

Chicago, Illinois

Multifamily Housing Update

February 2011

EXECUTIVE SUMMARY

The Chicagoland area economy improved in recent months. Indeed, the January purchasing managers survey revealed that business activity, production, new orders and employment were up in January. Specifically, the employment and new orders indices rose to the highest levels since 1984 and 1983, respectively.

Data from the BLS's household survey also suggested that labor market conditions improved. The metro's unemployment rate fell to 8.7% in December 2010, down from 10.6% in the same month of the previous year, owing to a robust 139,684 (3.3%) job increase in total employment.

On the other hand, the BLS's payroll survey suggests that employers continued to shed jobs at a -40,500 (-1.0%) job annual rate in December, in stark contrast to both the household and purchasing managers surveys. But **RED CAPITAL Research (RCR)** believe that the 2010 payroll estimates are likely to be revised upward next month. The source's Quarterly Census of Employment and Wage series suggest that the payroll survey significantly overestimated employment declines.

Based on current payroll estimates our econometric model predicts modest job growth over the next two year. Our model produces estimates of 27,800 (0.8%) net new jobs in 2011 and 61,200 (1.7%) net new jobs in 2012. Similarly, Economy.com predict gains of 32,450 (0.9%) and 87,160 (2.4%) jobs in 2011 and 2012, respectively.

Home prices declined over the past year. The National Association of Realtors report that the median price of a single-family MSA home decreased -4.2% y-o-y to \$183,400 in 4Q10. Additionally, Chicago registered a -7.6% decrease in the Case-

Shiller home price index in the year-ended in November, the second worst performance among the 20 markets tracked by the source.

The improving local economy contributed strong apartment demand in the fourth quarter. Property managers net leased 1,475 units and no units were completed during the four quarter. As a result, occupancy rose from 94.1% in 3Q10 to 94.4% in 4Q10. On an annual basis, occupancy improved 110 basis points as tenant demand (7,251 units) outpaced supply (2,505 units).

Higher occupancy fueled falling concessions and strong rent growth in the fourth quarter. The size of the average concession package fell from 7.6% of asking rent in 4Q09 to 6.9% in 4Q10. As a result, the average effective rent advanced at a 2.4% y-o-y rate, the fastest increase since 3Q08 (+2.5%).

Reis are optimistic about near-term rent and occupancy improvement. The service predicts occupancy to rise to 94.9% by year-end, the highest rate since 1Q08. Furthermore, the average effective rent is forecast to advance at a 4.8% annual rate this year, on par with growth observed in 2007.

Apartment sales activity accelerated in 2010. Real Capital Analytics were aware of 30 investor-grade transactions totaling \$871.4 million in sales proceeds. By comparison, volume totaled only \$408 million in 2009. Average prices also soared, rising 126.7% y-o-y to \$150,717.

Based on an assumed 5.0% going-in yield, **RCR** calculate a 9.7% expected rate of total return, above the 9.0% **RED** 50 average. Additionally, subdued historic rent trend volatility gives rise to the 17th highest measure of risk-adjusted return in the peer group.

SNAP SHOT

	Y-o-y change	Projected 2011
Vacancy (5.6% - 4Q10)	↓ 110bps	↓ 50bps
Effective Rents (\$994 - 4Q10)	↑ 2.4%	↑ 4.8%
Cap Rate (5.0% - 4Q10)	↓ 130bps	↑
Employment (4,213.6m - 4Q10)	↓ 50.5m	↑ 27.8m

KEY POINTS

- The metro vacancy rate decreased 30 basis points sequentially and 110 basis points year-over-year to 5.6% in 4Q10. Robust apartment demand contributed to the improvement. Positive net absorption totaled 1,475 units during the quarter and 7,251 units in the twelve-month period ended in December.
- The size of the average concession package fell from 7.6% of asking rent in 4Q09 to 6.9% in 4Q10. As a result, the pace of year-over-year effective rent growth accelerated to 2.4%.
- Reis are optimistic about near-term rent growth. The service forecasts a 4.8% increase this year, followed by a moderately slower 3.8% advance in 2012.
- Home prices trended lower in recent months. The Case-Shiller home price index showed that values plunged -7.6% year-over-year in November, worse than the -1.6% drop in the 20-market composite index.
- Real Capital Analytics were aware of 30 investor-grade transactions totaling \$871.4 million in sales proceeds in 2010. The average price per unit was \$150,717.



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