

Frank Fudem's Corporate Real Estate Letter

July 2003

2003 Mid Year Report

San Francisco just sustained its 11th consecutive quarter of "negative absorption:" a decline in the amount of office space occupied. Occupancy shrank by 121,000 square feet in the Central Business District in the second quarter, nudging vacancies up to 20.8%.

Notwithstanding the above, there seems to be a whiff of optimism in the air. The Iraq war is (mostly) over. Interest rates are down and the stock market is up. For the first time in a long time, we are hearing clients plan for future head count growth when making real estate decisions.

The reverse side of this letter tells an interesting story: Most of the decline in occupancy occurred in the North Financial, Union Square, and South of Market districts. Note that absorption was strongly positive in the South Financial, Jackson Square/North Waterfront, and Yerba Buena submarkets.

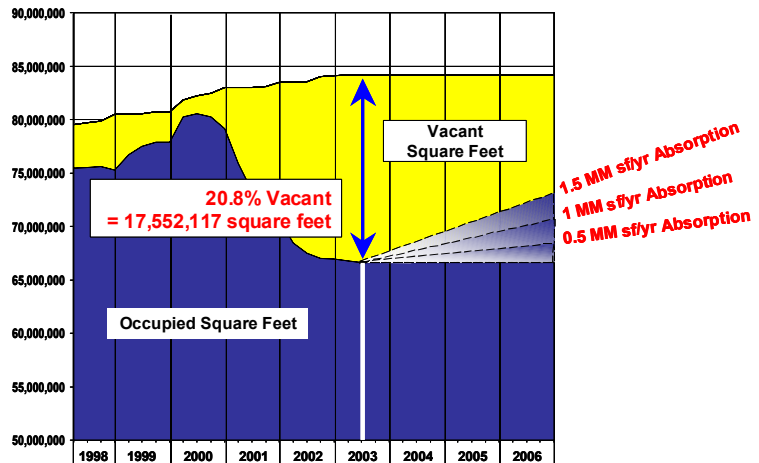
San Francisco lost more corporate headquarters in 2003, including DHL (to Florida), Matson Shipping (to Oakland), Cal Fed (acquired by Citicorp), Brobeck, Phleger and Harrison (disbanded), and Signature Bioscience (out of business). The loss of these headquarters is especially painful because of the "multiplier effect" their departure will have on their service providers, vendors and objects of corporate philanthropy.

There are some things in the "plus column" as well. A few companies recently chose to relocate to San Francisco, and some companies are expanding again. Since we are beginning to see spotty signs of economic growth, job growth may follow. Job growth would lead to positive absorption, which would begin to eat away at our 17 million feet of vacancy.

Is this the bottom of the real estate cycle? I don't know. The table below is a mathematic model (not a prediction!) of what would happen to San Francisco's vacancy rates if absorption turns positive.

How Can a Tenant Take Maximum Advantage of Today's Favorable Market Conditions?

1. If your lease expires within 18 months, negotiate a transaction with the longest term your business plans allow.
2. If your lease does not expire within 18 months, you might explore a "blend and extend" – an early extension with your current landlord.
3. Call us for a review of your lease and assessment of your real estate situation, and allow us to offer suggestions and recommendations.



If San Francisco Office Occupancy Were To Increase By An Average Of:	San Francisco Office Vacancy Rate Would Be:							Vacancy Rate Would Dip Below 10% in:
	12/31/03	6/30/04	12/31/04	6/30/05	12/31/05	6/30/06	12/31/06	
0.5 MM square feet / year	20.6%	20.3%	20.0%	19.7%	19.4%	19.1%	18.8%	2021
1.0 MM square feet / year	20.3%	19.7%	19.1%	18.5%	17.9%	17.3%	16.6%	2012
1.5 MM square feet / year	20.0%	19.1%	18.2%	17.3%	16.4%	15.5%	14.6%	2009

