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Housing Starts Here

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SOUTHERN CALIFORNIA CHAPTER OF THE APPRAISAL INSTITUTE

24th Annual Market Trends Seminar

January 2017

TOPICS FOR TODAY

1. National Economic and Housing Market Trends

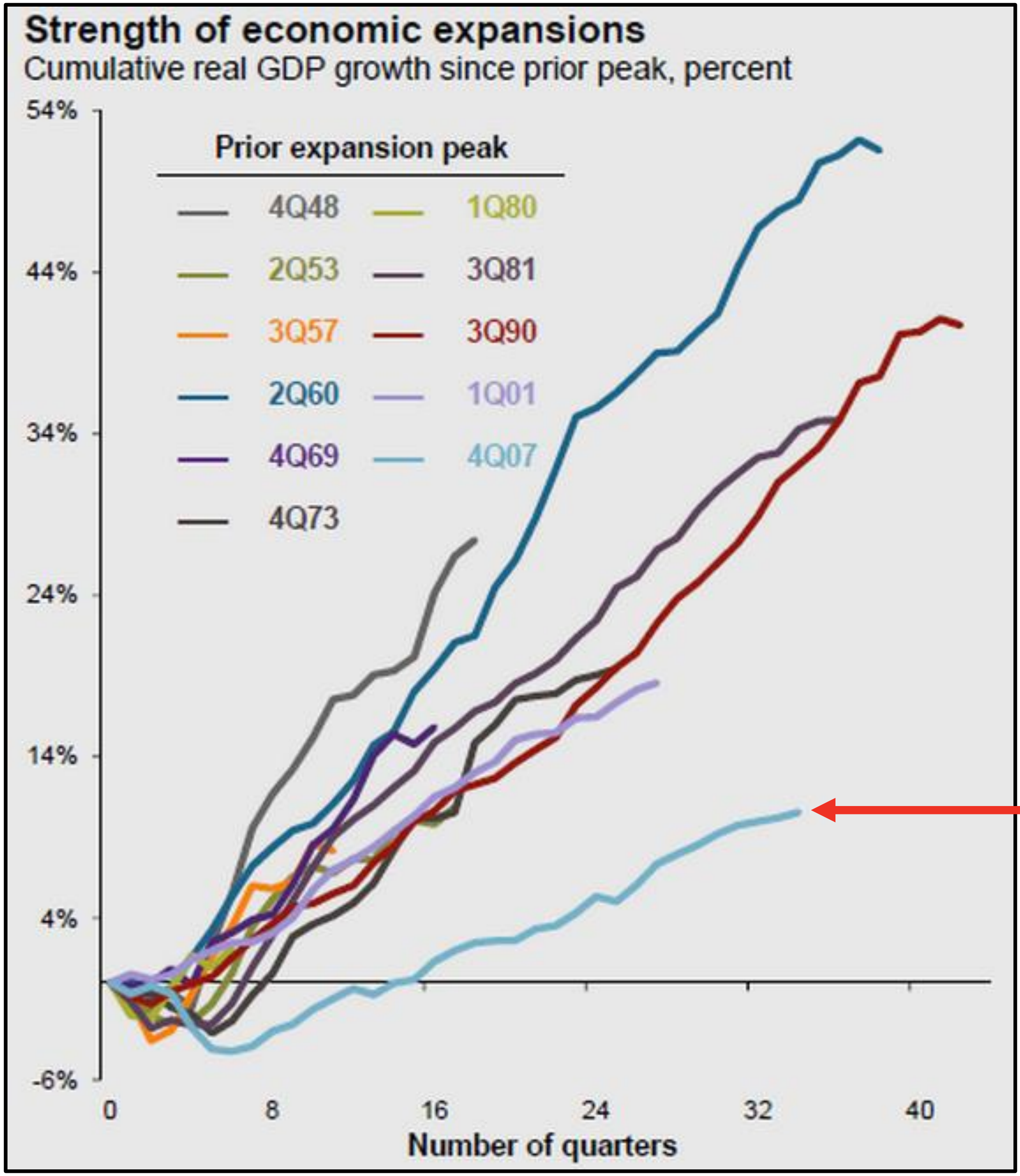
2. Changing Home Buyer and Workforce Characteristics

3. Review of Key Southern California Housing Markets

4. Interest Rate Outlook

National Economic and Housing Market Trends

GDP GROWTH COMPARED BY HISTORICAL EXPANSIONS

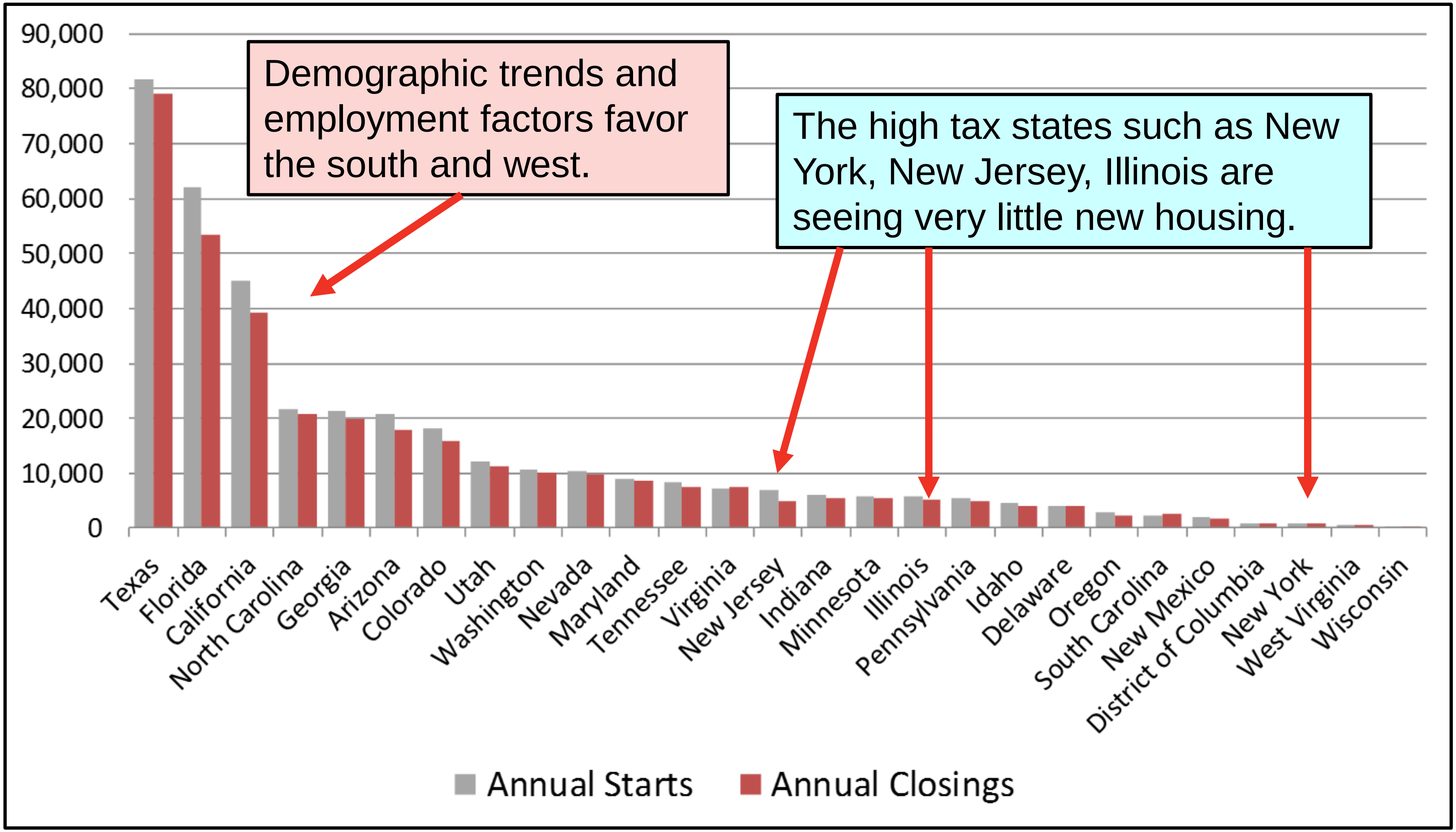


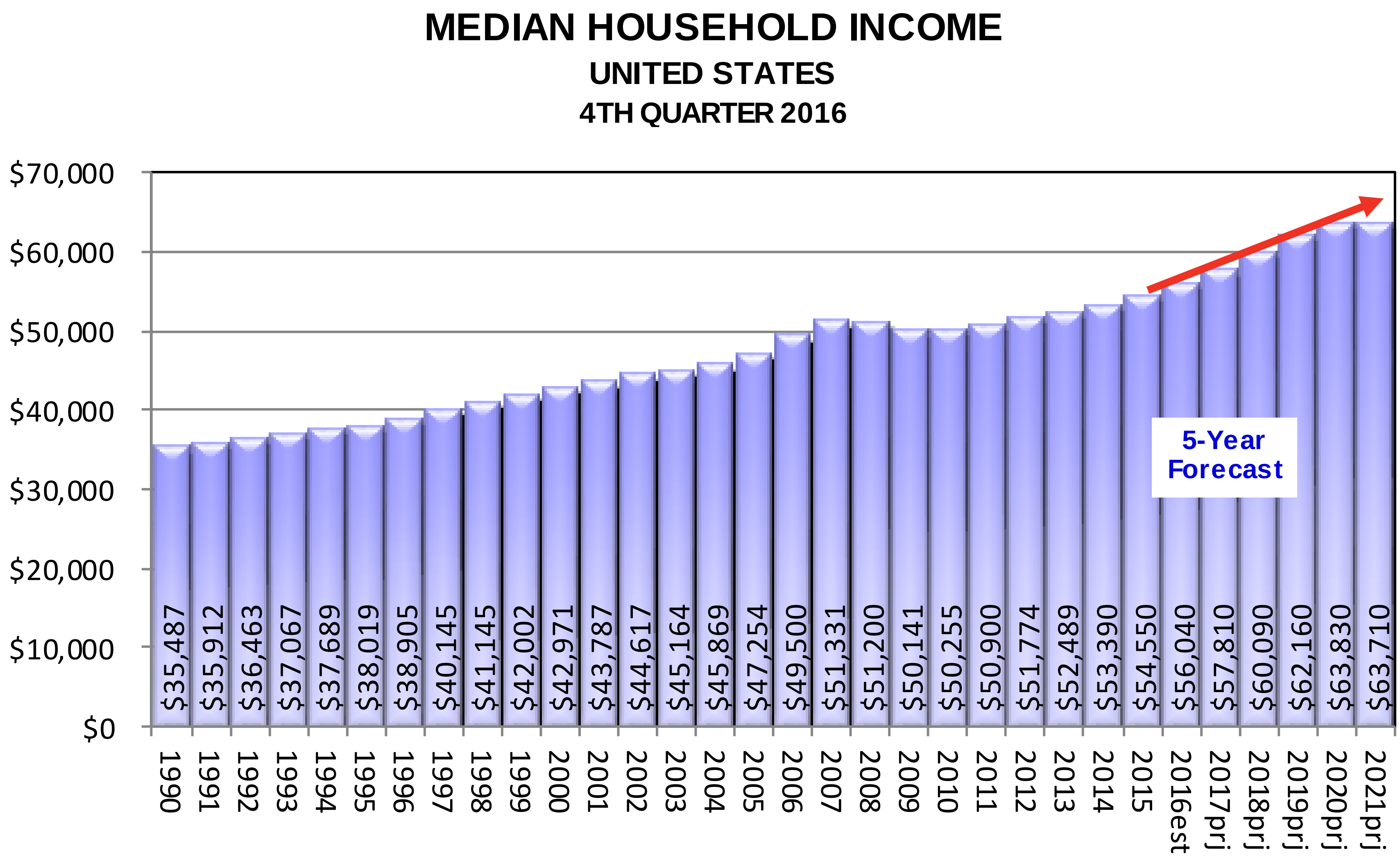
The current expansion has been, by far, the weakest in the post-WWII era.

We are here!

