

Q1
2007

TRI Commercial SAN FRANCISCO TRENDS



OFFICE MARKET REPORT

1st Quarter 2007

San Francisco Market Overview

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MARKET OVERVIEW

The San Francisco commercial real estate market is currently evolving from a recovery stage to an impressive growth market. In this economic rebound, an increase of employment opportunities, combined with growth in the technology sector, are driving rental rates into an upbeat performance for the office leasing market. Vacancy rates fell to a record low of 10.2%, the lowest since 2000, and office rental rates climbed 12% this quarter. The market is tightening as existing tenant expansions and renewals continue to be the majority of the leasing activity. UBS and Sephora both recently expanded and renewed about 50,000 square feet of space each.

Major commercial real estate investors account for another rationale for the tightening of the San Francisco rental market. In February, a record-high ten buildings located in the Financial District were sold to Morgan Stanley by the Blackstone Group LP, for \$2.5 billion. Property owners expect a greater return from these purchases as tenant demand becomes stronger. Without imminent delivery of new construction, property owners are taking advantage of strong tenant demand to push up their rents. On average, San Francisco citywide asking rental rates for Class A space are \$40.72 per square foot. Class B space average asking rates increased to \$28.89 per square foot.

With an estimated 300+ technology companies occupying more than three million square feet of space in San Francisco since 2004, the technology sector once again exerts itself as the primary driver to the resurgence of South of Market (SOMA). Rental rates have increased 18% since 2003, climbing to 1999 levels. With SOMA being one of the fastest growing submarkets, Class A average rent in this submarket is currently at \$33.00 and Class B rents are at \$25.00. Furthermore, Mission Bay is also becoming an office market hot spot for biotechnology companies. Some of the major biotech firms have already expanded into the city: FibroGen leased 450,000 square feet at 409 Illinois Street and Sirna Therapeutics leased an estimated 70,000 square feet at 1700 Owens Street. Also, other tenants like Versant Ventures, Arch Venture Partners and Novo Ventures are also planning to move into the neighborhood on Owens Street.

CBD OFFICE LEASING MARKET

Class A space in the Central Business District continues to account for the majority of leasing activity. The average asking rental rate for Class A space rose to the low \$40's per square foot, a 4% increase from December of last year. Many tenants are renewing and expanding their existing view space leases. Asking rents for the upper floors of the Class A trophy buildings now range from \$75-79 per square foot, reflecting similar rent numbers achieved in the same buildings during the dot com boom in 2000.

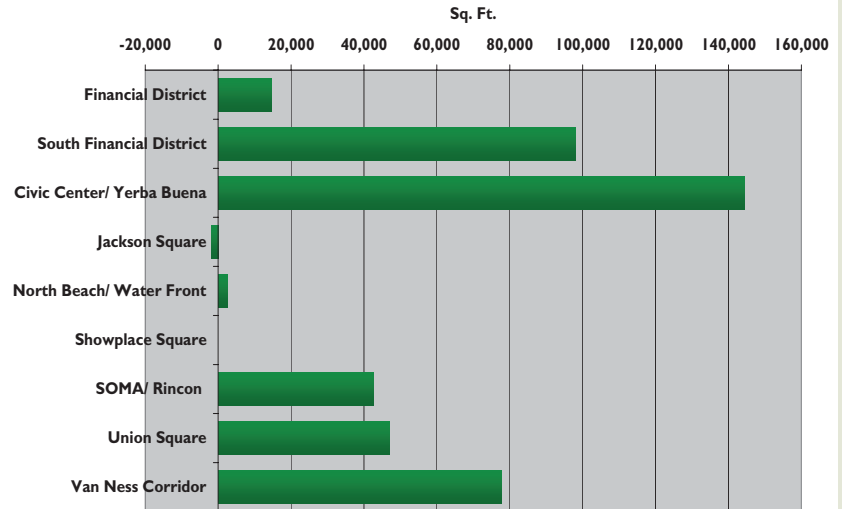
Throughout the city, large blocks of space are becoming more scarce due to existing tenants securing their lease deals with expansions and renewals in this rapidly

growing market. Some notable lease deals in San Francisco were: UBS, with a total of 50,000 square feet, renewing at \$78 per square foot on 555 California Street; Sephora, expanding into 50,186 square feet on the second and third floors of 425 Market Street at \$36 per square foot; and Babcock & Brown signed a 12 year lease of 155,000 square feet at the Presidio Building on 1 Letterman Drive. The irony is that despite all these indications of a very tight market, the vacancy rate in the North Financial District showed a slight increase to 10.1% from 9.7% last

