

MARKET OVERVIEW. Most of the first quarter was in the books by the time that shelter-in-place orders took effect in March. The first quarter will primarily act as a benchmark from which to compare the pandemic effects on the market over the subsequent quarter. The San Diego Flex /R&D market averaged less than 40,000 square feet of new construction per year from 2012 to 2015, while over the past four years the market has seen an average of more than 550,000 square feet of new construction per year. This has placed some pressure on the market's overall occupancy rate, and all the new product has pushed the average asking rental rate up significantly. While supply is up, the demand side of the market is down. There was negative net absorption in the first quarter, and transaction volume is down.

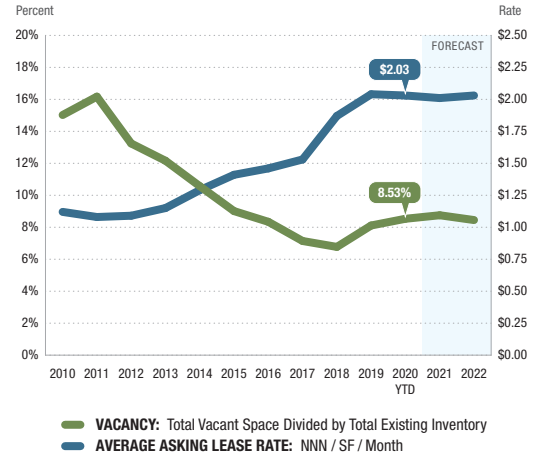
VACANCY. Direct/sublease space (unoccupied) finished the first quarter at 8.53%, a substantial increase of 66 basis points from the first quarter of 2019's vacancy rate of 7.87%. The current vacancy rate is at about half of the 2010 recession low of 16.12%, however. The Flex/R&D sector is the smallest of the major commercial real estate sectors in San Diego, and as such the metrics often change very rapidly.

LEASE RATES. The average asking lease rate per square foot per month in San Diego County was \$2.03 at the end of the first quarter, a one cent pullback from the average asking rate of \$2.04 at the end of 2019.

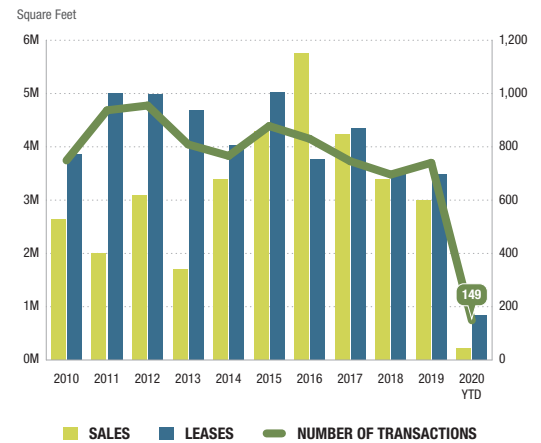
TRANSACTION ACTIVITY. The combined amount of square feet leased or sold in the first quarter totaled 1.1 MSF, a decrease from the 1.4 MSF transacted in the fourth quarter of 2019. Sales and leasing volume have recorded three consecutive years of decreases, and first quarter volume puts the market on a pace for four straight years of decreases. This statistic can have some lag time in being reported, so look for this quarter's figures to end up somewhat higher in the next report.

EMPLOYMENT. The unemployment rate in San Diego County was 3.2% in February 2020, down from a revised 3.3% in January 2020, and below the year-ago estimate of 3.4%. This compares with an unadjusted unemployment rate of 4.3% for California and 3.8% for the nation during the same period. According to the State of California Employment Development Department, San Diego County gained 26,400 payroll jobs between February 2019 and February 2020. In mid-March the unemployment claims for the United States as a whole came in at 3.28 million claims for a single week which was a record claim for a single week, nearly five times greater than the previous record which was set in 1982. Subsequent weeks had even more unemployment claims. With the normal delay in reporting from the California EDD, employment figures from March were unavailable at the time of publishing this report. Suffice it to say stay at home orders related to the COVID-19 pandemic will lead to an increase in local unemployment over the coming months.

