

3Q23

Silicon Valley Industrial Market Overview



NEWMARK

Market Observations

Economy

- The region’s labor market has begun to show cracks, with unemployment in the San Jose-Santa Clara-Sunnyvale MSA rising to 3.9% in August compared with 3.8% nationally. However, this level is still lower than the 4.3% 10-year historical average.
- Year over year, job gains have been most pronounced in the leisure/hospitality industry, which is still making up for lost ground during the pandemic. Leisure/hospitality led all sectors in job gains during the past 12 months and has done so in the past two quarters.
- After seeing a surge of employment in 2022, job growth in industrial sectors has fallen off slightly, with two months of negative job growth in the manufacturing sector and one month of negative job growth in the trade/transportation/utilities sector.

Major Transactions

- The largest deal this quarter was a renewal at 41707 Christy Street in Fremont from RK Logistics, who also preleased a 220,000 SF building in the first quarter of 2023.
- Several large vacancies were leased this quarter such as ±124,230 SF at 550 E Brokaw Road, the former Fry’s Electronics space, to Super Micro Computer, as well as one of the buildings in the newly-constructed Butterfield 5 Business Park in Morgan Hill, where Pinnacle Exhibits leased ±85,456 SF.
- Newark saw a large rise in vacancy this quarter, with Meta putting ±225,000 SF of warehouse space onto the market at 7380 Morton Avenue and ±155,000 SF of industrial space hitting the market at 38083 Cherry Street.

Leasing Market Fundamentals

- Net absorption in the third quarter of 2023 totaled negative 17,732 SF in the industrial sector and negative 183,851 SF in the warehouse sector, for a total of 201,583 SF of occupancy losses. As a result, the industrial vacancy rate held firm at 4.2% and the warehouse vacancy rate increased from 3.5% to 3.9% quarter over quarter.
- Asking lease rates in the industrial sector increased from \$1.54 to \$1.58, while warehouse asking rents fell from \$1.27 to \$1.16 quarter over quarter. Given the current low level of availability, rent fluctuations like this can be common and do not represent a contraction of the market.
- Of the 2.0 million SF of new industrial product under construction, 10% of it is preleased and 422,000 SF is set to complete this year, representing a significant amount of new supply that could drive up vacancy rates again.

Outlook

- Despite slowing activity in the office and R&D sectors, the industrial sector continues to grow due to persistent demand from logistics and manufacturing users.
- Projects like the Butterfield 5 and the Cochrane Technology Park currently under construction in Morgan Hill will continue to push the boundaries of what’s considered “Silicon Valley” from an industrial standpoint.
- Despite a large amount of unleased space in the current construction pipeline, vacancy is expected to remain at about the same levels, due to demand from life science companies and manufacturing companies.

1. Economy
2. Leasing Market Fundamentals

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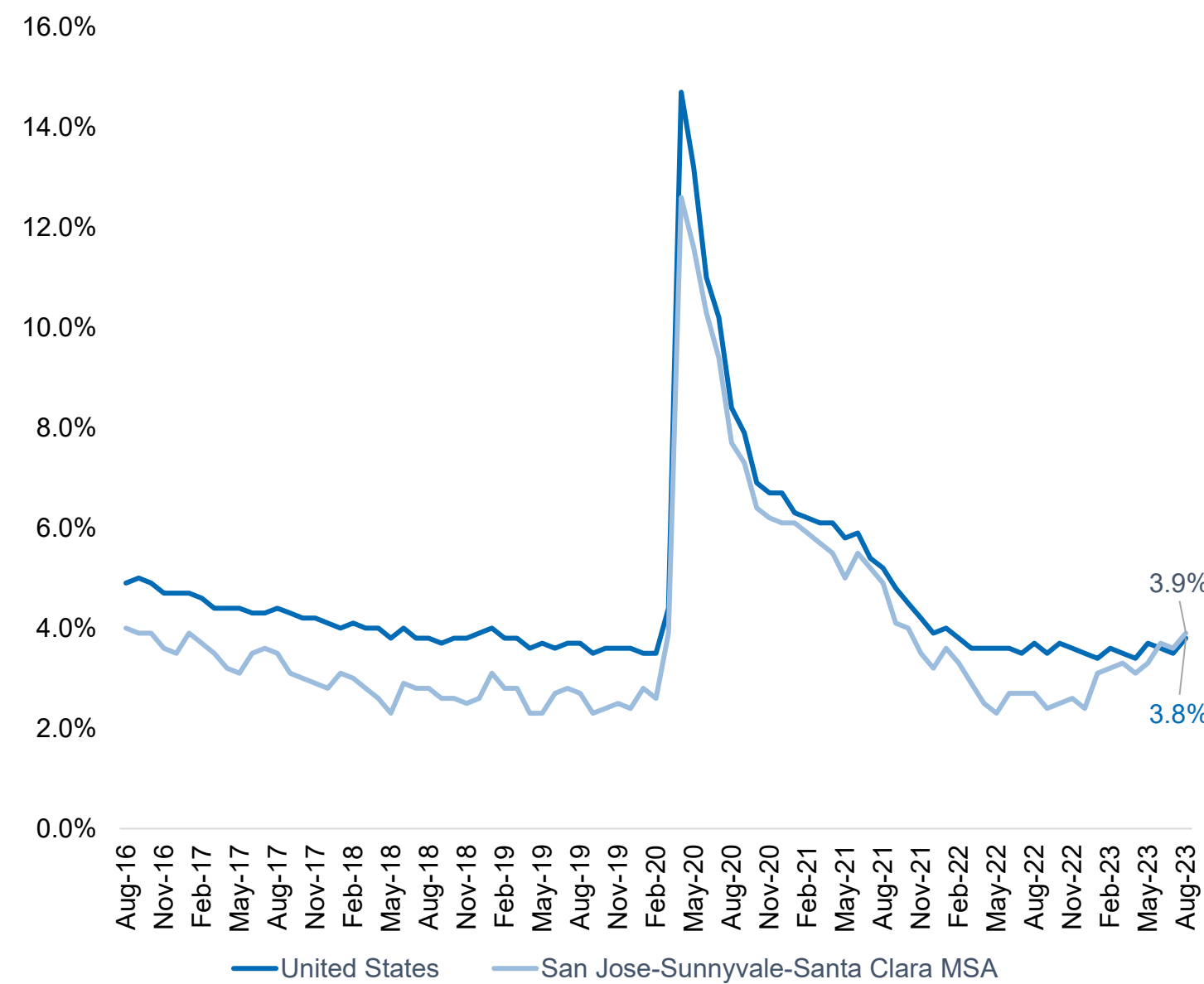
Economy



