

4Q23

Silicon Valley Industrial Market Overview

NEWMARK

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1. Economy
 2. Leasing Market Fundamentals

4Q23

Economy



Market Observations

Economy

- The region's labor market remained stable in the fourth quarter of 2023, holding at 3.9% quarter-over-quarter while the national unemployment rate fell 10 basis points to 3.7%. Though trailing the national average, local unemployment remains below the 10-year average of 4.3%.
- 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 three quarters.
- The manufacturing industry saw a correction at the end of 2023, ending the year with a 2.0% decline in total employment following a surge of hiring in 2022. Other industrial-using sectors saw modest gains year-over-year.

Major Transactions

- The largest deal this quarter was a 3-building renewal by DGA Services totaling 386,383 at the Fleming Business Park in Milpitas, followed by Verdagy, a green hydrogen production company, subleasing 123,000 SF from Lucid Motors at 7395 Morton Avenue in Newark.
- Several large tech tenants vacated this quarter, the largest being Zoox, which vacated the newly-built 47540 Kato Road in Fremont, and Seagate, which is now subleasing 103,000 SF from their campus at 47488 Kato Road, which sold earlier in 2023.
- There was one completion this quarter, the 209,916 SF warehouse project at 47020 Kato Road. That building remains unleased.

Leasing Market Fundamentals

- Net absorption in the fourth quarter of 2023 totaled negative 71,375 SF in the industrial sector and negative 157,498 SF in the warehouse sector, for a total of 86,112 SF of positive absorption overall. Vacancy in the industrial sector rose slightly to 4.3% from 4.2% quarter-over-quarter, while the warehouse vacancy rate fell from 3.9% to 3.4%.
- Asking lease rates in the industrial sector increased from \$1.58/SF to \$1.60/SF, while warehouse asking rents rose from \$1.16/SF to \$1.29/SF quarter-over-quarter. Industrial and warehouse rents have consistently posted growth year-over-year for the past five years, indicating demand that has risen in step with new supply.
- Tenant demand remains strong in the industrial sector, with 2.3 million square feet of industrial requirements in the Valley, up from 1.6 million square feet year-over-year.

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.
- There is currently 1.8 million SF of industrial product under construction, of which just 6% is preleased. Although vacancy in the region has been consistently low for the past several years, these new projects, if unleased by delivery, could drive up vacancy through 2024.
- Owing to persistent demand from life science, manufacturing, and tech industries, market fundamentals are expected to remain strong throughout the Valley, despite growing pessimism among other product types.

