AFFORDABLE CENTRAL TEXAS

Austin Workforce Multifamily Report

Spring 2018

Capital Pressure Pushes Pricing Despite Slower Market

In this second edition of the Affordable Central Texas Workforce Housing Multifamily Report, we examine the investment sales market. The 2017-year end and the first quarter of 2018 saw a lower than average number of offerings. Capital remains very focused on Austin and demand for these properties was extraordinary leading to terms and timing not seen before in central Texas. The emergence of non-refundable earnest money at the signing of purchase and sale, reduced inspection and closing periods and removal of financing contingency periods all are indications of an overheated market. Cap rates for Class B properties have fallen beneath 5% on trailing 3-month operating results and per unit pricing is setting new records. We expect to see a strong increase in property offerings during the normally slower summer months as the market responds to improved pricing.

A further indication of the power of capital to move this market is that market fundamentals have shown increasing weakness over the past 4 quarters (see pages 2 and 3 for more detail). Occupancy rates have declined and rental concessions have increased dramatically, especially on properties for sale where sellers have attempted to support higher rents with increased free rent and other concessions. The most recent quarter has shown a sign of stability with an increase in effective rents.

These market conditions further confirm the need to preserve workforce affordability in Austin. In order to support the current pricing, buyers will be aggressively seeking to increase rental rates on newly acquired properties, exacerbating an already difficult affordability situation. Affordable Central Texas recently announced it has raised sufficient capital to begin to acquire properties for the Austin Housing Conservancy. Please contact us to discuss our objectives and strategies.

Overall Market

Construction:

Deliveries move back in line with the five-year average and fall short of last year's peak in the construction cycle when more than 10,000 units came online.

8,300 units to be completed

Vacancy

Upward pressure remains on the vacancy rate which increases to 6.2 percent in 2018. Vacancy also ticked up during the last two annual periods

30 bp increase in vacancy

Rents:

Following a 1.9 percent bump last year, rent growth remains well below the previous five-year average of 5 percent during 2018, rising to $1,228 per month.

2.3% increase in effective rent

Competitive Home Buying Market Extends Residents' Stays in Rentals

Strong demographic trends continue, create favorable rental market. Steady migration and household formation are creating healthy demand for housing in Austin. The homeownership rate in the metro has fallen for three consecutive years amid a tight single-family housing market, pushing many new residents and would-be homeowners into rental housing. As a result, apartment development has been elevated over the past four years to meet rising demand, and developers have added more than 8,000 units to inventory each year, up from an average of 3,000 apartments completed each year from 2010 to 2013.

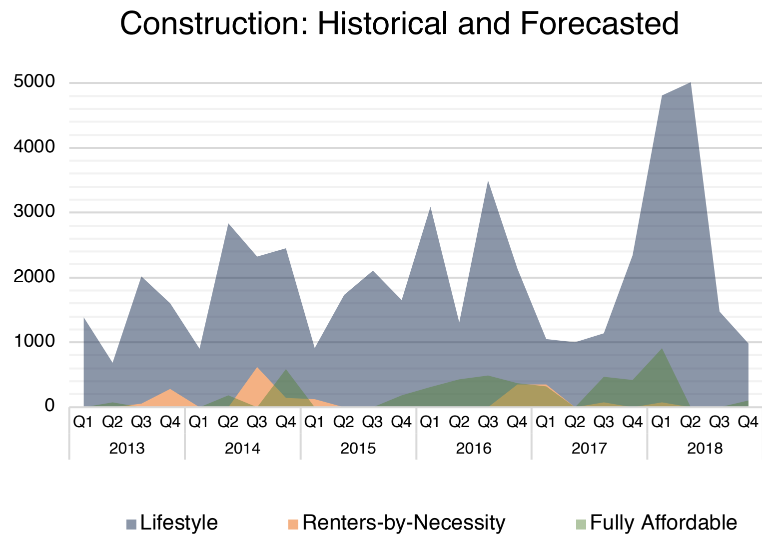
Heightened deliveries result in a competitive leasing environment. Although completions were delayed by an average of 4 months during the quarter, 2,086 conventional units were added, which brought the annual total to 11,514 new units. Units taken off the market because of property type changes, upgrades or a switch to condominiums diminished the number of new unit additions, leaving a net unit gain of 1,821 units. With such a large number of typically affordable units being taken off the market to upgrade we expect to see an overall increase in rent growth once upgrades are complete and units are absorbed in to the market. Further exacerbating the affordability issues plaguing the city of Austin.

