

# ApartmentResearch

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

Marcus & Millichap

Chicago Metro Area

Third Quarter 2010

## PRICE CUTS STIMULATING SALES OF SMALLER ASSETS

Chicago employers will add 40,000 jobs in 2010, supporting apartment fundamental improvements in the second half. Payroll expansion that was choppy during the first six months will proceed at a steady pace through year end, especially in the manufacturing and trade, transportation and utilities sectors, generating renter demand in the near term. Additionally, Walmart plans to expand its Chicago footprint over the next five years, creating up to 12,000 positions. Fundamentals show greater steadiness marketwide, but improvements vary significantly at the submarket level. In the city, owners in the Gold Coast submarket continue to record tight occupancy rates and slower concession rises due to the release of pent-up Class A demand from young professionals. Competition from foreclosures and shadow rentals in the City West submarket has driven up concessions steadily and kept the vacancy rate above 10 percent. In general, renters continue to opt for more affordable units in the suburbs, specifically in East and West Lake counties, resulting in recent rises in both occupancy and rents.

Firming confidence among small, local investors has supported acquisitions of assets with eight or fewer units. Buyers have targeted these properties in the city's Belmont-to-Montrose submarket due to stable renter demand, low vacancy rates and price declines of more than 20 percent from peak levels to approximately \$180,000 per unit. Similarly, a 12 percent year-over-year decline in the median price has generated greater investor interest for smaller assets in the close-in suburban areas of Oak Park and Glenview/Evanston. Deal flow involving large apartment properties, however, remains slow due to financing hurdles, with most buyers seeking either assets in the city offered with first-year yields at 8 percent or properties in the Oak Park submarket, where cap rates average 30 basis points above the city rate.

## 2010 ANNUAL APARTMENT FORECAST



**Employment:** Though the choppy start to the employment recovery will moderate Chicago payroll growth in 2010, area companies will still expand head counts by 40,000 positions, or 1 percent, following the elimination of 234,400 positions last year.



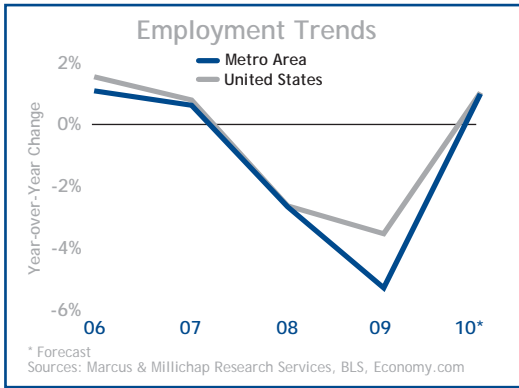
**Construction:** After developers expanded metrowide apartment inventory by 1,960 units in 2009, construction output will accelerate to 2,300 units this year. Over the past five years, completions averaged 1,500 units annually.



**Vacancy:** Despite growing inventory, rising employment levels will support a 10 basis point improvement in vacancy to 6.6 percent in 2010. The vacancy rate jumped 130 basis points last year.

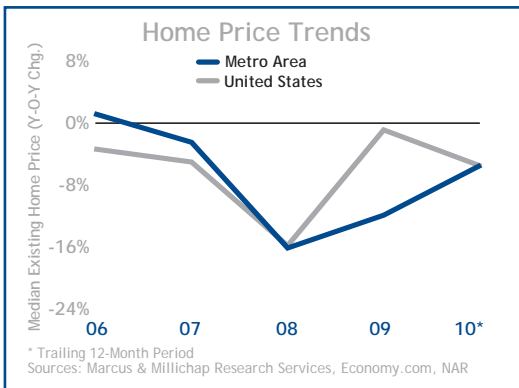


**Rents:** Sufficiently stabilized demand will allow local operators to raise asking rents 1.4 percent to \$1,047 per month this year, while effective rents will appreciate 2.5 percent to \$975 per month. In 2009, asking rents fell 3.5 percent, and effective rents regressed 4.5 percent.



## ECONOMY

- ◆ Job losses late in the second quarter wiped out a significant portion of the gains recorded earlier this year. Thus far in 2010, employers have added 6,600 positions, a 0.2 percent increase and a considerable improvement from the second half of 2009, when 78,900 workers were let go.
- ◆ So far this year, layoffs have been most acute in the leisure and hospitality and other services industries, which have contracted by a combined 5,500 jobs, or 0.9 percent; a total of 10,900 jobs were cut in these sectors during the previous six months. The greatest gains, conversely, have been in the trade, transportation and utilities and education and health services industries, where employers have added 12,800 workers to date, a 0.9 percent increase.
- ◆ Permitting activity suggests builders expect weak housing demand through mid-2011, despite the improving economy. The number of single-family permits requested in the past year decreased 57 percent to 5,140 units, while multifamily permit issuance slumped 74 percent to 3,220 units.
- ◆ Falling home prices continue to encourage sales. The median price of an existing single-family home declined 5 percent in the last year to \$189,710, raising homes sales by 64 percent. In the previous year, the median price fell 20 percent, and sales increased 22 percent.
- ◆ **Outlook:** Though the choppy start to the employment recovery will moderate Chicago payroll growth in 2010, area companies will still expand head counts by 40,000 positions, or 1 percent, following the elimination of 234,400 positions last year.



