MARKETWATCH

BOSTON
SECOND QUARTER 2010

FHO PARTNERS

Commercial
Real Estate
Value-Addvisors

A DTZ AFFILIATE

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Executive Overview

ECONOMY

While the worst of the recession may be over, greater Boston real estate fundamentals remained flat through the first half of 2010. According to the latest report from the Bureau of Labor Statistics, the national economy shed 125,000 jobs in June – an expected decline due to the cut backs in Census workers. However, private-sector employers added only 83,000 jobs in June – about half of the payroll growth the country needs to lower the national unemployment rate of 9.5%. While national unemployment did, in fact, decline between May and June, analysts believe it is because of a reduction in labor force participation, not due to increased employment. In fact, the U-6 unemployment rate, which includes those who have had to settle for part-time work as well as discouraged workers who have temporarily halted their job search clocked in at 16.5% in June 2010 – static over mid-year 2009.

Massachusetts has fared only slightly better than the nation with an unemployment rate of 9.2%. This number represents a statewide employment loss of nearly 5.0% since the recession began in late 2007. According to the latest figures from the U.S Bureau of Labor Statistics, the state's U-6 unemployment rate stands at 15.0%. While education and health services were among the only sectors to add jobs statewide, up 1.0% between April and May, it will take considerable investment from private employers before we see notable job growth.

MARKET SUMMARY

During the first half of 2010, greater Boston posted negative absorption of 1.2 million square feet (msf). While this does not signal a recovery, it is a marked improvement over mid-year 2009 when the region posted absorption of negative 5.1 msf. As a result of anemic leasing activity, the overall availability rate stands at 20.9%. While fewer sublet availabilities have come to market than in the 2001 to 2003 recession, dwindling demand has caused the erosion of average asking rents – down 7.7% in Boston in the past 12 months and 7.5% and 6.7% in the Cambridge and Suburban office sectors, respectively.

OUTLOOK

As federal stimulus funds wane, economic recovery will be contingent upon the business investment of private-sector employers. Rather than focusing on short-term balance sheet growth, businesses must begin investing in human capital. Until we begin adding enough jobs to stimulate growth, the greater Boston availability rate will remain elevated. While we have likely seen the worst of the market contraction, it is unlikely that we will see any real recovery until at least the first half of 2011. With few exceptions, we anticipate overall average asking rents to remain static or even decline through the end of 2010. As a result, we will continue to see a "flight to quality'" as those tenants who are able to take advantage of the lower prices of higher class space continue to upgrade.

Overall Market Statistics YTD 2010 Summary

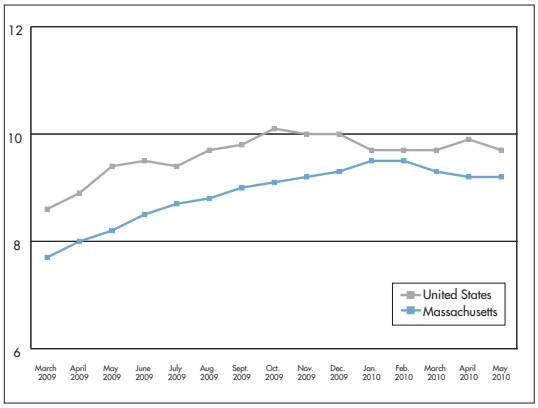
	Asking Rent	Vacancy	Absorption
Boston	⇓	⇑	⇓
Cambridge	⇔	⇓	⇑
Suburbs	⇔	⇑	⇓

The State of the Economy by the Numbers

	Q2 2009	Q2 2010
DJIA	8280.75	8300.02
US Unemployment	9.5%	9.5%
MA Unemployment	8.2%	9.2%
US Employment (June 2010)	140,038,000	139,119,000
MA Employment (May)	3,188,984	3,165,900

