AUSTIN, TEXAS

MARKET OVERVIEW & MULTIFAMILY HOUSING UPDATE

RED Capital Group | 1Q17 | June 2017

PAYROLL JOB SUMMARY

Average Payrolls	1,013.8m
Annual Change 1Q17	31.1m (3.2%)
RCR 2017 Forecast	30.7m (3.1%)
RCR 2018 Forecast	33.6m (3.3%)
RCR 2019 Forecast	27.0m (2.5%)
RCR 2020 Forecast	21.8m (2.0%)
RCR 2021 Forecast	23.0m (2.1%)
Unemployment (NSA)	3.2% (5/17)

1Q17 PAYROLL TRENDS AND FORECAST

Austin employment trends were steady in the first quarter as establishment payrolls increased at a 31,100-job, 3.2% year-on-year pace, nearly replicating 4Q16's 33,500-job, 3.4% performance. Service industry growth was off moderately, but goods producing sectors took up the slack. Austin's foundation high tech sector exhibited weaker trends, however, suggesting that the primary driver of the metro's recent hyper-growth may prove less potent going forward. Specifically, growth in the information sector — incorporating telecommunications, software publishing and internet services—declined from a brisk 5.4% annual rate in mid-2016 to a sluggish 1.1% rate in 1Q17, and a –2.1% retreat in April and May. Likewise, professional and technical service growth was halved in the same period.

The seasonally-adjusted series also offered hints that slower growth may be forthcoming. Austin created a net of only 4,600 jobs in 1Q17, the weakest quarter in six years, and 800 jobs in April and May, down from 5,200 in 2016.

RED Research's historically specified econometric payroll model doesn't buy the decline argument. The 96.3% adjusted-R^2 (SE=0.5%) equation uses the rate of change of US job growth, nominal GDP and personal consumption expenditure growth and annual S&P 500 returns as predictors. The model expects Austin to draft on moderate acceleration of US employment growth, and continued above trend equity returns and NGDP advances to maintain a 3% or faster head of steam through 2018; modestly weaker gains will follow.

OCCUPANCY RATE SUMMARY

Occupancy Rate (Reis)	93.6%
RED 51 Rank	49th
Annual Chg. (Reis)	-0.8%
RCR YE17 Forecast	93.5%
RCR YE18 Forecast	94.3%
RCR YE19 Forecast	94.1%
RCR YE20 Forecast	93.6%
RCR YE21 Forecast	93.3%

1Q17 ABSORPTION AND OCCUPANCY RATE TRENDS

Austin rental space demand took a downward turn at an inopportune time. Tenants net leased 479 units during 1Q17 (Reis), the fewest in any winter quarter since 2006. At the same time, developers continued to deliver new product at an accelerated pace; 1,589 units in this case. Occupancy plunged –50 basis points sequentially and -80bps year-on-year to 93.6%, lowest in six years. Submarkets proximate to the CBD were most affected, especially Near North Central, where occupancy declined -440bps y-o-y.

Surveys of 507 stabilized same-store properties conducted by Axiometrics were comparable, posting 93.6% and 93.9% rates during 1Q17 and May, respectively, up 30bps y-o-y in each case. Classes-A (93.8%) and –C (94.1%) posted higher occupancy than class-B (93.4%). San Marcos (96.0%) was the only submarket above 94.3%. Six areas posted sub-94% levels, with East (92.7%) and Southeast (91.7%) lagging. Close-in neighborhoods gravitated toward 94%.

Supply will remain a challenge as inventory is expected to increase 5.2% over the next six quarters. RCR's demand model (independent variables = the rates of change of supply and job growth and lagged occupancy and rent growth) suggests demand will improve and nearly keep pace, maintaining metro occupancy above the 93% threshold for the duration of the five-year forecast interval.

