

Houston Apartment Market Update

Edited by Kathryn Koepke

\$399/year

2nd Quarter 2006

If you build it, will they come?

Construction activity has picked up yet again following a brief reprieve in 2005. In 2004, 5 years after 64 projects with nearly 20,000 units entered the apartment market in 1999, construction activity peaked again. 48 projects with 16,800 units were introduced to the market in 2004. In 2005, construction activity weakened slightly as 28 projects totaling 13,687 units were developed. 2006 is promising to be another active year, as half way through the year, 10 projects with 3,454 units were already completed, and an additional 28 projects containing 11,795 units are underway.

Houston's Far West sector is bringing the most units to the apartment market with four projects and 1,120 units under construction. In addition to those being constructed, two more projects totaling 682 units are proposed for the area after already adding over 2,800 units in the past three years. The ever-expanding Woodlands area continues its steady pace of apartment construction as 918 units are currently underway, and upon completion, will have added just over 3,000 units in the past five years. After a short development pause in 2005, Midtown is seeing growth again as 989 units are under construction by Camden Property Trust, including the City Center development. An additional 625 units are proposed for the area as well.

With all of their activity in Midtown, Camden is currently the most active developer, leading the market with nearly 1,500 units currently under construction in various parts of town. 236 units are being constructed as Royal Oaks in the Far West sector, and 271 units are going up as Camden Plaza in the Greenway Plaza area. Sueba is next in line as the city's busiest developer with just under 700 units currently under construction. Their projects include the 372-unit San Paloma development in the Far West sector and the 324-unit Vintage Park in the Champions West area. Trammell Crow Co. is also making significant contributions to the market with 678 units in two of their Alexan brand developments, Cityside in the Medical Center and Bunkerhill in the Spring Branch area.

The combination of aggressive development and further Katrina evacuee vacancies will undoubtedly contribute to the increasing softness of the Houston apartment market. Over the second quarter, record levels of negative absorption were posted, and occupancy continued to slip. The influx of new units in the market will likely push occupancy numbers back to the pre-Katrina numbers if not even lower.

By: [Melissa Ray](#)

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O'Connor & Associates now offers online apartment market and property data in all four major Texas markets, Austin, DFW, Houston, and San Antonio. Brokers, lenders, investors, owners, and apartment vendors have relied on our superior research and accurate data for over decades!

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Houston Apartment Market at a Glance

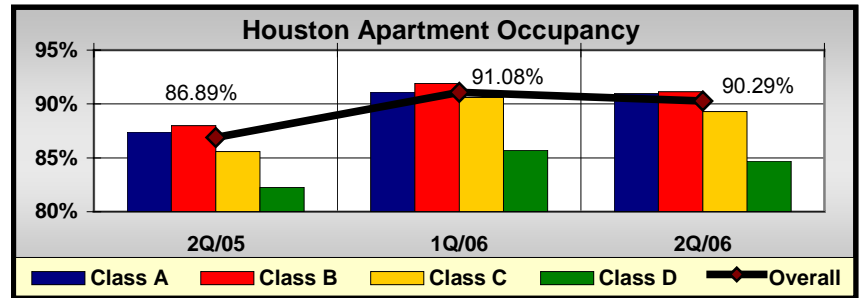
	Class A	Class B	Class C	Class D	Overall	Qtr	Yr
Occupancy	90.95%	91.14%	89.31%	84.70%	90.29%	▼	▲
Rent/Unit	\$1,025	\$657	\$555	\$520	\$702	▲	▲
Rent/SF	\$1.087	\$0.809	\$0.685	\$0.590	\$0.825	▲	▲
Absorption	324	-469	-1,751	-230	-2,126	▼	▼



