SAN JOSE, CALIFORNIA

MARKET OVERVIEW & MULTIFAMILY HOUSING UPDATE

RED Capital Group | 3Q15 | DECEMBER 2015

PAYROLL JOB SUMMARY

Total Payrolls	1,061.1m
Annual Change	56.0m (5.6%)
RCR FY15 Forecast	54.4m (5.4%)
RCR 2016 Forecast	39.3m (3.7%)
RCR 2017 Forecast	33.1m (3.0%)
RCR 2018 Forecast	26.3m (2.3%)
RCR 2019 Forecast	18.5m (1.6%)
Unemployment (NSA)	4.0% (Oct.)

3Q15 PAYROLL TRENDS AND FORECAST

The Santa Clara County labor market steadfastly refused to succumb to entropy as it followed a rocket like trajectory higher. San Jose payrolls increased at a 56,000-job, 5.6% year-on-year rate during the third quarter, on par with 2Q15 and otherwise the strongest quarterly growth recorded in 15 years. Professional, technical and scientific services continued to provide the principal impetus: concerns in this subsector expanded at a 16,900-job, 12.5% annual rate, fastest since 1997. Web hosting and software publishing also flourished, as information service sector employers hired at a 9,300-job, 13.6% pace.

Conversely, seasonally-adjusted data exhibited a decelerating trend. Expressed on this basis, headcounts increased only 6,000 jobs sequentially, the smallest quarterly advance posted since 4Q11. This phenomenon most likely stems from statistical issues in seasonal adjustments than an actual decrease in the rate of San Jose job growth.

RED Research analysis found that 98% of changes in San Jose payroll growth can be explained by an equation employing current and lagged U.S. payroll and nominal GDP and current metro personal income growth as independent variables. The 0.6% standard error equation projects gradually decelerating job gains for the 5-year forecast, consistently at two or more times the U.S. mean.

OCCUPANCY RATE SUMMARY

Occupancy Rate (Reis)	96.7%
RED 50 Rank	13th
Annual Chg. (Reis)	-0.8%
RCR YE15 Forecast	97.0%
RCR YE16 Forecast	96.9%
RCR YE17 Forecast	97.0%
RCR YE18 Forecast	97.0%
RCR YE19 Forecast	97.0%

3Q15 ABSORPTION AND OCCUPANCY RATE TRENDS

Reis report that demand for San Jose apartment space improved during the third quarter as renters leased a net of 611 vacant units, up from 441 in the prior quarter. Supply played a large part of it: developers completed 1,360 units, the largest quarterly vintage in two years. As a result, occupancy declined 60 basis points sequentially and 80 bps year-on-year to 96.7%, lowest in over four years.

Axiometrics surveys of 233 stabilized, professionally-managed properties arrived at a similar conclusion. Occupancy averaged 95.9%, down 70 bps y-o-y. Class-C properties recorded the highest occupancy (96.5%) for at least the fifth consecutive quarter, followed by classes-B (96.0%) and –A (95.5%). East S.J. (96.7%) posted the highest levels among submarkets, with Cupertino and South S.J. (each 96.4%) close behind. Every submarket notched a 95.6% rate or higher. Twenty properties in lease-0up absorbed an average of 17 units/month, down from 19 during 2Q15.

RCR specified a 96.1% adjusted-R^2 (S.E.=0.2%) occupied stock growth model using the rate of change of inventory (+) and job (+) growth as independent variables. The model projects that demand is likely to lag slightly through 3Q16, causing occupancy to fall about 10 bps. Otherwise, demand and supply should remain in sync for the balance of the 5-year forecast, maintaining occupancy around 97%.

