

UNITED STATES

260 Franklin Street, 17th Floor
 Boston, MA 02110
 Tel: 617 426-4446
 Fax: 617 426-4443

UNITED KINGDOM

15 St. Mary at Hill
 London EC3R 8EE
 Tel: +44 (0)20 7621 2100
 Fax: +44 (0)20 7623 8793

FOR IMMEDIATE RELEASE

Weak Economic Conditions Are Troubling For The Commercial Space Markets.

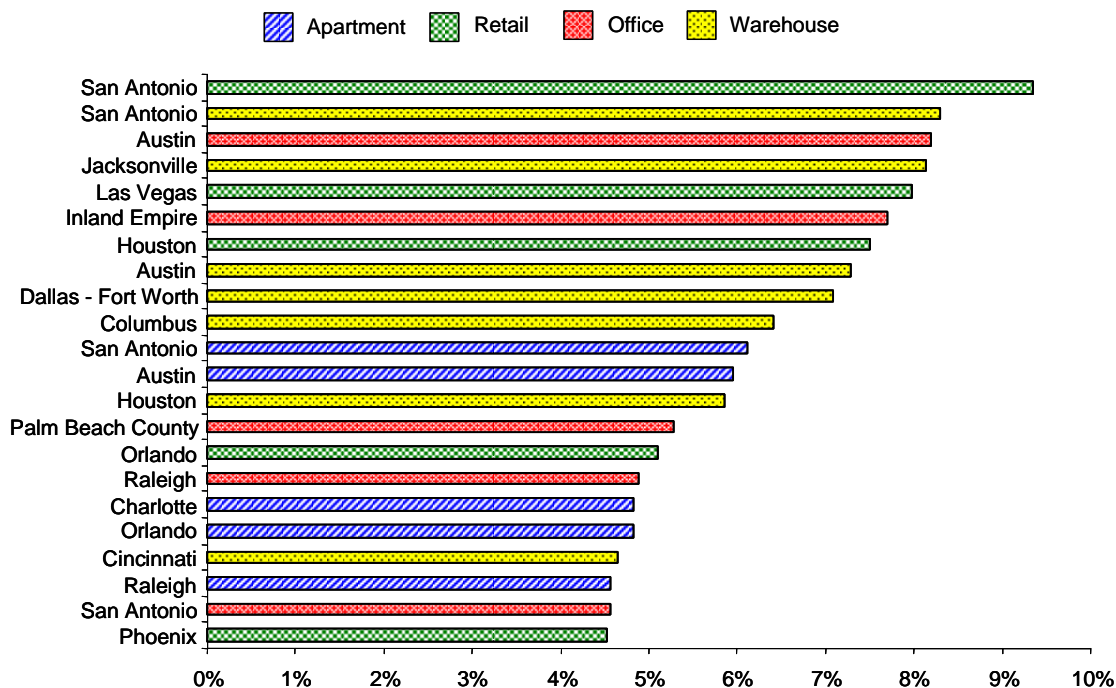
Boston, MA, July 30, 2008 - After all is said and done, a recession will likely be declared for 2008, a dreary outlook for the U.S. economy that will hinder the property type markets through the rest of 2008 and into 2009. Though recessionary conditions should begin to stabilize sometime in the second half of the year, there are numerous downside risks facing the economy. Consumers are still being hammered by falling home values, rising mortgage payments, tightening credit, and soaring oil and food prices. Finally, measuring expansion in the U.S. economy often simply boils down to job growth, and right now, there is none. In the past six months, mounting layoffs have wiped out all the jobs gained in the second half of 2007, leaving year-over-year employment growth (through June) at close to zero.

Every major market will suffer slower demand in the near term, and many markets will endure negative net absorption. Faring the worst will be overheated housing markets, such as Phoenix, Las Vegas, and the Florida markets, as well as markets significantly exposed to commercial and investment banking, such as New York and Charlotte. While demand is pulling way back, the near term supply pipeline is still quite full.

Demand may be retreating, but supply still has some legs ...

Despite the rash of concerns presently facing real estate investors, construction continues to trend upwards. In all property types except warehouse, supply growth will be stronger in 2008. The most notable increase will be in the apartment market, where the conclusion of the condo conversion craze has breathed new life into ground-up rental development, which will rise by 27% over last year, to 141,000 units. Office and retail will also build to lofty levels, with net completions up 17% (106 million SF) and 7% (148 million SF), respectively from 2007. Finally, warehouse supply will actually drift slightly lower this year, but expected completions (142 million SF) will still yield the highest annual supply growth figure (2.4%) of all the property types. Meanwhile, there are individual metros that drastically outpace even these supply growth figures, and Exhibit 1 highlights the outstanding markets.

