INVESTMENT

HAMPTON ROADS
MARKET SURVEY
2007

Acknowledgements

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General Overview

This report analyzes commercial real estate investments, during the year 2006, within the Virginia Beach-Norfolk-Newport News, VA-NC Metropolitan Statistical Area (the "MSA") that is also known as Hampton Roads, Virginia. This report provides both summary and specific data on investment sales of commercial properties located throughout the MSA. Where available the report includes properties in the cities of Chesapeake, Hampton, Newport News, Norfolk, Poquoson, Portsmouth, Suffolk, Virginia Beach and Williamsburg, as well as the counties of Gloucester, James City and York.

METHODOLOGY

The purpose of this Commercial Investment Review is to collect commercial real estate investment sales data and report on current national and local trends; and as future data is collected, establish longer-term trends within the Hampton Roads commercial real estate investment market.

This 2007 survey is the third in the series. Data has been collected for the period January 1, 2006 through December 31, 2006. As this report was required for publication at the end of December 2006, it may not include some transactions that took place at the very end of the year. This data should be used for trend analysis only, as the data collected is from multiple sources and the author was not always able to verify the specifics of all individual transactions.

The focus of this survey is on the four primary types of commercial investment real estate: apartments, office, retail and industrial. The objective of this report is to include as many building sales as possible. An effort has been made to limit the survey to buildings that are owned as investments. Single tenant buildings are included if the primary function of the ownership is as an investment. Owner occupied buildings are included if a significant part of the property is leased to third party tenants. Land is excluded from this report.

National and regional data, as well as analysis, have been provided by Real Capital Analytics and REIS, through Sperry Van Ness International. Local data has been gathered through Sperry Van Ness Commercial Real Estate Advisors in Virginia Beach with assistance from area brokers and real estate appraisers.

NATIONAL OVERVIEW

Although the national commercial property investment market managed to maintain the record levels set over the last few years, some dramatic changes in the landscape occurred during 2006. Changes included the impact of foreign capital, the condo conversion market, fluctuations in interest rates, mobility of capital, privatizations and mega deals. Foreign investors, REITs and syndicators all slowed their investments in 2006, while at the same time acquisitions by condo converters came to a screeching halt. Even with all these changes the total volume of sales in the commercial property investment market grew by over 10% during the year.

In 2005, foreign investors accounted for over $21 billion in acquisitions in U.S. commercial properties; in 2006 that number dropped by over 20% to below $16 billion. Across the U.S., foreign investors represented only 2% of the acquisitions of apartments, 4% of the acquisitions of industrial, 8% of the acquisitions of retail and 11% of the acquisitions of office properties. Across all four property types foreign investors showed a drop in the volume of acquisitions that they made in U.S. properties. The good news is that private investors, and for some part institutions, picked up the slack and then some.

The most dramatic shift in the market was the condo converters who went from spending over $30 billion in 2005 to well under $10 billion in 2006. Developers buying commercial properties for conversion to condominiums were the largest single group of buyers during 2005 and in the process took approximately 175,000 apartment units out of the apartment rental market. They also took over 12 million square feet of office and industrial space to be converted into residential condominiums and over 6 million square feet to be converted to commercial condominiums. At the beginning of the year we were skeptical on how this market would fare with the slow down in the residential markets. During the year, some of the conversion projects were never converted and managed to be resold as apartments, even at a profit. The condo market cooled during the year. Many conversion lenders tightened their criteria and we don't expect to see a return to that kind of acquisition activity in the near future.

Interest rates took an upward bump in the middle of the year but still remained at historically low levels. The mid-year bump in the interest rate did push capitalization rates up accordingly, but the second half of the year showed a corresponding drop in both rates. The availability of inexpensive capital kept investors looking for acquisitions while still willing to pay aggressive prices for these deals. As a result, capitalization rates crept down again at the end of the year and prices for the most part continued at their high levels. Nationally, average capitalization rates for institutional quality properties are still strong, ranging from 5.6% for apartments to 7.1% for industrial.

The mobility of capital has continued to explode nationally as local investors expanded their acquisitions well beyond their local markets. In search of competitive deals, West Coast buyers are moving east, and East Coast buyers are moving to the mid-west. Major market buyers are flocking to secondary markets; all are looking for means to increase their yields. Secondary and tertiary markets became popular as prized properties in these markets were picked up. Midwestern and southeastern sellers have been the beneficiaries of this capital flow and the trend should continue. Larger national investors, in addition to scouring smaller markets, have also started to look overseas for opportunities. The flow of capital for real estate has truly gone global and will remain that way for the foreseeable future.

