ORANGE COUNTY, CA

MARKET OVERVIEW & MULTIFAMILY HOUSING UPDATE

RED Capital Group | 3Q15 | DECEMBER 2015

PAYROLL JOB SUMMARY	
Total Payrolls	1,542.1m
Annual Change	49.0m (3.3%)
RCR FY15 Forecast	49.3m (3.3%)
RCR 2016 Forecast	41.5m (2.7%)
RCR 2017 Forecast	41.1m (2.6%)
RCR 2018 Forecast	34.6m (2.1%)
RCR 2019 Forecast	23.3m (1.4%)
Unemployment (NSA)	4.3% (Oct.)

3Q15 PAYROLL TRENDS AND FORECAST

The Orange County labor market maintained a full head of steam during the third quarter, adding workers to payrolls at a 49,000-job, 3.3% year-on-year rate, on par with the previous two quarters. Expansion in high wage professional, technical, health care and education services fueled metro growth as concerns in these subsectors hired at a 16,100-job, 5.2% annual rate, matching 2Q15's robust pace. The manufacturing and leisure services industries and government also showed good momentum, advancing at an 15,800-job, 3.2% rate, up from 2Q's 10,300-job, 2.0% performance, compensating for weakness in the information and financial services and non-professional business services sectors.

Seasonally-adjusted data were not, as vigorous. This series suggests the O.C. created only 15,600 jobs during the seven-month period ended in October, down from 33,700 jobs over the preceding seven months and 26,200 in the comparable period of 2014.

The RED Research O.C. payroll forecasting model suggests that the outlook remains bright. The model uses the rate of change of U.S. payrolls, metro personal income and nominal GDP growth as independent variables to achieve a 96.5% adjusted-R^2 (S.E.=0.5%). This equation projects strong job creation through 2017, followed by gradual slowing in harmony with national trends.

OCCUPANCY RATE SUMMARY	
Occupancy Rate (Reis)	97.2%
RED 50 Rank	7th
Annual Chg. (Reis)	-0.2%
RCR YE15 Forecast	97.3%
RCR YE16 Forecast	97.4%
RCR YE17 Forecast	97.3%
RCR YE18 Forecast	97.2%
RCR YE19 Forecast	97.0%

3Q15 ABSORPTION AND OCCUPANCY RATE TRENDS

Reis surveys found stronger household demand for O.C. apartment space as renters net leased 483 units during 3Q15, up from 410 and 233 during the prior and year-earlier periods, respectively. Increased availability of new product was in part responsible: developers delivered 1,205 units during the quarter, the largest one-quarter vintage in three years. As a result, metro occupancy declined -30 basis points sequentially to 97.2%, RED 50 #7.

Axiometrics surveys of 369 larger stabilized, same-store properties recorded materially lower occupancy. In this sample, 95.8% of units were occupied in 3Q15, down –60 bps year-on-year. Seventy-four class-C assets posted the highest rate (97.3%), followed by classes-B (95.8%) and –A (94.8%). Class-C occupancy increased 20 bps y-o-y, while class-A plunged –150 bps under supply pressure. Eight new complexes leased an average of 19 units per month, down from 2Q15's blistering 27-unit/month performance.

RCR's O.C. demand model uses the rate of change of supply (+) and lags of rent (-) and payroll (+) growth to achieve a lower than normal 81.5% ARS but a reliable 0.3% standard error. The model projects that demand will outpace supply through 2017, raising occupancy 10 to 20 bps before slower job growth and continued brisk rent increases cause absorption to decelerate in the out-years of the forecast.

EFFECTIVE RENT SUMMARY	
Mean Rent (Reis)	$1,694
Annual Change	3.5%
RED 50 Rent Change Rank	28th
RCR YE15 Forecast	3.4%
RCR YE16 Forecast	4.0%
RCR YE17 Forecast	5.0%
RCR YE18 Forecast	4.6%
RCR YE19 Forecast	3.7%

3Q15 EFFECTIVE RENT TRENDS

Reis reports that the average Orange County unit rent grew $19 (1.1%) sequentially, the largest quarterly advance in a year. Expressed on a year-on-year basis, rents increased 3.5%, down from 3.7% and 3.6% in the prior and penultimate quarters, respectively, ranking only 28th among the RED 50, trailing San Diego, the Inland Empire and Los Angeles.

