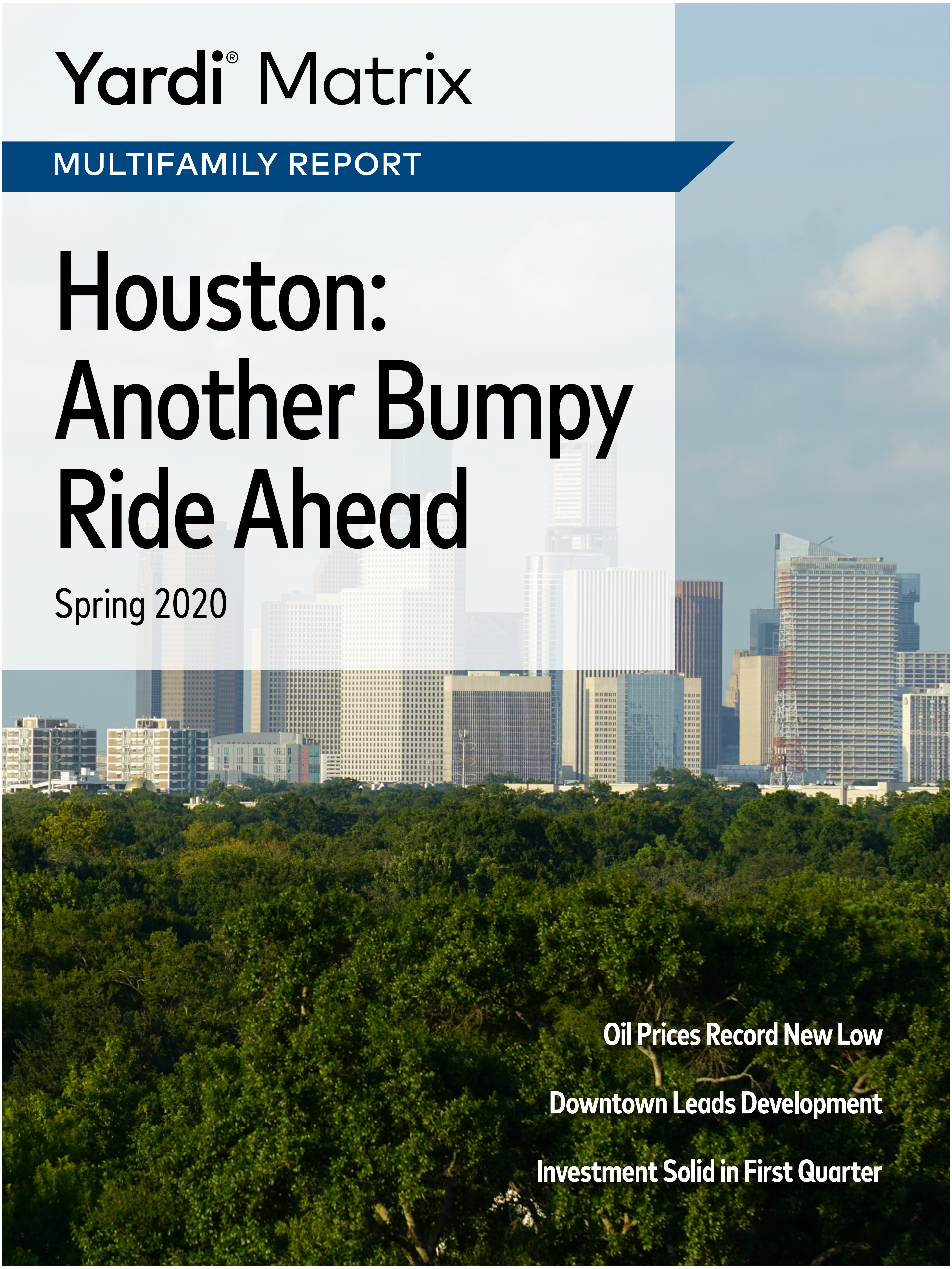
Yardi® Matrix

MULTIFAMILY REPORT

Houston: Another Bumpy Ride Ahead

Spring 2020



Oil Prices Record New Low

Downtown Leads Development

Investment Solid in First Quarter

HOUSTON MULTIFAMILY

Yardi® Matrix

Crisis Shakes Bayou City

Following several woes during the second half of this cycle, Houston's economy is facing another test. Rent growth was flat on a trailing three-month basis as of March. After COVID-19 pushed oil prices to an 18-year low, the energy sector was hit hard and many of the metro's jobs were impacted. With unemployment claims across the state skyrocketing, Houston's economy will likely continue to contract.

