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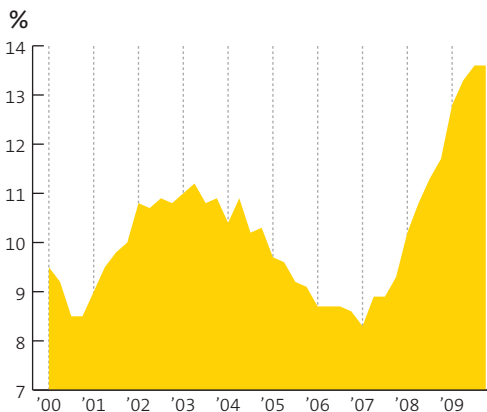
## State of the Market

The vacancy rate for logistics space leveled out in the fourth quarter at 13.6 percent, identical to the third quarter. This makes logistics one of the first property types to hit bottom. Other leasing market indicators are not quite as sanguine, however. Demand was still negative in the fourth quarter (barely so) as occupied space slipped by 1.4 million square feet while developers delivered 11.4 million square feet of new space, the lowest level in five years. Declining rental rates helped put a floor under demand. The average asking rental rate for logistics space available at year-end 2009 was \$3.79 per square foot per year, triple net. This was off by 10 percent from the peak of \$4.21 in the fourth quarter of 2007, and it was the lowest rate since the first quarter of 2003. Effective rates have fallen considerably more over this period, down by 31 percent as landlords negotiated down from asking rates and added valuable concessions such as periods of free rent in order to keep their space occupied.

Demand was strongest for Class A logistics space, offering top-of-the-market functionality, systems and finishes. Despite the depth of the recession and its devastating impact on freight movements, tenants and owner-users absorbed 14.1 million square feet of Class A logistics space last year. Much of this absorption came at the expense of Class B and C space as occupiers took better space at a discount. Class B and C facilities gave up a combined 39.9 million square feet in occupancy. As a result, the vacancy rate for Class A logistics space actually declined to 16.6 percent in the fourth quarter from 17.2 percent in the third quarter.

Vacancy rates for Class A logistics space were lowest in Los Angeles at 4.4 percent and highest in Portland at 37.3 percent versus the U.S. average of 16.6 percent. Despite the low vacancy rate in Los Angeles, asking rental rates for Class A space slipped by 15 percent last year. It is not unusual to see rents in very tight markets spike when demand surges and fall sharply when demand pulls back. Such markets can be volatile on the way up and the way down. *(continued on page 3)*

