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

Marcus & Millichap

Los Angeles County *Fourth Quarter 2009*

Buyers Anticipating Opportunities upon Economic Rebound

Like much of Southern California, Los Angeles County is besieged by severe job losses, a battered housing market and falling household incomes. Apartment property fundamentals are softening as a result, despite a significant decline in new construction. Countywide, only 2,000 new rental units will be delivered this year, down from an average of approximately 4,500 units annually during the past five years. While supply-side pressures are easing, areas where much of the county's new stock has come online in recent years, specifically the San Fernando Valley and downtown, will record annual renter demand drop-offs for the first time since the recession in the early part of this decade. Consequently, vacancy will rise and rents will decrease in nearly every submarket in the county this year, although conditions should begin to stabilize in mid-2010. Operating fundamentals are expected to be the strongest in Class B/C properties, as renter demand for affordable housing has slowed at a more modest pace than in the region's top-tier assets.

Buyers have responded to softening operating fundamentals and uncertainty in the economy by curtailing investment activity in Los Angeles County, but recent data suggests the market may be stabilizing, and a normalized level of sales velocity could return in the coming months. After a steep decline in late 2008 and early 2009, the investment market has gained momentum. During the second quarter, sales velocity spiked by more than 30 percent from the first three months of the year, and similar activity has been recorded thus far in the second half of 2009. As the recession begins to wind down, many investors are preparing for a recovery and positioning themselves to deploy accumulated capital. Average cap rates are in the low- to mid-6 percent range for properties that are not in distress, as much as 150 basis points above initial yields during the height of the market. Cap rates could inch up further, particularly in larger assets for which there are fewer active players, and in newer properties that typically face greater competition from existing assets and where anticipated rent gains failed to materialize.

2009 Annual Apartment Forecast

4.1% decrease in total employment

Employment: Countywide employment is forecast to contract by 4.1 percent in 2009 as employers shed 162,000 jobs. Next year, payrolls are expected to expand marginally.

2,000 units will be completed

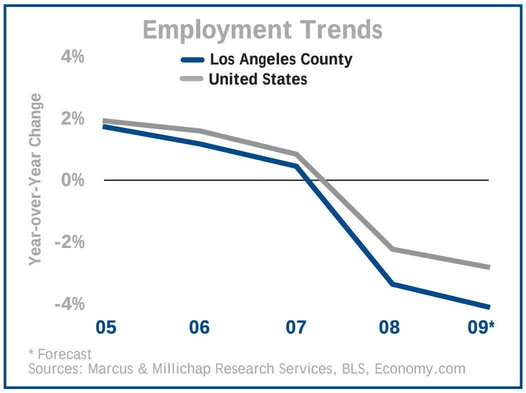
Construction: Following the delivery of 4,600 units in 2008, developers will complete 2,000 apartments this year, increasing countywide inventory by 0.3 percent. Similar stock growth is anticipated for 2010.

130 basis point increase in vacancy

Vacancy: Employers are forecast to contract payrolls through the end of the year, restricting renter demand for apartments. Vacancy is expected to rise 130 basis points in 2009 to 5.8 percent, following a 90 basis point increase last year.

3.8% decrease in asking rents

Rents: Easing tenant demand and the soft economy are projected to drive down asking rents 3.8 percent this year to $1,407 per month, while effective rents are forecast to retreat 6.7 percent to $1,316 per month. In 2010, rents will likely be flat.



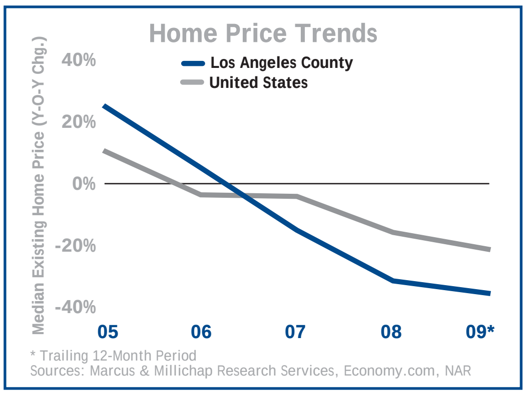
Economy

- Year over year through the third quarter, employers shed an estimated 187,300 workers, a 4.6 percent decline. Year-to-date losses have totaled approximately 126,800 jobs, although contraction is expected to slow modestly in the fourth quarter.

