19NINETEEN
Clarendon Apartments

Arlington, VA

Property Analysis

Presented by: Team USAA

Contents

1. Introduction

Team USAA is an affiliate of USAA Real Estate Company. Our function is to underwrite and analyze potential investment opportunities presented to or acquired by USAA Real Estate. Team USAA performs a completely objective and unbiased analysis for investment opportunities.

This report is the result of our analysis over 19Nineteen Clarendon, a mixed-use midrise apartment building currently under construction in Arlington, Virginia. Team USAA's task in this project is to:

"Analyze the current market conditions and determine the most profitable year of sale."

TEAM USAA

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2. Abstract

Team USAA is excited to present the following memorandum to USAA Real Estate on 19Nineteen Clarendon, a mixed-use midrise proposal currently under construction in Arlington, VA, one of the most sought after areas in the country. The site is located at 1919 Clarendon Blvd in the Courthouse area of Arlington's Rosslyn-Ballston (RB) Corridor and will comprise of apartments and retail. The Rosslyn-Ballston Corridor runs along the Orange Metro Line, one of Washington DC's most accessible subway lines. In addition, Arlington is one of the fastest growing neighborhoods in the DC Metro area and among the best opportunities for development in the country.

In 2007 ZOM Development acquired the 75,573 square foot property on Clarendon Boulevard with the intention of erecting a multi-use apartment building. Due to the financial crisis, ZOM was unable to secure financing and initiate development. ZOM held the property until 2010, when USAA acquired the land and financed construction.

Construction began in May 2010 and is on pace to be completed in December 2013. The development plan included the demolition of the previously existing one-story and three-story brick commercial buildings and the construction of the mixed-use multi-family and retail building, which will be five stories above ground level on the west, and seven stories high on the east due to sloping streets that border the property. The residential space will include approximately 191 apartment units, while the retail space will account for as much as 17,500 square feet of ground floor space. The proposal includes approximately seven units on the ground floor on Clarendon Boulevard that would be designed as flexible space, to be built out as residential lofts or possibly additional commercial space.

The Rosslyn-Ballston Corridor is an exciting area for development as it is a popular and growing neighborhood for young, high-salaried residents with great proximity to key areas of Washington DC. Near the property there is an immediate abundance of restaurants and entertainment that provides a desirable location for potential tenants in both the retail and residential spaces.

The project has inherent risks. These concerns include supply and demand factors in the market, uncertainties specific to the overall design of the structure, and completion of construction. However, as our analysis will show, these concerns can be mitigated and are far outweighed by the economic benefits that this asset creates.

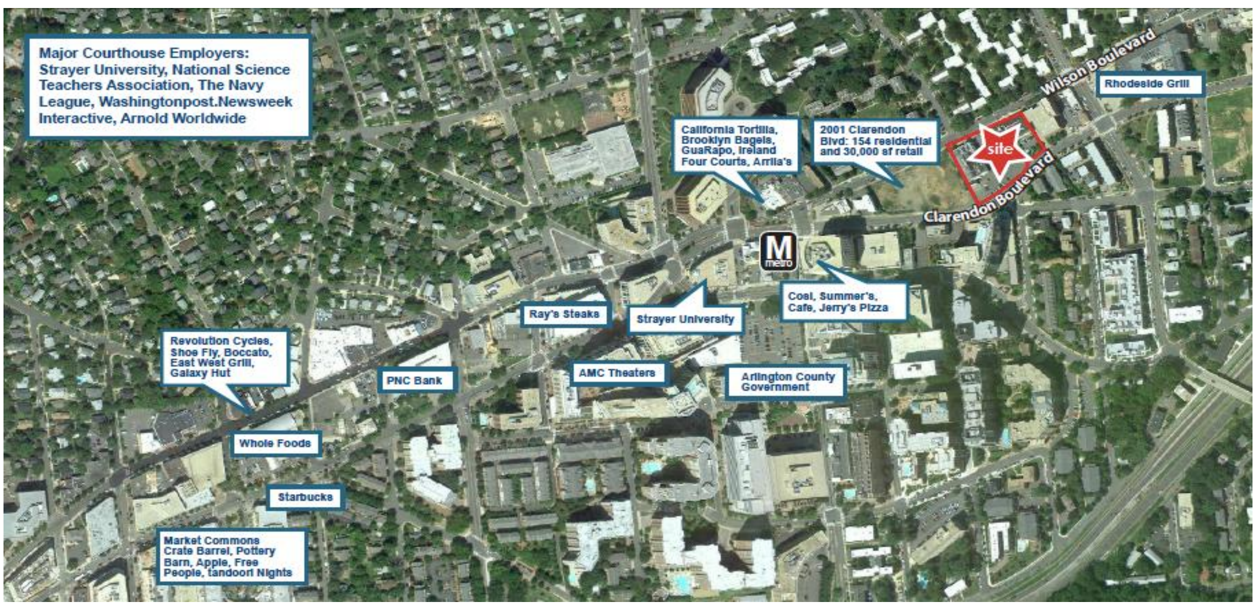
19Nineteen Clarendon presents a profitable and exciting opportunity for USAA. Our analysis shows that current market conditions support the project. Additionally, we calculated potential rates of return for each year of operation over a 10 year span after construction is completed. These rates consistently meet and exceed USAA's required preferred 9% return, and our research suggests that the most profitable period to sell the project would be at the end of the second year of operation, capitalizing third year cash flows.

3. Location and Property Overview

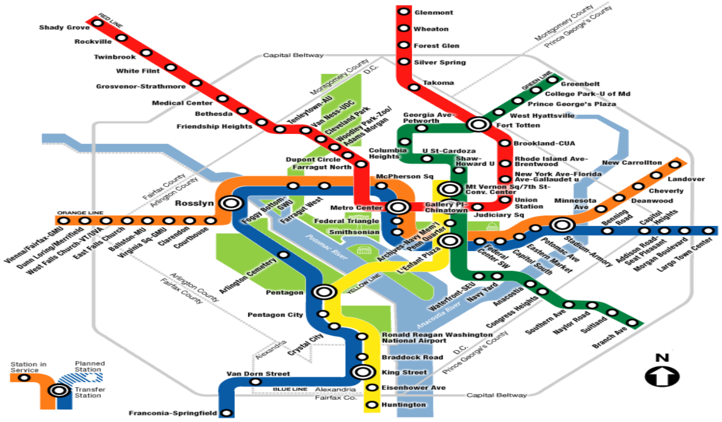
3.1 Overview

19Nineteen Clarendon will occupy prime land in the Rosslyn-Ballston Corridor between Wilson Boulevard and Clarendon Boulevard. The site has excellent accessibility, as Washington DC is only a few minutes' drive across the Key Bridge into the popular Georgetown area, and the Courthouse Metro stop is a short walk. Rosslyn itself is a vibrant, budding region with a wide variety of retail locations.

The proposed development will cover 75,573 s.f. of land. The final project will account for 168,300 s.f. of residential space and 17,500 s.f. of total retail. The building's design consists of a concrete platform and 5 levels of wood frame construction on top, giving the project both a Type I and Type 5A design rating.



The structure will be five stories high at the west end and seven stories high at the east end. Five retail bays will run along the ground floor bordering Wilson Boulevard, while the ground level along Clarendon Boulevard will consist of one space designated for retail and loft apartments ranging from 23 to 26 feet high. One retail bay and 23- 26' high loft apartments will face Clarendon.



3.2 Accessibility and Demographics

19Nineteen Clarendon has great accessibility as it is situated between Clarendon Blvd and Wilson Blvd, which are the two main roads of the Rosslyn-Ballston corridor. The site is located within a quarter mile or a 4 minute walk from the Courthouse metro station on the Orange line.

The Courthouse area of Arlington, Virginia is densely populated with high-income earners. Within a mile radius of 19Nineteen Clarendon, there are 34,832 residents with an average household income of \$94,353 and a daytime population of 30,918. Within five miles, there is a population of 664,457 with an average household income of \$97,898 and a daytime population of 758,799.

3.3 Adjacent Land Use

The properties surrounding 19Nineteen Clarendon are mostly residential and mixed-use developments with a number of retail locations. A series of restaurants runs along Wilson Boulevard between our site and the Arlington Courthouse Metro Station, including California Tortilla, Brooklyn Bagels, GuaRapo, Arrita's, and Ireland Four Courts.

The property immediately adjacent to the west of 19Nineteen Clarendon is currently under construction. This development is intended to be a mixed-use building similar to USAA's project. The developer Elm Street is underway on a 200-unit apartment building, which will incorporate ground floor retail. Construction is approximately six months behind the intended schedule of 19Nineteen Clarendon with leasing predicted to begin in June.

Other comparable multifamily properties within the Courthouse and Rosslyn area of the Rosslyn-Ballston Corridor that may be considered competitors include:

- 2201 Pershing
- Garfield Park
- Grayson Flats
- Lyon Place The Clarendon
- The Palatine
- The Residences at The Market Common
- Zoso Flats

3.4 Site

Improvements to the site include the need for land grading, addressing soil issues, and dealing with pre-existing land complications due to previous uses.

Due to descending terrain, the property required grading so that the foundation could be implemented properly. This results in one end of the building being five stories high and the other is seven stories high. It also provides for impressive views to the east of the building, but restricted views to the west.

