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1Q24

# San Francisco Office Market Overview



**NEWMARK**

# Market Observations

## Economy

- Leisure and Hospitality as well as the Education and Health sectors had the largest year-over-year increases of any industries. All of the office-using sectors shrank over the last year.
- After surging above pre-pandemic totals for several quarters, total office-using employment is now 1.8% below the pre-pandemic mark and 9.6% below a 2022 high point.
- Technology firms are continuing to adjust labor needs. Locally, the information sector was the office-using sector with the largest negative employment growth over the past 12 months declining by 11.5%.

## Major Transactions

- The largest lease of the quarter was the City of San Francisco 21-year lease at 1455 Market Street. The lease includes multiple renewal options as well as a purchase option. It is expected that the city will eventually purchase the property and consolidate many of its leases around the city into the single building.
- Major renewals occurred during the quarter as KPMG and Pillsbury Winthrop Shaw Pittman renewed their leases at 55 Second Street and 4 Embarcadero Center, respectively.

## Leasing Market Fundamentals

- Net absorption for the first quarter of 2024 was negative 520,467 square feet. While absorption remained negative for the ninth quarter in a row, absorption did not eclipse negative 1 million square feet for the first time since the third quarter of 2022.
- Market-wide asking rents continued to decline – decreasing \$0.29/SF quarter-over-quarter to \$69.99/SF. However, there remains pockets of trophy and view space being leased for rents well over \$100/SF.
- Despite several encouraging large leases being signed during the quarter, total market-wide leasing of just over 1.1 million square feet is a decline of 18% compared to the first quarter of 2023 and is down 50% quarter-over-quarter.

## Outlook

- San Francisco office tenant demand has steadily increased over the past several quarters and was up 21% in the first quarter of 2024 - the largest quarter-over-quarter increase since 2021.
- Per data from Placer.AI, San Francisco office visits in January increased year-over-year by 23% - the largest increase of any major city.
- Distressed properties are continuing to hit the market for sale. Anecdotally, there has been an increase in bid pools, causing prices to be pushed upwards and many to think the bottom of the sales market has already passed.

