



Commercial Market Insights

For the RE/MAX Commercial Practitioner and our Clients

Third Quarter 2009

Office • Industrial • Apartments • Retail

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RERC REAL ESTATE[®]
RESEARCH
CORPORATION

National Overview

Economic Environment

The 2.8-percent growth rate in gross domestic product (GDP) for third quarter 2009 was exciting news indeed. Even when it became clear that much of the growth was due to government spending in the “cash for clunkers” program and the \$8,000 tax credit for first-time homebuyers, we were relieved that it looked like the economy was finally climbing out of its hole. In addition, stock market returns have been increasing and a few investors are returning to the fold. Although the housing market remains weak, we are seeing signs of stability.

But typical to most recovery periods, it seems that for every positive sign we see, there are other indicators that detract from the progress and remind us that there are still many issues unresolved. The \$1.4 trillion federal deficit, double-digit unemployment, a million or more delinquent or about-to-be foreclosed on residential real estate mortgages, and hundreds of regional banks at risk of failure due to the commercial real estate loans on their books are just a few of the difficulties ahead. But for those with the stamina, means, and vision to persevere in this uncertain environment, the rewards may be worth the effort.

What Does This Mean for Commercial Real Estate?

It has been said that everything is relative. For example, if we have lost \$7 trillion in stock values since the bottom of the market dropped out last fall, and \$6 trillion in housing wealth since home values started falling, then the \$2 trillion in commercial real estate write-downs, as reported by CBRE Econometric Advisors (formerly Torto Wheaton Research), does not seem so huge or so hard to take.

Relatively speaking, this may be true. But for real people and real investors, this loss in value is immense. The industry has much pain in store before

this loss is settled. According to the Dec. 2, 2009 *Beige Book*, commercial real estate is described as weak and deteriorating in all districts. Fundamentals have continued to suffer, and we are seeing increasing vacancy rates and declining rents. In addition, the banking industry is experiencing “steady to softer conditions,” with some districts seeing weak loan demand. Credit standards on commercial loans in some districts were noted as increasingly tight. As the challenges for commercial real estate investments intensify, expect credit to remain tight, more commercial real estate foreclosures to occur, and more banks to fail.

Transaction Analysis

Transaction volume peaked in second quarter 2007, and fell nearly 90 percent before bottoming out in first quarter 2009.

National Transaction Breakdown 12-Month Trailing Averages (10/01/08 – 09/30/09)				
	Office	Industrial	Retail	Apartment
< \$2 Million				
Volume (Mil)	\$1,514	\$2,693	\$2,832	\$1,186
Size Weighted Avg. (\$ per sf/unit)	\$89	\$50	\$85	\$48,108
Price Weighted Avg. (\$ per sf/unit)	\$126	\$81	\$128	\$73,444
Median (\$ per sf/unit)	\$94	\$59	\$86	\$53,472
\$2 – \$5 Million				
Volume (Mil)	\$2,167	\$3,165	\$3,567	\$2,457
Size Weighted Avg. (\$ per sf/unit)	\$117	\$60	\$136	\$62,613
Price Weighted Avg. (\$ per sf/unit)	\$194	\$99	\$236	\$112,497
Median (\$ per sf/unit)	\$166	\$76	\$199	\$88,438
> \$5 Million				
Volume (Mil)	\$20,474	\$7,176	\$10,829	\$12,176
Size Weighted Avg. (\$ per sf/unit)	\$209	\$65	\$148	\$84,392
Price Weighted Avg. (\$ per sf/unit)	\$352	\$117	\$262	\$134,061
Median (\$ per sf/unit)	\$182	\$80	\$164	\$86,667
All Transactions				
Volume (Mil)	\$24,154	\$13,035	\$17,229	\$15,819
Size Weighted Avg. (\$ per sf/unit)	\$181	\$60	\$130	\$75,990
Price Weighted Avg. (\$ per sf/unit)	\$323	\$105	\$235	\$126,167
Median (\$ per sf/unit)	\$122	\$65	\$113	\$71,060
Source: RERC.				

