AUSTIN, TEXAS

MARKET OVERVIEW & MULTIFAMILY HOUSING UPDATE

RED Capital Group | 3Q16 | JANUARY 2017

PAYROLL JOB SUMMARY

Average Payrolls	993.8m
Annual Change	32.7m (3.4%)
RCR 2016 Forecast	35.5m (3.7%)
RCR 2017 Forecast	32.8m (3.3%)
RCR 2018 Forecast	32.2m (3.1%)
RCR 2019 Forecast	29.2m (2.8%)
RCR 2020 Forecast	26.9m (2.5%)
Unemployment (NSA)	3.0% (Nov.)

3Q16 PAYROLL TRENDS AND FORECAST

The pace of job growth in the Capital Area decelerated for the third consecutive quarter, slowing to a 32,700-job, 3.4% year-on-year rate from 4Q16's peak 4.8% performance and 2Q's 3.9% advance. Manufacturing was a principal factor. Headcounts declined at a 3,300-job, -5.7% rate in 3Q after being a net job contributor as recently as 4Q15. Gains were recorded in every other super-sector, but deceleration was observed broadly across industries, especially in retail trade and personal services. Retail, healthcare, leisure and personal services hired at a collective 11,200-job, 3.2% annual rate in 3Q16, following the prior quarter's 15,000-job advance and the 4Q15 cycle peak of 17,100. The tech sector remained a bright spot as information and professional service firms stepped up hiring, as did construction, where builder payrolls expanded at a blistering 6,200-job, 11.1% y-o-y rate, each a 27-year data history record.

Seasonally-adjusted data also evidenced softer trends. Indeed, Austin payrolls declined -600 jobs from July to September, representing the first down quarter in seven years.

The **RED Research** Austin payroll model is simple, reaching a 96.6% adjusted-R^2 (SE=0.5%) using only the rate of change of US payroll growth and the S&P500 as independent variables. Under our unbiased model-derived base case macroeconomic forecast the equation generates a very constructive forecast wherein metro job growth continues at a 3% or faster rate through 4Q18. The expansion begins to fray somewhat thereafter as US hiring slows and equity returns sputter but annual gains persist at above average rates throughout the 5-year forecast interval. Growth is expected to average 2.8% annually through 2021, 2nd among the **RED 47**.

OCCUPANCY RATE SUMMARY

Occupancy Rate (Reis)	93.6%
RED 51 Rank	48st
Annual Chg. (Reis)	-0.1%
RCR YE16 Forecast	93.4%
RCR YE17 Forecast	93.4%
RCR YE18 Forecast	94.4%
RCR YE19 Forecast	95.1%
RCR YE20 Forecast	94.3%

3Q16 ABSORPTION AND OCCUPANCY RATE TRENDS

Space demand was constructive during the third quarter but distinct signs of deceleration were evident. A net of 1,156 vacant units were absorbed, according to Reis, down from 1,498 and 2,107 during the prior and year-ago quarters and materially below the 17-year third quarter average of 1,512. Reduced supply played a role: developers completed 1,252 units, the smallest quarterly vintage in three years. But with metro inventory up nearly 4% over the prior year it was unlikely the decisive factor. By way of statistics, occupancy declined 10 basis points year-on-year to 93.6%, **RED 51** #48.

Axiometrics found that 490 stabilized same-store properties were 94.8% occupied during 3Q16, -60bps below the comparable period of 2015. Class-C (95.0%) recorded highest occupancy (for the 10th consecutive quarter), followed by classes-B (94.9%) and –A (94.3%). Among submarkets, highest occupancy was observed in San Marcos (96.2%) and Near So. Central (95.6%); lowest in East (92.6%) and Southeast (93.4%). Central, wherein inventory increased by about 28% since 2015, was firm at 93.9%/-0.3% y-o-y.

The **RCR** demand model employs the rates of change of inventory (+), job (+) and rent (-) growth and occupancy change$_{(t-1)}$ as independent variables to reach an 89.9% ARS (SE=0.4%). The model projects absorption of ~7,000, 4,000 and 2,350 units in 2017, 2018 and 2019, enough to boost occupancy ~150 bps. Supply is likely to reassert itself in the out-years. Much of the occupancy ground gained in 2017-19 may be lost if supply levels revert to the mean.

