

Industrial Market Trends Philadelphia

Grubb & Ellis Research
Fourth Quarter 2008



Fundamentals Still Strong; Future Uncertain

Executive Summary

Overall, the greater Philadelphia industrial market posted another positive year of activity and growth. Net absorption was positive, posting 8.8 million square feet at year-end. Vacancy rose for the sixth straight quarter as added supply outpaced demand. Current vacancy rests at 9.1 percent, up 48 basis points since the end of 2007. Current construction is 0.4 percent of the inventory, which is down from 1.2 percent at its last peak during the fourth quarter of 2007. Construction slowed almost in lock-step to softening demand as the year progressed and average asking rents moved sideways during the year, ending at a triple net rate of \$4.83 per square foot per year.

A negative economic outlook resulted in a shift in construction from speculative developments to build-to-suit or owner-built projects. Currently, less than 41 percent of construction is on a speculative basis as opposed to over 75 percent at the end of last year. This trend is likely to continue until the market posts a few consecutive quarters of decreased vacancy, which is not expected until the beginning of 2010.

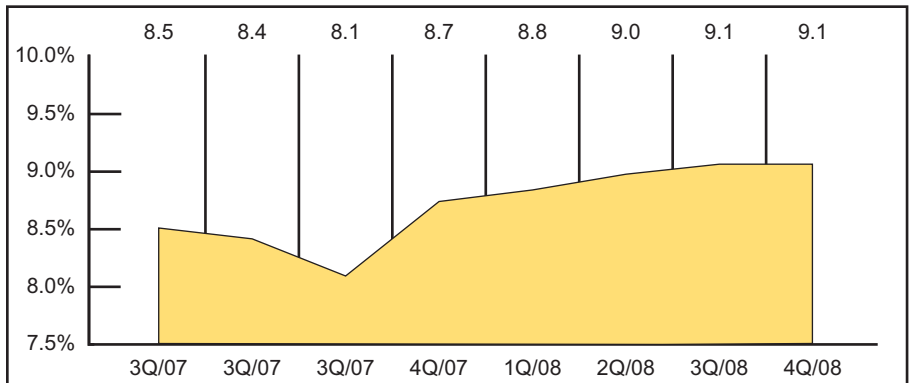
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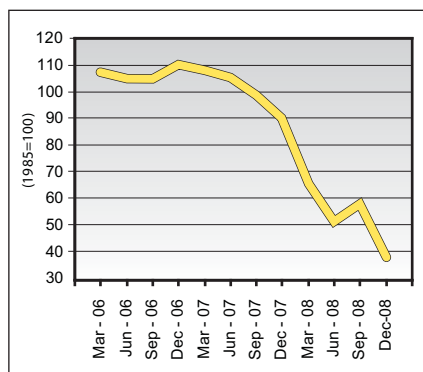


Industrial Vacancy Rate*

* All Property Types

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... sublease space, often an early indicator of future vacancy, has not shown any appreciable increase over the past four quarters.



Consumer Confidence Index
Source: Conference Board

Market Overview

Northeastern and Central PA

All product types enjoyed a year of positive net absorption in the I-81/I-78 Corridor as 2.4 million square feet of available space has been occupied during the last three months and more than 8 million over the past twelve months. In the context of today's onslaught of dire economic news, this is surprisingly the same amount the region tallied in 2007. The vacancy rate has been steadily pushed to 9.9 percent at year end as added product has been outpacing demand since the third quarter of 2007. This past quarter saw the disparity between the two shrink when 1.02 percent of the inventory was absorbed and inventory only grew by 1.05 percent.

The main driver for the lop-sided growth in recent quarters is clearly the area's emergence as a major geographical consideration in many companies' supply chain analyses. As more and more decision makers cast their attention to the Eastern PA markets as a node for their distribution network, developers enjoyed unprecedented demand and deal activity. But, as factory orders have been falling fast and companies are trying quickly to relieve themselves of excess inventories (and personnel), one expects future vacancy to push northward more as a function of stagnant demand rather than overdevelopment.