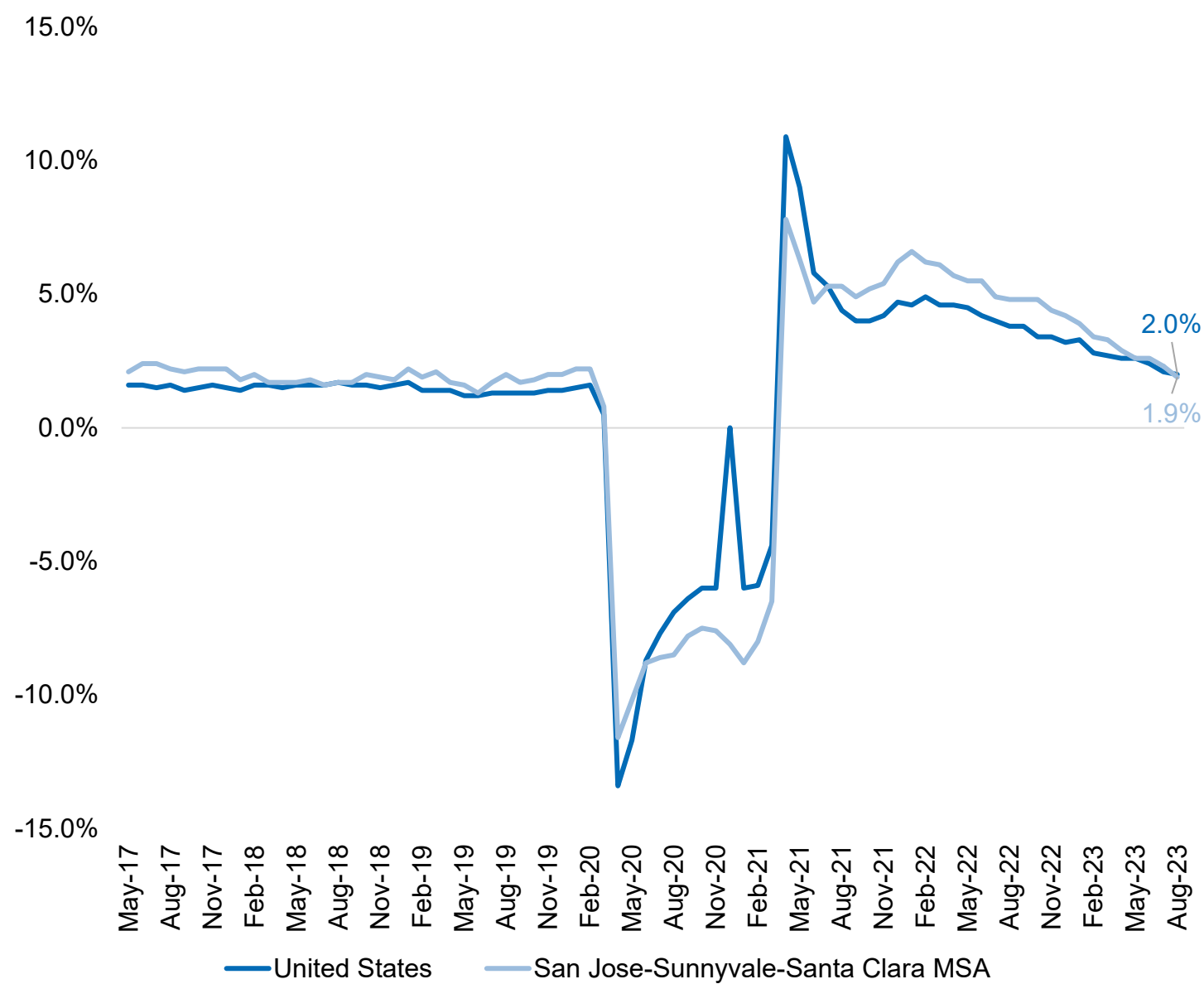
Metro Employment Trends Indicate a Slower Recovery Compared Nationally

The San Jose-Sunnyvale-Santa Clara MSA’s overall unemployment rate rose for the second time in two quarters and is trending above the national average, indicating a slower recovery compared with the rest of the country as the impact of tech sector labor reductions has yet to be fully realized.

