Yardi® Matrix

Steady Chicago

Multifamily Report Winter 2019

Rent Growth Hits 2-Year High

Upcoming Deliveries Target City Core

Per-Unit Prices Reach New Peak

Market Analysis

Winter 2019

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Rent Growth Advances Further

Chicago rent growth accelerated in 2018, reaching 2.5% as of November—the highest value of the last two years—due to a relatively healthy employment environment and a slowdown in deliveries. The rebound of Lifestyle rent growth has also contributed to the rise, as Millennials continue to move into well-located, modern apartments that facilitate easy access to employment and entertainment options.

The metro added 35,000 jobs in the 12 months ending in September, further fueling housing demand. Construction and manufacturing led gains due to a robust development pipeline and a ballooning e-commerce sector. The city is strengthening its emerging tech hub status, with companies such as Salesforce, Pinterest, Google and Facebook relocating or expanding their downtown footprint. Salesforce is slated to create 1,000 new jobs once it settles into its new base, a 57-story tower on the north bank of the river.

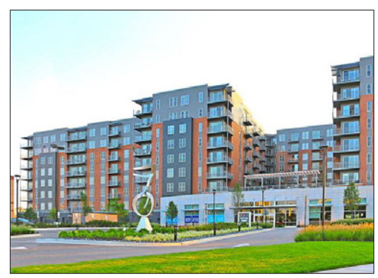
Development remained relatively strong, with 5,400 units delivered in 2018 through November, but overall healthy fundamentals should maintain steady absorption. Occupancy in stabilized assets dropped just 20 basis points over 12 months, reaching 94.6% as of October. Considering the supply-demand balance, we expect rents to continue advancing at a slow but steady rate in the foreseeable future.

Recent Chicago Transactions

ReNew Wheaton Center

City: Wheaton, Ill.
Buyer: FPA Multifamily
Purchase Price: $131 MM
Price per Unit: $172,823

TGM NorthShore



City: Northbrook, Ill.
Buyer: TGM Associates
Purchase Price: $118 MM
Price per Unit: $340,058

The Mil'Ton

City: Vernon Hills, Ill.
Buyer: Mesirow Financial
Purchase Price: $87 MM
Price per Unit: $296,259

Arc at Old Colony

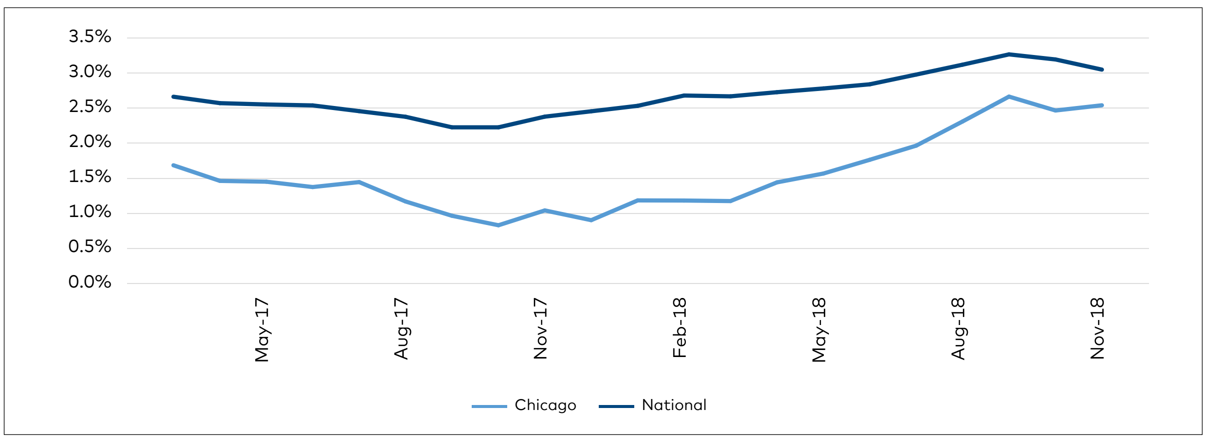
City: Chicago
Buyer: Deutsche Asset & Wealth Management
Purchase Price: $77 MM
Price per Unit: $560,584

