Arkansas Oklahoma Kansas

2017

Apartment Report Oklahoma City Tulsa

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Mike Buhl
CRRC - OKC
405.360.5966
buhl@crrc.us

Darla Knight
CRRC - Tulsa
918-557-5966
darla@crrc.us

www.crrc.us

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COMMERCIAL REALTY RESOURCES CO
MULTIFAMILY INVESTMENT SERVICES

2017
Multifamily Apartment Report

This year did not turn out as expected. In January, it seemed like interest rates would begin an upward climb, pushing cap rates higher for investments in multifamily properties. Instead, interest rates sagged from their highs at the end of 2016 and cap rates stayed low in 2017. Also, a bit unexpected is the amount of deal volume that surpassed 2016 by 23 percent. This contradicted the broad opinion that there was not much on the market for sale. The disconnect lies in the amount of off-market deals that were transacted in 2017. Notwithstanding, there is a bigger buyer pool that is putting pressure on what is a shrinking pipeline of deals.

The increased deal volume and pricing is most notable in the Pre-1980's category that recorded over 5,500 units sold in 2017. The other two categories; 1980's and Post 1990's recorded gains as well, but only 1,879 units collectively. What that means is that investors are less choosy about the properties they buy and the prices they are willing to pay. Why the change? At the forefront is the growing interest in workforce housing, which is generally viewed as a recession-proof asset class. Secondly, it comes down to financing. If a property has a good historical occupancy over 90%, than it will qualify for agency financing, which offers the best combination of maximum loan proceeds and attractive interest rates. Some of the sales in 2017 were financed with loans as low as 4% with 30-year amortization, 10-year maturity dates, and interest only payments in the beginning year(s). Freddie Mac continues to be the leader making more permanent loans on apartment properties than any other type of lender. And finally, investors are drawn by the prospects for strong rent growth and relatively healthy occupancy rates.

Because the market is changing, investors will have to change as well and counter those forces at work by seeking risk-adjusted returns instead of anticipating more cap rate compression. Except those returns need to come from occupancy and rent growth and not all properties are created equally. In the short term, that discipline will translate to even fewer properties from which to choose, especially if sellers still count on that cap rate compression to get them higher pricing. And largely, sellers are still holding to that expectation.

Consequently, investors continued to pay more than ever for apartments in 2017. One reason is that they were finding partners who were eager to contribute equity capital to their acquisitions. And many times, this equity capital came from partners who had not even seen the asset. So, in a changing environment when it seems less and less likely prices will rise as quickly in the future as they have in the recent past, the discipline towards yield should be ever-present. Investors turned owners may not have that cap rate compression going forward to paper over any mistakes they made in underwriting for the acquisition.

What is the bigger disruption to the market, the expected or the unexpected? As to interest rates, they have been the single biggest factor in fueling apartment acquisitions in recent years, including 2017. The market expected rate hikes that didn't happen, so the unexpected actually became the welcomed surprise. Unexpected rate hikes though might not be so well received. My point is that market disruptions usually happen when the unexpected occurs. The takeaway here is that 2017 was atypical to this belief. So interest rates aside, I think the multifamily market has stayed its course because it has performed as everyone has expected. However, with the end of 2017, the market is one more year farther into what has already been a very prolonged up cycle. So the question looms, what can we expect in 2018? Opinions will vary, but there are two factors that could disrupt the market. The first is directly tied to multifamily in the form of property fundamentals, or weakening fundamentals as the case may be. Perhaps better stated by saying; the absence of rising fundamentals.

