Yardi® Matrix

Houston Surmounts the Storm

Multifamily Report Winter 2019

Apartment Rents Inch Up

Transaction Volume Hits Cycle High

Employment Growth Outpaces U.S. Rate

Market Analysis
Winter 2019

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Bayou City Deliveries Hit the Brakes

The Houston multifamily market is back on top following Hurricane Harvey and the oil price drop. Strong demographic expansion and above-trend employment growth have been supporting demand.

The Category 4 Atlantic storm hit Houston in mid-2017 and accelerated a market that was already fighting to surpass its 2015-16 energy-related slump. The metro added 128,700 jobs in the 12 months ending in September, with mining, logging and construction accounting for more than a quarter of gains. Professional and business services and trade, transportation and utilities added 51,000 jobs combined. One of the largest infrastructure projects is the $815 million investment in State Highway 288, a critical north-south transit corridor. Thousands of workers are also on site at the $1.1 billion McNair medical campus, slated for completion in 2019. Moreover, roughly $4.5 billion in local and federal funds will be put into critical flood control projects, further boosting construction.

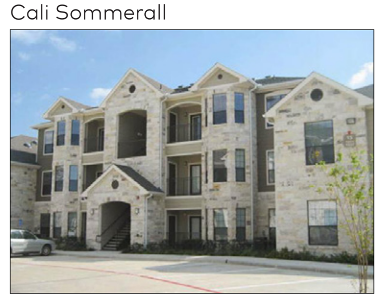
Interest in local assets—particularly in value-add properties—has been strong, with $4.5 billion in apartments having traded in the first 10 months of 2018. Following record delivery rates of more than 38,000 units in 2016 and 2017 combined, another 8,827 apartments were completed year-to-date through November, inhibiting rent growth.

Recent Houston Transactions

Baybrook Village

City: Webster, Texas
Buyer: Investcorp
Purchase Price: $51 MM
Price per Unit: $66,230

Cali Sommerall

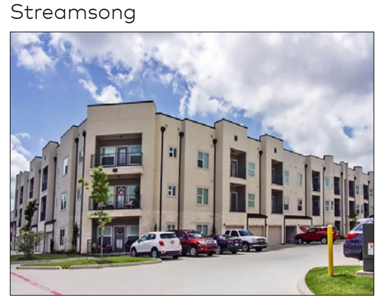


City: Houston
Buyer: 29th Street Capital
Purchase Price: $37 MM
Price per Unit: $101,507

Thornbury

City: Houston
Buyer: InterCapital Partners
Purchase Price: $46 MM
Price per Unit: $113,225

Streamsong



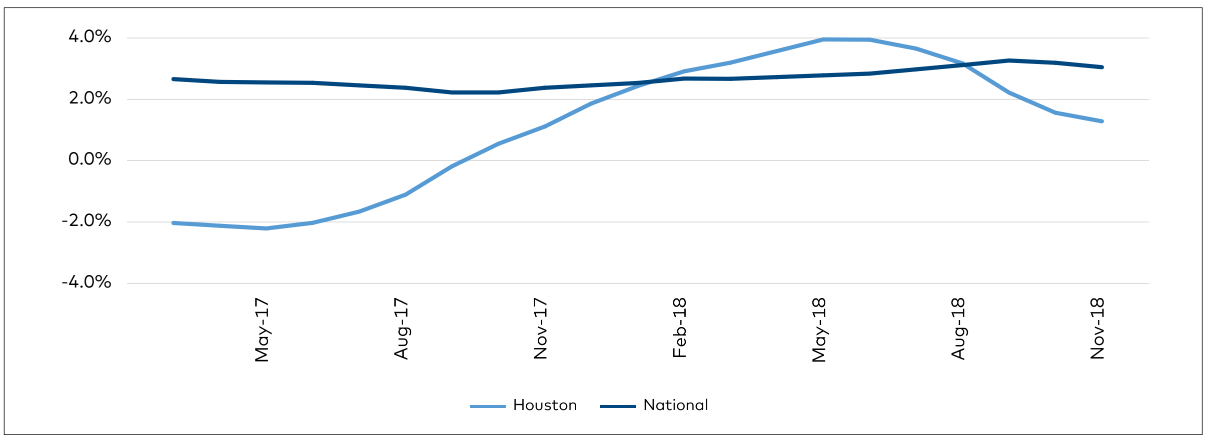
City: Katy, Texas
Buyer: Angelo Gordon & Co.
Purchase Price: $43MM
Price per Unit: $142,311

