STATE OF THE U.S. HOUSING MARKET

Identifying Investment Opportunities in Rental Housing

AMENDED MAY 2022

INVESTMENT THESIS

Evolving rental housing needs among a broad demographic coalition combined with inadequate housing supply has given rise to enduring investment opportunities across the rental housing spectrum (e.g., Premium, Middle-Market, Workforce, Inclusionary, and Single-Family Rental) that we believe should persist for years to come.

EXECUTIVE SUMMARY

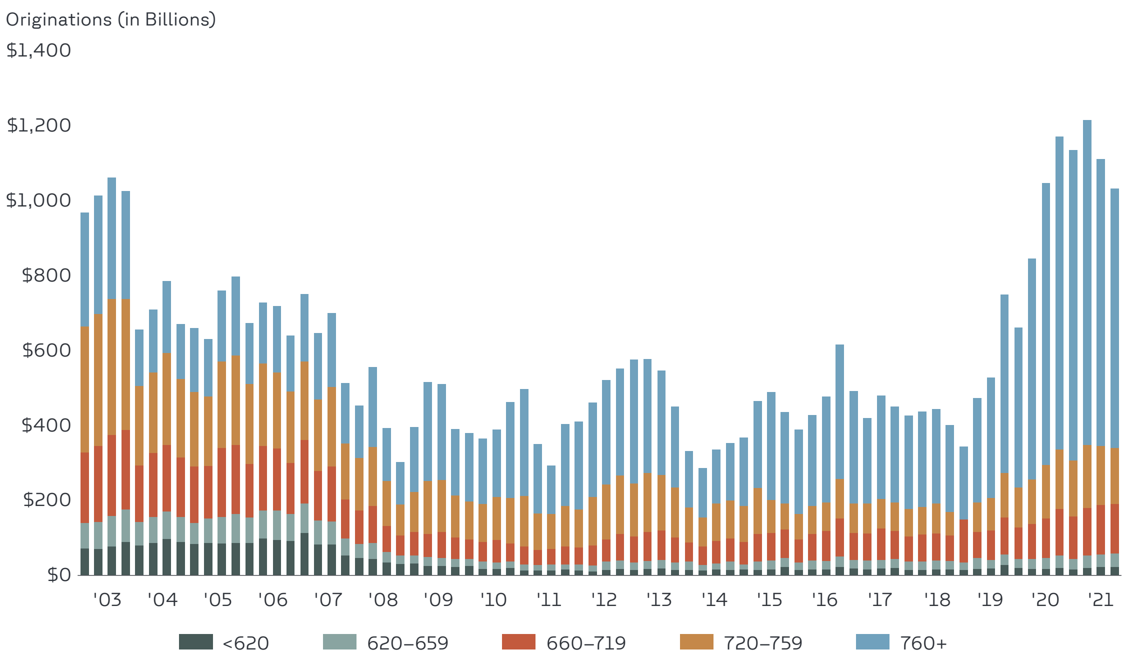
Housing is a necessity and the composition and trajectory of the U.S. population, combined with a supply and demand imbalance, have led to robust demand for rental housing and an enduring investment opportunity. This paper evaluates investment conditions across rental housing sectors, focusing on the long-term outlook, demand drivers, and developing macro trends that will likely impact the broader housing market going forward. It concludes by identifying a prudent approach for potentially capturing the opportunity in U.S. rental housing.

We believe a flexible strategy capable of capturing value across the rental housing spectrum remains an effective response to emerging and changing opportunities during both the current and future economic cycles, and that rental housing in the U.S. offers an attractive long-term investment opportunity, as highlighted in the following:

Favorable Demographics

The demographic tailwinds – driven primarily by Millennials, Generation Z, and the Baby Boomers – that will underpin the rental housing market over the long term remain robust and have strengthened as a result of the coronavirus health crisis. There are approximately 73 million Millennials, making up the largest demographic in the workforce today, which have been slower than previous generations in transitioning to homeownership due to mounting financial struggles in the aftermath of the Global Financial Crisis (GFC). In fact, the personal finances for nearly half of the Millennial cohort have yet to recover from the GFC.[1] Thus, mortgage origination levels favoring those with very high credit scores, as highlighted in **Exhibit 1**, and a period of elevated residential home prices coupled with a rise in the 30-year mortgage rate off historic lows should suppress overall homeownership rates. According to the National Association of Realtors, 2021 represented the highest median age (45 years old) of first-time homebuyers compared to 31 back in 1981, with this trend unlikely to reverse any time soon. Further, the nearly 67 million Americans in Generation Z have now become the fastest-growing renter segment in the U.S., which enhances the resilient nature of the multifamily sector.[2]

EXHIBIT 1: MORTGAGE ORIGINATIONS BY CREDIT SCORE



Source: U.S. Census Bureau, Moody's Analytics

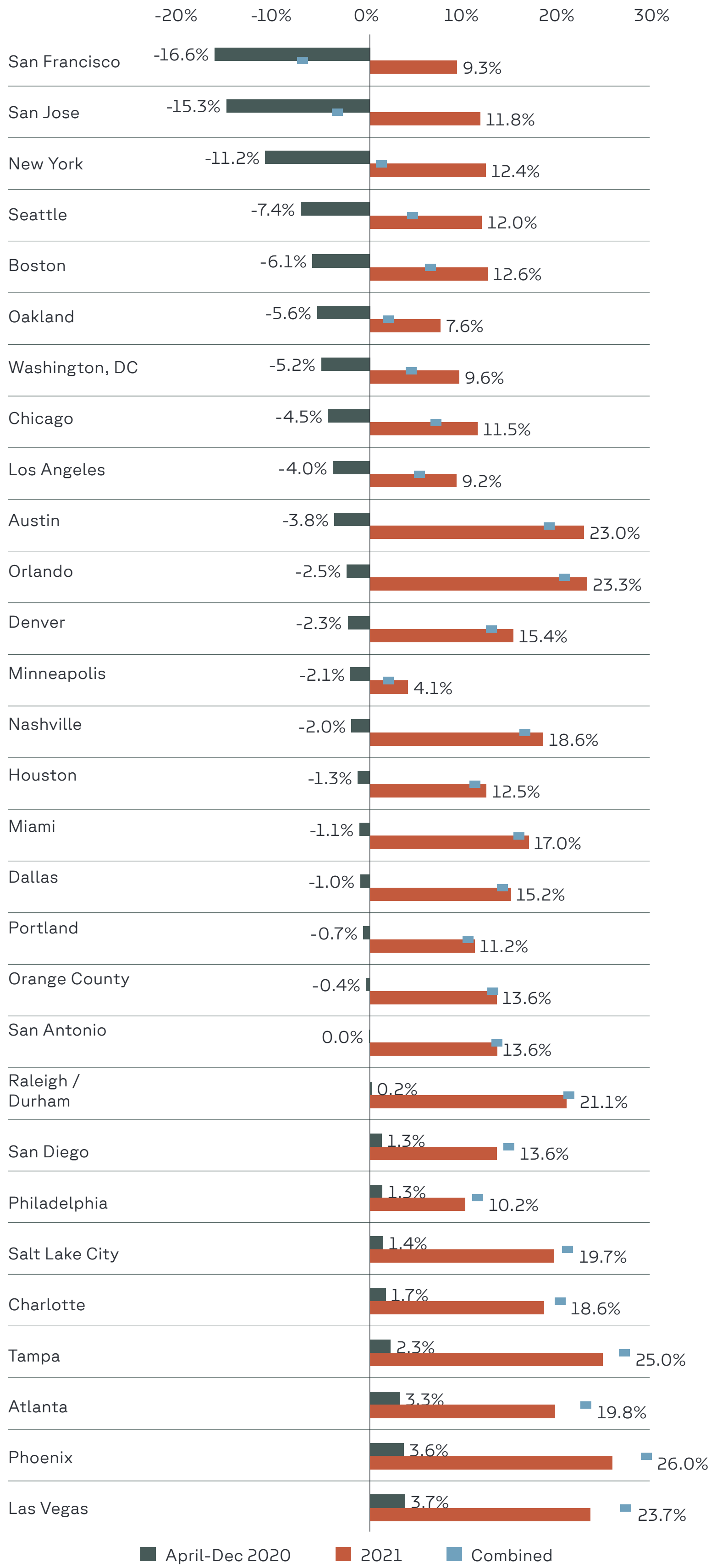
1. TD Ameritrade, June 2020. COVID-19 & Retirement Survey: Impact of the COVID-19 Pandemic on Americans' Retirement Plans.
2. RentCafe. Vibrant Small Towns In America's Heartland Are the Best Cities For Gen Z Renters. Published March 16, 2021.

