



Retail Development Tops Charts in 2007

The commercial real estate market continues to sustain resiliency in the face of a soft housing market. Local market indicators are not as dismal as national economic indicators would lead us to believe. The single-family home market began its volatile descent in the fourth quarter, 2005. Since that time, the rising rate of mortgage delinquencies and subsequent increase of foreclosures has placed downward pressure on housing prices nationally. Despite the housing crunch, local retail development rose at a fever-pitched pace in 2007, marking the highest year of new space added to inventory this decade. Strong market fundamentals will continue to drive Phoenix retail development. The downturn of the housing market has created challenges and may keep Valley retail developers cautiously optimistic in 2008.

The local economy continues to be supported by a rapidly expanding population. Population growth is estimated to have increased by approximately 102,000 new residents in 2007. This growth represents a 2.5 percent increase over the preceding year. The softening of the housing market has kept the population from increasing as quickly as it has in previous years. The stream of in-migration has slowed considerably to the Valley, as homeowners in other areas of the country find it difficult to sell their homes. Job growth has been affected as well. Employers added an estimated 50,000 new jobs to payroll this year, an increase of 2.7 percent, which still surpasses the national average of 1.3 percent. While many employment sectors related to the housing industry which include construction and financial activities took a hit, all due to the lackluster housing market, the Trade, Transportation and Utilities industry have reported healthy gains. Over the last two years, this sector gained an average of 14,500 new positions annually, or an increase of 3.8 percent each year. Retail trade employment accounts for approximately 250,000 positions and 12 percent of overall non-farm employment in the metro. The metro continues to be driven by leisure and hospitality which added an estimated 9,000 new positions, a 4.7 percent increase in 2007. Businesses in the tourism sector are sure to get a boost in February when the Super Bowl XLII is estimated to bring 150,000 visitors to the Valley. The metro can expect a surge in revenue of \$400 million in 2008 and the addition of 3,500 positions added to payrolls.

Retail development topped the charts in 2007. Phoenix developers have followed the residential boom in the

METRO TRENDS

	4Q07	Qtr	YOY
Vacancy	6.3%	↑	↑
Asking Rent	\$19.28	↑	↑
Completions*	9,500,000	↑	↑
Absorption	7,600,000	↑	↑
Median \$/PSF	\$177	↑	↑

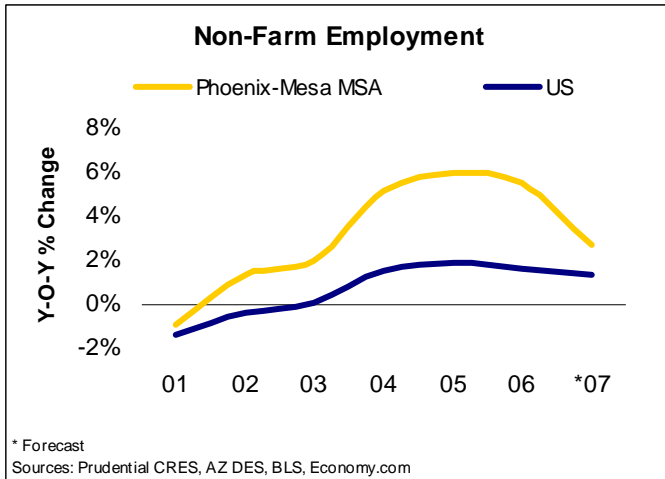
*YTD Estimate

Valley to the far-reaching suburbs for decades. As the residential component grows outward, retailers will always follow. Developers have been revisiting fully developed areas of the Valley with potential for high-return. In-fill locations dot some of the most populous areas of the Valley. Mixed-use development can be found throughout the Valley in areas with high-density employment. Mesa, Tempe, Glendale and now downtown Phoenix claim a firm foot-hold in the mixed-use infill phenomena. In the most under-served area of the Valley, Cityscape developers broke ground in the fourth quarter of 2007 in downtown Phoenix and will finish its first phase in 2009. This 2.5 million square-foot project will encompass major retailers such as AJ's Fine Foods as well as PF Chang's, in addition to a mix of residential, hotel and office space. This development is anticipated to create over 3,000 construction jobs in 2008 and almost 3,500 employees when complete. Valley developers will continue to look for opportunities to create work, live, play environments in high-density areas throughout the metro.

Valley developers added over 9 million square feet of new space in 2007 causing vacancy to edge upward. Throughout 2007, vacancy hovered in the 5 percent range. In the fourth quarter, vacancy rose 50 basis points to 6.3 percent. Almost half of the new space delivered to market in 2007 was in the form of the power center.

