
3Q24

South Peninsula R&D Market Overview

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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.
- Following the Federal Reserve's 0.50 percentage point reduction in September, lenders are optimistic about additional rate decreases anticipated in Q4 2024 and throughout 2025. This adjustment signifies the commencement of a strategic shift by the central bank from a restrictive to an accommodative monetary policy, marking its first rate cut since July 2023. Analysts forecast the possibility of one additional rate reduction in 2024 and additional cuts in 2025.

Major Transactions

- Life science dominated the largest transactions of Q3 2024, with 4 out of the 5 largest deals in South Peninsula being life science deals. Many of these deals also included lab space.
- The largest deal of the quarter for South Peninsula R&D was xAI’s deal for 77,269 SF at 1450 Page Mill Road. This direct deal marked another company moving out of the SF market, although xAI maintains some space in the historic Pioneer Building at 3180 18th Street in San Francisco’s Mission District (owned by X). This space had previously been occupied by OpenAI who also had a historic lease deal in San Francisco this quarter.

Leasing Market Fundamentals

The South Peninsula market recorded 493,358 square feet of gross absorption in the third quarter of 2024, marking the second consecutive quarter to exceed the five-year leasing average.

- All transactions in the quarter were direct leases, indicating a shift away from sublease opportunities despite their typical rental rate advantages.
- Despite the South Peninsula's historically strong rental rates—driven by premium R&D space and life science users—market softening has impacted pricing. Average asking rates decreased from \$5.59 to \$5.44 per square foot, consistent with broader commercial real estate market trends.

Outlook

- Following 2023's negative net absorption of 1.4 million square feet, the market's stabilization throughout 2024 suggests the downturn may have reached its floor. The combination of steady vacancy rates and anticipated lower federal interest rates indicates potential market improvement ahead.
- Life science leasing activity continues to be a crucial driver of R&D market performance, with this sector's influence expected to strengthen further in upcoming quarters. This trend is particularly evident, as four of our top five largest deals are in the life science sector.
- Improving economic conditions may catalyze both expansion opportunities for existing tenants and market entry for new occupiers in the competitive South Peninsula R&D submarket.

1. Economy
2. Leasing Market Fundamentals
3. Appendix

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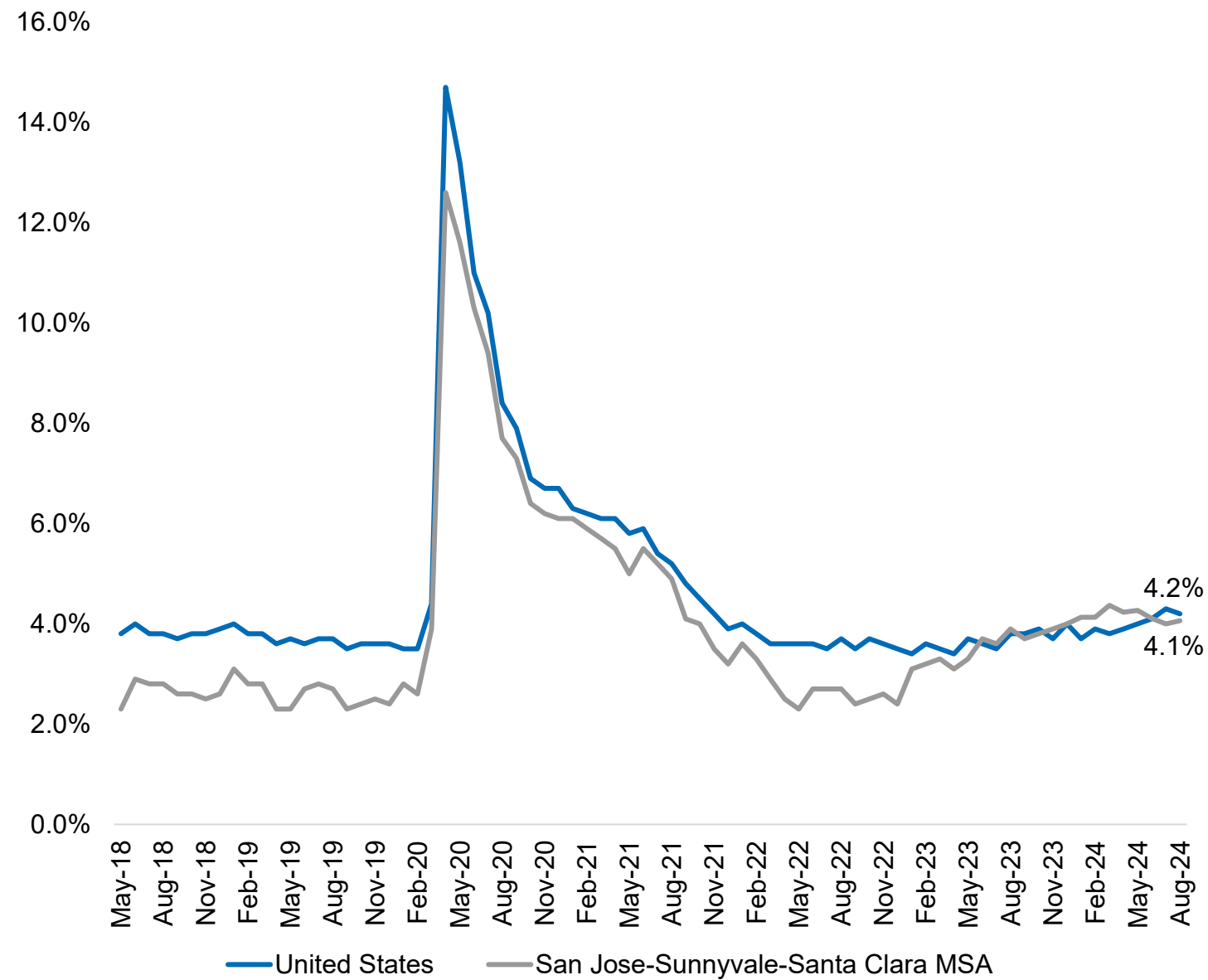
Economy