NATIONAL HOUSING MARKET

Annual Starts & Annual Closings by State



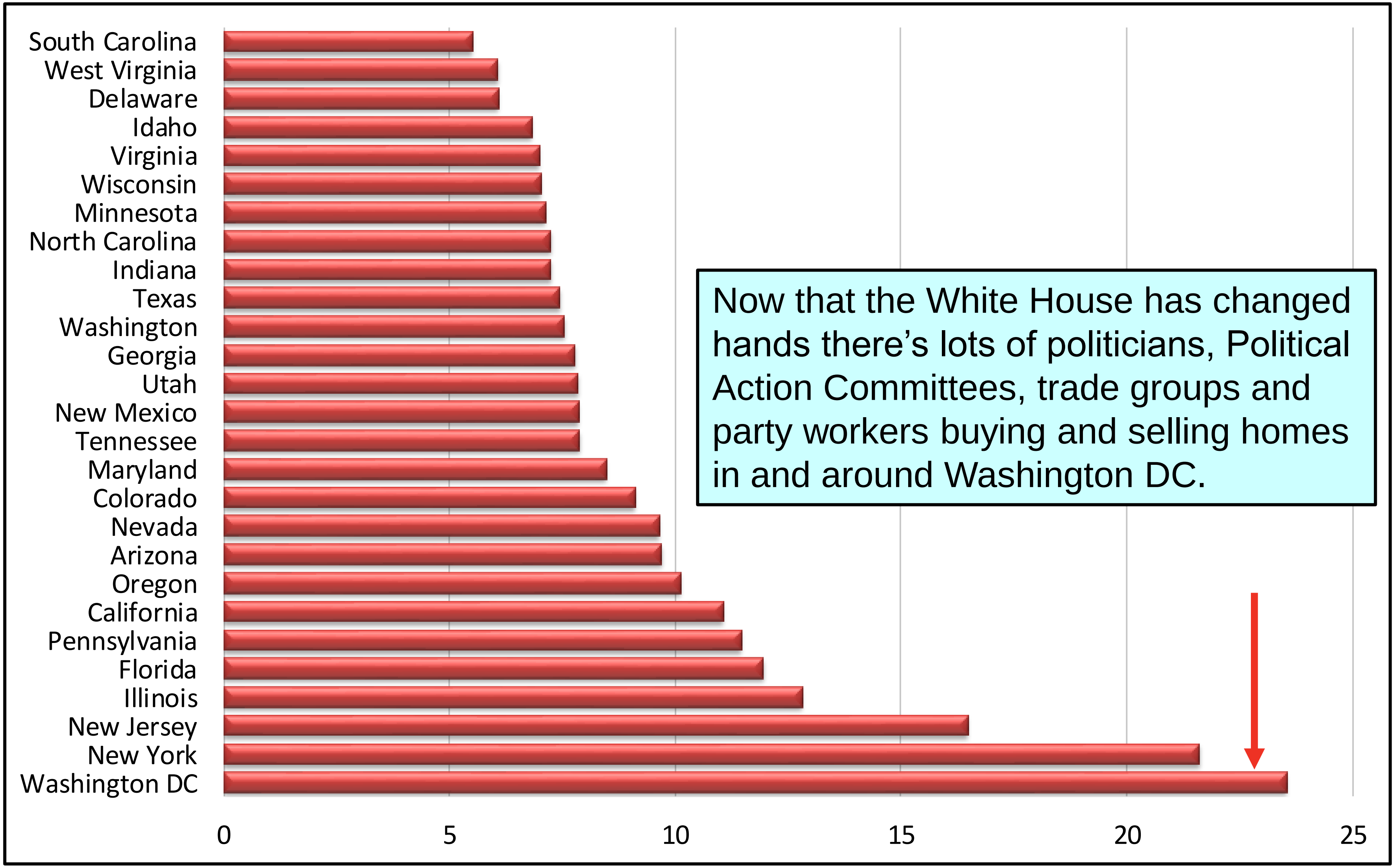


Wage growth is forecast to average 3.0% nationally through 2020, the highest in years.

Janet Yellin has publicly spoken about letting wages “run hot” before increasing rates.

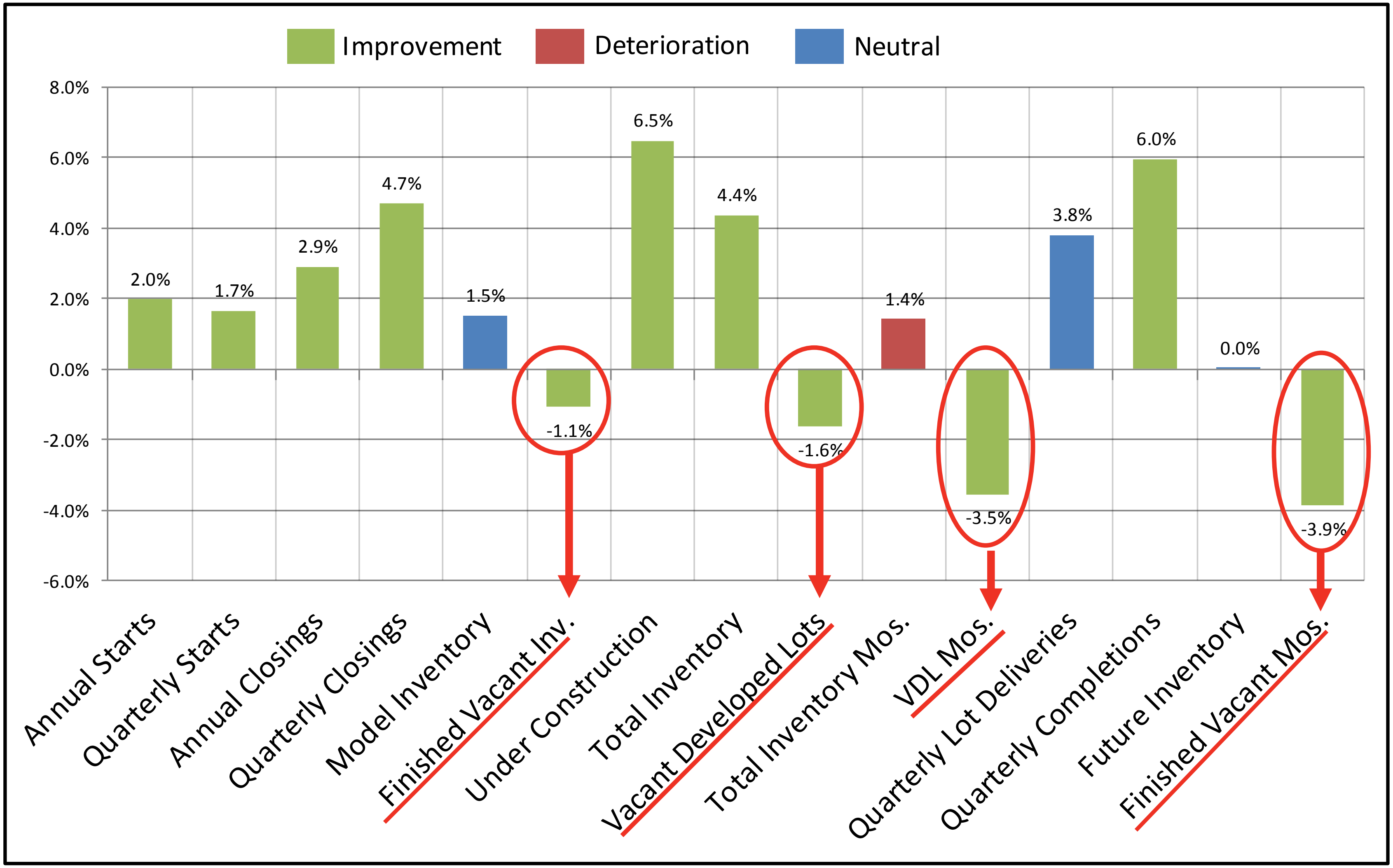
NATIONAL HOUSING MARKET

Housing Inventory Months of Supply by State

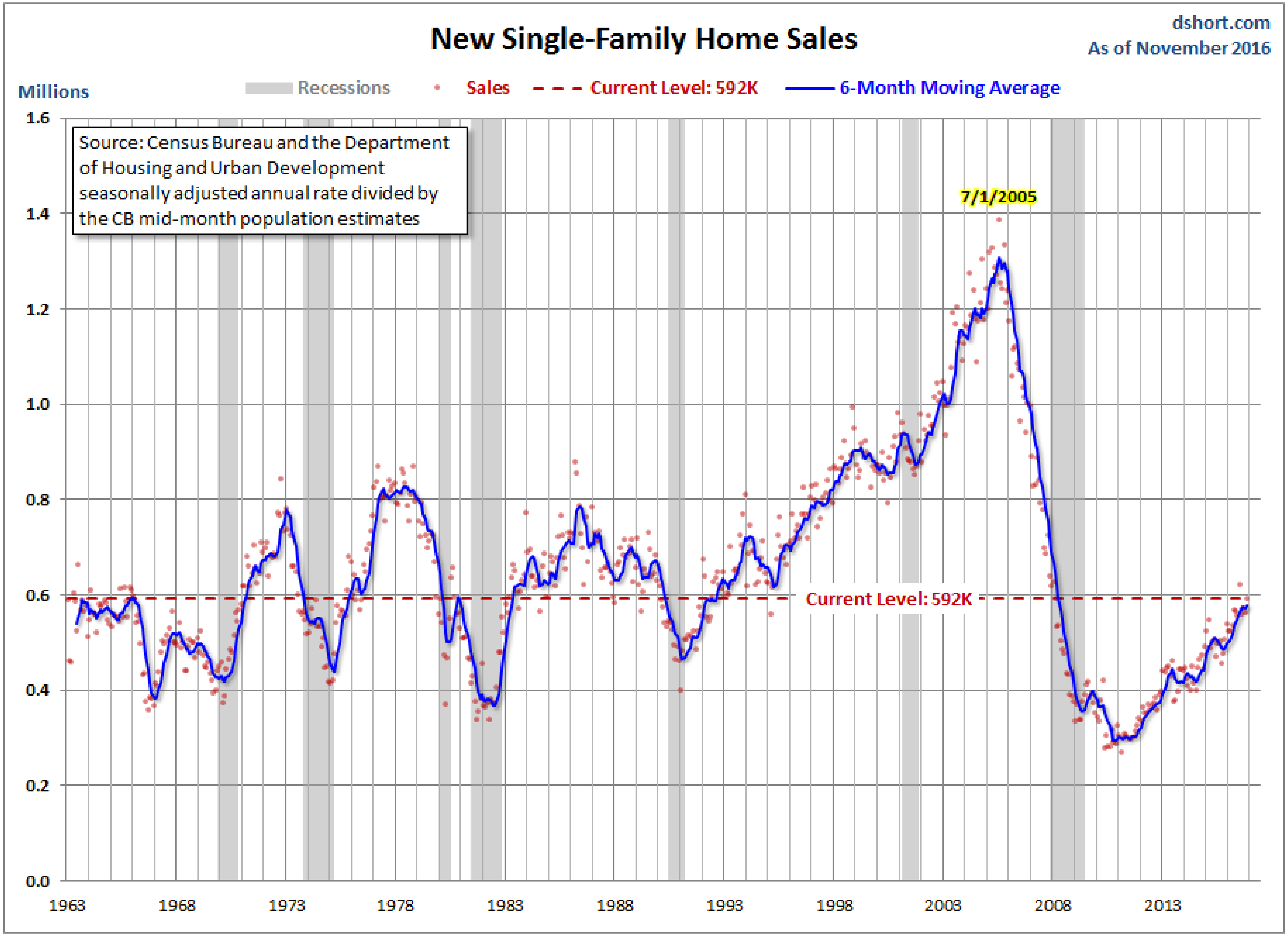


NATIONAL HOUSING MARKET

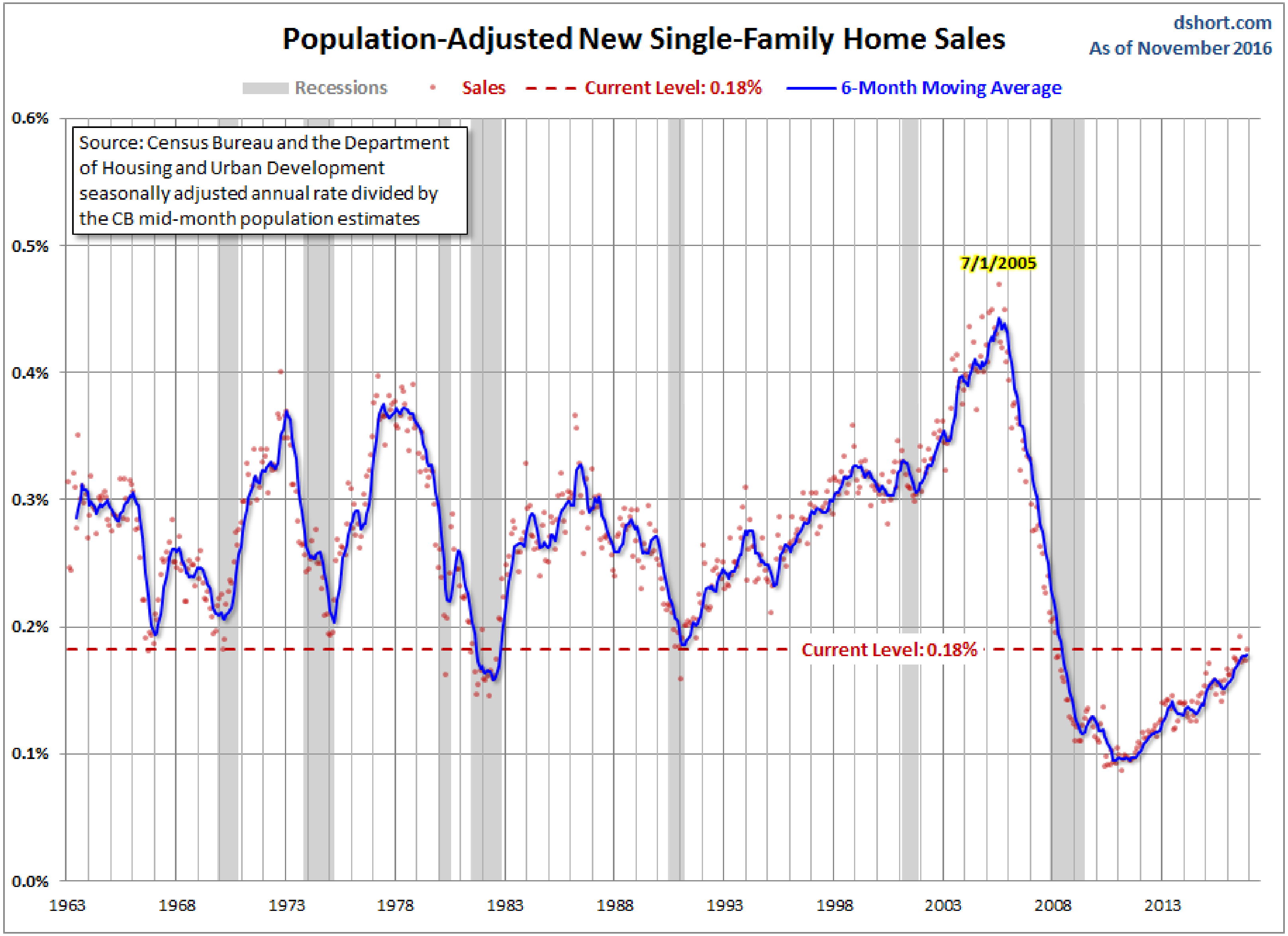
Quarter-over-Quarter Percent Changes of Major Housing Components



Homebuilder operational efficiencies are improving with fewer vacant homes and lots on the books. This would be typical as the cycle matures.

