

ApartmentResearch

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

Marcus & Millichap

Orlando Metro Area

Third Quarter 2009

WEAK RENTAL DEMAND PRESSURES PROPERTY VALUES

As the local economy progresses through one of its worst stretches ever, the Orlando apartment market continues to falter. The vacancy rate has remained at nearly 10 percent in the second quarter and is headed for a year-end reading above 11 percent. Rents have declined, and property owners have employed concessions more frequently. While supply growth over the past 12 months partly accounts for current conditions in the market, rental development is abating and will be less of an influence in the quarters ahead. Instead, greatly diminished demand will most affect key measures of property performance. The market is on its way to recording the most significant annual decrease in jobs, and net migration trends continue to erode housing demand. The inability of individuals to sell homes in other parts of the country and relocate to Orlando contributed to an estimated 35 percent drop in net migration during the year ending in the second quarter. In the second quarter alone, estimated net migration totaled less than 2,000 individuals, compared with quarterly averages of more than 12,000 persons from 2004 to the end of 2006, the height of the economic expansion.

The recent decline in property fundamentals will continue to place pressure on property values in the months ahead. Transaction activity thus far in 2009 has been subdued, reflecting investors' uncertainty over price trends. Gross property revenue has declined about 4 percent in the past year, and additional decreases are likely as concessions are employed more frequently and vacancy continues to rise. Activity in the months ahead will likely be centered in areas of the market with proven, though somewhat weakened, demand generators. These areas include submarkets in the southern half of the metro, as well as properties in eastern Orange County near the University of Central Florida. Marketwide, cap rates on recently listed assets generally range from 7.7 percent to 8.5 percent, depending on the property's current operating conditions. Cap rates may have to move slightly higher, however, to generate interest.

2009 ANNUAL APARTMENT FORECAST



Employment: Total employment will contract 4.9 percent this year, as 52,000 jobs will be cut, the steepest single-year decline on record. In 2008, local employers trimmed 39,500 positions from payrolls.



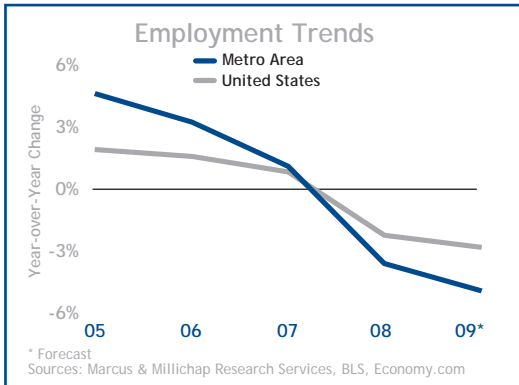
Construction: One year after developers delivered 3,100 units, production will slow to 900 units in 2009. Currently, 11,400 units are planned in the metro area, although none of the projects is scheduled to start.



Vacancy: A lack of demand will push the vacancy rate up 120 basis points this year to 11.2 percent. In 2008, vacancy climbed 280 basis points, primarily as a result of supply growth.



Rents: Weak demand will not provide any traction for owners to raise rents. This year, asking rents are forecast to slide 3.3 percent to \$861 per month, and effective rents are projected to decrease 4.4 percent to \$789 per month. Asking rents rose 1.6 percent in 2008, and effective rents advanced 0.9 percent.

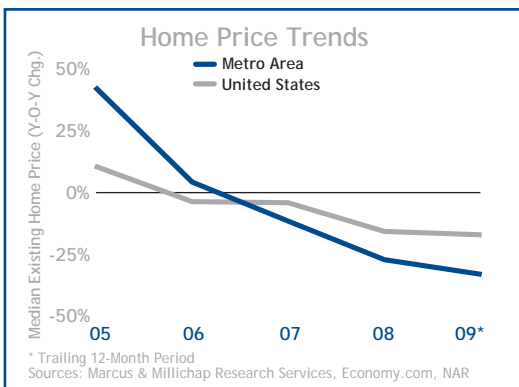


ECONOMY

- ◆ Local employers shed 33,500 jobs in the first half of 2009, a 3.2 percent decline. Since the second quarter of last year, 56,900 jobs have been lost.
- ◆ The contraction in the labor market has been significant, affecting all sectors. So far this year, 12,200 positions in the professional and business services segment have been cut. Also, 7,800 construction jobs have been eliminated due to the sluggish housing market.
- ◆ Year to date, 7,400 leisure and hospitality positions have been removed, as a decline in travel has forced hotels to trim staffs, while bars and restaurants have shut down. With fewer visitors, retailers also have been affected, resulting in the loss of 2,300 retail jobs in the first half of 2009.
- ◆ **Outlook:** Total employment will contract 4.9 percent this year, as 52,000 positions will be cut, the steepest single-year decline on record. In 2008, local employers trimmed 39,500 jobs from payrolls.

