



ANNUAL JOB GROWTH

San Diego created 29,300 net new jobs in the 12 months ending May 2014, led by employment gains in the Leisure & Hospitality, Construction, Professional & Business Services and Education & Health Services sector.



12-MO DIRECT NET ABSORPTION

Class A properties have witnessed the bulk of the occupancy gains, with North San Diego, I-5 Corridor and Downtown accounting for 81% of the absorption growth within the past year.



DIRECT VACANCY RATE

Since peaking at 18.8% at the beginning of 2010, the countrywide direct vacancy rate has dropped to a six-year low. Class A direct vacancy levels have dropped to their lowest level since 2005.



OVERALL RENTS

Overall asking rents are up 5.1% over the past 12 months, but must overcome a 16% deficit in order to restore rents to their cyclical peak of \$2.86 per sq. ft. recorded early in 2008. Asking rents are projected to reach their pre-recessionary levels in 2016.



UNDER CONSTRUCTION

Over the past five years, office construction has primarily been limited to build-to-suit and owner/user development. However, the return of pre-recession vacancy levels and obsolescence should prompt more developers to re-position existing buildings and move forward with speculative development.



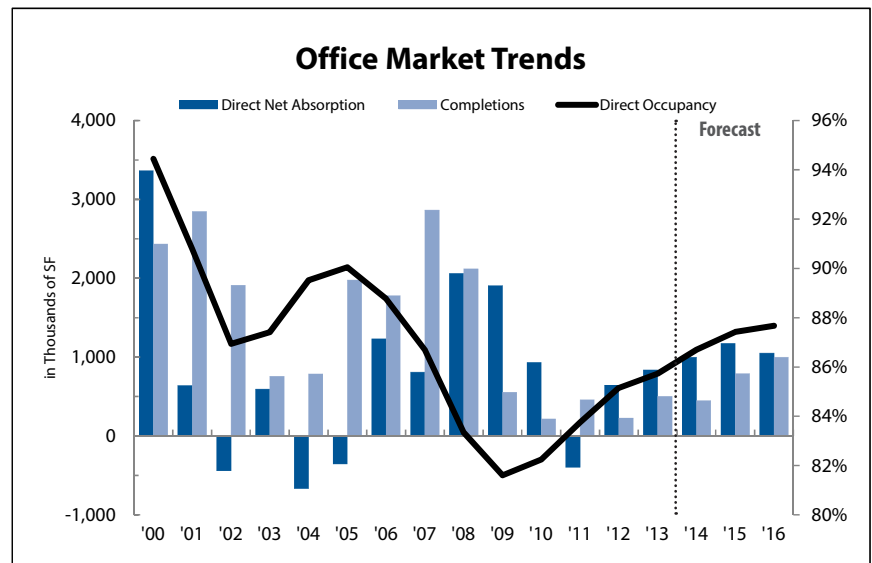
*Arrows represent change from previous 12 months

