Real Estate Market Intelligence 2016

Multifamily Development Quarterly Report–Q2

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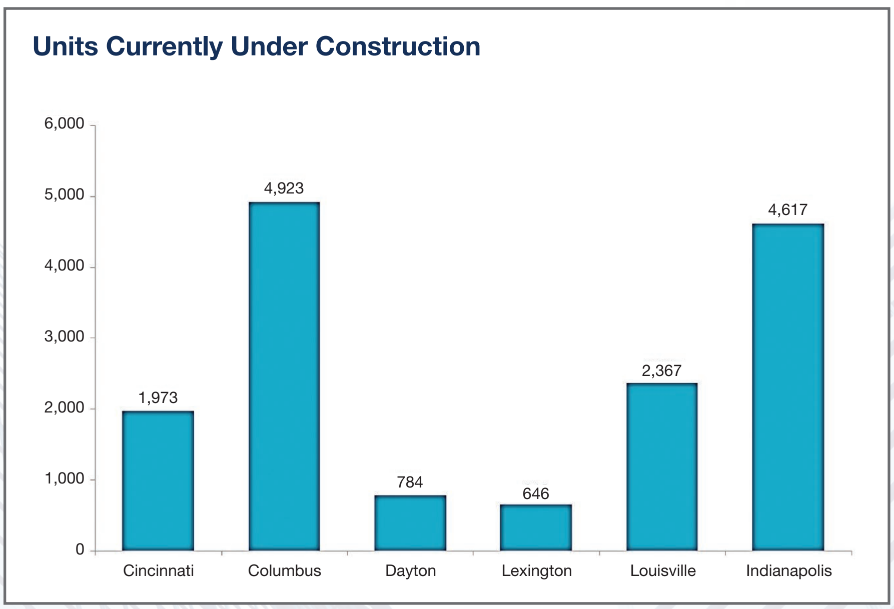
1. Key Findings

The multifamily asset sector saw nearly $35.4 billion of investment sales activity for the first-quarter of 2016. This figure represents an 8.6% increase compared to the first-quarter of 2015 and represents the largest first-quarter volume on record. Additionally, the first-quarter sales volume figure represents the second-largest figure of the last 15 quarters, eclipsed only by the unprecedented fourth-quarter 2015 volume of $49.2 billion.

Across Ohio and Indiana, over $500 million worth of multifamily units were sold by the beginning of Q2; nearly double the sales volume of the prior quarter. The majority of the sales were located in the Indianapolis and Louisville metro areas. Over 15,000 units are currently under construction in the region, which may cause an increase in the current vacancy rate.



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1. Key Findings *(continued)*

Demand for multifamily rental housing was higher than expected in 2015, absorbing much of the newly completed supply. Therefore, vacancy rates remained low and rents continued to rise in most markets. As more supply enters the market in 2016, multifamily fundamentals will moderate, more so in some geographic markets than others. Favorable demographic trends, strength in the job market and reduced affordability of owning a home will continue to fuel demand for multifamily rental units. The national vacancy rate will increase slightly, but it will remain less than the historical average through 2016.

With a strong pipeline of apartments under construction, deliveries in 2016 are expected to exceed 2015's levels. However, in the wake of the forecasted wave of deliveries expected in the multifamily market this year, many banks are pulling back on their construction lending even though so far absorption has kept pace with new supply. According to the most recent results of the NMHC Quarterly Survey, the Debt Financing Index stands at exactly 50, representing mostly unchanged conditions in the debt market. However, two-thirds of respondents indicated lower bank construction financing availability, with 40% reporting slightly lower availability and 26% reporting significantly lower availability.

Despite the Federal Reserve's decision to increase interest rates in December 2015, multifamily property price growth will remain strong and capitalization rates will not be significantly affected in the short-term. Multifamily origination hit record volumes in 2015. It may have another record year in 2016 because of increasing property prices, new completions and maturities, all of which present favorable investment opportunities.