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4Q23

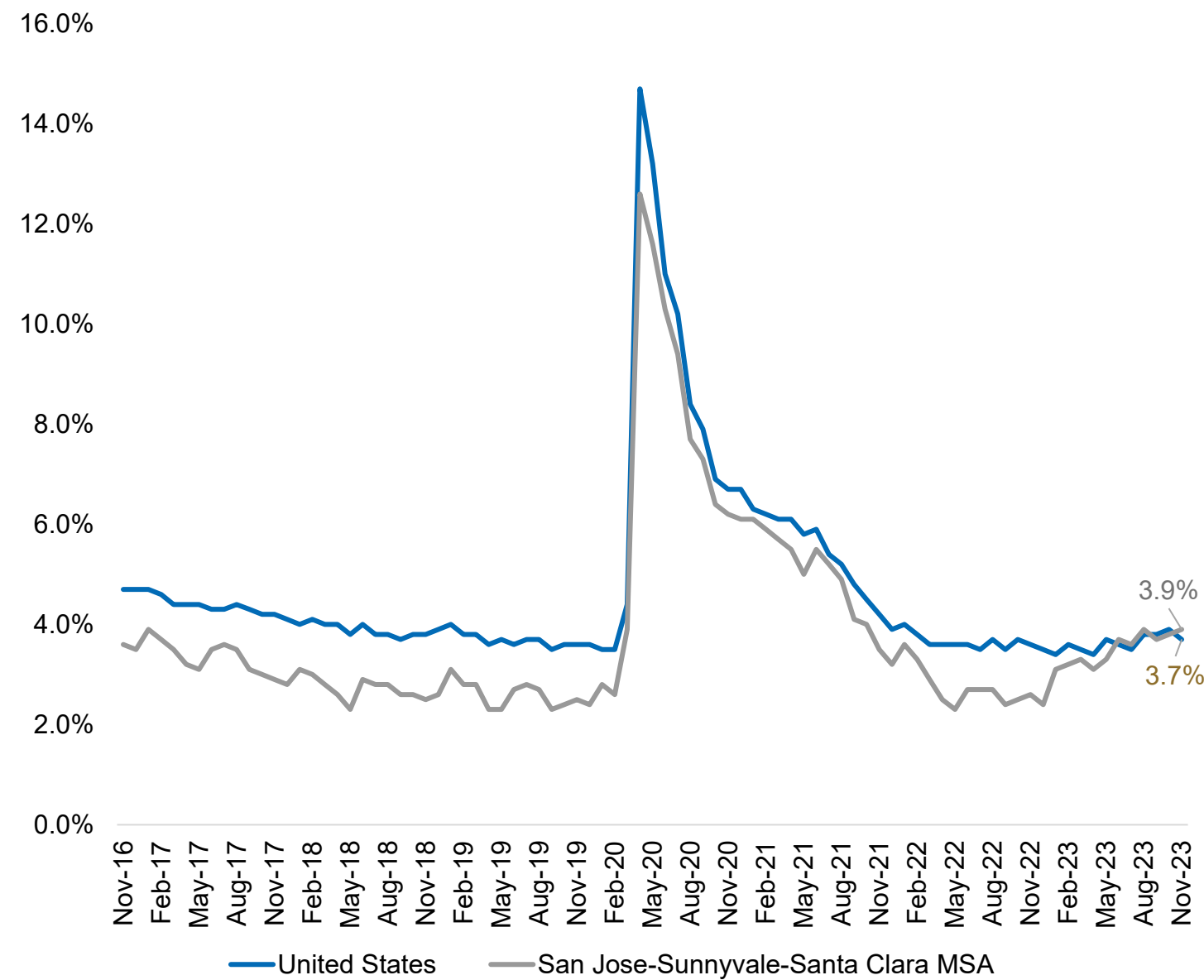
Economy



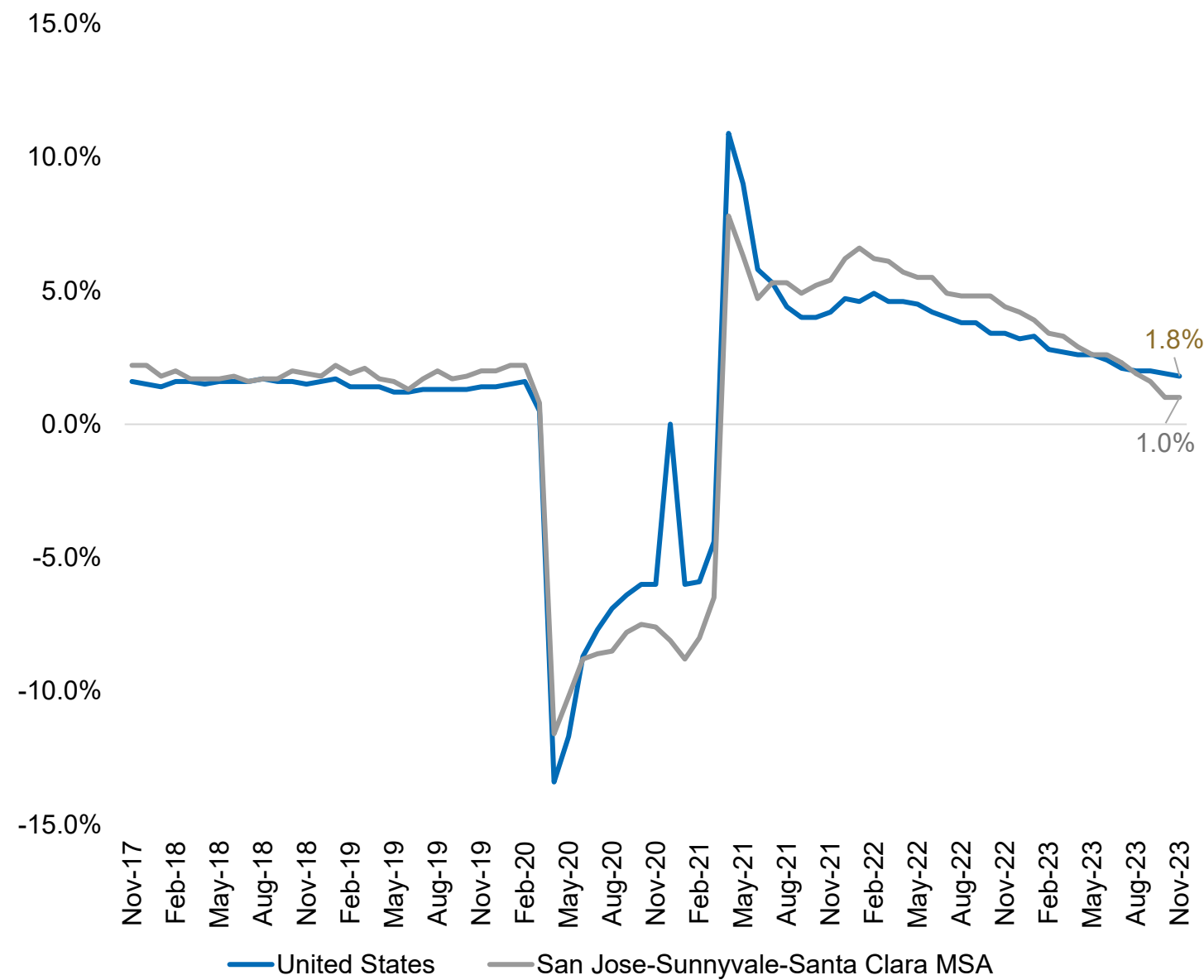
Metro Employment Trends Indicate a Slower Recovery Compared Nationally

The San Jose-Sunnyvale-Santa Clara MSA's overall unemployment rate rose for the third consecutive quarter to 3.9%, trending slightly higher than the national average of 3.7%. Though Santa Clara County has historically outperformed the US average, tech sector layoffs have caused companies to hit pause on hiring, tapering growth at the end of 2023.

Unemployment Rate, Seasonally Adjusted



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

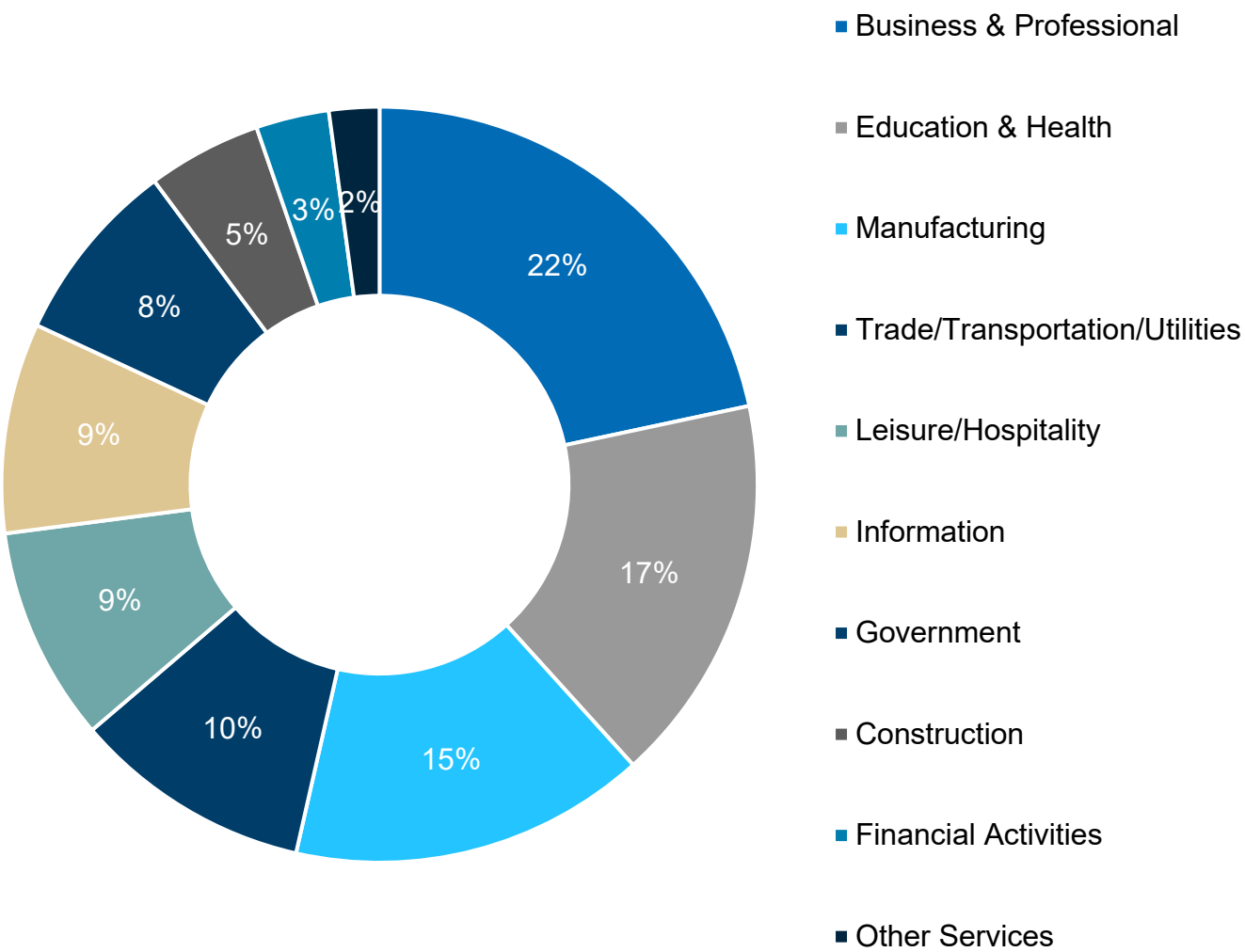


Source: U.S. Bureau of Labor Statistics, San Jose-Sunnyvale-Santa Clara MSA
Note: November 2023 data is preliminary.