- Education and health services is the only sector that has expanded in the metro on both a year-to-date and year-over-year basis. Roughly 4,300 positions have been added in the past 12 months, a 0.9 percent increase, with 3,200 of those jobs created in 2009. Growth is slowing, however, as the sector added more than 7,600 employees in 2008.

- Unemployment in Los Angeles County reached 12.6 percent in August, up approximately 500 basis points from one year earlier. In that time, nearly 44,000 employees were cut in the trade, transportation and utilities sector, the metro's largest segment, due to steep declines in export activity.

- **Outlook:** Countywide employment is forecast to contract by 4.1 percent in 2009 as employers shed 162,000 jobs. Next year, payrolls are expected to expand marginally.



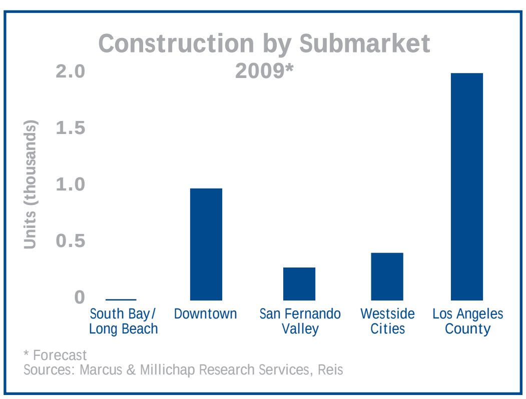
Housing and Demographics

- In the past 12 months, developers have pulled permits for approximately 2,400 single-family units, a 47 percent decline from the previous year. Multi-family permit issuance has declined by 50 percent in the past year to fewer than 4,900 units.

- The median single-family home price in Los Angeles County contracted 36 percent in the past year to an estimated $220,800 in the third quarter. Home prices have retreated to year-end 2001 levels.

- While home prices have fallen, the median household income has dropped 4.3 percent in the last 12 months to $50,500 per year, approximately $4,900 less than the amount required to purchase a median-priced residence, using traditional financing. The average Class A asking rent is now $600 per month more than the typical mortgage payment on a median-priced home.

- **Outlook:** Single-family homes are increasingly affordable, which will likely drive some renters to ownership. Also putting downward pressure on apartment rents are investors purchasing single-family homes for use as shadow rentals.



Construction

- During the past 12 months, roughly 1,700 apartment units have been completed countywide, down from more than 6,100 units one year earlier.

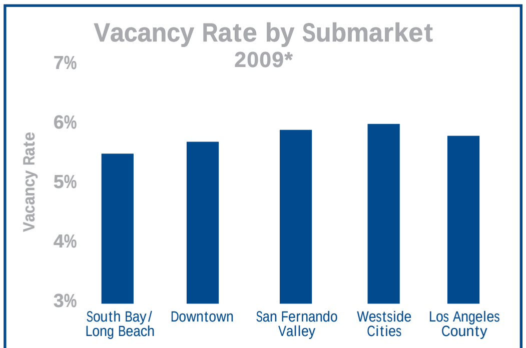
- Of the 2,200 rentals that are under construction in Los Angeles, 650 units are scheduled to be delivered in the fourth quarter of 2009. There are 10,500 apartment units planned in the metro.

- The 374-unit Hollywood and Vine apartment complex is the largest development under construction. The project is scheduled to be completed in the fourth quarter in the Hollywood/Silver Lake submarket.

- **Outlook:** Following the delivery of 4,600 units in 2008, developers will add 2,000 apartments this year, increasing countywide inventory by 0.3 percent. Similar stock growth is anticipated for 2010.

