North Santa Barbara County Commercial Real Estate

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Even with the milieu of the "Great Recession" Santa Maria has grown key core facility infrastructure. Marion Hospital has nearly completed its new 216,000sf facility. Also on the campus is a nearly complete cancer center of 45,000sf. These are significant assets for the community. On the agricultural front, Windset Farms has plans in process for later phases of its recently completed 165,000sf warehouses and offices; this is in addition to the millions of square feet of state of the art greenhouses.

Still on the sidelines, commercial financing remains key to a more normal commercial market returning. Unimproved land has the greatest in risk lender's portfolios as buildings have been selling below reproduction costs, signaling questionable land values. Commercial money is still available at relatively low interest rates (6-8%) depending on the credit of the asset and the borrower's ability to service debt. For stabilized investments, such as anchored performing shopping centers and stabilized apartments, interest rates can be below 5%.

Residential

As Santa Maria is the largest population center in the Central Coast, it remains the focal point for housing. With the continuing recession, it is also the focal point for bank owned residential assets. In 2010, we saw housing prices show slight improvement; however, these numbers retreated during 2011. Median sales value has dropped by approximately 50% over the last six years. Moreover, the percentage of short sales and REO sales constitute nearly 65% of the market.

The questions we are repeatedly asked center around the remaining backlog and how far we have to go before clearing the current backlog.

The bottom of the market is selling, but it is still unclear how many more foreclosures, short sales and workouts have yet to hit the market.

Market conversations with builders center on the question of when new home construction will start again. The latest data shows that values are approximately $139/sf. Given that, it may be a while until values climb back over the threshold for housing starts. The good news is that the volume of sales is picking up and existing entry level homes are selling.

Single Family Detached Unit Sales
Santa Maria and Orcutt

	2006	2007	2008	2009	2010	2011
Number of Single Family Sales	1,335	627	1,242	1,309	993	1,045
Number of Single Family Sales REO*	3	116	772	668	364	677
Percentage of Total Sales REO (%)	0.2	18.5	62.2	51.0	36.7	64.8
Median Price ($)	455,000	395,000	270,000	240,000	247,000	220,000
Median Cost Per Square Foot ($)	278	246	179	157	154	139

Source: Central Coast Regional MLS, Stafford-McCarty Commercial Real Estate

* 2011 data includes both REO and short sales

** Data may vary from last year's reported statistics due to data variable change to accommodate multi-year comparisons and regional area reporting.

Retail/Commercial

Available commercial/retail space decreased slightly from last year within the City of Santa Maria to a total of approximately 425,200 vacant square feet. This represents approximately 9.98% of vacancy. The retail inventory base for the City of Santa Maria is approximately 4,260,000sf. Historically retail has done well. However, in the last four years, retail vacancy has remained approximately three times higher than in previous periods.

Approximately 17,520sf has been added to the retail base in Santa Maria. This was primarily 11,172sf of shop spaces added to the Vallarta Market project at the northern end of the market. At the southwestern end of the market area is the Will family's 110,000sf project in Old Orcutt (technically the County of Santa Barbara) which has been well received. It has captured an "Old Orcutt" feel. 40,000sf has been developed in the first phase. According to the ownership, achieved rents are approximately $1.75/sf net.

Some of the larger retail projects which remain on the books for development include the following:

- The Stadium Theater expansion at the mall (which has reportedly hit a financing snag)
- The Westgate Marketplace – approximately 130,000sf
- Orcutt Plaza – approximately 225,000sf
- Orcutt Marketplace – approximately 295,000sf

As with other market sectors, rent reductions and concessions are the norm as noted in following sections.

