

RETAIL MARKET INVESTOR SURVEY

New Market Real Estate Group (NMREG) surveyed several active market participants in an attempt to capture a consensus regarding current market conditions for grocery-anchored neighborhood, community, and power shopping centers. This survey (see Table 1) was conducted by personal telephone interview in July and August of 2009.

OVERVIEW

The clear message from the respondents is that the shakeout in retail that began in 2008 can be divided into changes in (1) the capital markets and (2) demand for retail space. The combination of both has resulted in a precipitous decline in values. Now that the correction has taken place, investors are left to feel their way along the bottom adjusting to the new dynamics of the market.

The capital market changes that were evident in our prior survey have continued through the end of the Second Quarter of 2009, but appear to have stabilized somewhat. Class distinction is back, with many investors expressing no interest at all in Class-B properties. At the peak of the market, many Class-B properties were bid up and were assigned rates that were previously reserved only for Class-A properties.

The reduction in demand for retail space is a direct result of limited credit availability for tenants and reduced sales volumes. Store closings and bankruptcies have resulted in increased vacancy, reduced market rents, and limited re-leasing prospects. There is, however, a flight to quality with the few tenants positioned to lease space gravitating toward those centers with strong anchors and a dominant market position.

Preferred Property Type

The most desirable product type remains the grocery-anchored neighborhood center, assuming that (1) the center contains the dominant grocer in the area, (2) it is located in a primary market area with good demographics and not too much competitive space, (3) the center is not too large, and (4) there are barriers to entry for new competition. A center adhering to the requirements is considered the “safest” since people will continue to shop at the supermarkets; thus, insuring constant consumer traffic. The limited size of the center translates into a price point that is affordable, financeable, does not unduly concentrate assets, and limits the in-line space that must remain leased and occupied for profitability. While some tenant turnover is expected in these centers and, on average, vacancy rates have been increasing slowly, the vacancies are expected to be short lived as healthy businesses in less healthy centers are expected to gravitate to stronger centers with the most consumer traffic.

The survey respondents strongly indicated that power centers are regarded with a more negative outlook relative to grocery-anchored neighborhood and community centers. In general, there is little or no appetite for power centers with the exception of those anchored by a Wal-Mart or Super Target, having little in-line space, and no big-boxes with questionable viability. They believe that, with few exceptions, this product type has too much concentration on the big-box tenants, which have recently proven that they can be quite risky. Furthermore, many big-box stores are not readily adapted to other tenants or to redevelopment to in-line space. Only those power centers occupied by big-box stores that are considered to be creditworthy and are dominant in their merchandise lines are even considered by some investors. Others have no interest at all.

Table 1
National Retail Market Investor Survey (1)
Neighborhood and Community Shopping Centers, and Power Centers

Item	Participant Number											Range		Average	1Q 09 Survey	
	1	2	3	4	5	6	7	8	9	10	11	Low	High		Average	Change
Neighborhood and Community Shopping Centers (Grocery-Anchored) - Class-A																
Discount Rate																
Low	9.00%	9.00%	9.00%	11.00%	8.00%	9.00%	8.00%	9.00%	8.00%	9.00%	8.00%	8.00%	11.00%	8.82%	8.45%	0.37%
High	10.00%	9.00%	10.50%	15.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	9.00%	15.00%	10.41%	9.65%	0.76%
Average	--	--	--	--	--	--	--	--	--	--	--	--	--	9.61%	9.05%	0.56%
Residual Capitalization Rate																
Low	8.00%	7.50%	7.50%	--	8.50%	8.50%	7.00%	7.00%	8.00%	7.00%	7.50%	7.00%	8.50%	7.65%	7.64%	0.01%
High	9.00%	8.00%	9.00%	--	10.75%	9.00%	9.00%	8.00%	8.50%	9.00%	8.50%	8.00%	10.75%	8.88%	8.66%	0.22%
Average	--	--	--	8.50%	--	--	--	--	--	--	--	--	--	8.26%	8.15%	0.11%
Overall Capitalization Rate																
Low	7.50%	7.00%	7.50%	--	8.00%	8.50%	6.50%	7.00%	8.00%	7.00%	7.00%	6.50%	8.50%	7.40%	7.36%	0.04%
High	8.50%	7.75%	9.00%	--	10.00%	9.00%	8.00%	8.00%	9.00%	9.50%	9.00%	7.75%	10.00%	8.78%	8.23%	0.55%
Average	--	--	--	8.50%	--	--	--	--	--	--	--	--	--	8.09%	7.80%	0.29%
Growth Rates																
Market Rent																
Current Trend (2) (3)	--	-12.50%	-12.5	-15.00%	-10.00%	-15.00%	-7.50%	-7.50%	Down	--	-10.00%	--	--	--	--	--
Annual Change (3)																
Year 1 to 2	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	1.50%	0.00%	1.50%	0.14%	--	--
Year 2 to 3	0.00%	3.00%	0.00%	2.00%	0.00%	0.00%	1.50%	0.00%	0.00%	0.00%	3.00%	0.00%	3.00%	0.86%	-0.30%	1.16%
Year 3 to 4	3.00%	3.00%	3.00%	3.00%	2.00%	4.00%	3.00%	3.00%	1.50%	2.00%	3.00%	1.50%	4.00%	2.77%	2.00%	0.77%
Thereafter	3.00%	3.00%	3.00%	3.00%	2.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	2.00%	3.00%	2.91%	2.95%	-0.04%
Expenses	3.00%	3.00%	3.00%	3.00%	2.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	2.00%	3.00%	2.91%	3.00%	-0.09%

