CHICAGO, ILLINOIS

MARKET OVERVIEW & MULTIFAMILY HOUSING UPDATE

RED Capital Group | 4Q16 | April 2017

PAYROLL JOB SUMMARY

Average Payrolls	3,750.6m
Annual Change 4Q16	33.1m (0.9%)
RCR 2017 Forecast	42.5m (1.1%)
RCR 2018 Forecast	42.7m (1.1%)
RCR 2019 Forecast	22.1m (0.6%)
RCR 2020 Forecast	12.5m (0.3%)
RCR 2021 Forecast	17.9m (0.5%)
Unemployment (NSA)	5.1% (2/17)

4Q16 PAYROLL TRENDS AND FORECAST

The annual benchmark revision by the Bureau of Labor Statistics revealed that Chicago's labor market was stronger than previously understood in 2015. Establishments created 75,900 new jobs, about 10% greater than the initial estimate, But revised BLS data continue to show a material slowdown in 2016, with 2015's brisk 51,600-job 2.1% advance decelerating to 4Q16's 33,100-job, 0.9% year-on-year pace, the slowest rate recorded since 4Q10's 0.8% reading.

Declining growth was observed across industries in 4Q16, most notably in construction, retail trade and services. These sectors added workers at a collective 27,600-job y-o-y rate, down 42% from 3Q's 47,400-job gain. Annual comparisons in January and February were comparable (32,000/0.9%), but these data were boosted by an unsustainable 10,600-job, 4.1% bump in finance.

Seasonally-adjusted estimates were consistent. This series recorded a net loss of 2,000 position in 4Q16, down from a 20,800-job gain in the year-earlier quarter. Early 2017 data were more constructive, however, showing a 14,900-job betterment in January and February.

RED Research's CHI payroll model uses the rate of change of U.S. job growth, metro personal income and U.S. personal consumption expenditure growth and Baa-rated bond yields as independent variables to achieve an adjusted R^2 of 97.2% (S.E.=0.3%), The model shows job creation responding usefully to stronger national growth through MY18, reaccelerating to 1.1% to 1.4% annual growth rates. But we expect a return to the "new normal" slow growth regime by 2019, with negative consequences for Chicagoland: job growth is likely to slow to a sub-0.7% pace late in the forecast interval.

OCCUPANCY RATE SUMMARY

Occupancy Rate (Reis)	95.9%
RED 51 Rank	26th
Annual Chg. (Reis)	-0.1%
RCR YE17 Forecast	95.7%
RCR YE18 Forecast	95.4%
RCR YE19 Forecast	95.0%
RCR YE20 Forecast	95.0%
RCR YE21 Forecast	95.2%

4Q16 ABSORPTION AND OCCUPANCY RATE TRENDS

Chicago apartment demand was exceptional in 2016, sparked by healthy job growth and a distinct shift in household housing preferences in favor of renting. Tenants net leased 6,245 units last year, bettered only in 2010 in the 27-year Reis metro data history. Fourth quarter absorption also was useful as renters occupied a net of 1,715 units, the third highest single quarter result since 2011. But supply also increased — developers completed 2,825 units — enough to send occupancy down -0.2% sequentially to 95.9%.

Axiometrics surveys of larger, professionally-managed properties found materially weaker conditions. The average occupancy rate of 302 stabilized, same-store properties was 94.0%, down -40 basis points year-on-year. Classes-C (94.6%) and –B (94.1%) led among segments followed distantly by class-A (92.9%). Northside submarkets — Rogers & Lincoln Parks (96.7%), Belmont (95.1%) — were among the occupancy leaders. Conversely, core urban neighborhoods were prominent in the bottom half of the table, notably Loop (94.4%), City West (93.9%) and Gold Coast (92.5%).

Prospects for absorption in 2017 and 2018 are constructive. Point estimates from our model are, respectively, 5,062 and 4,748 units. But supply promises to be greater still — Reis project 2017 and 2018 deliveries to total 6,579 and 6,496—giving rise to a –50bps decrease in metro occupancy to 95.4%. Supply and demand should remain in near equilibrium for the balance of the forecast interval, holding occupancy steady in the low– to mid-95 percent region.

