INDUSTRIAL INSIGHT

A Semi-Annual Report on the U.S. and Canadian Industrial Markets

CBRE Torto Wheaton Research
Year End 2006

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Overall, the industrial markets that will outperform in the short-term are those concentrated in business-to-business services, while markets that are driven by the consumer may under-perform over the next two years.

Those manufacturing markets that do not concentrate on the manufacture of automobiles or parts are anticipated to see healthy increases in rents.

MARKETS CONCENTRATED IN BUSINESS-TO-BUSINESS WILL OUTPERFORM

The U.S. economic expansion is showing signs of maturity—the housing sector has cooled, gas prices remain elevated and consumer activity is moderating. The national industrial sector continues to expand, although net absorption and rent appreciation are tempered compared to the strong recovery of 2005. While the risk that the housing correction will put the national economy into a recession is very low, a minor slowdown over the next couple of years is anticipated as consumer spending is curtailed to reflect sagging home values.

As such, consumer-driven industries and markets that are based around discretionary spending are at a greater risk of a sharp slowdown, while business-to-business services are anticipated to show a strong performance, supported by healthy corporate balance sheets and reinvigorated corporate investment. Overall, the national industrial market should be only mildly affected by the U.S. economic slowdown, certainly helped in part by the resilience of the global economy and its ever-increasing trade volumes and voracious demand for efficient goods flows.

The trajectory of demand growth is moderate and sustainable, suggesting that the rate of decline in industrial availability rates will begin to flatten over the next several quarters. However, a slowdown is not the same as a recession and therefore goods-production, trade flows and industrial employment should continue to expand, albeit at a more measured pace.

While rent growth in 2006 was slower than in 2005 on average, breaking out markets by classification shows that the performance is quite varied and that the high-technology markets are experiencing stronger rent growth than in 2005. Currently, rent growth is greatest in the port and high-tech markets—at 3.3% and 3.0%, respectively—and the lowest in the small distribution, manufacturing and other categories at 0.0% and 0.5%, respectively.

Breaking out the small and large distribution markets shows that rents have behaved quite differently historically in each category. Rents in the secondary distribution hubs peaked in 2000, just above the port markets, and did not fall as much as the larger distribution hubs after the recession. New supply seems to be relatively contained in these markets, resulting in more stable rent growth, which is likely to persist in the outlook.

High-tech markets will see the most rent growth over the next two years as many business-to-business services are anticipated to continue to grow, supported by healthy corporate balance sheets that will support renewed investment in technology, equipment and human capital. The availability rate in the high-technology sector should decline 60 basis points by year-end 2008. San Francisco, San Jose and Raleigh will lead in terms of rent performance.

Nationally in the U.S., rents will increase 4.4% annually over the next two years; markets that will outperform—besides the California high-technology markets—are the supply-contained distribution markets and some of the port markets on the Gulf and East Coast. Growth will be fostered on the East Coast by the lower-cost practice of shipping goods by all-water services to the East Coast rather than intermodally from West Coast ports. As the increasingly congested Panama Canal approaches capacity, all-water services through the Suez Canal will be utilized more over the next five years, which will create the need for distribution centers along the East Coast to service the increase in imports. So far this year, TEU traffic to the Port of New York-New Jersey has increased almost 8%. Port markets on the East Coast are anticipated to see healthy rent gains as the share of cargo moving through East Coast ports is expected to rise.

Another indication that the East Coast will remain competitive is that the Heartland Corridor project—which will enable double-stack containers to be transported by rail between the Port of Hampton Roads and the Midwest, reducing the intermodal transit time by one day—is hoped to be completed by 2009.

MARKET FUNDAMENTALS

The industrial market continues to expand, driven by increased global trade. Import growth continues at about 13.3% annually in real terms while export growth is up 14.5%. Import growth is primarily fueled by the more cost-effective production of consumer goods offshore, and exports have increased as a result of the weakening dollar and the strong economies of our trading partners. While the outlook still looks favorable over the long-term for the economy and the consumer, there are short-term risks, including the likelihood of higher interest rates and the potential for a weaker housing market to damage liquidity in financial markets. There are also risks of oversupply in the large distribution markets that could stall positive rent traction.

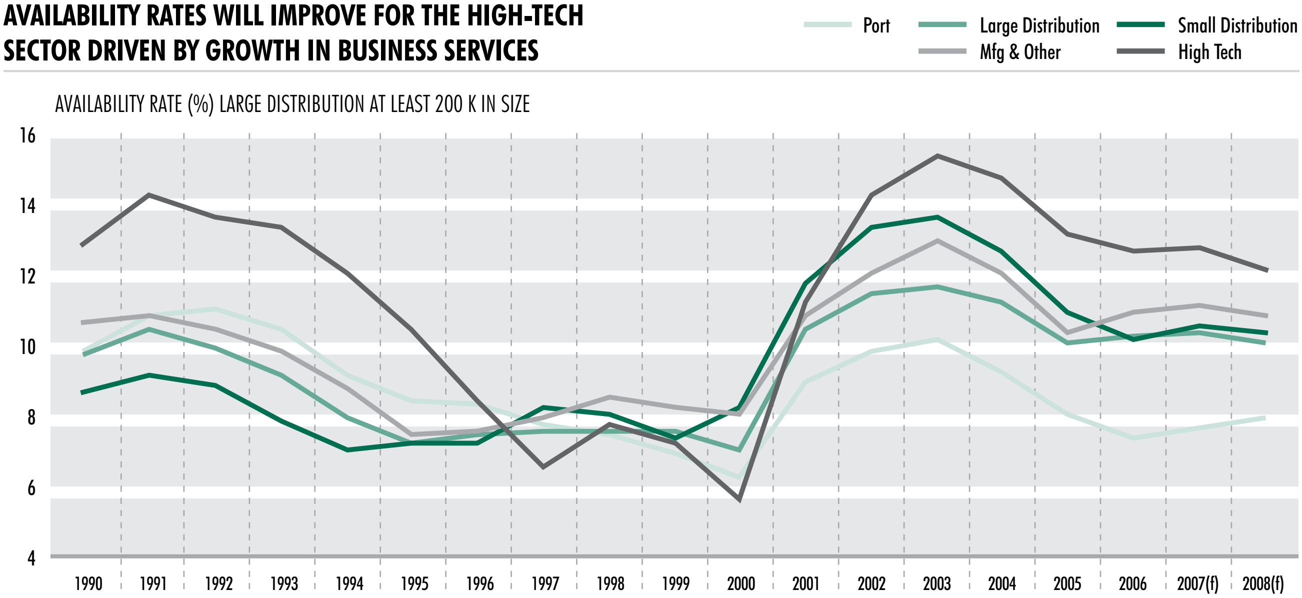
Although 2006 started off slowly, conditions for industrial demand improved. During the year, the availability rate declined 50 basis points, with 187 million sq. ft. of net absorption and 155 million sq. ft. of new space completed. All of the sub property types have shown improvement, with the largest improvement in availability in the R&D sector, declining 110 basis points in the first quarter to 13.2%. The warehouse sector has moved into the single-digits for the first time since 2001, currently at 9.7%. The manufacturing sector declined 40 basis points, to 7.1%.

