

KNIGHT DORIN & ROUNTREY

**Central Virginia
2015 Real Estate Market Participant Survey**

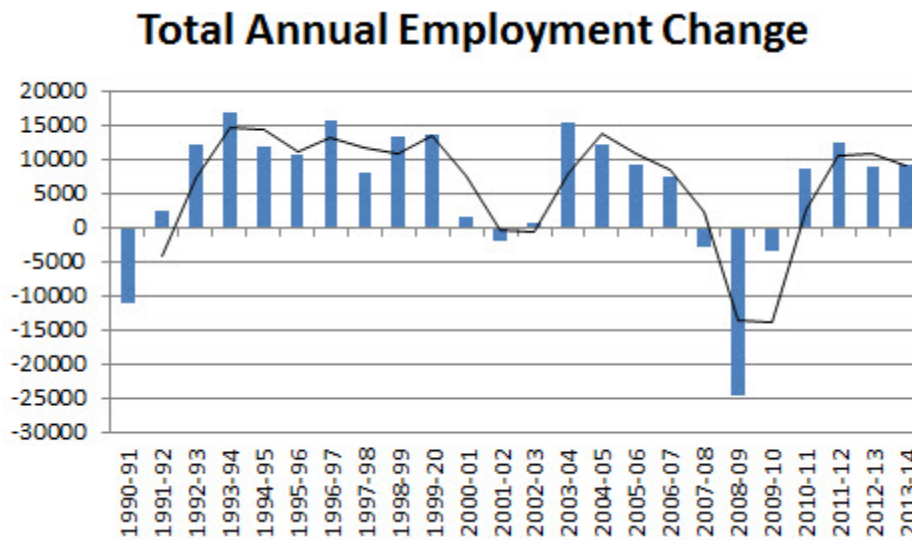


23rd Year Edition

CENTRAL VIRGINIA MARKET INSIGHT – 2015

Commercial Real Estate Market Outlook for 2015 – The Richmond Area economy continued on its slow path of improvement in 2014 and most economists expect a similar course in 2015. These economic fundamentals of demand are reflected in the results of our 2015 survey for expectations of CRE as it was nearly identical to 2014. Sixty nine percent of the respondents thought the market would be better in 2015 and 31% thought it would be the same – none indicated that it would be worse. Local experts see a stable to moderately improving CRE environment.

According to the Bureau of Labor Statistics, the 2014 Richmond MSA economy as reflected by job growth increased by 9,300 in 2014, which was preceded by growths of 8,900 in 2013, 12,400 in 2012 and 8,600 in 2011. This is a rather tepid rate of employment expansion relative to historical norms (see chart below). The trend line is a two year moving average. It shows that we seem to have leveled off now without ever reaching the growth peaks seen the past two recoveries. This coupled with the loss of 30,900 jobs during the Great Recession of 2007-09 has led the slow path of improvement for CRE.



Richmond MSA – Bureau of Labor Statistics

The good news is that at the end of 2014 the total employment of 631,100 was 8,300 above the peak of 622,800 in 2007 demonstrating a complete recovery from the recession. Health Services and Care remains the fastest growing industry sector, which has been the driving factor in the construction of medical related facilities. It is noted that the rate of growth has been slowing and there are reports of recently constructed facilities absorbing slower than the recent past. One possible trend to watch is manufacturing employment, which has been on a downward spiral for decades. The past two years have shown some slight growth (400 and 100) which maybe indicating a bottom has formed. The Shandong Tralin Paper Company is expected to create 2,000 new jobs in Chesterfield over the next five years. We have heard rumors of other significant manufacturing companies looking at Richmond.