Vacancy

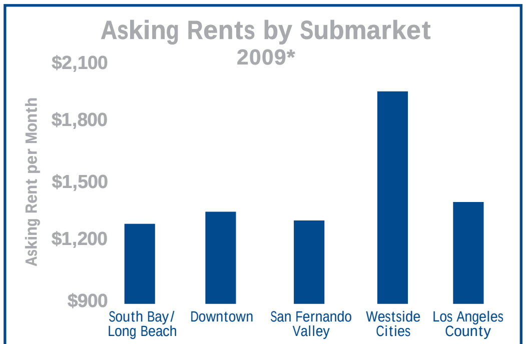
- Vacancy increased 140 basis points year over year to an estimated 5.7 percent through the third quarter, as demand has contracted due to steep job losses. Year to date, vacancy is up 120 basis points.
- As renter demand for apartments has lagged deliveries during the past year, Class A vacancy has increased 100 basis points to 7.4 percent. Vacancy in the top tier could continue to tick higher as home prices drop and renters move into homeownership.
- Vacancy in the county's Class B/C assets has spiked 170 basis points to 5.1 percent year over year, as many renters who have lost jobs are doubling up. Year to date, vacancy in the lower tiers has jumped 150 basis points.
- **Outlook:** As payrolls continue to contract, demand will wane and vacancy is expected to rise 130 basis points in 2009 to 5.8 percent. Last year, vacancy ticked up 90 basis points.



* Forecast
Sources: Marcus & Millichap Research Services, Reis

Rents

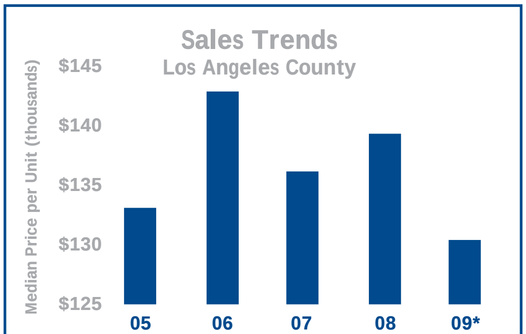
- Asking rents ended the third quarter at an estimated $1,418 per month, 3.4 percent lower than one year earlier. Effective rents have declined 5.8 percent in the past 12 months to $1,338 per month.
- Year over year, asking rents in Class A properties have retreated 4.9 percent to $1,860 per month, while asking rents in the lower tiers have dipped 2.5 percent to $1,223 per month.
- In the last 12 months, concessions have increased from 12 days of free rent to 20 days of free rent. Average revenues have fallen 7.2 percent during the past year and are forecast to approach 8 percent by the end of 2009.
- **Outlook:** Easing tenant demand and the soft economy are projected to drive down asking rents 3.8 percent this year to $1,407 per month, while effective rents are forecast to retreat 6.7 percent to $1,316 per month. In 2010, rents will likely be flat.



