

Tight financing halts sales of large apartments in S.D. County

By **THOR KAMBAN BIBERMAN**, The Daily Transcript
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No apartment complexes with more than 100 units have sold in San Diego County during the last six months and only five such sales have happened all year, according to **Novato-based RealFacts**.

Those five sales involved 1,063 units and a roughly \$130 million in total dollar volume.

This compares with 10 transactions of 100-plus units totaling 1,798 apartments and about a \$270 million volume during the first nine months 2008, and 21 transactions of 100-plus unit properties involving 3,797 apartments and about a \$725 million volume during the first three quarters 2007.

Not only have the number of large transactions gone down, the average price per unit has dropped significantly.

The average price per unit, which peaked at \$194,269 in 2006, dropped to \$186,401 in 2007, \$145,461 in 2008 and ended the third quarter of 2009 at just \$123,016.

Two of five sales were to **The Prime Group**, a San Francisco-based private real estate firm; the 424-unit Villages of Monterey in Oceanside for \$52 million and the 234-unit Montecito Village property in Oceanside for \$32 million.

Two more of the sales also involved the same buyer -- in this case the local Conrad Prebys Trust; the 117-unit Park Terrace Apartments in Escondido for \$12.4 million and the 144-unit Grove Apartments in El Cajon for \$14.7 million.

The fifth sale was the 114-unit Shadow Way Apartments in Oceanside for \$19.4 million to an entity of **Wasatch Pool Holdings LLC** of Utah.

A new **Grubb & Ellis|BRE Commercial** apartment report, which incorporated September data from San Diego-based **MarketPointe Realty Advisors** said investors feel this should be a good time for apartment investors if they can get into the game.

"As the nation continues to cope with one of the worst recessions on record, the long-term outlook for San Diego's multi-family market remains positive due to numerous barriers to entry, including high land costs, a large rental population and extremely limited new multifamily development," Grubb & Ellis|BRE reported.

So why aren't investors buying apartment complexes?

Sarah Bridge, RealFacts co-founder, said there is no single answer.

"The industry is at a complete standstill. The banks aren't lending, Wall Street conduit money has all but evaporated and properties are somewhat overvalued," she said.



Bridge also said apartment buyers who may have been accustomed to being able to finance as much as 95 percent financing, now have a loan-to-value ratio that's much closer to a 60/40 split.

"We are going back to fundamentals here ... The deals of the past were highly leveraged," Bridge said.

Bridge conceded she isn't sure who the new buyers will be who will purchase the large complexes, but added that she is certain the players will be very different than the existing entities such as Wall Street firms owning vast pools of assets.

"The new buyers will have to find a whole new way of structuring a deal," Bridge said, "but real estate people are creative. They do find ways to buy properties."

They haven't bought any large ones since the beginning of April here. Bridge suggested the recovery could well be helped along by apartment properties bought out of receivership.

"I'm not saying that it will happen that way, but that is one possibility. Another possibility is that funds might be created that will give apartment owners a way to make their loans work," Bridge continued. "In any case, there will be a big decision to make when the loan comes due."

While there has been a dearth of large apartment complex sales, there have been plenty of smaller ones. Most of these examined by the *Transcript* have involved complexes with five or fewer units, and many of those have in fact been bought out of receivership.

Based on RealFacts data, the average vacancy in San Diego County was 6.2 percent in the third quarter compared to 4.2 percent a year earlier.

It should be noted that RealFacts doesn't count complexes with less than 100 units however.

MarketPointe reported a 4.39 percent apartment vacancy in September, compared to a 5.29 percent vacancy in March and a 2.25 percent vacancy in September 2008. MarketPointe limits its surveys to complexes with 25 units or less.

Russell Valone, MarketPointe president, added that while vacancies may have climbed slightly and rents have dipped, (they still average more than \$1,300 per month here) apartments remain fundamentally strong.

Unfortunately the capitalization rates have nearly doubled in the past two years and lenders have severely tightened the purse strings. "We're under 5 percent so that's still very strong, but here's part of the problem: Here's the apartment market at 5 percent and here's the office market at a 20 percent vacancy and lenders treat us the same," Valone said.

"Multi-family financing remains available through **Fannie Mae** (NYSE: FNM), **Freddie Mac** (NYSE: FRE) and some smaller regional banks albeit with stricter loan terms, financial underwriting, loan-to-value and debt coverage requirements," Grubb & Ellis|BRE wrote.

"There has also been an increase in seller financing options, both from private owners and banks, although sales volume has decreased significantly," the report stated.

But Valone insists that lenders still need to listen to the pleas of apartments owners who need to refinance and would-be investors who might try to buy more than a few units at a time.

"Look at it this way. On the one side you have slightly higher rents and somewhat higher vacancy rates than a year ago, but you still low occupancy and strong economics. That's the feather," Valone said. "On the other side you have the lender. That's the prime heifer and nothing else matters."