

Quarterly Report

SILICON VALLEY COMMERCIAL SPACE

Q1 2022



This report is released on a quarterly basis by the Silicon Valley Institute for Regional Studies, in partnership with JLL Silicon Valley. It covers trends in commercial space within Silicon Valley, encompassing San Mateo and Santa Clara Counties and the cities of Fremont and Newark.

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Summary

Silicon Valley's largest technology companies seem to have finally overcome the numerous pandemic-related setbacks in their return-to-office planning. Apple, Google, and Meta, for example, have begun implementing their post-pandemic programs, signaling a conscious step toward a near-normal level of in-office operations. Leasing volume within the region continued at a steady cadence in Q1, in line with historical figures, despite increasing construction and fit-out (interior space build-out) costs. Meanwhile, regional commercial space rental rates increased slightly, in aggregate, following two years in which they had been artificially held steady; as a result, there were high-water marks (observed price-highs) observed in Q1 for Industrial and Lab space.

Leasing Activity. While leasing volume was similar to that of 2021 in terms of square footage, there was an increase in total number of leases executed in Q1 – indicating a smaller average amount of space per lease. A couple notable leases inked this quarter included the 438,000 square foot under-construction office lease at the Bay Meadows Project in San Mateo and Nio's 201,000 square foot Flex/R&D lease in North San Jose.

New Construction. Construction completions were fairly limited in Q1. Notable completions included two buildings at Kilroy Oyster Point I, pre-leased to both Stripe and Cytokinetics, and the new Fortinet Headquarters in Santa Clara. While the construction pipeline for the region remains healthy, construction costs have rapidly increased since December 2020. According to the California Department of General Services, the Construction Cost Index (CCCI) reflects a dramatic increase of +8.2% through Q1 2022 after a record high +13.4% increase in 2021.

Asking Rents. Asking rates have continued to maintain an upward trajectory; in particular, rental rates for Lab and Industrial space reached new all-time highs in Q1. As a result, landlords have continued to explore opportunities to secure higher rents by converting Office or Flex R&D space to Lab, which remains in extremely short supply.

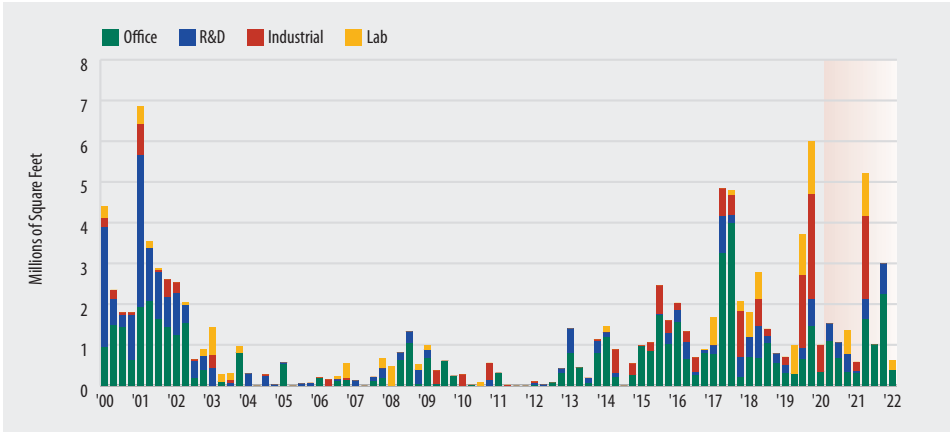
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A. New Commercial Development

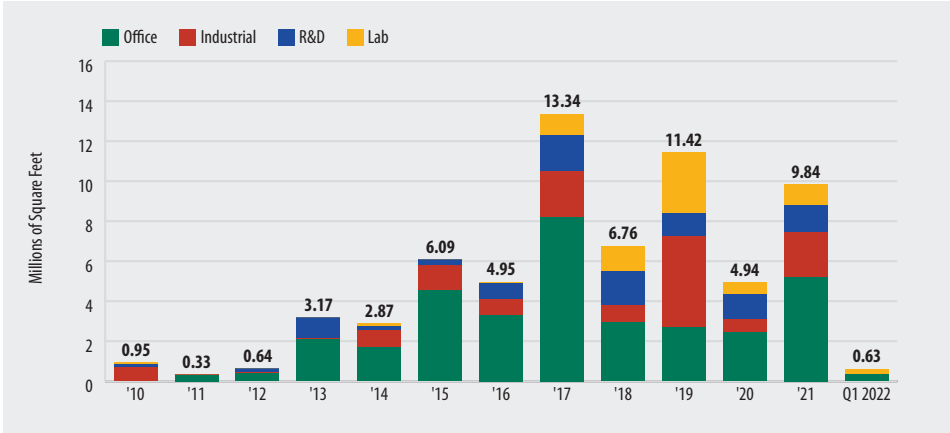
A1. Quarterly Commercial Space Completions by Sector, Silicon Valley, 2000 – Q1 2022

