MAREMA

MID ATLANTIC REAL ESTATE MARKETING ASSOCIATION

ESTABLISHED IN 1976

The MarketPlace

3rd Qtr 2021

PRESIDENT'S REMARKS....

Introducing the 3rd quarter MAREMA "**The MarketPlace**" 2021 edition. In this addition we discuss several topics important to our industry. We are just weeks away from the 2021 Annual Meeting. Remember the Annual Meeting this year will feature a trade show and highlight our 45th anniversary through past presidents and lifetime member's testimonials. Our theme this year is RE-imagine and will be held at Ocean City, MD. Don't miss out on seeing videos from many of our past presidents and hearing from our keynote speaker Jan Zachariasse. If you have not registered yet, do it right now and don't forget to reserve your hotel room. I would like to extend a welcome to all our new members introduced in this quarter's newsletter. Be sure to take advantage of our new feature "Ask An Expert" providing membership the opportunity to ask other members questions. Members, I look forward to seeing you at our Monthly Meetings and remember to invite a guest. If you are not a member yet, join us as my guest and learn how we share best practices and share Haves (property listings) and Wants each month. I hope everyone enjoys "**The MarketPlace**".

Annual Meeting October 28 - 30, 2021

Meet our New Members

MULUGETA DESSIE

Long and Foster

My name is Mulugeta Dessie and I am an experienced real estate consultant with Long & Foster Real Estate Company. My success is recognized with my membership in Long & Foster's prestigious GOLD TEAM. Acceptance into this team is a result of past sales accomplishments, but most importantly, customer satisfaction. In addition I am the recipient of the Best of Zillow title that is reserved for agents with experience scores of 90+, as well as past sales and validated real estate license numbers on their profiles. Best of Zillow agents are the top 10% of Zillow Premier Agents, known for demonstrating trustworthiness, responsiveness and knowledge in every client interaction.

My Mission is a firm belief that Home Ownership is one of the best means for clients to build a personal wealth foundation for themselves and their families. Buying or selling your home is a very personal and emotional decision involving many different circumstances. A caring and compassionate, yet business savvy approach is what I bring to every transaction.

On a personal note, I have a PhD and MBA in Business and Finance. I live in Montgomery County, am happily married and proud father of two.

RICHARD HUANG

CapStar Commercial realty

Richard Huang is a Licensed Real Estate Salesperson in Maryland. He received his bachelor's degree in Architecture from Virginia Tech and his master's degree in Real Estate Development from the University of Maryland. He joined CapStar Commercial Realty in 2021.

He is specialized in commercial property sales and leasing, landlord & tenant representation, business brokerage, real estate financial analysis, and market analysis.

DAN MARS

Freedom Bank

I specialize in helping small businesses all along the east coast receive SBA 7(a) loans that not only can help with real estate purchases but also with business acquisitions, equipment, refinancing debt, working capital, and tenant improvements. SBA loans are a great option if conventional lending does not work.

Also can help businesses purchase real estate in under served rural areas using a USDA loan which has flexible terms and rates.

Low equity requirements for business acquisitions and real estate financing for both SBA and USDAR.

RON ZABREISKIE

Century 21 Commercial New Millennium

Since 1997, Ron has specialized in wealth creation for his clients.

Whether it's a complicated quantitative managed futures fund, financial analysis reporting, or acquiring commercial real estate for investment, to Ron, it's all about investment analysis, risk assessment, and his fiduciary duties to his client to provide the best advice possible.

Areas of Specialty Commercial Real Estate, Investment , Property Analysis, Multi-Family Analysis, and Portfolio Investment Strategies.

Investment analysis has always been my passion. Whether it's a $325 million stock portfolio or $100 million commercial real estate portfolio, the numbers behind the deal drive the decision-making process.

Lives in Ashburn, Virginia with his wife Ann. Served on community finance committee. Enjoys sailing, boating and playing golf.

Tax Reform Again Threatens 1031 Exchanges for Investment Property Taxpayers

By: Frank Dillow

A 1031 property tax exchange refers to a sale and purchase of "like-kind" investment real estate completed under Section 1031 of the federal tax code. When one investment property is sold, it allows the tax on the gain from that sale to be deferred into another purchased investment property.

The provisions available under Section 1031 are purely for investment real estate. If the property is used as a home---even a second or third home, it does not qualify, unless it is leased and treated as an investment. Similarly, profits from "flippers" who buy a property in order to flip it for a profit do not qualify, as their profits are considered income under the tax code, not capital gains.

