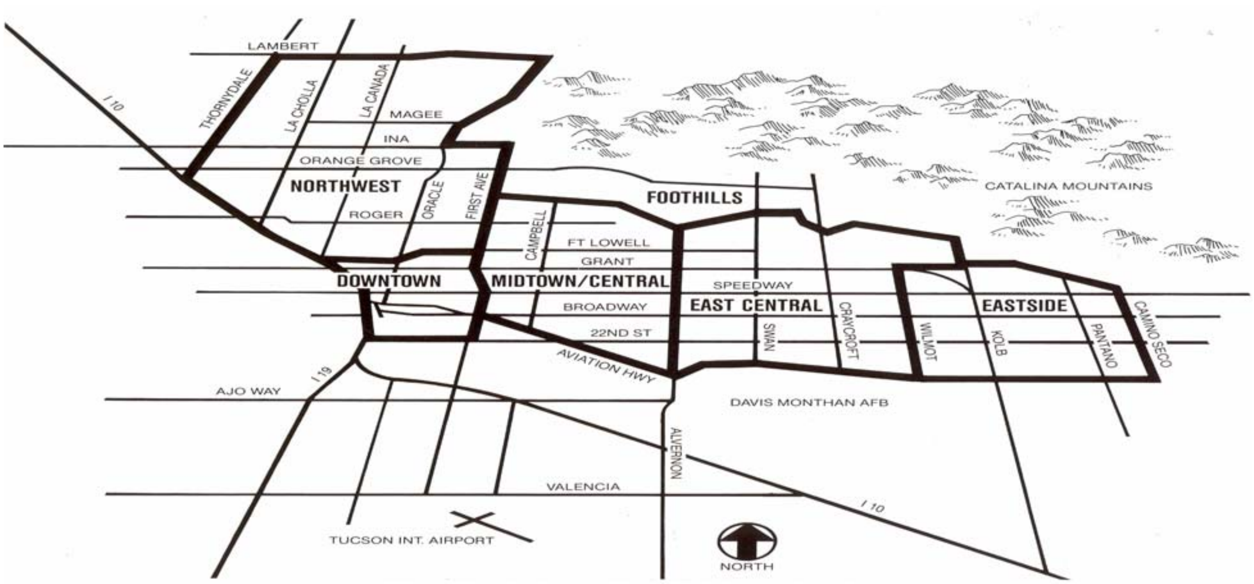
2006 OFFICE MARKET OVERVIEW - 2007 FORECAST

The office market was very strong during 2006. New office building construction combined with the conversion of former single-tenant properties to the multi-tenant for lease opportunities combined to increase the overall market. The office market grew and now encompasses 222 Class "A" and "B" buildings (10,000 square feet or larger) totaling just over 9,254,420 square feet. This is an increase of just over 500,000 square feet from the year before.

The market ended the year with just over 713,000 square feet of office space being available for lease resulting in an occupancy rate of 92.3%. Approximately 356,000 square feet was absorbed during the year. All in all it was a very strong year in the office market.

A brief overview of the office market and the general geographic boundaries is reflected below. This map shows the boundaries between the various office sub-market areas. Our firm looks at 8 distinct office sub-market areas – Campbell Corridor, Downtown, East Central, Eastside, Foothills, Midtown, North Central and Northwest.

