

Peninsula Industrial

Market Forecast

Industrial

Trends

Vacancy



Absorption



Rental Rate



New Construction



Notable Lease Transactions

*Evaluate

3885 Bohannon Dr, Menlo Park
84,643 s.f. (renewal)

Golden State Arts
210-212 Littlefield Ave, South San Francisco
34,100 s.f.

WHCI Plumbing Supply
11 Guittard Rd, Burlingame
22,250 s.f.

Cosentino USA
322 E Grand Ave, South San Francisco
21,350 s.f.

Notable Sales Transactions

Dividend Capital
1404-1422 San Mateo Ave
South San Francisco
\$8.02M - \$134/s.f.

SF Rent
50 Broderick Rd, Burlingame
\$7.45M | \$227/s.f.

150 Airport SSF LLC
150 Airport Blvd, South San Francisco
\$4.6M | \$171/s.f.

*R&M Properties LLC
1010 O'Brien Dr, Menlo Park
\$4.4M | \$314/s.f.

The Peninsula industrial market's vacancy rate kept falling to unprecedented levels following 39,932 s.f. of positive net absorption during the fourth quarter. The steady quarter brought the year's absorption gains to 775,115 s.f., which dropped the county's vacancy rate by 150 basis points year-over-year to a record low of 2%. Despite limited availabilities and increasing rental rates, tenant demand remains strong, with a particular emphasis on the north county region for logistics and distribution purposes. Steady demand is expected to support a healthy market throughout 2017, but activity is unlikely to reach the outstanding levels seen in previous years as tenants struggle to find available space that suits their requirements.

The north county region continues to be the epicenter that anchors the Peninsula's leasing activity. While there were no significant logistics or distribution transactions, warehouse activity guided the north county region to 63,904 s.f. of positive net absorption this quarter. The South San Francisco submarket led the way, as the whole-sale art store Golden State Arts occupied 34,100 s.f. at 210-212 Littlefield Drive. Cosentino USA procured 21,350 s.f. at 322 East Grand Avenue, which will be used as a showroom. Burlingame was the only north county submarket to finish in the red, but it turned in the third-largest transaction when WHCI Plumbing Supply obtained 22,250 s.f. at 11 Guittard Road. The northern region's strong finish, combined with space being pulled from the market, led to an extraordinary 330 basis point decline from the previous quarter's vacancy rate. Meanwhile, stagnant activity in the southern region caused the vacancy rate to increase 150 basis points over the previous quarter.

Record low vacancy rates led to another significant increase in the Peninsula's average rental rate, which currently stands at \$1.56/s.f., NNN. This was a 9.9% surge over the previous quarter, and a 26.8% year-over-year increase. The South San Francisco submarket encountered the most notable quarter-over-quarter increase of 24.2%, to \$1.18/s.f., NNN, while the particularly constricted submarkets of Belmont and Foster City/Redwood Shores have pushed rental rates to a Peninsula leading \$2.72/s.f., NNN.

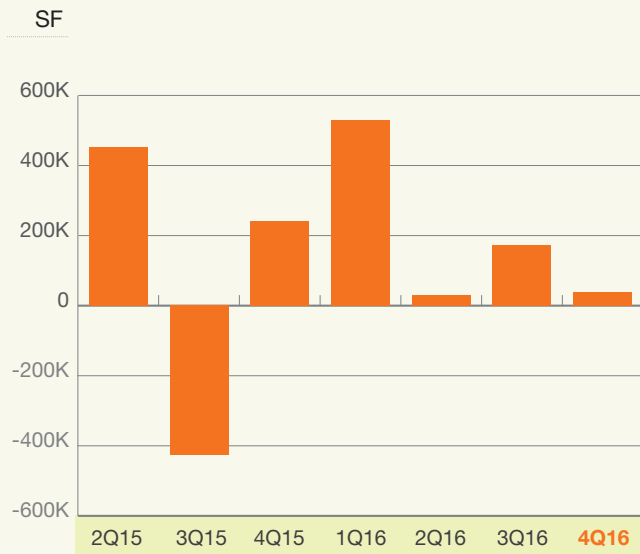
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Area Review

