ApartmentResearch
MARKET REPORT
Marcus & Millichap

Orlando Metro Area *Second Quarter 2014*

Demand Remains High as New Apartments Arrive

The Orlando economy is expanding at the most vigorous pace in years, although new rental demand will likely not fill enough of the new apartments coming online to avert an increase in the vacancy rate. Rental completions will reach one of the highest levels in several years during 2014, resetting inventory nearly all of the way back to the former peak before the conversion boom. While an increase in the vacancy rate this year appears unavoidable, bright prospects for further demand growth will shorten the duration of rises in the vacancy rate related to spurts in supply. Many households have recent foreclosures in their credit histories, precluding a near-term re-entry into homeownership. Also, single-family homes have become less affordable. Following a gain in the first quarter this year, the median price of an existing single-family residence is nearly 38 percent higher than three years ago when the median price bottomed. Wages and salaries, though, have grown by substantially less over the same stretch.

Despite the upswing in development, fluid capital markets are maintaining a highly favorable investment climate in Orlando. Investor demand remains keen, with well-priced assets typically generating multiple offers when brought to market. As equity continues to vie for deals, debt providers are also active, competing on terms and proceeds to finance apartment transactions. The low cost of capital offers a wide spread to Class B-minus and Class C cap rates, which sit at around 8 percent. In addition, higher leverage is enabling many property owners to sell and trade up to newer properties. For investors with long-term hold strategies, the window remains open to finance assets with low-cost 10-year loans. Buyers are expanding their search for properties across the entire metro, but areas such as downtown and the growing Lake Nona medical hub garner unwavering interest. In addition, the SunRail commuter rail, which recently opened, may have long-term effects on commuting patterns and neighborhood preferences that will open new areas for multifamily development and investment.

2014 Annual Apartment Forecast

3.4% increase in total employment

Employment: Led by job creation in the expanding private sector, employers in the metro will add 36,300 jobs in 2014, marking a 3.4 percent increase in payrolls. In 2013, 35,800 new hires were made.

6,500 units will be completed

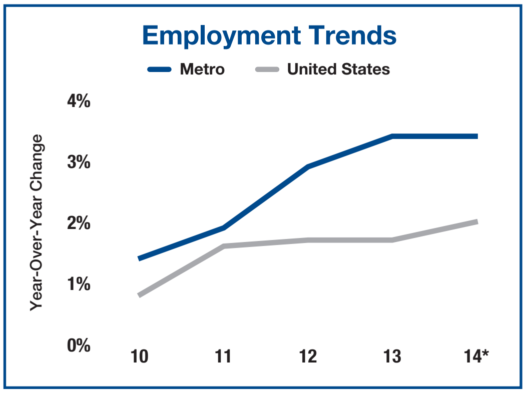
Construction: Multifamily building continues to ramp up. Developers will complete 6,500 units in 2014, expanding rental stock a hefty 4.1 percent. Nearly 3,300 rentals were brought online last year.

100 basis point increase in vacancy

Vacancy: Completions will overwhelm a sizable increase in demand during 2014, raising vacancy 100 basis points to 6 percent. The vacancy rate decreased 40 basis points in 2013 on far fewer completions and net absorption of 3,700 units.

3.4% increase in effective rents

Rents: The average rent in the metro will advance 3.4 percent this year, to $945 per month, the fifth consecutive annual increase. A gain of 2.4 percent was recorded in 2013.



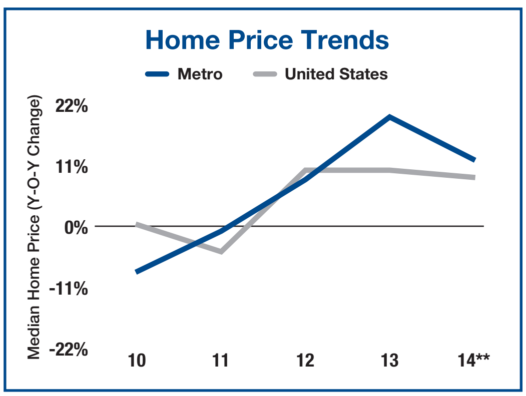
Economy

- Payrolls in the metro swelled 3.6 percent during the past year through the creation of 37,800 jobs. Positions were added in each month during the period to surpass the pre-recession peak in employment.

- The private sector added 37,400 positions over the past year, including 9,900 new hires in the first three months of 2014. Professional and business services staffing grew by 10,100 workers over the past 12 months, and a resumption of residential building contributed to a gain of 4,200 construction jobs. Leisure and hospitality, which encompasses bars, restaurants, hotels and tourist attractions, added 9,000 employees.

- Financial-services employers added 1,000 jobs during the past 12 months despite a loss of positions in the first quarter this year. The recovery in the single-family housing market has not appreciably affected hiring in housing-related finance fields.

- **Outlook:** Local staffing levels will expand in 2014 with the addition of 36,300 workers.



