

SAN FRANCISCO OFFICE MARKET

DROP IN ABSORPTION

San Francisco experienced the largest drop in absorption in nearly two decades, at negative 3.1 million square feet. While 1/3 of that is attributed to the delivery of the Uber campus at Mission Bay, which is not yet occupied, the remaining 2.1 million square feet of negative absorption is the greatest single-quarter drop since the beginning of 2001. As a result, vacancy jumped 360 basis points to 7.6% and availability increased 290 basis points to 14.2%. Nearly 65% of the increase in availability in the second quarter came from sublease space, which grew by 1.7 million square feet, or 46.9%. At 5,214,633 square feet, sublease availability has more than tripled over the last year and is expected to increase further.

The increase in available space came with only a small decrease in overall asking rents, which ended the quarter at \$84.39/SF, a drop of 2.4% since last quarter and just 0.6% less than year ago. Much of the overall drop came from the bottom of the market, with Class C rents falling 7.2% quarter-over-quarter to \$62.49/SF. At \$90.31/SF, Class A rents dropped only 1.8% since the first quarter and remain 1.1% higher than the mid-point of last year. Class B rates of \$77.08/SF fell just 1.7% quarter-over-quarter but have fallen 2.9% year-over-year. Overall sublease asking rates are 7.8% lower than direct rates at \$77.79/SF, although Class A sublease rates of \$79.08/SF offer a discount of 12.4% for that class. Further drops to asking rates are expected in coming months.

LEASING SLOWS

Leasing volume in the second quarter dropped to just over 350,000 square feet, only about 16% of the average quarterly leasing in 2019. Since the prohibition on touring contributed to this slowdown, it is not surprising that the top deals of the quarter were renewals, which are not included in the leasing tally. Morgan Lewis renewed 152,293 square feet at One Market Street, and First Republic Bank renewed 116,805 square feet at 388 Market Street; both companies downsized by a floor in the process. Additionally, the San Francisco AIDS Foundation renewed 45,322 square feet at 1035 Market Street and the Bleacher Report renewed 34,027 square feet at 153 Kearny Street. Airtable signed the largest sublease of the quarter, taking 48,812 square feet from Lever at 155 Fifth Street. The largest new direct lease signed this quarter was by User Testing, which leased 45,000 square feet at 144 Townsend Street.

A bright spot on the horizon is the handful of tenants beginning to inquire about spaces after putting requirements on hold early in the quarantine. Fortunately, the San Francisco office market entered this

CURRENT CONDITIONS

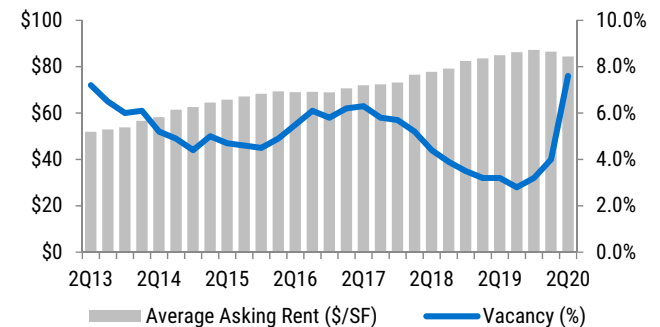
Overall vacancy increased by 360 basis points to 7.6%, and Class A vacancy increased 430 basis points to 7.4%.

Availability increased by more than 1.5 million square feet for the third quarter in a row, increasing from 9.5 million square feet last quarter to 12.1 million square feet.

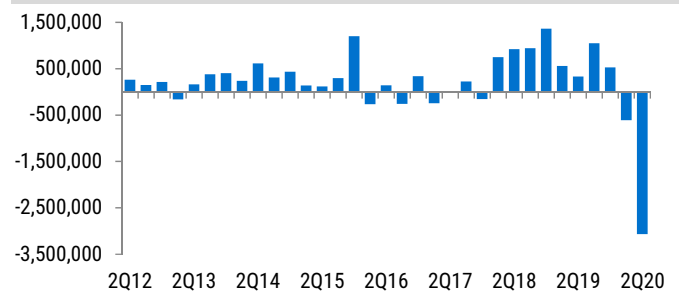
Class A direct average asking rates fell slightly to \$90.31/SF, and overall direct asking rates decreased to \$84.39/SF.