Sources: Dow Jones, Bureau of Labor & Statistics

Unemployment Rate

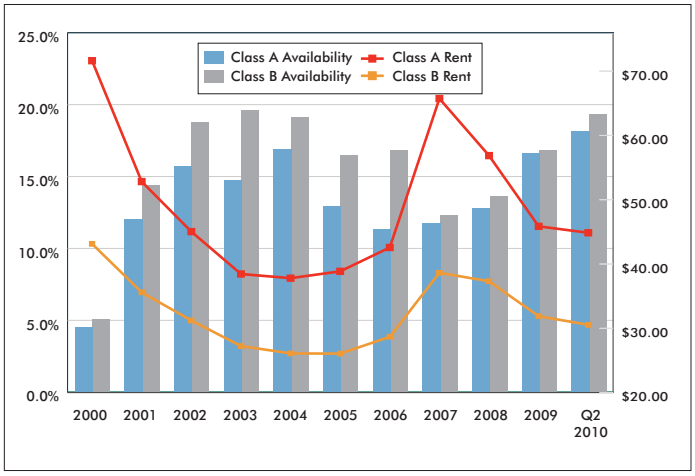


Greater Boston Market Snapshot

	Q2 2009	Q2 2010
Overall Availability	19.5%	20.9%
Average Rent (Office)	$32.29 psf	$30.13 psf
Net Absorption YTD 2010	(5,060,920) sf	(1,232,221) sf

Boston Market Overview

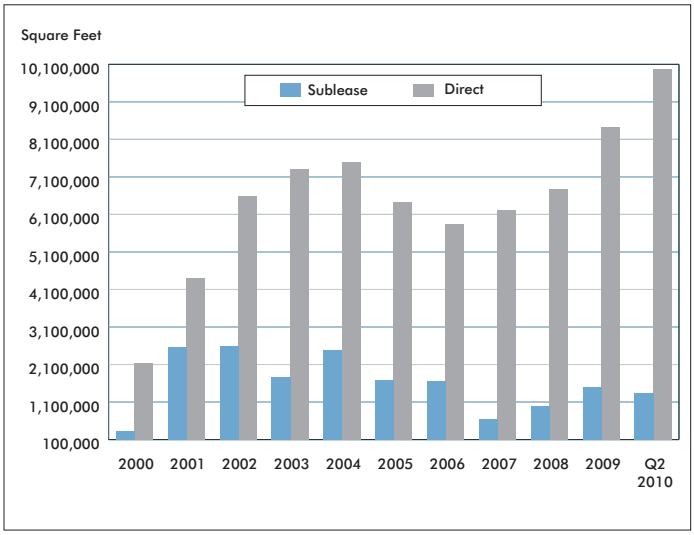
Boston Overall Availability vs. Average Asking Rent by Class



Market Highlights

Inventory	59,750,735 sf
Availability Rate	18.9%
Net Absorption YTD 2010	(611,626) sf
Average Asking Rent	$39.57 psf

Boston Direct Available vs. Sublease Available



The Boston office market remained essentially unchanged through the second quarter of 2010. While conditions are no longer worsening, we have yet to see any significant signs of improvement. Although some larger deals were completed, they were counteracted by numerous smaller blocks of available space that were added to the market. While it is unlikely that the market will see further detriment, marked improvement will likely not be evident in the next two quarters.

- Net absorption remains negative, totaling (611,626) square feet (sf). While this represents an improvement over mid-year 2009 when absorption stood at (1.9) million square feet (msf), Boston is still experiencing the aftershocks of a nearly 5.0% loss of employment since the recession began in late 2007. Only two submarkets have posted positive absorption year-to-date: Back Bay, at 194,938 sf and South Boston Waterfront, at 68,705 sf. This is due to Bain Capital's 208,000 sf lease at the Hancock Tower in the Back Bay and the delivery of Fan Pier (25% preleased to Fish & Richardson) in the South Boston Waterfront.

- Overall availability in Boston is up 2.2 percentage points over both mid-year and year-end 2009. While measured leasing activity has certainly slowed the rate at which availabilities are increasing, it should be noted that we have yet to see a significant decline in the overall availability rate. The most noted upticks in availabilities have occurred in the Class B and C markets. Class B posted a 3.0 percentage point increase over mid-year 2009 while Class C availability is up 4.1 percentage points in the same time period. However, Class A availabilities are up significantly less – 1.5 percentage points over year-end and 1.8 percentage points over mid-year 2009. This indicates that we are still experiencing the 'flight-to-quality" phenomenon.

