



## Recession Deepens; Broad-Based Economic Stimulus to Support Stabilization by Late 2009

The U.S. economy remained relatively resilient through the first part of 2008, posting moderate growth, below-trend job losses and a rise in consumer spending – due in part to a temporary boost from economic stimulus checks. However, a crisis of confidence spurred by record financial sector losses, corporate bankruptcies and government takeovers led to an interbank lending freeze and near-standstill in the commercial paper market. The escalation of the credit crunch to a full-blown crisis has contributed to the broadening of the recession.

**Governments around the world have joined forces, injecting an unprecedented amount of liquidity into the global economy, in attempts to prop up confidence and limit the depth of the downturn.**

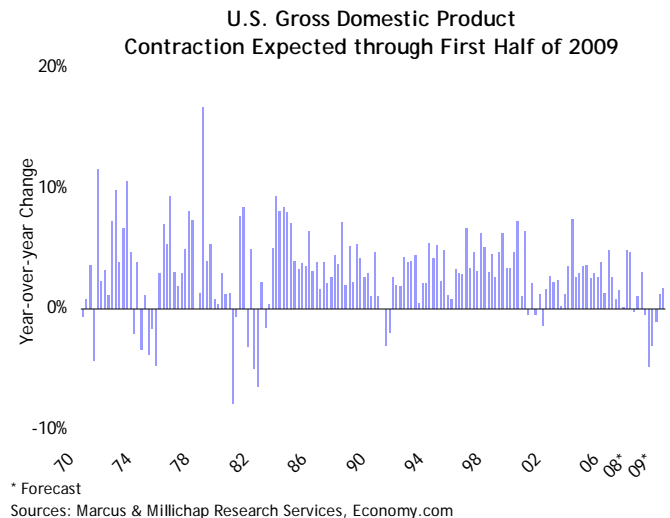
Overall, the effects of most U.S. government measures have yet to take hold. As banks begin lending again and additional initiatives are implemented, they will ultimately work their way through the economy. The process, however, will take time. In addition, the new administration is planning a large-scale stimulus package intended to create millions of jobs over the next few years. Discussions have centered upon tax cuts for U.S. households, tax incentives for businesses, and major infrastructure improvements to the nation's aging roads and bridges, and high-tech communications networks.

**The economic downturn has led to a dramatic reduction in oil prices.** Lower energy costs have taken some pressure off of household budgets and reduced inflationary concerns, providing the Fed with greater flexibility to cut rates. At its last meeting, the Federal Open Markets Committee (FOMC) cut the Fed funds rate by 75 basis points to 0.25 percent, the lowest rate on record. It must be noted, however, that the potential for deflation is present and poses a new set of risks. During October and November, the headline rate of inflation declined by 1.0 percent and 1.8 percent, respectively.

### Forecast:

**Job losses are expected to continue at an accelerated pace in the near term.** Employment has been declining since January 2008, with a total of 2.6 million jobs cut through December. From peak to trough, we expect losses to surpass 4 million – the greatest contraction since the early 1980s. One of the more significant downside risks to the employment outlook is the potential failure of one or more of the U.S. automakers.

**The economic situation is expected to worsen before showing signs of stabilization in late 2009.** U.S. GDP figures for the fourth quarter of 2008 are expected to reflect the greatest contraction since the early 1980s, following a decline of 0.5 percent in the third quarter. The current downturn is expected to be similar in magnitude to the 1974/75 recession, which was also global in nature and among the worst since WWII. GDP contraction is forecast to reach 2.5 to 3.0 percent from peak to trough.





## Retail Vacancy Rising as Consumers Pull Back, Store Closures Accelerate

**Retail vacancy rose to 8.5 percent in the fourth quarter, an increase of 130 basis points from one year earlier.** Effective rents began to edge down in 2008 and will continue to slip in 2009. Following the latest holiday season, many major retailers are already making efforts to renegotiate leases already in place to cut operating costs and prevent closures.

**The list of national chains filing for bankruptcy or slashing store counts is growing, leaving significant holes in shopping centers and malls.** The loss of anchor tenants is creating a more difficult environment for already struggling smaller retailers that occupy inline space. This trend is expected to continue well into 2009 as credit remains tight, and both businesses and consumers continue to pull back on spending.