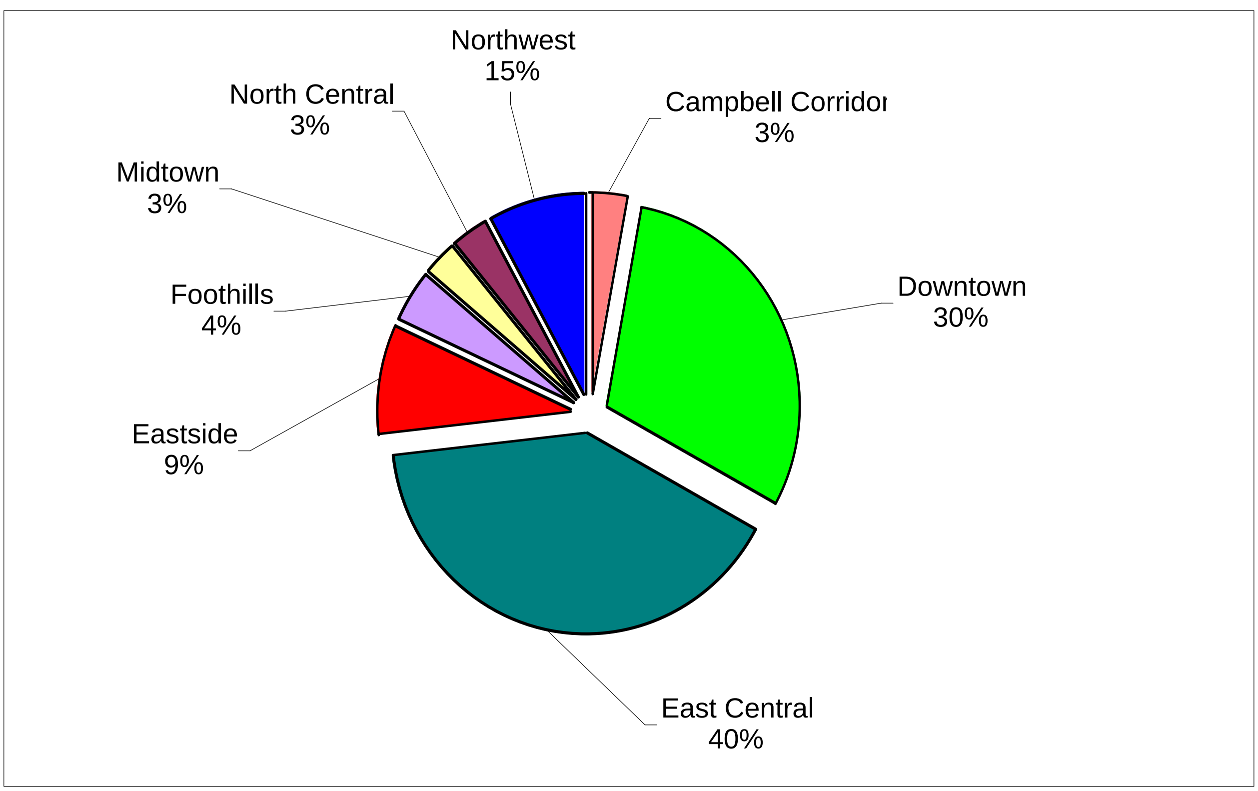


The following charts and graphs will provide a general overview of how each of these distinct office sub-markets performed during 2006.

OFFICE SUMMARY BY SUB-MARKET AREA

SUBMARKET AREA	NO OF BLDGS	TOTAL SQ FT	AVAILABLE SQ FT	LEASED SQ FT	OCCUPANCY RATE	NET ABSORPTION
Campbell Corridor	17	594,015	20,796	573,219	96.5%	16,159
Downtown	26	1,627,417	212,781	1,414,636	86.9%	(27,260)
East Central	56	3,158,706	288,676	2,870,030	90.9%	71,075
Eastside	21	951,870	61,676	890,194	93.5%	51,480
Foothills	15	467,184	28,660	438,524	93.9%	87,492
Midtown	30	677,071	22,758	654,313	96.6%	54,249
North Central	19	659,309	22,806	636,503	96.5%	17,793
Northwest	38	1,118,848	55,232	1,063,616	95.1%	85,908
Totals	222	9,254,420	713,385	8,541,035	92.3%	356,896

DISTRIBUTION OF VACANCIES BY SUB-MARKET AREA



With the exception of the Downtown sub-market - which remained flat or slightly declined by posting 27,000 square feet of negative absorption and an 86.9% occupancy rate - all of the seven suburban sub-market did exceptionally well with each posting occupancy rates that averaged 93.4% with the lowest being approximately 91% and the highest being 96.6%.

In fact, if data from the seven suburban sub-markets is considered only 500,614 square feet were available for lease out of 7,627,003 total square feet. This means 7,126,399 square feet were leased reflecting an overall occupancy rate of 93.4%. These seven sub-markets combined to experience just over 384,000 square feet of positive net absorption.

Leasing activity was down a bit in 2006 and tenants looking for larger spaces to lease – 10,000 square foot range – had nineteen options at year-end with nine of those being in the downtown area. This was a huge swing from a year before when only 9 such options were available citywide.

The mix of office tenants has changed drastically. Most local tenants have been focused on buying rather than leasing. The greater majority of new leasing activity was limited to national firms who prefer to lease rather than buy. Given the growth of the Tucson metroplex, in reaching the magic 1,000,000 population mark in 2006, more national firms are looking at opening offices in the area.

One area where tenants had challenges finding space were those who were looking to lease spaces 1,000 square feet or smaller. The options are for smaller office users were very limited and a similar situation exists with "executive suite" space too.

During 2006 we also saw the occupancy rate remain about the same – increasing slightly from 92% in 2005 to 92.3% in 2006. This is remarkable since many tenants elected to take advantage of low mortgage rates and became owners rather than continuing to lease space. Despite these factors the market chugged along and saw improvement in just about every sub market area except the Central Business District.

