

2010 National Apartment Forecast

"Management teams are sporting a new cloak of optimism, although it is heavily footnoted," said Citi REIT analyst Michael Bilerman in a research note.

Most companies said they are trying to boost occupancy by lowering rents, trading lower net operating income (NOI) in hopes of holding the line on vacancies during the current wave of job losses that has thinned the ranks of renters, especially among "echo boomers" in their 20s and 30s who are opting to double up with roommates or live with their parents. Just as their office and retail counterparts are doing, apartment companies are giving renters the upper hand.

Meanwhile, the long-expected flood of distressed property sales hasn't yet materialized, with deals held back by limited financing availability and low interest rates that have mostly allowed borrowers to continue to service their loan debt, even though many of those loans are under water. After dropping about 70% from the peak, confidence and investment activity began to stir modestly in the second half of 2009 and into 2010. Private local buyers account for most of the activity, but REITs and institutions that have built-up capital are expected to continue targeting large properties in major markets this year.

The largest apartment REIT, Equity Residential, has been first out of the gate. "This is all good news for the apartment business," Neithercut told investors earlier this month. "I'm not suggesting that we're experiencing any kind of sharp inflection here. I would rather say we think we are at the beginning of a period of slowly, and I do mean slowly, improving fundamentals. But ... if you add job growth to that picture, we believe that will quickly turn into one of the best operating periods in our history."

The cautious return of large investors may signal a shift in strategies from wait-and-see to bargain-hunting. Some believe values have dropped sufficiently to encourage investors to resume acquisitions in stronger metros and submarkets rather than risk missed opportunities by attempting to time the absolute bottom of the market.

REITs aren't the only buyers gearing up for future investments. Private local investors who liquidated their holdings at a tidy profit in the mid-2000s are coming back as buyers. In what may be "the clearest signal yet that prices have adjusted to levels that can be sustained," such smaller investors recently have accounted for 82% of the dollar value in the current acquisitions pool, compared with 37% at the peak four years ago.

The majority of apartment companies have chosen to either cancel or scale back their 2010 development plans, developers delivered just 94,000 units in 2009, a level expected to be the lowest level since 1995. New construction starts have fallen to a 15-year low, with new development constituting just 0.5% of existing inventory.

The construction pause, along with a population surge among

renters forming new households over the next three years, is expected to drive down vacancies and offer the opportunity to raise rents. With these numbers in mind, AvalonBay, unlike some of its rivals, said it remains committed to delivering new product.

The prospects for a recovery come as apartment vacancies hit a 30-year high in the fourth quarter, and rents fell 3% last year as landlords scrambled to retain existing tenants and attract new ones.

Rising unemployment contributed to a more than 3% decline in asking rents in 2009, while effective rents fell nearly 6% and concessions rose. Landlords quickly cut rent in the first half of 2009 and concessions have become commonplace in formerly torrid housing markets, such as Fort Lauderdale, Las Vegas, Miami, Orlando, Phoenix, the Inland Empire, Sacramento and Tampa-St. Petersburg possibly reflecting increased competition from the single-family and condo "shadow" market.

*~ Excerpted & abridged Co-Star Article
By Randy Drummer February 10, 2010*

2010 Sacramento Forecast

Class A owners in the Roseville/Rocklin and Elk Grove submarkets should post vacancy rates near 10 percent this year, with concessions averaging more than 30 days of free rent. Vacancy rates in the limited Class A inventory downtown should continue to improve modestly through 2010 as renters choose to relocate closer to dense job centers.

Class B/C properties, however, should continue to fair healthier than their Class A counterparts and are expected to recover rather quickly once more jobs are created in 2011. This year, a large student population will fuel strengthened performance in Class B/C complexes within the Davis and Woodland submarkets, where vacancy should stay below 6 percent.

After traditional apartment sales slowed dramatically in 2009, an anticipated rise in REO offerings should help boost sales activity this year, as already experienced by the Apartment Advisory Team. Smaller REO deals have begun to dominate distressed-asset sales toward the end of 2009 and in the early months of 2010, though larger bank-owned complexes will likely emerge later in the year. As REO deals begin to trade with greater frequency though, a pricing floor will emerge and help to align expectations.

Owners will continue to face challenges when attempting to divest traditional listings during the first half of the year and sellers will need to adjust prices to meet the market. According to a study conducted by MIT, currently there is a 13% to 14% gap between seller and buyer expectations regarding where prices should be, and this disconnect will be fully closed by 2011 with cap rates (set by a valuation perspective) reach their apex. Cap rates for stabilized properties ended last year at 8 percent and are projected to raise an additional 50 basis points in 2010, with slightly less expected for properties in downtown and midtown Sacramento.



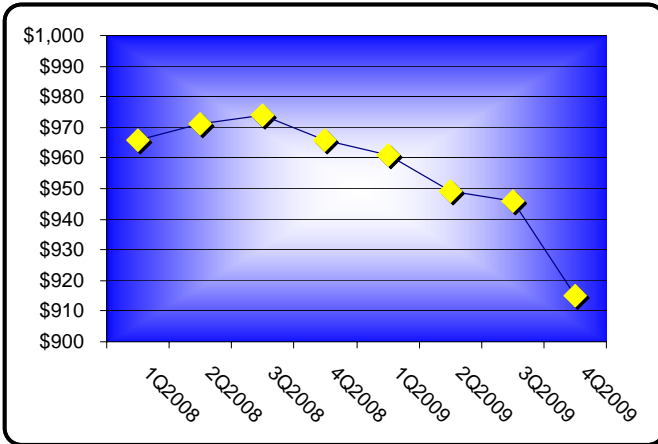
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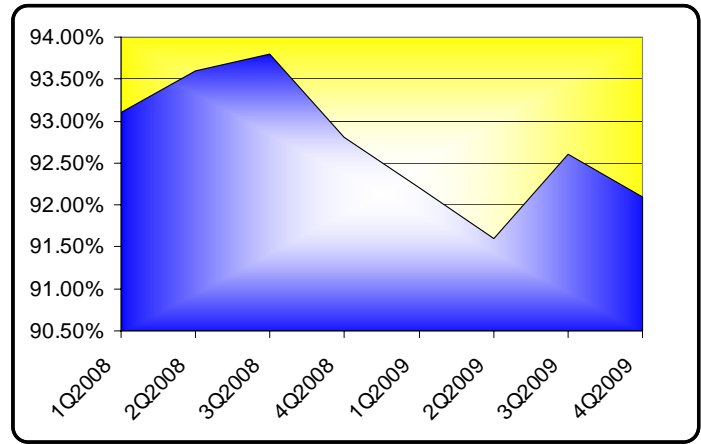
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