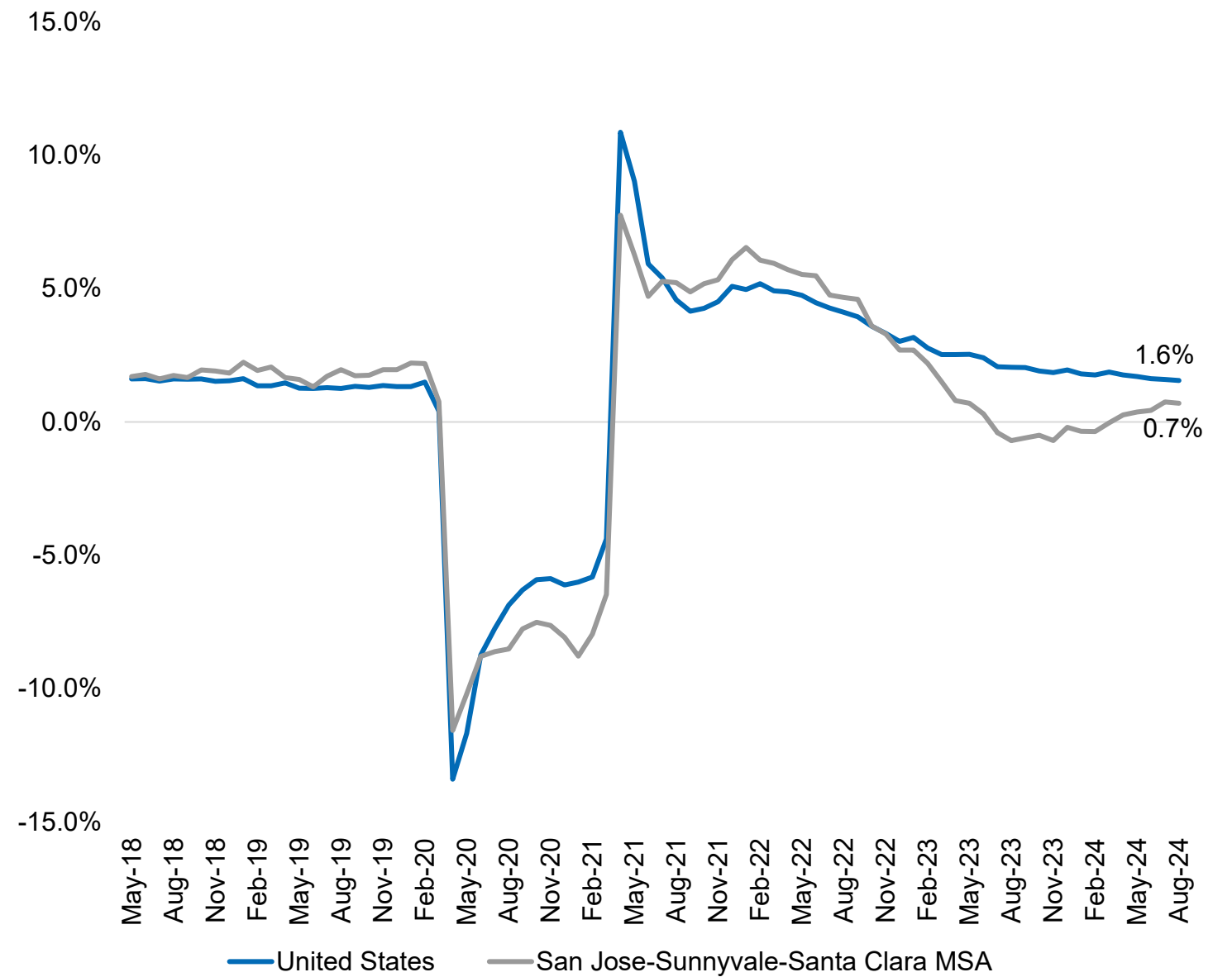
Job Growth Turned Positive, Indicating a Possible Turning Point in the Economy