1. Economy
2. Leasing Market Fundamentals
3. Appendix / Tables



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1Q24

# Economy

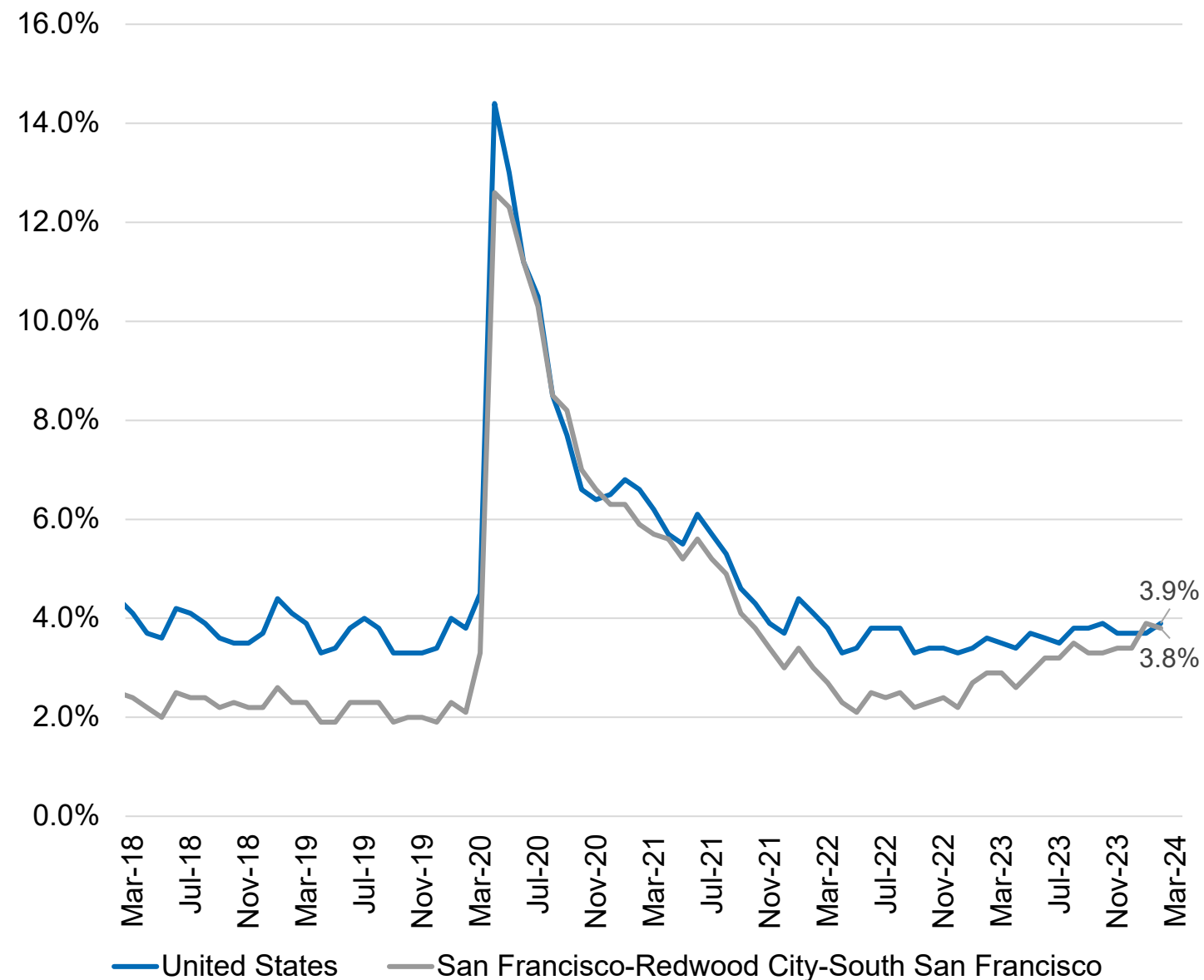




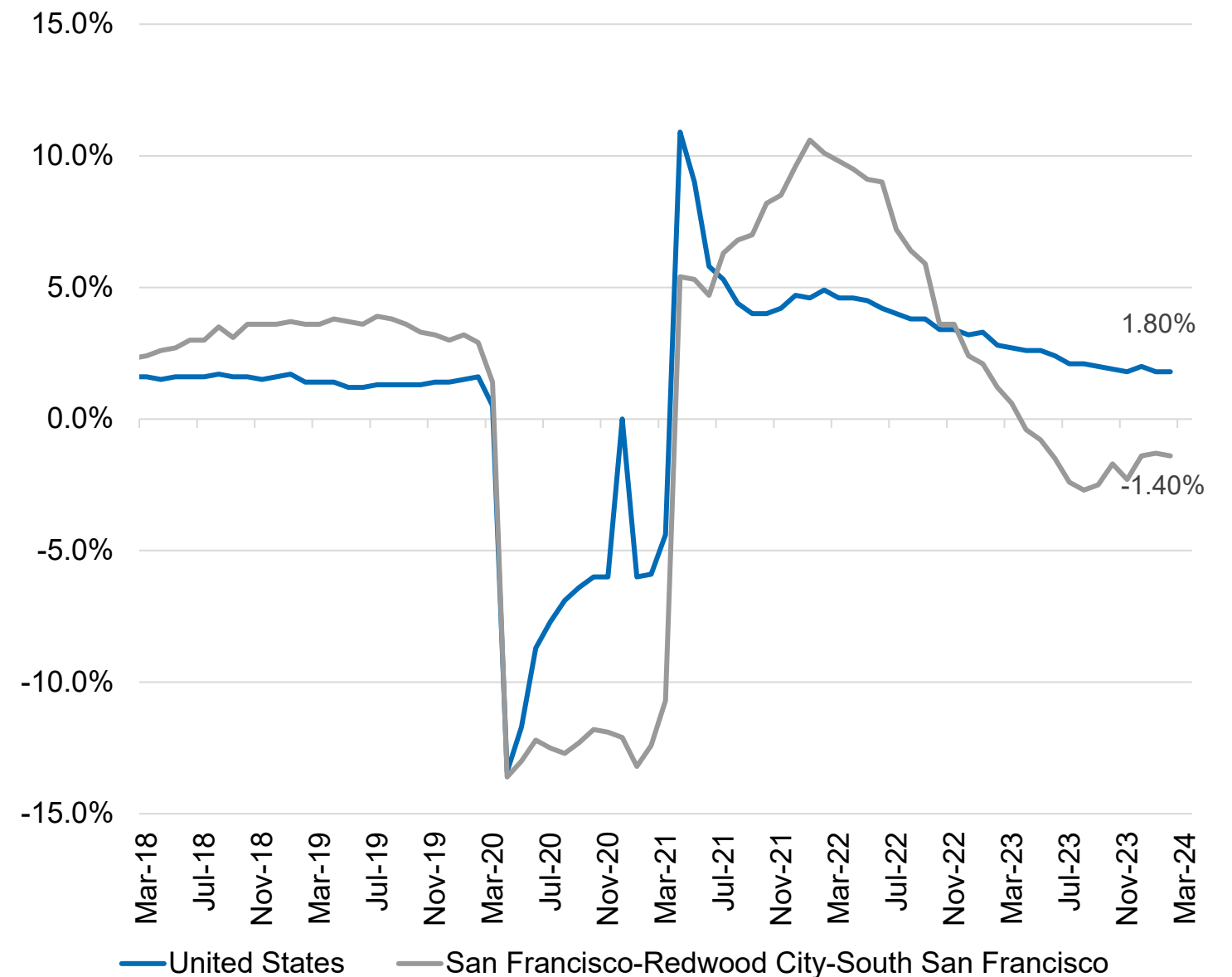
# Metro Employment Trends Signal a Slowing, Tighter Economy

The region's unemployment rate rose closer to the national average in recent months. Furthermore, the nonfarm employment in the region is down 1.4% year over year – a stark difference compared to the 1.8% increase nationally.

Unemployment Rate, Non-Seasonally Adjusted



Nonfarm Payroll Employment, Non-Seasonally Adjusted, 12-Month % Change

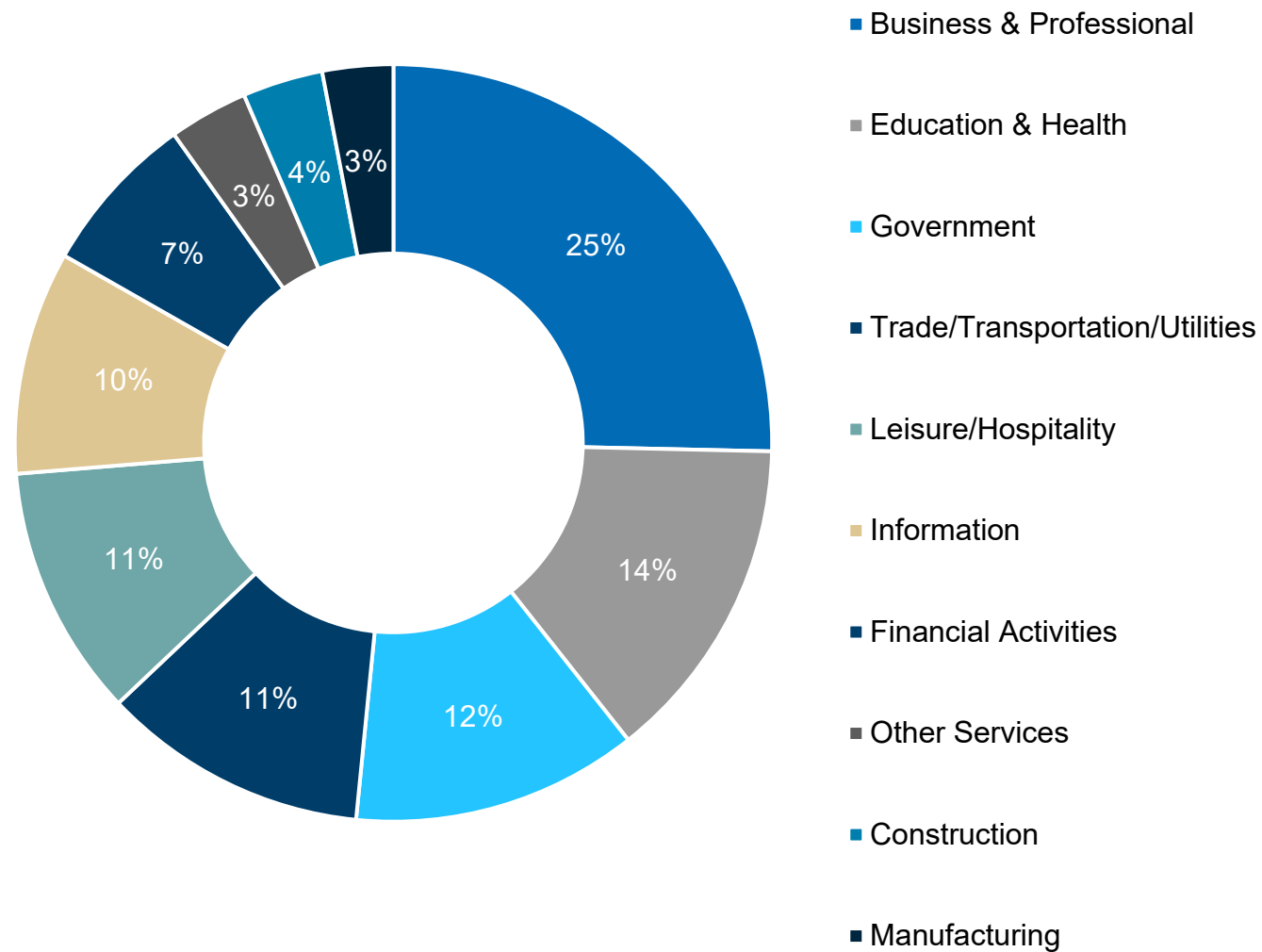


Source: U.S. Bureau of Labor Statistics, San Francisco-Redwood City-South San Francisco