MARKET ANALYSIS

Asking Rent and Vacancy



Net Absorption (SF)



MARKET SUMMARY

	Current Quarter	Prior Quarter	Year Ago Period	12 Month Forecast
Total Inventory	85.5M SF	84.3M SF	83.5M SF	↑
Vacancy Rate	7.6%	4.0%	3.2%	↑
Quarterly Net Absorption	-3.1M SF	-612K SF	328K SF	↓
Average FS Asking Rent	\$84.39/SF	\$86.44/SF	\$84.89/SF	↓
Under Construction	2.0M SF	3.3M SF	3.3M SF	↑
Deliveries	1.0M SF	0 SF	736K SF	↑

period of uncertainty with strong underlying fundamentals, which could potentially result in a quick and healthy rebound.

INVESTMENT SALES

The investment sales pace has slowed for both in-contract transactions as well as the launching of new marketing campaigns. As shelter-in-place is eased and third parties are allowed on-site, the rate of closing is anticipated to increase. Properties that were still pending sale at the end of the quarter included San Francisco's iconic Transamerica Pyramid, which was put under contract by SHVO/BVK/Deutsche Finance America as part of a 756,181-square-foot, three-property portfolio which includes 505 and 545 Sansome Street. Other pending transactions included 50 First Street, reportedly in contract with Chinese buyer Hony Capital for \$1.2 billion, 123 Townsend Street, and 123 Mission Street. Notably, 555 California hit the market with a price tag north of \$2 billion, testing the liquidity within the core market. San Francisco is still an attractive investment

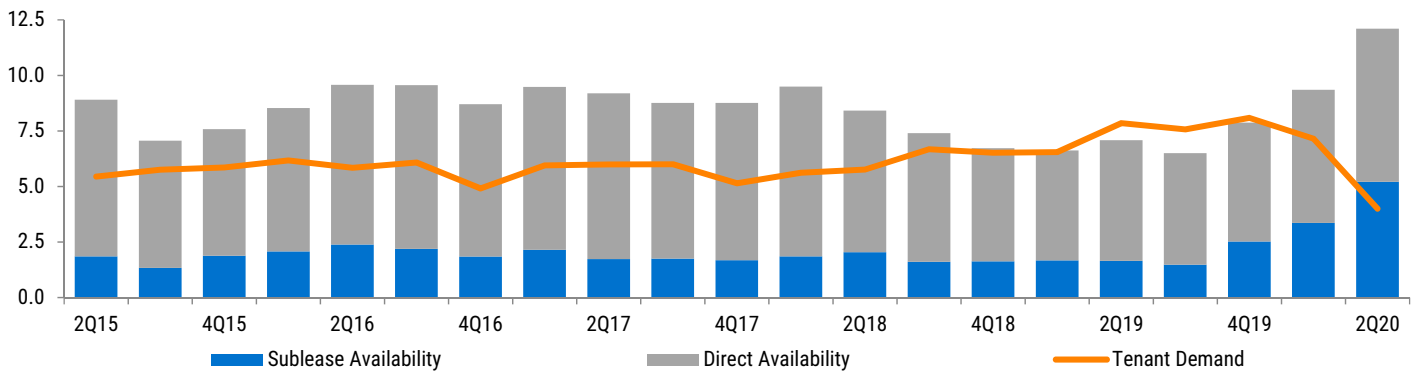
market that has a history of market fundamentals rebounding before most of the rest of the country, and it is anticipated that investors will take advantage of opportunities here once the path forward is clearer.