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

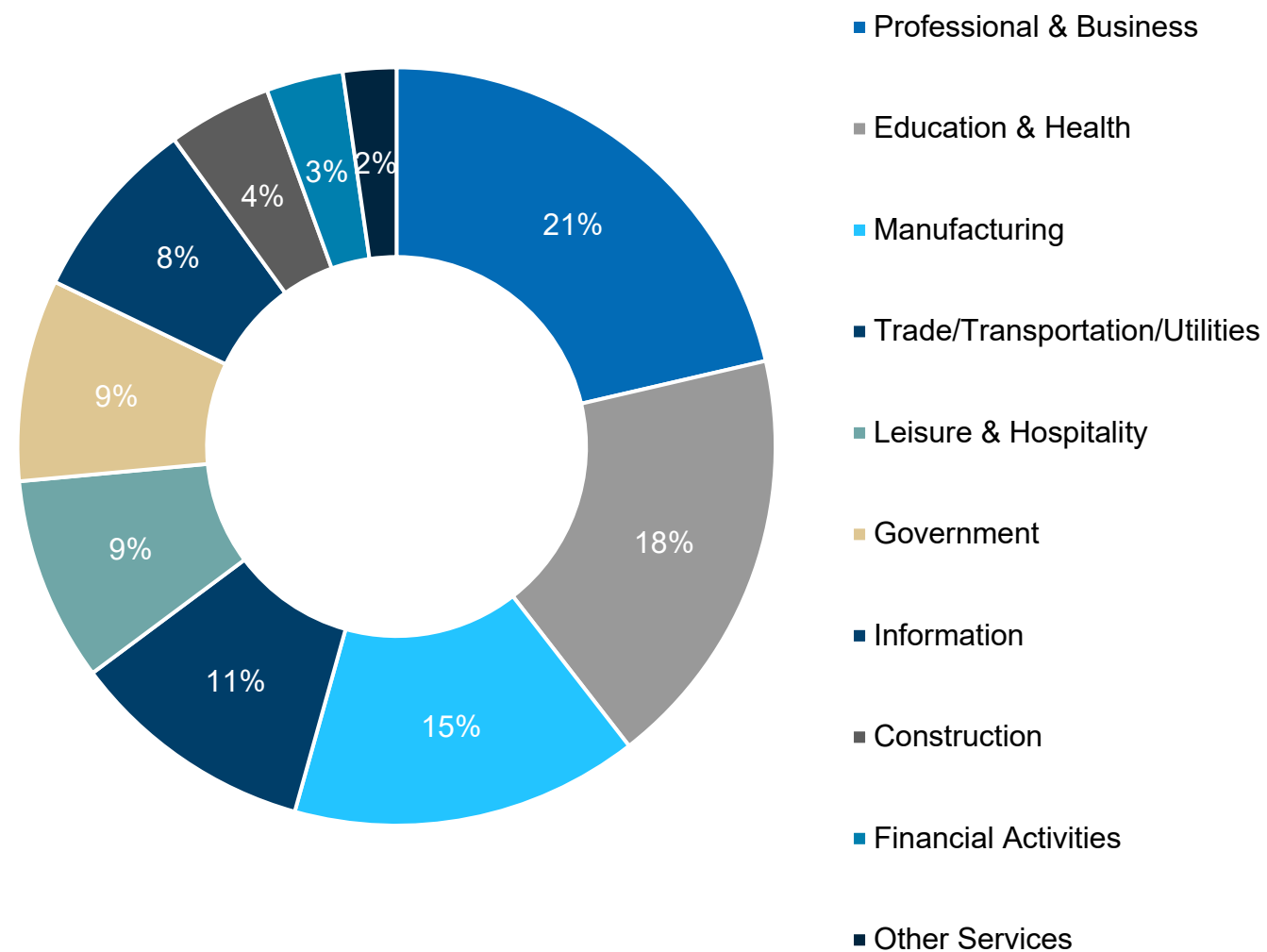


Source: U.S. Bureau of Labor Statistics, San Jose-Sunnyvale-Santa Clara MSA

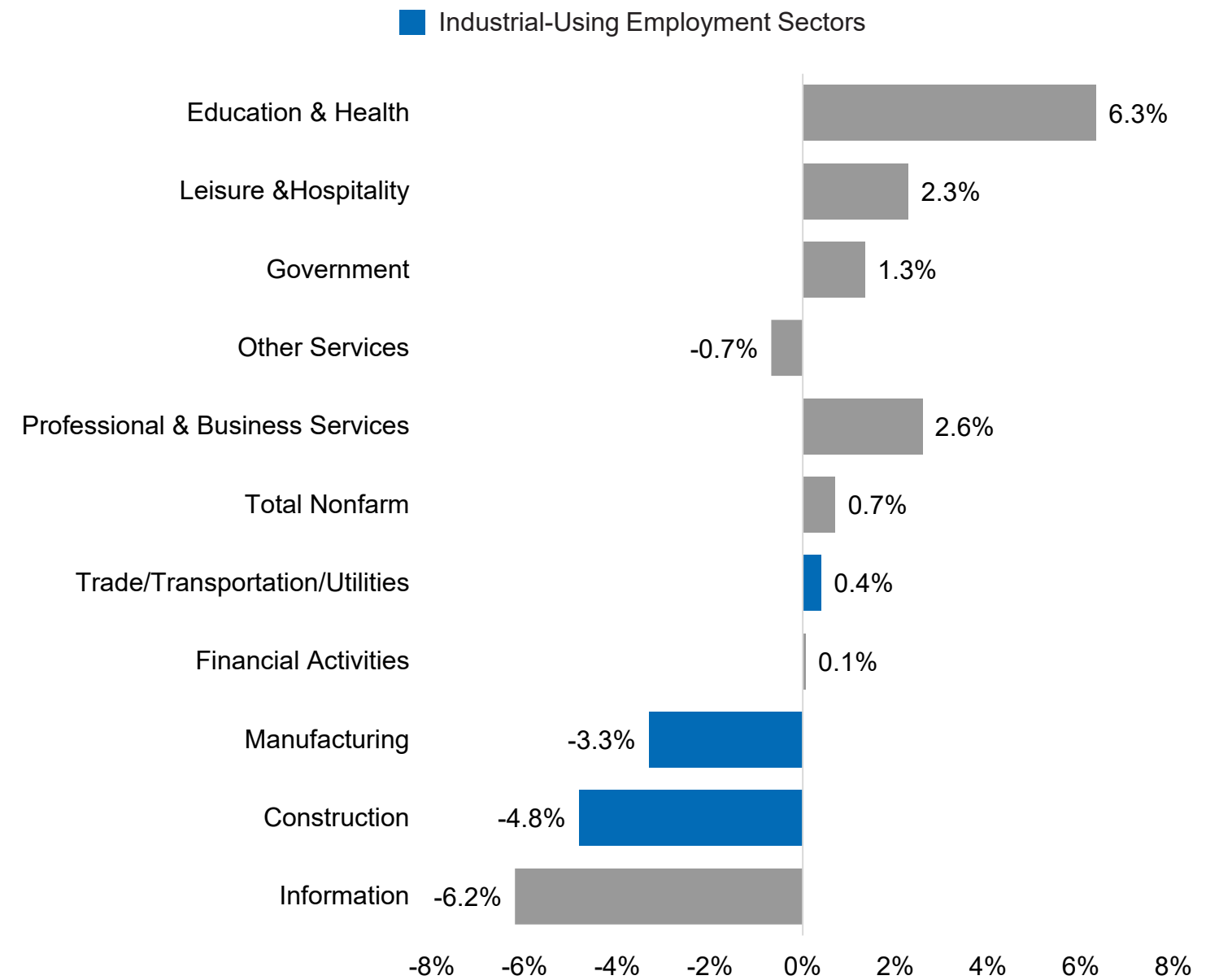
Professional & Business Services Added Jobs While the Tech Sector Continued to Shed

Job gains in the Professional & Business Services, Education & Health, Leisure & Hospitality and Government outpaced losses in the Tech (Information Technology), Construction, and Manufacturing sectors. Fortunately, Professional & Business Services remains Silicon Valley's largest employment sector and is expanding once again, which bodes well for the R&D 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

