

## MARKET TRENDS

# SAN FRANCISCO OFFICE

### MARKET DRIVERS

The San Francisco office market is reporting its eighth consecutive quarter of negative net absorption, approximately negative 5.1 million SF year-to-date, with this quarter accounting for nearly 40%. For additional perspective, 2023's negative absorption is higher than 2022's negative 4.9M SF with one more quarter remaining in the year. Total office vacancy continues rise and currently sits at 28.8% - up 200 basis points (bps) quarter-over-quarter. Firms continue to reassess their office needs, which can be seen in the uptick of 40 bps quarter-over-quarter to a 6.3% sublease vacancy rate. Year-over-year sublease vacancies increased by 130 bps, so despite the continuing popularity of subleases for companies that are wary of long-term commitments, supply is still outpacing demand.

Leasing activity throughout the quarter fell year-over-year by 21.8% to 724,039 SF. Class A and B office buildings accounted for 646,600 SF of the quarter's leasing activity, while Class C office buildings accounted for only 77,439 SF. Throughout the market, rental rates continue to decline as average direct rental asking rates fell to \$53.74/fs. Within Class A and B offices in the Financial District, average direct rental rates fell 9.1% year-over-year to \$56.83/sf full service. Despite the dip in rental rates, there is a large discrepancy in pricing with very limited compression. Premier Class A offices with desirable amenities and views remain highly competitive and have asking rates well over \$80/sf full service, with the very best suites commanding rents north of \$100/sf full service. Further demonstrating the "flight to quality" trend, the bifurcation in pricing can be seen in Class B and C offices reporting average direct rental rates of \$48.19/sf full service and \$39.76/sf full service respectively.

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## Market Summary

	3Q23	2Q23	3Q22	Annual Change
New Construction	310,971	126,782	0	N/A
Under Construction	873,881	1,184,852	1,155,503	-24.4%
Direct Vacancy Rate	22.5%	20.8%	17.5%	28.6%
Sublease Vacancy Rate	6.3%	5.9%	5.0%	26.0%
Overall Vacancy Rate	28.8%	26.8%	22.4%	28.6%
FIDI Direct Lease Rate (A&B)	\$56.83	\$57.47	\$62.53	-9.1%
Leased SF	724,039	1,038,768	926,449	-21.8%
Sold SF	483,299	85,365	177,378	172.5%
Total Net Absorption	(2,044,441)	(1,820,438)	(1,744,152)	N/A

724K SF  
LEASING ACTIVITY

-2.0M SF  
NET ABSORPTION

28.8%  
VACANCY RATE

\$56.83  
ASKING RENT (AVG)

