Report from the BOMA International Conference and The Office Building Show

State of the Industry

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Good morning! It's wonderful to see you all today after a terrific event last night. The combination of some fun and some history is my idea of a great time. Thank you, BOMA/Philadelphia!

I am a glass half full kind of guy, so let's get the bad news out of the way first. When I spoke to you this time last year, the economy was beginning to come off its pinnacle. The descent that followed came in the wake of the broad failures of our financial institutions and the aftermath that followed.

The resulting jobs losses, lack of available credit from banks, and a frozen CMBS marketplace created a turbulent economic landscape. Commercial real estate was not spared. In just a year, we've gone from stability to volatility to decline. Grubb & Ellis reported 1st quarter vacancy rates of 15.6%, the highest level in nearly four years, and a number that is projected to go to 20%. Negative net absorption totaling 18.4 million square feet continues to push those vacancy rates higher.

This kind of quarterly dip has not been seen since 2001 and really reflects what's happening in the labor market. Last year at this time, we had job losses of about half a million. Since then, we have lost an additional 5.7 million jobs and the unemployment rate is now 9.4%. The employment situation is not expected to stabilize until next year when the unemployment rate could be in the 10% range.

Torto Wheaton Research predicts that these job losses will push demand for office space down by 4% in 2009. And Dividend Capital Research tells us that eight U.S. markets now have vacancy rates above 20%

More and more, space is going unleased. Grubb & Ellis reported that available sublease space ended the first quarter at 111 million square feet.

The latest PPR research also confirms that demand is expected to be sharply negative for 2009. Expect cumulative NOI losses in the double digits for most major property types, including office.

The U.S. is hardly alone in this downturn. Markets across Europe and Asia are experiencing similar trends. A recent report by RREEF indicates that the financial lending crisis brought to a halt the five year run of an annual global growth rate of 4.5%.

Few are immune to the pain of the recession. Even firms that have strong balance sheets are finding it difficult to navigate the current climate. A considerable amount of capital is sitting on the sidelines waiting for more favorable rates. And, many firms are conserving their cash, as they revise their hold periods and five-year plans for each asset in their portfolios.

So there's the bad news, who's ready for some better news? I think we all are. The hemorrhaging of job losses looks to be easing. And there are even a few areas of strength. Not surprisingly, government jobs are on the increase but healthcare jobs are as well. Since the beginning of the year, healthcare has added between 15,000 and 20,000 new jobs each month. This of course is good news for the Medical Office Building Market, which continues to be a sought after asset class.

Construction, which has had been especially hard hit, is showing signs of stabilizing. According to Associated Builders and Contractors, non-residential construction job losses slowed significantly in May, going from a monthly average of 10,000 job losses to 1,400. And construction costs are down, so those who can afford to build are taking advantage of better pricing.

Many economists now believe the recession will be over within a year. And while no one is predicting a boomerang into full recovery, we are beginning to see the light. Because commercial real estate was late to get hit, we can also expect to be late to the recovery. 2010 will most certainly be another tough year for the marketplace, but look for signs of growth in 2011.

Although commercial real estate has taken its fair share of pummeling from the credit crisis, there is still a lot of capital out there that will be searching for a home once the recovery kicks into full swing. Billions and billions of dollars are waiting for investment opportunities once the marketplace stabilizes.

We continue to work closely with the Fed to spur recovery. The Treasury Department recently made commercial mortgage backed securities eligible collateral for TALF loans. This is significant because it helps prevent defaults on economically viable commercial properties, it increases the capacity of current holders of maturing mortgages to make additional loans, and it facilitates the sale of distressed properties.

This is a time to hunker down, but it is also a time to be seeking out value and maximizing opportunities. Our theme for this conference has been “survive today, thrive tomorrow.” Being proactive today to keep your assets strong and your tenants happy will position you to be the first to launch when we turn the corner.

So often, the best opportunities come during the darkest days. On a recent business trip I took to Edinburgh to attend the annual conference of the British Council for Offices, I heard entrepreneur Mike Harris, Founder of Egg, make an interesting observation. He compared the current economy to a forest fire – it’s ravaging and unforgiving but then it passes. And after it passes there is new growth. Be ready for growth when this fire passes.

