Marcus & Millichap

Industrial Research REPORT

2005

This report covers the national industrial market and features in-depth coverage of the Atlanta, Chicago, Dallas-Fort Worth, Houston, Riverside-San Bernardino, Los Angeles, Northern New Jersey and South Florida markets.

Executive Summary

- Employment in key industrial sectors is rising. Over the past 12 months, manufacturing employment increased by 25,000 jobs, wholesale trade gained 41,000 positions, and transportation and warehousing expanded by 87,200 jobs.

- Since 2002, annual warehouse construction volumes have been below the historical average of approximately 100 million square feet per year. In 2005, deliveries are expected to fall 26 percent short of this figure, and inventory additions in 2006 will also be moderate, according to early indicators.

- Net absorption of warehouse space is on track to exceed construction in 2005, enabling vacancy to decline at a faster pace.

- Owners are expected to regain some of the pricing power lost since 2000. The average market rent is set to rise 3.1 percent this year, with growth forecast to accelerate further in 2006.

- With abundant liquidity in the investment market, the average cap rate has dropped below 8 percent. To date in 2005, the median price per square foot across all industrial property types is up 4 percent over the 2004 figure.

Industrial Real Estate Market Hits the Accelerator

Sharply improving fundamentals point toward an acceleration in national industrial investment activity over the next year. Both supply and demand indicators turned strongly favorable in the early months of the year, and with new warehouse supply expected to increase total inventory by only 1.3 percent this year, additional improvement is anticipated. In addition, strong import volumes, higher domestic capacity utilization and a 3.9 percent increase in industrial production over the past year indicate greater upward pressure on user requirements for industrial property.

Vacancy Trends Downward, More Improvement Expected by Year End

Vacancy in the warehouse/distribution sector is down 30 basis points to date in 2005 to 9.8 percent. Absorption trends suggest that over the next 12 months, vacancy will continue to drop, falling below the 9 percent mark in the first half of 2006. A sizable amount of new construction over the past few years in major U.S. distribution hubs, particularly markets with port access, has been concentrated in the build-to-suit sector. Many national retailers have opened new distribution centers over the past year to position themselves for future growth. These properties, which range in size from approximately 1.5 million to 2.0 million square feet, have boosted absorption figures in many markets.

Limited Construction, Weak Dollar Support Transportation Hubs

Industrial construction has slowed more than 50 percent from its peak in 2000 when more than 150 million square feet came online. We expect construction to remain modest over the next two years with approximately 75 million square feet delivered per year. Looking forward, the industrial market is poised to post marked improvement given the relatively constrained construction pipeline. We expect demand to strengthen as the weak dollar continues to fuel exports and healthy retail sales support the need for transportation and warehousing of goods. This will be most evident in port cities and transportation hubs, as is illustrated by an expected increase in absorption of more than 80 percent in markets such as Atlanta, Tampa, Seattle and Oakland this year.

2005 Industrial Forecast

2.0 percent increase in total employment	74 million square feet will be completed	90 basis point decrease in vacancy	3.1 percent increase in asking rents	8.0 percent increase in sales prices

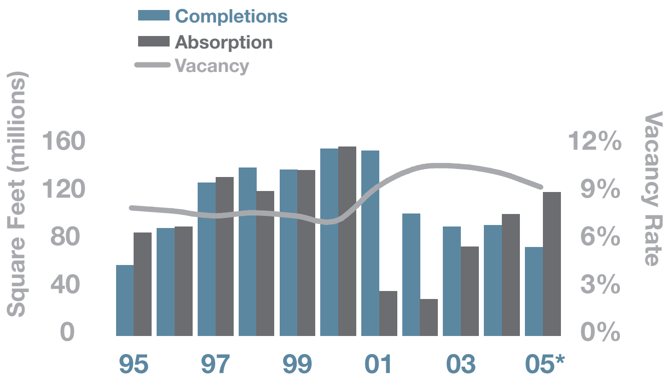
- **Construction Declining.** Warehouse developers are expected to deliver 74 million square feet of space this year, down 20 percent from 2004. Absorption is on pace to post an 18 percent gain.

- **Vacancy Rates Edge Down.** Only a few markets, including Boston and Raleigh, posted increased vacancy over the past year. Decreases of 100 basis points or more were registered over the past 12 months in Las Vegas, Phoenix, Orlando and Nashville, all markets that recorded above-average job growth over the same period.

- **Rent Growth Returns.** Rising prices reflect a positive shift in market fundamentals rather than speculative purchases, as investors have taken note of a 2.9 percent gain in the average rent over the last 12 months.

- **Port Cities Lead.** Over the past year, rent gains have been strongest in port cities, including Baltimore, Miami, West Palm Beach, Tampa and San Diego. In nearly 80 percent of the markets nationwide, however, tenants can still find space at rates below the previous peak.

Industrial Supply and Demand



Sources: Marcus & Millichap Research Services, Property & Portfolio Research

Industrial Overview: All Systems Go for Industrial Market

Industrial market cycles more closely track U.S. GDP than employment growth. This means that fundamental demand for industrial properties is trending upward sooner and more steeply than for employment-driven property types, such as office. Not only is the output of goods and services a better indicator of demand for space than job gains alone, but the warehousing/distribution function is driven by overall consumption, which has been 70 percent of GDP for the past several years. Even the flood of imports, which inhibits GDP growth, has been positive for the industrial property market, as foreign goods pass through the distribution system to final markets.

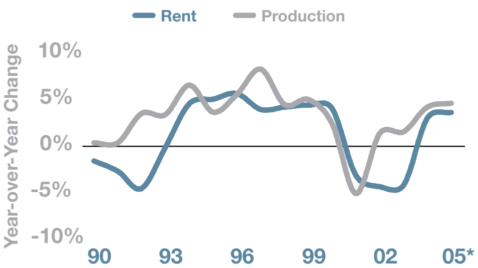
Sublet space has fallen to 5.5 percent of warehouse availabilities, down from 8 percent 24 months ago. Retailing trends carry over into the industrial sector. Some of the largest recent leases were inked by merchants such as Home Depot, Target and Office Depot. Logistics firms, including Maersk, Frontier Logistics and Eagle Global, are also well represented among large tenants taking space this year. While most industrial market indicators are positive, there is growing concern regarding General Motors. The automaker recently reported enormous losses, which will result in significant cutbacks. This will undoubtedly have a trickle-down effect on supporting entities, such as suppliers and distributors, which occupy millions of square feet of warehouse space. Near-term risk is concentrated in ancillary businesses clustered around manufacturing plants where underselling vehicles are produced.

- **Construction Forecast:** Development levels are expected to remain below net absorption for at least another year. Some speculative construction is under way, but the steady stream of build-to-suit projects has slowed as many national distribution tenants have already developed the large hubs needed for near-term growth.

- **Vacancy Forecast:** Nationwide, warehouse vacancy is forecast to decline to 9.2 percent by year-end 2005. Improvement could surprise on the upside over the next few years if economic growth exceeds expectations and positive momentum is sustained into 2006.

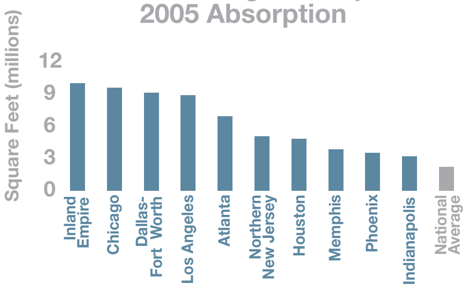
- **Asking Rent Forecast:** Asking rates are forecast to rise 3.1 percent this year, though we expect a wide gap in terms of growth rates by market. Many Midwestern markets will register minimal to no rent growth, while coastal markets will continue to outperform.

