LMC INSIGHTS

1Q 2022

LMC
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Inside Look

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Public Market Returns

	4Q21	1 Year	3 Year
S&P 500	11.03%	28.70%	26.07%
Dow	7.37%	18.72%	15.92%
Nasdaq	8.28%	21.39%	33.10%
FTSE NAREIT[1]	16.17%	41.30%	19.93%
Barclays Agg	0.01%	-1.54%	4.79%
10-yr Treasury[2]	1.52%	0.93%	2.69%
CPI[3]	1.52%	6.69%	10.21%

Private Market Returns

	4Q21	1 Year	3 Year
NCREIF Property Index			
Total Return	6.15%	17.70%	8.37%
Income	1.03%	4.24%	4.32%
Appreciation	5.12%	13.05%	3.92%
Hospitality	4.64%	5.48%	-6.68%
Industrial	13.34%	43.33%	22.01%
Multifamily	6.82%	19.91%	8.81%
Office	1.68%	6.12%	4.74%
Retail	2.18%	4.22%	-0.59%

Source: NCREIF, Morningstar, Federal Reserve Bank of St. Louis (FRED)

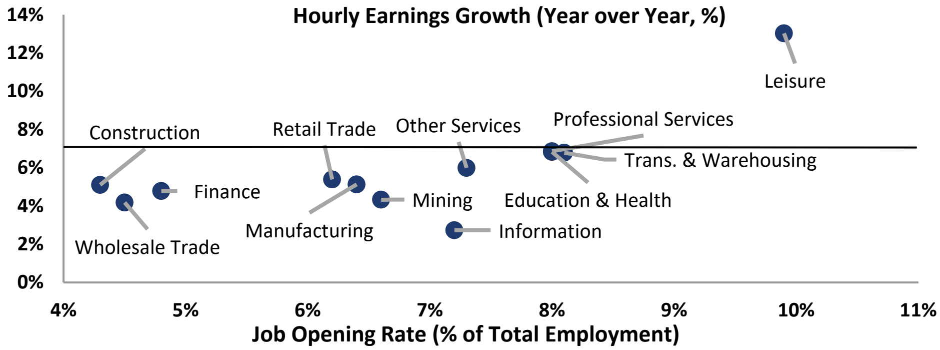
1. FTSE NAREIT All Equity REITs Index.
2. Represents current yield at the end of 4Q21, 4Q20, and 4Q18, respectively.
3. Consumer Price Index (USACPIALLMINMEI): All Items for the US, not seasonally adjusted. Represented as a percentage change at beginning of quarter over the specified time frame.

Despite the lingering effects of the COVID-19 pandemic, 2021 was a record-setting year for the United States' multifamily market

State of the Economy

The 4th quarter of 2021 was a period of diverging economic performance in the United States. COVID-19 cases surged to record highs as Omicron proved far more transmissible than any of the previous variants, with peak daily case rates nearly quadrupling the previous record. However, U.S. economic growth accelerated in the fourth quarter and real GDP grew by 5.5% year over year in 2021, achieving a 35-year high. Fixed nonresidential investment rebounded in the 2021 Q4, with investment in intellectual properties growing by more than 11% year over year. Consumption is still the driving force behind GDP growth, even as investment recovers, with consumption growing at an annual rate of 2.2%, 30 basis points faster than the pre-pandemic average. The consumer has begun to feel the pressure of both inflation and the waning effects of stimulus, along with a surge in COVID-19 cases during the quarter. Real personal consumption expenditures peaked in October of 2021 and have since declined by 1.2%, driven by a 4% decline in real goods consumption.

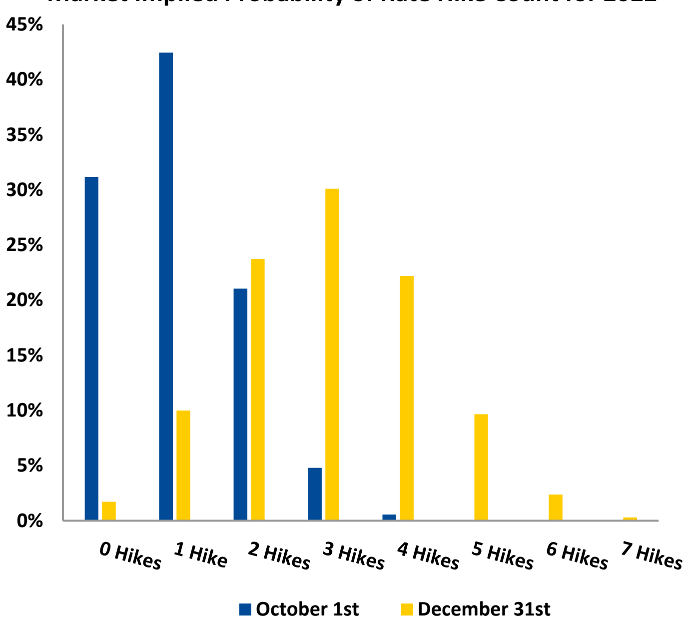
Consumption has been declining as wages have not been able to keep up with high inflation, despite a severe labor shortage. The U.S. added 1.83 million jobs in the fourth quarter, the third-best quarter behind 2021 Q1 and 2020 Q3, but the labor shortage remains a severe problem. Businesses still reported 10.9 million job openings, or 1.68 openings per unemployed worker, and a quits rate of 2.9%, 50 basis points above the pre-pandemic record. Businesses are pushing wages in an effort to keep their workers and entice new ones: Overall hourly earnings are more than double the previous cycle average. However, an inflation rate of 7.0% as of December 2021 has eroded those earning gains, with only leisure workers having seen real wage growth, as that industry is in the midst of a particularly severe labor shortage.



