

ApartmentResearch

M A R K E T U P D A T E

Marcus & Millichap

Charlotte Metro Area

Third Quarter 2010

PAYROLLS EXPANDING, DESPITE ONGOING FINANCE SECTOR DIFFICULTY

Although the pace of job growth will moderate in Charlotte during the second half of 2010, gains made in the first half will allow owners to raise rents measurably for the first time since the third quarter of 2008. Most employment segments have begun to recover, with job creation particularly robust in the professional and business services, government, and leisure and hospitality industries. Financial activities employers continue to contract, however, and further consolidations at Wells Fargo and Bank of America will likely result in additional job losses over the next two years. Also, slowing development metrowide has weighed on construction employment but should help support apartment absorption in the second half as supply-side threats abate. Over the past year, many apartment operators, realizing the diminishing effectiveness of concessions, slashed asking rents and withdrew leasing incentives, eliminating nearly a week of free rent. With concessions in line with pre-recessions levels, asking rent growth will resume in the third quarter, laying the foundation for revenue gains once supply-side pressure eases more considerably in 2011.

Sales of distressed properties will continue to comprise a large share of overall deal flow, placing downward pressure on prices through year end. As a result, many owners of stabilized properties will be dissuaded from listing. A few investor-to-investor trades have been executed, though, with prices remaining relatively stable due to a lack of available product. Buyers continue to target newer, operationally sound complexes near the Charlotte core and the Interstate 485 beltway, where accessibility to major employers keeps Class A cap rates around 7 percent. Prices in the top tier currently average near the \$70,000 per unit to \$80,000 per unit range, though top-notch luxury locations can trade for as much as \$120,000 per unit.

2010 ANNUAL APARTMENT FORECAST



Employment: Despite projections for a slower pace of job growth during the second half of the year, Charlotte businesses will add 19,500 employees in 2010, or a 2.4 percent gain. Last year, 47,000 positions were shed.



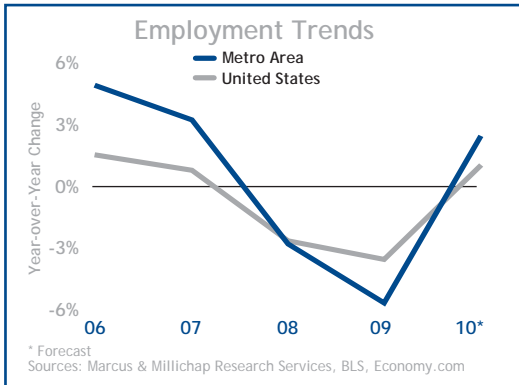
Construction: Metro apartment stock will expand by 2,250 units, or 2.3 percent, this year, after builders completed 3,625 units in 2009.



Vacancy: A more modest pace of job creation during the second half will keep marketwide vacancy steady at the current level of 10.9 percent, though this rate marks a 40 basis point improvement from last year, when vacancy surged 310 basis points.

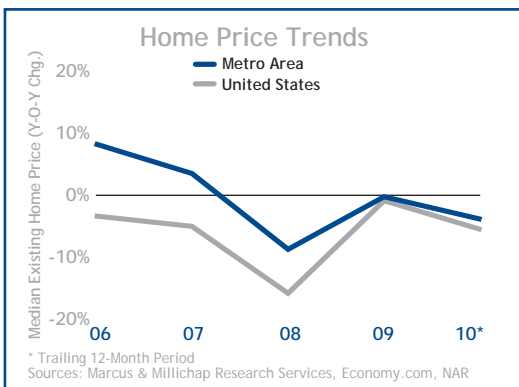


Rents: Asking rents will advance 1 percent to \$769 per month this year, while effective rents will climb 0.8 percent to \$682 per month. Last year, asking rents fell 4.6 percent, and effective rents were trimmed 5.4 percent.



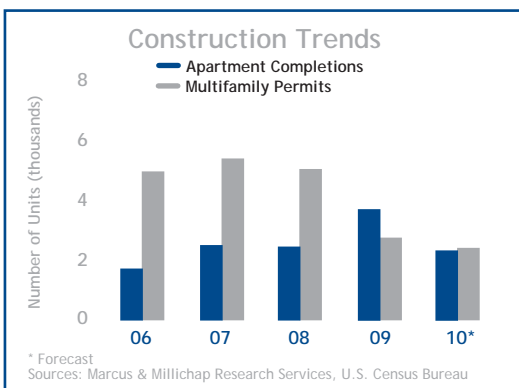
ECONOMY

- ◆ Charlotte employers began the year hiring at a healthy clip. So far in 2010, 13,500 jobs have been created for growth of 1.7 percent, the largest six-month job gain since the first half of 2007. During the second half of last year, 10,600 workers were let go.
- ◆ Hiring efforts have been most robust in the professional and business services and government sectors, which have expanded payrolls by a total of 9,100 positions, or 3.8 percent, year to date. Conversely, the construction and financial activities industries continue to contract, shedding an aggregate of 2,500 jobs during the first two quarters of 2010.
- ◆ In line with the improving economy, the local unemployment rate declined 120 basis points year over year to 11 percent. In the three years preceding the recession, the jobless rate averaged 5 percent.
- ◆ **Outlook:** Without the boost of temporary government positions, the pace of hiring will ease in the second half of the year. Charlotte businesses will add 19,500 employees in 2010, a gain of 2.4 percent. Last year, 47,000 positions were shed.