Trade growth continues to drive net absorption, particularly in the largest 20 distribution markets in both the U.S. and Canada. Southern California continues to see the greatest increases in demand as deepening trade flows invigorate both the ports of L.A. and Long Beach. The Inland Empire in particular continues to do well as supply constraints, transportation issues and land-use regulations have pushed new distribution center development from Los Angeles into Riverside.

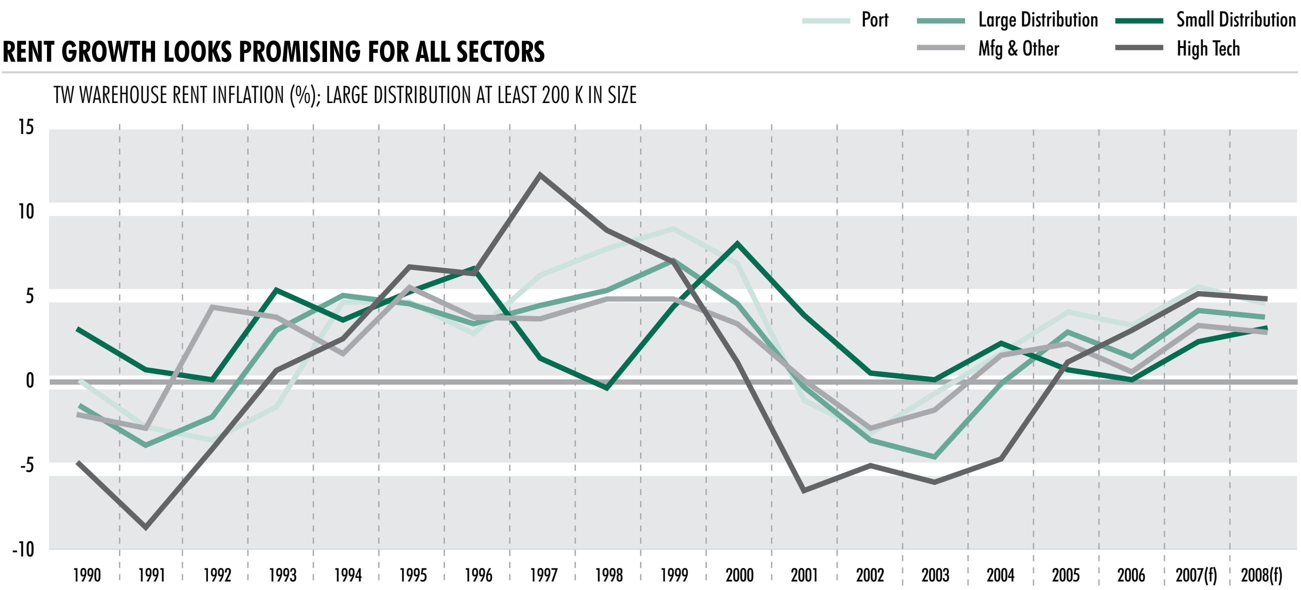
Other distribution markets that are doing well include Chicago, Atlanta, Dallas, Houston, Los Angeles, Seattle and Indianapolis. Demand in Chicago continues to be fueled by import flows moving from the West Coast to the East Coast. Chicago is the nation's busiest rail center and the third largest intermodal hub in the world. Intermodal growth has increased over 5% in the last year.

Atlanta continues to see strong net absorption as the gateway to the South, serving the port traffic from Savanna, Charleston and Jacksonville. Imports also flow into Atlanta from the West Coast via rail. Other markets that are doing well are tied to the regional supply chains and distribution networks such as Dallas and Indianapolis, both important inland hubs along the national supply chain.

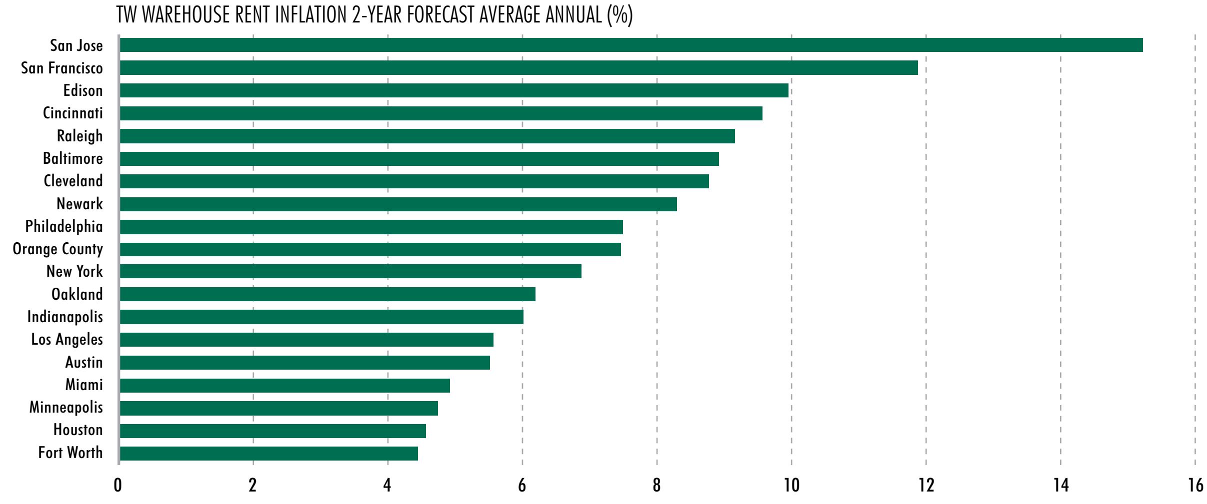
AVAILABILITY RATES WILL IMPROVE FOR THE HIGH-TECH SECTOR DRIVEN BY GROWTH IN BUSINESS SERVICES



RENT GROWTH LOOKS PROMISING FOR ALL SECTORS



HIGH-TECH MARKETS WILL BE TOP PERFORMERS FOR RENT GROWTH OVER THE SHORT-TERM FORECAST



Source: Torto Wheaton Research Outlook XL

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In 2006, the U.S. availability rate declined 50 basis points, with 187 million sq. ft. of net absorption and 155 million sq. ft. of new space completed.