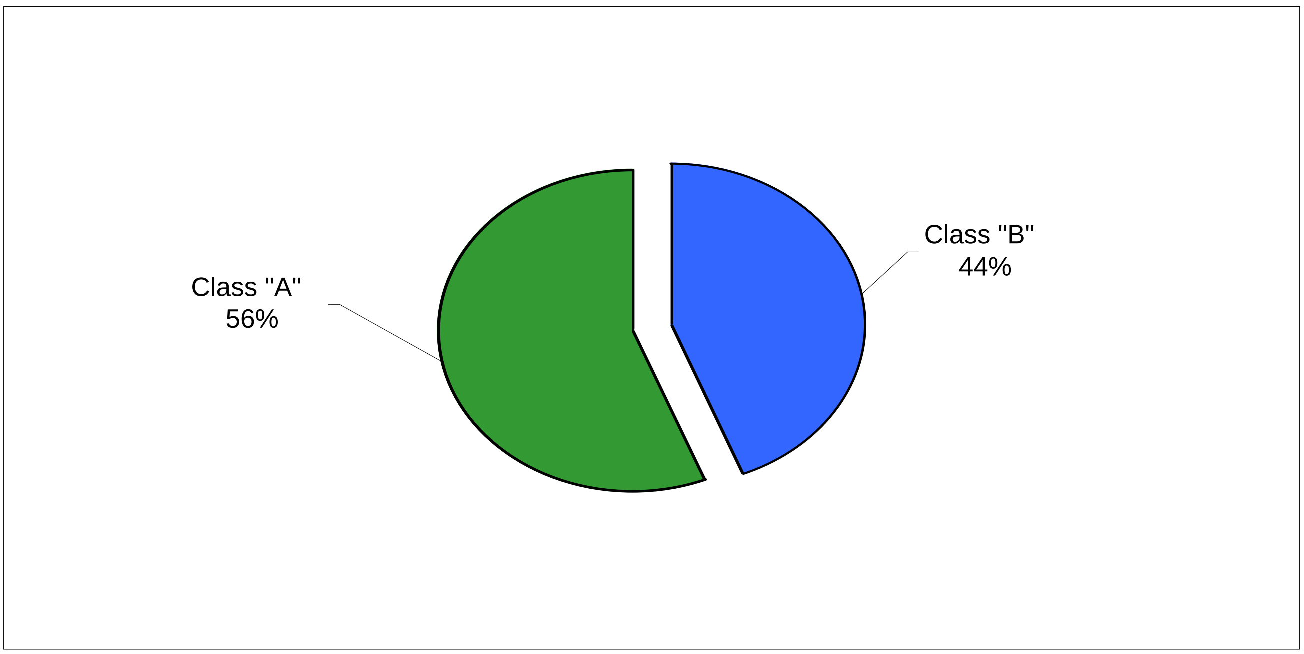
Having many former tenants buy or build their own office buildings, rather than leasing, is a huge factor that has significantly impacted the market overall. Developers have gotten smart and most are either renovating older projects or are doing new "garden style" office parks. Few new speculative office buildings "for lease" will be built this year.

The following two charts reflect how each Class "A" and Class "B" buildings performed during 2006.

OFFICE SUMMARY BY BUILDING CLASS

BUILDING CLASS	NO OF BLDGS	TOTAL SQ FT	AVAILABLE SQ FT	LEASED SQ FT	OCCUPANCY RATE	NET ABSORPTION
CLASS A	83	4,752,281	314,903	4,437,378	93.4%	143,393
CLASS B	139	4,502,139	398,482	4,103,657	91.1%	213,503
TOTALS	222	9,254,420	713,385	8,541,035	92.3%	356,896

DISTRIBUTION OF VACANCIES BY BUILDING CLASS



As can be seen, the occupancy rate between Class "A" and "B" properties stayed fairly level with Class "A" properties having a slight edge at 56% of the available vacancies. This is almost identical to the distribution of space in 2005. In 2004 it was the exact opposite with Class "A" only having 45% of the vacancies.

Likewise, the occupancy rates for both classes improved with Class "A" space jumping into the mid 93% occupancy range. Class "B" was right behind reflecting a 91% occupancy rate. Again, these figures almost mirror what occurred in 2005. Not a lot of significant differences occurred with both enjoying 143,000 and 213,000 square feet plus of positive net absorption, respectively.

Our firm looks at how the market performs in a three distinct areas. We have already discussed sub-market area data and data by building class. The final

