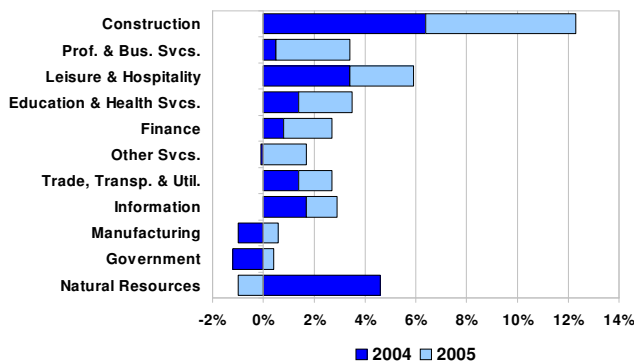


## The Economy

- The West Coast (CA, OR, WA) economy is one of the main sources of growth nationwide, adding more than 340,000 jobs in the year ended May 2005, more than any region besides the South Atlantic (see table on right). The annual growth rate in May was 1.8%, compared to 1.5% for the nation and second only to the Mountain States' growth rate of 3.3%.
- Within the West Coast region, growth in Washington has accelerated during 2005, while job growth in California and Oregon has recently been somewhat slower than in mid- to late-2004.
- The main growth sectors in the West Coast economy are Construction, Professional & Business Services, and Leisure & Hospitality (see graph below). The strong housing market is the main source of the construction sector gains. Temporary hiring is one of the sources of growth in the Professional & Business Services sector, and is a leading indicator of demand for office space.

West Coast Employment Growth By Sector as of May, Ranked by 2005 Growth



Source: Bureau of Labor Statistics

## Metropolitan Areas

- Among major metro areas, Seattle is the fastest growing (2.5% year-to-year gain in May), followed by Tacoma, Bakersfield and Portland (see table on next page). Growth in the Central Valley has increased slightly from its pace a year ago, while growth in Southern California has slowed somewhat from its pace in 2004. Northern California is growing slowly, with slight job losses in Silicon Valley since May 2004.

## Regional Employment Growth Trailing 12-Months as of May 2005

|                    | Percent    | Jobs (000s)  |
|--------------------|------------|--------------|
| United States      | 1.5        | 2,013.0      |
| Midwest            |            |              |
| East North Central | 0.4        | 92.2         |
| West North Central | 1.1        | 109.6        |
| Northeast          |            |              |
| Middle Atlantic    | 1.0        | 185.1        |
| New England        | 0.9        | 65.4         |
| South              |            |              |
| East South Central | 1.1        | 82.9         |
| South Atlantic     | 1.6        | 398.3        |
| West South Central | 1.2        | 165.9        |
| West               |            |              |
| Mountain           | 3.3        | 294.8        |
| Pacific            | 1.8        | 362.0        |
| <b>West Coast</b>  | <b>1.8</b> | <b>341.9</b> |

Source: Bureau of Labor Statistics

- Northern California shows the greatest improvement in the rate of increase, adding 13,500 jobs during May 2004-2005, as compared with a loss of 32,600 jobs during May 2003-2004.
- Smaller cities are among the fastest-growing areas in percentage terms. Areas such as El Centro CA, Mount Vernon WA, and Bend OR are growing rapidly, by 7.1%, 5.8% and 4.9%, respectively.
- The bulk of job gains, however, is in the largest metropolitan areas, which have contributed more than half of the jobs added in the last year in the West Coast region.

## Employment Sectors

- Some of the key industries are growing:
  - *Semiconductor manufacturing* is growing in San Jose, Portland, Sacramento and Orange County, driven in part by strong demand for semiconductors in a broad range of consumer goods.
  - The *information* sector is growing in the San Jose metropolitan area. Google has been hiring and has shown a strong appetite for space in the Mountain View submarket.
  - *Aerospace manufacturing* is driving growth in Seattle, and is also adding jobs in Portland and Los Angeles.
  - San Francisco's *finance* sector is growing.