Source: US Census Bureau; CoStar Advisory Services | As of December 2021

High nominal wage growth is typically a precursor for future inflation, as households attempt to maintain their quality of life in the face of rapidly rising prices by demanding higher pay. However, the primary driver remains the fact that supply chains are struggling to sort themselves out in the face of a pandemic and changing consumer preferences. Over the last two years, consumers have shifted billions of dollars into goods spending, which is up 12% since the start of the pandemic, and away from services spending, which is down 0.7%. The focus on goods consumption led to prices in cars and furniture to jump by over 10%, while services inflation is below 5%. The labor shortage, particularly around truckers on the west coast, has exacerbated the problem as well, and without a good short-term solution, the Fed is gearing up to respond.

Market Implied Probability of Rate Hike Count for 2022(1)



Sources: CME Group; CoStar Advisory Services
As of December 2021
1) One Rate Hike = 25 basis point increase

The fourth quarter of 2021 marked a remarkable hawkish shift for the Federal Reserve. At the beginning of the quarter, the market was expecting one to two rate hikes by the end of 2022. By the end of the quarter, the market had shifted from two to three, and more recent projections put the number closer to four to five. The Fed must walk a precarious line between controlling inflation and accommodating post-recovery growth. Going forward, a Fed policy mistake, by either hiking rates too slowly or too quickly, could pose a substantial risk to what will likely otherwise be solid U.S. economic growth.

Multifamily Investment Outlook

Despite the lingering effects of the COVID-19 pandemic, 2021 was a record-setting year for the national multifamily market. Annual net absorption totaled slightly more than 704,000 units, 54% higher than the previous record, set in 2020. With demand surging to record levels and construction levels remaining relatively steady, the average vacancy rate plummeted, dropping from 6.7% in the fourth quarter of 2020 to 4.7% as of 2021 Q4.

While demand growth slowed in the fourth quarter of 2021, quarterly net absorption still totaled 69,950 units, 11% greater than the historical average since 2004. The high end of the market has experienced the largest surge in demand, with the average 4- & 5-Star vacancy rate declining from 10.6% to 6.4% from 2020 Q2 to 2021 Q4. Meanwhile, vacancy rates in 1 & 2 Star and the 3 Star properties witnessed little movement in 2021 and sit around 4%. Strong demographic drivers and increased net migration have enabled vacancy rates to fall the furthest in Sunbelt markets like Orlando, Austin, and San Antonio. However, even more costly markets, such as those in the Bay Area, witnessed substantial demand growth throughout 2021, especially as in-person learning resumed at major universities.

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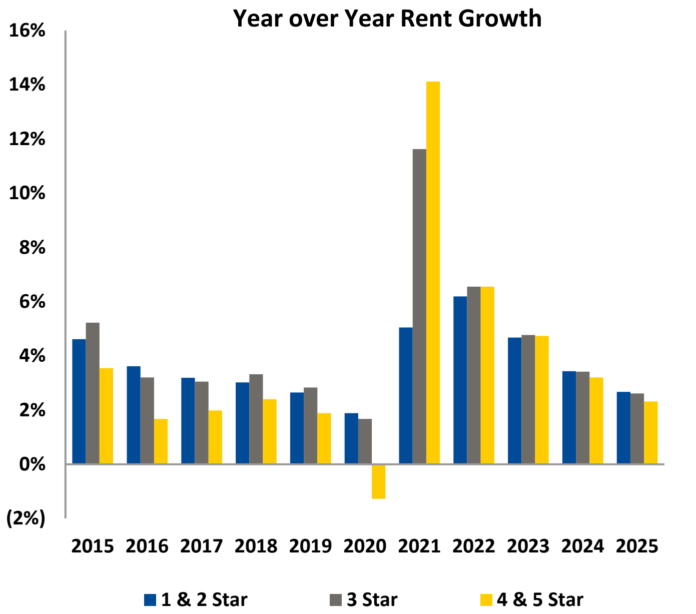
Despite multifamily demand and rent growth climbing to record highs, construction has remained relatively steady. Roughly 85,700 units were delivered in the fourth quarter, 9% below the five-year average, meanwhile the total number of units under construction declined by 1%, or 5,400 units, quarter over quarter. Construction activity remains highly concentrated in coastal and Sun Belt markets. Sun Belt markets have seen heavy amounts of construction as a share of their inventory, with 5.8% of total inventory underway, vs. 3.9% nationally. Core coastal markets have seen a more muted construction pipeline, with their under construction share sitting on par with the national average.

