

3Q23

Silicon Valley R&D 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 lease this quarter was a 588,111 SF leaseback by Western Digital (formerly Sandisk) at 901-1101 Sandisk Drive in Milpitas. Like many companies, Western Digital felt the pressure of upcoming economic uncertainty and made the deal to improve its cash position.
- Google put their entire ±477,000 SF Quad/Whisman campus up for sublease this quarter, causing vacancy in Mountain View to rise from 10.3% to 16.1% quarter over quarter. Following several large owner-user completions in prior years, the tech giant has put up ±1.8 million SF across the Valley this year to consolidate operations.
- The 1.4 million SF of construction pipeline is primarily comprised of bolstered by Intuitive Surgical’s campus expansion totaling 1.21 million SF.

Leasing Market Fundamentals

- Net absorption in the third quarter of 2023 totaled negative 1.04 million SF, with year to date net absorption measuring negative 2.02 million SF. This is the sixth consecutive quarter of occupancy losses in the R&D sector, and the largest quarter of occupancy losses since the third quarter of 2020.
- Despite occupancy losses, R&D rents have continued to climb in the Valley, increasing to \$2.86/SF, a 2.1% increase quarter over quarter. Life Science rents continue to push this level higher despite making up a small percentage of the total inventory, such as in Fremont, which now averages \$2.90/SF overall asking rent.
- The vacancy rate increased this quarter to 11.0%, a 110 basis point increase quarter over quarter primarily due a large influx of sublease space in Mountain View.

Outlook

- Deal volume remains low compared to pre-pandemic levels, with most large deals manifesting as renewals instead of new leases or expansions. This trend is expected to continue due to rising interest rates, tightening lines of potential credit for tenants and their investors alike.
- Despite several quarters of occupancy losses, rents among the region continue to climb, bolstered by life science conversions and a trend towards higher-end R&D space.
- The much-larger R&D market has stronger metrics than the Office market, however, given the movement towards smaller space and consolidation, the R&D sector is likely to continue to see occupancy losses in the immediate future.

1. Economy
2. Leasing Market Fundamentals
3. Appendix

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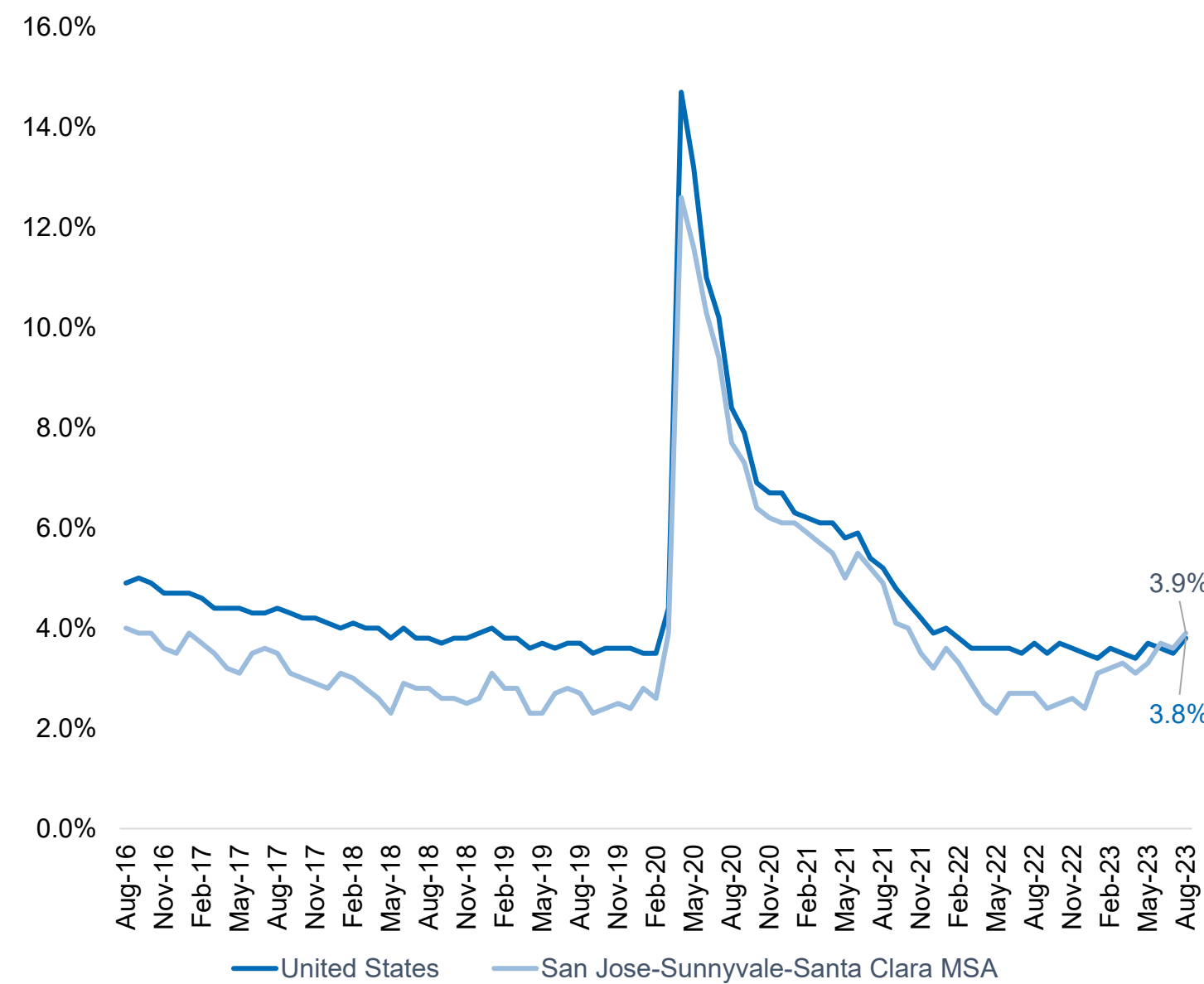
Economy



