

The Future Of Apartment Living

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CEL & Associates, Inc.

Real Estate Strategies, Benchmarking & Performance Solutions

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The Future Of Apartment Living

During the next 20+ years, several transforming demographic, economic and market trends are likely to reshape the future of apartment living in the U.S. A combination of shifting demographics, a protracted job and economic recovery period, new and more stringent single-family/condominium loan underwriting practices, a downsizing of the single-family home building industry, changing government priorities and tax policy, future generation obligations to reduce/service burgeoning federal deficits and borrowing, and a consumer shift to more sustainable lifestyles will result in a dramatic rise in apartment renters. A change in housing preferences and options for a generation-transitioning population will arise from: shifting consumer preferences to a more urban/mixed-use environment; growing immigrant, 18–44-year-old and aging populations; increasing cost and time for work commutes; federal, state and local housing policy shifts to incentivize more affordable/workforce urban housing options; and the lasting financial impact of the 2008/2009 recession on consumer behavior. These factors probably will reduce economic growth for a decade or more. Once the current economic malaise, capital and credit market crisis, and general financial instability are brought under control and stabilized, the outlook for apartments and apartment living over the next two decades is very robust. Based on conservative analytics, CEL & Associates, Inc. estimates that during 2008 – 2030, approximately \$1.1 trillion in new apartments will be needed to meet future demand.

The Genesis Of Apartment Living In America

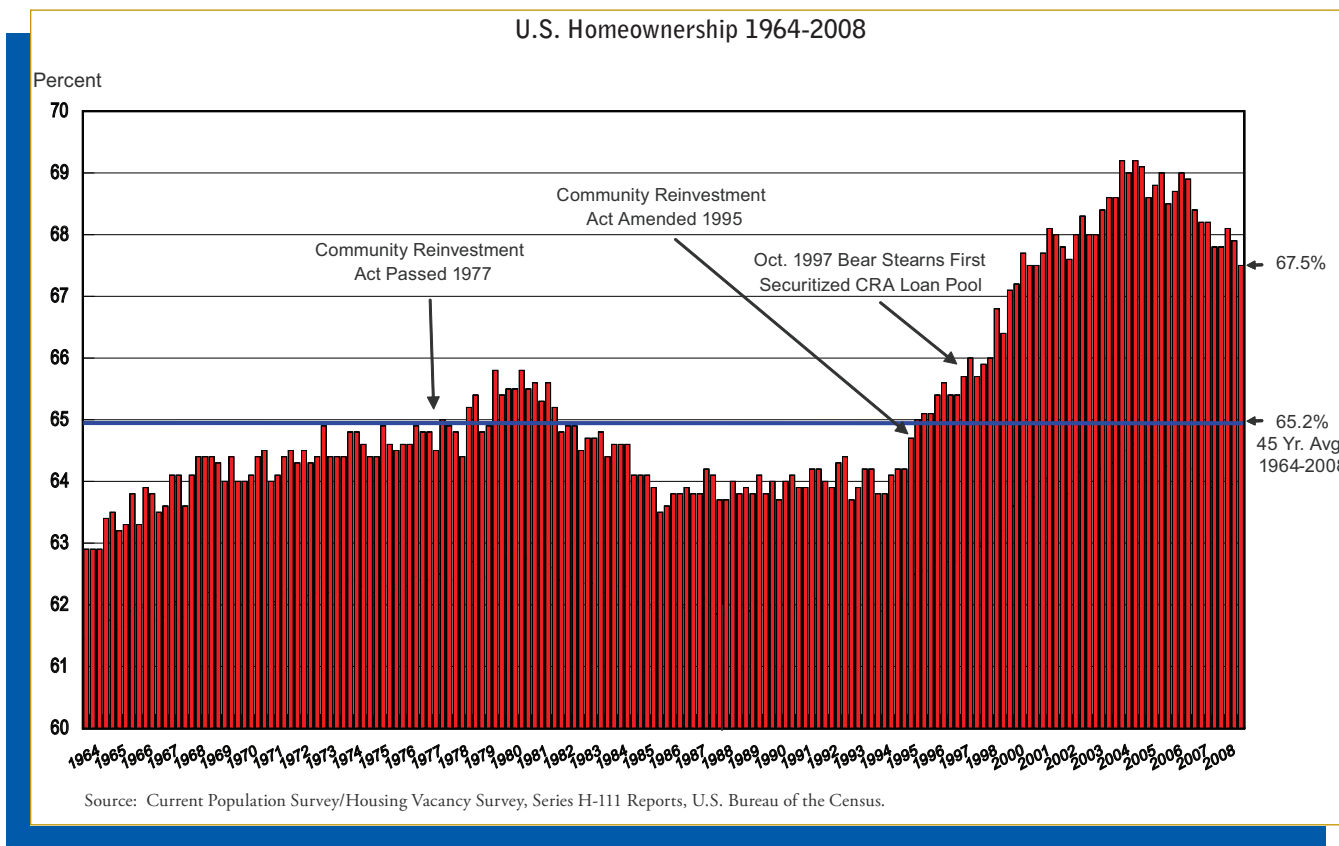
Apartment living began in ancient Rome when entrepreneurial Romans began building six- to seven-story mixed-use buildings with shops on the ground level and living quarters for rent on the upper floors. Often these “rental units” were leased by the shopkeepers below. Later, as Rome and other cities in the Roman Empire declined, the rapid emergence of the European continent, shift from rural to urban society and accelerated expansion of world commerce and banking created a workforce of life-long renters. By the 1800s, urbanization of already-crowded cities and growth of privately-held real estate resulted in a continent of entrepreneurial landlords renting to the “working class.” While it is unclear who developed the first apartment buildings in the U.S. and their location, historians believe they began appearing in the 1850s. Initially called “French flats” to attract renters and acknowledge their origin, the early apartment buildings were designed and developed for the more affluent. In 1869 the Stuyvesant Flats (a full-service building) opened in New York City on the Upper West Side, followed in 1884 by The Dakota luxury apartment building; these were among the first “for rent” properties in America. As a flood of immigrants arrived in America, many owners of single-family homes in the urban core of America’s employment centers subdivided their properties into “tenant houses” for rent. By 1890, more than 32,000 tenement houses in New York contained nearly 1.25 million residents. The increasing wave of immigrants saw the emergence of row houses, duplexes and quads for renters. By the 1900s, rental housing and apartment living in the U.S. was off and running as American cities grew taller, with far greater density. More than 100 years later, there are now more than 266,000 apartment communities housing nearly 33 million residents. Renting has become a housing option for many Americans.

The Current Situation

Demand for apartments generally is driven by several factors, including a function of job growth, the relationship of cost-to-own versus cost-to-rent, age demographics, household formation, household income, overall economic well-being, consumer confidence expectations and governmental policies. It is important to remember that homeownership was not always at today’s high. Between 1900 and 1940, homeownership in the U.S. ranged from 46.5% to 43.6%, respectively. In the early 1930s, home mortgage terms typically were only three to five years, and homeowners were required to refinance their homes at the end of each term; when refinancing wasn’t available or credit weakened, many owners lost their homes. From 1940 to 1950, homeownership increased 11.4 percentage points, from 43.6% to 55.0%. This dramatic increase was primarily due to the return of World War II soldiers, who married and started families and, encouraged by the GI Bill, purchased homes in suburban (Levittown-like) developments across the U.S. After the war, it was estimated that up to 5.0 million Americans needed homes, and the makeshift towns built surrounding war-related manufacturing facilities were not adequate. The perceived benefits of mortgage interest deductions (originally a 1913-law intended for businesses), and the fact that the Federal Housing Administration “insured” home mortgages, attracted returning GIs with dreams of “owning their own home.” The Federal National Mortgage Association (“Fannie Mae”) was created in 1938 to create a secondary market for residential loans and fresh capital for additional home mortgages. The

Government National Mortgage Association (“Ginnie Mae”) was created in 1968 to provide assistance to Fannie Mae. As part of President Johnson’s Great Society reform, much of Fannie Mae became a privately owned, government-sponsored enterprise (“GSE”) with authority to issue mortgage-backed securities and ensure that funds were consistently available to institutions lending money to home buyers. In 1970, Congress authorized Fannie Mae to purchase conventional mortgages and created Freddie Mac. From 1950 to 1975, homeownership increased from 55% to 64.5%...a nearly 10 percentage point jump.

In 1977, the Community Reinvestment Act (“CRA”) was signed by President Carter (revised in 1995), and encouraged/required lenders to issue mortgages to less-than-qualified (low-income) borrowers. President G.H.W. Bush signed the Financial Institutions Reform Recovery and Enforcement Act (“FIRREA”) of 1989 that mandated a public release of data regarding banks’ adherence to CRA legislation. From 1975 to 1997 homeownership increased slightly from 64.5% to 65.7%. In 1997, the Clinton Administration pushed for more loans to “benefit lower income families, minorities and those in undersecured areas.” In October 1997, Bear Stearns & Co. launched the first publicly available securitization of CRA loans (guaranteed by Freddie Mac). From 1991 to 1993, the number of single-family home starts jumped 22.6%.



By May 1999, the Los Angeles Times reported that African-American homeownership was increasing at a rate three times higher than whites, while Latino homeowners were growing five times as fast. Spurred on by the availability of subprime mortgages, buyers believed renting an apartment was no longer a desired option, because the cost of owning was less or on par with renting. By March 2007, the value of subprime mortgages was estimated to be \$1.3 trillion. From 2004 – 2006, the share of subprime mortgages relative to originations ranged from 18% – 21%, versus less than 10% between 2001 – 2003.

From 1997 through 2000, homeownership increased 1.8 percentage points from 65.7% to 67.5%. After 9/11, the U.S. Federal Reserve began to cut interest rates dramatically to expand the money supply and encourage borrowing. As lower interest rates worked their way through the market, owning real estate – particularly single-family homes – became attractive as mortgage rates dropped to their lowest level in 40 years. The injection of subprime mortgages (loans often to those with poor credit) into pools of asset-backed public securities and the introduction of teaser rates on adjustable-rate mortgages created a homebuilding and home-buying frenzy. By 2Q 2004, homeownership had peaked at 69.2%.