Industrial Rent and Industrial Production



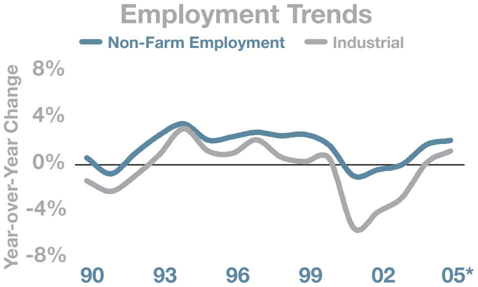
Sources: Marcus & Millichap Research Services, Economy.com, PPR

Markets with Highest Expected 2005 Absorption



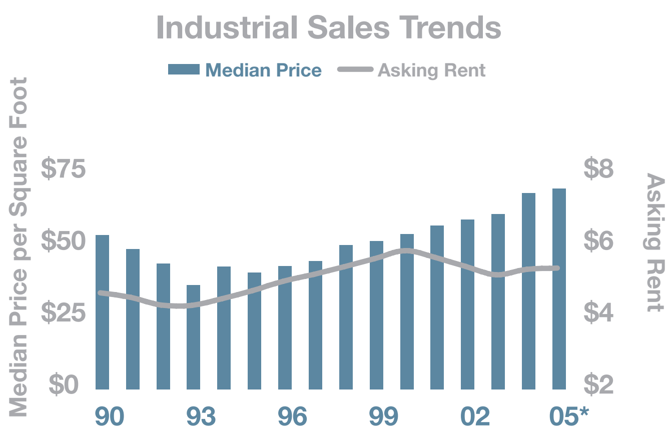
Sources: Marcus & Millichap Research Services, Property & Portfolio Research

Employment Trends



Sources: Marcus & Millichap Research Services, Economy.com, Reis

* Forecast



* 1H 05 Estimate
Sources: Marcus & Millichap Research Services, CoStar Group, Inc., NREI

▲ **Industrial Investment on the Rise.** As the economic recovery gained traction over the last year, institutions and REITs more than doubled investment in the industrial property sector.

■ **Smaller Deals Account for Largest Share.** In spite of increased institutional and REIT activity, the less-than-$5 million segment of the market accounts for approximately 90 percent of all transactions and nearly 50 percent of total dollar volume.

▼ **Private Local Investment Slows.** Local private investment in the $5 million and greater range declined 14 percent over the past year. Buyers in this segment are focusing on location over occupancy, with activity heaviest in major coastal metros such as Los Angeles, Orange County, Northern New Jersey and Boston.

▲ **Cap Rates Dip.** Cap rates to date in 2005 average 7.9 percent, down from 8.1 percent in 2004. As recently as the third quarter of 2002, cap rates averaged 9 percent or more.

Investment Outlook: Demand for Industrial Solid as Buyer Pool Expands

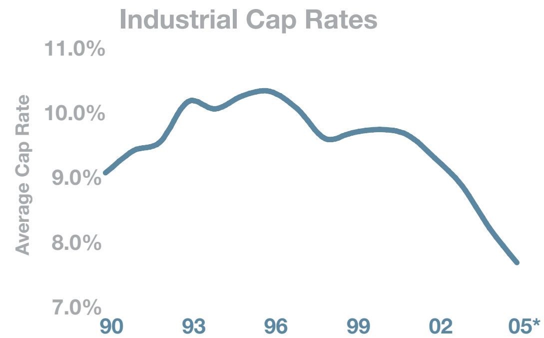
With equity and debt markets still volatile, warehouses remain attractive to real estate investors. Current returns are in excess of most debt instruments, and warehouse properties offer more reliable capital conservation aspects than stocks. Over the past year, rising transaction volume and price appreciation have characterized the industrial investment market, with dollar volume fluctuating in the $5 billion to $6 billion range per quarter. The median sales price for warehouse product has steadily increased, and cap rates are increasingly aggressive, with the average currently below the 8 percent mark.

Sale-leaseback transactions continue to gain popularity as a way for companies to free up cash. Recently, companies including Lockheed Martin (736,000 square feet), Mercedes-Benz (185,000 square feet), Motorola (382,000 square feet), Ross Stores (527,000 square feet) and Xerox (101,000 square feet) have all been involved in sale-leaseback transactions. Demand for sale-leaseback transactions is strong, and the average cap rate has dropped 100 basis points over the last year to 8.25 percent. The majority of sale-leaseback transactions involve small to medium-sized private companies raising cash for expansion. These offerings, although usually involving non-credit tenants, are highly sought after by 1031-exchange buyers.

▲ **Portfolios Attracting Investor Attention.** Through the first several months of 2005, portfolios of industrial properties accounted for more than 30 percent of dollar volume in the $5 million-plus sector. Activity is expected to remain strong as institutions and REITs have returned to the market in force as net buyers.

▲ **TICs Turn up the Heat.** Strong capital flows into real estate and the growing popularity of TICs are creating additional competition for institutions and REITs in the industrial arena. In addition, TICs are proving to be aggressive buyers, and the number of transactions involving TICs has doubled over the past year.

▲ **Activity Rising in Secondary and Tertiary Markets.** Private REITs and TICs are showing a growing interest for properties in secondary and tertiary markets as they typically offer above-average yields due to a smaller buyer pool. Higher yields are also attracting institutional investors to these markets.



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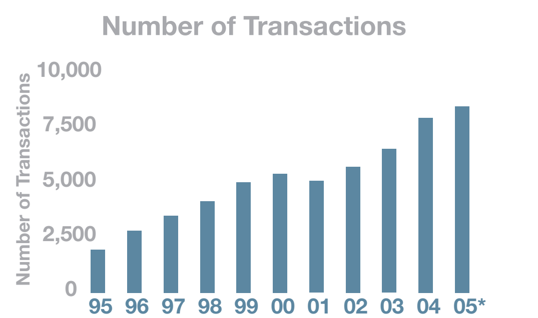
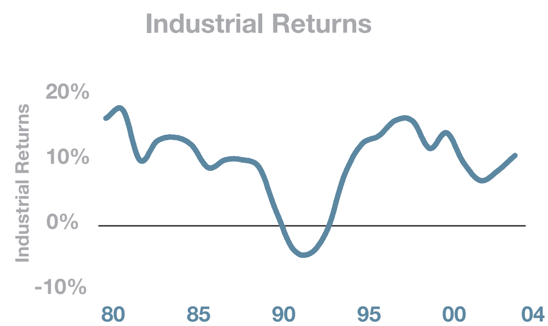


* Forecast
Sources: Marcus & Millichap Research Services, CoStar Group, Inc.



Sources: Marcus & Millichap Research Services NCREIF

- **Employment Forecast:** Total non-farm employment in Atlanta is on track to increase 2.7 percent this year, a gain of 61,000 jobs. Employment growth in trade, transportation and utilities is accelerating, which bodes well for the local industrial market. Gains in the sector during 2005 and 2006 are forecast at 1.0 percent and 1.6 percent, respectively.

