

MARKET TRENDS

SAN FRANCISCO OFFICE

MARKET DRIVERS

San Francisco continues a streak of ten consecutive quarters of negative net absorption in quarter one, posting negative 211,904 SF. Total office vacancy has decreased to 30.6% in Q1 2024, a drop of 20 basis points from the previous quarter. The continued popularity of subleases for companies wary of long-term commitments outpaced supply this quarter with the sublease vacancy rate decreasing 20 bps to 5.7%. This continued sublease popularity coupled with a historically low number of deliveries helped to lessen the impact of a decline in leasing activity to see the third smallest negative net absorption figure in the post pandemic era.

Leasing activity throughout the quarter shrunk year-over-year by 25.7% to 1,078,373 SF. Class A and B office buildings led leasing activity, accounting for approximately 62.6% (675,049 SF) and 31.7% (342,303 SF) of total leasing activity, respectively. Throughout the market, rental rates continue to decline as average direct rental asking rates fell to \$50.50/sf. Within the Financial District, direct rental rates for Class A and Class B spaces have fallen to \$55.90 /sf and \$49.00 /sf respectively. Despite the dip in rental rates, there is a large discrepancy in pricing with very limited compression. Overall, the office market still exhibits the bifurcation characteristic of the post-pandemic era as premier Class A offices with desirable amenities regularly rent for above \$75 /sf full service and average direct rental asking rates for Class B and C offices have fallen to \$42.50/ sf and \$34.50 /sf full service respectively. Meanwhile, turnkey and sub 10,000 SF spaces have continued to drive activity with larger and non-plug-and-play product remaining a difficult sell.

32,394 SF of office properties traded hands for \$12,170,000 throughout the quarter. This represents a historic low point in investment activity, even within the post pandemic era. The investment sales market remains depressed with this quarter underperforming all but four quarters in the post pandemic era. High interest rates continue to exert downward pressure on the market.

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Market Summary

	1Q24	4Q23	1Q23	YOY Change
Direct Vacancy Rate	25.0%	24.7%	19.6%	540 bps
Overall Vacancy Rate	30.6%	30.8%	24.4%	620 bps
FIDI Direct Lease Rate (A&B)	\$55.39	\$56.83	\$58.42	-5.2%
Under Construction SF	242,086	700,015	1,445,847	-83.3%
	1Q24	2023 Total	1Q23	YOY Change
Construction Deliveries	0	310,971	0	N/A
Leased SF	1,078,373	2,340,221	1,450,767	-25.7%
Sold SF	32,394	753,243	591,159	-94.5%
Total Net Absorption	(211,904)	(1,937,232)	(1,249,644)	N/A

↑ **1.1M SF**
LEASING ACTIVITY

↓ **-212K SF**
NET ABSORPTION

↑ **30.6%**
VACANCY RATE

↓ **\$50.50**
ASKING RENT (AVG)

