PAYROLL JOB SUMMARY

Average Payrolls	1,972.0m
Annual Change 1Q17	37.2m (1.9%)
RCR 2017 Forecast	34.9m (1.8%)
RCR 2018 Forecast	22.5m (1.1%)
RCR 2019 Forecast	1.8m (0.1%)
RCR 2020 Forecast	-5.0m (-0.2%)
RCR 2021 Forecast	-3.0m (-0.1%)
Unemployment (NSA)	3.6% (5/17)

OCCUPANCY RATE SUMMARY

Occupancy Rate (Reis)	97.6%
RED 51 Rank	2nd
Annual Chg. (Reis)	-0.1%
RCR YE17 Forecast	97.6%
RCR YE18 Forecast	98.4%
RCR YE19 Forecast	98.7%
RCR YE20 Forecast	98.3%
RCR YE21 Forecast	98.3%

EFFECTIVE RENT SUMMARY

Mean Rent (Reis)	$914
Annual Change	3.2%
RED 51 Rent Change Rank	31th
RCR YE17 Forecast	1.8%
RCR YE18 Forecast	2.8%
RCR YE19 Forecast	1.4%
RCR YE20 Forecast	1.5%
RCR YE21 Forecast	1.3%

TRADE & RETURN SUMMARY

$2mm+/80+ unit Sales	15
Estimated Proceeds	$240mm
Average Cap Rate (FNM)	5.9%
Average Price / Unit	$89,697
Expected Total Return	6.6%
RED 49 ETR Rank	33rd
Risk-adjusted Index	3.54
RED 49 RAI Rank	28th

1Q17 PAYROLL TRENDS AND FORECAST

Detroit employment trends were strong and steady during the first quarter as establishments added to payrolls at a 37,200-job, 1.9% year-on-year rate, representing the eleventh consecutive quarter in which annual growth came in between 1.8% and 2.2%. This impressive run was anchored by consistent expansion in manufacturing. The super-sector recorded annual growth in 28 straight quarters, a period in which industrial headcounts increased by 59,100 positions, inclusive of a 4,300-job, 1.8% advance over the year ended in March. Skilled service employment growth also was robust as financial, professional, technical and healthcare employment increased at a 13,800 (2.4%) job pace. Weakness only was evident in recent consumer driven sectors as retail and personal service payrolls declined.

Seasonally-adjusted payroll and household survey data also were constructive. The former reported solid 2017 year-to-date gains, and the latter showed sharp declines in unemployment, irrespective of material labor force growth.

RED Research specified a 97.6% adjusted-R^2 payroll forecasting equation using only data collected since 2000 to better reflect structural improvement in Detroit's economy. This model projects further healthy job creation trends through 2018, as the two positive coefficient variables (personal income and industrial production) are projected to evolve in beneficial ways. But the model remains somewhat negatively biased; so, as US growth is expected to slow late in the decade, the impact on Detroit is magnified.

1Q17 ABSORPTION AND OCCUPANCY RATE TRENDS

Apartment demand took a downward turn in the first quarter. Tenants vacated a net of −175 occupied units (Reis), a significant departure from a 151-unit gain in 4Q16, and absorption of 449 units in 1Q16. The occupied stock decline was the first in more than 7 years. Move-outs were concentrated in Farmington Hills submarket, suggesting a possible shift toward homeownership among higher income renters. Still, occupancy declined only −10 basis points sequentially and year-on-year to 97.6%. Preliminary data suggest 2Q17 occupancy was unchanged on 97.6%.

Axiometrics stabilized, same-store data reveals higher vacancy among professionally-managed assets. Occupancy rates in this sample were 95.0% and 95.9% in 1Q and 2Q17, respectively. A's (96.0%) were the class leader, topping classes-B (95.6%) and -C (95.3%). Novi (97.7%) and Livonia (97.4%) led among submarkets, while only Downtown (94.4%) and Southfield (94.3%) fell below 95%.

Detroit is one of the few major US markets not facing a daunting occupancy surge in 2017-18. Annual inventory growth is excepted to advance only from 0.7% in 2016 to 0.8% in 2017. Our demand model suggests that absorption is likely to outpace supply for the next three years, further tightening the market. Occupancy is likely to weaken after 2018, however, as economic conditions soften.

1Q17 EFFECTIVE RENT TRENDS

Soft space demand begat slower rent trends during the seasonally weaker winter quarter. Average effective fell $1 (-0.1%) sequentially to $914 (Reis), the first decline in three years. Annual growth slowed to 3.2% from 4.9% in 4Q16, the largest quarterly deceleration since 1Q03. A rare setback (-1.0%) in the Ann Arbor submarket was largely responsible. Preliminary data suggest Detroit bounced back in the spring as mean asking rent increased $9 (1.0%).