Trade growth continues to drive net absorption.

While the larger markets accounted for 52% of net absorption in 2006, they also accounted for 63% of new supply. With new supply increasing in many of these larger markets, there is a potential for below-average rental growth in the short-term. Markets where new supply is contained are the smaller industrial markets of less than 100,000 sq. ft.; 23 such markets accounted for 16% of national net absorption and only 8% of new supply. While there are a few exceptions such as Las Vegas and Trenton, overall net absorption is outpacing new supply and is very healthy in select markets where availability has fallen well over 100 basis points, such as Allentown, Raleigh, Jacksonville and Vallejo.

The Raleigh economy is booming as the market is benefiting from a rebound in the high-technology sector; the influx of venture capital is a major component pushing this rise in activity. Austin is also doing well, as the high-technology markets continue to expand due to growth in business-to-business service activity.

Allentown is experiencing strong demand for industrial space as an alternative to New Jersey, which is more expensive and congested. Vallejo, comprising Napa and Solano counties and totaling 43 million sq. ft., is also experiencing strong demand.

While net absorption remains strong, new supply is robust in several areas. One segment that is of particular importance is very large warehouse space of greater than 400,000 sq. ft.—a significant segment of the industrial sector totaling 1.2 billion sq. ft. Availability for these large buildings remains comparatively high at 11.8%. About 25% of this market, 300 million sq. ft., has been built since 2000, and this newer space has an availability rate of 17.3%, which is well above average and is a reason for some concern on the part of investors. The high availability rate is a signal that a considerable portion of this space is being built on speculation and that lease-up times are becoming longer. The markets of most concern are Inland Empire, Chicago, Atlanta, Indianapolis, Memphis, Dallas, Edison, Columbus and Nashville.

The Canadian industrial market is starting to slow, although there are sharp regional variations in demand and supply. Certainly, the strong dollar environment is more of a challenge to industrial real estate than office assets, with the burden of the strong dollar being borne by warehouse and distribution space in Quebec and Ontario. This is the manufacturing heartland of Canada, and much of what is manufactured is exported as finished consumer and capital goods. And while Vancouver industrial space is also closely related to trade, there is a fundamental difference between the trade-related warehouse and distribution space in the industrial heartland, serving North-South trade, and that in the West, which serves East-West trade.

The industrial markets will reflect these differences with higher availability rates in Central/Eastern Canada. Availability rates in the West are already miniscule as Calgary and, to a lesser extent, Edmonton benefit from the energy boom in Alberta. But even Vancouver, where industrial space is closely linked to trade, will fare well despite the strong dollar.

In the East, availability rates are higher and rising. There are fewer constraints to building in Toronto and Montreal, yet availability rates are currently below the historical average. As with the U.S., there is an incentive to build more modern warehouse and distribution space to replace older facilities. The combination of weaker demand over the next two years and new supply will keep availability rates on their rising trend. Industrial investor returns are above their historical averages and still compare favorably to other investment classes, especially considering improving cash flow stemming from higher occupancies and rent.

Toronto is among the top four East Coast distribution markets, along with northern New Jersey, Atlanta and eastern Pennsylvania.

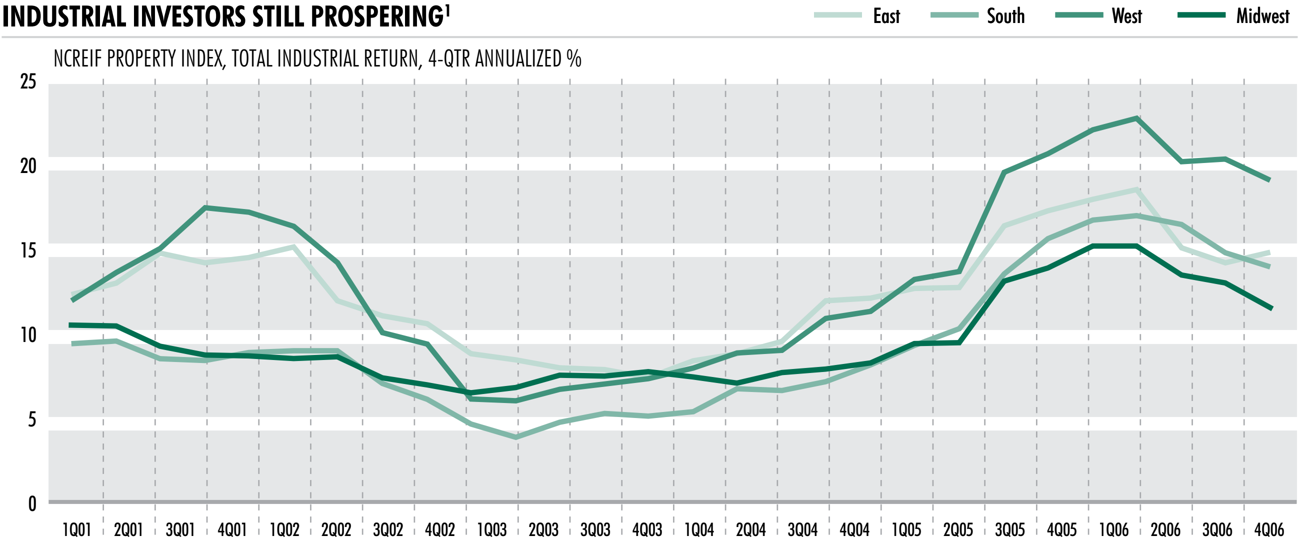
INDUSTRIAL CAPITAL MARKET TRENDS

Capital trends remain favorable for industrial properties across the country. While assets are generating quite good returns, the asset class has slipped off its highs from several quarters back. Yet, real estate's enduring popularity as an investment is sustaining pricing, despite slightly higher interest rates. Investor demand for industrial assets is evident in comparing investment returns now and at the height of the previous expansion before the downturn in 2001. Most returns remain above those previous highs in 2001, reflecting more favorable pricing of assets and the belief that real estate assets are intrinsically less risky than other assets—a mindset that galvanized after the sharp drop in the stock market.

