DENVER, COLORADO

MARKET OVERVIEW & MULTIFAMILY HOUSING UPDATE

RED Capital Group | 4Q16 | March 2017

PAYROLL JOB SUMMARY

Average Payrolls	1,450.1m
Annual Change 4Q16	29.8m (2.1%)
RCR 2017 Forecast	37.6m (2.6%)
RCR 2018 Forecast	36.8m (2.5%)
RCR 2019 Forecast	28.8m (1.9%)
RCR 2020 Forecast	25.8m (1.7%)
RCR 2021 Forecast	21.8m (1.4%)
Unemployment (NSA)	3.1% (1/17)

4Q16 PAYROLL TRENDS AND FORECAST

Initial BLS employment data suggested that the Denver labor market recorded another strong year in 2016. After posting 50,000- and 51,100-job adds in 2014 and 2015, Denver was thought to have created 45,000 (3.2%) payroll positions last year. But the annual re-benchmark revisions told another, murkier story. Calendar 2016 results were revised down to a 35,600 (2.5%) job advance, while the 4Q16 year-on-year growth comparison was trimmed from 48,200 (3.4%) jobs initially to a more pedestrian 29,800 (2.1%).

Revised 4Q16 data were the weakest in five years, hurt by materially smaller job gains in consumer driven sectors. Construction, retail trade and financial services concerns hired workers at a collective 3,200-job, 0.9% year-on-year pace, down from an 8,600 (2.6%) job rate two quarters earlier. The food service and accommodations subsector experienced a similar hiring slowdown. Seasonally-adjusted figures suggest Denver created a quarterly net of 6,600 positions, the smallest fourth quarter add in five years.

RED Capital Research re-specified the DEN payroll model, using the rate of change of U.S. payroll growth, and metro personal income (+) and GDP_{t-4} (-) growth as independent variables to achieve a robust 98.3% adjusted-R^2 (S.E.=0.3%) predictive model. Using our current base macroeconomic forecast, which anticipates faster GDP growth in 2017. but a return to "new normal" conditions after, the model projects stronger job creation in 2017 and 2018. followed by constructive but weaker job growth in the later years of the forecast interval. Moody's Analytics are more pessimistic, particularly in the final years (2020-2021)of the forecast period.

OCCUPANCY RATE SUMMARY

Occupancy Rate (Reis)	94.9%
RED 51 Rank	44th
Annual Chg. (Reis)	-0.9%
RCR YE17 Forecast	94.3%
RCR YE18 Forecast	94.2%
RCR YE19 Forecast	94.4%
RCR YE20 Forecast	93.7%
RCR YE21 Forecast	94.1%

4Q16 ABSORPTION AND OCCUPANCY RATE TRENDS

According to Reis, developers delivered 2,605 units to the Denver market during 4Q16, the largest single-quarter vintage since 2003. Although useful renter demand was recorded — tenants leased a net of 1,444 vacant units—occupancy declined 50 basis points sequentially and 90bps year-on-year to 94.9%, lowest in five years. Weak occupancy trends were entirely the province of the class-A sector. Segment vacancy increased 100bps sequentially to 7.0% (class-B&C=2.7%), highest metric since 2009.

Axiometrics surveys of same-store, stabilized properties recorded lower 4Q16 occupancy (93.8%), down 80bps y-o-y. Average occupancy was about 93.7% in February, 40bps below the year-earlier level. Class-C (94.1%, -120bps) occupancy was highest among segments, followed by classes-B (93.9%, -80bps) and –A (93.0%, -40 bps). Nine of 19 submarkets recorded rates above 94%, led by Denver Far Southeast and Lakewood North (94.6%). Downtown (92.8%) and Central (92.4%) Denver were among the submarkets with lowest occupancy. Aurora North (-150bps) and Central SW (-1.9%) suffered the largest year-on-year occupancy declines.

Supply will continue to hinder DEN occupancy. Reis expect 7,600 units to debut in 2017; 6,500 more in 2018. By contrast, our demand model projects absorption of 5,975 and 5,900, respectively; shortfalls that are expected to cut 70bps from average occupancy. Supply will subside in 2019, but metro occupancy is likely to remain under pressure as apartment demand decelerates as well.

