



Hurricane Katrina: One Year Update

Impact on Houston Multifamily

What's Inside...

- New Orleans - One Year Update
- Houston - One Year Update
- What's Next for Houston

Written by:
Leslie Countryman

Edited by:
Kathryn Koepke



2200 North Loop W., Suite 200 Houston, TX 77018 • 713-686-9955 • (fax) 713-686-3377
www.poconnor.com • www.oconnordata.com
Houston (Corporate) • Dallas • Newport Beach • Los Angeles

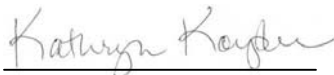
November 28, 2006

The following report is an update to the original O'Connor & Associates' Hurricane Katrina report written by Kathryn Koepke and published on December 16, 2005. Similar to the last report, we have made every reasonable effort, including phone calls with various officials, scouring newspaper and magazine articles, and reviewing multiple reports, to obtain the most current and accurate information. In spite of our persistent efforts, we realize there are some numbers that are difficult to come by, as multiple sources report differing information. In each case, what is published here represents the best information available.

The multifamily data in this report comes directly from O'Connor & Associates' online apartment database. O'Connor & Associates surveys every apartment complex with at least 50 units in each of the four major markets in Texas each month. We are confident that you will find this publication to be the most comprehensive source of information and analysis on the impact of Hurricane Katrina upon the Houston multifamily market.



Leslie Countryman
Senior Market Analyst



Kathryn Koepke
Manager, Research & Consulting

TABLE OF CONTENTS

1. New Orleans – One Year Update.....	4
2. Houston – One Year Update.....	9
3. Houston’s Multifamily Market – One Year Update.....	13
4. Future Expectations in Houston.....	25

New Orleans – One Year Update

New Orleans Recovery

Hurricane Katrina made landfall on August 29, 2005. The subsequent breach of the levee devastated the city. In a report by the Louisiana Recovery Authority, they estimated that Hurricane Katrina displaced 1.3 million residents from their homes; caused the deaths of 1,580 residents; destroyed 204,500 homes; and caused the loss of 220,000 jobs. Property and Infrastructure losses were estimated between \$75 and \$100 billion.

Greater New Orleans' pre-Katrina population was estimated at slightly over 1.3 million by the U.S. Census Bureau, while the pre-Katrina population of the City of New Orleans was estimated at 454,863 people. Since Katrina, residents have steadily moved back into the area, with a significant jolt coming from students and faculty when the city's universities, Tulane, Xavier, Southern University, Dillard, University of New Orleans, and Loyola reopened (some in nontraditional locations) in January 2006 for the Spring semester. The City of New Orleans' current population remains less than half of what it was pre-Katrina, at 190,000, according to multiple reports.

Although damage and debris are still prevalent in the hard hit areas of the city, many areas like the Garden District, French Quarter, Central Business District, and Warehouse District are up and running. Utility services have been restored to these areas, while public transportation has also resumed, albeit with fewer busses and routes. Public services to the heavily damaged areas, however, have for the most part, yet to be restored. Per the Brookings Institute report dated August 2006, gas and electricity service is reaching only 41% to 60% of the pre-Katrina customer base. Of the area's 22 hospitals, 11 have resumed full operations. It was also reported that 54 of the city's 128 public schools have reopened, and that another 200 parochial schools across the Greater New Orleans area have also reopened.

In terms of area business operations, the Louisiana Department of Economic Development reports that 17,716 businesses, or 90% of pre-Katrina business numbers, have reopened in New Orleans. Among the notable business re-openings: Shell Exploration and Petroleum Corporation, Northrop Grumman, Lockheed Martin, and Hertz Investment Group. Employment figures for the Greater New Orleans area indicate that the labor force is roughly 30% smaller than it was prior to Katrina. Nonagricultural employment in the area in September 2006 was 432,051, while pre-Katrina nonagricultural employment was 634,512, according to the Bureau of Labor Statistics. Unemployment in the area has improved dramatically over the last year. Bureau of Labor Statistics figures indicate that the unemployment rate in September 2005 was 17.7%. The unemployment rate has since declined to 4.6%, as of September 2006. The employment situation is expected to improve. Loren Scott, a professor at Louisiana State University, predicts that the New Orleans area will add 34,300 jobs over the course of 2006.

New Orleans' mainstay, the hospitality industry, has bounced back over the year. An estimated 85% of the city's 140 hotel rooms have reopened, and 700, or 46%, of the city's restaurants have reopened for business. New Orleans was also able to host 350,000 people during Mardi Gras festivities in February of 2006. Louis Armstrong International Airport has since resumed a significant amount of flight operations, as departures are up to 64% of their pre-Katrina levels. The Port of New Orleans is also once again operating at full capacity. And, the Louisiana Superdome has completed its \$168 million overhaul and reopened on September 25th for a New Orleans Saints versus Atlanta Falcons NFL prime-time football game.

The ever-important convention business has rebounded. In the wake of the storm, 73% of the conventions on the books for 2006 were canceled. Since Katrina, the Ernest N. Morial Convention Center has undergone a \$60 million clean-up and renovation. The first citywide convention since

Katrina, the American Library Association Convention, which brought to town 20,000 attendants, was successfully held in June 2006. Despite the drop off in 2006, New Orleans was able to retain 70% of the conventions scheduled for 2007 and 92% of the conventions scheduled for 2008, according to the New Orleans Convention and Visitors Bureau.

New developments that will bolster the convention and tourist industry are now in the works. Hyatt Jazz District, a \$716 million six-block development, is planned for the area around the Superdome and Hyatt Regency New Orleans hotel in Downtown New Orleans. The 20-acre development will be anchored by the National Jazz Center, which will house the New Orleans Jazz Orchestra as well as performance space, studios, classrooms, a library, and offices. In addition, there will be an outdoor auditorium and new city government buildings built within the development. A bridge will be built to link the Superdome to the Jazz Park and a bus and streetcar line will link the park to the French Quarter, convention center, and riverfront. The development is expected to generate 6,500 jobs and bring a \$6 billion economic benefit to the City of New Orleans of the next 20 years. The first stage, the clean-up and renovation of the Hyatt Regency New Orleans, is already underway.

Housing

A major limiting factor for those seeking to return to New Orleans is the lack of available, habitable, reasonably-priced housing. New Orleans city officials estimated that 160,000 homes were flooded after the hurricane. The rental market was also devastated, losing an estimated 43,000 rental units. Considering New Orleans was primarily a renter market, this has had a grave effect on the ability of many displaced residents to return to New Orleans. The Brookings Institute reports that rent prices are 39% higher than what they were prior to Katrina. Public housing in New Orleans has been very slow to return. As of June 2006, the Houston Chronicle reported that only 1,000 of 8,000 public housing units had reopened for occupancy, while 5,000 damaged units were slated for demolition. Housing relief in the area has come in the form of FEMA mobile trailers. The originally intended plan of housing groups of displaced residents in the trailers throughout the city drew protest from area property owners, and was abandoned. As it stands now, a few thousand FEMA trailers are scattered throughout the city, with most being located on individuals' private property, while their homes are being rebuilt.

Though it has taken a considerable amount of time, the clean up of neighborhoods is now underway. Individual homeowners have applied for 38,594 rebuilding permits in the city of New Orleans through the end of August. Homes that cannot be repaired are also being taken care of. As of August 2006, the U.S. Army Corps of Engineers has demolished roughly 300 damaged homes. The city has also issued notices to another 3,000 homes. These homes must be gutted by their owners within a specific timeframe, or they will be demolished by the city. Homes in the badly damaged 9th Ward have received hardship exemptions from the deadline.

Levees

Hurricane Katrina brought the gross deficiencies of New Orleans' levee system to light. Since then, the Army Corps of Engineers admitted they were responsible for the severe flaws in the design and construction of the 350-mile levee system. The Corps is still in the process of repairing the damaged levees. They have already largely returned the levee system to pre-Katrina flood and storm protection, however armoring of the levee system and completion of pumping upgrades is not expected to be completed until July 2007.

Rebuilding: Politics & Debate

A mixture of squabbling, tension, confusion, and general ineptitude have marred the rebuilding process in New Orleans. Immediately following the storm, in September 2005, Mayor Ray Nagin initiated the Bring New Orleans Back Commission who retained the services of the Urban Land Institute (ULI) to devise a restoration plan for New Orleans. In light of the city's shrinking population prior to Hurricane Katrina, and the knowledge that the city would return to at most three-fourths of its pre-hurricane size, ULI devised a plan that would accommodate the smaller population on a necessarily smaller land base. ULI divided the city into three zones: Zone 1, which are high-lying areas the group recommended rebuilding first; Zone 2, which are mid-ground areas ready for immediate rehabilitation and may be available for use as green space and redevelopment; and Zone 3, which are low-lying areas that need additional study but were likely not suitable for development and could possibly be used for parks, drainage, and green space that would help prevent future flooding. The group warned against scattered and uncoordinated rebuilding as that could result in the creation of slums, where pockets of rebuilt homes were surrounded by blight.