### Downhill from Here



**US Logistics Vacancy Rate**

All classes of logistics space

#### Logistics Market Trends

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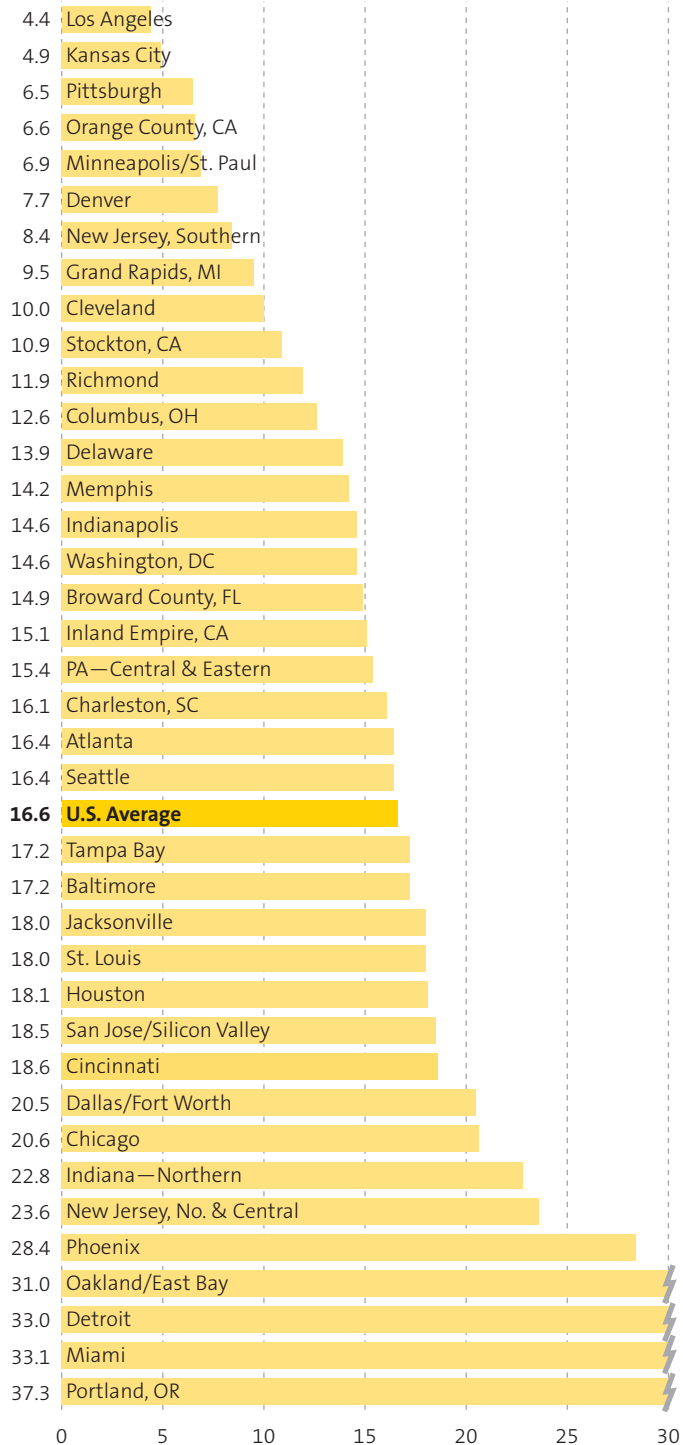
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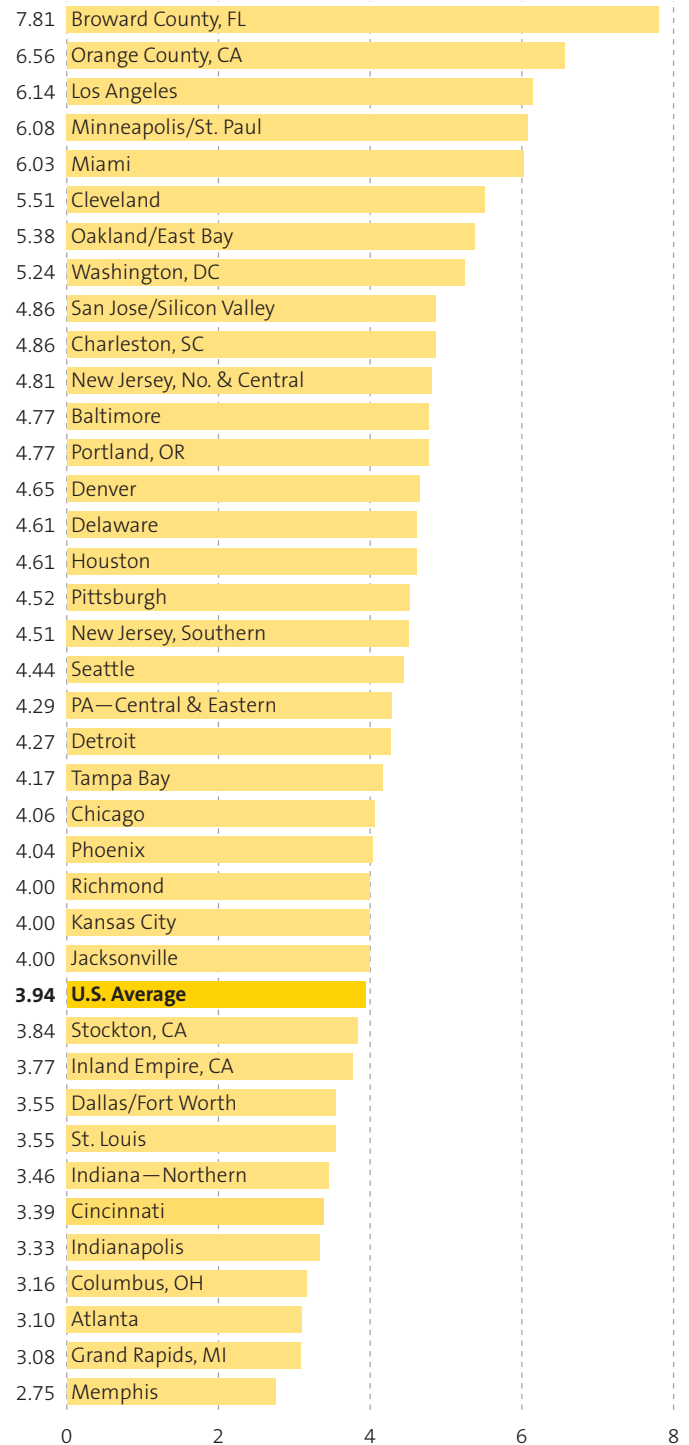
# Class A Logistics Market Vacancy and Rental Rates

