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## Corporate Office Perspectives

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Rental rates for almost every class and category of office and lab space are still at record-lows, with landlords now competing head-on against long-term plug and play space. The vacancy rates in most Bay Area sub-regions are still up, although a few stronger submarkets like the better San Francisco prime Financial District view space, Downtown Walnut Creek, Orinda (\$3.50/sf plus paid parking) boast of much lower vacancies. Check out [www.officetimes.com](http://www.officetimes.com) for a comprehensive mid-year Bay Area office market report. We haven't hit bottom yet, but at times it almost feels like we're just about there - maybe 6 to 18 months before the slow transition from the current tenant's market back to the landlord. Remember, we are in perfect balance for only one day and these cycles last years...

New York boasts 40 of the Fortune 500 firms headquartered there, but if you include the Bay Area cities as one locale, we are headquarters to 26, followed by Houston with 18.

While the Bay Area has lost or will be losing corporate headquarters jobs with firms like DHL, Jacuzzi and San Francisco Music Box Company announcing relocations to the Southeast, other firms which had the opportunity to flee our high-price cost of living choose instead to take advantage of super-low real estate costs and retain skilled workforces. Many times the employees won't move to Florida or North Carolina no matter how big a house they can buy for what their Bay Area house is worth. Another recent example is eBay, which is buying a 511,000 sf office campus in San Jose with extensive expansion opportunities. On the other hand, perhaps eBay is the smart kid in the class. Boeing Co. decided two years ago to move 1,100 engineering jobs from Southern California to Texas and Florida in search of lower costs. According to the *Los Angeles Times* (4/13/03), "The decision to move the jobs was highly unpopular among Boeing's workforce, and about 80 percent of the California engineers refused to relocate, forcing the company to hire workers in Texas and forfeit much of the experience of its California engineering base." There is now an investigation as to whether this inexperience has any part of the blame for the space shuttle Columbia disaster. What would happen to your companies product-line, engineering or corporate "intelligence" if 80 percent of your brainpower disappeared from your workforce?

According to a recent *San Francisco Business Times* article (4/18/03), "Pending appeals by commercial property owners claiming \$9.7 billion worth of lost value could cost the city \$109.2 million in tax revenue, according to the City Assessors Office records... with more than 17 million square feet of office space vacant, Class A rents at less than half their peak, and hotels largely under-occupied, hundreds of other commercial cases are under appeal."

In *Buildings* (April 2003) International Facility Management Association (IFMA's) 23<sup>rd</sup> research report, *Project Management Benchmarks*, reported that the most dramatic drop in measured space has been in upper management spaces. "Those occupying corner offices have found their average space decreasing from 280 to 239 square feet, while senior management offices have shrunk from 193 to 169 square feet. Office sizes have decreased an overall average of 13 percent since IFMA's last report." There was no mention of the latest trend in "bunk cubicles" where cubes are stacked on top of each other, with benefits including double the space utilization, and ensuring workers keep their heads down while working ... (just joking, what, you thought this was for real?).

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What a sign of the times! Usually the *Business Times* saves its real estate news for larger transactions, but in the April 4, 2003, Deals section there was a nice chunk of press because “Financial Services firm Wudski Rockman has signed a 2,073 square foot lease at the Ferry Building.” This was followed by another article for a 5,427 sf lease, so I knew we hadn’t yet hit bottom no matter what the “experts” are saying!

On the one hand you have recent articles by PeopleSoft, Inc. and others such as in the *San Ramon Valley Times* (5/7/03) “PeopleSoft shifts work to India to cut costs. Computer-related companies based in the U.S., have moved work to India to lower costs and tap the country’s pool of computer engineers. Oracle Corp. has 2,700 employees in India and plans to boost that to 4,000 by the end of the year. Intel Corp. last month said it’s spending \$41 million on a Bangalore development center.” In another *San Ramon Valley Times* article on May 13, 2003, in discussing Bank of America’s decision to send jobs to India, “Proponents say that hiring technology workers overseas will make the company stronger: For one, it cuts costs, A contractor in India, the most popular locale, is typically paid \$10,000 compared with \$100,000 for a U.S. worker with the same skills. Proponents argue that this allows companies to stay competitive, saving and creating U.S. jobs.” Yeah, right ...