Before the site became a Hollywood Video, it was a gas station. The general contractor discovered soil contamination during environmental testing caused by underground gas tanks that were never excavated. This discovery required extensive testing and cleaning performed by the county, to which the costs were incurred by the developer. A team of specialists were brought in by the Arlington County Government to resolve the contamination, and the site is currently in prime condition for development.

3.5 Zoning

The land was rezoned from C-2 and RA8-19 to C-O-2.5, or commercial office building, hotel and apartment districts as part of the Arlington County 4.1 process. This process is a standard way of obtaining more density and relief from certain zoning requirements in exchange for significant proffers related to affordable housing, LEED requirements, traffic fees, green space fees, and art fees.

The regulations for C-O-2.5 zoning are as follows:

A. Uses Permitted

Permitted uses for the site include office buildings, commercial uses including retail and service commercial uses, hotels and apartment buildings: Any building or group of buildings may have mixed office, commercial uses including retail and service commercial uses, apartment or hotel uses, as follows, but no part of any site shall be used more than once in calculating its permitted density of use. The amount of the site required for a given office, commercial and/or institutional floor area is determined by dividing the total amount of gross floor area for such uses by 2.5; the balance of the site is available for hotel and/or apartment use. The specific uses and the maximum density permitted by site plan approval shall be as follows:

Ratio of maximum office and/or commercial floor area to site area 2.5:1

Maximum apartment units per acre 115

Maximum hotel units per acre 180

Hotel meeting rooms and restaurants may be permitted to exceed the above density by site plan approval.

B. Height Limit

By site plan approval: No building, excluding penthouse area, shall exceed twelve (12) stories for office buildings and sixteen (16) stories for apartment and hotel buildings. Parapet walls may be extended upward to screen a penthouse. This area shall not be counted as a story but may be enclosed and used for elevator, mechanical and maintenance equipment, private clubs, auditoriums, meeting rooms and restaurants. All permitted penthouses use shall be limited to one (1) floor. Elevator service to the penthouse level may be considered in support of an approved penthouse use.

C. Area Requirements.

Each lot or plot shall have a minimum average width of one hundred (100) feet and a minimum area of twenty thousand (20,000) square feet. The County Board may authorize application for rezoning to the "C-0-2.5" District where a lot or plot having less width or less area which [sic] is any part of a block surrounded by streets and/or buildings that generally comply with the provisions of this section.

The 4.1 process and proffer allowed ZOM to add additional density to the site than what is allowed under current zoning. 19Nineteen Clarendon will have a FAR of 4.1. Otherwise, the development conforms to the zoning requirements.

3.6 Improvements

Troy Street will be constructed to separate 19Nineteen Clarendon from the neighboring site to the west known as 2001 Clarendon Blvd. The development will consist of five separate retail bays, approximately 191 residential units averaging 850 s.f., as well as two levels of below grade parking.

The retail space will primarily be set along the ground floor of the northern façade of the development, running along Wilson Boulevard. Four bays of different sizes - 3,120 s.f., 1,941 s.f., 4,393 s.f., and 3,928 s.f. - will make up most of the retail area for the site. One retail bay of 4,029 s.f., however, will be set at the SW corner of the development, facing Clarendon Boulevard and Troy Street.

The residential units will be a mix of loft, studio, one bedroom, two bedroom, and three bedroom units. The ground floor units will be the only lofts in the development, running along Clarendon Boulevard between the lobby and the east alley entrance for the parking garage. These units will be the developments highest residential spaces with 23’ to 26’ ceilings, including 9’lofts. The next three floors will be approximately 10’8’’ high apartments, and the top floor ceilings will reach about 9’.

The parking structure will provide a total of 257 spaces for residential and retail use. The lower parking level (G2) will provide 123 spaces exclusively for residential use. The mid-level (G1) will offer 62 for residential use and 64 for retail use. Finally, the retail lobby will include 8 additional spaces to maximize parking capacity.

As previously mentioned, Elm Street is developing the adjacent property to the west. Due to the eastern sloping grade, the prospective building developed by Elm Street may overshadow USAA’s project, restricting its western exposure to sunlight and damaging its marketing potential. Fortunately, that development is not set to be completed until June of 2014, six months after 19Nineteen Clarendon’s completion date, so USAA’s project will have that time between its completion and the completion of this competitor for marketing.

For elevations, see Exhibit 1.1, Pg 20. For ground floor layout and typical floor plan, see Exhibit 1.2, Pg 21

3.6.1 Site Acquisition

The property at 1919 Clarendon was originally purchased by ZOM in 2007 and acquired from ZOM by USAA in 2010. Construction began in May of that year.

3.6.2 Land Costs

There are two approaches that were utilized to appraise the market value of the land:

1) Land value appraisal provided by the Arlington County Department of Real Estate Assessment

2) Comparable land sales in Rosslyn-Ballston Corridor in Arlington, VA.

The formula to determine the land cost is based on the following factors:

1) Sales Comparison Approach: properties that have recently been sold that are comparable to the property

2) Income approach: The discounted income a property would produce if it were rented as an apartment

According to Arlington County Appraisal, the following chart shows the comparable land sales just near our lot.

Arlington Land Cost			
Development	**Address**	**Lot Size**	**Value**
1200 N Irving Street	1200 N Irving Street	51,902 s.f.	$14,742,900.00
The Palatine	1301 N Troy Street	67,953 s.f.	$20,390,000.00

According to Arlington County's appraisal, the average cost of land is approximately 284 dollars per s.f. as of Jan 2012. Considering the location factor, we estimate the value of land for 19Nineteen Clarendon is approximately 315 dollar per s.f.. The total site area of our land is 75,573 sq.ft. Therefore, we consider the land cost is about $ 22.6 million.

3.6.3 Hard Costs

Based on the construction type, the hard cost for residential is about $175,000 per unit for 191 units. Therefore, total hard costs for the residential portion are about $33,425,000. The hard cost for retail is about $3,575,000, giving a total hard cost for the entire project of approximately $37,000,000.

3.6.4 Soft Costs

Soft costs for the project include fees for architectural design, engineering, permitting, legal fees and other indirect costs involved with the development. The total for these costs is $11,100,000, which is roughly 24% of total development costs.

3.6.5 Parking

There are 64 spaces for retail parking and 193 spaces for residential parking. The construction costs for parking space is included in hard cost.

Combining these numbers gives a total development cost of $71,905,495. The breakdown is further illustrated in the table in the next section.

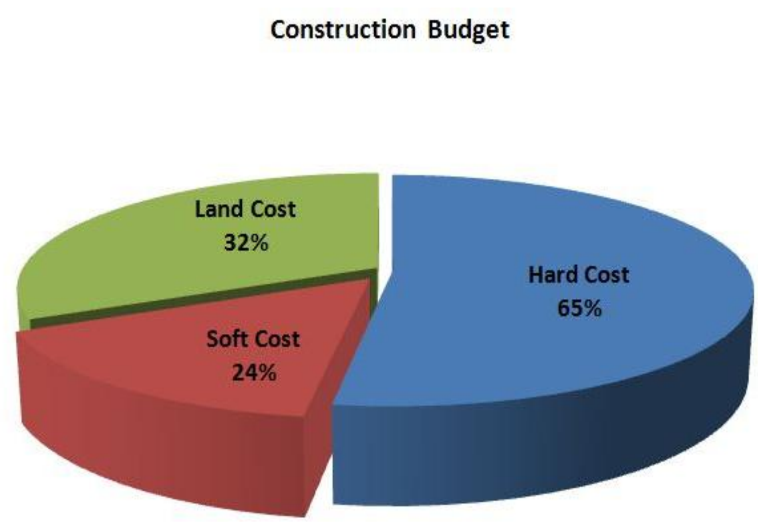
3.7 Mix-Use

<table>
<tr><th colspan="6">Mix-use of Nineteen19 Clarendon</th></tr>
<tr><th></th><th></th><th>Total Units</th><th>Total Space</th><th>Total Space</th><th>Average Unit Space</th></tr>
<tr><td rowspan="5">Retail</td><td>Space 1</td><td>1</td><td>4,029 s.f.</td><td rowspan="5">17,465 s.f.</td><td rowspan="5">3,493 s.f.</td></tr>
<tr><td>Space 2</td><td>1</td><td>3,982 s.f.</td></tr>
<tr><td>Space 3</td><td>1</td><td>4,393 s.f.</td></tr>
<tr><td>Space 4</td><td>1</td><td>1,941 s.f.</td></tr>
<tr><td>Space 5</td><td>1</td><td>3,120 s.f.</td></tr>
<tr><td rowspan="9">Multifamily</td><td>Studio</td><td>22</td><td>523 s.f.</td><td>11,506 s.f.</td><td rowspan="9">811 s.f.</td></tr>
<tr><td>JR 1 Bed</td><td>16</td><td>606 s.f.</td><td>9,696 s.f.</td></tr>
<tr><td>1 Bed</td><td>84</td><td>728 s.f.</td><td>61,152 s.f.</td></tr>
<tr><td>1 Bed + DEN</td><td>16</td><td>875 s.f.</td><td>14,000 s.f.</td></tr>
<tr><td>1 Bed FLEX</td><td>7</td><td>1,072 s.f.</td><td>7,504 s.f.</td></tr>
<tr><td>MEZZAN</td><td>1</td><td>1,379 s.f.</td><td>1,379 s.f.</td></tr>
<tr><td>2 Bed</td><td>34</td><td>1,055 s.f.</td><td>35,879 s.f.</td></tr>
<tr><td>2 Bed + DEN</td><td>8</td><td>1,255 s.f</td><td>10,040 s.f</td></tr>
<tr><td>3 Bed</td><td>3</td><td>1,477 s.f</td><td>4,431 s.f</td></tr>
</table>

3.8 Budget and Construction

The overall development budget, including costs for construction, soft costs, and cost of land is approximately $71 million. USAA has secured a loan for 65% of the total development budget, which amounts to approximately $46 million. The remaining required equity of $24.7 million has been covered by USAA and ZOM Development. USAA has committed 95% ($23.5 million) of the required amount and ZOM has provided the remaining 5%, or $1.2 million.

