



Office Real Estate

Atlanta Area Market Review

FIRST QUARTER 2009

Market Up Close

- The average asking rate for Atlanta office space dipped during first quarter to \$20.66 per rentable square foot (rsf). Asking rents fell by a little more than one percent in both Class A and Class B space, while rents rose slightly in the much smaller Class C market. This year landlords are adding more lucrative economic incentives for tenants, such as free rent and tenant improvement allowances, while still trying to keep face rents as high as possible.
- While much has been written lately about overdevelopment in metro Atlanta, it should be pointed out that the vast majority (more than 80 percent) of all new office space under construction is located in Class A trophy towers going up in Buckhead and Midtown. If “all real estate is local,” then most deals in the market will be largely unaffected by these upcoming space additions. High-end space users in those two submarkets, of course, could benefit greatly from the excess space coming to market in the next few months.

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The forces impacting the economy nationally continued to affect Atlanta’s office market in the first quarter of 2009. The downsizing of corporate payrolls pushed Atlanta’s office vacancy to 17.0 percent, while those companies not reducing their staffs were reluctant to make new space commitments unless absolutely necessary. Uncertainty is a hallmark of short-term economic forecasts, while long-term expectations for recovery remain high. As such, this is clearly a year of waiting for most firms, but opportunities abound for those firms able and willing to explore their space options.

Atlanta Market Summary

As 2008 drew to a close, it was clear to many that Atlanta’s office market was poised for a bumpy ride in 2009. With unemployment rising and companies considering layoffs, fully four million square feet of new office product was under construction, leading all but the most optimistic to expect a significant downturn in absorption as vacancy rates soared. As of the end of first quarter 2009, it’s clear that such worries were somewhat premature, if not in fact exaggerated.

First quarter saw minimally positive net absorption across metro Atlanta, with vacancy rising by only a tenth of a point. What’s clear in examining the past three quarters of activity is that office users are holding their breath, neither moving forward with expansion plans nor abandoning space in a panic. Businesses that are not in distress are “keeping their powder dry” while they wait for the picture to become clearer. Still, the market has responded to current conditions, with new construction all but halted across the metro area. Quoted rent rates are also on the decline, reflecting newfound aggression on the part of landlords in search of new tenants.

Though first quarter saw no significant new office deliveries, there remain approximately 3.9 million

square feet of space under construction around the city - with two-thirds of that space expected to come online within the next six months. (Following a breather at year’s end, the remainder is due for completion in the first quarter of 2010.) As this space is added to existing inventory, we can expect vacancy to rise in the affected submarkets.

Atlanta Market Outlook

There’s no doubt that 2009 will be a challenging year for the Atlanta office market, as for most areas of the country. The second half of 2009 may bring some improvement, but demand for office space is expected to remain subdued during the year and local unemployment may yet rise further before the recovery begins.

Rents will remain under pressure in 2009 as Atlanta office owners strive to differentiate themselves from competitors and attract the finite number of tenants in the market. As such, this year constitutes the very definition of a “tenant’s market.” Landlords will continue to focus on tenant retention in order to retain cash flows for their properties. The incentives offered to tenants will also ramp up as landlords work to extend and renew existing leases. As such, the two contrasting watchwords for the remainder of the year are “uncertainty” and “opportunity.”

Submarket	# of Bldgs	Rentable Inventory (SF)	Direct Vacant Space (SF)	Total Vacant Space (SF)	Vacancy Rate	Net Absorption	Deliveries	Under Construction	Quoted Rental Rates
Buckhead	113	17,768,557	2,399,714	2,732,387	15.4%	(18,194)	0	1,980,731	\$26.13
Central Perimeter	266	28,249,982	4,507,439	5,118,295	18.1%	(238,052)	0	0	\$21.35
Downtown Atlanta	130	23,435,253	3,721,944	4,016,545	17.1%	47,765	0	0	\$20.02
Midtown Atlanta	127	18,183,883	2,441,478	2,908,284	16.0%	39,610	0	1,253,277	\$23.75
North Fulton	335	24,879,348	3,866,402	4,480,597	18.0%	(50,234)	24,000	117,350	\$18.33
Northeast Atlanta	371	18,189,868	3,439,770	3,755,464	20.6%	(34,088)	0	108,700	\$17.86
Northlake	377	18,747,857	1,893,187	1,962,631	10.5%	80,946	40,400	62,400	\$18.30
Northwest Atlanta	424	31,719,174	5,138,927	5,742,323	18.1%	66,382	81,442	90,934	\$19.47
South Atlanta	229	9,721,315	1,705,644	1,773,833	18.2%	84,487	36,800	329,388	\$18.98
West Atlanta	46	1,796,774	275,902	283,063	15.8%	36,103	0	0	\$16.20
Totals	2,418	192,692,011	29,390,407	32,773,422	17.0%	14,725	182,642	3,942,780	\$20.66

