

San Francisco and Bay Area Condo Market Highlights - November 2006

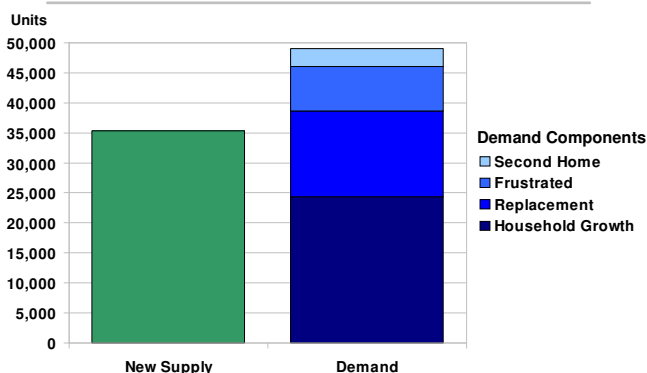
Overview

- Concerns about the health of the condo market have emerged, amidst a slowing housing market overall and recent growth in the pipeline of new condo projects.
- Despite the growth in new supply, San Francisco is a chronically undersupplied housing market, characterized by expensive housing prices and low levels of new construction. New development is a relatively small portion of the overall housing market in the Bay Area in general, and San Francisco in particular.
- More than 1,100 new homes sold annually in San Francisco between 2003 and 2005, and activity through the first half of the year indicates a similar pace in 2006.
- Activity within San Francisco has shifted to the South of Market (SOMA) area. During 2005 and the first half of 2006, about two-thirds of new condo sales took place in the SOMA area, which is also the location of the bulk of the city's new construction.
- these units will likely be built during the next five years.
- Substantial urban condo development is also occurring in other parts of the Bay Area, especially in areas with commercial and recreation cores. These areas offer urban amenities — such as plentiful dining, shopping and entertainment options — with less of an urban feel than downtown San Francisco. They also frequently offer easier entrance and egress, and in many cases, closer proximity to work and friends.
- In the East Bay, most condo development is occurring in downtown Oakland and Walnut Creek.
 - With more than 6,500 residential units, including condos and rental units, completed, under construction, or approved, Oakland is on track to surpass Mayor Jerry Brown's initiative to bring 10,000 new residents downtown.
 - Walnut Creek is another node of urban development that has attracted condominium activity to its commercial core of office buildings, entertainment and shopping. Projects include the Mercer luxury condominiums, and Stoneridge and 4 Seasons condo conversions.

Supply Trends

- High levels of new construction are of increasing concern, as some U.S. markets are suffering from an overhang of condo supply.
- Within the Bay Area, the greatest proportion of new urban condo construction, especially luxury development, is occurring in San Francisco.
- About 25,000 to 30,000 condo units are currently under construction, planned or proposed in San Francisco. Foresight Analytics believes that about half of these units will likely be built during the next five years.
- To the south of San Francisco, urban condo development is sprouting in downtown San Jose and on the Peninsula.
 - Almost 1,800 for-sale residential units are either recently completed or under construction in greater downtown San Jose, with another 3,400 for-sale units in the planning/permit process. Among the projects currently under construction are the 124-unit luxury City Heights and the 83-unit luxury 200 Park Avenue projects.
 - On the San Francisco Peninsula, a handful of larger projects are planned in Redwood City and downtown Millbrae.

Supply and Demand*
San Francisco, 1990 to 2000



* For all housing, including rentals.

Sources: Census Bureau, Foresight Analytics

- While buyers tend to be location-specific, increased transit options will give them greater flexibility in matching their work and entertainment preferences with their home purchase decision, thereby increasing competition between projects outside of and inside San Francisco.

Demand Dynamics

- Condos represent a significant proportion of new San Francisco for-sale housing. The urban nature of San Francisco favors dense multifamily development,

rather than detached single family homes. Additionally, national demographic trends point to increased demand for condos from an aging baby-boomer population and from their children who are reaching maturity and purchasing their first homes. Of particular interest to both older and younger buyers is the low maintenance and ability to lock and leave associated with condo living.

- Demand originates primarily from household growth, which is driven by both job growth and population growth and aging. Other sources of housing demand include replacement of older or outmoded structures, second home buyers and “frustrated” buyers. Frustrated buyers are buyers who would purchase in San Francisco or the Bay Area, but have not because of historical lack of product. Foresight Analytics estimates that these frustrated buyers comprised as much as 15% of the 50,000 units of residential demand during the 1990 to 2000 time period.
- A skilled workforce, rebounding technology and tourism, and the need for support services are driving growth in the Bay Area, including the San Francisco, San Jose, and Oakland metro areas. Following four years of job contraction, employment growth in the Bay Area turned positive during 2005 and the pace of growth is accelerating and is expected to average a solid 1.6% for 2006.