In the *Corporate Real Estate Leader* (CoreNet) March 2003, in answer to “What new trends incorporate real estate management do you see evolving? What new issues on the horizon?” Robin Ronne, SVP of Economic Development, Tampa Chamber of Commerce, “One big issue that I’m seeing now with both current clients and potential clients is the Federal Reserve white paper related to redundancy and resiliency for major financial services operations. Many of those operations currently are concentrated in downtown business districts and there’s a concern about the resiliency of the system if something else – another terrorist attack happens.” Gordon Lorig, VP, Strategic Infrastructure Group, JP Morgan Chase, “I’m in on that up to my ears at the moment. The proposal would require financial institutions to split up some of their functions, take them out of a highly concentrated areas and move them into new employment markets – possibly as far as 300 miles away. The idea is to minimize risk. If the two airplanes that struck the World Trade Center had been about three blocks further east, some significant banks would have been knocked off. But the concern is more about people than buildings ... the Fed has backed off a little on the 300 mile issue but it’s still requiring that each of the major financial institutions within the next six months have a plan to show how we’re going to minimize risk.” Do it at 10 cents on the dollar and move one operation to India or Asia ... that should save a lot of U.S. jobs to boot ...

Whether you are a major office property owner or a tenant in a high-profile office building, what are the long-term consequences if an unthinkable event like 9/11 were to occur in your business neighborhood? Yes, there is commercial insurance available, but what are all the exclusions? What is the immediate medium and long-term effect on your specific location? From an article in the March 31, 2003, *Tri-Valley Times*, “Buildings near World Trade Center still closed... Eighteen months after the World Trade Center was destroyed, several surrounding office buildings are still closed, and the future of the largest remains uncertain.” According to *tenantwise.com*, “nine of the 23 large office buildings damaged in the September 11 attack are still closed.” Also, according to *Real Estate Forum* (March 2003), “The new Federal Commercial Insurance backstop Terrorism Risk Insurance Act of 2002 law suggests that current exclusions for losses due to nuclear, biological and chemical weapons can remain in place, as well as domestic acts of terrorism such as the Oklahoma City bombing.”

*Deals and Rumors:* For a change, let’s start with **San Francisco**: KEI leased 13,641 sf at 543 Howard St.; The California Academy of Sciences is taking 204,000 sf at 875 Howard St.; Citigroup signed a 47,000 sf lease at One Sansome St.; Keen Inc. sublet 19,000 sf from Informatica Corp. at 100 California St.; California Appellate Project took 18,000 sf at 101 Second St., where Hong Kong Bank leased 17,000 sf at the same project; Flack & Kurtz leased 21,000 sf at Foundry Square; UCSF is taking 66,000 sf at 2300 Harrison St. as well as 50,000 sf at 185 Berry St.; Exploratorium might be purchasing the 211,000 sf building at 601 Townsend; United Way leased 32,000 sf at 221 Main St.; Service Employees International Union expanded to 15,000 sf at 1390 Market St., and David, Cowell & Bove leased 10,000 sf at 595 Market St. Heading South, Gryphon Therapeutics Inc. sublet 50,000 sf of biospace as did Corgentech Inc. for the same size in **South San Francisco**, Kaiser Permanente leased 120,000 sf of medical space on Hickey Blvd. in **Daly City**; California Teachers Association took 20,000 sf at 333/343 Hatch Dr. in **Foster City**; Made in France San Francisco Inc. leased 42,000 sf of office space at 211 South Hill Dr. in **Brisbane**; Check Point will be subletting 48,000 sf from Oracle in **Redwood City**; Catholic Healthcare West took 30,000 sf at 1825 S. Grant in **San Mateo**; Actel Corp. is leasing 160,000 sf at 2051/2061 Shoreline Court in **Mountain View**; and down in **Palo Alto**, Gray, Cary, Ware & Freidenrich leased 120,000 sf of the 143,000 sf former Brobeck space on University Circle. Over the other side of the Bay in **Fremont**, Mattson Technology just leased 100,000 sf at 47131 Bayside Parkway, and in **Oakland** the big rumor is Bart’s LOI for 200,000 sf at the Kaiser Center (I had my wedding reception there 13 years ago on the top floor at the Lakeview Club...), Laughlin, Falbo, Levy & Moresi leased 16,000 sf at 555 City Center, and also at the same building Boornazian, Jensen & Garthe leased 18,000 sf. The Salvation Army leased 13,000 sf of office space at 1914 Park St. in **Alameda**, and Pacific