(1) Personal survey conducted by New Market Real Estate Group in July and August of 2009.

(2) Change in market rent since the First Quarter of 2009.

(3) May represent an average of the reported range.

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	1	2	3	4	5	6	7	8	9	10	11	Low	High		Average	Change
Neighborhood and Community Shopping Centers (Grocery-Anchored) - Class-B																
Discount Rate																
Low	--	10.00%	10.00%	15.00%	--	11.00%	9.00%	10.00%	--	--	10.00%	9.00%	15.00%	10.71%	9.89%	0.83%
High	--	10.00%	12.00%	20.00%	--	12.00%	12.00%	11.00%	--	--	14.00%	10.00%	20.00%	13.00%	11.17%	1.83%
Average	--	--	--	--	--	--	--	--	--	--	--	--	--	11.86%	10.53%	1.33%
Residual Capitalization Rate																
Low	--	8.50%	8.50%	--	--	10.50%	8.00%	8.00%	--	--	8.00%	8.00%	10.50%	8.58%	8.55%	0.03%
High	--	9.00%	11.00%	--	--	11.00%	11.00%	9.00%	--	--	9.00%	9.00%	11.00%	10.00%	9.85%	0.15%
Average	--	--	--	10.50%	--	--	--	--	--	--	--	--	--	9.29%	9.20%	0.09%
Overall Capitalization Rate																
Low	--	8.00%	8.50%	9.50%	--	10.50%	7.50%	8.00%	--	--	9.00%	7.50%	10.50%	8.71%	8.35%	0.36%
High	--	8.75%	11.00%	10.50%	--	11.00%	10.00%	9.00%	--	--	10.50%	8.75%	11.00%	10.11%	9.70%	0.41%
Average	--	--	--	--	--	--	--	--	--	--	--	--	--	9.41%	9.03%	0.39%
Growth Rates																
Market Rent																
Current Trend (2) (3)	--	-12.50%	-20.00%	-15.00%	--	-15.00%	-7.50%	-15.00%	--	--	-15.00%	--	--	--	--	--
Annual Change (3)																
Year 1 to 2	--	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	--	--	1.50%	0.00%	1.50%	0.19%	--	--
Year 2 to 3	--	3.00%	0.00%	0.00%	0.00%	0.00%	1.50%	0.00%	--	--	3.00%	0.00%	3.00%	0.94%	-0.80%	1.74%
Year 3 to 4	--	3.00%	3.00%	2.00%	2.00%	4.00%	3.00%	3.00%	--	--	3.00%	2.00%	4.00%	2.88%	1.85%	1.03%
Thereafter	--	3.00%	3.00%	3.00%	2.00%	3.00%	3.00%	3.00%	--	--	3.00%	2.00%	3.00%	2.88%	2.95%	-0.08%
Expenses	--	3.00%	3.00%	3.00%	2.00%	3.00%	3.00%	3.00%	--	--	3.00%	2.00%	3.00%	2.88%	3.00%	-0.13%

