

An aerial photograph of the San Francisco Peninsula, showing a dense urban area with numerous office buildings, parking lots, and a complex highway interchange. The Golden Gate Bridge is visible in the distance, spanning across the water. The sky is clear and blue.

AVISON
YOUNG

San Francisco Peninsula Office Insight Report

Q2 2021

AVANT
by AVISON YOUNG

Key takeaways



Economic conditions

- Reopening efforts and higher vaccination rates have allowed the San Francisco Peninsula unemployment rate to rebound from a high of 11.8 percent to **4.8 percent**.



Recovery rate

- The overall U.S. post-COVID rate of recovery based on extrapolated cell phone data is **49.1 percent**.
- The overall rate of recovery in the Bay Area is comparatively higher at **65.7 percent**.
- However, the return of Bay Area office occupiers has lagged other primary markets given the concentration of tech and a lack across the sector of requiring workers back in the office. The rate of recovery across the Bay Area office market is **10.2 percent** compared to the U.S. average of 19.2 percent.



Office demand

- Leasing activity has paused, decreasing by **75.6 percent** compared with near-term historical averages.
- Occupancy losses have increased totaling almost **1 million sf** over the past 18 months.

Key takeaways



Office supply

- Direct and sublease vacancy have risen to recent highs of **9.2 percent**.
- The sublease market continues to drag aggregate fundamentals, accounting for **1.4 msf** of available space. However, some prospective sublandlords have pulled their space from the market after unsuccessfully capturing demand by subtenants.



Pricing trends

- Net effective rents decreased by **3.8 percent** over the first half of 2021 as landlords induced tenant commitments through increasing concessions packages and favorable lease provisions while keeping rents relatively steady.
- Demand is starting to increase as the economy reopens and tenants that postponed their long-term occupancy strategies re-enter the market.



Capital markets

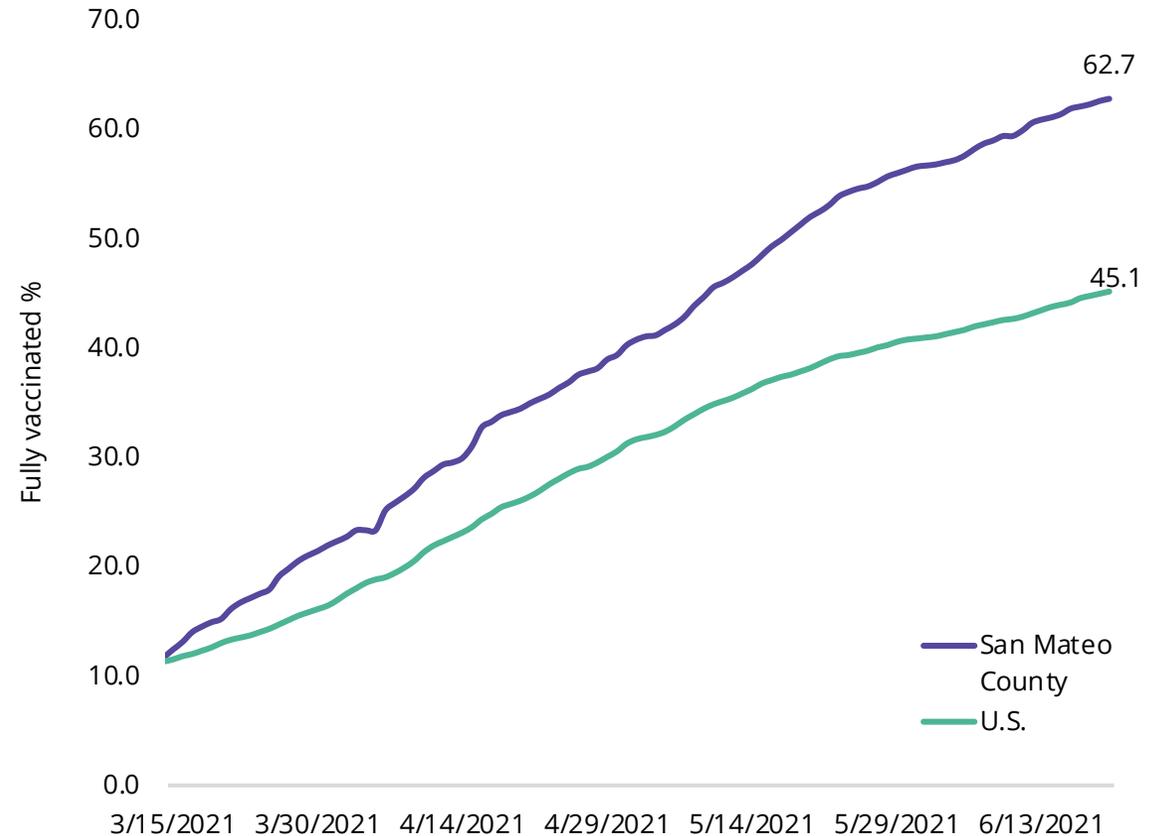
- The market has entered a risk-pricing crisis despite continued record levels of dry powder. As a result, only **\$1.06B** of Peninsula offices have been sold since 2020, a decrease of **40 percent** compared with the prior five-year average.
- Asset pricing has stabilized and mirrors pre-pandemic levels with sales pricing averaging around **\$700 psf**.

Vaccination rates

62.7%

Share of total San Mateo County population that is fully vaccinated

Manhattan proportionate vaccination rates have far surpassed U.S. averages, an important metric that has allowed the city to loosen restrictions.



Source: CDC

Employment and unemployment rate

4.8%

San Mateo County unemployment rate as of April 2021, marking a staggering recovery from the peak of the pandemic

Historically tightened labor market conditions were halted by the pandemic with nearly 72,000 job losses between February and May 2020. However, reopening efforts enabled the economy to add 6.9% jobs since May 2020.



