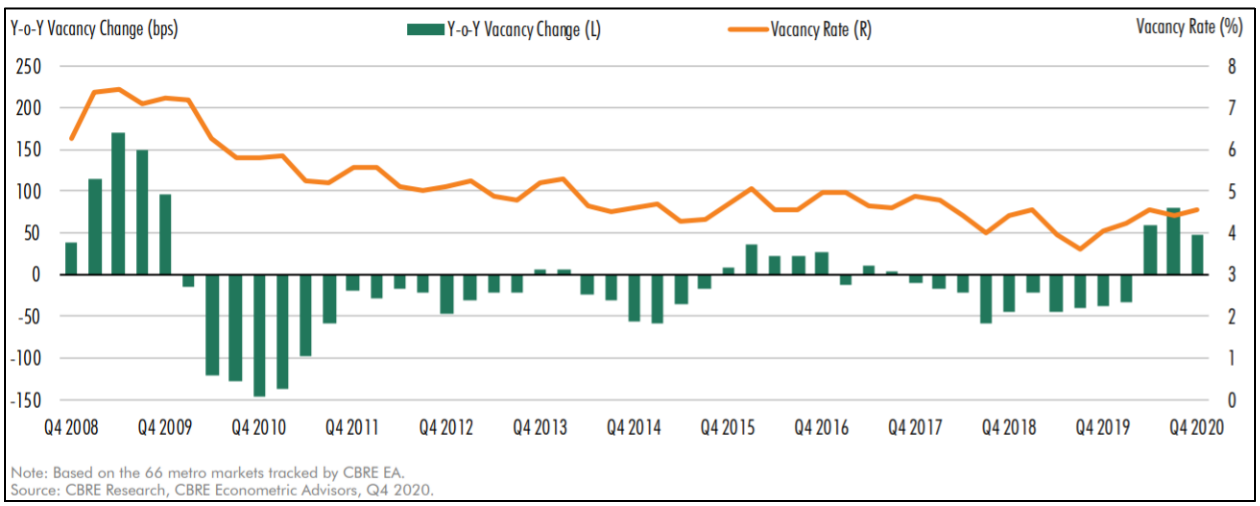
Mick Law P.C. – U.S. Multifamily Update
March 16, 2021

The multifamily sector of real estate continued its dominance among the retail private placements structured as Delaware Statutory Trusts (DSTs) and qualified opportunity zone funds (QOFs). In 2020, the multifamily sector accounted for 51.12% of the \$3.2 billion raised within retail syndicated DST programs, and with a majority of QOFs tracked by Novogratic & Company LLP utilizing multifamily assets as permissible investments within their offerings. In view of the considerable retail fundraising activities within the multifamily sector, we offer this update of the national multifamily market.

Vacancy

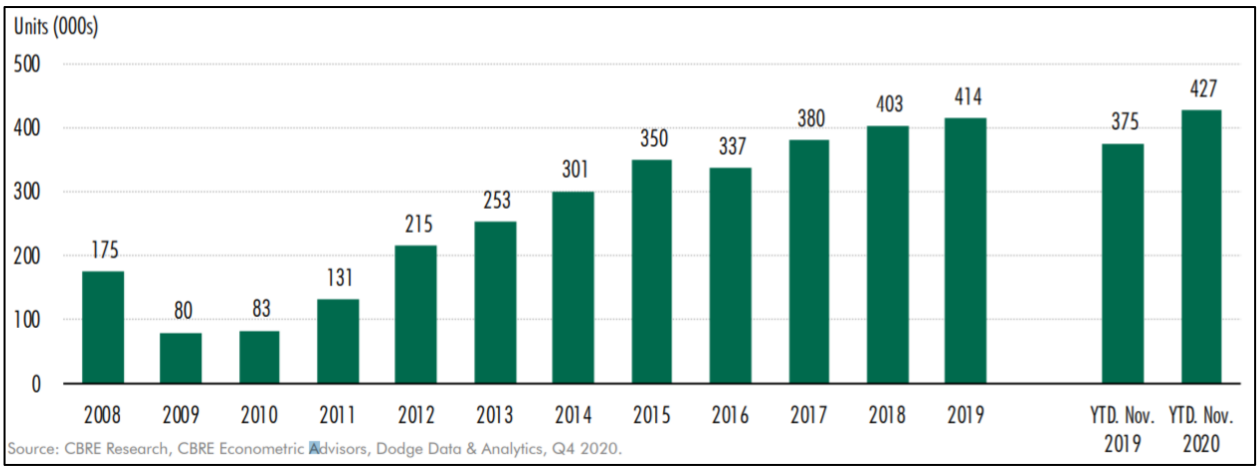
According to the fourth quarter 2020 CB Richard Ellis U.S. Multifamily Market Report (the latest report issued as of the date of this update), the U.S. multifamily vacancy rate was 4.5%, up 10 basis points over the prior quarter and up 50 basis points from the fourth quarter of 2019. In mid-2019, the national vacancy rate was 3.6%, the lowest level since 2000. According to REIS, the national vacancy rate is forecast to increase to 6.3%, in 2021, before falling to 5.5%, in 2022, and 5.0%, in 2023. *The fourth quarter 2020 vacancy rate was substantially lower than the 7.0% vacancy rate many had predicted early on during the Covid-19 pandemic.*