EFFECTIVE RENT SUMMARY

Mean Rent (Reis)	$1,121
Annual Change	4.3%
RED 51 Rent Change Rank	15th
RCR YE17 Forecast	4.1%
RCR YE18 Forecast	4.3%
RCR YE19 Forecast	4.0%
RCR YE20 Forecast	3.5%
RCR YE21 Forecast	3.5%

4Q16 EFFECTIVE RENT TRENDS

Rising vacancy hindered rent growth, according to Reis, holding sequential quarter average effective rent gains to $1 (0.1%) in 4Q16, down from $14 (1.4%) in the year earlier quarter and $16 (1.5%) in 3Q16. The advance was the smallest recorded in more than seven years. Weakness in the supply challenged class-A segment was primarily responsible as class asking rents declined $8 (-0.6%) quarter-to-quarter after posting 1% or higher increases in each of the prior 18 quarters. The year-on-year comparison slipped to 4.3% from 5.8%, slowest in nearly three years.

Axiometrics same-store comparisons recorded average annual rent growth of 2.7% in 4Q, down from 7.3% in the same period of 2015. Y-o-Y gains in February rebounded to 3.8%. Contra Reis, the class-A (3.4%) segment posted the fastest 4Q16 rent growth (for the first time since 2012) topping classes-C (2.8%) and –B (2.5%). Submarket results were mixed. Aurora-Central SW (5.5%), Aurora North (8.3%) and Denver-Central (5.3%) chalked down useful gains, but Lakewood North and Littleton saw rents fall and five other submarkets failed to post increases of as much as 2%.

RCR analysis found that the rate of job growth (+) and occupancy (+) account for 96.4% of changes in DEN effective rent growth rates (S.E.=0.7%). The model generates an optimistic forecast wherein gains slow to the high-3% area in 2017, but recover to the low-4% region in 2018 and 2019. Rents are projected to rise at a 3.9% annual compound rate through 2021, ranking **RED 48** #8.

TRADE & RETURN SUMMARY

$5mm+ / 80-unit+ Sales	28
Approximate Proceeds	$1,642.3mm
Average Cap Rate (FNM)	5.1%
Average Price / Unit	$203,862
Expected Total Return	7.2%
RED 48 ETR Rank	16th
Risk-adjusted Index	3.33
RED 48 RAI Rank	34th