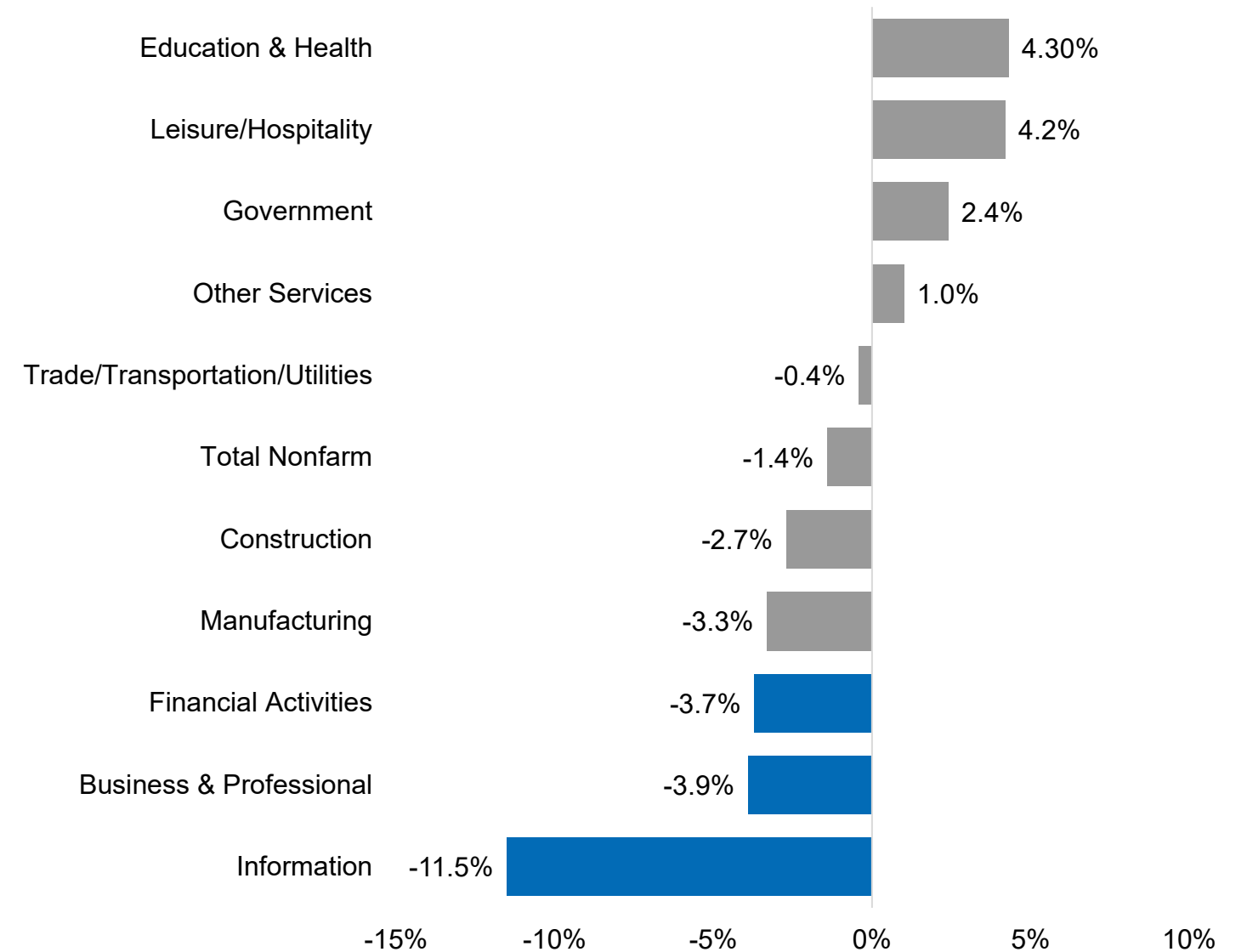
# Employment in Information Industry Down 11.5% Year-Over-Year

Leisure and Hospitality as well as the Education and Health sectors had the largest year-over-year increases of any industries. All of the office-using industries shrank in the last year.

Employment by Industry, February 2024



Employment Growth by Industry, 12-Month % Change, February 2024

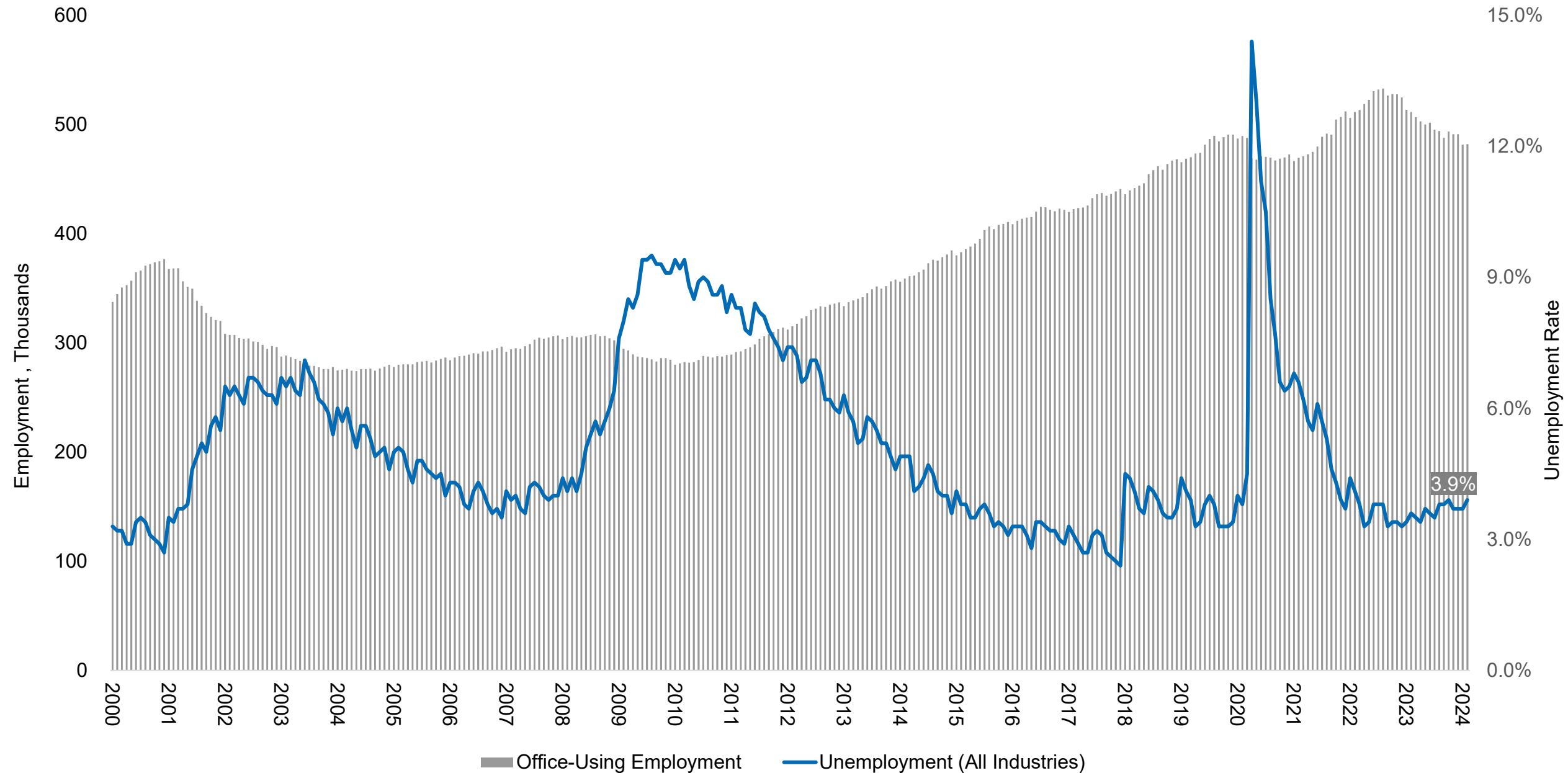


Source: U.S. Bureau of Labor Statistics, San Francisco-Redwood City-South San Francisco

