

The Apartment Report™

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Vol. 20, No. 21

December 6, 2010

MANAGEMENT COMPANIES MAP OUT 2011 PLANS

Look for a high transaction environment to bring a broader base of clients on the hunt for new management companies, and **Pinnacle Family of Companies, Greystar Management, Riverstone Residential, The Bozzuto Group** and **Eugene Burger Management Corporation (EBMC)** all hope to swoop up some new contracts. Pinnacle's focus next year is on primary cities, and it already has a little more than 10% growth in the works, while Greystar gains 32 properties through a management company acquisition and should add 100 new properties in 2011. Riverstone bets on 20% growth next year and will build out some newer markets. Count on Bozzuto to grow its management portfolio about 10% a year going forward in the Northeast, while EBMC hopes to expand 5% to 10% in 2011, mainly in California.

Transaction volume will be robust next year because of more favorable financing options and compressing caps, providing more opportunities for management companies to get in those assets. Foreclosures stemming from tighter lending parameters and maturing loans will also create an abundance of opportunities for management companies to provide services to lenders and receivers. In light of the current economy, expect a leading management strategy to focus on recovering lowered rents and have new tenants pay slightly higher rents than previous residents. Managers should see several markets experience some modest ability to increase rents and reduce concessions as demand catches up with supply. Management companies bet on Texas, Washington, D.C., major coastal cities and the Northeast for bountiful 2011 prospects.

Despite the voluminous business prospects, a big aim for management companies next year is to find ways to get more done for less money, which will involve greater use of technology, job restructuring and green initiatives. Look for more players to adopt automated revenue management systems next year, something that has been around for a while but is gaining significant acceptance in the market, especially with large institutional properties. Social networking will also play a big role in how managers work in 2011. Management was once a nine-to-five business but now goes around the clock with residents requiring 24-hour access. As such, companies need to take advantage of opportunities to improve technology to attract and retain residents. Eventually, residents will be able to do everything online except pick up their keys. Some developers and owners may also consider taking management in house in 2011 to save on the fees, but most will realize this is not a wise decision because overhead costs will exceed revenue and send them back into the arms of third-party players.

Anticipate Pinnacle to add 20,000 net new units next year. The current portfolio boasts 183,000 to 185,000 units, with 20,300 added by year's end. The newest properties were in Florida, Minneapolis and Las Vegas. Chief Administrative Officer **Ed Wolff**'s main objective next year will be on property performance, leveraging technology to improve performance, heightening marketing awareness, reducing turnover and minimizing delinquency, all while focusing on key performance indicators. He will continue to capitalize on good value play strategies and take advantage of the current market. Expect Pinnacle to be bullish in the coastal cities and major markets in Texas, including Dallas, Houston and San Antonio where Wolff sees improvement. Management fees fall in the 3% to 5% range.

Greystar will add 135 new properties this year and banks on around 100 in 2011. There are currently 175,000 units in the portfolio, of which around 16,000 are owned. Most of the product is market rate and predominately Class A and B. There are around 13,000 student beds and 2,500 senior units. Executive Director **Andrew Livingstone** believes a change in property ownership will continue to grow the business next year. Perhaps Greystar's most notable move this year is gaining 32 properties in Washington and Oregon with the recent purchase of Seattle-based **Glacier Real Estate Services**. The deal was perfect because Greystar wanted to increase its presence in the Seattle MSA for a couple years and the timing was right for both companies. Livingstone bets on the Glacier team's expertise in the Seattle area to help Greystar beat the competition in the market. Other acquisitions could be possible next year as good opportunities come up in the right areas. Fees are around 3%.

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Greystar is in 32 states and more than 100 markets, including Texas, Phoenix, the Carolinas, Atlanta, Charlotte and Raleigh, N.C., Southern California, the Midwest and D.C. It is also the largest fee manager in Florida. One of the goals for 2011 is to work with the onsite staff to provide personalized customer service for residents and prospects and improve technology.