2. Quarterly Transactions

Transactions in Ohio

- Towne Properties plans to build a 92-unit, $13.5-million apartment project in Evanston. The new project, referred to as DeSales Flats phase 2, will be available next spring or early next summer. The project has not been financed yet. Towne Properties is aiming for LEED Gold certification with this project. Working with the City of Cincinnati, the project would receive a 15-year, 75% tax abatement.
- RAIT Financial Trust, the owner of Tower at Erieview, is considering a conversion project that could yield 185 high-rise apartments, along with renovations to the building. RAIT took full possession of the property late last year.

Transactions in Indiana

- The U.S. Department of Housing and Urban Development is awarding Indiana over $600,000 to help pay for public housing projects across the state. Most of the money will go to public housing agencies in Evansville and Elkhart, with each receiving $250,000 for repairs and improvements to existing public housing units.

Transactions

- CBRE Capital Markets' Central Midwest Multifamily unit arranged the sale of 82 Flats at the Crossing, a 232-unit luxury apartment community located in Indianapolis. The firm represented the seller, Cityscape Residential, a locally-based developer that built the property in 2013. The buyer, an Indianapolis-based private investor, purchased the property for an undisclosed amount.
- Abbott Properties purchased Parkway Apartments and Townhomes, located in West Lafayette, for $10.85 million from an affiliate of FM Capital. The 446-unit property includes studio, one, two and three bedroom floor plans. Abbott plans to renovate both the interior and exterior and streamline operations.
- Jackson Development is developing an entire city block in Fountain Square, Indianapolis. The project, which has yet to be named, will sit on 1.02 acres at the southwest corner of Prospect and Spruce streets. Plans filed with the City include 8,500 square-feet of commercial space on the ground floor, topped with four stories of apartments ranging from studios to three-bedroom units.
- RESOURCE Commercial Real Estate announced the sale of Parkside Apartments, a 48-unit apartment community located in Franklin, Ind., for an undisclosed amount. Parkside Franklin Apartments was the buyer and the seller was Parkside Properties.
- Tikijian Associates arranged the sale of Aspen Chase Apartments, a 130-unit apartment community located in Indianapolis, to Capital 8 Group. Tikijian Associates represented the seller, Greater Vision IV. Financial terms were not disclosed.
- Tikijian Associates represented Barrett & Stokely in the sale of Cumberland Pointe Apartments, a 336-unit Class A apartment community in Noblesville, Ind. Terms of the transaction were not disclosed. Cumberland Pointe was marketed without an asking price and attracted significant interest from local, regional and national investors. The buyer was a Denver-based private real estate investor. Carter-Haston is managing the property for the new owner.
- Tikijian Associates arranged the sale of Beechmill Apartments, a 256-unit multifamily community located in Indianapolis. Tikijian represented the seller, an unnamed Indianapolis apartment owner and manager with more than 2,800 units in central Indiana. The buyer was an affiliate of Birge Asset Management, an Indianapolis-based PE and property management firm.

3. Multifamily REITs

Home Properties

- A privately held company, owned by Lone Star Funds, that owns, operates, acquires and rehabilitates apartment communities primarily in selected Northeast and Mid-Atlantic markets. It operates over 30,000 apartment units.

AvalonBay Communities

- A publicly traded REIT headquartered in Virginia, the company develops, redevelops, acquires and manages more than 250 apartment communities in U.S. markets that are defined as high barrier-to-entry.

Colonial Properties Trust

- Headquartered in Alabama, Colonial is a diversified REIT company that manages retail, office and multifamily properties throughout the U.S. In October, 2013, Colonial merged with MAA REIT.