EFFECTIVE RENT SUMMARY

Mean Rent (Reis)	$2,023
Annual Change	8.5%
RED 50 Rent Change Rank	2nd
RCR YE15 Forecast	7.4%
RCR YE16 Forecast	3.3%
RCR YE17 Forecast	5.5%
RCR YE18 Forecast	4.9%
RCR YE19 Forecast	4.4%

3Q15 EFFECTIVE RENT TRENDS

Reis upwardly revised year-on-year rent growth metrics for each of the previous four quarters, increasing average annual growth during the period from 9.0% to 9.5%. Growth decelerated for the third consecutive quarter, however, slowing from 8.9% to 8.5% in 3Q15. Sequential quarter growth also declined materially, falling from $82 (2.9%) in 2Q15 and $44 (2.4%) in 3Q14 to $41 (2.1%).

Axiometrics same-store, stabilized property comparisons recorded a similar pattern. Rent growth was very robust during 3Q15, rising 10.1% year-on-year, but moderately slower than each of the previous four quarters. Class-C posted the fastest gain (10.7%) and was the only class to record sequential quarter acceleration. Class-A and –B advanced by 8.7% and 10.1%, respectively. Five submarkets chalked down double-digit growth, led by Campbell (15.8%) and East S.J. (12.7%). Cupertino (5.5%) lagged.

RCR finds that personal income growth (+) , the rate of change of job growth (+) and current vacancy (-) are the most statistically significant predictors of S.J. rent trends. An equation specified with these variables (ARS=97.8%/ S.E.=1.5%) anticipates further deceleration through 2016, followed by reacceleration to a 5.7% peak during 2Q18.

TRADE & RETURN SUMMARY

$5mm+ / 60-unit+ Sales	1
Approximate Proceeds	$16.3mm
Average Cap Rate (FNM)	4.4%
Average Price / Unit	$242,537
Expected Total Return	7.0%
RED 46 ETR Rank	21st
Risk-adjusted Index	2.94
RED 46 RAI Rank	45th

3Q15 PROPERTY MARKETS AND TOTAL RETURNS

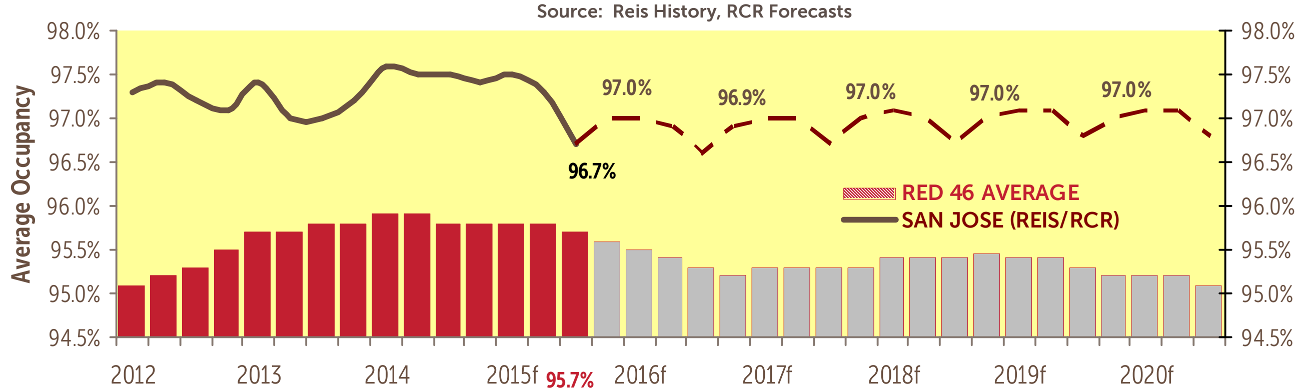
The pace of South Bay multifamily property trades ground to near standstill during the second half of 2015. Only one property of 60 or more units exchanged hands during the third quarter and only two trades were recorded in the fourth through the first week of December. Proceeds totaled $16.3 million during the third quarter and were $340 million 4Q15 quarter-to-date in December. The average price of 2H15 traded units was $274,249, up from $218,815 during the first half, when six trades for total proceeds of $270mm were consummated.