CLASS A VACANCY HITS LOWEST LEVEL SINCE 2005

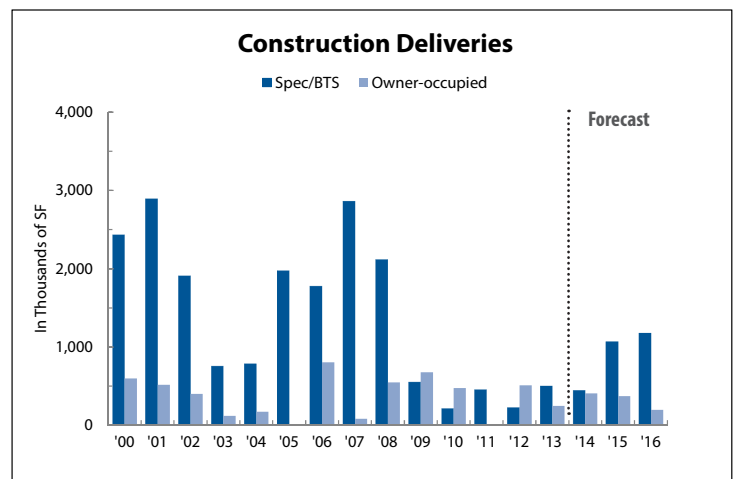
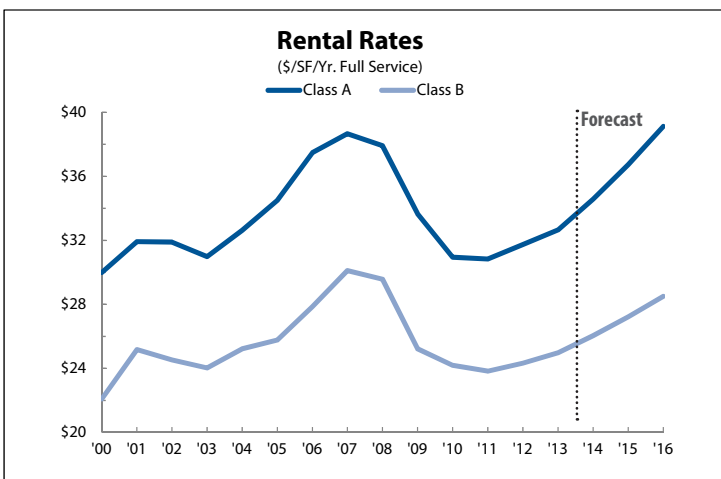
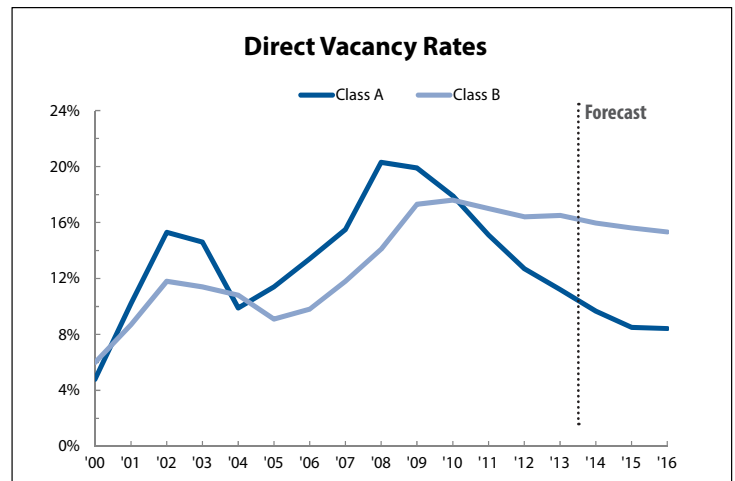
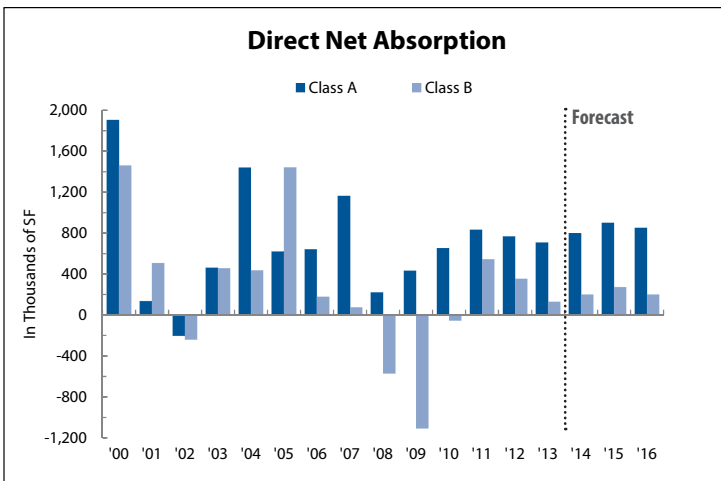
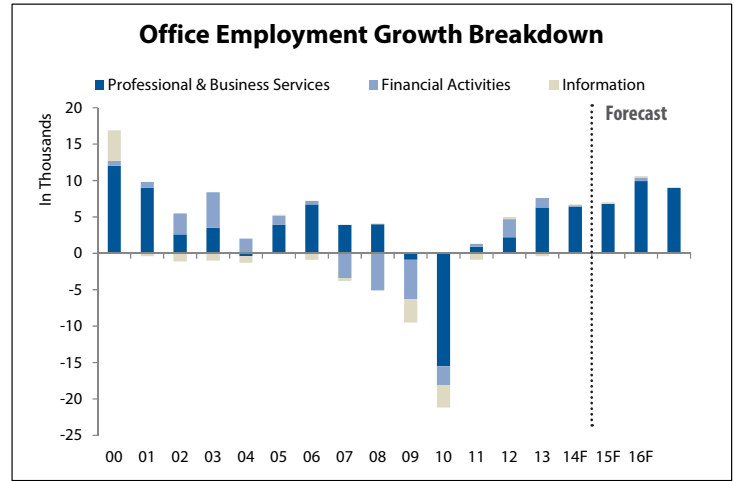
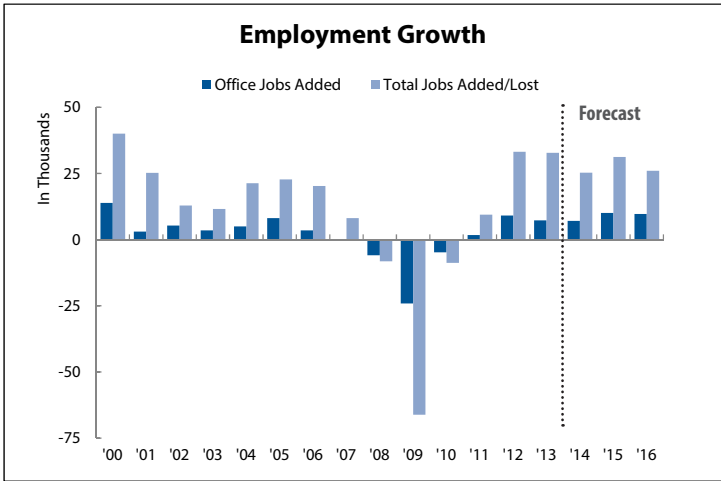
San Diego's economic expansion is well underway as sustained job growth continued to outpace the annual growth rates for the state and national level. Economic growth in San Diego has remarkably created 129,400 jobs since its post-recessionary trough in January 2010, pushing the total nonfarm employment level to a record high. As a result of the widespread growth, San Diego's unemployment rate has declined 150 basis points to 5.8% within the past 12 months. Looking ahead, employment payrolls are projected to increase by 25,330 jobs in 2014, with the pace expected to accelerate with the strong addition of 31,250 jobs in 2015, which will outpace the 20-year historical average of 1.5%.

