

MARKETBEAT

San Diego

Industrial Q1 2018



SAN DIEGO INDUSTRIAL

Economic Indicators

	Q1 17	Q1 18	12-Month Forecast
San Diego Employment	1.43M	1.46M	▲
San Diego Unemployment	4.4%	3.5%	▼
U.S. Unemployment	4.7%	4.1%	▼

Feb 2017/2018 used to represent Q1 for San Diego

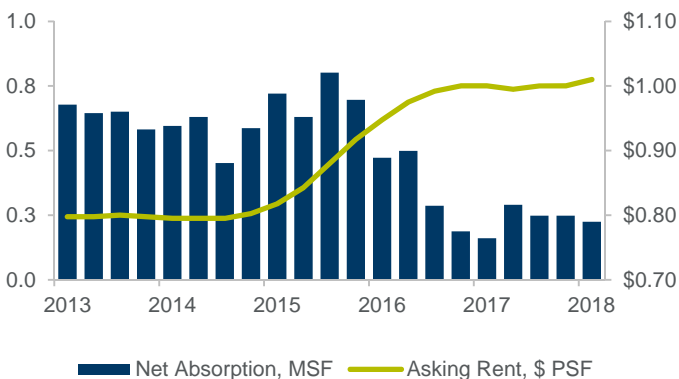
Market Indicators (All Product Types)

	Q1 17	Q1 18	12-Month Forecast
Overall Vacancy	5.1%	4.8%	▼
Direct Net Absorption (sf)	182K	89K	▲
Under Construction (sf)	0.9M	3.3M	▼
Average Asking Rent	\$1.00	\$1.04	▲

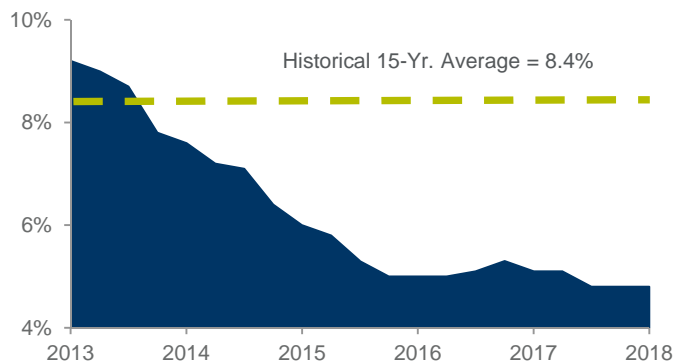
*Rental rates reflect triple net asking \$psf/monthly

Direct Net Absorption/Asking Rent (Triple Net, Monthly)

4-QTR TRAILING AVERAGE



Overall Vacancy – All Product Types, incl. Sublease



Economy

The San Diego employment market continued to record job growth, adding 27,900 jobs (+1.9%) year-over-year through February 2018. During the same time period, the unemployment rate decreased 90 basis points (bps), dropping to 3.5%. Also worth noting, the current rate is 250 bps below the 28-year average of 6%. All employment sectors are expected to grow at a combined growth rate of 1.4% in 2018, according to Moody's Analytics.

San Diego's economy of \$215.3 billion as measured by gross regional product in 2016 grew an estimated 2.9% in 2017 and is forecasted to grow an additional 3.8% in 2018 – above its 10-year average growth rate of 2.3%.

Continuing to bode well for the industrial marketplace is that economic activity in the manufacturing sector again expanded in March, with an ISM index reading of 59.3%. Although the ISM decreased 150 bps from February's reading of 60.8%, an ISM reading above 50% indicates that the manufacturing economy is generally expanding; below 50% indicates that it is generally contracting. The overall economy grew for the 107th consecutive month in the U.S. Of the 18 manufacturing industries, 17 reported growth in March of 2018.

Market Overview

At the close of Q1 2018, industrial vacancy (including sublease) in the San Diego marketplace stood at 4.8%, unchanged from last quarter and 30 bps lower compared to a year ago. Overall vacancy has been hovering around 5% for the past 10 consecutive quarters and now stands at the lowest level recorded by Cushman & Wakefield in 15 years.

