HAMPTON ROADS 2006

INVESTMENT

MARKET SURVEY

Acknowledgements

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2006 INVESTMENT

GENERAL OVERVIEW

This report analyzes commercial real estate investments, during the year 2005, 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 buildings 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 2005 survey is the second in the series. Data has been collected for the period January 1, 2005 through December 31, 2005. As this report was required for publication at the end of December 2005, 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 individual transactions.

The focus of this survey is on the four primary types of commercial investment real estate including 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.

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NATIONAL OVERVIEW

The commercial investment property real estate market remained at a record breaking pace throughout the entire year. Interestingly, 2005 was a duplicate of 2004, with more capital looking for opportunities, higher prices, more portfolio transactions, and more tightening of capitalization rates. Some of the factors that influenced this year's market included a change in the flow of foreign capital, condominiums, low interest rates and interest-only mortgages, mobility of capital and the economic recovery.

The change in the flow of foreign capital was brought up from Down Under. Australia more than doubled their acquisitions of commercial real estate in the United States during 2005. Their acquisitions reached over eight billion dollars as they became the largest buyers of strip centers and major owners of office and industrial properties. The Australians accounted for almost 40% of all foreign acquisitions for the year. Germany represented the second largest single group of investors as they acquired over $4 billion worth of real estate. They were followed by the Middle East with over $2 billion in acquisitions and then all others rounded out the field with over $7 billion in acquisitions. All told, foreign investors will have spent over $21 billion on U.S. real estate in 2005.

Developers buying commercial properties for conversion to condominiums were the largest single group of buyers during 2005. Condo converters spent over $30 billion to acquire commercial properties, 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. We will have to wait and see how this frenzy of conversion activity holds up with the slow down in the residential market. Regardless of how their efforts turn out, condominium converters were a major influencing factor for 2005's commercial investment market.

Interest rates rose slightly but remained historically low throughout the year. The availability of inexpensive capital kept investors looking for acquisitions while willing to pay higher prices for these deals. As a result, capitalization rates crept down again this year and prices continued at their record high levels. In addition to inexpensive capital, lenders were more aggressive and there was an abundance of interest-only mortgages made available. Almost 70% of recent conduit loans were interest-only or partial interest-only. This allows leveraged investors to maintain acceptable cash flows on aggressively priced deals. This could prove risky down the road for some buyers.

The mobility of capital has exploded 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 west. Major market buyers are flocking to secondary sites; all are looking for means to increase their yields. Secondary and tertiary markets became popular as prized properties in these markets were snapped 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.

It appears the long lost recovery 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 justification of higher prices and lower capitalization rates for most deals. The economy continues to trod along and it appears most investors are very optimistic about the coming years. The past year was a challenge for many commercial investors but the market remained aggressive and flexible, continuing to adjust to global influences. 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 as investors continue to prefer hard assets.

HAMPTON ROADS OVERVIEW

The Hampton Roads commercial investment market has been setting a blistering pace as it benefited from the mobility of capital and a stable economic base. In spite of the concerns and efforts 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 an increase in average nonagricultural employment. The gains are not large, but they are positive, reinforcing the stability of the market. One of the largest factors influencing the local investment real estate market for 2005 was the increase in portfolio sales. There were a significant number of transactions recorded locally that were part of larger national portfolio sales. In addition, a significant number of properties have been purchased by entities now focusing on the Hampton Roads region. The best example of this is First Potomac Realty Trust which has made a substantial investment in the local industrial and office market with acquisitions totaling over $100 million. Commercial real estate investment sales in the Hampton Roads region totaled over $770 million for 2005.

APARTMENTS

The national apartment market is still showing robust activity with an increase in acquisitions over last year and declining capitalization rates for the year. Although West Coast capitalization rates are frequently below 6% for quality properties, the national average for transactions valued over $5 million has ended the year right at 6%. That reflects a drop of 70 basis points during the year. The national average price per unit for garden style apartments has continued to climb to a high of $96,000 per unit. That reflects a 20% increase over the course of the year. Institutional buyers are still actively adding to their portfolios but condo converters have been the driving force in the current market. Condo converters acquired over 175,000 apartment units, effectively taking them off the rental market during the year.

The Hampton Roads apartment market is also showing continued robust activity. With vacancy rates among the nation's lowest, hovering around 3.5% and positive employment numbers for the year, this market is continuing to attract a lot of attention from buyers and builders. Builders have been very aggressive and the projected 1,753 units scheduled for delivery during the year made this the strongest year since 1988. Represented as a percentage of buyers, condo converters are not as active locally as they have been on the national scene. In addition, the number of properties that were part of portfolio sales dropped significantly.