- **Construction Forecast:** Industrial completions in 2005 will total 4 million square feet, 10 percent less than last year. Most new construction will consist of warehouses measuring from 250,000 square feet to 500,000 square feet in the Northeast and South submarkets.

- **Absorption Forecast:** Absorption is expected to total 6 million square feet by year end, 70 percent greater than the 2004 total. In spite of the increase, absorption will still be at one-half of the level recorded in 2000.

Asking Rent and Vacancy Trends

Sources: Marcus & Millichap Research Services, Property & Portfolio Research, NREI

Atlanta: Major Tenants Scouting Market for Industrial Space

Atlanta's industrial market will continue to post improvement thanks to its role as a key distribution hub in the Southeast. After some overbuilding in 2000 and 2001, which kept vacancy rising through part of 2003, the market began to stabilize and is now in its second year of recovery. Leasing activity in the market has picked up this year with a number of significant commitments. Home Depot recently signed on for more than 1 million square feet of space in the ProLogis Park Greenwood in McDonough, and PepsiCo revealed plans for an approximately 1 million-square foot distribution facility in Douglas County, which is being developed by a joint venture between Seefried Properties and Catellus. Several other major companies are also seeking large distribution facilities in the market, many searching for locations to house build-to-suits. These include Solo Cup and Petsmart. Some of the larger deals this year, including PepsiCo's lease signing, are being facilitated by economic incentives from the state of Georgia.

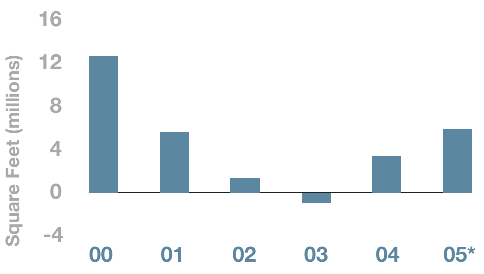
Improving fundamentals are allowing many owners to hold the line on concessions. The Airport submarket will post the most significant improvement in 2005, fueled by its strategic location at the crossroads of I-85, a main artery serving the Southeast region of the country, and I-20, a key east-west highway that connects Atlanta and Dallas. Atlanta's eastern submarkets will record the least improvement, as most tenant activity has been concentrated in newer properties around the airport and in the northern submarkets.

- **Vacancy Forecast:** Vacancy is improving but remains relatively high at 15 percent. The decline is due to an increase in leasing activity and a limited amount of speculative construction.

- **Rent Forecast:** Asking rents will rise 1 percent during the year to $3.67 per square foot as the economic recovery gains traction. Concessions are slowly burning off, a trend we expect will continue over the remainder of the year.

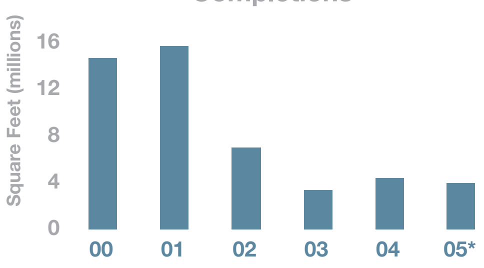
- **Investment Forecast:** The Airport submarket will continue to register some of the strongest price appreciation as institutional buyers compete for core assets. Marketwide, the median price per square foot has increased to the mid-$40 range, and prices are expected to rise further as the year progresses.

Net Absorption



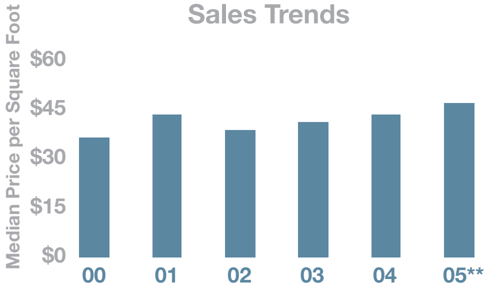
Sources: Marcus & Millichap Research Services, Property & Portfolio Research

Completions



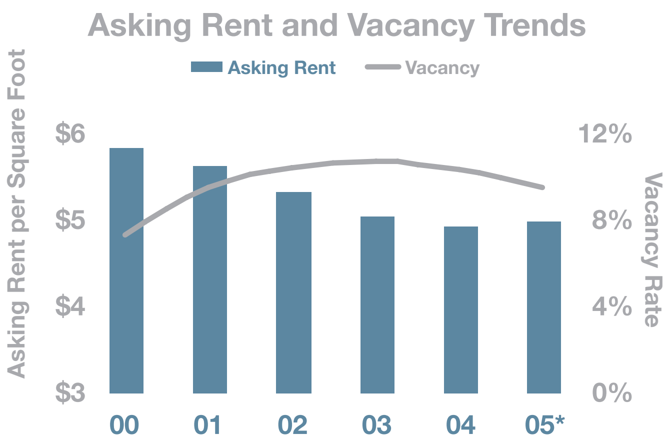
Sources: Marcus & Millichap Research Services, Property & Portfolio Research

Sales Trends



Sources: Marcus & Millichap Research Services, CoStar Group, Inc.

* Forecast ** Through 1H 05



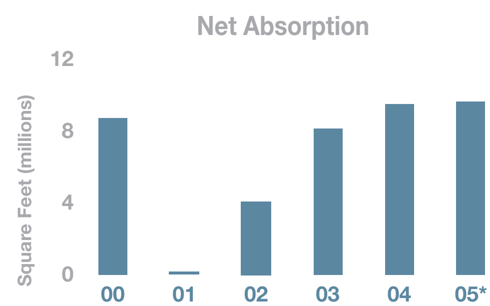
Sources: Marcus & Millichap Research Services, Property & Portfolio Research, NREI

Chicago: Investors Remain Focused on Industrial Properties

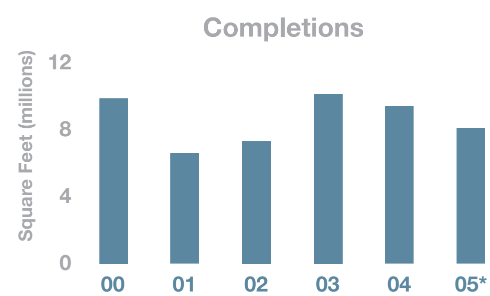
The Chicago industrial market has been relatively slow to recover. Vacancy has fallen slightly since reaching a high in 2003, but a large amount of lightly occupied, functionally obsolete stock is included in calculations, which is holding back greater improvement. This year, completions are trending downward and modern industrial properties are substantially occupied, which is helping to offset some of the effects of obsolete inventory on the overall vacancy rate. Rent concessions will continue to linger through 2005, as many owners are offering incentives to lease up space. The largest lease signed to date in 2005 was by R.R. Donnelley for approximately 650,000 square feet at Windham Industrial Center in the I-55 Corridor submarket, though the company also accounts for one of the larger move-outs this year as it leaves behind 261,000 square feet of space.

The median price is currently $52.50 per square foot, nearly equivalent to the 2004 median. A number of properties recently sold for less than $40 per square foot, which is not a reflection of declining values but rather the type of product sold. The O'Hare submarket will continue to be a focus of investment and leasing opportunities, as it is the premier industrial market in the metro area. Investors are also scouring the market for urban industrial properties that they can convert to residential and retail uses. Value investors, or those looking to assume more risk, will focus on the South Chicago/Cook County submarkets, which offer greater returns and slightly less buyer competition.

