PHOENIX, ARIZONA

MARKET OVERVIEW & MULTIFAMILY HOUSING UPDATE

RED Capital Group | 1Q16 | JULY 2016

PAYROLL JOB SUMMARY	
Total Payrolls	1,960.4m
Annual Change	66.8m (3.5%)
RCR 2016 Forecast	54.6m (2.9%)
RCR 2017 Forecast	32.1m (1.6%)
RCR 2018 Forecast	28.1m (1.4%)
RCR 2019 Forecast	27.5m (1.4%)
RCR 2020 Forecast	29.6m (1.4%)
Unemployment (NSA)	4.7% (Apr.)

1Q16 PAYROLL TRENDS AND FORECAST

The Phoenix labor market maintained a full head of steam during the first quarter. Establishments added to staff at a 66,800-job, 3.5% annual rate, on par with 4Q15's nine-year high 68,900-job, 3.6% performance. The finance and construction sectors assumed leadership roles, collectively expanding payrolls at a 16,900-job, 6.2% year-on-year pace, up from 11,800 (4.5%) jobs during the prior quarter. Business, education and healthcare continued to contribute the lion's share of new jobs, holding steady on a 29,000-job, 4.8% year-on-year clip. By contrast, the retail trade, transportation and leisure services were weaker.

Seasonally-adjusted data were somewhat at odds. This series recorded a sluggish 5,200-job 1Q16 advance, smallest since 2Q11. Gains in April and May fell to only 2,900 jobs. A quick reversal of form in June will be called upon to avoid another sequentially weaker outcome in 2Q16.

RCR's PHX payroll forecasting model suggests that May's soft performance may be a harbinger of future trends. The equation uses US payroll growth (+) and metro income (+) and home price (+) growth as independent variables to reach a 96.7% adjusted R^2 (S.E.=0.6%). In keeping with slower projected U.S. gains, the model expects metro expansion to decelerate to below 2% by 1Q17, and further to the mid-1% range for the duration of the 5-year forecast interval. Should home price appreciation decelerate, payroll growth could stumble further.

OCCUPANCY RATE SUMMARY	
Occupancy Rate (Reis)	95.0%
RED 50 Rank	33rd
Annual Chg. (Reis)	-0.5%
RCR YE16 Forecast	94.1%
RCR YE17 Forecast	93.5%
RCR YE18 Forecast	93.3%
RCR YE19 Forecast	93.6%
RCR YE20 Forecast	93.4%

1Q16 ABSORPTION AND OCCUPANCY RATE TRENDS

Apartment demand surged during the seasonally strong winter quarter as renters net leased 1,979 vacant units, according to Reis, up from 1,197 units during the prior quarter and nearly equal to 1Q15's 15-year high 2,105. On the other hand, developers delivered 3,003 new units to stock, the largest single quarter vintage in 17 years. As a result, occupancy fell -30 basis points sequentially and -50 bps year-on-year to 95.0%, equal lowest since 4Q13.

Analysis of same-store stabilized asset performance data published by Axiometrics uncovers similar conditions. These data reveal a 94.9% average occupancy rate, up 10 bps y-o-y. Class-B (95.2%) sports the highest rate; classes-A (94.5%) and –C (94.1%) trail. East Mesa submarket (96.1%) recorded highest occupancy, followed by Paradise Valley (95.6%) and North Scottsdale (95.8%). Central North notched the largest y-o-y gain (0.8%) yet maintained lowest occupancy (91.6%). Tenants absorbed 12.5 units/month at new properties after renting an average of 13.9 in 4Q15.

RCR's demand model uses inventory (+), US payroll (+), home price$_{(t-2)}$ (-) and rent$_{(t-3)}$ growth variables to achieve a 92.5% ARS (SE=0.4%). The model foresees lower absorption in 2016 (4,398 units) overwhelmed by near record supply (8,131), sending occupancy down –90 bps by year-end. Near equilibrium should prevail from 2017 to 2020.