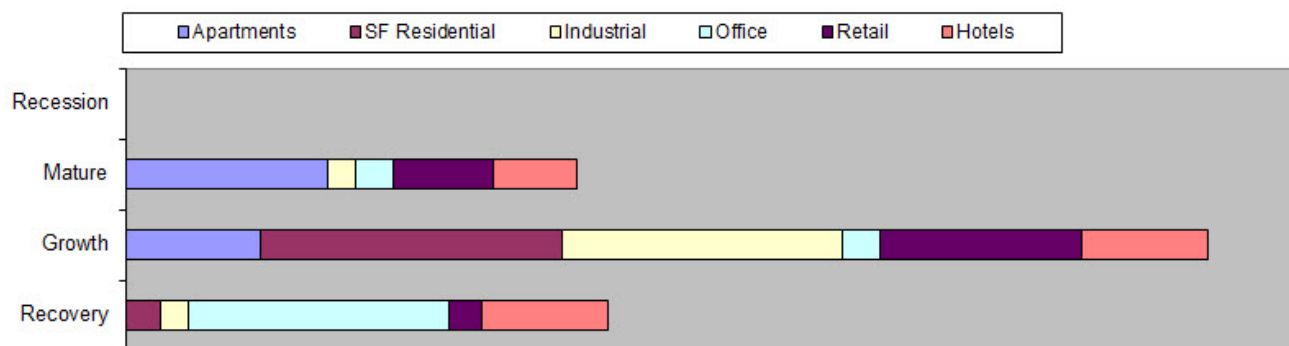
Our survey indicates that vacancies are down for all property types. The improvement of fundamental demand (positive job growth), scarcity of product and continued low interest rates should lead to a greater amount of new construction during 2015 and for several years to come. A recent ULI forecast for national CRE indicated that we should have three more years of favorable real estate conditions¹. We forecast a similar situation for the Richmond CRE market.

¹ “Urban Land Institute forecast sees three years of continued strength for commercial real estate”, Virginia Business, April 9, 2015

CURRENT STAGE OF REAL ESTATE MARKET CYCLE

	Recovery	Growth	Mature	Recession
Apartments	0.0%	40.0%	60.0%	0.0%
Single Family Residential	10.0%	90.0%	0.0%	0.0%
Industrial	8.3%	83.3%	8.3%	0.0%
Office	77.8%	11.1%	11.1%	0.0%
Retail	10.0%	60.0%	30.0%	0.0%
Hotels	37.5%	37.5%	25.0%	0.0%

This is the first year since the Great Recession that none of the respondents indicated a property type was in recession. In fact all but office properties were reported to be in a growth stage. Apartments have moved to predominantly being judged in the mature stage.



INVESTMENT CRITERIA

Office Market				
CATEGORY	2014 Range	2014 Average	2015 Range	2015 Average
Holding Period (Years)	5.0-10.0	7.3	5.0 - 10.0	7.3
Income (Growth Rate)	2.0% - 3.0%	2.3%	2% - 3.0%	2.7%
Operating Expenses (Growth Rate)	1.0% - 3.0%	2.1%	2.0% - 2.5%	2.2%
Vacancy Loss	5.0% - 10.0%	8.3%	5.0% - 10.0%	8.2%
Going-In Capitalization Rate	8.0% - 10.0%	8.7%	7.5% - 9.0%	8.3%
Terminal Capitalization Rate	8.5% - 11.0%	9.5%	8.0% - 10.0%	8.7%
Discount Rates (Unleveraged IRR)	8.5% - 12.0%	10.0%	9.0% - 12.0%	9.9%
Equity Yield (Leveraged IRR)	10.0% - 18.0%	12.7%	12.0% - 14.0%	13.0%
Tenant Retention Rates:				
Class A	60% - 75%	68%	60% - 89%	71%
Class B	60% - 65%	63%	60% - 75%	68%
Months vacant between tenants:				
Class A	3.0 - 12.0	8.2	3.0 - 12.0	6.8
Class B	4.0 - 18.0	11.5	6.0 - 18.0	11.8