EFFECTIVE RENT SUMMARY

Mean Rent (Reis)	$1,034
Annual Change	2.3%
RED 51 Rent Change Rank	41st
RCR YE17 Forecast	2.0%
RCR YE18 Forecast	2.5%
RCR YE19 Forecast	3.5%
RCR YE20 Forecast	3.0%
RCR YE21 Forecast	2.6%

1Q17 EFFECTIVE RENT TRENDS

Austin suffered a sharp $10 (-0.9%) sequential quarter setback in 4Q16 (Reis), the first decline in seven years. But owners retraced $5 (0.5%) of the loss in 1Q17, with constructive gains posted across all metro submarkets save the neighborhoods immediately south and northwest of the Capitol. Progress was entirely attributable to the class -A segment, which recorded a 0.9% sequential asking rent advance, while class-B&C rents declined another -0.2%. Rents rose 2.3% year-on-year, down –10bps from 4Q16.

The Axiometrics same-store sample recorded slower 1.3% y-o-y growth in 1Q17, and a -0.3% backward step in May. Class-A rents fell –0.3% in 1Q, incorporating a –1.7% decline in the elevator building subset. Classes-B (1.7%) and –C (1.2%) notched small gains, but each class was down y-o-y in May. High rent Central (-1.5%) and Near South Central (-2.1%) submarkets posted weakest results, while peripheral San Marcos (3.4%) and West (4.9%) led the pack.

RCR's 96.4% ARS (SE=0.8%) rent model suggests that slower than normal growth is likely to persist. Data analysis indicates that economic (+) and inventory (-) growth are the principal factors influencing changes in rent trends. Job growth is not projected to be strong enough to lift rent growth above the 4.2% long-term metro average and supply is likely to remain a rent impediment.

TRADE & RETURN SUMMARY

$5mm+ / 80-unit+ Sales	17
Estimated Proceeds	$550m
Average Cap Rate (FNM)	5.1%
Average Price / Unit	$138,435
Expected Total Return	7.0%
RED 49 ETR Rank	23rd
Risk-adjusted Index	2.51
RED 49 RAI Rank	43rd

