



## The Lee Industrial Brief

Q2  
2016

- 1 LEE OVERVIEW
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**155%**  
increase  
in transaction  
volume over 5 years

**\$12+ billion**  
transaction volume  
2015

**Ranked 2nd**  
june 2016  
Commercial Property Executive  
(2016 Top Brokerage Firms)

**870**  
agents  
and growing  
nationwide

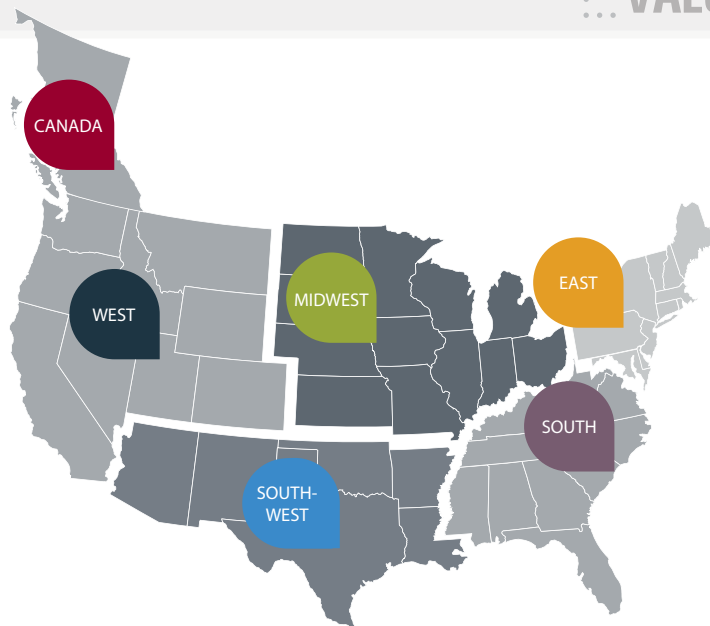
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Our agents understand real estate and accountability. They provide an integrated approach to leasing, operational efficiencies, capital markets, property management, valuation, disposition, development, research and consulting.

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OFFICE  
INDUSTRIAL  
RETAIL  
INVESTMENT  
APPRAISAL  
MULTI-FAMILY  
LAND  
PROPERTY MANAGEMENT  
VALUATION & CONSULTING



THE POWER OF THE  
LEE NETWORK

Irvine, CA  
Orange, CA  
Newport Beach, CA  
Ontario, CA  
Riverside, CA  
Los Angeles, CA  
Industry, CA  
Carlsbad, CA  
Stockton, CA  
Pleasanton, CA

West LA, CA  
Sherman Oaks, CA  
Central LA, CA  
Temecula Valley, CA  
Victorville, CA  
Calabasas, CA  
Los Olivos, CA  
San Luis Obispo, CA  
Ventura, CA  
San Diego, CA

Reno, NV  
Oakland, CA  
Antelope Valley, CA  
Santa Barbara, CA  
Palm Desert, CA  
ISG- LA, CA  
Boise, ID  
Long Beach, CA  
Denver, CO

Phoenix, AZ  
Dallas/Ft Worth, TX  
Houston, TX

Chicago, IL,  
St. Louis, MO  
Southfield, MI  
Madison, WI  
Indianapolis, IN  
Greenwood, IN  
Cleveland, OH  
Columbus, OH  
Twin Cities, MN

Atlanta, GA  
Greenville, SC  
Fort Myers, FL  
Orlando, FL  
Charleston, SC  
Valuation, Atlanta

Elwood, NJ  
Manhattan, NY  
Edison, NJ  
Chesapeake Region  
LI/Queens, NY  
Eastern Pennsylvania

Canada, BC

# US INDUSTRIAL MARKET

## Another Solid Performance

The US industrial property market posted another slate of good numbers in Q2. Despite economic indicators that have been sporadic at best, the industrial property market has been consistently strong. Net absorption has been positive in every quarter dating back to 2010. New deliveries have been running very close to total net absorption, which has kept the risk of overbuilding very low and vacancy in steady decline. A substantial percentage of new construction has been in build-to-suit transactions, which has given builders the confidence to get more aggressive in terms of speculative development. Of the 97.4 million square feet currently under construction in the six most active markets, 41% of that space was preleased. That's good news for developers, but also good for occupiers, as that means there is also

### ECONOMIC DRIVERS

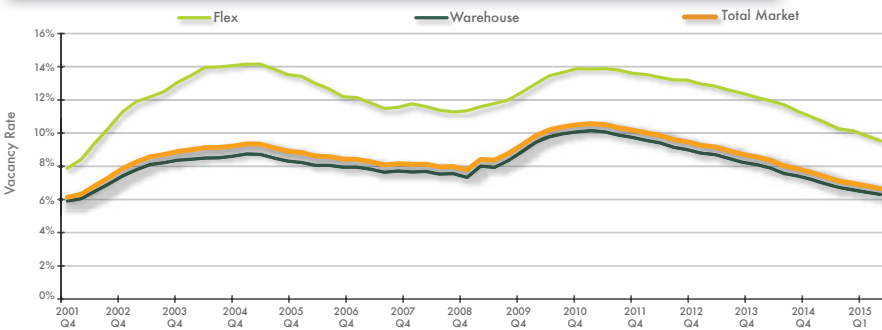
- GROWTH
- EMPLOYMENT
- MONETARY POLICY
- GLOBAL ECONOMY



### A LOOK AHEAD

steadily supply of new spec space that allows expanding companies to be more nimble in executing plans for growth. In the country's hottest markets, large blocks of spec space are being leased during construction or within just a few months of

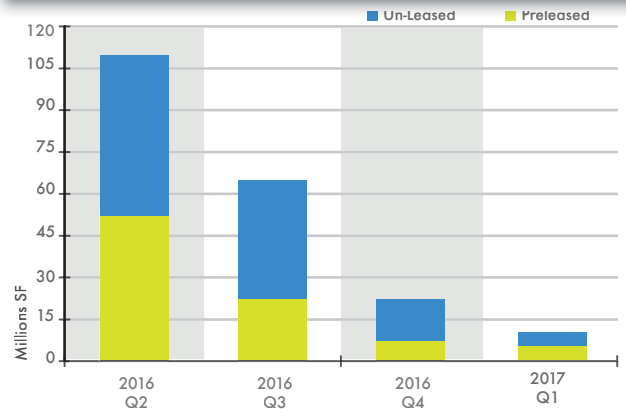
VACANCY RATES BY BUILDING TYPE 2001 - 2015



completion. With net absorption as strong as it has been, the construction pipeline for distribution product should continue to flow at least at current levels for the next several quarters. New deliveries for both speculative and build-to-suit projects for Q2 hit 53.2 million square feet in 381 buildings. That followed a nearly 60.8-million-square foot gain in inventory in Q1. The US industrial property topped 21.73 billion square feet in Q2, and another 224.8 million square feet was still under construction by the end of the period. However, construction is concentrated in just a handful of major markets including Dallas, Houston, Atlanta

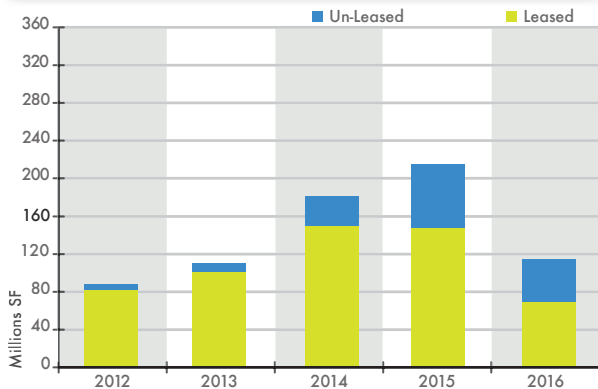
FUTURE DELIVERIES

PRELEASED & UN-LEASED SF IN PROPERTIES SCHEDULED TO DELIVER



RECENT DELIVERIES

LEASED & UN-LEASED SF IN DELIVERIES LAST 5 YEARS



Philadelphia, Chicago and Southern California's Inland Empire. Last quarter we reported that a disproportionate amount of market activity was concentrated in big deals by big tenants in big buildings. That hasn't changed. In fact, the warehouse sector accounted for just under 90% of the 74.4 million square feet of net absorption recorded in Q2. Most of that was in large distribution deals. The top three lease signings for the quarter were all over 1 million square feet each, and over 40% of the net absorption through the first half of the year was posted in just 10 markets.

It's not usual for the bigger distribution hubs to report multiple transactions over 1 million square feet in the same quarter. Large 3PL operators and online retailers like Amazon currently have the biggest appetite for space. Although, electric car manufacturer, Tesla Motors, also signed a lease in Q2 for over 1 million square feet in the Oakland/East Bay market.

The national vacancy rate for warehouse and flex space combined has been falling steadily, and that trend continued in Q2, as the amount of vacant space declined by another 10 basis points to finish the quarter at 5.9%. In the past four quarters, the vacancy rate has fallen by 50 basis points, but several major market areas have reached critically low levels, including Los Angeles and Long Island, New York, both of which are experiencing critically low vacancy and almost no new construction. Finding quality product there is problematic at best, as the aging inventory in those markets is becoming functionally obsolete. Relief is not in sight in those markets, either, as older industrial product is being repurposed for mixed use residential, retail and office projects, which means the base inventory of industrial product is shrinking despite rising demand.

Vacancy declines have average asking lease rates moving higher in the majority of US markets. The national average asking rate has moved up in every quarter dating back to 2011. In Q2, rents moved up another \$.10 to \$5.93 per square foot. Markets with the most construction are seeing more rapid rent growth as tenants

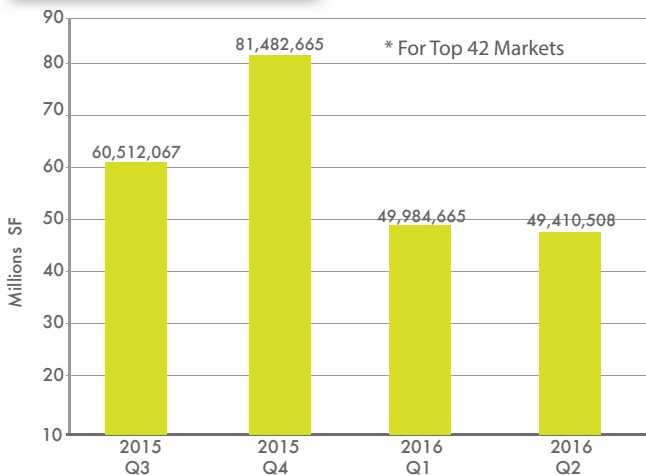
continue to pay a premium for first generation space that offers higher ceiling clearance and state-of-the-art fire suppression capabilities.

The owner/user market remains seriously out of balance. Demand from users to buy their own facilities is running much higher than supply. Competitive bidding and price points that exceed asking prices are commonplace these days. In most markets, prices have risen to levels beyond the previous market peak. Business owners who've had it with paying higher and higher rents are opting to buy so they can control occupancy cost with fixed rate loans in the 4% range, some fully amortized over 25 years at up to 90% loan-to-value. We have our central bankers to thank for the opportunity. The Fed's low interest rate policy has

kept the yield on 10 Year US Treasuries (the index used for setting rates for most commercial property loans) at record lows for the last six years. Without that stimulus, this niche market would not be getting near the attention that it is, and prices would be far below current levels. But, the Fed remains reluctant to move rates higher due to a long list of economic indicators that are still cause for concern. So, users can probably count on low rates to persist for the time being, and that means that prices are likely to keep moving higher, too. Even so, the temptation to lock in occupancy cost for decades is compelling.

Investors, both institutional and private, have lots of money to spend, but too few places to put it. As we point out every quarter, cap rates are compressed and there is no clear indication of a change in that trend. Though, for those who follow markets closely, the chatter is sounding more cautious and experts in all real estate disciplines are more inclined to sound the alarm about a potential market correction. Lenders are tightening up on underwriting for riskier deals and institutions are closely scrutinizing tenant credit. Some experts think this market is getting long in the tooth, but that sentiment doesn't seem to have dampened demand to any significant degree.

NET ABSORPTION



## LOOKING AHEAD

The US industrial market should finish 2016 as it began; high demand, low supply, rising prices and declining vacancy. The lack of global economic growth, along with fiscal, monetary and political turmoil around the globe hasn't put the fire out yet, but we believe the pace of growth will begin to slow as we get into 2017. At some point, interest rates have to move up, and when they do, cap rates may move up, too. A move of just 50 basis points is enough to make a lot of equity disappear.

There just isn't much in the way of good news coming from around the world these days. Trouble in the EU, including negative interest rates, quantitative easing and the uncertainty over the stability of the entire EU has been called into question due to the recent vote in the UK to exit the union. Then there's the news out of China, Brazil, Venezuela, Italy, Spain and all the other countries without a plan to fix the crippling effects of massive debt. The US economy is doing better, but only in comparison. GDP numbers are weak, job creation is slowing down, wages growth is sluggish and our manufacturing sector is struggling to keep from sliding backward. Yet, despite all that, the industrial market still has a full head of steam, and we see things moving in the same direction for at least the next several quarters. The market just has too much momentum, and even if it does slow down, the sheer mass of it will carry us forward for a while.

Interest from foreign investors may increase over the course of the year, as more money looks for a safe place to hide. The US is still the safest of safe havens, and owning assets traded in the US Dollar is looking pretty darn good from across both oceans right now. That will push demand further ahead of supply than it already is, especially in major markets on both coasts.

Vacancy will keep moving lower and more markets will run out of quality space and start looking more like Los Angeles, where vacancy is running at 2% and there is virtually no new construction. Net absorption should remain well into positive territory in most markets, but will decline where supplies are tight. More tenants will be forced to renew in place because of dwindling supplies of quality product. Average asking rental rates will continue to move up, especially in those markets with the first generation space. Construction will stay at current levels in major distribution hubs that still have land at prices affordable for industrial development.





# GDP GROWTH

After a dismal showing in the first quarter of 2016, the first estimate of GDP growth for Q2 came in at just 1.2%, less than half of what was expected. Inventories, thought by most experts to be on the rise, declined substantially. However, a 4.2% increase in consumer spending kept economic growth from being even more of a disappointment. Adding to concerns over chronically sluggish GDP was the downward revision of Q1's growth rate to .8% from 1.1%. Anemic growth in Europe, Japan and most of the world's other economies isn't helping sentiments here at home, either. Despite massive central bank interventions to stave off a deflationary spiral, little progress has been realized.

Persistent concerns over political and economic issues around the world are keeping optimism here at home in check. The year started with a big selloff in US equities. Fortunately, those losses were recovered late in Q1, and the Dow Jones Industrials Average surged back up to 18,000. The problem is there was little to point to for that to be



the case other than fear. But, the "Brexit" vote in late June surprised just about everybody and the Dow took another dive on the news. Four days later, the Dow set a new record high on July 8th.

Volatility in equities has become commonplace and savvy chief executives are going to take that into account as they make decisions for their companies that will show up in GDP numbers down the road. Now, volatility and uncertainty seems to be the rule of the day no matter what the topic may be.

Output of US goods and services are becoming more expensive around the world, and that fact will impact the net investment in business and the trade deficit, both major components of GDP. It now looks like US GDP growth will lag behind 2015's final tally of 2.4%. There just doesn't seem to be enough evidence to expect anything more, as nominal increases in consumer and government spending (the other components in the GDP equation) will not be

# GDP GROWTH

enough to make up the difference. The fact is that our economic growth is anemic despite unprecedented action by our central bankers to give the economy a booster shot.

Consumer spending, which accounts for roughly 70% of GDP, and the numbers don't look good. As we pointed out last quarter, US consumers are keeping a firm grip on their wallets because they're pessimistic about what's to come economically. Retail sales, a large component of consumer spending, has made some modest gains of late, but it did nothing more than make up for declines earlier in the year. Wage growth, or lack thereof, has been a persistent problem throughout this marathon of a recovery, and it is central the issue impacting consumer spending. Income growth is running just above the rate of inflation, which is still under the Fed's target of 2%. So, workers are just don't feel like they are getting ahead, and that makes them more cautious about making the kind of purchases that will move the GDP needle in any significant way. Instead, they continue to pay down existing debt, which doesn't contribute a penny to current GDP.

Net exports, another key component of the GDP equation, have been hurt by the US dollar's strength against other currencies. US goods and services have become more expensive abroad and the impact to US companies who sell products and services that are paid for in other currencies, has been substantial. Exchange rates fluctuate daily, but it's safe to say that the dollar will remain strong as long as the current level of economic uncertainty persists. If other countries voluntarily devalue their currencies to increase the competitiveness of their exports, the US Dollar will soar and things could get worse for American companies that have substantial exposure to foreign markets.



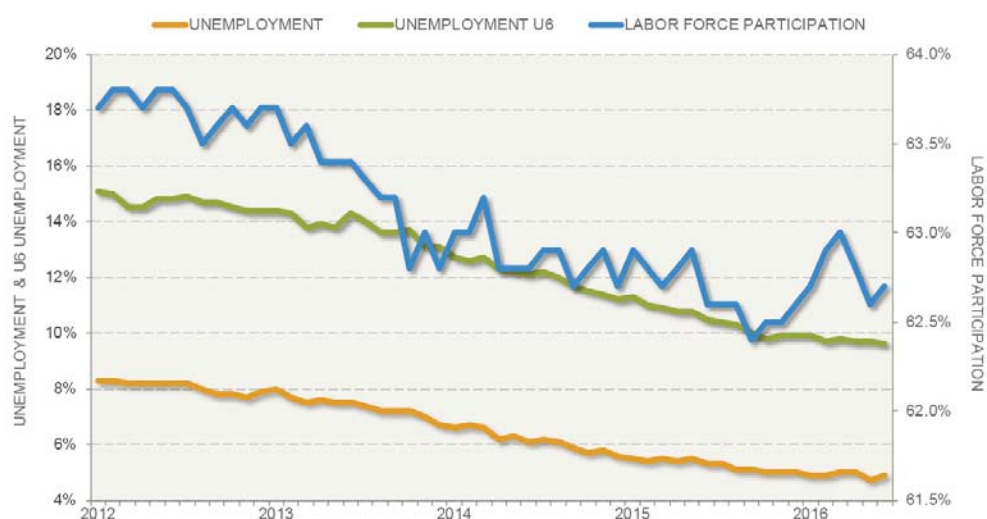
# EMPLOYMENT

Predicting job growth numbers is getting tougher each month. A year ago, the average monthly increase for non-farm employment over the previous 12 months was well over 200,000 new positions. That number has fallen substantially, and the monthly numbers are getting more erratic. Q2 is a good example. April's total was 144,000. The latest estimate for May came in at 11,000 and the first estimate for June was 287,000! How do people make big business decisions with numbers like that? The simple answer is: they get more careful about every decision they make. When they get more careful, they tend to spend less. When they spend less, they hire fewer people or lay more people off. Those people have less to spend. You get the picture.

The interesting thing here is that despite the erratic job growth number, the U3 unemployment rate (the index most widely used) is at a very low rate of 4.8%. Our Econ 101 professors taught us that an economy with 5% unemployment rate is fully employed. If it were only that simple. Tell that to the worker making close to minimum wage who doesn't have the skills for a better job, has a high level of skill for a job that doesn't exist or can only find part time work.

The U6 unemployment rate, which accounts for part-time workers who would prefer to work full time in their field, is at 9.7%. This index tells a different and perhaps more telling story about the realities of the US economy; too many people working at jobs that don't pay the bills. For these folks, discretionary income is a concept not a reality.

### NATIONAL UNEMPLOYMENT



Another way to get a clearer picture of the job numbers is to look at employment by business sector. Unfortunately, doing so makes things look even worse. For example, over 140,000 of the 287,000 created in June were in Leisure and Hospitality, Retail Trade and Healthcare and Social Assistance. These are generally lower-paying jobs that can disappear quickly as things change. By contrast, manufacturers hired 14,000 workers, and gains in construction jobs amounted to zero. Another 15,000 were hired on a temporary basis, and the total hours per worked on a weekly basis was unchanged from a year ago at just over 34 hours. The key manufacturing index compiled by the Institute of Supply Management (ISM) has spent most of the past year in negative territory.

Concerns over slowing domestic growth and the prospect of recessions abroad is prompting employers to hire more part time and temporary workers. The cost of health care pursuant to the Affordable Care Act (ACA) is also contributing to part time employment problem, as employers are inclined to hire workers just under the 30 hour per week threshold that would require them to provide health benefits.



# EMPLOYMENT

The Labor Participation Rate, the metric that measures the percentage of those eligible for employment between the ages of 16 and 64 who are currently working, is also stagnant. Sporadic job growth and the early exit of Baby Boomers, have combined to keep just 62.7% of potential workers in active production.

Wage growth is another problem that has dogged the US economy. While the general unemployment rate fell to 4.8% by the end of June, full-time, high-paying jobs are in short supply and wage growth overall is tracking at a rate of approximately 2.5%. For a worker making close to the minimum wage, that kind of growth is nothing to celebrate. This is one of the reasons why so many middle class workers feel left behind.

