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3Q24

# Silicon Valley Office Market Overview



**NEWMARK**

# Market Observations

## Economy

- The region’s labor market showed signs of stabilizing. After two months of declines in the beginning of 2024, we have now tracked five months of modest growth, a welcome sign. While employment growth has been slower in this market relative to the U.S., the unemployment rate has remained steady indicating an equilibrium between labor supply and demand.
- Layoffs in the large tech companies outpaced employment gains in the AI space, something that we are closely monitoring. Professional and business services, such as law and consulting firms, are staffing up in anticipation of an increase in work which bodes well for the office market, especially Class A buildings.
- Following along with the overall employment showing signs of stabilizing, office-using employment remains in line with the first few months 2024 after sharp declines in the previous few months. However, the level of office-using employment is still below the peak from one year ago. Small job growth in the AI sector was not enough to counter the overall decline in the information services sector.

## Major Transactions

- There were two lease renewals over 225,000 square feet in the third quarter, including Johnson & Johnson’s renewal for 229,626 square feet in Marriott Park.
- One noteworthy trend for the first three quarters of 2024 is that the bulk of the leases signed, nearly 50%, were for new deals whereas this past two years renewals comprised most of the activity.
- We tracked at least 147 office transactions in the third quarter alone, bringing the total for the first three quarters of the year to more than 500 deals. We are currently tracking 6.7 million square feet of active tenants in the market, which is far below the 16-year market average of 8.2 million square feet.

## Leasing Market Fundamentals

- Strong leasing activity in the first and third quarters of this year, coupled with modest activity in the second quarter, signals that the market is recovering from previous lows. Net absorption was negative in the third quarter as the combination of vacant space increased and new construction was delivered to the market.
- Direct available space continues to be added to the market in the third quarter of 2024 pushing the overall vacancy rate up to 20.1% from 18.8% at year-end 2023.
- Asking rents in Silicon Valley have remained relatively steady at \$5.05/SF full service in 2024. While full service asking rents are flat, concessions, including TIs and free rent, still play a big part in lease negotiations. In addition, as companies continue to look for ways to bring employees back to the office, amenities including flexible workspaces, more conference rooms, and up-to-date infrastructure also play a big role.

## Outlook

- Positive signs suggest an inflection point in the economy, but headwinds like the amount of available space, higher interest rates, election jitters, and ongoing tech right-sizing could cause further demand/supply imbalances.
- We are closely watching the AI space, tracking the investments and also leasing activity. As AI companies expand, law firms and professional and business services firms are growing as well to be located near these AI companies.
- We believe vacancy rates will likely hover around or even slightly above their current levels while any real growth in asking rents will remain muted in the short term. As the economy improves in the medium term, we expect market conditions will once again improve.

1. Economy
2. Leasing Market Fundamentals
3. Appendix

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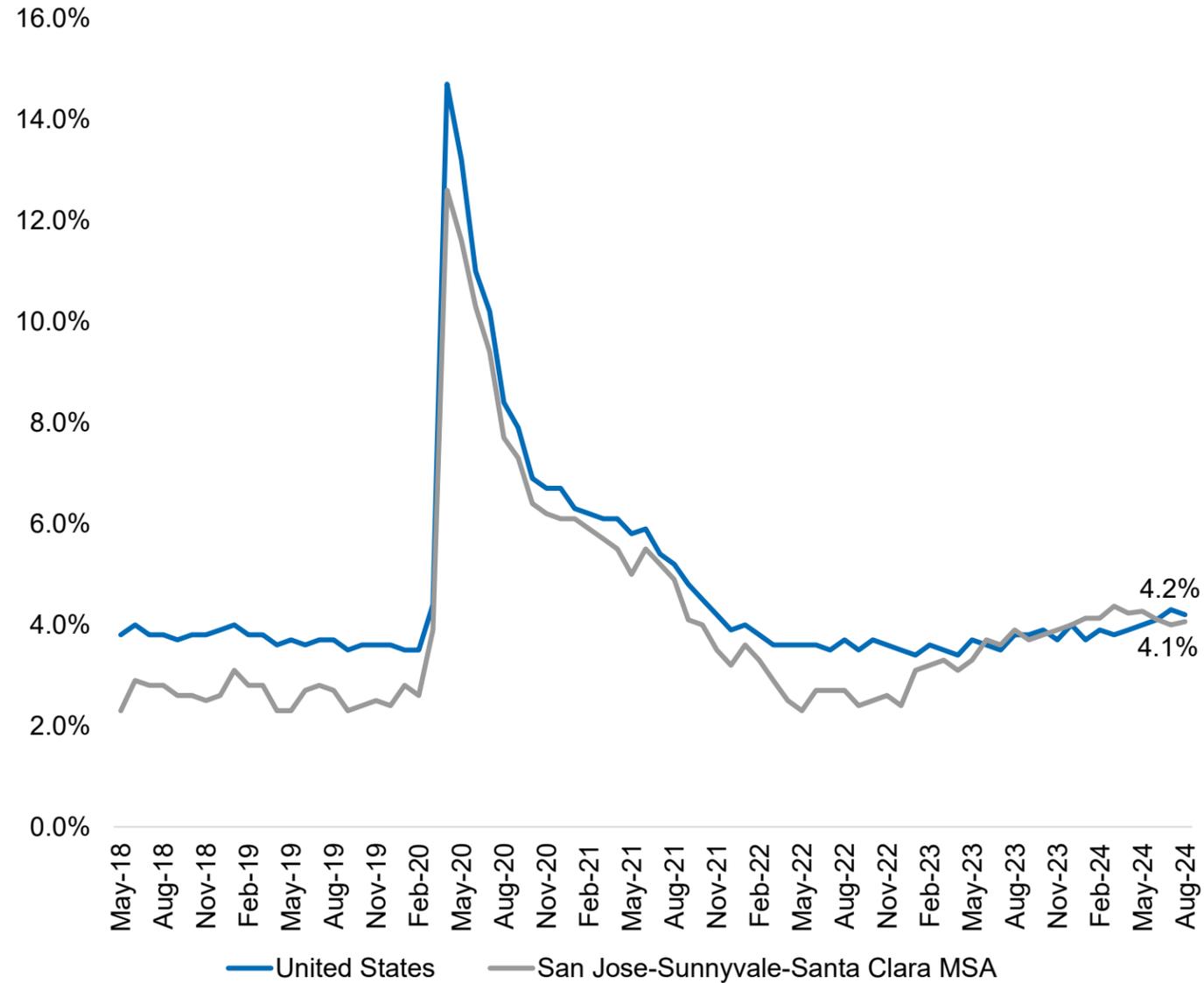
# Economy



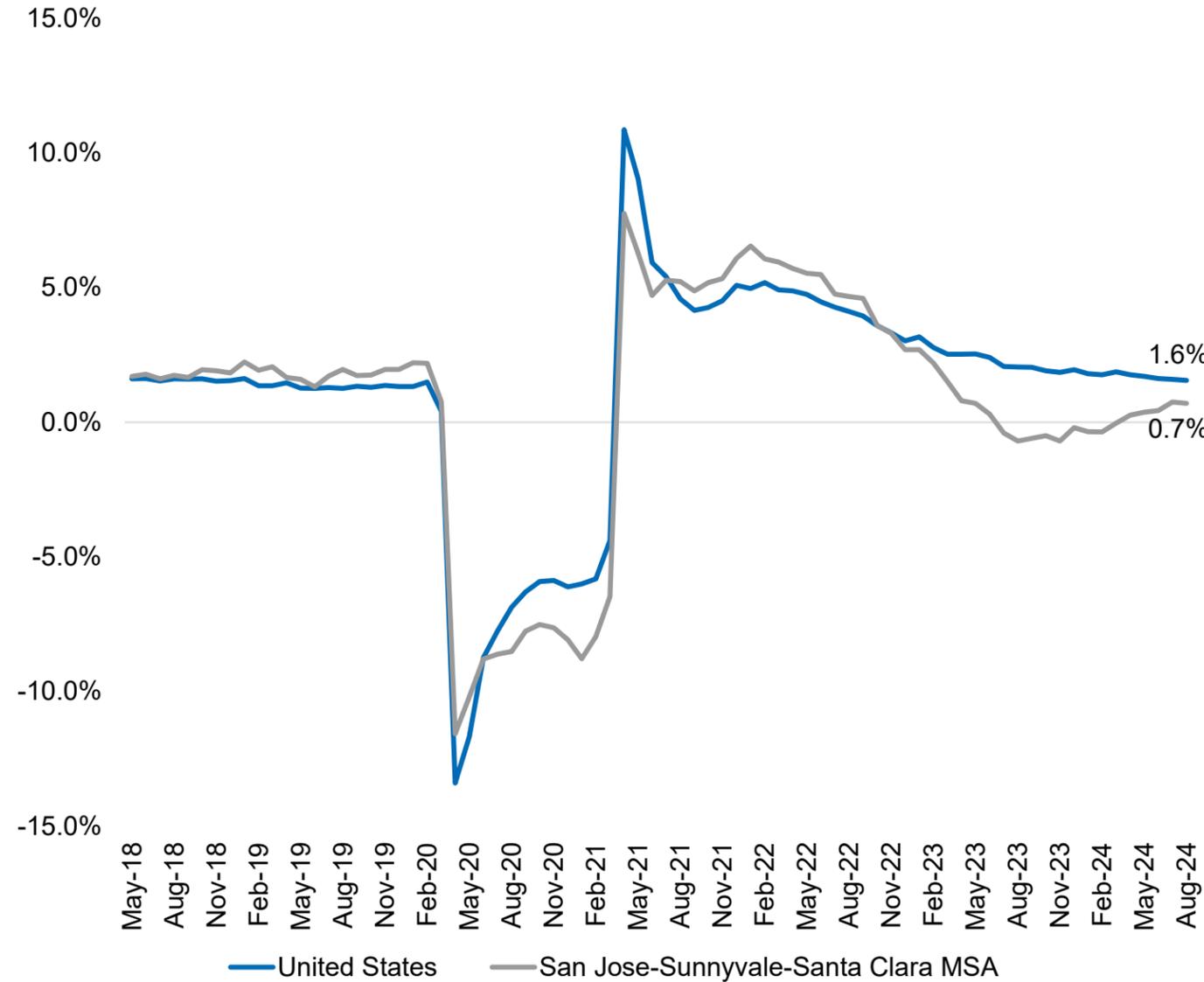
# Silicon Valley's Economy Shows Signs of Stabilizing After Job Losses

Modest job growth returned to the San Jose-Sunnyvale-Santa Clara's economy through August 2024 with employment inching up 0.7% year-over-year. This marks the fifth straight month in a row of employment gains after eight months of losses. The overall unemployment rate held relatively steady through August, dropping below the U.S. average within the past two months. Professional & Business and Educational services recorded the largest gains whereas Information Technology, Construction, and Manufacturing shed jobs.