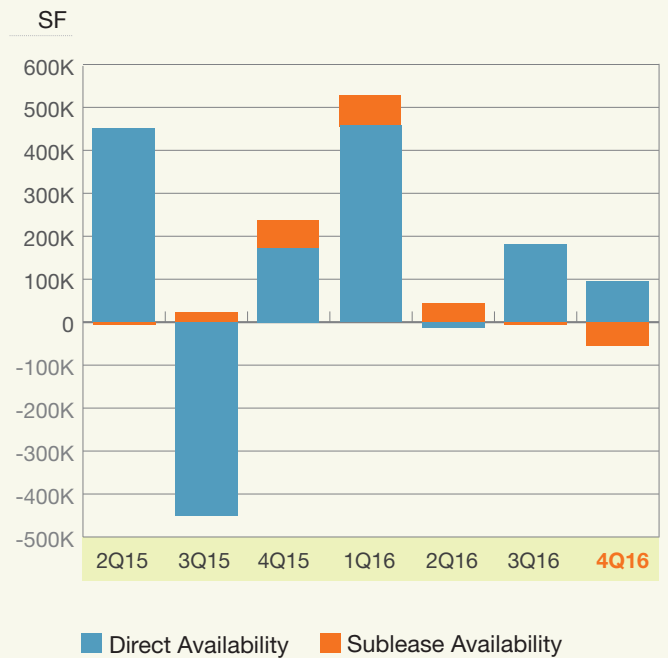
Industrial Submarket Statistics

Submarket	Number of Buildings	Total Inventory	Direct Available	Sublease Available	Total Available	Total Available Rate	Total Vacancy Rate	4Q Net Absorption
Brisbane/Daly City	85	4,738,021	106,895	28,170	135,065	2.9%	0.0%	19,000
South San Francisco	374	16,247,651	601,064	62,617	663,681	4.1%	2.3%	43,153
San Bruno/Millbrae	19	452,873	40,473	0	40,473	8.9%	1.7%	9,045
Burlingame	144	3,773,556	133,731	0	133,731	3.5%	1.8%	(7,294)
San Mateo	44	723,771	18,289	0	18,289	2.5%	3.3%	15,015
Foster City/Redwood Shores	33	920,524	47,982	0	47,982	5.2%	3.9%	13,000
Belmont	44	899,007	11,756	10,500	22,256	2.5%	1.3%	(9,770)
San Carlos	174	4,213,046	120,739	2,269	123,008	2.9%	2.0%	(35,230)
Redwood City	164	4,102,603	196,268	32,779	229,047	5.6%	2.9%	9,532
Menlo Park	134	5,274,662	179,897	14,965	194,862	3.7%	1.8%	(16,519)
Totals	1,215	41,345,714	1,457,094	151,300	1,608,394	3.9%	2.0%	39,932

Total Industrial Net Absorption



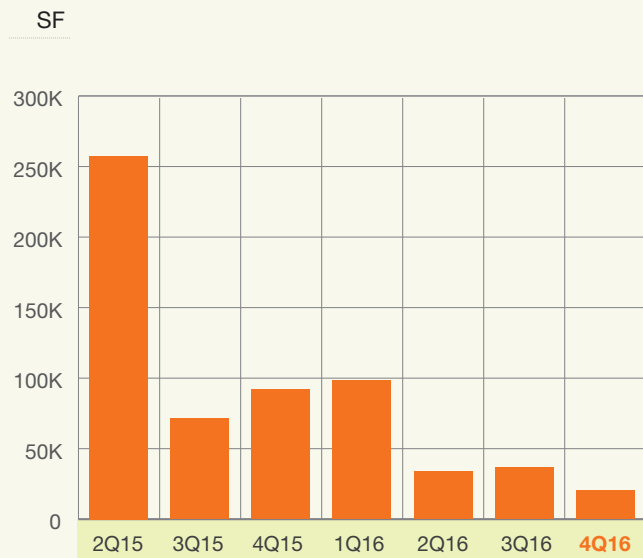
Available Industrial Space: Direct vs. Sublease



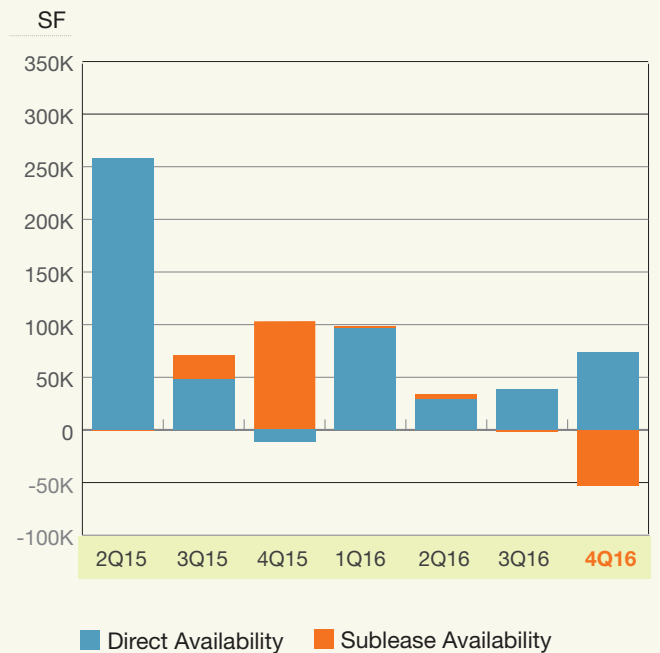
R&D Submarket Statistics

Submarket	Number of Buildings	Total Inventory	Direct Available	Sublease Available	Total Available	Total Available Rate	Total Vacancy Rate	4Q Net Absorption
Brisbane/Daly City	6	246,113	0	0	0	0.0%	0.0%	0
South San Francisco	73	3,709,650	47,723	6,327	54,050	1.5%	1.7%	34,875
San Bruno/Millbrae	6	231,212	7,680	0	7,680	3.3%	3.3%	9,045
Burlingame	37	1,036,572	33,910	0	33,910	3.3%	3.6%	(15,686)
San Mateo	11	259,902	0	0	0	0.0%	0.0%	0
Foster City/Redwood Shores	35	1,203,198	32,728	0	32,728	2.7%	1.7%	13,000
Belmont	13	376,652	7,500	10,500	18,000	4.8%	2.0%	(7,500)
San Carlos	47	1,498,341	38,320	0	38,320	2.6%	2.7%	(17,908)
Redwood City	49	1,837,527	161,384	22,779	184,163	10.0%	4.9%	(4,005)
Menlo Park	71	3,544,341	150,415	14,965	165,380	4.7%	1.9%	8,563
Totals	343	13,791,397	479,660	54,571	534,231	3.9%	2.4%	20,384

