

# MARKETBEAT

## San Francisco

### Office Q1 2017



#### SAN FRANCISCO OFFICE

##### Economic Indicators\*

	Q1 16	Q1 17	12-Month Forecast
San Francisco Metro Employment	1,080K	1,109K	▲
San Francisco Metro Unemployment	3.4%	3.0%	▼
U.S. Unemployment	4.9%	4.8%	■

\*Q1 17 data based on the average of January and February values

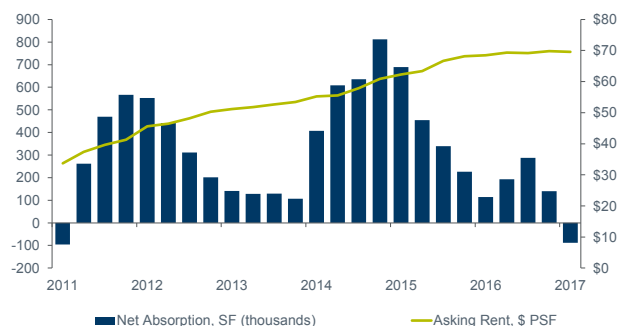
##### Market Indicators (Overall, All Classes)

	Q1 16	Q1 17	12-Month Forecast
Overall Vacancy	5.7%	8.7%	▲
Net Absorption (sf)	362K	-553K	▼
Under Construction (sf)	4.4M	5.1M	▼
Average Asking Rent*	\$68.44	\$69.66	▲

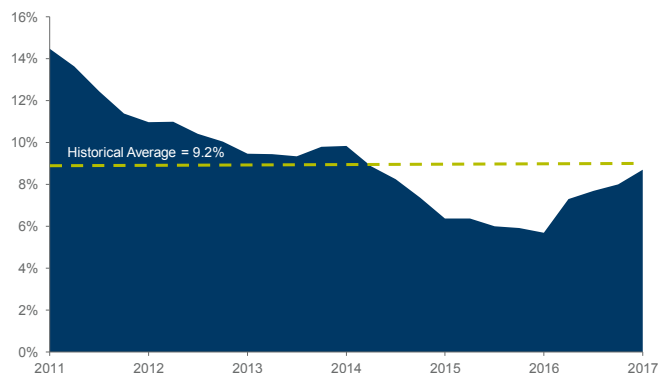
\*Rental rates reflect full service asking \$psf/year

##### Overall Net Absorption/Overall Asking Rent

###### 4-QTR TRAILING AVERAGE



##### Overall Vacancy



## Robust Leasing Activity for Q1 2017

The unemployment rate continued to hold at minimal levels for the San Francisco metropolitan division (San Francisco and San Mateo counties) with a 2.9% figure in February, down from a revised 3.1% in January, and below the 3.2% reported one year ago. And though growth has slowed, total private sector jobs still increased by +2.4% to 971,900 in February and office using positions climbed +2.1% annually to 420,800.

- The San Francisco office market has now experienced four consecutive quarters of increased vacancy. The Citywide overall vacancy rate closed the first quarter at 8.7%, a +70 basis point (BPS) increase from the fourth quarter and a +300 BPS increase from one year ago. This uptick in vacancy gives breathing room to the considerable number of tenants searching for space in a market that was, by all accounts, overheating. High asking (and effective rents) along with very few space options, had been giving tenants pause, forcing them to look beyond the city's limits for their office requirements. These tenants, large or small, can now find some relief with pricing and availability more reflective of a maturing market. There still remains a considerable amount of forward momentum in San Francisco. Leasing activity was solid in the first quarter and there are 31 large block users looking for 50,000 square feet (SF) or larger.
- The South Financial District has been a significant contributor to vacancy over the past year; direct vacant space has increased +890,000 SF (+63.6%) while sublease vacant space has jumped +400,000 SF (+181%). Nearly 100,000 SF of this vacant sublease space has already been leased and will only remain vacant until the new users take occupancy. This includes Gymboree (80,000 SF at 71 Stevenson Street). Tech tenants, the primary occupiers of space in this submarket, continue to show interest in several of the larger blocks of availability.
- The Citywide overall asking rent decreased -\$0.10 per square foot (PSF) or -0.1% to \$69.66 PSF in the first quarter, after a slight +0.8% bump in the fourth quarter. It has remained above the previous record peak of \$66.00 PSF (in the fourth quarter of 2000) for seven straight quarters. The CBD Class A direct average asking rent increased +\$0.51 PSF or +0.7% in the first quarter to \$74.62 PSF.