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SAN FRANCISCO CENTRAL BUSINESS DISTRICT
OFFICE MARKET CONDITIONS
Second Quarter 2003

	Direct Vacancy		Sublease Vacancy		Total Vacancy		Change in Total Vacancy Since Last Quarter		Change in Total Vacancy Since One Year Ago		Net Absorption (Change in Occupancy) Since Last Quarter		Net Absorption (Change in Occupancy) Year-To-Date	
	Sq. Ft.	%	Sq. Ft.	%	Sq. Ft.	%	Sq. Ft.	%	Sq. Ft.	%	Sq.Ft.	Sq.Ft.		
Submarket:														
North Financial District														
Class A 21,202,395 s.f.	2,903,838	13.7%	1,659,915	7.8%	4,563,753	21.5%	up 139,099	0.7%	up 708,113	3.2%	Neg (139,099)	Neg (112,109)		
Class B 6,163,969 s.f.	788,079	12.8%	443,804	7.2%	1,231,883	20.0%	dn (24,356)	-0.4%	up 14,240	0.2%	Pos 24,356	Pos 24,569		
Subtotal 27,366,364 s.f.	3,691,917	13.5%	2,103,719	7.7%	5,795,636	21.2%	up 114,743	0.4%	up 722,353	2.5%	Neg (114,743)	Neg (87,540)		
South Financial District														
Class A 18,822,816 s.f.	2,380,201	12.6%	1,338,910	7.1%	3,719,111	19.8%	dn (152,213)	-0.8%	up 554,840	2.5%	Pos 152,213	Pos 46,718		
Class B 3,504,579 s.f.	372,462	10.6%	130,129	3.7%	502,591	14.3%	dn (2,988)	-0.1%	up 96,367	2.7%	Pos 2,988	Pos 10,404		
Subtotal 22,327,395 s.f.	2,752,663	12.3%	1,469,039	6.6%	4,221,702	18.9%	dn (155,201)	-0.7%	up 651,207	2.6%	Pos 155,201	Pos 57,122		
Jackson Square/North Waterfront														
Subtotal 6,736,609 s.f.	1,074,615	16.0%	222,284	3.3%	1,296,899	19.3%	dn (76,687)	-1.1%	dn (18,223)	-0.3%	Pos 76,687	Neg (33,332)		
Union Square														
Subtotal 4,917,807 s.f.	601,091	12.2%	65,425	1.3%	666,516	13.6%	up 95,088	1.9%	up 108,709	2.2%	Neg (95,088)	Neg (96,778)		
Yerba Buena														
Subtotal 3,794,953 s.f.	577,192	15.2%	272,841	7.2%	850,033	22.4%	dn (112,887)	-3.0%	dn (22,313)	-0.6%	Pos 112,887	Pos 103,137		
South Beach/Rincon Hill/SOMA														
Subtotal 19,061,479 s.f.	3,573,564	18.7%	1,147,767	6.0%	4,721,331	24.8%	up 255,952	1.3%	up 50,505	0.2%	Neg (255,952)	Neg (195,632)		
All San Francisco CBD Markets														
Total 84,204,607 s.f.	12,271,042	14.6%	5,281,075	6.3%	17,552,117	20.8%	up 121,008	0.1%	up 1,492,238	1.6%	Neg (121,008)	Neg (253,023)		

Frank Fudem specializes in representing corporate tenants in office space transactions including relocations, lease renewals, and consulting. One of San Francisco's top brokers since 1984, he has represented local and national tenants in millions of square feet of successful negotiations. Personal Mission Statement: Increase my clients' success via real estate expertise.

BT Commercial Real Estate is the largest brokerage focusing exclusively on Northern California. BT Commercial has 130 agents in nine offices serving San Francisco, the Peninsula, Marin, and the East Bay. BT has consummated more than \$18 Billion of real estate transactions.

If you foresee a real estate need, or if you would like more information on San Francisco or Bay Area commercial real estate, please call, write, or email:
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