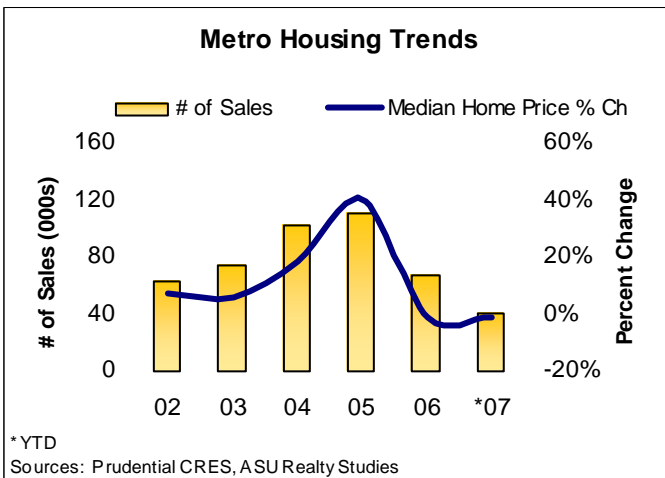
New retail will continue to serve new residential areas in the Valley, especially where land is more abundant. Commercial land values have increased greatly over the last few years urging many developers to build up instead of out. The median price of land per square foot rose by 23 percent to \$12 per square foot in 2007, however the average number of acres sold has decreased falling from 11.5 acres to 9.5 acres in the last 12-month period. With smaller parcels being purchased and prices rising, the potential for mixed-use infill over the next few years bodes well.

Employment



- In a year-over-year comparison ending in November 2007, employers added approximately 50,000 positions to the metro, a 2.7 percent gain, compared to 56,500 jobs and a 3 percent gain during the previous 12-month period.
- The Trade, Transportation and Utilities industry added 15,000 new jobs in a year over year comparison, an increase of 3.8 percent. Employment in the retail sector increased by 10,800 positions in the fourth quarter, due in part to holiday employment.
- **Forecast:** Total employment in the metro will increase by 1.7 percent in 2008, a gain of 34,200 positions. Over 14,000 new Trade positions will be added by the end of 2008, an increase of 3.5 percent.

Housing



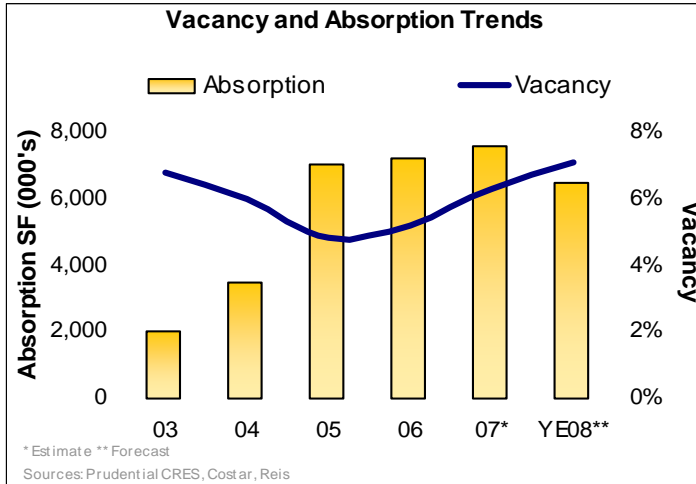
- Median home values for existing single family homes in the Phoenix metro is \$256,975, a seasonal decrease of 2.5 percent from the previous quarter. In a year-over-year comparison prices have decelerated by 1.2 percent, from \$260,000.
- Existing single family home sale velocity has slowed to 11,600 sales in the third quarter of this year, a 28 percent decrease from the previous year. In a year-to-date comparison, single family permits have decreased by 21 percent to 25,332 issued.
- **Forecast:** We estimate 2007 home sales to have decreased by 22 percent over the previous year to approximately 52,000 to 55,000 for existing single family homes. The housing market is anticipated to begin its recovery in the first quarter of 2009. Asset values will rise when excess supply and demand are balanced.