The labor market remains tight and a point of consternation. The worst of job losses have passed and despite all state economies now fully reopened, effects from coronavirus variants linger and the employment conditions still face headwinds relative to pre-crisis. Inflation has also added pressure to the U.S. economy, spiking to 8.5% at the end of the first quarter of 2022. While it is possible that core inflation, which excludes food and energy, may have peaked in March, inflation is expected to remain above average into 2023. Importantly, multifamily can provide a strong hedge against inflation as rents are continuously adjusted based on current market dynamics. Robust rent growth of the last 12 months in the multifamily sector (**Exhibit 2**) has exacerbated the affordability crisis, which will likely remain a key social concern and area of focus for Affinius Capital when evaluating investment opportunities in the years ahead.

The pandemic had an uneven impact on the multifamily sector by market, asset class, and area by density. Expensive and high-density markets that are dependent on mass transit (e.g., New York City and San Francisco) underperformed in 2020 even in the midst of the recovery. However, starting in 2021, markets across the U.S. experienced a broad-based rebound that witnessed rent growth of 20% or more in certain instances.

These issues, combined with historically weak housing supply, in our opinion suggests that the opportunity in rental housing remains attractive and could increase further as the coronavirus pandemic transitions towards the endemic stage in the U.S., given the significant progress made in vaccinating the overall population and the expanding supply of therapeutics.

EXHIBIT 2: RENT GROWTH OF SELECT MAJOR U.S. MARKETS



Source: AxioMetrics

Prudent Strategy

In some ways, the pandemic validated a key component of our Housing Platform strategy, which is centered around value creation and flexibility. This approach allows us to shift the investment focus between acquisitions and development across rental sectors and layers of the capital stack, at different points of the cycle, and in different markets depending on construction cost relative to market values and the associated risk-adjusted returns. Regardless of the economic catalyst a prudent strategy requires the ability to go where the value creation opportunities are compelling within the rental housing market

Early in a recession, for example, pockets of distressed opportunities could emerge in certain markets or subsectors, leading to the acquisition of core assets at attractive price points. As the economic recovery takes hold, apartment development could create significant value by capturing lower construction cost and better land pricing, while also delivering units during a period of relatively low supply, rising effective rents, and a recovering job market. Similarly, elevated supply in a submarket or high construction cost basis of a project may lead us to invest in high-quality multifamily through preferred equity structures with material sponsor subordination to deploy capital at a reduced basis, thereby offering above-market yields and protection to the investor's last dollar exposure. Further, preferred equity may provide a more optimal capital structure depending on the affordability of senior and mezzanine debt to close any investment financing gap with efficient speed of timing. Our investment focus will shift accordingly, due to a flexibility of strategy incorporated into the platform since its onset.

Thus, we are confident in our ability to maneuver through a dynamic market environment and position portfolios to outperform over the long term, primarily due to this agile approach combined with our knowledge of the market and highly selective and disciplined investment style that is informed by proprietary research and artificial intelligence tools. These include machine learning and predictive analytics that enable dedicated applications to drive better risk-adjusted returns and help identify rental housing opportunities.

Value Creation Philosophy & Defensive Approach

It is our view that a prudent strategy for capturing the value creation opportunity in U.S. rental housing must be flexible, as noted earlier, **while also having a combination of several key attributes:**

- **Maintain a highly selective and defensive**, but active investment stance
- **Adhere to guiding principles** that maintain a focus on market, product, and cost basis while creating value across rental housing sectors and layers of the capital stack
- **Harness the full value creation potential** via active management of the portfolio including strategically monetizing tactical investments, when appropriate
- **Execute asset-specific business plans** to enhance value and drive income growth for long-term holdings
- **Integrate purpose into strategy** and deliver a Green and Attainable Housing product while exceeding financial targets

In the face of geopolitical unrest, rising interest rates, the threat of a looming economic downturn, and a lack of single-family supply, the development of workforce and mid-market rental housing (Attainable Housing) represents a compelling defensive approach for a long-term, strategic investment program.

The following dynamics serve to reinforce this belief:

- **Housing is a necessity** and developing Attainable Housing delivers units at an attractive cost basis to satisfy deeply unmet demand for housing by a large percentage of households in each market, while being well-positioned to generate the attractive long-term risk-adjusted returns.
- **Multifamily presents a hedge against the current risk from inflation** with rents that are marked to market daily and provides investors the benefit from efficient cash flow without the ongoing requirements for tenant improvements and leasing commissions. The sector offers a high degree of liquidity and benefits from a low propensity to buy from potential homeowners.
- **Developing at a meaningful discount to market values** provides 'last dollar' protection against a future period of potential erosion of value, driven by increases in interest rates and pressure on operations during a future downturn. The defensive approach and flexible strategy in housing also includes remaining highly selective and focusing on opportunities that incorporate sufficient contingency and are projected to deliver healthy development spreads. Accordingly, these opportunities are well-positioned to deliver attractive returns and absorb potential cost escalation beyond assumed contingency and cost inflation.
- **Ability to pursue preferred equity structures or debt strategies** further insulates investments.

Looking ahead, we believe that conditions are in place for attractive opportunities to not only emerge in the rental housing sector as a result of the current environment, but they should also endure across economic cycles over the long term. Again, we are focused on being well-positioned to capitalize on attractive rental housing conditions.

Macro Objectives – Building on a Legacy of Leadership

Doing well and doing good are not mutually exclusive; they can be interconnected. Seeking opportunities for integrating social benefit into investment strategy and combining profit with purpose by pursuing a triple bottom line – profit, people, and planet – can lead to what's been referred to as a "higher kind of capitalism."[3] It is about emphasizing the intersection of strong investor returns and purpose-driven decisions that ultimately deliver social and environmental benefits while enhancing the financial results. In doing so, the business serves a greater purpose and builds a shared value for multiple stakeholders, in scale.

Creating rental housing in the U.S. offers the opportunity for doing good by addressing two of society's pressing problems:

1. Reducing the deficit in Attainable Housing and meeting deep demand from price-sensitive renters by providing more housing supply at price points for rents that are affordable to a larger percentage of the renter households in each market.
2. Mitigating the impact of the building sector on the environment by constructing sustainable apartment developments that meet green standards and utilize innovative design tools and construction techniques ("Green Housing").

