

San Diego Medical Office Leasing Up 77% Last Year

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By Kelsi Maree Borland

Last year, San Diego's medical office market built on momentum that began in 2020. In 2021, medical office absorption was up 77% with medical office users taking 280,000 square feet of space, according to research from JLL. The positive absorption helped push medical office vacancy down two basis points to 5.8%, the lowest levels since 2006.

The leasing activity has put upward pressure on medical office rents, which have increased more than 5% in the last 12 months to \$4.53 per square foot for class-A asking rents, \$3.90 per square foot for class-B rents and \$3.04 per square foot for class-C asking rents. Vacancy rates also show significant variation between product quality. Class-A product has the lowest vacancy rate at 3.7%, showing that there is a flight to quality. Class-C spaces, on the other hand, have an 8.1% vacancy rate.

On the investment sales side, capital stuck to the sidelines through the first half of the year as leasing activity gained momentum. Then, in the second half of the year, investment activity surged. In all, investment sales totaled \$606 million in San Diego last year, and assets traded at an average \$387 per square foot, representing record pricing, with a 5.6% average cap rate.

The healthcare industry is shifting toward outpatient care, which is driving much of the leasing demand and bullishness on the sector. This niche has a limited supply and a high barrier to entry for new development. Among the largest transactions, Madison Medical Center traded hands for \$26 million and Sycamore Health Center traded for \$11.3 million.

San Diego's medical office success story isn't a new one. The market has been **gaining momentum** since the beginning of the pandemic, after a brief pause for uncertainty. Medical office rents were also up more than 5% in 2020, according to an earlier report from JLL. The research suggested that two main factors were driving the rent increase. The biggest is simple supply-and-demand imbalance as due to low vacancy, particularly for quality space. Rising construction costs is the second. There is currently only 97,177 square feet of medical office space under construction, half of the construction pipeline at the end of 2020.

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