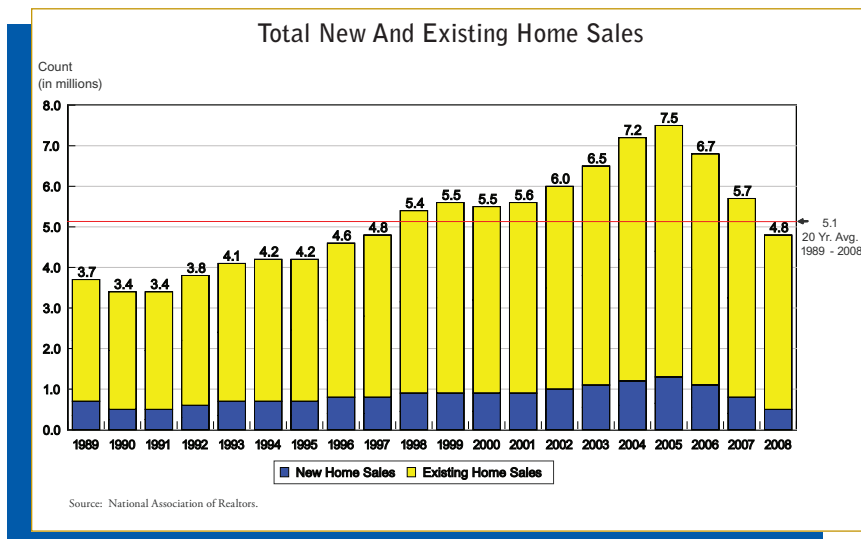
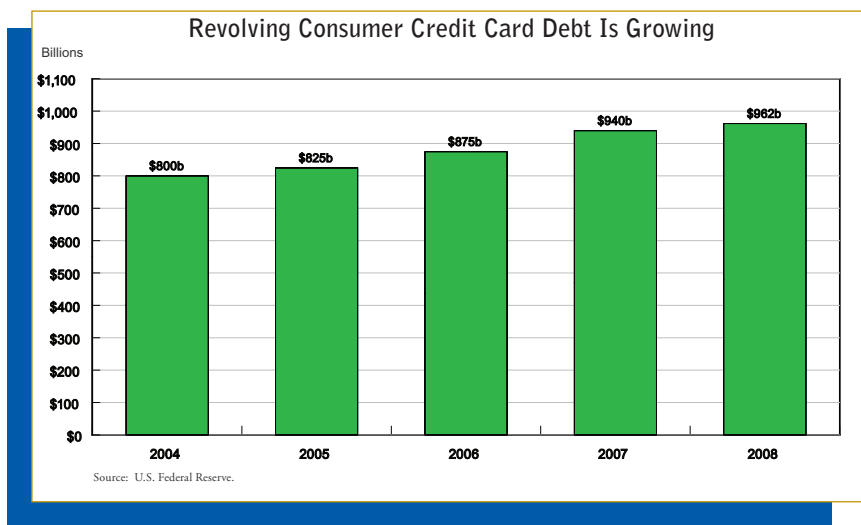
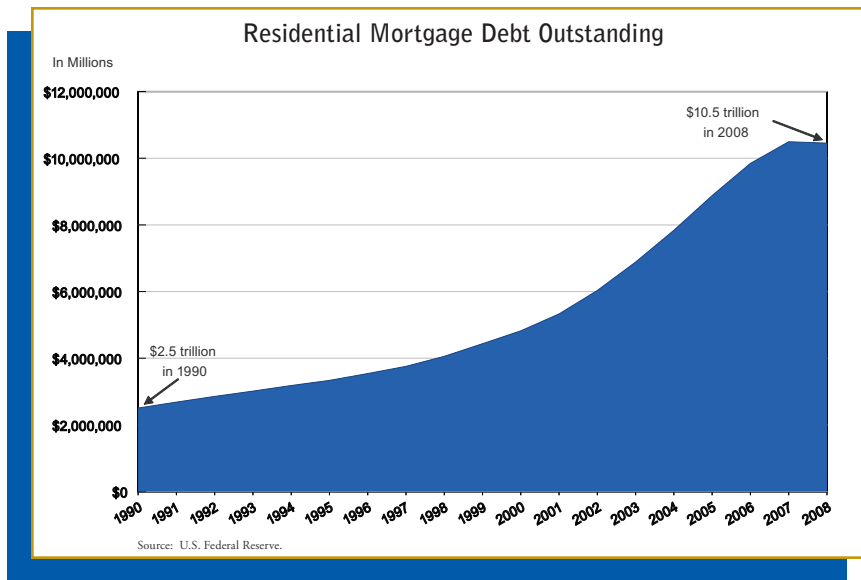
As homeownership increased, the value of the underlying asset did as well. Homeowners began to perceive their homes as not

only a place to live but a source of money for discretionary retail purchases, new cars, trips and other “home upgrades.” Between 1990 and 2008 the amount of mortgage debt outstanding grew over 317% from \$2.5 trillion to \$10.5 trillion

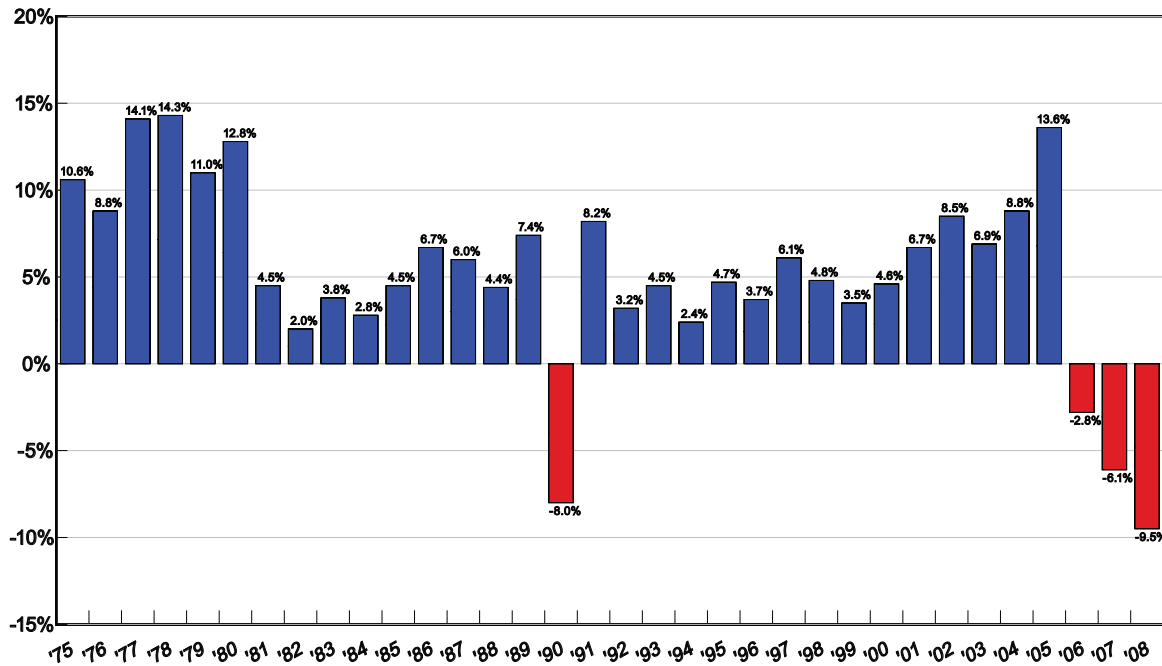
By 2008, overall household debt jumped to \$13.8 trillion as consumers increased their outstanding consumer credit. Consumer credit card debt reached over \$960 billion. The home had become a perceived unlimited ATM machine. As long as values continued to rise so did an ability to borrow and spend more. Subprime loans were nearly 12% of all residential mortgages.

The combined sales of new and existing homes rose from a low of 3.4 million units in 1990 to a peak of 7.5 million units in 2005. The process of buying, selling and “flipping” homes as a source of income and an ability to “move up” rendered living in an apartment a “non-preferred” housing option. Renting an apartment was only a “temporary” situation since the “real money” was in rapidly rising home ownership values. The availability of inexpensive debt, requirements for little or no money deposits and a perception that if one wasn’t “in the game” of owning a home you would be falling behind your peers placed consumer preference on owning vs. renting.

However, the economic glory years of the 1990s and 2000s ended in late 2008 with the global collapse of the financial markets. The events culminating in 4Q 2008 prompted the Federal Reserve and the U.S. government to pump hundreds of billions of dollars into the financial system to prevent wholesale financial panic. Freddie and Fannie, which owned or guaranteed nearly all of the \$10 trillion in U.S. mortgage market, were placed in conservatorship. During 2007, lenders began foreclosure proceedings on 1.3 million properties. This increased to 2.3 million in 2008. When the financial collapse finally is over, it is estimated that investors and financial institutions could face as much as \$2 trillion in losses from bad U.S. loans and bonds. In a January 13, 2009, report, Goldman Sachs estimated that losses from delinquent U.S. residential mortgages could reach \$1.1 trillion. Net household wealth has fallen 20% (approximately \$11.2 trillion) since its peak in 2Q of 2007.



Existing Median Home Price Appreciation, United States



Source: National Association Of Realtors.

By 4Q 2008, the economic, financial and subprime mortgage collapse saw homeownership levels (then 67.5%) begin to decline even further as foreclosures mounted. Approximately 7 million to 10 million homes may now be worth less than their mortgage, and another 1.0 million or more will fall into that category if home values continue to decline. Since the peak in 2006, approximately \$6.1 trillion in single-family home value has been lost. The U.S. government and Federal Reserve have spent, lent or committed \$12.8 trillion, an amount equal to nearly 90% of U.S. GDP to stabilize the crisis.

The Outlook For The Apartment Industry

While the single-family home market has fallen dramatically and may not have reached bottom, the lasting impact of today's recession and a major decline of detached housing could reshape residential patterns in the U.S. for years to come. Depending on which economist or forecaster one reads, the general consensus is that today's recession will be one of the longest in recent memory, recovery will take years and job growth will be very slow, despite a likely surge in the number of "created jobs" expected from government stimulus legislation. Rising unemployment, dramatic losses to household net worth, declining home values, increasing levels of delinquent mortgages and foreclosures as well as lack of credit may have reversed the long-standing homeownership trend to a new era of apartment living. While the current economic crisis is likely to prevail through 2010 or longer, a substantial increase in homeownership rates probably will not occur for at least 10 – 15 years as stringent regulatory oversight regarding lending practices is deployed, household net worth and income increase measurably, and federal stimulus capital is mainly directed to "bailout," "rescue" or "short-term stimulus" plans. Overall homeownership could decline from today's high levels to low 60% levels or less. While this economic transformation will be painful for many Americans, it will be good news for the apartment industry.

CEL & Associates, Inc. has completed an extensive study of the factors likely to shape and reshape residential housing patterns in the U.S. While many forces can and will determine the future housing characteristics in the U.S. – economic, demographic, political, geographic and financial – 10 major trends highlight the likely incredible opportunities ahead for rental housing. However, one fact is clear...demand for apartment living during the next two decades should increase dramatically, and the new renter lifestyle soon will be on par with single-family home ownership. The following trends highlight why the outlook for the apartment industry is very bright.

Trend 1 – Population Growth Creates Housing Demand

As the U.S. population increases, the need for housing units increases as well, illustrated in the table at right. Between 1990 and 2008 the number of housing units in the U.S. increased from 102.3 million to 130.4 million...a 27.5% jump. However, the ratio of housing units per person remained fairly constant as the table to the right indicates.

With a consistent number of housing units per person of 0.41 – 0.43, CEL & Associates, Inc. has applied the lower ratio (0.41) to project future housing needs, based on U.S. Census Bureau population projections. The number of growth-related housing units required over the 2008 – 2030 period is highlighted at right. Between 2000 and 2030 the U.S. population is expected to add 72.3 million residents and a demand for approximately 29.6 million additional housing units as indicated in the table to the right.

According to the U.S. Census Bureau's 2007 American Housing Survey for the United States, the percentage of occupied renter housing units to total occupied housing units (non-seasonal) was 28.3%. The percentage of occupied renter housing with 5 – 50 or more units (excluding mobile homes and trailers) to total occupied housing units (non-seasonal) was 12.3%. Based on this assumption, the number of growth-related apartment (5 – 50+) demand is expected to be over 1.2 million apartment units between 2008 and 2030.

It is important to note that this demand for over 1.2 million apartment units assumes a continuation of the current homeownership level of around 68%...a percentage very likely to decline over the next decade. However, each single percentage of decline in homeownership in a stable market creates potential demand for approximately 1.0 million rental housing units. Thus, if homeownership declines, additional growth-related apartment units may be needed, as highlighted at right. Obviously the number of apartments probably will be less due to the available rental single-family homes (approximately 1.3 million units in 3Q 08 or nearly 600,000 units in excess of the normal market vacancy level) for a period of time.