Silicon Valley's Q1 2022 commercial space completions totaled approximately 628,000 square feet — slightly higher than the previous year's Q1 totals.



The 628,000 square feet of newly-completed commercial construction in Q1 was completely pre-leased. While only around a third of all completions are for lab projects, lab completions are set to become a steadier contributor to this figure in the future.

A2. Annual and Year-to-Date Commercial Space Completions by Sector, Silicon Valley, 2010 – Q1 2022



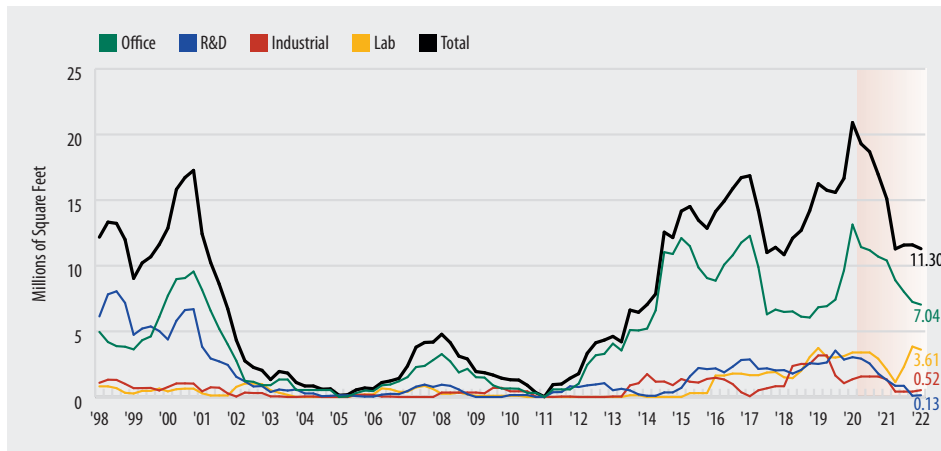
A total of 628,000 square feet of Silicon Valley commercial space was completed through Q1 2022. An additional 3.5 million square feet of commercial space is slated for completion within the remainder of the year.

A3. Large Commercial Space Completions, Silicon Valley, Q1 2022

| Development Name/Address | City | Owner/ Developer | Rentable Building Area (square feet) | Percent Leased at Time of Delivery | Class & Type of Space |
|--|---------------------|----------------------|--------------------------------------|------------------------------------|-----------------------|
| Fortinet Headquarters 901 Kifer Road | Santa Clara | Fortinet/Sares Regis | 172,000 | 100% | Class A Office |
| Kilroy Oyster Point I 370 Oyster Point Boulevard | South San Francisco | Kilroy Realty | 221,000 | 100% | Class A Office |
| Kilroy Oyster Point I 350 Oyster Point Boulevard | South San Francisco | Kilroy Realty | 234,892 | 100% | Class A Lab |

There were three notable large commercial space completions in Silicon Valley during the first quarter of 2022. The first two completed buildings were at the Kilroy Oyster Point project. While the project is marketed as a lab/life science use, fintech company Stripe had pre-leased two buildings in the first phase of the project, one of which was completed this quarter. The third building in the first phase remains consistent with the lab use, pre-leased by Cytokinetics.

