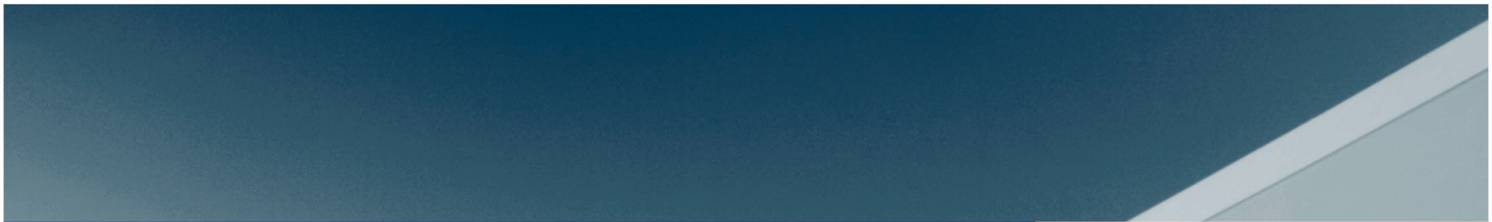


INDUSTRIAL

Metro: Los Angeles

Contents

Industrial- Reis Observer

THE ECONOMY

"Los Angeles was hit hard by the Great Recession," the Los Angeles County Economic Development Corporation (LAEDC) noted in its 2012 economic forecast. "Over 350,000 jobs were lost and the unemployment rate rose to 13%." Subsequently, according to this source, "Los Angeles County has participated somewhat unevenly in the economic gains of the past two years, but recovery is lagging the state as a whole." The data bear this out. According to Current Employment Survey (CES) data from the U.S. Bureau of Labor Statistics (BLS), annual average total non-farm payroll employment fell by 8.5% (350,000) from 2007 to 2010, compared with a national average loss of 5.8%. From 2010 to 2011 employment rose 0.6% by this measure in Los Angeles, and 1.1% in the United States.

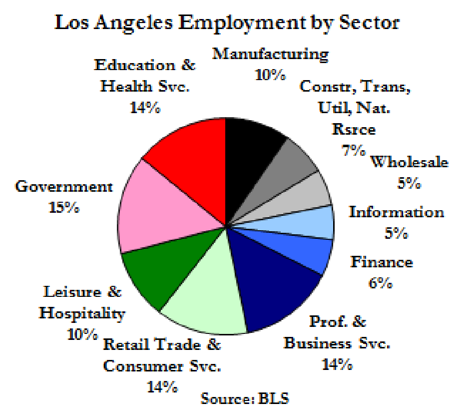
More up to date CES data for February 2011 to February 2012 show a gain of 39,600 payroll jobs (1.0%) in Los Angeles, about the same as in the increase from February 2010 to February 2011. The self-employed—freelancers, contract workers, and business owners—are a rising share of the workforce in Los Angeles, and CES data does not include them. According to household-based data from the BLS, including these non-employees, the employment gains are much smaller, with the number of employed residents of Los Angeles County rising by just 11,700 (0.3%) in the year to February 2012, less than in the previous 12 months.

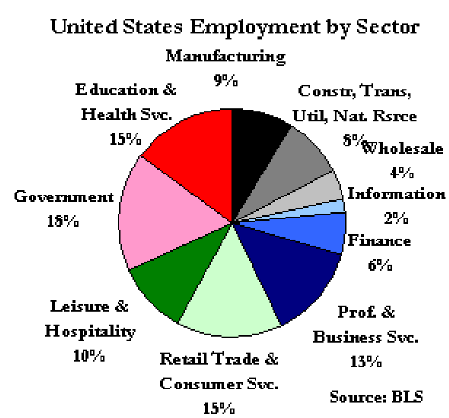
CES data by sector shows the diversity of the Los Angeles economy, with concentrations relative to the national average in Manufacturing, Professional and Business Services, and in particular, Information. Los Angeles is less Government depended than the nation as a whole. A large share of the recent job gains are in key office- and studio-based sectors. From February 2011 to February 2012, according to CES data, payroll employment increased by 14,400 (7.4%) in the Information Sector, led by a gain of 15,500 (12.6%) in the Motion Picture and Sound Recording industry. This industry also has a large number of self-employed workers as well, so its total increase in workers may be larger than this. According to LAEDC entertainment industry activity has increased, "with overall film production rising modestly last year after a large rebound in 2010. More motion pictures and commercials were filmed locally in 2011, but television pilots and shows declined slightly." The Financial Activities sector added 2,400 jobs (1.2%) year-over-year as of February, and Professional and Business Services employment increased by 11,500 (2.1%). The latter includes an increase of 6,600 (7.8%) in the Employment Services industry, which includes temporary workers.