# Overall Office-Using Employment Dips Below Pre-Pandemic Total

After surging above pre-pandemic totals for several quarters, total office using employment is now 1.8% below the pre-pandemic mark and 9.6% below a 2022 highpoint.

## Office-Using Employment\* and Unemployment Across All Industries



Source: U.S. Bureau of Labor Statistics, San Francisco-Redwood City-South San Francisco

Note: November 2023 data is preliminary.

\*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.



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1Q24

# Leasing Market Fundamentals

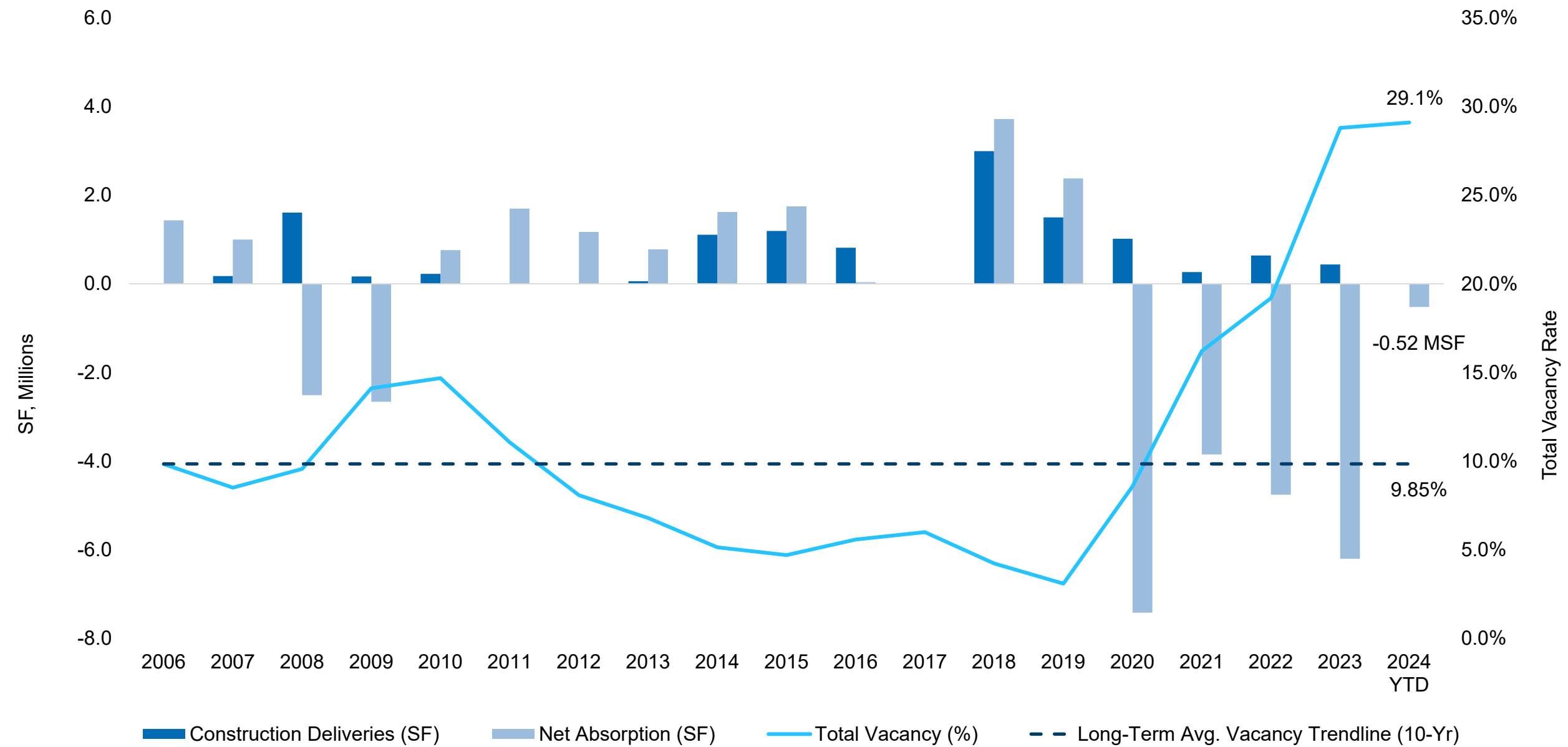




# Vacancy Rises Slightly as Net Absorption Remains Negative

While absorption remained negative for the ninth quarter in a row, absorption did not eclipse negative 1.0 million square feet for the first time since the third quarter of 2022.

