ApartmentResearch

MARKET UPDATE

Marcus & Millichap

Orlando Metro Area *Fourth Quarter 2009*

Despite Current Weakness, Positive Developments Emerging

Near-term fundamentals in the Orlando apartment sector are expected to erode further as a weak economy stifles household formation and rental housing demand. Despite projected vacancy of nearly 11 percent this year and additional declines in rents, some positive news emerged in the third quarter. For one, the rate of layoffs started to slow, with job cuts in the third quarter estimated to be the lowest in more than a year. Also, the University of Central Florida College of Medicine opened during the third quarter. While the opening did not avert a rise in vacancy in the area , the presence of the college is expected to help further diversify the local economy and become an engine for future growth. In the construction sector, multi-family building and permitting continued to ease considerably in the third quarter. A decline in apartment development will magnify the effects of the increase in demand that accompanies a resumption in hiring.

Investment activity has subsided from a few years ago, when more liberal lending standards and higher loan-to-value ratios fueled aggressive buying. Transaction velocity has decreased only 12 percent over the past year but is down more than 80 percent from the peak of the market four years ago. With only a few transactions recorded in the last 12 months, values are difficult to determine. Sales of lender-owned properties and fractured condo deals have occurred at substantial discounts, contributing to a low range of prices in recent deals. Greater vacancy and use of concessions, meanwhile, are pushing down prices for stabilized assets, although few of these properties have changed hands. A stabilization of the economy over the next few months may slow the rate of rent reductions and simplify underwriting heading into 2010. Despite the lingering economic downturn and a recent deceleration in population growth, the market's outlook for long-term expansion remains intact and will stimulate investors' interest.

2009 Annual Apartment Forecast

4.3% decrease in total employment

Employment: The pace of job cuts will continue to slow over the remainder of the year. In 2009, payrolls are forecast to shrink 4.3 percent, as 47,000 jobs will be eliminated. Last year, local employers trimmed 39,500 positions.

840 units will be completed

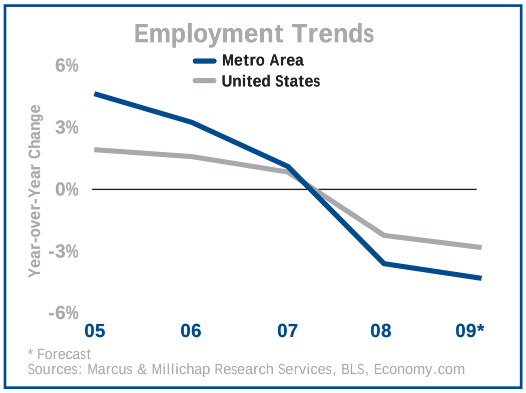
Construction: In 2009, developers will deliver 840 units, down from more than 3,100 units last year. An average of 2,100 units per year have come online over the past four years.

90 basis point increase in vacancy

Vacancy: Even as supply growth virtually stops, demand will remain weak until employment rebounds . As a result, vacancy in Orlando is expected to rise 90 basis points this year to 10.9 percent, the highest reading this decade.

3.9% decrease in asking rents

Rents: Asking rents are projected to fall 3.9 percent in 2009 to $855 per month. Effective rents will drop 5.5 percent to $780 per month. Last year, asking rents rose 1.6 percent, and effective rents decreased 0.9 percent.



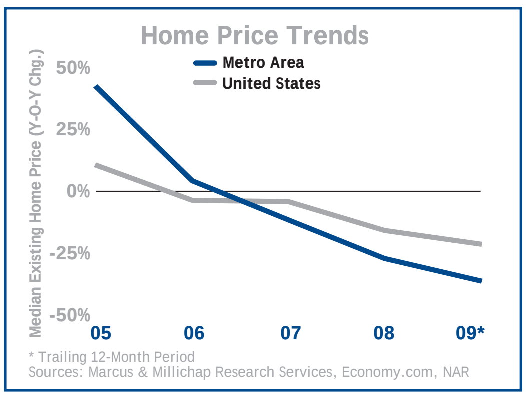
ECONOMY

- Total employment in the Orlando metro area declined 3.8 percent in the first three quarters of this year due to the elimination of 39,700 jobs. Since the recession started, the loss of 79,200 positions has reduced total employment to a level last recorded in early 2005.

- Although job cuts have been severe, the rate of layoffs has started to slow. Approximately 6,000 positions were eliminated in the third quarter, compared with average quarterly losses of 12,200 employees since the beginning of the recession.

- Among the positive notes in the local economy, approximately 2,900 workers were hired in the leisure and hospitality sector in the first two months of the third quarter. Some of the increase is attributable to the recent opening of the 1,400-room Hilton Orlando near the Orange County Convention Center.

- **Outlook:** The pace of job cuts will continue to slow over the remainder of the year. In 2009, payrolls are forecast to shrink 4.3 percent, as 47,000 jobs will be eliminated. Last year, local employers trimmed 39,500 positions.