Investment Breakdown	
Hard Cost	$ 37,000,000
Soft Cost	$ 11,100,000
Land Cost	$ 22,671,900
Development Cost	$ 70,771,900



The design of the building incorporates Type I concrete and Type VA wood. Integrating timber into the design allows between 15-30% cost efficiency in construction. The maximum vertical build up using wood framing is five stories, and this type of design comes with its own problems according to the contractor:

- More technical form of construction
- Additional rules and regulations to adhere to

- More specific design requirements as mistakes cannot be fixed later, and
- Increased fire hazard (must allow for a three hour burn time through building)

Another unique cost built into the budget is Harkins compliance with requirements for LEED for Multi-Family: Midrise. This standard of building is the USGB's recent certification process specifically for residential developments between four and eight stories high. Points of focus for approval include:

- Innovation and Design Process
- Location and Linkages
- Sustainable Sites
- Water Efficiency
- Energy and Atmosphere
- Materials and Resources
- Indoor Environmental Quality

The standards for qualification under these focuses are specific to the category of development that 19Ninteen Clarendon falls under. The property is expected to achieve LEED Silver, with a possibility of obtaining LEED Gold. Achieving these certifications helps to maintain a healthy and sustainable neighborhood environment by improving the impact and operating efficiency for the building, resulting in lower operating costs, and increases the appeal to retail and residential tenants alike.

Exhibit 1.1

Site Elevations

A. North Elevation – Wilson Boulevard

B. South Elevation – Clarendon Boulevard

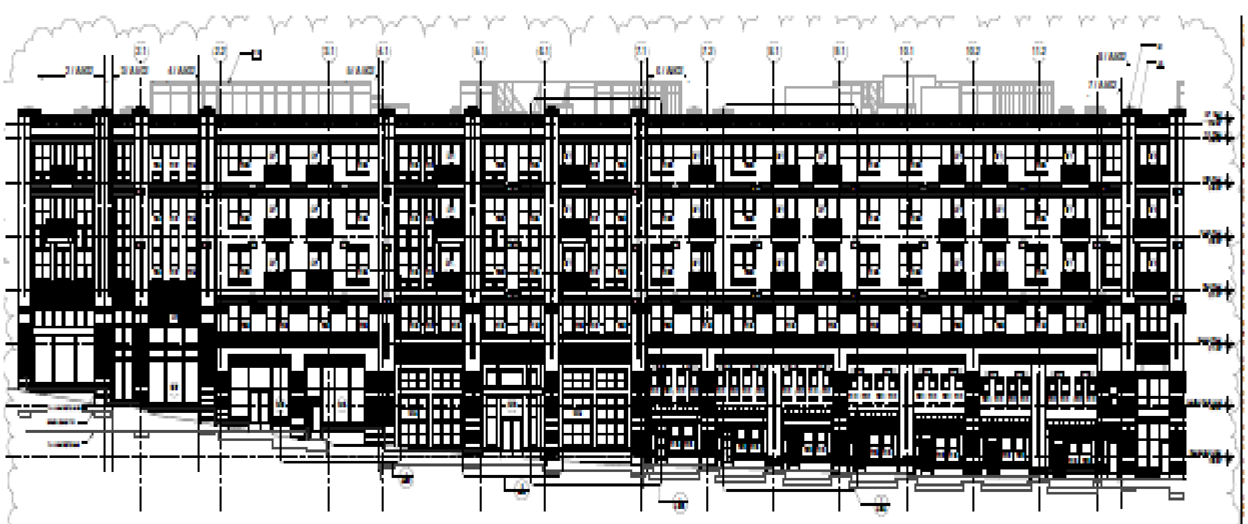
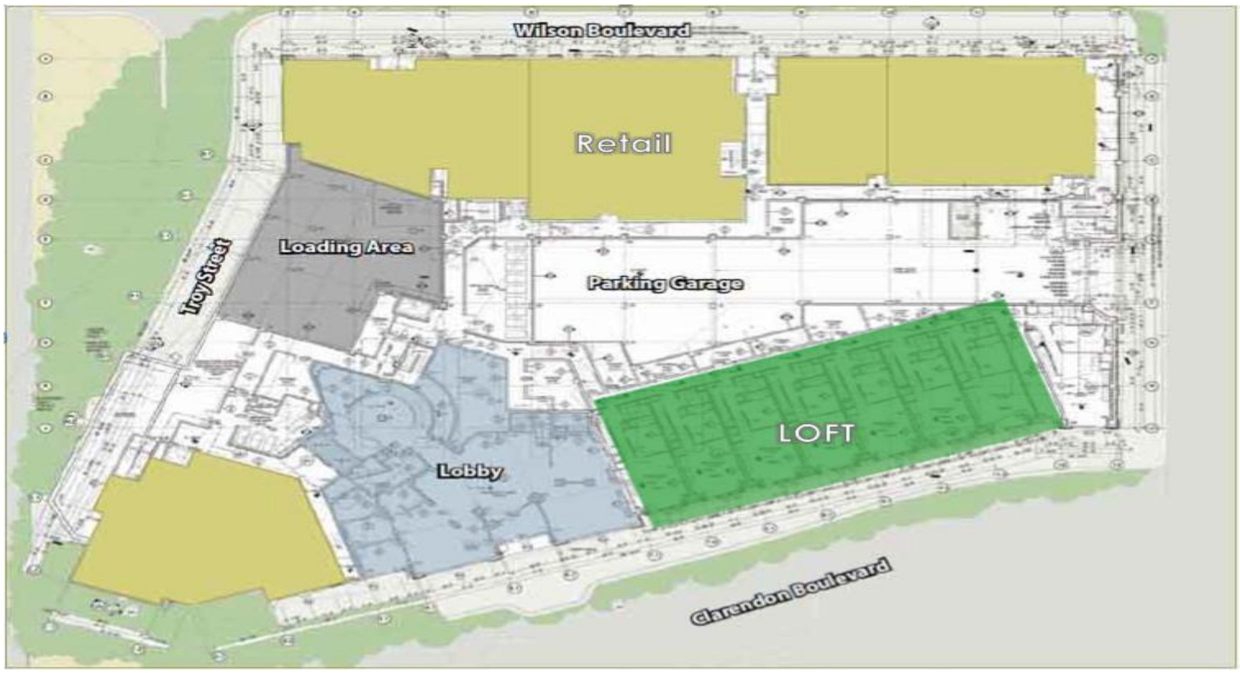


Exhibit 1.2

Floor Plan

A. Ground Floor



B. Typical Floor Plan

4. Development Team and Associates

4.1 Overview

In 2010, USAA joined ZOM as a capital partner, investing the required financing to get development moving again. As it stands, construction is set to be completed in December of 2013.

4.2 Development and Management

The developer behind 1919 Clarendon is ZOM Development, LLC (ZOM), who purchased the property and will be the property manager upon completion through their affiliate ZRS Management, LLC (ZRS). ZOM is one of the most highly regarded multifamily development companies in the United States. The company has joint ventured or directly developed over 11,000 apartments and has garnered over 60 industry awards, including National Multifamily Development Firm of the Year (NAHB) in 1999.

4.3 Investing Partners

USAA Real Estate and ZOM Development are the two equity partners. The USAA Real Estate Company is the real estate investment arm of USAA with over $12 billion in assets under management. They contributed a $46 million loan for construction and 95% of the remaining equity. ZOM provided the other 5% required funding. ZOM’s property management branch is ZRS Management. ZRS will manage 19Nineteen Clarendon after construction is completed. ZRS is known nationally as a leader in the property management field. ZRS currently manages over 24,000 units for various clients.

The developers are partnering with established and reputable companies. It is especially important that these companies have experience on the Washington area developments.

4.4 General Contractor

The general contractor is Harkins Construction. Founded in 1965, Harkins is an industry leader in providing professional preconstruction and construction management services for clients with negotiated and design-build projects, ranging from commercial mixed-use properties, student housing, multifamily, and even military site developments.