**Note:** Vacancy and rent data refer to Class A logistics buildings with minimum size thresholds of 100,000 square feet. Inventory includes multi-tenant, single-tenant and owner-occupied space. Rental rate data refer to space that is available for lease 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.

## % Vacant



## \$ Asking Rent



It is not too surprising that logistics space, particularly higher quality Class A space, is one of the first commercial real estate categories to bottom out. Gross domestic product began growing again in the third quarter of 2009. Although the labor market has yet to rebound, the linkage between employment growth and demand for logistics space is less direct than it is for the office, retail and apartment markets. Employment growth is tied to retail spending, and retailers

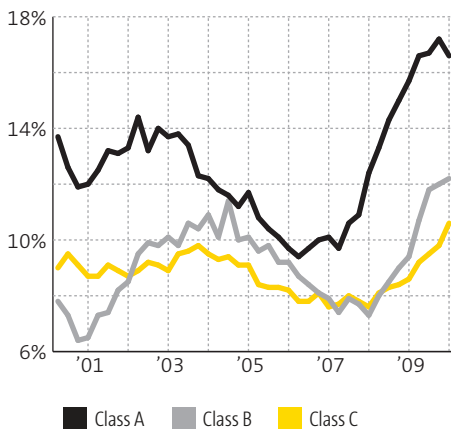
account for about one-quarter of the occupancy in logistics space with 3PL companies serving retailers accounting for more. But there are other drivers of demand for logistics space besides retail sales including business capital spending, manufacturing activity, inventory rebuilding and global trade, and these have been quicker to bounce back than employment growth. Even consumer spending is showing signs of a comeback. The International Council of Shopping Centers reported that U.S. chain store sales rose by 3.7 percent in February, the best showing since November 2007 just before the recession began.

With oil prices up substantially from their lows of last year, distributors are likely to resume their quest for more but smaller distribution centers, helping them get closer to their final customers and thereby reducing trucking costs. Markets such as Kansas City, Minneapolis, Columbus, Nashville, San Antonio, Denver and Cleveland are likely to see more interest from distributors and logistics companies as energy prices continue to rise.

Expect leasing market fundamentals such as vacancy rates and net absorption to firm up this year for logistics space, although rental rates are unlikely to bottom out before early 2011.

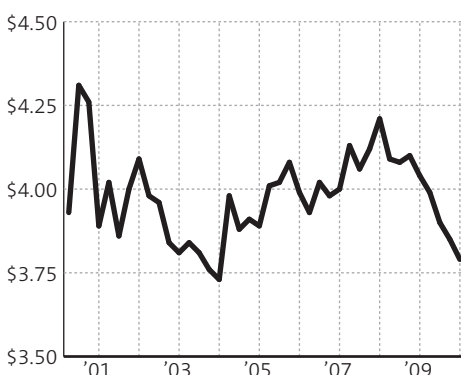
### Logistics Vacancy Rate

By Class of Space



### Logistics Rental Rate

Weighted Average Asking Rate NNN



## Logistics Building Classifications

### Class A Buildings

- State-of-the-art functionality, systems and finishes
- Minimum of 28-foot clear height for buildings over 100,000 square feet
- Excellent truck door/building ratio (minimum of 1/7,500 square feet)
- Excellent truck yards with minimum of 135-foot truck turning radius
- Minimum of .60/3000 or ESFR sprinkler system