Because it is part of the tax code, the sale and purchase must comply exactly with the statutory language, or the tax benefit is lost and the seller will pay all taxes due from the sale.

Here's how a Section 1031 exchange works. When sellers close on the sale of their real estate they have 45 days to identify up to three properties whose value totals at least as much as the sale price of the original property. The proceeds of the sale are given at closing to a disinterested third party, known as a "qualified intermediary," who can be an individual, a bank or some other entity as long as they are not connected to the seller. The intermediary holds the money until it is released in order to complete the purchase of replacement real estate. The "like-kind" replacement property does not need to be identical to the sold property-- it can actually be up to three properties – but all must be investment real estate located in the United States. The provision does not apply to purchases of foreign properties. The purchase(s) must be completed within 180 days of the original sale, at which time the intermediary facilitates the transaction by transferring the title of the replacement properties to the new owner.

In this way the seller never receives the cash from the property sale, but winds up with a new property or properties of at least equal value, just as if the properties had been "swapped." If the price of the new properties is less than the sales price of the original property, the cash difference is given to the seller and that portion is outside the limits of the 1031 exchange and is subject to taxes.

The deferred tax from the sold property comes due when its replacement is sold. However, the taxpayer can again exercise the provisions of Section 1031 on the sale of this property and defer the taxes further by again "swapping" for up to three additional properties. This can be done as long as the seller lives, creating a "swap 'till you drop" tax strategy. When the property owner dies, the property becomes a part of their estate and is subject to any estate taxes that may apply.

“First adopted one hundred years ago in 1921, Section 1031 was originally designed to allow farmers and other taxpayers to ‘swap’ property of equal value without paying taxes, at a time when cash was scarce and the need to pay taxes on the sale would have seriously discouraged the transaction,” explains Bill Horan, whose family has facilitated 1031 exchanges as “certified exchange specialists” for the past 90 years.“Backward swaps” were included in the deferral with Congressional revisions to the code in 2000. Since then, an investor has been able to first purchase up to three new properties through an intermediary, and then sell the old property and still defer taxes on the sale of the old property into the already purchased property, even though the sale of the first property occurs after the purchase of the replacement property.

As first enacted, the “like-kind exchange” included both real estate and other kinds of property, such as vehicle fleets or heavy equipment. Largely because of the perception that Section 1031 created a tax loophole allowing wealthy taxpayers to avoid taxes on the sale of their personal art collections or yachts, the tax reform act of 2017 eliminated tax deferrals for like-kind exchanges for all assets other than real estate.

Now the remaining real property provisions are again under attack.

In President Joe Biden’s budget proposal currently before Congress, the Administration proposes to limit the deferred benefit to $500,000 for each transaction, beginning December 31, 2021. A decision will likely be made by Congress to either adopt the restriction, or even eliminate the entire deferral, when they adopt their “budget reconciliation” legislation later this fall. Virginia Senator Mark Warner and Rep. Don Beyer are both members of their Congressional tax writing committees and will be key players in the outcome.

A coalition of 23 different organizations including the National Association of Realtors®, along with organizations for developers, investors, lenders and even farmers and foresters, have come together in an attempt to preserve the current deferral. They argue that such action could encourage taxpayers to sit on their assets and not purchase investment properties. As a result, existing properties could deteriorate as investors have less incentive to renovate or repurpose their properties for resale.

Horan’s firm, the Realty Exchange Corporation, has facilitated the sale of literally millions of properties during the past 90 years, mostly of the single transaction “mom and pop” variety. “They are the ones who will be hurt by these proposed changes,” Horan predicted.

Today, studies performed for the coalition show that 10-20% of all sales of investment property, including 40% of multi-family exchanges rely on Section 1031.

“As property owners strive to put diversity and inclusion concepts into action, the like-kind exchange established in Section 1031 of the U.S. tax code can serve as a powerful tool that fosters economic development and promotes job growth for people from all walks of life,” the NAR explains in a May 6 white paper.