* Forecast
Sources: Marcus & Millichap Research Services, Reis

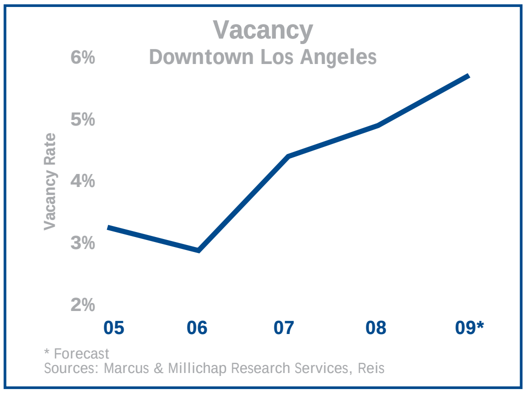
Sales Trends**

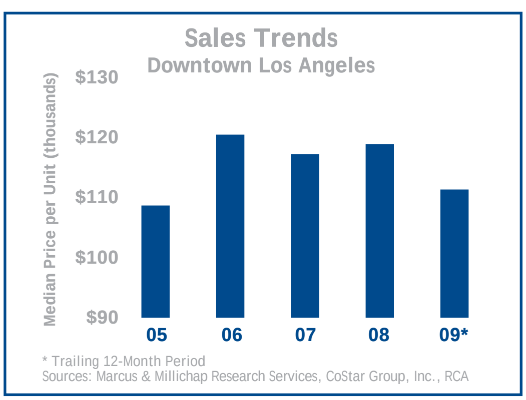
- In the past year, sales velocity has dropped 32 percent. As fundamentals have softened, owners have been reluctant to list properties at market prices, and lenders are underwriting deals more cautiously.
- The median price has receded 7 percent over the last 12 months to $130,300 per unit. In deals closed thus far in 2009, however, the median price has been $129,400 per unit.
- Stabilized properties are trading at average cap rates in the low- to mid-6 percent range, while distressed assets or properties with above-average vacancy levels are changing hands with initial yields of 8 percent or higher.
- **Outlook:** While fundamentals and NOIs will likely continue to soften in the coming quarters, vacancy should remain low enough to keep most properties performing soundly, sustaining buying activity. With cap rates rising, some private and institutional investors who left the area when initial yields were at their lowest may once again become active in the metro.



* Trailing 12-Month Period
Sources: Marcus & Millichap Research Services, CoStar Group, Inc., RCA

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





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Downtown Los Angeles Apartment Market

Construction and Vacancy

- In the past 12 months, approximately 680 apartment units have been completed in downtown Los Angeles, following the delivery of more than 1,600 rentals one year earlier. Thus far in 2009, 460 units have come online.
- Roughly 730 units are under construction in the area, and 4,300 units are in the planning phases. Nearly 40 percent of the proposed units are located in the Wilshire/Westlake submarket.
- Year over year, vacancy has increased 90 basis points to 5.5 percent, including a 60 basis point rise year to date. Modest stock growth and a slight drop-off in renter demand have driven the vacancy uptick.
- **Outlook:** Approximately 975 apartments will come online this year, after 929 units were delivered in 2008. Vacancy is expected to rise 80 basis points to 5.7 percent, following a 50 basis point increase last year.

Rents

- Operators have lowered rents in response to waning demand and the soft economy. Asking rents retreated an estimated 4.7 percent year over year to $1,372 per month through the third quarter. Nearly all of the decline was recorded in 2009; year to date, asking rents are down 4.5 percent.
- With vacancy rising, effective rents have fallen 7 percent in the past year to $1,294 per month, and further contraction is likely. Concessions now account for three weeks of free rent, up from less than two weeks of free rent one year ago.
- Average revenues have dropped 7.9 percent during the last 12 months and are expected to fall 9.3 percent in 2009.
- **Outlook:** Asking rents are forecast to decrease 5.4 percent this year to $1,358 per month, while effective rents are on pace to decline 8.5 percent to $1,273 per month. In 2008, asking and effective rents ticked up 2.4 percent and 1.4 percent, respectively.

*Sales Trends***

- Year over year, investment activity in the Downtown area has dropped 33 percent, as renter demand has fallen off and revitalization efforts have slowed.
- During the past 12 months, the median price has decreased 6 percent to $111,100 per unit. The decline in valuations has accelerated; the median price in deals closed so far this year was $100,300 per unit.
- Average cap rates for all properties that have changed hands in 2009 are in the mid-7 percent range, approximately 150 basis points higher than the average in 2008. In transactions involving properties with fewer than 10 units, cap rates have been in the mid-6 percent range.
- **Outlook:** Investment activity in area apartment properties is expected to remain modest until employers begin to increase staffing levels and fundamentals firm.

