# CAPITALIZATION RATE ANALYSIS

## DOUGLAS COUNTY, NEBRASKA

Kenneth Voss, MAI, SRA, CAE

The purpose of this report is to provide the Douglas County, Nebraska Assessor's Office recommended market derived capitalization rates for various property classes and applied for use in ad valorem tax purposes.

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May 25, 2010

Mr. Roger F. Morrissey
Douglas County Assessor
11422 Miracle Hills Drive, Suite 110
Omaha, Nebraska 68154-4420

RE: 2010 Douglas County, Nebraska Capitalization Rate Analysis

Dear Mr. Morrissey:

In accordance with your request, Kenneth Voss & Associates, LLC has researched and analyzed various sales, consisting of apartment/multifamily, office, retail, and industrial properties, to determination overall capitalization rates.

The purpose of the report is to aid your office in determining market derived capitalization rates to be applied for use in ad valorem tax purposes. The scope of this project involves gathering income and expense information on sales of income producing properties from a variety of sources available to the appraiser.

Through the study, I found that most buyers and sellers of investment properties make little or no allowance for replacement reserves. Most of the data reviewed indicated that buyers and sellers were divided when capitalizing net operating income (NOI) after tenant improvements and leasing commissions when quoting and using capitalization rates.

Therefore, I have estimated capitalization rates derived from the market without these items. As noted within the introduction section of this report, the documented capitalization rates are based on actual data at the time of the sale resulting in rates that vary widely due to the actual operations that may be above or below market rates.

Therefore, I have estimated capitalization rates to apply to market net operating income. I have concluded that properties generating below market net operating income would typically sell at capitalization rates lower, than those based on market operation, and that properties currently producing net operating income above a market rent would be expected to sell at higher capitalization rates than indicated by the recommended capitalization rates based on market income and expenses.

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Located on the following pages, is a summary of my opinions of capitalization rates for the various types and classes of property analyzed. The analysis is based on data summarized in the attached report as well as other data contained in the appraiser's files.

Kenneth Voss & Associates, LLC

Kenneth Voss

Kenneth Voss, MAI, SRA, CAE
Principal

# TABLE OF CONTENTS

## INTRODUCTION

The Assessor for Douglas County, Nebraska (the County) has retained Kenneth Voss & Associates, LLC to prepare a Report on Capitalization Rates. The report will assist Douglas County in selecting appropriate overall capitalization rates for four core property types: apartment (multi-family), office, retail and industrial.

Property transactions were analyzed between January 1, 2003 and December 31, 2009. The appraiser focused on the 2007-2009 data, adding sales that were considered appropriate and pertinent in the development of the capitalization rates. The report provides a written summary of my findings, organized under the following headings:

- Executive Summary of Capitalization Rates
- Definitions
- Approaches to Value
- Scope of Work
- Apartment Properties
- Office Properties
- Retail Properties
- Industrial Properties

## EXECUTIVE SUMMARY OF CAPITALIZATION RATES

**RECOMMENDED OVERALL CAPITALIZATION RATES**

| APARTMENT CAPITALIZATION RATES | | | | |
|---|---|---|---|---|
| APARTMENT/MULTIFAMILY | CLASS A | CLASS B | CLASS C | CLASS D |
| ALL PROPERTIES | 7.00% | 8.25% | 9.50% | 11.00% |

| OFFICE CAPITALIZATION RATES | | | | |
|---|---|---|---|---|
| OFFICE | CLASS A | CLASS B | CLASS C | CLASS D |
| ALL PROPERTIES | 7.75% | 8.50% | 9.25% | 10.25% |

| RETAIL CAPITALIZATION RATES-INCLUDING REAL ESTATE TAXES | | | | |
|---|---|---|---|---|
| RETAIL | CLASS A | CLASS B | CLASS C | CLASS D |
| ALL PROPERTIES | 5.50% | 6.50% | 7.00% | 8.75% |

| INDUSTRIAL CAPITALIZATION RATES-INCLUDING REAL ESTATE TAXES | | | | |
|---|---|---|---|---|
| INDUSTRIAL | CLASS A | CLASS B | CLASS C | CLASS D |
| ALL PROPERTIES | 5.50% | 6.00% | 7.00% | 8.50% |

The capitalization rates above are for the class of property indicated. I provided definitions for each class and sub-class for each type of sale analyzed to develop a capitalization rate. Not all capitalization rates developed include replacement reserves.

Although I provided a capitalization rate for each property class, there is a range for each rate, which I estimated at approximately 25 to 50 basis points. The range provides the staff appraiser's movement within each property class.

## DEFINITIONS

The following definitions or terms are used or implied throughout this report. A clear understanding of these definitions and terms provides a foundation of my analysis in the development of the recommended capitalization rates.

***Band of Investment*** A technique in which the capitalization rates attributable to components of a capital investment are weighted and combined to derive a weighted-average rate attributable to the total investment.

- ***Build-Out*** The interior construction that converts raw space into finished space ready for occupancy; includes installation of equipment, finished carpentry, construction of amenities, and initial tenant improvements.
- ***Capitalization*** The conversion of income into value.
- ***Capital Expenditure*** Investments of cash or the creation of liability to acquire or improve an asset, e.g., land, buildings, building additions, or site improvements.
- ***Capitalization Rate***-Any rate used to convert income into value.
- ***Common Area*** The total area within a property that is not designed for sale or rent, but is available for common use by all owners, tenants, or their invitees, e.g., parking and its appurtenances, malls, sidewalks, landscaped areas, recreation areas, public toilets, truck and service facilities.
- ***Common Area Maintenance (CAM)*** The expense of operating and maintaining common areas; may or may not management charges and usually does not include capital expenditures on tenant improvements or other such improvements to the property.
- ***Concession*** A benefit or benefits granted by a seller or lessor to induce a sale or lease.
- ***Debt Coverage Ratio*** The ratio of net operating income (NOI) to annual debt service; measures the ability of a property to meet its debt service out of net operating income.
- ***Discounted Cash Flow*** A procedure in which the discount rate is applied to a set of projected income streams and reversion.
- ***Discount Rate*** An interest rate used to convert future payments into present value.

- ***Effective Rent*** The rental rate net of financial concessions such as periods of no rent during the lease term; the effective rent may be calculated on a discounted basis, reflecting the time value of money, or a simple straight-line basis.
- ***Expense Stop*** A clause in the lease that limits the landlord's expense obligation because the lessee assumes any expense above an established amount.
- ***Going-In Capitalization Rate*** The going-in capitalization rate is usually defined as the first year net operating income (NOI-before capital items of tenant improvements, leasing commissions, and debt service but after real estate taxes) divided by present value or purchase price.
- ***Holding Period*** Average period of time that a property type is held for investment.
- ***Institutional Grade Real Estate*** Real property investments that are sought by institutional buyers and have the capacity to meet generally prevalent institutional investment criteria.
- ***Investor Survey*** The Investor Survey represents comprehensive data sets of investment activity for commercial real estate in a condensed format, providing capitalization rates, debt-coverage-ratios, and band-of-investment data for a variety of property types.
- ***Land-to-Building Ratio*** The ratio of land area to gross building area; one of the factors determining comparability of properties.
- ***Leasing Commissions*** Fees paid to an agent for leasing tenant space. When leasing fees are spread over the term of the lease or lease renewal they are treated as a variable operating expense. Initial leasing fees usually fall under capital expenditures for development and are not included among periodic expenses.
- ***Overall Capitalization Rate*** (Cap Rate, OAR)-An income rate for a total real property interest that reflects the relationship between a single year's net operating expectancy and the total property price or value; used to convert net operating income into an indication of overall property value.
- ***Market Rent*** The most probable rent that a property should bring in a competitive and open market reflecting all conditions and restrictions of the typical lease agreement, including the rental adjustment and revaluation, permitted uses, use restrictions, expense obligations, term, concessions, renewal and purchase options and tenant improvements.
- ***Net Operating Income*** The actual or anticipated net income that remains after all operating expenses are deducted from the effective gross income, but before mortgage debt service and book depreciation. The net operating income may be calculated before or after deducting replacement reserves, leasing commissions and tenant improvements.

- ***Pre-Tax Yield (IRR)*** The pre-tax yield is the rate of interest that discounts the pre-income tax cash flows received on an unleveraged investment back to a present value that is exactly equal to the original equity investment.
- ***Replacement Reserve Allowance*** An allowance that provides for the periodic replacement of building components that wear out more rapidly than the building itself and must be replaced during the building's economic life.
- ***Reversion*** A lump-sum benefit that an investor receives or expects to receive at the termination of an investment (holding period).
- ***Terminal (Residual) Capitalization Rate*** The terminal capitalization rate is the rate used to estimate resale or reversion value at the end of the holding period. Typically, it is the net operating income (NOI) in the year following the last year of the holding period. Similar to the going-in capitalization rate, but applied at the end of the holding period.
- ***Vacancy and Collection Loss*** A deduction from potential gross income made to reflect income reductions due to vacancies, tenant turnover, and nonpayment of rent.

As these terms apply directly to this study, the Overall Capitalization Rate (Cap Rate) and Net Operating Income (NOI) are the most important elements to the analysis. When referring to the capitalization rates within this report, the appraiser is implying that the NOI reflects a property's income potential at normal or stabilized operating levels regarding the rent, vacancy, and expenses. Consideration is also given to the point in time of the NOI estimate. This means whether or not the NOI is based on actual, previous year, current or projected income estimates. In estimating overall capitalization rates, the development of these rates in the analysis must be consistent.

**APPROACHES TO VALUE** Douglas County office properties are valued by mass appraisal. Mass appraisal is defined as the appraisal of groups of property as of a given date using standardized procedures and statistical testing. It differs from individual property appraisal, or fee appraisal, primarily in scope and quality control.

In the appraisal of real estate, there are three standard approaches to value: the cost approach, the sales comparison approach, and the income. Although all three approaches are given consideration, the income and sales comparison approaches are the preferred methods for most office properties.

The income approach is the process of estimating the future benefits to be generated by a property and converting them into an indication of present value. There are two methods that may be used to apply this process: yield capitalization and direct capitalization. In Douglas County, the direct capitalization method is used. Direct capitalization employs a single year of stabilized net income to estimate value. Models are developed from market sources and are applied to groups of similar properties. Standardized procedures and statistical testing are used to ensure accuracy.

The primary elements used in the income models are income, expenses, vacancy and collection loss, and a capitalization rate. Once developed, the models are applied to the properties by a computer assisted mass appraisal system (CAMA). Vacancy and collection loss and expenses are deducted from the property's potential gross income. The resulting net operating income (NOI) is divided by the capitalization rate to estimate the property's value. The models are designed to reflect the value of a typical or mean property in any given class. If the appraiser applying the model believes an individual property differs significantly from the typical property in the group, adjustments may be made to the model to reflect the differences.

## SCOPE OF WORK

The appraiser is required to identify the scope of work sufficient to produce credible results that are supported to the degree necessary for the intended use of the assignment. It is important that both the appraiser and the client fully understand the scope of work to ensure that it is appropriate for the intended use of the assignment. It is the intent of this assignment that all appropriate data pertinent to the development of this assignment to be collected and confirmed.

The Scope of Work sufficient for this engagement encompassed the following methodology:

- Meet with the Douglas County, Nebraska Appraisal Staff to discuss the study, review process and approaches to be undertaken
- Review the available data and information accessible in the Assessor's office and other sources for transactional data
- Determine a reasonable sample size of improved sales to accomplish the study for each property type analyzed
- Determine the most acceptable approach to developing net operating income (NOI) for the various property types
- Determine the most acceptable method to developing vacancy percentages
- Determine the most acceptable method to develop operating expense ratios
- Discuss which approaches and techniques are most acceptable and should be employed to support the capitalization rates such as transactions, investor interviews and surveys
- Develop a matrix of capitalization rates appropriate for the building classes and subcategories and review our conclusions with the County and submit our final report

## COMPETENCY STATEMENT

The appraiser has the appropriate knowledge, education, and experience to complete this report. The appraiser's professional qualifications are included in the **Addenda.**

## FORMAT OF REPORT

The following pages contains four distinct property types but similar in the narrative description. Each property type begins with a general over view of the Douglas County, Nebraska market through the fourth quarter 2009. The local overview is followed by a series of national publications providing an in-depth overview of the particular property under discussion. This part is followed by brief descriptions of the major class and subclasses of the property under discussion.

The critical part is the analysis of market sales by class with the capitalization rate and price per square foot for an additional measure I considered. I provided a range of capitalization rates, minimum-to-maximum, and the median and mean capitalization rate.

The final section deals with an overview of the capitalization rates and the final determination of capitalization rates.

## OPERATING EXPENSES

Proper appraisal practice requires the detailed analysis of operating expenses. A failure to properly estimate allowable operating expenses can significantly influence the potential net operating income or forecasted cash flows and thus the appraised value of commercial real estate.

The following pages illustrate two scenarios. The first scenario is developing a capitalization rate with or without replacement reserves. The second scenario is developing a capitalization rate with and without real estate taxes.

## CALCULATIONS-REPLACEMENT RESERVES

The following is an example of how we derived the various overall capitalization rates. In the example below, I assumed a 10,000 gross square foot office building with 9,500 net square feet sold for $750,000 and had a gross potential income of $95,000 with a 5% vacancy and collection loss. Fixed expenses were $8,000 (real estate taxes and insurance) and variable expenses of $15,000 (management, administration, maintenance, and utilities).

| | | | |
|---|---|---|---|
| GROSS POTENTIAL INCOME | | | $95,000 |
| LESS: 5% VACANCY & CREDIT LOSS | | | -$4,750 |
| EFFECTIVE GROSS INCOME | | | $90,250 |
| LESS EXPENSES | | | |
| FIXED | $ 8,000 | | |
| VARIABLE | $ 15,000 | | |
| TOTAL EXPENSES | | | $23,000 |
| NET OPERATING INCOME BEFORE RESERVES | | | $67,250 |
| | | | |
| LESS RESERVES | | | |
| | ROOF & PAVING | $2,500 | |
| | RENOVATION | $5,500 | |
| TOTAL RESERVES | | | $8,000 |
| | | | |
| NET OPERATING INCOME AFTER RESERVES | | | $59,250 |

The overall capitalization rate without replacement reserves, tenant improvements, and leasing commissions is 8.97% ($67,250 before replacement reserves divided by the sales price of $750,000). The overall capitalization rate with reserves is 7.90% ($59,250 after replacement reserves divided by the sale price of $750,000). The property may be appraised with either capitalization rate as long as it is applied to the proper net operating income as illustrated below:

NOI **BEFORE REPLACEMENT RESERVES** $67,250

Sale Price $750,000

Overall Capitalization Rate 8.97%

**OR**

NOI **AFTER REPLACEMENT RESERVES** $59,250

Sale Price $750,000

Overall Capitalization Rate 7.90%

If leasing commissions, tenant improvements or a greater allowance for replacement reserves were included as a deduction to derive the net operating income, the overall capitalization rate would be reduced by a pro-rata amount. The estimated overall capitalization rate without replacement reserves, leasing commissions and tenant improvements can be applied consistently within a specific property type and investment class. The majority of sales that were analyzed represent overall capitalization rates **without** replacement reserves. The market consistently cited rates in this manner.