The ULI recommendations were met immediately with stiff resistance, particularly from those who lived in the low-lying, predominately poor, African-American neighborhoods. Racial tensions escalated, and the plan was promptly abandoned by Mayor Nagin. Nagin then came out in support of plan that would allow residents to rebuild anywhere in the city. Residents of a neighborhood would come up with their own plans for rebuilding their neighborhoods, which would then be knitted together in a larger plan. With no central authority to coordinate efforts, neighborhood planning was disorganized. Some neighborhoods came up with detailed plans, while other neighborhoods never made a plan. And, the individual neighborhood plans that were made were mostly done without regard to nearby communities or the overall picture. Thus, it quickly became clear this was not a productive means to rebuilding the entire community.

Adding to the difficulties of rebuilding has been the federal government's ineffectiveness in approving and delivering monetary aid to the area in a timely manner. Shortly after the hurricane, Congress set aside \$62 billion for the Gulf Coast states. However, the first major monies the area received came in December, a full three months after Hurricane Katrina, when \$29 billion was divided up between Louisiana and Mississippi. The package gave Mississippi about five times as much aid per household as Louisiana.

Following the initial relief package, which had a great deal of shortcomings in regards to housing redevelopment in Louisiana, Richard Baker, a Republican Representative, proposed a bill where the federal government would spend as much as \$80 billion and create the Louisiana Recovery Corporation, which would pay off lenders up to 60% of what they were owed on homes in default, pay homeowners no less than 60% of their equity they had in their homes, restore public works, and buy the rights to large chunks of ruined land within the city. These areas would be cleared and then sold back to developers. Local authorities and developers would be in charge of the redevelopment of the land. This plan gained widespread support among New Orleans residents across all races, local New Orleans authorities, and across party lines in Congress. When it came time for final approval of Baker's plan, the Bush administration rejected the proposal.

In June 2006, Congress did appropriate \$4.2 billion for rebuilding homes and businesses in Louisiana, bringing the total rebuilding funds up to \$10.4 billion. Louisiana's latest incarnation of a rebuilding plan is the Road Home plan, which is similar to the Baker plan. The Road Home plan is estimated to cost a total of \$9 billion and provides eligible residents up to \$150,000 to rebuild or sell their severely damaged homes, using grants to cover repair costs above what was covered by

insurance policies and FEMA grants. People who choose to sell their homes and relocate to another state will pay a penalty. Those that stay and rebuild must follow certain construction codes.

After a year of political bickering and indecisiveness, it does appear that reconstruction is finally moving forward as homeowners and apartment owners now have the ability to rebuild or sell and move on with their lives. However, it is slightly disconcerting as the city still lacks a comprehensive rebuilding plan, one that combines an intelligent all-encompassing approach whilst avoiding haphazard development. Despite the fact that it has been an entire year since the hurricane and subsequent levee breach, it still remains to be seen how well New Orleans will reemerge from the disaster.

Houston – One Year Update

Evacuees in Houston

As one of the nearest and largest metropolitan areas to New Orleans, Houston took in a massive number of New Orleans residents before and after the hurricane. At its peak, approximately 300,000 evacuees took refuge in Houston. One year later, multiple reports indicate that approximately 120,000 evacuees remain in Houston.

Voucher Plan

In response to the influx of evacuees, the City of Houston created a voucher program to provide 12 months of free rent and utilities in affordably priced area apartments. Funding of the program was initially uncertain, however, the Federal Emergency Management Agency (FEMA) did eventually agree to reimburse Houston for the costs of the voucher program. According to a report released by the Joint Hurricane Housing Task Force Communications Team, Houston placed approximately 156,000 evacuees in roughly 37,000 Houston area apartments. As of October 2006, 15,000 households containing an estimated 50,000 people remain on FEMA rental assistance. This indicates that a large portion of the evacuees that remain in Houston are still receiving assistance. Though multiple FEMA deadlines have come and gone, FEMA is adamant that all assistance for Katrina evacuees will end, one way or another, in February 2007.

Schools

Houston area school districts experienced a dramatic increase in enrollment after Hurricane Katrina. According to a survey conducted by O'Connor & Associates, 15,764 student evacuees were enrolled in Houston-area public school districts in October 2005. By the end of November, this number increased to 19,013. Other reports in the media estimated peak student evacuee enrollment around 21,000, including private schools. The additional students crowded schools, caused increased disturbances at school due to tensions between students, and stretched the budgets of school districts. One year after the hurricane, 9,760 evacuee students remain enrolled in Houston-area public schools.

The September 2006 enrollment figures indicate that the Houston Independent School District (HISD) had the highest number of evacuee students at 2,846, followed by Alief ISD where evacuee enrollment was at 1,738 students. Other districts that report evacuee enrollment at over 500 students in September 2006 include: Spring ISD at 684, Cy-Fair ISD at 884, and Aldine ISD at 980 students.

From October 2005 to September 2006, 6,004 fewer students were enrolled in Houston area public schools. Of the seventeen surveyed school districts, only two, Alief ISD and Aldine ISD, reported increases in enrollment of evacuee students over the timeframe. District-wide the largest decreases in evacuee enrollment were found in Clear Creek ISD, Cy-Fair ISD, Katy ISD, and Fort Bend ISD. We believe the decreases recorded at these suburban districts reflect the likely fact that these students' families were middle-to-upper income families that had the financial ability to return to New Orleans.

The following table includes the number of evacuee students enrolled at each of the surveyed school districts in October 2005 and September 2006.

Student Evacuee Counts by District

School District	October 2005 Count	September 2006 Count	Difference
Houston ISD	3,400	2,846	-554
Fort Bend ISD	1,662	499	-1,163
Cy-Fair ISD	1,500	884	-616
Alief ISD	1,400	1,738	+338
Katy ISD	1,200	404	-796
Spring ISD	943	684	-259
Clear Creek ISD	865	268	-597
Aldine ISD	853	980	+127
Pasadena ISD	800	351	-449
Klein ISD	680	208	-472
Humble ISD	566	257	-309
Spring Branch ISD	526	192	-334
Pearland ISD	428	109	-319
Galena Park ISD	347	185	-162
Lamar CISD	260	109	-151
La Porte ISD	200	6	-194
Deer Park ISD	134	40	-94
Total	15,764	9,760	-6,004

* No data was obtained from the Stafford Independent School District.

Crime

Crime has been an area of major concern with the increase in population. Overall violent crime totals in Houston in 2005 increased 2.4% from the previous year. Non-violent crimes actually decreased by 1.7% from 2004 to 2005. Though overall crime totals are not much different than before Hurricane Katrina, the homicide rate is up significantly. From 2004 to 2005, homicides increased 23%, from 272 to 334. From January 2006 through late August 2006, 262 homicides had occurred, which represents a 17.5% increase from the same timeframe from the year before. Police reported that 59 of the 262 murders involved Katrina evacuees as either victims or suspects. In order to combat crime and ease public fears, Houston police chief Harold Hurtt announced the formation of a new 140-officer unit to patrol the high-crime areas, which include a concentration of apartment complexes in southwest Houston (Beltway 8 & Bellaire area), northwest Houston (U.S. 290 & Bingle area), and north Houston (Interstate 45 & Greens Road area).

Jobs

According the U.S Bureau of Labor Statistics October 2006 data, there are 235,000 displaced evacuees nationwide that are considered part of the civilian labor force. Of those 235,000 displaced evacuees, 14.5% remain unemployed, which is in stark contrast to the rate seen in the evacuee population that have been able to return to their homes (4.7%). The employment situation for evacuees in Houston appears worse. A report by National Public Radio in August 2006 found that 60% of evacuees in Houston were unemployed. Further, a study conducted in July 2006 by professors at Rice University found that 70% of evacuees were unemployed, 23% were employed,

and 7% were retired. Prior to Hurricane Katrina, 66% of evacuees reported that they were employed, 27% reported they were unemployed, while 7% reported they were retired.

What the Future Holds for Katrina Evacuees in Houston

When it became apparent there was no cohesive, national plan on how to aid, house, educate, and care for the many thousands of evacuees from New Orleans, the City of Houston devised their own plan. Houston managed this feat despite unclear information on how all the bills relating to housing, education, healthcare, and increased police protection for the evacuees would be paid. After squabbles with FEMA about reimbursement, money has trickled in to the City of Houston. In November 2005, FEMA awarded Houston a total of \$138 million to cover the costs of housing and interim expenses. In June 2006, the federal government awarded \$428 million to the State of Texas for hurricane-relief. The U.S. Department of Housing and Urban Development money will go toward rebuilding and repairing homes damaged by Hurricane Rita and to continue providing social services for evacuees from Hurricanes Katrina and Rita. And in August 2006, FEMA awarded Houston another \$55.9 million to cover continued expenses related to evacuee care.

