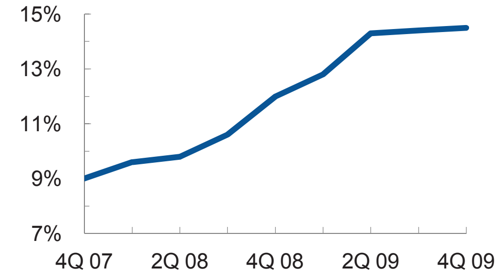
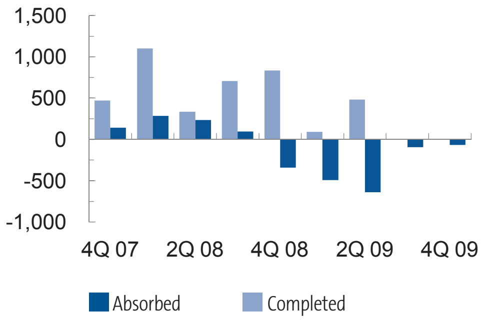
# Industrial Trends Report—Fourth Quarter 2009
**Austin, TX**

GRUBB & ELLIS.
From Insight to Results

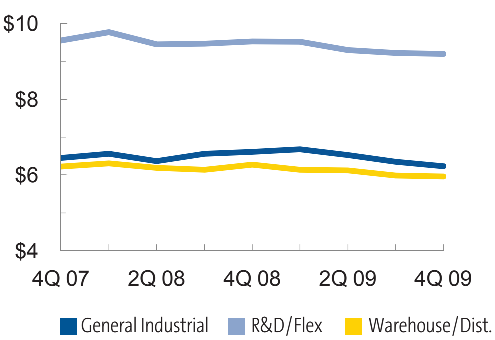
**Vacancy Rate**
Quarterly




**Completions vs. Absorption**
Quarterly (in Thousands of SF)




**Asking Rental Rates**
Quarterly ($/SF/Yr./Triple Net)




## Industrial Vacancy Inches Higher But Is Expected to Stabilize in 2010

Austin's industrial leasing market ended a challenging year by posting 68,000 square feet of red ink, bringing the annual net absorption totally to nearly 1.3 million square feet. This marked the fifth consecutive quarter the market has witnessed negative demand as the contraction among tenants has lead to the largest annual absorption loss since 2002. The warehouse/distribution sector was most affected by tenant move outs resulting in 61,000 square feet of negative absorption as the yearly total sank to 741,000 square feet. Although standard industrial and R&D/flex properties posted minimal space losses during the quarter, both sectors still ended the year with 243,500 and 311,500 square feet of negative absorption, respectively. Overall vacancy inched slightly higher during the final quarter, rising by 10 basis points to 14.5 percent to reach its highest level recorded in over six years. A large portion of this space lies within the warehouse/distribution sector - resulting from the slowdown in retail, manufacturing and trade cutting into demand, as well as the delivery of new supply - which has pushed vacancy rates to its highest level this decade.

Although Austin's industrial market fundamentals have weakened as a result of corporate consolidations and excess space deliveries, there are encouraging signs that the market has begun to stabilize. The diminished volume of negative absorption, following a surge in vacancies early in 2009, may indicate that many industrial users have completed their consolidations. Nationally, many economic indicators suggest that the recession has ended. Locally, there are companies such as Avant Technology, Electronic Arts, Inc. and Directed Manufacturing Inc. (to name a few), that have begun to make business decisions, resulting in an uptick in leasing activity. While the speculative construction pipeline has emptied out, the market should benefit by providing an opportunity for leasing activity to chip away at vacancy in the year ahead.

### FORECAST

- New construction will be limited to build-to-suit development until excess space is absorbed and lending restrictions ease.
- Landlords will remain aggressive in lease negotiations by offering more concessions in order to drive tenant demand.
- Small owner/user sales will dominate the market, but the number of properties on the market will far outpace available buyers.
- According to IHS Global Insight, Austin will return to pre-recession job levels in 2010, which bodes well for the local industrial leasing market.

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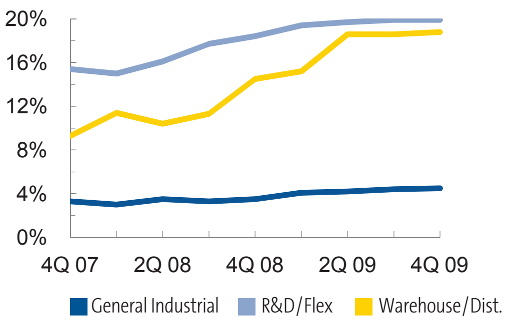
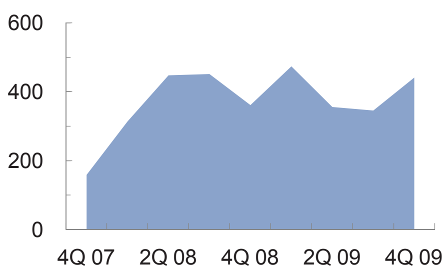
### Vacancy Rate
Quarterly