- **Vacancy Forecast:** The vacancy rate is expected to fall 80 basis points to 9.5 percent by year-end 2005, as the large amount of space recently added to the market is absorbed by new and expanding firms.
- **Rent Forecast:** A 1.2 percent increase in asking rents to $5 per square foot is projected this year as space is absorbed and construction slows. The Chicago economy is also starting to pick up steam, which should accelerate demand for industrial space.
- **Investment Forecast:** Following an 80 basis point decrease to 8.5 percent last year, early results for the first half suggest the average edged down only 10 basis points. As the year progresses, we expect some additional downward pressure on cap rates, yet the bulk of the decline has already been recorded over the past few years.
- **Employment Forecast.** Chicago firms are expected to expand payrolls by 1.2 percent in 2005, an increase of 52,000 positions. Manufacturing is expected to post the first gain since 1998, and employment in trade, transportation and utilities is forecast to expand by 15,000 jobs.
- **Construction Forecast.** Industrial completions in 2005 will total 8 million square feet, 15 percent less than last year's total. New buildings will be delivered in the Southwest I-55 Corridor and West Suburban submarkets. Pre-leasing of space under construction has been slow so far this year, averaging 26 percent of new availability.
- **Absorption Forecast.** Approximately 9.6 million square feet of industrial space is expected to be absorbed in the Chicago market this year, slightly more than the 2004 total and the highest level since 1999.



Sources: Marcus & Millichap Research Services, Property & Portfolio Research



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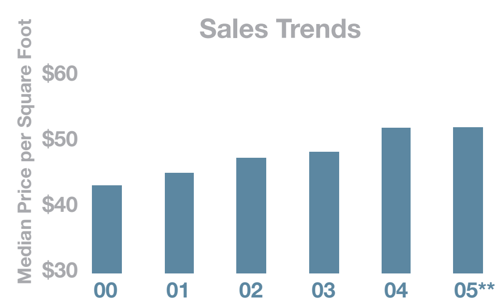


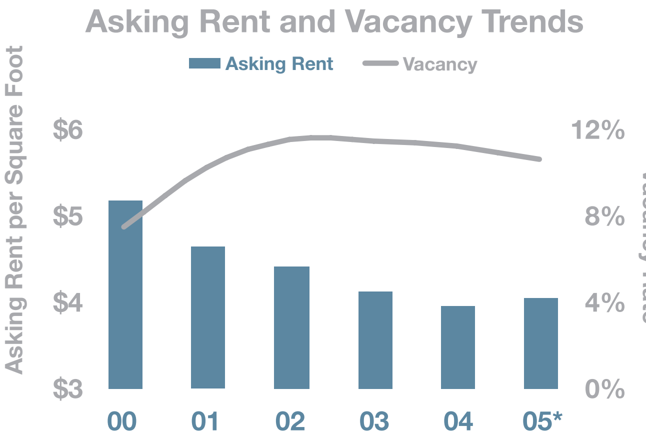
Sources: Marcus & Millichap Research Services, CoStar Group, Inc.

* Forecast ** Through 1H 05

- **Employment Forecast:** More than 76,000 jobs are expected to be created in Dallas-Fort Worth this year, a 2.8 percent increase from 2004. Sectors showing strength this year include financial activities, and leisure and hospitality, while increased defense spending should give a lift to manufacturers in Fort Worth.

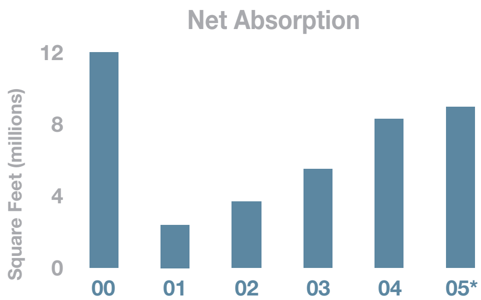
- **Construction Forecast:** Completions are expected to drop substantially in 2005. Approximately 8.8 million square feet of space was delivered in 2004, but deliveries this year are forecast to ease to 6.3 million square feet. Additionally, space coming online in the Dallas-Fort Worth market is 71 percent pre-leased.

- **Absorption Forecast:** Absorption is forecast to reach 8.5 million square feet this year, up modestly from 2004. If achieved, this will be the highest level of absorption recorded in the market since 2000.

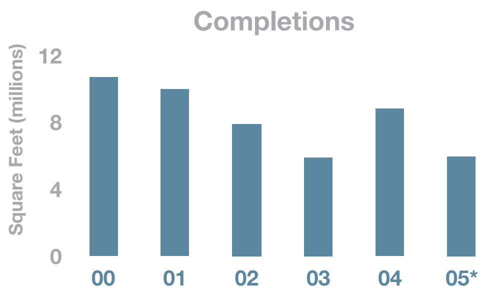


Sources: Marcus & Millichap Research Services, Property & Portfolio Research, NREI

Dallas-Fort Worth: Industrial Demand Rising as Economy Posts Gains



Sources: Marcus & Millichap Research Services, Property & Portfolio Research



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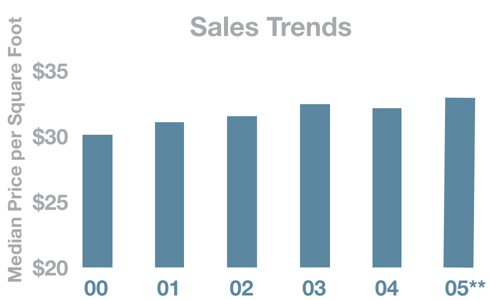


Sources: Marcus & Millichap Research Services, CoStar Group, Inc.

* Forecast ** Through 1H 05

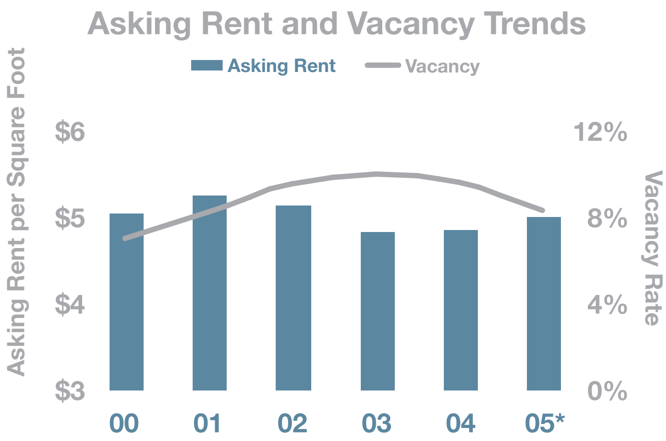
The Dallas-Fort Worth industrial market will continue to post steady improvement as new supply trails demand for space. There is, however, a growing urgency among developers to build new product close to the airport. As a result, one developer went so far as to enter into a 40-year ground lease to secure land for a 350,000-square foot speculative project. The vast majority of construction this year, however, will be build-to-suit. As a result, more than 70 percent of the space under way is pre-leased. Build-to-suits this year include Del Monte Foods' 690,000-square foot property in the North Fort Worth submarket and FedEx's 330,000-square foot facility in the South Dallas area. A few industrial properties, however, are coming online with minimal to no pre-leasing, but the majority are smaller buildings of less than 50,000 square feet. Leasing activity is expected to accelerate over the remainder of 2005 as job growth in the region rises.

