

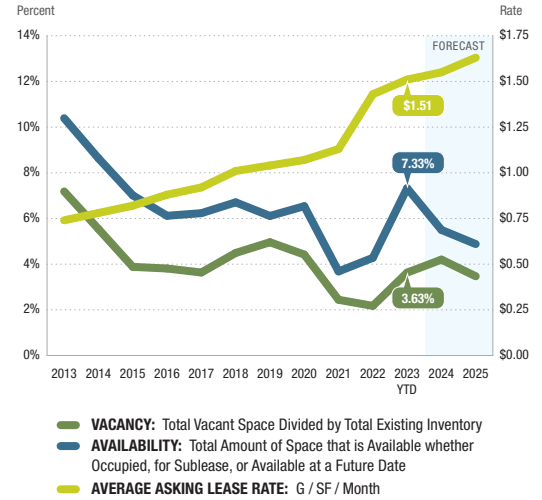
OVERVIEW. A reduced level of leasing and sales volume in the San Diego industrial market continued in the third quarter of the year. Construction activity is still strong, though largely concentrated in the South County. The market continues to push new all-time highs in rental rates quarter after quarter. There was negative net absorption in the first three quarters of the year which moved the vacancy rate up.

VACANCY & AVAILABILITY. Direct/sublease space (unoccupied) finished Q3 at 3.6%, an increase of half a percentage point from the previous quarter's vacancy rate of 3.1%. In 2010, during the "Great Recession," the overall vacancy rate for the county peaked at 9.7%. At the end of Q3 2023, every submarket other than South County had a vacancy rate of 4% or less. Available space being marketed (regardless of occupancy status) was 7.3% of the county's inventory at the end of Q3. South County had a 13.4% availability rate at the end of Q3, more than double any other submarket in the county, due to South County projects under construction which have available space not yet ready for occupancy.

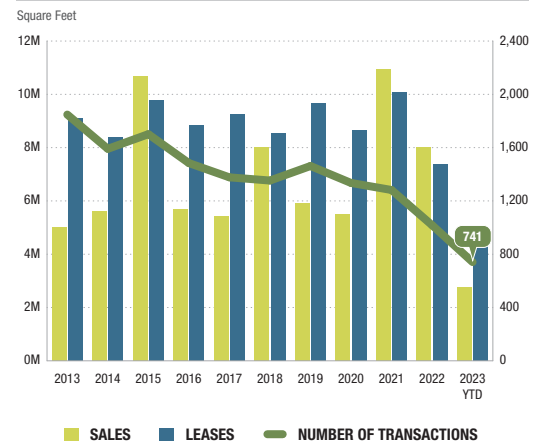
LEASE RATES. The average asking lease rate checked in at \$1.51 per square foot per month, which is an increase of one cent per square foot over the previous quarter. Compared with Q3 2022, we see a substantial 14.4% annual increase. Over the past five years, asking rental rates have increased by an average of 9.6% per year. With the broader economy slowing, sentiment in the market is that the pace of rental rate growth will decelerate into 2024. By and large, negotiating leverage in the industrial market remains in the hands of the landlords due to the limited availability in most parts of the county, and rental rates remain elevated. In many cases, tenants with expiring leases do not have a single alternative in their submarket, placing the negotiating leverage in the hands of landlords. In the most competitive areas, landlords are often able to backfill new availabilities before the existing tenant vacates. Over the past two years, fixed annual rental increases have moved up. It is now common to see landlords insist on increases of 4% per year, rather than 3%, which had been the standard for many years.

