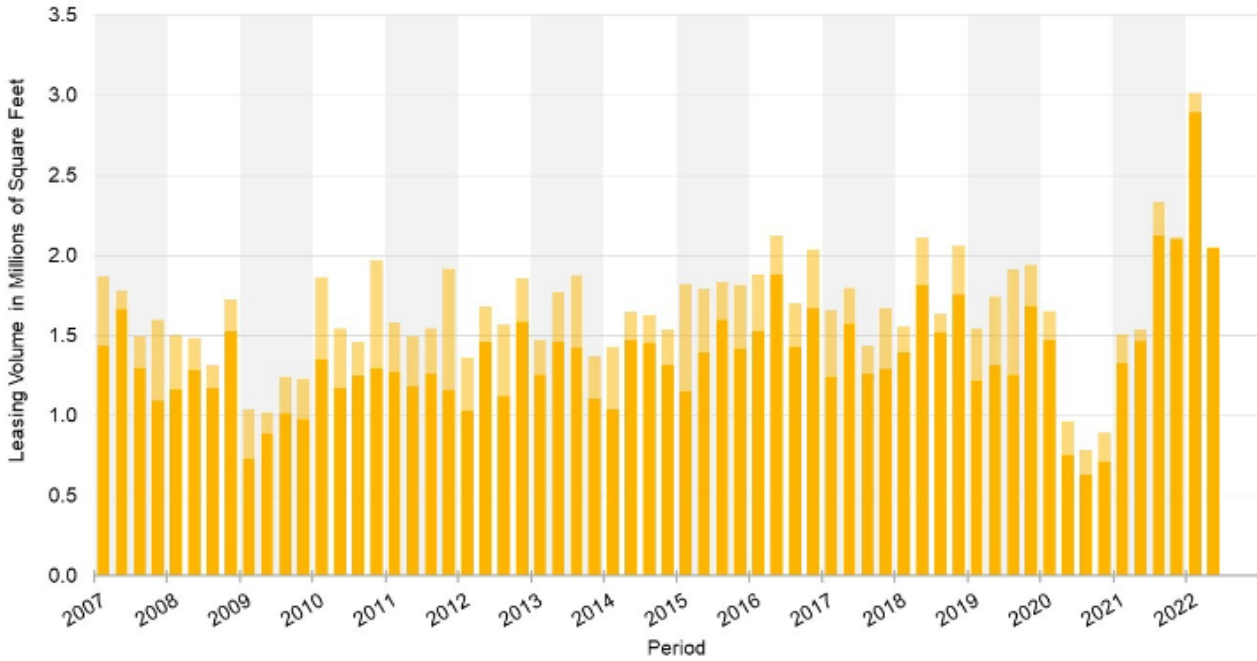


# Office Leasing Belies Recovery in San Diego

## Rent Growth Is Outperforming Other California Markets, but Challenges Remain

### New Office Leasing Activity Remains Strong in 2022 in San Diego



Source: CoStar, July 2022

Entered Before Quarter End

Entered After Quarter End



By Joshua Ohl

While there is still uncertainty over the pandemic's long-term impact on the office environment and the differing approaches to office use among tenants, new leasing activity appears to have normalized in San Diego.

The second quarter saw more than 2 million square feet of office space leased in San Diego. That has padded the record to now four straight quarters exceeding that level. In fact, San Diego had not seen two straight quarters exceed 2 million square feet of leasing over the past 15 years before this current run.

However, leasing activity has been relatively top heavy and dominated by a few sectors, and life sciences firms took a back seat to high-tech firms in the second quarter.

Leidos, an information technology firm, signed the quarter's largest deal for a 170,000-square-foot, build-to-suit property at Alexandria Point in the University Town Center area for a modest expansion

in the neighborhood. That is the same campus where Bristol Myers Squibb preleased more than 400,000 square feet at the beginning of the year.

Google increased its footprint after leasing 105,000 square feet in Sorrento Mesa at the Verge campus, which will double its current occupancy at the same campus after adding two more floors there.

Apple also further solidified its footprint in San Diego after signing two new leases during the second quarter and extending a third deal. The tech firm leased 53,000 square feet at Rancho Vista Corporate Center and 95,000 square feet at The Point. Apple also extended its 130,000-square-foot lease at Northridge Summit in Scripps Ranch for a space that it assumed after acquiring Intel's mobile division in 2019.

That leasing activity belies the current state of San Diego's office market. During the past year, the vacancy rate has fallen from 11.8% to 10.6%, placing it squarely in line with the long-term market average, although that is still 100 basis points higher than it was at the start of 2020.

The amount of available space in the San Diego office market is trending at a 10-year high of 18.7 million square feet, or about 15.1% of total inventory. The median months on market for available office space has increased in 2022 and has reached its highest level in more than five years, at roughly 13 months.

After falling for most of 2021, the amount of available sublet space increased for the third straight quarter, and there was roughly 2.1 million square feet available at the mid-point of 2022. But even with a historically high level of sublet space available, sublet space only accounted for 9% of total new office leasing volume in the past four quarters, an amount that has been exceeded several times in the recent past.

San Diego rent growth has recovered, and at 3.4% year over year at the midway point of 2022, San Diego was in the top 10 in the country among markets with more than 100 million square feet of total inventory.

The future of how tenants will utilize office space is still uncertain given that hybrid and remote work is likely here to stay. Uncompetitive space will hover over the market, though that could provide the opportunity for owners to redevelop some of those properties.

In Orange County, San Diego's neighbor to the north, more than 1% of office inventory has been sold since 2021 with the intention of redeveloping it into housing or modern industrial space. That trend could become more pronounced here, which would help stabilize the market in an uncertain future.

If high-tech and life sciences firms pull back from recent activity, that could spell additional trouble for the San Diego region.