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# Downtown Chicago Residential Market Overview – Second Quarter 2006

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Gail Lissner and Ron DeVries are co-authors of the Appraisal Research Counselors Downtown Chicago Residential Benchmark Report and the Suburban Chicago Apartment and Condo Conversion Report. The Benchmarks provide an in-depth analysis and review of the rental and for-sale housing market and are used by persons who want to make informed decisions regarding residential real estate investments in Chicago.

To purchase a Benchmark Report, contact Ron DeVries at 312 565 3432 or rdevries@appraisalresearch.com or Gail Lissner at 312 565 3423 or glissner@appraisalresearch.com

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## Downtown Chicago

The 2006 survey results presented in our Downtown Chicago Residential Benchmark Report clearly demonstrate the strength of the downtown rental market. Job growth, depletion of supply due to the 2005 condo conversions, and minimal new units coming on line have converged to produce some of the highest net historical gains in the market. In fact, current occupancy levels would suggest that owners have room to push rents further.

## Downtown Rent Trends

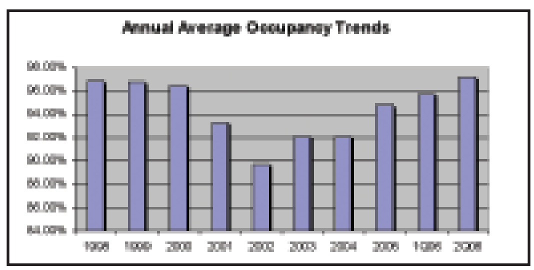
With the removal of concessions in the market, the net effective rents in the Class A market gained over 13 percent compared to second quarter 2005 and almost 8 percent over last quarter. In the B market, net effective rents were up over 10 percent compared to first quarter 2005 and almost 4 percent over the last quarter.

While net rents are certainly up significantly over the last quarter as well as last year, we believe the market supports additional rent increases in the near term. The continued rise in occupancy suggests tenants have a shortage of options and they are lining up to pay the higher rents.

Some owners are becoming more aggressive in raising rents at the expense of some occupancy, but many owners appear to be simply adjusting rates upward with greater frequency rather than only a few times a year. With occupancies above 95 percent and percent leased on many buildings approaching 98 to 99 percent, owners may be missing opportunities in rent growth by not raising rents further.

## Downtown Occupancies

The Class A market gained 230 basis points closing out the quarter at 97.5 percent while the gain over the first quarter 2005 numbers was over 300 basis points. The Class B occupancies are up 90 basis points at 96.9 percent while they are up 270 basis points over the first quarter 2005.




The market is undersupplied at this time. With occupancies overall at 97.2 percent, most properties are actually leased at roughly 98 percent or more. There are very few vacant units in the market which are not leased. Village Green's MDA and UBS's Bernardin reached stabilized operations in 2Q06 leaving only Sky55 in the South Loop in lease up. The Streeter and Residences at Left Bank are anticipated for later this year and should relieve some of the current pressure on supply.

## Downtown New Deliveries

The new rental product recently brought to the market has been absorbed at a record pace. The only building in a lease up program is Sky55 which began offering occupancy in April 2006. The Streeter is planning on occupancy in August 2006 with Residences at Left Bank leasing in the fourth quarter of this year.

In addition to the 1,960 units under construction and the 1,823 units on the drawing board, we are tracking a number of confidential deals containing over 4,000 units – some of which could potentially be announced in 2006 for delivery likely starting in 2009. Certainly, some of these deals will not materialize due to feasibility and/or financing issues but nonetheless, developers have new rental construction high on the priority list.

## Downtown Shadow Rental Market

We are tracking units leased on the MLS and the number is on a steep increase with almost 700 units leased in the second quarter alone. We believe the increase in condo leases is due to the limited options in the traditional for rent market rather than more condo units being place on the market for rent. We continue to see this as providing limited competition due to the unorganized nature of this market.

## Downtown Investment Market

After a record year in 2005, we are projecting transaction volume for 2006 could be half the volume of 2005 – more in-line with historical patterns. While operating performance is certainly up for apartments, there is simply less product available on the market.

The two major closings for 2Q06 included McClurg Court and River North Park. With the cooling of the higher end condo conversion unit sales in late 2005, converters (and their lenders) are now sitting on the sidelines. Non-converters will likely dominate the dollar volume of the market for 2006 with three of the six deals currently in play projected to go to a converter.

Cook County Real Estate Taxes – Cook County is on a triennial assessment cycle with 2006 being a reassessment year for Chicago. The first round of assessments for the northern townships has been released and the results are, as expected, wide ranging. For 2006, a further reduction in assessment ratios was approved for Cook County taking the assessment ratio from the current level (2005) of 26 percent of the assessor's opinion of market value to 20 percent in 2008.

Thus, even if the assessor's opinion of market value increases notably (which most believe will be the case), the decline in the ratio along with reductions in the equalization factor and tax rates should hold the resulting tax bills in check.

## Suburban Chicago Trends

The database for the 2Q06 Suburban Chicago survey presented in our Suburban Chicago Apartment & Condo Conversion Report consisted of 212 complexes with a total of 72,292 dwelling units. Our survey includes virtually every major community developed since 1995 plus older developments throughout the MSA. Median net rent per square foot is up 5.6 percent from a year ago. Rents are up over five percent from 4Q05 alone. The largest gains in net rent on a year over year basis were in the Waukegan/Gurnee and Naperville/Aurora markets. 2Q06 physical occupancy increased once again from 96.4 to 97.1 percent for the entire market.

There was a high level of condominium conversion activity taking place with 1,496 units added to the market in newly converted projects and 1,147 units sold during the quarter. This is a significantly higher level of both conversions and sales than occurred in the 1st Quarter 2006 when 458 units were added to the market in newly converted buildings, with 746 units reported to have been sold during the quarter. As of the 2nd Quarter 2006, Appraisal Research Counselors is tracking sales in 48 projects with a total of 9,002 units.