Across the region, the market is the tightest for manufacturing space with vacancy at 2.8%, a decrease of 120 bps from a year ago. Vacancy (including sublease) for incubator multi-tenant space (IMT) now stands at 4.4% countywide versus 4.6% twelve months ago. Distribution center space vacancy currently stands at 4.6%, a decrease of 20 bps from last year. Meanwhile, vacancy for R&D product has increased 170 bps over the last year and now stands at 9.3%.

After achieving nearly one million sf of occupancy growth in the latter half of 2017, fueled by a strong third quarter, tenant activity in San Diego's industrial sector slowed down a bit during the opening months of 2018 but still maintained its positive momentum - representing its 26th of the last 27 quarters of occupancy gains except for Q2 2017. Tenants absorbed 121,300 sf in North County submarkets, 61,650 sf in South County yet returned 94,300 sf to Central County – most of it to Kearny Mesa submarket - resulting in an overall positive net absorption of 88,600 sf countywide in Q1 2018.

Carlsbad's occupancy grew by just over 173,200 sf, making it the most active submarket in Q1 2018. Nortek, taking occupancy of its 89,000-sf space at the recently-delivered Beta building within Atlas at Carlsbad, contributed to the growth of the submarket. Additionally, Heat Factory moved into 42,000 sf at 2793 Loker Ave. and Cal-Comp USA moved into 38,500 sf at 1940 Camino Vida Roble. Vista also recorded a strong positive growth of 91,000 sf in Q1 2018. Notably, Killion Industries took back 45,360 sf at 2480 Ash St., a property it

owns. Otay Mesa rang in Q1 2018 with nearly 82,000 sf of positive net absorption. 3PL provider On Time Logistics contributed to Otay Mesa's growth this quarter by expanding into 44,000 sf at 2323 Avenida Costa Este.

Among submarkets where tenants returned space in Q1 were Kearny Mesa and Chula Vista. Kearny Mesa recorded a negative 124,000 sf of net absorption as a result of several mid-size move-outs. Notably, 5454 Ruffin Rd. was vacated this quarter as BLT Enterprises finished a complete renovation of the property. Similarly, in Chula Vista, Leviton vacated and sold 106,000-sf 860 Harold Pl. to Lincoln Property Company who plans to completely remodel the project.

Average asking rent for all product types combined was \$1.04 psf per month on a NNN basis compared to \$1.03 psf last quarter and \$1.00 psf a year ago. The average rent at \$1.04 psf as of Q1 2018 is at the highest level we have ever tracked and has increased 13.0% since the end of this past recession (\$0.92 psf Q2 2009). Since the end of the last recession in 2009, the average rent has increased the most for IMT space (+24.5%) compared to other product types, followed by R&D (+19.2%), distribution (+17.2%) and manufacturing (+12.2%).

Year-over-year, average rent for IMT has increased 11.4% to \$1.17 per month and rent for MFG space has increased 10.8% to \$0.92 psf per month. This trend is driven by the demand for modern and specialized space for manufacturers and small industrial users. In response, we are not only seeing asking rental rates increase but also an increasing trend of renovations of older product to make them more appealing to tenants.

COUNTYWIDE DIRECT VACANCY AT 3.8% IS AT A 15-YEAR LOW

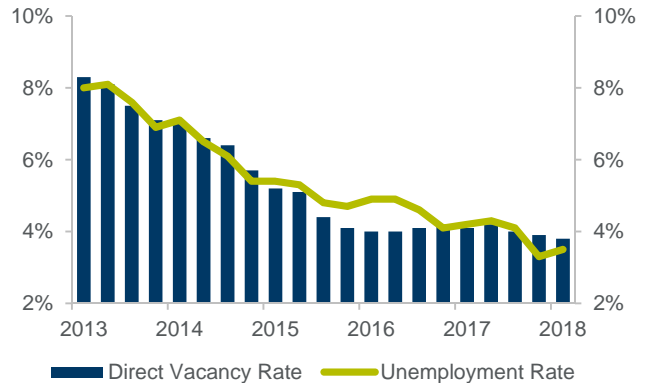
There are currently 32 industrial buildings totaling nearly 3.3 million square feet (msf) under construction, the highest level in 12 years (3.6 msf in Q1 2006). However, with a low countywide direct vacancy of 3.8%, it is unlikely that this supply will satisfy demand for new, functional space. According to our calculations, 57% of industrial space countywide was built before 1990 and barely 3.0% of space was built after 2010. This means that more than half of leasable industrial buildings in San Diego lack modern design features for today's demanding tenants who require high-functioning and efficiently designed product. This trend has led to an increase in speculative (SPEC) construction as developers and landlords become more bullish on their prospect of leasing new space. Of the space that is currently under construction, 74% (or 2.4 msf) is SPEC development.