**Unemployment Rate, Seasonally Adjusted**



**Nonfarm Payroll Employment, Non-Seasonally Adjusted, 12-Month % Change**

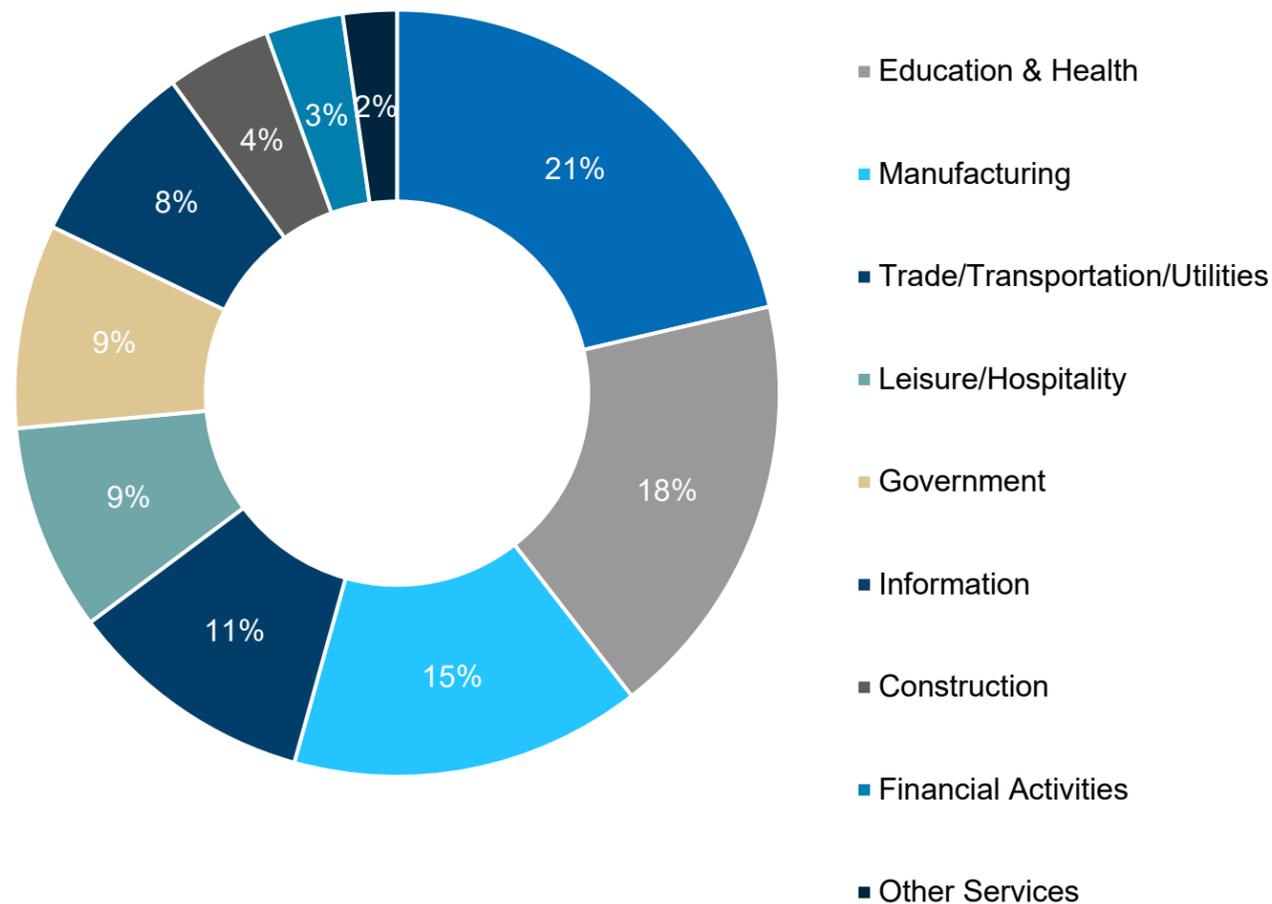


Source: U.S. Bureau of Labor Statistics, San Jose-Santa Clara-Sunnyvale

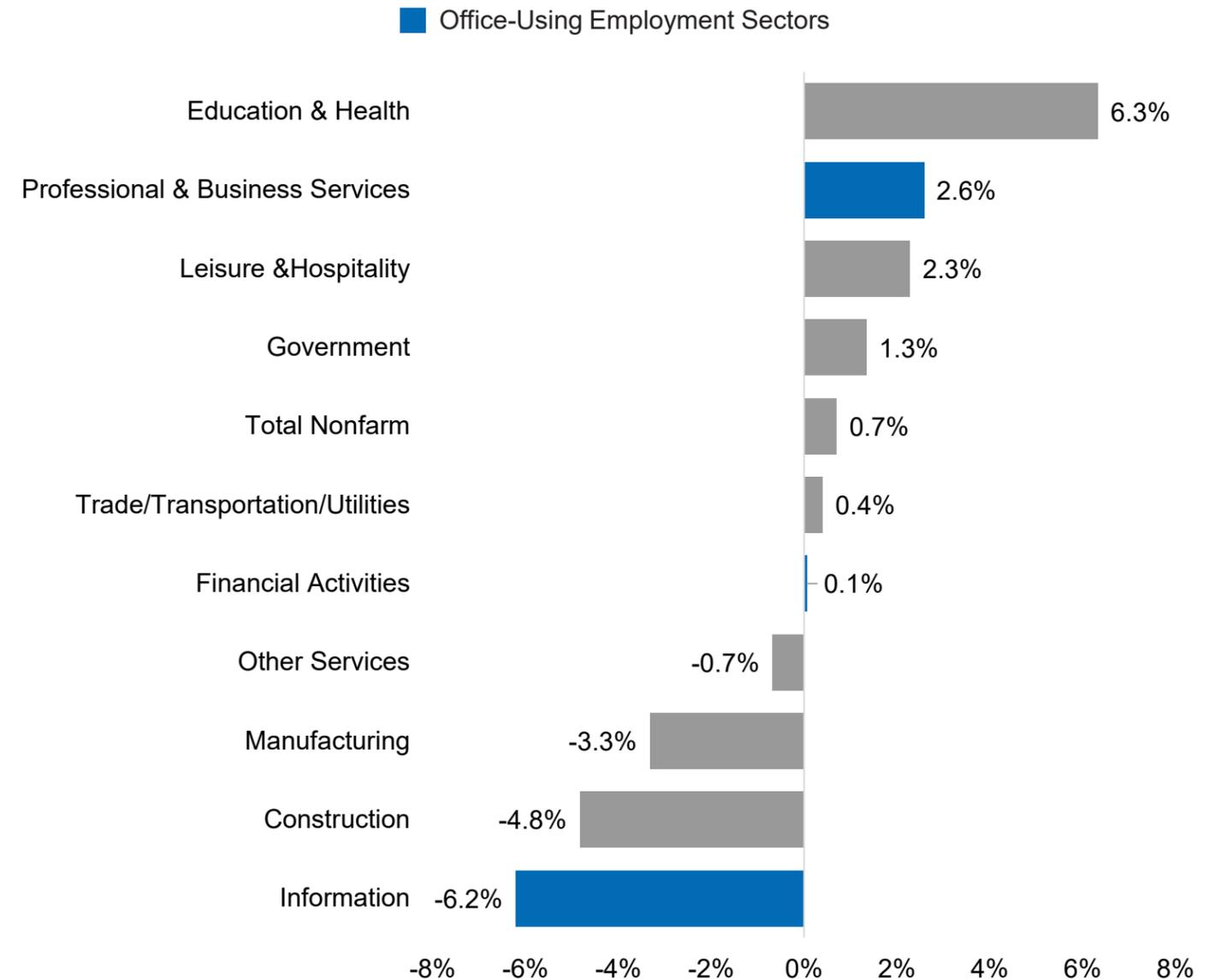
# Professional & Business Services Added Jobs While the Tech Sector Continued to Shed

Job gains in the Professional & Business Services, Education & Health, and Leisure & Hospitality and Government outpaced losses in the Tech (Information Technology), Construction, and Manufacturing sectors. Fortunately, Professional & Business Services – a key driver of the local office market - remains Silicon Valley's largest employment sector and is expanding once again, which bodes well for the office market, despite the Valley's reputation as a tech-only hub.

Employment by Industry, August 2024



Employment Growth by Industry, 12-Month % Change, August 2024

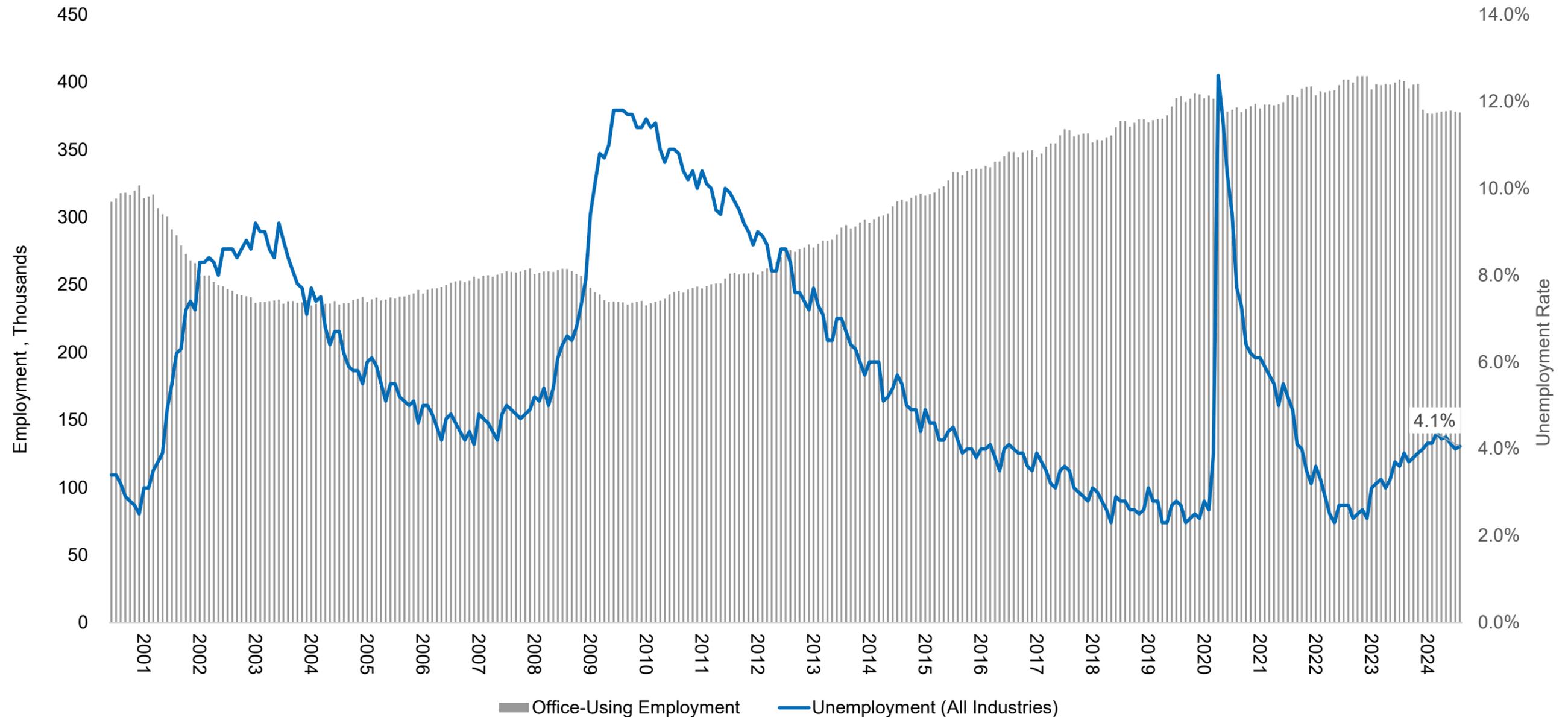


Source: U.S. Bureau of Labor Statistics, San Jose-Santa Clara-Sunnyvale, layoffs.fyi