Submarket Trends

Submarket	Vacancy			Effective Rent		
	3Q 07	4Q 07	Bps Change	3Q07	4Q07	Pct Change
Central-Northeast Phoenix	5.5%	6.0%	50	\$18.34	\$18.40	0.3%
Mesa-Chandler-Gilbert	7.7%	8.0%	30	\$15.79	\$15.97	1.1%
North Scottsdale-Paradise Valley	4.9%	5.5%	60	\$22.12	\$22.16	0.2%
Northwest Phoenix-Glendale	5.5%	6.2%	70	\$15.78	\$15.89	0.7%
Tempe-South Phoenix	5.7%	5.5%	-20	\$16.60	\$16.76	1.0%
West Phoenix-Southwest Valley	5.9%	6.7%	80	\$14.20	\$14.32	0.8%
Phoenix Metro	5.8%	6.3%	50	\$17.14	\$17.27	0.8%

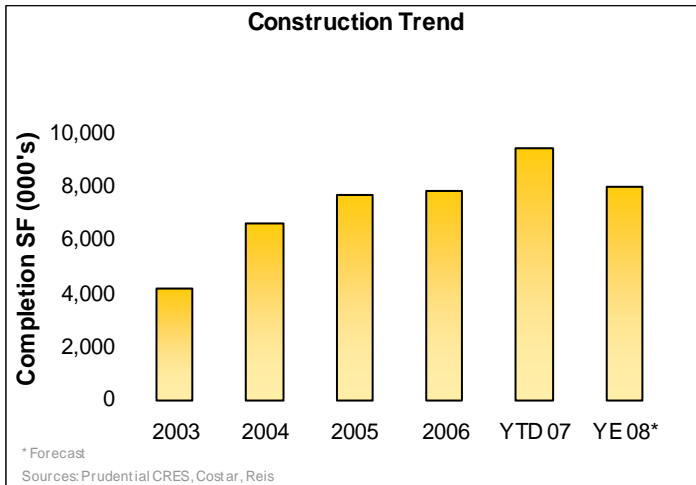
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Vacancy & Absorption



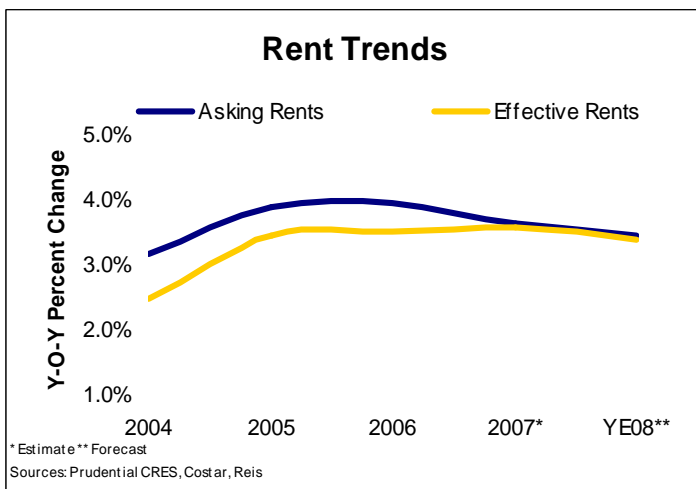
- Vacancy rose by 50 basis points in the fourth quarter of this year and has risen by 80 basis points over the past 12 months.
- Absorption is reported at 2.1 million square feet for the fourth quarter. In a year-to-date assessment, absorption has totaled approximately 7.6 million square feet.
- **Forecast:** Retail vacancy will increase by another 70 basis points by the end of 2008. While many new residential developments remain unoccupied, new retail space may sit vacant a little longer. It may be wise for developers to gain tenant commitment prior to breaking ground in 2008 until the housing market corrects itself. Absorption is expected to total approximately 6 million square feet by the end of 2008.

Construction



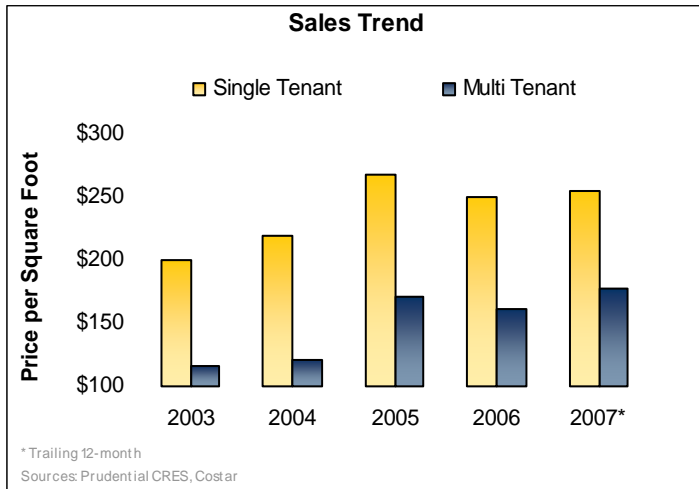
- Retail development rose to new heights in 2007, adding 9.5 million square feet in 2007. Development included 4.3 million square feet of power center space, 1.7 million square feet of strip centers, and 1.6 million square feet of neighborhood and community centers.
- Currently there is 8.8 million square feet under way with an additional 15.8 million square feet in the planning phase. Pinal County harbors 3.9 million square feet of planned development while the West-Southwest Valley submarket has 1.8 million square feet in the pipeline.
- **Forecast:** Retail developers are expected to increase inventory by almost 8 million square feet by year-end 2008, which accounts for almost 5 percent of the total retail inventory. Developers will continue to realize upside potential in in-fill locations.