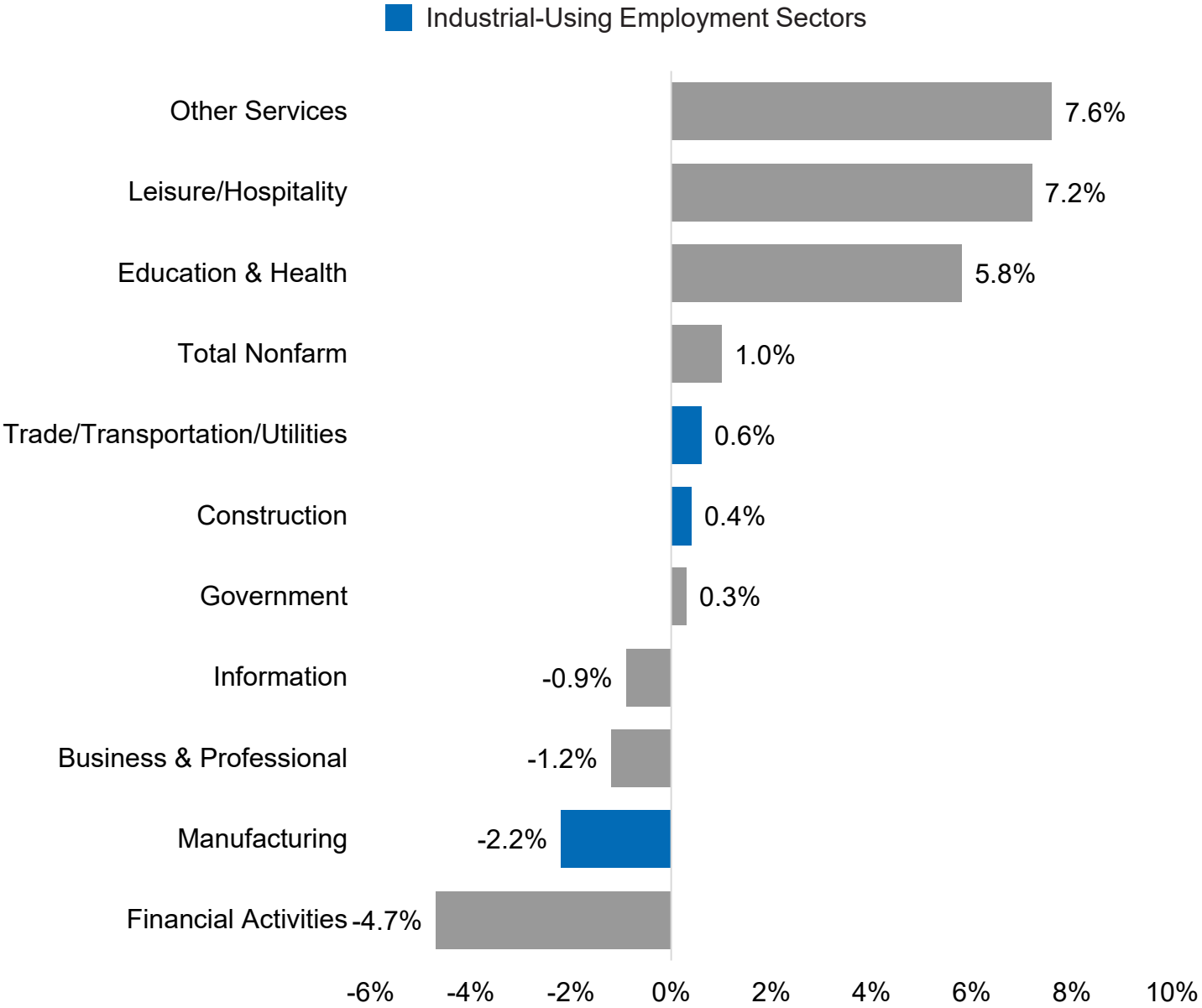
Job Growth Driven in Large Part by Services Still Making Up for Pandemic Losses

In step with a rising overall unemployment rate, several industries this quarter saw negative year-over-year growth, with the financial sector seeing the largest loss of employment year-over-year. The leisure/hospitality sector, however, consistently saw growth throughout 2023, as in-person dining and retail gradually returns to the region following the pandemic.

Employment by Industry, November 2023



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

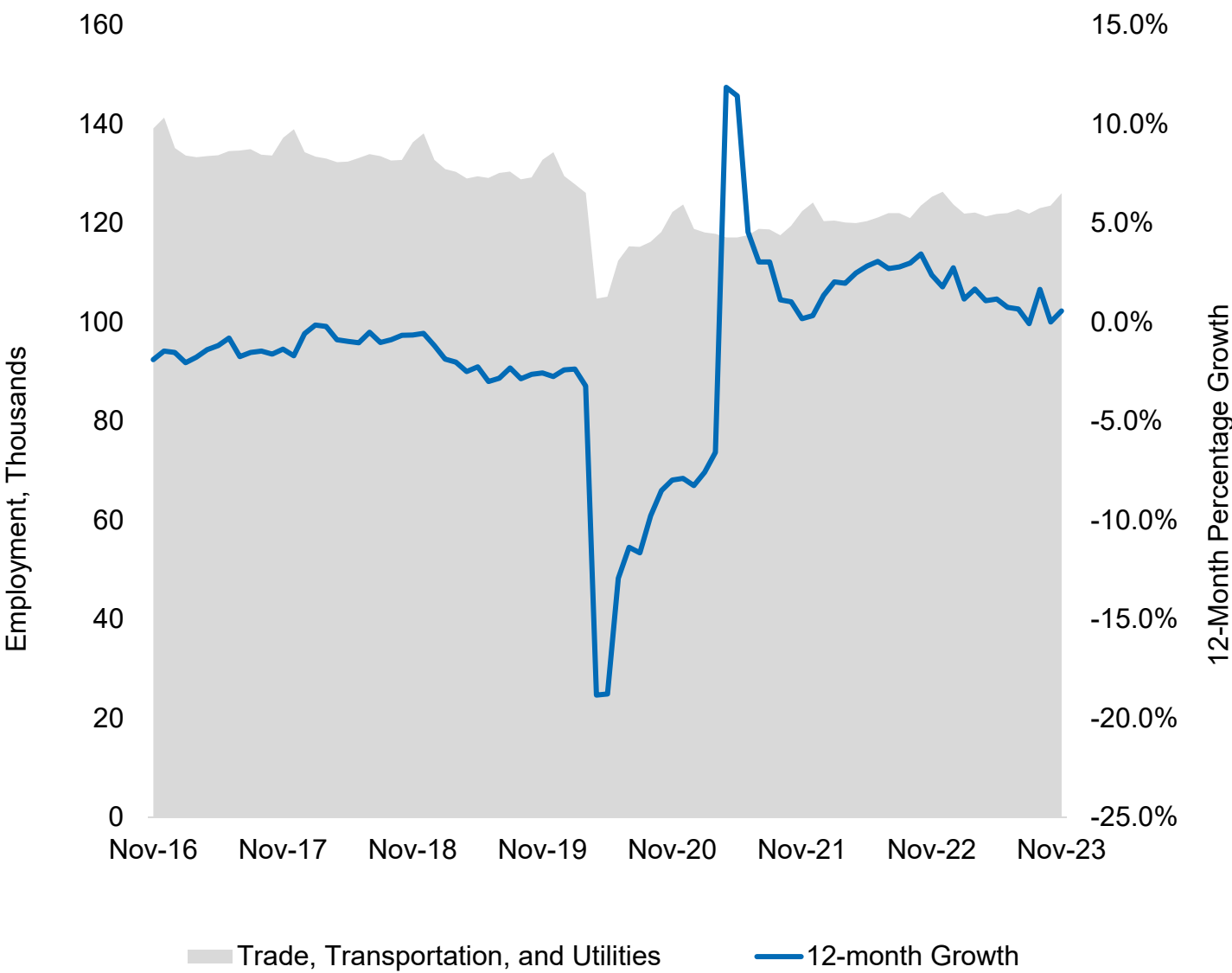


Source: U.S. Bureau of Labor Statistics, San Jose-Santa Clara-Sunnyvale
Note: November 2023 data is preliminary.