# Office-Using Employment Expected to Trend Upward

Office-using employment has recently declined from its peak as the tech sector undergoes readjustment. Between 2020 and 2022, tech companies rapidly expanded their workforces in response to the shift to remote work. By early 2023, many began layoffs as the world returned to 'normal.' We believe the market has bottomed out and is now trending upward, driven by growing economic confidence and strong local demand from the rapid growth of AI companies

Office-Using Employment\* and Unemployment Across All Industries



Source: U.S. Bureau of Labor Statistics, San Jose-Santa Clara-Sunnyvale

\*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.

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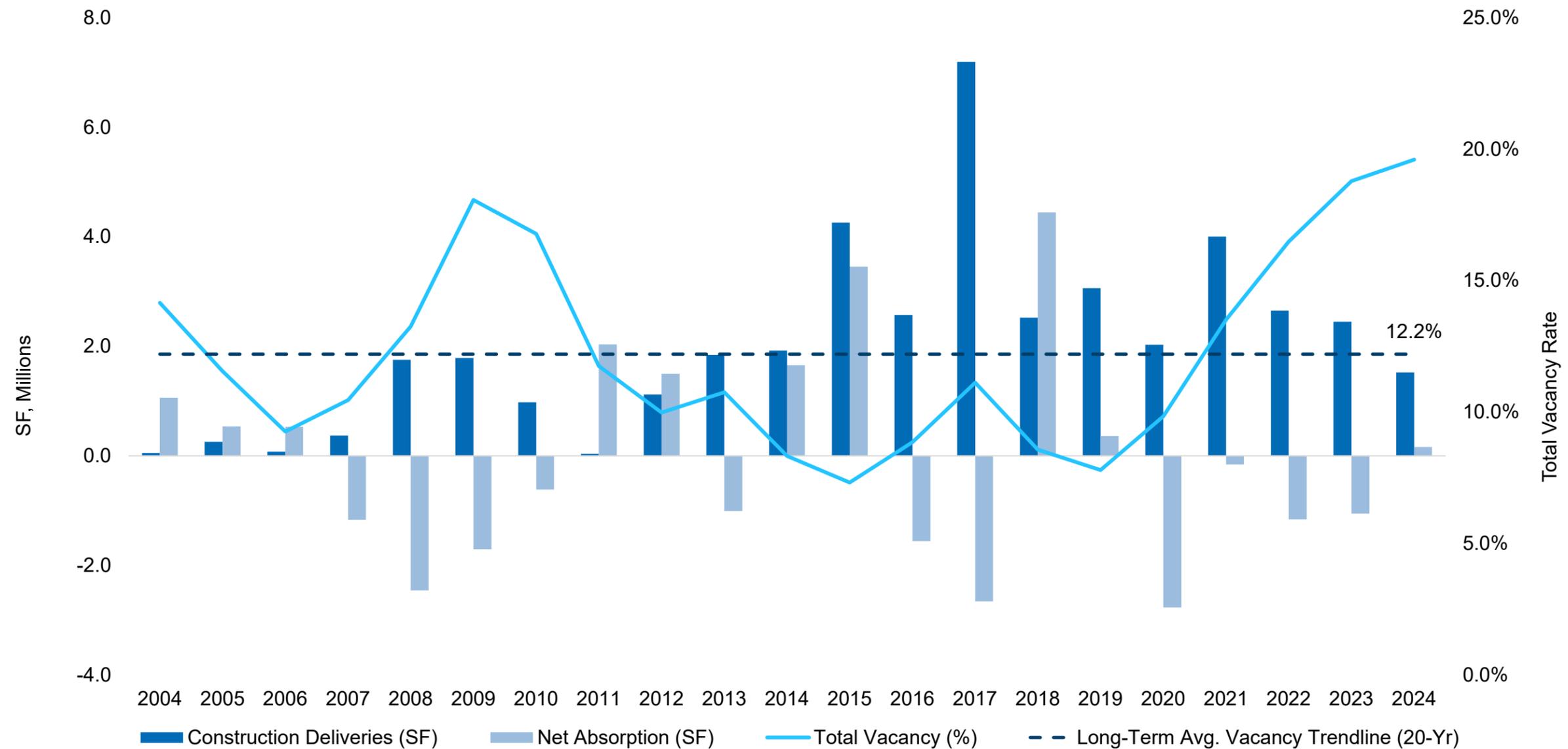
# Leasing Market Fundamentals



# The Office Market Is Stabilizing as Fundamentals Remain Consistent from Last Quarter

The return to positive net absorption this year strongly suggests that the market is stabilizing or nearing the bottom, despite a slight uptick in the vacancy rate. While Mountain View, Saratoga, and Milpitas showed positive net absorption, it was not enough to counterbalance negative absorption in other submarkets this quarter, leading to an overall decline in net absorption. However, the total vacancy rate only inched up by 25 basis points to 19.6% as the market continues to stabilize. A declining construction pipeline is positive for the market.