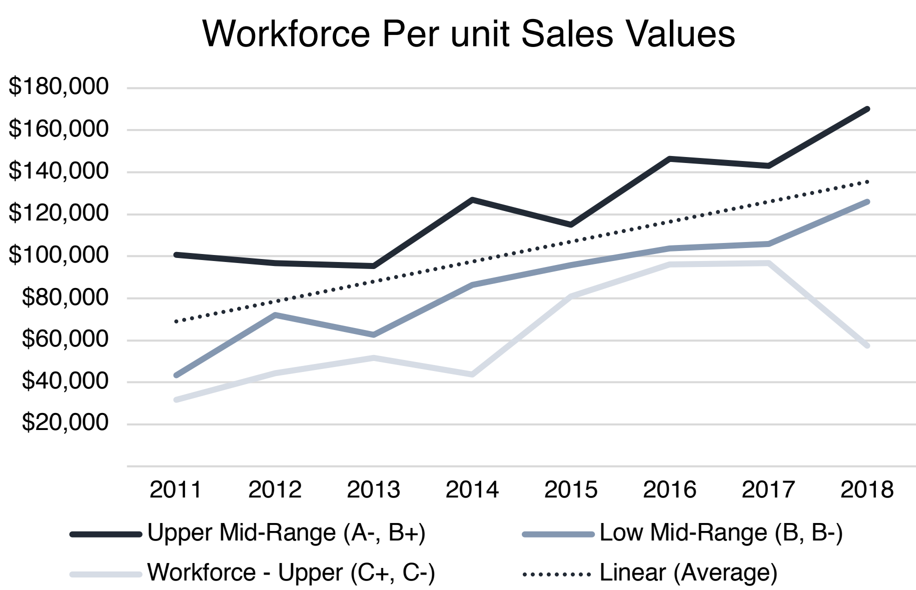
Overall Market Cont.

- Buyers familiar with the market are heavily targeting value-add apartment assets. These buyers are positioned to capitalize on any property-specific inefficiencies.

- As rent growth remains below the five-year average another year of slow NOI growth is expected for some owners. This could potentially cause investors to sell assets in search of higher-yielding opportunities. Those choosing to sell will be met with strong interest from buyers seeking to lock in lower interest rates in anticipation of rate hikes throughout 2018.

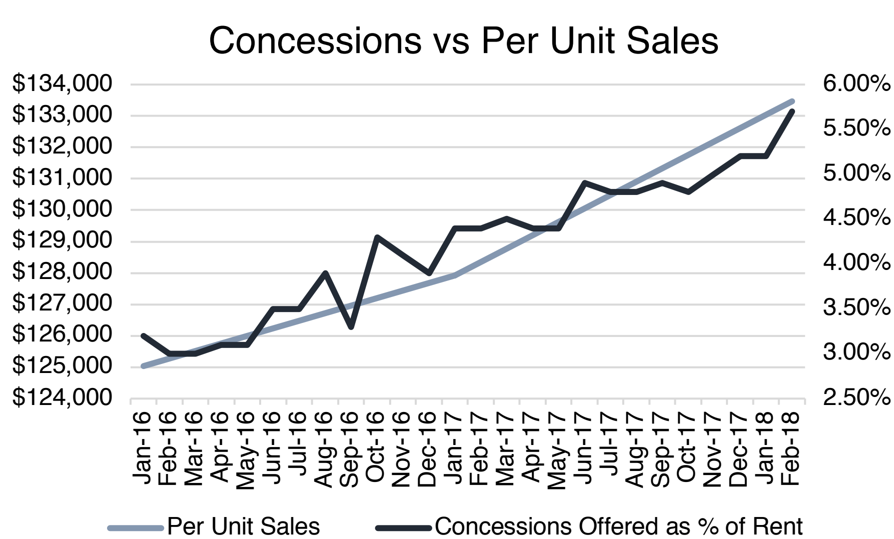
- A consistent stream of completions over the last few years will continue to provide opportunities for investment, and high land and construction costs will keep development limited to luxury apartments.