As the number of evacuees has dropped from the initial peak of 300,000 to its current level around 120,000, it is clear that many evacuees have made their way back home. To help some of the remaining evacuees that would like to move back home, Mayor Nagin and his staff in partnership with Mayor White officially opened the Journey Home Center in Houston on August 22, 2006. The center provides displaced New Orleans citizens with information and resources on how to get home and rebuild their lives in New Orleans. Through mid-September 2006, the center had helped 47 families move back to New Orleans.

Although it is impossible to predict exactly how many evacuees will stay in Houston, several surveys of evacuees have been conducted. Rick Wilson and Robert Stein of Rice University sampled 1,081 evacuees in Houston above the age of 18. Their survey indicated that 69% of respondents planned to stay in Houston permanently. This figure might be slightly high, as other area surveys have indicated that anywhere from one-half to two-thirds, or approximately 60,000 to 90,000 evacuees, plan to stay in Houston permanently.

Houston's Multifamily Market – One Year Update

Apartment Market Overview

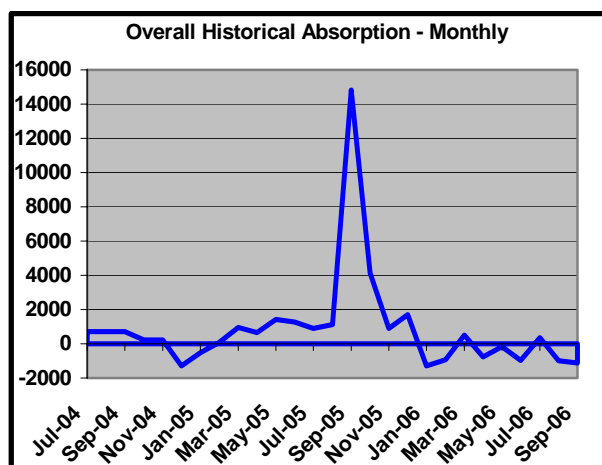
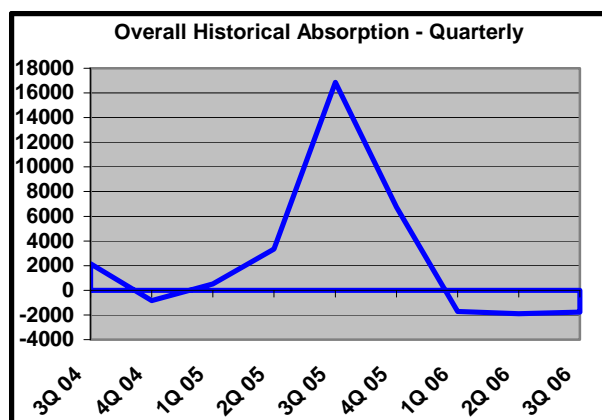
Hurricane Katrina greatly impacted the Houston apartment market. One year after Katrina, the effects on the apartment market have waned. The following table provides a snapshot of the Houston apartment market as of the third quarter of 2006, ending September 2006.

	Class A	Class B	Class C	Class D	Overall
Number of Projects	446	1,057	816	160	2,479
Number of Units	116,784	222,719	141,719	22,185	503,407
Rent per Square Foot	\$1.093	\$0.812	\$0.687	\$0.593	\$0.828
Occupancy	92.04%	90.53%	87.57%	84.63%	89.75%
Quarterly Absorption (in units)	1,776	-1,155	-2,368	-11	-1,758
Sept. 05 thru Sept. 06 Absorption (in units)	4,989	7,578	3,142	477	16,186

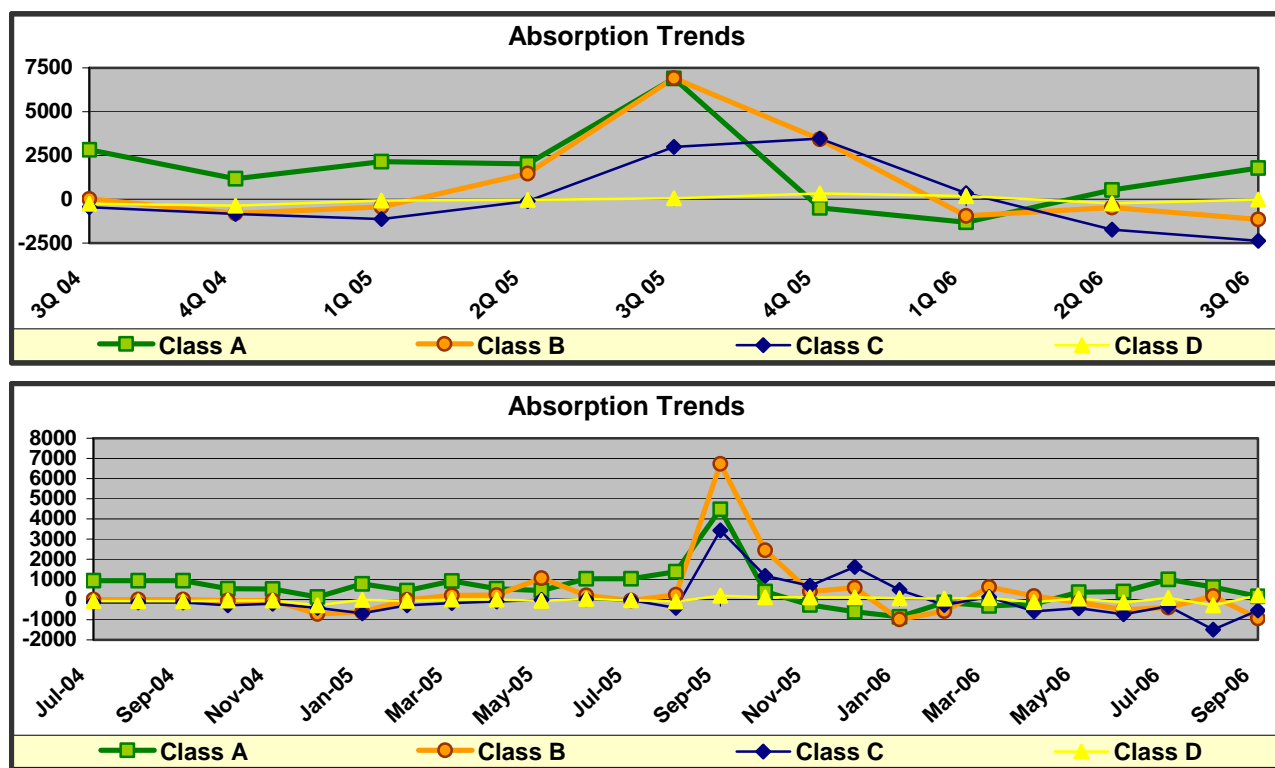
Third quarter 2006 (September 2006) figures indicate that overall occupancy is now below 90%, at 89.75%. Occupancy is strongest in the Class A market at 92.04%, followed by Class B at 90.53%. Classes C and D occupancy is comparatively weak at 87.57% and 84.63%, respectively. Overall rents average \$0.828 per square foot (psf), with Class A rents averaging \$1.093 psf, Class B rents at \$0.812 psf, Class C rents at \$0.687 psf, and Class D rents at \$0.593 psf. Overall third quarter absorption was negative for the third consecutive quarter, with -1,758 units absorbed. Class A was the only class to post positive quarterly absorption, with 1,776 units absorbed. Class C registered the weakest absorption with -2,368 units absorbed, while Class B also had significant negative absorption with -1,155 units absorbed. When reviewing absorption figures from September 2005 through September 2006, the Houston apartment market has absorbed 16,186 units, with the majority of absorption (7,578 units) in the Class B market.

Absorption

After weak absorption figures throughout 2003, demand picked up in 2004, as 2,108 units were absorbed over the year. Absorption remained on a strong path in early 2005, as 502 units were absorbed during the first quarter and 3,351 units were absorbed during the second quarter. Hurricane Katrina hit in late August during the third quarter of 2005, and subsequently caused an unprecedented spike in absorption. In September alone, 14,830 units were absorbed. Absorption during the third quarter, which extends from July through September, registered a record 16,853 units. Absorption remained elevated over the next three months as evacuees moved from hotels and friends' homes into apartments. Fourth quarter 2005 absorption, which extends from October through December, was 6,745 units, with the bulk of the absorption (4,139 units) coming in October. After record absorption figures during the third and fourth quarters of 2005, demand quickly waned as evacuees moved out of apartments en masse. Absorption over the first quarter of 2006 was -1,729, and was -1,902 units over the second quarter. The negative trend continued through the third quarter, as -1,758 units were absorbed.



Absorption trends by class are illustrated in the graphs below.



