CHICAGO, ILLINOIS

MARKET OVERVIEW & MULTIFAMILY HOUSING UPDATE

RED Capital Group | 1Q17 | July 2017

PAYROLL JOB SUMMARY

Average Payrolls	3,667.1m
Annual Change 1Q17	27.9m (0.8%)
RCR 2017 Forecast	29.2m (0.8%)
RCR 2018 Forecast	45.1m (1.2%)
RCR 2019 Forecast	23.2m (0.6%)
RCR 2020 Forecast	9.5m (0.3%)
RCR 2021 Forecast	14.3m (0.4%)
Unemployment (NSA)	4.1% (5/17)

1Q17 PAYROLL TRENDS AND FORECAST

Chicago job creation trends continued to decelerate over the winter. Metro payrolls advanced at a 27,900-job, 0.8% year-on-year rate in 1Q17, down from a 33,100-job pace in 4Q16, and less than half of the rate recorded in 1Q16. A downturn in business service sector hiring was largely responsible, most notably in the high-compensation professional and technical service (P&TS) sub-sector. Sector growth declined from a 9,300-job, 1.3% rate as recently as 3Q16, to a 1,300-job, -0.2% loss in 1Q17. P&TS trends were worse, as headcounts fell –0.5% in 1Q17. Winter trends may have been weaker save for a 10,400-job gain in financial service employment, the best quarter in metro history.

April and May data also were soft. Annual comparisons showed an average gain of only 18,700 (0.5%) jobs, while seasonally adjusted figures recorded a net -3,000 job loss. Household survey data revealed a sharp decline in unemployment, entirely attributable to labor force attrition.

RED Research's metro payroll model is optimistic for the next 18 months. The robust 97.3% adjusted-R^2 (SE=0.29%) equation uses the rate of change of US job growth and metro personal income, US personal consumption and nominal GDP growth as independent variables. Each is expected to be constructive through 2018, propelling the rate of job creation back above 1%. But we expect economic headwinds to develop afterward, trimming annual Chicagoland payroll expansion to 0.6% or slower .

OCCUPANCY RATE SUMMARY

Occupancy Rate (Reis)	95.9%
RED 51 Rank	22nd
Annual Chg. (Reis)	-0.3%
RCR YE17 Forecast	95.3%
RCR YE18 Forecast	95.3%
RCR YE19 Forecast	95.0%
RCR YE20 Forecast	94.8%
RCR YE21 Forecast	95.1%

1Q17 ABSORPTION AND OCCUPANCY RATE TRENDS

In line with broad major metro trends, Chicago space demand softened in the first quarter following four years of strength. Tenants leased a net of 175 vacant units (Reis), down sharply from 1,678 and 1,069 in the prior and year-earlier quarters, respectively, and the fewest in a winter quarter since 2009. Supply wasn't particularly heavy (499 units), however; and occupancy decreased only -20 basis points sequentially and -10bps year-on-year to 95.9%.

Axiometrics surveys of 347 stabilized, same-store properties found weaker conditions. This sample was 93.9% and 94.5% occupied in 1Q and 2Q17, respectively. Class-A properties were instrumental to the spring rebound, as occupancy rose 180bps sequentially to 94.3%. Class-B climbed 50bps to 94.6%, while class-C occupancy declined –30bps to 94.4%. Submarkets in and around the Loop were soft, with occupancy rates ranging from 92.9% (City West) and 93.5% (Gold Coast) to 93.8% (The Loop).

Inventory growth is expected to persist at above average rates over the next two years. RCR's CHI occupied stock growth model (ARS=93.8%, SE=0.2%) projects that absorption also will be above average but not to the degree necessary to keep pace with supply. Metro occupancy is forecast to decline about -90bps by YE2019, before stabilizing in the 5-year forecast interval out-years.

EFFECTIVE RENT SUMMARY

Mean Rent (Reis)	$1,303
Annual Change	4.0%
RED 51 Rent Change Rank	18th
RCR YE17 Forecast	3.0%
RCR YE18 Forecast	3.7%
RCR YE19 Forecast	2.6%
RCR YE20 Forecast	2.3%
RCR YE21 Forecast	2.8%

1Q17 EFFECTIVE RENT TRENDS

Reis report that rent growth was steady in the first quarter, matching $8 (0.7%) sequential gains in each of the prior and year-earlier quarters. Likewise, annual trends were steady on 4.0%, representing the sixth consecutive quarter of 4% or faster year-on-year growth. Class-A was the principal catalyst, posting a $23 (1.3%) sequential advance.