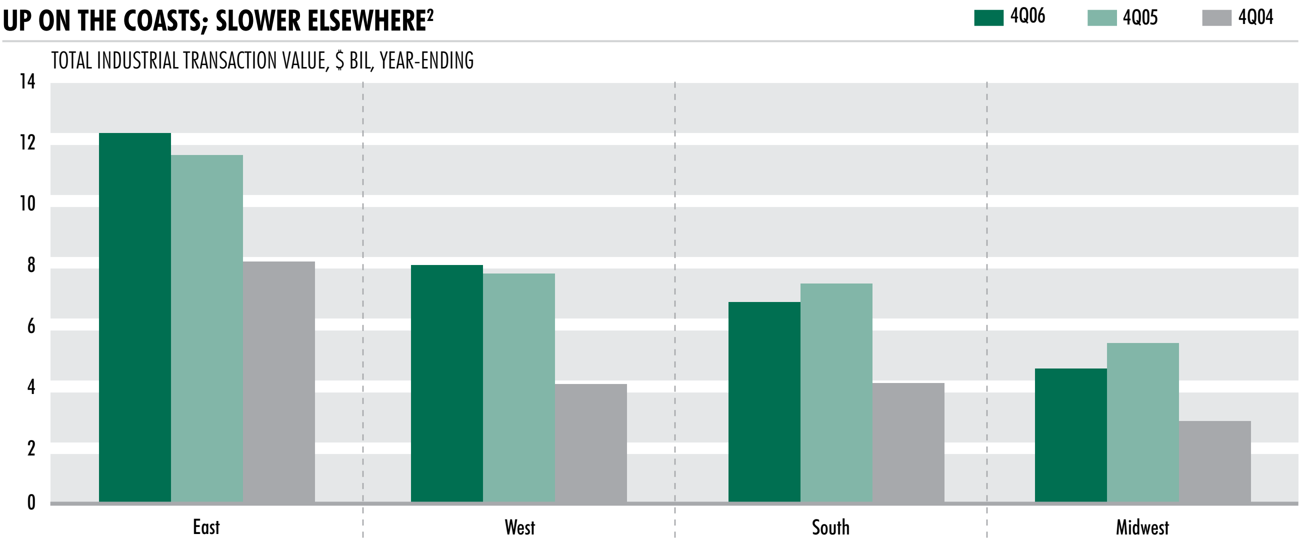
Transaction volumes largely reflect return trends. Investor interest in industrial properties is still on a high plateau, though a bit off of recent highs. Transaction volumes have now fallen from one year ago in the South and Midwest, yet volume is well above two years ago (see chart). Meanwhile, transaction volumes are rising on both coasts relative to the previous year, though the pace of these increases has slowed from what was generated in the previous year.

It is no surprise that investors remain particularly focused on the coasts, as port activity has risen in recent years, both as our trade ties have deepened with China, which has invigorated Los Angeles and Long Beach, but also as our exports to the rest of the world have increased in recent quarters. For instance, trade with Europe has increased as both North America and Europe are amid economic expansions encouraging the free movements of goods, which has invigorated the Port of New York/New Jersey, among other places.

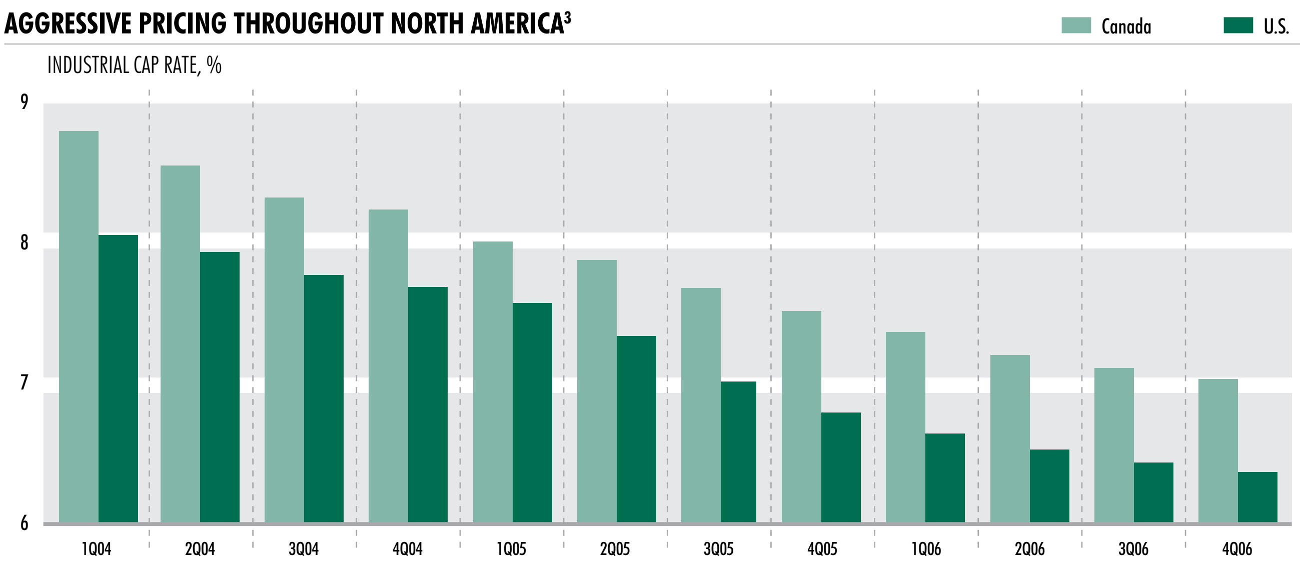
INDUSTRIAL INVESTORS STILL PROSPERING[1]



UP ON THE COASTS; SLOWER ELSEWHERE[2]



AGGRESSIVE PRICING THROUGHOUT NORTH AMERICA[3]



[1] Source: NCREIF

[2] Source: Real Capital Analytics

[3] Source: CB Richard Ellis, NCREIF

Moreover, the increasing number of wage earners has increased demand for consumer goods in metropolitan centers, many of which exist along either coast.