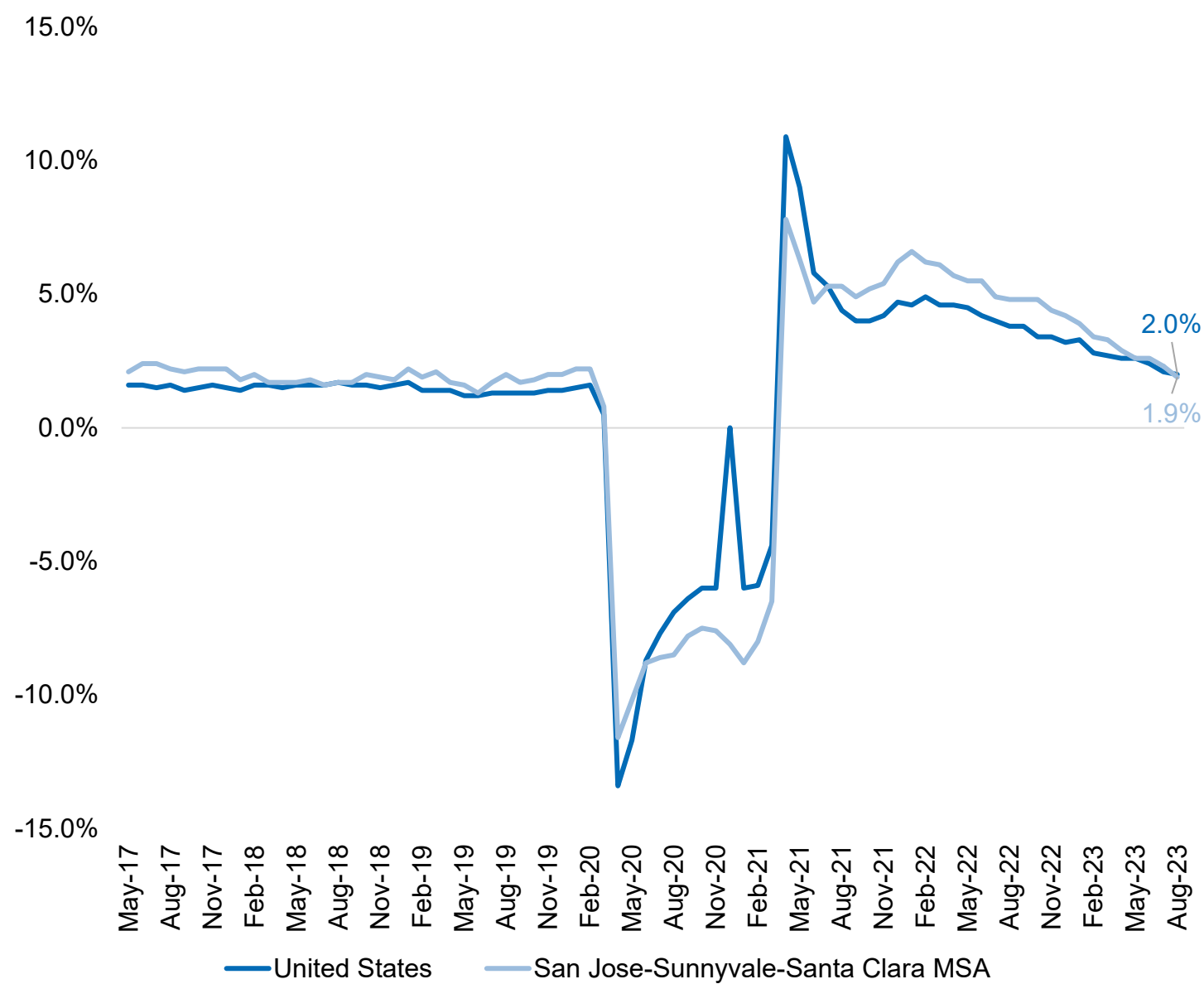
Metro Employment Trends Indicate a Slower Recovery Compared Nationally

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



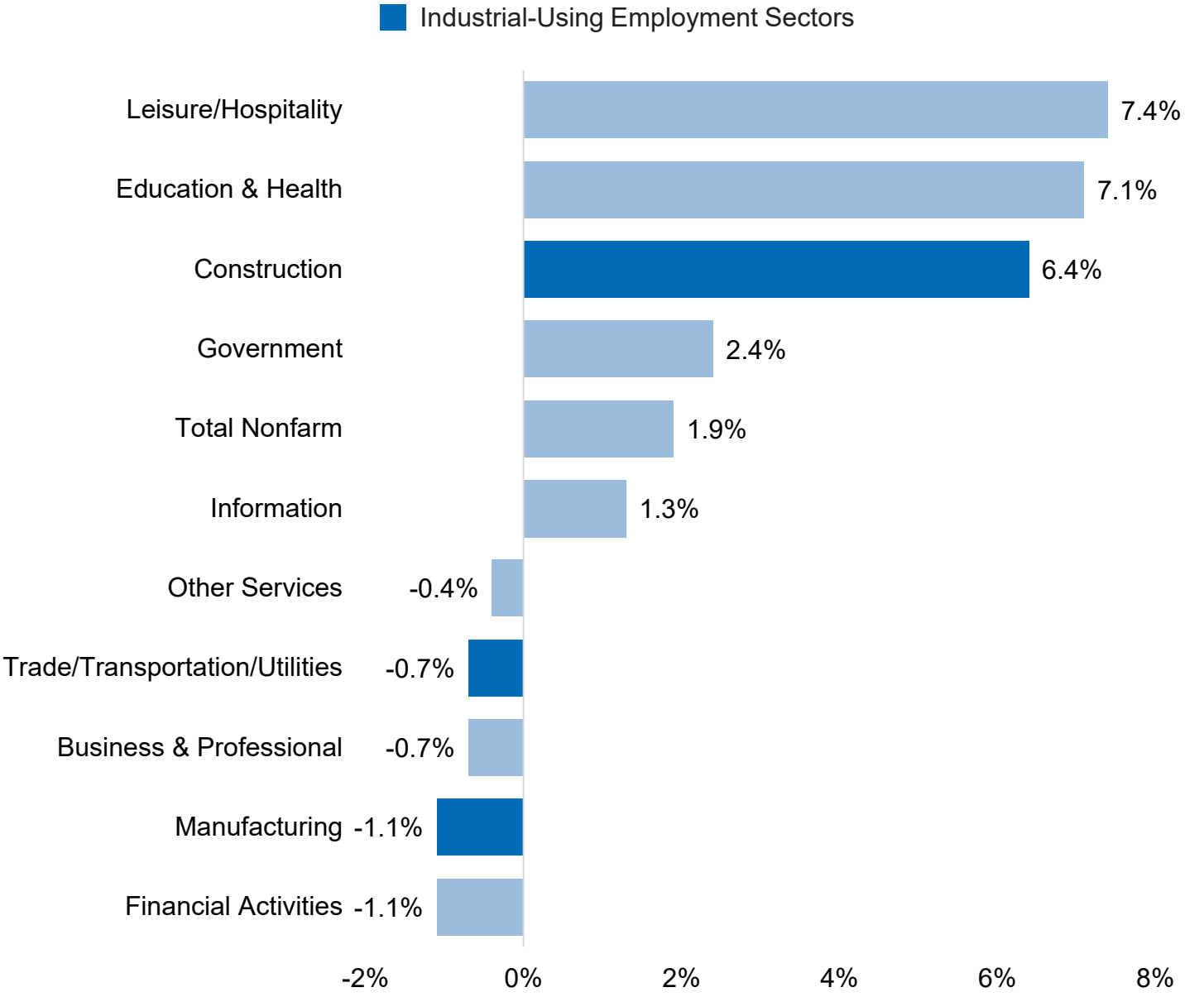
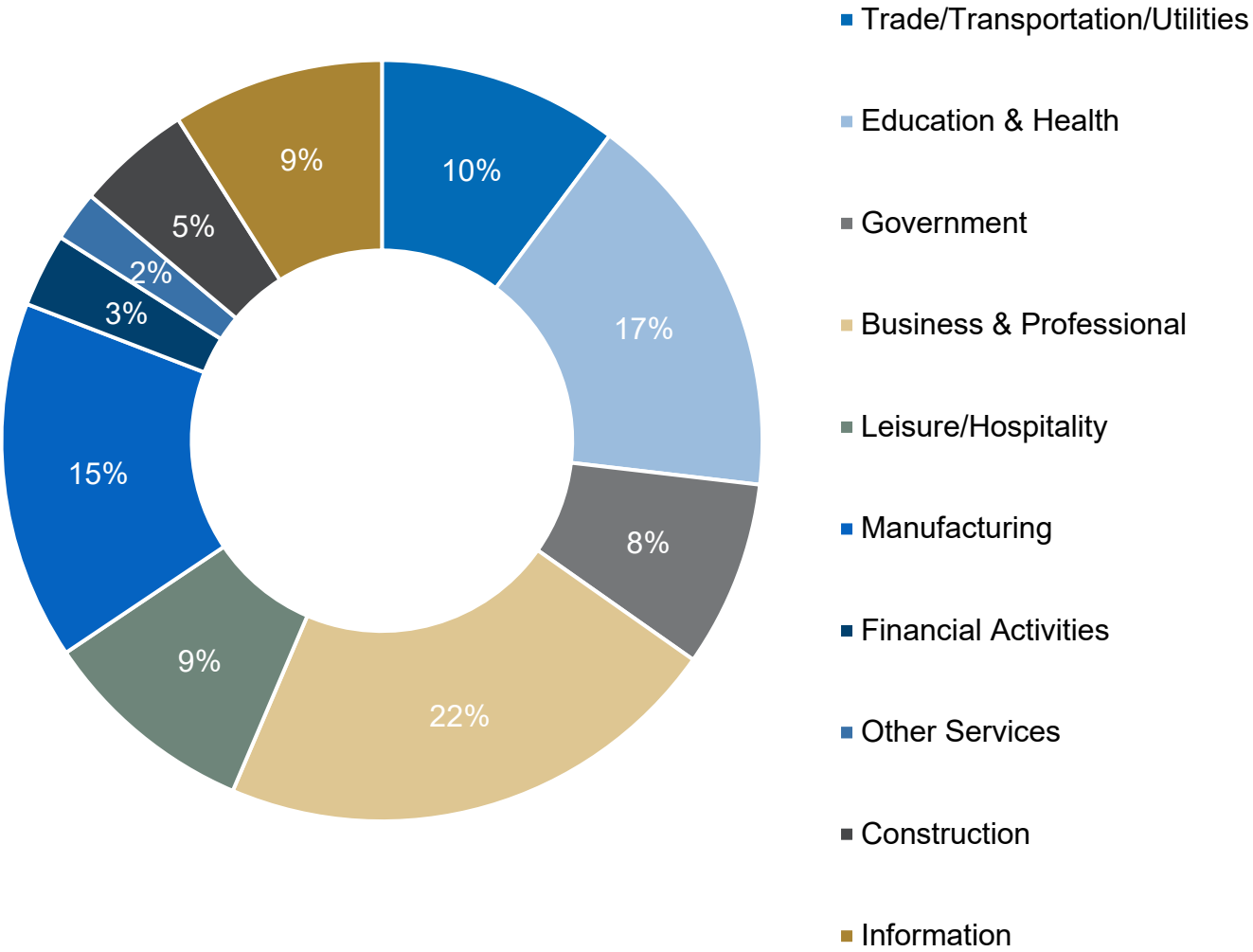
Source: U.S. Bureau of Labor Statistics, San Jose-Sunnyvale-Santa Clara MSA