Unemployment Rate, Seasonally Adjusted



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

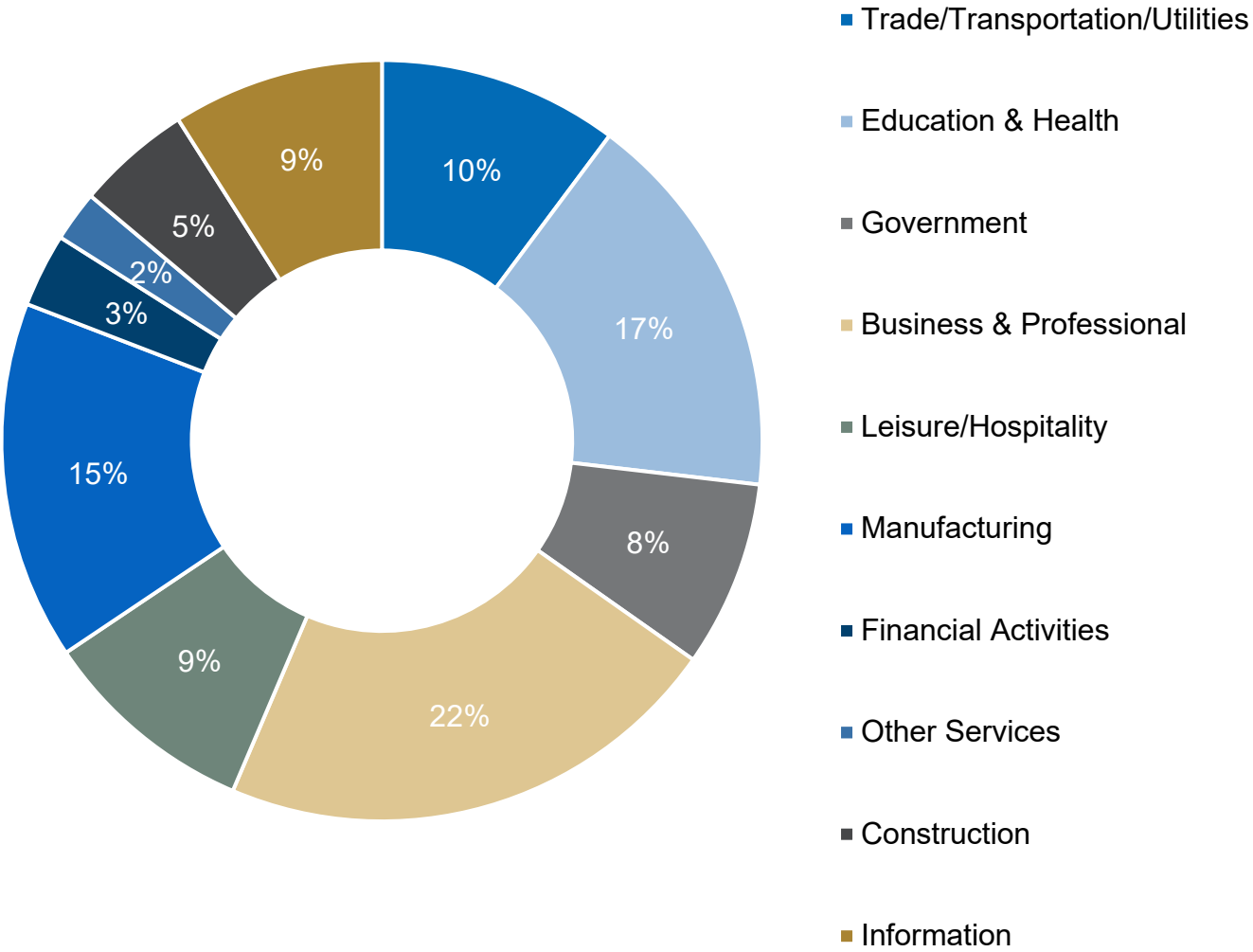


Source: U.S. Bureau of Labor Statistics, San Jose-Sunnyvale-Santa Clara MSA

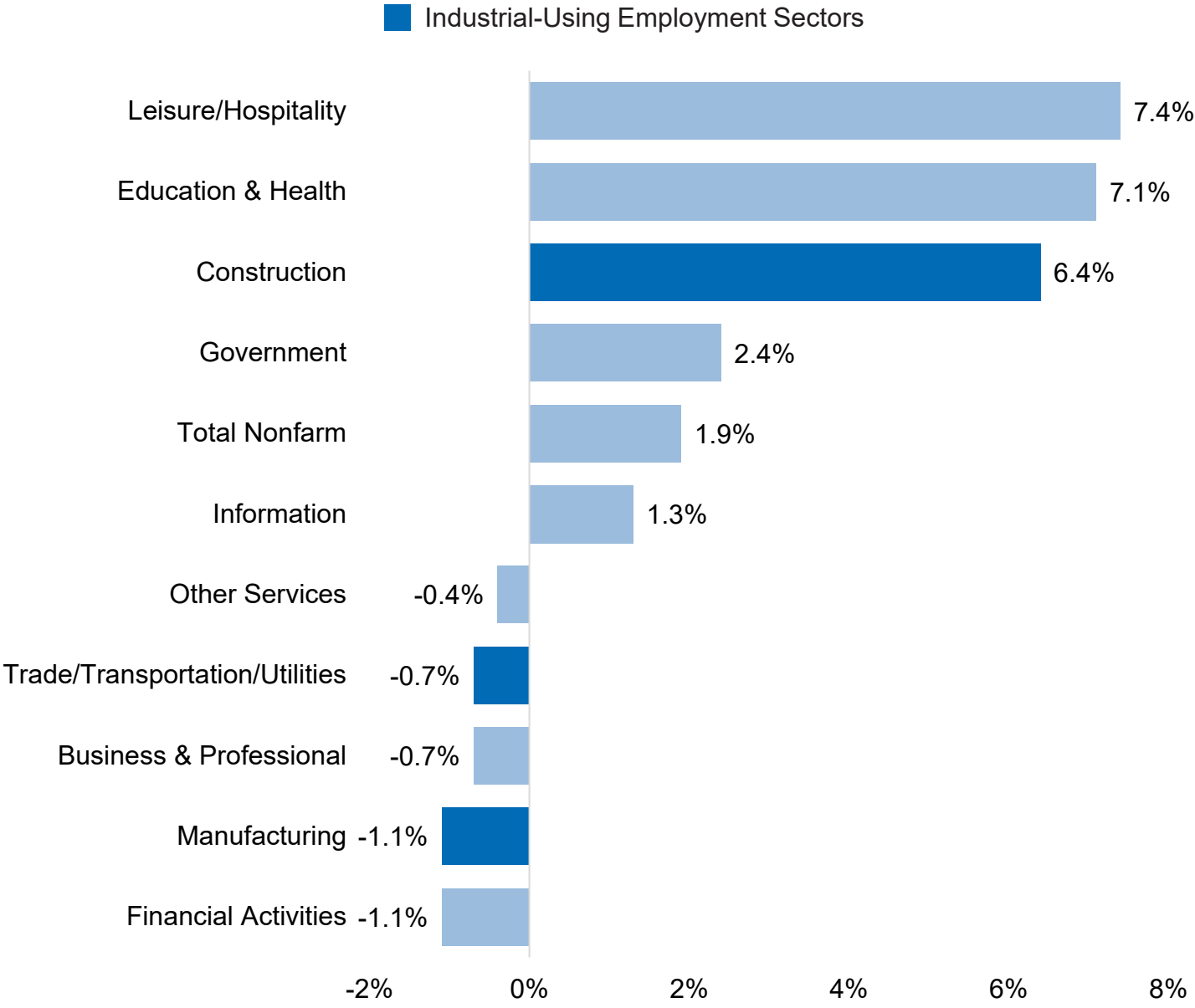
Job Growth Driven in Large Part by Services Still Making Up for Pandemic Losses

In step with a rising overall unemployment rate, several industries this quarter saw negative year over year growth, with the manufacturing and financial sectors hit the hardest. The leisure/hospitality sector continued to lead all industries in annual job growth, as expected of an industry hit hardest by the pandemic. Although the construction sector jobs also saw significant growth, this is likely not due to commercial real estate projects, many of which were put on hold in 2023.

Employment by Industry, August 2023



Employment Growth by Industry, 12-Month % Change, August 2023

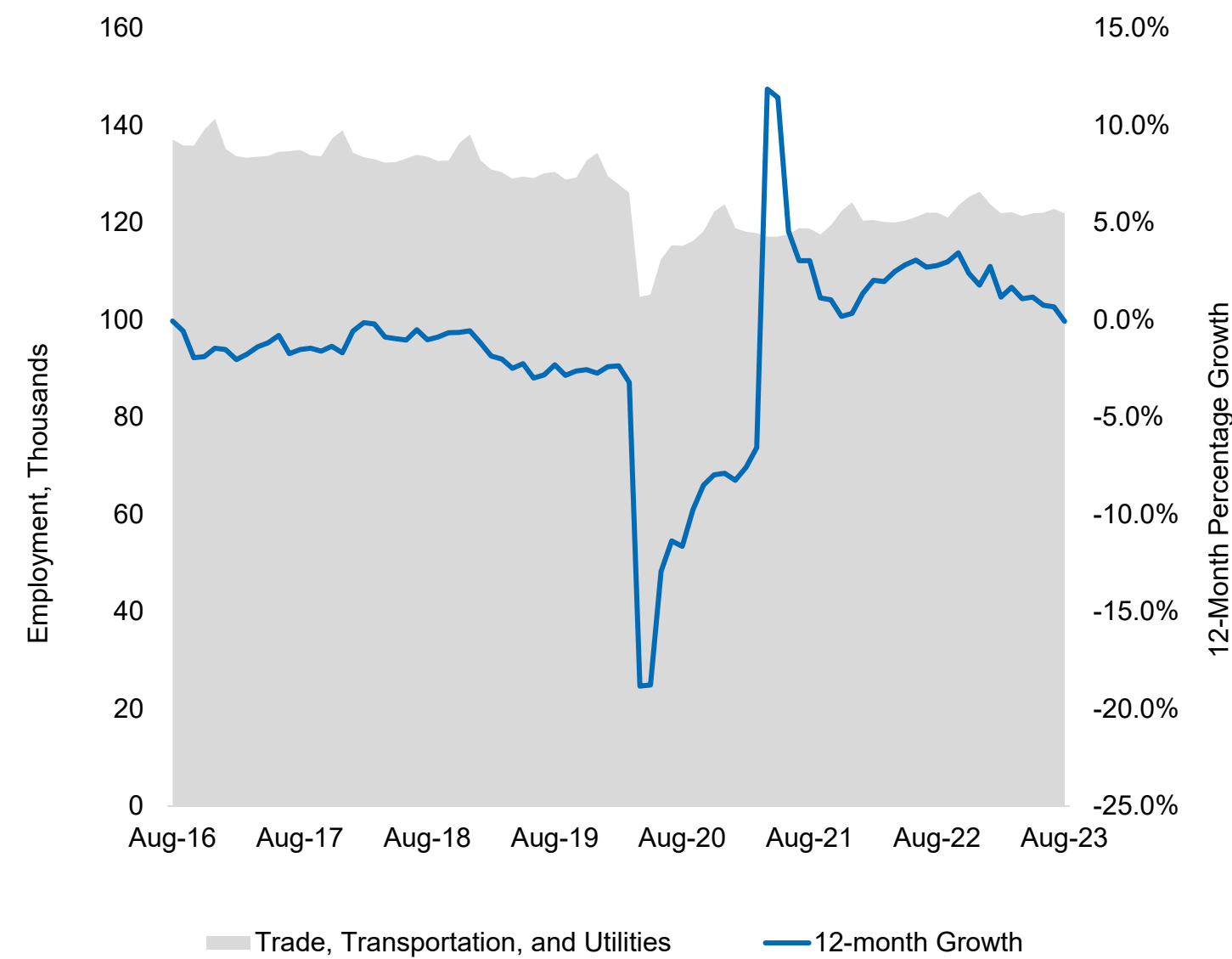


Source: U.S. Bureau of Labor Statistics, San Jose-Santa Clara-Sunnyvale
Note: August 2023 data is preliminary.