## Historical Construction Deliveries, Net Absorption, and Vacancy

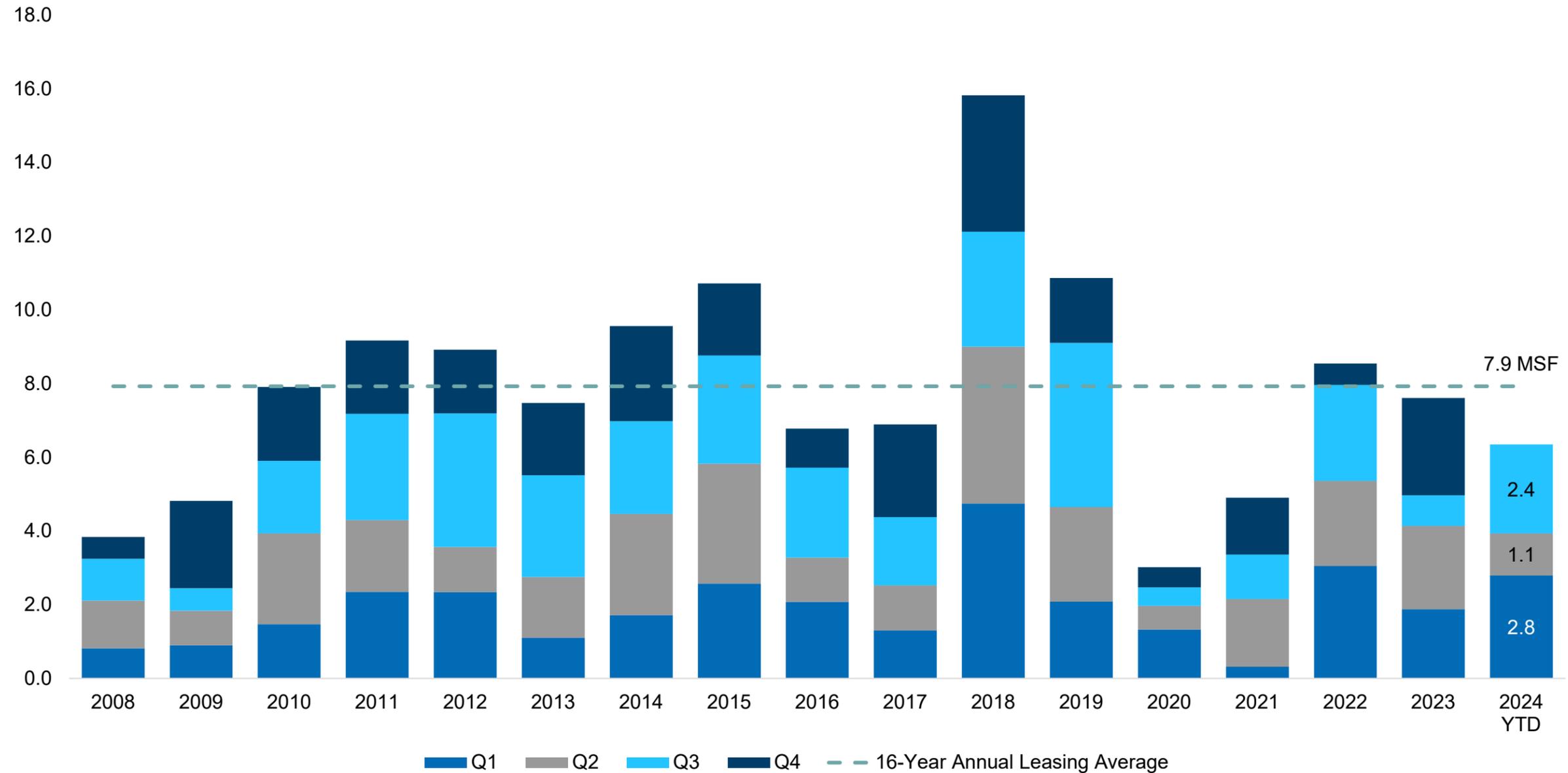


Source: Newmark Research

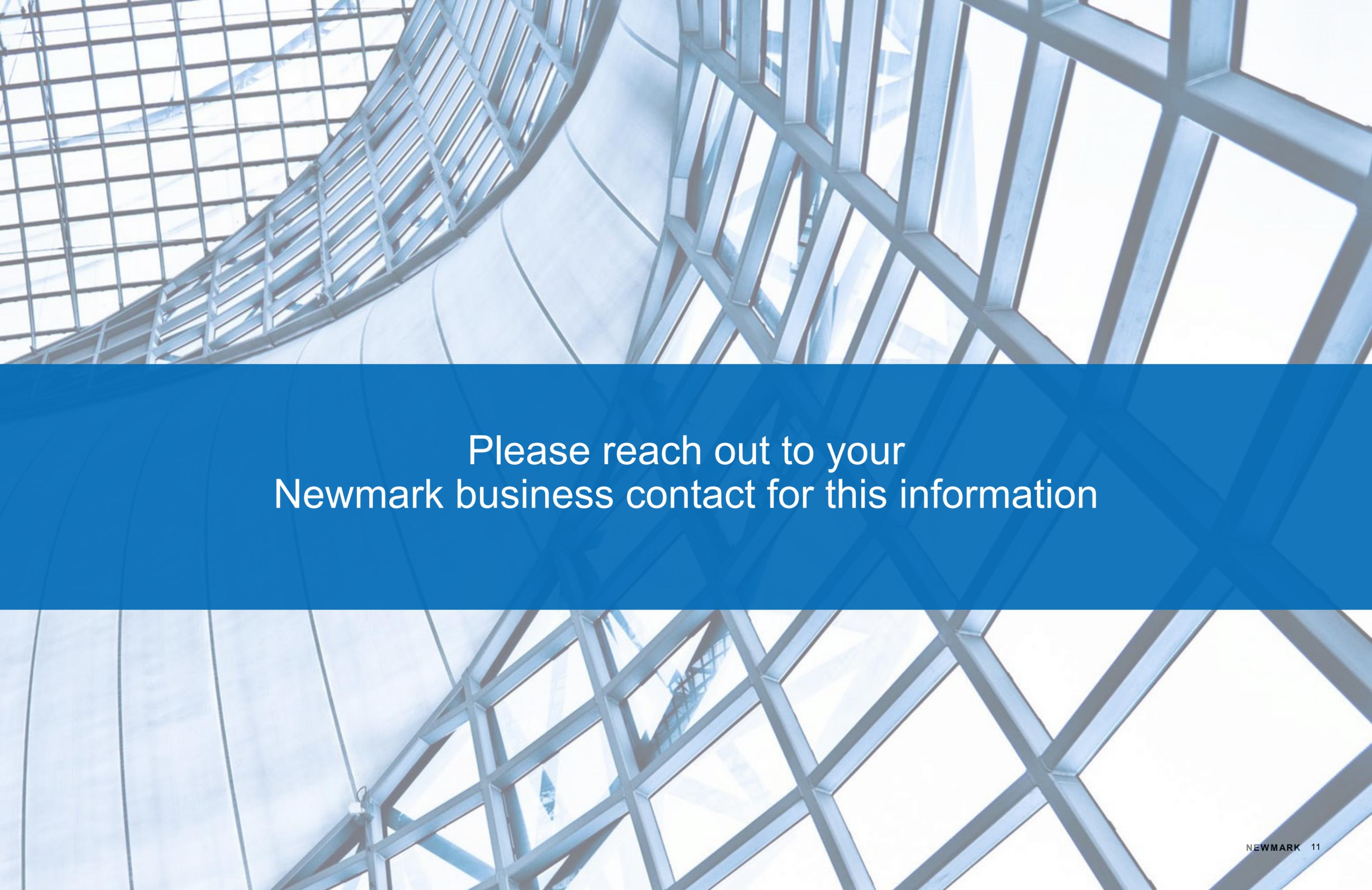
# Leasing Activity Is on Track to Surpass 16-Year Average by Year-End

Strong leasing activity in the first and third quarters of this year, coupled with modest activity in the second quarter, signals that the market is recovering from previous lows. In an effort to attract businesses back to Downtown San Jose, the City Council recently approved business tax breaks and free parking incentives as part of a broader 'Return-to-Downtown Office' program. This initiative aligns with companies implementing stricter return-to-work policies.

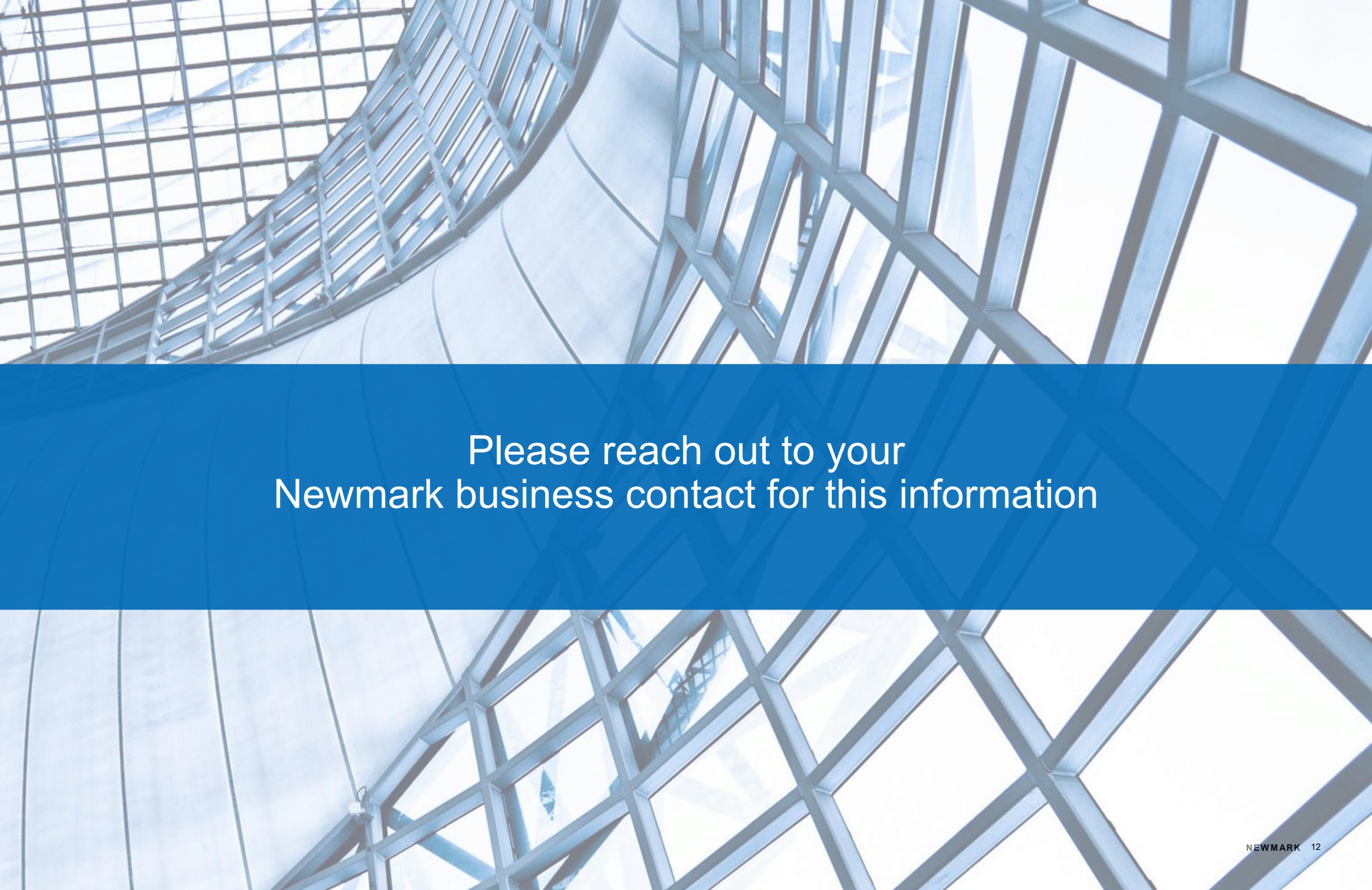
Total Leasing Activity (msf)



Source: Newmark Research, CoStar



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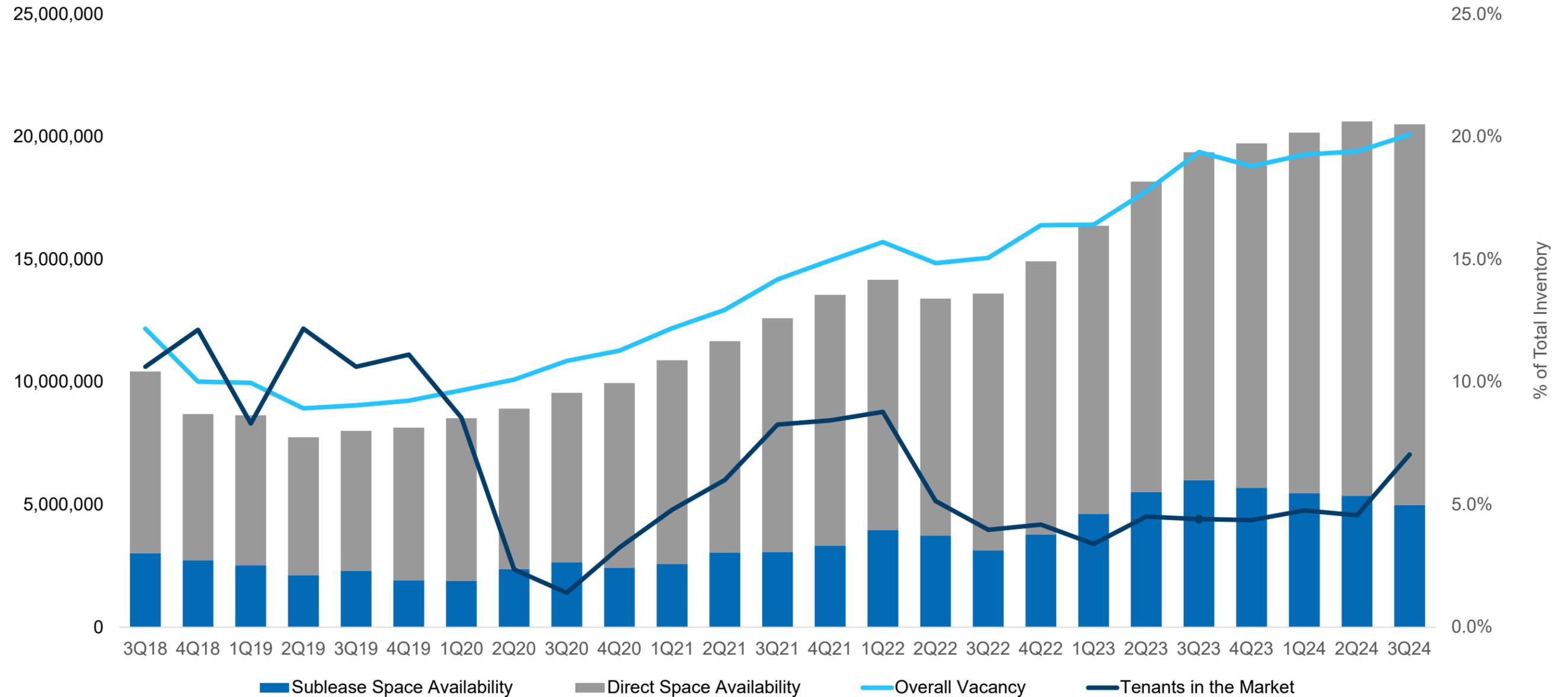