Retail Vacancy Rates
City of Santa Maria Metropolitan Area

	2004	2005	2006	2007	2008	2009	2010	2011
Rates (%)	2.30	1.00	2.00	2.70	9.80	12.50	10.62	9.98

Source: Stafford-McCarty Commercial Real Estate

Noted Transactions

Location	Size (SF)	Price ($)	($/SF)
2004 Preisker Ln.	28,000	3,000,000	107
service retail/ commercial service/ flex office			
227 E. Betteravia Rd	4,860	825,000	170
to be refurbished into David's Bridal			
2240 S. Bradley Rd.	32,088	3,000,000	93
Walmart purchased Linens 'N Things on the adjacent 2.3 acres			

Source:Stafford-McCarty Commercial Real Estate

Without any recent definitive land sales for several years, previous value ranges may still apply for appraisal purposes, but asking prices are softening. In prior years, retail land transaction ranges were from $20 to $50 per square foot depending upon size and location of the property. Talk among brokers indicates that their clients are looking for better values—maybe half of previous pricing.

Office

As to be expected, the office market saw little additions to its base this past reporting period and is still the weakest market segment. This has been attributed to the contraction of the financial markets. The office component of this market has a base inventory for 2011 at approximately 1,189,600sf with just over 266,000sf vacant.

Office vacancy has jumped to 22.37% from 16.7% in 2010. This is due to the UPS call center shutting down its local operations contributing approximately 58,000sf of vacancy. Even excluding the UPS space, office vacancy has not shifted dramatically from the all time highs, still resting near 2008 levels.

Typical deals for well located space are occurring at $1.15 NNN and up. Second generation asking rates are anywhere from $.50 to $1.25/sf/month/NNN. Newer space has asking rates as high as $1.85/sf modified gross. Similar to other market sectors, owners are working with existing tenants, rewriting leases with lower rent and terms to get tenants to stay.

As noted above Santa Maria will add significant medical square footage with Marion Medical Center's addition of approximately 216,000sf and the Hope Cancer Center addition of approximately 45,000sf. Both are scheduled for opening first quarter of 2012.

Office Vacancy Rates
City of Santa Maria Metropolitan Area

	2004	2005	2006	2007	2008	2009	2010	2011
Rates (%)	2.70	2.50	2.10	6.20	12.40	12.20	16.70	22.37

Source: Stafford-McCarty Commercial Real Estate

Noted Transactions

Location	Size (SF)	Price ($)	($/SF)
2811 Airpark Dr.	36,600	3,400,000	93
2318 Skyway Dr.	5,964	1,000,000	168

Source:Stafford-McCarty Commercial Real Estate

Similar to last year, asking rates for office zoned land have dropped. Some larger parcels are at $10.00 per square foot and have generated little interest in this last year. CPO zoned land has fallen from its high water mark of $20 to $25 per square foot as well. Hard-to-find smaller parcels, which typically command higher prices, have come down in asking rates as well.

Industrial

The expansion of several key players within the community has created optimism for the industrial market sector. The market has gone from essentially being dormant to having completed transactions with continuing market activity.

C and D Aerospace has expanded into multiple buildings in the Fairsky Business complex. Pope Group purchased the 37,500sf former CaféFX facility and Windset farms continues its significant greenhouse operation.

The message, and supported by the data in the transactions we are seeing, is that the buildings are selling for less - sometimes significantly less - than reproduction value. These purchasers are user/buyers acquiring value. Unfortunately, from a valuation perspective, this dictates that the value given to the land in these transactions is less than zero or "free", which causes portfolio issues with lenders and owners holding land notes and assets.

Given the weakened market, this sector increased its base inventory by approximately 178,000sf to approximately 7,862,000sf. This expansion is largely due to the Windset Farms warehouse and offices that are part of the substantial greenhouse project of 2.8 million square feet on Black Road.

Over the last four years, industrial vacancy has not shifted dramatically. However, there is slight improvement from the all time high vacancy with current vacancy resting near 2008 levels. The vacancy decreased from 9.08% in 2010 to 8.47% in 2011.

Asking industrial rental rates are still shifting downward, moving towards gross rent from triple net rent. Flex space from 1,500sf units and larger are in the $0.30 to $0 .60/sf gross range.