The Axiometrics same-store sample recorded weaker results. Average annual growth rates among these assets were 2.2% in 1Q17, and 2.0% in 2Q17. Class-A properties were the ballast in this case, managing only a 0.3% y-o-y increase during the spring quarter, in spite of a brisk recovery from the 4Q16 trough. Class-B (2.4%) posted the fastest growth, followed by class-C (2.0%). Suburban and peripheral urban submarkets were better performers, while infill areas lagged; especially Belmont (-2.3%), Gold Coast (-1.5%) and The Loop (0.1%). Lincoln (2.4%) and Rogers (4.2%) Parks and City West (1.4%)) were stronger.

RCR's rent model (ARS=93.2%, SE=0.5%) implies that metro job growth and occupancy changes are the primary influencers of rent trend shifts. As noted above, both independent variables are expected to be relatively neutral factors over the forecast interval. Thus, the rent projection also is a bit lackluster, with rents advancing at a 2.9% compound annual rate, ranking 23rd among the R49.

TRADE & RETURN SUMMARY

$5mm+/80-unit+ Sales	16
Estimated Proceeds	$755mm
Average Cap Rate (FNM)	5.9%
Average Price / Unit	$159,684
Expected Total Return	6.8%
RED 49 ETR Rank	29th
Risk-adjusted Index	5.72
RED 49 RAI Rank	4th

