DENVER, COLORADO

MARKET OVERVIEW & MULTIFAMILY HOUSING UPDATE

RED Capital Group | 3Q16 | DECEMBER 2016

PAYROLL JOB SUMMARY	
Average Payrolls	1,455.7m
Annual Change	48.0m (3.4%)
RCR 2016 Forecast	44.8m (3.2%)
RCR 2017 Forecast	50.6m (3.5%)
RCR 2018 Forecast	43.9m (2.9%)
RCR 2019 Forecast	31.7m (2.1%)
RCR 2020 Forecast	25.5m (1.6%)
Unemployment (NSA)	2.9% (Oct.)

3Q16 PAYROLL TRENDS AND FORECAST

Hiring by Denver establishments accelerated for the third consecutive quarter, rising to a 48,000-job, 3.4% year-on-year rate, up from 2Q's 44,700-job pace. The construction and extraction sectors set the pace, adding workers at a blistering 12,500-job, 13.0% annual rate, suggesting a housing boom and possibly an oil and gas renaissance. Leisure services establishments also recorded a hiring bump as growth advanced from 2Q16"s 7,900-job, 5.1% performance to 5.8%. Meanwhile, the skilled services sectors continued to expand at healthy rates, highlighted by 3.6% and 3.0% annual growth rates in the professional and technical business and healthcare services subsectors. Only financial services and manufacturing exhibited moderate decelerating trends.

Seasonally-adjusted figures were largely consistent. This series recorded a 11,200-job net payroll increase in 3Q15, up from 10,800 and 10,500 in the year-earlier and prior quarters, respectively. But the preliminary November datum was a negative outlier, reflecting a 5,500-job net loss, the worst month since April 2009.

Although a degree of early 4Q16 slowing was evident in the unadjusted data series as well, the **RED Research** payroll model projects further 3%+ job growth for the nest two years. The equation includes the rate of change of U.S. job growth (+) and $GDP_{(t-3)}$ (-) and metro personal income growth (+) as independent variables. The 98.2% adjusted-R^2 (S.E.=0.3%) model forecasts decelerating growth afterward, reflecting slower U.S. GDP, job and income expansion late in the decade. Still, Denver is expected to outperform U.S. job and income performance through 2021.

OCCUPANCY RATE SUMMARY	
Occupancy Rate (Reis)	94.9%
RED 51 Rank	38th
Annual Chg. (Reis)	-0.9%
RCR YE16 Forecast	94.3%
RCR YE17 Forecast	94.0%
RCR YE18 Forecast	94.1%
RCR YE19 Forecast	94.8%
RCR YE20 Forecast	93.9%

3Q16 ABSORPTION AND OCCUPANCY RATE TRENDS

Reis report that tenant demand fell materially during the summer quarter as renters net leased 632 vacant units, down from 1,151 and 2,345 during the prior and year-earlier quarters, respectively. This represented the fewest units absorbed during a July to September period in four years. Lower supply was partially responsible as developers completed only 960 units, the smallest vintage in nearly three years. No shortage of class-A units is evident though — vacant stock of 7,585 units was highest in 12 years - suggesting some demand weakness. Occupancy averaged 94.9%, lowest in five years, down -10 basis points sequentially and –90bps year-on-year.

Axiometrics data obtained from 484 stabilized same-store properties found average occupancy of 94.6%, also down –90bps y-o-y. Including 37 properties (10,021 units) that were in lease-up since 3Q15, occupancy averaged 94.3%. Stabilized occupancy across classes varied in a tight 94.3% ("A") to 94.8% ("C") range. Four of 19 submarkets reported occupancy above 95%. Three submarkets fell below 94%, most notably Denver-Central (93.3%)

The demand outlook is promising over the next five years. RCR's occupied stock growth model (ARS=93.1%/S.E.=0.4%) projects 2.4% average growth through 2021, down only 0.2% from the 2012-2016 average. Supply, however, is likely to be slightly above the recent average, resulting in moderate occupancy decay throughout the five-year forecast interval. Our point estimate forecast calls for a decrease to the high-93% region in the forecast out-year.

