

TRI SAN FRANCISCO TRENDS



OFFICE MARKET REPORT 1st Quarter 2006

San Francisco Market Overview

Landlords clearly possess the stronger hand and tenants are best advised to lock in long-term deals now. Fast rising rental rates, solid leasing activity, and positive yet slackening absorption clearly signal that we are in a tight market – with all indications that vacancy will continue to decrease along with a strong inverse increase in rental rates. However, tenants must nonetheless realize that over 10,000,000 square feet of office space remains vacant, and that tenants willing to forego view space can still find deals on lower floors.

San Francisco's 2006 office leasing market began expectedly slow after a torrid second-half of 2005 that saw over 1,246,000 sq.ft. of positive absorption. Nonetheless, the first quarter's positive absorption of 271,338 sq.ft. represents the 11th consecutive quarter of declining vacancy, pushing San Francisco's overall vacancy rate down to 12.6% from the previous quarter's vacancy of 13.0%. Across the city, average rental rates in Class A and B buildings increased 7.6% over the previous quarter – climbing from \$32.07 to \$34.51/sq.ft.

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MARKET TRENDS				
	1Q06	4Q05	Change	Forecast
Class A Overall Rents	\$38.67	\$34.76	↑	↑
Class B Overall Rents	\$26.05	\$24.83	↑	↑
City-Wide Absorption	271,338 sq.ft.	459,568 sq.ft.	↓	↓
Total Vacancy	12.6%	13.0%	↓	↓

2Q06 Office Leasing Forecast

The vacancy rate is declining at a significantly slower pace than previous quarters – a trend consistent with a tightening market. A dearth of available space, fast rising rental rates, and exploding tenant improvement costs are the principal factors that should slow office leasing activity in the second quarter. However, the trend of a decreasing unemployment rate and a strong (albeit tenuous) economy should nonetheless keep absorption positive for a twelfth consecutive quarter.



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CBD Office Leasing Market

The market is tight and rates are escalating quickly— especially for Class A view space, as direct vacancy in upper floors is now 9.7%. For the first time since the dot-com, landlords are obtaining \$60 +/- sq.ft. rents. Class A CBD rents increased a remarkable 13% from the previous quarter, with the 1st quarter CBD Class A rent standing at \$39.23/sq.ft.

The first quarter in the CBD was most notable for the deals that did not happen. Two of the most significant tenants in San Francisco with expiring leases, Citigroup and Blue Shield, are expected to remain at their current locations. High costs of tenant improvements, best exemplified by the current union rate of \$90/hr for electricians, are a principal factor for many companies opting for renewals over new space.

1Q06 Significant Leases

Fenwick & West LLP signed the most notable deal of 1Q06 – subleasing 58,000 sq.ft. from Bank of America at 555 California St. at over 30% below present market value. The deal is revealing because it represents the exception and not the rule. Companies looking for large blocks of space in trophy buildings should expect to pay mid-\$50 + rents with rates continuing to rise.

Several large law firms signed leases this quarter. Skadden Arps Slate Meagher & Flom LLP and Green Radovsky Maloney & Share LLP each renewed their leases at Four Embarcadero Center. In addition, Morrison & Foerster LLP picked up 48,000 sq.ft. at 525 Market where they plan to move their entire back-office production.

About Us

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We specialize in office and industrial leasing, investments, and owner-user sales.

In addition, we also provide commercial property management services.

1Q 2006 Significant Lease Transactions

Building	Tenant	Submarket	Sq. Ft.	Type
600 Townsend St.	Advent Software	Showplace Square	104,000	Direct
1 Embarcadero Center	Nixon Peabody	Financial District	75,000	Direct
555 California St.	Fenwick & West	Financial District	58,000	Sublease
650 Davis St.	Esurance	Jackson Square	49,612	Direct
525 Market St.	Morrison & Foerster LLP	South Financial District	48,000	Direct
4 Embarcadero Center	Kirkpatrick & Lockhart	Financial District	42,798	Renew/ Exp
475 Sansome St.	Yahoo!	Financial District	42,782	Direct



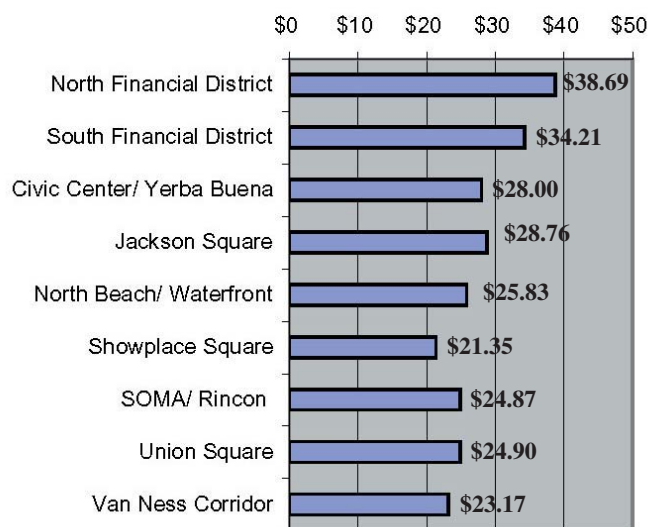
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San Francisco Submarket Analysis

