



Colliers International Silicon Valley

OVERVIEW

First Quarter - 2006 Market Report



April 2006

The first quarter produced the largest single-quarter occupancy gain for Silicon Valley since the dot-com explosion. Colliers measured positive net absorption of 3.13 million square feet in Q1. The big quarter was partially attributable to another 6.27 million square feet of gross absorption, marking the eleventh straight quarter of gross absorption in excess of six million square feet.

Q1

BIG Q1 NET ABSORPTION GAIN

In 2005, Colliers documented a trend that showed that less and less space was coming available as a result of tenants moving out of previously occupied space. In fact, less space was vacated in 2005 than any year dating back to 1998. This trend led us to forecast that 2006 would be a solid net absorption year for Silicon Valley.

So far, much of that forecast is ringing true for 2006. In fact, the first quarter produced the largest single-quarter occupancy gain for Silicon Valley since the dot-com explosion. Colliers measured positive net absorption of 3.13 million square feet in Q1. The big quarter was partially attributable to another 6.27 million square feet of gross absorption, marking the eleventh straight quarter of gross absorption in excess of six million square feet. At the same time, only 2.62 million square feet was vacated in Q1, and that combination led to big occupancy gains for Q1.

Our expectation is that net absorption will not continue in 2006 at the pace measured in Q1. For one, there was a significant amount of space that came available in the first quarter that has not been vacated yet. As a result, while Q1 net absorption was high, the overall availability rate only dropped from 17.2% to 16.9%. As that Q1 available space gets vacated, it will generate more occupancy loss to offset whatever occupancy gains are measured in Q2. Nonetheless, the trend for the year is still ahead of Colliers' forecast for total net absorption of 6-7 million square feet.

The economic, big picture still looks pretty good for Silicon Valley. Venture capital investment was up 4.8% over the same quarter last year, a 15% gain. According to Dow Jones VentureOne, \$1.9 billion was invested in local companies in the year's first quarter. In addition, Silicon Valley employment figures continue to provide a slow, but steady, boost to the commercial real estate market. Santa Clara County employment increased by 3,800 jobs from February to March, and the unemployment rate declined from 5.1% to 4.8%. Industrial production continues to clip along at a pretty good pace as well. The March increase was 0.6% and the annualized rate for Q1 stands at 4.5%. All in all, the economy is holding up its end of the bargain, laying the foundation for business growth in Silicon Valley.

FIGURE 1
Silicon Valley
Gross Absorption

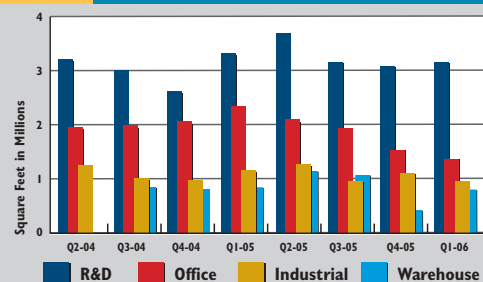
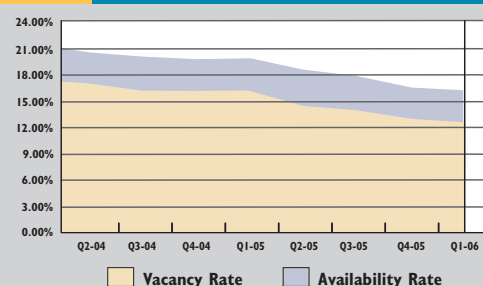


FIGURE 2
Silicon Valley
Availability



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Net absorption of R&D space totaled 1.80 million square feet in the year's first quarter. R&D available inventory was reduced by 1.0 million square feet and the R&D availability rate dropped from 21.16% to 20.55% during the quarter.

R&D Market

The momentum that built in 2005, sustained itself through the first quarter of 2006 in the R&D sector. Gross absorption of R&D space measured 3.29 million square feet in the first quarter, continuing a five-quarter trend during which R&D gross absorption has hovered between 3.08 and 3.64 million square feet. R&D gross absorption was up 6.8% from the results posted in the final quarter of 2005.

Net absorption of R&D space totaled 1.80 million square feet in the year's first quarter. R&D available inventory was reduced by 1.0 million square feet and the R&D availability rate dropped from 21.16% to 20.55% during the quarter. Presently, there is still 32.69 million square feet of R&D space available, a figure that is down 5.24 million square feet in the last year. Colliers forecasted that the R&D availability rate would drop below 20% in the first half of 2006, and that still appears to be in the cards for Q2.