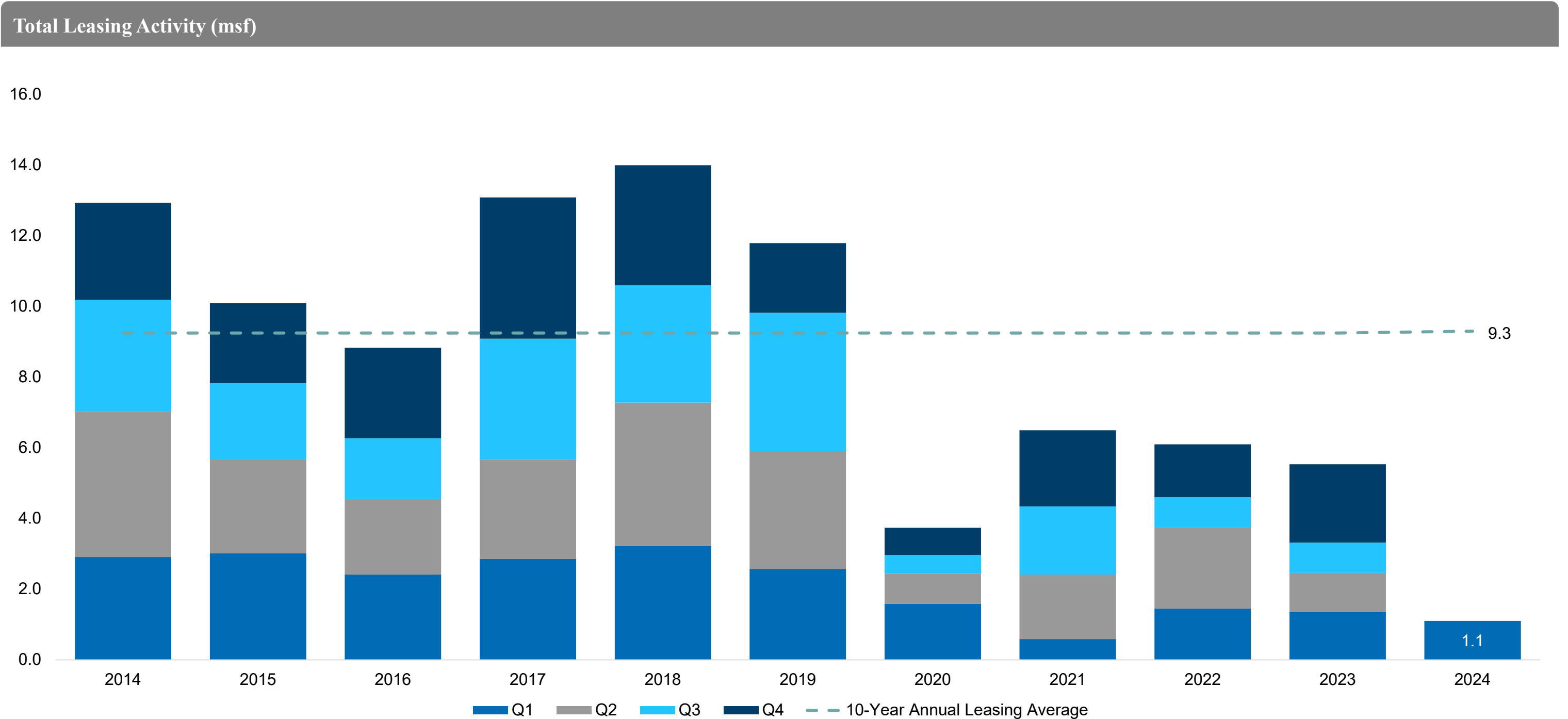
## Historical Construction Deliveries, Net Absorption, and Vacancy



Source: Newmark Research, CoStar

# Leasing Activity Remains Well Below Average

Despite an increase in demand, and seemingly an increase in large block leasing, total leasing in the quarter remained well below the pre-2020 benchmarks.



Source: Newmark Research, CoStar





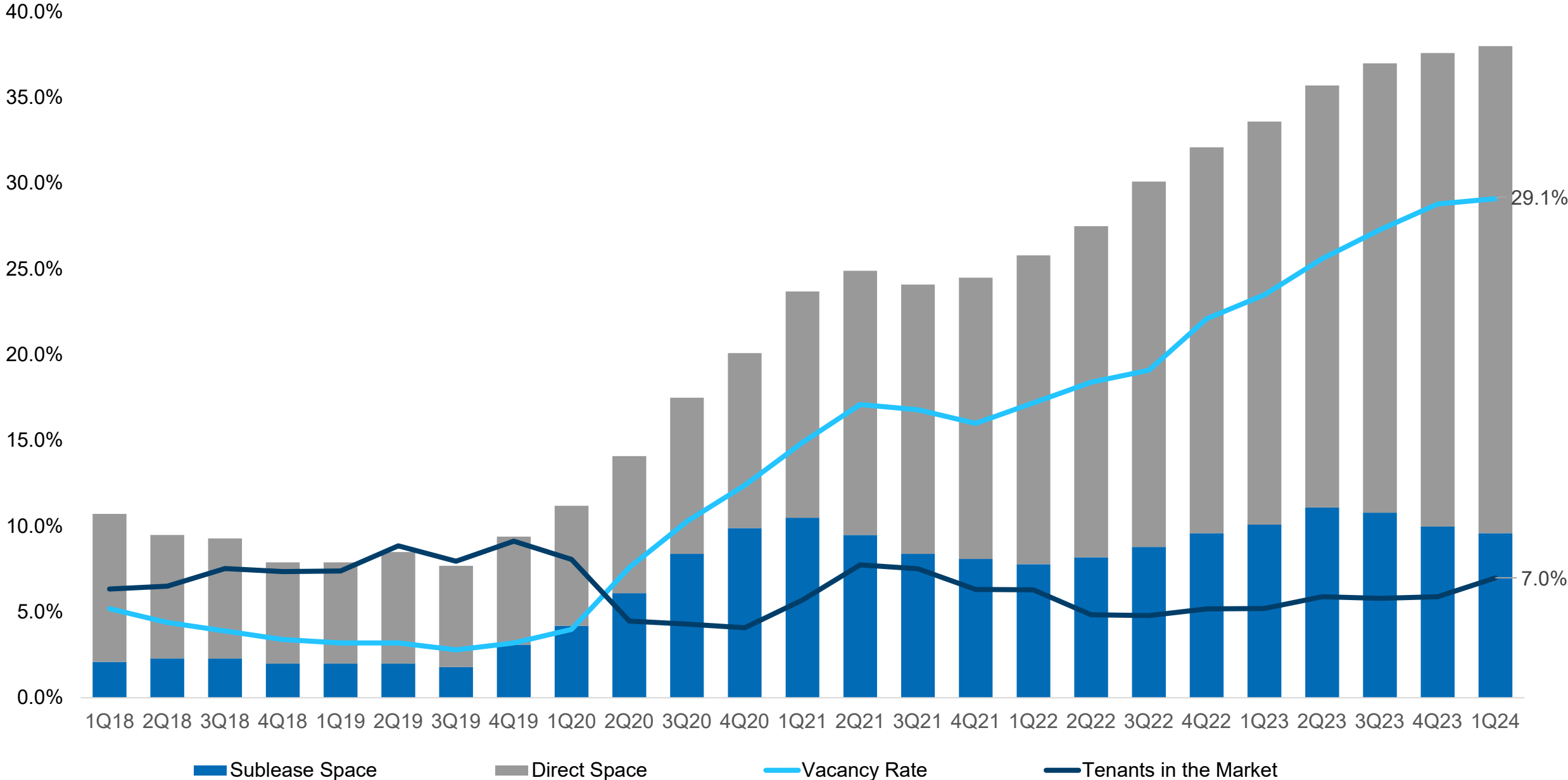
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# Sublease Availability Declines as Tenant Demand Increases

Though direct availability continues to increase, so does tenant demand. Demand increased for the third straight quarter and is up 21% in the first quarter of 2024. Available sublease space has steadily decreased, down 11%, since the second quarter of 2023 as large blocks get leased and other subleases expire and go direct.

