

Detroit, Michigan



Multifamily Housing Update

August 2010

EXECUTIVE SUMMARY

Employers in the Motor City continued to shed jobs, albeit at a slower rate in the second quarter. On a year-over-year basis, payroll headcounts declined -40,300 (-2.3%), down from -86,700 (-4.9%) in 1Q10. Moreover, only -19,400 (-1.1%) jobs were shed in the twelve-month period ended in July, the smallest over-the-year decline since January 2006. The improvement was largely attributable to turnarounds in the manufacturing and business service sectors. Combined, the sectors were responsible for -35,300 jobs lost in 1Q10 and only -3,900 lost jobs in 2Q10.

On a seasonally-adjusted basis, payroll headcounts rose 2,300 in the second quarter, following a modest -6,100 job decline in the previous period. Additionally, total employment advanced 48,463 (2.8%) in the first seven months of 2010, resulting in falling unemployment. The seasonally-adjusted unemployment rate fell from 16.0% at YE 2009 to 14.1% in July 2010.

RED CAPITAL Research (RCR) expect employers to continue to shed jobs through 2011. Specifically, our econometric model produces point estimates of -47,100 (-2.6%) jobs lost in 2010 and -10,000 (-0.6%) jobs lost next year. Assuming a return to strong domestic economic growth, we predict that the metro area will add 24,500 (1.4%) positions to payrolls in 2012, representing the metro's first net payroll gain since 2000. By comparison, Economy.com predict that Detroit will add 21,690 jobs in 2011 and 45,310 jobs in 2012.

Housing market conditions remained weak, largely owing to persistent economic turmoil. According to the Case-Shiller home price index, metro home prices decreased -2.5% y-o-y in May. Moreover, the May price level

was -33.1% below the comparable figure of May 2000. Additionally, the Federal Housing Finance Agency's 2Q home price index reveals a -9.8% y-o-y price decrease in the Detroit - Livonia - Dearborn metropolitan division and a -10.9% drop in Warren - Troy - Farmington Hills.

The metro apartment occupancy rate rose 20 basis points from 91.9% in 1Q10 to 92.1% in 2Q10 due to steady tenant demand. Positive net absorption totaled 364 units from April to June, comparing favorably to the 65 units vacated during the comparable period of 2009. On an annual basis, Class-A properties outperformed Class B/C assets. Marcus & Millichap report that Class-A occupancy advanced 40 basis points y-o-y to 92.8%, while Class B/C occupancy fell 60 basis points to 91.5% in the second quarter.

Rent trends also improved in 2Q10. The average effective rent increased 0.8% sequentially, following a -0.1% decline in the previous period, largely because the size of the average concession package fell from 8.5% of asking rent in 1Q10 to 8.0% in 2Q10. Additionally, annual effective rent trends turned positive (+0.1%) for the first time since 3Q08 (+0.7%).

Reis foresee improved market conditions over the five-year forecast period. The service predicts that occupancy will rise to 93.1% by year-end 2014 and also expects effective rent to advance at a 2.1% average annual rate from 2010 to 2014.

Based on an assumed 8.0% cap rate and optimistic revenue projections from Reis, we calculate an 8.6% expected rate of total return, ranking seventh highest among the **RED 50**. Similarly, Detroit registers the 11th highest measure of risk-adjusted return, owing to low levels of historic NOI growth volatility.

SNAP SHOT

	Y-o-y change	Projected YE 2010
Vacancy (7.9% - 2Q10)	↑ 30bps	↔ unchg
Effective Rents (\$757 - 2Q10)	↑ 0.1%	↑ 0.9%
Cap Rate (N/A - 2Q10)	↔ N/A	↑
Employment (1,709.3m - 2Q10)	↓ 40.3m	↓ 47.1m

