

StudleyReport

STUDLEY OFFICE MARKET AND SPACEDATA REPORT

MARKET HIGHLIGHTS

AVAILABILITY RATES REMAIN STABLE

Downtown Chicago's overall availability rate stood at 17.2%, down by 0.2 pp from last quarter but up by 0.8 pp from last year. The Class A rate, 18.5%, fell by 0.8 pp for the quarter but posted an increase of 0.7 pp for the year.

ASKING RENTS UP FOR THE QUARTER

Overall asking rent rose by 1.1% for the quarter to \$29.18. Class A asking rent also increased (+1.1% to \$31.36). Overall and Class A rents declined by 8.2% and 11.1%, respectively, from a year ago.

QUARTERLY LEASING DECLINES SHARPLY

Overall leasing activity totaled 1.1 million square feet, down by 41.9% for the quarter and 31.2% for the year. Trailing four-quarter volume, 7.2 msf, fell by 6.4% quarterly but registered an annual gain of 30.5%

CAPITAL MARKETS IMPROVE

Investment sales are picking up with six buildings sold and the pending sale of 300 N. LaSalle at a record-shattering \$503 psf.

Tenants Testing Market

Tenants were in "discovery mode" during the second quarter – leasing in Chicago's CBD retreated to subpar levels but several companies were exploring their options. With conditions still clearly favorable to tenants, more businesses were poised to capitalize on opportunities for significant savings. A number of companies with requirements exceeding 100,000 sf, most with lease expirations between 2012 through 2015, stuck their toes in the water.

Regional as well as national economic indicators did not change much – if anything, numbers took a negative turn in May and June. Wall Street slipped in the wake of the debt crisis in Greece, housing sales tumbled, jobs numbers were disappointing and household income languished. Office-using employment in the Chicago region has been erratic – increasing one month and declining the next. So far, the region has recovered about 3.0% of the total layoffs in office-using sectors during the recession, well below the national recovery rate of 7.3%. Of note, professional/business services employment has been increasing at a slow but steady pace since the start of the year, but financial services continues to shed jobs. In short, any hopes of a quick turnaround dissipated as the quarter progressed.

Completed transactions only reached 1.1 million square feet in the second quarter – 50.5% below the CBD's long-term historical average – but this volume of completed deals is not reflective of market activity. Within the next 12 months, many of the larger users circling their options will land, although many may ultimately renew or restructure their leases. Leases are still taking longer to complete because of rigorous due diligence and extensive precautions that have become a key part of ensuring that landlords will be able to follow through on lease agreements. Tenants also remain cautious in their decision-making. The market was quite fluid as a fair number of mid-sized firms moved forward with relocations, some involving expansions, to high-quality Class A properties. As a result, the Class A availability rate in the CBD registered its first significant decline since 2007, falling by 0.8 pp to 18.5%. Even so, the CBD still has more than 22.0 msf of space available for lease, 5.5 msf more than in late 2007 when supply was at its lowest point. Even if net absorption increased to an annual rate of 1.0 msf, the CBD still has several years of supply to absorb before availability would fall to the 10% range. Consequently, unless there are material changes to the economic environment, conditions should continue to favor tenants in the short term.

CLASS A TRANSACTION BAROMETER

	Under 50,000 sf	One Qtr Change	Over 50,000 sf	One Qtr Change
Average Term:	10 years	◀▶	10 years	◀▶
Concessions:				
Free Rent	10-15 months	◀▶	10-18 months	◀▶
Tenant Improvements	\$55-\$75/sf	◀▶	\$60-\$80/sf	◀▶
Other	Various	◀▶	Various	◀▶

