



### 2011 First Quarter: "Micro-bubble"...the return of the dot.com?

## MARKET OVERVIEW

In the first quarter of 2011, SoMa continued to enjoy positive absorption by technology companies focusing on social networking, gaming and mobile applications. This "micro-bubble" of rapid occupancies, in Rincon/South Beach, Mission Bay and South of Market submarkets, helped to end the quarter with 764,302 square feet of positive absorption for the San Francisco office market. The tight SoMa submarket continued to push tenants north into Financial District Class A buildings, putting pressure on rents and vacancies in that market.

### 1st QUARTER ACTIVITY

North and South Financial Districts closed the first quarter with roughly 6.2 million square feet of direct space available, down from 6.8 million square feet as of December 31, 2010. Direct average asking rates for Class A range from mid to high \$30's per square foot, and Class B from mid \$20's to low \$30's per square foot. Throughout the City, total available space shrank to around 8.9 million square feet, or 16.2% from 9.2 million at year-end 2010.

The South of Market space crunch and rising rents continue to drive tech tenants north, like Twitter's pending deal at 1355 Market. At the end of 2010, even Union Square landed tech tenants such as Craigslist, Technorati, Fluid and InKling. The tight vacancies drove average asking rates to the high 30's, for South of Market Class A properties. However, these are micro-bubbles of tight submarkets and rising rents. Vacancies still abound and rents fluctuate as one ventures west of SoMa, or to the North Financial and North Waterfront districts.

That said, tech tenants were the major

contributors to the large positive absorption for the San Francisco office market. They were also the main factors in driving the rents up.

Major lease transactions included Sedgwick, LLP's 89,000 square feet at 333 Bush, Goodby Silverstein's 81,065 square-foot renewal at 720 California, and Williams-Sonoma's 60,000 square feet at 100 North Point. Wells Fargo Insurance Services renewed their 51,081 square feet at 45 Fremont. Salesforce.com expanded 41,646 square feet at 123 Mission.

On the investment side, prices bounced back 40 to 50 percent from the 2009 bottom of the market. Argonaut is selling 250 Montgomery for \$34 million, or \$300 per square foot (they paid \$172 per square foot in 2009). 250 Brannan fetched \$340 per square foot, or 12 percent higher than its 2006 purchase price. Lembi sold 200 California for \$8.65 million or \$403 per square foot. The purported pending Sobrato purchase of 500 Terry Francois at \$91 million would be almost a 75 percent appreciation from the 2010 foreclosure sale price of \$52.5 million. However, troubled properties are selling for bargain prices such as the recent sale of 550 Kearny (50% vacant) for \$190 at 35% below the 2007 sales price.

### OUTLOOK FOR 2011

At the end of the first quarter, the national unemployment rate fell to 8.8%, with 13 straight months of private sector growth. Hirings in the South of Market district fueled by new social tech companies helped to lower San Francisco's unemployment rate to 9.1%, from 9.5% (12.3% for California). Overall, the economy looks like it is heading

in the right direction.

We should expect to see the continued expansion of the SoMa technology sector, as well as the biotech and medical facilities in Mission Bay (with UCSF). Salesforce's 14 acres in Mission Bay, purchased for their new headquarters, will further bolster the absorption in that district. San Francisco may soon experience the total number of tech jobs topping their dot-com peak. An important point to note, however, is that unlike the dot-com era, today's tech companies are more prudent in their usage of space--averaging 150 square feet per employee--down from 323 square feet in 2000, and are typically signing short-term leases.

As indicated in previous Trends reports, office absorption is closely related to business employment expansion. As the pace of tech sector expansion grows, the financial and legal sectors will be positively affected. We are starting to see some large professional firms entering the market early--as much as two years prior to lease expiration--to take advantage of low rents. In addition, the locally-based AMB and Denver-based Prologis merger should fuel growth and add some City jobs in the long run. An added boon is the preparation for the America's Cup, which is expected to create jobs and absorb space in the Waterfront districts over the next two years.

Unfortunately, California's economic woes still hang over the regional economy. The outcome of our State's budget solution will have a major impact on the local economy in ways which could influence business confidence and the pace of job growth. Job creation still remains the key for a turnaround in the overall economy.