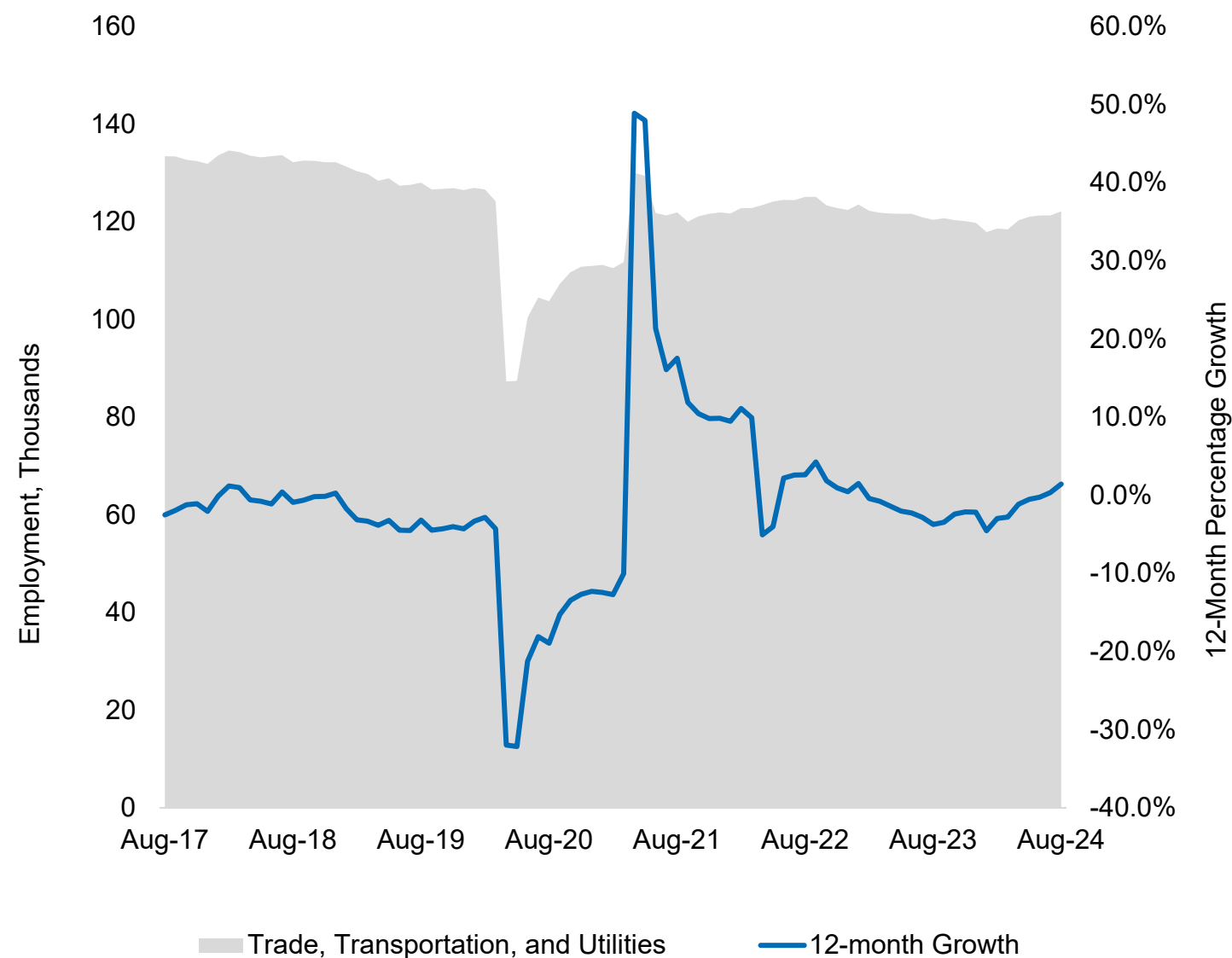


Source: U.S. Bureau of Labor Statistics, San Jose-Santa Clara-Sunnyvale

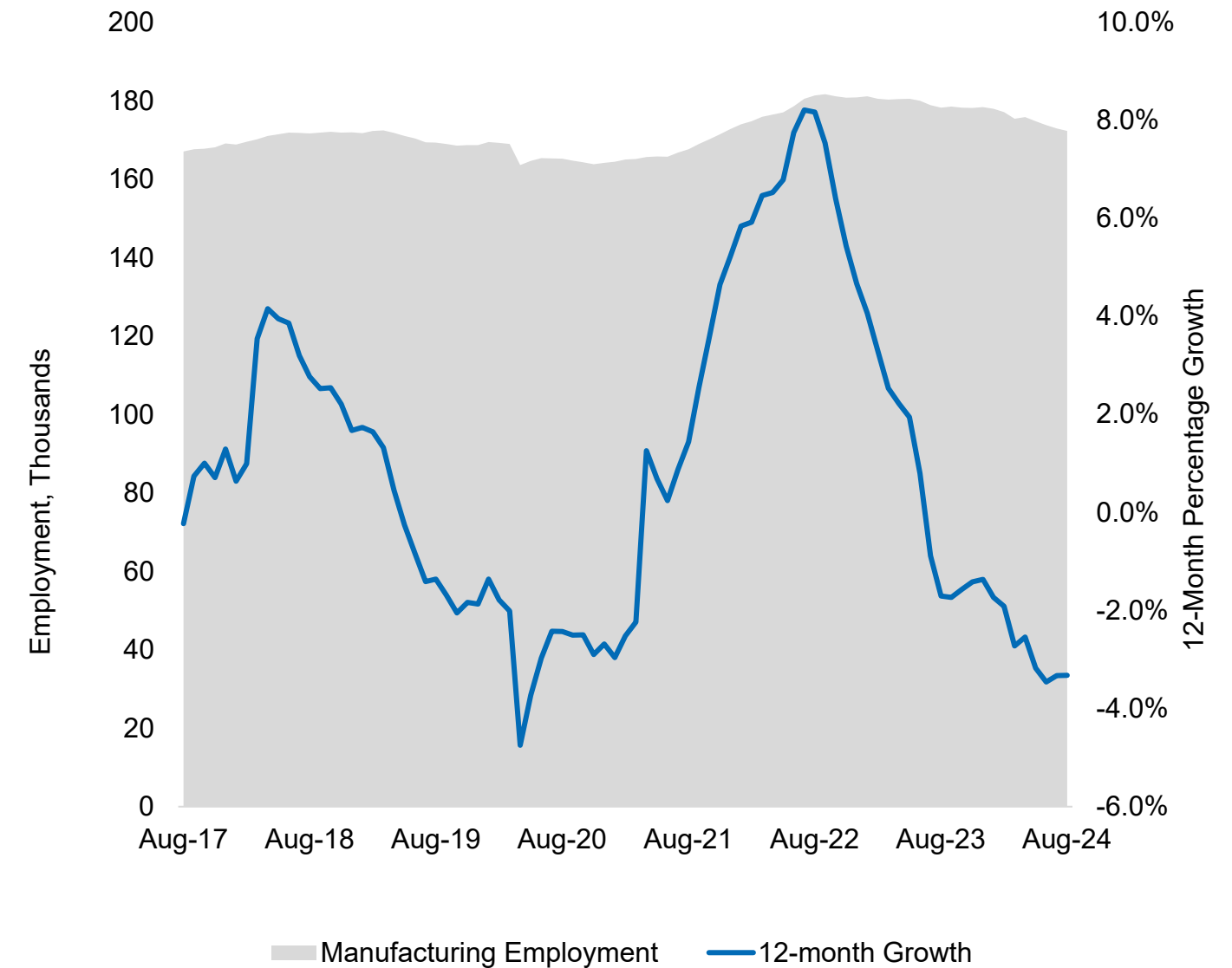
Mixed Signals for Industrial/R&D Demand Drivers

After peaking in the summer of 2022 as demand for AI hardware exploded, employment in the manufacturing sector shed jobs. Employment in this sector contracted by 3.3% year-over-year through August 2024. Meanwhile, the trade/transportation/utilities sector has posted 6 consecutive months of positive job growth after shedding jobs at the end of 2023 and into the first three months of 2024. As the economy hits bottom and then starts improving, we expect these two sectors will quickly rebound.