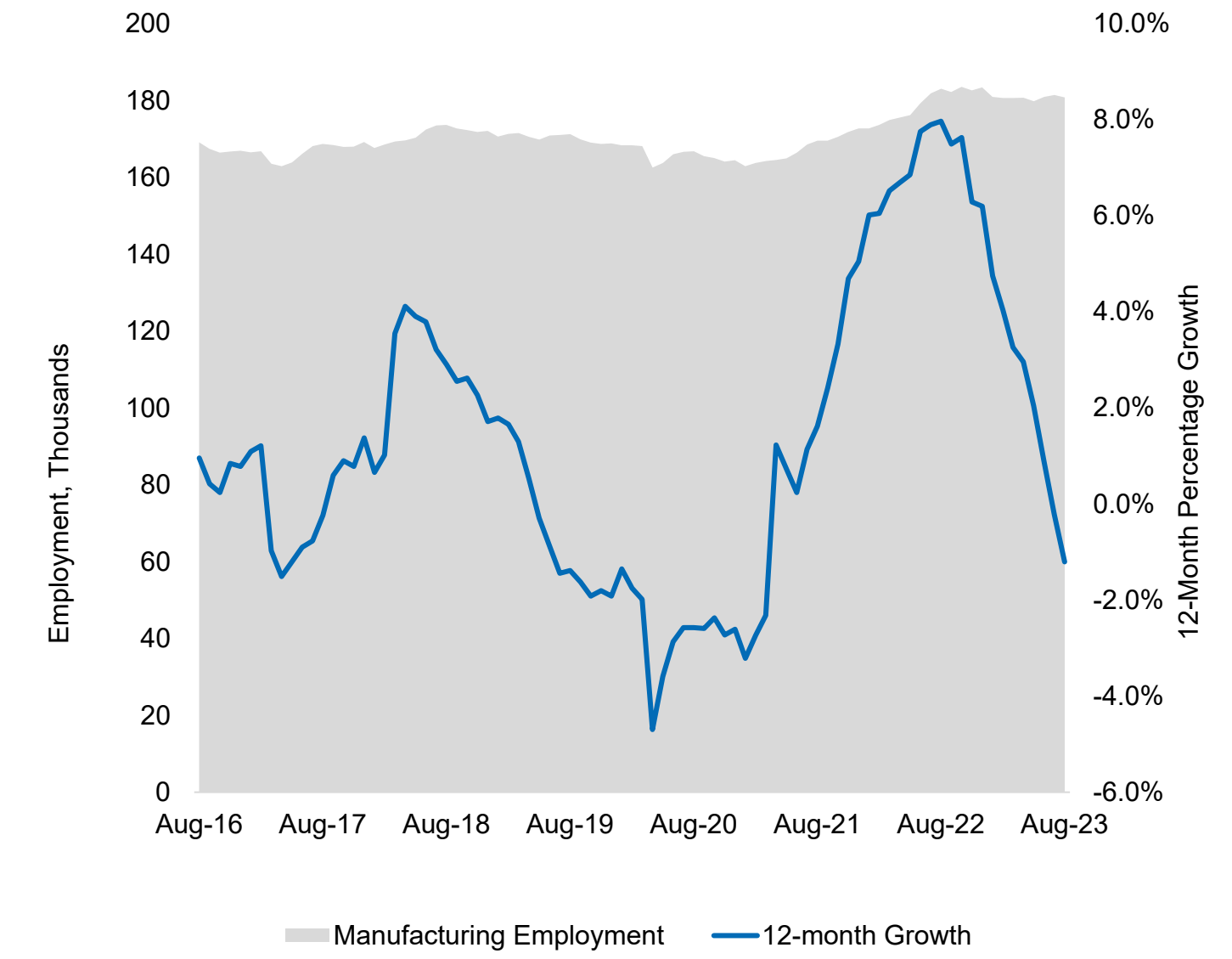
Industrial Employment Strong but Not Immune to Softening Conditions

After a strong rebound in 2022 and early 2023, the manufacturing sector has seen a slight correction in the past two months, posting two months of negative growth compared to the same time last year. Overall employment in both sectors remains high, however, and given the persistent demand from the tech industry for both sectors, its likely very little ground will be lost in the upcoming months.

Total Employment and 12-Month Growth Rate, Trade/Transportation/Utilities



Total Employment and 12-Month Growth Rate, Manufacturing



Source: U.S. Bureau of Labor Statistics, San Jose-Sunnyvale-Santa Clara MSA

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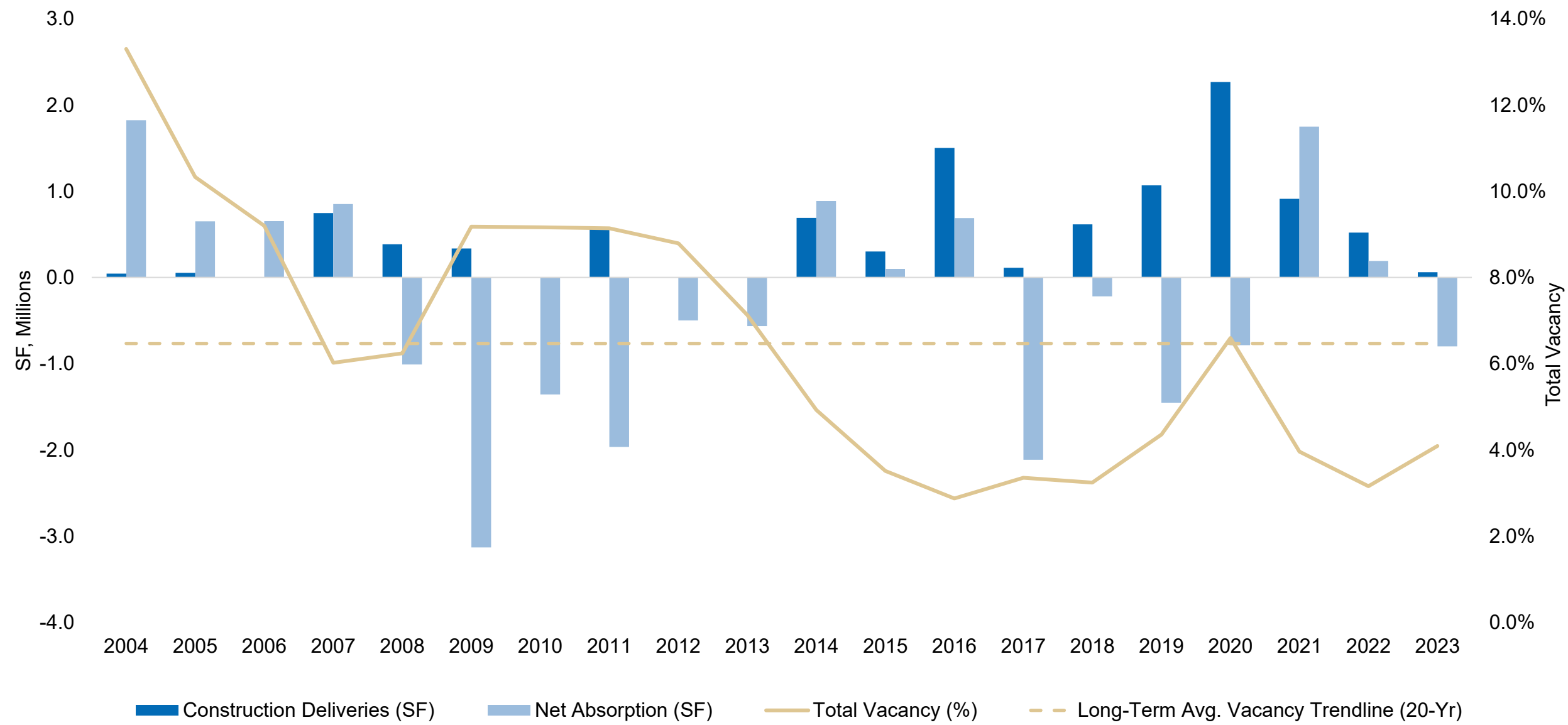
Leasing Market Fundamentals



Vacancy Remains Below Historical Average

The vacancy rate increased slightly in the third quarter to 4.1%, a 20-basis point increase from 3.9% in the previous quarter. Compared to the office and R&D sectors, demand for the industrial product has remained in step with supply and vacancy has remained low at a low level even throughout the pandemic. Although some companies have begun to shed space, those spaces have historically been leased up again fairly quickly.

