Grubb & Ellis
Property Solutions Worldwide

2008 | Real Estate Forecast

Custom Report

Reno Office
Reno Industrial
Reno Retail
Reno Land & Investment

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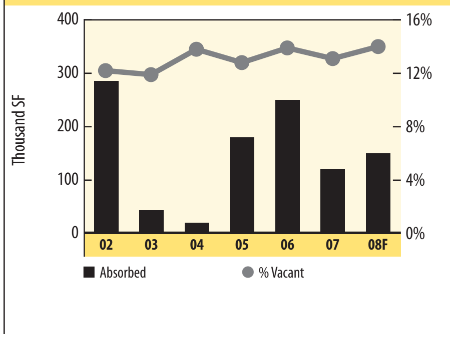
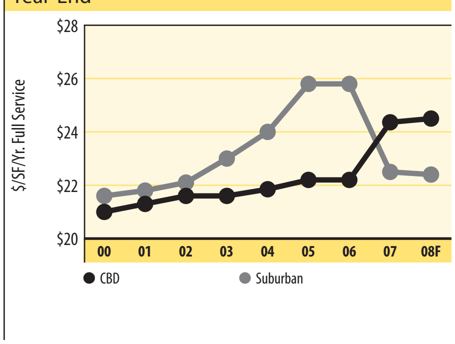
Reno
Office

The housing construction slowdown will carry over to the local office market with sublease space additions adding to vacancy woes. Downtown is looking good and the overall market growth is slowing with construction at a standstill.

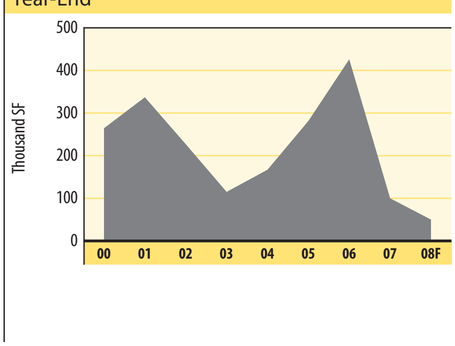
Vacancy and Absorption
Year-End



Class A Asking Rental Rates
Year-End



SF Under Construction
Year-End



The third quarter showed little improvement from the first half of 2007. Leasing activity has slowed to a crawl. National home builders are leaving the area and putting their slightly used Class A space back on the market at much reduced rates. It is still too early to predict the housing turnaround but the Fed's lowering of interest rates should help if this trend continues. It is also rumored that employment demands from growth in the industrial center east of town, Tahoe Reno Industrial Center, will add some 6,000 jobs to the area in the next six months. This would be well received.

Construction has come to a halt due to increased vacancy. Many of the pending projects are in a holding pattern until the leasing activity picks up and the current vacancy corrects. Tenants need to absorb the current building options at the lower rates prior to agreeing to the much higher rates that new construction will require to offset land, construction and TI costs. Some owner-users will break ground on smaller garden office projects. The majority of these will be for medical-related uses.

Rates have softened and concessions are showing up in inked deals. Free rent is typical in most deals. Additional tenant improvement dollars are also common among currently completed deals as landlords are willing to increase the offerings to cover entire costs for a strong tenant. The average cost for a typical tenant improvement is $65 per square foot. Base rent for second-generation space has softened and shorter terms are now being accepted. We may see this trend for the next 12 months.

The CBD is doing well. The Porsche Building located at 50 West Liberty recently sold for $38 million, a $16 million increase in sale price from only three years ago. It is also 100 percent occupied for the first time ever. There are other properties for sale in this submarket and landlords are looking for buyers due to the energy in the downtown market. News of a newly planned baseball facility in a blighted part of downtown will most certainly add to this energy.