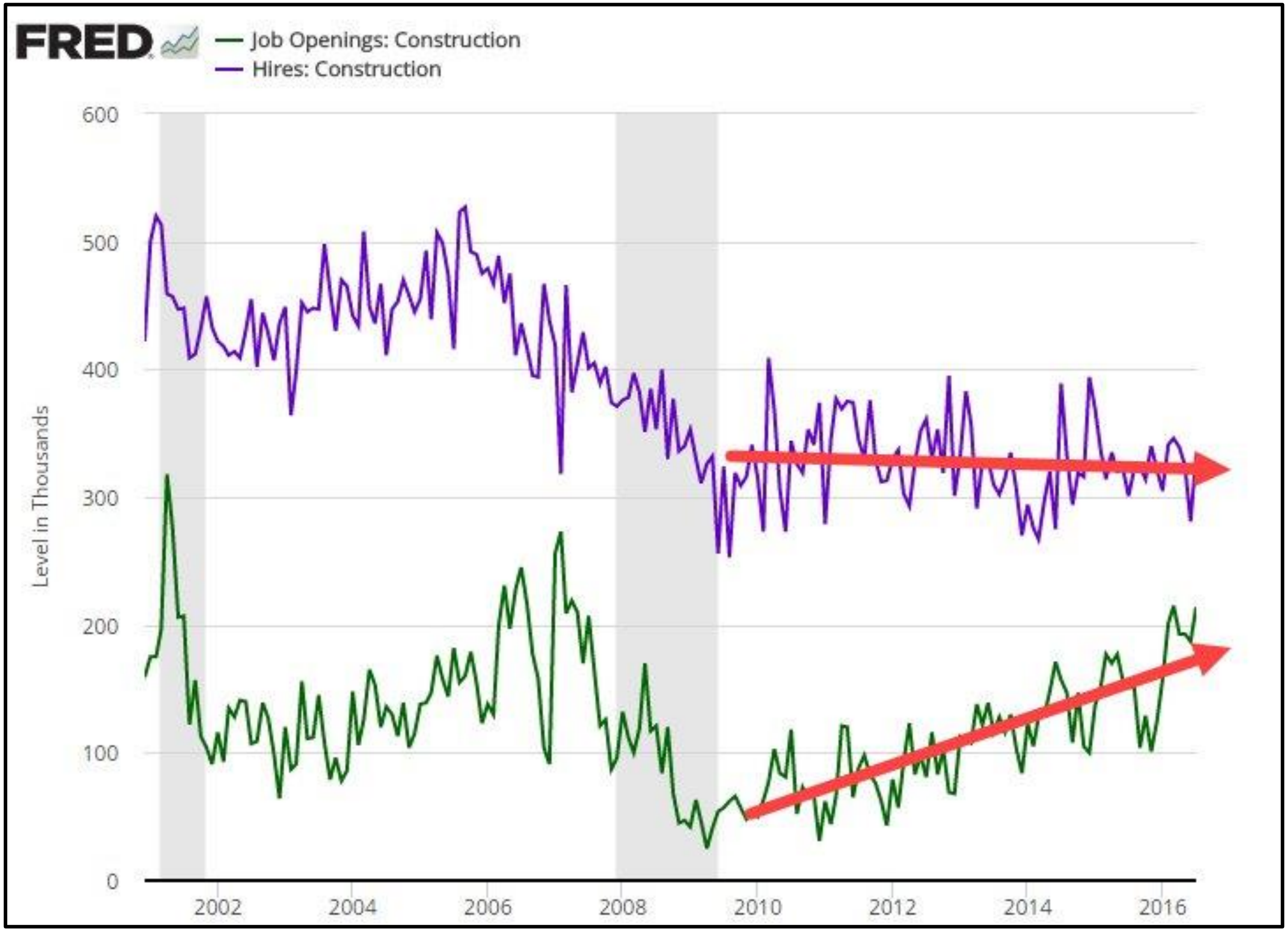


Numerically new home sales remain at VERY low levels.



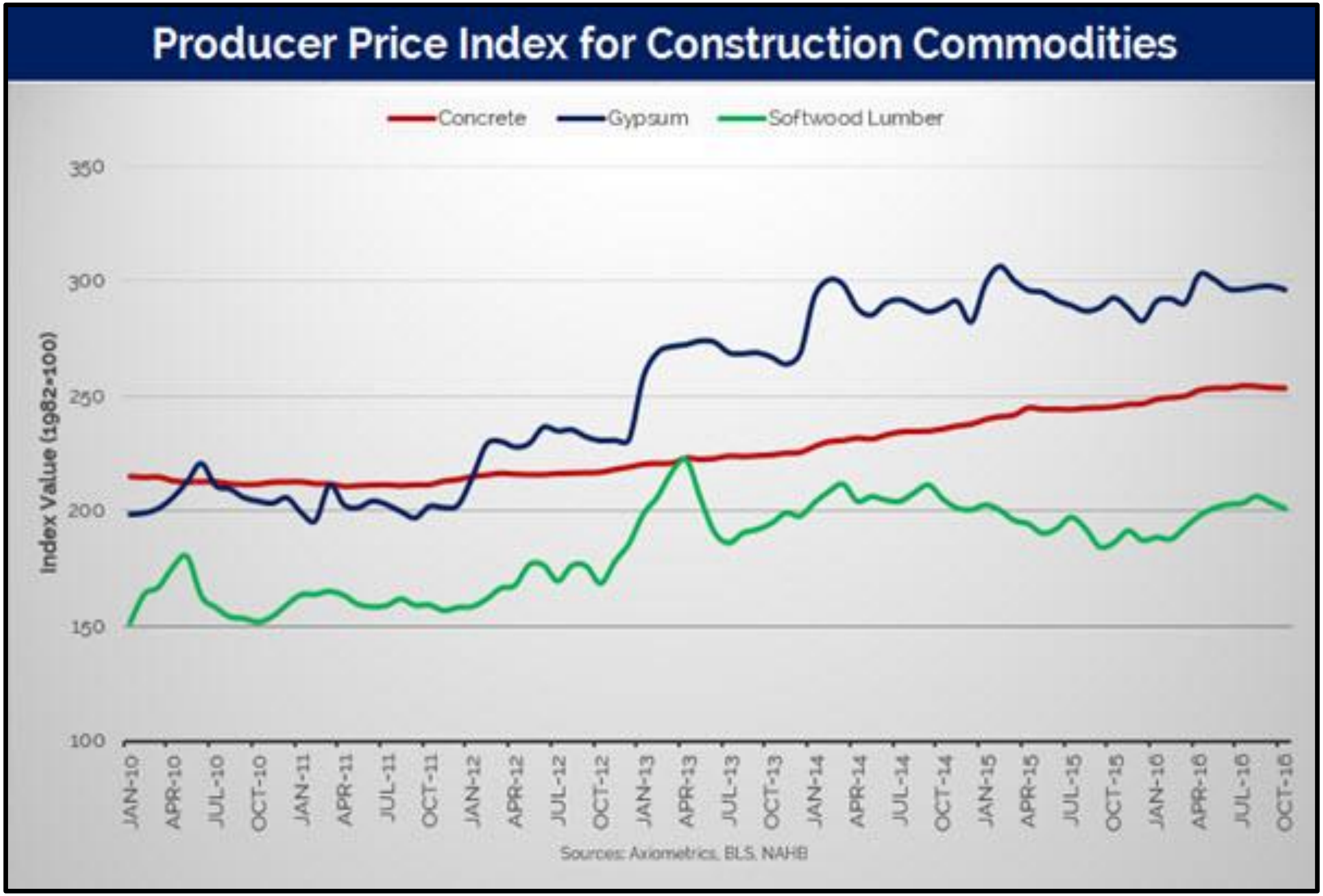
On the basis of population new home sales are at VERY low levels.

DEMAND FOR SKILLED LABOR IS OUTPACING SUPPLY



Nationally, job openings in construction have more than doubled while hiring is steady. This is the labor shortage you hear about.

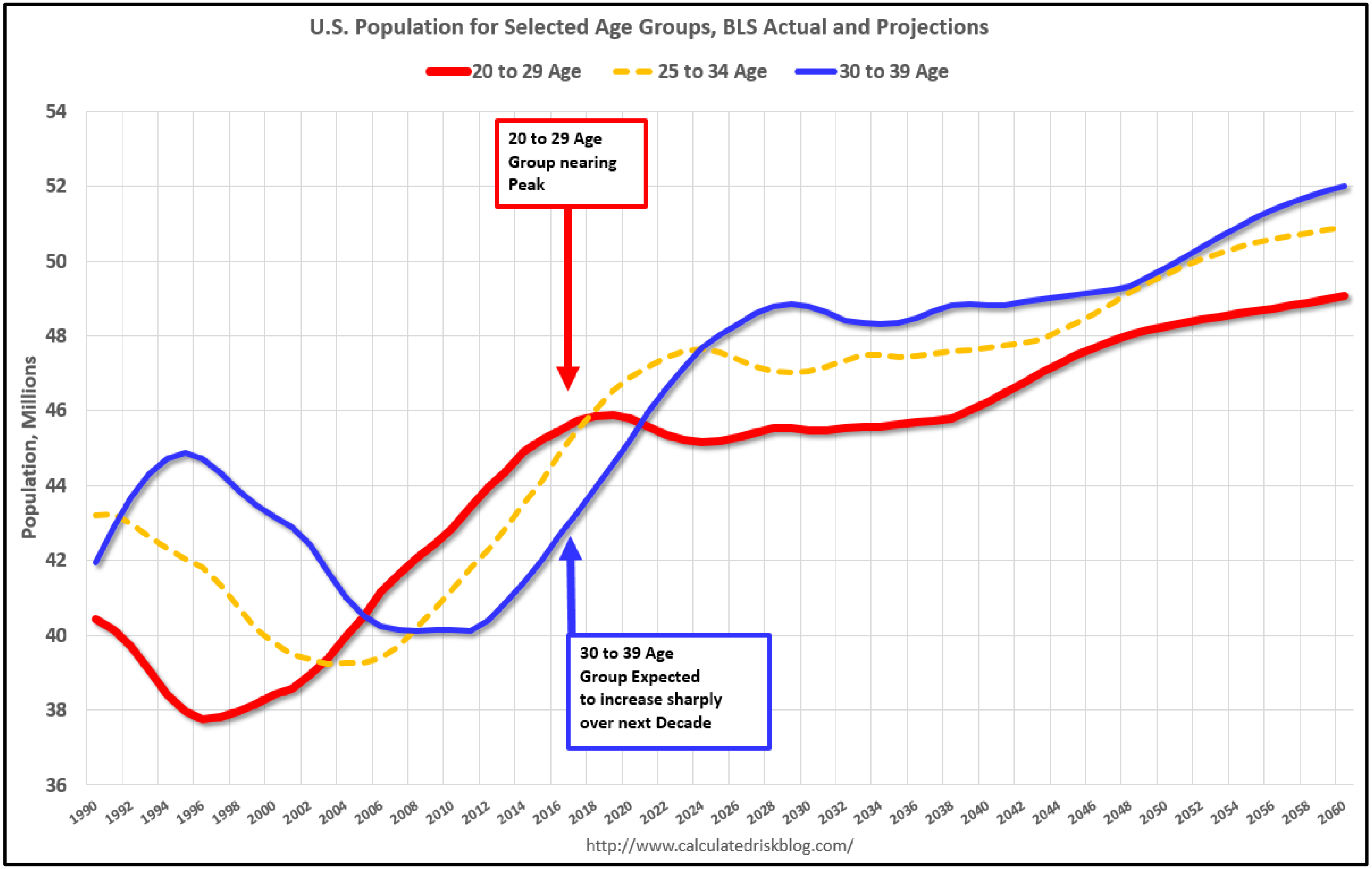
PRICES FOR CONSTRUCTION MATERIALS ARE RISING



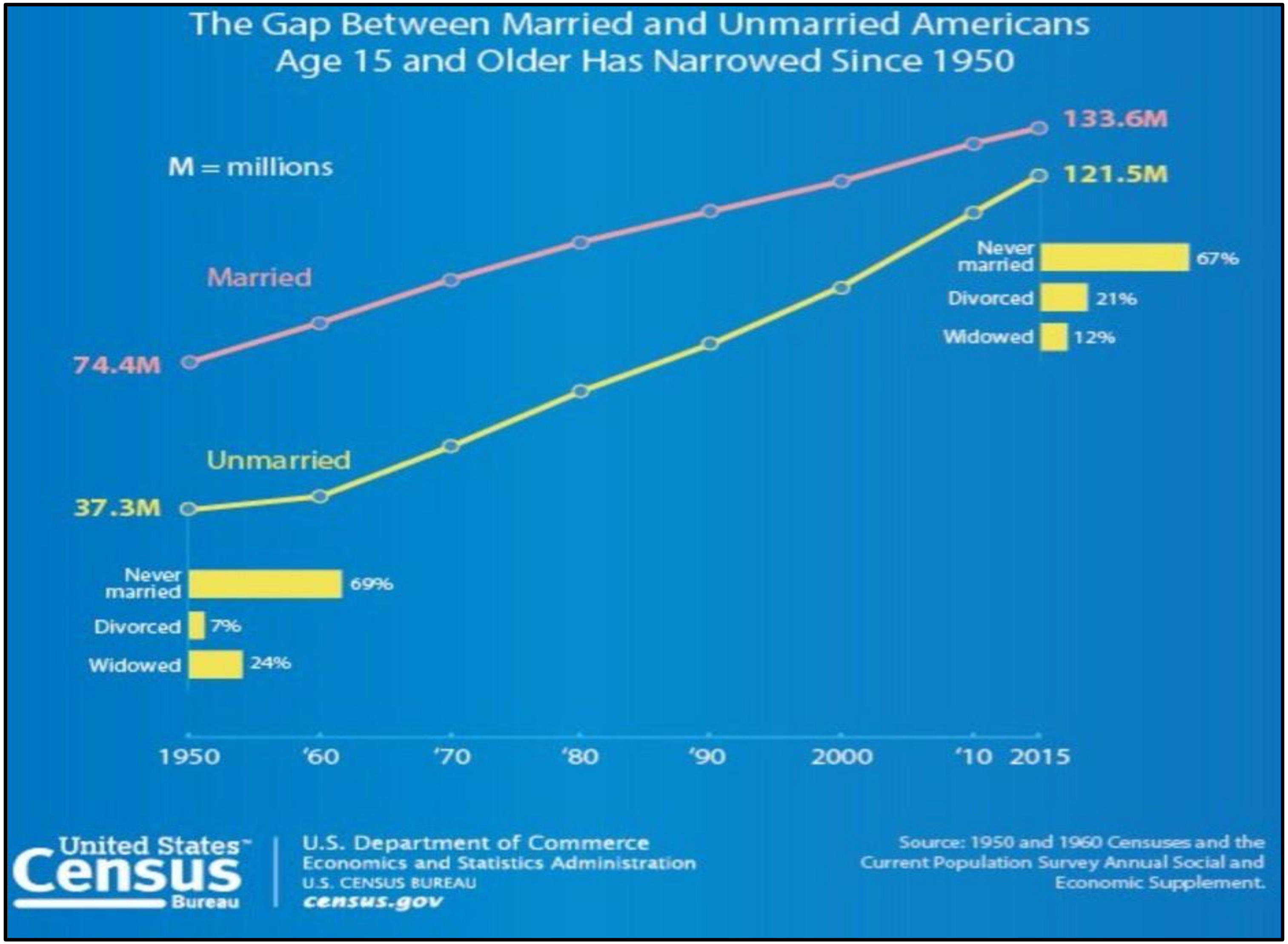
Lumber is experiencing the smallest price increases due to the weak Canadian dollar. U.S. – Canadian lumber trade agreement has expired.