↔ **0 SF**
NEW DELIVERIES

Year-Over-Year Trend

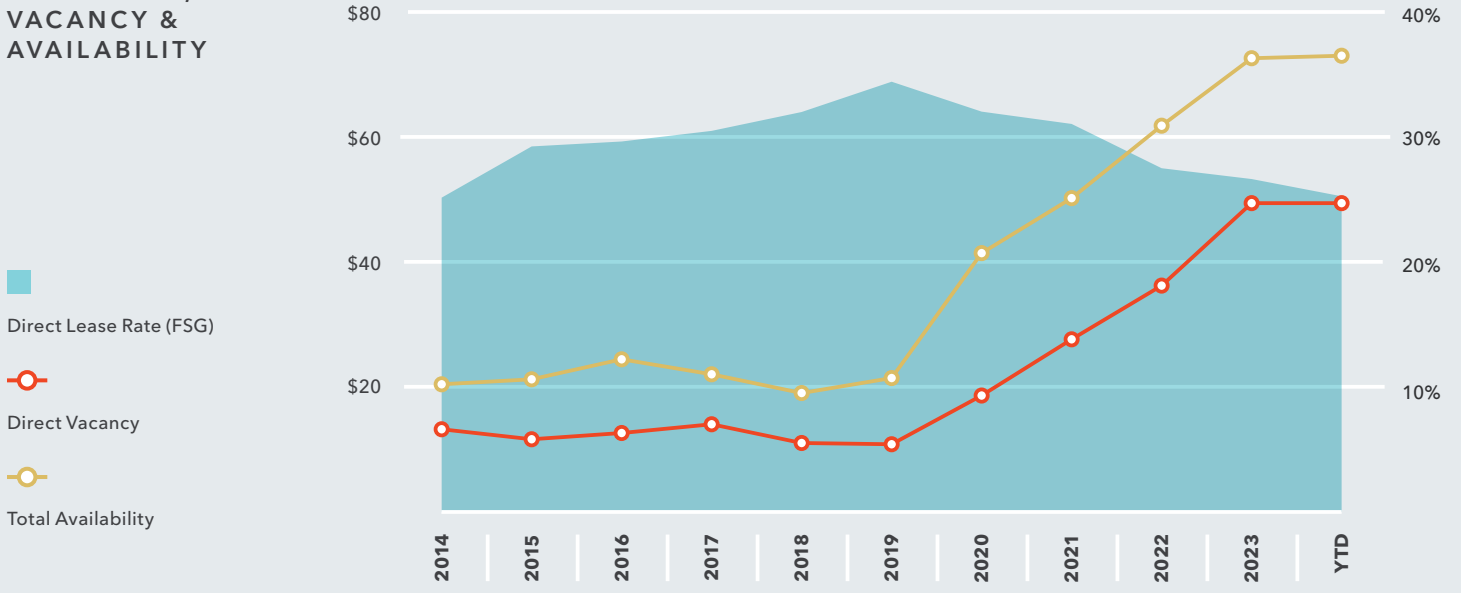
Market Highlights

NET ABSORPTION posted the smallest negative figure in 9 quarters at -211,903 SF

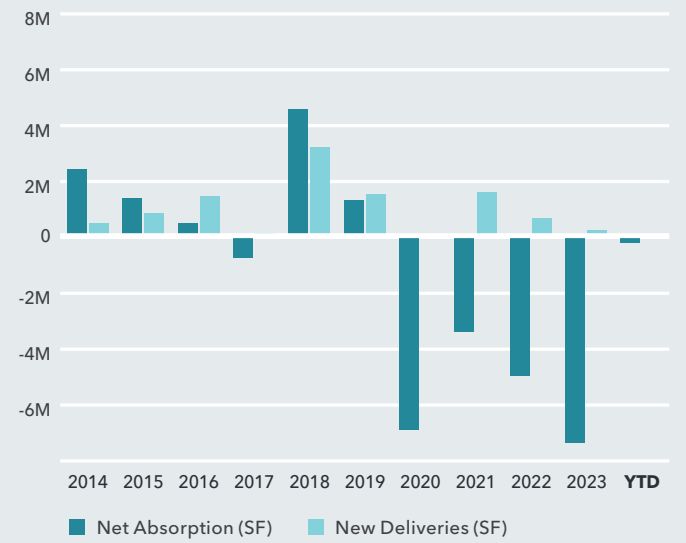
TOTAL VACANCY dropped to 30.6%, the first decline since 2019

