

DESPITE PRICING GAP, INVESTMENT ACTIVITY SETTLING

Apartment operating fundamentals in the Brooklyn apartment market have closely followed job losses. Steep employment reductions in the fourth quarter of 2008 resulted in a substantial increase in vacancy at large, market-rate properties during the first quarter. Since then, a still-elevated but milder pace of job cuts has underpinned less dramatic swings in rents and vacancy, with vacancy improving in the second quarter due to the efficient use of rent decreases. Operations in many submarkets have been influenced by how much rents appreciated during the recent redevelopment boom. In Bath Beach, Bensonhurst and Bay Ridge, for instance, renewal efforts were limited, and rents grew in tandem with demand rather than the completions of new, high-priced units. As a result, leasing challenges are present in these neighborhoods, but declines in fundamentals are modest. Conversely, owners in Prospect Heights, Park Slope, Clinton Hill and Fort Greene are reducing rents by as much as 15 percent year over year to combat potential vacancy spikes from new or over-priced apartment product.

Although it is unlikely that velocity and prices have reached a bottom, signs of stability are surfacing in the borough. Among properties with fewer than six units, more stringent lending standards have cut out less sophisticated buyers and owner-users. As a result, deal flow in these assets has steadied over the past 12 months, as experienced local investors with sufficient cash or established relationships with lenders have become more active. Alternately, sales of properties with six or more units continue to decline in response to credit availability, though values are stable, with the median price hovering near \$108,000 per unit over the past 24 months. Investors should note, however, that more than 70 percent of for-sale properties in this segment are listed at higher per-unit prices. This persistently wide bid-ask gap likely means that a recovery of the local investment market is still a few of quarters away.

2009 ANNUAL APARTMENT FORECAST



Employment: A total of 103,800 positions will be eliminated citywide in 2009, a 2.8 percent decline. Last year, 27,200 workers were let go.



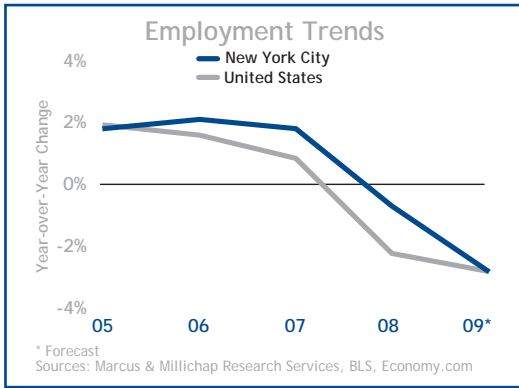
Construction: Multi-family permit issuance has fallen 90 percent year over year and, as a result, construction output will be limited in 2009 and beyond.



Vacancy: As job losses continue to weaken renter demand, vacancy in large, free-market buildings is forecast to climb 110 basis points to 2.9 percent in 2009, after the rate improved 140 basis points last year.



Asking Rents: Asking rents are projected retreat 3 percent to \$1,397 per month this year, following a 4.8 percent gain in 2008.

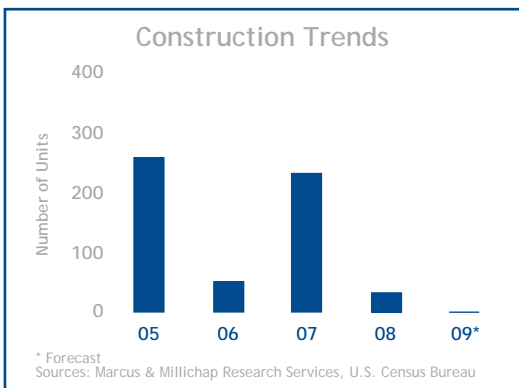


ECONOMY

- ◆ While cuts have eased over the past two quarters, New York City employers continue to shed a significant number of workers. In all five boroughs, 147,400 positions have been eliminated since the third quarter of 2008, a 3.9 percent decrease. In the previous 12 months, 57,200 jobs were created.
- ◆ Office-using employment across the city has fallen 5.2 percent in the last year, charting a sharper decline than the total work force.
- ◆ In August, the citywide unemployment rate surged 80 basis points to 10.3 percent, 440 basis points higher than one year earlier.
- ◆ Job losses are eroding income levels and lowering the amount of money residents are able to spend on housing expenses. In the past year, the median household income has receded 6.5 percent to \$58,400 annually.
- ◆ **Outlook:** A total of 103,800 positions will be eliminated citywide in 2009, a 2.8 percent decrease. Last year, 27,200 workers were let go.