Traded properties largely consisted of 30- to 50-year old class-B– or class-C assets. Cap rates for market rate properties of this nature fell in the high-4% to low-5% range. A class-B property with repositioning potential closed during 4Q15 at an approximate 4.2% cap based on in-place NOI.

In light of what appears to be a distinct imbalance between demand for San Jose properties and their availability, RCR elected to trim 20 basis points from the purchase cap rate proxy to 4.3%, 10 bps above San Francisco's. Using this level, a terminal cap rate of 5.0% and model derived rent and occupancy point estimates, we calculate that an investor would expect to achieve a 7.0% total return on a San Jose asset, ranking 21st among the RED 46 markets. High rent model standard error hampers risk-adjusted returns, however; the risk-adjusted index (2.94) ranks only #45 among the peer group.

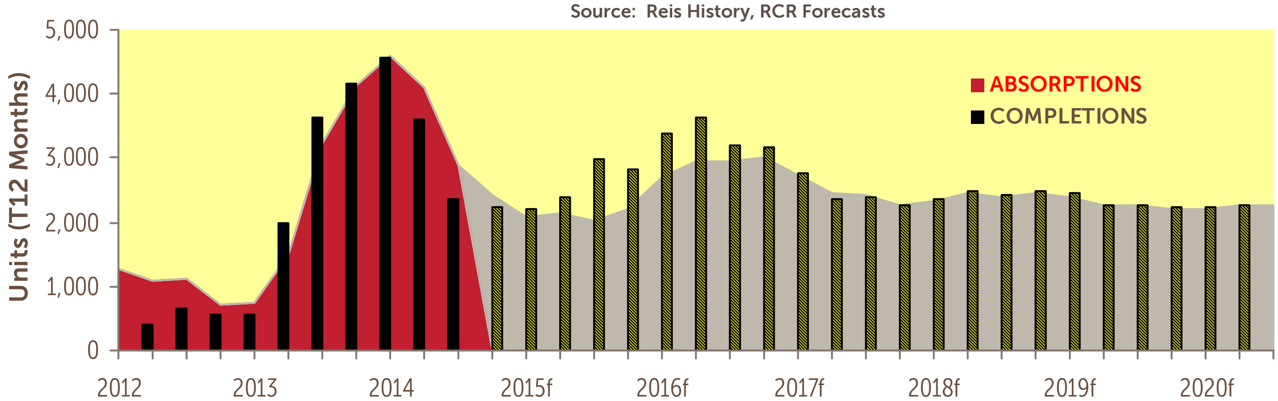
San Jose Occupancy Rate Trends

Source: Reis History, RCR Forecasts



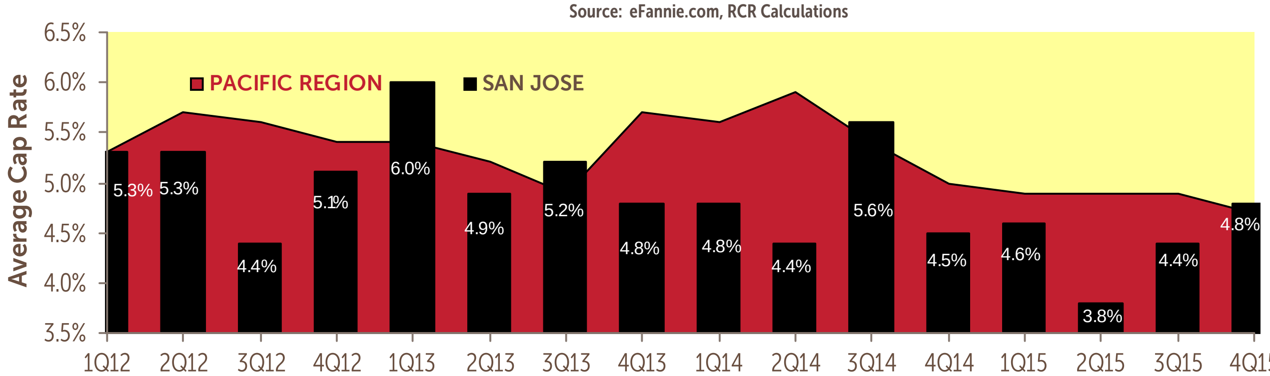
San Jose Absorption and Supply Trends

Source: Reis History, RCR Forecasts



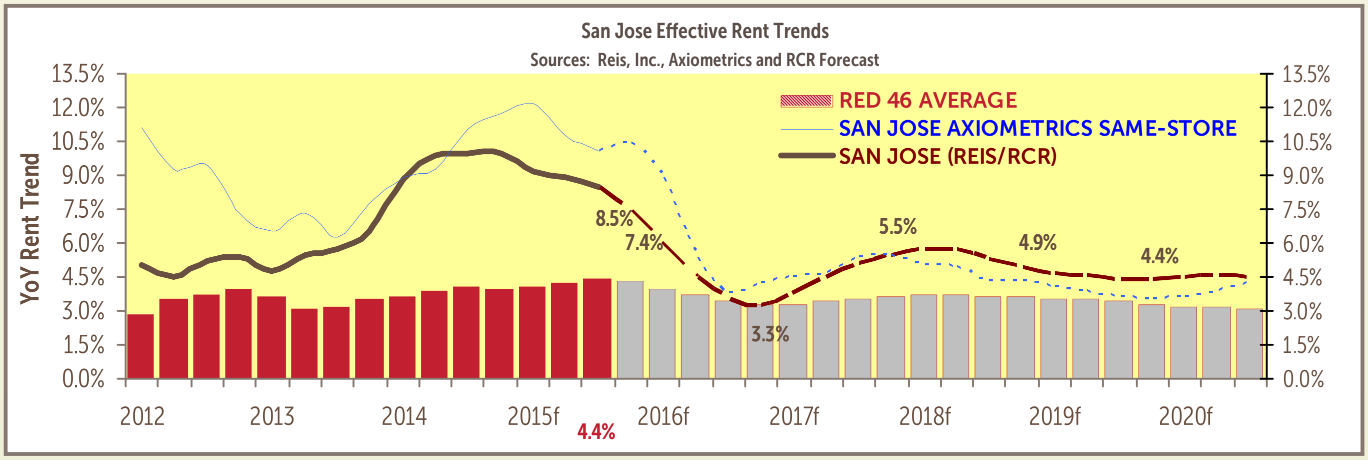
San Jose Cap Rate Trends