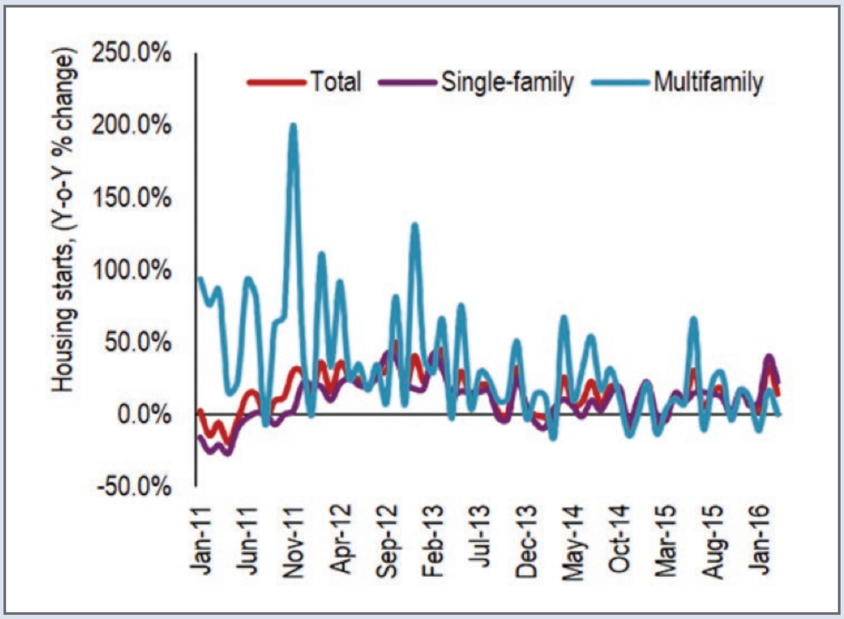
Equity Residential

- A publicly traded REIT based in Illinois. As as of January 31, the company owned or had investments in 316 properties consisting of 85,391 apartments located primarily in Boston, New York, Washington, D.C., Washington, and California.

4. Market Overview

Multifamily Construction

- The seasonally adjusted annual rate of multifamily construction for the month of March was 312,000, comprising 28.7 % of total construction starts for the month and essentially matching the rate from one year prior. This figure reflects a six-month trend of multifamily construction starts falling at or below the current 12-month rolling average of 384,000, reflecting a steady slowing of new starts. Multifamily construction permits, which serve as a leading indicator of starts, also saw declines in March.
- The seasonally adjusted annualized rate was recorded at 324,000 in March, down for the third straight month and 12.4% year-over-year. Comparatively, the seasonally adjusted annual rate of single-family construction starts was recorded at 764,000 in March.



Multifamily vacancies increasing in CBDs across the U.S.

- Tens of thousands of new apartments are now opening in central business districts (CBDs) around the country. However, downtown sub-markets continue to be strong, with developers creating new neighborhoods in CBDs. Many continue to benefit from all the new renters, including Millennials and Baby Boomers, who seem eager to live in the city.
- Developers continue to pull new permits to build, though it's not clear how many will start construction. In downtown sub-markets, the number of apartments is growing at a rate of 5% a year, on average and is expected to continue through the third quarter of 2017. The percentage of vacant apartments in downtown sub-markets averaged 6.3% at the beginning of Q2, up from 5.6% a year ago.
- In comparison, in the suburbs the number of apartments is growing by less than 2% a year. The percentage of vacant apartments in suburban areas averaged 4.2% at the beginning of Q2, up just slightly from 4% the year before. Rent growth is also stronger in suburban areas, particularly for class-A and class-B apartments.