Exhibit 1: Supply Growth as a Percentage of Inventory in 2008



Source: PPR

Not surprisingly, the pro-growth Texas markets are among the most construction-prone for apartments and will contribute nearly 30% of total net completions across the PPR54 in 2008. Joining Texas at the top in terms of supply growth as a percentage of total stock are a spattering of Southeastern metros (Charlotte, Raleigh, and Orlando), with outsized demographics that lure developers to the sun-soaked region.

In 2008, the top five markets with the greatest office inventory increases as a percentage of total stock are Austin, Inland Empire, Palm Beach, Raleigh, and San Antonio. All will see supply growth greater than 4.5% of stock. Meanwhile, retail supply will be strongest in high-growth metros with sweet demographics and low barriers to supply - San Antonio, Las Vegas, Houston, and Orlando are near the top of that list.

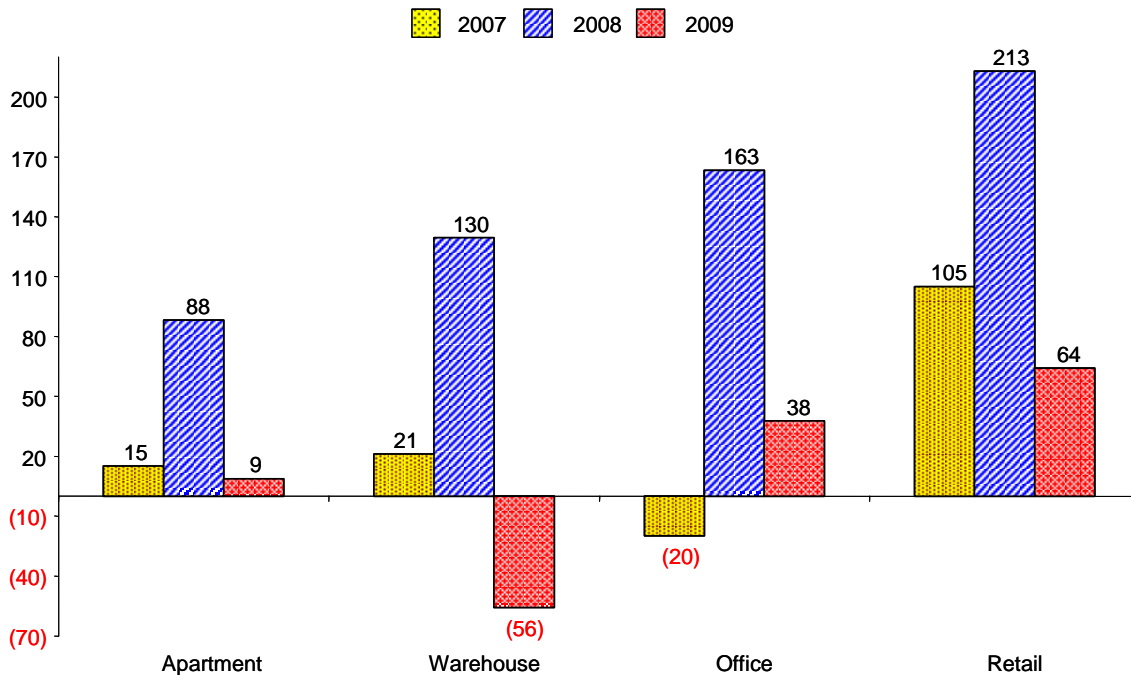
Warehouse demand growth will actually be the strongest of all the property types this year, but developers have grown overzealous. You can work a good horse to death, and that is exactly what is happening in several metros, as supply additions will easily surpass demand. Supply growth will be strongest in some of the national distribution hubs (Dallas - Forth Worth, Columbus, and Houston), as well as in smaller growth markets (San Antonio, Jacksonville, and Austin).

The heightened level of development in 2008 is unsustainable, and given the state of the economy and the floundering capital markets, supply deliveries will recoil considerably in 2009. Thanks to relatively short construction timelines, warehouse developers can more quickly switch off the supply faucet, and supply growth for this property type will shut down the fastest, with deliveries expected to fall by nearly 60% in 2009. Supply growth will also fall in retail (40%), office (20%), and apartment (15%).

Not surprisingly, vacancies are rising in all four major property types ...

Strong levels of supply are coming in 2008, and demand expectations are moderate or negative for each of the four property types. The combination of these two factors will lead to a swift uptick in vacancies in 2008 (and continuing into 2009 for some property types). As shown in Exhibit 2, retail will rise the most, with an increase of 213 basis points. Office (163) and warehouse (130) will follow, with apartment enduring a somewhat smaller increase (88 basis points).