Housing Units Per Person

Year	U.S. Population	Number of Housing Units	Units Per Person
1990	248,623,000	102,264,000	0.41
2000	281,646,000	115,905,000	0.41
2008	304,060,000	130,357,000	0.43

Source: U.S. Census Bureau and the American Housing Survey for the United States 2007. Numbers have been rounded.

Growth-Related Housing Demand (Units)

Period	Population Growth	Units Per Person	# Growth-Related Housing Demand (Units)
2000 – 2010	23,082,000	0.41	9,464,000
2011 – 2020	25,026,000	0.41	10,261,000
2021 – 2030	24,157,000	0.41	9,904,000
2000 – 2030	72,265,000	0.41	29,629,000

Source: U.S. Census Bureau (middle series projections) and the American Housing Survey for the United States 2007. Numbers have been rounded.

Growth-Related Housing Demand (5 – 50+ Units)

Period	# Growth-Related Housing Demand (Units)	% Renter-Occupied Units (5 – 50+)	# Growth-Related Apt. Demand (5 – 50+ Units)
2000 – 2010	9,464,000	12.3%	1,164,000
2011 – 2020	10,261,000	12.3%	1,262,000
2021 – 2030	9,904,000	12.3%	1,218,000
Subtotal 00 – 30	29,629,000	12.3%	3,644,000
Less 00 – 07 Supply Added			-2,399,000
Total 08 – 30			1,245,000

Source: U.S. Census Bureau (middle series projections) and the American Housing Survey for the United States 2007. Numbers have been rounded.

Potential Additional Demand For Apartments

Home Ownership Levels	# Growth-Related Apartment Demand (Units)
68%	
66%	2,000,000
64%	4,000,000
62%	6,000,000

In addition to growth-related housing units needed, the replacement of aging, outdated or apartment housing stock that is no longer habitable must be factored in. The table at right highlights a range of housing replacement percentages based on the life cycle of a housing unit.

Assuming a conservative, 50-year replacement rate ratio of 2.0% per year, the number of rental housing units to be replaced is highlighted at right.

Currently nearly 5.0 million apartment units were built before 1960. Thus, combining growth-related and replacement-related apartment units, the total number units (5 – 50+) needed during the next 20 or so years is highlighted at right.

Based on a conservative cost-to-build value of about \$125,000 per unit, CEL & Associates, Inc. estimates that nearly \$1.1 trillion (8,628,000 x \$125,000) in new apartments (5 – 50+) will be needed between 2008 and 2030. Again, it is important to remember that these totals do not assume any reduction in home ownership, new federal/state housing or affordable housing initiatives, or other significant changes to existing governmental housing policies and lending practices, which could increase or decrease the total number of apartments needed over the 2008 – 2030 period. In addition, this estimate does not include the impact of higher property, sales, or income taxes, higher energy costs, reduction in household income or changes to Federal or State tax policies.

Housing Unit Replacement Rate

Years of Service	20 Years	Typical Range			60 Years
		30 Years	40 Years	50 Years	
Annual Loss Rate*	5.0%	3.3%	2.5%	2.0%	1.7%

* CEL & Associates, Inc. acknowledges that the current apartment unit inventory is not evenly distributed by the year of construction, but based on industry experience, the 50-year 2.0% annual replacement rate is considered conservative.

Total Number Annual Unit Replacements

Total Housing Units In 2008 ¹	130,357,000	
Percent apartment (5 – 50+ Units)	12.3%	
Total Apartment Units (5 – 50+ Units)	16,033,911	
Annual Replacement Rate	2.0%	
Total Number Annual Replacements	320,678	321,000²

¹ Estimated.

² Rounded.

Total Apartment Unit Demand

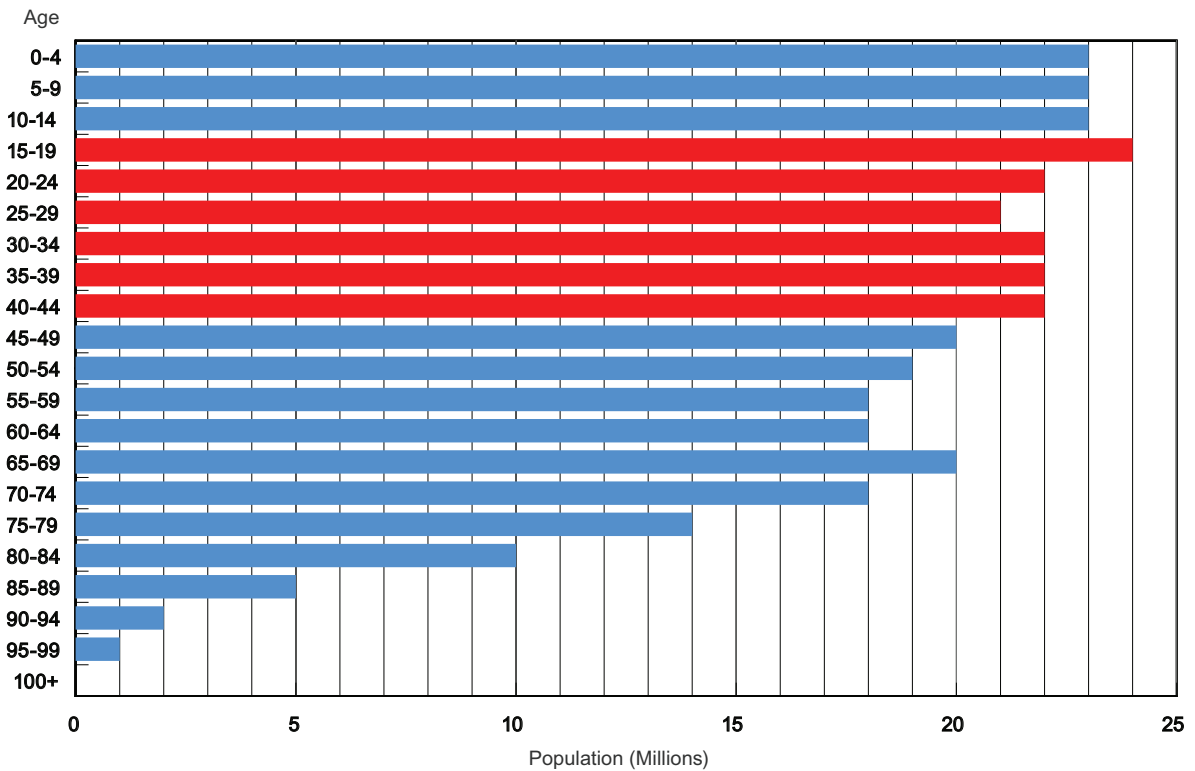
Period	# Growth-Related Apt. Units (5 – 50+)	# Replacement-Related Apt. Units (5 – 50+) ¹	Total Apartment Demand Units (5 – 50+)
2000 – 2010	1,164,000	3,210,000	4,374,000
2011 – 2020	1,262,000	3,210,000	4,472,000
2021 – 2030	1,218,000	3,210,000	4,428,000
Subtotal 00 – 30	3,644,000	9,630,000	13,274,000
Less 00 – 07 Supply Added	-2,399,000		-2,399,000
Less 00 – 07 Replacement		-2,247,000	-2,247,000
Total 08 – 30	1,245,000	7,383,000	8,628,000

¹ Assumed 321,000 x 10 years.

Trend 2 – The Y Generation Will Become The Next Wave Of Renters

Nearly 85 million U.S. citizens are in the Y Generation (born between 1977 and 1996), who were ages 12–31 in 2008. The overall Y Generation population is now larger than today’s Baby Boomer generation (76.9 million), and many are at or nearing the age when they become renters. This generation tends to prefer urban vs. suburban living, wants to be in 24/7 cities, is used to “college-like” living quarters and does not have enough savings or income to buy a home. A recent 2008 study conducted by the Aspen Institute examined the attitude preferences of MBA students’ intention/desire to seek work at companies that offer the potential to make a “contribution to society.” Raised by parents who were very “hands-on,” members of the Y Generation are ambitious and believe they can accomplish anything. It is likely this generation will involve their parents in housing selection, and in some cases employment. Utilizing the social media networks of YouTube, Facebook, Twitter, Craig’s List and MySpace, they will expect their residential landlords to do the same. Tolerant of diversity, this group will “want” to revitalize the urban core, live within proximity of a college or university for “continuing education,” and will “return home” if they can’t find a job or living accommodations that suit their “unique” needs. Currently 57% of those under age 34 rent, and of those under age 45, 46% rent. By 2010 nearly 107 million will be in the 18–44 age range (the prime renter group). By 2020 and 2030 this age group (the majority being Y Generation members) will increase to 112 million and 118 million, respectively, as highlighted on the following chart.

Population By Age 2030



Source: U.S. Census Bureau.

Based on three different “likely to rent” percentages, the number of potential renters between ages 18–44 years is highlighted at right.

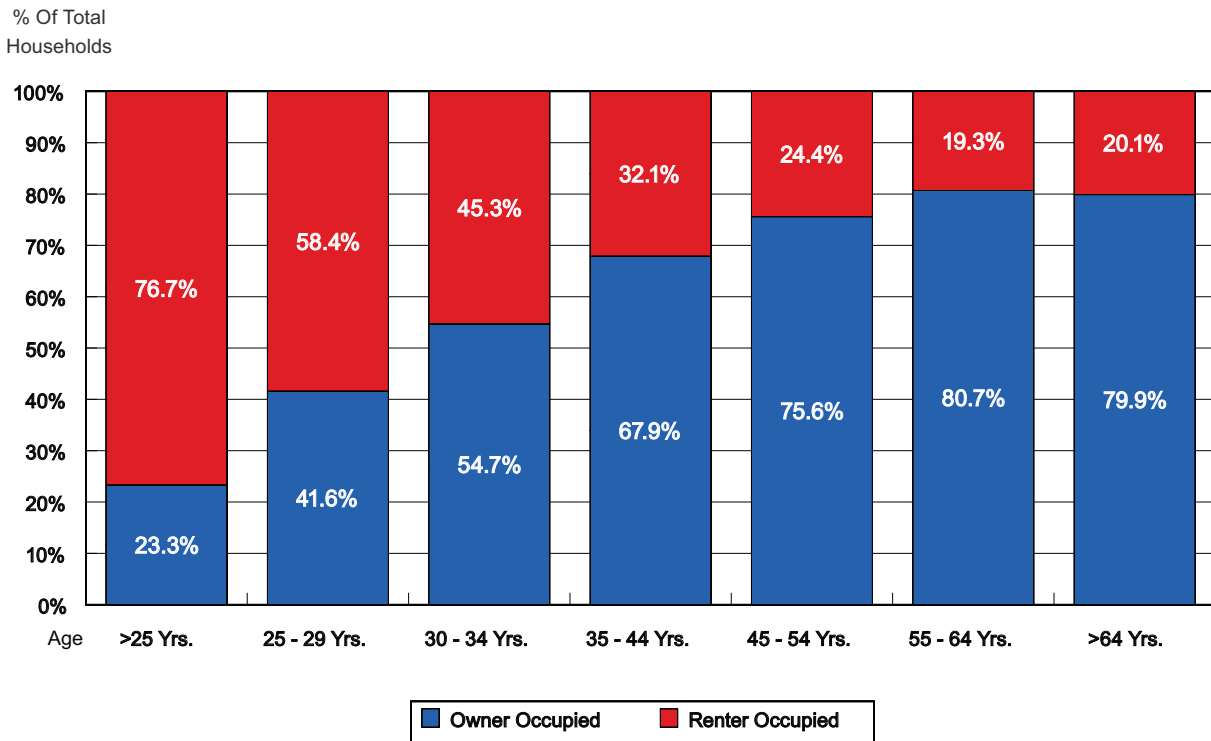
Thus, if the current percentage of 18–44-year-olds (46%) who rent remains fairly constant, the number of new renters could increase by 5.1 million (2010 – 2030). If the percentage of 18–44-year-olds increases due to an inability, unwillingness and/or lack of desire to own a single-family home, potential renters could jump from 49.2 million in 2010 to as many as 63.7 million by 2030...an increase of 14.5 million.