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

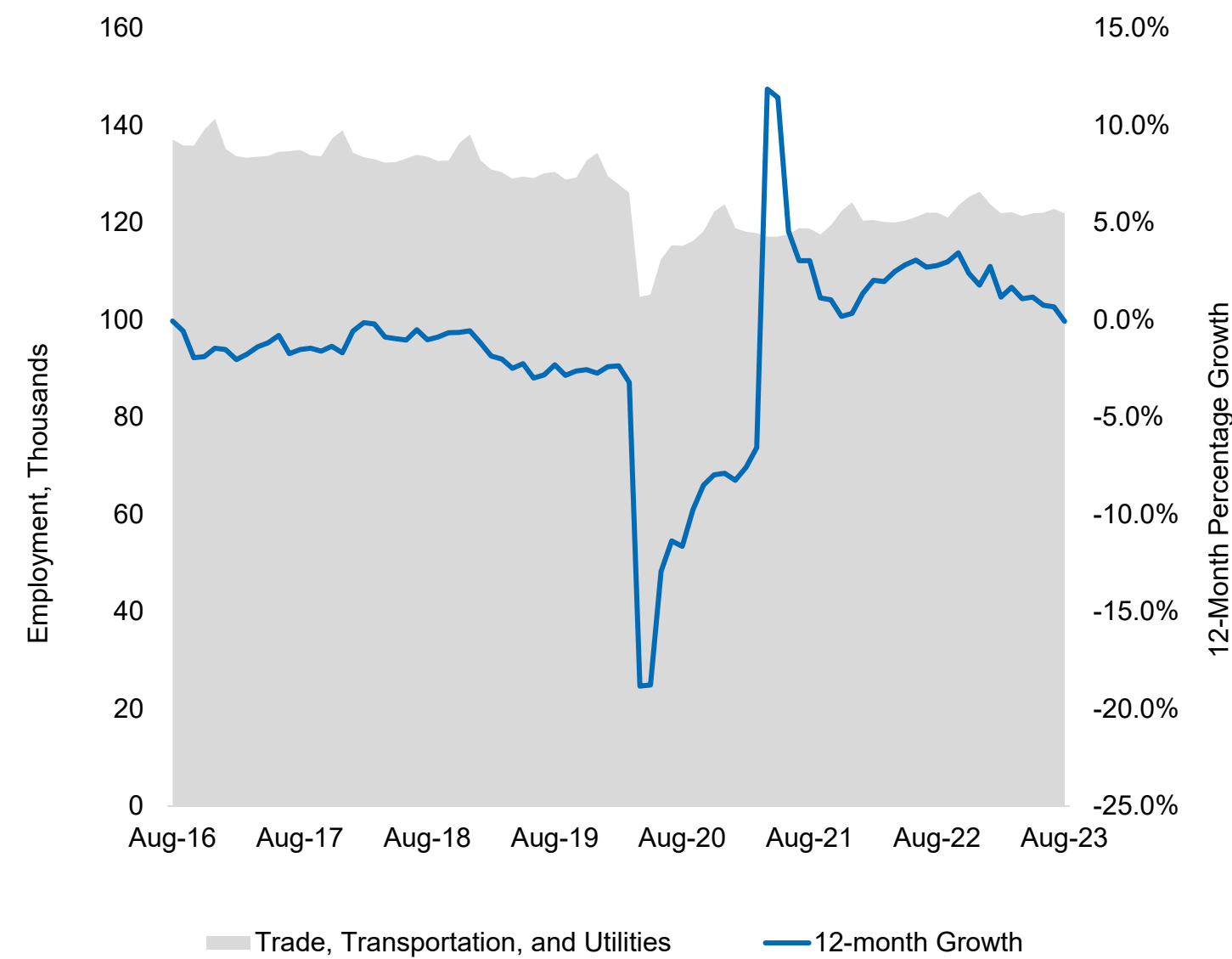


Source: U.S. Bureau of Labor Statistics, San Jose-Santa Clara-Sunnyvale
Note: August 2023 data is preliminary.