The second is tied to the overall economy of Oklahoma which would indirectly affect the multifamily market. This one has the greatest risk for wide-ranging disruptions. According to estimates from the Oklahoma Employment Security Commission, the average weekly earnings for someone employed in Oklahoma is $807.56 for the past 12 months through October, up 5.17 percent from last year's $767.85. Lynn Gray, the director of economic research and analysis for the commission, said Oklahoma's added 20,200 jobs during the past 12 months, setting a 1.2 percent pace of growth over the year. [1] Preliminary data from the U.S. Bureau of Labor Statistics shows Oklahoma's unemployment rate in October was 4.4 percent. A year ago, the state's unemployment rate was 4.9 percent. In Oklahoma City, the preliminary rate fell from 4.2 percent to 3.6 percent over the past 12 months through October. In Tulsa, it fell from 5 percent to 4.4 percent. In Enid, it fell from 4 percent to 3.4 percent, and in Lawton, it fell from 4.6 percent from 4.4 percent.

The economy is on the rebound and is up on all economic statistics statewide and in the metro, according to Dan Rickman, regents' professor of economics at the Spears School of Business at Oklahoma State University. But Rickman went on to say; "we don't seem able to fund basic government functions at the level we need to, primarily education." "What most alarms me is the growing dysfunction in state government, certainly in the legislative branch, and the inability to come together and compromise and find solutions to improve the state of Oklahoma," said Mickey Hepner, professor of economics at the University of Central Oklahoma. [2] And Governor Mary Fallin said "we are setting Oklahoma up for failure that will take many years to undo the damage we have done to our state's image." [3]

Going back to the first factor of fundamentals, these types of disruptions would likely be on a smaller scale and more related to property vintage. This can occur when the broader market experiences softness that then filters down to the property level causing those fundamentals to falter or decline. This can mean softness in the neighborhood, the submarket, or even the metro, as the case may be. I have seen this multiple times this year when an owner decides to sell and the occupancy and/or income are lower and the expenses higher than when he acquired the property. Without the aforesaid cap rate compression or some other force at work, those weakening fundamentals assert the property is worth less than he paid for it. This becomes especially distressing if that owner paid a premium on the acquisition side. These types of disruptions are not uncommon today. Fortunately, they are not widespread and remain at property levels. More importantly, there have been few sales where the asset is sold for a loss creating lower market values. I still contend this may be more about luck than strategy though for some sellers. Though few will admit it, there has been some artificial value created in this up cycle and there is an unspoken concern about pricing to valuation. But there has been little data to support that concern, so prices remain easy to justify and fears remain unfounded.

There is a point when both price and value are in unison and that balance translates to fair market value. This is a comment I made in my 2017 Mid-year Apartment Report. But we are not at that point right now. In my 2017 Mid-year Report, I also said "if you are an investor hoping for a bump in the road that would translate to better pricing, think again…2017 appears to be on par, if not better than 2016 in terms of pricing, which is favoring sellers". That has certainly proved true. In this cycle, it has been difficult to forecast just how high investors will go to acquire multifamily assets.

As in previous years, the catch phrase is still value-add. I remain a firm believer in value-add because of the need for good quality affordable housing in a market where new multifamily housing is mostly built for the luxury market. Plus, many of these older communities and apartment units exhibit functional obsolescence in their design features that make them outdated. The stumbling block is when value-add is structured for profit over purpose. Purpose driven value-add has the potential to deliver profits and effectively meet a need. The reverse of this is that some investors target value-add with no real intention of creating value other than to sell for a higher price than what they paid. But this strategy does nothing to meet the need of affordable housing and is a bit misguided because it provides no benefit to the tenant. The most successful value-add is the one with a purpose that can provide the best housing options within a given price point. It really comes down to aligning people's incomes with their desire to live in certain neighborhoods.

Oklahoma City Metro

For the twelve months of 2017, there were 52 sales on properties that exceed 25 units in size, for a total of 7,426 units. This was up 24% from 6,000 units sold in 2016. Total sales volume was $377.4 million in 2017, as compared to $308 million in 2016, a 23% increase. The historical high is $439.6 million set in 2015 when 8,483 units were sold. For 2017, the overall average price per unit on apartment communities with 25 units or more is $50,832, down only slightly from $51,333 at the end of 2016.