## CALCULATIONS-REAL ESTATE TAXES (OMITTED)

The below illustration below does not include real estate taxes as a fixed expense.

| | | | |
|---|---|---|---|
| GROSS POTENTIAL INCOME | | | $95,000 |
| LESS: 5% VACANCY & CREDIT LOSS | | | -$ 4,750 |
| EFFECTIVE GROSS INCOME | | | $90,250 |
| LESS EXPENSES | | | |
| FIXED | | | |
| REAL ESTATE TAXES **(OMITTED)** | **$ 7,500** | | |
| INSURANCE | $ 500 | | |
| VARIABLE | $15,000 | | |
| TOTAL EXPENSES | | | $15,500 |
| NET OPERATING INCOME | | | $74,750 |

The overall capitalization rate without real estate taxes is **9.97%** ($66,750 divided by the sales price of $750,000). Assessors add (load) the effective tax rate component to the estimated composite or base capitalization rate; in these cases, no specific expense deduction are made for real estate taxes.

## CALCULATIONS-REAL ESTATE TAXES (INCLUDED)

The below illustration includes real estate taxes as a fixed expense.

| | | | |
|---|---|---|---|
| GROSS POTENTIAL INCOME | | | $95,000 |
| LESS: 5% VACANCY & CREDIT LOSS | | | -$ 4,750 |
| EFFECTIVE GROSS INCOME | | | $90,250 |
| LESS EXPENSES | | | |
| FIXED | | | |
| REAL ESTATE TAXES **(INCLUDED)** | **$ 7,500** | | |
| INSURANCE | $ 500 | | |
| VARIABLE | $15,000 | | |
| TOTAL EXPENSES | | | $23,000 |
| NET OPERATING INCOME | | | $67,250 |

The overall capitalization rate with real estate taxes is **8.97%** ($67,250 divided by the sales price of $750,000).

The rational for loading the base capitalization rate is to preclude circular reasoning. By adding the effective tax rate to the capitalization rate, sufficient income is afforded to pay the taxes based on documented market value. Any bias in indicated value caused by reliance on previous assessed value or historic taxes is removed.

The effective tax rate is the product of the nominal tax rate and the assessment ratio. The effective tax rate provides the actual tax rate paid on the assessed value of the property.

The following pages provides my analysis and interpretation of income producing properties that were sold on the open market, specific market data on each property class where capitalization rates were developed, national and local indices.

## MARKET CONDITIONS

- Leasing activity is down in the real estate market over the last year and appears the trend will continue into 2011. Investors are concerned about the economy, future tenant demand (concessions) and tenant requirements (space).
- More stringent underwriting criteria and lack of debt funds has limited the number of real estate transactions.
- The volatility of the real estate market has seen sellers pull out of the market, and those remaining are negotiating prices that are below last year's acceptance level. The trend will continue into 2011.
- All sectors of the real estate market has seen a continuing decline in sales activity over the past two years.
- The failure of major banks around the country has lead to further erosion of consumer confidence in the real estate market. Residential foreclosures have led to a downturn in the commercial real estate market.
- In the final analysis, capitalization rates have gradually increased over the past two years, and unfortunately will continue to increase.

The current economy problems leading into the real estate market will not improve in the near future, but will linger until there is a move to increase job availability. The investment market is at a standstill; few properties are being sold, and when sold, usually at a lower price than originally offered making an analysis of where capitalization rates difficult

## EMERGING TRENDS IN REAL ESTATE

The Urban Land Institute and KORPACZ/PRICEWATERHOUSECOOPERS publish annually ***Emerging Trends in Real Estate***. The 2010 publication contained the following comments:

- The commercial real estate industry hits bottom in 2010, suffering a surge of painful writedowns, defaults, and workouts.
- Debt markets will remain severely compromised; resuscitated banks will increase lending slowly, employing strict underwriting standards, and requiring significant equity stakes from borrowers.
- A lackluster economic recovery characterized by problematic job growth will hamper the pace of any real estate market resurgence, which probably cannot gain much traction until late 2011 or 2012.
- Commercial property sectors generally avoided overbuilding, but slack demand pushes up vacancies and many new projects cannot hope to meet leasing projections or debt-service obligations.
- Value losses will be mitigated somewhat in the top-tier markets as institutional and foreign buyers look to acquire prime assets, keeping prices from free fall; capitalization rates in these cities rise close to or above historic norms from unsustainably low levels.

- And, *Emerging Trends* surveys indicate 2010 will be the worst time for investors to sell properties in the reports 30-years history, but will offer a much-improving environment to buy (with cash).

Referencing capitalization rates, the trend is upward, with the following points:

- Borrowers can find loans, but at "expensive," back-to-the-future pricing, 60 to 65 percent loan-to-value ratios, 7 to 7.25 percent interest rates, and 1.4 debt-service coverage.
- Shifts in capitalization rates indicate increases in all sectors of the commercial real estate market, from 25 to 250 basis points.
- Decreasing net operating income, coupled with increased vacancies and tenant concessions, and the ever-increasing capitalization rates, will continue to lower value.

## MARKET DATA

I researched and assembled sales of improved properties for this assignment. These sales were verified by one of the participating parties or a third party, or from a reliable source were utilized in my database. A number of sales were not included because of various reasons arising from validity and/or arm's length transactions.

The market data that an appraiser relies on is always dated but this factor is especially important in a market environment we are experiencing currently. Sales activity has declined across all commercial real estate sectors over the past two years. Overall capitalization rates across all commercial real estate sectors have increased during the same period. Therefore, with limited sale activity to rely on, I have to consider many different data sources to assist in the concluded overall capitalization rates. An important source is interviews with local real estate appraisers, forming a consensus about the current market conditions and the concluded overall capitalization rates.

The purpose of this section is to define capitalization rates and their use in this study. It is organized in five sub-sections:

1. Derivation of capitalization rates
2. Capitalization rates selection criteria
3. Direct capitalization strengths and weaknesses
4. Property class transition
5. Capitalization rate spreads

## DERIVATION OF CAPITALIZATION RATES

A capitalization rate study is a relationship of a single year of net operating income estimate from a property compared to its sale price. Capitalization rates can vary based upon the net operating income analyzed in this study. The net operating income may reflect the actual (historical) net income, the year-to-date annualized, or next year's budgeted net income. Generally, market transactions are based on the next twelve month budgeted net income or current-in-place net income. This is an area of inconsistency and should be understood in developing capitalization rates.

Capitalization rates may be derived from abstraction from market sales, mathematical formulas, and investor surveys. The emphasis in this study has been placed upon actual market transactions, investor surveys, and published studies.

- ***Published Studies***: Most surveys are performed on a national basis, then segregated into regional areas. Real Estate Research Corporation, Reis, Korpacz Real Estate Investor Survey (KORPACZ/PRICEWATERHOUSECOOPERS), RealtyRates.com, and Real Capital Analytics were analyzed for this study. Of the surveys analyzed, only Real Estate Research, Reis, and Real Capital Analytics addressed each property type in the Omaha area specifically. The surveys typically provide a range of capitalization rates applicable to certain property types and generally involve only investment or institutional grade properties.

  Each of the surveys cited in this study reflect investment grade property. An investment grade property includes only Class A and above average Class B real estate.

- ***Personal Interviews***: I conducted a personal interview of various appraisers and acquisition/dispositions professionals during the week of June 8, 2009 to gather data into the Omaha investment market, focusing mainly on capitalization rates. The results of these interviews follow:
  1. Few properties are trading, making it difficult to estimate real estate prices and capitalization rates currently and in the near future.
  2. Assets in second-tier cities, as Omaha are being adjusted 50-150+ basis points above national capitalization rates depending on the type of property.
  3. Capitalization rates have increased in all commercial real estate sectors, a trend that will continue into 2011/2012, or until lenders are willing to finance properties at reasonable terms.

## CAPITALIZATION RATE SELECTION CRITERIA

Various economic and physical factors influence the risk of a particular investment and its implied capitalization rate. These criteria should be understood in the application of and selection of capitalization rates. The economic and physical factors that affect risk are considered to be as follows:

- **Current alternative yields** involve rates of returns available in the current real estate market from alternative investments such as mortgages, bonds, and certificates of deposit.
- **Ease of entry into development of product type** may take years to conceive, approve, and develop whereas others are easily processed through the development cycle and possibly subject to overbuilding. This may restrict supply and influence capitalization rates.
- **Financing** is the availability and price of debt, which has a direct impact on new development and property transactions. Capitalization rates analyzed in this study assume an unleveraged position or cash equivalent financing. However, the availability of financing has an impact on

the potential buyer's ability to purchase a property since most commercial real estate is purchased with financing. The recent "credit crunch" has severely influenced activity in all types of real estate.

- **Geographical/Political Forces** can influence either positively or negatively the willingness of investors to purchase or develop property in an area. These issues could involve zoning, transportation issues, utility, infrastructure issues, and real estate taxes.
- **Location** is critical to the success of a real estate development and involves factors such as demographics, transportation, exposure, and marketability.
- **Management burden** varies by type of property and can influence expense ratios and, consequently capitalization rates accruing to certain property types.
- **Ownership position** refers to the interest or the estate being transferred such as fee simple, lease fee, or leasehold. The interest created by leases, mortgages, etc. can affect the risk ascribed to an investment.

Property specific criteria include the following:

- **Occupancy/Rollover Risk:** Overall capitalization rates are typically analyzed on an "as if" or stabilized basis. High vacancy rates or near term tenant expirations or rollover risk can influence the capitalization rate acceptable to a potential purchaser.
- **Tenancy:** A real estate investment is a portfolio of leases. The lease terms and conditions, lease type, credit worthiness of the tenants, quantity, quality, and durability of the income stream all influence the risk associated with the investment.
- **Operating expense ratio:** Typically, a higher expense to gross income ratio, reflects a higher capitalization rate.
- **Potential growth in net operating income:**
- **Reserve/allowance:** Reserve allowance are not typically included as an operating expense by buyers, sellers, or brokers for most property types. However, at the clients request, I have reflected these rates both with and without reserve allowances as an expense item for retail an industrial property types.
- **Remaining economic life:** Real property is a depreciating asset and as properties age, they experience class or quality transition, their remaining economic life shortens and the capitalization rates generally increase.

## DIRECT CAPITALIZATION STRENGTHS AND WEAKNESSES

An overall capitalization rate is applied to the net operating income through the process called direct capitalization. The capitalization rate is typically applied to a stabilized or typical net operating income for a single year. There are certain strengths and weakness in utilizing an overall capitalization rate in property valuation. The strengths are:

- Satisfies all of the investors' return requirements; the return on and of the investment.
- Reliable for income streams without variable income growth rates.
- Simple, easy to understand and apply and widely used.

There are also certain weaknesses that need to be understood regarding the application of an overall capitalization using direct capitalization. The weaknesses are:

- Difficult to apply to an un-stabilized income stream; this could be caused by higher than normal market vacancy, or significant spikes in market rental rates.
- Difficult to apply to single or multi-tenant properties with long-term leases that have substantial near term risk of roll-over of tenants.
- There is inconsistency of application regarding the calculation of net operating income and reserve allowances.
- In the current real estate market there is some level of uncertainty and agreement as to acceptable capitalization rates of return and deal pricing among market participants.

## PROPERTY CLASS TRANSITION

Over time, properties tend to transition between quality classes. A new property rated as class A grade at its completion may transition to a class B after a period of time depending on market conditions. Similarly, a class B property that receives significant capital infusion may be upgraded to a class A rating. The determination of property class or quality is based upon the analysis of several factors including location, size, age, quality and condition, occupancy, tenancy, and rent levels. To an extent, these factors are controlled through asset management, maintenance, and capital expenditures. However, external factors such as new supply, changing economic conditions, design, and amenities can cause a property to transition between classes. It is therefore necessary to review property class ratings periodically to insure that each property is classified correctly.

The property classifications are identified in the individual property type discussions to follow. The purpose of this study is to develop estimated capitalization rates for each class of property type: apartment/multifamily, office, retail, and industrial. The classes of property are commonly referred to as being, A, B, or C class property. Douglas County requested rates on D class property as well. Surveys analyzed and investors contacted do not involve themselves with this quality of asset and capitalization rates for low-end property are based on market transactions and the appraiser's judgment.

Finally, it is important to note that this assignment did not allow the appraiser to inspect any of the properties that were selected as market transactions. The conclusion, as to class of property is subjective and based on the age of the improvements, photographs of the property (if available), and discussion with the verifying source.

## CAPITALIZATION RATE SPREADS

It was possible to analyze a sufficient number of sales for each general property type from available market data in Douglas County. The sales I researched provided a wide range in capitalization rates. Since the available database from the Douglas County real estate market is limited and imperfect. The capitalization rates derived were limited to a certain extent for C class properties, and especially for D class properties. I have also analyzed the potential spread between property classes by employing separate techniques. The alternative techniques are:

- Investor surveys reflecting A and B class properties.
- Yield spreads between 10-year corporate bonds and 10-year Treasury Bills. The spread is the risk premium associated with various investment grades above a "safe investment".
- The analysis of capitalization rates of over 600 sales, ranging from 2002 through 2009 in Douglas County of various types of properties.
- The Korpacz Survey data of Institutional vs. Non-Institutional grade capitalization rates which are generally A or B vs. C class and lower.

## SUMMARY

In the final analysis, the data analyzed indicates a spread of 250 to 400 basis points to be a reasonable range from the risk difference between Class A and Class D real estate investments. The risk of owning real estate is generally regarded as higher than the risk of owning a corporate bond for liquidity and marketability reasons. Therefore, my analysis using a basis point spread begins with the overall capitalization rate that is determined appropriate for Class A property and adds a premium for perceived additional risk by property class.

## FUTURE OUTLOOK

Omaha and Douglas County offers several strengths as a business location. Omaha has an excellent transportation system, including highways, airport, railroad, and river. The local economy is diverse and the cost of doing business is moderate, including real estate rates relative to other medium size metropolitan areas, and a relatively low tax burden. Consumers are also impacted by the challenging housing market, although less than other areas in the United States. The current economy and related problems will impede economic growth in the near future.