San Diego's office leasing market has exhibited moderate occupancy gains, with an average of 1.1 million sq. ft. absorbed per year since 2011. The Class A office market recorded solid occupancy gains totaling 637,406 sq. ft. during the second quarter, bringing the trailing 12-month total to 920,228 sq. ft. As a result of the solid leasing gains, Class A direct vacancy rates have dropped by 180 basis points to 10.4% within the past 12 months, reaching their lowest level since 2005. However, the Class B properties exhibited 298,122 sq. ft. of occupancy losses during the quarter, as tenants sought out higher quality space options. Consequently, Class B vacancy rates ended the quarter at 16.9%, up 80 basis points from the prior quarter. In terms of new supply, a joint venture between Hines and JPMorgan recently completed La Jolla Commons Tower II, a 414,575 sq. ft. Class A building, fully pre-leased to LPL Financial. Also worth noting, The Irvine Company recently broke ground on One La Jolla Center, a speculative development consisting of 305,952 sq. ft. of Class A space in the UTC submarket. Due to the improved economy spurring leasing demand, Class A full-service gross asking rents increased by 6.8% to \$2.86 while Class B rents appreciated by 4.3% to \$2.16 per sq. ft. within the past 12 months.

San Diego's office market fundamentals will continue to strengthen with steady absorption growth outpacing modest construction deliveries, which will help push the overall vacancy rate down to 13.4% by year-end 2014. Leasing demand will be driven by sustained growth in office-using employment sectors, specifically in the technology and life sciences sub-sectors. With Class A vacancy levels reaching their lowest level since 2005 and limited large contiguous blocks of high quality space available in the market, additional office development could break ground in the year ahead. However, future demand growth is expected to continue outpacing new supply over the next few years.



