RetailResearch

MARKET OVERVIEW

Marcus & Millichap

Orlando Metro Area *Third Quarter 2014*

Rising Tourism Lifting Orlando Retail Space Demand

New developments are luring visitors to Orlando, benefiting retailers and tightening operations. In 2013, nearly 59 million people visited the metro, setting a record for a fourth year. Elevated tourism is propelling leisure and hospitality employment and driving retail spending at restaurants, bars and shopping centers. The industry is gaining further momentum with new attractions and hotels. Universal Orlando's Wizarding World of Harry Potter and Cabana Bay Beach Resort opened this summer, while SeaWorld and Walt Disney World expanded as well. These developments have translated into a rising number of visitors and business travelers, lifting hotel occupancy 300 basis points year to date in June. Additionally, renovations started on the Florida Citrus Bowl Stadium and ground broke on a multipurpose soccer stadium in downtown Orlando, both of which will attract future tourists. Improving economic trends are building developer's confidence. Retail completions will reach their highest level since 2009, though builders remain cautious as new construction is heavily pre-leased. Relatively limited available new inventory and rising space demand will lower vacancy through the remainder of the year.

Tightening vacancy, rent gains and widely available access to acquisition financing are sustaining investor interest in Orlando retail assets. The stable market is attracting foreign investors, particularly from South America and Canada, who are seeking properties that provide steady cash flow and therefore bid aggressively. Meanwhile, local private investors remain active in the market, and the growing buyer pool is intensifying competition for retail properties and pushing up property values. Highly visible properties with strong tenants along major roads are generating multiple offers. A shortage in inventory, most notably for quality single-tenant assets and grocery-anchored shopping centers, is compressing cap rates. Compared with the previous 12 months, initial yields in the multi-tenant sector have reduced roughly 20 basis points to the high-7 percent range and 50 basis points to the mid-6 percent area for single-tenant properties.

2014 Annual Retail Forecast

3.4% increase in total employment

Employment: Local employers will create 37,000 positions this year, increasing payrolls 3.4 percent and matching last year's growth. Steady hiring will pull down the unemployment rate 10 basis points to 5.9 percent, the lowest level since 2007.

880,000 square feet will be completed

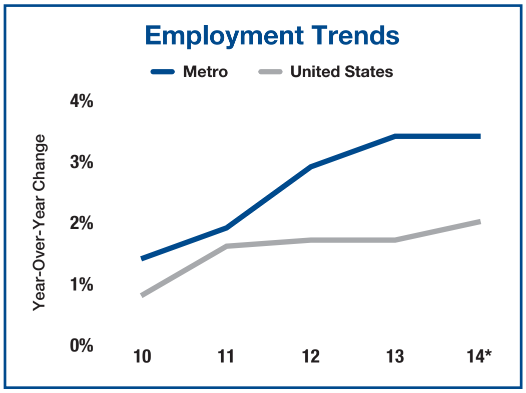
Construction: Developers will complete 880,000 square feet of retail space, the largest expansion of stock since 2009, yet well below pre-recession levels. One project, The Crosslands located in Kissimmee, accounts for nearly half of the new space coming online. Last year, 660,000 square feet was delivered.

60 basis point decrease in vacancy

Vacancy: Strong demand for retail space and heavily pre-leased new inventory will put downward pressure on vacancy. In 2014, vacancy will fall 60 basis points to 7.5 percent, building on the 10-basis point reduction last year.

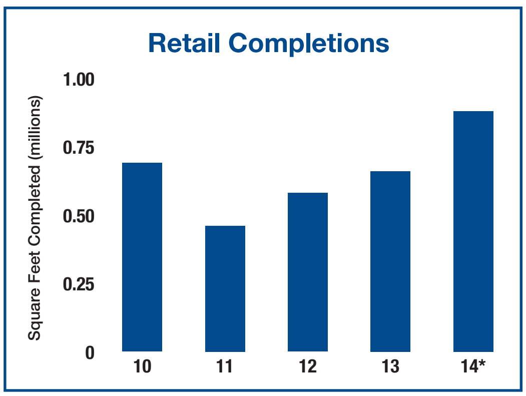
2.8% increase in asking rents

Rents: Tightening vacancy will encourage operators to raise the pace of rent growth. This year, asking rents will reach \$14.95 per square foot, representing a 2.8 percent increase. In 2013, rents advanced 1.3 percent.