## DOUGLAS COUNTY APARTMENT/MULTIFAMILY MARKET

| DOUGLAS COUNTY METRO DATA-APARTMENT/MULTIFAMILY PROPERTIES | | | | | |
|---|---|---|---|---|---|
| **Year** | **Qtr** | **Inventory/SF/Units** | **Completions** | **Inventory Growth** | **Vacant Stock** |
| 2008 | 1 | 37,672 | 302 | 0.8% | 2,189 |
| | 2 | 37,672 | 0 | 0.0% | 2,150 |
| | 3 | 37,762 | 0 | 0.0% | 1,924 |
| | 4 | 37,762 | 0 | 0.0% | 2,138 |
| 2008 | All | 37,762 | 302 | 0.8% | 2,138 |
| 2009 | 1 | 37,762 | 0 | 0.0% | 2,277 |
| | 2 | 38,170 | 498 | 1.3% | 2,422 |
| | 3 | 38,470 | 300 | 0.8% | 2,863 |
| | 4 | 38,470 | 84 | 0.2% | 2,637 |
| 2009 | All | 38,554 | 882 | 2.3% | 2,637 |

| Year | Qtr | Vacancy Rate | Vacancy Change (BP) | Occupied Stock | Net Absorption |
|---|---|---|---|---|---|
| 2008 | 1 | 5.8% | 20 | 35,483 | 219 |
| | 2 | 5.7% | -10 | 35,522 | 39 |
| | 3 | 5.1% | -60 | 35,748 | 226 |
| | 4 | 5.7% | 60 | 35,534 | -214 |
| 2008 | All | 5.7% | 10 | 35,534 | 270 |
| 2009 | 1 | 6.0% | 30 | 35,395 | -139 |
| | 2 | 6.3% | 30 | 35,748 | 353 |
| | 3 | 7.4% | 110 | 35,607 | -141 |
| | 4 | 6.8% | -60 | 35,917 | 310 |
| 2009 | All | 6.8% | 110 | 35,917 | 383 |

## APARTMENT/MULTIFAMILY CAPITALIZATION RATES, NATIONAL

### REAL ESTATE RESEARCH CORPORATION, MIDWEST INVESTMENT CRITERIA – SUMMER 2009

| APARTMENT/MULTIFAMILY | | | |
|---|---|---|---|
| | **First-Tier Properties** | **Second-Tier Properties** | **Third-Tier Properties** |
| **PRE-TAX YIELD (IRR) (%)** | | | |
| RANGE | 7.0 – 11.0 | 8.0 – 14.0 | 8.5 -15.0 |
| MEAN | 9.2 | 10.2 | 11.2 |
| **GOING-IN CAP RATE (%)** | | | |
| RANGE | 5.5 – 9.0 | 6.5 – 10.0 | 6.5 – 11.0 |
| MEAN | 7.1 | 8.6 | 9.1 |
| **TERMINAL CAP RATE (%)** | | | |
| RANGE | 6.0 – 10.0 | 7.8 – 10.5 | 8.0 - 12.0 |
| MEAN | 7.8 | 9.0 | 9.8 |

**REAL ESTATE RESEARCH CORPORATION, OMAHA – SUMMER 2009**

| | RERC ESTIMATE | MIDWEST | U.S. |
|---|---|---|---|
| GOING-IN CAP RATE (%) | 8.1% | 7.6% | 7.6% |
| TERMINAL CAP RATE (%) | 8.6% | 8.3% | 8.3% |

**KORPACZ/PRICEWATERHOUSECOOPERS, LLP, 4th Quarter 2009**

| KEY INDICATORS | CURRENT QUARTER | LAST QUARTER | ONE YEAR AGO |
|---|---|---|---|
| **DISCOUNT RATE (IRR)** | | | |
| RANGE | 6.50%-14.00% | 7.50%-14.00% | 6.00%-10.50% |
| MEAN | 10.17% | 10.06% | 8.32% |
| CHANGE (Basis Points) | | +11 | +185 |
| | | | |
| **OVERALL RATE (OAR)** | 5.75%-11.00% | 5.75%-10.00% | 3.80%-8.50% |
| RANGE | 8.03% | 7.84% | 6.13% |
| MEAN | | +19 | +190 |
| CHANGE (Basis Points) | | | |
| | | | |
| **RESIDUAL CAP RATE** | | | |
| RANGE | 5.75%-10.75% | 5.75%-9.75% | 5.00%-9.25% |
| MEAN | 8.19% | 8.06% | 6.88% |
| CHANGE (Basis Points) | | +13 | +131 |

**RealtyRates.com Investor Survey**

| | **4th Quarter 2009** | **MINIMUM** | **MAXIMUM** | **MEAN** |
|---|---|---|---|---|
| ALL TYPES | | | | |
| | DEBT COVERAGE RATIO | 4.87% | 12.25% | 8.16% |
| | BAND OF INVESTMENT | 5.44% | 14.53% | 8.91% |
| | INVESTOR SURVEY | 5.16% | 13.80% | 9.44% |
| GARDEN/SUBURBAN | | | | |
| | DEBT COVERAGE RATIO | 4.87% | 11.97% | 7.89% |
| | BAND OF INVESTMENT | 5.44% | 13.16% | 8.47% |
| | INVESTOR SURVEY | 5.16% | 12.51% | 8.70% |
| HI-RISE TOWNHOUSE | | | | |
| | DEBT COVERAGE RATIO | 5.85% | 12.25% | 9.66% |
| | BAND OF INVESTMENT | 6.33% | 14.53% | 9.65% |
| | INVESTOR SURVEY | 6.02% | 13.80% | 9.65% |

**APARTMENT/MULTIFAMILY CLASSIFICATIONS** The following definitions are used to describe apartment/multifamily classifications as interpreted with this report as Class A, B, C, and D.

Apartment Complex: A type of commercial building used exclusively or primarily for office use (business), as opposed to manufacturing, warehousing, or other uses.

**CLASS A** has an excellent location and appearance with abundance of amenities. The building has superior architectural design, finish, and ornamentation. Common characteristics may include new construction, luxury clubhouse, fully equipped fitness center, garages, controlled access, intrusion alarm, washer and dryer in each unit, fireplace, racquetball court, tennis court, pools, spa, sauna, oversized tub, vaulted ceiling, and premium view.

**CLASS B** has a desirable location and appearance with ample amenities. The building has above mean construction and finish with some detail. Common characteristics may include slightly older construction, clubhouse, fitness center, controlled access, intrusion alarm, washer and dryer connection in each unit, fireplace, tennis court, and pool.

**CLASS C** has an average location and appearance with standard amenities, construction, and finish with a lack of ornamentation. Common characteristics may include slightly older construction, an adequate clubhouse, fitness center, laundry center, and pool.

**CLASS D** has a less desirable location and appearance with minimum amenities. The building has simple construction and finish and generally in need of repairs. Common characteristics may include older construction, minimum clubhouse, and laundry room.

**APARTMENT/MULTIFAMILY OVERVIEW** The large amount of negative net absorption in 2009 is indicative of weakness continuing to pervade multifamily properties across the nation. Nationally, the apartment market gave up nearly 32,000 units and pushed the national vacancy rate to over 7.5%. For perspective, this is the largest amount of negative net absorption since the first quarter of 2002.

Asking and effective rents continued their precipitous decline, with negative effective growth passing asking negative rent growth as landlords offer more concessions in an attempt to stop further deterioration in occupancy levels. This is significant: a decline in asking rents implies that landlord's are lowering offering price even before meeting with tenants for negotiations about further concessions, and is indicative of the increased pressure apartment properties face to maintain occupancy levels in the continuing economic downturn.

New buildings coming online in 2010 will face higher initial vacancy levels, and will work to increase the pressure on leasing managers of existing properties to support current rent and occupancy levels. Without an indication of a more severe cutback in supply coming online in 2010, signs point to more difficulty for rental apartment/multifamily for the rest of the year unless economic conditions improve drastically. Large declines in both asking and effective rents may serve to hold off faster deterioration in occupancy.

## APARTMENT/MULTIFAMILY MARKET

**SALES** Kenneth Voss & Associates, LLC examined 36 apartment sales in the Douglas County area. Twenty-six apartment sales were used in the final analysis. Eight of these properties were classified as Class A, six as Class B, five as Class C, and seven were classified as Class D.

### SUMMARY OF APARTMENT/MULTIFAMILY SALES

| Sale # | Class | Sale Date | YOC | City | SP/Unit | Ro | | |
|---|---|---|---|---|---|---|---|---|
| 1 | A | July 2008 | 1998 | Omaha | $80,414 | 6.25% | Min | 5.80% |
| 2 | A | December 2007 | 1992 | Omaha | $48,958 | 6.59% | Max | 6.73% |
| 3 | A | December 2007 | 1997 | Omaha | $71,970 | 6.73% | Med | 6.19% |
| 4 | A | August 2007 | 1999 | Omaha | $78,788 | 6.38% | Mean | 6.25% |
| 5 | A | August 2007 | 2006 | Omaha | $85,833 | 6.12% | | |
| 6 | A | July 2008 | 1920(R) | Omaha | $112,782 | 6.00% | | |
| 7 | A | May 2006 | 1964 | Omaha | $95,500 | 5.80% | | |
| 8 | A | March 2007 | 1910(R) | Omaha | $69,129 | 6.10% | | |
| | | | | | | | | |
| 9 | B | December 2007 | 1914(R) | Omaha | $101,014 | 7.05% | Min | 7.05% |
| 10 | B | March 2007 | 1910(R) | Omaha | $69,129 | 7.29% | Max | 8.75% |
| 11 | B | August 2005 | 1976 | Omaha | $50,000 | 8.75% | Med | 7.80% |
| 12 | B | June 2005 | 1993 | Omaha | $56,974 | 7.54% | Mean | 7.83% |
| 13 | B | March 2005 | 1973 | Omaha | $49,811 | 8.32% | | |
| 14 | B | July 2004 | 1973 | Omaha | $43,056 | 8.05% | | |
| | | | | | | | | |
| 15 | C | October 2007 | 1972 | Omaha | $37,313 | 8.96% | Min | 8.56% |
| 16 | C | January 2007 | 1965 | Omaha | $37,097 | 9.24% | Max | 9.46% |
| 17 | C | October 2006 | 1967 | Omaha | $30,313 | 8.82% | Med | 8.96% |
| 18 | C | September 2006 | 1919(R) | Omaha | $21,250 | 8.56% | Mean | 9.08% |
| 19 | C | July 2005 | 1921 | Omaha | $21,364 | 9.46% | | |
| | | | | | | | | |
| 20 | D | July 2002 | 1971 | Omaha | $33,167 | 10.64% | Min | 10.17% |
| 21 | D | September 2002 | 1974 | Omaha | $39,394 | 10.17% | Max | 11.64% |
| 22 | D | February 2003 | 1913 | Omaha | $13,036 | 10.43% | Med | 10.44% |
| 23 | D | December 2003 | 1913 | Omaha | $19,683 | 10.44% | Mean | 10.74% |
| 24 | D | December 2003 | 1916 | Omaha | $15,600 | 11.64% | | |
| 25 | D | July 2005 | 1910 | Omaha | $15,000 | 11.60% | | |
| 26 | D | January 2006 | 1916 | Omaha | $21,250 | 10.24% | | |

## APARTMENT/MULTIFAMILY OVERALL CAPITALIZATION RATES

The capitalization rates for Class A sales range from 5.80% to 6.73%. The median capitalization rate for Class A sales was 6.19% while the mean was 6.25%. The capitalization rates for Class B sales ranged from 7.05% to 8.75%. The median capitalization rate for Class B sales was 7.80% while the mean was 7.83%. The capitalization rates for Class C sales ranged from 8.56% to 9.46%. The median capitalization rate was 8.96% and the mean was 9.08%. The capitalization rates for Class D sales ranged from 10.17% to 11.64%. The median capitalization rate was 10.44% and the mean was 10.74%. Please note that the number of market transactions decreased late 2008 and through 2009, the date of this report. I decided to analyze older sales because of the data obtained during the verification process. I adjusted the final rates based on my knowledge of the current real estate market. Below is my recommended Overall Capitalization Rates for Apartment properties.

| APARTMENT/MULTIFAMILY CAPITALIZATION RATE | | | | |
|---|---|---|---|---|
| **APARTMENT/MULTIFAMILY** | **CLASS A** | **CLASS B** | **CLASS C** | **CLASS D** |
| **ALL PROPERTIES** | **7.00%** | **8.25%** | **9.50%** | **11.00%** |

## DOUGLAS COUNTY OFFICE MARKET

| DOUGLAS COUNTY METRO DATA-OFFICE | | | | | |
|---|---|---|---|---|---|
| **Year** | **Qtr** | **Inventory/SF** | **Completions** | **Inventory Growth** | **Vacant Stock** |
| 2008 | 1 | 17,570,000 | 0 | 0.0% | 2,315,000 |
| | 2 | 17,570,000 | 0 | 0.0% | 2,249,000 |
| | 3 | 17,447,000 | 61,000 | -0.7% | 2,411,000 |
| | 4 | 17,273,000 | 16,000 | -1.0% | 2,413,000 |
| 2008 | All | 17,273,000 | 77,000 | -1.7% | 2,413,000 |
| 2009 | 1 | 17,112,000 | 0 | -0.9% | 2,379,000 |
| | 2 | 17,484,000 | 411,000 | 2.2% | 2,774,000 |
| | 3 | 17,450,000 | 33,000 | -0.2% | 2,940,000 |
| | 4 | 17,383,000 | 0 | -0.4% | 2,988,000 |
| 2009 | All | 17,383,000 | 444,000 | 0.6% | 2,980,000 |

| Year | Qtr | Vacancy Rate | Vacancy Change (BP) | Occupied Stock | Net Absorption |
|---|---|---|---|---|---|
| 2008 | 1 | 13.2% | -110 | 15,255,000 | 206,000 |
| | 2 | 12.8% | -40 | 15,321,000 | 66,000 |
| | 3 | 13.8% | 100 | 15,036,000 | -285,000 |
| | 4 | 14.0% | 20 | 14,860,000 | -176,000 |
| 2008 | All | 14.0% | -30 | 14,860,000 | -189,000 |
| 2009 | 1 | 13.9% | -10 | 14,733,000 | -127,000 |
| | 2 | 15.9% | 200 | 14,710,000 | -23,000 |
| | 3 | 16.8% | 90 | 14,510,000 | -200,000 |
| | 4 | 17.2% | 40 | 14,395,000 | -115,000 |
| 2009 | All | 17.2% | 320 | 14,395,000 | -465,000 |

## OFFICE CAPITALIZATION RATES, NATIONAL

### REAL ESTATE RESEARCH CORPORATION, MIDWEST INVESTMENT CRITERIA – SUMMER 2009

| OFFICE-CBD | | | |
|---|---|---|---|
| | **First-Tier Properties** | **Second-Tier Properties** | **Third-Tier Properties** |
| **PRE-TAX YIELD (IRR) (%)** | | | |
| RANGE | 8.6 – 13.0 | 9.0 – 14.0 | 9.0 -15.0 |
| MEAN | 10.2 | 11.1 | 11.7 |
| **GOING-IN CAP RATE (%)** | | | |
| RANGE | 7.0 –10.0 | 7.5 – 11.0 | 8.0 – 12.0 |
| MEAN | 8.3 | 9.2 | 10.0 |
| **TERMINAL CAP RATE (%)** | | | |
| RANGE | 8.0 – 10.5 | 8.0 – 11.0 | 8.5 - 12.0 |
| MEAN | 8.9 | 9.7 | 10.7 |

| OFFICE-SUBURBAN | | | |
|---|---|---|---|
| | **First-Tier Properties** | **Second-Tier Properties** | **Third-Tier Properties** |
| **PRE-TAX YIELD (IRR) (%)** | | | |
| RANGE | 8.5 – 13.0 | 9.0 – 15.0 | 9.5 -15.0 |
| MEAN | 10.7 | 12.0 | 11.9 |
| **GOING-IN CAP RATE (%)** | | | |
| RANGE | 7.5 – 10.0 | 8.0 – 10.5 | 8.3 – 12.0 |
| MEAN | 8.6 | 9.5 | 10.0 |
| **TERMINAL CAP RATE (%)** | | | |
| RANGE | 8.0 – 12.0 | 8.5 – 12.0 | 8.8 - 14.0 |
| MEAN | 9.3 | 10.1 | 10.9 |