- The catalyst for "flight-to-quality" is primarily lower asking rents on the low-rise floors of Class A towers. While large blocks of contiguous space on the higher floors of Class A towers are scarce (and commanding a premium), overall asking rents are down year-over-year to $39.57 per square foot (psf) from $42.85 psf a year ago. This represents a 7.6% decline in the past 12 months. Overall asking rents in Back Bay are down 6.9% year-over-year to $42.56 psf, while overall asking rents in Financial District are down 7.0% year-over-year to $42.72 psf.

Market Makers

The Commonwealth of Massachusetts signed a ten-year lease at One Congress Street for 61,000 sf.

Bain Capital signed a lease at 200 Clarendon Street for 208,000 sf.

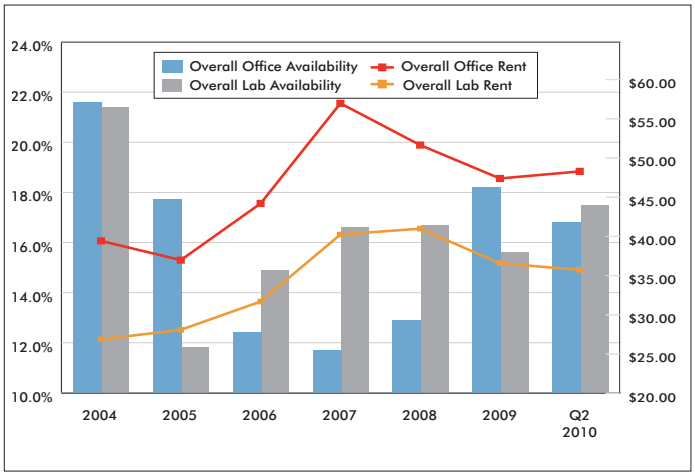
Liberty Mutual executed a short term expansion for 80,000 sf at 222 Berkeley Street.

Historical Perspective

At 18.9%, Boston's overall availability rate is higher than it has been since its peak of 19.4% in 1991. The 11.3 msf of available space is the highest we have seen in the past two decades. However, while net absorption totaled (611,626) sf year-to-date, it has shown improvement over year-end 2009 when it reached (1.95) msf.

Cambridge Market Overview

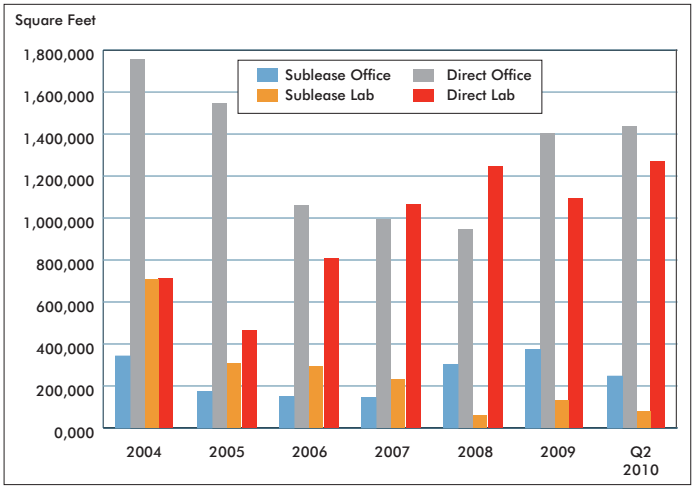
Cambridge Overall Availability vs. Average Asking Rent



Market Highlights

Office	
Inventory	10,046,144 sf
Availability Rate	16.8%
Net Absorption YTD 2010	91,089 sf
Average Asking Rent	$35.73 psf
Lab	
Inventory	7,723,685 sf
Availability Rate	17.5%
Net Absorption YTD 2010	(36,046) sf
Average Asking Rent	$48.29 psf NNN

Cambridge Direct Available vs. Sublease Available



Although Cambridge has been somewhat insulated from the recession, it is still not showing signs of significant growth. In the office sector, the East Cambridge submarket was the only one to show positive absorption. Nevertheless, due to the concentration of high technology and biopharmaceutical tenants, Cambridge, overall, has fared better than its neighboring markets.