Harkins also built the following DC area properties:

The Allegro Apartments, Washington DC

- Vibrant Columbia Heights area
- Features 297 residential units
- Street level retail

Ashbury Courts, Laurel MD

- First project in Howard Counties Rout 1 Revitalization Initiative
- 140 residential units
- 1st floor retail

The Jordan, Arlington VA

- 90 residential units

Twinbrook Station Phase 1A, Alaire

- Transit oriented development, 26 acres around Twinbrook Metro Station
- 1595 multi-family residential units
- Washington’s first LEED Gold Neighborhood Development (LEED-ND)

These projects are among to most profitable and well known landmarks in the mixed-use market in the Washington DC metro area. The concept behind 19Nineteen Clarendon should mirror the level of efficiency and innovation that Harkins has installed in its other landmark projects.

4.5 Design Team

The developer ZOM also partnered with an outstanding architecture and design team at Torti Gallas and Partners, Inc. Torti Gallas has had a lot of experience developing the Washington DC area suburbs.

This firm specializes in designing residential, commercial, and institutional buildings. Torti Gallas focuses on environmentally cohesive aesthetics, and they pride themselves on social responsibility.

They also have extensive expertise in critical areas of modern design, such as sustainability, new urbanism, and revitalization.

Comparable projects that Torti Gallas designed in Washington DC include:

The Ellington (under construction)

- U Street Corridor
- E-shaped, three wing design

Park Place (under construction)

- Five levels residential, apartments and townhouses
- First new apartment project along Georgia Avenue in decades

City Vista

- Project awarded through RLA Revitalization Corporation
- Safeway and Starbucks included in retail level

Torti Gallas was founded in 1953 and has designed more than 300,000 residential units in the Washington Metropolitan area. They've received over 400 international, national, and local design awards for planning and design from groups like AIA, the American Society of Landscape Architects, and the National Association of Home Builders. A few of these achievements include the National Planning Achievement Award for their Crystal City Master Plan project in 2013, the Energy Star Leadership in Housing Award in 2011, as well as the NAHB Pillars of the Industry Award for Best Mid-Rise Apartment Project in 2009, awarded for the Highland Park design in Washington DC. The exhibit 2.1 (pg 26) addresses the members in the design consultant team.

Exhibit 2.1

Role	Company
Civil Engineer	Bowman Consulting Group
Utility Consultant	Richer & Associates
MEP	WSP, Flack &Kurtz
LEED Provider	Architectural Energy Corporation
Structural	SK&A
ADA Review	ACA/Pete Skarzenski Consulting
Landscape Architect	Mahan Rykeil Associates, Inc
Waterproofing/Exterior	Simpson Gumpertz & Heger
Interior Design	RD Jones & Associates
Architect	Torti Gallas and Partners Inc

5. Market Analysis

As multi-family space is the major component of this project, our market analysis was focused solely on the residential supply and demand factors.

5.1 Market Overview

Analysis of the Rosslyn-Ballston Corridor submarket included calculation and forecast of supply and demand in the present and in the foreseeable future to determine whether the market will support the potential development of this multifamily building.

5.2 Washington DC Metropolitan

The examination will look at the Washington metro area as a whole, specifically the general economic conditions, occupancy, supply, demand, and rental rates in the area. Additionally, there is a more specific market analysis of Arlington and the Rosslyn-Ballston Corridor to see how the opportunity stands up to a more narrow analysis.

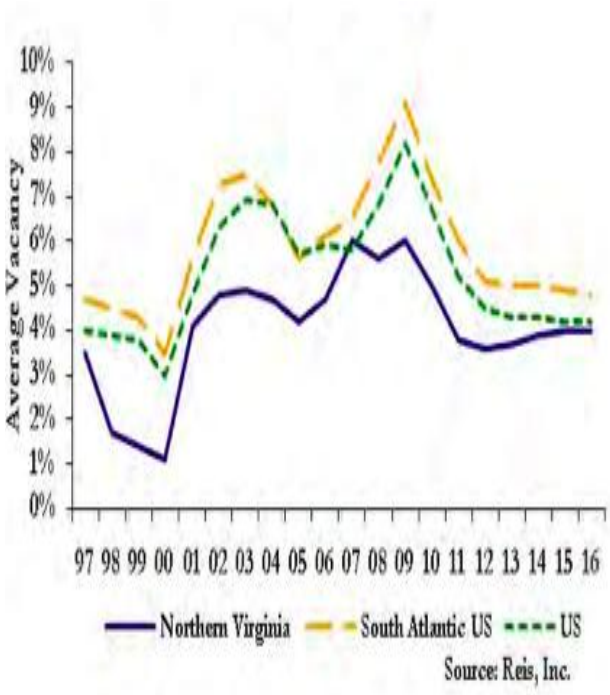
5.2.1 The Economy

The Washington DC Metro Area is reputed for having one of the most stable core commercial real estate multifamily markets in the United States. As home to the Federal Government, Washington has maintained steady growth historically and has proven to be less vulnerable to cyclical economic swings than the nation's other major cities. During the past few decades, Washington has maintained one of the country's strongest economies with high-wage jobs and a low unemployment rate.

According to Holiday Fenoglio Fowler, L.P, the apartment market of the Washington DC area has some unique advantages over competing cities:

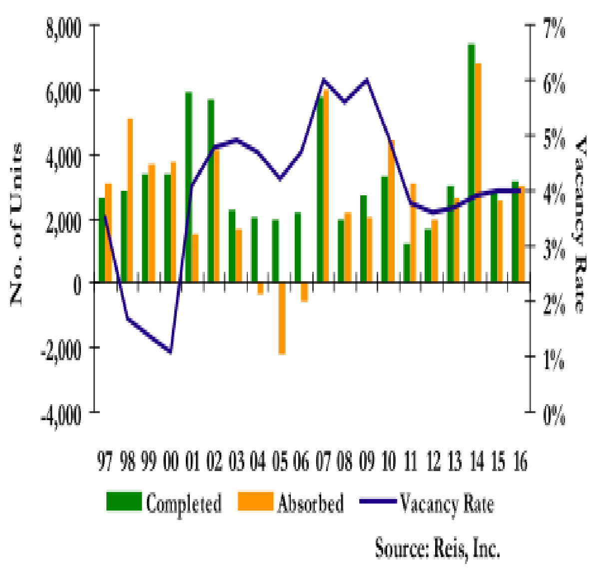
1. The DC area has 6 of the nation's top 10 educated counties with 47% of the population receiving a bachelor's degree and 22% receiving a graduate degree.
2. Because of the strong high-salary employment growth, the population of DC area continues to increase, which produces a strong demand for apartment buildings.
3. According to Moody's Economy.com, the "total employment rate" increased by 1.3% in 2011 and 1.2% in 2012, which shows a strong recovery from the recession.

5.2.2 Occupancy



The adjacent figure shows that the vacancy rate in Northern VA increased from 1997 to 2010 and decreased sharply from 2010 to the current year. According to forecasts made by Reis, Inc., the vacancy rate will level off at about 4% for the next 3 years. Additionally, Northern Virginia multifamily residential market finished the first quarter of 2013 with a vacancy rate of 3.8%. As the vacancy rate is below 5.0%, the market is considered fully occupied. Compared with vacancy rate in South Atlantic US and US average, the vacancy rate in Northern VA remains consistently low.

5.2.3 Supply and Demand



During 2007 to 2011, there were nearly 15,000 units completed in the Northern Virginia apartment market, averaging 2,984 per year. The net absorption is 17,738 in that period, which helped to keep the vacancy rate at a low level. According to the Reis report and seen in the figure above, the vacancy rate will maintain a low level of 4.0% from 2013 onward and indicates a strong demand in that market.

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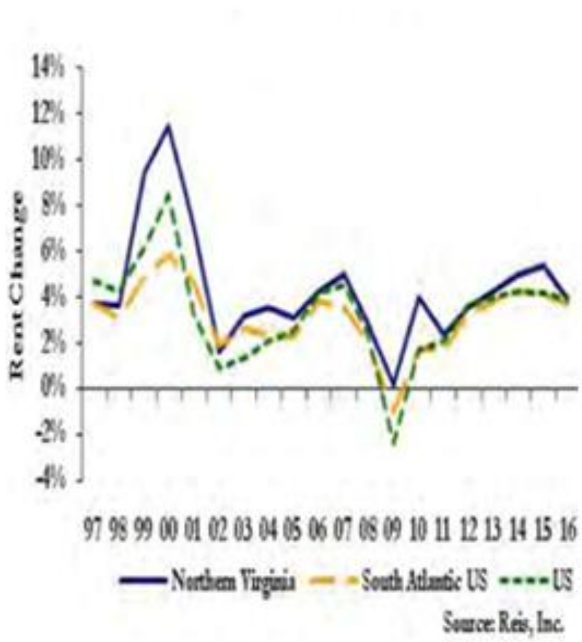
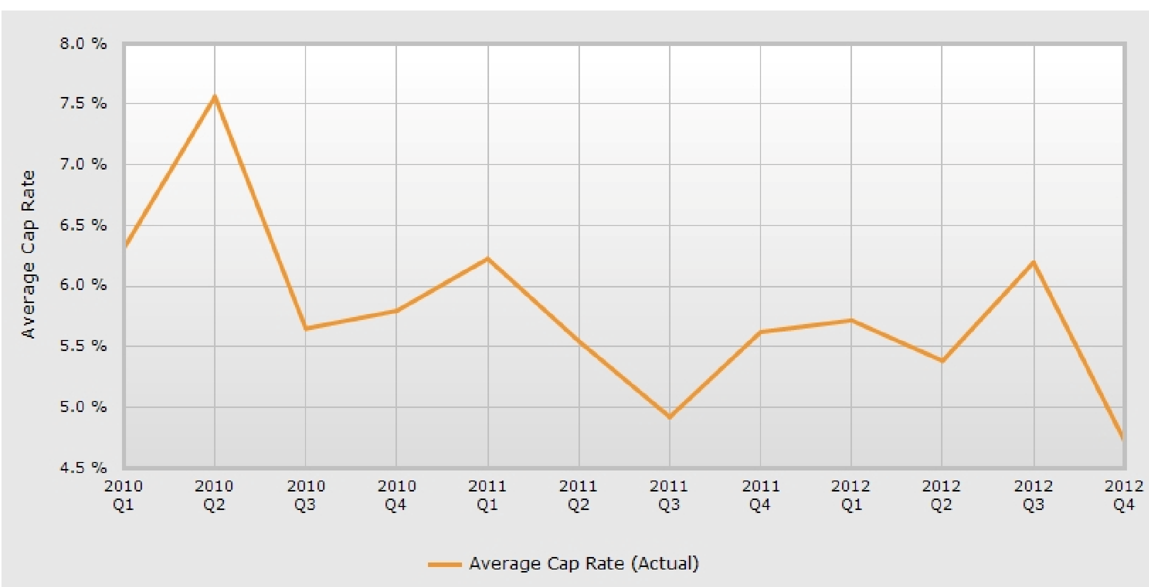
5.2.4 Rents