EFFECTIVE RENT SUMMARY

Mean Rent (Reis)	$1,015
Annual Change	3.2%
RED 51 Rent Change Rank	37th
RCR YE16 Forecast	3.0%
RCR YE17 Forecast	3.2%
RCR YE18 Forecast	3.3%
RCR YE19 Forecast	3.1%
RCR YE20 Forecast	2.7%

3Q16 EFFECTIVE RENT TRENDS

Austin property owners recorded moderate rent growth in 3Q16, notching a $7 (0.7%) sequential quarter gain to $1,015, keeping pace with the first half 2016 quarterly average. Expressed on a year-on-year basis, rents advanced 3.2%, down from 3.9% in 2Q16 and 2015's 5.7% increase. Class-B&C provided the bulk of the forward momentum as asking rent among 70,398 class units rose 1.1% sequentially, compared to 0.5% among 109,307 class-A units.

Rent growth among Axiometrics's 490-unit same-store sample averaged 3.7% in 3Q16, down from 5.5% and 6.0% in the prior quarter and year-ago periods, respectively. The "B" segment (4.3%) led among classes for the third consecutive quarter, followed by 2014 and 2015 leader class-C (3.9%). Supply pressure weighed heavily on class-A (0.9%). Trends at class-A high-rises were especially soft as rents tumbled –5.9% y-o-y. Central submarket's class-A and high-rise concentration was its undoing (-2.0%); West (-1.3%) also declined. Far No. Central (6.3%), Round Rock (5.9%) and Southwest (5.1%) were submarket leaders.

RCR analysis found that occupancy change (+) and metro income and job growth were statistically significant predictors of Austin rent growth. The equation specified with these variables had a 96.8% ARS (SE=0.8%) Under the base economic outcome, the model projects further, stable low-3% area growth through 2020, followed by slowing to the mid-2s during the out-year. Rents are expected to advance at a 2.9% compound annual rate, **R47** #28.

TRADE & RETURN SUMMARY

$5mm+ / 80-unit+ Sales	23
Approximate Proceeds	$650mm
Average Cap Rate (FNM)	5.5%
Average Price / Unit	$168,361
Expected Total Return	7.1%
RED 47 ETR Rank	20th
Risk-adjusted Index	2.89
RED 47 RAI Rank	40th