EFFECTIVE RENT SUMMARY	
Mean Rent (Reis)	$822
Annual Change	5.9%
RED 50 Rent Change Rank	9th
RCR YE16 Forecast	2.9%
RCR YE17 Forecast	1.0%
RCR YE18 Forecast	1.8%
RCR YE19 Forecast	2.1%
RCR YE20 Forecast	2.3%

1Q16 EFFECTIVE RENT TRENDS

Phoenix rents continued to soar, rising $12 (1.4%) sequentially, matching 4Q15's advance, according to Reis. Much of the impetus was attributable to the class-A sector. Class -A asking rents increased 1.4%, according to Reis, while class-B&C gained only 0.4%. Expressed on a year-on-year basis, rents rose 5.9%, the fastest quarterly read since 4Q06 and the 9th fastest advance among the RED 50.

Axiometrics same-store data pointed in a similar direction. In this case, average rent increased 7.5% y-o-y, representing the fifth consecutive print over 7%. Class-A rents were robust (6.1%) but surpassed by both classes-C (9.1%) and –B (7.4%). Two submarkets recorded annual gains of more than 10% — North Glendale/Peoria and Sunnyslope — while South and West Mesa topped 9%. At the other end of spectrum, South Scottsdale rent advanced only 1.2%.

Recent powerful trends notwithstanding, the RCR PHX rent model continues to project materially slower growth going forward. The model uses payroll job (+), U.S. home price (-) and metro inventory$_{(t-1)}$ (-) growth and metro occupancy$_{(t-3)}$ (+) as independent variables to specify a 97.0% ARS (SE=0.55%) equation. The model is influenced by our negative view of metro job trends, upbeat home price forecast and heavy pending supply. Thus, the model foresees slower rent growth developing by year end.

TRADE & RETURN SUMMARY	
$5mm+ / 80-unit+ Sales	28
Approximate Proceeds	$595.1mm
Average Cap Rate (FNM)	5.1%
Average Price / Unit	$86,077
Expected Total Return	5.2%
RED 46 ETR Rank	43th
Risk-adjusted Index	4.70
RED 46 RAI Rank	23rd