For Pre-1980's properties, there were 45 transactions involving 5,547 units for an average per unit price of $35,900. Of the overall $377.4 million in sales, $199.1 million was in this Pre-1980's vintage, continuing the trend of investors looking beyond core assets for opportunities. The category showed a significant increase from 2016 with $130.3 million in sales on 33 transactions, involving 3,734 units and an average price per unit of $34,906.

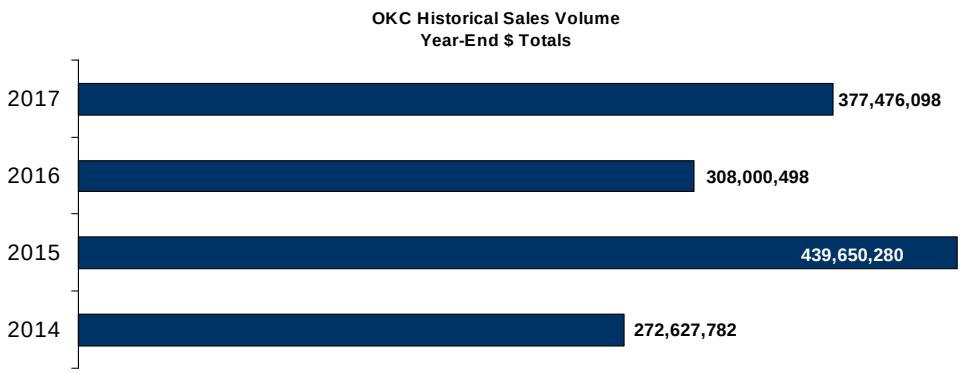
Within the 1980's category, there were three sales for a total of $44.4 million on 802 units. The average price per unit was $55,486. The largest sale in terms of pricing was the Waters-Edge Apartments at 4317 SW 22nd that sold for $23.6 million, or $64,130 per unit. This 368-unit community was built in 1986. The reported cap rate for this transaction was 6.07%. The second largest sale in terms of size was the Cambridge Landing Apartments at 8800 S. Drexel with 400 units. This property sold for $19.6 million, or $49,000 per unit. By comparison, there were six transactions in 2016 for $42.5 million in sales. In that year, there were 915 units sold for an average price per unit of $46,502. The comparison between years is similar with the exception of a 19% increase in the average price per unit for 2017.

Post-1990's properties recorded four sales in 2017, with each sale representing a different segment of the market ranging from purpose-built student housing to urban-core best-in-class. The Reserve on Stinson is a 204-unit community with 612 bedrooms serving students at the University of Oklahoma campus in Norman. The property was built in 2005 and sold for $17,639,904, or $86,470 per unit. At an equivalent of $76.42 per square foot, it reportedly sold for less than replacement value. It is worth noting that the property was originally sold by the developer for $30,500,000 in December of 2006 and then later sold for $22,948,000 in January of 2012, a 42% drop in value over that ten year period.

In my 2017 Mid-year Report, I discussed student population trends at the University of Oklahoma. That report is available at www.crrc.us. The point I made in this report was that unless 2017-Fall enrollment figures defy the historical trend, developers had created a vast oversupply of purpose-built student housing in Norman. I made the observation that even though demand for student housing around campus is a constant, the mathematics of supply and demand may not work. Fast forward to today and the Millennium Apartments, a 196-unit, 698-bed student housing community that was built in 2015 is being offered for sale at a 55% occupancy rate for the 2017 / 2018 academic year. The marketing materials state that the asset will sell for well below replacement cost, suggesting the current owner/developer will be taking a loss. While we were hopeful at mid-year that the ten year historical valuation of the Reserve would not be repeated, it appears there will be a second case study in Norman for overbuilding

Back to the positives, the Metropolitan Apartments in downtown Oklahoma City was another sale in this Post-90's category, but one that set record pricing at $194,665 per unit. The 329-units were finished in 2016 and sold for $64 million. Rental rates at this best-in-class community range from $894 to $1,752 per month for a 1-bedroom, $1,583 to $2,231 for a 2-bedroom and $2,245 to $3,250 for a 3-bedroom. The community also offers a 578 space parking structure for its residents. Deals at price points of $200,000 per unit though will remain rare.