OFFICE MARKET

- The Cambridge office market finished the first half of the year with a 16.8% overall availability rate. This represents a decline of 90 basis points since year-end 2009.
- Overall asking rents for office space averaged $35.73 psf. This represents a decline of 2.0% since year-end 2009 and a decline of 7.5% year-over-year.
- The office market posted positive absorption of 91,019 sf year-to-date – a notable increase over the (298,978) sf reported at mid-year 2009.

LAB MARKET

- In the lab market, availability remained flat, ticking up a nominal 10 basis points since year-end 2009 to 17.5%
- Asking rents for lab space, while declining 7.0% year-over-year, have actually increased 2.0% in the first half of 2010 to $48.29 psf.
- The Cambridge Lab market continued to post negative absorption through the first half of the year, totaling (36,046) sf year-to-date. This marks a decline over mid-year 2009 when lab absorption totaled 69,199 sf.

Market Makers

Blackbaud signed a five-year sublease from Monitor for 33,000 sf at 2 Canal Park

Start-up company **Foundation Medicine** signed a 22,000 sf deal for the 4th and 5th floors at One Kendall Square, Building 300.

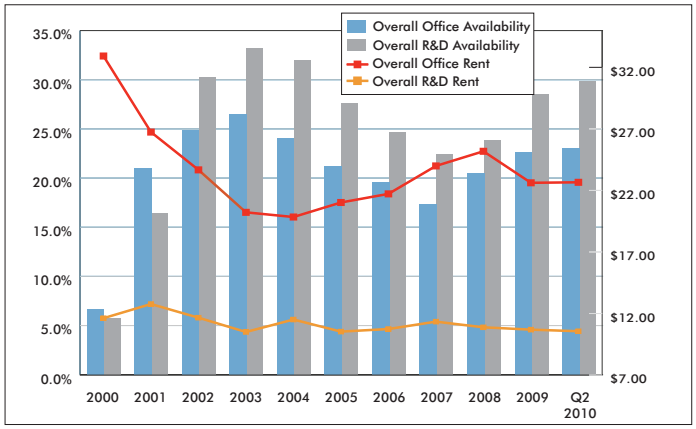
Aileron signed a five-year deal for 20,000 sf of lab space at 281 Albany Street.

Historical Perspective

At 16.8%, overall availability for the Cambridge office market has decreased 1.4 percentage points from year-end 2009. This is largely attributable to the positive absorption year-to-date of 91,089 sf. Availability in the Cambridge lab market has increased slightly to 17.5% from year-end 2009 when it was 15.6%. This resulted in slight negative absorption of (36,046) sf. However, these numbers are healthier than during the downturn of 2001 to 2003 when the combined office and lab availability rate peaked at 25.7% and absorption totaled (1.1) msf.

Suburban Market Overview

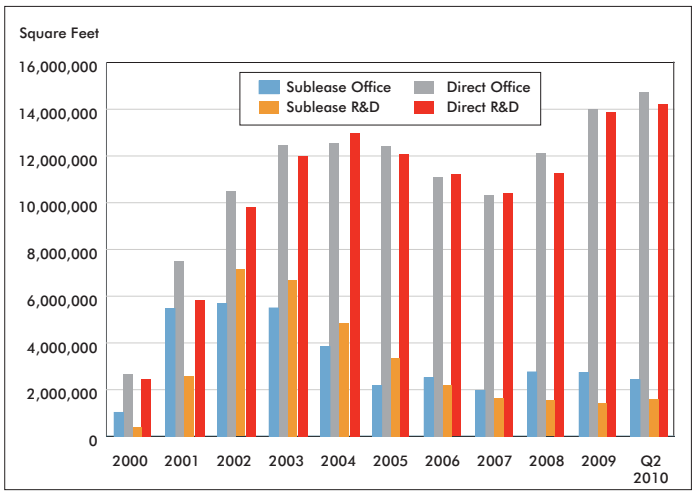
Suburban Overall Availability vs. Average Asking Rent



