

### PAYROLL JOB SUMMARY

Average Payrolls	2,516.0m
Annual Change	99.6m (4.1%)
RCR 2016 Forecast	103.1m (4.3%)
RCR 2017 Forecast	99.1m (4.0%)
RCR 2018 Forecast	94.0m (3.6%)
RCR 2019 Forecast	72.1m (2.7%)
RCR 2020 Forecast	57.7m (2.1%)
Unemployment (NSA)	3.4% (Nov.)

### 3Q16 PAYROLL TRENDS AND FORECAST

Dallas's third quarter employment growth was on the low-end of the recent range at a 99,600-job, 4.1% year-on-year pace but nevertheless represented the eighth consecutive quarterly advance of 4% or faster. Only two other metros among the nation's 50 largest can boast of as many as six (Austin, Orlando). High-skilled services contributed the lion's share as financial, business, education and healthcare services added workers to payrolls at a combined 44,200-job, 4.6% y-o-y rate, up from 2Q's 4.4% pace. Hiring by leisure and personal service concerns and retailers also was brisk (26,200/4.6%), but weaker conditions emerged in the goods producing sectors. Construction and factory headcounts declined -600 jobs; the first loss recorded in nearly six years. Electronic and transportation equipment manufacturing attrition was notable as each subsector declined more than -3% y-o-y.

The seasonally-adjusted data series painted a still brighter picture. These data show that Dallas minted a net of 34,800 jobs from July to September, representing the largest three consecutive month add in the 27-year BLS historical data series.

**RED Research's** personal income and payroll models project further above normal growth through 2018. The payroll model uses US job growth, the rate of change in the fed funds rate and personal consumption expenditure growth as independent variables to achieve a 98.6% adjusted-R<sup>2</sup> (SE=0.3%). The model projects 3.9% or faster growth until 2Q18, followed by gradual deceleration to the 2% area by the end of the 5-year forecast interval. Personal income should advance at a 5.9% annual average rate over the forecast period, 50% faster than the 3.9% national average.

### OCCUPANCY RATE SUMMARY

Occupancy Rate (Reis)	95.7%
RED 51 Rank	72 <sup>nd</sup>
Annual Chg. (Reis)	+0.5%
RCR YE16 Forecast	95.2%
RCR YE17 Forecast	94.6%
RCR YE18 Forecast	94.2%
RCR YE19 Forecast	93.3%
RCR YE20 Forecast	92.2%

### 3Q16 ABSORPTION AND OCCUPANCY RATE TRENDS

Reis recorded robust space demand during the third quarter as tenants leased a net of 3,883 vacant units, representing the third highest summer season absorption total in the 25-year Reis data series. After developers added a modest net of 1,015 units to inventory average occupancy jumped 60 basis points sequentially (50bps year-on-year) to 95.7%, a 15-year high. Supply-rich Richardson and Central Dallas submarkets chalked down the largest sequential occupancy gains, rising 340 and 310bps, respectively.

Axiometrics surveys of 1,450 Dallas properties found average same-store stabilized and total property occupancy rates of 95.2% and 95.0%, respectively. Each fell -10bps y-o-y. Among stabilized properties, class-B led on 95.3%, followed by classes-C (94.9%)

and -A (94.7%). Only "C" notched a y-o-y advance (+20bps), while supply heavy class-A tumbled -40bps. Carrollton and Grand Prairie submarkets recorded rates above 96%, while No. White Rock and Far Northeast remained sub-94%. Denton Co. (+160bps) and North Dallas (+130 bps) made the largest gains; Garland (-160bps) and No. White Rock (-70bps) retreated. Oaklawn dropped -30bp to 94.7%.

Supply will remain at a 10,000-unit annual pace or higher through 2018, and our supply model suggests that it may reaccelerate in the forecast out-years. Demand promises to be consistently constructive but no match for the anticipated supply wave, sending occupancy falling to the 93% level in a few years. Reis are more optimistic, projecting sharply lower supply in 2019 and 2020.