A4. Quarterly In-Progress Commercial Space Developments by Sector, Silicon Valley, 2000 – Q1 2022



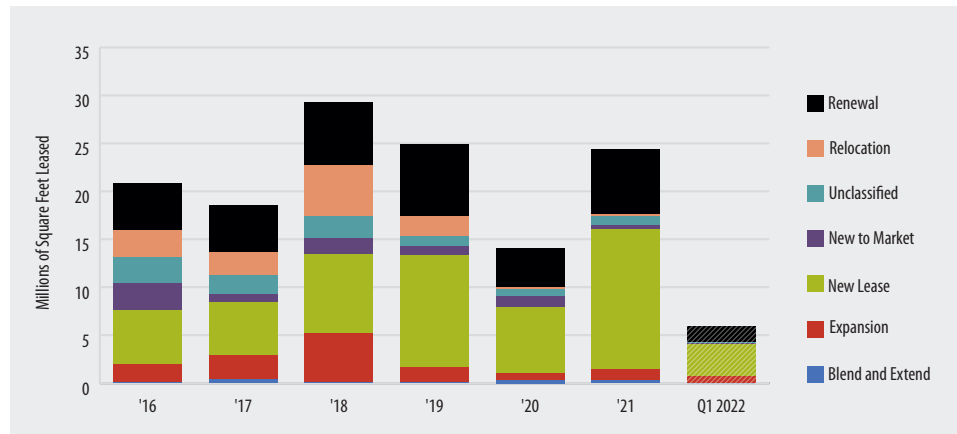
Of the Silicon Valley commercial construction underway in Q1 2022, a large share (62%) is Office, 32% is Lab, 5% Industrial, and the remaining 1% is Flex/R&D.

There was more than 11.2 million square feet of commercial space under construction in Silicon Valley at the end of Q1 2022. Of that total, 3.5 million square feet of space is expected to be completed by the end of the year, including Google’s Bay View Campus (1.1 million square feet of Office), Adobe’s North Tower (700,000 square feet of Office) and the fifth and sixth buildings of LinkedIn’s Mountain View Campus (518,000 square feet, combined).

B. Commercial Leasing Activity

B1. Square Footage of Commercial Space Leases by Type, Silicon Valley, 2016 – Q1 2022

The pace of Silicon Valley commercial leasing activity continued at pre-pandemic levels in Q1 2022. There continues to be a noticeable absence of relocations and new entrants to the market, however, which together contributed less than 4% of all leasing activity since the beginning of 2021.



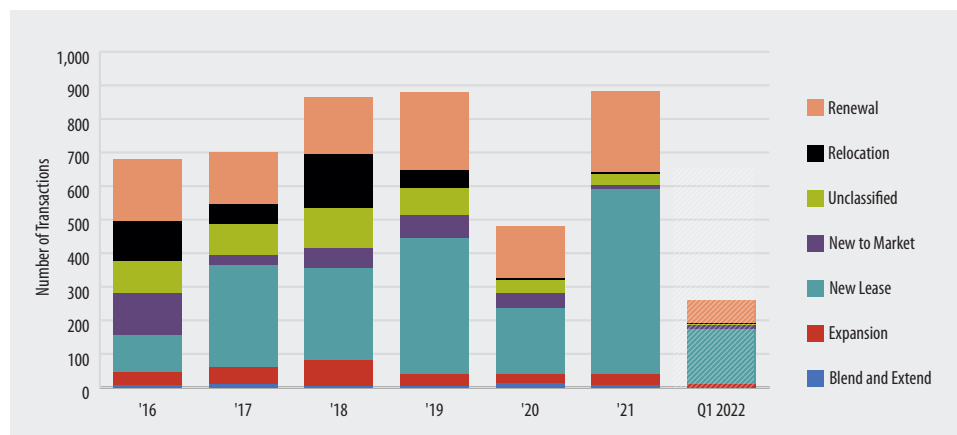
Lease transactions include New to Market (tenant moves into a new market from another market), Relocation (tenant moves from one location to another in the same market), Renewal (tenant renews its existing lease at its current location), Expansion (when a tenant expands its current premises to include new premises outside of its currently-leased premises), Blend-and-extend (tenant's remaining lease term, usually one to three years, is extended and the current rental rate is "blended" with a newly negotiated one), and New Lease (when it is unclear if the tenant is new to market, relocating, expanding, or renewing, to indicate that a new lease transaction has taken place).

B2. Total Number of Commercial Space Leases by Type, Silicon Valley, 2018 – Q1 2022

There were more than 260 commercial lease transactions in Silicon Valley in just the first quarter of 2022. This compares to an annual total of 882 in 2021 and 481 in 2020.