### Employment Growth - Major West Coast Metro Areas May 2005

| Metro Area          | <u>2005 vs. 2004</u> |             | <u>2004 vs. 2003</u> |             |
|---------------------|----------------------|-------------|----------------------|-------------|
|                     | Percent              | Jobs (000s) | Percent              | Jobs (000s) |
| Seattle             | 2.5                  | 33.8        | 0.8                  | 11.2        |
| Tacoma              | 2.2                  | 5.5         | 2.9                  | 7.2         |
| Bakersfield         | 2.1                  | 4.4         | 2.0                  | 4.2         |
| Portland            | 2.0                  | 18.7        | 2.0                  | 18.8        |
| Stockton            | 1.8                  | 3.6         | 2.1                  | 4.2         |
| Spokane             | 1.6                  | 3.2         | 1.0                  | 1.9         |
| Riverside-San Bern. | 1.6                  | 18.6        | 5.3                  | 57.6        |
| Fresno              | 1.5                  | 4.3         | 1.3                  | 3.8         |
| Sacramento          | 1.4                  | 12.2        | 1.1                  | 9.5         |
| Orange County       | 1.4                  | 19.8        | 2.6                  | 36.7        |
| San Diego           | 1.3                  | 16.2        | 1.7                  | 20.6        |
| San Francisco       | 0.8                  | 7.1         | -1.6                 | -15.7       |
| Oakland             | 0.8                  | 7.9         | -0.4                 | -4.5        |
| Los Angeles         | 0.6                  | 23.2        | 0.3                  | 11.5        |
| Oxnard-Ventura      | 0.6                  | 1.6         | 0.2                  | 0.6         |
| San Jose            | -0.2                 | -1.5        | -1.4                 | -12.4       |

Source: Bureau of Labor Statistics

- *Professional & business services* employment is growing in Southern California (Los Angeles, Riverside and Orange County) and the Northwest (Portland and Seattle). Temporary employment is a large component of this hiring, possibly a leading indicator for permanent hiring and more office net absorption to come.
- The *leisure and hospitality* sector is adding jobs in Los Angeles, San Diego and Oakland. Orange County surged last year, and has been relatively flat since then.

### Single Family Residential

- The West Coast single family residential markets have been among the fastest-growing in the nation, posting high rates of appreciation, despite the already high price of housing. Most housing markets in the West have shown double-digit appreciation in the last year.
- Four California areas - Riverside-San Bernardino, Sacramento, Los Angeles and San Diego - were in the list of top 20 U.S. markets for median home price growth in the first quarter 2005, according to data from the National Association of Realtors.

- The strongest home price growth has generally been in California's Central Valley, according to data from Freddie Mac (see table below). Bakersfield topped the list, with 33% price growth between the first quarter of 2004 and 2005.
- Southern California markets have also experienced strong price appreciation, with price increases mostly in the 20% to 30% range. Price appreciation has accelerated in Northern California, approaching 20% in some of the larger markets.
- Appreciation in the Pacific Northwest has increased, with year-over-year appreciation mostly in the 10% to 15% range.

### Home Price Gains As of 1Q 2005

| Metropolitan Area              | <u>Annualized Growth</u> |        |
|--------------------------------|--------------------------|--------|
|                                | 1-year                   | 2-year |
| Bakersfield, CA                | 33.1%                    | 25.8%  |
| Visalia-Tulare-Porterville, CA | 29.8%                    | 22.5%  |
| Salinas, CA                    | 28.3%                    | 20.9%  |
| Riverside-San Bernardino, CA   | 27.9%                    | 25.2%  |
| Stockton-Lodi, CA              | 26.9%                    | 19.8%  |
| Fresno, CA                     | 25.7%                    | 24.3%  |
| Los Angeles-Long Beach, CA     | 24.7%                    | 22.6%  |
| Modesto, CA                    | 24.4%                    | 19.7%  |
| Sacramento, CA                 | 24.3%                    | 19.8%  |
| Santa Barbara, CA              | 24.2%                    | 20.0%  |
| San Diego, CA                  | 23.4%                    | 20.8%  |
| Yolo, CA                       | 22.7%                    | 18.6%  |
| Ventura, CA                    | 22.5%                    | 21.6%  |
| Orange County, CA              | 22.0%                    | 20.8%  |
| San Luis Obispo, CA            | 21.1%                    | 17.1%  |
| Vallejo-Fairfield-Napa, CA     | 20.0%                    | 16.8%  |
| Oakland, CA                    | 19.5%                    | 14.0%  |
| Santa Rosa, CA                 | 18.9%                    | 15.0%  |
| Bellingham, WA                 | 18.7%                    | 15.8%  |
| San Francisco, CA              | 17.1%                    | 11.7%  |
| Santa Cruz-Watsonville, CA     | 15.2%                    | 11.0%  |
| Bremerton, WA                  | 14.5%                    | 11.9%  |
| San Jose, CA                   | 14.4%                    | 8.9%   |
| Eugene-Springfield, OR         | 14.3%                    | 9.9%   |
| Tacoma, WA                     | 13.8%                    | 10.8%  |
| Olympia, WA                    | 13.3%                    | 10.8%  |
| Spokane, WA                    | 12.4%                    | 8.6%   |
| Portland-Vancouver, OR         | 11.8%                    | 9.3%   |
| Seattle-Bellevue-Everett, WA   | 11.1%                    | 8.7%   |
| Salem, OR                      | 8.5%                     | 6.7%   |