ECONOMIC OUTLOOK

San Francisco's unemployment rate as of May was 12.6%, a stark contrast to the sub-3.0% rate in place since third-quarter 2017. Glassdoor reports that total job openings in San Francisco in June had dropped 31.0% from pre-COVID job listings. On June 15, San Francisco began allowing offices open for employees who are needed to keep offices running and cannot work from home, although offices with 20 or more staff can operate at no more than 20.0% of maximum occupancy. San Francisco currently has no timeline available for further office openings. The squeeze on market conditions are expected to remain until at least there is a more concrete reopening timeline in place.

HISTORICAL AVAILABILITY AND TENANT DEMAND

Square Feet, Millions



SELECT LEASE TRANSACTIONS

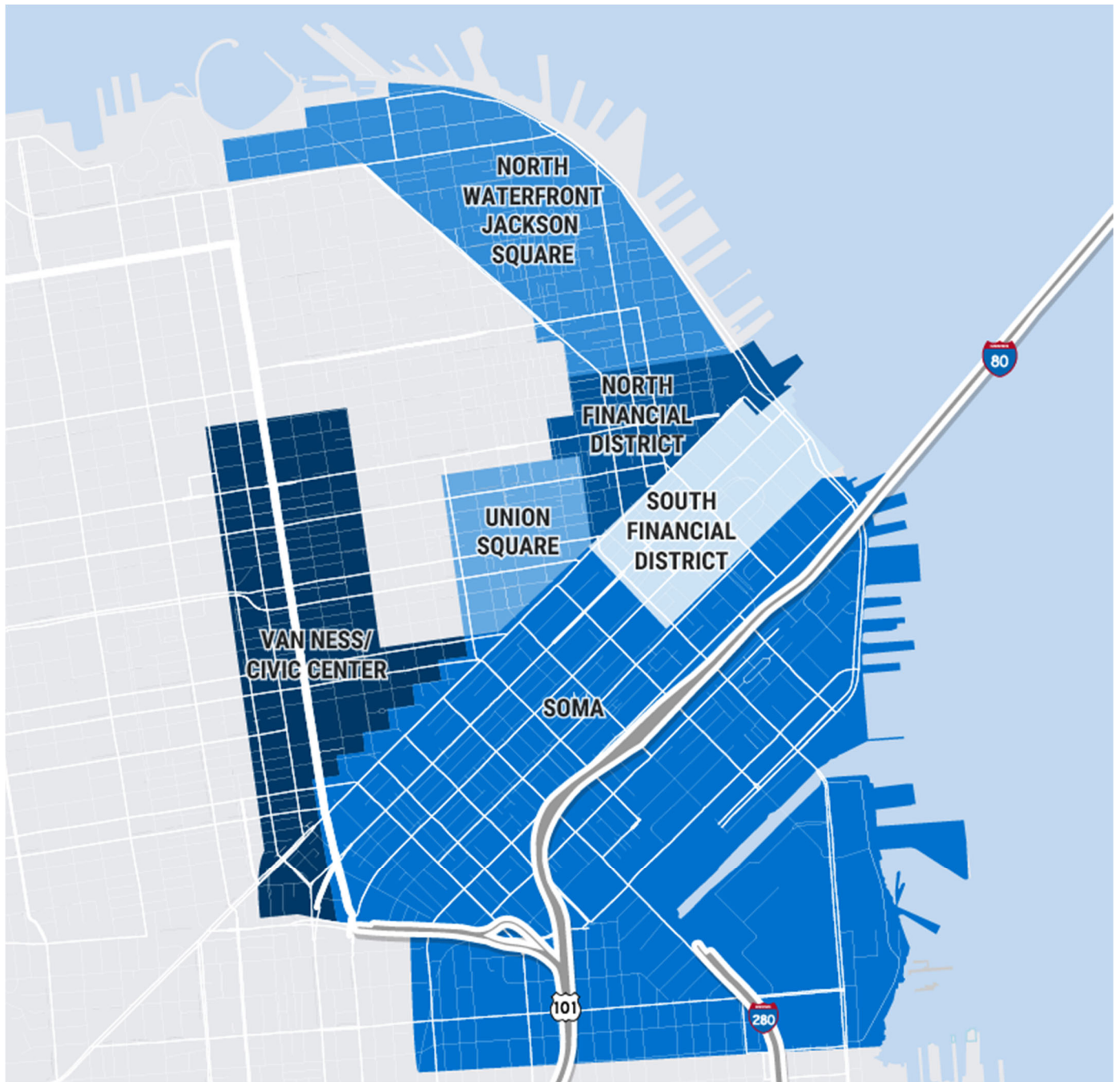
Tenant	Building	Submarket	Type	Square Feet
Morgan Lewis	1 Market Street (Spear Street Tower)	South Financial District	Renewal	152,293
First Republic Bank	388 Market Street	North Financial District	Renewal	116,805
Airtable	155 Fifth Street	Central SOMA/Yerba Buena	Sublease	48,812
San Francisco AIDS Foundation	1035 Market Street	Mid Market	Renewal	45,322
User Testing	144 Townsend Street	East SOMA	New	45,000
Bleacher Report	153 Kearny Street	Union Square	Renewal	34,027
Allstate Insurance	650 Davis Street	Waterfront North/Jackson Square	Renewal	27,480
Constellation Brands	101 Mission Street	South Financial District	New	26,914
Sitecore	101 California Street	North Financial District	Renewal	25,000
Lob.Com	210 King Street	Central SOMA/Yerba Buena	Sublease	24,950

