

*In most markets*

## U.S. commercial property vacancies may peak by early '11

*Daily Transcript Staff Report*

WASHINGTON — Vacancy rates continue to rise in most commercial sectors and are not expected to level out in most markets until the end of this year or early 2011, according to the National Association of Realtors (NAR).

Lawrence Yun, NAR chief economist, said there is one bright spot in commercial real estate.

"The multifamily sector can expect increased demand as the economy creates jobs and new households are formed, likely in the second half of this year," he said. "However, the office, warehouse and retail sectors continue to experience the delayed effects of the recession.

"These sectors should see gradual improvement after jobs pick up and create additional demand for space, meaning a broader improvement in commercial real estate is likely in

2011," Yun said.

The Society of Industrial and Office Realtors (SIOR), in its SIOR Commercial Real Estate Index, an attitudinal survey of nearly 700 local market experts, confirms that significant fallout from the recession remains, but to a lesser extent.

The SIOR index, measuring 10 variables, increased 2.7 percentage points to 38.2 in the first quarter, compared with a level of 100 that represents a balanced marketplace.

This is the second gain following nearly three years of declines; the last time the market was in equilibrium was in the third quarter of 2007.

Development activity remains at a standstill, with nine out of 10 respondents saying that it is virtually nonexistent in their markets.

Looking at the overall market, commercial vacancy rates appear to be approaching a plateau, according to NAR's latest Commercial Real Estate Outlook.

### **Office market**

With an elevated level of sublease space available, vacancy rates in the office sector are projected to increase from 16.9

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# Vacancy

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percent in the first quarter of this year to 17.6 percent in the first quarter of 2011, but should ease later next year.

Annual office rent is likely to fall 2.3 percent this year and decline another 2.1 percent in 2011. In 57 markets tracked, net absorption of office space, which includes the leasing of new space coming on the market, as well as space in existing properties, is forecast to be a negative 24.6 million square feet this year and then a positive 25.5 million in 2011.

In San Diego County, a pair of countywide office reports this spring indicated the market here may be on the mend, but substantial hiring will be necessary to bring down vacancies.

Both Colliers International and Jones Lang LaSalle (NYSE: JLL) were cautiously optimistic in their assessments, but acknowledged plenty of pain.

"Though San Diego's regional economy is still reeling from the global recession and a dramatically weakened labor market, some indicators point to the office market stabilizing," Jones Lang LaSalle wrote.

"Increased tenant requirements — especially from larger companies — and a resurgence of activity in the capital markets are giving market prognosticators hope of a timely recovery."

Colliers cited that at least by its own accounts, about a quarter of the submarkets posted negative absorption in the first quarter, compared to when a majority of them were in negative territory as recently as last fall.

By JLL's accounts, in excess of 15 million square feet of office space was vacant around the county as of March 31, when direct and sublease space is combined. Colliers reported a

13.7 million combined total vacancy figure.

## Industrial market

Leasing activity in the industrial sector is below historical levels with higher vacancies, more tenant concessions from landlords and a steeper decline in rental rates.

In addition, obsolete structures remain on the market.

Industrial vacancy rates are expected to rise from 14.3 percent in the first quarter of 2010 to 14.8 percent in the first quarter of 2011, then decline modestly as the year progresses.

Annual industrial rent will probably drop 6.3 percent this year, and decline another 1.5 percent in 2011.

Net absorption of industrial space in 58 markets tracked is seen at a negative 90.0 million square feet this year, and a positive 135.6 million in 2011.

San Diego County's nearly 200 million square feet of industrial property has traditionally maintained a healthy occupancy, according to CDC Commercial.

"However, our current economy has taken (countywide) vacancy from approximately 5 percent to just shy of 10 percent in just over a year," CDC noted.

A recovery in the San Diego County's industrial market is expected to begin in late 2010 or early 2011, CDC concluded.

## Retail market

Retail vacancy rates should rise from 12.6 percent in the first quarter of this year to 12.8 percent in the first quarter of 2011, and should hold at that level for most of next year.

Average retail rent is projected to decline 1.5 percent in 2010, then edge up by 0.4 percent next year.

Net absorption of retail space in 53 tracked markets is likely to be a negative 3.7 million

square feet this year and then a positive 8.9 million in 2011.

The newly formed commercial real estate brokerage Cassidy Turley BRE Commercial reported that in 2009, San Diego's retail market negative absorption of 1.2 million square feet.

However, effective rents are expected to decrease further as landlords offer more concessions to keep their tenants.

Limited construction activity should help San Diego's retail market deal with the recession.

## Multifamily market

The apartment rental market - multifamily housing - is expected to benefit from an improving economy and job market.

Multifamily vacancy rates are forecast to decline from 7.3 percent in the first quarter of this year to 6.3 percent in the first quarter of 2011.

With recent additions to supply, average rent is likely to slip 1.5 percent this year and then rise 1.2 percent in 2011.

Multifamily net absorption should be 145,700 units in 59 tracked metro areas this year, and another 214,500 in 2011.

While San Diego County's apartment market was hardly unscathed by the recession, a new report by **Marcus & Millichap** said it is poised for a modest rebound.

The brokerage reports landlords and investors may expect stable vacancies, and rents will be generally flat through next year.

A March MarketPointe Realty Advisors report pegged the countywide vacancy at a lower 4.75 percent, but that firm limits its survey to complexes with 25 or more units.

*Daily Transcript staff writer Thor Kamban Biberman contributed to this report.*

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