### Sublease Available
Quarterly (in Thousands of SF)




## MARKET OVERVIEW

Austin's industrial market was hit hard this past year with nearly 1.3 million square feet of negative net absorption, which caused the citywide vacancy to increase by 250 basis points to 14.5 percent. The warehouse/distribution sector largely contributed to dramatic annual increase as vacancy jumped 430 basis points to 18.8 percent. The combination of construction deliveries and negative absorption caused the vacancy rate to increase to its highest level this decade. However, there are encouraging signs that this sector is stabilizing as vacancy only inched up 20 basis points since the first quarter of 2009. The R&D/flex sector was also hit with recent consolidations, which has caused vacancy to increase by 150 basis points to 19.9 percent within the past year to remain the highest among all property types. With a vacancy rate of 4.5 percent, general industrial properties are by far the strongest in the city, but this property type has also seen vacancy rise by 100 basis points within the past year.

During the final quarter, the Far Northwest submarket posted the largest occupancy loss with 69,122 square feet of red ink, driving the annual total into negative territory with 49,122 square feet. The quarterly space loss within the submarket occurred as PharmaForm LLC moved out of 69,872 square feet of R&D/flex space at 9825 Spectrum. The Northwest submarket also registered 28,364 square feet of negative absorption as the annual tally declined to 24,411 square feet of positive absorption. The largest space loss occurred as Kodiak Assembly moved out of 28,364 square feet of standard industrial space in Northwest Techniplex – McNeil 6. The Round Rock submarket also recorded 28,319 square feet of negative net absorption, driving the annual total deeper into the red at 103,117 square feet.

The hardest hit submarket for the year remained the North with nearly 523,000 square feet of negative absorption. However, there are signs that the submarket may be stabilizing with less than 1,400 square feet of negative absorption during the final quarter. The diminished volume of negative absorption following a surge in vacancies early in 2009 indicates that many industrial users may have completed their consolidations. Although the North submarket continued to experience some consolidations, there was a flurry of leasing activity which countered the quarterly losses. The most notable occupancy gains occurred as DHL took down 36,333 square feet of R&D/flex space at 2631 Kramer Lane and U.S. Screen Corp. moved into a single-story, 22,206-square-foot manufacturing facility located at 2105 Denton Dr. In addition, Electronic Arts Inc. has signed a lease for 50,000 square feet in the Domain 2, which was previously occupied by Midway Games Inc. until late in 2008. Electronic Arts, which already has a presence in Austin through its BioWare studio and Pogo.com group, will move into the Domain in early 2010.

During the final quarter, the Far Northeast submarket recorded 50,400 square feet of

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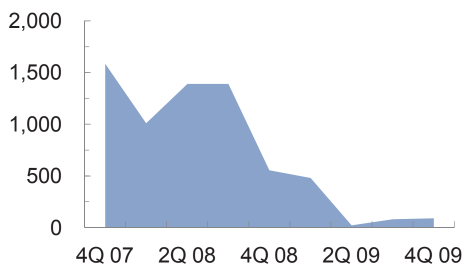
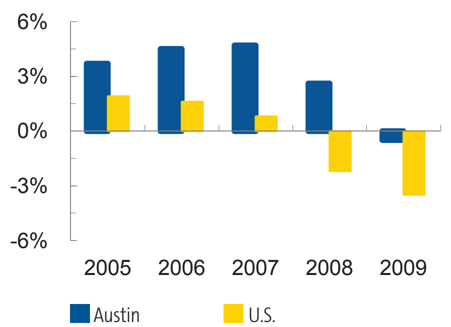
**Industrial Space Under Construction**
Quarterly (in Thousands of SF)




**Employment Growth**
Last Five Years




Source: U.S. Bureau of Labor Statistics

growth as Avant Technology moved into approximately 50,000 square feet of warehouse space at Verde Springbrook Corporate Center. Also making headlines, a California manufacturer recently moved its headquarters from San Diego to Pflugerville, with plans to continue its manufacturing in Central Texas while expanding the business here. Directed Manufacturing Inc., a subsidiary of Carslbad, California-based Forecast 3D, also leased 10,659 square feet at Wells Point One. The company has about 10 employees and plans to grow to about 40 workers as well as expand into about 25,000 square feet within five years.

Negative absorption and rising vacancy rates continued to have a negative impact on rents as the citywide average fell to its lowest level in three years. Overall asking rents decreased by $0.02 to $7.08 NNN during the final quarter. The largest drop in rents during the quarter occurred in standard industrial properties, which fell by $0.12 to $6.23 NNN. Following suit, warehouse/distribution rents decreased by $0.03 to $5.96 NNN while R&D/flex asking rents slipped by $0.02 to $9.20 NNN. Higher tenant improvement allowances, free rent and effective rents that are dramatically lower than asking rents have become more common as landlords aggressively compete to attract scarce tenants. Some landlords are finding themselves in a precarious position of needing to maintain rental rates to satisfy their proformas while competing to lure in tenants into their new projects. In the year ahead, expect asking rents to further subside while tenant demand remains sluggish resulting from a slow economic recovery.

