NATIONAL PERSPECTIVE
RELATIVE TO CY 2015 COMMERCIAL ASSESSMENT CHANGES

- Commercial real estate is viewed as a more predictable investment asset, unlike stocks, bonds, and other paper assets, which tend to fluctuate rapidly and react swiftly to economic sentiment. Commercial real estate performance is also sensitive to economic shifts. Changes tend to happen more slowly with assets usually encumbered with long-term leases which allow commercial assets to better weather downside risk.

- The volume of commercial acquisitions in the City involving other commercial property classes was nominal during the course of 2014, with owners of performing assets unwilling to sell, except at a premium. For the most part, purchasers have a clear preference for Class A "core" investment-grade properties which has acted to compress capitalization rates and increase values. In 2014, there were a number of purchase opportunities in Class B properties, which are generally older but maintain good management and quality tenants.

- The City divides the commercial real estate market into the following classes of property: conventional office buildings; hotels/motels; traditional shopping centers; multi-family rental apartments; industrial warehouses; and general commercial.

UNEMPLOYMENT

- The City of Alexandria's unemployment rate was 3.6% for November of 2014, just slightly lower than the previous year when it stood at 4.0% according to statistics compiled by the U.S. Bureau of Labor Statistics. The November 2014 unemployment rate for the Washington-Arlington-Alexandria Metropolitan Statistical Area was 4.5%. These compare favorably with the November rate of 4.8% within Commonwealth of Virginia, and the national unemployment rate of 5.6% (seasonally adjusted as of November 2014).

OFFICE MARKET OVERVIEW

- This year, the City's overall commercial office property tax base increased by only 0.60% from the original January 1, 2014 assessment to January 1, 2015, or $26,543,049 million from $4.418 billion in CY 2014 to $4.445 billion in CY 2015. This minimal increase reflects increases in vacancy and collection losses, and landlords' willingness to provide concessions to retain tenants; which was offset by the National Science Foundation (NSF) building start.

- Market conditions in Alexandria remained soft as weak tenant demand kept vacancy elevated. Growth is primarily attributed to escalated rental rates of in-place leases. Political uncertainty and tenant rightsizing continued to limited leasing and sales activity during 2015. The Washington D.C. region's economy has slipped in the last few years from one of the fastest growing economies in the U.S to one of the slowest growing regional economies in the U.S. Investors are still reluctant to take on risks in the office building market. New office construction in the region is almost exclusively occurring within a ¼ mile of operating Metrorail stations. However, in 2014 this market showed some improvement over prior years as evidenced by the increase number of transfers in the commercial office sector. Some of these value plays designed to improve the operating position of the property.

- According to statistics compiled by the CoStar Group's Year-End 2014 report, the City of Alexandria contained a conventional office inventory of approximately 20.2 million square feet with a vacancy rate of 16.7% including the 605,000 square foot Victory Center and a small inventory of sublet space. The average reported full-service rent in the City was $30.46 per-square-foot in 2014.

- Market conditions in Alexandria remained soft as weak tenant demand and densification kept vacancy elevated and rental rates stagnate. For the most part, leasing activity was concentrated in small to medium sized transactions. The largest new lease in the City was the very short-term renewal of the GSA's lease for the Department of Defense (DoD) on the entire 606,575 square foot office building at 200 Stoval Street in the Hoffman Town Center in the Eisenhower Valley. The building is fully leased but not fully occupied. Upon expiration in April 2017, it is anticipated the building will be completely vacated as the DoD the occupants slowly re-locate to Crystal City during the term of the lease renewal.

- Proximity to Washington, DC remains a long-term advantage for the Northern Virginia office market. Offices located inside the Capital Beltway (I-495) continue to outperform their counterparts outside the ring. Generally, the diversified tenant base provides an element of stability.

New Construction Activity

- The 700,000 square foot headquarters of the NSF is now under construction at 2401 Eisenhower Avenue in the Hoffman Town Center. It is scheduled for completion in the first quarter of 2017. The 605,000 square-foot Victory Center, in the West End of the City along the Eisenhower Avenue corridor, remains completely vacant with only core and shell complete.

