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Industrial Market Trends

is a newsletter published quarterly by Grubb & Ellis Company. To obtain additional copies or other Grubb & Ellis publications, please contact:

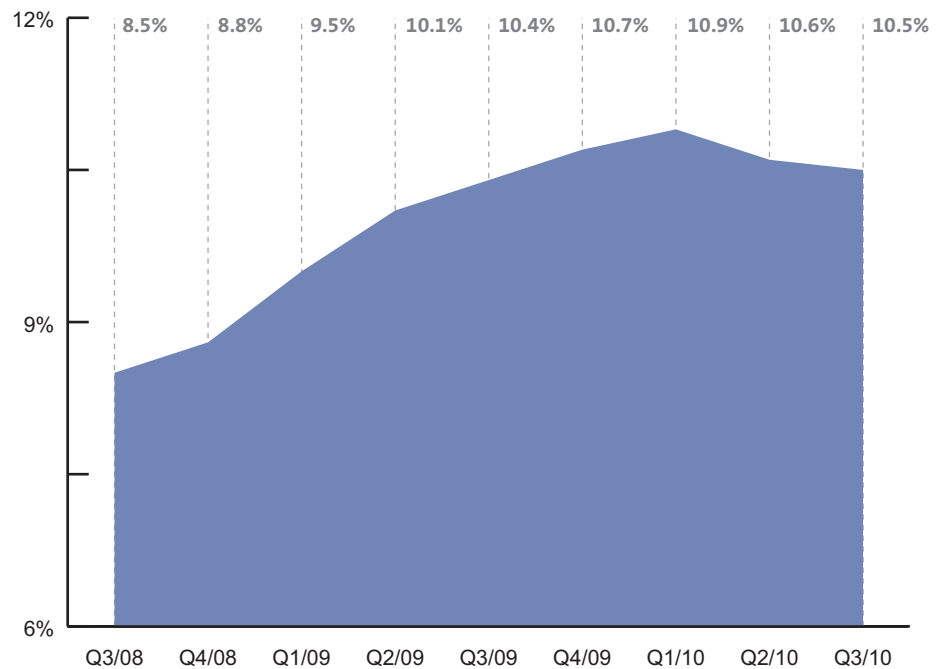
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Fits and Starts