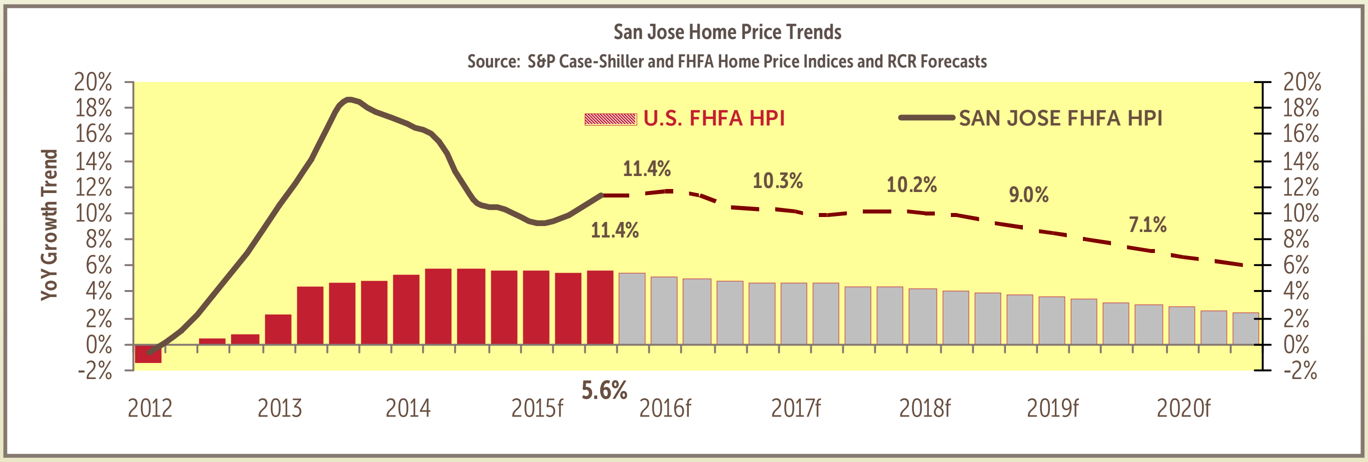
Source: eFannie.com, RCR Calculations

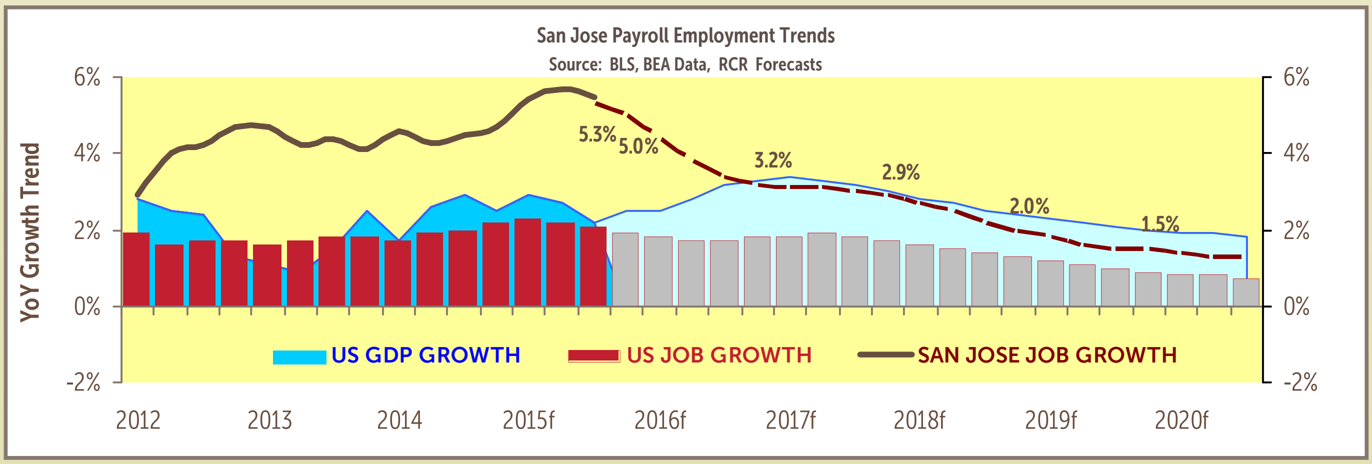


NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/ Type (Constr.)	Approx. Date of Transaction	Total Price / (in millions)	Price / per unit	Estimated Cap Rate
Thornbridge Apt. Homes (South San Jose)	B- / GLR (1976)	20-May-2015	$50.1	$175,175	5.7%
720 North (Sunnyvale)	C / GLR 1965	20-Jun-2015	$29.8	$256,897	5.2%
Village Park (Central San Jose)	B- / GLR (1970)	10-Jul-2015	$16.3	$242,537	4.8%
Waterstone San Jose (South San Jose)	B / GLR (1988)	6-Nov-2015	$160.0	$370,370	4.2%