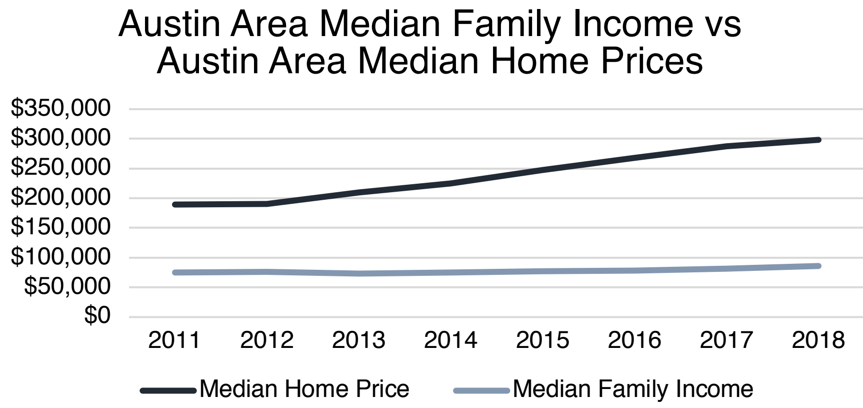




Apartment sales remain strong as over 1 billion in property value traded hands in the past year. The average price per unit advanced 7 percent to $119,500 per door. Apartment demand remains strong as companies and individuals continue to find the market an attractive place to work and live. Investors will remain active, seeking properties with upside potential.

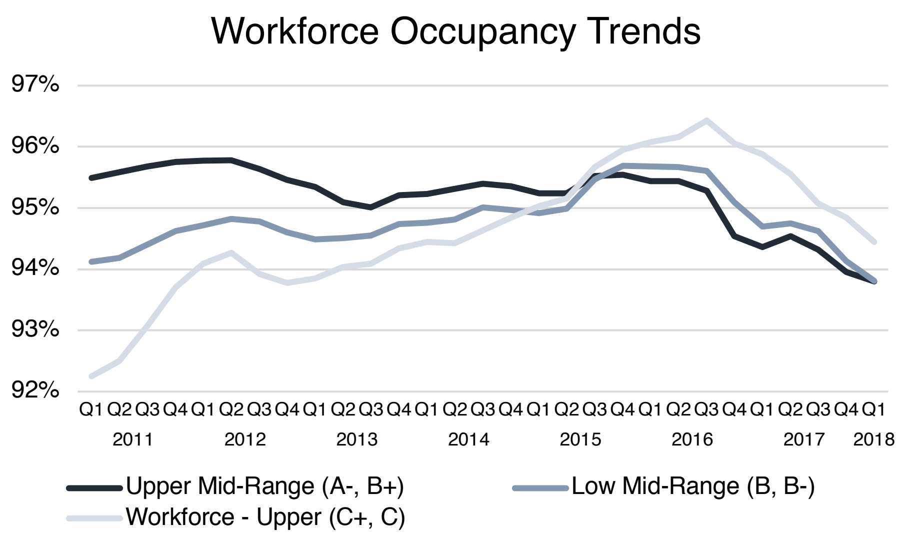
With such a large influx of new product in Austin there has been a drop in rent growth and an increase in concessions offered to renters. As these types of trends typically show a market ready to slow down, from an acquisition standpoint we are seeing continued growth in the per unit sales price on recently sold B and C properties. Showing that investors expect a rapid growth in rents in the coming years consequently reducing the number of affordable units in central Austin.