The dramatic tightening of vacancy rates across the national apartment market translated into significant rental rate increases in 2021. Year-over-year rent growth accelerated to 11.3%, up 70 basis points from the third quarter's rate. While suburban rents continued to outperform in 2021, downtown assets made up a lot of ground as in-person schooling returned, and workers returned to offices.

Rent growth has been the strongest in the Sun Belt markets with all of the top 10 rent growth markets residing in the Southeast and Southwest. Palm Beach, Tampa, Orlando, Las Vegas, and Phoenix all recorded annual rent growth above 20% in 2021 Q4. 4- & 5-Star assets lead way in terms of rent growth during 2021 with 3-Star properties coming in a distant second.



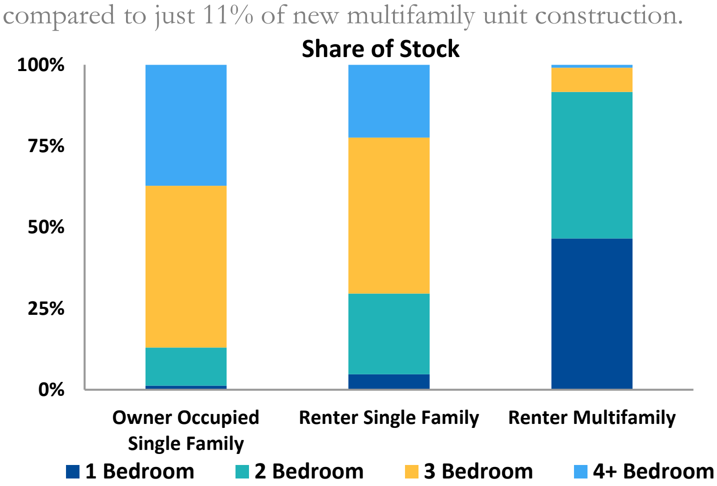
Sources: CoStar Advisory Services As of 4Q21

With the U.S. apartment market revealing itself to once again be a resilient asset class with significant upside, investment capital has poured into the multifamily sector. Multifamily transaction volume totaled more than $251 billion in 2021, more than doubling the 2020 total. And, in 2021 Q4, nearly $107 billion traded hands, eclipsing the previous single quarter record[1]. Atlanta, Houston, Dallas-Fort Worth, and Phoenix rank as top markets by total sales volume in the fourth quarter, as investors have generally shifted capital away from core coastal markets and into the Sun Belt over the last few years. The average price per unit experienced significant gains as well, increasing by 11% year over year as of 2021 Q4.

Addressing Different Needs: The Single-Family Rental and Multifamily Markets

The U.S. is in the middle of a well-documented housing shortage as a decade of little development activity has left the country with an estimated deficit of 2.7 million housing units, based on the ratio of housing stock to the total population aged 20+. High construction costs have meant that, on average, there have been more large, expensive homes that have been developed, creating a dearth of starter homes. New multifamily development has been a large part of the solution to the housing deficit since it has been easier to supply housing in volume with that product type given its greater density, but, in recent years, single-family rental (SFR) development has also joined the effort in solving this nationwide problem. It's often quipped that SFR and suburban multifamily directly compete and that one can not succeed without the other's demise, but recent data and studies have proven otherwise.

Suburban garden multifamily addresses a segment of the renter market that needs a place to live and doesn't want to pay what has historically been a premium for more highly amenitized, infill locations. This multifamily renter is typically, but not always, younger and without children. As younger adults get married and have families, they generally seek single-family homes with more space and want a cheaper cost per square foot; a different renter demand SFR is well-positioned to address. To illustrate the complementary nature of these two segments of the residential rental sector, a recent Harvard University study[1] of new residential construction found that 77% of single-family build to rent units had 3 or more bedrooms, compared to just 11% of new multifamily unit construction.