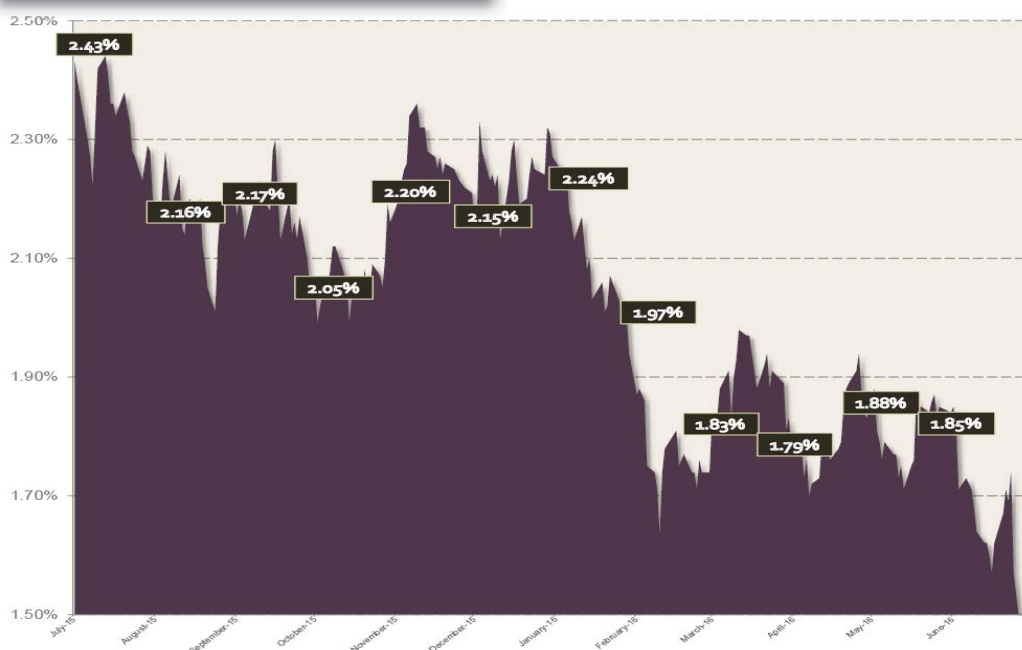
Ironically, many of the best-paying positions that are available go unfilled for lack of qualified candidates. Layoffs in the energy sector has not helped the job picture, either. Thousands of high wage positions are disappearing and it may be years before the energy sector recovers enough to see those jobs return. The jobs being lost are generally full-time, and that only makes things worse. The oil industry continued its belt tightening in Q2 idling more wells, laying off more workers and slashing capital budgets. So, further job losses in that sector can be expected.



# MONETARY POLICY

In December of last year, the US Federal Reserve Bank's open market committee finally pulled the trigger and boosted the Fed Funds rate by 25 basis points to .5%. While it had little immediate effect here at home, the rest of the world reacted, stock markets slid and the dollar strengthened against most of the world's currency. At the same time the European Central Bank was sending interest rates into negative territory and was buying 60 billion Euros worth of bonds each month in its own version of QE. Not exactly a well-coordinated effort, but that wasn't Congress' idea when they created our central bank back in 2013. Needless to say, central bankers around the world expressed their displeasure with the move and have since been warning the Fed that further rate

### TEN YEAR US TREASURY YIELD



rate hikes in the short term will be harmful to the global economy. The Fed's action reduced uncertainty about the policy direction in the beginning, but now Ms. Yellen has backed off the clear talk and returned to more familiar cryptic language when discussing the Fed's future actions. Though, most experts now agree that circumstances are too shaky around the world for the Fed to raise rates anytime soon. That may be the main reason why the Dow Industrials Average hit a record high on July 8th.

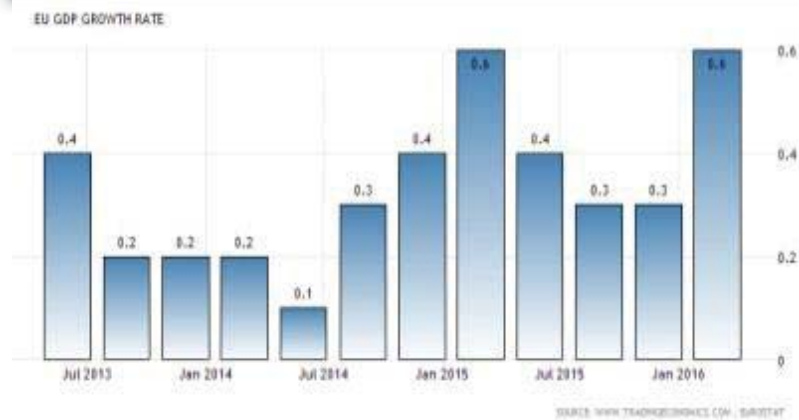
Real estate borrowers have been relieved to discover that the Fed's initial rate hike had little effect on mortgage interest rates, and they should be even happier now, as it appears that the days of cheap capital will be with us a while longer, and mortgage interest rates may even move lower in the coming months. The yield on the 10 Year US Treasury Bill has moved to a record low under 1.5% of late. It's that rate that is used as the index for most mortgage loans made on commercial real estate. It probably also means that the danger of cap rate decompression, a very real concern as it relates to real estate valuations, is abated at least for time being because borrowers will still have access to capital at a rate less than current cap rates. When the Fed finally follows through with more rate hikes, the possibility of higher cap rates will become very real indeed. Even a 50 basis point move up would have a massive impact on property values. Rents, even in the fastest growing markets are not climbing nearly fast enough to bridge that gap.

Keeping a close eye on what central bankers are up to around the world is a good idea. It seems that more drastic measures are being taken every day somewhere around the world, including the newest stimulative tool, negative interest rates. Imagine paying someone interest for the privilege of loaning them money. Sounds crazy, and it might be. But, it is also where over \$10 Trillion has recently been "invested".

# GLOBAL ECONOMY

Last quarter we described the global economic outlook as troublesome. As it turned out, we were wrong. It's worse than troublesome. It's downright scary and increasingly complex. The stakes are high and the outcome of the current global economic conundrum is anything but certain. Whether the topic is the European Union, emerging markets, energy-producing states or the manufacturers of the world's goods, the news is mostly bad. Global growth estimates keep moving down and several countries like Brazil and Venezuela that depend almost entirely on the export of raw materials and oil, are mired in recession with runaway inflation. Then came Brexit, the UK vote to leave the

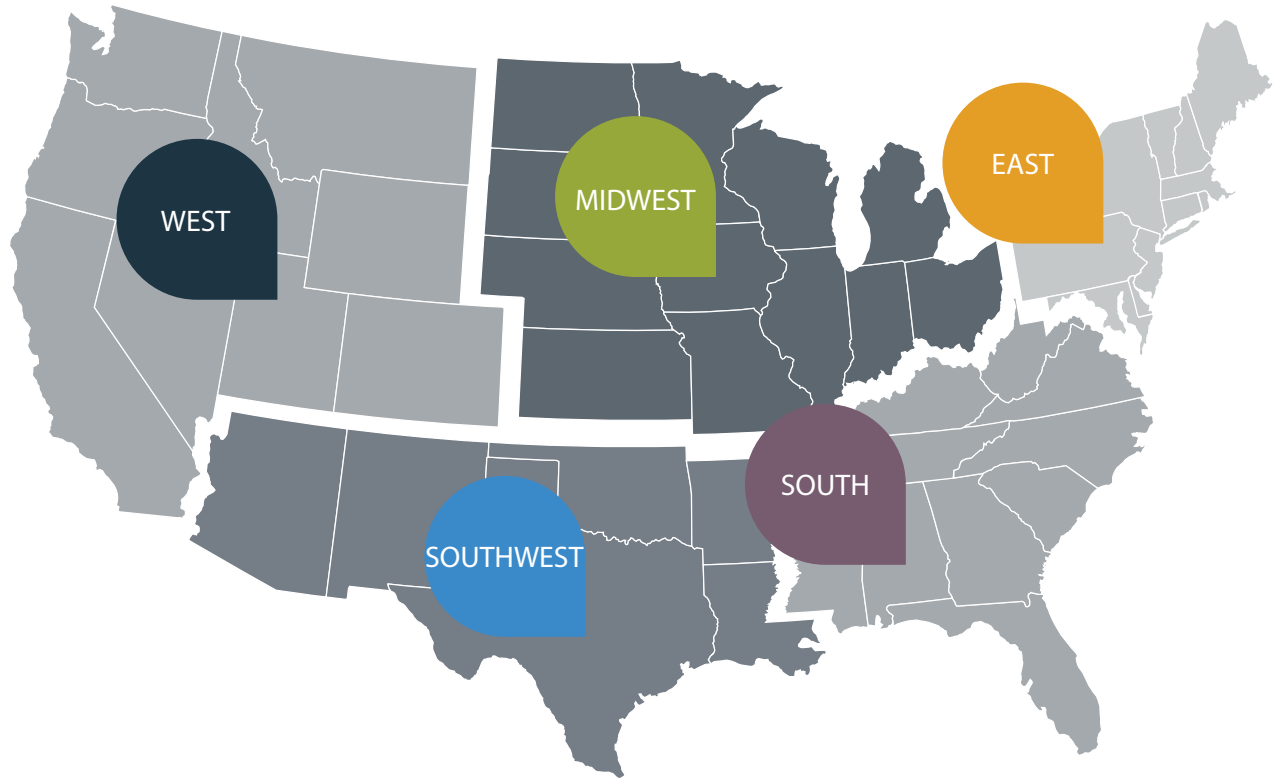
**EURO AREA REAL GDP<sup>2</sup>**  
(QUARTER-ON-QUARTER PERCENTAGE CHANGES)



European Union. Few gave it a chance and the shock wave from the vote was instantaneous. Europe's political union in constant crisis mode these days and there is no governing body with the real authority to enforce anything. EU leaders and European Central Bank have been ineffective in terms of getting things on track. Sovereign debts are mounting, unemployment is persistently high dismal economic growth in Europe makes the US economic look positively dazzling. Concerns over deflation are driving the European Central Bank to send interest rates into negative territory. The bank is also buying up sovereign bonds and has even resorted to buying corporate bonds, an action that would be illegal in the US. Calls for austerity from nations swimming in debt been largely ignored, and the recent refugee crisis is exacerbating economic problems and reigniting nationalist fervor throughout Europe. Many credit concerns over immigration for the surprise passage of the Brexit referendum in the UK. If nothing else, that vote brought the differences between European nations back into the light. The fate of the European Union is uncertain at best, and that bodes well for the US commercial real estate market. For all our failings, the US is still considered the safest place to keep money in troublesome times. The flight to safety phenomenon has already driven US Treasury yields to all time lows.

Oil-rich Middle-Eastern countries, including Saudi Arabia, are issuing sovereign debt and burning through cash reserves to cover revenue shortfalls precipitated by the falling price of oil. Even China is issuing sovereign bonds to help it cope with its massive transition from total dependence on the exportation of manufactured goods to a more consumer-based economy that can be self-supporting. Gone are the days of double-digit economic growth in the world's most populous country.

Despite all these concerns, the US economy is still growing, but sluggishly so, a fact not lost on major corporations that are already facing a slowdown in profit growth. Many of the nation's biggest companies are boosting share prices by buying back their own stock and slashing operating costs, rather than by increasing revenues. Even commercial real estate markets continue to grow at a steady and healthy pace. Rents are rising, vacancy is declining and new buildings are being delivered at a pace that limits the potential of overbuilding. Employment is on the rise, but wage growth is weak. Inflation, once considered evil, is the hoped-for outcome of central bank policy. Yet, even with all the Fed's efforts to boost inflation, it is still running well below the desired level of 2%. Without rising prices, there is little incentive to increase production by hiring new workers. We don't see things changing much to the good as we look ahead. So, we expect 2016 to be another year of so-so economic growth and more of the same for commercial real estate. All things considered, there's no place like home.



LA NORTH  
CENTRAL LA  
LOS ANGELES/LONG BEACH  
INLAND EMPIRE EAST  
ORANGE COUNTY  
SAN DIEGO  
DENVER

PHOENIX  
DALLAS/FT WORTH  
HOUSTON

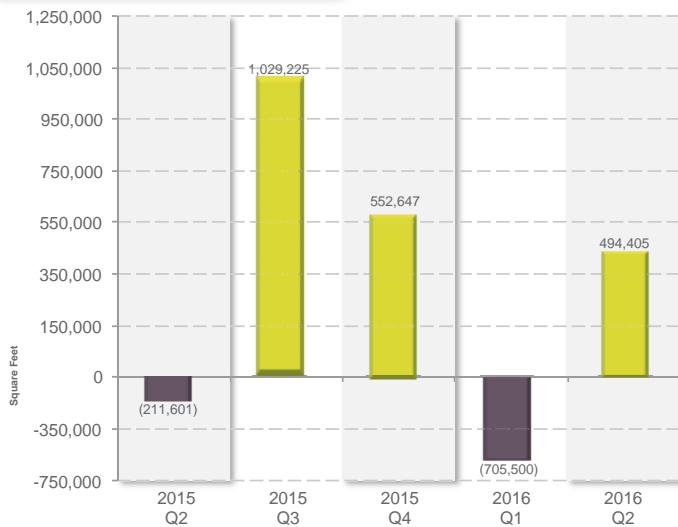
CHICAGO  
ST. LOUIS

ATLANTA  
GREENVILLE / SPARTANBURG

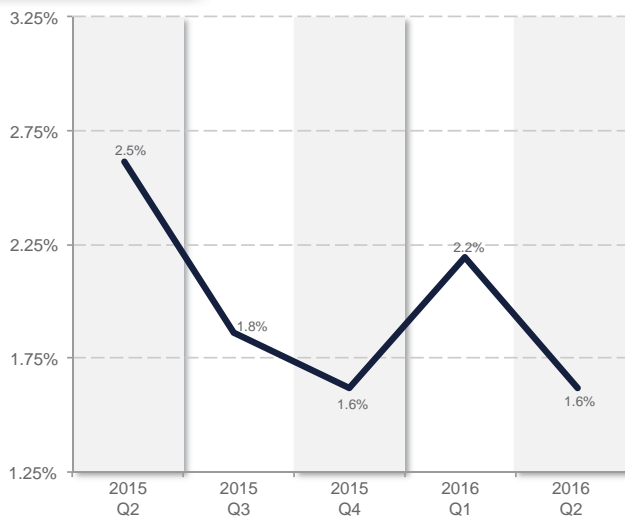
PHILADELPHIA  
LONG ISLAND/QUEENS  
BALTIMORE

# LA NORTH

## NET SF ABSORPTION



## VACANCY RATE



## TRENDING NOW

The ongoing supply shortage in the industrial sector continues to adversely impact activity in the Los Angeles North region, much as it has throughout Southern California. The vacancy rate dipped to a new low in Q2, offering no relief for tenants with requirements in all size ranges. As a result, much of the leasing activity is focused on renewals.

A total of 1.4 million square feet of leasing took place in the quarter with entertainment-related users accounting for a sizable percentage of that activity. Although box office revenue is down in early summer results compared to last year, local filming is up and the upswing in the digital media industry is continuing. But, warehouse and distribution users were still responsible for the largest lease transactions in the region this quarter. UPS inked a 136,000-square-foot lease in North Hills, a north-central submarket in the San Fernando Valley and Costco took 317,165 square feet of space in the northeastern submarket of North Hollywood.

The supply/demand imbalance is continuing to fuel lease rate increases. Although the average lease rate, up another \$0.12 PSF on a quarter-to-quarter basis, came in at \$9.84 per square foot in the quarter, some properties are commanding as much as \$12 per square foot depending on size, location and features. Average asking rates have risen nearly 14 percent on a year-over-year basis.

Despite the continuing rate climb, investors see value-add potential in the industrial sector compared with the office market. Combined with the surging demand, industrial has become a favored asset among both public and private investors. So much so that Liberty Property Trust is reported to be shifting its product mix,

1.6%

VACANCY

\$9.84

AVG. SF RENTAL RATES

494,405

NET SF ABSORPTION

117,250,244

INDUSTRIAL SF INVENTORY

759,258

SF UNDER CONSTRUCTION



## LA NORTH - TRENDING NOW (continued)

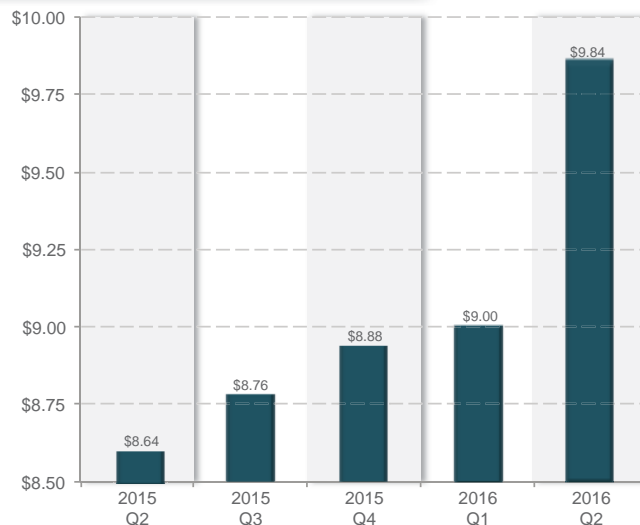
and expects 80% of its revenues to come from the industrial sector by the end of the year, up from a 60% office/40% industrial mix previously, according to real estate digital magazine, *Commercial Property Executive*.

Rexford Industrial Realty Inc., whose acquisition volume in 2016 to date exceeds \$223 million in industrial assets in Southern California, just acquired the remaining 85% interest in a 457,693-square-foot industrial park just outside the LA North region that it previously owned in a joint venture. Commenting on the acquisition, the company said it “exemplifies our ability to opportunistically recycle capital into favorably-priced, value-add and stabilized opportunities within our target infill submarkets.”

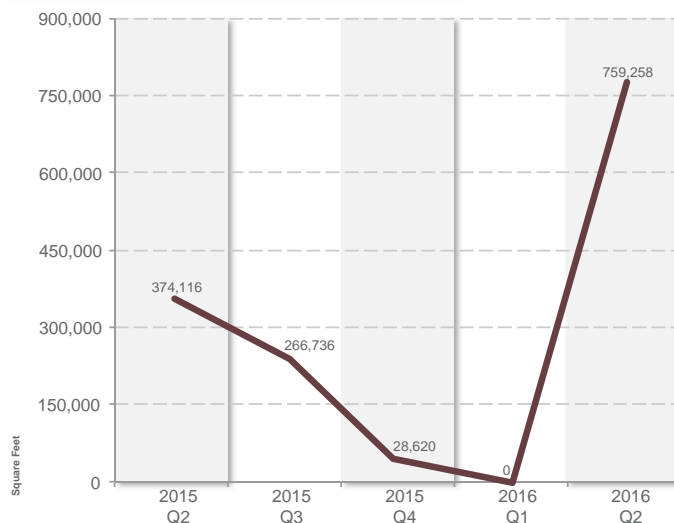
The vacancy rate declined to 1.6% from 2.2% in the prior quarter. Year-over-year, vacancies have fallen 90 basis points. Asking lease rates have risen \$1.20 per square foot on a year-over-year basis, and, with no letup in the space constraints, we expect to see further increases in the second half of the year.

The good news is that there is finally some development underway. Just under 400,000 square feet of industrial space is under construction in the Santa Clarita Valley and another 358,000 square feet of space is being built in the eastern portion of the San Fernando Valley. While the volume of construction is relatively small, it should alleviate some of the competition for Class B and Class C buildings, a bright spot for smaller users.

### AVERAGE SF RENTAL RATES



### SF UNDER CONSTRUCTION



### A LOOK AHEAD

- Average asking lease rates should rise 10% year-over-year
- Interest in owner/user properties will continue to run ahead of supply
- Positive net absorption will moderate due to low supply
- Vacancy will continue to run at historic lows
- Building sale prices will see another year of double-digit gains
- New construction will remain nominal due to low supply and high price of land



## CENTRAL LA

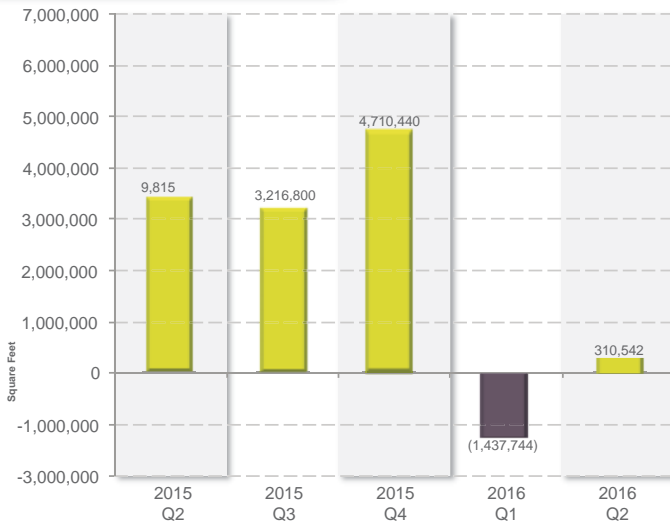
## TRENDING NOW

The Central Los Angeles market, which includes Downtown, along with the Vernon and Commerce areas, continues to tighten. Companies looking to expand in the region are facing tight supply, functionally obsolete product and rents and sales prices at levels above the previous market peak. This region of the sprawling Los Angeles area contains over 285 million square feet of industrial space.