Riverstone Residential hopes to add 150 new properties or 35,000 new units next year. There are currently 165,000 units in the portfolio and 100% of that is third party. Odds are the company will add 125 properties total for this year or just under 29,000 units. The bulk of the product, 88% to 90%, is market rate and around 10% accounts for affordable units. Class A and B each make up 40% of the product and 20% is C. Riverstone is located in 50 different markets nationwide. President **Terry Danner** wants to fill in markets where Riverstone does not have much of a presence including Salt Lake City, Chicago and St. Louis, with at least one dozen properties needed in each market. Expect bullish growth in Phoenix, as well. Fees range between 2% and 3% depending on the property and the market. In 2009, Riverstone implemented a business development team to focus on attracting new clients, a good strategy that led to half of the contracts this year. Look for an emphasis on affordable properties next year and Danner to beef up the transaction systems team. He points out that there is always a need for property management so this is a great industry to be in.

Bozzuto's portfolio houses more than 30,000 units and President of the Management Company **Julie Smith** counts on adding 3,000 doors next year. Third party makes up 75% of the portfolio. Bozzuto will add 3,040 units by the end of 2010, with around 1,200 coming this month. Market focus remains on the Northeast and most properties are located in Washington, D.C., with some in Baltimore, Philadelphia, New York and New Jersey. Smith notes that the plan for now is to stay in the existing footprint in the Northeast and she has a three-hour door-to-door strategy. Most units are market rate, in addition to about 2,500 affordable units spanning 13 properties and a small amount of senior housing. About 65% are Class A product, with 25% falling under Class B and 10% Class C. Smith sees a lot of opportunity in new transit-oriented developments in urban markets, assuming the deals can get financing. Her strategy has not changed much in the last few years because being an institutional manager in the Northeast has served Bozzuto well through all the cycles.

EBMC manages 2,500 market-rate apartments, 4,000 affordable units, as well as 20,000 HOAs, single-family and commercial properties. Around 5% of those are owned and 95% are third-party contracts. SVP **Jay Kacirk** hopes to see a 5% to 10% increase in new contracts or units in 2011. EBMC added about 36 contracts in 2010 throughout all its property types. Class A assets make up 35% of the product, while 45% are B and 20% are C. EBMC works throughout California including San Diego, Orange County, Los Angeles, Sacramento and Sonoma, along with Reno and Las Vegas, Nev. Fees are 3% of income on the low end. In light of the economy, the company focuses on capitalizing on energy-reducing programs that can be implemented at little or no cost due to government or utility provider subsidies. Kacirk does not plan to enter any new markets next year but would welcome the acquisition of existing management firms in the areas he currently serves.

DEVELOPERS OUTLINE BLUEPRINTS

Look for the rental sector to strengthen moderately and be one of the few bright spots for development next year. Several factors are already at work to set the stage for impressive construction opportunities, including improved demand, low construction costs and greater sources of capital. As such, the 2011 apartment development market should be a welcoming change from 2010. However, the volume of new deliveries will still be severely hampered from peak levels, even though most developers are somewhat optimistic on near-term prospects. This is due to the continued unemployment figures and overall economic uncertainty. Couple this with the fact that commencing any new development requires substantial due diligence, adequate financing and local approvals, builders are motivated to use 2011 to get a jump-start on zoning and planning stages. These sites will then be shovel-ready when the market returns to historical averages around 2012 and beyond. Indicators suggest a rebound to be in full swing by 2013, at which point project starts will see substantial movement.

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Development activity in 2010 was dominated by government-funded apartment projects, while companies seeking traditionally financed opportunities were kept on the sidelines by stringent capital requirements, resulting in anemic deliveries. However, change is on the horizon as the market continues to thaw at a glacial pace and existing land inventory held by developers in locations where current asset trade prices are close to or already outpace replacement costs sparks new product activity. **Equity Residential** already gets busy and acquires six land partners thus far in 2010 and expects to be able to begin construction on most of these sites in 2011, representing nearly \$340M of starts. The parcels are located in Arlington, Va., Berkeley, Calif., Alexandria, Va., Miami and Seattle. The REIT also has some land sites that were acquired before the downturn that are under consideration for near-term ground breaking.

From an industry perspective, look for most of 2011 development activity to be in core markets and in burgeoning segments such as student and senior housing. Trends point toward more urban-situated locations near employment and recreational hubs with a higher demand for smaller units. Amenity-rich environments situated in proximity to mass transit will also continue to dominate blueprints and are likely to gain substantial popularity during the next development wave. While initial delivery volumes will be narrow, the general consensus is the development market is poised for a very robust recovery, primarily as a result of insipid 2009 and 2010 delivery pipelines. However, as supply and demand ratios level off in select markets and development ramps up, construction costs will increase. This could set the stage for another development slowdown, especially if the dearth in construction financing lingers.