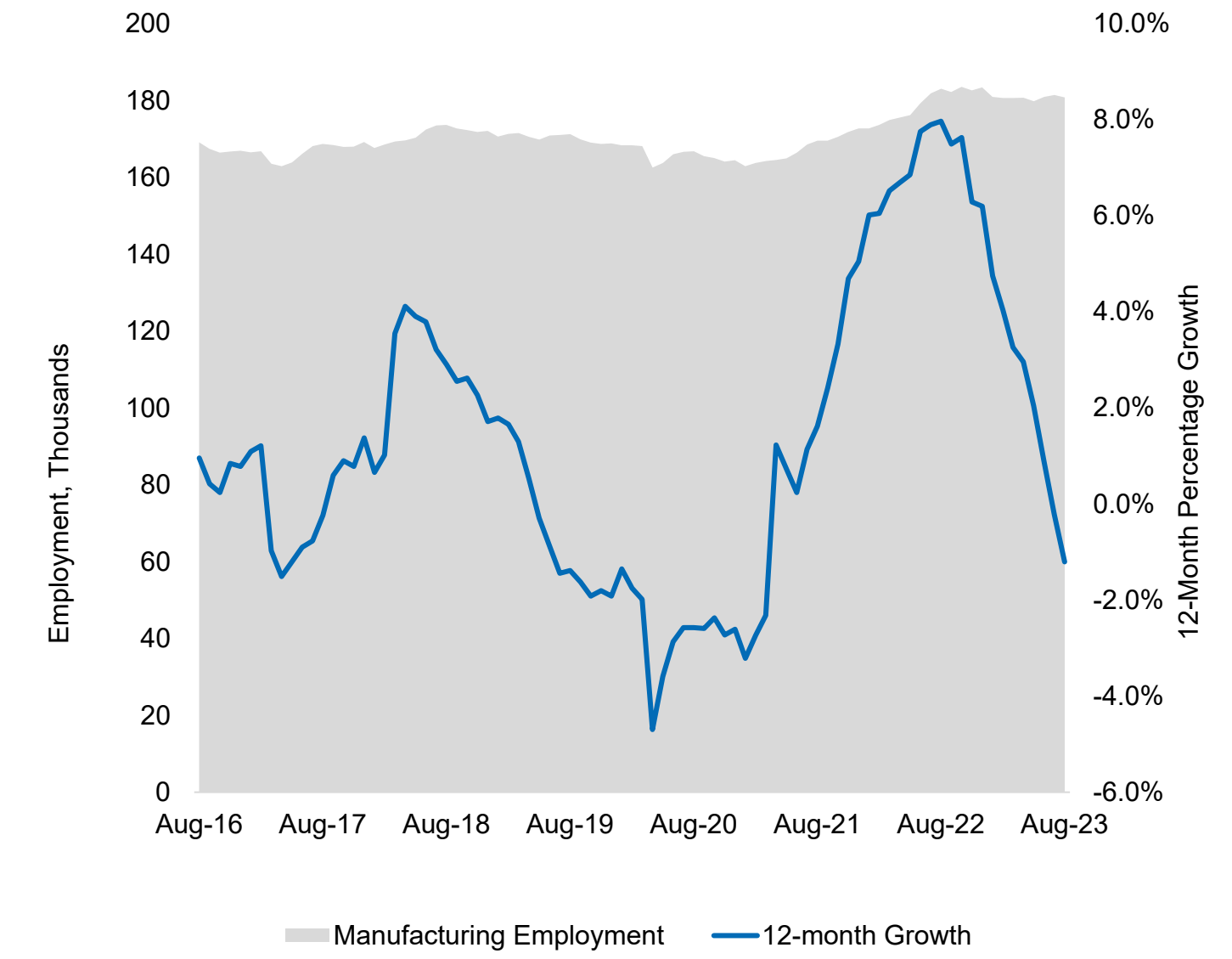
Industrial Employment Strong but Not Immune to Softening Conditions

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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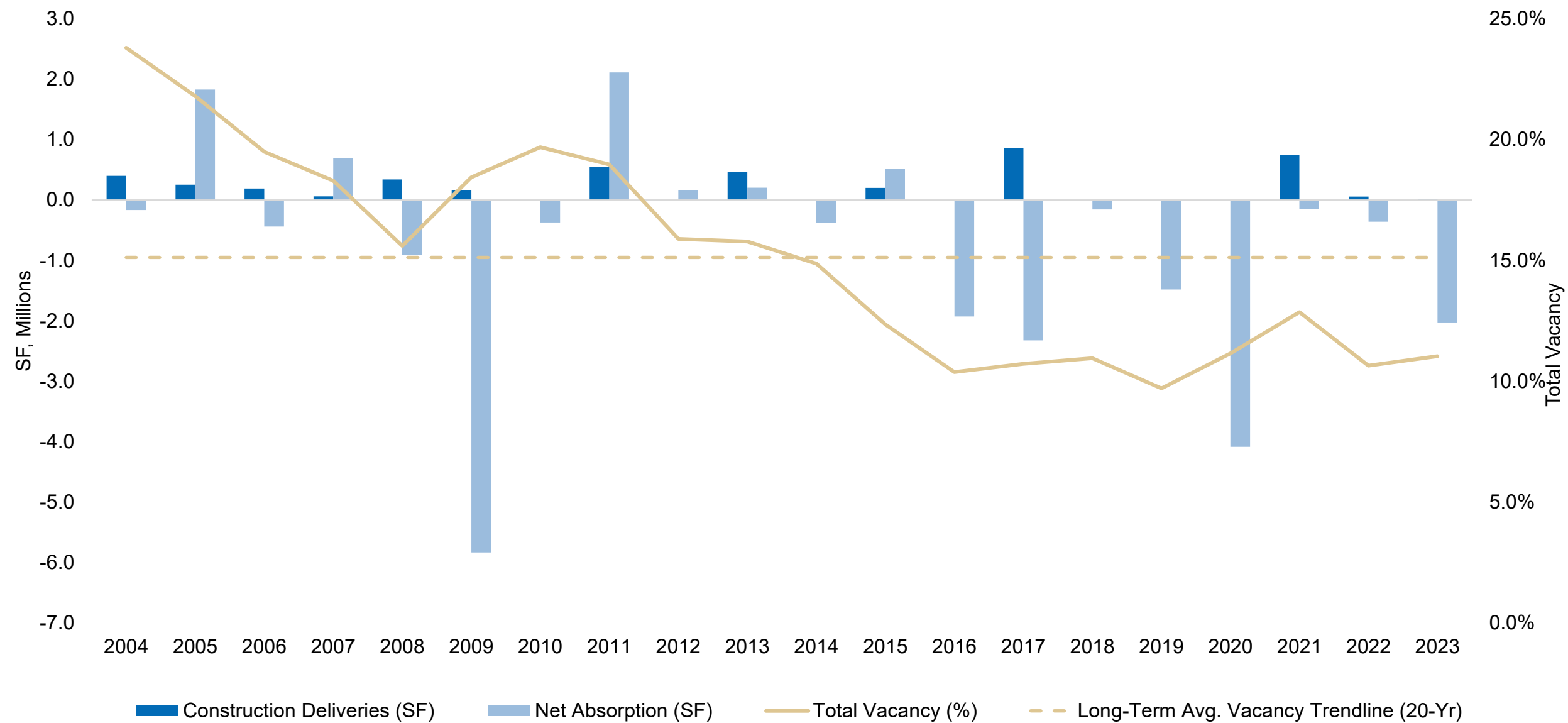
Leasing Market Fundamentals



