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Wow, this issue marks the beginning of the 22nd year that I have been writing this bimonthly office industry newsletter, reportedly the longest running private newsletter of its type in the United States. The distribution list is now in the thousands, and thanks goes out to all of our readers for your support as well as the hundreds of thank-you letters we have received through the years. Your comments are always welcome at jweil@colliersparrish.com!

Since the mid-1990s, corporations have been cutting costs by moving their phone banks and customer service departments from high-wage urban areas to outlying areas all across the United States. In some smaller towns, these huge phone banks can be among the region's largest employers, taking advantage of a lower-cost of living, lower wages and lower real estate costs. Residents are happy to take jobs paying as little as $7 an hour…However, the next evolutionary step in this cost-cutting process is to run these call centers out of overseas countries such as India, Philippines and Costa Rica, where employees work with accent coaches to Americanize their English and will work at a fraction of the cost compared with the United States. New problems, however, include higher telecom costs, additional management travel and uncertainty about changing government regulations (and governments themselves).

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According to the *San Francisco Chronicle* (2/23/2002), the Bay Area job meltdown accelerated last month. "As the rest of the nation seems to be getting better, we are still sliding," says Mike Curran, director of the North Valley Job Training Consortium in Santa Clara County. "I deal with the walking wounded," said Paul Greenblatt, a counselor with Cupertino's Career Action Center. Layoffs are "still coming thick and fast. The cuts are so deep core people are being let go," said Greenblatt.

"The office absorption along the I-680 Corridor is down 35%…" This quote is from the April 1, 1986 OfficeTimes newsletter, which compared first quarter 1986 with first quarter 1985, and marked the beginning of our last office "recession." Back then, permanent commercial financing was "down" to 9.75 percent. Flashing back to the February 1, 1981 issue, San Francisco office rents were as follows: Fair to good space: $18-22/sq. ft.: Quality space: $26-36/sq. ft. – just about what it is today, 20 years later…

I'm not quite sure when we will hit bottom in the office sector. I began to feel slightly encouraged by positive news such as the recent flurry of leasing activity in the 2 to 10,000 sf range, or the weeks that went by without another major sublease announcement, or by a statement from one of the nation's largest industrial/flex developers who, last year undertook a significant downsizing, but now announced he was thinking of perhaps expanding his staff later this year … just when I begin to think, maybe later this year we might see the first rays of end-of-the-tunnel light, BAM, a number of large sublease announcements such as AT&T subletting 120,000 sf in Emeryville, Ask Jeeves officially canceling its 160,000 sf lease at Oakland City Center, Emeryville's Class A vacancy rate hits 46 percent, Santa Clara announces it has a seven-year supply of office/R&D space, Verizon announces another 10,000 jobs will be cut, as does the post office for an additional 10,000 jobs, then SBC says more jobs on top of the 7,500 recent cuts will be eliminated in coming months, so this groundhog still can't see his shadow anytime in 2002…

NAIOP just announced that an economic stimulus package just passed by both the House and Senate will provide immediate 30 percent depreciation write-off during each of the next three years for qualified tenant improvements. President Bush is expected to sign this into law within the next few days. Check with your tax specialist on how this might affect you, and if you get a definition for what TI's qualify for this write-off, please e-mail me at jweil@collierssparrish.com.

