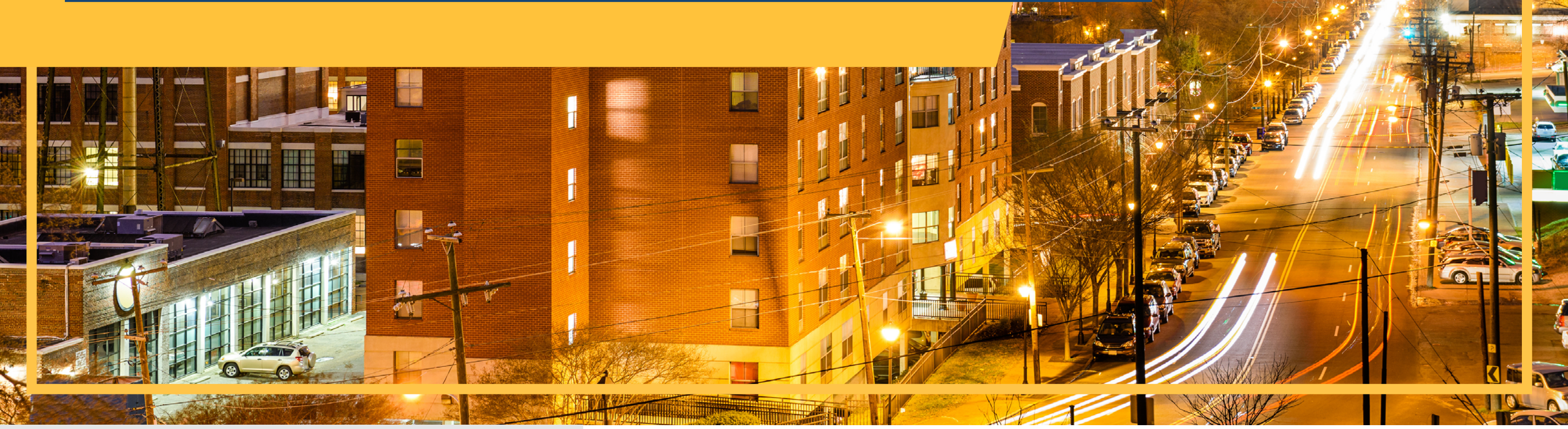
JOYNER COMMERCIAL

WINTER 2022

MARKET UPDATE



Greater Richmond
Commercial Real Estate

"Like all things these days, the calculations of creditworthiness are changing."

The New Math of Tenant Creditworthiness

Understanding the creditworthiness of your tenant is one of the most important aspects of successful commercial real estate ownership.

The riskiness of tenants can be the difference between profit and default for some properties and tenant strength factors into both a building's valuation and its ability to take out debt. Like all things these days, the calculations of creditworthiness are changing. Year three of a pandemic with no sign of normal in sight has redefined what a reliable tenant looks like. Some industry stalwarts have been hit hard by disruption and a changing work environment. But the big question is how much an office tenants' new work policies impact its creditworthiness.

Creditworthiness starts in the books. Balances sheets, income statements, tax returns, and other official financial records help paint a basic picture of health for any tenant. Rental history gives landlords a timeline to see how a potential tenant has honored their leases and relationships with other tenants. A general assessment of the industry the tenant operates in helps colors in the big picture. But the devil is in the details and the ass is in the assumptions. (Continued on next page)

Is a tenant that has robust hybrid work policies, allowing employees to work from home two or more days a week, a reliable tenant? Landlords across the country are scratching their heads. Taking an optimistic view, it's reasonable to think that companies with hybrid work policies during a pandemic are taking appropriate precautions to protect their staff and operations. Regardless of how much they use the space during the pandemic, they're still paying for it. That's good for the building's balance sheet, at least.