MARKET RENTAL RATES continue to decline, standing at \$50.50 PSF full service

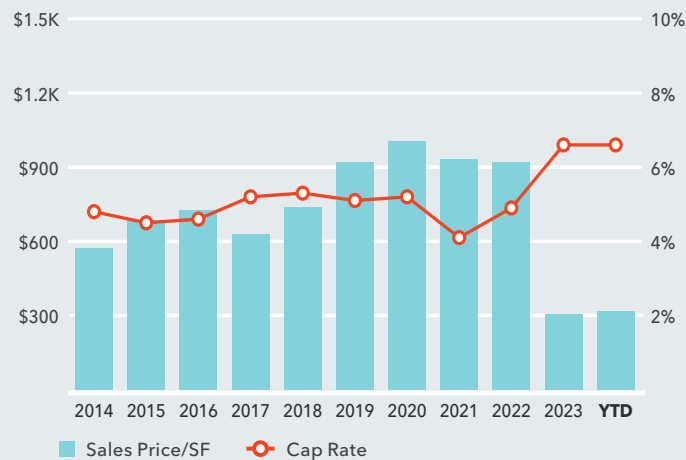
LEASE RATE, VACANCY & AVAILABILITY



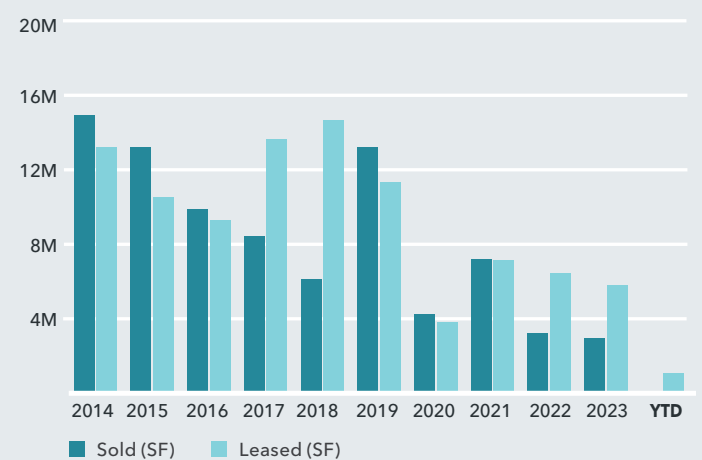
NET ABSORPTION & NEW DELIVERIES



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	1Q24 Total Net Absorption	YTD Total Net Absorption	1Q24 Leasing Activity	YTD Leasing Activity	Direct Rental Rate
Civic Center	616,967	0	23.8%	0.0%	23.8%	27.5%	-14,091	-14,091	885	885	\$35.02
Financial District	26,919,354	0	31.1%	3.5%	34.6%	37.3%	83,147	83,147	367,338	367,338	\$51.82
Jackson Square	2,369,488	0	16.4%	1.6%	18.0%	23.7%	25,390	25,390	42,206	42,206	\$43.42
Mid Market	4,968,155	0	31.7%	6.6%	38.3%	53.9%	-53,346	-53,346	43,328	43,328	\$47.46
Mission Bay/China Basin	5,431,909	212,796	15.3%	10.0%	25.2%	39.0%	8,314	8,314	9,239	9,239	\$57.10
Mission/Potrero	3,163,957	0	15.5%	4.3%	19.8%	26.0%	88,707	88,707	43,496	43,496	\$43.08
Rincon/South Beach	6,061,030	0	20.8%	7.6%	28.4%	35.8%	41,454	41,454	67,009	67,009	\$49.16
Showplace Square	3,736,388	0	18.4%	14.9%	33.3%	49.0%	4,679	4,679	0	0	\$44.76
South Financial District	30,221,183	0	19.7%	5.7%	25.4%	32.2%	-11,334	-11,334	370,766	370,766	\$53.37
SOMA	6,184,055	29,290	24.8%	4.3%	29.0%	34.7%	-62,664	-62,664	80,961	80,961	\$44.59
Union Square	4,335,405	0	25.2%	5.8%	31.0%	36.0%	-70,641	-70,641	10,869	10,869	\$48.46
Van Ness Corridor/Chinatown	1,340,853	0	16.0%	0.8%	18.0%	31.3%	2,296	2,296	4,575	4,575	\$45.14
Waterfront/North Beach	3,931,549	0	30.3%	4.7%	35.0%	37.6%	-159,029	-159,029	15,720	15,720	\$44.60
Yerba Buena	4,027,730	0	40.5%	9.1%	49.5%	52.4%	-94,786	-94,786	21,981	21,981	\$43.86
San Francisco Totals	103,308,023	242,086	25.0%	5.7%	30.6%	37.4%	-211,904	-211,904	1,078,373	1,078,373	\$50.50
Class A	57,787,888	212,796	24.7%	6.0%	30.7%	37.9%	169,808	169,808	675,049	675,049	\$56.00
Class B	37,655,794	29,290	26.7%	5.9%	32.6%	38.5%	-328,948	-328,948	342,303	342,303	\$42.50
Class C	7,864,341	0	21.6%	2.5%	24.1%	27.9%	-52,764	-52,764	61,021	61,021	\$34.50

ECONOMIC REVIEW

The unemployment rate throughout San Francisco continued to tick up slightly through January reaching 4.0%, the highest figure since October of 2021. Since then this growth has reversed course with February posting a figure of 3.8%. That said, this marginal recovery is fully attributable to a decrease in the labor force, not a growth in employment, thereby it should not be taken as an indicator of the strengthening of the labor market. Tech / Information industry and professional / business services sector layoffs have driven the majority of job loss from mid-2023 through Q1 2024 according to data from California Employment Development Department.