EFFECTIVE RENT SUMMARY	
Mean Rent (Reis)	$1,105
Annual Change	5.3%
RED 51 Rent Change Rank	12th
RCR YE16 Forecast	4.3%
RCR YE17 Forecast	4.0%
RCR YE18 Forecast	4.2%
RCR YE19 Forecast	3.4%
RCR YE20 Forecast	3.7%

3Q16 EFFECTIVE RENT TRENDS

Metro rents increased at a brisk if moderately slower pace during the third quarter. Reis report that effective rent advanced $17 (1.5%) sequentially, compared to $18 (1.7%) and $25 (2.5%) in the prior and year-earlier quarters, respectively. Expressed on a year-on-year basis, average rent ascended 5.3%, down from 6.3% in 2Q16, representing the smallest gain recorded in three years. B&C asking rent trends accelerated quarter-to-quarter, providing the lion's share of market impetus; "A" trends slowed.

Stabilized, same-store properties surveyed by Axiometrics indicated that the these trends were more advanced among larger, professionally-managed assets. Rents among this sample were up only 3.1% y-o-y, down from 5.1% in 2Q16 and 10.8% in the year-earlier period. Classes-B and –C led the market down, the former falling from 4.8% y-o-y to 2.8%, and 7.4% to 41%, respectively. Class-A gains were slightly stronger (3.2% vs. 3.0%). Aurora-Central-SE (6.6%) and Denver-Central (5.2%) posted the best growth, and Arvada (1.2%) and Littleton (1.4%) the slowest.

RCR analysis finds that absorption (+), occupancy (+), home prices (+) and inventory (-) growth are the principal economic drivers of DEN rent growth, serving as independent variables in its 96.6% ARS (S.E.=0.3%) forecasting equation. The model forecasts slower growth as Denver digests a further 2-year wave of heavy supply. As supply diminishes, rents again will accelerate above the 3.9% long-term historical average, averaging 3,8% over 5 years.

TRADE & RETURN SUMMARY	
$5mm+ / 80-unit+ Sales	24
Approximate Proceeds	$1,.316MM
Average Cap Rate (FNM)	5.1%
Average Price / Unit	$197,136
Expected Total Return	6.9%
RED 47 ETR Rank	25th
Risk-adjusted Index	2.65
RED 47 RAI Rank	43rd