Pessimists might say that using the office less could very likely lead to a significant reduction in space. Worse yet, if a company decides to go entirely remote, they might drop out of the office market altogether. The credit agency Fitch Ratings looked at two different stress level scenarios for 144 single-asset/single-borrower bonds. The first scenario assumes employees work remotely 1.5 days per week, the second assumes 3 days per week. The result of such stress would see "average market-value declines from at-origination appraised values of approximately 44 percent and 54 percent, respectively, for moderate and severe stress scenarios. Were these declines in value to occur, downgrades are possible, with 25 percent and 55 percent of investment-grade bonds potentially moving to below investment-grade."

Offices aren't going away anytime soon, but some portion of tenants are rethinking their real estate strategy in light of how they've operated during a pandemic. For office landlords, in particular, determining which tenants are likely to renew or expand is key to a building's financial health. Predicting office leasing depends on understanding and accounting for a tenant's new workplace policies.

It may still be too early to think about these things, at least so far as traditional credit and valuation go. With the pandemic still ongoing, the broader world of commercial office landlords, lenders, and brokers are convinced the disruption of workplace usage is a temporary measure of the pandemic. Office buildings have been largely empty for two years now but that's hardly impacted valuations. Repeated return-to-office delays have so far not led to lease termination en masse or even a significant shrinkage in space needs. On the contrary, rent collection has been resilient. But, office landlords are offering tens of millions of dollars worth of concessions to prop up rent and demand.

The office leasing environment is uncertain. Project all the data onto the situation you want, the truth of the matter is that the office sector is waiting for the other shoe to drop. The pandemic has tenants and landlords in wait-and-see mode. Very few occupiers are rushing to make major real estate decisions, must are struggling just to hang on during such a tumultuous time. When (if?) the pandemic calms down, then the reality of the situation will start to settle in. Leasing decisions are based on long-term planning, not short-term market disruptions. A tenant's attitude toward the office is an important part of their creditworthiness. Work from home policies define that attitude.

Office landlords took a bath during the 2008 recession. The property value of offices in the U.S. fell over 40 percent. So far nothing like that has happened because of the pandemic. That doesn't necessarily mean it won't. Just because a tenant hasn't made a major real estate decision yet doesn't mean their landlord will like the one they make when they finally do. In the storm that is the pandemic, seeing the horizon is nigh impossible, but it's out there. When the skies clear, landlords will need to properly assess the damage. Understanding a company's workplace and hybrid policies can help office landlords gauge how likely they are to renew, expand, or terminate their lease. Failing to account for the new creditworthiness of tenants could end up impacting the credit of the building itself. For anyone buying into the sky-high real estate valuations we have seen in the last few years, an unforeseen lease termination could be enough to push a building into default. All because the owner didn't do the creditworthiness math right.

Source: The New Math of Tenant Creditworthiness I Kyle Hagerty I Propmodo I January 20, 2022

SOLD/LEASED IN Q4 2021

See all our listings at: JoynerCommercial.net/Property-Search

Recently Sold:

- 4,591 sf commercial building on 24.29 acres at 2800, 2801, 2802 Lamberts Ave in Richmond for $600,000. Susan Haas represented the Buyer.
- 1.8 acres of vacant land at Rt 60 & Red Lan in Powhatan for $262,000. Bill Phillips represented the Seller.
- 2,080 sf retail building on 6 acres at 5380 Darbytown Rd in Richmond for $171,000. Rob Brown & Bernard Heyward represented the Buyer.
- 7.66 acres of vacant land at 00 Coffeys & Cumberland Rd in Farmville for $29,000. Susan Haas represented the Buyer.