On the investment front, REITs and institutions were active over the past 12 to 18 months. The $5 million and over sector in the Metroplex ranks second in the Southwest in terms of dollar volume, but prices are still affordable relative to other markets in the region. This year, the focus seems to be shifting to Class B/C assets. The most favored areas for buyers seeking stable, well-leased assets include the Airport, Mesquite, Valwood (Carrollton) and Pinnacle Park (Dallas). Many of the properties in these areas will generate strong cash flows. Value players should focus on Brook Hollow (Dallas), North Stemmons and the Great Southwest (near Beltline and I-30).

- **Vacancy Forecast:** The vacancy rate is expected to improve 90 basis points to 10.2 percent in 2005, as demand outpaces new supply and a large share of new construction comes online pre-leased.

- **Rent Forecast:** Asking rents are expected to rise 2.5 percent this year to $4.05 per square foot. Premium locations and sites offering rail service are likely to outperform the marketwide average.

- **Investment Forecast:** Competition among private investors will keep the average cap rate hovering around 8 percent, well below the 10 percent average registered just a few years ago. Many private buyers who want to avoid institutional competition will look for more value-added opportunities, such as former telecom warehouses.



Sources: Marcus & Millichap Research Services, Property & Portfolio Research, NREI

Houston: Improving Energy Sector and Foreign Trade Lift Local Economy

The Houston industrial market will ride higher in 2005 as significant economic growth materializes. Despite an increase in construction, demand and rents have edged upward. Improvement in the industrial property sector will also be driven by increased trade with Latin America, as many shipments originating in Latin American countries arrive at Houston's port. The Southeast submarket, which serves the Port of Houston and also the petrochemical industry, is outperforming the market with vacancy expected to end the year in the mid-7 percent range. The expansion of port facilities will continue to spark both construction and demand for industrial space in the area. Major retailers, including Home Depot and Wal-Mart, are setting up distribution centers in the submarket, a trend we expect will continue over the next several years.

The east side of the metro area is the focus of investors looking for greater appreciation potential, but some of those seeking more stability and comparatively better cash flows are focusing on the Northwest submarket. So far in 2005, the marketwide median price for industrial properties is running at approximately $34 per square foot, slightly below the year-end median of $34.20 per square foot. The minor decline recorded so far this year, however, can be attributed to a higher number of sales involving lower-quality assets.

- ▲ **Vacancy Forecast:** Demand for spaces measuring 10,000 square feet or less has cooled considerably, but 80 percent of the market's industrial tenants occupy larger spaces. The overall vacancy rate is forecast to decline by 90 basis points this year to 8.6 percent.

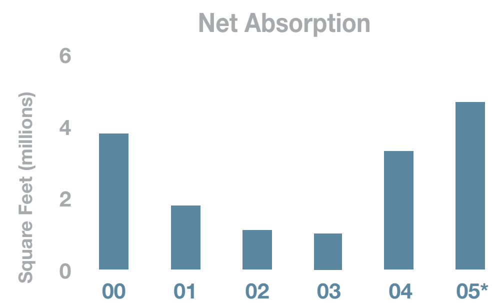
- ▲ **Rent Forecast:** Rents will rise 3 percent to $5 per square foot by year end, driven primarily by increases for large bulk warehouse space. Rents on smaller multi-tenant properties have flattened as leasing activity has slowed.

- ■ **Investment Forecast:** The average cap rate for industrial assets in the Houston market has inched up slightly this year for properties priced at $5 million or more, but overall cap rates have remained relatively consistent in the 8 percent to 9 percent range. Marketwide, demand for newer facilities with greater clear heights will continue to rise.

- ▲ **Employment Forecast:** Houston employment is on track to rise 2.5 percent in 2005, a gain of 57,000 jobs. The energy markets along with the strength of foreign trade will lead to a gain of nearly 16,000 jobs in the trade, transportation and utilities sector, and the natural resources and mining industries combined. These sectors are expected to account for 28 percent of total job growth.

- ▼ **Construction Forecast:** Developers are expected to complete 3.5 million square feet of industrial space this year, up from 2.7 million square feet in 2004. A large share of construction is occurring in the Southwest Corridor submarket, where more than 1 million square feet is under way.

- ▲ **Absorption Forecast:** Given the current economic environment, we expect absorption to reach its highest level since 1998. Approximately 4.8 million square feet is forecast to be absorbed this year, a gain of 45 percent from 2004.



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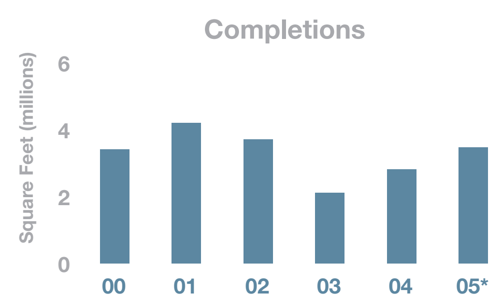

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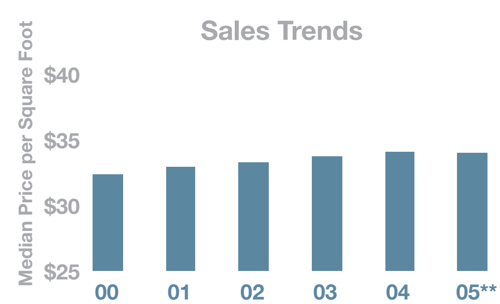


Sources: Marcus & Millichap Research Services, CoStar Group, Inc.

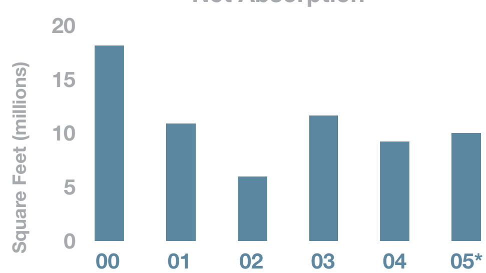
* Forecast ** Through 1H 05

- ▲ **Employment Forecast:** Employment in the Inland Empire is expected to rise 4 percent in 2005 with the addition of 46,000 jobs. The professional and business services sector is expected to add 7,000 jobs, while construction trades will expand by 4,400 positions. Following a minor decline in 2004, the trade, transportation and utilities sector is on pace to expand by 2.5 percent this year or 6,400 positions.

- ▼ **Construction Forecast:** Completions will climb 20 percent to 11 million square feet this year. In the first quarter of 2005, more than 4 million square feet of space was delivered, and approximately 15 million square feet was under construction.

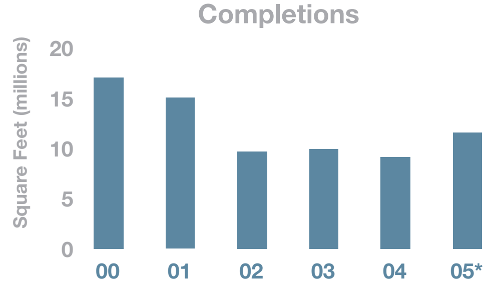
- ▲ **Absorption Forecast:** Steady demand will push absorption in the Inland Empire to 9.4 million square feet this year. Although absorption has been strong during the past three years, the current level is only 50 percent of the recent high reached in 2000.