Privatization and mega deals have been a driving force for the investment market throughout 2006. REIT mergers and acquisitions by equity funds doubled in 2006 to approximately $100 billion. Approximately half of this activity was privatization backed by equity funds. Blackstone's pending $36 billion purchase of EOP will be the largest real estate deal in history and is the precursor to mega deals to come. During 2006, transactions for 31 portfolios or properties valued over $1 billion each were announced. The largest REIT IPO in history was concluded during the third quarter of the year and the record for largest sale for an individual property was broken multiple times. These mega deals will continue to influence the national commercial property landscape during the coming year.

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As we concluded at the end of last year, it appears the economic recovery has started to show signs as most markets across the country posted positive absorption and many posted modest rent growth as well. The strengthening of the base fundamentals in many markets allowed the continued justification of higher values and lower capitalization rates for most deals. The economy continues to push along and it appears most investors are very optimistic about the coming years. The year ahead will hold very much the same as interest rates should remain relatively low, the economy should continue along on a positive pace and investors will continue to prefer hard assets.

HAMPTON ROADS OVERVIEW

The Hampton Roads commercial property investment market maintained a steady pace throughout 2006 as it benefited from the mobility of capital and a stable economic base. In spite of the scheduled closing of the Ford truck manufacturing plant in Norfolk and lingering concerns surrounding the Base Realignment and Closure Commission (BRAC) recommendations, the Hampton Roads MSA economy, according to the U.S. Department of Labor, was one of a limited number of MSAs nationwide to show a continued increase in average nonagricultural employment. The gains are not large, but they are positive, reinforcing the stability of the market. The strong presence of the wide variety of U.S. military branches and military support operations, along with the continued growth of the Ports of Hampton Roads, sustain the local economy.

One of the largest factors influencing the local commercial property investment market for 2005 were portfolio sales, which with a few exceptions all but disappeared during 2006. While several portfolio sales did take place in the office and apartment sectors, they paled in comparison to the $100 million invested by First Potomac Realty Trust in 2005. The largest transactions in Hampton Roads during 2006 included the Alta Cove apartments valued at $63 million, and the West Park Warehouses and the Dove Landing Apartment portfolio, both valued just over $32 million each. Most of the investment sales that took place in 2006 were smaller properties and the total volume of investment sales dropped by almost 30%. The total volume of commercial investment sales dropped from an adjusted $804 million in 2005 to $570 million for 2006.

APARTMENTS

The national apartment market is continuing to show robust activity highlighted by a record number of mega deals. Positive rent growth for apartments keeps a steady flow of capital pushing into this market segment and market dynamics has kept the national vacancy factor at a healthy low of 5.4%. In 2005, condo converters drove the apartment sales market pushing sales prices up and cap rates down. Although condo converters, who represented approximately 35% of the buyers in 2005, came to a screeching halt during 2006, institutions and REITs picked up the slack and then some. Mega deals drove the 2006 market with multiple portfolios valued over $1 billion each trading hands. The largest of the apartment mega deals was the Peter Cooper Village / Stuyvesant Town transaction in Manhattan valued over $5.4 billion. With condo converters basically out of the market and no longer driving up prices, the national average price per unit has come down slightly from last year to $94,500 per unit for 2006. Capitalization rates continue to be very aggressive with the national average continuing the downward trend to 5.28%.

The Hampton Roads apartment market continues to show robust activity. Vacancy rates that remain among the nations lowest, continued positive employment numbers and the slip in the housing market has Hampton Roads continuing to attract a lot of attention from both buyers and builders.. Builders were very aggressive in 2005 delivering a record 1,770 units and even more aggressive in 2006 with 2,319 units scheduled for delivery. This represents over a 30% increase in the

number of new units scheduled for delivery in 2006, now the strongest year since 1988. Another 1,700 units are under construction for 2007 and the impact of all these new units on rental rates will be seen in 2007 and 2008 as these and additional units are absorbed. Vacancy rates for 2006 were up to 4.4%, up 30% from 2005.

