

ApartmentResearch

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

Marcus & Millichap

Chicago Metro Area

Third Quarter 2009

RENT CUTS HINDERING CONDITIONS, INVESTMENT ACTIVITY

Job losses will continue to weigh on operating conditions in the Chicago apartment market through the remainder of the year. In response to increased cost-consciousness and waning demand, owners are looking closely at their rents. Asking rents are projected to retreat to pre-2007 levels, led by decreases in some downtown areas. In Lincoln Park and the Near North Side, for example, conditions are weaker than adjacent submarkets, and rents in these areas are forecast to recede the most in all of downtown. This trend is projected to result in a 3.2 percent revenue decline, which will likely cause some caution among investors. As such, transaction velocity for city assets is expected to remain modest through the coming quarters, while cap rates will continue to rise. Also affecting sales activity is a decrease in conventional listings, which will further drag on values but may create opportunities for investors to purchase city properties at attractive prices.

In the suburbs, the weak labor market will hinder fundamentals, and an increase in supply-side pressure will also contribute to softened metrics. Developers are on pace to expand apartment inventory by 0.3 percent this year, the largest annual increase in more than five years. Completions are concentrated in the Glen Ellyn/Wheaton and Glendale Heights/Lombard submarkets, which will likely cause area owners to reduce rents and increase concessions at a more dramatic rate than in other suburban cities. Despite a slowdown in condo construction in the suburbs, the outlying areas of the Glenview/Evanston submarket are slated to receive nearly 770 for-sale units in 2009, many of which may be employed as rentals, creating added competition. Investment activity in these submarkets is expected to lag deal flow in close-in neighborhoods, as well as areas along arterial routes and commuter rail lines, where cap rates are slightly below the metro average. Suburban initial yields are currently in the high-7 percent to low-8 percent range and are projected to rise as the number of distressed and REO offerings increases through the remainder of the year.

2009 ANNUAL APARTMENT FORECAST



Employment: Weakness in the professional and business services and trade, transportation and utilities segments will continue to drag on metro employment this year. Overall payrolls are expected to decrease by 3.4 percent, or 151,000 spots, following a 2.4 percent decline in 2008.



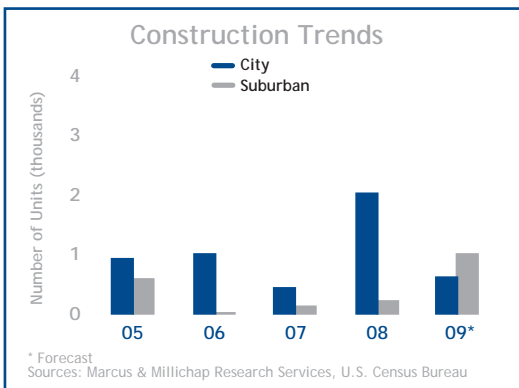
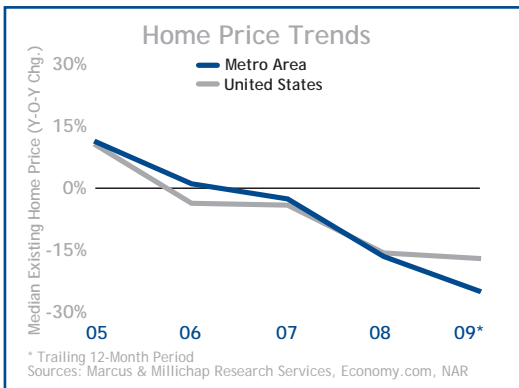
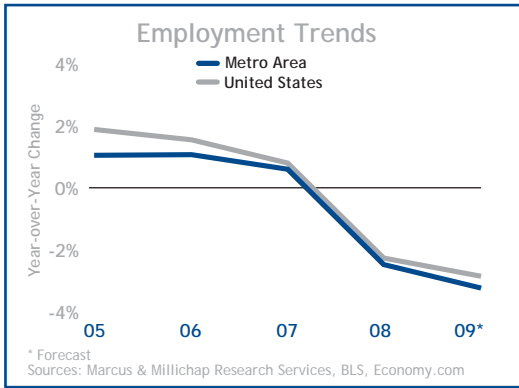
Construction: Roughly 1,590 units are projected to come online metrowide in 2009. Most of the 2,180 apartments that were delivered last year were located in the city, while more than 60 percent of the metro's projected completions this year are concentrated in the suburbs.



Vacancy: Job losses are forecast to drive up vacancy 200 basis points in 2009 to 7.4 percent, after vacancy rose 60 basis points last year.



Rents: Rent reductions and increased concessions are projected throughout the metro this year. Asking rents are expected to drop 2.1 percent to \$1,049 per month, while effective rents will be \$970 per month, an annual decline of 2.6 percent.



