



San Francisco office market report

Q4 2023

**AVISON
YOUNG**

San Francisco office market trends

\$279 psf

Office pricing reaches lowest point in 12 years

Mounting debt, interest rates, and increasing vacancy have weighed down pricing in San Francisco, causing properties to sell at significantly discounted rates not witnessed since 2011. Despite office pricing falling to \$279 psf, sales transactions nearly doubled in 2023 compared to the previous year. There is now a growing sentiment suggesting that the market is bottoming out, prompting investors to strategize for long-term investments.

1.33 msf

Q4 leasing activity shows marked improvement

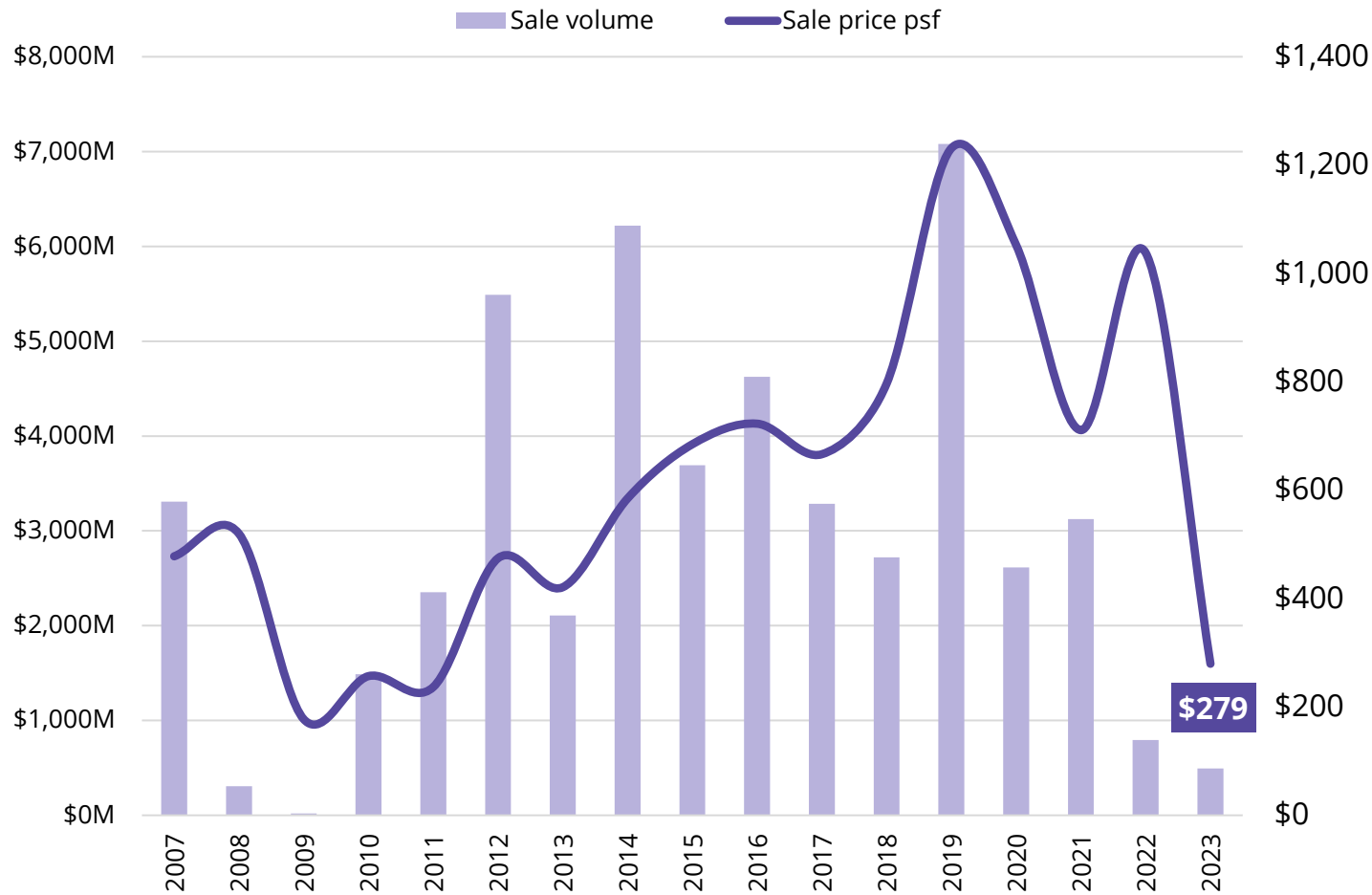
Leasing activity remains below the pre-Covid 5-year average as companies, constrained by limited capital, continue to opt for short-term solutions. End-of-year leasing figures indicate a 36.2% decrease compared to 2022 but are up 14.3% compared to the recent low of 2020. Noteworthy leases from OpenAI and Anthropic led to a 98.9% increase in leasing activity from Q3 2023 and the strongest quarter of 2023. Coupled with a rising number of tenants in the market, there is growing potential for a positive start to 2024.

22.8%

Remote job postings steadily inch downwards

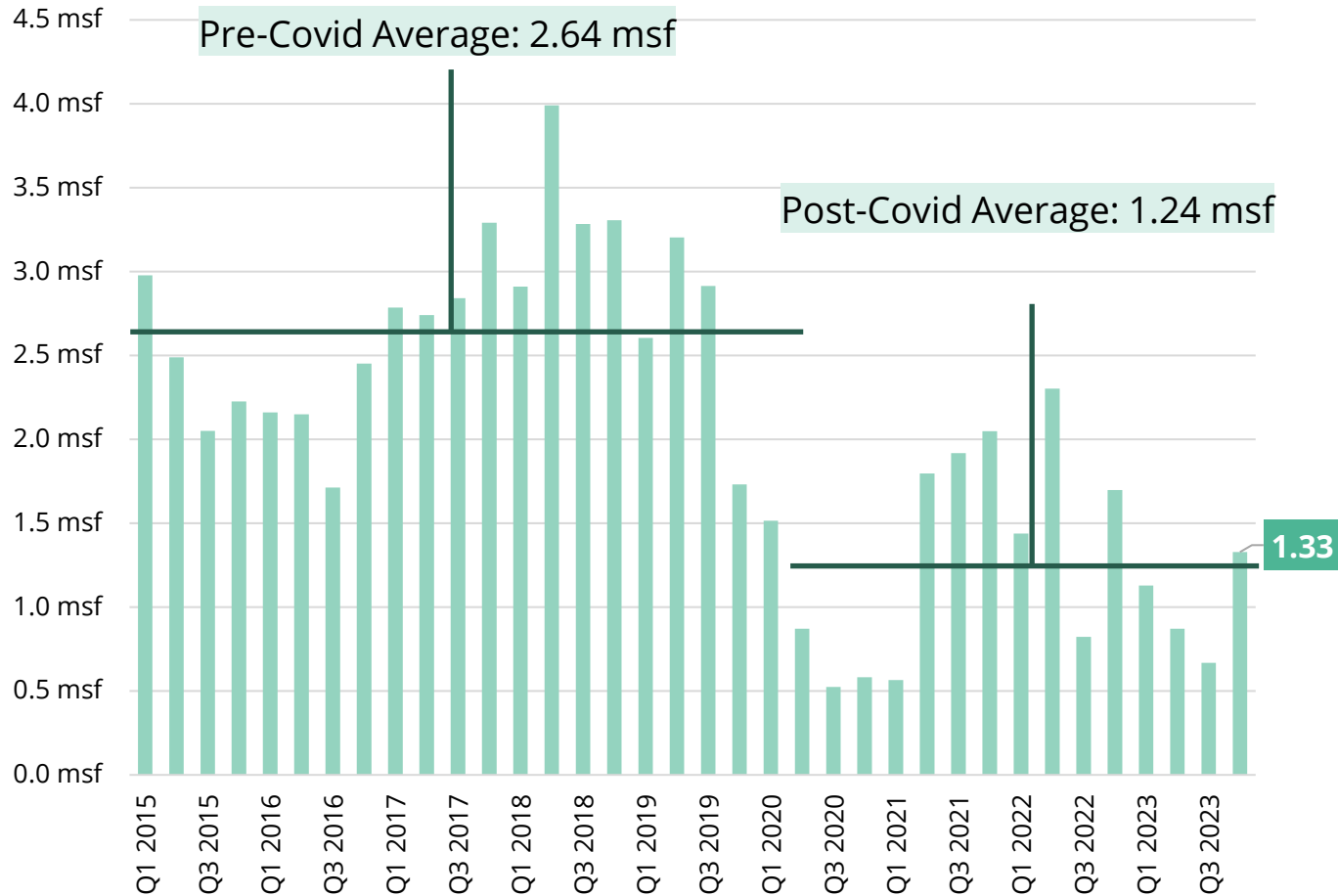
Q4 remote job postings averaged 23.7%, a 4.1% drop from the previous quarter. As the job market continues to soften, companies are likely to use this as leverage to get workers to return to the office. While major corporations such as Amazon, Meta, and Apple have already mandated a return to the office, mid-sized companies are opting to bide their time in the market, waiting for improved economic conditions before making a similar move.

