

Q2  
2008

# TRI Commercial SAN FRANCISCO TRENDS

## OFFICE MARKET REPORT

2nd Quarter 2008

### San Francisco Market Overview

#### OFFICES

**San Francisco**  
415.268.2200

**Oakland**  
510.622.8400

**Walnut Creek**  
925.296.3300

**Sacramento**  
916.669.4500

**Roseville**  
916.677.8000

#### Produced by:

**Kitty Lam**  
Market Research

**Tom Martindale, SIOR**  
Senior Vice President &  
Regional Manager

**Linda Mansberger**  
Marketing

**TRI Commercial**  
One California Street  
Suite 200  
San Francisco, CA 94111

#### MARKET OVERVIEW

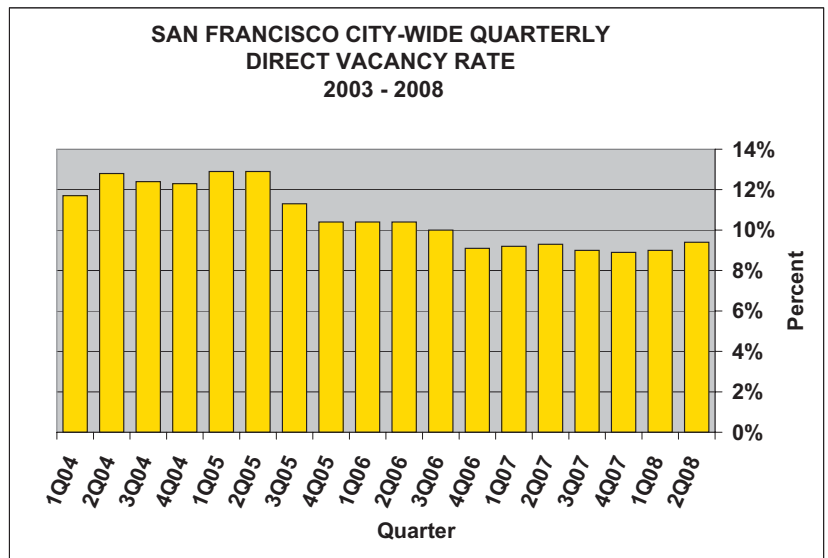
Office leasing activity has slowed considerably and there has been a slight decline in rental rates. The decline in rental rates is attributed to those buildings which traded hands in the last three years and failed to gain their “pro forma” rents on which they were purchased. Those buildings are now beginning to lower their rates in order to attract tenants. Rates will also tend to be down slightly as landlords attempt to secure long term tenants in a market where the future holds much uncertainty and most tenants are only looking at short term solutions to their office space needs.

Shrinkage in the financial services sector has opened up more space for subleases and short term renewals. These spaces are providing more selection to the companies who are anticipating a weaker economy ahead as they consolidate office space and hold off on expansions. Companies who recently filed for bankruptcy, like Sharper Image Corp., Red Envelope Inc. and Pay-by-Touch, are placing sublease spaces in the market. A total of over 500,000 square feet of sublease space is currently available in the downtown financial district.

Despite the slow economy caused by the subprime financial market, the technology and biotechnology sectors continue their rapid growth in San Francisco and, as a result, a healthy demand for space continues in these sectors. The City’s office leasing activity is benefiting from Silicon Valley tech firms such as Google, Facebook and Microsoft, who are taking an interest in office space in San Francisco to accommodate their younger employees that are attracted to the City’s urban living style. The current office vacancy rate is at a strong 9.4 percent, in comparison to the national rate at 11.4 percent.