The number of properties acquired during the year was fewer than last year, but the number of actual units sold was almost identical. We recorded 2,837 units sold during 2006. The biggest change factor for the year was the average price per unit which jumped over 20% from $66,500 per unit in 2005 to $80,307 per unit in 2006. The range of per unit values remained fairly disperse with a low for this year of $28,814 and a high of $168,449 per unit. Estimated capitalization rates were up slightly and ranged from 5.9% up to 10.5% with the majority in the mid 7% to mid 8% range. Sixty percent of the units sold were to three buyers from outside the market.

Major transactions for the year included Alta Cove in Chesapeake that sold for $63 million and the Dove Landing portfolio of apartments in Virginia Beach and Norfolk that sold for $32,636,000. This portfolio included eight properties with a total of 438 units that sold for $74,512.00 per unit.

Significant transactions for 2006 included:

Development	City	Units	Price	Price/Unit
Alta Cove	Chesapeake	374 units	$63,000,000	$168,449
Riverdale	Hampton	580 units	$30,150,000	$ 51,982
Brookfield	Va. Beach	352 units	$24,000,000	$ 68,181
Talbot Park	Norfolk	114 units	$17,200,000	$150,877
Gates of West Bay	Norfolk	202 units	$15,500,000	$ 76,732
Arbor Trace	Va. Beach	148 units	$14,750,000	$ 99,662
Dove Landing N	Va. Beach	150 units	$11,176,842	$ 74,512 *

**Price Allocated*

OFFICE

Nationally, office properties remained a prime target for buyers with a reported total acquisition volume estimated at over $120 billion. This represents a significant increase in sales volume over the prior year of almost 15%, after removing REIT privatizations. Declining vacancy rates, increasing rental rates and softening of concessions have all contributed to the strong investment activity in the office market. With capitalization rates remaining low and construction costs still rising, there is continued pressure on prices. Since sales prices remain high in primary markets there has been a strong shift from buyers to secondary and tertiary markets where capitalization rates do not have the same pressures. Nationally, average prices for office buildings rose to $220 per square foot, reflecting a gain of over 20% during the year. Capitalization rates continued their downward trend, closing the year at approximately 6.2%.

Office investment sales volume in Hampton Roads was off significantly from the prior year showing a decline in the number of building sales of almost half. Although the number of sales was off, the average price per square foot continued its

upward trend from $127 per square foot in 2005 to $135 per square foot in 2006. This increase is due in large part to the sale of several medical office buildings which have a higher cost to construct. The availability of office buildings for sale remains scarce as it appears a significant number of buildings were refinanced and repositioned over the last few years.

Major transactions for the year included the sale of the Patrick Henry Corporate Center in Newport News for $14,500,000 and the portfolio sale by Liberty Property Trust of their Rock Landing buildings in Newport News.

Significant transactions for 2006 included:

Development	City	Units	Price	Per SF
Jefferson Ave.	Newport News	100,000 SF	$14,500,000	$145
Rock Landing Dr.	Newport News	62,971 SF	$7,203,070	$114*
Kingsley La	Norfolk	31,856 SF	$4,330,000	$136
Center Point Dr.	Va. Beach	28,250 SF	$4,200,000	$149
Laskin Rd	Va. Beach	9,500 SF	$3,950,000	$416
Rock Landing	Newport News	33,224 SF	$3,800,397	$114*

**allocated – indicates the property was part of a multi-building portfolio transaction*

RETAIL

Retail, the investment poster child for 2005, lost a lot of its luster in 2006. The volume of retail investment sales dropped over 15% for the year. Although 2005 was a blistering year for all types of retail properties, 2006 showed dramatic declines in sales volumes for regional malls and portfolio sales of strip centers, the high dollar transactions. With the continued retail sales growth of big box users such as Target and Costco, power centers are still in the sights for investment buyers. Individual retail assets such as unanchored centers and free standing stores have been the only real bright spot with sales volume increases approaching 50% over 2005. The largest contributor to the slow down in overall sales volume has been continued aggressive pricing combined with the lack of quality of the properties for sale. The end of 2005 showed the beginning of a drop in the price per square foot that continued through 2006 at a slightly slower pace. By the end of the year the national average price per square foot had dropped to $157, from a high of $180 in mid 2005. The national average for capitalization rates did end the year lower, at 6.76%, after starting level and actually rising a bit mid year.