US INDUSTRIAL VACANCY RATE*



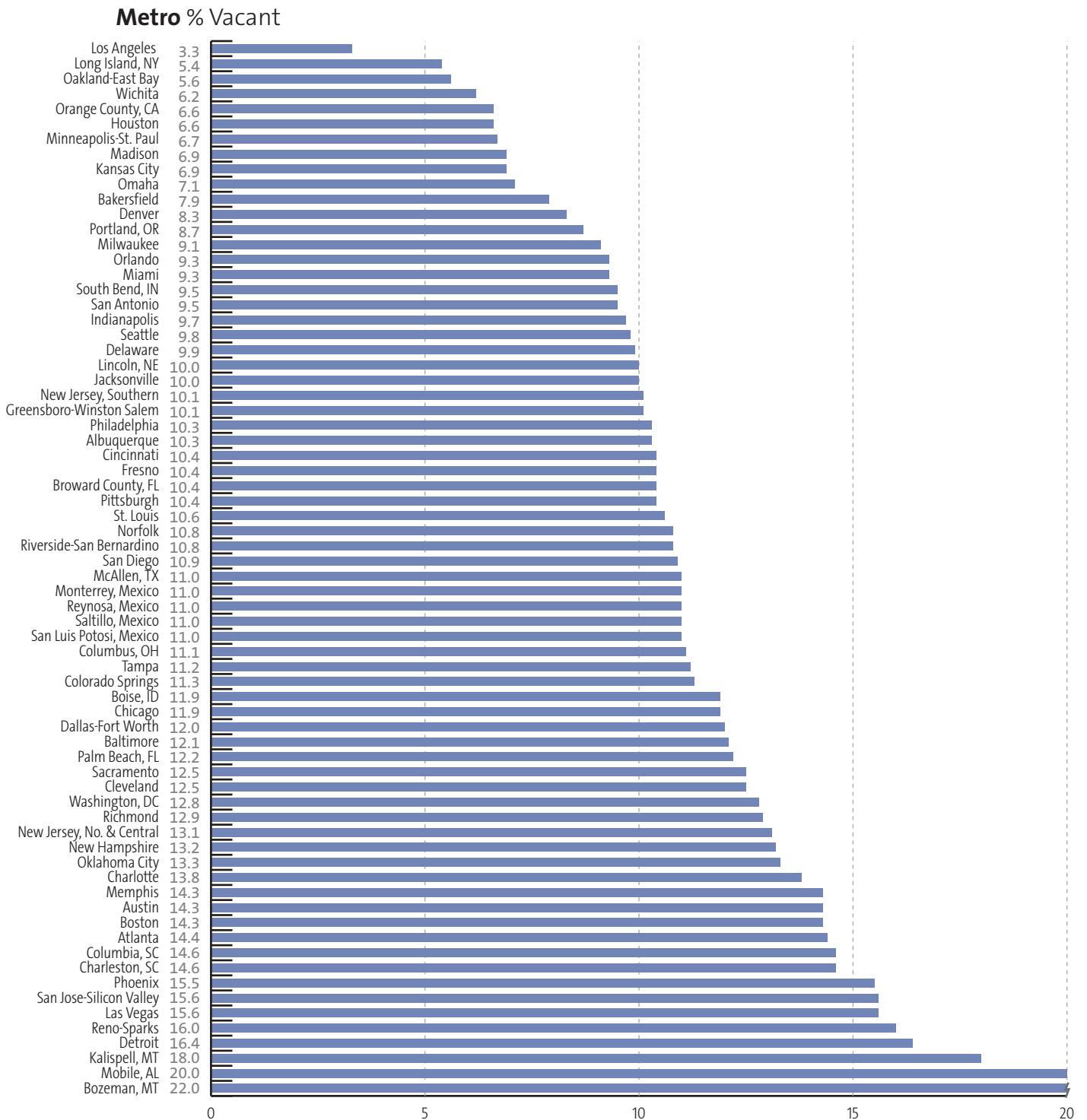
* All product types

THE BOTTOM LINE

The industrial market tightened very modestly in the third quarter after a stronger performance in the second quarter. The vacancy rate declined by a slender 10 basis points, and net absorption was a disappointing 2.4 million square feet. The recovery cycle, though weak, remains intact as befits an economy that is itself recovering at half-speed. Asking rental rates, usually the last indicator to respond in an early recovery cycle, are approaching the bottom but not yet begun to increase. The stop-and-start recovery in the industrial market reflects the inventory restocking cycle that began late last year and then cooled off over the summer. The latest economic readings indicate that the manufacturing sector, retail sales and trade—key drivers of demand for industrial space—continue to expand, suggesting that the recovery in the industrial market is likely to continue.

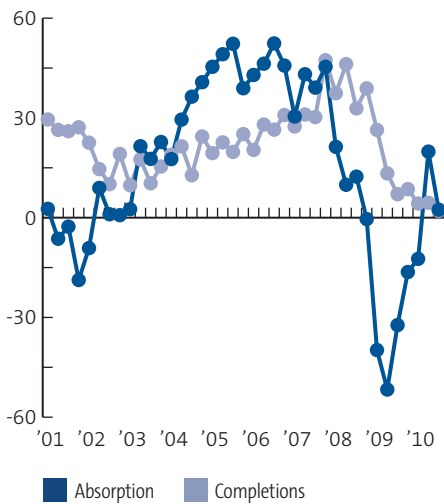
TOTAL MARKET VACANCY RATES

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.