In the third quarter 2012 Northern Virginia multifamily residential market, the average asking rent was $1,565 per month and the effective rent was $1,525 per month. These two rates were 0.9% and 1.3%, respectively, more than those of the previous quarter and 3.3% and 4.0% above the previous years. Traditionally, a 1.0% rent growth for a single quarter is an indication of a healthy market. As seen in the figure above, from 1997 to 2012 the residential market rent growth of Northern Virginia was consistently higher than the national average, and this pattern is expected to continue.

5.2.5 Capitalized Rate



The cap rate for multifamily buildings in the Washington DC market was around 5%-7% from September of 2010 to January of 2013 based on data from Costar. Compared with other leading markets in U.S, this cap rate is relatively low. As of December 2012, the cap rate in Washington is lower than 5%, which indicates a highly optimistic multifamily market. This cap rate is expected to remain at 5% for the near future.

5.3 The Rosslyn-Ballston submarket

5.3.1 Introduction

The Rosslyn-Ballston corridor submarket has nearly half the population of Arlington County and the majority of demand. Rosslyn-Ballston has the third most inventory units (17,189) and the second highest asking rent ($1,943) of the 15 Arlington County submarkets. As of the 4th quarter of 2012, Rosslyn-Ballston has 2,408 apartment units under construction and 2,086 apartments proposed for development.

5.3.2 Submarket Future Trends-Rent

According to Reis's report of the Q4 2012 Rosslyn-Ballston apartment market, the rent range is likely to be between $1,943 and $2,392. Compared to the previous quarter, rent growth is likely to be about 0.0%-1.9%.

Rent Growth Comparisons							
	Asking Rent Growth						
	Quarterly			Annualized			
	4Q12	3Q12	YTD Avg	1 Year	3 Year	5 Year	5 Yr Forecast
Rosslyn/Ballston	0.8%	1.0%	0.6%	2.5%	3.1%	2.2%	2.5%
Suburban VA	0.6%	0.9%	0.8%	3.3%	3.2%	2.5%	4.4%
South Atlantic	0.6%	0.8%	0.7%	2.9%	2.1%	1.5%	3.6%
United States	0.6%	0.8%	0.8%	3.1%	2.2%	1.4%	3.8%
Period Ending	12/13/12	09/30/12	12/31/12	12/31/12	12/31/12	12/31/12	12/31/17

(Source: REIS)

The rent growth of the Rosslyn-Ballston residential market in the last 5 years has been between 2.2%-3.1%, which is higher than the national average level of 1.4%-3.1%.

5.3.3 Submarket Future Trends - Vacancy

In Q4 2012, the vacancy rate in most of the properties in Rosslyn-Ballston was under 5.5% and the stabilized vacancy rate in the next 5 years will be around 5%.

5.3.4 Marginal Demand Calculation

Multifamily Demand Calculation			
Demand Category	Current Year	Year 5	Data Source/Comment
Population Forecast	99,861	105,007	Reconciled Forecast
Potential Demand got apartment units	42,535	44,727	Calculation
Multifamily Market Area Demand	24,755	26,030	Calculation

From the calculation above, we determined that there is a current demand for 24,755 units in the market area and potential for a 26,030-unit demand in five years. We forecasted these numbers by researching the current and future estimated population, calculating how much of the housing market consists of apartment units of the same type and class as 1919 Clarendon.

These data points provide the total demand for multifamily apartment units that this project can potentially absorb in this particular market.

5.3.5 Supply and Marginal Demand

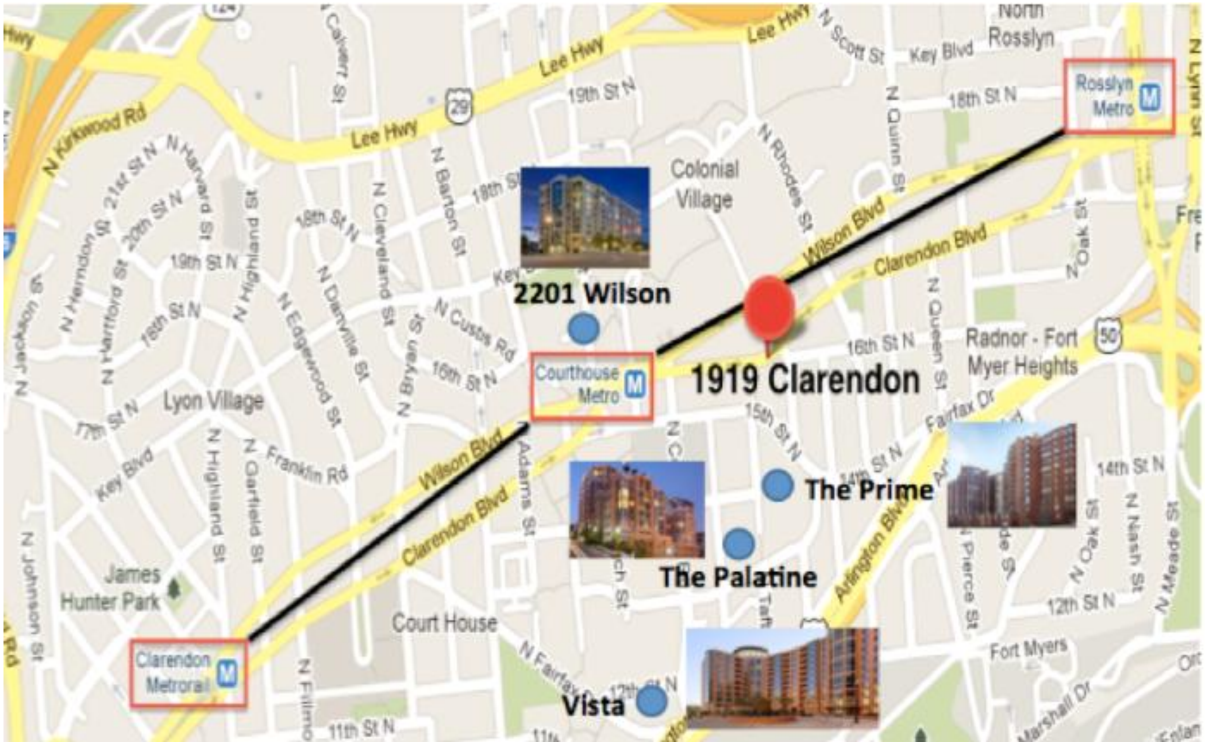
Multifamily Supply and Marginal Demand		
	Current Year	**Year 5**
Supply Net of Frictional Vacancy	18,617	21,095
Total Forecast Demand	24,755	26,030
Supply Net of Frictional	18,617	21,095
Marginal Demand	**6,137**	**4,936**

There are currently 17,189 units of existing competitive space in the Rosslyn/Ballston Corridor, with 19,597 units estimated in 5 years. There are approximately 2,408 units under construction at the time of analysis, with about 2,608 that are currently proposed. With consideration of frictional vacancy in the area (4%), current supply of apartment units in the market lies at 18,617 units presently, and 21,095 forecasted for 2019.

The goal for the supply and demand analysis of similar units in the Rosslyn-Ballston Corridor is to calculate marginal demand for units in the market area. The marginal demand suggests whether the current and forecasted market is one that can provide adequate absorption for the amount of units available to potential tenants. Based on our findings, the market as of 2013 provides a marginal demand of 6,137, which suggests demand greatly exceeds supply. In 2019, the estimated demand exceeds supply by 4,936 required units. Overall, the area promises adequate and attractive absorption currently and in future years.

5.4 Competitive Properties

The figure below shows the Rosslyn-Ballston corridor and the properties we consider competitors to 19Ninteen Clarendon. .