- Although there were more commercial office transfers in 2014 as compared to prior year's activity, the number of office building sales remains low. There were 13 sales of commercial office buildings in 2014 versus five transfers in 2013. Four of these, however, represented the sale of the entire, four-building Canal Square project. The 2014 office sales are summarized in the table below.

Property Location	Sale Date	Building Size in SF NLA	Consideration	Price/SF of NLA
115 South Union Street	9/30/2014	27,256 SF	$8,500,000	$311.86 SF
Canal Square Plaza (4 Buildings)	10/16/2014	523,670 SF	$176,000,000	$336.09 SF
950 North Washington	2/18/2014	19,907 SF	$4,500,000	$266.08 SF
209 Madison Street	7/1/2014	90,318 SF	$22,500,000	$249.12 SF
1650 King Street	6/23/2014	50,825 SF	$18,000,000	$354.16 SF
2900 Eisenhower Ave	6/20/2014	60,000 SF	$18,250.000	$304.16 SF
2800 Eisenhower Ave	6/13/2014	114,000 SF	$13,475,000	$118.20 SF
301 North Fairfax Street	4/10/2014	19,492 SF	$4,575,000	$234.71 SF
1199 North Fairfax St	3/18/2014	106,465 SF	$24,625,000	$231.30 SF

Conclusions and Projections

- Analysis of 2014 data for commercial office buildings does not support a projection of substantially improving market conditions for this market segment during 2015. Nationally, increasing vacancy rates are making investors cautious.

HOTEL MARKET OVERVIEW

- Although operating statistics summarized below indicate improvements in hotel operations. The overall performance of the City's hotel market in 2014 was uneven at best. For the second year in a row, the base for this property type decreased, in this case by 13.27%, or approximately $108.85 million, from $820.40 million in CY 2014 to $711.55 million for CY 2015.

- There are a total of 23 hotels in the City with a total of 4,253 rooms. This number includes the 88-room Fairfield Time Share near the King Street Metro. The smallest hotel is the 26-room Towne Motel on North Washington Street in Old Town and the largest is the 496-room Hilton Mark Plaza, a high-rise, convention hotel located in the Mark Center office park in the northwest quadrant of the City. Existing hotels are scattered throughout Alexandria with a large concentration in the Landmark/Van Dorn area and in the Old Town/Old Town North areas.

- Historically, the Washington area was less affected than the national hospitality market due to the presence of the Federal government, and Alexandria's convenient location inside the Beltway. Federal budget cuts and sequestration have tempered room demand to the point that the government consisted of only about 30% of current demand in the City.

- Hotels are considered to be leading economic indicators as they are generally operated on a day-to-day basis and respond quickly to changes in the national economy.

- Changes in Occupancy, Average Daily Room Rate (ADR) and Revenue per Available Room (RevPAR) over the last three years are in the table on the following page. The tables reflect City data from July through December for each year. The first table is an aggregate or summary report that does not distinguish among types of hotel. *Smith Travel Research (STR)* also reports hotel summaries divided into the following categories: "Upper Upscale", "Upscale and Upper Midscale" and "Midscale, Economy and Independent". This segregated data is summarized on the Table 2.

- Taken as a whole, the most recent market indices would suggest improving market conditions. Although it will likely require another years' of data to provide definitive support, the tables indicate that 2013 represents the worst year, with the lowest operational data for hotels in the City in recent years with as regards Average Daily Room Rate (ADR) and Revenue per Available Room (RevPAR).

- Both tables demonstrate that 2014 was a year of improvement for the Alexandria hotel market place. This is due, in part, to the fact that several hotels, either temporarily closed (Holiday Inn on Eisenhower) or underwent a changes in highest and best use to multi-family apartments (Washington and Hawthorne Suites) and are no longer part of the hotel room inventory in the City. The changes in land use added to the multi-family tax base.

It should be noted that the CY 2014 data detailed in the following tables is skewed by the loss of the aforementioned three hotels.

