

Retail Market Trends Phoenix

Grubb & Ellis Research

Year End 2008



Construction Activity Plummets

Executive Summary

The seemingly endless expansion of the Phoenix Retail Market reached a turning point in 2008. Construction activity by year-end was down significantly from the previous year. Currently there is only 2.8 million square feet under construction valley-wide. At the end of 2007 there was over 7.7 million square feet under construction. Of the total space under construction approximately 1.3 million square feet will deliver in 2009. In some cases construction progress has been completely stopped after breaking ground, with the anticipated completion dates being postponed indefinitely. Planned projects have been pushed back as well with start dates uncertain. The last time the market experienced such a low level of construction activity was in 1992 when 1.6 million square feet was delivered. Since 2000 over 48.6 million square feet has been added to the market, this massive expansion has driven the overall vacancy rate up to 8.7 percent. In addition to the new space delivered there have been significant tenant closures in 2008 including national retailers Mervyn's and Linen's N Things. By year-end 2009 more national, regional and local retailers are expected to close and push vacancy to an estimated 11 percent. In 1990 the overall vacancy rate was 14.2 percent, during that down cycle it took the market seven years to return to a normalized vacancy rate of 6.5 percent. Nearly 20 years later Phoenix is a more mature market with very strong population growth even during the current recession. The Phoenix area population has nearly doubled in size since 1992. The population forecast for 2009 is strong with over 112,000 new residents. Recovery estimates for the retail market are closer to three years before a normalized vacancy is reached.

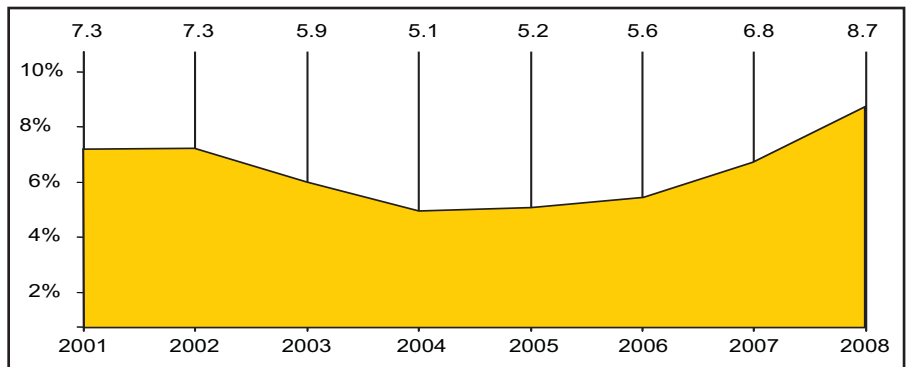
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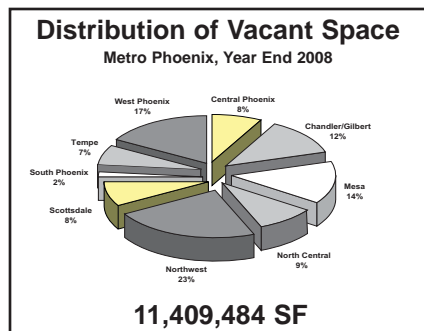


Retail Vacancy Rate*
* All Types of Space

Independently Owned and Operated

Retail Market Trends Year End 2008

"Recovery estimates for the retail market are closer to three years before a normalized vacancy is reached."



The Northwest submarket continues to have the greatest amount of vacant space, while South Phoenix represents the lowest available of all submarkets.

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Market Assessment

The Phoenix market absorbed nearly 2.6 million square feet in 2008. This was a considerable drop from the 4.7 million square feet absorbed in 2007. However, five out of the nine submarkets experienced positive net absorption in 2008. With several neighborhood and power centers being completed and subsequently fully leased, the Chandler/Gilbert submarket led all other submarkets with well over 1.3 million square feet absorbed. The Scottsdale submarket gave back the most space totaling 440,716 square feet. Of the individual product types, power centers eclipsed the two million mark with just over 2 million square feet absorbed. Strip centers gave back the most space of 56,923 square feet. Overall rental rates finished 2008 at \$19.75 per square foot, a \$.38 increase from a year ago. South Phoenix commands the highest rates of \$25.60 per square foot, while Tempe has the lowest with \$15.53 per square foot.

Vacancy rates jumped 190 basis points to 8.7 percent for year-end 2008. This was mainly due to the 6.2 million square feet of new product that was completed. Both Chandler/Gilbert and Scottsdale saw the lowest vacancy rates of 7.2 percent while South Phoenix saw a dramatic increase in vacancy to 11.4 percent. Space under construction declined sharply by 63 percent to over 2.8 million square feet under construction at year-end 2008. Builders have put projects on hold which will help stabilize vacancy rates over the next year. As in subsequent years, construction around the newly completed freeways remains the focal point for developers. The West Phoenix submarket saw roughly 34 percent of the total construction, or nearly 2.2 million square feet. Both the Northwest and Chandler/Gilbert submarkets had over 1.3 and 1.5 million square feet of new product being constructed respectively.