The number of properties acquired during the year was close to the record levels of 2004, but the number of actual units sold dropped significantly. We recorded 2,837 units sold during the year compared to 3,810 for 2004. In addition the average price per unit has dropped approximately 13% down to slightly above $66,500 per unit. The range of per unit values is not as disperse as we saw in prior years with a low for this year of $30,000 and a high of $121,787 per unit. Estimated capitalization rates ranged from 5.3% up to 9% with the majority in the mid 7% to mid 8% range. The drop in total and price per unit numbers is reflective of smaller properties being sold during the year.

Major transactions for the year included Lake Ridge Apartments in Hampton that sold for $34,344,000. Lake Ridge has 282 units that sold for $121,787 per unit with an estimated going in capitalization rate of 5.3%.

Significant transactions over $5 million for 2005 included:

Development	City	Units	Price	Price/Unit
Lake Ridge	Hampton	282	$34,344,000	$121,787
Oak Lake	Chesapeake	172	$15,710,000 *	$91,337
Ivy Stone	Chesapeake	368	$33,610,667 *	$91,333
Jefferson Point	Newport News	208	$17,859,000	$85,861
Dockside	Norfolk	190	$12,300,000	$64,737
Briarwood	Virginia Beach	600	$31,500,000	$52,500
Independence Square	Virginia Beach	152	$7,800,000	$51,316
Riverside Terrace	Norfolk	232	$11,600,000	$50,000
Warwick Village	**Newport News**	**160**	**$6,800,000**	**$42,500**

**Price Allocated*

OFFICE

Nationally, office properties remained high on the shopping list with a reported total acquisition volume estimated at $100 billion. The fundamentals that direct the office building market have continued to improve over the year and thus investment activity has remained strong. With capitalization rates low and construction costs still rising there is continued pressure on prices. Average prices for suburban office buildings rose to $174 per square foot, reflecting a gain of 22% during the year. Capitalization rates continued their downward trend, dropping 70 basis points for the year and closing the year at 7.3% for suburban office buildings. Central business district office buildings ended the year with average prices at $245 per square foot and capitalization rates hovering around 6.6%.

While the rental market for Hampton Roads office buildings has remained unimpressive, the sales market had another robust year. Just under two million square feet of office product changed hands during the year which reflects a turnover of approximately nine percent of the total market. The average price per square foot continued its upward trend from $109 per square foot in 2004 to $127 per square foot in 2005. This percentage increase is slightly below the national average. In a market where the needs for office space tend to be limited, the rise in the per square foot values is attributed to a variety of factors that include: lower local vacancy rates, scarce new construction, significant increases in the cost of new construction and steadily improving basic market fundamentals.

Major transactions for the year included the sale of the 400,000 square foot Joint Forces Simulation facility on Lake View Parkway in Suffolk for $68,500,000. This office building was sold as part of a portfolio sale of 14 buildings from Fortress Investment Group out of New York to a joint venture between Rubican America Trust and NGP Capital. The allocated per square foot building value for the sale was $171. Also in Suffolk, the office building across the street at 115 Lake View Parkway sold for $24,537,558. In addition, 150 West Main Street in Norfolk is under contract to an undisclosed buyer for approximately $50,500,000.

Significant transactions, over $5 million, for 2005 included:

Address	City	GBA	Amount	Price/SF
Lake View Parkway	Suffolk	114,045	$24,537,558	$215
Corporate Boulevard	Norfolk	53,830	$9,507,487	$177
Lake View Parkway	Suffolk	400,000	$68,500,000	$171
Jefferson Avenue	Newport News	98,083	$14,500,000	$148
Crossways Boulevard	Chesapeake	220,501	$28,000,000	$127
Commerce Drive	Hampton	71,066	$8,527,920	$120
Executive Drive	Hampton	134,179	$15,400,000	$115
Viking Drive	Virginia Beach	74,395	$6,750,000	$91
Bute Street	Norfolk	92,000	$5,750,000	$63

RETAIL

The national retail investment market led all other property types to start the year and has held the glamour spot of property types for most of the year. During the summer, average prices per square foot for strip centers reached an all time high. The national average capitalization rate was at an all time low of 7%. During the second half of 2005 the retail market appeared to have lost some of its momentum. Fall 2005 showed a shift in the strip center market with average per square foot prices dropping as much as $24 and average capitalization rates actually rising one half a point. Strip centers managed to finish off the year almost back at the peak per square foot prices of $161 but with average capitalization rates still up slightly to 7.4%. Malls and other retail investments showed the same end-of-summer slump as seen with the strip centers. The average price per square foot actually finished the year almost $22 off the early summer high of $180 per square foot and average capitalization rates ended the year very close to where it started, at 7.2%. The slip in the retail sector may be due to Real Estate Investment Trusts not raising as much capital from Wall Street in 2005, more money flowing into development than acquisitions, and an anticipated weakening of consumer retail spending in the coming year.