Investment volume



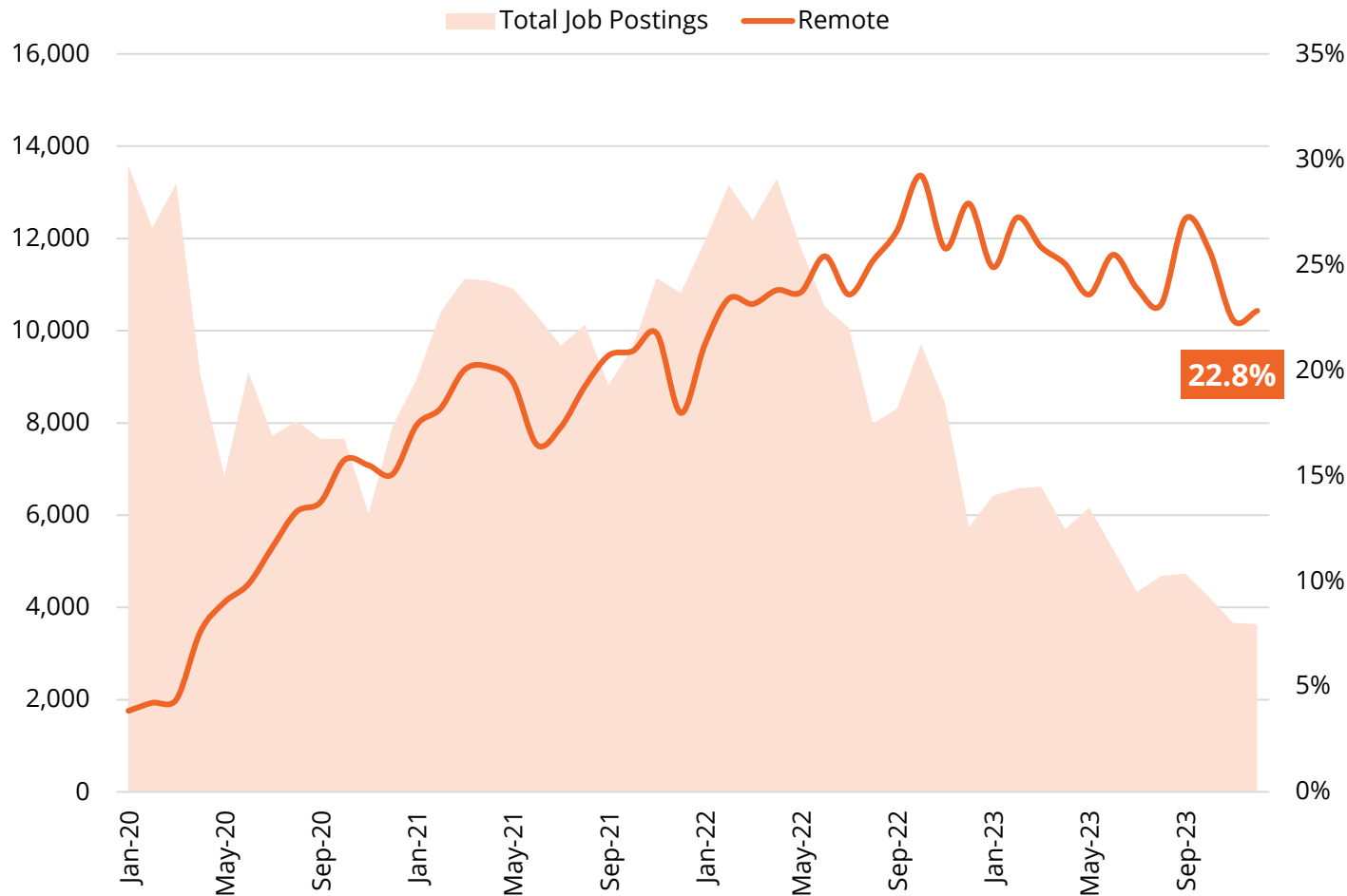
Mounting debt, interest rates, and increasing vacancy have weighed down pricing in San Francisco, causing properties to sell at significantly discounted rates not witnessed in the last 12 years. This has opened the door to a new generation of investors looking to capitalize on favorable pricing.

Leasing activity



Leasing activity continues to fall short of the 5-year pre-Covid leasing average. However, a strong end to Q4 saw 2023 narrowly avoid the recent low of 2020.

Remote job postings

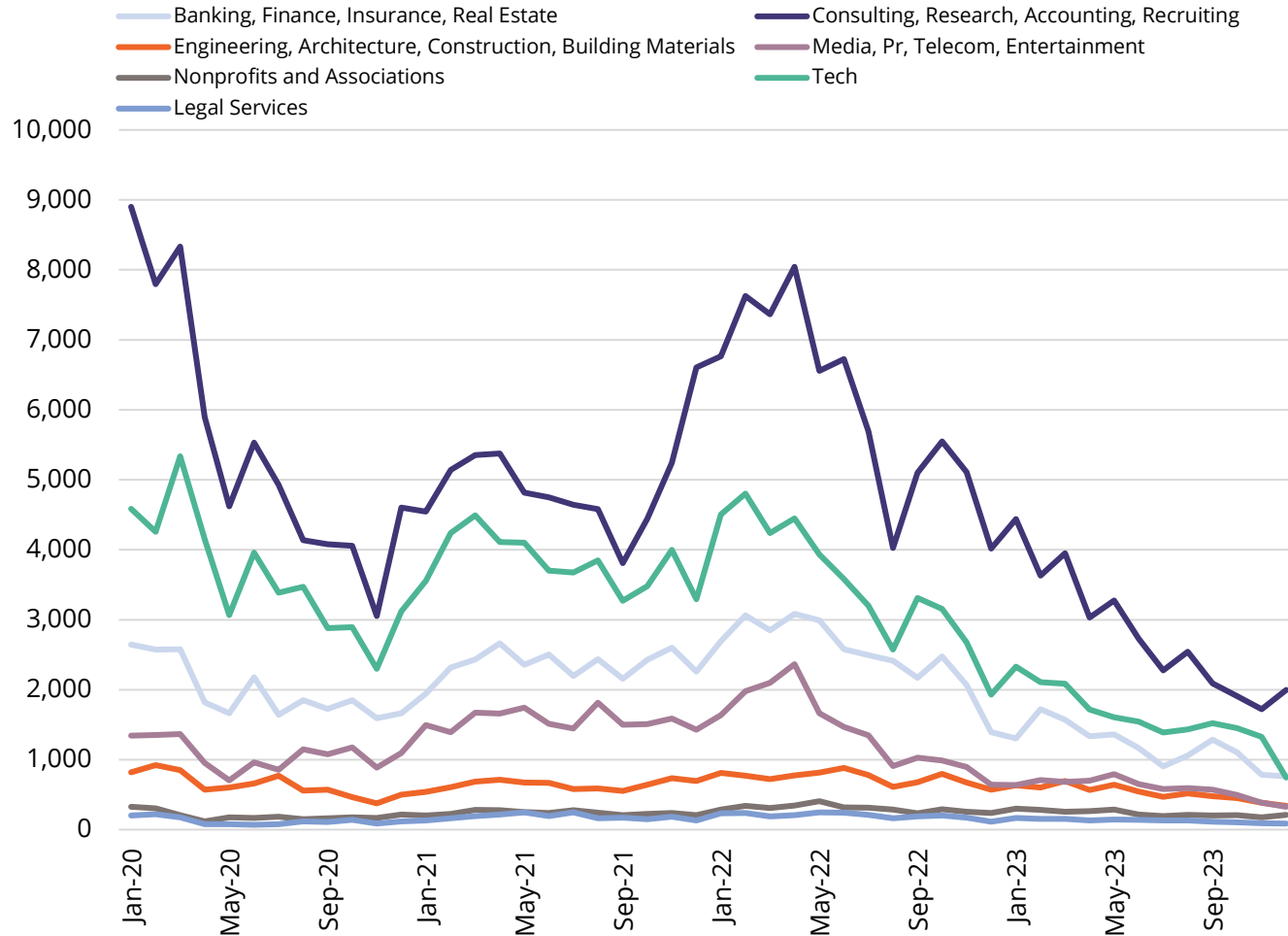


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Economic trends

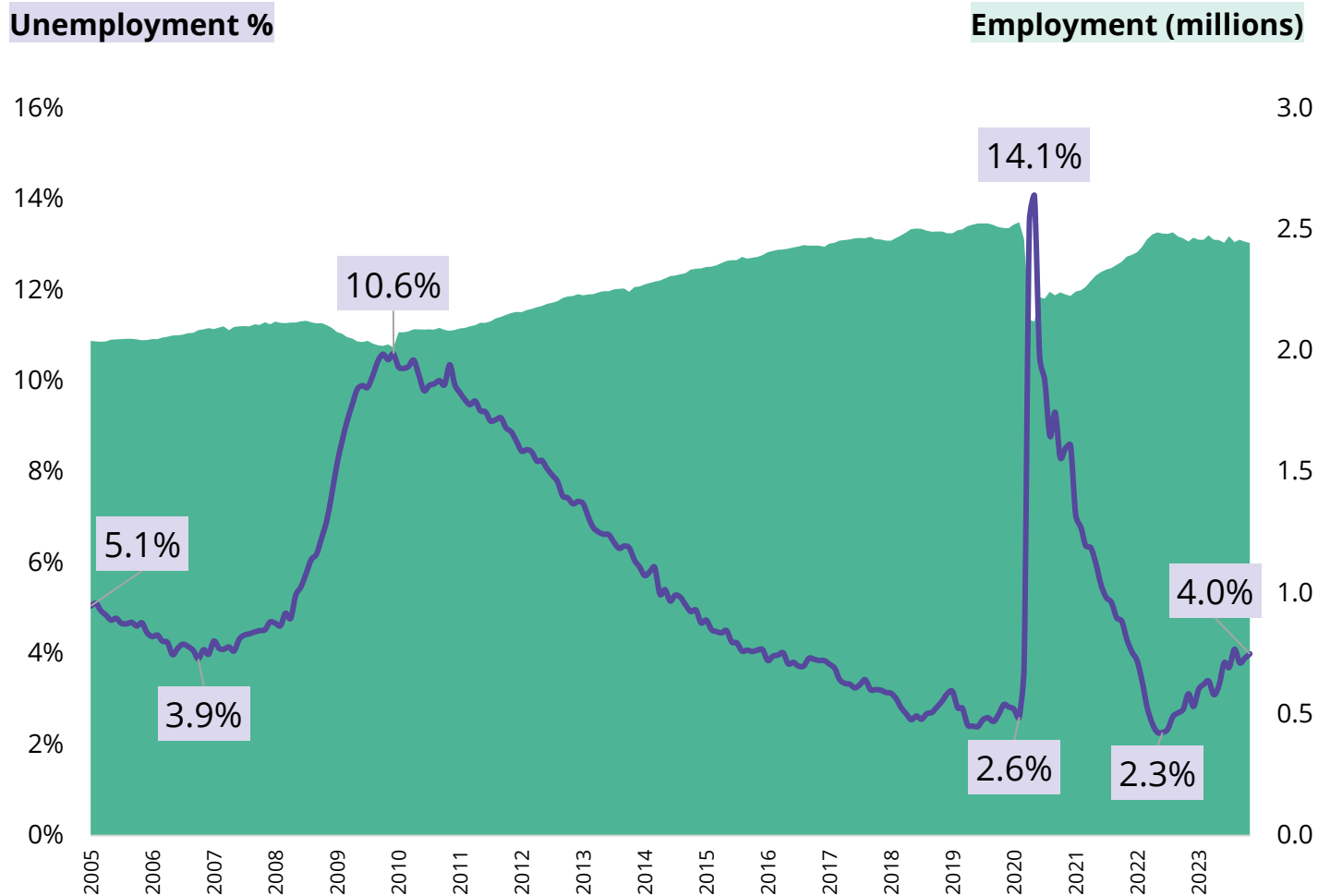


Job postings by industry type



Overall job postings saw a 19.5% decrease from the previous quarter, with all sectors experiencing declines. Consulting, Research, Accounting and Recruiting companies saw an 18.6% drop, while Tech fell 18.9%.