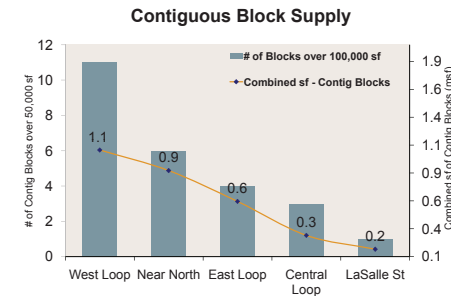
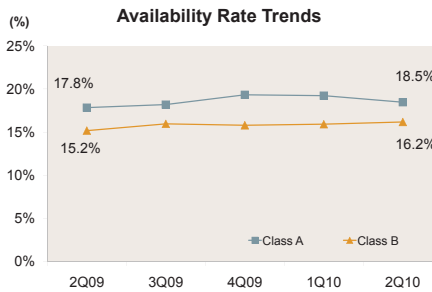
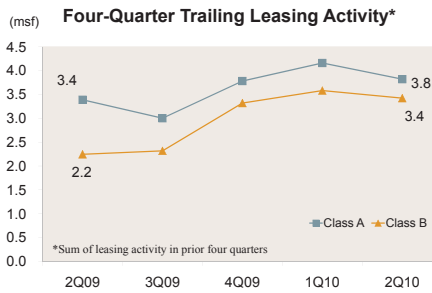
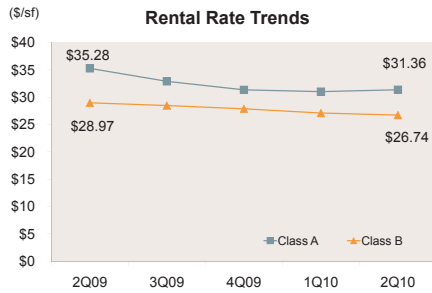
Outlook: Tenants looking for bigger blocks of space may have fewer options, but smaller and mid-sized tenants can select from a deep pool of space, giving them solid leverage to negotiate generous concessions.

CLASS B TRANSACTION BAROMETER

	Under 50,000 sf	One Qtr Change	Over 50,000 sf	One Qtr Change
Average Term:	7 years	◀▶	10 years	◀▶
Concessions:				
Free Rent	6-12 months	◀▶	8-15 months	◀▶
Tenant Improvements	\$45-\$65/sf	◀▶	\$55-\$70/sf	◀▶
Other	Various	◀▶	Various	◀▶

Outlook: Landlords in older Class A properties and Class B buildings have to extend ample tenant improvement allowances, free rent periods or discounted rents to stave off losses in their tenant rosters.

▲ Up ▼ Down ◀▶ Unchanged



Law firms accounted for many of the quarter's most notable leases. In the largest transaction of the quarter, Neal, Gerber & Eisenberg extended its lease on a short-term basis from 2017 to 2020, and in exchange the landlord took back a floor. In the West Loop, 500 W. Madison added two more law firms to its roster. Horwood Marcus & Berk agreed to a 29,000-sf lease, a notable expansion from the 20,000 sf it currently occupies at 180 N. LaSalle. Cleveland-based Ulmer & Berne LLP took 18,374 sf. Profits in the financial sector are not expected to match their stellar levels of 2009, but even so, smaller and mid-sized financial firms remained active. In one of the larger transactions of the quarter, and one of the only expansions, Brewer Investment Group signed a 30,919-sf lease at 303 E. Wacker. The wealth management advisory firm will relocate from approximately 18,000 sf at 200 S. Michigan. Also, Bank Leumi announced a lease that would move the firm to 10,071 sf at 1 N. LaSalle.

Gap in Expectations Narrowing

As Chicago-area businesses and landlords have come to terms with the "new normal" of subpar growth, the gap between the expectations of tenants and landlords has narrowed. More landlords have accepted what is required to retain or attract tenants, and tenants are becoming more aware about what landlords can offer and then deliver. Recognizing that tenant retention is critical, more landlords have been willing to discuss early renewals and restructures. Tenants shedding some of their space have extended their lease term in compensation for landlords' recapture of unneeded space. Neal, Gerber's lease was a case of such "give and take."

Conversations about similar trade-offs are becoming more commonplace. Companies with larger leases rolling over in the next few years have been intrigued by news of these leases that clearly offer significant long-term savings. The list of firms actively assessing the market for substantial blocks of space includes Motorola (400,000 sf), Citadel (300,000 sf), advertising firm Foote Cone & Belding (200,000 sf), PriceWaterhouse Coopers (200,000 sf) and Sonnenschein, Nath & Rosenthal, which is looking for about 150,000 sf. While noteworthy, this new set of requirements probably won't do much to absorb the CBD's excess space. Some of these firms will likely lease about the same amount of space as they currently occupy, and a few will shed space in the course of a renewal or relocation. Larger tenants currently have fewer major blocks of space to choose from but as some larger companies consolidate locations, the CBD's supply of bigger blocks may increase.