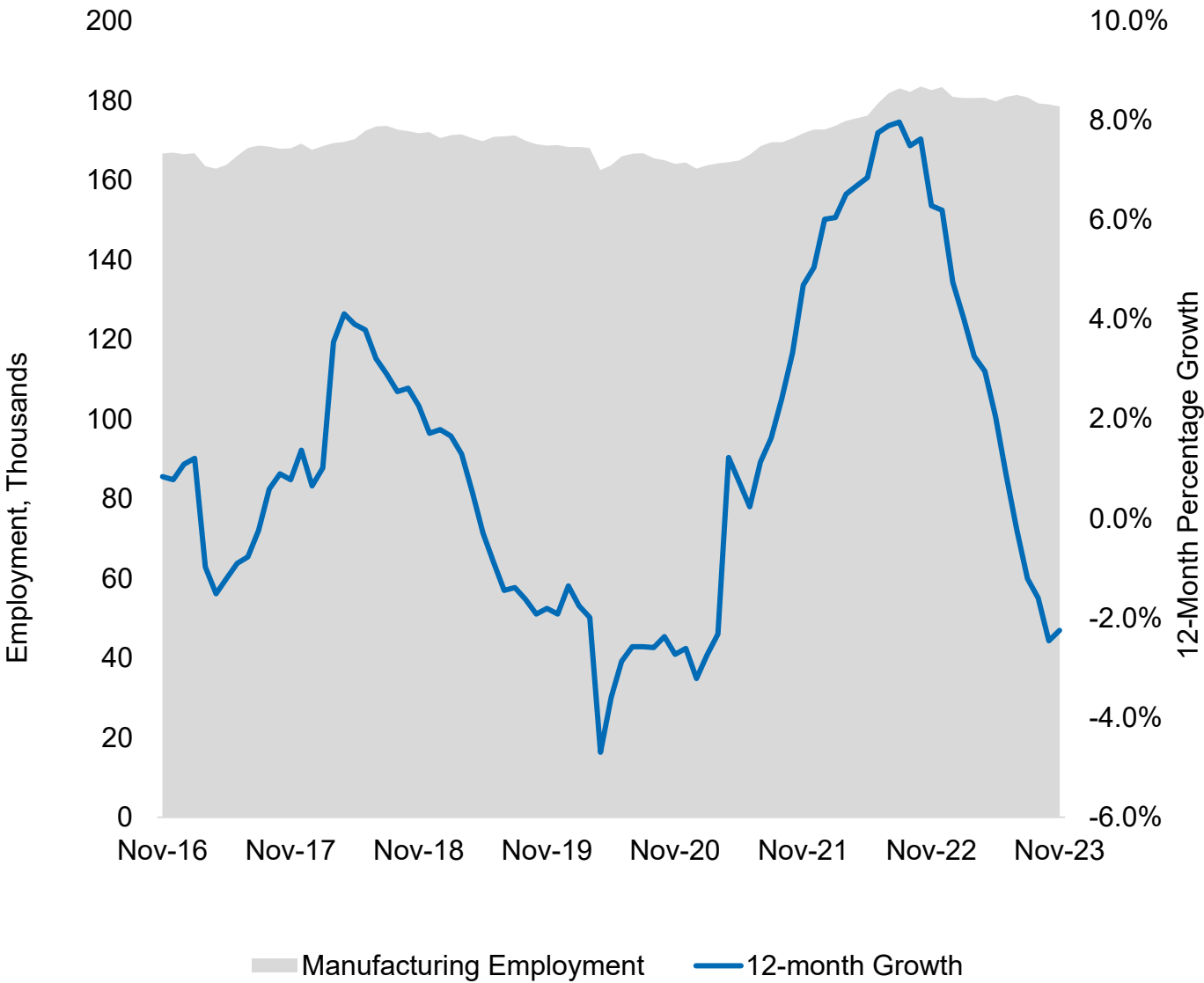
Manufacturing Sector Sees Slight Correction to 2022 Levels

Although the manufacturing sector saw impressive gains in 2022 from an increased demand for chips due to the AI boom, total employment in that sector saw a slight correction at the end of 2023, ending the year with a 2.2% decline in total employment year-over-year. Meanwhile, the trade/transportation/utilities sector saw slight growth year-over-year, with a 0.6% increase in total employment year-over-year. Given the persistent demand from the tech industry for both sectors, it's 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