Employment and unemployment rate

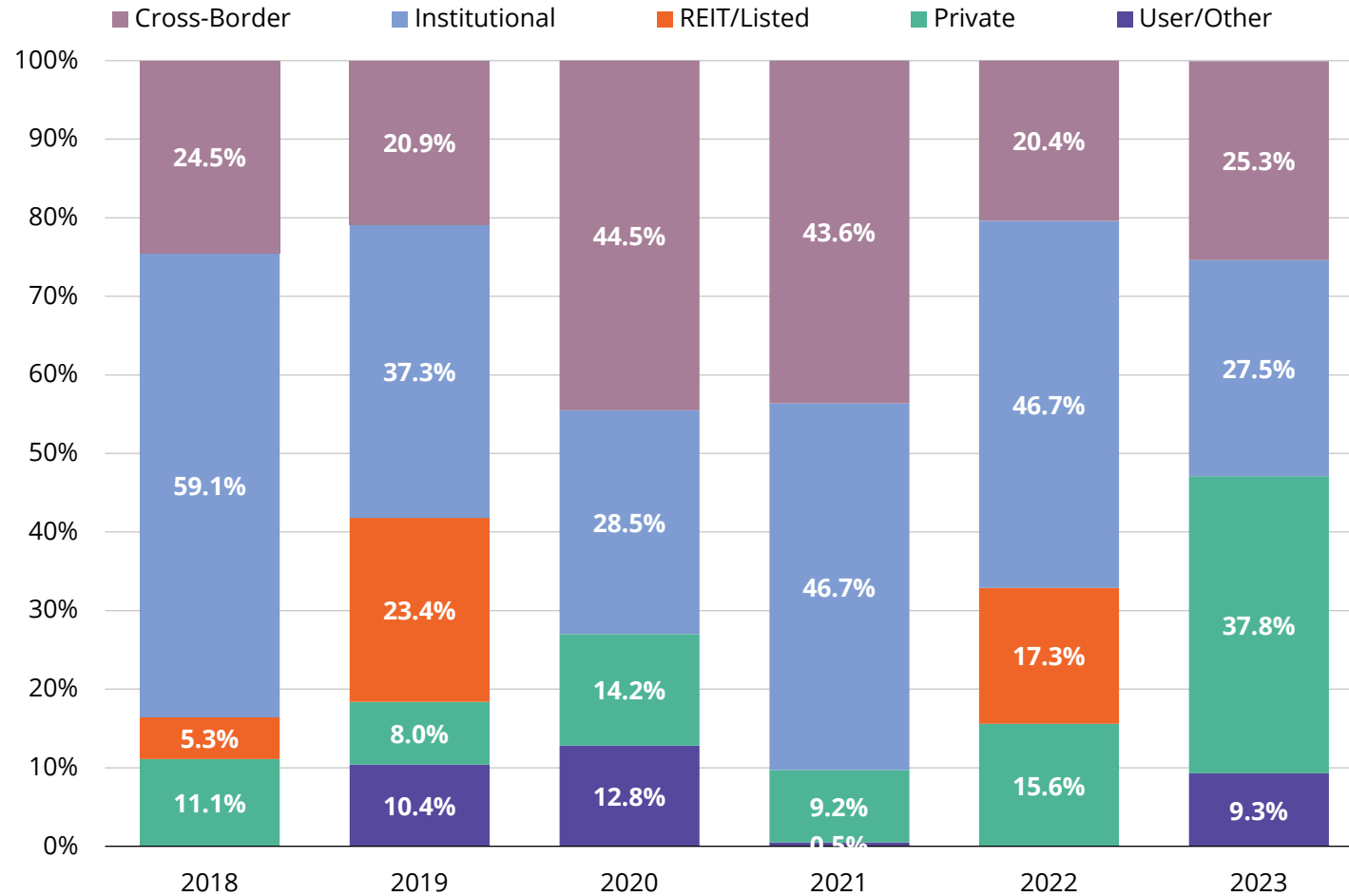


San Francisco's unemployment has crept up to 4.0% this quarter after bottoming out in June 2022 at 2.3%. This follows the latest rate hikes in July, as the Federal Reserve continues to combat rising inflation.

Office market trends

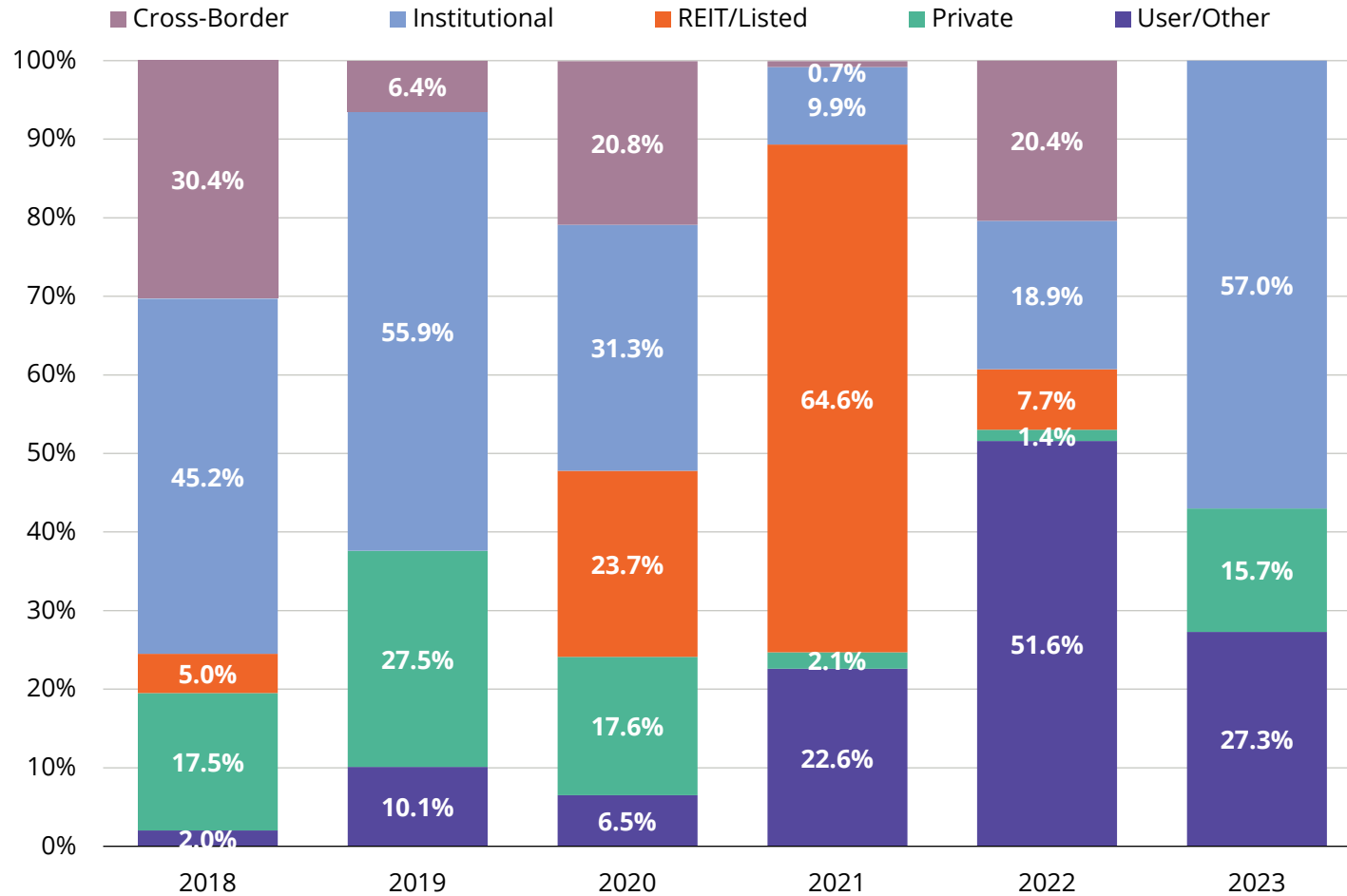


Buyer profiles



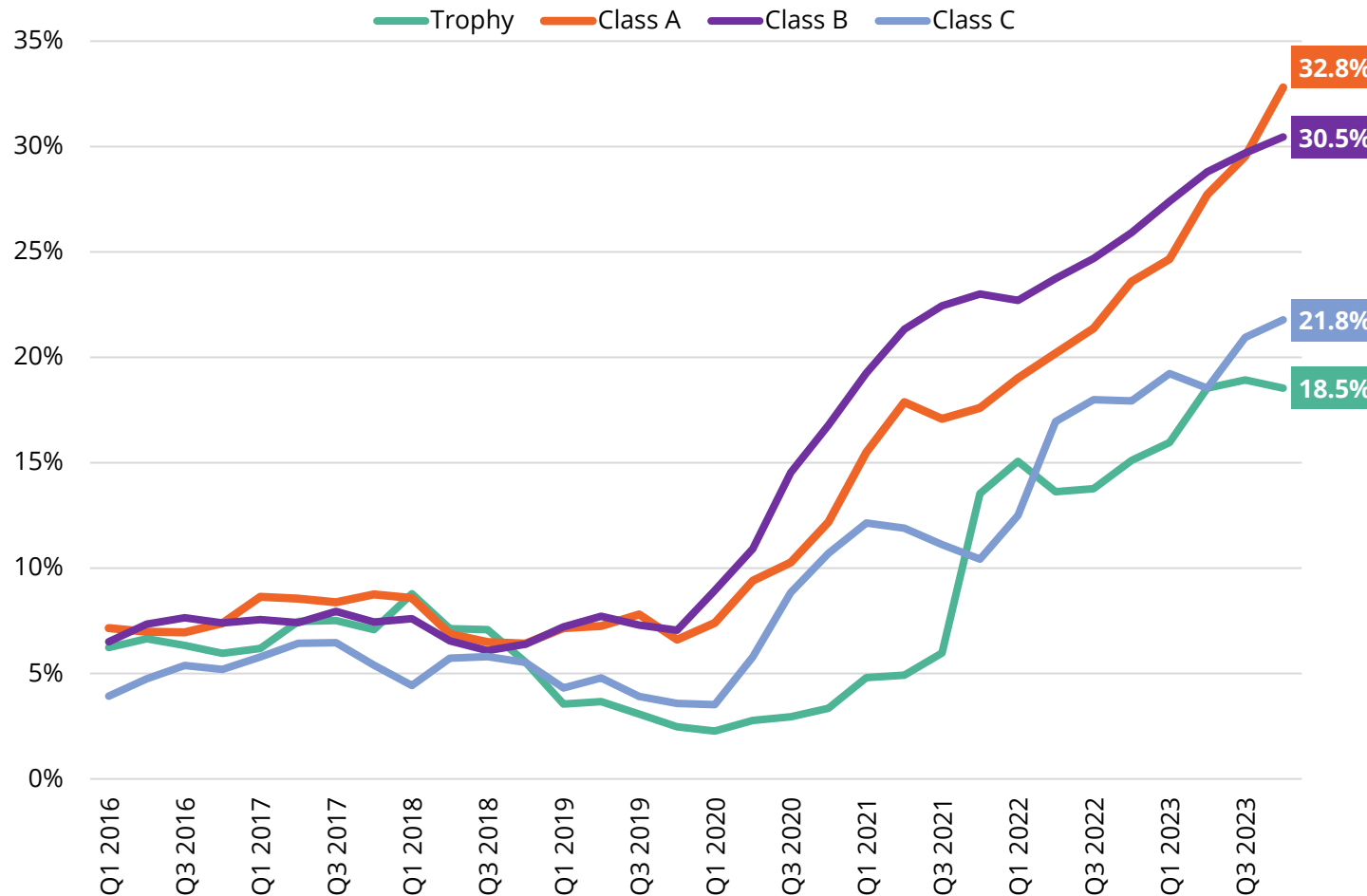
Due to softened pricing and the increase of distressed assets in the market, private buyers have become more active, whereas institutional capital has retreated. Although cross-border buyers typically participate during economic distress abroad, the absence of core investments in the market has prevented this trend in 2023.