Prior to Hurricane Katrina, the Class A market was in the best shape of all four classes. Katrina further elevated figures, as 6,889 units were absorbed during the third quarter of 2005, with the bulk of the absorption (4,476 units) occurring during September. Record Class A absorption was not sustained for long, and absorption figures quickly moved into the red in November 2005. Fourth quarter 2005 absorption registered -480 units, while first quarter 2006 absorption was even weaker at -1,319 units. Class A absorption has since moved back into the black. Modest gains were made during the second quarter of 2006 with 536 units absorbed, while even stronger gains were made in the third quarter with 1,776 units absorbed. Class A was the only class to post positive absorption over the second and third quarters of 2006.

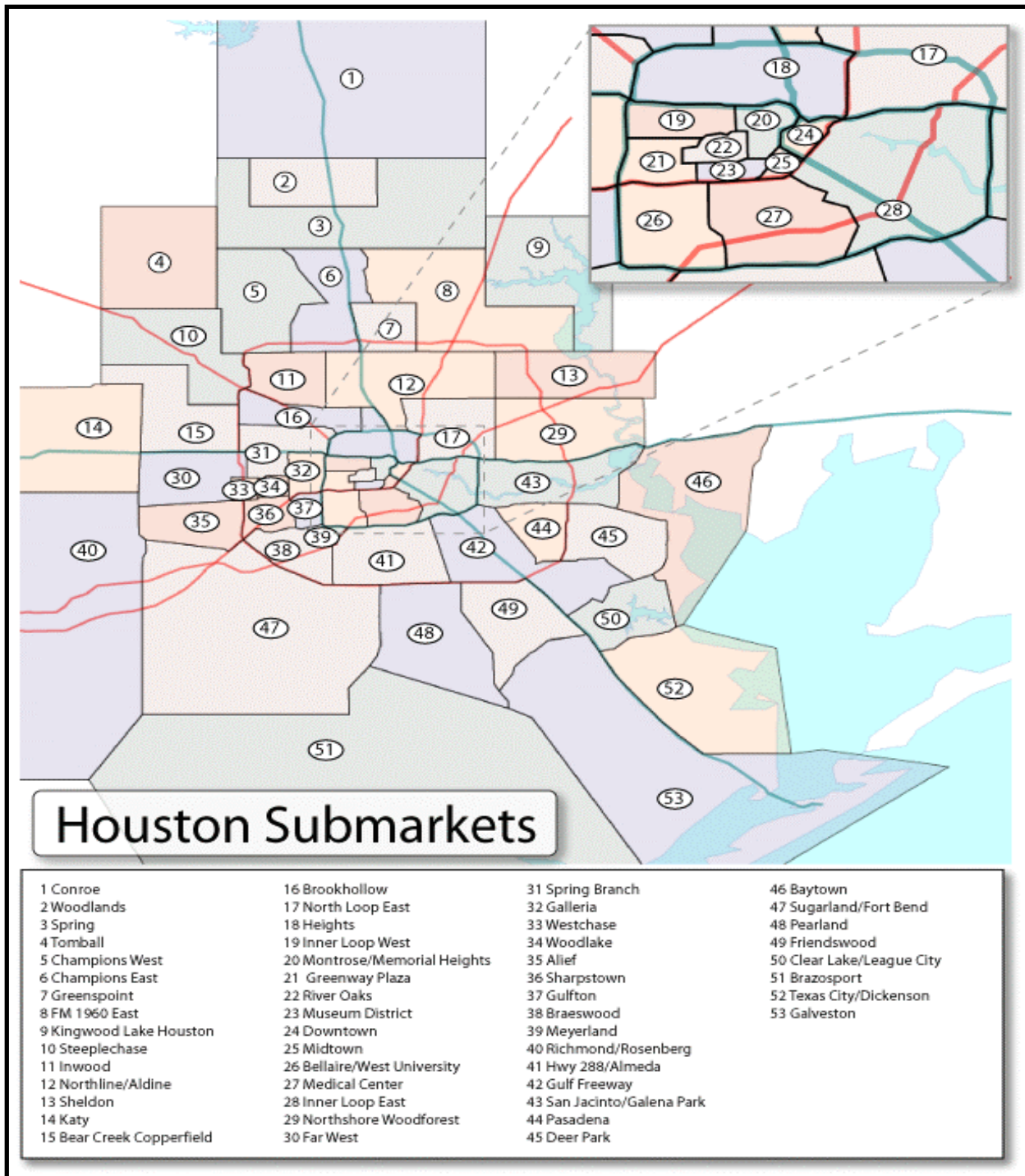
The Class B market posted the greatest absorption figures post Hurricane Katrina, with 6,908 units absorbed over the third quarter of 2005. Unlike the Class A market, absorption remained strong over the fourth quarter, as another 3,427 units were absorbed. Absorption has since moved into the red, as all three subsequent quarters in 2006 have registered negative figures. Year-to-date absorption stands at -2,572 units.

Class C apartments absorbed 2,993 units post-Katrina during the third quarter of 2005. Absorption further strengthened during the following quarter, as 3,467 units were absorbed. Slight positive absorption was recorded during the first quarter of 2006 (343 units), while absorption subsequently dipped to negative figures with -1,734 units of absorption in the second quarter and -2,368 units of absorption in the third quarter.

Hurricane Katrina had negligible effects on the Class D market. During the third quarter of 2005, absorption was 63 units. Absorption increased to 331 units over the fourth quarter, and was also positive during the first quarter of 2006 at 192 units. Second and third quarter 2006 figures have been negative, though only minimal, at -232 units and -11 units, respectively.

Submarket Absorption

O'Connor & Associates divides the Houston apartment market into 54 submarkets. The following is a map of the submarkets.



Submarket Absorption

Hurricane Katrina struck during the third quarter of 2005. Of Houston's 54 submarkets, 39 submarkets absorbed over 100 units during the quarter, 23 submarkets absorbed over 300 units during the quarter, 11 submarkets absorbed over 500 units during the quarter, while 5 submarkets absorbed over 700 units during the quarter. The sectors with the highest absorption over the third quarter of 2005 include Far West (1,253 units), Galleria (1,106 units), Medical Center (957 units), Katy (801 units), Greenspoint (749 units), SugarLand/Fort Bend (670 units), Champions-West (588 units), Brookhollow (574 units), Gulf Freeway (571 units), and Alief (561 units). It is noteworthy that the four sectors with the greatest third quarter 2005 absorption are highly desirable neighborhoods. This indicates that a significant amount of first-wave evacuees that came to Houston and rented apartments did so in nice areas of town based on their own financial means, as at that point in time individuals were not able to use vouchers to cover a portion of the rent at Class A apartments.

During the fourth quarter of 2005, which was when the voucher program was in full force, absorption patterns by submarket shifted. The submarkets with the highest fourth quarter 2005 absorption include Alief (1,247 units), Champions-East (762 units), Sharpstown/Westwood (762 units), Braeswood (618 units), Gulfton (506 units), Brookhollow (467 units), Woodlake (435 units), Northshore/Woodforest (375 units), Baytown (285 units), and Spring Branch (265 units). All of these submarkets have a high concentration of low-income housing. When looking at the concentration of Class B and C properties, which is where the vast majority of the vouchers were used, in these ten submarkets, they are all greater than 70%, with 8 of the 10 submarkets having Classes B & C concentrations greater than 80%.

When totaling third quarter 2005 and fourth quarter 2005 absorption figures together, the submarkets with the greatest jumps in absorption were Alief (1,808 units), Far West (1,378 units), Champions-East (1,247 units), Sharpstown/Westwood (1,239 units), Galleria (1,177 units), Braeswood (1,076 units), Brookhollow (1,041 units), Medical Center (1,039 units), Greenspoint (952 units), and Katy (793 units). These submarkets are a summation of the pattern that was seen over the third and fourth quarters, as they are a mix of relatively expensive areas (Far West, Galleria, Medical Center, Katy) and lower income areas (Alief, Champions-East, Sharpstown/Westwood, Braeswood, Brookhollow, and Greenspoint).

After two quarters of record absorption, absorption slowed considerably during the first quarter of 2006. Of the 54 submarkets in Houston, only 18 posted positive absorption over the quarter. Of those 18 submarkets with positive absorption, only 9 submarkets posted absorption of above 50 units, with the highest absorption that quarter in Pasadena, which absorbed 247 units. The areas that experienced the greatest negative absorption during the fourth quarter were the Galleria (-476 units), Far West (-284 units), and the Medical Center (-244 units). These three sectors with the greatest negative absorption during the first quarter of 2006 were the three sectors with the greatest positive absorption immediately after the hurricane during the third quarter of 2005. As these three submarkets are some of the most desirable and expensive submarkets in Houston, the evacuees that rented within these submarkets had the financial means to do so. It is not surprising then, that these evacuees with financial means were the first to leave Houston's apartments and either return home or establish permanent residence elsewhere.