On the cover: Photo by Sean Pavone/iStockphoto.com

Rent Trends

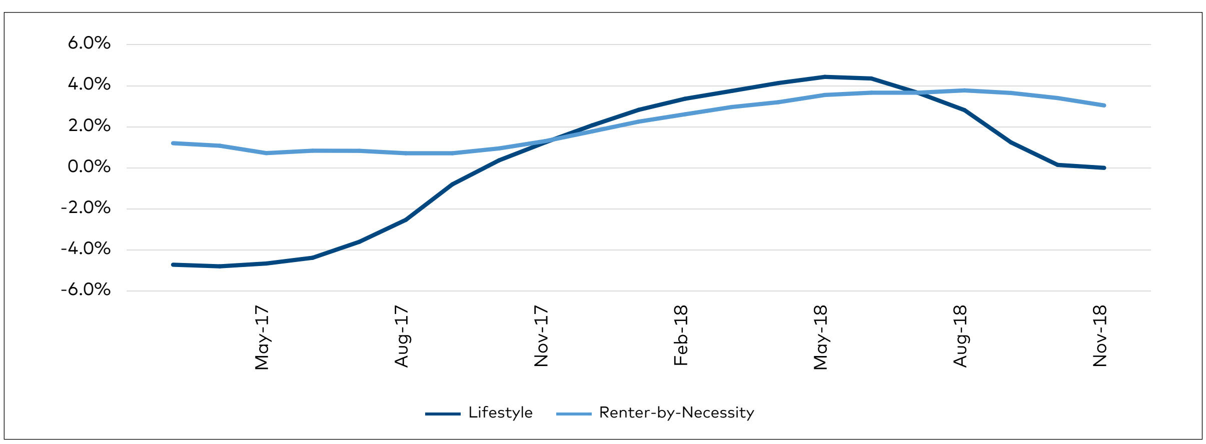
- Rents in Houston rose 1.3% in the year ending in November, severely lagging the 3.1% national rate. The metro's average rent stood at $1,103, well below the $1,419 U.S. figure. Occupancy in stabilized properties decreased by 30 basis points year-over-year through October, to 93.3%, as the completion of more than 47,000 units since the beginning of 2016 through November has put serious strain on absorption.
- Growth was led by the working-class Renter-by-Necessity segment, which consolidated and rose 3.0% year-over-year through November, to $880. Rent growth in the higher-end segment was flat, mostly because of the heavy Lifestyle supply delivered during the past two years. Demand for workforce apartments is on the rise, but the bulk of upcoming supply is geared toward market-rate renters, so rents in the RBN segment are not likely to increase significantly in the year ahead.
- Eastern Houston submarkets such as League City–West (6.7% to $1,109) and The Woodlands–East (5.9% to $1,120) saw the strongest year-over-year hikes. However, core urban areas in the Western part of the city remained the most expensive in the metro, with rents hitting $1,947 in the Museum District and $1,838 in West End/Downtown. Demand is driven by rapid employment growth and development has responded accordingly. Rent growth should remain tepid, at least during the first quarter of 2019.

Houston vs. National Rent Growth (Sequential 3 Month, Year-Over-Year)



Source: YardiMatrix

Houston Rent Growth by Asset Class (Sequential 3 Month, Year-Over-Year)