Last year, Houston gained 88,000 new jobs, with trade, transportation and utilities (20.3%) accounting for the largest share of the employment base. Despite job growth in the metro surpassing the 1.8% U.S. rate by 100 basis points, the statewide stay-at-home order has impacted all sectors. Although construction was deemed essential, many contractors temporarily closed their doors and supply chains were disrupted. An encouraging sign came from the Small Business Administration, which approved loans across Texas totaling nearly $22 billion—more than any other state—through April 13. The Paycheck Protection Program is a lifeline for small businesses struggling to remain open because of the health crisis.

Investor appetite remained high during the first quarter of 2020, following last year's $4.8 billion total transaction volume. The high number of completions during the past five years combined with the robust development pipeline and the effects of the pandemic will likely keep rent growth flat.

Market Analysis | Spring 2020

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Recent Houston Transactions

Greenhouse

City: Houston
Buyer: 29th Street Capital
Purchase Price: $53 MM
Price per Unit: $152,377

Jefferson Heights

City: Houston
Buyer: Kairoi Residential
Purchase Price: $37 MM
Price per Unit: $187,616

Royal Oaks at Westchase

City: Houston
Buyer: The Lynd Co.
Purchase Price: $36 MM
Price per Unit: $126,596

The Life at Clearwood

City: Houston
Buyer: Olive Tree Holdings
Purchase Price: $34 MM
Price per Unit: $122,029

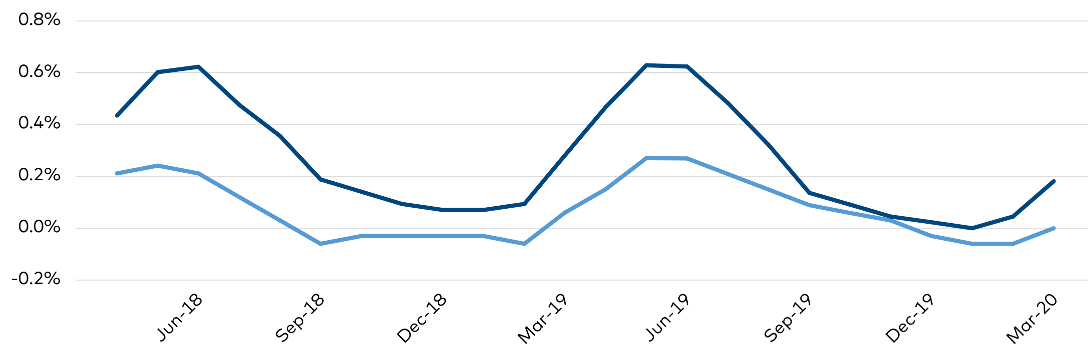
RENT TRENDS

- Rent growth in Houston was flat on a trailing three-month basis in March, lagging the 0.2% national rate. At $1,120, average rents in the metro remained well behind the $1,474 U.S. figure. March numbers don't reflect the full of impact the coronavirus on Houston's multifamily market—social distancing and the impact of the health crisis, or the oil-price drop, on employment will likely cause demand to deteriorate further, prompting rent contractions.

- In the first quarter of 2020, rent growth was led by the working-class Renter-by-Necessity segment, up by 0.1% on a trailing three-month basis to $898, while in the higher-end Lifestyle segment rent growth was negative (-0.1%). The average Lifestyle segment rent was $1,392.