Competition in the West Loop

Smaller to mid-sized tenants willing to commit to a long-term lease are in a strong position. The recent addition of several blocks of desirable sublet space of between 20,000 sf and 50,000 sf in the West Loop piqued the interest of many companies. The West Loop accounted for more than half of this quarter's top leases as several mid-sized firms snatched sublet space off the market. For instance, Neutral Tandem Inc. sublet 27,555 sf of space at 550 W. Adams from USG Corp. Additionally, mobile marketing firm Vibes Media signed a 21,620-sf, 10-year lease at 300 W. Adams. Finally Hometown America renewed for 18,300 sf at 150 N. Wacker after testing the market.

MAJOR TRANSACTIONS

Tenant	Sq Feet	Address	Market Area
Neal, Gerber & Eisenberg	179,451	2 N LaSalle St	LaSalle Street
Travelers Cos.	80,000	161 N Clark St	Central Loop
General Services Administration	50,139	525 W Van Buren St	West Loop
Help at Home, Inc	48,000	1 N State St	East Loop
Jewish Federation	40,904	216 W Jackson Blvd	West Loop
Brewer Investment Group	30,919	303 E Wacker Dr	Michigan Avenue
Horwood Marcus & Berk	29,000	500 W Madison	West Loop
TCS Education System	29,000	350 W Mart Ctr	Near North
Neutral Tandem, Inc.	27,555	550 W Adams St	West Loop
Vibes Media, LLC	21,620	300 W Adams St	West Loop
Ticketmaster	20,667	550 W Van Buren St	West Loop
Regional Transportation Authority	19,920	175 W Jackson Blvd	West Loop
Hometown America	18,300	150 N Wacker	West Loop
IEG, Inc.	17,000	640 N LaSalle St	Near North
Peerless Network Inc.	13,586	222 S Riverside Plz	West Loop
Sum of Top 15 Leases	626,061	Sum of 2nd Qtr Leasing Activity	1.1 MSF

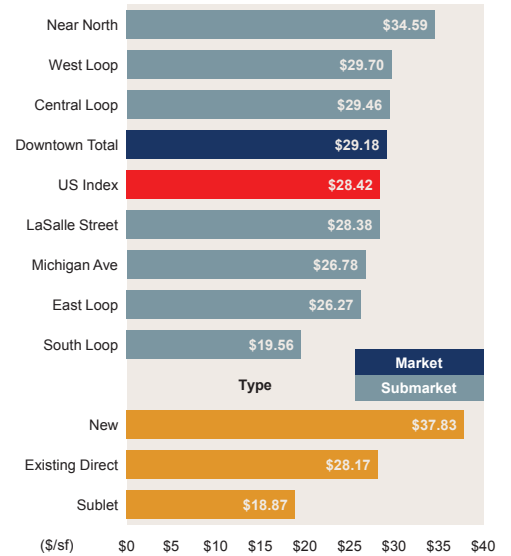
As a result of the growth in tenant activity, the West Loop's Class A availability rate dropped for the second quarter in a row, falling from 19.1% to 18.1%. The West Loop registered 2.9 msf of Class A leasing in the last four quarters and accounted for 76.2% of the CBD's Class A volume.

Completing a lease or a sale is not as difficult as it was a few quarters ago but all of the parties involved are still encountering obstacles. Tenants must perform rigorous due diligence on the capital structure of a property and incorporate protective clauses in their leases. The high volume of looming CMBS maturities remains a concern. The restructuring of the \$1.4-billion loan underlying Tishman Speyer's Downtown portfolio was reassuring – any other outcome would have deepened the concerns surrounding “zombie buildings.” Other properties such as 200 S. Wacker have missed key mortgage payments, lost key pieces of their tenant roster and do not have the capital to cover expenses or sign new leases, and this problem is not going to dissipate any time soon.

