2012 HAMPTON ROADS MARKET REVIEW

INDUSTRIAL

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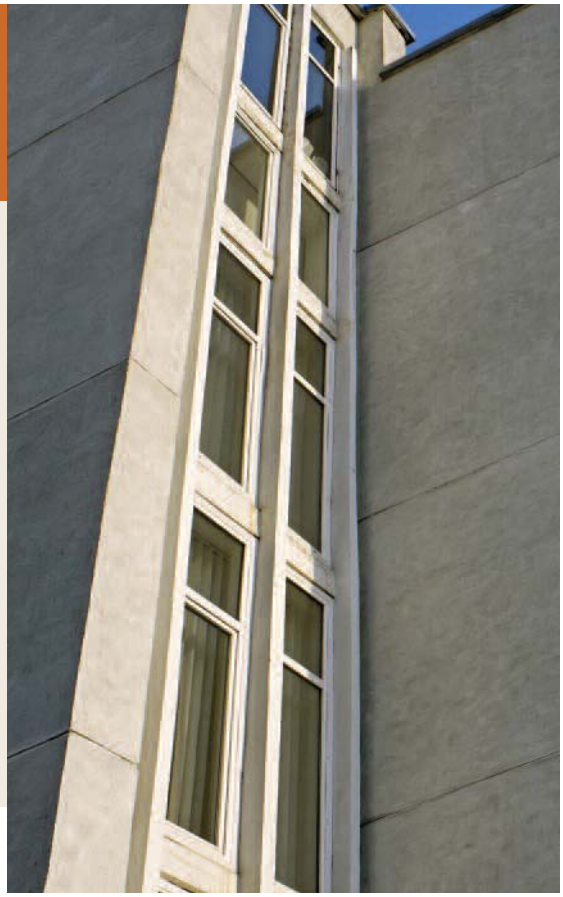

General Overview

This report analyzes the 2011 industrial real estate conditions within the Virginia Beach-Norfolk-Newport News, VA-NC Metropolitan Statistical Area (the MSA) that is 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 must have less than 80% office space to be included in the ODU survey.
- Both owner-occupied and leased properties are included. 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, 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).

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 2011) indicate that the Hampton Roads industrial market currently encompasses 106,691,857 square

feet or space located in 2,866 buildings throughout the region. This is a decrease of 2,030,258 square feet or 1.9% from last year's survey. The decrease is primarily due to the demolition of approximately 1 million square feet on the former Ford plant 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.

INTRODUCTION

The industrial market, while showing no improvement in the market below 50,000 square feet, fared better in 2011 than in 2010 for larger transactions. These major transactions obscured the overall weakness in the general industrial market.

Prior to the current recession, the Hampton Roads region began a significant transition toward servicing global markets through the Port of Virginia. Developers purchased land and began construction of new cross-dock and deconsolidation centers. By 2008, over 20 million square feet of industrial buildings were planned. Ultimately, less than half that total was built.

In 2011, the market saw absorption of much newly constructed Class A product. As a result, there is very little remaining high cube warehousing space. Over the past few years, building design has continued to evolve. Companies entering the market are demanding higher clear heights, larger truck courts, concrete construction, ESFR fire suppression and sustainable facilities. As a result, older generation distribution space will see greater vacancy and declining rental rates. Companies looking to relocate or expand in the market will have to look west for build-to-suit opportunities. Developers holding entitled properties, with site plan approvals and financing in place, should be in the best position to capture significant new tenants. Ironically, land may again become a desired commodity, with developers looking to position themselves as 'build-ready' for these companies. Waverton Commerce Park, CenterPoint Properties, McDonald Development, the Regional Companies, Liberty Properties, ProLogis, Devon USA and others all have significant entitled land holdings in Suffolk.

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The general industrial market has remained weak. Softness in the construction industry, defense spending, and light manufacturing continues to inhibit recovery. The service sector has also suffered in the current economy. Buildings that used to command a premium, such as small warehouse properties with yard space, have taken longer to lease, with diminished rental rates in comparison to past years.

VACANCIES AND ABSORPTION

In 2011, the Hampton Roads region saw vacancy rates edge downward. It appears vacancy rates peaked in 2010 at 12.48% with a reduction in 2011 to 12.12%. The Southside saw vacancy declines in 7 of the 12 submarkets, finishing the 2011 year 1.1% lower than in 2010. Markets that saw improvements were 'core' markets, such as Norfolk Industrial Park (4.2% drop in vacancy) and Airport Industrial Park (6.12% drop). Outlying markets, further from the center of population in Hampton Roads, continue to work through vacant space.