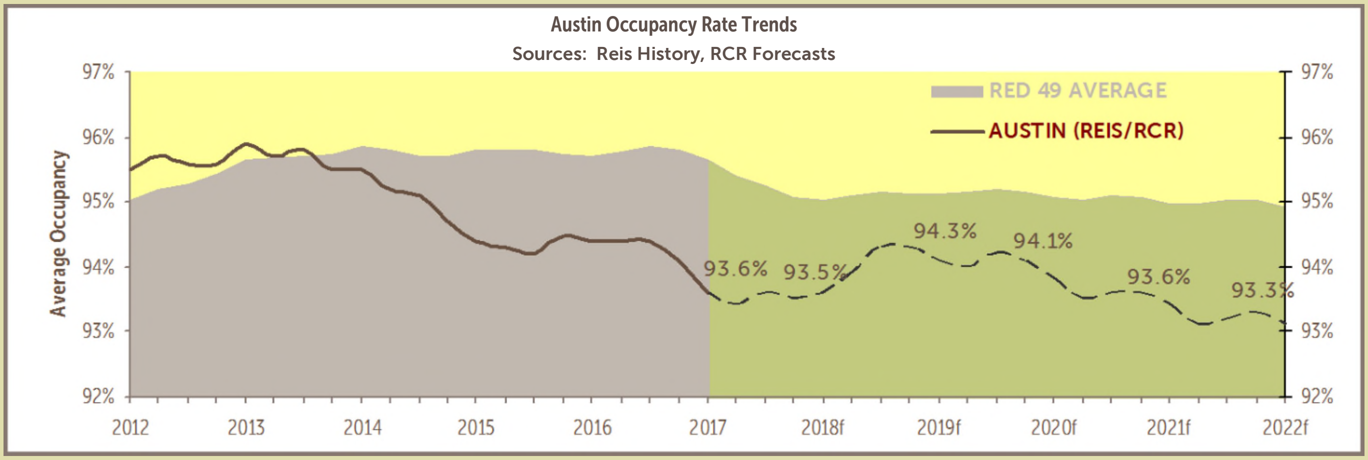
1Q17 PROPERTY MARKETS AND TOTAL RETURNS

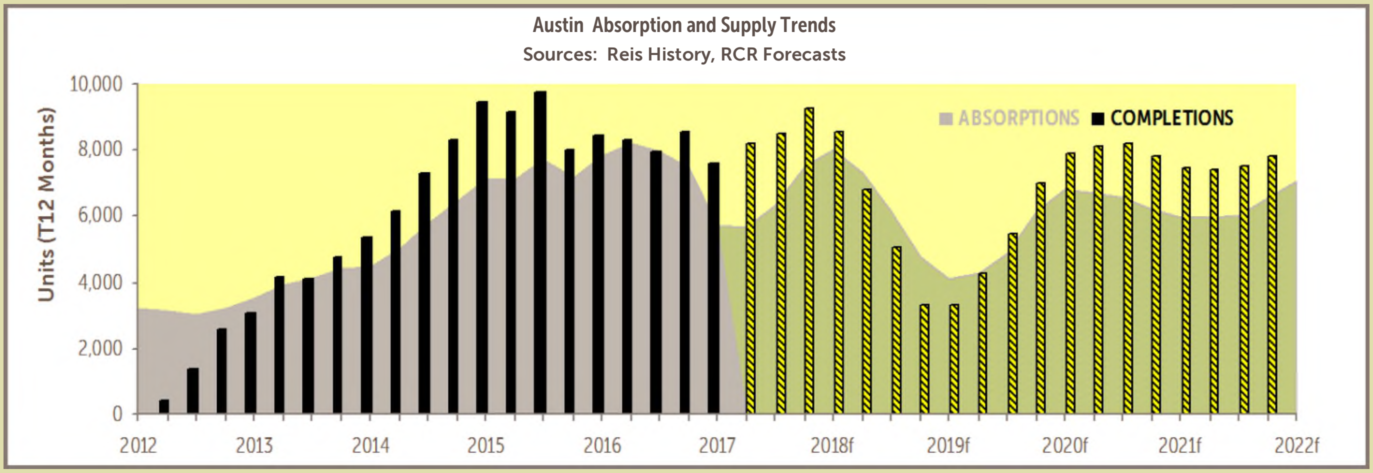
Austin property markets were relatively quiet during the first quarter, particularly when compared to 4Q16's near record activity. Seventeen sales of properties of 80 or more units were consummated, down from 30 and 25 in the prior and year-before quarters, respectively. Volume was estimated to be about $550 million, less than one-half of the sale proceeds collected in 4Q16.

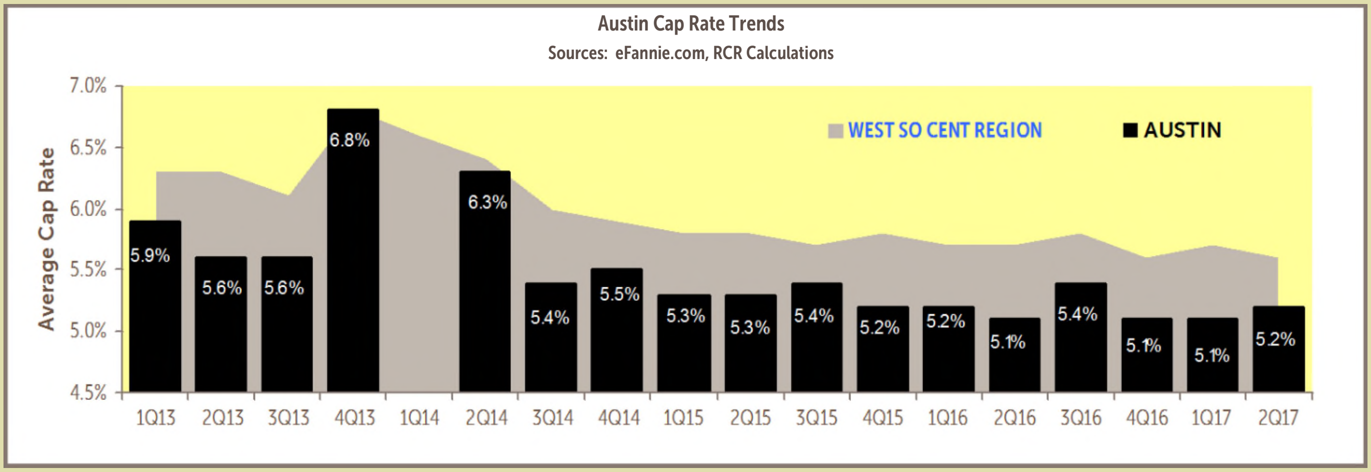
Sales activity gained momentum in 2Q17. Through the third week of June, twenty investment sales were recorded for estimated proceeds of more than $800mm. Trade was highlighted by the sale of a sprawling 2,044-unit Far Northwest asset that commanded a price near $400mm.