- *The BLS reports a seasonally unadjusted unemployment rate of 12.0% in February for the Los Angeles Metropolitan Division, down from 12.3% one year earlier.*

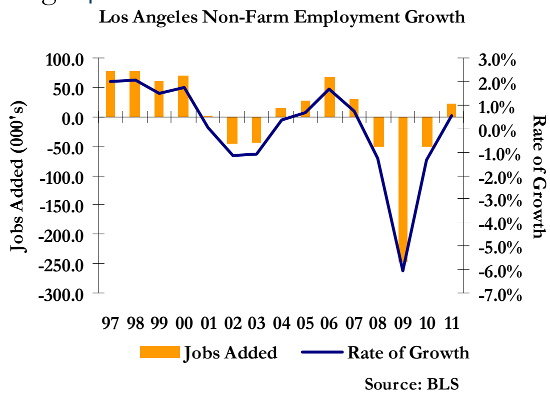
- *Total non-farm employment in Los Angeles was up 1.0% year-over-year in February, according to the BLS.*

- *Moody's Economy.com reports a first quarter 2012 average household income of $134,523 for Los Angeles. Average household incomes of $123,440 and $128,587 are reported for the top metros in the nation and West region, respectively.*

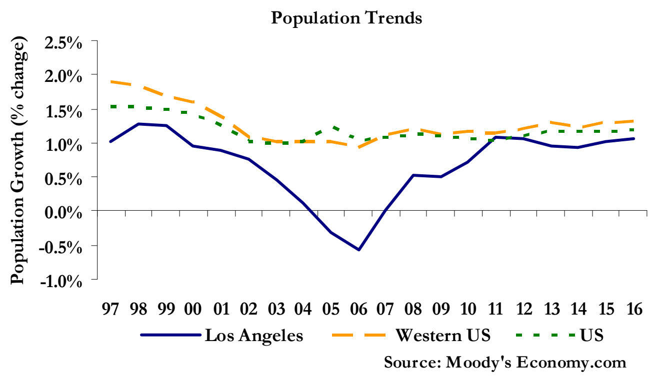




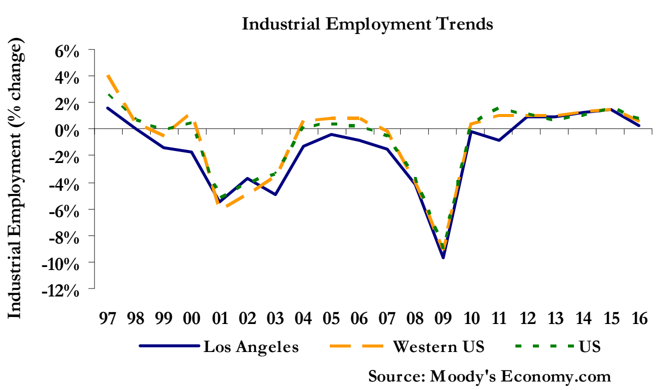
Employment in the industrial sectors has been weaker according to CES data for the most recent February-to-February period, with Manufacturing losing another 6,300 jobs (1.7%) and Transportation and Warehousing losing 3,000 (2.2%), offsetting gains of 2,700 (1.3%) in Wholesale Trade and 4,300 (4.3%) in the long suffering Construction sector. "International trade activity finished 2011 just behind the prior year, but only because of a strong finish in December," according to LAEDC. This causes "concerns about the impact of slower global economic growth on trade coming through the ports and the airports."



