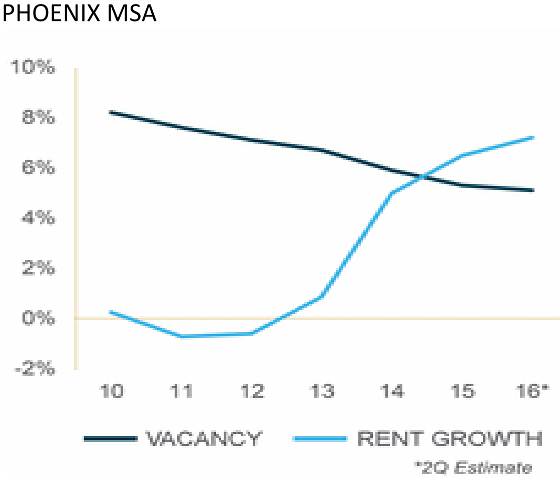
MULTIFAMILY HOUSING – SEPTEMBER 2016

OVERVIEW
The multifamily market continued to post strong gains in the first half of 2016. Employment across the US is at an all time high, and the length of the job growth gains have resulted in a boost in wage growth. Steady job and wage gains have supported the strength of the leasing market for apartments which has in turn increased effective rents of the prior years. Developer activity remains robust, with deliveries for 2016 expected to top 285,000 units, the most new apartments delivered in a year since the 1980s. Lenders have begun to more closely monitor development activity and are now tightening funding for new projects in markets they believe face overdevelopment risk. With builder activity concentrated in just 10 major metros nationally, those markets are receiving the greatest scrutiny. Secondary and tertiary markets are getting more attention.

OUTLOOK
The outlook for multifamily housing is optimistic. In JLL's Multifamily Investment Outlook, there were six themes that were identified: 1) Employment gains support consolidated advances in multifamily, 2) A homeownership bottleneck preserving a stable, strong rental pool, 3) National rent growth softens from peak while maintaining above average levels, 4) Leasing markets remain tight in spite of sustained completions, moderating absorptions, 5) Multifamily sales have the potential to outpace record high 2015, 6) Diversified growth and pricing discount retaining investor focus on secondary markets.

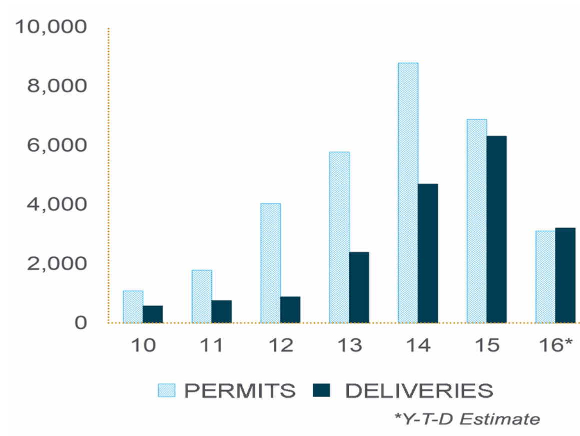
PHOENIX MSA



Source: Berkadia

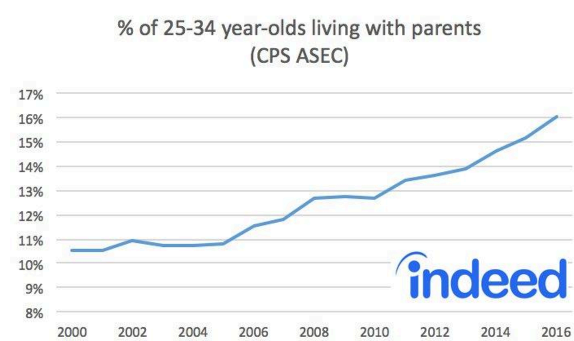
In Phoenix, the multifamily market showed continued strength through the second quarter. Vacancy was slightly higher which is somewhat seasonal, however rents are up more than 8% during the past 12 months. Most expect the vacancy rate to trend lower from the current 5.9% level in the second half of the year.

