

## Tech Firms Leading Commercial Real Estate Recovery

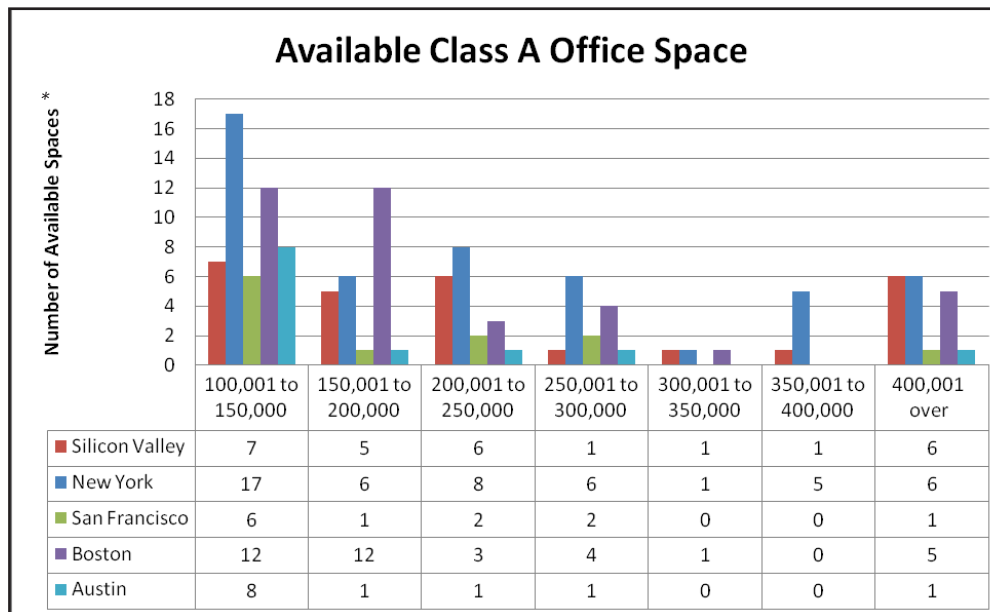
By Robert Bach, Senior Vice President, Chief Economist and  
Dick Scott, Managing Director, San Jose, Leader, Technology Practice Group

*Technology stocks have posted impressive gains in recent periods. According to Morningstar Inc., these stocks witnessed an average gain of 20.75 percent over the past year, an average gain of 12.39 percent annually over the past three years (leading all other sectors), and an average 10.09 percent gain annually over the past five years (trailing only basic materials). But has a strong stock market performance translated into demand for commercial real estate? In the following report, Grubb & Ellis examines five office markets with strong technology components to answer this question: Silicon Valley, San Francisco, Boston, New York City and Austin, Texas.*

In the Silicon Valley and San Francisco, tech firms are leading the commercial real estate recovery, while in New York City, Boston and Austin, Texas, they are instrumental to the market's rise in activity. In the Bay Area and New York City, Google, Facebook and LinkedIn are among the most active firms, while in Austin, SunPower Corp., Samsung and Apple Inc. have been prominent. Microsoft, IBM and Oracle have been significant market participants in Boston as well. These firms are largely focused on clustering their offices near each other, as well as tapping into a higher concentration of technology-skilled employees, a number of highly ranked universities and the metropolitan vibe these cities give that is current and hip.

### Impact on Speculative Construction

The activity by tech firms has created momentum and a spike in the absorption level of large blocks of space in some areas. The majority of technology companies require more than 100,000 square feet of space for their corporate headquarters and other company consolidations. As depicted in the following graph, there are few large blocks of Class A office space sized 100,000 square feet and above available for rent in each metropolitan area. This has led to the question of whether the markets will see an increase in speculative construction in these tech-heavy markets.



\*Number of contiguous blocks of Class A office space available as of March 31, 2011.