Southside submarkets that improved included two of Chesapeake's three submarkets: Greenbrier Area and the Bainbridge/Elizabeth River area. Both saw absorption of over 200,000 square feet by multiple tenants and multiple transactions. Vacancy rates for both finished the year around 8%. These are indicators of a return to health in these submarkets.

Suffolk also recorded a reduction in vacancy of 4.19%. Distribution and supply chain related companies accounted for the bulk of the leasing, with positive absorption of over 475,000 square feet in existing space. Suffolk also saw renewed activity in development, with CenterPoint Properties constructing two new build-to-suites totaling almost 700,000 square feet.

Markets that saw significant increases in vacancy rate include:

Lynnhaven	**+5.09%**
Greenwich/Cleveland Street	**+3.2%**
Portsmouth	**+4.14%**
Isle of Wight	**+7.05%**

The Peninsula submarkets were consistent in 2011 with virtually no change in the total vacancy rate. There were a number of internal changes of note, including the demolition of the Hiden warehouses, a group of WWII vintage buildings owned by the Huntington-Ingalls shipyard. These buildings totaled approximately 900,000 square feet, and reduced the size of the Copeland/Lower Peninsula area Submarket substantially.

Copeland has historically had to carry Camp Morrison as a vacancy. At approximately 600,000 square feet, this has contributed, perhaps unfairly, to the total vacancy of 17.73%. Also in Copeland, the former Speigel warehouse at 5201 City Line Road came on the market in 2011, adding 352,000 square feet to vacancy, bringing the total to almost 2 million square feet empty.

On the other side of the ledger, Oyster Point/Middle Peninsula and the Williamsburg Extended Submarkets both held to vacancy rates of less than 7%. These would be good rates in a healthy economy.

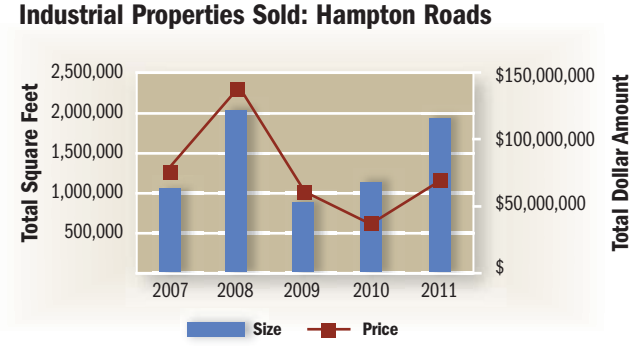
Submarket Totals

Submarket	City	Bldgs Surveyed	Reporter	Total Sq Ft	Vacancy Sq Ft	Vacancy %
Greenbrier Area	Chesapeake	283	Kaempfe	8,593,530	718,667	8.36%
Bainbridge/S. Elizabeth River Area	Chesapeake	143	Worley	5,829,489	447,921	7.68%
Cavalier Industrial Park Area	Chesapeake	189	Mumey	6,138,520	884,537	14.41%
Norfolk Commerce Park/ Central Norfolk Area	Norfolk	143	Remick	5,492,451	622,279	11.33%
Norfolk Industrial Park Area	Norfolk	352	Dickinson	10,408,152	788,433	7.58%
West Side/Midtown Norfolk Area	Norfolk	277	King	6,780,759	546,271	8.06%
Lynnhaven Area	Virginia Beach	283	Baker	8,618,677	1,648,242	19.12%
Greenwich/Cleveland Streets Area	Virginia Beach	125	Beasley	3,057,300	300,717	9.84%
Airport Industrial Park Area	Virginia Beach	72	Beasley	3,641,362	445,215	12.23%
City of Portsmouth	Portsmouth	158	Walker	4,228,501	478,849	11.32%
City of Suffolk	Suffolk	126	Throne	11,637,163	1,638,902	14.08%
Isle of Wight	Isle of Wight	34	King	3,807,023	980,650	25.76%
Southside Totals		**2,185**		**78,232,927**	**9,500,683**	**12.14%**
Copeland/Lower Peninsula Area	Peninsula	346	Culbreth	11,218,810	1,989,149	17.73%
Oyster Point/Middle Peninsula Area	Peninsula	129	Phillips	4,395,259	284,829	6.48%
Oakland/Upper Peninsula Area	Peninsula	116	Culbreth	4,829,759	669,549	13.86%
Williamsburg Extended Area	Peninsula	62	Phillips	9,128,673	625,487	6.85%
Peninsula Totals		**653**		**29,572,501**	**3,569,014**	**12.07%**
Totals		**2,838**	**Sanker**	**107,805,428**	**13,069,697**	**12.12%**