Another of the four sales was the Summit Pointe Apartments at 1002 SW 89th Street that sold for $17.55 million, or $95,380 per unit for the 184-units that were built in 2009. Both the Metropolitan and Summit Pointe were sold to Weidner Apartment Homes of Kirkland, WA.



Total Sales Volume

23%
Compared to 2016

Total Units Sold

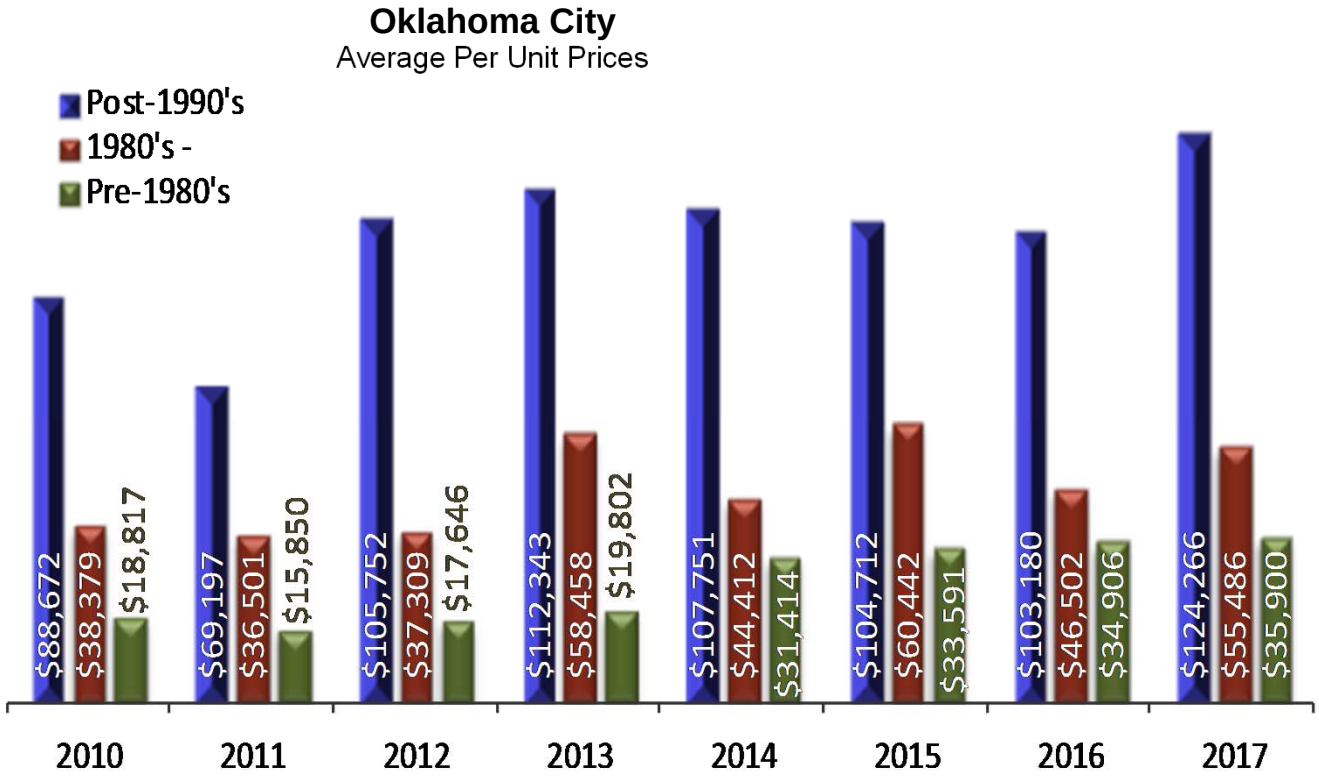
24%
Compared to 2016

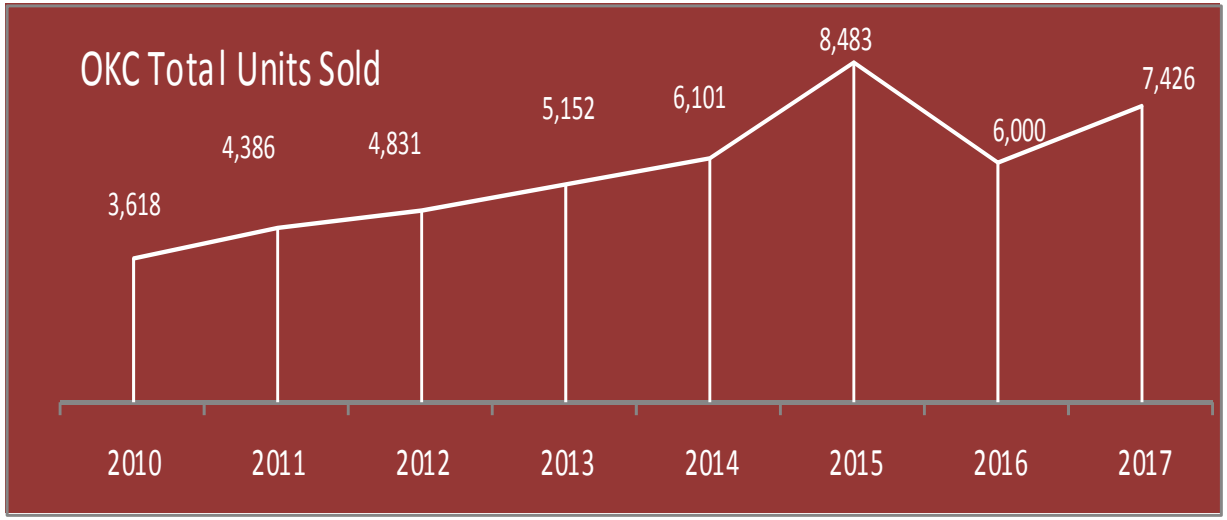
Average Price Per Unit

1%
Compared to 2016

No. of Transactions

13%
Compared to 2016





Tulsa Metro

There were 14 sales in 2017 on properties that exceeded 25 units in size, for a total of 2,890 units sold. This was slightly above the 2,725 units sold in 2016.

Total transaction volume in Tulsa was $148.4 million, which was also up from $112.7 million in 2016. The overall average price per unit in Tulsa was $51,356 versus $41,392 in 2016, a 24% increase. The difference in comparing Tulsa to Oklahoma City is that the majority of sales, 79 percent, occurred in the 1980's or newer product.

For Pre-1980's properties, there were eight transactions involving 865 units for an average per unit price of $36,173. This compares to 14 transactions on 2,288 units sold in 2016 for an average price per unit of $39,442, an 8% decline. Total volume though in 2016 was $90.2 million, versus only $31.2 in 2017, a 65% year-over-year decline. The largest sale in terms of size was the Sierra Pointe Apartments at 1433 S. 107th East Avenue at 348-units. The property sold for $12.35 million, or $35,488 per unit. The highest price per unit belonged to French Villa Apartments at $58,450. French Villa is 100-units at 4752 S. Harvard that sold for $5.845 million.