Table 1: Occupancy %, ADR, and RevPAR: City of Alexandria CY 2012 - CY 2014

Measure	2012	2013	2014
% Occupancy	67.2%	66.1%	70.7%
ADR	$137.41	$129.31	$140.44
RevPAR	$92.38	$85.51	$99.29
Source: Smith Travel Research - December 2014			

Table 2: Changes by Hotel Class from 2013 and 2014 – July through December

Hotel Class	Occupancy	ADR	RevPAR
Upper Upscale	4.7%	5.4%	10.4%
Upscale/Upper-Mid	7.6%	9.2%	17.5%
Midscale/Economy	10.2%	16.3%	28.1%
Source: Smith Travel Research - December 2014			

- There was one sale of a hotel in the City in 2014. On June 17, 2014, the 246-room Hilton Metro Place Hotel sold for a consideration of $93,938,000 or $381,861 per room. As the name implies, the hotel is located directly opposite of the King Street Metro station. The sale was reported to be an arm’s length transaction that included significant consideration paid for non-real estate components such as fixtures, furniture, and equipment (FF&E) and franchise related values.

- Income and Expense data from responding hotel operators for calendar year 2013 indicate that well-located hotels, particularly near the King Street Metro station, for the most part operate successfully.

- The hotels located in the West End of the City are the most distressed segment of the Alexandria hotel market. In the past, this market consisted of the Washington Suites hotel, the Alexandria Suites hotel, the Days Inn, the Comfort Inn, and Bragg Tower. As of the date of valuation, January 1, 2015, the Washington Suites and Alexandria Suites had converted to multi-family residential apartments. Unlike the other three hotels in the West End, both improvements were originally designed and operated as multi-family properties, which facilitated re-conversion to their original purpose.

- For many years, the Best Western - Old Colony Hotel, adjacent to the North Old Town Holiday Inn was assessed as an operating hotel, with excess land available for development. Although the hotel is still in operation, the owners are seeking approvals to redevelop the site with 24 residential townhomes that will be known as the North Parc Residences. The hotel improvement currently on the site will not be retained. As a result, for 2015, the property is now valued based on its redevelopment potential and not as an operating hotel.

Projections for 2015

- Despite the declines in performance noted above, market evidence indicates that the hotel market is still seen as an attractive investment. For example, in addition to the former Holiday Inn site across from the NSF site, there is a 400-room hotel approved for development in the Hoffman Town Center and there are preliminary plans for a 625-room hotel in the Potomac Yard mixed-use development. The Carr group is in the process of building a 109-room "boutique" hotel at 1620 Prince Street; and developers recently received approvals to build a 120-room hotel on the former Cummings warehouse site on Union Street as part of the Old Town waterfront re-development plan.

- The NSF headquarters building is now under construction in the Hoffman Town Center on Eisenhower Avenue. It is estimated that upon completion in 2017, the NSF, will add 60,000 to 90,000 hotel room nights annually to hotel room demand in the City. As a consequence, the former Old Town Holiday on Eisenhower is likely to reopen, and additional hotel rooms will likely be built in the NSF area.

- In spite of the positive activity summarized above, the outlook for the Alexandria hotel market is mixed. Negative factors include the fact that there is continued uncertainty in the market concerning the Federal government's continuing budget/debt crisis, and the continuing subpar performance of hotels in the City's West End market. Interviews with knowledgeable market participants indicate a mood of "cautious optimism" for the hotel market in 2015.

SHOPPING CENTER MARKET OVERVIEW

- The base for shopping center properties between 2014 and 2015 increased slightly. It rose by 2.48%, or $13,548,172; from $546.89 million in CY 2014 to $560.43 million for CY 2015. The 2015 increase in value was entirely attributable to appreciation. There was no new growth as of January 1, 2015 for this land use. The 2.487% increase in the base for shopping centers is modest but also indicates an almost complete recovery from the 3.23% decrease in shopping center values suffered between 2013 and 2014.

- The city has 25 properties classified as shopping centers. Except for Landmark Mall and the Potomac Yard center, the remaining multi-tenant shopping centers would generally be considered neighborhood strip centers, many of which being anchored by a grocer.