Evolving Buyer Profile and Workforce Characteristics

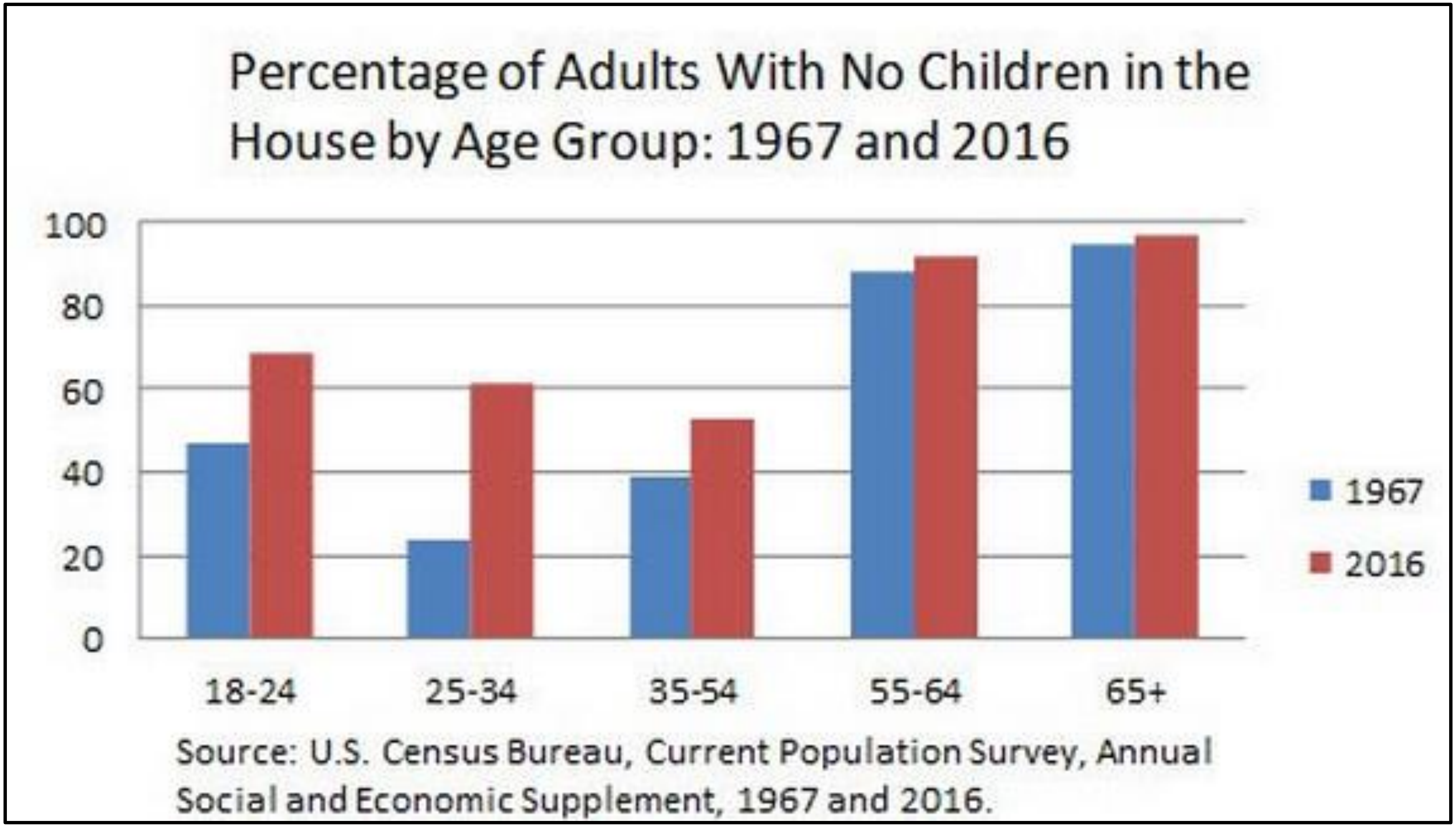
MILLENIALS ARE AGING INTO THEIR PRIME HOME BUYING YEARS



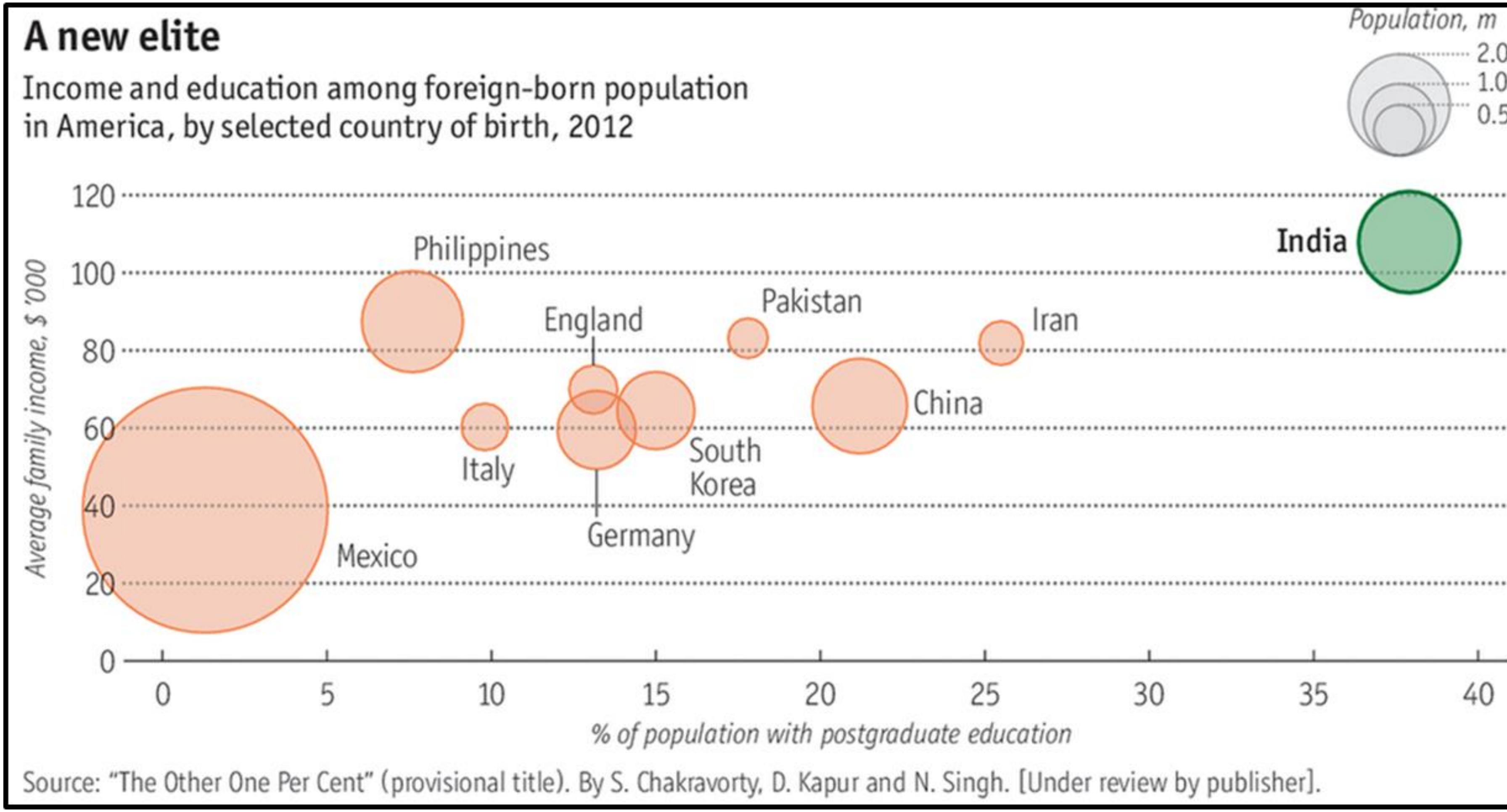
The 20 to 29 year olds haven't been strong home buyers, but they are entering their prime home buying years.



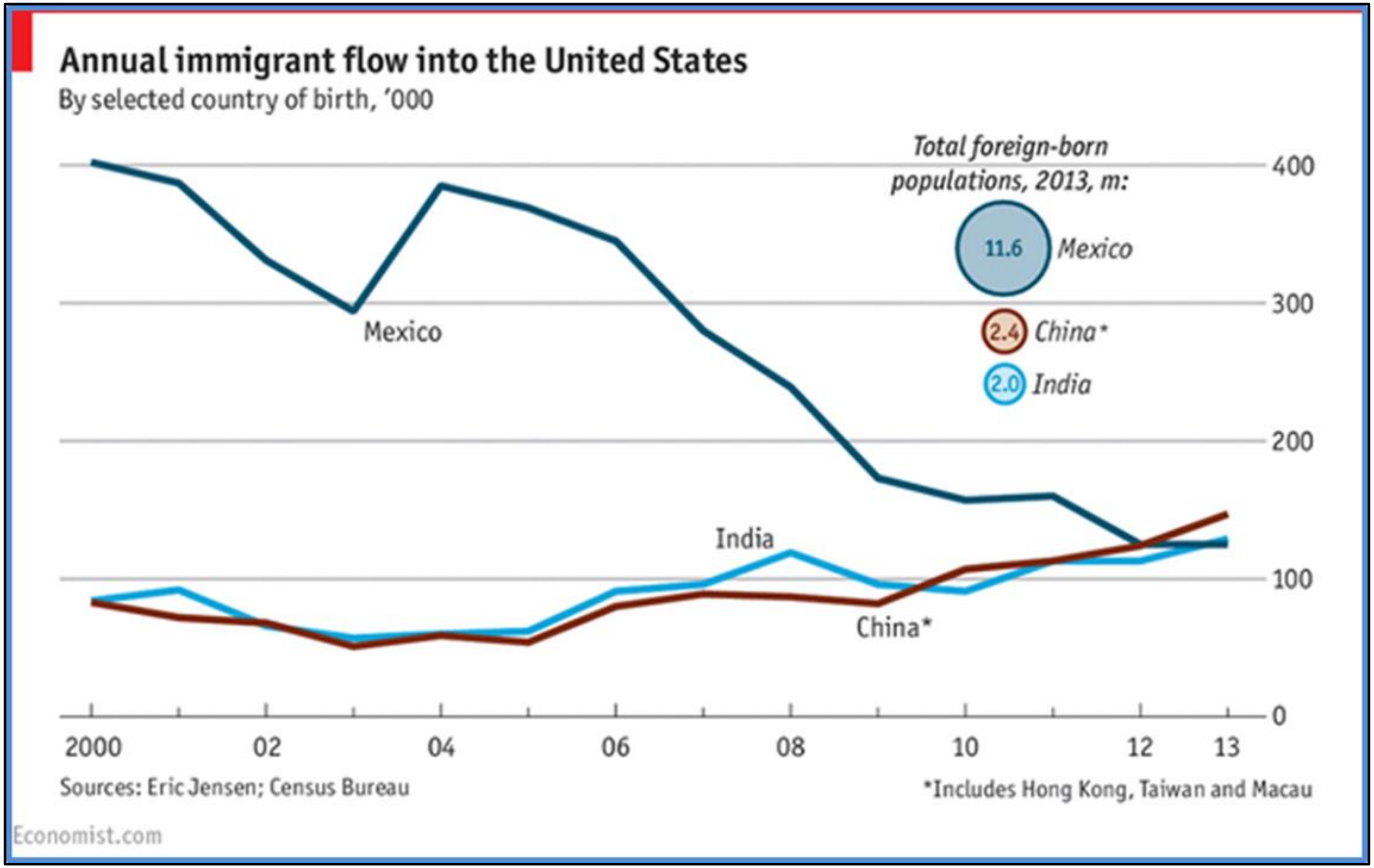
The percentage of “family” buyers is declining while other types of households are increasing. Different designs will be needed to fill this demand.