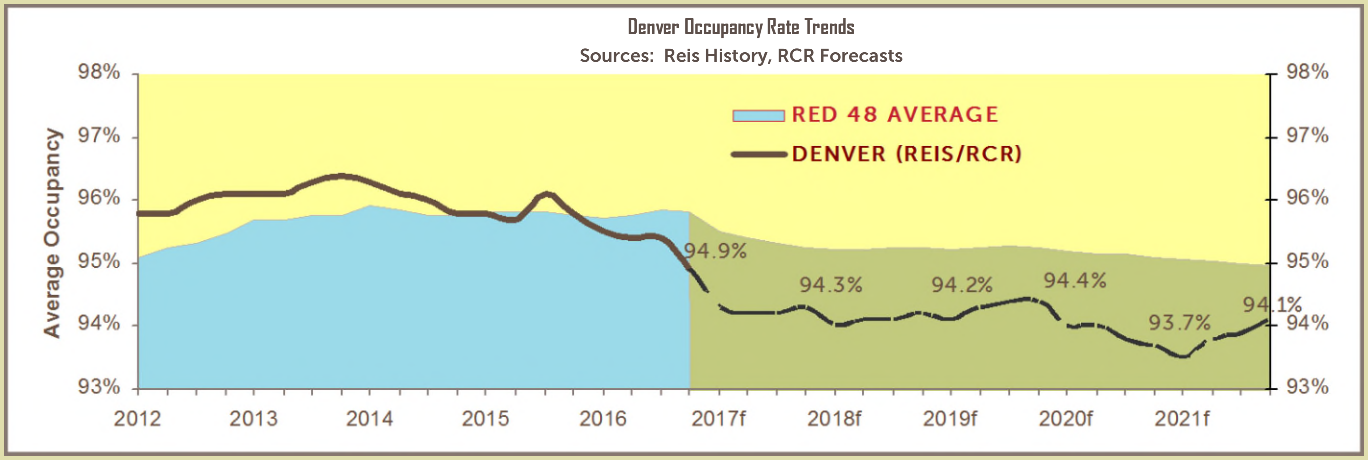
4Q16 PROPERTY MARKETS AND TOTAL RETURNS

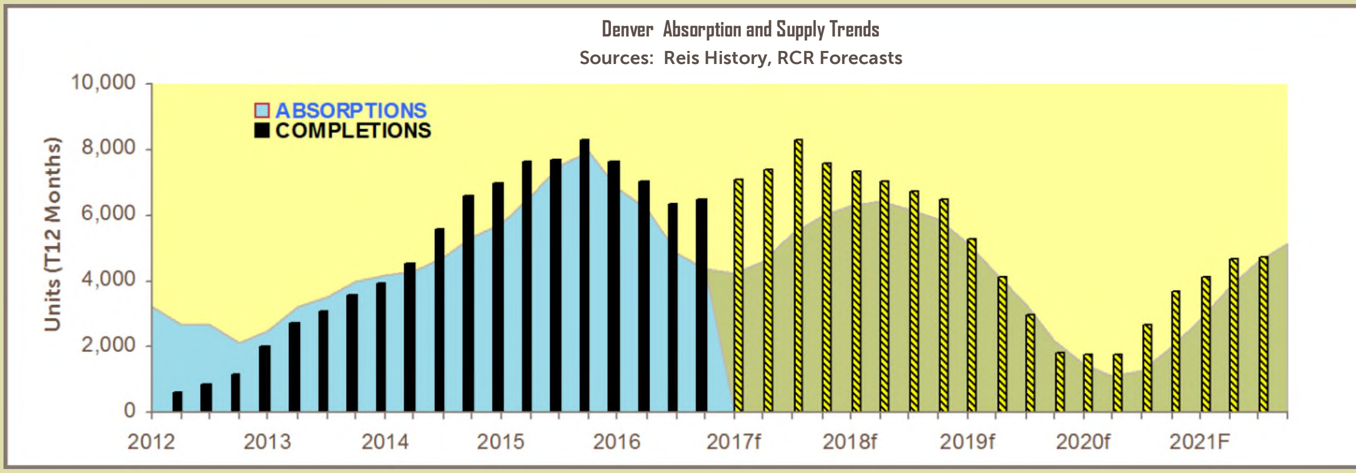
Sales velocity was healthy during the fourth quarter as 28 transactions of properties valued at $5 million were closed compared to 27 in the prior quarter. Proceeds totaled $1,642 million, up 17% from 3Q16 and 6% from the year-earlier period. With respect to total proceeds, 4Q16 was the second highest quarter in Denver series history after 1Q16's $2.8 billion, 50 transaction blow-out. The average price paid per unit was $203,862, third highest figure in the Denver series after 1Q16 ($211,139) and 2Q16 ($220,382).

