

COMMERCIAL REAL ESTATE UPDATE

Office Market Presents Opportunities for Upward Mobility

REAL ESTATE: Declining Rents Encourage Tenants to Shop for Upgraded Space

■ By EMMET PIERCE

The current tenants' market for leased office space has created a game of musical chairs among businesses in San Diego County.

Firms routinely vacate their old space to take advantage of less expensive rent, only to be replaced by other companies that also are looking to cut costs. The recession and high unemployment have placed steady downward pressure on office lease and purchase costs.

"It is just tenants changing chairs right now," said David Marino, executive vice president at **Irving Hughes Inc.**, a real estate company that represents tenants. "Most companies are downsizing. The resulting effect is availability is up and it is not going down."

Much of the activity is a result of downsizing or restructuring among existing tenants, said Matt Carlson, a director with **Cushman & Wakefield Inc.**

"There are healthy companies out there that are taking advantage of historically low rents and some of the premier spaces that are out on the market," Carlson said.

Many businesses are using today's low prices to move up to quality space, said Alan Nevin, director of economic research for **MarketPointe Realty Advisors**.

"Often they can get more space for less than what they were paying previously," he explained.

Nevin expects the bargain-hunting to continue into 2010, fueling a flurry of transactions. However, some analysts anticipate an end to the cycle because of rising prices in the year ahead. In order for that to happen, there must be job growth and a reduction in unemployment.

For the present, the values of office properties have declined to the point where builders say it is difficult to rationalize new development. For most investors, it makes more sense to buy existing properties.

"There is really no new private development," said developer Dennis Cruzan, a principal of commercial real estate property company **Cruzan|Monroe**. "It is principally because of the financial markets we are in and a lack of confidence in the economy."

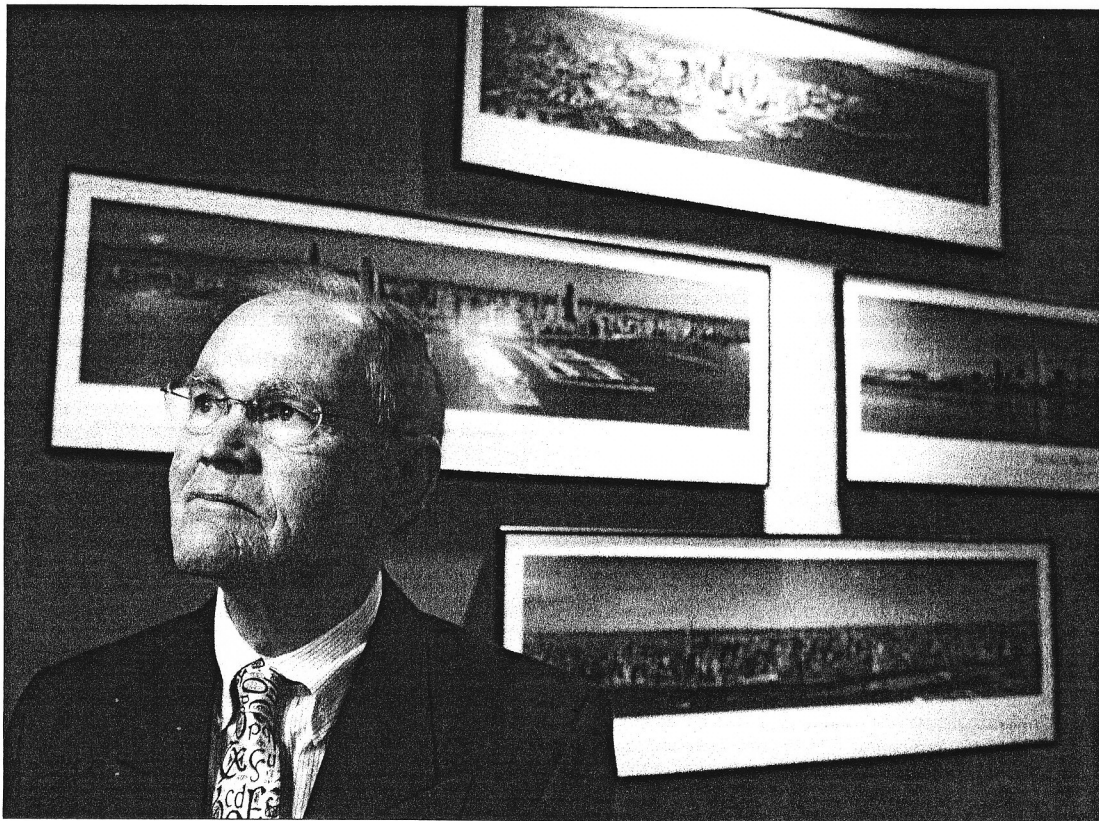
Many real estate professionals still are reeling from the speed at which the market declined during the past two years, said Dan Ryan, a principal at **Veralliance Properties Inc.**, an acquisition and development firm.