Westside Cities Apartment Market

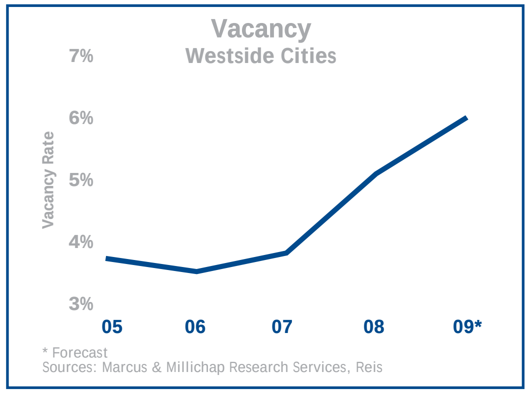
Construction and Vacancy

- Development in the Westside Cities has slowed considerably during the past 12 months, as approximately 500 apartments have come online, down from 1,560 units in the preceding annual period.

- There are fewer than 200 units under way in the area, with nearly all of the projects scheduled to come online in 2010 or later. The planning pipeline contains 1,800 units, 1,050 units of which are located in the Marina Del Rey/ Venice/Westchester submarket.

- Vacancy in the Westside Cities has increased 70 basis points year over year to 5.8 percent. Following an 80 basis point rise when job losses peaked in the first quarter, vacancy has retreated 10 basis points.

- **Outlook:** In 2009, developers are expected to complete 405 apartment units in the Westside Cities, down from more than 1,500 units last year. Despite slowing construction, vacancy is forecast to rise 90 basis points to 6 percent; vacancy jumped 130 basis points in 2008.



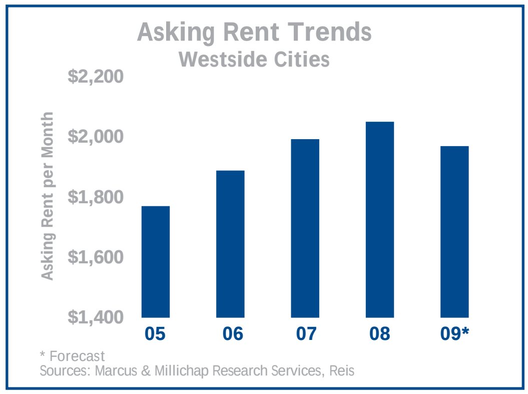
Rents

- Year over year, area asking rents have fallen 3.8 percent to $1,987 per month, as job losses have intensified, especially in some of the metro's higher-paying sectors. Asking rents have declined in each of the past four quarters.

- Effective rents have contracted 5.7 percent in the past year to $1,876 per month, as operators have increased leasing incentives in an effort to fill units. Average concessions have grown by one week in the last 12 months to 20 days of free rent.

- Average property revenues have dropped 6.4 percent during the past year as a result of falling rents. In 2010, completions are expected to slow further and rents should stabilize, which will likely keep revenues essentially flat.

- **Outlook:** Asking rents are forecast to decline 4 percent to $1,965 per month this year, and effective rents will slip 6.1 percent to $1,845 per month.



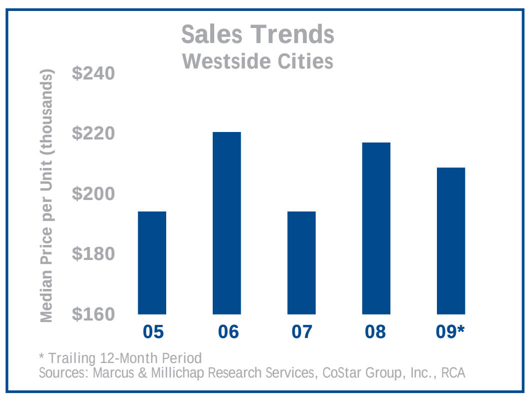
*Sales Trends***

- In the Westside Cities, investment activity has cooled 27 percent in the past 12 months and nearly 45 percent year to date. The area's high per-unit prices and falling rents have pushed buyers to the sidelines and increased lenders' caution for local properties.

- While revenues are retreating, the median price has remained fairly resilient, creeping down just 4 percent in the past 12 months to $208,300 per unit. During the last six months, the median price has slipped to $198,300 per unit, as rent cuts have accelerated.