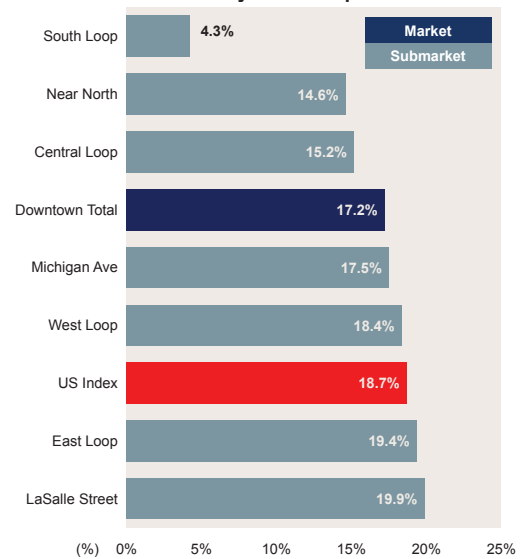
Improvement in Investment Sales

The outlook for investment sales improved during May and June. So far, the investment sales market seems to have averted the worst-case scenario many envisioned just a few months ago. In June, California-based KBS Realty Advisors agreed to acquire 300 N. LaSalle for approximately \$625 million. KBS will pay about \$503 psf for the 1.3-msf tower – eclipsing the previous high-water mark of \$422 psf paid for 1 S. Dearborn in 2006. The property garnered this high price on the basis of its being 95% leased to creditworthy tenants such as Kirkland & Ellis, and there are very few truly similar high-caliber assets on the market. Investors with ample funds to disburse have been surveying major U.S. CBDs for high-quality assets. Class A properties with secure cash flow in principal CBDs such as Boston, Manhattan and Dallas have commanded high prices and low cap rates over the last few months. In Chicago, though, this is the first transaction of such magnitude since the market collapsed. There remains ample capital on the sidelines looking for a safe return on investment and a dearth of quality assets being marketed, and fundamentals are starting to work in favor of sellers. The recent turnaround is pushing other landlords to put their properties on the market. For example, Mesirow Financial is marketing 353 N. Clark. Additionally a consortium lead by Mark Karasick is reportedly close to putting 550 W. Jackson on the market, and has lined up Cornerstone Realty to sell the asset. Properties with extensive vacancies continue to incur a stiff penalty. In May, Prime Group Realty Trust announced the \$72.25-million sale of 180 N. LaSalle to New-York based Berkley Properties. The building, which has a vacancy rate of just above 30.3%, sold for slightly less than \$95 psf and nearly \$50 million below the \$124 million Younan Properties had agreed to pay for the building in the Fall of 2008.

Overall Rental Rate Comparison



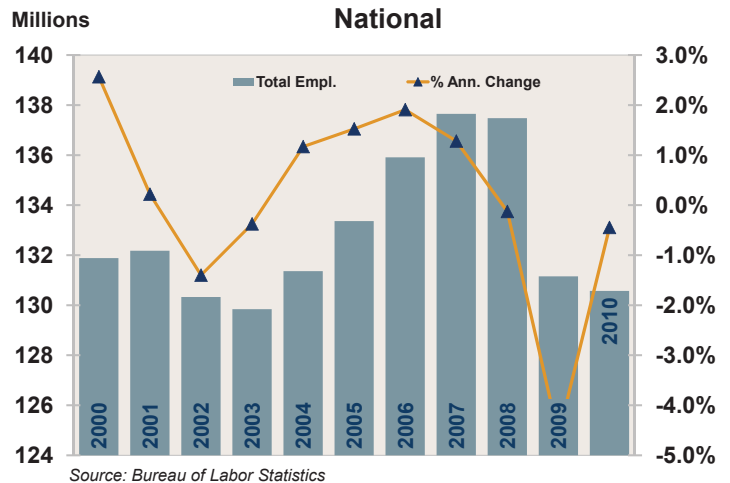
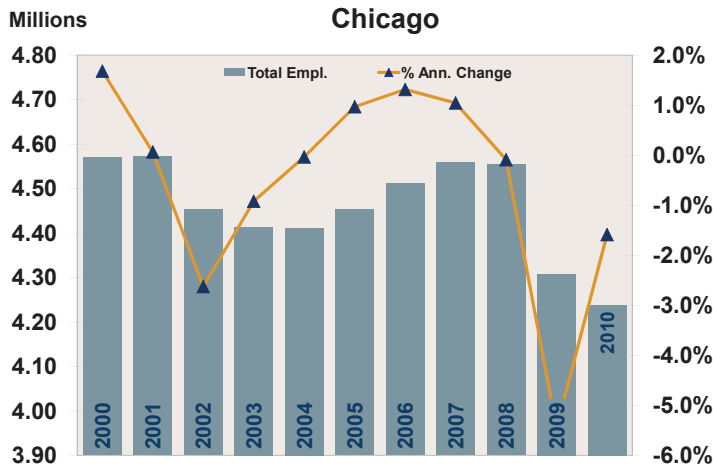
Availability Rate Comparison