After all, the building sector has long been plagued by inefficiency and waste and is responsible for contributing 40% of the greenhouse gas emissions that have fueled climate change over the years.[4]

Conclusion

Our housing platform is designed to take advantage of our core creation capabilities in the face of market disruptions, which from our experience ultimately leads to value-creation events. As the Commercial Real Estate (CRE) market has stabilized following the rapidly evolving conditions caused by COVID-19, we will also aggressively seize on opportunities that reflect our primary themes across the investment spectrum.

3. Michael Porter and Marc W. Pfitzer: The Ecosystem of Shared Value – Harvard Business Review October 2016.
4. IEA. Global Status Report for Buildings and Construction 2019. www.iea.org.

"The housing platform strategy is to capitalize on a sharp supply and demand imbalance in U.S. rental housing and capture a significant value creation opportunity for our investors through ground-up development and value-add acquisitions along with creating a geographically diverse and sustainable portfolio that is overweighted to Workforce and Mid-Market housing and what we are referring to as 'Attainable Housing'."

— Hailey Ghalib, AIA

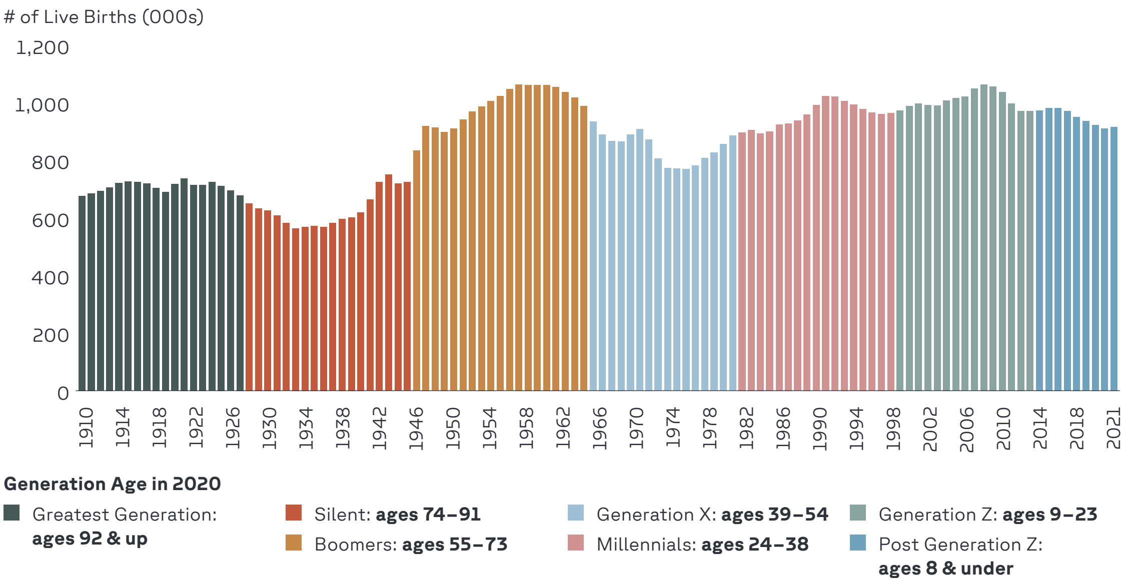
**EXECUTIVE MANAGING DIRECTOR,
HEAD OF HOUSING INVESTMENT AND DEVELOPMENT**

MARKET OVERVIEW

Demographics Drive Demand

The Millennial generation, approximately 73 million people, is the largest cohort in the U.S. labor force, and nearly 65% of them are renters today. This group consists primarily of young people in their late 20s and 30s who have delayed getting married and having children relative to previous generations, while overwhelmingly opting to rent versus own a home. **Due, in part, to entering the workforce during the Global Financial Crisis (GFC), the Millennial cohort has experienced financial hardships, including record levels of student loan debt and difficulty saving for a down payment required to purchase a home.** A TD Ameritrade retirement survey from 2020 found that 46% of Millennials say they are still financially recovering from the Great Recession of 2008.[5] This group not only dealt with the GFC but also the most recent downturn, which only reaggravated their inability to financially qualify for homeownership. Therefore, Millennials will likely rent for an extended period of their lifetimes relative to previous generations, evidenced by the median age (45 years old) of first-time homebuyers climbing to its highest point since 1981 in 2021.

EXHIBIT 3: DEMOGRAPHIC COHORT SIZE IMPACTS HOUSING DEMAND



Source: U.S. Census Bureau, Moody's Analytics

Over the next decade, we expect Millennial family formations will gain momentum, and some members of this cohort will begin to transition to single-family housing – prioritizing attributes such as school district quality, yard size, and privacy. At the same time, Generation Z (the post-Millennial cohort) has begun to backfill the apartment space vacated by Millennials. Demographers have yet to agree on a start/end date for the post-Millennial generation. Still, it is generally considered that the cohort began between 1995-1997. For the sake of this paper, we will reference 1997-2012 as the Generation Z age, as defined by Pew Research Center (a leader in demographic studies); however, it is worth mentioning that the official start/end period could change at a later date.[6] According to Moody's, approximately 65 million births occurred during Generation Z's era, which is four million more than the comparable 16-year reign (1981-1996) of the Millennial cohort. **As such, the nearly 67 million Americans in Generation Z have now become the fastest-growing renter segment in the U.S.** However, the Millennials' transition to single-family homeownership could be delayed, given COVID-19's impact on the broader economy and resulting in increased competition in the single-family residential market. Thus, rental housing demand should increase substantially to accommodate the larger Generation Z cohort, as well as the resilient number of Millennials who will become longtime renters.

5. TD Ameritrade, June 2020. COVID-19 & Retirement Survey: Impact of the COVID-19 Pandemic on Americans' Retirement Plans.
6. Defining Generations: Where Millennials end and Generation Z Begins, January 2019, Pew Research Center. Pewresearch.org

Meanwhile, an increasing number of Baby Boomers and members of the Silent Generation are aging into senior housing. **An average of 10,000 Baby Boomers reach retirement age every day, and this trend will continue into 2030. Furthermore, the number of people over the age of 75 is forecasted to almost double from 21 million today to over 40 million by 2035. Collectively, these favorable demographics will continue to spur rental demand across the housing spectrum.**

Significant Supply Shortage

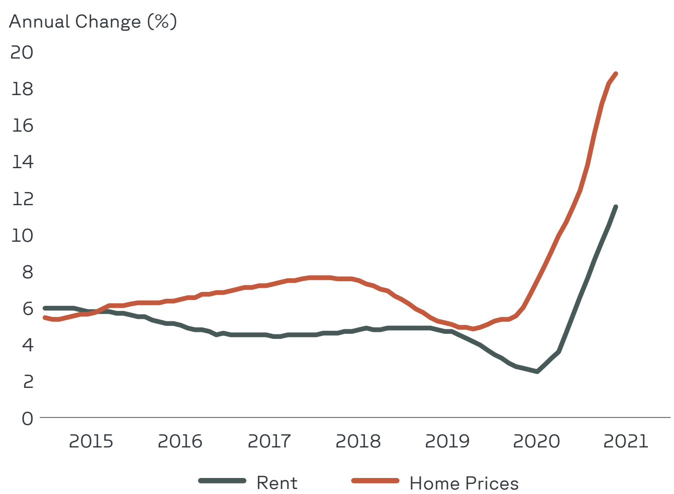
From a supply perspective, the fundamentals continue to favor investment opportunities in the housing sector, given that the market is woefully undersupplied. From 1980-2008 the U.S. averaged nearly 1.5 million total housing completions, including both single-family homes and apartments. Over the next decade, the economy produced an average of only 870,000 units annually – a shortage of nearly five million homes during those 10 years when compared to the long-run average. As of early 2022, total housing completions were approaching a relatively healthy pace of roughly 1.3 million units, their highest level since 2007. However, rising construction costs combined with higher interest rates should reduce the likelihood of overbuilding.