311K SF  
NEW DELIVERIES

Year-Over-Year Trend

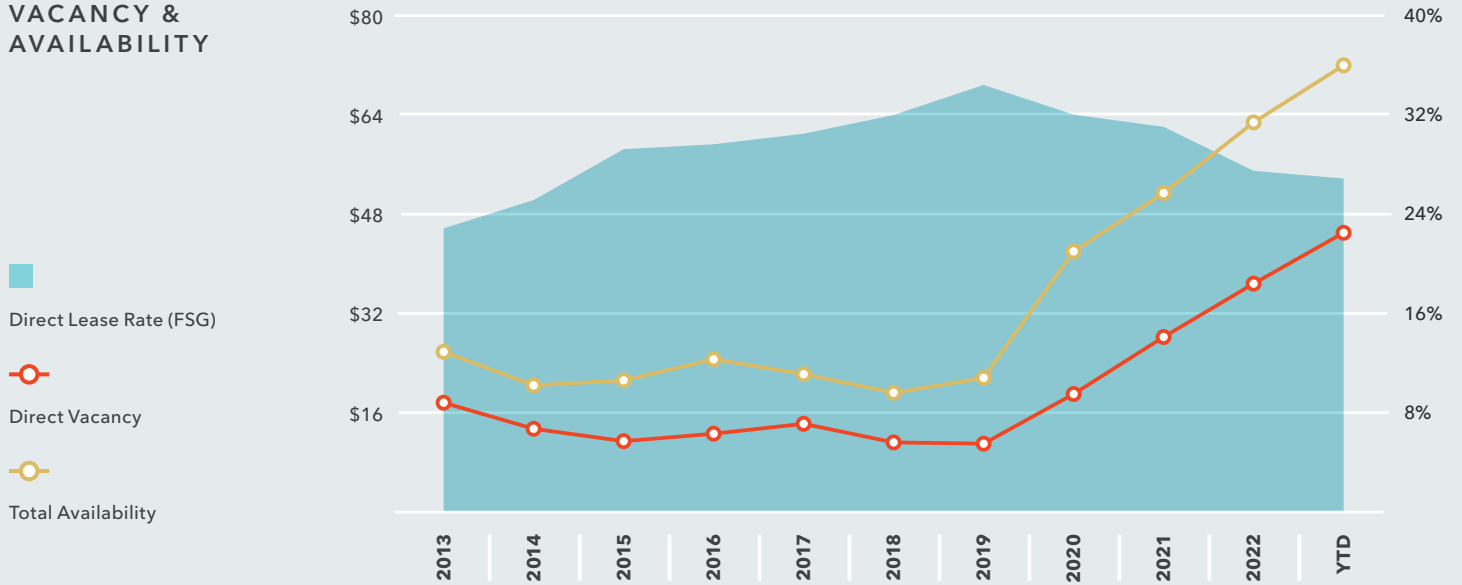
## Market Highlights

**TOTAL VACANCY** continues to rise, currently 28.8%.

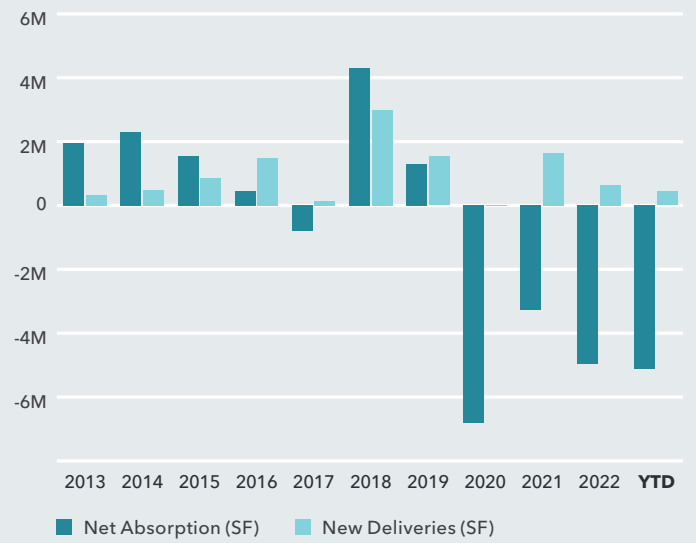
**SUBLEASE VACANCY** increased by 40 bps quarter-over-quarter to 6.3%.