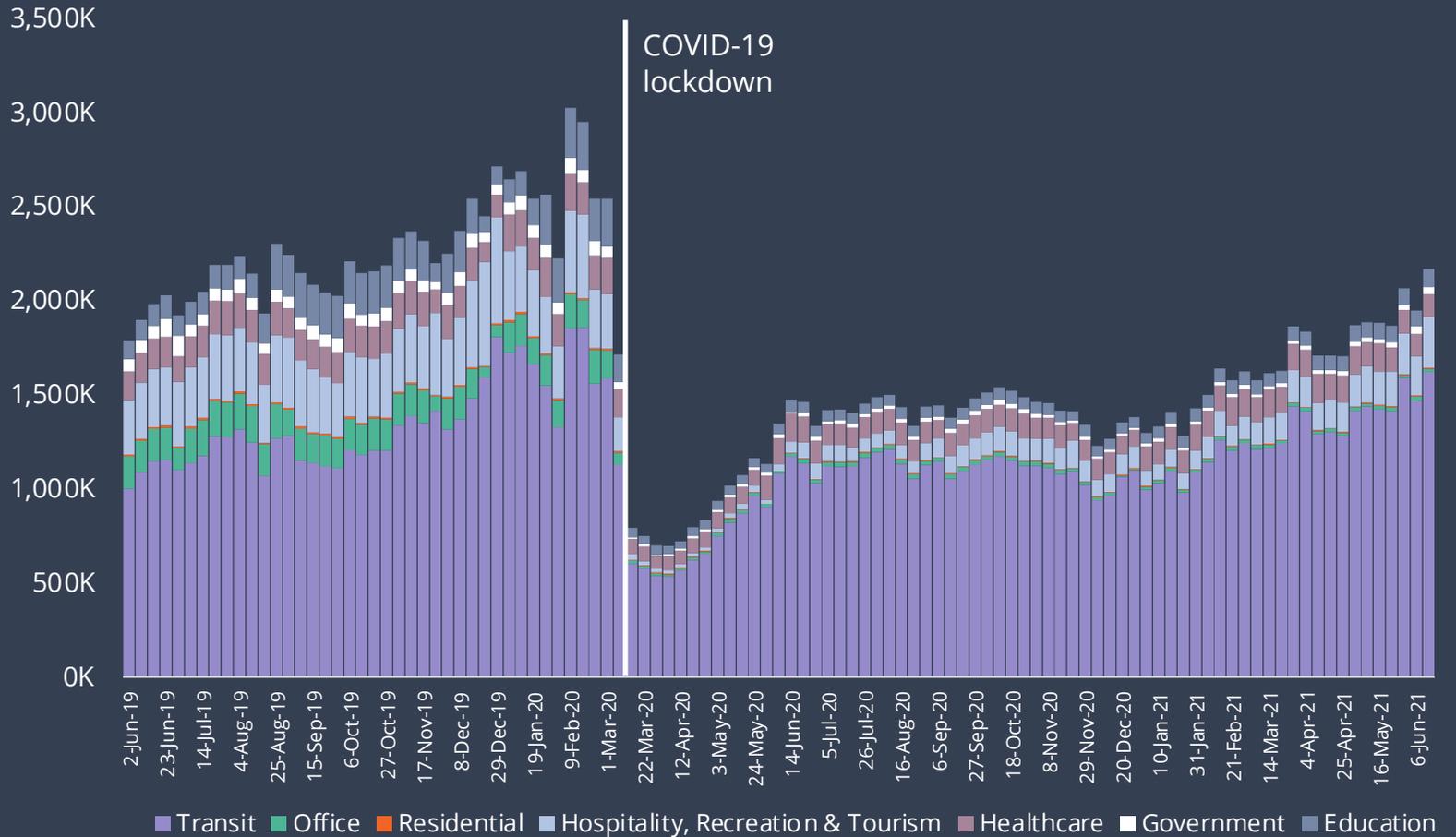
Note: Not seasonally adjusted data.
Source: Bureau of Labor Statistics

Bay Area recovery index

65.7%

Post-COVID rate of recovery based on representative locations through 6/20/2021

Activity levels have escalated in recent months and continue to trend upward. Activity has increased by 47% year-over-year, underpinned by strong growth in hospitality (+353%) and government (+239%).



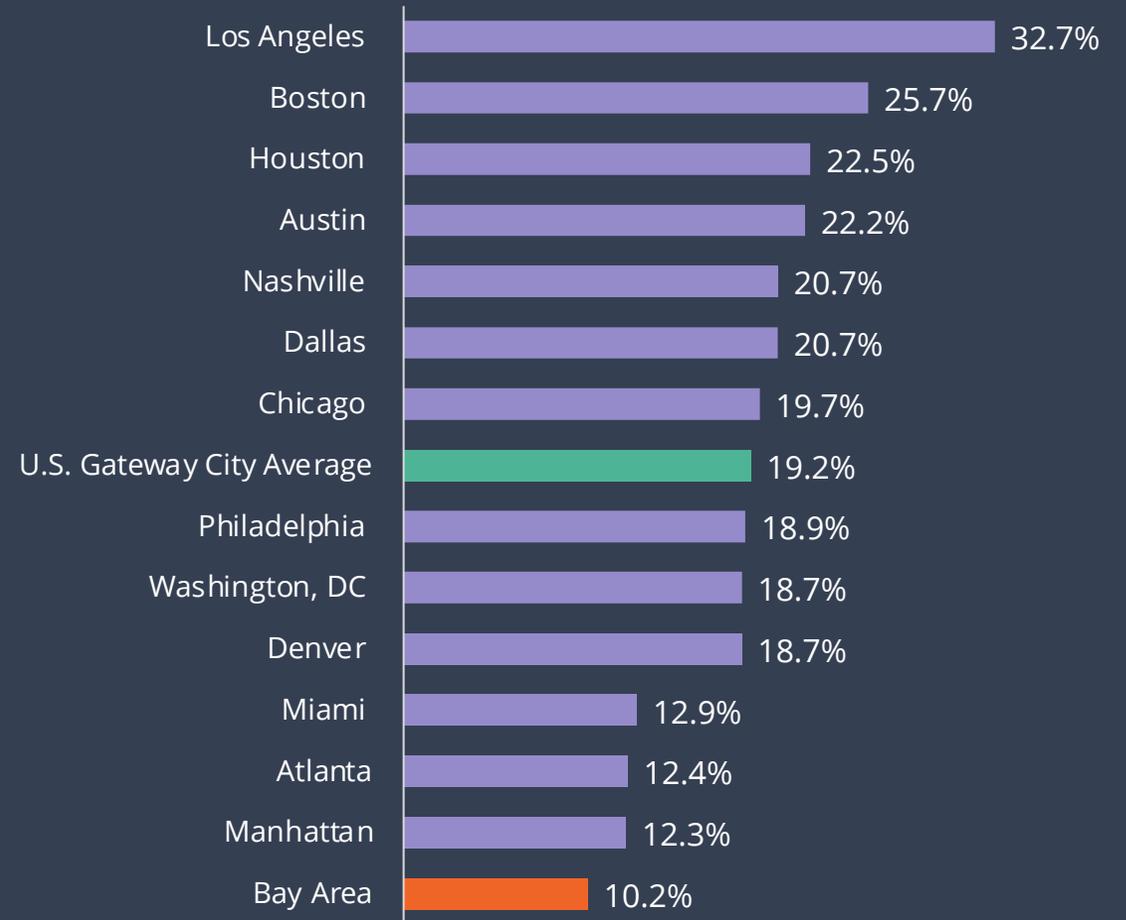
Note: Representative areas of interest.
Pre-COVID period measured as 12/1/2019 to 3/8/2020.
Post-COVID period measured as 3/15/2020 to 6/20/2021.
Source: Orbital Insights, AVANT by Avison Young

Bay Area office recovery vs. U.S. gateway cities

10.2%

Post-COVID rate of recovery for Bay Area office employers

Bay Area office employers have been comparatively hesitant to return to the office, as measured by the lowest recovery rate among U.S. gateway cities.