Activity levels were solid in each of the five cities boasting the Valley's largest R&D building bases. San Jose, which came off a huge fourth quarter, generated 599,995 square feet of R&D gross absorption, the lowest level of activity since the third quarter of 2004. R&D gross absorption was also down in Mountain View, from the 440,578 square feet recorded in Q4 2005, to 293,580 square feet in Q1 2006. Activity levels were up from the prior quarter in Santa Clara, Sunnyvale, and Fremont.

Milpitas, which does not have one of the five largest R&D building bases, boasted the largest R&D deal of the quarter. SanDisk subleased 288,250 square feet on McCarthy Boulevard and Sumac Drive. Other significant R&D transactions included Alps' 175,998 square foot purchase on Wolfe Road in Sunnyvale, Asyst Technologies' 95,939 square

foot lease on Bayside Parkway in Fremont, and Symantec's lease of 166,834 square feet on Whisman Road in Mountain View.

The average start rate for R&D transactions dropped to \$0.79 per square foot (NNN) in the first quarter, down \$0.10 per square foot from the prior quarter, but only \$0.03 per square foot from Q3 2005. This is certainly not a sign of any downward pressure on rents and we expect that the Q2 figure will rebound.

Office Market

Silicon Valley's office market generated mixed results during the year's first quarter. Gross absorption totaled 1.38 million square feet, a decent enough figure, but still the lowest since the second quarter of 2003. Office net absorption was a robust 724,913 square feet, the most since the fourth quarter of 2001. However, there was relatively large amount of occupied office space that came on the market in Q1 (1.15 million square feet) and Colliers anticipates that much of this space will have a negative impact on office occupancy in Q2.

At the end of Q1, the office availability rate stood at 17.5%. That figure represents a 10.9% decline from the 19.6% availability rate one year ago, but it is up slightly from the 17.4% rate that closed out 2005. The general trend is still one of solid activity and positive net absorption.

As with the R&D market, activity was spread amongst Silicon Valley cities in a relatively normal pattern. San Jose and Santa Clara generated most of the office demand, with 365,545 square feet and 416,216 square feet of gross absorption respectively. Santa Clara continues its 2005 trend of being a magnet for office demand. Office net absorption was positive for the fourth straight quarter in Santa Clara, measuring 274,809 square feet. Tellabs was the leading contributor, with its 125,044 square foot lease on Central Expressway.

The average starting rent for office leases in the first quarter was \$1.90 per square foot (full service). Office rents have now exceeded an average start rate of \$1.90 per square foot in each of the last three quarters. While the general trend for office rents is upward, there

FIGURE 3 R&D Availability and Rent Trends

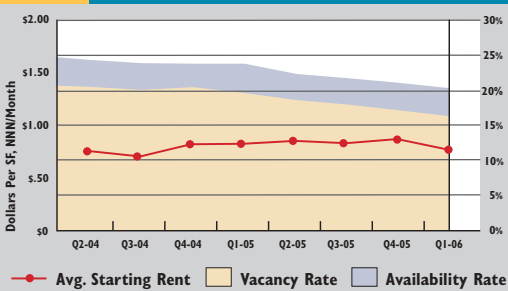
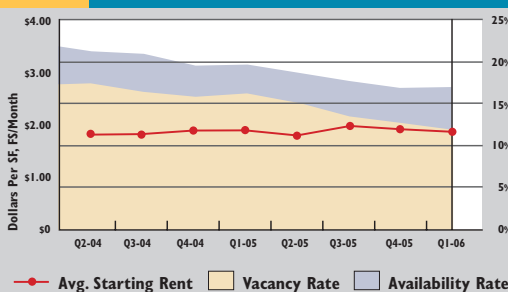


FIGURE 4 Office Availability and Rent Trends





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is less class-A space available than there was one year ago. Consequently, fewer "high-rent" deals are included in our tabulations and that is showing up in our rental statistics as a flattening of office rents.

Industrial Market

Results were also somewhat mixed in the industrial marketplace, where the 859,718 square feet of gross absorption was the lowest recorded quarterly total since the third quarter of 2001. However, the figure was not significantly lower than the 1.0 million square feet that has become commonplace for quarterly industrial leasing, and there are no market dynamics at play that would suggest that industrial leasing and sales activity is on the decline. Industrial net absorption was less than the Q4 2005 results, but the 306,705 square foot occupancy gain was still significant.

