RED CAPITAL GROUP®

Market Overview

Little Rock, Arkansas

Multifamily Housing Update **January 2008**

EXECUTIVE SUMMARY

Arkansas payroll job growth ground to a near standstill last year. The Bureau of Labor Statistics estimate that state establishments produced only 3,500 (0.3%) seasonally adjusted jobs from December 2006 to November 2007, down considerably from a 21,700-job add in 2006. Manufacturing was the principal culprit, as nearly every major durable and non-durable goods category recorded material decreases in net payroll totals.

The capital city's more services-oriented economy weathered the rough patch with ease, creating 5,900 (1.7%) jobs in the 12 months ended in November. Payrolls in every major job category with the exception of non-durable goods manufacturing advanced, led by health care and business services, which produced a net of 2,800 jobs .

In contrast to sluggish national trends, the pace of hiring accelerated in the fall. Year-over-year, Little Rock added 6,800 jobs in the third quarter and 6,400 jobs in the three months ended in November. Propelled by rapid hiring in hospitality, trade and construction, November payrolls surged 400 sequentially, reaching an all-time high total of 351,500, and rising 6,600 (1.9%) jobs above the over-the-year comparison.

Although the state's sluggish economy will exert a degree of downward pressure on metro growth in the first half, the outlook for 2008 is largely positive. The **RED CAPITAL Research** econometric payroll model forecasts net job growth ranging from 5,000 to 8,000 jobs in 2008, with point estimate of 6,000 (1.7%). Stronger GDP growth in 2009 should give rise to faster expansion in the City of Roses next year.

Metro home price appreciation trends moderated in 2007 following a robust 6.7% advance in 2006. Prices fell in the six months ended in March, but rallied in the second and third quarters. According to the NAR, the median price of a home was $131,600 in 3Q07, up 2.1% year-over-year.

Although the median priced home was affordable to nearly 70% of metro households, retail demand for rentals is constructive. Tenants absorbed 149 units in 3Q07, according to Reis surveys, up from 14 units in the comparable period of 2006 and 65 units in 2Q07. The Little Rock inventory was unchanged for the third consecutive quarter, by Reis's count, allowing average occupancy to rise 60 basis points to 92.4%, the highest figure recorded in twelve months.

In spite of pending supply representing 2.3% of the existing inventory in 2008, Reis are sanguine regarding occupancy levels. The service forecast a 40 bps increase in 2008 and a 50 bps advance to the 93.9% level in 2009.

Owners maintained a cautious pricing posture, bearing in mind the competition posed by for-sale housing. Average effective rent inched up $4 to $593 in 3Q07, a 0.7% sequential hike. Over-the-year, real rent increased only $9, representing annual growth of 1.5%. Were the "Rock" a component of the **RED 50**, it would rank 49th on this measure, bettering only Palm Beach. Asking rents also rose $4, holding the value of the standard concession package to a low $17 (2.3%), calculated monthly. Concessions were lower in only two **RED 50** metros.

Property trade was active 2H06 and 1H07, as investors accumulated assets in this appealingly stable market. The $50mm sale of class-B Chenal Lakes and Brightwater to an out-of-state private buyer was the bellwether transaction. The trade was priced to yield about 5.5%. In late 2006, a public Reit sold four assets to a local TIC group for about $49.7mm ($67m/unit), priced to an initial yield of less than 6%. Since mid-year, activity has been light. Only one small ($3mm) trade was recorded: a class-B– complex priced at $30m/unit to yield approximately 8%.