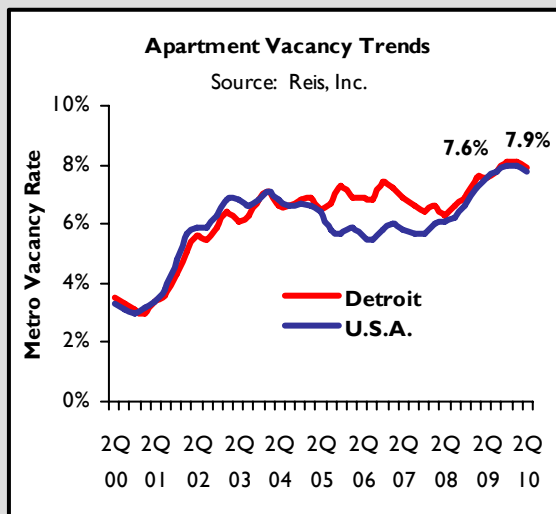
KEY POINTS

- The metro vacancy rate fell 20 basis points sequentially in 2Q10, but rose 30 basis points year-over-year to 7.9%. The annual increase was largely attributable to weak tenant demand. Tenants vacated 337 units and developers delivered only 184 units in the twelve-month period ended in June.
- Effective rent advanced 0.8% sequentially in 2Q10, comparing favorably to the -0.1% drop recorded in the previous period. Consequently, year-on-year effective rent growth accelerated from -1.4% in 1Q10 to 0.1% in 2Q10.
- Class-A rentals reduced asking rent -1.5% year-over-year to \$1,000 in 2Q10. As a result, the vacancy rate among Class-A properties fell from 7.2% in 2Q09 to 6.8% in 2Q10. By comparison, Class B/C properties cut asking rent only -0.3% year-over-year, contributing to a 60 basis point over-the-year increase in vacancy.
- CBRE estimate that cap rates for stabilized Class-A properties ranged from 8.0% to 9.0% in August. Going-yields for stabilized Class-B properties were only slightly higher, ranging from 8.5% to 9.5%.

VACANCY TRENDS

- Positive net absorption totaled 364 units in the second quarter, up from 145 units absorbed in the previous period. As a result, the metro vacancy rate decreased 20 basis points sequentially to 7.9%. On the other hand, vacancy increased 30 basis points year-over-year as tenants vacated 337 units and developers completed 184 units in the twelve-month period ended in June.
- Marcus & Millichap report that the Class-A vacancy rate decreased 40 basis points year-over-year from 7.2% in 2Q09 to 6.8% in 2Q10. By contrast, Class B/C vacancy increased 60 basis points year-over-year to 8.5%.
- Reis believe that vacancy will remain unchanged by year-end, before falling 30 basis points to 7.6% in 2011.

