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Drop expected for apartment values in 2010

Roger Showley, *The San Diego Union-Tribune, September 25, 2009*

Although they think they own the best real estate to weather the recession, local apartment investors, managers and analysts still expect values to drop in 2010.

"The good news is that we haven't heard anyone single out apartment investing" as a bad move, said Robert Vallera, a principal at Commercial Realty Advisers, at a briefing yesterday on the apartment market and the overall economy.

Vallera asked the 200 attendees at the Mission Valley Marriott what they expect to happen to apartment values next year. Virtually all raised their hands to indicate a drop — the result of distressed properties selling at bargain prices.

But that presents an opportunity, said Lorne Polger, senior managing partner of the Pathfinders Partners real estate investment group.

"We buy problems; we're cash buyers," Polger said, and he laid out plans to invest $500 million to $1 billion next year in distressed multifamily housing units across the country.

The session, sponsored by the San Diego County Apartment Association and the local chapter of the CCIM Institute for certified commercial investors, also featured former San Diego City Councilman Fred Schnaubelt and University of San Diego economics professor Ryan Ratcliff.

Ratcliff said while economic indicators suggest the recession has ended, unemployment will be slow to fall and California's state budget problems will likely delay any recovery.

"I can't see the light around the corner, but I can see a glow around the corner that suggests the light at the end of the tunnel is coming up real soon," Ratcliff said.

There's only darkness on the construction side, according to a report on building permits released yesterday by the Construction Industry Research Board. The Burbank-based group said a record low of just four multifamily housing units was authorized in San Diego County in August, down from 32 in July and 451 in August of last year. Year to date, there have been only 778 units approved, down from 2,431 for the same period last year.

Single-family production was no better, a near-record low of 98 homes authorized, down from 151 in July and 213 in August 2008.

"I think we're in a period where we're trying to get back to a normal market," said CIRB director Ben Bartolotto. "It's hard to read it. We're forecasting that things will improve."

Statewide, he said, 2008, 2009 and 2010 are likely to represent the least construction activity in 40 years of record keeping. He's projecting total housing units for this year at 39,500, eclipsing last year's low of 64,962. Next year may come in at 65,000, he said.

The California Building Industry Association said the drop in construction statewide is partly due to the lapse of the $10,000 new-home tax credit that spurred interest early this summer. An $8,000 federal first-time-buyer tax credit expires Nov. 30.

Robert Pinnegar, executive director of the apartment association, said construction is virtually nonexistent because current rent levels are not high enough to support new projects.

"You haven't really seen a large number of apartments developed in quite some time," Pinnegar said. "The reason for that is just economics. Unless you have the land entitled for sometime, it just doesn't pencil out. It's cost prohibitive."

For the next 12 to 18 months, he said, apartment rents are expected to remain stable and vacancies will likely remain at their current level of around 5 percent. As the economy improves and demand grows, construction should increase.

"Demand is driven by job growth," he said. "Unless we have meaningful job growth, it'll be status quo."