That is not to say that capital is not flowing to industrial real estate in the inland distribution areas; quite the contrary. Industrial transaction volumes remain high, and cap rates are low throughout North America. However, coastal ports and coastal knowledge centers have been among the healthiest economies in recent quarters and are understandingly piquing the interest of investors.

Capital markets remain liquid in Canada as well, where industrial cap rates track those of the U.S., but at a somewhat higher level. The lowest industrial cap rates can be found in Calgary and Vancouver, at 6% and 6.25%, respectively. Capital markets do share essentially the same capital pool throughout North America, and given this relationship as well as the slightly higher cost of capital in all regions now, one would expect that capital, as a rule, will favor those assets with the best income potential, whether in the U.S. or Canada.

Aside from the headwind of a higher cost of capital that is likely in the quarters ahead as the economic expansion continues, capital flows will find renewed competition from other investment vehicles. Whether it is stocks, venture capital or the draw of profiting in the developing world, the global economic expansion is providing an increasingly diverse package of well-performing investments. Corporate real estate does, nonetheless, provide its unique combination of cash flow and diversification benefits that are allowing it to remain a favored asset class, particularly in the eyes of institutions and private equity.

According to Torto Wheaton's Investment Database, the highest returning markets in which to have held an industrial property over the last five years are Orlando, Inland Empire and Sacramento.

According to the NCREIF data, of the markets in which they collect data, Los Angeles currently has the lowest industrial cap rate in the U.S. at 5.3%. There are a total of 12 industrial markets with cap rates below 6%.

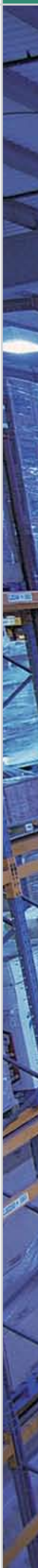
ECONOMIC CONDITIONS

This year began with two notable changes. First, the long anticipated pop in the housing bubble finally came in the second half of last year, and there is no longer any need to wring our hands about that inevitability any longer. Second, as we are now in the wake of this significant event, we can look around and see that, in fact, real estate fundamentals continue to do remarkably well.

So, is it true that what doesn't kill us makes us stronger? In this case, we believe that to be the case. Over-investment in as important a sector of the economy as single-family homes and condos is a very serious thing indeed. Moreover, the inevitable disinvestment is always proportional to the initial over-investment. In other words, the bigger the bubble, the louder the pop. For the good of our industry, we did not want that bubble to get any larger. And, since there is still remarkable liquidity in the economy, we have been allotted the time and capital to slowly work through this issue which, ultimately, has done the minimum potential damage to commercial real estate markets and the economy at large.

Looking at the likely effects in the year ahead, there are two: job and income. The job effect is already playing out and will affect real estate tenants directly involved in housing. Markets are already dealing with the rapid disintegration of the residential development industry, which is and will continue to lead to some new vacancy—sublet and direct. Moreover, retailers specializing in appliances and residential refurbishing are struggling, requiring fewer shipments of goods, and one can also expect manufacturers of building materials to also start decreasing their use of industrial space.

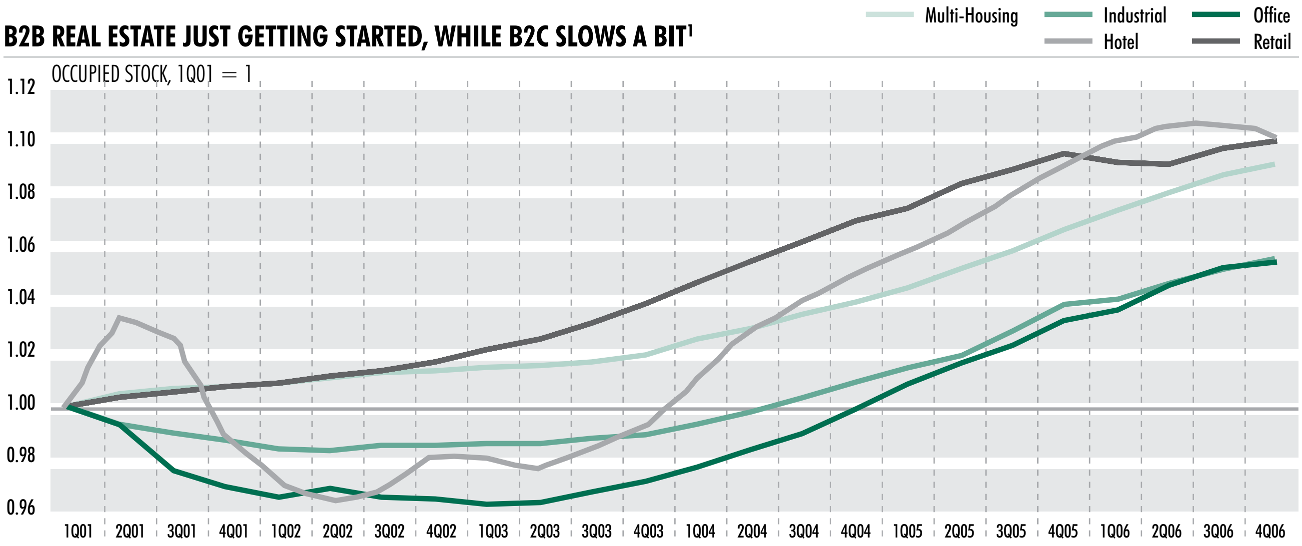
The income effect is also playing itself out in demand for autos. This have concentrated implications for the