Potential 18–44-Year-Old Rental Market

Year	Population 18–44 Years	Propensity/Likelihood Of Renting		
		46%	50%	54%
2010	107m	49.2m	53.5m	57.8m
2020	112m	51.5m	56.0m	60.5m
2030	118m	54.3m	59.0m	63.7m

Assuming the Y Generation continues to delay or forgo marriage and starts a family later than their parents, it is increasingly likely that the average apartment household size will remain at approximately 1.9 – 2.3 for many years. In 1946 a Gallup poll reported that the “ideal” age for women to marry was 21; and for men, age 25. By 2006 the “ideal” marrying age had increased to age 27 for men and age 25 for women. The Y Generation appears to put personal and professional/career development ahead of marriage. Postponing marriage until they are “ready for it” is clearly a continuing and growing trend for those with college degrees. Delays in marriage and having children are likely to keep the demand for rental properties high and increase demand from 46% to perhaps as high as 50% or 54%. In addition, rising birthrates for unmarried women could result in fewer single-family households. In 2007, for example, 1.7 million babies born in the U.S. were to unmarried women, and teen mothers accounted for 23% of total births.

Young People Tied To Rent



Source: U.S. Census Bureau, American Housing Survey, 2007.

As the table above indicates, the younger the individual the more likely he/she will rent. With an average household size of 1.9 – 2.3, the number of potential renters (18–44) is significant. Using three average household sizes and three assumptions on the percentage of this population segment who rents, the potential number of rental units needed to accommodate the housing needs of the Y Generation is highlighted to the right.

Based on conservative estimates for average household size (about 2.1), and no change to the current propensity to rent for 18- to 44-year-olds (about 46%), as many as 25.9 million apartment units or more will be occupied predominately by Y Generation residents in 2030.

Potential Size Of 18–44-Year-Old Market

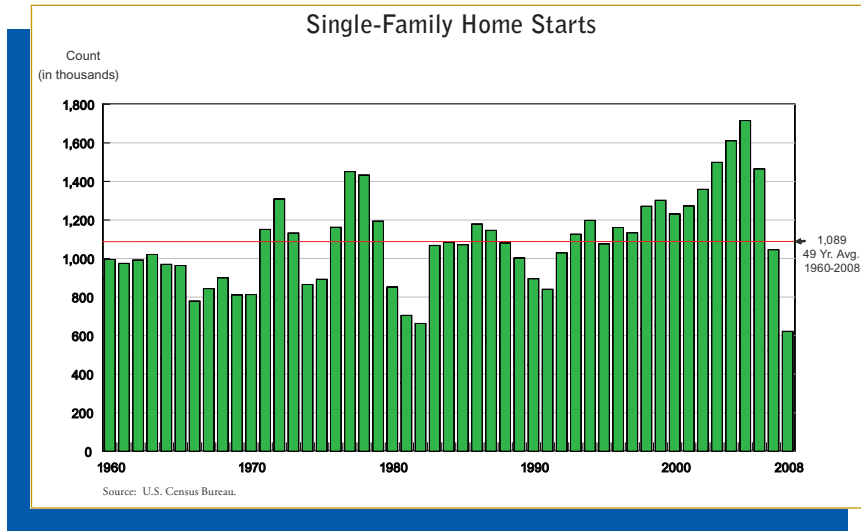
Years	% Renters	# Renters 18–44 Yrs.	# Rental Units Needed (Millions)		
			Average Household Size ¹		
			1.9	2.1	2.3
2010	46%	49.2m	25.9	23.4	21.4
2010	50%	53.5m	28.2	25.5	23.3
2010	54%	57.8m	30.4	27.5	25.1
2020	46%	51.5m	27.1	24.5	22.4
2020	50%	56.0m	29.5	26.7	24.3
2020	54%	60.5m	31.8	28.8	26.3
2030	46%	54.3m	28.6	25.9	23.6
2030	50%	59.0m	31.1	28.1	25.7
2030	54%	63.7m	33.5	30.3	27.7

¹ The average household size is based on a range of industry standards.

Trend 3 – The Appeal Of Homeownership Is Declining

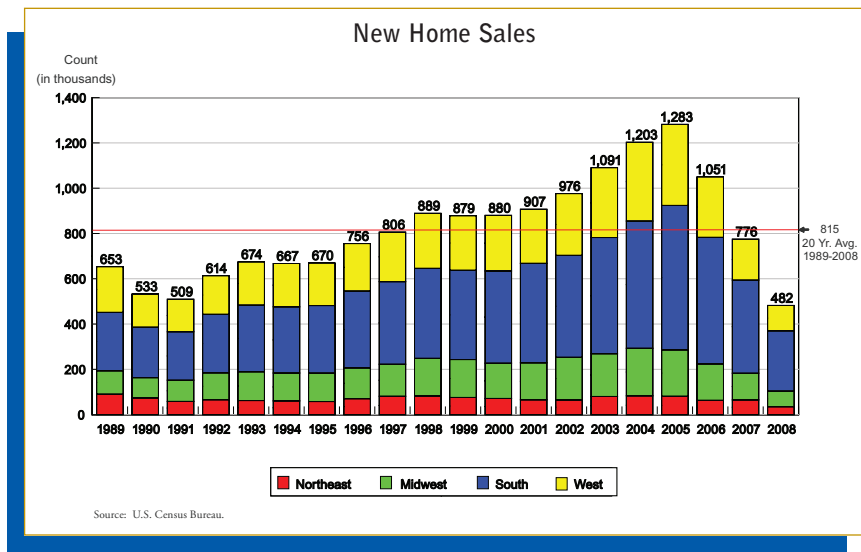
In 2007, single-family home starts were 1,046,000. Twelve months later, single-family home starts had dropped to only 622,000, a 40% decline. This level of single-family starts is one of the lowest since the U.S. Census Bureau has collected such data. During the periods 1980 – 1989 and 1990 – 1999, single-family starts averaged 985,000 and 1,103,400, respectively. However, from 2000 – 2007, the average number of new home starts jumped to nearly 1.4 million. While single-family home starts rose dramatically, so did sales of new and existing single-family homes and existing inventory of single-family homes, as illustrated in the following tables.

The recession of 2007 – 2009 saw the sales of new and existing single-family homes decline, as illustrated in the previous tables; however, the inventory of existing single-family homes for sale increased in 2008 to an all-time high.

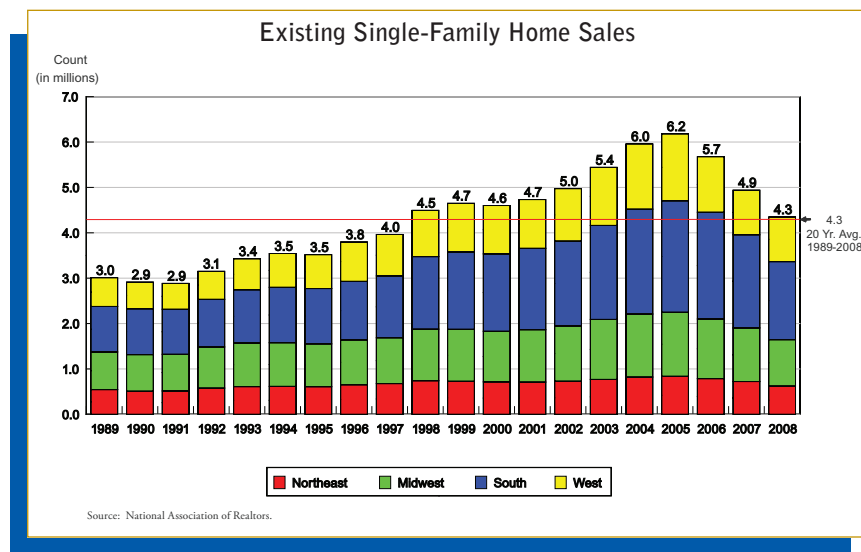


With a December 2008 existing inventory of new (12.9 months) and existing (8.7 months, down from 10.6 months in November) unsold single-family homes at all-time highs, sales volume at or near all-time lows, and the S&P/Case-Shiller Home Price Index indicating 20% or more decline in home values, the home building industry is unlikely to rebound for several more years.

CEL & Associates, Inc. estimates that the home building industry will shrink significantly, and it is very unlikely that annual, new home starts will reach the 800,000 level for many years. The annual number of new home starts into 2020 could very possibly remain around pre-2000 levels... assuming no change in lending practices, and/or governmental policies meant to encourage or discourage homeownership.



In addition, the appeal of homeownership may be changing. Since the peak of homeownership in 2006, more than \$6.1 trillion in home value has been lost. In calendar year 2008 alone, homeowners lost \$3.3 trillion in home value. Homeownership over the long term appears to produce very low annual returns. During the past 18 years, after-tax mortgage payments have averaged 26% more than rent payments, according to Green Street Advisors.

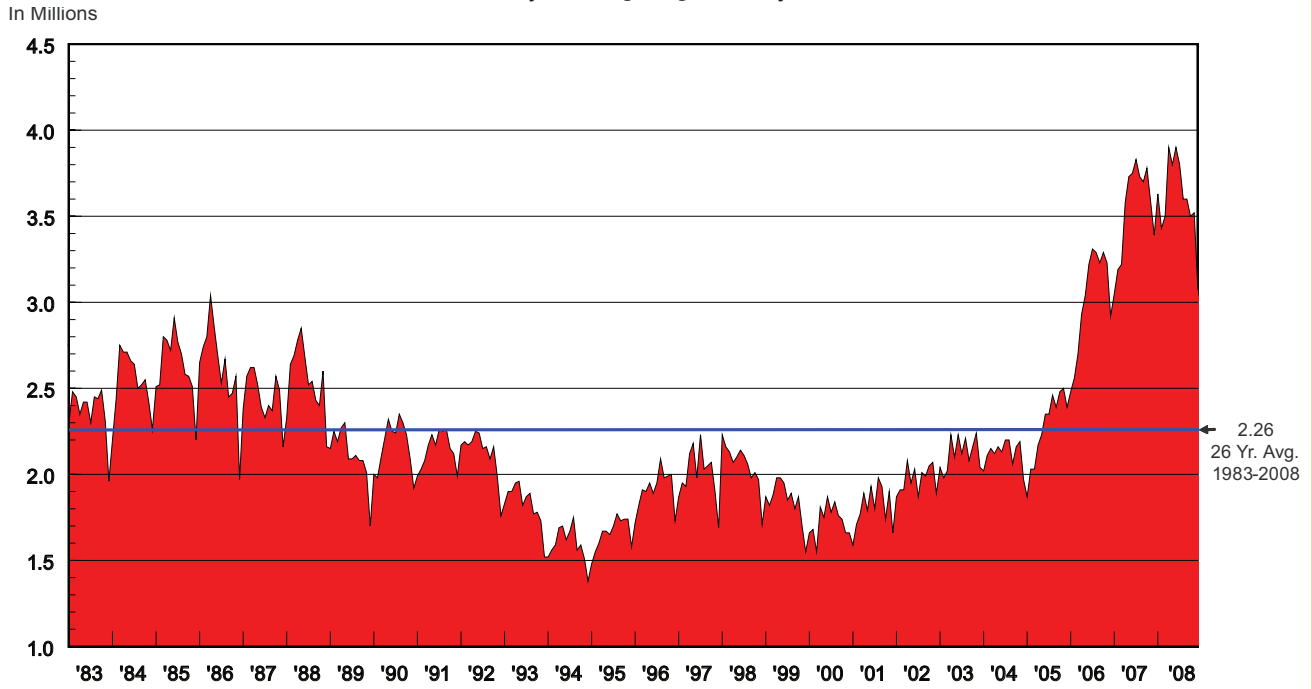


In 2006, at the height of the housing bubble, mortgage payments reached a high of 66% more than rent payments. While the mortgage payments could drop as short-term government bailouts and rent concessions take hold, the long-term outlook for homeownership appears to be waning. A housing shift to more urban locations will create new multihousing products (for sale and for rent) in walkable urban areas. Homeowners tend to have longer commuting times to and from work than renters.