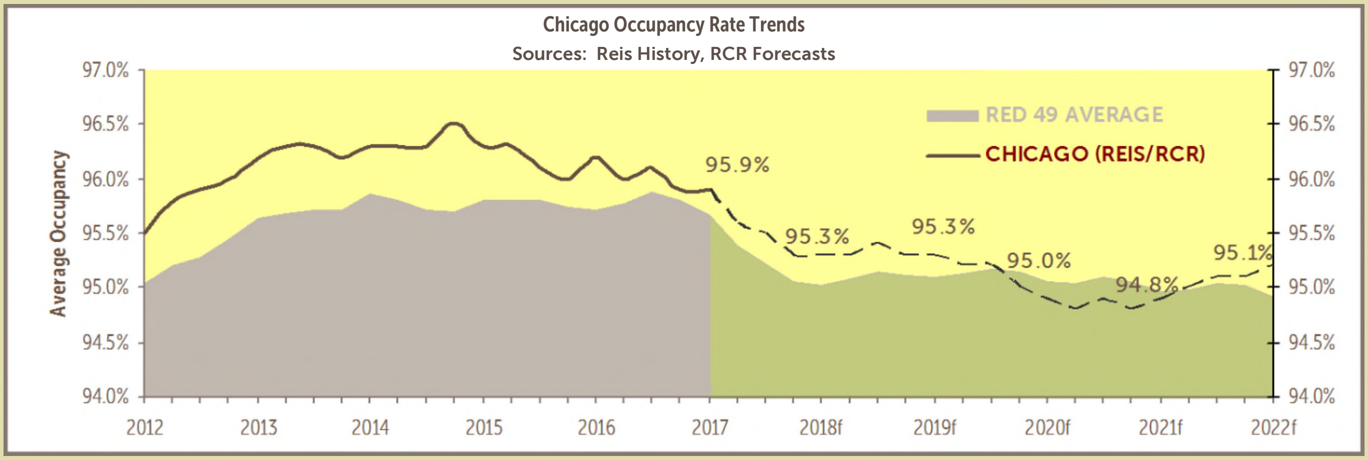
1Q17 PROPERTY MARKETS AND TOTAL RETURNS

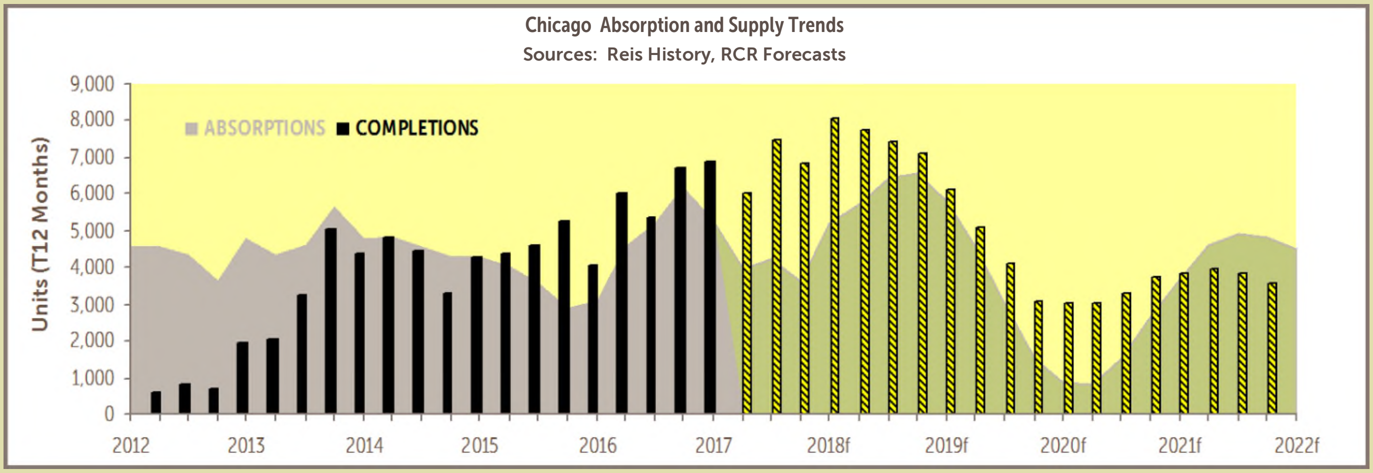
Sales of apartment assets of 80 units or more declined in the first quarter but regained momentum in the spring. CoStar recorded 16 large property sales during 1Q17, down from 38 and 28 during the prior and year-earlier quarters, respectively. Sales volume declined from about $1.6 billion in 4Q16 and $928mm in 1Q16 (RCA) to approximately $755mm. The average price of traded units was $159,684, up 2% sequentially but off –10% year-on-year.

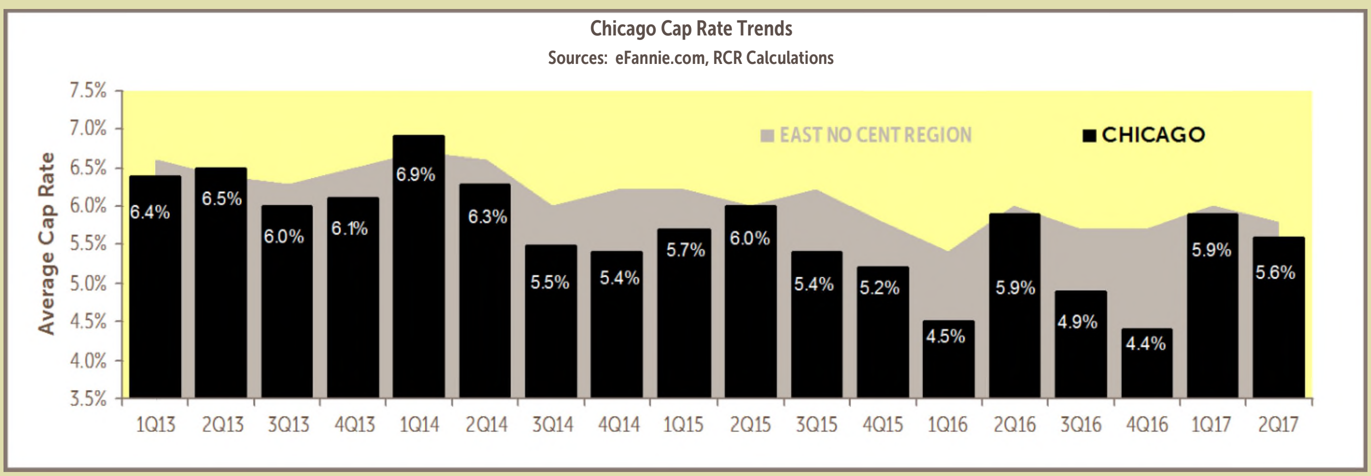
Velocity picked up in the spring. Investors acquired 28 properties, up 56% y-o-y. Estimated proceeds approached $900mm, about 5% above the year-earlier quarter. Buyers moved down the credit spectrum, focusing on value-adds.

