

Suburban Maryland



In Short

- McShea is pleased to be representing Natelli Communities in what will be the largest office lease signed so far this year. Banner Life Insurance Co. has chosen Natelli's Urbana Corporate Park for its 115,000 SF headquarters.
- No building sales completed in the 1st quarter
- 1.9 million SF of new construction underway-39% preleased
- Unemployment up 44% to 48% in each Suburban MD County from February 2008 to 2009
- Overall vacancy is 12.8% - up from 12% over the quarter

ANNUAL CHANGE

Vacancy	↑
Absorption	↓
SF Under Construction	↓
Pre-leasing Rate	↑
Rental Rates	↓

Vacancy & Absorption

As the recession deepened in the first quarter, tenants across Suburban Maryland reacted by tightening their belts and returning office space to the market. Consequently, vacancy rose in each of the three counties that comprise the Suburban MD market. Frederick County led the way with a 1.2 percentage point increase to 15.1% followed by Montgomery and Prince George's County, where vacancy rose by less than a percentage point to 11.1% and 18.6% respectively. Last year, vacancy increased as a result of new supply; however, this quarter vacancy rose almost solely on anemic demand. For instance, Lockheed Martin's consolidation and ACS's sublet space in Montgomery County returned several hundred thousand square feet of supply to the market. Net absorption for the quarter totaled negative 612,491 square feet. Almost 70% of the total came from Montgomery County, although Prince George's and Frederick County contributed as well.

Leasing Activity

Not surprisingly, leasing volume plummeted in the first quarter to just forty percent of the 4th quarter 2008 level. At this pace, leasing volume will be half of what it was in 2008. That's the bad news. The good news is that there are still mid to large tenants, such as BAE Systems and United Health Group, in the market. Another indication that tenants may be starting to take advantage of the market is the absence of renewals in the top leases of the quarter.

1ST QUARTER 2009—TOP LEASES

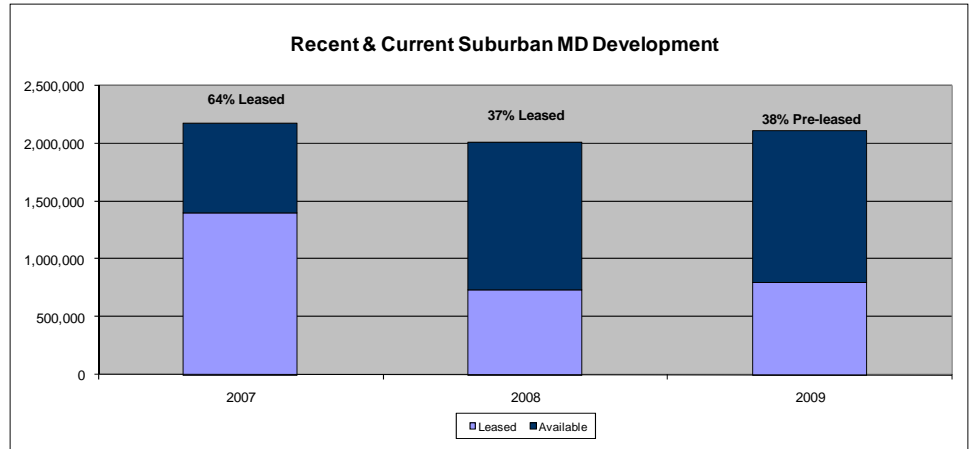
TENANT	ADDRESS	SF
Banner Life Insurance Co.	Urbana Corporate Park	115,000
SA Biosciences	6951 Executive Way	33,400
SRA International	8490 Progress Drive	30,974
MNCPP	7833 Walker Drive	27,192
KAI	11300 Rockville Pike	22,365
Vietnam Veterans	8719 Colesville Road	16,956
University of MD	5700 Rivertech Court	16,602
Scientific Hospital Supplies	9900 Belward Campus Drive	15,664
School Nutrition Assn.	120 Waterfront Street	15,265
Case Design	4701 Sangamore Road	14,759

Highlighted deals completed by McShea.