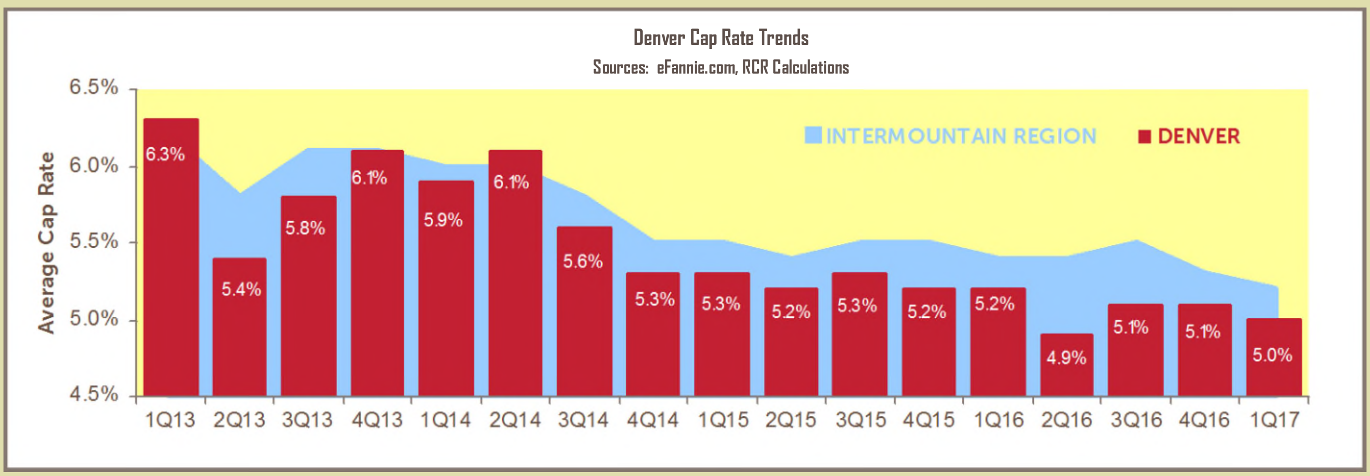
Activity in 1Q17 appears to have moderated. Through mid-March proceeds of 20 transactions totaled $994mm, down from $2.8 billion in the year-earlier period. The average price of units sold was comparable, however, on $206,239, down only 2% from 1Q16.

Cap rates of investment quality properties were largely below 5%. Mid-rise assets in top submarkets traded in the low-4% area. Assets in second tier submarkets were priced to high-4% to low-5% yields. Affordable properties gravitated to the mid-5% range.

Using 4.7% as the purchase cap rate proxy, 5.3% as the terminal cap rate and model derived occupancy and rent point estimates **RCR** calculate that an investor would expect to earn a 7.2% annual unlevered total return on a five-year hold. This ETR ranks sixteenth among the **RED 48** peer group. With respect to risk-adjusted returns, Denver's moderately high rent model standard error increases return uncertainty, causing the risk-adjusted index to fall to 3.33, ranking a lower 34th among the peer group.