Axiometrics surveys of stabilized same-store properties recorded similar trends. This sample posted y-o-y growth of 4.9%, down from 6.3% and 6.0% in 2Q and 1Q15, respectively. Rent growth was strongest among the class-C segment, which chalked down a 6.5% advance. Class-B (4.6%) and class-A (4.5%) properties achieved comparable gains. Not coincidentally, submarkets near the L.A. County border notched the fastest growth; notably Placentia (8.0%), South Anaheim (7.8%), Huntington (7.7%), Fullerton (7.6%) and Brea (7.3%), while Irvine and Newport Beach lagged.

RCR achieved good results (ARS=97.5/SE=.05%) with a simple model using six lags of the dependent variable and personal income and occupied stock growth as independent variables. The model projects accelerating rent growth through 1Q18, before slowing to the low-3% area in 2020. The model projects five-year annual compound rent growth of 4.1%, comparing favorably to forecasts of 3.1% and 4.0% gains by Reis and Axiometrics, respectively.

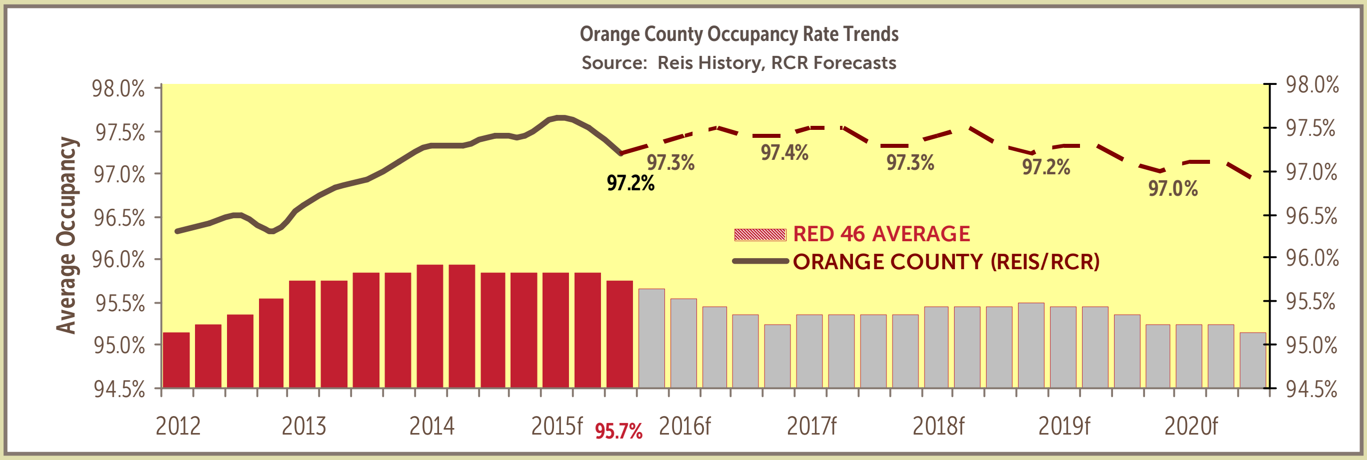
TRADE & RETURN SUMMARY	
$5mm+ / 60-unit+ Sales	7
Approximate Proceeds	$550mm
Average Cap Rate (FNM)	5.0%
Average Price / Unit	$267,233
Expected Total Return	6.8%
RED 46 ETR Rank	29th
Risk-adjusted Index	4.71
RED 46 RAI Rank	24th