Recently Leased:

- 16,219 sf of office space at 6641 W Broad St in Richmond. Bill Phillips represented the Tenant.
- 6,679 sf of office space at 9011 Arboretum Pkwy in Richmond. Bill Phillips represented the Tenant.
- 2,400 sf of flex space at 2028 Dabney Rd in Richmond. Lebs Breeden represented the Tenant.
- 2,160 sf of retail space at 10835 W Broad St in Henrico. Todd Buttner represented the Tenant.
- 1,531 sf of flex space at 7921 Iron Bridge Pkwy in Chesterfield. Lebs Breeden represented the Landlord.
- 1,216 sf of retail space at 2100 John Rolfe Pkwy in Henrico. Bill Phillips represented the Tenant.
- 2,000 sf of retail space at 9015-9018 W Broad St in Henrico. Todd Buttner represented the Tenant.

What's New in RVA

Drive-Thru Coffee

Ironclad Coffee Roasters signed a lease last month on the former Bruster's Real Ice Cream at 2100 John Rolfe Parkway, in the Publix-anchored John Rolfe Commons shopping center.

Dubbed Ironclad West End, the 1,200-square-foot location will offer both drive-thru and walk-up window service. The plan is to open in mid-February. Bill Phillips of Joyner Commercial represented the buyer.

Louisa County Brewery, Winery

A new brewery and winery with a historical twist has opened on the outskirts of the Richmond region. Southern Revere Cellars opened at 1100 E. Jack Jouett Road in Louisa County.

Located on 70 acres about 45 miles west of downtown Richmond, Southern Revere offers both beer and wine — most of which will be made with grapes and hops that are currently growing on the land.

New Manufacturing Facility

Governor Ralph Northam announced that Starplast USA, will invest approximately $17.7 million to develop a new manufacturing facility in Chesterfield. Virginia successfully competed for the project, which will create 300 new jobs over five years. Established in 1958, Starplast is a family-owned company with a wealth of experience and a long-standing commitment to superior plastics.

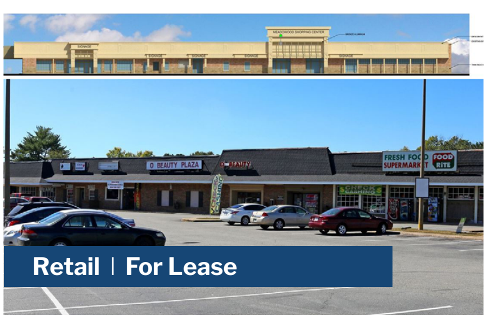
Source: Richmond BizSense | 2021

FEATURED PROPERTIES

2550 PROFESSIONAL RD
5,000 SF ON 2.98 ACRES
$15.00/SF (MG) | 2,700 SF
Lebs Breeden | (804) 536-3933
Excellent owner-occupant opportunity for purchase or lease. Two-story Office Building located in Bon Air.

1208 HULL ST
$4,000/MONTH (NNN) | 2,700 SF
Susan Haas, MURP | 804) 349-5788
Live and/or work with 6 medium and small rooms for office/retail, efficiency apartment in rear with private off-street entrance and 1 off-street parking space.

3630 CALL FEDERAL DR
$999,900 | 2.731 ACRES
Ahsan Qureshi | (804) 967-2742
Excellent redevelopment opportunity of 2.721 acres of C3 Zoned Lot just south of Hull Street populated with hotels and retail.



5100-5118 RICHMOND HENRICO TPKE
NEGOTIABLE $ | 952-15,493 SF
Todd Buttner | (410) 382-7109
Meadowood Square Shopping Center redevelopment property undergoing major upgrades. Proximity to Hanover County and City of Richmond.

1301 E CARY ST
$15.00/SF | 2,914 SF
Bill Phillips, CCIM | (804) 967-2739
Creative office space located on the basement level of the Columbian Block in Historic Shockoe Slip adjacent to The Martin Agency.

5611 PRIDE RD
$6.50 (NNN) | 26,190 SF
Lebs Breeden | (804) 536-3933
26,190 SF industrial warehouse building situated on 1.16 acres, currently zoned M-1. Located right off Route 60 w/ convenient access to Chippenham Parkway.