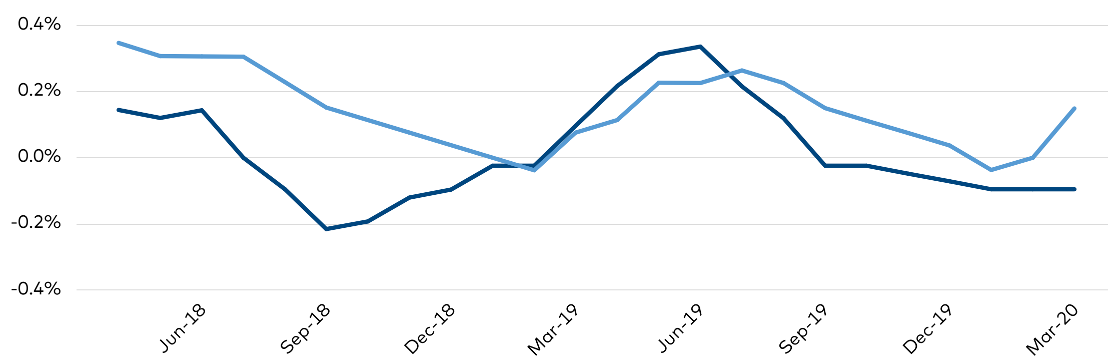
- In the past five years, Houston's multifamily market has been through a rough patch. Following the 2015-2016 energy downturn, the economy briefly rebounded—rents in the metro spiked for a short period in 2018 after Hurricane Harvey, but returned to moderate growth at the beginning of 2019. Now, the collapse in oil prices, coupled with the decline in demand caused by coronavirus shutdowns, is again pressuring the multifamily sector. However, the $2 trillion economic stimulus package—which includes direct payments to individuals and families as part of a $250 billion program—might offer a bright spot in a sea of economic uncertainty.

Houston vs. National Rent Growth (Trailing 3 Months)



Source: Yardi Matrix

Houston Rent Growth by Asset Class (Trailing 3 Months)



Source: Yardi Matrix

ECONOMIC SNAPSHOT

- Houston gained 88,000 jobs in 2019, a 2.8% year-over-year increase and 100 basis points above the U.S. rate. Following a robust year, the first quarter of 2020 was defined by economic turbulence. Aside from the damages inflicted by COVID-19, Houston was highly impacted by the collapse of oil prices, as the metro's economy remains driven, to a large degree, by energy.

- Trade, transportation and utilities (20.3%) and professional and business services (16.3%) accounted for the largest shares of employment last year. Houston-area voters approved a $3.5 billion bond issuance for transit projects, and several companies including Hewlett Packard announced expansions in the metro. Despite Houston's diversifying economy, energy companies still drive the office market, and shattering oil prices, coupled with the health crisis, will likely dent leasing and construction activity.

- Although Texas' statewide stay-at-home order exempts construction on housing, energy projects and infrastructure, Houston's workforce is expected to see significant losses. According to the Texas Workforce Commission, almost one million Texans applied for unemployment insurance in the four weeks ending on April 11, exceeding the roughly 700,000 people across the state who filed for relief in 2019.

Houston Employment Share by Sector

		Current Employment	
Code	Employment Sector	(000)	% Share
60	Professional and Business Services	527	16.3%
15	Mining, Logging, and Construction	318	9.9%
40	Trade, Transportation, and Utilities	655	20.3%
65	Education and Health Services	409	12.7%
80	Other Services	122	3.8%
30	Manufacturing	243	7.5%
70	Leisure and Hospitality	328	10.2%
90	Government	426	13.2%
55	Financial Activities	168	5.2%
50	Information	30	0.9%

Sources: Yardi Matrix, Bureau of Labor Statistics

Population

- Houston gained 91,689 residents in 2018—a 1.3% uptick and more than double the 0.6% U.S. rate, but behind other major Texas metros.

- According to the Kinder Institute for Urban Research, aging Baby Boomers are the fastest-growing segment of Houston's population.