- Cap rates have averaged approximately 6 percent thus far in 2009, roughly 100 basis points higher than during the second half of last year.

- **Outlook:** Institutions and REITs becoming more active in the coming quarters may lead to greater sales velocity in the Westside Cities, where the prevalence of Class A assets should appeal to large buyers.



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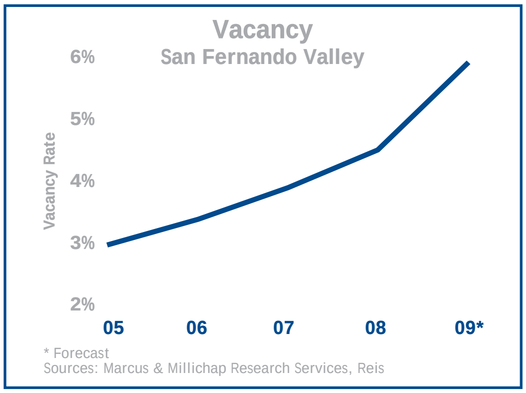
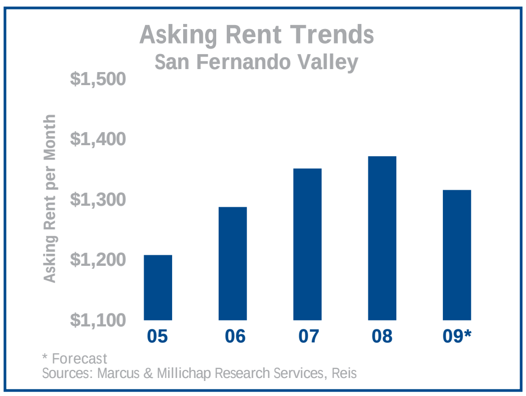
San Fernando Valley Apartment Market



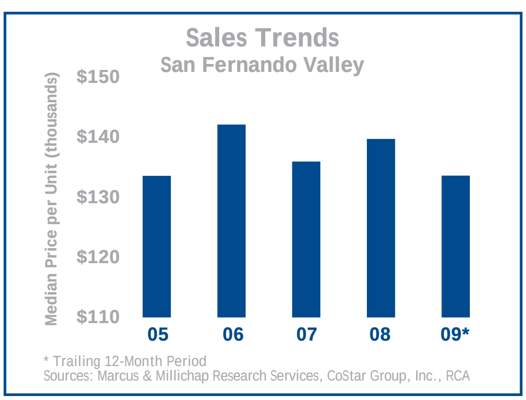
Construction and Vacancy

- Approximately 275 rental units were completed in the San Fernando Valley during the 12-month period ending in the third quarter, down more than 70 percent from year-earlier levels. No additional deliveries are scheduled for the remainder of 2009.
- The development pipeline consists of 625 apartment units currently under construction and 1,900 units in the planning stages.
- Preliminary forecasts place vacancy in the Valley at 5.5 percent in the third quarter, 110 basis points higher than 12 months earlier. Nearly all of the increase has occurred in 2009; year to date, vacancy is up 100 basis points.
- **Outlook:** After averaging nearly 1,100 units annually for the past three years, completions in the San Fernando Valley are expected to total just 275 units in 2009, increasing inventory by 0.2 percent. More than 600 units are forecast to be delivered in 2010. Vacancy is projected to rise 140 basis points to 5.9 percent this year, following a 60 basis point uptick in 2008.



Rents

- Asking rents in the San Fernando Valley retreated an estimated 2.9 percent year over year to $1,321 per month through September. Asking rent declines have accelerated in each of the past four quarters, although the pace is expected to moderate beginning in early 2010.
- As weakness in the economy has slowed household creation over the last 12 months, effective rents have dropped 4.9 percent to $1,262 per month. Year to date, concessions have increased by one week to 20 days of free rent.
- In the past year, average revenues in the San Fernando Valley have declined 9.2 percent, one of the largest drops in Los Angeles County. Early forecasts suggest renter demand for apartments will gain momentum in 2010, which should result in more stable property performance.
- **Outlook:** Area asking rents are projected to slip 4.1 percent this year to $1,314 per month, while effective rents are expected to approach 2006 levels by falling 6.4 percent to $1,235 per month.