James Pyle, president and CEO for **LandSouth Construction** maintains the 2011 construction market will be driven by demand for new product and the loosening financial market. He feels the apartment segment will be one of the first sectors to come back, and he is taking proactive steps in preparing LandSouth's operations to deal with the new layout of the industry, such as uncertain price changes, new subcontractors/suppliers, very competitive bidding and new and smaller clients.

LandSouth kept busy in 2010, completing more than 750 rental units in two projects. The year saw no new starts, however it did break ground on a community center for an existing development. The developer has two active projects that should start in Q1 2011. It continues to work on about eight other potential prospects and hopes to start at least two of these by the third quarter. LandSouth's typical apartment project is a Class A, medium-density, garden-style layout in secondary markets. Its 2010 apartment development volume comprises 100% HUD d (4) 221 projects, which are privately funded but federally insured. Next year should be approximately 50% HUD and 50% conventional. Pyle aims to build a mix of student housing, military and market-rate apartments.

LandSouth's business is currently 100% new development, however it is looking at some rehab properties. Its territory spans the Southeast, but LandSouth is willing to travel further for existing clients. The company has not changed its strategy in light of the market and continues to look for any type of multifamily product which is well diversified by market rate, low-med-high density projects, student housing, military housing, senior living and townhomes.

The **McShane Companies** has always maintained a well-balanced portfolio of industrial, office, healthcare and multifamily development projects. It has 41 projects under construction throughout the United States, of which 17% are apartment communities. This is up slightly from recent years when multifamily represented approximately 10% to 12% of new developments. McShane Companies operates several affiliates to drive its business.

Look for **McShane Development** to move dirt on one, if not two, new apartment projects in 2011, situated in one of its target markets within the Sunbelt or West Coast regions. It also continues to monitor additional geographical target markets likely to experience population growth, job expansion and commercial development including Phoenix, Denver and Las Vegas. McShane traditionally develops institutional-quality properties that showcase luxury features at realistic rental rates allowing the company to enjoy a high occupancy rate shortly after project completion. The company has a national scope and focuses its activity in markets with strong demand drivers and in areas where it can draw upon its local personnel and specific market expertise. Looking forward, expect the developer to continue to monitor and prepare development strategies to meet market demand.

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DEVELOPERS OUTLINE BLUEPRINTS ...

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McShane Development has a shovel-ready site located in Dallas that CEO **James A. McShane** anticipates starting in 2011. The market fundamentals support this luxury, market-rate apartment complex, but at this time the capital markets still prefer to chase acquisitions of stabilized projects rather than to fund new ground-up development. The company also recently completed the new development of two large multifamily communities in Round Rock and Austin, Texas. **City North at Sunrise Ranch** located in Round Rock offers 384 units, while the 276-unit luxury residence **Estancia** in Austin features apartments from 600 s.f. to 1,300 s.f. Traditionally, McShane Development's projects, including those being contemplated for 2011, have been 100% conventionally financed. It did not launch any new developments in 2010.

Meanwhile, **McShane Construction Company** has been actively initiating numerous new construction projects primarily on behalf of both affordable housing and market-rate developers. This includes the 120-unit **Springs at Jordan Creek** in West Des Moines, Iowa, and **Phillips Swift Creek** in Cary, N.C., that has 196 units.

Crescent Resources has 11 projects in its 2011 pipeline. Like many of its counterparts, its 2010 development activity was slow, and the company spent its time focused on stabilizing the existing four communities and pursuing a 2011 pipeline. Changes to the company's strategy include adding environmentally friendly student housing to its portfolio, and it is currently tracking two student housing developments. Crescent's typical apartment development follows its Circle concept, which was inspired through extensive review and analysis of current industry trends and marketplace needs.

In the fourth quarter of 2010, president of Crescent's multifamily development group **Todd Farrell** has seen a significant amount of market improvement and recently started construction on a 428-unit apartment community in Franklin, Tenn. The project was financed as a presale to **Mid-America Apartment Communities Inc.** Plans call for a mix of ones, twos and threes in a series of three-story buildings. Look for the first apartments and clubhouse to be complete in July 2011. Anticipate the entire community to wrap up by the end of the Q1 2012.