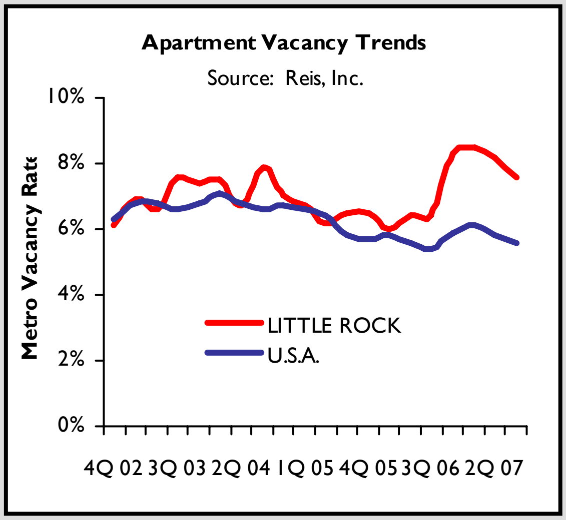
SNAP SHOT

	Y-o-y change	Projected 2008
Vacancy (7.6% - 3Q07)	120 bps	40 bps
Effective Rents ($593 - 3Q07)	1.5%	2.2%
Cap Rate (NA - 3Q07)	Unchd	Unchd
Employment (348.6m - 3Q07)	6.8m	6.0m

KEY POINTS

- This stable economy harvested 2m to 7m net jobs in ten of the past twelve years. Only the recessionary 2002 (-3,5m) and booming 2006 (+8.6m) years broke the mold.
- At 5,800 jobs, the 2007 vintage easily topped the 4,300 12-year average, and ranks as the second most bountiful harvest since 1996. Expansion in the skilled service and hospitality industries was largely responsible: business, health care and leisure services combined to produce 3,100 jobs in the first eleven months of the year and 4,400 (3.8%) year-over-year in the third quarter.
- Reis report that occupancy rallied in 2007 after a supply induced 180 bps (to 91.7%) setback in 2006. Tenants absorbed 179 units y-t-d, including 149 units in 3Q07, raising average occupancy 70 bps to 92.4%. Reis forecast further progress during 2008—09.
- Owners sought higher occupancy rather than revenue growth. Third quarter average effective rent increased only $9 (1.5%) y-o-y and $4 (0.7%) sequentially. The former figure would rank 49th among the **RED 50**.
- The "Rock" earns a weak ***"Accumulate"*** ranking principally in recognition of its innate stability rather than potential returns.

VACANCY TRENDS

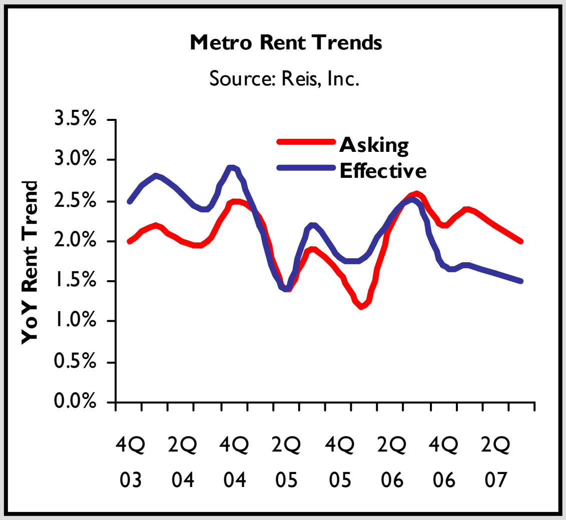


- The Reis vacancy rate series for Little Rock is remarkably stable, tracking closely with the national average.
- Vacancy veered upward in 2006 (to a Reis series high 8.5%), however, as a supply spike exacerbated by faster tenant migration to homeownership contributed to a meaningful increase of vacant inventory (1,452 units in 1Q06 to 2,055 units in 3Q06)
- Reis are optimistic on the occupancy front, anticipating stable demand and moderate supply. The service expect occupancy to rise 40 basis points in 2008 and 50 bps in 2009.