JOYNER COMMERCIAL

SUMMER 2022
MARKET UPDATE

Greater Richmond Commercial Real Estate

Short-Term Leases Complicate Under-writing

As lease terms shorten, the value of properties becomes more uncertain.

If the pandemic has infused business with any one idea, it's flexibility. Companies need to be flexible to get work done. Employees want flexibility to work but also be safe and manage personal and family obligations.

Flexibility has largely come down to space and, uncertainty. When executives aren't sure what normal will look like in where employees work, they can't tell how much office space they need. While some sectors of commercial real estate are stable in terms of tenants, others are a question. That's leading to some pushing for shorter term leases ironically, both by tenants and some owners as well as headaches for underwriting as the predictability of ten ancy is up in the air.

The impact short-term leases could have on overall markets depends on.their number, and that's tough to estimate, as it can vary greatly by location and type. Visual Lease is a proptech company that tracks several hundreds of thousands of leases in its systems. CEO Marc Betesh says that, first, it's still early to see what's happening, as given average lease turnovers of about five years, only roughly 20% of them have been at a natural point of renegotiation.

''Because of the instability of the market generally, the pandemic and new variants and all of the things that are happening, you probably have a bell curve of reactions," Betesh says. But there will be an inclination among many to look at their options. "When people don't know, they hedge. They take the safest, more conservative route."

"Most average rent rolls have decreased from 12 months to 18 months for an office building," says Transwestem associate Erik Coglianese.

"Specific to the office, we've seen a lot of short-term deals signed," Eric Enloe, head of commercial valuation for JLL's valuation and advisory services platform in Chicago, tells GlobeSt.com. "The reality is large firms, Fortune 1000 companies, private companies, they don't know what their space needs are, Everybody has been hoping they'd get clarity as time went on. Even today, people have still not figured out what their design needs are and what theirwork from home versus work in office plan is. Most companies haven't figured this out yet. So, they sign a two-year deal, one-year deal, six-month deal."

Besides the tenants, many landlords have been wary of longer leases. "The owners didn't want to lock in lowprices [during the impact of pandemic conditions on prices]for a long lease," says Toni Jordan, president of the central PA division at Univest Bank and Trust Co.

The dynamic of asking for shorter leases has been largely a function of timing, Jordan adds. "As leases were rolling off, they were inclined to do shorter terms," he says. "As bankers, we look at a building a client owns. We were in touch with all of those clients. 'What's going on with all of your tenants?Are you being asked to offer concessions?' Ninety percent said they weren't asked to offer concessions or rewrite leases. I see that as evidence that [the tenants are] financially healthy and able to pay rent if they're dark or partially dark."

One sector that Transwestern has found largely ignored short-term leases have, surprisingly;

been Class B and C buildings with small tenants using anywhere from 500 to 3,000 sq. ft. "These are small companies that rely on being in the office and some of the employees may not have space to work in the house from," says Coglianese. "Those buildings have done extremely well during the pandemic."

For property owners that go this route, there are financial implications. Those with long-term lease single-tenants are in good shape. "That market is vibrant," says Enloe. "It can be a Fortune 500 company that's viewed as a very secure investment. That's trading at levels that are higher than pre pandemic."

Multi-tenant office buildings are entirely different stories. "We've seen WALT [weighted average lease terms for entire properties] continue to diminish across office product," says Coglianese. "Underwriting and valuation of properties are seeing an impact. Risk profile is increasing for the building as the terms are decreasing. Even in a normal market, it would have an impact on value and buyer underwriting. More so now because there's a question of what tenants will do."

"Some [tenants] are going to take more, some are going to take less, and some are going to take the same," Enloe says. "If you're thinking of buying a multi-tenant office building, you're trying to figure out what the tenants will do in the future." Guess wrong and you could lose big, which is why Enloe says that lenders are charging more in such situations. "Because these corporations have not figured out their real estate strategy yet, it's causing these short-term leases that are harder to underwrite."

