Office Insight

San Francisco| Q2 2015

San Francisco's shifting supply and demand

Increasingly competitive market drives rent growth

Only three contiguous blocks over 50,000 square feet are available in existing buildings. With more than 35 tenants in the market for space 50,000 square feet or larger, the supply-demand imbalance is increasing competition and pushing rents upward. North Financial District (NFD) has the most availabilities on the market, as traditional large tenants, including legal and financial firms, continue to consolidate, creating opportunity for tenants looking for larger blocks. Southern submarkets remain in high demand with the majority of large leases having been signed there in the last six months. The NFD could provide relief for tenants who wish to remain in the CBD but cannot compete with South Financial District prices.

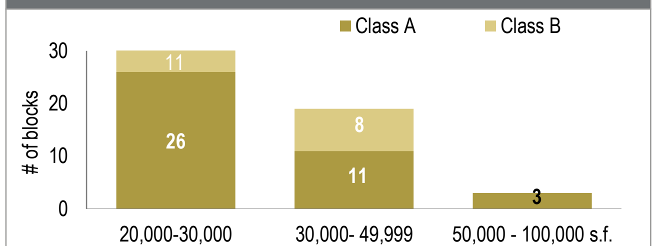
Class B and C rents rise as preferences change

Tech tenants driving the market gravitate toward less traditional office space, preferring high ceilings, operable windows, and unique architectural features. As a result, Class B and C buildings have seen 8.9 and 12.0 percent year-over-year rent growth, respectively, outpacing the overall market. New developments are incorporating these space preferences and including open floor plans and creative touches in the design. These shifting preferences could create opportunities for other tenants to take on more traditional space that is less in demand. Continued upward pressure on asking rates and concessions compression is expected in the remainder of 2015.

Approaching Prop M limit

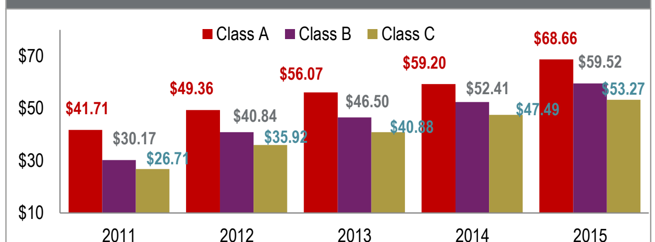
Although more than three million square feet of construction is underway, the majority is preleased, and new development is still constrained by the Prop M development cap. Currently, there are more than 11 million square feet of projects filed with the Planning Department, but only 2.4 million square feet left for allotment. At the rate of job growth and leasing activity, supply restrictions will favor landlords and hurt tenants as rents continue to grow. Smaller and non-tech tenants are the most at risk and may start to seek space outside the city. Prop M's supply limitations create a more demand-heavy competitive market that ultimately hurts tenants ability find affordable office space.

Dismal supply of existing large blocks



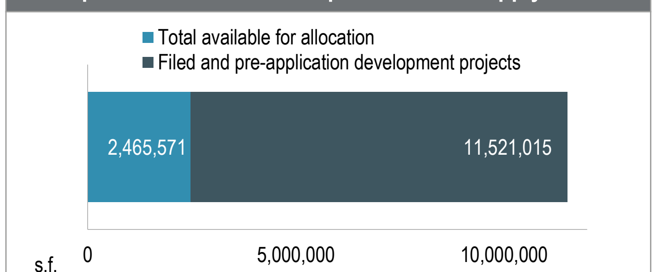
Source: JLL Research

Gap between Class A and B rents narrow



Source: Thomson Reuters, JLL Research

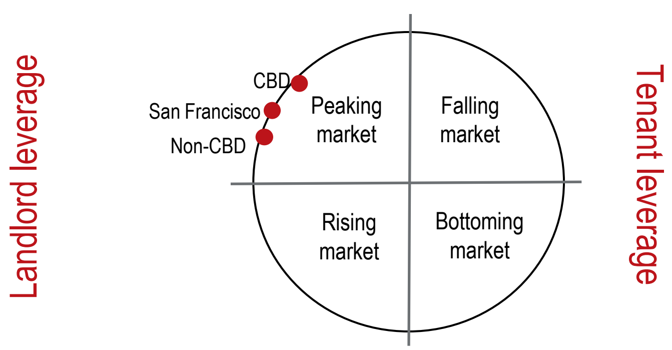
Development restrictions limit potential new supply



Source: JLL Research

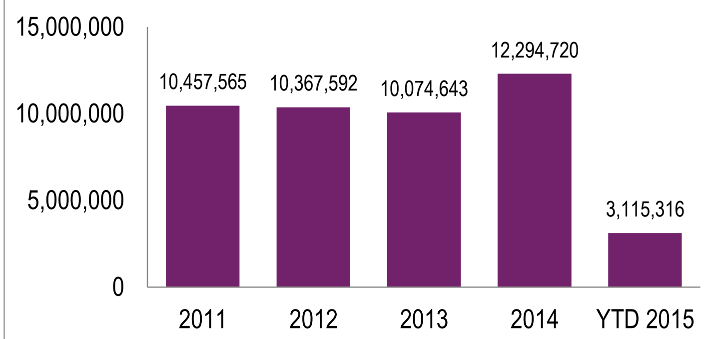
74,526,199 Total inventory (s.f.)	**447,353** Q2 2015 net absorption (s.f.)	**$66.11** Direct average asking rent	**3,134,205** Total under construction (s.f.)
9.2% Total vacancy	**826,387** YTD net absorption (s.f.)	**10.0%** 12-month rent growth	**52.5%** Total preleased