San Jose and Santa Clara generated the bulk of the quarter's industrial leasing activity, and the results were consistent with established patterns. San Jose generated 431,662 square foot of industrial gross absorption, almost identical to the results posted in Q4 2005. It was the third straight quarter of gross absorption exceeding 400,000 square feet for San Jose. Santa Clara's industrial gross absorption topped out at 220,680 square feet, a bit less than the preceding quarter, but right in line with activity levels posted over the last several quarters. Fremont posted a very modest, 44,533 square foot of industrial gross absorption in Q1, marking the third straight sub-par quarterly results for that city.

There were not many unusually large industrial leases during the quarter to boost overall results. Source Corporation leased 50,000 square feet on Zanker Road in San Jose. Also in San Jose, Channing Associates sold a 36,358 square foot industrial building on Channing Avenue. Santa Clara's largest industrial transaction was a 45,900 square foot building sale to Extra Space Storage on Scott Boulevard.

The average starting rental rate of industrial leases in the first quarter was \$0.72 per square foot per month (NNN). Industrial starting rents recorded in Q1 are 7.5% higher than rents recorded in the period one year earlier.

Warehouse Market

After posting lackluster results in Q4 of 2005, warehouse gross absorption rebounded nicely in the first quarter of 2006, to 732,359 square feet. That figure is very consistent with the strong warehouse activity levels that have been generated over the last ten quarters. Warehouse net absorption was also a solid, 302,169 square feet.

Warehouse space is rolling over at a similar pace as the Valley experienced in 2005. 829,526 square feet of warehouse space came on the market in Q1, including 606,385 square feet that is still occupied. That additional, pending vacancy may result in some negative warehouse net absorption in Q2.

Warehouse activity levels were strong in all the logical cities. San Jose generated 342,851 square feet of gross absorption, with Fremont contributing 164,283 square feet. Both cities produced warehouse gross absorption that was up from the results posted in Q4 2005. Results in Milpitas and Santa Clara were also improved, but those smaller warehouse markets contributed only 52,164 square feet and 91,786 square feet of warehouse gross absorption respectively.

Significant transactions during the quarter include a 71,296 square foot user sale at 1500 Duane Avenue in Santa Clara, a 66,893 square foot lease by McCollister's Moving & Storage in Fremont, and a 61,340 square foot warehouse lease to InterWorld Networks, also in Fremont.

Warehouse rents remained flat in the first quarter of 2006, at an average starting rental rate of \$0.35 per square foot (NNN). This figure is identical to the average starting rate of Q4 2005 deals and it is largely unchanged from the two-year running average. Our forecast continues to call for relatively flat rents, with an annualized upward trend that will fall short of 10% for the year.

FIGURE 5 Industrial Availability and Rent Trends

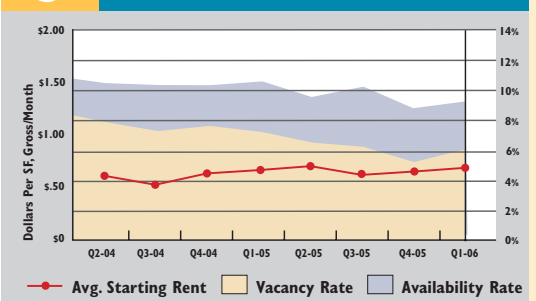
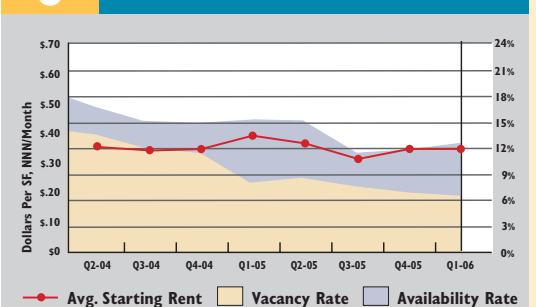


FIGURE 6 Warehouse Availability and Rent Trends



San Jose generated 431,662 square foot of industrial gross absorption, almost identical to the results posted in Q4 2005. It was the third straight quarter of gross absorption exceeding 400,000 square feet for San Jose. Santa Clara's industrial gross absorption topped out at 220,680 square feet.



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the U.S. and abroad.