"Guys are in shell shock from how quickly the market has deteriorated," Ryan said. "Perhaps 2010 will be the year when color returns to their faces."

Moving Into New Space

The recession has made it difficult to sell or lease new office space, but it's not impossible.

Rich Simons, a partner in **Sudberry Properties Inc.**, said luck and hard work

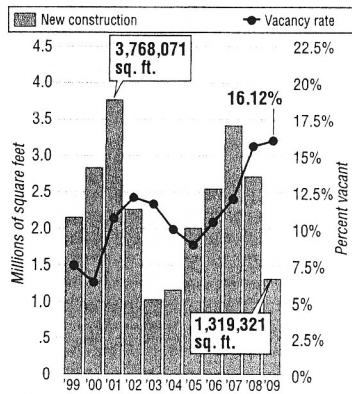


Alan Nevin of MarketPointe Realty Advisors expects the chase for reduced-rate office space will continue this year.

Stephen Whalen

ANNUAL OFFICE NEW CONSTRUCTION VS VACANCY RATE

San Diego County, 1999-2009:



SDBJ graphic

combined with opportunity when the development and asset management firm completed two Class A, six-story office buildings that were built in partnership with Prudential Real Estate.

The Terraces at Copley Point are located near the intersection of state Route 52 and Interstate 805. The buildings encompass 380,000 square feet.

"They took us 18 months to complete," Simons said. "We had built it as a spec project. We leased one whole building to Cricket Communications/Leap Wireless.

We manage the Cricket building."

The other building, which encompasses 175,000 square feet, recently was sold to Kaiser Permanente.

"I think it was location, design and tenacity," Simons said. "Sometimes you get lucky."

The Kaiser transaction represented a purchase at more than \$300 per square foot, said Chris Hobson, a real estate broker with **Grubb & Ellis|BRE Commercial San Diego**. "That was significant."

There have been other bright spots in the marketplace during the past two years, said Nevin. He noted that **Bridgepoint Education Inc.** took over hundreds of thousands of square feet in Sabre Springs and Kearny Mesa in 2009. Global defense and security firm BAE Systems leased about 80,000 square feet at Liberty Station in Point Loma, he added.

Buildings Lose Value

Some analysts were disturbed when Seaview Corporate Center in Sorrento Mesa sold for about \$17 million less than the \$92 million the property sold for in 2004.

"There are huge write-downs in commercial real estate," said Marino. "When you talk about our market, the word on the street is the buildings have lost 30 to 40 percent of their value from the peak a couple of years ago."

Stacey Hansen, a senior property manager at Irvine-based **Essex Realty Management Inc.**, doesn't foresee a quick turnaround.

"I figure there will be see-through buildings for a while," she said. "No occupancy. You see from one window out the other."

Nevin was more hopeful, asserting that some firms will take advantage of low leases and reduced building costs to make new transactions before the economy turns around.

Emmet Pierce is a freelance writer for the *Business Journal*.

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