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Metro Occupancy Overview

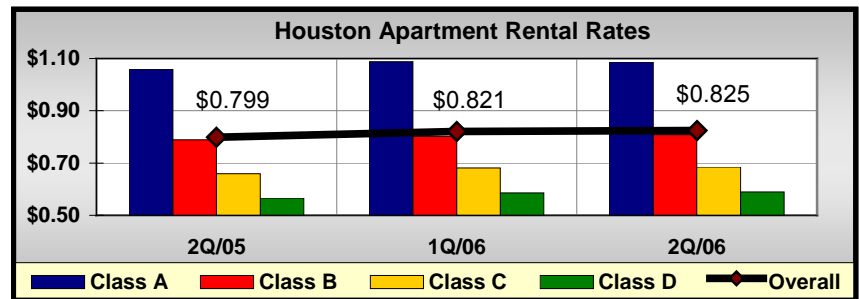
Overall occupancy decreased for the third consecutive quarter, falling 0.79 points to 90.29% over the second quarter with all classes of apartments posting decreases. **Class A** occupancy dropped 0.16 points over the quarter to 90.95%, but is still up 3.55 points from the previous year. **Class B** occupancy declined by 0.77 points to 91.14% but continues to carry the highest occupancy of the classes. The **Class C** market had the greatest decrease in occupancy as it fell 1.29 points and is now at 89.31%, which is 3.72 points above occupancy levels from last year. **Class D** occupancy dropped a full point over the quarter from 85.70% to 84.70%, but remains 2.45 points above levels this time last year.



Quarter	Class A	Class B	Class C	Class D	Overall
2Q/05	87.40%	87.98%	85.59%	82.25%	86.89%
1Q/06	91.11%	91.91%	90.60%	85.70%	91.08%
2Q/06	90.95%	91.14%	89.31%	84.70%	90.29%

Metro Rent Overview

Overall rental rates for the Houston apartment market continued to post steady increases as rents were up \$0.004 per square foot (psf) over the quarter and \$0.026 psf over the year. **Class A** apartments recorded the only decrease in rents over the quarter, though minimal, losing \$0.001 psf and are now at \$1.087. **Class B** rents posted the largest quarterly increase with \$0.006 psf, and at \$0.809 psf, are \$0.020 psf higher than last year. The **Class C** market gained \$0.004 psf in rental rates over the quarter, and are up \$0.026 psf over the year to \$0.685 psf. **Class D** rents also gained \$0.004 psf over the quarter bringing rents to \$0.590 psf, which is \$0.024 psf higher than this time last year.



Quarter	Class A	Class B	Class C	Class D	Overall
2Q/05	\$1.058	\$0.789	\$0.659	\$0.566	\$0.799
1Q/06	\$1.088	\$0.803	\$0.681	\$0.586	\$0.821
2Q/06	\$1.087	\$0.809	\$0.685	\$0.590	\$0.825

Submarket Performance

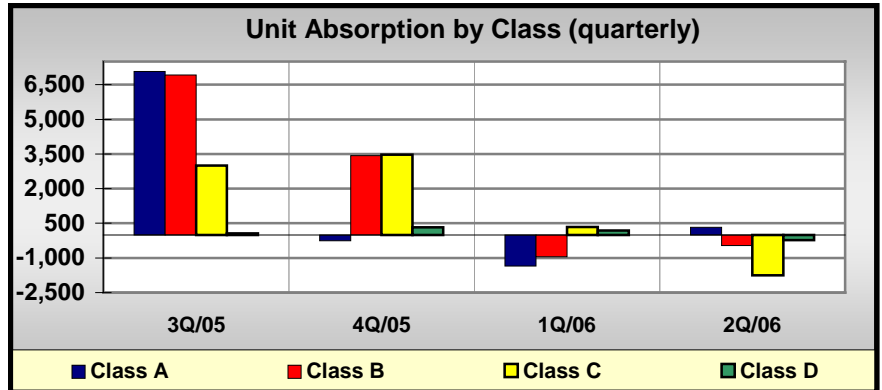
Of the 53 Houston submarkets, overall occupancy was highest in the **Inner Loop West** submarket at 95.77%, while the lowest occupancy was found in **Pearland** at 84.46%. The highest overall rental rates were found in the **Midtown** submarket at \$1.515 psf, while the lowest rents were found in **San Jacinto/ Galena Park** at \$0.672 psf.

Of the submarkets with more than one property, **Deer Park** reported the highest Class A occupancy at 99.00%, while the lowest Class A occupancy was reported by **Conroe** at 75.13%. In the Class B market, **Montrose/Memorial Heights** reported the highest occupancy at 99.05%, while **Brookhollow** posted the lowest occupancy at 86.10%. In the Class C market, **Highway 288/Alameda** recorded the highest occupancy at 98.45%, while **Far West** reported the lowest occupancy at 80.08%. In the Class D market, **Conroe** reports the highest occupancy at 100.00%, with **North Shore/Woodforest** reporting the lowest occupancy at 59.09%.