The Axiometrics same-store sample also posted faster second quarter growth. Rents increased 3.9% year-on-year in 1Q17, and 4.1% in 2Q. The service recorded positive sequential growth (2.8%) in 2Q, materially better than the −1.0% and 0.0% 2Q16, and 1Q17 results. Class-A (6.1%) was the class of the field in 2Q, followed by B (3.8%) and C (2.3%). Southfield (4.2%) and Pontiac (2.3%) led among submarkets; Downtown (0.1%) and Troy (-0.4%) trailed.

RCR's DET rent model (91.6% ARS, 0.6% SE) anticipates constructive but slower growth through 2019, but materially softer conditions in the out-years. We found only two independent, statistically significant predictors of future rents: job and personal income growth. As our respective models are cautious on both, especially later in the decade, so, too, is our rent forecast: rents are projected to rise at a 1.8% compound annual rate through 1Q22: R49 #48.

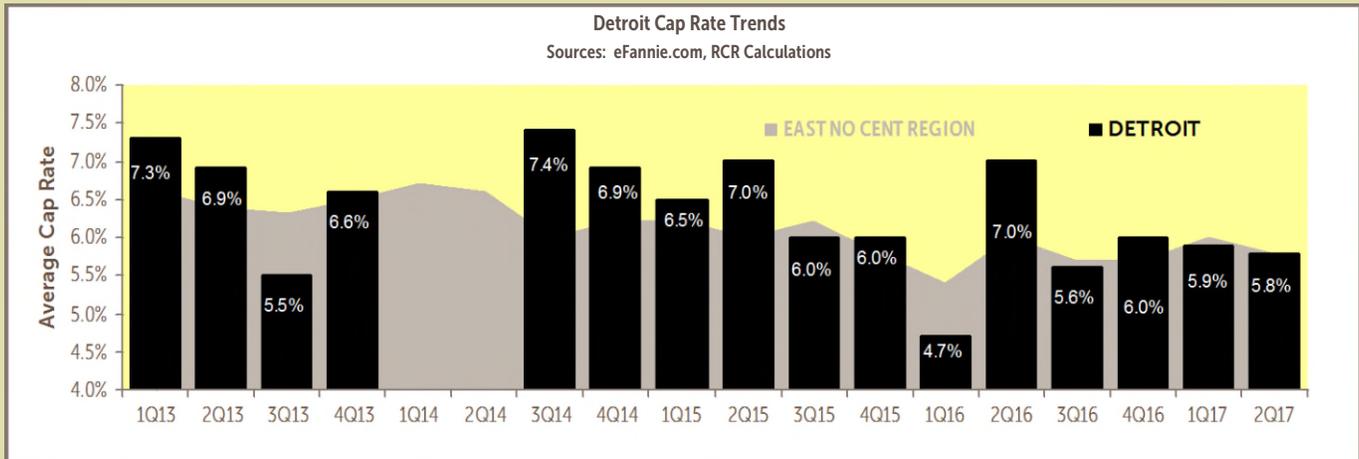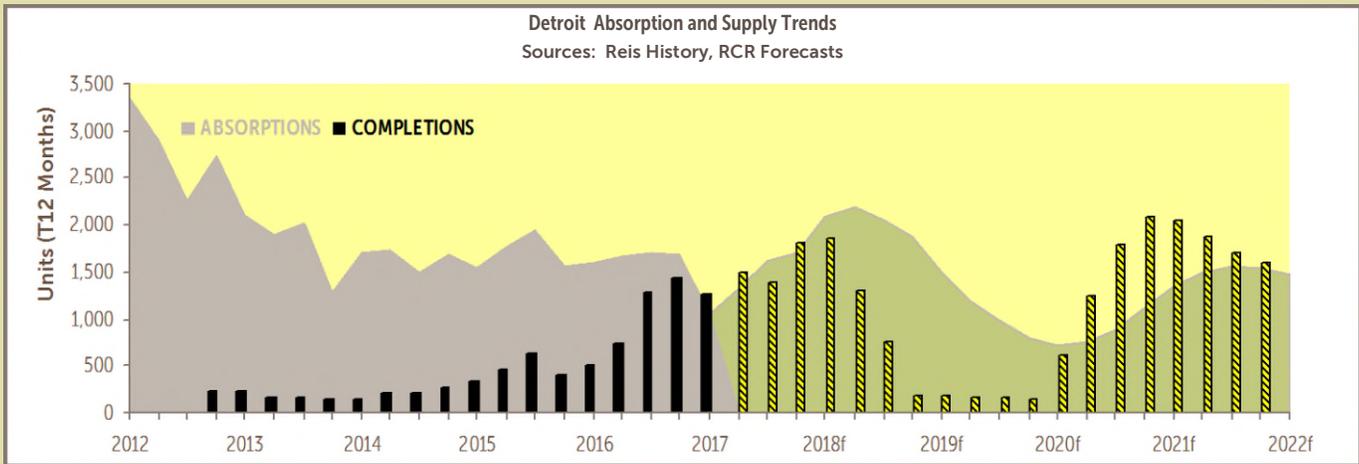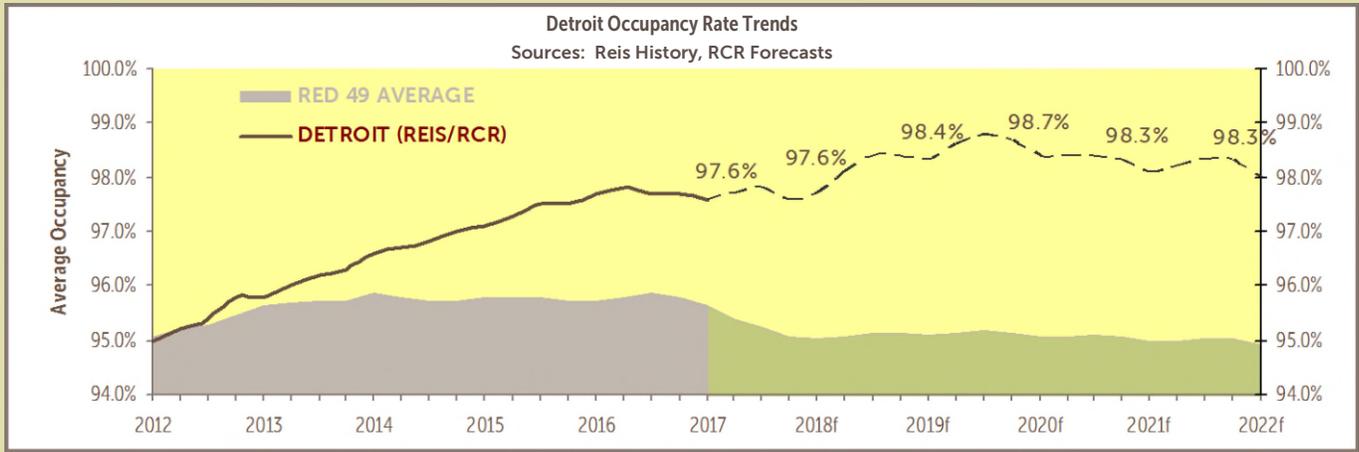## 1Q17 PROPERTY MARKETS AND TOTAL RETURNS