**SF Citywide Quarterly Direct Vacancy Rate**

Quarter	Vacancy Rate	Quarter	Vacancy Rate
<b>2Q08</b>	<b>9.4%</b>	1Q06	10.4%
1Q08	9.0%	4Q05	10.4%
4Q07	8.9%	3Q05	11.3%
3Q07	9.0%	2Q05	12.9%
2Q07	9.3%	1Q05	12.9%
1Q07	9.2%	4Q04	12.3%
4Q06	9.1%	3Q04	12.4%
3Q06	10.0%	2Q04	12.8%
2Q06	10.4%	1Q04	11.7%



\*Submarket included: Bayview/Hunters Point, Chinatown/Nob Hill, Civic Center, Financial District, India Basin, Jackson Square, Lower South of Market, Mission Bay/China Basin, Potrero East of I01, Potrero West of I01, Rincon/South Beach, Showplace Square, South Financial District, South of Market, Southern City, Union Square, Van Ness Corridor, Waterfront/North Beach, West of Van Ness, Yerba Buena

**Major Lease Transactions**

Tenant	Address	Class	Submarket	Sq. ft.
McCann Erickson	600 Battery Street	B	Jackson Square	112,208
Loopnet	185 Berry Street	A	Mission Bay/China Basin	46,126
Comcast Spotlight	50 Francisco Street	B	Waterfront/North Beach	33,310
Quantcast	201 Third Street	B	Yerba Buena	26,355
SimplyShe	149 New Montgomery Street	B	South Financial District	24,000
Liberty Mutual Insurance*	71 Stevenson Street	A	South Financial District	23,242
Next Internet	153 Kearny Street	B	Union Square	20,342
Meraki	99 Rhode Island	B	Showplace Square	20,000
Jawbone	99 Rhode Island	B	Showplace Square	20,000
Atlas (Microsoft Co.)	225 Bush Street	B	Financial District	19,754
HOK	1 Bush Street	A	Financial District	17,044
Clyde & Company	101 2nd Street	A	South Financial District	15,290
Clickability^	300 California Street	B	Financial District	15,246
WRNS Studios LLP	501 2nd Street	B	Rincon/South Beach	12,354
Steyer Lowenthal"	1 California Street	A	Financial District	9,800

"Tenant Represented by TRI Commercial

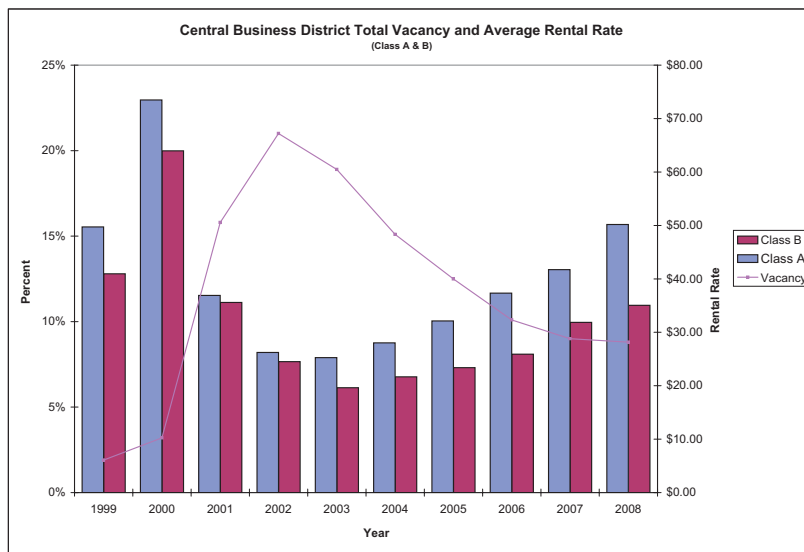
\*Landlord Represented by TRI Commercial

^Sublease

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**CBD Total Vacancy and Average Rental Rate**

Year	Total Avg. Class A	Total Avg. Class B	Direct Vacancy
2008	\$50.19	\$35.04	8.8%
2007	\$41.74	\$31.86	9.0%
2006	\$37.33	\$25.91	10.1%
2005	\$32.14	\$23.38	12.5%
2004	\$28.02	\$21.68	15.1%
2003	\$25.27	\$19.64	18.9%
2002	\$26.22	\$24.51	21.0%
2001	\$36.89	\$35.59	15.8%
2000	\$73.49	\$63.95	3.2%
1999	\$49.71	\$40.96	1.9%