Of the submarkets with more than one property, **Downtown** reported the highest Class A rents at \$1.773 psf, while the lowest Class A rents were found in **Texas City/Dickinson** at \$0.857 psf. In the Class B market, rental rates were the highest in **River Oaks** at \$1.040 psf, while the lowest rents were found in **Montrose/Memorial Heights** at \$0.663 psf. Class C rents were the highest in **The Woodlands** at \$0.994 psf and the lowest were found in **Brazosport** at \$0.614 psf. In the Class D market, **Highway 288/Alameda** reported the highest rents at \$0.782 psf, while the lowest rents were found in **Pasadena** at \$0.514 psf.

Metro Absorption Overview

Overall absorption for the Houston apartment market posted the weakest quarterly showing on record with -2,123 units absorbed over the quarter. Annual absorption was also weaker than this time last year, though remained in the black with 20,125 units absorbed. **Class A** apartments were the only market to show positive absorption over the quarter as they absorbed 324 units, leaving annual at 5,789 units. The **Class B** market posted -469 units of absorption for the quarter. Class B annual absorption was the strongest with 8,925 units absorbed. **Class C** absorption was the weakest over the quarter, absorbing -1,751 units. Annual absorption for the class remains positive with 5,058 units absorbed. The **Class D** market posted weak numbers in quarterly and annual absorption with negative 230 units absorbed over the quarter, and 353 units absorbed over the year.



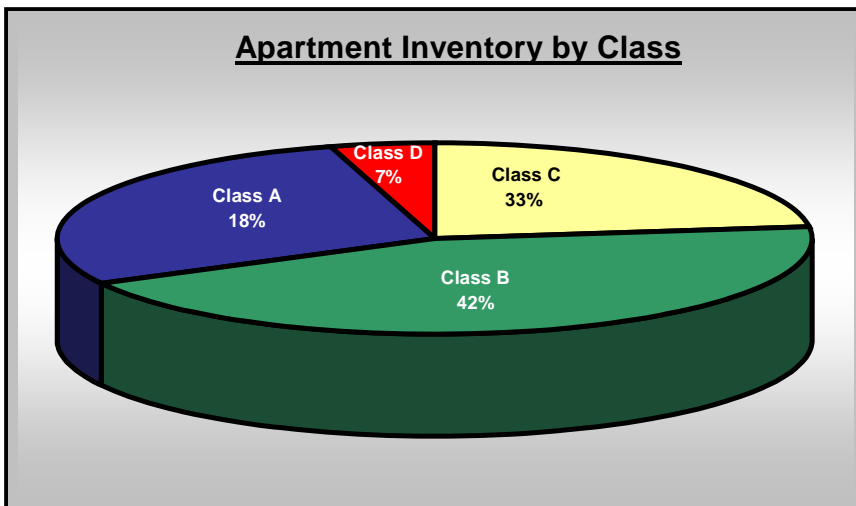
12-mo Ending	Class A	Class B	Class C	Class D	Overall
2Q/04	5,556	-1,412	-4,297	-413	-566
2Q/05	8,155	247	-2,523	-721	5,158
2Q/06	5,789	8,925	5,058	353	20,125

Submarket Performance

Of the 53 Houston submarkets, **Steeplechase** reported the strongest absorption over the quarter with 232 units absorbed. Demand was weakest in **Sharpstown**, where -637 units were absorbed. The **Gulf Freeway** also recorded soft quarterly absorption, as -534 units were absorbed. Within each of the classes, **Champions West** reported the strongest Class A absorption over the quarter with 187 units absorbed, while **Champions East** reported the weakest absorption with -234 units absorbed. In the Class B market, **Deer Park** posted the strongest absorption, as 119 units were absorbed over the quarter. **Gulf Freeway** posted the weakest Class B absorption, with -172 units absorbed. Class C absorption was strongest in **Gulfton**, with 93 units absorbed, and weakest in **Sharpstown**, with -549 units absorbed. Absorption in the Class D market over the quarter was strongest in **Pasadena** with 65 units absorbed and weakest in the **Gulf Freeway** with -144 units absorbed.

