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Commentary

Market Opinions and Topics of Interest

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Owners' Equivalent Rent And The Relative REIT Indicator As 2010 Dawns

We concluded in [October 2009](#):

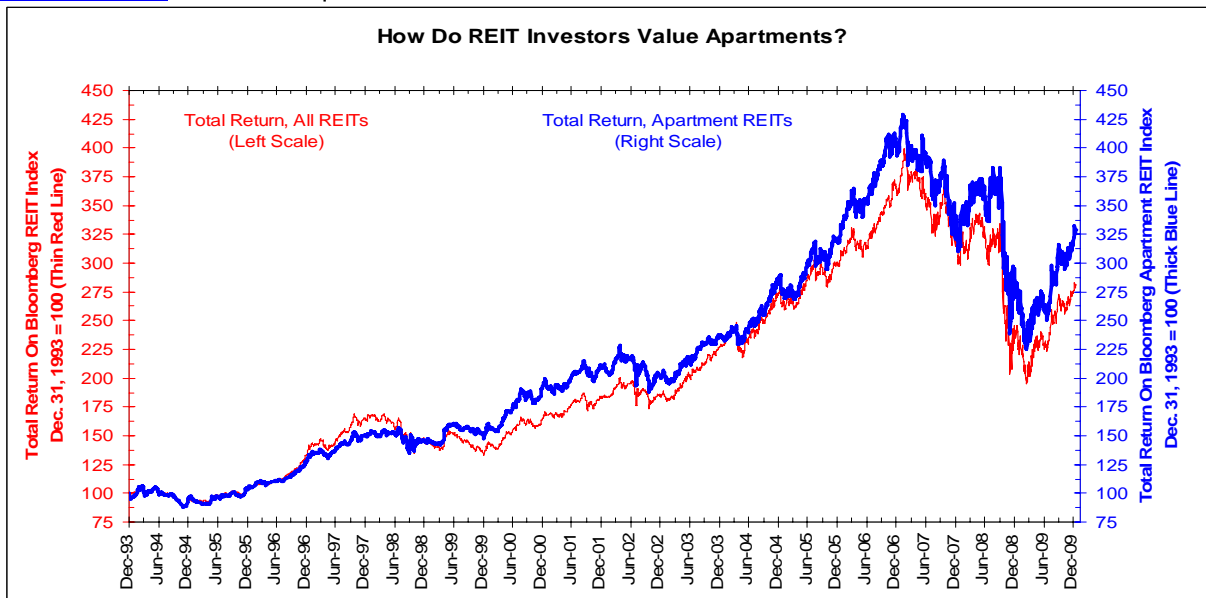
As the FOMC has stated its intention to wind down this facet of quantitative easing by the end of the first quarter of 2010, we should expect a shift at the margin from homeownership back to tenancy; this will support the OER indicator by the second quarter of 2010. Termination of the tax credit for qualified first-time homebuyers will have the same effect, if and when enacted.

The end of downward pressure on consumer price indices resulting from OER is coming into view.

As the FOMC stated its [mortgage-backed securities purchases will end](#) in the first quarter and the first-

time homebuyer [tax credit will end](#) for residences purchased after April 30, 2010, we should review the current state of affairs with OER and the REIT-based indicator first introduced in [May 2006](#).

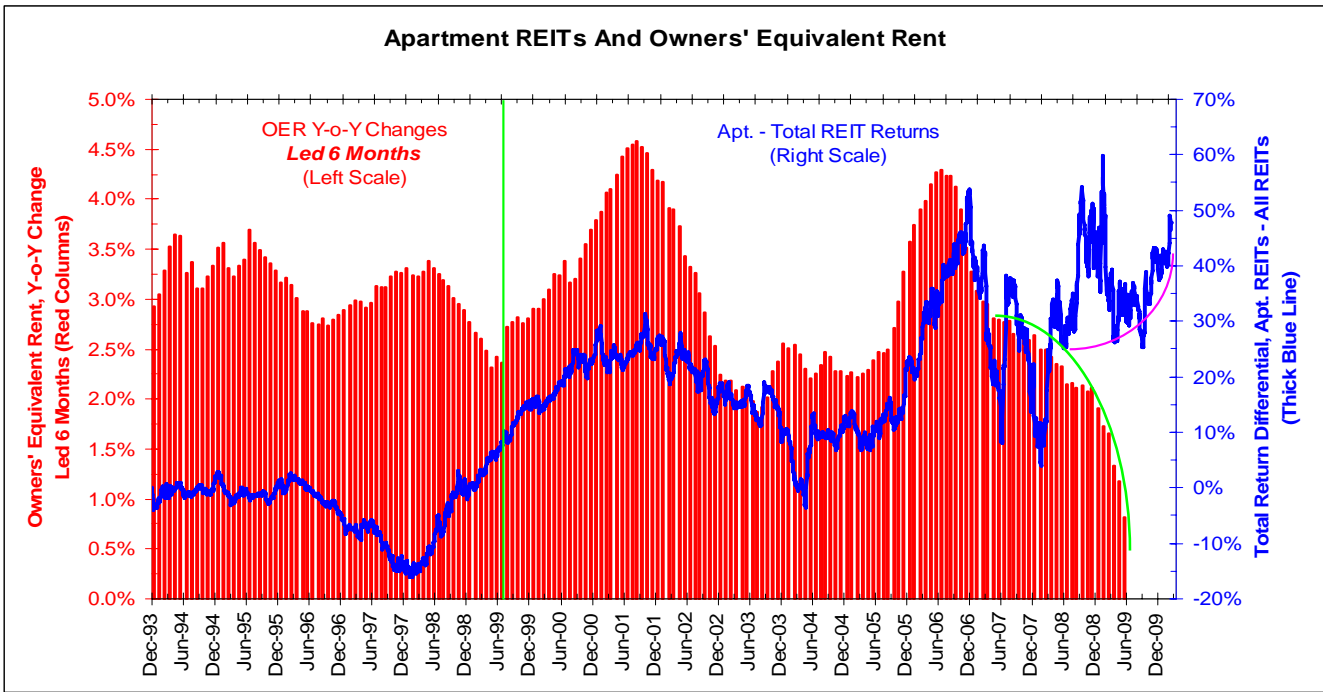
This indicator is based on the total return differential between apartment REITs (thick blue line) and all REITs (thin red line). OER increased 0.8% on a Y-o-Y basis versus 1.8% for headline CPI and 1.7% core CPI through November 2009. **This is consistent with the original hypothesis of OER following relative REIT returns: Total returns for all REITs have outpaced those for apartment REITs 120.26% to 107.04% since March 2009.**



