

PAYROLL JOB SUMMARY

Average Payrolls	1,582.0m
Annual Change 1Q17	19.2m (1.2%)
RCR 2017 Forecast	25.5m (1.6%)
RCR 2018 Forecast	28.0m (1.7%)
RCR 2019 Forecast	18.7m (1.1%)
RCR 2020 Forecast	7.6m (0.5%)
RCR 2021 Forecast	5.5m (0.3%)
Unemployment (NSA)	3.7% (3/17)

1Q17 PAYROLL TRENDS AND FORECAST

After an exceptional run of good form during the two years ended last summer the OC economy began to exhibit distinct decelerating tendencies in recent months. First quarter payroll employment growth declined to a 5-year low 19,200-job, 1.9% year-on-year pace, less than one-half of the growth rate recorded in spring 2016. Materially slower expansion in business, healthcare and leisure service accounts was primarily responsible. Sector growth declined from a 21,100-job, 3.1% annual rate last summer to only an 8,400-job, 1.2% pace in 1Q17. Notably, hiring in professional and technical services, a key metro economic catalyst, was among the weaker industry segments.

Seasonally-adjusted payroll and Household Survey data

told a similar story. The former indicates that 4Q16 net job creation (-2,200) was the weakest quarter in six years, and 1Q17 (1,300 jobs) was hardly better. Household surveys show 1Q17 total employment up only 0.3% y-o-y.

RED Research's OC payroll model remains optimistic, however, reading the recent soft patch as a temporary lull. The 96.3% adjusted-R² (S.E.=0.5%) model uses US and LA_(t-1) payroll and personal consumption expenditure_(t-4) growth as independent variables. The model projects that metro job growth will catch a wave of faster national GDP and job growth in summer to reignite 2%+ expansion by the fall. Solid hiring should continue through 2018, followed by another slowdown as US growth shifts down to lower gear.

OCCUPANCY RATE SUMMARY

Occupancy Rate (Reis)	96.8%
RED 51 Rank	7 th
Annual Chg. (Reis)	+0.1%
RCR YE17 Forecast	96.9%
RCR YE18 Forecast	97.5%
RCR YE19 Forecast	97.7%
RCR YE20 Forecast	97.8%
RCR YE21 Forecast	97.6%

1Q17 ABSORPTION AND OCCUPANCY RATE TRENDS

County households continued to express pent-up demand for multifamily space as tenants absorbed a net of 720 vacant units (Reis) during 1Q17, up from 439 in the comparable period of 2016. Not coincidentally, developers concurrently delivered 718 new apartments, demonstrating the close correlation of supply and demand in the Southland. Occupancy was unchanged on 96.8% for second consecutive quarter and up 10 basis points year-on-year.

Axiometrics surveys of 401 same-store, stabilized properties recorded a 95.6% rate of occupancy in 1Q17, -20bps and -30bps below the year-earlier and prior quarters, respectively. Class-C (97.1%) posted highest occupancy, a

laurel held for more than seven years. Classes-B (95.6%) and -A (95.4%) followed. Seven of eighteen submarkets reported occupancy above 96% of which six featured average rent below \$2,000. Conversely, highest rent Newport Beach (\$2,625) chalked lowest occupancy on 92.9%.

OC is performing very much like a "barrier protected" market as inventory is projected to rise only 5% over five years, less than half the rates of Denver, Seattle and S.F. This will hold metro occupancy in good stead. RCR's demand model suggests that absorption will move in near lock-step with supply, maintaining average occupancy in the 97% region for the duration the forecast interval.

EFFECTIVE RENT SUMMARY

Mean Rent (Reis)	\$1,767
Annual Change	2.1%
RED 51 Rent Change Rank	43 rd
RCR YE17 Forecast	4.0%
RCR YE18 Forecast	5.0%
RCR YE19 Forecast	3.6%
RCR YE20 Forecast	2.2%
RCR YE21 Forecast	2.4%

1Q17 EFFECTIVE RENT TRENDS

As in LA and San Diego, OC effective rents recorded a rare sequential quarter setback in 1Q17 (the first in eight years), falling \$2 (-0.1%) from 4Q16. Rising concessions was the principal culprit: the average discount increased 30% from December to -\$39. Year-on-year comparisons suffered accordingly, dropping from 4.1% in the year-earlier quarter to 2.1%, the smallest annual advance in six years.

