2011 Indiana Apartment Market Overview

Multifamily Investment

Tikjian Associates
Multihousing Investment Advisors
Multifamily Real Estate - Shining in a Year of Uncertainty

Slowing job growth in the third quarter and continuing concern over European and US debt have caused economic pessimists to worry about a “double dip” recession - and even optimists generally predict no change until after the election year of 2012. In the midst of this economic uncertainty, multifamily real estate has been a shining star.

Major Issues - 2011

Continuing Concern About Commercial Real Estate Defaults

Since 2009, the specter of massive commercial real estate defaults has been a drag on real estate values and the economy in general. In 2010, 17.3% of all commercial property sales were distressed assets (up from 10.5% of total sales in 2009). And the volume of delinquencies continues to rise. Most loan foreclosures have been of the CMBS variety. Trepp reports that 9.6% of all CMBS loans are now delinquent nationally and 9.0% are “seriously delinquent” (over 60 days or in foreclosure). Multifamily loans have the highest delinquency percentage as a property class at 17.0%. In Indiana, 6.9% of CMBS multifamily loans are in default and in Indianapolis the percentage is 13.8%. To date there has been no avalanche of foreclosures, but rather a steady stream which the market has been able to absorb in a somewhat orderly manner. Through October of 2011, properties totaling 2,800 apartment units have passed through foreclosure in Indianapolis. It should be noted that lenders have increased the use of note sales to clear their backlog of nonperforming loans (particularly loans on smaller properties or in secondary markets), even though note sales have generally produced a lower percentage of debt recovery than sales of the real estate.

Strong Apartment Fundamentals – The Changing “American Dream”?

Per MPF Research, average apartment occupancy nationally climbed to 94.8% in the third quarter of 2011, up from 93.8% a year ago and 91.8% at the market’s low point in late 2009. Effective rents also climbed a full 1.6% in the third quarter and are now up 4.3% from one year ago.

This impressive recovery has been driven by strong and growing demand in spite of a struggling economy and no sustained job growth (historically a key to a strong apartment market). What we are witnessing is the beginning of a new age in the balance between home ownership and apartment rentals, the result of two powerful and long term forces: changing demographics and changing living preferences.

Changing Demographics - Three major demographic groups are boosting demand for rental housing. First, an estimated 80 million “Echo Boomers” (children of Baby Boomers) are coming of age and beginning to establish their own households. Traditionally, over 65% of householders under the age of thirty are renters. If tradition holds, the impact of this group on rental housing could be huge. Secondly, aging Baby Boomers (over 70 million in number and the second largest population group behind the Echo Boomers) are becoming empty nesters and approaching retirement. Undoubtedly many of this age group will choose to downsize to lower maintenance apartment living. Finally, America’s Hispanic population is growing incredibly rapidly. Between 2000 and 2010 Hispanics accounted for over half of the total population increase in America. Almost half of Hispanic householders have historically rented compared with just 31% of the total population.

Changing Lifestyle Preferences - Between 1965 and 2005, home ownership – The American Dream grew steadily. At its peak in 2005, 69% of American households owned their home. Since 2005, however, home ownership has fallen for 6 consecutive years (to 66% in 2011). Indiana mirrors the nation with a declining homeownership trend (69% in 2011 compared to 71% in 2000). In addition to the demographic factors discussed above, more people are now choosing to rent rather than buy. Reasons for this change in preference include (a) fear that home values will fall further as more foreclosed homes hit the market (b) uncertainty in their own financial future (c) tightened credit standards making home buying more difficult and (d) the desire for flexibility, mobility and freedom from the maintenance demands of home ownership.

Slow but Continued Improvement in Credit Markets

With interest rates at historic lows, the primary challenge to buyers and developers is not the cost, but rather the availability, of financing (although credit markets continued to improve in 2011). CMBS has not yet returned as an option for most borrowers. Insurance companies are becoming more active but at lower loan-to-values than Fannie Mae and Freddie Mac. Fannie and Freddie have both exceeded their 2011 lending goals nationwide and done several deals in Indiana, but generally have not been overly aggressive here. HUD continues to be backed up due to the volume of loans it is currently processing, making it better suited for refinancing and less preferred as a source for acquisition financing.