In spite of the slip in interest nationally, the Hampton Roads retail market maintained a brisk pace for 2006. Sales volume for retail properties almost matched 2005 both in square footage and dollar volume. In 2005, there were a significant number of transactions that were portfolio related, whereas in 2006 almost all the transactions were individual property sales. The average price per square foot slipped slightly from $104 in 2005 to an average of $97 per square foot in 2006. These smaller unanchored centers have lower quality credit ratings and thereby demand higher capitalization rates and lower per square foot prices. Quoted capitalization rates for the stronger properties ranged from 6.7% to 9%, while many smaller

centers, though only estimated, sold for capitalization rates ranging from 9% and up. Local free standing triple net drug store properties sold for $400 per square foot on capitalization rates of 7%.

Major retail transactions for the year included Chesapeake Crossing Shopping Center, Lynnhaven East and North and Patriot Plaza. Significant transactions for 2006 included:

Development	City	Units	Price	Per SF
Richmond Rd. Food Lion	Williamsburg	68,060 SF	$14,500,000	$213
Chesapeake Crossing	Chesapeake	287,679 SF	$12,010,000	$42
Lynnhaven East & North	Va. Beach	106,657 SF	$11,800,000	$111
Victory Blvd. AJ Wright	Portsmouth	72,800 SF	$10,650,000	$146
Holland Rd - Kmart	Va. Beach	190,547 SF	$10,000,000	$52
Linens & Things Center	Newport News	34,103 SF	$6,300,000	$185
Patriot Plaza	Williamsburg	76,520 SF	$6,200,000	$81

INDUSTRIAL

The national industrial property investment market is separated into two distinct property types that include warehouses and flex buildings. Warehouses are typically 300,000 square feet and larger distribution buildings while the flex properties are smaller in size and have a greater percentage of office space. Flex properties are typically designed for high tech, research and back office operations. Increases in wholesale trade and logistics operations have bolstered the national warehouse market, while the flex market, though continuing to struggle with high vacancies, showed signs of renewed investor interest in 2006. Nationally, flex properties ended the year at an average price per square foot of $96, down slightly from the $99 per square foot posted at the end of 2005. Warehouses ended the year with an average price per square foot of $57, up slightly from the end of year 2005 figure of $55 per square foot. Capitalization rates for warehouse properties fluctuated slightly during the year, but ended the year down at just over 7%. Capitalization rates for flex properties fluctuated during the year but also ended the year down closer to 7.3%.

The Hampton Roads industrial investment market was off substantially from the blistering pace set during 2005. In 2005, the volume of industrial investment property sales more than tripled over the prior year and portfolio sellers and buyers targeting Hampton Roads set the pace, accounting for 80% of the investment transactions during that year. In 2006, the volume of industrial sales based on square footage dropped over 40%, down to just over 2 million square feet from an adjusted 3.5 million in 2005. The dollar volume of investment sales was almost identical to 2005, but the number of buildings sold more than doubled. This indicates that a wider variety of investment buyers were purchasing much smaller assets. The average price per square foot increased dramatically based on the smaller asset size, from $37 per square foot in 2005 up to $64 per square foot for 2006. Significant increases in construction costs also helped drive these values up. Flex properties lead the values, pushing $70 to $90 per square foot, while warehouse values remained in the $40 to $55 per square foot range.

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Major industrial investment transactions included the purchase of the West Park warehouses in Hampton, Crossways I in Chesapeake and the mixed use property that was formerly the Williamsburg Candle Factory. Although the Williamsburg Candle Factory included retail and office property the majority of the square footage was manufacturing and warehouse.

Significant transactions for 2006 included:

Development	City	Units	Price	Per SF
West Park warehouses	Hampton	515,486 SF	$32,219,450	$ 63
Crossways I	Chesapeake	143,122 SF	$15,700,000	$109
Williamsburg Candle	Williamsburg	261,000 SF	$10,916,500	$ 42
Middleground Blvd	Newport News	77,125 SF	$5,950,000	$ 77
Stephanie Way	Chesapeake	51,209 SF	$5,100,000	$100
Central Drive	Va. Beach	56,444 SF	$4,850,000	$ 86
Gateway II	Norfolk	42,429 SF	$3,600,000	$ 85
Steel Street	Chesapeake	143,000 SF	$3,600,000	$ 25
Miller Store Rd	Va. Beach	41,673 SF	$2,700,000	$ 65