Deals and Rumors: In **San Francisco**, Triton Funding Group leased 14,000 sf at 221 Main Street; YMCA took 12,000 sf at 631 Howard Street; Far West Laboratory for Education leased 11,000 sf at 730 Harrison Street; Achex will be taking 11,000 sf at 149 New Montgomery Street; Thoughtworks leased 10,000 sf at 410 Townsend Street; Orrick Herrington & Sutcliffe announced it is in the renewal/relocation market for 175,000 sf; Treadwell & Rollo leased 12,000 sf at 555 Montgomery Street; San Francisco Art Institute leased 52,000 sf at 2565 Third Street; Bechtel took 25,000 sf at 425 Market Street; and Signature Bioscience, reported last issue to be relocating from Hayward to 65,000 sf at 475 Brannan Street; expanded this relocation to 100,000 sf. In **South San Francisco**, Coremank International leased 23,000 sf at 395 Oyster Point Blvd. and AGY Therapeutics will be consolidating its operations to 60,000 sf at Edgewater Business Park. In **Daly City**, Genesys Telecommunications is taking 113,000 at Pacific Plaza. Down in **San Mateo,** Net Ledger sublet 13,000 sf from PeopleSoft at 2955 Campus Drive. Up in **Marin**, Marin Community Foundation announced leasing 54,000 sf at Hamilton Landing in **Novato**. In **Emeryville**, Silicon Valley College relocated its Oakland campus to 21,000 sf at EmeryTech. In **Oakland**, Jack London Square Partners sublet 15,000 at 70 Washington Street and Internexus leased 10,000 sf at 2201 Broadway. Over in **Alameda**, Geneteric Inc. leased 32,000 sf at Alameda Harbor Bay. In **Pleasanton**, Prudential Realty signed for 21,000 sf at 5724 West Las Positas Blvd. United Grocers is rumored to be hunting for 10,000 sf in the **Tri-Valley** region, as is Team Health. In **Livermore**, Operating Engineers is proceeding on a 60,000 sf build-to-suit on North Canyon Road. The rumor in **San Ramon's** Bishop Ranch is 24 Hour Fitness relocating its headquarters to the 41,000 sf former ENRON space at Bishop Ranch 15. Up in **Concord**, Contra Costa County is rumored to be working on a 30,000 sf office lease at the Conco Cement building on Port Chicago, as well as a 30,000 sf requirement in the Neon facility in **Pacheco**. A few more biggies to report by the next issue…

Contrary to rosy predictions by some real estate professionals, analyst Jay Leupp at Robertson Stephens in San Francisco does not think the market will turn around this year. He's not even sure it'll get better in 2003. "We continue to believe that a meaningful rebound in San Francisco occupancy and rental rates will not likely occur until 2003 or later," Leupp wrote in a recent report. "Our bearish outlook is based on the fact that market rents and occupancies continue to fall at an accelerating rate, and our belief that Bay Area job growth will continue to languish over the next quarters." This was published in the *San Francisco Chronicle* (3/3/2002).

Summarizing the just-released Korpacz Investment Survey Q1 2002: Sales activity way down; 2002 looks to be the opposite of a stellar year for transactions (is that a tactful way to say it?); well-capitalized owners are refinancing rather than selling; lack of terrorism insurance is keeping sales activity to a minimum particularly for prominent skyscrapers and shopping malls; market conditions need to deteriorate further before buyers will act.

In the *Real Capital Analytics Office Capital Trends Monthly* report of March 2002, "Foreign Sellers accounted for approximately 17 percent of the CBD office market and 7 percent of the suburban market. Where Germans represent the bulk of foreign buyers, the Japanese represent the vast majority of foreign sellers. Sellers from the Pacific Rim accounted for $2 billion of sales, approximately 80 percent of all the office sales from the foreign sector."

Buildings (January 2002), in an article titled 'Why Go Wireless? Why Not?,' "Imagine a 1 million-square-foot building with 3,000 pieces of fire and safety equipment. All require inspection to prove compliance to the National Fire Protection Association. That includes more than 1,000 fire extinguishers, hundreds of fire pumps, safety exits, and tamper switches. For many facilities, that means arming fire and safety technicians with clipboards, paper, and pencils." Weeks later, after handwritten reports are turned in and entered into the computer system the reports are complete. "Now, imagine this: a fire and safety technician uses a hand-held computer to scan barcodes placed on fire extinguishers and other safety equipment. The time, date and location of the information is automatically recorded, and sent to the host PC for detailed report generation." This technology is here and now. Advice at the end of this article: When choosing your wireless system, it's important to pick a solution that doesn't force you to redesign your current processes. You shouldn't have to change your business to use the product. You should look for an off-the-shelf approach instead of a customized solution. Look for companies that have been around for a while and have a large customer base. Do they have any clients in your industry?