Source: YardiMatrix

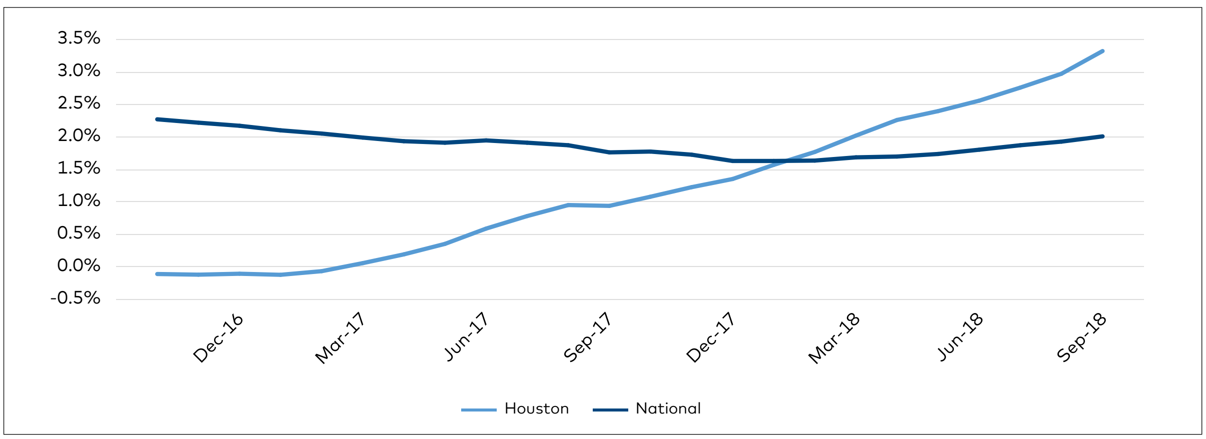
Economic Snapshot

- The metro is once more among the country's top cities for employment growth, with Houston having added a record 128,700 jobs in the year ending in September, a 3.3% increase and 130 basis points above the national rate. The employment numbers include the months in which the Hurricane Harvey reconstruction efforts propelled the local economy.

- Professional and business services and mining, logging and construction drove growth, with approximately 66,000 jobs added year-over-year through September. The Texas Department of Transportation is spending $815 million to design and construct expansive new interchanges and toll lanes along a 61-mile state highway between Houston and the Gulf of Mexico. Development is also underway in northeast Houston, with a 4,000-acre project adding building after building. Anchored by Fortune 500 oil-and-gas company TechnipFMC's 173-acre campus and its 1 million-square-foot first phase, McCord's Generation Park continues to act as a catalyst for the Lake Houston area.

- The three devastating calamities that hit the metro in as many years have driven authorities to make the largest investment in flood protection in Harris County's history. A $2.5 billion bond for flood-control projects passed in August, and Texas officials will get another $2 billion in federal funds as part of the $6 billion water infrastructure projects authorized by the U.S. government in October.

Houston vs. National Employment Growth (Year-Over-Year)



Sources: YardiMatrix, Bureau of Labor Statistics (not seasonally adjusted)

Houston Employment Growth by Sector (Year-Over-Year)

		Current Employment		Year Change	
Code	Employment Sector	(000)	% Share	Employment	%
60	Professional and Business Services	518	16.5%	33,200	6.8%
15	Mining, Logging and Construction	325	10.4%	32,500	11.1%
40	Trade, Transportation and Utilities	628	20.0%	17,800	2.9%
30	Manufacturing	233	7.4%	11,800	5.3%
70	Leisure and Hospitality	323	10.3%	10,900	3.5%
65	Education and Health Services	394	12.6%	10,800	2.8%
55	Financial Activities	164	5.2%	4,900	3.1%
80	Other Services	113	3.6%	4,600	4.2%
90	Government	406	12.9%	2,600	0.6%
50	Information	31	1.0%	-400	-1.3%

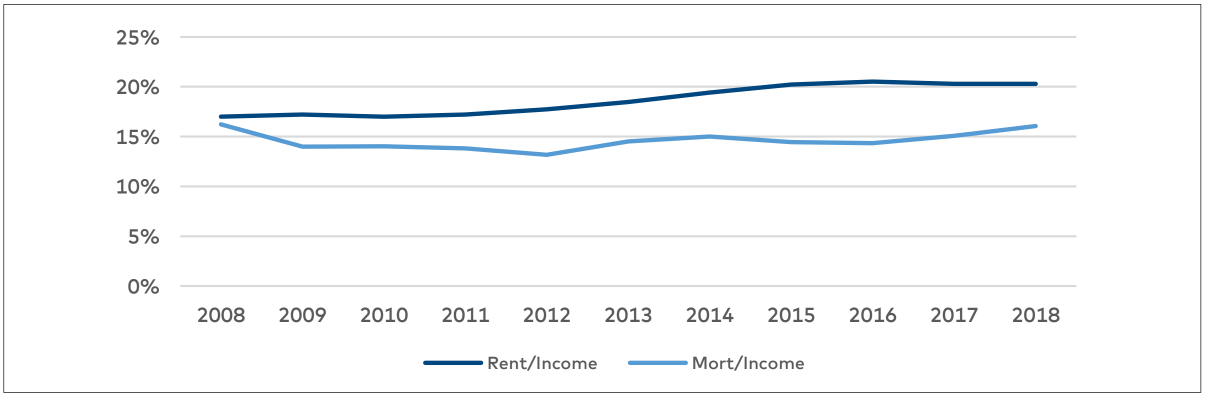
Sources: YardiMatrix, Bureau of Labor Statistics