A global economy and diversification in culture is also diluting the traditional U.S. “American Dream” of homeownership, as we have seen greater evidence of the “European model” of density and lifestyle, where homeownership is low in countries such as France (55%), Germany (42%) and Switzerland (35%). It is more than a remote

possibility that the U.S. homeownership rate (currently 67.5%) could drop to 57% – 62% during the next decade. Remember, only since the Baby Boomer generation of buyers has the U.S. homeownership risen above 60%. Recent statistics on renters

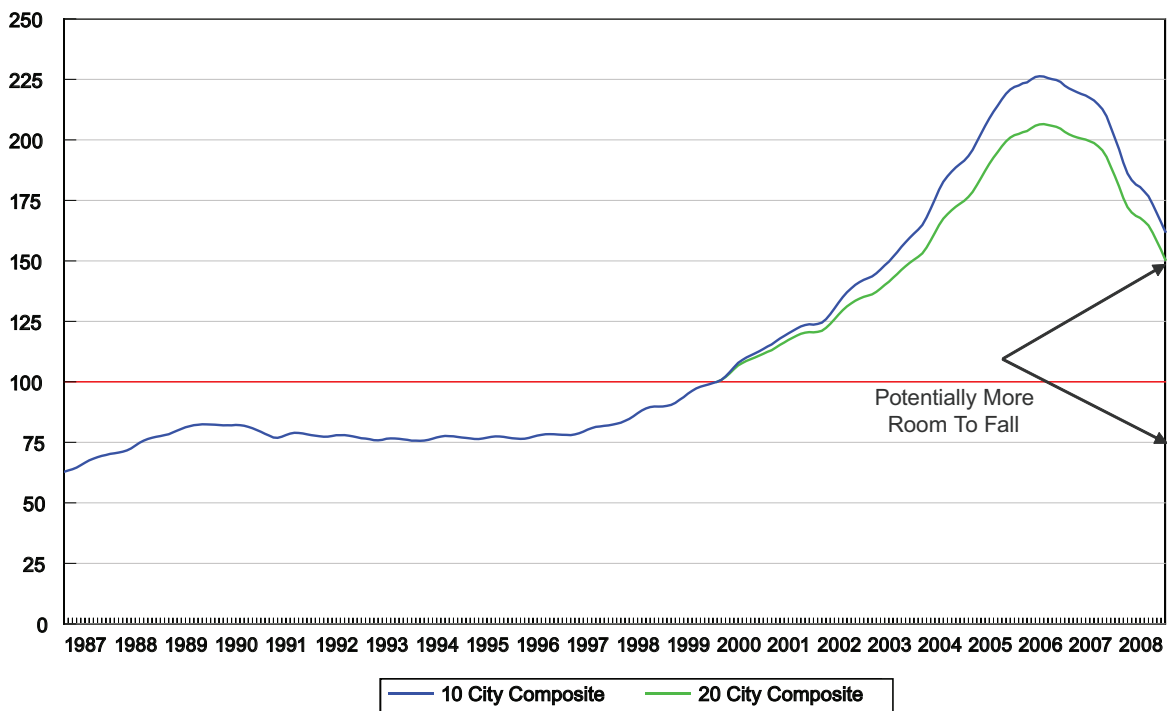
Inventory Existing Single-Family Homes



Source: National Association Of Realtors

moving out to buy homes in 3Q 2008 were down 10% – 15% from their high in 2004. Today only 12% – 14% of renters are leaving to buy a home... a number that is expected to decline further in the short term. Nearly 80% of the benefits from mortgage interest and property-tax deductions go to the top 20% of taxpayers in terms of income, according to the Urban-Brookings Tax Policy Center, thus the mortgage interest deduction may well disappear or be restricted to first-time buyers. Major home repairs and maintenance usually have a per-year cost of 2% – 4% of the home purchase price, and financing fees and sales commissions can equate to 7% – 10% of the cost of buying a home. **Renting is now becoming an economic as well as a lifestyle choice.**

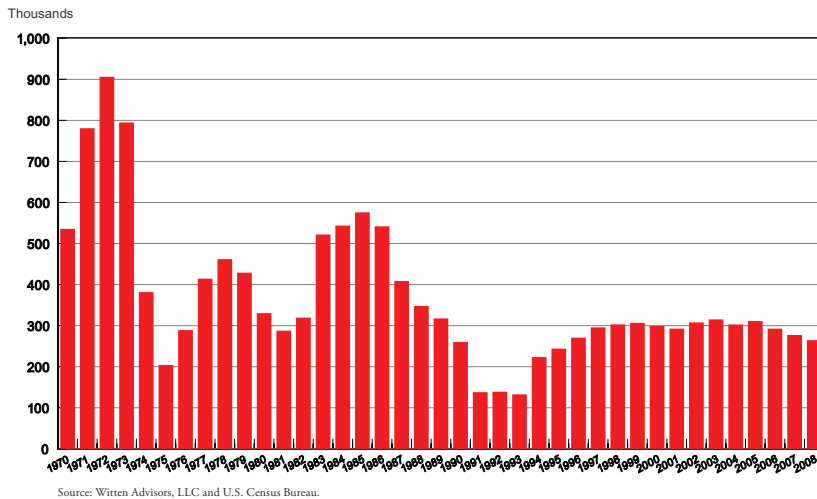
S&P/Case-Shiller Home Price Indices



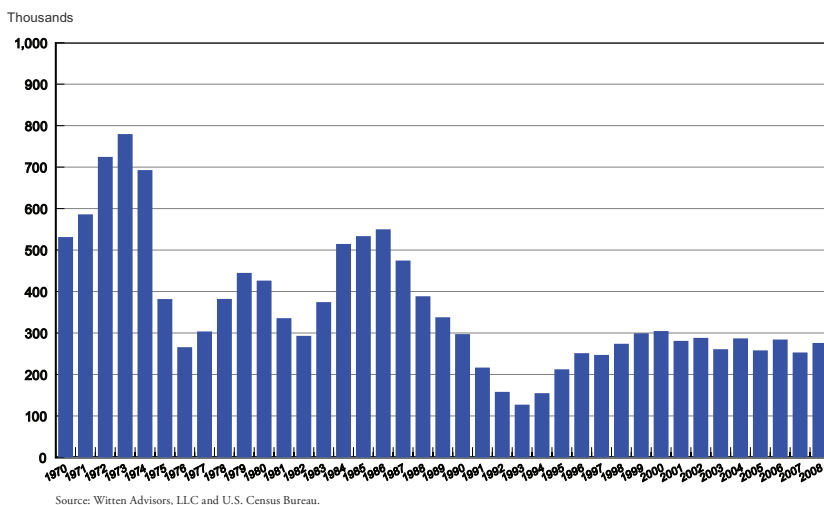
Both indices have base value of 100 in January 2000.

Source: Standard & Poor's

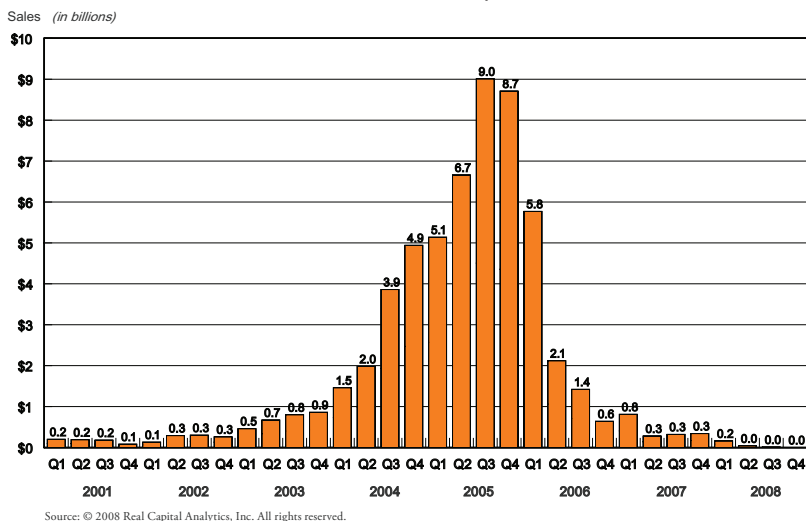
Number Of Multifamily Starts 5+, 1970 – 2008



Number Of Multifamily Completions 5+, 1970 – 2008



Demise Of Condo Converter, 2001 – 2008



In addition, according to historical S&P/Case-Shiller Home Price Indices, the value of many single-family homes will likely decline further in 2009 – 2010. As home values drop, the percentage of homeowners who have mortgages higher than the value of their home will increase. In the 2009 – 2015 period many homeowners will become, in essence, “renters” as home prices remain low by historical standards and there is little or no equity in the home. The financial crisis of 2008 – 2009 has narrowed not expanded the pool of potential homeowners. Based on current trending data, the recovery of the single-family home market could be 10 – 15 years away. New and more stringent borrowing criteria will thus be put in place that will require prospective homeowners to have a sufficient down payment, proof of an ability to pay the monthly debt service and an acceptable credit history. Homeowning will no longer be as attractive as it was prior to 2008.

Trend 4 – Multifamily Starts Likely To Rebound As Condo Converters Exit

Since the mid-1990s, the apartment industry has averaged slightly less than 300,000 starts and 275,000 completions per year, as illustrated in the following tables.

The robust single-family home market has kept multifamily development activity far below the levels experienced in the 1980s. In addition, many apartment developers and owners shifted to the condo and/or condo-converter marketplace. As the following table highlights, the number of apartment properties sold for condo conversion peaked in 2005.