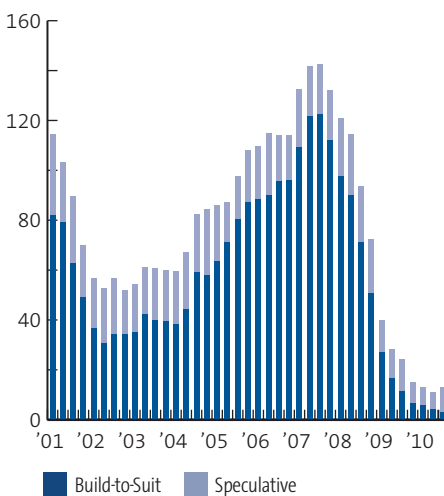


STATE OF THE MARKET

Absorption and Completions
in Millions of Square Feet



Space Under Construction
in Millions of Square Feet



On the heels of a strong performance in the second quarter, the market took a breather in the third quarter as the vacancy rate fell by just 10 basis points to end the quarter at 10.5 percent. Vacancy, though down from its recent peak of 10.9 percent in the first quarter, remains elevated.

- **Los Angeles** retains the lowest vacancy rate in the U.S. at 3.3 percent, a position it has held for a long time due to its shortage of developable land combined with surging container traffic through the ports of Los Angeles and Long Beach.
- **Bozeman, Mont.**—far from the logistics hotspots—posted the highest vacancy rate at 22.0 percent. Bozeman is typical of small industrial markets where construction companies, struggling in the wake of the housing crisis, account for a big slice of the occupier base.
- Markets posting year-over-year vacancy declines greater than 100 basis points, or 1 percentage point, included southern California’s **Inland Empire** (Riverside-San Bernardino-Ontario area), **Miami** and **Broward County** in south Florida, **Houston** and **Denver**.
- Markets posting the largest year-over-year vacancy gains were led by **Las Vegas**, **San Jose-Silicon Valley**, **Oakland-East Bay** and **Fresno**.

Net absorption plunged from a revised 19.9 million square feet in the second quarter to a slim 2.4 million square feet in the third quarter.

- Third quarter absorption was strongest in the **Inland Empire**, **Delaware** and **Houston**, all with at least 1 million square feet of net new absorption.
- Quarterly absorption was weakest in **Cleveland**, **Atlanta** and **Northern and Central New Jersey**, all with negative absorption of 1 million square feet or more.
- On a year-to-date basis, top honors were taken by the **Inland Empire** with a gain in occupied space totaling just above 10 million square feet. Next in line were **Northern and Central New Jersey**, **Greater Philadelphia** (including central and eastern Pennsylvania) and **Houston**. The top four markets all derive strength from nearby ports that have registered strong increases in imports and exports over the past year.
- **San Jose**, **Detroit** and **Atlanta** registered the largest losses in occupied industrial space year-to-date through the third quarter, all in the range of negative 3 million square feet. **Pittsburgh** and **Cleveland** also registered big occupancy losses, although in both markets the losses were related to large, one-time plant closings—Sony in Pittsburgh and Chrysler in Cleveland. Demand remains moderate to firm for modern warehouse space in those two markets.

Only 2.0 million square feet of new space was delivered in the third quarter, a little over half of which was speculative. Projects still under construction at the end of the quarter totaled 13.2 million square feet, of which 3.2 million square feet was speculative. Total space under construction increased by 2 million square feet in the third quarter, suggesting that the construction pipeline is bouncing along the bottom. Spec construction will be minimal until the market firms.

- **The Inland Empire and Charleston, S.C.** both have more than 2 million square feet in the pipeline, followed by **Cincinnati, Philadelphia and Chicago**, each with between 1.4 and 1.8 million square feet under way. Charleston, a relatively small market compared with the others, occupies this rarified position by virtue of a 1.1 million-square-foot build-to-suit project 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 third quarter was \$5.30 per square foot per year triple net, a decline of 0.9 percent from the second quarter and 4.5 percent from the year-ago quarter. Rates for available space ended the quarter at \$5.08 for general industrial (primarily manufacturing), \$4.26 for warehouse-distribution and \$9.23 for R&D-flex. Over the past four quarters, the average rates slipped by 6.8 percent for general industrial, 4.6 percent for warehouse-distribution and 5.2 percent for R&D-flex.

Slow economic growth is expected to constrain the pace of the industrial market recovery, though the recovery should remain intact.

