INDUSTRIAL

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OLD DOMINION UNIVERSITY

HAMPTON ROADS REAL ESTATE MARKET REVIEW

2010

GENERAL Overview

This report analyzes the 2009 industrial real estate conditions within the Virginia Beach-Norfolk-Newport News, VA-NC Metropolitan Statistical Area (the MSA), also known as Hampton Roads. It provides inventory, vacancy, rent, sale and other data for the MSA. The survey includes properties in the cities of Chesapeake, Hampton, Newport News, Norfolk, Poquoson, Portsmouth, Suffolk, Virginia Beach and Williamsburg, plus the counties of Gloucester, James City, York and Isle of Wight.

Methodology

This survey includes the following types of properties:

- Office-warehouse, industrial and shop facilities of 5,000 square feet or greater, although some facilities of less than 5,000 may be included.
- Properties having less than 80% office space.
- Both owner-occupied and leased properties; owner-occupied is defined as property that is 100% occupied by a business that is the same as or is related to the owner of the building.
- All properties that are available and are listed for sale or lease, regardless of whether they are occupied, unless they are strictly available for sale as an investment property are included. For example, a property that is available for sale and is currently occupied on a short term lease is included.
- All properties that have commenced construction (foundations installed as a minimum) are included.

The survey excludes the following types of properties:

- Land.
- Warehouse or shop facilities on shipyard properties.
- Warehouse or industrial facilities on federal government property (e.g. military installations).
- Industrial facilities on government property (e.g. Norfolk International Terminal or Newport News Marine Terminal).

Functional submarket delineations are determined with some regard to city boundaries, but boundaries are not determinative. The entire market is divided into 16 submarkets defined by industrial building concentrations, the transportation network, and pertinent physical features. The area map included in this report provides a location for key reference.

The E.V. Williams Center for Real Estate and Economic Development (CREED) at Old Dominion University has been tracking the inventory of the Hampton Roads industrial market since 1995. The results of this year's survey (collected during the 4th quarter of 2009) indicate that the Hampton Roads industrial market currently encompasses 108,722,115 square feet or space located in 2,876 buildings throughout the region. This is an increase of 4,304,462 square feet, or 4.1% from last year's survey. The increase is primarily due to delivery of new construction in 2009 begun in 2007/2008 and increased accuracy of surveyors over previous years. Totals may differ from other market surveys due to the self-imposed limitations established by the ODU CREED methodology described above.

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Dissecting The Market

The Hampton Roads industrial market is driven by three major forces: the government, the port, and the local economy. Building size, configuration and overall composition is shaped by these three forces. Four different product types emerge to serve the region:

a. **Distribution:** Services the port and the military. Offers dock level loading and clear heights in excess of 22 feet.

b. **Flex, sales and service:** Offering a higher percentage of office area to warehouse, with lower ceiling heights in the production and warehouse area. Can require supporting yard area.

c. **General Industrial:** Typically multi-tenant and smaller space designed for a broad range of industry types providing moderate clear height, grade and dock level loading and a 10-20% office build-out.

d. **Manufacturing:** Traditional blend of office, manufacturing, shipping and receiving, with facilities specifically designed for each specific use. Usually owner-occupied.

Hampton Roads has been buffeted by the global economy specific to distribution space. The area continues to suffer from the glut of existing and new product. With TEU volume down 17.4% through November 2009 in comparison to 2008, much of the space is expected to continue to sit idle. Asking lease rates for new construction distribution space exceeded $5.00 NNN per square foot per year in 2008. The current 'market' for Class A space is hovering at $4.00 NNN per square foot. Sublease space has leased for as low as $1.00 NNN per square foot.

This downward trend in rates is expected to hit bottom in 2010 for new, highly functional space. Modest absorption is expected. Second generation warehouse with limited loading and/or reduced clear heights will continue to languish as rental rates for Class A space hits a practical bottom, with no reduction left for lesser quality product.