Demographics

Affordability

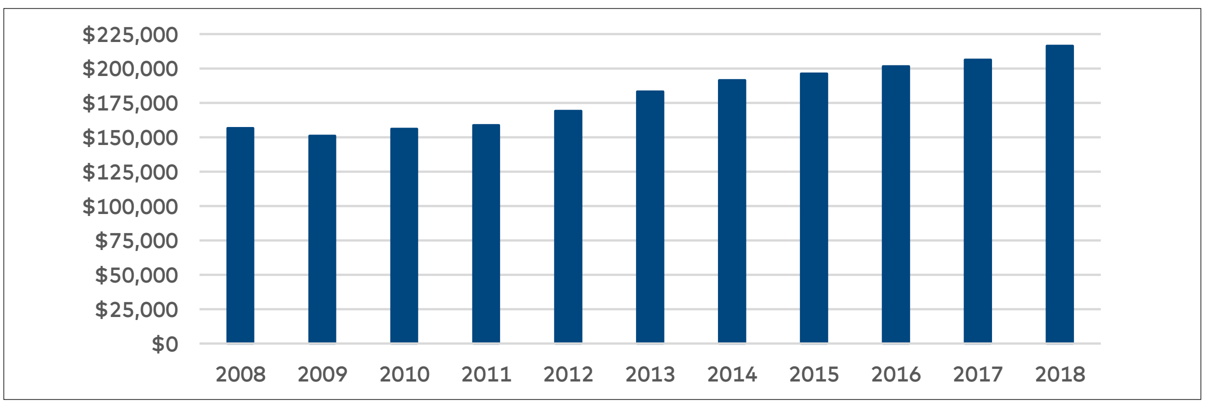
- The median home price in Houston peaked in 2018 at $216,422, up 4.9% over 2017. At a monthly rate of $1,103, renting has remained the more expensive option, accounting for 20% of the area's median income. The average mortgage payment comprised just 16%.
- Houston's rise as a strong job hub has generated steady population gains, putting pressure on workforce housing. Despite significant supply delivered in recent years, rents in the Renter-by-Necessity segment kept increasing. However, Houston is one of the most affordable major metros, according to a Council for Community and Economic Research report.

Houston Rent vs. Own Affordability as a Percentage of Income



Sources: YardiMatrix, Moody's Analytics

Houston Median Home Price



Source: Moody's Analytics

Population

- Houston's population rose 1.4% last year, 70 basis points above the national average. The metro added almost 95,000 residents.
- Since 2010, Houston has added roughly 945,000 residents, a 15.9% uptick.