Sales Trends**

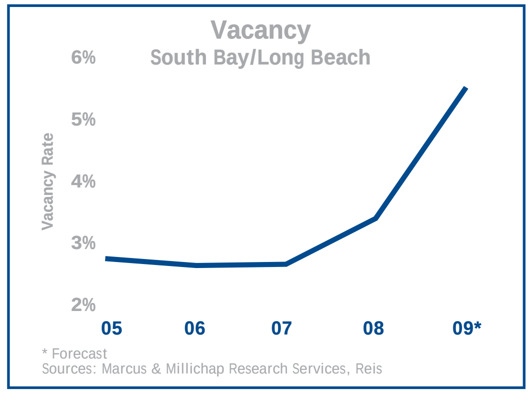
- During the past 12 months, sales velocity in the San Fernando Valley has slowed by 30 percent, although investment activity accelerated from the first quarter to the second quarter, and properties have changed hands at a steady pace so far in the second half.
- In the past year, the median price has retreated 4 percent to $133,400 per unit. Buyers primarily have pursued top properties in 2009, causing the median price to tick up to $142,300 per unit in deals closed year to date.
- Cap rates are averaging in the mid- to high-6 percent range this year. In a few properties where vacancy has been near double digits, initial yields have averaged between 7.5 percent and 8.5 percent.
- **Outlook:** The San Fernando Valley is expected to record some the strongest household growth in Los Angeles County in the coming years, which should support investor demand for area properties.

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

South Bay/Long Beach Apartment Market

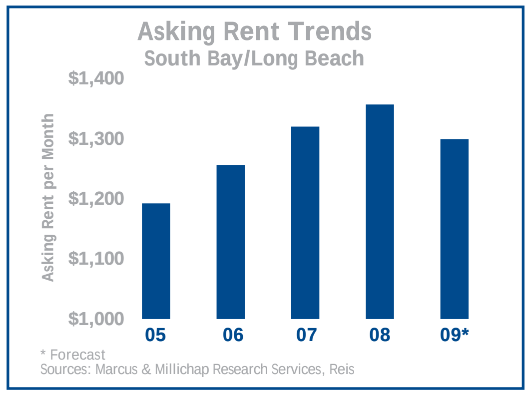
Construction and Vacancy

- Apartment development remains limited in the South Bay/Long Beach region. No new units have been delivered since the first quarter of 2008, and total inventory has increased by a scant 0.5 percent this decade.
- While development has been minimal in the area, there are a handful of commercial construction projects under way and planned in downtown Long Beach. The 265-unit West Gateway apartments broke ground earlier this year and will come online in the first half of 2010. An additional 128 rental units are proposed.
- Vacancy ended the third quarter at an estimated 5.2 percent, 200 basis points higher than one year earlier. Negative net absorption of nearly 2,000 units has been recorded year to date, as vacancy has spiked 180 basis points.
- **Outlook:** No new apartment completions are forecast for the South Bay/Long Beach region this year, although deliveries will pick up in 2010. Vacancy is expected to reach 5.5 percent by the end of 2009, a 210 basis point rise. The rate ticked up 70 basis points last year.