Over the second quarter of 2006, absorption dwindled further. The submarkets that experienced the greatest negative absorption over the quarter include Sharpstown/Westwood (-637 units), Gulf Freeway (-534 units), and Brookhollow (-516 units). These three sectors that experienced the greatest drop in demand during the second quarter of 2006 contain a high concentration of Class B and C properties and are generally considered as low-income areas of town. This indicates

evacuees left in waves. The first wave was likely the upper-income households who had the financial means to either return home and rebuild or settle somewhere else relatively quickly, while the second wave was likely from middle-income households who were financially stable enough to forgo the remainder of their 12-month housing vouchers and return home or settle elsewhere. We expect the second was likely mostly middle-income households and not low-income households, as there is still virtually no low-income housing available in New Orleans, and there is no program offering the same benefits as Houston's 12-month voucher program.

During the third quarter of 2006, one year after Hurricane Katrina, overall absorption remains negative. Despite that fact, typical absorption patterns across the submarkets have returned. The submarkets with the highest absorption over the third quarter include Bryan/College Station (578 units), Gulf Freeway (282 units), Medical Center (270 units), Pearland (264 units), The Woodlands (151 units), and Katy (147 units). Many of these submarkets are suburban submarkets, which typically lead absorption figures in the Houston area. The submarkets with the weakest demand over the third quarter include Sharpstown/Westwood (-500 units), Braeswood (-441 units), Alief (-436 units), Far West (-424 units), Pasadena (-277 units), and Brookhollow (-240 units). Although Far West is a desirable area of town, the remaining submarkets contain a high concentration of Class B and C properties, indicating that even more evacuees, that were likely on the 12-month vouchers, have been able to leave Houston area apartments and return to New Orleans.

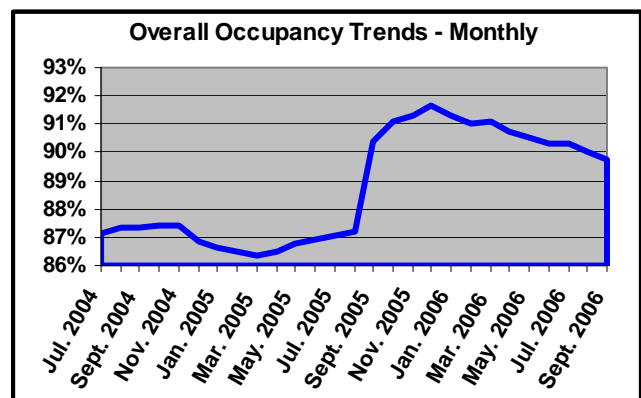
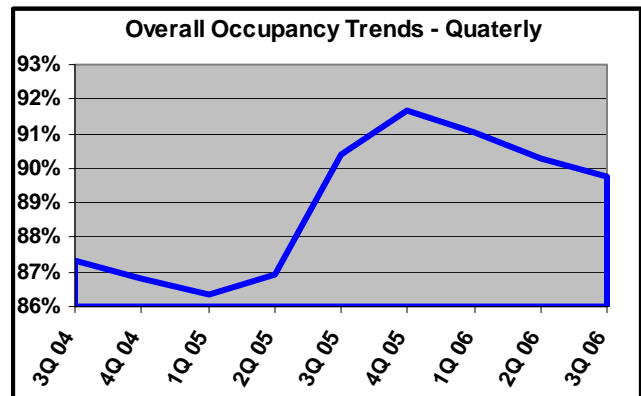
While the two quarters immediately after the hurricane, the third and fourth quarters of 2005, recorded record positive absorption, the three subsequent quarters, the first, second, and third quarters of 2006, all recorded significant negative absorption. The submarkets that experienced the greatest decline in demand over the first, second, and third quarters of 2006 were Sharpstown/Westwood (-1,160 units), Far West (-900 units), Alief (-686 units), Brookhollow (-682 units), Braeswood (-677 units), Westchase (-423 units), Galleria (-410 units), Gulf Freeway (-373 units), Champions-East (-202 units), and Northshore/Woodforest (-173 units). The significant negative figures indicate that high-income households that resided in Far West, Galleria, and Westchase submarkets as well as many lower-to-middle income households that resided in the other submarkets have made their way out of Houston apartments and likely back to New Orleans. As stated previously, we expect that the majority of households with the financial means, opportunity, and desire to move home have already made their way back home. The majority of those that remain in Houston in apartments, are likely very low-income households that have no other options but to remain in Houston throughout the duration of the free voucher program, which is set to terminate in February 2007.

The following chart displays absorption per quarter from the third quarter of 2005 through the third quarter of 2006 by submarket.

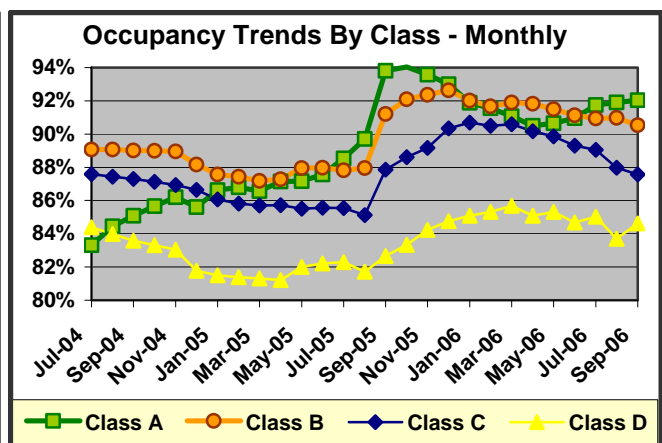
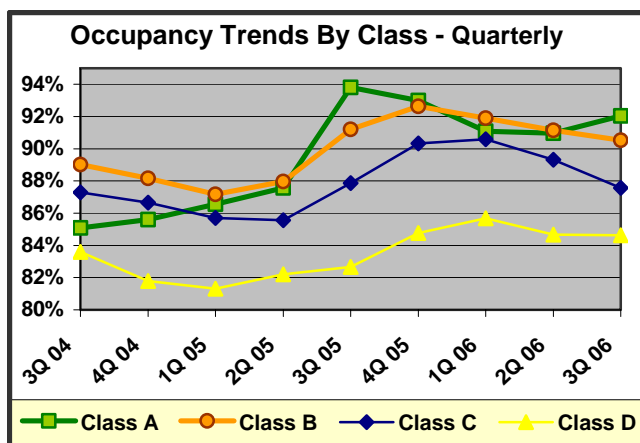
Absorption By Submarket	3Q05	4Q05	1Q06	2Q06	3Q06
Alief	561	1,247	-95	-155	-436
Baytown	336	285	91	5	-232
Bear Creek / Copperfield	443	-7	-76	-114	101
Bellaire / West University	13	6	-11	4	-11
Braeswood	458	618	7	-243	-441
Brazosport	155	-22	-15	37	-39
Brookhollow	574	467	74	-516	-240
Bryan / College Station	-27	23	-215	-245	578
Champions – East	485	762	46	-47	-201
Champions – West	588	-58	41	77	97
Clear Lake / League City	266	80	-231	150	18
Conroe	176	-73	-36	110	55
Deer Park	307	-43	-1	125	-40
Downtown	53	-38	0	20	-63
Far West	1,253	125	-284	-192	-424
FM 1960 East	530	231	-103	180	36
Friendswood	225	-19	-6	-70	35
Galleria	1,106	71	-476	70	-4
Galveston	241	-25	-213	64	-5
Greenspoint	749	203	89	77	-230
Greenway Plaza	113	-53	-72	39	3
Gulf Freeway	571	183	-121	-534	282
Gulfton	214	506	74	42	-63
Heights	175	-2	45	60	72
Highway 288 / Almeda	107	82	-8	-36	139
Inner Loop East	69	60	0	37	-157
Inner Loop West	93	20	-14	-10	12
Inwood	405	140	180	-172	-45
Katy	801	-8	-56	-50	147
Kingwood / Lake Houston	149	46	-74	-9	40
Medical Center	957	82	-244	-155	270
Meyerland	9	32	-68	3	-69
Midtown	148	0	-47	24	-29
Montrose / Memorial Heights	71	-60	-25	6	-6
Museum District	54	36	91	21	67
North Loop – East	229	4	-3	-58	22
Northline / Aldine	411	73	23	-24	-133
Northshore / Woodforest	155	375	-133	-55	15
Pasadena	178	-3	247	42	-277
Pearland	484	-84	-9	74	264
Richmond / Rosenberg	82	-15	51	47	71
River Oaks	47	-17	-19	14	24
San Jacinto / Galena Park	8	42	17	4	-32
Sharpstown / Westwood	477	762	-23	-637	-500
Sheldon	3	0	1	-5	-7
Spring	44	18	-11	-24	24
Spring Branch	-17	265	-50	-2	-107
Steeplechase	444	-9	90	232	129
Sugarland / Fort Bend	670	102	-93	1	-12
Texas City / Dickinson	234	33	48	-83	10
Tomball	44	-4	-29	-13	19
Westchase	359	32	-89	-263	-71
Woodlake	337	435	-95	-12	13
The Woodlands	209	-138	-114	12	151