Houston vs. National Population

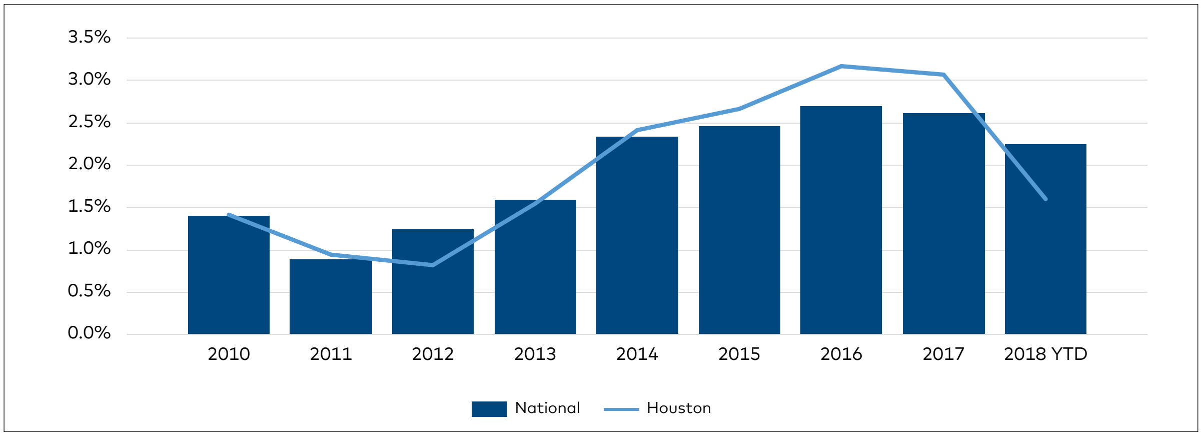
	2013	2014	2015	2016	2017
National	316,234,505	318,622,525	321,039,839	323,405,935	325,719,178
Houston Metro	6,329,553	6,496,862	6,664,187	6,798,010	6,892,427

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

Supply

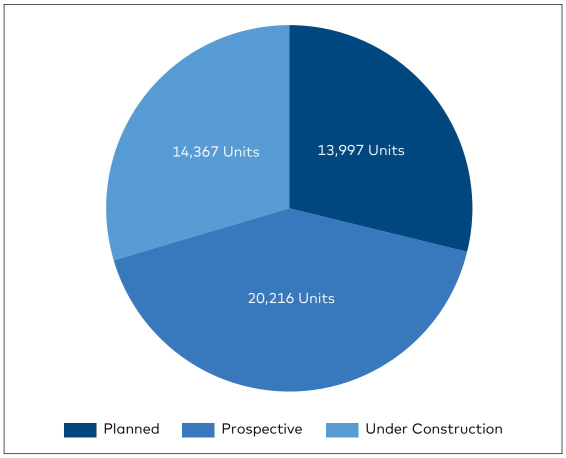
- During the first 11 months of 2018, Houston added 8,827 units, less than half of the units it added in 2017. Construction slowed down following a two-year period when 38,000 units were delivered. Although the market's needs were significantly changed due to the effects of Hurricane Harvey, rebounding rent growth and strong absorption are slowing, as overbuilding is once again an issue.
- As of November, the metro had 14,367 units under construction and 34,000 units in the planning and permitting stages. West End/Downtown led multifamily development with 3,687 units underway, accounting for roughly a quarter of the pipeline. All properties under construction in this submarket are earmarked for the Lifestyle segment, even at a time when the spread between upscale and Renter-by-Necessity rent growth is only increasing. However, the cost effectiveness of high-end properties still overwhelmingly attracts developers.
- The Pointe at Valley Ranch Town Center was the largest property underway as of November. The 550-unit project built by Signorelli Co. is the first of six projects that the company plans to develop within the 240-acre Valley Ranch Town Center, one of the largest mixed-use developments underway in Texas.

Houston vs. National Completions as a Percentage of Total Stock (as of November 2018)



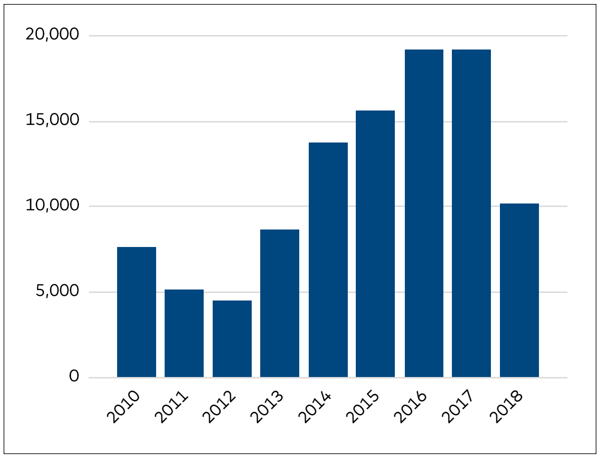
Source: YardiMatrix

Development Pipeline (as of November 2018)