ECONOMY

- ◆ Chicago-area employers have eliminated approximately 203,000 positions over the past 12 months, a 4.5 percent decline and the largest annual contraction in 27 years. Losses have accelerated in the last two quarters, when 118,000 jobs have been trimmed.
- ◆ Led by large cuts in the manufacturing and trade, transportation and utilities segments, payrolls in Lake and Kenosha counties have been thinned by 3.2 percent during the past year, while the size of the labor market in the southeastern suburbs and Gary, Ind., has contracted by 4.5 percent.
- ◆ On a year-over-year basis through the second quarter, the median home price dropped 24 percent to \$190,200, and the median household income dropped 11.2 percent. As such, the median household income is currently 11 percent greater than the amount needed to qualify for a mortgage on a median-priced home.
- ◆ Developers are easing the pace of permit applications amid tight credit markets and waning demand. Single-family permit issuance has retreated 48 percent in the last year to nearly 6,300 units, while the number of multi-family permits pulled has fallen 62 percent to 4,660 units.
- ◆ **Outlook:** Weakness in the professional and business services and trade, transportation and utilities segments will continue to drag on metro employment this year. Overall payrolls are expected to decrease by 3.4 percent, or 151,000 spots, following a 2.4 percent decline in 2008.

CONSTRUCTION

CITY

- ◆ While 1,020 units have been added in the city during the last 12 months, there were no deliveries in the first half of 2009. Completions are expected to ramp up in the final two quarters of the year.
- ◆ The largest project slated for delivery this year is the second phase of The Streeter. This portion will add 480 units to the Gold Coast submarket upon completion in the fourth quarter. One notable development under way in the city is an 800-unit phase at K Station; the project, located in the City West submarket, is slated to start accepting tenants in 2012.
- ◆ **Outlook:** Deliveries in the city are projected to accelerate in the second half. In 2008, just over 1,600 units came online, whereas approximately 600 apartments are anticipated to open this year.

SUBURBAN

- ◆ Over the last year, 845 apartments have been completed in the suburbs, expanding the area's inventory by 0.3 percent. Just 110 units debuted in the previous 12-month period.
- ◆ There are two apartment projects under way in the suburbs, which will boost local stock by 730 units. The largest of these developments is the 390-unit Arboretum Landmark complex in the Woodridge/Lisle submarket, which is slated for delivery in 2010.
- ◆ **Outlook:** Contrary to last year's trend, completions in the suburbs are projected to outpace those in the city. Nearly 990 units are slated to come online this year, after 320 units were delivered in 2008.

VACANCY AND RENTS

CITY

- ◆ Despite reduced construction activity in recent months, ongoing job losses pushed up vacancy in the city 100 basis points during the past year to 6.6 percent in the second quarter.
- ◆ Year over year, asking rents have ticked down 0.1 percent to \$1,191 per month, while effective rents have slipped 0.8 percent to \$1,112 per month.
- ◆ **Outlook:** Vacancy in the city is forecast to reach 7 percent this year, 110 basis points higher than in 2008. Asking rents are expected to fall to \$1,179 per month, and effective rents will be \$1,096 per month.

SUBURBAN

- ◆ A downturn in the local economy has played a large role in raising suburban vacancy 180 basis points year over year to 6.8 percent. Most of the increase came from heavy job losses and a sizable shadow rental market in the outlying submarkets.
- ◆ Asking rents in the suburbs ended the second quarter at \$992 per month, 0.3 percent lower than one year earlier. Effective rents, meanwhile, contracted 1.9 percent to \$910 per month.
- ◆ **Outlook:** Suburban vacancy is projected to increase 150 basis points to 7.6 percent in 2009. As a result, owners are expected to lower asking rents by 2.7 percent to \$969 per month and increase concessions, driving down effective rents 3.5 percent to \$893 per month.

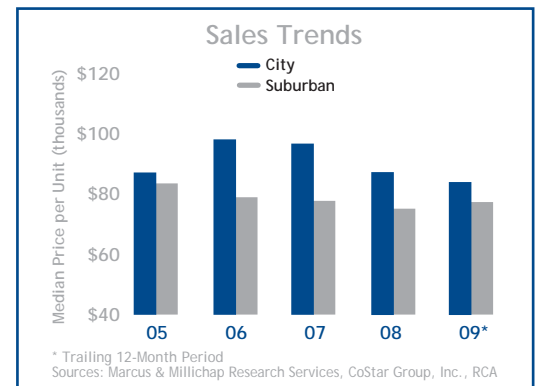
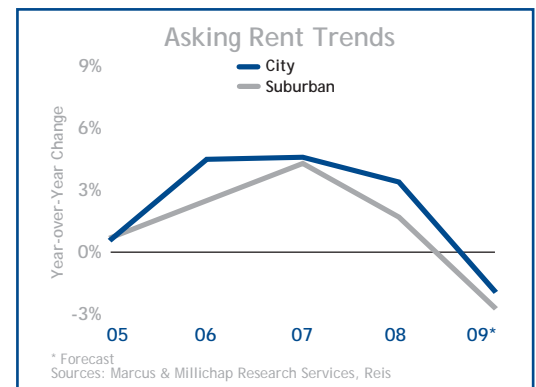
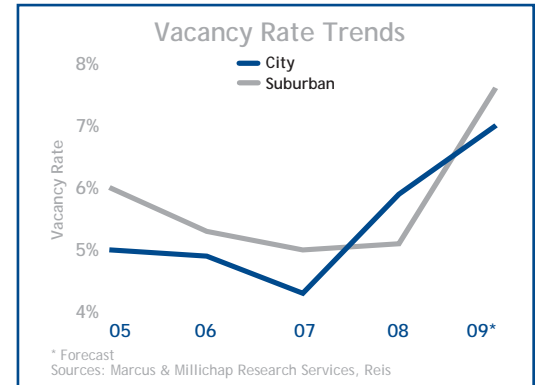
SALES TRENDS**