RANK: Not a **RED 50** metro

COMMENT: **Reis anticipate solid occupancy gains through the end of the decade.**

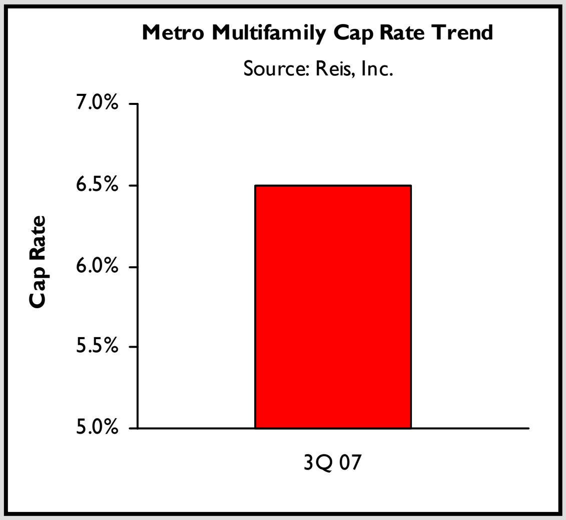
RENT TRENDS



- Effective rent increased $4 (0.7%) in 3Q07, the equal largest dollar advance recorded since 4Q04. Over-the-year, tenant payments increased $9 (1.5%), down from a 1.6% metric recorded in 2Q07.
- Effective rents trends varied widely by submarket. The value-priced Downtown / South submarket (average rent $485), enjoyed y-o-y effective rents gains equal to 4.6%. Conversely, Central submarket owners registered 3.2% and 1.5% declines in average occupancy and effective rent, respectively. On the other side of the coin, the submarket with highest average rent (West / $705) achieved a 4.3% y-o-y average rent hike and a 40 bps increase of average occupancy.
- Reis project compound average rent growth of 2.9% through 2011.