On the cover: Photo by Timothy Wang/iStockphoto.com

Rent Trends

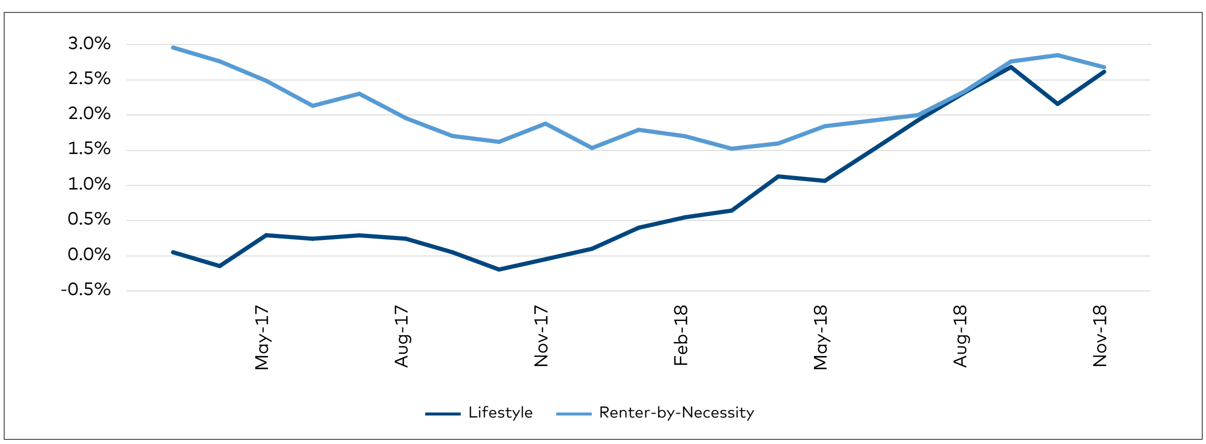
- Chicago rents were up 2.5% year-over-year as of November, 60 basis points below the U.S. rate of growth. The average rent peaked at $1,493, above the $1,419 nationwide average. With the pace of deliveries slowing down, rent growth picked up notably in the second half of 2018, reaching its fastest pace of the last two years.
- The metro's tech environment is attracting talented professionals looking for modern urban housing in central areas. Increasing demand has led to a jump in rent growth for Lifestyle units, from rate contractions in the last quarter of 2017 to a 2.6% growth as of November, with the average rate reaching $2,079. Rents in the working-class Renter-by-Necessity segment were up 2.7%, to $1,225.
- Growth was spotty across the map, with rents contracting in several submarkets, including Skokie (-1.5%), Berwyn (-1.4%), Evanston–South (-1.2%), Schaumburg (-0.8%) and Oak Park (-0.8%). Growth was mainly led by suburban assets, with Grayslake (up 11.3% to $1,198) and Chicago Heights–North (up 7.3% to $1,046) recording some of the strongest rent hikes. Core submarkets that provide easy access to employers, entertainment and leisure facilities command the highest rents. The least affordable areas as of November were the Loop ($2,499), the Near North Side ($2,391), West Town–Garfield Park ($2,262), the Near West Side ($2,204) and Evanston–North ($2,168).

