



Corporate Office Perspectives

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EDITOR:

Jeffrey S. Weil,
MCR.h, CCIM, SIOR
Executive Vice President

1850 Mt. Diablo Blvd.
Suite 200
Walnut Creek, CA 94596

Phone: +1 925 279 5590
Fax: +1 925 279 0450
CA Lic: 00786195
Email: jeff.weil@colliers.com
Blog: www.officetimes.com

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As I write this newsletter in mid-January, the stock market has just fallen more than 1,000 points just during the first week of the new year, the price of oil at unbelievable low prices, interest rates are up, unemployment is down, China's economy is scaring many, Americans fear another Paris or San Bernardino-type attack, California is finally getting lots of rain, and skiers and boarders are in heaven. Most Americans feel just "OK" about their personal economic situations but overall are still nervous and uncertain about the future. Tech in the San Francisco Bay Area continues to be over the top, the big boys like Google and Facebook are still taking down hundreds of thousands of square feet of new facility space, and San Francisco has more than 5 million square feet of new office space under construction, most of it already committed. The East Bay has more than 3 million feet of vacant Class A office space just waiting for San Francisco and Oakland tenants looking for comparatively cheap office rent.

I was recently asked to describe cutting-edge office design trends in one sentence, and here is what I said, "Cutting-edge office space design, to account for baby boomers, most of whom will be retired within 10 years and be replaced by Millennials, has much less emphasis on private offices and more focus on collaboration space, different types of space within the office to allow choice, whether it be lounge area for meeting with associates, small and large conference rooms, lunchrooms that also allow for both individual and group work, and technology allowing for mobility, so employees can work when, where and how they can be most productive."

An estimated 7.8 million people live in the Greater Bay Area, representing 20.2% of California's and 2.5% of the U.S. population. Compared to national economies, the Bay Area would rank 20th in the world. The GDP for San Francisco/Oakland was up 6.4% and for Santa Clara up 8%. ([Newmark Realty Capital, November 2015](#))

According to the Milken Institute's annual Best-Performing Cities Index, the San Jose metro area is number one in the United States, followed by San Francisco – San Mateo at number two. In another report, Christopher Thornberg, principal economist with Beacon Economics stated, "Ultimately, people are coming to the Bay Area and California because of the great lifestyle, great climate, arts, entertainment, sun, skiing, beaches, mountains, it goes on and on." "Despite red tape, high taxes and a burdensome cost of living, California is still deemed to be a good place to do business ..." ([Contra Costa Times, December 10, 2015](#))

As reported in the 4th Fourth Quarter 2015 National Real Estate Investor, Sam Zell just sold 23,262 apartment units (72 apartment properties) for \$5.37 billion. Sam has a track record of selling near or at the top of the market, then waiting for the market to turn to buy when it bottoms. He made a fortune selling his huge office portfolio right before the Great Recession began.

I recently gave a real estate forecast sponsored by RINA Accountancy Corporation and Chicago Deferred Exchange Company at Scott's Seafood, and the bottom-line prognosis was positive for 2016 and onto 2017 for East Bay commercial real estate, with an expectation of higher rental rates across the board for office, retail and industrial. At least here in the East Bay we aren't building much new inventory. If you would like to see the speech as well as all the links to the handouts (lots of great articles were referenced), just [click here](#).

In a recent report, "The New Westward Migration Is Real", just published by [Earnest - Personal Finance, The New-Fashioned Way](#), "nearly a quarter of all graduates who attended a top 25 school outside the West Coast moved to the West Coast within five years of finishing school and 81 percent of those who earned a degree from a top school on the West Coast remain in the region for at least five years after finishing their degree." What does this mean for our office market? More brainy people to fill office space in California and Washington. Let's see, today is supposed to be cold out here, getting down to the mid-50s ... compare that to Midwest or Back East temperatures ...

I am not sure where else this is occurring, but Walnut Creek is experiencing an influx of 3 - 8,000 square foot office tenants from Oakland and San Francisco. Plug & Play sublease space is becoming a scarcity all along the I-680 Corridor. Several premier Walnut Creek office buildings have raised asking rental rates to \$48/rsf or more (\$4/rsf per month), and rents in nearby Concord have gone up 20% during the past six months.

