

### EXECUTIVE SUMMARY

#### *National Economic Trends*

- The pace of economic expansion was considerably weaker in the fourth quarter 2007. Real gross domestic product advanced at a 0.6% seasonally-adjusted annual rate, significantly below trend and comprehensively slower than the 4.9% surge recorded in the third quarter. The housing downturn was largely to blame: residential fixed investment fell 25.2%, as developers cut production in order to stem a sharp rise in unsold home inventories. Personal consumption advanced at a 1.9% rate, down from 2.8% in 3Q07, and import levels fell 1.9% on sluggish domestic demand. The decline in spending was felt most acutely at retailers exposed to the housing industry, especially building supply, home furnishings and department stores, which registered declining sales year-over-year. Even export growth, which ignited the economy in the third quarter, decelerated significantly, dropping from a 19.1% burst in 3Q07 to a more modest 4.8% advance.
- January and February payroll data suggest that the economy continued to decelerate in 2008 and raised the prospect that GDP growth will be negative in the first quarter. Establishments trimmed 22,000 and 63,000 jobs, respectively, in January and February, the first seasonally adjusted losses recorded since August 2003. On a year-over-year basis, payroll employment rose 0.6% in February, the slowest annual comparison observed in 48 months. New orders for manufactured goods fell 2.5% in January, following a 2.0% increase in December. This decline was primarily attributable to reduced demand for cars, trucks and other transportation equipment, which fell 13.0% following a 10.1% gain posted in December.
- National City Bank economist Dr. Richard DeKaser forecasts GDP growth to decelerate to 1.9% in 2008 but rebound to 2.5% in 2009. Similarly, the rate of payroll growth is expected to fall to 0.6% this year, and accelerate to 1.1% in 2009.

#### *Southeast Economic Trends*

- Economies in the Southeast Region were less dynamic in 2007 as well. Payroll job creation declined from 326,800 (2.0%) in 2006 to 253,000 (1.5%) last year. The housing downturn played a significant role in the process, leading construction firms to reduce net hiring from 41,200 (4.7%) and 45,700 (5.0%) workers in 2005 and 2006, respectively, to 25,800 (2.7%) in 2007. In addition, lower mortgage origination volume contributed to less aggressive expansion by financial institutions, which hired a net of 15,200 (1.7%) employees last year after adding 22,200 (2.6%) in 2006. Manufacturing was not unscathed, primarily due to -10,400 (-4.8%) job losses in the transportation equipment sector, due in part to weak domestic auto sales.
- Regional home price trends were comparatively healthy in 4Q07. Four of the five Southeast Region states posted year-over-year price gains that surpassed the national average, according to OFHEO. According to the National Association of Realtors, metro specific home price trends outpaced the national average.
- **RED** are relatively optimistic with regard to regional payroll growth in 2008 and 2009. Our econometric model generates a point estimate of 199,000 (1.2%) new jobs for 2008 and 248,000 (1.5%) for 2009. We are biased toward the lower end of our forecast range, however, given the uncertainty surrounding national economic and credit conditions. The forecast confidence intervals range from 165,000 (1.0%) to 233,000 (1.4%) for 2008 and 207,000 (1.2%) to 290,000 (1.7%) for 2009.

#### *Total Return Analysis*

- Generic multifamily asset five-year holding period total returns in the region are generally below average, stymied by high asset prices and a negative occupancy trend outlook. Of the five markets in the Southeast (Atlanta, Charlotte, Nashville, Norfolk and Raleigh-Durham) only Charlotte assets provide an above average rate of expected return (6.8%). The region is also characterized by above average rent trend and occupancy volatility, with the exception of the stable Norfolk market, depressing risk-adjusted returns.

#### *Investment Rankings*

- The historic stability of rent and occupancy trends observed in **Norfolk**, coupled with optimistic rent expectations earn the market an *Accumulate* ranking. **Charlotte**'s strong economy makes it an interesting alternative, but the market remains too volatile to warrant an active buying program, relegating it to the *Opportunistic* ranks. Our analysis of **Nashville** and **Raleigh-Durham** investments follows a similar line, placing them in the same category. On the other hand, market fundamentals do not support asset prices in **Atlanta**, by our way of thinking, leading us to assign a *Hold* rating.