Total Employment and 12-Month Growth Rate, Trade/Transportation/Utilities



Total Employment and 12-Month Growth Rate, Manufacturing



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

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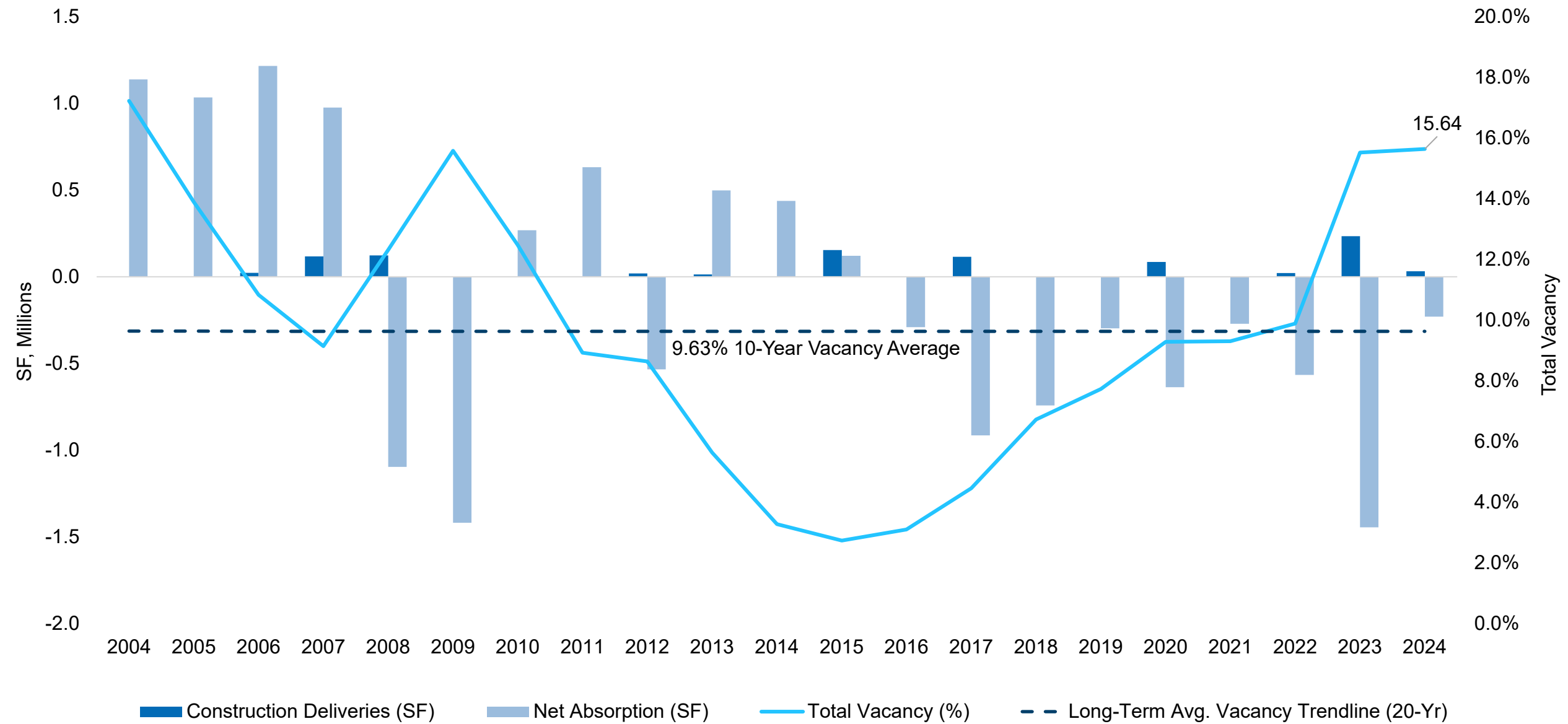
Leasing Market Fundamentals



Vacancy Rate Stabilization Signals a Plateau of High Vacancy Rates

The South Peninsula's Research and Development (R&D) market continues to show signs of stabilization, evidenced by steady vacancy rates since early 2024. Despite negative net absorption of 116,623 square feet in the third quarter, market indicators suggest vacancy levels may have peaked. A notable transition from sublease to direct lease transactions indicates improving market fundamentals in the South Peninsula.