That being said, sublease space, often an early indicator of future vacancy, has not shown any appreciable increase over the past four quarters. In fact, over 1 million square feet of this discounted space-type was removed from the market in 2008. While this is good news for the present, recent history has shown that market conditions can change in a matter of hours in today's business environment. This sentiment is most likely the reason developers have slowed construction starts this year compared to 2007. Further evidence of risk aversion in today's market is witnessed by the fact that over 45 percent of the construction currently underway is pre-leased and 6 of the 12 major developments underway are on a build-to-suit or owner-built basis.

Year-over-year rent changes were negative across all product types. The slips were modest as the overall asking rent fell \$0.06 to a triple net rate of \$4.36 per square foot per year. Rental rate increases have always been tempered by the abundance of developable land along the major interstates. But downward pressure is most likely a result of less desirable spaces remaining on the market. High quality logistic-type product has been enjoying the majority of activity in this market in recent past as it's vacancy rate has slowly declined since the end of last year. Lower-end quality product naturally fetches an asking rent at a discount to the premium, state-of-the-art distribution centers.

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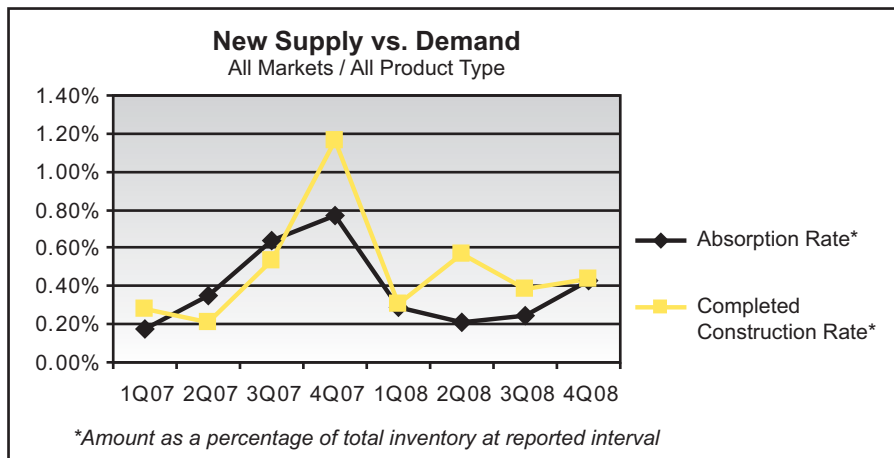
Philadelphia and Suburbs

Overall, demand held-up throughout 2008 in Philadelphia and its surrounding suburbs as over 800,000 square feet of net positive absorption was totaled for the year. Comparatively, though, activity is off 83 percent since last year when over 4.3 million square feet of available space was occupied. The biggest change was in manufacturing space which suffered a retraction, putting 857,404 square feet of space back on the market. This came as no surprise on the heels of news that manufacturing has been undergoing major contraction across the globe on a scale not seen since the thirties. But as an unforeseen and troubling indicator, the R&D/flex sector has seen a steady weakening in demand since its peak in the third quarter of 2007 when 1.45 percent of the then existing inventory was absorbed. The last quarter of 2008 bore witness to the first quarter of negative net absorption for this sector since early 2007.

Future vacancy rates for the area are projected to push upward precipitated by a combination of future product delivering and demand lagging.

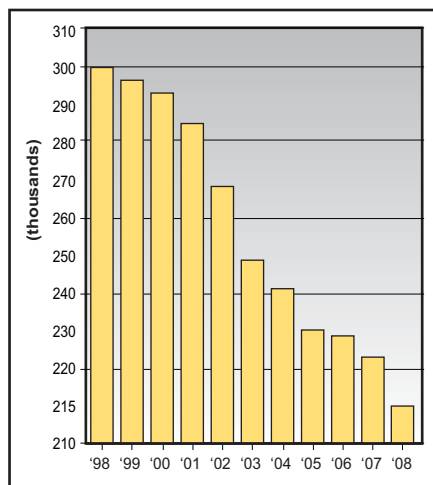
Future vacancy rates for the area are projected to push upward precipitated by a combination of future product delivering and demand lagging. On the supply side, there is over 1 million square feet of new product under construction in contrast to only 466,000 square feet at the beginning of 2007. Current construction set to deliver in a softening market could push the vacancy rate up nearly 20 basis points when completed in the near future.