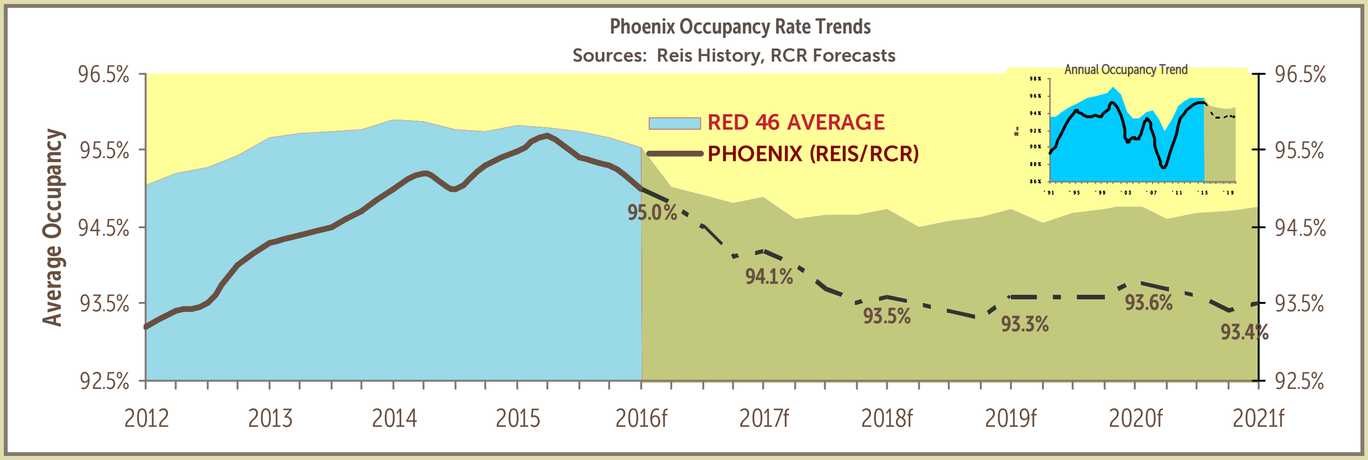
1Q16 PROPERTY MARKETS AND TOTAL RETURNS

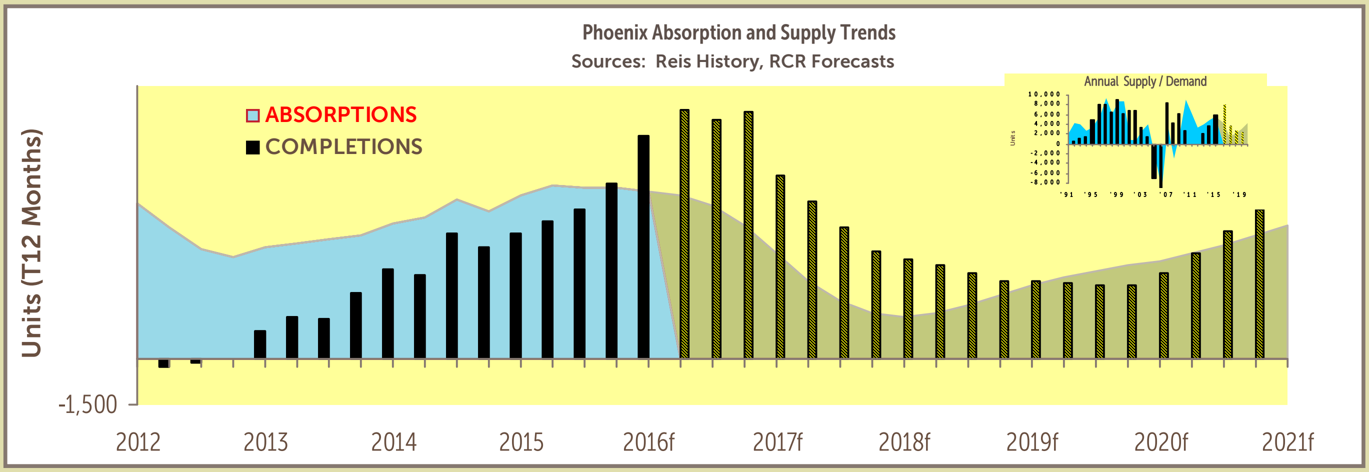
Following six months of torrid property sales activity, when 73 larger Phoenix assets exchanged hands for total value of $2.3 billion, trade velocity decelerated over the winter. Closings of apartment properties valued at $5 million or more declined –33% quarter-to-quarter to 28, and proceeds declined –55% to $595mm as investors focused almost exclusively on 70's and 80's construction value-add situations. For similar reasons the average price of sold units declined from $131,221 to $86,077 or -34%.

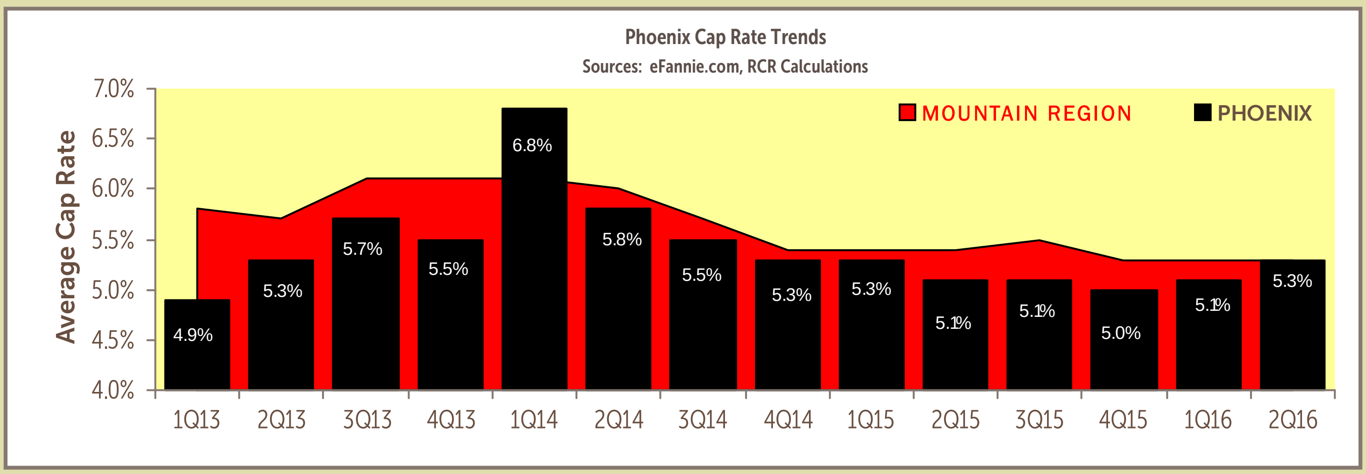
Trade velocity reaccelerated during 2Q16, however; through mid-June buyers already had consummated 56 acquisitions for $1.5bn, both record totals. The average price per unit recovered to $102,830, reflecting a larger concentration of complexes built since 1990 in the mix.

