APARTMENT DEVELOPMENT RAMPS UP IN OMAHA, BUT ABSORPTION REMAINS STRONG

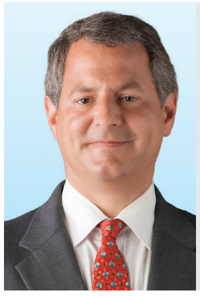

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Image courtesy of Alley Poyner Macchietto Architecture

NuStyle Development Corp. is converting the former Northwestern Bell regional headquarters building in downtown Omaha into a 300-unit apartment complex known as The Wire. The development, scheduled for completion in March 2015, is 12 stories tall plus a two-story sky deck with pool.

The strong performance of the Omaha apartment market is expected to continue in 2014 and beyond. According to MPF Research, Omaha's apartment occupancy stood at 95.8 percent in the third quarter of 2013, up from 95.5 percent at the end of 2012 and in line with Omaha's average occupancy rate of slightly under 96 percent since 2000.

On the new construction front, developers continue to bring new projects to the market. During the first 10 months of 2013, multifamily building permits totaled 1,454 units in metro Omaha, which was 47 percent above the 986 multifamily housing units permitted during the same period in 2012 and 19 percent above the 1,225 units permitted during all of 2012. The figure was also slightly above the upper end of my range of expectations of 1,300 to 1,400 units for all of 2013.

On a percentage basis, the addition of 1,454 units would increase the apartment housing stock by 1.6 percent based on an overall inventory of approximately 88,000 units.

More Shovels in the Ground

During 2014, I expect construction activity to continue to be strong. Indeed, we could see multifamily building permit issuance reach 1,300 to 1,400 units. Included in these new development numbers is the surging downtown/near downtown market, the focal point of multiple projects that have been announced.

One high-profile project is The Wire, NuStyle Development Corp.'s conversion of the former Northwestern Bell regional headquarters building, located at 100 S. 19th Street, into 300 apartment units. The developer expects to complete the project in March 2015.

Other developments include Bluestone Development's 154-unit Spaces Apartments under construction in Midtown; City Ventures' 125-unit planned complex at Ninth and Jones streets; and America First Real Estate Group's 100-unit Jones 13 Apartments near the Old Market District area. Darland Construction Co. expects to wrap up construction of Jones 13 at the end of August 2014, and several of the other projects are scheduled for completion during summer 2014.

There are also a number of local and regional developers that are actively seeking multifamily land. I expect construction to begin on several suburban complexes in 2014, including the planned 272-unit Grove Ridge development at 192nd and Leavenworth streets.

As was the case in 2013, I expect Omaha to continue to have the ability to absorb the new construction without significantly affecting the overall multifamily occupancy rate. According to the Greater Omaha Chamber, Omaha continues to outperform the national economy. The local unemployment rate registered 4.2 percent at the end of October compared with 7.3 percent nationally.

For the 12 months ending in October, Omaha's economy added approximately 4,500 net new jobs. On a percentage basis, the jobs increase was 1 percent during that time span, an indicator that Omaha is able to absorb additional apartments.

Healthy Rent Growth

On the rental rate front, we saw strong revenue gains in Omaha, with rents increasing by 5.7 percent so far in 2013, up $42 per unit to $777 per unit per month, according to MPF Research.

While most of the apartment owners I have spoken with confirm that 2013 has been a strong year for their portfolios in terms of occupancy and rent growth, they indicate that the true rent growth has been a bit less than the 5.7 percent noted above.

According to the Institute of Real Estate Management (IREM), average monthly rental rates on a per square foot basis were $1.03 for studios, 88 cents for one-bedroom units, 77 cents for two bedrooms, and 74 cents for three bedrooms.

In the latest IREM survey from this spring, the occupancy rate for the Omaha multifamily market was 96.2 percent, which is a 17-year high, a strong indication of Omaha's ability to absorb the new supply completed in 2013 and projected for 2014.

Interest Rates Creep Up

From a financing perspective, Omaha continues to be an attractive place for lenders given Omaha's strong underlying economy, reasonable valuations per unit, solid occupancy rates market-wide and modest growth in supply.

The one change that has occurred is that the yield on the 10-year Treasury note has risen almost exactly 100 basis points since Jan. 1, 2013, and the market's summer reaction to a potential change in the Federal Reserve's bond buying program left little doubt that at some point interest rates will rise further.

Consequently, most apartment landlords have already taken the opportunity to refinance at attractive long-term rates during the past two years, and most developers are rushing to get shovels in the ground while attractive financing remains available.

Financing rates on stabilized projects are typically running 180 to 200 basis points over the corresponding 10-year Treasury yield with loan-to-values generally at 75 percent, and sometimes reaching 80 percent.

Deal Velocity

Through mid-December of 2013, there were two relatively large multifamily sale transactions (150 or more units) closed, down significantly from the five that sold in 2012. Of the two properties that sold, one was a sale by a merchant developer and the other was the repositioning and sale of a value-add deal.

In addition, we expect that one larger five-complex portfolio may trade in the coming months. As of mid-December, there were two other properties with 200 or more units on the market, which are likely to trade in the first quarter of 2014.

While demand for Omaha multifamily assets continues to far exceed supply, there is always the challenge of bridging the gap between buyer and seller expectations, especially in an environment where interest rates have moved up 100 basis points during the past year.

That being said, Omaha continues to be an attractive market for investors who are able to acquire properties at slightly higher yields and lower prices per door than in larger cities.