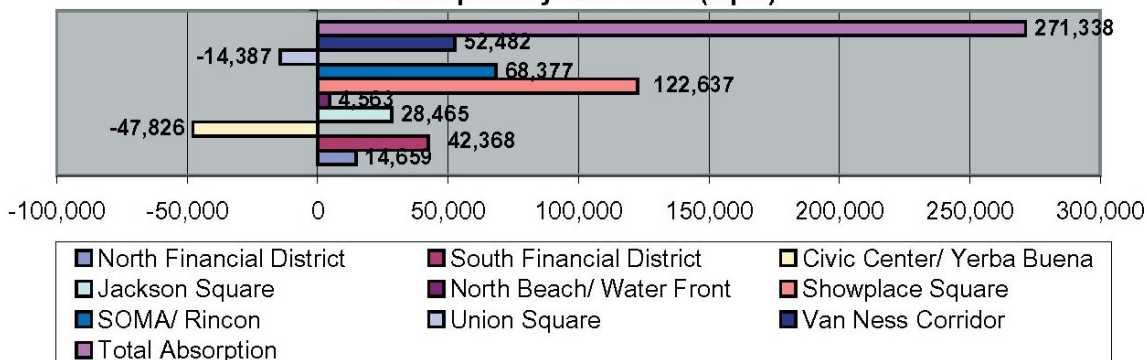
Showplace Square accounted for the largest absorption of any submarket due to the 104,000 sq.ft. lease Advent Software signed at 650 Townsend St. However, the deal will produce a net negative absorption as Advent is downsizing from 110,000 sq.ft between 303 2nd St. and 301 Brannan St.

With sizeable tenants leaving and considerable amounts of office being converted into residential and retail space, the Civic Center/ Yerba Buena submarkets continued to experience negative absorption, losing 47,826 sq.ft. during the first quarter. The submarket's negative absorption was more than made up with an incredibly tight SOMA/ Rincon market. SOMA's direct vacancy rate is currently 9.3% - it's lowest since the dot-com era.

1Q06 Submarket Rental Rates



Absorption by Submarket (sq.ft.)



Investment Market Analysis

As expected, the San Francisco office investment activity slowed down considerably compared to the blistering pace of activity over the last two years. With one-third of CBD office buildings changing hands in 2004 and 2005, inventory is low and investors are waiting to see to whether the market will, in fact, justify the high rates paid for these buildings.

2006 Investment Forecast

All indications point to a slow second quarter with interest rates expected to increase and inventory and cap-rates continuing to remain low.

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1Q06 Significant Sale Transactions

Building	Class	Buyer	Submarket	Sales Price	Price/ Sq. Ft
215 Fremont St.	A	Sterling American Property	Financial District	\$97,110,000	\$260
120 Montgomery St.	B	Resnick Development	South Financial District	\$67,500,000	\$160
300-320 California St.	B	LC Cal 300, LLC	Financial District	\$30,000,000	\$250

New Inventory

New Construction: Due to be completed this summer, Piers 1 ½, 3, and 5 will provide 69,000 sq.ft. of Class A office space near the Ferry Building, with several hedge funds having already signed leases. Shorenstein obtained entitlements to construct a 19-story, 350,000 sq.ft. office and retail building at 350 Bush St alongside a proposed 50,000 sq.ft. building office and retail building at 500 Pine St, adjacent to St. Mary's Square. Lastly, all indications have it that Tishman-Speyer will in fact begin construction at 555 Mission St., making it the first spec-building since 1999.

Office/ Residential Conversions: While the removal of office inventory for residential condo conversions is still in effect, a new source of decreasing inventory is the emerging commercial condo trend. Though the long-term success of the commercial condo model cannot be determined until the after-market value of the condos is defined, it nonetheless seems clear that some investors are preparing to take the risk. The 114 Sansome St. condos are now on the market, while 490 Post St. is prepared to undergo conversion soon. Both buildings are hoping to fetch rates in the neighborhood of \$500 +/- sq.ft.

Bio Tech: After considering competitive offers from Chicago, San Diego, and South San Francisco, biotech company Sirna Therapeutics agreed to a 40,000 sq.ft. lease at 1700 Owens St. (the first of four buildings Alexandria plans to build). The deal is significant because Sirna represents the first tenant to commit to Alexandria's 2.1 million sq.ft. campus at Mission Bay.

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