A summary of the U.S. multifamily vacancy rate since the third quarter of 2008 is outlined within the chart below:



Multifamily demand has remained relatively stable despite the recession. In the fourth quarter of 2020, net absorption was 55,600 units, substantially higher than expected. The annual net absorption total was 190,600 units, a very respectable level given the recessionary conditions, but still 39% below the net absorption realized in 2019. Suburban submarkets generally outperformed urban submarkets during the most recent quarter due to a higher number of Covid-19 cases in urban areas and remote-working arrangements being extended for most major corporations.

Nationally, through November 2020, year-to-date multifamily construction starts totaled 427,100 units, up 13.8% over the same period in 2020. Starts moderated in April and May to a monthly average of 32,100 units, down 24.5% from the first quarter of 2020 average of 42,500 units. Construction moratoria in some areas delayed the delivery of some developments and delayed commencement of others during the second and third quarters. Third quarter 2020 starts averaged 42,100 units per month. High levels of permit activity indicate that developers are looking well beyond the pandemic period. According to the U.S. Census Bureau for 2020, 429,300 multifamily units received permit approval, down 10.8% from 2019. In the fourth quarter of 2020, the new permit total was 110,700 units, the highest quarter of the year, and up 4.9% over the third quarter. New York, Houston, and Dallas lead the country in completions for 2020. New deliveries have been nearly all concentrated in the Class A sector. New completions in 2020 were from construction projects begun prior to the 2020 recession. Similarly, most of the multifamily projects that were started in 2020 were planned before the Covid-19 pandemic. A summary of historical construction starts as compared to current trends is outlined below:



Market Rents

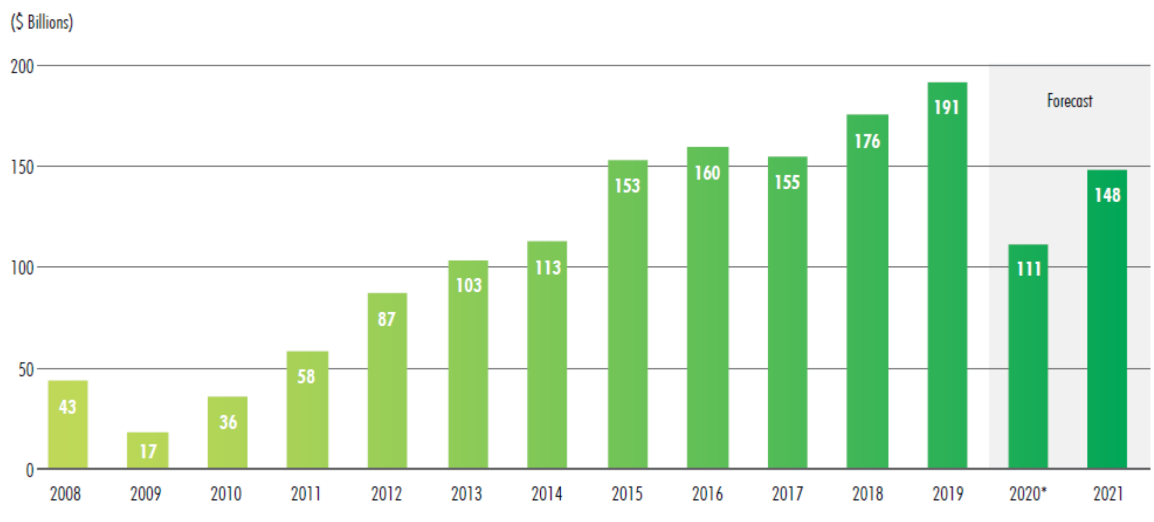
According to REIS, as of the fourth quarter of 2020, the national monthly average asking and effective rental rates were $1,455/unit and $1,385/unit, respectively, down moderately from $1,499/unit and $1,429/unit as of the fourth quarter of 2019. REIS has forecast asking rates to fall another 1.7%, to $1,430/unit, and effective rental rates to fall by 1.9%, to $1,358/unit, in 2021. Beginning in 2021, REIS is forecasting rental rates will begin to climb, reaching normalized growth rates between 2% and 3% by 2023.