Meanwhile "major construction projects will support the Los Angeles economy" as "LAX, Metro, and the two ports all have significant construction programs underway." As Los Angeles transitions from a sprawling area growing horizontally on undeveloped land to a built out area adding density, its rail transit system is growing. According to *CurbedLA*, plans are moving forward to expand the subway west on Wilshire Boulevard, with an EIS released for three new stations between Koreatown and Westwood. The light rail network is also growing.



Expanding activity has spilled over to the hard-hit consumer-driven sectors, with CES data showing an increase of 6,400 jobs (1.7%) year-over-year in February in Leisure and Hospitality, and 5,500 (1.4%) in Retail Trade. Within the latter sector the Food and Beverage Store industry added 2,600 jobs (3.0%) and the big-box General Merchandise Stores industry added 2,400 jobs (3.7%). According to Moody's Economy.com, household average income increased 1.6% in the year to first quarter 2012, and the population rose by 1.0% (103,000) or about the national average pace.



OUTLOOK

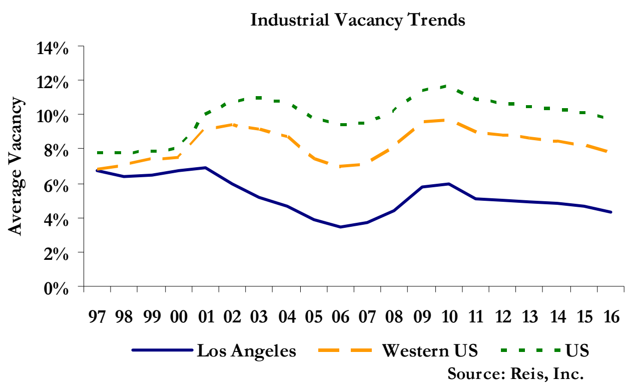
Moody's Economy.com predicts an increase of 51,700 jobs (1.4%) in 2012 and slightly more in 2013. Very strong job gains are forecast for the following two years. LAEDC is more pessimistic, and predicts it will take years to regain the pre-recession job peak.

THE REAL ESTATE MARKET

The Los Angeles industrial market was still moving forward in the first quarter of 2012, but the pace slowed somewhat due to extensive new supply. Demand remains solidly positive, according to Reis data, and rent gains are starting to pick up. "Increased leasing activity has helped stabilize vacancy rates, but there are signs leasing rates might soon turn the corner," according to the 2012 forecast by the Los Angeles County Economic Development Corporation (LAEDC). "Prospective tenants are still aggressive in their lease negotiations, and leases are taking a long time to close."

OCCUPANCY

Reis reports a first quarter 2012 vacancy rate of 8.9% for 443 million square feet of multi-tenant warehouse/distribution space in Los Angeles County, down 10 basis points from the prior quarter, and 120 from the first quarter of 2011. The rate had peaked at 10.5% in the third quarter of 2010. For 38.8 million square feet of multi-tenant Flex/R&D space, Reis reports a vacancy rate of 6.6%, down 10 basis points from the prior quarter and down 190 basis points year-over-year. Industrial vacancy in Los Angeles is well below the U.S. and West Region averages.

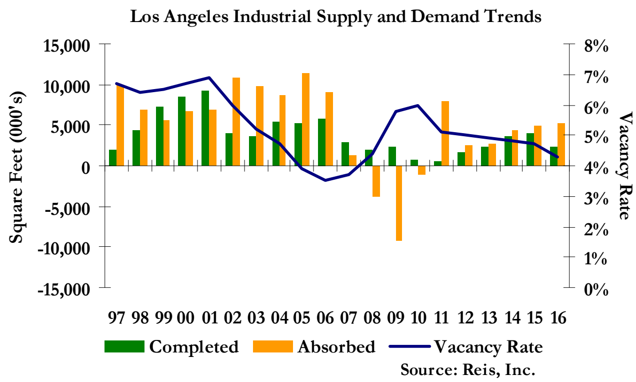


Cushman & Wakefield puts the overall vacancy rate for 1.1 million square feet of all industrial space at 4.7%, while Colliers reports 4.8% for 881 million square feet, down 20 basis points from the prior quarter. "Los Angeles and the Inland Empire still score in the 'market tightening' range for the Industrial Space Index, but are less robust than the other markets," according to the UCLA Anderson Forecast for 2012. Reis predicts the warehouse/distribution vacancy rate will continue to edge down, reaching 8.7% at year-end 2012 and 8.1% at year-end 2016. The Flex/R&D rate is forecast to level off until 2013, then edge up to 6.9% in 2016.