TRANSACTION ACTIVITY. There were 189 lease transactions recorded in Q3. Since the beginning of 2021 there has been an average of 215 leases recorded per quarter. The preceding five years had a quarterly average of 294 lease transactions. The market is so tight there are many tenants deciding to stay in their current location rather than move to a new facility because of the lack of available options. Many of these renewals do not get captured in the quarterly tally. The market has now seen six consecutive quarters without Amazon among the largest leases recorded. Amazon is slowing down following its rapid expansion which had been a major component of the leasing volume in recent years. From 2020-2022, Amazon executed a dozen different leases in San Diego County totaling more than 2.5 MSF. This does not include the 3.4 MSF build-to-suit in Otay Mesa. Amazon's pullback has taken some of the wind out of the sails of the leasing market. Sales activity ticked back up in Q3 with \$229 million in total, compared to the \$108 million in sales recorded in Q2. The industrial market is still on pace for less than \$1 billion in sales in 2023, which would be the first such year since 2017.

VACANCY, AVAILABILITY & AVERAGE ASKING LEASE RATES



TRANSACTION VOLUME & NUMBER OF TRANSACTIONS



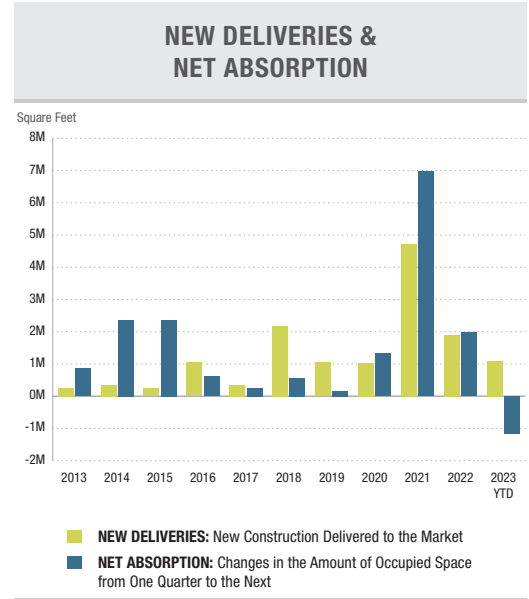
Market Statistics

	Change Over Last Quarter	Q3 2023	Q2 2023	Q3 2022	% Change Over Last Year
Vacancy Rate	▲ UP	3.63%	3.08%	2.66%	36.40%
Availability Rate	▲ UP	7.33%	6.65%	4.02%	82.20%
Average Asking Lease Rate	▲ UP	\$1.51	\$1.50	\$1.32	14.39%
Sale & Lease Transactions	▬ FLAT	2,022,555	2,088,847	2,943,693	(31.29%)
Gross Absorption	▬ FLAT	1,248,720	1,282,643	1,652,197	(24.42%)
Net Absorption	▼ NEGATIVE	(408,621)	(307,976)	(131,538)	N/A

ABSORPTION. There were 408,621 SF of negative net absorption in Q3, marking the third consecutive quarter of negative net absorption. The low leasing volume in 2022 led to the decrease in the tenant footprint to start 2023, and with the slow start to industrial leasing in the first three quarters of 2023, the market may see more negative net absorption in coming quarters. Outside of the South County, all of the major submarkets in the county are at or near all-time low levels of vacancy. Without significant construction in these areas, negative net absorption will be a welcome sight for tenants in the market looking for available space.

CONSTRUCTION. 1.9 MSF of new industrial projects were delivered in 2022, which was the sixth year out of the past seven with more than 1.0 MSF of new construction completed. This is in stark contrast to the 360,000 SF per year of new construction which was the annual average from 2008 through 2015. With very little land in the central county area available for development, most new construction in the county is happening around the edges. Over the past six years there have been more than 1.0 MSF of new industrial development in each of South County, North County, and the I-15 Corridor, while Central County and East County have each seen less than a half a million total square feet of new development during that span. More recently, construction has been concentrated in Otay Mesa, which accounts for more than 80% of the construction completions since the start of 2020, and 71% of the industrial real estate currently under construction.

