

Q3
2007

TRI Commercial SAN FRANCISCO TRENDS

OFFICE MARKET REPORT

3rd Quarter 2007

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

San Francisco's office leasing market continued to tighten in the third quarter, despite the current liquidity crisis rippling through financial markets and the customary softness in business activity associated with summer months.

The citywide total vacancy rate declined from 9.9 percent at the end of the second quarter to its current 9.2 percent. At the end of the third quarter a year ago, the vacancy rate for office space was 11.7 percent. The average asking rental rate for Class A space, citywide, rose to \$43.69 per-square-foot from \$41.19 per-square-foot; Class B space rose to \$31.95 per-square-foot from \$29.93 per-square-foot. For prime view space in the premium Class A trophy properties, asking rates continue to be as high as \$100 per-square-foot.

One of the higher-priced lease transactions, since the dot-com era, closed this quarter when financial news services provider Bloomberg LP acquired 30,000 square feet of space at Piers 1½, 3, and 5 for \$100 per-square-foot, on a fully serviced basis. Numerous major lease transactions of 10,000 square feet and larger were completed this quarter, with absorption totaling more than 300,000 square feet. Regus/HQ Workplaces and Bovis Lend Lease both inked more than 29,014 square feet at 71 Stevenson Street. Visa USA recently renewed their lease for 42,861 square feet at 123 Mission Street. Vontu Inc. and Bebo Inc. will be occupying more than 30,000 square feet of space each at separate locations – Vontu is moving to 475 Sansome Street and Bebo is moving to 795 Folsom Street.

In the investment sector, severe turmoil in debt markets has slowed, but not stopped, the red-hot market of buying and selling commercial property. From July through mid-September this year, six buildings in the Central Business District traded hands and all but one of the transactions were valued below \$500 per square foot. By comparison, during the second quarter of 2007, and before the crumbling residential mortgage industry affected global liquidity markets, more than ten buildings were sold -- five of which traded for more than \$500 per square foot.

Significant recent transactions: Ashforth Pacific Properties purchased 405 Howard Street in July for \$247 million, a Class A, 502,424-square-foot office building; and Kennedy Wilson purchased 300 California Street in August for \$50 million, a Class B, 120,000-square-foot office building.

Recent Sale Transactions

Address	Submarket	Square Feet	Sales Price	Price/ Sq.Ft	Class
1 Market Street [^]	South Financial District	1,500,000	\$720,000,000	\$960	A
405 Howard Street	Rincon/South Beach	503,576	\$247,000,000	\$490	A
114 Sansome Street	Financial District	180,000	\$67,000,000	\$372	B
444 De Haro Street [*]	Showplace Square	140,178	\$38,000,000	\$249	B
300 California Street	Financial District	120,000	\$50,000,000	\$400	B
600 Townsend Street	Showplace Square	64,214	\$26,100,000	\$406	B
654-660 Market Street	Financial District	42,000	\$19,000,000	\$452	B

^{*}Apollo Real Estate Advisors, L.P. Portfolio Sale

[^]Paramount Group Inc. Portfolio Sale (Structures include: Spear Tower, Steuart Tower, 75 Howard St: Parking Garage) 50% interest

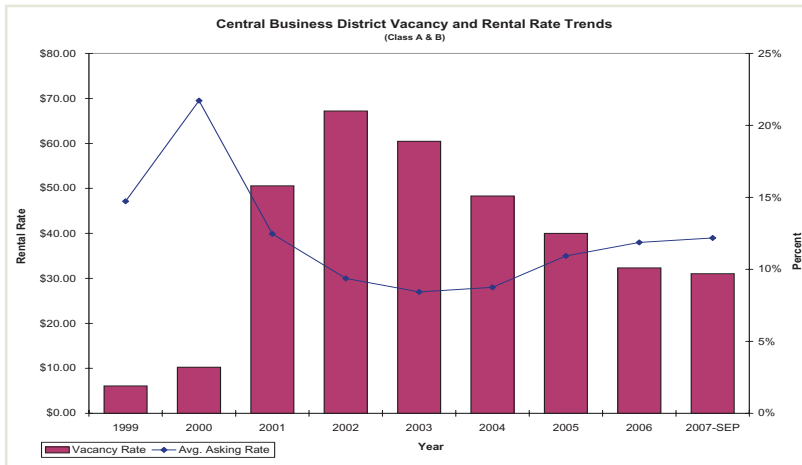
“One of the most expensive lease transactions since the dot-com era closed this quarter.”