RANK: Not a **RED 50** metro

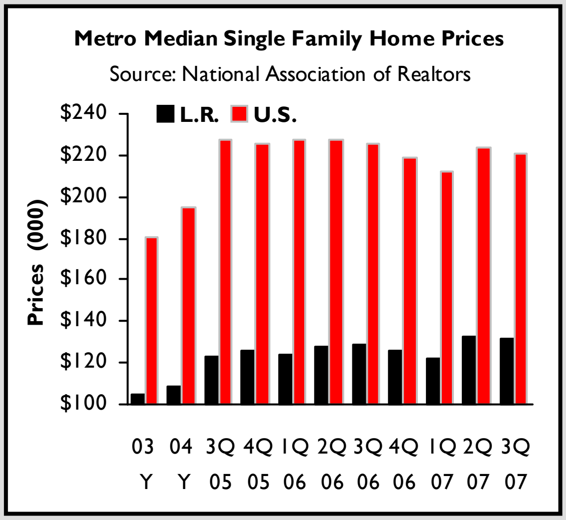
PROPERTY MARKET & CAP RATE TREND

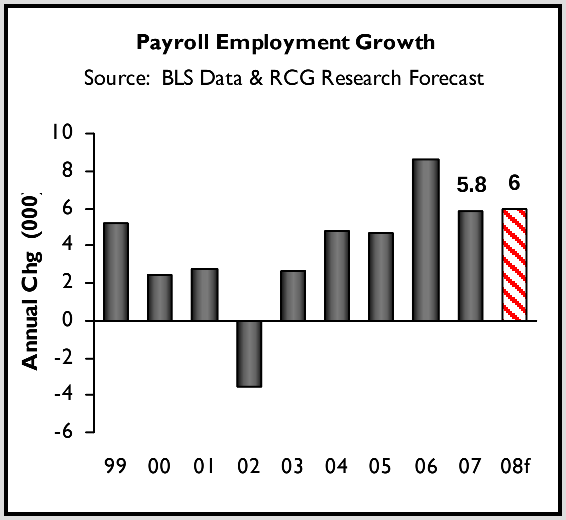


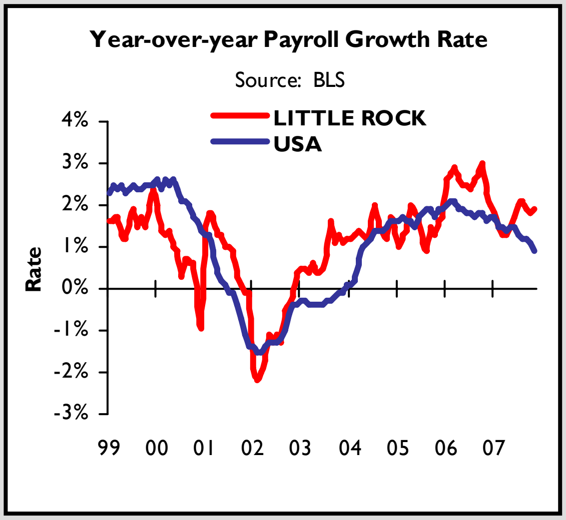
- **RED** assign a weak ***"Accumulate"*** rating to Little Rock assets, based on the metro's below average rent and occupancy volatility since 1999. Total returns are not likely reach the **RED 50** average, but we are of the mind that investors will achieve satisfactory risk-adjusted returns.
- Price indications for Little Rock are based primarily on the results of two portfolio sales of institutional quality assets. The first was the divestment of four assets by a public Reit to a TIC group. Buyer acquired 756 units of class-B product for $49.7mm ($65,750 per unit). RED estimate the average initial yield of the portfolio to be 6.0%. The second was a $50 two-property pool acquired by an out-of-state buyer. The pool consisted of 712 units, priced at an average of $70,200 per unit. The larger of the two was priced to yield a RED-estimated 5.1%, and the smaller of the two, located on the Riverwalk, generated an estimated 5.9% cash return.
- Cap rates for all Little Rock transactions average in the mid-6% range.

NOTABLE TRANSACTIONS

Property Name	Property Class	Date of Transaction	Total Price (in millions)	Price per unit	Estimated Cap Rate
Pleasant Valley Pointe (West)	BC	Jun-2007	$10.0	$89,152	5.8%
Chenal Lakes Phase I (West)	BC	May-2007	$34.0	$74,561	5.1%
Brightwater (West)	BC	May-2007	$16.0	$62,500	5.9%
Riverwalk (West)	A	Dec-2006	$18.0	$68,702	6.0%







DEMOGRAPHICS & HOUSING MARKET

- Following a chilly first quarter, the Little Rock housing market thawed during the spring and summer selling season. The median price of a home reached a record $132,600 in June, up 3.4% year-over-year. Prices subsided slightly in 3Q07, falling to $131,600. This represented a 2.1% advance from September 2006.
- Value data from the Office of Federal Housing Enterprise Oversight was more upbeat. OFHEO aver that Little Rock home values increased by an average of 4.59% in the 12 months ended in September. This ranked 70th among the nation's top 287 metro areas. On the other hand, the agency found that prices increased only 0.3% in 3Q07.
- Metro population increased 10,204 (1.6%) in 2006, the largest absolute gain since 1974, and the fastest one-year growth rate since 1993. A surge of domestic in-migration was primarily responsible.

EMPLOYMENT TRENDS

Past 12 Months

- Metro payrolls increased 5,900 (1.7%) jobs during the 12 months ended in October. The result is marginally slower than the decade high 6,800 (2.0%) jobs added in the same period of 2005 and 2006.
- Robust growth in skilled services industries and the hospitality sector contributed to the positive result. Business services added 1,200 (3.0%) jobs, despite some slowing in recent months. The health care / education services industry hired a net of 1,600 (3.6%) employees, as Little Rock's status as the regional medical services center grew. The build-out of Little Rock's restaurant, food service and hospitality sector contributed to a 1,600-job add in the leisure service super-sector, also representing a 3.6% advance. Only durable-goods manufacturing trends were demonstrably weak. The sector lost -200 net jobs for a –2.1% annual rate of decline.

Third Quarter 2007

- Employment growth accelerated in the third quarter after a mid-year slowdown. Total metro payrolls increased at a 6,800 (2.0%) year-over-year pace, up from a 5,100 (1.5%) annual pace in the first half of the year. A rebound in business services expansion was the principal catalyst, with help from retail trade and food services.