The five largest commercial space leases executed in Q1 included a mixture of different space types.

The largest deal was Roblox's new lease at the Bay Meadows project in San Mateo, growing by an additional 438,000 square feet. Nio leased approximately 201,000 square feet of Flex/R&D space in North San Jose, and K&Z Cabinet Company leased approximately 196,000 square feet of Industrial warehouse space in South San Francisco.

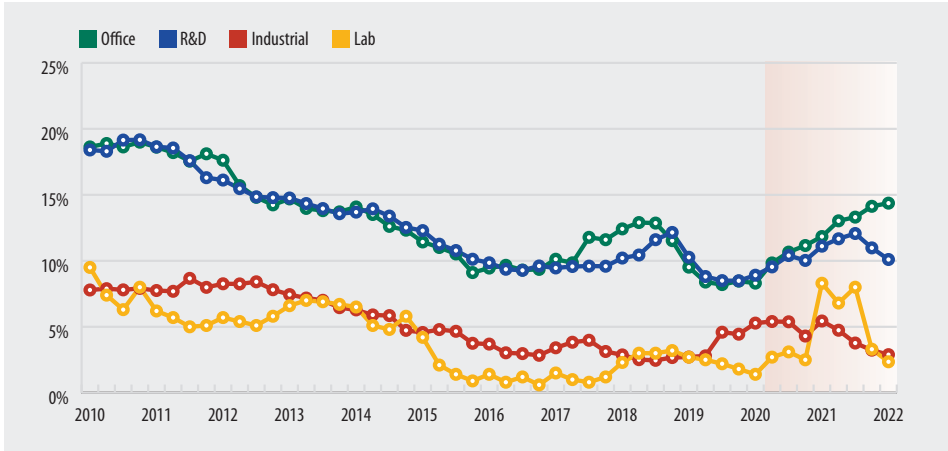


Note: Lease transactions include New to Market (tenant moves into a new market from another market), Relocation (tenant moves from one location to another in the same market), Renewal (tenant renews its existing lease at its current location), Expansion (when a tenant expands its current premises to include new premises outside of its currently leased premises), Blend-and-extend (tenant's remaining lease term, usually one to three years, is extended and the current rental rate is "blended" with a newly negotiated one), and New lease (when it is unclear if the tenant is new to market, relocating, expanding, or renewing, to indicate that a new lease transaction has taken place).

While the number of lease transactions in Q1 indicates a pace that could exceed the annual total in 2021, the average amount of square feet committed per lease continues to trend downwards, reaching the lowest it has been since 2009. This indicates that the average tenant has been cautious about committing to additional space as hybrid work policies may reduce the overall need for traditional space.

C. Commercial Vacancy Rates

C1. Quarterly Vacancy Rates, Silicon Valley, 2010 – Q1 2022



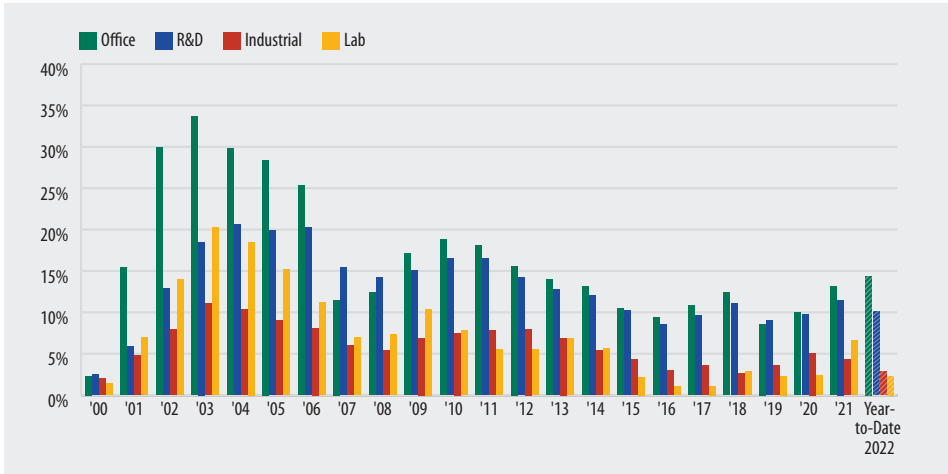
The region continues to have the lowest vacancy rates of any major market across the country. The rebound of leasing activity that was observed in 2021 will likely keep vacancy rates steady through 2022.