Houston vs. National Population

	2015	2016	2017	2018
National	320,742,673	323,071,342	325,147,121	327,167,434
Houston Metro	6,676,565	6,812,260	6,905,695	6,997,384

Sources: U.S. Census, Moody's Analytics

SUPPLY

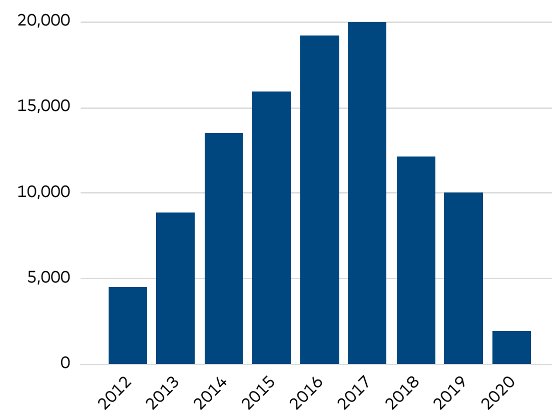
- Houston had 22,009 units under construction as of March, with more than three-quarters of these set to be delivered this year. Although Harris County authorities placed Houston under a stay-at-home order, construction was deemed an essential industry during the COVID-19 pandemic. Therefore, delays in completions are likely, but activity won't be halted.

- During the first three months of this year, 1,351 apartments came online, following the 10,062 units added last year. The number of units delivered in 2019 accounted for 1.6% of total stock, 90 basis points below the national rate.

- Developers are focusing more on building mid- and high-rise multifamily properties, a trend that signals Houston's transition to higher-density development, particularly in urban core submarkets. With 5,342 units underway as of March, the metro's West End/Downtown submarket accounted for almost one-quarter of the construction activity across the metro. Eighteen of the 19 projects underway in this Inner Loop submarket are geared toward high-income residents. The metro is an attractive option for Millennials and empty nesters, who prefer living in core walkable areas.

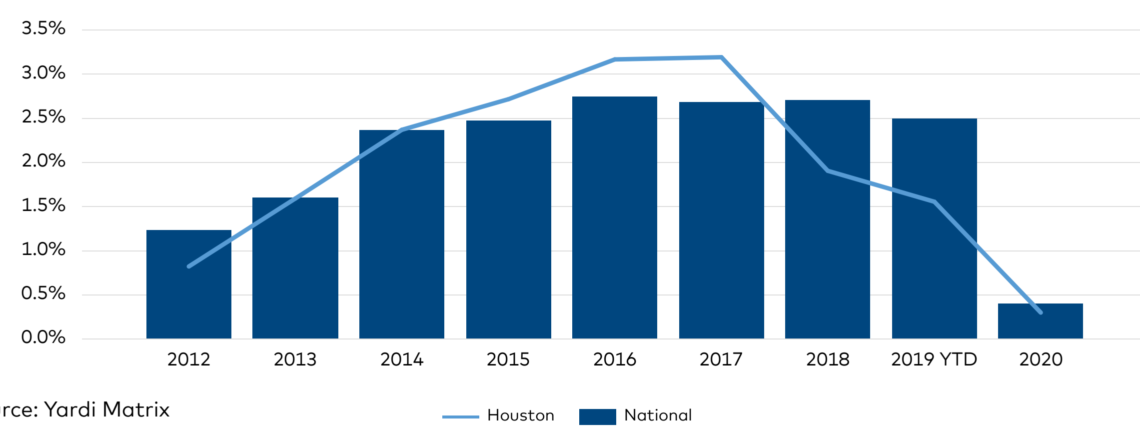
- Although core Houston submarkets led the pipeline, suburban areas also saw intense construction activity as of March. In Katy, Jersey Village/Satsuma and Louetta, there were 3,241 units combined under construction. With 384 apartments, Hines Interests' Champions Glen project ranked as one of the largest underway.

Houston Completions (as of March 2020)



Source: Yardi Matrix

Houston vs. National Completions as a Percentage of Total Stock (as of March 2020)