ABOUT OUR FIRM

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EMPLOYMENT TRENDS



MARKET SNAPSHOT: 2Q 2010

MAP	SUBMARKET	TOTAL Inventory SF (1,000's)	LEASING & ABSORPTION		AVAILABLE SF				AVAILABILITY RATE				ASKING RENTS PER SF			
			LEASING- Last 12 Mos	Qtrly Net Abs	This Qtr	% Change from Last Qtr	Last Qtr	1 Yr Ago	This Qtr	pp Change from Last Qtr ⁽¹⁾	Last Qtr	1 Yr Ago	This Qtr	% Change from Last Qtr	Last Qtr	1 Yr Ago
1	West Loop	45,663	3,660	-589	8,391	-2.9%	8,641	8,183	18.4%	-0.5%	18.9%	17.9%	\$29.70	0.7%	\$29.50	\$33.24
	West Loop - Class A	29,761	2,910	-416	5,377	-5.6%	5,698	5,371	18.1%	-1.1%	19.1%	18.0%	\$31.08	2.5%	\$30.33	\$35.17
2	LaSalle Street	15,145	604	-137	3,012	3.1%	2,922	2,711	19.9%	0.6%	19.3%	17.9%	\$28.38	1.1%	\$28.06	\$30.71
	LaSalle Street - Class A	4,734	334	-83	938	-3.1%	968	939	19.8%	-0.6%	20.4%	19.8%	\$30.23	-2.6%	\$31.03	\$33.38
3	Central Loop	18,265	1,080	199	2,775	1.0%	2,748	2,705	15.2%	0.1%	15.0%	14.8%	\$29.46	1.4%	\$29.04	\$29.99
	Central Loop - Class A	9,086	240	21	859	-7.3%	927	900	9.5%	-0.7%	10.2%	9.9%	\$35.14	6.0%	\$33.15	\$35.74
4	East Loop	21,101	1,139	188	4,085	-7.8%	4,428	3,735	19.4%	-1.6%	21.0%	17.7%	\$26.27	0.2%	\$26.21	\$29.42
	East Loop - Class A	6,083	163	-19	1,787	-3.7%	1,856	1,395	29.4%	-1.1%	30.5%	22.9%	\$27.58	1.4%	\$27.20	\$33.74
5	Michigan Avenue	7,309	138	-29	1,280	3.0%	1,243	1,374	17.5%	0.5%	17.0%	18.8%	\$26.78	-2.2%	\$27.39	\$31.97
	Michigan Avenue - Class A	4,354	52	-75	811	-0.9%	818	858	18.6%	-0.2%	18.8%	19.7%	\$26.67	-6.9%	\$28.64	\$33.17
6	Near North	17,212	614	-622	2,519	1.7%	2,478	2,405	14.6%	0.2%	14.4%	14.0%	\$34.59	4.4%	\$33.13	\$34.34
	Near North - Class A	6,537	120	-589	1,406	2.4%	1,373	1,336	21.5%	0.5%	21.0%	20.4%	\$37.30	-0.6%	\$37.53	\$38.90
7	South Loop	4,310	5	-5	184	143.2%	76	70	4.3%	2.5%	1.8%	1.6%	\$19.56	-3.0%	\$20.16	\$20.13
	South Loop - Class A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
1-7	DOWNTOWN CHICAGO TOTAL	129,005	7,240	-995	22,245	-1.3%	22,535	21,183	17.2%	-0.2%	17.5%	16.4%	\$29.18	1.1%	\$28.86	\$31.80
	DOWNTOWN CHICAGO TOTAL - Class A	60,553	3,819	-1,161	11,178	-4.0%	11,640	10,800	18.5%	-0.8%	19.2%	17.8%	\$31.36	1.1%	\$31.02	\$35.28

(1) Percentage point change for availability rates.

Unless otherwise noted, all rents quoted throughout this report are average asking gross (full service) rents psf.

The information in this report is obtained from sources deemed reliable, but no representation is made as to the accuracy thereof. Statistics compiled with the support of The CoStar Group.

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