**Submarket Statistics Table**

Submarket	Net Rentable Area (Class A&B)	Total Vacancy (Class A&B)	Net Absorption (Class A&B)	Asking Rent* Class A	Asking Rent* Class B
Financial District	28,074,055	9.5%	(10,205)	\$50.27	\$36.33
South Financial District	24,787,137	8.1%	(213)	\$50.11	\$33.75
Civic Center/ Van Ness	4,700,868	5.2%	8,389	\$33.71	\$18.81
Waterfront/North Beach	3,821,406	6.0%	(1,633)	\$44.45	\$33.91
South of Market	5,089,827	19.1%	(137,966)	\$34.33	\$33.92
Union Square	4,458,568	5.3%	23,663	\$42.58	\$33.33
<b>Total Office Market</b>	<b>70,931,861</b>		<b>(117,965)</b>	<b>\$42.58</b>	<b>\$31.68</b>

**CBD OFFICE LEASING MARKET**

Activity in San Francisco stays flat with a negative 117,965 square feet of absorption this quarter. Central Business District vacancy rates are relatively stable at 8.8 percent, and the average CBD asking rental rate remains in the low \$50's. With a wave of job cuts and layoffs in the financial service industries, such as brokerage firms, mortgage companies, banks, etc., we are now starting to see more sublease space coming onto the market.

Although the Class A office building lease rates are settling, they are still above what Class B and Class C buildings are renting for. Some of the Class B tenants can afford the Class A subleases that are coming to the market. The leasing market should remain steady for the next two quarters; vacancy rates could increase slightly from the upcoming space availabilities at buildings like 500 Terry Francois Blvd., One Kearny St. and 555 Mission St.

## INVESTMENT MARKET ANALYSIS

The investment market has been fairly quiet throughout the year thus far; punctuated by a significant decrease in office building investment compared to the same time last year. Over 11,000,000 square feet of office space, comprised of more than thirty major office buildings, was sold at this point last year. This year less than 400,000 square feet of office space has been sold through this quarter, in three major office buildings. A more difficult financing environment is the reason for a decreased volume in sale transactions. Buyers are on the sidelines expecting a slow economy, waiting for a gradual cooling of the real estate market to bring down sale prices before jumping back in.

Significant recent transactions are: CB Richard Ellis purchased 500 Terry Francois Boulevard, a Class A, 291,000 square feet office building in June, for \$149 million. Sansome and Pacific Investments, LLC, purchased 755 Sansome Street, a Class B, 55,243 square feet office building, in April for \$17.5 million. In addition, One Sansome Street is expected to close in August; it will be the biggest sale of the year thus far. Mirae Asset Maps Investment, a unit of South Korea's biggest mutual fund sponsor, is expected to purchase this \$370 million (\$567/sq.ft.), 43 story, 652,000 square feet Class A office building.

**Recent Major Sale Transactions**

Address	Submarket	Square Feet	Sales Price	Price/ Sq.Ft	Class
500 Terry Francois Boulevard	Mission Bay/China Basin	291,129	\$149,000,000	\$512	A
117 Post Street	Union Square	18,246	\$18,800,000	\$1,030	Retail
755 Sansome Street	Jackson Square	55,243	\$17,500,000	\$317	B

## 3Q 2008 COMMERCIAL REAL ESTATE FORECAST

Investment and leasing activity is expected to continue its cooling effect throughout the next two quarters, as the nation continues to show signs of a slower economy. The national unemployment rate is currently at 5.5 percent, a slight increase from this time last year at 4.5 percent. The San Francisco unemployment rate is currently at 4.8 percent, a 0.2 percent decrease from last month. Due to the slowdown in home development, there is much less demand for contractors and construction workers related to residential development. There are also mortgage businesses failing, hedge fund closures, and companies consolidating, so the unemployment rates may continue to rise. The positive side is that technology and biotechnology sectors continue to grow strongly in San Francisco, and demand for those spaces stays strong. San Francisco is similar to the Silicon Valley in relation to the strong performance of the larger technology firms, and that is making up for the sluggish job growth overall.

The information above is believed reliable. While we do not doubt its accuracy, we make no guarantee, warranty or representation about it.