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Industrial Market Trends

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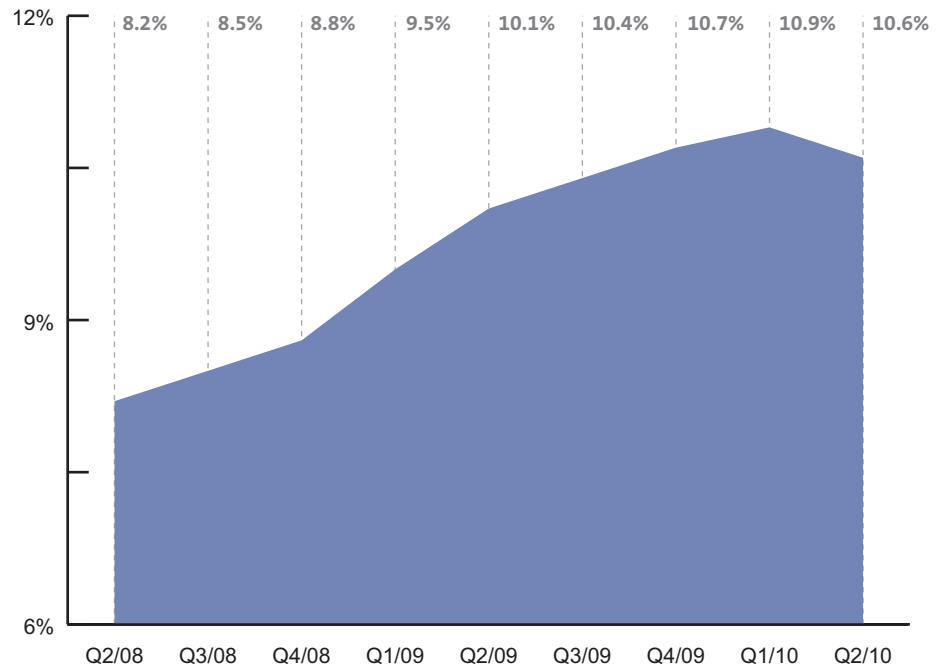
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Sudden Reversal