2015 REAL ESTATE MARKET SURVEY

Retail Market				
CATEGORY	2014 Range	2014 Average	2015 Range	2015 Average
Holding Period (Years)	5.0 – 10.0	8.3	7.0 – 10.0	8.0
Income (Growth Rate)	1.5% - 3.0%	2.3%	2.5% - 3.0%	2.8%
Operating Expenses (Growth Rate)	1.0% - 2.0%	2.0%	2.0% - 2.5%	2.2%
Vacancy Loss	8.0% - 10.0%	9.0%	7.0% - 10.0%	8.2%
Going-In Capitalization Rate	7.5% - 10.0%	8.6%	6.8% - 9%	7.9%
Terminal Capitalization Rate	8.0% - 11.0%	9.2%	7.3% - 8.5%	8.3%
Discount Rates (Unleveraged IRR)	9.5% - 12.0%	10.3%	9.0% - 12.0%	9.8%
Equity Yield (Leveraged IRR)	11.0% - 18.0%	13.2%	12.0% - 17.5%	14.8%
Tenant Retention Rates:				
Neighborhood	65% - 80%	72%	70% - 95%	81%
Community	70% - 75%	73%	65% - 90%	79%
Months vacant between tenants:				
Neighborhood	3.0 – 18.0	10.4	6.0 – 13.0	8.3
Community	6.0 – 12.0	10.0	3.0 – 7.0	5.6

Apartment Market				
CATEGORY	2014 Range	2014 Average	2015 Range	2015 Average
Holding Period (Years)	5.0 – 10.0	7.5	2.0 – 10.0	6.0
Income (Growth Rate)	1.5% - 3.5%	2.5%	2.0% - 3.0%	2.8%
Operating Expenses (Growth Rate)	1.0% - 3.0%	2.0%	2.0% - 3.0%	2.5%
Vacancy Loss	4.0% - 8.0%	6.0%	4.0% - 7.0%	5.3%
Going-In Capitalization Rate	6.0% - 7.5%	6.6%	6.0% - 8.0%	6.5%
Terminal Capitalization Rate	6.8% - 9.0%	7.4%	7.0% - 8.0%	7.3%
Discount Rates (Unleveraged IRR)	8.0% - 9.5%	8.7%	8.0% - 9.0%	8.3%
Equity Yield (Leveraged IRR)	10.0% - 15.0%	11.6%	12.0% - 17.5%	14.1%

Industrial Market				
CATEGORY	2014 Range	2014 Average	2015 Range	2015 Average
Holding Period (Years)	7.0 -10.0	8.5	7.0 - 10.0	9.1
Income (Growth Rate)	1% - 3.0%	2.4%	1.0% - 3.0%	2.3%
Operating Expenses (Growth Rate)	1.0% - 3.0%	2.3%	2.0% - 3.0%	2.3%
Vacancy Loss	5.0% - 8.0%	9.0%	3.0% - 10.0%	6.6%
Going-In Capitalization Rate	8.0% - 11.0%	9.1%	7.0% - 10.0%	8.2%
Terminal Capitalization Rate	8.5% - 11.0%	9.6%	7.5% - 12.0%	9.1%
Discount Rates (Unleveraged IRR)	8.5% - 12.0%	10.4%	9.0% - 10.5%	10.1%
Equity Yield (Leveraged IRR)	11.0% - 18.0%	13.3%	12.0% - 20.0%	14.5%
Tenant Retention Rates:				
Office/Whse.	65% - 80%	70.0%	65% - 90%	74%
Distribution	60% - 80%	71.2%	65% - 91%	75%
Months vacant between tenants:				
Office/Whse.	3.0 – 12.0	8.2	4.0 – 25.0	10.4
Distribution	4.0 – 33.0	12.2	5.0 – 24.0	10.4

LAND LEASE RATES

	Range	Average	Change From 2014
Cap Rate (with flat rent)	5.00% - 10.00%	6.93%	-24 basis points
Cap Rate (average 2% ann. escalation)	5.00% - 10.00%	6.19%	-36 basis points

RESERVES, LEASING COSTS, AND TI'S

Include in Cap Rate Analysis	Yes	No
Reserves for Replacement	80%	20%
Leasing Commissions	73%	27%
Tenant Improvement Costs	60%	40%

COST OF SALE

Price Range	Low	High	Average
<\$500K	3%	10%	6.25%
\$500K to \$1M	3%	8%	5.38%
\$1M to \$3M	3%	6%	4.53%
\$3M to \$5M	2%	6%	3.93%
>\$5M	1%	5%	3.07%