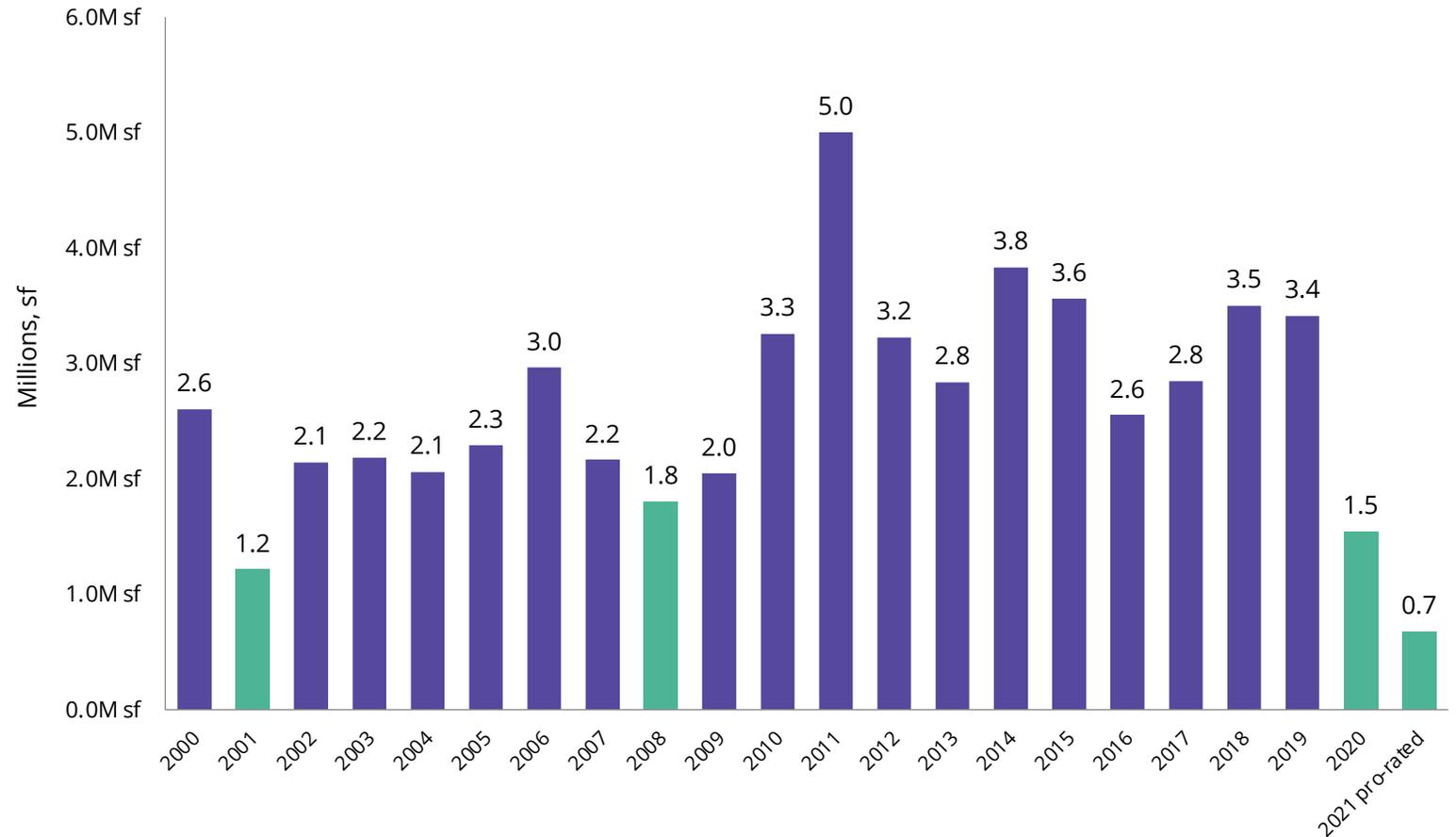
Note: Select, representative occupiers only. Weekdays only.
Pre-COVID period measured as 6/1/2019 to 3/14/2020.
Post-COVID period measured as 3/15/2020 to 6/20/2021.
Source: Orbital Insights, AVANT by Avison Young

Office leasing activity

-75.6%

2021-pro-rated vs. prior 20-year annual average leasing activity

There is no modern precedent for the post-COVID slowdown in leasing activity—not 2001 nor 2008—due to the sudden change in office occupiers’ future workplace strategies and the 2020 recession.