US INDUSTRIAL VACANCY RATE*



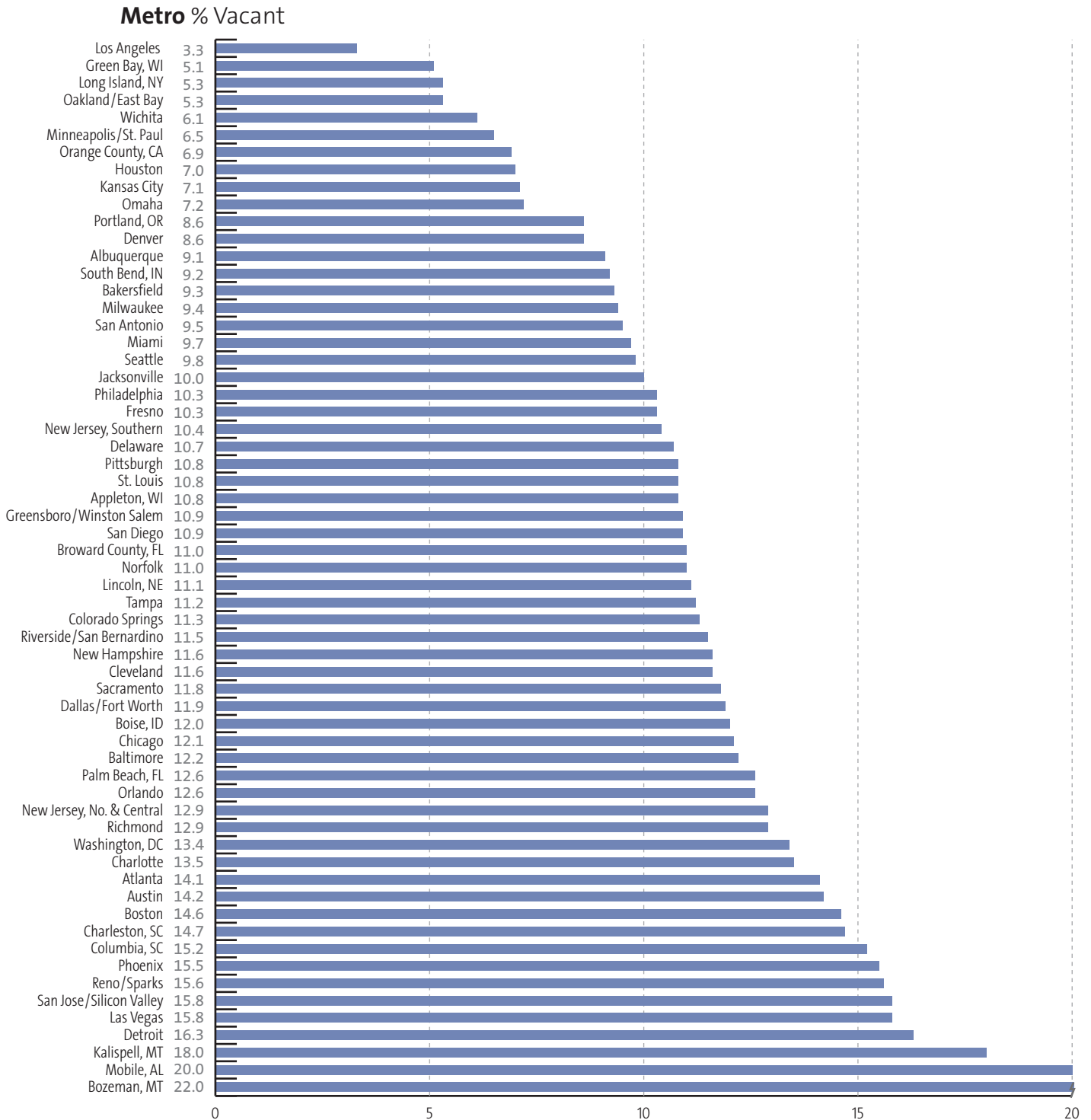
* All product types

THE BOTTOM LINE

The U.S. industrial market began to tighten in the second quarter as the vacancy rate fell by a surprising 30 basis points, the sharpest quarterly decline in nearly five years. The decrease in space under construction to 0.1 percent of the existing inventory—the lowest ratio in the 24-year history of Grubb & Ellis' national database—set the stage for the recovery to begin while net absorption totaling 19.9 million square feet was the catalyst. Asking rental rates continued to sag, however, which is to be expected in the very early stages of a recovery. The market is finally reacting to the rebound in manufacturing activity and freight shipments that has been under way since late last year. The question is whether the market has built up enough momentum to carry it through the soft economic patch forecast for the remainder of this year.

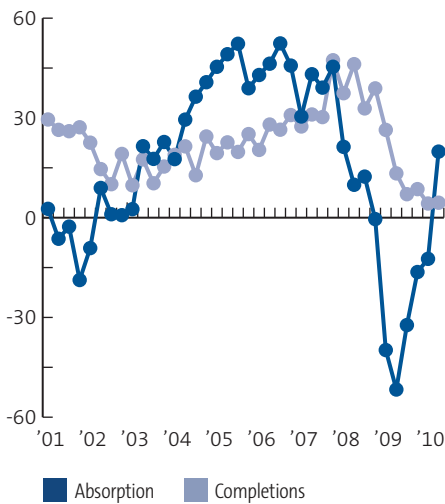
TOTAL MARKET VACANCY RATES

Note: Vacancy data refer to general industrial, warehouse/distribution, R&D/flex and incubator buildings with size thresholds ranging from 5,000 square feet in smaller markets to 25,000 square feet in larger markets. Inventory includes multi-tenant, single-tenant and owner-occupied space.

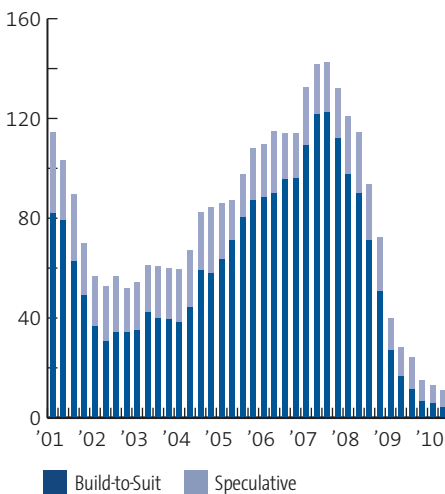


STATE OF THE MARKET

Absorption and Completions
in Millions of Square Feet



Space Under Construction
in Millions of Square Feet



The market turned around in a big way in the second quarter as measured by vacancy and absorption while construction activity and rental rates continued to move lower—all signs of a nascent recovery.