While no new buildings were completed in Q1 2018, a whopping 2.6 msf of new construction is expected to be delivered this year. Further, at least 874,000 sf of the expected 2018 deliveries have been committed to by tenants or owners including General Atomics, Vertex Pharmaceuticals, Exeter and HM Electronics.

Several projects across the county officially broke ground during Q1 2018. LBA Realty broke ground on a major renovation of 4400 Ruffin Rd. in Kearny Mesa; the renovation will result in a new 106,000-sf warehouse that will enable the campus to accommodate a variety of users. Additionally, 9269 Lightwave also broke ground in Kearny Mesa. This infill project is expected to be completed in 2018.

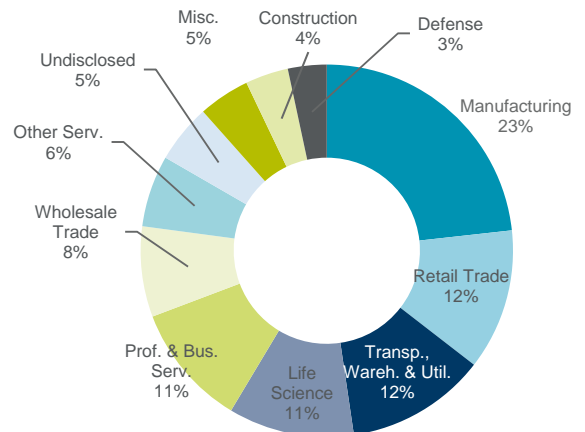
Direct Vacancy vs. Unemployment Rate

DECLINE IN VACANCY CORRELATES DECLINE IN UNEMPLOYMENT



Tenant Demand by Industry Type

TOP 3 INDUSTRY SECTORS ACCOUNT FOR 47% OF TOTAL DEMAND



Outlook

- With just 37% of 2018's expected deliveries pre-leased at this time, we anticipate a momentary uptick in vacancy as those SPEC projects are delivered vacant. However, we do not expect this new, well-equipped space to be vacant long due to fervent demand.
- There are 3.7 msf of active tenant requirements for space over the next 24 months. Over 53% or 2.0 msf of these users are in the earliest stages of their pursuit, having opened their search or toured the market. While not all of the tenants in the market will transact in the short-term, these levels provide a barometer of leasing activity in quarters to follow. Additionally, those tenants in early stages of their pursuit may line up their timing with the delivery of new construction.

SUBMARKET	TOTAL BLDGS	INVENTORY (SF)	SUBLET VACANT (SF)	DIRECT VACANT (SF)	OVERALL VACANCY RATE	CURRENT DIRECT NET ABSORPTION (SF)	YTD DIRECT NET ABSORPTION (SF)	UNDER CNSTR (SF)	AVERAGE ASKING RENT (ALL Types)
North County	2,023	51,712,442	412,985	2,242,827	5.1%	121,297	121,297	1,973,638	\$0.96
Central County	2,281	80,569,354	990,854	2,638,525	4.5%	-94,338	-94,338	969,064	\$1.30
South County	621	30,246,403	174,916	1,373,944	5.1%	61,653	61,653	347,504	\$0.70
TOTAL	4,925	162,528,199	1,578,755	6,255,296	4.8%	88,612	88,612	3,290,206	\$1.04
R&D	837	33,650,159	642,009	2,492,310	9.3%	-158,722	-158,722	615,250	\$1.49
MFG	2,457	64,179,811	238,210	1,510,952	2.8%	211,893	211,893	949,937	\$0.92
IMT	628	20,630,944	167,400	744,130	4.4%	-101,829	-101,829	0	\$1.17
DIST	1,003	44,067,285	531,136	1,507,904	4.6%	137,270	137,270	1,725,019	\$0.76
TOTAL	4,925	162,528,199	1,578,755	6,255,296	4.8%	88,612	88,612	3,290,206	\$1.04

Rental rates reflect triple net (NNN) asking rents \$psf/monthly. Vacancy rate includes direct and sublease. Net absorption excludes sublease.