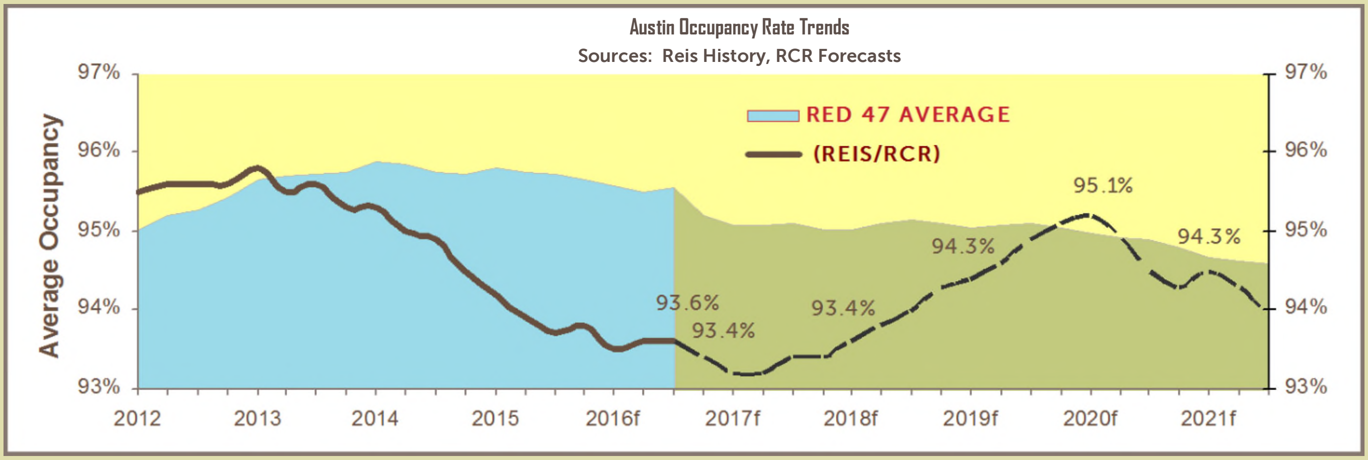
3Q16 PROPERTY MARKETS AND TOTAL RETURNS

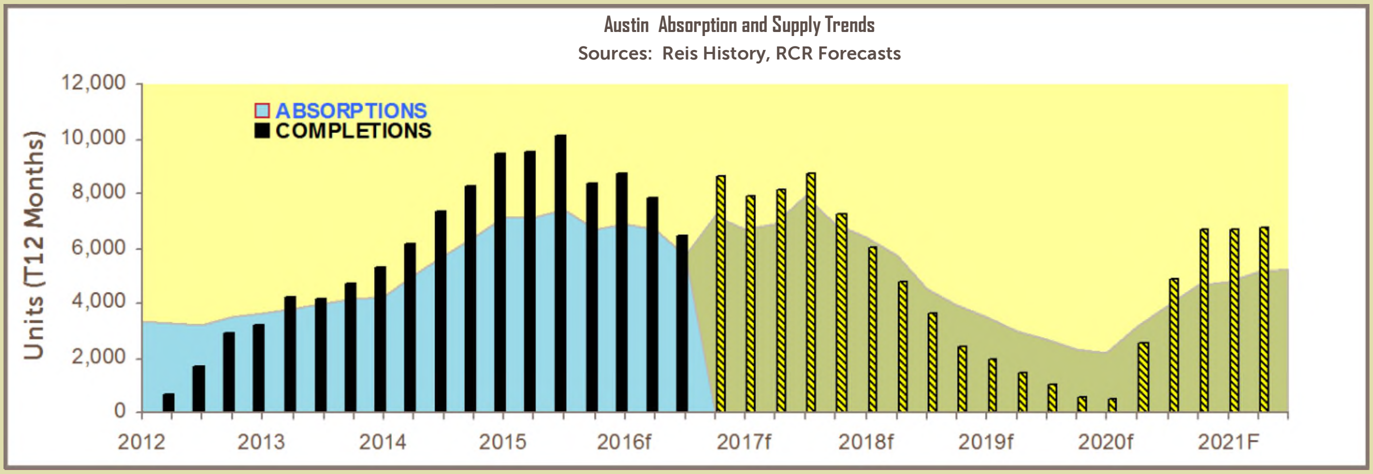
Sales velocity declined during the summer as 23 properties valued at $5 million or more exchanged hands, down from 32 and 26 trades in the prior and penultimate quarters and 26 during the year-earlier period. **RCR** estimate that proceeds averaged about $650mm, down from $800mm and $950mm in 2Q16 and 1Q16, respectively. The average price of units sold for which pricing information was publicly available was $168,361, a series record.

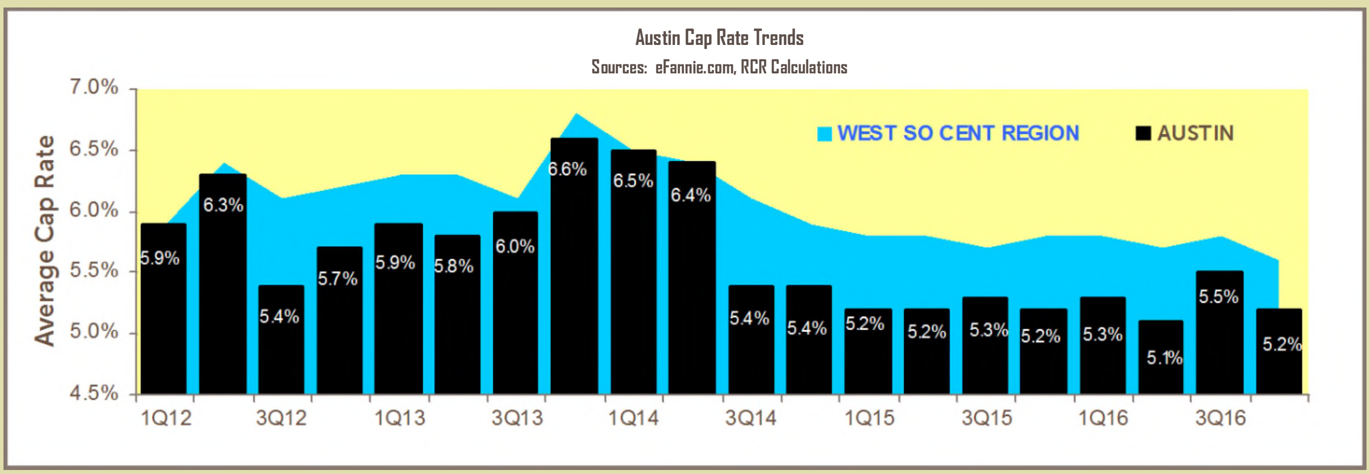
Fourth quarter velocity was considerably faster. A total of at least 38 transactions were consummated valued at more than $1.1 billion. The average unit price was $151,049, second highest in the series.