## Construction & Development

A total of 5.1 million square feet (MSF) was under construction at the end of the first quarter. The newest addition was Oceanwide Center's ground breaking at 50 First Street in the South Financial District. Scheduled for completion in 2021, it will be the second tallest office building in San Francisco, and add 1.0 MSF of office space to inventory.

There will be 3.0 MSF of new construction deliveries in 2017. At the close of the first quarter, 1.3 MSF (42.7%) of this inventory was pre-leased. The most recent leasing transactions were closed at Salesforce Tower where Accenture signed for 101,000 SF and a global real estate firm will occupy 39,000 SF. If any space is still available at Salesforce

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Tower, 181 Fremont Street, or 350 Bush Street upon delivery, the average asking rent will rise as this trophy product will be priced well above most existing, older office buildings.

### Leasing Activity & Absorption

New leasing activity totaled 1.5 MSF in the first quarter, which is just below the quarterly historical average going back to 2006. There were four large deals signed in excess of 100,000 square feet – Slack, located at 500 Howard Street for 225,000 SF; Google, located at 121 Spear Street for 166,000 SF; Adobe, pre-leasing an additional 105,000 SF at 100 Hooper Street, and the aforementioned Accenture, pre-leasing 101,000 SF at Salesforce Tower.

### THERE STILL REMAINS A CONSIDERABLE AMOUNT OF FORWARD MOMENTUM IN SAN FRANCISCO

Although there was a healthy amount of leasing activity in the first quarter, overall net absorption totaled -553,000 SF. The combination of increasing vacancy, a lack of significant move-ins, and no pre-leased new construction deliveries kept absorption in the red.

### Sublease Activity

Sublease vacancy remained essentially unchanged since mid-year 2016 at 1.5 MSF. The more forward-looking metric of sublease availability (all space being marketed whether vacant or occupied) increased +30.0% annually to 2.3 MSF. Sublease space now accounts for approximately 17.9% of all available space in San Francisco, compared to the historical quarterly average of 12.4%. A large percentage of the prime product (built-out, good location, longer-term) will likely be subleased before ever moving into vacancy statistics as has been the case over the past year.

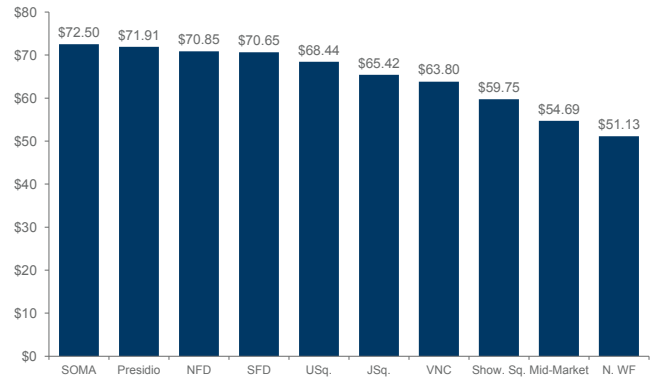
The largest new sublease availabilities to hit the market in the first quarter were Medivation's 114,000 SF at 525 Market Street, Medivation's 44,000 SF at 499 Illinois Street, and Splunk's 95,000 SF at 250 Brannan Street.

### Outlook

- Expect office job growth to remain above the historical average in 2017.
- Delivery by year-end of 3.0 MSF of trophy office product with 5.4 MSF of active tenant requirements in the market.
- Pricing of space (for lease or for sale) will remain at or near record levels.

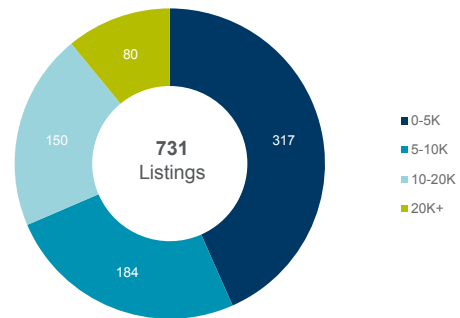
### Average Asking Rate by Submarket (Full Service)

