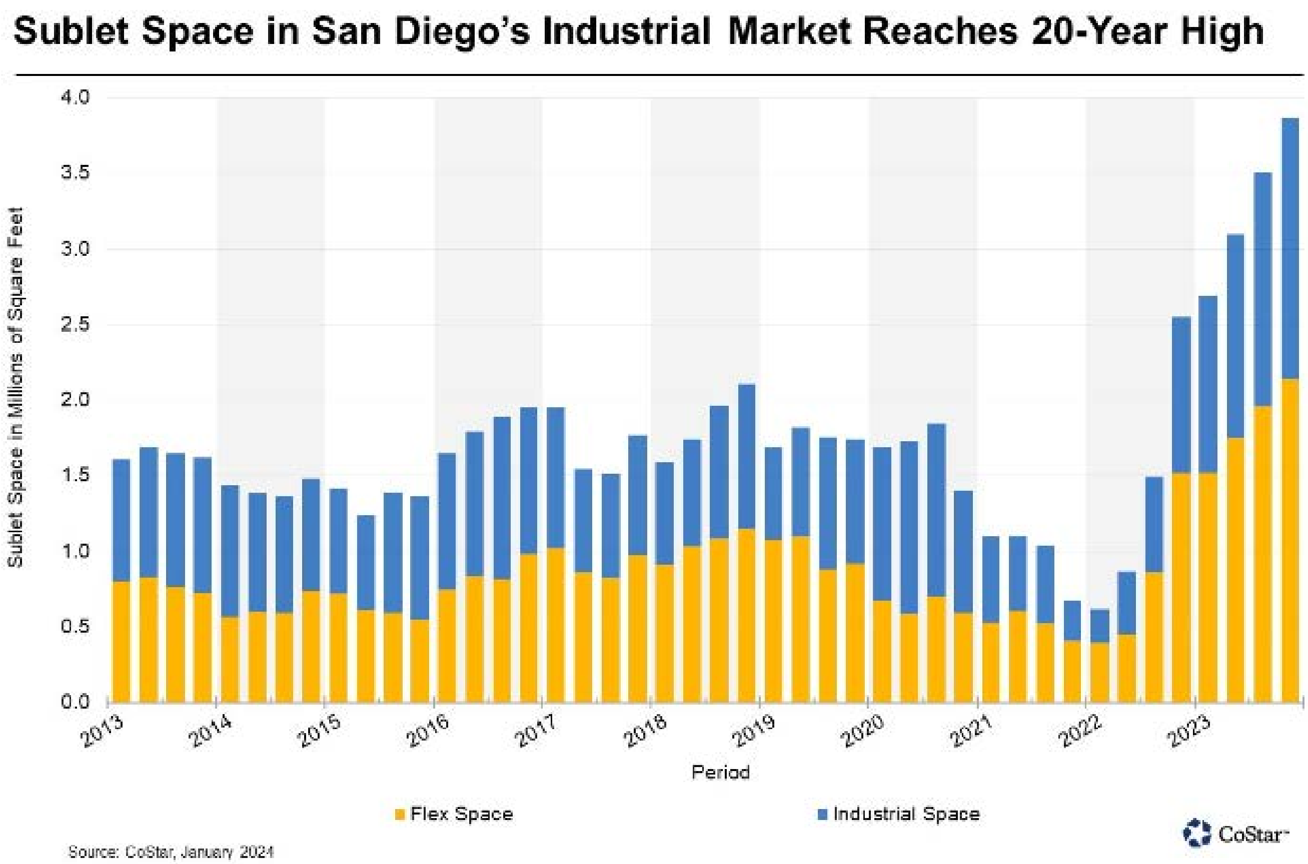
Sublease Space Adds Pressure to San Diego's Industrial Market
Vacancies Are on the Rise for Industrial and Flex Properties



By Joshua Ohl

A record level of industrial and flex space has joined the sublease market in San Diego, bringing it to a dizzying high of 3.9 million square feet at the end of 2023.