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



Source: YardiMatrix

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

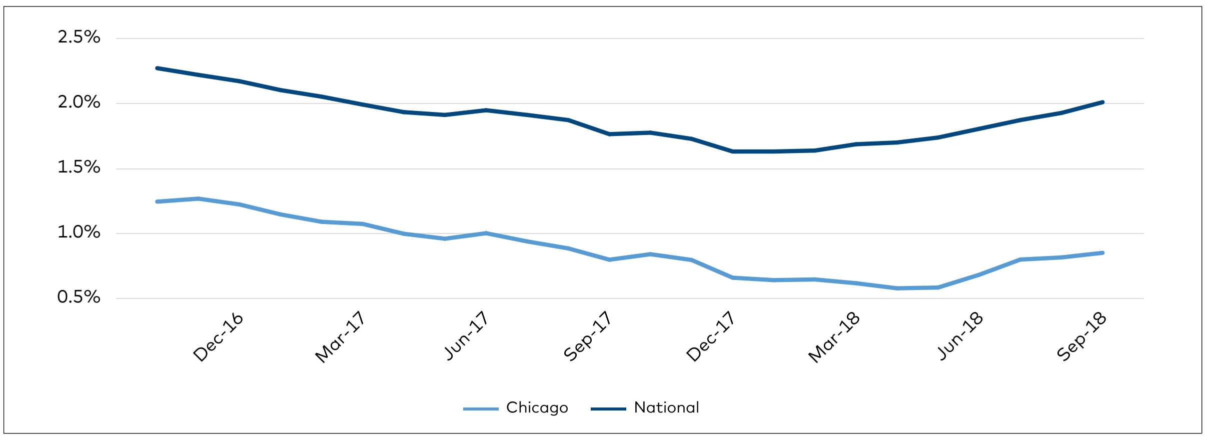


Source: YardiMatrix

Economic Snapshot

- Chicago added 35,000 jobs in the 12 months ending in September for a 0.9% expansion, lagging the 2.0% national figure. Gains were led by construction (8,800 jobs), manufacturing (8,700), education and health services (7,500), and government (7,500). Strong development activity has led to a 4.8% increase in construction jobs, the most significant growth rate of all employment sectors.
- The metro added 3,900 jobs in the financial activities sector, and gains are expected to continue. BMO Harris plans to relocate and consolidate its headquarters in the city. The bank will occupy 14 floors in the 50-story tower near Union Station, currently underway, and will move 3,600 employees there. The property has been dubbed BMO Tower. Developers Riverside Investment & Development and Convexity Properties also plans to transform Union Station's headhouse into a 400-key hotel.
- Chicago lost a total of 7,300 jobs in the 12 months ending in September across three employment sectors, more than half of them in information. According to research by the University of Toronto School of Cities and CityLab, the total number of corporate headquarters in Chicago declined by 28% over the past four decades. However, when it comes to headquarters geography, the metro is still a national leader in retail and wholesale as well as second in consumer services and in goods and materials, after New York.

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



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

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

		Current Employment		Year Change	
Code	Employment Sector	(000)	% Share	Employment	%
15	Mining, Logging and Construction	193	4.1%	8,800	4.8%
30	Manufacturing	424	8.9%	8,700	2.1%
65	Education and Health Services	730	15.4%	7,500	1.0%
90	Government	560	11.8%	7,500	1.4%
55	Financial Activities	309	6.5%	3,900	1.3%
70	Leisure and Hospitality	491	10.3%	3,200	0.7%
60	Professional and Business Services	839	17.7%	2,700	0.3%
40	Trade, Transportation and Utilities	946	19.9%	-400	0.0%
80	Other Services	178	3.8%	-3,200	-1.8%
50	Information	74	1.6%	-3,700	-4.8%

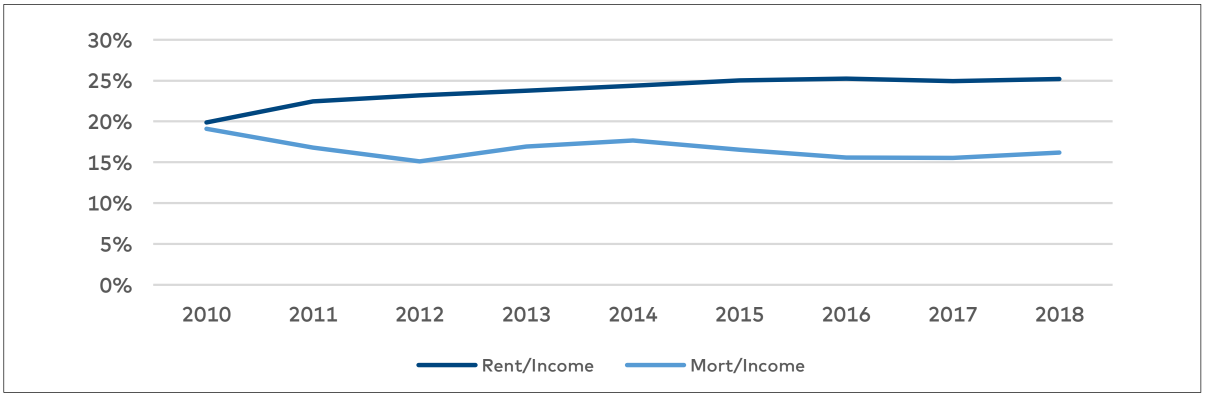
Sources: YardiMatrix, Bureau of Labor Statistics