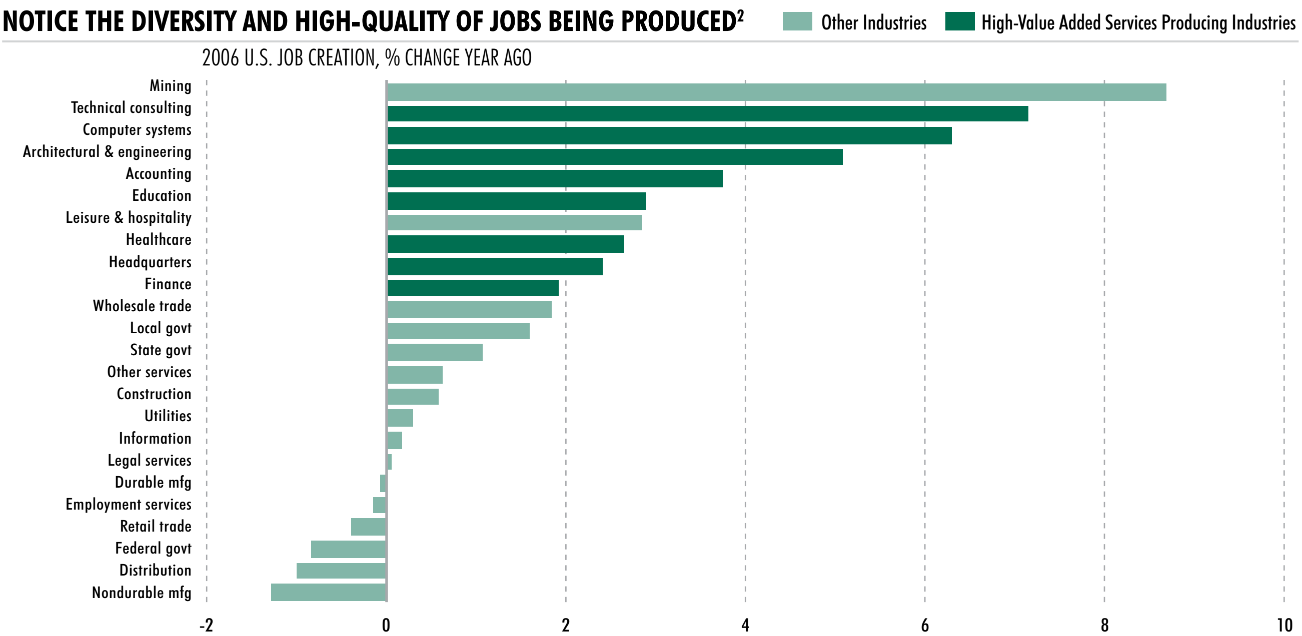
Even though job growth in the economy is slowing, the downturn has been most pronounced in goods-producing regions. Most service-producing, office-occupying regions continue on at a steady or somewhat slower pace of expansion, supporting demand for warehousing and distribution.

industrial Midwest and will affect all property types there. Moreover, the income effect will play itself out in household spending in affected areas as the year wears on. Fortunately, while all these things do sound a bit depressing, just about everything else in the economy is going at full steam, which means that, by and large, fundamentals are continuing to improve. Booming corporate financing, investment in R&D, expansion and re-investment in the means of production, spending on healthcare, and investments in education are among those forces that are invigorating some of the largest markets in the country—places like Boston, New York, Atlanta, Dallas, San Francisco and Denver. While many of these services industries do not occupy space directly, they do support jobs and spending that require absorption of warehouse and distribution space in and around regions.

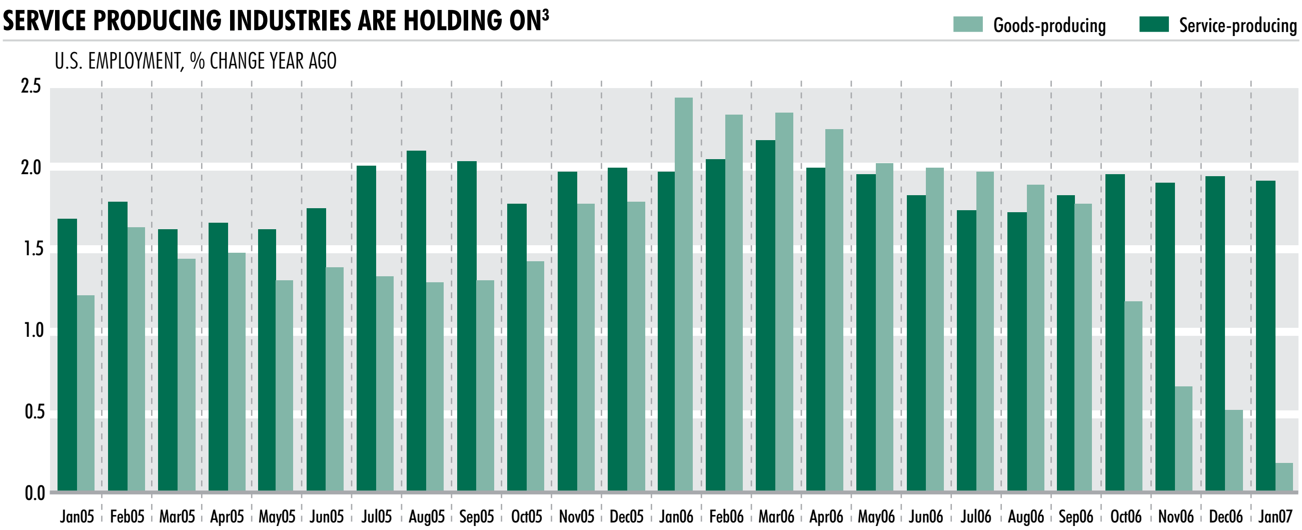
B2B REAL ESTATE JUST GETTING STARTED, WHILE B2C SLOWS A BIT[1]



NOTICE THE DIVERSITY AND HIGH-QUALITY OF JOBS BEING PRODUCED[2]



SERVICE PRODUCING INDUSTRIES ARE HOLDING ON[3]



[1] Source: Torto Wheaton Research Outlook XL

[2] Source: BLS

[3] Source: BLS

Since 2001Q1, the Mountain NCREIF division outpaced all others in terms of its rise in occupied industrial stock. While all divisions are now above where they were in 2001, the Northeast and West North Central have only recently regained that mark.

