



Swisher Commercial 2006 Year-end Office/Flex Vacancy Report

David Hamilton, CCIM
John Swisher III
Ronald Dankert
Douglas Smith, CCIM
Barton Wise

John Evans
Tony Capraese
Paul Bidwell, MAI, CCIM
Reynold Hendrickson

Gretchen Driskell
Mark Buerkle
Larry Zahn
Willem van Reesema

Enclosed is **Swisher Commercial's** fourteenth annual survey of vacancy rates for office and flex space in the Ann Arbor area. This report will help you better understand the current market and assist you in planning your real estate decisions for the future. We surveyed **299 buildings** of 3,000 square feet (sf) or larger, totaling almost **11.6 million sf**. Our report includes a breakdown of vacancy rates by sub-market and charts the vacancy trends over the last fourteen years.

As of December 31, 2006, the total market vacancy rate, including office and flex space, was 14.69%, 2% higher than one year ago. This said, most of the submarket areas actually either improved slightly or remained unchanged. The major increases in vacancy in two submarket areas were due, in large part, to a few larger vacant buildings being added to the market.

ANALYSIS BY SUBMARKET

Compared to December 31, 2005, the South and East office submarket areas were relatively unchanged, while the vacancy rates for the South flex, West flex, and the Clark-Golfside Medical Area (CGMA) office space declined. The North office and Downtown office area vacancy rates increased significantly. See the attached vacancy rate analysis for the precise vacancy rates for these areas.

The North office area had the largest increase in vacancy, from 6.96% twelve months ago to its current 17.29%. This large jump shouldn't be interpreted as a widespread weakness in the North office area. It is almost entirely caused by increased supply due to the construction of nearly 200,000 sf at the Earhart Corporate Center and 25,000 sf at 201 Depot. These two properties make up over half of the total vacancy in the North office area and account for most of the increase in vacancy in this sector. On the other hand, the failure of these buildings to pre-lease does indicate soft demand for new space.

The East office market remained basically flat at 12.46%. This market traditionally caters to small office users. Even though leasing activity this year was slow, landlords seemed to do a better job of retaining existing tenants. The spectacular growth in the Washtenaw Avenue retail development could have a positive affect on the East office market.

Surprisingly, the South office area remained the same, which is contrary to Swisher broker's instinct that the South office market would strengthen in 2006. Further study of the market statistics revealed that the vacancy rate for multi-story Class A office buildings in the South office area is indeed lower - under 8%; notably, the 777-789 Eisenhower office complex and the Burlington Office Center, two of the larger office complexes reported zero vacancy. But the remaining office buildings that are part of the South area continued to struggle, offsetting the strength of the Class A buildings, leading to almost no net change in the last year for this area as a whole.

After six years of increasing vacancies in the flex market, both the South flex area and the West flex area vacancy rates decreased. The South flex rate decreased from 18.2% to 17.01%, while the West flex rate decreased from 8.57% to 6.08%, compared to December of 2005. Does this mean that the loss of tenants for Ann Arbor's high tech buildings has finally hit bottom? A single dip in the statistics doesn't tell the whole story, so we look forward to Swisher's 2007 Mid-year report to see if the trend continues.

The West office vacancy rate increased from 5.77% to 8.12%, while the CGMA vacancy decreased from 8.51% to 2.16%. While both show what appears to be measurable differences, they are both of limited statistical significance due to the small sample size of each area.

The Downtown Ann Arbor vacancy rate increased significantly to 15.67% from 12.49% in December 2005. The 60,000 sf Tally Hall building, which was reported to us as "leased" but "unoccupied" over recent years, finally had its lease to a non-occupying tenant end and is now reported as vacant. This statistical adjustment



Swisher
COMMERCIAL

208 E. Washington Street, Ann Arbor, MI, 48104

tel: 734.663.0501 fax: 734.663.0316

Building relationships.

www.swishercommercial.com

117 S. Evans Street, Tecumseh, MI, 49286

tel: 517.424.7080 fax: 517.424.7298

accounts for the 3% change in the vacancy rate downtown. Taking into account Google's commitment to rent 80,000 sf downtown at the McKinley Towne Centre starting in 2007, there is room for optimism for the downtown market regardless of the new statistically higher vacancy rate.

SUBLEASE SPACE

The vacancy rates in this report do not include suites available for sublease. However, **Swisher Commercial** still tracks this important market component. Similar in scale to last year we have identified approximately 115,000 sf of sublease space available in the market. This is a far cry from 2002, 2003 and 2004 when the market had twice the sublease space available.

NEW CONSTRUCTION

New construction added approximately 270,000 sf of available office space to the market in 2006, plus our survey added 100,000 sf of office space as the TCF headquarters downtown was converted into multi-tenant space as the McKinley TownCenter. We are anticipating that 2007 new construction will bring over 200,000 sf more to our survey, depending on construction schedules. New buildings may include:

- A 34,000 sf office building at the Valley Ranch Business Park
- The completion of 120,000 sf of office space at the South State Executive Park
- At Miller Road & M14, the Forest Cove Office Park will build a new 16,000 sf office building.
- The completion of 2395 Oak Valley, offering 10,000 sf of office space for lease.
- The Dakota building on West Stadium with 30,000 sf of medical/office space.