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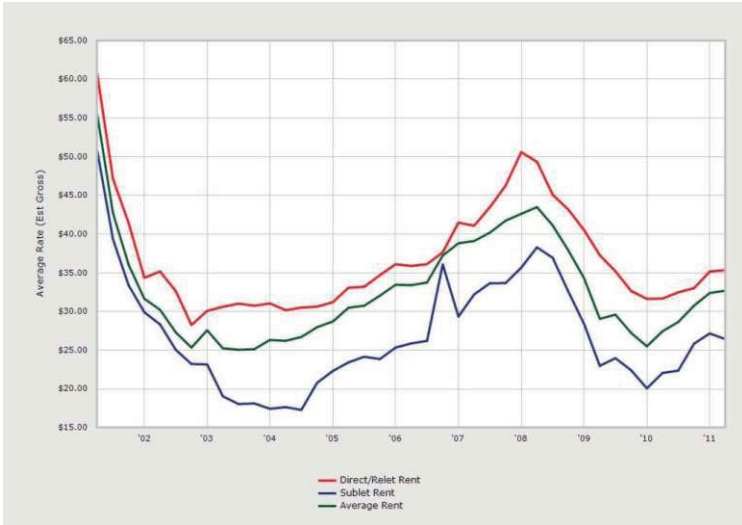
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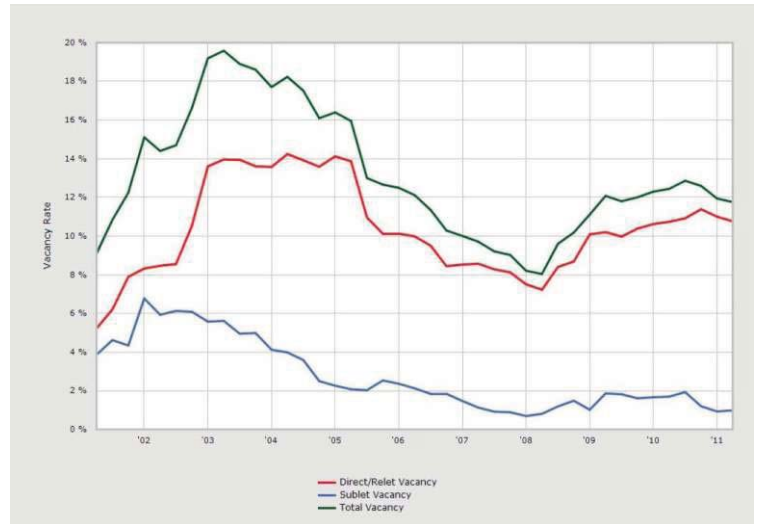
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**2011 Q1 SAN FRANCISCO TRENDS**

DOWNTOWN CORE RENTAL RATES - CLASS A



DOWNTOWN CORE VACANCY RATES - CLASS A



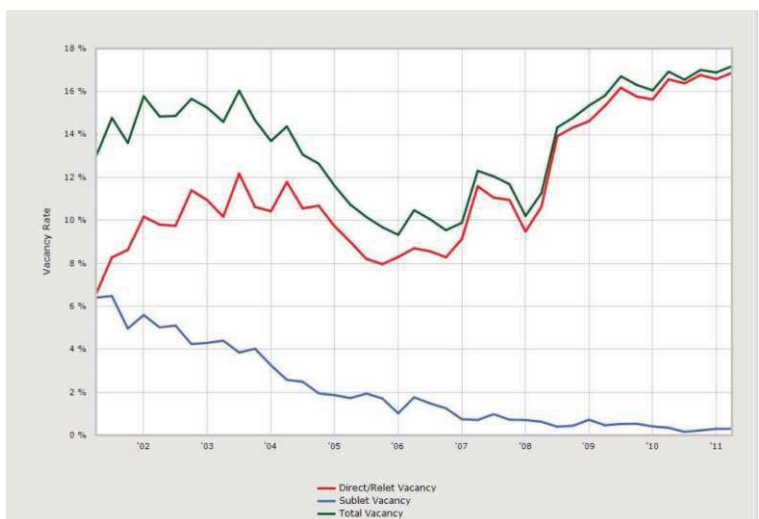
**Q1 LEASE TRANSACTIONS**

Tenant	Address	Class	Submarket	Sq.Ft.
Sedgwick, LLP	333 Bush	A	Financial District	89,000
Goodby Silverstein & Partners	720 California	C	Financial District	81,065
Williams Sonoma	100 North Point	A	North Waterfront	60,000
Wells Fargo Insurance Services	45 Fremont	A	South Financial District	57,081
Catholic Health Care West	185 Berry	A	Mission Bay	55,000
Aptimus	199 Fremont	A	South Financial District	51,000
Salesforce.com	123 Mission	A	South Financial District	41,646
California Dept. of Health Care Services	575 Market	A	South Financial District	36,324
Flack & Kutz	405 Howard	A	Rincon/South Beach	33,000
Mellon Bank	100 Pine	A	Financial District	32,000
ABM	600 Harrison	A	Rincon/South Beach	31,179
Recurrent Energy, Inc.	300 California	A	Financial District	30,610
Corporate Exec Board	580 California	A	Financial District	28,000
Yammer	410 Townsend	B	Lower South of Market	19,301
Mypoints.com, Inc.	50 California	A	Financial District	18,212
Calvary Management Group, LLP	2 Embarcadero	A	Financial District	18,098

DOWNTOWN CORE RENTAL RATES - CLASS B



DOWNTOWN CORE VACANCY RATES - CLASS B



Submarket	Net Rentable Area (sqft)	YTD Absorption (sqft)	Total Available (%)	Direct Available (%)	Direct Asking Rent	
					Class A	Class B
Financial District	29,195,942	77,742	17.2	14.8	\$33.06	\$28.09
South Financial District	26,174,302	263,072	15.1	13.9	\$38.29	\$25.18
Rincon/South Beach	5,486,763	79,324	9.2	8.2	\$42.49	\$31.40
Jackson Square	2,992,168	5,629	12.5	11.8	\$34.50	\$26.42
Union Square	5,681,704	29,959	16.5	14.9	\$39.50	\$26.50
Civic Center	5,643,635	11,306	14.1	14.1	\$30.72	\$18.83
Van Ness Corridor	2,730,319	48,158	11.5	8.7	\$27.57	\$26.12
Waterfront/North Beach	4,312,288	12,175	12.5	10.3	\$26.00	\$25.49
South of Market	6,341,851	(6,670)	21.0	21.0	\$33.66	\$30.56
Mission Bay/China Basin	2,911,026	37,842	26.4	26.4	\$58.74	n.a.

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