**REAL ESTATE RESEARCH CORPORATION, OMAHA – SUMMER 2009**

| CBD | RERC ESTIMATE | MIDWEST | U.S. |
|---|---|---|---|
| GOING-IN CAP RATE (%) | 9.2% | 8.3% | 8.1% |
| TERMINAL CAP RATE (%) | 9.8% | 8.9% | 8.8% |

| SUBURBAN | RERC ESTIMATE | MIDWEST | U.S. |
|---|---|---|---|
| GOING-IN CAP RATE (%) | 9.7% | 8.6% | 8.4% |
| TERMINAL CAP RATE (%) | 10.3% | 9.3% | 9.1% |

**KORPACZ/PRICEWATERHOUSECOOPERS, LLP, 4th Quarter 2009**

| **CBD** | | | |
|---|---|---|---|
| **KEY INDICATORS** | **CURRENT QUARTER** | **LAST QUARTER** | **ONE YEAR AGO** |
| **DISCOUNT RATE (IRR)** | | | |
| RANGE | 6.75%-14.00% | 7.50%-13.00% | 6.25%-12.00% |
| MEAN | 9.39% | 9.24% | 8.52% |
| CHANGE (Basis Points) | | +15 | +87 |
| | | | |
| **OVERALL RATE (OAR)** | | | |
| RANGE | 5.60%-11.00% | 5.00%-11.00% | 4.50%-10.00% |
| MEAN | 8.24% | 8.11% | 7.14% |
| CHANGE (Basis Points) | | +13 | +110 |
| | | | |
| **RESIDUAL CAP RATE** | | | |
| RANGE | 6.50%-11.00% | 6.50%-11.00% | 6.25%-10.00% |
| MEAN | 8.44% | 8.44% | 7.80% |
| CHANGE (Basis Points) | | 0 | +64 |

**KORPACZ/PRICEWATERHOUSECOOPERS, LLP, 4th Quarter 2009**

| SUBURBAN | | | |
|---|---|---|---|
| **KEY INDICATORS** | **CURRENT QUARTER** | **LAST QUARTER** | **ONE YEAR AGO** |
| **DISCOUNT RATE (IRR)** | | | |
| RANGE | 7.25%-14.00% | 8.00%-14.00% | 7.00%-12.50% |
| MEAN | 10.02% | 10.24% | 9.12% |
| CHANGE (Basis Points) | | -22 | +90 |
| | | | |
| **OVERALL RATE (OAR)** | | | |
| RANGE | 6.75%-12.00% | 7.00%-12.00% | 5.50%-11.00% |
| MEAN | 8.75% | 8.72% | 7.59% |
| CHANGE (Basis Points) | | +3 | +116 |
| | | | |
| **RESIDUAL CAP RATE** | | | |
| RANGE | 7.00%-11.50% | 7.50%-11.50% | 6.50%-11.50% |
| MEAN | 8.76% | 8.85% | 8.09% |
| CHANGE (Basis Points) | | -9 | +67 |

**RealtyRates.com Investor Survey**

| | **4th Quarter 2009** | **MINIMUM** | **MAXIMUM** | **MEAN** |
|---|---|---|---|---|
| ALL TYPES | | | | |
| | DEBT COVERAGE RATIO | 4.85% | 12.88% | 8.49% |
| | BAND OF INVESTMENT | 6.24% | 14.11% | 9.26% |
| | INVESTOR SURVEY | 5.93% | 13.40% | 10.08% |
| CBD | | | | |
| | DEBT COVERAGE RATIO | 5.17% | 12.88% | 8.87% |
| | BAND OF INVESTMENT | 6.63% | 14.11% | 9.86% |
| | INVESTOR SURVEY | 6.30% | 13.40% | 10.17% |
| SUBURBAN | | | | |
| | DEBT COVERAGE RATIO | 4.85% | 9.72% | 8.14% |
| | BAND OF INVESTMENT | 6.24% | 13.60% | 9.73% |
| | INVESTOR SURVEY | 5.93% | 12.92% | 9.20% |

**OFFICE CLASSIFICATIONS** The following definitions are used to describe office classifications as interpreted with this report as Class A, B, C, and D, or properties indicated as first, second or third tier office buildings.

**OFFICE BUILDING:** A type of commercial building used exclusively or primarily for office use (business), as opposed to manufacturing, warehousing, or other uses. Office buildings may sometimes have other associated uses within part of the building, i.e., retail, sales, financial, or restaurant, usually on the ground floor.

**CLASS A Multi-Story (First Tier):** A classification used to describe buildings that generally qualify as extremely desirable investment grade properties and command the highest rents or sale prices compared to other buildings in the same market. Such buildings are well located and provide efficient tenant layouts as well as high quality and in some buildings, one-of-a-kind floor plans. They can be an architectural or historical landmark designed by prominent architects. These buildings contain a modern mechanical system, and have above-mean maintenance and management as well as the best quality materials and workmanship in there trim and fittings. They are generally the most attractive and eagerly sought by investors willing to pay a premium for quality.

**CLASS B Multi-Story (Second Tier):** A classification used to describe buildings that generally qualify as a more speculative investment, and command lower rents or sale prices compared to other buildings in the same market. Such buildings offer utilitarian space without special attractions, and have ordinary design, if new or fairly new; good to excellent design if an older, non-landmark building. These buildings typically have mean to good maintenance, management, and tenants. They are less appealing to tenants in Class A properties, and may be deficient in a number of respects including floor plans, condition, and facilities. They lack prestige and must depend chiefly on a lower price to attract tenants and investors.

**CLASS C Multi-Story (Third Tier):** A classification used to describe buildings that generally qualify as no-frills, older buildings that offer basic space and command lower rents or sale prices compared to other buildings in the same market. Such buildings typically have below-mean maintenance and management, and could have mixed or low tenant prestige, inferior elevators, and/or mechanical/electric systems. These buildings lack prestige and must depend on a lower rent to attract tenants and investors.

**CLASS D Multi-Story:** A classification used to describe buildings that generally below mean and reaching the end of their economic life. These buildings with have lower rental rates and lower occupancy rates. Such buildings typically have lower quality construction and finish, often in need of extensive renovation. The buildings have below-mean maintenance and management, and could have mixed or low tenant prestige. Usually not in a prime location and generally a break-even basis; not income producing

**Class A One-Story Office** has excellent location, access, appearance, and construction. The building has superior architectural design and construction and is usually new or competitive with new buildings.

**Class B One-Story Office** class has a good location, access, appearance, and construction. Property may be slightly older than "A" properties.

**Class C One-Story Office** is an older building with a secondary location. Often these are single family dwellings have been converted for office use.

**Class D One-Story Office** is an older building often in need of renovation and/or repairs. These buildings are usually in the least desirable location.

## OFFICE OVERVIEW

Reflecting the rest of the nation, Douglas County experienced a declining office market in 2009. What initially was a deteriorating housing industry in the beginning, escalated into job losses in nearly all segments of the local economy, including the office market. Although other elements of the weakening economy contributed, job losses were the principal reason for the worsening office market. Given the economic development, it is unsurprising that there was a rise in vacancy for office buildings in 2009. Over 26 million square feet of negative absorption were recorded in 2009.

Asking rents and effective rents declined in 2009 and reflect a spike for concessions landlord's were willing to negotiate. Negative rent growth combined with a fall in occupancy represents strong downward pressure on net operating income, a trend that combined with difficulties in the credit markets are resulting in delinquencies and defaults.

Two Thousand Ten will be marked by continuing challenges with few new properties coming online competing with a difficult lease-up environment. Office vacancies will continue to rise given the typical lag in recovery.

The reported office vacancy in the Douglas County Metro Area was 17.2% at year-end 2009. However, other indices reported direct office vacancy rates of 15.0% to 17.5%, up from approximately 14.0% in 2008. Absorption of office space was negative, estimated at -465,000 square feet, as illustrated on the following tables.

## OFFICE MARKET

**SALES** Kenneth Voss & Associates, LLC examined 113 office sales in the Douglas County area. Fifty-one office sales were used in the final analysis. Nine of these properties were classified as Class A, fifteen as Class B, seventeen as Class C, and ten were classified as Class D.

## SUMMARY OF OFFICE SALES

| Sale # | Class | Sale Date | YOC | City | $SP/PSF | Ro | | |
|---|---|---|---|---|---|---|---|---|
| 201 | A | January 2009 | 1988 | Omaha | $ 136.79 | 6.81% | Min | 5.64% |
| 202 | A | May 2005 | 2001 | Omaha | $ 199.49 | 6.84% | Max | 8.20% |
| 203 | A | May 2006 | 1998 | Omaha | $ 185.63 | 7.31% | Med | 7.31% |
| 204 | A | January 2007 | 1995 | Omaha | $ 144.61 | 7.39% | Mean | 7.15% |
| 205 | A | February 2005 | 1994 | Omaha | $ 106.99 | 7.91% | | |
| 206 | A | February 2007 | 1995 | Omaha | $ 141.92 | 8.12% | | |
| 207 | A | August 2006 | 1986 | Omaha | $ 125.91 | 8.20% | | |
| 208 | A | May 2007 | 1980(R) | Omaha | $ 158.45 | 5.64% | | |
| 209 | A | December 2005 | 2005 | Omaha | $ 184.22 | 6.12% | | |
| | | | | | | | | |
| 210 | B | January 2009 | 1986 | Omaha | $ 125.43 | 7.43% | Min | 7.43% |
| 211 | B | April 2005 | 2001 | Omaha | $ 90.52 | 7.56% | Max | 9.95% |
| 212 | B | April 2004 | 2001 | Omaha | $ 148.80 | 7.71% | Med | 8.18% |
| 213 | B | May 2007 | 1980 | Omaha | $ 105.63 | 7.76% | Mean | 8.28% |
| 214 | B | June 2006 | 1970 | Omaha | $ 159.93 | 8.07% | | |
| 215 | B | January 2005 | 1993 | Omaha | $ 122.16 | 8.16% | | |
| 216 | B | December 2005 | 1997 | Omaha | $ 106.52 | 8.18% | | |
| 217 | B | November 2006 | 1980 | Omaha | $ 119.17 | 8.45% | | |
| 218 | B | June 2008 | 1996 | Omaha | $ 145.60 | 8.51% | | |
| 219 | B | December 2007 | 1997 | Omaha | $ 130.48 | 8.69% | | |
| 220 | B | September 2006 | 1964 | Omaha | $ 170.58 | 8.40% | | |
| 221 | B | September 2006 | 1984 | Omaha | $ 129.85 | 9.95% | | |
| 222 | B | August 2006 | 1987 | Omaha | $ 228.52 | 7.44% | | |
| 223 | B | November 2005 | 2002 | Omaha | $ 106.99 | 8.64% | | |
| 224 | B | May 2008 | 1985 | Omaha | $ 100.59 | 9.26% | | |
| | | | | | | | | |
| 225 | C | August 2004 | 1966 | Omaha | $ 75.00 | 8.57% | Min | 7.73% |
| 226 | C | May 2008 | 1983 | Omaha | $ 78.67 | 8.76% | Max | 9.26% |
| 227 | C | July 2004 | 1991 | Omaha | $ 89.62 | 8.82% | Med | 8.76% |
| 228 | C | November 2005 | 1999 | Omaha | $ 116.21 | 8.08% | Mean | 8.89% |
| 229 | C | January 2007 | 1976 | Omaha | $ 85.00 | 8.10% | | |
| 230 | C | April 2005 | 1975 | Omaha | $ 81.15 | 8.29% | | |
| 231 | C | August 2004 | 1983 | Omaha | $ 111.01 | 8.47% | | |
| 232 | C | June 2008 | 1996 | Omaha | $ 145.60 | 8.51% | | |
| 233 | C | December 2007 | 1997 | Omaha | $ 130.48 | 8.69% | | |
| 234 | C | September 2004 | 2002 | Omaha | $ 138.84 | 8.79% | | |
| 235 | C | August 2008 | 1970 | Omaha | $ 73.23 | 8.88% | | |
| 236 | C | January 2004 | 1984 | Omaha | $ 88.48 | 9.25% | | |
| 237 | C | September 2005 | 1970 | Omaha | $ 68.16 | 9.30% | | |
| 238 | C | August 2004 | 1977 | Omaha | $ 82.50 | 9.67% | | |
| 239 | C | January 2005 | 1986 | Omaha | $ 91.82 | 9.73% | | |
| 240 | C | June 2004 | 1994 | Omaha | $ 82.10 | 9.89% | | |
| 241 | C | May 2008 | 1985 | Omaha | $ 100.59 | 9.26% | | |

| Sale # | Class | Sale Date | YOC | City | $SP/PSF | Ro | | |
|---|---|---|---|---|---|---|---|---|
| 242 | D | March 2008 | 1957 | Omaha | $ 88.47 | 7.73% | Min | 7.73% |
| 243 | D | September 2005 | 1945 | Omaha | $ 92.89 | 7.82% | Max | 11.16% |
| 244 | D | November 2008 | 1966 | Omaha | $ 76.92 | 8.34% | Med | 8.61% |
| 245 | D | April 2005 | 1998 | Omaha | $ 110.01 | 8.35% | Mean | 8.88% |
| 246 | D | August 2006 | 1972 | Omaha | $ 53.05 | 8.46% | | |
| 247 | D | December 2006 | 1993 | Omaha | $ 149.71 | 8.75% | | |
| 248 | D | April 2005 | 2000 | Omaha | $ 104.88 | 8.75% | | |
| 249 | D | January 2006 | 1989 | Omaha | $ 80.59 | 9.45% | | |
| 250 | D | May 2004 | 1982 | Omaha | $ 100.86 | 9.97% | | |
| 251 | D | July 2006 | 1971 | Omaha | $ 46.11 | 11.16% | | |

## OFFICE OVERALL CAPITALIZATION RATES

The capitalization rates for Class A sales range from 5.64% to 8.20%. The median capitalization rate for Class A sales was 7.319% while the mean was 7.15%. The capitalization rates for Class B sales ranged from 7.43% to 9.75%. The median capitalization rate for Class B sales was 8.18% while the mean was 8.28%. The capitalization rates for Class C sales ranged from 8.57% to 9.26%. The median capitalization rate was 8.76% and the mean was 8.89%. The capitalization rates for Class D sales ranged from 7.73% to 11.16%. The median capitalization rate was 8.61% and the mean was 8.88%. Please note that the number of market transactions decreased in late 2008 and through 2009, the date of this report. I decided to analyze older sales because of the data obtained during the verification process. I adjusted the final rates based on my knowledge of the current real estate market. Below is my recommended Overall Capitalization Rates for Office properties.

| OFFICE CAPITALIZATION RATE | | | | |
|---|---|---|---|---|
| **OFFICE** | **CLASS A** | **CLASS B** | **CLASS C** | **CLASS D** |
| **ALL PROPERTIES** | **7.75%** | **8.50%** | **9.25%** | **10.25%** |