HISTORICAL TRENDS & FORECAST



SUBMARKET STATISTICS

Submarket	Total Inventory SF	TOTAL SPACE AVAILABLE		DIRECT VACANCY RATES		DIRECT NET ABSORPTION		OVERALL RENTAL RATES		
		Direct Available	Sublease Available	Direct Vacancy	Y-O-Y Change	Current Qtr.	Rolling 12-Month	Avg Rents PSF/Yr	Avg Rents PSF/Mo.	Y-O-Y % Change
Downtown	10,348,016	1,864,840	216,494	16.0%	-0.8%	130,689	86,329	\$27.37	\$2.28	4.07%
Class A	6,168,645	827,011	179,932	11.5%	-2.7%	131,481	168,403	\$29.79	\$2.48	6.24%
Class B	4,179,371	1,037,829	36,562	22.6%	2.0%	(792)	(82,074)	\$25.16	\$2.10	4.40%
Central San Diego	13,926,465	2,015,789	354,195	11.7%	-1.4%	51,770	197,295	\$25.97	\$2.16	8.93%
Class A	4,264,522	533,291	261,752	8.0%	-2.8%	44,891	118,522	\$32.43	\$2.70	10.72%
Class B	9,661,943	1,482,498	92,443	13.3%	-0.8%	6,879	78,773	\$23.41	\$1.95	6.99%
North San Diego	18,319,760	3,082,574	974,209	14.3%	2.8%	78,852	(154,461)	\$31.43	\$2.62	7.31%
Class A	7,946,502	794,992	487,483	6.9%	-0.2%	414,698	398,831	\$39.40	\$3.28	4.79%
Class B	10,373,258	2,287,582	486,726	19.9%	5.3%	(335,846)	(553,292)	\$27.08	\$2.26	6.45%
I-15 Corridor	8,392,981	1,382,070	93,010	15.8%	3.6%	(106,935)	(3,278)	\$27.35	\$2.28	3.68%
Class A	3,825,462	411,902	19,967	11.3%	4.3%	(30,386)	59,528	\$31.33	\$2.61	3.33%
Class B	4,567,519	970,168	73,043	19.5%	3.4%	(76,549)	(62,806)	\$26.22	\$2.18	4.63%
SR-78 Corridor	2,178,660	491,770	3,016	20.9%	3.6%	(31,994)	(78,240)	\$24.59	\$2.05	-5.57%
Class A	554,919	155,538	3,016	27.5%	4.3%	(25,848)	(23,831)	\$31.60	\$2.63	-3.92%
Class B	1,623,741	336,232	0	18.7%	3.4%	(6,146)	(54,409)	\$21.24	\$1.77	-10.49%
I-5 Corridor	10,769,765	1,847,543	325,512	13.4%	-4.7%	152,332	319,560	\$33.57	\$2.80	4.64%
Class A	5,051,020	894,284	223,635	12.5%	-2.4%	93,970	176,894	\$38.35	\$3.20	6.71%
Class B	5,718,745	953,259	101,877	14.3%	-5.3%	58,362	142,666	\$30.29	\$2.52	3.98%
South Bay	2,089,683	395,132	2,144	18.8%	-4.7%	46,090	98,003	\$23.77	\$1.98	0.85%
Class A	433,156	147,735	2,144	33.4%	-2.4%	6,308	10,352	\$27.25	\$2.27	6.03%
Class B	1,656,527	247,397	0	15.0%	-5.3%	39,782	87,651	\$22.17	\$1.85	-2.38%
East County	1,436,213	90,370	2,788	4.6%	-1.2%	18,480	17,360	\$27.62	\$2.30	-5.35%
Class A	233,830	18,438	0	7.1%	-4.9%	2,292	11,529	\$30.07	\$2.51	6.74%
Class B	1,202,383	71,932	2,788	4.1%	-0.5%	16,188	5,831	\$26.64	\$2.22	-12.20%