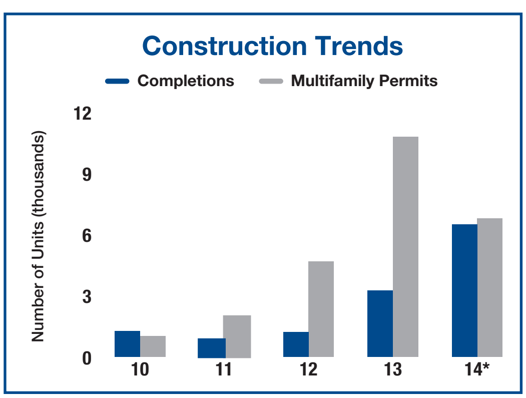
Housing and Demographics

- The median price of an existing single-family home rose 12 percent during the past 12 months to $169,300 behind an 8 percent jump in the number of units sold. The monthly payment on the median-priced home is $1,076 per month, which exceeds the average metrowide rent.

- Housing stock is growing. More than 13,000 units of single-family and multifamily housing were completed during the past four quarters, nearly 60 percent more than the total in the previous year.

- Demand for housing is increasing. The combination of a high quality of life and more abundant employment opportunities supported net migration of more than 9,000 new residents to the metro over the past year.

- **Outlook:** Housing demand will continue to grow as employers expand, and many new households will prefer the mobility offered by multifamily rentals.



*Forecast
** Trailing 12-month period through 1Q

Construction

- Rental stock expanded 2.3 percent, or by more than 3,700 units, over the past 12 months. In the first quarter alone, nearly 1,800 rentals were brought online.

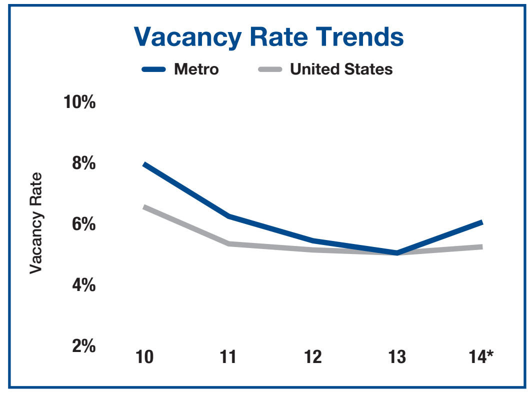
- All of the units completed in the first quarter were market rate. The Colonial Grand at Randal Lakes, with 462 rentals, was the largest project placed in service during the period. Three complexes with an aggregate 824 apartments expanded inventory in the Ocoee/Winter Garden/Clermont submarket a considerable 11 percent in the first quarter.

- An additional 6,600 units are underway in the metro, with completion dates extending into 2015. In Downtown Orlando, the 1,245 rentals under construction will expand rental inventory 18 percent, while a 10 percent impact on stock will occur in Sanford/Lake Mary.

- **Outlook:** Developers will complete 6,500 units this year, leaving apartment inventory less than 1,000 units from regaining the former peak 10 years ago, before the conversion boom.

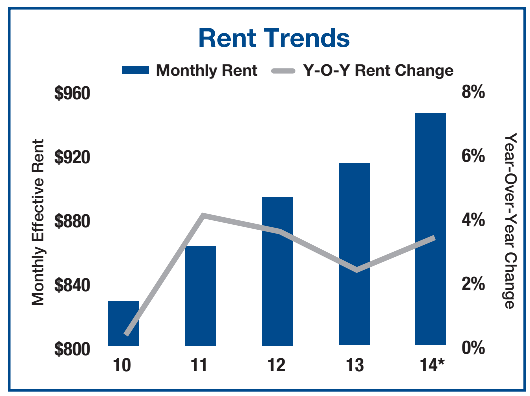
Vacancy

- During the January-to-March span, metrowide vacancy ticked up 10 basis points to 5.1 percent. Since the first quarter of last year, however, the vacancy rate has fallen 10 basis points.
- Vacancy in suburban submarkets was 4.5 percent in the first quarter, marking an increase of 10 basis points from year-end 2013 but a drop of 90 basis points since one year ago. More than 3,400 additional rentals were occupied in the suburbs over the past 12 months, including an additional 600 units in the South Orange County submarket, an expanse encompassing the airport and the Lake Nona region.
- Significant completions in the Ocoee/Winter Garden/Clermont submarket contributed to a 180 basis-point jump in vacancy in the first quarter to 5.3 percent despite net absorption of more than 600 units. The vacancy rate in units built since 2000 rose to 6.5 percent during the period, up from 3.7 percent at year end.
- **Outlook:** Substantial completions will underpin a 100 basis-point rise in vacancy this year to 6 percent.