Before the global pandemic, the housing market's supply/demand fundamentals were already out of balance. Historically, new housing starts have outpaced household formation growth. From 1960-2016, there were 11 new housing units built for every 10 households formed. This dynamic allowed for vacancies, demolition due to obsolescence, and owners of second homes; thus, there was not an issue with oversupply.

The slow recovery in housing starts compared to household formations that occurred between 2010-2016 has contributed to the inadequate housing supply that persisted until more recently. Further, supply chain challenges have resulted in increased and more volatile material prices, leading to further escalation in residential homes prices, effectively locking many first-time buyers out of the market (per **Exhibit 4**).

Various factors contribute to this situation, such as anti-development sentiment with communities limiting zoning for dense residential housing due to pressure on public facilities (e.g., schools, hospitals, and transportation systems). More recently, rising materials and land prices have negatively impacted constructions costs. Consequently, without innovative and collaborative solutions (which we will discuss in the Workforce Housing: Tackling the Cost Issue section), the current housing shortage will likely intensify over the long run as the robust demographic tailwinds continue to take hold.

EXHIBIT 4: SOARING HOME PRICES HAVE OUTPACED RENT GROWTH



Source: Joint Center for Housing Studies at Harvard University

SECTOR INSIGHTS

Apartments: A Multi-Dimensional Story

Over 43 million U.S. households rent their homes today (an all-time high).[7] The nation will add approximately 12.2 million new households over the decade, from 2018 to 2028.[8] **If the current renter-to-household ratio holds steady around 36%, the market would require nearly 4.5 million new units over that period, or an average of almost 450,000 units per year, to maintain a healthy supply/demand equilibrium. While this estimate includes all major rental types (i.e., condos, duplexes, and multifamily), it does not account for losses in inventory due to obsolescence for example, meaning the need for rental units could be even higher.** The apartment sector has become an increasingly important part of the rental housing mix, delivering 374,000 units in 2021 – the second-highest level since CoStar started tracking this data in the year 2000, following last year's 435,000 units. Over the last five years, new construction averaged 342,000 units annually. Per Axiometrics, the U.S. multifamily sector absorbed over 666,000 units in 2021, more than twice the annual figure averaged over the past five years through 2020, and it significantly outpaced the number of new units delivered last year. As a result, vacancy levels dropped from 4.4% a year ago to 2.6% as of the fourth quarter of 2021 after staying in the 6.1-6.7% range from 2015 through early 2020.[9] When considering the financial obstacles delaying homeownership for first-time homebuyers, a cultural/demographic shift toward rental housing, and a single-family housing market that is dealing with its own set of evolving challenges, the apartment sector is well positioned to benefit from considerably more renter demand going forward.

Even in the wake of COVID-19, high-quality properties in the multifamily sector outperformed the broader market. Per the National Multifamily Housing Council ("NMHC"), which tracks 11.5 million institutionally managed properties in the U.S., collections have been substantial– 98.2% of rent was paid in 2020 and 2021 versus 2019 before the onset of COVID-19. Consistent with the trend observed in the prior cycle, the multifamily recovery has outpaced most other commercial real estate sectors due to its efficient cash flow and diverse tenant base. Additionally, Class A and B properties experienced better rent collections than Class C given low-wage workers were disproportionately impacted by job losses early in the pandemic.

Ultimately, markets with diverse economic drivers and strong population growth will likely outperform over the long term, even if supply levels rise above the historical average in the near term. Finding success in this sector will heavily depend on an investor's ability to align the appropriate rental product at the right price point for a given submarket. For example, **Exhibit 5** classifies renter households in the Denver metro based on various affordability price points.

We believe the most attractive opportunities over the next decade will occur primarily around the Middle-Market and Workforce pricing segments (per **Exhibit 5**), referred to as "Attainable Housing." These market segments reduce the deficit in Attainable Housing and meet deep demand from price-sensitive renters by providing more housing supply at price points that are affordable to a larger percentage of the renter households in each market, while generating strong returns for our investors.

7. Number of renter occupied housing units in the United States from 1975 to 2020, February 2022, Statista. www.statista.com.
8. Updated Household Growth Projections: 2018 – 2028 and 2028 – 2038, December 2018, Joint Center for Housing Studies of Harvard University. Jchs.harvard.edu.
9. Data per Axiometrics. As of Q4 2021.

EXHIBIT 5: RENTER HOUSEHOLD CLASSIFICATIONS RELATIVE TO AFFORDABLE MONTHLY RENT LEVELS

PREMIUM:

The highest rent range within a major market and often accounts for 15-25% of renter households.

MIDDLE-MARKET:

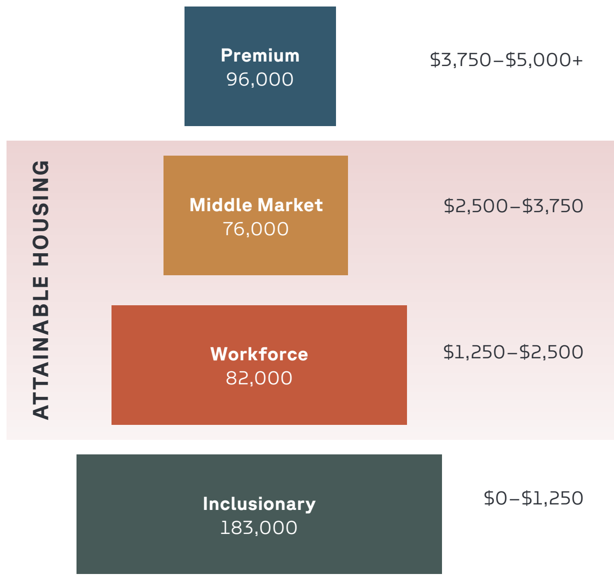
The centerpiece of a critical price point segment that we believe is an attractive investment opportunity over the long run, generally accounting for 15-25% of renter households in major markets.

WORKFORCE:

For the sake of this analysis, it is housing that is affordable for those making 80-120% of an area's median income (AMI) and typically accounts for 15-35% of renter households in major markets.

INCLUSIONARY:

For the sake of this analysis, it includes renters making below 80% of AMI. It is associated with affordable housing programs intended for lower-income families, typically accounting for 35-50% of renter households in major markets.