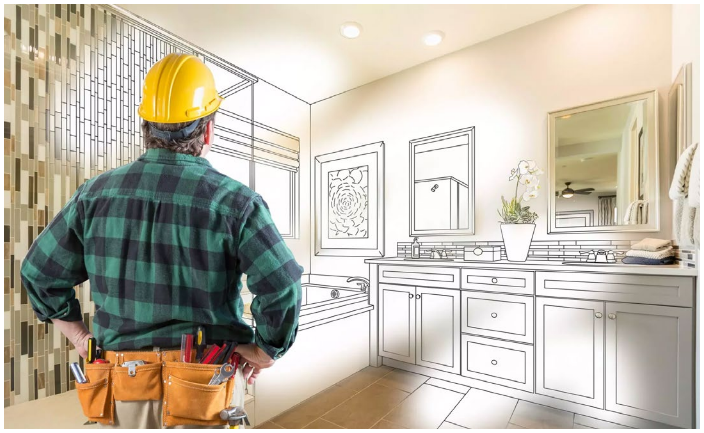
NAR advises that Realtors® can play a key role educating their Congressional delegations on the importance of this provision. “Who better knows the communities and economies of the states and districts of Senate and House members,” the NAR pointed out. “Who can better pull together key commercial leaders to meet with policymakers and convince them that success in rebuilding and hiring has, and can again, come from carefully planned real estate development, based in many cases on the bedrock of like-kind exchanges?”

Small Construction Jobs

A Construction Agreement that protects a Property Owner

By: Peter Pokorny

Introduction – Real estate owners frequently hire contractors for small and less complex projects to construct, remodel or improve their property. Even for small jobs, a construction contract is beneficial. The contract requires both parties to reach an agreement on the scope of the project and payment before work begins and protects the owner if a dispute arises. This article discusses some key terms an owner may want to consider in a small job construction contract.



Even for small construction projects, a construction contract can protect a property owner in several ways.

- **Pre-Work Obligations** – Before starting the project the contractor should provide the owner (i) plans and specifications showing all of the work in reasonable detail, (ii) copies of all permits required to perform the work, and (iii) evidence of comprehensive general liability insurance, worker's compensation insurance and umbrella insurance.

- **Inspection** – The owner should have the right to inspect and be present during the performance of the work to protect interest in the Property. The owner should make sure that the contractor agrees that it has no claims because of the owner's presence or inspections.

- **Completion** – The contract should specify the outside date of completion and if there are any penalties or consequences if there is a delay in completion.

- **Indemnity** - The contractor should indemnify and hold the owner harmless from any claims and damages that were caused by the contractor's breach of the agreement. In addition, the indemnity provisions should survive the expiration or termination of the agreement.

- **Warranty** – The Contractor should guaranty its work be free from defects for a period of not less than one year from the date of completion. Further, the contractor should assign to the owner any other applicable warranties or guaranties received by the contractor from its subcontractors or suppliers with regard to the work.

- **Repair** – The contractor should restore any affected area of the property damaged during the performance of the work.

- **Termination** – The owner may want to have the right to terminate the contract and/or take over the work if contractor is not performing the work timely and properly. For even more protection, the owner may want the right to terminate, at its sole discretion, regardless of how the contractor is performing. The contractor, however, may demand some compensation to cover lost profit for any discretionary termination right.

Conclusions – Even for a small job, a well written construction agreement provides multiple benefits. An experienced business attorney can draft an agreement to address the issues discussed above and any other issues that may pertain to the specific project.

What Are Commercial Real Estate Investors Buying These Days?

How Current Times Have Changed Investors' Interest in Property Types

By: Joe Serafin

CRE Investor Focus: The Big Picture

What are the best commercial real estate sectors? Which sectors are attracting the most investor interest? Where are the upside opportunities?

CRE is poised for growth. Goldman Sachs forecast a YoY GDP growth of 6.8% this year, inflation is likely to accelerate, positively impacting the cost of debt. Lending rates will remain low, and the Fed Funds Rate will remain stable for the foreseeable future so, all-in-all, principal values should rise. Additionally, as of August 30, the S&P REIT index showed an annual return of 37.99%.

The COVID-19 pandemic has forced us to look again at traditional market sectors. Transitions in CRE were already happening, but they are expected to accelerate. New technology, e-commerce advances, changes in spending habits, the great resignation, the younger generations' focus on more flexibility, more money, and more happiness are driving the increase in remote working. These, in turn, also seem to be generating greater demands for better health care.

These factors and forces are impacting the commercial real estate market, nationally, regionally, and locally. Let us now take a whistle-stop look at four specific CRE sectors before refocusing on our own area.

