

ApartmentResearch

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

Marcus & Millichap

Atlanta Metro Area

Third Quarter 2009

WEAK MARKET DRIVING TENANTS TO SEEK AFFORDABLE SOLUTIONS

In Atlanta, a reduction in apartment construction this year was expected to offset weaker employment-generated demand, although significant job losses are still weighing heavily on the apartment market. Concerns over the near-term direction of the local and national economies, along with a lack of available construction financing, have limited development. Completions in 2009 will reach the lowest level since 2004 and fall 50 percent below the 10-year average. The drop in construction activity is a welcome trend, although staff cuts within the professional and business services and trade, transportation and utilities sectors are softening renter demand. Unemployment has spiked 510 basis points over the last year to 10.7 percent, causing many tenants to seek to reduce living expenses by doubling up or migrating into the metro's expanding shadow rental market. Subsequently, rents for studio apartments have declined the most, falling 3.1 percent year to date, while rents for two-bedroom units have decreased 1 percent. Currently, concessions are averaging one-and-a-half months of free rent, up from one month of free rent a year ago.

In the investment market, transaction velocity remains constrained due to investors' concerns over the near-term stability of the market and tighter underwriting. Sales activity has slowed by more than 60 percent during the past two quarters, and soft demand is causing prices to decline as buyers target more stable submarkets in the northern areas of the metro, such as North Atlanta, Sandy Springs and Marietta. The median price in sales completed year to date is approximately \$43,000 per unit, a level last recorded in 2003. Cap rates continue to rise and currently average in the low- to mid-8 percent range for Class A properties, while Class B/C assets are being offered at initial yields 100 basis points higher. Owners looking to exit the market in the coming months should consider listing properties, as cap rates will continue to trend higher as investors account for greater short-term risks.

2009 ANNUAL APARTMENT FORECAST



Employment: Approximately 90,000 jobs are forecast to be cut this year, a decline of 3.8 percent. In 2008, 92,500 positions were eliminated.



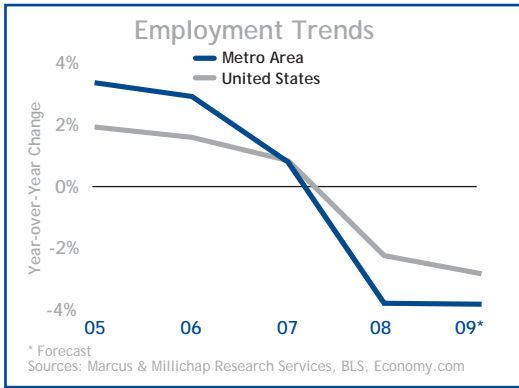
Construction: Developers are responding to waning renter demand and greater competition from shadow stock by decreasing completions to 3,600 units in 2009, after 5,100 units were added last year.



Vacancy: Reduced construction activity, coupled with competition from condos and single-family residences in the rental pool, will push vacancy higher this year. By year end, vacancy is forecast to reach 12.2 percent, up 190 basis points from 2008.

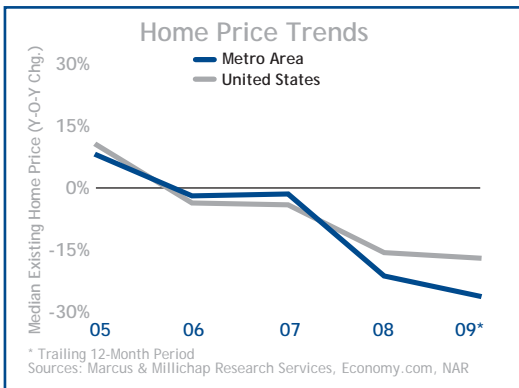


Rents: Rents will continue to be hampered by a drop in tenant demand associated with employment losses. Asking rents are expected to decline 3.9 percent in 2009 to \$828 per month, while effective rents will fall 4.9 percent to \$730 per month.



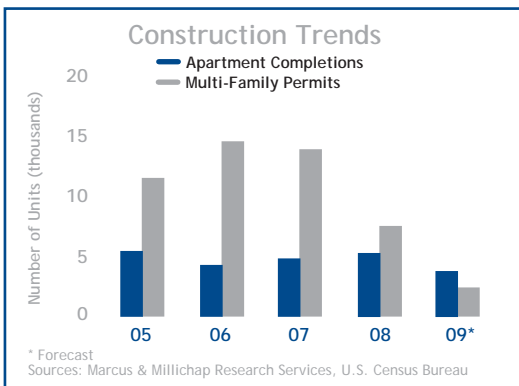
ECONOMY

- ◆ Employment losses have accelerated. In the first six months of 2009, nearly 65,000 jobs were shed, compared with 16,600 new hires in the corresponding period last year.
- ◆ In the 12 months ending in the second quarter, 46,700 professional and business services positions were trimmed from payrolls, following the elimination of 500 such jobs in the preceding year. Companies involved in the trade, transportation and utilities sector also are cutting back, as an estimated 34,000 workers were let go in this industry during the 12-month span ending in the second quarter, up from the loss of 7,800 jobs the year before.
- ◆ Staff levels in the education and health services sector have expanded by 8,200 positions in the past year, a trend that is likely to persist through the remainder of 2009, albeit at a slower pace, due to the metro's growing population.
- ◆ **Outlook:** Approximately 90,000 jobs are forecast to be cut this year, a decline of 3.8 percent. In 2008, 92,500 positions were eliminated.