"What we're not seeing [at high valuations are] multi-tenant office buildings and short-term leases," says Enloe. The problem is not blanket unwillingness to underwrite deals but difficulty in forecasting rents and cash flow, meaning risk is difficult to estimate.

"Does it hurt your valuation? Absolutely," Coglianese says. The working rule of thumb used to be that 75% of tenants would renew for terms of five, seven, or ten years. That's greatly changed. Currently, Transwestern's clients have seen 60% of their tenants sign short-term deals of 12 to 24 months, with many of those "possibly downsizing," according to Coglianese. Then there is the 35% signing new leases in the five- to ten -year range.

"The length of the lease was really saved by the [tenant improvement, or TI allowance] because construction costs have increased significantly," Coglianese says. "They're moving or downsizing in their existing building. They're getting a new TI package because they want their space to be really special." The only way to make things affordable is to amortize TI over a longer term. "Landlords say, 'Sure, higher TI, but a longer-term lease. And if the tenant doesn't agree, they amortize the TI numbers over a shorter period, which greatly increases the cost of the space."

As a result, owners of multi-tenant office properties are often keeping them off the market unless they have to list them for sale. "That's the reality," Enloe says. "The projects getting listed that are multi-tenant offices it could be the timing of the fund they're in and need to do redemptions and need to sell it for that reason."

The assumption is that next year might bring a stronger economy and, hopefully, lesser problems with Covid-19 and its variants. "Most of them would rather take the chance of waiting it out, seeing what happens with the pandemic, betting on office space that the employers will start to value having employees in the office and creating the company culture and people would return to the office again positively impacting their cash flows and values," Coglianese adds. ''Most of these properties are still cash flowing. Have we seen vacancies increase? Sure. But it's not enough that [some] people aren't servicing their debt." Most still can and they've been able to "renew a fair amount of their tenants."

But that has its own risk, especially if new pandemic variants like omicron have additional impacts on societies and business. If enough companies continue their real estate needs, or enough time passes so that tenants can't keep waiting for things to improve, the strategy won't last forever.

"For tenants, the things they need to be concerned about and balance is Covid safety protocols and saving money by downsizing or leaving the office space versus company culture and a sense belonging where people are excited to go to work," Coglianese says. "For landlords, they're probably concerned about media and the perception of the office space and so many people are perceived as leaving the office space. That's a concerning figure for an owner. A question for them is what are you going to do to change that? We've seen a flight to quality. The best amenified buildings, best locations are getting tenants."

Then comes the potential reckoning time. As the months pass, more and more leases will come up for renewal, all facing the potential issue that has dogged businesses and real estate since 2020. Each new variant and additional questions of what measures might be necessary to keep people safe increases the amount of uncertainty for what steps companies will take and what their space needs will be.

A lease comes up for renewal. Even the most financially steady company that had been keeping hold of long-term leases as a hedge against changing practices versus the need to create company culture will begin to ask if there is easy additional profit to be made from reconsidering the amount of leased space on hand. Perhaps flex space might be the answer, as JLL has predicted 30% of all office space globally to be flexible over the next decade.

A rush to expand flex space could keep a lid on pricing, making the approach even more fiscally interesting to companies trying, as always, to improve their balance sheet. If that happens, underwriters might see a more definite and predictable movement away from the need for as much space, reducing demand on traditional office space and providing the rationale to lower valuations.

Source: Short-Term Leases Complicate Underwriting I Erik Sherman I GlobeSt. Real Estate Forum I January/February , 2022

SOLD/LEASED IN Q2 2022

See all our listings at: JoynerCommercial.net/Property-Search

Recently Sold:

- 5,000 SF of office space at 2550 Professional Road in Richmond for $695,000. Lebs Breeden represented the seller.
- 4,603 SF of restaurant space at 119 N 18th Street in Richmond $800,000. Bill Phillips represented the seller.
- 2,934 SF of office space at 531 S Sycamore Street in Petersburg for $192,000. Todd Buttner represented the buyer.
- 1,462 SF of retail space at 802 E Nine Mile Road in Highland Springs for $175,000. Robert Brown represented the seller.