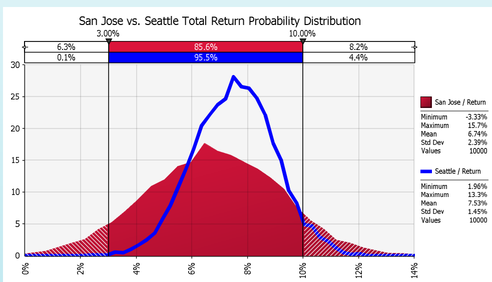

San Jose Effective Rent Trends
Sources: Reis, Inc., Axiometrics and RCR Forecast
YoY Rent Trend
RED 46 AVERAGE
SAN JOSE AXIOMETRICS SAME-STORE
SAN JOSE (REIS/RCR)
8.5%
7.4%
5.5%
4.9%
4.4%
3.3%
4.4%
2012
2013
2014
2015f
2016f
2017f
2018f
2019f
2020f

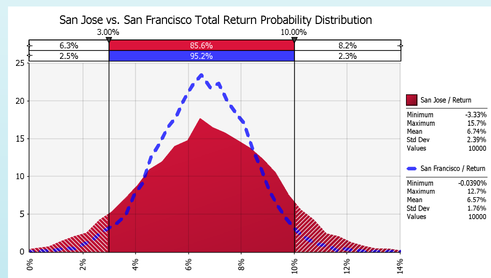

San Jose Home Price Trends
Source: S&P Case-Shiller and FHFA Home Price Indices and RCR Forecasts
YoY Growth Trend
U.S. FHFA HPI
SAN JOSE FHFA HPI
11.4%
10.3%
10.2%
9.0%
7.1%
11.4%
5.6%
2012
2013
2014
2015f
2016f
2017f
2018f
2019f
2020f

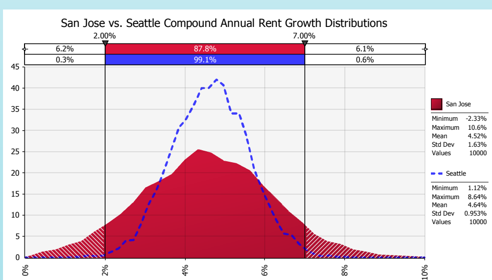

San Jose Payroll Employment Trends
Source: BLS, BEA Data, RCR Forecasts
YoY Growth Trend
5.3%
5.0%
3.2%
2.9%
2.0%
1.5%
US GDP GROWTH
US JOB GROWTH
SAN JOSE JOB GROWTH
2012
2013
2014
2015f
2016f
2017f
2018f
2019f
2020f

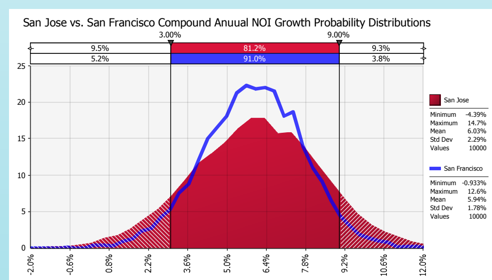
SUBMARKET TRENDS (REIS)

Submarket	Effective Rent			Physical Vacancy		
	3Q14	3Q15	Change	3Q14	3Q15	Change
Campbell / Los Gatos	$1,501	$1,677	11.7%	1.4%	2.5%	110 bps
Central San Jose	$1,581	$1,729	9.4%	3.5%	4.1%	60 bps
Cupertino / Saratoga	$2,311	$2,583	11.8%	2.3%	2.4%	10 bps
East San Jose	$1,629	$1,830	12.3%	1.5%	0.9%	-60 bps
Mountain View/Los Altos	$2,113	$2,290	8.3%	2.3%	4.1%	180 bps
Northeast San Jose	$2,115	$2,279	7.8%	3.7%	5.3%	160 bps
Santa Clara	$1,832	$2,022	10.4%	1.4%	1.8%	40 bps
South San Jose	$1,367	$1,466	7.3%	1.8%	2.5%	70 bps
Sunnyvale	$1,873	$2,009	7.3%	2.3%	2.4%	10 bps
Metro	$1,864	$2,023	8.5%	2.5%	3.3%	80 bps









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