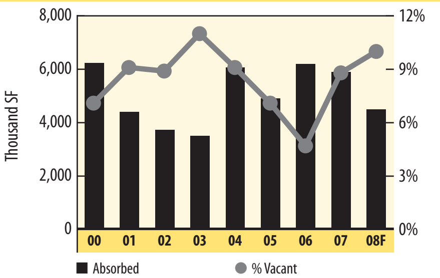
Land prices have stabilized and little change is projected for 2008. Some large parcels (five acres plus) have asking prices of $12 per square foot. These projects are in different stages of finish and this could add $4 per square foot for on-sites. South Meadows office land is still listed at higher rates as are the other preferred office sites.

Office leasing will remain slow well into 2008. Vacancy will increase and rates will soften. This slowdown will effect all office types including the once popular flex space. Again, the housing slowdown is the primary factor as builders and construction firms downsize to adjust. It will take time to absorb the existing lease and sublease space and sizable new construction will wane in 2008.

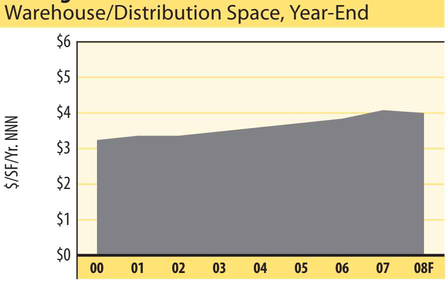
Reno
Industrial

Three years of declining vacancies and steady demand brought new developers to Northern Nevada, resulting in the largest single year's growth in 30 years. Second half slowing leaves year-end vacancy approaching double digits.

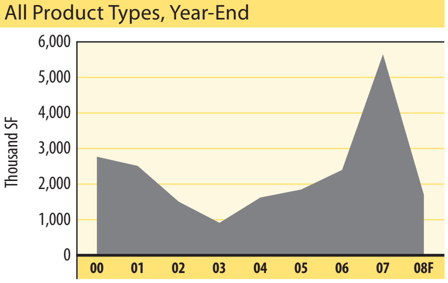
Vacancy and Absorption
All Product Types, Year-End



Asking Rental Rates
Warehouse/Distribution Space, Year-End



SF Under Construction
All Product Types, Year-End



Big Boxes Lead the Growth

Approximately 5.65 million square feet was added to the Northern Nevada industrial base in 2007, growing the market to over 68.4 million square feet. Gross absorption for the year topped out at 5.9 million square feet and positive net absorption at 2.9 million square feet, maintaining the five-year average. Overall vacancy rose from the 5.4 percent posted at the end of 2006 to 8.8 percent. Strong demand carried over from 2006 and fueled multiple speculative projects; 3.7 million square feet was completed in 2007 and 2.2 million square feet of this space is currently vacant. Expansions within the market accounted for 40 percent of growth. PetsMart led the way quadrupling its required space to 890,000 square feet. Most expansions were not quite as large and ranged from 135,000 to 418,000 square feet.

New construction starts slated for completion by early summer of 2008 include Chicago-based McShane's 560,000 square feet, local developers DP Partners' 545,550 square feet and Development Arts' 632,000-square-foot West America Commerce Center. New projects can be demised for smaller tenants, but the trend has been for larger high cube space. The market is dominated by warehouse/distribution companies and when it comes to distribution in the west, Reno stands out as a favored location from which to operate.

Market Dynamics

Available industrial zoned land in the central city is almost nonexistent, and of those remaining parcels, size and pricing virtually eliminate warehouse/distribution uses, forcing growth into the suburban submarkets. An ample supply of land in the submarkets remains affordable at $2.25 to $4 per square foot.

Cooling demand and oversupply of industrial space has created a very competitive environment for those in the market for larger space. Asking rent rates for warehouse distribution space average $0.33 per square foot per month, with landlords aggressively competing for tenants. Central City vacancy is running in the mid-7 percent range with a tightening supply in the 20,000 to 50,000-square-foot space range.