**OFFICE INVESTMENT** sales activity grew, totaling 483,299 SF.

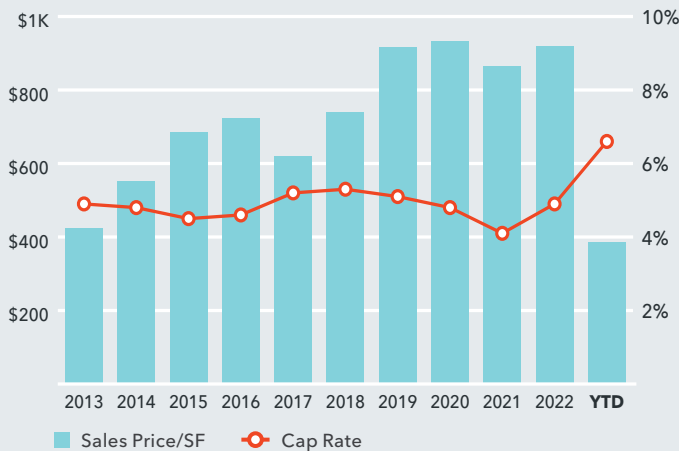
## LEASE RATE, VACANCY & AVAILABILITY



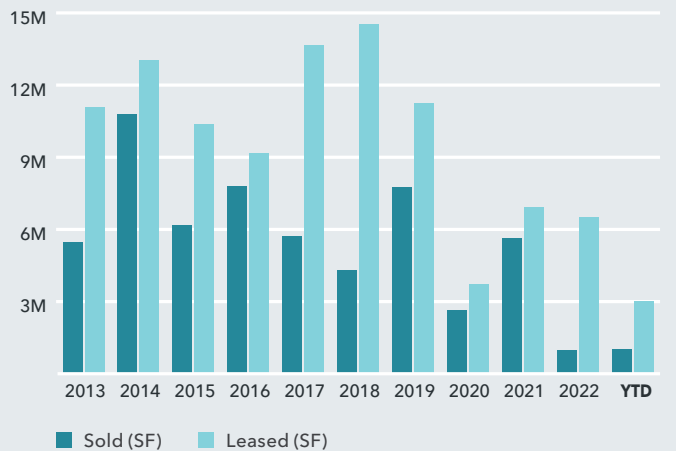
## NET ABSORPTION & NEW DELIVERIES



## AVERAGE SALES PRICE/SF & CAP RATE



## SALE VOLUME & LEASING ACTIVITY



## SUBMARKET STATISTICS

Submarket	Total Inventory	Under Construction	Direct Vacancy Rate	Sublet Vacancy Rate	Total Vacancy Rate	Total Availability Rate	3Q23 Total Net Absorption	YTD Total Net Absorption	3Q23 Leasing Activity	YTD Leasing Activity	Average Rental Rate (FS)
Civic Center	616,967	0	21.9%	0.0%	21.9%	23.3%	5,166	17,302	12,289	38,150	\$37.38
Financial District	26,612,222	0	26.6%	4.4%	31.0%	36.1%	-569,229	-1,268,683	194,033	885,145	\$56.71
Jackson Square	2,369,488	0	16.9%	1.7%	18.6%	24.3%	21,147	33,448	69,889	155,637	\$45.90
Mid Market	4,790,617	0	21.2%	6.9%	28.0%	43.3%	-25,434	-330,401	0	39,251	\$51.01
Mission Bay/China Basin	5,368,289	539,046	9.3%	19.7%	28.9%	41.7%	-609,940	-553,216	5,737	274,814	\$60.57
Mission/Potrero	3,215,584	0	18.6%	2.9%	21.5%	24.6%	4,755	106,115	103,854	202,094	\$45.49
Rincon/South Beach	6,048,878	0	22.8%	8.1%	31.0%	40.4%	-68,775	-434,958	37,772	129,055	\$51.75
Showplace Square	3,773,958	24,956	17.3%	15.3%	32.6%	45.9%	-36,458	-226,347	1,834	32,673	\$48.10
South Financial District	29,964,529	77,589	18.2%	5.9%	24.0%	33.2%	-430,397	-1,791,538	170,739	829,741	\$56.24
SOMA	5,904,050	232,290	28.4%	4.7%	33.1%	35.7%	-92,763	-316,125	13,720	122,134	\$47.27
Union Square	4,360,240	0	25.5%	2.7%	28.2%	32.6%	11,886	-43,560	35,756	142,313	\$53.36
Van Ness Corridor/Chinatown	1,339,263	0	16.9%	0.2%	17.1%	30.3%	-42,844	-13,187	500	16,581	\$47.76
Waterfront/North Beach	3,930,295	0	24.5%	5.4%	29.9%	39.6%	-190,033	-185,032	33,895	73,990	\$46.95
Yerba Buena	4,051,906	0	39.9%	6.7%	46.5%	51.7%	-21,522	-132,664	44,021	73,828	\$50.18
<b>San Francisco Totals</b>	<b>102,346,286</b>	<b>873,881</b>	<b>22.5%</b>	<b>6.3%</b>	<b>28.8%</b>	<b>36.3%</b>	<b>-2,044,441</b>	<b>-5,138,846</b>	<b>724,039</b>	<b>3,015,406</b>	<b>\$53.74</b>
Class A	57,149,589	768,412	22.0%	7.1%	29.1%	37.3%	-1,571,484	-3,709,132	290,194	1,691,268	\$59.25
Class B	37,729,121	105,469	23.4%	5.9%	29.3%	36.7%	-429,829	-1,271,747	356,406	1,032,743	\$48.19
Class C	7,467,576	0	21.6%	1.6%	23.3%	27.0%	-43,128	-157,967	77,439	291,395	\$39.76

## MARKET DRIVERS CONTINUED

483,299 SF of office properties traded hands throughout the quarter, after several quarters with very limited sales activity. Two major transactions that occurred include 350 California and 60 Spear. 350 California traded for \$61 million (\$204.94/sf) and 60 Spear sold for \$41 million (\$260.42/sf). While the sale of 350 California closed at a fraction of its initial listing price back in 2020, the transaction may “unfreeze” the investment sales market, generating fresh activity the region hasn’t seen since the start of the pandemic, though interest rates remain a significant wild card.