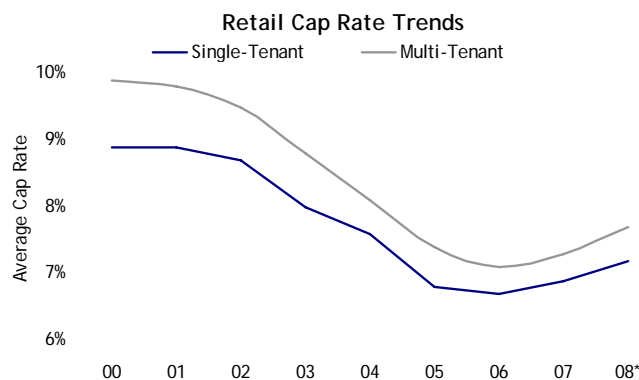
**Retail sales declined during the latter part of 2008 due to reduced consumer spending on autos and other nonessentials, and a rapid decline in gas prices.** Although declining energy prices provided some relief to already struggling consumers in recent months, early estimates for the recent holiday season suggest it was not enough to stimulate spending. Excluding autos and gas, retail sales during the holiday season were down by an estimated 2-plus percent, the worst results in several decades. Auto sales also ended the year on a sour note, with major domestic and foreign automakers reporting year-over-year declines of 30 to 50 percent in December.

**Approximately 4,630 store closures were announced during the first three quarters of 2008, with estimates for the fourth quarter at 1,900 closures.** Food and beverage store closure announcements increased considerably in the third quarter, accounting for 36 percent of the total, followed by jewelry and apparel stores, which combined accounted for another 43 percent. The shift in closure announcements – away from furniture/home furnishings stores, which dominated in the early part of 2008 – reflects how broad-based the downturn has become, affecting all aspects of the retail sector.

### Forecast:

**Nationally, completions reached an estimated 130 million square feet in 2008, with a decline to 90 million square feet anticipated in 2009.** Despite the rapid deceleration in development activity, vacancy is forecast to rise approximately 170 basis points to 10.2 percent this year. Following the disappointing holiday season, which typically accounts for more than one-quarter of retailers' annual sales, store closures are expected to accelerate during the first six months of 2009.

**The wide gap between buyers' and sellers' expectations, weakening market fundamentals and the tighter lending environment will continue to hamper retail property sales through the first half of 2009.** Retail investment dollar volume was down an estimated 70 percent through the majority of 2008, while the number of transactions slipped close to 50 percent. Risk premiums have returned to the marketplace, with lower-quality properties, and assets in secondary/tertiary locations experiencing the greatest correction. The spread between cap rates in primary markets versus those in tertiary markets has already widened from less than 50 basis points one year ago to nearly 100 basis points today. Many owners who do not need to sell today are choosing to hold properties, but for those who must sell due to maturing debt or operational challenges, discounting will be necessary to clear the market.



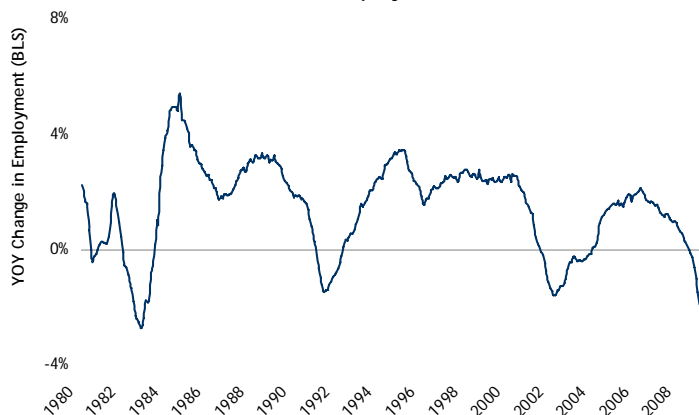
\* Through 3Q (All figures include sales \$1M+)