Vacancy Levels Out as Demand Remains Low

The vacancy rate increased to 11.0% at the end of the third quarter of 2023, rising from 9.9% after seeing 1.0 million SF of occupancy losses region-wide. Deliveries remain at a low level due to the office sector primarily capturing developer interest. The exception to this would be owner-user build-to-suits, of which 1.1 million square feet is currently in the pipeline.

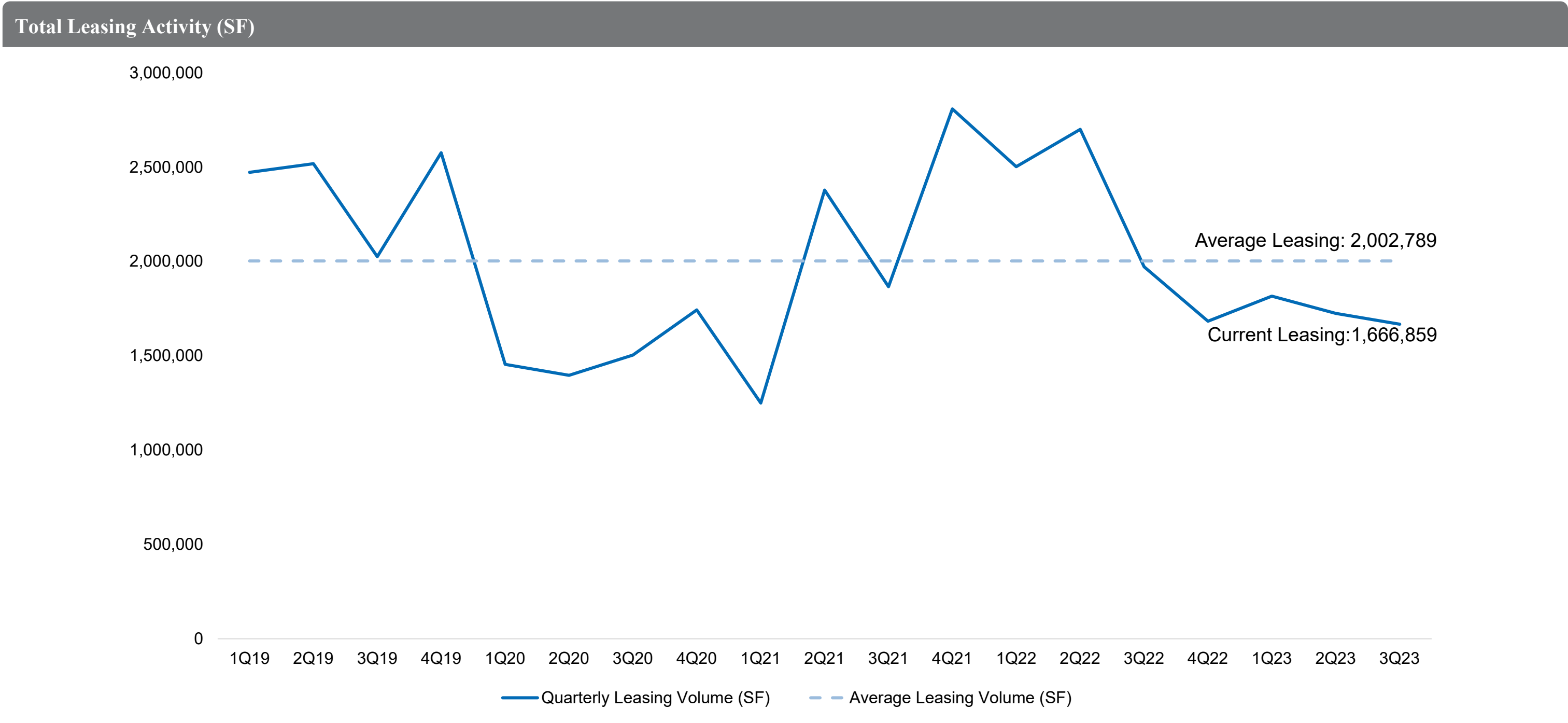
Historical Construction Deliveries, Net Absorption, and Vacancy



Source: Newmark Research

R&D Leasing Activity Decelerates to Pre-Pandemic Measures

Demand for R&D space remained at a contracted level in the third quarter of 2023, with leasing activity trending below the levels of the pre-pandemic era. Although current leasing seems to be on par with the year, a 588,000 SF leaseback drove a significant chunk of leasing this quarter and actual leasing volume is much lower than what it seems. Activity in 2023 has fallen off significantly compared to 2022 and will likely remain low going forward.