4Q23

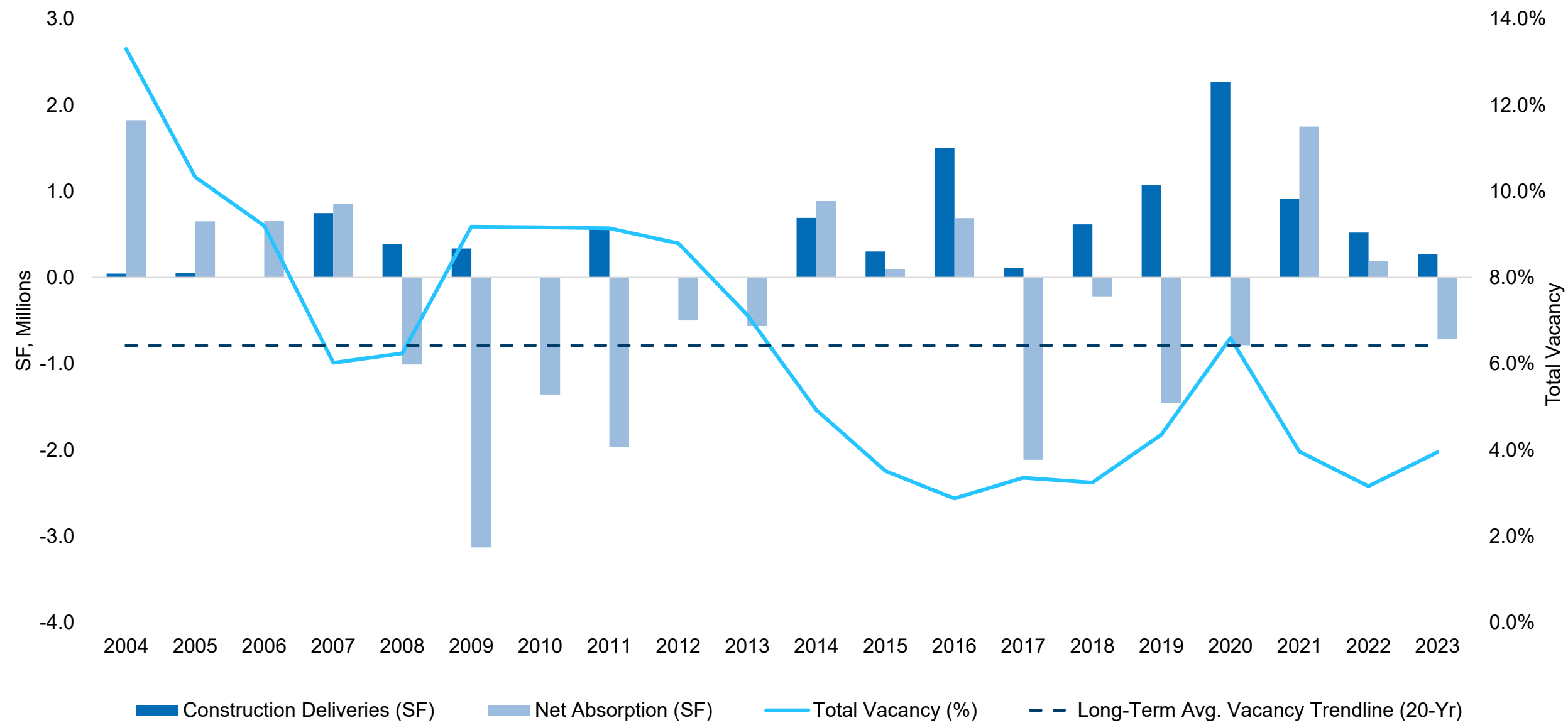
Leasing Market Fundamentals



Vacancy Remains Below Historical Average

Silicon Valley combined industrial and warehouse vacancy increased to 3.9% year-over-year, up from 3.2% in the previous year, but still below the long-term historical average of 6.2%. 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. Although 2023 saw fewer deliveries on the year compared to previous years, the pipeline remains healthy and will likely keep pace with demand.

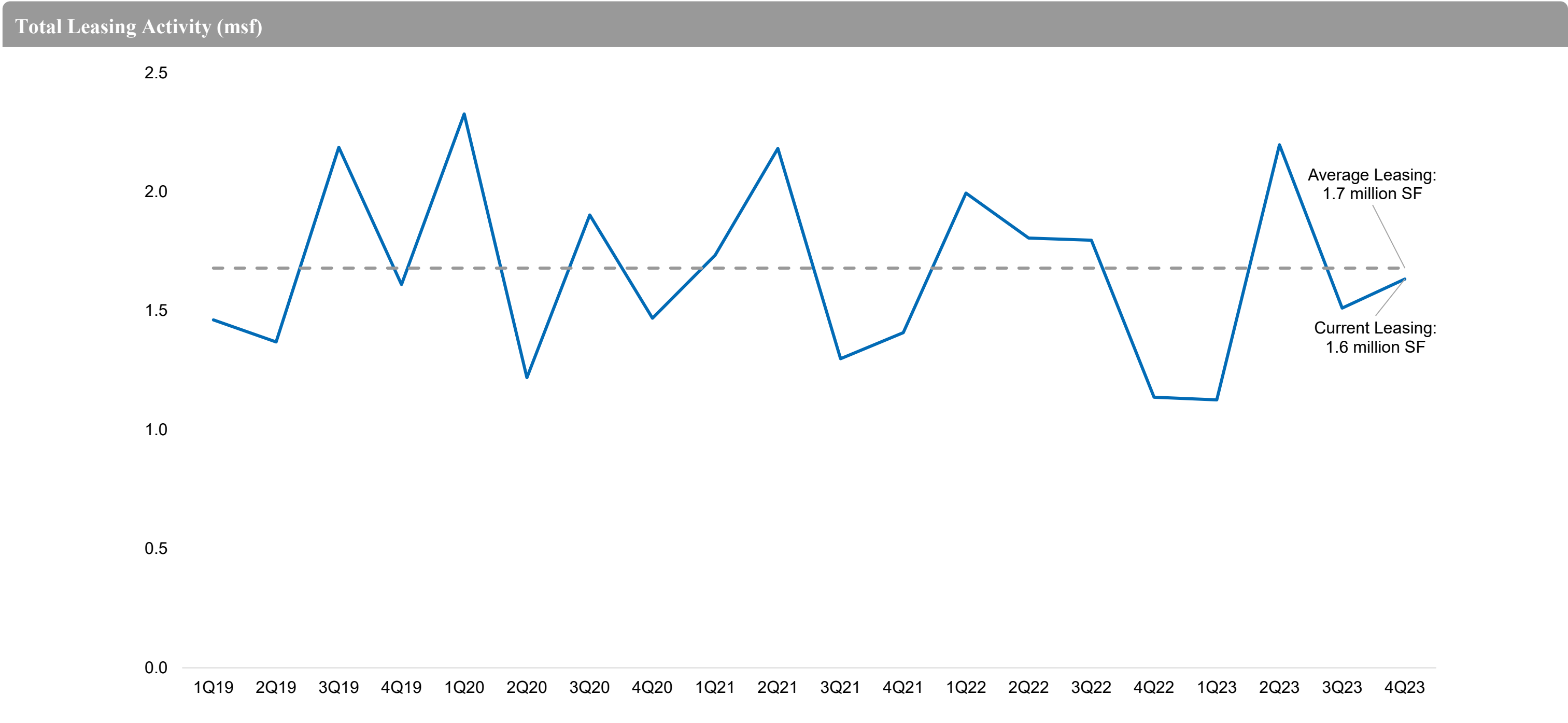
Historical Construction Deliveries, Net Absorption, and Vacancy



Source: Newmark Research

Industrial Leasing Remains Stable in Post-Pandemic Era

Industrial leasing has remained at roughly the same level in the second half of 2023, posting 1.6 million SF of leasing activity this quarter, up slightly from the previous quarter’s leasing volume of 1.5 million SF. Transaction volume has remained consistent in recent years, even throughout the pandemic, evidencing the industrial sector’s persistent demand from both manufacturing and tech users for industrial and warehouse space.