Recently Leased:

- 7,611 SF of office space at 1603 Santa Rosa Road. Bill Phillips represented the tenant.
- 5,590 SF of flex space 1521 Brook Road in Richmond. Lebs Breeden represented the landlord.
- 5,903 SF of retail space at 480 Winter Place Way in Midlothian. Bill Phillips represented the tenant.
- 2,400SF of retail space at 308 W. Broad Street in Richmond. Rob Brown represented the tenant.
- 2,382 SF of retail space at 5114 Richmond Henrico Turnpike in Richmond. Todd Buttner represented the landlord.
- 1,758 SF of office space at 2727 Enterprise Parkway in Richmond. Bill Phillips represented the landlord.
- 1,555 SF of office space at 2923 Polo Parkway in Midlothian. Todd Buttner represented the tenant.

What's New in RVA

'The Lake' in Chesterfield

A water-centric mixed-use development years in the making appears primed to get a boost from Chesterfield County.

The development is currently expected to cost $323 million and would rise at 13400 Genito Road, and 2500, 2601 and 2991 Genito Place.

The development is expected to have 250,000 square feet of office, retail, entertainment and restaurant uses, though a specific breakdown hasn't yet been determined, Burkhart said. A 170-bed hotel is planned.

Riverfront Amphitheater Planned

The centuries-old stonework at Historic Tredegar could soon form the framework for Richmond's version of Red Rocks.

The outdoor venue, which would host concerts as well as community events, would be fitted between Tredegar and the filled-in portion of the Kanawha Canal, which follows a curve in the hillside that forms an amphitheater-shaped footprint.

"Project Rocky"

A massive e-commerce fulfillment center, similar to Amazon's robotics facility near Richmond Raceway, is in the works for a site in northeastern Goochland County about two miles west of Wyndham and Short Pump.

The center would be built off a 650,000-square-foot footprint, the same footprint as the raceway facility, which Amazon refers to as its RIC4 fulfillment center.

Source: Richmond BizSense I 2022

FEATURED PROPERTIES

KENTUCKY SPRINGS RD & HALEY DR
$225,000 | 0.42 ACRES
Lebs Breeden | (804) 536-3933
3.316 acres of land fronting on Haley Drive and the corner of Kentucky Springs Road. Property is zoned C-2 for widespread commercial uses.

921 HULL ST
$1,200,000 | 4,662 SF
Susan Haas, MURP | 804) 349-5788
Renovated, one-story 4,662 SF brick storefront retail/office space is located in RVA'S fastest growing residential neighborhood.

12009 CHURCH ROAD
$900,000 | 1.57 ACRES
Sean Yoon | 804.355.4000
1.57 Acres, zoned as A-1, is rare property is suitable for a skilled nursing facility, daycare center or multifamily units. Situated in densely populated Tuckahoe Farms.

2821 N PARHAM ROAD
NEGOTIABLE | 1,500 – 3,500 SF
Todd Buttner | (410) 382-7109
This two-story, 21,776± SF medical office building is located in the heart of Henrico County and right across the newly renovated J.R. Tucker High School.

1301 E CARY STREET
$15.00 / SF | 2,914 SF
Bill Phillips, CCIM | (804) 967-2739
Creative office space located on the basement level of the Columbian Block in Historic Shockoe Slip adjacent to The Martin Agency.

3318 JEFFERSON DAVIS HIGHWAY
$895,950 | 2400 SF
Newton Carroll | 804.967.2624
Outstanding opportunity to own a thriving business that has been at this location for over 50 yrs. Location and VPD make this a very profitable investment opportunity.

2727 ENTERPRISE PARKWAY
RICHMOND, VA 23294
Phone: 804-270-9440
JoynerCommercial.net