

MARKET TRENDS

SAN FRANCISCO OFFICE

MARKET DRIVERS

San Francisco continues a streak of eleven consecutive quarters of negative net absorption, posting negative net absorption of 473,735 SF in Q2 2024. Total office vacancy has increased to 30.8% in Q2 2024, a bump of 260 basis points from the previous quarter. While the total number of leases outpaced the first quarter, total square footage transacted fell marginally short due to a six-quarter low in sublease activity. While trends are still down, they are doubtless starting to change, with Q2 negative net absorption the second lowest since Q1 2022 and the fifth lowest in the post-Covid era. Overall, the picture of the market becomes clearer: long-term work-from-home trends have stabilized, most of the city's office tenants with a desire to have already rightsized, and owners of non-performing assets have begun to restructure their financing, incentivizing them to do business again.

Leasing activity throughout the first half of the year grew year-over-year by 24.6% to 3,251,131 SF. Class A and B office buildings led leasing activity, accounting for approximately 52.9% (1,719,193 SF) and 42.2% (1,372,301 SF) of total leasing activity, respectively. Throughout the market, rental rates continue to decline as average direct rental asking rates across all building classes and submarkets fell to \$48.58/SF. Within the Financial District, direct rental rates for Class A and Class B spaces have fallen to \$54.20/SF and \$47.50/SF, respectively. Despite the dip, there is a large discrepancy in pricing with very limited compression. Overall, the office market still exhibits the bifurcation of the post-pandemic era as trophy Class A offices with desirable amenities regularly rent for above \$65/SF full service (some well above) and enjoy a substantially lower vacancy rate, and average direct rental asking rates for Class B and C offices have fallen to \$41.20/SF and \$33.40/SF full service, respectively. Meanwhile, turnkey and sub-10,000 SF spaces have continued to drive activity with larger and non-plug-and-play products remaining a difficult sell.

1,655,727 SF of office properties traded hands for \$117,253,000 throughout the quarter, though this includes the sale of a 45% interest in 1455 Market Street, thus overstating square footage transacted and understating price per square foot. The investment sales market remains depressed with this quarter underperforming all but five quarters in the post-pandemic era. High interest rates continue to exert downward pressure on the market with rate cuts seemingly on the horizon for late 2024.

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Market Summary

	2Q24	1Q24	2Q23	YOY Change
Direct Vacancy Rate	25.1%	24.7%	20.4%	470 bps
Overall Vacancy Rate	30.8%	28.2%	25.7%	510 bps
FIDI Direct Lease Rate (A&B)	\$53.73	\$55.39	\$55.72	-3.6%
Under Construction SF	411,040	411,040	784,286	-47.6%
	2Q24	2024 YTD	2023 YTD	YOY Change
Construction Deliveries	54,452	54,452	101,782	-46.5%
Leased SF	1,618,032	3,251,131	2,608,887	24.6%
Sold SF	1,655,727	1,733,407	995,731	74.1%
Total Net Absorption	(473,735)	(685,639)	(2,803,910)	-75.5%

↑ **1.7M SF**
LEASING ACTIVITY

↑ **-473K SF**
NET ABSORPTION

↑ **25.1%**
DIRECT VACANCY RATE

↓ **\$48.58**
ASKING RENT (AVG)