Cap rates averaged about 5.5% overall. A-/A quality assets traded to initial yields in the 4.75% to 5.20% region. Class-B+ properties commanded yields in the 5% to 5.5% range. Value-adds traded from the low-5% area to so high as 6.5%.

Employing a generic B+ purchase cap rate of 5.1% (down 15bps quarter-on-quarter), a terminal cap rate of 5.8%, and model derived rent and occupancy point estimates, we calculate that an investor would expect to earn a 7.1% 5-year unlevered IRR over the course of a 5-year hold. At this level, Austin ranks #20 among the **RED 47** metro peer group., 2nd in Texas after Houston. Unfortunately, model standard errors are well above average, denoting a relatively uncertain (risky) environment. As a result, Austin's risk-adjusted index is only 2.89, ranking 40th among the **RED 47** peers.

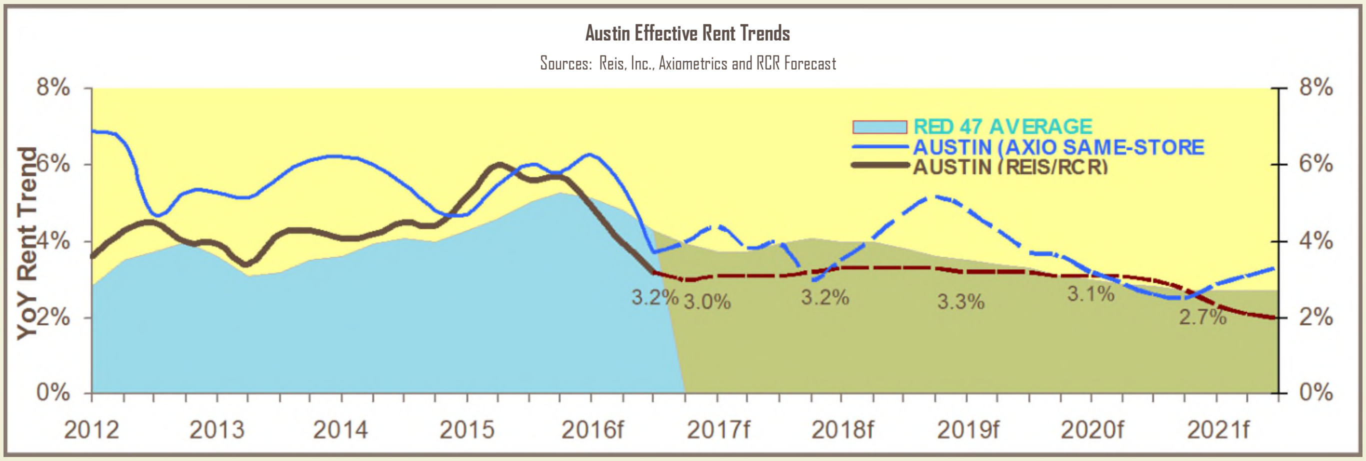