Opportunities and Challenges

During the current down cycle, landlords will face more challenges as they experience a reduced demand for space, a slowdown or decline in rental rolls and growing demands from tenants for rental concessions and shorter lease terms. Some existing tenants are leveraging their position in the market to renew or revise their leases early at lower rental rates. In exchange for temporary rental concessions some owners will secure extended lease terms. The dilemma for owners becomes to whom and how much they grant concession requests, otherwise risking closures of these businesses.

Phoenix Forecast

Asking rental rates, which began to soften in 2008, will continue to decline in 2009. Rental concessions will be higher this year with increased free rent terms and tenant improvement allowances. Owners will focus on maintaining occupancy levels as overall vacancy for retail has been rising since 2004 when the vacancy rate was 5.1 percent. By the end of 2009 vacancy may reach 11 percent. A return of record vacancy is unlikely because of the drastic slowdown in construction. In 2008 there was roughly 6.5 million square feet delivered. This year the forecast is for only 1.3 million square feet to be completed in market with a base of 131 million square feet.

Retail Market Trends Year End 2008

Retail Market Snapshot Phoenix Year End 2008

By Submarket (All Types)	Total SF(1)	Vacant SF	Vacant %	Net Absorption		Under Construction(2)	Weighted Average Rate(3)
				YTD 2007	YTD 2008		
Central Phoenix							
Neighborhood	4,367,457	518,351	11.9%	(155,291)	35,964	125,436	\$17.15
Power	3,462,664	79,771	2.3%	(5,377)	6,830	0	\$20.83
Regional	596,593	71,708	12.0%	(49,302)	(12,406)	0	-
Specialty/Theme	216,805	15,547	7.2%	(6,955)	(5,087)	0	\$22.00
Strip	1,443,899	200,004	13.9%	(25,452)	(116,568)	0	\$22.72
Subtotal	10,087,418	885,381	8.8%	(242,377)	(91,267)	125,436	\$19.01
Chandler/Gilbert							
Neighborhood	9,902,942	908,952	9.2%	(84,639)	362,229	179,250	\$20.24
Power	7,658,193	221,400	2.9%	52,142	900,960	0	\$31.54
Regional	2,522,770	25,826	1.0%	1,167,280	33,274	540,000	-
Specialty/Theme	422,337	31,734	7.5%	0	1,266	0	\$25.44
Strip	1,882,569	232,495	12.3%	(76,246)	50,942	73,030	\$19.51
Subtotal	22,388,811	1,420,407	6.3%	1,058,537	1,348,671	792,280	\$22.27
Mesa							
Neighborhood	9,799,076	1,149,975	11.7%	61,053	18,104	31,811	\$15.30
Power	3,451,853	199,293	5.8%	473,367	16,948	214,400	\$22.26
Regional	2,315,370	16,373	0.7%	8,599	2,933	0	-
Strip	2,144,654	294,580	13.7%	80,890	(39,742)	0	\$16.25
Subtotal	17,710,953	1,660,221	9.4%	623,909	(1,757)	246,211	\$16.09
North Central							
Neighborhood	6,185,730	737,599	11.9%	(176,680)	(18,516)	176,000	\$18.20
Power	2,433,148	133,295	5.5%	31,587	69,776	0	\$29.13
Regional	2,322,802	26,337	1.1%	139,390	17,156	0	\$25.00
Strip	1,207,563	138,135	11.4%	(3,414)	(53,371)	0	\$17.96
Subtotal	12,149,243	1,035,366	8.5%	(9,117)	15,045	176,000	\$19.78
Northwest							
Neighborhood	12,203,509	1,328,925	10.9%	(76,954)	15,327	436,597	\$15.98
Power	7,745,634	552,431	7.1%	832,913	682,077	145,000	\$22.03
Regional	3,612,866	363,608	10.1%	44,574	(334,216)	0	-
Specialty/Theme	600,000	111,000	18.5%	0	0	0	\$40.00
Strip	2,106,571	258,765	12.3%	20,249	74,684	40,985	\$17.60
Subtotal	26,268,580	2,614,729	10.0%	820,782	437,872	622,582	\$18.55
Scottsdale							
Neighborhood	6,084,407	506,903	8.3%	21,746	(169,917)	130,000	\$25.47
Power	5,135,046	280,639	5.5%	(63,627)	(226,465)	0	\$20.67
Regional	1,928,000	2,368	0.1%	28,168	1,960	0	-
Specialty/Theme	806,818	12,394	1.5%	6,073	(9,958)	0	\$36.50
Strip	1,127,594	146,261	13.0%	(8,776)	(36,336)	0	\$24.76
Subtotal	15,081,865	948,565	6.3%	(16,416)	(440,716)	130,000	\$23.95
South Phoenix							
Neighborhood	1,398,620	124,945	8.9%	12,950	68,160	0	\$25.64
Power	813,737	55,820	6.9%	0	392,917	0	-
Strip	155,945	3,600	2.3%	3,855	23,200	0	\$25.25
Subtotal	2,368,302	184,365	7.8%	16,805	484,277	0	\$25.60
Tempe							
Neighborhood	4,019,495	357,907	8.9%	11,569	(142,916)	0	\$15.62
Power	1,592,711	199,211	12.5%	79,351	(83,747)	0	\$15.37
Regional	2,767,169	86,722	3.1%	1,300,000	(86,722)	0	\$36.50
Specialty/Theme	225,096	19,711	8.8%	0	(19,711)	0	-
Strip	1,060,557	103,346	9.7%	(15,960)	(12,824)	0	\$14.27
Subtotal	9,665,028	766,897	7.9%	1,374,960	(345,920)	0	\$15.53
West Phoenix							
Neighborhood	6,548,054	736,071	11.2%	239,121	210,124	0	\$19.47
Power	7,056,048	775,860	11.0%	811,636	305,785	731,326	\$26.91
Regional	1,799,190	317,318	17.6%	7,627	606,024	0	-
Strip	658,437	64,304	9.8%	28,346	53,092	43,855	\$18.56
Subtotal	16,061,729	1,893,553	11.8%	1,086,730	1,175,025	775,181	\$22.30
By Type (All Submarkets)							
Neighborhood	60,509,290	6,369,628	10.5%	(147,125)	378,559	1,079,094	\$18.04
Power	39,349,034	2,497,720	6.3%	2,211,992	2,065,081	1,090,726	\$24.74
Regional	17,864,760	910,260	5.1%	2,646,336	228,003	540,000	\$28.57
Specialty/Theme	2,271,056	190,386	8.4%	(882)	(33,490)	0	\$36.15
Strip	11,787,789	1,441,490	12.2%	3,492	(56,923)	157,870	\$18.88
Total	131,781,929	11,409,484	8.7%	4,713,813	2,581,230	2,867,690	\$19.75