## DOUGLAS COUNTY RETAIL MARKET

| DOUGLAS COUNTY METRO DATA-NEIGHBRHOOD & COMMUNITY SHOPPING CENTERS | | | | | |
|---|---|---|---|---|---|
| **Year** | **Qtr** | **Inventory/SF** | **Completions** | **Inventory Growth** | **Vacant Stock** |
| 2008 | 1 | 13,760,000 | 37,000 | 0.3% | 1,220,000 |
| | 2 | 13,782,000 | 22,000 | 0.2% | 1,248,000 |
| | 3 | 13,807,000 | 25,000 | 0.2% | 1,207,000 |
| | 4 | 13,905,000 | 98,000 | 0.7% | 1,276,000 |
| 2008 | All | 13,905,000 | 182,000 | 1.3% | 1,276,000 |
| 2009 | 1 | 13,905,000 | 0 | 0.0% | 1,302,000 |
| | 2 | 13,905,000 | 0 | 0.0% | 1,262,000 |
| | 3 | 13,923,000 | 18,000 | 0.1% | 1,255,000 |
| | 4 | 13,923,000 | 0 | -0.4% | 1,451,000 |
| 2009 | All | 13,923,000 | 18,000 | 0.1% | 1,451,000 |

| Year | Qtr | Vacancy Rate | Vacancy Change (BP) | Occupied Stock | Net Absorption |
|---|---|---|---|---|---|
| 2008 | 1 | 8.9% | 50 | 12,540,000 | -37,000 |
| | 2 | 9.1% | 20 | 12,534,000 | -6,000 |
| | 3 | 8.7% | -40 | 12,600,000 | 66,000 |
| | 4 | 9.2% | 50 | 12,629,000 | 29,000 |
| 2008 | All | 9.2% | 80 | 12,629,000 | 52,000 |
| 2009 | 1 | 9.4% | 20 | 12,603,000 | -26,000 |
| | 2 | 9.1% | -30 | 12,643,000 | 40,000 |
| | 3 | 9.0% | -10 | 12,668,000 | 25,000 |
| | 4 | 10.4% | 140 | 12,472,000 | -196,000 |
| 2009 | All | 10.4% | 120 | 12,472,000 | -157,000 |

## RETAIL CAPITALIZATION RATES, NATIONAL

### REAL ESTATE RESEARCH CORPORATION, MIDWEST INVESTMENT CRITERIA – SUMMER 2009

| RETAIL-REGIONAL MALL | | | |
|---|---|---|---|
| | **First-Tier Properties** | **Second-Tier Properties** | **Third-Tier Properties** |
| **PRE-TAX YIELD (IRR) (%)** | | | |
| RANGE | 8.0 – 12.0 | 9.0 – 14.0 | 9.0 -16.0 |
| MEAN | 9.8 | 10.8 | 12.0 |
| **GOING-IN CAP RATE (%)** | | | |
| RANGE | 5.0 –9.0 | 7.5 – 10.5 | 8.0 – 12.0 |
| MEAN | 8.1 | 9.1 | 10.1 |
| **TERMINAL CAP RATE (%)** | | | |
| RANGE | 7.7 – 10.0 | 8.0 – 12.0 | 8.3 - 15.0 |
| MEAN | 8.8 | 9.8 | 10.9 |

| RETAIL-POWER CENTER | | | |
|---|---|---|---|
| | **First-Tier Properties** | **Second-Tier Properties** | **Third-Tier Properties** |
| **PRE-TAX YIELD (IRR) (%)** | | | |
| RANGE | 8.0 – 12.0 | 9.0 – 14.0 | 10.0 -16.0 |
| MEAN | 9.8 | 10.7 | 12.1 |
| **GOING-IN CAP RATE (%)** | | | |
| RANGE | 6.5 – 9.0 | 6.5 – 10.0 | 8.5 – 12.0 |
| MEAN | 8.3 | 9.1 | 10.1 |
| **TERMINAL CAP RATE (%)** | | | |
| RANGE | 7.8 – 11.0 | 8.5 – 13.0 | 9.5 - 14.0 |
| MEAN | 9.1 | 9.8 | 10.9 |

| RETAIL-NEIGHBORHOOD & COMMUNITY CENTER | | | |
|---|---|---|---|
| | **First-Tier Properties** | **Second-Tier Properties** | **Third-Tier Properties** |
| **PRE-TAX YIELD (IRR) (%)** | | | |
| RANGE | 8.0 – 12.0 | 9.0 – 14.0 | 10.5 -15.0 |
| MEAN | 10.0 | 10.9 | 11.7 |
| **GOING-IN CAP RATE (%)** | | | |
| RANGE | 5.8 – 10.0 | 6.5 – 12.0 | 8.5 – 13.0 |
| MEAN | 8.5 | 9.4 | 10.1 |
| **TERMINAL CAP RATE (%)** | | | |
| RANGE | 6.0 – 11.0 | 8.0 – 12.5 | 9.3 - 14.0 |
| MEAN | 9.2 | 10.0 | 10.7 |

**REAL ESTATE RESEARCH CORPORATION, OMAHA – SUMMER 2009**

| REGIONAL MALL | RERC ESTIMATE | MIDWEST | U.S. |
|---|---|---|---|
| GOING-IN CAP RATE (%) | 9.0% | 8.1% | 8.1% |
| TERMINAL CAP RATE (%) | 9.7% | 8.8% | 8.9% |

| POWER CENTER | RERC ESTIMATE | MIDWEST | U.S. |
|---|---|---|---|
| GOING-IN CAP RATE (%) | 9.4% | 8.3% | 8.3% |
| TERMINAL CAP RATE (%) | 10.1% | 9.1% | 9.1% |

| NEIGHBORHOOD & COMMUNITY | RERC ESTIMATE | MIDWEST | U.S. |
|---|---|---|---|
| GOING-IN CAP RATE (%) | 9.5% | 8.5% | 8.4% |
| TERMINAL CAP RATE (%) | 10.1% | 9.2% | 9.1% |

**KORPACZ/PRICEWATERHOUSECOOPERS, LLP, 4th Quarter 2009**

| REGIONAL MALL | | | |
|---|---|---|---|
| **KEY INDICATORS** | **CURRENT QUARTER** | **LAST QUARTER** | **ONE YEAR AGO** |
| **DISCOUNT RATE (IRR)** | | | |
| RANGE | 7.00%-17.00% | 7.00%-15.00% | 7.00%-11.00% |
| MEAN | 10.36% | 10.43% | 9.02% |
| CHANGE (Basis Points) | | +20 | +161 |
| | | | |
| **OVERALL RATE (OAR)** | | | |
| RANGE | 5.00%-11.00% | 5.00%-11.00% | 5.00%-9.50% |
| MEAN | 8.06% | 7.98% | 6.96% |
| CHANGE (Basis Points) | | +8 | +110 |
| | | | |
| **RESIDUAL CAP RATE** | | | |
| RANGE | 6.25%-12.00% | 6.25%-12.00% | 6.00%-10.00% |
| MEAN | 8.84% | 8.64% | 7.53% |
| CHANGE (Basis Points) | | +20 | +131 |

**KORPACZ/PRICEWATERHOUSECOOPERS, LLP, 4th Quarter 2009**

| POWER CENTER | | | |
|---|---|---|---|
| **KEY INDICATORS** | **CURRENT QUARTER** | **LAST QUARTER** | **ONE YEAR AGO** |
| **DISCOUNT RATE (IRR)** | | | |
| RANGE | 7.50%-15.00% | 7.50%-15.00% | 7.00%-12.00% |
| MEAN | 10.08% | 9.92% | 8.95% |
| CHANGE (Basis Points) | | +16 | +113 |
| | | | |
| **OVERALL RATE (OAR)** | | | |
| RANGE | 7.50%-10.00% | 7.50%-10.00% | 6.00%-10.00% |
| MEAN | 8.60% | 8.63% | 7.57% |
| CHANGE (Basis Points) | | -3 | +103 |
| | | | |
| **RESIDUAL CAP RATE** | | | |
| RANGE | 7.50%-10.00% | 7.50%-10.50% | 6.75%-12.00% |
| MEAN | 8.68% | 8.88% | 8.20% |
| CHANGE (Basis Points) | | -20 | +48 |

**KORPACZ/PRICEWATERHOUSECOOPERS, LLP, 4th Quarter 2009**

| STRIP SHOPPING CENTER | | | |
|---|---|---|---|
| **KEY INDICATORS** | **CURRENT QUARTER** | **LAST QUARTER** | **ONE YEAR AGO** |
| **DISCOUNT RATE (IRR)** | | | |
| RANGE | 7.50%-12.00% | 7.75%-12.00% | 7.00%-10.00% |
| MEAN | 9.44% | 9.38% | 8.49% |
| CHANGE (Basis Points) | | +6 | +95 |
| | | | |
| **OVERALL RATE (OAR)** | | | |
| RANGE | 7.25%-11.00% | 7.50%-11.00% | 5.80%-9.00% |
| MEAN | 8.53% | 8.41% | 7.49% |
| CHANGE (Basis Points) | | +12 | +104 |
| | | | |
| **RESIDUAL CAP RATE** | | | |
| RANGE | 7.25%-11.00% | 7.25%-10.00% | 6.00%-10.50% |
| MEAN | 8.63% | 8.61% | 7.82% |
| CHANGE (Basis Points) | | +2 | +81 |

**RealtyRates.com Investor Survey**

| | **4th Quarter 2009** | **MINIMUM** | **MAXIMUM** | **MEAN** |
|---|---|---|---|---|
| ALL TYPES | | | | |
| | DEBT COVERAGE RATIO | 5.36% | 13.33% | 8.28% |
| | BAND OF INVESTMENT | 6.20% | 14.42% | 9.27% |
| | INVESTOR SURVEY | 5.89% | 13.70% | 9.98% |
| ANCHORED CENTERS | | | | |
| | DEBT COVERAGE RATIO | 5.36% | 13.17% | 8.89% |
| | BAND OF INVESTMENT | 6.20% | 13.10% | 9.09% |
| | INVESTOR SURVEY | 5.89% | 12.44% | 9.90% |
| UNANCHORED CENTERS | | | | |
| | DEBT COVERAGE RATIO | 6.13% | 13.33% | 9.60% |
| | BAND OF INVESTMENT | 6.98% | 14.42% | 10.22% |
| | INVESTOR SURVEY | 6.63% | 13.70% | 10.62% |
| FREE STANDING | | | | |
| | DEBT COVERAGE RATIO | 6.02% | 13.11% | 8.67% |
| | BAND OF INVESTMENT | 6.21% | 13.76% | 9.00% |
| | INVESTOR SURVEY | 6.26% | 13.07% | 10.26% |

**RETAIL CLASSIFICATIONS** The following definitions are used to describe apartment/multifamily classifications as interpreted with this report as Class A, B, C, and D.

**SUPER REGIONAL MALL** offers extensive variety in general merchandise, apparel, furniture, and home furnishings, as well as a variety of services and recreational facilities. It is built around three or more full-line department stores generally not less than 75,000 square feet each, although there are exceptions in small communities. The typical size of a super regional center is about 1,000,000 square feet of gross leasable area. In practice the size ranges from about 500,000 square feet to more than 1,500,000 square feet.

**REGIONAL MALL** provides general merchandise, apparel, furniture, and home furnishings in depth and variety, as well as a range of services and recreational facilities. It is built around two-full line department stores of generally not less than 50,000 square feet, although there are exceptions in small communities. The typical size is about 500,000 square feet of gross leasable area. In practice, it may range from 250,000 square feet to more than 900,000 square feet. The regional center provides services typical of a business district yet not as extensive as those of a super regional center.

**COMMUNITY CENTER** is any center larger than a neighborhood center but with neither a traditional department store nor the trade area of a regional shopping center. The typical size of a community center is about 180,000 square feet of gross leasable area, but in practice, may range from 100,000 to 500,000 square feet.

**NEIGHBORHOOD CENTER** provides for the sale of convenience goods and personal services for the day-to-day living needs of the immediate neighborhood. It is built around a supermarket as the principal tenant and typically contains a gross leasable area of 60,000 square feet. In practice, it may range in size from 30,000 to 100,000 square feet.

**POWER CENTER** contains at least four category-specific anchors of 20,000 or more square feet. These anchors typically emphasize hard goods, such as consumer electronics, sporting goods, office supplies, home furnishings, and personal computer hardware/software. Anchors in power centers typically occupy 85 percent or more of the total gross leasable area.

**CONVENIENCE CENTER** provides for the sale of personal services and convenience goods similar to those of a neighborhood center. It contains a minimum of three stores, with a total gross leasable area of 30,000 or less. Instead of being anchored by a supermarket, it is usually anchored by some other type of service such as a minimarket.

**Class A One-Story Retail** is a store with excellent location, access, appearance, and construction. These buildings are usually new or competitive with new buildings.

**Class B One-Story Retail** is a store with an average location, access, appearance, and construction. Finish typically has little ornamentation.

**Class C One-Story Retail** is a store with a less desirable location, access, appearance, and construction. Finish typically has a lack of ornamentation.

**Class D One-Story Retail** is a store in the least desirable location, access, appearance, and construction. These buildings are old and in need of repair.

Retail properties are generally classified by size of center, types of tenants, and trade area draw. I have considered freestanding single tenant retail, unanchored strip centers, and/or neighborhood centers anchored by grocery stores, and community centers, which are larger than neighborhood centers and have several anchor tenants, often including a large discount retailer. Retail properties are also classified on a scale of A to E, based on a variety of factors as indicated below.

**CLASS A**

Wealth distribution, specific location, visibility, and/or access greatly contribute to the potential success of the project when compared to others in the market area.

**CLASS B**

Wealth distribution, specific location, visibility, and/or access to the project are above mean and have a positive impact to the potential success of the project when compared to others in the market area.

**CLASS C**

Sub-neighborhood wealth, specific location, visibility, and/or access to the project are typical when compared to others in the market area.

**CLASS D**

Wealth distribution, specific location, visibility, and/or access are inferior to others in the market area

**RETAIL OVERVIEW** A spike in deterioration characterized the performance of neighborhood and community centers in 2009. Negative net absorption in 2009 represents the largest single-period figure in negative net absorption. Asking and effective rents also registered declines as landlords came under increasing pressure from tenants who were either downsizing or going out of business. The amount of concessions increased significantly, as effective rents decreased. Larger properties were not spared, as Mall vacancy increased to over 8.0%. Asking rents for regional malls also decreased. Unless conditions change, there will be a continued increase in vacancy, and negative asking and effective rent decreases in neighborhood and community centers through 2011.

The current weakness weighting down retail properties is the pullback in consumer spending and low level of consumer confidence. With continuing uncertainty in both stock of wealth and flow of future income, there appears to be little basis for optimism required to maintain or increase spending and therefore keep retail businesses afloat. With tenants downsizing in terms of their space or going out of business, the near-term future of retail space remains daunting.