Historical Construction Deliveries, Net Absorption, and Vacancy

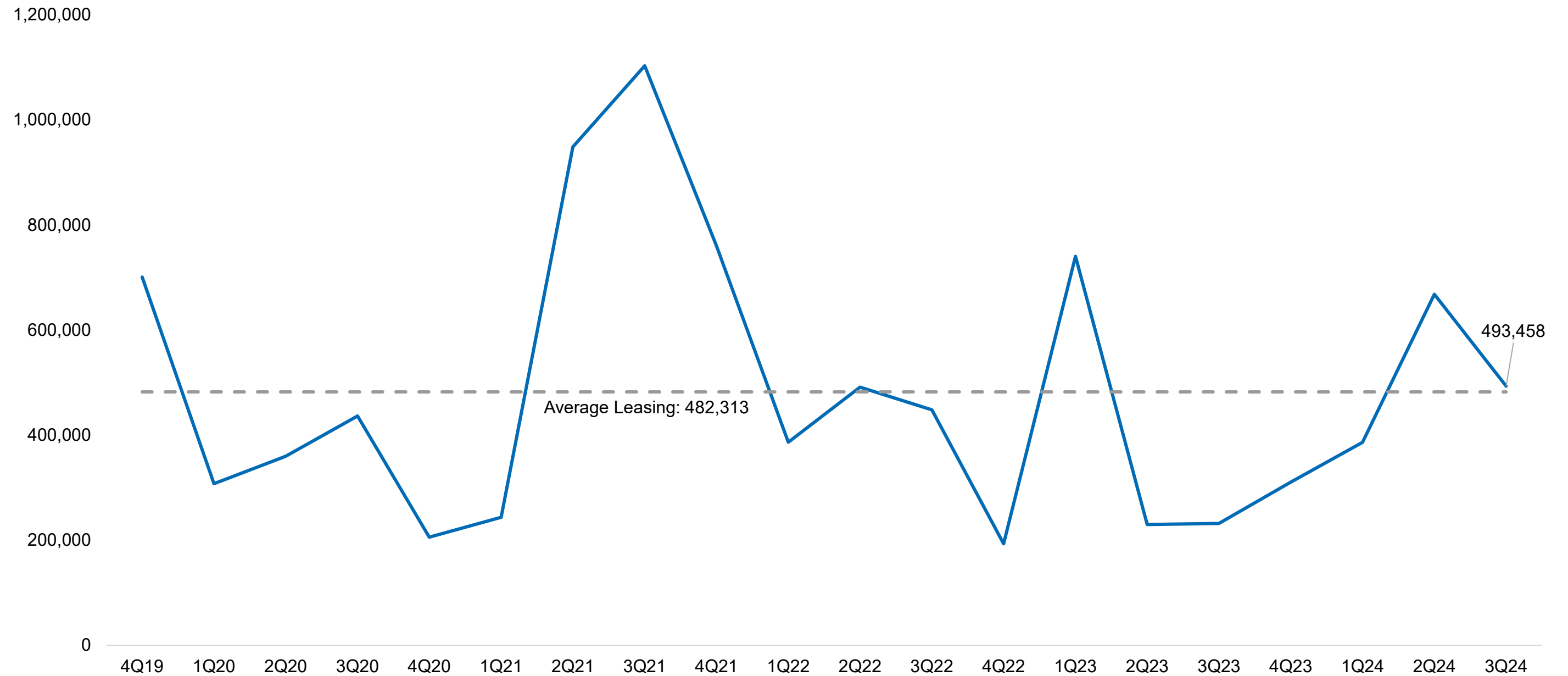


Source: Newmark Research

Leasing Activity Stabilizes in Q3

In line with previous projections, R&D sector leasing activity moderated this quarter but remained marginally above the five-year average. This moderation reflects typical market fluctuations rather than a broader trend. Our brokers predict multiple large R&D transactions approaching completion will support robust leasing activity for the fourth quarter like what we saw in the second quarter of 2024.

Total Leasing Activity (SF)

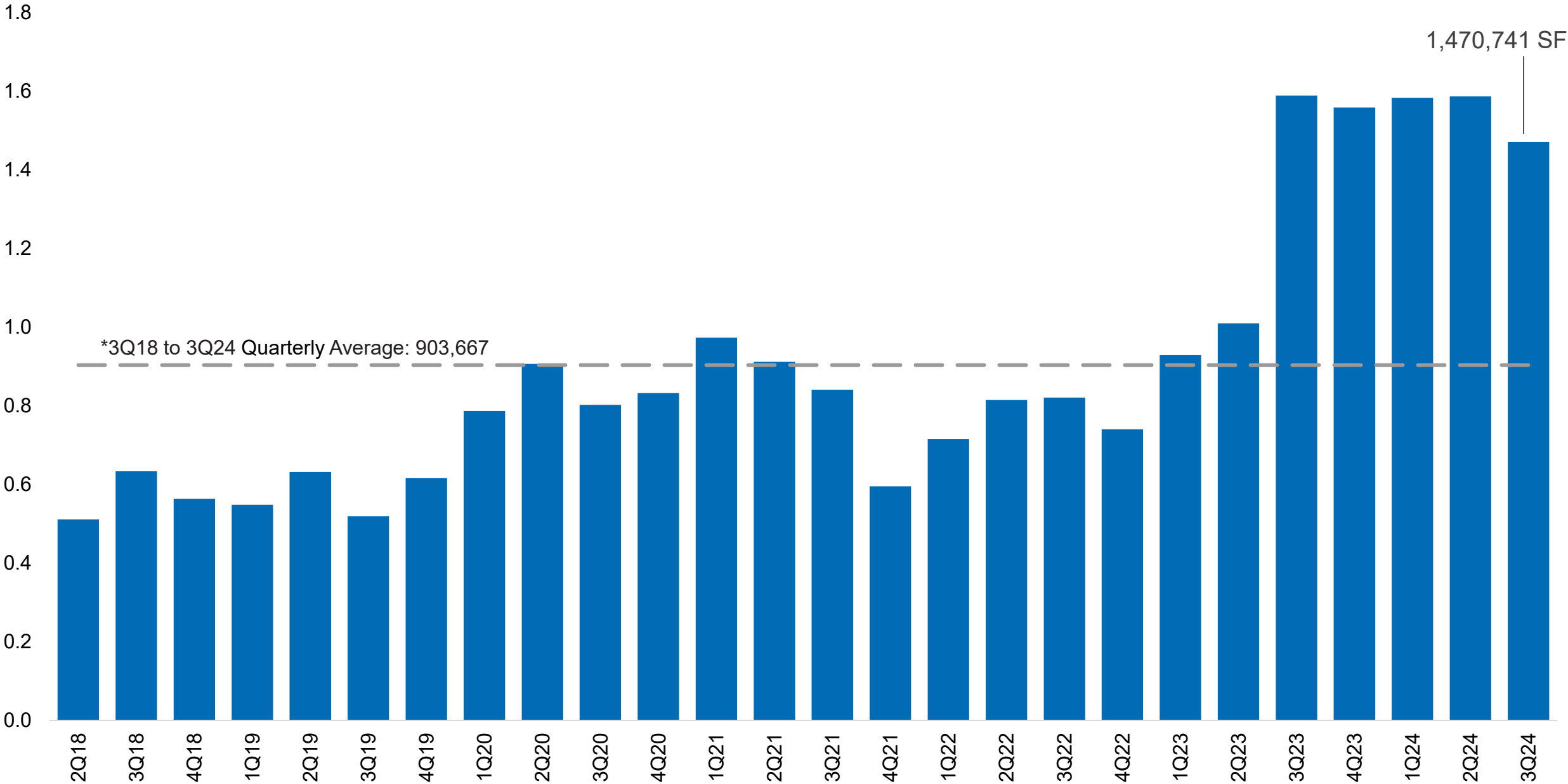


Source: Newmark Research, CoStar

South Peninsula Shedding R&D Sublease Availability

Sublease availability in the South Peninsula market decreased by 116,213 square feet during the third quarter of 2024, though no new sublease transactions were recorded. Significant sublease inventory remains in the market, largely due to space reductions by major occupiers in 2023, with Google and Meta alone accounting for 631,810 square feet. The increasing proportion of direct lease transactions relative to subleases suggests early signs of market recovery since hitting record high sublease availability in 2023.

Available R&D Sublease Volume (msf)