Tulsa	Post 1990's	1980's	Pre-1980's
Number of Transactions	1	5	8
Total Number of Units	132	1,893	865
Total Number of Sales Tulsa		5	6
Total Number of Sales Other	1		1
Total Number of Sales Broken Arrow			1
Price High per unit Price Low per unit	$102,272 $102,272	$59,600 $32,421	$58,450 $24,861

Oklahoma City	Post 1990's	1980's	Pre-1980's
Number of Transactions	4	3	45
Total Number of Units	1,077	802	5,547
Total Number of Sales OKC	2	3	27
Total Number of Sales Edmond			3
Total Number of Sales Norman	1		9
Total Number of Sales Other	1		6
Price High per unit Price Low per unit	$194,665 $86,470	$64,130 $38,235	$71,718 $986

Post 1980's recorded five transactions for 1,893 units sold in 2017. Combined sales accounted for $103.6 million for an average price per unit of $54,744. This compares to 2016 with only one sale at $6.3 million involving 132 units. Sales in 2017 included Westport on the Rivers, Creekwood / Columbine and South Port Apartments. Westport is 682-units, built in 1984 that sold for $40,600,000, or $59,530 per unit. Creek wood/Columbine sold for $38,800,000, or $59,600 per unit for the 651-units that were built in 1984 and 1986. South Port at 6326 S. 107th East Avenue was built in 1984 containing 240-units. The property sold for $13 million, or $54,166 per unit.

The one sale in the Post-1990's vintage category involved the Marquis on Memorial Apartments in Bixby that sold for $13,500,000, or $102,272 per unit for the 132-units that were built in 2009. The Seller acquired the property in December 2014 for $12,750,000, or $96,590 per unit.

Property Name	Address	Price	No. of Units	Year Built	Price Per Unit
Sale Highlights Tulsa					
Lake Terrace	3218 S. 93rd Ave E	$2,560,000	79	1973	$32,405
Oak Creek	2340 W. Newton	$2,930,000	64	1981	$45,781
Sierra Pointe	1433 S. 107th Ave E	$12,350,000	348	1967	$35,488
Delaware Gardens	5104 S. Delaware	$990,000	30	1975	$33,000
South Port	6326 S. 107th Ave E	$13,000,000	240	1984	$54,166
Prescott Woods	1337 E. 61st Street	$8,300,000	256	1985	$32,421
French Villa	4752 S. Harvard	$5,845,000	100	1962	$58,450
Melrose	6321 E. 9th Street	$1,600,000	52	1968	$30,769
Marquis on Memorial	14681 S. 82nd	$13,500,000	132	2009	$102,272
Sale Highlights Oklahoma City					
Villas at Countryside	9501 S. I-35	$34,600,000	360	2002	$96,111
Cambridge Landing	8800 S. Drexel	$19,600,000	400	1983	$49,000
Metropolitan	800 N. Oklahoma	$64,045,000	329	2016	$194,665
Old Tuscan Village	300 Hal Muldrow	$2,820,000	71	1969	$39,718