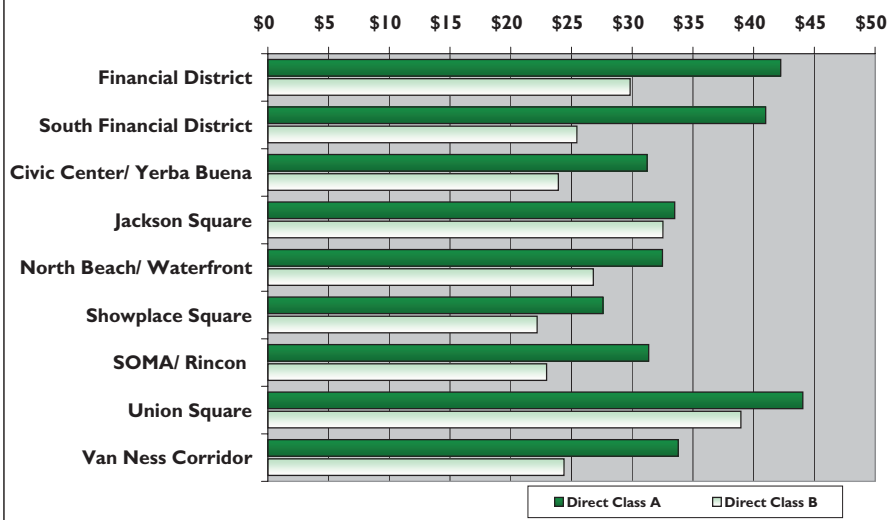
quarter 2006 without any construction delivery.

The continuing rise in rents and increased demand is producing a surge in new office construction. A new 33 story office tower, with an estimated 555,000 square feet on 555 Mission Street, is expected to be delivered in August of 2008. It will be the first 'spec' construction office building since the dot-com crash. Also, 370 Third Street, a Class C office building of 419,263 square feet is currently under renovation and is expected to be delivered in January of 2008.

CLASS A QUARTERLY ABSORPTION RATE BY SUBMARKET



1Q2007 RENTAL RATE BY SUBMARKET



San Francisco Lease and Sale Transactions

Major Lease Transactions 1Q2007

Tenant	Address	Class	Submarket	Sq. ft.
Google Inc.	345 Spear Street	A	Rincon/ South Beach	210,000
Babcock & Brown	One Letterman Drive	A	Waterfront/ North Beach	155,000
Pay By Touch	560 Mission Street	A	South Financial	92,936
Farallon Captial	One Maritime Plaza	A	North Financial	63,250
California Pacific Medical Center	475 Brannan Street	B	SOMA	61,831
Sephora	425 Market Street	A	South Financial	50,000
UBS	555 California Street	A	North Financial	50,000

Recent Sale Transactions

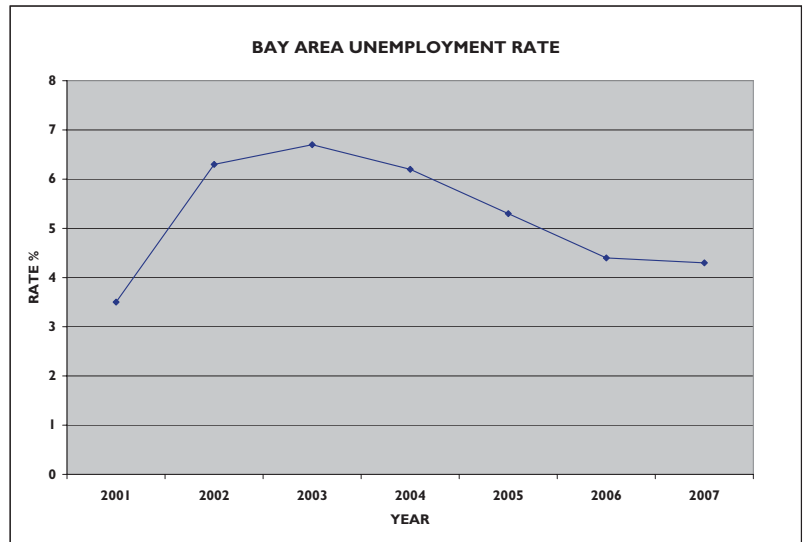
Address	Submarket	Square Feet	Sales Price	Price/ Sq.Ft
160 Spear Street	South Financial District	288,309	\$86,000,000	\$298
625 2nd Street	Rincon/ South Beach	134,847	\$51,000,000	\$378
250 Montgomery Street	Financial District	116,078	\$47,000,000	\$405
180 Montgomery Street	Financial District	299,351	\$128,000,000	\$428
425 Market Street	South Financial District	996,760	\$260,000,000	\$433
600 California Street	Financial District	363,000	\$158,000,000	\$435
1 Sansome Street	Financial District	550,000	\$276,100,000	\$502
1 Market Street (Steuart Tower)	South Financial District	490,726	\$2,600,000,000	\$675*
1 Market Street (Spear Tower)	South Financial District	883,778	\$2,600,000,000	\$675*
201 California Street	Financial District	240,546	\$2,600,000,000	\$675*
580 California Street	Financial District	313,012	\$2,600,000,000	\$675*
1 Maritime Plaza	Financial District	534,874	\$2,600,000,000	\$675*
201 Mission Street	South Financial District	483,289	\$2,600,000,000	\$675*
1 Post Street	Financial District	421,121	\$2,600,000,000	\$675*
60 Spear Street	South Financial District	133,782	\$2,600,000,000	\$675*
188 Embarcadero	South Financial District	85,432	\$2,600,000,000	\$675*
150 California Street	Financial District	201,787	\$2,600,000,000	\$675*

