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Hot downtown apartment market piques developer interest

By: [Alby Gallun](#) August 30, 2010

(Crain's) — The downtown apartment market is on such a roll that developers like Tony Rossi are getting ready to start building again.

Mr. Rossi, president of Chicago-based [RMK Management Corp.](#), is putting together cost estimates for a 44-story tower in the Loop and expects to start soliciting lenders in the next few weeks. Leasing at a recently completed project Mr. Rossi co-developed in River North has been surprisingly strong, giving him the confidence to push forward with another one.

"The leasing [pace](#) has been really good," he says. "I don't want to uncross my fingers, but we're pretty happy right now."

So are a lot of his competitors. The occupancy rate at top-tier downtown apartments rose to 94.5% in the second quarter, up from 93.6% in the first quarter and 93.4% in the year-ago period, according to a recent report by [Appraisal Research Counselors](#), a Chicago-based consulting firm. It was the highest Class A occupancy rate in nearly three years.

Net effective rents, which include concessions such as free rent, rose to \$2.22 a square foot in the quarter, up 2.8% from the first quarter and 2.3% from the year-earlier period, the Appraisal Research report says.

The downtown apartment market is flourishing this year even as other real estate sectors, like office and retail, struggle with soaring vacancies, falling rents and mounting loan delinquencies.

While a bad job market usually means tough times for apartment owners, this time it's different, thanks to depressed demand for condominiums and single-family homes. Some downtown denizens can't qualify for mortgages, while others are scared of falling home prices, or of making any kind of major financial commitment. Renting has become the preferred alternative for many.

"People are retrenching, and I think renting is consistent with that mindset," says Appraisal Research Vice-president Ron DeVries. "Everyone wants to reduce their risk, I guess."

Mr. DeVries expects Class A occupancies to rise to about 95.5% by the end of the year, and he forecasts a 9.5% year-over-year rent increase. Class A rents haven't risen that much since 2006.

Demand for apartments is so strong that landlords have been able to hike rents even during a much-feared building boom that has added 3,620 apartments to the market since the beginning of last year. The last of the new buildings, a 329-unit tower at 210 N. Wells St., opens this fall, and it could be three years before another new apartment project is ready for occupancy, good news for landlords of existing buildings.

But Mr. Rossi and other developers are laying the groundwork for the next construction wave. Chicago-based [Amli Residential Partners LLC](#) recently signed a ground lease for a site at the southeast corner of Clark and Hubbard streets, where it plans to build a 49-story apartment tower that would open in 2013 at the earliest.

Related story: [Apartment tower slated for River North](#)

Securing construction financing remains a huge obstacle for developers, but Mr. Rossi says he sees signs that lenders are starting to loosen up. He and partner Thomas Moran want to build a 321-unit tower at 73 E. Lake St. and plan to have a book on the roughly \$120-million project

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\$600 million
invested in
in 2009.

Source: U.S. Dept.

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ready for lenders and equity partners in the next two weeks. If all goes according to plan, they would break ground next year and complete the tower in 2013.

In June the developers opened their current project, the Parc Huron, and the 221-unit tower at 469 W. Huron St. is already about 60% leased, Mr. Rossi says. Net rents in the River North building are about 5% higher than originally forecast.

"The market continues to respond well to new product with strong leasing activity," the Appraisal Research Report says. "There is clear demand for high-end product downtown with leasing agents reporting diverse demand sources including transferees, relocation from the suburbs and unbundling of households in addition to typical move-up demand in the market."

Strong demand and the end of development means downtown could soon have a shortage of apartments, the report says, setting the stage for some big rent increases in the next couple years. In one key indicator of demand, renters occupied 19,054 downtown apartments in the second quarter, up 28% from the end of 2007. Appraisal Research expects another 12% increase over the next year.

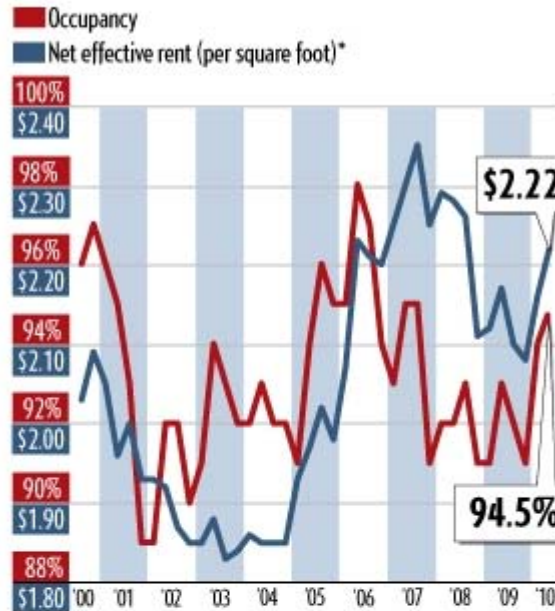
Most apartment landlords are prospering despite competition from rentals at downtown condo buildings. In most cases, individual condo owners are renting out their units rather than trying to sell them for a loss, but some developers are also offering unsold condos for rent as a survival strategy.

The number of downtown condos rented through the Multiple Listing Service rose to 1,808 in the second quarter, up 72% from the first quarter and 32% from the prior-year period, according to Appraisal Research.

LANDLORDS' LEVERAGE

Landlords at Class A apartment buildings have hiked rents this year as occupancies have risen to their highest since mid-2007.

DOWNTOWN CLASS A APARTMENTS By quarter



* Net effective rent factors in the value of concessions

With more residents favoring renting over buying, the number of occupied downtown apartments has jumped 28% since the end of 2007.



Source: Appraisal Research Counselors

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