

Oakland-East Bay Office Insight Q4 2009

Economy

Closing out one of the worst years the East Bay economy had seen in more than two decades was a welcomed relief. Positive signs late in the year included stabilization in unemployment and substantial improvement in housing sales volume. Economists believe that Alameda and Contra Costa Counties have reached bottom, and 2010 will show modest growth. Although jobs in construction and hospitality continued to see declines, retailers provided a small boost with increased holiday season hiring. Replenishment of office jobs, however, will continue to occur at a slow pace as the economy recovers.

Market conditions

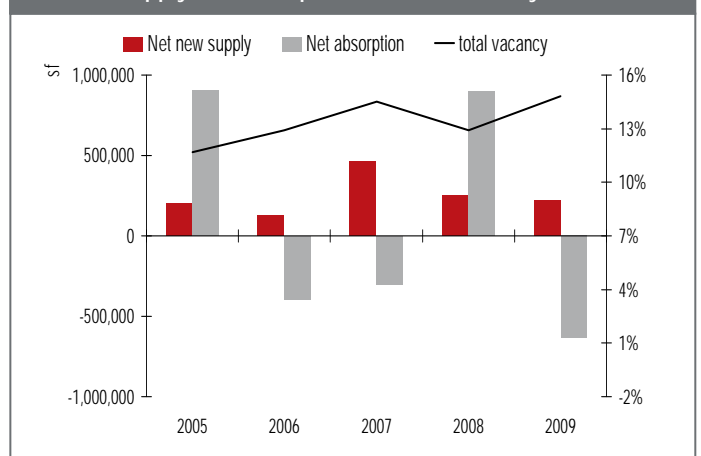
The fourth quarter of 2009 continued to show weakened office market fundamentals. Tenant demand and subsequent leasing activity remained significant obstacles to landlords during the quarter, as many tenants continued to wait for economic improvements prior to making lease commitments. Net absorption for the year, while not as severe as neighboring metros such as San Francisco and the Silicon Valley, contributed to the rising vacancy rate. The result was a further deterioration in the market. Although vacancies have increased since the start of the recession, the East Bay has consistently posted vacancy rates above 10.0 percent since 2001. Challenges facing the office market, while largely tied to current economic conditions, have also been linked to excess supply plaguing certain submarkets for nearly a decade.

Outlook

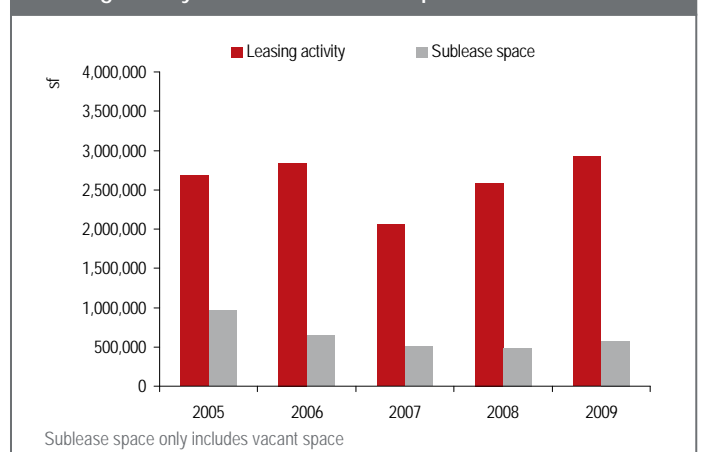
2010 promises to provide the Oakland-East Bay market with some relief from the recession as confidence returns. Rocked by the crash of the residential real estate market, the Oakland-East Bay market now provides buyers with great value, contributing to new growth in one of the most severely affected industries in the market. Additionally, when companies begin to replenish jobs that were lost, the abundance of supply in the office market will provide attractive options for companies to expand. The Oakland-East Bay market can expect to see rents reach bottom in the coming months, while increases in vacancy rates begin to slow.