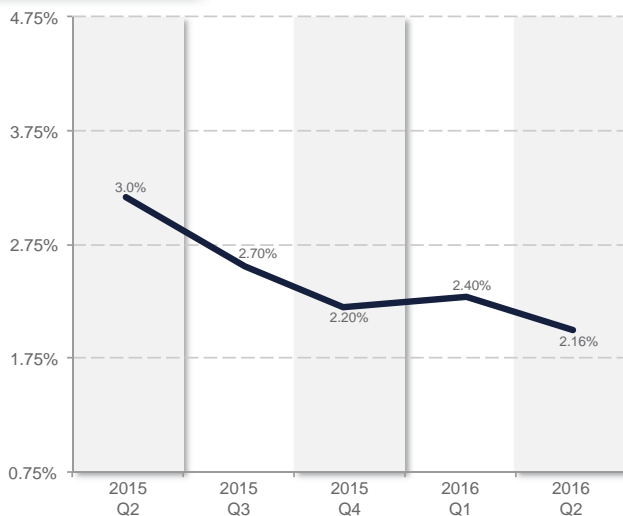
Vacancy, ticked up slightly to 2.16% in Q2 of 2016, adding 17 basis points over Q1's result. But, that wasn't enough for tenants who are frustrated by the lack of good quality space. Even those business owners willing to pay today's higher rents are struggling to find properties suitable for their needs, which has led many to settle for renewing existing leases. Compounding the problem is the fact that the Central Los Angeles industrial base, as in other older urban markets around the country, is undergoing a conversion to residential and creative office users who can and will pay more for space than traditional industrial users. This has the effect of decreasing the industrial base at a time when it needs to expand to handle the internal growth of industrial businesses. Downtown industrial users impacted by this trend are moving southeast to Vernon and Commerce, pushing industrial lease rates and sales prices even higher in those areas, even for space with substantial functional obsolescence. Lack of inventory is also challenging to institutional landlords, who are at risk of losing tenants to other markets and may be saddled with vacancy in the least desirable spaces within their portfolios.

Vacant land for the development of modern facilities is also in very short supply and much of what does become available is at prices that don't justify the

## NET SF ABSORPTION



## VACANCY RATE



2.16%

VACANCY

\$7.92

AVG. SF RENTAL RATES

310,452

NET SF ABSORPTION

285,472,149

INDUSTRIAL SF INVENTORY

410,000

SF UNDER CONSTRUCTION

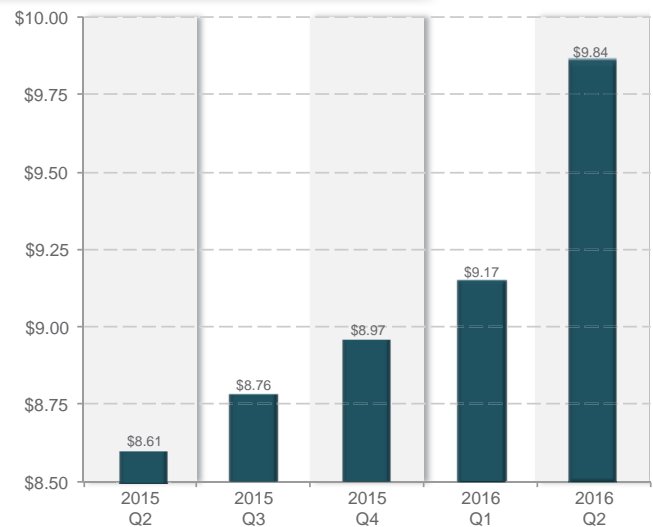
CENTRAL LA - TRENDING NOW  
(continued)

construction of industrial space. Higher uses, including multi-family and mixed use retail-office-residential developments are becoming more common, shrinking the industrial base with each new project. But, there are still developers willing to pay the premium to build industrial, as they see an opportunity to collect even higher rents from tenants who will pay to stay in this strategically located market. So far this year, 290,000 square feet of new industrial space has been delivered, but just 410,000 square feet is under construction to mitigate ongoing demand.

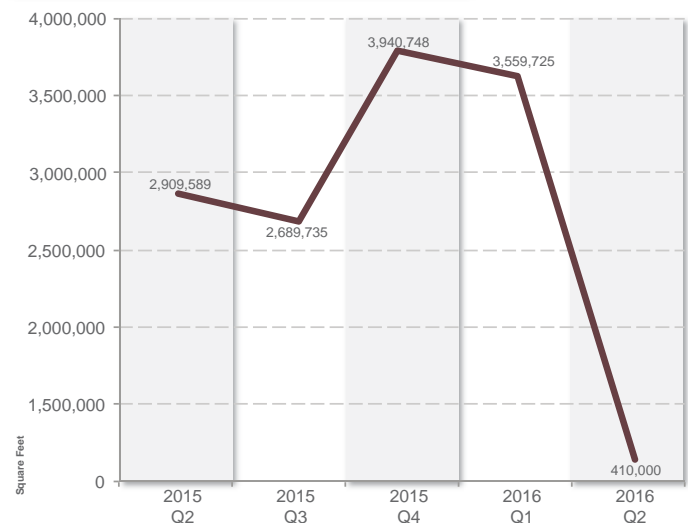
Net absorption has been positive despite the constrictive force of short supply. In Q2, the Central Los Angeles market area posted another modest gaining occupied space of 310,452 square feet, as compared to (316,482) square feet in Q1. In the past year, 1,230,741 square feet of positive net absorption has been recorded.

The average asking rental rate in Central LA moved down by \$.03 in Q2. The Downtown area saw a decline of \$1.08 to finish the quarter at \$8.64. Vernon also saw a decline of \$.72 to end the period at \$7.08, while the Commerce area posted a \$.96 gain to settle at \$8.16. It is important to note that with such short supply and so much functionally obsolete product in the mix, rates will vary significantly quarter to quarter. In all, the average asking lease rate for the region has risen by \$0.36 vs Q2-2015. Sale prices are also up, but with virtually no available product, most users looking to take advantage of the low cost of capital, remain on the sidelines.

## AVERAGE SF RENTAL RATES



## SF UNDER CONSTRUCTION

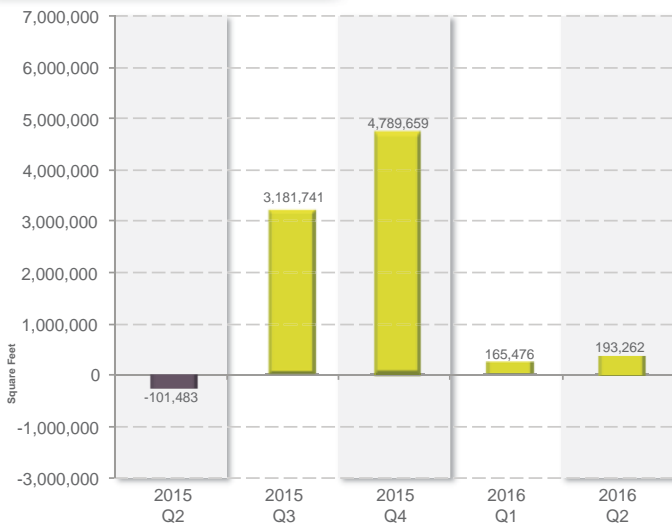


## A LOOK AHEAD

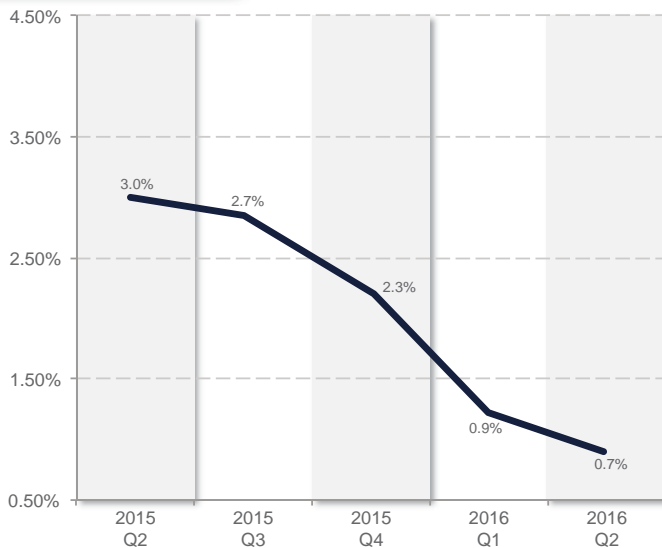
- Leasing activity will continue to be restricted by low supply
- Lease rates overall will move up, but vary by quarter depending on quality of the space leased
- Development of new industrial product will become even more difficult going forward
- Net absorption will remain marginally positive, restricted by sub-2% vacancy
- Conversion to higher uses in the downtown market will push property values up further
- Owner/user demand will be restricted by low supply and tax implications for outright sales

# LOS ANGELES/LONG BEACH

## NET SF ABSORPTION



## VACANCY RATE



## TRENDING NOW

The Los Angeles/Long Beach industrial market remained strong in Q2. Vacancy continued its downward trend to a new low 0.7%. Robust demand and limited supply have put upward pressure on lease rates and sale prices. Landlords and sellers maintain a firm upper hand, forcing tenants and buyers to pay higher prices. This trend is ongoing but may level off as we approach the general election.

Despite high demand, it's important to make note of extreme fluctuations in the price of oil, sluggish global growth, and the new megaships which are bringing down the price of shipping (especially exports). The trickle-down effect is yet to be seen in the local market, as it is well insulated by its diverse industry mix of transportation, warehouse, aerospace, entertainment, automotive, construction and service sectors.

The direct industrial vacancy rate in the Los Angeles/Long Beach area fell another 20 basis points in the 2nd Quarter 2016 to just .7%. Average asking rents increased during the quarter by \$.24 to finish Q2 at \$9.36 per square foot. The average sale price actually decreased slightly in Q2 to \$142 PSF, which is likely due to the closing of functionally obsolete buildings that lack the clear height, energy efficiency and fire suppression technology associated with Class A properties.

Development activity in the Los Angeles/Long Beach region continued to gain momentum with 1,805,559 square feet under construction. Activity remained strong with over 30% of that space being pre-leased. Retailers are leasing warehouse space at a record pace due to the expansion of e-commerce strategies that call for locating closer to heavily populated areas to meet the growing desire for quick deliveries. Recent projects

0.7%

VACANCY

\$9.36

AVG. SF RENTAL RATES

193,262

NET SF ABSORPTION

209,855,936

INDUSTRIAL SF INVENTORY

1,805,559

SF UNDER CONSTRUCTION

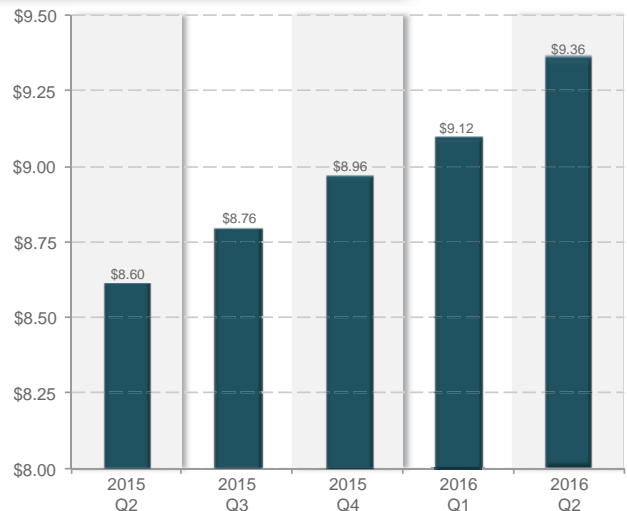
### LOS ANGELES/LONG BEACH - TRENDING NOW (continued)

suggest that development of larger facilities is on the upswing. Traditionally, the region caters to users under 300,000 square feet, as it has been assumed that larger users would opt to locate in the Inland Empire. However, recent activity and construction starts suggest that may be changing, as bigger users opt to remain closer to the Ports of Long Beach and Los Angeles. Recently, a major retailer leased a two-building complex totaling over 450,000 square feet, a record for Class B product.

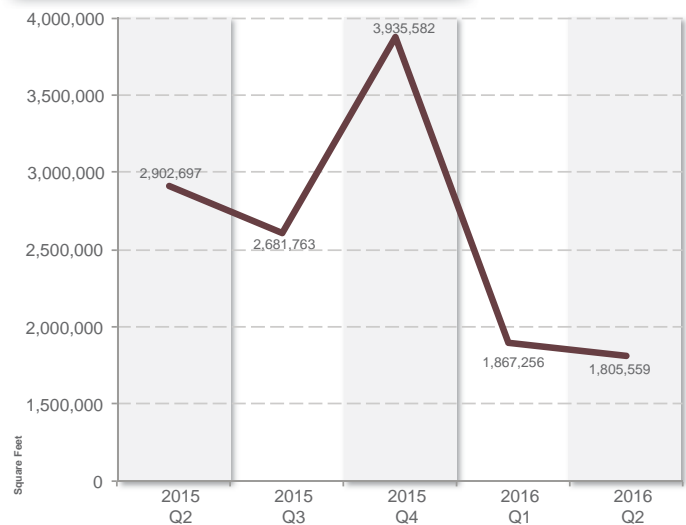
Investors continue to be attracted to fully leased industrial investments and have been willing to pay record high prices to obtain them. Cap rates have been lower in 2016, averaging 5.29%, compared to the first three months of last year when they averaged 5.79%. Another trend worth noting is the negative impact of cheap oil on local businesses that service the oil industry. As these companies have downsized, it has freed up badly needed supply of available space. A correction is also taking place in the shipping, transportation and warehousing sectors, which could bring additional sublease product to the market after the peak season. The health of other industries that service the local market such as furniture, construction and medical have backfilled the space.

Combined TEU port activity is up approximately 3% in 2016, but the second quarter was slow. Long Beach was down by 6.4%, while Los Angeles managed a slight gain of 1%. Both ports experienced gains in imports and exports in May and June. Most Christmas holiday merchandise arrives in the third quarter and these container volumes will greatly influence 2016's overall performance for the Ports, the economy, as well as demand for industrial space.

#### AVERAGE SF RENTAL RATES



#### SF UNDER CONSTRUCTION



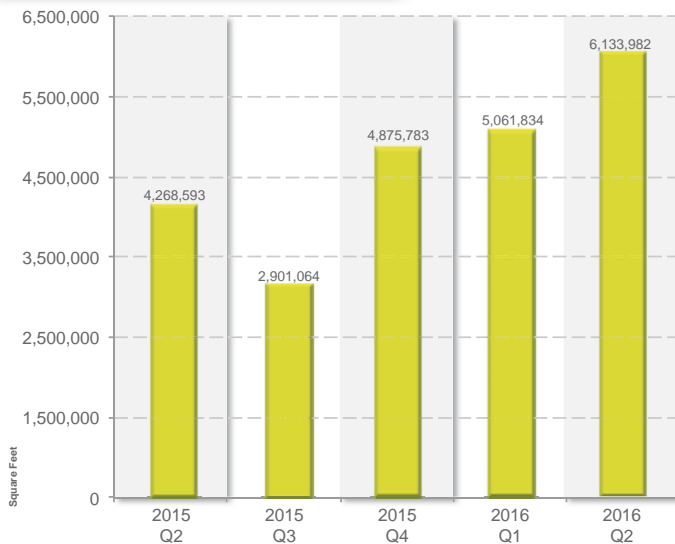
#### A LOOK AHEAD

- Overall demand will remain strong, but limited supply will impact transaction activity
- Renewals in-place will increase due to limited supply of quality options
- Vacancy should remain low, but could increase if the ports lose market share to east coast ports that have expanded to accommodate larger ships
- Sales prices will increase in the high single-digit range for 2016
- Land suitable for industrial development will remain scarce and get even more expensive
- Construction levels will increase slightly over the next several quarters due to planned projects completing the entitlement process

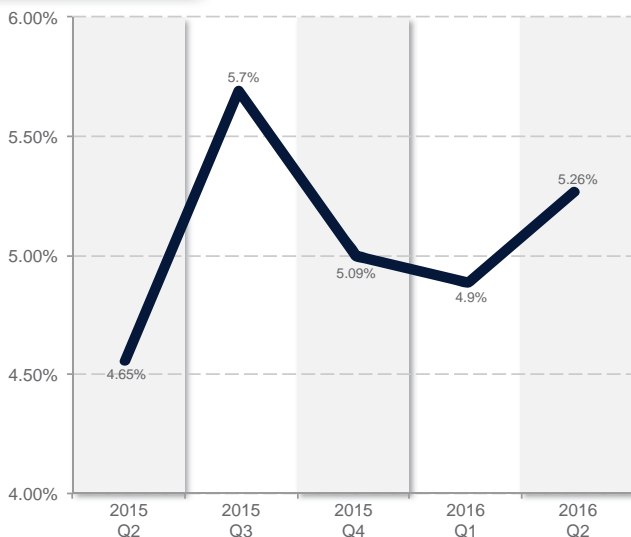


# INLAND EMPIRE-EAST

## GROSS SF ABSORPTION



## VACANCY RATE



## TRENDING NOW

The Inland Empire-East (East Valley) industrial market includes the Cities of Colton, Grand Terrace, Moreno Valley, Perris, Loma Linda, Mentone, Redlands, Yucaipa, Bloomington, Rialto, Riverside, Jurupa Valley (Portions), Highland, San Bernardino, Banning and Beaumont. The area is served by the Interstates 10, 15, 215 and the 60, 71, and 91 freeways, which makes it one of the largest distribution hubs in the US when combined with the Inland Empire-West market.

Industrial lease and sale activity is still running at nation-leading levels. Gross absorption set a new record in 2015, reaching 15.3 million square feet, and besting totals for 2014 and 2013, which hit 11.4 and 14.8 million square feet respectively. That trend continued in Q2 of 2016, as gross activity (including investment sales and renewals) topped 7.7 million square feet, despite the lack of quality available inventory. Gross absorption, which tracks the total of amount of move-ins for a period, was 6.1 million square feet, up 1 million square feet compared to Q1 and almost 2 million square feet above the total for Q2 of 2015. It is important to note that momentum has slowed in the "mega" buildings, but users in the 100,000 to 500,000-square-foot range remain very active.

Tenants have learned to decide quickly when the right space comes along, as the competition for quality product is intense. Lease rates have been moving up consistently for the past several years and concessions like free rent and tenant improvements are disappearing. Time on market is measured in days or weeks for top quality, functional space, and credit is becoming more of a barrier for tenants, as well. Those without strong financials are having even a tougher time, as landlords push for greater safety as well as high rents.

5.26%

VACANCY

\$7.21

AVG. SF RENTAL RATES

6,133,982

GROSS SF ABSORPTION

186,490,361

INDUSTRIAL SF INVENTORY

7,500,415

SF UNDER CONSTRUCTION

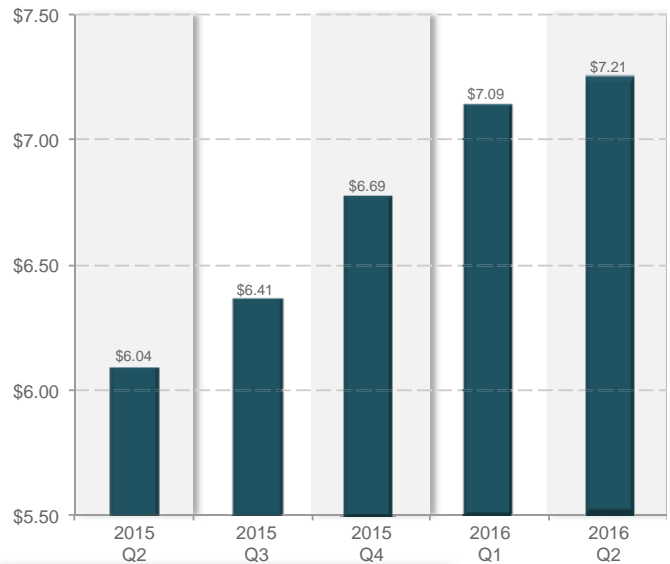
## INLAND EMPIRE (EAST) - TRENDING NOW (continued)

That relegates lesser credit tenants to lower quality product, much of which has elements of functional obsolescence. That's the reality of a market that has an overall vacancy rate of just 5.3%, down from a whopping 19% back in 2010.

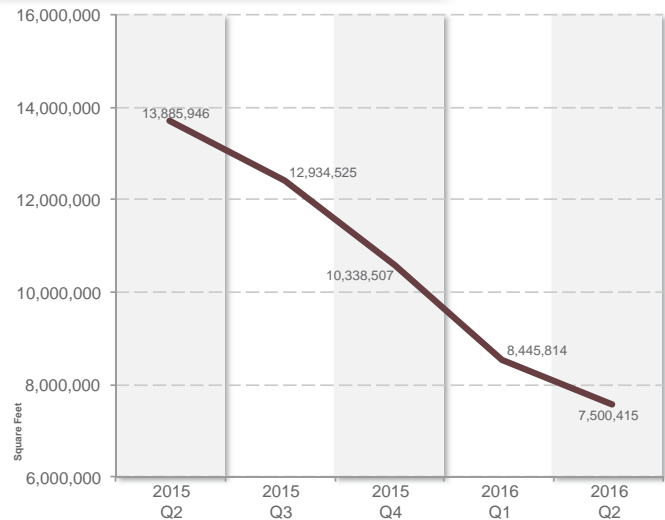
In Q2, average asking lease rates for manufacturing and distribution space combined, posted a slight increase to settle at \$7.21. However, actual GRS rates and asking and actual NNN rates decreased slightly, but this may be due to new space deliveries that are offered for lease without an asking rate in conjunction with the strict confidentiality of actual rates for closed transactions. With that in mind, it can be reasonably assumed that actual GRS and NNN rates are still moving up.

Over 7.5 million square feet of space was still under construction at the end of Q2, with 91% of that total in buildings over 200,000 square feet. However, due to big increases in sales prices and lease rates for smaller buildings, developers are responding by planning projects that cover a wider square footage range. Twelve buildings were delivered in the second quarter, and another 13 buildings are scheduled for completion in Q3. Almost 4,192,990 square feet of new space was delivered in the second quarter, bringing total base inventory up to 186.4 million square feet. Redevelopment of older, obsolete buildings is also back in play, as the availability of prime sites for ground-up development is getting thin.