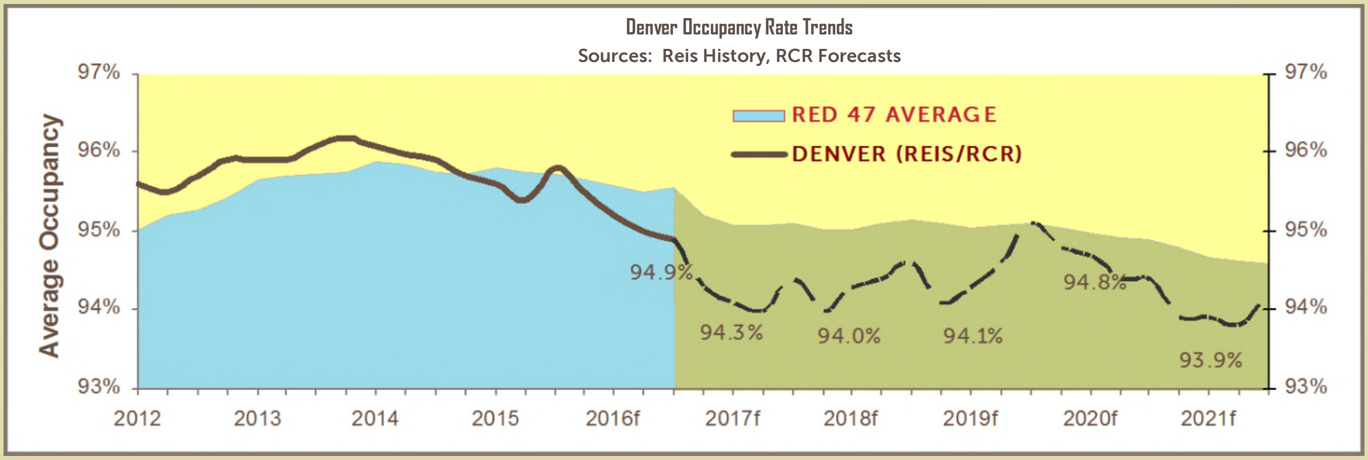
3Q16 PROPERTY MARKETS AND TOTAL RETURNS

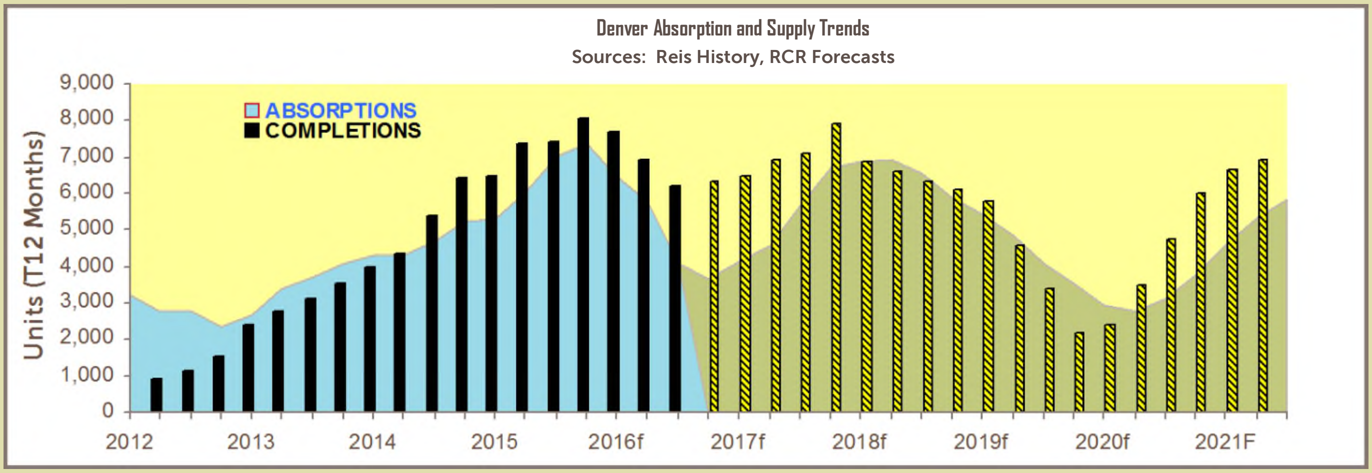
Sales velocity was steady over the summer as 24 multifamily properties valued at $5 million or more exchanged hands, matching the previous quarter performance. Sales totaled $1,316mm in proceeds, a 13% increase quarter-on-quarter. By the same token, the average price per traded unit fell –11% to $197,136, largely due to greater buyer concentration in older value-add properties

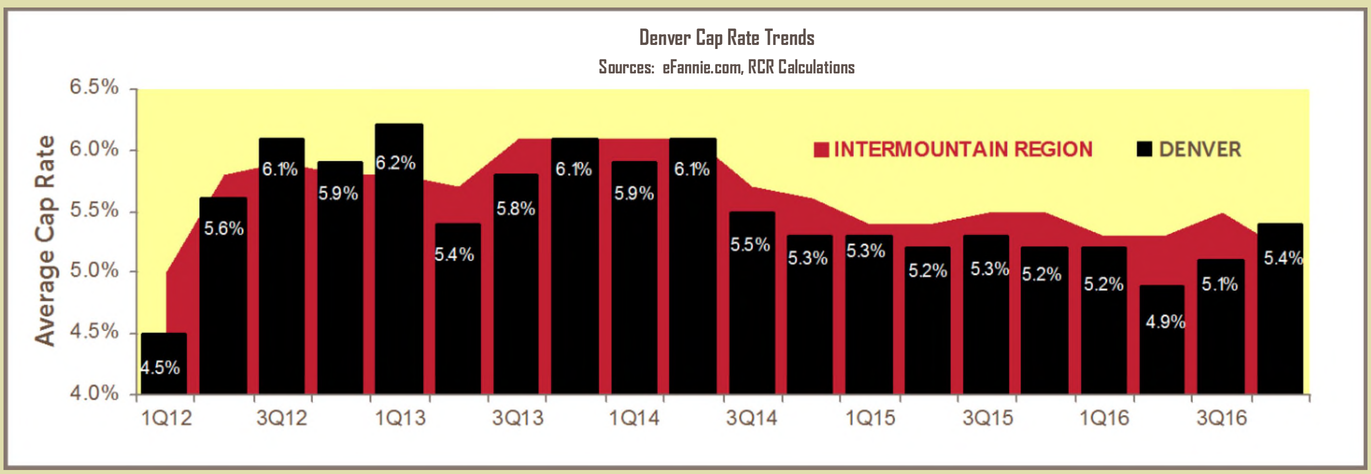
Fourth quarter trade promises to be the strongest since 1Q16 (46 transactions/$2.8bn) and the second most prolific quarter ever. Through mid-December, buyers had closed on 23 acquisitions for proceeds of $1.3bn. Although per-unit prices were nearly unchanged, the average cap fell to 4.96%, according to CoStar, down from 5.42% in 3Q16, and the lowest metric observed in the series.