Special Real Estate Factors:

- *"In Southern California, industrial real estate is becoming an endangered species fighting for its survival," according to Western Real Estate Business. "The numbers tell the story: Only 8.0% of land in the City of Los Angeles is zoned for industrial uses, and 30.0% of that space is currently being used for non-industrial purposes. This leaves less than a meager 6.0% of the land in the City of Los Angeles available for active industrial uses in one of the most sought-after trade regions in the world." While manufacturing has been leaving the U.S., land for the industry is still required for distribution, according to this source. "Companies such as Hager Pacific, who specialize in acquiring, rehabilitating, and repositioning industrial, retail, office, and multifamily properties, have been able to bring renovated properties to market by buying former manufacturing plants and repositioning them to conform to today's requirements, leading to smart value investments." One example is a 28.27-acre chemical manufacturing site in Torrance, located next to a retail property. "Hager Pacific is acquiring is one of very few heavy manufacturing properties remaining in the neighborhood that has not been converted to a higher use." The firm believes it will attract tenants because there are "no other options in Torrance" and due to "the property's strategic location near the Port of Los Angeles" despite "the age and limitations of its older structures."*

SUPPLY AND DEMAND



Warehouse/distribution net absorption remained strong in the first quarter at 1.1 million square feet, following the 6 million square feet absorbed in 2011. The vacancy rate decrease slowed due to the addition of 541,000 square feet of new space, slightly more than had been built all year in either 2010 or 2011. As of the date of this report, Reis tabulates 1.2 million square feet under construction in named warehouse/distribution projects, with another 350,000 square feet in planned projects expected to break ground soon. Much of this space could complete construction in 2012, but net absorption is forecast to slow to 2.5 million square feet this year. While demand is forecast at a solid 1.5 million to 3 million square feet per year during the 2013 to 2016 period, developers and not existing landlords will reap most of the benefits, as new supply is forecast to trail only slightly.

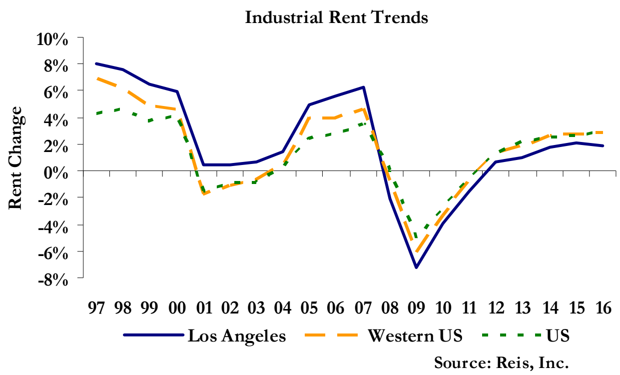
The first quarter saw a slowdown in Flex/R&D net absorption, as the quarter's total of plus 45,000 square feet was a small fraction of the plus 900,000 recorded for all of 2011. No new space completed construction during the quarter and just 90,000 square feet was added last year, but 251,000 square feet is forecast to complete construction in 2012. Reis predicts net absorption will slow to a similar 271,000 square feet this year all told, bringing the decrease in the vacancy rate to a halt. Both annual net absorption and annual new supply are forecast to remain in the 250,000 to 500,000 square feet range from 2013 to 2015, with the latter taking the lead after 2014.

"Net absorption for Los Angeles County was 1,824,500 square feet as demand remained strong in the South Bay and the Mid Counties," according to Colliers. "There is currently 799,300 square feet of industrial space under construction. Developers are optimistic about the prospect of future rental rate increases, especially for Class A modern space." Cushman & Wakefield also reports a shortage of large Class A warehouses on the market, as little of the limited new space being built is speculative.