### AVERAGE GROSS SF RENTAL RATES



### SF UNDER CONSTRUCTION



### A LOOK AHEAD

- Activity for larger spaces will remain strong in East Valley due to speculative development of bulk distribution space
- Low vacancy will limit leasing activity and gross absorption going forward
- Sales prices and lease rates for smaller product will see the biggest increases
- Overall vacancy will remain near 5%, as leasing activity and new deliveries remain in relative balance with current demand
- Look for development to shift more to smaller building sizes throughout the region

# ORANGE COUNTY

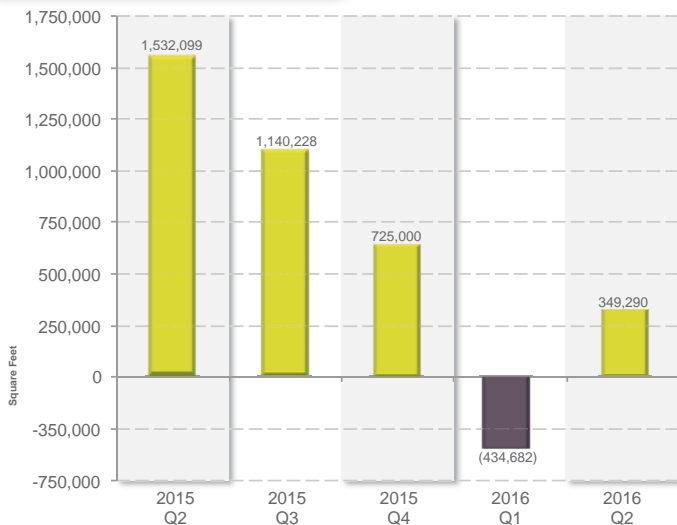
## TRENDING NOW

Orange County's industrial market, which has been on a roll for the last several years, is finally showing signs of slowing down. Lease rates that recently moved past their pre-recession high back in 2007, are continuing to increase but not as rapidly as they had. Leasing activity has slowed, but that can be explained, at least in part, by a shortage of quality space on the market, as the overall vacancy rate remains below 3% countywide. Construction is still at a trickle due to a lack of available land at a price that makes sense to local developers. So, the thin supply of Class A industrial space presents an ongoing problem for expanding businesses, leaving many of them no choice but to renew existing leases while they wait out the shortage.

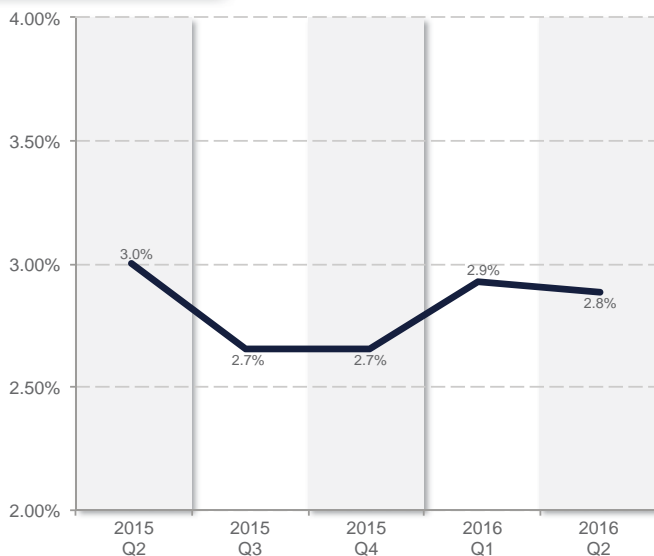
More evidence of a change in market trajectory is surfacing in the sale market. Demand from owner/user buyers have sent sales prices soaring over the past three years, driven by low interest rates and fixed term loans offered through the SBA. But, time-on-market has gone up and price increases have slowed in all size ranges. Asking prices have been reduced in some cases, but some of that may be the result of overly optimistic expectations by owners who have seen a chance to cash in on the recent price run-up.

While it's too soon to call the recent lull in activity a long term trend, it can't be denied that economic uncertainty over the strength of the US and global economies is figuring in to the real estate decision making process. Slow GDP growth around the world, currency fluctuations and the upcoming US presidential election, along with political and social issues impacting the European Union are also contributing factors. Those companies that rely on the exporting of their products and services will be especially mindful of world events

### NET SF ABSORPTION



### VACANCY RATE



2.8%

VACANCY

\$10.08

AVG. SF RENTAL RATES

349,290

NET SF ABSORPTION

278,384,982

INDUSTRIAL SF INVENTORY

41,668

SF UNDER CONSTRUCTION

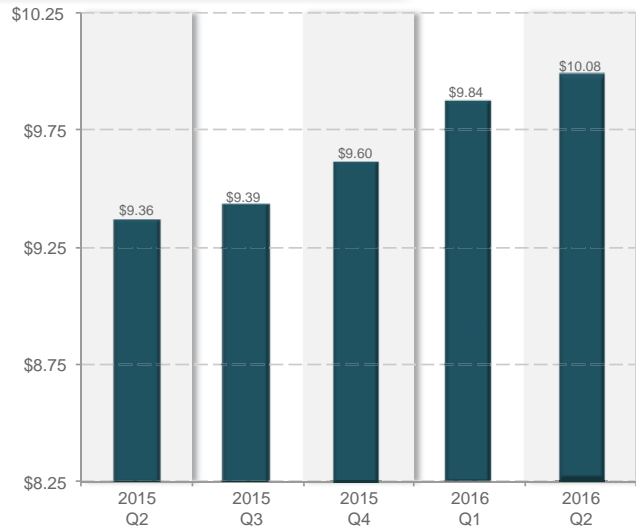
## ORANGE COUNTY - TRENDING NOW (continued)

and its impact on the US Dollar. Conversely, distributors of imported goods will see the dollar's strength as a signal of higher revenues going forward.

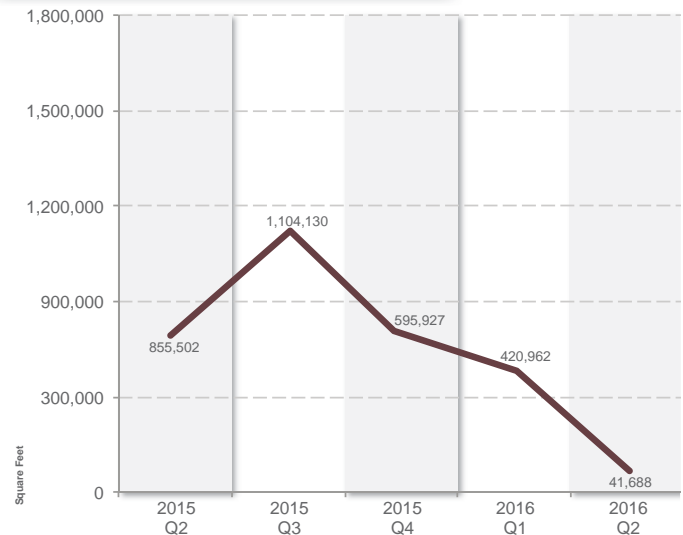
Tenants and buyers still need to give themselves plenty of time to locate facilities that offer greater efficiency. Vacancy, which fell another 10 basis points in Q2, to settle at 2.8%, is still running at record low levels and construction of new inventory is not likely to increase any time soon. In Q2, just 379,294 square feet of new product was delivered and only 41,668 square feet was under construction as the period ended. What is left in terms of buildable sites is cost prohibitive, resulting in the repurposing of industrially-zoned land for high-density residential and mixed-use, office and retail projects. New industrial projects will only be offering larger buildings that are cheaper to build. The last of buildings under 20,000 square feet may already be in the existing inventory of Orange County's 278.4 million square feet.

The county's top-performing submarket was North County, which saw vacancy fall to 2.2% with net absorption of 302,000 square feet. The year-over-year jump in asking rental rate was up by nearly 15%. Over 175 transactions were completed in this submarket with a total base inventory of almost 117 million square feet.

### AVERAGE SF RENTAL RATES



### SF UNDER CONSTRUCTION

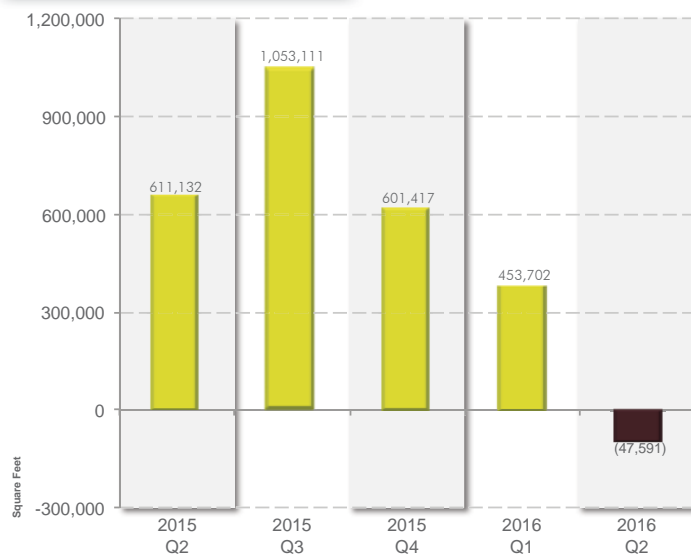


### A LOOK AHEAD

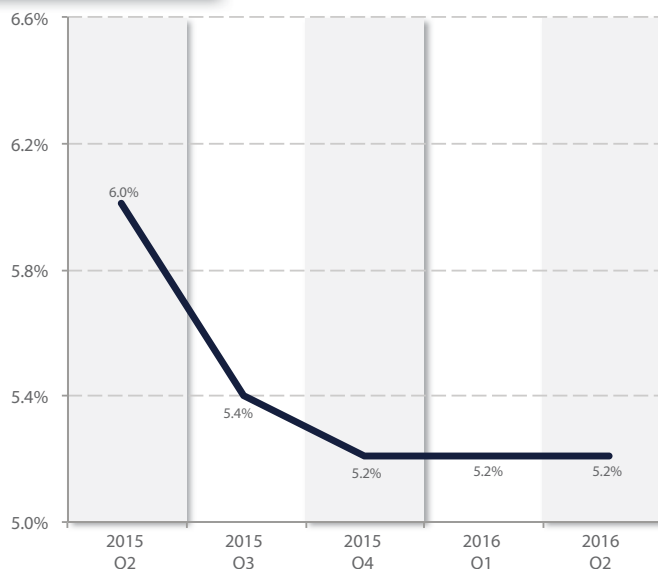
- Competition for high quality product for sale and lease product will still keep upward pressure on rents and sale prices
- Transaction volume and net absorption will continue to be constricted by low supply
- Landlords of Class A product will keep tightening concessions further and demand stronger credit
- Construction will remain restricted to larger buildings
- Vacancy will stay under 3% for the remainder of 2016
- Orange County's economy will continue to outperform the US economy

# SAN DIEGO

## NET SF ABSORPTION



## VACANCY RATE



## TRENDING NOW

San Diego has several active business sectors driving industrial activity. In particular, the Defense Industry, which employs over 100,000 active duty and 30,000 civilian workers, combined, accounts for more than \$20 billion in annual economic activity. The Life Sciences industry attracts significant venture capital, employs over 42,000 physicians and scientists and is the center for human genome research. The Aerospace sector, led by General Atomics, is expanding due mainly to the development and manufacture of drones. Cross-border commerce is also on the upswing, in part due to the strategic location between Mexico and neighboring Riverside, Orange and Los Angeles Counties in the north. As a result, the unemployment rate in San Diego has fallen to 4.2% by the end of the current quarter, down 50 basis points since March of this year.

Net absorption for Q1 totaled 441,533 square feet, but the run of positive gains in occupied space dating back to 2010, came to an end in Q2, as the region recorded negative absorption of 47,951 square feet. The flex sector stayed in the black in Q2, registering a gain in occupied space of 502,626 square feet. Carlsbad, in the North San Diego area, has been a bright spot for the flex sector, posting almost 297,000 square feet of net absorption so far this year, more than half the county's total. Activity there is concentrated in spaces under 50,000 square feet. This reflects the strong growth of businesses in the biomedical and aerospace sectors that need more highly improved space.

Overall vacancy throughout San Diego has been in steady decline in the last several years, but finished Q2 nearly unchanged at 5.2%. Flex vacancy is falling faster than the overall rate, losing 110 basis points in the past

5.2%

VACANCY

\$11.99

AVG. SF RENTAL RATES

(47,591)

NET SF ABSORPTION

189,368,399

INDUSTRIAL SF INVENTORY

1,513,760

SF UNDER CONSTRUCTION





## Key Market Snapshots

### SAN DIEGO - TRENDING NOW

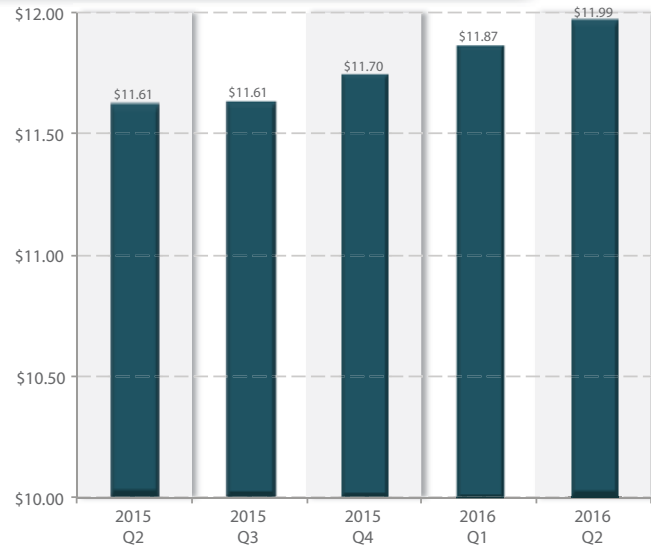
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year to end Q2 at 8.3%. The warehouse rate fell 10 points in Q2 to 4.2%, but is unchanged in the past four quarters. North County's warehouse vacancy factor stands at just 3.7%, but Central San Diego is even lower at 2.7%. Finding quality space anywhere in San Diego has become a big problem for expanding tenants, as a disproportionate share of the available inventory has elements of functional obsolescence. North County, which was harder hit by the last recession, now has vacancy numbers on par with neighboring submarkets to the south.

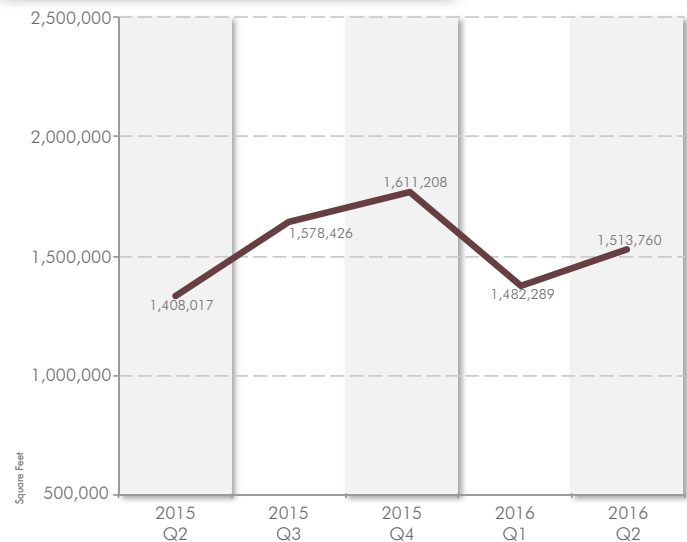
Average asking rents keep moving up across all submarkets as a result of scarce supply. In the past year, San Diego County average asking lease rates rose by approximately \$.38 to \$11.99, but warehouse rents have jumped by \$.66 in the same period. In Q2, the overall rate jumped another \$.08, but the warehouse sector jumped \$.21 in the same period. Flex rents actually declined in Q2 after a string of strong increases dating back to 2011. For the period the average rate for flex space stood at \$17.21. Carlsbad has the largest inventory of flex space in the county, and the average asking rent there hit \$14.93 by the end of the quarter. Flex rents are highest in the Torrey Pines area at \$48.52 due to that submarket's high concentration of specialized laboratory space for the San Diego's growing biomedical sector.

Owner/user demand is strong throughout the region, and would-be buyers are frustrated from the low supply and high demand of properties offered for sale. Interest rates remain at historic lows because of the Fed's continuing reluctance to raise interest rates. So, long term financing is still available at 90% of building value in the low 4% range. Even with prices as high as they are, it still makes sense for a business owner to buy and lease the building back to his own company. Demand is still strongest for buildings under 15,000 square feet.

#### AVERAGE SF RENTAL RATES



#### SF UNDER CONSTRUCTION

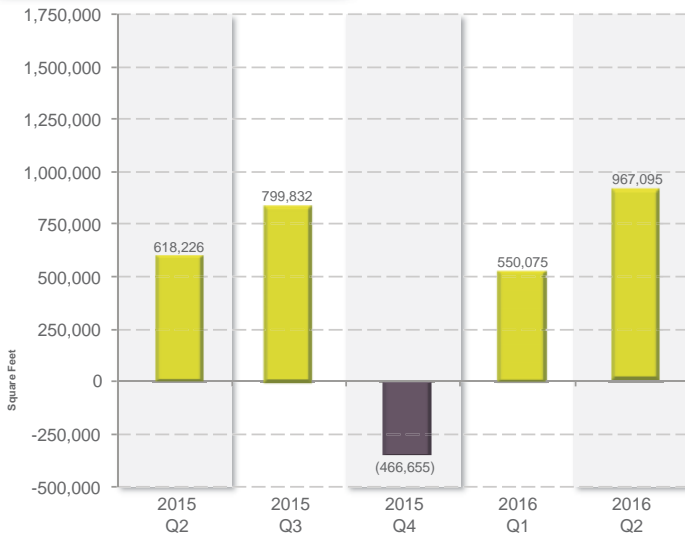


#### A LOOK AHEAD

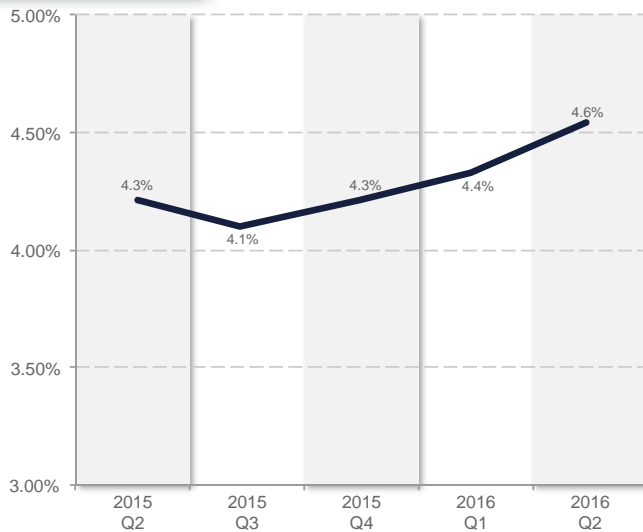
- Lease rates should move up another 5% to 10% in the next year due to continuing tight supply
- The Life Science industry will continue to boost absorption of flex space
- Sales prices for user buildings will keep moving up, especially for smaller buildings
- Developers remain bullish on the prospects for continued strong rent growth countywide
- Construction activity should increase soon as several planned projects cycle through the entitlement process
- Vacancy will keep moving down in 10-20 basis point increments for the next several quarters

## DENVER

## NET SF ABSORPTION



## VACANCY RATE



## TRENDING NOW

The Denver industrial property market is still going strong, despite the recent slowdown in the energy sector. Layoffs in energy markets have been on the rise. Also, the number of active wells in US has decreased by more than half since the crisis began, and capital budgets for exploration have been slashed. Most of the job losses have been concentrated in the office sector thus far, but no energy-dependent market is safe from further challenges. While the price of oil has rebounded to nearly \$50 per barrel, that rise has done little to re-ignite the industry. While some less well-capitalized energy companies are folding, larger players are in merger talks to gain economies of scale. Unless and until world demand for oil returns to healthier levels, further troubles for energy sector users should be expected. To some degree, Denver's entire economy, including its industrial market, will be affected.

Vacancy ended Q2 at 4.6%, up from 4.3% a year ago. Activity is still mainly in the bulk distribution sector, but the marijuana industry, which has been extremely active since 2003, still has owners with functionally obsolete product very happy, as marijuana users are less in need of building characteristics that other industrial users need to operate efficiently. For big distribution users, it's a different story. Short supply continues to be a problem for tenants looking for the highest quality space with high ceiling clearance and modern fire suppression capabilities that maximize space utilization.

Net absorption topped 967,095 square feet in Q2, bringing the total change in occupied space for the year to 1.5 million square feet. New deliveries for the quarter totaled 2,019,000 square feet, adding to Q1's total of 636,475 square feet.

4.6%

VACANCY

\$8.26

AVG. SF RENTAL RATES

967,095

NET SF ABSORPTION

292,522,107

INDUSTRIAL SF INVENTORY

4,268,976

SF UNDER CONSTRUCTION

## Key Market Snapshots

DENVER - TRENDING NOW  
(continued)

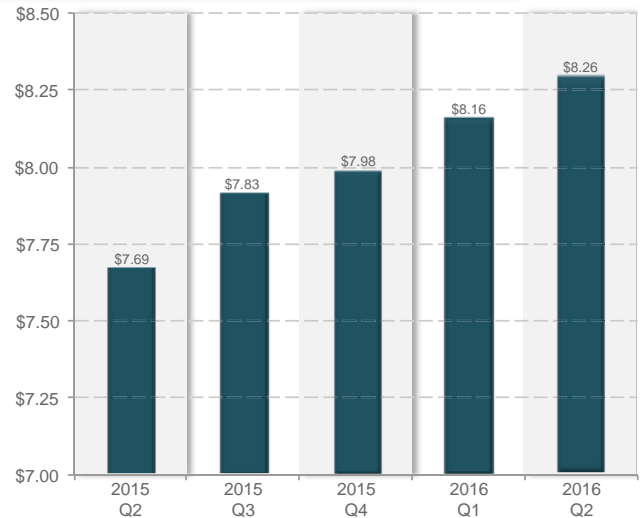
Another 4,268,976 square feet of space was under construction at the end of the quarter, mostly larger buildings that will accommodate users over 75,000 square feet.