Sources: GVA Advantis Research, CoStar

DEVELOPMENT NEWS

As noted elsewhere in this report, the bulk of Atlanta’s signature development at this time is going on in Buckhead and Midtown:

The 2.5 million-square-foot, mixed-use, 12th & Midtown project, developed by Selig Enterprises and Daniel Corp., is currently underway - with half of that space projected to consist of Class A office product; the remainder will include hotel, residential, and retail space.

Also in Midtown, the third office building at Atlantic Station is nearing completion and being marketed by Carter. 271 17th Street is approximately 45 percent leased.

Buckhead’s four current projects include: Cousins’ next building at its Terminus project, Terminus 200; Tishman Speyer’s first ground-up development in Atlanta, Two Alliance Center; Crescent Resources’ Phipps Tower, projected to be the last one completed of the four and due in 2010; and 3630 Peachtree, a joint mixed-use project at the north end of Buckhead with the office portion being marketed by Pope & Land.

SUBMARKET OVERVIEW

Atlanta Submarkets

During the first quarter of 2009, Atlanta’s Downtown submarket saw vacancy decline slightly to 17.1 percent; this was the seventh consecutive quarter of declining vacancy here, as Downtown arguably experienced its downturn earlier than most Atlanta submarkets. Following a number of moves out of the submarket in the middle of the decade (primarily law firms relocating to Midtown), Downtown has benefitted more recently from moderate occupancy growth combined with a lack of new development. In addition, rents here have stabilized around an average of \$20.00 per rsf in the past three quarters. While Downtown can not exactly be characterized as booming, this submarket is certainly holding its own so far in 2009.

Atlanta’s Buckhead submarket is a different story. Historically Atlanta’s hub for finance and insurance firms, Buckhead has attracted national notice recently for the significant amount of development currently going on. In a submarket that traditionally absorbs 300,000 - 400,000 square feet of net new occupancy in a good year, Buckhead currently has nearly two million square feet of new space under construction in four new Class A towers. This is taking place during a time when many of this submarket’s tenants are downsizing and putting space up for sublease. As such, Buckhead’s property owners are forced to be more aggressive in attracting space users, and quoted rents here fell for the fifth consecutive quarter to reach an average of \$26.13 per rsf at the end of first quarter. Net absorption remains essentially flat here as well. Buckhead’s reputation and amenities ensure that the new space will eventually find tenants, but this submarket may have a rocky year or two ahead.

The Midtown office submarket also is experiencing some trophy tower construction at this time, with 1.25 million square feet under development in two buildings. Still, positive though anemic absorption brought this submarket’s vacancy down slightly during first quarter to 16.0 percent. The spacing of upcoming new deliveries here (one in second quarter, the other in early 2010) may allow Midtown to absorb this new supply with less stress than Buckhead, even with only moderate demand. Quoted rents slipped a bit here during the quarter, reaching an average of \$23.75 per rsf; this figure is still well within the range of rents here over the past two years.

Quoted rents in the Central Perimeter submarket dipped again this quarter, averaging \$21.35 per rsf. This submarket has weathered three consecutive quarters of negative absorption, losing nearly 250,000 square feet of net occupancy in first quarter alone. As a result, vacancy here rose to 18.1 percent - one of metro Atlanta’s higher rates - from 15.7 percent just one year ago. Like Buckhead, this submarket’s prime office users have been hit hard by the economic downturn, but this area remains a choice location for regional headquarters and other offices, and will likely recover along roughly the same timeline as the economy in general..