Major Lease Transactions

Tenant	Address	Class	Submarket	Sq. ft.
Visa USA	123 Mission Street	A	South Financial District	42,861
Vontu Inc.	475 Sansome Street	A	Financial District	33,000
Bebo Inc.	795 Folsom Street	B	Yerba Buena	31,600
Bloomberg LP	Piers 1½, 3, and 5	A	Jackson Square	30,000
Regus / HQ Workplaces [*]	71 Stevenson Street	A	South Financial District	18,196
Artist Capital Management	1 Market Street	A	South Financial District	18,000
Readisuite LLC	647 Mission Street	C	South Financial District	17,820
Success Factors	655 Montgomery Street	A	Financial District	16,974
Carlton DiSante & Freudenberger	601 Montgomery Street	A	Financial District	16,974
Bargen Coffin Lewis & Trapp	350 California street	A	Financial District	14,165
Intuit [*]	71 Stevenson Street	A	South Financial District	14,094
Tucker Ellis & West LLP	135 Main Street	A	South Financial District	13,260
Pearl Law Group	315 Montgomery Street	B	Financial District	13,173
Judicial Council of California	303 2nd Street	A	Rincon / South Beach	11,619
Bovis Lend Lease [*]	71 Stevenson Street	A	South Financial District	10,818

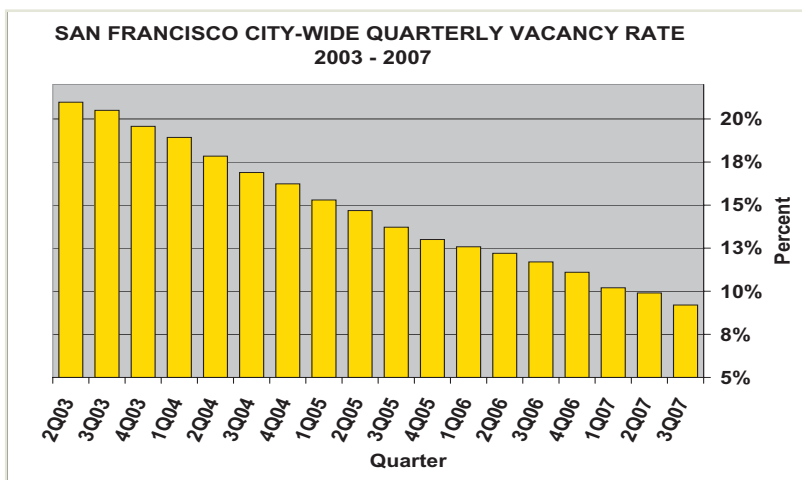
^{*}Landlord Represented by TRI Commercial

With offices in San Francisco, Sacramento, Roseville, Oakland, Walnut Creek, and Santa Rosa, we have access to every major commercial market in Northern California. As a member of CORFAC International, we also provide our clients with national and international coverage.



CBD Vacancy & Rental Rate Trends

Year	Vacancy	Rental Rate
2007-SEP	9.70%	\$38.97
2006	10.10%	\$38.00
2005	12.5%	\$34.97
2004	15.1%	\$28.00
2003	18.9%	\$27.00
2002	21.0%	\$29.99
2001	15.8%	\$39.89
2000	3.2%	\$69.50
1999	1.9%	\$47.14



SF Citywide Quarterly Vacancy Rate 2003 - 2007

Quarter	Vacancy Rate	Quarter	Vacancy Rate
3Q07	9.20%	2Q05	14.68%
2Q07	9.90%	1Q05	15.30%
1Q07	10.20%	4Q04	16.23%
4Q06	11.10%	3Q04	16.89%
3Q06	11.70%	2Q04	17.84%
2Q06	12.20%	1Q04	18.93%
1Q06	12.58%	4Q03	19.57%
4Q05	13.00%	3Q03	20.50%
3Q05	13.72%	2Q03	20.97%