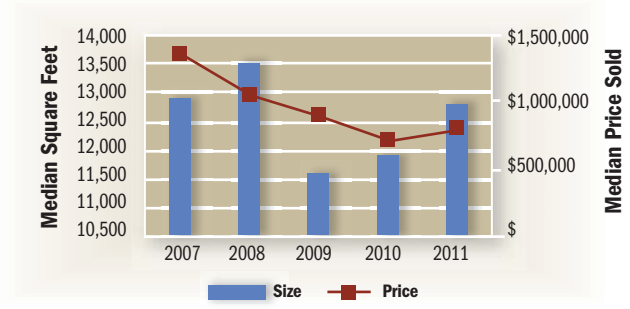
BUILDING SALES

Sales activity grew fairly dramatically in 2011. 36 buildings sold, totaling 2,106,555 square feet, valued at almost $78 million. This is a significant jump over 2010 totals of 1,143,117 square feet sold valued at over $36 million.

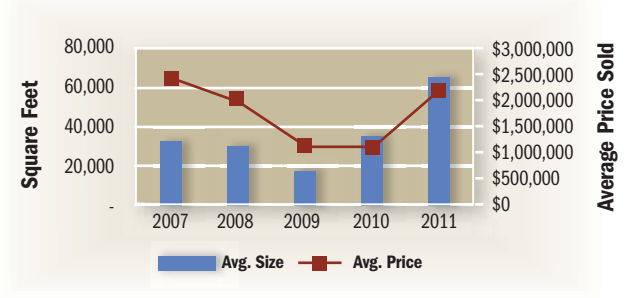
Industrial Properties Sold: Hampton Roads



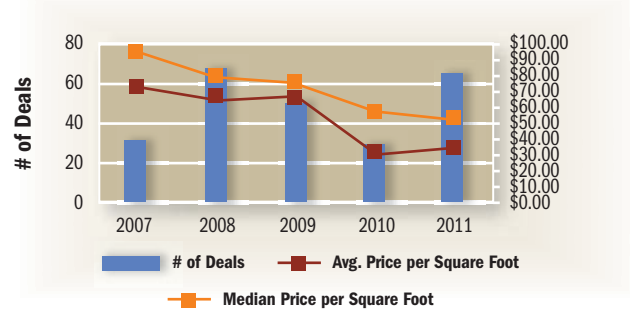
Median Industrial Properties Sold: Hampton Roads



Average of Industrial Properties Sold: Hampton Roads



Number of Industrial Properties Sold: Hampton Roads



A few analytical notes:

- **Numbers:** Generally trending upward across the board.
- **Average Size:** Larger building sales continue to skew the average results.
  - The former Ford building at 2424 Springfield Avenue in Norfolk of 664,000 square feet sold to KTN.
  - MDV Nash Finch purchased their leased building of 601,640 square feet at 3616 Virginia Beach Boulevard in Norfolk.
  - Iron Mountain purchased 112,000 square feet at 4555 Progress Road at foreclosure, also in Norfolk. They were leasing the property.
  - 272 Benton Road in Suffolk sold to the City of Suffolk. 83,413 square feet on 17 acres.
- **A significant number of smaller building sales** were completed in 2011. While nowhere near peak transaction volumes in 2008 and 2009, we are seeing a broad improvement market wide.