Exhibit 2: Annual Basis Point Change in Vacancies



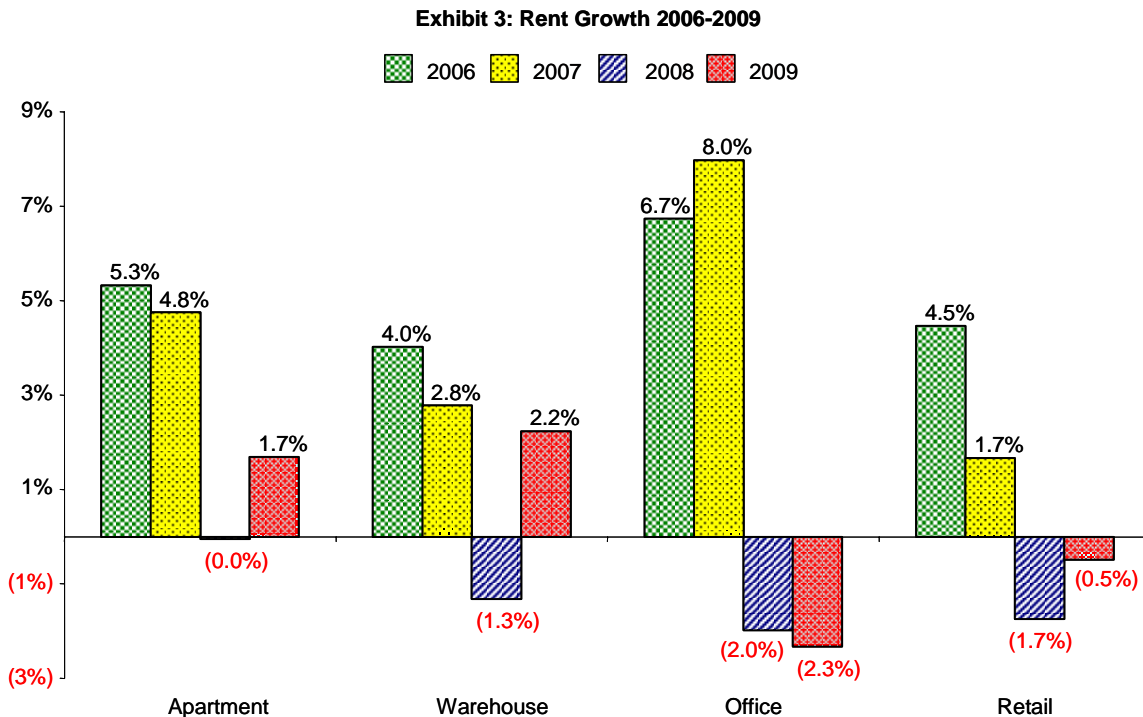
Source: PPR

Apartment also has the most markets (nine) that will enjoy declining vacancies in 2008, mostly slow-moving Midwest markets (Minneapolis, Indianapolis) or supply-constrained markets (San Francisco, San Jose). Speculative deliveries amid a negative demand environment will cause office vacancies to rise in every market but one (Portland - where vacancies will be flat). LA's suburban outpost, the Inland Empire, will get it the worst (with vacancies lifting 750 basis points in 2008). But some major markets (like New York and Washington D.C. - NoVa - MD) will also suffer worse vacancy increases than the PPR54 average.

Looking ahead to 2009, apartment, office, and retail will all continue to suffer from rising vacancies (albeit at a much slower rate). Demand will remain slow through at least the first half of that year, and supply concerns will linger on, depending on the market. However, the warehouse market will turn itself around rather quickly, with vacancies dropping by 56 basis points in 2009, as the recovery begins.

Tenants will finally regain some power in 2008 ...

The perfect storm of slowing demand, excessive supply, and rising vacancy rates has put landlords back on their heels. They will be forced to return some of their past gains over the next two years as power shifts back to the tenants (see Exhibit 3). In all property types, annual rent growth will slow severely from first quarter levels. The worst idler will be office, losing 2% in 2008, with retail not far behind, at a 1.7% decline. Losses for these two property types will also stretch into 2009. Even warehouse rents will fall by 1.3% through 2008. Apartment rents will perform the best, but that's not saying much, as growth will be negligible for the year.



Source: PPR

Given current weak economic conditions and their impact on commercial real estate markets, market selection is more important than ever. For example, retail rents will suffer the most in Phoenix and Nashville, while Seattle and Honolulu will have some of the largest gains. Rent growth in Houston office will be more than six full percentage points above that in the next closest metro, at 12%. Changing fundamentals will also have a significant impact on value growth (or more often, losses). With such dramatic differences in performance, it's important to know your markets, and PPR can help you decide what markets are right for your strategy!