Forecast

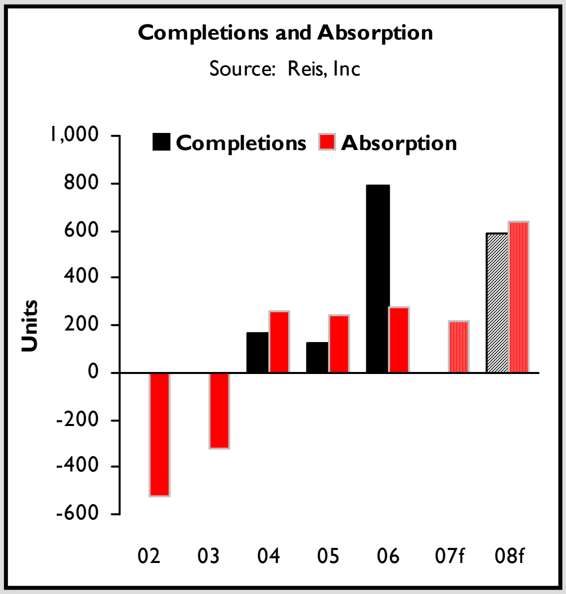
- **RED Research** expect the Little Rock economy to continue to exhibit stable, above U.S. average growth in 2008. The firm's econometric payroll model yields a forecast interval for average job growth ranging from 5,000 to 8,000 for FY2008, with a point estimate of 6,000. National City Bank economist Dr. Richard DeKaser expects the U.S. economy to rebound with some degree of vigor in 2009 (2.9% GDP growth rate). Although **RED Research** did not explicitly forecast Little Rock performance for 2009, it is likely the payroll growth will rise moderately relative to 2008's result in keeping with firmer national trends.
- Although the Reis data series is not deep enough to support a probabilistic total return analysis, Little Rock's low occupancy and rent volatility would likely give rise to an attractive risk-adjusted return profile. While expected returns are likely to fall below the **RED 50** average, the low-degree of implied risk would make metro investments attractive to risk-averse yield buyers or portfolio investors seeking to reduce expected portfolio volatility.

SUBMARKET TRENDS

Submarket	Effective Rent			Physical Vacancy		
	3Q06	3Q07	Change	3Q06	3Q07	Change
Downtown/South	$459	$480	4.6%	6.8%	7.0%	**20 bps**
Central	$598	$589	-1.5%	5.8%	9.0%	**320 bps**
West	$658	$686	4.3%	6.2%	5.8%	**-40 bps**
North Little Rock	$556	$566	1.8%	7.3%	8.2%	**90 bps**
Metro	**$593**	**$584**	**1.5%**	**6.4%**	**7.6%**	**120 bps**

SUPPLY TRENDS

- The Little Rock apartment market added a decade high 792 investor grade units to inventory in 2006, according to Reis. The impact on average occupancy was significant. As noted in the table above, occupancy fell sharply last year, due in large part to the supply factor, exacerbated by faster migration of tenants to homeownership.
- Through 3Q, Reis record no new supply in 2007. A local source proffers a different view. In comments published in July, this insider estimated 2006 supply at approximately 1,400 units. During 2007, the source reported six project completions totaling 1,600 units, including Riverpointe; Parc at Maumelle; Foothills; Palisades at Chenal Valley; Highland Pointe; and Chapel Ridge of Sherwood (Reis data indicate that some of these projects were delivered in 2006, while others are project phases with fewer than the reported number of units). The source expected 600 to 800 units to be delivered in 2008.
- Reis estimate 2008 deliveries totaling 584 units. The service has no other projects on the radar screen scheduled for delivery prior to 2011.
- Reis report that the Parc at Maumelle and Highland Pointe were better than 90% occupied at September 30, 2007, suggesting that new properties leased up at a brisk clip last year.



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