Cap rates were slightly higher. Class-A/B+ institutional quality gardens traded to high-4% to low-5% yields. Class-B value-adds commanded prices equating to 5.25% to 5.5% caps. Lower quality asset yields fell in the mid-6% range.

Cap rates appeared to drift slightly higher in 2017 trade, leading RCR to raise the purchase cap rate proxy 5 basis points to 5.25%. At this level, a 5.79% terminal cap and model derived occupancy and rent point estimates, we calculate that a 1Q17 investor would expect to earn a 7.0% unlevered annual return on a 5-year hold. This ranks 23rd in the RED 49, and is 16bps above the peer group mean. High rent model standard error trims the RAI to group #44.

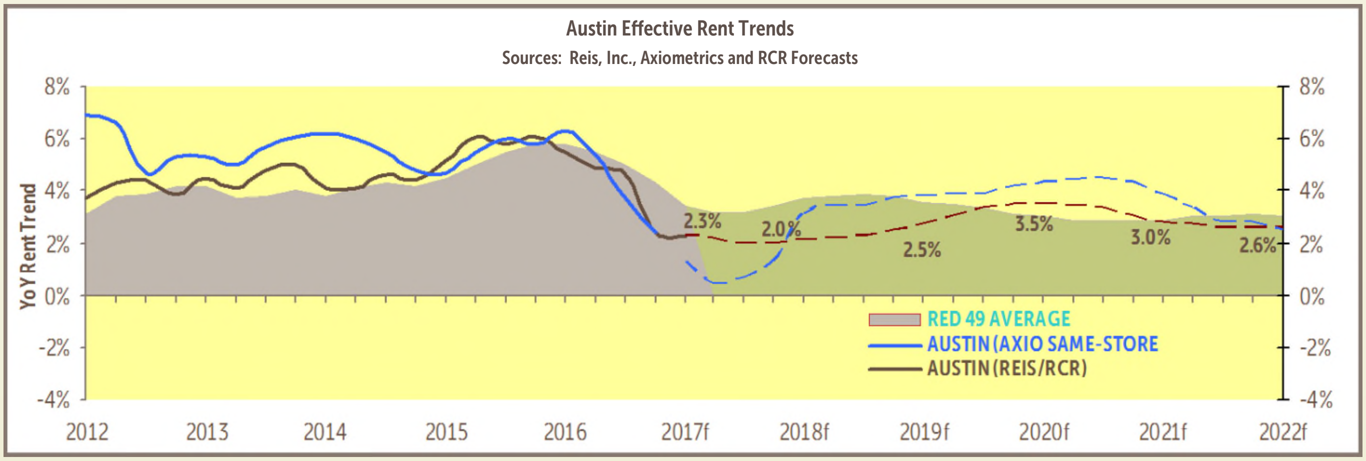


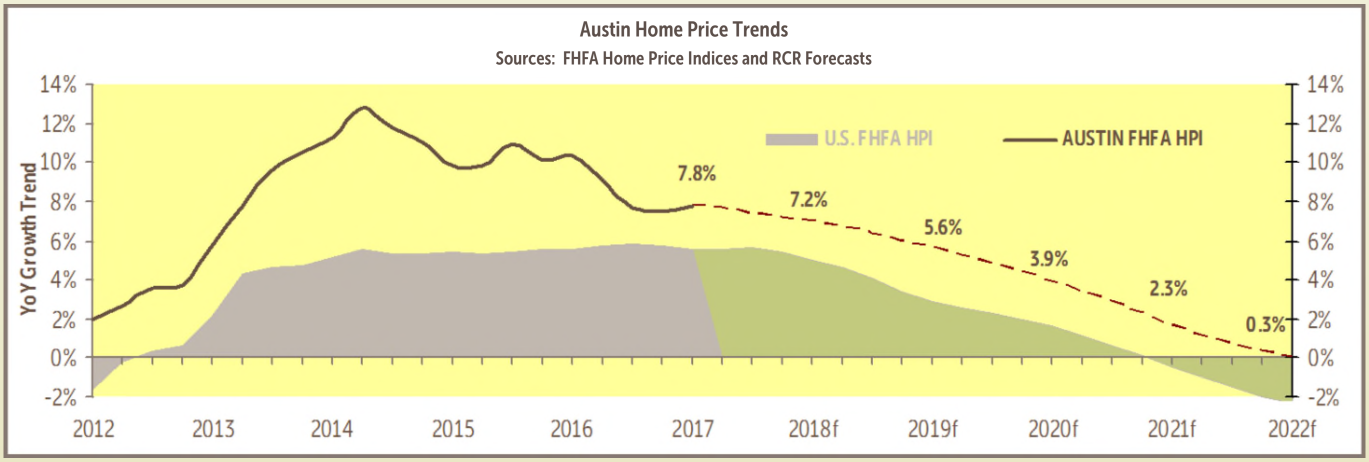


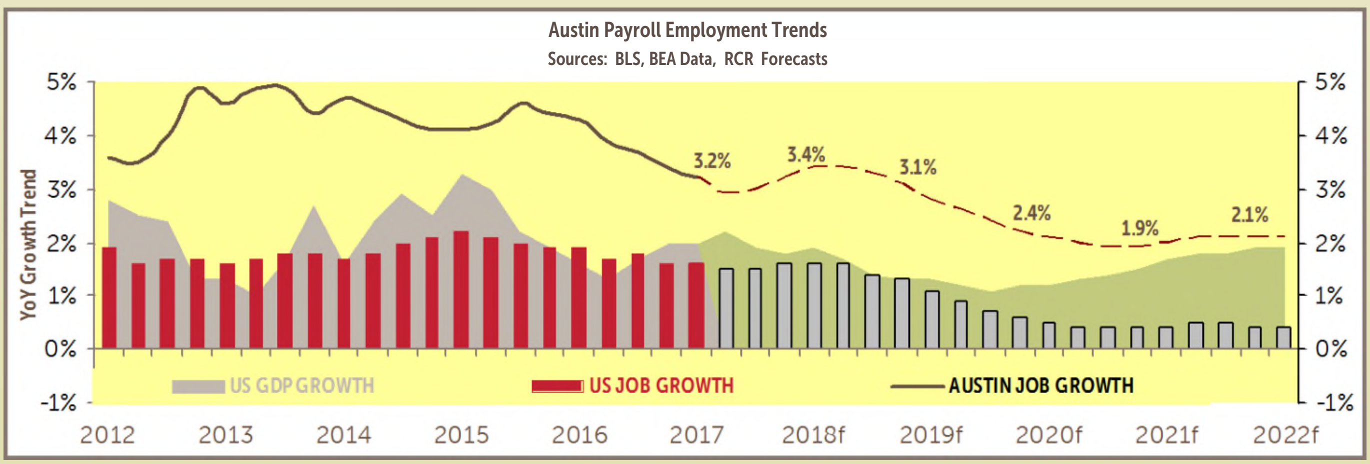


NOTABLE TRANSACTIONS

Property Name (Submarket)	Property Class/ Type (Constr.)	Approx. Date of Transaction	Total Price (in millions)	Price / Per Unit	Estimated Cap Rate
Ridge at Barton Creek (Near So. Central/Barton Hills)	B / GLR (1973/2008)	6-Jan-2017	$51.8	$126,838	5.28% (FRD)
Bristol Heights Apts. (North Travis / Parmer Park)	B+ / GLR (2003)	20-Jan-2017	$51.5	$146,811	5.5%
Windsor Barton Creek (Near So. Central /Rollingwood)	B+ / GLR (1978/2008)	4-Apr-2017	$21.3	$158,955	4.94% (FNM)
Copper Mill (Far North Central / North Lamar)	B- / GLR (1983)	5-May-2017	$32.0	$100,000	6.33% (FNM)
Riata (Far Northwest / Riata Trace Parkway)	B+ to A / GLR (97-01)	26-May-2017	$379.8 (allocated)	$185,830	5.0%
Landing at Round Rock (Far Northwest / Brushy Creek)	B+ / GLR (2000)	16-June-2017	$90.5	$155,232	4.9%