### Class B Buildings

- Some functional obsolescence
- Fair to good building systems
- Minimum of 22-foot clear height for buildings over 100,000 square feet
- Adequate loading capability
- .33/3000 to .45/3000 sprinkler system
- Minimum of 110-foot truck turning radius

### Class C Buildings

- Considerable functional obsolescence
- Less than 110-foot truck turning radius
- Below 22-foot clear height for buildings over 100,000 square feet
- Insufficient number of truck doors
- Non-calculated fire sprinkler system

# Market in the Spotlight

## Greater Philadelphia Region

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### Demographics and Access

The Philadelphia region's legacy as a center for trade and commerce dates back to the origin of the United States when it was the commercial hub of the "New World." Fast forwarding 300 years, the region remains a strategic node in the nation's distribution network given its infrastructure, compelling demographics and proximity to dense population centers. The Philadelphia MSA is the fifth most populous region nationally, and it offers close proximity to multiple major domestic population centers up and down the eastern seaboard and to a multitude of densely populated inland markets. Forty-six million people live within 200 miles of Philadelphia, and 100 million people live within a one day drive.

In addition to a well developed highway network, the region's extensive rail network includes three Class 1 railroads. Canadian Pacific, CSX and Norfolk Southern link their extensive rail systems directly to The Delaware River Port Complex, one of world's largest freshwater ports. Private and public capital is being deployed in new infrastructure projects. There is a plan to dredge a 102-mile stretch of the Delaware River from 40 feet to 45 feet enabling the region's port complex to accommodate the larger vessels that dominate the world's shipping channels. Norfolk Southern has committed to build out its \$2.5 billion Crescent Corridor, expand its intermodal facility at the Philadelphia Navy Yard and break ground on a new \$95 million, 200-acre facility in Green Castle, Pa. along I-81 in the Central Pennsylvania submarket.

### Logistics Market Overview

The Philadelphia region, inclusive of eastern Pennsylvania, southern New Jersey and northern Delaware is home to one of the nation's largest industrial markets with over 717 million square feet of competitive inventory. Grubb & Ellis tracks a 261 million-square-foot subset that is categorized as logistics space. Half of the regional logistics inventory is Class A, with its increasing share driven by the 84 million square feet of product that was delivered in the past 10 years.

Like other markets across the country, the Philadelphia metro logistics market felt the effects of sluggish trade volume, depressed retail sales, reduced manufacturing activity and declining inventories, all byproducts of the recent recession. From year-end 2007 through year-end 2009, the vacancy rate in the regional logistics market increased from 10.2 to 12.9 percent, mirroring the trend at the national level both in terms of direction and degree of relative change. This increase was driven more by the delivery of new space rather than a collapse in demand. During the past two years, the market recorded only one quarter of negative absorption – the first quarter of 2009. Net absorption during this period totaling 7.7 million square feet was overwhelmed by 17.7 million square feet of new supply added to the inventory. The average asking rental rate for Class A and B logistics space ended the year at \$4.29 and \$4.06 per square foot per year, triple net, with Class C space at \$3.50.