Vacancy fell by a decisive 30 basis points to 10.6 percent, ending a string of 10 consecutive quarterly increases. While the softening cycle appears to be over, the market remains awash in space with vacancy still 50 basis points above its year-ago level and 300 basis points above its cyclical low of 7.6 percent notched in the second and third quarters of 2007.

- Warehouse-distribution space accounted for the bulk of the vacancy decline as the rate fell by 60 basis points to end the second quarter at 11.6 percent. The vacancy rate for general industrial space (primarily manufacturing) fell 10 basis points to 8.1 percent while the R&D-flex vacancy rate rose by 10 basis points to 14.3 percent.
- At the metro market level, vacancy was lowest in **Los Angeles County** at 3.3 percent, down a notch from 3.4 percent in the first quarter. Even so, asking rental rates in LA continued to slide, reaching their lowest level in more than 10 years. Aside from a handful of smaller markets, vacancy was highest in **Detroit** at 16.3 percent. Second quarter absorption in the Motor City was still in the red but by a relatively modest 685,000 square feet compared with negative 1 to 2 million square feet in the past five quarters, raising hopes that the brutal downturn is moderating.

Net absorption lunged ahead to 19.9 million square feet, breaking a string of six consecutive quarters in the red. This was the strongest performance since the first quarter of 2008 but still less than half the quarterly totals during the vigorous expansion of 2005 and 2006.

- All types of industrial space recorded positive second quarter absorption led by warehouse-distribution product with 12.1 million square feet, general industrial with 7.2 million square feet, R&D-flex with 244,000 square feet and incubator space with 308,000 square feet.
- **Northern and Central New Jersey** rebounded sharply in the second quarter with absorption of 7.5 million square feet, which not only ended an eight-quarter string of negative absorption but also filled about half the empty space vacated during that period (on a net basis). California's **Inland Empire** market, **Atlanta** and **Denver** all absorbed between 2 and 3 million square feet.
- **Pittsburgh** lagged all markets in the second quarter with negative absorption of 2.4 million square feet. As a market barometer, this is misleading because the former Sony plant alone added 2.3 million square feet of available inventory. Leasing and construction activity in the Pittsburgh market was fragile, however.

Just 4.5 million square feet of new space was delivered in the second quarter, three-quarters of which was build-to-suit. Proj-

ects still in the construction pipeline at the end of the quarter totaled 11.1 million square feet, 61 percent of which was build-to-suit.

- Warehouse-distribution space continued to dominate the construction pipeline as it has for the past decade, accounting for 7.2 million square feet of the space under way, followed by 3.1 million square feet of general industrial space and just under 1 million square feet of R&D-flex space.
- The **Inland Empire** with 2.5 million square feet in the pipeline led all other markets, followed by Greater **Philadelphia** (including Central and Eastern Pennsylvania) with 1.5 million square feet and, surprisingly, **Charleston, S.C.** where a 1.1 million-square-foot build-to-suit project is under construction for TBC Tire Kingdom.

The average asking rental rate for all types of industrial space offered on the market at the end of the second quarter was \$5.35 per square foot per year triple net, a decline of 0.8 percent from the first quarter and 4.6 percent from the year-ago quarter.

- Rates for available space ended the quarter at \$5.16 for general industrial space, \$4.29 for warehouse-distribution space and \$9.34 for R&D-flex space.
- For warehouse-distribution space, the average asking rate was highest in **San Diego** at \$8.55. San Diego has high land costs and smaller buildings with high per-square-foot rental rates. **Northern Indiana** (the South Bend area) posted

The second-quarter turnaround raises hope that the market has built up enough momentum to carry it through a soft patch in the economy through the rest of this year.

the lowest average rate at \$2.71. Although this market has a relatively low vacancy rate and saw good second-quarter absorption, it remains a tenant's market to the point where landlords are offering deep discounts even for shorter lease terms.