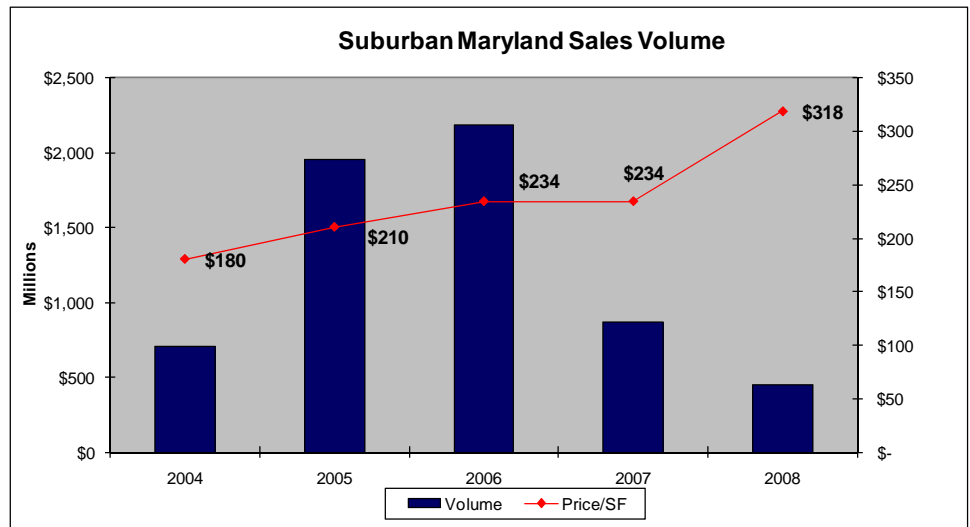
Development Activity

Two buildings totaling 174,000 square feet were completed during the first quarter—both buildings were 100% available. The largest was 16901 Melford Boulevard, a 155,000 square foot building in Bowie. There were no groundbreakings to add to the 1.9 million square feet of development which was underway at the end of the quarter. Thirty-nine percent of this space is preleased and almost 70% of is located in Montgomery County, primarily in Rockville and North Rockville.



Investment Sales

There were no office building sales completed in the first quarter, although more foreign and domestic investors are rumored to be refocusing on the Washington, DC metropolitan area. As the year progresses, we expect to see more sales as landlords with significant vacancies or cash flow issues are forced to sell or hand over the keys to the bank. These distressed sales should help to establish a “bottom” to the market.