Axiometrics stabilized, same-store property surveys also identified a sequential quarter decline (-0.3%), but found stronger annual trends. The 401-property sample posted a 4.2% year-on-year increase, down from 5.1% in both the prior and year-before quarters. Class-C regained top

honors in this category, rising 5.1%, followed by classes-B (4.5%) and -A (3.5%). Elevator buildings (1.3%) were especially soft. Brea (6.9%) and Laguna Beach (6.3%) led the submarket pack, while Huntington (2.4%) and Newport Beach (2.9%) remained at the bottom of the league table.

Nonetheless, RCR's OC rent model foresees stronger growth going forward. The 97.4% ARS (S.E.=0.47%) model uses LA job (+) and US nominal GDP growth (+), and OC occupied stock growth (+) as independent variables. Each variable is projected to strengthen over the next 6 to 18 months, giving rents considerable forward impetus. The rally should run out of steam in about two years.

TRADE & RETURN SUMMARY

\$5mm+ / 80-unit+ Sales	19
Approximate Proceeds	\$445.7mm
Average Cap Rate (FNM)	4.7%
Average Price / Unit	\$246,082
Expected Total Return	7.0%
RED 49 ETR Rank	23 rd
Risk-adjusted Index	3.30
RED 49 RAI Rank	36 th

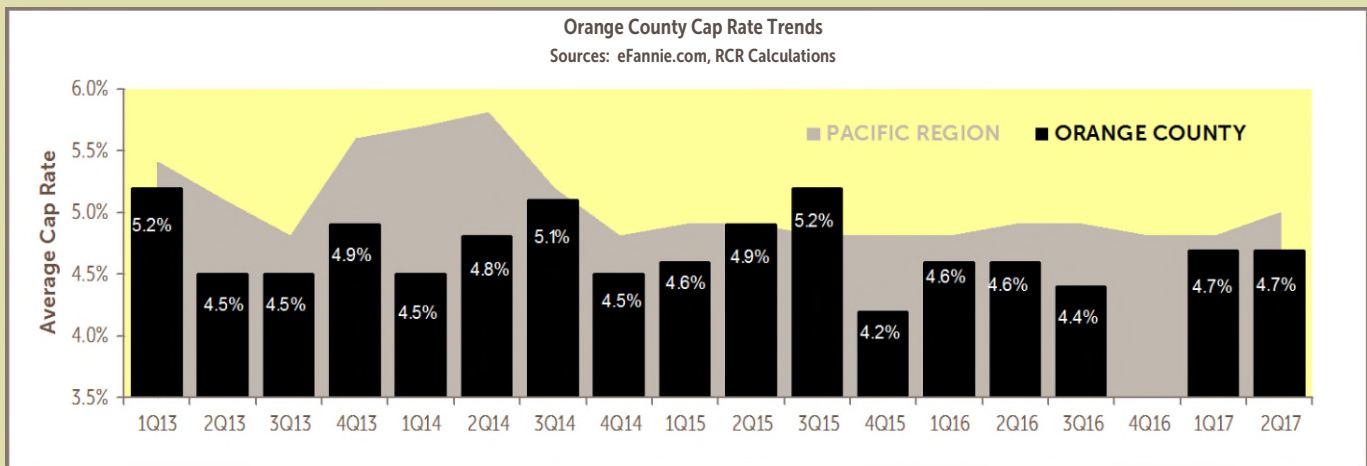
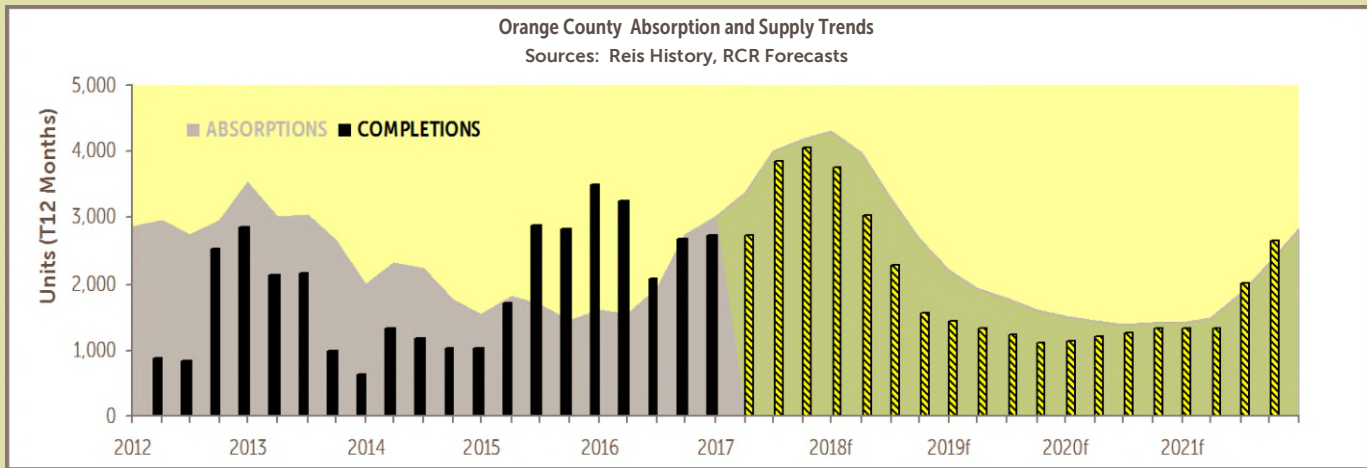
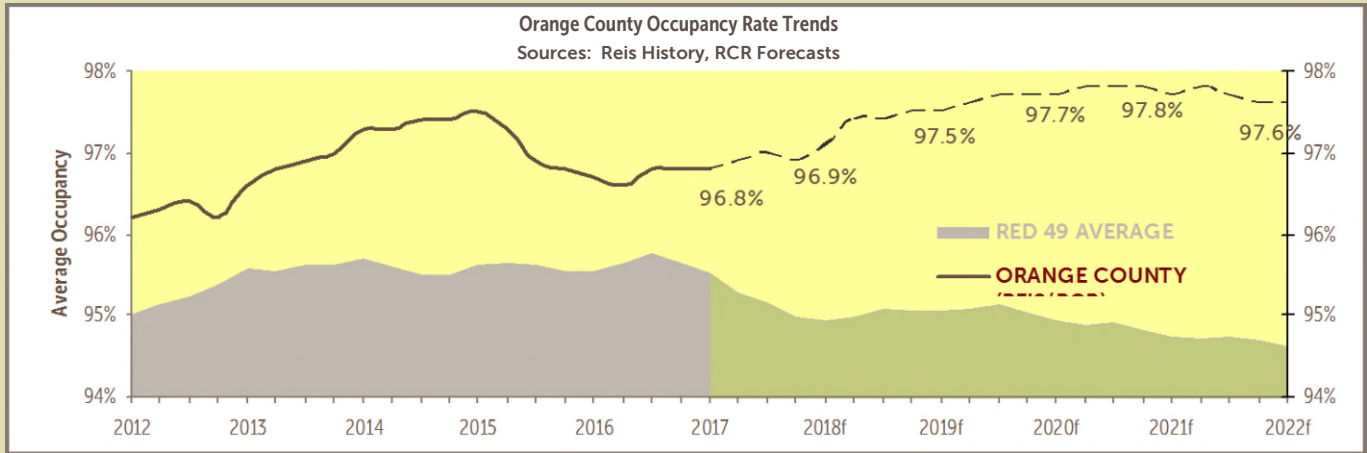
1Q17 PROPERTY MARKETS AND TOTAL RETURNS