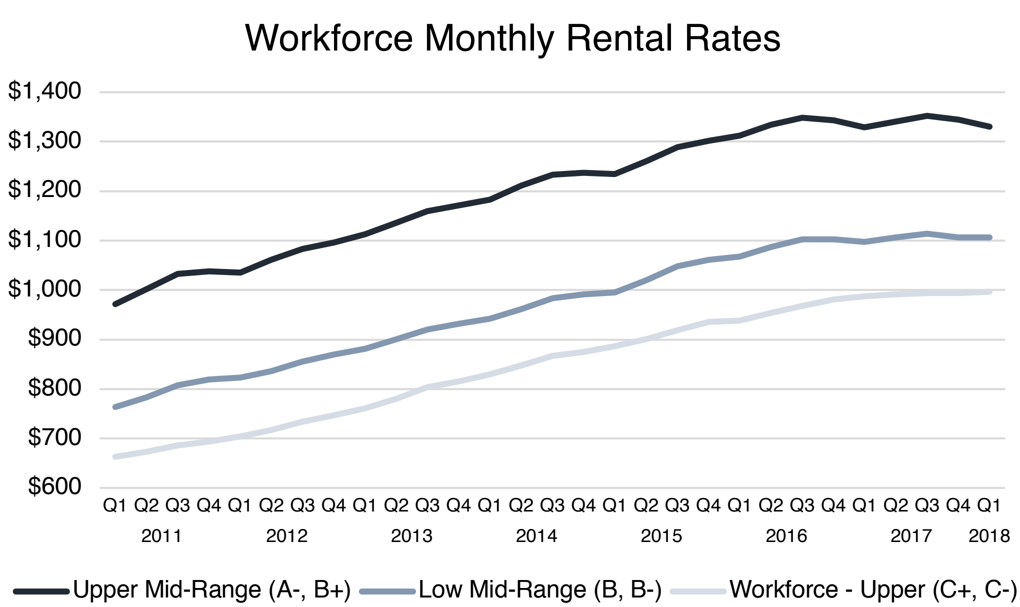




With the median home price in Austin going up over 56% and median family income only rising 13% since 2012 many prospective homeowners are being forced to rent as a competitive and expensive housing market would force them outside the city limits into more affordable areas. This in turn has created a greater demand for rentals and is increasing prices, pushing current workforce apartment residents out of the downtown area and into surrounding suburbs.

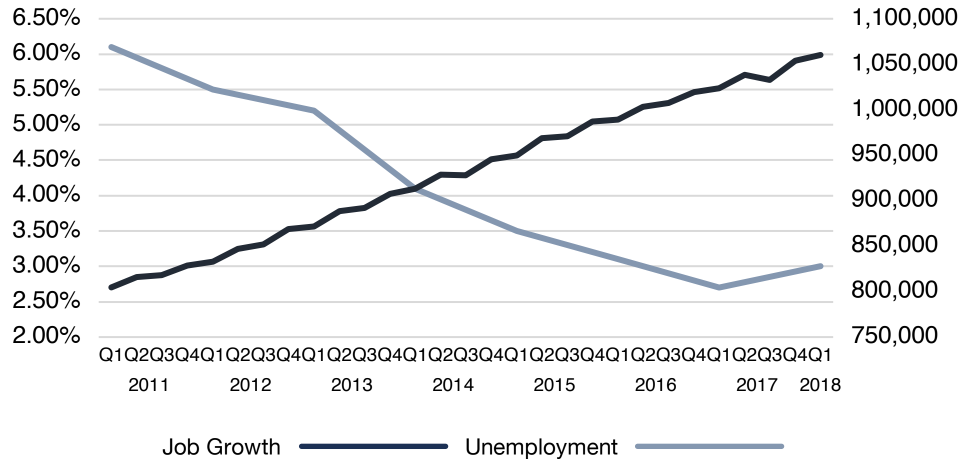
The market's occupancy rate decreased from 94.1% in 4Q17 to 93.9% in 1Q18 and was down from 94.5% a year ago. The market's occupancy rate was below the national average of 94.5% in 1Q18. For the forecast period, the market's occupancy rate is expected to be 95.0% in 2019, and average 95.0% from 2020 to 2022.