Total Sales Volume

32%
Compared to 2016

Total Units Sold

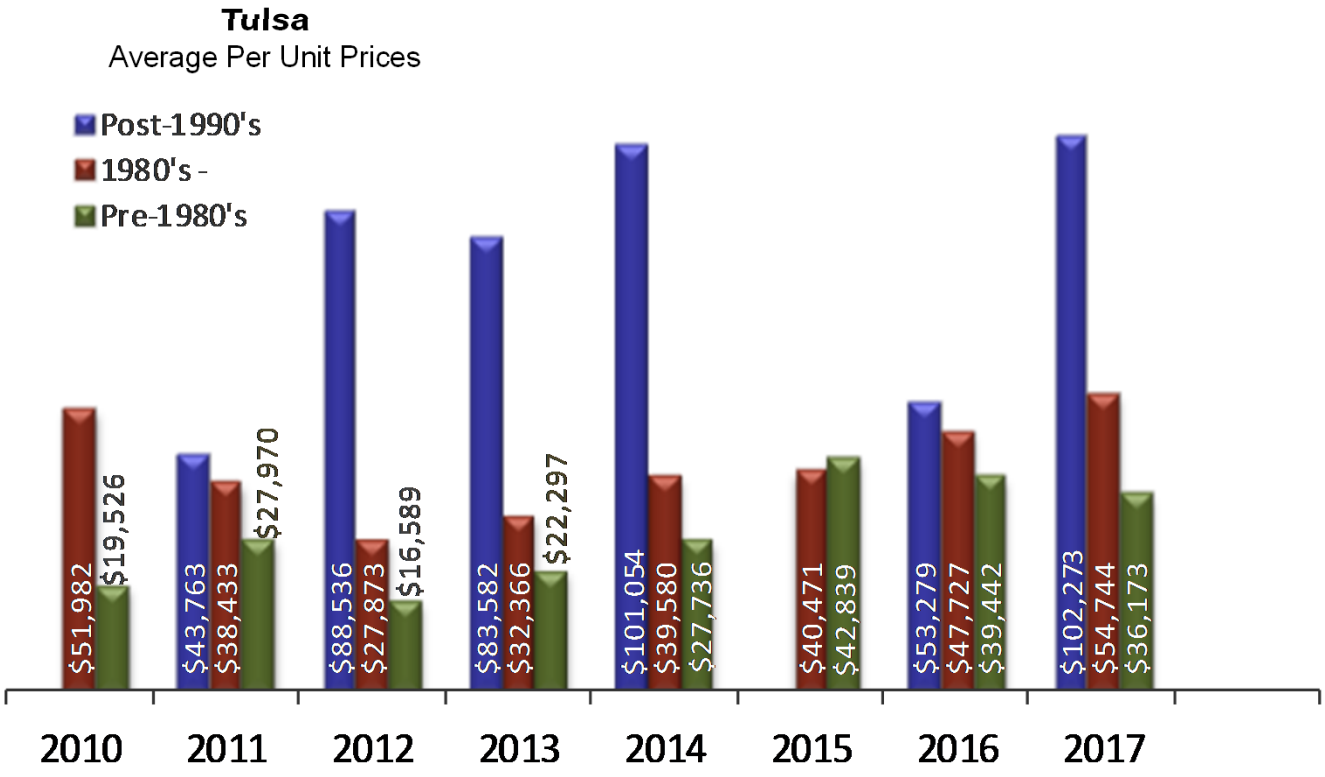
6%
Compared to 2016

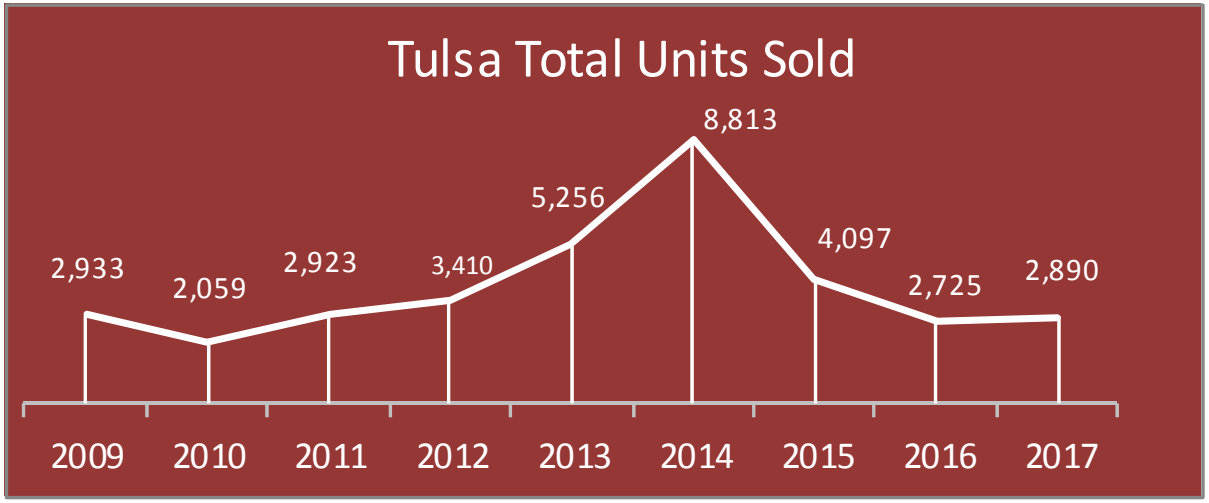
Average Price Per Unit

24%
Compared to 2016

No. of Transactions

13%
Compared to 2016










Arkansas Oklahoma Kansas

Outlook

Investors look set to continue on the same path and go after apartment assets in the face of high prices. But as an owner, if you expect the cap rate to be higher when it comes time to sell or refinance, you better be pushing rents. Otherwise, those investors waiting for a bump in the road will be in the driver's seat.

Despite a potential shrinking pipeline of deals, there should be adequate inventory available in 2018 that we will see similar pricing to 2017. The outlook for occupancy remains stable compared to 2017, although sentiment has eroded slightly. The picture is similar on rents. There remains overall bullishness that fundamentals will remain stable, although the level of optimism is a bit lower than in years past.

So turning back to the looming question; what can we expect in 2018? I think we will see more of the same; opportunities and challenges. There is a psychology developing where people are wondering how long this cycle will last. But, it's worth contemplating that maybe the length of the cycle is not a determinant of a turn in the cycle.

1-Number of Oklahoma jobs nearing all-time state high, Oklahoman, November 18, 2017
2-Oklahoma economy recovering, but challenges remain, economists say, Oklahoman, November 16, 2017
3-The gang that sold out Oklahoma, Journal Record, November 17, 2017