Flex and general industrial space has also suffered in the current recession. Specifically, the building and service support industries have pulled back, but not abandoned the Hampton Roads market. The demographic strength of the region coupled with anticipated migration trends from rust belt states continues to make the area an attractive market. Most companies that operate here plan to continue, perhaps with some reduction in size. Other national and regional

companies have been active in establishing a presence.

Market uncertainty has forced most landlords to reduce rents in exchange for continued tenancy. Companies with leases rolling over in 2009 chose either to move to smaller facilities or negotiate reduced rental rates. While distribution space has seen lease rate reductions of 25% or more, flex and general industrial rents have suffered a more modest 10-15% decline over 2008.

Statistically, manufacturing facilities in large measure are owner occupied. Manufacturing properties that come to market are most often for sale and do not compete directly with the lease market. Unfortunately, manufacturing buildings such as the Ford plant in Norfolk dramatically contribute to overall vacancy. Due to their specialized nature, they are often on the market for extended periods. The recent closing of the International Paper plant in Franklin resulted in buildings placed on the market in the Cavalier submarket (Chesapeake: 127,600 square feet) and in the Oakland Upper Peninsula submarket (Newport News: 268,750 square feet). The effect these buildings had on vacancy was to add 2.1% to the Cavalier submarket and 5.52% to the Oakland Upper Peninsula submarket.

Fulton Bank is still lending locally to the industrial sector, as are other regional banks such as BB&T, Towne Bank, and Bank of Hampton Roads.

Vacancies in 2010 should stabilize due to a combination of no new construction and continued modest absorption. Manufacturing may suffer further in 2010 with plant closures if the U.S. economy does not rebound.

The Effect Of The General Economy On The Local Market

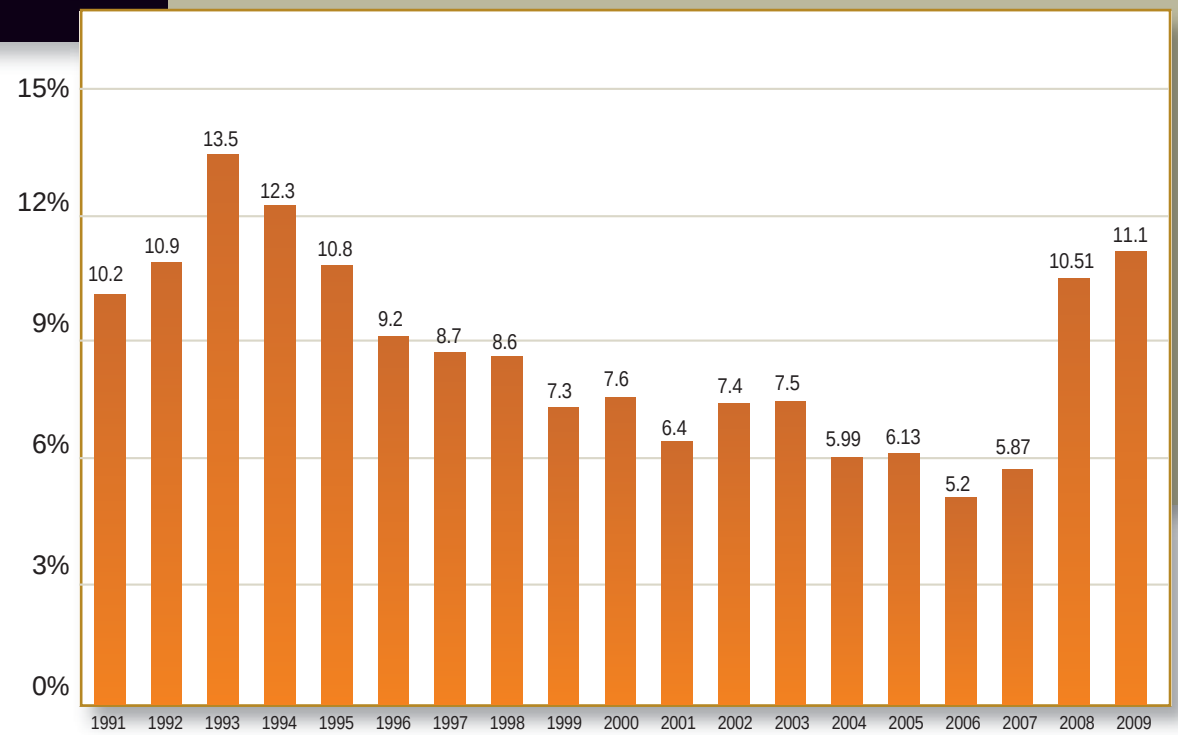
The global economy, U.S. public policy decisions, and private sector reaction has affected the real estate market in Hampton Roads, as it has in the broader national industrial market.

