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MID YEAR 2008
MARKET REPORT AND FORECAST

For the first time in 22 years of collecting and writing on the North Georgia real estate market, Norton Native Intelligence is publishing a **Mid -Year Report and Forecast**.

For the last 18 months the regional real estate market has moved with such downward velocity that it makes even the strongest person's head spin. While there are great opportunities amidst the hubris and rubble, the soundings are at best confusing and sobering as **Reality** is taking hold of the marketplace. The clear picture as the dust of foreclosures, banking stress and declining consumer confidence levels settle is that:

- The development engines produced too much residential product in the wrong price ranges using misguided proforma economics for sustained housing demand.
- The reality of too much money flowing into the market 2001 to 2005 has set in. The fundamentals of lot cost to construction cost ratios, supply and demand, absorption rates, rates of return, equity ratios and credit scoring were largely ignored in the midst of reported exorbitant profits.
- Banks have moved from a "state of denial" to a "state of shell shock" as the developers interest reserves dwindle and the buyer interest slow down, lengthens.
- With inventory peaking in late 2007 and new construction starts plummeting, the appetite at the development buffet will start to return to normal in the second half of 2008 and continuing through 2009. The bouncing-along bottom experienced so far in 2008 will see a slight lift-off over the next 2 quarters.
- Despite reports to the contrary, houses are selling every day. Mortgage companies have money to lend and are anxious to qualify prospective buyers. Small industry is still producing strong goods and services and North Georgia comparatively…is weathering the storm better than most communities.

As a loyal reader and follower of our annual prognostications, you will see that we have departed from our traditional Top 10 Trends in order to focus succinctly on the core of the real estate components.

Single Family Resales
Inventory (FMLS/MLS) peaked for resale homes in November 2007 and statistically has been in a decline ever since. At Mid Year some 19,995 resale homes are for sale throughout the Atlanta and The North Georgia service area or a 10.8 month supply. The Northern arc of counties has the following supplies of homes.

County	Month of Supply	County	Month of Supply
Banks	10.6	Hall	12
Barrow	7.8	Jackson	16.6
Cherokee	10.4	Lumpkin	10.1
Dawson	17.6	Rabun	24.5
Forsyth	8.9	Stephens	13.73
Gwinnett	10.5	Walton	12.67
Habersham	13.47	White	17.39

(Equilibrium might be 8.5 months of supply)
Source: Norton Native Intelligence™ FMLS/MLS

Only the most motivated of sellers have their homes for sale (those that have needs of relocation, family size changes, financial stress or health issues). Asking prices are for the most part the most realistic in decades…cutting through the hope and prayer, winning the lottery attitudes and cashing- in euphoria…now to the core of real value. Buyers of homes in the last 6 months have taken advantage of price concessions and capitalized on motivated sellers to stretch their home-buying dollar. More house, more value than perhaps in the last 5 years. Resale sellers must price their product against the competing developer inventory or bank foreclosure down the street. Norton Native Intelligence™ sees the buying window only open for strong capitalistic purchases during the next 2 or 3 quarters then drying up with home shortages in some price points surfacing.

New Single Family Construction

Inventory peaked in October of 2007 and builders have been strategically dumping inventory overboard to reduce the load on their sagging life boat. Concessions on new product (depending on original offering price points) range from $17,000 to as high as $70,000. The inventory of major institutional builders, for example (Centex KB Homes, Pulte, and DR Horton) is surprisingly low at 3 to 4 months of inventory. It's the midsize builder that overshot the mark on supply and price points. Norton Native Intelligence™ January 2008 prediction of a lot and housing shortage is now fulfilled. New homes under $250,000 have moved briskly, lot inventories for the same workforce housing are moving to critically short levels. With very few signs of development life out there, the engine for this market segment has been shut off and shortages starting in August, may last 24 to 30 months. This could have an unintended consequence on industrial recruitment and business growth since an expanding labor force is dependant upon available housing inventory in this segment of the market. New Homes supplies by micro-market are as follows:

County	Month of Supply	County	Month of Supply
Banks	8	Hall	10.1
Barrow	9	Jackson	11.4
Cherokee	9.5	Lumpkin	10.5
Dawson	12.5	Rabun	12
Forsyth	9.8	Stephens	8
Gwinnett	11.2	Walton	11.4
Habersham	10.5	White	12.5

