

OUT-OF-STATE BUYERS DRIVING INVESTMENT ACTIVITY

Heavy job losses and increased construction activity have weakened fundamentals in the Oklahoma City apartment market. Heavy supply-side pressure in the first half of 2009 drove vacancy to the highest rate in seven years. Consequently, owners have offered greater concessions to counteract waning demand. Incentives amount to roughly 19 days of free rent, with the largest offerings found in lower-tier properties located within the South and Northwest submarkets. Class B/C conditions throughout most of the market are being outpaced by those in the top tier, as considerable job losses in traditionally lower-paying industries have caused many renters to double up or move out of the metro. In the East Central submarket, for example, vacancy in Class A assets has fallen 310 basis points year over year, while Class B/C vacancy has climbed 60 basis points. Renter demand near the University of Oklahoma and the University of Central Oklahoma, however, will boost lower-tier occupancy levels in the Norman and Edmond submarkets. Early estimates for the third quarter indicated that Class B/C conditions in these areas outperformed upper-tier operations, due largely to students signing leases for the new school year.

Transaction velocity in Oklahoma City has slowed in the last year; however, unlike in other areas, this decrease is largely the result of a drop-off in activity from highly-leveraged local investors. The few area buyers active in the market are focusing on older complexes. Properties in the Northwest and Northeast submarkets are drawing the most interest from these investors; conditions in both areas are relatively weak and cap rates are elevated, as sellers are compensating for higher near-term risk. Out-of-state buyers, meanwhile, are targeting newer, stabilized assets in areas like Norman and along interstates 40 and 235 in the West Central submarket. As such, during the past 12 months, the average property sales price in deals involving regional buyers was \$13 million, while the average asset price in sales involving local investors, who favored older properties, was \$4.4 million.

2009 ANNUAL APARTMENT FORECAST



Employment: Oklahoma City was one of the few metros in the nation to add jobs in 2008, increasing head counts by 3,700 spots. Recessionary pressures are weighing on employment this year, however; roughly 13,500 jobs are expected to be cut from local payrolls in 2009, a 2.3 percent decline.



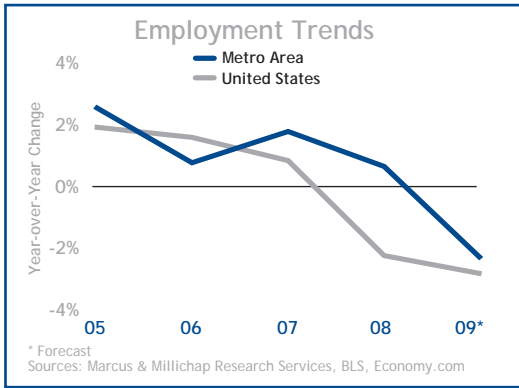
Construction: Approximately 670 units were projected to come online this year, all of which were delivered in the first three quarters. Total completions in 2009 are more than double the five-year annual average.



Vacancy: Vacancy in Oklahoma City is forecast to climb 110 basis points this year to 9.7 percent, the highest rate in seven years, as accelerating job losses are moderating renter demand.



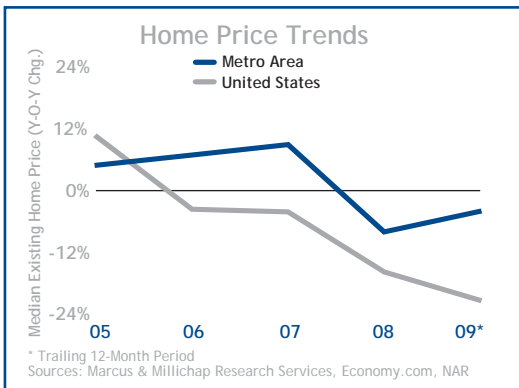
Rents: Owners will reduce rents and increase concessions in response to waning demand. Asking and effective rents are projected to end the year at \$541 per month and \$511 per month, drops of 0.4 percent and 1.5 percent, respectively, from 2008.



