

### EXECUTIVE SUMMARY

#### *National Economic Trends*

- Condition in the US economy continued to deteriorate in 3Q08. The -0.5% preliminary estimate of third quarter GDP growth represented the second quarterly contraction in the last four quarters. The decline was largely attributable to a reduction in personal consumption expenditures. PCE advanced 1.2% in 2Q08 but declined -3.7% in 3Q08.
- Payroll employment trends took a dramatic turn for the worse in September. In the first eight months of 2008, a net of 655,000 jobs were trimmed from payrolls. A monthly average of 418,600 positions were cut in September, October, and November. Weak retail sales figures do not bode well for seasonal hiring, indicating that significant job losses will persist through year-end.
- In his latest forecast, National City Bank economist Richard DeKaser predicts that GDP will continue to contract through 1Q09. Mr. DeKaser projects a -3.4% decline in 4Q08 and a -0.6% drop in 1Q09. Consistent with reduced output, establishments are forecast to shed about 1.5 million payroll employees (-1.0%) next year, giving rise to a 7.4% unemployment rate.

#### *Midwest Region Economic and Housing Trends*

- Employers in the Midwest continued to experience falling payrolls. Headcounts fell -69,900 (-0.4%) year-over-year in 3Q08, down from the -44,900 (-0.3%) reduction in the previous period. Construction and manufacturing businesses lost jobs at a rapid pace as attrition in the foregoing sectors totaled -31,000 (-4.1%) and -39,600 (-2.0%), respectively. Conversely, education and health service firms continued to create job opportunities. Combined, the sectors added 28,100 (1.3%) positions to payrolls year-over-year in 3Q08.
- Home sales activity fell at a modest -1.5% sequential rate in 3Q08 as a seasonally-adjusted annual total of 534,000 homes were sold. Relatively stable transaction velocity was partially due to an increase in foreclosures and corresponding drop in home prices. Annual appreciation was negative in four (Minnesota, Illinois, Wisconsin, Missouri) of the five states in the Midwest Region.

#### *Total Return Analysis*

- Four of the five metro markets in the Midwest (Kansas City, 6.5%; Milwaukee, 6.4%; Minneapolis, 6.0%; and Chicago, 6.0%) enjoy expected total returns that exceed the **RED** 50 average (5.8%). At 5.6%, base-case returns in Saint Louis are short of the threshold, but relatively stable historic revenue growth produces an above average level of risk-adjusted return.

#### *Investment Rankings*

- **RED CAPITAL Research (RCR)** believe that Midwest apartment markets produce healthy risk-adjusted returns for investors, owing to above average going-in yields and relatively stable historic rent and occupancy trends. Heightened economic risks are the most significant investment risk factor.
- Indeed, we assign cautious "*Accumulate*" rankings to Kansas City, Milwaukee and Chicago assets. Each of the markets exhibits an above average measure of expected and risk-adjusted return. Conversely, Minneapolis returns are not rich enough to compensate investors for above average revenue growth volatility. Therefore, we recommend that buyers purchase Twin City assets at "*opportunistic*" going-in yields. Forecasted rent and occupancy trends in Saint Louis are a concern. Reis expect rent growth to average 2.2% annually through 2012, coinciding with a 150 basis point drop in occupancy. As a result, investors should seek discounted up-front yields; purchase assets *opportunistically*.