(Equilibrium might be 9 months of standing completed inventory)
Source: Norton Native Intelligence™ FMLS/MLS

New Homes Communities

The heavy overbuilding in outlying markets of North Cherokee, North Forsyth, Dawson, North Hall, Jackson and Walton gives the entire market a Monday morning hangover. Norton Native Intelligence™ and its sister investment arm Southern Capital Funds have been tracking the deterioration now for 5 quarters and pegs the new homes community stress at in excess of $2 billion in development value. Norton Native Intelligence™ predicts that 30 to 40% of the 2007 existing product will be under bank or financial institution control in 12 months. Traffic in new home communities has been spotty, many look abandoned, some ravaged by subprime foreclosures, others half-finished as the developer lost steam in other markets. We see great builder incentives and stepped- up marketing efforts with unbelievable value pricing. Going forward, builders and developers will have limited specs available (their lenders won't let them) and will work out of more "model" villages, requiring substantial down payments for presale construction and permanent loan take- out commitments.

Developed Available Lots

The inventory of completed lots peaked in the first quarter of 2008 as those developments with financing in place completed their pipeline of construction. With few exceptions (Village of Deaton's Creek in Hall County) the new lot development process has come to a grinding halt. While shortages are already appearing (homes under $200,000) Norton Native Intelligence™ does not for see any uptick in development of new lots or the completion of 2nd and 3rd phases of standstill developments for 18 to 24 months. No right- minded small bank board would approve an A & D (acquisition and development) loan while continuing to face the fundamental struggles, stresses and foreclosures of some of their oldest, most loyal developer borrowers. Mind you, Norton Native Intelligence™ thinks this posture is short-sided. **Work force housing**, not row after row of petite McMansions is the true market for North Georgia. <u>Our demographics are solid; the deepest part of the housing pool is under $250,000</u> contains as strong a current of buyers as the Mississippi.

Mid-Year months of lot supplies are projected by Norton Native Intelligence™ as follows:

County	**Month of Supply**	**County**	**Month of Supply**
Banks	45	Hall	60
Barrow	50	Jackson	124
Cherokee	52	Lumpkin	50
Dawson	91	Rabun	65
Forsyth	56	Stephens	45
Gwinnett	60	Walton	106
Habersham	50	White	80

(Equilibrium is estimated to be 25 months of completed lot supply)
Source: Norton Native Intelligence™ Metrostudy's

The opportunities abound for small lot group purchases and custom home lot seekers; they may find themselves the only buyers and can virtually name their price during this window of **extreme** opportunity.

Raw but Entitled Property
During the last days of the 2000's real estate boom, developers worked feverishly to entitle/zone property in advance of new impending government regulations. Fast forward only 18 to 24 months and those same holdings sit languishing on the sidelines, a common casualty of the market's overestimation of needed supply. Mostly located in outlining areas (see above), they have **some** value…<u>Just not right now</u>. The existing lot inventory must be absorbed in good order before values return. Unless these have hope: economics, zoning for work force housing, it is best that these are placed in suspended animation for now.

Raw Land Unzoned
For the most part, we must readjust our thinking on raw land holdings. Without immediate speculative value and in the face of mountains of lots piling up, raw land is no longer an ATM machine, 401K or a pot of gold at the end of the rainbow. Strategic holdings in the direct line of growth will rebound swiftly, but the raw land properties stuck in the nooks and crannies of North Georgia hinterlands will return to pre -2000 values. Land for agriculture, recreational use, aesthetic and enjoyment <u>is always in demand.</u> Rolling gentlemen farm property will always have intrinsic value but the rest of the landed gentry will have to wait for their windfall.

Foreclosures
While North Atlanta foreclosures in 2007 were dominated by builder/developer takebacks, the individual foreclosures will dominate 2008. We are a lucky market. The subprime phenomena is largely confined to South Atlanta and isolated pockets in Dekalb and Fulton. The only subprime effect we see in North Georgia is the large number of Hispanic defaults which we point to predatory Hispanic lenders preying on our market from 2001 to 2005. Stressed borrowers exist in every market. The workforce buyer stretched their borrowing capacity

well beyond their reasonable means. Housing went from 25% of adjusted gross income to averaging 40% and many borrowers counted on overtime and bonuses to round out their family expenses. Low interest rates and great housing programs gave many buyers too much incentive to stretch their home-buying ability. We saw strong evidence of this when first time home buyers were purchasing 2,700 to 3,000 square foot homes vs. work force housing product of 1,500 to 2,000 square feet. The market just has to be allowed to digest the foreclosures along with the other products. Norton Native Intelligence™ believes, barring a catastrophic rise in unemployment, the foreclosure wave will last no more than 16 to 18 months forward. That means great buys for 18 to 24 months on individual use homes, second homes and rental potential investments.