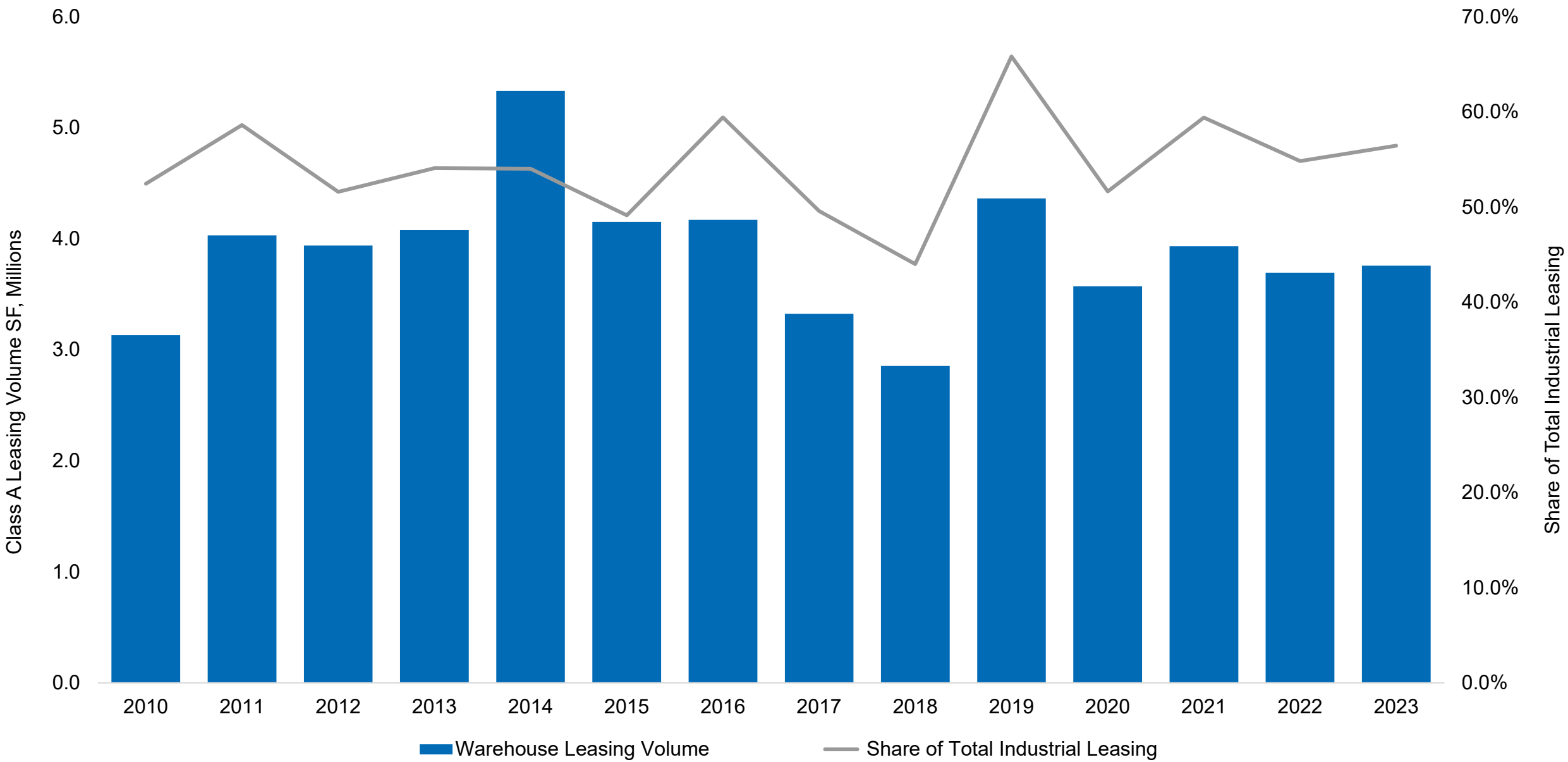


Source: Newmark Research, CoStar

Warehouse Retains 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

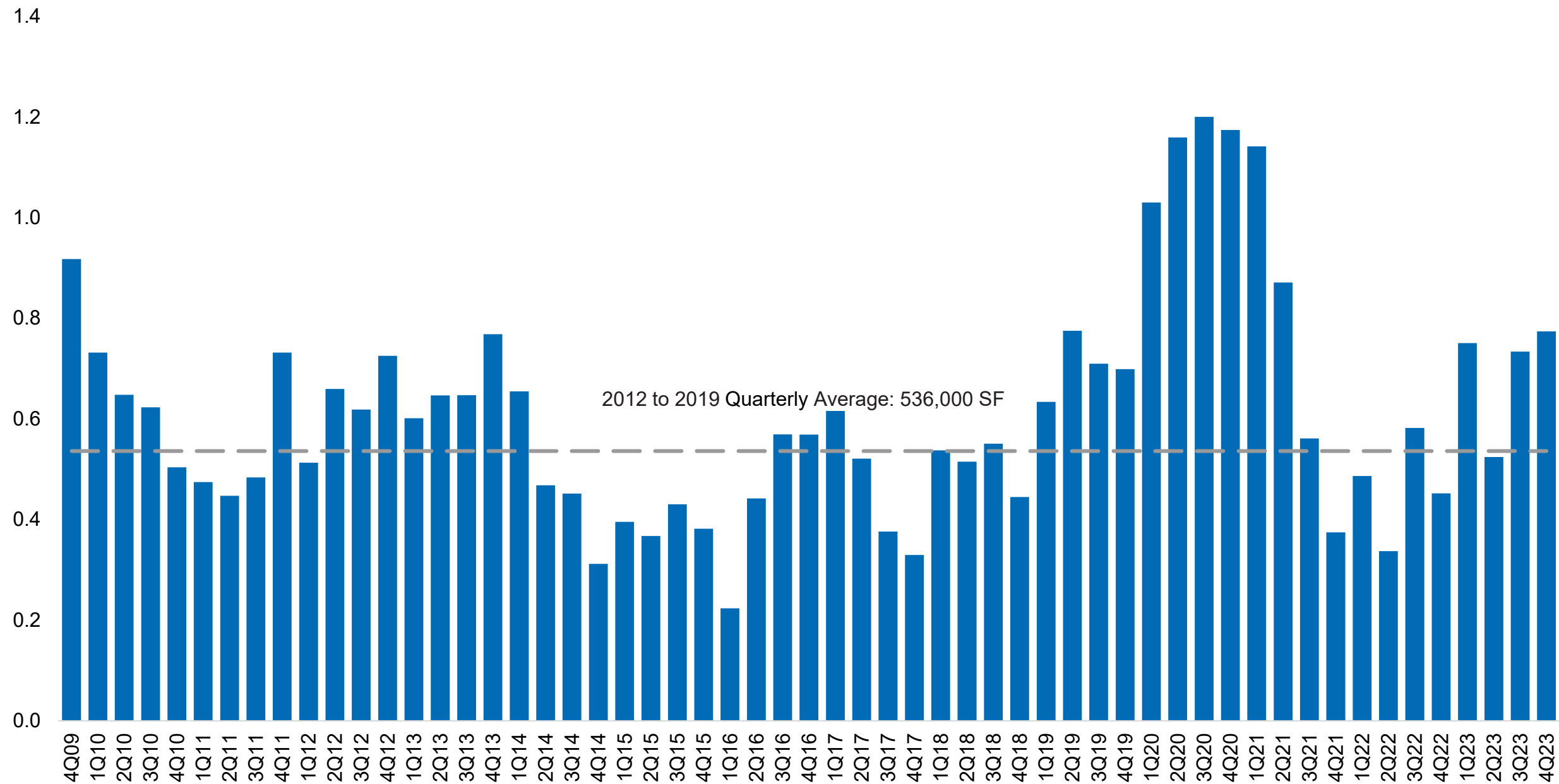


Source: Newmark Research, CoStar

Sublease Volume Increases Past Pre-Pandemic Levels

Total sublease volume rose slightly during the fourth quarter of 2023, increasing 773,745 SF, a 5.4% quarter-over-quarter. Although there were several large subleases this quarter, they were negated by other subleases hitting the market. Although the sublease market in the Valley was never very large due to consistently 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)