Net Absorption



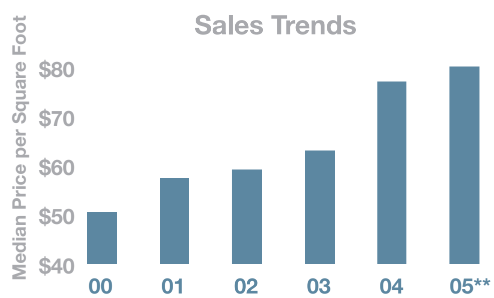
Sources: Marcus & Millichap Research Services, Property & Portfolio Research

Completions



Sources: Marcus & Millichap Research Services, Property & Portfolio Research

Sales Trends



Sources: Marcus & Millichap Research Services, CoStar Group, Inc.

* Forecast ** Through 1H 05

Asking Rent and Vacancy Trends

Sources: Marcus & Millichap Research Services, Property & Portfolio Research, NREI

Inland Empire: Construction Indicative of Rapidly Escalating Demand

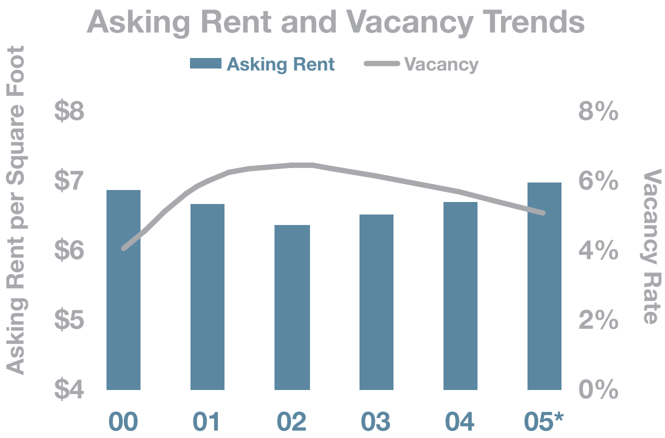
The Inland Empire's industrial market continues to grow at a rapid pace, as the region's expanding transportation infrastructure increases its role as the distribution hub for Southern California. Trade activity at the Los Angeles ports continues to increase, with most cargo containers now being transported directly to local warehouses and distribution centers. This has resulted in robust demand for space from logistics companies and manufacturing firms as they seek to take advantage of lower business costs while getting closer to their parts distributors. Developers have responded by adding approximately 10 million square feet annually. Most projects are speculative in nature, with pre-leasing activity averaging only 33 percent. There are also some large build-to-suits under way, including a 1.7 million-square foot warehouse/distribution center for Stater Brothers at the former Norton Air Force Base and a 1.6 million-square foot warehouse/distribution center for Target in the city of Rialto.

Both transaction velocity and volume reached all time highs in 2004, and based on closings reported through the first half of this year, new records will be achieved in 2005. Buyers of all types are targeting anything from under-construction properties to existing half-filled assets, especially in cities where rapid expansion is occurring. For example, substantial development plans are in place in the city of Fontana, and prices for industrial properties have increased by 35 percent over the last year to $69 per square foot.

- ▼ **Vacancy Forecast:** While demand is high and rising, it will take time for all of the new supply coming online to be absorbed. As a result, the vacancy rate is forecast to increase by 20 basis points this year to 8.7 percent.

- ▲ **Rent Forecast:** The consistent delivery of new supply and the rising popularity of the region among major companies have led to modest gains in asking rents since 2002. This year we expect a mild gain of 1.6 percent to $5.70 per square foot.

- ▲ **Investment Forecast:** The investment market for industrial properties in the Inland Empire will remain robust, and prices will continue to reflect the high level of buyer demand. The median price for properties sold to date in 2005 is in the high-$70 range.



Sources: Marcus & Millichap Research Services, Property & Portfolio Research, NREI

Los Angeles: Rebounding Economy Raises Industrial Outlook

The Los Angeles industrial sector will remain a solid performer in 2005. Property fundamentals have improved with construction easing and absorption picking up. If combined, the Los Angles and Long Beach ports would be the third-busiest in the world. The volume of goods passing through is expected to increase as the economy improves and the dollar remains relatively weak. Los Angeles ports are capitalizing on increased trade with eastern Asian countries, but an increasing amount of the goods arriving at the Los Angeles ports are being transported to the Inland Empire. As a result, the South Bay submarket may not realize a significant increase in warehouse demand from port activity; however, increased defense/homeland security spending will continue to have a positive effect on the area. In addition to Northrop Grumman, Boeing and General Dynamics, there are many other aerospace and defense-related companies in the South Bay.

Industrial investment activity continues at a strong pace. As competition for assets has intensified, the average cap rate has fallen to the low-7 percent range, about 50 basis points below the average reported last year. The median price per square foot has soared to approximately $100 per square foot, up from $90 per square foot in 2004. There have been some very large institutional transactions over the past year – a few at prices in excess of $100 million, but the vast majority of deals involve private buyers

- **Vacancy Forecast:** The vacancy rate for Los Angeles industrial properties will decrease 60 basis points to 5 percent by the end of 2005 thanks to an improving local economy and a slight decline in development activity.

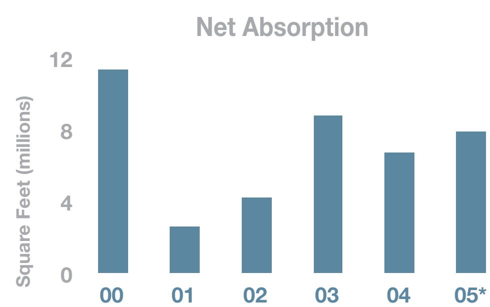
- **Rent Forecast:** Rents are forecast to rise 3.5 percent to $6.95 per square foot in 2005 after a 3 percent increase last year. Concessions still exist in some submarkets but will be employed less frequently as demand strengthens over the next 12 to 18 months.

- **Investment Forecast:** Competition for industrial assets in Los Angeles will remain fierce, prompting further price appreciation. Institutions and REITs will continue to lower their minimum deal sizes, which will create additional competition for private investors in the market. Sellers will continue to benefit from this trend.

- **Employment Forecast:** Los Angeles employers are expected to add 50,000 positions this year, a 1.3 percent increase from 2004. While the education and health services sector, along with leisure and hospitality, are driving growth, expansion in trade, transportation and utilities will accelerate this year, with 9,000 new positions expected.

- **Construction Forecast:** Industrial completions will total 5 million square feet this year, down slightly from 2004. Most new construction will consist of speculative projects. As a result, only an estimated 20 percent of space under way is pre-leased.

- **Absorption Forecast:** A 15 percent jump in absorption to 8 million square feet is expected this year. As a port city, the Los Angeles industrial market is benefiting significantly from the weak dollar, which is supporting high levels of foreign trade.



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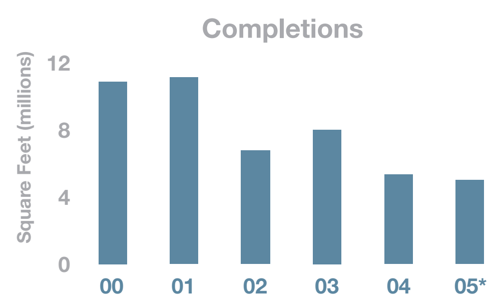

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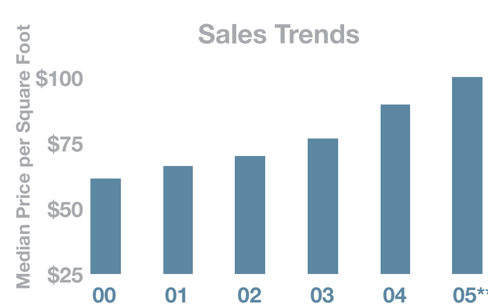


Sources: Marcus & Millichap Research Services, CoStar Group, Inc.