Special Real Estate Factors:
Continued

- *"Many of the larger companies have already expanded after years of contraction, and consolidation of operations may be hitting its peak," according to Colliers. "Of chief concern will be the role of rising fuel prices and how the supply chain reacts to them. In years past, logistics professionals were not quick to change their plans as fuel prices skyrocketed and demand for larger and larger distribution centers continued. It remains to be seen if that trend will be repeated, or if a more decentralized and shorter supply chain will be the norm."*
- *"International trade activity finished 2011 just behind the prior year, but only because of a strong finish in December," according to the Los Angeles County Economic Development Corporation. "With gradual improvement in the national economy, trade gains are in store for the year ahead as are increases in jobs. However, there are concerns about the impact of slower global economic growth on trade coming through the ports and the airports."*
- *"A massive expansion of the Panama Canal prompted the Port of Los Angeles to adopt a five-year plan aimed at remaining commercially competitive and financially fit," according to the LA Daily News. "The strategic plan is aimed at maintaining Los Angeles' distinction as the nation's busiest port by developing infrastructure projects, growing market share, and*

RENTS



Warehouse/ distribution rents are edging up, with the average asking rent rising 0.3% in the first quarter to $5.98 psf, and the average effective rent up 0.4% to $5.49 psf. The year-over-year gains are 0.2% and 0.7%, respectively, and Reis predicts rents will rise by 1.0% asking and 1.3% effective for all of 2012. For Flex/R&D space, the average asking rent increased 0.4% to $10.97 psf in the first quarter, with the average effective rent up 0.3% to $9.82 psf. The year-over-year gains are 0.8% and 1.3% in this segment, with increases of 0.5% and 0.8% forecast for all of 2012 Reis predicts rent increases will improve over the forecast period, but will remain below 2.5% in all years through 2016. After years of outperformance, Los Angeles rents have been trailing the U.S. and West Region averages since the start of the recession.

Cushman & Wakefield reports a 2.0% increase in overall rents in the first quarter, to $6.24 psf. The weighted average asking lease rate is $5.88 psf according to Colliers, and the average sales price for industrial space is $87 psf. "Over the year, the average asking rent for industrial space in Los Angeles County held steady" at $6.12 psf, according to LAEDC. "Improvement in 2012 will depend largely on increases in port activity, manufacturing and population growth."

Single property industrial sales volumes and prices remain low in Los Angeles compared with the boom years of 2005 to 2007, according to Reis Transaction Analytics. In the first quarter 54 deals netted $300 million at a mean price of $76 psf. The quarterly sales volume is consistent with the approximately $1.25 billion in property that changed hands in both 2010 and 2011. The mean price, however, is well below the $88 psf figure recorded for all of 2011, and the second lowest quarterly mean that Reis has recorded here. During the 2006 to 2008 period, the annual mean sales price for Los Angeles had varied between $120 psf and $130 psf. Those prices may have reflected a redevelopment potential premium now absent.

Special Real Estate Factors:

Continued

advancing technology, according to David Mathewson, director of planning and economic development for the port." The canal expansion is a threat because it would "allow Asian container ships to bypass Los Angeles and Long Beach and move on to ports along the East Coast and Gulf Coast. Additional competition is coming from a rapid growth of ports in Canada and Mexico." The Port of Los Angeles plans to parry with a "timely completion of terminal expansion projects, wider use of zero-emission big rigs and bolstering trade with emerging markets such as Latin America and Vietnam."

