

Savills Studley Report Silicon Valley office sector

Q3 2018



SUMMARY

Market Highlights

LEASING STEADY

Deal volume exceeded 2.6 million square feet (msf), as larger leases continued to boost volume. Tenants have leased 7.9 msf in the four most recent quarters.

AVAILABILITY PUSHES LOWER

The region's overall availability rate continued its sharp decline, falling by 170 basis points to 14.1%. The Class A availability rate dropped by 330 basis points to 16.3%, its lowest mark since 1Q 16. Availability remains negligible in Menlo Park, Palo Alto and Sunnyvale/Cupertino with single-digit availability in these core locations.

RENTAL RATE DECLINES

Regional overall asking rent fell by 3.8% to \$49.01 (\$4.08 monthly) during the third quarter. Class A rent dipped by 1.5% to \$51.74 (\$4.31 monthly), but has jumped by 2.0% year on year.

SALES DROP

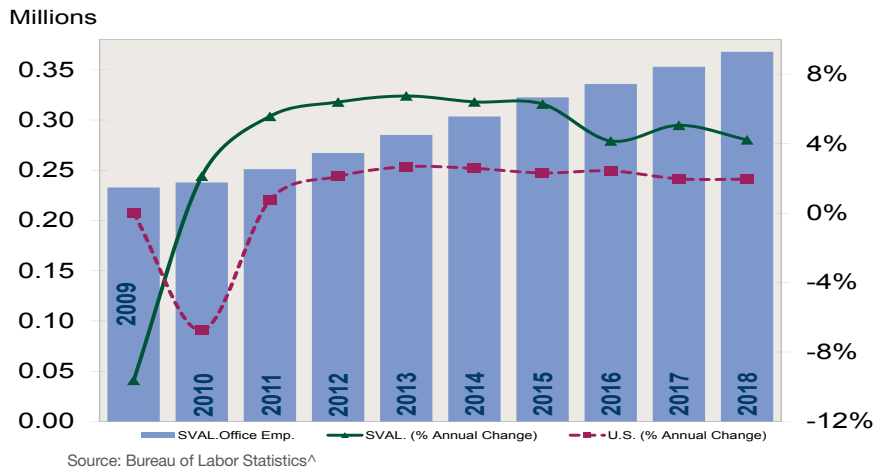
Office property sales during the first seven months of the year totaled \$1.7 billion, a 28.6% decrease compared to the first seven months of 2017.

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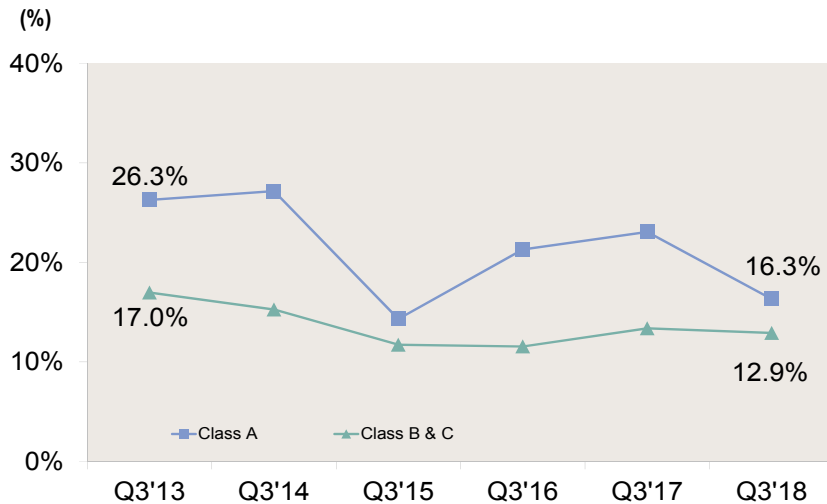
"The Valley's steady streak of major leases continued in the third quarter as new developments such as Coleman Highline and Santana Row captured additional activity from major tenants. Even as larger firms boost activity the flow of smaller businesses out of the market is a growing concern."

