Industrial Trends Report—Second Quarter 2010
Austin, TX

GRUBB & ELLIS.
From Insight to Results

Demand Counters Consolidations

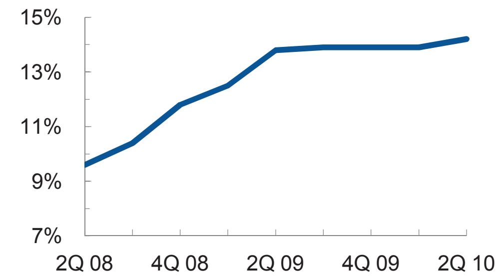
Austin's industrial leasing market took a step back during the second quarter by posting 46,058 square feet of negative net absorption, marking the sixth time during the last nine quarters to witness negative growth. The majority of the quarterly space losses occurred in the R&D/flex sector with 155,199 square feet of red ink. The largest occupancy loss resulted from Applied Materials' decision to place nearly 600,000 square feet on the market for sale or lease, which is more than a third of their 1.6-million-square-foot Northeast Austin industrial campus. The company has initially moved out of 244,797 square feet with plans occupy the remaining 349,000 square feet until sometime next year. The warehouse/distribution sector also witnessed sluggish demand by positing 24,740 square feet of negative absorption as vacancy has climbed to a 20-year high. On the flip side, general industrial or manufacturing properties experienced an uptick in demand with 133,881 square feet of absorption growth.

Despite the quarterly space loss, positive signs in the leasing market have emerged indicating that fundamentals will likely stabilize by year-end, rather than deteriorate further. Recent leases by Ultra Electronics Advanced Tactical Systems Inc., Blizzard Entertainment, Formaspace Technical Furniture, Excel Directional, and several other smaller firms have contributed to a 14 percent increase in total square feet leased during the first-half of 2010, compared to the previous year. Although leasing activity has not been sufficient to offset the space that has become available during the same period, the uptick in demand indicates that the market is on a path to recovery. While it is evident that leasing fundamentals have improved since last year, the market is far from making a complete turnaround. Presently, there is roughly over 10 million square feet of industrial space sitting dark across the city holding vacancy at a lofty 14.2 percent. Even though leasing velocity is expected to gradually increase in the coming quarters, it will take several years until the vacancy rate returns to equilibrium.

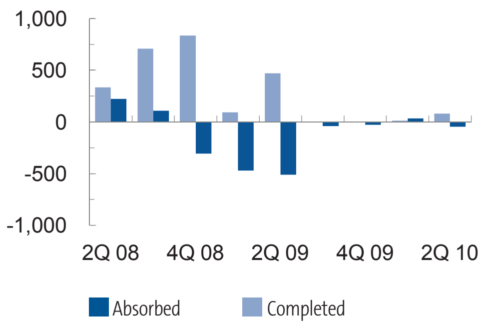
FORECAST

- Tenants will continue to take advantage of early renewal packages, including free rent and reduced overall occupancy costs.
- With no projects in the pipeline, 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 in order to drive tenant demand.
- According to Angelou Economics, Austin's economy will experience mild job growth in 2010 before returning to form in 2011, with employment increasing by 9,200 and 17,100, respectively.

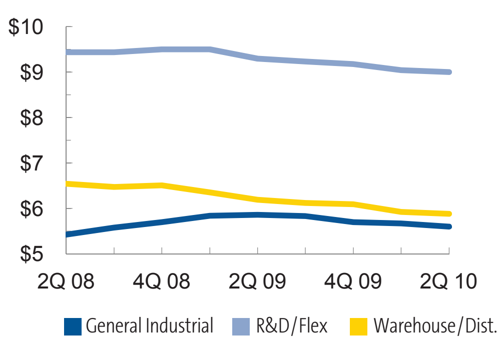
Vacancy Rate



Completions vs. Absorption
(in Thousands of SF)



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



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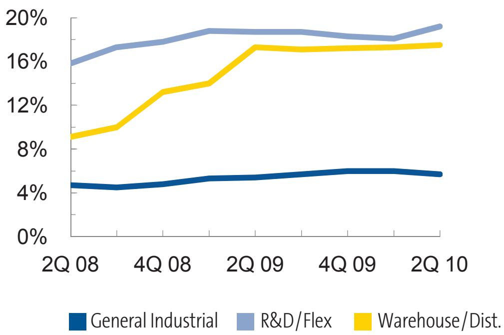
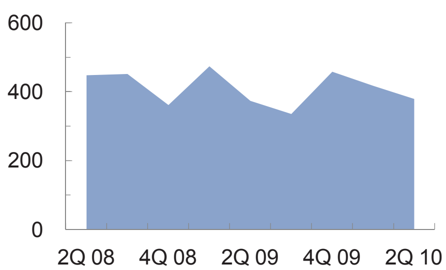