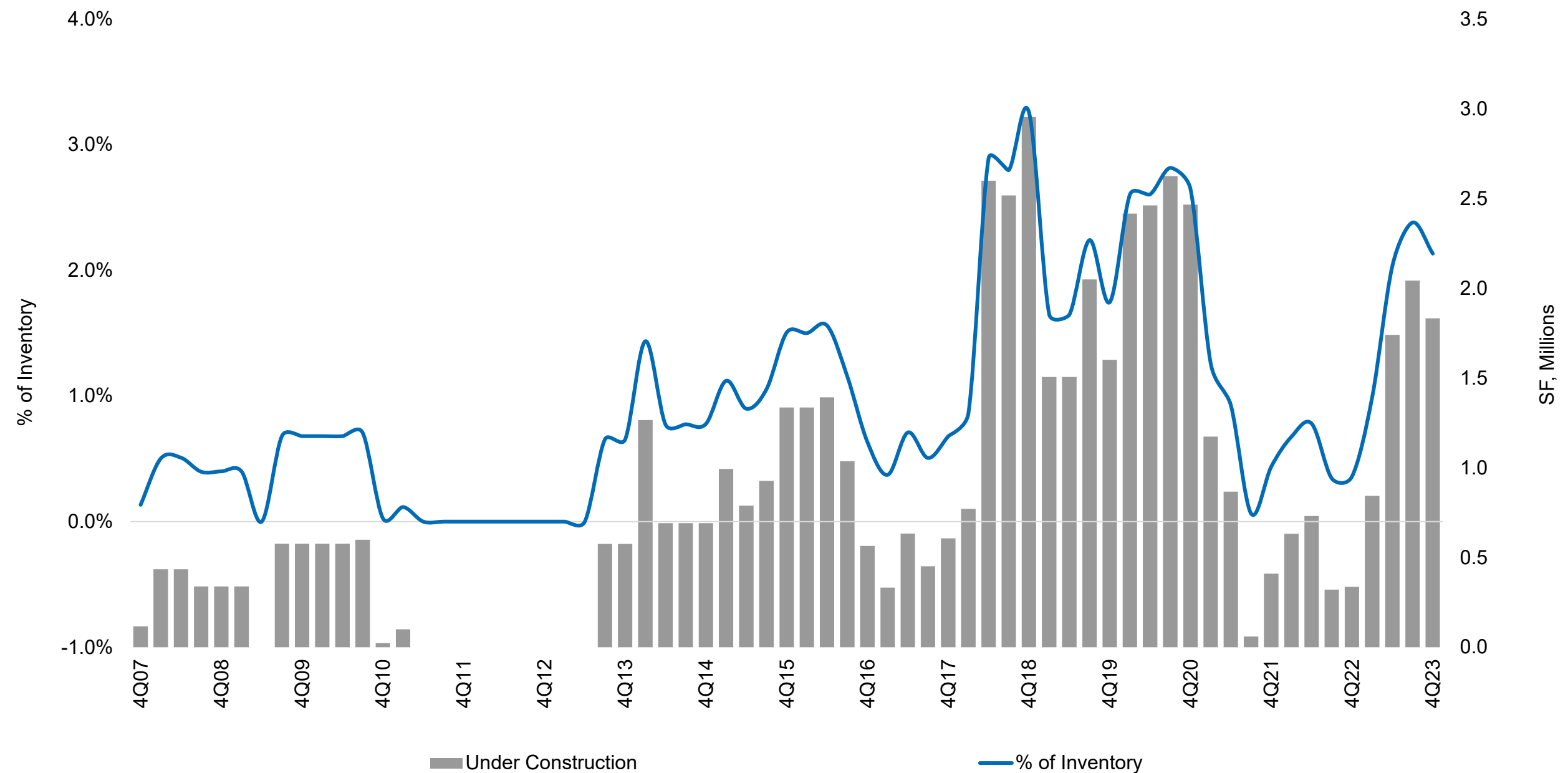


Source: Newmark Research, CoStar

Industrial Pipeline Surges Through 2023

Although no new projects broke ground this quarter, the current pipeline of 1.8 million square feet currently under construction indicates that developers anticipate a growing need for advanced manufacturing and 3PL space. Of the 1.8 million SF figure, 1.1 million SF is set to complete in 2024, with the remainder set to complete in 2025, which will in turn expand total inventory by 2.1%. These modest increases in supply have helped the industrial sector in Silicon Valley post growth consistently over the past few years.