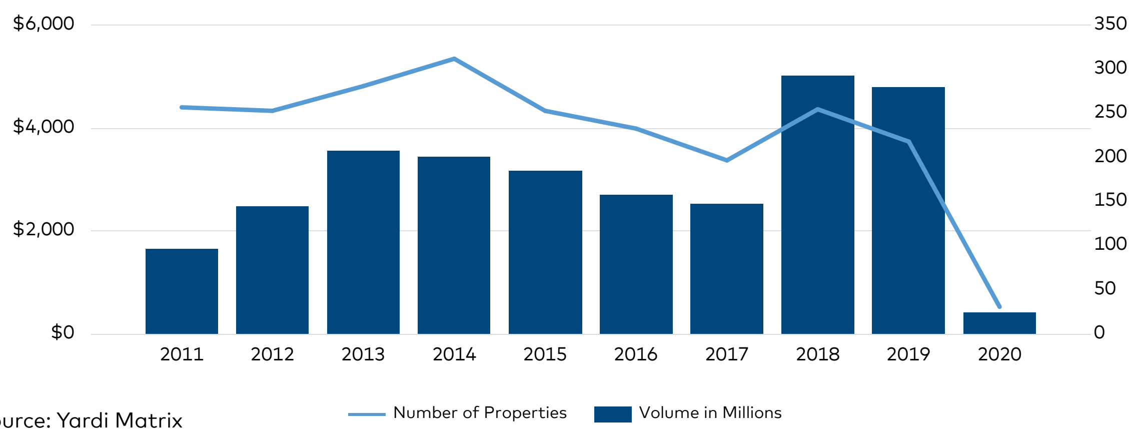
Source: Yardi Matrix

TRANSACTIONS

- Investor appetite was solid in Houston with $430 million in multifamily assets trading during the first quarter of 2020. This follows last year's $4.8 billion total transaction volume, the second highest of the cycle. In 2019, per-unit prices crossed the $120,000 mark for the first time this decade, but remained significantly below the $168,297 national average.

- With West Houston accounting for $3.5 billion of the $4.5 billion total investment volume in the 12 months ending in March, this part of the metro remained the most coveted. Eight of the top 10 submarkets for transaction volume were in West Houston, with West Bellaire ($495 million) leading the way. Investors eyed both Lifestyle and Renter-by-Necessity assets, with a slight preference for high-end products. Madera Cos. paid a combined $183 million for three Class A communities totaling 1,263 units.

Houston Sales Volume and Number of Properties Sold (as of March 2020)



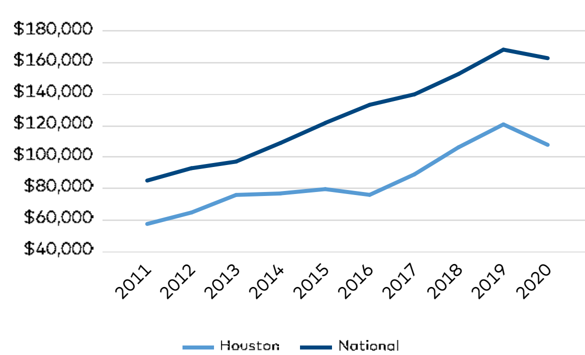
Source: Yardi Matrix

Top Submarkets for Transaction Volume[1]

Submarket	Volume ($MM)
West Bellaire	495
Jersey Village/Salsuma	356
Addicks	295
Nassau Bay/Seabrook	274
Bammel	260
The Woodlands	218
Spring Valley	214

Source: Yardi Matrix
[1] From April 2019 to March 2020

Houston vs. National Sales Price per Unit



Source: Yardi Matrix

Laneways Midtown: A Growth Story From the South

By Alexandra Pacurar

Inspired by Melbourne's local culture and eclectic vibe, Laneways Midtown in Houston is Australian developer Caydon's first U.S. project. The 27-story high-rise, only half a mile from downtown, was designed and built around the idea of wellness and life's must-haves. In an interview with *Multi-Housing News*, Caydon Principal & CEO Joe Russo talks about the company's first American venture and how it encapsulates concepts such as progressive living.

Why did you choose Houston for your first U.S. project?

When I came to the U.S., I instantly had a good feeling about Houston. I loved the city's diversity and vibrant community from every corner of the globe. From a business standpoint, the city had a strong appeal—it has a rapidly growing population, a booming economy, strong employment growth and has attracted 22 of the top Fortune 500 companies.

Houston also reminded me a lot of the culture and livability in Melbourne, Australia. My team and I saw great potential in the Midtown area, as it is located between two large employment hubs—the world's largest medical center and downtown Houston—and the premier green space, Midtown Park.

In addition to Drewery Place and the Kimpton Hotel, what will Laneways offer?

In addition to the Kimpton Hotel, the full development will include multifamily properties, a high-rise

condominium, ground-floor retail, and art and outdoor spaces.

How is the wellness theme manifested in Laneways?