Rents are still on the rise. By the end of Q2, average asking rates for all industrial product stood at \$8.26, up \$.10 for the quarter and \$.57 over the past year. The warehouse sector ended the period with an average rate of \$7.68, \$5.84 in the largest industrial bulk submarket, while flex the rates came in at \$10.14.

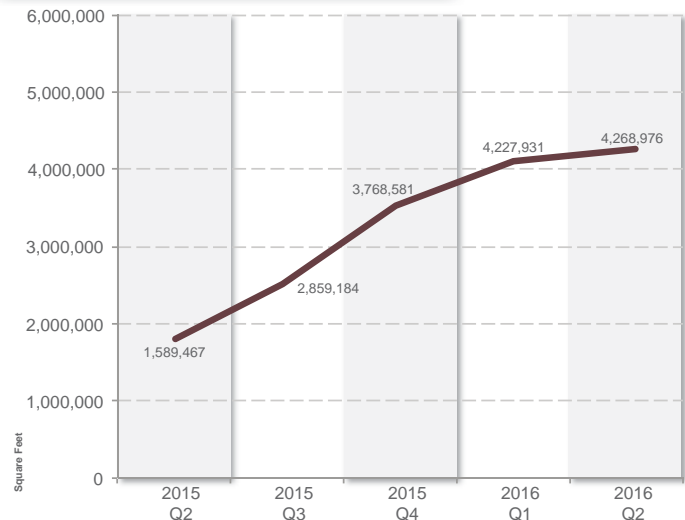
The story as far as investors are concerned is much the same as it is throughout the US. Optimism is still running high for the long-term potential of the Denver industrial market in terms of rent growth and net absorption. The area is very attractive to an ever-younger workforce that likes the variety of recreational activities and the developing urban cores like LoDo, RiNo and The Highlands, which all offer the live-work-play lifestyle that has become so popular across the country. No wonder Denver is one of the country's fastest growing cities.

The supply of owner/user buildings offered for sale has run thin and prices are at all-time highs. The "marijuana effect" has contributed disproportionately to the price spike, giving traditional owner/users reason to question the concept of building ownership. However, mortgage rates offered through the SBA have declined of late, mainly because of the decline in the yield of the 10-Year T-Bill, the index used to set rates for most industrial property loans. Fixed rate loans in the low 4% range are available in loan amounts of up to 90% of appraised value.

## AVERAGE SF RENTAL RATES



## SF UNDER CONSTRUCTION



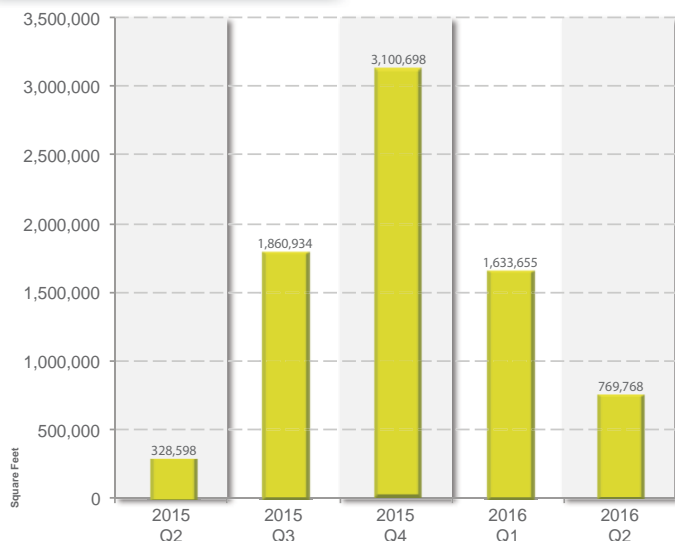
## A LOOK AHEAD

- Vacancy will remain tight, holding near 5% for the next several quarters
- Construction will remain near current levels, as developers will be cautious not to overbuild
- Gross sale and lease activity will moderate for the rest of the year due to lack of supply
- Look for a further push of industrial out of the central core
- Average asking lease rates will hold stabilize near current levels
- Owner/user prices may top out this year

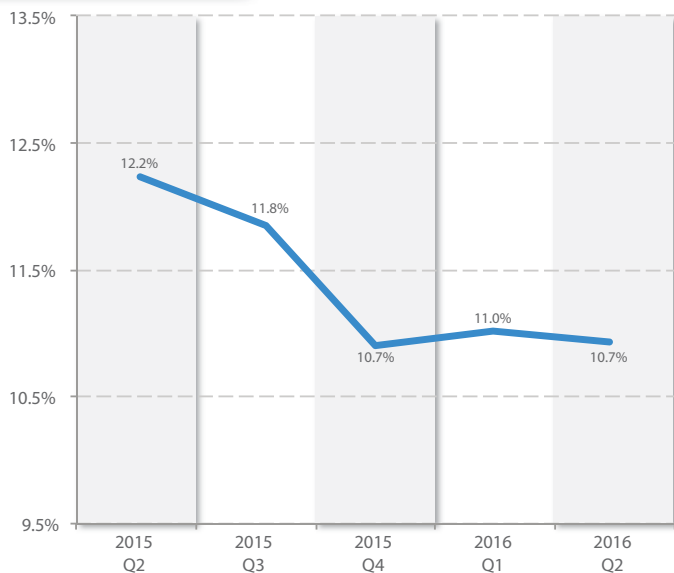
# PHOENIX

## TRENDING NOW

### NET SF ABSORPTION



### VACANCY RATE



In the first half of 2016, the Phoenix industrial market moved in a positive, but less than robust direction than it did in the second-half of 2015. Economic uncertainty fueled by several uneven jobs reports persists, and the Fed's indecision on raising interest rates along with a contentious political climate, has served to stifle market enthusiasm. Additional inventory delivered this quarter added to vacancy pressure.

However, a tight California industrial market is still fueling the Phoenix industrial sector and keeps the market in relative good health. The Phoenix area housing market has picked up the pace, consumer confidence has been on the rise along with purchasing power, which have helped to mitigate some of the negative pressures on the industrial sector.

This quarter saw a rise in the number of larger distribution lease transactions. Favorable rates for larger spaces that have s after last quarter's flat level. Good deals are still available with modest concessions. Other notable transaction for the quarter include First Solar Space's 176,340-square-foot deal at 2950 S. Litchfield Road in Goodyear, and the 148,797-square-foot lease to Dexcom at 232 N. Dobson Road in Mesa.

The Phoenix vacancy rate was unchanged in Q2, finishing the period at 10.7%, mostly because of new deliveries of over 1 million square feet and modest absorption of only 769,768 square feet. The highest vacancy rate, 12.9%, was recorded in the Southwest Valley submarket, which includes Goodyear, Tolleson and surrounding areas, while the lowest vacancy rate, 6.7%, was posted in the Northwest Valley, which includes Deer Valley/Pinnacle Peak and Glendale. By product type, distribution/warehouse space still has the lowest vacancy at 9.7%, while manufacturing and flex space run higher at 12.1% and 14.3%, respectively.

10.7%

VACANCY

\$6.72

AVG. SF RENTAL RATES

769,768

NET SF ABSORPTION

295,214,735

INDUSTRIAL SF INVENTORY

2,949,799

SF UNDER CONSTRUCTION



## PHOENIX - TRENDING NOW (continued)

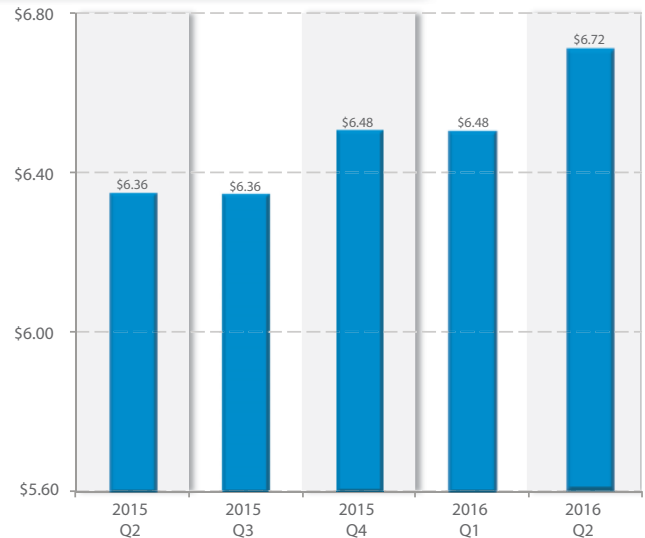
Manufacturing space in the Northeast Valley posted the lowest vacancy rate, a scant 2%, on an inventory base of 3,003,000 square feet.

Absorption for the first half of 2016 was just shy of 2.3 million square feet. Rental rates rose by 1.8% in Q2 to \$0.56 per-square-foot per month, up from last quarter's \$0.54.

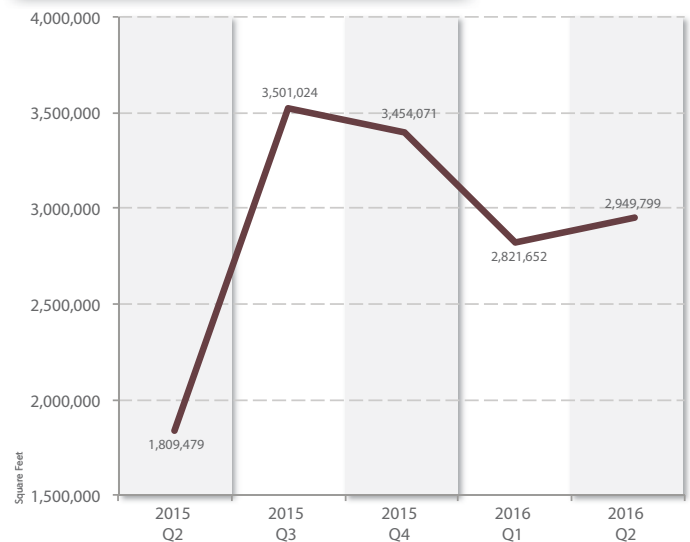
Industrial construction, a mixture of spec and built-to-suit projects, rose to 2.9 million square feet in Q2, while deliveries to inventory fell to just over 1 million square feet from last quarter's 1.9 million square feet.

In the largest industrial lease transaction of the quarter, Nestle Water took 394,775 square feet of distribution space at 43rd Ave. Logistics Center, 1635 S. 43rd Ave., Phoenix. In the largest sales transaction in Q2, Exeter Property Group purchased a three-building distribution portfolio totaling 923,908 square feet from Duke Realty for \$55.9 million, or \$60.50 per square foot. The largest of those buildings is 603,909 square feet, located at 4570 W. Lower Buckeye Road in Phoenix.

### AVERAGE SF RENTAL RATES



### SF UNDER CONSTRUCTION



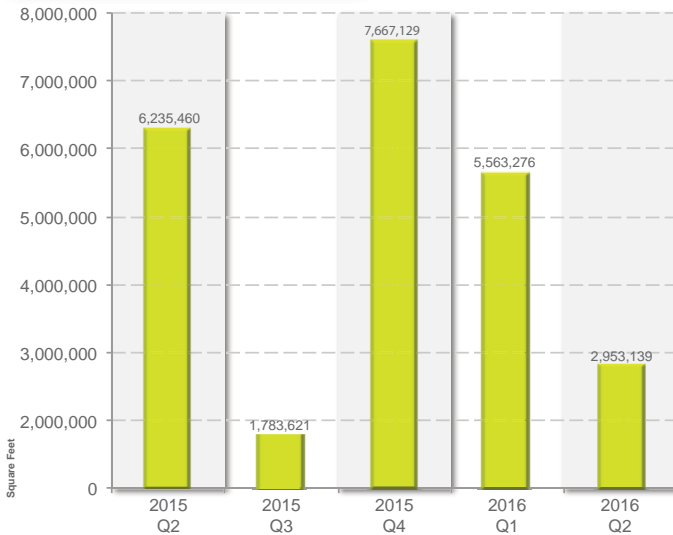
### A LOOK AHEAD

- Gross activity will remain at current levels, but shift to transactions involving smaller spaces
- Net absorption could be modest in 2016, challenged by a steady stream of new deliveries
- Lease rates will be generally flat for the balance of the year
- Vacancy could drop to single digits by end of 2016
- Construction activity will remain at current levels, with emphasis on multi-tenant business park projects
- Investor interest in Phoenix will remain strong as it offers more buying opportunities than in tighter markets like Southern California

# DALLAS/FT WORTH

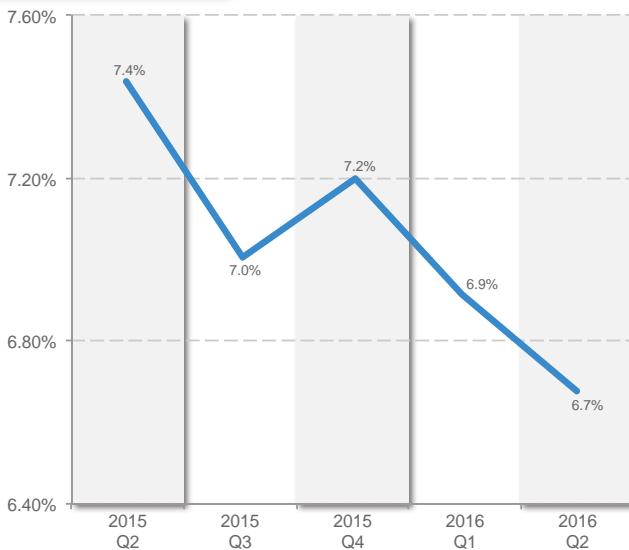
## TRENDING NOW

### NET SF ABSORPTION



The Dallas/Fort Worth (DFW) industrial market is still one of the nation's industrial hot spots. While the region is not immune to the downturn in the energy sector, the industrial market is still being fueled by a combination of Fortune 500 retailers, a rapidly expanding e-commerce sector and a robust housing market that mirrors a big increase in population. New deliveries of industrial space for the year topped 9.5 million square feet by the end of Q2, ranking the market second to Atlanta nationwide. Another 22 million square feet of space remained under construction as the period ended. Despite such high construction activity, the area is still not overbuilt, though there are rumblings that supply might move ahead of demand going forward. For the time being, preleasing in the DFW area remains strong and speculative space is also leasing up quickly, which is helping builders beat underwriting assumptions.

### VACANCY RATE



DFW continues to attract distribution users over manufacturers because of its infrastructure and hub location. As a result, almost all new construction is bulk distribution product with high clearance and state-of-the-art fire suppression technology. Big users making recent moves in the region include Kimberly-Clark's 874,214-square-foot lease at 4808 Mountain Creek Parkway and Shippers Warehouse lease of 874,214 square feet Prime Pointe I. Even flex product is experiencing good leasing activity, especially from office users looking for relief from rising rents in the office sector. Microbreweries, technology-based businesses and even retail/showroom are also impacting overall industrial market activity.

The industrial vacancy rate ticked up 30 basis points in Q2 to finish the quarter at 6.7%. However, vacancy is down by 40 basis points in the past four quarters. The timing of new deliveries has caused some gyrations in

6.7%

VACANCY

\$5.36

AVG. SF RENTAL RATES

2,953,139

NET SF ABSORPTION

833,317,470

INDUSTRIAL SF INVENTORY

21,959,987

SF UNDER CONSTRUCTION



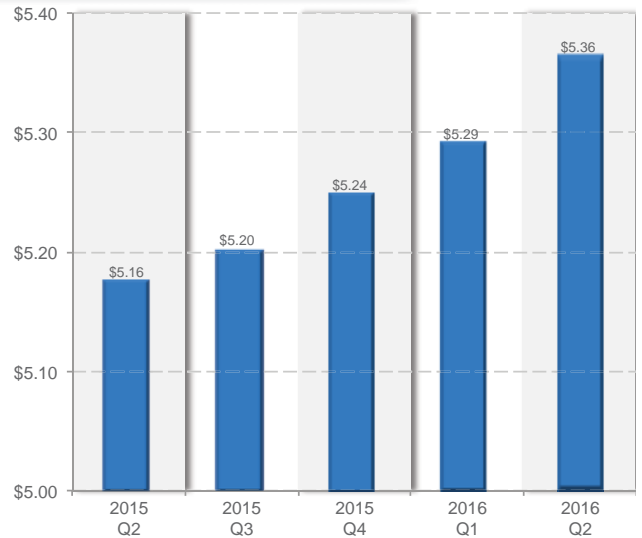
### DALLAS/FT WORTH - TRENDING NOW (continued)

the vacancy factor, but the overall rate is heading down, which landlords are using to their advantage in their negotiations for new leases as well as renewals. The current balance of leasing activity and development should keep vacancy from falling too low to interfere with growth plans of expanding distributors, which is not the case in more mature markets like Los Angeles that have vacancy rates under 2% and virtually no construction.

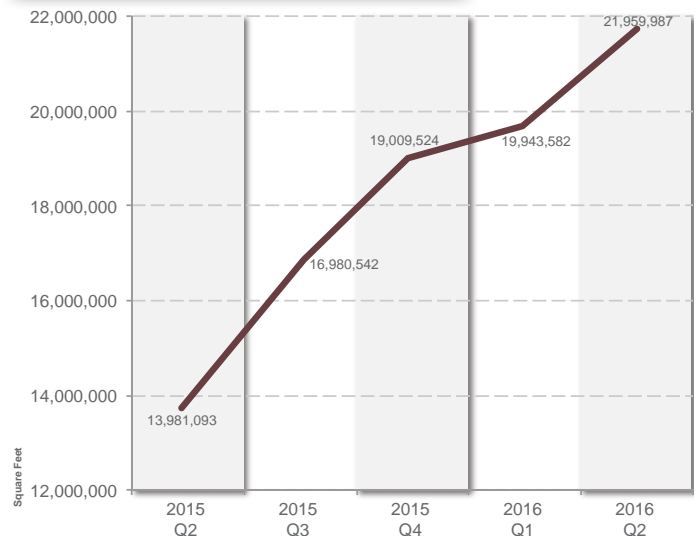
Net absorption for Q2 came in at 2,953,000 square feet, bringing 2016's net gain in occupied space to over 9.4 million square feet. Big box users continue to pay more for quality and that has kept average asking rental rates trending up. In Q2, the overall rate moved up another \$.08 to \$5.36. The inner loop submarkets are still experiencing more rent growth than outlying areas, allowing tenants willing to move 5-10 miles to lower occupancy costs. Some tenants renewing leases originated in 2010 and 2011 are seeing their rates double when they renew in place.

Since bulk distribution product is still the preferred industrial asset class for institutional investors, supply is running short and cap rates have moved to record lows, as they have in other major markets across the country. Investors of all types are having serious trouble finding a place to deploy their capital, including foreign-sourced money coming to the US as a safe haven. That keeps seller expectations moving higher and buyers under pressure to keep bidding prices up despite concerns for higher interest rates going forward. Though, the Fed has, for the time being, taken no action on interest rates after raising its benchmark rate 25 basis points back in December of 2015.

#### AVERAGE SF RENTAL RATES



#### SF UNDER CONSTRUCTION



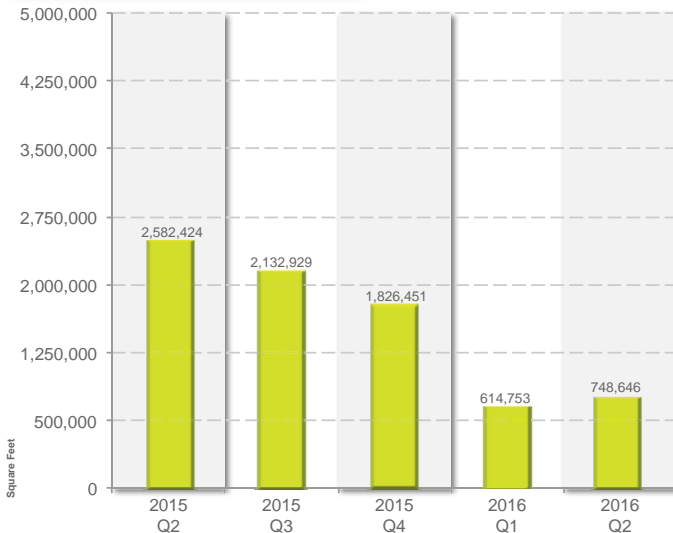
#### A LOOK AHEAD

- Leasing activity should remain steady through the end of 2016
- Net absorption in 2016 should keep pace with 2015 totals
- Vacancy will remain near current levels, keeping balance with new deliveries
- Lease rates will continue to rise for existing and new inventory in 2016
- Construction will remain strong, but will keep in sync with current demand
- 36 foot clear heights will become more of a priority for tenants above 100,000 square feet

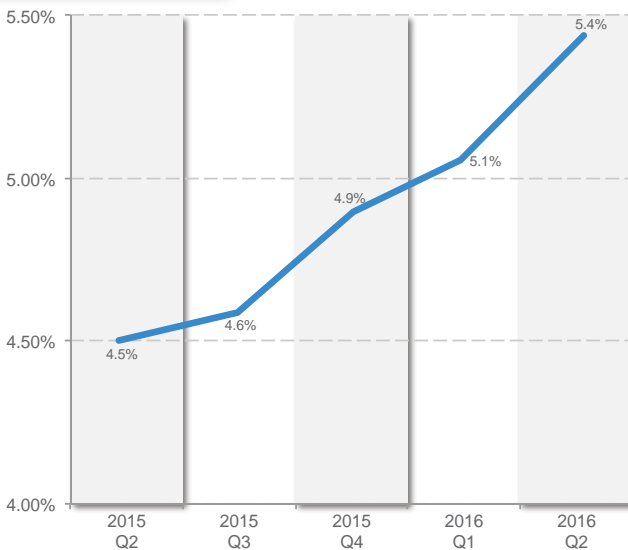
# HOUSTON

## TRENDING NOW

### NET SF ABSORPTION



### VACANCY RATE



Houston's regional economy continues to battle with effects of the fall in oil prices, and that has caused significant shifts in the industrial property market. Hardest hit have been those companies involved in exploring for and extracting crude oil and natural gas, the so-called upstream users. They have responded by cutting operating budgets through drastic reductions in capital expenditures and personnel. Oil prices moved up early in Q2, but were on the way back down toward \$40 per barrel as the period ended due to global economic uncertainty and surplus supply. So, energy sector woes are far from over and the industry is likely to continue with current austerity measures for the time being.

