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SPECIAL REPORT: COMMERCIAL REAL ESTATE

Landlords Still Hold Favorable Cards

Sizzling Market Downshifts Slightly; Trends Emerge in Submarkets

BY LOU HIRSH

As the early months of 2017 unfold, it's clear that demand for San Diego County commercial real estate remains strong, even if most sectors aren't exhibiting red-hot characteristics like those seen during the past two years, particularly in the multifamily and industrial segments.

Still, the numbers at the end of the first quarter showed that landlords remained the chief beneficiaries in the multifamily and retail categories, where the countywide vacancy rate hovers around 4 percent, as well as the industrial segment, where most local experts report a vacancy around 5 percent.

With regional vacancy around 10 percent, the office category is tilted more closely toward an equilibrium between landlords and tenants, except for high-demand markets like Del Mar Heights and Torrey Pines where demand far outstrips supply, with rents reflecting that.

Property sales and leasing remain generally strong in markets such as University Towne Center, Sorrento Mesa and Carlsbad. Downtown San Diego continues what has been a long recovery since the end of the Great Recession, fueled by a gradual influx of apartment dwellers and small businesses.

The region as a whole is still posting low unemployment, with continued job growth in sectors such as technology and life science. Other key local industries that fuel demand for real estate, such as tourism and defense, remain healthy by historical standards.

As always, conditions on the ground can vary widely depending on the submarket. But San Diego County during the past decade has not been significantly overbuilt in any of the major commercial categories, and is currently not showing signs of becoming so.

With the midpoint of 2017 approaching, the **San Diego Business Journal** asked local experts — including brokers, investors and developers in the four categories — to assess key emerging trends of the year's first half, and discuss local and national factors that could impact the region in the second half and beyond. Excerpts of their written responses are on pages 18-20.

Industrial PAGE 18

Photo courtesy of JLL

In April, a joint venture that included La Jolla's Hill Properties acquired a nine-building industrial park in Scripps Ranch for $31.4 million.

Multifamily PAGE 18

Photo courtesy of CoStar Group

In April, San Diego's American Assets Trust Inc. announced its purchase of the 533-unit Pacific Ridge Apartments in the city's Morena submarket for approximately $232 million.

Office PAGE 20

Photo courtesy of CoStar Group

In January, the Regents of the University of California acquired a four-building office portfolio in Governor Park for $83.5 million.

Retail PAGE 20

Photo courtesy of CoStar Group

In May, Chicago-based GEM OPS LLC acquired the eight-building Beachwalk retail center in Solana Beach for $33.25 million.

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Adam Robinson

Adam Robinson
Principal
RAF Pacifica Group
Owner and developer

First-half Takeaways: San Diego has historically lagged behind other markets in terms of new industrial construction and is now poised for new development. The first five months of 2017 have proven this concept, as demand for new industrial product has reached a pressure point, sparking spec development projects across San Diego.

The changing variable in this new market landscape is an increased demand for creative spaces in the industrial sector. We've seen this trend for years in the office product, but it is now shifting into the local industrial market.

Second-half Outlook: The outlook for the second half of 2017 remains strong. The national economic forecast projects steady growth in the technology, distribution and manufacturing industries, which will continue to drive the industrial sector well into 2017.

The rise of e-commerce is one variable that will continue to positively impact demand for industrial real estate. Big-box retailers are beginning to rethink the way they utilize distribution space, and we are now leasing smaller warehouses in urban infill markets such as San Diego, located in close proximity to consumers.

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