Luxury Condos

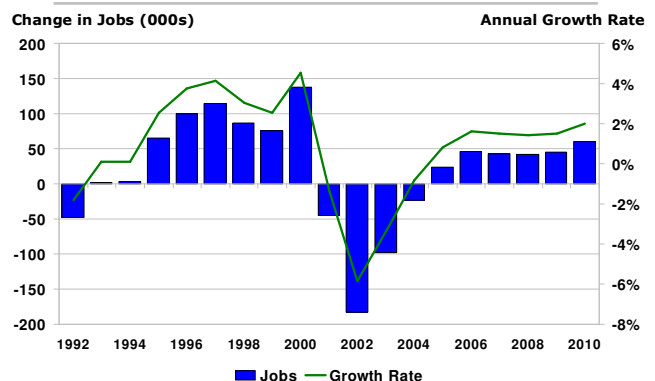
- More than half of luxury buyers in San Francisco are empty nesters older than 50 years of age. Most other luxury buyers are move-up buyers, with almost no first-time homebuyers.
- While jobs, population growth and household formation drive overall demand for housing, demand for luxury condos is tied primarily to wealth, and secondarily to income.
- With demand tied to wealth, the stock market is a likely better gauge of demand for luxury homes and condos than the local economy or job growth statistics. As of October 31, the Dow is up 12.7% year-to-date, reaching all-time highs above 12,000. The NASDAQ is up 8.6% year-to-date.
- The Bay Area possesses a significant number of potential luxury condo buyers. Foresight Analytics estimates that more than 10,000 Bay Area households have annual incomes greater than \$1 million, with the ability to afford a luxury condo.
- The relevant market for luxury condos actually extends well beyond the Bay Area, to both U.S. and foreign buyers. Foresight Analytics estimates 100,000 to 200,000 households nationwide with the wealth and income to purchase a luxury condo.

- For buyers from abroad, paying \$1,000 to \$1,500 per square foot for a luxury condo in San Francisco can seem like a relative bargain, as compared to prices that reach \$2,000 per square foot in New York City, \$2,300 per square foot in London, and \$2,500 per square foot in Hong Kong.

San Francisco Condo Market Outlook

- Foresight Analytics estimates regional employment growth averaging 1.6% per year during the next five years, adding 47,200 jobs annually and serving as a significant component of new residential demand. The greatest proportion of this job growth, almost 40%, will occur in the San Francisco metro area.
- Because San Francisco has historically been a supply-constrained market, equating demand with actual absorption of units underestimates potential demand for condo units. After factoring out supply limitations, Foresight Analytics estimates San Francisco condo demand in the 11,000 to 18,000 unit range during the 2006 to 2010 period.
- San Francisco condo absorption will keep pace with new supply through 2010. Demand will be sufficient to absorb the units being built, albeit with somewhat of a lag during 2007 and 2008. Absorption will outpace supply during 2009 and 2010, as the rate of new deliveries falls.
- With the large number of units expected to come on the market in 2007 and 2008, the average time to sell a unit will lengthen to six to nine months. In the past, new units in San Francisco have averaged sales times of three months or less because of the supply-constrained nature of the market.
- Price appreciation will slow dramatically from the recent double-digit growth rates of 2004 and 2005, but will stay positive. Foresight Analytics estimates that

Employment Growth
Major Bay Area Economies*



* San Francisco, San Jose and Oakland Metro Areas Sources: Bureau of Labor Statistics, Foresight Analytics

condo price growth in San Francisco will average 3% to 5% annually between 2006 and 2010.

- The demand outlook for other condo markets in the Bay Area is generally good. Long term demographic trends bode well, especially with empty nesters increasingly looking to downsize, desiring the amenities of urban living, yet not wanting to move away from an established network of friends and family. Moreover, increased commercial activity indicates growth in office market hiring that will further spur demand for condos in close proximity to workers' offices.

This report provides highlights from Foresight Analytics' recent in-depth market studies of the San Francisco Bay Area. For more information, contact us at:

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About Foresight Analytics

Foresight Analytics LLC is a California-based provider of real estate market consulting services. We focus on real estate market analysis and forecasting, for commercial and residential product types, in both domestic and international markets. Our clients are mainly institutional investors, lenders and developers.

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