ANALYSIS OF THE COMMERCIAL MARKET RELATIVE TO CY 2017 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 2016, 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.

- 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 3.0% for November of 2016, just slightly higher than the previous year when it stood at 2.9 % according to statistics compiled by the U.S. Bureau of Labor Statistics. The November 2015 unemployment rate for the Washington-Arlington-Alexandria Metropolitan Statistical Area was 3.7%. These compare favorably with the December rate of 4.1% within Commonwealth of Virginia, and the national unemployment rate of 4.7% (seasonally adjusted as of December 2016).

OFFICE MARKET OVERVIEW

- This year, the City's overall commercial office property tax base increased by 0.28% from the original January 1, 2016 assessment to January 1, 2017, or $13 million from $4.510 billion in CY 2016 to $4.523 billion in CY 2017.

- Location remains the motivating factor in the City. Old Town and Carlyle areas remain the most desirable. The West End of the City – Park Center, Mark Center, and the Landmark area – continues to suffer vacancy problems, as office tenants seek office locations within walking distance of metrorail stations.

- 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. New office construction in the region is almost exclusively occurring within a ¼ mile of operating Metrorail stations.

- 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.

- The number of office building sales remains low. There were seven sales of commercial office buildings in 2016 versus six transfers in 2015. The 2016 office sales are summarized in the table below.

Property Location	Sale Date	Building Size in SF NLA	Consideration	Price/SF of NLA
810 King Street	12/08/2016	27,878	$13,600,000	$488
1605 King Street	11/2/2016	11,335	$3,504,800	$309
950 N Washington Street	8/24/2016	19,907	$6,250,000	$314
2000 Eisenhower Avenue	4/8/2016	261,021	$44,900,000	$172
312 S Washington Street	2/23/2016	19,181	$3,107,000	$162
1555 King Street	2/3/2016	28,519	$9,469,100	$332
1711 King Street	1/21/2016	11,000	$4,200,000	$382

New Construction Activity

- The 700,000 square foot headquarters of the NSF is under construction at 2401 Eisenhower Avenue in the Carlyle Town Center. It is scheduled for completion in the third 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. The Victory Center owners are actively seeking federal government tenants.

HOTEL MARKET OVERVIEW

- The operating statistics summarized for hotels indicate improvements in hotel operations in 2016. On an equalized basis, the assessed value base for this property type increased, in this case by 16.35%, or approximately $116.0 million, from $709.3 million in CY 2016 to $825.3 million for CY 2017. Of this increase, approximately $11.8 million was attributable to new growth. The Victory Center owners are actively seeking federal government tenants.

- There are a total of 24 hotels in the City with a total of 4,536 rooms. This number includes the 88-room Fairfield Time Share near the King Street Metro. The City's hotels are scattered throughout Alexandria with a large concentration in the Landmark/Van Dorn area and in the Old Town/Old Town North areas.

- There were a number of hotel sales in the City and surrounding jurisdictions in 2016.

2016 sales in the City included: The Hotel Monaco, which sold in December for $96,309,000; Morrison House, which sold in December for $12,081,000; The Holiday Inn North Old Town, which sold in September for $37,822,638; and Bragg Tower, which sold in August for $7,125,000.

- Overall, the market appears to have substantially improved for hotels; as indicated by recent sales in the City and surrounding jurisdictions and construction of The Indigo Hotel at the waterfront on Union Street.

SHOPPING CENTER MARKET OVERVIEW

- The base for shopping center properties between 2016 and 2017 showed some growth in 2017. It increased by 4.2%, or $24.7 million, from $585.5 million in CY 2016 to $610.2 million for CY 2017.

- 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.

- Although Landmark Mall has continued to struggle and will be closing as it is planned for redevelopment, the City's 24 other centers, for the most part, have continued to perform well with most enjoying stable levels of occupancy and stable 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.

- Though there have been no recent sales of shopping centers in the City, Income and Expense data from shopping centers in the City indicate that this market sector continues to perform well.

MULTI-FAMILY MARKET OVERVIEW

- The multi-family rental apartment market tax base increased 2.24% for CY 2017 (Attachment 2, Page 2, Line 26, Column 5) to $6.931 billion. New growth in CY 2016 of $78 million (1.15%) was complemented by almost $74 million (1.09%) in appreciation.