Source: Freddie Mac

- Despite the strong demand for housing and sharp appreciation increases, the pace of single family residential construction has not increased significantly in most West Coast markets. In fact, for the largest markets, activity year-to-date through May 2005 was off slightly from the pace through May 2004.

**Multifamily Residential**

- Many West Coast apartment markets are healthy or improving, and owners began to report positive NOI growth in 2004 for the first time in several years.
- Apartment vacancies in Southern California are in the 4% range, which are the lowest on the West Coast (see table below). These areas have benefited from undersupply of housing and a healthy economy that has created an expanding population base and higher demand for all types of housing. Rent growth was a healthy to strong 5% to 6% in many parts of Southern California between the first quarters of 2004 and 2005. West Los Angeles, the location of significant commercial leasing activity, posted an exceptionally strong 9.4% gain in rents as new luxury properties came to market. Los Angeles and San Diego lead the West Coast in multifamily construction permit activity for both apartments and condominiums.

**Apartment Market Conditions - West Coast  
1Q 2005**

| Market                     | Vacancy Rate | Rent Growth |       |
|----------------------------|--------------|-------------|-------|
|                            |              | 2005        | 2004  |
| <i>Southern California</i> |              |             |       |
| San Diego                  | 4.8%         | 2.8%        | 3.4%  |
| Orange County              | 4.7%         | 4.6%        | 3.7%  |
| Inland Empire              | 4.4%         | 5.8%        | 7.1%  |
| Los Angeles-South          | 3.7%         | 4.9%        | 5.2%  |
| L.A.-North / Ventura       | 4.1%         | 4.5%        | 4.3%  |
| West Los Angeles           | 4.0%         | 9.4%        | 2.9%  |
| <i>Northern California</i> |              |             |       |
| Oakland/East Bay           | 5.5%         | 0.1%        | -3.4% |
| South Bay                  | 5.2%         | -0.3%       | -4.8% |
| Sonoma/Napa/Solano         | 7.0%         | 1.6%        | 1.5%  |
| Sacramento                 | 7.6%         | 2.0%        | 2.8%  |
| Central Valley             | 5.9%         | 3.8%        | 1.9%  |
| <i>Pacific Northwest</i>   |              |             |       |
| Seattle-Tac.-Bellevue      | 7.3%         | 0.9%        | -0.8% |
| Portland                   | 6.9%         | 0.9%        | -2.0% |
| Spokane                    | 5.4%         | 5.0%        | 3.7%  |
| Salem                      | 4.4%         | 2.4%        | 0.6%  |

Source: Hendricks & Partners

- Northern California was harder hit by the 2000-2001 economic downturn, and it is recovering more slowly than Southern California. Northern California apartment vacancy rates are mostly in the 5% to 6% range. Rents have bottomed out and concessions have diminished, but rents are not yet growing in most Northern California markets.

- Parts of the Pacific Northwest, including the Puget Sound area and Portland have vacancies in the 7% range. Although vacancy is relatively high, it has decreased, and rent growth is positive, but slow.