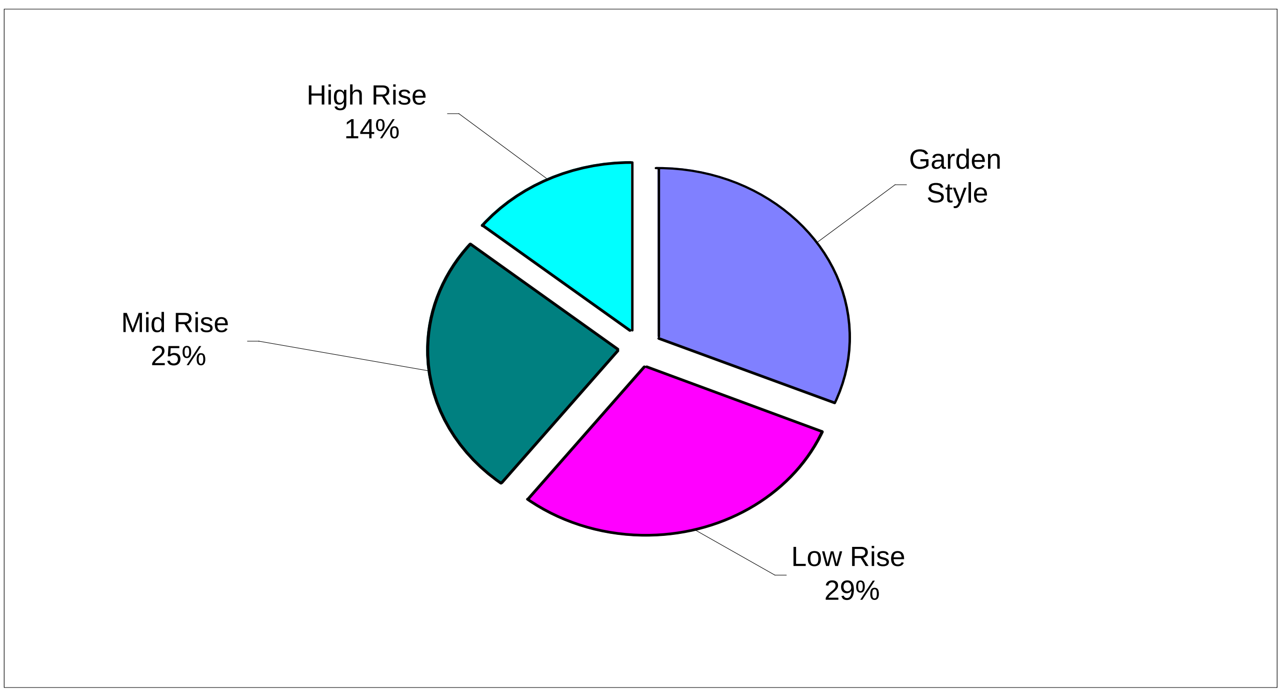
area we consider is by building type. Tucson has four distinct types of buildings – Garden Style, Low Rise, Mid Rise and High Rise.

The table and graph on the following page reflects how each of these four building types performed during 2005.

OFFICE SUMMARY BY BUILDING TYPE

BUILDING TYPE	NO OF BLDGS	TOTAL SQ FT	AVAILABLE SQ FT	LEASED SQ FT	OCCUPANCY RATE	NET ABSORPTION
Garden Style	108	3,136,784	219,738	2,917,046	93.0%	267,246
Low Rise	79	2,677,974	210,380	2,467,594	92.1%	41,453
Mid Rise	28	2,258,157	180,365	2,077,792	92.0%	54,653
High Rise	7	1,181,505	102,902	1,078,603	91.3%	(6,456)
Totals	222	9,254,420	713,385	8,541,035	92.3%	356,896