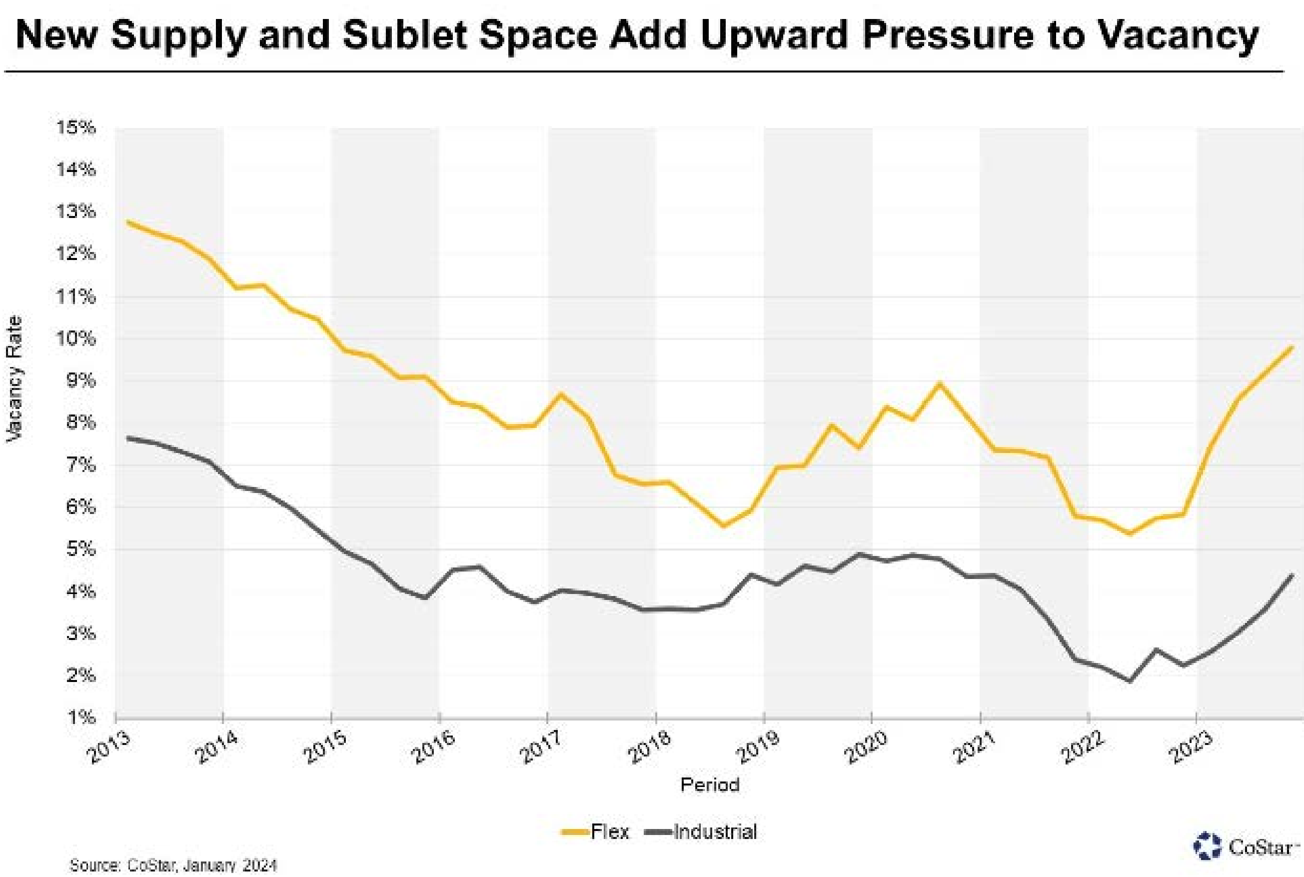
That was 1.3 million square feet more than was available at the end of 2022 and a touch more than the 3.8 million square feet on the market during the height of the Great Recession.

More than half of that available sublet space — 2.1 million square feet — sits in flex properties. That's the first time that sublet space in flex buildings has exceeded 2 million square feet in the past 20 years. Vacancy has nearly reached 10%, which is the highest level in nearly 10 years and two percentage points above the 10-year average.

Nearly two-thirds of flex sublet space is within flex/lab properties. The level of sublet space, in both new and existing lab buildings, coupled with the amount of available direct space in the lab pipeline, has unsettled market participants who worry that it might take another year or more for biotech demand to recover. Torrey Pines and Sorrento Mesa — two of San Diego's primary life science nodes — have the highest levels of available sublet space in flex properties.

But performance in the flex market has somewhat obfuscated shifts in the industrial market in San Diego. The amount of sublet space in industrial properties grew by 700,000 square feet over the past year to 1.7 million. While that is the highest level in the past decade, there was a two-year period during the Great Recession when it averaged 2.3 million square feet.

Amazon, which leased roughly 3 million square feet of space between 2020 and early 2022 across the region — not including its 3.4 million square-foot facility in San Diego's Otay Mesa neighborhood — added roughly 600,000 square feet to the sublease market in the second half of 2022. Several of those facilities have since found sublessees from Carlsbad to the Morena district, and only about 200,000 square feet remained on the sublease market at the start of 2024.



While vacancy in industrial properties rose 210 basis points to 4.4% at the end of 2023, the metric remained in line with the 2019 to 2020 level and within range of San Diego's 10-year average.

Although net absorption, which tracks the change in occupancy over time, was negative during each quarter last year, more than 1.9 million square feet completed, which was the third-highest amount of industrial space to open in the region over the past 10 years.

Of that new 2023 inventory, almost all of which was in Otay Mesa, 1.4 million square feet is still available for lease. Otay Mesa’s vacancy rate has climbed toward 10%, more than doubling over the past year.

Although there is some concern locally about rising vacancy and availability among market participants, particularly due to a significant drop in leasing for spaces larger than 100,000 square feet, stakeholders remain confident in the long-term demand drivers for the region.

Improving consumer confidence and easing recessionary concerns should spur returning demand for logistics facilities larger than 100,000 square feet in the coming quarters. A new, second port of entry under construction to support significantly higher northbound commercial warehouse traffic destined in Otay Mesa and along the I-15 corridor could also help boost demand.