↓ **54K SF**
NEW DELIVERIES

Year-Over-Year Trend

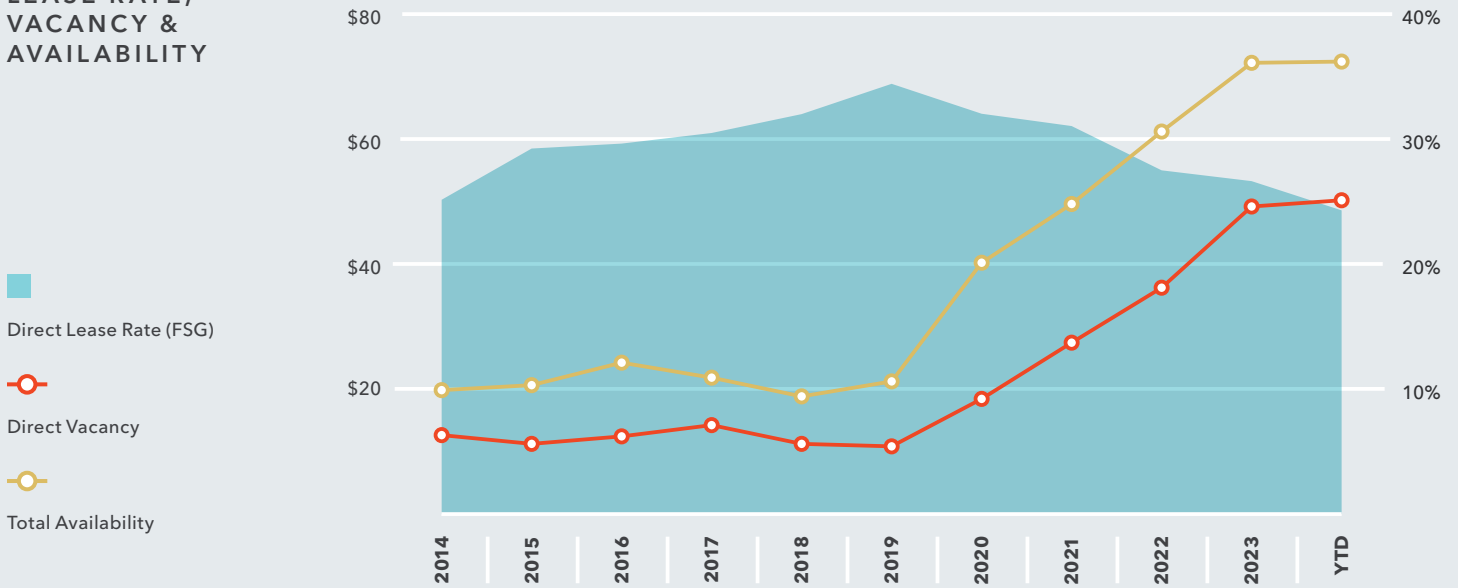
Market Highlights

NET ABSORPTION posted the second lowest negative figure in 11 quarters at -473,735 SF.

LEASING ACTIVITY had the highest in three-quarter total since Q4 2021-Q4 2022.

MARKET RENTAL RATES continue to decline, standing at \$48.58/SF Full Service.