1. Lending has been significantly curtailed. New construction lending for speculative building is practically non-existent. Investment lending is coming under increased scrutiny in keeping with national trends. Debt coverage, appraised values, cash flow discounts for vacancy/credit loss/management are increasing, and loan to values are subsequently falling to 'conservative' lows.

   Tom Dillon, Senior Vice President with Fulton Bank, a strong regional bank, believes we are back to a more normal, healthy lending climate: less risk, with more measured and realistic underwriting criteria reminiscent of the banking environment prior to the recent market run-up. Fulton Bank is still lending locally to the industrial sector, as are other regional banks such as BB&T, Towne Bank, and Bank of Hampton Roads.

2. The global slowdown in import and export container traffic has had a significant effect on industrial space in the region. The current glut of distribution space is directly attributable to diminished port activity.

Hampton Roads Industrial Market Vacancy Rate



3. Business expansion and relocation plans for many corporations were put on hold for most of 2009. Business expenses associated with potential health care reform, proposed tax changes, and environmental legislation have created uncertainty in corporate planning. This has, in turn, tabled most facility decisions.

The net effect on the industrial market throughout 2009 has been a slowing in deal volume. National industrial leasing activity in 2009 fell to 230.8 million square feet according to Cushman and Wakefield's *4Q09 Marketbeat US Industrial Report.* This is significantly less than the ten year average of 293.5 million square feet. Construction in the fourth quarter of 2009 of 13.5 million square feet was one of the lowest totals ever recorded. Investor sales totaled only 60.5 million square feet, the lowest amount recorded since 1991.

REAL Capital Analytics recorded similar trends in their *Industrial Year in Review* published January 21, 2010. 2009 deal volume was off by 63%. Total number of industrial properties sold was down 58%.

For Hampton Roads, 20 buildings were sold in 2009 in comparison to 35 for 2008 for a 43% reduction. Lease volume shared a similar downward trend in 2009 in comparison to 2008, with 2.7 million square feet of leasing in 2009 compared to 3.1 million in 2008.

Market Overview

There are a number of bright spots in the Hampton Roads industrial market. The ODU CREED Market Report is defined by sixteen submarkets. Out of those sixteen submarkets:

a. Six submarkets (37.5%) have lowered vacancy rates since last years report.

b. Six submarkets (37.5%) have a vacancy rate less than 8%.

c. Four submarkets (25.0%) have a vacancy rate less than 6%.

d. Two submarkets (12.5%) have a vacancy rate less than 5%.

As a whole, the Peninsula fared well in 2009, primarily with the leasing of large blocks of sublease space. Vacancy in total for the Peninsula dropped from 10.08% to 9.49%, with all but the Oyster Point/Middle Peninsula submarkets registering drops in vacancy.

Overall, vacancy for 2009 in Hampton Roads increased moderately in comparison to 2008.