Key market indicators			12-month forecast
Supply	Supply	44,346,358 sf	↔
	Direct vacancy rate	13.5%	↓
	Total vacancy rate	14.8%	↓
	Under construction (% preleased)	0 (0.0%)	↔
Demand	Leasing activity 12 mo. % change	-63.2%	↑
	YTD net absorption	-637,260 sf	↓
Pricing	12-month overall rent % change	-5.8%	↓
	Class A overall asking rent	\$28.86 psf	↓
	Class B overall asking rent	\$23.52 psf	↓

Net new supply, net absorption and total vacancy



Leasing activity vs. sublease vacant space

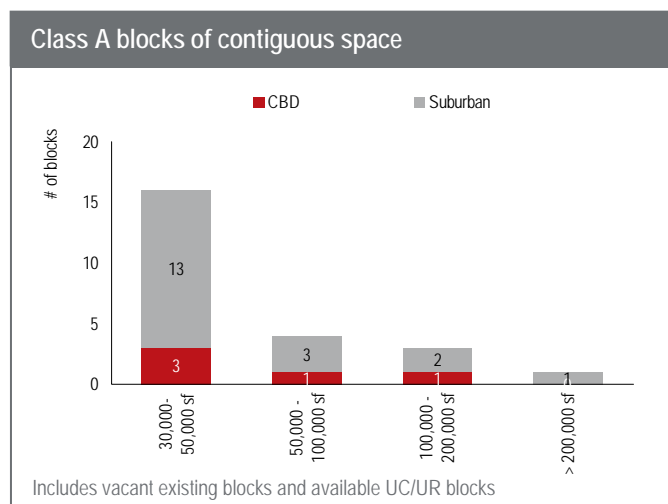
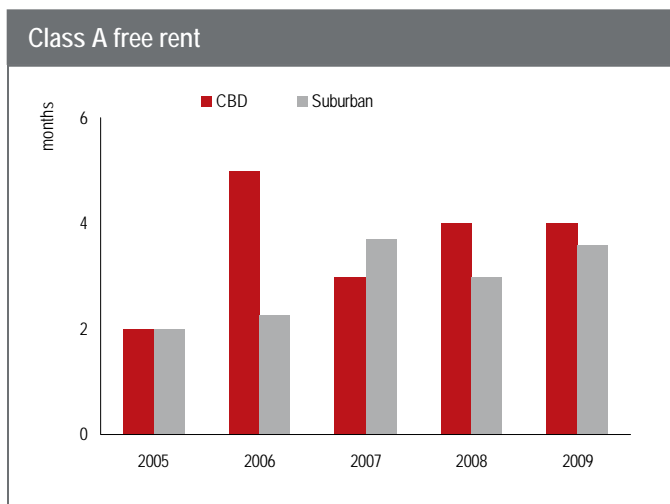
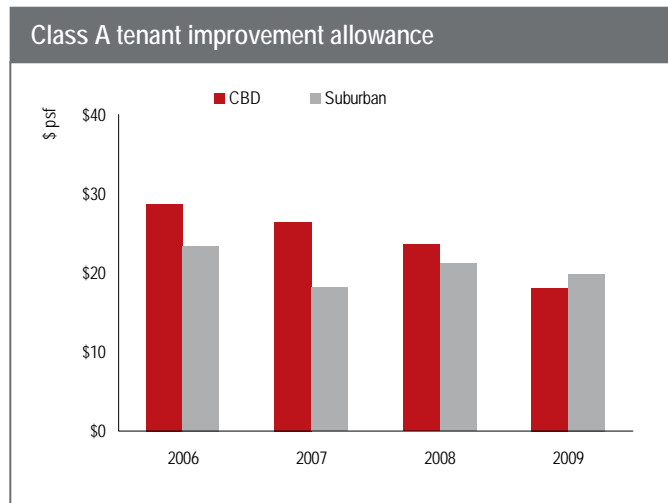
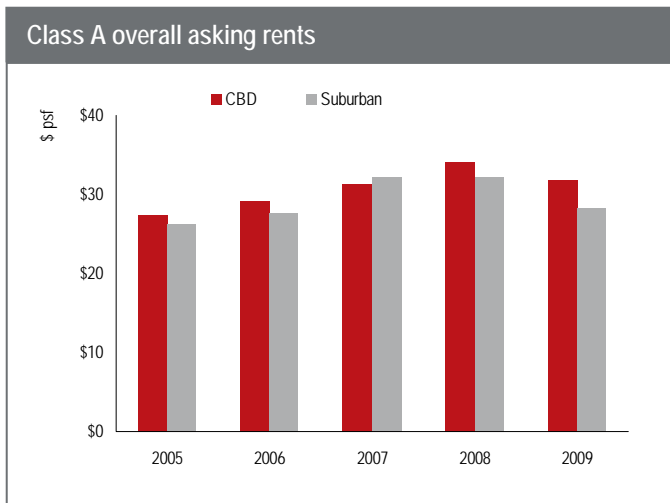