Office amenities are on the rise ... "The worker-friendly tech sector is also sparking the rapid expansion of amenity spaces in other industries. In order to keep people productive and engaged, and attract a new generation of workers, many companies are doubling the size of their amenities. Headquarters used to allocate between 3 and 5 percent of total space to amenities. Now, 8 to 15 percent is more common." ([Gensler Dialog 28](#))

Google gobbles Alameda Naval Air Station space for offices, engineering, R&D and manufacturing. On top of the 17,000 square feet it has through acquisition of a wind power company in 2013 and 110,000 sf it took in 2014, the City Council is considering another 65,000 square feet, with additional potential expansion of 300,000 ... Googleicious for Alameda! ([San Jose Mercury Business News, December 31, 2015](#))

According to John McNellis, "From 2012 to 2014, the San Francisco Bay Area created 382,500 jobs while providing only 68,200 new dwellings (homes and apartments). The forecast for 2015 is roughly another 4 new jobs for each new dwelling. Even if you consider economists' predictions on a par with those of shamans, you know the dismal science is dead-on about supply and demand. The 2014 median house price in America was \$206,800. In San Francisco, it was

\$1,006,600, five times more. Median apartment rents nationwide are \$1,231 while San Francisco's weigh in at \$3,396." ([LinkedIn.com, Apr 27, 2015](#))

Deals and Rumors: San Francisco continues to be hot with Twilia Inc. leasing 92,000 sf at 375 Beale St.; Delphix Corporation is taking 12,000 sf at 343 Sansome St. where Medidata Solutions leased 14,000 sf. WeWork might be out looking for another 100,000 sf, Oculus VR is reportedly looking for 40,000 to 60,000 sf, and Stripe, Stitch Fix and Twitch might also all be out looking for expansion space. Pivotal Labs is rumored to be seeking 125,000 rsf, NerdWallet seeking 100,000 sf, Asana looking for 100,000 sf, and Zymergen searching 100,000 sf. Airbnb reportedly is looking at 150,000 sf at 999 Brannan St. Google just purchased 925 and 935 East Meadow Circle (15,000 sf office building on 1.1 acres and 17,000 sf building on 1 acre) in **Palo Alto** where it already owns 10 buildings. Down in **Brisbane**, Ultragenyx Pharmaceutical leased 60,000 sf at 5000 Marina Blvd. YouTube just purchased a 554,000 sf office complex, the Bayhill office center in **San Bruno** which can accommodate 2,800 YouTubers. Bristol-Myers Squibb expanded by 61,000 sf to 255,650 sf at the Woodside Technology Park in **Redwood City**, Novartis leased 41,000 sf and Natera leased 88,000 sf at 201 Industrial Road in **San Carlos**. Intarcia leased 24,000 sf at Bridgeview Technology Park and Kaneka is taking 16,000 sf at Pacific Research Center in **Hayward**. Across the Bay in **Pleasanton**, Roche expanded by another 30,000 sf at 4155 Hopyard and Cisco took 21,000 sf at Rosewood Commons. In **Walnut Creek**, Mass Mutual rented 17,000 sf at 3003 Oak Road and Stearns Lending took 15,000 sf at 2700 Ygnacio Valley Road. In **Oakland**, Union Bank leased 37,000 sf at 1221 Broadway, CoreLogic took 24,000 sf at 555 12th St. and in **Alameda**, Cost Plus leased 107,000 sf at Marina Village Parkway for its new headquarters.

I was at a luncheon presentation recently and learned that for many Bay Area cities, just the city fees to get a building permit to build a new house can be as high as \$80,000 to 125,000 per home! That is before land or construction costs - no wonder housing prices are so crazy around here!

Big textile plants return to the U.S., bringing clothing production back to America, but without the jobs. "One-third of American companies with manufacturing overseas said they were considering moving some production to the United States." ([The New York Times, September 19, 2015](#)) Remember the one key word in The Graduate, which was "plastics"? Now the secret key word is "robotics"!

"In the San Francisco Bay Area, they can't build net-zero buildings fast enough and they are being leased for more than market value." (Site Selection, November 2015) I am not sure I agree as out here in the East Bay, I am not aware of a single net-zero building under construction at this time. Some of the elements in these buildings include solar power, green roofs, natural daylight, high-efficiency water fixtures, low-water landscaping, recycled rainwater, recycled building materials and sustainable wood.

Energy savings win-win program. One of the larger office building owners in the U.S., Shorenstein Properties, has a Sustainability Program Manager (great title and one that should last) who encourages and partners with office

tenants to conserve and prioritize sustainability through friendly competition, whereby individual facility teams are challenged to achieve as much energy savings below the previous year as possible. "Five properties have already realized over 4% improvement over 2014." (*Buildings, November 1, 2015*)

According to the November 20, 2015 Los Angeles Times, California has added 498,000 new jobs in 12 months. According to the Bureau of Labor Statistics, between October 2014 to October 2015, 463,000 new jobs were created.