### EFFECTIVE RENT SUMMARY

Mean Rent (Reis)	\$958
Annual Change	5.6%
RED 51 Rent Change Rank	9 <sup>th</sup>
RCR YE16 Forecast	5.5%
RCR YE17 Forecast	4.8%
RCR YE18 Forecast	4.5%
RCR YE19 Forecast	3.7%
RCR YE20 Forecast	3.0%

### 3Q16 EFFECTIVE RENT TRENDS

Dallas rents continued to grind higher over the summer, rising \$14 (1.5%) sequentially to an average of \$958, according to Reis, representing the 6th consecutive quarterly advance of 1.3% or greater. Expressed on a year-on-year basis, the average advanced at a 5.6% pace, down marginally from 2Q16's 18-year record high 5.8%. The service noted that class-B&C units provided the greater impetus as sector asking rents pushed 1.6% higher to \$772 in 3Q, while class-A rents increased only 1.2% to \$1,270.

Axiometrics data suggest rents at larger, professionally-managed properties increased at a slightly faster pace. A sample of 1,187 stabilized, same-store assets recorded average sequential and annual rent growth of 1.5% and 6.3% in 3Q16, down from 2.6% and

6.9%, respectively, in 2Q. Annual rent growth topped 6% for the 8<sup>th</sup> consecutive quarter. Class-A lagged badly at 2.3%, as classes-B and -C increased more than 7%. Far Northeast, Grand Prairie and Mesquite submarkets enjoyed 10%+ growth, while five others gained 8% or more. On the other hand, supply-rich infill East and Northwest Dallas and Oaklawn posted sub-2% annual increases.

**RCR** employed payroll (+), home price (-) and Baa spread (+) variables to specify a 97.6% ARS (SE=0.4%) Dallas rent growth model. The model projects 4%+ y-o-y rent increases through 2Q19, with slower trends after attributable to weaker job growth. Dallas rents are forecast to rise at a 3.8% annual compound rate, ranking 15<sup>th</sup> among the **RED 47** peer group; 1<sup>st</sup> among Texas metros.

### TRADE & RETURN SUMMARY

\$5mm+ / 80-unit+ Sales	91
Approximate Proceeds	\$1.9bn
Average Cap Rate (FNM)	5.8%
Average Price / Unit	\$122,851
Expected Total Return	7.3%
RED 47 ETR Rank	17 <sup>th</sup>
Risk-adjusted Index	8.26
RED 47 RAI Rank	1 <sup>st</sup>