Market Highlights

Office	
Inventory	74,452,776 sf
Availability Rate	23.0%
Net Absorption YTD 2010	82,295 sf
Average Asking Rent	$22.66 psf
R&D	
Inventory	52,972,275 sf
Availability Rate	29.9%
Net Absorption YTD 2010	(757,933) sf
Average Asking Rent	$10.56 psf NNN

Suburban Direct Available vs. Sublease Available



The overall suburban market displays striking disparity between the office and R&D sectors. While the office market is showing positive absorption for the first time since the recession began in late 2007, the R&D market is not faring as well. Although a discernable recovery may not be immediate in the office sector, it is likely that conditions will not erode further. The same cannot be said of the R&D market, but it should be noted that the rate of deterioration in overall market conditions has drastically decelerated since the end of 2009.

- The suburban office market posted positive net absorption of 82,295 sf year-to-date. This is a considerable improvement over mid-year 2009 when absorption stood at (1.29) msf. While still negative, overall suburban R&D posted (757,933) sf of absorption year-to-date – also an improvement over 12 months ago when absorption totaled (1.56) sf.

- Overall availability in the office market remained virtually unchanged year-over-year, increasing a mere 70 basis points to 23.0%. R&D availability continued to increase through the first half of 2010. At 29.9%, it has risen 3.2 percentage points in the past 12 months.

- As a result of significant availability, asking rents for office space are down 6.3% year-over-year to $22.66 psf but have remained flat since year-end 2009. At $10.56 psf triple net, R&D asking rents have remained static for the past 12 months, declining a nominal 0.8%.

Market Makers

Symantec renewed for 59,000 sf at 266 Second Avenue in Waltham.

NRT Realogy / Coldwell Banker leased 55,414 sf at 52 Second Avenue in Waltham.

Historical Perspective

While overall net absorption for the suburban office and R&D market stands at (675,638) sf with an availability rate of 25.9%, this is not the worst we have seen. The downturn of 2001 to 2003 led to 21.0 msf of negative absorption while the availability rate soared to nearly 30%. At 82,295 sf year-to-date, net absorption for the suburban office market is positive for the first time since 2007. Despite negative net absorption and rising availability in the suburban R&D market, asking rents have remained steady hovering between $10.50 and $12.00 psf, triple net for the past eight years.

