

KNIGHT DORIN & ROUNTREY

2011 Real Estate Market Participant Survey



of Central Virginia

CENTRAL VIRGINIA MARKET INSIGHT – 2011

Commercial Real Estate Market Outlook for 2011 – As of first quarter 2011 the experts' views regarding the 2011 local CRE market were dramatically more upbeat than they have been in the past 3 years. This optimistic outlook is detailed in the charts that follow. The residential housing market still has not found a bottom. However, the CRE market has firmed and most agree – that recovery is under way. The economy of Central Virginia remains better than many other areas in the country and the Richmond area actually posted employment gains in 1Q 2011 for the first time in 3 years. Growing government deficits and mounting debt remain a source of much concern relative to the long term economic outlook. Commercial real estate values are benefiting from easier financing, lower cap rates and stabilizing or even increasing rents. Although many of our survey participants as of early 2011 still felt financing availability was sub-par, a few phone calls revealed a dramatic improvement in financing prospects by mid-2011. By most accounts 2011 will be much better than 2010 for CRE.

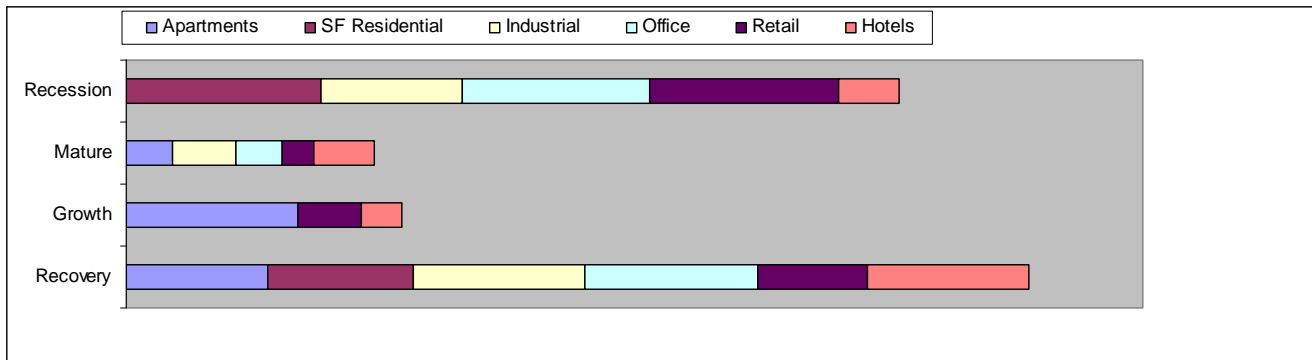
- Overall Cap Rates are anticipated to decline 10 to 40 basis points for 2011.
- Unleveraged Discount Rates are anticipated to decline 60 to 160 basis points for 2011.
- Expected vacancy rates declined in all categories.
- Mortgage financing availability is improving for Office, Industrial and Retail properties in 2011. Single family development has the lowest rating and shows no improvement from 2010.
- Marketing times are projected to decrease in 2011.
- Negative trends of the past three years have abated and the CRE market is poised to advance.

CURRENT STAGE OF REAL ESTATE MARKET CYCLE

	Recovery	Growth	Mature	Recession
Apartments	34.6%	42.3%	11.5%	00.0%
Single Family Residential	36.0%	0.0%	0.0%	48.0%
Industrial	42.3%	0.0%	15.4%	34.6%
Office	42.3%	0.0%	11.5%	46.2%
Retail	26.9%	15.4%	7.7%	46.2%
Hotels	40.0%	10.0%	15.0%	15.0%

Most of the results show a split of opinion - primarily between Recovery and Recession. Apartments were the only category where no one indicated recession. Single family residential, office and retail all had a higher percentage of being in a recession than in any other part of the cycle. From the responses it can be gleaned that a new upward cycle has begun with apartments now in full recovery. Industrial has moved to a higher percentage indicating recovery. It is followed by office, hotels, single family residential and retail. Single family residential is out of sync with most cycles in the past, but it is the property type that was most overbuilt in the last economic expansion. Hotels usually recover at the end of the cycle and it is noted that there was not a strong response on this property type and the indication is therefore suspect.