Downstream energy companies are enjoying higher profit margins due to the lower feedstock costs. Petrochemical companies are expanding as a result. There is an estimated \$60 billion being spent on petrochemical construction projects in the Houston area. Exxon, Chevron Lyondell Basell and Dow Chemical all have major projects in the works. Output from these operators should boost exports from the Port of Houston, assisted by the completed Panamax project, which allows for the passage of larger vessels through the Panama Canal.

Changing demand is causing a significant shift in leasing activity from the North/Northwest/North submarkets to the East/Southeast submarkets. Landlords with bulk distribution space in the North and Northwest are becoming more aggressive on lease terms, as tenants are choosing to move closer to the Port of Houston, and will pay a premium to do it. Throughout the city, owners of crane-served buildings (widely used by struggling upstream energy users) are lowering rates and increasing concessions to attract tenants. Of note

5.4%

VACANCY

\$6.51

AVG. SF RENTAL RATES

748,646

NET SF ABSORPTION

565,236,531

INDUSTRIAL SF INVENTORY

12,275,281

SF UNDER CONSTRUCTION

## Key Market Snapshots

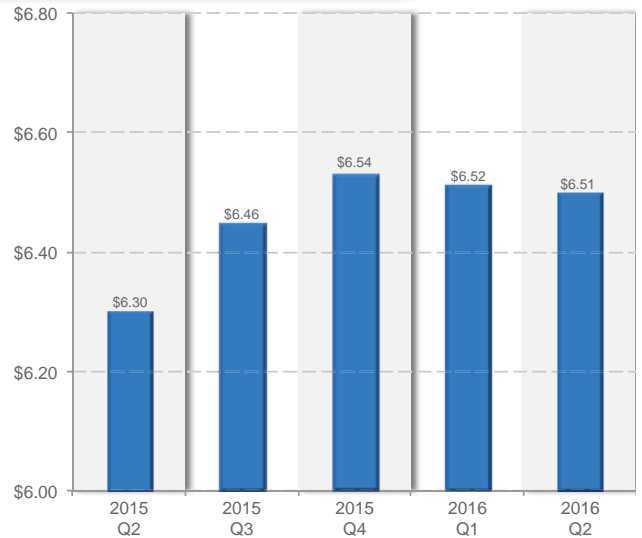
HOUSTON - TRENDING NOW  
(continued)

is the fact that many buildings are being offered for lease without an asking price. Some tenants are shifting their focus to purchase opportunities due to new lease accounting rules and low mortgage interest rates. Some landlords who are feeling the pain of the burn rate on their vacant properties, are deciding to sell rather than wait out the downturn. For owners of rail-served facilities throughout the region, it's a different story. Demand for those facilities over 250,000 square feet remains high, especially in the East submarket where supply is lowest.

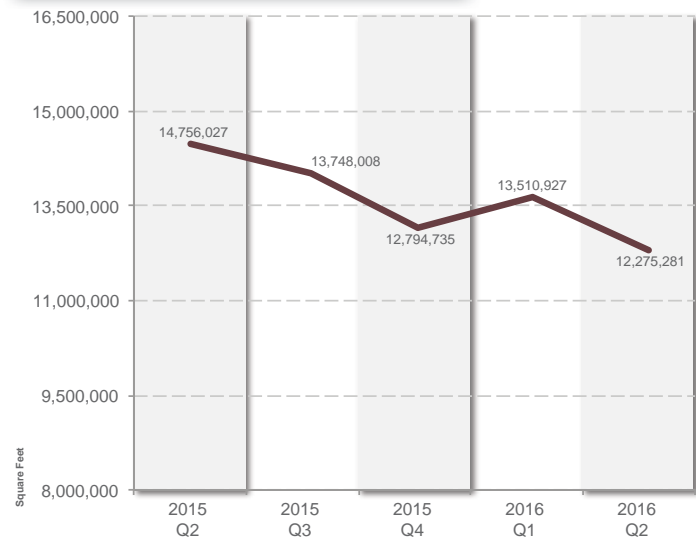
The vacancy rate for the Houston market moved higher for the fourth consecutive quarter in Q2. In the past year the region has experienced an 80-basis-point increase in vacant space, ending Q2 at 5.4%. Flex vacancy, which is included in the overall number, stands at 6.8%, up 10 basis points, while the warehouse market rose 30 basis points to 5.3%. In all, the Houston region contains almost 550 million square feet of industrial space after adding another 2.6 million square feet of new product in the second quarter. Another 12.3 million square feet is currently in the construction pipeline, including the Daiken HQ, a fully-committed 3.9 million square foot building, and an 800,000 square foot building fully leased to FedEx.

Net absorption remained in positive territory, adding over 748,000 square feet to the total of occupied space, despite rising vacancy. A significant share of new deliveries are immediately occupied, increasing absorption, but speculative deliveries increase the vacancy rate at the same time. Considering the severity of the energy downturn, the Houston industrial market is doing remarkably well. The overall average asking lease rate is up \$.21 year-over-year, but fell by a penny in Q2 to settle at \$6.51. Warehouse rents actually moved up \$.02 during the quarter, ending \$6.17.

## AVERAGE SF RENTAL RATES



## SF UNDER CONSTRUCTION

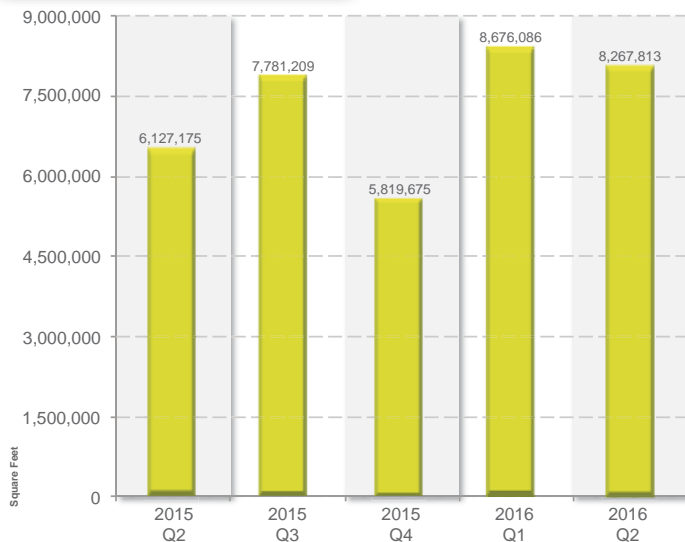


## A LOOK AHEAD

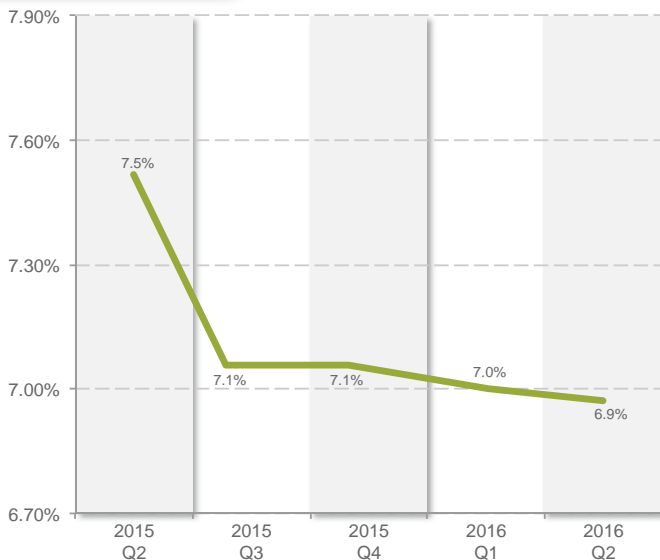
- Gross leasing activity will remain strongest in the East submarkets
- Net absorption will vary widely by region, with decreases to the West and North and increases in the East
- Vacancy will move slightly higher overall, but decline in the East by as much as 150 basis points
- Rents in the East will rise by 5% by year end
- Landlords and tenants will be signing shorter term leases due to near term market uncertainty
- Construction will slow in the Northwest / North submarkets, but remain active in the East and Southeast
- Pricing for NET land (net of detention with public utilities) will range from \$3.50 to \$5.00 per square foot depending on tract size

# CHICAGO

## NET SF ABSORPTION



## VACANCY RATE



## TRENDING NOW

While Chicago has been and will remain a key transportation hub, high levels of taxes and regulation present a significant, if not insurmountable, problem for area businesses. However, other nearby markets like Northwest Indiana and Southeast Wisconsin do present a significant challenge to the Chicago area, as these areas are seen by many more business-friendly and less expensive areas to do business. While there has been some movement to those areas, it has not been the mass exodus that many predicted. Chicago's central location and extensive air, rail and trucking infrastructure just can't be ignored. Due to its fundamental strengths, the region continues to attract institutional investment in industrial product. Unlike some other transportation hubs around the country, the Chicago area also has a significant manufacturing sector, which provides additional overall market balance. While the manufacturing sector has been struggling of late, it continues to contribute substantially to Chicago's local economy.

Vacancy for the region continues to decline. By the end of Q2, the overall vacancy rate fell by 10 basis points to 6.9%. Year-over-year that represents a 60 basis point decline, making life more difficult for tenants looking for functional expansion space. Competition for quality product is intense, especially in submarket like O'Hare and the 1-55 Corridor. Add the facts that tenants are faced with higher taxes and more regulatory controls, it is easy to understand why tenants are looking to more "business-friendly" markets to meet their expansion needs.

The drop in vacancy has resulted in a corresponding increase in lease rates. At the end of Q2, the average

6.9%

VACANCY

\$5.71

AVG. SF RENTAL RATES

8,267,409

NET SF ABSORPTION

1,172,258,839

INDUSTRIAL SF INVENTORY

14,273,812

SF UNDER CONSTRUCTION

## CHICAGO - TRENDING NOW (continued)

asking rental rate in the Chicago metro area stood at \$5.71, up \$.02 in the period and \$.24 higher year-over-year. Lease rates are moving up faster for Class A product, which is a scarcity in the Chicago market. For tenants who can work around functional issues associated with Class B and C space in other submarkets like North Kane County and Southeast Wisconsin, there are more buildings to choose from.

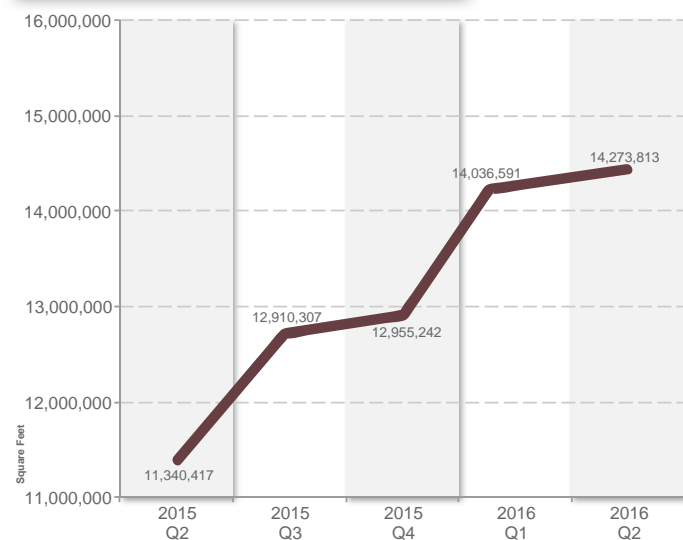
Positive net absorption for Q2 hit over 8.2 million square feet, with larger distribution deals accounting for the bulk of net gains in occupied space. In 2015, over 20.3 million square feet of net absorption was reported. Through, the first half of 2016, 6.3 million square feet of space has been absorbed, compared to 6.9 million square feet for the first half of 2015. However, as we reported last quarter, much of the existing inventory lacks the clear height, fire-suppression and truck access preferred by today's distributors, which could force more expanding tenants to give those other markets a harder look going forward.

New deliveries totaled more than 3.8 million square feet in Q1, and another 1.9 million square feet was delivered in the second quarter of 2016. Currently, 15.3 million square feet is still under construction. The largest project delivered in Q2 was a 626,848-square-foot spec building at 1750 Bridge Drive, which is still unoccupied. New construction remains primarily in larger distribution facilities. Tightening vacancy has emboldened developers to keep building more speculative product to add to the existing industrial base, which topped 1.17 billion square feet by the end of Q2.

### AVERAGE SF RENTAL RATES



### SF UNDER CONSTRUCTION



## A LOOK AHEAD

- Expect a lull in sale/lease activity this summer as compared to the first half of the year
- Average asking lease rates should keep making modest gains
- After slowing over the past few months, expect net absorption to pick back up for the balance of the year
- Construction activity should maintain current pace over the next several quarters
- Leasing activity should keep pace with new construction, keeping vacancy in the 7% range
- Look for redevelopment as an emerging trend

# ST. LOUIS

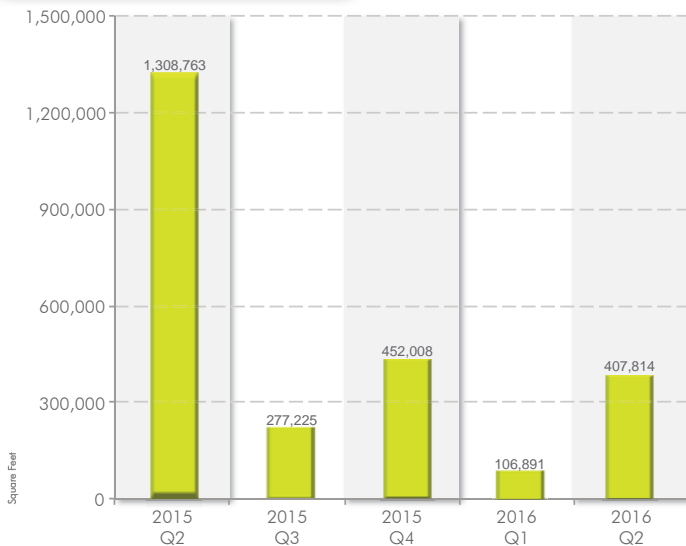
## TRENDING NOW

Three major economic drivers are giving a significant boost to the St. Louis area economy. First is the award of Tax Increment Funding dollars to redevelop the former Chrysler site in Fenton and the Ford site in Hazelwood. Second is the recent award of over \$2 Billion for the National Geo-spatial Intelligence Agency facility in the struggling North St. Louis City area. Third is the high level of tech-based venture capital coming to the St. Louis area. Cultivation Capital, the largest VC investor in Missouri, is investing in numerous regional start-ups. Combined, these three major initiatives will result in thousands of good-paying jobs, which helps to offset the estimated \$80 Million in lost commercial activity due to the departure of the St. Louis Rams.

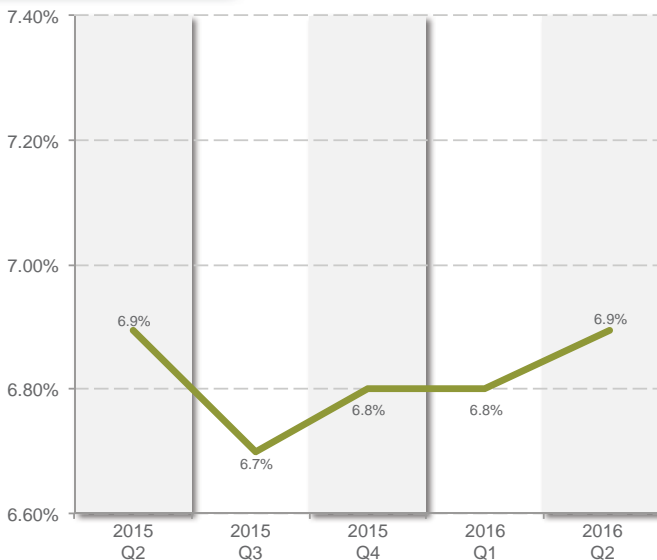
The industrial base in St. Louis moved up to 264.2 million square feet in Q2, after another four new buildings totaling 1.1 million square feet were delivered. As the period ended, 4.7 million square feet of industrial space was underway, with most of that being built on a speculative basis. Over 88% of recently completed speculative space has been preleased prior to completion. Recent large transactions in new space include two 700,000-square-foot buildings leased by Amazon, a 1 million-square-foot facility for Schnuck's supermarkets, SKF's 400,000-square-foot distribution center and an 800,000-square-foot build-to-suit for Reckitt Benckiser. All these new facilities have the high ceiling clearance and fire suppression systems preferred by today's expanding businesses.

Institutional demand for quality distribution product is still intense, prompting some developers to sell right away to take advantage of the cap rate compression that has found its way to the St. Louis area. Developers have responded by acquiring more land in anticipation of continuing strong demand for new product.

### NET SF ABSORPTION



### VACANCY RATE



6.9%

VACANCY

\$4.23

AVG. SF RENTAL RATES

407,814

NET SF ABSORPTION

264,253,475

INDUSTRIAL SF INVENTORY

4,735,533

SF UNDER CONSTRUCTION



## Key Market Snapshots

ST. LOUIS - TRENDING NOW  
(continued)

Unfortunately, development of smaller building is not in the offing, leaving demand from owner/users running well ahead of supply. The economies gained by building larger distribution product, coupled with such strong demand from the larger players, remains the safer play for area builders.

Landlords of existing buildings are having a tough time competing with first generation space, as small bay sizing is affecting racking patterns impacts distribution users looking to maximize warehouse capacity. However, quality space is becoming scarce and owners of the best buildings are tightening up on concession packages, demanding longer lease and insisting on stronger credit. Tenants looking for quality have to move fast and be willing to compete, as the best space moves quickly.

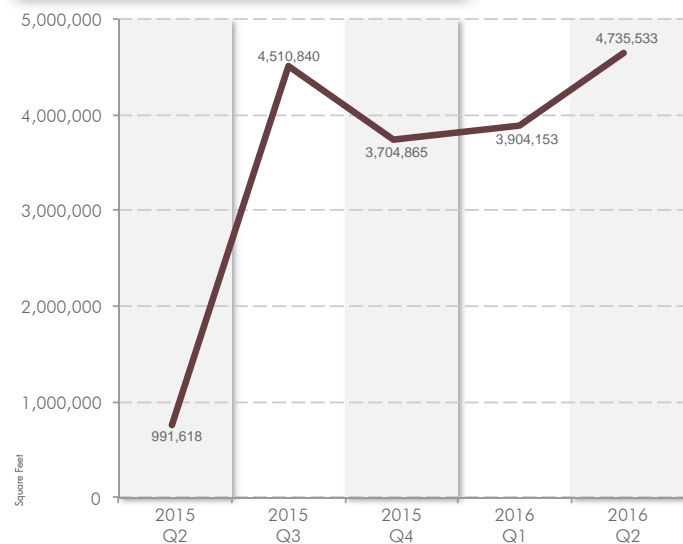
In Q2, net absorption bounced back to finish the period at nearly 408,000 square feet, after a sluggish gain in occupancy of just 107,000 square feet in Q1. Overall average asking lease rates rose by \$.06 in Q2 to finish the period at \$4.23. Year-over-year, the rate has risen by just under 3%, lower than many other major markets around the country like Los Angeles and Long Island, New York that have tighter supplies and lower levels of construction activity.

The vacancy rate finished the quarter at 6.9%, an increase of 20 basis points over Q1, unchanged year-over-year. Bulk distribution deals still account for the biggest share of market activity but, due to a large pool of skilled manufacturing labor, the manufacturing sector is still expected to contribute significantly in the coming years. The 2 million-square-foot redevelopment of the old Chrysler plant in Fenton is expected to include a significant amount of space to accommodate manufacturers.