Construction activity will remain strong through the end of the year. Builders completed construction on 3,210 apartments across the metro during the first half of 2016. The chart below outlines permits and deliveries in the Phoenix MSA:



Source: Berkadia

Developers submitted permits for 3,110 multifamily units since the close of 2015. Recent issuance expanded the planning pipeline to 75 multifamily communities, which could bring approximately 20,900 apartments to the market.



While the amount of future supply may seem daunting, there are many indicators which point to pent up housing demand. The for-sale housing market has shown modest demand growth in prior years, however apartments will be a primary source of housing for younger workers.

FOR-SALE ATTACHED HOUSING

As part of the exercise we also looked at for-sale multifamily housing. While the number of projects has increased significantly in the past few years with builders increasing focus on 'infill' the sales numbers show relative weakness when compared to the broader for-sale single family detached housing market. Sales of condos/townhomes were a meager 1.75 per month for 2016, on par with 2015 and down from 2014. While much of this is likely supply related, the figures are nonetheless disappointing.

INSIDER KNOWLEDGE:

- Despite some grumblings of overbuilding, job growth should keep pace with deliveries to keep vacancies low and rents on an upward trend.
- Look for new construction to taper off in 2017 and into 2018.
- Some lenders are reaching their capacity limits on construction financing for new supply which could also have an impact on timing of new development.
- The homeownership rate of households headed by 25- to 34-year-olds was 36.9 percent in 2014, nearly 10 percentage points lower than in 2006, at roughly the peak of the housing bubble.
- Even if homeownership rates begin to improve, job growth and more normal rates of household growth (i.e. pent up demand) should support multifamily market.

OPPORTUNITIES:

Taking into account these factors, we evaluate on an ongoing basis the types of investments we are pursuing and how the general market opportunities fit with our investment platforms. Here are some key takeaways from that analysis.

MULTIFAMILY ACQUISITION

Everest is currently pursuing a strategy to acquire high quality Class B apartments that have value-add potential and the ability to raise rents once improvements are made.

MULTIFAMILY LAND

Everest is also pursuing land opportunities that are either zoned for multifamily or have the potential to be rezoned to that designation. Many of these parcels are in areas that have not seen new MF development due rents and the cost of construction.

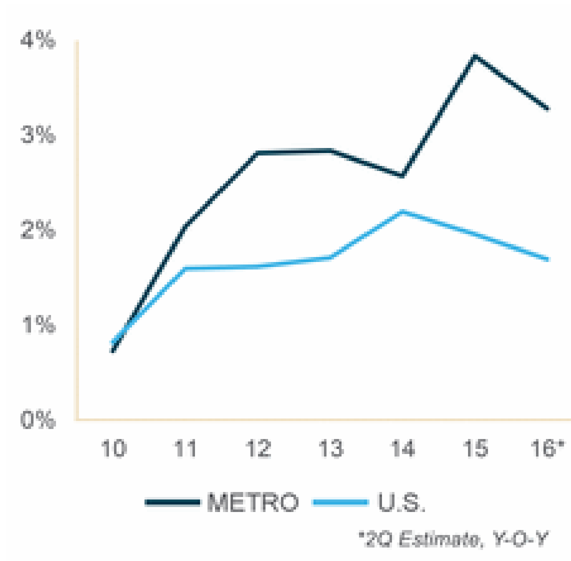
DISTRESSED DEALS

Based on the anemic sales at many of the new condominium projects in the Phoenix MSA, there may be opportunities to recapitalize or acquire distressed condo projects.

LENDING

A second potential investment platform is providing primary or 'mezzanine' financing to multifamily developers. These opportunities arise as primary lenders hit their limits or there is a funding gap between the equity partner and the primary lender.

PHOENIX MSA VS US – EMPLOYMENT GROWTH



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