Cap rates for infill trophies remain in the low– to mid-4% area. Transit oriented mid-rises and class-B+ suburban garden projects fall in the mid-4% area to 5.0%. Value-add class-B and B– properties traded in a wider range, from the low-5s to mid-6s.

In light of the strong second-half 2016 bid for DEN assets, **RCR** elected to trim another 10 basis points from the cap rate proxy to 4.7%. At this purchase yield, a terminal cap of 5.5%, and model derived rent and occupancy point estimates we estimate than an investor would expect to earn a 6.9% 5-year unlevered total return, ranked 25th among the **RED 47** peer group. As regards risk -adjusted returns, Denver's risk-adjusted index of2.65 ranks group #43, reflecting the low cap rate and moderately high model errors.

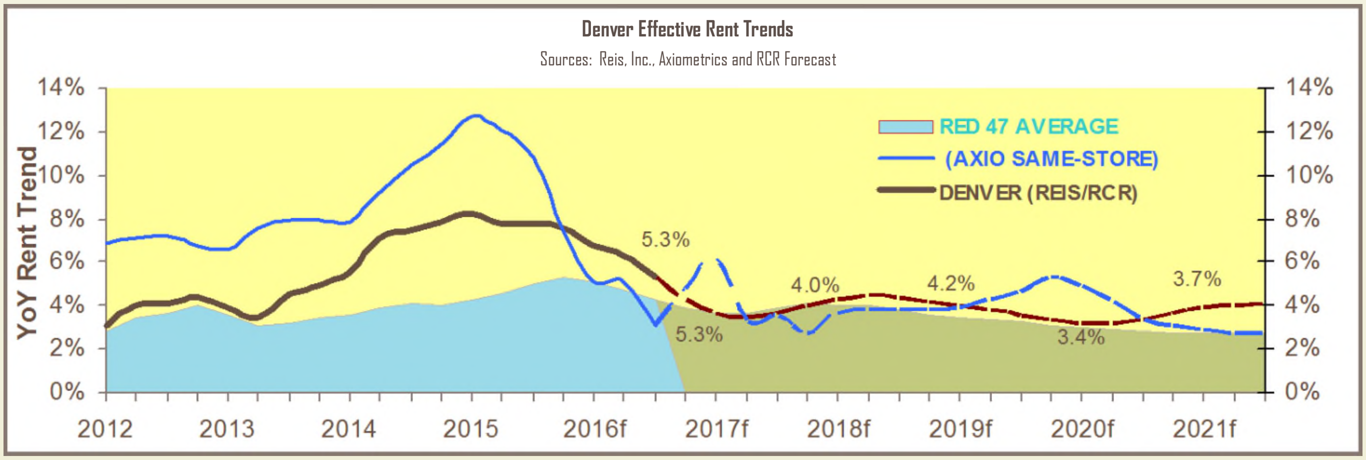