Apartment Inventory

There are a total of 2,513 operating or under-construction projects in the Houston area market (greater than 25 units) with a total of 503,529 units. Approximately 23% of the total units are Class A, 44 are Class B, 28% is Class C, and 4% are Class D. The chart below displays market inventory by class.



Operating	Projects	Units
Class A	448	116,489
Class B	1,068	222,539
Class C	833	142,227
Class D	164	22,274
TOTAL	2,513	503,529

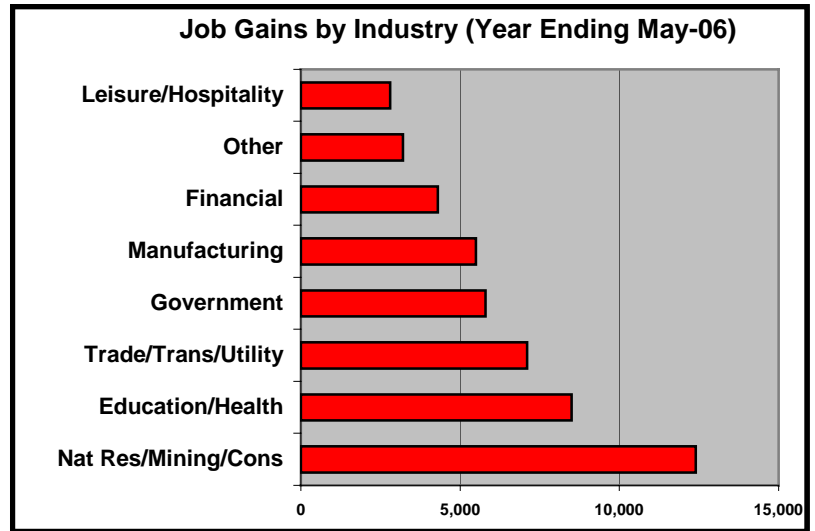
Under Cons.	Projects	Units
Class A	28	8,294
Class B *	20	3,313
TOTAL **	48	11,607

* Class B projects are primarily Tax Credit developments

** There are additional Unclassified (Class U) projects

Job Growth

The civilian labor force unemployment rate in the ten-county Houston MSA increased to 5.0%, while the total number of nonagricultural wage and salary jobs increased to 2,410,900 in May 2006, according to the **Texas Workforce Commission**. This month's total is 68,000 jobs more than at this time last year. Of the nonagricultural employers, Professional & Business Services gained 19,400 jobs over the previous 12 months; Natural Resources, Mining, & Construction gained 12,400 jobs; Education & Health Services is up 8,500 jobs; Trade, Transportation, & Utilities added 7,100 jobs; Government added 5,800 jobs; Manufacturing gained 5,500 jobs; Financial Activities gained 4,300 jobs; and Leisure & Hospitality added 2,800 jobs. The only industry to lose jobs over the year was the Information sector with -1,000 jobs. The largest monthly gain was in the Leisure & Hospitality industry driven by seasonal factors.

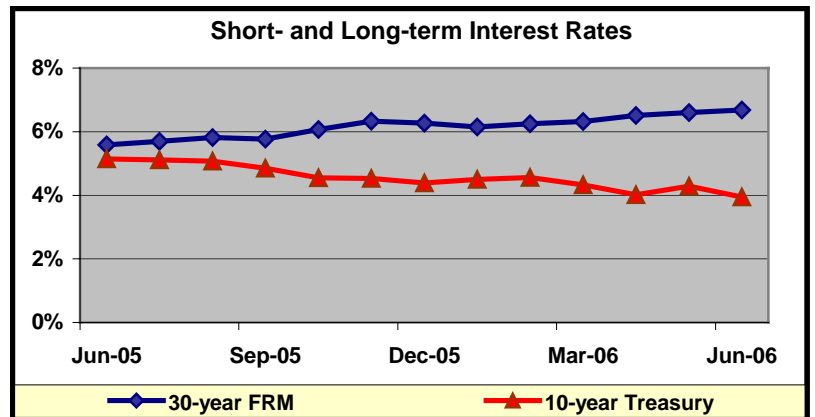


Interest Rates

The yield on the **10-year Treasury** note rose to 5.14% on the last Friday of June 2006, up 1.2 points from its 3.94% yield one year ago.