Multi-Family

In the top 20 metro areas, multifamily construction is strong. In 2020 Q3, 110,000 units had been delivered, with another 580,000 under construction. Rent collections, overall, and financial performance are strong, making this sector a desirable asset class. Older class B office buildings are being repurposed as residences to provide larger living and work spaces for the modern family.

Industrial

CBRE 's 2021 US Real Estate Market Outlook stated that the industrial sector is one of the most resilient and will be driven by e-commerce demand. Net absorption is expected to reach 250 million SF this year. Retail-to-industrial conversion will accelerate. The strong demand for infill warehouse space in many urban areas is constrained by land availability and high costs. Adaptive reuse of retail property to industrial is expected to continue its upward trend. E-commerce demands new design features, and it may be more advantageous in some urban areas to refit rather than build new ones.

New industrial completions are expected to increase by 21% on top of last year's growth. Inventory control, it seems, is a strong driver since safety stock holdings, needed to avoid inventory disruption, could increase from 15 days to 60 days. Despite low cap rates, domestic and foreign investors are expected to continually inject the necessary capital to ensure supply meets demand. Rent increases are expected to offset any low going-in cap rate.

CBRE also said that almost 80% of industrial markets will see rent rises which will exceed historical averages in the next few years.

Hospitality

COVID-19 saw this sector plummet to a 22% occupancy rate and an 81% decline in RevPar at its lowest point last year. 2021 should see an average occupancy rate climbing to 52%, then 61% in 2022. The long recovery could mean this sector will offer good long-term opportunities. Vacationers and conference organizers are likely to look for locations where guests will find cultural amenities, high quality entertainment, and unique attractions.

Some long-stay properties are being converted to student housing. The increasing demand for lower income homes, which includes hospital workers, teachers, some police officer ranks, and retirees is also likely to create demand for repurposed properties to house them.

Retail

The retail sector has been hit hard, but opportunities exist for the creative mind. Converting mall space to logistics space is a strong possibility. Zoning restrictions and less than ideal locations may limit this opportunity, but this sector could see 5 to 10 MSF a year, and 50 to 100 MSF over the next ten years.

The desire for remote working and living in suburban, rather than urban, settings may well result in higher density residences and a preference for increased walkability ratings. This in turn may result in more last-mile distribution and warehouse centers. These warehouses could also attract on-site shoppers who can both buy at wholesale prices as well as satisfy their buy online, pickup in-store, and ship from store lifestyles.

Now let us turn to the DC Metro area.

The DC Metro Area

The Metro area's investment property market shows 44,700 buildings owned as investment totaling 914 million SF. (19.3 MSF was the amount for sale last year.) Market rent per SF, across all sectors, stands at $29.06 with a market sale price averaging $278/SF, and a cap rate of 6.0%. 12-month occupancy at delivery was 74%. The overall current vacancy rate is 11%.

Looking at sales, we see that the asking price per SF was $177, and the selling price averaged $163.72 (a negative difference of 7.5%) for a total of $14.2B of investment property sold in the past year.

Qs 1 and 4 were the two peak selling quarters in 2020. Q4 sales exceeded $4 billion. 2021's peak quarter in Q2 with sales approaching $2.25 billion. The most active buyer profiles in both years are private investors, followed by institutional buyers. 2021's Q3 has REITs as the major investing group.

If we do a deep dive into the ten subsectors since March 2020, we see total sales equaled $23,551,701,136, broken down into:

Office

Total sales equaled 343 properties with an average
$/SF of $288.25. The actual cap rate averaged 7.59%, and the sold to asking price was 90.54%.

Flex

Total sales equaled 72 properties with an average $/SF of $234.83. The actual cap rate averaged 7.52%, and the sold to asking price was 93.86%.

Industrial

Total sales equaled 109 properties with an average $/SF of $117.47. The actual cap rate averaged 7.11%, and the sold to asking price was 104.11%.

General Retail

Total sales equaled 252 properties with an average $/SF of $262.38. The actual cap rate averaged 6.35%, and the sold to asking price was 91.66%.

Sports and Entertainment

Only one property was sold. The selling price was $1,600,000, which was 91.43% of the asking price equaling $145.45/SF.

Multi-Family

Total sales equaled 328 properties with an average $/SF of $235.27. The actual cap rate averaged 5.69%. The gross rent multiplier averaged 8.78. The average price per unit (on 266 properties reported) was $240,679 and the sold to asking price averaged 95.41%.