Seller profiles



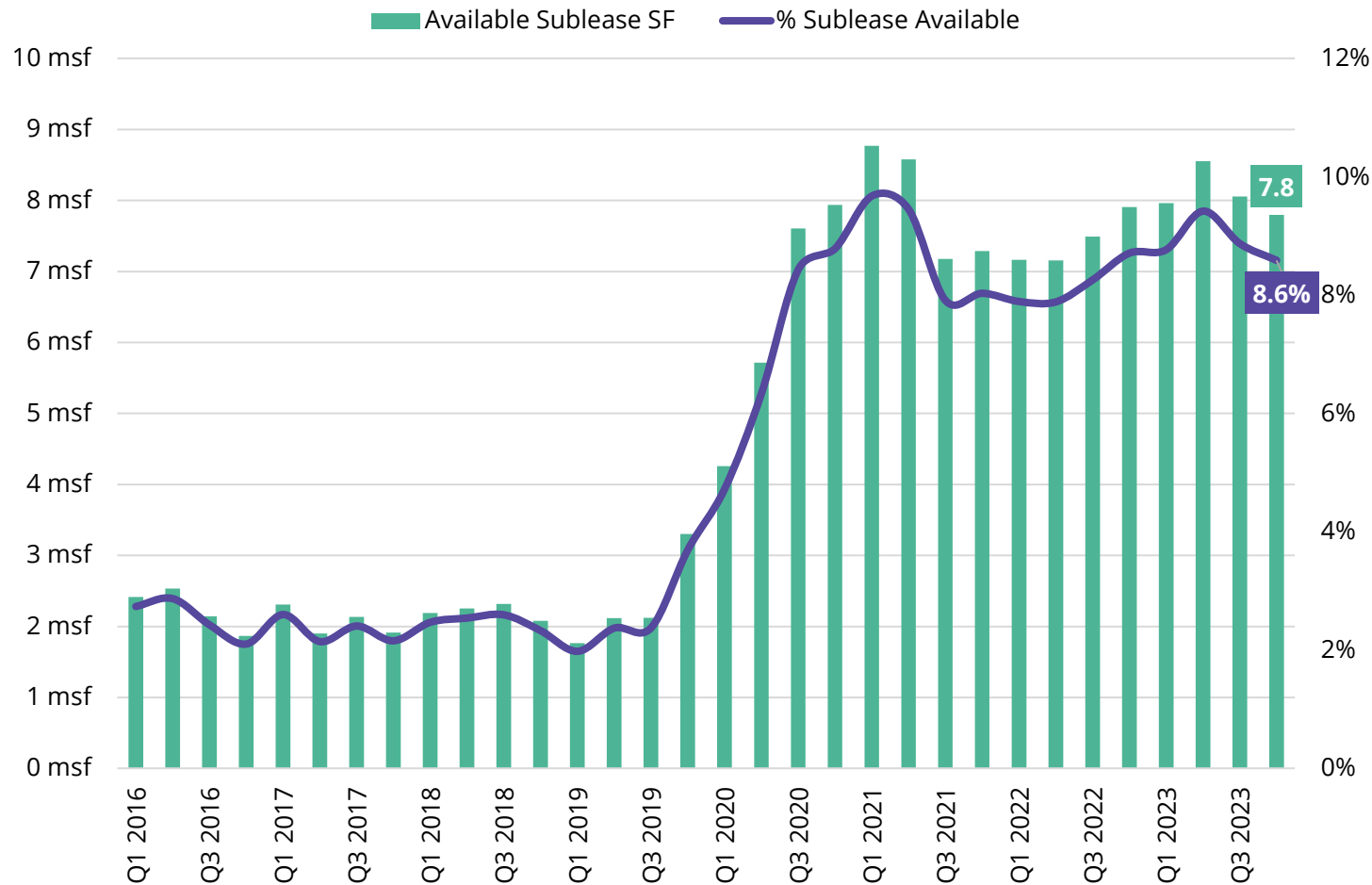
Private investors have been compelled to sell their assets at a significantly higher rate than in previous years due to the challenging conditions in the debt markets. Asset refinancing has become an increasingly challenging task, with an increasing threat of defaults.

Total vacancy by class



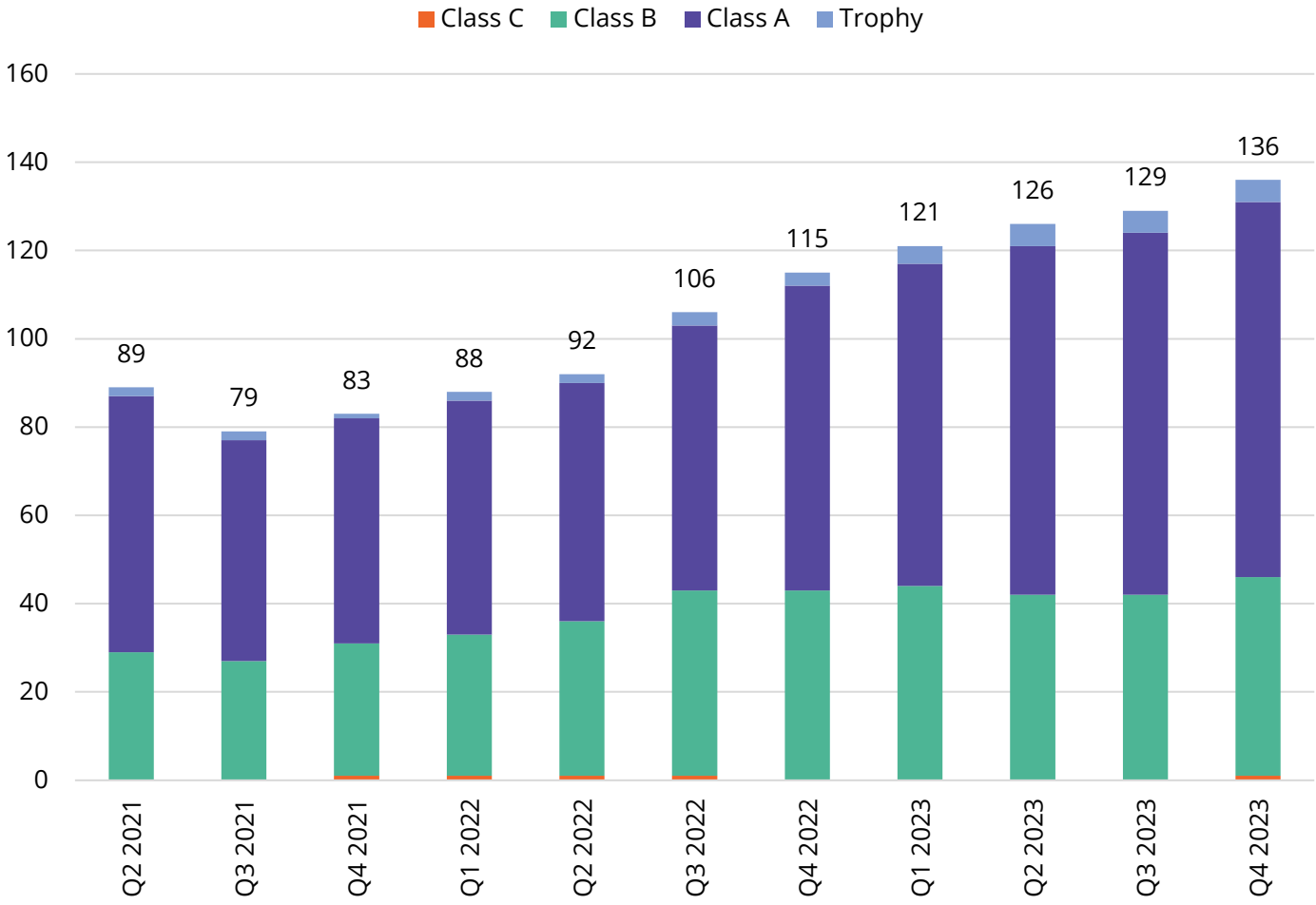
First-class amenity-rich and location-favorable spaces continue to be coveted assets, demanding premium rents. However, class A commodity space vacancy continues to increase, as cash-constrained landlords struggle to attract tenants.

Sublease availability



OpenAI's sublease of Uber's Mission Bay space mirrors the growing theme of preference for premium over commodity space. This along with expiring leases on the sublease market contributed to a 3.2% drop of sublease availability, with this trend expected to continue in 2024.

Historical office large block availability

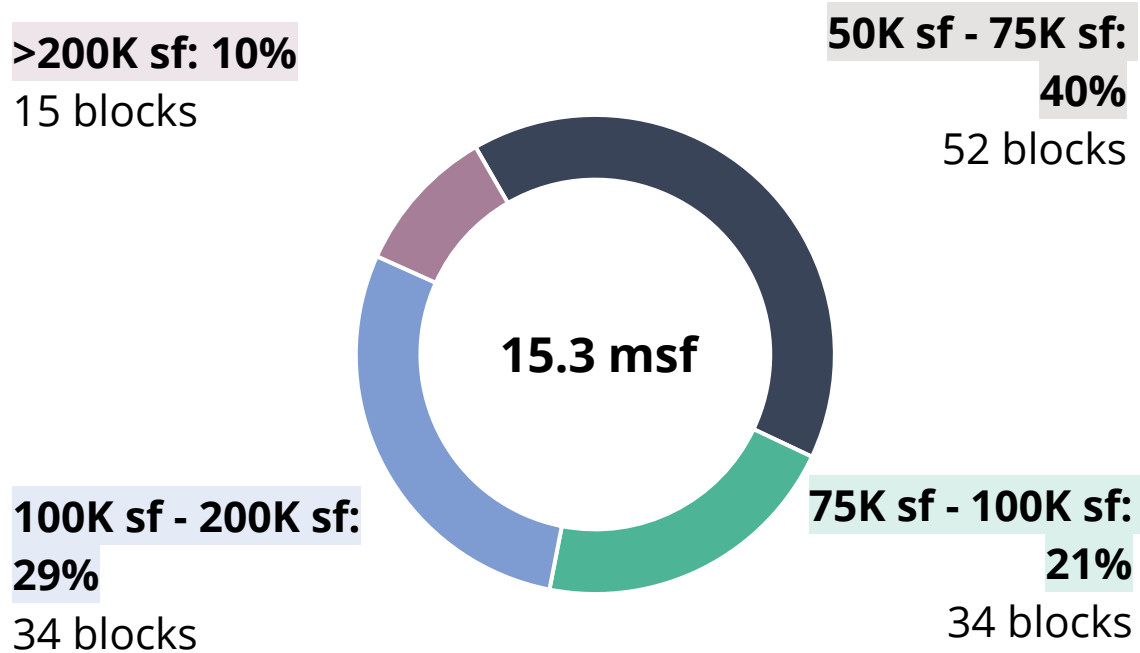


Once limited supply, large blocks are now becoming saturated in both size and number due to tenants downsizing office requirements.