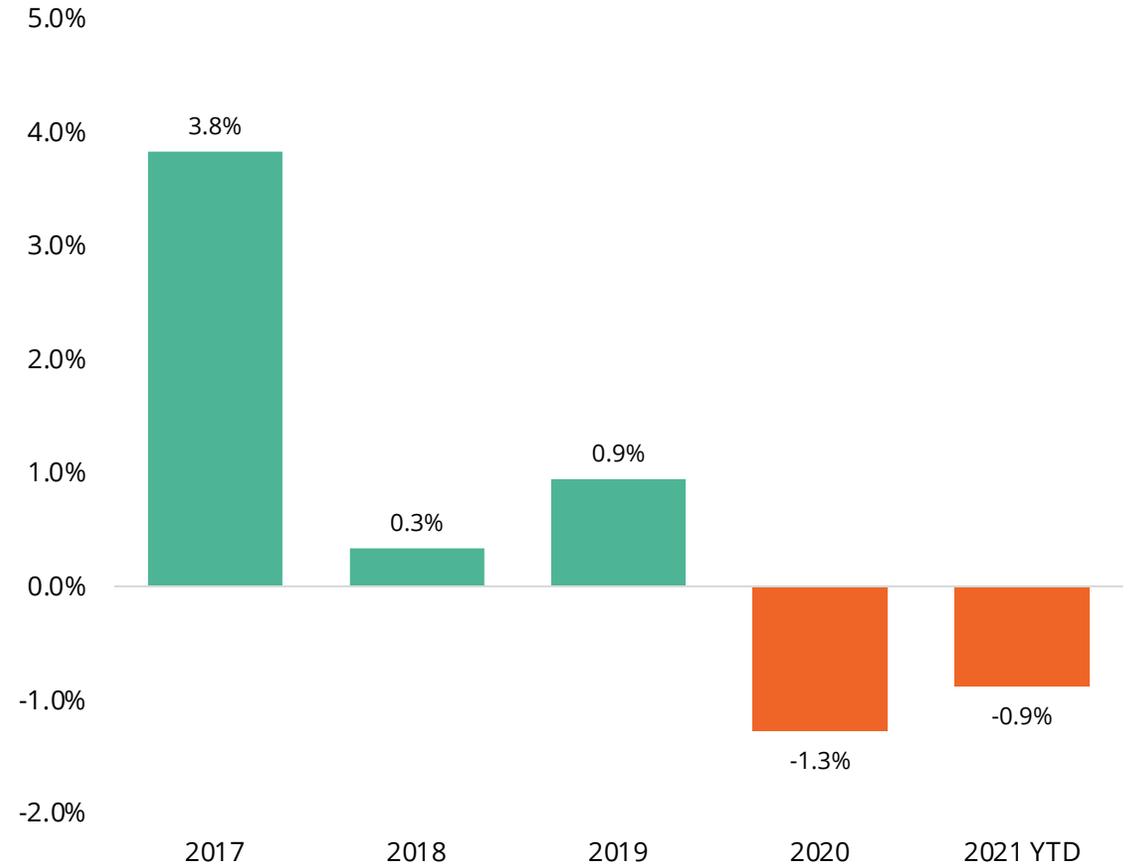
Source: AVANT by Avison Young

Absorption

-0.9%

Net absorption as a percentage of inventory, 2021 YTD

Occupancy losses have totaled almost 1 million sf over the past 18 months



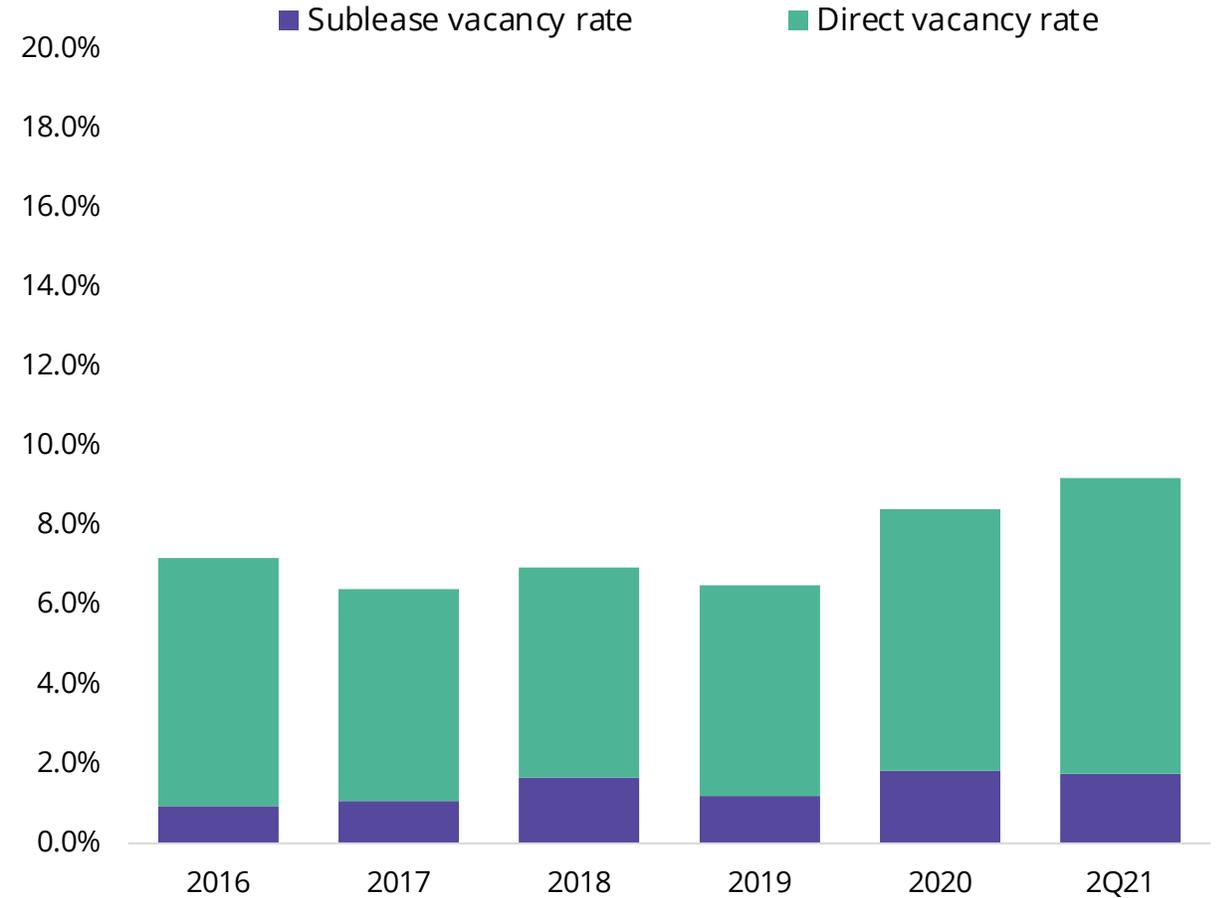
Source: AVANT by Avison Young

Vacancy rate

9.2%

Near-term high Peninsula vacancy as of Q2 2021

Vacancy continued to rise jumping from 9.2% in Q2 from 8.4% at YE 2020. The ratio of sublease-to-total vacancy is currently 24%.