Sales

Representative Building Sales:

Location/Submarket	Date	Sq. Ft.	Price	$/SF
875 Middleground Boulevard, Oyster Point	January 2009	62,052	$5,161,370	$83.13
3749 Progress Road, Norfolk Industrial	May 2009	52,553	$3,200,000	$60.89
1425 Air Rail Road, Virginia Beach	September 2009	5,000	$421,500	$84.30
129 Pennsylvania, Virginia Beach	September 2009	8,550	$450,000	$52.63
3728 Profit Way, Chesapeake	September 2009	32,500	$2,240,000	$73.44
415 Rotary Street, Hampton	October 2009	12,000	$605,000	$50.42
11850 Canon Boulevard, Newport News	June 2009	20,292	$1,500,000	$73.92

Financing is the challenge for 2010. Owner-buyers will find regional banks receptive, while investors will have a difficult time meeting underwriting requirements. Banks are requiring higher loan-to-values and stronger cash flows to find favor with loan committees.

Leasing

Representative Lease Rates:

Location/Submarket	Sq. Ft.	$/SF Per Year	Term
200 West Park, Hampton	56,129	$4.75	5 year
500 Woodlake Circle, Greenbrier	11,000	$6.30	5 year
101 Lummis Road, Suffolk	35,000	$3.50	2 year
4500 Progress Road, Norfolk	44,000	$3.75	5 year
4021 Seaboard Court, Portsmouth	6,500	$9.23	2 year
680 Carolina Road, Suffolk	7,695	$4.05	3 year

Rents For Available Spaces By Size Range 2009

Begin Size (s.f.)	2001	2002	2003	2004	2005	2006	2007	2008	2009
< 5,000	$6.34	$7.16	$6.95	$7.30	$7.75	$7.85	$7.90	$7.95	$6.50-$7.00
5,000 - 20,000	$4.46	$5.80	$5.89	$6.20	$6.50	$6.75	$6.95	$6.95	$5.00-$6.00
20,000 - 40,000	$4.35	$4.99	$5.21	$5.45	$5.75	$5.85	$5.90	$5.75	$4.75-$5.50
40,000 - 60,000	$4.15	$4.13	$4.44	$4.75	$4.95	$5.00	$4.75	$4.50	$4.00-$5.00
> 60,000	$3.24	$3.43	$3.15	$4.00	$4.30	$4.35	$4.25	$4.00	$3.25-$4.25

Percentage Of Available Spaces By Size Range 2009

Begin Size (s.f.)	2001	2002	2003	2004	2005	2006	2007	2008	2009
< 5,000	30%	15%	32%	25%	30%	25%	20%	23%	18%
5,000 - 20,000	40%	52%	44%	40%	42%	30%	15%	13%	23%
20,000 - 40,000	15%	18%	12%	15%	13%	15%	20%	17%	17%
40,000 - 60,000	9%	8%	7%	8%	6%	10%	20%	20%	15%
> 60,000	6%	7%	5%	12%	9%	20%	25%	27%	27%

Submarket Totals

Submarket	City	Bldgs Surveyed	Total s.f.	Vacancy s.f.	Vacancy %
Greenbrier Area	Chesapeake	202	8,469,468	749,882	8.85%
Bainbridge/S. Elizabeth River Area	Chesapeake	142	5,877,538	489,508	8.33%
Cavalier Industrial Park Area	Chesapeake	188	6,045,061	555,686	9.19%
Norfolk Commerce Park/ Central Norfolk Area	Norfolk	144	7,080,388	2,719,450	38.41%
Norfolk Industrial Park Area	Norfolk	348	10,372,544	1,399,257	13.49%
West Side/Midtown Norfolk Area	Norfolk	271	6,463,281	443,771	6.87%
Lynnhaven Area	Virginia Beach	278	7,994,242	1,015,633	12.70%
Greenwich/Cleveland Streets Area	Virginia Beach	125	3,089,916	184,214	5.96%
Airport Industrial Park Area	Virginia Beach	71	3,611,776	349,086	9.67%
City of Portsmouth	Portsmouth	154	4,775,530	262,595	5.60%
City of Suffolk	Suffolk	123	11,762,676	2,249,644	19.13%
Isle of Wight	Isle of Wight	28	2,658,340	756,216	28.45%
Southside Totals		**2,074**	**78,200,760**	**11,179,842**	**14.29%**
Copeland/Lower Peninsula Area	Peninsula	400	12,213,348	2,041,608	16.72%
Oyster Point/Middle Peninsula Area	Peninsula	128	4,430,793	192,957	4.35%
Oakland/Upper Peninsula Area	Peninsula	133	4,872,279	303,221	6.22%
Williamsburg Extended Area	Peninsula	60	9,004,935	359,143	3.99%
Peninsula Totals		**721**	**30,521,355**	**2,896,929**	**9.49%**
Totals		**2,876**	**108,722,115**	**14,076,771**	**12.95%**

