

MARKETBEAT

Office Snapshot Q1 2016

San Francisco



SAN FRANCISCO OFFICE

Economic Indicators*

	Q1 15	Q1 16	12-Month Forecast
San Francisco Employment	521K	534K	▲
San Francisco Unemployment	3.9%	3.3%	▼
U.S. Unemployment	5.6%	4.9%	▼

*Q1 16 data based on the average of January and February values

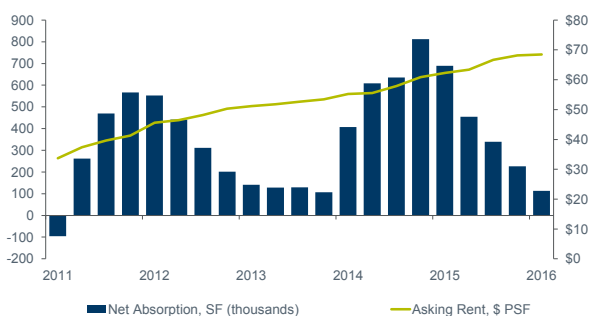
Market Indicators (Overall, All Classes)

	Q1 15	Q1 16	12-Month Forecast
Overall Vacancy	6.4%	5.7%	▲
Net Absorption (sf)	812K	359K	▼
Under Construction (sf)	4.3M	4.4M	▼
Average Asking Rent*	\$62.29	\$68.44	▲

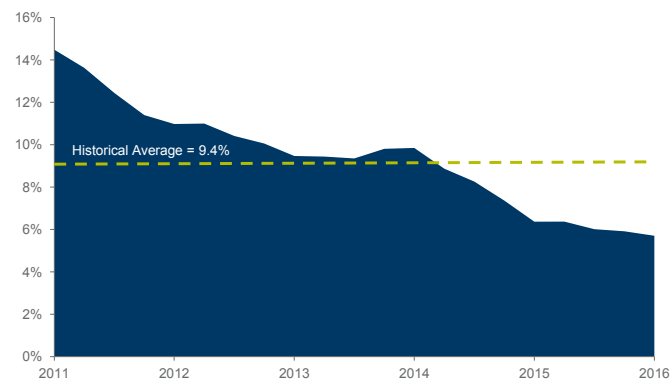
*Rental rates reflect full service asking \$psf/year

Overall Net Absorption/Asking Rent

4Q TRAILING AVERAGE



Overall Vacancy



Solid Fundamentals but Tremors Underfoot?

The metropolitan division of San Francisco (San Francisco and San Mateo counties) began 2016 essentially at full employment. Total private sector positions closed February at 939,900, up by 37,700 or 4.2% year-over-year. Office using positions have increased 6.0% since February 2015 to 403,300. The subsector of computer systems led the way, rising by 13.2% to 69,600. Financial activities increased 2.1% to 73,400, while information saw a healthy increase of 5.0% to 60,500. Standouts from the non-office using employment side included construction (up 11.9%) and retail trade (up 3.0%). Other Services which includes many non-profits saw jobs fall 1.3% over the past year.

From a high level, fundamentals in the first quarter of 2016 appeared to continue in the same trajectory as previous quarters; declining vacancy, increasing rents (albeit at a slower rate), and positive absorption. Several factors are influencing the market and pointing to a cooling in the next 12 months: primarily over-blown valuations in the tech industry and a soaring cost of living. New sublease space has been hitting the market at an increasing level with more than half of that space originating from tech tenants. Furthermore, almost half of that new sublease space is due to tenants contracting or consolidating.

Citywide, the overall asking rent closed Q1 16 at a record high of \$68.44 per square foot (psf). However, not all submarkets fared the same, as the class A overall CBD asking rent actually decreased 0.9% to \$70.64 psf. This marks the first quarterly decrease since Q2 10. Citywide overall vacancy fell to 5.7%, declining 20 basis points (bps) over the quarter and finished well below the 6.4% reported at Q1 15.

CBD vacancy landed at 6.5%, down from the 6.8% reported in Q4 15 and down from the 7.5% reported in Q1 15. Non-CBD vacancy remained flat at 4.1%. Class A direct CBD vacancy completed the quarter at 5.6%, a 140 bps decline over the past year. The North Financial class A submarket recorded the highest negative net absorption: 141,955 square feet (sf) with 101 California Street the largest contributor of new space. Class A rents in that submarket fell for the first time since Q3 12, dipping 3.1% to \$70.05 psf.