Available Space and Tenant Demand as Percent of Overall Market



Source: Newmark Research, CoStar





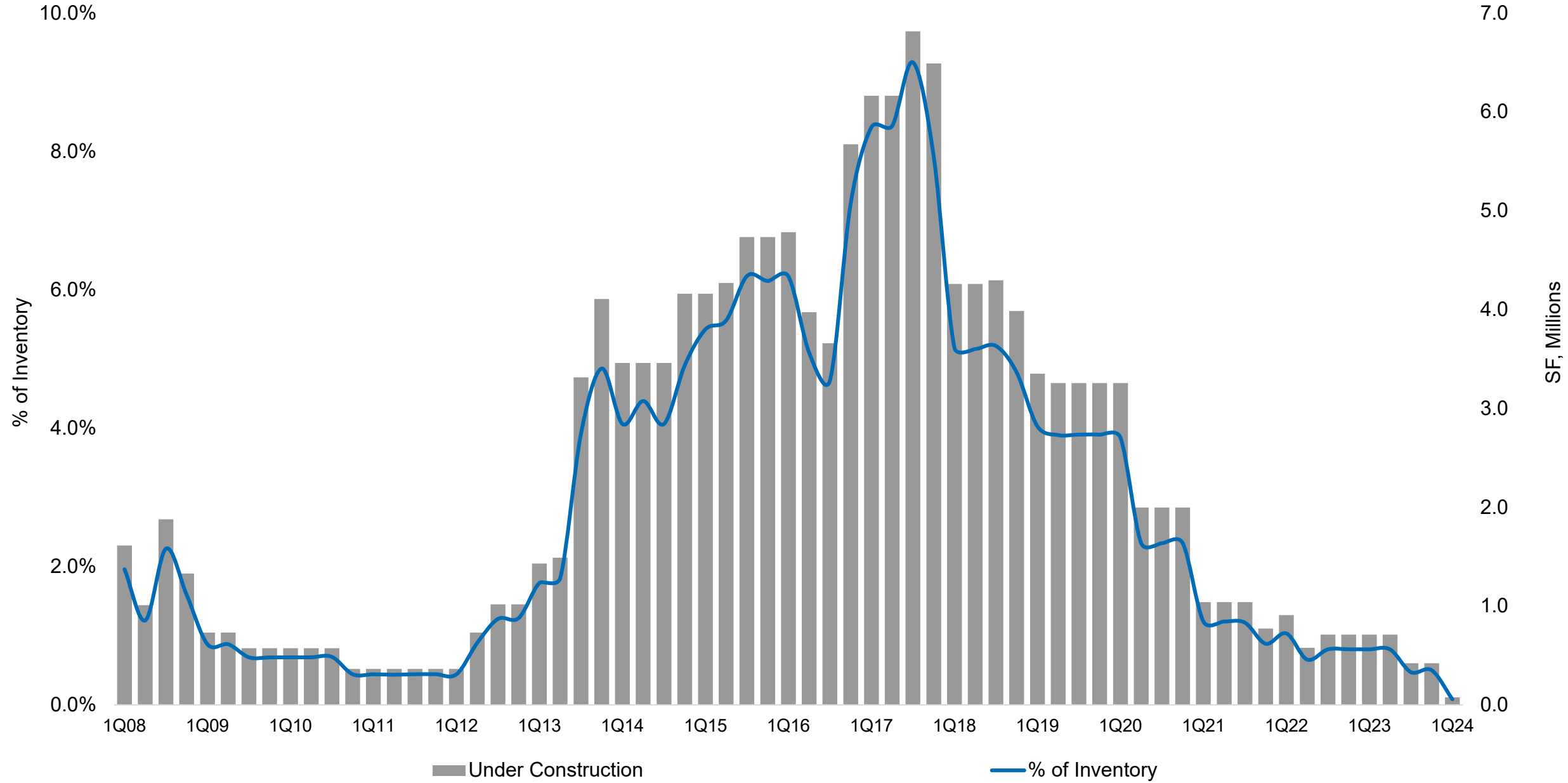
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# Square Feet Under Construction Reaches Lowest Level In Recent History

Rising construction costs and an uncertain economic outlook has halted new office construction for several quarters. Presently, there's only roughly 85,000 square feet of office space under construction across two properties – 531 Bryant Street and 828 Brannan Street.