Looking Forward - We see the following in 2012: (1) Strong rental demand will continue although in Indianapolis the demand will barely keep pace with new development, meaning overall occupancy will remain relatively flat; (2) With the Fed’s promise to keep rates down until 2013, and implementation of the “Twist” stimulus measure (buying longer-term US debt), interest rates will remain low, at similar levels to today, with credit availability improving only slightly; (3) the number of distressed assets hitting the market will continue, but still no flood.
Economic Overview

Indiana continues to be the envy of much of the country for its diversified and stable economy. Although job growth slows slightly in the summer of 2011, a flurry of new job announcements were issued in the early fall, primarily by smaller businesses and in a variety of different industries. The state offers a decidedly pro-business environment and exceptional resources, including a very real public-private working relationship between business and the state’s respected universities, i.e. Purdue, Indiana and Ball State. As evidence of the state’s resolve to attract new business, legislation passed in May to actually cut corporate taxes. Success is reflected in recent rankings:

- Since January 2010 Indiana has accounted for 10% of the nation’s private sector job growth
- Indiana ranks 1st in the US in per capita income from foreign owned business
- Indiana ranks 1st in the US in per capita employment in manufacturing
- Indiana ranks 3rd in the US in per capita employment in life sciences
- Indiana ranks 9th in the US in per capita employment in logistics
- Indiana was named the best place in the Midwest to do business and 6th best nationally in a recent survey of 500 CEO’s conducted by Chief Executive magazine.

The state appears poised to be a national leader in capturing repatriated global manufacturing jobs as a result of our comparative low cost structure and pro-business policies. Most economic observers expect Indiana’s economy to continue to significantly outperform other Midwestern states and lead much of the nation in future business growth as the economy improves.

Indianapolis continues to be the engine of much of the state’s economic growth. Unemployment in the city decreased in 2011 and much of the recent positive job and economic news in the state is coming from Indianapolis and central Indiana. The Indianapolis metro area has become a national leader in a number of important industries, most prominently health care and life sciences, logistics, information technology, motorsports, and advanced manufacturing. As commercial development remains at a near standstill in many other cities, it is vibrant in central Indiana. Notable projects completed in the last twelve months include a major convention center expansion, the 1,005-room JW Marriott hotel (largest of its brand in the US), and the Carmel Center for the Performing Arts (the crown jewel of Carmel’s $300M City Center development), to name just a few. In addition, CityWay, an ambitious $155M mixed use development near the Eli Lilly headquarters on downtown’s near south side has recently broken ground and is just one of the numerous revitalization projects now underway as Indianapolis prepares to host the Super Bowl in February, 2012.

Due to their relative fiscal health the city and state have become national standouts, attracting the interest of investors of all stripes.

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Apartment occupancy in the Indianapolis Metro area improved for the second consecutive year, climbing to 91.4% in 2010 from 90.8% in 2010. Downtown leads all submarkets at 94.4%, up significantly from 91.6% a year ago. Only the west submarket saw an occupancy decline, dropping to 89.5% from 90.0% last year. Class A properties experienced a significant gain in occupancy in 2011, growing from 93.2% to 95%. Occupancies for Class B and C properties were nearly unchanged, with Class B occupancy gaining 0.1% and Class C properties losing 0.1%. The gap between Class A and Class C occupancies increased to almost 9% in 2011, the widest margin in several years.

After declining slightly (by 0.4%) in 2010, overall metro rents increased by an average of $18 per month or 1.3% (on a gross basis prior to concessions). This growth was experienced in all submarkets and among all property classes. Downtown, continuing to benefit from strong student and young adult demand, experienced the highest growth at 2.2%. Gross rents downtown climbed to $855 per month, over $100 per month above the North Submarket which ranked second in both gross rents and rent growth. Class A properties saw the highest rent growth in the city with a 1.5% increase over last year. It should be noted that one reason for the smaller increase in average rent within Class B properties is that our survey classifies all new Section 42 tax credit properties.

Although most new development (other than tax credit) is occurring in Class A properties, rents continue to grow in spite of the increased supply. In 2011 rents exceeded the $90 per sq. ft. average for the first time. The newest downtown Class A properties are commanding rents between $1.30 and $1.50 per sq. ft.
In spite of economic uncertainty and continuing weak job growth, occupancy increased in 2011. The market absorbed an additional 2,900 units in the trailing 12 months. Increasing occupancy was due to strong demand and only a small increase in rental inventory through new development.

The strength of Class A properties provides evidence that more individuals and families are choosing to rent and are willing to pay for higher end finishes and amenities.

This chart shows the number of new apartment units completed in a given year as a percentage of the overall inventory. The total market vacancy rate is also shown to contrast unit additions against the overall market vacancy.