LIKELY BEGINNING OF RECOVERY STAGE



This chart provides a forecast of when recovery will start for the various property types from the respondents who indicated we were still in recession. All respondents indicated that Apartments were no longer in recession and were in recovery or better. None of the recession respondents thought that SF Residential would recover this year. Approximately 50% thought it would happen in 2012 with the other 50% split between 2013 and 2014. Industrial is projected to make a comeback in 2012, with over 70% of the respondents indicating a recovery during that year. Office had similar results with approximately 75% forecasting recovery in 2012. Retail also indicated a recovery in 2012 with 70% of the responses indicating second or fourth quarter. Hotel recovery was undecided with one third of the responses falling in each of the years 2011, 2012 and 2013.

	1 st Quarter	2 nd Quarter	3 rd Quarter	4 th Quarter
SF Residential				
2011	0%	0%	0%	0%
2012	16.7%	25.0%	0%	8.3%
2013	16.7%	8.3%	0%	0%
2014	25.0%	0%	0%	0%
Industrial				
2011	0%	0%	28.6%	0.0%
2012	28.6%	12.5%	12.5%	12.5%
2013	0%	0%	0%	0%
Retail				
2011	0%	0%	0%	0.0%
2012	0.0%	50.0%	0.0%	20.0%
2013	0.0%	10.0%	0%	0.0%
2014	10%	10%	0%	0%
Office				
2011	0%	8.3%	0%	0%
2012	16.7%	25.0%	16.7%	16.7%
2013	8.3%	0%	0%	0%
2014	8.3%	0%	0%	0%
Hotels				
2011	0%	0%	33.3%	0%
2012	0%	0%	0%	33.3%
2013	0%	0%	0%	33.3%

INVESTMENT CRITERIA

Office Market				
CATEGORY	2010 Range	2010 Average	2011 Range	2011 Average
Holding Period (Years)	7.0-10.0	8.0	5.0 – 10.0	8.4
Income (Growth Rate)	(5.0)% - 3.0%	.8%	0% - 6.0%	2.5%
Operating Expenses (Growth Rate)	1.0% - 5.0%	2.9%	1.0% - 3.0%	2.5%
Vacancy Loss	10.0% - 12.0%	10.3%	5.0% – 15.0%	9.8%
Going-In Capitalization Rate	8.0% - 10.5%	9.3%	8.0% - 11.0%	8.9%
Terminal Capitalization Rate	8.5% - 11.0%	9.9%	8.0% - 12.0%	9.5%
Discount Rates (Unleveraged IRR)	9.0% - 16.0%	12.1%	9.5% - 12.0%	10.8%
Equity Yield (Leveraged IRR)	11.0% - 18.0%	13.7%	12.0% - 20.0%	14.2%
Tenant Retention Rates:				
Class A	50% - 90%	62%	50% - 85%	68%
Class B	40% - 90%	59%	50% - 85%	64%
Months vacant between tenants:				
Class A	8.0 – 20.0	13.0	6.0 – 12.0	9.9
Class B	10.0 – 24.0	15.0	6.0 – 18.0	12.1
Retail Market				
CATEGORY	2010 Range	2010 Average	2011 Range	2011 Average
Holding Period (Years)	7.0 – 10.0	8.0	7.0 – 10.0	9.0
Income (Growth Rate)	(5.0)% - 3.0%	.8%	(5.0)% - 3.0%	2.0%
Operating Expenses (Growth Rate)	2.0% - 4.0%	2.8%	1.0% - 3.0%	2.7%
Vacancy Loss	7.0% - 15.0%	11.7%	8.0% - 20.0%	11.0%
Going-In Capitalization Rate	8.0% - 10.0%	9.2%	8.0% - 12.0%	9.1%
Terminal Capitalization Rate	9.0% - 10.5%	9.8%	8.0% - 13.0%	9.6%
Discount Rates (Unleveraged IRR)	10.0% - 18.0%	12.6%	9.5% - 12.0%	11.0%
Equity Yield (Leveraged IRR)	13.0% - 18.0%	15.3%	12.0% - 16.0%	14.3%
Tenant Retention Rates:				
Neighborhood	40% - 85%	63%	50% - 80%	64%
Community	40% - 85%	58%	60% - 80%	67%
Months vacant between tenants:				
Neighborhood	6.0 – 24.0	11.1	6.0 – 18.0	10.4
Community	6.0 – 24.0	11.5	4.0 – 18.0	9.0
Apartment Market				
CATEGORY	2010 Range	2010 Average	2011 Range	2011 Average
Holding Period (Years)	7.0 – 10.0	8.5	7.0 – 10.0	9.0
Income (Growth Rate)	(2.0)% - 5.0%	1.7%	2.0% - 5.0%	3.0%
Operating Expenses (Growth Rate)	2.0% - 4.0%	2.7%	1.0% - 4.0%	3.0%
Vacancy Loss	6.0% - 10.0%	7.8%	4.0% - 10.0%	6.8%
Going-In Capitalization Rate	7.0% - 9.0%	8.0%	6.0% - 9.0%	7.6%
Terminal Capitalization Rate	8.0% - 9.5%	8.8%	7.0% - 9.0%	8.3%
Discount Rates (Unleveraged IRR)	9.5% - 12.0%	10.4%	8.0% - 11.0%	9.7%
Equity Yield (Leveraged IRR)	12.0% - 16.0%	13.5%	12.0% - 15.0%	13.2%