## AVERAGE SF RENTAL RATES



## SF UNDER CONSTRUCTION

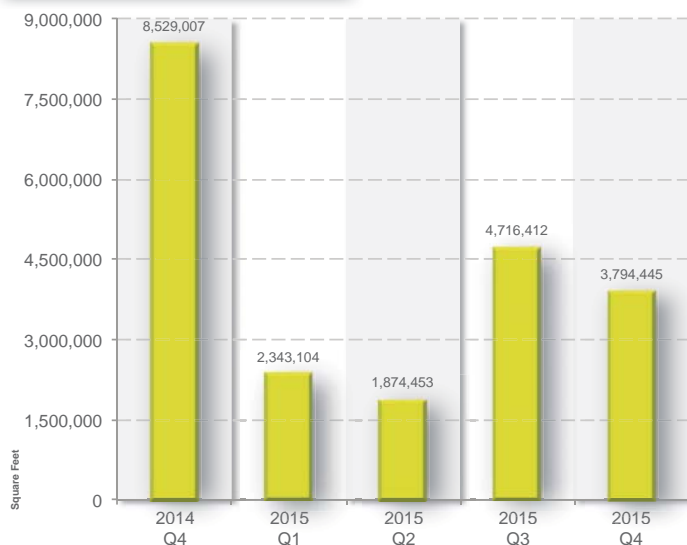


## A LOOK AHEAD

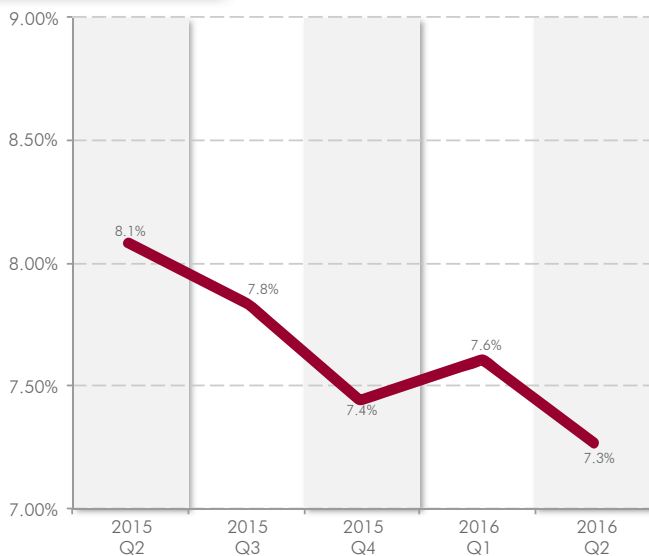
- Leasing activity should continue to increase
- Sale activity will be held back by short supply, which will keep prices moving up
- Vacancy will remain stabilized in the 6% range due to new deliveries
- Average asking lease rates should move up by 7% in 2016
- Construction activity will increase by 15% or more in the coming quarters
- Users who build their own facilities will build more space than they currently need to accommodate future growth and as a hedge against rising construction costs

## ATLANTA

## NET SF ABSORPTION



## VACANCY RATE



## TRENDING NOW

Atlanta's industrial market remains one of the nation's top performers. Activity in bulk distribution buildings is still extremely strong. Net absorption for Q2 hit nearly 5.2 million square feet during the period, mainly in warehouse product. The quarter's biggest move-in honors go to Wayfair for its 846,496-square-foot lease at King Mill Distribution Park. Net absorption for all of 2015 hit 13.5 million square feet and 2016 is running almost double that pace through the first half of the year vs the same period last year. So, 2016 is shaping up to be another outstanding year in terms of net growth in occupied space.

Vacancy moved down in Q2 with a decline of 30 basis points to 7.3%. Year-over-year vacancy is down by 80 basis points despite high levels of construction. Tenants are still paying a premium for greater functionality offered in newer product. They like the high ceiling clearance and more advanced fire suppression technology that allows greater cubic storage capacity. Landlords see the strong demand as an opportunity to squeeze tenants by offering little in the way of tenant improvements and free rent. Tenants deciding to move up to more functional product have to be ready to sign on the dotted line, as most of the new space being built is either preleased or snapped up just after being delivered to the market. So, it is important for tenants who need to move to get out in front of the decision by starting the move process early.

Development activity is still robust. Last year nearly 7.9 million square feet of industrial space was delivered. In Q1, another 5.9 million square feet was completed, and Q2 added nearly 4.2 million square feet to bring Atlanta's industrial inventory up to 607.6 million square feet. Almost 12.7 million square feet is under

7.3%

VACANCY

\$4.31

AVG. SF RENTAL RATES

5,119,575

NET SF ABSORPTION

607,617,459

INDUSTRIAL SF INVENTORY

12,675,979

SF UNDER CONSTRUCTION

## Key Market Snapshots

ATLANTA - TRENDING NOW  
(continued)

construction. Large distribution users are glad to see development of so much speculative space in Atlanta, as it allows for more flexibility in terms of their expansion planning. Only one building delivered in 2015 remained vacant by the end of Q2. Speculative space deliveries continue to outpace build-to-suit projects by a wide margin.

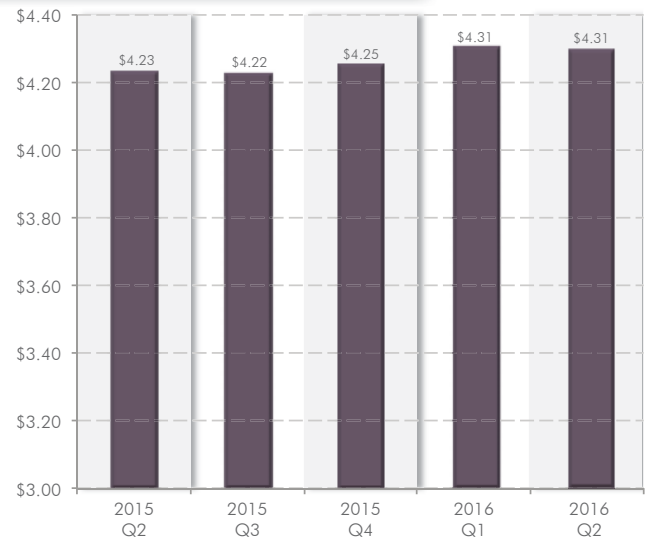
Activity in general industrial product is also strong. Lease rates have risen and some tenants are running short of quality facilities to choose from as they look to expand. As we reported last quarter, construction in prime niche markets like Union City, Kennesaw and Suwanee/Buford has picked up, as well-located, quality buildings have seen recent rent growth rates as high as 20%-30%. The manufacturing sector is another story. Unlike the distribution sector, which is still rapidly expanding, manufacturing activity across the country has declined over the past year, and that could negatively impact leasing activity for manufacturing product going forward.

Investor demand for quality industrial product in the Atlanta area is still running well ahead of supply. Cap rates are at or near all-time lows for all industrial product types, and there's still a lot of available capital looking for a place to call home in Atlanta. Large bulk distribution product is still the big prize, and institutional investors are competing aggressively to make acquisitions. They can't ignore the stellar performance in that sector over the past several years. Lack of suitable up-leg product remains a problem, as many would-be sellers refuse to face the consequences of cashing out. Fear of cap rate decompression has been subdued by the Fed's failure to make further moves on interest rates due to uncertainty over job growth at home and the UK's recent vote to leave the European Union.

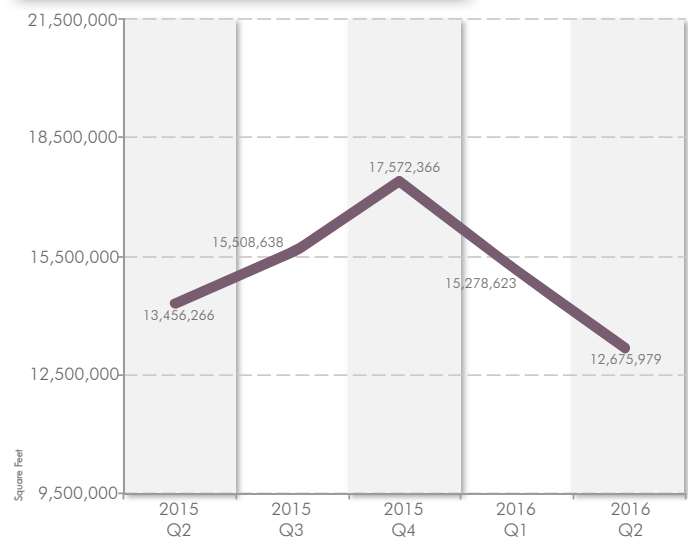
## A LOOK AHEAD

- Leasing activity should stay near current level for the rest of the year
- High rate of new deliveries will moderate declines in vacancy
- Overall average asking lease rates should increase by 5% in 2016
- New deliveries will remain at current levels for 2016
- Rents will still move up faster and lease up times will be shorter for product near I-285
- The market will test the efficiency of 40-foot clear heights with a 1 million-square-foot spec building
- Construction of two stadiums is driving up labor cost and causing delays

## AVERAGE SF RENTAL RATES



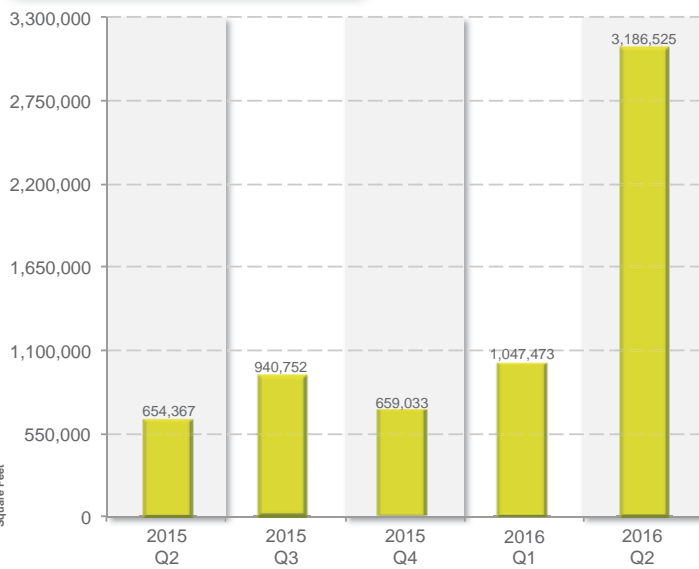
## SF UNDER CONSTRUCTION



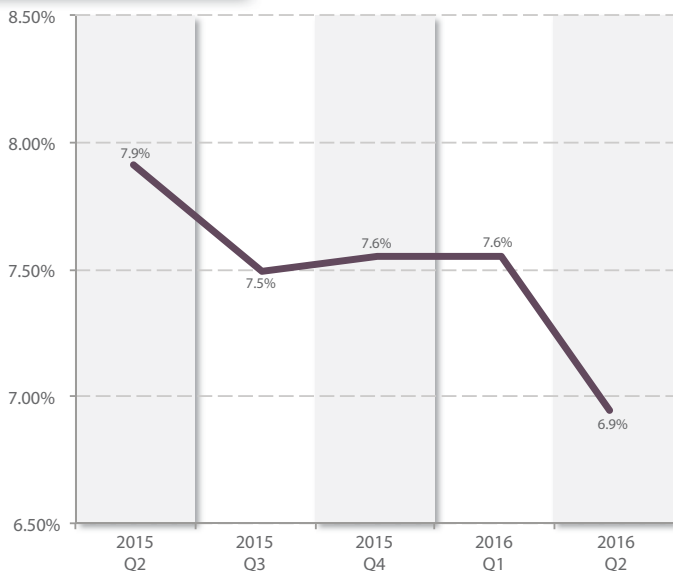
# GREENVILLE/SPARTANBURG

## TRENDING NOW

### NET SF ABSORPTION



### VACANCY RATE



The Greenville/Spartanburg area is located between the larger markets of Atlanta and Charlotte, NC. Interstate highways 26 and 85 cross in the center of the region that also has easy access to the deep water Port of Charleston that can handle 8,400 TEU vessels drafting up to 48 feet. To extend the reach of the port and boost efficiency for the movement of international freight, the South Carolina Inland Port was opened in 2013. The project has performed much better than expected, experiencing year-over-year growth of over 100%. Also known for its pro-business environment, major companies like Michelin North America, General Electric, Verizon, Hubble Lighting, BMW and Fluor Corporation have responded by making major commitments to the area. That has attracted a highly qualified workforce looking for new, high-paying job opportunities, along with a wide variety of suppliers and sub-contractors who are also looking to hire more workers

As a result of the rapidly expanding business base, net absorption of industrial space has been consistently positive. In Q2, nearly 3.2 million square feet was added to the total of occupied space, almost triple the total for Q1, and more than was recorded in all of 2015. If not for scarce availability in the smaller size ranges, where demand is especially strong, absorption totals would be even higher. Absorption of this magnitude rivals that of markets that double or triple the region's 202-million-square-foot base inventory.

Demand is still running well ahead of supply in all size ranges. Vacancy moved down again in Q2 by 20 basis points to end the quarter at 6.9%, a post-recession low. Despite the delivery of over 3 million square feet of new space during the quarter, tenants are still running short

6.9%

VACANCY

\$3.64

AVG. SF RENTAL RATES

3,186,525

NET SF ABSORPTION

202,294,891

INDUSTRIAL SF INVENTORY

4,689,462

SF UNDER CONSTRUCTION

## GREENVILLE / SPARTANBURG - TRENDING NOW (continued)

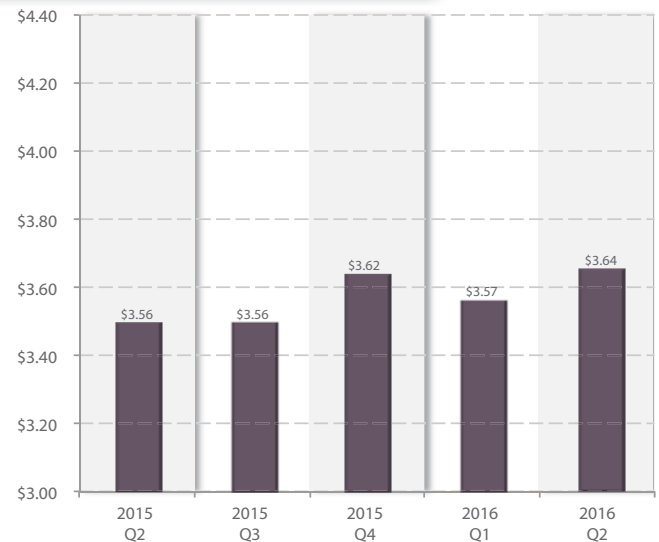
of options, as development of new product is just not keeping pace with demand. Developers and conventional lending sources have been conservative in their approach to new spec development, and the supply of quality sites for build-to-suits, especially in the Greenville area, is tight and getting more expensive. So, builders are taking a harder look at neighboring Spartanburg and Anderson Counties along the I-85 corridor for new projects.

Builders with non-traditional funding are in a stronger position to take full advantage of speculative opportunities, as recent projects have been leasing up within six months of completion, despite higher rents. The pipeline of space under construction for Q2 totaled nearly 4.7 million square feet. But, that may not even be enough to satisfy current demand, which is often based on immediate need. Tenants, hungry for space, are willing to pay a premium to get it. Essentially, they have little other choice, as existing inventory of quality product available for lease has run short, as well.

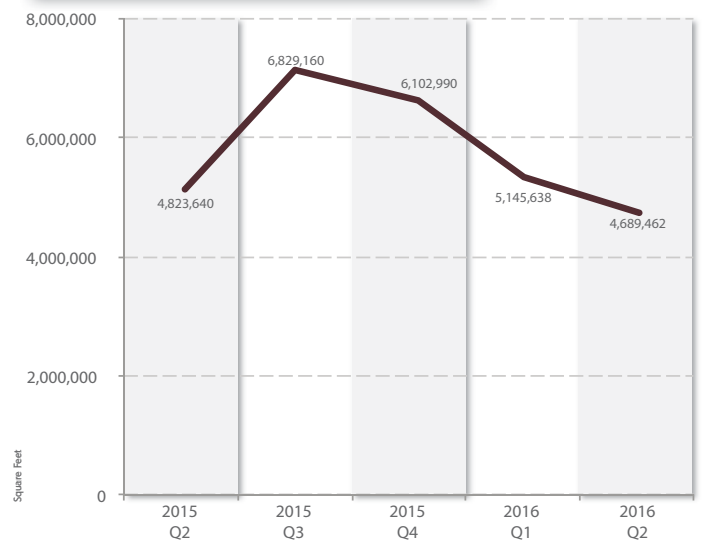
Average asking rents moved up another \$.06 to \$3.64. Greenville County and the Highway 101 and 290 segment of Spartanburg County are still the most active areas because of the proximity to major corporate users. Landlords are taking full advantage of the rising rents and are showing little interest in selling properties that are performing so well. So, there are still more buyers than sellers for quality properties.

Recent transactions getting attention include Colgate-Palmolive's move into 306,000 square feet along the I-85 Corridor near White Horse Road, and a major facility for Rite-Aid Corporation. That 900,000-square-foot concrete tilt-up building officially opened one year after ground was broken. The facility, located near I-85 between Highways 9 and 221 near the inland port, sits on 97 acres.

### AVERAGE SF RENTAL RATES



### SF UNDER CONSTRUCTION



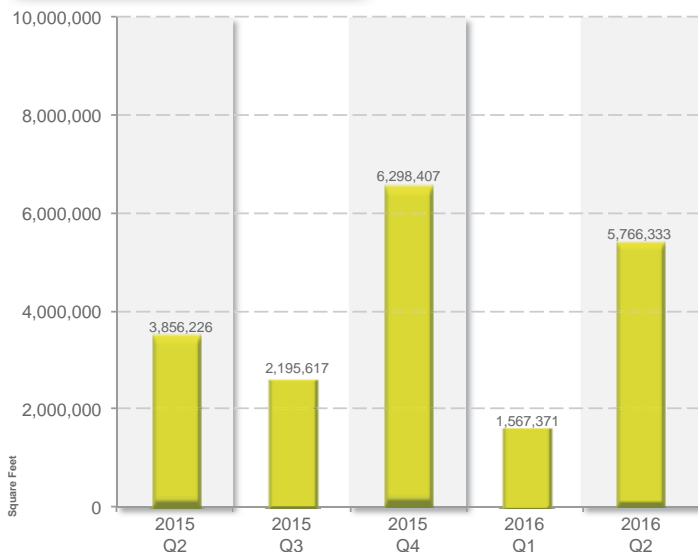
### A LOOK AHEAD

- Lease and sale activity should increase in 2016
- Net absorption will vary significantly quarter to quarter based on delivery of new space
- Vacancy will keep moving lower for the rest of the year
- Lease rates will keep moving up, especially for first generation space
- Development activity will increase in response to strong business growth
- Banks will continue to be cautious on lending for spec projects

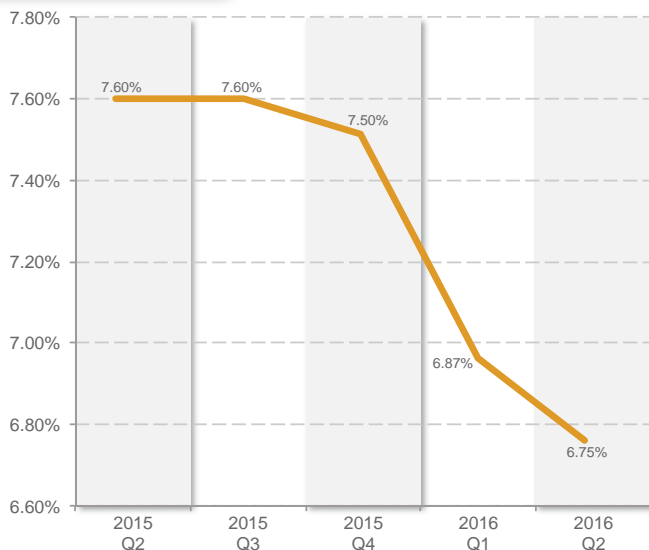
# PHILADELPHIA

## TRENDING NOW

### NET SF ABSORPTION



### VACANCY RATE



With a base inventory of just over 1 billion SF, the Philadelphia industrial market is one of the top five industrial hubs in the nation. The region includes Eastern Pennsylvania, Southern New Jersey and all of Delaware. Like other major metro markets in the US, the area continues to experience declining vacancy, rising lease rates and steady, positive net absorption.

As a direct result, lease renewal activity has been on the rise, especially in the Lehigh Valley, the region's most active submarket. Vacancy there is running at historic lows and development activity is struggling to keep pace with rising demand. Average time from delivery to lease execution in the Lehigh Valley is three to four months, and almost 40% of the space currently under construction is already committed. For tenants requiring more than 500,000 SF in the Lehigh Valley, options will be limited going forward as few projects with footprints that large are in the pipeline. That may be good news for landlords of available Class A product in peripheral submarkets.

In our "Core Data Set" (which focuses on industrial properties of at least 100,000 SF) there was roughly 12 million SF under construction across the market at the end of Q2. Approximately 6.5 million SF was delivered in Q2, with half of that new space leased prior to delivery. Developers seeking entitlements for future development have found it increasingly difficult market-wide, with fully entitled sites becoming increasingly rare. Existing land use constraints and scarcity in general have escalated land acquisition prices across the market. However, this has yet to have a negative impact on development activity, as investment capital continues to expand its reach in terms of both class and geography.

6.75%

VACANCY

\$4.76

AVG. SF RENTAL RATES

5,766,333

NET SF ABSORPTION

1,061,566,384

INDUSTRIAL SF INVENTORY

11,885,928

SF UNDER CONSTRUCTION



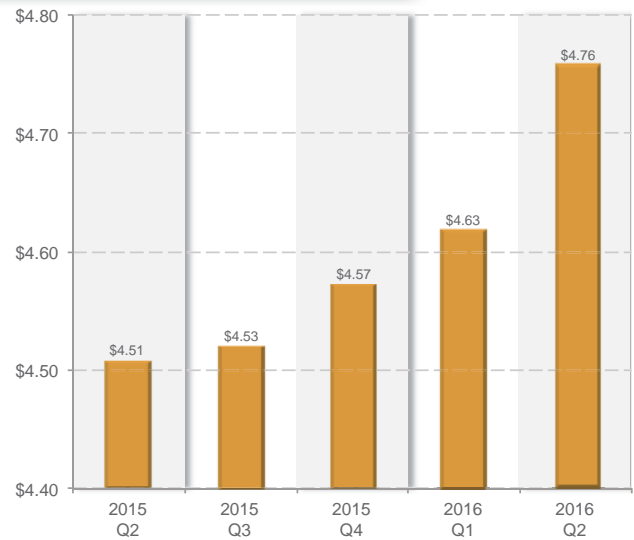
## PHILADELPHIA - TRENDING NOW (continued)

Tenants continue to be eager for new product in the popular submarkets of the Lehigh Valley and Central Pennsylvania, and demand for space in Central PA and the Lehigh Valley continues to lead the market. Southern New Jersey is also experiencing a rise in rental rates, and is emerging as the region's third most active submarket. Asking lease rates continue to climb as a result. In Q2, average rent moved up over 2%, or \$.10, to settle at \$4.76. That brings the year-over-year rise in rental rates to 5.02%.