INDUSTRIAL MARKET OUTLOOK

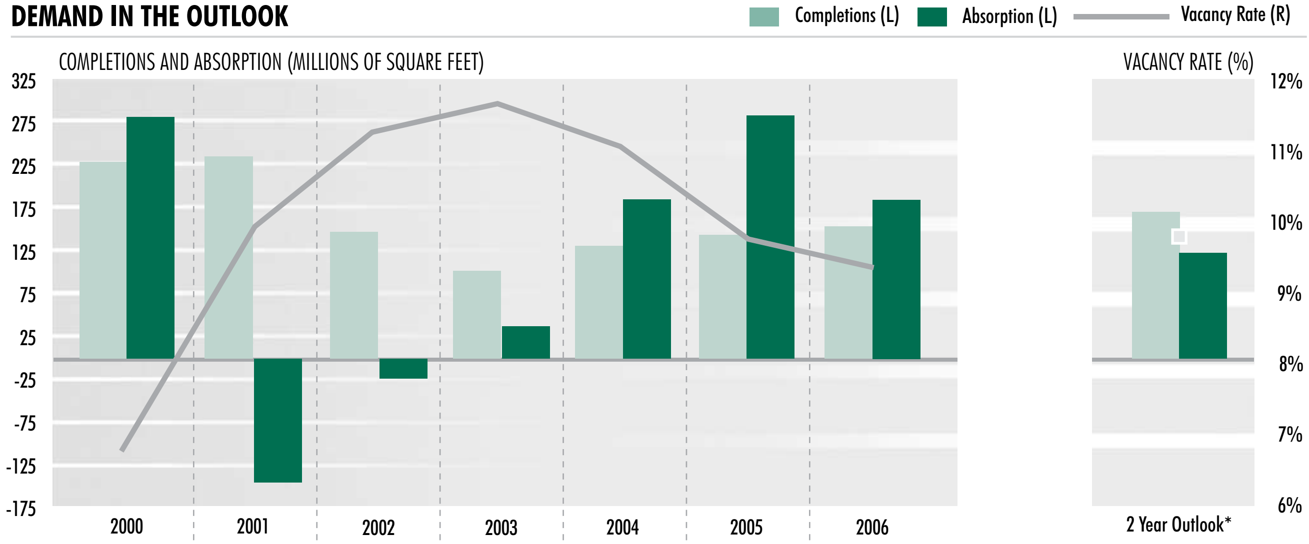
The pace of demand for industrial space in the U.S. is likely to ease in the quarters ahead, generally flattening industrial availability rates. However, a slowdown is not the same as a recession, and goods-production, trade flows and industrial employment should continue to expand, albeit at a more measured pace. Another issue that may impact market and submarket availability levels is the impact of high energy prices, which look likely to remain elevated for some time on user space needs.

Availability is likely to be very uneven geographically in the quarters ahead, as the pace of new construction will not be uniform across the U.S. New supply will average 169 million sq. ft. per year over the next five years. While this is less than the long-term average of 191 million sq. ft. per year, many large distribution markets will experience new supply greater than the long-term average. Nationally, rent growth will remain positive, averaging 3.9% annually over the next five years.

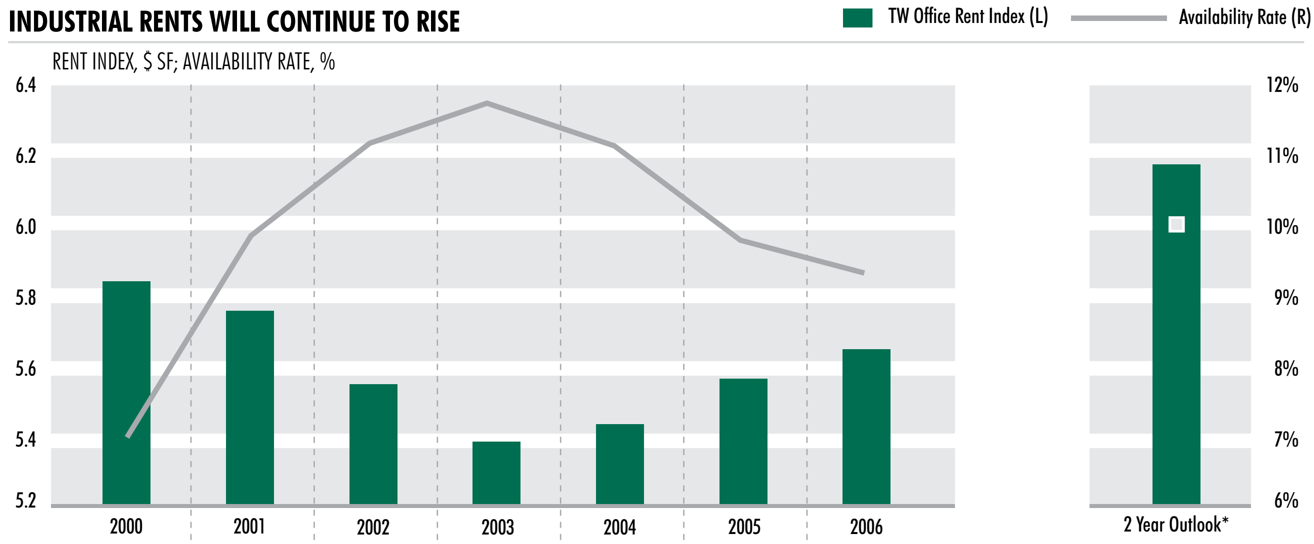
In Canada, demand for industrial space will slow over the next few years relative to recent experience. This is not purely a function of the ongoing manufacturing slowdown, however. For Vancouver and Calgary, reduced demand is a function of the current very tight markets. In both cases, demand would be greater were it not for the paucity of modern distribution and warehouse space.

On the other hand, Toronto, Montreal, Ottawa and Winnipeg will see moderating demand. Median historical demand for this group of markets is 3.45 million sq. ft. per quarter. Weaker exports and imports and a below-trend pace of macroeconomic growth will push that count down to just more than 600,000 sq. ft. of absorption per quarter through the end of 2008. By then, U.S. consumption will be on the rebound, as will the Canadian economy.