* Forecast ** Through 1H 05

- **Employment Forecast:** Total non-farm employment in Northern New Jersey is expected to increase by 1.8 percent in 2005, a gain of 35,000 jobs.

- **Construction Forecast:** Approximately 4 million square feet of industrial space will be completed in 2005. Three-quarters of the new construction will be delivered in the Brunswick/Piscataway submarket and will consist of warehouses ranging in size from 350,000 square feet to 400,000 square feet. Approximately 25 percent of the industrial space currently under construction in the market has been pre-leased.

- **Absorption Forecast:** The Northern New Jersey market is expected to achieve a 30 percent increase in absorption to 5.3 million square feet by year end, which will mark the fourth-consecutive year of improvement.

Asking Rent and Vacancy Trends

Sources: Marcus & Millichap Research Services, Property & Portfolio Research, NREI

Northern New Jersey: Port Activity Fueling Industrial Market

The Northern New Jersey industrial market is posting improvement this year. Increased shipments into Northern New Jersey ports have benefited the local industrial market. In addition, the local economy is gaining momentum. These trends have begun to show up in industrial leasing activity. For example, Automated Distribution Systems moved into 360,000 square feet at 23 Mack Dr. in Edison, and one of the largest deals so far in 2005 was Home Depot's commitment for 800,000 square feet at ProLogis Park Cranbury in the Exit 8A submarket. There are some very large projects nearing completion, however, which will hinder further improvement in the overall vacancy rate. For example, in the Brunswick/Piscataway submarket, a 1.3 million square foot property will soon come online, which at present is only 50 percent pre-leased.

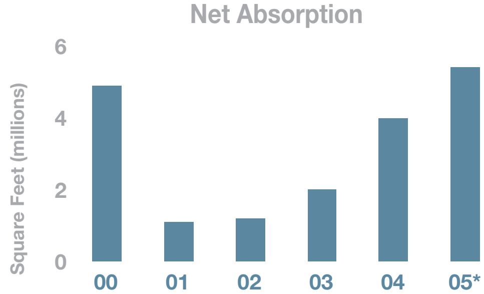
Northern New Jersey industrial assets are highly regarded by investors for their consistent long-term returns, a trend we expect will continue well into the future. Additionally, East Coast industrial properties continue to find a place in many portfolios due to the region's dense population and numerous points of entry from foreign markets. Over the past year, 42 percent of large transactions in the market involved REITs, compared to 33 percent in the Northeast region and 29 percent nationally. A few of the warehouse/distribution properties purchased by REITs sold for prices ranging from $70 to $90 per square foot, well above the marketwide median of $62 per square foot.

- **Vacancy Forecast:** The vacancy rate will decrease from 10.1 percent last year to 9.5 percent at the end of 2005 as rising demand offsets the increase in new supply. The Newark submarket is expected to outperform due to increased cargo volume coming through its port.

- **Rent Forecast:** Asking rents will post a modest increase of 1 percent in 2005 to $7.40 per square foot; however, concessions are slowly burning off, a trend that we expect will continue over the near term.

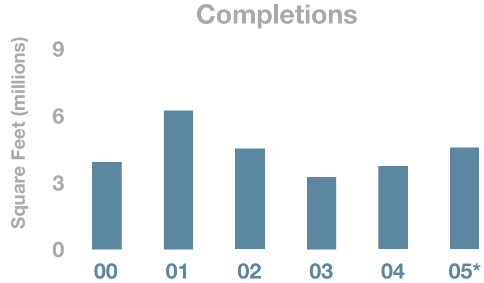
- **Investment Forecast:** Competition is strong for properties within industrial parks due to the high level of institutional activity in the market. This is, however, squeezing many private buyers out of the market for this core asset type. As a result, we expect to see strong appreciation for quality assets outside of these developments.

Net Absorption



Sources: Marcus & Millichap Research Services, Property & Portfolio Research

Completions



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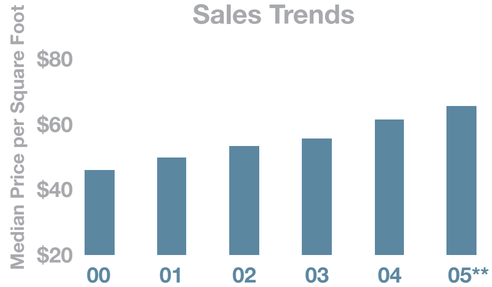
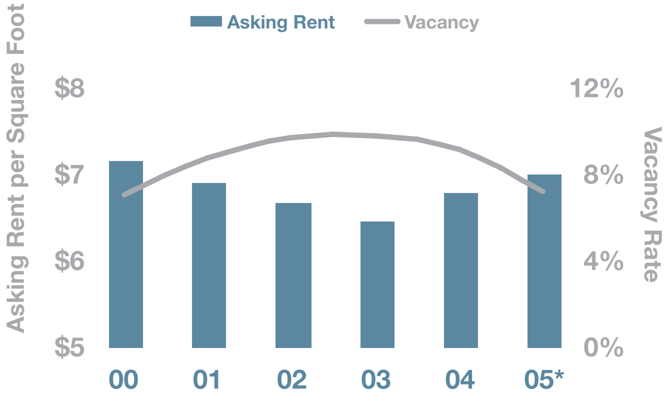
Sales Trends



Sources: Marcus & Millichap Research Services, CoStar Group, Inc.

* Forecast ** Through 1H 05

Asking Rent and Vacancy Trends



Sources: Marcus & Millichap Research Services, Property & Portfolio Research, NREI

South Florida: Foreign Trade Elevates Local Market Prominence

The South Florida industrial market, with a vacancy rate of 7 percent, is one of the tightest markets in the country. A rise in absorption, particularly in the Miami Airport submarket, will push vacancy even lower in 2005 and produce an increase in asking rents. Effective rents, meanwhile, are also rising as the use of concessions slowly eases. Miami is the largest and most active of the three South Florida industrial markets, and offers a level of port- and airport-based trade that will sustain consistent improvement of property fundamentals in the region. South Florida's consistently strong population growth also boosts the need for local storage and distribution facilities. Additionally, a lack of land suitable for industrial development is beginning to limit additions to supply, which is likely to become an even greater issue for builders going forward.

The Miami market will account for a considerable amount of South Florida's industrial investment volume, if for no other reason than it has more inventory than either Fort Lauderdale or Palm Beach. Greater stock numbers are only part of the story, however, as Miami's rising stature as a hub for Latin American commerce underpins strong property performance. The Miami Airport submarket, in particular, will continue to draw buyers seeking the consistent returns of assets located in an established freight hub.

- **Vacancy Forecast:** The overall vacancy rate will decrease from 8.9 percent at year-end 2004 to 7 percent at the end of this year due to competition arising from lighter construction and surging demand from new and expanding firms.

- **Rent Forecast:** Regionwide, a 3 percent gain in asking rents is forecast this year with the average expected to reach $6.95 per square foot by year end. In addition, owners will continue to cut back on concessions as demand intensifies.