Value-adds were priced to yields in the low– to mid-5% area. Scant evidence was available indicating that cap rates for newer stabilized assets fell below this range.

Based on recent trade RCR elected to raise the PHX purchase cap rate proxy 10 basis points to 5.4%. At this level and model derived rent and occupancy point estimates we calculate that an investor would expect to achieve a 5.2% unlevered IRR on a 5-year hold (RED46 #43). Risk-adjusted returns are more favorable, ranking peer group #23)

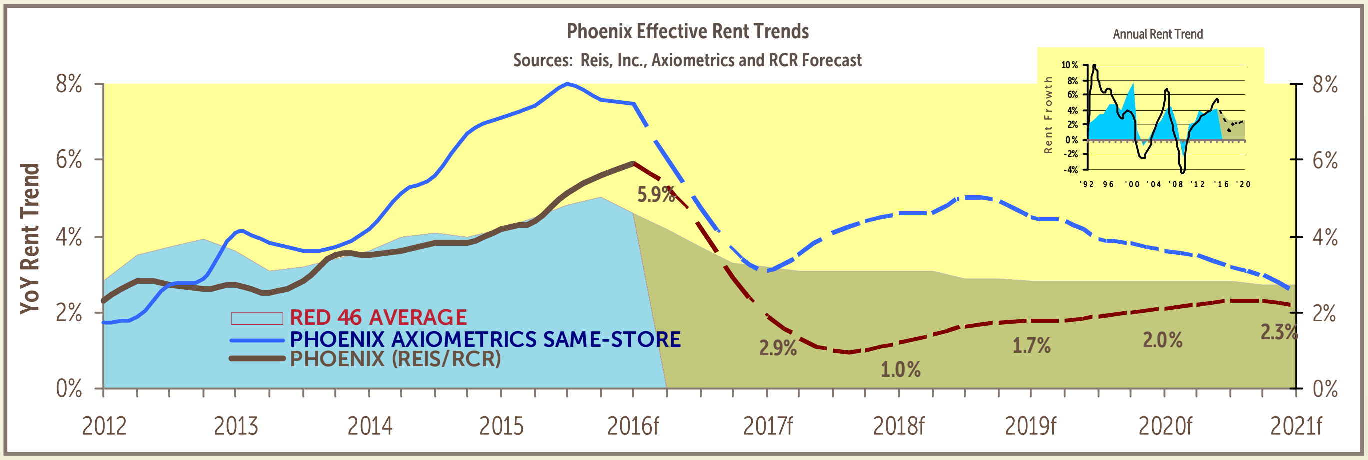


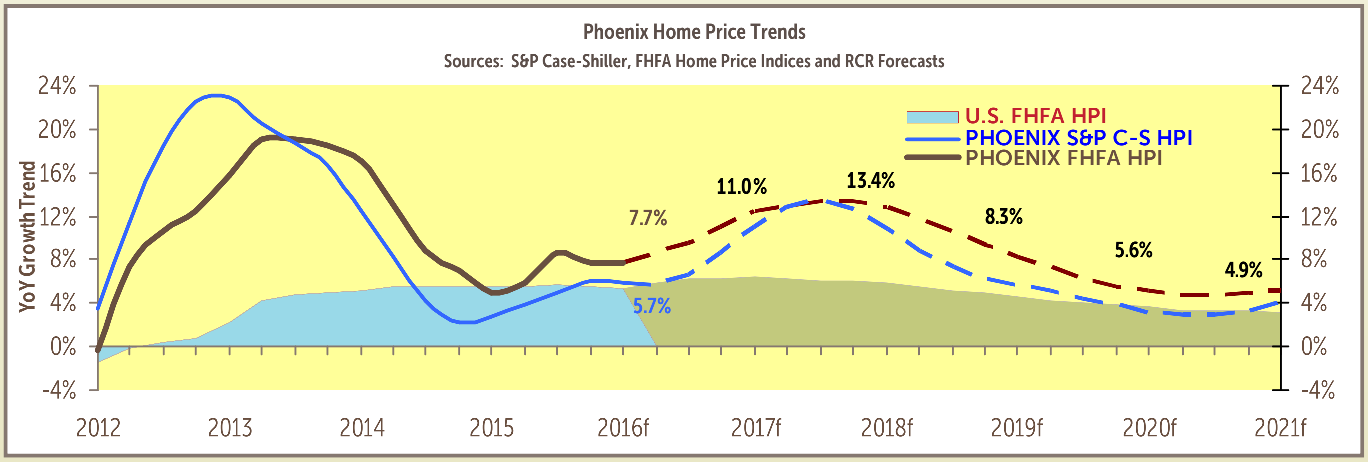


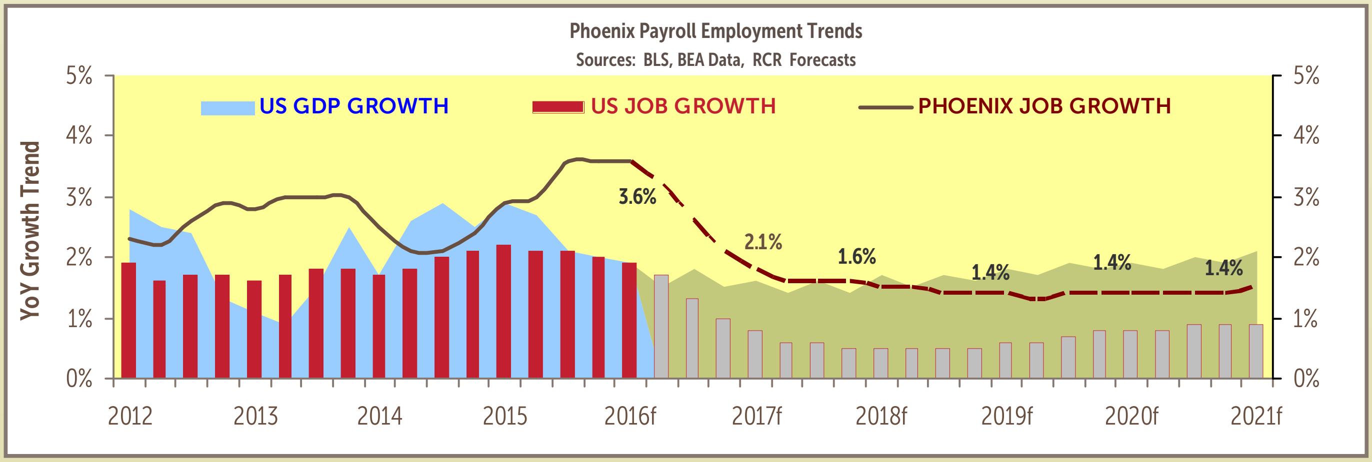


NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/ Type (Constr.)	Approx. Date of Transaction	Total Price / (in millions)	Price / per unit	Estimated Cap Rate
Casa Santa Fe (South Scottsdale)	B / GLR (1988)	20-Apr-2016	$33.9	$128,220	5.6%
Reserve at Arrowhead (Deer Valley)	B / GLR (1998)	28-Apr-2016	$64.5	$136,653	5.4%
Desert Horizon (North Scottsdale)	B+ / GLR (1985)	29-Apr-2016	$71.2	$138,551	5.2%
Monte Viejo Apts. (Deer Valley)	B / LR (2004)	21-May-2016	$58.6	$121,979	5.1%
Saratoga Ridge (Deer Valley/Grover Park)	B- / GLR (1986)	24-May-2016	$75.5	$88,201	5.9%
Park on Bell (Deer Valley)	B+ / WF LR (2008)	21-Jun-2016	$31.0	$135,965	5.4%