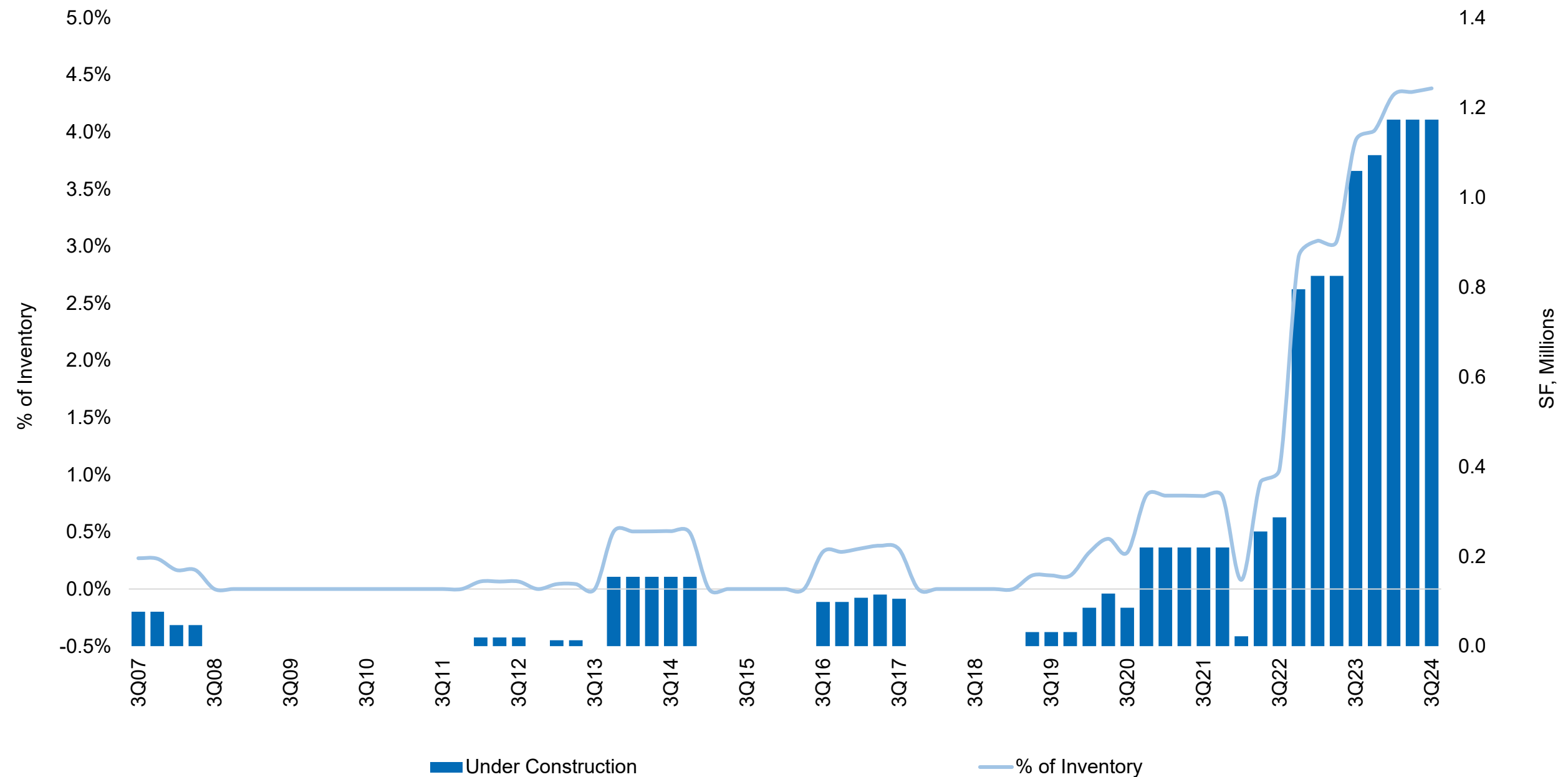


Source: Newmark Research, CoStar

R&D Construction Pipeline Remains Unchanged in Q3

The R&D construction pipeline remained static during the third quarter of 2024, with no new groundbreakings or project deliveries. The initial phase of the Elco Yards development in Redwood City is scheduled for completion in early 2025. New construction projects are unlikely in the near term due to several market factors: weakened demand, elevated interest rates, high construction costs, and increased caution among both lenders and developers.