The North Fulton submarket also saw vacancy rise, reaching 18.0 percent this quarter from a recent low of 14.9 percent this time last year. Following a strong fourth quarter, absorption was again negative in first quarter, with just over 50,000 square feet in net losses. Rents here reached their lowest point in more than a year, averaging \$18.33 per rsf. Development is not a

Property / Address	Submarket	RSF	Sales Price	Price Per Foot	Buyer
BellSouth / 675 West Peachtree St.	Midtown	1,794,677	\$345,000,000	\$192.24	Icahn Enterprises
Lakeside Commons I	Central Perimeter	519,730	\$102,800,000	\$197.80	Intercontinental
Three Glenlake	Central Perimeter	356,000	\$100,600,000	\$282.58	Wells REIT II
BellSouth Lenox Park	Buckhead	980,018	\$275,300,000	\$280.91	Wells REIT II

Sources: GVA Advantis Research, CoStar, Real Capital Analytics

ATLANTA SUBMARKETS (CONTINUED)

major concern here at this time, so even moderate demand should pull the vacancy rate back into the mid-teens in coming quarters.

The Northwest submarket regained most of the occupancy in first quarter that it had lost during fourth quarter 2008, but the vacancy rate here remains unchanged at 18.1 percent. A few small office buildings were completed this quarter; indeed, development in the Northwest has been consistent of late -- never booming but never completely halted, either. Quoted rents here rose during first quarter to \$19.47 per rsf, but this figure is still well below this submarket's peak of \$19.79 recorded this time last year.

The story is less positive in the Northeast, where three consecutive quarters of negative net absorption have pushed the vacancy rate to 20.6 percent - metro Atlanta's highest. Low levels of development continue here as well, with a 100,000 square-foot property under construction, while another one was completed last quarter. Quoted rents continued to decline here following a brief foray over the \$18.00 mark last year; currently, rates average \$17.86 per rsf, slightly lower than this time last year when rates were rising. Historically, development runs ahead of demand here, which generally keeps the vacancy rate elevated. Still, this submarket continues to be attractive to space users in need of back-office, call center, or other space at an affordable price, and this is reflected in the willingness of developers and lenders to continue speculating in the area.

Investment Market Summary

The dramatic downturn in office investment sales nationally has certainly affected the Atlanta market as well, as office sales volume declined by fifty percent in the past year, while the number of buildings sold declined by even more. Still, both of these figures indicate a less severe decline in metro Atlanta than across the U.S. as a whole, where sales volume plunged by more than seventy percent.

Of course, some buildings are being successfully sold in Atlanta, with the greatest volume going to syndicators and private buyers. This reflects one counter-trend present in this economy: as with the leasing market, investors (and space users) with access to capital or credit have a wide variety of options available to them now. Anyone willing and able to finance a deal and close quickly can be fairly certain of finding an attractive offering from a motivated seller -- particularly because, due to the depressed sales environment, many of today's sellers are in distress. Sellers who don't have to dispose of properties now are inclined to wait for more favorable conditions after the investment market recovers. In the past few quarters, few of Atlanta's trophy towers or significant office properties have been put on the market, due to a still-sizable pricing gap between sellers and buyers.

The outlook for 2009 is filled with more questions than answers, with the best opportunities reserved for cash buyers chasing distressed properties. Still, higher-quality assets with strong credit tenants will remain in demand and should significantly outperform the general market in the coming months. As with leasing, those with the ability and willingness to swim against the prevailing tides will find a multitude of opportunities.

INVESTMENT SALES TOTALS

Market	Year-End 2005	Year-End 2006	Year-End 2007	Year-End 2008
Number of Transactions	187	221	221	186
Total Sales Volume	\$2.3 Billion	\$4.4 Billion	\$3.7 Billion	\$1.6 Billion
Average Price Per Foot	\$141.54	\$166.27	\$152.57	\$148.94
Average Cap Rate	8.2%	7.4%	7.7%	7.9%

Sources: GVA Advantis Research, CoStar, Real Capital Analytics

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