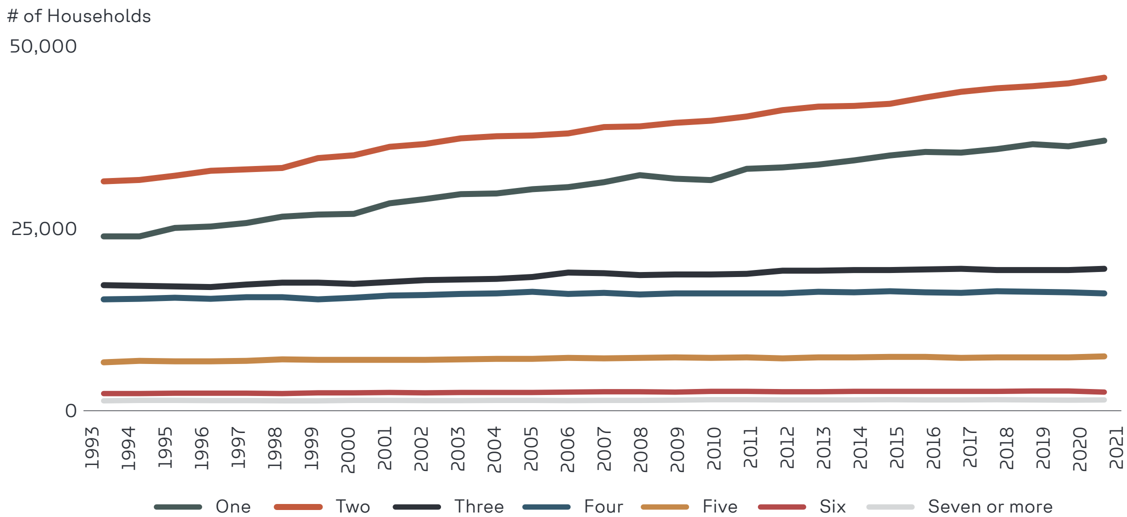


This exhibit uses the Denver market as a proxy, and household rent assumptions are based on 30% of Gross Household Income.

Source: Affinius Capital Research reporting via Environics demographics data and Moody's Analytics as of April 2021.

The rise in single-person households reflects a shift in the nation's family structure and its renter profile. As of 1975, this group accounted for 19% of households and has since risen steadily, to 28% or 37 million households in 2021. This change in household structures is due to various factors such as older adults living alone and younger adults delaying marriage and having kids, which bodes well for rental housing demand.[10]

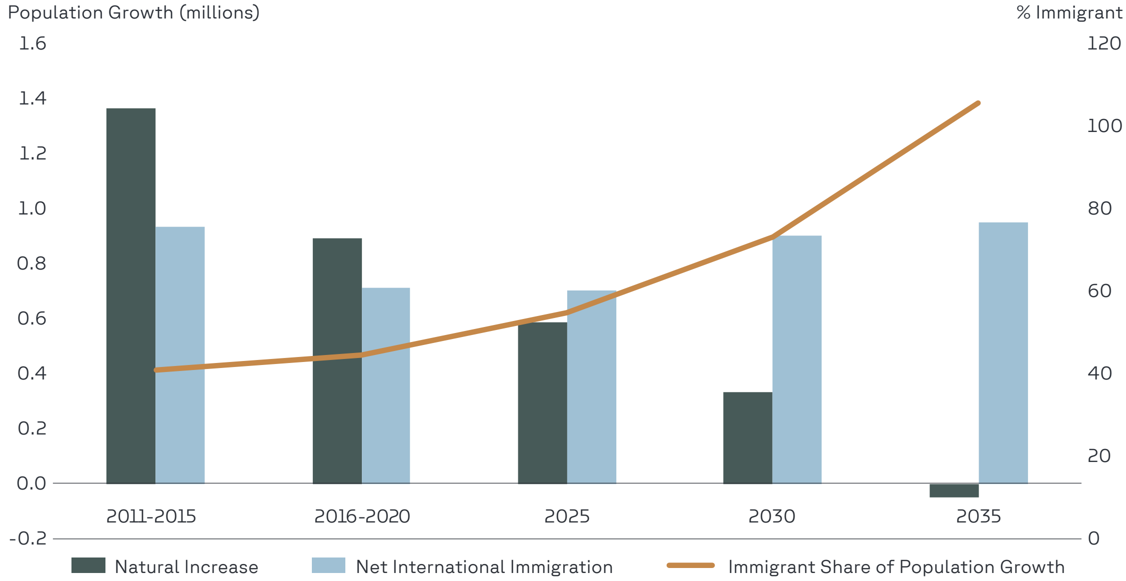
EXHIBIT 6: SINGLE PERSON HOUSEHOLDS ON THE RISE



Source: For more information about ASEC, including the source and accuracy statement, see the technical documentation accessible at: https://www.census.gov/programs-surveys/cps/technical-documentation/complete.html

10. U.S. Census Bureau. New Estimates on America's Families and Living Arrangements, November 2021.

EXHIBIT 7: IMMIGRATION IS A KEY DRIVER OF POPULATION GROWTH



Source: U.S. Census Bureau, Moody's Analytics

In the U.S., immigration will become a significant driver of population growth in the coming years, which in turn could deliver a steady stream of potential renters. **By 2030, immigrants will account for 15.1% of the population, the highest level since the U.S. Census began tracking this data in the 1850s.** Additionally, the year 2025 marks a turning point as net immigration is projected to overtake natural increases (the excess of births over deaths) as the primary driver of population growth for the country.[11]

Consequently, the apartment sector should be less impacted by the overall decline in population growth, given the steady flow of immigrants into the U.S.

In 2021, President Biden lifted the previous administration's executive order that suspended entry into the country for certain immigrants temporarily in the wake of the coronavirus.[12] This initiative was a short-term measure because the U.S. economy will rely heavily on immigrants in the years ahead, especially as disruption caused by the novel coronavirus to international supply chains and manufacturing drives future repatriation of these functions. Under the current administration, we believe that having a strong immigrant pipeline will play a vital role in the years ahead. Ultimately, the multifamily sector's demand drivers (e.g., favorable demographics, evolving family structures, and a stable immigration growth) should support the sector's momentum over the next decade and beyond.

Workforce Housing: Tackling the Cost Issue

What is workforce housing? The criteria surrounding workforce housing tends to vary by region, but most definitions are based on housing affordability for those making near the median household income of a particular area. For the sake of this paper, we will define workforce housing as rental units that are affordable to households earning 80-120% of the area's median income, assuming tenants spend 30% of their income on housing. **Workforce housing is often associated with the ability of essential employees – such as emergency personnel, healthcare professionals, and teachers – to find reasonably-priced accommodations in their respective communities.**

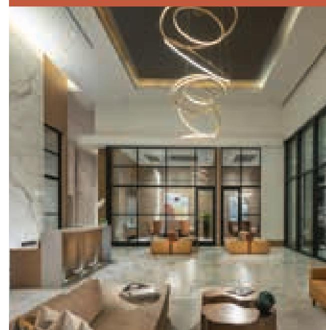
11. U.S. Census Bureau. Population Estimates and Projections. Revised February 2020
12. A Proclamation on Suspension of Entry, November 2021, White House. Whitehouse.gov.

Today, workforce housing encompasses an even larger group (e.g., young professionals, retail sales personnel, some office workers, and service workers). All of them have found it increasingly difficult to afford housing in both urban and rural areas. According to the Joint Center for Housing Studies, 44 million homes in 2019 (14% more than in 2009) were "cost-burdened," meaning they spent more than the recommended industry standard of 30% on housing. In the aftermath of COVID-19, this already dire situation has been amplified by elevated levels of inflation coupled with residential home prices at all-time highs, as measured by the S&P Case-Shiller U.S. National Home Price Index. Given that nearly 60% of U.S. households were living paycheck to paycheck before the pandemic, it is reasonable to expect affordable housing to remain both a critical social issue and potential investment opportunity in the years ahead as the economy normalizes.

Several other factors have also contributed to the affordability issue. To start, the increased demand for rental housing has led to rising rental prices that have outpaced wage increases across the country. While apartment construction has been near record levels in recent years, most of the new deliveries focused on Class A product that typically has rents that fall outside what would be considered practical for the average U.S. household. Affordability issues have even begun to limit rental growth in Premium Class A product in some submarkets and urban centers as well. Lately, residential home-ownership costs have exceeded the above average levels of multifamily rental rate increases.