CBD OFFICE LEASING MARKET--A TALE OF TWO MARKETS

Landlords who have recently acquired Class A office buildings in the range of \$500 to \$750 per-square-foot have to ask aggressive lease rates in order to justify the purchase price. In essence, they are trying to “pull” the market significantly higher in a very short period of time. The result is a bifurcated market wherein buildings that have not recently changed hands are asking 20-30 percent less in an effort to attract and retain tenants. We will soon learn whether the new landlords will prevail in “making the market”, or the tenants will seek more value-oriented space elsewhere. Even if the tenant initially succeeds in avoiding the “rent spike” dynamic currently being played-out, they still could end up in a building that is ultimately sold and they could be paying a significant increase in future pass-throughs due to increased taxes. It’s a little like playing “Building Roulette”.

The foregoing notwithstanding, premium space in San Francisco is now near the previous rental “peak” just before the ‘dot-com’ bust in 2001. Two recent transactions are of note: Bloomberg LP signed a 30,000 square feet lease at Pier 1½, 3, and 5 for \$70 NNN with \$30 per-square-foot in operating expense and taxes, and hedge fund Artis Capital Management signed an 18,000 square foot lease on the 27th floor of One Market Street for close to \$100 per-square-foot.

INVESTMENT MARKET ANALYSIS

Turbulence in the sub-prime mortgage market has caused lending requirements to tighten. Given the dynamic situation in financial markets, funding property sales will remain the principal challenge for the investment sector. Furthermore, investors are likely to wait and see if the recent run up in rental rates will affect leasing absorption and property values. Despite current trends; buyers remain active in the market, yet will probably move more cautiously toward making offers than in past months.

“Five significant transactions were completed under \$500 per square foot.”

Over \$1.5 billion worth of investment sales closed this quarter; five significant transactions were completed under \$500 per-square-foot. Morgan Stanley Real Estate sold a 50 percent interest in a Class A building -- One Market Street, to Paramount Group Inc. for \$720 million. The deal includes the Spear Tower, the Stuart Tower and a parking garage at 75 Howard Street. Another significant transaction is 405 Howard Street -- a Class A building that sold for \$24.7 million, an average of \$490 per-square-foot. In addition, buyers and sellers in the Rincon/South Beach submarket traded a total of 503,576 square feet of commercial space in the third quarter.

Submarket Statistics Table

Submarket	Net Rentable Area	Total Vacancy	Net Absorption	Avg. Rent Class A	Avg. Rent Class B
Financial District	30,339,275	10.4%	339,156	\$45.25	\$35.26
South Financial District	25,443,683	8.5%	164,608	\$42.50	\$32.87
Civic Center/ Van Ness	6,492,443	5.1%	(63,251)	\$33.39	\$28.86
Waterfront/North Beach	4,586,941	7.1%	84,662	\$35.55	\$28.34
South of Market	6,353,849	13.1%	(15,045)	\$34.33	\$32.70
Union Square	5,987,145	7.4%	58,310	\$42.56	\$31.25
Yerba Buena	4,844,317	13.1%	80,439	\$41.75	\$34.34
Total Office Market	84,047,653	9.24%	648,879	\$39.33	\$31.95

4Q 2007 COMMERCIAL REAL ESTATE FORECAST

Since 2003, quarterly vacancy rates in San Francisco have declined while average rental rates have marched steadily upward. For the next two quarters, we expect the vacancy rate to decline only slightly and rental rates to remain relatively constant, or increase only marginally. While tenant demand for commercial office space remains strong, recent and significant spikes in asking rental rates (in certain buildings) could slow leasing activity. The regional economy appears to be stronger than other portions of the state and nation, which bodes well for business expansion. Since most of the banks moved out of San Francisco in previous economic cycles, the City should not be adversely affected by the mortgage industry's turmoil. Questions remain about how much demand there will be for some 1.3 million square feet of new office space scheduled for delivery by the third quarter of 2008. It depends on the economy's performance: if we will avoid recession, and enjoy positive job growth.

While San Francisco remains on most property investors' "A" lists, the investment market should be relatively quiet in coming months, or until global financial markets settle down after the sub-prime lending speed bump and resultant market uncertainty.

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