Reflections on Real Estate

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Commercial Real Estate Easing in Economic Slowdown

National Association of Realtors®

Commercial real estate vacancies are trending up modestly, while investment has dropped sharply in the wake of the credit crunch, according to preliminary information for the latest *COMMERCIAL REAL ESTATE OUTLOOK* of the National Association of Realtors®.

NAR Chief Economist Lawrence Yun said economic weakness is impacting commercial real estate. "Although the supply-demand fundamentals are broadly favorable in most commercial real estate markets, vacancy rates are rising modestly and rent gains are slowing," he said. "Slow economic growth is lowering demand for commercial space, mostly in the office and industrial sectors. Despite the slowdown, the commercial real estate market is in much better shape compared to conditions during the 2001 recession."

Patricia Nooney of St. Louis, chair of the Realtors® Commercial Alliance Committee, said credit has been a problem. "Tight credit availability has significantly slowed the volume of commercial real estate transactions," she said. "Even so, institutional investors, along with foreign investors who are encouraged by the drop in the dollar, remain active in the current market."

Investment in commercial real estate during the first four months of 2008 was $48.2 billion, down 69.5 percent from $157.8 billion during the same period in 2007 when the credit markets were functioning normally; those totals do not include transactions valued at less than $5 million or investments in the hospitality sector.

The NAR forecast in four major commercial sectors analyzes quarterly data for various tracked metro areas. The sectors are the office, industrial, retail and multifamily markets. Historic data were provided by Torto Wheaton Research and Real Capital Analytics.

OFFICE MARKET

With a growth in inventory, office vacancy rates are projected to increase to 13.7 percent in the fourth quarter of this year from 12.5 percent in the fourth quarter of 2007. As a result, annual rent growth in the office sector is

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House Passes Bill to Extend Tax Break for Developers

Shopping Centers Today--June 2008

The House of Representatives passed a bill that would extend certain tax breaks important to developers and landlords. H.R. 6049, also called the Energy and Tax Extenders Act of 2008, would allow landlords to write off leasehold improvement depreciations over a 15-year period, versus a 39-year period.

The shorter term allows companies to move the expenses of renovating and retrofitting stores for new tenants off the balance sheet sooner and thus boost after-tax cash flow. Landlords have been forced to use the 39-year depreciation schedule since December 31, 2008, when previous legislation expired. In addition to the leasehold-improvement provisions, the bill would extend tax deductions per square foot for "energy-efficient investments" in commercial buildings and allow developers to go back to recouping brownfield cleanup expenses the same year the money is spent, as opposed to waiting until the cleaned-up property is sold. Developers had been enjoying those benefits before last December's expiration.

It remains unclear how the Senate will proceed with the tax extender legislation this week, says Betsy Laird, senior vice president of global public policy for the International Council of Shopping Centers (ICSC). But the measure would essentially extend these tax breaks for one more year. The shorter write-off period could help boost the overall economy as tenants and landlords reinvest in their businesses, Laird says. "ICSC has been pushing for the enactment of these important tax provisions since the start of the 110th Congress last year," she said. "If there is no certainty about these incentives, then businesses are hamstrung when making decisions concerning building improvements or adding energy efficiencies to their operations. In an already tight economic climate, Congress should move forward to help by extending these incentives as quickly as possible and for as long as possible."

Slowdown continued

expected to be 3.0 percent this year, following an 8.0 percent jump in 2007.

Estimates for the second quarter show vacancies rising sharply in Phoenix and West Palm Beach, Fla., to nearly 20 percent, double the levels of a year ago. Other central business districts in Florida have shown notable increases. The housing market downturn is having a spillover effect on commercial real estate in some local areas.

Net absorption of office space in 57 markets tracked, which includes the leasing of new space coming on the market as well as space in existing properties, is likely to total 31.3 million square feet this year, about half of the 60.0 million absorbed in 2007. "Part of the slowdown in office absorption results from new space coming online and the challenge of back-filling older class B and class C buildings," Yun said.

Office building transaction volume has dropped significantly. In the first four months of 2008, a total of only $18.5 billion in office buildings traded hands, compared with $95.0 billion during the same timeframe in 2007. The greatest decline was in suburban markets.

INDUSTRIAL MARKET

Warehouse demand has fallen because of the economic slowdown, although the demand for light manufacturing space has risen slightly. "The drop in the dollar is favoring American goods, stimulating some manufacturing with a solid pickup in exports," Yun said.

Even so, overall vacancy rates in the industrial sector are forecast to rise to 9.9 percent in the fourth quarter of this year, up from 9.4 percent in the same period of 2007. Annual rent growth should be 1.2 percent by the end of the year, down from 3.6 percent in the fourth quarter of 2007.