Source: Newmark Research, CoStar

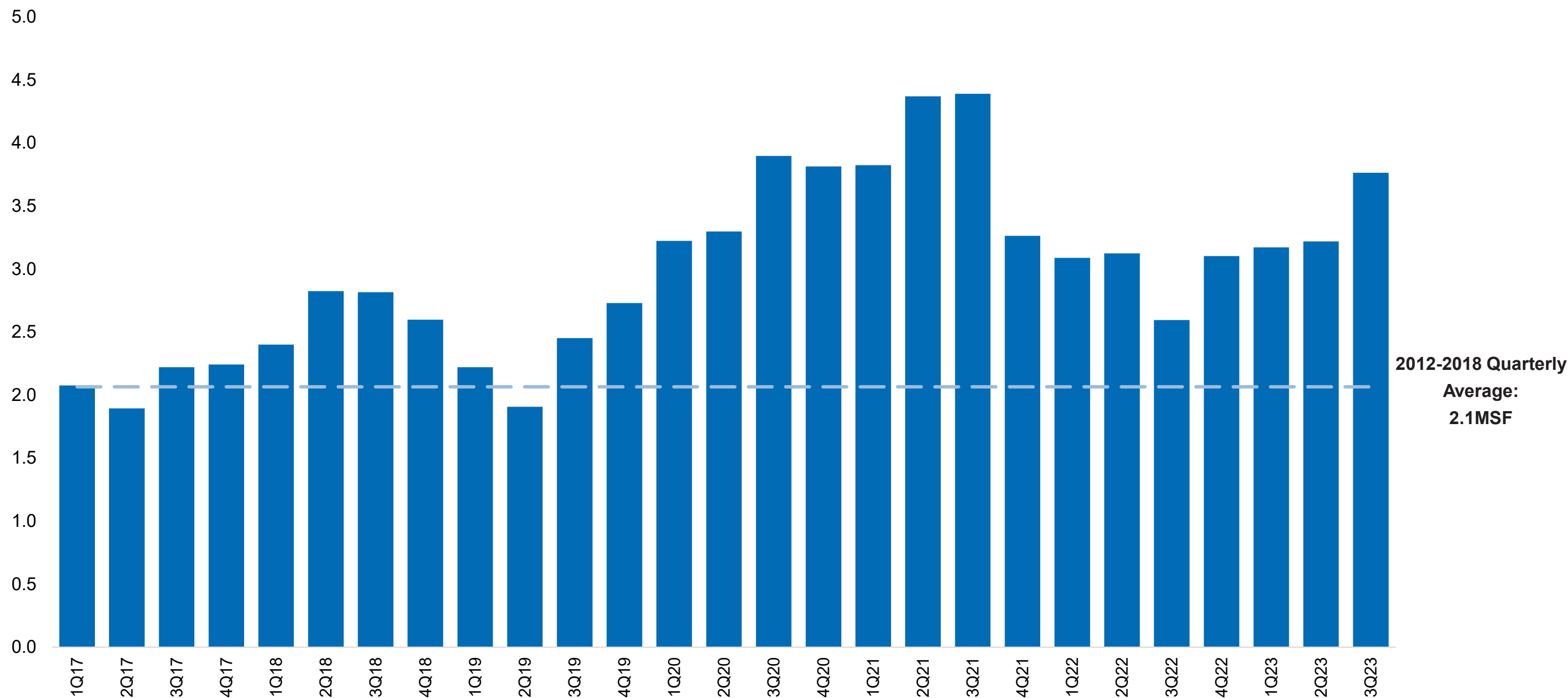
Mountain View Sees Surge in Vacancy

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Sublease Availability Spikes above Pre-Pandemic Levels

Sublease volume in the third quarter of 2023 rose significantly from the previous quarter, as ±477,000 square feet was added in the Mountain View submarket from a single sublessor. Sublease space is again on the rise, although not at the same level following the pandemic. Given the low level of demand, it's likely that sublease space will continue to rise through 2024.

Available Industrial Sublease Volume (msf)



Source: Newmark Research, CoStar

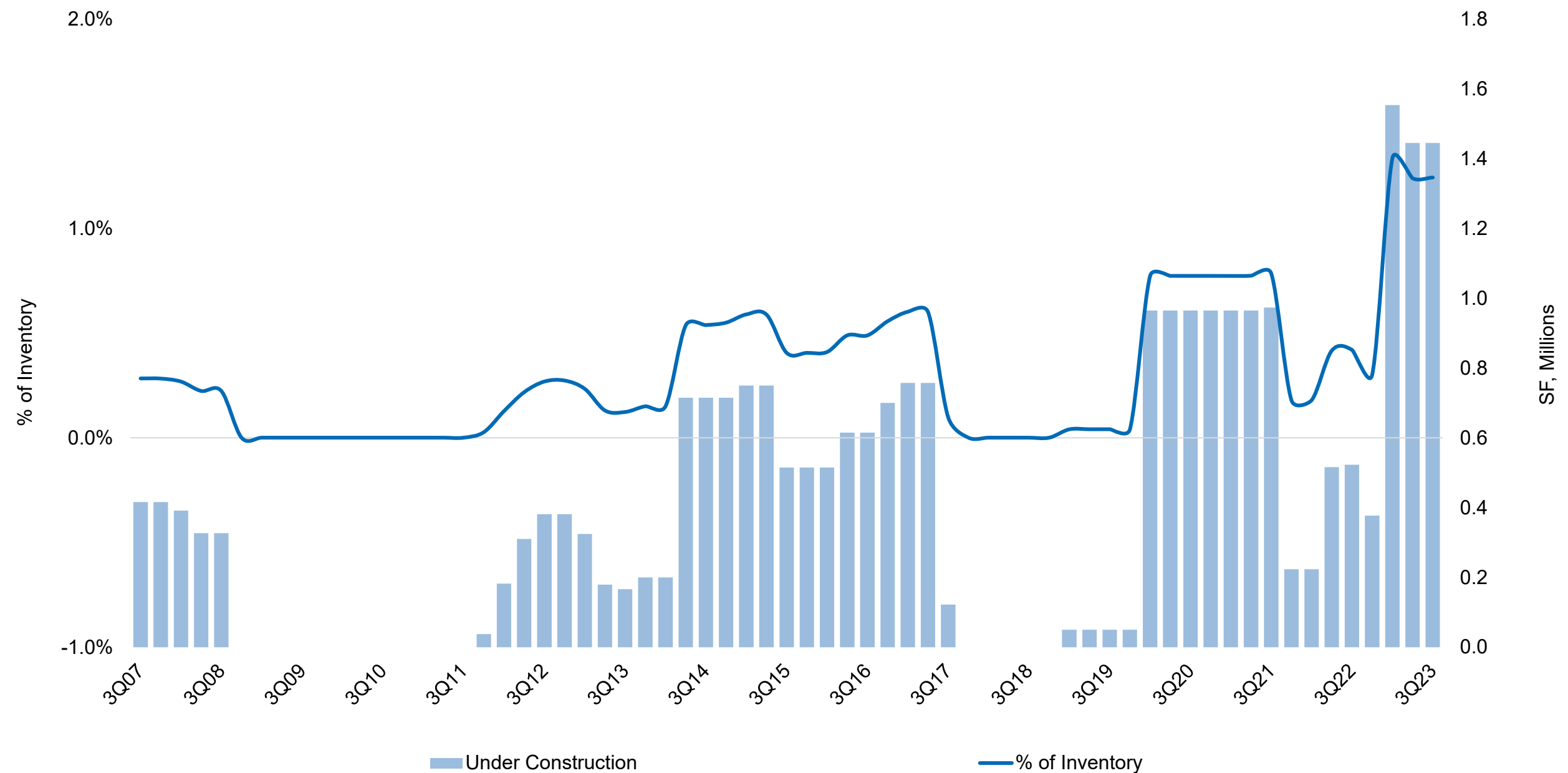
Uptick in Sublease Space Found Mostly in San Jose, Mountain View

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R&D Construction Remains High Thanks to Owner-Users

The construction pipeline remained at a historically high level primarily due to Intuitive Surgical’s new campus expansion, however, no new projects broke ground this quarter. Although previously neglected in favor of office, hybrid office/R&D space has been shown to be a popular choice among tech and medical device occupiers in the Valley, with several recent R&D build-to-suits delivering in the past few years.