Although overall quarterly transaction volume has been inching upwards since then, RERC's 12-month trailing overall volume continued to decline during third quarter 2009.

In addition, signs of pricing stabilization were present for the office, retail, and apartment sectors on a quarterly basis during third quarter 2009, although the industrial market is still seeing size-weighted price declines. However, RERC's 12-month trailing size-weighted prices continued to decline across the four core property types during third quarter.

The 12-month trailing weighted average capitalization rates increased for all property types during third quarter 2009. These rates have been steadily increasing since fourth quarter 2008.

However, the quarterly weighted average capitalization rates bottomed out around first quarter 2008, and are starting to show signs of stabilization with third quarter 2009's mixed results. Rates for the office sector declined by 10 basis points, while rates for the industrial sector increased by 50 basis points. The weighted average capitalization rate for the retail sector was unchanged, and the rate for the apartment sector increased by 30 basis points.

Property fundamentals continue to deteriorate on a national level. Vacancy rates increased for all property types during third quarter 2009, and are forecasted to continue to climb throughout the majority of 2010. Rents have been on a downward trend, and are projected to continue in this direction throughout 2010.

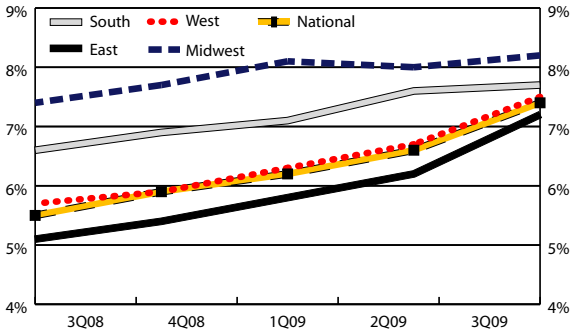
National Transaction Breakdown				
Current Quarter Rates (07/01/09 - 09/30/09)				
	Office	Industrial	Retail	Apartment
< \$2 Million				
Volume (Mil)	\$349	\$608	\$623	\$265
Size Weighted Avg. (\$ per sf/unit)	\$88	\$50	\$88	\$45,427
Price Weighted Avg. (\$ per sf/unit)	\$121	\$79	\$132	\$71,723
Median (\$ per sf/unit)	\$91	\$58	\$89	\$50,000
\$2 - \$5 Million				
Volume (Mil)	\$498	\$630	\$695	\$502
Size Weighted Avg. (\$ per sf/unit)	\$129	\$56	\$143	\$57,292
Price Weighted Avg. (\$ per sf/unit)	\$210	\$93	\$237	\$108,451
Median (\$ per sf/unit)	\$182	\$75	\$202	\$85,683
> \$5 Million				
Volume (Mil)	\$4,168	\$1,242	\$3,785	\$2,735
Size Weighted Avg. (\$ per sf/unit)	\$215	\$58	\$148	\$84,009
Price Weighted Avg. (\$ per sf/unit)	\$363	\$102	\$244	\$176,097
Median (\$ per sf/unit)	\$211	\$76	\$154	\$76,709
All Transactions				
Volume (Mil)	\$5,016	\$2,480	\$5,104	\$3,502
Size Weighted Avg. (\$ per sf/unit)	\$184	\$55	\$136	\$74,269
Price Weighted Avg. (\$ per sf/unit)	\$331	\$94	\$229	\$158,497
Median (\$ per sf/unit)	\$119	\$64	\$123	\$64,566

Source: RERC.