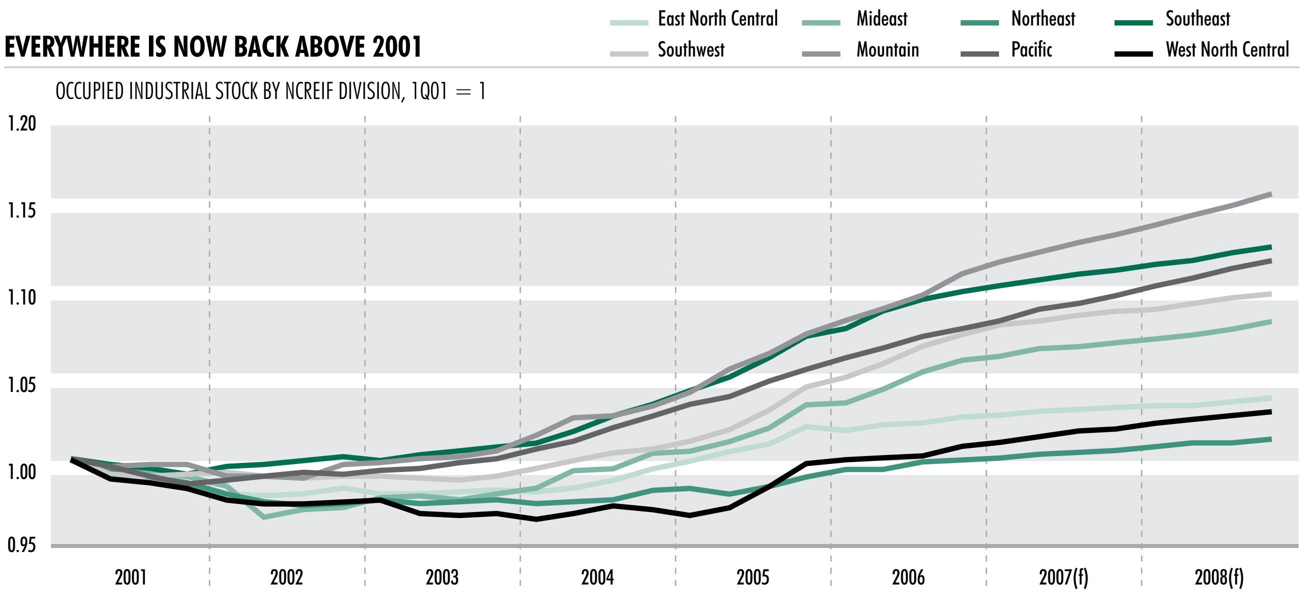
INDUSTRIAL COMPLETIONS WILL OUTSTRIP DEMAND IN THE OUTLOOK



INDUSTRIAL RENTS WILL CONTINUE TO RISE



EVERYWHERE IS NOW BACK ABOVE 2001



Source: Torto Wheaton Research Outlook XL

*2yr. Outlook – Completions & Absorption are annualized across the eight quarter outlook, availability is the ending availability rate eight quarters out.

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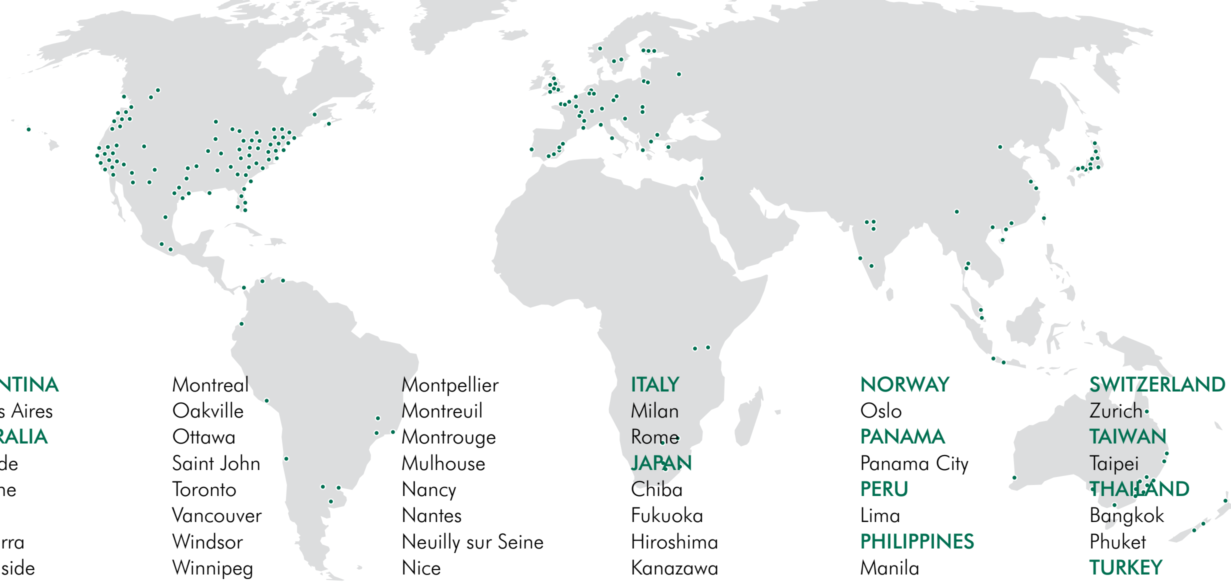

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Parramatta
Perth
South Sydney
Sunshine Coast
Sydney
Townsville
Tweed heads
Underwood
AUSTRIA
Vienna
BELGIUM
Brussels
CROATIA
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Uganda
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Leeds
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Manchester
Southhampton
UNITED STATES
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VENEZUELA
Caracas
Puerto la Cruz
VIETNAM
Hanoi
Ho Chi Minh City
ZIMBABWE
Bulawayo
Harare

TERMS & DEFINITIONS

Availability — Space that is considered available for lease, sublease or sale, but is not necessarily vacant. The CB Richard Ellis U.S. Industrial Availability Index measures the supply of available space in large industrial buildings as a percentage of the total amount of such space. The index is based on a quarterly survey of large industrial properties, 100,000 square feet or larger in size. Available properties include both vacant and occupied available space in existing and under-construction buildings (within six months of completion). Canadian data is based upon industrial properties 5,000 square feet or larger.

Bay Depth — The distance between columns.

Cap Rate — The capitalization rate, the net operating income of the property divided by purchase price.

Capacity Utilization — A measure of what portion of existing output capability is in use.

Clear Height — The distance from the floor to the bottom edge of the beams which support the roof. It is used as a measure of the vertical warehouse storage capacity of a property.

Construction Starts — Buildings which have begun construction as evidenced by site excavation or foundation work.

GDP — Gross Domestic Product – The sum of personal consumption expenditures, gross private domestic investment (including change in private inventories and before deduction of charges for CFC), net exports of goods and services (exports less imports), and government consumption expenditures and gross investment. GDP excludes intermediate purchases of goods and services by business.

Lease Rates — Average asking rental rates.

MO (Manufacturing Output) — A component of the Index of Industrial Production (IIP), which is published by the Federal Reserve Board. MO is calculated by subtracting the mining and utility industry components from the IIP.

Net Absorption — The change in occupied square feet from one period to the next.

Net Export of Goods and Services — Exports less imports of goods and services.

Private Inventories — The physical volume of inventories owned by private business, valued in average prices of the period as reported by the U.S. Bureau of Economic Analysis.

Real Value Added — Net profit after taxes and cost of capital.

REIT — Real Estate Investment Trust.

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