Occupancy

Throughout 2004, Houston apartment occupancy levels were trending downward. This occurred as a result of overbuilding in the market, sluggish job growth, and record low mortgage rates. Occupancy bottomed out in the first quarter of 2005 at 86.33%. The market posted small gains during the second quarter of 2005 as Houston’s economic situation strengthened. In September, the effects of Hurricane Katrina on the apartment market came to light, as occupancy immediately jumped more than three percentage points in one month, climbing above the 90% mark to 90.41%. As evacuees made their way out of hotels, shelters, and friends’ homes, with many taking advantage of the 12-month apartment voucher program, occupancy continued to climb over the next three months. Occupancy peaked in December, during the fourth quarter of 2005, at 91.69%. Since then, as many evacuees with the financial ability have made their way back home, occupancy has steadily declined. During the first quarter of 2006 occupancy registered 91.06%; overall occupancy fell further to 90.28% during the second quarter of 2006. Third quarter 2006 figures indicate that occupancy has once again fallen below the 90% mark, to 89.75%.



Occupancy trends by class are illustrated in the graphs below.



Hurricane Katrina affected all classes of Houston’s multifamily market. Corporations were quick to sign leases in Class A apartments for their displaced employees immediately following the Hurricane. Individuals and families with financial means also leased a large amount of Class A apartments, some under the Houston voucher program, which essentially paid a portion of the rent and allowed the household to pay any additional rent not covered by the voucher. Most voucher holders leased units in Class B and C apartments, as the rents in those apartments were low enough to be mostly covered by the voucher.

After the Hurricane, quarterly occupancy in the Class A market jumped a staggering 6.25 points, from 87.56% in the second quarter of 2005 to 93.81% in the third quarter of 2005. Class B occupancy increased 3.23 points, from 87.97% to 91.20%; Class C occupancy gained 2.30 points, from 85.56% to 87.86%; while Class D occupancy nudged up 0.45 points, from 82.21% to 82.66%.

After the initial jolt, Class A occupancy declined from its high of 93.81% in the third quarter of 2005 to 93.00% in the fourth quarter of 2005. Occupancy continued to decline over the first quarter of 2006 to 91.08%, and fell further to 90.96% in the second quarter of 2006. Class A occupancy rebounded in the third quarter of 2006 and is now at 92.04%. The recent occupancy increase is likely not attributable to the hurricane evacuees, but is a result of Houston's improving overall economic situation including moderate job growth figures, slightly elevated mortgage rates, multiple recently completed apartment complexes, as well as an increase in the amount of concessions being offered, especially at the new complexes which are offering lease-up specials.

The Class B market, which is where the majority of the vouchers were used, posted further occupancy gains after the initial jolt. Class B occupancy went from 91.20% in the third quarter of 2005 to 92.63% in the fourth quarter of 2005. Since then Class B occupancy has steadily declined; occupancy in the first quarter of 2006 was at 91.90%, in the second quarter of 2006 occupancy registered 91.14%, and in the third quarter of 2006 occupancy was at 90.53%.

Similar to what happened in the Class B market, Class C occupancy posted further gains after the initial jump in occupancy. Class C occupancy went from 87.86% in the third quarter of 2005, to 90.34% in the fourth quarter of 2005, and up further to 90.59% in the first quarter of 2006. Occupancy then dipped to 89.31% in the second quarter of 2006, and is now at 87.57%.

Class D saw the least amount of gains, with occupancy going from 82.66% in the third quarter of 2005 to 84.76% in the fourth quarter, and peaking at 85.69% in the first quarter of 2006. During the second quarter occupancy declined to 84.67%, and declined further in the third quarter of 2006 to 84.63%.

Submarket Occupancy

In regard to submarket occupancy, occupancy gains were made in 50 of the 54 submarkets during the quarter immediately following the hurricane. Of those, 37 submarkets had gains of greater than 2 points, 17 submarkets registered gains of more than 5 points, while 2 submarkets had gains greater than 8 points. After the dramatic increase over the third quarter of 2005, occupancy increased further over the fourth quarter. Comparing occupancy from before the hurricane to the fourth quarter of 2005, 37 submarkets had gains of greater than 2 points, 22 submarkets had gains of greater than 5 points, and 5 submarkets had gains greater than 8 points.

The submarkets registering the largest increases in occupancy from the quarter prior to the hurricane to the fourth quarter of 2005, which was when overall occupancy peaked, include: Inwood at 12.15 points, Midtown at 11.03 points, Baytown at 9.99 points, FM 1960 East at 8.40 points, Katy at 8.34 points, Friendswood at 7.98 points, Sugar Land/Fort Bend at 7.64 points, the Medical Center at 7.51 points, Highway 288/Almeda at 7.46 points, Alief at 7.38 points, Far West at 7.34 points, Northline/Aldine at 6.80 points, Greenspoint at 6.76 points, Brookhollow at 6.08 points, and Northshore/Woodforest at 6.05 points. Many of these submarkets are considered to be lower income areas of Houston, in particular the Inwood, FM 1960 East, Highway 288/Almeda, Alief, Northline/Aldine, Greenspoint, Brookhollow, and Northshore/Woodforest submarkets. The concentration of Class B and C properties in these submarkets is at 78% or greater.

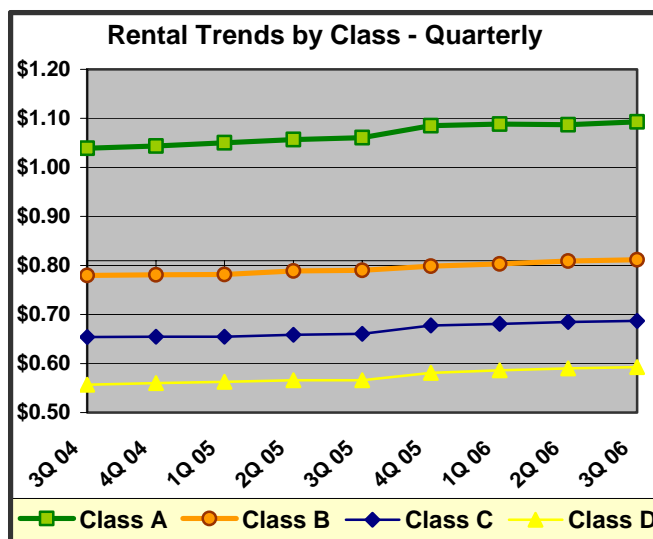
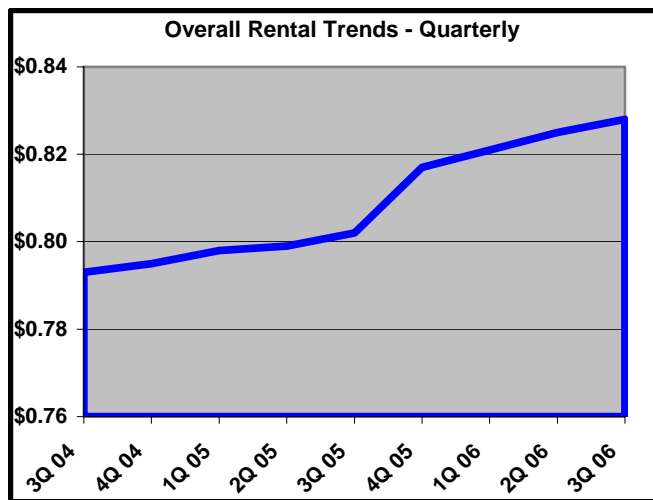
Third quarter 2006 figures indicate that occupancy has trended downward in the majority (31 of 54) of submarkets over the last year since Hurricane Katrina. The following chart shows the trends in occupancy by submarket from the quarter prior to the hurricane through the current quarter.