Year-over-year asking rents appreciated only slightly. As of the end of the fourth quarter 2008, asking rents for all product types averaged a triple net rate of \$5.39 per square foot per year, a \$0.03 increase over last year's average asking rent. The area's more active R&D/flex market actually saw rents depreciate under weakening demand as rents are down \$0.20 since last year and averaging \$8.64 per square foot per year. Rents are expected to stagnate at current levels, or possibly drop, as landlords feel the mounting pressures of a competitive leasing environment.



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While fundamentals have been softening in most markets, it is far too early in the cycle to concede the upper hand to tenants.



**Manufacturing Employment
Philadelphia - Camden
Wilmington MSA**

Source: Bureau of Labor Statistics

Southern New Jersey

The Southern New Jersey industrial market suffered 261,336 square feet of net negative absorption this year as the vacancy rate climbed to 7.7 percent. Construction has acted in kind with only 50,000 square feet of new product underway. The market's dearth of developable land and developers reaction to softening demand will help dampen supply side effects on future vacancy as demand is expected to remain negative to negligible at best over the next few quarters.

Asking rents have pushed downward over the year, dropping \$0.18 since the end of 2007 and currently averaging a triple net rate of \$4.56 per square foot per year. Manufacturing space posted the largest drop over the year while average warehouse/distribution asking rents dipped below \$4.00 per square foot for the first time in years. But this, as was in the I-81/I-78 corridor, is more a symptom of the quality of space available, not the performance of the warehouse distribution sector which was the only to post net positive absorption for the year at 224,740 square feet.

Wilmington

The fourth quarter witnessed the end of a trend of positive demand for three straight quarters having posted negative 45,367 square feet of absorption over the past 90 days. The year-end total settled at 124,983 square feet of net positive absorption. Shielding the area from an overdevelopment scenario, construction is limited to a 26,000-square-foot flex project on River Road. Rents have held up for the year, with average asking rents ending the fourth quarter of 2008 at a triple net rate of \$4.86 per square foot per year. As demand becomes scarce in this market, expect rents to move downward slightly, but avoiding any sharp declines as underlying fundamentals have not suffered any large set-backs over the past 12 months.

Opportunities and Challenges

While fundamentals have been softening in most markets, it is far too early in the cycle to concede the upper hand to tenants. Vacancy is still well below 10 percent, absorption remains positive, construction is slowing and rents have softened overall, at best. That being said, landlords certainly are not tightening their grip on negotiation leverage as future industrial indicators are off in almost all sectors. While it lasts, landlords need not bend too much to sign deals, but know that deal activity will most likely slow considerably by the second to third quarter of 2009.

Industrial Market Trends Fourth Quarter 2008

Forecast

The area has already begun to feel the effects of a contracting manufacturing market after posting its third straight quarter of negative net absorption. The first two quarters of the year will most likely witness the same trend as factory orders have been on a sharp decline since the early part of 2008. What has yet to be seen is the overall economy's effect on warehouse/distribution space. More likely than not, vacancy for this sector will continue its rise, but more a symptom of negative demand rather than oversupply, as companies look to purge inventories in order to free up capital. Asking rents will most likely slide southward, maintaining a trend that began in the latter part of 2008.

Major Transactions

Grubb & Ellis is pleased to announce that it represented the following industrial transactions during the fourth quarter of 2008:

LTS Logistics LLC

Leased 439,088 Square Feet at
1485 West Commerce Drive
Carlisle, PA

Interamerican Motor Corporation

Extended Their
62,400-Square-Foot Lease at
7253 Grayson Road
Harrisburg, PA

Retrievex Acquisition Corp.