Demographics

Affordability

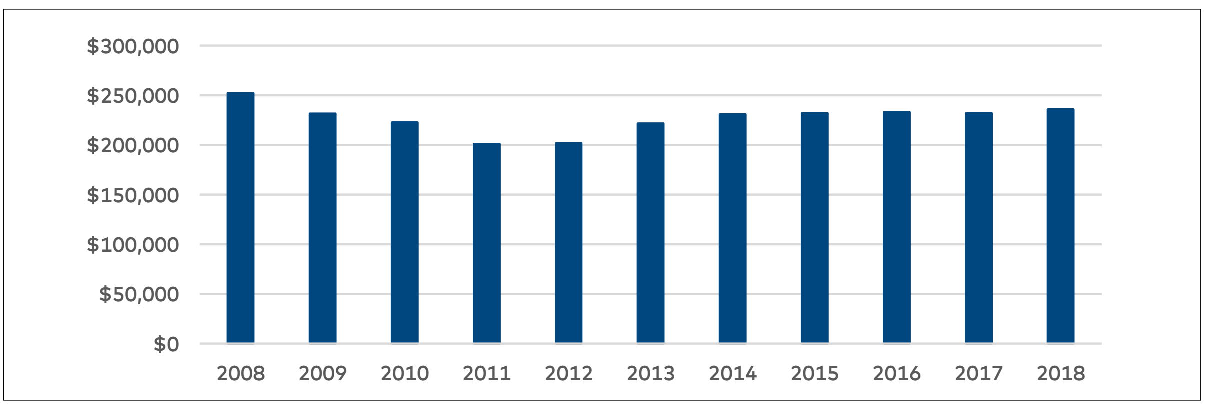
- Changing market conditions have had limited impact on the metro's affordability rates, which remained relatively flat over the past three years. The median home price in Chicago was up 2% to $235,696 in the first half of 2018, the highest value in a decade. Rising interest rates have yet to deeply affect mortgage prices, with ownership remaining the more affordable option. The average mortgage payment accounted for 16% of the area's median income, while the average rent equated to 25%.
- Chicago City Council has increased the affordable housing requirement from 10% to 20% of all units built within large-scale, market-rate developments in a 7.2-mile area including Pilsen and Little Village.

Chicago Rent vs. Own Affordability as a Percentage of Income



Sources: YardiMatrix, Moody's Analytics

Chicago Median Home Price



Source: Moody's Analytics

Population

- Chicago's population has decreased over the past four years. The metro lost 15,000 residents in 2017.
- Affordability issues are pricing residents out of Chicago, with Baby Boomers relocating mostly to southern cities.

Chicago vs. National Population

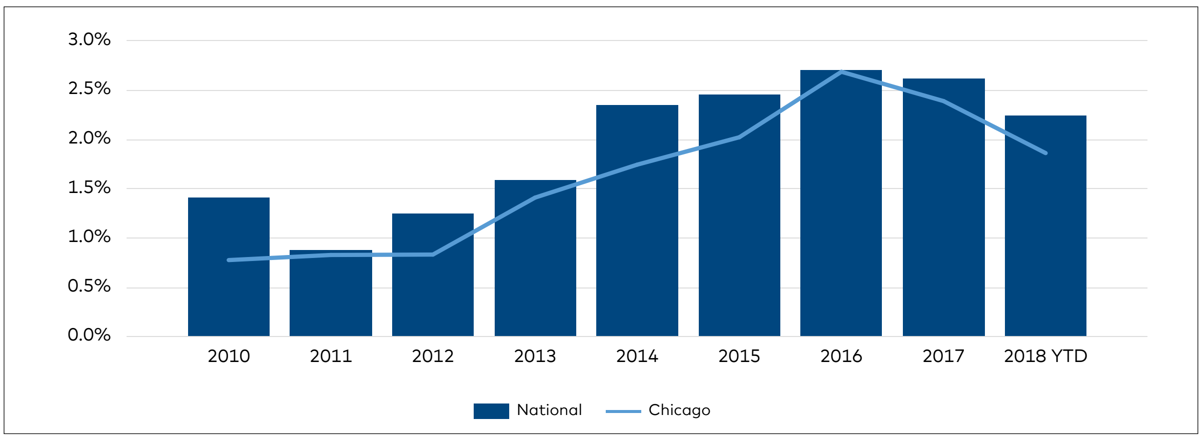
	2013	2014	2015	2016	2017
National	316,234,505	318,622,525	321,039,839	323,405,935	325,719,178
Chicago Metro	7,343,501	7,351,417	7,347,063	7,335,054	7,319,978