Hospitality

Total sales equaled 69 properties with an average $/SF of $225.37. The average rooms per property equaled 136, resulting in an average price paid per room of $147,344. The actual cap rate averaged 7.50%, and the average sold to asking price was 95.91%.

Vacant Land

219 parcels were sold in the period averaging 35.02 acres for a price of $251,725 per acre. The sold to asking price averaged 98.11% on 78 reported parcels.

Healthcare

Total sales equaled 23 properties with an average $/SF of $235.95 and an average building size of 52,805 SF. The sold to asking price was 94.49%.

Specialty

Total sales equaled 78 properties with an average $/SF of $228.65. The actual cap rate averaged 6.44%, and the sold to asking price was 93.51%.

Dulles Area

Let’s now focus on an 8-mile radius of Dulles Airport. There are currently 2,297 investment-owned properties totaling 114 MSF. Market rent per SF, across all sectors, stands at $25.39 (87% of DC Metro) with a market sale price averaging $253/SF (91% of Metro), and a cap rate of 6.3% (5% above DC Metro) and 12-month occupancy at delivery was 93.7% (26.6% higher than DC Metro). The overall current vacancy rate is about the same at 10.7%.

The average asking price across all sectors was $174/SF (less than 1% difference) and the selling price averaged $160.08 (-8% from asking price, and 9% below the Metro area average.) 238 properties were sold in an average timeframe of 17.2 months.

2020 Q1 was by far the highest quarter for sales, following 2019 Q4’s exceptional record. 2021 Q2 is the best quarter so far, with sales of $500 million. The most active buyer profile in both years is the institutional investor. Overall, national buyers made up 69% of total contracts. Now we will look at each of the 9 subsectors (no sports and entertainment property sales were recorded.) Total sales volume in the period from March 2020 was $3,257,718,185 on a total of 220 transactions.

Office

Total sales equaled 47 properties with an average $/SF of $276.93. The actual cap rate averaged 7.13%, and the sold to asking price was 96.80%.

Flex

22 properties sold at an average of $307.26/SF. The actual cap rate on sold transactions averaged 7.4%, and the sold to asking price was 94.02%.

Industrial

The total number of industrial properties sold was 5, for a total sales price of $29,550,000 at an average $/SF of $21,400. The actual cap rate averaged 6.43%, and the sold to asking price was 77.19%.

General Retail

15 properties sold at an average $/SF of $359.04 with an average center size of 20,965 SF. The actual cap rate averaged 5.63%, and the sold to asking price was 115.95%.

Multi-Family

9 properties were sold at an average of $262.44/SF. The actual cap rate averaged 4.14%. The average price per unit was $307,296 across all 9 properties.

Hospitality

12 properties sold with an average $/SF of $112.94. Rooms per property averaged 113 giving us an average price paid per room of $80,553.

Vacant Land

56 parcels were sold with an average acreage of 25.42 for a price of $380,417 per acre. Sold to asking price averaged 78.97% on just 7 reported parcels.

Healthcare

2 properties sold. One was 49,203 SF and the other 102,785 SF. The average $/SF was $78.40.

Specialty

Total property sales equaled 10 at an average $/SF of $284.40. The actual cap rate averaged 7.0%, and the sold to asking price was 92.49%.

Summary Comment

The COVID-19 pandemic impacted the commercial real estate market. The Delta variant will be with us for the foreseeable future and, perhaps, forever. The economy is set to grow, despite some barriers, and that means commercial investors have ample opportunity to focus on their preferred business sectors.

Traditional markets will continue. They will also change in ways referred to in the initial comments, enabling investors and users to maximize opportunities and capitalize on both social and economic drivers.

The DC Metro and the Dulles Airport areas both show positivity and opportunity across all subsectors. We know what the past 18 months have delivered, let us make the most of the next 18.

UPCOMING

EVENTS

MAREMA 45th Anniversary Annual Meeting

Registration

October 28 - 30, 2021
Ocean City, MD

MAREMA members meet on the
3rd Wednesday of each month
9:30 am - 12:00 PM

We are open for business, meeting this month in person at our new meeting location and online.

8230 Old Courthouse Road

Vienna VA 22182

ASK AN EXPERT

A new forum in **The Market Place** will provide an opportunity for members to seek answers to CRE topics from our panel of experts.

Please forward questions you are encountering in your practice to:

Peter Pokorny

peter@recdc.com

or

Ed Cave

ecave@mcenearney.com