HOUSING AND DEMOGRAPHICS

- ◆ Permits for 7,000 units of single-family housing and 2,200 units of multi-family housing were projected to be issued over the year ending in the second quarter, decreases of 46 percent and 73 percent, respectively, from the preceding 12-month period. Housing supply continues to outpace demand, as just 2,900 households were created in the metro during the same span.
- ◆ The median price of a single-family home in Atlanta was estimated at \$115,000 in the second quarter, a year-over-year decline of 26 percent. Sales velocity of single-family homes dropped 14 percent in that time.
- ◆ Currently, the metro's median household income of \$58,000 per year is 53 percent greater than the income needed to meet the monthly mortgage obligations on a median-priced residence.
- ◆ **Outlook:** While for-sale housing remains affordable in Atlanta, conservative mortgage financing and lingering uncertainty regarding the stability of the economy are keeping more people in the renter pool.

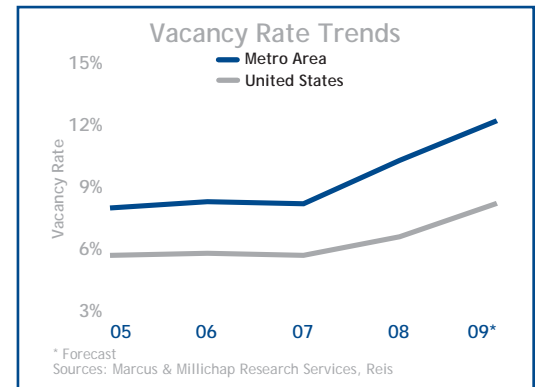


CONSTRUCTION

- ◆ Apartment inventory has increased 1.2 percent, or by 4,100 units, year over year. In the preceding 12 months, rental stock grew by 4,300 units, or 1.3 percent.
- ◆ Approximately 17,000 rental units are planned in the metro. The Midtown submarket is the most targeted area, with 4,600 units proposed. The Roswell/Alpharetta and Sandy Springs/Dunwoody submarkets, meanwhile, each contain about 1,500 planned units.
- ◆ By year end, the Midtown and South Fulton County submarkets are expected to receive approximately 1,000 new units apiece. Developers are focusing on close-in areas near downtown Atlanta and employment hubs.
- ◆ **Outlook:** Developers are responding to waning renter demand and greater competition from shadow stock by decreasing completions to 3,600 units in 2009, after 5,100 units were added last year.

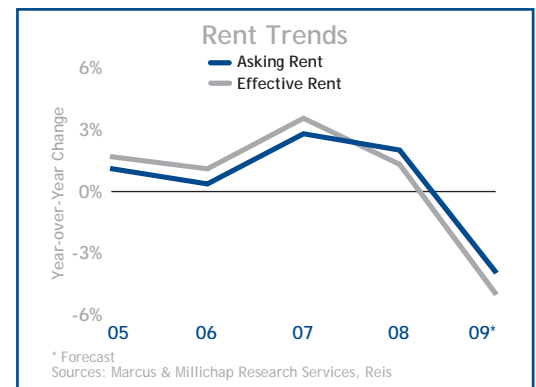
VACANCY

- ◆ Growing shadow stock and ongoing completions have pushed vacancy higher in recent months. As of the second quarter, vacancy was 11.2 percent, a 240 basis point spike from one year earlier.
- ◆ Class A vacancy edged up significantly, ending the second quarter at 9.9 percent, or a jump of 220 basis points over the past year. The rise is the result of added inventory amid weaker renter demand.
- ◆ The vacancy rate in the lower tiers has increased 270 basis points in the last 12 months to 12.6 percent. Job losses among the traditionally lower-paying construction and manufacturing sectors are softening demand for Class B/C apartments.
- ◆ **Outlook:** Reduced construction activity, coupled with competition from condos and single-family residences in the rental pool, will further elevate vacancy this year. By year end, vacancy is forecast to reach 12.2 percent, up 190 basis points from 2008.