Sublease Available
(in Thousands of SF)



MARKET OVERVIEW

The Northeast submarket was hardest hit during the quarter with 115,682 square feet of red ink causing vacancy to increase by 160 basis points to 16.2 percent. The bulk of the space losses occurred in the R&D/flex market with 222,998 square feet of negative absorption as Applied Materials dumped nearly 600,000 square feet on the market for sale or lease, which is more than a third of their 1.6-million-square-foot Northeast Austin industrial campus. The 600,000 square feet is the largest contiguous block of space available in the city, well-suited for a variety of industry groups such as high-tech companies, educational institutions and large corporate users. The two available buildings include about 49,000 square feet of manufacturing space, 184,000 square feet of office/flex space, an 11,800-square-foot cafeteria and about 92,000 square feet of mechanical mezzanine capacity. Applied Materials has initially vacated only 244,797 square feet of the 593,349 square feet being marketed. The company vacated Building 30 and plans to occupy the remaining 348,552 square feet in Building 36 until mid-2011.

Despite the significant hit, the Northeast submarket still witnessed some positive movement. Formaspace Technical Furniture inked a lease for 56,700 square feet at Harris Ridge Business Center - Building 4. The deal enables Formaspace, which makes custom workbenches, worktables and laboratory furniture, to add both new employees and equipment – and take advantage of a unique taxing designation created for manufacturers. The company relocated from approximately 30,000 square feet in Hutto to Harris Ridge Business Center in June. Another sizeable deal to counter the recent losses included Trans Pak finally taking occupancy of 55,379 square feet of warehouse space at Tech Ridge – Building 4.1, after signing their lease late in 2009.

Even with overall negative growth witnessed during the quarter, several submarkets still managed to post positive growth. Leading the way, the Georgetown submarket recorded 77,254 square feet of black ink, which was mainly a result of AirBorn, Inc opening their new 58,000-square-foot manufacturing facility. The manufacturer relocated from their former location on Royal Drive in Georgetown. The new LEED-certified facility is twice the size of the former plant, allowing for expansion of the growing company, which employs about 400 people. The Far Northwest also experienced growth with 70.225 square feet of positive absorption. The submarket's largest transaction involved Blizzard Entertainment occupying a 65,365-square-foot flex building in Davis Springs Corporate Center - Building 1, located at 9825 Spectrum Drive.

Although the North submarket experienced a slight absorption loss of 8,090 square feet, the submarket's general industrial sector managed to post 30,532 square feet of positive net absorption. The largest occupancy gain involved Excel Directional taking down 32,500 square feet at North Austin Business Park, located at 2106 Denton Drive. Other recent lease transactions worth mentioning involved UT occupying 32,400 square feet of warehouse space at McKalla 1 and Impact Floors taking down 18,385 square feet of flex space at 11700 Stonehollow Drive. However, the submarket's warehouse/distribution

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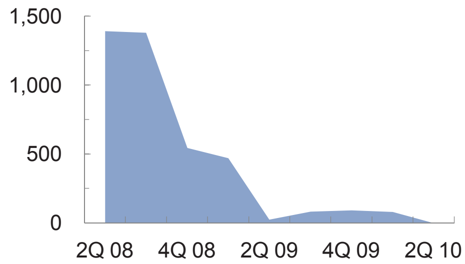
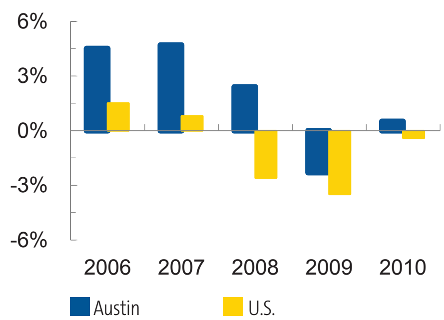
Industrial Space Under Construction
(in Thousands of SF)



Employment Growth
% Change From Same Period Last Year



Source: U.S. Bureau of Labor Statistics

sector posted the largest loss to counter these gains as SabeRex left behind 67,147 square feet at North Austin Business Park and consolidated their operation on Technology Blvd.