Condo Market

Attached zero lot line or stacked unit condo product has not fared well in North Georgia. Developers need to remember that Americans moving out to the Hinderlands (that's us) want **space**. The product is right on target for some small part of the buyer market (2 to 7%), those wanting zero maintenance to lock and go or affordable luxury at a small price (look at isolated lake condos). The last half of 2008 and 2009 will see major stress in the overbuilt National and Atlanta condo market but will have little if any effect on our market since the problems and noise will be focused to our south.

Single Family Rental Homes

We see super strong rental activity especially where the monthly rental is $1,200 and below. It's that price point that remains **attractive** to post foreclosure families who want to transition into a single family home rental (with a yard, verses taking a bigger step backwards into an apartment). For the astute buyer look for low maintenance homes in neighborhoods not dominated by other foreclosures and in marketable elementary school districts.

Multi-Family

With occupancies on the rise, rates increasing and home buying programs absent in the market, we see the multi-family economics (both investment and development) becoming once again an attractive investment vehicle. Gwinnett County has already seen an uptick in multi-family development plan submissions and if leading indicators continue, we could see a mini development explosion in 2009. Rents will rise through 2010 as consumer confidence keeps qualified buyers in the rental pool along with hardship renters and post foreclosure families.

Industrial

Transportation and fuel cost are on the minds of every industry both large and small. The ability to pass on added fuel charges is limited by the market pressure on available goods and services. We see limited industrial expansion for the next 6 to 9 months as business leadership studies the energy and transportation effects on their individual product and distribution network. Long term, industrial parks along the major transportation corridors of I-75 and I-85 will benefit the most and those with quick on-and-off logistics capturing the strongest market share of uses. GA 400, I-985 and GA 316 will continue to attract those industries wanting ease of access to North Atlanta markets and not the cross county tracks to I-85 or I-75. Rest assured, traffic congestion, bottlenecks and idling times are on the mind of every small industrialist.

Retail/Commercial

Food and drugs remain the king, **Long Live the Kings**. While large and mid-big box users are playing a wait and see strategy with consumer confidence, the food and drug components are playing a game of catch up and market positioning with the past 10 years of roof top growth. Forsyth, Hall, Cherokee and Barrow are all clearly under-retailed and the next tier of counties Dawson, Lumpkin, Rabun, Habersham and Jackson demographics also get the majority of their goods and services out of county. We see strong retail centers emerging at GA 400/Highway 60, GA 211 & Thompson Mill Road and GA 400/US 141. The soft spot is among the small mom and pop entrepreneur side shop space tenant which like the big box (Wal-mart, Target) leaders is too concerned with consumer confidence levels to risk expansion or start up new concepts.

Office

The office markets of Clarkesville, Gainesville, Lawrenceville, Buford, Cumming, Jefferson and Commerce continue to have small professional leasing expansion dominated by legal and accounting sectors. The bank consolidation by SunTrust/GB&T and Regions coupled with the start of City Center in Downtown Gainesville will put pressure on occupancy levels but the achievement of new rates at City Center will pull rates for other class A space upward as it breaks new ceilings for suburban Atlanta rental rates.

Medical Office Space

This product type is proving recession proof as medical projects are out of the ground or in proposal stages across the face of the mountain region. The solid foundation of medical facilities in Lumpkin, Forsyth, Johns Creek, Habersham, Toccoa and Gainesville will continue to have major medical office influences on the direct service areas. New facilities at River Place (Chateau Elan) and smaller medical components in Cleveland, Jefferson and Dawsonville will stimulate the need for more feeder network medical offices. In case anyone missed it MEDICAL is big business in our region and a magnet for quality support services…an added plus in an age of uncertainty.