Total R&D Net Absorption



Available R&D Space: Direct vs. Sublease



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Offices

Seattle
206.296.9600

Bellevue
425.454.7040

South Seattle
206.248.7300

Tacoma
253.722.1400

Olympia
360.705.2800

Portland
503.221.9900

San Francisco
415.229.8888

Redwood Shores
650.769.3600

Silicon Valley
408.970.9400

Sacramento
916.970.9700

Roseville
916.751.3600

Orange County
949.557.5000

Inland Empire
909.764.6500

San Diego
858.509.1200

Carlsbad
760.430.1000

Reno
775.301.1300

Phoenix
602.513.5200

Contact

Reed Payne
Executive VP, Brokerage
Northern California
415.229.8888
rpayne@kiddermathews.com

Designated Broker
Reed Payne | LIC #00818935

With no plans for new construction in the pipeline, and inventory being lost to R&D conversions, industrial tenants will be hard-pressed to find vacancy relief in the near future.

Investment activity occurred throughout the Peninsula, but transactions remained relatively small as 2016 came to a close, with just six total deals combining for \$31.12 million in dollar volume. The average price per square foot was \$196, the second highest price per square foot of 2016 behind the third quarter. However, the third quarter figure was heavily influenced by Greenland USA's Oyster Point redevelopment acquisition for \$437/s.f. The largest investment transaction of the fourth quarter was an off-market deal carried out by Dividend Capital, who purchased 1404-1422 San Mateo Avenue in South San Francisco for \$8.02 million, or \$134/s.f. Following close behind was SF Rent's procurement of 50 Broderick Road in Burlingame for \$7.45 million, or \$225/s.f. SF Rent plans to conduct interior and exterior renovations before leasing the property. As vacancy rates settle near record lows and demand persists, investment activity will likely continue into 2017.

R&D

R&D properties experienced their 11th consecutive quarter with positive absorption, but activity continued to fluctuate throughout the Peninsula as gains this quarter totaled only 20,384 s.f. Half of the submarkets finished the quarter with positive absorption, while the other half finished in the red. South San Francisco maintained its momentum from the previous two quarters to close the year with 34,875 s.f. of positive net absorption, while the Foster City/Redwood Shores submarket followed up with 13,000 s.f. Menlo Park was home to the most notable transaction, as the medical device company Evalve renewed its 84,643 s.f. at 3885 Bohannon Drive, but the submarket was otherwise dormant, finishing with just 8,563 s.f. of positive net absorption. Despite the growing interest in R&D space in the mid-to-southern region of the county, San Carlos led the Peninsula with 17,908 s.f. of negative net absorption.

Leasing activity caused the vacancy rate to dwindle to 2.4%, a 20 basis point dip over the previous quarter and a 30 basis point year-over-year decline. Tenants in the market continue to be plagued by availability constraints as Redwood City became the only submarket with a vacancy rate exceeding 4%. As a result, the number of transactions declined 61% year-over-year to 16. New R&D space continues to come from converted industrial buildings, as there are no plans for new development, but the rate of conversion is insufficient when compared to the tenant demand.

Rental rates continued their torrid ascent in correlation to the constricted market, with the average Peninsula rate increasing 10.3% over the previous quarter to \$2.69/s.f., NNN. On a year-over-year basis, the average rate has increased 27.5%. The South San Francisco submarket set a new high-water mark during the fourth quarter after experiencing an extraordinary 35.2% quarter-over-quarter increase to \$3.34/s.f., NNN, while San Bruno/Millbrae and Belmont surged 23.8% and 20.9%, respectively. Rent growth will continue as the demand continues to exceed the available supply, adding to the historic 57.6% surge in rents that has already occurred since the fourth quarter of 2014.

Investment activity declined significantly from the previous quarter, with just a single transaction in the past three months. R&M Properties purchased the 14,000 s.f. property at 1010 O'Brien Drive in Menlo Park for \$4.4 million, or \$314/s.f. The seller, Noren Products, previously occupied the space as an owner/user, but R&M Properties intends to lease out the property. The final sale caps off a year that experienced six investment transactions totaling \$84.56 million, for an average price per square foot of \$337. 2016's total number of transactions and dollar volume declined roughly 29% and 22% over the previous year, respectively, but the price per square foot increased 24.4% during that same time frame. Although the number of transactions declined, investment activity should carry into 2017 as steady demand will continue to support low vacancy rates, enhancing the attractiveness of the area's R&D assets.