Capitalization rates are holding in the 6.25 to 6.75 percent range due in part to a very tight inventory of available property. DP Partners sold its entire portfolio, 12 million square feet of which was located here in northern Nevada, at a sub-6 percent capitalization rate. There still appears to be a large pool of investors with funds seeking quality investment real estate at aggressive capitalization rates.

The Reno market has weathered economic downturns in the past. Expect companies to continue to consolidate to northern Nevada, expand existing businesses and become home to new companies looking to better serve western markets.

Reno
Retail

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Larger retail locations remain strong as the spread of retail continues…but small to mid-size in-line space leasing has slowed and mom and pops are afraid to play…

The residential housing "correction" taking place in northern Nevada is having an effect on retail development throughout the area. Anchor tenants continue to land from deals inked some time ago, but small and midsize in-line shop space leasing activity has slowed dramatically. Retailers are reticent to commit to space rents which exceed $3.00 per square foot for inline space until they see the housing market improve. The high rents are being driven by the availability and cost of retail land, water rights and the escalating cost of construction. Rising costs also contribute to the property tax base raising NNN reimbursements to over $.50 per square foot for new centers.

Small retailers, ever fearing the 500-pound gorillas like Bed Bath & Beyond and Best Buy will land nearby and force their closure, are becoming increasingly cautious of the 'big fish eating the small fish' syndrome. Local retailers have long benefited from the 'small town support' structure but the shift is now to more value-oriented retailers.

Retail openings in 2007 included several restaurants and the Cinemark Theater at Summit Sierra in south Reno, which opened with Dillard's in 2006. Ridgeview Plaza in northwest Reno added Kohl's in the former Shopko space and also added 80,000+ square feet in a new phase. In the new 1.4 million square feet massing in Spanish Springs new users include PetsMart, Ross, Old Navy, Cost Plus, Michaels, Best Buy, Bed Bath & Beyond, Red Robin, Chili's, Longs and Office Depot. West of Reno along the I-80 corridor the much anticipated opening of Cabella's occurred in mid-November. Centers under construction or planned for opening in 2008 include: The Legends at the Sparks Marina anchored by Scheel's All Sports, Wal-Mart, Target and a 1,000-room resort/casino; Los Altos Crossing and Eagle Landing in Spanish Springs have broken ground and will open next summer in phases. Others in Spanish Springs include Pioneer Meadows (Raley's and Longs); plus final phases of Sparks Galleria, Sparks Crossing and Spanish Springs Town Center East. In south Reno, Summit Sierra will complete its 100,000 square feet third phase; Damonte Ranch will build its in-line stores and additional pads; but Bass Pro Shops' new 150,000-square-foot shop will likely be pushed back to 2009 or 2010. Bonefish Grill will make its entry into the market in the spring and Whole Foods should open in early 2008. The redeveloping down-town Reno area has inked Ruth's Chris Steak House along with a host of other users to help serve the new condo market in the area, which will start occupying in earnest in 2008.

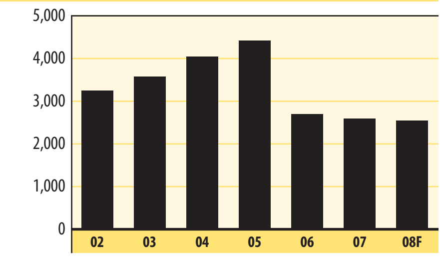
Retail Centers Opened in 2007, Under Construction or Planned for 2008

Project Name	Center Type	Size (SF)	Status	Anchors	Area
The Legends at the Sparks Marina	Open Air	1,350,000	Under Construction	Scheels, Wal-Mart, Target, Legends Resort & Casino	Sparks
The Summit Sierra	Open Air	690,000	Completed/ Under Construction	Cinemark Theatre, Dillard's, BJ's Brewhouse,	South Reno
Longley Town Centre	Neighborhood	138,300	Completed/ Under Construction	Gold's Gym, Starbucks, Shear Bliss, Spicy Pickle	South Reno
Ridgeview Plaza Phase II	Power	81,000	Completed	PetsMart, Ross, Kohl's, Famous Footwear	Northwest Reno
Damonte Ranch Town Center	Power	507,000	Completed/ Under Construction	Home Depot, RC Wiley, McDonalds, Bully's	South Reno
Sparks Crossing	Power	345,000	Completed	Old Navy, Bed Bath & Beyond, Ulta, Best Buy, Chili's, Cost Plus	Spanish Springs
Shoppers Square Phase II	Power	63,000	Planned	Staples	Park Lane