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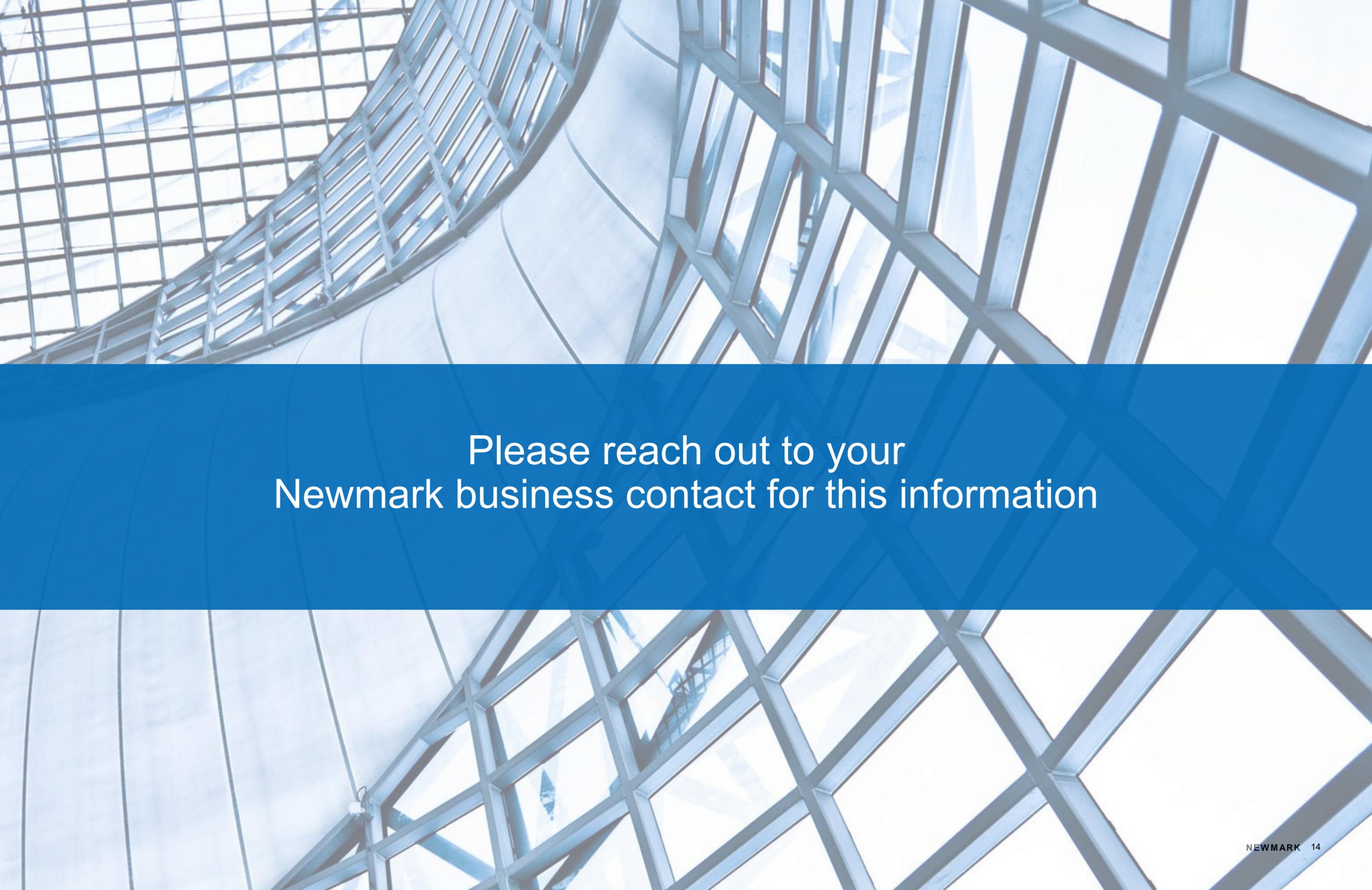
# A Jump in Tenant Demand Signals Positive Trends for the Market Is Nearing

While the amount of sublease space dwindled during the third quarter, direct space availability increased. This pushed the overall vacancy rate up to 20.1% in the third quarter from 19.4% in second quarter of 2024 and 18.8% at year-end 2023. One positive shift that we are closely watching, however, came from tenant demand (as measured by tenants out in the market), which grew to 6.7 MSF, or 7.0% of inventory, up from 4.6% of inventory in the second quarter.

Available Space and Tenant Demand as Percent of Overall Market



Source: Newmark Research

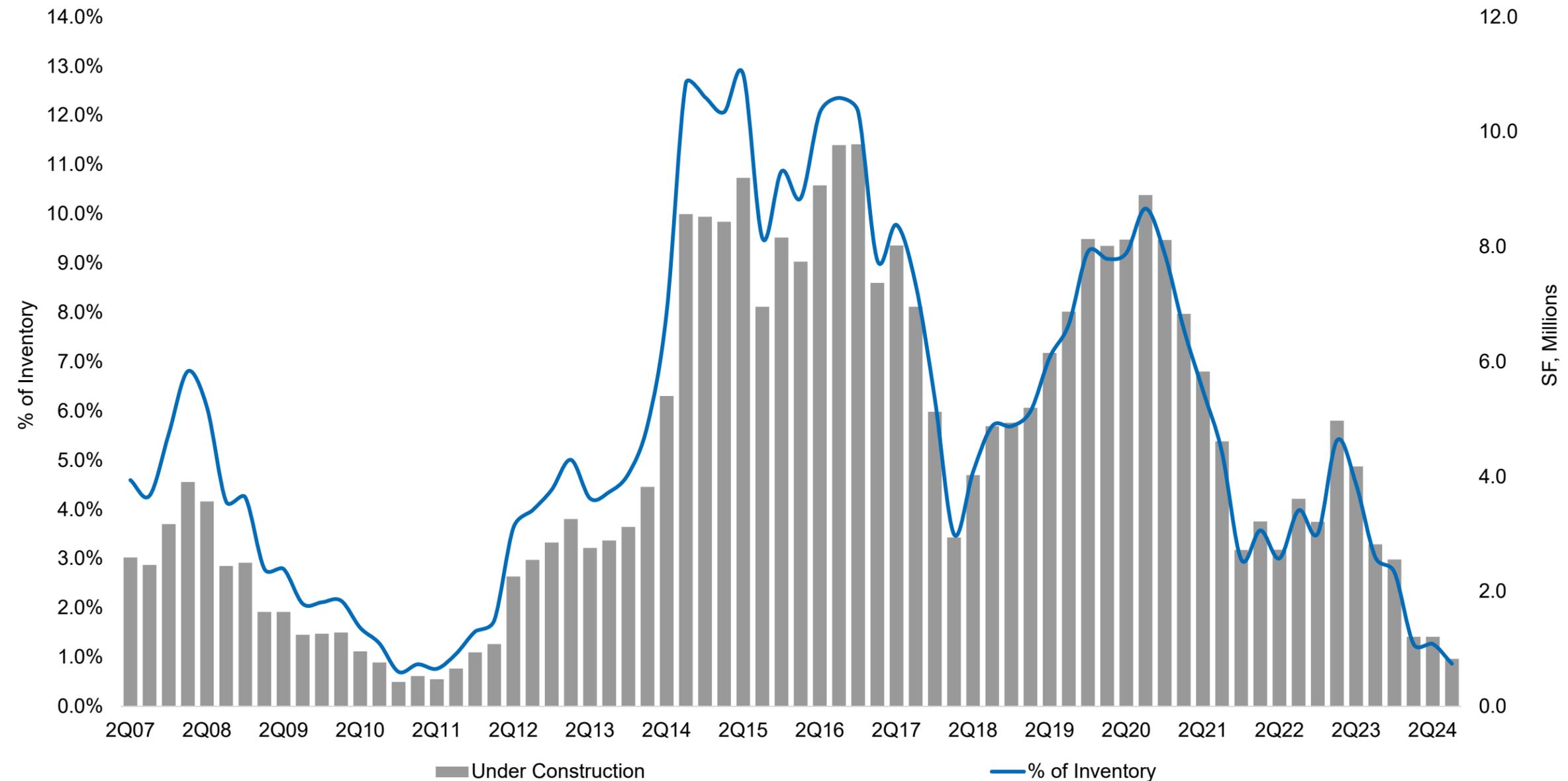


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# Construction Pipeline Tempered Down, a Positive Sign for the Market

In addition to rising demand, another positive indicator for the markets improved demand and supply balance is that the construction pipeline has dramatically dropped. In addition to developers holding off on starting new projects until stronger market conditions return, the tight capital markets has kept construction lending at bay. With the Fed's recent interest rate cut of 50 bps, many believe the economy will start firing on more cylinders, which will hopefully lead to more positive momentum for the market in the near term.