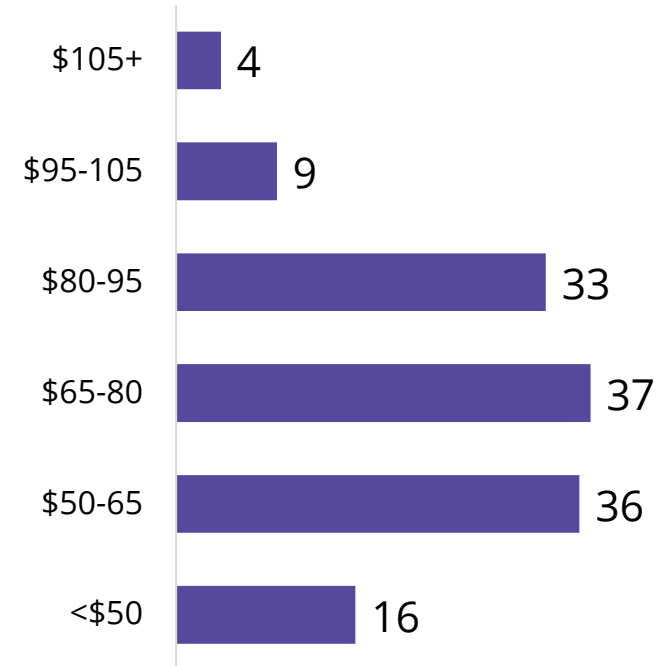
Note: Large blocks over 50k RSF
Source: AVANT by Avison Young, CoStar

Office large block availability - 50,000+

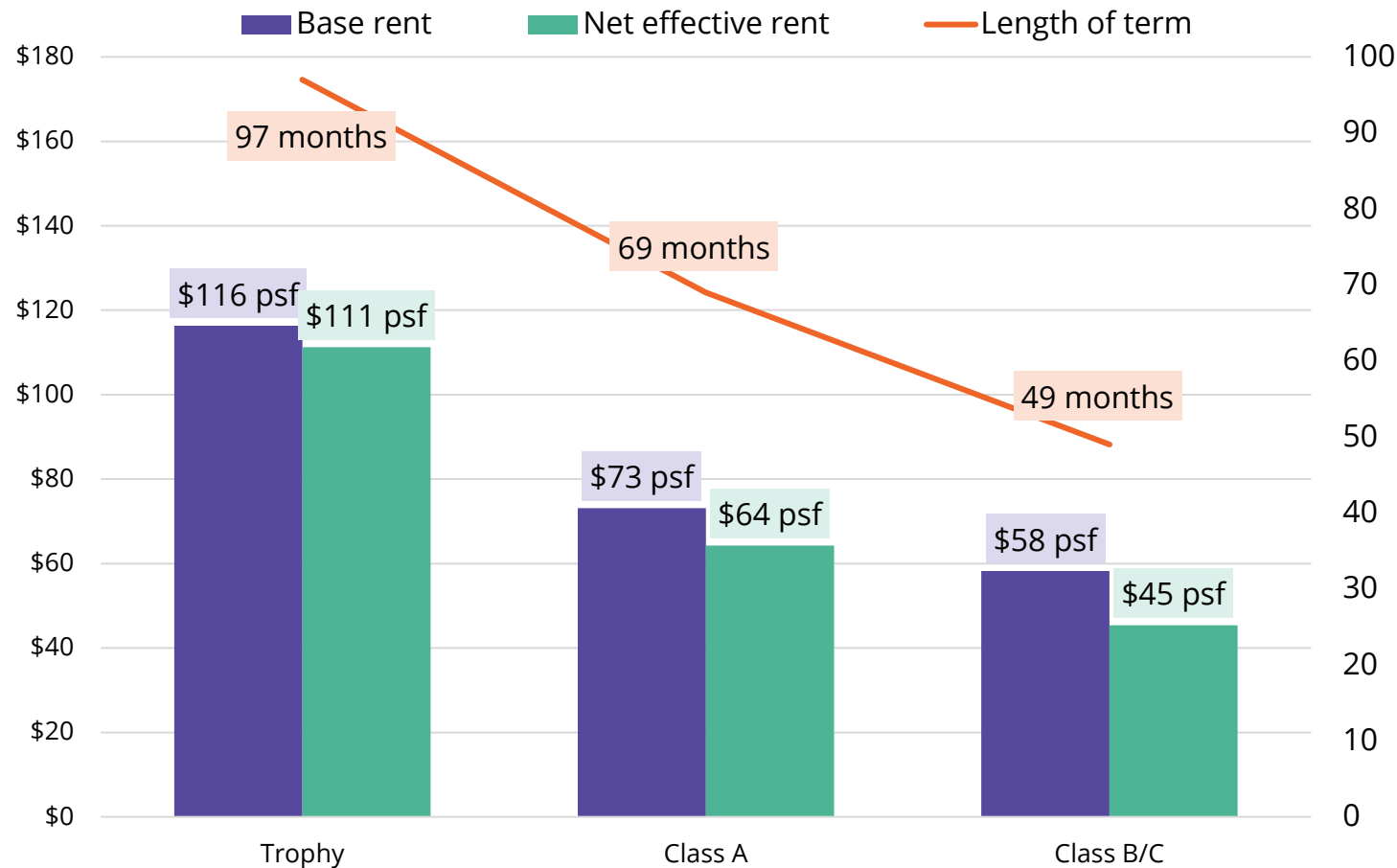
Number of blocks by size:



Asking rents FS:



Lease economics by class



Higher-quality assets are experiencing longer lease terms and a smaller gap between base and net effective rents. The correlation between premium rents and the flight to quality continues.