Crescent's pipeline is more than 3,000 units spanning from San Antonio to Washington, D.C. In October it contracted to purchase six acres adjacent to the historic Erwin Mill building in Durham, N.C., and has filed for rezoning to create an apartment community. Farrell plans for approximately 300 units in a four-story building. Historical Concepts is the design architect.

NORMALIZING CAPS COULD SPUR REO/DISTRESSED SALES

The amount of distressed/REO assets that came to the market in 2010 was much less than the tidal wave that was originally expected. This is especially true for CMBS properties that have not flooded the market at predicted levels. In many cases, owners were scared to sell because of skyrocketing caps and either renegotiated the loan terms, asked for an extension or recapitalized the property. Also, increases in operating incomes and improving fundamentals prompted receivers and special servicers to hold onto properties until caps got back to normal. But caps are suppressing, and sellers are now breakeven or make a profit over existing debt, which was not the case a year ago. Overall the process is taking longer than expected, but some private buyers will pick up some properties before year's end.

Expect a lot of servicers and receivers to see a second window of opportunity over the next year or two to dispose of assets. The first wave of distressed was the Class A trophy properties that were earmarked as condos back in the boom. But now, caps on B and C properties have gone down 50 to 100 basis points year-over-year, so we are starting to see a second wave that will most likely be more of this product. Also, keep an eye out for a cluster of 11,000- to 12,000-unit portfolios coming to the market where the original borrower used short-term debt back in 2006 and 2007 that has now matured. Buyers will be value-added purchasers or groups with private money, high net worth individuals or institutional partners that are well capitalized. They will come in and execute improvements on the real estate, especially on properties with reasonable caps, and improve the cash flow. REITs will most likely stay away from the smaller asset deals

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Bozzuto Group 7850 Walker Drive Suite 400 Greenbelt, MD 20770	(301) 220-0100 Julie Smith President of Management jsmith@bozzuto.com	Manager of over 3,000 units throughout the Mid-Atlantic and Northeast with a goal to grow 10% a year in the existing markets.
Crescent Resources 227 W. Trade St. Suite 1000 Charlotte, NC 28202	(980) 321-6000 Todd Farrell President of Multifamily Development Group	Real estate development and land management company with interests in the Southeast and Southwest. It builds mixed-use, single-family, apartments, condominiums, office, business and industrial parks and retail.
Equity Residential 2 N. Riverside Plaza Chicago, IL 60606	(312) 474-1300 David Neithercut President/CEO dneithercut@eqrworld.com	REIT focused on acquisition, development and management of quality properties in top U.S. markets. Owns or invested in more than 490 properties in 23 states.
Eugene Burger Management Corp. 6 Venture Suite 210 Irvine, CA 92618	(949) 341-9033 Jay Kacirk SVP jaykacirk@ebmc.com	Currently manages 4,000 affordable apartments with plans to expand its property management services in California and Nevada.
Greystar Real Estate Partners 4030 Boy Scout Blvd. Suite 800 Tampa, FL 33607	(818) 887-4200 Andrew Livingstone Executive Director alivings@greystar.com	Company that does apartment management, development and investment nationwide. Currently manages 175,000 units. Acquisitions of smaller management companies could be on the horizon.
HSBC Bank 425 Fifth Ave. 24 th Floor New York, NY 10018	(212) 525-1125 Fax: (212) 525-1151 Neil Brazil Media	Does construction and floating rate lending on major property types and hospitality including office.
LandSouth Construction 1680 The Greens Way Jacksonville Beach, FL 32250	(904) 273-6004 James Pyle President/CEO kimjohnston@landsouth.com	Southeast contractor that builds apartments, hotels, senior housing, student housing, military housing, condominiums and townhomes. The company has completed more than 6,000 units.
Marcus & Millichap 2398 E. Camelback Road Suite 550 Phoenix, AZ 85016	(602) 687-6763 Cliff David National Multi Housing Group cliff.david@marcusmillihcap.com	(The Crossroads deal) Firm that specializes in commercial real estate investment services nationwide.
McShane Companies 9550 W. Higgins Road Suite 200 Rosemont, IL 60018	(847) 292-4300 Jim McShane CEO j.mcshane@mcshane.com	Operates four affiliate companies, including McShane Development Company that develops, repositions, acquires, constructs, consults and manages multifamily, healthcare, office, industrial and mixed-use properties.
Mid-America Apartment Communities 6584 Poplar Ave. Memphis, TN 38138	(901) 682-6600 Eric Bolton CEO investor.relations@maac.net	Apartment REIT with a 42,252-unit portfolio that stretches across the Southeast and South Central U.S. markets.
Pinnacle Family of Companies 5910 N. Central Expressway Suite 1145 Dallas, TX 75206	(214) 891-7845 Ed Wolff Chief Administrative Officer ewolff@pinnaclefamily.com	One of the largest apartment managers with approximately 183,000 units nationwide. Around 65,000 of those are owned.
Riverstone Residential Group 1201 Elm St. Suite 1600 Dallas, TX 75270	(214) 965-6008 Terry Danner President tdanner@riverstoneres.com	Management company that is 100% third party and will end the year with 125 properties and just under 29,000 units.
Sperry Van Ness 112 S. Sangamon St. Second Floor Chicago, IL 60607	(312) 676-1873 Jeffrey Baasch Senior Investment Advisor jbaasch@svn112.com	(The Sheridan Terrace deal) One of the largest and fastest growing commercial real estate brokerage firms in the U.S.
Transwestern 6700 Rockledge Drive Suite 400A Bethesda, MD 20817	(301) 571-0900 Dean Stigmon SVP/Director dean.stigmon@transwestern.com	One of the largest privately held real estate firms in the country. Active in real estate services, development and investment management business.