In the 2/28/02 issue of the on-line newsletter, *sublease.com*, Sam Zell, chairman of Equity Group states, "This is the largest supply of sublease space that has ever been available on the U.S. market." For example, the national vacancy of office space has gone from 5 percent a year ago to 12 percent today, a number Zell expects to increase further. According to *The Wall Street Journal* 2/25/02, "Last year, the office-building sector saw 117.8 million square feet in negative absorption," according to Reis, Inc., a real-estate research firm. "Between 1995 and 2000, the office market averaged an annual 88.1 million square feet in positive absorption," Reis says.

I've mentioned in prior recent newsletters that since 9/11/01 the commercial insurance market is in flux, with a government bill which would have created a pool covering 90 percent of major terrorist attack losses still stuck in Congress. Reported in the *San Francisco Chronicle* (2/27/02), "San Francisco architect Jeffrey Heller, recently returned from a conference in London on the future of tall buildings, warned that September 11th has put a damper on the development of skyscrapers for the foreseeable future." "Insurers won't insure them," he said. "Nobody is going to finance them. Tenants won't rent them, and workers won't work in them." It may not be quite as bleak as this statement. Even if terrorism insurance increases premiums 100 to 200 percent or more, this still remains one of the smallest cost components in a full-service lease and in a declining rental market may not even make a significant economic impact on the tenant. However, what if there was no coverage available, what if the landlord is unable or unwilling to carry a policy which includes protection against terrorism, what if you are in or near a "trophy" building, power plant, or landmark location, and how will this affect your business if another unthinkable act were to occur?

Just one example of where values went: Just two years ago, a certain San Francisco office building on California Street sold for $375/sf, when rents were skyrocketing in the $80 to 100/sf per annum range. Operating expenses were and still are around $12/sf, but current rents for this one particular example are now down to $24/sf serviced or $12/sf net. How would you even begin to estimate a value figure today?

In *Today's Facility Manager* (February 2002), the mobile warrior now has four basic choices ranging from PDA's such as Palm; Clamshell which is one step larger and comes with a keyboard; Tablets, which are like thick yellow pads with either touch-sensitive screens or keyboards; and laptop computers. "But, with all of the high-tech hype around, smart facility managers may feel compelled to ask one deciding question: Can mobile devices really provide a substantial return on investment and transform an organization's business process?" Greg Kozlik answers that question with an emphatic "Absolutely!" Kozlik is manager of mechanical systems and engineering technology for Rush Presbyterian St. Luke's Medical Center in Chicago, Ill. He incorporated mobile devices 3½ years ago and the results were nearly phenomenal. A 30 percent increase in efficiency was documented by a bench-mark study that compared a stable six-month period before mobile with a similar period after the implementation. The paperwork load for the techs has been eliminated. "They love the system," says Kozlik. "Instead of endlessly filling out paper forms, they can now complete a work order with just a few taps on the screen. The increased efficiency allows us to meet the demands of limited budgets and a never-ending workflow."

Synthetic Leases A Huge Potential Problem – U.S. companies may have to add more than $100 billion in debts to their books after accounting rule makers pass new regulations on the use of so-called synthetic leases used to hide real estate loans. The Financial Accounting Standards Board members recently agreed on most new rules for the type of financing vehicles that contributed to Enron Corp.'s collapse. Those rules will force "the large majority of all synthetic lease" arrangements to be reflected on corporate balance sheets, said FASB Chairman Edmund Jenkins. Investors say the leases, which provide the tax benefits of real estate ownership while keeping the debt off the company's books, obscure the extent of a company's liabilities and expose it to interest-rate risks. In *CFO Magazine* 1/1/2002, "Currently, interest payments on a synthetic lease for even a noninvestment-grade borrower can be as little as 150 basis points over Libor. That currently works out to roughly 4 percent -- interest payments under a sale/leaseback for such a company can run as high as 15 percent." High-tech companies that financed new property through synthetic leases might be forced to sell property even as values fall.