- **Orange County, Calif.** and **Los Angeles** posted the sharpest year-over-year declines in asking rates for warehouse-distribution space at 18 percent and 11 percent, respectively. Markets that are subject to rent spikes when times are good can also experience sharp declines when demand dries up even when vacancy rates are low compared with less volatile markets—a dynamic that is playing out in Los Angeles and Orange County. A small handful of markets posted positive year-over-year rent growth for warehouse-distribution space led by **Omaha, Neb.** and **Long Island, N.Y.**, both in the mid-single digits.

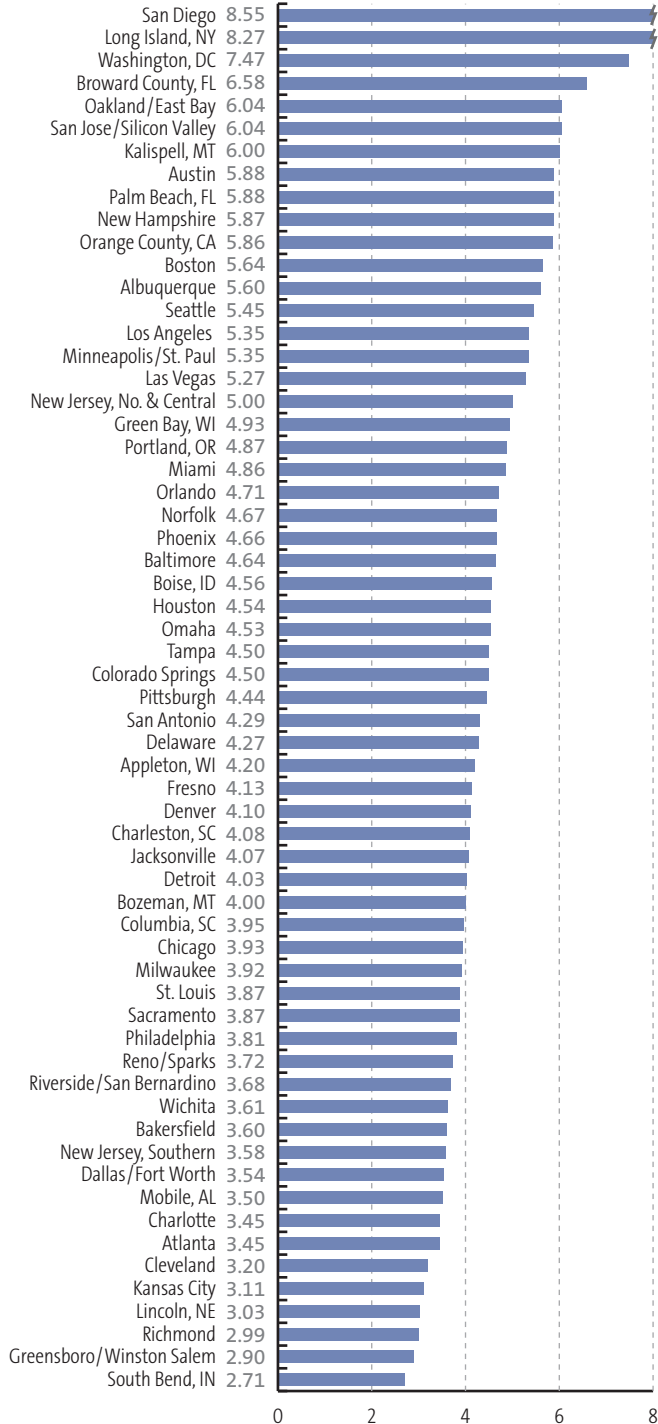
FORECAST

The abrupt turnaround in market conditions during the second quarter was both heartening and surprising considering that the economy decelerated last quarter. The sluggish economy raises the possibility that the industrial recovery could falter in the second half of 2010. The inventory cycle has started to wind down; manufacturers, wholesalers and retailers that let inventories fall to subsistence levels during the recession have restocked to meet final demand levels that have firmed up but are still far from robust. Thus, while the manufacturing sector continues to expand, it is slowing down. Additionally, a lot of excess space is weighing down rental rates, which have not hit bottom in most markets and could be slow to recover after they do. Occupied space declined by 153 million square feet from the fourth quarter of 2008 through the first quarter of 2010 at the same time that developers delivered 99 million square feet of new space, so the market will need about three years of steady absorption to get back to even. Nevertheless, the second-quarter turnaround raises hope that the market has built up enough momentum to carry it through a soft patch in the economy through the rest of this year.