HOUSING AND DEMOGRAPHICS

- ◆ Resurgent home sales due to the first-time homebuyer tax credit encouraged builders to pull 5,625 single-family permits in the past year, up 22 percent from the previous annual period. Soft demand for new multifamily assets, however, drove down permitting activity in this segment 54 percent in the past year to 1,690 units, following a 32 percent decline a year earlier.
- ◆ Since the start of 2010, home sales have decreased 29 percent; sales remained steady during the corresponding period in 2009. The median price of an existing single-family home declined 4 percent year over year to \$188,420.
- ◆ While local household incomes are conducive to homeownership, renting remains an affordable option. The average Class A asking rent of \$882 per month is \$132 below the monthly mortgage obligation on the area's median-priced home, using conventional financing.
- ◆ **Outlook:** The sharp decline in home sales during the first half of the year indicates renters' continued reluctance to transition into homeownership.

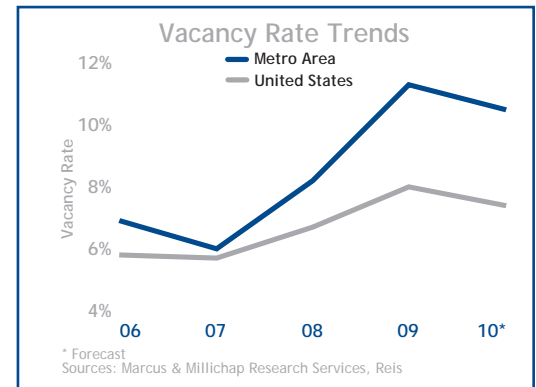


CONSTRUCTION

- ◆ Construction output has begun to ease. Approximately 1,475 rental units were delivered during the first two quarters of this year, down from the second half of 2009, when 2,050 units were added.
- ◆ There are 1,860 units under construction marketwide, most with completion dates stretching beyond this year. Additionally, 8,625 rentals are planned, though limited construction financing will keep many developers from breaking ground on these projects.
- ◆ Arwen Vista, one of the largest developments under way in the metro, will be completed later this year in the Harris Boulevard submarket. Rents at the complex will range between \$690 per month and \$1,100 per month, in line with the submarket Class A average of \$830 per month.
- ◆ **Outlook:** Metro apartment stock will expand by 2,250 units, or 2.3 percent, this year, after builders completed 3,625 apartments in 2009.

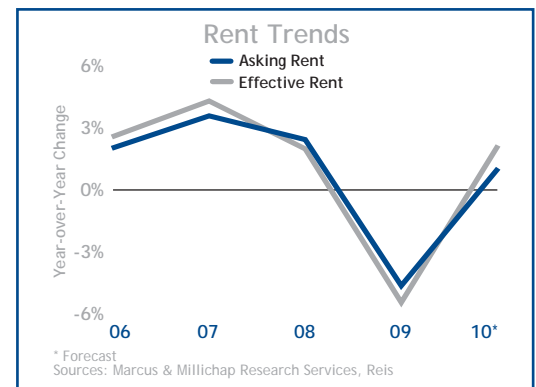
VACANCY

- ◆ Vacancy improved 80 basis points during the first half as the local economy steadied, though the second quarter rate of 10.5 percent was 40 basis points higher than in the same period in 2009.
- ◆ Resurgent Class A leasing activity has driven down the top-tier vacancy rate 100 basis points year to date to 10 percent. During the second half of 2009, vacancy in the segment climbed 140 basis points.
- ◆ Operators of lower-tier apartment properties recorded a 70 basis point decline in vacancy to 11 percent in the first half of 2010. In the preceding six-month stretch, the Class B/C vacancy rate increased 100 basis points.
- ◆ **Outlook:** A more modest pace of job creation during the second half will keep marketwide vacancy steady at the current level of 10.9 percent, though this rate marks a 40 basis point improvement from last year, when vacancy surged 310 basis points.