Silicon Valley commercial vacancy rates overall have declined slightly, with only a minuscule amount of growth in vacancy rates for Office (up 0.2 percentage points in Q1). In contrast, Industrial, Lab, and Flex/R&D vacancy rates have continued a downward trend through Q1 2022.

Silicon Valley office space vacancy rates continued to inch upward through Q1 2022 (+14.4%), though vacancy only grew by a third of a percentage point quarter-over-quarter. The Mid-Peninsula saw occupancy gains, attributed to the delivery of two pre-leased buildings at Kilroy Oyster Point I in South San Francisco, totaling 456,000 square feet. Conversely, we saw occupancy losses farther south in Q1, such as Nutanix vacating several floors in San Jose.

Q1 2022 vacancy rates were 14.4% for Office, 10.1% for Flex/R&D, 2.9% for Industrial, and 2.3% for Lab space. Only office space vacancy rates remained elevated, while all other space types neared pre-pandemic levels.

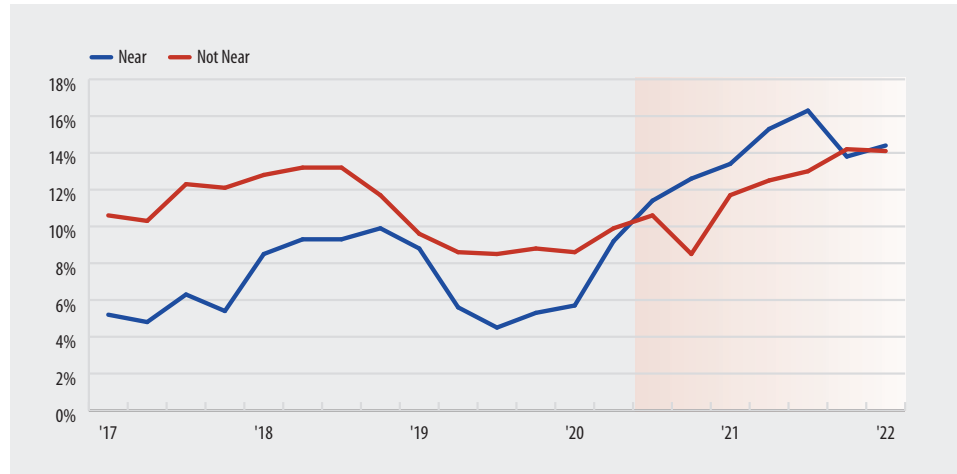
C2. Annual Rate of Commercial Vacancy by Sector, Silicon Valley, 2000 – Q1 2022



Lab space vacancy rates dropped down to 2.3% in Q1 2022, in contrast to 2021's average of 6.6% vacancy.

Silicon Valley's average office vacancy rate in Q1 2022 grew slightly (+1.3%) compared to last year's annual average, whereas Industrial (-1.4%), Flex/R&D (-1.4%), and Lab (-4.3%) vacancy rates came down. This trend was expected, given that the utilization of office space evolves with the proliferation of remote work, whereas Industrial, Flex/R&D, and Lab space have a more practical, in-person use for their space.

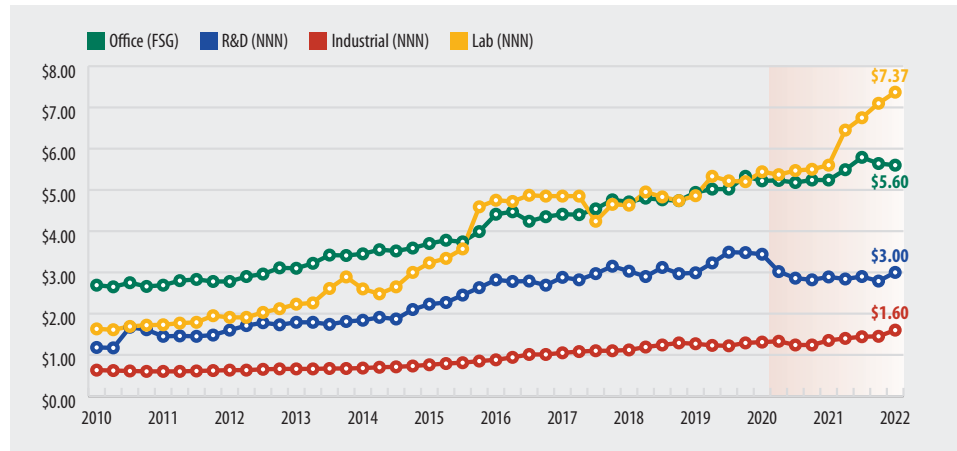
C3. Average Office Space Vacancy Rates by Proximity to Transit, Q1 2017 – Q1 2022