Current Bay Area office/R&D vacancy rates are somewhere between 50 to 60 million square feet. The bulk of this in Santa Clara/Silicon Valley, where industry experts estimate a seven-year supply of space. Quotes from a few major office building developers printed in the *San Francisco Chronicle* (2/21/02): "It's like a mortuary," Michael Covarrubias, president of the Martin Group, a San Francisco developer, said of the lack of demand. There is no leasing activity and little demand, he said. Another developer, Matt Lutucci, senior vice president for Jay Paul Company which built the 1.6 million-square foot Pacific Shores Center, where six of the 10 buildings sit empty, "It's clearly a very depressing time," Latucci said, "But we're in this for the long haul."

According to *Silicon Valley Business Ink* (2/8/2002), the number one workplace annoyance is cell phone ringing, followed by malfunctioning equipment. Just wait until we get the LAN and WANs up to full speed and your cell phone might be your main communication tool wherever you go…I like the new feature out, which instead of ringing sprays water, and the longer the callee takes to reach his/her phone the wetter they get…(of course that's a joke!)

*Buildings Magazine (*February 2002) had a terrific short article on how better space usage prediction through automated space planning can help organizations to maximize their current resources and strategically anticipate future needs. "Planners update records online, or better yet, they instruct individual departments to update their own records in one central database.

Organizations that have adopted the latter method have saved thousands of dollars a year in funds that would otherwise go to a heavily-staffed and overburdened planning department. Using this data, space planners can anticipate their client's needs. Vacancies are quickly identified to accommodate new hires; telecommunication and furniture tracking tools ensure that employees moving into a new area will have all the equipment they need to start being productive right away. Users can create multiple 'what-if' scenarios to determine the most cost-effective solution. Strategic space planning is an essential cost-cutting tool, too. Charging departments for the space they use is easy when all the data needed can be extracted from a database – even if a department uses a room only once a week." This article was written by Jim Goodfield, vice president at Archibus, who can be reached at james_goodfield@archibus.com.

In another viewpoint supporting the theory that we have yet to see bottom in the commercial real estate arena, *California Real Estate Journal* (Feb. 25, 2002) included an article, 'Fire Sale, Anyone?' "As cash-strapped companies mount and real estate values plummet around the state, the 'vultures' are circling. But with the economy going south in 2001, opportunity funds are scouting once tight markets such as the Silicon Valley, looking for bargains. Other prominent regions for opportunity funds in California include Oakland and San Francisco; two other tech-dependant markets with increasing vacancy rates and weakening real estate values, according to Torto Wheaton Research in Boston. Currently, there's a lot of cash waiting to go somewhere-- about $20 billion in equity to be placed in real estate investments within the next few years, according to Ernst & Young."

It seems that whatever the current age of our son, Jordan, it is the coolest. Jordan turns 5 next month on May 26th, sharing the same birthday with my wife, Lisa (wish I could take credit for that birthday present, but…). I've been taking Jordan up to Tahoe's Northstar ski school whenever possible, and just two weeks ago his class instructor suggested that the little guy was ready for the intermediate runs at the top of the mountain. So, father and little son took the main chairlift up the mountain (you have to "scoop" a child his size onto the chair, then lift them off at the top). Jordan and I had a blast going down intermediate runs together, me with the huge face-wide grin all proud parents experience in times like these. His most recent photos can be seen at http://www.officetimes.com/JordanApril02.htm. Have a safe beginning of spring, and as always please feel free to contact me at jweil@colliersparrish.com.

Sincerely,

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