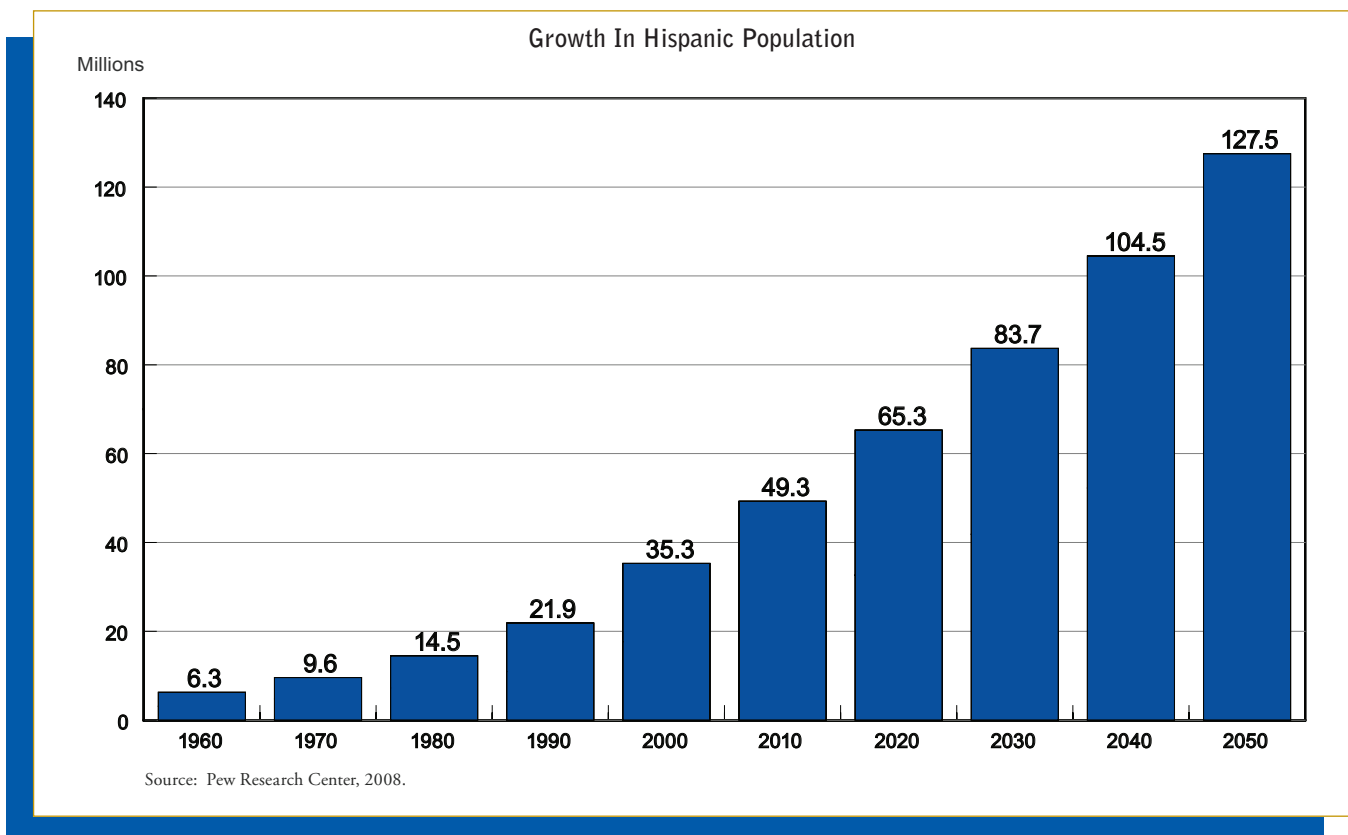
Today the home building industry is in turmoil, and condo developers and condo converters have exited the marketplace...albeit with several lingering projects at or nearing a need for recapitalization at significantly reduced values. **A return to normalcy within the apartment industry is soon to begin, and the number of 5+ housing starts is expected to rise dramatically over the next 20 years.** Between 2010 and 2013, apartment rents should rise significantly as the lack of new development projects started during 2007 – 2009 create a supply/demand imbalance. This imbalance could continue into 2014 – 2015 until normal levels of apartment starts return. This increase in starts could be tempered by a growing difficulty to find and entitle land where housing demand is acute.

In addition to the decline in single-family home starts and the likely rise in multifamily starts, the protracted housing market downturn has also made America a less mobile society. The population growth within the geographic areas of the U.S. which traditionally have attracted retirees, job seekers, and lifestyle-seeking citizens has slowed. The level of employment diffusion is now below the low points of the 1990 – 1991 and 2001 recessions. There are now fewer areas of the country that look attractive to those seeking jobs. While the Sun Belt states are still attracting more population, the beneficiary of this reduced migration flow are likely to be apartment owners. Those residents who tend to relocate or are more mobile are generally those age 18–44 years... who are starting their careers and/or households. Thus the outlook for apartment demand is expected to increase dramatically in the Sun Belt states.

Trend 5 – Hispanic Population Is Growing Rapidly And Tends To Rent

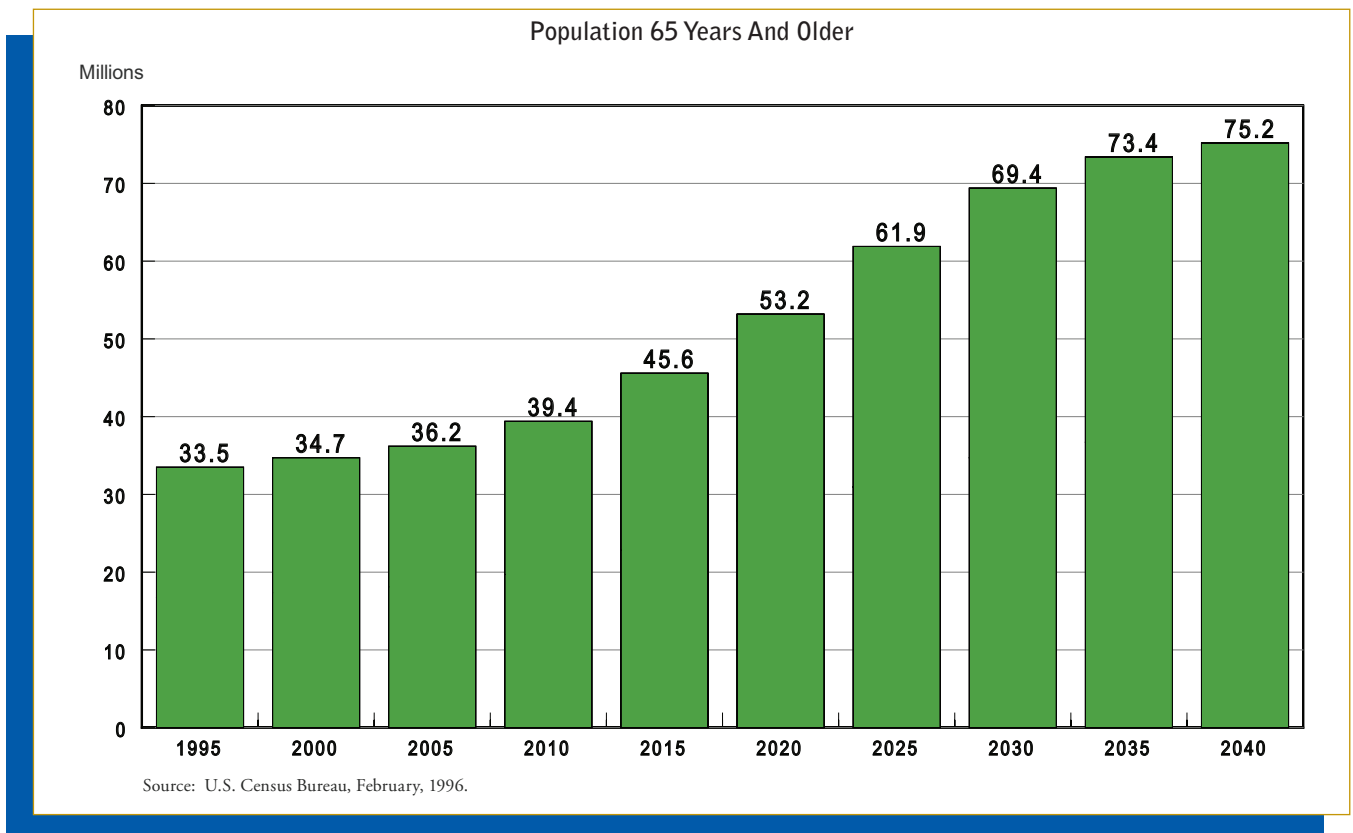
In 2000 the U.S. was home to 35.3 million Hispanics. By 2010 this ethnic group’s population is expected to jump to 49.7 million, and by 2020 the Hispanic population is expected to be 66.4 million. In 2030, 85.9 million Hispanics are projected to be living in the U.S., and 54% of the U.S. population growth between 2000 and 2030 will be Hispanic. In 2008 the homeownership rate for all Hispanics was 48.9%.

An estimated additional 11 – 12 million Hispanics also are in the U.S. illegally. According to a recent Pew Research Center study, 36% of Hispanics fear that their home may go into foreclosure, and in 2006 Hispanics had taken out approximately 40% of all subprime loans. Based on a projected Hispanic population of 83.7 million in 2030, CEL & Associates, Inc. estimates there will be a rental housing demand for 12.9 million (1 – 50+) units (83.7m x 54% who rent, divided by 3.5 average household size) to accommodate the demand for this population group. The percentage of Hispanic renters could rise if the current recession and recovery are prolonged. The number of rental units with a Hispanic household, at an average household size of 3.5, will increase from 6.5 million in 2000 to 12.9 million by 2030. Serving the housing needs of this burgeoning population will likely be a focus of future governmental policy and new residential development activity. The apartment industry will be a beneficiary of this rising immigrant class as “newly arrived” Hispanics seek “affordable” housing options in or adjacent to major employment centers.



Trend 6 – An Aging Population Shifts Housing Patterns

By 2010, 40.2 million Americans will be age 65 and older. By 2020 and 2030, the number of U.S. residents age 65 and older increases to 54.8 million and 72.1 million, respectively. By 2050 the U.S. senior population is projected to be 86.7 million. The oldest population group (those age 85 and above) is projected to double...from 4.7 million in 2003 to 9.6 million in 2030... and double again to 20.9 million by 2050. The likelihood of renting increases as householders age. Approximately 33% of U.S. citizens age 85 years and older are renters (versus only 18% age 60–64 years). With increasing life expectancy, medical and well-ness advances improving and healthcare services more accessible, the number of aging Americans will increase, creating new and additional demands for senior-related housing options.



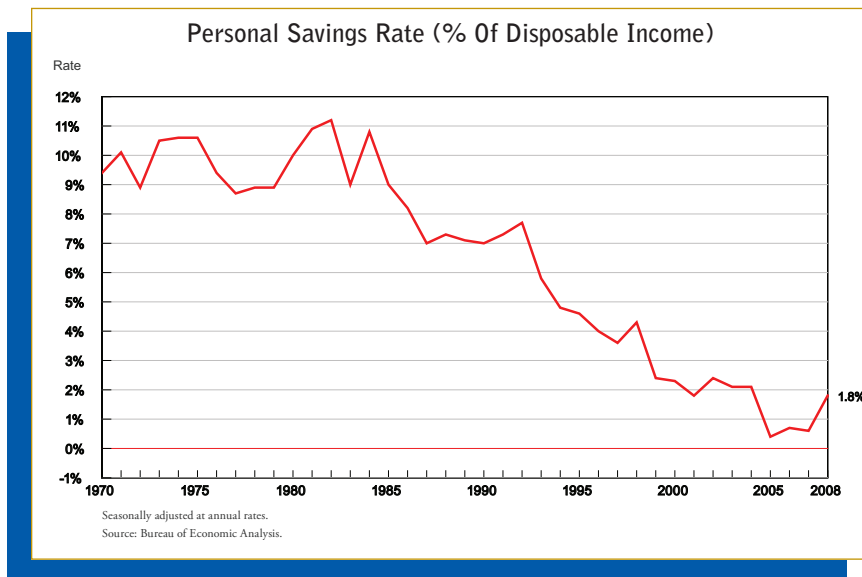
In addition, it would not be surprising if aging Baby Boomers lacking sufficient funds to fully retire downsize to apartments. The combination of rising taxes, home maintenance and repair costs, insurance and distance from major retail and healthcare facilities could cause a growing number of retirees to become renters. Many of these retirees may sell their single-family homes and, if the mortgage has been paid off, provide financing for the buyer. This source of income plus Social Security and/or other retirement monies may enable many to seek a smaller, more urban lifestyle choice, with sufficient income to enjoy their respective “retirement years”.