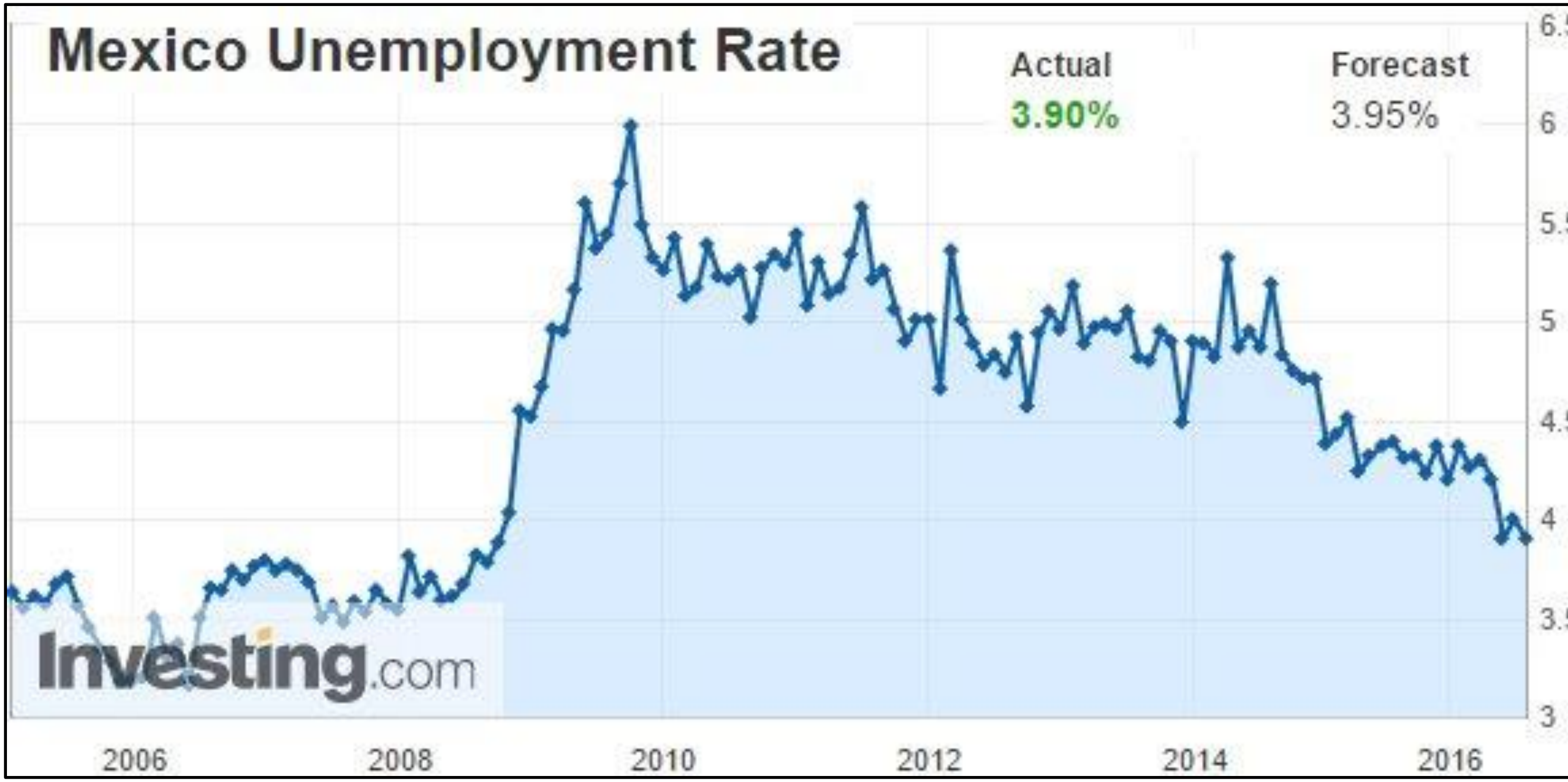
“Family” households with children are no longer the “go to” buyer profile.



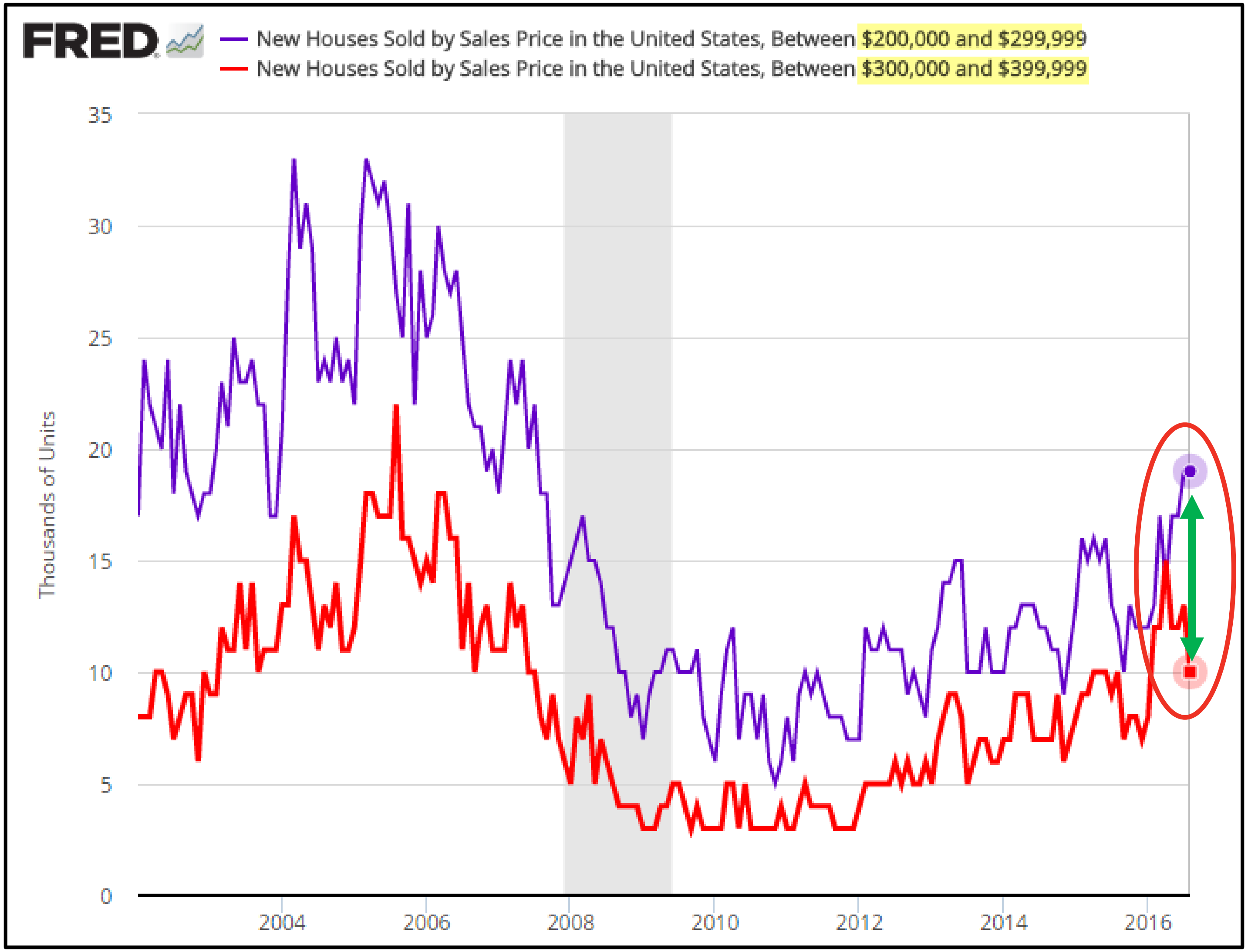
Given the age of this survey, the trends are likely to have intensified. Increased immigration from Europe should be expected as political unrest grows.



Immigration numbers from Mexico have plummeted. Most new immigrants are from various parts of Asia.

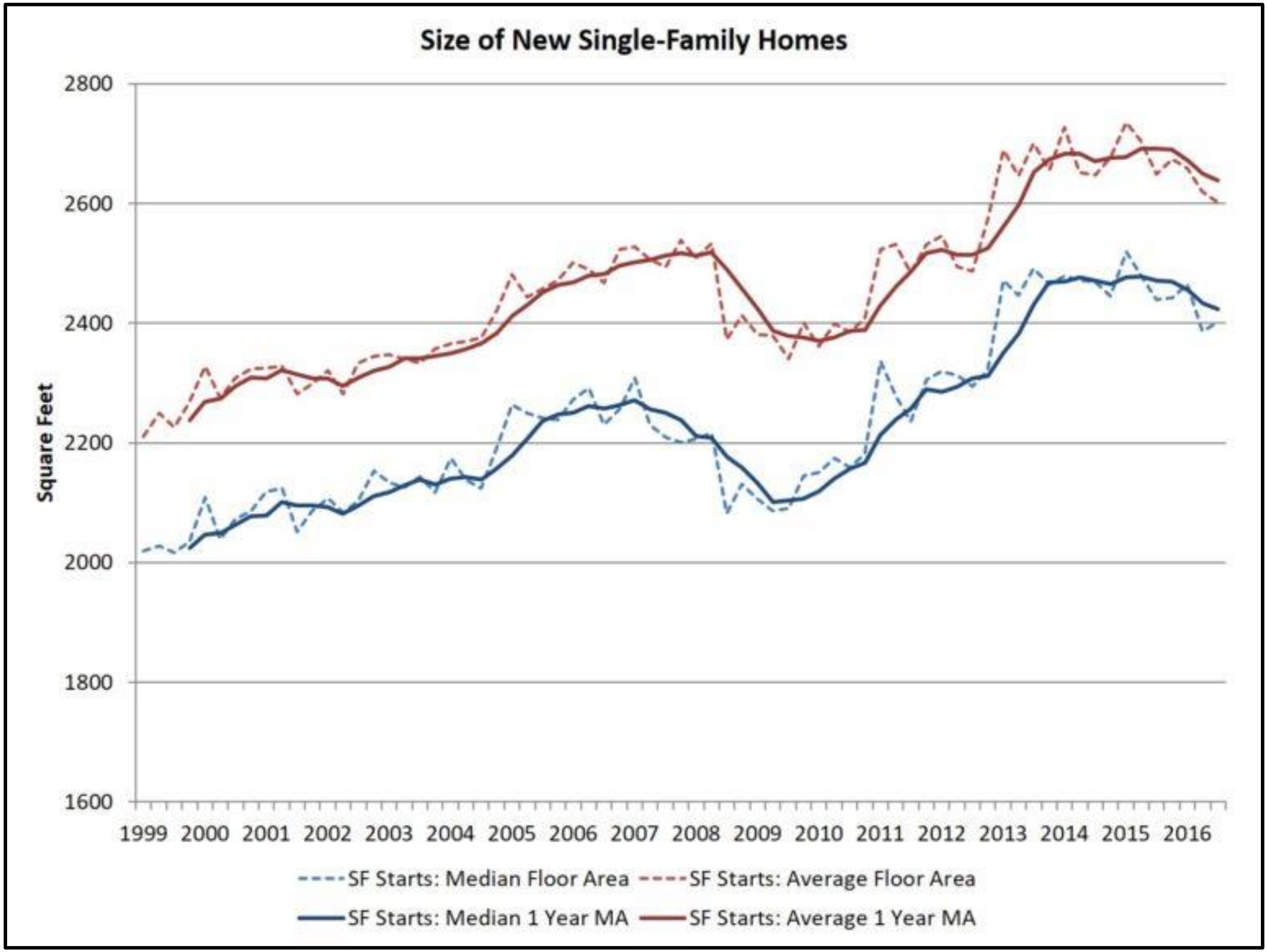


Unemployment in Mexico was below U.S. levels during the recession and it remains lower today.



Nationally, sales volume in the lower price brackets and higher price brackets are diverging. This is first timers, Millennials and retired persons being drawn to more affordable alternatives.

NATIONAL NEW HOME SIZES ARE SHRINKING



Nationally, new home sizes are declining with builders aiming to provide more homes in lower price brackets.

Review of Key Southern California Markets

SURVEY-TO-SURVEY NEW HOME MARKET CHANGES REPORT

Detached New Housing Developments Surveyed in Select Areas of
Los Angeles County as of 2016 Q4 Field Audit.

	QUARTERLY MARKET STATISTICS FROM THE 4TH QUARTER OF THE LAST NINE YEARS								
Category	2008 Q4	2009 Q4	2010 Q4	2011 Q4	2012 Q4	2013 Q4	2014 Q4	2015 Q4	2016 Q4
No. of Active Developments	84	52	44	58	56	45	59	64	53
Average of Base Prices	$503,166	$477,706	$534,313	$523,318	$527,714	$537,246	$608,740	$677,560	$686,792
Incentive as a % of Base Price	2.7%	2.6%	1.6%	1.4%	1.4%	0.8%	0.7%	0.8%	0.7%
Average of Unit Sizes (S.f.)	2,740 sf	2,667 sf	2,706 sf	2,683 sf	2,608 sf	2,453 sf	2,546 sf	2,671 sf	2,664 sf
Average of Minimum Lot Sizes	7,165 sf	6,968 sf	7,186 sf	7,407 sf	6,738 sf	5,680 sf	5,136 sf	5,635 sf	5,524 sf
Average Monthly Sales Rate Per Dev.	1.5/mo	1.6/mo	1.3/mo	1.0/mo	1.5/mo	1.6/mo	2.0/mo	2.7/mo	2.8/mo
Total Inventory	3,909 du	1,442 du	1,785 du	2,274 du	1,539 du	1,459 du	1,603 du	1,831 du	1,274 du
Months of Total Inventory	30.6 mos.	17.6 mos.	32.2 mos.	38.6 mos.	18.0 mos.	19.9 mos.	13.7 mos.	10.5 mos.	8.5 mos.

L.A. County detached home community counts are very low.

Months of inventory are also very low.

Market is depressed due to the Newhall Ranch litigation.

SURVEY-TO-SURVEY NEW HOME MARKET CHANGES REPORT

Attached New Housing Developments Surveyed in Select Areas of
Los Angeles County as of 2016 Q4 Field Audit.