Construction activity has virtually vanished as the tightened credit market and lack of demand has shelved any speculative development until the market recovers. Only 91,805 square feet remain in the construction pipeline, which mainly consists of small industrial facilities underway. Over 3.6 million square feet of new industrial space has delivered within the past two years, of which 68 percent remains available. These large spaces can accommodate large relocating businesses looking to reduce their real estate costs.

Landlords will face unique challenges to fill an abundance of vacant space. Those landlords in a position to be aggressive could benefit the most since many companies are now redefining their revenue growth strategies, reorganizing operations, reducing costs and positioning themselves for what many economists project to be a 2010 turnaround for the economy. For tenants looking to renew a lease or expand in the near future, the window of opportunity is wide open to negotiate favorable long-term leases with their landlords. Building owners with little or no debt on their industrial property will have an advantage, as they can afford to reduce their rents in order to attract tenants without taking on added financial risk. Developers with the flexibility to offer owner financing and tenant improvements will have the upper hand in absorbing space, as lending practices have tightened dramatically over the past year.

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| By Submarket | Total SF | Vacant SF | Total Vacancy % | Net Absorption Current | Net Absorption Year To Date | Under Construction SF | Asking Rent WH/Dist | Asking Rent R&D/Flex |
|---|---|---|---|---|---|---|---|---|
| CBD | 708,954 | 7,600 | 1.1% | - | 16,900 | - | - | - |
| Central | 2,811,300 | 221,955 | 7.9% | (17,368) | (62,872) | - | $5.39 | $9.41 |
| East | 5,842,756 | 1,150,636 | 19.7% | 1,501 | (79,125) | - | $6.89 | $9.08 |
| Far Northeast | 1,090,546 | 53,800 | 4.9% | 50,400 | 61,388 | 33,805 | $7.33 | $13.82 |
| Far Northwest | 2,234,305 | 212,759 | 9.5% | (69,122) | (49,122) | - | $8.00 | $11.00 |
| Georgetown | 1,078,625 | 368,354 | 34.2% | - | 55,746 | 58,000 | $4.26 | - |
| North | 16,982,852 | 2,727,335 | 16.1% | (1,365) | (522,926) | - | $5.85 | $9.69 |
| Northeast | 11,394,638 | 1,685,586 | 14.8% | (22,102) | (370,375) | - | $6.18 | $7.64 |
| Northwest | 4,878,433 | 204,040 | 4.2% | (28,364) | 24,411 | - | $6.49 | $10.55 |
| Round Rock | 5,565,002 | 1,213,548 | 21.8% | (28,319) | (103,117) | - | $6.55 | $10.72 |
| South | 4,000,973 | 234,048 | 5.8% | 30,254 | (29,322) | - | $6.75 | $6.02 |
| Southeast | 13,033,317 | 2,445,045 | 18.8% | 8,529 | (227,160) | - | $5.98 | $8.79 |
| Southwest | 3,215,486 | 28,258 | 0.9% | 7,800 | (10,458) | - | $9.90 | $13.20 |
| West Central | 100,512 | 17,067 | 17.0% | - | - | - | - | $10.00 |
| **Totals** | **72,937,699** | **10,570,031** | **14.5%** | **(68,156)** | **(1,296,032)** | **91,805** | **$5.96** | **$9.20** |

| By Property Type | Total SF | Vacant SF | Total Vacancy % | Net Absorption Current | Net Absorption Year To Date | Under Construction SF | Asking Rent |
|---|---|---|---|---|---|---|---|
| General Industrial | 23,613,668 | 1,052,746 | 4.5% | (3,408) | (243,607) | 58,000 | $6.23 |
| R&D/Flex | 20,991,761 | 4,180,458 | 19.9% | (3,909) | (311,294) | 23,805 | $9.20 |
| Warehouse/Distribution | 28,332,270 | 5,336,827 | 18.8% | (60,839) | (741,131) | 10,000 | $5.96 |
| **Totals** | **72,937,699** | **10,570,031** | **14.5%** | **(68,156)** | **(1,296,032)** | **91,805** | **$7.08** |

## Grubb & Ellis—Austin


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## INDUSTRIAL TERMS AND DEFINITIONS

**Inventory:** Industrial inventory includes all multi-tenant, single tenant and owner occupied buildings at least 10,000 square feet.

**Industrial Buildings Classifications:** Industrial buildings are categorized as warehouse/distribution, general industrial, R&D/flex and incubator based on their physical characteristics including percent office build-out, clear height, typical bay depth, typical suite size, type of loading and typical uses.

**Vacancy and Availability:** The vacancy rate is the amount of physically vacant space divided by the inventory and includes direct and sublease vacant. The availability rate is the amount of space available for lease divided by the inventory.

**Net Absorption:** The net change in physically occupied space over a period of time.

**Asking Rent:** The dollar amount asked by landlords for available space expressed in dollars per square foot per year in most parts of the country, and dollars per square foot per month in areas of California and selected other markets. Industrial rents are expressed as triple net where all costs including, but not limited to, real estate taxes, insurance and common area maintenance are borne by the tenant on a pro rata basis. The asking rent for each building in the market is weighed by the amount of available space in the building.

** Grubb & Ellis statistics are audited annually and may result in revisions to previously reported quarterly and final year-end figures.*