ECONOMY

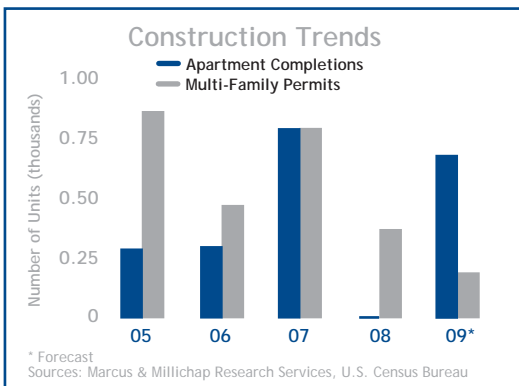
- ◆ During the last year, employers in Oklahoma City have eliminated roughly 11,100 positions, a 1.9 percent reduction. The pace of losses accelerated recently, as approximately 9,000 jobs have been cut in the past six months.
- ◆ Head counts in the professional and business services sector have been thinned by 11.5 percent over the last year with the loss of 8,600 spots. Leisure and hospitality employers, on the other hand, have added 1,400 workers in that time, expanding payrolls by 2.5 percent.
- ◆ According to early estimates, the metro unemployment rate increased 210 basis points year over year to 6.1 percent in the third quarter.
- ◆ **Outlook:** Oklahoma City was one of the few metros in the nation to add jobs in 2008, increasing head counts by 3,700 spots. Recessionary pressures are weighing on employment this year, however; roughly 13,500 jobs are expected to be cut from local payrolls in 2009, a 2.3 percent decline.

HOUSING AND DEMOGRAPHICS



- ◆ Long-term construction activity will be limited. Single-family builders pulled permits for 2,700 units in the 12-month period ending in the third quarter, a drop of 35 percent from the same period one year earlier, while just 180 multi-family units were issued, down 70 percent year over year.
- ◆ The weakening employment base and lingering effects of the economic downturn have slowed household formation in the metro. In the past year, the pace of household creation in Oklahoma City has eased to 0.7 percent, roughly half of the rate recorded in the previous 12 months.
- ◆ The median home price has dipped 4 percent over the past year to \$125,400, and the median household income slipped 2.8 percent year over year to \$51,800 per year in the third quarter. As such, there is currently an \$18,400 surplus in the income needed to meet the debt obligations on a median-priced home.
- ◆ **Outlook:** With the deceleration of permitting activity, apartment supply and demand may realign relatively quickly, which should produce healthy revenue growth ahead of other area metros.

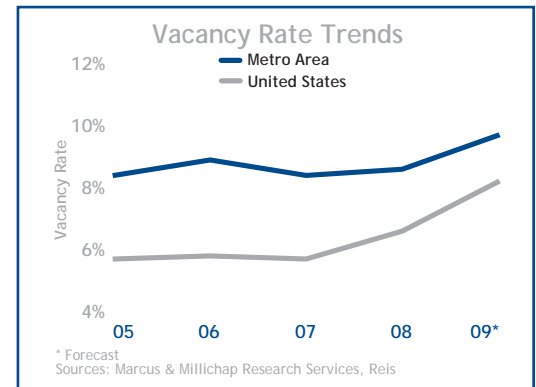
CONSTRUCTION



- ◆ Developers have added 670 units to metro inventory in the last year, a 0.8 percent boost and the largest 12-month expansion in two years.
- ◆ The second and third phases of the Lincoln at Central Park development are the only projects under way. The development will add 708 units to the East Oklahoma City submarket early next year, making the complex one of the largest in the metro.
- ◆ The planning pipeline consists of nearly 530 units, 46 percent fewer than one year ago.
- ◆ **Outlook:** Approximately 670 units were projected to come online this year, all of which were delivered in the first three quarters. Total completions in 2009 are more than double the five-year annual average.

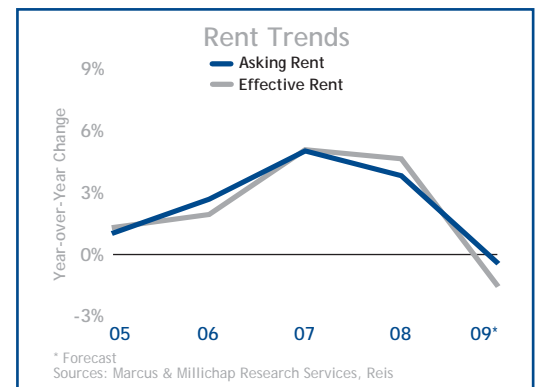
VACANCY

- ◆ Preliminary figures show that metrowide vacancy reached 9.5 percent in the third quarter, 140 basis points higher than one year earlier. The rate is down 10 basis points from the second quarter, as demand for the new projects is relatively healthy; however, this trend is not expected to continue due to mounting job cuts.
- ◆ Growing affordability has lured renters with stable employment into homeownership, shrinking the Class A renter pool. As a result, upper-tier vacancy rose 120 basis points during the last 12 months to 7 percent in the third quarter.
- ◆ Many Class B/C tenants are opting to double up to control costs, driving a year-over-year increase in vacancy of 150 basis points to 10.5 percent.
- ◆ **Outlook:** Vacancy in Oklahoma City is forecast to climb 110 basis points this year to 9.7 percent, the highest rate in seven years, as accelerating job losses are moderating renter demand.