Source: YardiMatrix

Houston Completions (as of November 2018)

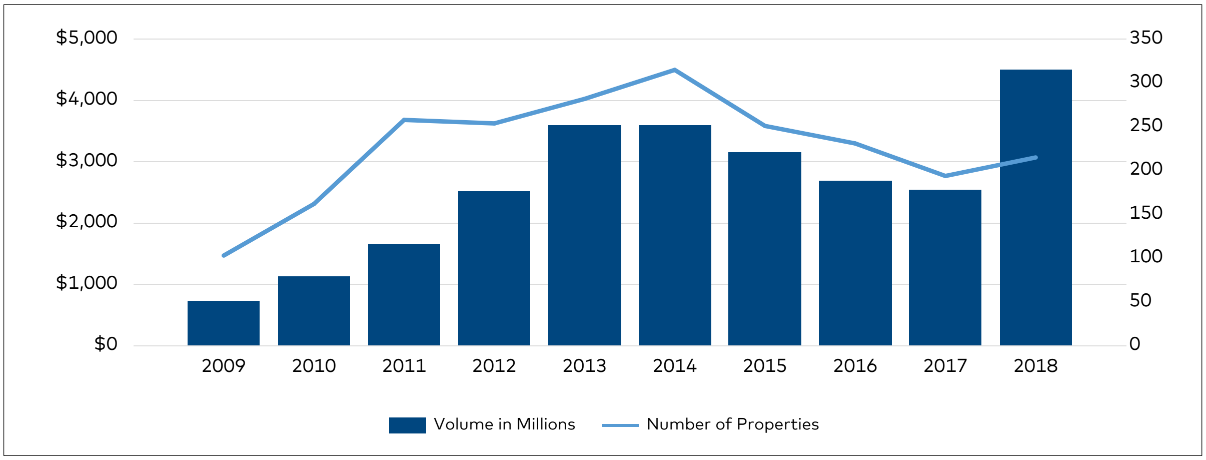


Source: YardiMatrix

Transactions

- With $4.5 billion in multifamily assets trading in the first 10 months of 2018, transaction volume hit a new cycle high. Investment activity has accelerated significantly over the past three years, with investors mostly eyeing Renter-by-Necessity communities with value-add appeal. Local job creation and steady in-migration should continue to positively impact Houston's rental market.
- Acquisition yields for stabilized Class A properties were in the 5% range and between 5.0% and 5.5% for Class B properties.
- Western submarkets—such as Jersey Village/Salsuma ($399 million), Bammel ($277 million) and Royal Oaks Country Club ($261 million)—were the most sought after in the year ending in October. FPA Multifamily and Nitya Capital invested more than $210 million each in Houston properties.

Houston Sales Volume and Number of Properties Sold (as of October 2018)



Source: YardiMatrix

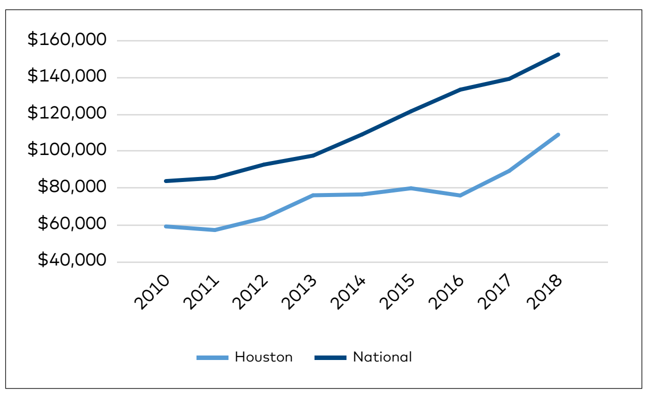
Top Submarkets for Transaction Volume[1]

Submarket	Volume ($MM)
Jersey Village/ Salsuma	399
Bammel	277
Royal Oaks Country Club	261
River Oaks	252
Piney Point Village–South	248
Spring Valley	222
Louetta	206
West End/Downtown	197

Source: YardiMatrix

[1] From November 2017 to October 2018

Houston vs. National Sales Price per Unit



Source: YardiMatrix

News in the Metro

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C&W Facilitates Houston Portfolio Sale

Justin Shuart and Jason Pumpelly from the company's equity, debt and structured finance team in Dallas arranged the deal on behalf of Nicholas Residential.