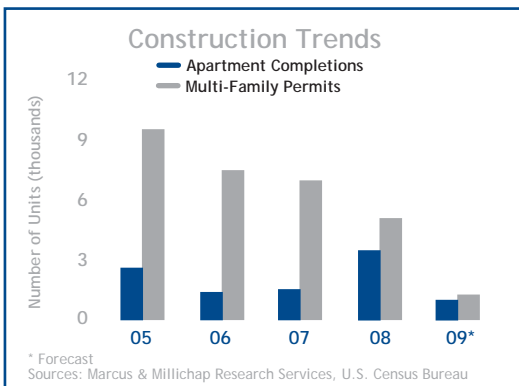
HOUSING AND DEMOGRAPHICS

- ◆ Builders continue to realign production with slumping demand. In the 12 months ending in the second quarter, permits for 5,600 single-family units were issued in the metro area, a 63 percent drop from the year before and the lowest level in more than 30 years. Housing starts in the second quarter were also off more than 30 percent from the year-earlier level.
- ◆ On the multi-family side, permit issuance plunged 70 percent in the 12 months ending in the second quarter to 2,200 units. Permits for fewer than 900 units have been issued so far this year.
- ◆ The median price dropped 36 percent over the year ending in the second quarter to \$142,000. Affordability has improved as a consequence, as the median household income of \$47,100 per year is nearly twice the minimum level needed to cover the monthly mortgage payment on the median-priced home. As recently as two years ago, single-family homes in the metro area were out of reach for most area residents.
- ◆ **Outlook:** Supply-side pressures will continue to ease in the housing market, while sales of distressed or deeply discounted homes will push down the median price.



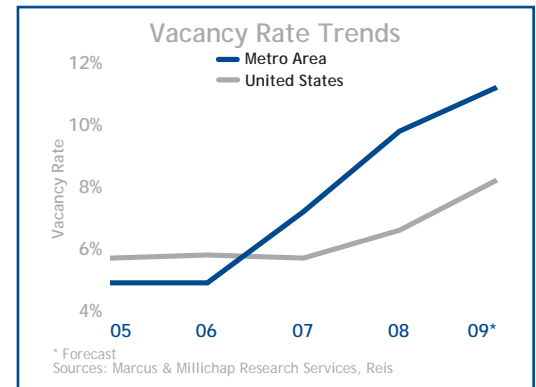
CONSTRUCTION

- ◆ Including 760 units brought online earlier in 2009, 1,990 apartment units have been delivered in the past 12 months, a 1.8 percent increase to stock. The pace of construction is slowing, as approximately 3,000 units were completed in the 12 months ending in the second quarter of 2008.
- ◆ About 1,000 units are under construction in the market, and most will be delivered in 2010. The 384-unit Verano project in Osceola County is under way and slated for completion in the third quarter of this year.
- ◆ There are 11,400 units planned in the market, about the same number as reported earlier this year. The primary areas of interest for developers are the Maitland/Winter Park submarket, where 3,700 units are planned, and the South Central submarket, with 3,800 planned apartments.
- ◆ **Outlook:** One year after developers delivered 3,400 units, production will slow to 900 units in 2009.



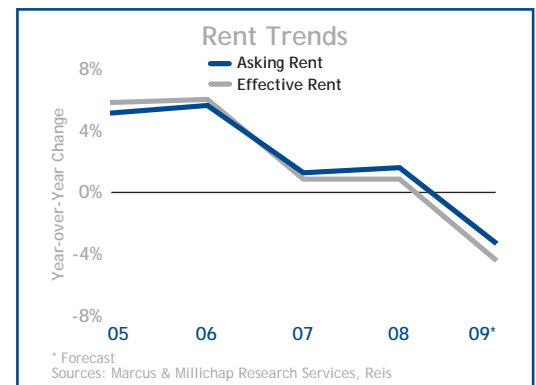
VACANCY

- ◆ The market has been affected by supply growth over the past year, as new units contributed to a 100 basis point rise in the vacancy rate to 9.8 percent. Seasonal fluctuations yielded a 50 basis point drop in the vacancy rate during the second quarter, however.
- ◆ In the Class A sector, the vacancy rate declined 70 basis points in the second quarter to 9.6 percent, but the rate is up 30 basis points over the past year. Supply additions over the past year contributed to the rise.
- ◆ Class B/C vacancy was 10.2 percent in the second quarter, 30 basis points less than in the preceding quarter but 170 basis points more than one year earlier. The lower-tier segment has been most affected by a decline in household creation that accompanies a weak labor market.
- ◆ **Outlook:** A lack of demand will push up the vacancy rate 140 basis points this year to 11.2 percent. In 2008, vacancy climbed 260 basis points, primarily as a result of supply growth.