Grubb & Ellis does not expect the recent positive absorption levels for large blocks of space to turn into an increase in major speculative construction in the Bay Area immediately. What the company does expect to see in the Silicon Valley, however, is additional company consolidations, which have been occurring more frequently, large redevelopments and the acquisition of strategically located buildings and land parcels.

In Austin, two noteworthy projects recently broke ground in the Southeast region, including Data Foundry's 250,000-square-foot data center and CyrusOne's 72,000-square-foot data center. Beyond these projects, extensive development of new office and flex space is believed to be unlikely in the near-term. New York City is similar, in that with the completion of construction for 11 Times Square, no new significant office construction is expected to be finished for at least two years.

Boston tells a more unique story, with the Cambridge market being the hot spot for technology companies. Due to the city's high barriers to entry and the lack of large blocks of space that come on to the market, Cambridge will likely see construction sooner. Alexandria Real Estate Equities is planning a \$1 billion, 1.5-million-square-foot office/laboratory complex in East Cambridge. Additionally, the master-planned Cambridge Discovery Park is currently being marketed with permits in place allowing for the development of more than 800,000 square feet of space. Beyond Cambridge, Grubb & Ellis expects additional construction to take the form of a build-to-suit.

### Time to Invest

Technology corporations flush with cash are showing signs that it's time to invest in Silicon Valley's commercial real estate market. Microsoft, Dell, Qualcomm and Google are making large leasing commitments in the Silicon Valley. Brocade, Yahoo, Apple, Google and Facebook are just a few of the firms that are in the process or have purchased land near a building or project they plan to lease or redevelop. In San Francisco, Salesforce.com recently purchased 14 acres of land to potentially build a 2-million-square-foot campus and Zynga leased 270,000 square feet of space. By acquiring land, companies have the option to expand right next to their headquarters location when the time is right, eliminating the need for a corporate relocation. With the banking of this land, however, developers can't compete with the users, creating a barrier to construction in the Silicon Valley. Additionally, the current income from leasing space does not outweigh the cost to build it, making the only construction to take place mostly build-to-suit projects.

In New York City, Google recently purchased 111 Eighth Ave. for \$1.8 billion, ensuring their future growth in the market. The company currently occupies more than 500,000 square feet of the 2.9-million-square-foot building.

Austin has more than 90,000 professionals employed by technology firms. Intel Corp. invested \$39.8 million into the market by acquiring a 388,000-square-foot office building located at 1300 S. Mopac Expressway. SunPower Corp. is currently searching for space in the market and is expected to bring 450 jobs; the company has invested \$10 million in capital into Austin's economy through the expenses of opening a new operation. Cirrus Logic Inc. announced a \$30 million headquarters building to be built in downtown Austin that will house more than 550 employees and is expected to be completed in summer 2012.

### Aces and Spaces

To borrow a term used in the game of Bridge, several technology-rich markets are seeing "aces and spaces," where companies are moving into large, Class A buildings in prominent locations (the aces), while leaving spaces behind in the buildings they previously occupied (the spaces). In the Silicon Valley, there are a number of Class A office lease transactions closing in and around the larger existing projects in the market. Since these transactions often are a consolidation of operations and/or a flight to quality, they leave behind a number of smaller, typically older spaces, which generally take longer to be absorbed. Large firms such as IBM, Microsoft, Texas Instruments, Symantec and Oracle continue to acquire smaller companies in the area, often consolidating these new groups into their existing Silicon Valley campus locations or moving them to more visible, strategic locations.

Surrounding Boston, Acme Packet recently consolidated three offices into one location in Bedford, with additional expansion plans expected to occur within a few years. IBM and Oracle have also been active in acquiring companies, like Netezza Corporation and Art Technology Group, and moving them near their existing locations in Littleton and Burlington.

### In the Long Run

The U.S. continues to lead the global technology industry from both an innovation and market share perspective. It's important to note that although Grubb & Ellis does not expect speculative construction to return to the Bay Area and Austin immediately, construction should return within the next few years, and new buildings will get a lot of attention then.