CITY

- ◆ A lack of traditional listings in the city caused transaction velocity to slow 30 percent during the most recent 12-month period.
- ◆ An increase in distressed offerings and an adjustment of pricing strategies have pushed average cap rates approximately 75 basis points higher over the last year to the mid-7 percent range. The median sales price during that time was \$67,100 per unit.
- ◆ **Outlook:** Investors are targeting assets in the eastern portion of the City West submarket, where more affordable rents will continue to attract renters looking to cut costs.

SUBURBAN

- ◆ Weakened conditions have increased investor wariness, resulting in a deceleration of transaction velocity in the suburbs.
- ◆ The median price in the area is roughly \$70,400 per unit, 2.5 percent lower than one year ago. This relative stability is due to ongoing flight-to-safety patterns among buyers; however, the number of suburban REOs is expected to increase in the coming months, which will likely weigh down prices.
- ◆ **Outlook:** Densely populated corridors, particularly those along the Metra line, are projected to garner the most buyer attention this year. The Des Plaines and Villa Park areas recorded upticks in activity during the first half of 2009, a trend expected to continue through the remainder of 2009.



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

Marcus & Millichap

NATIONAL MULTI HOUSING GROUP

Visit www.NationalMultiHousingGroup.com or call:

Linwood C. Thompson

Senior Vice President, Managing Director

National Multi Housing Group

Tel: (678) 808-2700

lthompson@marcusmillichap.com

Marcus & Millichap

Real Estate Investment Services

Prepared and edited by

Josh Gisselquist

Research Analyst

Research Services

For information on national apartment trends, contact

John Chang

National Research Manager

Tel: (602) 687-6700 ext. 6803

john.chang@marcusmillichap.com

Chicago Office:

Greg LaBerge

Regional Manager

glaberge@marcusmillichap.com

8750 W. Bryn Mawr Avenue, Suite 650

Chicago, Illinois 60631

Tel: (773) 867-1500

Fax: (773) 867-1510

Chicago Downtown Office:

John M. Przybyla

Regional Manager

jprzybyla@marcusmillichap.com

333 W. Wacker Drive, Suite 200

Chicago, Illinois 60606

Tel: (312) 327-5400

Fax: (312) 327-5410

Oak Brook Office:

Steven Weinstock

Regional Manager

sweinstock@marcusmillichap.com

One Mid America Plaza, Suite 200

Oakbrook Terrace, Illinois 60181

Tel: (630) 570-2200

Fax: (630) 570-2210

Price: \$150

© Marcus & Millichap 2009

www.MarcusMillichap.com

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.

CITY VACANCY RANKING

Rank	Submarket	Vacancy Rate	Y-O-Y Basis Point Change	Effective Rents	Y-O-Y % Change
1	Lincoln Park	3.8%	90	\$1,159	-3.9%
2	Belmont to Montrose	4.0%	70	\$1,136	0.4%
3	Rogers Park/Uptown	5.1%	210	\$777	-2.1%
4	South Shore	6.1%	60	\$872	-1.7%
5	Gold Coast	7.4%	-40	\$1,582	-0.3%
6	City West	10.4%	80	\$931	-1.9%
7	The Loop	13.2%	660	\$1,568	-1.7%

SUBURBAN VACANCY RANKING

Rank	Submarket	Vacancy Rate	Y-O-Y Basis Point Change	Effective Rents	Y-O-Y % Change
1	O'Hare	4.5%	80	\$831	-3.7%
2	Southwest Cook County	5.3%	20	\$775	-3.1%
3	Glendale Heights/Lombard	5.5%	110	\$1,016	0.7%
4	Southeast Cook County	5.9%	260	\$772	-4.5%
5	Wheeling	6.0%	140	\$970	-1.3%
6	Woodridge/Lisle	6.3%	60	\$910	-0.9%
7	Joliet	6.4%	80	\$751	-4.1%
8	Schaumburg/Hoffman	6.5%	160	\$950	-4.9%
9	Glenview/Evanston	6.5%	290	\$1,004	-6.4%
10	Aurora/Naperville	6.8%	140	\$982	-0.6%
11	East Lake County	7.1%	100	\$925	4.4%
12	Kane County	7.1%	220	\$940	3.0%
13	Glen Ellyn/Wheaton	7.8%	220	\$909	-3.7%
14	McHenry County	7.8%	230	\$882	1.8%
15	West Lake County	8.2%	170	\$861	-5.4%
16	Palatine	8.4%	70	\$1,086	4.7%
17	Oak Park	8.5%	410	\$893	-0.3%
18	Downers Grove	8.8%	340	\$876	-1.1%