NORMALIZING CAPS COULD SPUR REO/DISTRESSED SALES ...

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Looking ahead, distressed and REO sales will be pushed by caps that have compressed on C and B apartments, and capital will be plentiful on these deals because the ROI is more compelling than other property types, values have escalated and there is improving NOI. Tertiary markets, especially in the South, are expected to bring a lot of distressed product to the table in 2011. South Florida, Phoenix, Las Vegas and Southern California should also be active. But we will not see the top of the crest on loan maturities until 2013, which should bring another wave.

HSBC Bank unloads the 148-unit **The Crossroads** in Tempe, Ariz., for \$4.8M (\$32K/unit). The private buyer owns adjacent buildings and plans to hold the property long term. This is a class C asset in an A/B location right near Arizona State University. Average unit size at the circa-1963 property is 717 s.f. and occupancy was 97% at the time of purchase. The cap is 7.73% based on broker pro forma. The buyer used a \$3.6M first loan and a \$1.125M second, plus some rehab money on the sale through UNIFI Companies, which is also a joint venture partner.

Miami-based **DREA Group** acquires 179 apartment units of the 300-unit **San Michele** condo community in West Palm Beach, Fla., for \$11.15M (\$62K/unit), which is way below replacement costs. The seller was a trustee in a 363 bankruptcy sale. There were five private bidders on the Class B property, which was built in 1999. Average unit size is 1,071 s.f. Occupancy was 85% at the time of purchase and this was an all-cash transaction. Look for DREA to be active in buying distressed properties next year.

Newport Landing I and II was purchased by a private investor in Oxnard, Calif., for \$19M (\$111K/unit). The class C+/C property was sold by a large institutional lender that also provided bridge financing for the sale. Newport Landing has 170 units in two buildings and was built in 1965 and 1970. There were 17 offers on this asset mostly because there are not many distressed opportunities in the market. The cap was 5.5% based on current numbers. Occupancy was just under 82% at time of the sale. Count on the buyer to refinance and do renovations to the property.

A private investment groups picks up the 18-unit **The Sheridan Terrace** in Evanston, Ill., for \$2.86M (\$160K/unit) from the bank in an all-cash transaction. The cap is 7.5% based on in-place rents. The circa- 1960s class A-/B+ property is in very good shape, which attracted a lot of bidders. The former owner originally planned a condo conversion for the asset. Occupancy was 94.5% and average unit size in 1,000 s.f. Anticipate the buyer to hold the property long term and acquire more properties like this in the next 12 to 18 months.

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