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

Supply

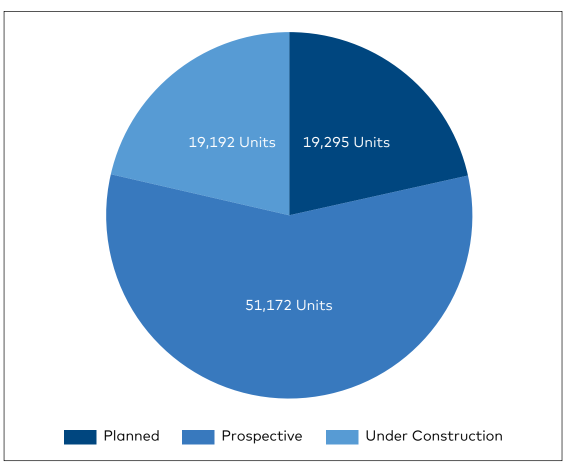
- Multifamily deliveries in Chicago reached their current cycle peak in 2016—approximately 8,700 units—and have been slowly declining since. However, the number of completions remained sizeable, with 5,400 units completed in 2018 through November.
- Despite the decrease in deliveries—due in part to delays caused by labor shortages and mounting construction costs—development activity remains relatively strong. Roughly 19,200 units were underway in Chicago as of November and 70,500 more were in the planning and permitting stages. Occupancy in stabilized properties dropped just 20 basis points in the 12 months ending in October, to 94.6%. Strong housing demand led to the absorption of more than 4,000 units during the same period.
- Construction activity is concentrated in Chicago's core submarkets, with the Near North Side (2,346 units underway), the Near West Side (2,017), the Loop (1,972) and the Near South Side (1,300) leading the way. The city council has approved zoning for a $7 billion, 62-acre South Loop project developed by Related Midwest, which would bring about 10,000 units to the intersection of Roosevelt Road and Clark Street.

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



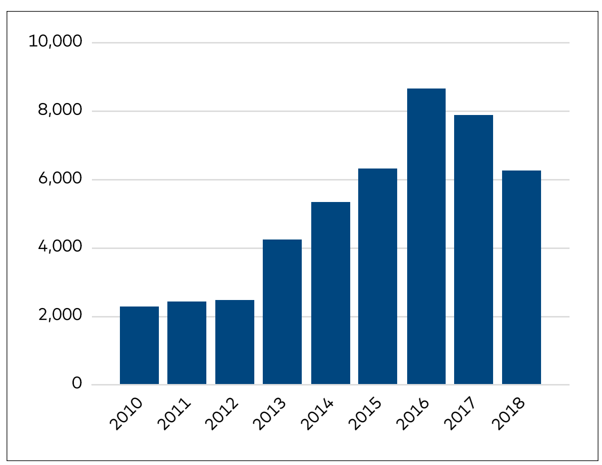
Source: YardiMatrix

Development Pipeline (as of November 2018)



Source: YardiMatrix

Chicago Completions (as of November 2018)