Caydon takes pride in creating dynamic projects that encourage a sense of community, and support people's health, happiness and well-being. One of the reasons we were drawn to Midtown was that it is Houston's only truly walkable neighborhood, and we have designed Laneways to ensure it complements the community and premier green neighbors—Midtown Park and Whole Foods. Laneways will become a destination where residents, community members and their pets will enjoy a 360-degree active lifestyle with walkable alleyways, green spaces for outdoor fitness programs, health-centric amenities, tech-savvy homes and more.

How does tech fit into all of this?

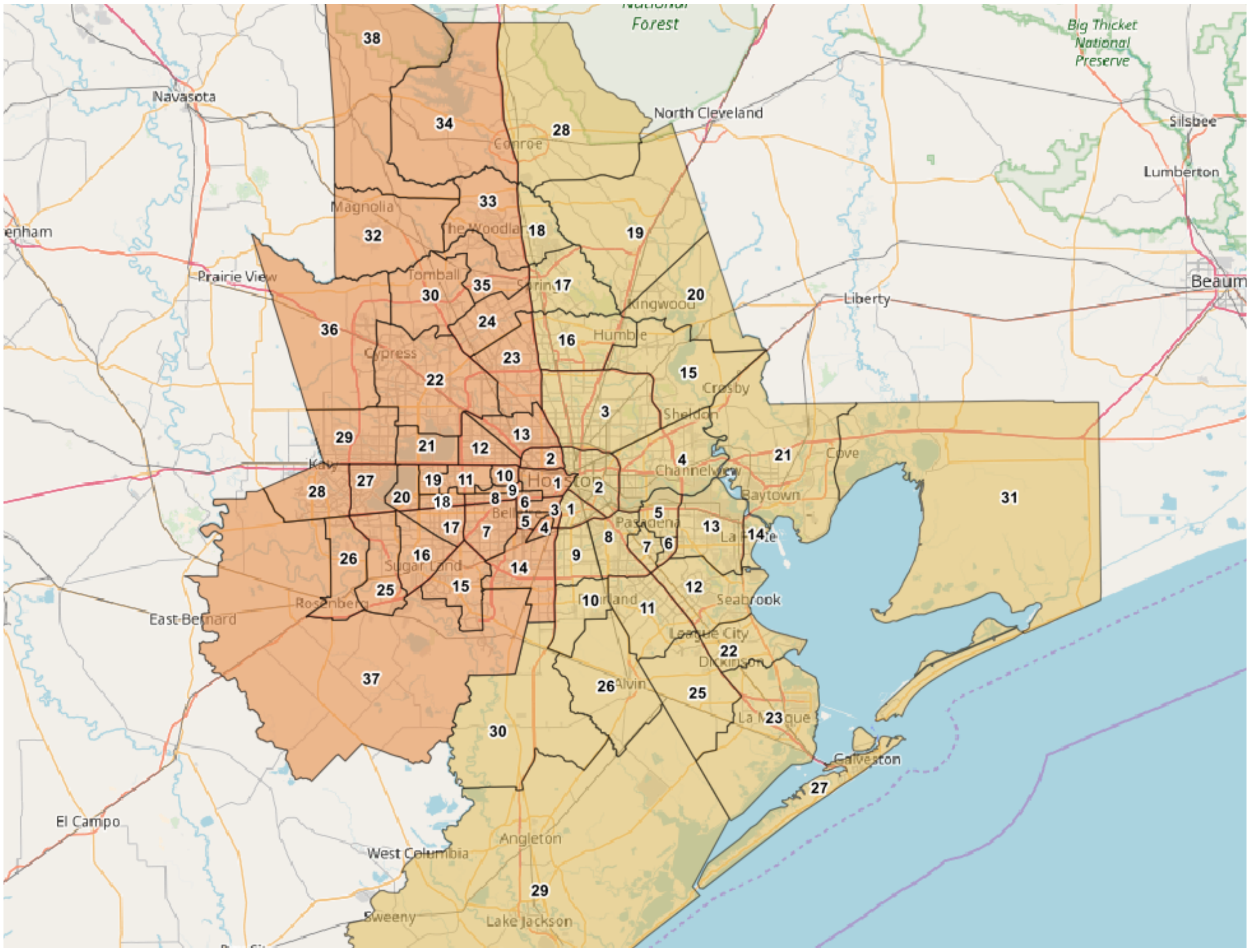
The 27-story is one of the only developments in Houston that offers endless tech-savvy features, including scene programmable lighting, smart Honeywell thermostats, latch Bluetooth-enabled door hardware and IT consultants to set up new tenants.