## Office Under Construction and % of Inventory

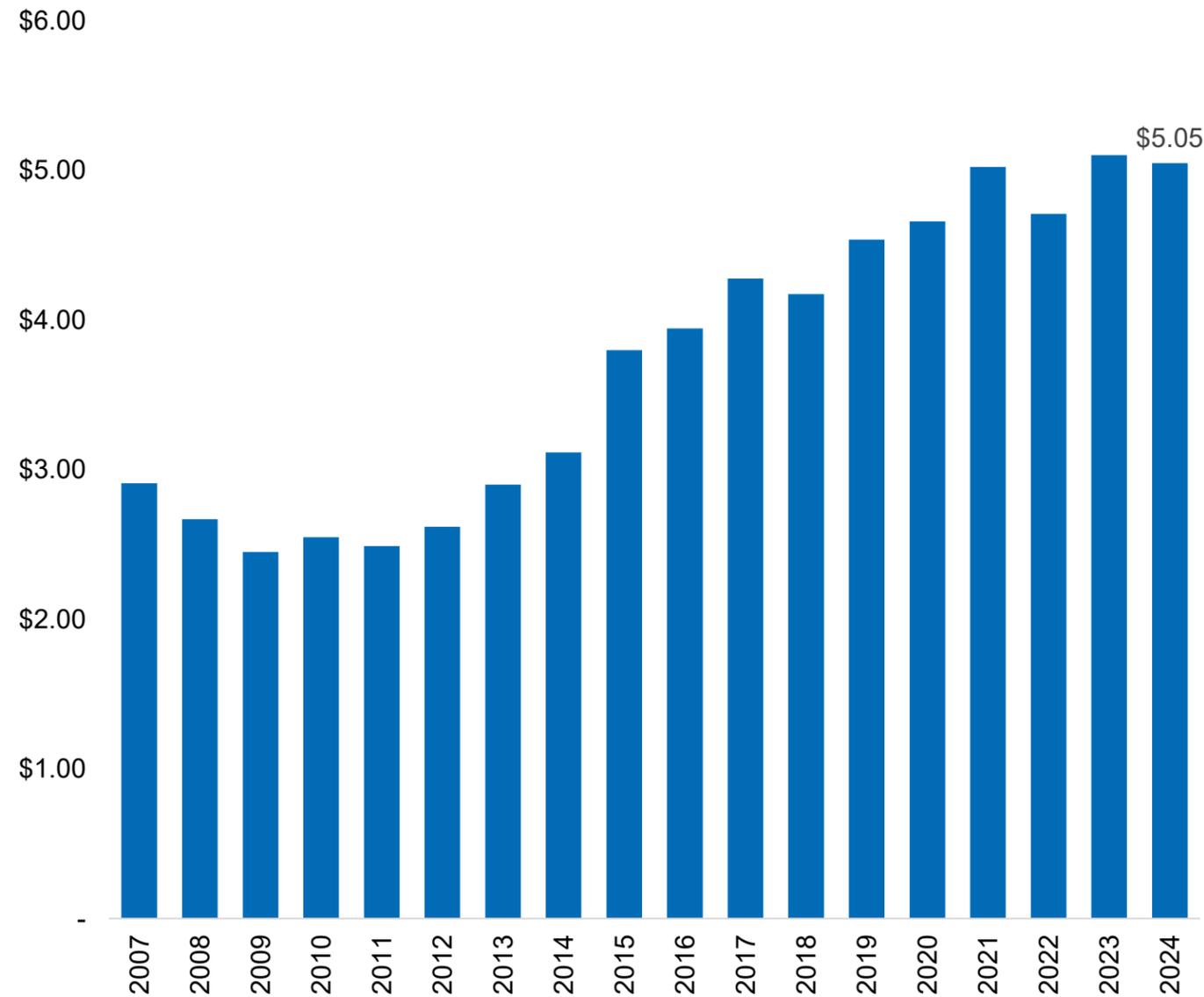


Source: Newmark Research, CoStar, San Jose-Santa Clara-Sunnyvale MSA

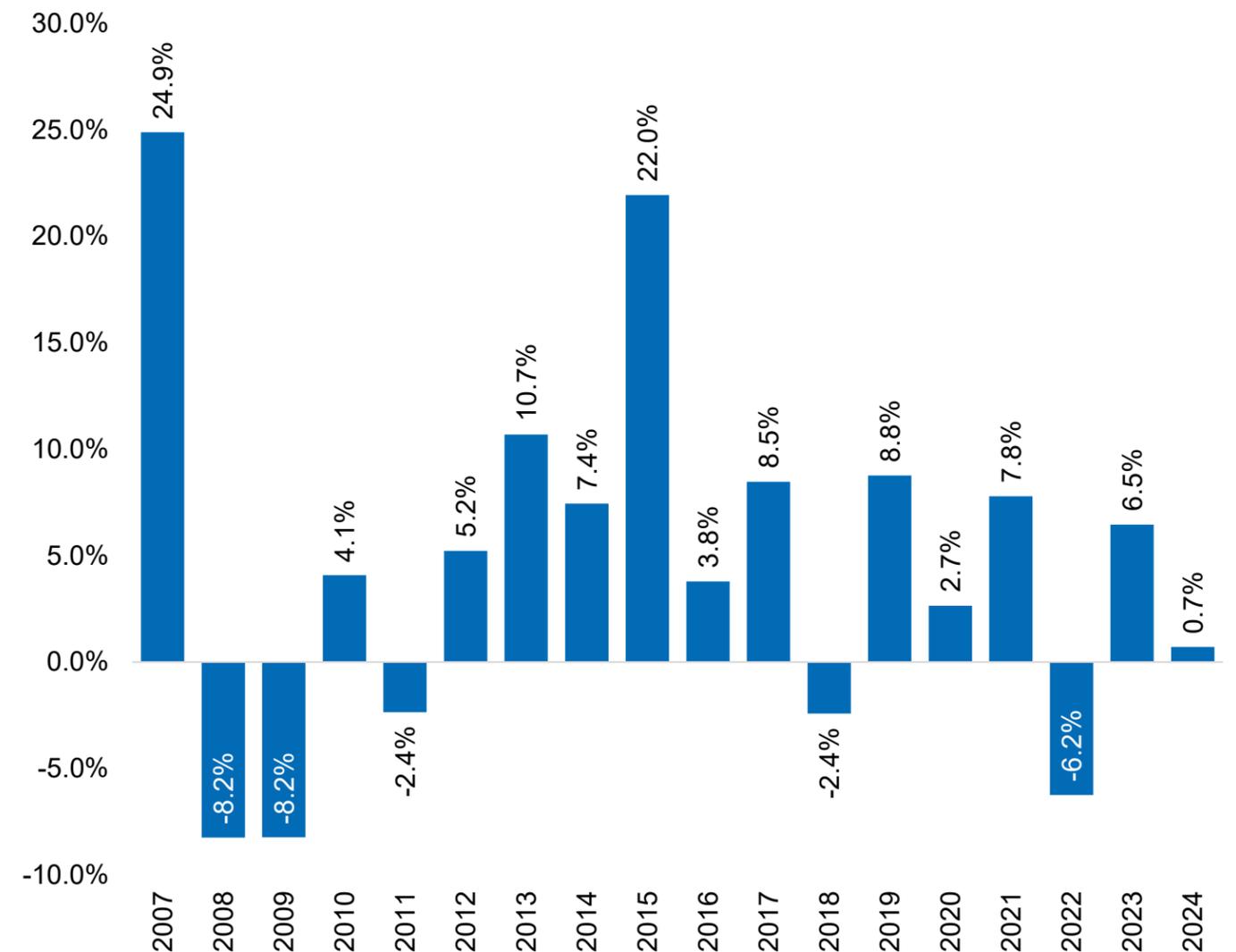
# Asking Rents Are Holding Relatively Steady in 2024

The average asking rent has been bumping along the \$5.00/SF full service range since the end of 2023 as confidence in the market is improving. Effective rents, however, are still hampered by higher-than-average Tis and free rent. Moreover, as organizations seek strategies to bring employees to return to the office, amenities are paramount in enhancing the workplace's appeal. Features such as flexible workspaces, additional conference rooms, abundant natural light, open spaces, and cutting-edge infrastructure all support this.