SUBMARKET STATISTICS – ALL CLASSES

	Total Inventory (RSF)	Under Construction (RSF)	Total Vacancy Rate	Total Availability Rate	Qtr Net Absorption (RSF)	YTD Net Absorption (RSF)	Class A Asking Rent (Price/SF)	Class B Asking Rent (Price/SF)	Direct FS Asking Rent (Price/SF)
North Financial District	28,281,078	0	6.9%	13.8%	(567,273)	(775,229)	\$89.78	\$83.31	\$87.88
South Financial District	26,588,807	956,968	4.8%	12.4%	(645,064)	(760,086)	\$91.72	\$89.22	\$90.42
SOMA	19,601,890	1,040,000	11.6%	14.8%	(1,473,249)	(1,623,662)	\$95.84	\$74.83	\$79.21
Union Square	3,623,871	0	12.3%	19.3%	(173,324)	(216,095)	\$84.85	\$69.03	\$71.34
Van Ness/Civic Center	1,803,770	0	10.9%	22.4%	(54,726)	(45,380)	\$64.36	\$59.62	\$57.55
N Waterfront/Jackson Sq	5,566,238	0	7.1%	16.5%	(155,828)	(260,605)	\$91.90	\$79.70	\$83.36
San Francisco	85,465,654	1,996,968	7.6%	14.2%	(3,069,464)	(3,681,057)	\$90.31	\$77.08	\$84.39

SUBMARKET STATISTICS – CLASS A

	Total Inventory (RSF)	Under Construction (RSF)	Total Vacancy Rate	Total Availability Rate	Qtr Net Absorption (RSF)	YTD Net Absorption (RSF)	Class A Asking Rent (Price/SF)
North Financial District	21,655,509	0	6.2%	12.3%	(453,642)	(629,916)	\$89.78
South Financial District	23,992,815	956,968	4.6%	11.3%	(629,904)	(714,647)	\$91.72
SOMA	10,403,065	1,040,000	15.7%	13.6%	(1,255,905)	(1,392,066)	\$95.84
Union Square	535,837	0	21.2%	54.6%	(86,835)	(86,835)	\$84.85
Van Ness/Civic Center	342,693	0	21.2%	23.0%	(33,406)	(19,416)	\$64.36
N Waterfront/Jackson Sq	1,964,187	0	4.5%	18.5%	(47,437)	(66,359)	\$91.90
San Francisco	58,894,106	1,996,968	7.4%	12.8%	(2,507,129)	(2,909,239)	\$90.31



NEWMARK KNIGHT FRANK

One Bush Street, Suite 1500
San Francisco, CA 94104
415.445.5155
Corporate CA RE #: 00832933

ANDREA ARATA

Research Director
415.445.5133
aarata@ngkf.com

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