EMPLOYMENT. The unemployment rate in San Diego County was 4.3% in August 2023, up from a revised 3.9% in April 2023, and above the year-ago estimate of 3.5%. This compares with an unadjusted unemployment rate of 5.1% for California and 3.9% for the nation during the same period. Over the 12-month period between August 2022 and August 2023, San Diego County employment increased by 33,800 jobs, an increase of 2.2%. With the normal delay in reporting from the California EDD, employment figures from September were unavailable at the time of publishing this report. For the nation as a whole, 336,000 jobs were added in September, the second highest monthly total of the past year.



Forecast

Going into the last quarter of 2023, we find ourselves in an environment of high interest rates and lingering concern about an economic slowdown. We are seeing signs of a cooldown in investment sales, and the uncertainty surrounding the economy will exacerbate that trend. The ongoing construction boom, light leasing activity, and the widening gap between availability and vacancy all point towards an increase in vacancy in the coming quarters.

Significant Transactions

Sales

Property Address	Submarket	Square Feet	Sale Price	Buyer	Seller
9040 & 9050 Airway Rd.	Otay Mesa	199,997	\$57,000,000	Ares Management Corp	Lincoln Property Company
7880 & 7920 Airway Rd.	Otay Mesa	132,667	\$34,580,000	T&S Properties	TA Tealty
10054 Old Grove Rd.	Scripps Ranch	85,824	\$33,999,000	Southwest Reg. Council of Carpenters	Old Grove, LLC
131 W. 33rd St.	National City	78,699	\$20,330,000	131 W 33rd St - NC, LLC	Unilev Capital Corp
6695 Rasha St.	Miramar	37,747	\$16,000,000	Wholesalers Property Co, LLC	TCP Investments, LLC

Leases

Property Address	Submarket	Square Feet	Transaction Date	Tenant	Owner
1756 Weld Blvd.	El Cajon	160,000	Aug-2023	GKN Aerospace	Chesnut Properties
3939 Market St.	Southeast San Diego	51,262	Sep-2023	Cruise	(Sublease)
5995 Pacific Center Blvd.	Sorrento Mesa	47,498	Aug-2023	Abbot (Renewal)	Sukut Real Properties
4039 Calle Platino	Oceanside	30,082	Sep-2023	Undisclosed	Rexford Industrial
2809 Ocean Ranch Blvd.	Oceanside	23,490	Sep-2023	Floral Trade Group	First Industrial Realty