Market participants have struggled to provide a comprehensive and viable solution to the affordability crisis that also meets commercial return requirements. Still, investors are beginning to take a more innovative approach to this issue, particularly regarding new development. Aside from delivering inclusionary housing as part of established local zoning requirements on new ground-up developments in certain cities, possible solutions could include:

- Technology-driven construction methods that could potentially lower construction costs and reduce delivery schedules
- Creation of mixed-use, ex-urban nodes to ease pressure on urban centers while offering an affordable solution
- Public-private cooperation to encourage and facilitate more housing that helps offset high land prices
- Corporate sponsorship of affordable housing initiatives



The multifamily sector ultimately benefitted from the pent up demand created by COVID-19.

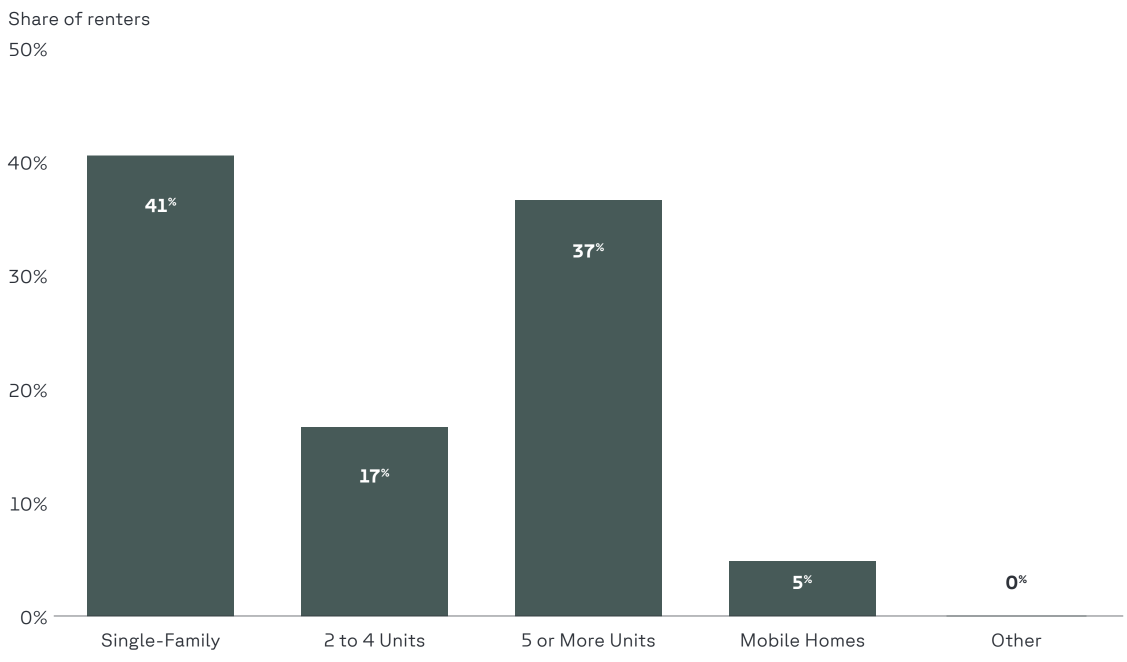
Young people have been a critical driver in the revitalization of the urban core during the most recent cycle, especially in large metro areas like New York and San Francisco. However, the pandemic temporarily made these areas less attractive, given the difficulty of quarantining in small apartments that are also relatively expensive compared to suburban options that offer more space. This situation was further compounded by work-from-home policies that have been extended due to the health crisis, allowing many professional office employees to work remotely into 2022 and possibly beyond. In the near term, this situation allowed for a short-lived tactical buying opportunity in select submarkets, as values softened on slowing demand due to the unique conditions created by the health crisis.

To reiterate, Affinius Capital is committed to integrating purpose into strategy and integrating benefit with profit by addressing the affordability crisis in the United States. Continued strength in residential home prices and large increases in multifamily rents, in addition to a volatile economic landscape and other socio-economic factors, have contributed to roughly half of all renter households being cost-burdened.[13] We will focus on Attainable Housing that delivers supply that is affordable to a large percentage of households in each market, bolstering current practices and strategies that drive the bottom line, while supporting a commitment to society and the environment.

Single-Family Rental: Reshaping the American Dream

Today, single-family detached homes account for more than 62% of the housing stock in the U.S. While most of these houses are owner-occupied, single-family rentals have long played a critical role in the housing market. Approximately 20% of single-family homes were rentals during the 1970s. The number of renters declined during the 1990s as easing credit standards and falling interest rates made buying a home more accessible. In the wake of the GFC, single-family rentals expanded rapidly. In the 10 years between 2006 and 2016, nearly four million additional households became renters of single-family homes. **Over the last 10 years, the single-family rentals sector one of the fastest-growing segments of the housing market.**[14] **As of 2019, approximately 41% of renters in the United States lived in single-family homes (Exhibit 8).**

EXHIBIT 8: DISTRIBUTION OF RENTAL ACCOMMODATIONS IN THE U.S. BY STRUCTURE TYPE (2019)



Source: Statista

While in our opinion the GFC may have reignited today's rental housing revolution, this trend will rely heavily on demographic tailwinds going forward, mainly from Millennials for the time being. **This generation represents the largest cohort in the workforce today, and they will likely follow in the footsteps of previous generations and eventually marry, have kids, and gravitate toward single-family homes, but not necessarily as buyers.** As noted earlier, this group has generally faced significant financial challenges (e.g., record levels of student loan debt, poor credit scores, and difficulty saving for a down payment). These conditions could limit their ability to purchase a home as they transition into the next phase of life. Thus, many Millennials are expected to rent versus own a single-family home over the next decade, mostly out of financial necessity.

13. Joint Center for Housing Studies of Harvard University. The state of the Nation's Housing 2021.
14. Housing Supply Chartbook, January 2020. Urban Institute. www.urban.org.

The construction of purpose-built, single-family neighborhood rentals offers what we view as a compelling opportunity to capitalize on the previously described conditions. Unlike the assemblage of disparate homes, purpose-built, single-family rentals provide a viable solution for consumers who cannot afford to purchase a home, while also providing investors/owners with operational efficiencies, a consistent renter experience, and opportunities for amenitization. This type of emerging housing opportunity suggests that the single-family rental market has significant investment potential going forward.

