APARTMENT INDEX

APARTMENTS CONTINUE TO BE A MODEST DRAG ON THE OVERALL NCREIF PROPERTY INDEX

The NCREIF Apartment Subindex reported a quarterly total return of 1.54% and a one-year total return of 6.46%, as of 2Q18. Although the second quarter total return was 10 basis points ("bps") higher than the same period one year ago, it remains well below the stellar performance (i.e., double-digit annual returns) enjoyed by the apartment sector six years in a row from 2010 through 2015. And it continues the trend of underperformance, vis-à-vis the NCREIF Property Index (NPI"), plaguing apartments since 2012.

Apartments came out of the Great Financial Crisis with three years (2010, 2011, and 2012) of significant outperformance (i.e., 233 bps per year, on average), but have underperformed on an annual basis since then by an average of 95 bps per year through 2017. Year-to-Date ("YTD") through June 30, 2018, the Apartment Subindex has delivered a 3.06% total return, 48 bps less than the NPI's total return of 3.54%.

This deceleration in the total return is substantially attributable to a drop in the appreciation component of the return. From 2010 through 2015 appreciation averaged 7.4% per year while income averaged 5.3% per year. In the two-year period of 2016 and 2017, appreciation averaged 2.2% per year, 520 bps lower than the average rate enjoyed during the previous six years. At the same time, income averaged 4.5% per year over the 2016/2017 time period, just 80 bps lower than the previous six-year average.

The slowdown in appreciation for the NCREIF Apartment Subindex is geographically widespread, i.e., five of the NPI's eight sub regions: East North Central, Mideast, Northeast, Southwest, and West North Central were a drag on the Subindex's appreciation component both YTD and over one-year. However, the Mountain, Pacific, and Southeast sub-regions all experienced substantially greater appreciation for the quarter, YTD, and one-year periods than the Subindex.

Likewise, not all Apartment Subtypes are created equal. Specifically, Garden-Style Apartments (one of three Apartment Subtypes, along with HighRise and LowRise, tracked by NCREIF) have been an impressive bright spot within the Apartment sector outperforming the broader Apartment Subindex by 77 bps during the second quarter, 137 bps YTD, and 311 bps over the past year. Conversely, HighRise Apartments, which account for approximately 62% of all Apartment properties (by value) in the Apartment Subindex, have been abysmal performers of late. Specifically, HighRise Apartments have delivered second quarter, YTD, and one-year total returns of 1.19%, 2.42%, and 4.92%, respectively. Those returns are 35 bps, 64 bps, and 154 bps lower than the overall Apartment Subindex for those time periods.

Notwithstanding a decline in the appreciation component of returns, supply and demand, in general, are in balance. According to CBRE Research, year-to-date construction completions (276,000 units) and absorption (249,000 units) are at cyclical highs. Despite construction outpacing absorption, vacancy remains low (4.7%) and has only increased by 10 bps, year-over-year. Solid fundamentals should provide security to the apartment sector's income component for the foreseeable future, though appreciation may remain difficult to come by.

Geoff Esmail
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APARTMENT TOTAL RETURNS

	Total NPI	Total Apartment	East	Midwest	South	West
2nd Q 2018	1.81	1.54	1.26	1.31	1.56	1.83
1st Q 2018	1.70	1.50	1.33	0.96	1.86	1.57
One Year	7.19	6.46	5.11	4.40	6.86	8.01
Three Years	8.25	7.48	5.89	5.58	6.97	9.96
Five Years	9.77	8.78	6.85	7.75	9.11	10.81
Ten Years	6.22	6.23	4.32	6.97	7.01	7.46
Twenty Years	9.19	9.08	8.77	8.47	9.04	10.15

APARTMENT INCOME RETURNS

	Total NPI	Total Apartment	East	Midwest	South	West
2nd Q 2018	1.14	1.06	1.03	1.01	1.10	1.07
1st Q 2018	1.12	1.06	1.03	1.07	1.13	1.05
One Year	4.64	4.33	4.16	4.26	4.54	4.35
Three Years	4.74	4.50	4.31	4.44	4.82	4.48
Five Years	4.98	4.67	4.40	4.70	5.06	4.65
Ten Years	5.51	5.03	4.69	5.26	5.48	4.96
Twenty Years	6.50	5.83	5.69	5.95	6.15	5.72

APARTMENT APPRECIATION RETURNS

	Total NPI	Total Apartment	East	Midwest	South	West
2nd Q 2018	0.67	0.48	0.23	0.30	0.45	0.77
1st Q 2018	0.58	0.44	0.30	-0.11	0.74	0.52
One Year	2.46	2.07	0.91	0.13	2.25	3.55
Three Years	3.40	2.88	1.53	1.10	2.08	5.30
Five Years	4.63	3.97	2.37	2.94	3.91	5.96
Ten Years	0.68	1.16	-0.36	1.64	1.48	2.41
Twenty Years	2.57	3.12	2.97	2.41	2.76	4.25

APARTMENT INDEX—QUARTILE RANGE OF RETURNS