Occupancy By Submarket	2Q05	3Q05	4Q05	1Q06	2Q06	3Q 06
Alief	84.90%	87.93%	92.28%	91.84%	90.23%	88.18%
Baytown	78.60%	83.41%	88.59%	89.89%	87.43%	84.16%
Bear Creek / Copperfield	89.64%	94.65%	94.04%	93.25%	92.00%	93.12%
Bellaire / West University	94.97%	97.21%	97.79%	96.93%	97.17%	96.26%
Braeswood	85.13%	87.61%	90.96%	91.05%	89.65%	87.21%
Brazosport	86.02%	87.94%	87.93%	87.74%	87.36%	86.89%
Brookhollow	83.13%	86.47%	89.21%	89.64%	86.70%	85.28%
Bryan / College Station	96.00%	87.00%	92.69%	90.36%	88.18%	94.16%
Champions – East	85.45%	87.21%	90.53%	90.62%	89.38%	88.01%
Champions – West	86.93%	92.39%	90.81%	88.85%	89.72%	91.01%
Clear Lake / League City	89.19%	90.94%	91.00%	89.80%	90.59%	89.41%
Conroe	89.16%	89.95%	88.66%	87.90%	88.38%	89.37%
Deer Park	85.65%	93.04%	91.08%	88.36%	91.17%	90.32%
Downtown	92.40%	95.46%	94.07%	94.03%	95.12%	91.83%
Far West	85.55%	91.81%	92.89%	91.56%	88.47%	86.64%
FM 1960 East	82.97%	88.75%	91.37%	88.48%	89.04%	89.35%
Friendswood	87.80%	95.47%	95.78%	95.49%	93.08%	94.26%
Galleria	89.26%	94.17%	94.27%	92.36%	92.74%	92.70%
Galveston	89.76%	94.91%	93.87%	90.25%	91.36%	91.07%
Greenspoint	83.94%	88.67%	90.70%	91.38%	92.07%	90.20%
Greenway Plaza	93.60%	96.34%	95.12%	93.36%	94.26%	94.42%
Gulf Freeway	87.84%	91.01%	91.70%	91.10%	88.03%	89.40%
Gulfton	87.59%	89.09%	91.68%	92.10%	92.39%	92.03%
Heights	84.86%	92.15%	87.78%	89.41%	93.05%	94.17%
Highway 288 / Almeda	89.00%	93.10%	96.46%	96.11%	90.33%	94.78%
Inner Loop East	86.37%	87.24%	88.12%	87.81%	88.30%	86.32%
Inner Loop West	92.66%	95.96%	96.61%	96.06%	95.77%	96.18%
Inwood	73.71%	82.41%	85.86%	89.72%	86.18%	85.26%
Katy	84.43%	93.11%	92.77%	92.14%	91.61%	93.24%
Kingwood / Lake Houston	88.19%	91.02%	93.10%	91.65%	91.46%	92.27%
Medical Center	86.90%	93.98%	94.41%	92.73%	91.64%	93.53%
Meyerland	89.99%	90.99%	91.90%	90.23%	90.34%	88.70%
Midtown	83.98%	90.66%	95.01%	92.72%	91.60%	90.33%
Montrose / Memorial Heights	95.77%	97.93%	96.00%	95.26%	95.51%	86.14%
Museum District	89.74%	91.87%	88.67%	91.15%	91.29%	93.69%
North Loop – East	88.11%	94.21%	91.75%	91.78%	88.91%	89.37%
Northline / Aldine	85.66%	90.79%	92.46%	92.73%	93.33%	91.61%
Northshore / Woodforest	83.90%	85.80%	89.95%	88.29%	87.63%	87.80%
Pasadena	88.33%	89.38%	89.41%	90.13%	89.80%	88.22%
Pearland	81.16%	88.36%	86.74%	86.44%	84.46%	90.37%
Richmond / Rosenberg	92.39%	91.63%	91.09%	87.15%	88.68%	90.69%
River Oaks	93.14%	96.48%	95.27%	93.91%	94.59%	96.20%
San Jacinto / Galena Park	92.60%	84.62%	89.79%	92.08%	92.55%	88.85%
Sharpstown / Westwood	86.85%	88.71%	91.82%	91.71%	89.22%	87.21%
Sheldon	92.84%	96.55%	96.55%	97.96%	92.29%	85.91%
Spring	93.31%	94.53%	95.03%	94.76%	94.21%	94.79%
Spring Branch	88.99%	88.94%	90.63%	90.34%	90.32%	89.58%
Steeplechase	88.16%	90.13%	89.96%	88.64%	90.55%	90.68%
Sugarland / Fort Bend	86.19%	92.80%	93.83%	92.97%	92.98%	92.86%
Texas City / Dickinson	85.33%	89.96%	90.63%	91.57%	89.89%	90.10%
Tomball	90.61%	93.60%	94.39%	92.47%	91.99%	92.88%
Westchase	88.80%	91.46%	92.73%	92.08%	90.37%	89.93%
Woodlake	88.54%	94.01%	94.44%	93.10%	92.99%	93.22%
The Woodlands	92.25%	93.77%	93.55%	91.17%	90.07%	92.61%

Rental Rates

Rental rates naturally trend upward over time due to inflation and rising costs of living. From the third quarter of 2004 through the third quarter of 2005, overall rents in Houston increased 1.13%, from \$0.793 per square foot (psf) to \$0.802 psf. Although Hurricane Katrina occurred during the third quarter of 2005, rental rates did not register a significant hike until the fourth quarter, where rents jumped 1.87% (from \$0.802 psf to \$0.817 psf) over the single quarter. The rental increase occurred in response to the spike in occupancy during the third quarter. As area apartments filled up, properties were able to increase their rental rates. Since the spike, rents have continued to increase, though at a slower pace. From the fourth quarter of 2005 to the third quarter of 2006, rents have risen 1.35%, which is consistent with Houston’s natural rate of rental increases.

Within each of the classes, rents also registered a spike during the fourth quarter of 2005. Class A rents increased 2.26% from \$1.061 to \$1.085 psf; Class B rents gained 1.14% from \$0.790 psf to \$0.799 psf; Class C rents jumped 2.57%, from \$0.661 psf to \$0.678 psf; while Class D rents gained 2.65%, from \$0.566 psf to \$0.581 psf. Since then, rents in all classes have continued to increase at their natural rates.



Submarket Rents

In regards to submarket rental rates, 39 of Houston’s 54 submarkets registered greater than a 1% increase, while 18 submarkets reported gains of greater than 2% from the third quarter of 2005 to the fourth quarter of 2005, which was when overall rents spiked. The submarkets reporting the greatest gains over the fourth quarter of 2005 include: Midtown at 4.89%, River Oaks at 4.02%, The Woodlands at 3.84%, Baytown at 3.56%, Northline/Aldine at 3.54%, Sharpstown/Westwood at 3.23%, Museum District at 2.88%, Inwood at 2.62%, Richmond/Rosenberg at 2.60%, and Braeswood at 2.52%. It is noteworthy, that the highest rent gains occurred in all areas of Houston. Of the ten submarkets with the highest rental increases, four are in what are generally characterized as affluent, high-income neighborhoods (Midtown, River Oaks, The Woodlands, and Museum District), two are in middle-income suburban communities (Baytown and Richmond/Rosenberg), while four are in what are mostly considering lower-income neighborhoods (Northline/Aldine, Sharpstown/Westwood, Inwood, and Braeswood).

The following chart shows the quarterly rental trends by submarket over the last year.