CRRC has sold over 34,000 apartment units. We deliver value to our clients by providing exceptional service that increases your bottom line. **CRRC** has one of the best success rates of any of its competitors for achieving the highest sale to list price at 94%*.

*Based on $167.6 million in sales on 4,677 units between March 2013 and March 2017

Sale Highlights Oklahoma City, continued

Property Name	Address	Price	No. of Units	Year Built	Price Per Unit
Summit Gardens	3500 NW 51st	$1,310,000	38	1964	$34,473
Oakleaf / Sunrise	5700-5731 NW 19th	$5,339,000	148	1972	$36,074
Warehouse Flats	1325 W. Lindsey	$1,460,000	33	1968	$44,242
El Greco	3525-3541 NW 50th	$1,275,000	32	1964	$39,843
Lakewood Estates	7806 Lyrewood	$6,000,000	208	1971	$28,846
The Brittany	2620 N. Meridian	$3,430,000	110	1970	$31,181
South Shore	616 SW 59th	$2,600,000	68	1963	$38,235
Charleston	2011 W. Lindsey	$5,972,970	163	1972	$36,643
Summit Pointe	1002 SW 89th	$17,550,000	184	2009	$95,380
Mulberry Parke	7652 NW 10th	$2,900,000	96	1971	$30,208
Continental	2424 Nottingham	$2,575,000	80	1973	$32,187
Bridge Port	1000 NW 105th	$1,250,000	91	1972	$13,736
Market on Paseo	600 NW 29th	$2,295,000	32	1966	$71,718
University Pointe	1509 NW 30th	$1,350,000	127	1968	$10,629
Tuscany Village	6900 London Way	$10,000,000	300	1973	$33,333
Country Club	5700 S. Agnew	$2,965,000	189	1962	$15,687
MacArthur Park	6100 MacArthur Park	$1,300,000	34	1984	$38,235
Ashwood	3451 SE 44th	$4,292,500	153	1972	$28,055
Reserve on Stinson	730 Stinson	$17,639,911	204	2005	$86,470
Brookwood	9401 S. Shartel	$60,500,000	1128	1970	$53,634