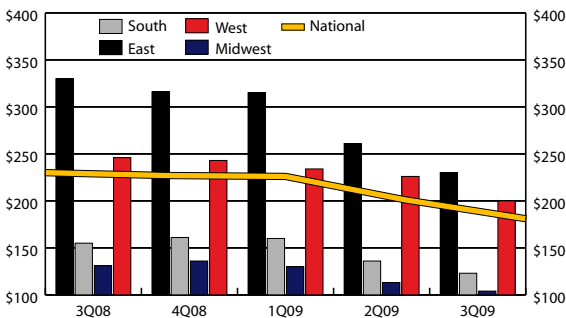
Capitalization Rates (All Transactions)				
	Office	Industrial	Retail	Apartment
12-Month Trailing Averages (10/01/08 - 09/30/09)				
Range (%)	4.1 - 11.6	5.5 - 13.1	4.7 - 13.3	3.4 - 12.8
Weighted Avg. (%)	7.4	8.1	7.3	6.7
Median (%)	7.6	8.0	7.3	6.7
Current Quarter Rates (07/01/09 - 09/30/09)				
Range (%)	6.0 - 11.6	6.7 - 13.1	4.7 - 13.3	4.0 - 10.6
Weighted Avg. (%)	8.1	9.2	7.4	7.1
Median (%)	8.5	8.6	7.4	6.7

Source: RERC.

**RERC Weighted Average Capitalization Rate
(12-Month Trailing Average)**



**RERC Size-Weighted Average PPSF
(12-Month Trailing Average)**



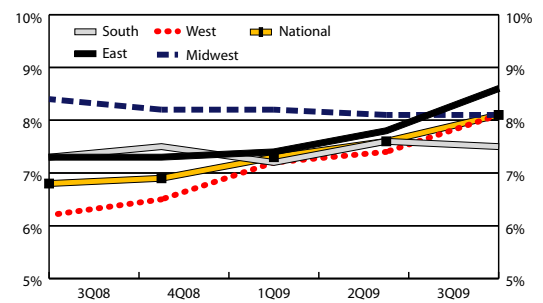
Office:

- The office market continues to suffer as job losses mount and demand for office space continues to fall. Reasons for this decline include eroding fundamentals, excess supply, and continuing high unemployment.
- According to CBRE Econometric Advisors (formerly Torto Wheaton Research), the office vacancy rate increased to 16.1 percent during third quarter 2009. The vacancy rate has increased 360 basis points since its peak 3 years ago, and is projected to continue to increase throughout 2010.
- Office transaction volume and prices continued to decline during third quarter 2009, according to RERC's 12-month trailing transaction analysis. The 12-month trailing volume declined almost 25 percent, and the 12-month trailing weighted average and median capitalization rates increased to 7.4 percent and 7.6 percent, respectively. However, current quarter data showed increases in both volume and price.
- Weighted average 12-month trailing capitalization rates for the office sector have risen steadily during the past year, while the 12-month trailing size-weighted average price has been declining.

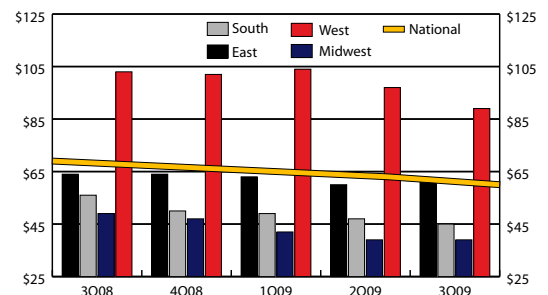
Industrial:

- Manufacturing activity has seen steady to moderate improvement in recent months. Although the industrial economy is moving towards stabilization, it will take the industrial property sector through 2010 to start to stabilize.
- The availability rate for the industrial property sector increased to 13.5 percent during third quarter 2009. This is the eighth consecutive increase in the availability rate, and is the highest that this rate has been since CBRE Econometric Advisors (formerly Torto Wheaton Research) began tracking it in 1989.
- Prices continued to decline and capitalization rates increased for the industrial sector during third quarter 2009 on both a 12-month trailing and current quarter basis. The 12-month trailing volume declined by more than 25 percent compared to the previous quarter.
- The 12-month trailing size-weighted average price per square foot of industrial space declined significantly in the West and Midwest regions since first quarter 2009, while the decline in the other regions has been more gradual.