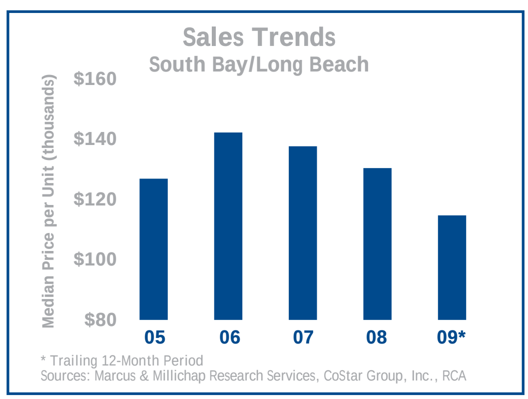
Rents

- In the past year, asking rents have declined 3.3 percent to $1,310 per month. Effective rents have fallen 5.8 percent to $1,245 per month, as owners have increased concessions in response to waning renter demand.
- The rises in vacancy and concessions have resulted in a 7.7 percent decline in average revenues in the past 12 months; by the end of this year, annual revenue contraction is expected to exceed 8 percent.
- Operators in the Hawthorne/North Torrance submarket have benefited from growing demand for affordable apartments. The area, which has the lowest rents in the South Bay/Long Beach region, has been one of only a handful in the county to record an effective rent increase during the past year.
- **Outlook:** Asking rents are forecast to drop 4.3 percent this year to $1,297 per month, and effective rents will contract 6.3 percent to $1,229 per month.



Sales Trends**

- Year over year, transaction activity in the South Bay/Long Beach area has dropped 70 percent, as reduced port activity has caused renter and investor demand to ease. During the first half of 2009, sales velocity fell 40 percent from the same period last year.
- As buyer demand has softened and fundamentals have weakened, the median price has decreased 12 percent year over year to $114,300 per unit.
- Cap rates have averaged in the mid-6 percent to mid-7 percent range for most properties that have changed hands this year, approximately 90 basis points higher than at the end of 2008.
- **Outlook:** With the development pipeline limited, competition stemming from new deliveries is minimal in the South Bay/Long Beach area. As the local economy recovers and renter demand picks up, fundamentals in existing properties should recover at an above-average pace, which will support future valuations.



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Capital Markets

By WILLIAM E. HUGHES, Senior Vice President, Marcus & Millichap Capital Corporation

- 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.

Submarket Vacancy Ranking

Rank	Submarket	Vacancy Rate	Y-O-Y Basis Point Change	Effective Rents	Y-O-Y % Change
1	Panorama Hills/San Fernando/Pacoima	3.7%	60	$1,041	-1.5%
2	Mid-City/West Adams/Pico Heights	3.7%	50	$1,031	-0.2%
3	Hollywood/Silver Lake	3.8%	110	$1,367	-2.8%
4	South/Central L.A.	3.8%	80	$902	-3.4%
5	East L.A./Alhambra/Montebello/Pico Rivera	3.8%	40	$1,083	-2.8%
6	Mar Vista/Palms/Culver City	4.1%	90	$1,438	-4.1%
7	Hawthorne/North Torrance	4.1%	80	$987	0.5%
8	Van Nuys/North Hollywood	4.4%	140	$1,066	-1.5%
9	Santa Monica	4.4%	150	$2,359	2.3%
10	Chatsworth/Canoga Park	4.5%	-110	$1,234	0.3%
11	El Segundo/Hermosa Beach/Redondo Beach	4.6%	230	$1,704	-1.2%
12	Carson/San Pedro/East Torrance/Lomita	4.6%	230	$1,125	-3.3%
13	Paramount/Downey/Bellflower/Norwalk	4.9%	140	$1,177	-0.8%
14	Inglewood/Crenshaw	5.0%	70	$969	-3.5%
15	East Long Beach/Los Altos	5.0%	180	$1,358	-4.3%
16	Beverly Hills/W. Hollywood/Park La Brea	5.2%	-90	$1,791	-1.5%
17	Tujunga/La Crescenta/Montrose	5.4%	320	$1,225	-2.6%
18	Burbank/North Glendale	5.5%	280	$1,408	-0.4%
19	North Long Beach/Lakewood/Artesia	5.5%	190	$1,153	-3.9%
20	West Torrance/Ranchos Palos Verdes	5.6%	280	$1,489	-2.8%
21	West L.A./Westwood/Brentwood	5.7%	160	$2,186	-3.0%