- For warehouse-distribution space, the average asking rent was highest in **San Diego** at \$8.55 followed by **Long Island, Washington, D.C.** and **Broward County, Fla.**, all of which have relatively high land prices and/or constraints on the supplies of available land.
- Tenants in search of a bargain are advised to look in **Northern Indiana, Richmond, Va.** and **Kansas City**, all with asking rates below \$3.

further softening. The Federal Reserve's plan to implement a second round of quantitative easing (QE2) is causing the dollar to weaken, which should make U.S. exports more competitive. Also on the positive side, retail sales appear to be firming modestly, which should put a floor under inventory demand. Overall, slow economic growth is expected to constrain the pace of the industrial market recovery, though the recovery should remain intact.

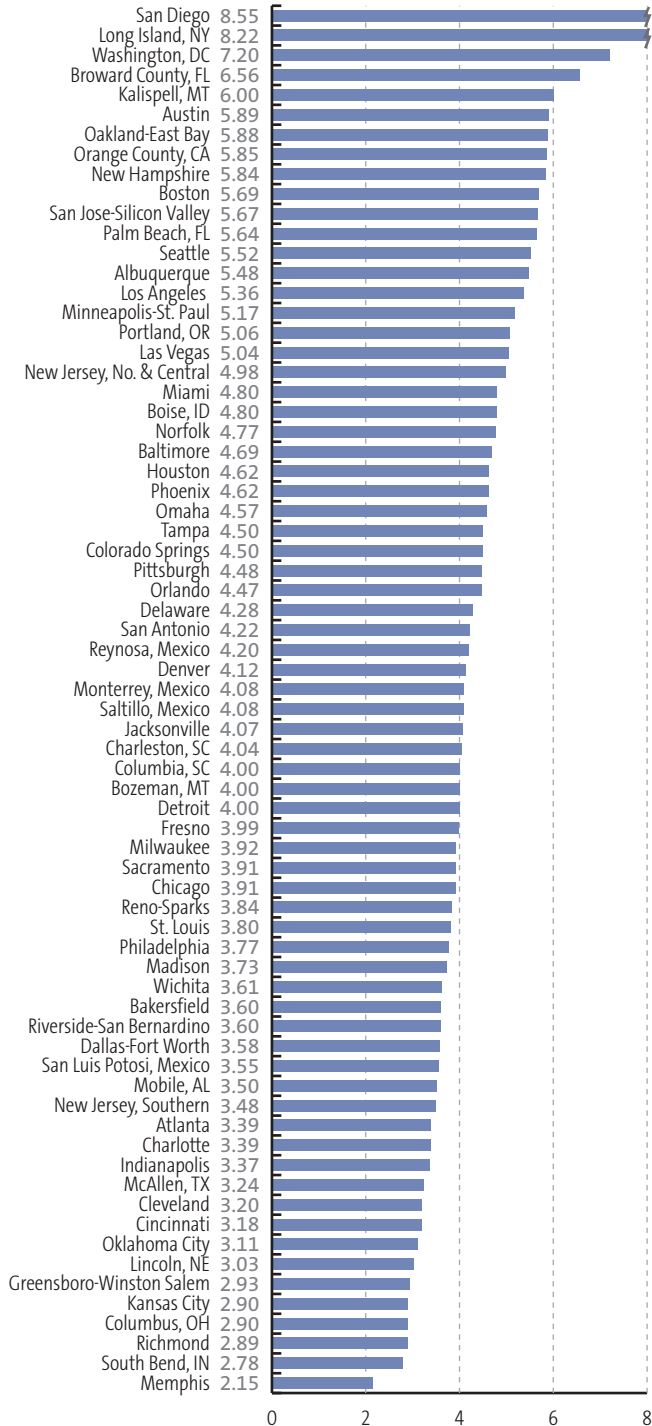
FORECAST

In our *Industrial First Look* email released at the end of the second quarter, we warned that the market was "not out of the woods by a long shot" despite the strong second quarter performance. We said, "The sluggish economy raises the possibility that the industrial recovery could falter in the second half of 2010." That appears to be happening. Second quarter activity most likely was fueled by pent-up demand. According to the Institute for Supply Management's Purchasing Managers Index, the manufacturing sector continues to expand but at a slower rate than in the spring, and other indicators such as industrial production point to