San Diego Totals	Total Inventory SF	TOTAL SPACE AVAILABLE		DIRECT VACANCY RATES		DIRECT NET ABSORPTION		OVERALL RENTAL RATES		
		Direct Available	Sublease Available	Direct Vacancy	Y-O-Y Change	Current Qtr.	Rolling 12-Month	Avg Rents PSF/Yr	Avg Rents PSF/Mo.	Y-O-Y % Change
Class A	28,478,056	3,783,191	1,177,929	10.4%	-1.8%	637,406	920,228	\$34.29	\$2.86	6.79%
Class B	38,983,487	7,386,897	793,439	16.9%	1.1%	-298,122	(437,660)	\$25.87	\$2.16	4.31%
Overall	67,461,543	11,170,088	1,971,368	14.2%	-0.1%	339,284	482,568	\$28.82	\$2.40	5.11%

METHODOLOGY

Total Inventory: The total inventory includes all single and multi-tenant leased office buildings with at least 20,000 square feet of gross rentable square footage.

Total Space Available: Available space currently being marketed which is either physically vacant or occupied.

Direct Space Available: Space that is being offered for lease directly from the landlord or owner of a building. Under construction space is not included in space available figures.

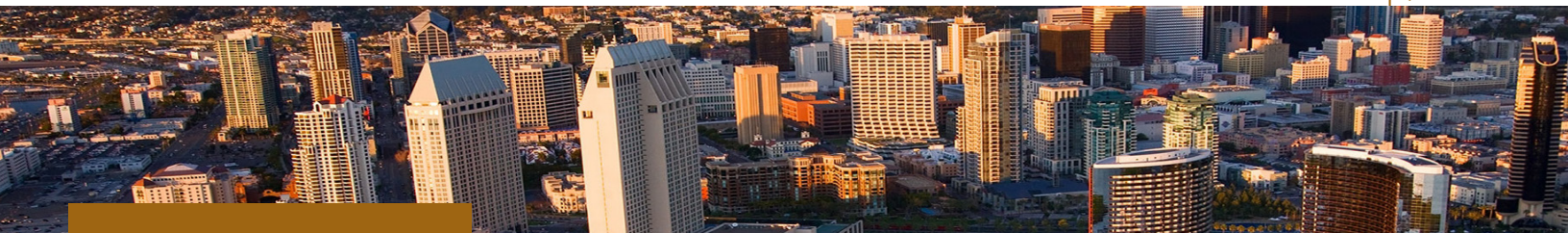
Sublease Space Available: Space that has been leased by a tenant and is being offered for lease back to the market by the tenant with the lease obligation.

Direct Vacancy Rate: Direct space physically vacant divided by the total rentable inventory.

Direct Net Absorption: The net change in occupied direct space over a given period of time.

Under Construction: Office buildings which have commenced construction as evidenced by site excavation or foundation work.

Direct Asking Rents: The quoted full-service asking rent for available space expressed in dollars per sq. ft.



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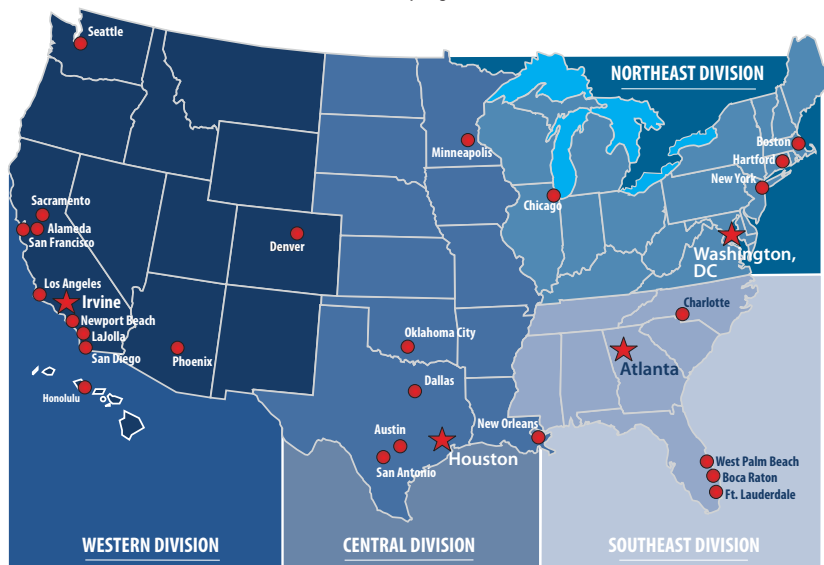
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