Research Institute took 18,000 sf at 1995 University Ave. in **Berkeley**. Over in **Mill Valley** Redwood Trust Inv. leased 21,000 sf of office space at One Belvedere Place; in **Novato** HRH of N. Cal. took 12,000 sf of office space at 7250 Redwood Blvd., and Provident Funding leased 17,000 sf at 1235 N. Dutton in **Santa Rosa**. The big news in the East Bay was Ross's headquarters relocation from **Newark** to 150,000 sf at 4440 Rosewood Dr. in **Pleasanton**. University of Phoenix will be leasing 25,000 sf in **Livermore** near the Airway Blvd. exit. In **East Dublin**, Ellie Mae sublet 31,000 sf at 4140 Dublin Blvd., and in **San Ramon**, Centex Homes leased 62,000 sf at Bishop Ranch 7 and Priority Financial took 11,000 sf at 4000 Executive Parkway. In **Walnut Creek**, Virgin Mobile might be leasing 16,000 at Mt. Diablo Plaza; I helped Valent U.S.A. with a long-term sublease for 22,000 from Homestake Mining Company at 1600 Riviera Drive; Bank of America leased 11,000 sf and Raines, Melton & Carella Inc. took 11,000 sf; both tenants going to Three Ygnacio.

There are a number of differing opinions on the condition of the economy, both statewide as well as nationally. In the *Tri-Valley Herald* (4/15/03), "State's economic forecast bleak ... California to remain in morass until 2005, economist says." Sung Won Sohn, chief economist at Wells Fargo & Co., said on the same day, "The state's forecast is overly optimistic about a resurgence in corporate profits next year, and that could translate into disappointing corporate income tax receipts." Sohn says ... "The jump in corporate profits is not consistent with the rest of the economic picture."

In the April 11, 2003, *Tri-Valley Times*, "Chief executives of large companies, perhaps the most accurate economic forecasters recently, expect the economy to remain weak during the next six months, only about one company out of 10 plans to increase employment in the United States. The rest, about 90 percent of companies, are divided almost evenly between those that plan job cuts and those that expect to hold employment at current levels.

A number of years ago I predicted that San Joaquin County was developing some of the same similarities as the I-680 Corridor of 25 years ago, and if you fast-forward to 2030 (I may still be writing this Newsletter but most of you will be out playing golf and spending your kids' inheritance), there may be hundreds of thousands of residents, large-scale experienced business parks, and as Walnut Creek witnessed last month, the grand-opening of the very upscale jeweler Tiffany's, who knows that Tracy won't experience the same one day in the future. A new town is underway called Mountain House, just over the hills from Livermore. All current home releases are sold out as soon as they hit the market, with homes priced from \$300,000 to \$500,000. At full build-out the 7.5 square mile town will be home to 44,000 residents, 22,000 jobs, 12 elementary-middle schools, and two golf courses. Each of the 12 neighborhoods will feature an elementary school, park and small shopping center within a 10-minute walk.