Market Summary

Market	Total Inventory	Total Available	Availability Rate	Total Vacant	Vacancy Rate	YTD 2010 Net Absorption	Direct Weighted Average Rent
BOSTON OFFICE	59,750,735	11,285,591	18.9%	6,521,158	10.9%	(611,626)	$39.57
Back Bay	12,182,324	1,524,321	12.5%	917,109	7.5%	194,398	$42.56
Charlestown	1,748,336	220,065	12.6%	144,929	8.3%	(19,534)	$23.67
Fenway	1,911,890	71,131	3.7%	41,700	2.2%	(33,531)	$30.29
Financial District	28,202,230	6,046,226	21.4%	3,286,514	11.7%	(580,109)	$42.72
Government Center	1,878,278	397,565	21.2%	294,797	15.7%	10,207	$34.39
Midtown	1,863,609	384,487	20.6%	197,178	10.6%	(49,369)	$24.74
North Station	1,638,642	260,902	15.9%	108,587	6.6%	(4,849)	$28.37
South Boston Waterfront	6,187,511	1,756,315	28.4%	1,167,802	18.9%	68,705	$29.26
South Station	4,137,915	624,579	15.1%	362,542	8.8%	(197,544)	$36.07
CAMBRIDGE OFFICE	10,046,144	1,684,037	16.8%	994,716	9.9%	91,089	$35.73
Alewife/West Cambridge	1,714,404	397,001	23.2%	276,424	16.1%	(44,536)	$26.18
East Cambridge	6,160,198	1,034,633	16.8%	606,569	9.8%	182,481	$40.59
Mass Avenue Corridor	2,171,542	252,403	11.6%	111,723	5.1%	(46,856)	$32.38
CAMBRIDGE LAB	7,723,685	1,351,517	17.5%	981,951	12.7%	(36,046)	$48.29*
Alewife/West Cambridge	533,311	64,287	12.1%	64,287	12.1%	7,007	$33.79
East Cambridge	4,872,719	970,342	19.9%	681,030	14.0%	(15,762)	$49.46
Mass Avenue Corridor	2,317,655	316,888	13.7%	236,634	10.2%	(27,291)	$54.13
SUBURBS OFFICE/R&D	127,425,051	32,980,899	25.9%	23,082,502	18.1%	(675,638)	$22.66**
128 Central	41,240,865	9,845,348	23.9%	6,758,360	16.4%	(325,433)	$25.65**
128 North	9,628,176	2,744,121	28.5%	1,970,404	20.5%	104,225	$19.63**
128 South	14,492,982	3,712,153	25.6%	2,521,480	17.4%	(314,145)	$19.94**
3/24 South	1,982,663	482,665	24.3%	424,910	21.4%	31,580	$21.46**
495 Central	17,874,486	4,463,393	25.0%	3,087,914	17.3%	64,864	$19.90**
495 North	31,756,702	10,044,968	31.6%	7,055,244	22.2%	(177,625)	$18.17**
495 South	4,285,045	1,007,547	23.5%	782,905	18.3%	(79,277)	$19.95**
Inner Suburbs	6,164,132	680,704	11.0%	481,285	7.8%	20,173	$23.14**
TOTAL	204,945,615	47,302,044	23.1%	31,580,327	13.8%	(1,232,221)	$30.13**

*Rents quoted on NNN basis **Average of office rents only

Glossary of Terms

METHODOLOGY

The information included in this report is the result of a compilation of information on Class A, B and C office, R&D and investment properties located in the Boston area. The information was obtained by FHO Partners from representatives of each property.

All of the information gathered is stored in a FHO Partners database which is updated quarterly. From this database, total inventory, vacancy rate, rental rate and absorption figures may be calculated and presented.

Total inventory may change from year to year as a result of newly constructed or newly renovated buildings, recently remeasured properties, or significant change or deletion of a particular building status. The database is thoroughly checked and balanced from year to year. The appropriate adjustments are made in order to balance the figures and calculate the most accurate vacancy and absorption figures.

DEFINITIONS

Inventory:

Includes all existing competitive office and R&D buildings over 20,000 sf as well as significant buildings less than that size. Under construction, government, medical, educational and 100% owner-occupied buildings are not included.

Direct Space:

Space available directly from the building owner. Includes space available for occupancy within the next 24 months. Does not include space in under construction buildings.

Sublease Space:

Space available through a lessee to a third party for the remainder of the original lease term and/or beyond. Includes space being actively marketed.

Vacancy Rate:

Space, available both directly and by sublease, that is currently vacant and being marketed for immediate occupancy. Does not include space under construction.

Availability Rate:

Available space is generally defined as space that is being actively marketed and/or available for occupancy within the next 24 months.

Construction Completions:

Buildings which have received their certificate of occupancy in the stated time period.

Under Construction:

Buildings which have had excavation work commence, but have not yet received their certificate of occupancy.

Office:

Space designed for general office use. Buildings are generally two or more stories and offer tenants a higher-level of finish than R&D space.

R&D:

Space designed for high technology, office or light industrial use. Buildings are generally one or two stories.

Net Absorption:

The net change in occupied space over a given period of time. Calculations are based on available space.

Rental Rates:

Gross: Rents which include tax and operating expenses, but generally not electricity.

Triple Net:

Rents where the tenant is directly responsible for all tax, operating and utility expenses.

Weighted Average Rent:

An average rental rate that is weighted by the amount of square footage available at each respective rental rate.

Submarket Map

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