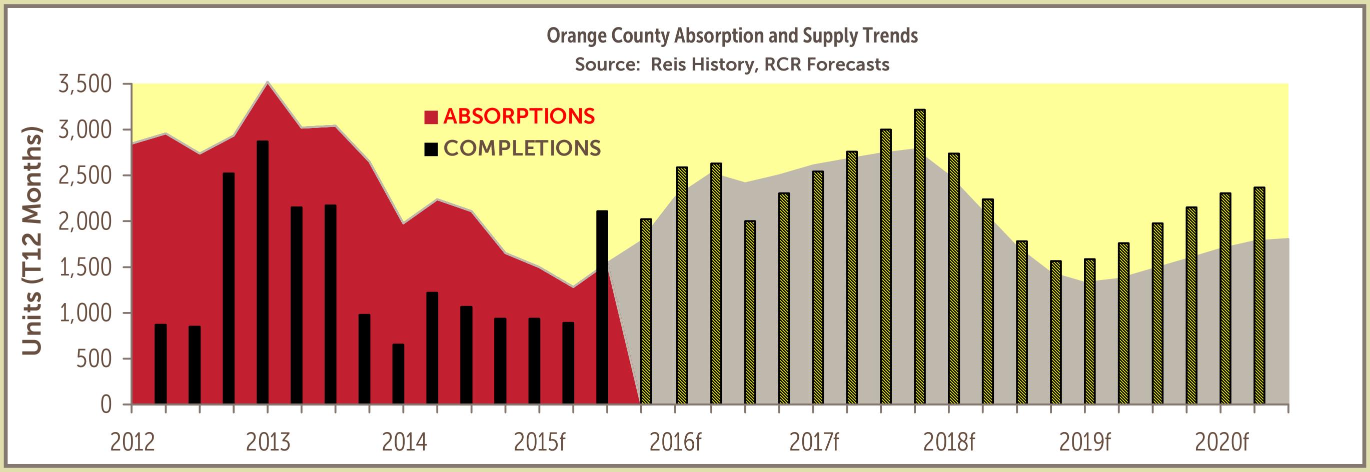
3Q15 PROPERTY MARKETS AND TOTAL RETURNS

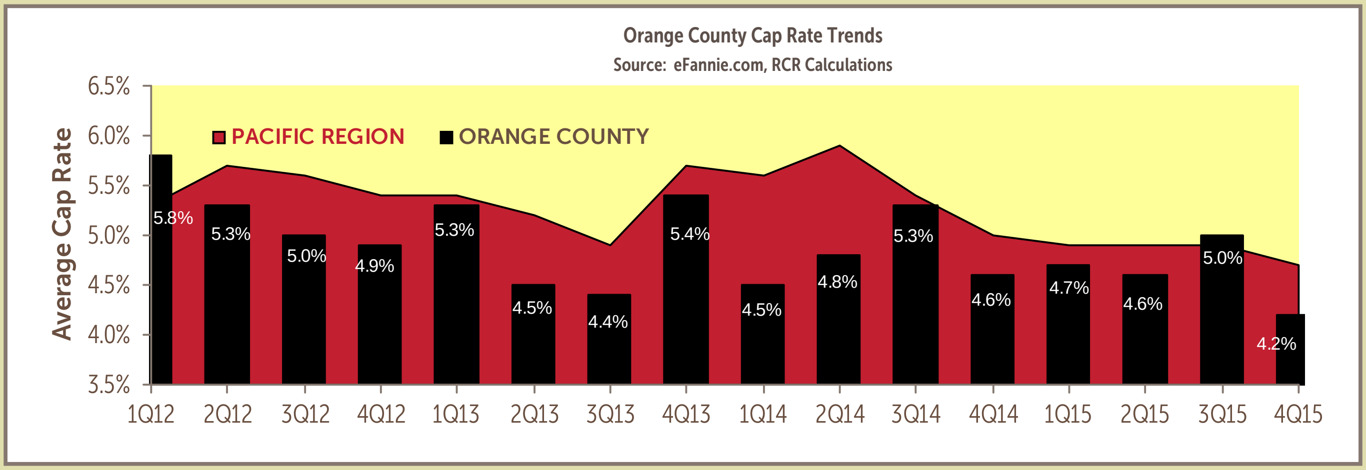
Property market velocity regained momentum during the third quarter when investors closed on seven investment sales, up from only three during 2Q15. Proceeds totaled an about $550 million, three times the approximate $182mm 2Q15 aggregate. The average price of 906 units sold was $267,233, down about -9% quarter-over-quarter. The average age of sold properties was 19 years.

