

Market Research

INVESTMENT | SECOND QUARTER | 2009

Total investments sales volume for Nashville in 2005, 2006 and 2007 surpassed the \$1 billion mark. 2008, buoyed by a strong first two quarters, recorded a respectable \$793 million in total transactions. After the first two quarters of 2009, the Nashville market has chalked-up a sparse \$208 million in total sales. While it is hard to find a silver lining among these dismal numbers, there are some glimmers of hope that can be gleaned from these figures. All but about \$20 million of these transactions came in the last three months and as much as 40% closed in June alone – leaving many investors thinking that perhaps we are, in fact, turning a corner in Nashville.

While Nashville is no different than the rest of the nation as to the cause of the downturn, it is important to continue to emphasize why we find ourselves in this position. Currently there is a perfect storm of factors driving values significantly lower and cap rates higher. The tightening credit markets have resulted in limited availability of debt at much less favorable terms. A softer leasing environment has dropped overall asset income levels. Finally, higher perceived risk/return parameters have restricted the amount an investor is willing to pay for an asset. The example below of a fictional building disposition exemplifies a precipitous drop in pricing.

	2007 Scenario	2009 Scenario
Building's Net Operating Income	\$1,000,000	\$900,000
Investor's Desired Leveraged Return	7%	11%
Available Financing		
Loan to Value	80%	60%
Total Debt	\$11,315,417	\$5,346,535
Total Equity	\$2,828,854	\$3,564,356
Interest Rate	5.85%	7.25%
Amortization	30 Years	20 Years
Debt Service	\$801,051	\$507,093
Cash Flow After Debt Service	\$198,949	\$392,907
Property's Market Value	\$14,144,272	\$8,910,891
Property Cap Rate	7.07%	10.10%
Total Loss of Market Value	\$5,233,380 or	37.00%

The resulting speed with which prices have dropped has created not only an unwillingness among sellers to sell at all, but also an ever-widening bid-ask spread among willing buyers and sellers that has only recently begun to narrow.

The apartment sector for the last six months has been the tale of two markets. The continued availability of agency debt has mitigated somewhat the price depreciation on the newer, well-located assets. On the other end of the spectrum, there is a glut of product that has entered the market as a result of the slow unwinding of the Steve Green portfolio. These dispositions have resulted in price declines for older assets in less than desirable locations far in excess of that of any other product type. Through the first six months of the year there have been eight apartment complexes trade with an aggregate value of around \$115 million. The two major transactions over the last six months of the year both fall into the category of well-located assets whose values, though

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"The second half of the year should see increased investment activity. Hopefully, before the end of the year we will begin to see some pricing stabilization."

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PARKLANE BUILDING

SECOND QUARTER SALE



Square Feet:	110,347 SF
Value:	\$10,700,000
Buyer:	Panattoni Development Company
Seller:	Principal Life Insurance Company
Date:	June 2009
Brokers:	Crews Johnston, SIOR Perry Gooch

Why do quarterly market statistics vary from company-to-company? Two of the major reasons are: Commercial real estate companies report data using a different set of properties. Methodologies used to compute absorption, vacancies, and the treatment of sublet space are also unique to the reporting company. Any questions concerning our research processes should be directed to Nick Minadeo, 615.301.2839.

The information contained in this report was provided by sources deemed to be reliable; however, no guarantee is made as to the accuracy or reliability. As new, corrected or updated information is obtained, it is incorporated into both current and historical data, which may invalidate comparison to previously issued reports.



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down from the peak, have at least held true to historic norms. In March of this year, Covenant Capital purchased from Equity Residential, The Brixworth at West End. Covenant paid \$20.7 million or \$95,833 per unit for this class A asset in Belle Meade. In another noteworthy transaction, Principal Financial sold the last of their Nashville apartments, The Gardens of Hillsboro Village, to Centennial Holding Company for around \$27 million or \$139,000 per unit. Looking ahead, the rest of 2009 should be more of the same - the nicer assets should continue to hold their value while there continues to be a tremendous glut of older assets that will further drive down pricing on the class B and C product.

The industrial market continues to wait to see its first class A bulk transaction since the end of 2007. While there has been a steady flow of transactions since then, the vast majority of industrial sales are user sales. As a result, gauging exactly where pricing is in this sector is extremely difficult. As was the case in 2008, the investment sales that took place through the first half of 2009 were characterized by older class B transactions. In total the sector saw only three properties trade in the first six months for a total transaction value of around \$30.5 million. Perhaps the most significant transaction of the first half of the year was the sale lease back portfolio by Cracker Barrel. The majority of the assets in this transaction were stand alone restaurants. However, Cracker Barrel also disposed of a warehouse facility in Lebanon. The 383,000 square foot property was valued within the portfolio at approximately \$12.445 million, or \$32.49 per square foot.

2009 has seen little activity in the office sector in Nashville. Several products were in the market during the third quarter of last year, but when the credit crisis hit and subsequent pricing plummeted most sellers, not being forced to sell, chose to pull their properties. As a result, Nashville office sales for the first half of the year failed to top \$20 million. The only noteworthy sale of the first six months was Principal Financial's sale of The Parklane Building to Panattoni that closed just last month. The acquisition marks Panattoni's first entry into the office sector. The 110,347 square foot Parklane Building sold for \$10.7 million or around \$97 per square foot. Despite the lackluster first half of the year there are office properties in the market currently that

should be interesting to track as they entered the market after the credit crisis and have been priced accordingly.

If there was a bright spot in the Nashville investment sales market, as it relates to transaction volume, it was the retail sector. In the past, the Nashville retail market has been characterized by a large volume of small single tenant transactions, single transactions within a larger portfolio or off-market transactions that sometimes go un-recorded. The latter results in what can be artificially low overall numbers. The first six months of this year were different though with two high profile properties trading hands so far this year. Overall, the retail sector saw approximately \$46 million in total volume over the course of the first half of the year spread out over six different deals. The significant trades during the period included the sale by Centro Properties Group of the 99,000 square foot Lion's Head Village to Boyle Investment Group. The property traded for \$13.5 million or around \$136 per square foot. Also of note this year was the recent sale of The Marketplace. This 168,000 square foot big box anchored center sold last month for \$14.3 million or \$85 per square foot. The center was sold by DDR to Monroe Investments. In addition to the respectable volume of transactions thus far in the retail market, there are several interesting deals on the market as well. Finally, because the retail market is experiencing the greatest softness among property types on the leasing side, it is only a matter of time before distressed assets begin to enter the market.

As was the case at the end of 2008, the vast majority of buyers continue to remain on the sideline awaiting some clarity as to the market's direction, and many of the stalwarts of the Nashville commercial market have begun to trim their holdings. With Wall Street lenders perhaps out of the game for good and other traditional sources of non-recourse debt skittish to invest outside of core markets, it remains likely that pricing pressures will continue into the second half of the year. As a silver lining, many savvy investors have secured their cash position, and are eager to begin making acquisitions. As a result, it is reasonable to assume that the second half of the year should see increased activity, and hopefully before the end of the year, we will begin to see some pricing stabilization.