JV Purchases 2 Houston Communities

Greybrook Realty Partners and Marlin Spring Investments paid $68 million for the garden-style properties in the city's Romano Woods neighborhood.

Olympus Property Buys Houston-Area Community

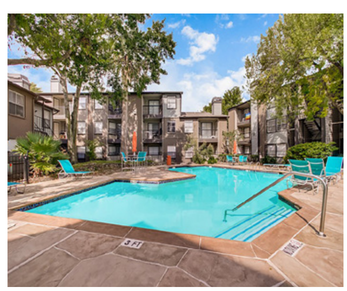
The company has renamed the 341-unit property Olympus Sierra Pines. Built in 2014, the asset is part of the Woodlands master-planned community.

Investcorp Acquires $311M Multifamily Portfolio

The properties, totaling 2,876 units, include three communities in Houston, two in Tampa and one in Salt Lake City. With the inclusion of this portfolio, the firm now owns 13,000 units across the country.

29SC Expands Houston Presence With Value-Add Asset

The privately held firm plans to invest more than $2 million in capital improvements in the 17-building community located 23 miles northwest of downtown Houston.



ClearWorth Capital Buys Houston Community

HFF marketed The Edge at City Centre on behalf of the seller, 29th Street Capital, which invested around $2.6 million to rebrand, renovate and reposition the asset.

Executive Insight

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MULTI-HOUSING NEWS

Soaking Up Opportunities in the Sunbelt

By Keith Loria

American Landmark Apartments specializes in the acquisition, repositioning and management of multifamily communities, mostly in the Sunbelt region, where there's strong population and job growth. Last fall, the company acquired Haven at Liberty Hills, a Class A community in Houston. That same month, ALA and its debt and equity partner, Electra America, purchased Hilltops Apartments, a 208-unit community located 40 miles north of downtown Houston, in Conroe. CEO Joe Lubeck reveals his company's investment strategy and what he sees stoking the hot Southern secondary markets.

What are the trends you've seen in the multifamily investor market in 2018?

In many ways, it's a continuation of trends we've seen unfold over the past several years. First, on the demand side, there's been a real shift away from traditional homeownership. More people are renting today than ever before, and as a result, rents are rising. With this dynamic, we're continuing to see more players entering the value-add multifamily space in secondary market locations.

Our country's strong job growth supports the value-add proposition, so the field has become even more crowded. Still, we believe there are opportunities out there. Core-plus is becoming as attractive as—if not more attractive than—value-add opportunities at this stage in the cycle.

What's happening in the sectors you follow? What's on your radar and why?

We continue to look at job growth in and around Southern secondary

market areas like Houston and Orlando. Rising interest rates are obviously on our radar, but it's not impacting our deals so much because rates are still relatively low and there are a lot of different sources of capital. One thing we are seeing right now is that builders are overextended, which obviously has an impact on value-add players who, like us, complete in-place renovations in a compressed period of time.

What are the locations you are most interested in?