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	1	2	3	4	5	6	7	8	9	10	11	Low	High		Average	Change
Power Centers - Class-A																
Discount Rate	--	10.00%	--	12.00%	10.50%	10.00%	--	9.50%	8.00%	--	9.00%	8.00%	12.00%	9.86%	9.39%	0.46%
Low	--	10.00%	--	12.00%	10.50%	10.00%	--	9.50%	8.00%	--	9.00%	8.00%	12.00%	9.86%	9.39%	0.46%
High	--	12.00%	--	15.00%	12.50%	11.00%	--	10.50%	10.00%	--	11.00%	10.00%	15.00%	11.71%	10.93%	0.79%
Average	--	--	--	--	--	--	--	--	--	--	--	--	--	10.79%	10.16%	0.63%
Residual Capitalization Rate	--	8.00%	--	9.00%	10.50%	9.00%	--	7.50%	8.00%	--	8.00%	7.50%	10.50%	8.57%	8.25%	0.32%
Low	--	8.00%	--	9.00%	10.50%	9.00%	--	7.50%	8.00%	--	8.00%	7.50%	10.50%	8.57%	8.25%	0.32%
High	--	8.50%	--	10.00%	12.50%	9.50%	--	8.50%	9.00%	--	9.50%	8.50%	12.50%	9.64%	9.89%	-0.25%
Average	--	--	--	--	--	--	--	--	--	--	--	--	--	9.11%	9.07%	0.04%
Overall Capitalization Rate	--	7.75%	--	10.00%	10.00%	9.00%	--	7.50%	8.00%	--	8.00%	7.50%	10.00%	8.61%	8.14%	0.46%
Low	--	7.75%	--	10.00%	10.00%	9.00%	--	7.50%	8.00%	--	8.00%	7.50%	10.00%	8.61%	8.14%	0.46%
High	--	8.50%	--	11.00%	12.00%	9.50%	--	8.50%	9.00%	--	9.50%	8.50%	12.00%	9.71%	9.71%	0.00%
Average	--	--	--	--	--	--	--	--	--	--	--	--	--	9.16%	8.93%	0.23%
Growth Rates																
Market Rent																
Current Trend (2) (3)	--	-12.50%	--	--	--	-15.00%	--	--	Down	--	-10.00%	--	--	--	--	--
Annual Change (3)																
Year 1 to 2	--	0.00%	--	0.00%	0.00%	0.00%	--	0.00%	0.00%	--	1.50%	0.00%	1.50%	0.21%	--	--
Year 2 to 3	--	3.00%	--	0.00%	0.00%	0.00%	--	0.00%	0.00%	--	3.00%	0.00%	3.00%	0.86%	-0.60%	1.46%
Year 3 to 4	--	3.00%	--	0.00%	2.00%	4.00%	--	3.00%	1.50%	--	3.00%	0.00%	4.00%	2.36%	1.20%	1.16%
Thereafter	--	3.00%	--	2.00%	2.00%	3.00%	--	3.00%	3.00%	--	3.00%	2.00%	3.00%	2.71%	2.90%	-0.19%
Expenses	--	3.00%	--	3.00%	2.00%	3.00%	--	3.00%	3.00%	--	3.00%	2.00%	3.00%	2.86%	3.00%	-0.14%

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	1	2	3	4	5	6	7	8	9	10	11	Low	High		Average	Change
Power Centers - Less Desirable																
Discount Rate																
Low	--	12.00%	--	15.00%	--	12.00%	--	--	--	--	11.00%	11.00%	15.00%	12.50%	9.75%	2.75%
High	--	14.00%	--	20.00%	--	13.00%	--	--	--	--	15.00%	13.00%	20.00%	15.50%	10.25%	5.25%
Average	--	--	--	--	--	--	--	--	--	--	--	--	--	14.00%	10.00%	4.00%
Residual Capitalization Rate																
Low	--	10.00%	--	10.50%	--	11.00%	--	--	--	--	8.50%	8.50%	11.00%	10.00%	8.75%	1.25%
High	--	10.50%	--	12.00%	--	11.50%	--	--	--	--	9.50%	9.50%	12.00%	10.88%	9.75%	1.13%
Average	--	--	--	--	--	--	--	--	--	--	--	--	--	10.44%	9.25%	1.19%
Overall Capitalization Rate																
Low	--	9.75%	--	11.00%	--	11.00%	--	--	--	--	9.00%	9.00%	11.00%	10.19%	8.75%	1.44%
High	--	10.50%	--	12.00%	--	11.50%	--	--	--	--	10.00%	10.00%	12.00%	11.00%	9.75%	1.25%
Average	--	--	--	--	--	--	--	--	--	--	--	--	--	10.59%	9.25%	1.34%
Growth Rates																
Market Rent																
Current Trend (2) (3)	--	-12.50%	--	--	--	--	--	--	--	--	--	-15.00%	--	--	--	--
Annual Change (3)																
Year 1 to 2	--	0.00%	--	0.00%	--	--	--	--	--	--	1.50%	0.00%	1.50%	0.50%	-7.50%	8.00%
Year 2 to 3	--	3.00%	--	0.00%	--	--	--	--	--	--	3.00%	0.00%	3.00%	2.00%	-4.50%	6.50%
Year 3 to 4	--	3.00%	--	0.00%	--	--	--	--	--	--	3.00%	0.00%	3.00%	2.00%	1.00%	1.00%
Thereafter	--	3.00%	--	2.00%	--	--	--	--	--	--	3.00%	2.00%	3.00%	2.67%	3.00%	-0.33%
Expenses	--	3.00%	--	3.00%	--	--	--	--	--	--	3.00%	3.00%	3.00%	3.00%	3.00%	0.00%

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MARKET TRENDS

By historical perspectives, consumer confidence has remained low resulting in a significant decline in discretionary spending. The most common reason cited is fear of, or actual, job loss. During the early summer, many stores were devoid of customers. Even the hot consumer electronics merchants reported significant declines in retail sales levels. Investors are concerned that retail sales levels may deteriorate further if there is not some tangible positive economic news to restore consumer confidence.