Silicon Valley office space vacancy rates at locations within a 10-minute walk from public transit – which have traditionally been lower than elsewhere due to the ease of employee commutes – rose significantly during the pandemic then trended downward over the past two quarters. Office demand appears to be less one-sided as measures combating COVID outbreaks have re-enabled the amenities proximate to near-transit locations.

D. Commercial Rents

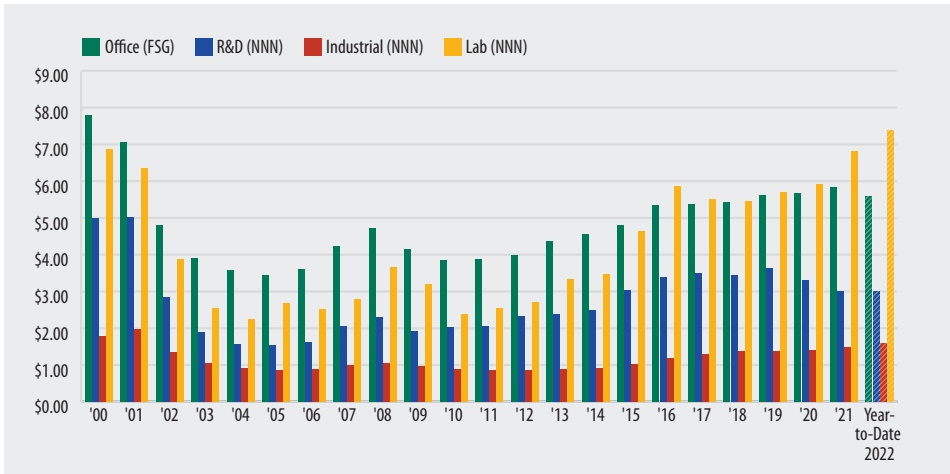
D1. Nominal Quarterly Asking Rents by Sector, Silicon Valley, 2010 – Q1 2022



With the exception of Office, average rental rates continued to rise into 2022, with Industrial and Lab rates reaching new highs quarter after quarter. Of particular note, Lab rates were 31% higher year-over-year in 2022 than during the prior year.

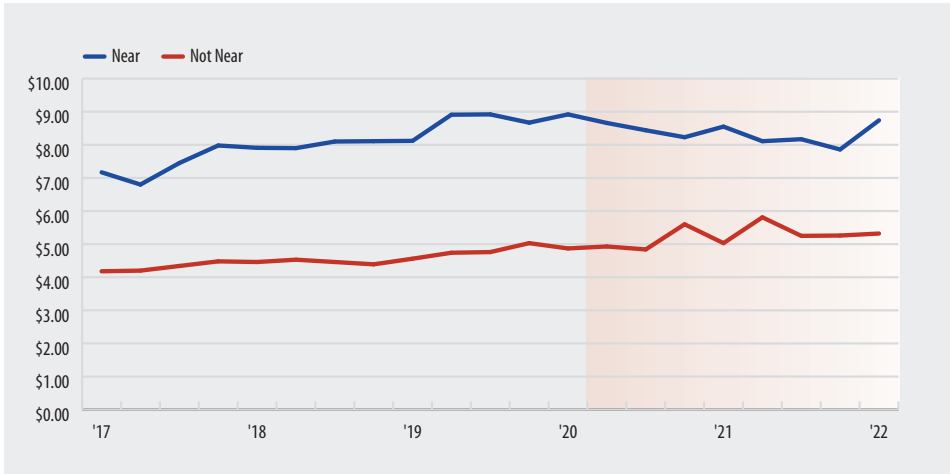
Office space rental rates in Silicon Valley remained lower in Q1 than in New York City (by 17%) but higher than Austin (by 25%), Seattle (by 31%), Portland (by 50%), and Denver (by 53%).