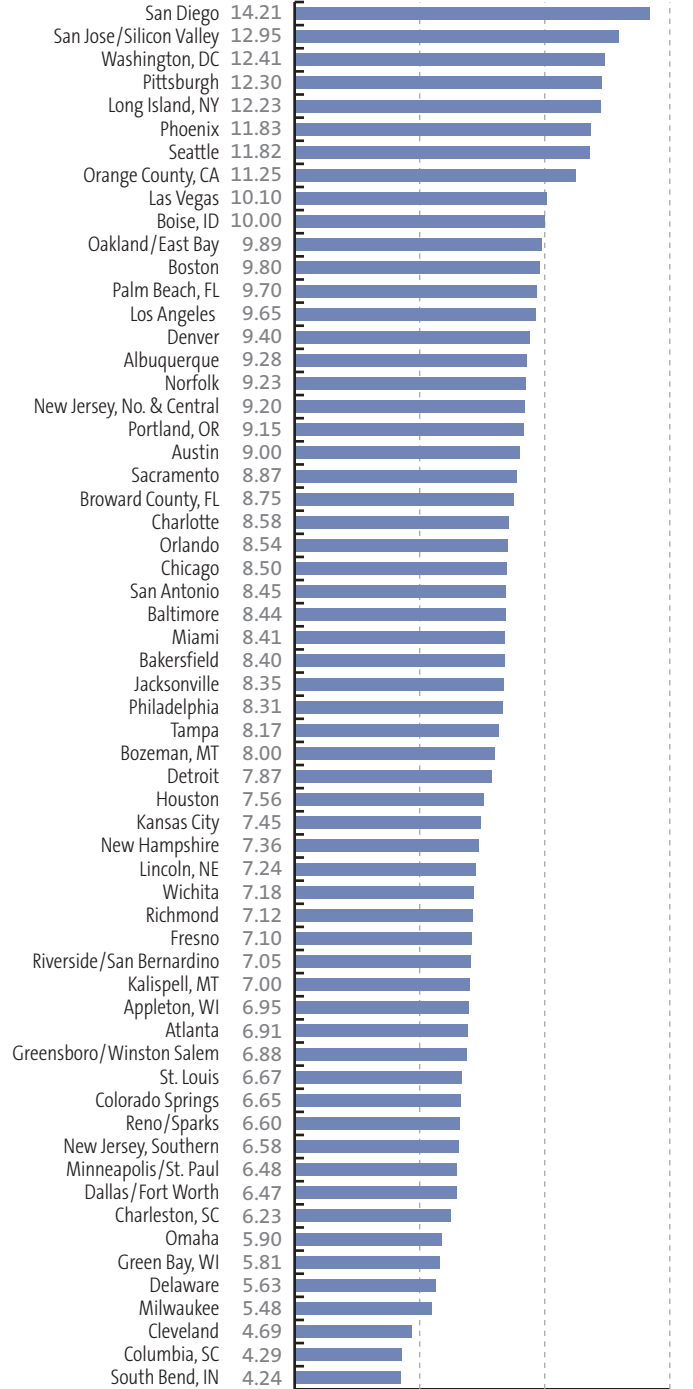
ASKING RENTAL RATES

Note: Rental rate data refer to space that is available on the market at the end of the quarter. Rates are per square foot, quoted on a triple net basis. Rates for each building are weighted by the amount of available space within the building.

Warehouse/Distribution \$ Asking Rent



R&D/Flex \$ Asking Rent





NORTHERN CALIFORNIA/ PACIFIC NORTHWEST

Oakland-East Bay: Sales activity improved slightly with several significant deals completed in the second quarter... **Portland:** The I-5 South Corridor saw the biggest gains this quarter with the 109,000-square-foot occupancy of Medline in Wilsonville and two large tenants leasing space at 115th Commerce Park: Stanton Furniture with 92,000 square feet and Consolidated Molding & Millwork with 48,000 square feet... **Sacramento:** Several larger tenants took occupancy of spaces across virtually all submarkets this quarter, resulting in 300,000 square feet of positive net absorption and a reduction in the regional vacancy rate by one full percentage point... **San Jose-Silicon Valley:** Semiconductor chip sales were up 50 percent year-over-year, which is expected to drive absorption in the coming quarters... **Seattle:** Service Paper Company moved into 178,000 square feet at the Rainier Park of Industry in Sumner. The investment market picked up steam this quarter with 30 industrial transactions totaling \$96 million in sales volume.