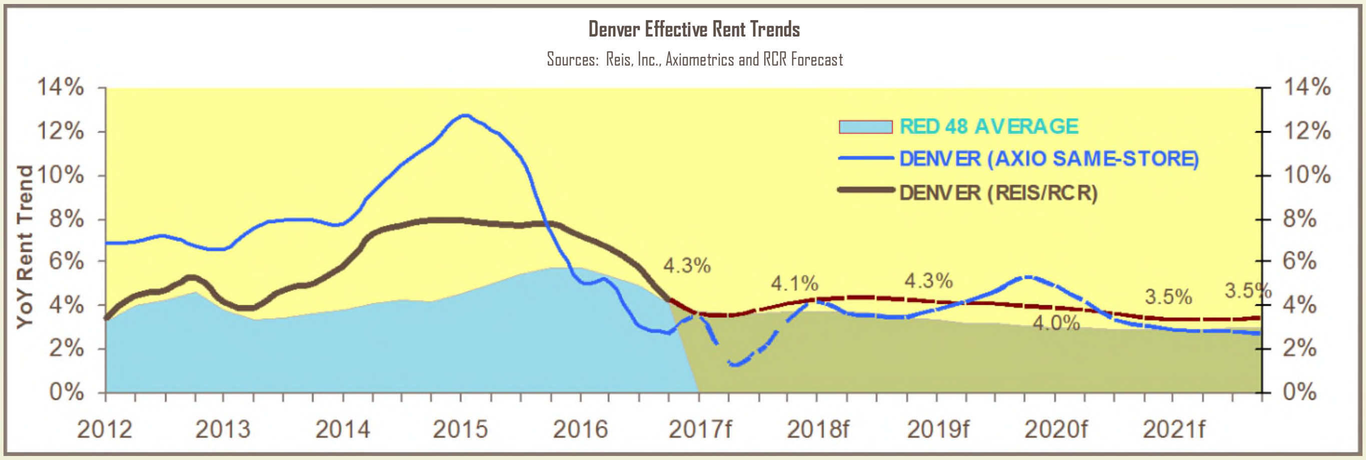


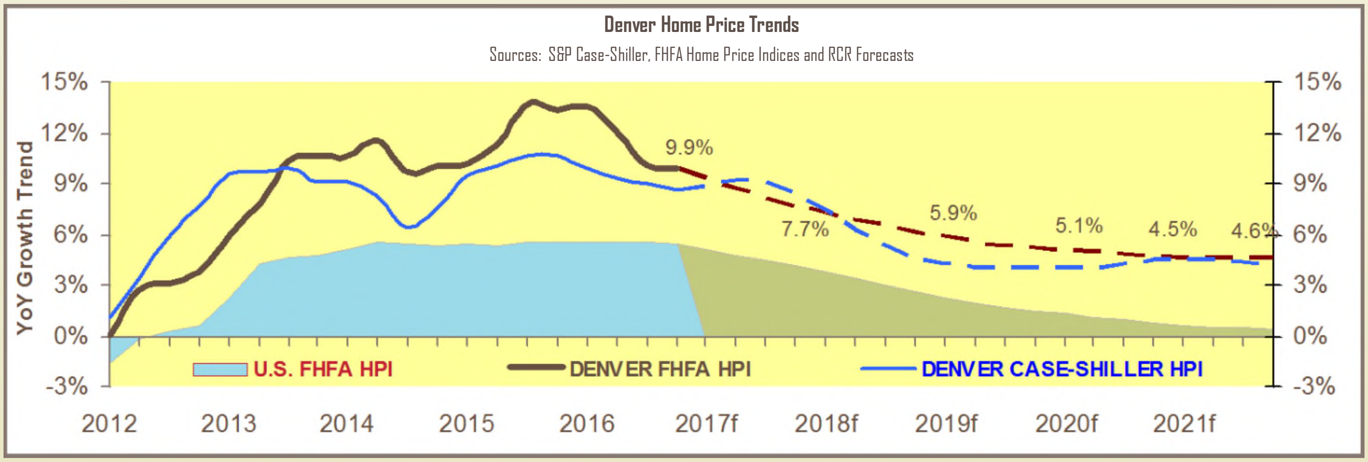


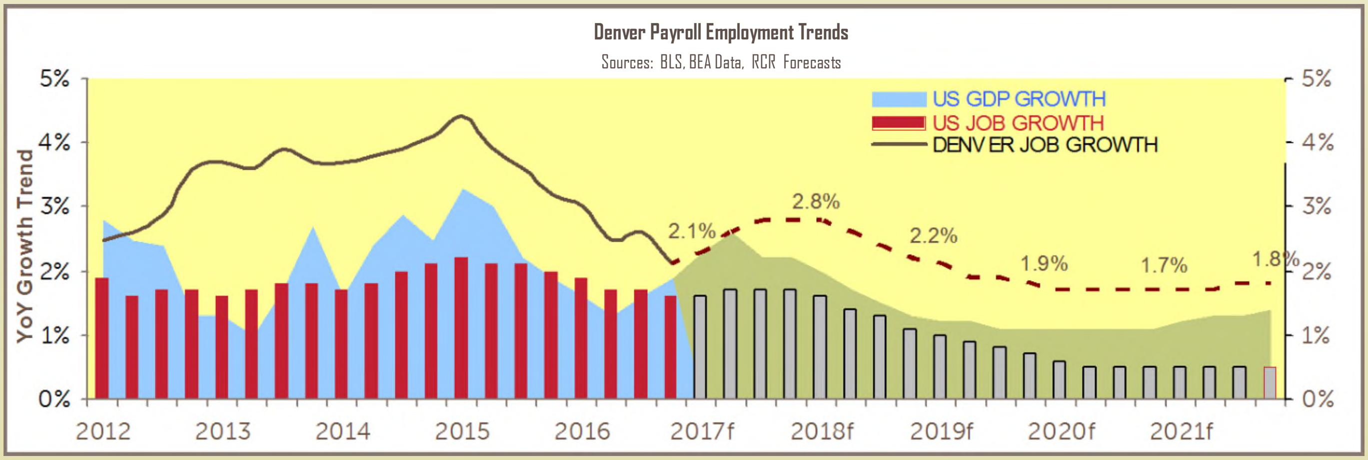


NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/Type (Constr.)	Approx. Date of Transaction	Total Price (in millions)	Price / Per Unit	Estimated Cap Rate
Griffis Marston Lake (Lakewood-South / Marston)	B- / GLR (2003)	14-Dec-2016	$62.0	$186,747	5.1%
Regatta (Northglenn / Jaycee Park)	B / GLR (2000)	14-Dec-2016	$81.8	$232,386	4.0%
Helios Apartments (Aurora-South / Tech Center / Belleview)	B+ / WF MR (2015)	20-Dec-2016	$69.9	$270,930	4.2%
Advenir Bear Valley (Lakewood-South / Bear Valley)	C / LR (1977)	15-Feb-2017	$38.0	$165,217	5.4%
Metropolitan Lincoln Station (Douglas Co. / Lone Tree)	B+ / MB MR (2006)	28-Feb-2017	$99.1	$229,930	4.7%
Griffis Union Station (Denver-Downtown / Five Points)	A- / SR MR (2010)	16-Mar-2017	$12.0	$315,000	4.2%


Denver Effective Rent Trends
Sources: Reis, Inc., Axiometrics and RCR Forecast
YoY Rent Trend
RED 48 AVERAGE
DENVER (AXIO SAME-STORE)
DENVER (REIS/RCR)
4.3%
4.1%
4.3%
4.0%
3.5%
3.5%
2012
2013
2014
2015
2016
2017f
2018f
2019f
2020f
2021f


Denver Home Price Trends
Sources: S&P Case-Shiller, FHFA Home Price Indices and RCR Forecasts
YoY Growth Trend
9.9%
7.7%
5.9%
5.1%
4.5%
4.6%
U.S. FHFA HPI
DENVER FHFA HPI
DENVER CASE-SHILLER HPI
2012
2013
2014
2015
2016
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
2.1%
2.8%
