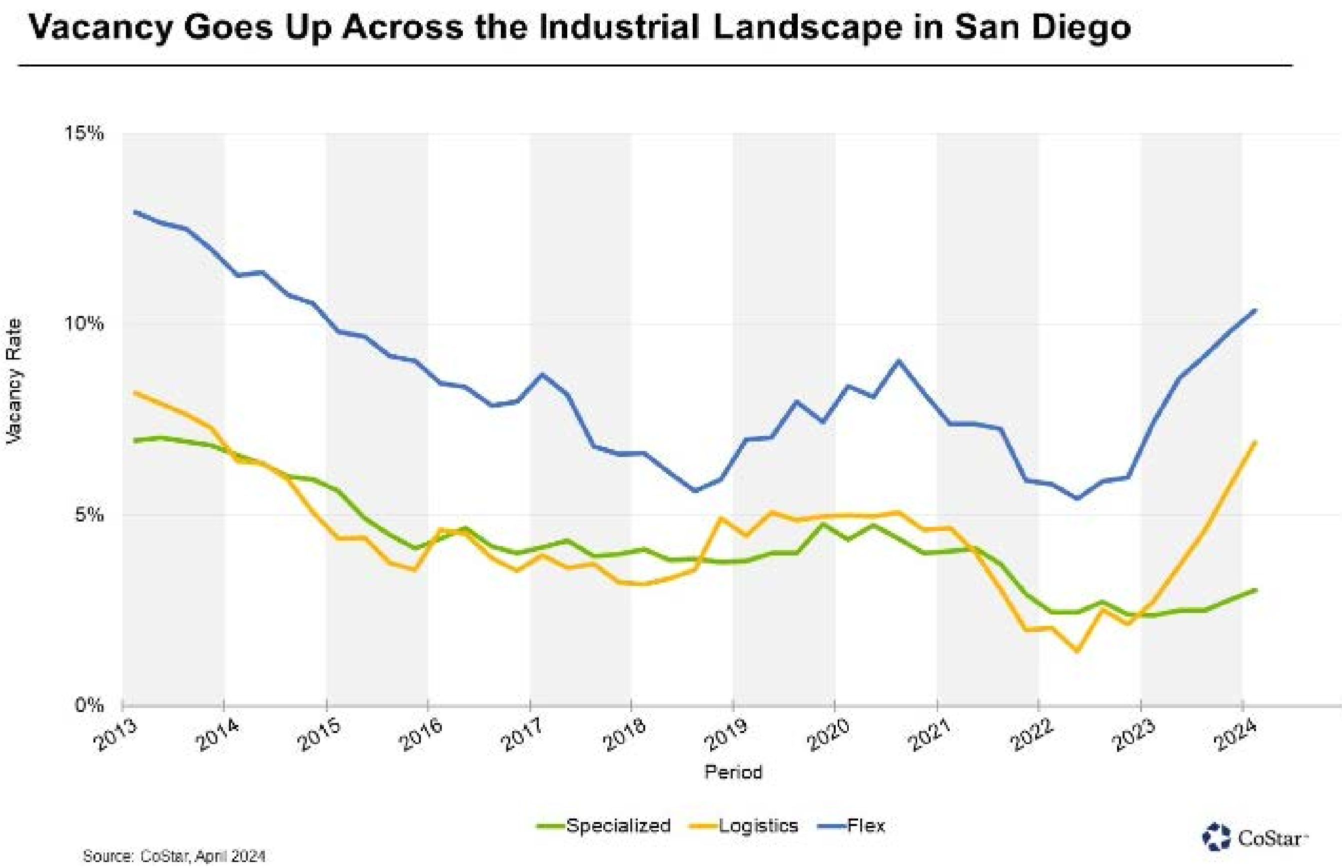
Rising Availability and Vacancy Highlight San Diego's Industrial Market

New Vacant Space Is Piling Up



By Joshua Ohl

San Diego's overall industrial vacancy rate climbed to 6.6% at the end of the first quarter. That was nearly three percentage points higher than the first quarter of 2023 and the highest level since 2014. Market participants have noted that San Diego's industrial market is not normalizing but is instead navigating a period of weaker demand.

They have pointed to economic uncertainty among logistics users as a primary culprit.

Part of that rise can be attributed to vacancy created by biotech firms in the UC San Diego area and logistics tenants such as Amazon, which vacated yet another facility in the region earlier this year. San Diego is amid the longest run of negative quarterly absorption, which tracks the change in occupancy over time, since the period from 2008 to 2010, after the first quarter saw negative absorption for the fifth straight quarter.

It can also be attributed to new inventory. More than 650,000 square feet of inventory was completed in the first quarter, and 600,000 square feet of that space was completed vacant. That's in addition to the 1.6 million square feet still available in space that opened last year and the 2.8 million square feet available in the pipeline.

Most of the new inventory in San Diego is concentrated in South County, near the border with Mexico. The demand drivers in Otay Mesa, including access to Mexico's labor force and transportation arteries through the region along the Interstate 15 Corridor, are unmatched in San Diego and should ensure that the space there is absorbed. But market participants have noted that broader macroeconomic concerns continue to weigh on large occupiers, and demand may not resurface until 2025.

Logistics vacancy ended the first quarter at 6.7%, up four percentage points in the past year. Flex vacancy climbed three percentage points to over 10%, and specialized industrial inventory rose marginally to 3%.

The amount of available space in industrial and flex buildings climbed above 21 million square feet earlier this year for the first time since 2014. That marked the seventh consecutive quarter of rising availability, which now stands above 10% of existing inventory.

Although there was an uptick in leasing above 50,000 square feet during the first quarter, with four deals representing 25% of new leasing volume, those have done little to reduce the amount of available space, which increased 1.2 million square feet quarter over quarter.

If there is a silver lining, in the past seven quarters of rising availability, the average quarterly increase has been nearly two million square feet, with the lowest quarter-over-quarter rise being 400,000 square feet. With fewer buildings expected to break ground until new inventory is absorbed, the pace of rising availability may finally be slowing.

San Diego has always been a small-bay market, which remains the case today. Vacancy in buildings with less than 50,000 square feet is historically low. Demand remains robust for industrial spaces between 5,000 to 25,000 square feet, and local brokers have noted that they have never been busier searching for those requirements from Vista to National City.

San Diego's demand environment has become more bifurcated, and market participants anticipate that the current leasing trends will likely continue throughout the year.