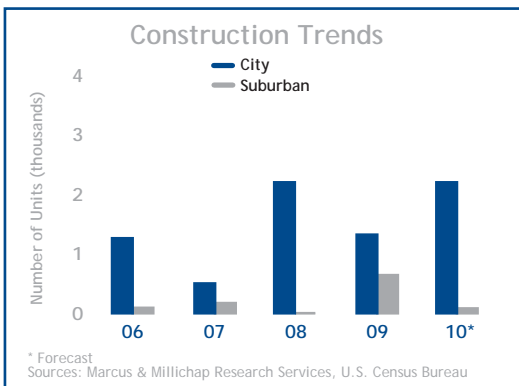
## CONSTRUCTION

### CITY

- ◆ Builders added 2,325 rental units to inventory in the city over the past 12 months, after delivering just over 2,000 apartments during the prior year.
- ◆ There are 580 units under construction in the Loop, with deliveries stretching into early next year, and another 1,900 units are planned for the area.
- ◆ **Outlook:** City apartment stock will grow by 2,210 units in 2010, after 1,320 units came online last year.

### SUBURBAN

- ◆ In the 12-month period ending in the second quarter, developers delivered just 84 units to suburban apartment stock. Construction output climbed to 644 apartments in the previous year.
- ◆ Proposed construction in the suburbs totals 5,450 units in 21 projects, none of which have a target groundbreaking date yet. The planning pipeline is largest in the Glenview/Evanston submarket, where 1,720 units are slated for construction.
- ◆ **Outlook:** The second quarter delivery of the 84-unit Commons at Town Center in Vernon Hills will be the only completion this year in the suburbs. Since 2000, construction efforts in the area have yielded an average of 780 units annually.



## VACANCY AND RENTS

### CITY

- ◆ Vacancy fluctuated within a narrow band in recent quarters. The second quarter rate of 6.8 percent was 30 basis points lower than at the start of 2010 but unchanged on a year-over-year basis.
- ◆ In the city, asking rents have appreciated 1.1 percent year to date to \$1,168 per month, while effective rents have improved 1.9 percent to \$1,081 per month. During the second half of 2009, asking and effective rents retreated 1.5 percent and 1.9 percent, respectively.
- ◆ **Outlook:** After increasing 50 basis points last year, vacancy in the city will rise 40 basis points to 6.9 percent in 2010. Asking rents will grow 1.7 percent to \$1,175 per month, and effective rents will gain 2.9 percent to \$1,092 per month.

### SUBURBAN

- ◆ In the first half of 2010, the improving economy supported a 40 basis point decline in the suburban vacancy rate to 6.4 percent. During the previous six months, vacancy ticked up 10 basis points.
- ◆ So far this year, asking rents have remained flat at \$961 per month, while owners have withdrawn concessions and raised effective rents 1 percent to \$894 per month. Asking rents slid 1.5 percent in the last half of 2009, and effective rents fell 1.8 percent.
- ◆ **Outlook:** Declining construction efforts will underpin a 30 basis point decrease in vacancy to 6.5 percent in 2010, after the rate surged 170 basis points last year. Asking rents will rise 0.9 percent to \$970 per month this year, and effective rents will climb 2.2 percent to \$905 per month.

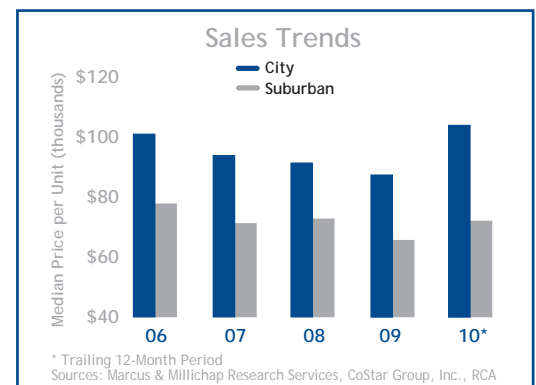
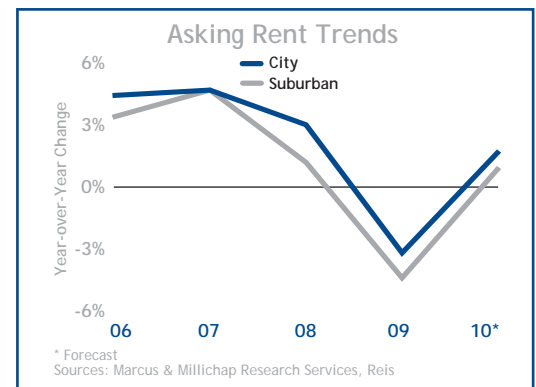
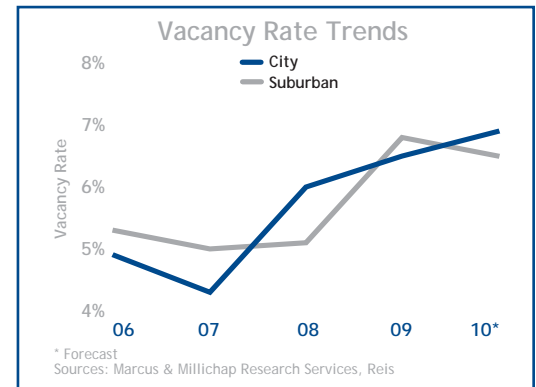
## SALES TRENDS\*\*