Nathan Currie,
Corporate Managing Director
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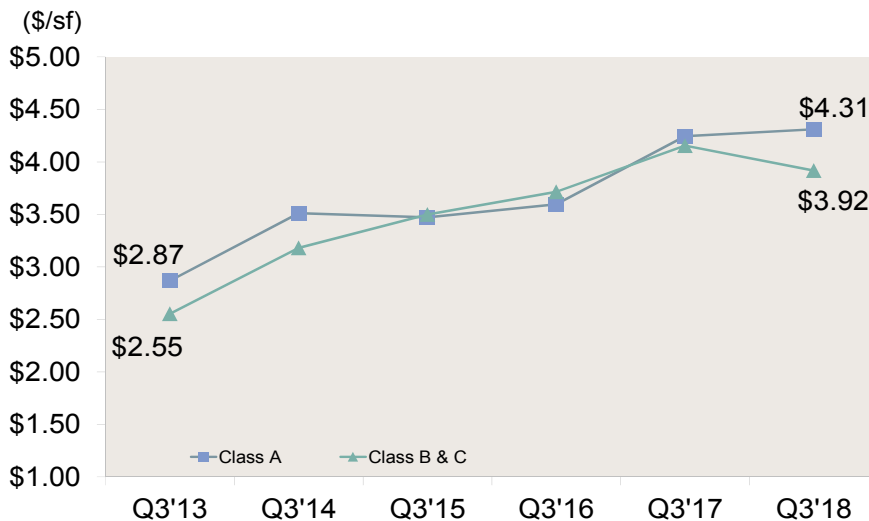
Office-Using Employment Trends



Vacant Availability Rate Trends



Asking Rent Trends



Life Beyond the Valley

A recent cover article in the Economist contends that the Valley has lost its status as the mecca for startups. Companies come and go in every cycle in the Valley. This article makes a stronger claim – saying in effect that is no longer a simple case of life after the Valley – more and more companies are starting life outside of the innovation cradle. Some are choosing to avoid the costs, the competition and the headaches of the Valley, rejecting the longheld notion that the Valley's deep talent pool, access to capital and synergy are unmatched. The article also suggests that other markets may be a better nursery – more hospitable to the experimentation and innovation that was once the Valley's trademark. Tech heavyweights, it is argued, have a kill zone – they acquire and sometimes stifle innovators and potential competitors.

Venture capital funding and employment seem to suggest otherwise. According to the PwC/Moneytree Report, venture capital funding jumped by 24% to \$4.8 billion in the third quarter. Hiring in office-using sectors is still rolling along at a 4% annual rate, more than twice the national average.

San Jose Rally Rolls On

For the time being, the Valley has more than enough significant leases to mask the negative impact of company displacement. North San Jose has been on a winning streak of late. Roku recently signed a 472,000-sf lease in the Coleman Highline office and retail complex in North San Jose. The manufacturer of digital media players will move from about 200,000 sf in Los Gatos to four different buildings at the park, leaving it with about 700,000 sf remaining. The transit-oriented project will have 1.5 msf of office space in eight buildings, 1,600 apartments, a hotel and retail space. Earlier this year 8x8 took 162,000 sf in the new park. In addition to the leases by Roku and 8x8 – Bloom Energy, Hewlett Packard Enterprise and Micron Technology all recently moved operations to San Jose.

Additionally, San Francisco-based Splunk announced that it will pre-lease the entire 301,000 sf at 700 Santana Row in San Jose/ West Valley, adding to the 234,000 sf they already lease at 500 Santana. The latest building is scheduled to be completed in 2019, but some floors can be occupied this fall. Splunk's big splash may push the owner, Federal Realty, to expedite development plans for Santana West. The proposed 1.0-msf development would

replace the Century 21 Theater across the street from 500 Santana.

Area firms remain aggressive in their pursuit of new properties. As the third quarter was ending, Nokia announce that it will lease the entirety of 520 Almanor Ave in the Peery Park district. The 231,000-sf building in Sunnyvale is scheduled to deliver in 2020.

Coworking Options Expand

Startups deciding to stay in the Valley now have an alternative to traditional office space. They can set up shop in the proliferating coworking space sector. In late June, WeWork announced a lease for its second location in Downtown San Jose, adding 70,926 sf at 75 E. Santa Clara Street (333 W. San Carlos Street). Additionally, in Mountain View, WeWork is preparing to open a 450,000-sf development called The Village at San Antonio Center. Top tenants are crowding into coworking as well, though. Facebook grabbed the entire new complex.

Investors Target San Jose

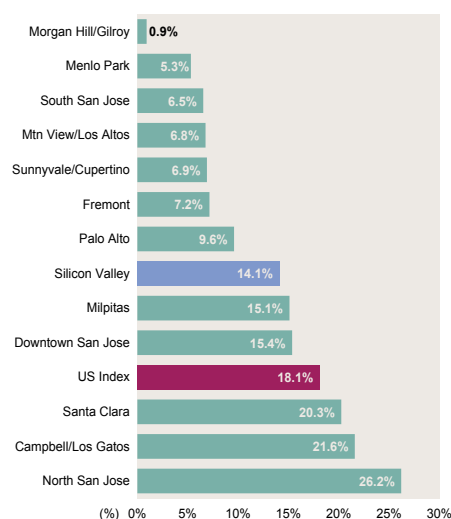
North San Jose has also drawn the attention of investors. PSAI Realty Partners recently paid \$91.5 million (\$302/sf) for Gold Street Technology Campus, Tivo's five-building 302,600-sf campus. A year ago, Tivo renewed its lease at the complex. In June, several investors teamed up to acquire eBay's campus, also in North San Jose – paying \$132.5 million (\$530/sf) for the 250,000-sf campus.