During the pandemic, the Midwest region of the country had the highest number of markets experiencing positive rental rate growth; only Chicago and Minneapolis had rent declines. The Pacific region, conversely, had the most major markets recording quarter-over-quarter rent declines.

CBRE data indicates a monthly effective rental rate near $1,666/unit as of the fourth quarter of 2020, down 4.2% over the prior 12 months. This decline is the first since 2009. According to CBRE, Class A effective rents declined by more than Class B and Class C rents. CBRE data indicates a steady recovery staring in the second half of 2021.

Capital Markets

The Covid-19 pandemic weighed heavily on commercial real estate activity. According to CBRE's "U.S. Real Estate Market Outlook 2021," multifamily investment volume for 2020 was $111 billion, the lowest volume since 2013, representing a 42% decline over the 2019 investment volume of $191 billion. A summary of multifamily investment from 2008 to present can be found below:



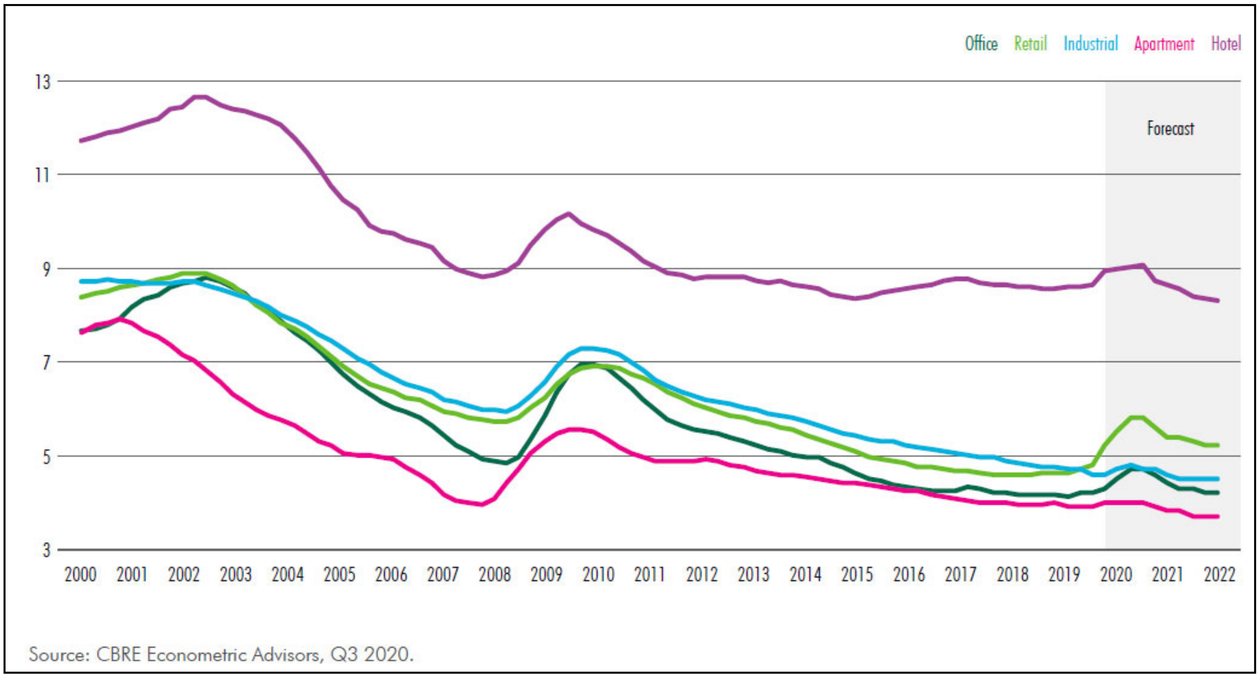
*2020 forecast is based on actual numbers through September.
Source: CBRE Research, Real Capital Analytics (historical), Q4 2020.