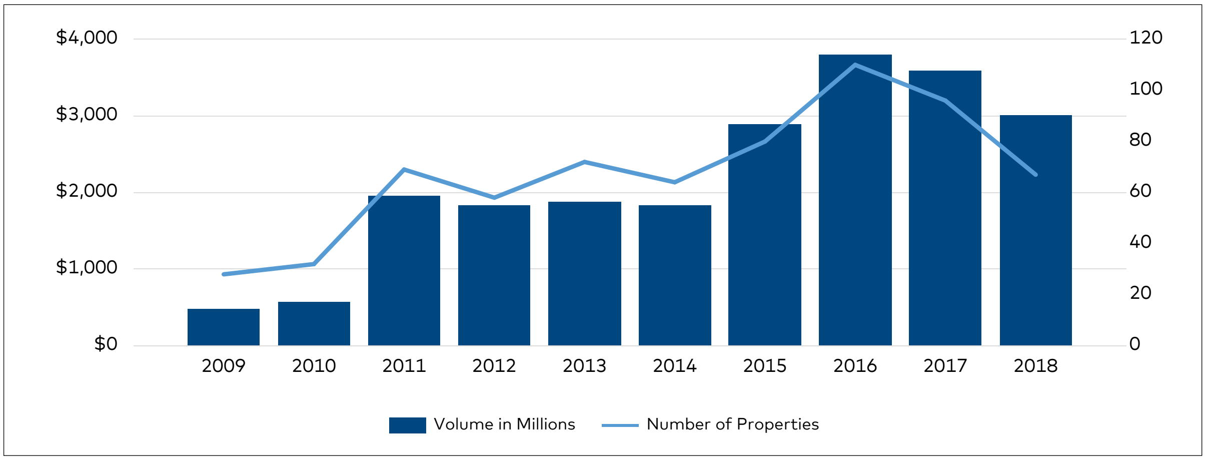


Source: YardiMatrix

Transactions

- After a slow start to the year, investment picked up in Chicago, with more than $3 billion in multifamily properties trading in the first 10 months of 2018. The full-year figure could surpass the 2016 cycle peak, when 110 deals closed for a total of $3.8 billion. Investors remained focused on value-add strategies, looking for higher returns farther away from Chicago's downtown. In the 12 months ending in October, the total sales volume for suburban properties amounted to approximately $2.3 billion, compared to $1.7 billion for urban assets. The Loop led the pack for sales volume for the period, with a total of $659 million in multifamily assets changing hands.
- Investors continue to focus on Renter-by-Necessity assets that offer solid yields. Competition for high returns is also reflected in surging per-unit prices, up 11% on average over the 2017 value, to $196,034. The metro's price per unit was well above the $152,601 U.S. average.

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



Source: YardiMatrix

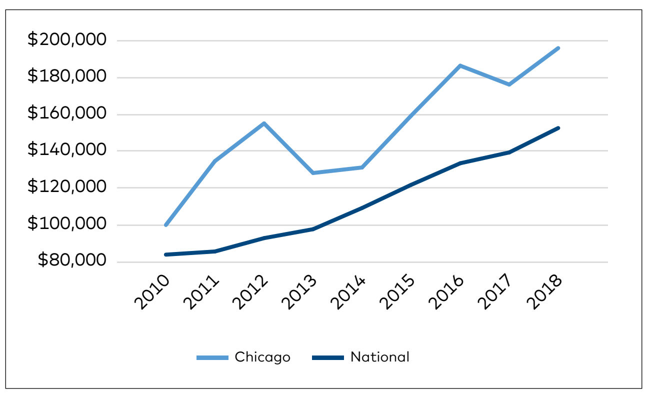
Top Submarkets for Transaction Volume[1]

Submarket	Volume ($MM)
Loop	659
Wheaton	448
Schaumburg	268
Near South Side	207
Glendale Heights	198
Mundelein	194
Palatine	192
Near North Side	174

Source: YardiMatrix

[1] From November 2017 to October 2018

Chicago vs. National Sales Price per Unit



Source: YardiMatrix

News in the Metro

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MULTI-HOUSING **NEWS**

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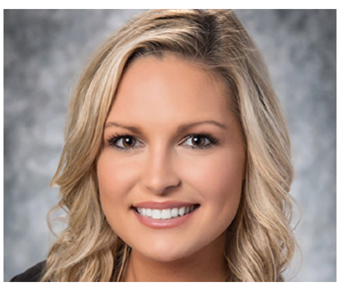
Essex Realty Sells Chicago Community

Partners Jim Darrow and Jordan Gottlieb represented seller JAB Real Estate in the $24.5 million 1031 exchange transaction. The property is close to the Sedgwick "L" station.

Draper and Kramer Acquires Chicago Luxury Apartments

CBRE facilitated the sale of the 180-unit rental property that sold as part of a 1031 exchange. The new ownership assumed management of the community.



CA Ventures Adds New VP

Taylor Gunn brings years of experience in student housing analytics. She will lead the Chicago-based company's market research and development strategies across Europe, but also support domestic development strategies.

Chicago Tower Lands $149M Refi

The Gallery on Wells is a recently completed 40-story residential building situated in the River North submarket. CBRE Capital Markets Group in Chicago arranged the debt transaction.

$200M Mixed-Use Development Coming to Chicago

Ogden Commons will be built on 10 acres on the city's West Side, bringing hundreds of mixed-income housing units to the area starting in 2019, along with commercial space.

Chicago's Largest Co-Living Home Breaks Ground

Upon completion, Common Addams will include 223 beds and access to more than 5,000 square feet of shared amenity space, marking the partnership's third project in the city.