Subleased 54,587 Square Feet
at 9230 Ashton Road
Philadelphia, PA

Office Locations



Industrial Market Snapshot Philadelphia Fourth Quarter 2008

By Submarket (All Property Types)	Total (1)	Vacant (2)	Vacant %	Net Absorption		Under Const. (3)	Asking Rent (4)	
	SF	SF		Current Qtr	Year To Date	SF	WH/Dist	R&D/Flex
Berks County	18,177,858	2,881,633	15.9%	(107,948)	(125,871)	-	\$3.21	\$7.07
Bucks County	53,218,592	3,695,514	6.9%	20,001	(104,581)	-	\$4.05	\$9.11
Burlington County	36,564,532	3,159,797	8.6%	85,696	251,101	-	\$3.71	\$8.75
Camden County	33,844,050	1,817,276	5.4%	(21,229)	(179,276)	-	\$3.98	\$5.40
Central PA	143,980,024	12,479,332	8.7%	(168,244)	792,859	2,722,160	\$4.12	\$8.79
Chester County	28,044,133	1,781,138	6.4%	157,329	495,516	-	\$5.33	\$9.99
Delaware County	30,877,642	2,217,832	7.2%	29,813	(173,882)	58,020	\$4.60	\$7.10
Gloucester County	27,063,802	2,555,345	9.4%	106,582	(333,161)	50,000	\$4.06	\$6.65
Lancaster County	37,313,692	1,862,334	5.0%	231,599	(238,311)	145,000	\$3.89	\$5.08
Lehigh Valley	72,023,126	7,409,629	10.3%	1,586,689	3,127,230	1,334,000	\$4.65	\$7.87
Montgomery County	70,642,118	6,883,697	9.7%	(4,493)	635,425	340,600	\$3.82	\$9.70
New Castle County	26,753,159	2,332,978	8.7%	(45,367)	124,983	26,000	\$4.60	\$10.22
Northeastern PA	42,860,090	5,842,376	13.6%	1,245,022	4,201,419	2,076,400	\$3.90	\$4.81
Philadelphia County	100,455,024	10,747,285	10.7%	188,246	368,823	484,736	\$4.73	\$8.55
Totals	721,817,842	65,666,166	9.1%	3,303,696	8,842,274	7,236,916	\$4.19	\$8.36

By Property Type (All Submarkets)

Asking Rent

Property Type	Total SF	Vacant SF	Vacant %	Current Qtr	Year To Date	Under Const. SF	Asking Rent
General Industrial	387,795,658	26,122,082	6.7%	(47,206)	386,698	1,620,500	\$4.70
R&D/Flex	61,740,443	7,319,574	11.9%	79,043	985,469	541,256	\$8.36
Warehouse/Distribution	272,281,741	32,224,510	11.8%	3,271,859	7,470,107	5,075,160	\$4.19
Totals	721,817,842	65,666,166	9.1%	3,303,696	8,842,274	7,236,916	\$4.83

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

Construction Watch

Fourth Quarter 2008

	Speculative Development				Build-to-Suit Development			Owner-Built Development		
	Under Construction	Preleased %	Completed This Qtr	Completed YTD	Under Construction	Completed This Qtr	Completed YTD	Under Construction	Completed This Qtr	Completed YTD
Total	2,914,816	9.0%	1,592,520	6,524,092	2,930,500	1,855,520	5,088,608	1,391,600	251,800	1,283,800

Industrial Market Terms and Definitions

Inventory: Industrial Inventory includes multi-tenant, single tenant and owner-occupied buildings with at least 20,000 sq. ft.

Construction Type: Speculative ("spec") construction is designed to attract tenants likely to be in the market when the project is leasing. Build-to-suit construction is designed for a specific tenant.

Industrial Product Types: 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. 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.

Average Weighted Asking Rent: An average market rent where the asking rent for each building in the market is weighted by the amount of available space in the building.