HOUSING TRENDS

- ◆ Multi-family permitting activity, an indicator of future supply growth, has declined markedly in Brooklyn. Over the last 12 months, the number of permits requested has fallen 90 percent to 1,418 units, as developers expect decreased household creation and softer residential demand. The drop-off also is attributable to a high level of permit issuance one year ago, prior to the expiration of the 421a tax abatement program.
- ◆ Lackluster sales trends persist in the Brooklyn condominium market. Year over year, sales velocity has plummeted more than 46 percent, while sellers have increased the average listing discount from 3.4 percent of the asking price to 7.0 percent of the asking price. Sizable price cuts at newer developments in particular have generated a boroughwide 7.7 percent decline in the median price to \$475,280 per unit over the past year.
- ◆ Plans have been revived for the mixed-use City Point development on the site of the former Albee Square Mall. Construction on the first phase could start as soon as early 2010, and the project could add up to 260 free-market and 120 affordable units downtown.
- ◆ The Edge, located in Williamsburg, is the largest condominium development under way in the borough, with completion slated for the fourth quarter of this year. Once-robust purchasing activity at the project has moderated, however, and dozens of units remain available.
- ◆ **Outlook:** Approximately 1,540 condominium units will be added to borough stock in 2009, with as many as 360 units coming online in the first half of next year. Given plummeting sales activity and the expanding for-sale inventory, the threat of shadow rental stock will likely persist.



CONSTRUCTION

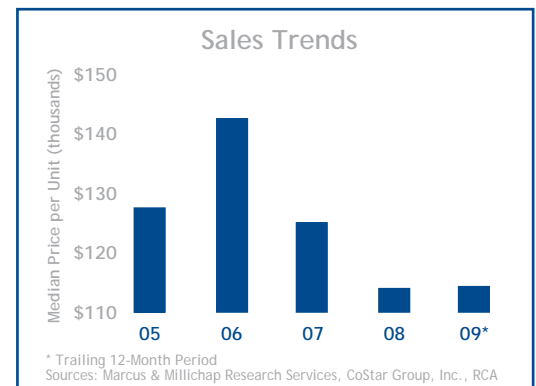
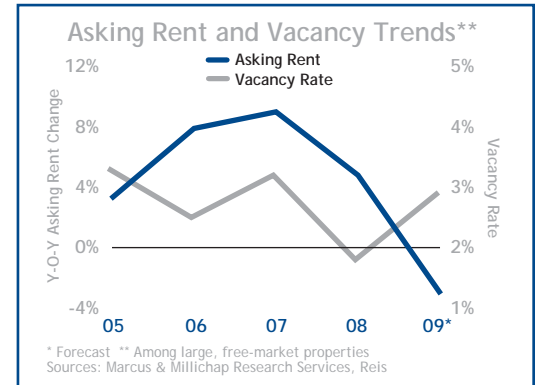
- ◆ There were no deliveries of large, free-market apartment buildings during the 12-month period ending in the third quarter of 2009. In the previous year, one 32-unit complex was added to the borough's inventory.
- ◆ Developers have three projects consisting of approximately 1,500 free-market units under construction in Brooklyn. Although no completions are scheduled for the remainder of this year, two-thirds of the units under way are expected to come online in 2010.
- ◆ More than 500 free-market units are under construction at unnamed development sites. Both the 142-unit building at 34 Berry Street in northern Williamsburg and the 365-unit complex at 80 Dekalb Avenue in Fort Greene are slated to be completed in the second quarter of next year.
- ◆ There are three major projects with a total of 580 units planned throughout Brooklyn, though falling rents and a lack of construction capital may prevent some of these developments from progressing.
- ◆ **Outlook:** After 32 free-market apartment were brought online in 2008, no major rental projects are expected to be completed in the borough this year.

VACANCY AND RENTS

- ◆ In large, free-market buildings, the vacancy rate was a still-healthy 2.7 percent in the third quarter, 80 basis points higher than one year earlier. After surging in the first quarter of the year, vacancy has declined 150 basis points over the past six months due to a spike in tenant demand.
- ◆ As apartment demand remains soft, owners are cutting rents. In the past 12 months, asking rents at large, free-market properties have receded 1.8 percent to \$1,401 per month.
- ◆ **Outlook:** Job losses will continue to erode renter demand, driving up vacancy in large, free-market buildings 110 basis points to 2.9 percent in 2009, after the rate improved 140 basis points last year. Asking rents, in turn, are forecast to retreat 3 percent to \$1,397 per month this year, following a 4.8 percent gain in 2008.