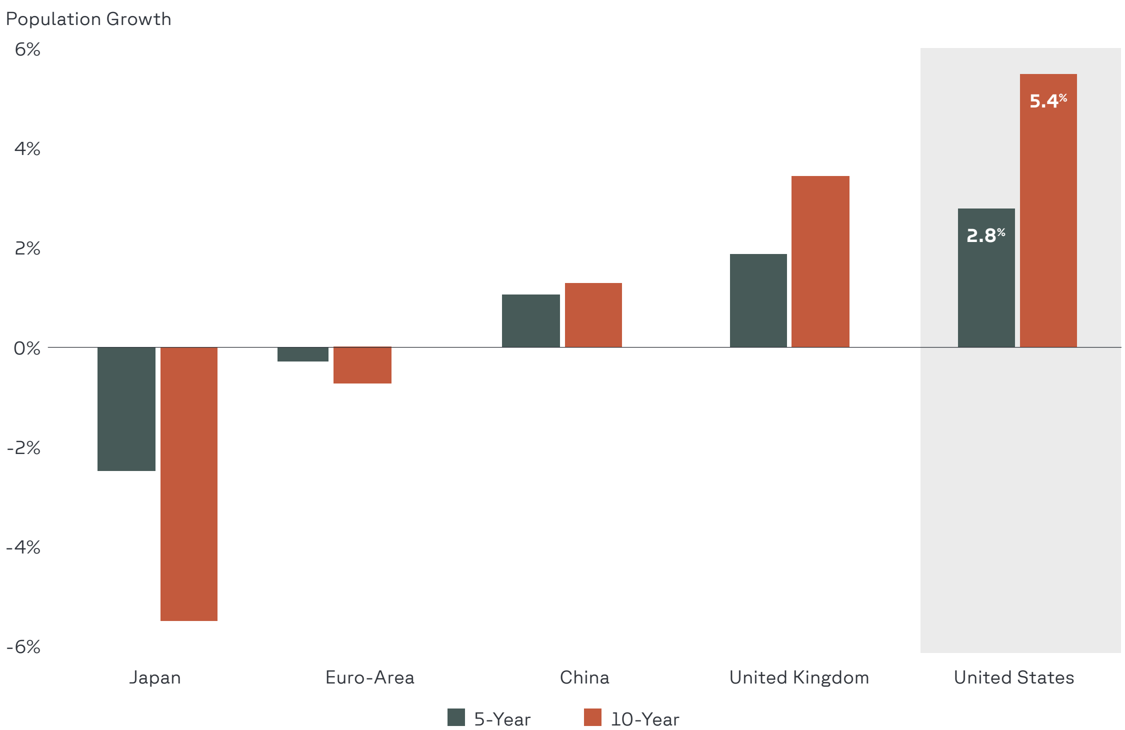
MACRO FACTORS

Looking Ahead: Key Issues in the Next Decade and Beyond

The following factors have historically influenced U.S. housing conditions, and investors should be mindful of these issues when considering a long-term housing investment program:

Population Growth: The pace of population growth is arguably one of the most critical demand drivers across all major segments of the housing market. An increase in a market's population tends to be associated with an uptick in job growth, which ultimately impacts the demand for housing across all sectors. The U.S. population growth rate has gradually declined over the last several decades; however, the long-term forecast ranks near the top among advanced economies (see **Exhibit 9**). In absolute terms, the U.S. population will top 355 million by 2030, 24 million more than in 2020.[15] Furthermore, the nation's steady immigration growth will help buffer multifamily and other rental housing sectors against slower population growth. From a global perspective, the U.S. housing market offers investors other attributes as well – a resilient economy, highly-developed legal system, strong corporate governance, and healthy liquidity. Therefore, the U.S. housing market remains an attractive investment opportunity on both a relative and absolute basis.

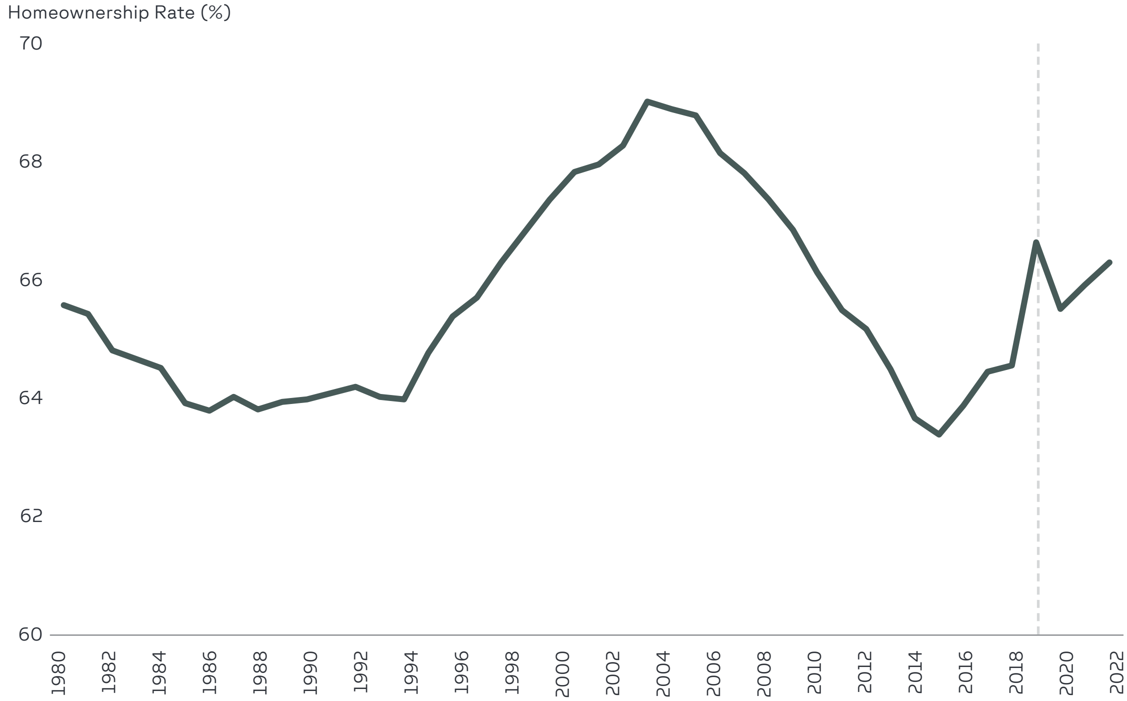
EXHIBIT 9: U.S. POPULATION GROWTH FORECAST OUTPACES OTHER ADVANCED ECONOMIES



Source: World Bank

15. U.S. Census Data.

EXHIBIT 10: U.S. HOMEOWNERSHIP RATE AROUND HISTORIC AVERAGE



Source: U.S. Census Bureau (BOC); Moody's Analytics Forecasted

Policy Initiatives: Government policy will have an ongoing influence on the housing market. By way of example, given the significant impact that the coronavirus has had on the housing market, the U.S. government helped to prevent a single-family housing crisis like the one that occurred during the GFC. Government officials provided forbearance for nearly 15 million loans to keep foreclosures to a minimum. The government agencies (e.g., FHA, Fannie Mae, and Freddie Mac) account for about 70% of outstanding mortgages, and they allowed homeowners to receive up to 12 months of forbearance. While the remaining 30% of lenders may not be as forgiving, the government's approach should hold the homeownership rate steady at around 65%, still below the 2004 high of 69.2%. Additionally, Government Sponsored Entities (GSEs) have been a reliable source of liquidity and low cost of capital in the multifamily sector. Since 2007, they have more than tripled their lending balances from $235 billion of multifamily loans outstanding to over $750 billion as of the start of 2020.

> "This crisis highlights that a flexible strategy, capable of capturing value across the spectrum of rental housing sectors through development and acquisitions, remains an effective approach for responding to emerging and changing opportunities across this and future economic cycles."
>
> — Hailey Ghalib, AIA
>
> **EXECUTIVE MANAGING DIRECTOR,**
> **HEAD OF HOUSING INVESTMENT AND DEVELOPMENT**

This represents more than 2x the growth of any other source of lending capital during this period. Over the last decade, there have been ongoing discussions regarding the potential privatizations of the GSEs, which is an issue that investors should monitor, given the potential impact on the housing credit market. Furthermore, while longstanding inclusionary housing policies (such as entitlements for new developments) are a viable path to delivering affordable housing in many cities, abrupt changes in these requirements or rent stabilization laws run the risk of creating an environment of uncertainty – limiting new supply and exacerbating the problem they were intended to resolve. **Ultimately, while the current socioeconomic and demographic tailwinds suggest that homeownership rates will fluctuate in the near term, prudent investors must be mindful of evolving political and regulatory factors that could impact housing conditions.** As shown in **Exhibit 10**, homeownership rates have increased more recently due to dynamics related to COVID-19 combined with historically low mortgage rates as a result of dynamics related to COVID-19; however, the recent rise in mortgage rates should begin to push homeownership back towards pre-crisis levels.