EFFECTIVE RENT SUMMARY

Mean Rent (Reis)	$1,225
Annual Change	4.3%
RED 51 Rent Change Rank	22nd
RCR YE17 Forecast	3.7%
RCR YE18 Forecast	3.3%
RCR YE19 Forecast	2.2%
RCR YE20 Forecast	2.3%
RCR YE21 Forecast	2.5%

4Q16 EFFECTIVE RENT TRENDS

The pace of rent increases held steady during the fourth quarter. Average unit effective rent increased $10 (0.9%) sequentially, matching the result from the prior quarter, Expressed on a year-on-year comparison basis, rents increased 4.3%, largely indistinguishable from results in each of the previous four quarters. Leadership shifted toward the class-B&C segment, which posted faster sequential growth, something of a change in form.

Axiometrics surveys of mostly larger assets again pointed toward moderately weaker conditions than reported by Reis. This sample recorded a unit-weighted average 2.4% year-on-year rent growth trend, down from 2.6% and 3.4% in the prior and year-earlier quarters, respectively. Class-B provided most of the momentum, rising at a 3.1% rate, easily outpacing classes-A (1.4%) and –C (0.5%). Four submarkets notched gains of 5% or more (Lincoln and Rogers Park, Glenview and Aurora). Again, core urban submarkets filled the lower ranks, most notably The Loop (-0.1%) and the Gold Coast (-0.2%). City West chalked down 12th highest of 19 submarkets with an annual rent advance of 2.8%.

RCR's rent outlook is fairly optimistic for the next two years, boosted by constructive trends in the variables with positive coefficients in our rent forecasting equation: job growth, absorption and home price appreciation. But these catalysts are expected to fade after 2018, slowing expected rent growth to 2.5% or slower for the balance of the 5-year forecast interval.

TRADE & RETURN SUMMARY

$5mm+ / 80-unit+ Sales	38
Approximate Proceeds	$1,553.2mm
Average Cap Rate (FNM)	5.4%
Average Price / Unit	$155,464
Expected Total Return	6.4%
RED 48 ETR Rank	43rd
Risk-adjusted Index	4.36
RED 48 RAI Rank	17th