Sales velocity gained momentum over the winter after sluggish trade in 4Q16. Investors acquired 19 Orange County properties valued at \$5 million or more during 1Q17 for total proceeds of \$445.7mm, representing 111% and 37% increases in deal count and volume, respectively. The average price of traded units declined sharply, however, falling -17% from \$297,149 in 4Q16 to \$246,082.

Second quarter transaction volume through mid-May was relatively slow. Only five exchanges were closed for proceeds totaling \$91.1mm, and these consisted entirely of older, lower value properties. The average unit price was \$198,043, which would be lowest statistic since 4Q14.

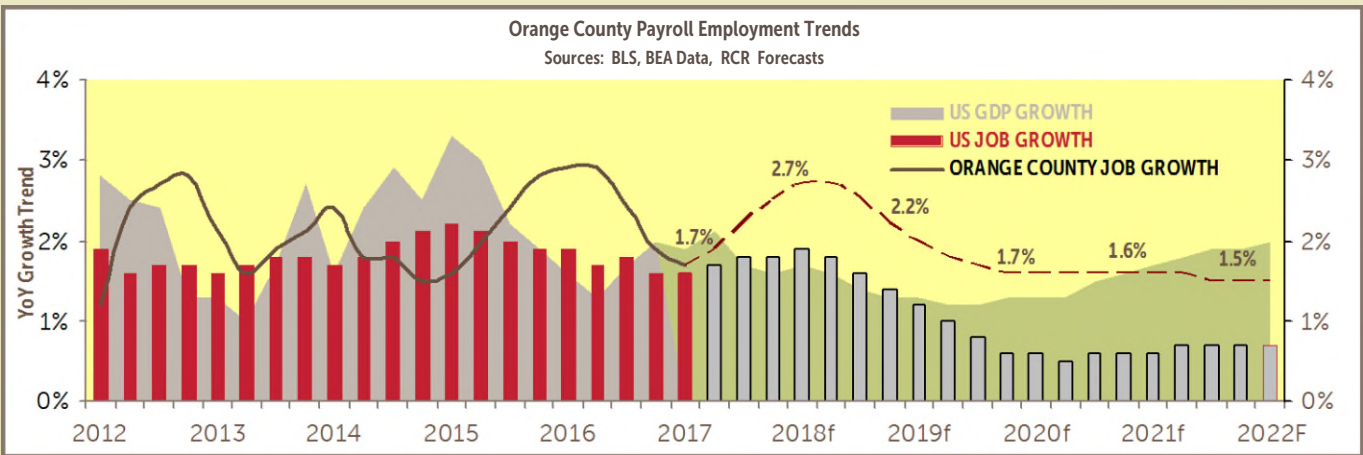
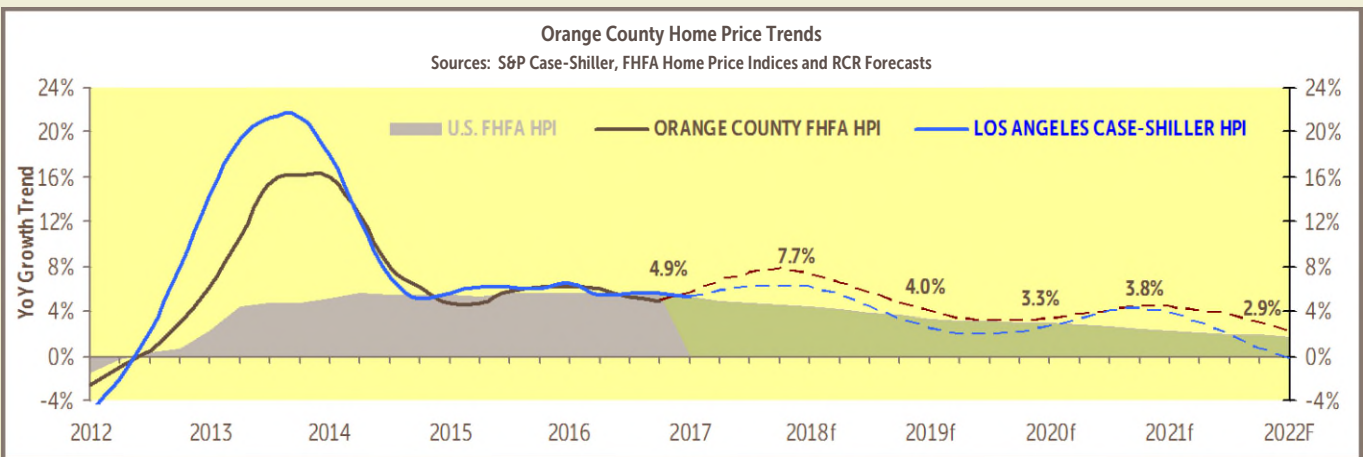
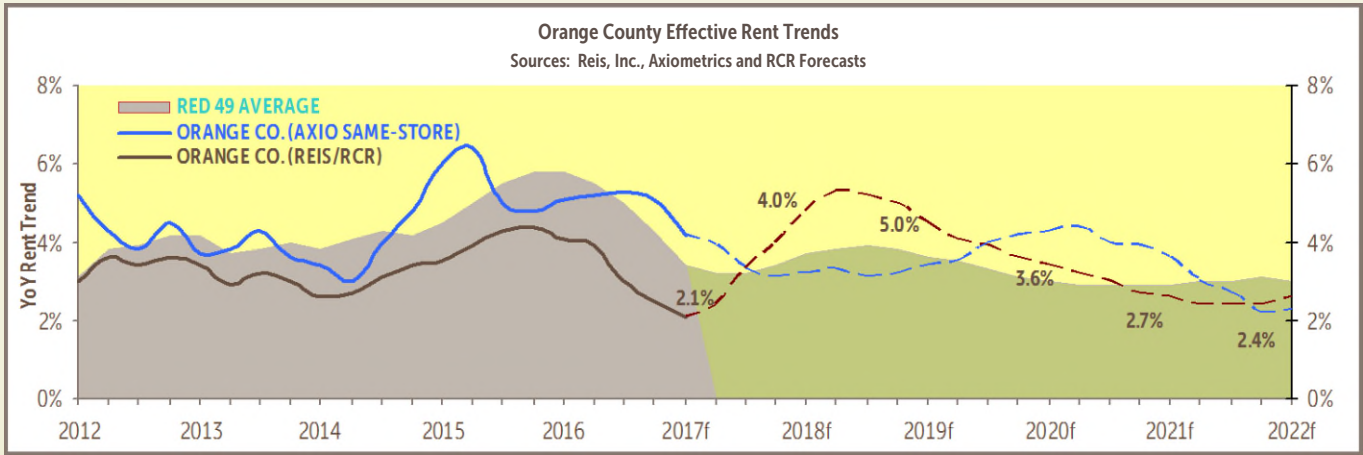
Cap rates fell in the high-3% to low-5% range with a central tendency of about 4.6%. Class-B+/A mid-rise buildings trade in the 4.2% to 4.4% area; class-B gardens about 4.6% to 4.8%; and B-/C value-adds from 5.0% to 5.4%.