SOUTHERN CALIFORNIA/ PACIFIC SOUTHWEST

Bakersfield: The market is improving slightly. Tenants are looking for inexpensive rates, and landlords are trying to accommodate through incentives such as free rent. Sales remain slow due to the lack of available credit... **Los Angeles:** The largest lease this quarter was signed by CEVA Logistics, which committed to a five-year term on a 284,885-square-foot, Class A warehouse in Carson that was previously occupied by Hitachi Transport System Ltd... **Orange County:** There continues to be strong demand for well-located industrial space as tenants expand, contract or consolidate into quality buildings. ENS Granite Workshop committed to

122,300 square feet in Anaheim for its nationwide wholesale distribution center. The largest sale was Frick Family Properties' \$22.2 million purchase of a 246,732-square-foot distribution facility in Orange... **Riverside-San Bernardino:** Users are focused on slimming their operating costs, which has prompted significant movement in recent months. Year-to-date, 46 transactions have been signed for spaces in excess of 100,000 square feet... **San Diego:** The market has begun to stabilize. Rental rates continue to drop, but absorption is bottoming out.



MOUNTAIN/SOUTHWEST

Albuquerque: The market is seeking a solid foundation for growth. Tenants still lack confidence to take advantage of current market conditions. Demand is weakest for warehouse-distribution space... **Boise:** There has been little activity in recent months. Landlords are offering concessions to attract new tenants... **Bozeman:** There is a significant amount of new product in the Four-Corners submarket, but demand is soft with rental rates falling and vacancies increasing... **Colorado Springs:** Leasing activity, lease rates and values are declining... **Denver:** Vestas' occupancy of its new 660,000-square-foot Brighton campus comprised a third of total absorption in the market this quarter... **Kalispell:** Absorption of warehouse product has slowed with rates starting to move down slightly. The market is not very overbuilt... **Las Vegas:** Vacancy is expected to remain fairly flat for the duration of the year. Until a significant amount of product is absorbed, lease rates and sales prices will continue to drop... **Phoenix:** Construction is at zero for the first time in 22 years, setting the stage for a recovery... **Reno:** Vacancy remains high as leasing activity cannot quite keep up with space returning to the market. Rental rates are beginning to firm, however.



TEXAS/GREAT PLAINS

Austin: Applied Materials placed nearly 600,000 square feet on the market for sale or lease, more than a third of its 1.6-million-square-foot campus... **Dallas-Fort Worth:** Business has improved in several sectors of the local economy, including manufacturing, transportation services, housing and energy, providing some stability to the industrial market... **Houston:** The federal government's moratorium on offshore drilling looms large as thousands of jobs are at risk, which could threaten the industrial market... **Kansas City:** Trinity Architectural Products moved from 114,867 square feet in Lenexa, Kan. to a 66,000-square-foot building in Kansas City, Mo. The property vacated by Trinity was leased to Premium Mills... **Lincoln:** FedEx expanded into its newly constructed 67,216-square-foot facility. Kawasaki was awarded a contract to build rail cars for the transit system in Washington, D.C., which will add jobs and create demand for additional warehouse space... **Omaha:** Negative absorption came from Nashua Label Product vacating 170,000 square feet. Two owner-user projects totaling 50,000 square feet broke ground... **San Antonio:** American Standard plans to vacate 404,000 square feet later this year... **St. Louis:** Landlords are very aggressive and focused on maintaining short-term cash flow. Many concessions are being offered to tenants although owners are finding it difficult to fund TIs and commissions... **Wichita:** To keep pace with changing business and workforce needs, Sedgwick County will open The National Center for Aviation Training in August. The \$49 million, 200,000 square-foot campus will offer classes on general aviation manufacturing, composites manufacturing and robotics.



GREAT LAKES/ OHIO VALLEY

Appleton: Several smaller properties came on the market including the former UBC Building Supply facility, adding 40,000 square feet to the available inventory...