Trend 7 – Job Growth In Urban Areas

More than 80% of U.S. jobs are located in urban areas, and most U.S. jobs are located in the top 50 MSAs. The average, national, single-family home price is now at more than \$181,000, and considerably higher in the top MSAs. For a prospective home buyer facing the traditional 30% income-to-loan qualifying criterion, the vast majority of young adults seeking work will not be able to own a home and are likely to be renters...many for much of their lifetime. This demand for affordable and workforce housing will generate a wave of redevelopment, mixed-use and transit-proximate rental housing options in walkable communities. Work-life balance is important to the Y Generation, and most appear to want more personal time, so are willing to forgo long commutes to recapture that time, albeit with higher density. In addition, the emergence of a rent-to-own high density housing option will be preferable, as 41% of men and 49% of women want to own a home but cannot afford it initially.

Trend 8 – Affordability

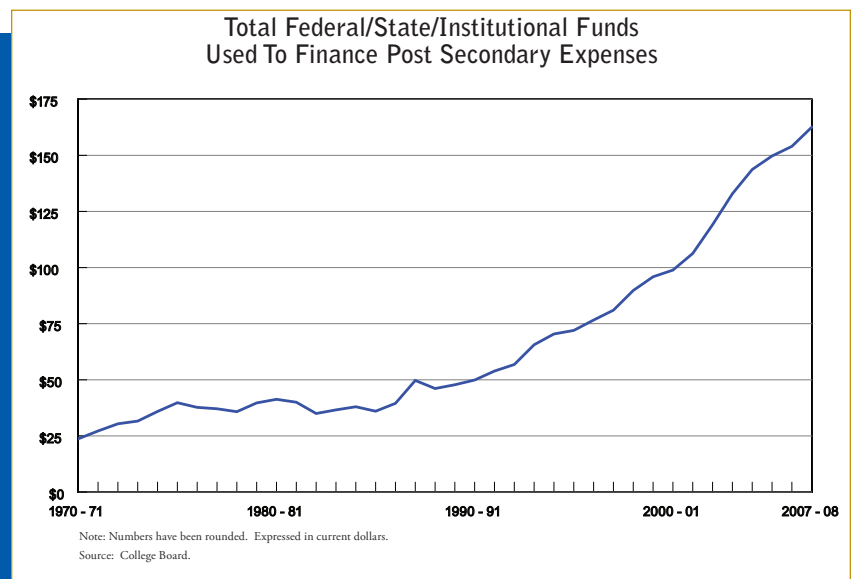
The recent collapse of many single-family home loan lenders as a result of the subprime lending debacle and lending policies to those generally unable to make market rate mortgage payments is now becoming a benefit to the apartment industry. According to a report by Goldman Sachs Group, Inc. and Morgan Stanley, at the end of 2006, 6% of mortgage borrowers had negative equity. This percentage is expected to increase to 21% or 10.5 million households. In 2008, U.S. home values declined \$3.3 trillion, and since the housing peak in 2006 \$6.1 trillion in home value has been lost. Foreclosures made up nearly 20% of all transaction value in 2008. Stringent underwriting and very disciplined lending practices will likely prevail for at least the next decade. With memories fresh on the \$500+ billion recent and potential subprime loan losses, government regulators, appraisers, loan agents, banks, rating agencies and others will make buying a home an option for only the most qualified. Of note: overall savings rates fell from 8% in the early 1990s to 1.8% in 2008.



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Average household debt has nearly doubled, outstanding credit card debt is now over \$960 billion and several trillion dollars in household net worth has been lost with the collapse of the stock market and home values. According to several economists, the excessive borrowing and deficit spending of the Obama administration will leave a present-value legacy of \$6.5 trillion of additional future taxes unless government spending declines dramatically. Many Americans have debt obligations far more than their capacity to pay, and higher taxes will only result in a declining ability of Americans to own homes.

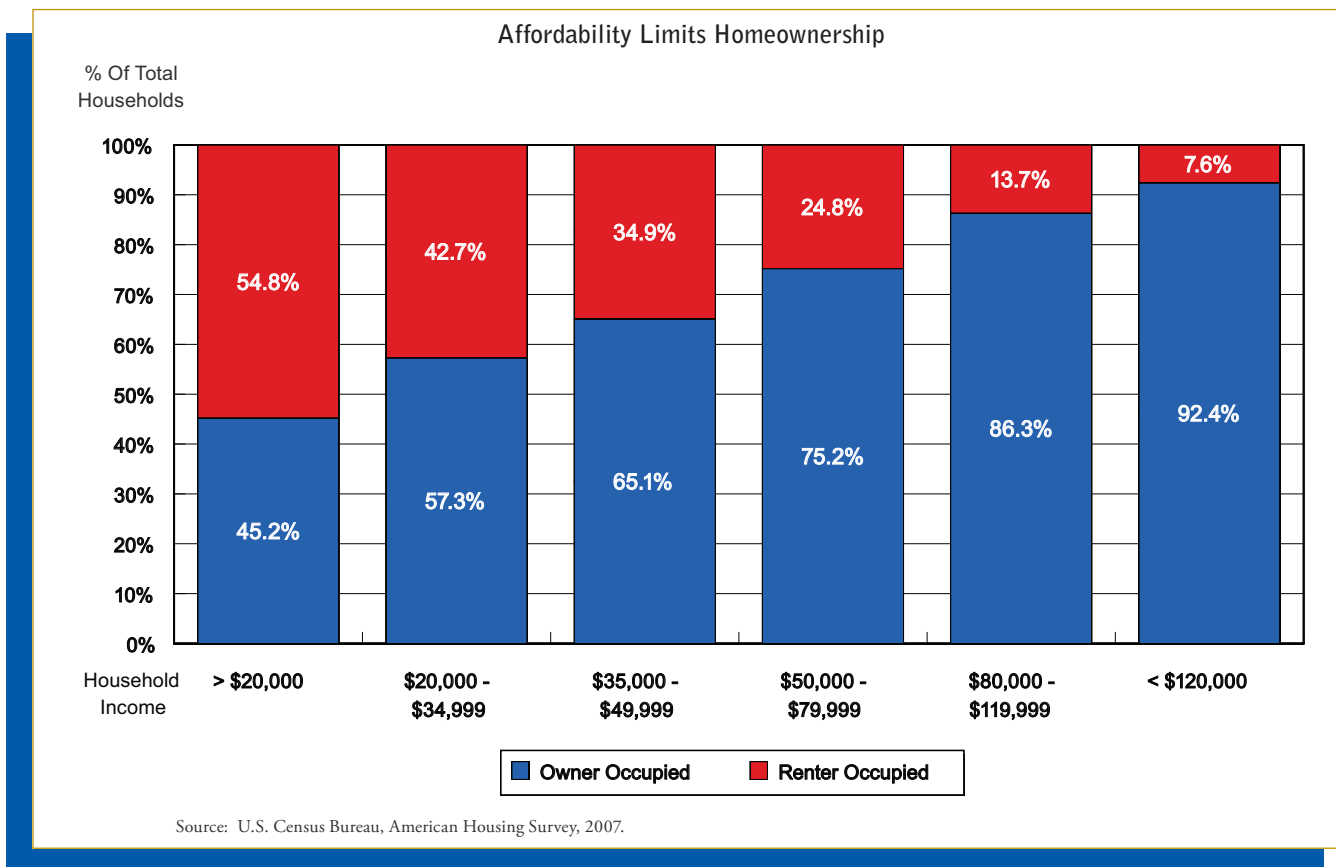
For those 25–34 years old, the debt load relative to their asset base has increased between 1985 and 2005. Census data shows that college graduates earn on average \$57,500 per year...hardly enough to purchase a home. A 2007 study by SLM Corporation (“Sallie Mae”) showed that more than half of college students had credit card debt in excess of \$5,000 while in school, and a third had more than \$10,000. Further, as tuitions and fees at public four-year colleges have risen 50% over the past ten years and with more than \$500 billion in outstanding student loan debt, there is a potentially more difficult financial road ahead for many young, first-time home buyers.



In addition, flat or declining wages and less disposable income will contribute to a real and perceived need to reduce the cost of living expenditures...and apartments tend to be less expensive than single-family homes or condominiums. According to Mark Zandi, chief economist at Moody’s Economy.com, “over the last 10 years education costs have risen 5.91% annually and health-care costs have gone up 4.16% annually, while wages and income have risen only 3.7% annually over the same span.” A new report by the National Low Income Housing Coalition revealed that a “person with a full-time job needs to earn an hourly wage of \$17.84 to afford a two-bedroom rental” apartment. This hourly rate is much higher in the desired urban job centers across the U.S. With a U.S. economy experiencing the “paradox of thrift,” a declining consumer expenditure pattern, a rising savings rate

and an inability to purchase an existing home from a reluctant seller who still expects to make money from the sale, the demand for apartment living should begin to increase dramatically. The overall issue of affordability (or lack thereof) creates demand for apartment living.

CEL & Associates, Inc. expects the federal government to invest hundreds of millions of dollars in infrastructure, urban renewal, sustainable technologies and affordable housing initiatives. The recent takeover of Freddie Mac and Fannie Mae by the Federal Housing Finance Agency is likely to bring additional fiscal responsibility to both GSEs and in the near term reduce national mortgage originations. Recent trends indicate that added fees based on credit scores also will increase the cost of financing a home purchase.