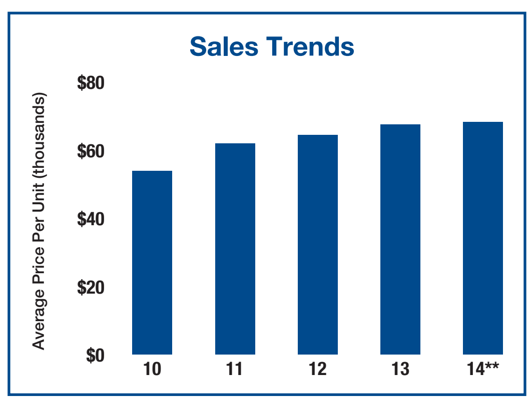
Rents

- The average rent in the metro advanced 0.8 percent in this year's opening quarter to $921 per month. On a year-over-year basis, the average rent increased 2.4 percent, marking a moderation in growth from the 3.1 percent gain in the preceding 12 months.
- At complexes built since 2000, the average rent was $1,060 per month, which breaks down to less than $1 per square foot. Measured year over year, the average monthly rent at recent vintage properties increased 1.4 percent, primarily reflecting a large jump in the first quarter.
- Concessions equal 5.7 percent of the average rent, or roughly three weeks of free rent. Leasing incentives have declined since the first quarter last year and since hitting 13.4 percent of average rent in the first quarter 2010.
- **Outlook:** Influenced by the delivery of several thousand high-end units, the average rent in the metro will rise 3.4 percent this year to $945 per month.



Sales Trends**

- Competitive sources of acquisition debt and intense investor appetites ignited a 10 percent rise in transaction velocity over the past year.
- Dollar volume also rose 19 percent, reflecting additional sales of properties priced at more than $10 million. The share of properties selling for less than $10 million, meanwhile, slipped over the past year as small investors took advantage of favorable lending terms to purchase larger assets.
- The average price of properties sold increased marginally to $68,200 per unit over the past 12 months. Sales of larger assets kept the average cap rate in the mid- to high-6 percent range, but Class B and Class C assets transacted roughly 100 basis points higher.
- **Outlook:** The growing local economy will buoy investors' outlooks and sustain an elevated level of deals in the months ahead.



*Forecast
**Trailing 12-month period
Sources: CoStar Group, Inc.; Real Capital Analytics

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Capital Markets

By WILLIAM E. HUGHES, Senior Vice President, Marcus & Millichap Capital Corporation

- The U.S. economy is tracking a solid recovery that is supporting a robust multifamily sector. Assessing positive developments in the labor and housing markets, and the resiliency of the U.S. consumer, the Federal Reserve recently voted to reduce its monthly bond purchases by an additional $10 billion. The yield on the 10-year U.S. Treasury has remained in the mid-2 percent range throughout the second quarter.
- Nationwide apartment vacancy was flat in the first quarter at 5 percent as demand growth virtually offset the completion of more than 45,000 apartments. Completions are on track to reach 215,000 rentals in 2014, the highest yearly total in several years. For the entire year, U.S. vacancy will rise 20 basis points to 5.2 percent, while the average rent will advance 2.6 percent.
- Fannie Mae and Freddie Mac are underwriting terms of five, seven and 10 years and offer maximum leverage of 80 percent. Interest rates currently range from about 3.5 percent at the low end of a short maturity loan to 4.5 percent for 10-year debt on loans of more than $3 million. For loans greater than $15 million, interest rates are 12 to 15 basis points less across the maturities, and for financing of less than $3 million, interest rates rise from 20 basis points to 30 basis points.
- Conduits are more active and are considering a wide range of markets and asset quality. CMBS loans are generally written at rates varying from 4.5 percent to 5 percent and leverage up to 75 percent and, in limited instances, 80 percent. Other active sources of apartment lending include commercial banks and life-insurance companies, and specialty providers of bridge and mezzanine financing.

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Submarket Vacancy Ranking

Rank	Submarket	Vacancy Rate	Y-O-Y Basis Point Change	Effective Rent	Y-O-Y % Change
1	South Orange County	3.5%	-70	$1,020	1.2%
2	Casselberry/Winter Springs/Oviedo	3.9%	-30	$925	3.4%
3	Kissimmee/Osceola County	3.9%	-110	$827	1.8%
4	Altamonte Springs/Apopka	4.5%	-80	$872	3.2%
5	University/East Orange County	4.9%	0	$1,161	-1.3%
6	East Orlando	5.2%	140	$814	1.6%
7	Ocoee/Winter Garden/Clermont	5.3%	-170	$915	0.5%
8	Southwest Orlando	5.5%	70	$834	5.7%
9	Winter Park/Maitland	5.6%	200	$884	3.0%
10	North Lake County	5.9%	-220	$744	-6.9%
11	Northwest Orlando	6.2%	-140	$785	3.2%
12	Sanford/Lake Mary	6.2%	-50	$899	5.0%
13	West Orlando	6.2%	30	$905	3.0%
14	Downtown/North Central Orlando	6.3%	250	$1,450	5.0%