D2. Inflation-Adjusted Annual Average Asking Rents by Sector, Silicon Valley, 2000 – Q1 2022



Inflation-adjusted asking rents for Office space remained steady from 2020 through 2022. Asking rents for Industrial space continue to rise as the lack of land for new development over the past year has stifled overall supply and in turn squeezed the market for industrial space. Lab rents also continue to strike higher due to increased demand paired with the recent influx of new development.

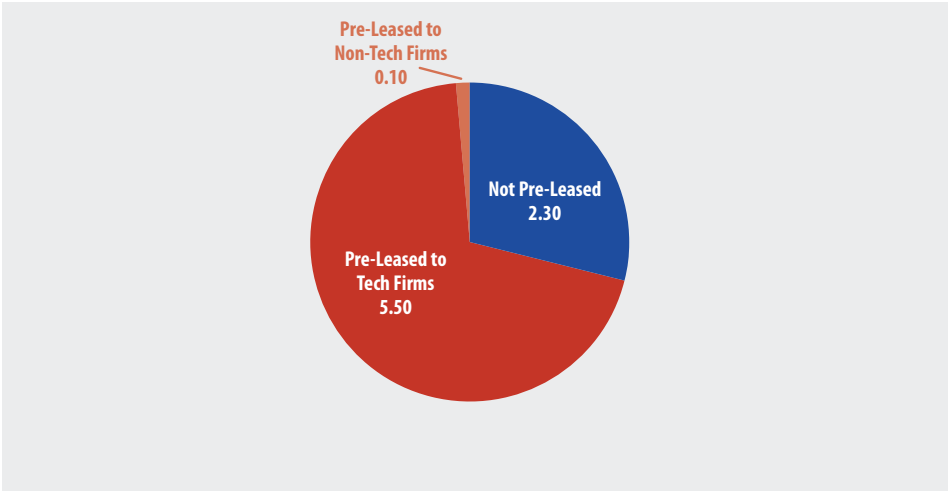
D3. Average Office Space Asking Rents by Proximity to Transit, Q1 2017 – Q1 2022



Silicon Valley Office rents have fluctuated since prior to the pandemic at locations near and not near to transit (within a 10-minute walk of a Caltrain, BART, or VTA station). Asking rents appear to have recovered, and were 64% higher near transit in Q1 2022 than not near transit.

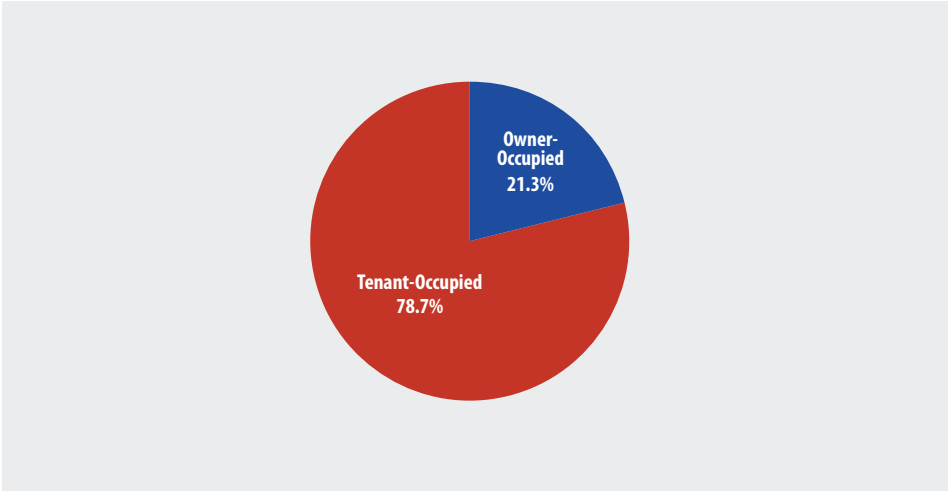
E. Occupancy

E1. Commercial Office Space Under Construction and Share Pre-Leased to Tech Firms, Bay Area, Q1 2022



A total of 7.9 million square feet of new commercial office space was under construction throughout the Bay Area in Q1 2022. Of that total, 5.6 million square feet (71%) has been pre-leased, primarily (98.2%) to tech companies.