Rents



- Asking rents have increased by 1 percent in the fourth quarter to \$19.28 per square foot, and have advanced by 3.7 percent in a year over year assessment. Effective rents rose by 3.6 percent for the year, and 0.8 percent for the quarter to \$17.27 per square foot.
- Rent increases have started to slow due to the glut of new space coming on line. Rents for unanchored strip centers have started to decline. Landlords looking to move space have become more apt to work with tenants ready to occupy space.
- **Forecast:** Landlords are anticipated to increase asking rents to \$19.95, a 3.5 percent increase in 2008. Effective rents will improve by 3.4 percent to \$17.86 per square foot. Building owners are expected to raise concessions in 2008 in an effort to attract tenants. Rents for new retail space may be in direct competition with older well-placed centers that are currently unoccupied, but offer more affordable rates.

Sales



- Sales activity amongst multi-tenant assets continues to decelerate. Transaction velocity has slowed by 30 percent on a trailing-12 month basis. During the same period, median sales prices improved by 9.2 percent to \$177 per square foot.
- Single tenant building sales rose slightly from the previous 12-month period. The median price per square foot among single-tenant assets increased by 1.6 percent over the past 12 months to \$254 per square foot. Currently, cap rates are reported between 6.7 and 7 percent. At the same time last year, cap rates were approximately 7 percent.
- **Forecast:** As crediting institutions have tightened their lending standards, some investors may have taken a “wait-and-see” attitude. Retail assets will continue to provide solid returns in 2008, attracting buyers with cash as opposed to those needing financing. The first half of 2008 will report sluggish sales and pick-up again in the latter part of the year while sellers adjust to new pricing structures.

Recent Retail Sales Transactions

Multi-Tenant

Property Name	Property Address	City	GLA	\$/PSF	Sale Price	Type
Santa Fe Square Shopping Center	1107 South Gilbert Road	Mesa	263,101	\$108.32	\$28,499,100	Community Center
Lindsay Square Plaza	870 North Williams Field Road	Gilbert	47,900	\$283.53	\$13,581,087	Strip Center
Marketplace Square	1420-1442 East Chandler Boulevard	Phoenix	29,726	\$265.76	\$7,899,982	Strip Center
Western Skies Village	1534 East Ray Road	Gilbert	24,100	\$319.50	\$7,699,950	Strip Center

Single-Tenant

Property Name	Property Address	City	GLA	\$/PSF	Sale Price	Type
Bank	1101 East Florence Boulevard	Casa Grande	5,142	\$666.08	\$3,424,983	Bank
X-Tapa Joe's	7500 East Pinnacle Peak Road	Scottsdale	6,600	\$318.18	\$2,099,988	Restaurant
Buffalo Wild Wings	6558 East Superstition Springs Boulevard	Mesa	5,700	\$345.08	\$1,966,956	Restaurant
Starbucks Coffee	4985 North Sunland Gin Road	Eloy	2,000	\$804.69	\$1,609,380	General Freestanding
La Presa Mexican Restaurant	4333 West Thomas Road	Phoenix	2,125	\$517.65	\$1,100,006	Fast Food
Burger King	1210 North Scottsdale Road	Tempe	3171	346.89	\$1,099,988	Fast Food



Prudential

CRES Commercial Real Estate

Prudential CRES
Commercial Real Estate Solutions
David Illsley – Managing Director
Shara M. Galonsky – Director of Research

14287 North 87th Street, Suite 220
Scottsdale, Arizona 85260
Ph – 480-451-9077

Agents

Ron Akridge – Associate VP
Sheila Bale – Associate VP
Jake Cramer – Commercial Advisor
Andrea Davis – Senior Advisor
Stacie Harrison – Senior Advisor
Paul Honeycutt – Associate VP
Jennifer Keeler – Senior Advisor
Larry Miller, Jr. – Senior Associate

Matt Leonard – Associate VP
Barbara Lloyd – Associate VP*
Kathleen Morgan – Senior VP*
Nick Pelusio – Senior VP
Jeff Tricco – Associate VP
Trisha Talbot – Senior Associate*
Mike Uhrich – Associate VP
Angie West – Senior Advisor

CRES Appraisal

Dan Paulus – MAI, President
David Blanco – Analyst

*CCIM

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