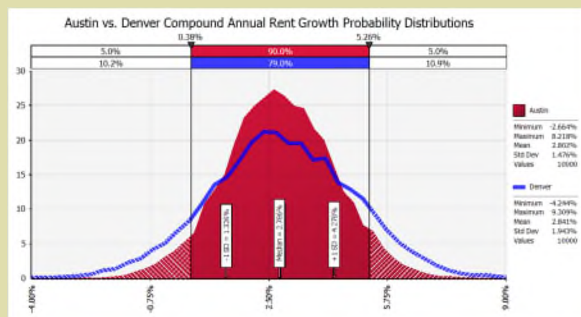

Austin Effective Rent Trends
Sources: Reis, Inc., Axiometrics and RCR Forecasts
YoY Rent Trend
8%
6%
4%
2%
0%
-2%
-4%
2.3%
2.0%
2.5%
3.5%
3.0%
2.6%
RED 49 AVERAGE
AUSTIN (AXIO SAME-STORE
AUSTIN (REIS/RCR)
2012
2013
2014
2015
2016
2017f
2018f
2019f
2020f
2021f
2022f


Austin Home Price Trends
Sources: FHFA Home Price Indices and RCR Forecasts
YoY Growth Trend
14%
12%
10%
8%
6%
4%
2%
0%
-2%
U.S. FHFA HPI
AUSTIN FHFA HPI
7.8%
7.2%
5.6%
3.9%
2.3%
0.3%
2012
2013
2014
2015
2016
2017
2018f
2019f
2020f
2021f
2022f


Austin Payroll Employment Trends
Sources: BLS, BEA Data, RCR Forecasts
YoY Growth Trend
5%
4%
3%
2%
1%
0%
-1%
3.2%
3.4%
3.1%
2.4%
1.9%
2.1%
US GDP GROWTH
US JOB GROWTH
AUSTIN JOB GROWTH
2012
2013
2014
2015
2016
2017
2018f
2019f
2020f
2021f
2022f

SUBMARKET TRENDS (REIS)

Submarket	Reis Inventory Percent Change	Effective Rent			Physical Vacancy		
		1Q16	1Q17	Change	1Q16	1Q17	Basis Point Change
Central	3.3%	$1,262	$1,248	-1.1%	8.7%	9.1%	40 bps
East	1.6%	$895	$942	5.2%	7.4%	6.9%	-50 bps
Far North Central	0.0%	$717	$741	3.4%	4.2%	3.6%	-60 bps
Far Northwest	3.1%	$1,073	$1,104	2.9%	4.4%	4.6%	20 bps
Far South	8.2%	$1,078	$1,157	7.3%	6.7%	8.4%	170 bps
Highway 183 / Cedar Park	4.0%	$897	$974	8.7%	7.2%	5.4%	-180 bps
Near North Central	9.9%	$847	$911	7.5%	2.6%	7.0%	440 bps
Near Northwest	0.0%	$937	$942	0.5%	1.8%	2.1%	30 bps
Near South Central	1.3%	$1,190	$1,161	-2.4%	10.7%	7.3%	-340 bps
North Travis	6.9%	$945	$984	4.1%	5.7%	6.3%	60 bps
Ranch Rd 620N / FM2222	0.0%	$1,222	$1,240	1.5%	10.8%	7.0%	-380 bps
Round Rock/Georgetown	0.4%	$956	$981	2.6%	4.5%	3.9%	-60 bps
San Marcos / North Hays	6.5%	$911	$974	6.9%	7.9%	6.1%	-180 bps
Southeast	2.2%	$913	$928	1.6%	6.4%	8.3%	190 bps
Metro	4.0%	$1,011	$1,034	2.3%	5.6%	6.4%	80 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

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