Cap rates applied to infill trophies ranged from 4.5% to 5%, with the trend moving toward the high-end. Class-B/B+ gardens gravitated to the 5% to 5.9% region, while older properties and value-adds traded from 5.5% to 6.25%.

RCR elected to raise the purchase cap rate proxy for the second consecutive quarter, this time 0.05% to 5.3% Using this level, a terminal cap rate of 5.9%, and model derived occupancy and rent point estimates, we calculate that an investor acquiring a property in 1Q17 would expect to earn a 6.8% unlevered total return over a 5-year hold. This metric ranks 29th among the RED 49. Extra low rent volatility boosts risk-adjusted returns: Chicago ranks 4th highest.

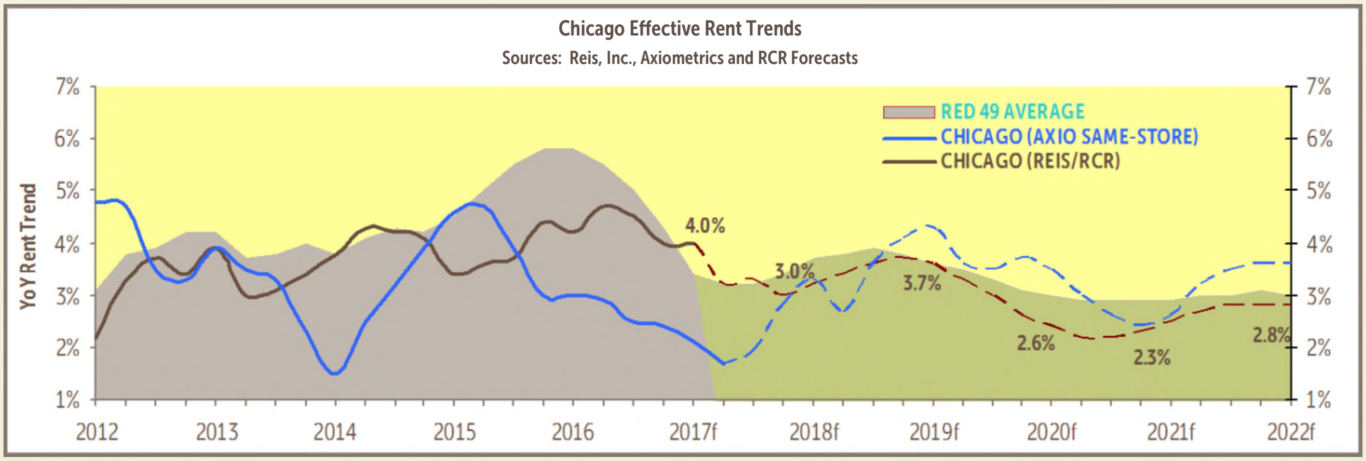