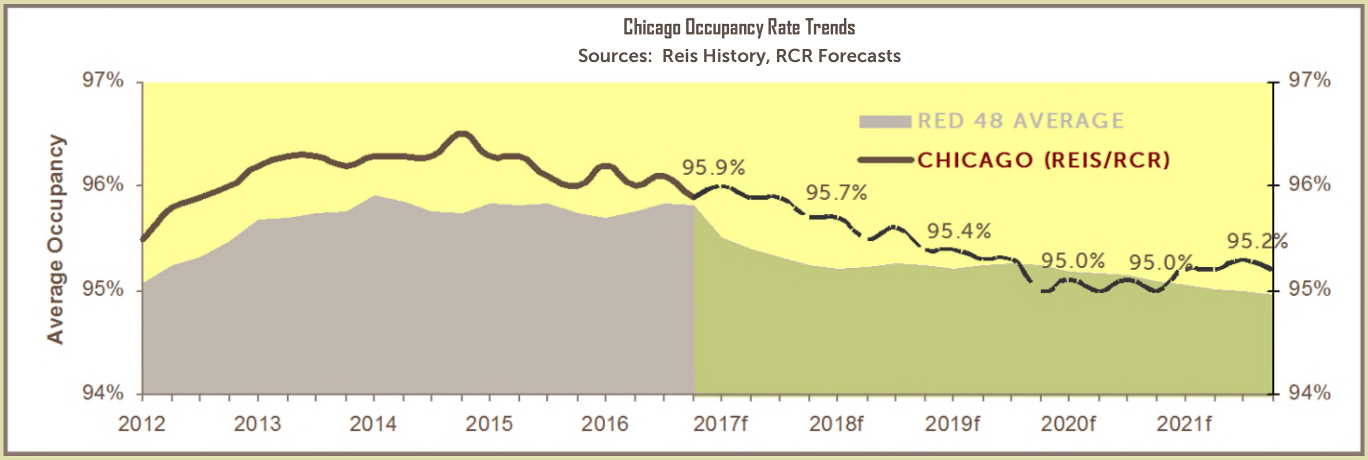
4Q16 PROPERTY MARKETS AND TOTAL RETURNS

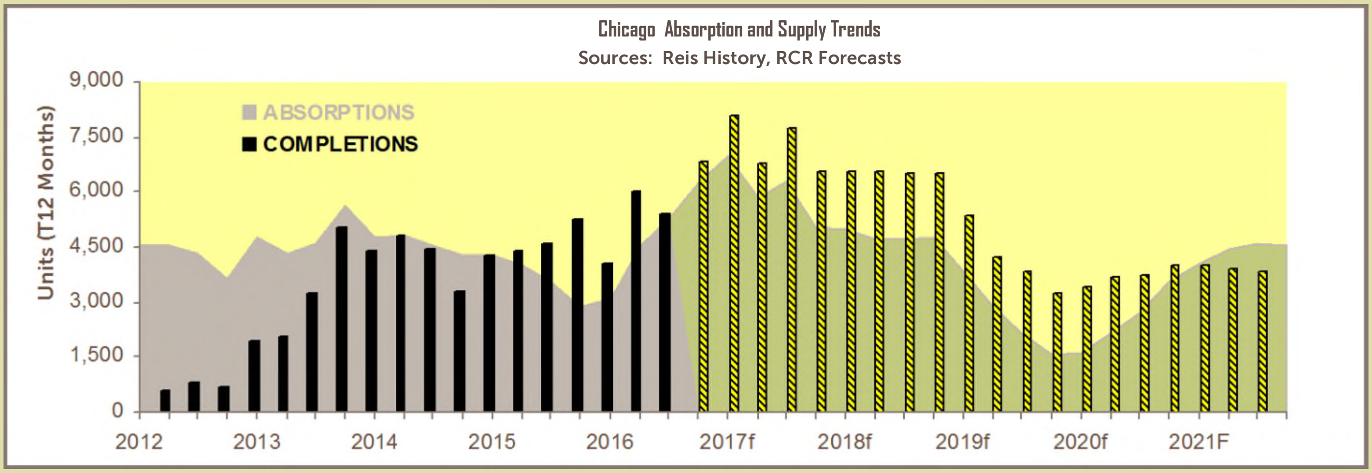
Perhaps in celebration of the Cubs, investors embraced Chicago opportunities in a big way in the fourth quarter. Buyers acquired $1.553 million of metro properties in 38 transactions, a quarterly market record for proceeds by 40%, and the second highest total for trade velocity after 2015. The average price per unit was $155,464, representing an 19% increase year-on-year.

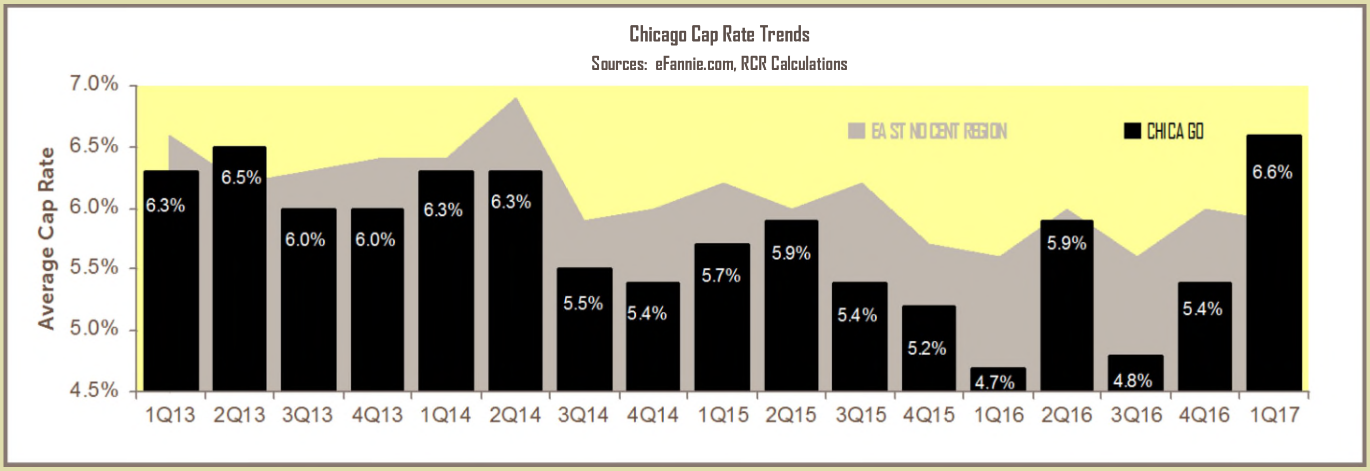
As observed in a number of markets, transaction volume declined precipitously in 1Q17, based on preliminary data. Proceeds fell –74% sequentially and -58% year-on-year to about $402 million, and only 10 properties exchanged hands.