ENTREPRENEURIAL INCENTIVE

Basis	Year	Low	High	Median
Improvements Only	2015	8%	20%	14%
	2014	10%	20%	15%
	2013	10%	20%	15%
	2012	10%	18%	14%
	2011	10%	15%	11%
	2010	10%	20%	15%
	2009	10%	25%	15%
	2008	8%	20%	12%
	2007	10%	18%	15%
Land and Improvements	2015	8%	30%	12%
	2014	8%	18%	12%
	2013	8%	20%	10%
	2012	5%	15%	10%
	2011	10%	25%	15%
	2010	10%	30%	15%
	2009	10%	20%	14%
	2008	10%	15%	10%
	2007	9%	25%	16%
Gross Lot or Unit Sales	2015	25%	33%	25%
	2014	25%	50%	30%

LOT PRICE RATIOS

Improved Property Price Range	Lot Value Ratio Range as % of Total Price					Median				
	2011	2012	2013	2014	2015	2011	2012	2013	2014	2015
Starter Housing \$200-\$300K	20-25%	20-25%	18-30%	15-30%	20-25%	24%	25%	22%	28%	25%
Move Up Housing \$300-\$400K	20-25%	20-27%	15-25%	17-30%	23-26%	25%	24%	20%	23%	26%
Luxury Housing \$400-600K	20-30%	20-30%	14-25%	18-25%	20-30%	25%	25%	20%	25%	28%
High End Luxury Housing Over \$600K	20-25%	20-30%	18-25%	20-28%	15-29%	25%	27%	20%	20%	27%
Townhouse	25-33%	25-30%	20-30%	15-32%	23-25%	28%	25%	20%	30%	25%

AVAILABILITY OF MORTGAGE FINANCING

Property Type	Past 12 months	Next 12 months
Apartments	2.9	2.8
Hotels	2.2	2.4
Industrial	2.4	2.5
Office	2.1	2.3
Retail	2.8	2.6
Residential (A & D)	1.8	2.2
Rating Scale:	1 = Inadequate	2 = Adequate
		3 = Abundant

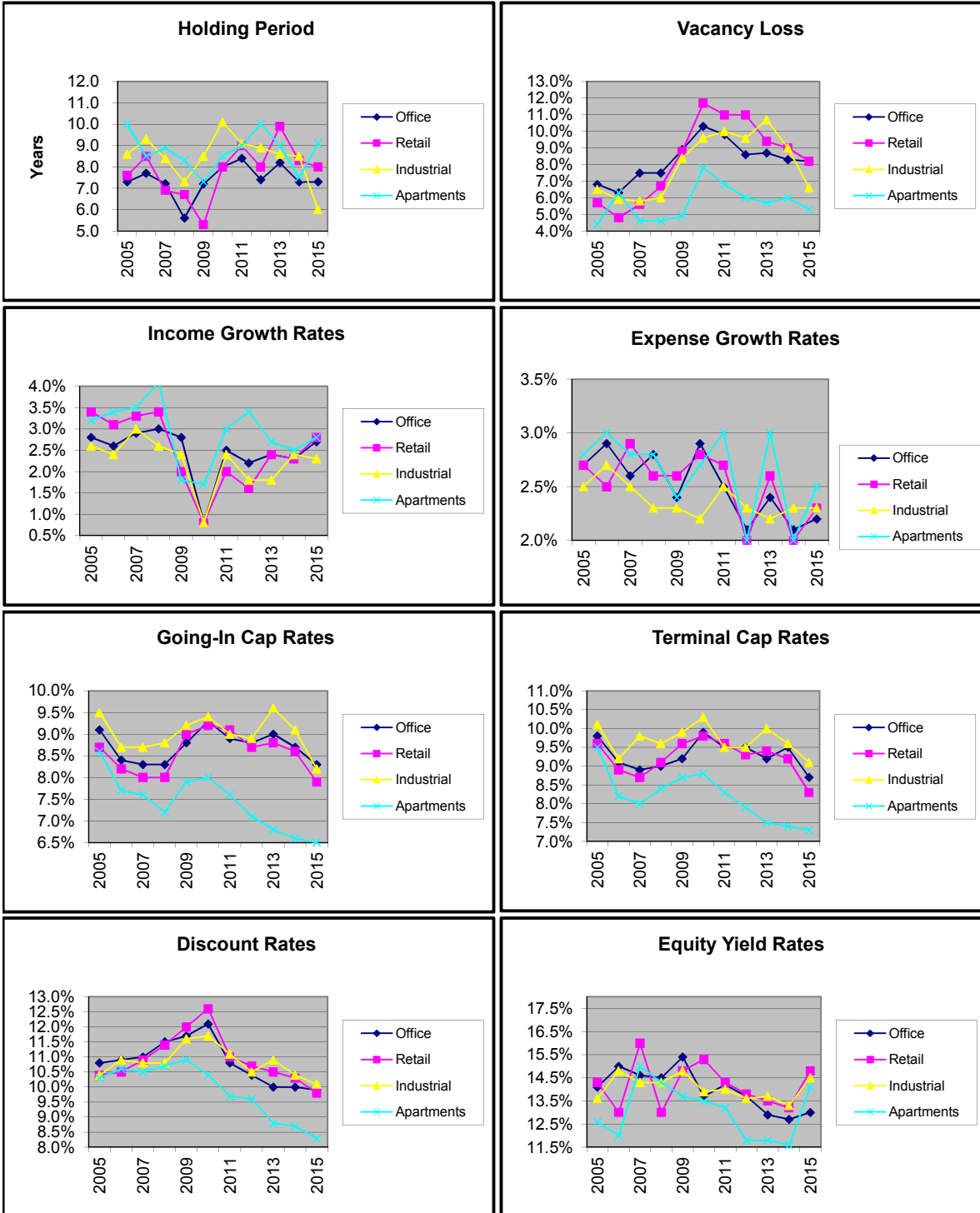
REAL ESTATE LIQUIDITY – MARKETING PERIOD