Rents And REITs

If the last five months are any indication, the OER picture will stabilize or turn higher soon. The total return differential between apartment REITs and all REITs (thick blue line, both charts, following page) has led year-over-year changes in OER by six months on average since mid-1999 (green vertical

line). This differential peaked in early December 2008, and moved erratically lower through July 2009 and is now cleaving to a rising trend curve (magenta arc). **Year-over-year changes in OER itself have been in what technical analysts would recognize as a waterfall decline (green arc) since the financial crisis erupted in the summer of 2007.**

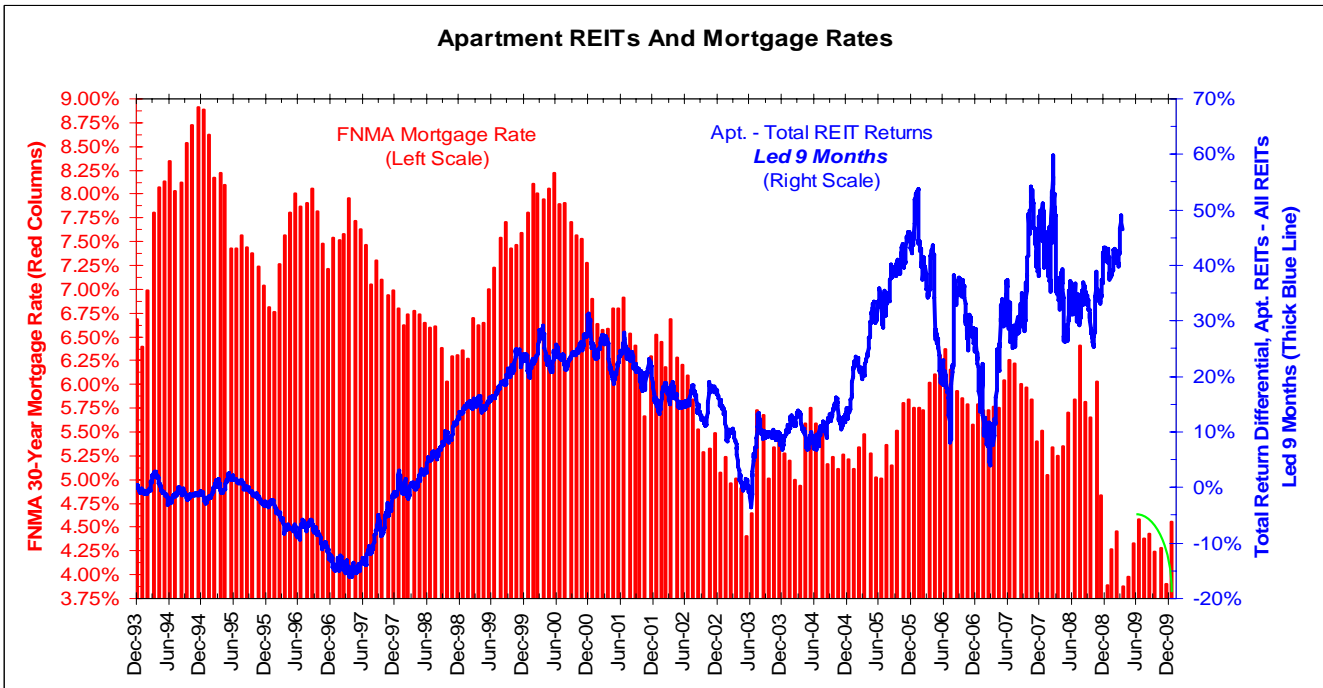


Conclusion

Mortgage rates (red columns), which had been pushed lower by the Federal Reserve's purchases of MBS, have broken out of their incipient waterfall decline (green arc). As the observed pattern has been for mortgage rates to lead the relative REIT return differential by nine months on average, we should view this upturn along with the imminent conclusion of the first-time homebuyers' tax credit

and the end of the Federal Reserve MBS purchases (Idle thought: When have two unprecedented interventions in a market ended simultaneously?) as putting the relative REIT differential under upward pressure.

The October 2009 conclusion of OER's downturn coming into view by the second quarter of 2010 is affirmed.



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