CBRE forecasts multifamily investment to rebound in 2021, increasing by 33% to $148 billion. The pause in multifamily investment is expected to be short-lived because of long-term demographic drivers and social trends, including growth in the younger population and lack of affordable housing. Capital targeting investment in the sector is at historically high levels and the mix of investors is more diverse than ever.

Despite the decline in investment volume discussed above, investor demand for multifamily assets in 2020 was well above the level found during previous recession, due in part to a shift in investor preference towards industrial and multifamily assets, and away from office and retail. *According to CBRE, if the Covid-19 vaccine is widely distributed by mid- to late-2021, the commercial real estate market will normalize based on abundant liquidity, low cost of capital and attractive returns*. Available capital for real estate investment remains at more than $300 billion globally, the majority of which is targeting North America.

Meanwhile, the Federal Reserve plans to keep interest rates near zero until 2023. Both inflation and the risk-free yield from the 10-year US Treasury declined sharply in 2020. Cap rates have remained relatively stable in 2020. Investors were able to take advantage of the ultra-low cost of borrowing, which will offset the potentially slower growth in rental income.

A summary of capitalization rates across all major US property types can be found below:



Multifamily Investment Returns

As reported by *Newmark Knight and Frank* (NKF) within its *Capital Markets Report* for the fourth quarter of 2020, the annualized return for the U.S. multifamily sector was 1.80%. While sector returns were down from a 5.5% annualized return reported in 2019, the sector did manage to generate positive returns in the fourth quarter of 2020 (with returns in the fourth quarter of last year increasing by 162 basis points from the 2Q 2020 low of (-) 0.60%).

Despite the downward effect that Covid-19 placed on multifamily returns, it is noteworthy that certain pockets of the U.S. outperformed the average sector return by 250-1,000 bps, which included Salt Lake City, Utah (12.7%), Phoenix, Arizona (10.4%), Denver, Colorado (6.3%), Raleigh, North Carolina (6.2%), Charlotte, North Carolina (5.6%), Orlando, Florida (4.3%), and Tampa, Florida (4.3%). The worst performing cities in 2020 included San Francisco, California ((-) 3.1%), New York, New York ((-) 2.3%), and Chicago, Illinois ((-) 2.3%) (with Covid lock down policies affecting population trends within these blue states per NKF research).

With the exception of the industrial sector, multifamily returns have outpaced other sectors of our real estate industry, as illustrated by the table below:

Total Returns - Multifamily

	2020	2019	10-Year	20-Year
U.S. Multifamily	1.8%	5.5%	8.0%	8.6%
U.S. Office	1.6%	6.6%	7.4%	8.4%
U.S. Industrial	11.8%	13.4%	9.9%	13.1%
U.S. Retail	(-) 7.5%	1.9%	8.8%	7.6%
U.S. Hospitality	(-) 25.3%	3.5%	4.6%	4.1%

Source: NKF Research (4Q 2020)

Summary of Data

While vacancy rates are rising and rental rates declined for the first time in over a decade, the full impact of the Covid-19 pandemic within the multifamily sector was not nearly as significant as was forecast mid-year 2020. Interest rate declines and a shift in investor preference have continued to spur deal flow, despite challenging conditions. Supply side development appears unphased, but the true test will come in 2021 as projects previously in planning and pre-development phases have commenced construction. The forecast is for conditions to moderate in 2021, with a recovery beginning in 2022.

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