Private buyers continued to dominate trade, accounting for 66% of purchases over the past six months. Institutional and private equity players accounted for most of the balance. Cap rates averaged about 5.5%, with infill trophies trading in the mid– to high-4s, B+ gardens in the low-5s and value-adds in the 5.5% to 6% range.

For valuation purposes, **RCR** bumped up the purchase cap rate proxy 20 basis points to 5.2%. Using a 5.9% terminal cap rate and model derived rent and occupancy point estimates we calculate that investor would expect to earn a 6.4% unlevered annual rate of return over a five-year hold. On this basis, Chicago ranks 43rd among the **RED 48** peer group. Chicago is a low-volatility market, however, especially with respect to rents. As a result, it ranks a strong peer group 17th on the basis of its risk-adjusted index.

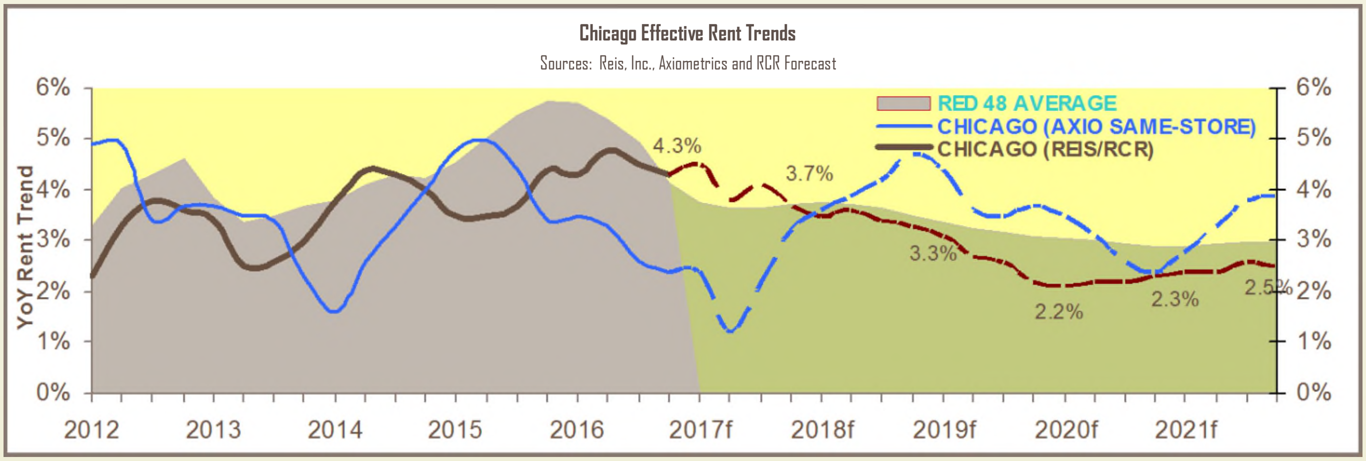


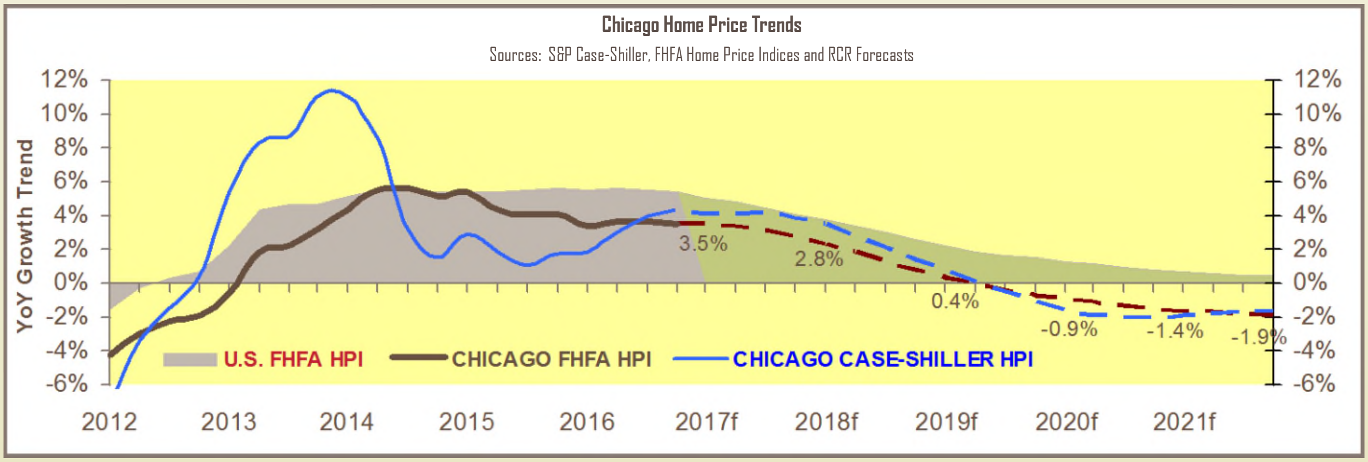


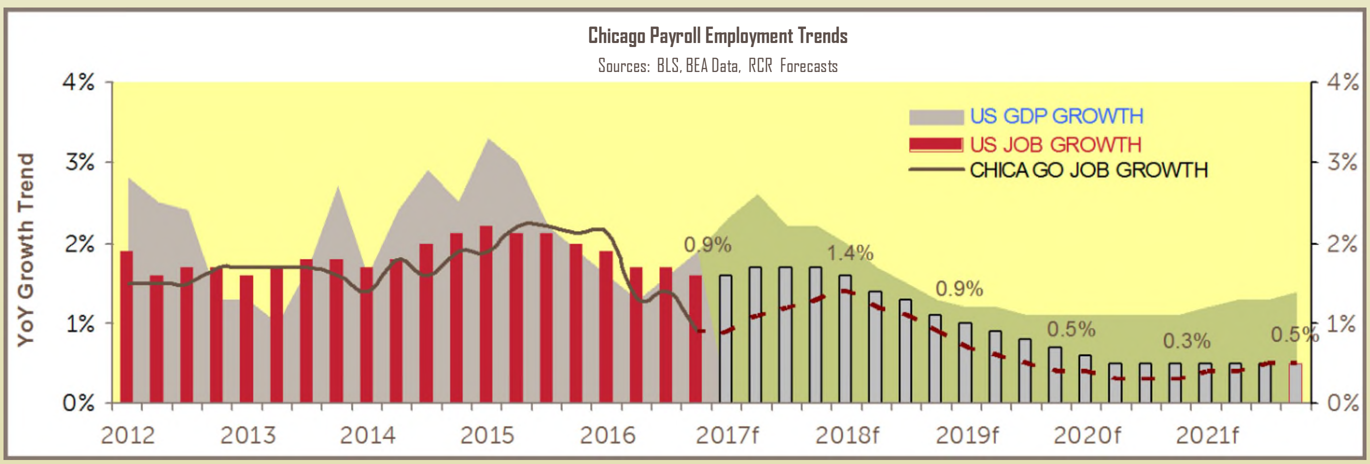


NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/Type (Constr.)	Approx. Date of Transaction	Total Price (in millions)	Price / Per Unit	Estimated Cap Rate