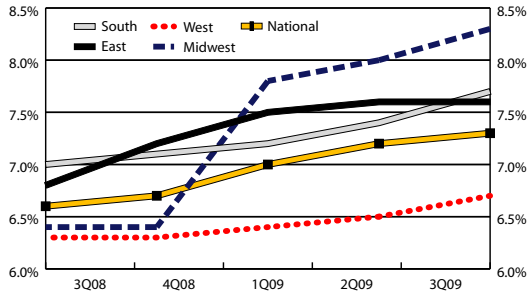
**RERC Weighted Average Capitalization Rate
(12-Month Trailing Average)**



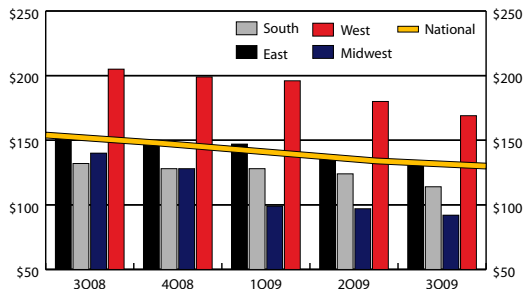
**RERC Size-Weighted Average PPSF
(12-Month Trailing Average)**



RERC Weighted Average Capitalization Rate (12-Month Trailing Average)



RERC Size-Weighted Average PPSF (12-Month Trailing Average)



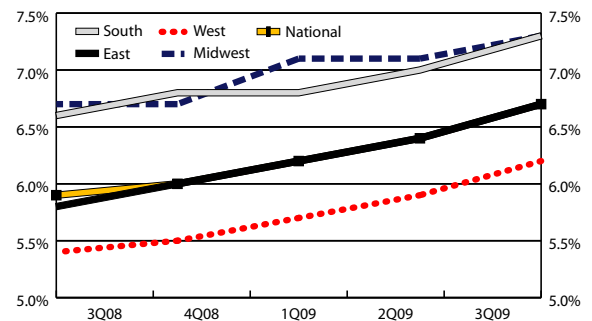
Retail:

- Due to weak consumer spending, still-high job losses, and low consumer confidence, the retail availability rate is expected to increase while average rent is predicted to fall in 2010. The second quarter 2009 availability rate for the retail sector increased to 11.7 percent, according to CBRE Econometric Advisors (formerly Torto Wheaton Research). The retail availability rate has been rising since 2006, and is the highest it has been since Torto Wheaton Research began tracking it in 1989.
- RERC's current quarter transaction analysis shows that the retail market may be starting to stabilize, while the 12-month trailing data continued to show lower prices and increasing capitalization rates. In addition, 12-month trailing volume declined in third quarter 2009, but did increase for the current quarter.
- The 12-month trailing weighted average capitalization rates increased over the past year in the West, South, and Midwest regions, while this rate leveled off in the East region. The national 12-month trailing weighted average capitalization rate has climbed steadily over the past year, with the largest increase from fourth quarter 2008 to first quarter 2009.

Apartment:

- Families who have lost their homes have helped keep the apartment sector afloat, and as such, the apartment market is expected to be the first property type to recover, despite the delay caused by high unemployment. The vacancy rate for the apartment sector increased by 10 basis points to 7.8 percent during third quarter 2009, according to Reis, Inc. The vacancy rate is expected to peak in 2010 at a yearly rate of 8.3 percent.
- RERC's 12-month trailing volume for the apartment sector declined more than 30 percent from the previous quarter, while the current quarter volume increased slightly. The 12-month trailing price per unit decreased from the previous quarter. The 12-month trailing weighted average and median capitalization rates increased by 40 basis points and 20 basis points, respectively.
- The 12-month trailing weighted average capitalization rate consistently increased over the past year. According to RERC's size-weighted average price per unit data, the apartment sector has experienced steady to slightly declining prices over the past year, with the steepest decline during third quarter 2009.

RERC Weighted Average Capitalization Rate (12-Month Trailing Average)



RERC Size-Weighted Average PPU (12-Month Trailing Average)