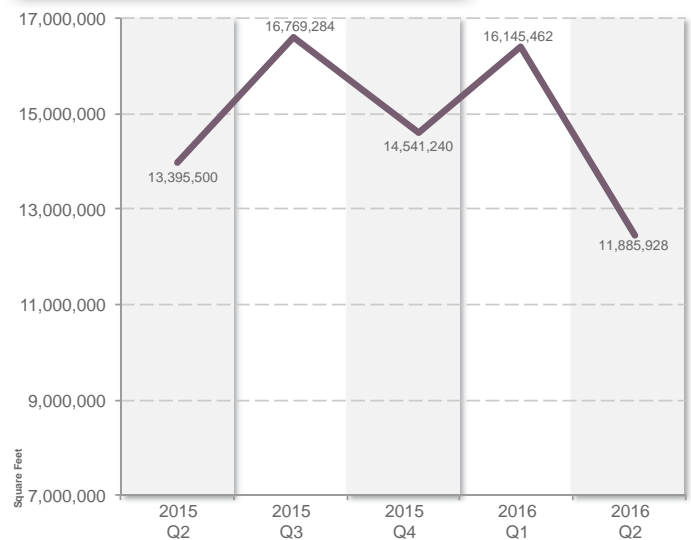
The Q2 regional vacancy rate for industrial product ticked downward slightly, ending the quarter at 6.75%, despite over 3 million SF of new space being delivered to the market as vacant. Net absorption was up from Q1, ending at a positive 5.77 million SF. With such strong net absorption, decreased vacancy makes clear the struggle between demand and new deliveries. This bodes well for ongoing high levels of speculative development, although a maturing pipeline and tendency toward large scale transactions will cause vacancy levels to fluctuate in Central PA.

Significant contributors to net absorption in Q2 include the 1.29 million SF leased by Starbucks and UPS's 335,000 SF lease in Central PA. In the Lehigh Valley, California Cartage, Fed Ex, and Behr Paint contributed to over 1 million SF in positive absorption, while Jet.com leased 700,000 SF at Matrix's new building at Gateway Business Park in Pedricktown, NJ. Also in New Jersey, Grainger completed its 1.3 million SF facility in Bordentown. In the past year over 12.7 million SF of gains in occupied space have been recorded.

### AVERAGE SF RENTAL RATES



### SF UNDER CONSTRUCTION

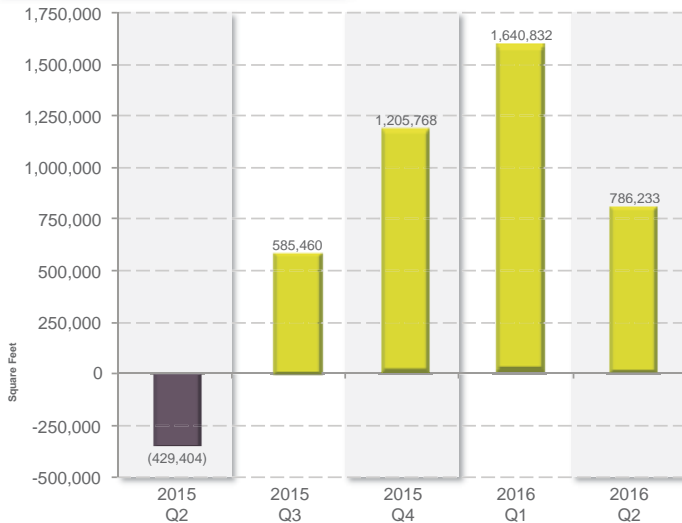


### A LOOK AHEAD

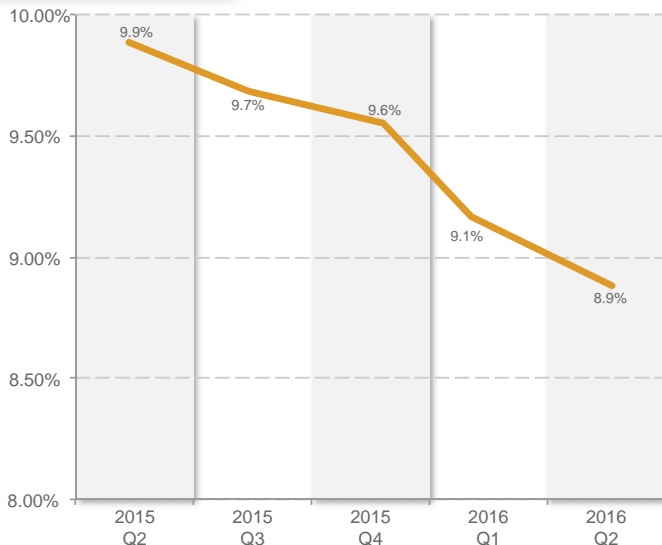
- Overall lease and sale activity will remain strong, driven by logistics-based business expansion
- Central Pennsylvania vacancy will fluctuate due to new deliveries and large-scale transactions
- Vacancy in the Lehigh Valley will remain at historic lows
- Class A space in the Lehigh Valley will cost more than \$5 this year
- Construction activity will maintain current momentum, maintaining the current balance with net absorption across the market
- Land prices will continue to set new records in the next several quarters

# BALTIMORE

## NET SF ABSORPTION



## VACANCY RATE



## TRENDING NOW

The Baltimore/Washington Corridor is driven primarily by the consumer market of one of the nation's largest MSAs. The e-commerce sector is located north of Baltimore, an area that competes with the Lehigh Valley and Exit 8A in New Jersey. The region also has a large government presence. Agencies located in the area include the NSA, DOD, NIH, the Department of Homeland Security and the Social Security Administration. Howard County is home to the largest concentration of engineers in the country. Johns Hopkins and the University of Maryland are among the major universities located within the region.

The Baltimore industrial market continued to tighten in Q2. Total base inventory grew to 237.3 million square feet after another 303,900 square feet came to market during the quarter. Significant projects delivered so far this year include the 300,000-square-foot Hollins Ferry Logistics Center at 4803 Hollins Ferry Road and the Chesapeake Commerce 1500 at 1500 Broening Hwy, a 263,500-square-foot building that is already 76% leased. Construction of even larger "big box warehouse" buildings has been focused north of Baltimore in Harford and Cecil Counties, while new big box projects are proposed for Tradepoint Atlantic, a 3,000 acre development project east of the city at the Sparrows Point Steel Mill.

Just over 1 million square feet was still under construction by the end of Q2. A lack of land continues to put constraints on development activity, and has pushed new projects further from I-95, the main trucking corridor. However, some builders are still reluctant to bring new projects on line, as higher construction costs require lease rates to be 20% above the rents achieved on second generation product.

8.9%

VACANCY

\$5.87

AVG. SF RENTAL RATES

786,233

NET SF ABSORPTION

237,342,026

INDUSTRIAL SF INVENTORY

1,052,916

SF UNDER CONSTRUCTION

### BALTIMORE - TRENDING NOW (continued)

The region recorded positive net absorption of 786,233 square feet in the second quarter, as compared to over 1.6 million square feet in Q1. In the past year, over 4.2 million square feet of net absorption has been recorded, almost all of that in the warehouse sector, as flex activity has been lackluster as of late. In fact, flex absorption was in negative territory in three of the last six quarters. Bigger deals contributing to absorption in 2016 include RPM's move to 283,000 square feet at 1411 Tangier Drive and Coastal Sunbelt Produce Company's lease of 244,500 square feet at 9001 Whiskey Bottom Road.

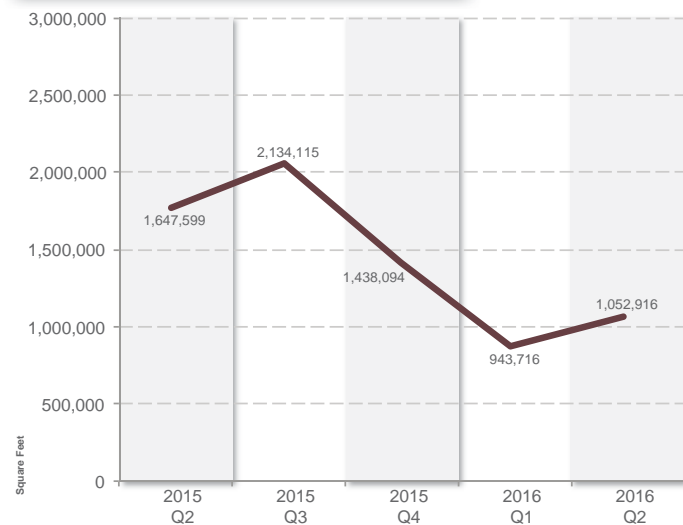
The vacancy rate declined by 20 basis points in Q2 to 8.9%, a year-over-year drop of 100 basis points. Vacancy has fallen below 9% for the first time in several years. However, some major submarket vacancy rates are ranging as high as 15%. In those areas, tenants still believe they have the upper hand, but is changing little-by-little as landlords continue to push for higher rents and a reduction of tenant concessions. Well-located, functional properties are commanding the highest rents, but tenants who can work around functional obsolescence can still find a good bargain. Overall, average asking rental rates remain relatively flat, having gained just \$.03 in the last four quarters. But, rates range much higher in prime submarkets.

Cap rates remain severely compressed and that is keeping existing local owners of industrial product out of acquisition mode. They fear that the market might be overheated. Despite the highest prices ever recorded, they tend not to be sellers either, as they are unwilling to cash out and suffer the tax consequences of an outright sale, and don't want to pay the price premium for up-leg exchange properties.

#### AVERAGE SF RENTAL RATES



#### SF UNDER CONSTRUCTION



#### A LOOK AHEAD

- Institutional buyers will continue to drive the investment sale market, as local owners stay on the sidelines
- Net absorption will moderate due to lack of quality product
- Average asking rental rates will move up by as much as 3% this year
- Vacancy will fall under 8% in the next several quarters
- Speculative development will be limited by the high price and limited availability of land
- Increased government spending should reduce uncertainty over the local economy

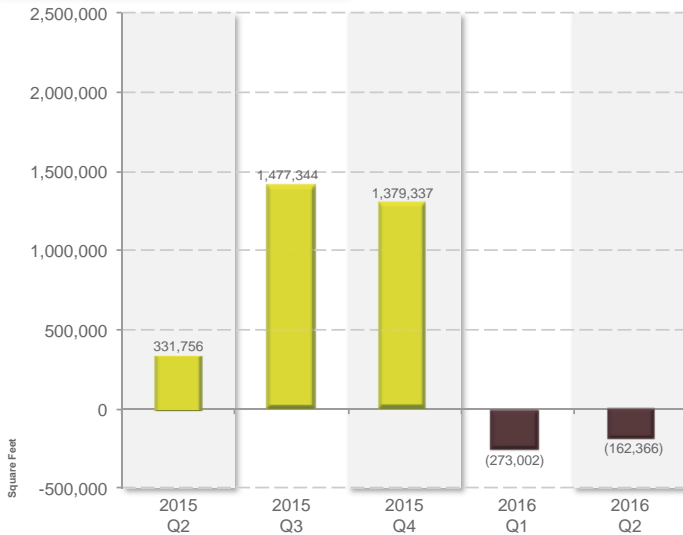
# LONG ISLAND / QUEENS

## TRENDING NOW

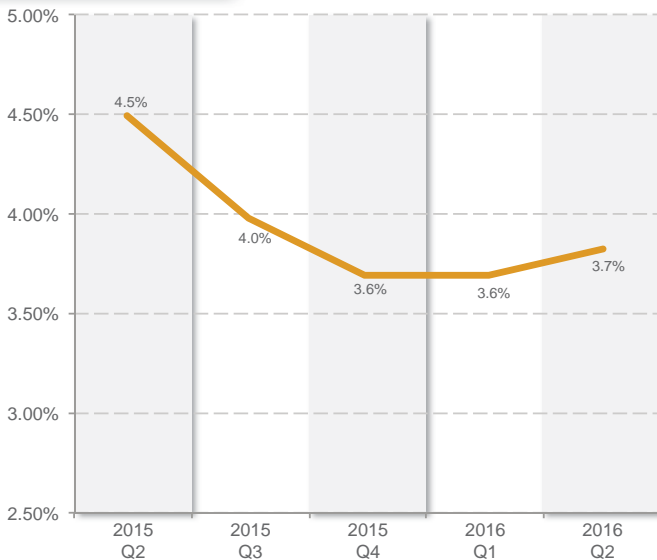
The supply of industrial property on Long Island has reached critically low levels. Many true industrial users are being forced to move to New Jersey where inventory is deeper and traditional industrial product makes up the market. This is particularly true for distribution users that can improve the flow of goods by locating along the Interstate 95 Corridor. Other industrial users are moving further east on Long Island to take advantage of government incentive programs. Most of the industrial-zoned properties now have residential overlays, and as the properties are gradually repurposed to residential use, the supply of industrial property is reduced. The potential for these so-called higher uses, have driven sales prices sharply higher, so much so that many industrial businesses cannot justify remaining in the area. Industrial product on the western edge of Long Island has been particularly impacted, as residential conversions are most prevalent there, while a limited amount of new development is occurring further east.

The industrial vacancy rate for Long Island increased to just 3.7% by the end of Q2, up 10 basis points year-over-year. Demand for distribution and general warehouse property continued to outpace supply, but delivery of new product remains at a standstill. That, coupled with residential conversions, is shrinking the industrial base and making the search for quality product even more difficult. Some property owners have been making improvements to mitigate functionally obsolete buildings in order to accommodate the needs of distribution users, but the process is expensive, and it generally makes more sense to give in to market forces and convert to residential uses. R&D space is faring better, though, as some older industrial product located near public transportation is being converted to R&D to capture higher rents.

### NET SF ABSORPTION



### VACANCY RATE



3.7%

VACANCY

\$14.13

AVG. SF RENTAL RATES

(162,366)

NET SF ABSORPTION

353,724,683

INDUSTRIAL SF INVENTORY

574,268

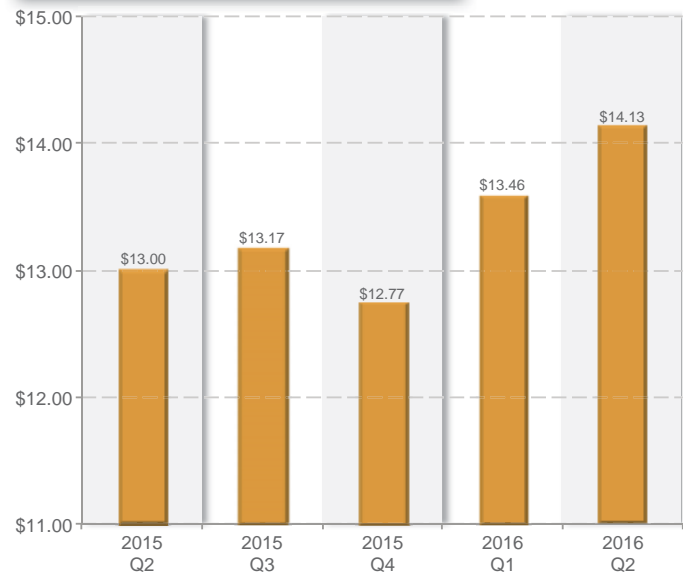
SF UNDER CONSTRUCTION

### LONG ISLAND / QUEENS - TRENDING NOW (continued)

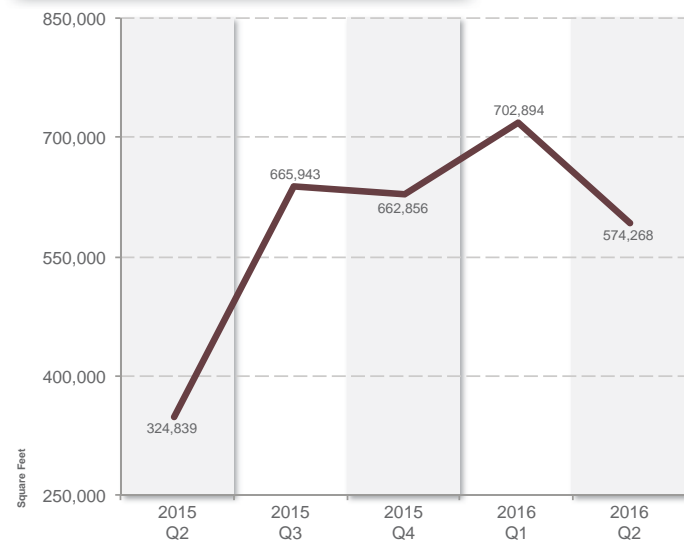
As a result of these trends, average asking lease rates have moved higher. In Q2, the rate for Long Island industrial space edged up \$.67 to \$14.13. Rising prices and tightening supplies are also prompting tenants to look to neighboring New Jersey for space. Local governments are responding by creating EDZ zones and offering tax incentives created to encourage industrial users to stay put. Net absorption for the Long Island market in Q2 came in at a negative 162,366 square feet, down 110,636 square feet compared to Q1. Demand remains ahead of supply, especially for users looking to upgrade the functionality of their facilities. This parallels a trend in markets throughout the country, like Central Los Angeles, that have a disproportionate amount of older product.

The low cost of capital continues to fuel owner/user demand, but the up-zoning of industrial properties makes it even harder for industrial users trying to grow their businesses without leaving the area. Even with today's low interest rates for fixed term financing, owner/users just can't compete with developers looking to build high density residential product. Development of owner/user product is at a standstill, and that fact is not likely to change. Values for the few owner/user properties that do come to the market, are selling for as high as \$200 per square foot.

#### AVERAGE SF RENTAL RATES



#### SF UNDER CONSTRUCTION



#### A LOOK AHEAD

- Gross leasing activity will be challenged by low supply of functional industrial space
- Average asking lease rates for industrial space in Queens will be in the \$20 per square foot range vs \$13 for Nassau County
- Construction will be limited to residential conversions in Queens and R&D conversions on Long Island
- Sale demand will remain strong, but supply will get even tighter
- EDZ zones will continue to encourage new development and boost activity in eastern submarkets
- Residential conversions in Queens/Brooklyn port areas will shift more port activity to Port Elizabeth/Newark

## SELECT TOP INDUSTRIAL LEASES Q2 2016

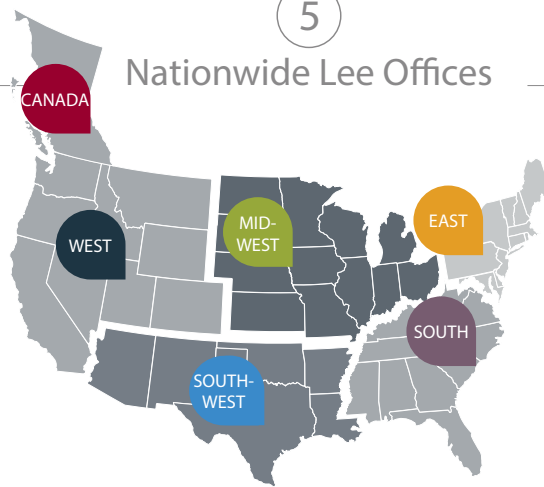
BUILDING	MARKET	SF	TENANT NAME
Duke Perris Logistics Center	Inland Empire	1,244,874	Wayfair, Inc.
Trammell Crow at 35 Eagle Bldg B	Dallas/Ft Worth	1,041,879	Amazon
The Oaks Logistics Center	East Bay/Oakland	1,003,267	Tesla Motors
130 Distribution Drive	Atlanta	846,496	Wayfair, Inc.
1125 Remington Blvd.	Chicago	767,161	Amazon
Gateway East 717	St. Louis	717,250	Amazon.com, Inc.
26090 23 Mile Rd	Detroit	711,547	Topvalco, Inc.
Gateway Business Park - 700	Philadelphia	705,000	Jet.com
965 Cranbury South River Rd	Northern NJ	550,050	TFH Publications
1635 S. 43rd Ave	Phoenix	394,775	Netle Water
i3-Bldgs A/B/C	San Diego	316,262	Illumina, Inc.

## SELECT TOP INDUSTRIAL SALES Q2 2016

BUILDING	MARKET	SF	PRICE PSF	CAP RATE	BUYER	SELLER
101 Possumtown St	Northern NJ	360,000	\$347.22	4.76%	QTS Realty Trust, Inc.	DuPont Fabros Technology
100 Louis Pkwy	Philadelphia	400,596	\$72.02	5.65%	Industrial Property Trust	IDI Gazeley
Riverside Business Center Bldg A	Atlanta	653,484	\$62.15	5.1%	Clarion Partners	Brookefield Property Partners
5555 Auto Mall Pkwy	Oakland	177,041	\$160.98	4.5%	LBA Realty	Lifestyle Solutions, LLC



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Q2  
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COMMERCIAL REAL ESTATE SERVICES