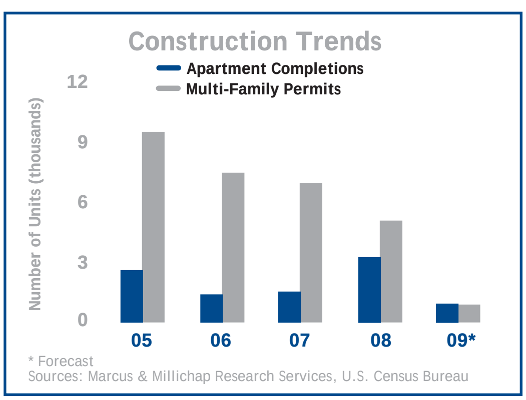
HOUSING AND DEMOGRAPHICS

- Supply-side pressures are easing. In the 12 months ending in the third quarter, permits for 4,300 units of single- and multi-family housing were issued, a decline of 67 percent from the corresponding year-earlier period.

- Sales of distressed homes at discounted prices and a first-time homebuyer credit ignited an estimated 45 percent increase in sales of existing single-family homes in the annual period ending in the third quarter. The median price has fallen 40 percent year over year to $124,600.

- The average Class A asking rent in the market is $281 per month more than the typical mortgage and other payments on the median-priced home. The average asking rent for a Class B/C rental is about $12 less than the monthly debt on the median-priced home.

- **Outlook:** Single-family residences are affordable to renters. There will be some migration of renters to owner-occupied housing, but lingering uncertainty over the employment market and stricter credit standards will cause many renters to avoid the risks of homeownership.



CONSTRUCTION

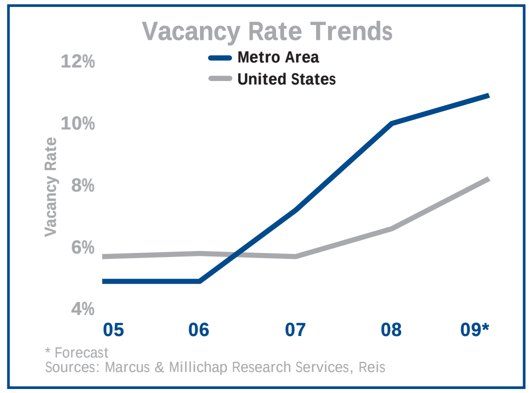
- No projects were completed in the third quarter. Over the past 12 months, 1,875 units have been delivered. The pace of construction is slowing significantly, as more than 2,500 units were put into service in the preceding year.

- Year to date, 760 units have come online. Significant projects include the 456-unit Cumberland Park complex in the Far South/Lake Buena Vista submarket, which was delivered in the first quarter.

- The pipeline of planned projects has thinned to about 10,000 units, compared with 11,400 planned rentals earlier in the year. Meanwhile, multifamily permit issuance has fallen 84 percent over the past 12 months to approximately 1,000 units.

- **Outlook:** In 2009, developers will deliver 840 units, down from more than 3,100 units last year.

Vacancy



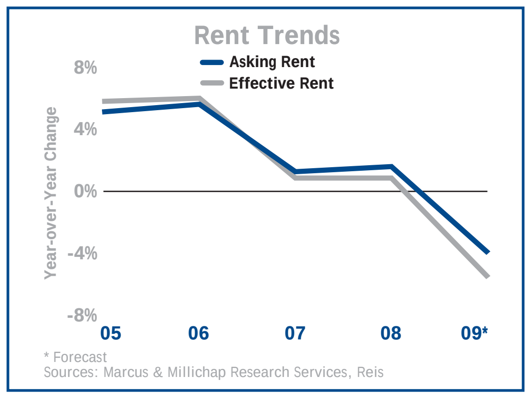
- A reduction in employment suppressed housing demand in the third quarter, leading to a 50 basis point increase in the vacancy rate to 10.3 percent. On a year-over-year basis, vacancy has climbed 150 basis points.

- Demand trends in the Class B/C segment contributed to most of the decline in the overall vacancy rate. In the third quarter, lower-tier vacancy rose 80 basis points to 11 percent as the number of occupied units fell 0.9 percent. Class B/C vacancy has increased 220 basis points since the third quarter of last year.

- Class A vacancy inched up 30 basis points in the third quarter to 9.5 percent and is 70 basis points more than one year earlier, as growth in stock has exceeded an increase in occupied units.

- **Outlook:** Even as supply growth virtually stops, demand will remain weak until employment rebounds . As a result, vacancy in Orlando is expected to rise 90 basis points this year to 10.9 percent, the highest reading this decade.