Same Store Rent Growth is the rent growth of properties that have been in existence during an entire respective survey period. Properties built during a respective study period are not included.
All major cities surveyed attained occupancies above 90% in 2011. Columbus, driven by strong performance and hiring by Cummins, showed the strongest occupancy at 96.5% followed closely by Bloomington at 95.5%. Bloomington was also the leader in both gross rents ($856 per month) and rent growth (5.3%), reflecting the strong Indiana University student housing market.
Indiana is poised to be a national leader in capturing repatriated manufacturing jobs as a result of our comparatively low cost structure, highly skilled manufacturing workforce, low tax rates, strong fiscal position and pro-business policies.
Multifamily completions are down significantly in 2011, with completion of 1,752 units estimated to hit the market, 30% below the number of new units completed in 2010. The decline in new units is clearly attributable to the severely constrained credit markets which prevented commencement of construction for most projects in 2009. However, it appears that the trend will completely reverse in 2012 when developers plan to complete over 3,400 new units. If all units are actually finished, it will represent the largest number (by far) of new units hitting the market in any single year in this millennium. This surge in development is further evidence of the optimism for continued strong rental fundamentals for multifamily.

The two charts below illustrate the percentage of multifamily building permits (by units) relative to the total residential building permits. Even though single family permits have fallen in the trailing 12 months, permits for new apartment units were also down in this period. Apartment units permitted were approximately 20% of total residential units permitted in 2011, down from 23% in 2010.

Source: US Census Bureau Residential Construction Branch

New construction of single family homes in the Indianapolis metro area also remained very slow, with total permits dropping to just 3,840 units in the trailing 12 months, just above the permits issued in 2009 during the recession. Between 1999 and 2005 single family permits averaged in excess of 14,000 units each year.
## 2011 Indianapolis Apartment Development

### 2010 Starts

<table>
<thead>
<tr>
<th>Market Rate</th>
<th>Units</th>
</tr>
</thead>
<tbody>
<tr>
<td>1201 Indiana Ave - TrinItas Ventures</td>
<td>253</td>
</tr>
<tr>
<td>The blvd at Anson II - Flaherty &amp; Collins</td>
<td>213</td>
</tr>
<tr>
<td>Sophia Square - Keystone Construction</td>
<td>202</td>
</tr>
<tr>
<td>Waverley II - JC Hart</td>
<td>48</td>
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<tr>
<td>Di Rimini</td>
<td>30</td>
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### Tax-Credit

| 16 Park - Insight Development | 155   |
| Trotters Pointe III - Pedcor   | 96    |
| Meredith Meadows - NRP Group   | 84    |
| Preston Pointe - Herman & Kittie | 76    |
| Clary Crossing Senior Villas - RealAmerica | 72    |
| National Apts on the Monon - Development Concepts | 62    |
| 707 North - Whitsett Group     | 40    |
| Stonehurst Pointe - Milestone Ventures | 37    |

| 2010 Totals                   | 1,368 |

### 2011 Starts

<table>
<thead>
<tr>
<th>Market Rate</th>
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<tbody>
<tr>
<td>CityWay - Buckingham</td>
<td>320</td>
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<tr>
<td>The Fort Apartments - JC Hart</td>
<td>224</td>
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<tr>
<td>Domain at Bennett Farms - REI</td>
<td>219</td>
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<tr>
<td>Canyon Club - Sheehan</td>
<td>206</td>
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<tr>
<td>One One Six at College - JC Hart</td>
<td>191</td>
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<tr>
<td>The Avenue - Buckingham</td>
<td>142</td>
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<tr>
<td>Aspen Lakes II - Hunt Pacific</td>
<td>135</td>
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<tr>
<td>Residences at Keystone Crossing - Flaherty &amp; Collins</td>
<td>129</td>
</tr>
<tr>
<td>Harding Street Lofts - Core Redevelopment</td>
<td>124</td>
</tr>
<tr>
<td>Alexandra at Carmel - Edward Rose</td>
<td>76</td>
</tr>
<tr>
<td>The Hinge - Von Dewlen</td>
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| 2011 Totals                   | 3,193 |

### 2012 Starts

<table>
<thead>
<tr>
<th>Market Rate</th>
<th>Units</th>
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<tbody>
<tr>
<td>Penn Circle - Millhaus</td>
<td>192</td>
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<tr>
<td>Bella Vista - Edward Rose</td>
<td>180</td>
</tr>
<tr>
<td>Monon Place II - Buckingham</td>
<td>136</td>
</tr>
<tr>
<td>Stadium Lofts - Core Redevelopment</td>
<td>131</td>
</tr>
<tr>
<td>Cosmopolitan on the Canal II - Flaherty &amp; Collins</td>
<td>120</td>
</tr>
<tr>
<td>Linden Square II - JC Hart</td>
<td>71</td>
</tr>
<tr>
<td>Glendale Site - Glick</td>
<td>50</td>
</tr>
</tbody>
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### Tax-Credit

| Brownstone - Whitsett Group  | 95    |
| 1010 Central - Whitsett Group | 86    |

| 2012 Totals                   | 1,810 |
Sales Activity

Apartment sales nationally increased to an estimated $20.7 billion during the first half of 2011, more than doubling the sales volume for the same period in 2010 (but still well below the record $120 billion in sales closed in all of 2006).