	**The Palatine, 1301 N. Troy Street** Arlington VA Neighborhood: Courthouse Distance from site: 0.2 miles Units: 262 Project Type: Apartment Status: Delivered, Leasing Up
	**The prime, 1415 North Taft Street** Arlington VA Neighborhood: Courthouse Distance from site: 0.1 miles Units: 256 Project Type: Apartment Status: Delivered, Leasing Up

	**Grayson Flats, 1200 N. Rolfe Street** Arlington VA Neighborhood: Courthouse Distance from site: 0.4 miles Units: 67 Project Type: Apartment Status: Delivered, Leasing
	**2001 Clarendon Boulevard** Arlington VA Neighborhood: Courthouse Distance from site: 108 ft Units: 154 Project Type: Apartment Status: Under Construction
	**The Tellus, 2009 14th street North** Arlington VA Neighborhood: Courthouse Distance from site: 0.1 miles Units: 254 Project Type: Apartment Status: Under planed

	**Sedona & Slate, 1510 Clarendon Blvd** Arlington VA Neighborhood: Rosslyn Distance from site: 0.5 miles Units: 262 Project Type: Apartment Status: Under construction
	**Archstone Virginia Square, 901 N. Nelson St.** Arlington VA Neighborhood: Virginia Square Distance from site: 1.4 miles Units: 231 Project Type: Apartment Status: Delivered, Leasing
	**Archstone, 2201 Wilson Blvd** Arlington VA Neighborhood: Courthouse Distance from site: 0.3 miles Units: 219 Project Type: Apartment Status: Delivered, Leasing

Current competitors are The Palatine, The Prime at Arlington Courthouse, The Tellus, 2201 Wilson Blvd, Grayson Flats, the Sedona & Slate and Archstone Virginia Square. Their current asking rents range from $2,095 per month to $2,904 per month.

Competitors currently under-construction include Sedona & Slate, a nearby high-rise residential project across developed by the JBG Companies

2001 Clarendon is the main competitor as it is located immediately adjacent to 1919 Clarendon and is similar in use and size. In the following figure, 1919 Clarendon can be seen outlined in red, whereas 2001 Clarendon is highlighted by blue. The rival project is scheduled for completion in the June of 2014, six months after our scheduled completion in December. This six month window is a crucial lease-up period. That being said, research shows strong demands and the fantastic timing.

Property Name	Type	Total Sizes (Units)	Structure	Est. Completed	Count
1919 Clarendon	Apartment	191	Wood	Dec 2013	Arlington
2001 Clarendon	Apartment	154	Steel	June 2014	Arlington

5.5 Summary

19Ninteen Clarendon is an excellent development with a great location and fortuitous timing. Population and employment are two major components to the rise in demand for housing, and they continue to increase.

The area is also a vibrant and popular location for the young professional target market that this development hopes to tap into. Retail and transportation amenities, such as numerous bars and restaurants, and convenient metro locations as well as being a short drive to the downtown DC area continue to attract this demographic to the area

Other strong signals, such as rising rental rates and low vacancy, currently at 4% in this submarket, create even more optimism.

The demand for units that 19Nineteen Clarendon will provide should continue to exceed supply. The Washington DC market is more stable than most around the country. Additionally, the Rosslyn-Ballston corridor, as well as the overall Arlington market, has outperformed all other suburban DC office markets over the years, and this strength is projected to continue.

6. Risk and Return

6.1 Return

6.1.1 Equity and Investment Structure

The proposed investment is structured as two separate financing instruments; a fixed-rate first mortgage and an equity joint venture between USAA and ZOM. USAA has self-financed by providing a $46,738,572 amortizing loan, which bears an interest rate of 4% with a 30-year term and a five-year prepayment prohibition.

USAA also provided an equity contribution of $23,531,657, which accounts for approximately 95% of the required equity investment. They guarantee to fund any negative cash flow for a period of 24 months. The original owner ZOM is the developer and has contributed the remaining 5% of required equity, which amounts to $1,238,508. As part of the development agreement, ZOM has a promoted interest in the property described in detail in Part III - Return Structure, of this section.

6.1.2 Pro Forma

The graphs and cash flow attached in the appendices show all potential income and expenses in the 11 years discounted cash flow analysis.

Residential rental rates are projected at $37.20 per s.f. every year with an inflation rate of 3.00%. The residential area is approximately 155,578 s.f.. Retail rental rates are projected to return $35.00 per s.f. annually with an inflation rate of 3.00%. This rate for retail rent is conservative and is aimed at promoting quick lease-ups for the retail space. The retail area is approximately 17,500 s.f., and the total operating expense rate is projected at 30% of effective gross revenue with an inflation rate of 3.00%. The vacancy allowance of 3.8%, and total operating expenses of 30% will be deducted from the gross income to get the net operating income for years one through 11. There are a total of 193 parking spaces for residential tenants and 62 parking spaces provided for retail space. Retail parking spaces will be free to customers, while residential parking spaces will be charged at $90 per month with an expected occupancy of 80%. Assumptions are further explained in Exhibit 3.1 on page 52.

Effective gross revenue in the first year of operation is projected to reach $1,558,527. Total operating expenses would be deducted from effective gross revenue to get net operating income, which ranges from $1.08 million at the end of year 1 to $5.65 million at the end of year 11 (Exhibit 3.2, pg. 53).

According to the year 2012 investment report of comparable properties near the Courthouse Metro Station, we were able to find assumptions of operating expense rates that we are confident are accurate and applicable to what 19Nineteen Clarendon will experience (Exhibit 3.1 pg 53). The total operating expenses consist of controllable operating expenses and fixed operation expenses. For example, during year one, the total operating expenses account for $457,507, in which the total controllable operating expense is $241,728 and the total fixed operating expense is $233,779.

In order to calculate the overall value of the property, a cash flow analysis was completed with income and expenses escalated at a constant growth of 3.00% up to and through the year 2022. The reversion value at the end of tenth year is calculated by dividing the NOI of achieved during the projected 11th year of operations by the terminal cap rate of 5.00%. The reversion value at the end of year 10 is more than $115 million. The selling cost is 3.00% of the reversion value and the loan balance at the end of tenth year is $3,171,998. After subtracting the selling cost and outstanding loan balance, the net proceeds are approximately $52.6 million.

6.1.3 Return Structure

USAA contributed 95% of the equity in the project but will pay ZOM a development fee plus an increasing interest in the cash flows. The equity partner structure is listed as follows:

Joint Partner	Percentage funded	Equity Required	Reversion Payout
USAA	95%	$23,908,577	95%
ZOM	5%	$1,258,346	5%

USAA has a preferred return of 9%. Any return above 9% will be split with ZOM, even though ZOM has not contributed equity to the investment. The split between USAA and ZOM will occur for returns above 9% as follows:

Joint Partner	**Preferred Return**	**1st Distribution (9%-14%)**	**2nd Distribution (14%-18%)**	**3rd Distribution (Above 18%)**
USAA	9%	80%	65%	60%
ZOME	0%	20%	35%	40%

The net sale proceeds from the eventual sale of the property will be split accordance with each partner's percentage interest after payment of mortgage loan balance, outstanding equity balance, and any earned but unpaid cumulative preferred return.

6.1.4 Investment Return

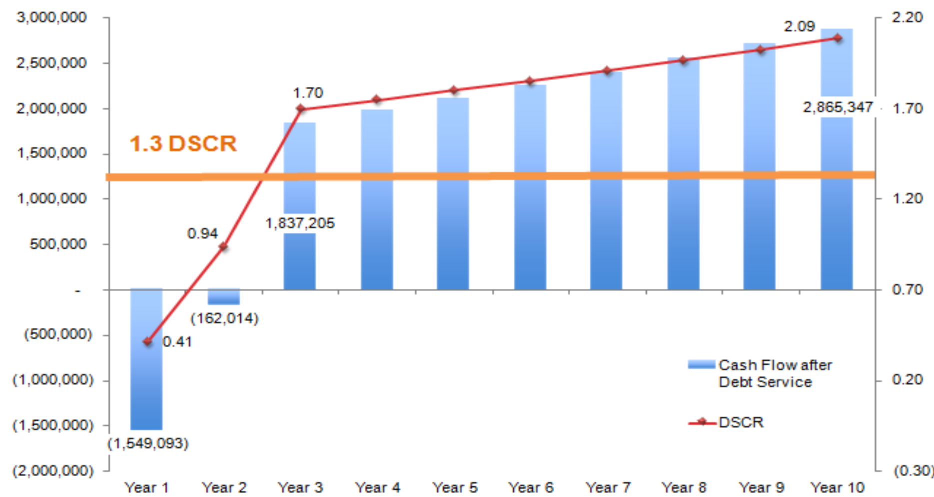
In order to determine when the sale of the project will generate the highest return, we calculated potential cash flows as well as the leveraged IRR that could be received over the 10 year span of operations. Reversion is calculated based on a 6.25% terminal cap rate.

The first year of operation understandably delivers a negative cash flow and negative IRR on reversion, as the property is expected to experience a lease up period in both residential and retail space over this year. However, at the end of the second year of operations, when stabilization has been met, the return on sale for 19Nineteen Clarendon reaches a very attractive 26.98% IRR after capitalizing year 3 cash flows to sell at the end of year 2.