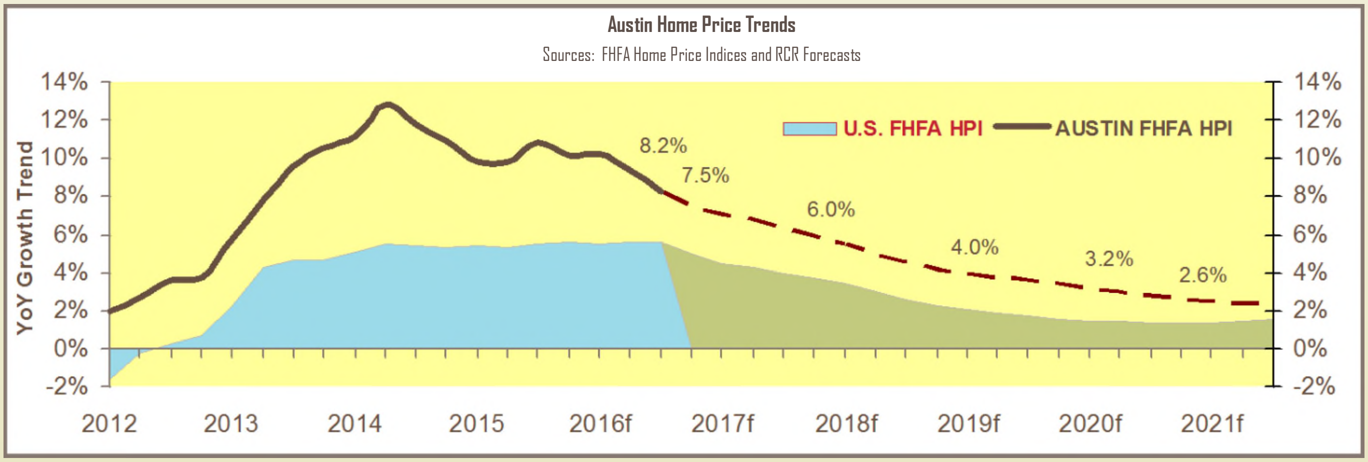


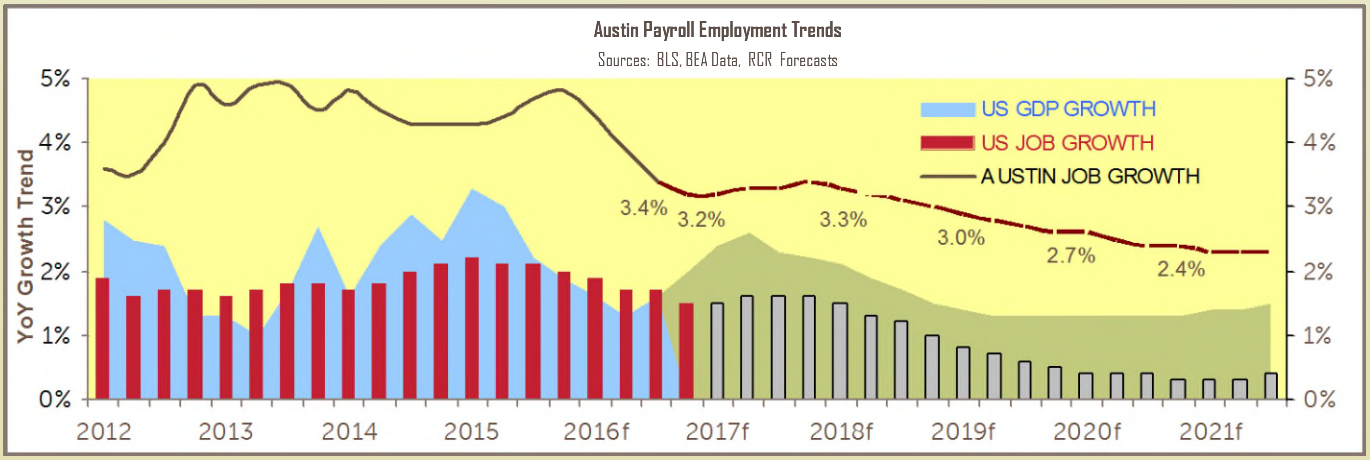


NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/Type (Constr.)	Approx. Date of Transaction	Total Price (in millions)	Price / Per Unit	Estimated Cap Rate
Bexley at Lakeline (Highway 183 / Lakeline Mall)	A+ / WF LR (2015)	10-Sep-2016	$41.6 (est.)	$121,047	5.05%
Remington Hills Apts. (Far South / Shady Hollow / Ford Oaks)	B- / GLR (2008)	25-Sep-2016	$27.2 (est.)	$130,926	4.8%
The Timbers (San Marcos / Texas State University)	C+ / Std. Hsg. (1984)	4-Oct-2016	$16.3	$105,161	5.23%
Bridge at Volente (Cedar Park / Anderson Mill)	B / GLR (1999)	5-Oct-2016	$26.4 (est.)	$127,094	6.51%
Deerfield (Far South / Cherry Creek / Grand Oaks)	A / GLR (2001)	6-Nov-2016	$48.9	$150,926	5.1%
Post West Austin (Central Austin W. / Rosedale)	A- / MB MR (2009)	1-Dec-2016	$56.3 (alloctd.)	$171,058	5.0%