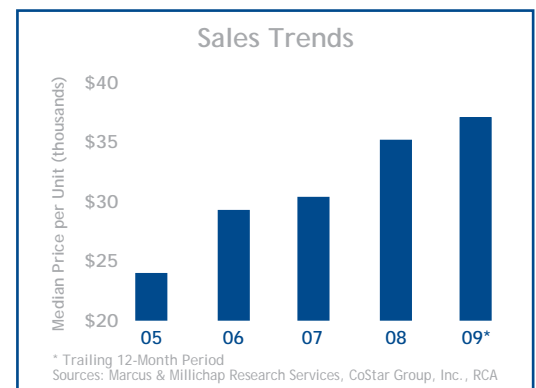
RENTS

- ◆ New-space premiums buoyed marketwide asking rents in the third quarter, according to early estimates, but owners have begun to elevate concessions to counteract waning demand. Asking rents were \$543 per month during the most recent quarter, 0.1 percent higher than one year earlier, while effective rents slipped 0.6 percent year over year to \$514 per month.
- ◆ During the last 12 months, Class A asking rents have increased 0.3 percent to \$679 per month, while Class B/C rents have fallen 0.2 percent to \$488 per month, erasing more than a year of gains.
- ◆ Concessions are currently 5.3 percent of asking rents, as incentives are rising amid weakening demand. As such, owners have recorded a 2.1 percent decline in revenues during the past 12 months, marking the first annual contraction since 2003.
- ◆ **Outlook:** Owners will reduce rents and increase concessions in response to waning demand. Asking and effective rents are projected to end the year at \$541 per month and \$511 per month, drops of 0.4 percent and 1.5 percent, respectively, from 2008.



SALES TRENDS**

- ◆ Persistent credit market issues have kept many smaller, local investors on the sidelines recently. As a result, transaction velocity slowed by 28 percent during the most recent 12-month period.
- ◆ With out-of-state buyers targeting stabilized assets in strong locations, the median sales price has risen 22 percent in the last year to \$37,000 per unit.
- ◆ The average cap rate for an operationally strong property is in the low-8 percent range, while initial yields for mid-tier assets are in the high-8 percent range.
- ◆ **Outlook:** Buyers seeking relatively safe properties may find opportunities in Class B/C buildings near colleges and universities. Complexes in Norman, Edmond and on the west side, near Oklahoma State University-Oklahoma City, will benefit from expanding student demand, as enrollment figures at all of the metro's universities are expanding.



** 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 150 basis points to 175 basis points lower. The government recently assumed full control of Fannie Mae and Freddie Mac, which may boost confidence in the GSEs, putting downward pressure on rates, but it also creates several near-term uncertainties.
- ◆ 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 OVERVIEW

- ◆ In the East Central Oklahoma City submarket, a proposed streetcar line that would run along Sheridan Avenue from Bricktown to the CBD is gaining traction among local officials. If completed, the project could spur transit-oriented development and increase renter demand over the long term.
- ◆ Owners in the Midwest/Del City submarket have posted a revenue improvement of 0.8 percent during the past year. Renters are attracted to one of the lowest rental rates in Oklahoma City, which has contributed to a modest 10 basis point annual uptick in vacancy.
- ◆ South Oklahoma City is the only submarket where Class B/C vacancy levels have improved over the last year; area owners have reported an 80 basis point drop in vacancy during that time to a metro-low 5.7 percent. Recent weakening in Class A conditions has driven up the average vacancy rate for all properties in the submarket 20 basis points year over year.

SUBMARKET VACANCY RANKING

| Rank | Submarket | Vacancy Rate | Y-O-Y Basis Point Change | Effective Rents | Y-O-Y % Change |
|------|----------------------------|--------------|--------------------------|-----------------|----------------|
| 1 | South Oklahoma City | 5.3% | 20 | \$494 | -2.0% |
| 2 | Edmond | 5.6% | 0 | \$599 | 0.6% |
| 3 | East Central Oklahoma City | 6.8% | 100 | \$582 | 1.9% |
| 4 | Norman | 7.7% | 110 | \$511 | -0.4% |
| 5 | Northeast Oklahoma City | 9.1% | 270 | \$537 | -1.5% |
| 6 | Midwest/Del City | 9.6% | 10 | \$460 | 0.9% |
| 7 | Northwest Oklahoma City | 12.3% | 110 | \$548 | -0.9% |
| 8 | West Central Oklahoma City | 17.7% | 410 | \$447 | 0.1% |