



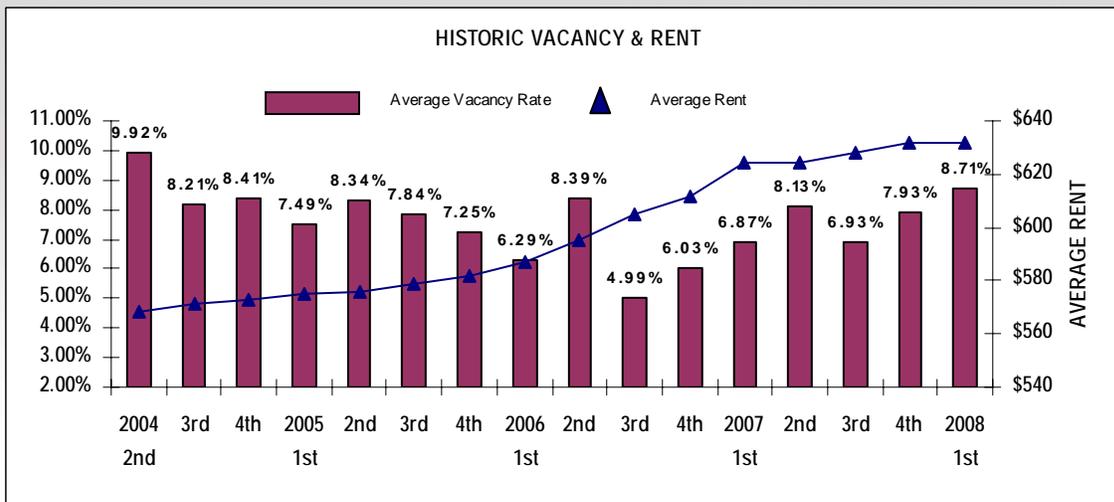
WINTER CHILL

As expected, the past quarter has seen operating fundamentals continue on their mild downward trend. Vacancy in the first quarter continued to rise, up to 8.71% from the 7.93% experienced at year end. Expect vacancy to increase an additional 1% to 2% during the second quarter as it typically does each year when students and seasonal visitors leave town. This will bring vacancy to about 10% by the end of June, but we should see an improvement in the 3rd and 4th quarters of the year. More disturbing than the small increase in the vacancy is the negative net absorption of 1,215 units year over year. Absorption will have to turn positive to turn around the vacancy factor even with the extremely low amount of new construction planned.

Interestingly, A properties have been affected less by this downturn than B and especially C properties. C properties have felt more of a negative impact from the loss of construction-related jobs and the Arizona employer sanctions laws. Properties may be experiencing some positive effects from potential home owners opting to rent instead of buying in the current market of declining home values. However, A properties are also experiencing competition from the shadow market of rental homes. All said, the A properties are faring better. In fact, some areas with a high % of A and B properties such as the Foothills and Oro Valley showed improvements in occupancy in the quarter.

A BIT OF SPRING WARMTH

The student apartment market is showing a bit of warmth in an otherwise cold environment. With Student enrollment increasing (the U of A is again expecting its largest freshman class ever) and student retention rates slowly improving (both of these being stated goals of U of A President Robert Shelton), the demand for housing near the U of A is at a peak. Rent up for the fall semester at student apartments both near campus and further off campus is going very well, and owners have been able to increase rental rates at a rate greater than the rest of the marketplace. Properties in close proximity to the U have done particularly well and will do so for the foreseeable future. Reasons being that the University is slow to respond to housing demands, and developable land for new housing is at a premium and hard to find.



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DEEP SLEEP – INVESTMENT MARKET FROZEN

While the Tucson apartment operating environment has been in a mild winter chill, the sales market has essentially been in a deep freeze. This is in keeping with market activity throughout most of the country except for a few countercyclical markets such as Houston. The chart below shows that sales activity is down almost 90% for the 1st quarter of 2008 as compared to 1st quarter of 2007! Merely 298 units of properties of 40 units or more closed during the first quarter compared to 2793 in 2007. The lower price per unit and price PSF is a bit overstated due to the quality and age of the few buildings that did sell.

The second quarter will show more activity however as there are a number of transactions in escrow which should close in the next 60 days. However, activity is still quite low. The issues slowing down the transaction volume, in my opinion, do not have to do with the credit markets and the inability to attain financing. The issues slowing the market include:

- ◆ Differences in Buyers and Sellers pricing expectations,
- ◆ More conservative underwriting by Buyers,
- ◆ A less than bright short term outlook on the AZ economy felt by many Buyers and;
- ◆ Many Buyers and Sellers simply sitting on the sidelines waiting to see how things shake out.

This will change with time as a clearer economic picture unfolds.

The question remains, how long will the slowdown last? I don't have the answer. However, the fundamentals for Southern Arizona remain strong and we are weathering the economic and apartment market downturn better than many other areas of the country. Tucson remains a great place to be an apartment owner with many positive long term trends still in place.

TUCSON APARTMENT SALES			
	1st Qtr 2006	1st Qtr 2007	1st Qtr 2008
# of Units	2,230	2,793	298
Total Sales \$	\$143,682,000	\$199,299,593	\$14,440,000
Avg Price/Unit	\$66,519	\$68,481	\$50,108
Avg Price PSF	\$76.20	\$84.05	\$77.91
Avg Year Built	1980	1983	1972