- *The indefinite shutdown of two nuclear reactors could lead to power shortages in Los Angeles with the onset of an extended heat wave, unless steps are taken to fill the gap according to ABC7 News. The problems are at the San Onofre Nuclear Generating Station in Pendleton, where "hundreds of alloy tubes in massive steam generators are wearing down at an alarming rate." "Analysts say a meeting is planned to outline a series of possible steps to avoid blackouts. They're said to include bringing in electric generators on barges, restarting retired power plants or urging consumer conservation." Shutdowns of industrial businesses were not mentioned by ABC7.*

SUBMARKETS

The South Bay area is the home of the ports of Los Angeles and Long Beach, and the key to the region's economic prosperity, although distribution centers are located throughout the county and further inland, particularly in the Mid Cities submarket. The San Gabriel Valley contains more traditional manufacturing, along with high-tech and distribution space while the San Fernando Valley is more technology and local-market oriented. Labor-intensive light manufacturing, including apparel and toys, clusters in central areas.

San Fernando Valley

- Reis reports a vacancy rate of 21.1%, highest among eight submarkets, and an average asking rent of $8.59 psf, also the highest countywide, for 6.6 million square feet of warehouse/distribution space in the San Fernando Valley West submarket.

- The vacancy rate is down 710 basis points year-over-year including 220 in the first quarter. Rents are up despite the high vacancy, with the average asking rent up 1.4% for the quarter, and the average effective rent up 2.0% to $7.71 psf. The year-over-year increases are 6.4% and 9.2%, respectively.

- For 22.2 million square feet of warehouse/distribution space in the San Fernando Valley East submarket, Reis reports a vacancy rate of 8.0%, second lowest among the submarkets, and an average asking rent of $7.20 psf, the second highest.

- There the vacancy rate is down 90 basis points from the prior quarter and 250 from a year earlier. The average asking rent was unchanged from the prior quarter and down 0.3% year-over-year, but the average effective rent is up 0.3% for the quarter, and 2.0% year-over-year to $6.64 psf.

- Reis reports a vacancy rate of 8.1%, second highest among eight submarkets, and an average asking rent of $12.40 psf, the second highest countywide, for 3.1 million square feet of Flex/R&D space in the San Fernando Valley West submarket.

- The vacancy rate is down 50 basis points from the prior quarter, but it is up 240 year-over-year. The asking average increased 2.1% during

Special Real Estate Factors:
Continued

- *"Apparel manufacturing employment in Southern California has been in decline for several years," according to LAEDC, as "labor intensive production of apparel has largely shifted to lower wage countries in Latin America and Asia, particularly China. On the other hand, design related activity has expanded helping Southern California to retail a strong presence in the apparel industry." Higher fashion and faster turnarounds are advantages to local production. "Los Angeles based companies rely on a rapid production cycle, locally manufactured apparel instead of waiting for overseas shipments. In spite of rising demand for Los Angeles fashion, increasing local production is hindered by trade barriers. The apparel and accessories export-to-import ratio is roughly 1:40, measured by dollar value. The disparity reflects import tariffs by countries protecting their own large apparel manufacturing industries. Small- to medium-sized companies, in particular, struggle to gain a foothold with foreign retailers." There are over 1,000 independent fashion designers in the Los Angeles area.*

the first quarter, with the average effective rent up 2.5% to $11.21 psf. The year-over-year increases are 1.9% and 3.0%, respectively.

- The vacancy rate for 2.1 million square feet of Flex/R&D space in the San Fernando Valley East submarket is 7.5% according to Reis, while the average asking rent is $8.61 psf, the second lowest.

- Flex/R&D vacancy is down 380 basis points from a year earlier, including a 130 basis point first quarter decrease. The average asking rent is down 0.3% for the quarter and 2.9% from a year earlier, but the average effective rent is up 0.3% during the quarter to $7.69 psf. It remains down 0.5% year-over-year.

- For a 222 million-square-foot Los Angeles North submarket that also includes the Los Angeles County portion of the Inland Empire, Cushman & Wakefield reports an overall vacancy rate of 4.9% and a direct weighted average net rental rate of $6.96 psf for warehouse/ distribution space, and $10.32 psf for office service.

- Lease highlights for this area as reported by Colliers were "AMS Fulfillment leasing 121,400 square feet at 27801 Avenue Scott in Valencia, NBC leasing 110,000 square feet at 11651 Hart St in North Hollywood, Pepsi leasing 92,000 square feet at 2100 Eastman Ave in Oxnard, and Sage Publications renewing for 77,200 square feet at 2590 Conejo Spectrum in Thousand Oaks."