	INVENTORY				VACANCY & LEASE RATES					ABSORPTION			
	Number of Bldgs.	Net Rentable Square Feet	Square Feet U / C	Square Feet Planned	Square Feet Vacant	Vacancy Rate Q3 2023	Square Feet Available	Availability Rate Q3 2023	Average Asking Lease Rate	Net Absorption Q3 2023	Net Absorption 2023	Gross Absorption Q3 2023	Gross Absorption 2023
Central County													
Central City	83	1,388,882	0	0	17,000	1.22%	136,450	9.82%	\$1.23	3,353	(13,647)	6,706	6,706
East City	59	605,732	0	0	7,575	1.25%	7,575	1.25%	\$1.50	1,525	5,348	1,525	14,448
Southeast City	366	4,253,332	0	0	60,732	1.43%	103,357	2.43%	\$1.38	10,135	30,450	10,919	76,347
Kearny Mesa	410	9,578,188	0	322,251	233,981	2.44%	442,452	4.62%	\$1.93	43,157	(113,783)	114,429	248,290
Mission Gorge	106	1,758,295	0	0	34,959	1.99%	76,810	4.37%	\$1.84	(14,136)	(25,486)	6,384	21,421
Rose Canyon / Morena	128	1,993,568	0	0	140,450	7.05%	156,750	7.86%	\$1.48	(5,230)	(48,409)	12,000	134,757
Sports Arena / Airport	139	1,578,188	32,661	0	40,218	2.55%	45,718	2.84%	\$1.63	33,231	18,981	39,089	53,539
Miramar	579	13,390,589	0	0	458,281	3.42%	1,106,306	8.26%	\$1.74	24,568	(345,912)	156,437	371,977
Sorrento Mesa	69	3,244,895	0	0	68,288	2.10%	140,540	4.33%	\$1.82	28,651	27,326	43,301	158,955
Sorrento Valley/UTC	41	993,145	0	0	0	0.00%	800	0.08%	-	0	0	0	800
Central County Total	1,980	38,784,814	32,661	322,251	1,061,484	2.74%	2,216,758	5.71%	\$1.69	125,254	(465,132)	390,790	1,087,240
East County													
El Cajon	449	9,148,138	381,240	0	32,259	0.35%	379,556	3.98%	\$1.60	21,619	74,398	38,981	131,933
La Mesa / Spring Valley	310	2,678,534	0	3,000	19,551	0.73%	19,403	0.72%	\$1.27	14,575	11,111	33,628	73,560
Santee / Lakeside	289	3,982,801	0	0	39,656	1.00%	78,733	1.98%	\$1.50	8,090	86,967	30,073	157,997
Rural East County	85	987,257	0	0	55,400	5.61%	48,400	4.90%	\$0.50	0	(42,926)	0	4,074
East County Total	1,133	16,796,730	381,240	3,000	146,866	0.87%	526,092	3.06%	\$1.39	44,284	129,550	102,682	367,564
North County													
Escondido	635	7,606,049	0	67,300	156,718	2.06%	229,338	3.02%	\$1.41	10,719	(30,566)	50,921	135,925
Oceanside	398	9,375,258	0	520,446	224,011	2.39%	556,623	5.94%	\$1.39	46,061	(70,374)	107,930	243,162
San Marcos	474	8,119,900	0	223,175	580,140	7.14%	631,540	7.78%	\$1.31	(103,328)	(252,813)	51,129	209,869
Vista	526	13,076,417	0	0	444,764	3.40%	720,683	5.51%	\$1.40	(1,540)	(108,492)	100,616	398,006
Carlsbad	223	8,433,987	222,959	0	489,982	5.81%	691,762	7.99%	\$1.58	(215,043)	(205,139)	16,314	89,078
North Beach Cities	40	236,337	0	0	0	0.00%	0	0.00%	-	4,976	4,976	4,976	4,976
Rural North County	117	1,048,910	0	0	22,000	2.10%	48,282	4.60%	\$0.92	2,800	25,000	2,800	36,150
North County Total	2,413	47,896,858	222,959	810,921	1,917,615	4.00%	2,878,228	5.98%	\$1.38	(255,355)	(637,408)	334,686	1,117,166
I-15 Corridor													
Poway	187	7,634,736	0	0	196,320	2.57%	355,316	4.65%	\$1.65	(117,015)	(160,252)	8,671	63,321
Rancho Bernardo	39	2,986,860	0	0	91,974	3.08%	78,445	2.63%	\$1.75	0	(40,746)	0	37,699
Scripps Ranch	26	696,993	0	0	6,000	0.86%	10,875	1.56%	\$1.82	(6,000)	31,589	0	42,819
I-15 Corridor Total	252	11,318,589	0	0	294,294	2.60%	444,636	3.93%	\$1.70	(123,015)	(169,409)	8,671	143,839
South County													
Chula Vista	326	8,880,397	205,266	288,814	640,473	7.21%	1,167,909	12.85%	\$1.35	(186,485)	(174,907)	148,012	330,309
National City	251	3,640,155	0	80,970	43,288	1.19%	86,232	2.37%	\$1.68	(1,684)	11,890	19,176	71,299
Otay Mesa	368	23,186,898	2,023,666	3,503,410	1,384,326	5.97%	3,921,163	15.55%	\$1.35	(6,457)	166,234	242,617	918,292
South San Diego	63	1,331,136	0	24,121	23,212	1.74%	95,294	7.16%	\$1.33	(5,163)	(20,547)	2,086	4,751
South County Total	1,008	37,038,586	2,228,932	3,897,315	2,091,299	5.65%	5,270,598	13.42%	\$1.39	(199,789)	(17,330)	411,891	1,324,651
San Diego County Total	6,786	151,835,577	2,865,792	5,033,487	5,511,558	3.63%	11,336,312	7.33%	\$1.51	(408,621)	(1,159,729)	1,248,720	4,040,460
0-9,999	3,061	15,599,368	0	3,000	246,818	1.58%	466,355	2.99%	\$1.66	(3,534)	(578)	114,997	348,938
10,000-19,999	1,760	24,926,867	14,947	16,000	409,019	1.64%	738,479	2.96%	\$1.56	(11,674)	76,556	201,137	722,574
20,000-34,999	963	24,711,549	87,788	51,841	592,986	2.40%	1,285,802	5.18%	\$1.54	75,872	(35,339)	323,043	736,857
35,000-49,999	372	15,371,079	164,435	137,438	472,628	3.07%	1,167,081	7.51%	\$1.36	8,879	(227,298)	149,037	388,174
50,000-99,999	391	26,986,716	291,696	429,596	898,769	3.33%	2,251,590	8.25%	\$1.46	127,101	199,157	381,740	1,265,534
100,000 Plus	239	44,239,998	2,306,926	4,395,612	2,891,338	6.54%	5,427,005	11.66%	\$1.43	(605,265)	(1,172,227)	78,766	578,383
San Diego County Total	6,786	151,835,577	2,865,792	5,033,487	5,511,558	3.63%	11,336,312	7.33%	\$1.51	(408,621)	(1,159,729)	1,248,720	4,040,460