- Investment activity is strong throughout the West Coast, and apartment cap rates are exceptionally low, largely because investors purchasing apartments with the intention of converting them into condominiums can pay more for the units than those who will maintain their use as apartments. San Diego, Los Angeles and San Francisco are among the top markets for condominium conversion activity, according to Real Capital Analytics.

**Office Sector**

- Renewed employment growth in most West Coast markets has generated increased demand for office space. Vacant shadow space is being absorbed, and in some cases, job creation is generating net new demand for office space.

- In many cases, Class A CBD vacancy rates have fallen substantially during the past twelve months and are well below the vacancy rate for lower quality space (see table below). In several markets, the Class A

**CBD Office Market Conditions - West Coast  
1Q 2005**

| Market             | Vacancy Rate |       |           |         |               |
|--------------------|--------------|-------|-----------|---------|---------------|
|                    | Class A      |       | Class B/C | Class A | Annual Change |
|                    | 1Q 04        | 1Q 05 | 1Q 05     | Rent    |               |
| Bellevue, WA       | 19.9%        | 7.4%  | 13.0%     | \$24.39 | 2.9%          |
| Oakland, CA        | 15.5%        | 8.0%  | 19.1%     | \$26.99 | 1.3%          |
| Orange County, CA  | 15.9%        | 9.3%  | 13.2%     | \$29.78 | 4.3%          |
| Portland, OR       | 13.2%        | 9.6%  | 16.3%     | \$22.69 | -2.4%         |
| Seattle, WA        | 14.3%        | 12.6% | 16.8%     | \$27.10 | -3.0%         |
| Los Angeles, CA    | 18.1%        | 16.0% | 18.2%     | \$26.91 | -0.3%         |
| San Francisco, CA  | 19.3%        | 16.7% | 15.2%     | \$31.20 | 1.2%          |
| Silicon Valley, CA | 29.0%        | 27.8% | 22.3%     | \$30.77 | -7.1%         |

Source: Cushman & Wakefield

### Non-CBD Office Market Conditions - West Coast 1Q 2005

| Market                  | Cl. A Vacancy Rate |       | Rent    | Rent Growth |
|-------------------------|--------------------|-------|---------|-------------|
|                         | 1Q 04              | 1Q 05 |         |             |
| Los Angeles-North       | 12.1%              | 8.0%  | \$26.17 | 1.9%        |
| Orange County           | 11.7%              | 8.8%  | \$25.26 | 1.7%        |
| Los Angeles-Tri-Cities  | 14.1%              | 11.2% | \$28.79 | 1.2%        |
| Bellevue, WA            | 16.4%              | 12.1% | \$23.21 | 3.1%        |
| Los Angeles-West        | 18.8%              | 12.5% | \$33.51 | 0.8%        |
| Contra Costa            | 19.4%              | 15.8% | \$25.05 | -2.5%       |
| Los Angeles             | 19.9%              | 15.9% | \$21.18 | 5.7%        |
| Portland                | 22.3%              | 16.4% | \$21.01 | 0.8%        |
| Los Angeles-South       | 17.1%              | 16.8% | \$23.58 | -4.6%       |
| Silicon Valley          | 27.6%              | 18.7% | \$24.59 | 0.0%        |
| Ontario                 | 8.8%               | 19.0% | \$22.83 | 0.7%        |
| Seattle                 | 31.2%              | 25.0% | \$20.17 | 0.0%        |
| San Francisco           | 35.9%              | 26.7% | \$23.76 | -8.3%       |
| Oakland                 | 31.7%              | 28.4% | \$24.63 | 1.6%        |
| San Francisco Peninsula | 32.7%              | 29.6% | \$25.17 | -7.2%       |

Source: Cushman & Wakefield

market is significantly tighter than that for Class B/C space. Positive rent growth has resumed in some CBD markets. As this trend continues, we expect to see either upgrading of B/C space or conversion to other uses, such as condominiums.