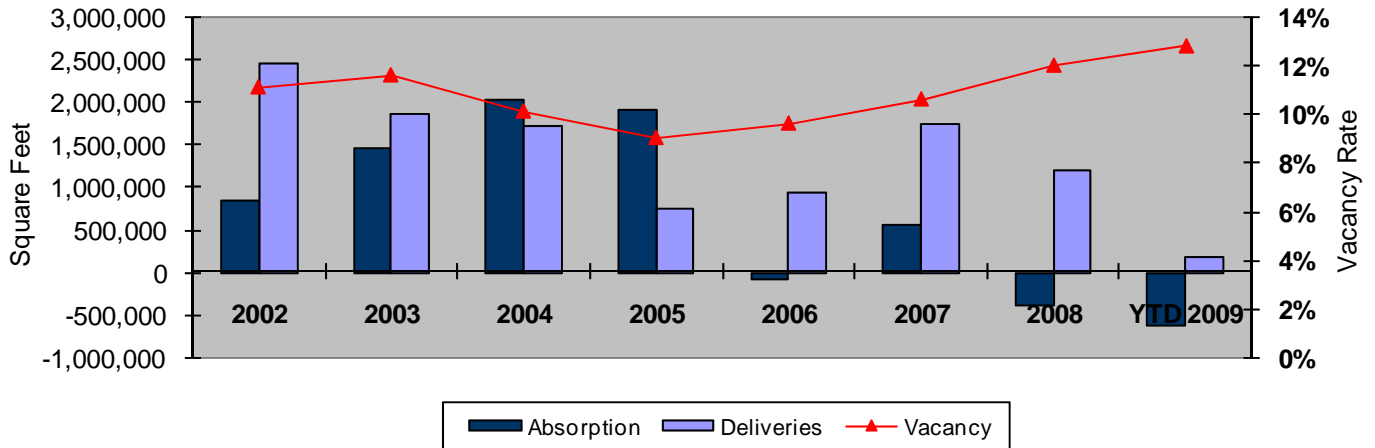


Rental Rates and Concessions

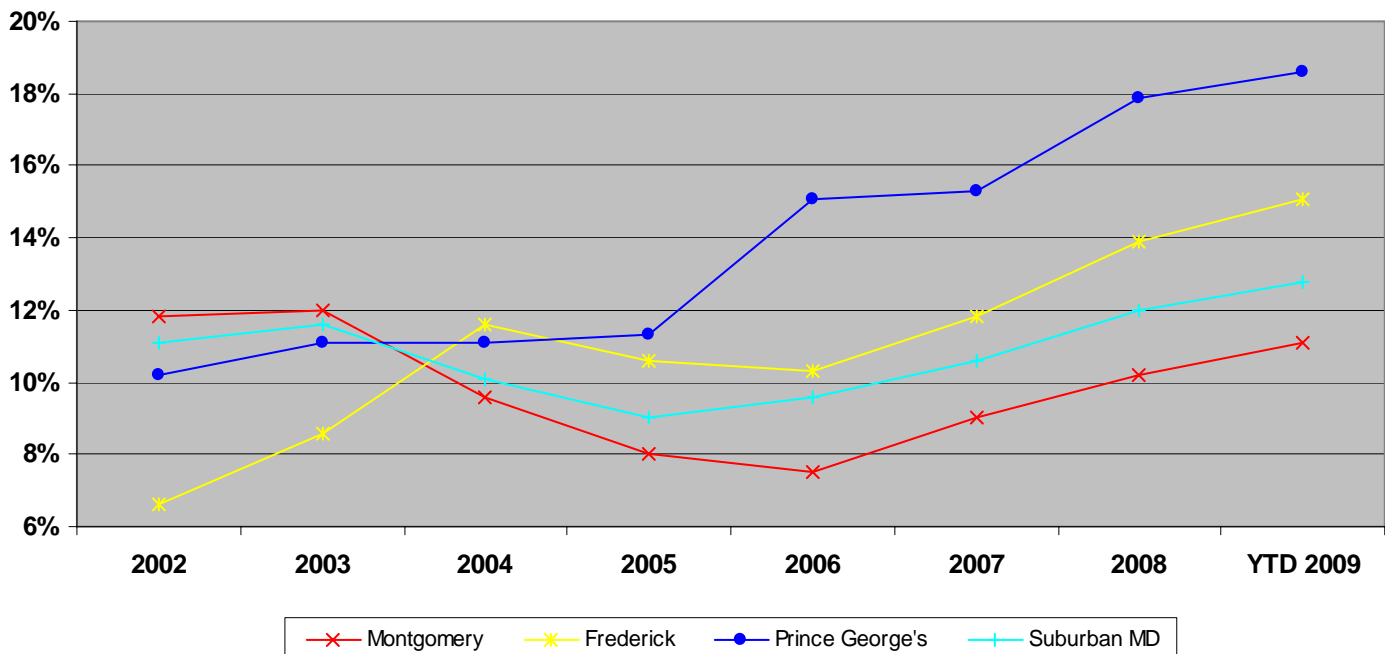
Landlords reduced asking rates across Suburban MD again in the first quarter by 0.8%. Frederick County experienced the largest decline of 1.3%. Asking rates started to noticeably decline in the fourth quarter of 2008. Of course, **effective** rental rates had been shrinking for most of 2008 as landlords offered larger concession packages to attract and retain tenants. Tenants, realizing that they have the upper hand, have started asking for ever larger concessions including significant free rent and tenant improvement packages. While tenants may not be getting everything they want, free rent has certainly made a comeback. Smaller annual base rent escalations have become more common as have turnkey build-outs. Rental rates will remain under negative pressure until demand stabilizes.