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SELECTED COLLIERS INTERNATIONAL TRANSACTIONS, Q1 2006

A&B Investments purchased a 71,296 square foot industrial building at 1500 Duane Avenue in Santa Clara from **Melvin Sosnick Company**.

Philips Electronics North America, sold a 150,000 square foot R&D building at 440 Wolfe Road in Sunnyvale to **ALPS**.

InterWorld Network International, Inc., signed a 61,340 square foot warehouse lease at 48541 Warm Springs Boulevard in Fremont, with landlord, **Milpitas Industrial Properties, Inc.**

CarrAmerica Realty Corporation purchased a 85,585 square foot office building at 3553 North First Street in San Jose, from **NetIQ Corporation**.

Apple Computer purchased a 106,690 square foot R&D building at 39800 Eureka Drive in Newark, from **Stream Realty, LP**.

Ultra Pac, Inc., completed a 110,925 square foot warehouse sublease at 2401 Bert Drive in Hollister, with subtenant **Pactiv Corporation**.

Apple Computer inked a long-term, 124,000 square foot R&D lease renewal at 5201 Patrick Henry Drive in Santa Clara, with landlord, **Batton Associates, LLC**.

Carlyle Fortran Trust sold a 77,805 square foot R&D building at 4435 Fortran Court in San Jose, to **Korean Emmanuel Presbyterian Church**.

Hope Forest, LLC, purchased 7.34 acres of land at Murray and Forest Street in Gilroy.
Hope Rehabilitation Services is the seller.

Mission West Properties, LP sold a 95,690 square foot R&D building at 233 South Hillview Drive in Milpitas, to **Sipex Corporation**.

RREEF inked a long term, 66,893 square foot warehouse lease at 45125 Industrial Drive in Fremont, with tenant **McCollister's Moving & Storage of California, Inc.**

UBS Realty Investors completed the sale of Meridian Square, a 163,625 square foot office/retail leased investment project at 4300-4400 Stevens Creek Boulevard in San Jose. **JZM, LLC (ATC Partners)** is the buyer.

Netflix, Inc., inked a long term, 80,000 square foot lease expansion at 100 Winchester Circle in Los Gatos. **Sobrato Land Holdings** is the landlord.

UNDERSTANDING ABSORPTION

Colliers uses several measurements to track market conditions and deal flow. While related, the formulas to arrive at these measurements differ. Using the results of the most recent quarter, here is how Colliers measures change in availability, net absorption and effective net absorption.

Change in Availability: This measurement is simply the difference between the amounts of space available at the end of one period to the next. The table below shows that total available space decreased by 546,768 square feet in the year's first quarter. Note that "change in availability" includes adjustments for space that is "taken off the market". Space "taken off the market" is not a factor in net absorption measurements.

Total Available end of 4Q05	53,359,399
Plus: Vacant & occupied space that came available IQ06	6,067,447
Q4 Available + Newly Available in Q1 =	59,426,846
Less: IQ06 Gross Absorption	-6,268,253
Less: IQ06 Taken off the Market	-345,962
Total Available end of IQ06	52,812,631

Net Absorption: Net absorption measures the change in occupied space from one period to the next. In this measurement, it is important to distinguish that a building may be "available", but not vacant (often the case in a sublease situation, for example). Therefore, occupancy is not reduced (negative net absorption) until the space is vacated, and sometimes that does not happen until the space is leased, creating a net absorption "wash" for the deal and for that particular period.

Vacant space that came available IQ06	-2,650,842
Previously available space that was vacated in IQ06	-483,324
IQ06 Total Vacant Added (occupancy loss)	-3,134,166

IQ06 Gross Absorption (occupancy gain)	6,268,523
IQ06 Net Absorption (change in occupancy)	3,134,357

Effective Net Absorption: In 2003, Colliers created a measurement of "effective net absorption". Effective net absorption uses the same formula as the net absorption formula, except that it treats any space that comes available as if it is vacant, whether it is or it isn't. The purpose of the measurement is to get a better "real time" gauge of occupancy flow in and out of the market, acknowledging that space that is available for lease is likely to be vacated shortly and under utilized presently.

Vacant space that came available IQ06	-2,650,842
Occupied space that came available IQ06	-3,416,605
IQ06 Total Available Added	-6,067,447

IQ06 Gross Absorption	6,268,523
IQ06 Effective Net Absorption	201,076