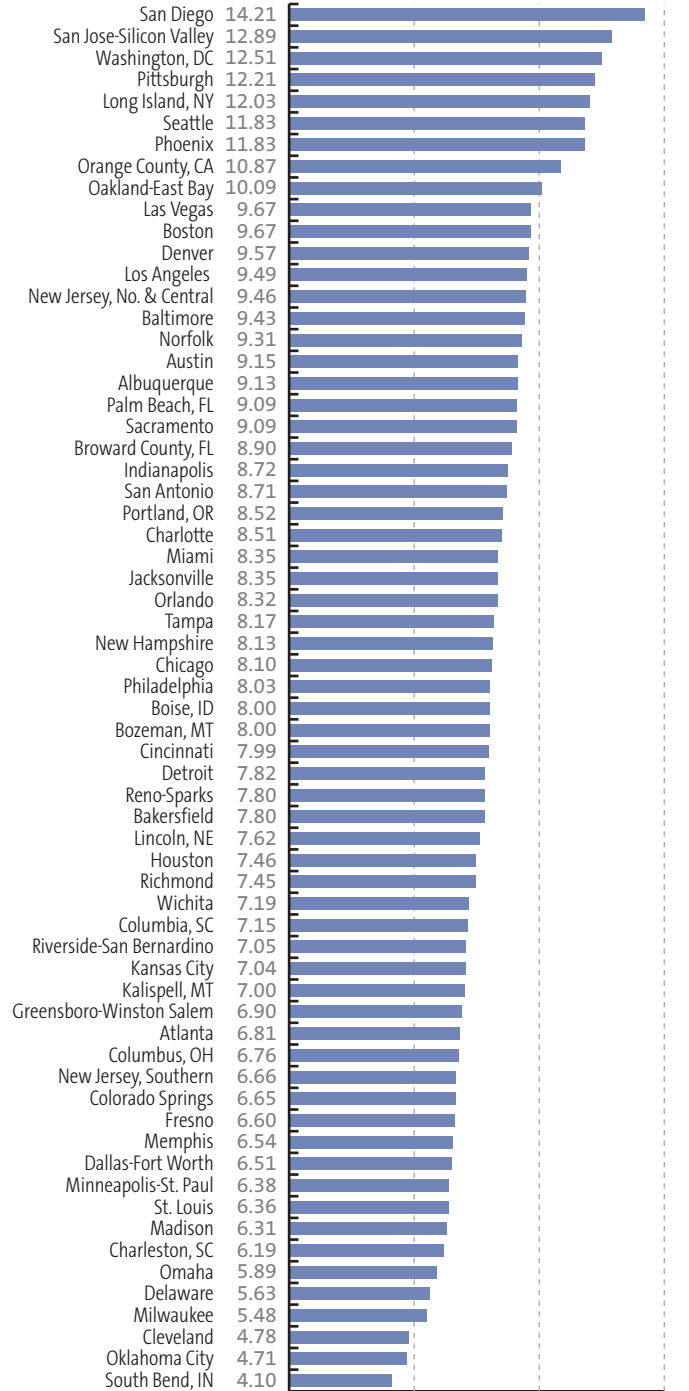
ASKING RENTAL RATES

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: Investment activity continued to increase as evidenced by several noteworthy third-quarter transactions in San Pablo. Look for demand to heat up over the next few quarters... **Portland:** TA Associates sold its 475,000-square-foot portfolio of Portland properties to Industrial Income Trust, a Denver-based REIT... **Sacramento:** Several large tenants took occupancy of their spaces across virtually all submarkets, resulting in 300,000 square feet of positive absorption and a reduction of one full percentage point in the vacancy rate during the quarter... **San Jose-Silicon Valley:** Leases signed for spaces greater than 100,000 square feet increased 11 percent from last quarter. However, nearly 30 percent of the deals done were between 20,000 and 40,000 square feet... **Seattle:** In 2010's largest industrial lease, Quaker Distribution moved into 444,000 square feet at Tacoma's Port Commerce Center. Two tenants, ULine and Performance Team Trucking, signed leases for 282,393 square feet and 179,339 square feet, respectively.