Current conditions – submarket



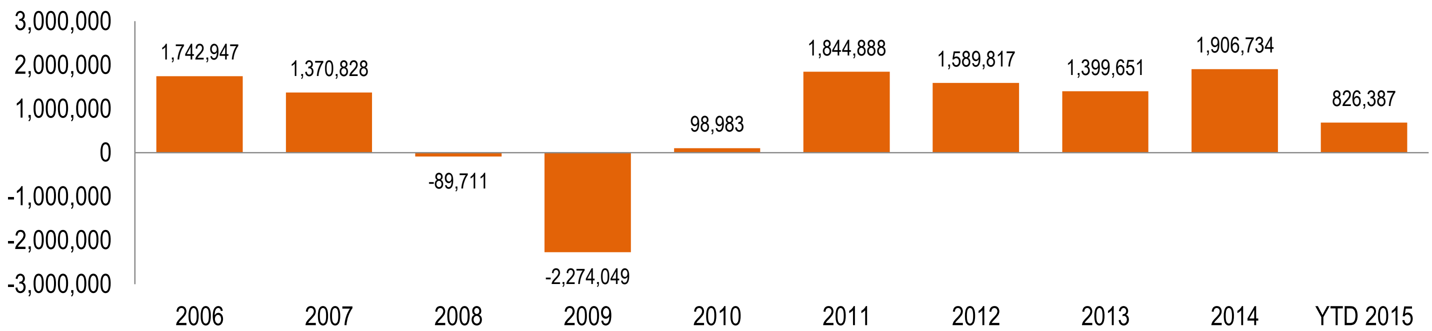
Source: JLL Research

Historical leasing activity (s.f.)



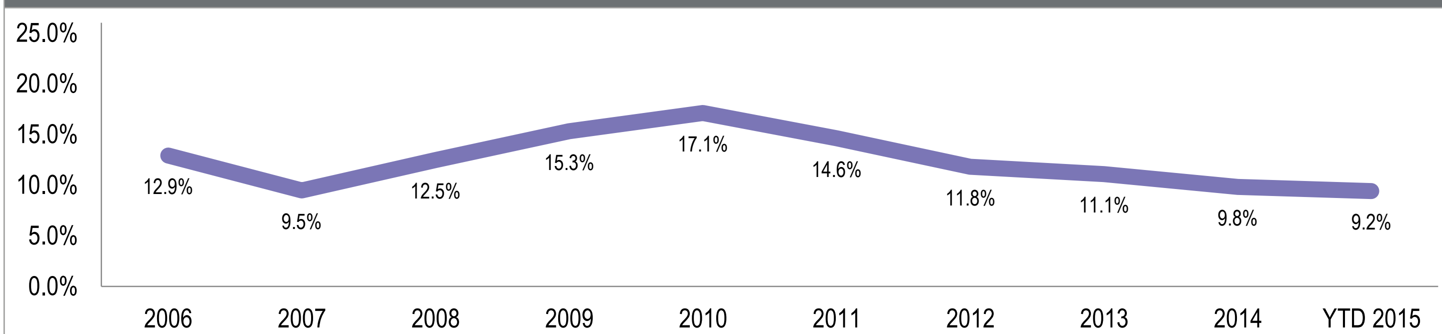
Source: JLL Research

Total net absorption (s.f.)



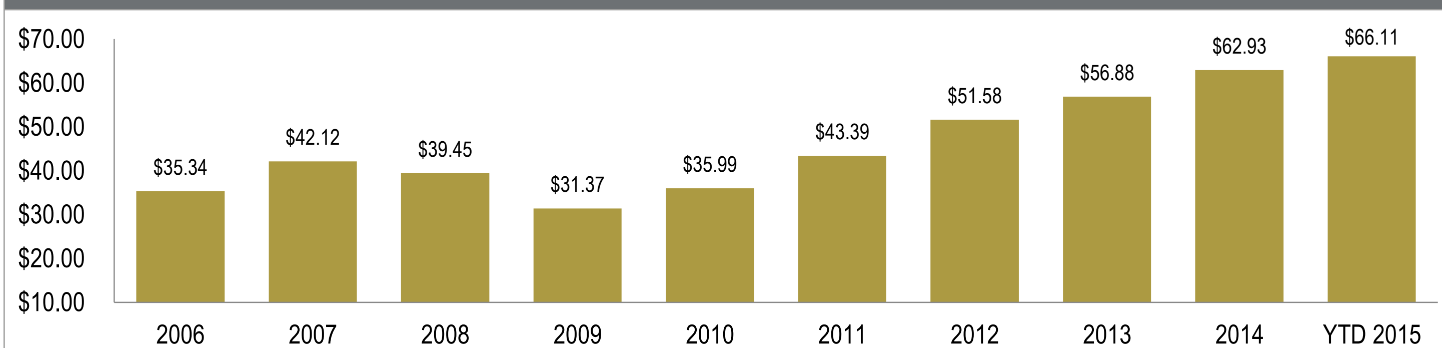
Source: JLL Research

Total vacancy rate (%)



Source: JLL Research

Direct average asking rent ($ p.s.f.)



Source: JLL Research

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