Investor continued to maintain a healthy appetite for Detroit properties in the first half 2017. A total of 21 exchanges were closed (CoStar) for estimated total proceeds of $325 million. The average price per unit of trades for which pricing data were available was $85,205.

Private investors maintained the largest market share (74% of proceeds) but institutional investors were more active than in the past. Institutional participation accounted for the remaining 26% of 2017 year-to-date purchases, well above their 11% historical average.

Cap rates applicable to investment quality assets fell mostly in the 6%-7% range. Ann Arbor properties traded at the low-end of the range; suburban Detroit properties gravitate toward the 6.25% to 6.75% area. Class-C and value-add situations may trade to 7% or higher yields.
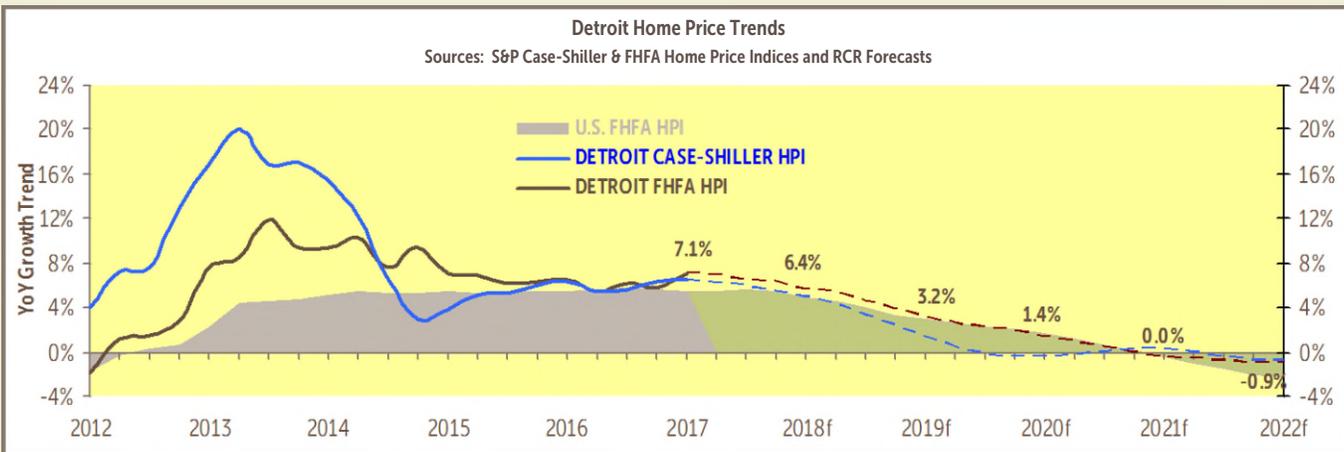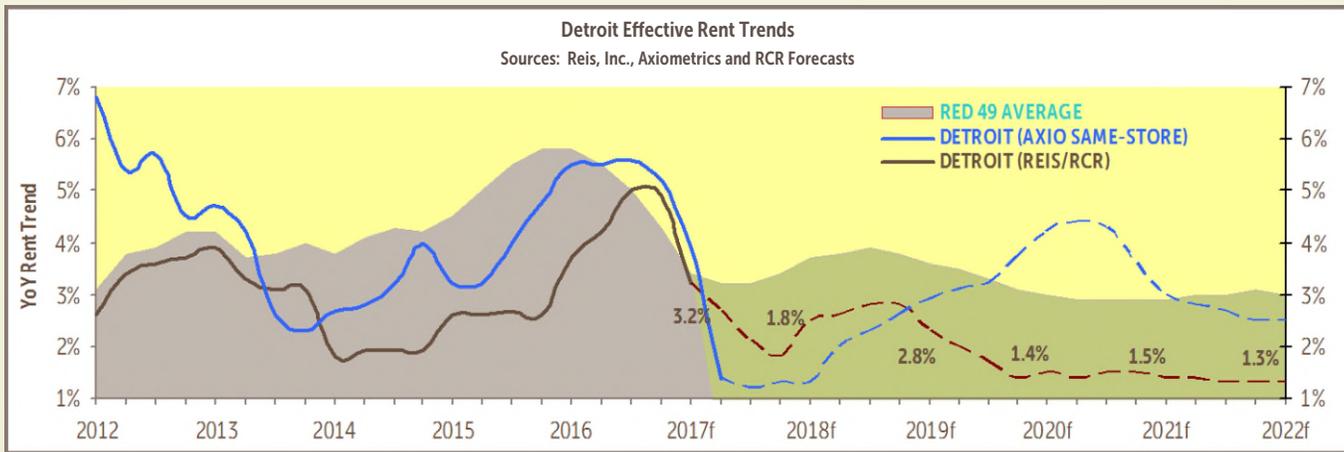
Using a 6.2% class-B/B+ purchase cap rate proxy, a 6.8% terminal cap rate assumption and model derived rent and occupancy point estimates, RED Research estimates that a 1Q17 purchaser of a Detroit property would expect to achieve a 6.8% unlevered total return on a 5-year hold. This ranks #29 among the RED 49 large metro peer group. High rent and demand model standard error hinder risk–adjusted returns. Detroit ranks 28th, low for the Midwest.

Detroit Occupancy Rate Trends
Sources: Reis History, RCR Forecasts

Detroit Absorption and Supply Trends
Sources: Reis History, RCR Forecasts

Detroit Cap Rate Trends
Sources: eFannie.com, RCR Calculations

NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/ Type (Constr.)	Approx. Date of Transaction	Total Price (in millions)	Price / Per Unit	Estimated Cap Rate
Chimney Hill (Farmington Hills / West Bloomfield)	A- / GLR (1986)	13-Jan-2017	$52.1	$158,841	6.1% (RCA)
Waterford West Apts. (Pontiac / Waterford)	B+ / GLR (1997)	17-Feb-2017	$16.4 (appraisal)	$95,349	6.44%(UW)
Haven of Ann Arbor (Ann Arbor / King)	B / GLR (1990)	23-Mar-2017	$71.4	$137,308	6.1%
Harbor House (Ann Arbor / So. Campus / Ward Park)	B+ / SF GLR (1992)	5-Apr-2017	$28.2	$135,577	6.3%
Autumn Ridge Village (Macomb Co. / Sterling Heights)	C Sr. Aff./RC MR (1983)	26-May-2017	$10.2	$40,615	6.38% (UW)