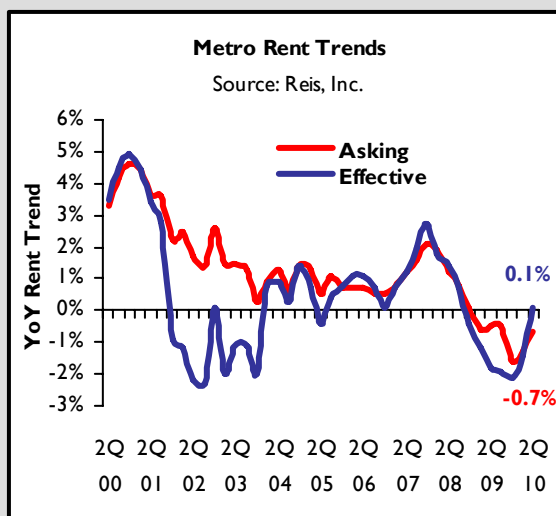
RANK: 30th out of 50



RENT TRENDS

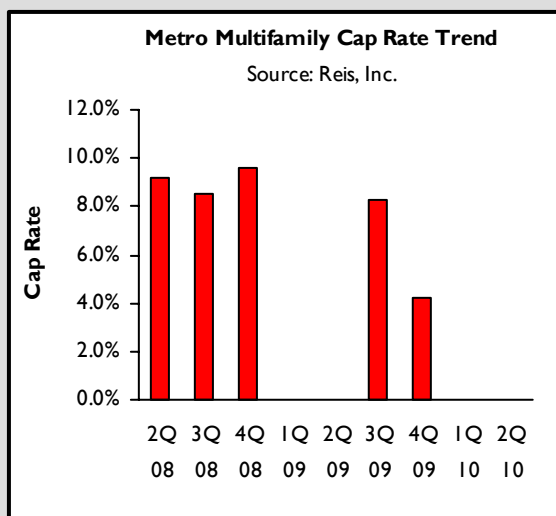
- The average effective rent increased 0.1% year-over-year, owing to a strong 0.8% sequential gain in the second quarter. The pace of over-the-year asking rent growth also rebounded from -1.3% in 1Q10 to -0.7% in 2Q10.
- According to Marcus & Millichap, Class-A asking rent averaged \$1,000 in 2Q10, down -1.5% year-over-year. Class B/C asking rent decreased at a slower -0.3% rate to a \$699 average.
- At 3.0%, the Macomb County submarket posted the fastest rate of effective rent growth among the metro’s 13 submarkets in 2Q10.
- Reis predict that effective rent will advance at 0.9% annual rate in 4Q10.

RANK: 30th out of 50



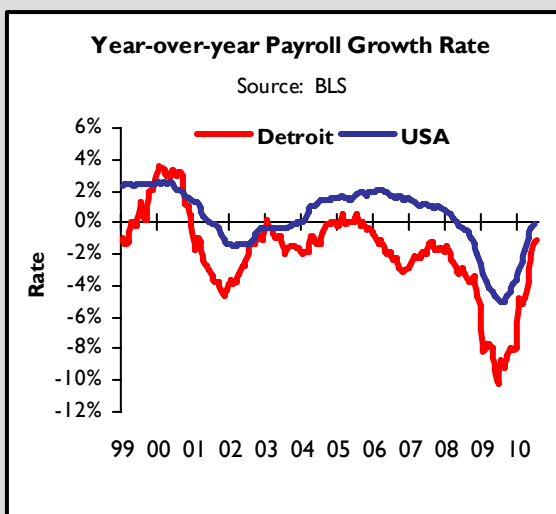
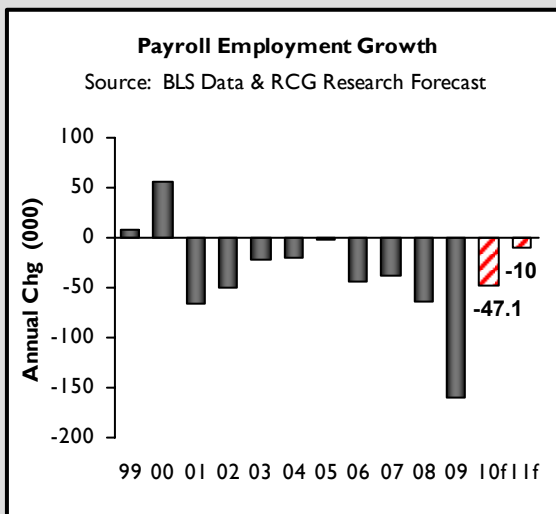
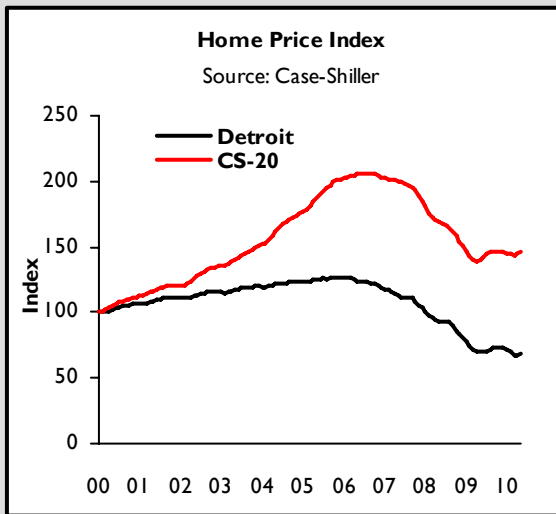
PROPERTY MARKET & CAP RATE TRENDS