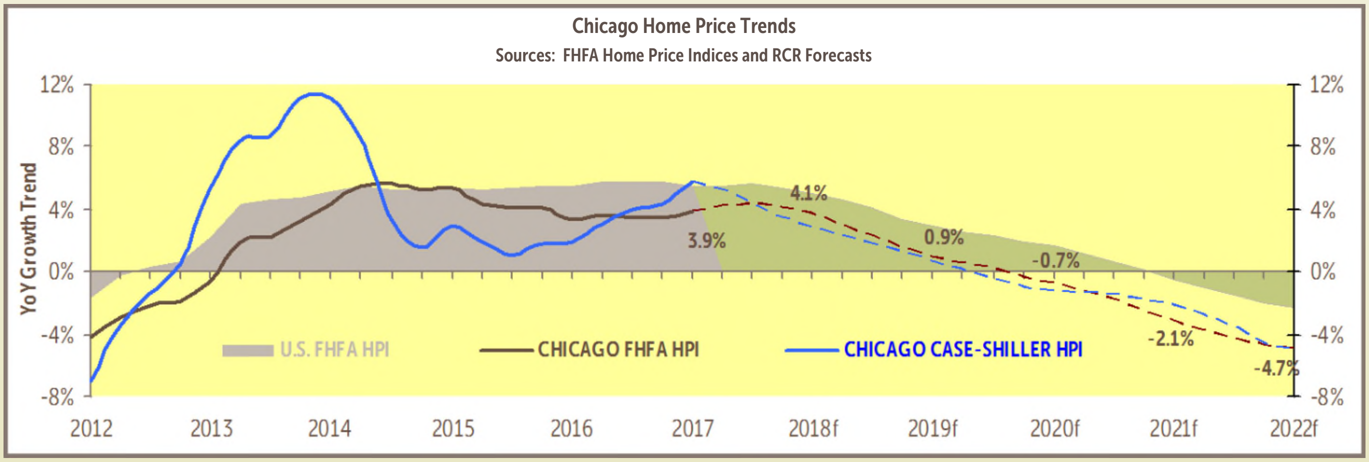


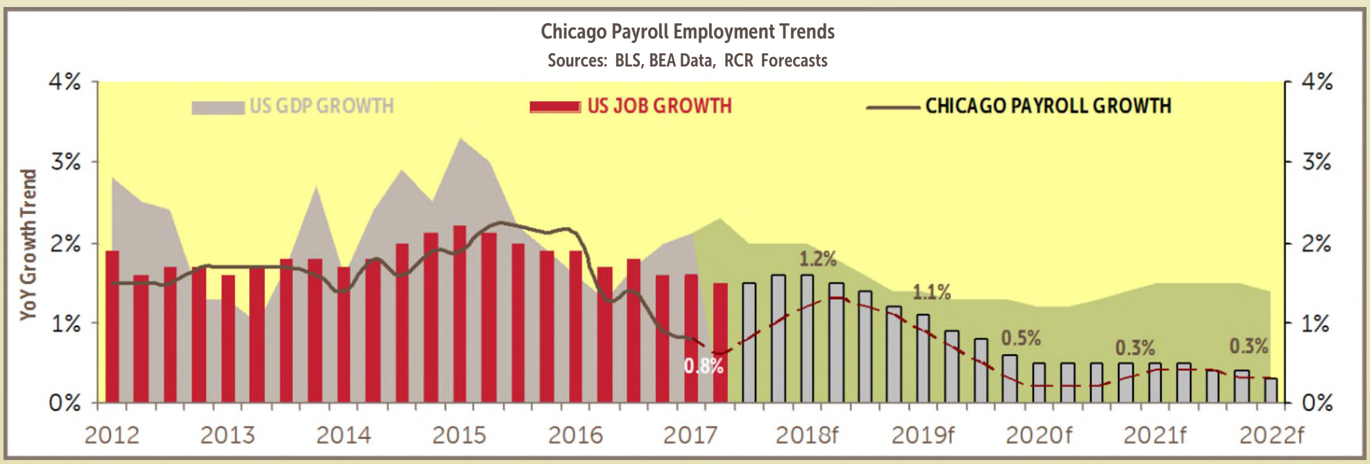


NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/ Type (Constr.)	Approx. Date of Transaction	Total Price (in millions)	Price / Per Unit	Estimated Cap Rate
Madison at Racine (City West / Fulton Market)	A- / MB MR (2014)	16-Mar-2017	$99.6	$461,111	4.7%
Camden at Bloomingdale (Schaumburg / Bloomingdale)	B / WF GLR (1991)	23-Mar-2017	$59.5	$165,278	5.9%
Commons at Town Center (East Lake Co. / Vernon Hills)	B+ / MB MR (2010)	8-May-2017	$23.0	$270,588	5.9%
100 West Chestnut (Gold Coast / Near North / LaSalle)	B+ / MB HR (1986)	16-Jun-2017	$100.0	$357,143	4.5%
Coast at Lakeshore (Gold Coast / New East Side)	A+ / SR HR (2013)	7-Jul-2017	$222.5	$432,039	5.0%