- The trends for non-CBD space are not as readily apparent; vacancies have not fallen substantially in the majority of the markets, nor is the Class A market notably stronger than that for lower quality space (see table above). The exceptions are Los Angeles (most submarkets except for the South), Orange County and Bellevue, all of which have shown significant improvement in Class A vacancy rates, and positive rent growth.
- San Francisco and San Jose are beginning to experience positive net absorption, although vacancy rates are still above equilibrium in these markets. Rents for high quality view space are in the \$60 per square foot range, which is the highest level in recent years. Improving economic conditions will likely lead to continued net absorption, though recovery is probably still at least a couple years away.
- Despite sometimes weak office market fundamentals, office investment activity is strong throughout the West Coast because of the significant amount of capital chasing deals and low interest rates. Buildings have been purchased at record prices of more than \$400 per square foot. In San Francisco, American Assets is purchasing One Market for about \$500

per square foot and is purchasing 160 King Street for \$400 per square foot.

### Warehouse Sector

- West Coast warehouse markets are holding steady, fueled by population growth, port expansion, and the U.S. post-9/11 defense ramp-up.
- Tight conditions prevail in Southern California. Vacancy rates in the Los Angeles area are in the 2% to 3% range, according to Cushman & Wakefield, and vacancy rates in Orange County have declined to 5% (see table below).
- Seattle and San Francisco have tightened significantly, leading to rent growth.
- With the exception of San Francisco, Northern California is experiencing higher than average vacancies and generally soft rent conditions.
- As the Northern California and Pacific Northwest economies continue to recover, trade and demand for warehouse space in these areas should increase.

### Warehouse Market Conditions - West Coast 1Q 2005

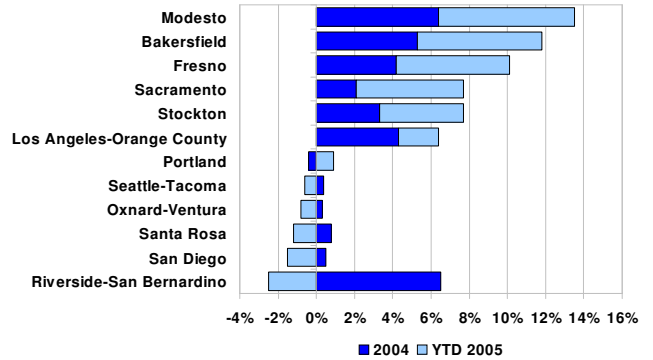
| Metro Area              | Vacancy Rate |         | Rent   | Annual Change |
|-------------------------|--------------|---------|--------|---------------|
|                         | 1Q 2004      | 1Q 2005 |        |               |
| Los Angeles-South, CA   | 4.3%         | 2.0%    | \$0.53 | 1.3%          |
| Los Angeles, CA         | 2.8%         | 2.8%    | \$0.46 | 1.1%          |
| Los Angeles-North, CA   | 3.3%         | 3.4%    | \$0.62 | 6.9%          |
| Orange County, CA       | 8.4%         | 5.0%    | \$0.55 | 4.8%          |
| San Fran. Peninsula, CA | 8.4%         | 5.2%    | \$0.73 | 3.4%          |
| Seattle, WA             | 8.9%         | 6.6%    | \$0.38 | 5.6%          |
| Ontario, CA             | 8.7%         | 6.9%    | \$0.36 | -9.2%         |
| Portland, OR            | 9.6%         | 8.8%    | \$0.36 | 1.9%          |
| Oakland, CA             | 8.9%         | 10.4%   | \$0.37 | -2.9%         |
| Contra Costa, CA        | 10.1%        | 10.4%   | \$0.56 | -4.4%         |
| Bellevue, WA            | 14.9%        | 11.2%   | \$0.62 | 0.0%          |
| Napa/Solano, CA         | 13.2%        | 13.0%   | \$0.42 | 8.1%          |
| Silicon Valley, CA      | 15.5%        | 15.3%   | \$0.43 | -3.4%         |
| Weighted Average        | 6.3%         | 5.3%    | \$0.47 | 0.6%          |

Source: Cushman & Wakefield

**Retail Sector**

- Retail sales growth in the California Central Valley is strong, driven by general economic growth and strong population growth (see graph to the right).
- Department store sales growth in the Inland Empire has slowed in 2005, after very strong growth in 2004. Growth will likely resume in the second half of 2005.
- The retail sector has been one of the strongest performers for institutional investors in recent years. Continued economic and population growth will be positive trends for retail real estate performance during the next several years.

Department Store Sales Growth  
May 2005 vs. Calendar Year 2004



Source: ICSC

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