The following years return, while still reaching over the preferred rate of 9% for USAA, decline consistently, eventually reaching 14.68% in year 10.

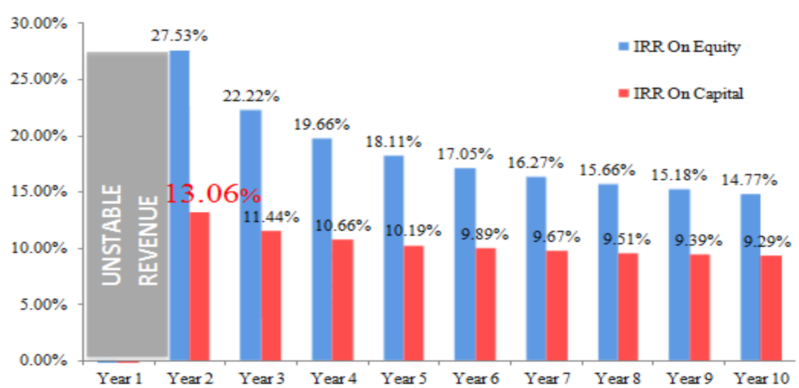
Upon sale at the end of the second year of operations, 19Nineteen Clarendon returns a projected reversion of $42,258,620. After USAA and ZOM receive their invested equity and USAA receives its 9% preferred return, the residual profit from sale is still $15,370,606. This balance would be split according to the return structure illustrated above, providing USAA with a residual return of $11,622,593, and a $35,154,250 return on equity.

6.1.5 Debt Service



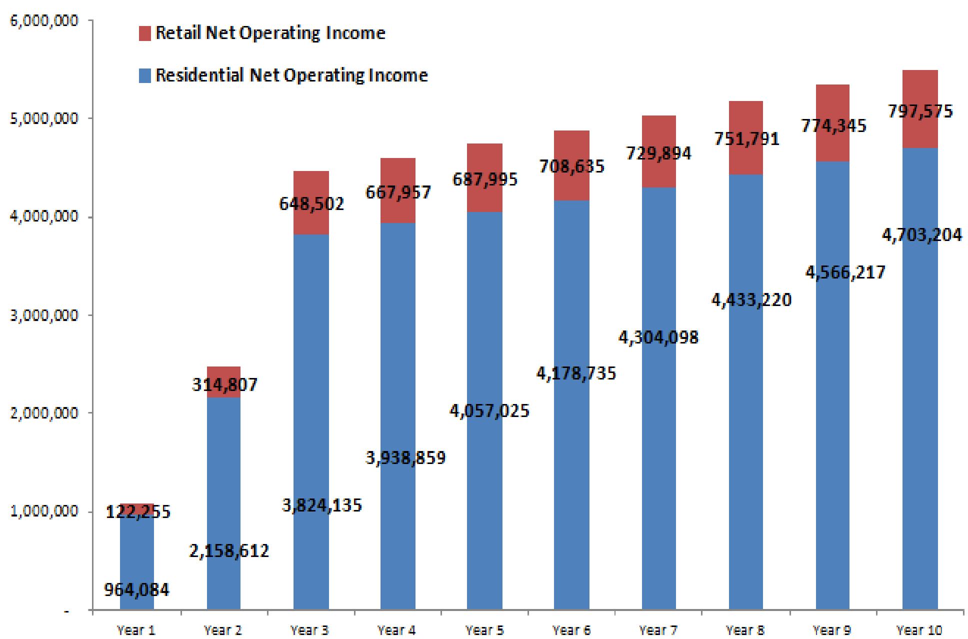
The financing for development of 19Nineteen Clarendon is received as a loan from USAA for $46 million amortized over 30 years with an interest rate of 4%. This amount will cover 65% of total development costs. The loan covenant requires a 1.3 debt coverage ratio at stabilization. 19Nineteen Clarendon will stabilize during year two and NOI will be sufficiently high enough to cover debt in year three according to Team USAA's 10 year analysis. From year 3 to year 10, the debt service coverage ratio is above 1.3, which indicates that the default risk during this period is low.

6.1.6 Internal Rate of Return



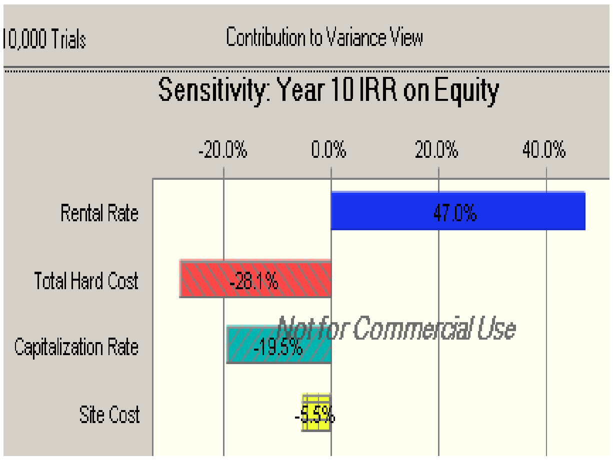
We projected IRR on equity and IRR on capital from year 1 to year 10. Generally speaking, the higher a project's IRR, the more desirable it is to undertake the project. From the chart above, IRR on equity and IRR on capital in year one are both negative. As the returns on the investment are not sufficient during these periods, we cannot sell the property in year one. For year two, IRR on equity is 27.53% whereas IRR on capital is 13.06%. Every year thereafter, the IRR on equity decreases. The descent is rapid at first and then tapers off and becomes more stable during the last few years of the projected operation. In year 10, IRR on equity is projected 14.77%. IRR on capital is projected 9.29%.

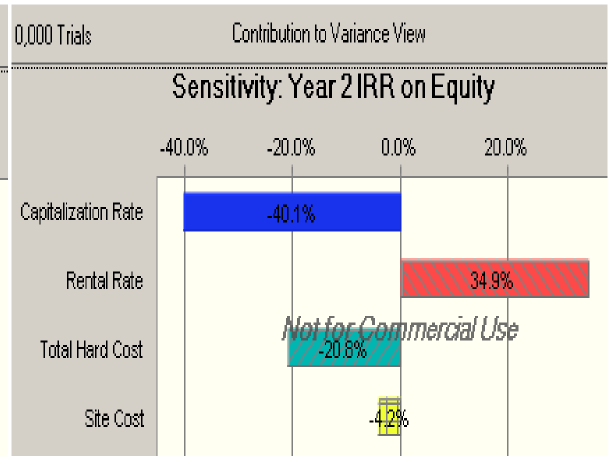
6.1.7 Economic Benefits



Both the residential and retail space are expected to experience significant lease up periods over the first two years of operation, generating a high vacancy and loss in rental income over that span. Therefore, as seen in the figure above, the net operating income will be comparatively low during those years but will continue to rise steadily. From our projections, year three will be the first year of stabilization, and both the EGI and operation expenses will increase at the 3% of annual inflation. As a result, the net operating income will trend upwards from year 3 to year 10.

6.1.8 Sensitivity Analysis





In finding the most feasible period to sell the project, we analyzed which factors had the greatest impact on the rate of return on total equity during each year of operation. The variables included in the experiment were:

- Construction costs
- Land Costs
- Rental Rates
- Capitalization Rate

When considering the entire projected life of 19Nineteen Clarendon's operation, we discovered that the most impactful variable to the IRR was the rental rates.

The most profitable projected period to sell the project was found to be at the end of year two of operations. This year was impacted the most by a potential fluctuation in the capitalization rate.

Both years were also sensitive to hard costs. The comparison shows that as time progressed, the IRR on equity was negatively affected when construction costs were considered. The amount of debt was kept so low that the annual cash flows, while consistently rising from year to year, were not enough to raise the value of the development more than what it is worth in its first year of stabilization.

6.2 Risk

Like any other project, this one does not come without its risks. There are obvious concerns, such as a slowly improving economy, which makes investors weary and unconfident in any project and the risk involved with construction. There are also project specific issues that need attention too. The five major and most significant forms of risk facing 19Nineteen Clarendon are the following:

6.2.1 Timing

Timing will be a major risk for the development team. Slow and prolonged lease-up and subsequent reversion will lead to significantly different outcomes of return. It is critical that 19Nineteen reach stabilized occupancy quickly, and that USAA be able to sell the property at the most opportune time.

In addition, unforeseen events such as design and construction modifications are contingent on the developer and contractor's ability to deliver the project on time. Some delays have already been encountered on the site due to soil contamination from unexcavated gasoline tanks. In order to decrease timing risk, financial incentives can be built into the developers' contract to encourage on time or early delivery. Some of the time lost has already been made up by the developer, and construction is set to be completed in December of 2013.

6.2.2 Market Risk

One major market risk is that competition can interfere with the projected return of the project by thwarting the lease up projections for 1919 Clarendon. As mentioned in market analysis, recently finished developments, existing competitors, projected construction and competing markets are components that can affect the demand and absorption of space for this project.

Another market factor is overall economic health, which will have a big influence on potential tenants ability to absorb space. Economic conditions are always contingent out of legal, global and other perspectives. Time of year should be also considered. For example, people may be less likely to relocate in December due to lack of disposable income over the holiday season and the fact that most leases run parallel to the fiscal calendar, ending in September. Consumer spending could potentially also impact the real estate market and potential cash flows.