VACANCY vs. AVERAGE ASKING LEASE RATE



TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



Market Statistics

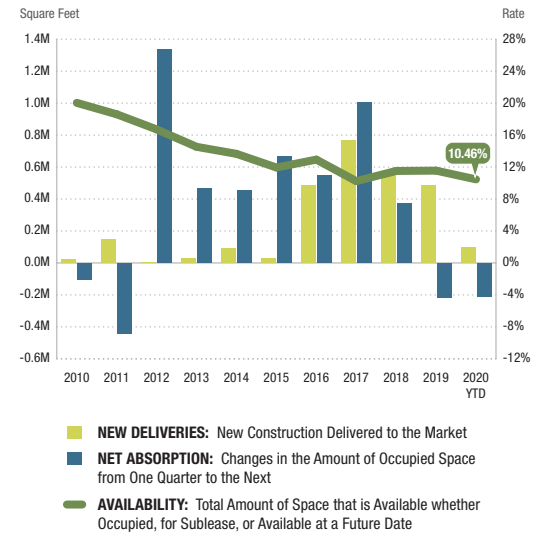
	Change Over Last Quarter	1Q 2020	4Q 2019	1Q 2019	% Change Over Last Year
Vacancy Rate	▲ UP	8.53%	8.11%	7.87%	8.36%
Availability Rate	▼ DOWN	10.46%	11.55%	12.09%	(13.47%)
Average Asking Lease Rate	▼ DOWN	\$2.03	\$2.04	\$1.89	7.41%
Sale & Lease Transactions	▼ DOWN	1,056,419	1,832,393	1,308,266	(19.25%)
Gross Absorption	▼ DOWN	583,689	869,883	370,861	57.39%
Net Absorption	▼ NEGATIVE	(209,821)	295,065	(393,004)	N/A

CONSTRUCTION. In 2019 there was a total of 485,707 square feet of new construction completed, and there were 230,418 square feet under construction at the end of the first quarter of 2020. The biotech subset within the Flex/R&D market continues to be the primary driver of new construction.

AVAILABILITY. Direct/sublease space being marketed was 10.46%, which is a decrease of more than a percentage point from the fourth quarter of 2019's rate of 11.55%. The gap between vacancy and availability has narrowed over the past year as space that was available but not vacant has since been vacated.

ABSORPTION. The San Diego Flex/R&D market recorded 209,821 square feet of negative net absorption in the first quarter of 2020. This level of negative absorption nearly eclipses the 218,091 square feet of negative net absorption in 2019, which was the first calendar year with negative net absorption since 2011.

NEW DELIVERIES & NET ABSORPTION vs. AVAILABILITY RATE



Forecast

Last quarter we were most concerned about warnings of a global slowdown, US GDP growth and trade relations between the US and China. But the world has changed, and we are finally able to identify the Black Swan that economists have been hedging their forecasts with for years. The COVID-19 virus, first identified in China, has circled the planet in a matter of weeks, causing leaders around the world to take aggressive steps to stop it. Entire countries are on lockdown and our own federal and state governments have taken steps similar to our neighbors in Asia and Europe.

It's too early to tell what the exact long-term impact the reaction to the virus will have on the San Diego Flex/R&D market, but we do predict a near-term decrease in occupancy rates and transaction volume. We should see the statistical evidence of that in the second quarter numbers. We expect the decrease in occupancy and leasing volume to place downward pressure on Flex/R&D rental rates in the next quarter, and all eyes will be fixed upon the depth of the downturn and the speed of the recovery to formulate forward guidance.

Significant Transactions

Sales

Property Address	Submarket	Square Feet	Sale Price	Buyer	Seller
2750 Auto Park Way	Escondido	42,150	\$8,250,000	Providence Capital Group	MCA Realty
7630 Carroll Rd.	Miramar	42,261	\$6,800,000	University Vista, LLC	Miramar Metroplex, LP
6190 Yarrow Dr.	Carlsbad	17,668	\$2,814,000	Ryoma Estate, LLC	Coretests, Inc.

Leases

Property Address	Submarket	Square Feet	Transaction Date	Tenant	Owner
9940 & 9940 Barnes Canyon Rd.	Sorrento Mesa	139,807	Feb-2020	Qualcomm	La Jolla Management Company
9125 Rehco Rd.	Miramar	60,786	Feb-2020	Undisclosed	LBA Realty
6740 Cobra Way	Sorrento Mesa	52,959	Jan-2020	Sekisui Diagnostics	Auerbach Commercial Realty Corp.
10455 Pacific Center Ct.	Sorrento Mesa	36,936	Dec-2020	Resonetics, LLC	Miller Family Trust
4242 Campus Point Ct.	UTC	21,180	Dec-2020	Heron Therapeutics	Alexandria RE Equities
9477 Waples St.	Sorrento Mesa	40,016	Feb-2020	Undisclosed	Clarion Partners