Category	QUARTERLY MARKET STATISTICS FROM THE 4TH QUARTER OF THE LAST NINE YEARS								
	2008 Q4	2009 Q4	2010 Q4	2011 Q4	2012 Q4	2013 Q4	2014 Q4	2015 Q4	2016 Q4
No. of Active Developments	50	42	37	50	39	36	45	40	50
Average of Base Prices	$473,914	$430,457	$436,695	$438,573	$446,745	$619,699	$694,973	$724,401	$780,462
Incentive as a % of Base Price	1.3%	1.2%	1.3%	1.4%	1.1%	0.5%	0.4%	0.4%	0.5%
Average of Unit Sizes (S.f.)	1,187 sf	1,239 sf	1,268 sf	1,308 sf	1,292 sf	1,608 sf	1,685 sf	1,717 sf	1,704 sf
Average Price Per Square Foot	$399	$348	$344	$335	$346	$385	$412	$422	$458
Average Premium	$40,202	$38,762	$41,895	$16,874	$15,381	$58,608	$72,367	$82,193	$57,567
Average Monthly Sales Rate Per Dev.	1.9/mo	2.2/mo	2.6/mo	1.7/mo	2.0/mo	1.5/mo	2.2/mo	2.5/mo	3.3/mo
Total Inventory	2,440 du	2,013 du	1,875 du	1,941 du	1,316 du	1,073 du	1,121 du	835 du	992 du
Months of Total Inventory	25.4 mos.	21.8 mos.	19.3 mos.	23.1 mos.	16.8 mos.	19.4 mos.	11.5 mos.	8.2 mos.	6.1 mos.

New attached home offerings in L.A. County have modestly rebounded.

Accelerating prices show that most of the attached supply is coastal.

Supply is plummeting!

ORANGE COUNTY – DETACHED DEVELOPMENTS ONLY

SURVEY-TO-SURVEY NEW HOME MARKET CHANGES REPORT

Detached New Housing Developments Surveyed in Select Areas of
Orange County as of 2016 Q4 Field Audit.

	QUARTERLY MARKET STATISTICS FROM THE 4TH QUARTER OF THE LAST NINE YEARS								
Category	2008 Q4	2009 Q4	2010 Q4	2011 Q4	2012 Q4	2013 Q4	2014 Q4	2015 Q4	2016 Q4
No. of Active Developments	53	37	37	49	59	73	80	94	98
Average of Base Prices	$973,565	$888,887	$853,484	$801,903	$837,310	$939,897	$1,034,219	$1,160,400	$1,250,116
Incentive as a % of Base Price	1.9%	2.0%	1.5%	1.2%	0.7%	0.4%	0.4%	0.5%	0.5%
Average of Unit Sizes (S.f.)	2,876 sf	2,858 sf	2,700 sf	2,494 sf	2,588 sf	2,569 sf	2,694 sf	2,766 sf	2,878 sf
Average Price Per Square Foot	$338	$311	$316	$322	$324	$366	$384	$419	$434
Average Premium	$35,394	$41,150	$31,922	$36,316	$46,245	$43,573	$50,462	$66,723	$82,125
Average of Minimum Lot Sizes	5,807 sf	5,387 sf	5,060 sf	4,492 sf	4,966 sf	4,640 sf	4,615 sf	4,599 sf	4,710 sf
Average Monthly Sales Rate Per Dev.	1.1/mo	1.0/mo	1.9/mo	1.4/mo	2.2/mo	2.5/mo	2.8/mo	3.2/mo	3.4/mo
Total Inventory	1,786 du	1,312 du	1,159 du	2,022 du	1,553 du	2,101 du	2,026 du	2,957 du	2,305 du
Months of Total Inventory	31.1 mos.	33.9 mos.	16.9 mos.	30.3 mos.	12.1 mos.	11.6 mos.	9.0 mos.	9.9 mos.	7.0 mos.

The Orange County detached market has become well supplied and pricey.

Employment is solid, however, prices are stretched.

SURVEY-TO-SURVEY NEW HOME MARKET CHANGES REPORT

Attached New Housing Developments Surveyed in Select Areas of Orange County as of 2016 Q4 Field Audit.

Category	QUARTERLY MARKET STATISTICS FROM THE 4TH QUARTER OF THE LAST NINE YEARS								
	2008 Q4	2009 Q4	2010 Q4	2011 Q4	2012 Q4	2013 Q4	2014 Q4	2015 Q4	2016 Q4
No. of Active Developments	40	20	32	31	24	29	27	37	31
Average of Base Prices	$506,057	$464,757	$494,699	$475,238	$523,899	$573,097	$595,634	$648,575	$614,227
Incentive as a % of Base Price	2.5%	2.4%	1.0%	1.3%	1.2%	0.5%	0.7%	0.6%	0.6%
Average of Unit Sizes (S.f.)	1,516 sf	1,546 sf	1,695 sf	1,711 sf	1,830 sf	1,705 sf	1,696 sf	1,674 sf	1,626 sf
Average Price Per Square Foot	$334	$301	$292	$278	$286	$336	$351	$388	$378
Average Premium	$23,375	$38,414	$30,852	$7,724	$11,419	$13,166	$9,539	$9,314	$10,665
Average of Minimum Lot Sizes	1,629 sf	1,669 sf	1,749 sf	1,802 sf	1,743 sf	1,844 sf	2,175 sf	1,837 sf	1,668 sf
Average Monthly Sales Rate Per Dev.	2.1/mo	2.2/mo	2.1/mo	1.6/mo	2.3/mo	2.4/mo	3.0/mo	4.0/mo	4.5/mo
Total Inventory	1,914 du	819 du	1,269 du	1,094 du	587 du	1,014 du	1,098 du	1,112 du	843 du
Months of Total Inventory	23.0 mos.	18.9 mos.	18.8 mos.	21.9 mos.	10.6 mos.	14.3 mos.	13.7 mos.	7.5 mos.	6.0 mos.

Orange County new attached product is affordable (by comparison).

Sales rates are high, although there is a lot product in certain segments.

SURVEY-TO-SURVEY NEW HOME MARKET CHANGES REPORT

Detached New Housing Developments Surveyed in the Inland Empire (NO DESERTS)

Riverside County as of 2016 Q4 Field Audit, San Bernardino County as of 2016 Q4 Field Audit.

	QUARTERLY MARKET STATISTICS FROM THE 4TH QUARTER OF THE LAST NINE YEARS								
Category	2008 Q4	2009 Q4	2010 Q4	2011 Q4	2012 Q4	2013 Q4	2014 Q4	2015 Q4	2016 Q4
No. of Active Developments	329	194	125	139	133	115	165	175	181
Average of Base Prices	$390,086	$345,036	$338,993	$332,173	$333,836	$383,055	$410,363	$435,873	$452,795
Incentive as a % of Base Price	4.3%	2.7%	2.8%	2.7%	2.2%	1.7%	1.8%	1.6%	1.4%
Average of Unit Sizes (S.F.)	2,869 sf	2,773 sf	2,653 sf	2,570 sf	2,539 sf	2,581 sf	2,642 sf	2,688 sf	2,676 sf
Average Monthly Sales Rate Per Dev.	1.6/mo	1.8/mo	1.7/mo	1.2/mo	1.6/mo	2.4/mo	2.7/mo	2.9/mo	3.5/mo
Total Inventory	14,223 du	6,150 du	3,760 du	5,778 du	4,253 du	3,905 du	7,406 du	7,256 du	5,765 du
Months of Total Inventory	26.6 mos.	18.0 mos.	18.0 mos.	35.9 mos.	19.5 mos.	14.0 mos.	16.3 mos.	14.1 mos.	9.2 mos.

Community counts are growing, but not that quickly.

Construction starts are growing at a faster rate than lots are being purchased, builders are going to need more land soon!

Supply levels are tightening.

SURVEY-TO-SURVEY NEW HOME MARKET CHANGES REPORT

Attached New Housing Developments Surveyed in the Inland Emprie (NO DESERTS)

Riverside County as of 2016 Q4 Field Audit, San Bernardino County as of 2016 Q4 Field Audit.

Category	QUARTERLY MARKET STATISTICS FROM THE 4TH QUARTER OF THE LAST NINE YEARS								
	2008 Q4	2009 Q4	2010 Q4	2011 Q4	2012 Q4	2013 Q4	2014 Q4	2015 Q4	2016 Q4
No. of Active Developments	31	20	14	8	8	5	10	14	12
Average of Base Prices	$280,434	$253,583	$257,135	$237,702	$251,942	$343,782	$337,687	$359,634	$351,847
Incentive as a % of Base Price	4.2%	3.7%	3.7%	3.4%	3.5%	1.6%	2.0%	1.8%	1.5%
Average of Unit Sizes (S.F.)	1,555 sf	1,575 sf	1,590 sf	1,544 sf	1,537 sf	1,650 sf	1,695 sf	1,643 sf	1,609 sf
Average of Minimum Lot Sizes	1,933 sf	1,811 sf	1,834 sf	2,134 sf	1,836 sf	1,680 sf	1,830 sf	1,757 sf	1,742 sf
Average Monthly Sales Rate Per Dev.	2.0/mo	2.6/mo	2.5/mo	1.4/mo	1.8/mo	2.5/mo	2.8/mo	3.9/mo	5.8/mo
Total Inventory	1,575 du	511 du	202 du	368 du	257 du	238 du	349 du	894 du	654 du
Months of Total Inventory	25.2 mos.	9.9 mos.	5.7 mos.	33.0 mos.	18.0 mos.	19.4 mos.	12.7 mos.	16.6 mos.	9.3 mos.

The I.E. attached market may be coming out of its coma.

Attached communities are selling out faster than new openings are taking place.

Sales rates are strong and inventory levels are low.

SURVEY-TO-SURVEY NEW HOME MARKET CHANGES REPORT

Detached New Housing Developments Surveyed in San Diego County as of 2016 Q4 Field Audit.

Category	QUARTERLY MARKET STATISTICS FROM THE 4TH QUARTER OF THE LAST NINE YEARS								
	2008 Q4	2009 Q4	2010 Q4	2011 Q4	2012 Q4	2013 Q4	2014 Q4	2015 Q4	2016 Q4
No. of Active Developments	95	64	59	74	73	49	51	64	52
Average of Base Prices	$706,534	$688,142	$592,680	$607,257	$621,934	$759,385	$878,742	$934,671	$979,085
Incentive as a % of Base Price	2.4%	2.5%	3.1%	2.6%	2.0%	1.5%	1.6%	1.2%	0.9%
Average of Unit Sizes (S.F.)	2,983 sf	3,058 sf	2,729 sf	2,808 sf	2,847 sf	3,081 sf	3,250 sf	3,073 sf	3,030 sf
Average of Minimum Lot Sizes	10,802 sf	10,644 sf	6,607 sf	6,816 sf	6,766 sf	7,300 sf	11,427 sf	10,351 sf	7,736 sf
Average Monthly Sales Rate Per Dev.	1.1/mo	1.2/mo	1.3/mo	1.2/mo	1.6/mo	1.7/mo	1.8/mo	2.5/mo	3.5/mo
Months of Total Inventory	29.7 mos.	22.5 mos.	23.0 mos.	26.0 mos.	11.1 mos.	12.6 mos.	10.5 mos.	11.5 mos.	7.8 mos.

San Diego new home detached supply is clearly lacking.

This market could perform at a higher level with much MORE product.

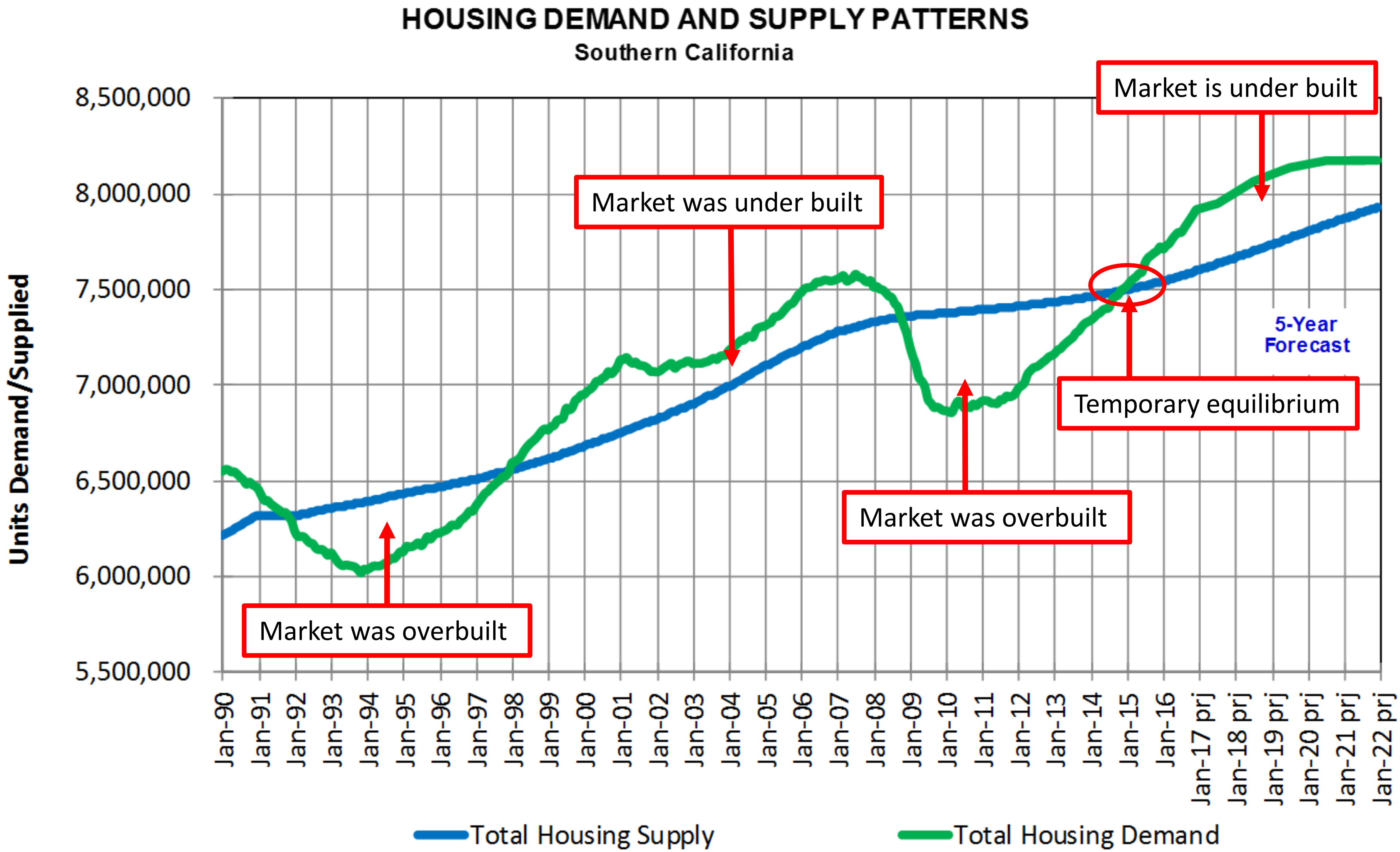
SURVEY-TO-SURVEY NEW HOME MARKET CHANGES REPORT

Attached New Housing Developments (NO HIGH RISES) Surveyed in San Diego County as of 2016 Q4 Field Audit.