The **30-year fixed-rate mortgage (FRM)** averaged 6.68% in June 2006, the highest level since January 2002. One year ago, the 30-year FRM was at 5.58%. The average for the **15-year FRM** in June was 6.31%, the highest level since January 2002 and up 1.14 points from a year ago.

The **Prime Rate** in June was reported in the Wall Street Journal at 8.25%, up 2.00 points from a year ago. It is now at the highest rate since February 2001.



Apartment Data News Release

O'Connor & Associates is pleased to re-launch the **ApartmentLink**, the best online apartment data source in Texas, previously offered by **Monarch Data**. Some of the upgrades and enhancements made to the platform include:

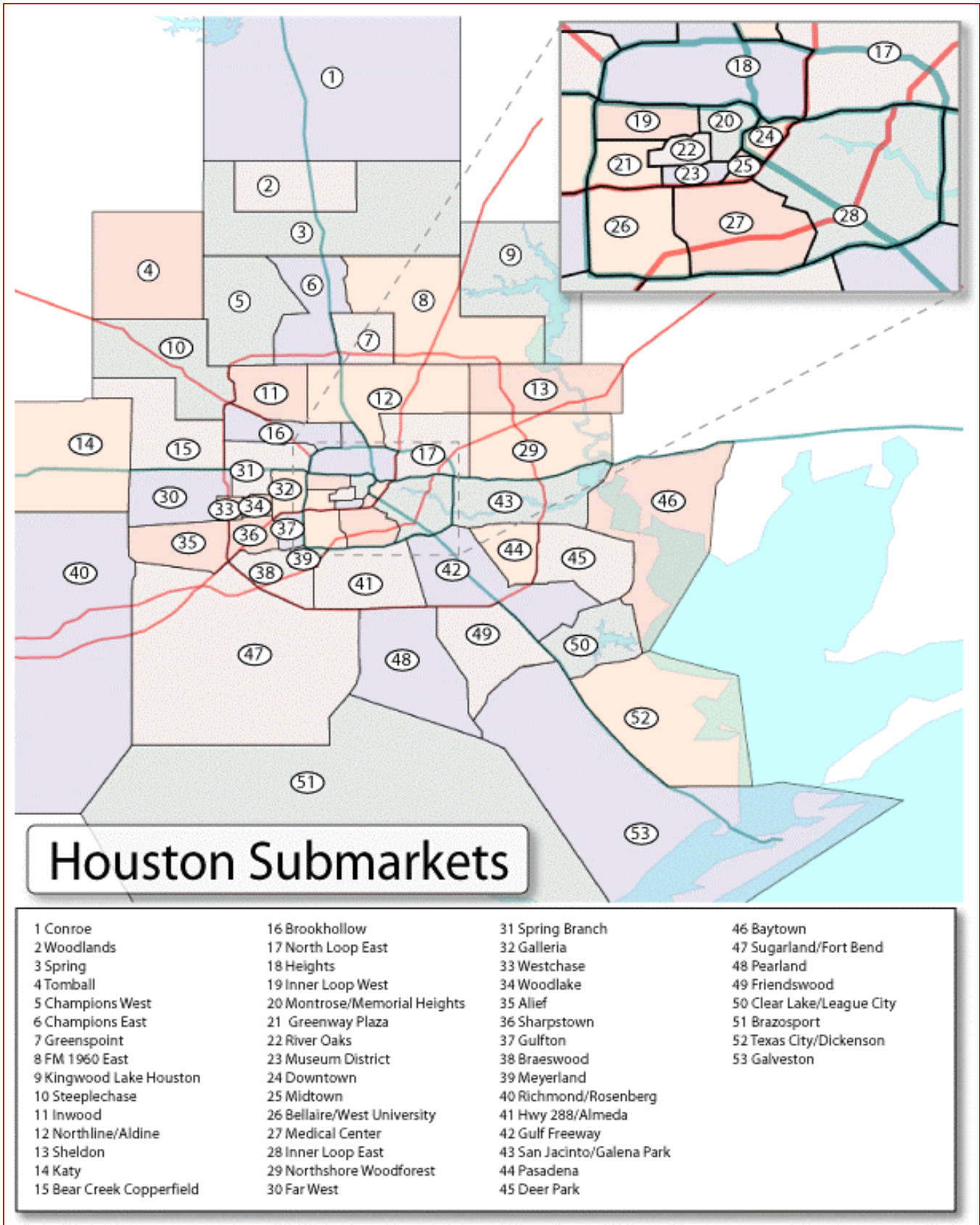
- ◆ Ownership Information
- ◆ More comprehensive data
- ◆ More search options
- ◆ More analytical reports
- ◆ More user-friendly
- ◆ Mapping & emailing options
- ◆ Excel exporting function
- ◆ Monthly updates, real-time data