Land

Land sales were non-existent in 2009. Financing for speculative development was unavailable. Land owners were not in the mood to discount prices. That trend is not expected to change in 2010, with most industrial land owner's content to hold and wait out the current downturn in value.

Investment

There were few investment sales traded in 2009. Most out-of-town investors looked for 'vulture' buys, which to date have not materialized. Local cash buyers are content to wait to see if the market erodes further before spending their funds. 'Keep your powder dry' was a phrase most often heard in investment circles.

Hampton Roads Versus The World

"Hampton Roads was one of the first areas of the country outside the commodity-producing states of Texas and the upper Midwest to commence economic recovery. The Brookings Institute's MetroMonitor project reported a 1.4% increase in gross metropolitan product (GMP) over the third quarter, and GMP now exceeds the pre-recession peak set in the fourth quarter of 2008. November's not-seasonally-adjusted unemployment rate was 6.6 %, still above historical averages, but 2.8 percentage points below the comparable national rate, and the 0.4% decline in non-farm employment over 12 months remained below job loss rates of 2.0% statewide and 3.4% nationally." So says *Thalhimer's Marketbeat Hampton Roads Industrial Report for the Fourth Quarter of 2009*. The report also notes that Hampton Roads experienced a 3.6% year-over-year drop in local manufacturing compared to 10.7% reduction nationally and an 8.6% loss statewide. Good news is sometimes relative.

This year's Old Dominion report shows an industrial vacancy rate of 12.95%. While Hampton Roads appears to be weathering the economic storm fairly well in many categories, the following statistics from Cushman and Wakefield's *4Q09 Marketbeat US Industrial Report* show us in league with most other markets in terms of industrial vacancy.