River North Park Apts. (Gold Coast / River North)	B+ / MB HR (1985)	23-Nov-2016	$117.0	$292,500	4.5%
Arbor Lakes Apts. (Wheeling / Arlington Heights)	B / GLR (1980)	1-Dec-2016	$60.5	$159,631	5.0%
River Run (Joliet / Naperville)	B+ / GLR (2003)	22-Dec-2016	$47.8	$231,917	5.2%
Axis Apartments (Gold Coast / Lakeshore & Erie)	A / SR HR (1986/2014)	30-Dec-2016	$225.0	$365,854	4.7%
Dwell at Naperville (Aurora / Naperville / Warrenville)	B / GLR (1990)	17-Feb-2017	$84.0	$210,000	5.3%
Madison at Racine (City West / Near West Side)	A / MB MR (2014)	14-Mar-2017	$99.6	$461,111	4.8%







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SUBMARKET TRENDS (REIS)

Submarket	Reis Inventory Percent Change	Effective Rent 4Q15	Effective Rent 4Q16	Change	Physical Vacancy 4Q15	Physical Vacancy 4Q16	Basis Point Change
Aurora / Naperville	0.0%	$1,122	$1,154	2.8%	2.2%	3.1%	90 bps
Belmont-Montrose	0.1%	$1,306	$1,333	2.0%	2.3%	3.6%	130 bps
City West	3.6%	$1,183	$1,249	5.6%	7.6%	6.6%	-100 bps
Downers Grove	0.0%	$998	$1,068	7.0%	2.5%	2.9%	40 bps
East Lake County	0.0%	$1,052	$1,074	2.1%	2.5%	2.1%	-40 bps
Glen Ellyn / Wheaton	1.0%	$1,014	$1,125	11.0%	3.3%	4.3%	100 bps