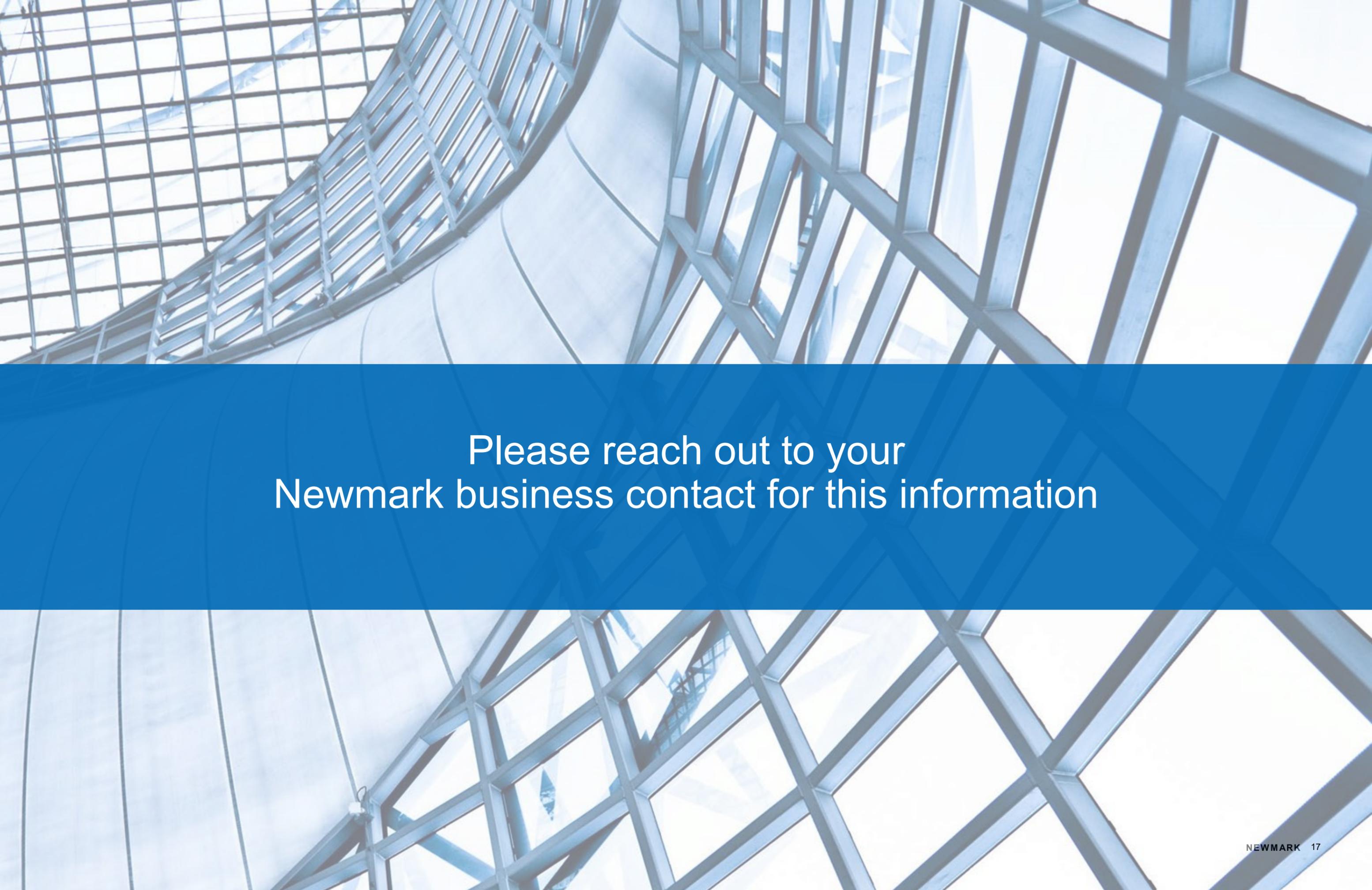
Office Average Asking Rent, \$/SF, FS



Year-over-Year Asking Rent Growth Rate



Source: Newmark Research, CoStar

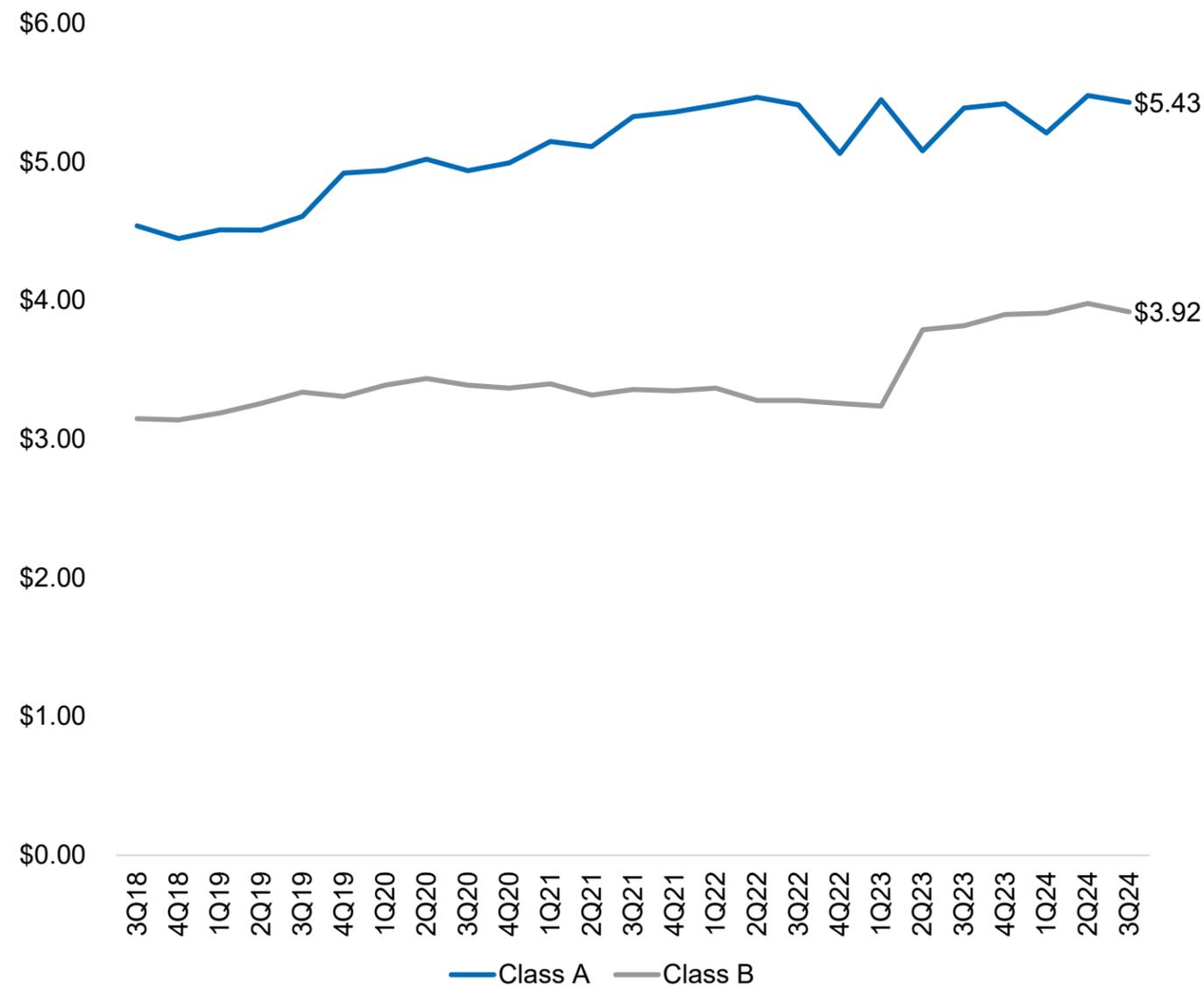


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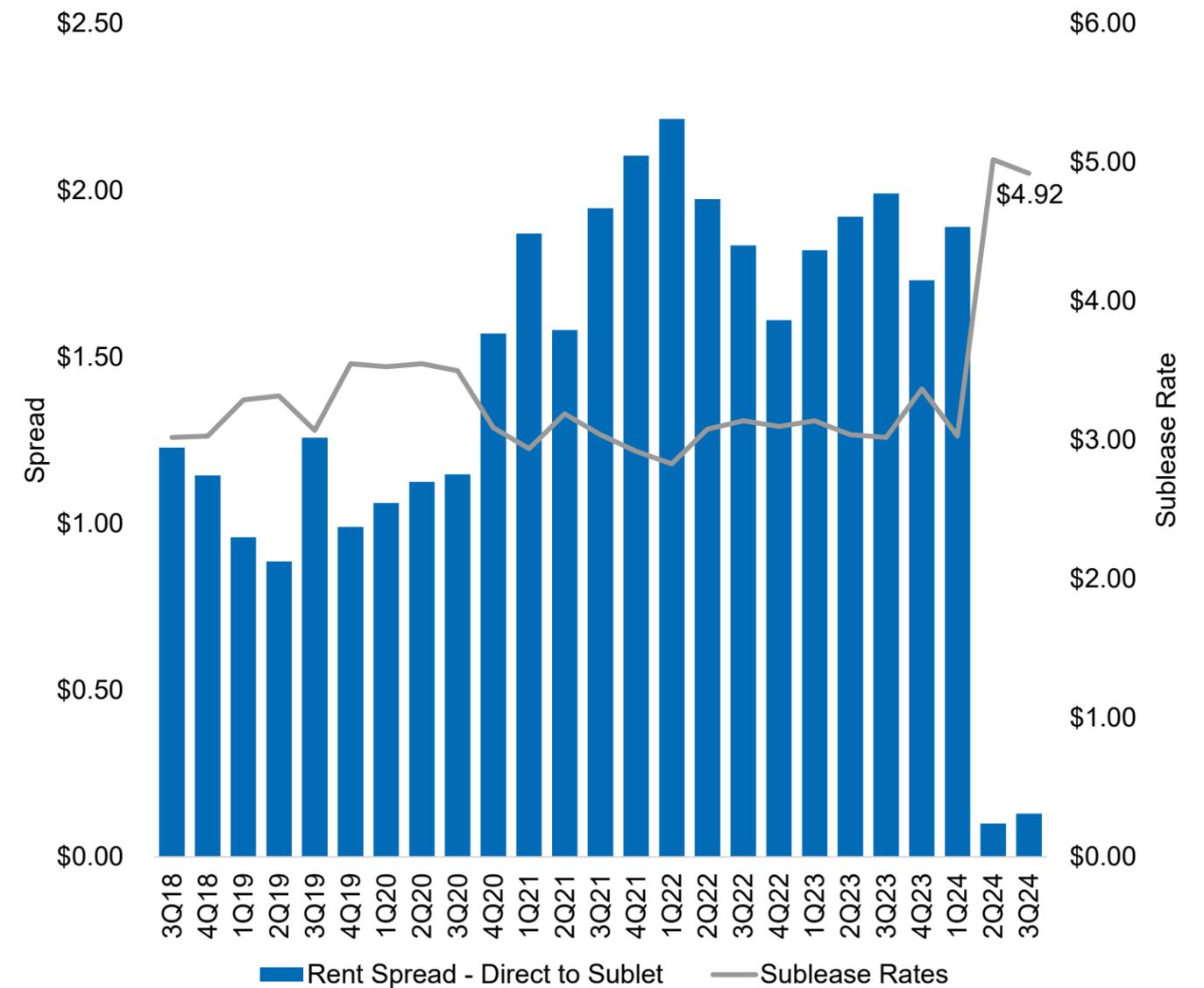
# Asking Rents Holding Relatively Steady

Class A and Class B asking rents have been modestly fluctuating up and down in recent quarters as the market is trying to find its footing while supply and demand stabilize. The spread between A and B is slightly tighter now than it has been in recent quarters, given the jump in Class B rents mid-2023. In addition, the spread between direct and sublease space asking rents notably compressed in the second and third quarters of 2024 as sublease space is garnering more attention with rents ticking up while direct rents hold steady.

Class A and Class B Asking Rents



Sublease Rates



Source: Newmark Research, CoStar

# Despite Negative Headlines, Tech Companies are Maintaining Sizeable Footprints

Despite a slowdown in hiring, technology companies continued to lead leasing activity, which included significant renewals, subleases, expansions, and even a major direct lease by Nvidia. As one of the region's standout performers, Nvidia has made headlines with its substantial growth and expansion, further solidifying its dominant position. We are currently tracking 6.7 MSF of active tenants in the market, and at least a dozen requirements are greater than 100,000 SF and about a half are looking for 50,000+ SF.