Out here in the East Bay Tri-Valley and I-680 Corridor, any office lease or sale larger than 10,000 sf is a significant event, and the occasional 25,000 sf transactions are a huge deal. I know it is comparing grapes to watermelons, but just the San Jose Colliers offices monthly report announced: 191,000 sf long-term R&D lease; 12,000 sf sublease, 20,000 sf R&D sale, 210,000 sf office sublease, 32,000 sf office lease; 333,000 sf R&D lease; and more ... and that was just our office. That market averages more in a two-week period than ours does for an entire year!

Not totally office building-relevant, but related: "Why Renters Can't Make the Move" according to Lawrence Yun, National Association of Realtors chief economist says apartment rents have gone up dramatically, wages have not, home builders aren't building enough new homes, so house prices are also going up, with the result that renters have been unable to save for a home purchase down payment as the percentage of their income going to rent leaves them with little savings.

I was on a panel sponsored by CREW with the topic addressing the imbalance between all the new jobs that are being created in the Bay Area and the severe lack of housing to keep up with all this job growth. Studies are out showing we need 1.2 million new housing units by 2040 and yet we are on track to produce only a small fraction of this amount.

Top energy efficient states - The American Council for an Energy Efficient Economy ranked Massachusetts #1, followed by California at #2, then Vermont, Oregon and Rhode Island. State energy policies are assessed in six categories - utility programs, transportation, building energy codes, combined heat and power, state initiatives and appliance standards. (*Buildings, December 15, 2015*)

Are prorata office building operating expense passthroughs still a fair and equitable way to handle landlord reimbursement if you have a densely-packed tech company in the same complex as a traditional office user? If the 10,000 sf tech company using bench seating has 100 employees using electricity, going up and down the elevator, and using the restrooms 400% more than a traditional financial services, law or CPA firm with only 25 employees in the same size space, what is a fair way to deal with this? (*Buildings, December 2015*)

LinkedIn puts 100,000 sf on sublease market as it repositions its office space holdings, and Dropbox wants to sublease 200,000 sf of its China Basin offices in San Francisco. So far, tech sublease space gets gobbled up as quickly as it comes on the market, but when (not if, when) there comes a time where there is a massive influx of sublease space that may outstrip demand, this might be

the signal that the market has already peaked and we are on our way down the other side of the curve.

In a 2015 Robert Half survey, CFOs think giving employees benefits like health care is something employees care about, but in reality the young 20-something workers would rather have personal time off, be able to work from home, and have a cool company culture with “cool get togethers and happy hour.” (*SF Business Times January 1, 2016*)

Madison, who is in the 7th grade, just started her 2016 lacrosse season with the Scorpion Stringers, her second year in this new sport. One of Madison’s other fun hobbies is bowling, where she bowled a 160 a few weeks ago. Jordan who is in his first mid-year at Cal Poly, just became a member of the Alpha Epsilon Pi fraternity and spent the winter holidays in Cambodia. One of the many of his adventures was his assistance to doctors and nurses, helping villagers out in the hinterlands where medical facilities were scarce. He came back with lots of great stories and memories. Their recent photos can be seen [here](#).

Reflecting back over the years, the IBM 360 punch card in college, slide rule, TWA and Pan Am, the amazing VCR, my first reel-to-reel tape recorder in high school, the revolutionary Walkman, using floppies at work, the days when fax was king, and through it all, we still depend on decent warehouse space for our goods, retail space while different is still a necessity, and office space might look different, but is still an integral part of our economy. Tens of millions of us get up five days a week to commute to our place of work. There never was and still never is enough time to get everything done before we pack up for the evening and head home to our families, our pets and favorite television shows. For most of us, appreciative for what we have, all in all, it’s not a bad life and usually a great way to work and live. In America there are few limits beyond those we place on ourselves, as the many millions who came here from elsewhere with nothing but enthusiasm, perseverance, energy and optimism can attest - success is very much an achievable commodity in our land of opportunity. Be safe, be loving, and thank you for reading this!

Sincerely,



Jeffrey Weil, MCR,h,SIOR, CCIM
Executive Vice President
CA License No. 00786195

925 279 5590

jeff.weil@colliers.com

www.officetimes.com