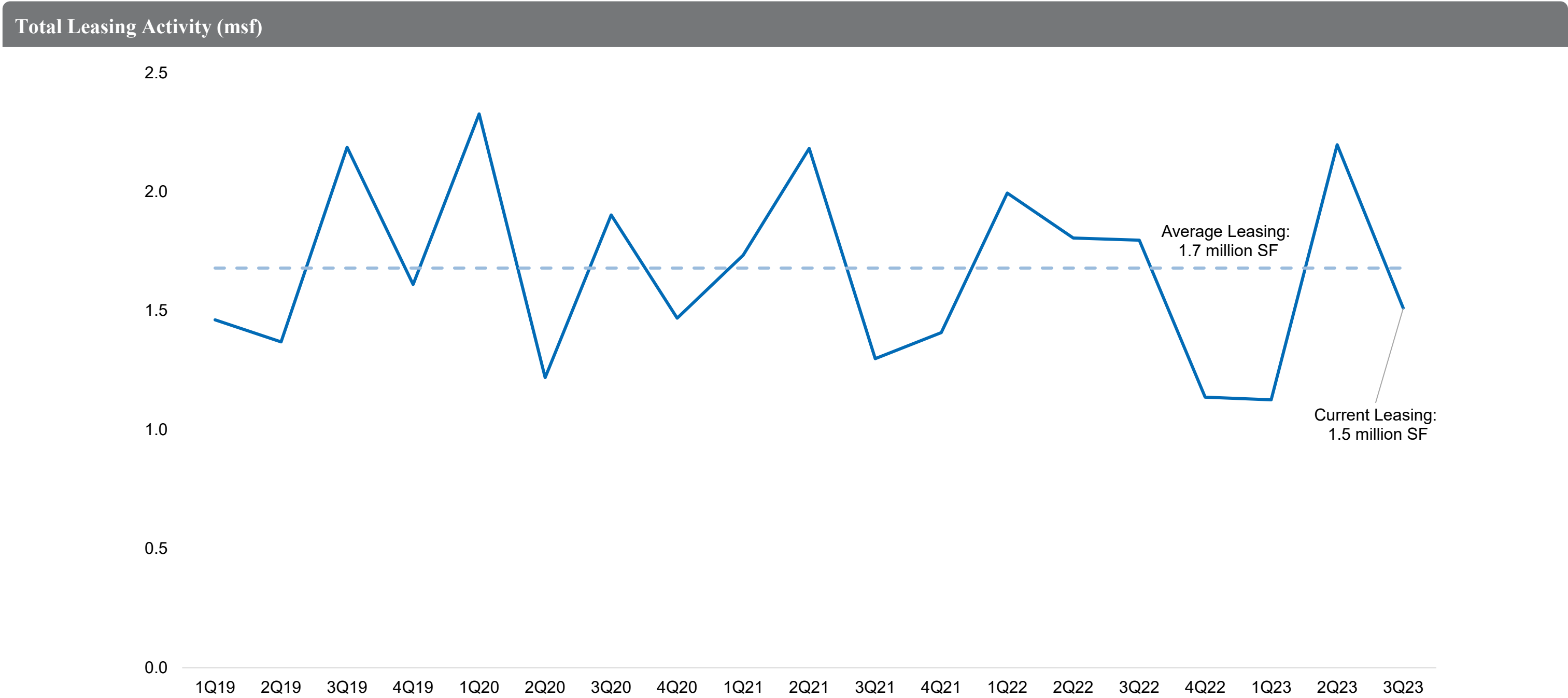
Historical Construction Deliveries, Net Absorption, and Vacancy



Source: Newmark Research

Industrial Leasing Remains Stable in Post-Pandemic Era

Industrial leasing has remained at roughly the same level throughout all of 2023, with a slight dip this quarter below the average leasing volume of 1.7 million SF. Leasing volume has hovered around this average point for the past few quarters due to persistent demand from both manufacturing and tech users for industrial space.

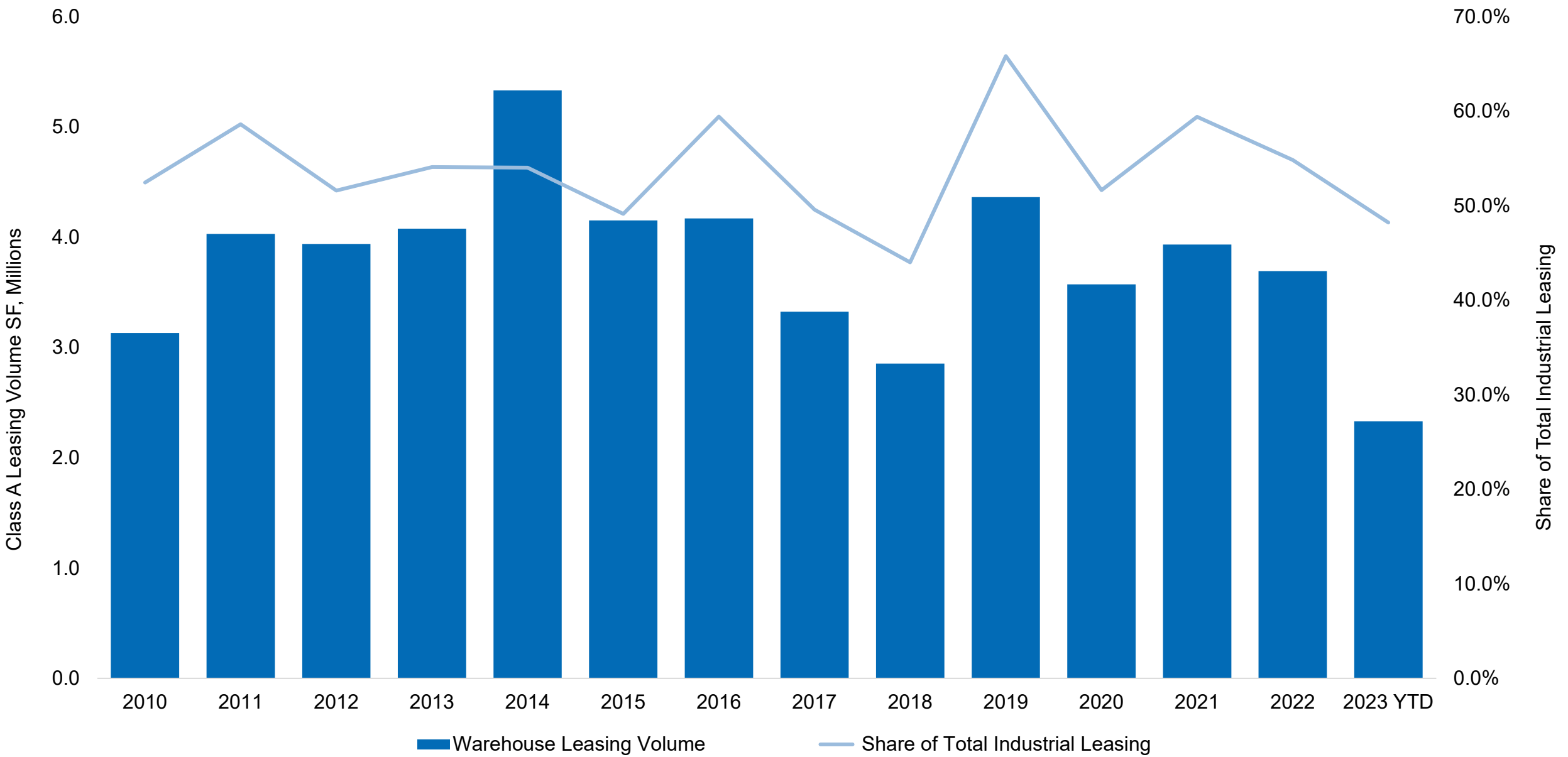


Source: Newmark Research, CoStar

Warehouse Leasing a Significant Portion of Industrial Leasing

Warehouse leasing has always comprised a significant portion of industrial leasing, dropping off slightly in past years and the current one following a surge of activity during the pandemic. Although warehouse commercial activity has historically centered in Fremont and San Jose, as land becomes scarcer, tenants and developers alike have sought secondary markets to build and base their operations.