Investors concentrated their fire on class-C and class-B– garden projects with repositioning potential. Cap rates for these properties ranged in the high-4% to mid-5% area. A in investment quality class-B asset traded in the mid-4s. The only legitimate class-A trophy was acquired by a large publicly traded REIT. The non-stabilized asset traded to a low-3% cap, with pro forma potential to 4.5%.

RCR elected to maintain the purchase cap rate proxy at 4.6%, although some evidence suggests that the level may be 10 to 20 bps lower. Using this going-in yield, a terminal cap rate of 5.3% and model derived rent and occupancy point estimates, we calculate that an Orange County investor would expect to achieve a 6.8% unlevered annual total return over a 5-year hold, ranking 29th among the RED 46. Low model standard errors reduce the uncertainty of Orange County total returns: the metro ranks 24th in the peer group on a risk-adjusted basis with an RAI of 4.71.

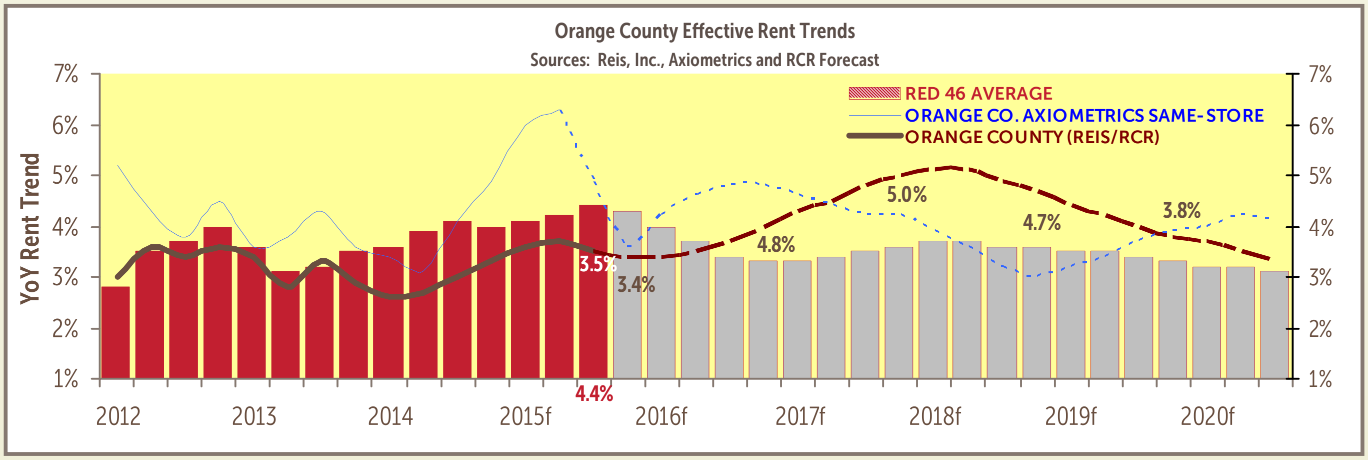


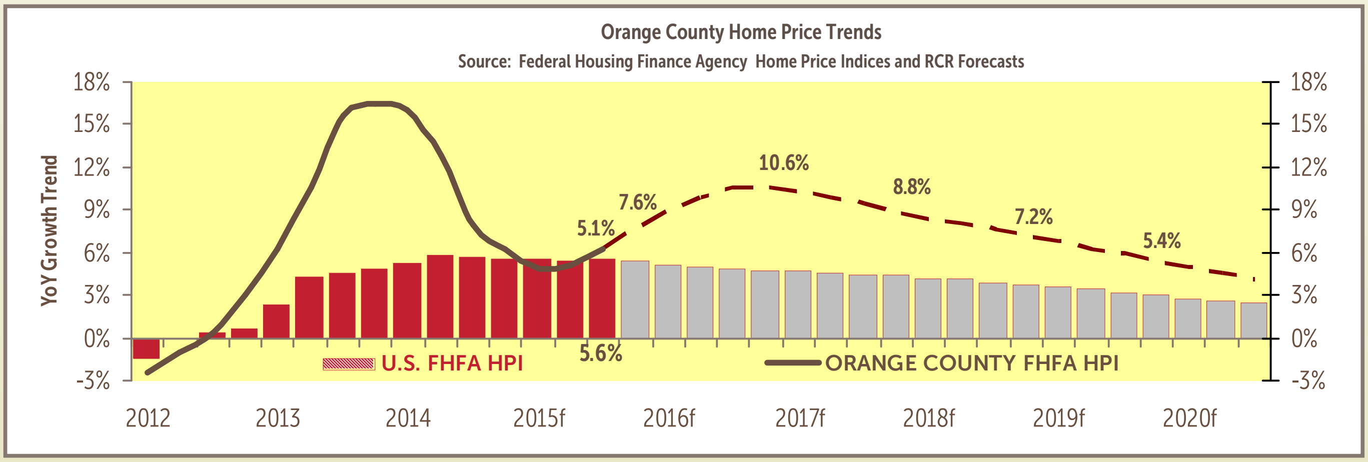


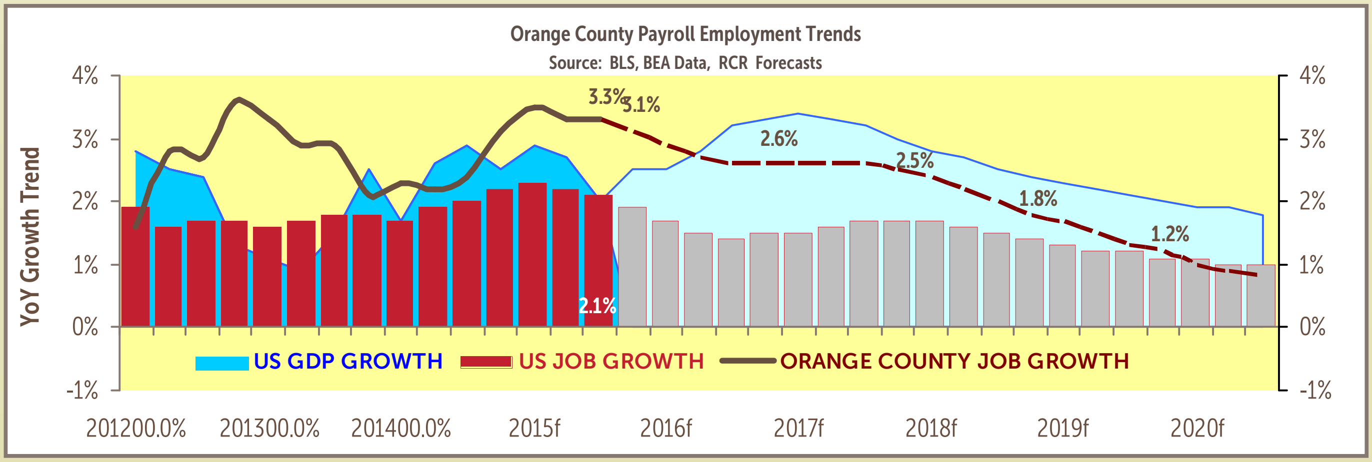


NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/ Type (Constr.)	Approx. Date of Transaction	Total Price / (in millions)	Price / per unit	Estimated Cap Rate
Yorba Linda Apts. (Placentia/Yorba Linda)	M.I. / GLR (1986)	3-Jun-2015	$118.0	$295,000	3.9%
Cypress Village (Buena Village/Lincoln Ave.)	C+ / GLR (70/05)	12-Jul-2015	$20.9	$237,500	5.0%
Eaves at Los Alisos (Mission Viejo)	B / GLR (1978)	26-Aug-2015	$39.5	$282,143	4.6%
Crystal View Apt. Homes (South Anaheim)	C / GLR (1968)	16-Oct-2015	$84.0 (allocated)	$208,955	5.5%
Modera Irvine (Irvine / Jamboree @ I-405)	A- / SR MR (2014)	17-Oct-2015	$80.4	$414,304	3.1% / 4.5% p.f.
Tustin Parc Apts. (North Santa Ana / Zoo)	B- / GLR (1969)	30-Oct-2015	$60.3	$245,091	5.0%