R&D Under Construction and % of Inventory

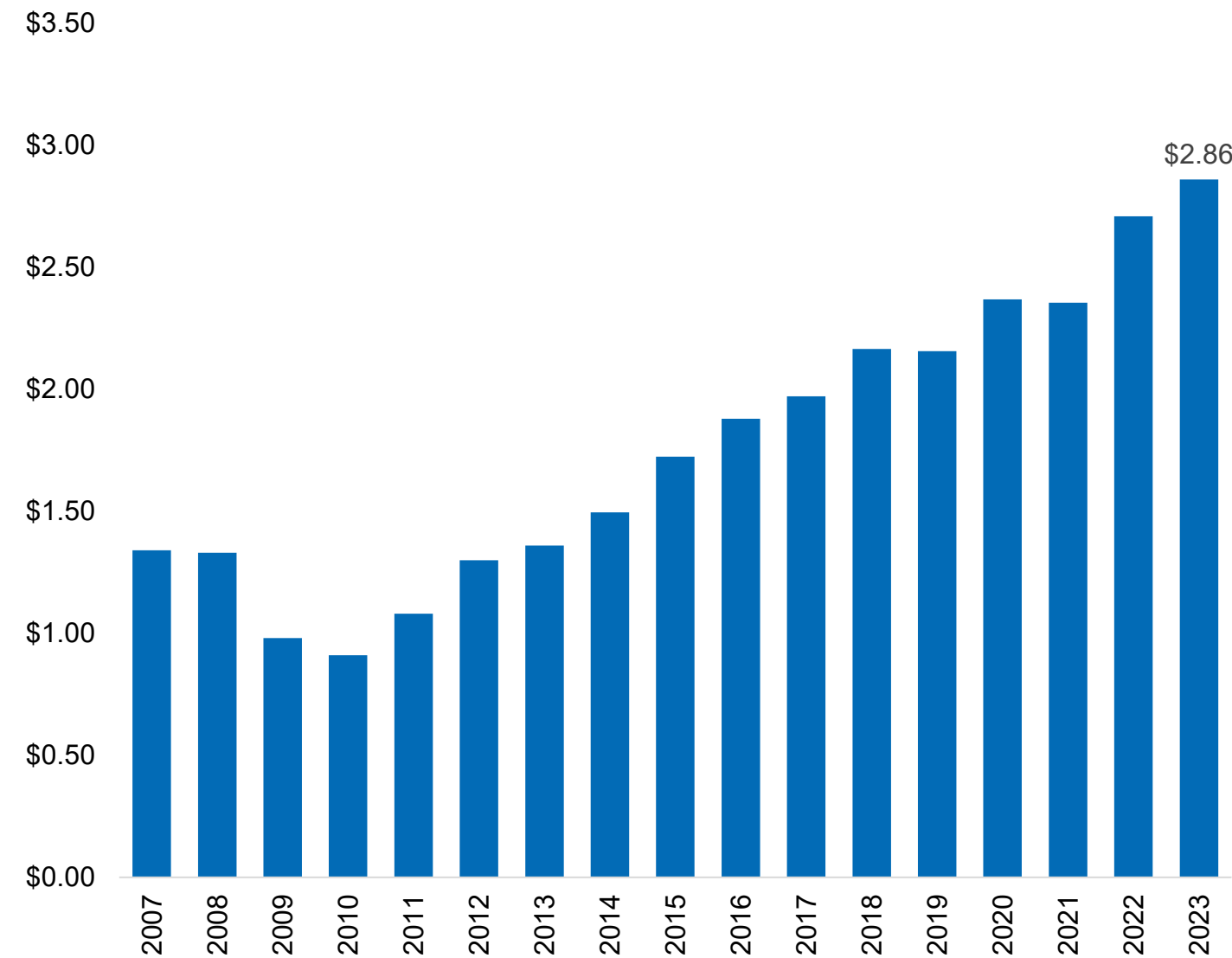


Source: Newmark Research, CoStar

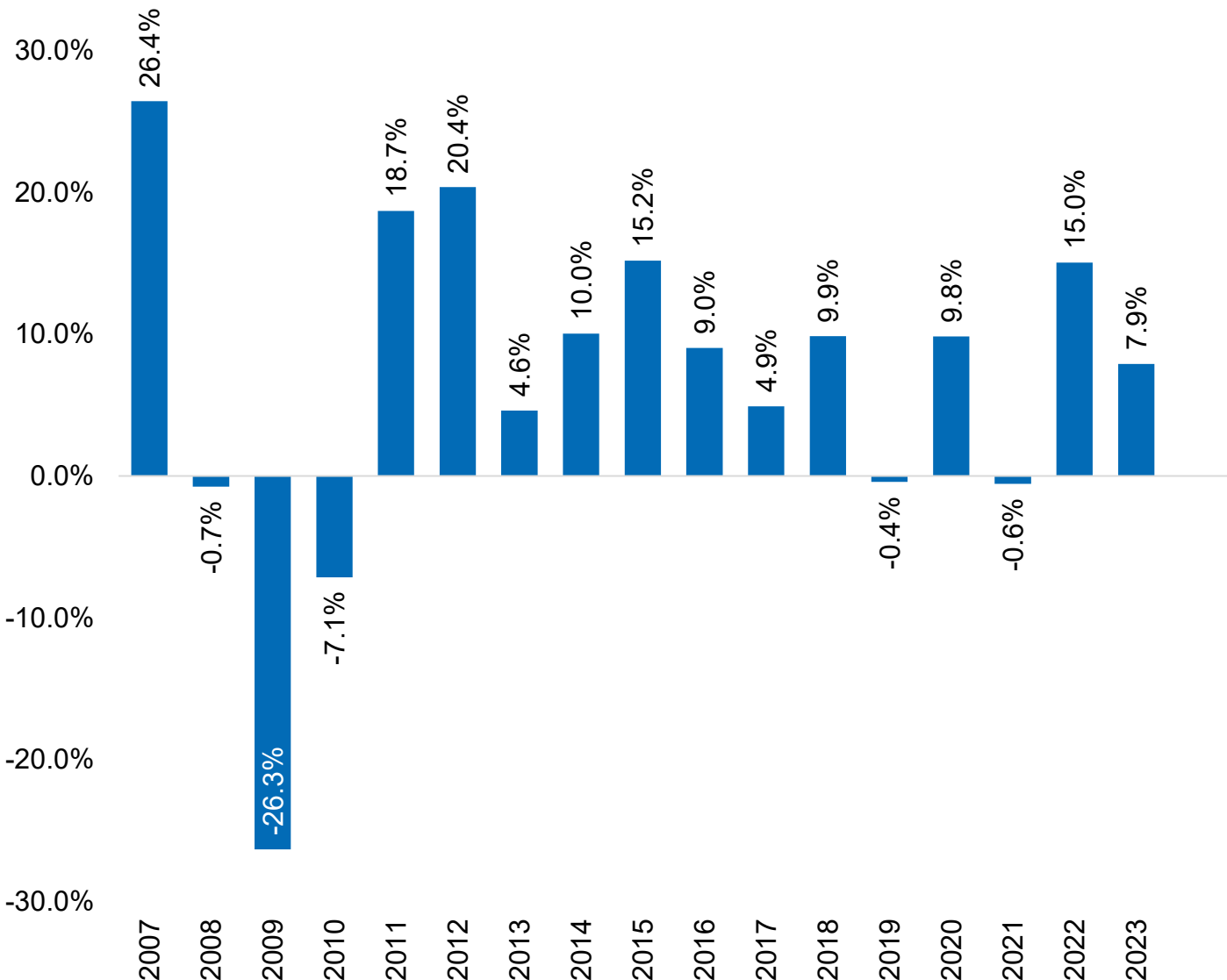
R&D Asking Rents Continue to Rise

R&D asking rents continued to grow, increasing to \$2.86/SF in the third quarter of 2023, a 2.1% increase since the previous quarter and a 7.9% increase year over year. Despite rising availability, rents continue to climb due to life science conversions as well higher-end R&D spaces being put back onto the market from tech vacancies.

R&D Average Asking Rent, \$/SF, NNN



Year-over-Year Asking Rent Growth Rate % Change



Source: Newmark Research, CoStar

Rent Performance Varies by Submarket

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Tenants Primarily Staying in Place

Four of the top five largest transactions this quarters did not involve any tenant movement, indicating that current tenants are not currently compelled to expand or relocate. Due to current economic conditions, financing has become increasingly expensive, making expansion or new leases riskier. Although the R&D sector has a lower vacancy rate compared to the office sector, demand for both product types remains low.