Interest rates for construction loans will remain favorable in the short term; however, it is difficult to predict interest rate trends starting from three years from now, and there is always a risk of interest rates rising before the permanent loan is closed. What's more, in the coming years, the property will also face refinancing risk out of consideration of renovation due to the unique design of the project.

6.2.3 Liquidity Risk

Liquidity risk can be divided into market risk and funding risk.

<u>Market liquidity</u>

The market liquidity refers to the risk that the property cannot be sold or leased up due to lack of demand in the market. The goal of this analysis is to determine the most attractive period for sale. If the market does not line up with assumptions, projected returns for the suggested year of sale may not be achieved.

<u>Funding liquidity</u>

There is also a risk that the NOI of the property is unable to cover debt services, especially in the first year of operations when lease-ups are uncertain. If additional equity is required in the future, it may be difficult to find new investors and the deal may no longer be feasible. Additionally, returns will have the possibility to be insufficient to pay obligation to general contractors and subcontractors, mainly the management company.

6.2.4 Business (legal, operational, strategic, transactional)

Business risk can be classified into legal, operational, strategic, and transaction risks, as well as other types.

The operational risk refers to the probability that the property will not be efficiently managed or marketed. The property will be managed by ZOM's property management team, which is known nationally as a leader in the property management field. It has extensive experience in real estate management.

Human factors can trigger business risk. Unforeseen events such as contractor delays and unfamiliarity with the project can be solved by elite organizations. As mentioned in the development team section, USAA does not have an established history with the general contractor, designer, and subcontractors, so this does create a risk generated by unfamiliarity.

6.2.5 Supply Risk

The presence of significant supply of residential units in the Rosslyn-Ballston Corridor market also provides a source of risk to the project. There are currently 17,189 units of existing competitive space in the Rosslyn-Ballston Corridor, with 19,597 units estimated in 5 years. Existing competitors such as The Palatine and Grayson flats, which are recent additions to the supply in the area, provide barriers to 19Nineteen Clarendon's target market.

There are approximately 2,408 units under construction at the time of analysis, with about 2,608 that are currently proposed. With consideration of frictional vacancy in the area (4%), current supply of apartment units in the market lies at 18,617 units presently, and 21,095 forecasted for 2019.

The goal for the supply and demand analysis of similar units in the Rosslyn-Ballston Corridor is to calculate marginal demand for units in the market area. The marginal demand suggests whether the current and forecasted market is one that can provide adequate absorption for the amount of units available to potential tenants. Based on our findings, the market as of 2013 provides a marginal demand of 6,137, which suggests demand greatly exceeds supply. In 2019, the estimated demand exceeds supply by 4,936 required units. Overall, the area promises adequate and attractive absorption currently and in future years.

However, these more comparable developments have experienced a consistently high rate of occupancy ever since they reached stabilization, so they are evidence of a market that is healthy enough to strongly support the projects currently in the area that are comparable to 19Nineteen Clarendon’s.

6.2.6 Project Specific Risk

The design of 19Ninteen Clarendon is complicated. Four of the structure’s levels are wood framing. Wood framing provides a significantly cheaper. This design choice could lead to concerns over stability, maintenance, and future major renovations. As the wood structure is flexible, the building faces potential safety hazards; therefore, this specific project may not be as long-lived as one made of steel or 100% concrete.

As the concept of green buildings becomes increasingly popular, LEED certification is almost a must for new construction projects and increased density. Having the certification associated with the project can significantly improve the value of the project, as well as improve the attractiveness of the project for potential tenants.

The certification that 19Ninteen Clarendon will attempt to achieve is LEED for Mid-Rise, a result of the LEED for Multifamily Pilot program, which applies to multifamily and mixed-use projects between four and eight stories high. However, neither ZOM nor USAA has ever attempted a project for this new certification, so there-in lies the potential for miss-steps and failure to reach the certification.

7. Recommendation

Team USAA's analysis of 19Nineteen Clarendon concludes that the current market conditions support the development and that USAA should attempt to sell the asset at the end of the second year of operations. This recommendation was determined based on comparing the forecasted IRR for the project being highest at the end of the second year, at 26.98%, as stabilization will be achieved in or around May or 2015. This rate, while remaining above the USAA's preferred 9% return, declines consistently over the remaining years of operations based on our projections.

Concerns exist over risks involving timing, potential excessive supply, and achieving design and construction goals. However, projected NOI and cash flows account for an appropriate amount of time between when lease up begins and stabilization is achieved. 19Nineteen Clarendon's NOI will exceed the debt coverage ratio of 1.3 in year three of operation, 6 months following the projected point of stabilization. In addition, Team USAA's market analysis has determined that demand for multifamily residential units should continue to increase at a desirable rate compared to the development of supply in the Rosslyn-Ballston corridor over the next five years.

As was concluded by our sensitivity analysis, one of the most influential factors to the successful return on this project is the construction costs covered by USAA's loan. The chosen design features of 19Nineteen Clarendon allows for the debt required for development to remain relatively low when compared to other design strategies. The result is a very attractive IRR. Achieving LEED for Multi-Family Mid Rise is a challenge, but according to the general contractor construction has adhered to design plans successfully thus far. Earning a LEED Silver Certification will significantly improve the attractiveness of the building to tenants as well as potential buyers in the future.

Exhibit 3.1

Assumption

		Total Units	Total Space	Monthly Rent	Annual Rent
Retail	**Space 1**	1	4,029 s.f	$2.9/s.f	$35/s.f
	Space 2	1	3,982 s.f	$2.9/s.f	$35/s.f
	Space 3	1	4,393 s.f	$2.9/s.f	$35/s.f
	Space 4	1	1,941 s.f	$2.9/s.f	$35/s.f
	Space 5	1	3,120 s.f	$2.9/s.f	$35/s.f
Multifamily	**Apartment**	191	155,578 s.f	$3.1/s.f	$37.2/s.f
Operation Expense		**Growth Assumption**		**Equity Structure**	
Controllable Expense	% of EGI	Rental Growth	3.00%	USAA	95%
General and Administrative	3.00%	Other Income Growth	3.00%	ZOM	5%
Traffic Management fee	1.82%	Expense Growth	3.00%	Preferred Return	9%
Marketing	1.50%				
Utilities (Common Area)	3.29%	**Permanent loan**		**Residual Value Calculation**	
Repair and Maintenance	3.00%	Capitalization Rate	5.00%	Terminal Cap Rate	6.75%
Contact Service and Other	1.78%	Interest Rate	4.00%	Cost of Sale	3%
Turnover	1.12%	Amortization Period	30 Years	Discount Rate	12.00%
Fix Expense	% of EGI				
Insurance	2.00%	**Investment Structure**			
Real Estate Taxes	10.00%	Debt	65%		
Management Fee	13.00%	Equity	35%		
Total Operation Expense	30.51%				

Exhibit 3.2

Pro Forma

			Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11
Residential Effective Gross Revenue			1,387,370	3,106,363	5,503,144	5,668,239	5,838,286	6,013,434	6,193,837	6,379,652	6,571,042	6,768,173	6,971,218
Residential Net Operating Income			964,084	2,158,612	3,824,135	3,938,859	4,057,025	4,178,735	4,304,098	4,433,220	4,566,217	4,703,204	4,844,300
Retail Net Operating Income			122,255	314,807	648,502	667,957	687,995	708,635	729,894	751,791	774,345	797,575	821,502
Cash Flow Before Debt Service			1,086,339	2,473,418	4,472,637	4,606,816	4,745,020	4,887,371	5,033,992	5,185,012	5,340,562	5,500,779	5,665,802
Total Capital Cash Flow		(70,771,900)	1,086,339	2,473,418	4,472,637	4,606,816	4,745,020	4,887,371	5,033,992	5,185,012	5,340,562	115,417,341	
Debt Service			2,635,432	2,635,432	2,635,432	2,635,432	2,635,432	2,635,432	2,635,432	2,635,432	2,635,432	2,635,432	2,635,432
DSCR			0.41	0.94	1.70	1.75	1.80	1.85	1.91	1.97	2.03	2.09	
Cash Flow after Debt Service			(1,549,093)	(162,014)	1,837,205	1,971,384	2,109,588	2,251,939	2,398,560	2,549,580	2,705,130	2,865,347	3,030,370
Total Equity Cash Flow		(24,770,165)	(1,549,093)	(162,014)	1,837,205	1,971,384	2,109,588	2,251,939	2,398,560	2,549,580	2,705,130	76,539,921	
IRR	**14.77%**												
USAA Preferred Return	**9%**	2,229,315											
Amount Should be Distributed			2,229,315	4,547,802	7,127,523	7,731,246	8,219,572	8,583,698	8,814,344	8,901,730	8,835,551	8,604,953	
Amount Will be Distributed			0	(162,014)	1,837,205	1,971,384	2,109,588	2,251,939	2,398,560	2,549,580	2,705,130	2,865,347	
USAA Preferred Equity CF		(24,770,165)	(1,549,093)	-	1,837,205	1,971,384	2,109,588	2,251,939	2,398,560	2,549,580	2,705,130	76,539,921	
IRR USAA	**14.83%**												