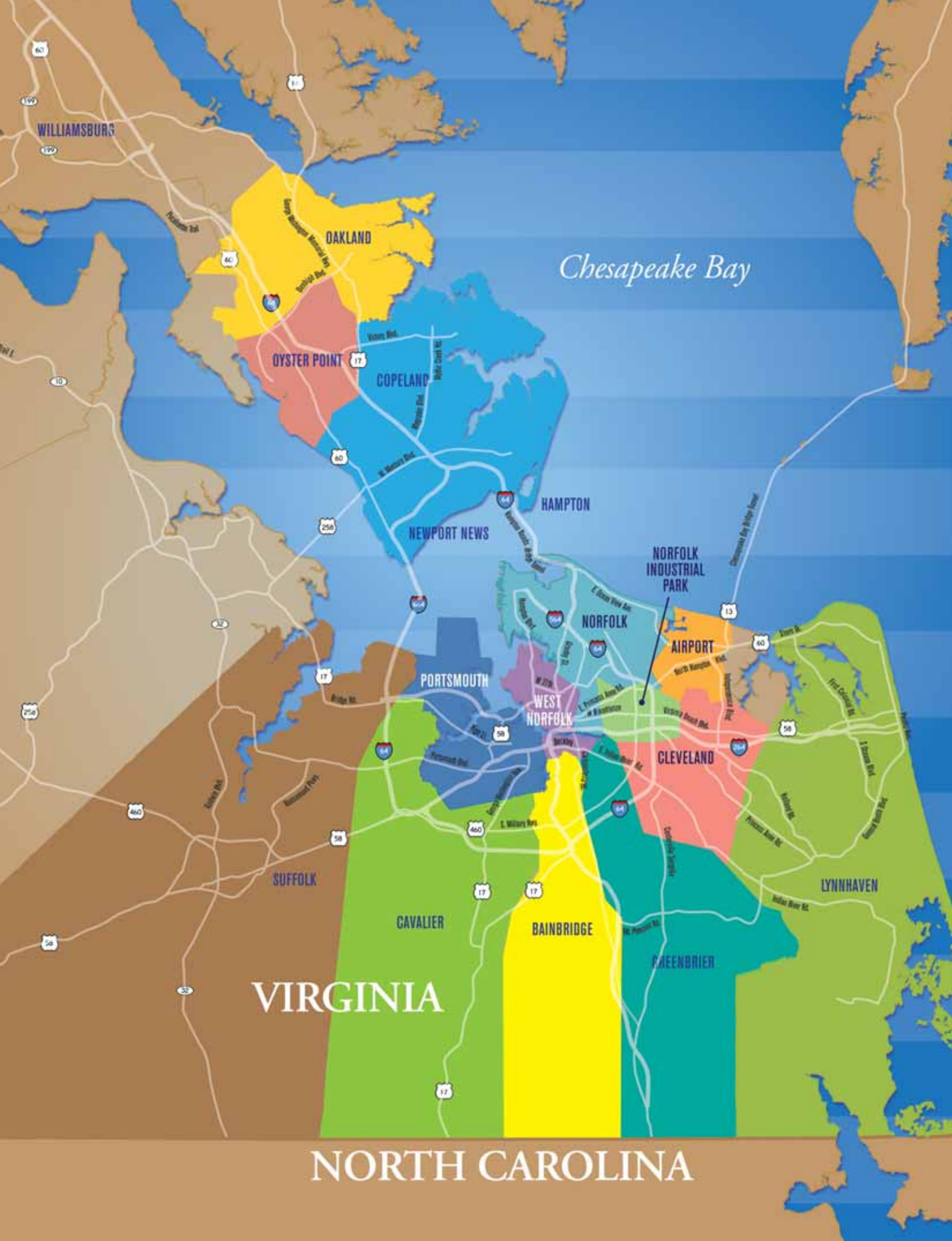
City	Vacancy Rate
Atlanta, Georgia	10.6%
Baltimore, Maryland	12.5%
Central New Jersey	9.5%
Chicago, Illinois	11.4%
Dallas/Ft. Worth, Texas	12.5%
Indianapolis, Indiana	10.6%
Inland Empire, California	13.4%
Los Angeles (South), California	5.7%
Oakland, California	9.2%
PA I-81/I-78 Distribution Corridor	14.6%
Richmond, Virginia	10.9%
Savannah, Georgia	19.9%
Seattle, Washington	9.3%
TOTAL-ALL MARKETS:	**10.8%**

Conclusions

Hampton Roads, the United States and the world are in unusual territory with events and circumstances not experienced in generations. How the future ultimately shapes the national and regional industrial market is hard to predict.

The Hampton Roads industrial market is expected to maintain the new 'status quo' in 2010: modest absorption, limited growth, and slightly reduced vacancy rates. Rents for distribution space will continue to soften in the coming year. General manufacturing building prices are expected to fall by 5-10%, particularly with more specialized properties. General industrial rents will stabilize, and vacancy should ease slightly by year end. Deal 'velocity' is not expected to increase in 2010. Subsequently, total transactions will most likely remain at levels established in 2009.

Beyond 2010, Hampton Roads should follow local historical trends with a modest recovery leading to a healthy, balanced industrial market. The Port of Virginia will renew its quest to become the dominant East Coast port of the 21st century. Government spending will continue to drive a large portion of industrial demand. Moderate population growth due to immigration from other regions of the country will require building space for general industrial uses. Words used in 2010 to describe the industrial market will most likely be 'patience', 'conservative', 'modest' and 'survived another year'.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Industrial Submarkets

Southside

Airport Industrial Park
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