Markets in the West and Florida have been most impacted by the economic slowdown. Industrial markets with rising availability include Orlando, Fla.; Phoenix; Tampa, Fla.; and West Palm Beach.

Net absorption of industrial space in 58 markets tracked is estimated at 68.8 million square feet this year, down from 158.3 million in 2007. Most of the new industrial completions have been built-to-suit, leaving many obsolete or nearly obsolete structures on the market.

"Tight credit availability has significantly slowed the volume of commercial real estate transactions."

Secondary markets have become most attractive to institutional investors and users. Industrial transaction volume during the first four months of 2008 was $8.5 billion, down from $11.9 billion in same period of 2007. The biggest slowdown is in the mid-Atlantic and the Midwest.

RETAIL MARKET

Retail spending has been hurt by high oil prices with consumers throttling back on their spending habits, even in the re-

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Reflections on Real Estate is published quarterly by Souza Realty & Development. SR&D is a family-run real estate firm specializing in development, development consulting, land and commercial brokerage, and land valuation.

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Recent Land & Ranch Sales

Below are a sampling of land sales that have occurred since our last newsletter. Note that this information has been extracted from the Multiple Listing Service and public records and has not been verified for accuracy. If you have any questions regarding these sales, please contact our office.

ALAMEDA CO.	AC.	PRICE
4659 Proctor Rd., Castro Valley	6.80	1,840,000
TRACY AREA	**AC.**	**PRICE**
21 E. Vernalis Rd.	45.22	480,000
355 W. Vernalis Rd.	55.22	615,000
SANTA CLARA CO.	**AC.**	**PRICE**
Mines Rd.	160.00	220,000

CONTRA COSTA CO.	AC.	PRICE
Camino Ramon, Danville	4.35	68,000
Sellers Ave., Oakley	7.29	133,000
Los Palos Colorados, Lafayette	8.01	349,500
35 Pastor Ln., Knightsen	10.00	600,000
430 Camino Diablo, Brentwood	10.00	712,500
Happy Valley Rd., Lafayette	14.27	650,000
112 Bethany Ln., Byron	20.33	205,000
100 Bethany Ln., Byron	21.26	320,000

From 2005 forward, the San Joaquin County population growth is expected to continue to outpace the state and the nation. Between 2005 and 2030, the San Joaquin County population will grow averaging 1.9% per year, well above the state's 1.0% and the nation's 0.8% projected growth rates. The county population will triple its 1970 population in 2020 and reach the one million milestone in 2030.

San Joaquin Co. Council of Governments

Slowdown continued

tailing hotbed of Southern California. “Fortunately, the construction of retail space has slowed, which is helping preserve some balance in the market,” Yun said.

Vacancy rates in the retail sector will probably edge up to 9.3 percent in the fourth quarter from 9.2 percent in the fourth quarter of 2007. Average retail rent is expected to rise 1.3 percent in 2008, compared with a 2.9 percent gain last year.

Net absorption of retail space in 53 tracked markets is projected to grow to 18.2 million square feet in 2008 from 12.9 million last year.

Retail transaction volume during the first four months of 2008 totaled $7.5 billion, significantly below the $27.7 billion in the same period last year. Markets like Cincinnati and Detroit have seen a 100 percent decline in investment activity so far this year. Only Sacramento is showing a gain, up 47 percent.

Foreign buyers are focused on retail strip centers in Southern California, Chicago, the Northeast and the Southeast. Even so, strip center transaction volume is down 77 percent from a year ago.

MULTIFAMILY MARKET

The apartment rental market – multifamily housing – could see less demand during the second half of the year as some first-time home buyers jump off the fence and into the market.

Multifamily vacancy rates are likely to rise to 5.7 percent in the fourth quarter from 4.8 percent in the fourth quarter of 2007. Average rent is forecast to rise 4.0 percent in 2008, up from a 3.1 percent increase last year.

Multifamily net absorption is seen at 219,900 units in 59 tracked metro areas this year, up from 230,900 in 2007.

Transaction volume in the multifamily market so far this year is only $13.7 billion, compared with $23.2 billion in the first four months of 2007. Even so, some markets have seen increasing sales including San Francisco; San Jose; Tampa; Portland, Oregon; and Raleigh, North Carolina.