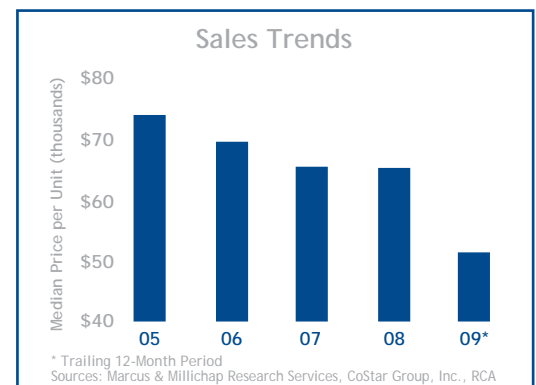
RENTS

- ◆ The average asking rent decreased 0.9 percent in the second quarter to \$883 per month and are 0.6 percent less than one year ago. Effective rents fell 1.1 percent in the second quarter to \$813 per month and are down 1.6 percent from the second quarter of 2008.
- ◆ In the Class A tier, asking rents of \$1,033 per month in the second quarter marked a decline of 0.9 percent from the preceding quarter and 0.2 percent from the second quarter of last year. Class B/C asking rents slipped for the third straight quarter, notching a 0.8 percent drop to \$765 per month. Asking rents in the lower tiers are also 1.3 percent less than one year ago.
- ◆ With the decline in effective rents, concessions were 7.8 percent of asking rents in the second quarter, compared with 6.9 percent of asking rents in the corresponding period in 2008. Concessions are on course to approach the peak level of 8.6 percent of asking rents recorded six years ago.
- ◆ **Outlook:** Weak demand will not provide any traction for owners to raise rents. This year, asking rents are forecast to slide 3.3 percent to \$861 per month, and effective rents are projected to decrease 4.4 percent to \$789 per month.



SALES TRENDS**

- ◆ Transaction velocity has declined 29 percent in the past 12 months. Only a few sales were executed in the first half of this year.
- ◆ The median price of properties sold in the last 12 months was \$51,400 per unit, a decline of 23 percent from the preceding year. Since peaking in 2005, the median price has decreased 30 percent, although a steep drop in velocity since then makes comparisons difficult.
- ◆ Cap rates on new listings range from approximately 7.7 percent to 8.5 percent. Properties with operational challenges such as high vacancy rates or concessions may be listed with initial yields well above the range.
- ◆ **Outlook:** Although the availability of financing has modestly improved in the past few months, a lack of clarity on prices will keep prospective buyers on the sidelines for a while longer.



** 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

- ◆ Planned projects represent about 10 percent of existing stock in the market. About 1,400 units are planned in the Southeast/Airport submarket, an area that includes the Lake Nona Medical City, the new home of the Burnham Institute and the University of Central Florida medical school.
- ◆ Hilton Hotels will hire 1,450 workers to staff three hotels opening later this year near the Orange County Convention Center and Walt Disney World. The hirings will provide an economic boost and enhance rental housing demand in submarkets in the southern half of the metro area.
- ◆ The increase in vacancy in the Far South/Lake Buena Vista submarket is attributable to weakened demand for Class B/C units, perhaps stemming from layoffs at Walt Disney World. In the past 12 months, the Class B/C vacancy rate in the submarket has climbed 450 basis points to 10.1 percent.

SUBMARKET VACANCY RANKING

Rank	Submarket	Vacancy Rate	Y-O-Y Basis Point Change	Effective Rents	Y-O-Y % Change
1	Southwest	7.4%	150	\$871	-2.2%
2	West Altamonte Springs	7.7%	-60	\$799	-1.7%
3	East Altamonte/Casselberry	7.8%	-20	\$780	-0.1%
4	Far North	8.3%	-20	\$860	-1.9%
5	Northeast	8.9%	200	\$805	-1.6%
6	Far South/Lake Buena Vista	9.9%	320	\$959	-0.2%
7	Southeast/Airport	10.4%	-10	\$849	-0.9%
8	South Central	11.0%	-170	\$780	-2.4%
9	Kissimmee/Osceola	12.0%	350	\$817	-1.9%
10	Maitland/Winter Park	12.1%	430	\$823	-0.5%