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## **Grubb & Ellis Predicts Commercial Real Estate Leasing Recovery to Proceed in 2011, Investment Recovery to Continue**

*Multi housing will recover fastest; office market will continue to lag without faster job growth*

SANTA ANA, Calif. (Jan. 3, 2011) – Grubb & Ellis Company (NYSE: GBE), a leading real estate services and investment firm, today released its 2011 Real Estate Forecast, which foresees the start of a slow recovery in the leasing market for all property types in the coming year. Activity in the investment market, which began its recovery earlier than anticipated in 2010, will expand beyond assets at the top and bottom of the quality scale to include properties with slightly more risk.

“All things being considered, 2010 was actually better than most anticipated it would be – we saw positive net absorption and an uptick in investment sales during the second half of the year, positioning us for a continued recovery in 2011,” said Robert Bach, senior vice president, chief economist of Grubb & Ellis. “We have challenges to overcome, and we don’t expect fundamentals to return to their pre-recessionary peaks for several more years, but we’re slowly and cautiously building the foundation necessary to do just that.”

### **More Liquidity in Debt and Equity Markets to Spur Higher Investment Activity**

In 2010, both investors and lenders began to re-enter the playing field, with the primary focus being minimizing risk. As a result, core, well-leased assets were in strong demand, often receiving multiple bids, while extremely distressed, low-occupancy assets traded at modest prices. Properties between these two extremes – suburban assets in second-tier markets, for example – were largely unsuccessful in attracting buyers and underwriters. Lenders and investors will broaden their search parameters in 2011, leading to more activity in the higher-risk middle of the scale. Prices for the best properties will stay strong, although the national price indexes may be restrained by a greater volume of riskier properties in the sales mix.

“With all of the capital that lenders and investors have been sitting on, they are more likely to consider transactions farther off the ‘fairway’ than we saw last year now that the capital markets are thawing,” said Bach. “Look for investors to broaden their horizon beyond trophies and trainwrecks, which should result in a 75 percent increase in transaction dollar volume from 2010 levels.”

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### **Office Market Lags as Jobs Remain Elusive**

In 2011, employers are likely to add just 1.5 million net new payroll jobs – right at the level needed to accommodate the growing labor force but not enough to substantially offset the unemployment rate, generating a modest recovery in the office market. Uncertainty over employer health care costs could further discourage hiring, especially among small businesses. Corporations dealing with these and other challenges will continue to focus on minimizing occupancy costs.

As a result, the office market will experience a half-speed recovery in 2011. After peaking at 17.9 percent in the second quarter – just 10 basis points shy of its all-time high in the past 24 years – the vacancy rate ended 2010 at 17.8 percent. Grubb & Ellis researchers expect the vacancy rate in 2011 and 2012 to drop to 17 percent and 15.9 percent, respectively. This is approximately half of the 200-basis-point annual decline typical for a healthy recovery cycle.

The company expects positive net absorption of 35 million square feet in 2011, while 2012 is expected to see 47 million. This represents moderate performances compared with the expansion of 2005 to 2007, when annual absorption ranged from 62 to 89 million square feet per year. The pace of recovery will be held back by slow job growth and the substantial inventory of shadow space – unoccupied space due to layoffs but not officially accounted for as vacant. One-third of the net new demand for space in 2011 will be accommodated by shadow space and thus will not affect the vacancy rate or count in the absorption tally. In 2012, shadow space will accommodate one-quarter of the net new demand. New construction completions will be low in the next two years, consisting primarily of build-to-suit projects and a handful of larger projects, such as the World Trade Center reconstruction in New York.

Asking rental rates bottomed out in 2010 but will experience only slight gains in the next two years, with tenants retaining the bargaining leverage. Class A asking rents, which ended the year at \$30.83 per square foot per year gross, are expected to rise by 0.4 percent in 2011 and 1.4 percent in 2012. Effective rents are likely to see more improvement as landlords decrease concessions, such as free rent and tenant improvement allowances, before they raise asking rates. CBD markets will see slightly higher rental rate increases, powered by stronger tenant demand for the best properties in supply-constrained, high-profile areas such as the District of Columbia, Midtown Manhattan, and key submarkets in Boston and the San Francisco Bay Area. Smaller, non-coastal CBDs are unlikely to share in that market dynamic.

Each year, Grubb & Ellis develops an Investment Opportunity Monitor geared to identify the metropolitan markets with the strongest investment prospects for each major property type over the coming five years. The rankings are based on 15 to 20 variables, are divided into three categories – demographics, economics and real estate fundamentals – and are assigned weights based on their relative importance. (A complete listing follows the release.)