### 3Q16 PROPERTY MARKETS AND TOTAL RETURNS

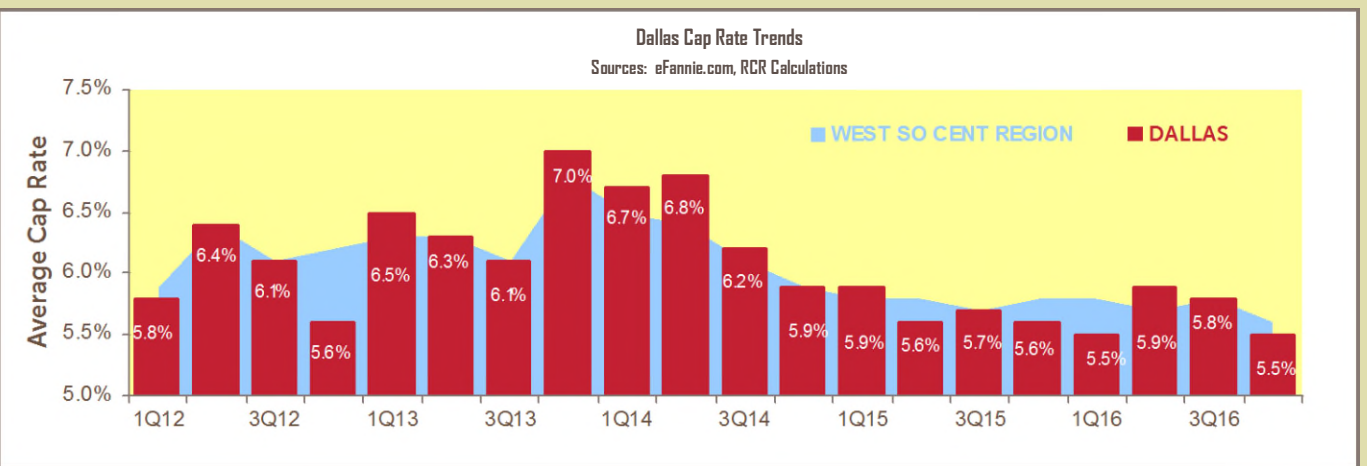
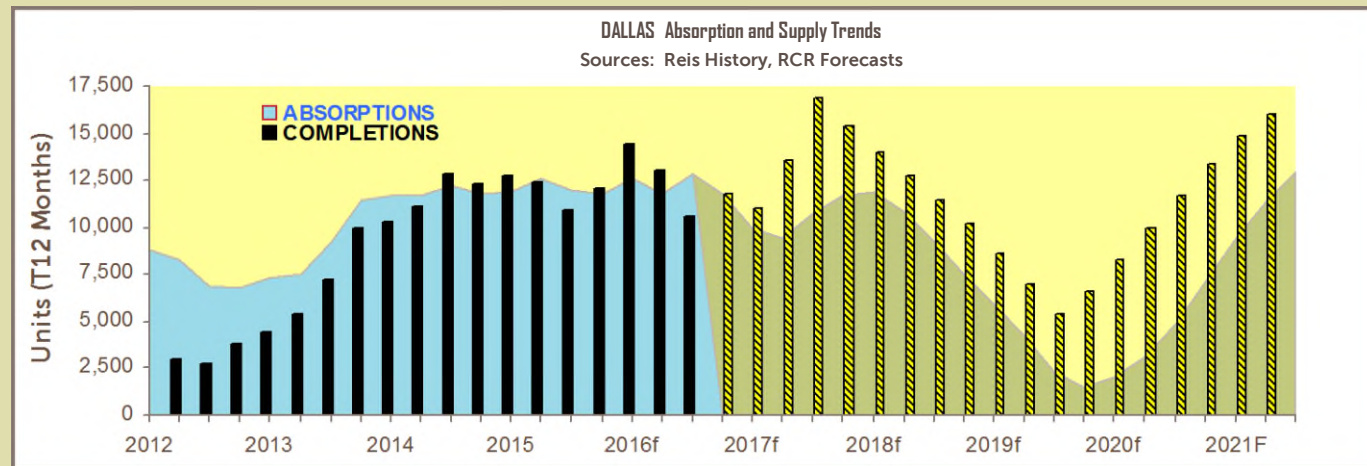
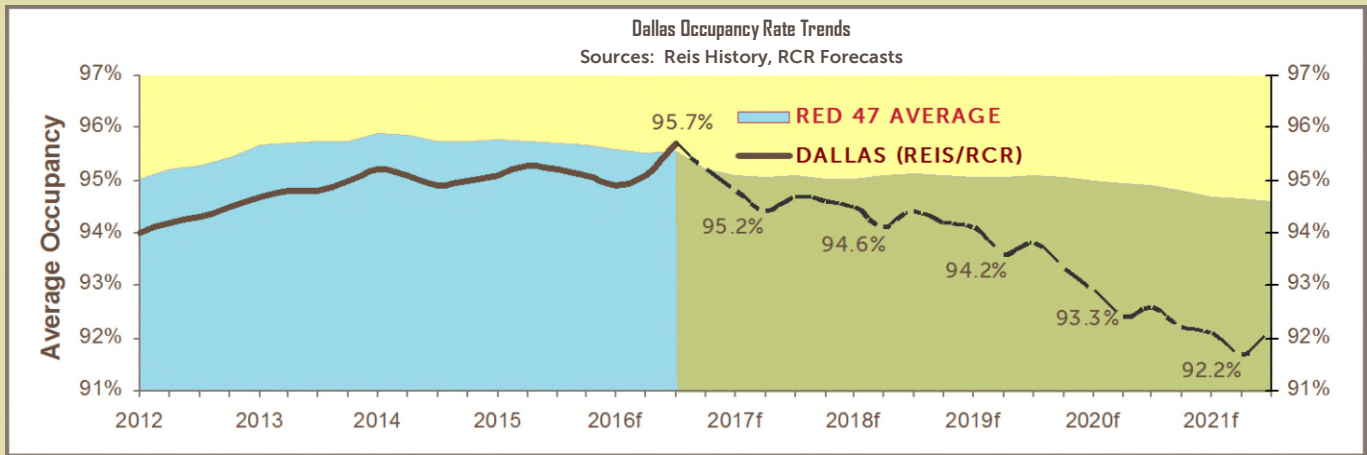
Sales velocity soared during the third quarter, from 46 transactions of 80-unit properties valued at \$5 million or more in 2Q16 to 91, an all-time Dallas record. Proceeds totaled at least \$1.9 billion, based on an average unit value of \$90,000, up from about \$1.2bn in the prior quarter. The average price of units sold for which pricing information were available was \$122,851.