(1) Inventory includes speculative multi-tenant buildings greater than 20,000 SF (excludes medical, owner occupied and other specialized buildings).

(2) Space under construction includes speculative for lease projects.

(3) Asking rates are per square foot per year triple net.

Retail Market Snapshot Phoenix Year End 2008

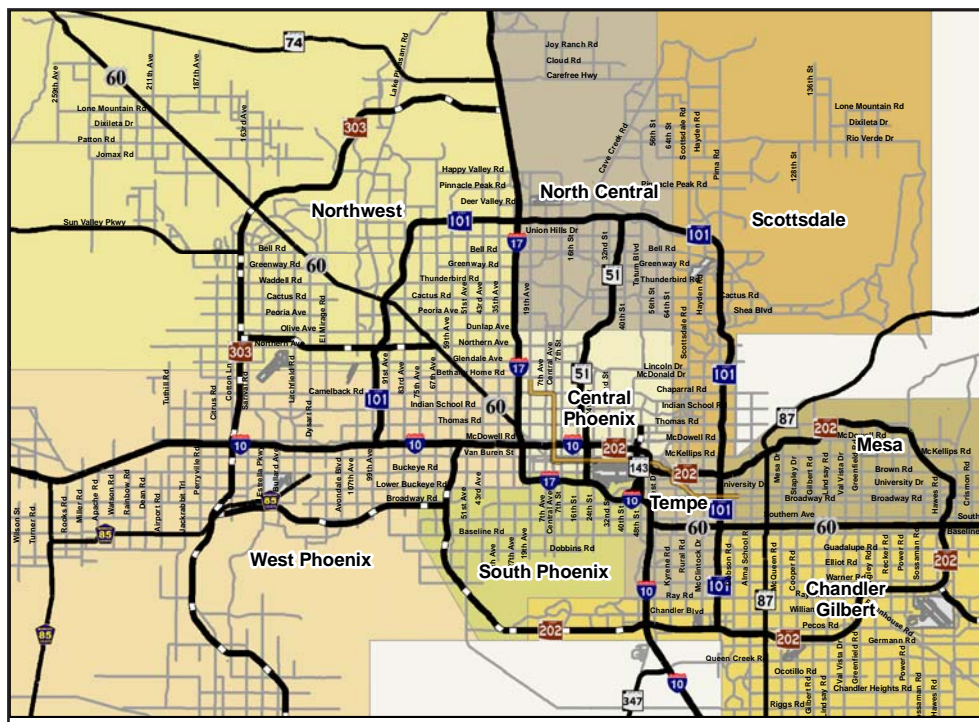
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Retail Market Terms and Definitions

Shopping Center Product Types: Shopping centers are characterized as strip, neighborhood, regional, power, and specialty, based on the center size, anchor tenants and configuration.

Vacancy and Availability: The vacancy rate is the amount of physically vacant space divided by the inventory. The availability rate is the amount of space available for lease divided by the inventory.

Net Absorption: The net change in physically occupied space over a period of time.

Asking Rent: The dollar amount asked by landlords for available space expressed in dollars per square foot per year in most parts of the country and dollars per square foot per month in areas of California and selected other markets. Retail rents are expressed as triple net where all costs including, but not limited to, real estate taxes, insurance and common area maintenance are borne by the tenant on a pro rata basis.