

The Hampton Roads office market remains strong. Staying the course it has established over the last few years, the local office market ends the third quarter with a lower direct vacancy rate and higher average rental rates than the previous quarter.

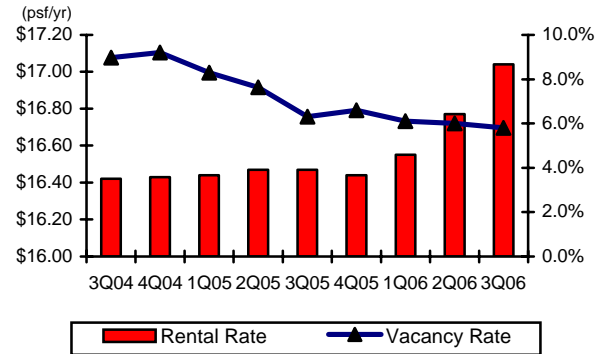
The direct weighted average annual rental rate on full service leases rose \$0.27 per square foot (psf) in the third quarter, to \$17.04 psf. The cost of leasing class A office space leapt from \$19.61 psf to \$20.13 psf, a significant jump for a single quarter.

Driving those higher rents is an ever-dwindling availability of space. Vacancy continues to drop with the direct vacancy rate dipping to a scarce 5.8%. To capitalize on this lack of availability, investors and developers have already delivered nearly 750,000 square feet (sf) of new space to the market this year (279,815 sf this quarter) and have almost 1.5 million square feet (msf) currently under construction.

No sales of significant impact to the market were recorded during the third quarter. The largest transfer noted was the purchase of 1716 Corporate Landing Parkway by Liberty Tax Service. The 30,000-sf class B office building located in the Princess Anne submarket sold for \$2.65 million or \$88.33 psf.

Leasing activity, consistently in the 300,000-sf range over the past several quarters, remained steady with 391,057 sf for this quarter. Given the size of the market and the steady stream of new construction being introduced, the absorption of new and existing space alike continues to be strong and justifies the necessity of the buildings currently under construction.

Direct Rental vs. Vacancy Rates



Staying the course it has established over the last few years, the local office market ends the third quarter with a lower direct vacancy rate and higher average rental rates than the previous quarter.

Approximately one million of the 1.4 msf of new office space currently under construction in the Hampton Roads region will be located in Southside non-CBD submarkets. The demand for office space on the Southside has driven an increase in rents from \$16.11 psf in January to \$17.06 psf at the end of the third quarter.

The largest delivery to the Peninsula during the third quarter was Port Warwick's Turner Building, a 120,000-sf, class B office building in Newport News. Rents on the Peninsula have increased from a year-end rate of \$15.97 psf to \$16.27 psf.

The Downtown Norfolk CBD remains somewhat dormant. Leasing activity was in the normal range while the submarket experienced 5,445 sf of negative absorption. Rental rates remained consistent around \$18.00 psf.

Overall, by absorbing the 750,000 sf of space delivered year-to-date while continuing to experience a drop in the vacancy rate, the Hampton Roads office market has demonstrated that it will absorb the nearly 1.5 msf currently under construction with little difficulty. The quality of this new office space should help drive up rent rates in the non-CBD areas of the region without discouraging other construction projects currently in the proposed/planning stages. ■

THALHIMER MARKET HIGHLIGHTS**Significant 3Q06 New Lease Transactions**

BUILDING	SUBMARKET	TENANT	SQUARE FEET	CLASS
Bridgeway Tech Center III	Harbourview/N Suffolk	N/A	15,000	A
500 E. Main St	Downtown Norfolk	Norfolk Southern	14,215	A
11820 Merchants Walk	Oyster Point	Progressive	11,341	A

Significant 3Q06 Sale Transactions

BUILDING	SUBMARKET	BUYER	SQUARE FEET	PURCHASE PRICE
1716 Corporate Landing Pkwy	Princess Anne	Liberty Tax Service	30,000	\$ 2,650,000
Holland Plaza	S Independence/Holland Rd	N/A	15,378	\$ 1,125,000
932 Professional Place	Greenbrier	N/A	11,500	\$ 1,500,000

Significant 3Q06 Construction Completions

BUILDING	SUBMARKET	MAJOR TENANT	SQUARE FEET	COMPLETION DATE
7447 Gregory Drive	Central Norfolk	N/A	53,815	September 2006
5741 Cleveland St	Newtown/Witchduck	N/A	24,000	August 2006
244 Clearfield Ave	Newtown/Witchduck	N/A	15,306	April 2006

Significant Projects Under Construction

BUILDING	SUBMARKET	MAJOR TENANT	SQUARE FEET	COMPLETION DATE
150 Granby St	Downtown Norfolk	Trader Publishing	220,000	November 2006
Research Quad III	Hampton Roads Center	N/A	100,000	January 2008
Convergence Center III	Virginia Beach CBD/Pembroke	N/A	100,000	November 2007

THALHIMER MARKET/CLASS STATISTICS

Market/Class	Inventory	No. of Bldgs.	Overall Vacancy Rate	Direct Vacancy Rate	YTD Leasing Activity	Under Construction	YTD Construction Completions	YTD Direct Absorption	Direct Wtd. Avg. Class A Rental Rate*
CBD	4,697,847	98	8.0%	6.5%	158,298	220,000	0	(23,621)	\$19.89
Class A	2,104,880	9	8.4%	6.6%	70,597	220,000	0	32,584	\$19.89
Class B	2,128,820	53	5.6%	4.1%	87,701	0	0	16,103	N/A
Class C	464,147	36	17.3%	17.3%	0	0	0	(72,308)	N/A
Non-CBD/Southside	22,313,661	1,290	6.0%	5.5%	692,026	990,157	396,547	395,730	\$20.32
Class A	5,556,196	84	6.7%	5.8%	214,278	870,847	300,199	197,213	\$20.32
Class B	11,649,272	468	7.1%	6.7%	428,404	119,310	71,848	144,286	N/A
Class C	5,108,193	738	3.5%	3.3%	49,344	0	24,500	54,231	N/A
Non-CBD/Peninsula	10,360,199	771	6.4%	6.0%	263,459	235,083	347,500	215,447	\$19.70
Class A	3,033,497	45	5.4%	5.0%	115,379	216,830	143,500	80,681	\$19.70
Class B	5,850,222	511	4.9%	4.5%	131,506	18,253	204,000	145,632	N/A
Class C	1,476,480	215	14.1%	14.1%	16,574	0	0	(10,866)	N/A
Total	37,371,707	2,159	6.4%	5.8%	1,113,783	1,445,240	744,047	587,556	\$20.13

* Rental rates reflect \$psf/year