San Gabriel Valley

- In the San Gabriel Valley, Reis reports a first quarter vacancy rate of 9.8% and an asking rent of $6.21 psf for 16 million square feet of multi-tenant warehouse/distribution space.

- The vacancy rate is down 40 basis points over three months and 110 year-over-year. The average asking rent rose 0.3% during the first quarter, while the average effective rent increased 0.7% to $5.69 psf. Rents are up 0.5% by both measures from a year earlier.

- This is one of Los Angeles County's largest industrial markets according to other sources, but the Reis inventory is small. This implies that a large share of the space is single-tenant, owner-occupied or general industrial space. The square footage per building in the Reis inventory is less than 38,000 square feet.

- Moreover, Reis breaks out some of the more prominent industrial areas, such as City of Industry, in its separate and adjacent E. Los Angeles/Covina/Pomona Corridor submarket, which has 83.5 million square feet of warehouse/distribution space. Here Reis reports a vacancy rate of 9.7% and an average asking rent of $6.04 psf.

- In February, the 300,000-square-foot building 11 at Grand Crossings Business Park completed construction in City of Industry.

- For 2.4 million square feet of multi-tenant Flex/R&D space in the San Gabriel Valley, Reis reports a vacancy rate of 6.6% and an average asking rent of $10.90 psf.

- The vacancy rate increased 20 basis points in the first quarter, but it is down 140 from a year earlier. Both the average asking rent and the average effective rent fell 0.4% in the first quarter, the latter to $9.80 psf. The year-over-year decreases are 5.6% and 5.8%, respectively.

- Cushman & Wakefield reports an overall vacancy rate of 4.8% and a direct weighted average net rental rate of $5.52 psf for warehouse/distribution space and $13.68 psf for office/service in the San Gabriel Valley. This source gives an inventory of 192 million square feet.

- The leading leases of the quarter took place in City of Industry according to this source, where Acme Furniture leased 500,000 square feet of warehouse/distribution space at 20002-20180 Business Parkway. Also in Industry, NFI leased 300,000 square feet of warehouse/distribution space at 179 Grand Avenue and Newegg leased 200,000 square feet at 18045 Rowland Street. In Pomona, GPR Logistics leased 205,185 square feet at 2849 Ficus Street.

- Colliers reports that Traveler's Choice Travelware leased 157,300 square feet of space in Pomona. "The largest sale of the quarter was a 124,200-square-foot two-building R&D investment sale for $15.7 million, or $126 PSF in Azusa."

- *CurbedLA* reports the 80 year old terminal at the Bob Hope Airport, a competitor to LAX owned by the cities of Burbank, Glendale, and Pasadena, does not meet earthquake codes. A new terminal is under discussion, but traffic at the airport is down 27.0% since American Airlines stopped flying there, and money is tight. Obviously this would be a large and valuable development site.

South Bay

- The South Bay submarket is home to the Ports of Los Angeles and Long Beach. There, Reis reports a first quarter vacancy rate of 9.4%, and an asking rent of $6.35 psf for 100 million square feet of multi-tenant warehouse/distribution space.

- The multi-tenant inventory here, according to Reis, is the second largest among the submarkets behind the adjacent Mid-Cities submarket. The average building size is 65,300 square feet.

- This submarket has racked up 910,000 square feet of positive net absorption in the warehouse/distribution category in the first quarter, the vast majority of the marketwide total. In January the 225,800-square-foot Watson Corporate Center, a warehouse/distribution property, completed construction in Carson. The vacancy rate is down 80 basis points for the quarter and 160 year-over-year.

- The average asking rent rose 0.3% during the first quarter and the average effective rent rose 0.7% to $5.85 psf. The asking average is down 0.5% year-over-year, but the effective average is up 0.2%.

- All of the 1.2 million square feet of warehouse/distribution space under construction is located in the South Bay submarket, according to Reis.

- For 9.0 million square feet of multi-tenant Flex/R&D space in South Bay, the most among the submarkets, Reis reports a vacancy rate of 6.5% and an average asking rent of $10.40 psf.