Property Type	% of Responses		
	< 6 Months	6-12 Months	> 12 Months
Retail			
Free-standing single user retail	71.4%	28.6%	00.0%
Small unanchored retail center	28.6%	57.1%	14.3%
Neighborhood retail center	57.1%	42.9%	00.0%
Community retail center	42.9%	42.9%	14.3%
Regional retail center	40.0%	40.0%	20.0%
Multi-family			
Apartment (> 120 units)	71.4%	28.6%	00.0%
Apartment (< 120 units)	85.7%	14.3%	00.0%
Office			
Large - well leased	66.7%	33.3%	00.0%
Large – poorly leased	16.7%	33.3%	50.0%
Small – well leased < 20,000 sf	50.0%	33.3%	16.7%
Small – poorly leased < 20,000 sf	16.7%	33.3%	50.0%
Industrial			
Small single user	44.4%	44.4%	11.1%
Multi-tenant flex/bulk distribution	50.0%	50.0%	00.0%
Manufacturing buildings	30.0%	20.0%	50.0%
Special use properties			
Banks, historic, churches, etc.	20.0%	40.0%	40.0%
Land			
Single family development	14.3%	57.1%	28.6%
Multi-family development	42.9%	42.9%	14.3%
Retail	16.7%	33.3%	50.0%
Office	16.7%	16.7%	66.7%
Industrial	0.0%	50.0%	50.0%

In general 73% of the respondents felt that there would be no change, 9% felt there would be an increase and 18% projected a decrease in marketing time. Reasons stated for a decrease include “Vacancy is shrinking quickly and there is no development on the horizon” and “lack of new construction”. A reason for no change was “if properties are reasonably priced, they will sell; time doesn’t help”.

This Real Estate Market Survey is an annual publication of Knight, Dorin & Rountrey. *This is our 23rd 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.

**CENTRAL VIRGINIA
MARKET SURVEY HISTORICAL SUMMARY 2015**
(Response Averages)



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
- Fredericksburg Area
- Williamsburg Area

OWNER

Edward G. Knight, MAI, SRA

PROFESSIONAL STAFF

J. Parks Rountrey, MAI, SRA
William A. Hopkins, Jr., MAI, SRA
Michael A. Knight
James A. Wood, Jr.
Nicholas W. Stafford
W. Wickham Smith, III

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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