

Demand for apartments remains high

If you’re looking for an upside to the squeeze on mortgage underwriting, it’s in the forecast for multifamily housing. When home sales cool, apartment activity heats up.

Last year, for example, domestic and foreign investors looked at the economic picture in Dallas and liked the prospects for multifamily housing. As a result, 190 complexes of more than 100 units each changed hands locally, the highest transaction total in a decade, according to Brian O’Boyle, partner at Apartment Realty Advisors in Dallas. Particularly convincing was a job-growth rate that led the nation.

Today the picture is equally attractive, with 75,000 new jobs expected by June, slightly down from a year ago, but factor in tougher rules for obtaining home mortgages and rental demand pick up.

“If you took 100 people who qualified for a home loan a year ago, maybe 60 to 70 would qualify today,” Mr. O’Boyle says. “A lot of people who were exiting the apartment market to enter single-family [homes] have seen that door close.”

In June 2006, the apartment occupancy rate in Dallas registered at 92.7 percent; this year, net leasing stands at 94 percent, the highest level in six years, according to analysts at M/PF YieldStar Inc.

Going forward, Mr. O’Boyle expects the demand for Class A and “better Class B” buildings to stay strong, though last year a seller who may have entertained 25 or 30 offers may see only 20 today.

“There’s still a significant appetite in our market because investors see an upside opportunity,” he says. “They know performance is tied heavily to new job formation, and all the signs are still in place: A relatively low cost of living, reasonable office lease rates, available skilled workforce, and affordable middle-class housing.”

Sales volume will likely slip somewhat this year as a result of recent disruptions in the financing market. In particular, the “meltdown” in Commercial Mortgage-Backed Securities (which fed financing) hurt Class C and B-minus deals, he says. “Financing for better properties is largely unaffected.”

The number of properties listed to date is slightly less than a year ago, probably because so many deals traded in 2006 when properties were closing at all-time low capitalization rates, he explains.

Though Mr. O’Boyle exclusively handles sales of complexes with more than 100 units, sales activity is equally steady for apartment buildings with only a few units, he says.

“There are no fire sales going on, in my opinion.”

Apartment construction added about 5,500 new units in Dallas so far this year, and that number outpaced those that came down: More than 3,500 older apartments were demolished in the first six months of the year.

Some of the aging buildings that can’t command market-rate rents wind up back in the lenders’ hands. Most of those are older, underperforming and “not your pride-of-ownership type properties,” says George Roddy Sr., president of Addison-based Foreclosure Listing Service. As of

September, lenders had taken back 18 apartment buildings this year, says Mr. Roddy. At the same time last year, the total was 19.

— Jane Hill

“Some sellers now are taking a wait-and-see attitude.”

Brian O’Boyle, partner at Apartment Realty Advisors in Dallas



Hotel industry favors new construction over rehab

It’s checkout time for certain hotel properties that are past their prime.

Even those with charm, character and stories to tell can’t sway the hearts of investors because their operating costs are high compared to their younger counterparts. In particular, the older buildings are leaking profits because they lack the energy efficiencies possible in new construction.

Take the Green Oaks Hotel in Fort Worth. Back in the day, its guest list included Janet Leigh, Bob Hope and Elvis Presley, among other celebrities, but nostalgia is not bankable. Dallas-based Wilcox Capital Partners, owner of the property, announced it would tear down the vintage 280-room hotel in December and replace it with an office building and perhaps another hotel on the 12-acre site. Both new buildings will be certified “green buildings,” ensuring that materials are environmentally-sound and the design is energy-efficient.

For the same reasons, Akal Corp, an Irving-based hotel franchisee recently announced that it had shifted its focus from buying existing buildings to developing new hotels, says Paul Singh, Akal’s president.

The hotel industry is by nature labor-intensive, and as the minimum wage climbs, operators are looking for ways to shave expenses. Conserving energy is a prime focus.

“Moving forward you have to be smart enough to save money in operations. You will need sustainable design to survive,” Mr. Singh says.

The company used to buy existing properties and turn them around through improved management, but the per-room rate for acquisition no longer makes sense, he says. The cost of acquiring existing hotels is up to nearly \$79,000 per room, as compared with new construction costs of

\$60,000 to \$70,000 per room, he says.

Though energy-efficient design adds to the initial cost of construction, the extra investment pays for itself in two years of operations and, by year three, you’re making money from energy savings, he says.

The Akal group recently opened a new LaQuinta Inn in Mansfield, and has three others, each with 70 to 75 rooms, set to open in Lakeport, McKinney and Kilgore. Mr. Singh says the company also is working with Hilton to secure a location in the Dallas area.

As part of its new strategy to build, hold and manage midsized hotels, the firm has sold or is selling a few of its older properties.

“The Texas hotel market is very strong,” with about a 69 percent occupancy rate in 2007, says Mr. Singh. The Dallas market comes in a little lower, at 65 percent, he says, but still in the healthy range.

When an estimated 20,000 new hotel rooms open in 2008, that occupancy rate may dip slightly, he predicts.

In addition, the average daily room rate is expected to go up, even when adjusted for inflation, says Bobby Singh, vice president of development for Akal.

According to PKF Hospitality Research, based in Atlanta, hotel occupancy nationwide is projected at 63.4 percent in 2008, no change from 2007, and the average daily room rate is expected to grow at 4.2 percent.

— Jane Hill



Photo by Aeneas Ford

2007

TEXAS TRENDS

Office and Industrial Market Overview

Thursday, November 8, 2007

8:00 a.m. Breakfast

9:00 a.m. Presentation

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