RENTS CONTINUE TO CLIMB, NOTABLY IN NON-CBD SUBMARKETS



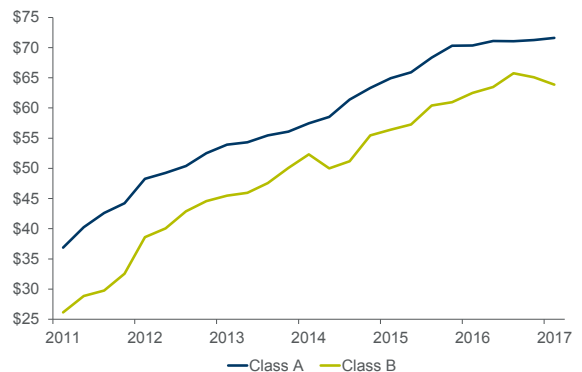
### Availabilities by Size Segment

DECREASING SUPPLY FOR QUALITY LARGE BLOCK SPACE



### Average Asking Rate by Class (Full Service)

CLASS B RENTS DIP IN FIRST QUARTER



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SUBMARKET	INVENTORY (SF)	SUBLET VACANT (SF)	DIRECT VACANT (SF)	OVERALL VACANCY RATE	CURRENT QTR OVERALL NET ABSORPTION (SF)	YTD OVERALL NET ABSORPTION (SF)	YTD LEASING ACTIVITY (SF)	UNDER CNSTC (SF)	OVERALL AVERAGE ASKING RENT (ALL CLASSES)*	OVERALL AVERAGE ASKING RENT (CLASS A)*
North Financial District	25,908,335	444,442	2,405,712	11.0%	-152,340	-152,340	417,498	370,000	\$70.85	\$73.25
South Financial District	25,627,040	619,130	1,585,979	8.6%	-326,750	-326,750	803,452	3,618,398	\$70.65	\$70.41
<b>CBD</b>	<b>51,535,375</b>	<b>1,063,572</b>	<b>3,991,691</b>	<b>9.8%</b>	<b>-479,090</b>	<b>-479,090</b>	<b>1,220,950</b>	<b>3,988,398</b>	<b>\$70.77</b>	<b>\$72.01</b>
Jackson Square	1,490,806	13,176	40,942	3.6%	8,748	8,748	9,021	0	\$65.42	\$69.00
North Waterfront	3,176,308	95,106	135,381	7.3%	-88,641	-88,641	49,410	0	\$51.13	\$57.60
SOMA	7,947,198	239,996	525,341	9.6%	-104,963	-104,963	60,868	153,117	\$72.50	\$76.59
The Presidio	1,030,627	0	15,661	1.5%	-1,667	-1,667	8,563	0	\$71.91	\$71.91
Union Square	3,173,989	20,911	184,012	6.5%	-30,778	-30,778	26,101	0	\$68.44	\$74.06
Van Ness Corridor	878,956	2,553	108,458	12.6%	-1,540	-1,540	0	0	\$63.80	\$59.29
Showplace Square / Potrero Hill	3,261,042	35,743	180,539	6.6%	83,288	83,288	139,072	314,000	\$59.75	\$62.27
Mission Bay	1,056,735	43,625	0	4.1%	-43,625	-43,625	0	680,000	N/A	N/A
Mid-Market	4,223,733	29,482	35,562	1.5%	104,850	104,850	0	0	\$54.69	\$61.56
Third Street Corridor	349,465	0	0	0	0	0	0	0	N/A	N/A
<b>TOTAL</b>	<b>78,124,234</b>	<b>1,544,164</b>	<b>5,217,587</b>	<b>8.7%</b>	<b>-553,418</b>	<b>-553,418</b>	<b>1,513,985</b>	<b>5,135,515</b>	<b>\$69.66</b>	<b>\$71.60</b>

\*Rental rates reflect full service asking \$psf/year

OFFICE CLASS BREAKDOWN										
Class A	55,190,495	1,155,173	3,719,758	8.8%	-241,476	-241,476	1,244,819	4,982,398	\$71.60	
Class B	15,634,271	310,939	1,132,798	9.2%	-230,604	-230,604	164,606	153,117	\$63.87	
Class C	7,299,468	78,052	365,031	6.1%	-81,338	-81,338	104,560	0	\$66.46	

#### Key Lease Transactions Q1 2017

PROPERTY	SF	TENANT	LANDLORD	TRANSACTION TYPE	SUBMARKET
500 Howard Street	225,490	Slack	Heitman	Direct	South Financial
121 Spear Street	166,460	Google	Hudson Pacific Properties	Direct	South Financial
100 Hooper	104,667	Adobe	Kilroy Realty	New Construction	Showplace Square
415 Mission Street	100,630	Accenture	Boston Properties	New Construction	South Financial
201 Spear Street	64,858	WeWork	KBS Realty Advisors	Direct	South Financial