E2. Total Inventory of Silicon Valley Office Space, by Owner vs. Tenant Occupancy, Q1 2022



Silicon Valley office space was 79% tenant-occupied and 21% owner-occupied in Q1 2022. This compares to 79% and 21%, respectively, in Q1 of the prior year.

Annotations

Data Source: JLL

Analysis: Silicon Valley Institute for Regional Studies; JLL

Notes: Data represents the end of each annual period unless otherwise noted. Commercial space includes Office, Industrial, R&D and Lab. The JLL statistical inventory and all related reports include office, Flex/R&D, and Lab buildings above 30,000 square feet in Santa Clara County (plus Fremont and Newark) and 20,000 square feet in San Mateo County, and all industrial developments above 10,000 square feet; any attached retail space is not included in total square footage. Silicon Valley data includes San Mateo County, Santa Clara County, and the Cities of Fremont and Newark. Bay Area data includes all San Francisco Bay Area Submarkets, including Silicon Valley, North Bay, Mid-Peninsula, and the East Bay including Alameda and Contra Costa Counties (less Fremont and Newark, which are included in the Silicon Valley submarket). Average office space asking rents are “Full Service Gross” (FSG), which is the monthly rental rate and includes common area maintenance fees, utility fees, and taxes/insurance fees. Industrial, R&D, and Lab asking rents are quoted “triple net” (NNN), which is the monthly base rental rate in which common area maintenance fees, utility fees, and taxes/insurance fees are excluded. The vacancy rate is the amount of unoccupied space, and is calculated by dividing the direct and sublease vacant space by the building base. The vacancy rate does not include occupied spaces presently being offered on the market for sale or lease. Average asking rents, where not noted as nominal, have been inflation-adjusted and are reported in 2022 dollars using the Bay Area Consumer Price Index for all urban consumers from the Bureau of Labor Statistics, 2022 estimate based on data through March. Near transit is defined as located within a 10-minute walk of a Caltrain, BART, or VTA station. Lease transactions include New to Market (tenant moves into a new market from another market), Relocation (tenant moves from one location to another in the same market), Renewal (tenant renews its existing lease at its current location), Expansion (when a tenant expands its current premises to include new premises outside of its currently leased premises), Blend-and-extend (tenant’s remaining lease term, usually one to three years, is extended and the current rental rate is “blended” with a newly negotiated one), and New lease (when it is unclear if the tenant is new to market, relocating, expanding, or renewing, to indicate that a new lease transaction has taken place). In an effort to provide more accurate data and reporting, JLL Silicon Valley redefined inventory classifications for office and Flex/R&D properties. Beginning with the Q1 2021 data, the definition of a property as Office or Flex/R&D was altered to focus more on the structure of the building rather than the use. Apart from downtown areas, the El Camino and Sand Hill Road Corridors, and other office-only pockets, office is now defined as any building with at least four stories in Santa Clara County (plus Fremont and Newark) and at least three stories in San Mateo County. Flex/R&D properties are defined as buildings that have three or fewer stories in Santa Clara County (plus Fremont and Newark) and one to two stories in San Mateo County. Additionally, as of Q1 2021, owner-occupied buildings are included in the JLL statistical inventory and reports. As of Q4 2020, Lab buildings were included as a separate category from R&D. All the aforementioned changes resulted in a large shift in the existing inventory and historical statistics related to both property types; however, as a result of these changes, statistics and reporting now more accurately represent market dynamics in the region.

Resources

For questions regarding this report, contact Ricky Manago (manago@joinventure.org) or Rachel Massaro (massaro@jointventure.org).

For more information about Silicon Valley's commercial real estate market, contact Nicole Chu (Nicole.Chu@am.jll.com) or visit www.jll.com/silicon-valley/en-us/research.

To access Silicon Valley's online data hub, visit www.SiliconValleyIndicators.org.

This quarterly report was prepared by Ricky Manago and Rachel Massaro at the Silicon Valley Institute for Regional Studies, in partnership with Nicole Chu, Wing Lee, and Alexander Quinn at JLL Silicon Valley. Jill Jennings created the report's layout; Robin Doran served as copy editor.

Silicon Valley Institute for Regional Studies

The Silicon Valley Institute for Regional Studies provides research and analysis on a host of issues facing Silicon Valley's economy and society. The Institute is housed within Joint Venture Silicon Valley.

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