Warehouse Leasing Volume and Percentage of Total Industrial Leasing Volume

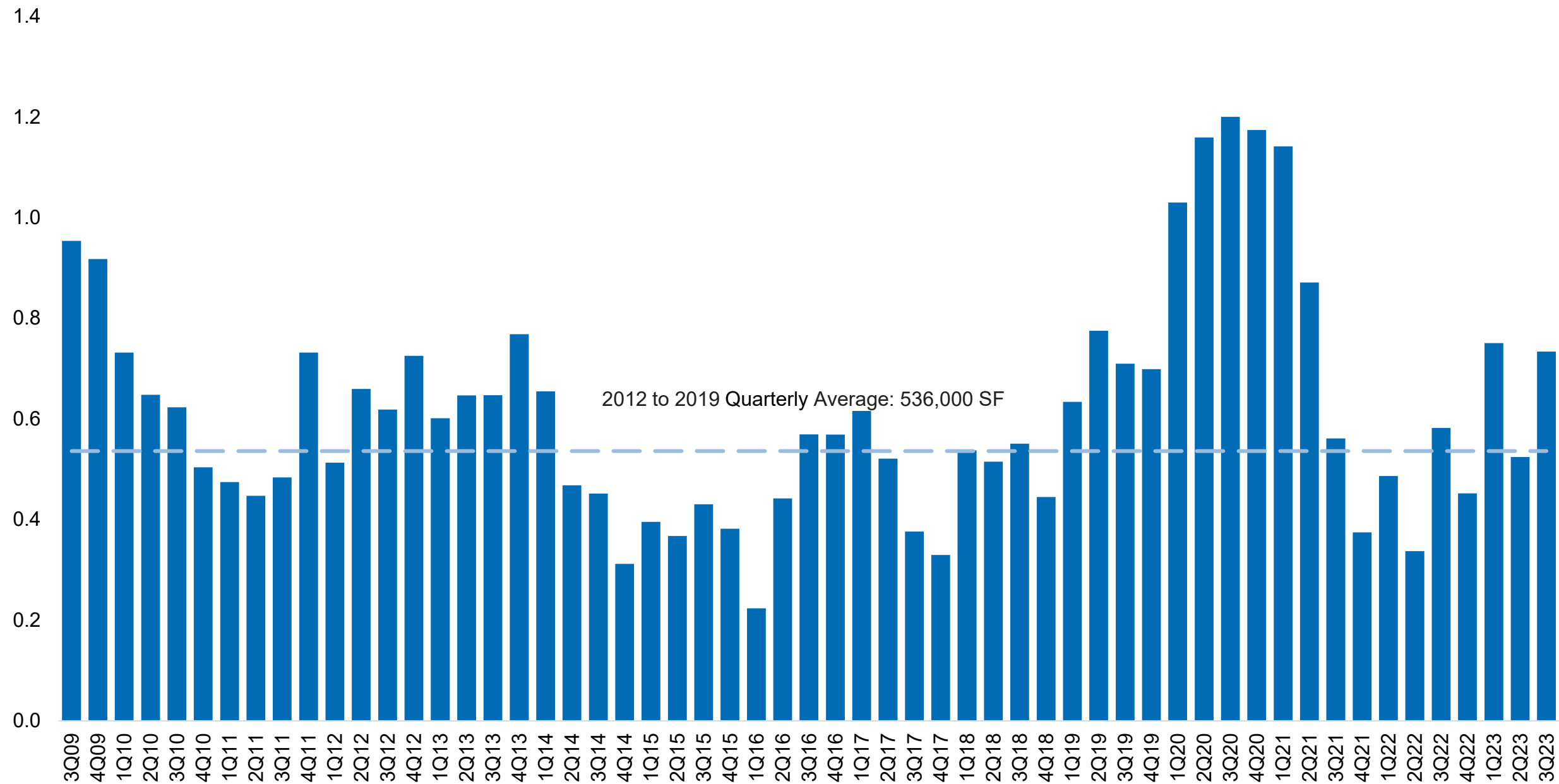


Source: Newmark Research, CoStar

Industrial Sublease Falls to Pre-Pandemic Levels

Sublease space in the third quarter of 2023 rose above pre-pandemic levels, primarily due to Meta putting their ±226,000 SF warehouse in Newark on the market this quarter. Although the sublease market in the Valley was never very large due to consistent low levels of vacancy, the rate of new subleases added to the market has slowed due to many tenants opting to stay in place rather than pay potentially higher costs to relocate.

Available Industrial Sublease Volume (msf)