#### Key Sale Transactions Q1 2017

PROPERTY	SF	BUYER	SELLER	PRICE / \$PSF	SUBMARKET
One Post Street	424,000	Brookfield	McKesson Corporation	\$250,000,000 / \$590	North Financial
211 Main Street	417,000	The Blackstone Group	CIM Group	\$293,000,000 / \$703	South Financial
100 Pine Street	402,000	Rockpoint Group	LaSalle / Alaska Permanent Fund	\$287,500,000 / \$714	North Financial
150 Spear Street	264,000	Walnut Hill Group	Principal Global Investors	\$185,000,000 / \$699	South Financial
114 Sansome Street	184,000	Deka Immobilien	Credit Suisse	\$147,800,000 / \$797	North Financial

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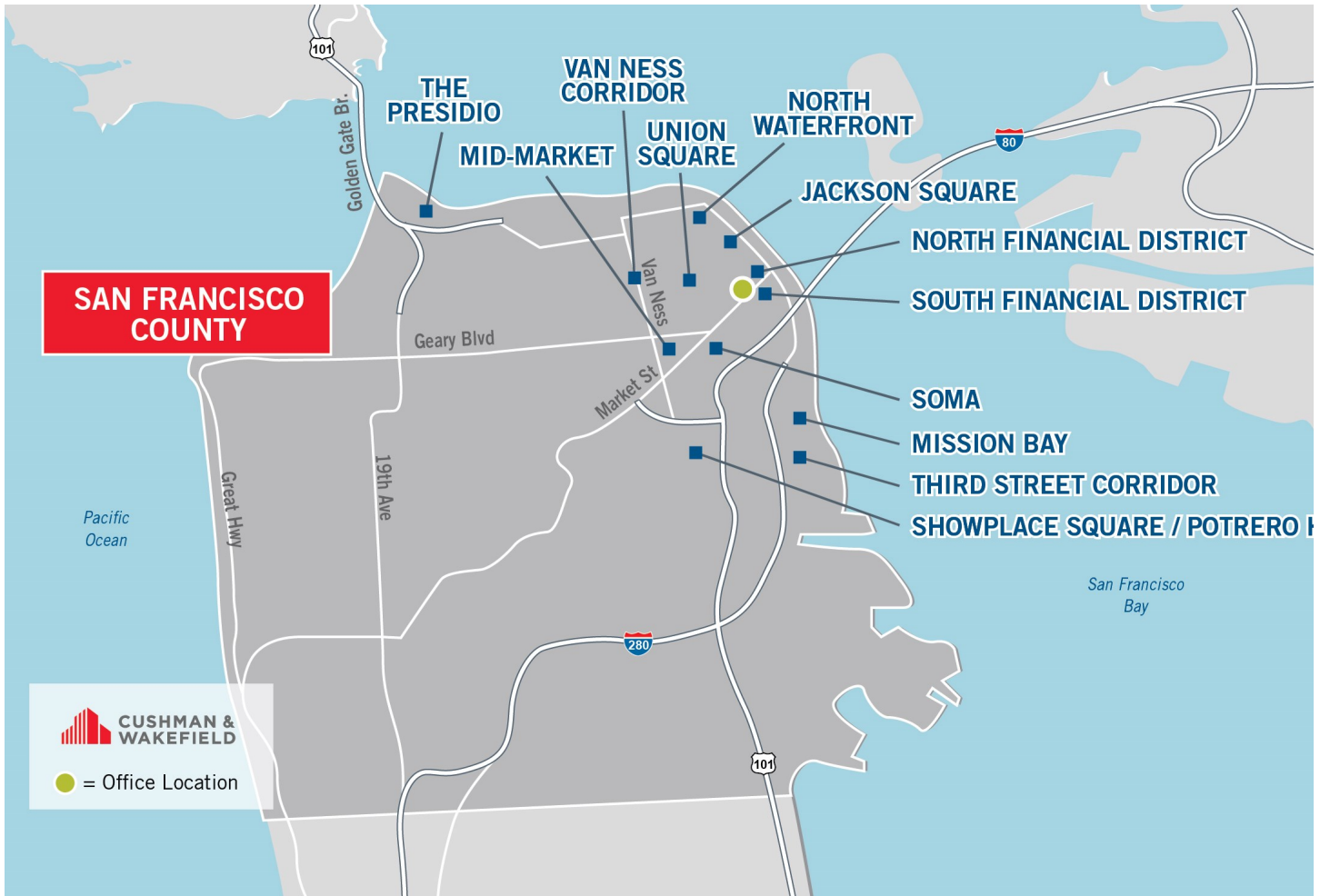
## San Francisco

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#### Office Submarkets

San Francisco



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