RCR elected to chip 10 basis points from the purchase cap rate proxy to 4.7%. Using model derived rent and occupancy point estimates and a terminal cap rate of 5.25% we calculate that an investor would expect to earn an unlevered total return of 7.0% over a 5-year hold. This ranks 23rd among the RED 49 peers and is equal to the group average. On risk-adjusted returns, the OC ranks 36th, hampered by above average economic and rent volatility.



NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/ Type (Constr.)	Approx. Date of Transaction	Total Price (in millions)	Price / Per Unit	Estimated Cap Rate
The Galleria (Westminster / Fountain Valley)	B / GLR (1987)	19-Dec-2016	\$52.3	\$287,088	4.65%
El Paseo Apts. (Tustin / Aliso)	B+ / MB GLR (1987)	16-Jan-2017	\$43.6	\$272,500	4.98%
Malden Station Apts. (Fullerton / Downtown Fullerton)	A / WF MR (2016)	14-Feb-2017	\$77.6	\$388,158	4.4%
The Verandas (Fullerton / Fullerton Town Center)	B+ / WF GLR (1987)	30-Mar-2017	\$35.0	\$273,438	4.4%
Villas at Tustin (North Santa Ana / Portola Park)	C+ / WF GLR (1972)	4-Apr-2017	\$94.0	\$231,527	5.25%



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SUBMARKET TRENDS (REIS)

Submarket	Reis Inventory	Effective Rent			Physical Vacancy		Basis Point Change
	Percent Change	1Q16	1Q17	Change	1Q16	1Q17	
Brea	0.0%	\$1,481	\$1,539	3.9%	1.0%	0.9%	-10 bps
Buena Park	0.0%	\$1,432	\$1,490	4.0%	1.1%	1.2%	10 bps
Costa Mesa	0.8%	\$1,821	\$1,882	3.4%	2.1%	2.3%	20 bps
Fullerton	5.7%	\$1,452	\$1,551	6.8%	1.7%	4.4%	270 bps
Huntington Beach	2.6%	\$1,657	\$1,723	4.0%	6.5%	4.1%	-240 bps
Irvine	2.0%	\$2,247	\$2,307	2.7%	6.3%	4.5%	-180 bps
Laguna Beach	0.0%	\$1,860	\$1,903	2.3%	4.1%	3.1%	-100 bps
Laguna Hills	10.0%	\$1,919	\$2,000	4.2%	3.4%	7.0%	360 bps
Mission Viejo	-0.2%	\$1,780	\$1,856	4.2%	2.9%	2.1%	-80 bps
Newport Beach	0.0%	\$2,271	\$2,451	7.9%	2.8%	2.6%	-20 bps
North Anaheim	0.0%	\$1,374	\$1,400	1.9%	1.9%	2.3%	40 bps
North Santa Ana	2.0%	\$1,364	\$1,434	5.2%	1.2%	2.6%	140 bps
Orange	0.0%	\$1,710	\$1,830	7.0%	1.3%	1.8%	50 bps
Northeast Anaheim	0.0%	\$1,385	\$1,474	6.4%	3.4%	2.7%	-70 bps
South Anaheim	5.5%	\$1,515	\$1,657	9.3%	3.9%	5.0%	110 bps
South Santa Ana	0.0%	\$1,821	\$1,912	5.0%	3.8%	3.8%	0 bps
Tustin	-1.1%	\$1,599	\$1,836	14.8%	2.9%	1.7%	-120 bps
Westminster	1.4%	\$1,485	\$1,519	2.3%	1.9%	2.2%	30 bps
Metro	1.3%	\$1,730	\$1,767	2.1%	3.3%	3.2%	-10 bps

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