- Although Landmark Mall has continued to be in a holding pattern, pending planned redevelopment, the City's 24 other centers, including the 589,905 square-foot Potomac Yard Center, have continued to perform well with most enjoying stable occupancy levels and operating positions. Most of these centers have a grocery and/or drug store anchor tenants. The owners of the highly successful Potomac Yard Center are continuing to plan for the future redevelopment of the property with a 7.5 million square-foot, mixed-use project.

- Alexandria regional shopping center vacancy (excluding Landmark Mall) is hovering at 3.8%, down from 4.5% at the end of the second quarter of 2013. The vacancy rate for neighborhood and community centers in Northern Virginia was 5.9% for the same period.

- Alexandria has grown its sales tax base year-over-year ending in June 2014, according to AEDP; whereas the surrounding localities saw a decrease in retail sales tax. The King Street Retail merchants have enjoyed some of this increase and this has been reflected in some of the sales activity. Of particular interest are the national chain stores that are trading at lower cap rates with what is perceived as a lower risk investment.

- A number of national and regional chains have now located in Old Town. We believe, overall this will be a positive influence for all of the retailers, as higher foot traffic usually results in to higher sales in a given market area. AEDP also notes that hotel occupancy has been near record breaking for 2014. This type of transient foot traffic also drives retail sales and ultimately real estate values.

- King Street retail properties reflect a very low vacancy rate, indicating a higher demand for retailer location in Old Town. A final note, which could lead to positive results for general commercial retail properties along King Street, is the large number of new apartment communities that have been recently built in the Old Town, Braddock, and Potomac Yard areas. Over 1500 new apartment units have come on-line with many more in the pipe-line. These new City residents have disposable income that will be added to the local retail sector leading to positive results.

Summary and Projections

- Nationally, a decrease in consumer spending in 2014 and increasing vacancy rates are making investors cautious. Some centers suffer from increased vacancy and collection losses and are offering concessions, extensive build-out, and periods of free rent in order to attract or retain tenants. However, income and expense data from shopping centers in the City indicate that this market sector continues to perform well, with a very modest growth over the previous year.

MULTI-FAMILY MARKET OVERVIEW

- The multi-family rental apartment market tax base increased 4.60% for CY 2014 (Attachment 1, Page 1, Line 30, Column 5) to $6.3 billion. Excluding new growth (which included the hotel to apartment conversions), the multi-family increase was flat at 0.30%, a very small portion of the increase. This represents a continuation of CY 2014 when this class led all of the commercial sectors by increased 9.20%, over the previous year. New growth in CY 21014 of $287.3 million was complemented by $19.3 million in appreciation.

- Nationally the multi-family market leveled off in 2014. The lack of multi-family transfers during 2014 support this trend. Locally, the market saw slight declines based on the risk of federal budget cuts and increased multifamily supply. "With apartment stock anticipated to rise 3.4 percent this year, a potential misalignment of supply and demand will push vacancy higher. Currently, projected completions will exceed demand by nearly 6,000 units and push vacancy to a level not posted since 2009."[1] Construction of new multifamily projects increased the number of units in Alexandria by 1,553 units and several more projects will be completed in 2015, further increasing the number of units in Alexandria. This has led to increased vacancy rates and concessions in Class A apartment properties. Class A and Class B apartment properties saw stabilized rents in 2014 resulting in slight decreases for many of the 2015 valuations.

- There were no investment grade apartment properties sold in the City in 2014, but adjacent jurisdictions reported investment grade apartment sales in 2014. Arlington County reported the sale of one garden style apartment at $139,000 per unit, two mid-rise apartments at $191,630 per unit and $207,500 per unit, and one high-rise apartment at $290,517 per unit. Fairfax County reported the sale of two garden style apartments at $210,030 per unit and $219,959 per unit.

WAREHOUSE MARKET OVERVIEW

- The warehouse market in the City often conforms to national and regional data. The *PwC Real Estate Investor Survey* in capitalization rates in the national warehouse, flex, and R&D markets for the fourth quarter of 2014 indicates a -15 basis point change with a range of 5.0 to 10.0 percent.