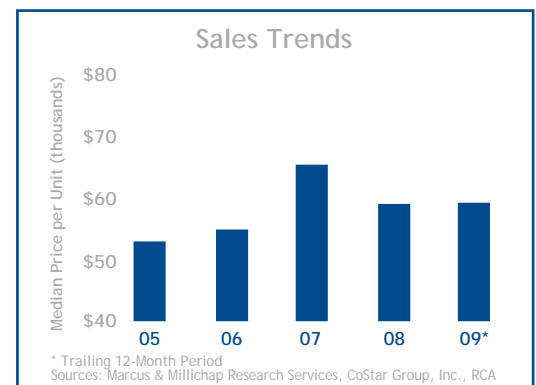
RENTS

- ◆ Increasing vacancy is causing rents to moderate. Asking rents ended the second quarter at \$856 per month, down 0.5 percent from one year earlier, while effective rents fell 2.9 percent during that stretch to \$749 per month.
- ◆ Asking rents in Atlanta's Class A properties dipped 0.6 percent over the 12 months ending in the second quarter to \$956 per month due to competition from new units and rising unemployment. In the lower tiers, rents have declined 0.5 percent year over year to \$725 per month.
- ◆ Revenues have fallen as a result of lower occupancy levels and an uptick in concessions. Over the past year, the average gross revenue has dropped 3.5 percent, after increasing 2.8 percent in the previous 12 months.
- ◆ **Outlook:** Rents will continue to be hampered by a decrease in tenant demand associated with employment losses. Asking rents are expected to decline 3.9 percent in 2009 to \$828 per month, while effective rents will fall 4.9 percent to \$730 per month.



SALES TRENDS**

- ◆ Sales velocity in the Atlanta metro has slowed by approximately 51 percent over the past 12 months. Tighter lending standards and softer economic conditions have kept many would-be buyers on the sidelines.
- ◆ Year over year, the median price has declined 4.4 percent to \$59,700 per unit. Some of the decrease can be attributed to more conservative underwriting and expectations for higher vacancy rates in the near term.
- ◆ In the last 12 months, cap rates have averaged from 8.0 percent to 8.5 percent for Class A assets and 9.0 percent to 10.5 percent for lower-tier properties. Cap rates in both segments have risen about 100 basis points in that time.
- ◆ **Outlook:** Concerns over the near-term stability of the local economy and ongoing job losses will continue to weigh on investor activity. Well-located, stabilized Class A properties in high-demand neighborhoods north of downtown, such as Roswell and Alpharetta, currently receive the most interest.



** 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

- ◆ During the first quarter, multi-family mortgage originations were 61 percent below year-earlier levels and 79 percent lower than the late-2006 peak. Though considerable, the reduction in apartment originations remains less significant than declines among other core commercial property types, due largely to the availability of financing through Fannie Mae and Freddie Mac.
- ◆ Portfolio lenders are issuing apartment financing at all-in rates of 6.0 percent to 6.3 percent for three-year loans and up to 6.8 percent to 7.5 percent for a 10-year term. Loan-to-value requirements range from 55 percent to 75 percent.
- ◆ Agency lenders are offering five-year loans at all-in rates of 4.8 percent to 5.0 percent with 10-year mortgages available at rates averaging 5.35 percent and 5.7 percent, respectively. Maximum leverage among agency lenders ranges from 55 percent to 75 percent.
- ◆ Freddie Mac recently completed a \$1 billion securitization of multi-family debt, the first issuance to hit the market since last June. The securities, dubbed "K Certificates," vary from traditional CMBS in that buyers are provided a guarantee by Freddie Mac. In addition to the potential for another similar offering, government programs designed to increase credit flows into commercial real estate could be operational by late summer/early fall.

SUBMARKET OVERVIEW

- ◆ The Midtown submarket is scheduled to receive approximately 1,000 units this year, a 7.8 percent addition to stock. As a result, vacancy in the area is expected to rise 280 basis points to 13 percent by year end, pushing concessions from 9.5 percent of asking rents to 10.0 percent of asking rents.
- ◆ Class A properties in the Decatur/Avondale submarket are operating at an average vacancy rate in the mid-5 percent range, while Class B/C assets are recording vacancy above 14 percent. Investors with long-term holding periods may realize upside potential through the repositioning of lower-tier properties in this area.
- ◆ Robust office and retail completions continue within the Buckhead submarket. Over the next 18 months, approximately 1 million square feet of office space and 600,000 square feet of retail space will be delivered in the area, driving demand for apartments.

SUBMARKET VACANCY RANKING

Rank	Submarket	Vacancy Rate	Y-O-Y Basis Point Change	Effective Rents	Y-O-Y % Change
1	Roswell/Alpharetta	8.4%	110	\$817	-4.8%
2	Smyrna	9.0%	170	\$713	-5.6%
3	South Gwinnett	9.7%	210	\$696	-2.9%
4	North Gwinnett	10.1%	90	\$736	-3.0%
5	Midtown	10.2%	130	\$924	-8.2%
6	I-20 West	10.3%	190	\$667	-1.0%
7	North DeKalb	10.4%	210	\$814	-2.9%
8	Decatur/Avondale	10.8%	250	\$715	-4.2%
9	Clayton/Henry	10.8%	240	\$672	-1.0%
10	Marietta	11.3%	280	\$729	-3.2%