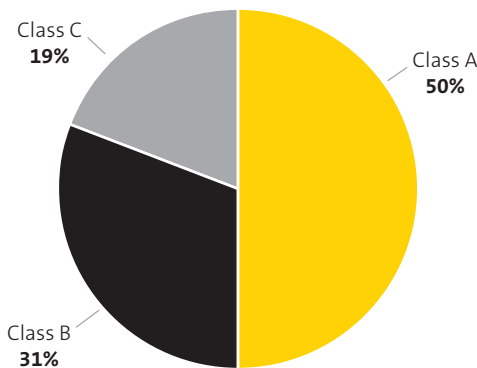
## Logistics Inventory by Size Category

Greater Philadelphia Region

Size Category (SF)	# Buildings	Total SF
100,000–250,000	496	75,996,997
250,000–500,000	213	75,685,494
500,000–750,000	79	46,773,597
750,000 +	59	62,853,575
<b>Totals</b>	<b>847</b>	<b>261,309,663</b>

## Logistics Inventory by Class of Space

Greater Philadelphia Region



### KEY FINDINGS

Analysis of demand parameters during the past two years confirmed the following: Well located, bigger, newer buildings dramatically outperformed the broader market

**QUALITY SELLS:** Class A logistics space accounted for 11.3 million square feet of positive absorption, while Class B and C properties combined for 3.6 million square feet of negative absorption.

**NEWER IS BETTER:** Buildings delivered after 2007 absorbed 13.3 million square feet while buildings delivered before then experienced negative absorption of 6 million square feet.

**LOCATION, LOCATION, LOCATION:** The three submarkets arrayed along the I-81 and I-80 corridors – Central Pennsylvania, Lehigh Valley and Northeastern Pennsylvania – accounted for 80 percent of all new product delivered in the past 10 years. Absorption in these submarkets since 2007 approached 8 million square feet while all remaining submarkets combined registered a negative 250,000 square feet.

**BIGGER IS BETTER:** Buildings 500,000 square feet and larger accounted for two thirds of all space delivered since 2007. They absorbed 9.1 million square feet while buildings less than 500,000 square feet lost approximately 1.5 million square feet of occupancy. The average size of buildings delivered from 2007 to 2009 was 47 percent larger than the period from 1997 to 1999 and 110 percent larger than 1987 to 1989. This is evidence of supply chain optimization models that favor fewer but larger distribution points. Ninety percent of all buildings delivered since 2007 have a clear height of at least 30 feet.

**THE SWEET SPOT:** The Class A market in the 500,000 to 750,000-square-foot range posted a vacancy rate of 5.6 percent at year-end 2009, well below the market average.

The most significant concentration of logistics product in the region is in three submarkets along the I-81 and I-80 corridors. To the west, the Central Pennsylvania submarket, and to the north, the Lehigh Valley and Northeastern Pennsylvania clusters are home to over 160 million square feet, or 60 percent of the specialized logistics inventory in the Philadelphia region. Developers in the Central PA submarket added nearly 9 million square feet of product since the beginning of 2007. Unfortunately, demand cooled during this period as only 2.5 million square feet was absorbed. Currently, tenants in the market with 100,000 to 500,000 square-foot requirements have the negotiating leverage given the 50 or so spaces available. But larger occupiers have very few options as only three buildings can accommodate requirements greater than 500,000 square feet, and only two offer over 750,000 square feet.

Northeastern Pennsylvania is a rapidly emerging submarket where 12.4 million square feet of logistics space has been added during the past three years. This was due in large part to the submarket's most active developer, Mericle, which developed more than 5.6 million square feet of product in its CenterPoint Commerce & Trade Park as well as in the Humboldt Industrial Park. The gamble seems to have paid off considering that almost 80 percent of the space is occupied, which is impressive considering that the majority of the construction was speculative.

# Market Quick Takes

## Regional Overview



### **NORTHERN CALIFORNIA/ PACIFIC NORTHWEST**

**Oakland-East Bay:** The Port of Oakland managed to sustain export activity through 2009 with stronger performance anticipated in 2010. Growth at the Port should translate into increased demand for industrial space...

**Portland:** Several new regional distribution centers including Colgate Palmolive, Home Depot, Case New Holland and Mor Furniture have recently been leased. These tenants were attracted by aggressive lease rates,

state-of-the-art facilities and generous concession packages... **San Jose-Silicon Valley:** Warehouse product, which saw significant clean technology deals in the third quarter,

did not fare as well in the fourth quarter as more space was returned to the market...