**RETAIL MARKET**

**SALES** Kenneth Voss & Associates, LLC examined 216 retail sales in the Douglas County area. One hundred-seven retail sales were used in the final analysis. Fifteen of these properties were classified as Class A, twenty-eight as Class B, forty-five as Class C, and nineteen were classified as Class D.

**SUMMARY OF RETAIL SALES**

| Sale # | Class | Sale Date | YOC | City | $SP/PSF | Ro | | |
|---|---|---|---|---|---|---|---|---|
| 301 | A | February 2007 | 1989 | Omaha | $365.68 | 6.67% | Min | 6.67% |
| 302 | A | August 2008 | 2007 | Omaha | $232.09 | 6.74% | Max | 8.23% |
| 303 | A | February 2007 | 2004 | Omaha | $483.35 | 6.87% | Med | 7.15% |
| 304 | A | June 2007 | 2006 | Omaha | $223.53 | 6.93% | Mean | 7.25% |
| 305 | A | March 2004 | 2004 | Omaha | $345.21 | 6.99% | | |
| 306 | A | October 2005 | 2001 | Omaha | $231.59 | 7.00% | | |
| 307 | A | July 2007 | 1995 | Omaha | $117.26 | 7.15% | | |
| 308 | A | March 204 | 2004 | Omaha | $143.05 | 7.15% | | |
| 309 | A | September 2008 | 1999 | Omaha | $152.19 | 7.17% | | |
| 310 | A | April 2008 | 2005 | Omaha | $330.33 | 7.22% | | |
| 311 | A | November 2004 | 2001 | Omaha | $138.89 | 7.39% | | |
| 312 | A | October 2006 | 2004 | Omaha | $214.85 | 7.45% | | |
| 313 | A | February 2007 | 2003 | Omaha | $162.28 | 7.79% | | |
| 314 | A | May 2007 | 2000 | Omaha | $150.00 | 7.98% | | |
| 315 | A | May 2007 | 1999 | Omaha | $145.52 | 8.23% | | |
| | | | | | | | | |
| 316 | B | November 2007 | 1985 | Omaha | $124.83 | 7.14% | Min | 7.14% |
| 317 | B | February 2006 | 1976 | Omaha | $82.00 | 7.15% | Max | 9.25% |
| 318 | B | December 2006 | 1976 | Omaha | $124.81 | 7.30% | Med | 8.15% |
| 319 | B | March 206 | 1974 | Omaha | $98.48 | 7.48% | Mean | 8.48% |
| 320 | B | January 2006 | 1974 | Omaha | $93.80 | 7.60% | | |
| 321 | B | March 2007 | 1940 | Omaha | $40.71 | 7.69% | | |
| 322 | B | May 2007 | 2003 | Omaha | $108.16 | 7.74% | | |
| 323 | B | September 2006 | 1986 | Omaha | $126.92 | 7.83% | | |
| 324 | B | September 2007 | 1973 | Omaha | $43.15 | 7.87% | | |
| 325 | B | September 2004 | 1990 | Omaha | $75.32 | 7.90% | | |
| 326 | B | March 2008 | 1997 | Omaha | $124.50 | 7.98% | | |
| 327 | B | March 2009 | 1996 | Omaha | $65.23 | 8.07% | | |
| 328 | B | May 2009 | 1984 | Omaha | $155.73 | 8.11% | | |
| 329 | B | August 2007 | 1996 | Omaha | $133.28 | 8.15% | | |
| 330 | B | July 2009 | 1995 | Omaha | $132.79 | 8.19% | | |
| 331 | B | June 2009 | 2003 | Omaha | $64.06 | 8.22% | | |
| 332 | B | November 2005 | 1979 | Omaha | $77.29 | 8.34% | | |
| 333 | B | December 2005 | 1987 | Omaha | $63.84 | 8.52% | | |
| 334 | B | March 2008 | 1929 | Omaha | $125.39 | 8.53% | | |
| 335 | B | December 2005 | 1988 | Omaha | $125.00 | 8.56% | | |
| 336 | B | October 2007 | 1969 | Omaha | $74.24 | 8.60% | | |
| 337 | B | November 2008 | 1981 | Omaha | $37.81 | 8.86% | | |
| 338 | B | November 2004 | 2004 | Omaha | $144.63 | 8.86% | | |
| 339 | B | August 2008 | 1970 | Omaha | $73.23 | 8.88% | | |
| 340 | B | February 2007 | 1971 | Omaha | $76.94 | 9.00% | | |
| 341 | B | December 2008 | 1994 | Omaha | $128.19 | 9.25% | | |
| 342 | B | December 2008 | 1994 | Omaha | $128.19 | 9.25% | | |

| Sale # | Class | Sale Date | YOC | City | $SP/PSF | Ro |
|---|---|---|---|---|---|---|
| 343 | C | August 2006 | 1956 | Omaha | $85.00 | 7.15% |
| 344 | C | September 2005 | 1930 | Omaha | $58.75 | 7.20% |
| 345 | C | August 2005 | 1978 | Omaha | $57.44 | 7.36% |
| 346 | C | May 2008 | 1976 | Omaha | $122.67 | 7.43% |
| 347 | C | September 2005 | 1925 | Omaha | $39.62 | 7.60% |
| 348 | C | January 2005 | 1919 | Omaha | $63.89 | 8.03% |
| 349 | C | December 2006 | 1961 | Omaha | $25.00 | 8.10% |
| 350 | C | February 2005 | 1905 | Omaha | $88.07 | 8.10% |
| 351 | C | July 2005 | 1913 | Omaha | $138.33 | 8.15% |
| 352 | C | November 2006 | 1930 | Omaha | $70.18 | 8.30% |
| 353 | C | December 2006 | 1920 | Omaha | $123.37 | 8.32% |
| 354 | C | August 2004 | 1992 | Omaha | $55.00 | 8.39% |
| 355 | C | January 2006 | 1980 | Omaha | $115.37 | 8.41% |
| 356 | C | September 2005 | 1945 | Omaha | $92.89 | 8.47% |
| 357 | C | March 2007 | 1975 | Omaha | $65.35 | 8.51% |
| 358 | C | August 2007 | 1944 | Omaha | $54.35 | 8.54% |
| 359 | C | November 2005 | 1925 | Omaha | $106.99 | 8.64% |
| 360 | C | November 2004 | 1980 | Omaha | $120.07 | 8.69% |
| 361 | C | March 2005 | 1978 | Omaha | $69.99 | 8.70% |
| 362 | C | June 2004 | 1962 | Omaha | $43.73 | 8.73% |
| 363 | C | November 2005 | 1971 | Omaha | $66.38 | 8.91% |
| 364 | C | December 2006 | 1981 | Omaha | $36.74 | 8.91% |
| 365 | C | September 2007 | 1966 | Omaha | $62.93 | 8.93% |
| 366 | C | December 2008 | 1991 | Omaha | $69.23 | 8.95% |
| 367 | C | October 2004 | 1991 | Omaha | $108.61 | 9.06% |
| 368 | C | October 2008 | 1974 | Omaha | $57.62 | 9.06% |
| 369 | C | February 2006 | 1990 | Omaha | $109.58 | 9.13% |
| 370 | C | January 2006 | 1992 | Omaha | $70.00 | 9.16% |
| 371 | C | May 2009 | 1974 | Omaha | $34.69 | 9.17% |
| 372 | C | May 2004 | 1900 | Omaha | $60.44 | 9.21% |
| 373 | C | October 2007 | 1999 | Omaha | $58.98 | 9.23% |
| 374 | C | February 2008 | 1974 | Omaha | $52.93 | 9.23% |
| 375 | C | April 2006 | 1974 | Omaha | $94.23 | 9.23% |
| 376 | C | July 2004 | 1986 | Omaha | $86.70 | 9.51% |
| 377 | C | October 2005 | 1976 | Omaha | $80.91 | 9.61% |
| 378 | C | May 2008 | 1968 | Omaha | $128.19 | 9.69% |
| 379 | C | March 2004 | 1922 | Omaha | $87.95 | 9.72% |
| 380 | C | August 2004 | 1911 | Omaha | $42.14 | 9.72% |
| 381 | C | December 2007 | 1968 | Omaha | $40.87 | 9.79% |
| 382 | C | June 2004 | 1950 | Omaha | $47.26 | 9.85% |
| 383 | C | June 2006 | 1998 | Omaha | $130.56 | 9.93% |
| 384 | C | January 2005 | 1987 | Omaha | $46.15 | 10.05% |
| 385 | C | April 2008 | 1987 | Omaha | $51.19 | 10.22% |
| 386 | C | August 2008 | 1970 | Omaha | $128.19 | 10.35% |
| | | | | | | |

| | |
|---|---|
| Min | 7.15% |
| Max | 10.35% |
| Med | 8.92% |
| Mean | 8.85% |

| Sale # | Class | Sale Date | YOC | City | $SP/PSF | Ro | | |
|---|---|---|---|---|---|---|---|---|
| 387 | D | October 2007 | 1927 | Omaha | $66.56 | 8.70% | Min | 8.70% |
| 388 | D | October 2007 | 1971 | Omaha | $83.33 | 9.23% | Max | 14.10% |
| 389 | D | May 2005 | 1996 | Omaha | $55.23 | 9.87% | Med | 10.64% |
| 390 | D | January 2009 | 1930 | Omaha | $46.25 | 10.00% | Mean | 10.88% |
| 391 | D | June 2008 | 1971 | Omaha | $24.01 | 10.12% | | |
| 392 | D | January 2004 | 1974 | Omaha | $75.45 | 10.20% | | |
| 393 | D | December 2005 | 1986 | Omaha | $56.32 | 10.28% | | |
| 394 | D | March 2007 | 1938 | Omaha | $54.56 | 10.45% | | |
| 395 | D | July 2004 | 1985 | Omaha | $37.67 | 10.53% | | |
| 396 | D | September 2006 | 1964 | Omaha | $22.37 | 10.64% | | |
| 397 | D | October 2005 | 1957 | Omaha | $28.95 | 10.96% | | |
| 398 | D | July 2007 | 1957 | Omaha | $30.16 | 11.01% | | |
| 399 | D | February 2008 | 1915 | Omaha | $33.32 | 11.18% | | |
| 400 | D | August 2006 | 1880 | Omaha | $63.00 | 11.32% | | |
| 401 | D | March 2004 | 1922 | Omaha | $36.40 | 11.78% | | |
| 402 | D | November 2006 | 1948 | Omaha | $23.19 | 11.92% | | |
| 403 | D | July 2004 | 1937 | Omaha | $37.20 | 12.13% | | |
| 404 | D | June 2004 | 1977 | Omaha | $58.73 | 12.28% | | |
| 405 | D | March 2008 | 1950 | Omaha | $45.51 | 14.10% | | |

## RETAIL OVERALL CAPITALIZATION RATES

The capitalization rates for Class A sales ranged from 6.67% to 8.23%. The median capitalization rate for Class A sales was 7.15% while the mean was 7.25%. The capitalization rates for Class B sales ranged from 7.14% to 9.25%. The median capitalization rate for Class B sales was 8.15% while the mean was 8.48%. The capitalization rates for Class C sales ranged from 7.15% to 10.35%. The median capitalization rate was 8.92% and the mean was 8.85%. The capitalization rates for Class D sales ranged from 8.70% to 14.10%. The median capitalization rate was 10.64% and the mean was 10.88%. Please note that the number of market transactions decreased in late 2008 and through 2009, the date of this report. I decided to analyze older sales because of the data obtained during the verification process. I adjusted the final rates based on my knowledge of the current real estate market. Below is my recommended Overall Capitalization Rates for Retail properties.

| RETAIL CAPITALIZATION RATE | | | | |
|---|---|---|---|---|
| **RETAIL** | **CLASS A** | **CLASS B** | **CLASS C** | **CLASS D** |
| **ALL PROPERTIES** | **7.50%** | **8.50%** | **9.00%** | **10.75%** |

## INDUSTRIAL PROPERTIES

| DOUGLAS COUNTY METRO DATA-INDUSTRIAL | | | | | |
|---|---|---|---|---|---|
| **Year** | **Qtr** | **Inventory/SF** | **Vacant SF** | **Inventory Growth** | **Net Absorption** |
| 2008 | 1 | 33,339,980 | 1,593,870 | 4.8% | 371,862 |
| | 2 | 33,346,980 | 1,907,514 | 5.7% | -306,644 |
| | 3 | 33,242,780 | 1,704,767 | 5.1% | 98,547 |
| | 4 | 33,242,780 | 1,758,077 | 5.3% | -53,310 |
| 2009 | 1 | 33,242,780 | 1,820,072 | 5.5% | -61,995 |
| | 2 | 33,249,780 | 1,851,511 | 5.6% | -24,439 |
| | 3 | 33,249,780 | 1,884,275 | 5.7% | -32,764 |
| | 4 | 33,249,779 | 1,844,078 | 5.5% | 40,196 |
| 2009 | All | 33,271,400 | 1,888,398 | 5.7% | -44,320 |

| Year | Qtr | No. Buildings | Buildings Delivered | Area/SF Delivered | SF Under Const. |
|---|---|---|---|---|---|
| 2008 | 1 | 1,022 | 1 | 7,000 | 7,000 |
| | 2 | 1,023 | 0 | 0 | 0 |
| | 3 | 1,022 | 0 | 0 | 0 |
| | 4 | 1,022 | 0 | 0 | 7,000 |
| 2009 | 1 | 1,022 | 0 | 0 | 7,000 |
| | 2 | 1,023 | 1 | 7,000 | 0 |
| | 3 | 1,023 | 0 | 0 | 52,255 |
| | 4 | 1,022 | 0 | 0 | 52,255 |
| 2009 | All | 1,025 | 1 | 40,000 | 52,255 |

## INDUSTRIAL CAPITALIZATION RATES, NATIONAL

### REAL ESTATE RESEARCH CORPORATION, MIDWEST INVESTMENT CRITERIA – SUMMER 2009

| WAREHOUSE | | | |
|---|---|---|---|
| | **First-Tier Properties** | **Second-Tier Properties** | **Third-Tier Properties** |
| **PRE-TAX YIELD (IRR) (%)** | | | |
| RANGE | 8.0 – 13.0 | 8.8 – 15.0 | 9.0 -15.0 |
| MEAN | 9.7 | 10.5 | 11.2 |
| **GOING-IN CAP RATE (%)** | | | |
| RANGE | 7.0 –9.3 | 7.5 – 10.0 | 8.0 – 12.0 |
| MEAN | 8.4 | 9.0 | 9.7 |
| **TERMINAL CAP RATE (%)** | | | |
| RANGE | 7.5 – 10.0 | 8.0 – 11.0 | 8.5 - 13.0 |
| MEAN | 8.9 | 9.4 | 10.2 |

| R&D | | | |
|---|---|---|---|
| | **First-Tier Properties** | **Second-Tier Properties** | **Third-Tier Properties** |
| **PRE-TAX YIELD (IRR) (%)** | | | |
| RANGE | 8.0 – 13.0 | 9.0 – 14.0 | 9.0 -15.0 |
| MEAN | 9.9 | 10.7 | 11.6 |
| **GOING-IN CAP RATE (%)** | | | |
| RANGE | 7.0 – 9.5 | 7.0 – 10.5 | 8.0 – 11.5 |
| MEAN | 8.6 | 9.2 | 10.0 |
| **TERMINAL CAP RATE (%)** | | | |
| RANGE | 7.5 – 10.0 | 8.0 – 11.0 | 8.5 – 12.5 |
| MEAN | 9.1 | 9.7 | 10.5 |

| FLEX SPACE | | | |
|---|---|---|---|
| | **First-Tier Properties** | **Second-Tier Properties** | **Third-Tier Properties** |
| **PRE-TAX YIELD (IRR) (%)** | | | |
| RANGE | 8.0 – 14.5 | 9.0 – 14.0 | 9.0 -15.5 |
| MEAN | 10.0 | 10.6 | 11.6 |
| **GOING-IN CAP RATE (%)** | | | |
| RANGE | 7.0 – 9.5 | 7.0 – 10.5 | 8.0 – 11.5 |
| MEAN | 8.6 | 9.3 | 10.0 |
| **TERMINAL CAP RATE (%)** | | | |
| RANGE | 7.5 – 10.5 | 8.0 – 11.0 | 8.5 - 12.0 |
| MEAN | 9.2 | 9.8 | 10.5 |