Industrial Market				
CATEGORY	2010 Range	2010 Average	2011 Range	2011 Average
Holding Period (Years)	7.0 -15.0	10.1	5.0 - 10.0	9.1
Income (Growth Rate)	(5.0)% - 3.0%	.8%	1.0% - 3.0%	2.4%
Operating Expenses (Growth Rate)	1.0% - 3.0%	2.2%	1.0% - 3.0%	2.5%
Vacancy Loss	7.0% - 12.0%	9.6%	5.0% - 15.0%	10.0%
Going-In Capitalization Rate	8.0% - 10.5%	9.4%	8.0% - 11.0%	9.0%
Terminal Capitalization Rate	9.0% - 12.0%	10.3%	8.0% - 12.0%	9.5%
Discount Rates (Unleveraged IRR)	10.0% - 15.0%	11.7%	9.5% - 12.0%	11.1%
Equity Yield (Leveraged IRR)	12.0% - 18.0%	13.9%	12.0% - 16.0%	14.0%
Tenant Retention Rates:				
Office/Whse.	50% - 90%	71.5%	40% - 85%	65%
Distribution	50% - 80%	65.6%	50% - 85%	66%
Months vacant between tenants:				
Office/Whse.	4.0 – 18.0	11.1	3.0 – 18.0	11.5
Distribution	6.0 – 24.0	13.3	4.0 – 18.0	11.6

LAND LEASE RATES

	Range	Average	Change From 2010
Cap Rate (with flat rent)	6.50% - 10.00%	9.11%	-54 basis point
Cap Rate (average 2% ann. escalation)	6.00% - 10.00%	8.25%	-75 basis points

RESERVES, LEASING COSTS, AND TI'S

Include in Cap Rate Analysis	Yes	No
Reserves for Replacement	83%	17%
Leasing Commissions	65%	35%
Tenant Improvement Costs	59%	41%

COST OF SALE

Price Range	Low	High	Average
<\$500K	4%	10%	6.7%
\$500K to \$1M	3%	10%	6.2%
\$1M to \$3M	2%	9%	4.9%
\$3M to \$5M	1%	8%	4.2%
>\$5M	.5%	7%	3.2%

ENTREPRENEURIAL PROFIT

Basis	Year	Low	High	Median
Improvements Only	2011	10%	15%	11%
	2010	10%	20%	15%
	2009	10%	25%	15%
	2008	8%	20%	12%
	2007	10%	18%	15%
	2006	10%	25%	15%
	2005	10%	30%	15%
Land and Improvements	2011	10%	25%	15%
	2010	10%	30%	15%
	2009	10%	20%	14%
	2008	10%	15%	10%
	2007	9%	25%	16%
	2006	8%	35%	15%
	2005	8%	30%	15%

LOT PRICE RATIOS

Improved Property Price	Lot Value Ratio Range as % of Total Price					Median				
	2007	2008	2009	2010	2011	2007	2008	2009	2010	2011
Starter Housing \$200-\$300K	13-34%	20-40%	20-30%	20-35%	20-25%	25%	28%	28%	25%	24%
Move Up Housing \$300-\$400K	13-33%	20-35%	20-28%	20-30%	20-25%	25%	25%	25%	22%	25%
Luxury Housing \$400-600K	13-30%	15-35%	20-28%	20-25%	20-30%	25%	25%	23%	23%	25%
High End Luxury Housing Over \$600K		15-35%	20-25%	20-25%	20-25%		25%	20%	22%	30%
Townhouse					25-33%					28%