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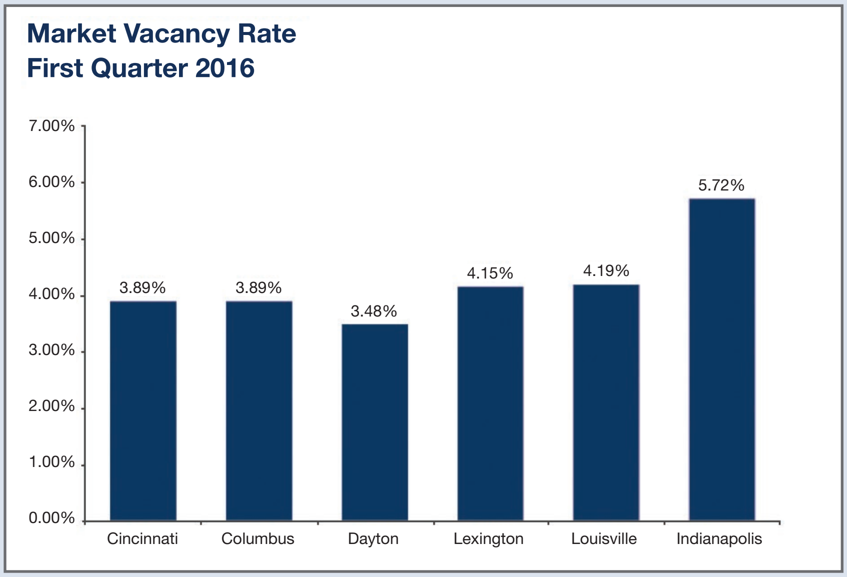
4. Market Overview *(continued)*

Multifamily vacancies increasing in CBDs across the U.S.

- However, prices for apartment properties in CBDs has risen much more strongly than prices for suburban apartments, which helps explain why developers are eager to build downtown. Prices for downtown properties rose nearly 450% from 2000 to the end of 2015.
- Prices also rose for suburban properties, but not nearly as much. And the more suburban locations resembled a downtown, the more price growth they experienced. Prices rose nearly 300% for suburban apartments in "highly walkable" areas, close to 250% in "somewhat walkable" areas and just 200% in "car-dependent" suburban areas.



Multifamily rentals driving housing market

- The rental market continues to drive housing's recovery—36% of U.S. households opted to rent in 2015, the largest share since the 1960s. Last year marked the largest single-year increase in renter households in Housing Vacancy Surveys (HVS) records dating back to the mid-1960s, up 1.4 million. The surge in rentership caused the multifamily construction sector to boom—mostly in high density areas—hitting a 27-year high for starts at 397,300, an 11.8% increase from 2015.
- Affordability remains one of the largest issues highlighted in the current rental market. The number of cost-burdened renter households rose by 3.6 million to 21.3 million from 2008 to 2014, and the number of households paying more than 50% of income for housing jumped by 2.1 million to a record 11.4 million. While the multifamily sector saw a surge in construction starts, new home construction was still near historic lows last year with only 1.1 million units. Mortgage conditions for spec homes are still tight, and student debt continues to burden young renters and hinders them from making down payments on homes. Over the next 10 years, the millennial generation is expected to form 2 million households per year, increasing the total number of millennial-headed households from 16 million in 2015 to a projected 40 million in 2025.
- The rental market should remain robust over the next decade as millennials will begin to form households, and households ages 30-40 will remain in multifamily, and baby boomers downsize into apartments.

5. Outlook—Trends to Watch

Short term rentals affecting multifamily sector

- Multifamily property owners are being impacted by Airbnb, VRBO and other similar services in various ways. As the number of people choosing to rent out their living space for short-term stays has continued to grow at an explosive rate, many cities and counties have moved aggressively to regulate, restrain and tax short-term rental housing, typically defined as a rental of less than 30 consecutive days.
- Ordinances have been created to address concerns that many communities have about how short-term rentals affect the protection of the neighborhood environment, the safety of renters, the collection of transit occupancy tax revenue and the playing field for traditional hotels. Some communities have adopted outright bans, while others have put geographical restraints into place. New operational and occupational requirements, as well as licensing and tax ordinances, have also been implemented in some jurisdictions.
- With a real estate market where more than 80% of home seekers are leveraging online search tools, it was only a matter of time before an application like Airbnb was launched, with a rather unique twist, to address a special market of accommodation seekers. So far, the company is valued at more than $25.5 billion, and is increasingly growing in popularity among home owners, tourists and business.