LEASING DEMAND

Demand for lease space in 2006 was at times eerily slow; brokers talked about how few phone calls were coming in. But at other times, particularly in the last four months of the year, activity jumped, with numerous small and medium size leases being secured as well as the headline 80,000 sf lease with Google. Those tenants out looking for new space seemed to be exercising caution and financial care. Rent concessions and shorter lease lengths were common. The question looking forward to 2007 is how well the market can absorb the new office buildings added to the North and Downtown sectors as well as those planned for completion (listed above).

According to published reports in Business Review (November 23-29, 2006), the experts continue to predict difficult economic conditions for Michigan in the near future, but true to its reputation, Ann Arbor is a bright spot of activity and optimism.

SALES ACTIVITY

Industrial and office building sales activity at Swisher Commercial have continued at a steady pace since 2003. Sales of campus apartments, which had been trading hands at Cap rates of 5% or lower (and Gross Rent Multipliers of 10.5 or higher) seem to have slowed. An increase in mortgage rates, returning vigor in the stock market, and general deterioration of the economic climate in southeast Michigan probably all contributed to a slowdown in the sales of both user and investor properties in the Ann Arbor area. **Swisher Commercial will be releasing its annual Cap Rate Report on January 17th at the Ann Arbor Chamber's Morning Edition event at Weber's Inn.** It will be placed on the Swisher website (www.swishercommercial.com) shortly thereafter.

Swisher Commercial is dedicated to helping our clients make informed real estate decisions. Our brokerage efforts continue to yield creative solutions that culminate in successful real estate transactions. We have assembled the largest and most experienced team of commercial real estate professionals in Washtenaw County. We understand the greater Ann Arbor market including Ypsilanti, Saline, Chelsea and Dexter, Lenawee and Jackson Counties, and are committed to serving the long-term needs of the business community. We look forward to assisting you with your lease, purchase/sale, investment, property management and advisory needs in the future.

Feel free to contact **Swisher Commercial** at (734) 663-0501, visit our website and weblog at www.swishercommercial.com, or e-mail us at info@swishercommercial.com if you have any questions or suggestions.



208 E. Washington Street, Ann Arbor, MI, 48104

tel: 734.663.0501 fax: 734.663.0316

Building relationships.

www.swishercommercial.com

117 S. Evans Street, Tecumseh, MI, 49286

tel: 517.424.7080 fax: 517.424.7298



Swisher Commercial 2006 Year-end Office/Flex Vacancy Report

ANN ARBOR AREA YEAR ENDING DECEMBER 31, 2006

	Area	# Blds	Gross SF	Vacant SF	Vac %	YE 2005	% Chg.
OFFICE	Downtown	71	1,680,357	263,369	15.67%	12.49%	3.18%
	North	36	2,446,078	423,032	17.29%	6.96%	10.33%
	East	37	688,511	85,811	12.46%	12.51%	-0.05%
	CGMA	8	472,349	10,199	2.16%	8.51%	-6.35%
	South	68	3,337,788	486,965	14.59%	14.58%	0.01%
	<u>West</u>	<u>15</u>	<u>322,950</u>	<u>26,214</u>	<u>8.12%</u>	<u>5.77%</u>	<u>2.35%</u>
	Total	235	8,948,033	1,295,590	14.48%	11.28%	3.20%
FLEX	South	54	2,241,229	381,196	17.01%	18.20%	-1.19%
	<u>West</u>	<u>10</u>	<u>384,427</u>	<u>23,390</u>	<u>6.08%</u>	<u>8.57%</u>	<u>-2.48%</u>
	Total	64	2,625,656	404,586	15.41%	16.80%	-1.39%
OFFICE & FLEX	Downtown	71	1,680,357	263,369	15.67%	12.49%	3.18%
	North	36	2,446,078	423,032	17.29%	6.96%	10.33%
	East	37	688,511	85,811	12.46%	12.51%	-0.05%
	CGMA	8	472,349	10,199	2.16%	8.51%	-6.35%
	South	122	5,579,017	868,161	15.56%	16.12%	-0.56%
	<u>West</u>	<u>25</u>	<u>707,377</u>	<u>49,604</u>	<u>7.01%</u>	<u>7.31%</u>	<u>-0.29%</u>
	Total	299	11,573,689	1,700,176	14.69%	12.62%	2.07%

ASSUMPTIONS

- Area:** City of Ann Arbor plus Scio, Pittsfield & Ann Arbor Twps. North includes Plymouth Road corridor. East includes Washtenaw, Packard and Carpenter Rds. South includes S. Industrial, S. Main, S. State, Briarwood and airport areas. West includes W. Liberty and Jackson Road areas. CGMA is the Clark-Golfside Medical Area; McAuley campus and the Huron River Drive/Golfside-Clark area.
- Buildings:** Includes all identified non-owner-occupied buildings over 3,000 SF.
- Flex:** Defined as high-bay type buildings, often combining office, high-tech, research, warehouse & similar.
- % Change:** A negative denotes a decreasing vacancy rate. Calculation is YE 2006 rate less the YE 2005 rate.