DISTRIBUTION OF VACANCIES BY BUILDING TYPE

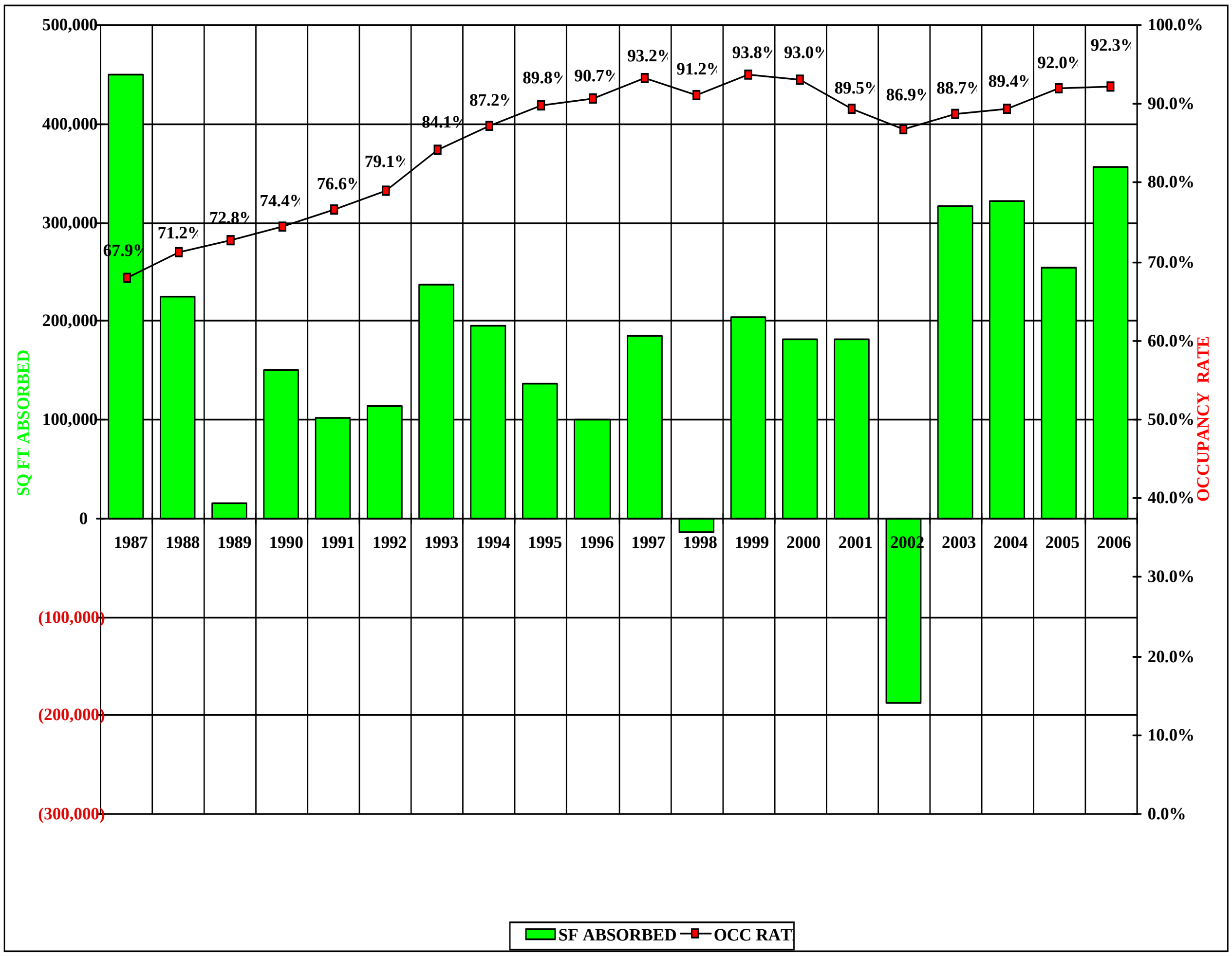


For the first time in many years the high-rise properties had the least amount of space available for lease overall. They also had the lowest occupancy rate. Overall, not a lot of distinction in occupancy rates between the four property types ranging from 91.3% to 93%.

Another indicator of market health is how much net absorption occurred. Comparing this figure to