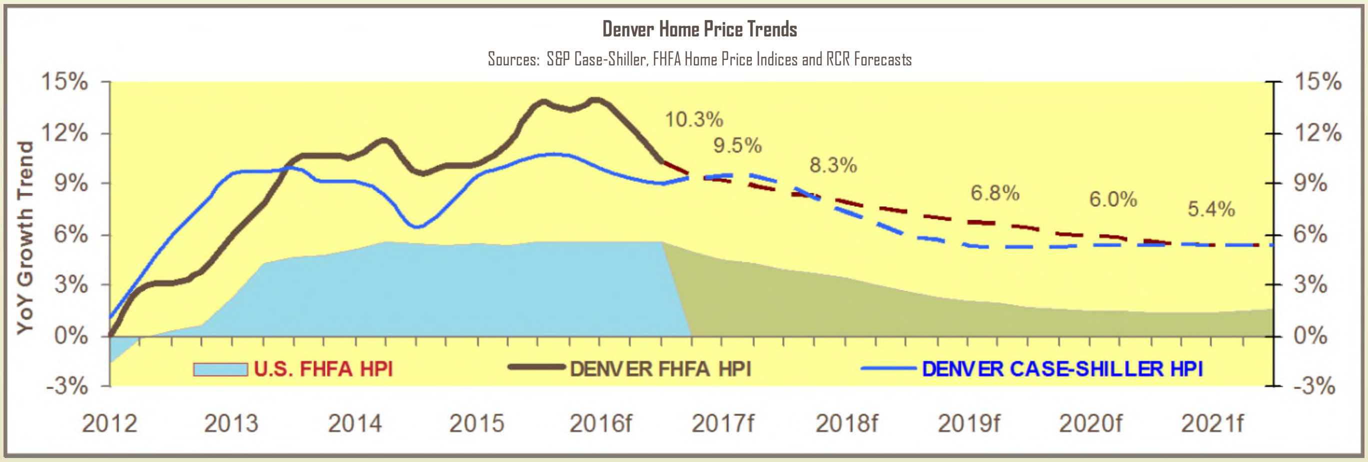


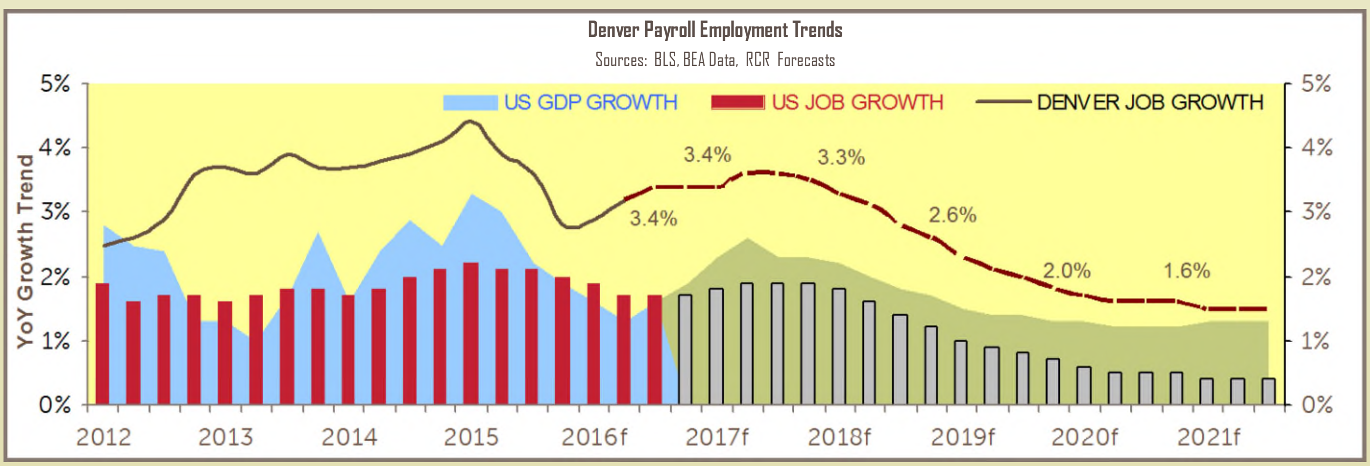


NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/Type (Constr.)	Approx. Date of Transaction	Total Price (in millions)	Price / Per Unit	Estimated Cap Rate
Grand Lowry (Denver-Northeast / Lowry Field)	B+ / LR (37/01)	18-Oct-2016	$23.3	$89,138	6.4%
Pembrooke on the Green (Aurora / South / Kennedy Fields)	C / GLR (1974)	7-Nov-2016	$128.4	$133,884	5.2%
Solaire Apts. (Northglenn / Brighton / Sorrento)	B+ / GLR (2014)	13-Nov-2016	$57.5	$228,175	4.75%
IMT Cherry Creek (Denver / Southeast / Glendale)	B+/RC LR (1999)	14-Nov-2016	$43.7	$238,988	4.9%
Advenir French Quarter (Aurora / South / Kennedy Fields)	B/GLR (1973/10)	17-Nov-2016	$65.8	$150,803	5.6%
Arista Uptown (Broomfield Urban Transit Village)	A- / WF LR (2013)	23-Nov-2016	$65.0	$238,971	4.6%