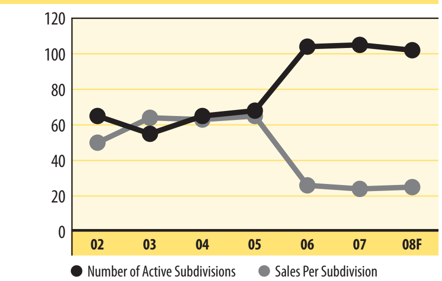
Reno
Land and Investment

Residential land values continued to decline in 2007 as a result of the cooling new home market and will face similar challenges in 2008. Right now is a great time for builders and land speculators to buy.

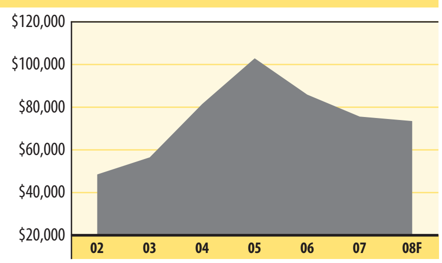
New Home Sales



New Home Subdivisions



Land Prices*



**Based upon a blended average of 5,000 SF lots*

Land

2,600± new home sales were registered in 2007, representing a 60 percent drop from the peak of 4,425 sales in 2005. Sparks/Spanish Springs again led the submarkets, accounting for 40 percent of 2007 sales but also had the greatest supply of new homes. The number of active communities in the region climbed to 108 in 2007, pushing sales per community to a record low.

Builders continue to sell off standing inventory and are very cautious about the number of speculative starts in each community. New home inventory levels should continue to drop in 2008.

New home pricing on average declined over 12 percent since the fourth quarter of 2006. Nearly 60 percent of new homes sales in 2007 were under $350,000 as compared to only 28 percent in 2005. The resale market continues to put downward pressure on the new home market as the number of active listings climbed to 5,000 in June 2007. Increasing foreclosure rates should keep resale inventory levels high for most of 2008.

Land prices have fallen nearly 50 percent since 2005 and may decline an additional 10 percent before hitting bottom in the second half of 2008. An extensive supply of land ranging from paper to finished lots has become available with few buyers still in the game. New home prices will need to stabilize before northern Nevada builders will re-enter the land market and begin to absorb the excess lot supply.

Investment

Lower capitalization rates continued throughout 2007, while strong buyer demand kept prices high. This trend should continue throughout 2008. Investors are plentiful but inventory remains limited. Capitalization rates should remain in the mid-5 to 6 percent range for most product types.

The office investment market remains strong for leased properties. The residential slump affected office vacancy rates in 2007. Activity for Class A office product slowed due to available inventory. Higher vacancy rates and flat rental rates may increase transfers in 2008.

Retail investment was popular but inventory remained limited. Low vacancy, increasing rates and property appreciation confirmed a hold rather than sell philosophy. The soft residential market may affect occupancy in newer neighborhood developments in 2008.

Demand for industrial property remained strong with limited inventory and low vacancy. Past increases in rental rates encouraged speculative development which is resulting in higher vacancies, starting a trend for 2008.

The past few years condos replaced apartment development. Now, condo developments are being converted back to apartments due to a lack of sales. Flat land prices and construction costs could create new development in 2008. Vacancy rates dropped to 4.5 percent in 2007 and rental rates will continue their upward trends in 2008.

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