Leasing trends pre versus post-COVID

From 2018 through March 2020

New leases, direct relocations
66.5%

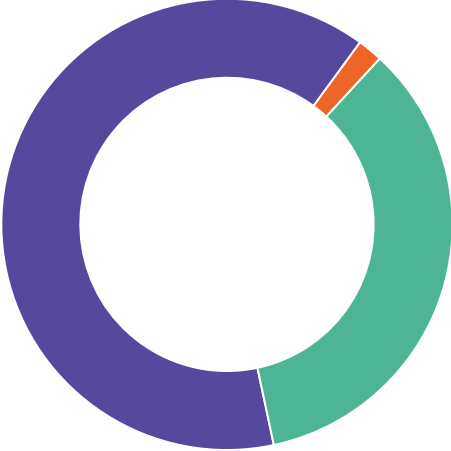


Expansions
7.3%

Direct renewals
26.2%

Leasing activity post-COVID

New leases, direct relocations
63.4%

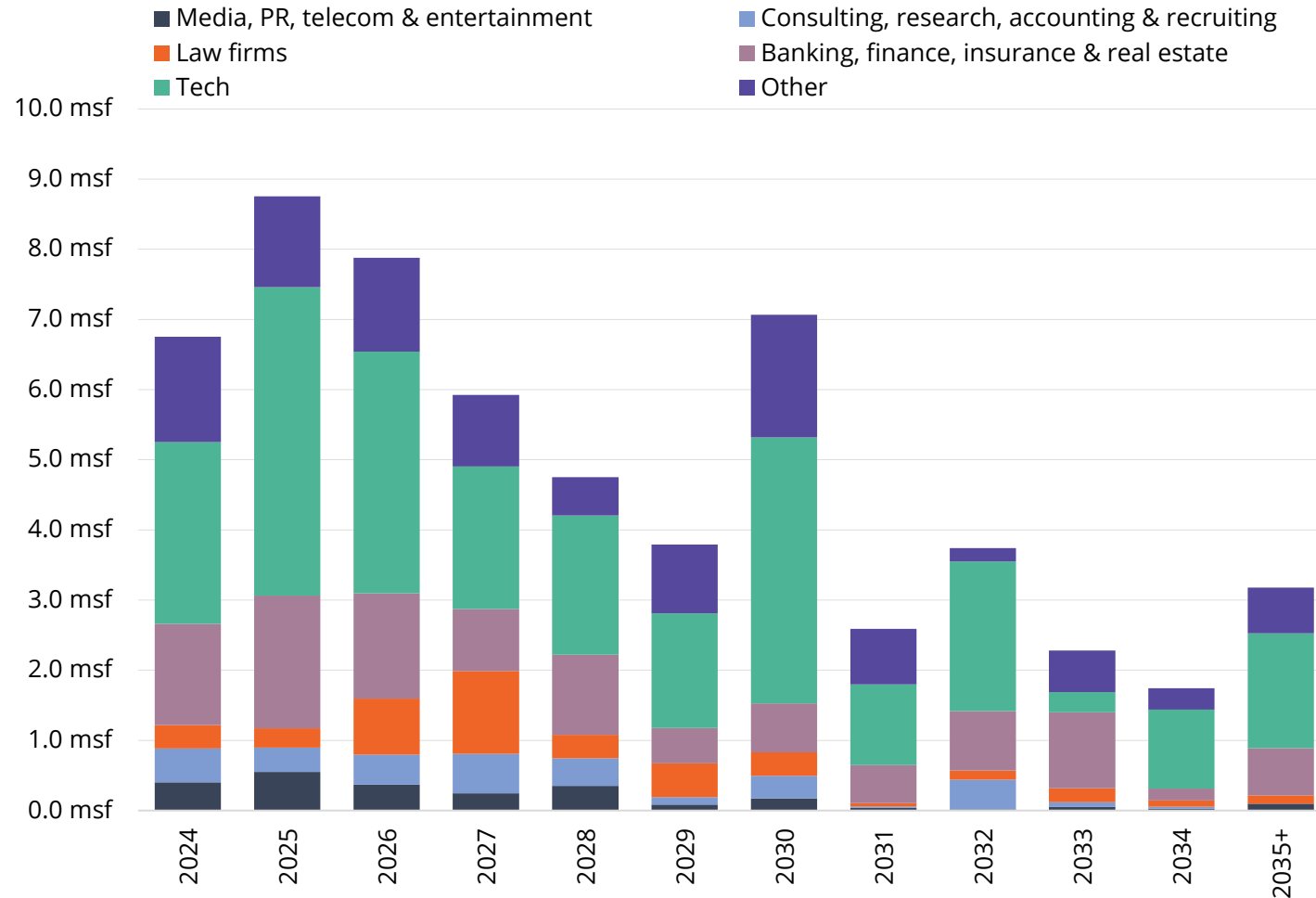


Expansions
1.8%

Direct renewals
34.8%

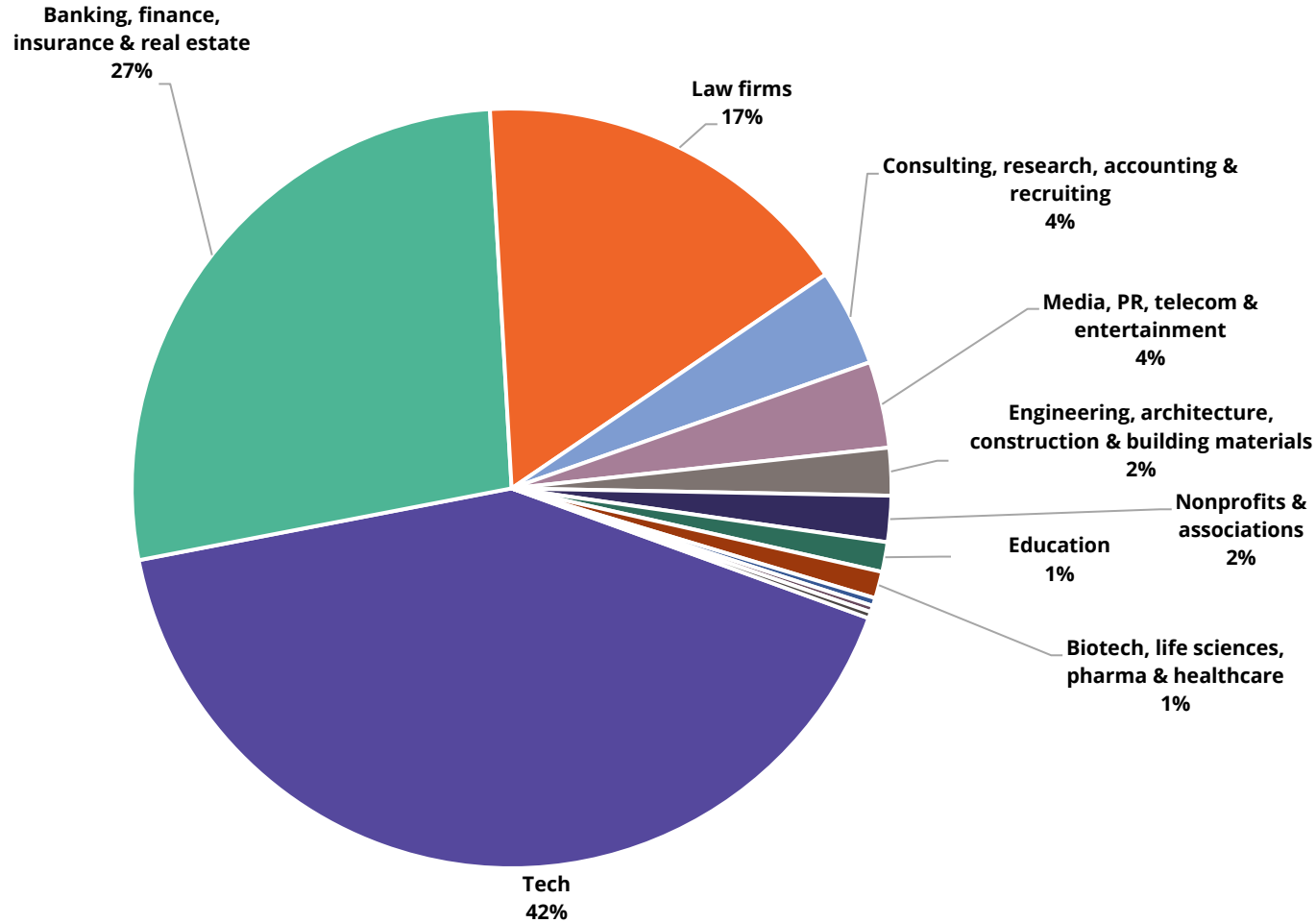
Tenants have become increasingly selective, forcing landlords to offer lucrative concession packages for new leases and renewals.

Future lease expirations by industry

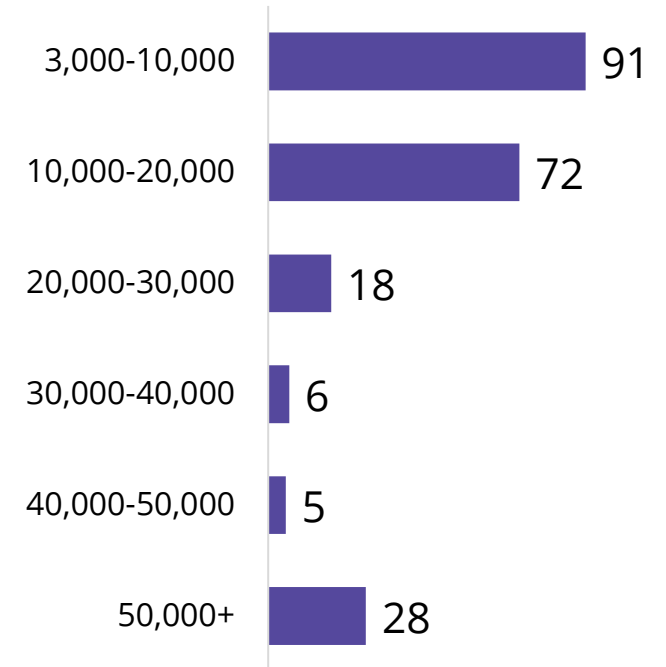


Tech companies account for 44.8% of upcoming lease expirations among major industries, with financial services trailing behind at 19.5%.

Current San Francisco tenants in the market



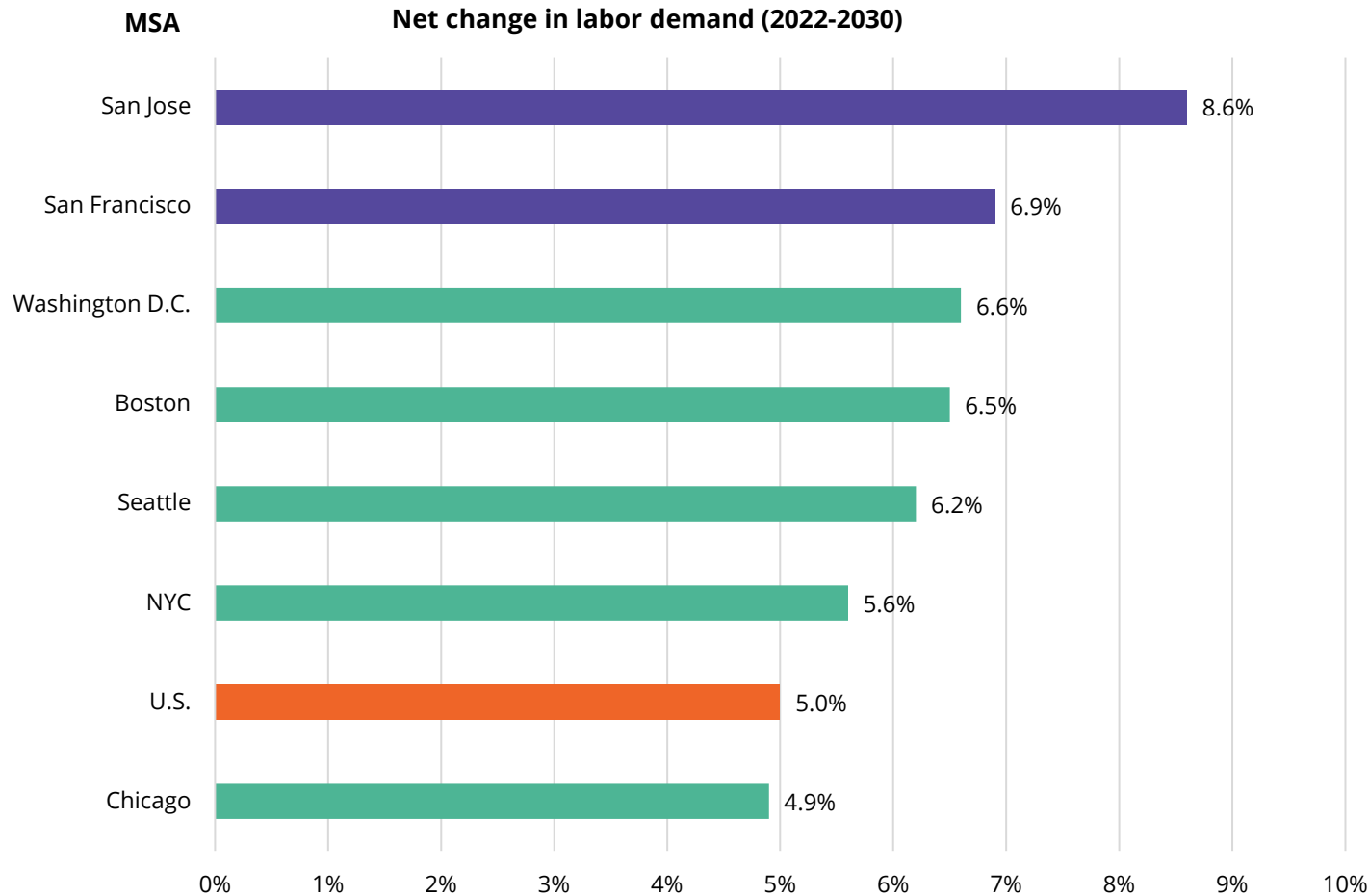
Total requirements by size



AI trends



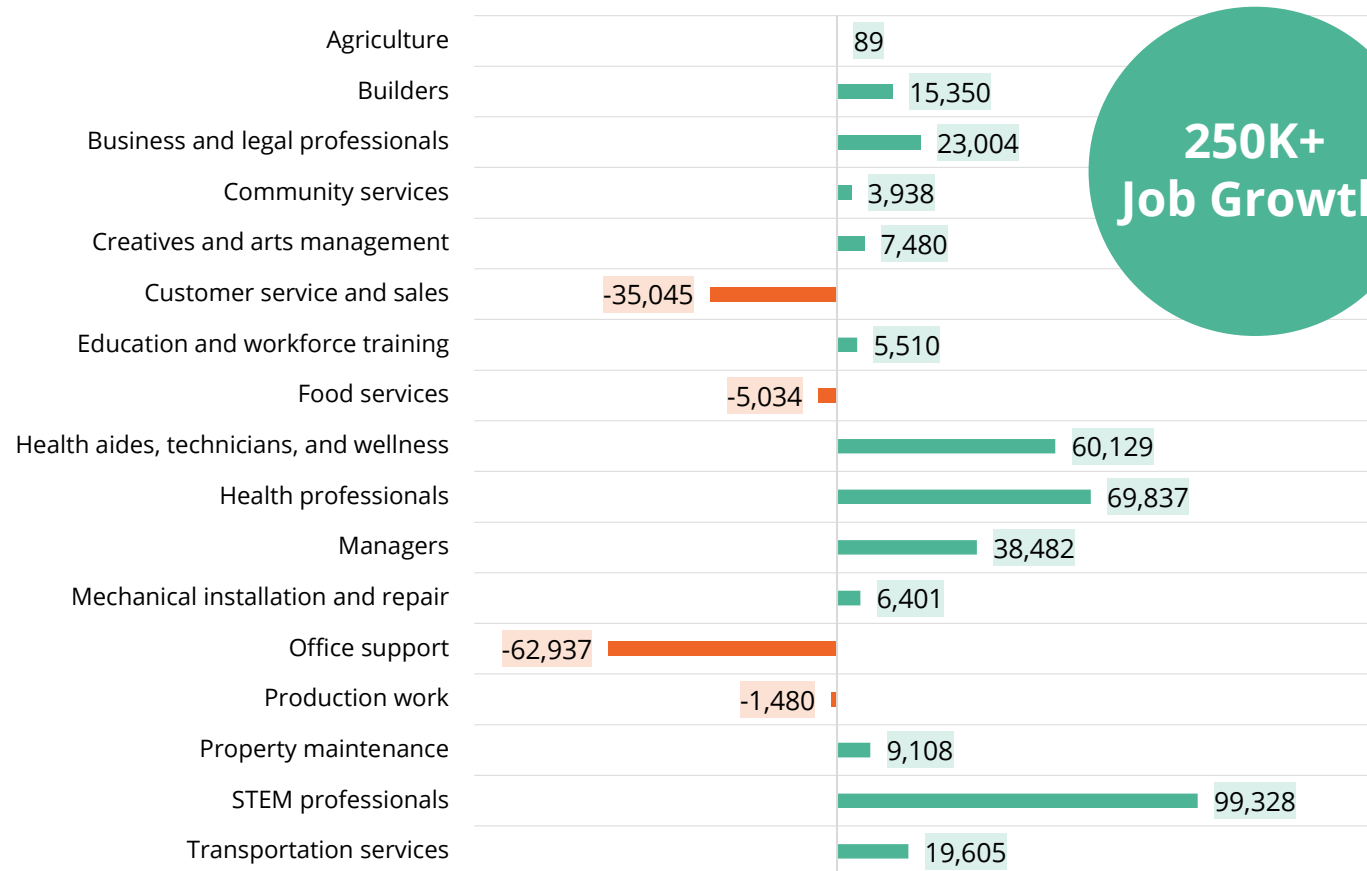
AI-driven labor demand by MSA



The two markets at the center of AI, San Francisco and San Jose, could unsurprisingly benefit the most from AI-driven changes in labor demand. MSAs with a lower concentration of college-educated workers could be the most negatively affected.