- Real Capital Analytics was aware of one apartment that was sold in the first half of 2010. The property sold for \$5 million or \$30,256 per unit. The source reports a 13.4% cap rate for the trade.
- Marcus & Millichap estimate that cap rates were in the 9.75% to 10.25% range in the twelve-month period ended in June. On the other hand, the source notes that suburban properties traded at cap rates around 8.75%.
- According to CB Richard Ellis, cap rates for stabilized Class-A assets ranged from 8.0% to 9.0% in August.
- Based on an assumed 8.0% going-in yield, **RCR** calculate an 8.6% expected rate of total return, comparing favorably to the 7.4% **RED** 50 average.



NOTABLE TRANSACTIONS

Property Name	Property Class	Date of Transaction	Total Price (in millions)	Price per unit	Estimated Cap Rate



DEMOGRAPHICS & HOUSING MARKET

- The population of the Detroit metro area declined -0.5% in 2009, moderately slower than the -0.7% decrease observed in 2008.
- According to the Case-Shiller home price index, housing values in Detroit fell -2.5% year-over-year in May, ranking 18th among the 20 markets tracked by the source.
- Additionally, the Detroit metropolitan division (Wayne County) registered a -9.8% year-over-year decrease in the FHFA home price index in 2Q10. Similarly, the source reports a -10.9% year-over-year drop in the Warren - Troy - Farmington Hills metro division (Lapeer, Livingston, Macomb, Oakland and St. Clair Counties).
- HousingTracker.net calculate a \$104,438 median home and condo asking price in July 2010, down -15.5% year-over-year.

EMPLOYMENT TRENDS

Non-Seasonally Adjusted

- Payroll headcounts decreased -40,300 (-2.3%) year-over-year in the second quarter, following a sharp -86,700 (-4.9%) job decline in the previous period. Furthermore, only -19,400 (-1.1%) jobs were eliminated from payrolls in the twelve-month period ended in July.
- Turnarounds in the manufacturing and business service sectors were largely responsible. The sectors lost a combined -35,300 jobs year-over-year in 1Q10 and only -3,900 year-over-year in 2Q10.
- On the other hand, the pace of year-over-year education and health service job creation slowed from 3,100 in July 2009 to 1,000 in July 2010.

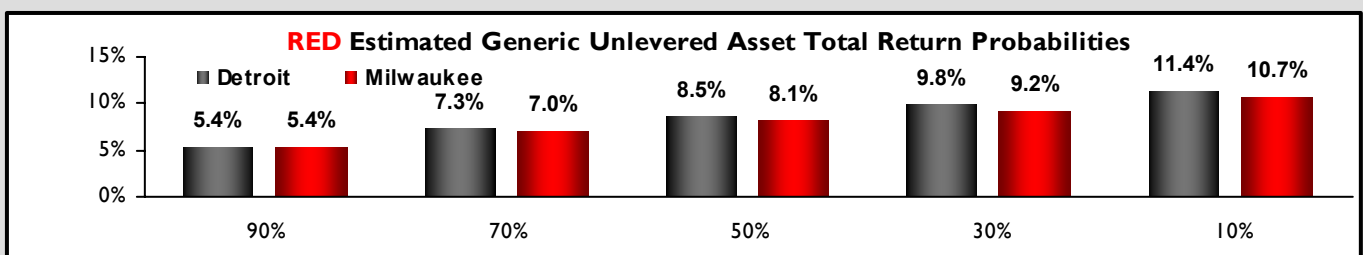
Seasonally-Adjusted

- On a seasonally-adjusted basis, employers created 9,900 jobs in the first seven months of 2010, following attrition of -106,300 jobs in the same period last year.
- By comparison, total employment (from the BLS's household survey) rose 48,463 (2.8%) from December to July. As a result the seasonally-adjusted metro unemployment rate fell from 16.0% in December to 14.1% in July.