**Seattle:** Even though the region is slowly beginning to emerge from the recession, vacancy will likely continue to increase for several more quarters as firms regain their economic footing. Now that some semblance of stability has returned to the broader economy, expect canny tenants to leverage their increased market power...

**Stockton:** The San Joaquin Valley has experienced great volatility in the last six months. Several large new tenants relocating or expanding in the market include General Mills (740,000 square feet), O'Reilly Auto Parts (520,000), Del Monte (258,000), Frito Lay (247,000) and Ball Container (202,000). On the negative side, the NUMMI auto plant in Fremont is scheduled to close, which will cause a ripple effect among parts suppliers in the San Joaquin area. Within some size segments, there are opportunities to obtain a lease rate significantly below the asking rate. In other size ranges, the rates are more stable.



### **SOUTHERN CALIFORNIA/ PACIFIC SOUTHWEST**

**Inland Empire:** After rampant development in recent years, tenants have many options for first-generation Class A buildings at rates far lower than older spaces in neighboring markets. With the monthly average asking rental rate for warehouse space down 22 percent from 2008, big box transaction activity is beginning to pick up... **Los Angeles:** In-bound loaded cargo volume, one of the principal drivers of demand for logistics space, fell 17 percent in 2009 compared with 2008. The slack demand for logistics space is reflected in the rate of decline in asking rental rates; Class A and B rates slipped 15 percent and 23 percent, respectively, versus 2008 while effective rates slid even further. For January 2010, in-bound volume was down a much improved 5 percent over January 2009, indicating that activity is bottoming... **Orange County:** Most companies requiring large amounts of warehouse space have turned to the Inland Empire where space is ample and cheap. But not all: Saddle Creek, which provides warehousing, transportation and logistics services, leased 626,304 square feet in Orange County's Buena Park, which is closer to the ports than the Inland Empire. The deal shows that Orange County is still a viable logistics location. Margins are very tight, and occupiers are looking for highly discounted rents and, in most cases, a shorter term.



### **MOUNTAIN/ SOUTHWEST**

**Denver:** Demand remains strong for Class A distribution product as numerous large deals were inked in 2009. Newer, more efficient product, which attracted the majority of these transactions, absorbed 456,000 square feet last year, more than twice as

much activity as in older properties. Rental rates have proved to be stickier for newer product with landlords giving up less ground compared with older properties...

**Reno:** Land sales are nearly nonexistent due to a lack of available financing.



### **TEXAS/GREAT PLAINS**

**Dallas-Fort Worth:** Although construction has ground to a halt, developers still managed to deliver more than 10 million square feet of warehouse space last year. The glut of new supply coupled with over 7 million square feet of sublease space has forced landlords to offer aggressive rental rates and concessions. Logistics companies with an immediate requirement will enjoy a broad choice of spaces... **Houston:** Diminished leasing demand and excess space deliveries last year pushed vacancy to a five-year high. Within the past two years, developers have delivered over 13 million square feet of warehouse space, nearly half of it concentrated near the Port of Houston and IAH Airport. The completion of the Panama Canal in 2014 is predicted to triple freight tonnage at the Port of Houston... **Kansas City:** Coleman Outdoor Products recently completed its 1.1 million-square-foot distribution facility in Gardner, Kan. While the pace of large transactions has slowed, some companies continue to search for sites to expand in the near term. Limited speculative construction has kept vacancies in check... **St. Louis:** Rental rates are near the bottom and are unlikely to fall much further, but vacancy rates will continue to rise in 2010 as tenants shed unused space. All development activity remains on hold.