## ECONOMIC REVIEW

The unemployment rate throughout San Francisco ticked up slightly to 3.2% in July, 50 bps higher than the 2.7% in April of this year. Throughout 2023, the unemployment rate has remained relatively flat ranging from 2.7% to 3.3% indicating a stable labor market.

Inflation has been on the rise over the last two years which has led to interest rate hikes, lay-offs, and continues to strain the supply chain. In turn, the cost of raw materials used in construction have increased, delaying delivery times and tenant improvement projects.

## NEAR-TERM OUTLOOK

Office occupancy in San Francisco for the week of September 13th grew to 42.6%, up 2.6% from the previous week according to data from Kastle Systems, a company that tracks building occupancy through its access card systems. While occupancy recently ticked up, it remains relatively flat compared to the 41.8% reported in December of 2022 and appears to have leveled out in the low-mid 40% range.

As firms continue to shed space and “right-size”, office requirements under 10,000 SF have been highly competitive. Smaller suites that are at most 5,000 SF remain difficult to find. Many of the large sublease spaces that have been on the market over the last two years are starting to disappear—as they are either being absorbed, or the remaining term length is no longer viable. The growing emergence of new Artificial Intelligence companies is bringing some optimism back to the market as companies like OpenAI have been rumored to be looking to expand their office footprint. That said, the impact of AI company office leasing very much remains to be seen, particularly given the amount of space available on the market and the continuing trend of negative net absorption.

TOP SALE TRANSACTIONS 3Q 2023

Property	Submarket	Square Feet	Sale Price	\$/SF	Buyer	Seller
350 California	Financial District	297,642	\$61,000,000	\$204.94	The Swig Company	Mitsubishi UFJ Financial Group
60 Spear	South Financial District	157,436	\$41,000,000	\$260.42	Presidio Bay Ventures	Clarion Partners
550 Bryant	SOMA	13,220	\$4,968,000	\$375.79	Broad Spectrum	First Person, Inc.

TOP LEASE TRANSACTIONS 3Q 2023

Property	Submarket	SF	Transaction Date	Landlord	Tenant
100 1st	South Financial District	57,117	July 2023	OKTA	HiveAI
55 Francisco	Waterfront/North Beach	22,021	July 2023	Jamestown, LP	DPR Construction
One Front	Financial District	11,248	August 2023	Paramount Group, Inc.	LaceWork

TOP UNDER CONSTRUCTION

Property	Address	Submarket	SF	Owner	Delivery
Block 15 Station A	420 23rd St	Mission Bay/China Basin	326,250	Associate Capital	2Q 2025
45 3rd	45 3rd St	South Financial District	77,589	Hearst	1Q 2024
531 Bryant	531 Bryant St	South of Market	51,223	Urban Land Development	2Q 2024

Data Source: KM Research, CoStar, U.S. Bureau of Labor Statistics



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The information in this report was composed by the Kidder Mathews Research Group.

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<b>COMMERCIAL BROKERAGE</b>	<i>\$12B</i> TRANSACTION VOLUME ANNUALLY	<i>32.1M</i> ANNUAL SALES SF	<i>41.2M</i> ANNUAL LEASING SF
<b>ASSET SERVICES</b>	<i>53M</i> MANAGEMENT PORTFOLIO SF	<i>771+</i> ASSETS UNDER MANAGEMENT	<i>250+</i> ASSET SERVICES CLIENTS
<b>VALUATION ADVISORY</b>	<i>2,800+</i> ASSIGNMENTS ANNUALLY	<i>41</i> TOTAL APPRAISERS	<i>23</i> WITH MAI DESIGNATIONS

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