Noted Transactions

Location	Size (SF)	Price ($)	($/SF)
807 West Main St.	38,775	1,900,000	49
2004 Preisker Ln.	28,000	3,000,000	107
1341 McCoy Ln.	20,000	1,250,000	63
1317 McCoy Ln.	22,000	1,200,000	55
1376 W. Main St.	12,000	645,000	53
1455 Fairway Dr.	5,080	570,000	112
250 Roemer Ct.	7,553	665,000	90

Source:Stafford-McCarty Commercial Real Estate

Industrial Vacancy Rates
City of Santa Maria Metropolitan Area

	2004	2005	2006	2007	2008	2009	2010	2011
Rates (%)	7.50	5.60	3.60	5.70	8.80	9.60	9.08	8.47

Source: Stafford-McCarty Commercial Real Estate

Industrial Land

As noted above, land is difficult to value in the current market. Previously, land could have been justified at a value over $8.00/sf. However, very few land sales have transpired over the last couple of years. In December, 3.21 acres in the county were sold for $475,000 ($3.41/sf). This was an unimproved parcel purchased by the neighboring property owner. In 2010, there was a land sale of an approximate four acre parcel to the Chumash Tribe at $5.00/sf. We are aware of improved land parcels currently being offered for less than the $5.00/sf.

As previously noted, the inventory of finished or near finished lot product is still minimal. Price differentials between M1, CM and M2 zoning designations are negligible. Location is more of a determining factor influencing the interest and price. This is significant as the City of Santa Maria is in the process of readying extensive industrial land inventory within Area 9 of the City planning area.

Agricultural

2010 was an active year for agricultural values and there has been no evidence of change for 2011. Prime row crop ground on the west side is approximately $55,000 per acre. These values are comparable with California's iconic Salinas Valley. Quality ranches are rare on the market.

For vineyard land, quality Santa Rita and La Purisma AVA planted acres are still holding values in the $50,000 and $40,000 ranges respectively. It is interesting to note that on the east side of Santa Maria, where strawberry ground currently has a higher value than planted grapes, there has been conversion of vineyards to berries.

Commercial Investment

Those seeking high real estate returns have had a difficult time finding transactions; expectations of increasing real estate yields have yet to materialize. Market uncertainty and mixed signals are the norm. There are some rumored transactions at cap rates of high nines and low tens in the making-more in line with market expectations. There were few investment sales and cap rates for non credit tenants are approximately the same as last year. However, we note a 7.5 cap investment sale with an 8 year lease at 1467 Fairway Drive, where the 10,250sf property sold for $2,275,000. As the market recovers we anticipate seeing more commercial investment transactions.

A common discussion with local appraisers is that they are looking beyond the local market to find cap rate data. Locally, there is a dichotomy in the market with low cap rates for the credit worthy tenants with good leases or strong locations and higher cap rates associated with investments of lesser quality tenants or locations. For Santa Maria, this would translate to cap rate ranges between approximately 6.5 and 10. This is frustrating for prospective buyers as they assume there is a specific cap rate for the market area. As more sales take place, this broad range should narrow in scope.

Following are capitalization rate ranges evinced over the last six years:

Capitalization Rates
City of Santa Maria Metropolitan Area

	2006	2007	2008	2009	2010	2011
Capitalization Rate Range	6.0 - 7.5	6.0 - 7.5	8.0 - 8.5	8.0 - 10.0	7.0 - 9.5	7.0 - 9.5
Corresponding Valuation* (Millions of $)	1.66 - 1.33	1.66 - 1.33	1.25 - 1.18	1.25 - 1.00	1.42 - 1.05	1.42 - 1.05

Source: Stafford-McCarty Commercial Real Estate

* Value based upon $100,000 annual net operating income

Summary

The market is getting better every day as indicated by transactions occurring. Price stabilization may be starting to happen; as transaction data points create references, those in turn affect the valuation for the next transaction—hopefully creating an upward spiral. As the markets stabilize, we will see the return of notably absent commercial financing.

Santa Maria has key catalysts in place, with significant expansion in medical, agricultural and manufacturing space. 2011 may be seen as a turning point year.

Notes:

For the purpose of this report, databank numbers include functional, non-competitive inventory (older buildings and warehouses) and excludes non-market square footage such as mini-storage, airport hangers, etc.

A Cap Rate (Capitalization Rate) is calculated by dividing the annual net operating income (NOI—which does not include debt service) by the purchase price, e.g. $100,000 NOI/ $1,500,000 purchase price equals .0667 or a 6.67 cap rate.