## GREAT LAKES/ OHIO VALLEY

**Chicago:** UTi Integrated Logistics renewed its lease of 593,000 square feet in Aurora, extending the lease from mid-2010 through 2013. Several other logistics company renewals took place in the last few months, including Midwest Warehouse & Distribution System renewing 350,000 square feet, Exel Direct renewing 110,000 square feet, and Caterpillar Logistics renewing 295,000 square feet. Demar Logistics leased 90,000 square feet in Carol Stream, a block away from its current warehouse, gaining access to over a dozen more trailer stalls... **Cincinnati:** The contraction of global supply chains resulted in numerous large blocks of vacant space in the region's two primary distribution hubs. Many indicators point towards a slow rebound in 2010. As economic conditions improve, logistics tenants will have multiple spaces from which to choose and the upper hand in negotiations... **Cleveland:** Tenants are either taking more space at the same rate or moving up in quality without much of a price increase... **Columbus:** With distribution space accounting for more than 90 percent of the total industrial inventory, Columbus is well-suited for logistics operations. Third party logistics providers account for more than half of the tenants in this market. Central Ohio is accessible through major interstate highways 70 and 71, both CSX and Norfolk Southern rail lines, and three intermodal yards capable of over 600,000 lifts per year... **Detroit:** Continued investments in alternative energy and advanced battery systems are forming a new base of tenants. Logistics vacancy continued to rise in 2009, but the rate of increase slowed late in the year... **Grand Rapids/ West Michigan:** New speculative construction has come to a halt. Effective rental rates will slide further in 2010, and sales prices will reach historic lows... **Indianapolis:** Recent tenant activity seems to indicate a more positive outlook for 2010... **Minneapolis:** After several very strong years, the distribution market softened in

late 2009 with more space expected to come back on the market in 2010. Tenants will have strong opportunities over the next 12 to 18 months... **South Bend:** With companies keeping a close eye on expenses, many have closed their smaller distribution centers throughout the Midwest, leaving a patchwork of empty properties.



## NORTHEAST/ MID-ATLANTIC

**Baltimore:** Market activity has increased slightly, but rental rates are still dropping, and concessions continue to rise. Vacancy rates are also still increasing, but with no new construction, they are expected to level out in the near future...

**New Jersey:** An increased appetite for big-box warehouse space led to nearly 673,000 square feet of absorption in the Exit 8A submarket during the final quarter of 2009. Despite this recent uptick in demand, more than 12.3 million square feet of warehouse space remains available in the submarket...

**Philadelphia:** Proving its role as a major logistics node on the eastern seaboard, the Central Pennsylvania submarket absorbed over 2 million square feet of warehouse space in the fourth quarter, erasing losses incurred at the beginning of the year and pushing absorption into the black for 2009. This trend is expected to continue... **Pittsburgh:** At Findlay Industrial Park, The Appliance Dealers Cooperative opened its new 155,000-square-foot warehouse, and The Okonite Company took occupancy of 80,000 square feet... **Washington, D.C.:** While activity has picked up sharply along the I-81 and I-95 corridors, no significant transactions have yet occurred. New industrial space still floods the market, keeping rental rates consistently low.



## SOUTHEAST

**Atlanta:** Absent significant business expansion or relocation activity, more occupancy losses are expected in 2010, particularly in the first half of the year...

**Broward County:** In Pompano Beach, two warehouse-distribution facilities totaling 225,000 square feet that were built at Premier Turnpike Park in 2009 have yet to find a single tenant... **Charleston:** Maersk Shipping Company, the Port of Charleston's largest customer, renewed its contract until 2014, which should coincide with the completion of the Panama Canal reconstruction. TBC Tire Kingdom signed a lease to occupy a 1.1 million-square-foot build-to-suit distribution facility to be completed by year-end...

**Jacksonville:** The market is stable thanks to growing port traffic and the absence of overbuilding. Low lease rates and aggressive terms are winning the deals... **Memphis:** The market absorbed 1.3 million square feet in the fourth quarter following four consecutive quarters of negative absorption...

**Miami:** The decline in trade between the U.S. and Latin America has chilled demand for warehouse space. The most recent trade figures indicate some stabilizing... **Nashville:** The market remains stagnant. Vacancy, hovering around 11 percent, is not expected to vary much this year... **Richmond:** Pressure on rates is strong. Leases are being completed at 20 to 40 percent below the published triple net asking rates.

# GRUBB & ELLIS OFFICE LOCATIONS



## Logistics Market Trends

United States Q4 2009