Industrial Under Construction and % of Inventory



Source: Newmark Research, CoStar

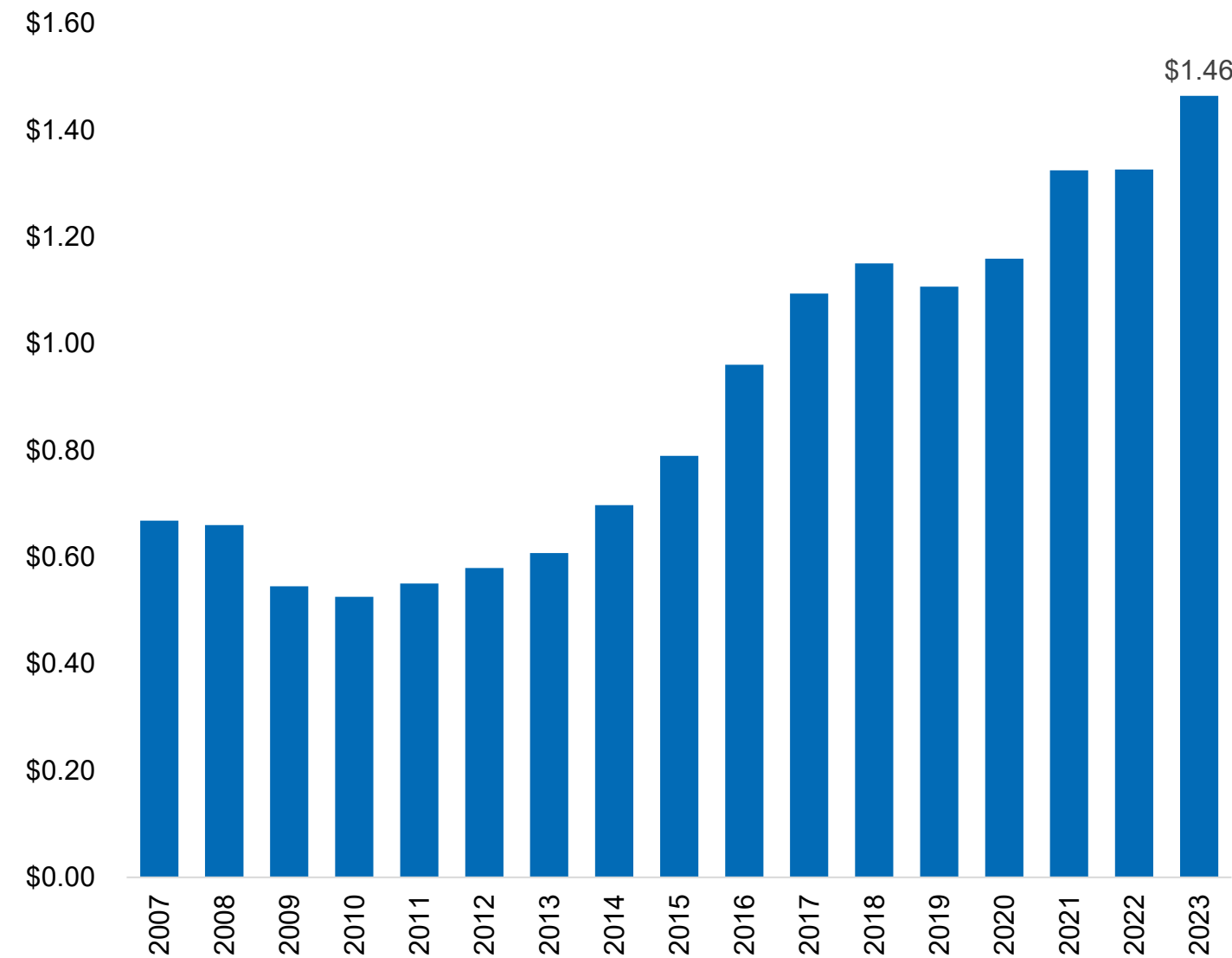


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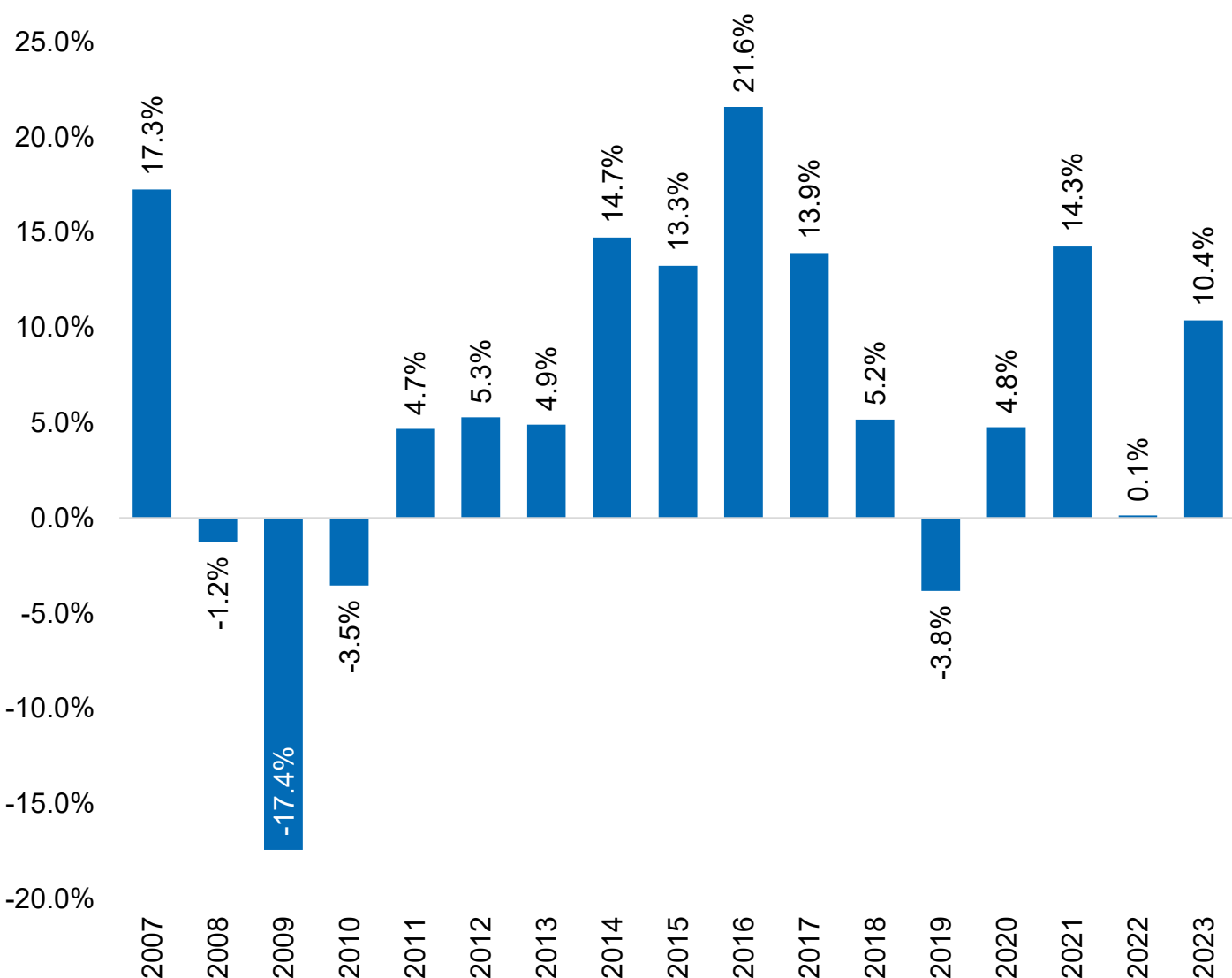
Industrial Rents Post Another Year of Growth

Industrial average asking rents continued to grow in 2023, increasing 10.4% year-over-year to \$1.46/SF. 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 push rents higher.

Industrial Average Asking Rent, \$/SF, NNN



Year-over-Year Asking Rent Growth Rate % Change



Source: Newmark Research, CoStar



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Strong Leasing Activity Compared to Office, R&D Sectors

Leasing activity picked up slightly in the fourth quarter of 2023, with gross absorption totaling 1.6 million SF, up from 1.5 million SF in the previous quarter. 2023 annual gross absorption measured 6.5 million SF. Milpitas posted the strongest quarter among all submarkets with 572,521 SF of gross absorption and capturing three of the five top deals, primarily due to DGA Services’ renewal. Overall, leasing volume remains strong in the industrial sector and is unlikely to abate soon.

Select Lease Transactions				
Tenant	Building	Submarket	Type	Square Feet
DGA Services	1001-1075 Montague Expressway	Milpitas - East 880	Renewal	386,383
Lease renewal. DGA Services renewed in 3 buildings in the Fleming Business Park. They have been in the Park since 2012, and have expanded their footprint to 386,383 SF since their original lease.				
Verdagy	7395 Morton Avenue	Newark	Sublease	123,000
Sublease. Verdagy subleased ¾ of the building from Lucid Motors. Verdagy, a tech company specializing in producing green hydrogen, is one of the many specialized users that also make use of industrial space.				
East Star Building Supply	44560 Osgood Road	Fremont - Warm Springs	New Lease	87,592
New lease. East Star leased this freestanding warehouse building in Fremont, expanding its footprint in Fremont.				
CRST Specialized Transportation	881 Wrigley Way	Milpitas - East 880	Renewal	84,000
Lease renewal. This 3PL tenant has been in this location since 2019.				
Valley Relocation	776-800 S Milpitas Boulevard	Milpitas - East 880	New Lease	72,576
New lease. Prologis terminated an existing lease on the space to lease this space to Valley Relocation directly.				

Source: Newmark Research

4Q23

Appendix / Tables





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