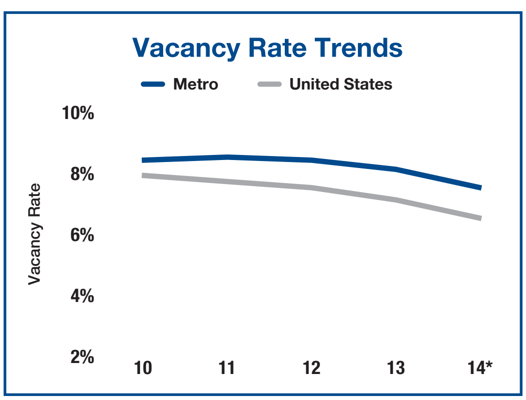
Economy

- Metro employers created 39,300 jobs during the last 12 months, expanding payrolls 3.7 percent and surpassing the pre-recession peak. In the corresponding period last year, 35,500 workers were hired.
- The leisure and hospitality segment led employment gains after generating nearly 12,500 positions. Universal Orlando Resort is supporting growth in the sector as the employer created 3,500 jobs for the opening of Diagon Alley and the Cabana Bay Beach Resort.
- Steady hiring has lifted confidence in the economy and motivated consumers to spend. Retail sales in the Orlando metro jumped 6.0 percent year over year in June, far above the national average of 4.4 percent.
- **Outlook:** This year, employment will rise 3.4 percent with the addition of 37,000 jobs.



Construction

- Developers completed 560,000 square feet during the past four quarters, lifting retail inventory 0.4 percent. In the preceding 12-month period, 630,000 square feet was delivered.
- The largest project finished year to date is the second phase of Viera Shops, totaling 46,000 square feet. The combination T.J. Maxx and HomeGoods store opened its doors at the shopping center in the first quarter. A 10,000-square foot build-to-suit for Ulta Beauty and a Subway will soon join.
- Approximately 560,000 square feet is under construction and slated for completion this year. This includes the first phase of The Crosslands, which will span 427,000 square feet in Kissimmee. Marshalls, Hobby Lobby, PetSmart and HomeGoods have committed to space scheduled to be completed this fall.
- **Outlook:** Nearly 880,000 square feet of retail space will be added to inventory this year, marking a 0.6 percent increase to stock.



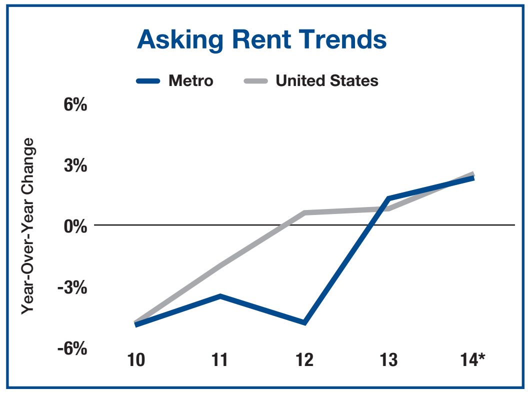
*Forecast
Source: CoStar Group, Inc.

Vacancy

- Elevated space demand and limited construction put downward pressure on vacancy. In the second quarter, vacancy dropped 70 basis points year over year to 7.8 percent, the lowest rate since mid-2009. During the same period last year, vacancy slipped 20 basis points.
- The Tourist Corridor submarket has one of the tightest vacancy rates in the metro and improved the most over the past year, plummeting 290 basis points to 6.5 percent. Meanwhile, vacancy fell 110 basis points to 10.5 percent in the Brevard County submarket.
- Multi-tenant vacancy was 9.7 percent at midyear, a 100-basis point annual decline. In the same span, vacancy in the single-tenant segment edged down 30 basis points to 6.1 percent, the lowest level in five years.
- **Outlook:** Heavily pre-leased new construction and strong demand for retail space will pull down metrowide vacancy. In 2014, vacancy will fall 60 basis points on net absorption of 1.3 million square feet to 7.5 percent.

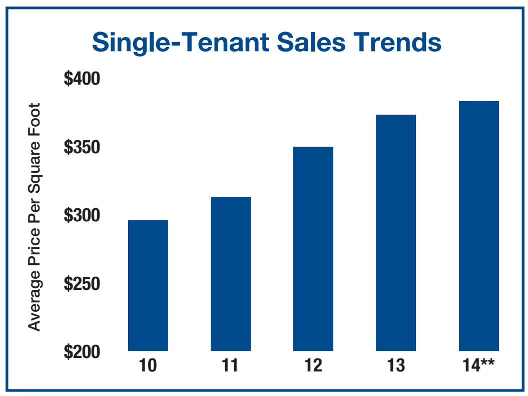
Rents

- Tightening conditions over the past year encouraged operators to raise asking rents. In the second quarter, rents reached $14.75 per square foot, a 2.6 percent year-over-year climb, the highest growth since 2008. Rent gains in the period more than erased the 2.3 percent reduction recorded one year earlier.
- Average rents in the Tourist Corridor and South Outlier submarkets jumped 7.0 and 2.5 percent over the last year to $19.19 and $18.15 per square foot respectively. In the same span, rents inched up 1.4 percent to $10.98 in the Brevard County submarket. Meanwhile, an uptick in vacancy pushed rents down 1.0 percent to $12.43 percent in the Lake County submarket.
- Single-tenant asking rents climbed 3.1 percent to $15.19 per square foot over the last year, building on the 0.2 percent rise last year. Rents at multi-tenant properties improved 2.0 percent to $14.28 per square foot, following a 5.0 percent reduction in the previous year.
- **Outlook:** As vacancy lowers, operators will lift average rents 2.8 percent to $14.95 per square foot.