Industrial Under Construction and % of Inventory

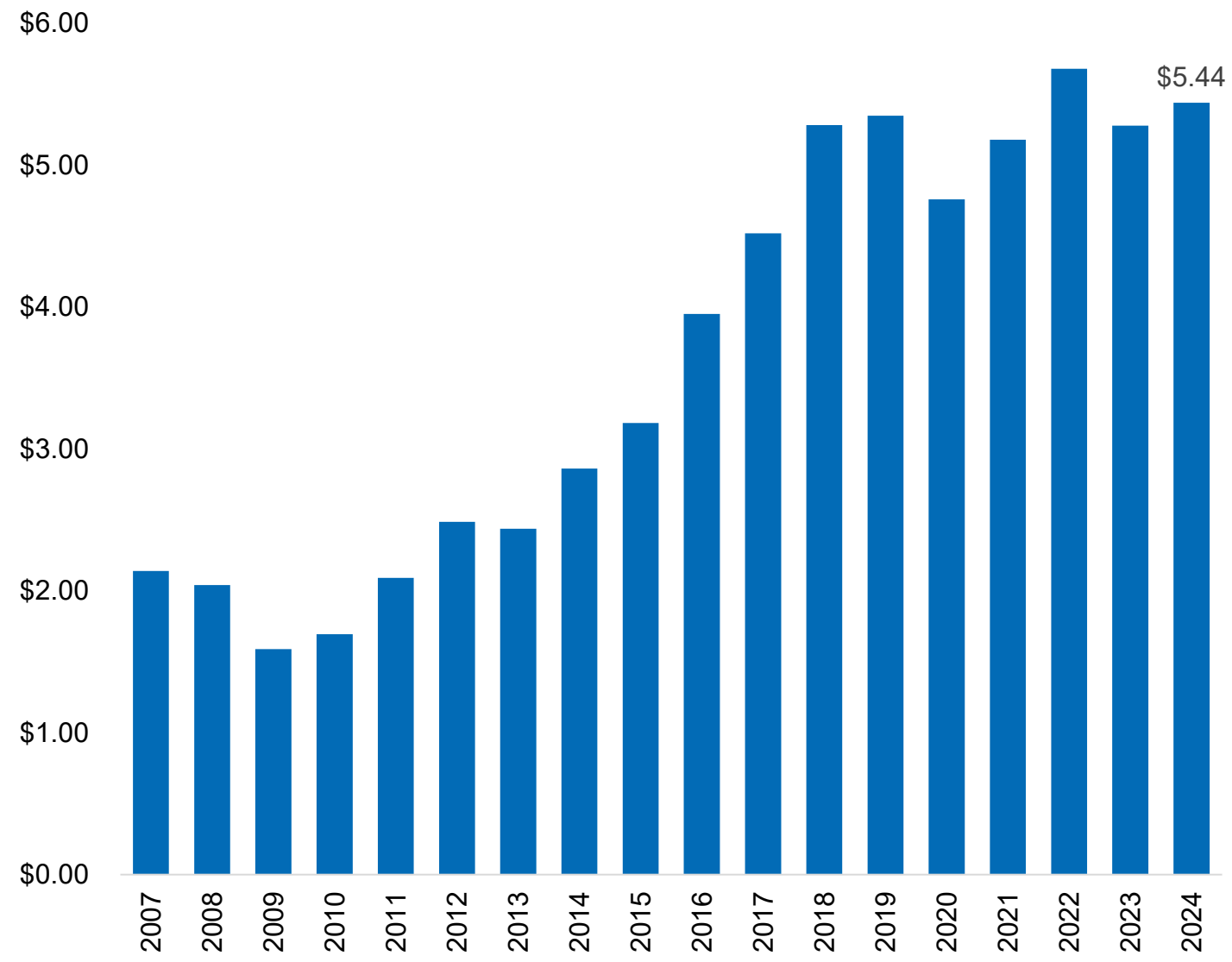


Source: Newmark Research, CoStar

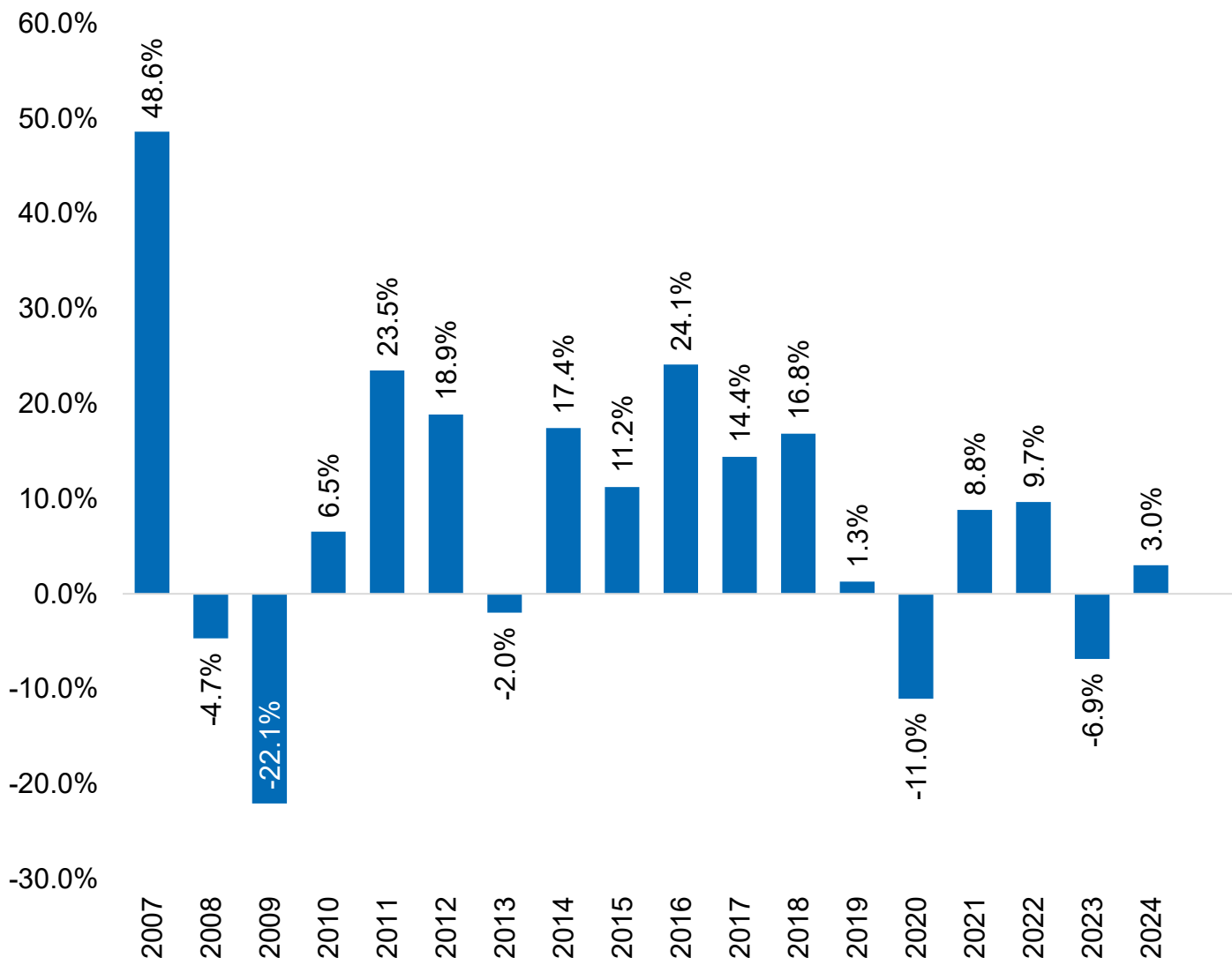
Stabilizing R&D Rents: A Balancing Act in the South Peninsula Market

After a promising rebound in R&D asking rents in the second quarter, when prices rose to \$5.59/SF, the third quarter witnessed a slight adjustment, bringing the average rent down to \$5.44/SF in the South Peninsula. This change reflects current market-wide trends in the R&D and office property markets. The previous rise had offered a glimpse of recovery after a prolonged six-quarter period of rent declines, which had peaked at \$5.82/SF in the third quarter of 2022.

R&D Average Asking Rent, \$/SF, NNN



Year-over-Year Asking Rent Growth Rate % Change



Source: Newmark Research



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Life Science Drives Q3 Leasing Success

Third-quarter 2024 leasing volume reached 493,458 square feet, marking the second consecutive quarter to exceed the 10-year average of 475,596 square feet. The South Peninsula market is experiencing increased activity in the life science sector, with life science transactions accounting for more than 50% of third-quarter deals. This trend is particularly relevant in the Redwood City submarket.

Select Lease Transactions

Tenant	Building	Submarket	Type	Square Feet
xAI	1450 Page Mill Road	Stanford Research Park	Direct Lease	77,269
<i>xAI has secured a new direct lease, which accommodates the majority of its research teams. Additionally, xAI maintains a small presence in San Francisco, occupying a portion of the former OpenAI building.</i>				
Impossible Foods	400 Saginaw Drive	Redwood City - Seaport	Lease Renewal	60,841
<i>Impossible Foods has renewed its lease for 60,841 square feet at 400 Saginaw Drive, a location they have occupied since 2016.</i>				
Revolution Medicines	500 Saginaw Drive	Redwood City - Seaport	Lease Expansion	43,293
<i>Revolution Medicines has secured a direct lease, increasing its total footprint in Redwood City to 186,104 square feet.</i>				
Astrazeneca	200 Cardinal Way	Redwood City – Seaport	Direct Lease	40,573
<i>AstraZeneca, the biopharmaceutical company, has leased the entire 1st and 2nd floors, totaling 40,573 square feet.</i>				
PTC Therapeutics	303 Ravendale Drive	Mountain View – South Middlefield	Direct Lease	35,849
<i>PTC Therapeutics has signed a lease exceeding 12 years for a Class A lab space in Mountain View, further contributing to the list of significant life science transactions in the South Peninsula R&D market.</i>				

Source: Newmark Research

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Appendix / Tables





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