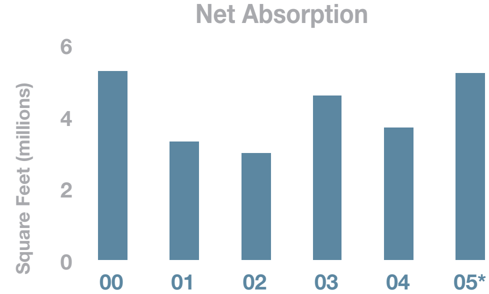
- **Investment Forecast:** The Miami metro area will continue to garner the lion's share of industrial investment activity, but the burgeoning biotechnology industry will drive demand for flex space in North Palm Beach County. Overall, prices in the Palm Beach area are being driven more by expected appreciation over the next several years than by cash flows.

- **Employment Forecast:** South Florida's three metro's, which include Fort Lauderdale, Miami-Dade and Palm Beach, are expected to add 73,000 jobs this year, a gain of 3.1 percent. Total employment in the Palm Beach metro is forecast to grow 4 percent, led by gains in professional and business services and trade, transportation and utilities.

- **Construction Forecast:** Developers are on track to deliver 2.2 million square feet this year, a 19 percent decrease from 2004. A significant amount of new construction will be delivered in Fort Lauderdale's Coral Springs and Southwest Broward submarkets.

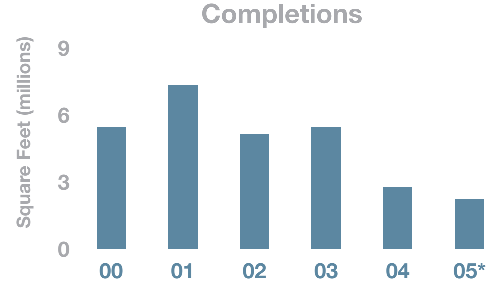
- **Absorption Forecast:** Absorption in South Florida is projected to reach 5.5 million square feet by the end of this year, 50 percent more than the 2004 total. Absorption has been strong for the past several quarters due to population-driven commercial growth and the region's rising importance in terms of Latin American trade.

Net Absorption



Sources: Marcus & Millichap Research Services, Property & Portfolio Research

Completions



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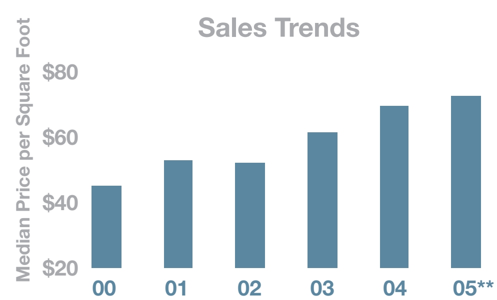
Sales Trends



Sources: Marcus & Millichap Research Services, CoStar Group, Inc.

* Forecast ** Through 1H 05

Marcus & Millichap

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Capital Markets Outlook

By WILLIAM E. HUGHES, Senior Vice President, Marcus & Millichap Capital Corporation

Bond market bears and bulls have alternated turns pushing 10-year U.S. Treasury rates in opposite directions so far in 2005. Fed Chairman Greenspan's observation that persistently low rates were a "conundrum" that defied logic ignited a bond market sell off and a resulting surge in rates. Rates climbed through March and reached a high of 4.62 percent on March 28 as oil prices spiked and signs of inflation emerged. Shortly thereafter, market sentiment turned again on economic news, and rates fell to around 4.2 percent in early May. More bullish sentiment sent the 10-year rate to less than 4 percent in early June, although a subsequent sell-off pushed rates into the low-4 percent range.

As the year progresses, the bond market seems poised to turn sharply on the latest economic news. An increase in long-term rates is likely as economic growth trends become clearer, but the magnitude of an increase is uncertain. Under these conditions, owners of and investors in industrial properties may want to lock in long-term financing, especially while a flat yield curve persists. Current loan spreads are approximately 30 basis points tighter than a year ago, and both conduits and life insurance companies are competing for industrial business. In the conduit sector, demand for commercial mortgage securities remains strong, leading to high bond prices and low yields, as yields move inversely to prices. Life companies, meanwhile, are willing to compete on rates, but tend to prefer more seasoned deals located in larger markets and look to offset leasing risk with multi-tenant properties. For both capital sources, high leverage loans beginning at 75 percent LTV are pricing from 100 basis points over the 10-year U.S. Treasury for the best-quality assets to 120 basis points over for lesser properties. Low leverage loans of up to 60 percent LTV are pricing very tight to the Treasury, sometimes as low as 85 basis points over for the best deals. Property distinctions are being made on the basis of tenant credit, multi-tenant income diversification and location.

Construction financing often begins at LIBOR plus 75 to 150 basis points, though short-term rates are slowly creeping up as the Fed seeks a neutral monetary policy. Lenders will closely watch speculative building in the industrial sector in the months ahead as such activity tends to pick up whenever the economy expands.

Recent Sales Highlights

Property Name	Address	City	Sales Price	Sq. Ft.	Price per Sq. Ft.
Multi-Tenant Industrial	112 Melrich Road	South Brunswick	$28,220,000	470,315	$60
Multi-Tenant Industrial	17246 South Main Street	Gardena	$25,220,000	307,377	$82
Dr. Pepper/7-Up	950 Stelzer Road	Columbus	$18,600,000	150,866	$123
Multi-Tenant Industrial	3800 Marshall Lane	Bensalem	$18,200,000	465,800	$39
Haden International	1399 Pacific Drive	Auburn Hills	$16,250,000	167,000	$97
Single-Tenant Industrial	5300 Region Court	Lakeland	$15,550,000	292,140	$53
West Valley Business Park	6520 190th Street	Kent	$14,888,000	212,950	$70
Multi-Tenant Industrial	2211 Newmarket Parkway	Marietta	$14,700,000	177,579	$83
Invensys	100 Victoria Street	Long Beach	$12,750,000	219,000	$58
R.R. Donnelley	254 Internationale Drive	Bolingbrook	$12,700,000	261,544	$49
Single-Tenant Industrial	3245 Meridian Parkway	Weston	$12,500,000	232,000	$54
Single-Tenant Industrial	11600 East 56th Avenue	Denver	$12,000,000	210,600	$57
ABB, Inc.	100 Distribution Circle	Mt. Pleasant	$11,900,000	132,222	$90
Foothills Vista Tech Center	15210 South 50th Street	Phoenix	$11,850,000	100,202	$118
Multi-Tenant Industrial	543 Forbes Boulevard	South San Francisco	$11,200,000	114,000	$98
Multi-Tenant Industrial	2152 Alton Parkway	Irvine	$10,900,000	120,000	$91
Mission Valley Cabinets	12250 Iavelli Way	Poway	$8,750,000	65,825	$133
Multi-Tenant Industrial	7100 Business Park Drive	Houston	$8,250,000	216,000	$38
Lockheed Martin	2400 West Marshall Drive	Grand Prairie	$6,825,000	111,471	$61

The information contained in this report was obtained from sources deemed to be reliable. Every effort was made to obtain accurate and complete information; however, no representation, warranty or guarantee, express or implied, may be made as to the accuracy of the information contained herein. Sources: Marcus & Millichap Research Services, Bureau of Labor Statistics, CoStar Group, Inc., Economy.com, National Real Estate Index, Property & Portfolio Research, Real Capital Analytics, Reis.
Flex properties are not considered industrial properties for purposes of this report.

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