the occupancy rate over time shows an upward trend in both areas – again, an indicator of the vitality of the office market.

The following graph reflects 19 years with of data tracking net absorption and comparing it to the occupancy rate. As is shown, Tucson has only seen two years that reflected negative absorption since 1987 with the most recent being 2002.

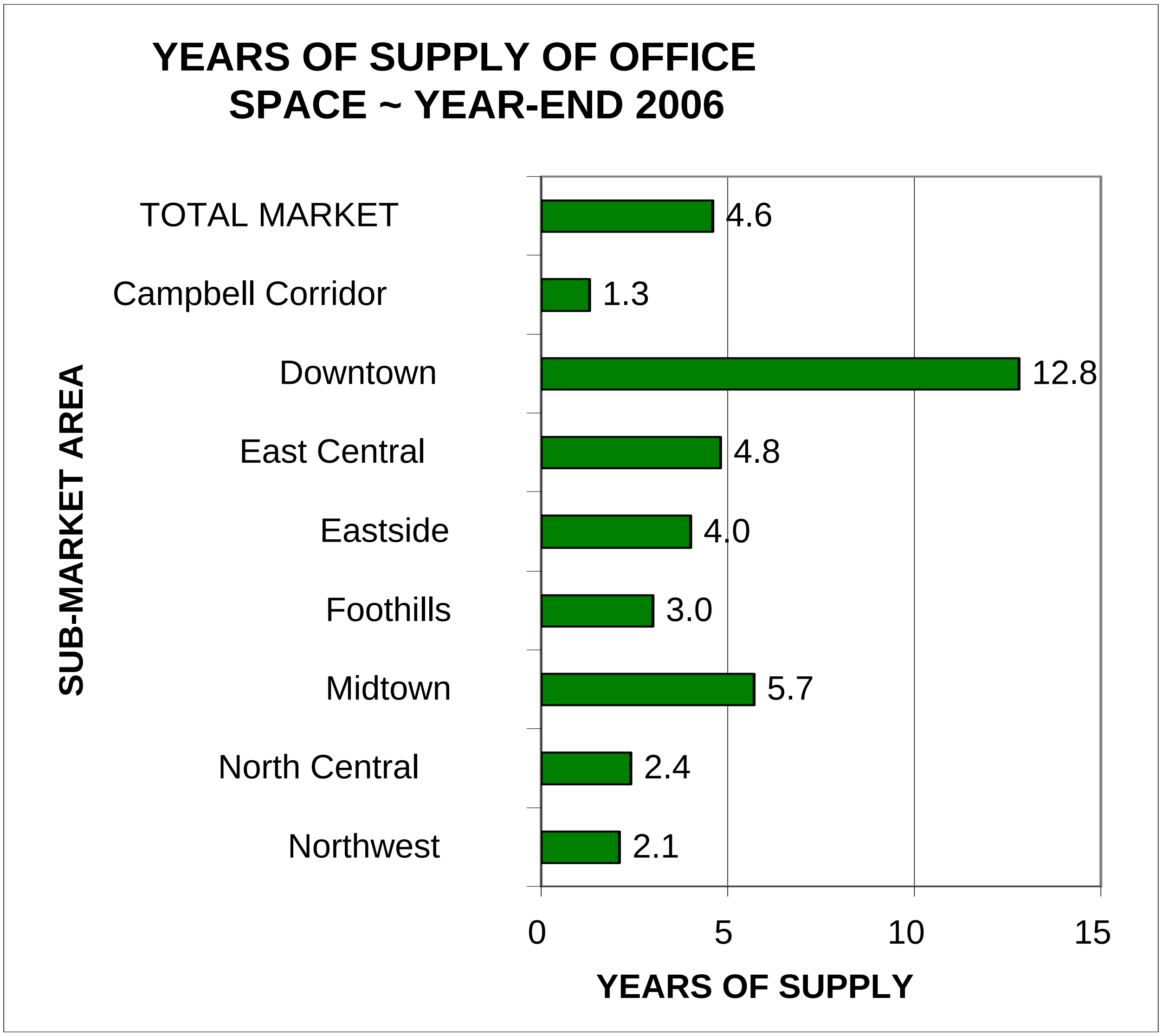
HISTORICAL NET ASBORPTION AND OCCUPANCY RATE