Chicago: RTC Industries moved into 503,000 square feet, and ALG Direct occupied 499,000 square feet, both in Romeoville...

Cleveland: Segments of manufacturing such as steel processing, metal fabricating and forging are gearing up for increased orders with improved capacity utilization and worker recalls. Lefco Worthington, a manufacturer of shipping products, has experienced vigorous demand in recent months...

Detroit: Tag International leased 222,308 square feet in Wixom. In Novi, CVS purchased a 73,000-square-foot warehouse-distribution facility... **Elkhart:** Companies recently announcing expansions include Atwood Products, NIBCO, ABC Bus and Santelli Tempered Glass. Vacancy appears to have leveled out...

Green Bay: Vacancy rates have stayed within a narrow band of 200 basis points for more than three years... **Milwaukee:** U-Line occupied a 1.1 million-square-foot build-to-suit in Kenosha County. Racine County had positive absorption due to the sale of the former Ametek building to Wholesale Christian Books...

Minneapolis: Year-to-date negative absorption of nearly 1 million square feet comes as tenants are downsizing while few large users are growing... **South Bend:** Although 225,000 square feet of additional space hit the market, the quarter ended with positive absorption of approximately 220,000 square feet.



NORTHEAST/ MID-ATLANTIC

Baltimore: Tenants have a wide choice of new and used product and the ability to dictate deal terms. Landlords are wheeling and dealing... **Boston:** After five consecutive quar-

ters of red ink, the market absorbed 144,000 square feet in the second quarter thanks to large deals by tenants including Dealer Tire and Price Chopper... **Long Island:** During the second quarter both industrial availability and vacancy rates improved. General industrial properties continued to perform well despite the turbulent economy, with users attracted by falling rental rates... **New Hampshire:** Tenant improvement allowances remain plentiful... **New Jersey:** Increased tenant requirements spanning a variety of product types produced nearly 7.5 million square feet of positive net absorption in the second quarter, handily outrunning all other markets. The market is holding its collective breath to see whether the momentum can be sustained in the second half of the year...

Philadelphia: Performance remains mixed across submarkets. Logistics maintains its dominant role in the I-81/I-78 Corridor...

Pittsburgh: Marcellus Shale-related oil and gas companies continued to drive demand, but they were unable to neutralize the 2.3 million square feet of available space added in a single facility, the former Sony plant in the Westmoreland submarket... **Washington, DC:** Second quarter absorption was flat.



SOUTHEAST

Atlanta: The General Mills Distribution Center, a 1.5 million-square-foot LEED Gold certified build-to-suit, was recently delivered. General Mills' expansion into Atlanta will bring 118 new jobs...

Broward County: With the completion of a 69,000-square-foot project in the second quarter, the construction pipeline is now empty... **Charleston:** Food Handler renewed its 200,000-square-foot lease, and a mobile home manufacturer subleased 300,000 square feet from Briggs Plumbing...

Jacksonville: Several quality properties are under contract at substantially better cap rates than have been seen over the past two

years... **Miami:** Merck & Co. is the second major pharmaceutical company in 12 months to announce plans to close local manufacturing operations. By year-end, it intends to sell a 134,000-square-foot facility in Miami Lakes acquired through its merger with Schering-Plough... **Mobile:** Warehouse vacancies and rents continue to soften.

There are no plans for new development at this point... **Nashville:** Most deals done within the last year are either flood relocation deals or companies downsizing. Within the last year or two, rents have fallen from roughly \$6.50 to \$4.00 for shell space... **Orlando:** Downward pressure on prices continued, but the market may be close to bottoming. REO properties will continue to hit the market... **Palm Beach County:** Geo-Global Partners moved into 45,000 square feet of general industrial space. Demand remained weak for warehouse-distribution space...

Raleigh-Durham: Leasing activity remains anemic for both R&D-flex and warehouse-distribution space. Warehouse distribution vacancy remains above 20 percent market-wide but is below 8 percent in the region's premier industrial submarket, Research Triangle Park... **Richmond:** An abundant supply of inexpensive warehouse space from consolidations and the shrinking tobacco warehousing industry will put pressure on rents for Class B- and C properties...

Tampa: Modest signs of recovery include positive absorption for the first time in a year, a slight decrease in the vacancy rate and an increase in activity.