Although a heavy new supply of Class A apartments is creating a flattening of rent growth throughout the Austin-Round Rock MSA, Class B and C properties continue to show growth rates higher than Class A, with just over a 1% increase in rental rates as of March 2018, compared to a 0.7 % loss in Class A properties. Rent growth is expected to rise throughout 2018. As development slows and new units are absorbed, Yardi Matrix predicts an overall rent growth of 1.6% by the end of 2018, returning to above 2.1% by the end of 2019.

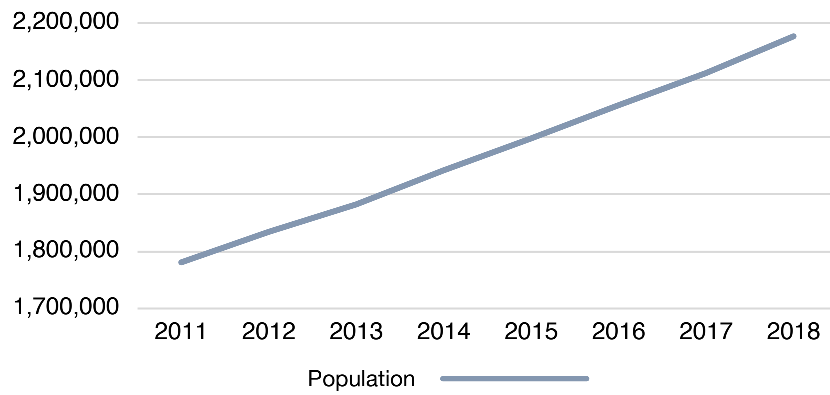
Job Growth vs Unemployment Rate



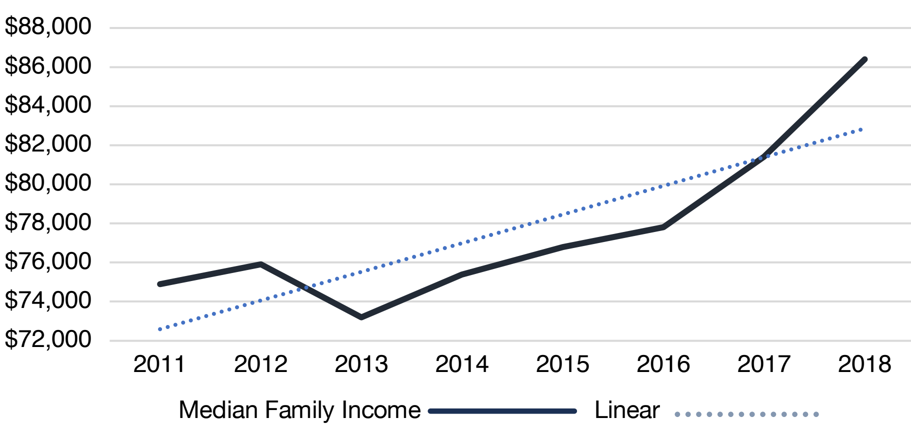
Austin's employment continues to grow adding 37,300 jobs in the year ending in February 2018. The Professional and Business Services sector gained 11,400 jobs during the 12 months ending February 2018, constituting job growth of 6.7%. The Trade, Transportation, and Utilities sector grew 8,500 jobs during the same period; a 4.9% growth rate.

Population Growth

With a growth of just over 3% the Austin-Round Rock MSA population continues to increase at a rapid rate. With growth expected to continue at a similar rate in the coming years, Austin is projected to reach over 3 million people by 2030.



Median Family Income



Median Family Income continues to grow at a rate not seen in most parts of the country. From 2017 to 2018 median family income grew 5.65%. A flattening in growth is expected to occur in the coming years taking MFI growth back down to 2% annually.

Contact Affordable Central Texas

2525 Wallingwood Drive
Building 13 Suite A
Austin, TX 78746

David Steinwedell - CEO
(512) 592-9906
steinwedell@affordablectx.org

Sources: Yardi Matrix, Axiometrics, U.S. Department of Housing and Urban Development, Marcus&Millichap Services, Bureau of Labor Statistics, Austin Investor Interests LLC, Austin Board of Realtors.