AVAILABILITY OF MORTGAGE FINANCING

Property Type	Past 12 months	Next 12 months
Apartments	2.0	2.3
Hotels	1.0	1.4
Industrial	1.5	1.6
Office	1.5	1.6
Retail	1.5	1.6
Residential (A & D)	1.0	1.0
Rating Scale:	1 = Inadequate	2 = Adequate
		3 = Abundant

REAL ESTATE LIQUIDITY – MARKETING PERIOD

Property Type	% of Responses		
	< 6 Months	6-12 Months	> 12 Months
Retail			
Free-standing single user retail	50.0%	35.7%	14.3%
Small unanchored retail center	14.3%	71.4%	14.3%
Neighborhood retail center	38.5%	53.8%	7.7%
Community retail center	33.3%	50.0%	16.7%
Regional retail center	16.7%	58.3%	25.0%
Multi-family			
Apartment (> 120 units)	69.2%	30.8%	0.0%
Apartment (< 120 units)	53.8%	38.5%	7.7%
Office			
Large - well leased	46.7%	46.7%	6.7%
Large – poorly leased	6.7%	20.0%	73.3%
Small – well leased < 20,000 sf	31.3%	62.5%	6.3%
Small – poorly leased < 20,000 sf	6.3%	18.8%	75.0%
Industrial			
Small single user	43.8%	43.8%	12.5%
Multi-tenant flex/bulk distribution	18.8%	62.5%	18.8%
Manufacturing Buildings	6.3%	25.0%	68.8%
Special use properties			
Banks, historic, churches, etc.	0.0%	33.3%	66.7%
Land			
Single family development	6.3%	6.3%	87.5%
Multi-family development	12.5%	62.5%	25.0%
Retail	0.0%	28.6%	71.4%
Office	0.0%	17.6%	82.4%
Industrial	0.0%	25.0%	75.0%

	No Change	Increase	Decrease
Marketing period change from 2010	65%	15%	20%

This Real Estate Market Survey is an annual publication of Knight, Dorin & Rountrey. This is our 19th year publishing the survey. At the beginning of each year we send our survey questionnaire to over 200 of the most active and respected commercial real estate professionals in Central Virginia. The survey participants include real estate brokers, developers, investors, consultants and lenders. We hope this survey proves useful and welcome your comments and suggestions.

CORPORATE PROFILE

KNIGHT, DORIN & ROUNTREY

REAL ESTATE ANALYSTS

REAL ESTATE MARKET KNOWLEDGE

- Leading real estate appraisal and consulting company founded in 1986
- Strong network with other real estate professionals
- Comprehensive commercial real estate transaction database covering most of the developed areas of Virginia (outside of Northern Virginia)
- Over 1,000 commercial lease and sale transactions analyzed annually
- Clients – include financial institutions, government agencies, law firms, investors, developers, and major corporations

COMMERCIAL APPRAISAL SERVICES FOR

- Office, retail, industrial, apartment, subdivision, and special purpose properties
- Mortgage, securitization, investments, and exchanges
- Buyer, seller, tenant – decision support analysis
- Estates, trusts, partitions, partial interests, valuation subject to environmental impairment
- Portfolio evaluation
- Appraisal reviews
- Litigation support
- Bankruptcy
- Estate planning

MARKET COVERAGE – VIRGINIA

- Richmond-Petersburg MSA
- Newport News-Hampton Area
- Fredericksburg Area
- Williamsburg Area
- Charlottesville MSA

OWNER

Edward G. Knight, MAI, SRA

PROFESSIONAL STAFF

J. Parks Rountrey, MAI, SRA
William A. Hopkins, Jr., MAI, SRA
Michael S. Larson
Michael A. Knight
James A. Wood, Jr.

ADVISORY & CONSULTING SERVICES

- Market studies
- Feasibility analysis
- Project development analysis
- Litigation support
- Highest and best use analysis
- Lease analysis
- Asset evaluation
- Strategic planning
- Due diligence research and advice
- Site selection
- Land use analysis

Contact Us

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**CENTRAL VIRGINIA
MARKET SURVEY HISTORICAL SUMMARY 2011**
(Response Averages)