Some markets that were experiencing rapid retail expansion now appear to be overbuilt due to the abrupt halt in residential development resulting in a retail-space-per-capita ratio that is too high to support all of the existing space.

Most survey participants are not expecting any dramatic recovery in retail property markets. While there has been leasing activity (both new tenants and renewals) during the Second Quarter, the leasing has not kept pace with the increase in available space and vacancy rates have increased. Those centers anchored by the dominant supermarket chain in the area will likely survive with reasonable occupancy levels and rental rates, and will continue to be sought by investors.

Rental Rates

All survey participants recognize that rental rates have decreased since our First Quarter survey; however, some chose not to generalize since market rents are property and market specific. Most expected further modest declines during the remainder of 2009, particularly in secondary markets, followed by little or no growth for 2010. The increase in market rent is expected to return to near inflationary levels gradually during 2011, achieving inflation by 2012.

One participant suggested market rent increases slightly in excess of inflation for one year but indicated that this was reserved for the best centers in the best markets. Another participant indicated that they recognize that both land values and construction costs have declined. As a result, they are utilizing rent spikes in the later years of a forecast to return rents to the point of feasibility for new construction.

VALUATION ASSUMPTIONS

Some of the more significant trends impacting valuations as indicated by our interviews include the following:

- ❑ With the decline in market rents, many properties are exhibiting contract rent levels that are above today's market levels. Some investors indicated that they are discounting or "stripping out" the premium.
- ❑ The traditional gap between the implied going-in return and the residual capitalization rate is diminishing due to low increases in NOI over the holding period.
- ❑ Very little rent growth is expected prior to 2011.
- ❑ No investors are underwriting lease-up of vacant space in year one and some are not willing to forecast any over the holding period. Any possible upside would seem to belong to the buyer.

TRANSACTION CHARACTERISTICS

Available capital, willing sellers, the quality of properties offered, and transaction time - these issues are all related. All market participants are aware that the current market remains in a contraction phase and that any properties offered for sale are going to command prices that are low compared to historical peak levels. Some believe that the market has reached bottom and that while it may “bounce along the bottom for a while”, improvement is near. Others make a distinction between the primary markets and the other (secondary and tertiary) markets. They indicate that the bottom has probably been reached for the primary markets but that the other markets may still have a way to go.

There are indications that a few properties are being offered by owners that are not under pressure to sell. However, the “ask-to-offer” gap is often too great to overcome and properties are most often not trading or are withdrawn. Only those sellers who are motivated by the need to raise cash to cover redemptions, loan maturities, debt service, or need to improve portfolio loan-to-value ratios are offering properties at prices that buyers are willing to consider. The more desperate the seller is to raise cash, the better the quality of the properties offered for sale.

Some participants reported that there is little or no capital available; however, most claim that there is significant capital available “sitting on the sidelines” waiting to see how the market performs. Generally, the participants believe that the smaller deals in the \$10.0 million to \$50.0 million range are possible while there is limited appetite for the larger deals. As a result, transaction velocity is low.

The \$1.73 billion portfolio sale rumored during our last survey has gone to contract. The 86 grocery-anchored shopping centers were sold by CalPERS for approximately \$210.00 per square foot in 2005. CalPERS is buying them back for \$154.00 per square foot, reflecting a 26.67% reduction in value. The closings are scheduled to occur over the next 24 months.

VALUE TRENDS

Prospective purchasers indicate that they expect stable IRRs, OARs, and TCRs for the foreseeable future for the best properties in the best markets, but modest increases in rates for those properties in secondary markets. Sellers know that the buyers are cautious and will only pursue deals that involve prime properties offered at pricing levels reflective of the current market environment. Most sellers are reluctant to offer their properties for sale during this phase of the cycle. Most offering properties are driven by a need to generate cash for a variety of reasons.

Whether or not there is further erosion in the demand for retail space will be determined by the changes in the economy, particularly employment. Consumer confidence is low primarily due to the fear of losing a job. If unemployment continues to increase, additional declines in market rents and increases in vacancy are expected. Once employment numbers stabilize or turn positive, stabilization of rents and improvement in vacancy is expected. Further changes in space demand are expected to be at a slower pace than the rate of change over the past six months.