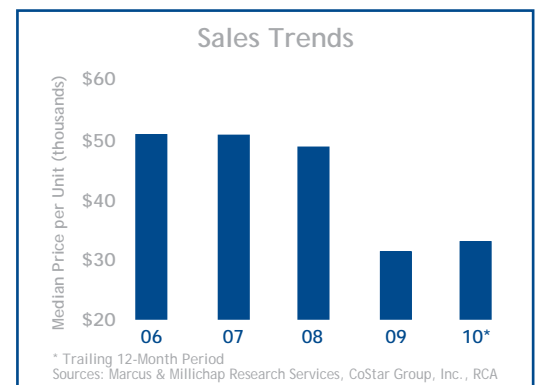
RENTS

- ◆ Despite mild fluctuations throughout the first half of the year, asking rents of \$761 per month during the second quarter were unchanged from the close of 2009. Effective rents, however, surged 1 percent in that span to \$684 per month. During the prior half year, asking and effective rents plunged 3.2 percent and 2.4 percent, respectively.
- ◆ So far in 2010, Class A asking rents have slipped 0.1 percent to \$882 per month, while lower-tier asking rents have appreciated 0.3 percent to \$629 per month.
- ◆ Concessions declined 160 basis points in the past year to 10.1 percent of asking rents. Despite reduced leasing incentives, rising vacancy rates eased average revenues 1.1 percent in that time.
- ◆ **Outlook:** Asking rents will advance 1 percent to \$769 per month this year, while effective rents will climb 2.1 percent to \$692 per month. In 2009, asking rents fell 4.6 percent, and effective rents were trimmed 5.4 percent.



SALES TRENDS**

- ◆ Expectations for fire-sale pricing and the prevalence of opportunistic buyers in the market have caused the number of deals involving stabilized properties to fall drastically. Consequently, overall deal flow slowed 45 percent in the past 12 months.
- ◆ Softening investor demand and distressed sales have depressed values, with the median price regressing 17 percent year over year to \$33,000 per unit. In the prior 12-month period, the median price decreased 27 percent.
- ◆ A small number of stabilized properties continue to trade, though cap rates are rising. After averaging near 6.8 percent in 2009, initial yields have since risen into the low-7 percent range to account for falling NOIs.
- ◆ **Outlook:** Sales of distressed assets will continue to dominate the local investment market over the second half of 2010, though velocity will tick up among top-tier investments as it becomes clear cap rates in this segment will not rise as high as previously anticipated.



** 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

- ◆ Mixed economic indicators, stock market volatility and concerns surrounding the European debt crisis continue to drive investors to safety. As a result, the yield on the 10-year U.S. Treasury has declined since peaking at 4 percent in April; as of late July, the yield had fallen to 3 percent.
- ◆ Capital markets loosened over the past year, with life insurance companies ramping up lending and CMBS showing renewed signs of life. Nonetheless, the agencies remain the dominant sources of multifamily lending. This trend will continue through 2010 as the GSEs' multifamily portfolios outperform their residential mortgage operations, reducing the likelihood of drastic government-mandated changes to their apartment lending arms.
- ◆ Multifamily loan originations increased 37 percent in the second quarter but remained below levels reported during the same period last year. Fannie Mae and Freddie Mac's origination volume followed a similar pattern, rising in the second quarter but falling short of year-earlier levels.
- ◆ Loan-to-values range from 60 percent to 75 percent for portfolio lenders and push up to around 80 percent for best-of-class, agency-financed deals. All-in rates for five-year agency loans fall into the low-4 percent range, while 10-year loans price between 4.75 percent and 5.15 percent. While life companies will compete at these levels for best-of-class deals, most portfolio lenders are 100 basis points to 225 basis points higher.

SUBMARKET OVERVIEW

- ◆ Year-to-date vacancy surges have offset rent gains in the Concord/North Concord submarket, driving down average revenues 0.9 percent.
- ◆ The planning pipeline remains full in the Harris Boulevard/Mallard Creek Church Road submarket. Currently, nine projects totaling more than 3,200 units are under consideration, which could boost area inventory by 23 percent. The 772-unit Sam Furr Station Apartments is the largest development proposed; the complex is slated for Old Statesville and Sam Furr roads.
- ◆ Tenant incentives remain low in the Gaston County submarket, where the metro's lowest rents continue to attract renters. Area owners trimmed concessions by 120 basis points in the past year to 4.2 percent of asking rents, equivalent to just over two weeks of free rent.

SUBMARKET VACANCY RANKING

Rank	Submarket	Vacancy Rate	Y-O-Y Basis Point Change	Effective Rents	Y-O-Y % Change
1	Carmel	6.5%	-310	\$779	-2.1%
2	Northwest Charlotte	8.1%	-150	\$793	-1.4%
3	Downtown	8.6%	-650	\$1,014	-7.2%
4	Harris Blvd./Mallard Creek Church Rd.	8.9%	70	\$741	-3.3%
5	Gaston County	9.4%	-90	\$589	-2.5%
6	North Pineville	9.5%	-20	\$660	-1.6%
7	East Charlotte-Albemarle Corridor	9.8%	-20	\$576	-3.8%
8	East Charlotte-Central Avenue	11.2%	-220	\$621	-4.3%
9	North Tryon Street-The Plaza	14.9%	240	\$530	-3.3%
10	Concord/North Concord	18.2%	380	\$588	-5.9%