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San Diego Leasing Update

Wednesday, February 15, 2012 | Western Real Estate Business | David Marino, Jason Hughes

San Diego's commercial real estate market finished 2011 showing positive signs of a recovering market. Employment growth began to have an impact on occupancy rates for both the office and industrial sectors – as nearly 865,000 square feet of office, lab and industrial space was leased. The total net absorption for 2011 in San Diego was about 1,957,000 square feet. That, combined with the 2,134,000 square feet leased in the fourth quarter of 2010, reduced the total inventory by 8 percent over the past five quarters alone.

While every San Diego office submarket except for Downtown saw a drop in availability over the past two years, the most improved submarkets were Sorrento Mesa, the I-15 corridor, Del Mar Heights and Mission Valley. UTC, Carlsbad and Downtown ended the year with the highest office space availabilities in the county and continue to be where the best values can be found.

Downtown and Carlsbad both struggle with anemic leasing volume – averaging vacant space on the market of nearly 2.5 years a piece. There has been a mild recovery in Torrey Pines' wet lab space, as the biotech sector shows signs of recovery and bio-fuel companies have demanded more wet lab space. As UTC Class A office shows signs of firming up in the near future, 2014 will be a tough year as LPL Financial relocates out of six buildings on the Towne Centre Drive corridor and into a new 417,000-square-foot, high-rise, build-to-suit building with Hines at La Jolla Commons in UTC. Del Mar Heights should see some recovery slowing in the next year when Bank of Internet moves out of 40,000 square feet in that market, while other tenants like Covario and Legend 3D consider value-oriented submarkets and move accordingly. Latham & Watkins will be also moving out of second-generation space, likely into a new build-to-suit opportunity that the firm is pursuing. Downtown's new challenge is a lack of quality "cool" space to accommodate the surge in tech companies interested in locating there. Alternatively, San Diego companies are beginning to fully understand the value of being in Downtown's California Enterprise Zone which, in many cases, offsets all of a company's parking expenses.

This year will be another year of net absorption across all product types, as another 2 million square feet is likely to come off the market. This will also go down as a transitional year, where the pendulum starts to move toward the landlords' favor.

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