SOUTHERN CALIFORNIA/ PACIFIC SOUTHWEST

Bakersfield: The market is generally stagnant, but reduced prices have attracted a slight increase in sales activity... **Los Angeles:** Price Transfer, a large third-party logistics operator, signed a 64-month lease for a 219,097-square-foot building in Carson. Watson Land Company is the landlord. The market has witnessed a flurry of sales in response to easier financing and falling prices... **Orange County:** Berlin Packaging occupied 86,814 square feet in Santa Ana, helping to reverse negative absorption in the first half of the year... **Riverside-San Bernardino:** Some companies are expanding. Summer Infant Inc., previously based in two

Los Angeles County facilities, committed to a 459,000-square-foot distribution center in Riverside, tripling its space. Chinese Laundry doubled its local operational capacity, and MVP RV bought two manufacturing facilities previously owned by Fleetwood Enterprises...

San Diego: Slight increases in cross-border freight traffic and a rise in overall imports boosted demand for distribution space as evidenced by PartsBandit.com's lease of 107,000 square feet in Otay Mesa.



MOUNTAIN/SOUTHWEST

Albuquerque: Economic uncertainty is preventing tenants from expanding. Landlords are fighting to hold onto their existing tenants... **Boise:** The market has been slow. Recent transactions are short-term with minimal tenant improvements from the landlord... **Bozeman:** New warehouse product absorption is very slow with the downturn of construction-related companies... **Colorado Springs:** Leasing activity, lease rates and values are declining... **Denver:** Absorption was positive for a second consecutive quarter, totaling 681,000 square feet. This year's occupancy gains may approach 2008's absorption of nearly 5 million square feet... **Kalispell:** Warehouse absorption has slowed with rates starting to move down slightly. Development is non-existent, though the market is not terribly overbuilt... **Las Vegas:** For the first time since the third quarter of last year, absorption was positive. Amonix leased 214,030 square feet while Czarnowski Display Service relocated to 214,200 square feet, both in North Las Vegas... **Phoenix:** More large users are moving into the market, beginning to work down the excess space. Look for gradual improvement in 2011... **Reno:** Net absorption year-to-date remains negative due to business downsizing and closures. Look for the market to stabilize by year end.



WEST NORTH CENTRAL/ GREAT PLAINS

Kansas City: Positive absorption appeared for the first time since the fourth quarter of last year, totaling a moderate 416,000 square feet in the third quarter... **Lincoln:** Absorption surged to 305,000 square feet, the strongest quarterly performance in more than two years... **Omaha:** The quarter ended with nearly 97,000 square feet of positive absorption and a decrease in the vacancy rate... **St. Louis:** There has been good activity with tenants extending their leases at today's discounted rates... **Wichita:** Construction of a FedEx distribution center is nearing completion in southwest Wichita.



TEXAS/MEXICO

Austin: Recent leases signed by Goodwill Industries, FTP Productions, and U.S. Courier & Logistics have contributed to a 12 percent increase in leasing activity year-to-date versus the same period last year. The market is on a path to recovery... **Dallas-Fort Worth:** Demand for R&D-flex properties picked up in the third quarter as users absorbed 308,000 square feet, ending a six-quarter string of negative absorption... **Houston:** In the first three quarters of 2010, industrial users have absorbed five times more space than they did for all of 2009... **McAllen:** Rents have slowly increased since the first quarter as space has been taken off the market. While this trend is expected to continue, the market will favor tenants awhile longer... **Monterrey, Mexico:** Third-quarter activity was up sharply, driven by large transactions including Philips taking 369,000 square feet and Polaris taking 425,000 square feet. In the Apodaca submarket, lease rates are on the rise due to recent absorption and limited new construction... **Reynosa, Mexico:** Recent activity has been subdued, but some existing manufacturers are looking at expanding... **Saltillo, Mexico:**

Automotive manufacturing has driven recent activity, some of which is related to model changes. Absorption will generate opportunities for construction starts by year-end, both build-to-suit and speculative... **San Antonio:** Third-quarter demand was spread between the warehouse-distribution and general industrial segments of the market... **San Luis Potosi, Mexico:** New spec construction is limited, though the market is seeing build-to-suit projects. Lease rates on existing space remain under downward pressure with reductions of up to 15 percent possible. The market will continue to favor buyers.