Category	QUARTERLY MARKET STATISTICS FROM THE 4TH QUARTER OF THE LAST NINE YEARS								
	2008 Q4	2009 Q4	2010 Q4	2011 Q4	2012 Q4	2013 Q4	2014 Q4	2015 Q4	2016 Q4
No. of Active Developments	55	30	17	17	24	19	22	18	19
Average of Base Prices	$334,096	$337,069	$354,463	$334,871	$370,254	$397,239	$439,825	$501,333	$547,375
Incentive as a % of Base Price	4.2%	3.8%	4.1%	3.0%	2.6%	1.7%	1.4%	1.3%	0.9%
Average of Unit Sizes (S.F.)	1,208 sf	1,295 sf	1,504 sf	1,545 sf	1,550 sf	1,521 sf	1,570 sf	1,653 sf	1,700 sf
Average of Minimum Lot Sizes	1,248 sf	1,343 sf	1,526 sf	1,541 sf	1,659 sf	1,684 sf	1,778 sf	1,699 sf	1,913 sf
Average Monthly Sales Rate Per Dev.	1.6/mo	2.0/mo	1.3/mo	1.4/mo	1.6/mo	2.2/mo	3.2/mo	3.2/mo	3.7/mo
Months of Total Inventory	27.4 mos.	17.8 mos.	39.4 mos.	38.9 mos.	23.2 mos.	14.3 mos.	6.7 mos.	11.9 mos.	7.7 mos.

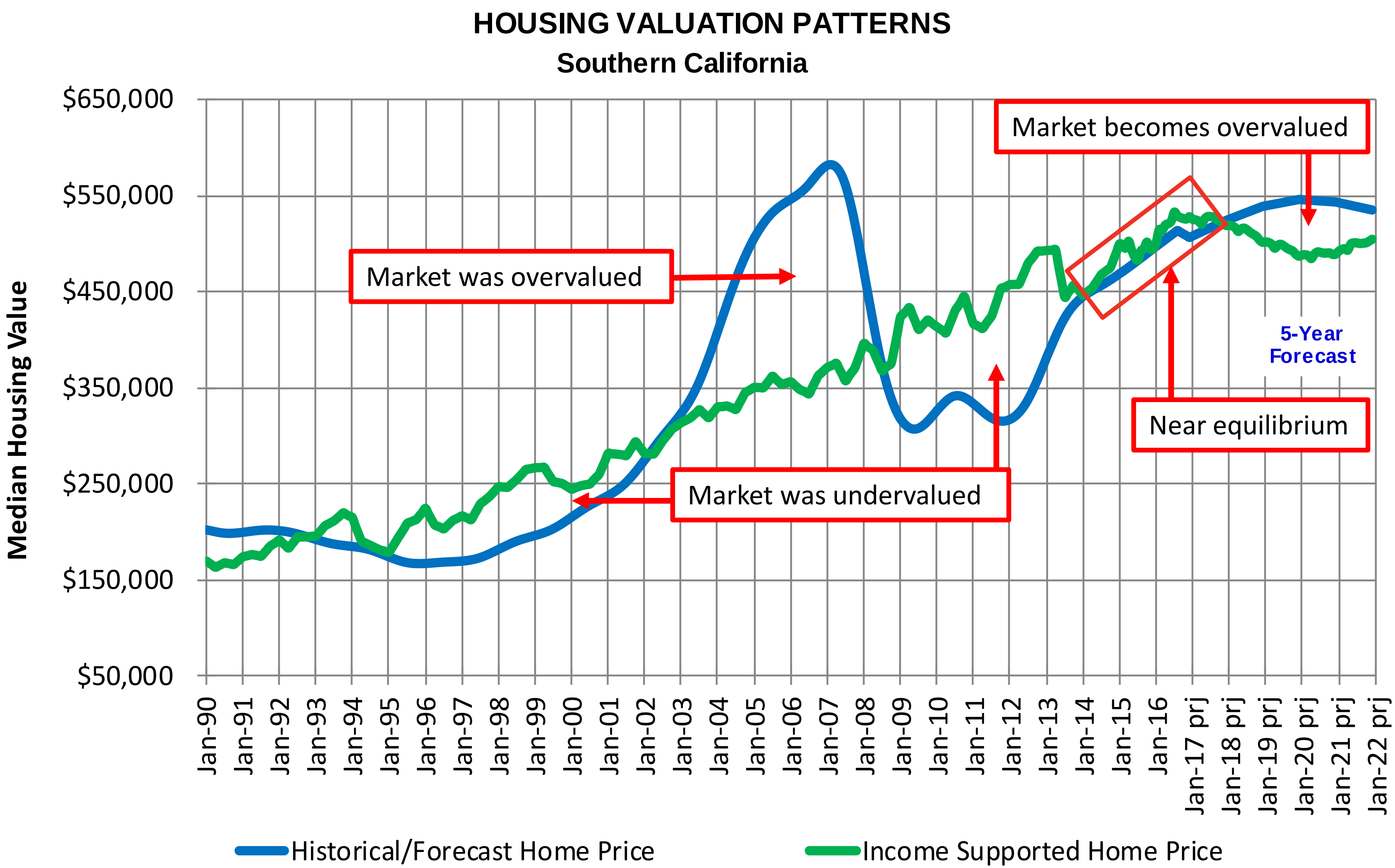
San Diego attached new home supplies have not meaningfully recovered.

Buyers have very few product and location options.



Source: Bureau of Labor Statistics; Moody's Analytics; Real Estate Economics
www.realestateeconomics.com

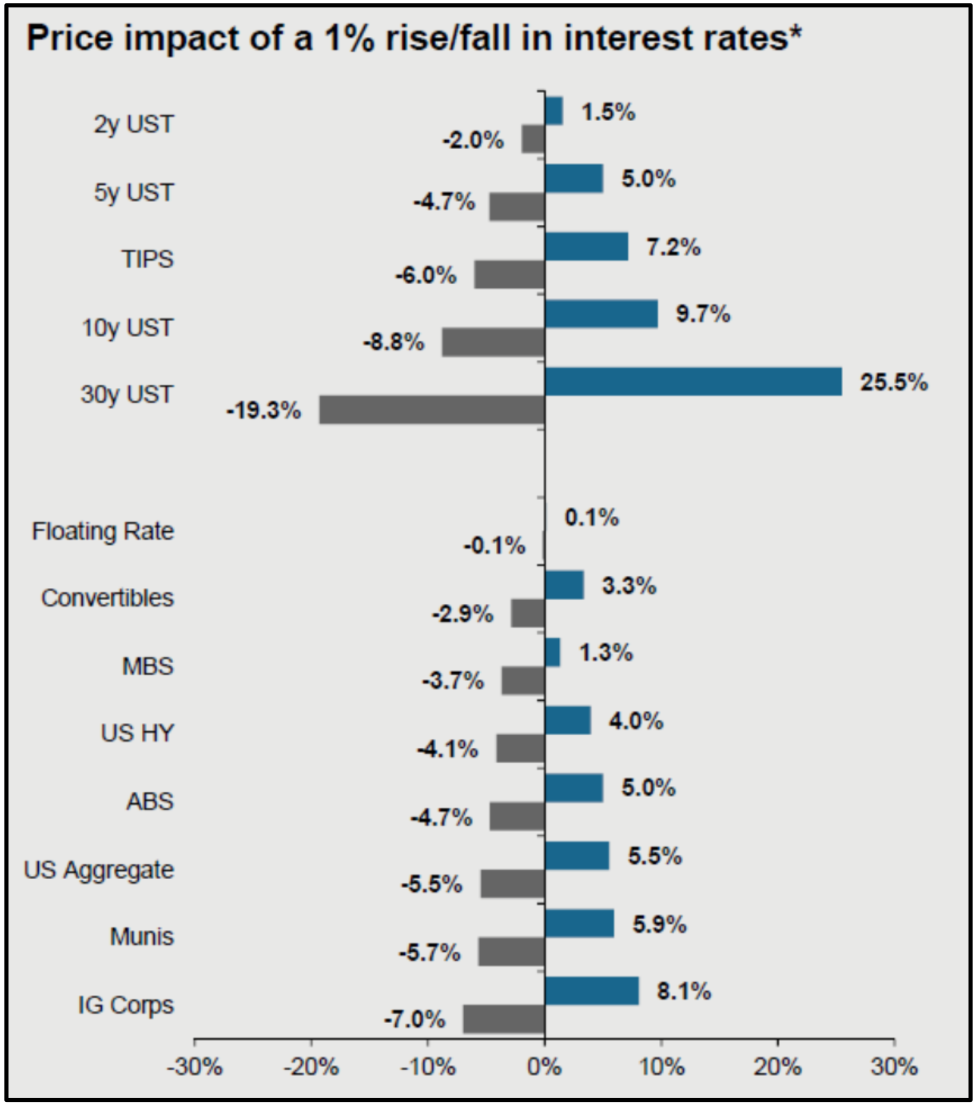
OVERVALUATION VS. UNDERVALUATION



Source: Bureau of Labor Statistics; Moody's Analytics; Real Estate Economics

Interest Rate Outlook

HOW RISING RATES IMPACT BOND PRICES



Source: JP Morgan Asset Management, 4th Quarter 2016

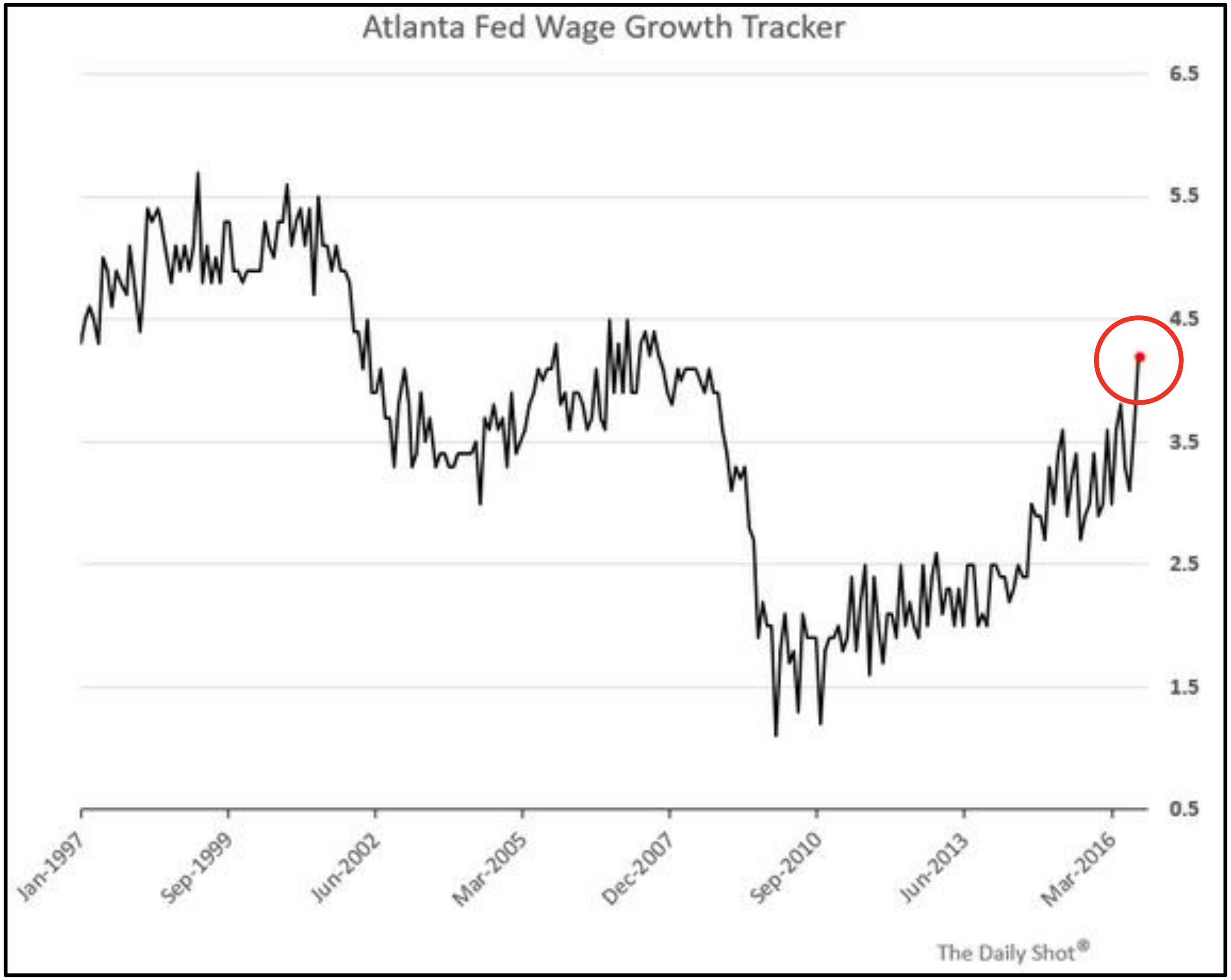
Interest rate markets are very sensitive to higher rates since small rate increases can cause bond prices to fall substantially.