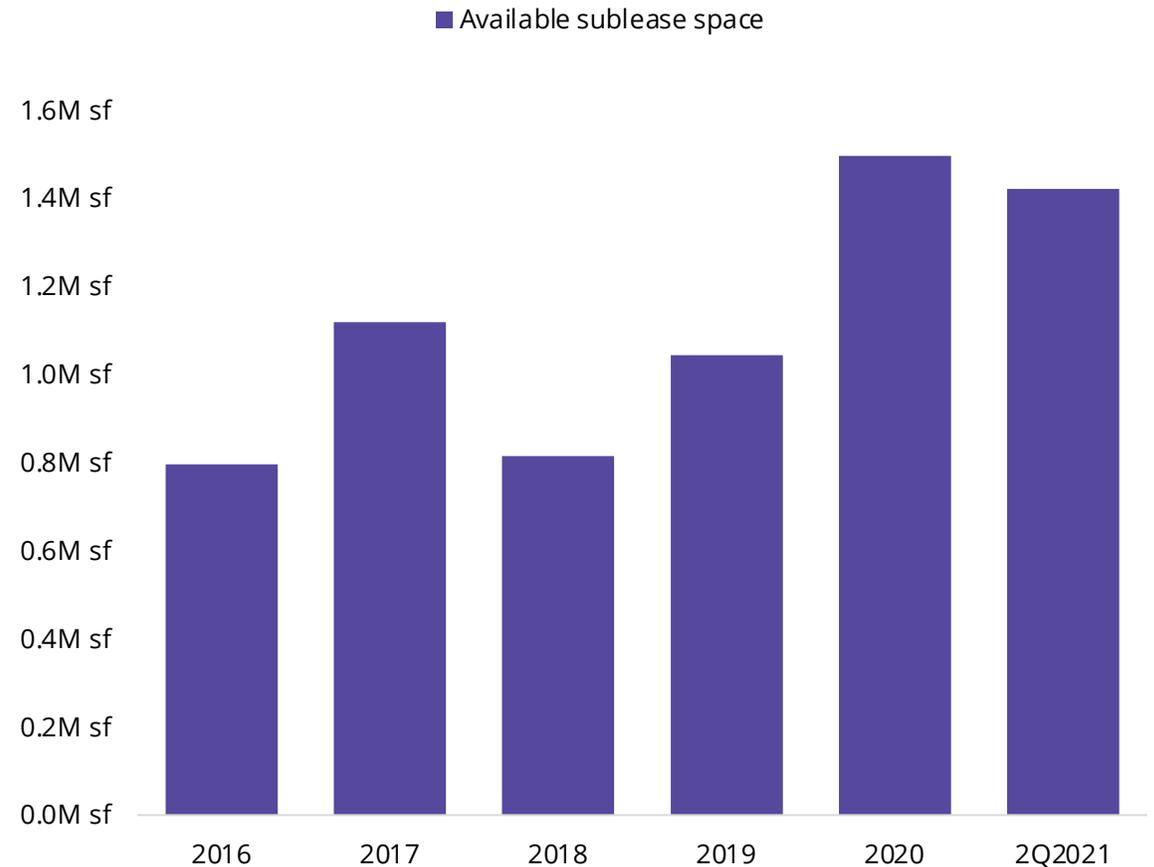
Source: AVANT by Avison Young

Available sublease space

1.4 msf

Of available sublease space

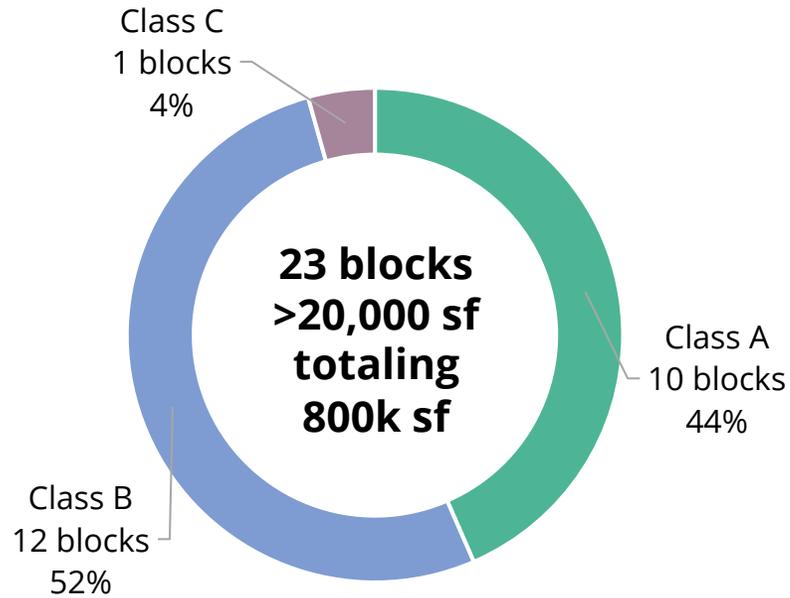
Sublease space has increased by 36% over the past 18 months as tenants have listed their space for sublease while contemplating the future of their office footprints.