After falling for four consecutive years, Indianapolis area sales have increased in 2011. Thirty-nine transactions totaling 5,700 units and approximately $250 million have closed in the first 10 months of 2011 (up from 4,400 units and $200 million in all of 2010). An additional ten transactions totaling 3,200 units are currently pending with a number of these sales scheduled to close before year-end. When these year-end closings are added to the existing volume, the increase over 2010 will be significant.

The increase in sales is due to an “alignment of stars” decidedly in favor of multifamily investment, including: (1) anticipated growing demand for rental housing for at least the next several years; (2) the view of multifamily as the “safest haven” in commercial real estate; (3) a lack of investment alternatives which can provide higher returns, more control and less volatility in today’s economic environment; (4) a lack of new inventory (although this dynamic is changing); (5) an improving, albeit slowly, credit market which offers more financing sources than other property types; (6) historically low interest rates; (7) an abundance of equity capital; and (8) a steady stream of available properties, both distressed and stabilized.

Virtually all property classes are popular with investors, from Class C (which are sought after due to “cheap” per unit pricing) to more easily financeable high-end Class A properties.

The strong demand has caused cap rates to compress in the last twelve months, particularly on sales of higher end properties. (Note - the increase in cap rates noted in the chart is due to the mix of properties sold in 2011, not due to higher required yields.) It should be noted that the cap rate a buyer may be willing to accept can vary based upon loan sizing – that is to say, a buyer can pay a higher price for an asset and still attain desired yields if the property can be highly leveraged at today’s low interest rates. As equity requirements increase for a prospective purchase, the cap rate will likely increase.

Because of increasing transaction volume and the attractiveness of multifamily investment (due to the aligning stars): (a) the 1031 exchange requirement is returning as a factor influencing prices; (b) buyers have been willing to buy distressed assets at prices based on “as stabilized” pro formas; and (c) acquisitions are being closed with cash, lines of credit or bridge loans in order to satisfy the desired time frames of sellers (with permanent financing placed after closing).

Cap rates increased in 2011 due more to the mix of properties that sold than to higher required yields. There were more Class B sales in 2011 than prior years. Forecast cap rates declined due in part to lower capital costs, therefore lower stabilized cap rates were acceptable to buyers.

Average price per unit declined due to the mix of properties that sold, more than a decline in prices.
SELECTED 2011 INDIANA APARTMENT SALES

Coppertree
Kushner/Apollo Property Mgmt
772 Units
Indianapolis

Scandia
Thiemann Real Estate
444 Units
Indianapolis

Keeneland Crest
Thiemann Real Estate
424 Units
Indianapolis

Knobs Pointe
Bluestone Management
384 Units
New Albany

Lighthouse Landings
Goldoller Real Estate Investments
336 Units
Indianapolis

Fishermans Village
White Eagle Property Group
328 Units
Indianapolis

Washington Quarters
Thiemann Real Estate
256 Units
Indianapolis

Thompson Village
Gene B Glick Company
240 Units
Indianapolis

Regency Park
White Oak Partners
226 Units
Fort Wayne

Waterstone Place
Zidan Management Group
192 Units
Indianapolis

Quail Run
McCann Realty Partners
166 Units
Zionsville

Maxwell
Gene B Glick Company
105 Units
Indianapolis

Please visit www.TAmultihousing.com for more information
Tikijian Associates is a boutique brokerage firm specializing exclusively in the sale of multihousing properties in Indiana and Kentucky.

The experience and accomplishments of its professionals are second to none among multihousing brokers in Indiana and include:

- Over 60 years of combined experience in the multihousing brokerage industry
- $1.8 Billion in multihousing sales
- 55,000 units sold throughout Indiana and Kentucky for clients including local, regional and national private equity investors; public pension funds; and public and private REITs

By narrowing our focus to this specific segment of the real estate industry, we offer: (1) In-depth knowledge of local markets, specific properties and investors and owners active in these markets; (2) credibility among sellers and prospective buyers based on experience; and (3) an unparalleled expertise in capital markets, financial underwriting and property operations.

We believe that there is no substitute for hard work in the valuation and marketing of a property. We perform our own extensive due diligence on all aspects of a property including: (1) location, (2) physical condition, (3) operations (current financial performance and marketing) and (4) existing financing. Based upon this advance due diligence, we provide owners with fair property valuations and strategic advice on value-enhancement to assure a successful closing.

ABOUT TIKIJIAN ASSOCIATES

Tikijian Associates was founded with the specific goal of offering the highest achievable level of client service in the evaluation, marketing and sale of multihousing properties. The Principles that guide us in this mission are simply stated: Focus and Work Ethic.

Our Associates

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