- The City does not have a conventional industrial inventory. There are 145 properties in the City classified as warehouses for assessment purposes for CY 2015; four fewer than there were in CY 2014. The number of properties classified as warehouses has decreased for several years due to redevelopment opportunities. Valid sales are typically based on redevelopment potential, indicating the warehouse supply will continue to decrease. Redevelopment pressure may be influencing whether space is leased and the terms of leases that landlords are willing to sign. Above-market vacancy is only concentrated in a few small submarkets. Oakville Industrial Park is an example of a site with proposals to

[1] Change, John and Hughes, William E. 2014. "2014 Real Estate Investment Research: National Apartment Report." *Marcus and Millichap Real Estate Investment Services.*

redevelop as a mixed use project with apartments, townhouses, condo townhouses, retail, office and hotel uses.

- Most warehouse properties saw a modest increase in its assessed value as a result of the lower cap rates. Typical increase ranged from 3% to 4%. The nine self-storage facilities increased in value due to substantial improvements in their operating positions. Overall, the industrial warehouse property tax base increased $11.1 million, or 1.64%, for CY 2015 to $686.99 million (Attachment 1, Page 1, Line 37, Column 6). This was primarily attributable to properties slated to be redeveloped in the near future.

GENERAL COMMERCIAL OVERVIEW

- General Commercial properties typically contain uses such as small retailers, repair and service establishments, restaurants, and financial institutions. This property type is broadly defined as commercial properties that contain less than 12,000 square feet of space. The volume of sales in 2014 for this property type was modest, but it provided an indication of only modest change in some property types, such as convenience stores and drug stores. There is very mixed indicators for small offices, small strip centers/general retail and service stations/garages as well for other types such as restaurants (fast or sit-down) resulting in few changes in market values for 2015 Assessments. All property types were primarily valued for CY 2015 based on comparable sales in the City of Alexandria and in neighboring Metro area jurisdictions, with Income and Expense data lending support for value increases.

- The base for general commercial increased 3.60%, or approximately $50.20 million, from $1.394 billion in CY 2014 to in $1.444 billion CY 2015 (Attachment 1, Page 1, Line 33, Column 6).

- *The U.S. Census Bureau* estimated 5.74% population growth for the City of Alexandria from the April 1, 2010 Census to July 1, 2013. The City's Office of Planning and Zoning estimate a more modest rate of 1.43%. The region, including the City, experienced above average population growth and below average unemployment (3.6% est. November 2014, Source: Virginia Employment Commission) when compared to the nation as a whole (5.5%, November 2014). This, in addition to high income levels ($85,706 Median Household Income, Source: U.S. Census Bureau), contributes to a strong local economy, essential for the strength of this property type.

- According to "Retail Research- Market Overview, Washington D.C. Metro Area" published by Marcus & Millichap 3rd Quarter 2014: "quality inventory inside the Beltway receives the strongest interest and is challenging to find. Here net-lease assets with national credit tenants can begin trading in the low-5 percent range."

- The following categories of general commercial were changed based on national and regional trends, due mostly to higher rents and lower capitalization rates, and higher sales prices which drive value increases: fast food, convenience stores, drug stores, banks, auto dealerships, specialty shops and restaurants

- Alexandria has grown it's sales tax base year-over-year ending in June 2014, according to AEDP; whereas the surrounding localities saw a decrease in retail sales tax. These categories noted have enjoyed some of this increase and this has been reflected in some of the sales activity. Of particular interest are the national chain stores that are trading at lower cap rates with what is perceived as a lower risk investment.

- A number of national chains have also come to Old Town. We believe, overall this will be a positive influence for all of the retailers, as higher foot traffic usually leads to higher sales in a given market area. AEDP also notes that hotel occupancy has been near record breaking for 2014. The type of transient foot traffic also drives retail sales and ultimately real estate values.

- A final note, which could lead to positive results for general commercial properties, is the large number of new apartment communities that have been recently built in the City. Over 1500 new apartment units have come on-line with many more in the pipe-line. These new City residents have disposable income that will be added to local retail sector leading to positive results.