All this and more now available at your fingertips from a company trusted by apartment industry leaders for over 30 years!

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Data Collection

Our in-house research team continuously updates over 100 fields of data for nearly 6,000 apartment complexes in our database. We update at least 90% of properties on a monthly basis to generate accurate market trend reports on rents, concessions, occupancy, etc. Our monthly surveys also update other property-specific data such as fees, policies, management, and owner information. On a less-frequent basis we update amenities, schools, and other data fields that change rarely. We perform current and historical data audit after we close each month's survey to identify any data inconsistencies or incorrectly keyed values.

Research

We monitor various news media, press releases, marketing materials, web-sites, CAD records, permit issuance, and other sources to capture new construction, planned projects, financing, and sales. Our researchers conduct phone interviews with relevant developers, brokers, or lenders to gather information on new construction and sales. We add properties to our database on a regular basis to ensure we offer the most up-to-date and complete apartment database.

Market Coverage

Our online apartment database covers all four major Texas metro markets – Austin, Dallas-Fort Worth, Houston, and San Antonio. The **Austin** market includes Caldwell, Hays, Travis, Bastrop, and Williamson counties. The **DFW** market covers Dallas, Tarrant, Wise, Denton, Collin, Hunt, Rockwall, Kaufman, Ellis, Johnson, Parker, and Erath counties. The **Houston** market includes Harris, Montgomery, Fort Bend, Brazoria, and Galveston counties (Brazos county is also included in the database but excluded from the trend reports). **San Antonio** includes Bexar, Comal, Guadalupe, Kendall and Kerr counties.

We subdivide each market into submarkets (see map on previous page): Austin has 23 submarkets, DFW has 50 submarkets, Houston has 53 submarkets, and San Antonio has 26 submarkets. The submarkets are based on neighborhood-style areas with defining boundaries such as major roads and other factors that establish a neighborhood. This approach allows the user to view distinct areas of properties that have evolved into their own sections of town and can be identified together.

Glossary

Absorption = Change of Occupied Units, including new construction. Absorption is a proxy for demand.

Occupancy = Percentage of physically occupied units on property.

Pre-leased = Net of percentage of units that have been pre-leased but not yet occupied and units on notice to be vacated.

Rents = Market rents (excluding concessions).

Class = Properties are classified as A, B, C, D, or Unclassified (U) based on various factors, such as age, location, amenities, curb appeal, overall condition, rents, etc. Class A properties are generally less than 10 years old, have excellent amenities, prime location, and great appeal, thus they tend to have the highest rents. Older properties built in early 1900s that were converted from warehouses or office buildings, or older apartment projects that have had major renovations may also be classified as A. Class B properties are generally 10 to 20 years old, have good locations, good level of amenities, are somewhat less appealing than Class A projects, and are in overall good condition. New affordable projects are also classified as B. Class C projects are usually 20 to 30 years old, have few amenities, are in poor locations, and are not well maintained. Class D projects are generally more than 30 years old, in poor condition, have no or limited amenities, are in poor locations, and have poor curb appeal. They tend to have the lowest rents per unit (although per-square-foot rents may be high since the units are usually small). Unclassified or Class U projects are senior housing, student housing, or other properties that have unusual lease terms, include meals with the rent, or other services, so their rents and occupancies are not representative of the actual market. We exclude these from our statistical reports as they skew the averages for the other classes.

Reporting

Occupancy, Rent, and Absorption trend data is based on Operating, Under-construction, and Under-renovation projects, Classes A, B, C, and D (excluding Class U).