## Office Under Construction and % of Inventory



Source: Newmark Research, CoStar, City and County of San Francisco





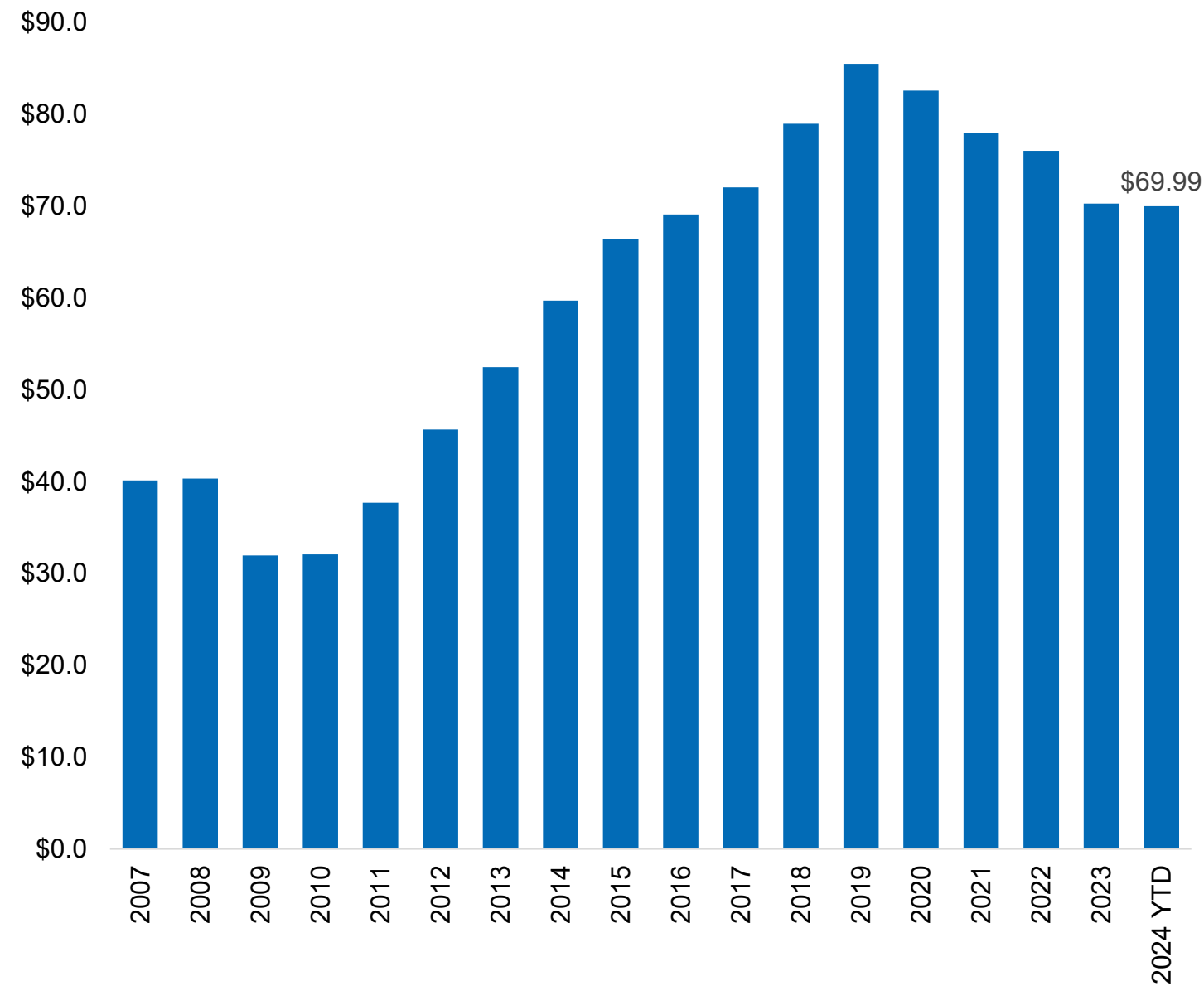
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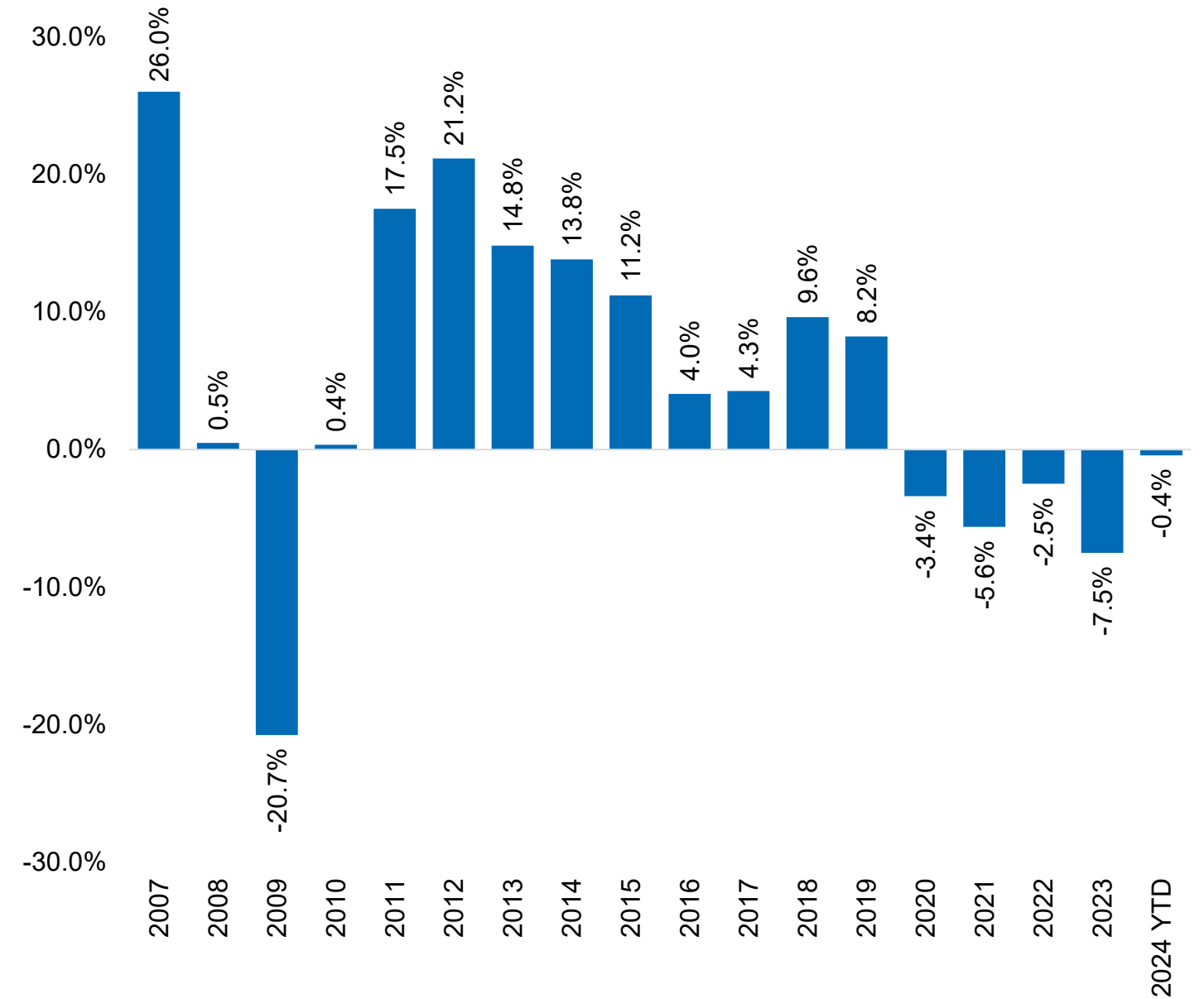
# Overall Market Rents Continue at Lowest Level Since 2016

Rents have steadily declined since the start of 2020. Most recently, overall asking rates declined to \$69.99/SF. Asking rates are expected to keep declining as assets are beginning to trade hands and reprice. However, there remains pockets of trophy and view space being leased for rents well over \$100/SF.