**REAL ESTATE RESEARCH CORPORATION, OMAHA – SUMMER 2009**

| WAREHOUSE | RERC ESTIMATE | MIDWEST | U.S. |
|---|---|---|---|
| GOING-IN CAP RATE (%) | 9.4% | 8.4% | 8.1% |
| TERMINAL CAP RATE (%) | 9.9% | 8.9% | 8.8% |

| R&D | RERC ESTIMATE | MIDWEST | U.S. |
|---|---|---|---|
| GOING-IN CAP RATE (%) | 9.7% | 8.6% | 8.3% |
| TERMINAL CAP RATE (%) | 10.2% | 9.1% | 9.0% |

| FLEX SPACE | RERC ESTIMATE | MIDWEST | U.S. |
|---|---|---|---|
| GOING-IN CAP RATE (%) | 9.7% | 8.6% | 8.4% |
| TERMINAL CAP RATE (%) | 10.2% | 9.2% | 9.1% |

**KORPACZ/PRICEWATERHOUSECOOPERS, LLP, 4th Quarter 2009**

| WAREHOUSE | | | |
|---|---|---|---|
| **KEY INDICATORS** | **CURRENT QUARTER** | **LAST QUARTER** | **ONE YEAR AGO** |
| **DISCOUNT RATE (IRR)** | | | |
| RANGE | 7.50%-12.50% | 7.50%-12.50% | 6.00%-11.00% |
| MEAN | 9.74% | 9.35% | 8.19% |
| CHANGE (Basis Points) | | +39 | +155 |
| | | | |
| **OVERALL RATE (OAR)** | | | |
| RANGE | 6.50%-12.00% | 6.50%-12.00% | 5.00%-9.00% |
| MEAN | 8.80% | 8.46% | 6.73% |
| CHANGE (Basis Points) | | +34 | +207 |
| | | | |
| **RESIDUAL CAP RATE** | | | |
| RANGE | 6.50%-12.00% | 6.50%-11.00% | 5.50%-9.50% |
| MEAN | 8.73% | 8.53% | 7.26% |
| CHANGE (Basis Points) | | +20 | +147 |

**KORPACZ/PRICEWATERHOUSECOOPERS, LLP, 4th Quarter 2009**

| SR&D/FLEX SPACE | | | |
|---|---|---|---|
| **KEY INDICATORS** | **CURRENT QUARTER** | **LAST QUARTER** | **ONE YEAR AGO** |
| **DISCOUNT RATE (IRR)** | | | |
| RANGE | 8.00%-13.00% | 7.75%-13.00% | 6.75%-11.00% |
| MEAN | 10.27% | 9.84% | 8.85% |
| CHANGE (Basis Points) | | +43 | +142 |
| | | | |
| **OVERALL RATE (OAR)** | | | |
| RANGE | 7.50%-11.50% | 7.00%-11.50% | 5.50%-10.00% |
| MEAN | 9.14% | 8.77% | 7.76% |
| CHANGE (Basis Points) | | +37 | +138 |
| | | | |
| **RESIDUAL CAP RATE** | | | |
| RANGE | 7.50%-12.50% | 7.50%-12.50% | 7.00%-10.50% |
| MEAN | 9.20% | 9.11% | 8.24% |
| CHANGE (Basis Points) | | +9 | +96 |

**RealtyRateS.com Investor Survey**

| | 4th Quarter 2009 | MINIMUM | MAXIMUM | MEAN |
|---|---|---|---|---|
| ALL TYPES | | | | |
| | DEBT COVERAGE RATIO | 4.60% | 12.80% | 8.40% |
| | BAND OF INVESTMENT | 6.24% | 14.54% | 9.39% |
| | INVESTOR SURVEY | 5.93% | 13.82% | 10.27% |
| WAREHOUSE | | | | |
| | DEBT COVERAGE RATIO | 4.60% | 11.61% | 7.71% |
| | BAND OF INVESTMENT | 6.24% | 12.61% | 8.76% |
| | INVESTOR SURVEY | 5.93% | 11.98% | 8.93% |
| R&D/FLEX | | | | |
| | DEBT COVERAGE RATIO | 6.16% | 12.80% | 9.54% |
| | BAND OF INVESTMENT | 7.68% | 14.54% | 10.66% |
| | INVESTOR SURVEY | 7.30% | 13.82% | 10.62% |
| | | | | |

**INDUSTRIAL BUILDING** A type of building adapted for such uses as the assemblage, processing, and/or manufacturing of products from raw materials or fabricated parts. Additional uses include warehousing, distribution, and maintenance facilities. The primary purpose of the space is for storing, producing, assembling, or distributing product. The following definitions are used to describe industrial classifications as interpreted with this report as Class A, B, C, and D. Factors that aid in the classification of industrial properties are location, access, site, truck court configuration, ceiling height, column spacing, overall construction quality, and percentage and quality of office build out, among other factors.

The following definitions are used to describe industrial classifications as interpreted with this report as Class A, B, C, and D.

**Class A Light Manufacturing** Good percentage of office space and A/C interior finish. Good lighting and plumbing to accommodate higher personnel density. Usually used as manufacturing plant or possibly a mill. The improvement has above mean ceiling heights and design.

**Class B Light Manufacturing** The improvement has adequate office space and interior finish. These types of buildings are typically located in industrial parks. Design, workmanship, and fenestration are of good quality.

**Class C Light Manufacturing** The building has very little office space and interior finish. Usually no A/C and has mean ceiling heights. The building has mean design and workmanship. A typical use would be a cabinet shop.

**Class D Light Manufacturing** The building has no office space or interior finish. The building could be used for light manufacturing or storage warehouse depending on quality of lighting. Design and workmanship are below mean and height of building may limit the use of the building.

**Class A Warehouse** A good percentage of the building is office space. The building contains heavy roof structures to support Craneways and good wall structures. Typically these buildings have a wall height of 24-36 feet. The building has adequate fenestration and good exterior finish.

**Class B Warehouse** Distribution or storage warehouse with storage vaults and interior firewalls as well as some exterior firewalls. Structures are primarily designed for heavy floor use. Adequate interior and office finish.

**Class C Warehouse** Large open areas and some interior finish. This is typically a lighter structure than a good classed warehouse. The building contains small office space.

**Class D Warehouse** The building is a structure with large open areas and little finish. No fenestration or office space. These buildings typically have low ceiling heights. Normal use is for storage or service garage. The building is built to minimum building code standards.

**Class A Flex/Warehouse** The exterior of the building will tend to look like an office building. Large area devoted to office space. High intensity lighting, plumbing, good partitioning, and finish work.

**Class B Flex/Warehouse** Typical of industrial park development. The building can be divided for multiply tenancy with adequate display, office space storage and work areas.

**Class C Flex/Warehouse** Plain building with little trim and few interior subdivisions and finish. These buildings normally have adequate office reception areas with rear portions of building being warehouse space.

**Class D Flex/Warehouse** Very little, front office entry and finish. The building is normally subdivided into smaller spaces.

## INDUSTRIAL MARKET

**SALES** Kenneth Voss & Associates, LLC examined 216 industrial sales in the Douglas County area. One hundred-nine retail sales were used in the final analysis. Seven of these properties were classified as Class A, twenty-nine as Class B, forty-five as Class C, and twenty-eight were classified as Class D.

**SUMMARY OF INDUSTRIAL SALES**

| Sale # | Class | Sale Date | YOC | City | $SP/PSF | Ro | | |
|---|---|---|---|---|---|---|---|---|
| 501 | A | January 2008 | 2000 | Omaha | $105.34 | 6.37% | Min | 6.37% |
| 502 | A | November 2007 | 2007 | Omaha | $123.10 | 6.53% | Max | 8.87% |
| 503 | A | July 2009 | 2005 | Omaha | $74.79 | 7.04% | Med | 7.38% |
| 504 | A | March 2006 | 1991 | Omaha | $94.56 | 7.38% | Mean | 7.44% |
| 505 | A | April 2005 | 2001 | Omaha | $90.52 | 7.56% | | |
| 506 | A | April 2008 | 2005 | Omaha | $50.31 | 8.31% | | |
| 507 | A | March 2009 | 2005 | Omaha | $78.31 | 8.87% | | |
| | | | | | | | | |
| 508 | B | April 2005 | 1986 | Omaha | $34.29 | 6.74% | Min | 6.74% |
| 509 | B | May 2004 | 1986 | Omaha | $53.61 | 6,76% | Max | 8.78% |
| 510 | B | October 2005 | 1995 | Omaha | $80.83 | 6.82% | Med | 8.00% |
| 511 | B | March 2008 | 1994 | Omaha | $53.25 | 6.84% | Mean | 7.85% |
| 512 | B | February 2008 | 1999 | Omaha | $80.35 | 7.06% | | |
| 513 | B | October 2007 | 1979 | Omaha | $34.05 | 7.13% | | |
| 514 | B | May 2008 | 1972 | Omaha | $45.54 | 7.15% | | |
| 515 | B | June 2004 | 2001 | Omaha | $54.58 | 7.22% | | |
| 516 | B | July 2006 | 1970 | Omaha | $25.73 | 7.43% | | |
| 517 | B | June 2004 | 1995 | Omaha | $56.36 | 7.59% | | |
| 518 | B | March 2004 | 1990 | Omaha | $73.48 | 7.80% | | |
| 519 | B | June 2004 | 1987 | Omaha | $60.00 | 7.83% | | |
| 520 | B | October 2006 | 2000 | Omaha | $56.30 | 7.91% | | |
| 521 | B | July 2007 | 1964 | Omaha | $33.09 | 7.96% | | |
| 522 | B | October 2008 | 1970 | Omaha | $49.01 | 8.00% | | |
| 523 | B | April 2005 | 1999 | Omaha | $69.95 | 8.12% | | |
| 524 | B | November 2008 | 1992 | Omaha | $46.30 | 8.13% | | |
| 525 | B | November 2007 | 1996 | Omaha | $63.24 | 8.14% | | |
| 526 | B | May 2005 | 1995 | Omaha | $66.67 | 8.15% | | |
| 527 | B | April 2007 | 1994 | Omaha | $46.11 | 8.24% | | |
| 528 | B | July 2005 | 2002 | Omaha | $38.46 | 8.37% | | |
| 529 | B | July 2004 | 1989 | Omaha | $100.03 | 8.40% | | |
| 530 | B | November 2005 | 1996 | Omaha | $75.10 | 8.44% | | |
| 531 | B | June 2007 | 1999 | Omaha | $74.26 | 8.45% | | |
| 532 | B | July 2008 | 2004 | Omaha | $48.00 | 8.46% | | |
| 533 | B | May 2005 | 2002 | Omaha | $70.65 | 8.48% | | |
| 534 | B | July 2008 | 1977 | Omaha | $31.58 | 8.48% | | |
| 535 | B | February 2004 | 2001 | Omaha | $48.51 | 8.72% | | |
| 536 | B | February 2004 | 1991 | Omaha | $46.60 | 8.78% | | |

| Sale # | Class | Sale Date | YOC | City | $SP/PSF | Ro |
|---|---|---|---|---|---|---|
| 537 | C | May 2006 | 1968 | Omaha | $88.38 | 6.32% |
| 538 | C | May 2007 | 1986 | Omaha | $77.97 | 6.58% |
| 539 | C | April 2006 | 1980 | Omaha | $49.14 | 6.81% |
| 540 | C | July 2004 | 1977 | Omaha | $40.14 | 7.04% |
| 541 | C | June 2006 | 1979 | Omaha | $62.82 | 7.17% |
| 542 | C | May 2004 | 1988 | Omaha | $53.58 | 7.18% |
| 543 | C | January 2007 | 1971 | Omaha | $83.18 | 7.20% |
| 544 | C | January 2006 | 1966 | Omaha | $44.25 | 7.40% |
| 545 | C | September 2007 | 1973 | Omaha | $43.15 | 7.87% |
| 546 | C | February 2006 | 1973 | Omaha | $42.84 | 7.89% |
| 547 | C | February 2008 | 1972 | Omaha | $55.02 | 7.99% |
| 548 | C | April 2006 | 1976 | Omaha | $61.41 | 8.01% |
| 549 | C | February 2006 | 1985 | Omaha | $60.00 | 8.08% |
| 550 | C | December 2007 | 1954 | Omaha | $55.53 | 8.11% |
| 551 | C | December 2005 | 1987 | Omaha | $63.25 | 8.12% |
| 552 | C | July 2005 | 1975 | Omaha | $37.50 | 8.19% |
| 553 | C | July 2007 | 1996 | Omaha | $53.82 | 8.28% |
| 554 | C | November 2005 | 1980 | Omaha | $47.66 | 8.28% |
| 555 | C | June 2006 | 1979 | Omaha | $75.37 | 8.32% |
| 556 | C | October 2006 | 1968 | Omaha | $30.73 | 8.35% |
| 557 | C | September 2005 | 1990 | Omaha | $60.36 | 8.37% |
| 558 | C | May 2006 | 1978 | Omaha | $31.11 | 8.46% |
| 559 | C | April 2004 | 1969 | Omaha | $41.74 | 8.52% |
| 560 | C | June 2007 | 1977 | Omaha | $53.03 | 8.54% |
| 561 | C | March 2004 | 1967 | Omaha | $33.05 | 8.67% |
| 562 | C | October 2006 | 1966 | Omaha | $31.93 | 8.67% |
| 563 | C | June 2007 | 1977 | Omaha | $48.72 | 8.78% |
| 564 | C | June 2005 | 1989 | Omaha | $34.36 | 8.90% |
| 565 | C | April 2007 | 1996 | Omaha | $45.17 | 8.99% |
| 566 | C | April 2008 | 1978 | Omaha | $47.54 | 8.99% |
| 567 | C | January 2005 | 1991 | Omaha | $13.83 | 8.99% |
| 568 | C | March 2006 | 1986 | Omaha | $49.04 | 9.06% |
| 569 | C | June 2007 | 1952 | Omaha | $25.33 | 9.06% |
| 570 | C | June 2004 | 1993 | Omaha | $34.74 | 9.23% |
| 571 | C | February 2005 | 1974 | Omaha | $39.30 | 9.25% |
| 572 | C | January 2005 | 1973 | Omaha | $45.46 | 9.30% |
| 573 | C | December 2007 | 1994 | Omaha | $54.74 | 9.37% |
| 574 | C | June 2006 | 1999 | Omaha | $35.89 | 9.38% |
| 575 | C | February 2005 | 1989 | Omaha | $51.29 | 9.47% |
| 576 | C | March 2006 | 1995 | Omaha | $61.29 | 9.53% |
| 577 | C | July 2005 | 1978 | Omaha | $34.92 | 9.58% |
| 578 | C | June 2006 | 1977 | Omaha | $44.01 | 9.71% |
| 579 | C | April 2005 | 1982 | Omaha | $31.42 | 9.77% |
| 580 | C | November 2005 | 1967 | Omaha | $56.02 | 9.79% |
| 581 | C | January 2006 | 1989 | Omaha | $34.51 | 9.98% |