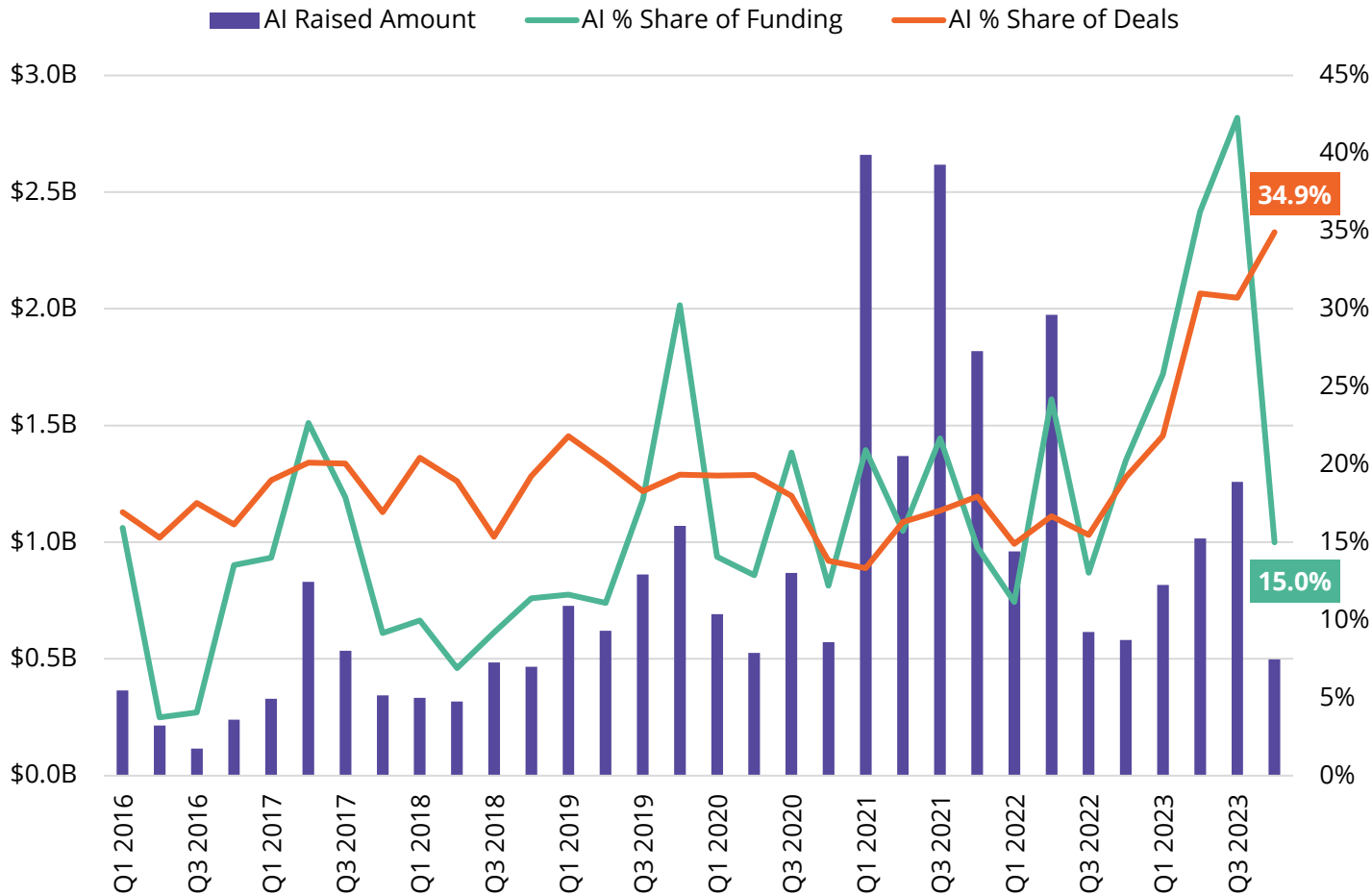
AI-driven labor demand by occupation

Net change in Bay Area labor demand (2022-2030)



San Francisco and San Jose represent the two major MSAs that could benefit the most from AI in terms of labor demand. The implementation of automated systems would drastically reduce the need for office support and customer service, while driving demand for STEM and healthcare occupations.

San Francisco VC funding for AI dominates

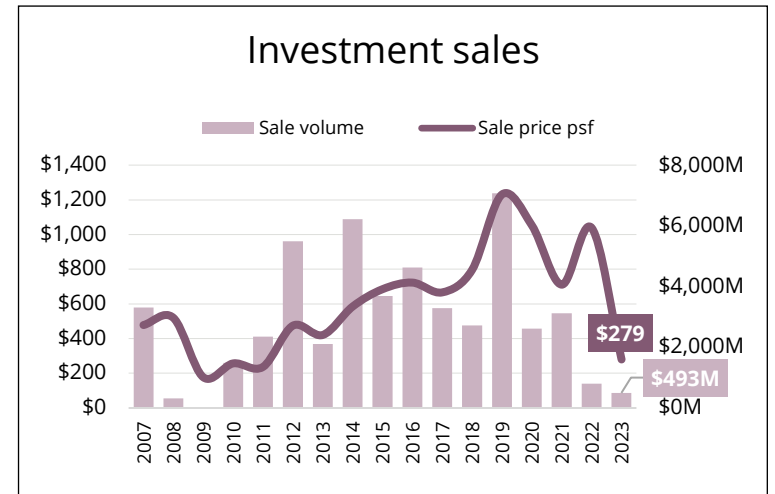
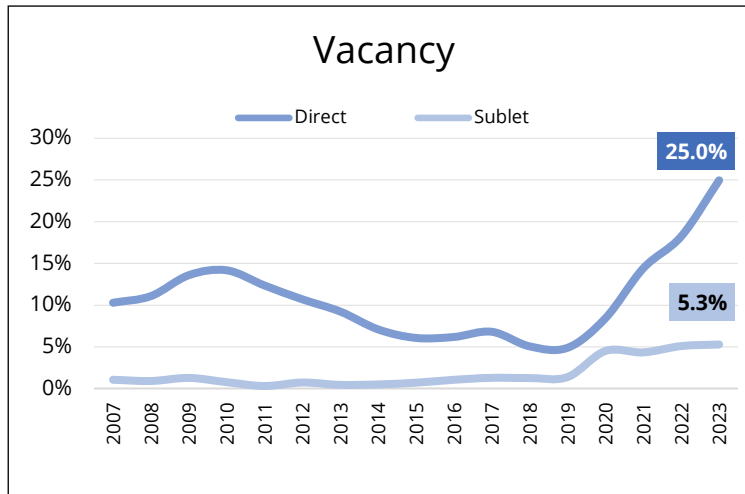
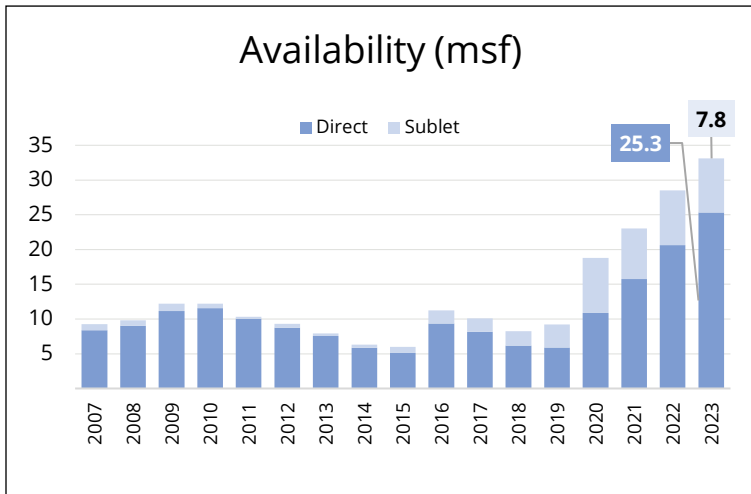
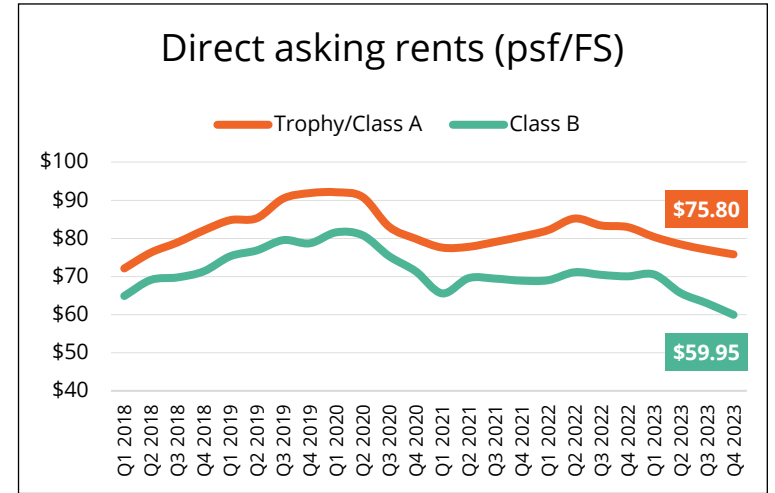
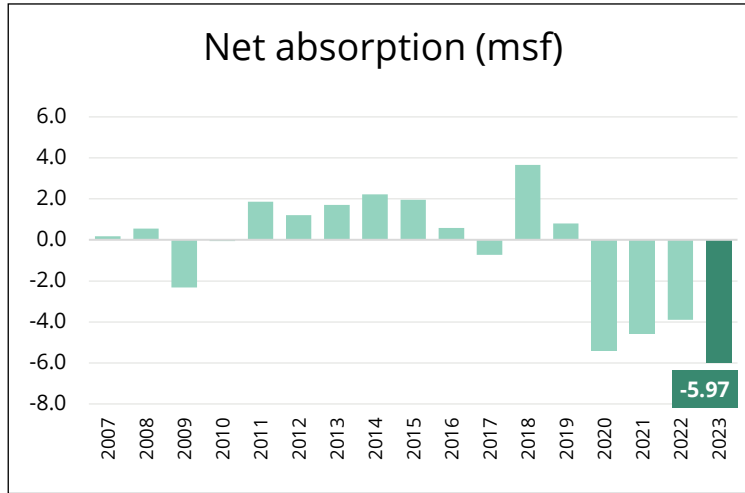
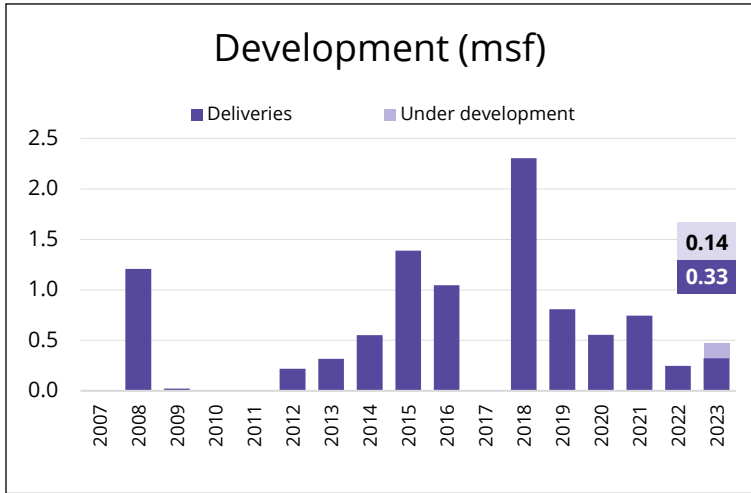