Source: AVANT by Avison Young

Sublease supply pipeline

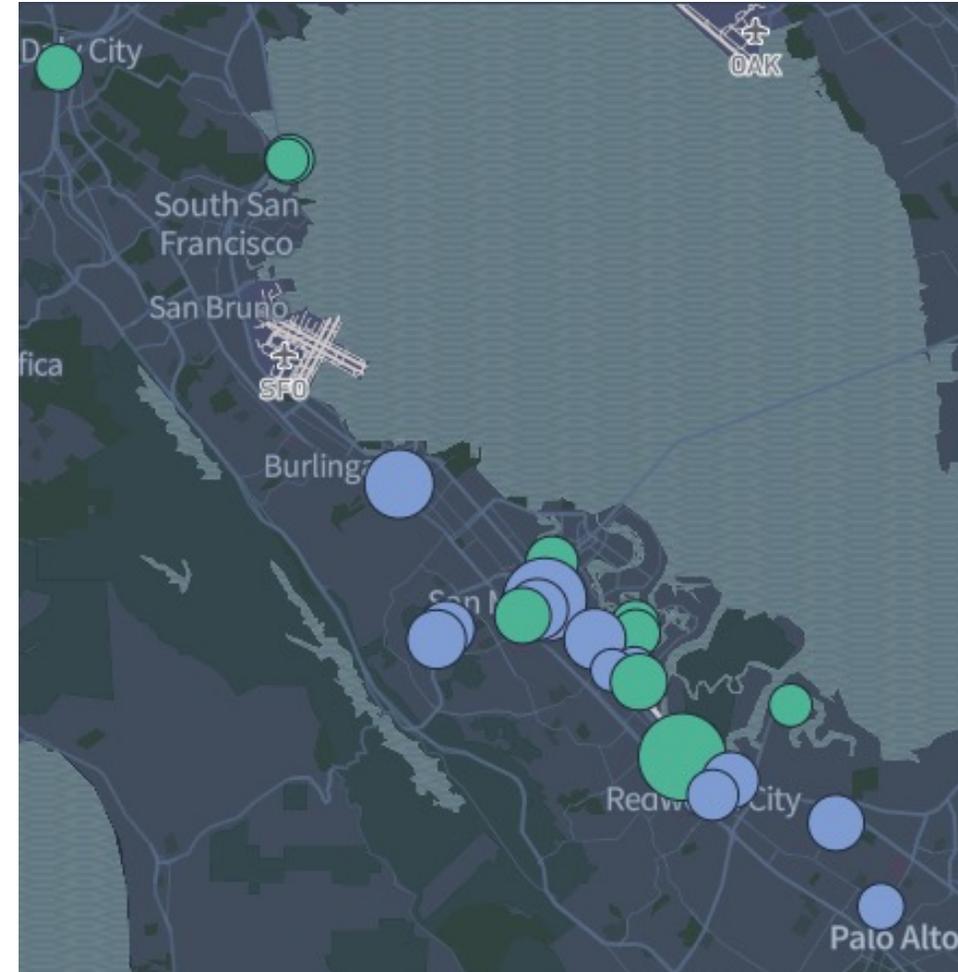
Building classification



Asking rent per square foot



Source: AVANT by Avison Young

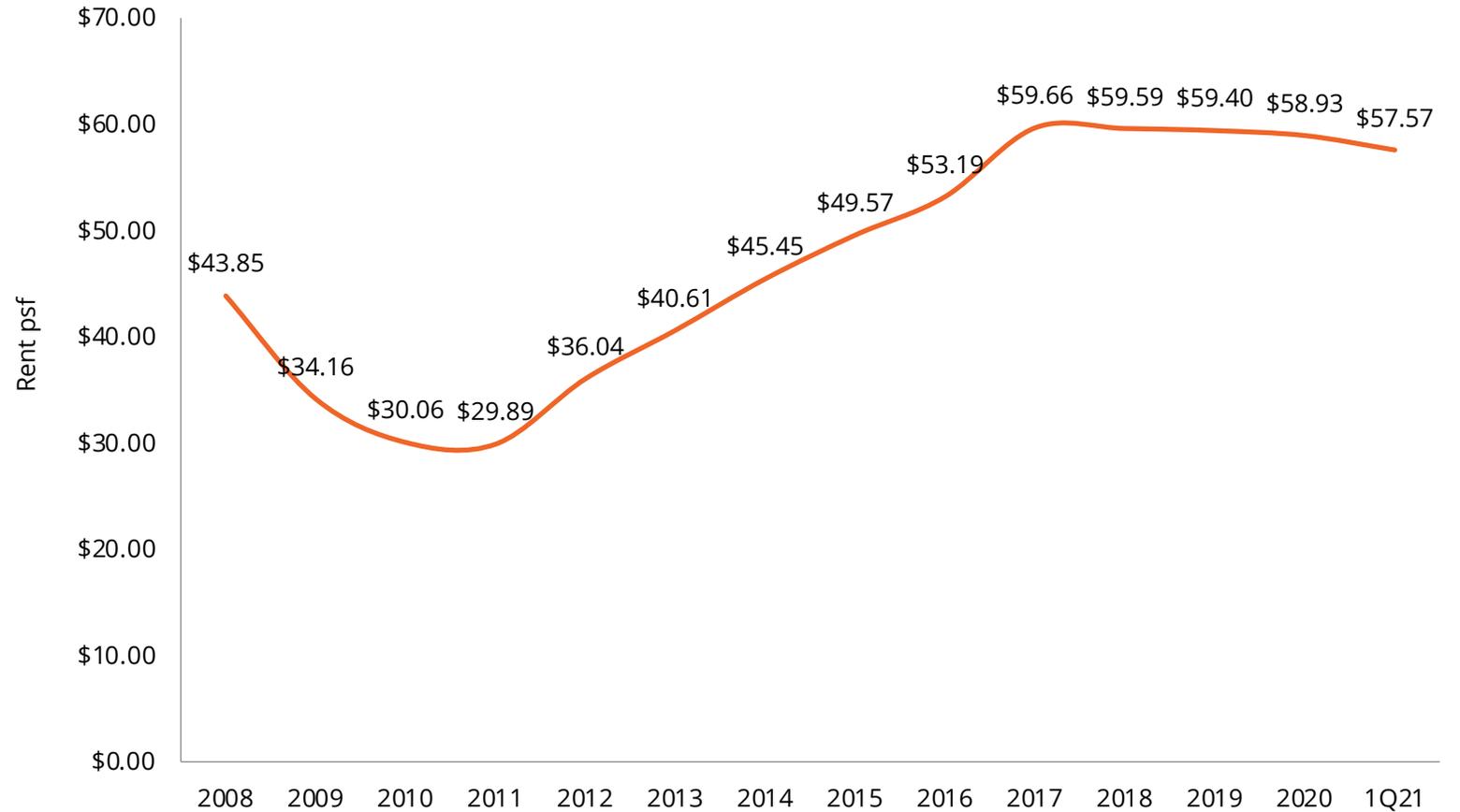


Base rents

-2.3%

Change in rents
since YE 2020

Base rents have incrementally softened following the pandemic and the resultant recession, but have not dropped as drastically as the Great Recession in the late 2000s.



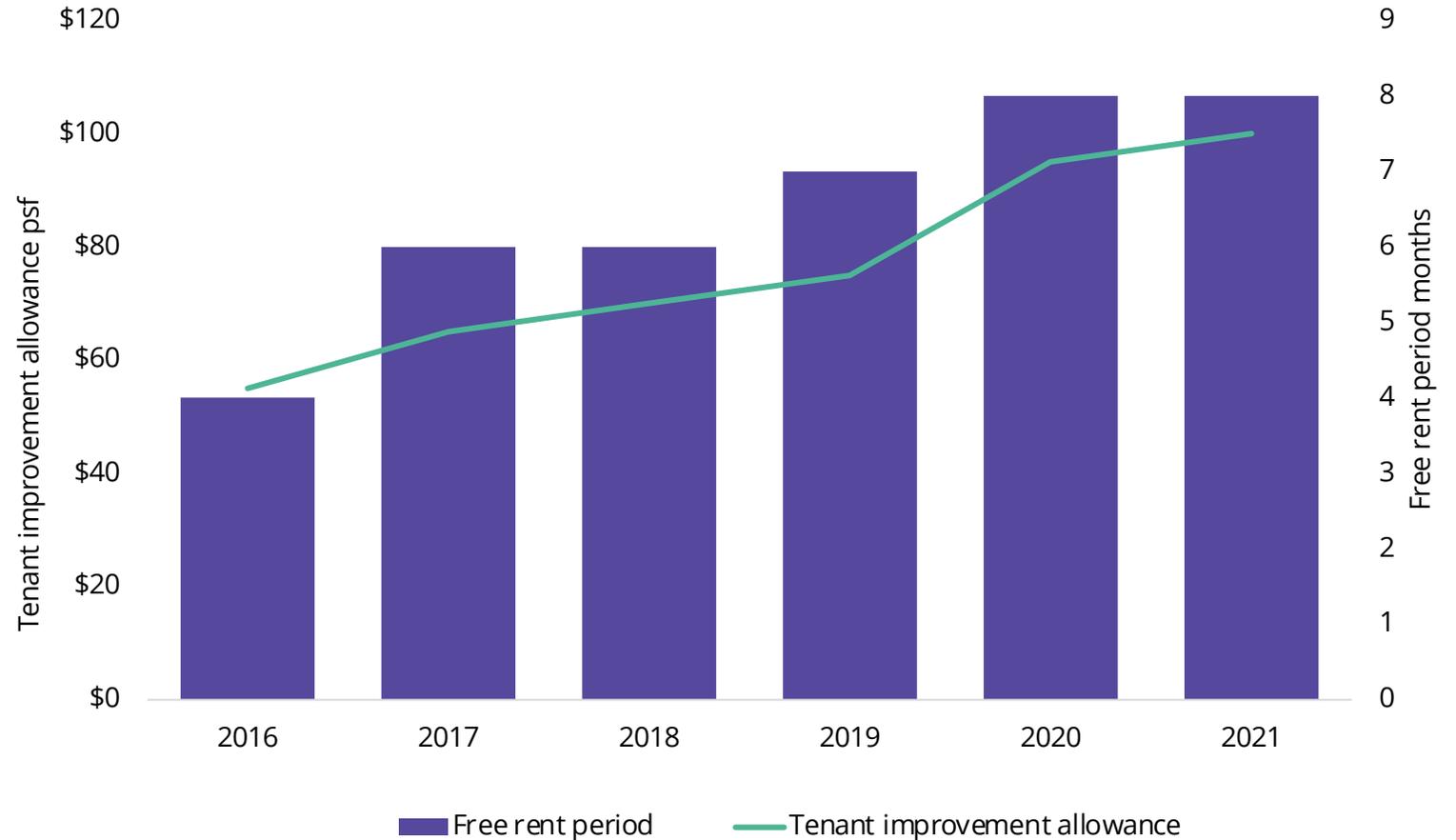
Source: AVANT by Avison Young

Concessions

5.2%

Increase in concessions over the first half of 2021

Tenant improvement allowances and free rent periods have increased as activity levels remain subdued.