Rents



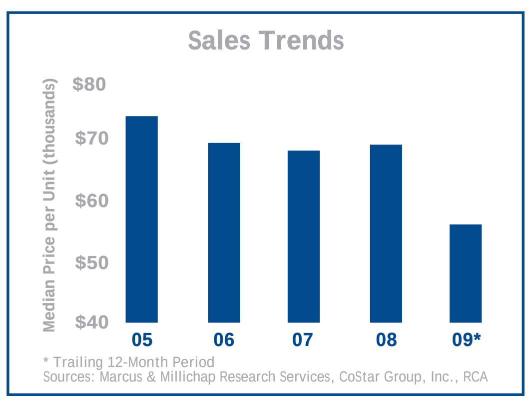
- Driven by slumping demand in the Class B/C segment, marketwide asking rents were estimated to fall 1.5 percent in the third quarter to $869 per month. Effective rents slid 2 percent to $797 per month. Year to date, asking and effective rents have receded 2.4 percent and 3.4 percent, respectively.

- A weak job market has reduced rental housing demand, contributing to a 1.6 percent decline in Class B/C asking rents in the third quarter to $750 per month. So far in 2009, asking rents in the lower tiers have decreased 3.1 percent. Asking rents at Class A complexes dropped 1.2 percent in the third quarter to $1,019 per month and are down 1.7 percent year to date.

- Faltering demand has resulted in a gradual increase in concessions this year. Average concessions were 8.3 percent of asking rents in the third quarter, the equivalent of one month of free rent. At year-end 2008, concessions were 7.3 percent of asking rents.

- **Outlook:** Asking rents are projected to fall 3.9 percent in 2009 to $855 per month. Effective rents will drop 5.5 percent to $780 per month.

Sales Trends**



- Transaction velocity declined 12 percent over the most recent 12-month period, based on a limited number of sales.

- The median price in deals closed in the past year was $56,300 per unit, a drop of 19 percent from the preceding annual period. Prices in sales recorded this year range from about $30,000 per unit to $60,000 per unit.

- The lack of activity makes it difficult to establish cap rate trends. Generally, cap rates start at about 8 percent for stabilized properties and rise based on location, asset quality and financial performance.

- **Outlook:** Investors in large properties typically have driven activity in the market, but this pool of buyers will remain mostly sidelined in the months ahead, as financing for such assets is challenging. Sales of large, deeply discounted properties in financial distress will persist due to highly motivated buyers and sellers.

*** Data reflect a full 12-month period, calculated on a trailing 12-month basis by quarter.*

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Capital Markets

By WILLIAM E. HUGHES, Senior Vice President, Marcus & Millichap Capital Corporation

- Compared to other core property sectors, apartments have fared best due to the availability of financing through government-sponsored enterprises (GSEs) Fannie Mae and Freddie Mac. Recent modifications to GSE guidelines will impact lender decisions, however, as borrower requirements include more substantial apartment ownership experience.

- Loan-to-value requirements range from 55 percent to 75 percent. Portfolio lenders are issuing loans at all-in rates of 6.00 percent to 6.75 percent for a five-year term and 6.9 percent to 8.0 percent for a 10-year term. Rates among agency lenders are roughly 150 basis points to 175 basis points lower. The government recently assumed full control of Fannie Mae and Freddie Mac, which may boost confidence in the GSEs, putting downward pressure on rates, but it also creates several near-term uncertainties.

- Delinquencies will rise further as a wave of maturities approaches; however, at-risk borrowers may find lenders amenable to loan extensions/modifications. Furthermore, Freddie Mac is under way on its second securitization of multi-family debt this year, and the government's TALF program is expected to at least provide a much-needed spark to the traditional CMBS market.

Submarket Overview

- A large daytime population and proximity to major employers in downtown Orlando have encouraged developers to plan 2,800 rentals in the Maitland/Winter Park submarket. There are no scheduled start dates for any of the projects, which represent about 80 percent of the area's existing stock.

- Class B/C vacancy is greater than 10 percent in six of the metro's 11 submarkets. In the Northwest submarket, vacancy has climbed 250 basis points this year to 15.6 percent. The increase represents a 200-unit drop in occupied units. High unemployment and job losses will suppress rental demand in the near term.

- In the Southeast/Airport submarket, the addition of 839 top-tier units over the past year has contributed to a 260 basis point jump in Class A vacancy to 11.6 percent.

Submarket Vacancy Ranking

Rank	Submarket	Vacancy Rate	Y-O-Y Basis Point Change	Effective Rents	Y-O-Y % Change
1	West Altamonte Springs	8.1%	30	$789	-0.5%
2	Southwest	8.2%	220	$850	-3.8%
3	Far North	8.3%	40	$851	-3.0%
4	East Altamonte/Casselberry	8.6%	40	$769	-1.7%
5	Northeast	9.5%	220	$799	-2.6%
6	Far South/Lake Buena Vista	10.5%	340	$938	-3.6%
7	Southeast/Airport	10.7%	70	$837	-0.4%
8	South Central	11.3%	10	$770	-4.6%
9	Maitland/Winter Park	12.4%	300	$811	-3.3%
10	Northwest	14.8%	330	$616	-5.2%

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