

OFFICE

Seattle Real Estate Market Review

King, Snohomish and Pierce Counties

1st Quarter 2008

Seattle's office market begins 2008 singled out as the strongest in the nation in terms of supply and demand stability dynamics and anticipated rent growth. While the national economic news is troubling, the Seattle economy is outperforming the nation. Even with some moderation expected, there is no sign that property values or rental rates will be significantly affected. Sales activity has slowed from the torrid pace of 2007, but deals are being made. First quarter leasing activity has also slowed, due in part to the limited inventory of large blocks of space in the Seattle and Bellevue CBDs.

The region recorded modest absorption in the first quarter, with encouraging strength in the South King County market. The result was a minor drop in the regional vacancy rate to 8.41%. Just underneath the flat numbers, there are a number of deals in the works but tenants appear to be taking more time in due diligence. Part of this is a reflection of the slowing economy, part is the re-analysis of requirements in light of rental rates that increased as much as 40% over the past two years. Near-term, the economy is expected to moderate, following but not equaling the declining national trend. Tenants in the Technology sector are a major exception in the market, exhibited by Microsoft, Google and Expedia.com, pre-leasing a combined 2,200,000 s.f. on the Eastside in the past year. The traditional businesses that are predominant in the Seattle CBD have not yet shown the same need for additional space. Currently, 6,730,152 s.f. is under construction in the region, most of which is located in the Seattle and Bellevue CBDs. Nearly half of that is pre-leased, including almost all of the space underway in the tight Eastside market. Tenants will continue to feel the pressure as rental rates in the best locations are expected to continue to increase.

VACANT SPACE/VACANCY RATE

The amount of vacant space in the Seattle office market decreased by 294,871 s.f. during the first quarter of 2008. This tenuous performance came as

the national economic news and wildly fluctuating stock market brought about caution on the part of many businesses. The absorption was also affected by the lack of larger vacancies in both of the CBD markets. The overall vacancy rate declined slightly from 8.53% at the end of 2007 to 8.41% at the end of the first quarter. Looking forward, the rate is expected to continue downward through 2008, with projections of job growth only slightly lower than 2007 and no major deliveries of new inventory until 2009. One positive side of the turmoil in the financial markets is that it will stall many proposed projects, limiting the potential of significant overbuilding as the market moves through this part of the cycle.

NEW CONSTRUCTION ACTIVITY

The first quarter of 2008 saw work continuing on 14 office projects in Close-In Seattle markets and four in the Bellevue CBD, including Bentall's recently started Summit III building. Pre-leasing in the Seattle product is less than 5% of the total, after backing out two build-to-suit projects. The first significant deliveries will take place in the third quarter of this year. In the Bellevue market, Tower 333 will be delivered next quarter, fully leased by Expedia.com. City Center II will be next, expected mid-year. It has not yet announced any pre-leasing, and rumors of Microsoft taking a major portion of the building are starting to lose some certainty. All told, there is currently over 6,730,000 s.f. under construction in the region, spikes of delivery

Market ^{Up} Close

- The Puget Sound regional economy is expected to outperform the national economy and institutional investors have placed the region's office market at the top of their lists. A healthy technology sector continues to propel demand for space, particularly in the Eastside market.
- The first quarter was relatively quiet with about 300,000 s.f. absorbed and vacancy inching down to 8.41%. While the number of deals in negotiation is encouraging, the pace is more cautious than a year ago. Rent growth continues, but has slowed as the market stabilizes.
- Space under construction pushes past the 7,000,000 s.f. mark with ground breaking for the Summit III tower in the Bellevue CBD and the first buildings in the Amazon.com South Lake Union campus. About a third of the total under construction is pre-leased.

2007 GVA Kidder Mathews Results

- \$2.5 Billion Total Transaction Volume
- 14 Million SF Leasing Transactions
- 11 Million SF Sales Transactions
- 22 Million SF Under Management
- 900 Valuation Assignments

SUB-MARKET STATISTICS

	Seattle	South King County	East King County	Snohomish County	Pierce County	Overall Seattle Office Market
Market Size	in sq. ft.	in sq. ft.	in sq. ft.	in sq. ft.	in sq. ft.	Summary
4/1/08	61,060,921	16,836,136	40,167,760	17,264,593	14,293,611	149,623,021
1/1/08	61,060,921	16,805,754	40,167,760	17,227,693	14,223,335	149,485,463
1/1/07	60,331,691	16,653,412	39,501,631	16,583,462	14,099,306	147,169,522
1/1/06	59,083,183	16,614,666	39,691,051	16,399,245	13,909,964	145,698,109
Vacant Space						
4/1/08	4,672,071	1,860,600	2,119,844	2,405,040	1,531,169	12,588,724
1/1/08	4,780,977	2,078,520	2,100,211	2,429,375	1,356,954	12,746,037
1/1/07	5,046,743	2,206,251	2,216,602	1,939,490	1,305,260	123,714,346
1/1/06	6,697,660	2,632,467	2,985,690	1,797,213	1,310,848	15,423,878
Vacancy Rate						
4/1/08	7.65%	11.05%	5.28%	13.93%	10.71%	8.41%
1/1/08	7.83%	12.37%	5.23%	14.10%	9.54%	8.53%
1/1/07	8.36%	13.25%	5.61%	11.70%	9.26%	8.64%
1/1/06	11.34%	15.84%	7.52%	10.96%	9.42%	10.59%
Under Construction						
4/1/08	3,664,408	269,133	2,609,848	65,987	120,776	6,730,152
1/1/08	3,664,408	299,502	2,609,848	102,887	191,052	6,867,697
1/1/07	1,650,727	132,945	2,571,428	525,359	239,301	5,119,760
1/1/06	1,248,000	0	42,994	45,422	16,925	1,353,341
Absorption						
First 1/4 of 2008	108,906	248,302	-19,633	61,235	-103,939	294,871
All of 2007	994,996	280,073	782,520	154,326	72,335	2,284,250
All of 2006	2,899,425	464,962	579,668	41,960	194,930	4,180,945
All of 2005	599,731	577,693	1,243,985	215,669	630,369	3,267,447

are expected in mid-2008 and late 2009. Overall, the pre-leasing is about 30% of this total.

RENT FORECAST

After jumping up by as much as 40% in 2007, rental rates were relatively flat over the last quarter. Asking rates did move up slightly, but the limited number of signed deals gave little evidence of their achievement. Rates continued to firm up in South King County as a value location in comparison to the Eastside and Seattle markets. The projection is for rates to be fairly stable in most areas, although the Bellevue and Kirkland submarkets are expected to outperform the regional market.

SEATTLE CBD/SURROUNDING AREA REVIEW

The Downtown CBD submarket vacancy rate dipped to 7.65%

in the first quarter. Construction continues on 14 office projects, including breaking ground for the first buildings in the Amazon.com campus in South Lake Union. The major speculative projects are yet to announce any preleasing; the stabilizing market should give tenants and developers a better feel of what market rent should be for the space that will start being delivered in about six months. One potential challenge for the Seattle CBD market is the instability of Washington Mutual, whose 900,000 s.f. headquarters tower might become available if they were acquired. Lease rates have moved above \$40/s.f./year, fully serviced, for Class A buildings in Seattle and Bellevue CBD markets. These rates have caused some tenants to consider the perimeter markets, and others are taking a careful look at their space needs.

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