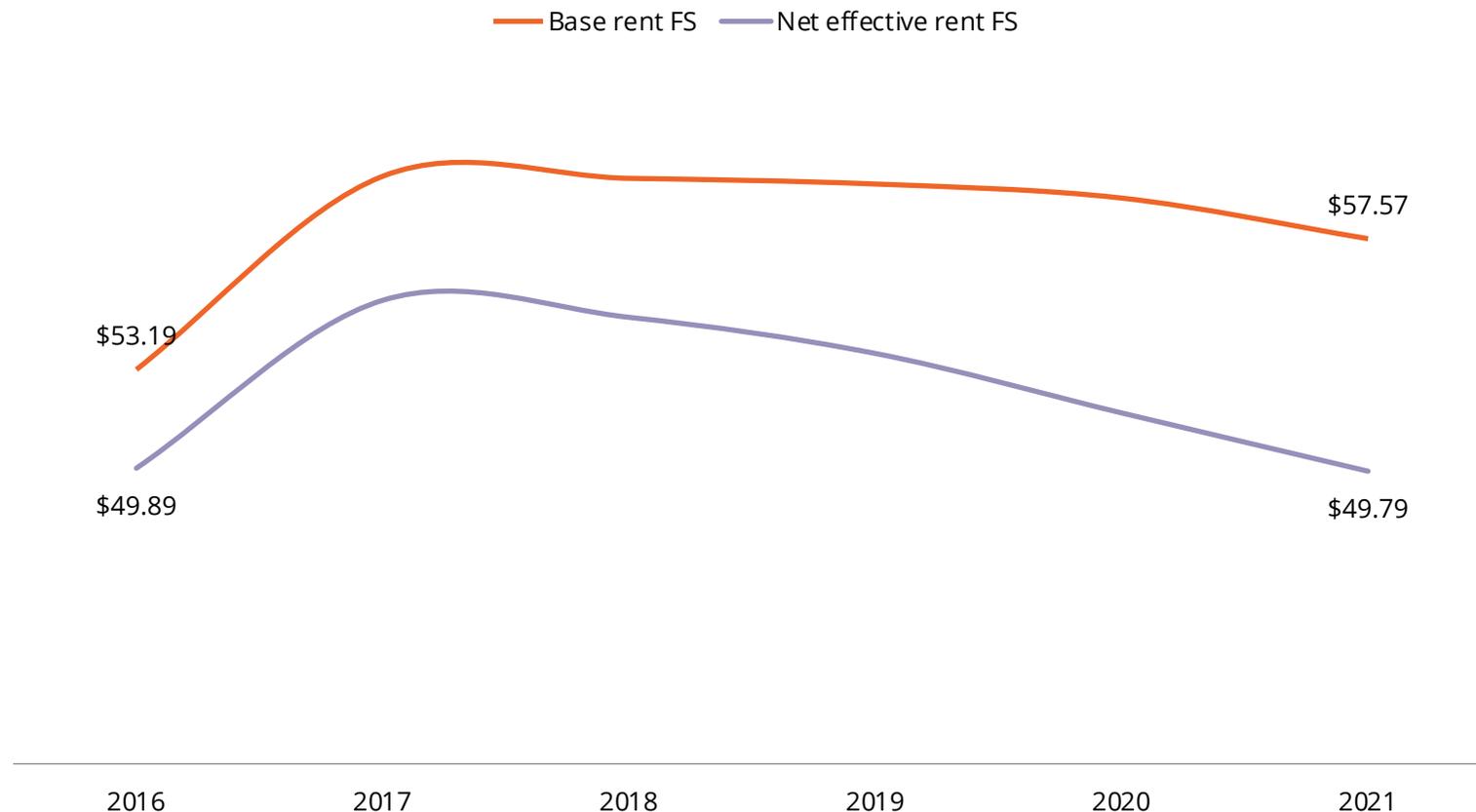
Note: Class A office properties.
Trailing 12-month unweighted averages. Excludes subleases, renewals and expansions.
Normalized to 10-year lease terms. Source: AVANT by Avison Young

Net effective rents and base rents

8.2%

Increase in delta between base and net effective rent since YE 2020

Net effective rents declined by 3.8 percent over the past six months as landlords were more motivated to provide additional concessions in lieu of lowering base rents.



Note: Class A office properties. Trailing 12-month unweighted averages. Excludes subleases, renewals and expansions. Source: AVANT by Avison Young