2.2%
1.9%
1.7%
1.8%
2012
2013
2014
2015
2016
2017f
2018f
2019f
2020f
2021f

SUBMARKET TRENDS (REIS)

Submarket	Reis Inventory Percent Change	Effective Rent			Physical Vacancy		
		4Q15	4Q16	Change	4Q15	4Q16	Basis Point Change
Arapahoe County	5.7%	$1,272	$1,338	5.2%	10.7%	6.4%	-430 bps
Arvada / Broomfield	4.4%	$1,049	$1,107	5.5%	6.2%	6.2%	0 bps
Aurora-Central-Southeast	-0.5%	$925	$933	1.0%	2.9%	2.4%	-50 bps
Aurora-Central-Southwest	0.0%	$862	$874	1.5%	5.2%	5.1%	-10 bps
Aurora-North	-0.4%	$837	$911	8.8%	2.2%	2.0%	-20 bps
Aurora-South	1.8%	$1,195	$1,176	-1.6%	5.7%	6.1%	40 bps
Denver-Central	5.6%	$1,127	$1,505	33.6%	7.6%	8.1%	50 bps
Denver-Downtown	9.0%	$1,218	$1,255	3.1%	7.9%	8.7%	80 bps
Denver-Far Southeast	0.0%	$894	$922	3.1%	3.8%	3.7%	-10 bps
Denver-North	12.9%	$1,616	$1,592	-1.5%	18.5%	12.5%	-600 bps
Lakewood-North	4.5%	$970	$1,023	5.5%	2.0%	3.3%	130 bps
Lakewood-South	0.0%	$1,096	$1,132	3.3%	2.8%	2.2%	-60 bps
Littleton	0.0%	$1,066	$1,053	-1.2%	5.6%	5.8%	20 bps
Northglenn / Thornton	0.0%	$946	$1,021	8.0%	5.4%	5.2%	-20 bps
Westminster	-2.2%	$999	$1,108	11.0%	2.9%	4.5%	160 bps
Metro	10.0%	$1,121	$1,298	15.8%	5.1%	5.9%	80 bps

Reis made material revisions to the Denver data series in 4Q16. The 4Q15 data show reflect unrevised data that may not be directly comparable.

FOR MORE INFORMATION ABOUT RED'S RESEARCH CAPABILITIES CONTACT:

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