Austin Effective Rent Trends
Sources: Reis, Inc., Axiometrics and RCR Forecast
YoY Rent Trend
RED 47 AVERAGE
AUSTIN (AXIO SAME-STORE
AUSTIN (REIS/RCR)
3.2%
3.0%
3.2%
3.3%
3.1%
2.7%
8%
6%
4%
2%
0%
2012
2013
2014
2015
2016f
2017f
2018f
2019f
2020f
2021f


Austin Home Price Trends
Sources: FHFA Home Price Indices and RCR Forecasts
YoY Growth Trend
U.S. FHFA HPI
AUSTIN FHFA HPI
8.2%
7.5%
6.0%
4.0%
3.2%
2.6%
14%
12%
10%
8%
6%
4%
2%
0%
-2%
2012
2013
2014
2015
2016f
2017f
2018f
2019f
2020f
2021f


Austin Payroll Employment Trends
Sources: BLS, BEA Data, RCR Forecasts
YoY Growth Trend
US GDP GROWTH
US JOB GROWTH
AUSTIN JOB GROWTH
3.4%
3.2%
3.3%
3.0%
2.7%
2.4%
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		
		3Q15	3Q16	Change	3Q15	3Q16	Change
Central	6.0%	$1,259	$1,291	2.5%	11.7%	10.0%	-170 bps
East	6.1%	$832	$949	13.9%	7.1%	6.5%	-60 bps
Far North Central	0.6%	$677	$726	7.3%	5.0%	4.0%	-100 bps
Far Northwest	1.4%	$1,047	$1,085	3.6%	4.3%	3.9%	-40 bps
Far South	4.6%	$1,051	$1,101	4.8%	6.2%	7.0%	80 bps
Highway 183 / Cedar Park	4.2%	$886	$913	3.0%	6.8%	7.6%	80 bps
Near North Central	18.5%	$828	$890	7.6%	1.5%	8.1%	660 bps
Near Northwest	0.0%	$922	$948	2.8%	1.5%	1.1%	-40 bps
Near South Central	5.0%	$1,130	$1,193	5.6%	12.4%	9.9%	-250 bps
North Travis	5.6%	$906	$964	6.4%	4.7%	5.6%	90 bps
Ranch Rd 620N / FM2222	0.0%	$1,207	$1,247	3.3%	12.0%	9.1%	-290 bps
Round Rock / Georgetown	1.6%	$949	$984	3.7%	5.9%	3.7%	-220 bps
San Marcos/North Hays Co.	14.9%	$876	$922	5.3%	6.6%	7.9%	130 bps
Southeast	2.2%	$897	$916	2.1%	5.0%	7.0%	200 bps
Metro	4.3%	$984	$1,015	3.2%	6.3%	6.4%	10 bps

Axiometrics 3Q16 Same-Store, Stabilized Property Submarket Occupancy & Effective Rent Trends (Unit-weighted Averages)

Submarket	Annual Rent Growth	Occupancy	Submarket	Annual Rent Growth	Occupancy
Central	-2.0%	93.9%	Near South Central	1.3%	95.6%
East	1.7%	92.6%	North Travis	5.2%	95.1%
Far North Central	6.3%	94.9%	Northwest	3.4%	93.5%
Far Northwest	4.3%	95.7%	Round Rock/Georgetown	5.9%	95.3%
Far South	2.9%	94.9%	San Marcos	4.0%	96.2%
Hwy 183/Cedar Park	3.7%	95.3%	Southeast	5.1%	93.4%
Near North Central	4.0%	95.2%	West	-1.3%	93.8%
Near Northwest	2.4%	95.4%	Metro	3.7%	94.8%

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