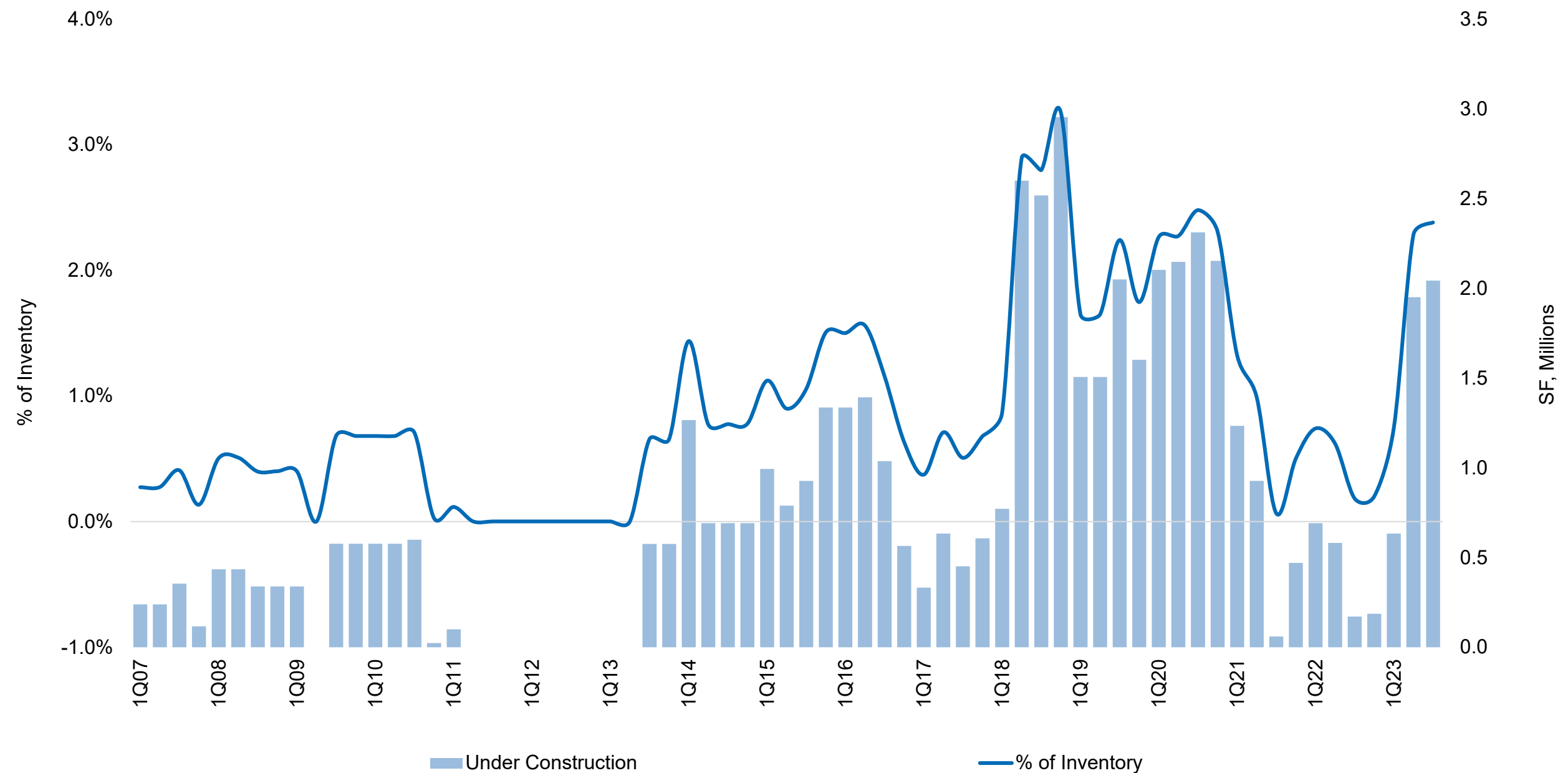


Source: Newmark Research, CoStar

Industrial Supply Pipeline Increases as Construction Starts Dwindle

Although no new projects broke ground this quarter, the level of construction currently underway indicates that developers anticipate a growing need for advanced manufacturing and 3PL space. The two projects slated to complete this year, 47020 Kato Road in Fremont and 650 N King Rd are should add ±400,000 SF of new shell, though the Kato project was leased earlier this year. The current pipeline is set to expand the industrial market by 2.4% by the end of 2025.

Industrial Under Construction and % of Inventory



Source: Newmark Research, CoStar

Total Construction Is Concentrated in the 200,000 – 350,000 sf Segment

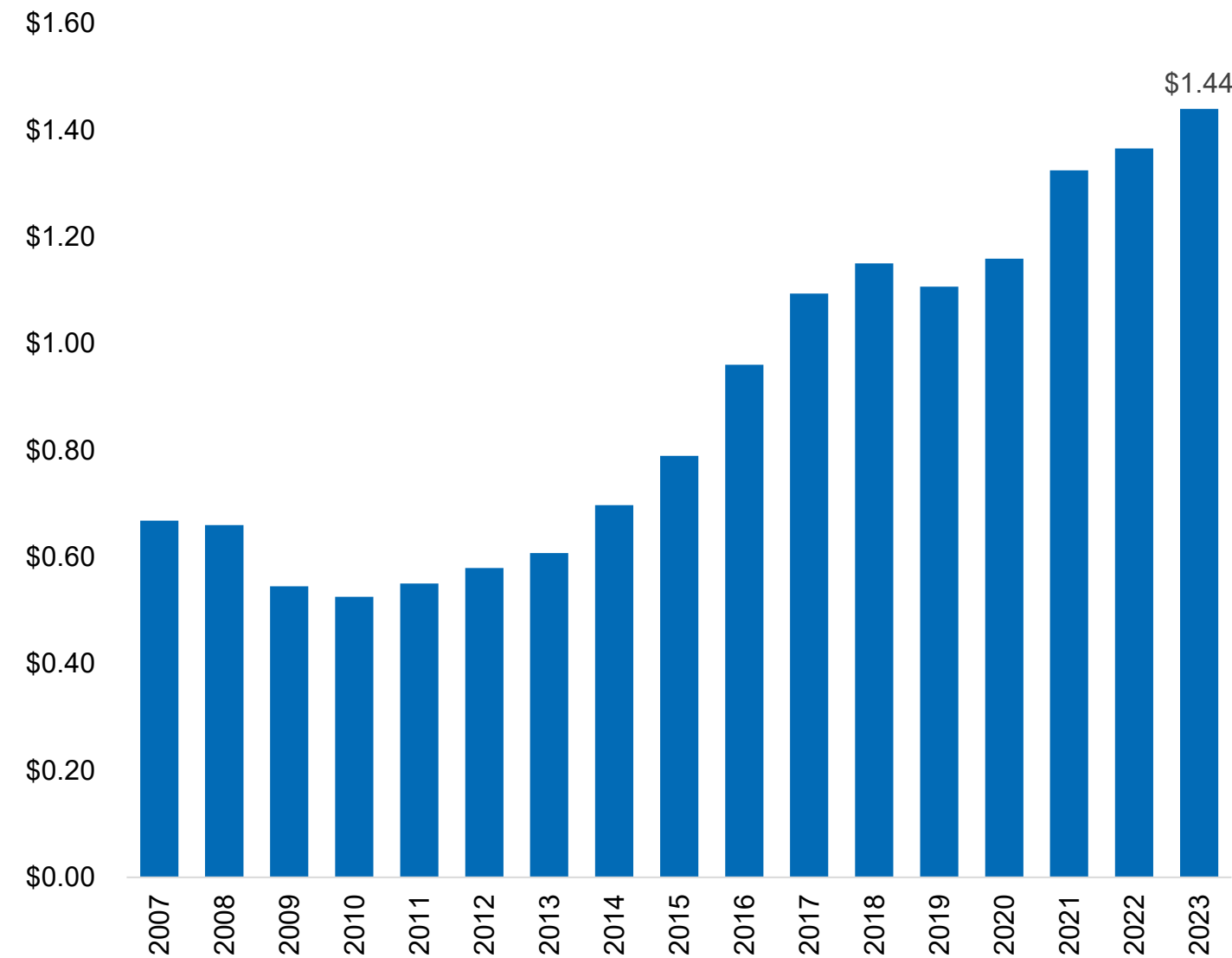


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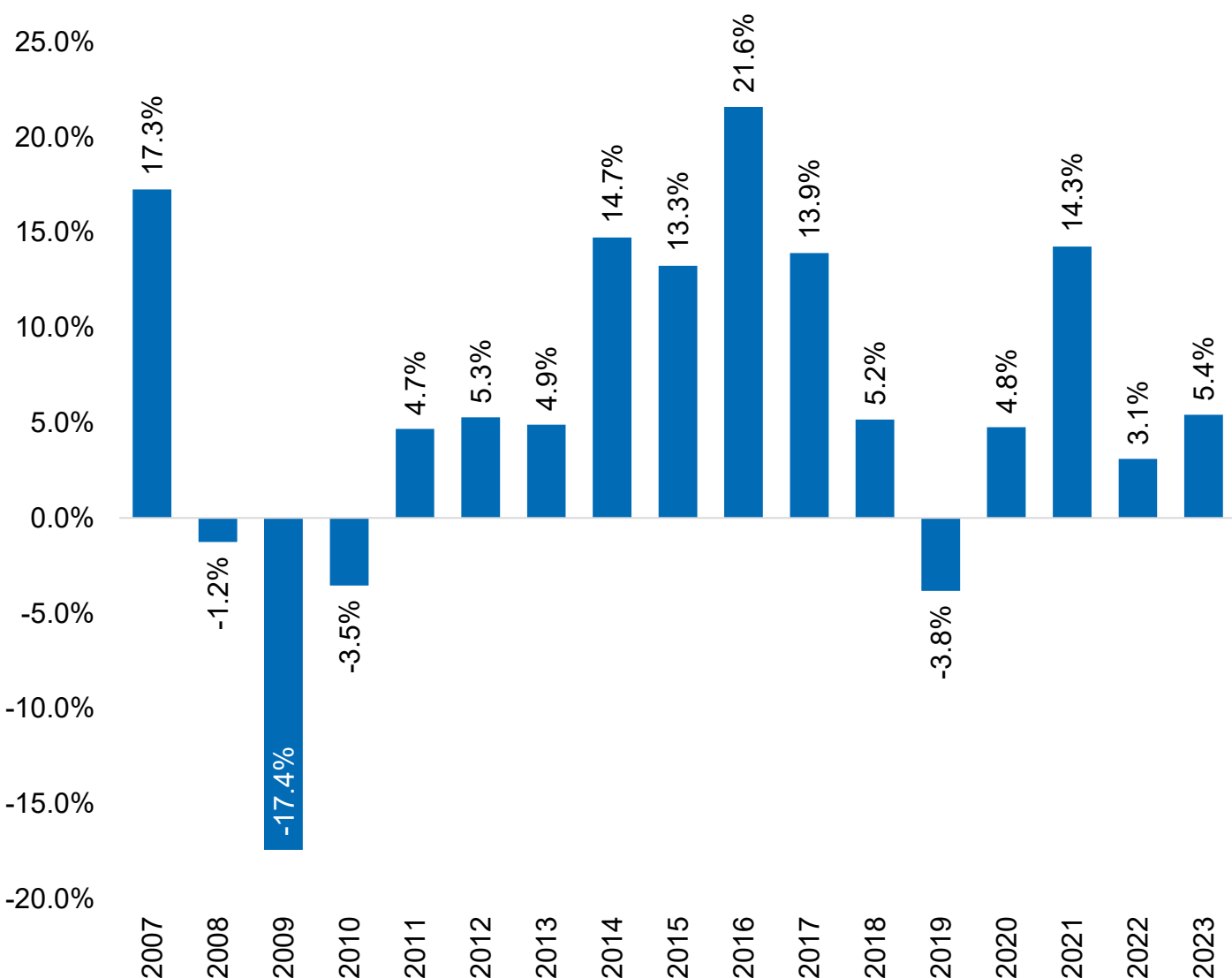
Industrial Asking Rent Growth Continues into 2023 to Record Highs