- Nationally, the multi-family market continued the generally static pace in 2016 as seen in 2015, with absorptions keeping pace with recent deliveries of most recently constructed units. The lack of large project, multi-family transfers locally (only one - now known as the Avalon at Potomac Yard) during 2016 supports this trend. The largest urban metropolitan centers have a continuity of mildly upward-trending job growth and a steady supply of young professionals gravitating to urban rental markets which should produce mild rental increases over the coming year.

- Locally, the delivery of new multi-family construction units has slowed due declining rates of absorption of new units. The availability of new construction capital has continued with relatively lower interest rates but changes in the Presidential Administration may obscure clarity of broader investor market trends until at least mid-year 2017. In general, the higher cost of existing multi-family units inside the Beltway has caused investors to look toward existing older Class B & C quality properties to achieve safer, higher returns due to the higher rents.

- One Class A, investment-grade apartment property sold in the City in 2016. The two-year-old property called The Alric at the time of the sale, sold in February 2016 for $108,250,000, which equates to $335,139 per unit. The apartment property is now called Avalon Potomac Yard. Adjacent jurisdictions reported investment-grade apartment sales in 2016. Arlington County reported the sale of one Class A, mixed-use, mid-rise with a substantial multi-family component in the Clarendon submarket called The Market Common for over $400,000 per unit. Fairfax County reported two Class A, mid-rise apartment sales, one Class B, high-rise property, and two older garden projects (Class B & C) along the evolving U.S. Route 1 corridor. Several smaller (11 to 20 Units) Class C properties (built 1930-1965) in the City sold during 2016; most of these sales were part of an investor portfolio transfer.

WAREHOUSE MARKET OVERVIEW

- The warehouse market in the City often conforms to national and regional data. The *PwC Real Estate Investor Survey* for Q4 2016 reports warehouse capitalization rates continue to decrease, ranging from 3.00 to 7.00%, as rents increase and vacancy declines.

- The City does not have a conventional industrial inventory. There are 137 properties in the City classified as warehouses for assessment purposes for CY 2017; 7 fewer than there were in CY 2016. The number of properties classified as warehouses has decreased for several years due to redevelopment opportunities. For example, the multi-parcel site, Oakville Industrial Park, was reclassified as vacant land. The site has proposals to redevelop as a mixed use project with apartments, townhouses, condo townhouses, retail, office and hotel uses. Valid warehouse sales are typically based on redevelopment potential, indicating the warehouse supply will continue to decrease. Redevelopment pressure seems to influence whether space is leased and the terms of leases that landlords are willing to sign. There is very little above-market vacancy concentrated in a few small submarkets.

- Most warehouse properties saw an increase in their assessed values as a result of the lower cap rates and lower vacancy rates. The median warehouse assessment increase was 3.13%, with the typical range from 2.7 to 9%. After accounting for the redevelopment and reclassification of warehouse properties, there was an overall increase of 5.78% in the equalized warehouse assessments from $687,890,671 to $727,636,049. The average assessment of warehouse properties over 20,000 square feet is $134.53 per square foot of gross building area.

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 with less than 12,000 square feet of space. The volume of sales in 2016 for this property type was modest for West End properties, but a robust sales sample was available for Old Town, providing an excellent indication of the overall increase in market values. All property types were primarily valued for CY 2017 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 this property type increased 9.18%, or approximately $141.1 million, from $1.54 billion in CY 2016 to in $1.68 billion CY 2017 (Attachment 2, Page 2, Line 29, Column 5). $10.73 million was due to growth from new construction, $130.4 million was due to appreciation, and the balance of change was due to supplemental assessments over the course of 2016.

- Old Town retail is drawing the attention of institutional investors. A total of 21 parcels were purchased by a single institutional investor at the end of the year (mostly from a single entity that was divesting its portfolio) with a combined sales price of $62.26 million.

- The U.S. Census Bureau estimated population growth of 9.65% for the City of Alexandria from April 1, 2010 (140,006) Census to July 1, 2015 (153,511). Households grew from 72,376 units in (2010) to 76,512 units in (2015) or 5.71%. Median household income is $89,134 in 2015 dollars. 61.4% of persons 25 years of age or older have Bachelor’s Degree or higher. Unemployment in Alexandria stood at 3.0% as of November 2016 per U.S. Bureau of Labor Statistics.