In 2005, the Hampton Roads retail market had one of the most active years for development since 1990. Vacancy rates continued their downward trend and finished off the year at 7.7%. Retail investment sales were brisk with close to 1.6 million square feet changing hands. A significant number of transactions were actually part of several national portfolio transactions involving as many as 69 properties in a single portfolio. Cedar Shopping Centers purchased six centers in the region as part of an eleven-property portfolio. These portfolio sales highlight the mobility of investment capital around the country. In the Hampton Roads market, the average price per square foot rose close to 17% during the year to close at an average of $103 per square foot. Estimated capitalization rates ranged from 6.7% up to 11.4%. Freestanding retail and drug stores showed going in capitalization rates of 6.7% to 7% while strip centers averaged going in rates closer to 8%.

Major retail transactions for the year included Suffolk Plaza Shopping Center, Smithfield Shopping Center and General Booth Shopping Center, all of which were purchased by Cedar Shopping Centers as part of an eleven property, $93.8 million, portfolio. These properties sold for $16 million, $12.4 million and $12 million, respectively, with an allocated per square foot value of $101. Separately, Wal-Mart Way Crossing Shopping Center in Chesapeake sold for $19,399,669.

Significant transactions, over $5 million, for 2005 included:

Property	City	GBA	Price	Price/SF
Eckerd Drug Lynnhaven	Virginia Beach	13,813	$5,760,800	$417
Wal-Mart Way Crossing	Chesapeake	80,160	$19,399,669	$242
General Booth SC	Virginia Beach	73,320	$12,048,353 *	$164
Smithfield SC	Smithfield	123,620	$12,491,831 *	$101
Little Creek SC	Norfolk	66,120	$6,681,442 *	$101
Suffolk Plaza SC	Suffolk	160,803	$16,249,182 *	$101
Coliseum Marketplace	Hampton	117,000	$11,822,878 *	$101
Kempsville SC	Virginia Beach	71,420	$7,217,008 *	$101
Kroger Plaza	Virginia Beach	63,324	$6,246,759 *	$99
Hilltop Plaza SC	Virginia Beach	152,025	$13,200,000 *	$87

** Price allocated*

INDUSTRIAL

The national industrial 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 continues to struggle with high vacancies. Both property types saw average prices per square foot fluctuate up and down during the year by as much as 20%, but closed lower than their peak for the year. The national average price per square foot for both warehouse space and flex space did rise during the year, at about 10%. Nationally, flex properties ended the year at an average price per square foot of $99 while warehouses ended the year with an average price per square foot of $55. Because warehouse properties are considered by investors to be more stable than flex properties, the national average capitalization rates are reflective of the slight spread. Both property types saw their capitalization rates fluctuate but eventually go down for the year. The national average capitalization rate for warehouse properties was 7.6% while the national average capitalization rate for flex space was at 7.7%.

2006 INVESTMENT

The Hampton Roads industrial investment market set a blistering pace during 2005. The volume of industrial investment property sales more than tripled over the prior year. Portfolio sellers and buyers targeting Hampton Roads set the pace, accounting for 80% of the investment transactions during 2005. Hampton Roads saw over 2.8 million square feet of investment property valued over $122 million change hands. The average price per square foot climbed only slightly to $43. These buyers saw substantial value opportunities in the local market.

Major industrial investment transactions included the purchase of four warehouses owned by D.D. Jones in Chesapeake by First Potomac Realty Trust. These warehouses totaling 712,500 square feet sold for $29,000,000. First Potomac Realty Trust also purchased the former Gateway Computers building in Hampton, the former Lucas property in Hampton and Bay Warehouses in Chesapeake. First Potomac Realty Trust's investment in Hampton Roads industrial properties totaled over $68 million during 2005, which represents more than half of all the industrial investment acquisitions in Hampton Roads for the year. Branscan Real Estate Opportunity Fund purchased four buildings in the Norfolk Commerce Park as part of a national 25 building portfolio acquisition. The local investment by Branscan totaled over $25.5 million, which represented over 20% of all the industrial investment acquisitions in Hampton Roads for the year.

Significant transactions for 2005 included:

Address	City	GBA	Price	Price/SF
Lucas Way	Hampton	182,175	$12,100,000 *	$66.42
Robin Hood Road	Norfolk	165,000	$9,177,300**	$55.62
Cavalier Boulevard	Chesapeake	300,000	$13,200,000	$44.00
Fenway Avenue	Chesapeake	168,000	$7,200,000	$42.86
Diamond Hill Road	Chesapeake	267,000	$10,867,434**	$40.70
Campostella Road	Chesapeake	216,000	$8,791,632**	$40.70
Campostella Road	Chesapeake	154,000	$6,268,108**	$40.70
Gateway Boulevard	Hampton	421,000	$14,010,000	$33.28

** $60,000 was for office component*
*** Allocated - indicates the property was part of a multi-building portfolio transaction*