OTHER REPRESENTATIVE BUILDING SALES

3527 Business Center Drive, Chesapeake			
February 2011	7,434 square feet *Fenced yard area.*	$815,000	$109.63 per square foot
2010 Amedeo Court, Suffolk			
August, 2011	30,000 square feet *New, tilt-concrete, no improvements, bank REO property.*	$1,272,000	$42.40 per square foot
1164 Kingwood Avenue, Norfolk			
April, 2011	11,611 square feet *Older facility undergoing retrofit*	$747,000	$64.34 per square foot
230 Enterprise Drive, Newport News			
September, 2011	83,413 square feet	$1,900,000	$22.78 per square foot
805 Live Oak Drive, Chesapeake			
July, 2011	22,645 square feet *46% office build-out*	$1,650,000	$72.86 per square foot
121 Old Aberdeen Road, Hampton			
July, 2011	5,440 square feet *Smaller building*	$435,000	$79.96 per square foot
2861 Crusader Circle, Virginia Beach			
December, 2011	23,000 square feet *Owner financing*	$1,650,000	$71.74 per square foot

LEASING

Lease rates saw modest increases in 2011. *CBRE Hampton Roads* reported in their 4th Quarter Hampton Roads Industrial Report that "Current average leasing rates rose from $4.41 per square foot triple net to $4.62 per square foot triple net." It is expected that rates will continue to increase in 2012 as absorption continues to remove quality product from the market. The small space market and the large block market are expected to experience increasing rents. Both can expect to experience shortages of available space.

Older generation distribution space will continue to have high vacancy rates, particularly those properties in the 50,000 to 100,000 square foot range. Functionally obsolete mid-size properties between 10,000-40,000 square feet in older environs will also face challenges filling their space.

New speculative space should be received well in the market.

REPRESENTATIVE INDUSTRIAL LEASING

160 Wellman Street, Norfolk	4,153 square feet *General industrial*	$5.80 NNN psf/yr
4021 Seaboard Court, Portsmouth	6,500 square feet *1 acre fenced and stabilized yard*	$9.79 NNN psf/yr
5621 Raby Road, Norfolk	8,000 square feet *General industrial*	$6.25 NNN psf/yr
1417 Miller Store Road, VB	8,509 square feet *General industrial*	$5.94 NNN psf/yr
1347 Diamond Springs Road, VB	23,033 square feet *Warehouse*	$5.30 NNN psf/yr
981 Scott Street, Norfolk	24,657 square feet *Custom retrofit, crane service added*	$7.95 NNN psf/yr
2125 Smith Avenue, Chesapeake	37,623 square feet *Warehouse*	$5.00 NNN psf/yr
713 Fenway Avenue, Chesapeake	38,000 square feet *Warehouse*	$3.60 NNN psf/yr
5601 City Line Road, NN	42,000 square feet *Warehouse*	$3.58 NNN psf/yr
550 Woodlake Drive, Chesapeake	67,615 square feet *High quality manufacturing space*	$5.75 NNN psf/yr
3700 Village Avenue, Norfolk	110,000 square feet *Warehouse*	$3.25 NNN psf/yr

RENTS FOR AVAILABLE SPACES BY SIZE RANGE 2011

<5,000 square feet	$5.00-$7.00
5,000 to 20,000 square feet	$4.50-$6.00
20,000-40,000 square feet	$3.25-$5.25
40,000-60,000 square feet	$3.00-$4.50
>60,000 square feet	$1.00-$4.00

MAJOR MARKET ACTIVITY

Aside from normal market transactions, there have been a number of significant industrial market developments worthy of note.

- *Former Ford Plant*. This project traded first to Jacoby Development in total for $14.25 million, who in turn sold the main manufacturing building to KTN for $10.4 million. Jacoby retained 46 acres of land now on the market for sale.
- *Ace Hardware*. CenterPoint landed this build-to-suit of 336,960 square feet at their project in Suffolk.
- *US Navy Exchange*. CenterPoint also secured this build-to-suit requirement of 350,000 square feet in Suffolk.
- *CalCartage*. McDonald Development landed this cross-dock requirement of 385,000 square feet at their Virginia Commerce Center off Kenyon Road in Suffolk, Virginia.

- *DANA*. Another build-to-suit project landed in Northern Suffolk at Liberty Properties Bridgeway Commerce Center: 126,000 square feet.
- *Regional Commerce Center, the Regional Company*. This building of 400,000 square feet in Suffolk off Rt. 460 scored no less than four tenants for their new building: Art FX, 80,000 square feet; Caspari, 65,000 square feet; Massimo Zanetti, 67,500 square feet, and Best Brakes, 38,000 square feet.
- *Green Mountain Coffee*. Johnson Development announced the pending sale of their 330,000 square foot warehouse building along with additional acreage for expansion.
- *IMS Gear*. Miller Group in Virginia Beach will be providing a new facility for IMS Gear in the Lynnhaven area. Total square footage: 112,000 square feet.
- *Enviva LP* purchased and opened their new 60 acre deep water terminal on the Elizabeth River to export over 3 million tons of wood chips and pellets per year to Europe.