3Q23 Top Lease Transactions

Tenant	Building	Submarket	Type	Square Feet
Sandisk	910-1101 Sandisk Drive	Milpitas – Oak Creek	Leaseback	588,111
Sale leaseback. Sandisk sold 5 buildings totaling 588,111 square feet to Blue Owl Capital and signed a leaseback spanning through January 2039.				
ServiceNow	2251 Lawson Lane	Santa Clara – 101 South	Renewal	130,399
Renewal. This full-building lease is the only R&D building in ServiceNow’s Lawson Lane campus, owned by Sobrato.				
Institute for Business & Technology	91 E Tasman Drive	San Jose – North	New Lease	84,049
New lease. This building was renovated in 2009 and was on the market for 26 months prior to being leased.				
Trimble Navigation	510 DeGuigne Drive	Sunnyvale – Oakmead	Renewal	75,093
Renewal. Tenant has been in this space since 2005.				
WeRide	2630 Orchard Parkway	San Jose – North	Renewal	64,333
Sublease renewal. WeRide has been subleasing this space from Toshiba since 2019.				

Source: Newmark Research

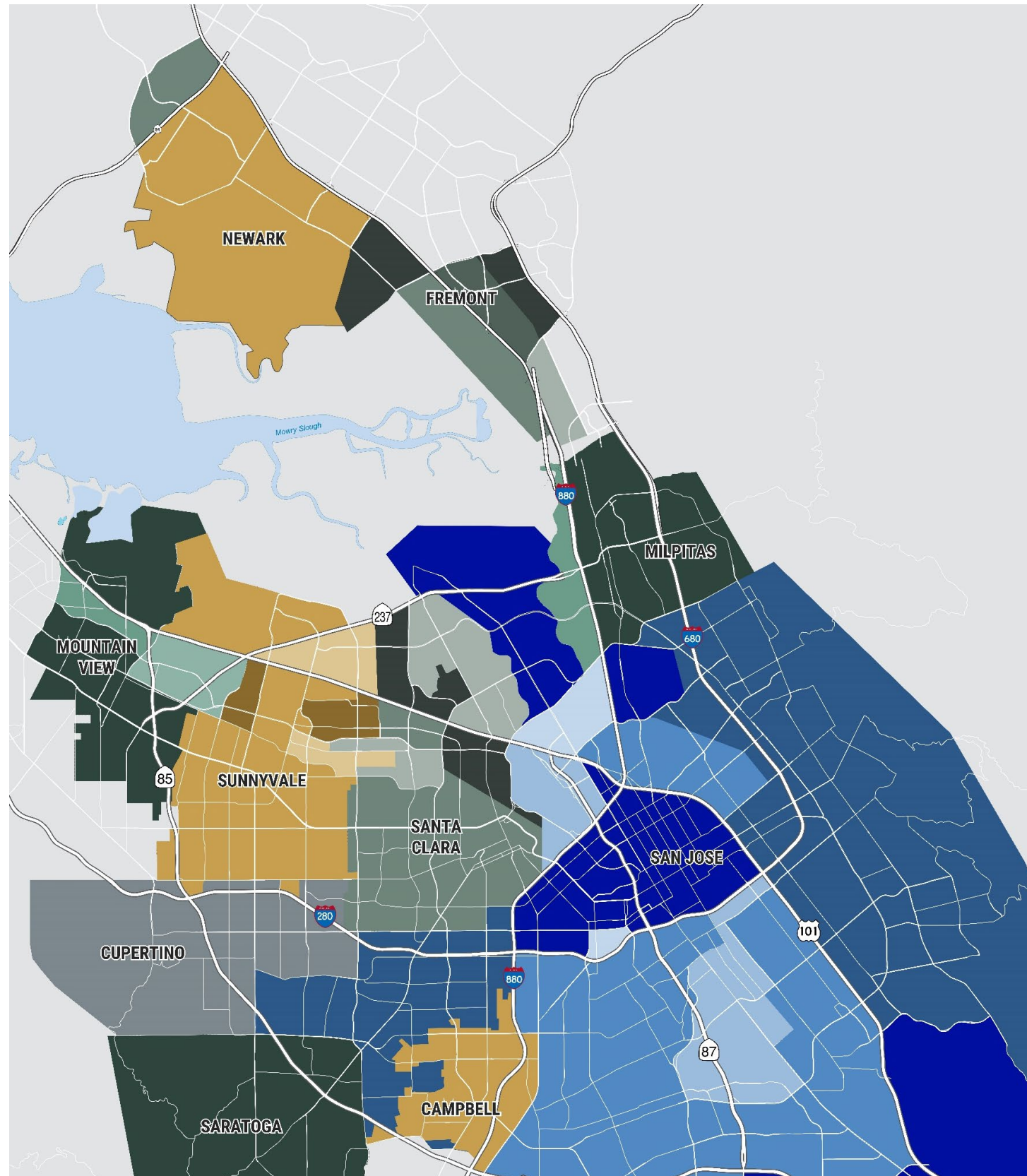
Appendix / Tables



Silicon Valley Statistics Overview

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Silicon Valley – Submarket Map



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