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In the office sector, employment growth and barriers to entry, including scarcity and price of development sites, are two of the major factors ranked by the Investment Opportunity Monitor. Among institutional investors, New York (No. 1) – specifically Midtown Manhattan – and Washington, D.C. (No. 2), are in a class by themselves, with Boston (No. 4) and the San Francisco Bay Area, including San Francisco (No. 7) and Oakland/East Bay, Calif. (tied for No. 7), just below them. Other markets offer a different mix of advantages, however, including fewer constraints on new supply in exchange for stronger employment growth prospects. Though demand remains weak across much of Los Angeles (No. 5), the five-year outlook is stronger in terms of economic expansion, and land remains scarce and relatively expensive. Raleigh-Durham, N.C. (No. 9) and Austin, Texas (No. 10), offer few supply constraints but very strong prospects for population growth and job creation over the next five years, fueled by their superior universities, reasonable housing and business costs and ability to attract a young, educated labor force. Portland, Ore. (No. 3) and San Diego (No. 6) also share likely population and job growth over the next five years.

### **Increased Trade to Spur Industrial Sector Recovery**

With the weak dollar expected to boost exports and stronger consumer spending spurring imports, landlords are expected to see increased activity and demand for space. Manufacturers, wholesalers and retailers will continue to optimize their supply chains, and as a result, state-of-the-art distribution facilities in key logistics markets will win out among all industrial property subtypes. The risks to the recovery include rising protectionism in the form of currency devaluations, tariffs and other trade barriers, but the industrial market is well-positioned for recovery given the existing climate.

The national industrial vacancy rate, which peaked in the first quarter of 2010 at 10.9 percent and ended the year at 10.5 percent, is expected to decline gradually to 10.1 percent by year-end 2011 and 9.3 percent by year-end 2012. Net absorption of 60 million square feet in 2011 and 120 million square feet in 2012, combined with minimal new construction, will propel the expected tightening in the market. Despite these improved fundamentals, the recovery will be slow relative to the strong demand during the expansion that took place from 2005 to 2007, when annual absorption ranged from 173 to 192 million square feet. As a result, landlords will not have much pricing power over the next two years with the notable exception of supply-constrained markets near major port and transportation facilities.

The average asking rental rate for warehouse space ended 2010 at \$4.26 per square foot per year triple net, a 13-percent decline from the cyclical peak of \$4.90 per square foot recorded in the first quarter of 2007. Grubb & Ellis researchers expect the average rate to increase slightly to \$4.30 per square foot by year-end 2011 and \$4.35 per square foot by year-end 2012, both of which represent annual gains of 1 percent. The market will benefit from increasing global trade, recovering consumer spending and supply chain optimization. A better outlook for small businesses, which have missed out on the recovery so far, should generate some demand for smaller industrial buildings and spaces.

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A market's proximity to ports or inland ports continues to boost placement in the Grubb & Ellis Investment Opportunity Monitor industrial rankings; in fact, all of the top 10 markets this year – Houston (No. 1), Los Angeles (No. 2), Oakland/East Bay, Calif. (No. 3), Dallas-Fort Worth (No. 4), Seattle (No. 5), Riverside, Calif. – known as the Inland Empire (No. 6), Chicago (No. 7), Atlanta (No. 8), Portland, Ore., (No. 9), and Miami (No. 10) – fit that criteria. While other markets may not have made the top 10, a track record of strong employment growth and evidence of rising gas prices may rekindle interest in that market as a regional logistics hub in the future.

### **Multi Housing Sector to Recover First in 2011**

Foreclosures continue to add shadow supply to the availability of rentals, but modest job growth and lack of home buyers is causing the number of renter households to outpace that shadow supply. As a result, multi housing is the sector expected to recover first, according to the report. Home prices remain soft, and mortgages, while at low rates, are difficult to obtain with more conservative underwriting standards in the wake of the mortgage lending crisis.

For the multi housing sector, as for most property types, the top-scoring markets in Grubb & Ellis' Investment Opportunity Monitor are coastal markets with supply constraints in terms of land availability and pricing. Although knowledgeable investors can profit in other markets, particularly due to lower pricing in inland markets, it does suggest that the slow leasing market recovery envisioned for the next few years may continue to put a premium on well-located, well-leased properties in stronger gateway cities.

The top 10 markets for multi housing investment – New York (No. 1), San Francisco and Long Island, N.Y. (tied for No. 2), San Jose, Calif. (No. 4), Los Angeles (No. 5), Oakland/East Bay, Calif. (No. 6), Washington, D.C. (No. 7), Orange County, Calif. (No. 8), Westchester County, N.Y. and San Diego (tied for No. 9), share many characteristics, including generally high housing prices, relative scarcity of land and moderate to strong five-year employment growth forecasts, all contributing to strong apartment demand. The aging of Generation Y (children of Baby Boomers growing into their 20s and early 30s – prime apartment-renting years), will further boost apartment demand across all markets.

### **Retailers Repositioning for “New Normal”**

One of the most pronounced trends resulting from the recession seems to be a “new normal” for the retail industry. Like 2010, 2011 will see retailers repositioning stores to create leaner, more effective organizations and securing high-profile locations that are now available at lower rates.

Despite these changes in the landscape, retail leasing activity has revived more quickly than originally expected. Luxury retailers in particular are on their way to recovery as the financial pressure on the demographic they serve has eased, though the relatively high level of unemployment at the working class level will result in a slower recovery for big-box discount retailers and other merchants.