Economic Outlook: Recessions have occurred approximately every seven years on average since the 1960s, and any long-term housing investment strategy will almost certainly face an economic slowdown. The U.S. economy is unique relative to other advanced countries in its resilience following a recession. For instance, the U.S. was the first advanced economy to emerge from the GFC and has experienced the most robust GDP growth amongst that group over the last decade as well. Further, the nation's recovery from the recent coronavirus-induced recession was the strongest in history. The U.S. has the youngest population among countries with advanced economies, which should fuel GDP growth and serve as a catalyst for solid economic growth on a secular basis. The U.S. economy is projected to grow at a more normalized rate of 3.0%, and then 2.0% in 2022 and 2023, respectively.[16]

The interest rate environment is rapidly evolving in relation to high inflation, looming interest rate hikes, and receding federal monetary and fiscal support. Over the past six months, the 10-Year Treasury rate has increased by approximately 120 basis points. More recent events have driven the 10-Year Treasury yield to over 2.90% and this key benchmark is expected to reach as high as 3.50% in 2023 on the heels of an aggressive series of rate hikes by the Federal Reserve (Fed).

The Federal Open Market Committee (FOMC) released their recent meeting minutes in April, revealing that officials envision a series of 50 bps rate hikes to quickly return policy to a more neutral level. The Fed is expected to hike interest rates six times in 2022. The Fed is then likely to maintain a healthy series of four additional 25 bps hikes in 2023. As such, interest rate expectations have risen and markets now anticipate the Federal Reserve will hike the Federal Funds Rate to 2.00% by the end of 2022 and between 2.50-3.00% by the end of 2023.[17] We believe the 10-Year Treasury rate will settle back into the mid-2% range and remain low relative to historic averages for the medium- to long-term. As economic growth slows and governments deal with the massive level of debt accumulated in recent year, central banks will be compelled to keep interest rates low.

16. Capital Economics. 2022: High Inflation to Drive U.S. Policy Tightening. Published January 5, 2022.
17. Capital Economics. US Economic Outlook. Economy will bend not break under higher rates. Published April 12, 2022. www.capitaleconomics.com/clients/publications/useconomics/us-economic-outlook/economy-will-bend-not-break-under-higher-rates/

Intersection of Real Estate & Technology: **The intersection of real estate and technology is an important focus for Affinius Capital. This theme encompasses several key functions (Investment Execution, Business Operations, and Management), as shown in Exhibit 11, that will play a vital role as the industry continues to evolve in the years ahead.** In addition to innovative construction techniques, as mentioned earlier, we have focused our efforts on machine learning and predictive analytics that enable dedicated applications used to identify rental housing opportunities. These tools also provide better visibility into the economic and business cycles while enhancing our understanding of relative investment risk across property markets – including downside protection measures at the asset level during our underwriting, due diligence, and property operations. Therefore, in time, the more sophisticated managers will balance the use of technology as a tool to enhance the decision-making process across different stages of an investment against their institutional knowledge and human intuition.

EXHIBIT 11: OPPORTUNITIES FOR TECHNOLOGICAL ENHANCEMENT IN COMMERCIAL REAL ESTATE BY FUNCTIONAL AREA

INVESTMENT EXECUTION	BUSINESS OPERATIONS	MANAGEMENT
Market data and analysis	Revenue management tools	Facility and building management
Predictive analytics	Valuation and appraisals	Capital projects management
Automated workflows	Real-time data harvesting, analytics and reporting	Asset and portfolio management
Construction methods and materials	Mortgage lending	Lease and tenant management

Source: Affinius Capital Research

INVESTMENT PERSPECTIVE

Execution & Strategy: A Prudent Approach

A demographic coalition – consisting of Millennials, Generation Z, and aging seniors within the Baby Boomer and Silent Generation cohorts – combined with insufficient housing supply in our view has given rise to enduring investment opportunities across the rental housing spectrum (e.g., Premium, Middle-Market, Workforce, and Single-Family Rental) that should persist for many years to come.

We believe that it is prudent to consider the entire rental housing market (including all the major sectors as noted earlier) as a cohesive housing platform opportunity, with an emphasis on investments that primarily target middle-market and workforce rents (per **Exhibit 5**) while maintaining a keen focus on location, quality, and other differentiation attributes. **This approach allows investors access to a deep pool of potential renters in each market while focusing on the sectors that serve the most significant population segments, provide the highest renter demand, and offer attractive long-term risk-adjusted returns.** This method is appropriate primarily because the housing market is multifaceted, fluid, and shaped by several complex factors (e.g., an evolving demographic landscape, government policy, consumer preferences, and economic cyclicality).

Multifamily housing should continue to generate strong performance even in a rising rate environment, benefiting from, among other things, the likely slowdown in home sales. In a recession, leasing demand would cool but given that many submarkets continue to be undersupplied, we believe absorption will remain relatively strong. Depending on the severity and duration of a possible recession, we could see a slowing of rent growth as tenants may seek lower cost alternatives, but again given the combination of supply shortages together with demographic tailwinds, we expect sustained demand over the long-term.

As cap rates stabilize, we expect investor interest will remain strong because of the inflation protection and consistent income offered by this sector, and we continue to believe that the value creation provided by development offers attractive risk-adjusted returns at a cost basis below the cost of core investments. Finally, even as construction costs rise and values flatten or recede slightly, we believe a satisfactory spread will be maintained between the cost of new construction and the value of core multifamily.

Based on this view of the supply demand dynamic and expected liquidity, we remain bullish on build to core and value-add strategies in rental housing. However, we will also actively monitor the market to determine if rising rates or a more severe recession might generate opportunities to acquire high-quality assets at prices below replacement cost.

We believe rental housing is an attractive long-term investment mainly due to the following attributes:

1. HAVING AN EFFICIENT CASH FLOW,
2. BEING AN EXCELLENT INFLATION HEDGE,
3. AND PROVIDING RENT GROWTH THAT HAS HISTORICALLY OUTPACED INFLATION.

Over an extended period, the various underlying housing sectors will eventually present more significant opportunities for value creation and risk-adjusted returns depending on the market and the timing in the economic cycle. **Therefore, a flexible, value-oriented strategy that seeks rental housing opportunities in different markets at various points in the cycle and can allocate capital across the rental housing spectrum and layers of the capital stack has the potential to outperform.** Furthermore, it allows for both strategic and tactical investing and geographic diversity, all while focusing on segments where the opportunity for value creation is the greatest.

Successfully capitalizing on the U.S. rental housing opportunity in a post-COVID-19 environment requires the ability to recalibrate an investment focus as market conditions fluctuate, understand the demand drivers within each underlying housing sector, and recognize how macro factors influence the investment environment. This approach allows investors to remain nimble and to respond quickly to where the greatest rental housing opportunity is, in a given market, or point in the cycle. Additionally, Affinius Capital will leverage its access to the technology sector (as highlighted in the Intersection of Real Estate & Technology section) to execute the housing platform strategy – specifically regarding the issue of construction costs and housing affordability.

Thus, given this environment, we believe conditions are in place to capitalize on enduring investment opportunities within the U.S. rental housing market in the years ahead.

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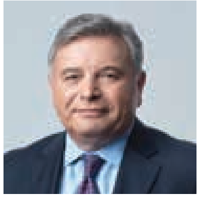

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