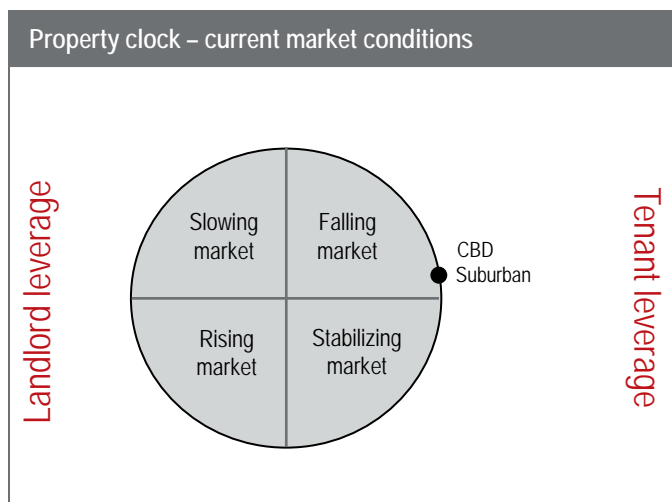
Tenant perspective

The deterioration in commercial real estate market fundamentals has created a very favorable environment for tenants in the market for office space. As landlords seek creative ways to maintain their occupancy rates, tenants have been able to negotiate better leasing terms and lower rental rates. While average tenant improvement allowances declined from 2008 to 2009, landlords during that time began to offer more free rent. Likewise, rental rates in Class A properties have also become more attractive for tenants, making it possible for companies to upgrade into higher quality buildings. During the next several quarters tenants can continue to expect favorable conditions and negotiating power.

Landlord perspective

Landlords, facing the prospect of prolonged vacancies, have been forced to find ways to maintain their bottom line in an environment requiring steep discounts in rental rates. With the rise in distressed assets and the return of hundreds of thousands of square feet to the market, supply has become a landlord's biggest competitor. However, while many landlords tried to maintain healthy occupancy by giving tenants greater negotiating power, some landlords have been unable to compete. More than 8.0 million square feet traded hands at the height of the market in 2007 causing a spike in rental rates. Today, those owners may find that current market rates have dropped to a level that would result in net negative deals. During the next several quarters landlords will continue to vie for credit-worthy tenants, but those tenants are becoming increasingly more active.





Submarket leverage – market history and forecast

Submarket	2007	2008	2009	2010	2011
CBD	Landlord-favorable conditions	Landlord-favorable conditions	Tenant-favorable conditions	Tenant-favorable conditions	Balanced conditions
Suburban	Landlord-favorable conditions	Landlord-favorable conditions	Tenant-favorable conditions	Tenant-favorable conditions	Balanced conditions

■ Landlord-favorable conditions
 ■ Balanced conditions
 ■ Tenant-favorable conditions

Completed lease transactions

Tenant	Address	Submarket	sf	Type
Old Republic Home Protection	Bishop Ranch 12 – Bldg B	Bishop Ranch	40,000	Renewal
Tria Beauty, Inc.	Dublin Corporate Ctr – Bldg 4	Dublin	32,168	New
Paradigm Health Corporation	Galaxy Office Park I	Concord	28,396	Renewal
WLC Architects	Saul Zaentz Media Center	Berkeley	11,800	New
Elavon	Hacienda Lakes – Bldg E	Hacienda Business Park	10,488	New
Wells Fargo	Mount Diablo Plaza 1	Walnut Creek-BART/DT	7,700	Renewal
enXco, Inc.	Bishop Ranch 8 – Bldg P	Bishop Ranch	7,584	Extension
Carroll, Burdick & McDonough LLP	1676 N California Blvd	Walnut Creek-BART/DT	7,465	Renewal
BKF Engineers	1646 N California Blvd	Walnut Creek-BART/DT	7,200	New

Completed sale transactions

Address	Submarket	Buyer / Seller	sf	\$ psf
1650 Harbor Bay Pkwy	Alameda	Worthington CA Investors LLC/Cawley Partners	67,700	\$118

Oakland-East Bay methodology: Inventory includes all Class A, B, & C office properties > 50,000 square feet, and non-owner occupied buildings



Real value in a changing world

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