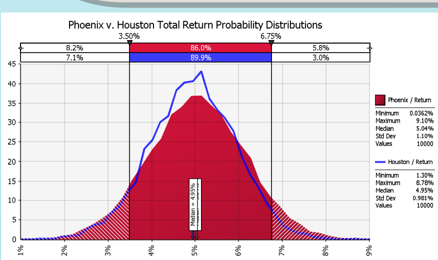

Phoenix Effective Rent Trends
Sources: Reis, Inc., Axiometrics and RCR Forecast
Annual Rent Trend
YoY Rent Trend
RED 46 AVERAGE
PHOENIX AXIOMETRICS SAME-STORE
PHOENIX (REIS/RCR)
5.9%
2.9%
1.0%
1.7%
2.0%
2.3%
8%
6%
4%
2%
0%
2012
2013
2014
2015
2016f
2017f
2018f
2019f
2020f
2021f

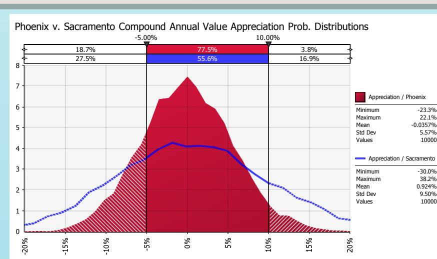

Phoenix Home Price Trends
Sources: S&P Case-Shiller, FHFA Home Price Indices and RCR Forecasts
YoY Growth Trend
U.S. FHFA HPI
PHOENIX S&P C-S HPI
PHOENIX FHFA HPI
7.7%
11.0%
13.4%
8.3%
5.6%
4.9%
5.7%
24%
20%
16%
12%
8%
4%
0%
-4%
2012
2013
2014
2015
2016f
2017f
2018f
2019f
2020f
2021f

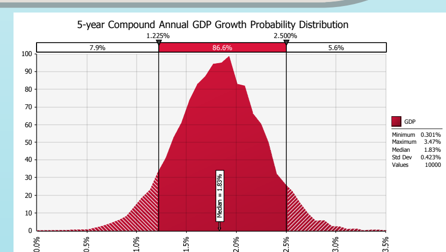

Phoenix Payroll Employment Trends
Sources: BLS, BEA Data, RCR Forecasts
YoY Growth Trend
US GDP GROWTH
US JOB GROWTH
PHOENIX JOB GROWTH
3.6%
2.1%
1.6%
1.4%
1.4%
1.4%
5%
4%
3%
2%
1%
0%
2012
2013
2014
2015
2016f
2017f
2018f
2019f
2020f
2021f

SUBMARKET TRENDS (REIS)

Submarket	Inventory % Change	Effective Rent			Physical Vacancy		
		1Q15	1Q16	Change	1Q15	1Q16	Change
Central Phoenix-North	1.2%	$633	$658	4.1%	6.0%	5.5%	-50 bps
Central Phoenix-South	3.0%	$733	$767	4.7%	4.4%	6.4%	200 bps
Chandler / Gilbert	6.6%	$886	$985	11.3%	5.5%	7.5%	200 bps
Deer Valley	1.0%	$716	$750	4.8%	3.4%	2.9%	-50 bps
East Mesa	0.0%	$765	$803	5.0%	1.2%	1.1%	-10 bps
Glendale South	0.0%	$636	$656	3.2%	6.2%	4.8%	-140 bps
Goodyear / Avondale	1.5%	$863	$895	3.8%	1.9%	1.8%	-10 bps
Maryvale	0.0%	$581	$596	2.5%	4.9%	3.6%	-130 bps
North Scottsdale	6.0%	$1,045	$1,114	6.6%	6.1%	7.0%	90 bps
North Tempe	6.4%	$842	$916	8.8%	3.0%	7.8%	480 bps
Northeast Phoenix	1.0%	$755	$796	5.5%	4.4%	4.7%	30 bps
Paradise Valley	0.0%	$721	$754	4.5%	4.6%	4.0%	-60 bps
Peoria/Sun City/Surprise	0.0%	$803	$838	4.3%	1.6%	1.8%	20 bps
South Mesa	0.0%	$661	$698	5.6%	4.6%	3.7%	-90 bps
South Scottsdale	14.9%	$897	$981	9.4%	10.7%	13.1%	240 bps
South Tempe	5.2%	$891	$945	6.0%	4.2%	5.4%	120 bps
Sunnyslope	0.5%	$669	$689	2.9%	2.7%	2.7%	0 bps
West Mesa	0.0%	$632	$656	3.8%	3.3%	2.5%	-80 bps
Metro	2.8%	$776	$822	5.9%	4.5%	5.0%	50 bps







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