- The vacancy rate decreased 100 basis points in the first quarter on 92,000 square feet of net absorption, and is down 190 from a year earlier. The average asking rent is up 0.7% for the quarter and 2.8% from a year earlier. The average effective rent increased 1.2% for the quarter and 5.3% for the year to $9.42 psf.

- Cushman & Wakefield reports an overall vacancy rate of 5.3% and a direct weighted average net rental rate of $6.60 psf for warehouse/ distribution space and $10.08 psf for office/service for 231 million square feet in South Bay.

- Office Depot leased 434,500 square feet at 3366 Willow Street in Signal Hill according to Cushman & Wakefield. Simple Human LLC leased 219,575 square feet at 415-501 W. Walnut Street, Compton, and 3PL Global leased 270,800 square feet at 2211 E. Carson Street in Carson. Also on W. Walnut Street in Compton, Hollander Home Fashions leased 200,000 square feet.

- "The South Bay was the top performing market this quarter within the Los Angeles Basin with a number of large deals taking place," according to Colliers. This source reports Parker Hannifin leased 126,900 square feet of space in Carson. "The largest sales of the quarter were all investment transactions. Verde Realty Group purchased a 5 building portfolio totaling 612,000 square feet for $57.5 million, or $94 psf."

- *The Brentwood Patch* reported the official opening of a $238 million terminal renovation at Los Angeles International Airport, "noting it was done on time and under budget. The renovation of Terminal 6, which was financed jointly by Los Angeles World Airports, the Transportation Security Administration and Alaska Airlines, was originally expected to cost $271 million."

<u>*Central Los Angeles*</u>

- In Central Los Angeles, the older but intensely-used industrial submarket surrounding Downtown Los Angeles, Reis reports a vacancy rate of 7.8%, lowest among the submarkets, and an average asking rent of $5.86 psf, the second lowest, for 77.3 million square feet of multi-tenant warehouse/distribution space.

- The vacancy rate is unchanged in the first quarter and down 120 basis points from a year earlier, despite the January completion of 15,700 square feet at the Apollo Freight Expansion in Los Angeles. The average asking rent is up 1.0% over three months and 0.5% over twelve months. The average effective rent is up 1.1% and 1.5%, respectively, to $5.41 psf.

- For 8.2 million square feet of multi-tenant Flex/R&D space, Reis reports a vacancy rate of 8.2%, highest among the submarkets, and an average asking rent of $14.30 psf, also the highest.

- The vacancy rate increased 60 basis points in the first quarter on 51,000 square feet of negative net absorption, but it is down 240 from a year earlier. The average asking rent increased 1.4% for the quarter, with the average effective rent up 1.0% to $12.55 psf. The year-over-year gains are 2.7% and 1.9%, respectively.

- Colliers reports a vacancy rate of 4.6% and a weighted average asking lease rate of $5.52 psf for 245 million square feet in Central Los Angeles.

- A controversial, large-scale showroom space on Melrose Avenue at Westmont Drive received approval from the Planning Commission according to the West Hollywood Patch. BMB Investment Corp. plans to build "a two-story, 30,000-square-foot building with 130 parking spaces on two underground levels. The building will primarily house wholesale home furnishings showrooms." BMB Investment also owns the other two buildings on that block, home to a Waterworks showroom and a Kitson fashion boutique.

- "Long one of the tightest submarkets in the region, the vacancy rate in Central Los Angeles stood at 2.4%," according to LAEDC. "Central Los Angeles is the county's largest industrial submarket and one of the densest in the nation."

OUTLOOK

"The region's manufacturing and logistics industries, both of which are major users of industrial space, persist as the bright spots in an otherwise subdued recovery," according to LAEDC. "The market for industrial property in Los Angeles County held its ground fairly well…Improvement in 2012 will depend largely on increases in port activity, manufacturing and population growth."

Reis expects both the warehouse/distribution market and the Flex/R&D market will show only modest improvement over the next few years, as new supply is sufficient to meet the demand for Class A space and older properties struggle for tenants. Rent gains are forecast to be limited.