What can you tell us about financing such a project?

Drewery Place is a $200 million residential tower. Caydon worked with HFF to secure debt and equity financing for Drewery Place through Bank of the Ozarks and Invesco Real Estate.

(Read the complete interview on multihousingnews.com.)

HOUSTON SUBMARKETS



Area No.	Submarket
1	West End/Downtown
2	The Heights
3	Museum District
4	Reliant Park
5	Bellaire
6	River Oaks
7	West Bellaire
8	Piney Point Village–South
9	Piney Point Village–North
10	Hunters Creek
11	Bunker Hill Village
12	Spring Valley
13	Rosslyn
14	Missouri City
15	Suger Land–South
16	Sugar Land–West
17	Suger Land–North
18	Royal Oaks Country Club
19	Addicks

Area No.	Submarket
20	George Bush Park
21	Bear Creek Park
22	Jersey Village/Satsuma
23	Bammel
24	Louetta
25	Richmond
26	Rosenberg
27	Cinco Ranch–South
28	Katy
29	Cinco Ranch–North
30	Tomball
32	Magnolia
33	The Woodlands
34	Conroe–West
35	Avonak
36	Northwest Harris County
37	Outlying Fort Bend County
38	West Montgomery County

Area No.	Submarket
1	Greater Third Ward
2	East End
3	Mount Houston
4	Cloverleaf
5	Pasadena
6	South Houston Crenshaw Park
7	South Houston
8	William P. Hobby Airport
9	Pierce Junction
10	Clear Creek
11	Pearland/Friendswood
12	Nassau Bay/Seabrook
13	Deer Park
14	La Porte
15	Atascocita
16	Humble/Westfield

Area No.	Submarket
17	Spring
18	The Woodlands–East
19	Porter
20	Kingwood
21	Baytown
22	League City/Dickenson
23	Texas City
25	League City–West
26	Alvin
27	Galveston
28	Conroe–East
29	Lake Jackson/Angleton
30	Northwest Brazoria County
31	Outlying Chambers County

DEFINITIONS

Lifestyle households (renters by choice) have wealth sufficient to own but have chosen to rent. Discretionary households, most typically a retired couple or single professional, have chosen the flexibility associated with renting over the obligations of ownership.

Renter-by-Necessity households span a range. In descending order, household types can be:

- *A young-professional*, double-income-no-kids household with substantial income but without wealth needed to acquire a home or condominium;
- *Students,* who also may span a range of income capability, extending from affluent to barely getting by;
- *Lower-middle-income ("gray-collar") households,* composed of office workers, policemen, firemen, technical workers, teachers, etc.;
- *Blue-collar households,* which may barely meet rent demands each month and likely pay a disproportionate share of their income toward rent;
- *Subsidized households*, which pay a percentage of household income in rent, with the balance of rent paid through a governmental agency subsidy. Subsidized households, while typically low income, may extend to middle-income households in some high-cost markets, such as New York City;
- *Military households*, subject to frequency of relocation.

These differences can weigh heavily in determining a property's ability to attract specific renter market segments. The five-star resort serves a very different market than the down-and-outer motel. Apartments are distinguished similarly, but distinctions are often not clearly definitive without investigation. The Yardi® Matrix Context rating eliminates that requirement, designating property market positions as:

Market Position	Improvements Ratings
Discretionary	A+ / A
High Mid-Range	A- / B+
Low Mid-Range	B / B-
Workforce	C+ / C / C- / D

The value in application of the Yardi® Matrix Context rating is that standardized data provides consistency; information is more meaningful because there is less uncertainty. The user can move faster and more efficiently, with more accurate end results.

The Yardi® Matrix Context rating is not intended as a final word concerning a property's status—either improvements or location. Rather, the result provides reasonable consistency for comparing one property with another through reference to a consistently applied standard.

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