San Francisco's AI boom saw over \$3.5B in funding in 2023, accounting for 29.3% of the market's total funding. Despite a 60.5% drop in total funding for AI companies from the previous quarter, there was a 13.7% increase in the share of deals, signaling a shift towards early-stage companies.

Appendix



San Francisco office market indicators



San Francisco office market stats

	Existing inventory sf	Deliveries sf (YTD)	Under development sf	Direct vacancy	Sublet vacancy	Total vacancy	Net absorption sf (Q4 2023)	Net absorption sf (YTD)	Direct asking rent FS
Financial District	28,563,868	0	0	27.1%	3.4%	30.6%	(435,634)	(1,700,186)	\$69.88
South Financial District	27,286,442	0	0	20.7%	6.5%	27.2%	(438,499)	(2,257,962)	\$72.28
CBD Total	55,850,310	0	0	24.0%	4.9%	28.9%	(874,133)	(3,958,148)	\$70.95
Chinatown/Nob Hill/Russian Hill	105,570	0	0	17.4%	5.7%	23.1%	(18,042)	(24,401)	n/a
Jackson Square	1,909,445	0	0	21.9%	1.8%	23.7%	34,662	64,098	\$55.40
MidMarket	4,477,124	0	0	30.8%	8.9%	39.6%	(608,053)	(883,513)	\$59.80
Mission	910,492	0	0	32.2%	0.0%	32.2%	(42,153)	(88,816)	\$71.00
Mission Bay	1,853,239	300,000	0	29.6%	1.3%	30.9%	30,784	51,773	\$109.08
Outer San Francisco	1,212,250	0	0	6.1%	0.0%	6.1%	13,725	37,930	\$45.00
Potrero Hill	1,095,605	0	0	27.3%	7.7%	35.0%	46,958	(233,681)	\$63.64
Rincon Hill/South Beach	5,703,641	0	0	23.0%	8.9%	31.9%	(41,498)	(463,062)	\$59.66
Showplace Square	3,382,166	0	51,409	24.1%	9.9%	34.0%	4,687	(152,799)	\$57.60
South of Market	874,596	25,000	93,138	27.9%	8.0%	35.9%	(53,101)	(59,828)	\$53.84
Union Square	4,015,776	0	0	24.9%	3.6%	28.5%	(57,065)	(64,714)	\$38.09
Van Ness Corridor	1,628,858	0	0	14.6%	0.1%	14.8%	2,525	28,138	\$74.81
Waterfront/North Beach	3,240,626	0	0	26.0%	5.1%	31.1%	(104,325)	(89,420)	\$84.86
Yerba Buena	3,718,149	0	0	42.7%	6.1%	48.8%	(19,217)	(134,361)	\$71.66
Non-CBD Total	34,127,537	325,000	144,547	26.6%	5.9%	32.4%	(810,113)	(2,012,656)	\$71.19
Market total	89,977,847	325,000	144,547	25.0%	5.3%	30.2%	(1,684,246)	(5,970,804)	\$69.88

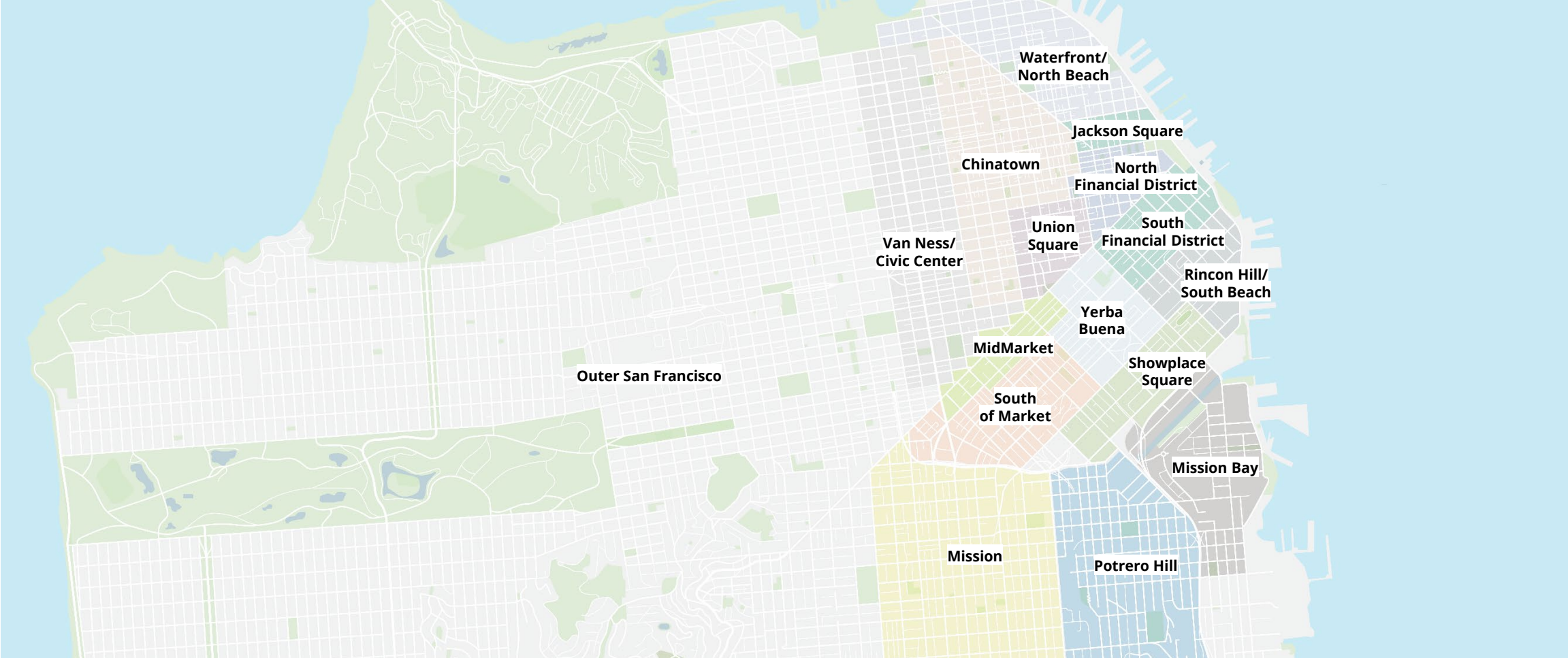
The charts and statistics in this report are composed by Class A, B, and C, non-owner-occupied office buildings 20,000 sf and above in the submarkets listed above.

San Francisco office market stats by class

	Existing inventory sf	Deliveries sf (YTD)	Under development sf	Direct vacancy	Sublet vacancy	Total vacancy	Net absorption sf (Q3 2023)	Net absorption sf (YTD)	Direct asking rent FS
Trophy	8,630,431	0	0	14.6%	3.9%	18.5%	33,826	(296,044)	\$98.52
Class A	29,902,415	300,000	0	25.2%	5.4%	30.6%	(217,774)	(1,361,425)	\$72.63
Class B	47,615,062	0	0	27.2%	5.7%	32.9%	(1,467,960)	(4,157,275)	\$59.95
Class C	3,829,939	25,000	144,547	18.2%	2.1%	20.2%	(32,338)	(156,060)	\$48.32
Market total	89,977,847	325,000	144,547	25.0%	5.3%	30.2%	(1,684,246)	(5,970,804)	\$71.19

The charts and statistics in this report are composed by Class A, B, and C, non-owner-occupied office buildings 20,000 sf and above in the submarkets listed above.

San Francisco submarket map



Office insights glossary of terms

Demand

- **Leasing activity:** total square footage of relocations, renewals, expansions and subleases expressed when the leases are signed, not when tenants take physical occupancy of the space
- **Absorption:** period-over-period change in occupied square footage

Supply

- **Direct vacancy rate:** space operated by landlords that is ready for immediate occupancy
- **Sublease vacancy rate:** space operated by sublandlords that is ready for immediate occupancy
- **Total vacancy rate:** sum of direct vacancy rate and sublease vacancy rate
- **Availability rate:** space that is vacant plus space that will become vacant over an indefinite time horizon, including spaces that are occupied by vacating tenants and under-construction properties

Office rents and concessions

- **Asking rents:** pricing guidance provided by landlords to tenants for available space expressed as full service (FS)
- **Base rents:** fair market value of market-level lease pricing based on representative executed leases, expressed as full service (FS)
- **Free rent period:** months of free rent that are typically provided upfront by landlords to tenants as a concession to offset the total cost of a lease and/or the construction timeline of an office suite
- **Tenant improvement allowance:** an allowance expressed in dollars per square foot provided from landlords to tenants to offset build-out, engineering, space planning and related permit costs
- **Net effective rent:** base rents discounted by the dollar values of tenant improvement allowance and free rent concessions expressed as full service (FS)

Capital markets

- **Investment volume:** office sales dollars expressed when the transactions close and based on inventory thresholds; partial-interest sale dollar amounts are not grossed-up to reflect the 100% value of the sale
- **Asset pricing:** unweighted average per-square-foot asset pricing of market-level closed sales
- **Cap rate:** net operating income divided by sale price; this measurement of market-level investment returns is calculated as an unweighted average based on closed investment sales

For more market insights and
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