Industrial average asking rents posted modest growth, increasing by 5.4% since the end of 2022. Rent growth in the industrial sector has remained remarkably stable, with industrial and warehouse rents climbing consistently. This trend is expected to continue due to low vacancy and new product steadily entering the market, which will in turn push rents higher.

Industrial Average Asking Rent, \$/SF, NNN



Year-over-Year Asking Rent Growth Rate % Change



Source: Newmark Research, CoStar

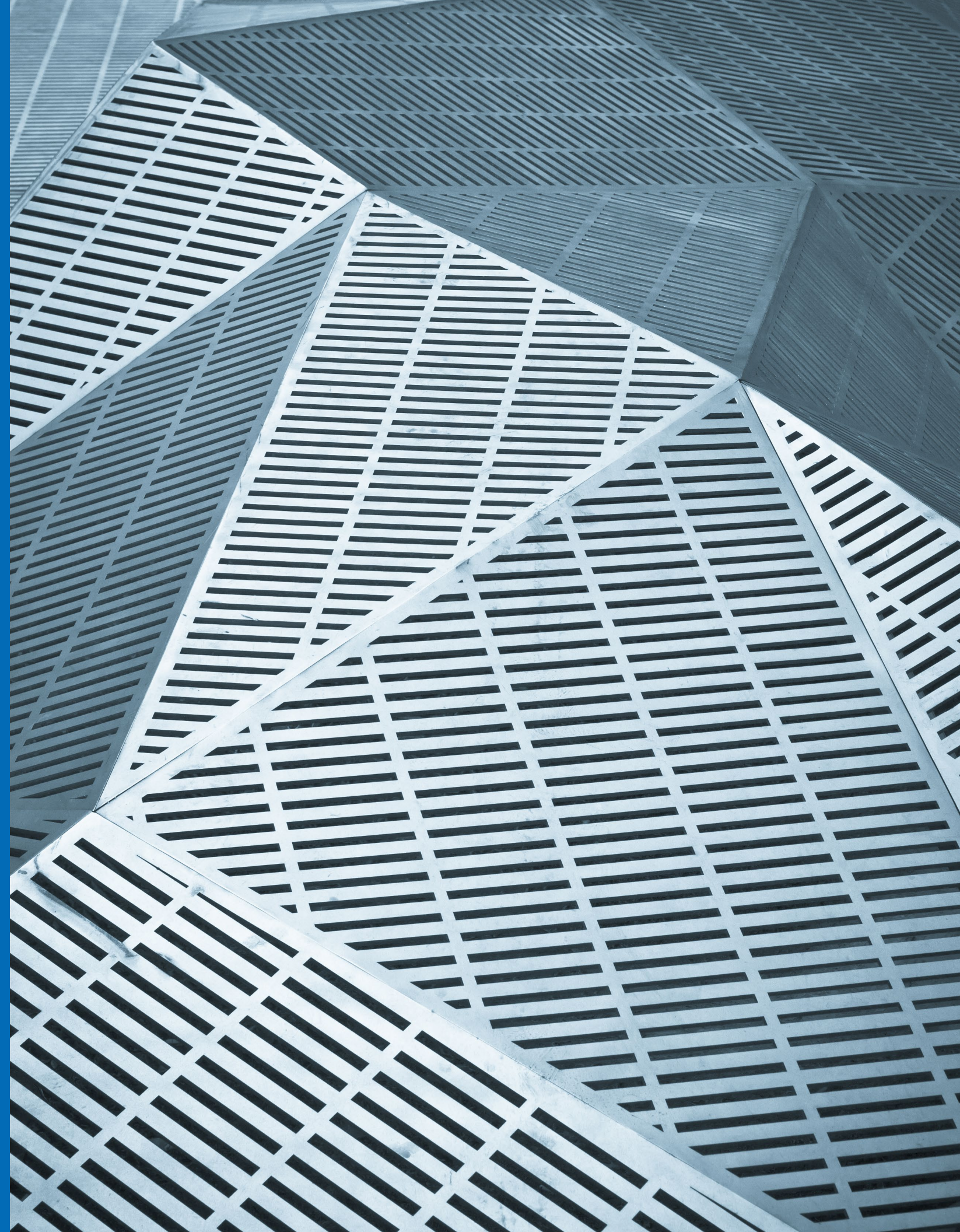
Strong Leasing Activity Compared to Office, R&D Sectors

Leasing activity fell slightly in the third quarter of 2023, with gross absorption totaling ±1.5 million SF, down from ±2.2 million square feet in the previous quarter, but remains strong compared to other sectors. Several of the top deals this quarter were new leases from tenants expanding within the region, including the former Sana Biotechnology building that was built in 2019, evidencing that growth continues in the industrial market, especially for newer logistics projects.

Select Lease Transactions				
Tenant	Building	Submarket	Type	Square Feet
RK Logistics Group	41707 Christy Street	Fremont	Renewal	190,080
Lease renewal. RK Logistics has been in this location since 2012 and currently occupy over 750,000 SF in Silicon Valley, and signed a prelease last quarter for an additional 210,000 SF in Fremont.				
Quanta Computer	5567 Cushing Parkway	Fremont	New Lease	163,193
New lease. This space was formerly marketed as a sublease from Sana Biotechnology, but Sana’s lease was terminated and Quanta made a deal directly with OMP. The space has never been occupied.				
Super Micro Computer	550 Brokaw Road	San Jose	New Lease	132,900
New lease. This building is the former Fry’s Electronics space and will likely be significantly renovated to suit a new technology/manufacturing user.				
Bintang Badminton	48900 Milmont Drive	Fremont	New Lease	129,979
New lease. This building was recently improved and will be used as an indoor badminton court.				
Slakey Brothers	1480 Nicora Avenue	San Jose	Renewal	93,605
Lease renewal. Slakey Brothers has been in this space since 2013.				

Source: Newmark Research

Appendix



Silicon Valley Overview



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