Executive Insight

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MULTI-HOUSING NEWS

Chicago's Condo Deconversion Sales: Will the Trend Last?

By Roxana Baiceanu

It's not only new, cutting-edge residential developments that are defining Chicago's real estate market, especially when it comes to investments. Value-adds are still attractive for most real estate investors. Interra Realty Managing Partner Patrick Kennelly discusses his company's most recent moves on the market, highlighting the opportunities behind condo buildings suitable for deconversion. Interra Realty closed a large number of such deals in the north part of the metro in recent quarters. The trend reached its peak in 2017 but doesn't show signs of stopping.

How has condo deconversion to apartments impacted Chicago's multifamily market?

I know of more than 2,000 units that have gone from condo to rental over the past two years, with the majority of these deconversions happening on the north side of Chicago and in inner-ring suburban locations like Evanston and Oak Park. As for impact, it will definitely answer the strong demand for more rental units in these areas, though without an effect on rents. Although we have seen thousands of rental units come online in the past few years, we have not seen a major softening of rents in these areas yet.

What are the risks of such investments?

According to Illinois condo law, governed by Section 15, generally, a deconversion sale requires that more than 75 percent of the ownership of the common elements approve the sale. The most obvious risk is the offer being sent to vote and not passing. The association incurs legal fees,

stress of whether they are moving or not and undue cost of their time. Additionally, from a buyer's perspective, we have seen closings drawn out for months because of various issues and seller holdouts. We have recently dealt with a holdout in a deconversion sale that deferred the closing so much that the interest rates changed. It was enough to have a meaningful impact on the deal, so the buyer requested a credit for the additional costs.

How have changes in interest rates and tax legislation influenced multifamily investment in Chicago so far?

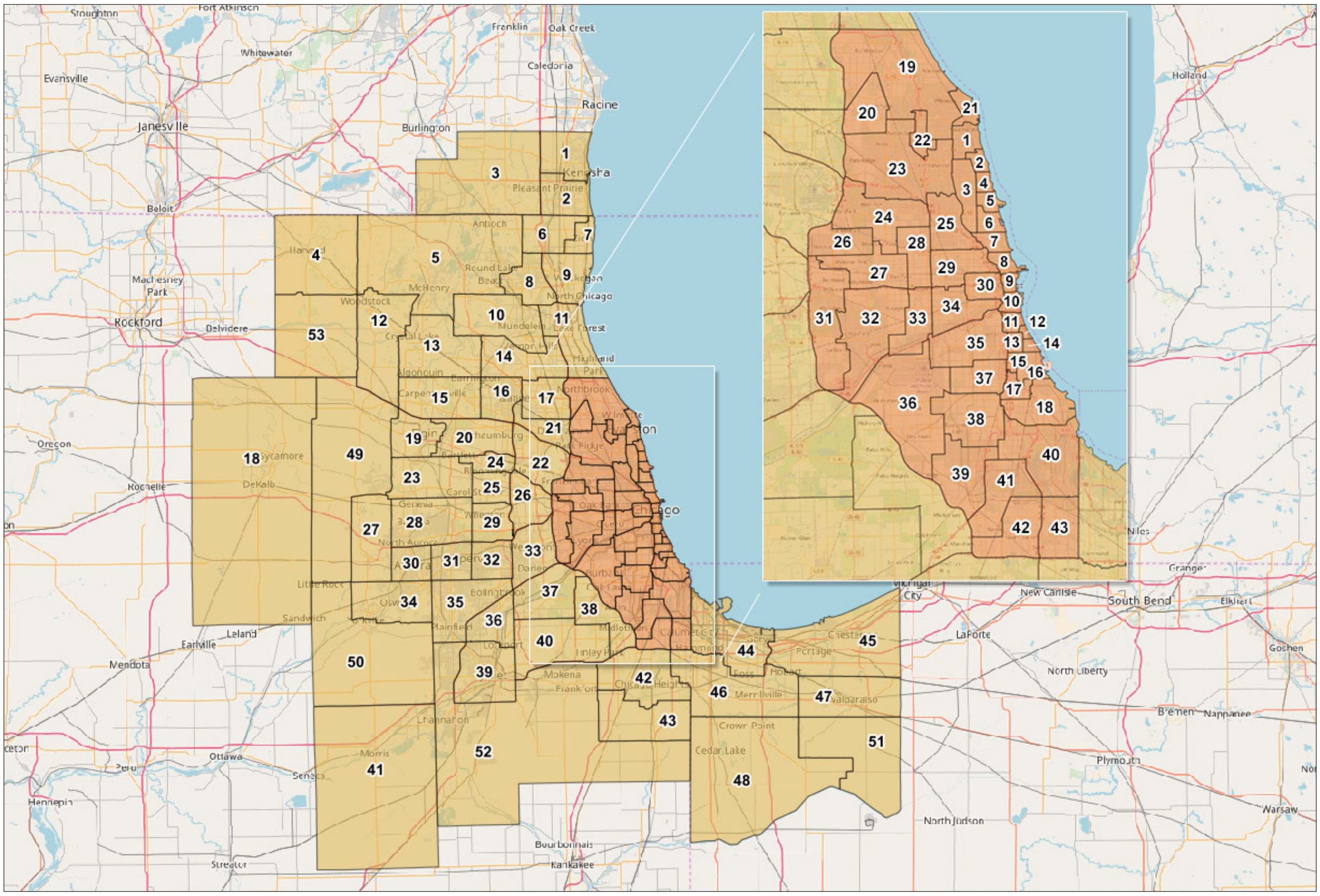
With rising interest rates and pricing remaining strong, investors face a compression in their cash-on-cash returns. In turn, we are seeing some buyers exploring neighborhoods outside their core holdings to hit their desired returns.