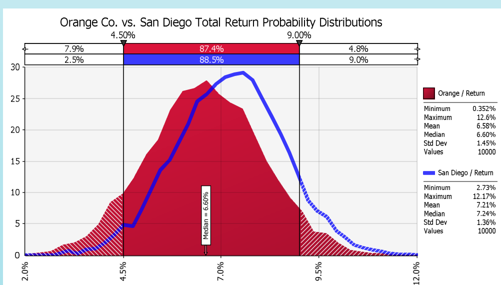

Orange County Effective Rent Trends
Sources: Reis, Inc., Axiometrics and RCR Forecast
RED 46 AVERAGE
ORANGE CO. AXIOMETRICS SAME-STORE
ORANGE COUNTY (REIS/RCR)
YoY Rent Trend
3.5%
3.4%
4.8%
5.0%
4.7%
3.8%
4.4%
2012
2013
2014
2015f
2016f
2017f
2018f
2019f
2020f

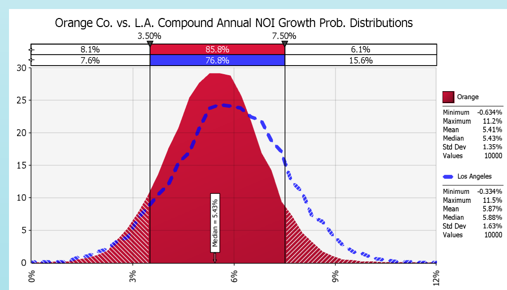

Orange County Home Price Trends
Source: Federal Housing Finance Agency Home Price Indices and RCR Forecasts
YoY Growth Trend
10.6%
8.8%
7.6%
7.2%
5.1%
5.4%
5.6%
U.S. FHFA HPI
ORANGE COUNTY FHFA HPI
2012
2013
2014
2015f
2016f
2017f
2018f
2019f
2020f


Orange County Payroll Employment Trends
Source: BLS, BEA Data, RCR Forecasts
YoY Growth Trend
3.3%
3.1%
2.6%
2.5%
1.8%
1.2%
2.1%
US GDP GROWTH
US JOB GROWTH
ORANGE COUNTY JOB GROWTH
201200.0%
201300.0%
201400.0%
2015f
2016f
2017f
2018f
2019f
2020f

SUBMARKET TRENDS (REIS)

Submarket	Effective Rent			Physical Vacancy		
	3Q14	3Q15	Change	3Q14	3Q15	Change
Brea	$1,434	$1,478	3.0%	1.4%	0.9%	-50 bps
Buena Park	$1,380	$1,416	2.6%	1.5%	0.9%	-60 bps
Costa Mesa	$1,763	$1,806	2.5%	2.5%	2.0%	-50 bps
Fullerton	$1,397	$1,440	3.1%	1.4%	1.4%	0 bps
Huntington Beach	$1,513	$1,604	6.0%	1.6%	5.6%	400 bps
Irvine	$2,078	$2,164	4.2%	4.2%	5.1%	90 bps
Laguna Beach/Dana Point	$1,774	$1,859	4.8%	2.9%	3.8%	90 bps
Laguna Hills	$1,847	$1,882	1.9%	3.3%	3.2%	-10 bps
Mission Viejo	$1,695	$1,779	5.0%	1.7%	3.1%	140 bps
Newport Beach	$2,200	$2,332	6.0%	1.7%	1.2%	-50 bps
North Anaheim	$1,321	$1,352	2.3%	2.3%	2.0%	-30 bps
North Santa Ana	$1,311	$1,346	2.7%	1.2%	1.0%	-20 bps
Orange	$1,648	$1,687	2.4%	1.9%	1.4%	-50 bps
Northeast Anaheim	$1,327	$1,353	2.0%	3.8%	3.4%	-40 bps
South Anaheim	$1,445	$1,484	2.7%	2.8%	2.1%	-70 bps
South Santa Ana	$1,754	$1,780	1.5%	3.9%	3.8%	-10 bps
Tustin	$1,509	$1,570	4.1%	2.0%	2.1%	10 bps
Westminster	$1,410	$1,454	3.2%	2.3%	2.1%	-20 bps
Metro	$1,636	$1,694	3.5%	2.6%	2.8%	20 bps





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