A few thoughts on these major transactions:

First, the leasing and sales may be a precursor to activity in the market related to the Panama Canal expansion, with expected completion in 2014. Second, we may be seeing the leading edge of an economic recovery, led by major corporations anticipating the upturn and need for space. Third, build-to-suits dominate the larger transactions. This is a common occurrence nationwide. The absence of speculative building, coupled with a lack of remaining large facilities, has forced large users to look to developers with entitled land to construct facilities to their specifications. Look for 2012 to continue this trend as long as large entitled sites are still available. Note the following comments from around the country:

Raleigh, North Carolina

> **"Vacancy rates continue to demonstrate disparate performance between Class A assets with clear heights above 24' and ESFR sprinkler systems versus older facilities without these features. While the overall market vacancy continues to hover around 20%, vacancy rates within Class A product continue to be relatively tight at 7% market wide."**
>
> — *Christopher Norvell, Managing Director*
> *Cassidy Turley*
> *Southeast Real Estate Business, January 2012*

Tampa, Florida

> **"We are beginning to see a shortage of Class A warehouse space for users 100,000 square feet or larger. With the combined Tampa, Pinellas and Lakeland markets ending 2011 at 6.7% vacancy, you would think developers would start new construction."**
>
> — *Bruce K. Erhardt, Executive Director*
> *Cushman and Wakefield of Florida*
> *Tampa Bay Land Market Overview 4Q 2011*

Nationwide

> **"Industrial markets in the United States have also begun the recovery process. Integra Realty Resources research indicates that the underlying fundamentals in the industrial sector have improved only slightly over the course of the last three years, as a glut of speculative space built throughout the country prior to the crash is only now beginning to be absorbed. With this space beginning to be absorbed and little speculative building adding supply to the market in recent years, the sector could be poised for the strongest rebound in coming years as demand for space recovers."**
>
> — *Integra Realty Resources*
> *Real Estate Value Trends*
> *Viewpoint 2012*

REGIONAL INFLUENCES ON THE LOCAL MARKET

Beyond real estate transactions, the following events occurred in 2011 and will influence the Hampton Roads industrial market for years to come.

- **The Port of Virginia:**
  - With the installation of a new Board of Directors, the Port is expected to move into 2012 with a resolve to build on the modest improvements shown in 2011.
  - TEU volumes (import and export) at the Port of Virginia were up in 2011 by 1.2% to 1.9 million TEU's.
  - The Federal Government has agreed to a FY12 budget that includes $26.9 million for the expansion at Craney Island.
  - Intermodal transport is expected to be a major innovation in moving containers off the APM terminal to Suffolk for both the CSX and NS rail lines. In 2011, rail container traffic increased by 26%.
  - The Virginia Port Authority signed a five year lease to operate the Port of Richmond, providing barge traffic.
- **Industrial Properties:**
  - Development of the remaining large waterfront properties should occur in 2012 with growing demand for break bulk offloading and exporting. Recent examples include agricultural product exported to China, stone imported for road and tunnel construction in Hampton Roads, and manufacturing and maintenance for offshore wind facilities.
  - Exports of specialty products are also expected to increase demand for heavy industrial real estate. Wood pellet exports, coal export, steel and metal recycling.
  - General manufacturing. Domestic and international companies consider Hampton Roads and Commonwealth of Virginia a good place to do business. Labor, right-to-work state, cost of living and quality of life consistently rank high when compared to other areas.

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CONCLUSION: CUSHMAN AND WAKEFIELD, BAY ENVIRONMENTAL, AND AMAZON.COM

Where is the market going in 2012? Will the Panama Canal really stimulate the local industrial warehousing market? Will we continue to see major announcements for Hampton Roads and the Commonwealth of Virginia? First, a look at the national industrial market for a little perspective:

The national economy is beginning to show some life, as related by Mr. Ken McCarthy, Senior Economist, Research with Cushman and Wakefield in New York:

"The US Labor Department reported that the economy added 243,000 payroll jobs in January 2012, the largest increase in employment since last April. The strongest job growth was in the professional business services sector…Large increases were also reported in the manufacturing sector (50,000+ jobs). For the real estate industry there is nothing more important than employment. More jobs represent demand for space. So a return to healthy job growth is the most positive sign in the last six months. Rising spending will also spur higher demand for manufacturing, warehouse and other industrial spaces. We are cautiously optimistic on 2012…"

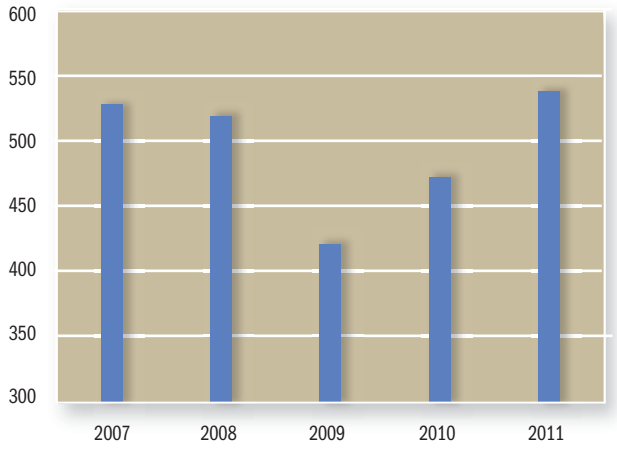
A few more thoughts on the national market from Tina Arambulo of Cushman and Wakefield, Director, Southern California & U.S. Industrial Research:

- More than 306.3 million square feet of new leases were completed during the year, up 14% from 268.8 square feet signed in 2010, and the highest level of activity since 2007. Of the 33 U.S. industrial markets tracked by

Cushman & Wakefield, 22 reported an increase in new activity. Markets with the largest year-over-year gain in leasing included: Central & Northern New Jersey (+ 83.2%), Phoenix (+ 76.1%), Miami (+ 44.2%) and Dallas/Fort Worth (+ 32.4%).

- For leases over 100,000 square feet, there were 538 deals signed during the year, an increase of 14.0% over 2010 and 28.1% over 2009. This year's total is also more in-line with levels seen prior to the recession. With big-box users dominating leasing activity in 2011, the large distribution hub markets have captured a significant share of the activity. The Inland Empire market in Southern California captured 37.8% of new leases signed over 500,000 square feet in the U.S.
- With double-digit growth in on-line retail sales, E-commerce firms like Amazon.com have emerged as an important part of U.S. industrial demand. During the year, Amazon.com signed a 1.2-msf lease for a fulfillment center in Phoenix and two facilities totaling 1.8 million square feet in Indianapolis. Demand for big-box warehouse and distribution centers accelerated significantly in 2011 and we expect to see continuing demand for Class A big-box space in key logistics hubs such as Inland Empire, New Jersey, Chicago, and Dallas/Fort Worth.

U.S. Leasing Activity over 100,000 square feet



Source: C&W Research Services. NOTE: Only markets tracked by Cushman & Wakefield offices are included in this analysis which includes new leases, expansions and subleases not counting renewals.

It should be reasonable to expect the Hampton Roads market to benefit from a national upturn in the economy and the industrial market in general. The recent announcement concerning Amazon.com locating two new fulfillment centers in Virginia should help the confidence of Hampton Roads looking into next year. Amazon chose Virginia over other states, and most of the positive business features of Virginia as a business environment apply to our region.

On the other end of the spectrum, Bay Environmental is a local Chesapeake firm providing environmental surveys of commercial buildings and land in Hampton Roads. Phase I environmental inspections are commonly done prior to the purchase and/or financing of real estate. Bay Environmental reported the following summary of Phase I studies they have performed by year, giving us a 'street level' view of the market.

Year	Bay Environmental number of Phase I studies performed
2006	120
2007	120
2008	60
2009	30
2010	40
2011	60

Finally, the Port of Virginia with plenty of TEU capacity, positions the Hampton Roads region for a good 2012. Look for the decreasing vacancy trend to continue, rental rates in most sectors to firm up, and more build-to-suit construction.

Industrial Submarkets

Southside

Airport Industrial Park
Bainbridge
Cavalier
Central Norfolk
Cleveland
Greenbrier
Lynnhaven
Norfolk Industrial Park
Portsmouth
Suffolk
West Norfolk

Peninsula

Copeland
Oakland
Oyster Point
Williamsburg Extended