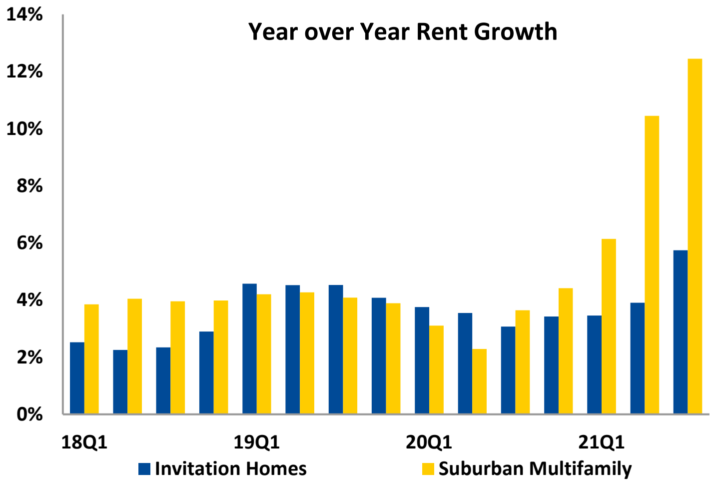


Sources: CoStar Advisory Services, U.S. Census Bureau As of 2019

1) Source: Harvard.edu

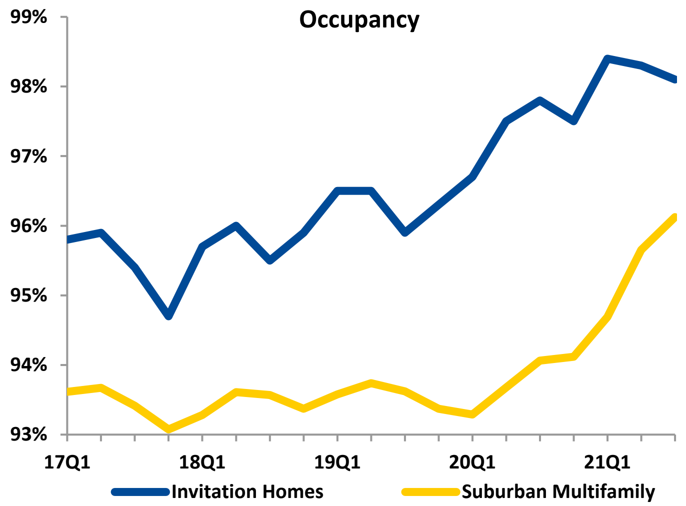
The COVID-19 pandemic was certainly world-changing from a global health perspective but also caused an acceleration of many trends that were already occurring in the above-mentioned demographics of renters. This is perhaps most pronounced in the lack of affordability of housing and an acceleration in demand for rental housing. Low-interest rates and a demographic shift out to the suburbs has caused single-family home prices to soar 29% since February of 2020, pricing out many would-be buyers, especially younger potential homeowners. First-time homebuyers made up 27% of total home purchases in January 2021, down from a historic average of 40%[(1)].

While the SFR and multifamily sectors in the US have both been around for well over 50 years, the COVID-19 pandemic gave new attention to SFR as an institutionally investable and complementary residential asset class. SFR is an important part of the overall rental market, making up 36% of the total US residential rental market with multifamily making up the bulk of the remainder. While multifamily properties are, on average, 55% institutionally owned, SFR is in its infancy with only 2% of the market being institutionally owned. That said, it's estimated that nearly 20% of single-family homes bought in 2021 Q4 were by institutional investors as this institutional investment interest grows[(2)].



Sources: CoStar Advisory Services, Invitation Homes, SEC Filings As of 3Q21

It is not just about space, but also the different type of households SFR and multifamily units are targeting. The median single-family rental household made 83% more than the median multifamily renter household, while serving a younger market than owner-occupied units: 41% of SFR households are under the age of 35, vs. 25% of new, owner-occupied single-family households. While the target demographics are somewhat different, SFR and suburban multifamily performance has generally moved in line with each other. Suburban multifamily rent growth has exploded over the past few years, as the relative lack of construction has been met with huge demand. However, SFR rents have accelerated as well, and occupancies in both product types indicate a historically tight market.



Sources: CoStar Advisory Services, Invitation Homes, SEC Filings As of 3Q21

Going forward, both multifamily and SFR are expected to benefit from continued strong demand given the decade-long production deficit of homes in the U.S. Ultimately, both sectors address the needs of a very broad, diverse, renter market in different ways. This demand, given the secular tailwinds, will persist, all things equal, and savvy investors focused on diversification and durable returns will make both sectors part of their mixed-asset portfolios.

1) Source: NPR.org
2) Source: CommercialObserver.com

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1. AUM as of 12/31/2021

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