Think about the economic bursts we had after the ‘70s oil crisis, the ‘90s savings and loan crisis, the 2000-2001 dotcom and 9/11 crisis – the new ideas and entrepreneurial firms take off. Great possibilities are in front of us with all the investment capital on the sidelines!

If there’s one guaranteed winner in the value equation, it has to be energy efficiency. An efficiently run building is a high performance building. Exceptional energy management will help us run our buildings better today, enhance asset value, and position us for what’s ahead tomorrow.

The green movement will only increase in the foreseeable future. President Obama plans to invest $150 billion over the next 10 years in energy research and development, all while driving the development of green jobs.

A recent Green Survey of existing buildings, put out by BOMA, Incisive Media and USGBC, found that more than 80 percent of respondents allocated funds to green initiatives last year.

And market data from Kingsley Associates indicates that more than 60% of their respondents rated green building operations as important or very important. And more and more state and city governments are requiring leases in green buildings or new green building standards. We’re seeing this in places like D.C., Boston and San Francisco. Through our extensive, voluntary network, BOMA is preparing its members to be ahead of the “green” curve and well positioned to meet these coming green tenant demands. You have the tools to standout. They include:

> -The reach of the 7-Point Challenge now expands across the marketplace, with Challenge endorsers representing more than 2 billion square feet.
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> -Benchmarking energy performance through the EER and ENERGY STAR is helping you stay competitive by knowing how you stack up in your local market, and what you need to do to rise to the top.

Real opportunities will soon be available at the state and local level. A major focus of the recent stimulus package is an investment of $3.2 billion in energy efficiency and conservation projects in the nation’s cities, counties and states. This funding will support a variety of projects related to commercial real estate, including:

> -Energy audits and energy efficiency retrofits
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> -Development and implementation of advanced building codes and inspections
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> -And, financial incentive programs for energy efficiency improvements.

The stimulus funding presents a tremendous opportunity for all of you to work with local governments on the implementation of these programs. AOBA in Washington D.C. has already jumped on this and recently released a report to help its members in understanding these opportunities.

We are ready for recovery and opportunities are before us, but a pivotal part of our recovery plan is playing out in the Halls of Congress and in state capitals and city halls across the country.

Congress is changing and priorities are changing. We know that keeping real estate strong, and the entrepreneurial spirit alive, not only helps our industry but the economy as a whole. But we have to make sure that our legislators know this.

A big part of the government's path to recovery is being paved by spending. When those bills come due, commercial real estate cannot afford to ante up more than its fair share of the cost. We are working to ensure that our future tax burden does not get in the way of our ability to create jobs, generate business and lead this recovery.

We just congratulated our first class of BOMA 360 designees. Programs like BOMA 360 are value creators for commercial buildings at a crucial time. The program is unique to the marketplace because it recognizes excellence across all aspects of building operations and management. Today's designees are setting the bar higher at a time when value is paramount.

We all have to work hard to make our assets stand out in a competitive market, but I think that's why we are entering a golden era of property management. Gone is the dealmakers buy and flip market. Today, Value is King. And if you can navigate market uncertainty, you can claim that throne. I'll borrow some recommendations from Kingsley Associates on exactly how to navigate uncertainty:

> -Enhance asset value through proactive asset management. Listen to your tenants and preserve those occupancy levels.
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> -Target efficiency and cost control – we talked about it before, energy is the largest controllable operating cost. Be efficient.
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> -Fine-tune your team – put your best people in key positions and keep them focused and engaged.
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> -Stay close to clients and employees – exceptional client service is critical, understand your owner's priorities and your tenants' needs.
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> -Communicate and be responsive
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> -And don't forget to maintain a long-term perspective – the markets will come back.

With a son about to start college, I would like to close optimistically with something I took from Fareed's book "The Post-American World." It's not that America is behind the rest of the world, it's just that the rest of the world is catching up. If anything, there are more opportunities than ever before, but now those opportunities are presented on a larger, more global scale. And though American students have never led the world in testing scores, they always seem to grow up be great problems solvers and creative thinkers. Our kids are going to take us to the next level, and it will be fun to watch.

Let's position ourselves for the upcoming recovery. Look around you. The BOMA business network is incredible. Use it. Share great ideas and solutions. Get creative and solve problems together and take those insights back to your companies. Let's make our value-add our advantage.