It is important to note that during this twenty year time frame the overall size of the office market has grown from 4,700,000 to roughly 9,250,000 square feet.

Over the past four or five years the market has enthusiastically accepted the office park concept. More importantly, so have the bankers and lenders and financing for owner-users is readily available. Many SBA lenders are providing fixed 20 and 25 year loans at a 90% loan to value ratio. On existing construction, most require the owner-user to occupy 51% and 65% on new construction projects that they finance.

A review of each sub-market and how many years of supply of office space for lease is reflected below. This chart was prepared using almost 20 years of statistical data on annual absorption in each specific sub-market area.



The Downtown sub-market is an area of concern. Despite all the hoopla about Rio Nuevo, the central business district continues to be plagued by lower occupancy rates but seems to be recovering slightly and has posted positive absorption the last couple of year. The Midtown sub-market reflects an anomaly, with only 22,000 square feet available for lease this sub-market area is very healthy.

This overall growth in the office market is evidenced in the following chart that tracks the growth of the office market since 1986.

HISTORICAL OFFICE MARKET OVERVIEW

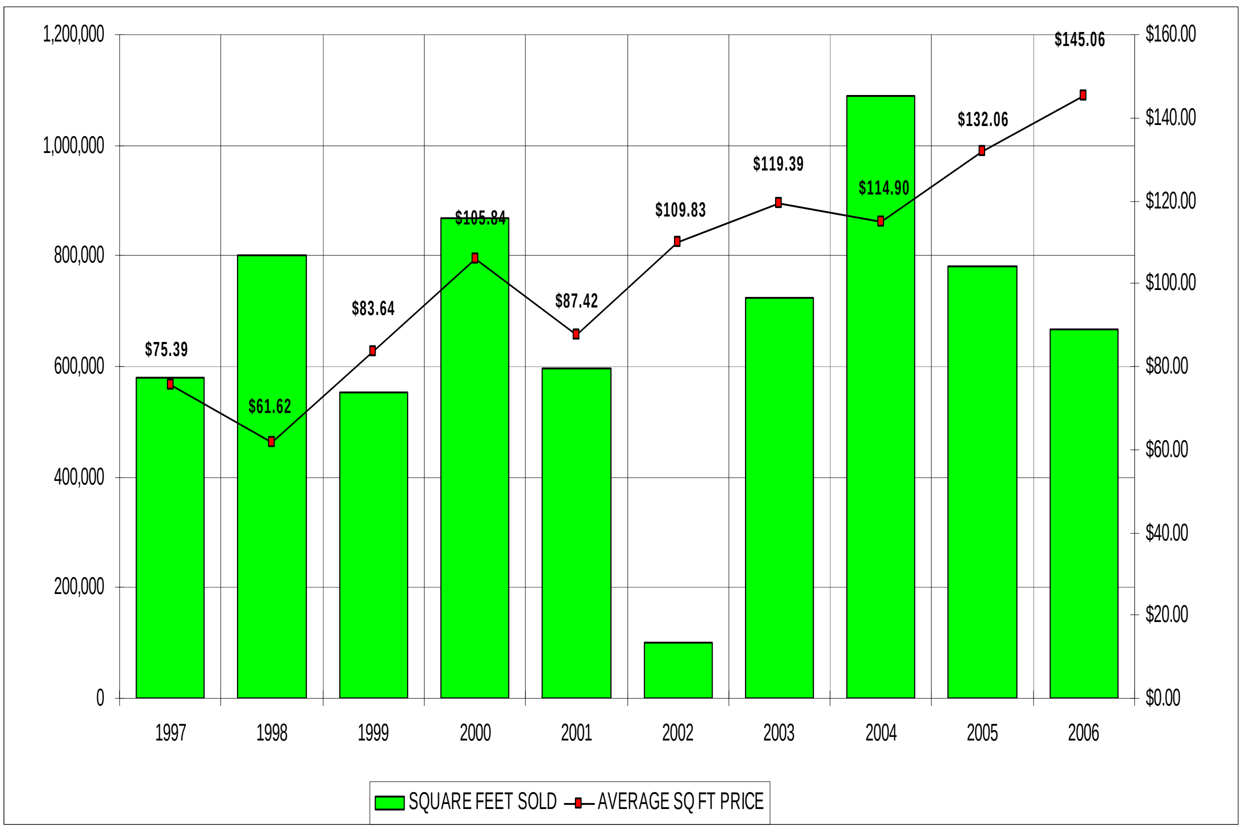
YEAR	NEW CONSTRUCTION SQ FT	NET ABSORPTION SQ FT	OCCUPANCY RATE	TOTAL SQ FT
1986	1,000,000	600,000	72.6%	4,700,000
1987	600,000	450,000	67.9%	5,800,000
1988	125,000	225,000	71.2%	6,300,000
1989	55,000	16,000	72.8%	6,500,000
1990	12,000	150,000	74.4%	6,500,000
1991	38,000	101,000	76.6%	6,300,000
1992	-	114,000	79.1%	6,375,000
1993	10,000	237,000	84.1%	6,203,000
1994	-	196,000	87.2%	6,265,000
1995	51,000	136,328	89.8%	5,926,000
1996	14,000	99,710	90.7%	6,261,000
1997	52,000	185,003	93.2%	6,242,000
1998	126,000	-15,060	91.2%	6,440,530
1999	109,000	203,312	93.8%	6,422,530
2000	275,000	180,965	93.0%	6,674,770
2001	305,000	182,103	89.5%	7,022,100
2002	305,000	(186,982)	86.9%	7,138,245
2003	116,000	316,404	88.7%	7,352,960
2004	334,270	211,135	89.4%	8,326,357
2005	385,000	254,780	92.0%	8,756,357
2006	425,000	356,896	92.3%	9,254,420