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate 1Q2020	Square Feet Available	Availability Rate 1Q2020	Average Asking Lease Rate	Net Absorption 1Q2020	Net Absorption 2020	Gross Absorption 1Q2020	Gross Absorption 2020
Central													
Central City	13	224,781	0	0	28,946	12.88%	28,639	12.74%	\$1.78	0	0	0	0
East City	2	26,892	0	0	0	0.00%	0	0.00%	-	0	0	0	0
Southeast City	21	223,879	0	0	0	0.00%	0	0.00%	-	0	0	0	0
Kearny Mesa	203	5,479,562	0	10,200	422,374	7.71%	0	0.00%	\$1.75	(11,072)	(11,072)	9,344	9,344
Mission Gorge	27	279,740	0	0	3,770	1.35%	3,770	1.35%	\$1.65	8,074	8,074	11,844	11,844
Rose Canyon/Morena	38	597,194	0	0	30,898	5.17%	36,615	6.13%	\$1.40	13,605	13,605	14,733	14,733
Sports Arena/Airport	32	409,430	0	0	65,779	16.07%	70,079	17.12%	\$1.89	0	0	0	0
Miramar	220	4,895,993	0	130,510	311,687	6.37%	487,482	9.96%	\$1.81	9,329	9,329	86,020	86,020
Sorrento Mesa	162	6,773,167	28,000	618,000	1,067,502	15.76%	1,050,137	15.50%	\$2.37	(131,578)	(131,578)	112,005	112,005
Sorrento Valley	102	2,592,745	0	220,180	276,307	10.66%	422,002	16.28%	\$3.00	(23,294)	(23,294)	41,837	41,837
Torrey Pines/UTC	72	6,340,213	202,418	1,040,944	527,937	8.33%	959,498	15.13%	\$4.60	(53,448)	(53,448)	57,149	57,149
Central County Total	892	27,843,596	230,418	2,019,834	2,735,200	9.82%	3,058,222	10.98%	\$2.46	-188,384	-188,384	332,932	332,932
East County													
El Cajon	78	873,199	0	40,000	7,156	0.82%	19,790	2.27%	\$1.46	4,785	4,785	8,601	8,601
La Mesa/Spring Valley	41	295,786	0	0	9,236	3.12%	20,938	7.08%	\$1.40	5,938	5,938	13,174	13,174
Santee/Lakeside	54	554,061	0	0	8,297	1.50%	6,650	1.20%	\$1.21	(3,800)	(3,800)	2,000	2,000
Outlying SD County South	22	96,424	0	0	0	0.00%	3,719	3.86%	-	0	0	0	0
East County Total	195	1,819,470	0	40,000	24,689	1.36%	51,097	2.81%	\$1.36	6,923	6,923	23,775	23,775
North County													
Escondido	80	754,617	0	0	32,118	4.26%	33,003	4.37%	\$1.22	(6,442)	(6,442)	1,165	1,165
Oceanside	33	983,515	0	0	21,560	2.19%	45,974	4.67%	\$0.96	3,888	3,888	5,538	5,538
San Marcos	60	1,089,953	0	0	71,479	6.56%	92,317	8.47%	\$1.20	(2,135)	(2,135)	18,810	18,810
Vista	62	1,390,453	0	0	95,284	6.85%	333,359	23.97%	\$1.08	(21,966)	(21,966)	0	0
Carlsbad	259	6,662,840	0	0	820,674	12.32%	915,522	13.74%	\$1.27	(10,636)	(10,636)	150,710	150,710
North Beach Cities	19	164,051	0	0	2,660	1.62%	6,980	4.25%	\$2.75	2,951	2,951	5,511	5,511
Outlying SD County North	19	139,572	0	0	1,550	1.11%	1,550	1.11%	\$0.79	0	0	0	0
North County Total	532	11,185,001	0	0	1,045,325	9.35%	1,428,705	12.77%	\$1.24	(34,340)	(34,340)	181,734	181,734
I-15 Corridor													
Poway	61	1,851,590	0	0	21,575	1.17%	57,285	3.09%	\$1.28	(8,541)	(8,541)	3,599	3,599
Rancho Bernardo	95	4,646,678	0	0	256,717	5.52%	403,583	8.69%	\$1.89	7,184	7,184	18,892	18,892
Scripps Ranch	28	751,466	0	235,276	14,214	1.89%	11,702	1.56%	\$1.18	0	0	0	0
I-15 Corridor Total	184	7,249,734	0	235,276	292,506	4.03%	472,570	6.52%	\$1.81	(1,357)	(1,357)	22,491	22,491
South County													
Chula Vista	79	1,501,626	0	66,860	154,578	10.29%	209,516	13.95%	\$1.47	(2,756)	(2,756)	9,757	9,757
National City	23	333,897	0	0	1,046	0.31%	1,046	0.31%	\$1.10	0	0	0	0
Otay Mesa	7	156,455	0	0	27,153	17.36%	27,246	17.41%	\$0.73	10,093	10,093	13,000	13,000
San Ysidro/Imperial Beach	5	86,361	0	0	0	0.00%	0	0.00%	-	0	0	0	0
South County Total	114	2,078,339	0	66,860	182,777	8.79%	237,808	11.44%	\$1.15	7,337	7,337	22,757	22,757
San Diego County Total	1,917	50,176,140	230,418	2,361,970	4,280,497	8.53%	5,248,402	10.46%	\$2.03	(209,821)	(209,821)	583,689	583,689