Glendale Heights	0.0%	$1,194	$1,242	4.0%	1.6%	1.7%	10 bps
Glenview / Evanston	2.1%	$1,215	$1,292	6.4%	6.4%	7.1%	70 bps
Gold Coast	6.8%	$2,105	$2,162	2.7%	8.4%	8.6%	20 bps
Joliet	0.0%	$879	$900	2.5%	4.7%	4.6%	-10 bps
Kane County	0.3%	$1,100	$1,136	3.2%	5.6%	4.2%	-140 bps
Lincoln Park	0.0%	$1,325	$1,346	1.6%	1.4%	1.6%	20 bps
McHenry County	0.0%	$1,006	$1,009	0.3%	2.4%	4.4%	200 bps
O'Hare	0.0%	$972	$970	-0.2%	3.0%	3.1%	10 bps
Oak Park	1.6%	$962	$1,020	6.1%	2.5%	3.1%	60 bps
Palatine	0.0%	$1,163	$1,208	3.9%	3.8%	3.9%	10 bps
Rogers Park / Uptown	1.6%	$873	$901	3.2%	2.9%	3.8%	90 bps
Schaumburg / Hoffman	0.0%	$1,066	$1,083	1.6%	3.0%	3.0%	0 bps
South Shore	1.0%	$957	$1,183	23.6%	3.6%	3.9%	30 bps
Southeast Cook County	0.0%	$864	$880	1.8%	2.8%	2.7%	-10 bps
Southwest Cook County	0.0%	$850	$869	2.3%	2.5%	2.3%	-20 bps
The Loop	14.0%	$1,889	$1,956	3.6%	6.4%	7.0%	60 bps
West Lake County	7.4%	$963	$1,049	8.8%	2.8%	4.8%	200 bps
Wheeling	1.4%	$1,189	$1,206	1.4%	3.5%	3.3%	-20 bps
Woodridge / Lisle	0.0%	$1,072	$1,091	1.7%	2.4%	2.2%	-20 bps
Metro	1.5%	$1,175	$1,225	4.3%	4.0%	4.1%	10 bps

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