This historic overview adjusts for new construction in the multi-tenant for lease inventory and nets out buildings that were purchased by owner-users that are no longer available for lease. Conversely it also adds back into inventory buildings sold by owner-users to investors with the intention of leasing those properties.

Finally, sales activity was down from its recent high in 2004 when over 31 office buildings totaling over 1,000,000 square feet were sold. The year before (2005) saw 22 office building sales, consisting of approximately 782,000 square feet. In 2006 the number of properties sold increased slightly to 29 office buildings changing hands. The square footage of properties sold decreased to just over 665,000 square feet.

The following graph provides a historical overview of how many square feet of space were sold compared to the average sales price over the past ten years. Additional market sales data is available extending back to 1988 for review by contacting us.

SQUARE FEET SOLD COMPARED TO AVERAGE SALES PRICE



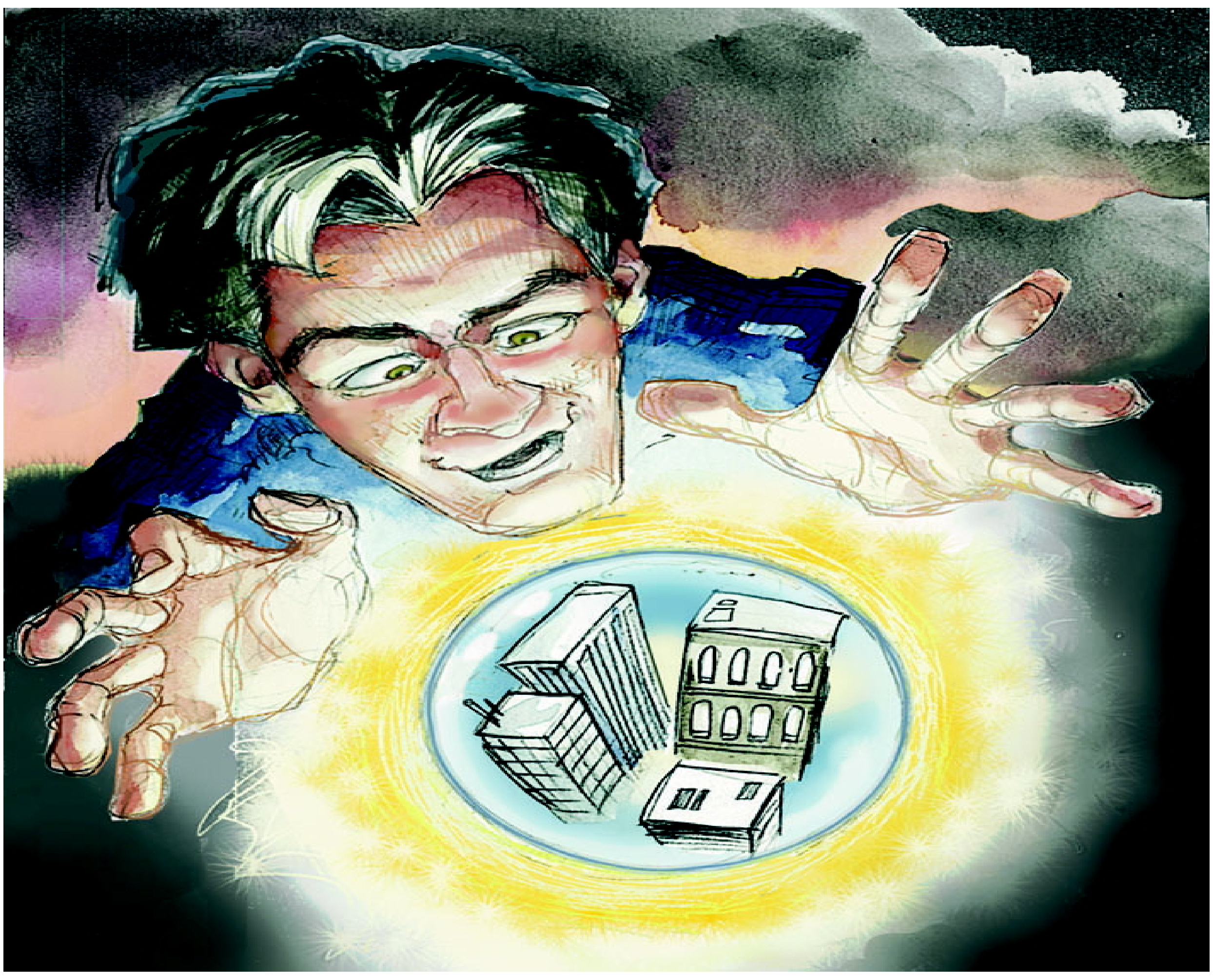
Sales to investors outnumbered sales to owner-users by just over a 5 to 1 ratio. The average square foot price paid by investors was $145.91 compared to $137.70 by owner-users. This is the first time this has occurred in many years and typically sales to owner-users are generally higher in the number of transactions and in the price paid per square foot.

Office building sales in the 5,000 to 10,000 square foot range saw an average price of $139.08 with the average Investor price per square foot being $149, and $134.70 for owner-users. Again, this is another first on the investor versus owner-user on a price per square foot basis.

Buildings in the 2,500 to 5,000 square foot range saw average prices at $199.89 per square foot. Investors paid $260.65 on average per square foot and Owner-users $182.69 per square foot. Again, this square foot pricing saw another first in the Investor/Owner-user market.

Pricing for new construction reached new milestones in 2006. Pad prices for improved office lots sold at prices between $75 and $100 per building square foot. Shell building pricing – including the land costs – ranged from $175 - $195 per square foot. With office interior finishes fully improved building saw prices in the $225 to $250 per square foot. Medical offices are typically $25 to 50 per square foot higher in price.

So, what does our crystal ball tell us to expect in 2007?



FORECAST

- **Occupancy rate will remain fairly flat but improve slightly and are expected to end the year at about a 93.5% overall occupancy rate.**

- **Lease rates will rise slightly with Class "A" full-service annual rates for existing building ranging between $22 and $26 per square foot and lease rates for new construction being in the $30 to $33 range. Some properties in the Foothills sub-market will be in the mid to upper $30 range. Class "B" rates for existing building being in the $16 to $22 per square foot with little if any Class "B" office space being constructed during the year.**

- **Allowances for tenant improvements for new and renewing tenants will continue to be lower than in years past. Most landlords are providing "paint and carpet" allowances only for renewing tenants.**

- **Most new leases will be with national, rather than local, tenants and due to the area reaching 1,000,000 population mark, we will see more national tenants opening offices in Tucson.**

- **Tenants looking for smaller office spaces will continue to find it difficult to find suitable options in the market.**

- **Tenants needing larger spaces – 10,000 square feet and larger – will have ample options available during the year as many former single-tenant properties will be converted to multi-tenant for lease properties.**

- **Owner-users will continue to buy buildings rather than continue to lease which will ultimately keep the occupancy rate in check and below 94%.**

- **Construction costs and rising real estate taxes on office properties will continue to impact the cost of new construction. It will keep the speculative office market construction to a minimum although 200,000 square feet of new speculative construction is expected to occur with most being in the Foothills or Northwest sub-market areas.**

- **Office Condominium/Office Park developments will continue to be the preferred property for most office buyers. Approximately 10 new projects will break ground during 2007 and due to the lack of in-fill opportunities most new projects will be in the Northwest and Foothills sub-market areas.**

- **Capitalization rates will continue to be in the 7% range for well positioned and leased properties but finding buying opportunities will continue to be a challenge.**