Suburban Maryland Office Class A & B Absorption, Deliveries & Vacancy



Suburban MD Historical Vacancy





**FIRST QUARTER 2009
VACANCY ANALYSIS**

	# of Bldgs	RSF	Direct Vacant	Sublet Vacant	1Q09	2008	2007	2006	2005	2004
Bethesda	159	10,571	547	248	7.5%	6.1%	6.2%	5.9%	8.6%	11.5%
N. Bethesda	94	9,775	1,189	115	13.3%	12.1%	9.1%	8.8%	11.0%	10.9%
Rockville	107	7,383	879	41	12.5%	11.9%	7.8%	4.8%	6.4%	9.7%
N. Rockville	122	10,870	1,023	269	11.9%	11.7%	12.9%	11.8%	11.0%	10.4%
Gaithersburg	123	5,141	821	147	18.8%	16.5%	17.4%	9.5%	8.2%	11.2%
Germantown	48	2,736	372	70	16.2%	15.1%	9.0%	10.4%	12.1%	13.3%
Silver Spring	119	8,761	545	78	7.1%	6.8%	4.7%	3.5%	2.6%	6.1%
Montgomery Co.	849	58,122	5,451	972	11.1%	10.2%	9.0%	7.4%	8.1%	9.8%
Prince George's	439	20,796	3,569	301	18.6%	17.9%	15.3%	13.3%	11.0%	11.4%
Frederick Co.*	671	13,820	2,018	65	15.1%	13.9%	11.8%	11.5%	11.1%	10.9%
Suburban MD	1,529	85,341	9,644	1,303	12.8%	12.0%	10.6%	9.1%	9.0%	10.3%

(In Thousands)

ABSORPTION (in thousands)

DEVELOPMENT

	5 YR Average							YTD	SF. U.C.	Percent Preleased
	1Q09	2008	2007	2006	2005	2004	Average			
Bethesda	(151)	188	(4)	435	327	195	228	0	295,000	58%
N. Bethesda	(136)	11	(67)	(18)	238	23	64	0	-	
Rockville	(34)	54	(153)	197	225	490	163	0	318,970	26%
N. Rockville	(32)	(33)	292	114	20	835	246	0	540,995	0%
Gaithersburg	(5)	(143)	279	0	143	(92)	(74)	0	-	
Germantown	(35)	(33)	167	(28)	222	182	102	0	-	
Silver Spring	(25)	(259)	(36)	(30)	391	298	73	0	105,116	44%
Montgomery Co.	(417)	(216)	71	670	1,565	1,923	803	0	1,260,081	24%
Prince George's	(139)	(247)	(44)	(340)	451	92	(18)	155,000	391,762	100%
Frederick Co.	(68)	(79)	547	243	587	125	31	19,000	255,365	19%
Suburban MD	(612)	(382)	574	753	2,089	2,000	1,006	169,000	1,877,208	39%

AVERAGE ASKING RATES

	1Q09	2008	2007	2006	2005	2004	Change %
Bethesda	\$35.88	\$35.89	\$34.98	\$31.03	\$29.12	\$26.68	34%
N. Bethesda	\$31.68	\$31.98	\$31.09	\$29.30	\$28.36	\$27.12	17%
Rockville	\$31.51	\$32.03	\$33.26	\$29.97	\$26.46	\$26.60	18%
N. Rockville	\$27.29	\$27.45	\$28.19	\$27.08	\$25.05	\$24.24	13%
Gaithersburg	\$23.27	\$23.45	\$23.69	\$23.71	\$21.26	\$22.61	3%
Germantown	\$26.08	\$26.55	\$27.25	\$23.64	\$23.35	\$22.49	16%
Silver Spring	\$28.88	\$29.43	\$27.97	\$25.27	\$25.11	\$24.55	18%
Montgomery Co.	\$29.42	\$29.65	\$29.49	\$27.63	\$25.93	\$25.88	14%
Prince George's	\$22.23	\$22.40	\$22.27	\$22.16	\$20.36	\$19.69	13%
Frederick Co.*	\$10.11	\$10.46	\$11.79	\$11.72	\$10.39	\$9.59	5%
Suburban MD	\$26.77	\$26.98	\$26.57	\$25.68	\$24.16	\$23.75	13%