Office Average Asking Rent, \$/SF, FS



Year-over-Year Asking Rent Growth Rate

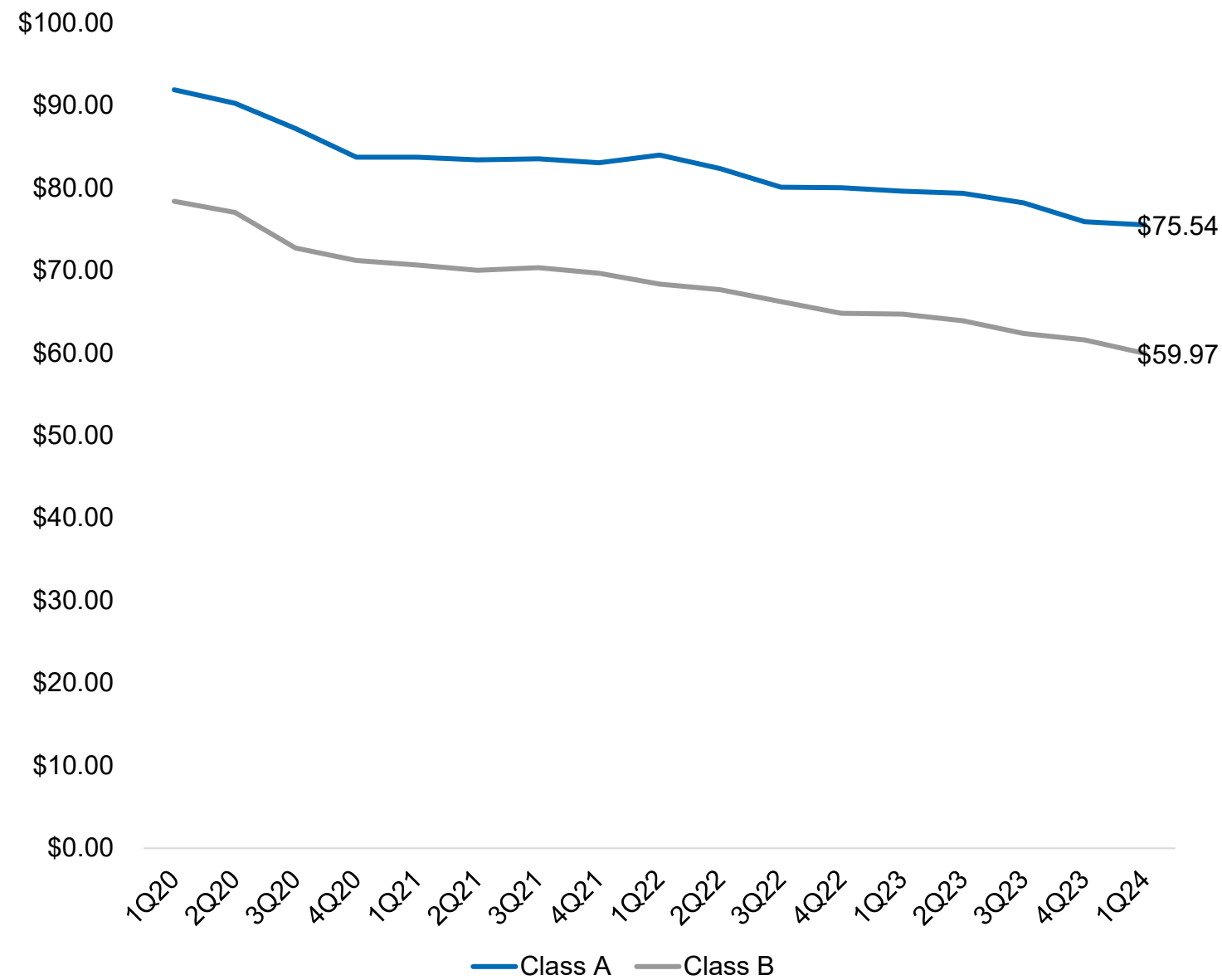


Source: Newmark Research, CoStar

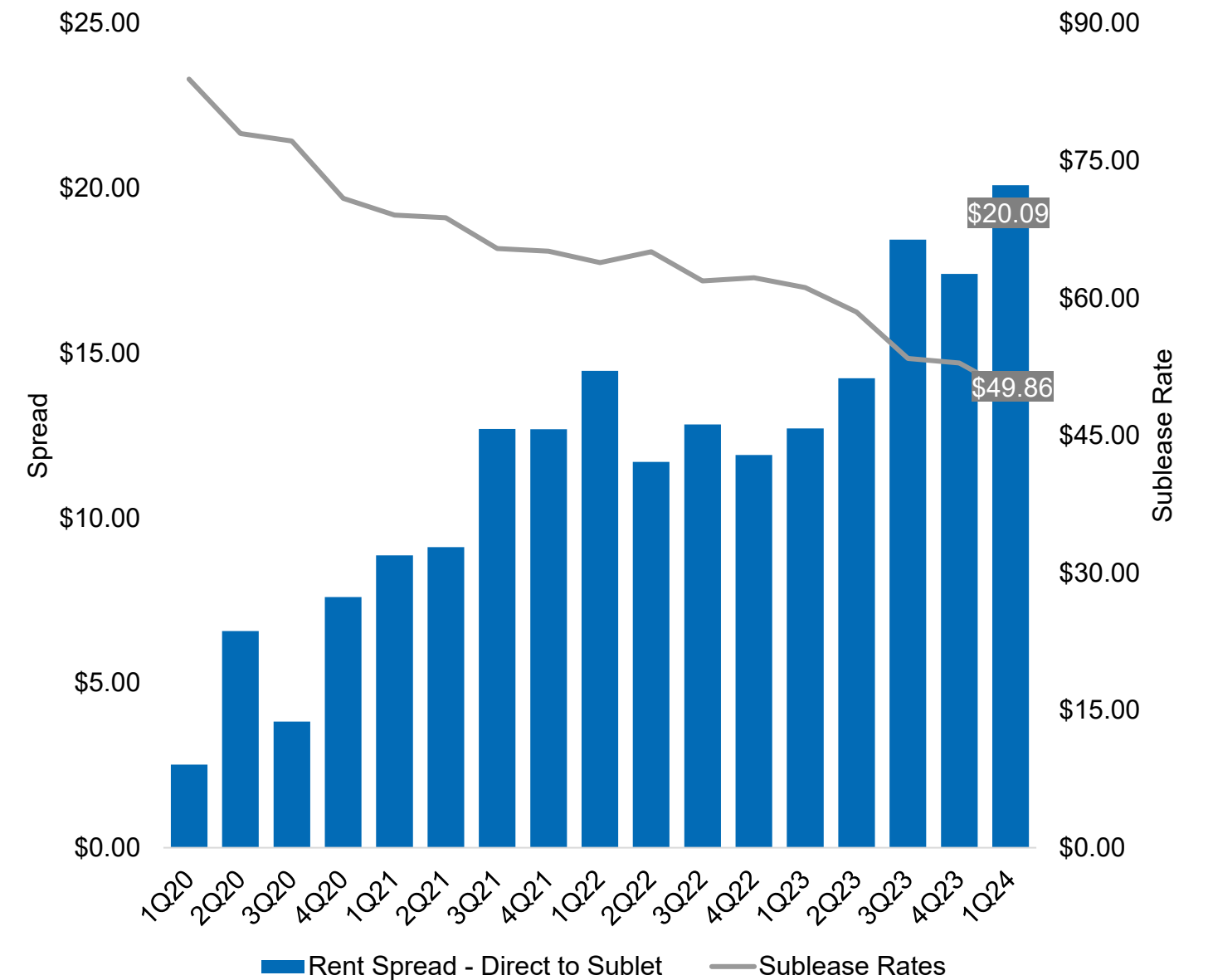
# Asking Rent Spread Between Direct and Sublease Reaches New High

Since the start of 2020, Class A asking rates have declined by 18%, while Class B rates have declined by just over 24%. Similarly, sublease asking rates declined by just over 40% since the start of 2020. As a result, the spread between sublease space and direct space has widened since the beginning of 2020 by roughly 697% from under \$3/SF to over \$20/SF.

Class A and Class B Asking Rents



Sublease Rates



Source: Newmark Research, CoStar



# Leasing Activity

Following the trend in tenant demand, four of the five largest leases signed during the quarter were from traditional office-users.

## Notable 1Q24 Lease Transactions

| Tenant  | Building(s)          | Submarket                  | Type          | Square Feet |
|---|----------------------|----------------------------|---------------|-------------|
| City of San Francisco   | 1455 Market Street   | SOMA – Midmarket           | Direct        | 157,000     |
| <i>21-year lease with multiple renewal options and a purchase option.</i> |                      |                            |               |             |
| Adyen   | 505 Brannan Street   | SOMA – Central Yerba Buena | Sublease      | 148,146     |
| <i>Subleased the entire building from Pinterest.</i>                      |                      |                            |               |             |
| KPMG  | 55 Second Street     | South Financial District   | Lease Renewal | 142,785     |
| <i>Renewed on floors 6-12 as well as 14.</i>                              |                      |                            |               |             |
| Pillsbury Winthrop Shaw Pittman   | 4 Embarcadero Center | North Financial District   | Lease Renewal | 76,132      |
| <i>Renewed on floors 8-10 and 22-23.</i>                                  |                      |                            |               |             |
| Goodwin Procter   | 525 Market Street    | South Financial District   | Direct        | 58,992      |
| <i>Leased floors 30 and 31.</i>   |                      |                            |               |             |

Source: Newmark Research, CoStar



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1Q24

# Appendix







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