* \$675 Per square foot represents an average purchase price by Morgan Stanley from Blackstone Group.

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INVESTMENT MARKET ANALYSIS

San Francisco office sales initiated a sizzling hot year with purchases in record high volume and at record high prices. In February, the Blackstone Group LP acquisition of more than 500 EOP properties nationwide, for \$39 billion, made headlines. Morgan Stanley then bought 10 of the properties from Blackstone Group LP for \$2.5 billion, at an average \$675 per square foot. Brokers who represent tenants are understandably concerned with new landlords attempting to raise rents in order to compensate for the high purchase prices. For existing tenants, base rental rates are not immediately impacted by recent sales. However, those same tenants may not be protected against significant property tax increases resulting from transfer of ownership.

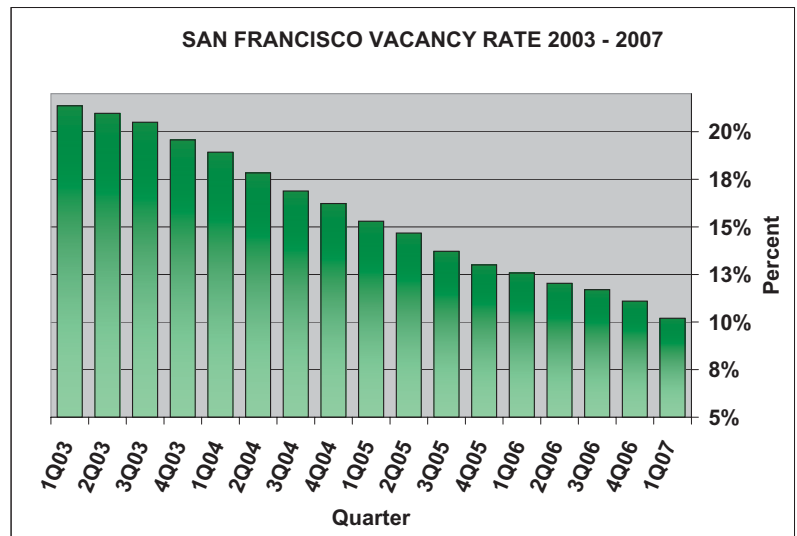


In addition to the Blackstone Group LP/ Morgan Stanley transaction, other major sales this quarter include the Legacy Partner's purchase of 160 Spear Street for \$86 million (\$298.29 per square foot) and 581 Market Street, a four story retail building sold for \$11 million (\$426.76 per square foot) to Redwood Real Estate Partners LLC. The BofA tower at 555 California Street is also changing hands from Hudson Waterfront Associates to Vornado Realty Trust as part of a two property portfolio sale for \$1.8 billion, at approximately \$575 per square foot for 555 California Street.

2Q 2007 OFFICE LEASING FORECAST

Demand for prime view space remains strong. Due to the increase of employment opportunities, approximately more than 20 companies are still looking for work spaces of up to 50,000 square feet in today's market. With minimal supply delivery, the vacancy rates will continue to decline throughout the quarter.

The rising office rental rate market is driven by a combination of the high price per square foot that many buildings have recently traded for, low vacancy rates, and a lack of significant new construction and inventory. As a result, market fundamentals will remain positive for landlords in 2007. Tenants are feeling pressure to anchor their current location or renew their lease terms before rental rates rise even higher if they delay. Will San Francisco's prime view space rental rate reach \$100 per square foot, like New York City did last year? Overall, that is a possibility if demand remains strong throughout the quarter with little or no construction delivery.



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