Lease rates are on an industrial-gross basis.



Conditions Easing

by **Josh West, SIOR**

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As we wrap up the third quarter of 2023, “normal” life seems to be coming back into the picture, and the industrial market is easing off of the boom from the past couple of years. Interest rates are on the rise, while vacancy remains low, and rental rates are still perched at historic levels. This has all combined to create problems for tenants and owner-users in their search for quality space.

The low vacancy has reduced the volume of leases and sales completed as many tenants are deciding to renew in place due to the lack of options. The I-15 Corridor, for example, finished the third quarter of 2023 at a vacancy rate of 2.6%. Much of this demand is driven by e-commerce business. Brick-and-mortar retail has lost a large chunk of business to online shopping, and with that change in habits came a huge rise in demand for warehouse space resulting from increased logistics demand across the board.

Due to high interest rates curtailing purchase options, and limited leasing availability options, lease rates have continued to stay strong. The average lease rate in the San Diego market is \$1.50 per square foot NNN while the Central County average lease rate is closer to \$1.69 per square foot NNN. As of now, there does not seem to be an end in sight for industrial demand. The overall industrial market has remained stable and is still considered one of the safest places to put your money. Cap rates for quality product in the industrial sector remain around 5-6%.

San Diego companies in the market to purchase a building are feeling the squeeze as well. The average price per square foot for quality industrial buildings has remained fairly stable despite the high interest rates. Sellers have not adjusted their expectations to the reality of diminishing market values, and buyers are unwilling or unable to pay the high prices seen during the era of low interest rates.

Overall, the industrial market is healthy and will continue to do well for the foreseeable future. New product will relieve the pressure and will allow occupiers to move within the inventory base.

Product Type

MFG./DIST.

Manufacturing / Distribution / Warehouse facilities with up to 49.9% office space.

Submarkets

CENTRAL COUNTY

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

EAST COUNTY

El Cajon, La Mesa / Spring Valley, Santee / Lakeside, Rural East County

NORTH COUNTY

Escondido, Oceanside, San Marcos, Vista, Carlsbad, North Beach Cities, Rural North County

I-15 CORRIDOR

Poway, Rancho Bernardo, Scripps Ranch

SOUTH BAY

Chula Vista, National City, Otay Mesa, South San Diego

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