GREAT LAKES/ OHIO VALLEY

Chicago: RTC Industries moved into 503,000 square feet while ALG Direct took 499,000 square feet, both in Romeoville... **Cleveland:** Despite isolated pockets of new, large vacancies, activity has increased especially in more up-to-date facilities. The average vacancy in buildings with at least a 24-foot clear height and built since 1990 is in the low single-digits... **Detroit:** Western Wayne County attracted several large leases and sales. Most notable was Roush Enterprises' purchase of a 124,000-square-foot facility in Livonia... **Elkhart:** RV companies continue to expand product lines. The momentum that began in the second quarter continued into the third quarter with over 573,000 square feet absorbed... **Milwaukee:** User-sales accounted for about one-third of the largest industrial transactions completed in the third quarter... **Minneapolis:** Investment-grade industrial properties have been the focus of activity this year, evidenced by AMB Properties' recent portfolio sale... **South Bend:** Industrial properties that once languished on the market are now beginning to see activity.



NORTHEAST/ MID-ATLANTIC

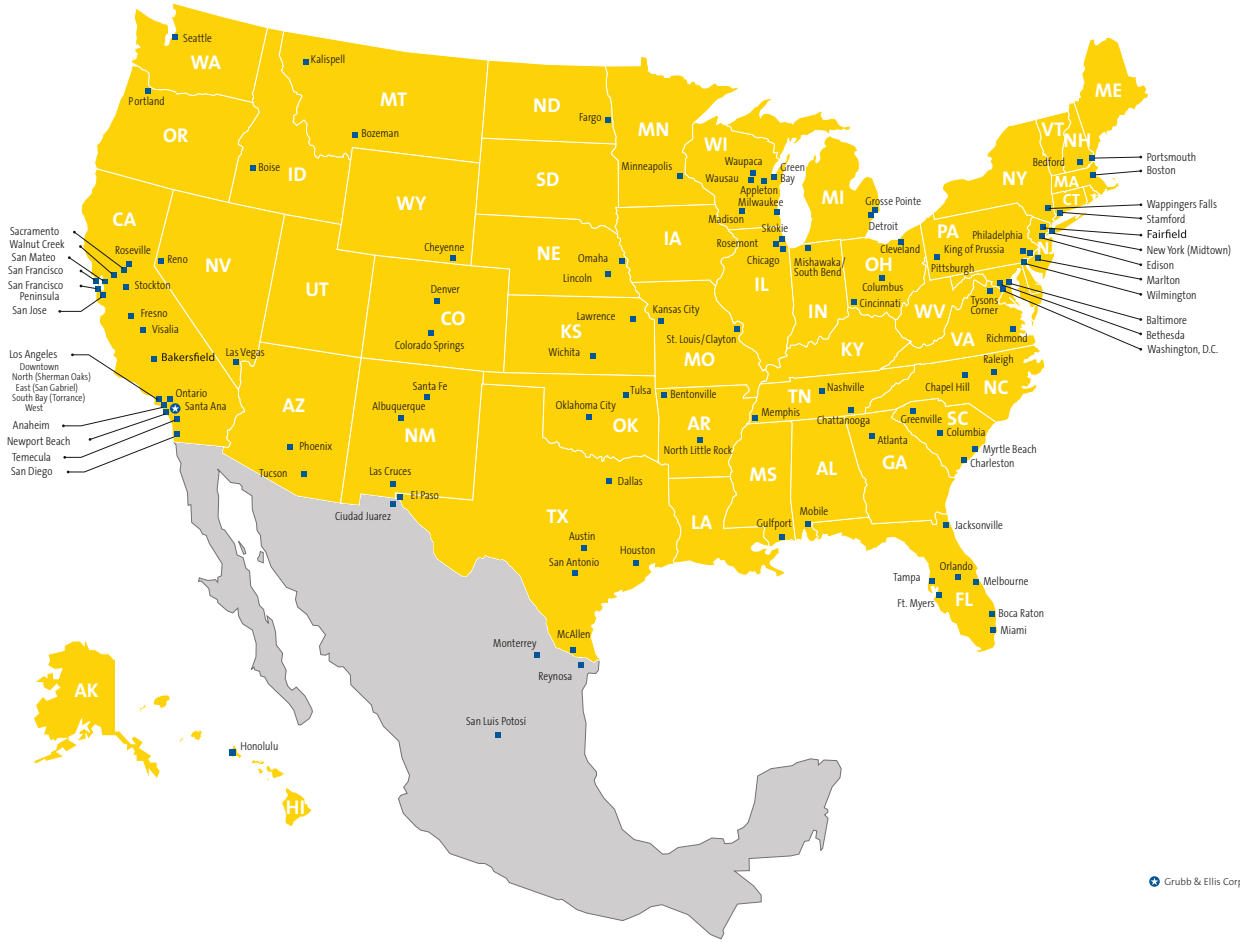
Baltimore: An increase in subleasing activity pushed the vacancy rate lower by 30 basis points... **Boston:** Demand remains tepid at best. Opportunities abound for aggressive tenants to trade up in product without increasing occupancy costs... **Long Island:** The market remained tight despite a 10 basis-point increase in vacancy to 5.4 percent... **New Hampshire:** There has been increased activity from tenants looking for smaller spaces under 10,000 square feet... **New Jersey:** While demand for standard industrial product moderated, a growing appetite for R&D-flex space led to positive absorption... **Philadelphia:** Manufacturing activity in the region has slowed since the beginning of the year. But manufacturers continue to expand, which should help sustain the ongoing economic recovery... **Pittsburgh:** Two transactions that took place in the third quarter may point to a brighter outlook for the steel industry. Two companies partnered to purchase the former Ryerson Steel facility in Carnegie for \$3 million while Alro Steel acquired 15 acres of land for future expansion in the Findlay Industrial Park at Westport... **Washington, DC:** The Route 28 North and I-95 Corridors, which topped the list of submarkets with negative absorption in the third quarter, are currently experiencing the highest levels of tenant interest. The activity is broad-based, coming from a variety of users ranging in size from 5,000 to 50,000 square feet, representing a mix of moves and expansions.