Category	Direction	Short Term Trend
Incomes	⇧	Accelerating
Housing Costs	⇧	Moderating
Medical Costs	⇧	Accelerating
Fuel Costs	⇧	Plateau
Taxes (All types)	⇧	Accelerating
Insurance Costs	⇧	Accelerating

With most major cost categories increasing inflationary pressures are building.

Rising inflation is NOT a U.S. phenomena, it’s global.

ACCELERATING WAGE GROWTH

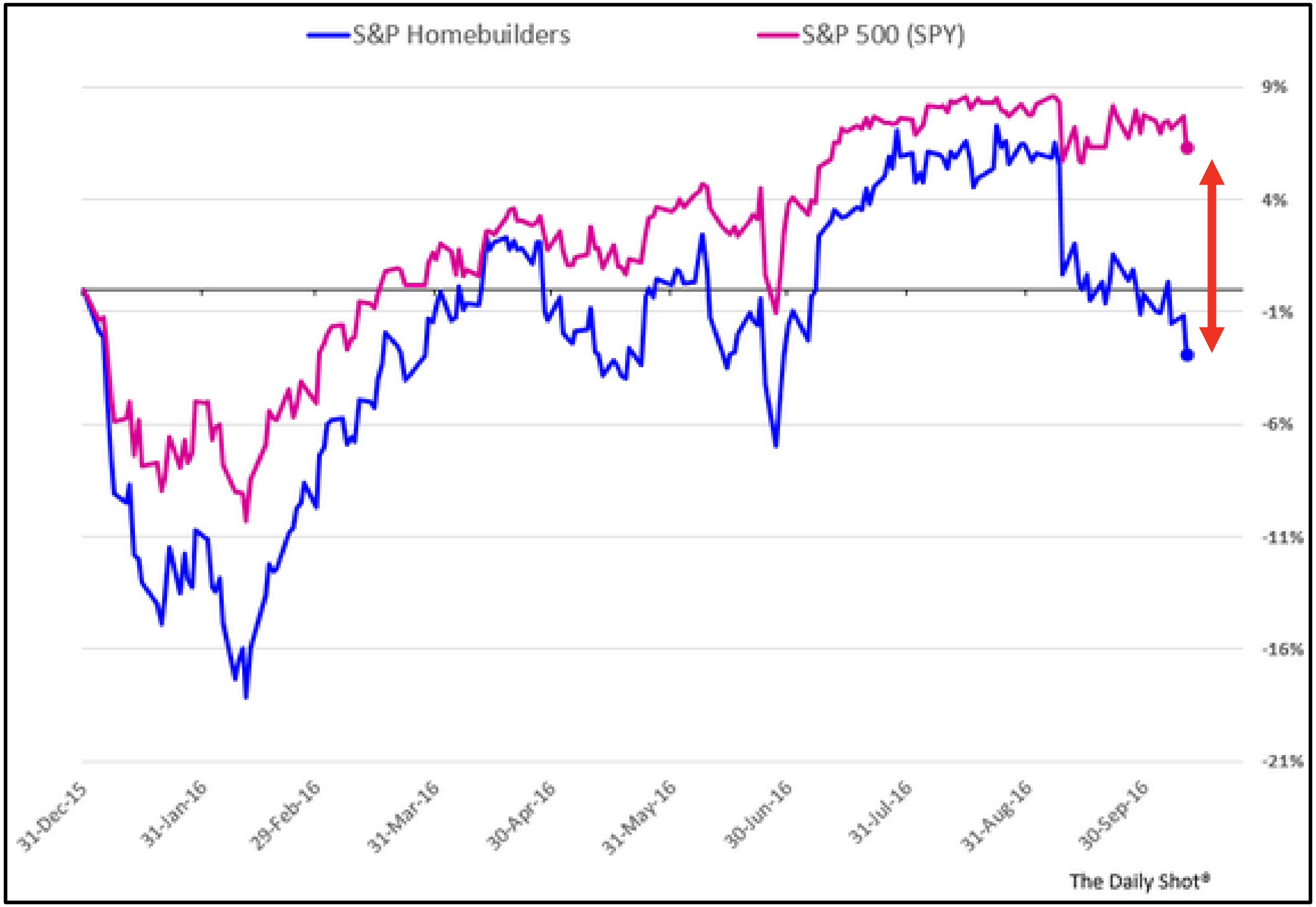


Wage inflation is the most important driver of general inflation.

GASOLINE COSTS ARE TRENDING HIGHER

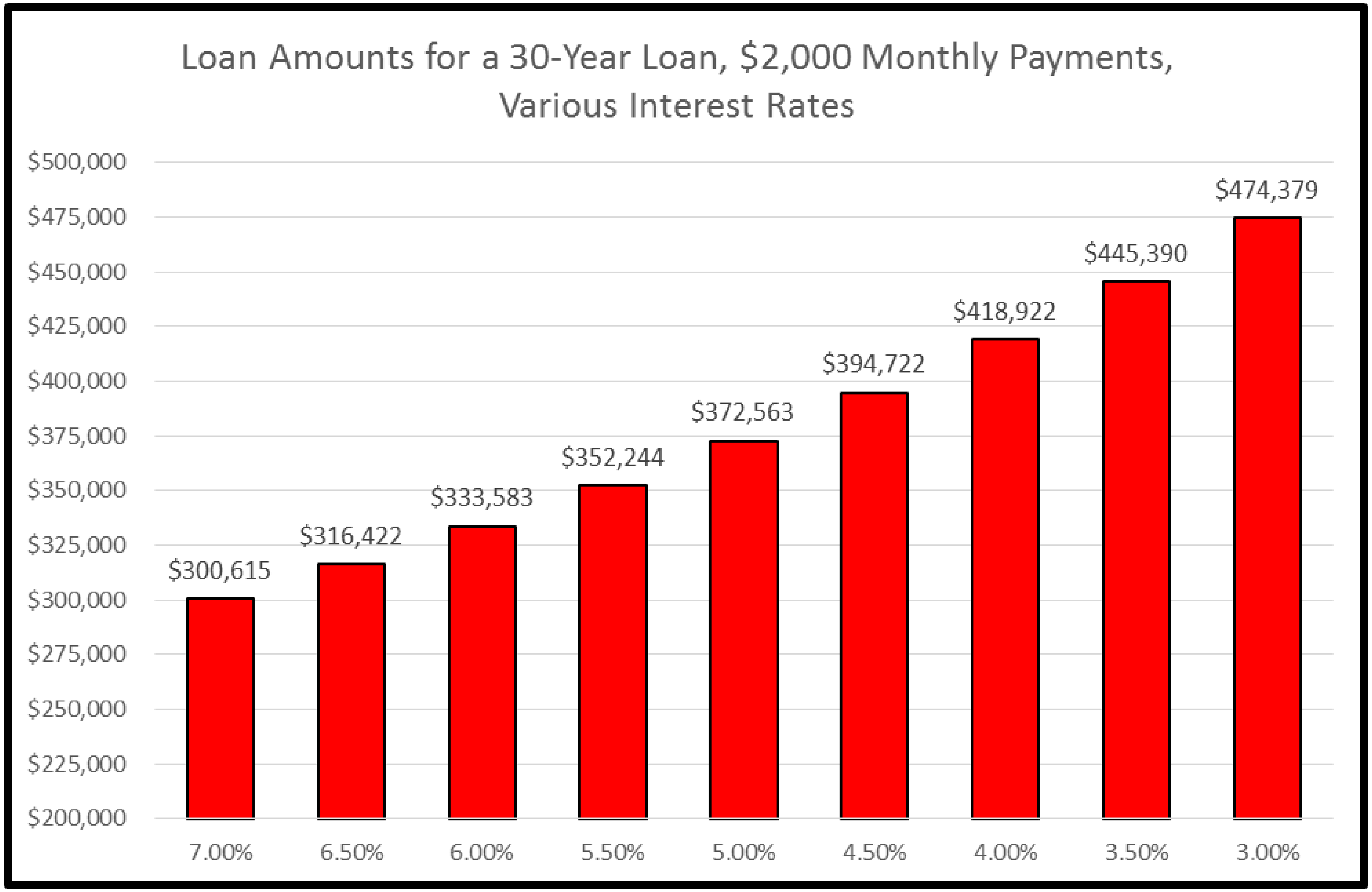
Fuel prices are rising off of a very low base. As a result, year-over-year comparisons will show large increases.

RATE EXPECTATIONS ARE IMPACTING HOMEBUILDER STOCKS



Homebuilder stocks moved with the S&P 500 for most of 2016. Investors are expecting that interest rates will be more impactful to the homebuilders than the stock market as a whole.

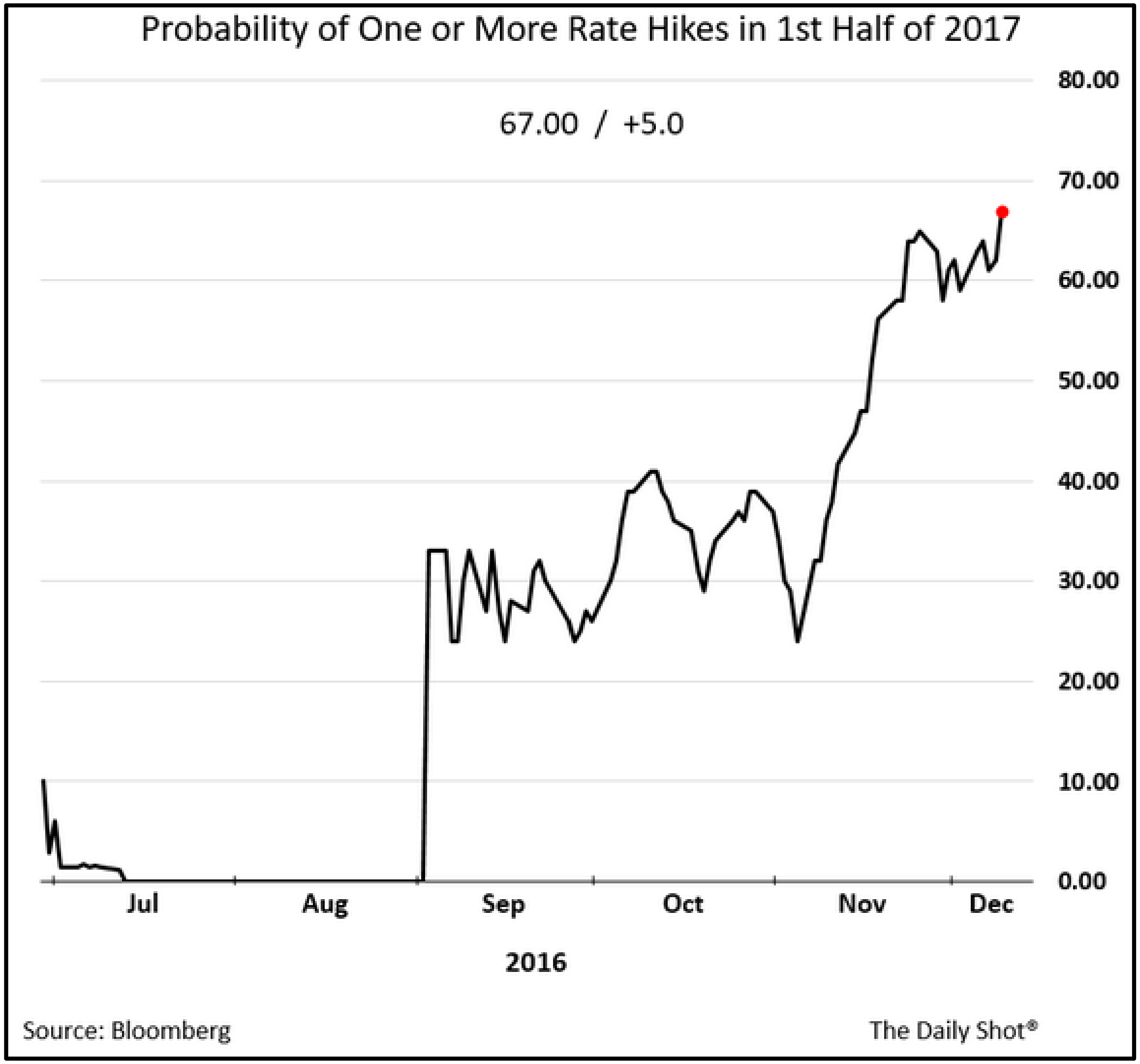
INTEREST RATE INCREASES WILL IMPACT AFFORDABILITY



Rate increases have been “around the corner” for so long that the market was desensitized.

Small increases WILL be impactful to affordability and land values.

PROBABILITY OF MORE RATE HIKES IN 2017



Source: Bloomberg, Fed Funds Futures 12/20/16

The chance of another rate increase in the first half of 2017 are perceived to be increasing.

CONCLUSIONS

- Growing incomes and continued low interest rates are supportive of housing demand.

- Housing demand is broadening, Millennials, first timers, skilled immigrants and mature households are all poised to play a greater role.

- Builders have not been able to add enough supply. As a result, housing is expensive, but it is not plentiful.

- Interest rates will trend modestly higher (not jump). <u>Make sure lenders will lock their rates until your buyers homes are ready to close.</u>

- The economies of Europe, Japan, Russia and China have enormous problems. The U.S. is in a far better position than is widely realized.

- There are some problems on the horizon.

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Thank you for your time and attention.

Please direct any questions to:

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