Sources: Marcus & Millichap Research Services, CoStar, RCA



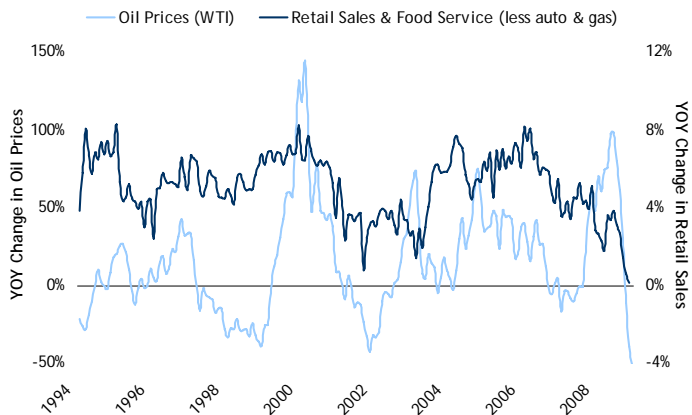
## Retail Market Vital Signs

Total Non-Farm Employment Growth



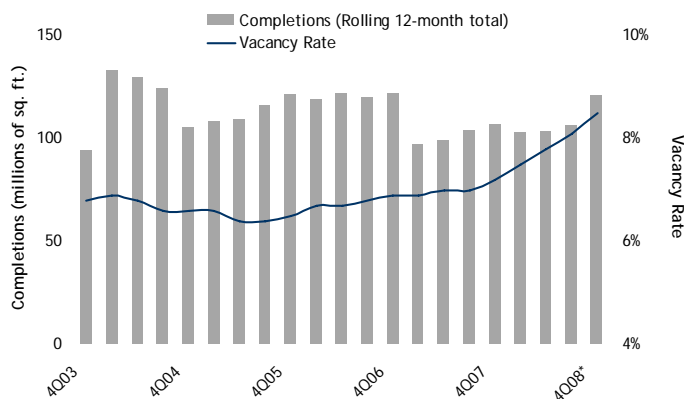
Sources: Marcus & Millichap Research Services, Economy.com

Retail Sales and Oil Prices



\* Retail sales through Nov, oil prices through Dec  
Sources: Marcus & Millichap Research Services, Economy.com

Total Retail Supply and Demand Trends



\* Estimate (All figures includes single-tenant and multi-tenant)  
Sources: Marcus & Millichap Research Services, CoStar Group, Inc.

Retail Sales Trends



\* Estimate (Sales data includes multi-tenant transactions of \$5M+)  
Sources: Marcus & Millichap Research Services, CoStar Group, Inc.

### 3Q 2007 to 3Q 2008 Change in Retail Vacancy

#### Top 10 Markets by YOY Change in Vacancy

Metro	3Q 2008	YOY Chg (bps)
New York	4.7	-30
Austin	8.5	-10
Milwaukee	9.7	-10
Boston	5.9	0
Indianapolis	11	10
Philadelphia	7.6	10
San Francisco	4.0	10
Dallas-Fort Worth	11.3	20
Charlotte	7.6	30
San Diego	3.6	40
<b>US Metro Average</b>	<b>8.1</b>	<b>110</b>

#### Bottom 10 Markets by YOY Change in Vacancy

Metro	3Q 2008	YOY Chg (bps)
Sacramento	7.6	160
Tampa-St. Petersburg	7.5	160
Salt Lake City	9.8	200
Tucson	7.2	200
Jacksonville	7.7	220
Phoenix	8.4	220
Las Vegas	7.8	250
Inland Empire	8.9	250
Cleveland	11	260
Fort Lauderdale	7.6	270
<b>US Metro Average</b>	<b>8.1</b>	<b>110</b>

Sources: Marcus & Millichap Research Services, Costar Group, Inc.

The information in this report is deemed to be reliable. Every effort was made to obtain accurate and complete information; however, no representation, warranty or guarantee, expressed or implied, may be made as to the accuracy or reliability of the information contained herein. Sources: Marcus & Millichap Research Services, CoStar Group, Inc., Economy.com, Federal Reserve, ICSC, NAR, National Retail Federation, RCA, Reis, S&P.

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