Available Properties

2,520 Sq. Ft. Light Industrial/Flex Suites
24500 S. MacArthur Drive
Tracy, CA
$0.60-0.65/Sq. Ft. NNN

±52.92 Acres
18775 S. Tom Paine Road
Tracy, CA
$875,000

±103.53 Acres
Morgan Territory Road
Contra Costa County
$1,545,000

Other properties currently available:

RANCH PROPERTIES			
Address	**Ac.**	**Price**	**Price/Ac.**
Byron Highway, Byron	43.70	300,000	6,865
24300 S. Banta Rd., Tracy	51.36	1,540,000	29,984
18775 S. Tom Paine Rd., Tracy	52.92	875,000	16,534
Cummings Skyway, Martinez	71.46	1,900,000	26,588
18137 S. Tom Paine Rd., Tracy	78.68	1,220,000	15,506
5208 W. Lovely Rd., Tracy	78.83	1,970,000	24,990
Morgan Territory Rd., Livermore	103.53	1,545,000	14,923
Marsh Creek Rd., Clayton	460.64	4,000,000	8,684
Palomares Rd., Sunol	1,368.00	8,900,000	6,506

OFFICE PROPERTIES			
Address	**Sq. Ft.**	**Rent**	**Price**
632 W. 11th St., Tracy	2,235 SF	1.85/SF NNN	690,000
346 W. Grant Line Rd., Tracy	2,727 SF	1.00/SF NNN	
652 W. 11th St., Tracy	2,743 SF	1.85/SF NNN	775,000
West Park Executive Suites	1 and 2 office suites; call for pricing		

INDUSTRIAL PROPERTIES		
Address	**Sq. Ft.**	**Rent**
S. MacArthur Dr., Tracy	2,500-25,000 SF	0.60-0.65/SF NNN
S. MacArthur Dr., Tracy	4,380-13,140 SF	0.65/SF NNN

RETAIL PROPERTIES		
Address	**Sq. Ft.**	**Rent**
348 W. Grant Line Rd., Tracy	1,385	1.85/SF NNN
336 W. Grant Line Rd., Tracy	2,800	1.75/SF NNN
340 W. Grant Line Rd., Tracy	8,988	0.90/SF NNN

For further information please visit our website at souzard.com

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Interest Rates

By Rich Davidson

Interest rates have declined over the past three months. Credit remains tight for all types of mortgages, credit cards, auto loans and leases. Consumer spending is weakening. Commercial real estate is weakening. However, according to the Wall Street Journal, there are some positive signs on the horizon.

First, the amount of short term debt issued by public companies to finance their operations is starting to rise. This means more liquidity is coming back into that market. Commercial paper was one of the first markets to freeze up at the start of the credit crisis, so the increased liquidity could be good news for this and potentially other credit markets.

Secondly, both Fannie Mae and Freddie Mac found investors in the debt markets more receptive to their debt offerings this week after a very difficult August. Investors have increased their interest in several debt issues and it has resulted in lower financing costs to both companies.

The Federal Reserve will have a difficult time in raising interest rates to control inflation with job losses and home values declining. Therefore the Fed is expected to keep interest rates steady at their next meeting.

KEY INTEREST RATES & INDICES
September 3, 2008

INDEX	CURRENT RATE	CHANGE FROM 6/12/08	NOTES
Bank Prime	5.00%	unchanged	
1 Yr. Treasury	2.08%	-0.54%	
5 Yr. Treasury	2.95%	-0.73%	
10 Yr. Treasury	3.71%	-0.52%	
30 Yr. Treasury	4.32%	-0.45%	
LIBOR (1 Mo.)	2.49%	+0.03%	
LIBOR (6 Mo.)	3.12%	+0.21%	
LIBOR (1 Yr.)	3.21%	+0.05%	
Freddie Mac 60 day	6.33%	+0.01%	30 year fixed rate
12 Month Treasury Average	2.664%	-0.626%	T average
11th District Cost of Funds	2.698%	-0.413%	Fund Cost
Consumer Price Index	219.96 (Jul)		+5.6% from year ago
Federal Funds Rate	2.00%	unchanged	
Dow Jones Industrial Avg.	11,533		-13.1% YTD
Consumer Confidence Index	56.9 (Jul)		Decline in confidence

RECENT LOAN CLOSINGS

1. $1,387,000 First Trust Deed Industrial Condominium refinance 5.95% North Bay.
2. $1,524,000 Second Trust Deed on 5 Residential Condominiums in San Francisco.
3. $246,000 Second Trust Deed on 2 Residential Condominiums in SF.
4. $421,000 Second Trust Deed on 2 Residential Condominiums in SF.

If I can be of any assistance with your real estate financing needs, please do not hesitate to call me at (650) 579-3995. My email address is rdavidson@redcofinance.com.