For those of you not familiar with leasing space to the Federal Government, there are both benefits as well as pitfalls. In the *Real Estate Forum* (February 2003), GSA leases are structured with no annual rent hikes. Increases in operating expenses, excluding real estate taxes, can only be increased by the CPI for that year. The government can also be slow moving, and any lease larger than \$2.3 million in lease payments must get permission from Congress. On the benefit side, great credit ...

Bad economy and dotbombs notwithstanding, California still grew by almost 600,000 people last year, the fourth in a row that annual population has exceeded the half-million mark. Most new residents arrived at the hospital whereas in the past they came from other states ...

*California Real Estate Journal* (5/19/03), "Some Northern California real estate leaders are preparing a turnaround, but many don't expect a strong market for years. Peter Adams, executive vice president with Equity Office Properties Trust, said, "The market is not going to recover until we get more jobs." Adams predicts the Bay Area recovery and a return to a 10 to 12 percent vacancy rate could take between three and seven years." Tom Poggi, vice president of the CAC Group, predicts "vacancy will drop to 18 percent in 2004, then 16.55 percent in 2005. We see the market getting better but not until the '06-'07 time frame," Poggi said. However, according to Colliers International in the *California Real Estate Journal* (4/21/03), "San Francisco Sees First Positive Absorption in 9 Quarters - 56,194 square feet." So figure ... What do I think? At times the East Bay office market almost feels like we've hit bottom, with several of the submarkets beginning to experience an improvement, deals are actually being done, and for brokers working the sub-5,000 sf market, a definite velocity of transactions. This feeling of pseudo-euphoria quickly dissipates when another 50,000 sf block of long-term Class A space hits the market, quickly wiping out whatever strides the 20 2,500 sf tenant signings may have made. There are also terrific bargains, like 40 to 80,000 sf of Bishop Ranch Class A plug and play sublease space for \$1.50/sf full-service, 50,000 sf of Class A long-term Pleasanton plug and play for \$1.25/sf full-service, and 60,000 sf of Walnut Creek office space for \$0.60/sf nnn ... just sitting there ... if the market were improving wouldn't the quality bargains be quickly snapped up?

A recent article published in *Business Facilities* (March 2003) titled, "How to Move Your Office Successfully" lists 10 things you must know to make sure your office move goes without a hitch. 1) How will you communicate throughout the project with your architect, contractor, move team and staff? 2) How will you manage all of the information? 3) Who will be the sole point of contact and take responsibility? 4) How will you make purchases? 5) Identify contract requirements, your basis for selecting a vendor. 6) Divide the move into phases. 7) Develop realistic budgets. 8) Know your responsibilities versus the contractor's responsibilities. 9) Identify long-lead items (such as security, furniture, phone systems, etc.). 10) Develop your relocation plans.

All within 30-days, announcements of a resurgence in San Francisco South of Market office leasing with more than 400,000 sf leased since the beginning of the year, tempered by a nearby South San Francisco major biotech closure throwing more than 200,000 sf of space on the market which will double available lab space there. South San Francisco has around 6 million square feet of lab/R&D space and is one of the largest biotech real estate markets in the world. Totally different markets but a good example of a market still in flux ...

Jordan, our son who just turned 6 last week on May 26, had an awesome ski season and graduated to level 8 (out of 9), skiing the black diamond runs and scaring his folks with terminologies like "helicopter" and "reverse 180's", whatever these are ... Jordan's other three passions are T-Ball, chess and Tai Kwan Do (click <http://www.officetimes.com/JordanJune03Page.htm> to see his latest adventures). Another milestone in the life of a parent is when your child bonds with a neighbor kid the same age and would rather spend time with his buddy than you... one part of me is saying, "Yes, I now have part of my life back after all these years," but the other hand it's sad because his world no longer totally revolves around me. I know from more experienced parents, this gets worse (or better)... savour the moments, go out of you way to find roses to smell and have the best Spring of your life!

Sincerely,

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