There was one new office building completed in Q1 2016 - Tishman Speyer's 450,000 sf class A building at 222 Second Street in the South Financial submarket with LinkedIn occupying the entire building. It was the first new building delivery Citywide since 2014. As of the end of the quarter there was 4.4 million square feet (msf) of space under construction Citywide of which 52% is pre-leased. Several projects have pushed completion dates into the second quarter of 2016, including Dropbox and Splunk's new buildings on Brannan Street, and the fully available speculative office building at 500 Pine Street.

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New Leasing Activity

New leasing activity totaled 1.1 msf in the first quarter, down from 2.2 msf recorded in Q1 15. The significant leases signed during the quarter were from diverse industries although the top three were all tech firms. The largest transaction of the quarter was the signing of Airbnb's new headquarters at 999 Brannan Street in the Showplace Square/Potrero Hill submarket. They leased the 150,000 sf building previously occupied by Dolby Laboratories. Dolby purchased the property in 1998 and remains the landlord. Quantcast signed a long term lease totaling 95,000 sf at 795 Folsom Street in Yerba Buena. Twilio leased 92,000 sf at 375 Beale with that project now 96% leased. At 600 California Street, WeWork leased 73,000 sf, taking floors 11-17. Last but not least,

AT THE CLOSE OF Q1 16, TENANT REQUIREMENTS AMOUNTED TO 4.6 MSF, DOWN FROM THE 6.5 MSF REPORTED IN Q1 15.

Bain & Company pre-leased 70,000 sf at Salesforce Tower for occupancy in 2017/2018, in what will be a relocation out of 84,000 sf at Embarcadero Center. At the close of Q1 16, active tenant requirements amounted to 4.6 msf, down from the 6.5 msf reported in Q1 15.

Sales Activity

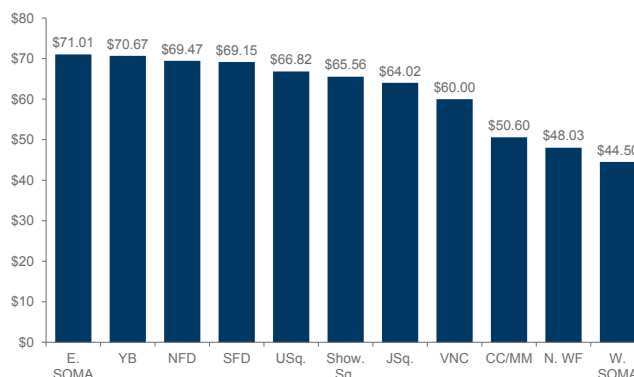
2016 is poised to be a record year for investment office sales. Three sales closed in Q1, totaling 597,000 sf and \$384 MM. JP Morgan Asset Management purchased the 312,000 sf class A office building at 580 California Street from LaSalle Investment Management. Madison International Realty purchased a partial interest in 550 Kearny, a 196,000 sf class B property in the North Financial submarket. And in February, Bridgeton Holdings purchased 995 Market Street, a 91,000 sf building from Long Market Capital Partners. It was recently announced that Pembroke Real Estate was selected as the buyer for 140 New Montgomery Street, which is rumored to be trading close to a record price per foot for San Francisco.

Outlook

- Overall asking rent closed Q1 16 at a record high \$68.44, a 9.9% increase over the past four quarters. Asking rents are forecast to bump up to \$69.45 by year-end.
- The overall vacancy rate is expected to rise 70 bps by year-end 2016 to 6.4%.
- We are tracking 4.4 MSF of under construction office buildings of which 52% is pre-leased. Upcoming deliveries/move-ins include the HQ's of Dropbox and Splunk.

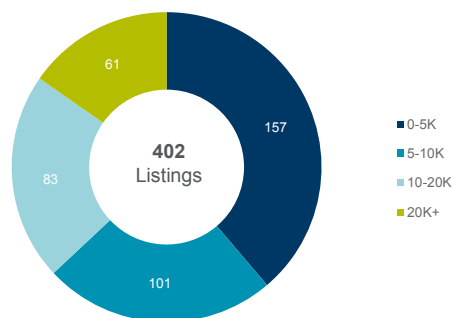
Average Asking Rate by Submarket (Full Service)

EAST SOMA AND YERBA BUENA SURPASSES NFD AND SFD



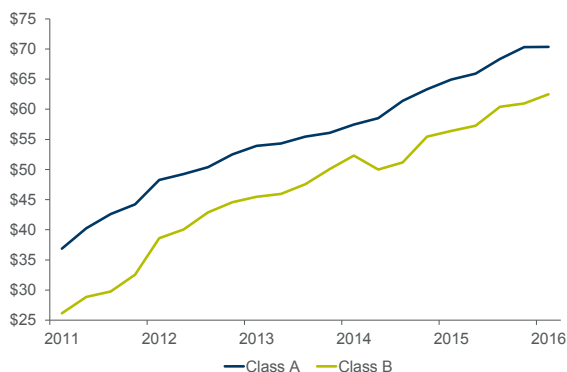
Availabilities by Size Segment

INCREASING SUPPLY OF SPACE UNDER 10K SQUARE FEET



Average Asking Rate by Class (Full Service)

