MHA

Multi Housing Advisors

TRENDS INFLUENCING APARTMENTS IN THE SECOND- AND THIRD-TIER CITIES OF THE SOUTHEAST

Historically, many investors avoided or severely limited their exposure to apartments located in second- and third-tier cities in the Southern US. This reluctance was due to the perception that smaller markets would offer less rent growth. During recent years, however, the market has seen values and operating conditions demonstrate the contrary. ***Investors who chose to purchase or develop properties in these secondary and tertiary markets have been rewarded.***

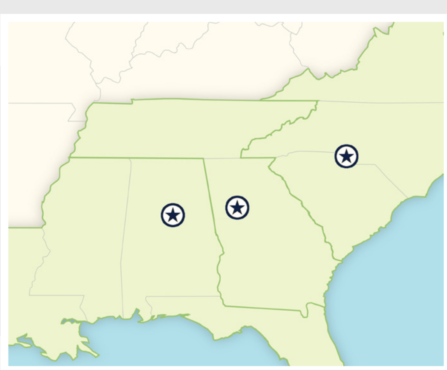
The improvement in underlying operating conditions has resulted in higher values due to a compression in cap rates as ***investors view these smaller markets as "less risky" than in years past***. These rates, created by record low interest rates and increased demand from purchasers, were driven by the lack of alternative investments, a minimum level of new construction and from improvement in the economy after the economic crisis of 2008. Operating conditions generally experienced their worst levels in 2009, but virtually every market has experienced improvement in occupancy and rent levels each year thereafter. ***These improved operating conditions have been nearly universal in the second- and third-tier cities throughout the Southeast.***

"With improved operating conditions, an expanded willingness by lenders to provide funds, and less overall risk, second- and third-tier cities are demanding more attention in today's investment landscape."

With respect to new construction in the secondary and tertiary markets, lenders are still reluctant to provide funds compared to the terms being offered in Tier 1 markets. However, the communities that are built in these markets often experience rent and absorption levels that far exceed the developer's pro forma. Some properties are seeing a return on cost far above what would be considered normal in larger cities, such as Atlanta, Nashville, Charlotte, etc. ***Actual return on cost figures in the mid-to-high 8% range are increasing lenders' willingness to make loans in the smaller cities.*** In addition to these improved operating conditions, lenders are looking for ways to circumvent the heightened competition in the larger MSAs, which will drive additional capital to these second and third tier markets.

Traditionally, investors looking at smaller markets often felt the need to "get their yield day one". Lenders are now offering 10-year mortgages at approximately 3.75% (frequently with a few years of interest only), resulting in attractive returns on a leveraged basis. ***Buyers are also beginning to recognize that smaller markets do not have the risk to justify the higher spreads seen in the past, as compared to the larger markets.*** Cap rates for class A product in these markets (generally defined as properties constructed during the last 10 years) range from 5.75% to 6.25%, while class B properties (in good condition) range from 6.0% to 6.75%. A few of the recently constructed apartments have dipped below the indicated range for the class A properties, but there have been relatively few sales due to the lack of new product.

With improved operating conditions, an expanded willingness by lenders to provide funds, and less overall risk, second- and third-tier cities are demanding more attention in today's investment landscape.



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Greenville, SC Apartment Market

Overall Market	YE 2009	% Change	YE 2010	% Change	YE 2011	% Change	YE 2012	% Change	YE 2013	% Change	3rd Qtr. 2014
Asking Rent (per Unit)	$622	3.7%	$645	2.2%	$659	2.9%	$678	3.7%	$703	2.0%	$717
Effective Rent (per Unit)	$570	4.7%	$597	2.5%	$612	3.6%	$634	3.9%	$659	2.3%	$674
Reported Occupancy	88.5%	4.3%	92.3%	0.8%	93.0%	2.3%	95.1%	-0.4%	94.7%	0.5%	95.2%

Birmingham, AL Apartment Market

Overall Market	YE 2009	% Change	YE 2010	% Change	YE 2011	% Change	YE 2012	% Change	YE 2013	% Change	3rd Qtr. 2014
Asking Rent (per Unit)	$705	0.4%	$708	2.8%	$728	3.2%	$751	3.1%	$774	1.0%	$782
Effective Rent (per Unit)	$656	1.5%	$666	3.2%	$687	3.6%	$712	3.4%	$736	1.0%	$743
Reported Occupancy	90.0%	2.1%	91.9%	1.6%	93.4%	0.6%	94.0%	0.4%	94.4%	-0.1%	94.3%

Greensboro/Winston-Salem, NC Apartment Market

Overall Market	YE 2009	% Change	YE 2010	% Change	YE 2011	% Change	YE 2012	% Change	YE 2013	% Change	3rd Qtr. 2014
Asking Rent (per Unit)	$665	-0.6%	$661	2.0%	$674	1.8%	$686	1.9%	$699	1.3%	$708
Effective Rent (per Unit)	$608	1.3%	$616	2.4%	$631	2.2%	$645	2.2%	$659	1.5%	$669
Reported Occupancy	87.2%	3.0%	89.8%	3.0%	92.5%	0.5%	93.0%	1.0%	93.9%	0.9%	94.7%

Knoxville, TN Apartment Market

Overall Market	YE 2009	% Change	YE 2010	% Change	YE 2011	% Change	YE 2012	% Change	YE 2013	% Change	3rd Qtr. 2014
Asking Rent (per Unit)	$587	1.4%	$595	1.5%	$604	2.6%	$620	1.6%	$630	2.5%	$646
Effective Rent (per Unit)	$560	2.5%	$574	2.3%	$587	2.7%	$603	1.8%	$614	2.4%	$629
Reported Occupancy	92.2%	2.0%	94.0%	0.1%	94.1%	0.0%	94.1%	1.4%	95.4%	0.4%	95.8%

Columbia, SC Apartment Market

Overall Market	YE 2009	% Change	YE 2010	% Change	YE 2011	% Change	YE 2012	% Change	YE 2013	% Change	3rd Qtr. 2014
Asking Rent (per Unit)	$704	2.0%	$718	0.7%	$723	2.6%	$742	2.3%	$759	1.4%	$770
Effective Rent (per Unit)	$667	2.8%	$686	0.9%	$692	3.3%	$715	2.5%	$733	1.6%	$745
Reported Occupancy	87.5%	3.8%	90.8%	1.0%	91.7%	0.9%	92.5%	0.6%	93.1%	0.5%	93.6%

Savannah, GA Apartment Market

Overall Market	YE 2009	% Change	YE 2010	% Change	YE 2011	% Change	YE 2012	% Change	YE 2013	% Change	3rd Qtr. 2014
Asking Rent (per Unit)	$711	1.5%	$722	2.8%	$742	1.1%	$750	2.1%	$766	2.7%	$787
Reported Occupancy	88.9%	3.1%	91.7%	0.5%	92.2%	1.7%	93.8%	0.0%	93.8%	0.3%	94.1%

Macon, GA Apartment Market

Overall Market	YE 2009	% Change	YE 2010	% Change	YE 2011	% Change	YE 2012	% Change	YE 2013	% Change	3rd Qtr. 2014
Asking Rent (per Unit)	$631	1.6%	$641	1.6%	$651	0.0%	$651	1.5%	$661	-0.2%	$660
Reported Occupancy	90.0%	-0.1%	89.9%	1.9%	91.6%	0.3%	91.9%	1.1%	92.9%	0.6%	93.5%

Source: Reis