Forecast

- RCR believe that job trends will remain negative through next year as -47,100 (-2.6%) jobs are lost this year and another -10,000 (-0.6%) jobs were eliminated in 2011. Based on optimistic domestic economic growth assumption, we predict that employers will create 24,500 jobs in 2012.

RANK: 45th out of 50

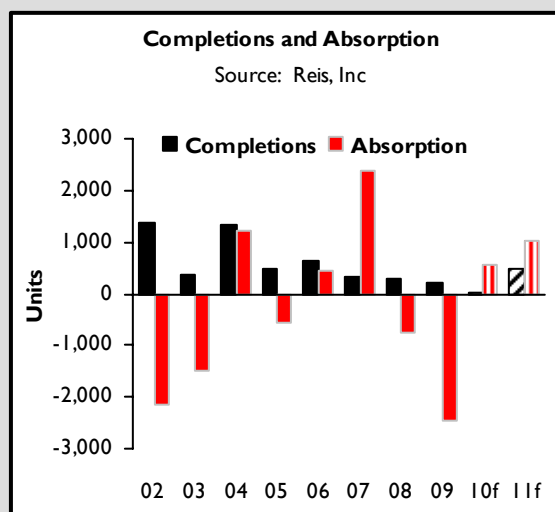


SUBMARKET TRENDS

Submarket	Effective Rent			Physical Vacancy		
	2Q09	2Q10	Change	2Q09	2Q10	Change
Farmington Hills	\$911	\$891	-2.2%	6.4%	6.8%	40 bps
Macomb County	\$672	\$692	3.0%	6.9%	6.9%	unchg
Southfield	\$805	\$814	1.1%	5.7%	8.0%	230 bps
Oak Park / Royal Oak	\$641	\$636	-0.8%	4.3%	5.3%	100 bps
Troy	\$945	\$893	-5.5%	7.1%	8.0%	90 bps
Dearborn / Dearborn Heights	\$719	\$725	0.8%	8.7%	8.7%	unchg
Novi / Livonia	\$789	\$792	0.4%	8.9%	9.8%	90 bps
Downtown	\$859	\$815	-5.2%	9.9%	10.9%	100 bps
Pontiac / Waterford	\$752	\$743	-1.1%	8.9%	8.8%	-10 bps
Westland	\$706	\$708	0.2%	5.8%	5.9%	10 bps
Downriver / South Wayne	\$660	\$668	1.2%	7.0%	7.5%	50 bps
Midtown / West Detroit	\$560	\$549	-2.0%	15.8%	14.6%	-120 bps
Ann Arbor	\$821	\$845	2.9%	7.4%	6.3%	-110 bps
Metro	\$756	\$757	0.1%	7.6%	7.9%	30 bps

SUPPLY TRENDS

- Reis identified one apartment property totaling 28 units that was completed in the first eight months of 2010. The property was delivered to the Midtown / West Detroit submarket in January.
- The source also was aware of one apartment asset containing 156 units that was under construction in August. The property is located in Pittsfield Township, just outside the Ann Arbor submarket boundary.
- The development pipeline, on the other hand was robust. Reis were aware of 2,432 apartment units in the planned / proposed phase. By comparison, only 1,924 units were completed from 2005 to 2009.
- Six condo properties also were under construction in May, totaling 716 units. The largest development (264 units) is located in the Dearborn / Dearborn Heights submarket.



Daniel J. Hogan
Director of Research
djhogan@redcapitalgroup.com
614-857-1416

William T. Hinga
Business Development
wthinga@redcapitalgroup.com
614-857-1499

RED CAPITAL GROUP
Two Miranova Place
Columbus, OH 43215
www.redcapitalgroup.com
800.837.5100



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