### CITY

- ◆ Sliding prices and economic improvements maintained steady investor demand for in-city properties over the past 24 months. The number of sales decreased by nearly half in the previous year.
- ◆ A surge in trades of smaller assets boosted the median price 23 percent to \$103,160 per unit during the most recent 12-month period. The median price for properties with more than eight units remained near \$59,000 per unit.
- ◆ **Outlook:** Though few stabilized Class A apartment assets trade, limited for-sale supply and stabilizing operations will keep cap rates in the mid- to high-6 percent range through the end of the year.

### SUBURBAN

- ◆ Deal flow in the suburbs slipped 27 percent during the most recent one-year stretch, after decreasing 42 percent in the preceding 12 months.
- ◆ The suburban median price increased 14 percent to \$71,230 per unit in the last year due to rising valuations and a greater percentage of smaller property sales. During the previous 12 months, the median price fell 14 percent.
- ◆ **Outlook:** While the near-in Oak Brook submarket remains popular with investors, tight occupancy, below-market rents and a stabilizing economy will likely attract buyers seeking to add value to the neighboring O'Hare area.



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

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## NATIONAL MULTI HOUSING GROUP

Visit [www.NationalMultiHousingGroup.com](http://www.NationalMultiHousingGroup.com) or call:

**Linwood C. Thompson**

Senior Vice President, Managing Director

National Multi Housing Group

Tel: (678) 808-2700

[lthompson@marcusmillichap.com](mailto:lthompson@marcusmillichap.com)

# Marcus & Millichap

## Real Estate Investment Services

Prepared and edited by

**David Delich**

Research Analyst

Research Services

For information on national apartment trends, contact

**John Chang**

Vice President, Research Services

Tel: (602) 687-6700 ext. 6803

[john.chang@marcusmillichap.com](mailto:john.chang@marcusmillichap.com)

*Chicago Office:*

**Greg LaBerge**

Regional Manager

[glaberge@marcusmillichap.com](mailto: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](mailto: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](mailto:sweinstock@marcusmillichap.com)

One Mid America Plaza, Suite 200

Oakbrook Terrace, Illinois 60181

Tel: (630) 570-2200

Fax: (630) 570-2210

**Price:** \$150

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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.

## CITY VACANCY RANKING

Rank	Submarket	Vacancy Rate	Y-O-Y Basis Point Change	Effective Rents	Y-O-Y % Change
1	Lincoln Park	3.6%	-20	\$1,132	-1.0%
2	Belmont-to-Montrose	4.1%	10	\$1,136	1.3%
3	Rogers Park/Uptown	5.5%	40	\$751	-2.8%
4	Gold Coast	6.7%	70	\$1,550	1.0%
5	South Shore	6.7%	60	\$844	-1.9%
6	City West	11.0%	60	\$965	5.0%
7	The Loop	11.8%	-150	\$1,476	-4.8%

## SUBURBAN VACANCY RANKING

Rank	Submarket	Vacancy Rate	Y-O-Y Basis Point Change	Effective Rents	Y-O-Y % Change
1	O'Hare	4.2%	-30	\$800	-2.4%
2	Wheeling	4.9%	-110	\$961	0.4%
3	Glenview/Evanston	5.5%	-100	\$975	-1.6%
4	Southwest Cook County	5.6%	30	\$759	-0.8%
5	Woodridge/Lisle	5.7%	-60	\$877	-2.3%
6	Aurora/Naperville	5.8%	-100	\$961	-0.8%
7	Southeast Cook County	5.9%	0	\$758	-0.5%
8	Schaumburg/Hoffman	6.1%	-40	\$914	-2.5%
9	Glendale Heights/Lombard	6.2%	70	\$1,020	1.7%
10	Joliet	6.5%	10	\$740	-0.1%
11	East Lake County	6.7%	-40	\$909	-0.4%
12	West Lake County	6.8%	-140	\$856	0.7%
13	Kane County	7.1%	0	\$931	0.3%
14	Oak Park	7.6%	-90	\$877	-0.5%
15	Downers Grove	8.6%	-20	\$875	1.3%