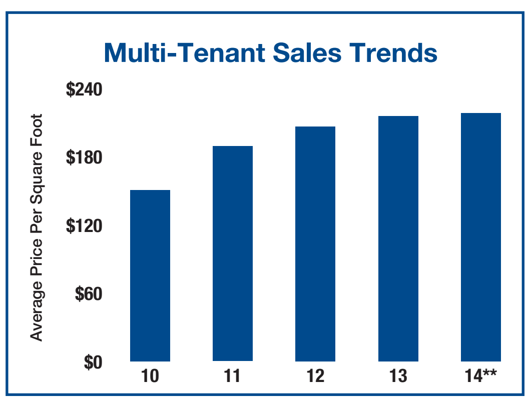
Single-Tenant Sales Trends**

- During the most recent 12-month period, sales activity dipped 12 percent as a result of a shortage in for-sale inventory.
- Buyers paid an average price of $377 per square foot for single-tenant properties sold over the past 12 months.
- Average cap rates compressed nearly 50 basis points over the past year to the low-6 percent range. A CVS or Walgreens typically change hands at cap rates in the low-6 percent area, while a Wawa begins trading at 5 percent.
- **Outlook:** Favorable financing and limited inventory will sustain heightened interest among buyers. Single-tenant investors should find more buying opportunities as retailers follow residential growth in Minneola and Clermont.



Multi-Tenant Sales Trends**

- Multi-tenant transaction velocity increased 12 percent over the past 12 months. Deal flow more than doubled at centers measuring 100,000 to 200,000 square feet as well as 10,000 to 20,000 square feet.
- In the last year, average prices for multi-tenant assets rose moderately to $216 per square foot. Meanwhile, cap rates averaged in the mid- to high-7 percent range, after contracting 20 basis points over the last year.
- Unanchored centers in the market trade at a wide cap rate range of 7.5 to 10 percent depending heavily on property quality and location. First-year returns for a Publix anchored strip center are in the low-7 percent range, while Winn-Dixie trades 150 basis points higher. Listings for these grocery-anchored properties remain a challenge to find.
- **Outlook:** Neighborhood centers with restaurant and service tenants, retailers that generally do not compete with e-commerce, are becoming more attractive to investors.



* Forecast
** Trailing 12-month period
Sources: CoStar Group, Inc., Real Capital Analytics

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Capital Markets

By WILLIAM E. HUGHES, Senior Vice President, Marcus & Millichap Capital Corporation

- According to the minutes of the most recent FOMC meeting, the Fed will cease asset purchases associated with the third round of quantitative easing in October this year. The tapering was announced in late 2013 and commenced in January. Healthy economic indicators encouraged the Fed to pare $10 billion in asset purchases during each meeting thus far in 2014. Employment reached pre-recession levels in the second quarter and the unemployment rate has fallen into the low-6 percent range.

- While the latest round of quantitative easing comes to a close, little impact on interest rates is anticipated until 2015. Investors long ago reacted to the taper and any potential increase in Treasurys has been baked into current prices. Recently, the 10-year Treasury dipped below the 2.5 percent threshold as foreign and local investors sought a safe haven for capital because of international conflicts. The rate is anticipated to stay in the current range until early 2015, when the Fed lifts targets on the discount and funds rates.

- In the single-tenant arena, nearly all lenders are active for properties occupied by national credit tenants. Many national banks have been aggressive in specific areas, which has pushed national LTVs between 65 and 80 percent. Interest rates for single-tenant, net-leased properties range from the mid-3 percent to the high-4 percent areas, depending upon tenant creditworthiness and length of lease.

- Underwriting is loosening in the multi-tenant arena as strong evidence of healthier property fundamentals emerges and lenders awash with capital seek to provide loans. CMBS is a growing presence in the $10 million-plus asset class, joining life companies as the primary loan issuers for larger deals. Interest rates for these transactions are in the mid- to high-4 percent area for 10-year terms. Below $10 million, national and regional banks offer loans in the low-4 to high-4 percent range on five- to seven-year terms.

Local Highlights

- Orlando's attractions are luring a record number of visitors. In June, hotel occupancy was 76.9 percent, the best performance for that month in almost a decade. Since January, vacancy improved 4.5 percent compared with the previous period one year earlier, above the national average.

- Developers are awaiting approval on a 260,000-square foot retail complex just north of Orlando International Airport. The project, named Lee Vista Promenade, features a movie theater, grocery store, restaurant and retail space. Besides creating 500 temporary construction jobs, the center is expected to bring hundreds of permanent positions.

- Northrop Grumman Corp. plans to make a $500 million capital investment and will bring 1,800 high-paying jobs to Melbourne. The expansion will occur over several phases. First, 300 positions will be created upon the completion of a 220,000-square foot office building. Another 1,500 workers will be hired as additional facilities, totaling up to 500,000 square feet, are delivered.

- Last year, construction began on Downtown Disney's transformation into Disney Springs. The multi-million dollar project will double the attraction's shopping, dining and entertainment options. The expansion is expected to employ 1,200 construction workers and add 4,000 workers upon completion in 2016.

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