Rent By Submarket	3Q05	4Q05	1Q06	2Q06	3Q06
Alief	\$0.729	\$0.742	\$0.745	\$0.750	\$0.750
Baytown	\$0.675	\$0.699	\$0.696	\$0.698	\$0.699
Bear Creek / Copperfield	\$0.849	\$0.851	\$0.857	\$0.860	\$0.866
Bellaire / West University	\$1.073	\$1.094	\$1.094	\$1.105	\$1.111
Braeswood	\$0.675	\$0.692	\$0.695	\$0.702	\$0.704
Brazosport	\$0.665	\$0.675	\$0.676	\$0.684	\$0.691
Brookhollow	\$0.700	\$0.715	\$0.719	\$0.724	\$0.726
Bryan / College Station	\$0.583	\$0.769	\$0.776	\$0.785	\$0.787
Champions – East	\$0.768	\$0.781	\$0.775	\$0.788	\$0.793
Champions - West	\$0.883	\$0.879	\$0.885	\$0.867	\$0.868
Clear Lake / League City	\$0.880	\$0.879	\$0.878	\$0.882	\$0.883
Conroe	\$0.763	\$0.771	\$0.783	\$0.795	\$0.796
Deer Park	\$0.709	\$0.705	\$0.703	\$0.718	\$0.717
Downtown	\$1.624	\$1.441	\$1.439	\$1.439	\$1.535
Far West	\$0.847	\$0.864	\$0.872	\$0.879	\$0.883
FM 1960 East	\$0.757	\$0.768	\$0.769	\$0.770	\$0.771
Friendswood	\$0.814	\$0.806	\$0.807	\$0.814	\$0.820
Galleria	\$0.997	\$1.022	\$1.026	\$1.027	\$1.031
Galveston	\$0.867	\$0.853	\$0.860	\$0.866	\$0.867
Greenspoint	\$0.689	\$0.700	\$0.709	\$0.717	\$0.716
Greenway Plaza	\$1.122	\$1.139	\$1.141	\$1.144	\$1.144
Gulf Freeway	\$0.723	\$0.741	\$0.740	\$0.750	\$0.749
Gulfton	\$0.692	\$0.705	\$0.709	\$0.712	\$0.718
Heights	\$1.105	\$1.029	\$1.037	\$1.039	\$1.022
Highway 288 / Almeda	\$0.789	\$0.792	\$0.789	\$0.782	\$0.794
Inner Loop East	\$0.739	\$0.754	\$0.790	\$0.792	\$0.793
Inner Loop West	\$1.019	\$1.029	\$1.037	\$1.045	\$1.050
Inwood	\$0.686	\$0.704	\$0.705	\$0.706	\$0.707
Katy	\$0.871	\$0.886	\$0.890	\$0.898	\$0.907
Kingwood / Lake Houston	\$0.893	\$0.904	\$0.907	\$0.903	\$0.909
Medical Center	\$0.976	\$0.987	\$0.991	\$0.988	\$0.998
Meyerland	\$0.911	\$0.928	\$0.928	\$0.940	\$0.940
Midtown	\$1.391	\$1.459	\$1.521	\$1.515	\$1.516
Montrose / Memorial Heights	\$1.298	\$1.231	\$1.232	\$1.239	\$1.239
Museum District	\$1.076	\$1.107	\$1.106	\$1.115	\$1.120
North Loop - East	\$0.741	\$0.739	\$0.740	\$0.744	\$0.759
Northline / Aldine	\$0.650	\$0.673	\$0.684	\$0.688	\$0.687
Northshore / Woodforest	\$0.745	\$0.755	\$0.754	\$0.758	\$0.761
Pasadena	\$0.688	\$0.698	\$0.704	\$0.705	\$0.705
Pearland	\$0.890	\$0.906	\$0.910	\$0.912	\$0.920
Richmond / Rosenberg	\$0.768	\$0.788	\$0.787	\$0.787	\$0.785
River Oaks	\$1.270	\$1.321	\$1.323	\$1.322	\$1.332
San Jacinto / Galena Park	\$0.651	\$0.664	\$0.668	\$0.672	\$0.681
Sharpstown / Westwood	\$0.651	\$0.672	\$0.675	\$0.678	\$0.680
Sheldon	\$0.749	\$0.760	\$0.760	\$0.760	\$0.760
Spring	\$0.824	\$0.829	\$0.834	\$0.836	\$0.840
Spring Branch	\$0.680	\$0.697	\$0.698	\$0.706	\$0.711
Steeplechase	\$0.885	\$0.901	\$0.894	\$0.903	\$0.903
Sugarland / Fort Bend	\$0.896	\$0.915	\$0.922	\$0.923	\$0.931
Texas City / Dickinson	\$0.715	\$0.729	\$0.735	\$0.745	\$0.745
Tomball	\$0.825	\$0.831	\$0.836	\$0.840	\$0.840
Westchase	\$0.870	\$0.880	\$0.882	\$0.886	\$0.888
Woodlake	\$0.904	\$0.899	\$0.906	\$0.907	\$0.911
The Woodlands	\$0.937	\$0.973	\$0.972	\$0.976	\$0.983

Future Expectations in Houston

Population Expectations

Over the last year since Hurricane Katrina and subsequent levee breach, rebuilding, albeit at a slow pace, has occurred in New Orleans. Currently, many areas in New Orleans are operational and livable, as numerous households have returned to repair their homes, city services have been restored to certain areas, businesses have returned, retailers have reopened their doors, and restaurants have reopened. In addition, many schools are now operational; over 200 parochial schools and 54 public schools have reopened. Considering the state of New Orleans, we believe that it is in all likelihood that the majority of middle-to-upper income households that had the financial ability and desire to return to their homes in New Orleans already have returned. A significant proportion of evacuees, however, have yet to return as it is estimated that 120,000 evacuees remain in Houston a full year after Hurricane Katrina and the evacuation of New Orleans.

Of those 120,000, an estimated 50,000, or roughly 40% of the evacuees that remain in Houston, continue to receive rental assistance from FEMA. The remaining 60% are supporting themselves and have decided to stay in Houston for various reasons including job opportunities, school districts, housing situation, etc. Those that remain in Houston on FEMA rental assistance are mainly low-income families that do not have the means to return to New Orleans and have no other housing options. In a recent survey by professors Rick Wilson and Robert Stein of Rice University, 75% of those evacuees living in apartments have household incomes below \$25,000, 33% have less than a high school education, while 70% are still unemployed. The survey also indicated that 69% intend to remain in Houston long-term. As the data indicates, these are very low-income households that are still in Houston and that plan to remain in Houston, and will likely create a burden on city and state welfare services. Based on various reports and our best estimations, we expect around 60% of the 120,000 evacuees still in Houston, or approximately 70,000 people, to remain in Houston long-term.

Houston Apartment Market Expectations

Hurricane Katrina caused unprecedented spikes in absorption and occupancy, as well as boosting rental rates in the Houston multifamily market. The increases, in occupancy and absorption in particular, were short lived. Demand has been negative over the last three quarters, while occupancy has once again fallen below the 90% mark.

The voucher program, which allowed evacuee households to live rent- and utility-free for twelve months, was a huge demand driver. According to a report released by the Joint Hurricane Housing Task Force Communications Team, 37,000 households, approximately 156,000 people, moved into Houston area apartments on the voucher program. Over the last year, many people have left their Houston area apartments and either returned to New Orleans or settled elsewhere. There currently remain 15,000 households, or roughly 50,000 individuals, still receiving some form of rental assistance from FEMA. Although multiple FEMA deadlines have come and gone, they are adamant that all benefits for Katrina evacuees will cease after February 2007.

In our opinion, it is expected that FEMA will go ahead and cut off reimbursement for the apartment vouchers by their February 2007 deadline, as they will have fulfilled more than the original twelve-month obligation. The Class A market, which is currently in better shape than the other markets, will be considerably less volatile than the Class B and C markets over the coming months, considering very few vouchers were used to rent Class A apartments. The termination of FEMA rental assistance will have the greatest effect on the Class B and C markets, which is where the vast majority of evacuees rented apartments. In the Class B and C markets, we expect to see continued negative absorption levels, with significant negative absorption in March 2007, after the

final FEMA deadline expires. Absorption in March 2007 is expected to be around -3,500 units, with the possibility of figures in the -5,000 to -7,000 range.

Though many households will not be able to fulfill their current rental obligations on their own once rental assistance expires and will have to leave their apartments, which will in turn cause the steep negative absorption figures in March 2007, there will be many households that will be able to meet their rent obligations either through their own volition or through qualification for the tax-credit programs. We do not expect the termination of FEMA rental assistance to cause mass homelessness, as there are many local representatives that are looking and working to prevent that from happening, especially in their own districts. Of those households that will be vacating their apartments once FEMA rental assistance expires, there will likely be a significant portion that qualify and end up on government assistance and in public housing in the Greater Houston area, which will undoubtedly tax the system and strain resources. There will also likely be significant amount of households that choose return to New Orleans upon the termination of benefits in Houston.

Houston multifamily occupancy has been on the decline over the last three quarters. With the upcoming FEMA deadline looming, we expect overall occupancy to decline even further. The greatest effects will likely be seen in the Class B and C markets, which absorbed most of the voucher-holding households. The Class A market will likely be minimally affected with regards to any more hurricane repercussions, as it is expected that those evacuees that rented Class A apartments that wanted to return to New Orleans, have already done so. We expect occupancy in the Class A market to decline slightly over the next quarter, which is consistent with normal market trends during the winter months, and that it will subsequently stabilize around 90% to 91%. We expect occupancy levels in the Class B and C markets will continue to decline, with a sharp decline expected in March 2007 as FEMA rental assistance for Katrina evacuees expires at the end of February 2007. After the expected sharp decline in March 2007, occupancy will likely remain depressed for a short time and then begin to slowly increase, stabilizing near their pre-Katrina levels.

The following table includes current occupancy figures, and our projections for the Houston apartment market for March 2007, after FEMA rental assistance expires, and for one year out in September 2007.

Occupancy Projections

Occupancy	Class A	Class B	Class C	Class D	Overall
September 2006	92.04%	90.53%	87.57%	84.63%	89.75%
March 2007	91.46%	87.84%	85.28%	84.11%	88.00%
September 2007	90.88%	88.96%	87.38%	85.07%	89.05%

As the effects of Katrina on the Houston apartment market greatly diminish, a lasting lesson on the necessity of proper planning has been learned by all. Living near the Gulf, where hurricanes threaten the coast every season, all cities need an effective pre-disaster and post-disaster response plan. Further, all businesses and individual families need to be prepared with their own emergency plans. Though not everything can be truly prepared for, we are all hopeful that if there is a next time around, we are at least in a better position to avoid another tragedy like what transpired in New Orleans last year.