Denver Effective Rent Trends
Sources: Reis, Inc., Axiometrics and RCR Forecast
YoY Rent Trend
RED 47 AVERAGE
(AXIO SAME-STORE)
DENVER (REIS/RCR)
5.3%
5.3%
4.0%
4.2%
3.4%
3.7%
14%
12%
10%
8%
6%
4%
2%
0%
2012
2013
2014
2015
2016f
2017f
2018f
2019f
2020f
2021f


Denver Home Price Trends
Sources: S&P Case-Shiller, FHFA Home Price Indices and RCR Forecasts
YoY Growth Trend
10.3%
9.5%
8.3%
6.8%
6.0%
5.4%
U.S. FHFA HPI
DENVER FHFA HPI
DENVER CASE-SHILLER HPI
15%
12%
9%
6%
3%
0%
-3%
2012
2013
2014
2015
2016f
2017f
2018f
2019f
2020f
2021f


Denver Payroll Employment Trends
Sources: BLS, BEA Data, RCR Forecasts
YoY Growth Trend
US GDP GROWTH
US JOB GROWTH
DENVER JOB GROWTH
3.4%
3.3%
3.4%
2.6%
2.0%
1.6%
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		
		3Q15	3Q16	Change	3Q15	3Q16	Change
Arapahoe County	3.1%	$1,293	$1,319	2.0%	9.7%	6.2%	-350 bps
Arvada / Broomfield	2.4%	$1,040	$1,051	1.1%	4.7%	6.2%	150 bps
Aurora-Central-Southeast	-0.5%	$917	$963	4.9%	3.0%	2.8%	-20 bps
Aurora-Central-Southwest	0.0%	$849	$872	2.7%	5.0%	5.5%	50 bps
Aurora-North	0.0%	$852	$843	-1.0%	1.9%	2.3%	40 bps
Aurora-South	3.7%	$1,169	$1,217	4.2%	4.7%	6.9%	220 bps
Denver-Central	5.2%	$1,119	$1,178	5.2%	6.8%	9.3%	250 bps
Denver-Downtown	-0.1%	$1,210	$1,220	0.8%	7.6%	1.7%	-590 bps
Denver-Far Southeast	0.0%	$884	$916	3.6%	4.2%	3.7%	-50 bps
Denver-North	16.3%	$1,584	$1,628	2.8%	14.0%	12.1%	-190 bps
Denver-Northeast	4.5%	$1,040	$1,154	11.1%	5.2%	6.8%	160 bps
Denver-South	15.5%	$892	$923	3.5%	5.1%	7.7%	260 bps
Denver-Southeast	2.6%	$879	$956	8.7%	1.1%	2.9%	180 bps
Douglas County	1.6%	$1,181	$1,211	2.5%	3.3%	4.4%	110 bps
Englewood / Sheridan	6.2%	$823	$890	8.1%	2.2%	4.8%	260 bps
Golden / Wheat Ridge	14.5%	$973	$1,089	12.0%	2.8%	6.2%	340 bps
Lakewood-North	5.0%	$954	$986	3.4%	2.4%	3.6%	120 bps
Lakewood-South	3.0%	$1,095	$1,128	3.0%	1.8%	2.5%	70 bps
Littleton	-0.1%	$1,066	$1,091	2.4%	5.9%	5.5%	-40 bps
North Glenn / Thornton	0.0%	$941	$1,026	9.1%	5.1%	5.3%	20 bps
Westminster	0.0%	$988	$1,120	13.4%	4.1%	2.5%	-160 bps
Metro	3.3%	$1,049	$1,105	5.3%	4.2%	5.1%	90 bps

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