As far as taxes go, many areas have recently been reassessed in Chicago and many owners were hit with big increases. This has caused some investors to look outside of the Chicago market in fear that taxes will continue to rise.

What are the challenges and opportunities for financing multifamily acquisitions in Chicago at this point?

Many buyers are aggressively shopping different banks to squeeze points, as pricing is tight in today's market. ... With the recent deconversion trend, the biggest challenge in many of these deals is achieving an occupancy level that meets the bank's standards. In most cases, banks are requiring between 85 and 90 percent occupancy to finance the deal.

Chicago Submarkets



Area #	Submarket
1	Kenosha-North
2	Kenosha-South
3	Bristol
4	Harvard
5	McHenry
6	Zion-West
7	Zion-East
8	Grayslake
9	Waukegan
10	Mundelein
11	Highland Park-Libertyville
12	Huntley
13	Crystal Lake
14	Buffalo Grove
15	Carpentersville
16	Palatine
17	Arlington Heights
18	DeKalb
19	Elgin
20	Schaumburg
21	Mt Prospect
22	Bensenville
23	St Charles
24	Roselle
25	Glendale Heights
26	Lombard
27	Elbum

Area #	Submarket
28	Batavia
29	Wheaton
30	Aurora
31	Naperville-West
32	Naperville-East
33	Downers Grove
34	Yorkville
35	Bolingbrook
36	Romeoville
37	Hickory Hills
38	Palos Heights
39	Joliet
40	Orland Park
41	Grundy
42	Chicago Heights-North
43	Chicago Heights-South
44	Gary-West
45	Gary-East
46	Gary-South
47	Valparaiso-South
48	Crown Point
49	Outlying Kane County
50	Outlying Kendall County
51	Outlying Porter County
52	Outlying Will County
53	Southern McHenry County

Area #	Submarket
1	Evanston-South
2	Rogers Park
3	Lincoln Square
4	Edgewater
5	Uptown
6	Lake View
7	Lincoln Park
8	Near North Side
9	Loop
10	Near South Side
11	Douglas
12	Oakland
13	Grand Boulevard
14	Kenwood
15	Hyde Park
16	Woodlawn
17	Greater Grand Crossing
18	South Chicago
19	Wilmette-Northbrook
20	Des Plaines
21	Evanston-North
22	Skokie

Area #	Submarket
23	North Park-Niles
24	Montclare
25	Irving Park-Logan Square
26	Northlake
27	Oak Park
28	Belmont Cragin-Austin
29	West Town-Garfield Park
30	Near West Side
31	Countryside-Westchester
32	Berwyn
33	Cicero
34	Lawndale
35	New City
36	Burbank-Oak Lawn
37	Englewood
38	Auburn Gresham
39	Blue Island
40	South Deering-Pullman
41	Riverdale
42	South Holland
43	Calumet City

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.