Inflation has exhibited declines in recent months, though it still remains above the Federal Reserve's long-term target. This said, the continued overall improvement has largely eliminated the chance of any further rate hikes in 2024, with cuts and their potential timing very much TBD. Despite this decline, inflation remains high, and the effects of two years of robust price increases continue to contribute to layoffs, supply chain strain, and high raw material costs used in construction, the latter of which is delaying delivery times and tenant improvement projects.

NEAR-TERM OUTLOOK

Despite a historically slow quarter in terms of leasing and investment activity, there are a number of positive trends that may signal a long-awaited recovery for the office market in 2024. Firstly, many landlords are faced with critical near-term decisions: years of large vacancies coupled with a bottoming out of both the office and retail markets will drive many properties back into the hands of lenders, force debt restructuring, and/or drive many into discounted sales of their underperforming assets. This reset should not just drive up sales activity but will increase landlord willingness to lease their product at current market rates, thus driving up leasing activity and bringing tenants back into the market. Secondly, looking forward there are limited deliveries scheduled for San Francisco in the near-term. This consistency in supply will help to bring about a return to positive net absorption and will help to stem the decline in rental rates.

Office occupancy in San Francisco for the week of March 13th was measured at 45.7% according to data from Kastle Systems, a company that tracks building occupancy through its access card systems. While occupancy has varied throughout 2024, it has exhibited a general affinity for the mid-upper 40th percentile range, with Q1 occupancy figures the best in four years, marginally outperforming 2023. Federal Reserve narrative concerning cutting rates in 2024 has fluctuated in recent months. If rate cuts were to occur, real estate transaction activity of all kinds would in all likelihood surge upwards. This said, with rates still well in line with historical averages and with other positive trends likely to affect the market this year, we may see a persistent recovery begin in 2024 with or without this stimulus.

SIGNIFICANT SALE TRANSACTIONS 1Q 2024

Property	Submarket	SF	Sale Price	\$/SF	Buyer	Seller
2745-2747 19th Street	Mission/Portrero	7,565	\$5,800,000	\$766.69	STUDY Ventures, LLC	Ahmad Mohazab
47-49 Drumm Street	Financial District	3,894	\$3,000,000	\$770.42	47 Drumm Street, LLC	Eric Smith Ketchum
652-660 Kearny Street	Financial District	5,942	\$2,650,000	\$445.98	JKD Holdings LLC	Chin and Send Tov LLC

SIGNIFICANT LEASE TRANSACTIONS 1Q 2024

Property	Submarket	SF	Transaction Date	Landlord	Tenant
1170 Market Street	MidMarket	37,100	February 2024	Haig G Mardikian Enterprises	Felton Institute
163 Freelon Street	South of Market	24,000	March 2024	Freelon	Undisclosed
275 Battery Street	Financial District	17,073	March 2024	Rockpoint	Consulate General of Japan

SIGNIFICANT UNDER CONSTRUCTION

Property	Address	Submarket	SF	Owner	Delivery
Block 15 Station A	420 23rd St	Mission Bay/China Basin	381,750	Associate Capital	2Q 2025
952-960 Howard St	952-960 Howard St	South of Market	29,290	oWOW	2Q 2024

Data Source: CoStar, United States Bureau of Labor Statistics, Kastle Systems, Kidder Mathews



Kidder Mathews is the largest independent commercial real estate firm on the West Coast, with over 900 real estate professionals and staff in 19 offices in Washington, Oregon, California, Nevada, and Arizona. We offer a complete range of brokerage, appraisal, asset services, consulting, and debt & equity finance services for all property types.

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

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COMMERCIAL BROKERAGE	<i>\$10B</i> 3-YEAR AVERAGE TRANSACTION VOLUME	<i>31.7M</i> ANNUAL SALES SF	<i>42.4M</i> ANNUAL LEASING SF
ASSET SERVICES	<i>51M SF</i> MANAGEMENT PORTFOLIO SIZE	<i>750+</i> ASSETS UNDER MANAGEMENT	<i>250+</i> CLIENTS SERVED
VALUATION ADVISORY	<i>2,600+</i> 3-YEAR AVERAGE ASSIGNMENTS	<i>43</i> TOTAL APPRAISERS	<i>25</i> WITH MAI DESIGNATIONS

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