CLASS A RENTS FLATTEN IN FIRST QUARTER



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SUBMARKET	INVENTORY (SF)	SUBLET VACANT (SF)	DIRECT VACANT (SF)	OVERALL VACANCY RATE	CURRENT NET ABSORPTION (SF)	YTD OVERALL NET ABSORPTION (SF)	YTD LEASING ACTIVITY (SF)	UNDER CONSTRUCTION (SF)	OVERALL AVERAGE ASKING RENT (ALL CLASSES)*	OVERALL AVERAGE ASKING RENT (CLASS A)*
North Financial District	25,853,335	280,222	1,794,146	8.0%	(156,800)	(156,800)	435,539	425,000	\$69.47	\$70.05
South Financial District	24,751,356	220,276	969,738	4.8%	612,495	612,495	349,593	2,790,130	\$69.15	\$71.63
CBD	50,604,691	500,498	2,763,884	6.5%	455,695	455,695	782,729	3,215,130	\$69.35	\$70.64
Jackson Sq.	1,490,806	16,348	27,264	2.9%	(10,248)	(10,248)	20,988	0	\$64.02	\$64.44
North Waterfront	3,176,308	15,858	120,850	4.3%	43,468	43,468	113,086	0	\$48.03	\$56.04
East SOMA	4,306,970	86,193	196,335	6.6%	33,600	33,600	23,174	531,845	\$71.01	\$74.38
West SOMA	851,672	0	3,500	0.4%	0	0	0	0	\$44.50	N/A
The Presidio	1,030,627	0	0	0.0%	0	0	0	0	N/A	N/A
Union Square	3,173,989	21,770	105,995	4.0%	(53,029)	(53,029)	18,191	0	\$66.82	\$63.55
Van Ness Corridor	785,956	0	14,188	1.8%	(975)	(975)	0	0	\$60.00	\$60.00
Showplace Square / Potrero Hill	3,111,042	80,864	88,878	5.5%	(53,319)	(53,319)	0	0	\$65.56	\$66.14
Mission Bay	1,056,735	0	0	0.0%	0	0	0	680,000	N/A	N/A
Yerba Buena	3,108,383	42,284	150,590	6.2%	(28,970)	(28,970)	118,774	0	\$70.67	\$69.75
Civic Center / Mid-Market	3,159,668	58,486	16,469	2.4%	(27,544)	(27,544)	55,380	0	\$50.60	\$50.60
Third Street Corridor	349,465	N/A	N/A	N/A	N/A	N/A	N/A	0	N/A	N/A
TOTAL	76,206,312	822,301	3,487,953	5.7%	358,678	358,678	1,132,322	4,426,975	\$68.44	\$70.33

*Rental rates reflect full service asking \$psf/year

OFFICE CLASS BREAKDOWN										
Class A	52,544,536	627,520	2,648,416	6.2%	493,555	493,555	822,001	3,897,743	\$70.33	
Class B	16,044,208	165,091	577,961	4.6%	(178,742)	(178,742)	215,019	529,232	\$62.48	
Class C	7,617,568	29,690	261,576	3.8%	43,865	43,865	95,302	0	\$58.68	

Key Lease Transactions Q1 2016

PROPERTY	SF	TENANT	LANDLORD	TRANSACTION TYPE	SUBMARKET
999 Brannan Street	150,000	Airbnb	Dolby Laboratories	New Lease	Showplace Square
795 Folsom Street	95,000	Quantcast	ASB Capital Management	New Lease	Yerba Buena
375 Beale Street	92,000	Twilio	MTC	New Lease	South Financial District
600 California Street	73,000	WeWork	MEPT	New Lease	North Financial District
415 Mission Street	69,000	Bain & Company	Boston Properties / Hines	New Lease	South Financial District
343 Sansome Street	60,000	Airwave	Yahoo	Sublease	North Financial District

Key Sale Transactions Q1 2016

PROPERTY	SF	BUYER	SELLER	PRICE / \$PSF	SUBMARKET
580 California Street	312,355	JP Morgan Asset Mgmt.	LaSalle Investment Mgmt.	\$218,000,000 / \$698	North Financial District
550 Kearny Street*	196,630	Madison International	Brickman	\$103,700,000 / \$527	North Financial District
995 Market Street	91,308	Bridgeton Holdings	Long Market Property Partners	\$62,000,000 / \$679	Yerba Buena

*Partial interest 90% sale

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Office Submarkets

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