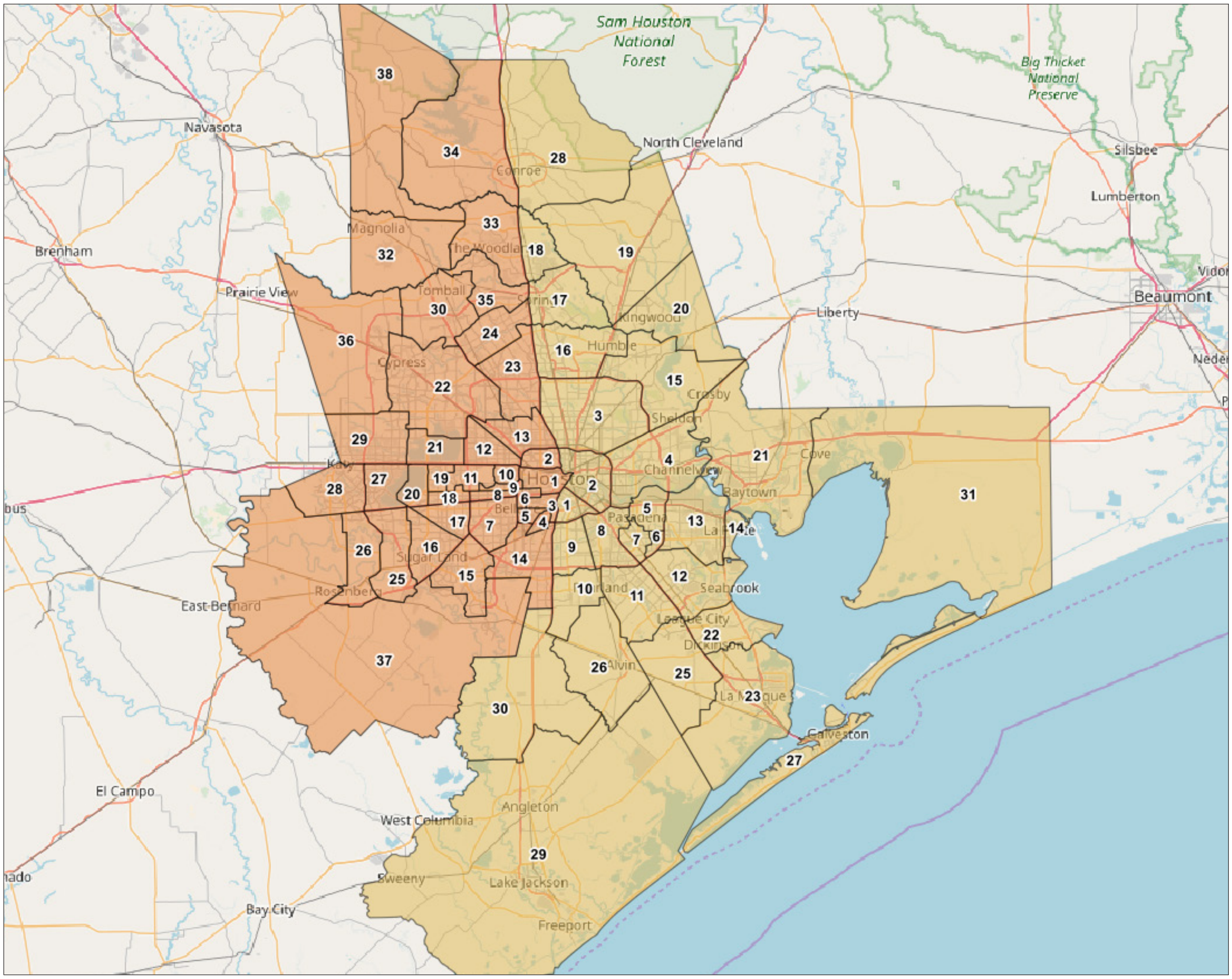
We're investing heavily in metro areas such as Charlotte, N.C.; Orlando, Fla.; Atlanta; Houston; and San Antonio. In 2017, we were probably one of the largest buyers in the country.

What's your key to planning a successful strategy?

There's product, process and service. On the product side, we focus on well-located, nicely built properties in high job-growth areas. All of our properties have to meet certain criteria. On the process side, we have a very fine-tuned repositioning approach to meet the demands of today's renters. This usually entails adding new flooring, stainless steel kitchen appliances and, sometimes, washers and dryers—but we also invest a lot in amenities.

Our communities have 24-hour state-of-the-art fitness centers, Wi-Fi cafes, dog parks, package delivery rooms, and tennis or volleyball courts, for example. Lastly, we deliver exceptional customer service. Our management professionals are hands down the most well trained in the industry, and that's critical in today's market to attract and retain residents.

Houston Submarkets



Area #	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
20	George Bush Park

Area #	Submarket
21	Bear Creek Park
22	Jersey Village/Salsuma
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 #	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 #	Submarket
17	Spring
18	The Woodlands–East
19	Porter
20	Kingwood
21	Baytown
22	League City/Dickenson
23	Texas City/San Leon
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.

To learn more about Yardi® Matrix and subscribing, please visit www.yardimatrix.com or call Ron Brock, Jr., at 480-663-1149 x2404.