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The top 10 markets for retail property investors, according to the Grubb & Ellis Investment Opportunity Monitor, are Washington, D.C. (No. 1), Los Angeles (No. 2), New York (No. 3), San Francisco (No. 4), Portland, Ore., (No. 5), San Diego (No. 6), Boston (No. 7), Long Island, N.Y. (No. 8), Chicago (No. 9) and Seattle (No. 10). Like the top apartment markets, most of these locations are coastal markets where land is relatively scarce, and therefore expensive, and employment prospects for the next five years are good.

### **Business Travel, Weak Dollar to Bring Back Lodging**

Like other investment classes, the hotel market has seen a clear bifurcation as investment capital chased higher-end investment grade product and avoided non-institutional grade assets. The monthly volume of closed sales remained above the \$9-billion mark from June through October 2010, reflecting an increase of more than 50 percent over 2009 during the same period. Assets trading in the \$25 million and over range experienced the greatest increase in value, with a 124 percent change in price-per-unit over 2009, with all asset classes below this threshold recording negative price-per-unit growth. This unexpectedly good 2010 in core hotel industry fundamentals, which should see continuing improvement in 2011, will help alleviate some distress in the sector and provide an opportunity for some hoteliers to increase rates.

Coastal cities will continue to surge ahead, with markets such as New York, Washington D.C., Miami, Boston, Los Angeles and San Francisco still outpacing non-coastal metropolitan markets in terms of pricing and demand, though increased consumer and business travel will help to reduce the gap in investment activity between the coastal cities and Middle America metros.

Editor's Note: The complete Grubb & Ellis Forecast and regional forecasts are available on the Grubb & Ellis Company web site: [www.grubb-ellis.com](http://www.grubb-ellis.com).

### **About Grubb & Ellis Company**

Grubb & Ellis Company (NYSE: GBE) is one of the largest and most respected commercial real estate services and investment companies in the world. Our 6,000 professionals in more than 100 company-owned and affiliate offices draw from a unique platform of real estate services, practice groups and investment products to deliver comprehensive, integrated solutions to real estate owners, tenants and investors. The firm's transaction, management, consulting and investment services are supported by highly regarded proprietary market research and extensive local expertise. Through its investment subsidiaries, the company is a leading sponsor of real estate investment programs that provide individuals and institutions the opportunity to invest in a broad range of real estate investment vehicles, including public non-traded real estate investment trusts (REITs), mutual funds and other real estate investment funds. For more information, visit [www.grubb-ellis.com](http://www.grubb-ellis.com).

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**GRUBB & ELLIS INVESTMENT OPPORTUNITY MONITOR**

**U.S. OFFICE MARKET STRENGTH FORECAST**

Top 10 Markets 2011-2015

<b>United States</b>	<b>Overall Score*</b>	<b>Rank</b>
New York	77.7	1
Washington, D.C.	77.4	2
Portland, Ore.	75.0	3
Boston	73.2	4
Los Angeles	71.5	5
San Diego	70.6	6
San Francisco	69.7	7
Oakland/East Bay, Calif.	69.7	7
Raleigh/Durham, N.C.	65.0	9
Austin, Texas	64.3	10

\*Markets were ranked from 0 to 100 against 13 property, economic and demographic variables.

**U.S. INDUSTRIAL MARKET STRENGTH FORECAST**

Top 10 Markets 2011-2015

<b>United States</b>	<b>Overall Score*</b>	<b>Rank</b>
Houston	86.6	1
Los Angeles	81.9	2
Oakland/East Bay, Calif.	72.1	3
Dallas-Fort Worth	71.7	4
Seattle	70.6	5
Riverside, Calif.	69.2	6
Chicago	66.4	7
Atlanta	66.1	8
Portland, Ore.	63.9	9
Miami	61.3	10

\*Markets were ranked from 0 to 100 against 14 property, economic and demographic variables.

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**U.S. MULTI HOUSING MARKET STRENGTH FORECAST**

Top 10 Markets 2011-2015

<b>United States</b>	<b>Overall Score*</b>	<b>Rank</b>
New York	70.4	1
San Francisco	64.5	2
Long Island, N.Y.	64.5	2
San Jose, Calif.	62.8	4
Los Angeles	62.6	5
Oakland/East Bay, Calif.	60.1	6
Washington, D.C.	59.7	7
Orange County, Calif.	59.2	8
Westchester County, N.Y.	58.6	9
San Diego	58.6	9

\*Markets were ranked from 0 to 100 against 15 property, economic and demographic variables.

**U.S. RETAIL MARKET STRENGTH FORECAST**

Top 10 Markets 2011-2015

<b>United States</b>	<b>Overall Score*</b>	<b>Rank</b>
Washington, D.C.	87.0	1
Los Angeles	83.3	2
New York	73.1	3
San Francisco	72.8	4
Portland, Ore.	70.0	5
San Diego	69.8	6
Boston	69.3	7
Long Island, N.Y.	69.2	8
Chicago	68.9	9
Seattle	65.2	10

\*Markets were ranked from 0 to 100 against 17 property, economic and demographic variables.