Of note, in Downtown San Jose, Jay Paul has been highly active. In August, the developer bought the former JC Penney building for \$46 million, paying \$383/sf for the 120,000-sf property. The seller, Lift Partners acquired the property for \$17.6 million in 2016 and had arranged financing of nearly \$40 million for renovations. Earlier in the summer, Jay Paul paid \$283.5 million for Cityview Plaza. The 580,000-sf mixed-use complex includes 535,000 sf of office space, 45,000 sf of retail and more than 1,000 parking stalls.

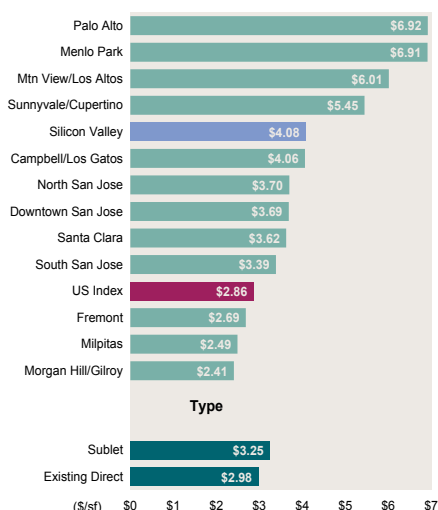
IPO Rebound

Rumors of the death of the IPO market appear to have been greatly exaggerated. Between 2015 and 2017, concerns about overvaluation suppressed tech IPOs. They have finally improved in 2018, evidenced by the aforementioned increase in venture capital activity. Successful IPO fundraising

Availability Rate Comparison



Rental Rate Comparison



Major Transactions

Tenant	Sq Feet	Address	Market Area
Roku	472,000	1173, 1167 & 1155 Coleman Ave	North San Jose
Splunk	301,000	700 Santana Row	Santa Clara
Nokia	231,000	520 Almanor Ave	Sunnyvale/Cupertino
Verb Surgical	227,618	5490 Great America Pky	Santa Clara
Facebook	120,573	6520-6532 Kaiser Dr	Fremont (880 Corridor)
Facebook	103,472	34800 Campus Dr	Fremont (880 Corridor)
NIO	99,000	3100 N 1st St	North San Jose
Amazon Web Services	75,378	20400 Stevens Creek Blvd	Sunnyvale/Cupertino
WeWork	70,926	333 W San Carlos St	Downtown San Jose
Singularity	35,067	395 Page Mill Rd	Palo Alto

is supporting payroll expansion and leasing activity. NIO USA leased the entirety of 3100 N. First Street in North San Jose. The Chinese-based maker of electric vehicles already leases nearby 3200 N. First Street. It quickly grabbed the 99,000-sf building after Broadcom vacated the property. NIO USA (one of the many competitors testings autonomous electric vehicles in California) has started a closed initial IPO with a goal of raising \$2 billion.

Arlo Technologies is about to move to 77,882 sf at 3030 Orchard Parkway. The security camera business, a spinoff of Netgear, has about 150 employees. Arlo Technologies raised about \$163 million in its recent IPO. Most of its comes from home security cameras that are integrated with voice assistants from Amazon or Google.

Looking Forward

It is an open question whether Silicon

Valley's status as the sine qua non for startups is slipping. IPOs and venture capital funding certainly still put the Valley on top. The movement of companies to other markets, or choice by some to not start in the Valley to begin with, is arguably the price of success. Additionally, downturns have a way of spurring entrepreneurial activity. Once the dust settles, the Valley suddenly becomes the land of opportunity again.

For now there are no imminent signs of a slowdown; however, the bull run market for the big five FAANG stocks has certainly seen its fair share of volatility. Uncertainty still looms large. Fortunately, Apple products were not included on the latest round of tariffs the Trump Administration imposed on China. The rise of government regulation for issues such as privacy, censorship and monopoly is already a reality in China and Europe and remains an x-factor in the U.S. as well.