Chicago Effective Rent Trends
Sources: Reis, Inc., Axiometrics and RCR Forecasts
RED 49 AVERAGE
CHICAGO (AXIO SAME-STORE)
CHICAGO (REIS/RCR)
YoY Rent Trend
4.0%
3.0%
3.7%
2.6%
2.3%
2.8%
2012 2013 2014 2015 2016 2017f 2018f 2019f 2020f 2021f 2022f


Chicago Home Price Trends
Sources: FHFA Home Price Indices and RCR Forecasts
YoY Growth Trend
U.S. FHFA HPI
CHICAGO FHFA HPI
CHICAGO CASE-SHILLER HPI
4.1%
3.9%
0.9%
-0.7%
-2.1%
-4.7%
2012 2013 2014 2015 2016 2017 2018f 2019f 2020f 2021f 2022f


Chicago Payroll Employment Trends
Sources: BLS, BEA Data, RCR Forecasts
YoY Growth Trend
US GDP GROWTH
US JOB GROWTH
CHICAGO PAYROLL GROWTH
1.2%
1.1%
0.8%
0.5%
0.3%
0.3%
2012 2013 2014 2015 2016 2017 2018f 2019f 2020f 2021f 2022f

SUBMARKET TRENDS (AXIOMETRICS)

Submarket	Surveyed Properties	Year-on-year Same-Store Effective Rent Growth 1Q16	1Q17	2Q17	Physical Occupancy 2Q16	2Q17	Basis Point Change
Aurora / Naperville	29	5.3%	4.0%	2.4%	95.1%	94.8%	-32 bps
Belmont to Montrose	5	4.2%	6.1%	-2.3%	96.0%	93.1%	-284 bps
City West	21	0.4%	1.5%	1.4%	95.0%	92.9%	-211 bps
Downers Grove	12	-0.6%	-1.0%	2.3%	96.8%	95.3%	-150 bps
East Lake County	26	2.2%	1.7%	2.1%	95.9%	95.7%	-20 bps
Glen Ellyn / Wheaton	16	1.7%	1.6%	2.2%	95.9%	95.3%	-52 bps
Glendale Heights / Lombard	21	1.2%	3.0%	2.1%	96.1%	94.5%	-168 bps
Glenview/Evanston	13	5.3%	1.8%	0.2%	96.3%	95.2%	-108 bps
Gold Coast / River North	41	0.3%	0.5%	-1.5%	94.6%	93.5%	-115 bps
Joliet	9	2.1%	9.4%	3.8%	94.8%	94.9%	17 bps
Kenosha County	7	4.2%	4.2%	4.5%	98.7%	97.3%	-142 bps
Lincoln Park / Old Town	8	5.8%	1.9%	2.4%	96.6%	95.9%	-75 bps
McHenry County	6	-1.6%	-0.5%	4.3%	94.6%	94.3%	-33 bps
Oak Park	7	2.3%	2.3%	7.7%	95.7%	95.4%	-29 bps
O'Hare	12	1.1%	2.9%	1.5%	93.4%	96.1%	268 bps
Palatine	14	3.0%	3.9%	1.6%	95.0%	93.8%	-129 bps
Rogers Park / Uptown	10	7.6%	5.9%	4.2%	96.7%	96.7%	8 bps
Schaumburg / Hoffman	19	1.7%	1.3%	1.0%	94.3%	94.2%	-11 bps
South Shore	13	1.6%	2.5%	3.1%	95.3%	93.9%	-134 bps
Southeast Cook County	5	-2.0%	1.0%	0.1%	94.3%	88.1%	-618 bps
Southwest Cook County	17	4.6%	-1.1%	2.9%	96.2%	94.9%	-127 bps
The Loop	19	0.2%	-0.4%	0.1%	95.6%	93.8%	-179 bps
West Lake County	6	0.7%	4.8%	0.6%	95.5%	97.3%	178 bps
Wheeling	17	5.0%	2.4%	3.7%	95.2%	95.6%	42 bps
Woodridge / Lisle	14	3.4%	1.1%	1.6%	94.2%	94.1%	-4 bps

FOR MORE INFORMATION ABOUT RED'S RESEARCH CAPABILITIES CONTACT:

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