RED CAPITAL GROUP®

Market Overview

Dallas, Texas

Multifamily Housing Update | **February 2011**

EXECUTIVE SUMMARY

The Dallas economic recovery proceeded at a measured pace in late 2010, producing moderate payroll job gains and slow and steady business activity expansion. Metro establishments added workers to payrolls at a 29,500-job year-on-year pace in 4Q10, a 1.5% advance, up from a 22,600-job, 1.1% gain recorded in the prior quarter.

Although the 4Q10 results were the strongest recorded in nearly two years, the data contained a few sour notes. First, the y-o-y payroll comparison in December fell sequentially from 32,000 jobs in the 12 months ended in November to 28,400, a sharp contrast from the solid positive momentum observed nationally. Moreover, payroll job creation expressed on a seasonally-adjusted basis disappeared after mid-year, as Dallas payrolls actually declined 1,500 positions from June to December after adding 29,300 during the year's first half.

The Dallas Fed's Business Cycle Index mirrored the foregoing trends. The index improved steadily in the first half of 2010, rising 1% from December 2009 to June, but declined moderately during the summer and advanced without conviction in 4Q. Likewise, the 11th District Fed's January Beige Book comments were cautious, reporting firmer manufacturing and retail conditions but largely stagnant labor markets and persistent weakness in home sales, prices and construction in the district.

RED Research's econometric payroll model projects modest acceleration this year but stronger conditions developing in 2012. By the numbers, the model yields a forecast of 38,900 (1.9%) net jobs in 2011, followed by robust 60,000 and 69,000 job adds during the following two years.

Although home sales velocity was sluggish, demand for rental housing remained exceptionally strong. Reis report that tenants net leased 4,035 units during the seasonally-weak fourth quarter, representing the strongest October-to-December demand recorded in five years. By the same token, 4Q10 supply levels slid to a 5-year one-quarter low 227 units, allowing average market occupancy to surge 90 basis points sequentially to 91.9%, a two-year series high.

Demand was concentrated in the northwest Dallas Co. quadrant as the Northwest and North Irving submarkets chalked down 2.1% and 1.7% sequential quarter gains. Interest in urban living didn't wane as Oaklawn properties enjoyed a robust 370 bps quarter-to-quarter advance. Only one of Dallas's 24 Reis-defined submarkets recorded a net occupancy rate decrease (Far NW/Farmers Branch).

Leasing agents took advantage of tighter markets to push rents higher. Average asking rents rose $4 (0.5%) sequentially to $825, up from 3Q's $1 advance and one of the largest fourth quarter moves ever registered in this market. Moreover, concession burn-off continued for the fourth consecutive quarter, allowing average effective rents to rise $5 (0.7%) sequentially and $15 (1.9%) y-o-y to $749.

Rent trends remained weak in some suburban submarkets with older apartment stock: Far Northeast, Far NW and South Irving recorded –1% or larger sequential effective rent setbacks. Conversely, substantial gains were recorded in infill and north suburban submarkets: Central and East Dallas and Oaklawn posted 1%+ hikes and Carrollton, Richardson and Lewisville advanced 90 bps or more.

Investment momentum accelerated. Loopnet report that at least 10 institutional quality trades closed during 4Q, accounting for total proceeds of approximately $320 million.

SNAP SHOT

	Y-o-y change	Projected 2011
Vacancy (8.1% - 4Q10)	↓ 2.6%	↓ 0.5%
Effective Rents ($749 - 4Q10)	↑ 1.9%	↑ 3.9%
Cap Rate (6.0% - 4Q10)	↓ 100bps	↓ 25 bps
Employment (2,045.1m - 4Q10)	↑ 29.5m	↑ 38.9m

KEY POINTS

- Dallas households expressed strong demand for rental housing options during the fourth quarter. Reis report that apartment properties absorbed 4,035 units during the period, raising occupancy 90 bps sequentially to a 91.9% average metropolitan area average.
- Enhanced pricing power developed with tighter markets. Leasing agents improved on 3Q10's modest $1 sequential quarter average effective rent hike with a useful $5 (0.7%) quarter-to-quarter advance during 4Q10.
- Reis expect rents to rise $29 (3.9%) in 2011 and $28 (3.6%) in 2012 and foresees further occupancy improvement, too, but at a much slower pace than 2010's 260 bps surge.
- The Dallas economy made measured gains in the fourth quarter. Establishments added payroll employees at a 29,500-job annual rate, up from 3Q's 22,600-job gain. The unemployment rate remained at an elevated level, however, standing at 8.0% in December, unchanged from 2009.
- Institutional investors exhibited a healthy appetite for Dallas-area trophies. At least 6 projects of 1998 vintage or younger traded during 4Q at cap rates between 5.5%-6.5%.