Detroit Effective Rent Trends
Sources: Reis, Inc., Axiometrics and RCR Forecasts

RED 49 AVERAGE
DETROIT (AXIO SAME-STORE)
DETROIT (REIS/RCR)

YoY Rent Trend

3.2% 1.8% 2.8% 1.4% 1.5% 1.3%

Detroit Home Price Trends
Sources: S&P Case-Shiller & FHFA Home Price Indices and RCR Forecasts

U.S. FHFA HPI
DETROIT CASE-SHILLER HPI
DETROIT FHFA HPI

YoY Growth Trend

7.1% 6.4% 3.2% 1.4% 0.0% -0.9%

Detroit Payroll Employment Trends
Sources: BLS, BEA Data, RCR Forecasts

US GDP GROWTH   US JOB GROWTH   DETROIT PAYROLL GROWTH

YoY Growth Trend

1.9% 1.5% 0.7% -0.2% -0.2% -0.2%

SUBMARKET TRENDS (REIS)

Submarket	Reis Inventory Percent Change	Effective Rent			Physical Vacancy		
		4Q16	1Q17	Change	4Q16	1Q17	Basis Point Change
Ann Arbor	2.0%	$1,080	$1,070	-1.0%	1.8%	1.8%	0 bps
Dearborn/Dearborn Heights	0.0%	$814	$830	2.0%	2.3%	2.2%	-10 bps
Downriver / South Wayne	0.0%	$782	$790	1.1%	1.1%	1.4%	30 bps
Downtown	0.3%	$1,073	$1,078	0.4%	2.5%	2.9%	40 bps
Farmington Hills	0.0%	$1,040	$1,040	0.1%	3.5%	3.0%	-50 bps
Macomb County	0.3%	$804	$803	-0.1%	1.6%	1.8%	20 bps
Midtown / West Detroit	3.0%	$648	$644	-0.6%	5.2%	5.2%	0 bps
Novi / Livonia	0.0%	$966	$966	0.0%	3.9%	4.0%	10 bps
Oak Park / Royal Oak	0.6%	$767	$774	0.9%	1.3%	1.3%	0 bps
Pontiac / Waterford	0.2%	$925	$932	0.8%	2.7%	2.8%	10 bps
Southfield	0.8%	$993	$995	0.2%	2.3%	2.9%	60 bps
Troy	-0.7%	$1,151	$1,163	1.0%	1.6%	1.5%	-10 bps
Westland	0.3%	$802	$802	0.0%	1.4%	1.4%	0 bps
Metro	0.6%	$915	$914	-0.1%	2.3%	2.4%	10 bps
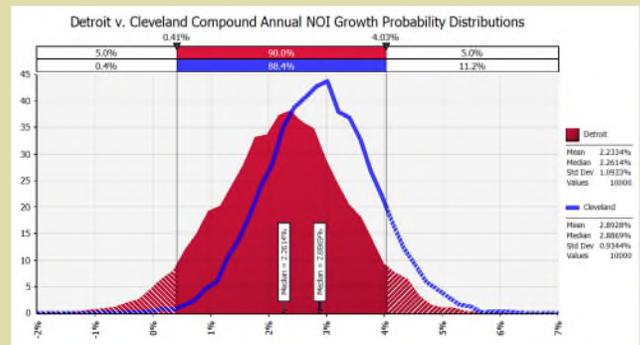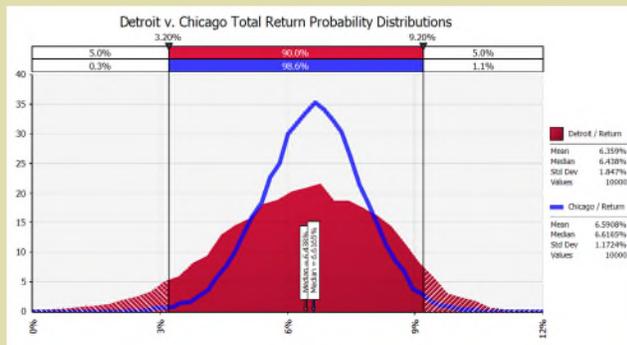
FOR MORE INFORMATION ABOUT RED'S RESEARCH CAPABILITIES CONTACT:

Daniel J. Hogan
Director of Research
djhogan@redcapitalgroup.com
+1.614.857.1416 office
+1.800.837.5100 toll free

THE FACE OF LENDING