Trend 9 – States And Localities Take Action

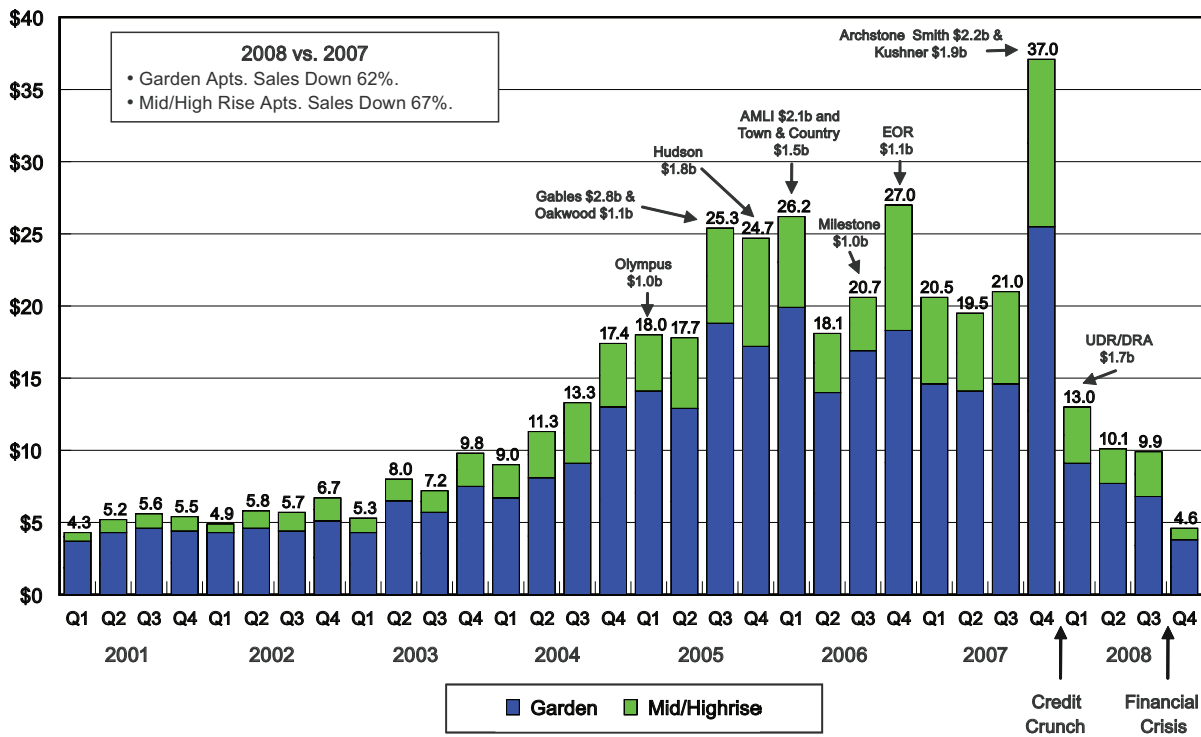
According to a 2007 study by Harvard University’s Joint Center for Housing Studies, 37 states and more than 350 counties and cities “have used dedicated sources of public revenue...to create housing trust funds that collectively spend nearly \$1.0 billion annually on the production and preservation of affordable housing.” More than 130 localities nationwide have taken steps to mandate the production of affordable housing through inclusionary zoning ordinances. CEL & Associates, Inc. expects the federal government to increase the minimum wage standard and Earned Income Tax Credit while mandating states, counties and cities to prepare regional housing strategies that encourage production of affordable rental housing options and support non-profit regional housing corporations. Increases in HOPE VI funding are likely, while programs such as the Low Income Housing Tax Credit, Community Development Block Grants and the HOME Investment Partnership Program will receive greater attention and funding. In addition, changes in regulatory and/or tax codes regarding the development of new or conversion of existing apartment units to a more “sustainable” property could render many apartment buildings in need of significant redevelopment.

Trend 10 – Investors Like Apartments

Investors, like city planners, demographers and employers recognize the growing need for affordable, workforce housing. Driven by the availability of agency and conventional financing, the apartment industry has attracted institutional and private capital. Between 2000 and 2008, over \$438 billion of institutional-grade apartment assets have been sold. The following two tables on the next page illustrate the recent sales and cap rate activity within the apartment industry.

Sales Volume – Apartments 2001 – 2008

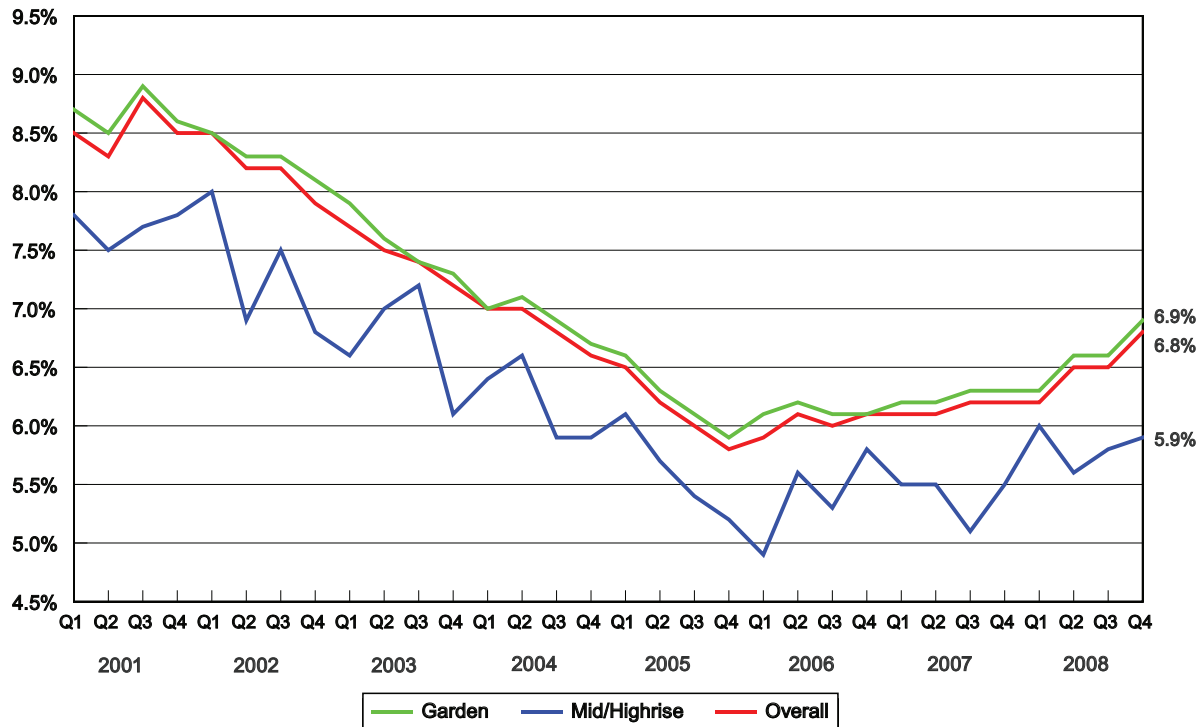
Sales (in billions)



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Cap Rates – Apartments 2001 – 2008

Cap Rate



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Since 1996, financial returns within the apartment Equity REIT sector have outperformed the S&P 500 and NASDAQ.

During the next 20 years, investor interest in apartment buildings will continue, drawn by growing demand, communities seeking more vibrant urban areas, employers who want access to an educated workforce and public/private partnerships to revitalize the nation's urban and suburban locations. From those investors who want to acquire and/or (re)develop an existing 5- or 10-unit or more apartment buildings to those entities which want to acquire or redevelop a 150-, 200-, 300-unit or more Class A or B apartment property, the ownership of apartment buildings will continue to attract capital. Apartments have consistently shown resiliency during periods of economic downturn and/or recession. The fact that apartments have shorter lease terms makes them attractive to investors who want greater market flexibility. Apartments are fundamentally a paint and carpet business, while office, retail and industrial can and do require extensive tenant improvement dollars and sizeable leasing commissions. Apartments continue to be under-weighted within institutional portfolios. According to NACREIF, "apartments convert 83% of net operation income into cash flow." The historically attractive loan terms preferred by Fannie Mae and Freddie Mac should continue, albeit at a significantly reduced level and with slightly different terms. It is very likely that a national rating system will be put in place to reward the "good" borrowers and create disincentives for the "inferior" borrowers.

Real Estate Becomes A Preferred Asset Class

Year	NAREIT Equity REIT Index Of Total Returns		Stocks		
	Apt.	All Equity REITS	S&P 500	Russell 2000	NASDAQ
1996	28.9%	35.3%	22.7%	16.5%	23.0%
1997	16.0%	20.3%	33.1%	22.4%	22.1%
1998	-8.8%	-17.5%	28.6%	-2.5%	39.6%
1999	10.7%	-4.6%	21.0%	21.3%	85.6%
2000	35.5%	26.4%	-9.0%	-3.0%	-39.3%
2001	8.7%	13.9%	-11.8%	2.5%	-21.1%
2002	-6.2%	3.8%	-22.0%	-20.4%	-31.2%
2003	25.5%	37.1%	28.7%	47.3%	50.0%
2004	34.7%	31.6%	10.8%	18.3%	8.6%
2005	-14.7%	12.2%	4.9%	4.5%	1.4%
2006	40.0%	35.1%	15.8%	18.4%	9.5%
2007	-25.4%	-15.7%	5.5%	-1.6%	9.8%
2008	-25.1%	-37.7%	-37.0%	-33.8%	-40.5%
Avg. Annual Return	9.2%	10.8%	7.0%	6.9%	9.0%

Total Return: A stock's dividend income plus capital appreciation, before taxes and commissions. Source: NAREIT and CEL & Associates, Inc.

Summary Of Demand Variables

The future of the apartment industry is very robust. Driven by changing demographics (growth in the aging, Hispanic and Y Generation populations), softening but continuing lack of affordability, a limited number of apartment units under development in 2008 – 2009, a dramatic decline in net worth as a result of the 2008 – 2009 recession, rising taxes and debt to support an aggressive political and social agenda by the White House, and more stringent underwriting criteria for home loan applicants will shift the focus away from single family homeownership toward renting. The rapid rise in homeownership, long the standard of economic growth, will decline as America returns to levels of the 1960s. Renting in 2009 has achieved parity with homeownership as an equal housing option for millions of Americans.

The Apartment Of The Future

So what will the apartment living experience be like in the future? How will the resident experience of tomorrow differ from today? The following paragraph should shed a little light on what the apartment industry can look forward to.

Imagine...you have just signed your state-approved, standard apartment lease online after taking a virtual tour, reviewing the published rating data from an independent consumer group and blogging with current community residents...your new neighbors. You have set up and printed out your biometric access card before arriving at your new home. As your car approaches, a sensor scans your parking and entrance access chip on the car's window to open gates and welcome you. The lapel chip you received from the Welcome Office activates access to the elevator and notifies the on-site team of your arrival. (This notification system was installed after the last natural disaster). Walking into your new unit, you are pleased to note that all paint colors, ame-

nities, appliances and features ordered online have been added. First, you activate the smart walls, which are linked to emergency centers, security, your doctor(s) and the hospital; they can sense any sudden medical emergency. You sync your laptop, PDA, smart phone and your “Twin” (an electronic companion you have had since birth that “remembers” everything in your life) so all of the wireless features of your unit are communicating with each other. Next, you slip your custom “My Home” disk into the built-in “control panel” and all your favorite songs, television/cable shows and Internet links are set up for flat-screen monitors throughout the unit. Your digital artwork now appears in all the wall-mounted picture frames, and your customized multimedia room has been activated. The sensor-operated faucets and touch-screen appliances are working, all approved “green” materials were used, and the special automated window shades now operate between two panes of glass. Perhaps the most exciting feature is your “assigned robot”...a featured amenity in this apartment complex – “free” with your lease – and you can’t wait to activate your new copier that reproduces objects, not merely paper copies. Opening your gift basket, you sit back, sigh and think...“Life is pretty good.”

Conclusion

Looking beyond today’s economic and financial crises du jour, the demographic facts for the future of the apartment industry are clear. The U.S. population will likely shift back to a much higher number of apartment dwellers for financial, lifestyle, age, health and/or personal reasons. What is needed...governmental and regulatory recognition that rental housing must be a priority to bring the workforce closer to available jobs and provide a shelter option for those with reduced financial means, serve as a catalyst for urban renewal and to accommodate a future tsunami of potential renters. Several potential threats to the apartment industry include: national rent control for those who have loans from Freddie Mac, Fannie Mae or any lender receiving government assistance; restrictive policies or mandates from local, state or federal agencies that drive construction or operating costs higher than what the renter is willing or able to pay; and over-zealous “greening” or “immigration enforcement” laws that place the apartment owner/operator in a regulatory role. These are viable concerns. However, an active involvement by all those who lead, work, and serve the apartment industry can assure an incredible future. ●

FOR MORE INFORMATION

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