Austin's overall vacancy rose by 30 basis points to 14.2 percent to end the quarter. However, the deterioration has moderated as vacancy has only increased by 40 basis points within the past year. R&D/flex properties experienced the largest quarterly increase in vacancy as it jumped 110 basis points to 19.2 percent, the highest vacancy among all categories. Following suit, warehouse/distribution properties witnessed a 20-basis-point jump to 17.5 percent, reaching its highest level in 20 years. Meanwhile, standard industrial vacancy moved downward by 30 basis points to 5.7 percent and remains the lowest among all property types. The good news is that the construction pipeline has emptied out and is expected to remain dormant for a few years, which will allow the market to regain traction and allow vacancy to return to equilibrium.

Although the leasing market has improved since last year, elevated vacancy rates are still the blight of asking rents as landlords are forced to lower their quoted rents in order to attract tenants. The elevated vacancy rates continue to have a negative impact on rents as the citywide average has fallen to its lowest level in three years. The largest reduction in rents during the second quarter occurred in general industrial or manufacturing product, declining $0.07 to $5.60 per square foot. Following suit, the R&D/flex and warehouse/distribution sector saw rents each decline by $0.04 to $9.00 and $5.88 per square foot, respectively.

On the investment side, the first major industrial acquisition since 2008 occurred as PS Business Parks Inc. paid $42.9 million in cash for a 704,000-square-foot portfolio. The deal includes three business parks with multi-tenant flex space in 13 separate single-story buildings. The portfolio was 88 percent leased at time of sale.

Austin industrial tenants are finding themselves in the friendliest leasing climate since the previous downturn with lower contract rents, tenant improvement allowances and concession packages offered by landlords to tenants willing to commit. Looking forward, whether rents continue to decline or simply stabilize, will depend upon how soon the manufacturing and technology sector recovers. 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. As the local industrial leasing market progresses toward recovery, however, the window of opportunity for tenants will begin to close. Therefore, tenants are advised to act within the next 12 months. The challenge for landlords will be holding rents steady through times of sluggish demand. While landlords must take the necessary steps to remain competitive in the present market, they are well advised to remember that improved leasing conditions will soon come to Central Texas. With that in mind, some landlords will abstain from short-term leases tying up their facilities during the wave of returning demand and instead hold out for tenants looking for a long-term home.

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By Submarket	Total SF	Vacant SF	Vacancy %	Net Absorption Current Qtr	Net Absorption Year To Date	Under Construction SF	Asking Rent WH/Dist	Asking Rent R&D/Flex
CBD	439,183	41,844	9.5%	-	(3,700)	-	-	-
Central	2,492,768	176,617	7.1%	(14,005)	(8,661)	-	$5.34	$10.34
East	5,832,256	1,193,097	20.5%	(34,955)	(34,961)	-	$6.22	$9.29
Far Northeast	1,134,851	39,100	3.4%	12,105	28,005	-	$7.20	$10.27
Far Northwest	2,260,877	139,752	6.2%	70,225	73,007	-	$7.96	$11.00
Georgetown	1,136,625	342,307	30.1%	77,254	77,254	-	-	-
North	17,011,998	2,467,150	14.5%	(8,090)	60,075	-	$5.70	$9.71
Northeast	12,086,208	1,957,308	16.2%	(115,682)	(197,159)	-	$6.27	$6.98
Northwest	4,798,439	212,534	4.4%	(41,640)	(19,026)	-	$5.34	$9.82
Round Rock	5,779,466	1,201,343	20.8%	12,334	42,325	-	$6.66	$10.43
South	3,999,773	230,314	5.8%	7,097	13,234	-	$6.08	$7.80
Southeast	13,216,123	2,388,284	18.1%	(27,168)	(61,365)	-	$5.42	$8.53
Southwest	3,215,486	25,858	0.8%	(600)	2,400	-	$9.95	$13.20
West Central	100,512	-	-	17,067	17,067	-	-	-
Totals	**73,504,565**	**10,415,508**	**14.2%**	**(46,058)**	**(11,505)**	**-**	**$5.88**	**$9.00**

By Property Type	Total SF	Vacant SF	Vacancy %	Current Qtr	Year To Date	Under Construction SF	Asking Rent
General Industrial	23,712,416	1,349,032	5.7%	133,881	132,528	-	$5.60
R&D/Flex	21,507,021	4,127,564	19.2%	(155,199)	(96,470)	-	$9.00
Warehouse/Distribution	28,285,128	4,938,912	17.5%	(24,740)	(47,563)	-	$5.88
Totals	**73,504,565**	**10,415,508**	**14.2%**	**(46,058)**	**(11,505)**	**-**	**$6.84**

Grubb & Ellis—Austin Industrial Professionals

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INDUSTRIAL TERMS AND DEFINITIONS

Total SF: Industrial inventory includes all multi-tenant, single tenant and owner occupied buildings at least 20,000 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.*