SALES TRENDS**

- ◆ Though deal flow continues to slow, the deceleration is easing. Over the past year, sales activity has dropped 30 percent, compared with a nearly 50 percent decrease during the previous 12 months that was due to limited financing and buyer hesitancy.
- ◆ In the last year, the median price has ticked up slightly to \$114,290 per unit, after declining 19 percent in the preceding 12-month period.
- ◆ After cap rates averaged in the low- to mid-6 percent range for most of 2009, initial yields are climbing and will likely near 7 percent by year end.
- ◆ **Outlook:** Many sellers have yet to come to terms with current market conditions and lower property values. Buyers are more likely to find realistically priced apartment properties in areas where renewal efforts were fleeting and price escalation was brief, such as Crown Heights and eastern Bedford-Stuyvesant.



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

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CAPITAL MARKETS

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- ◆ Compared to other core property sectors, apartments have fared best due to the availability of financing through government-sponsored enterprises (GSEs) Fannie Mae and Freddie Mac. Recent modifications to GSE guidelines will impact lender decisions, however, as borrower requirements include more substantial apartment ownership experience.
- ◆ Loan-to-value requirements range from 55 percent to 75 percent. Portfolio lenders are issuing loans at all-in rates of 6.00 percent to 6.75 percent for a five-year term and 6.9 percent to 8.0 percent for a 10-year term. Rates among agency lenders are roughly 100 basis points to 150 basis points lower. The government's creation of a conservatorship for Fannie Mae and Freddie Mac has most likely boosted confidence in the two GSEs, putting downward pressure on rates, but it also creates several near-term uncertainties, as the conservatorship is due to expire at the end of the year.
- ◆ Delinquencies will rise further as a wave of maturities approaches; however, at-risk borrowers may find lenders amenable to loan extensions/modifications. Furthermore, Freddie Mac is under way on its second securitization of multi-family debt this year, and the government's TALF program is expected to at least provide a much-needed spark to the traditional CMBS market.

BROOKLYN SALES HIGHLIGHTS

Property Address	Sales Price	Number of Units	Price per Unit	Price per Square Foot
3030 Ocean Avenue	\$13,000,000	86	\$151,163	\$156
333 Ovington Avenue	\$11,225,000	119	\$94,328	\$122
390 Lorimer Street	\$10,000,000	28	\$357,143	\$292
75 Bushwick Avenue	\$6,733,452	96	\$70,140	\$44
419 16th Street	\$4,200,000	16	\$262,500	\$355
951 Carroll Street	\$3,375,000	43	\$78,488	\$110
40 E. 17th Street	\$3,300,000	42	\$78,571	\$78
84 Lawrence Avenue	\$3,150,000	35	\$90,000	\$98
1280-1288 Dean Street	\$3,150,000	32	\$98,438	\$90
3813-3821 18th Avenue	\$2,800,000	31	\$90,323	\$98
1455 E. 68th Street	\$2,040,000	23	\$88,696	\$92
1852 67th Street	\$1,900,000	19	\$100,000	\$133
239 Prospect Place	\$1,750,000	12	\$145,833	\$204
29 Meserole Street	\$1,730,000	8	\$216,250	\$220
334 Dean Street	\$1,545,000	12	\$128,750	\$227
906 Avenue S	\$1,375,000	12	\$114,583	\$132
209 Avenue F	\$1,300,000	16	\$81,250	\$74
1608 Mermaid Avenue	\$980,000	7	\$140,000	\$144
2033 78th Street	\$955,000	6	\$159,167	\$171
60 Sixth Avenue	\$950,000	8	\$118,750	\$168
1628 11th Avenue	\$918,333	2	\$459,167	\$283
402 Franklin Avenue	\$900,000	7	\$128,571	\$446
572 Pacific Street	\$850,000	10	\$85,000	\$347
237 Troy Avenue	\$645,000	8	\$80,625	\$107
824 Classon Avenue	\$630,000	8	\$78,750	\$110
122 33rd Street	\$595,000	6	\$99,167	\$93