Lease rates are on a triple-net basis.



How Will the COVID-19 Impact COMMERCIAL REAL ESTATE?

by **Alex Jize**

SENIOR ASSOCIATE, SAN DIEGO

858.458.3361 · ajize@voitco.com · Lic. #01947389

As an active commercial real estate agent, I spend a lot of my time each day on the phone with commercial owners. Over just the last few days, it has become more evident what the reality of this current pandemic mean to the commercial real estate industry.

I have spoken with clothing distribution companies, food processing businesses, machine shop owners and others who are all being directly affected by what is going on globally, all in different ways. Many business owners are yet to feel an impact, but are closely monitoring the situation. Some are making moves to conserve cash in response to higher levels of near-term economic uncertainty.

On a positive note, I am currently managing escrows for clients who are taking advantage of the lowest interest rates in history. Fully amortized, 25-year SBA mortgages are currently available at the stunning low rate of 2.93%, a nice surprise for those who expected to pay a much higher rate when their escrows opened just weeks ago. Also, investors who are buying assets with long-term leases in place, with credit tenants, are in a great position. Unlike what we are seeing with the volatility of the stock and bond markets, commercial real estate is remaining strong and is offering much higher returns than any other asset class. Currently, the US 10-year Treasury bond is at 0.75%. You can buy a quality triple-net property with zero or minimal ownership responsibilities, with a long-term corporate-backed lease, at a cap rate ranging from 4.00% to 5.50%, depending on location and tenant's credit strength.

As a local owner, it makes the most sense to stay the course and let this unexpected anomaly run its natural course. Low-rate mortgage money from the SBA will be an offsetting factor and should help demand keep pace with current supply. As far as the leasing market stands, I believe there is going to be a bit of a slowdown over the next two or three months due to the coronavirus and its global repercussions.

Please Contact Us for Further Information

Josh Brant
Regional Director of Research
jbrant@voitco.com

Anaheim, CA
714.978.7880

Carlsbad, CA
760.517.4000

Inland Empire, CA
909.545.8000

Irvine, CA
949.851.5100

Los Angeles, CA
424.329.7500

San Diego, CA
858.453.0505

This survey consists of properties representing both single tenant and multi-tenant buildings. The lease rates are based on a triple-net basis. The information contained in this report is gathered from sources that are deemed reliable, but no guarantees are made as to its accuracy. This information is for Voit Real Estate Services' use only and cannot legally be reproduced without prior written consent from the management of Voit Real Estate Services. ©2020 Voit Real Estate Services, Inc. DRE License #01991785.

Represented in 150 Markets
Nationally & Internationally.



Product Type

MFG./DIST.: Flex/Research and Development (R&D) buildings can be one story, one story with a mezzanine, and two story built-out structures with a high ratio of window wall to floor area with lower ceilings. They generally have over 50% built-out office space or laboratory use, with the remaining space being utilized as light manufacturing or warehousing. In addition, the parking ratio must be at least 3 spaces or greater per 1,000 square feet.

Submarkets

CENTRAL COUNTY

Central City, East City, Southeast City, Kearny Mesa, Mission Gorge, Rose Canyon/Morena, Sports Arena/Airport, Miramar, Sorrento Mesa, Sorrento Valley, Torrey Pines/UTC

EAST COUNTY

El Cajon, La Mesa/Spring Valley, Santee/Lakeside, Outlying SD County South

NORTH COUNTY

Escondido, Oceanside, San Marcos, Vista, Carlsbad, North Beach Cities, Outlying SD County North

I-15 CORRIDOR

Poway, Rancho Bernardo, Scripps Ranch

SOUTH BAY

Chula Vista, National City, Otay Mesa, San Ysidro/Imperial Beach