Map	Submarket	Total	Leasing Activity		Available SF		Availability Rate			Asking Rents Per SF		
		SF (1000's)	Last 12 Months	This Quarter	% Change from Last Qtr.	Year Ago	This Quarter	pp Change from Last Qtr. ⁽¹⁾	Year Ago	This Quarter	% Change from Last Qtr.	Year Ago
1	Campbell/Los Gatos	3,359	121	725	-0.6%	457	21.6%	-0.1%	13.6%	\$4.06	1.9%	\$3.69
	Campbell/Los Gatos - Class A	1,009	42	244	-7.5%	203	24.2%	-2.0%	20.2%	\$4.66	3.8%	\$3.96
2	Downtown San Jose	8,708	496	1,339	-17.8%	1,454	15.4%	-3.3%	16.7%	\$3.69	1.1%	\$3.53
	Downtown San Jose - Class A	3,590	218	603	-16.4%	592	16.8%	-3.3%	16.5%	\$4.07	-0.3%	\$3.82
3	Milpitas	2,778	70	420	3.3%	597	15.1%	0.5%	21.5%	\$2.49	-0.4%	\$2.48
	Milpitas - Class A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
4	Morgan Hill/Gilroy	723	5	7	11.3%	8	0.9%	0.1%	1.1%	\$2.41	3.2%	\$2.03
	Morgan Hill/Gilroy - Class A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	\$0.00	N/A	\$0.00
5	Mountain View/Los Altos	7,583	1,166	514	-7.1%	993	6.8%	-0.5%	13.1%	\$6.01	-1.4%	\$6.45
	Mountain View/Los Altos - Class A	1,232	2	193	-6.6%	173	15.7%	-1.1%	14.0%	\$6.56	1.5%	\$5.98
6	North San Jose	12,786	2,431	3,351	-9.1%	3,658	26.2%	-2.6%	28.6%	\$3.70	-6.2%	\$3.46
	North San Jose - Class A	5,613	1,445	1,632	-11.5%	1,777	29.1%	-3.8%	31.7%	\$3.67	-6.1%	\$3.53
7	Palo Alto	6,643	468	627	-16.0%	558	9.4%	-1.8%	8.4%	\$6.92	-0.6%	\$7.07
	Palo Alto - Class A	273	117	N/A	-1.9%	78	17.6%	-0.3%	28.6%	\$7.95	0.0%	\$0.00
8	Santa Clara	14,870	1,258	3,012	-2.2%	4,132	20.3%	-0.5%	27.8%	\$3.62	-6.0%	\$3.88
	Santa Clara - Class A	7,000	794	1,578	-16.4%	3,020	22.6%	-4.4%	43.1%	\$4.14	-0.6%	\$4.47
9	South San Jose	4,184	596	274	-51.1%	487	6.5%	-6.8%	11.6%	\$3.39	-15.4%	\$4.39
	South San Jose - Class A	844	394	25	-92.1%	389	3.0%	-34.6%	46.1%	N/A	N/A	\$5.17
10	Sunnyvale/Cupertino	13,972	610	966	-3.9%	868	6.9%	-0.3%	6.2%	\$5.45	-0.4%	\$4.66
	Sunnyvale/Cupertino - Class A	8,009	414	357	-0.9%	426	4.5%	0.0%	5.3%	\$5.99	-4.4%	\$5.15
11	Menlo Park	5,005	260	266	-41.1%	411	5.3%	-3.7%	8.2%	\$6.91	-0.2%	\$7.91
	Menlo Park - Class A	1,502	128	65	13.2%	45	4.4%	0.5%	3.0%	\$7.54	-36.0%	\$8.66
12	Fremont	2,009	406	144	-32.5%	242	7.2%	-3.5%	12.0%	\$2.69	-1.0%	\$2.15
	Fremont - Class A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
1-12	Silicon Valley Total	82,620	7,890	11,645	-10.9%	13,864	14.1%	-1.7%	16.8%	\$4.08	-3.8%	\$4.19
	Silicon Valley Total - Class A	29,071	3,554	4,745	-16.8%	6,703	16.3%	-3.3%	23.1%	\$4.31	-1.5%	\$4.25

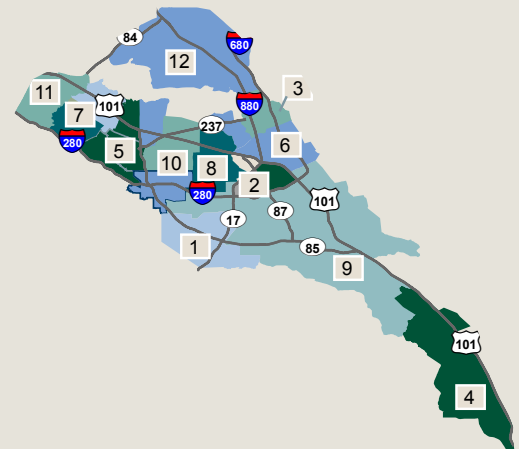
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(1) Percentage point change for availability rates.
Unless otherwise noted, all rents quoted throughout this report are average asking gross (full service) rents psf.
Statistics are calculated using both direct and sublease information.
Short-term sublet spaces (terms under two years) were excluded.
^Unless otherwise noted, source for data is Savills Studley.
The information in this report is obtained from sources deemed reliable, but no representation is made as to the accuracy thereof. Statistics compiled with the support of The CoStar Group.
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