## Notable 2Q24 Lease Transactions

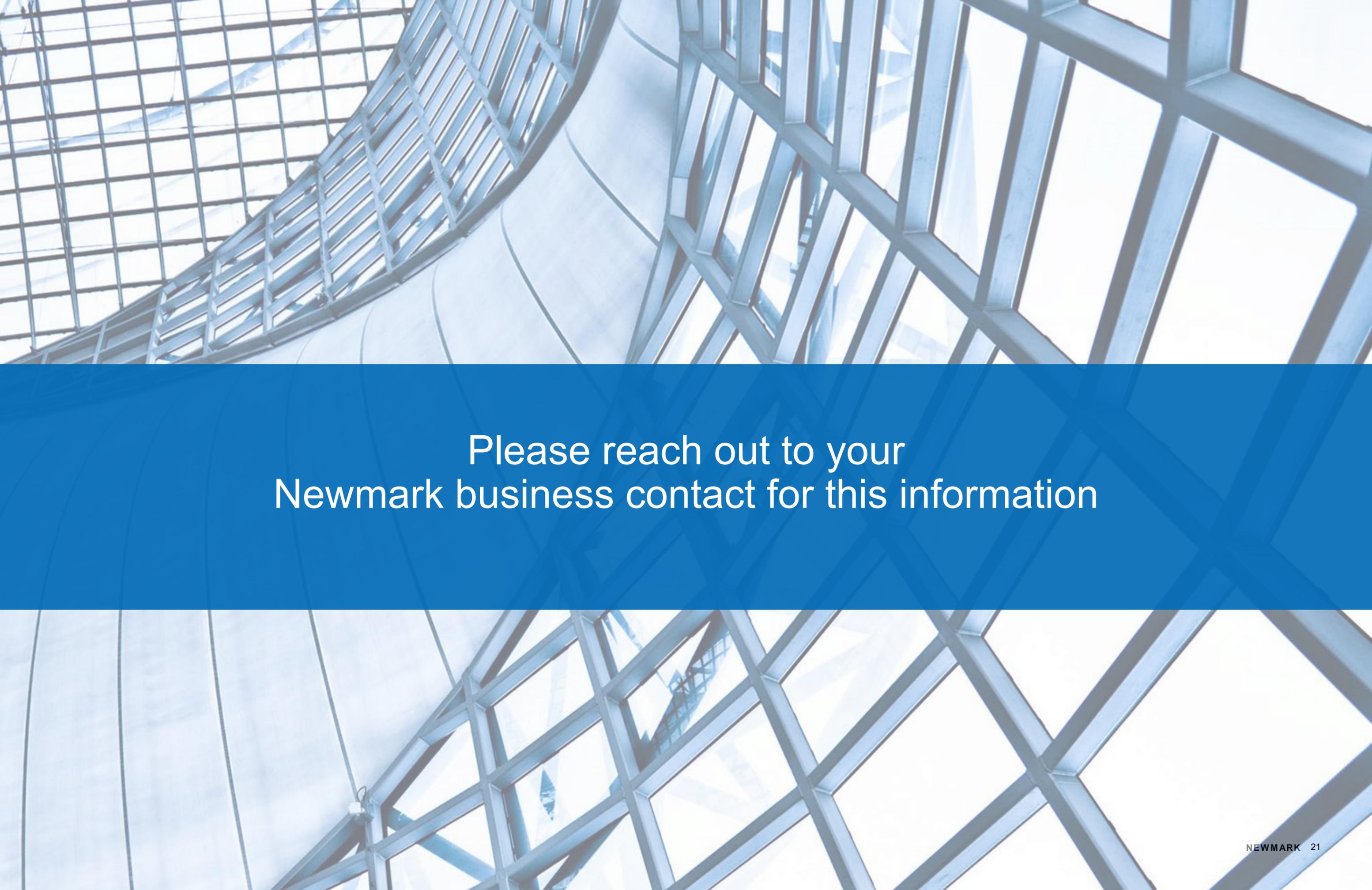
Tenant	Building(s)	Submarket	Type	Square Feet
Confidential	420 N Mary Avenue	Sunnyvale - Peery Park	Lease Renewal	230,000
<i>Lease Renewal. Occupied by confidential tenant.</i>				
Johnson & Johnson	5490 Great America Parkway	Santa Clara - Marriott Park	Lease Renewal	229,626
<i>Lease Renewal. Johnson &amp; Johnson, one of the nation's leading medical technologies corporations with a presence in the Valley, renewed in their facility in Santa Clara.</i>				
TikTok	1155 Coleman Avenue	San Jose - Airport	Sublease	194,549
<i>Sublease. Tiktok subleased the building from Roku and is set to expire in September 2030.</i>				
Yahoo	391 San Antonio Road	Mountain View - El Camino Corridor	Sublease Expansion	119,884
<i>Sublease Expansion. Yahoo has extended their current sublease of the fifth and sixth floor, while expanding their sublease to also include the entirety of the second floor.</i>				
NVIDIA	300 Holger Way	San Jose - North	Direct Lease	101,626
<i>New Lease. NVIDIA continues to expand their presence in the Bay Area with their HQ at 2788 San Tomas Expy, Santa Clara.</i>				

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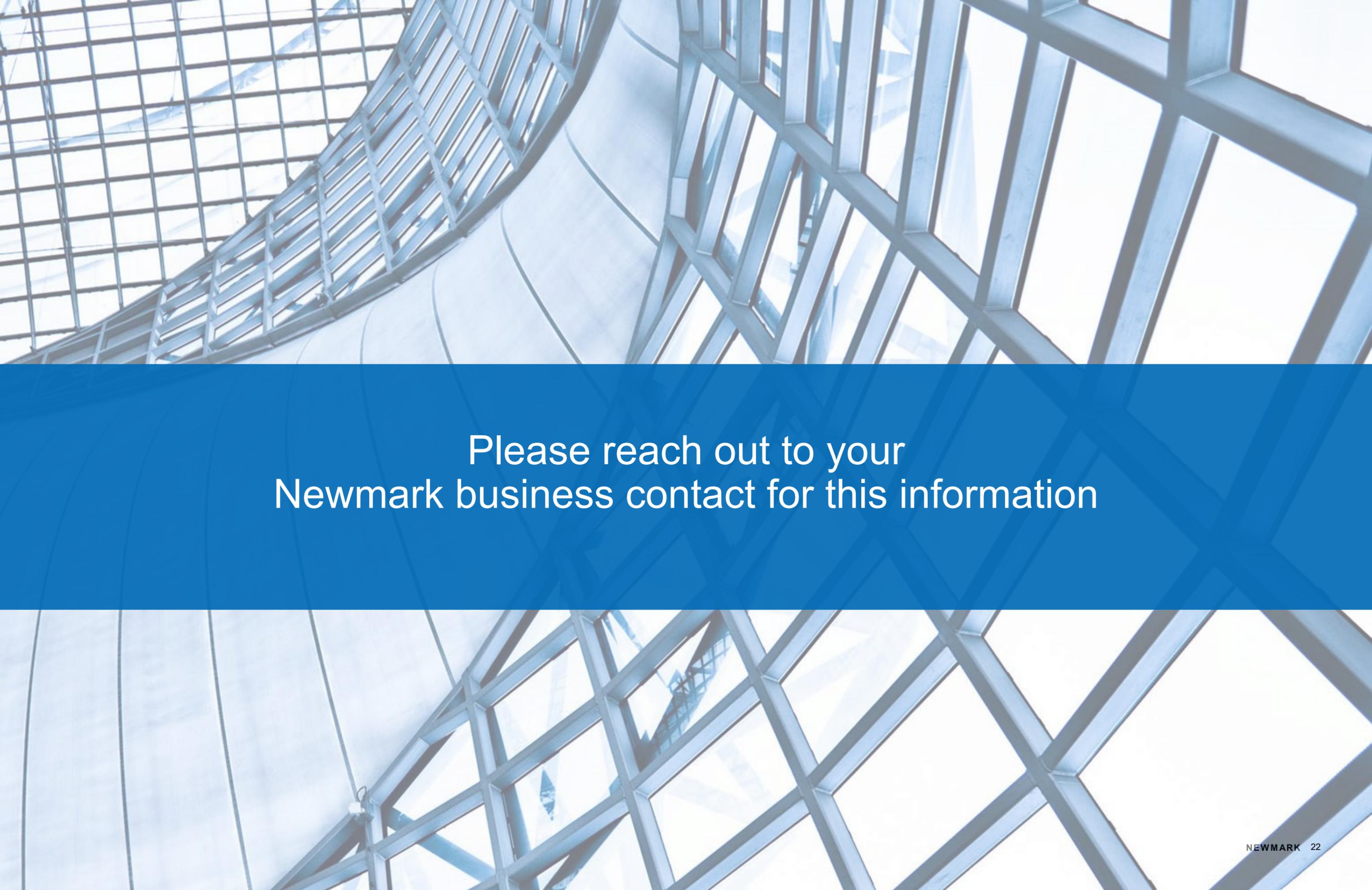
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# Appendix



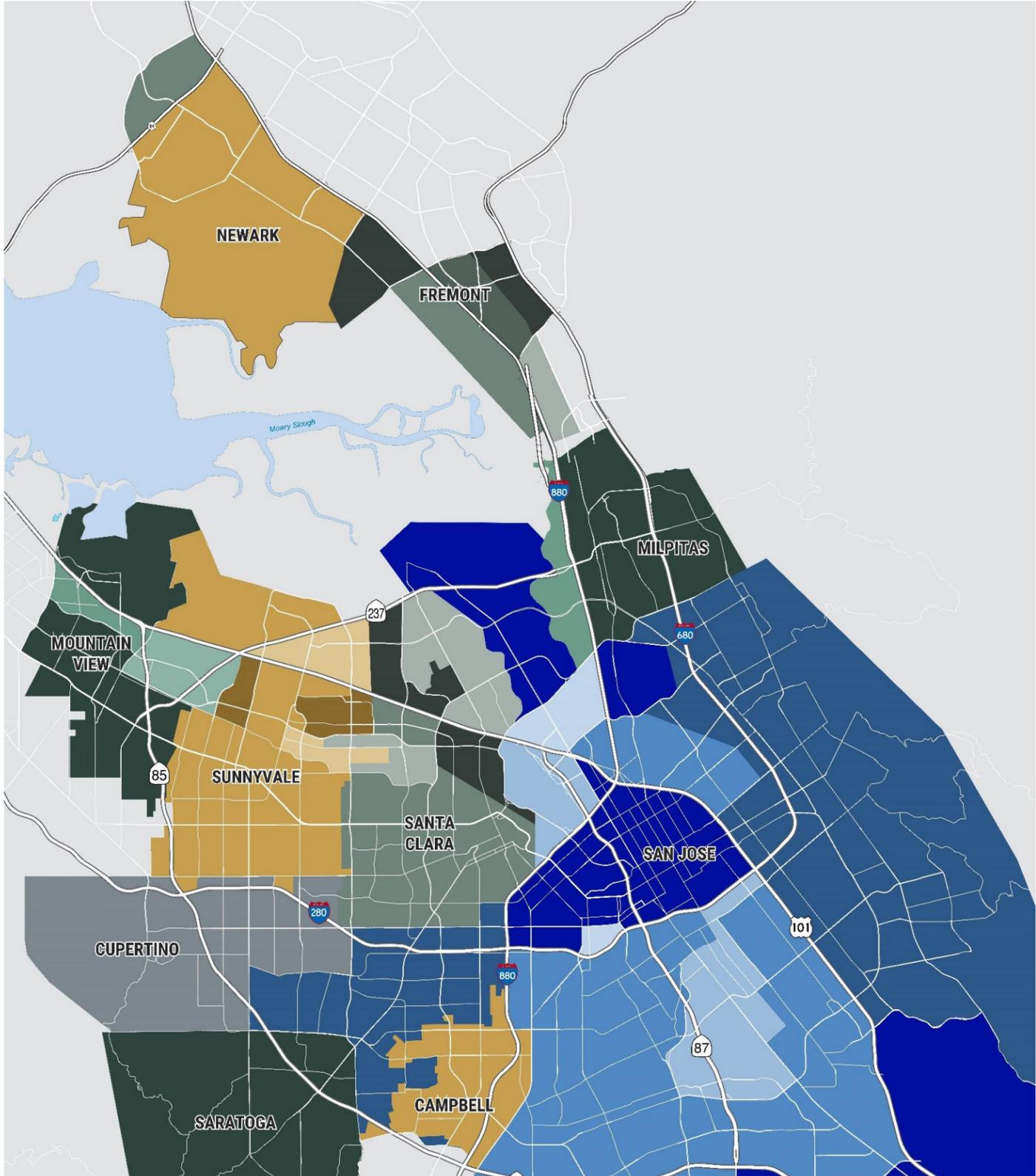


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# Silicon Valley - Submarket Map



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