LEASE RATE, VACANCY & AVAILABILITY



BIGGEST SALE OF THE QUARTER

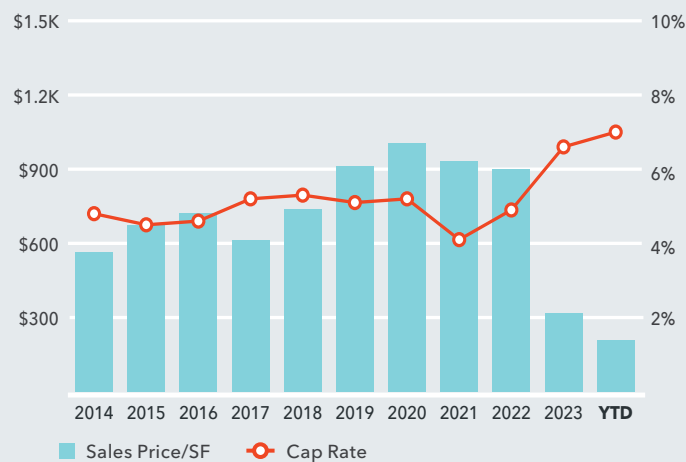
*1455 Market St
San Francisco*



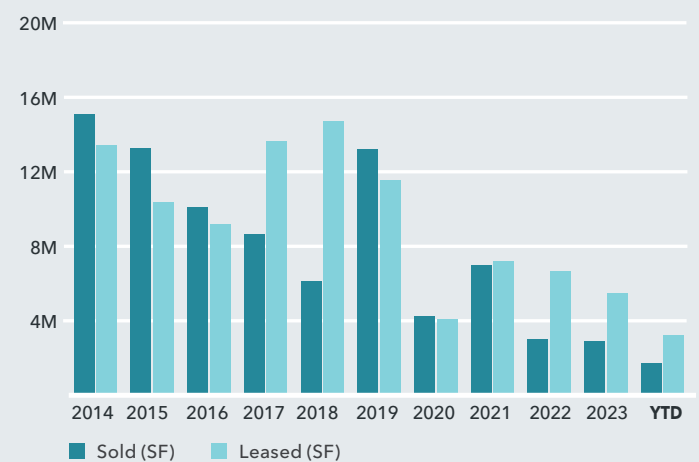
NET ABSORPTION & NEW DELIVERIES



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	2Q24 Total Net Absorption	YTD Total Net Absorption	2Q24 Leasing Activity	YTD Leasing Activity	Direct Rental Rate
Civic Center	616,967	0	23.7%	0.0%	23.7%	24.1%	1,112	-12,979	13,866	14,751	\$33.97
Financial District	26,919,354	0	30.5%	3.3%	33.8%	34.7%	76,759	112,505	621,497	1,023,660	\$50.27
Jackson Square	2,369,488	0	15.9%	1.6%	17.5%	22.4%	45,459	64,299	28,588	85,794	\$42.55
Mid Market	4,968,155	0	28.8%	6.6%	35.5%	49.5%	121,635	283,221	171,261	372,589	\$45.56
Mission Bay/China Basin	5,431,909	212,796	23.2%	9.9%	33.2%	46.2%	-40,453	-68,227	13,442	42,001	\$55.67
Mission/Potrero	3,163,957	0	17.0%	4.2%	21.2%	30.6%	-29,502	63,854	28,159	73,907	\$41.79
Rincon/South Beach	6,061,030	0	21.0%	8.3%	29.3%	37.3%	39,644	54,212	32,993	97,802	\$47.69
Showplace Square	3,736,388	126,537	23.1%	14.8%	37.8%	48.5%	55,327	60,006	21,282	27,461	\$43.42
South Financial District	30,221,183	0	20.8%	6.7%	27.5%	33.5%	-841,482	-537,172	440,122	818,388	\$51.77
SOMA	6,184,055	29,290	23.9%	2.0%	25.8%	30.0%	82,541	33,761	92,857	373,329	\$43.03
Union Square	4,335,405	0	27.3%	4.6%	32.0%	36.2%	-40,851	-127,418	70,941	183,121	\$46.76
Van Ness Corridor/Chinatown	1,340,853	0	15.2%	0.6%	17.9%	29.8%	14,548	16,844	6,759	11,334	\$43.56
Waterfront/North Beach	3,931,549	0	29.9%	4.2%	34.1%	35.2%	33,049	-125,980	62,697	78,917	\$43.04
Yerba Buena	4,027,730	0	37.7%	9.0%	46.7%	50.1%	8,479	-56,041	13,568	48,077	\$42.33
San Francisco Totals	103,308,023	368,623	25.1%	5.7%	30.8%	36.2%	-473,735	-239,115	1,618,032	3,251,131	\$48.58
Class A	57,787,888	339,333	25.7%	6.5%	32.2%	39.1%	-938,809	-449,484	850,629	1,719,193	\$54.30
Class B	37,655,794	29,290	26.8%	5.6%	32.4%	36.7%	455,870	233,520	681,315	1,372,301	\$41.20
Class C	7,864,341	0	22.0%	1.9%	23.9%	26.9%	9,204	-23,151	86,088	159,637	\$33.40

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 the California Employment Development Department.

Inflation has exhibited declines in recent months, though it still remains above the Federal Reserve's long-term target. That 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's 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 2Q 2024

Property	Submarket	SF	Sale Price	\$/SF	Buyer	Seller
1455 Market Street (45% Interest Sale)	Mid Market	1,320,000	\$43,500,000	\$32.95	Hudson Pacific Properties	CPP Investments
300 California Street	Financial District	119,000	\$28,500,000	\$239.50	REDCO Development	LeFrak
410 Townsend Street	South of Market	78,000	\$22,000,000	\$282.05	New York Life Real Estate Investors	Nationwide Mutual

SIGNIFICANT LEASE TRANSACTIONS 2Q 2024

Property	Submarket	SF	Transaction Date	Landlord	Tenant
1455 Market Street	MidMarket	157,000	May 2024	Hudson Pacific Partners	City and County of San Francisco
405 Howard Street	South Financial District	153,000	Jun 2024	TIAA	Orrick
400-430 California Street	Financial District	123,320	April 2024	Kennedy Wilson	Rippling

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	3Q 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 across Washington, Oregon, California, Idaho, Nevada, and Arizona. We offer a complete range of brokerage, appraisal, asset services, consulting, and debt & equity finance services for all property types.

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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>55M SF</i> MANAGEMENT PORTFOLIO SIZE	<i>800+</i> ASSETS UNDER MANAGEMENT	<i>260+</i> CLIENTS SERVED
VALUATION ADVISORY	<i>2,600+</i> 3-YEAR AVERAGE ASSIGNMENTS	<i>43</i> TOTAL APPRAISERS	<i>27</i> WITH MAI DESIGNATIONS

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