Hotel/Motel

This is an emerging sector in North Georgia. Once dependant upon the business travelers, the recreational tourist and an occasional convention now and then, the foundation has been laid for a strong hospitality sector in all reaches of our 30 county study. New hotel/motels are under construction or proposed in almost every market Flowery Branch, Braselton, Commerce, Jefferson, Forsyth and Cherokee and major upgrades to Lake Lanier offerings set the stage for the next generation of hospitality development. With gas prices still soaring look for shorter run travel (interstate vs. intrastate). The important factor is that North Georgia playground is adjacent to 6 million potential customers (Atlanta).

General Investments

The strong investment buyer cash in hand still outpaces the availability of quality product 10 to 1. Pressure on cap rates continues as does "cash on cash" calculations. It is a **buyer's market** for at least the next 18 months. Changes in tax laws, depreciation and capital gains may alter that formula some, but it's way too early to forecast. Hometown investing, that is putting hard-earned investment money in your own backyard still is the preference for the small investor, only now we seem to be competing with out-of-towners who see the attractiveness and opportunities in our vibrant region. At times it's the forest for the trees syndrome. Invest here the opportunities are unlimited.

Senior Housing

With the phenomenal success of The Villages of Deaton's Creek (thank Vintage Communities and Del Webb/Pulte) the mark has been set on our area as the next retirement Mecca. Our region's story is too compelling…attractive lifestyle components, reasonable land and infrastructure cost, low taxes, great healthcare, close proximity to urban attributes, forests, trees, lakes, recreational "stuff to do"…all give our region THE EDGE. Despite the housing slow down and missteps by Levitt and Sons, we are encountering copy cat developers across the country interested in putting their toe in the retirement water of North Georgia. We are confident that over the next 5 years we will see a waterfall of retirement and active lifestyle product come our way. The downside for that market today is 70 to 80% of the buyers have another house to sell.

Second Home

As the primary home market slowed down, the second home market came to an abrupt halt. A second home is a discretionary expense that can be delayed until times get better or the waters calm. Second home developers have been caught by the shift in market and like their primary home developer cousins are experiencing extreme stress. But this too shall pass. The good news is that while some speculative second home development did occur, it was only a small fraction that of the primary home glut. Yes, there are way too many hard to construct mountainside lots available, but the market is largely a custom home one with those properties quickly absorbed once consumer confidence settles mid 2009. Once reignited, developers and builders need to remember that most (85%) of 2nd home buyers in our region are price sensitive, there is virtually no rental market to fall back on and its hard to justify a mega purchase for only occasional recreational use. The deepest part of this second home market is $200,000 to $400,000 much more than that and the risks for sales failure accelerate.

Lake Lanier

What goes down must come up...We hope and pray. Well absolutely…cycles come and go as we have seen for 50 years now, El Nina vs. El Nino...The pain continues. We project that with moderate rainfall, Lake Lanier could fill up by spring of 2010, but that the fall of 2009 will set month by month new lows. This, of course, has greatly affected the velocity of home sales on Lake Lanier for the first 6 months of 2008. 55 homes with private boat docks sold and closed compared to 99 homes in the same period of 2007 and 132 homes in 2006. But while the unit count is off by 44% the per house average sale price was only off 2%. $634,000 in 2008 to $645,000 in 2007. This points to the resiliency of the Lake Lanier market's ability to weather most any storm (or lack thereof). By year end 2008, we project lake sales will register at the same level as those sold in 2003. For those wanting to buy in on Lake Lanier this is THE TIME to buy the most house possible.

Market Rap Up

It's the bottom of the ninth inning, second game of a great double header. Score tied, 2 outs and the superstar player in the batter's box has 2 strikes, bases are loaded…Will the market produce a homerun of a recovery? The opportunities are clearly there. Everyone sits, waiting on the edge of their seat for what happens next…

Norton Native Intelligence™ sees the bottom and in fact believes we've been bouncing up and down on bottom for several months now. Housing led us into this credit crisis and this downturn. It is likely to lead us out and that process is underway, right now. Our market is on a solid firm foundation, our recovery will be faster because of our demographics and the strength of our fundamentals. Yes, pain is everywhere, but so is OPPORTUNITY. We must lift ourselves up, clear our way through the smoke and fog and seek a clear path to capitalize on those opportunities. *"When everyone is being greedy, be fearful. When everyone is being fearful, be greedy". Warren Buffet.* We are prepared to make lemonade out of lemons. ARE YOU?

For expert straight up advice and professional real estate brokerage service call Norton.

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