SOUTHEAST

Atlanta: Atlanta is becoming a preferred logistics hub in the Southeast. Six of the largest business deals, which brought more than 3,000 new jobs to the region this year, included port customers such as NCR Corporation, SF Friedrichshafen AG and The Clorox Company... **Broward County:** Ballistic Recovery Systems recently committed to opening its first manufacturing facility in the market, creating 500 new jobs... **Charleston:** Industrial sales transactions remain weak, but buyers, especially users, are back in the market – a big change from 2009... **Jacksonville:** Several quality properties are under contract at substantially better cap rates than have been seen over the past two years... **Miami:** In the largest lease transaction since 2007, Bel, Inc. committed to 343,000 square feet at the Lincoln Logistics Park in Medley... **Mobile:** The warehouse market continued to soften with rising vacancies and declining rents... **Nashville:** Absorption was low but positive in the third quarter totaling 45,000 square feet... **Orlando:** Third quarter absorption exceeded 1 million square feet, suggesting the market has turned the corner... **Palm Beach County:** Modest net absorption and no new construction contributed to the second consecutive quarter of declining vacancy... **Raleigh-Durham:** Flex space is competing aggressively with multi-story office space, where effective rental rates have fallen dramatically. Despite high overall vacancy and limited demand, few Class A options are available for warehouse users, keeping a floor under rental rates... **Richmond:** The buyer/tenant market is holding firm. Users can purchase existing buildings with attractive pricing and historically low interest rates in the range of 5 percent... **Tampa:** Vacancy rates are falling for both larger and smaller spaces across the region.

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Industrial Market Trends United States Q3 2010