Key Lease Transactions Q1 2018

PROPERTY	SF	TENANT	LANDLORD	TYPE	SUBMARKET
2820 Whiptail Loop	116,000	PODS of San Diego LLC	Ryan Co / Carlsbad Industrial Park LP	Direct	Carlsbad
3210 Executive Ridge	67,476	Vista Industrial Products	TDA Investment Group	Direct	Vista
16262 W. Bernardo Dr.	55,964	LRAD	STOS Partners	Direct	Rancho Bernardo
1210 Air Wing Rd.	54,404	Whalen, LLC	San Diego Industrial 1, LLC	Direct	Otay Mesa
2793 Loker Ave. W.	42,268	Heat Factory	MCP SoCal Industrial – Loker LLC	Direct	Carlsbad

Key Sale Transactions Q1 2018

PROPERTY	SF	BUYER	SELLER	PRICE / \$PSF	SUBMARKET
9965-9995 Summers Ridge Rd.	247,168	ARE, Inc.	Quidel Corporation	\$148,650,000 / \$601	Sorrento Mesa
2819 Loker Ave.	161,310	BLT Enterprises	Hines Global REIT, Inc.	\$40,000,000 / \$248	Carlsbad
Activity Business Center	160,811	BKM Capital Partners LP	Lincoln Property Company	\$28,100,000 / \$175	Miramar
901 Bay Marina Dr.	91,541	RREEF	Stos Partners	\$21,000,000 / \$229	National City
1395 Park Center Dr.	158,784	CapRock Partners	Vista Industrial Products	\$18,440,000 / \$116	Vista

Under Construction Q1 2018 — selected projects 75,000 sf+

PROPERTY	RELEASED			ADDRESS	PRODUCT TYPE	ESTIMATED COMPLETION	SUBMARKET
	SF	SF	%				
Pacific Vista Commerce Ctr.	405,907	116,000	29%	2800-2820 Whiptail Loop	DIST	2019	Carlsbad
Ridgeview Business Park	302,500	152,000	50%	14311-14177 Kirkham Way	DIST	2018	Poway
Carlsbad Raceway - Distribute	277,351	0	0%	Lionshead Ave.	DIST	2018	Carlsbad
Otay Logistics Center	268,454	24,839	9%	7110-7112 Enrico Fermi Pl.	MFG	2018	Otay Mesa
Production	222,028	0	0%	2946-2954 Norman Strasse Rd.	MFG	2018	San Marcos
Exeter Distribution Center	212,088	212,088	100%	1925-2005 Harmony Grove Rd.	DIST	2018	Escondido
Carlsbad Oaks North - Vector	172,655	0	0%	2882 Whiptail Loop	MFG	2018	Carlsbad
La Jolla Spectrum Tech Park - Bldg. B	170,523	170,523	100%	3215 Merryfield Row	R&D	2018	Torrey Pines
Carlsbad Oaks North - Create	146,108	0	0%	2827 Whiptail Loop	R&D	2018	Carlsbad
HM Electronics - Lots 18 & 19	140,000	140,000	100%	2848 Whiptail Loop	MFG	2018	Carlsbad
Carlsbad Oaks North - Lot 17	126,020	0	0%	Lot 17 Whiptail Loop	DIST	2018	Carlsbad
Pacific Coast Collection	124,581	0	0%	1319 Rocky Point Dr.	DIST	2018	Oceanside
4400 Ruffin Rd.	106,000	0	0%	4400 Ruffin Rd.	DIST	2018	Kearny Mesa
Carlsbad Oaks North - San Diego Hat Co.	83,000	83,000	100%	Whiptail Loop	MFG	2018	Carlsbad
Siempre Viva Business Park - Bldg. 17	79,050	0	0%	8500 Kerns St.	DIST	2018	Otay Mesa

INDUSTRIAL SUBMARKETS
SAN DIEGO



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Jolanta Campion

Director of Research, San Diego & Las Vegas
jolanta.campion@cushwake.com

Alexa Kruthers

Research Analyst
alexa.kruthers@cushwake.com

4747 Executive Drive, Suite 900
San Diego, CA 92121
Tel: 858.625.5235
Fax: 858.630.6320
CA License 01880493

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