| | |
|---|---|
| Min | 6.32% |
| Max | 9.98% |
| Med | 8.52% |
| Mean | 8.48% |

| Sale # | Class | Sale Date | YOC | City | $SP/PSF | Ro |
|---|---|---|---|---|---|---|
| 582 | D | July 2004 | 1938 | Omaha | $31.03 | 8.45% |
| 583 | D | August 2007 | 1956 | Omaha | $55.44 | 8.48% |
| 584 | D | December 2005 | 1987 | Omaha | $63.84 | 8.52% |
| 585 | D | June 2007 | 1945 | Omaha | $29.57 | 9.01% |
| 596 | D | July 2006 | 1930 | Omaha | $37.50 | 9.02% |
| 587 | D | October 2005 | 1961 | Omaha | $27.06 | 9.19% |
| 589 | D | March 2007 | 1973 | Omaha | $34.04 | 9.31% |
| 590 | D | December 2006 | 1970 | Omaha | $40.78 | 9.53% |
| 591 | D | February 2007 | 1992 | Omaha | $55.56 | 9.56% |
| 592 | D | February 2006 | 1928 | Omaha | $24.08 | 9.56% |
| 593 | D | June 2007 | 1979 | Omaha | $45.00 | 9.60% |
| 594 | D | January 2008 | 1958 | Omaha | $25.76 | 9.76% |
| 595 | D | October 2005 | 1973 | Omaha | $29.60 | 9.95% |
| 596 | D | October 2004 | 1963 | Omaha | $42.44 | 9.96% |
| 597 | D | September 2006 | 1979 | Omaha | $43.03 | 9.99% |
| 498 | D | April 2006 | 1954 | Omaha | $34.77 | 10.02% |
| 499 | D | February 2006 | 1969 | Omaha | $30.24 | 10.15% |
| 600 | D | July 2004 | 1977 | Omaha | $34.26 | 10.15% |
| 601 | D | August 2007 | 1979 | Omaha | $31.85 | 10.20% |
| 602 | D | December 2004 | 1970 | Omaha | $28.01 | 10.28% |
| 603 | D | August 2006 | 1961 | Omaha | $18.11 | 10.57% |
| 604 | D | November 2004 | 1979 | Omaha | $25.13 | 10.66% |
| 605 | D | December 2006 | 1947 | Omaha | $43.66 | 10.79% |
| 606 | D | August 2004 | 1967 | Omaha | $50.60 | 10.82% |
| 607 | D | October 2005 | 1957 | Omaha | $28.95 | 10.96% |
| 608 | D | June 2007 | 1977 | Omaha | $24.49 | 11.68% |
| 609 | D | March 2005 | 1971 | Omaha | $26.13 | 12.53% |
| 610 | D | May 2004 | 1947 | Omaha | $12.34 | 12.95% |

| | |
|---|---|
| Min | 8.45% |
| Max | 12.95% |
| Med | 9.98% |
| Mean | 10.06% |

## INDUSTRIAL OVERALL CAPITALIZATION RATES

The capitalization rates for Class A sales ranged from 6.37% to 8.87%. The median capitalization rate for Class A sales was 7.38% while the mean was 7.44%. The capitalization rates for Class B sales ranged from 6.74% to 8.78%. The median capitalization rate for Class B sales was 8.00% while the mean was 7.85%. The capitalization rates for Class C sales ranged from 6.32% to 9.98%. The median capitalization rate was 8.52% and the mean was 8.48%. The capitalization rates for Class D sales ranged from 8.45% to 12.95%. The median capitalization rate was 9.98% and the mean was 10.06%. Please note that the number of market transactions decreased in late 2008 and through 2009, the date of this report. I decided to analyze older sales because of the data obtained during the verification process. I adjusted the final rates based on my knowledge of the current real estate market. Below is my recommended Overall Capitalization Rates for Industrial properties.

| INDUSTRIAL CAPITALIZATION RATE | | | | |
|---|---|---|---|---|
| INDUSTRIAL | CLASS A | CLASS B | CLASS C | CLASS D |
| ALL PROPERTIES | 7.50% | 8.00% | 9.00% | 10.50% |

# ADDENDA

## CERTIFICATION

**CERTIFICATION**

**I certify that, to the best of my knowledge and belief:**

- The statements of fact contained in this report are true and correct.
- The reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions, and is personal, impartial, and unbiased professional analyses, opinions and conclusions.
- I have no present or prospective interest in the properties that are part of this report, and no personal interest with respect to the parties involved.
- I have no bias with respect to the properties that are the subject of this report or to the parties involved with this assignment.
- My engagement in this assignment was not contingent upon developing or reporting predetermined results.
- My compensation for completing this assignment is not contingent upon the development or reporting of a predetermined value or direction in value that favors the cause of the client, the amount of value opinion, the attainment of a stipulated result, or the concurrence of a subsequent event directly related to the intended use of this assignment.
- Kenneth Voss, MAI, SRA made a personal inspection of a sample of the properties that are the subject of this report.
- No one provided significant real property consulting assistance to the person signing this certification other than data extracted from various national indices.
- The reported analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the requirements of the Code of Professional Ethics and Standards of Professional Appraisal Practice of the Appraisal Institute, which include the Uniform Standards of Professional Appraisal Practice.
- The use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives.
- As of the date of this report, Kenneth Voss, MAI, SRA has completed the continuing education program of the Appraisal Institute.
- There were no steps taken in performing the analysis that were either necessary or appropriate to comply with the Competency Provision of the USPAP.
- This assignment was made subject to regulations of the State of Georgia Real Estate Appraiser Commission. The undersigned state certified appraiser has met the requirements of the board.

Kenneth Voss

Kenneth Voss, **MAI, SRA, CAE**
State of Georgia Certified General Real Property Appraiser License #5763

# PROFESSIONAL QUALIFICATIONS

# Kenneth Voss, MAI, SRA, CAE

## Background

Mr. Voss attended East Carolina University, Greenville, North Carolina graduating in 1970, with a Bachelor of Arts in Geography and History. Mr. Voss also graduated from Lindenwood College, St. Charles, Missouri in 1984 with a Master Degree in Real Estate. He began his career as an appraiser with the Snohomish County Assessors Office in Everett, Washington in 1970.

## Real Estate Experience

Mr. Voss is the principal of the firm Kenneth Voss & Associations, LLC, specializing in real estate valuation, real estate consulting, and arbitration with concentration in the south and southeast United States. Prior to opening his own appraisal practice, Mr. Voss was associated with Hoffert & Associates, Southfield, Michigan and a former Vice President with Tennenbaum & Associates, Kansas City, Missouri. Mr. Voss is a partner in the firm, Farley, Mendola, Voss & Associates, and a Senior Consultant in TEAMConsulting. Mr. Voss has spent over 35-years in county and state government, tax consulting and independent appraisal work. Mr. Voss has appraised all property types, including office, industrial facilities (manufacturing and distribution warehouses), multifamily, hospitality, land development and recreational properties. Prior to establishing Kenneth Voss & Associates, he was affiliated with the firm of Hoffert & Associates where he was Director of the Southeast Region from 1995 through 2000, Vice President, Valuation Services with Tenenbaum & Associates from 1989 to 1995 prior to their merger with Ernst & Young, LLP. He received his CAE designation in 1975, SRA designation in 1978 and the MAI designation in 1991. Mr. Voss is also a Senior National Instructor for various IAAO Courses and various seminars.

## Professional Affiliations

**MAI** Member of the Appraisal Institute
**SRA** Member of the Appraisal Institute
**CAE** Member of the International Association of Assessing Officers
Real Estate Appraiser, Georgia and West Virginia
Affiliate Member, Certified Commercial Investment Member (CCIM)
Georgia Association of Assessing Officials (GAAO)
Marine Corps Reserve Officers Association (MCROA)

## Author and Lecturer

"Highest and Best Use," National Association of Review Appraisers, 1989
Mr. Voss has served as a moderator and speaker at various Annual Conferences, Legal Seminars and The Trail Preparation Seminars hosted by the International Association of Assessing Officers.

## Education

Various real estate courses offered by the Appraisal Institute and other appraisal organizations including Highest and Best Use Analysis, Standards of Professional Appraisal Practice, Advanced Income Capitalization, and Advanced Applications.

# GENERAL ASSUMPTIONS AND LIMITING CONDITIONS

# FOR A CONSULTING ASSIGNMENT

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# FOR A CONSULTING ASSIGNMENT

The following Standard Conditions apply to ***real estate consulting and market analysis engagements*** by Kenneth Voss & Associate, LLC. Special conditions are added as required.

**Report Content:**

Analyses are performed and written reports are prepared in accordance with the Uniform Standards of Professional Appraisal Practice of the Appraisal Foundation and with the Appraisal Institute's Standards of Professional Appraisal Practice and Code of Professional Ethics.

The analysis assumes market conditions as observed as of the current date of our research stated in the letter of transmittal. These market conditions are believed to be correct; however, the analysts assume no liability should market conditions materially change because of unusual or unforeseen circumstances.

No opinion is rendered as to property title, which is assumed to be good and marketable. Unless otherwise stated, no consideration is given to liens or encumbrances against the property. It is assumed that legal, engineering, or other professional advice, as may be required, has been or will be obtained from professional sources and that the report will not be used for guidance in legal or technical matters such as, but not limited to, the existence of encroachments, easements or other discrepancies affecting the legal description of the property. It is assumed that there are no concealed or dubious conditions of the subsoil or subsurface waters including water table and flood plain, unless otherwise noted. We further assume there are no regulations of any government entity to control or restrict the use of the property unless specifically referred to in the report. It is assumed that the property will not operate in violation of any applicable government regulations, codes, ordinances, or statues.

This report is not intended to be an engineering report. We are not qualified as structural or environmental engineers; therefore, we are not qualified to judge the structural or environmental integrity of the improvements, if any. Consequently, no warranty or representations are made nor any liability assumed for the structural soundness, quality, adequacy or capacities of said improvements and utility services, including the construction materials, particularly the roof, foundations, and equipment, including the HVAC systems, if applicable. Should there be any question concerning same, it is strongly recommended that an engineering, construction and/or environmental inspection be obtained. We will call to your attention any apparent defects or material adverse conditions which come to our attention.

In the absence of competent technical advice to the contrary, it is assumed that the property being analyzed is not adversely affected by concealed or unapparent hazards such as, but not limited to asbestos, hazardous, or contaminated substances, toxic waste, or radioactivity.

Information furnished by others is presumed to be reliable, and where so specified in the report, has been verified; but no responsibility, whether legal or otherwise, is assumed for its accuracy, and it cannot be guaranteed as being certain. No single item of information was completely relied upon to the exclusion of other information.

Analysis reports may contain estimated of future financial performance, estimates opinions that represent the analyst's view of reasonable expectations at a particular point in time, but such information, estimates or opinions are not offered as predictions or as assurances that a particular level of income or profit will be achieved, that events will occur, or that a particular price will be offered or accepted. Actual results achieved during the period covered by our prospective financial analyses will vary from those described in our report, and the variations may be material.

Any proposed construction of rehabilitation referred to in the analysis is assumed to be completed within a reasonable time and in a workmanlike manner according to or exceeding currently accepted standards of design and methods of construction.

It should be specifically noted by any prospective mortgagee that the analysis assumes that the property will be competently managed, leased, and maintained by financially sound owners over the expected period of ownership. This engagement, unless otherwise noted, does not entail an evaluation of management's or owner's effectiveness, nor are we responsible for future marketing efforts and other management or ownership actions upon which actual results will depend.

The Americans with Disabilities Act ("ADA") became effective January 26, 1992. Kenneth Voss & Associates, LLC has not made a specific compliance survey and analysis of this property to determine whether or not it is in conformity with the various detailed requirements of ADA. It is possible that a compliance survey of the property, together with a detailed analysis of the requirements of the ADA, could reveal that the property is not in compliance with one or more of the requirements of the Act. If so, this fact could have a negative effect upon the value of the property. Since Kenneth Voss & Associates, LLC has no direct evidence relating to this issue, Kenneth Voss & Associates, LLC did not consider how possible non-compliance with the requirements of ADA would impact the value of the property being analyzed.

**Use of the Report:**

The analysis applies only to the property or market area described and for the purpose so stated and should not be used for any other purpose. The report and estimates of the future financial performances included herein, are intended for the information of the person or persons to whom they are addressed, solely for the purposes stated herein, and should not be relied upon for any other purpose. The addressee shall not distribute the report to third parties without prior permission from Kenneth Voss & Associates, LLC. Before such permission shall be provided, the third party shall agree to hold harmless relative to their use of the report. Neither our report, nor its contents, nor any reference to the analysts or Kenneth Voss & Associates, LLC, may be included or quoted in any offering circular or registration statement, prospectus, sales brochure, appraisal, loan or other agreement or documents without prior written permission. Permission will be granted only upon meeting certain conditions. Generally, Kenneth Voss & Associates, LLC will not agree to the use of its name as a "named expert" within the meaning of the Securities Act of 1933 and the securities Act of 1934.

Neither the report nor any portions thereof (especially the identity of the analysts or Kenneth Voss & Associates, LLC) shall be disseminated to the public through public relations media, news media, advertising media, sales media or any other public means of communications without the prior written consent and approval of Kenneth Voss & Associates, LLC. The date(s) to which the conclusions apply is set forth in the letter of transmittal and within the body of the report. The financial analysis is based on the purchasing power of the United States dollar as of that date.

**Terms of the Engagement:**

Assignments are accepted with the understanding that there is no obligation to furnish services after completion of the original document. If the need for subsequent service related to a specific assignment (e.g., testimony, updates, conferences, reprint, or copy service) is contemplated, special arrangements acceptable to Kenneth Voss & Associates, LLC must be made in advance. The working papers for this engagement have been retained in our files and are available for your reference.

Unless otherwise stated, no effort has been made to determine the possible effect, if any, on the subject property of energy shortage or future federal, state or local legislation, including environmental or ecological matters or interpretations thereof.

We take no responsibility for any events, conditions or circumstances affecting the subject property or its value, that take place subsequent to either the effective date of the analysis cited in the report or the date of our field inspection, whichever occurs first.