SF Peninsula aging inventory

69 properties

proposed or under construction

19.3 msf

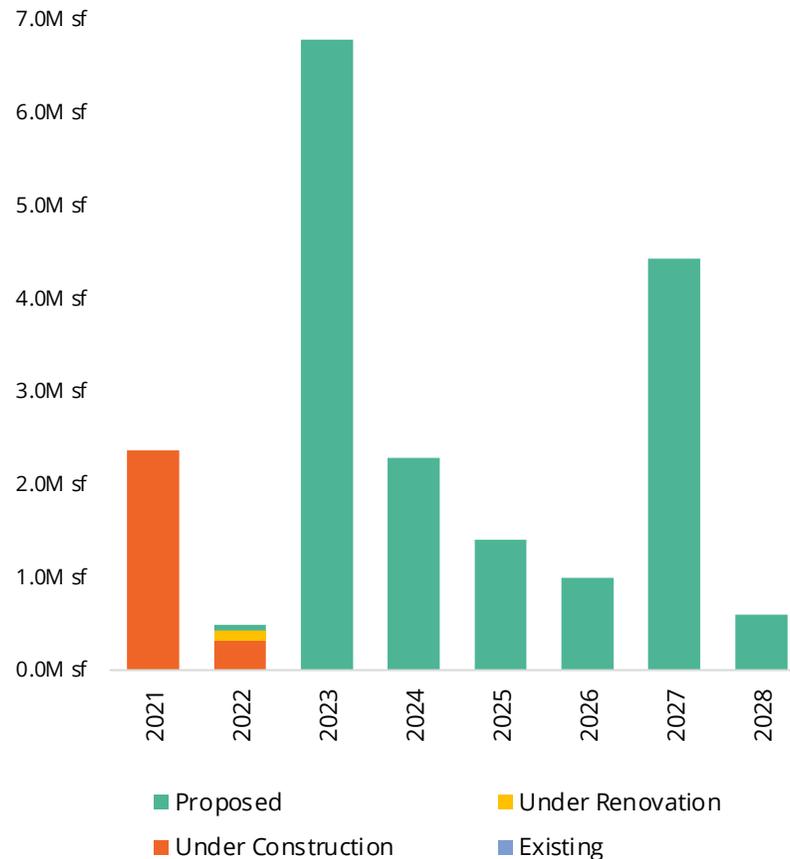
proposed or under construction

40.4%

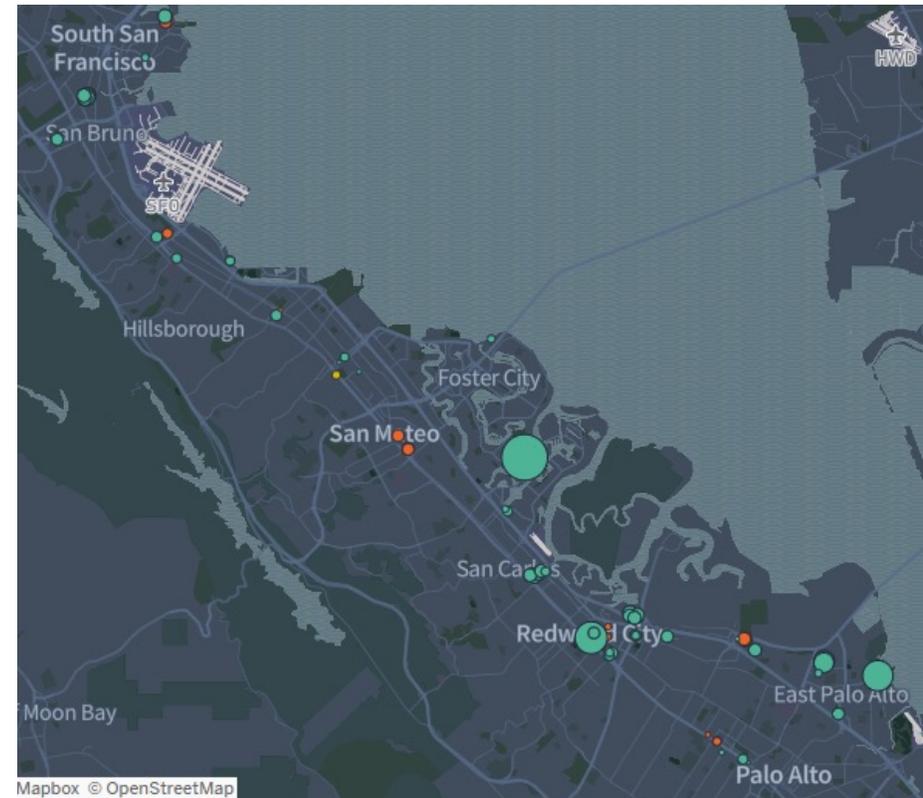
share of office inventory

1987

average delivery date of existing Silicon Valley offices



Source: AVANT by Avison Young

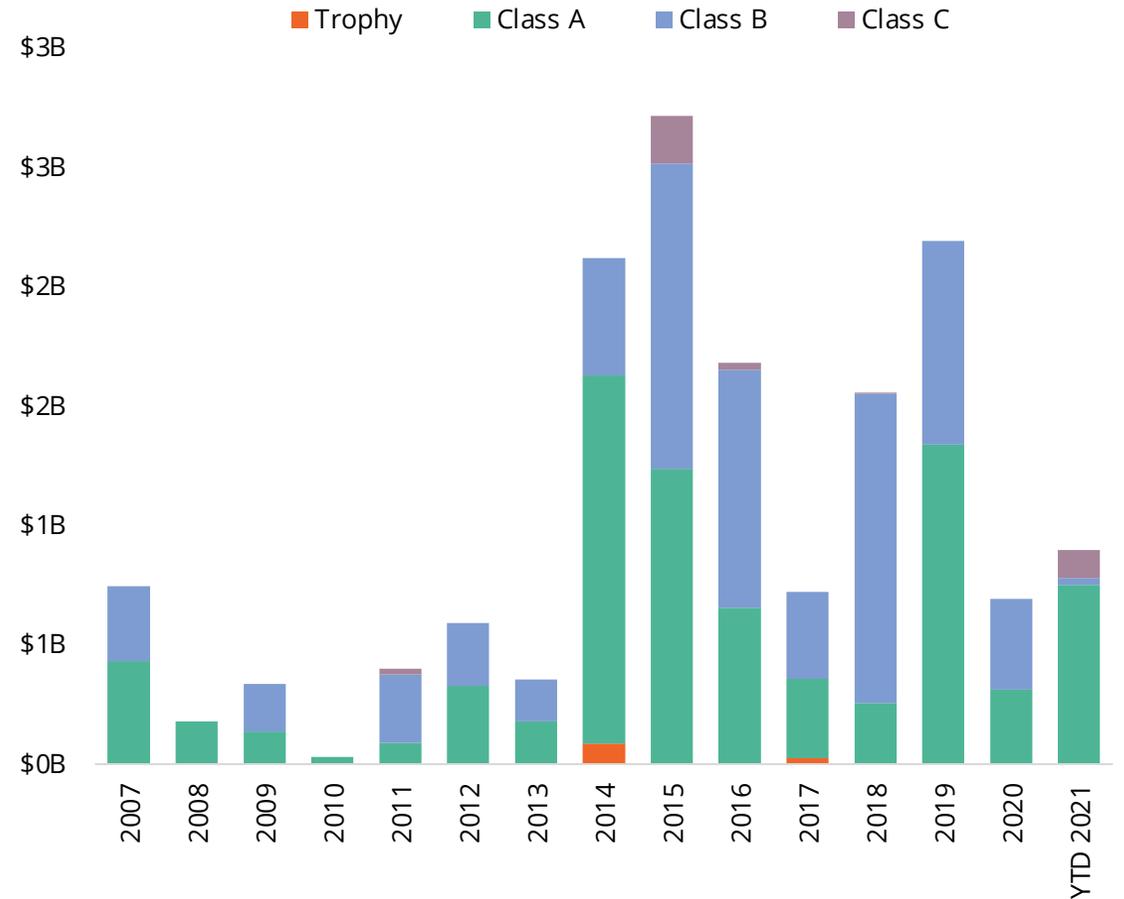


Office investment dollar volume

\$1.06B

Peninsula office dollar volume
2020 to present

Office sales activity has temporarily paused during the pandemic and subsequent risk-pricing crisis, decreasing by 40% compared with the prior five-year average dollar volume.



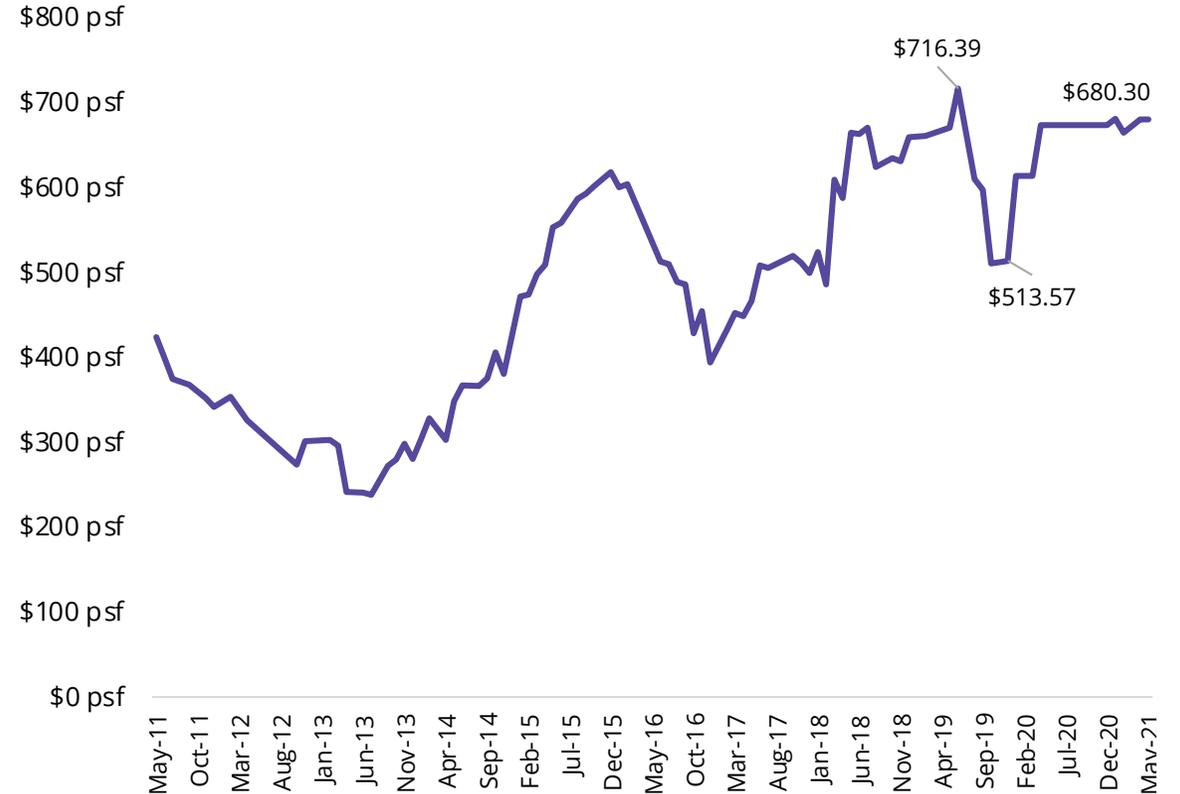
Source: AVANT by Avison Young,
California Department of Finance, RCA

Office asset pricing

32.46%

Peninsula office pricing from November 2019 to present

Pricing has nearly returned to pre-pandemic levels as investors see an end to the pandemic in sight, employees begin to return to the office, and leasing activity beginning to increase. Pricing hit a temporary low of \$513.57 psf at the height of the lockdowns in May 2020, but has increased every month since, now at \$680.30 psf.



Source: AVANT by Avison Young
New York City Department of Finance, RCA

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Let's talk

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