Fourth quarter trade was nearly as robust. Data available in early January identified 76 completed transactions during the period for gross proceeds of approximately \$1.7bn. Moreover, the average price per unit was \$123,033, the highest metric ever recorded.

Third quarter cap rates averaged 5.25%, according to CoStar, near

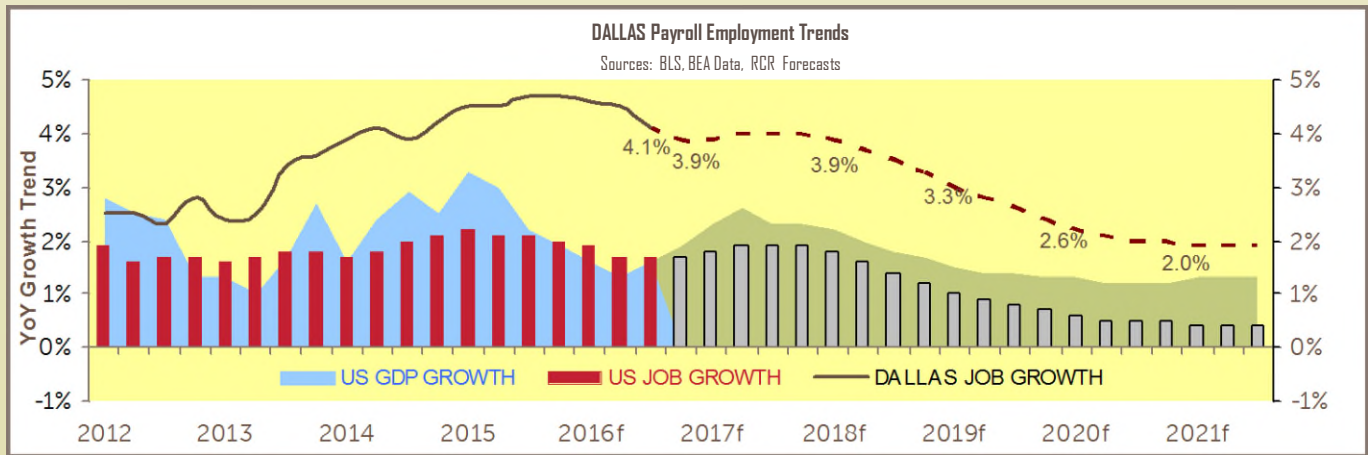
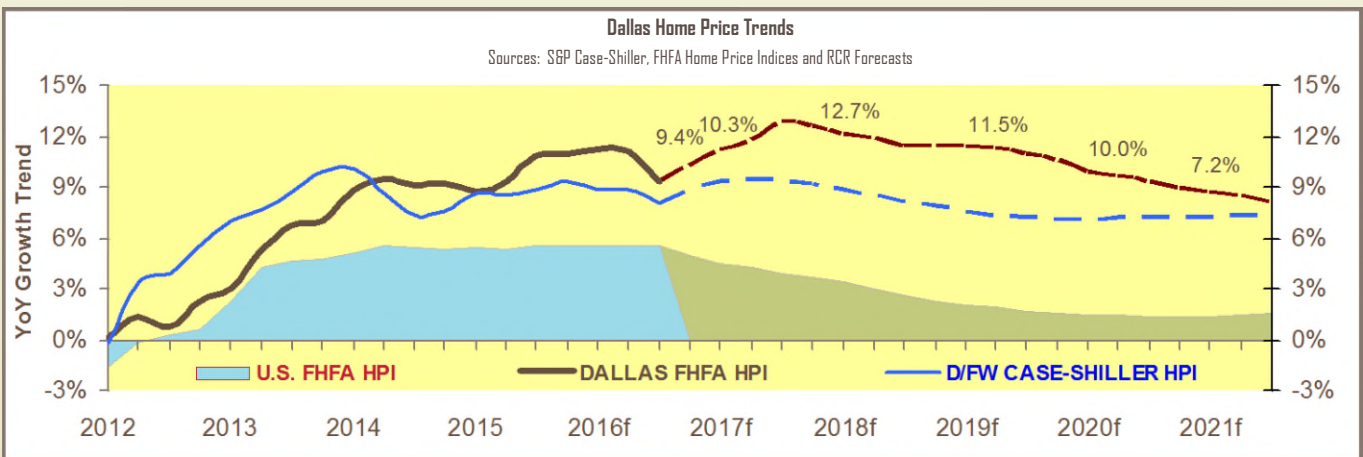
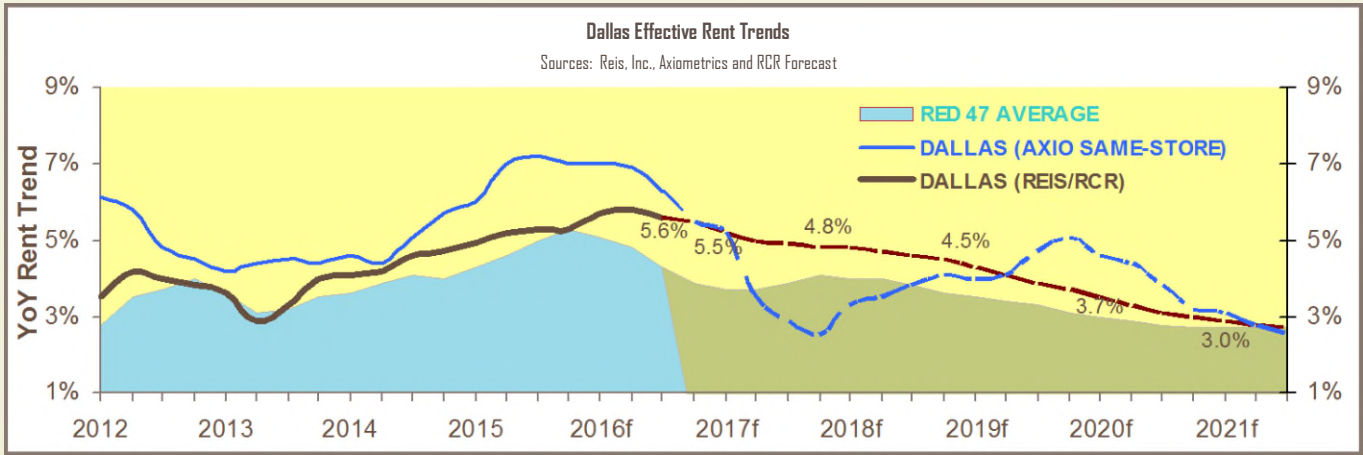
the historic series low. Class-A/B+ properties traded in the high-4% to low-5% range. Class-B and valued-add assets gravitated toward the 5.25% to 5.75% area. Class-C and affordable situations traded to yields ranging from 6% to 7%.

**RCR** elected to reduce the Dallas cap rate proxy 15bps to 5.25% to reflect current market conditions. Using this going in rate, a terminal cap of 5.9% and model derived occupancy and rent point estimates we calculate that an investor would expect to earn a 7.3% unlevered annual total return on a five year hold, 17<sup>th</sup> highest among the **RED 47**. Model standard error and thus uncertainty are low, boosting risk-adjusted returns. Indeed, Dallas's risk-adjusted index (RAI) of 8.26 ranks first among the **R47** metro peer group.



## NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/Type (Constr.)	Approx. Date of Transaction	Total Price (in millions)	Price / Per Unit	Estimated Cap Rate
Skyline Place (Southeast / Parkdale)	LIHTC / GLR (1987)	12-Sep-2016	\$16.0	\$50,314	6.95%
Villa Vista (No. White Rock / Highland Meadows)	C / GLR (1983)	25-Sep-2016	\$13.0	\$61,905	5.61%
The Livingston Apts. (Plano / Windhaven & Midway)	A- / GLR (1998)	8-Nov-2016	\$34.3	\$190,556	5.20%
Highlands of Preston (Plano / Preston Ridge)	B / GLR (1984)	23-Nov-2016	\$48.6	\$127,895	5.15%
Post Sierra Frisco Bridges (Plano / Frisco / Preston Ridge)	B+ / MB MR (2009)	6-Dec-2016	\$38.0 (alloctd)	\$141,861	4.9%
Post Addison Circle (Carrollton / Addison / Prestonwood)	B+ / RC MR (1998)	6-Dec-2016	\$161.4 (alloctd)	\$156,846	4.9%



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## SUBMARKET TRENDS (REIS)

Submarket	Inventory % Change	Effective Rent			Physical Vacancy		
		3Q15	3Q16	Change	3Q15	3Q16	Change
Carrollton / Addison	1.0%	\$863	\$894	3.7%	3.6%	3.8%	20 bps
Central Dallas	6.8%	\$1,896	\$1,941	2.4%	8.6%	8.3%	-30 bps
East Dallas	4.2%	\$1,062	\$1,075	1.2%	8.8%	7.5%	-130 bps
Far North	0.9%	\$884	\$910	3.0%	2.0%	2.1%	10 bps
Far Northeast	0.0%	\$659	\$673	2.2%	3.4%	1.8%	-160 bps
Far Northwest	1.5%	\$762	\$799	4.9%	3.2%	3.7%	50 bps
Garland	0.9%	\$740	\$764	3.2%	4.2%	3.8%	-40 bps
Grand Prairie	0.0%	\$708	\$723	2.0%	2.8%	1.7%	-110 bps
Lewisville	3.7%	\$954	\$992	3.9%	7.7%	8.2%	50 bps
Mesquite / Seagoville	0.0%	\$730	\$767	5.0%	2.4%	2.0%	-40 bps
North	6.8%	\$896	\$943	5.2%	3.6%	4.3%	70 bps
North Irving	3.8%	\$924	\$1,005	8.7%	2.5%	2.7%	20 bps
North White Rock	0.8%	\$718	\$794	10.6%	4.0%	3.3%	-70 bps
Northwest	3.0%	\$989	\$1,027	3.8%	9.7%	4.4%	-530 bps
Northwest Denton County	2.9%	\$1,012	\$1,044	3.2%	9.0%	8.0%	-100 bps
Oaklawn	4.0%	\$1,352	\$1,435	6.2%	14.1%	9.5%	-460 bps
Plano / Allen / McKinney	2.4%	\$1,067	\$1,103	3.4%	6.0%	5.5%	-50 bps
Richardson	12.6%	\$909	\$972	6.9%	5.7%	6.4%	70 bps
South	9.4%	\$782	\$849	8.7%	8.2%	6.0%	-220 bps
South County	0.0%	\$747	\$766	2.6%	5.7%	4.5%	-120 bps
South Irving	0.0%	\$725	\$745	2.7%	2.0%	2.0%	0 bps
South White Rock / I-30	0.0%	\$658	\$682	3.6%	4.6%	4.3%	-30 bps
Southeast Dallas	0.0%	\$594	\$603	1.5%	3.0%	3.0%	0 bps
Southwest Dallas	0.3%	\$724	\$764	5.5%	5.5%	5.0%	-50 bps
Metro	2.9%	\$907	\$958	5.6%	4.8%	4.3%	-50 bps

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