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THOMPSON THRIFT

2023 Multifamily Market Outlook

PREPARED FOR OUR INVESTMENT PARTNERS

APRIL 2023

THIS DOCUMENT IS BEST VIEWED IN LANDSCAPE ORIENTATION, SPREAD VIEW.

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A REAL ESTATE COMPANY

THOMPSONTHRIFT.COM

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The Crossings • Lyon Township, MI



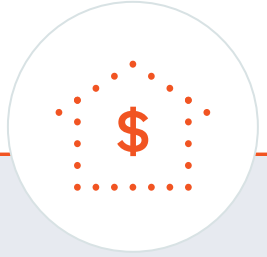
Key Facts

Key Facts



Migration to new growth states continues, driving population growth in the southern and western regions and outpacing the national average between 2010-2022.

(IPA, 2023)



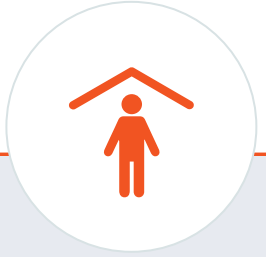
Demand drivers for multifamily are high; structural supply remains low with new supply forecasted to reach a deeper deficit.

(JBREC, 2023)



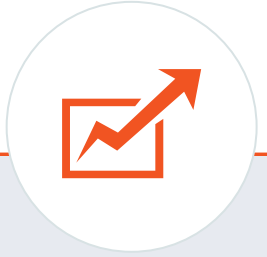
Forecasters predict multifamily starts will fall 50% from 2022 levels through 2024, reducing future supply.

(JBREC, 2023)



Single-family housing starts are predicted to drop 25% from peak 2021 levels.

(JBREC, 2023)



The affordability gap (cost of owning versus renting) has never been higher at over $1,100/month.

(IPA, 2023)



The upward movement in interest rates from 3.5% at the beginning of 2022 to 6.5% in early 2023 has effectively priced an estimated 16 million U.S. households out of homeownership.

(NAHB, 2023)

Key Facts



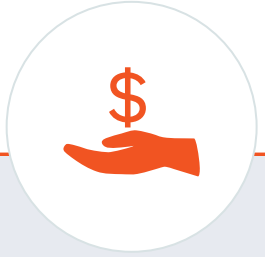
With 2.9 months of supply, the U.S. supply of existing homes for-sale remains near record lows.

(JBREC, 2023)

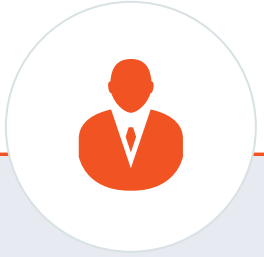


Multifamily occupancy remains strong at 94.7% as of February 2023.

(RealPage, 2023)

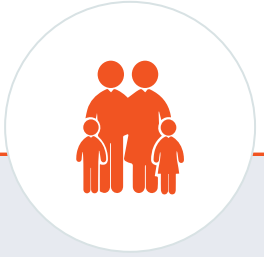


Rent-to-income ratios for our stabilized properties remain healthy at 23%, showing that our renters have capacity for increased rent growth.



The median age of first-time buyers has jumped from 29 years in 1981 to 36 in 2022, the oldest age recorded by the National Association of Realtors.

(NAR, 2022)



Since 2020, the number of young adults continuing to live at home, potential future renters, has increased to highs not seen since the 1940s.

(NMHC, 2023)



Average student loan debt reached a record high of $41,700 in 2022, further impacting homeownership affordability.

(NSLDS, 2022)



Avenue64 • O’Fallon, MO



Opening Letter

FROM PAUL THRIFT

"There is terrific opportunity to complete successful multifamily development projects and generate solid returns."

Opening Letter

FROM PAUL THRIFT

To our valued partners,

This 2023 first quarter Market Outlook covers how we see multifamily market conditions now and going forward, including the latest market data informing our outlook.

In short, current macroeconomic headwinds persist. However, we believe there is terrific opportunity to complete successful multifamily development projects and generate solid returns.

WINNING CYCLE

We develop properties in high in-migration markets that are creating jobs and attracting a highly qualified workforce. The markets we are focused on (FL, AZ, CO, NC, GA, and TX) have decades-long histories of population growth and are seeing an enormous amount of capital investment and job creation. We believe this job and population migration from old growth markets to new growth markets will continue for many years to come as job creation follows lower-cost environments and a qualified workforce, and population follows jobs (the “Winning Cycle”).

THOMPSON THRIFT IS INFORMED ON CURRENT MARKET CONDITIONS

We pride ourselves on being students of the multifamily market. We are data and research driven, exceeding the standard diligence typically applied in our industry. Over the past 12 months, we have increased observation and study of market conditions to an even higher level to match the shifting dynamics of the market.

The economy has experienced significant change in the past year. As the Federal Reserve has acted to slow inflation by slowing economic growth through increased interest rates, we have seen debt and equity capital sources tighten and single-family (for sale) and multifamily (for rent) new starts slow, reducing future housing supply.

Although market headwinds create near-term challenges, we are bullish that current circumstances create increased opportunity for Thompson Thrift to capitalize on market conditions and continue to create value through our development process, offering the opportunity for premium returns.

CURRENT THOMPSON THRIFT PROJECTS CONTINUE TO PERFORM WELL AND LOOK VERY PROMISING

Current projects in our 2020, 2021, and 2022 Funds continue to perform well with promising expected performance.

Our current leasing volume remains in line with the three previous consecutive years and is keeping pace with our proforma

lease-up schedules. We experienced explosive rent growth in 2021 and early 2022, and our properties currently in lease-up are exceeding proforma rents.

Projects under construction are progressing at a pace that exceeds the past few years. These projects have an attractive cost basis compared to current valuations and are projected to deliver good returns when we are ready to take them to the market for sale.

Increased interest rates have raised the cost of our construction loan interest carry, causing our interest expense to exceed our interest budgets. These interest expense overages, while material, are manageable and have minimal impact on the overall cost basis. We remain in a strong cash position and plan to provide loans to the partnerships to fund these interest expense overages.

We remain highly confident in our markets, locations, product type, cost basis, and overall potential to deliver strong returns from these assets.

2023 AND 2024 WILL PRODUCE HIGH MULTIFAMILY DELIVERIES

2023 and 2024 will bring high deliveries of annual multifamily housing units due to a high volume of project starts in 2021 and 2022 (JBREC, 2023). This new supply will likely subdue rent growth and slow absorption during this period. However, an estimated 40% of this new product is concentrated in the top 10 U.S. gateway markets, much within the urban cores (IPA, 2023).

Our suburban projects will certainly experience some effects of this heavy supply, but not to the same extent as the gateway and urban markets. This affirms our strategy of carefully selecting our target suburban markets with high in-migration, high job growth, barriers to entry, and proper supply and demand balance.

Additionally, our commitment to developing sites with a compelling story located near high traffic corridors, high-end housing, job centers, and convenient retail continues to pay dividends with strong performance. Adhering to disciplined fundamentals pays off in turbulent environments.

OCCUPANCIES AND RENTS ARE PREDICTED TO REMAIN STRONG

Despite high multifamily deliveries in 2023 and 2024, respected industry sources forecast occupancies to remain healthy at 94-95% through 2024 (RealPage, 2023; Yardi, 2023). Year-over-year national multifamily rent growth is 4.5% as of February 2023 (RealPage, 2023). Average rent growth for 2023 and 2024 is projected to be 2-4% nationally with growth projected in later years as new supply is constrained (RealPage, 2023; Yardi, 2023).

Rent-to-income ratios (renter's percentage of income paid on housing) for our stabilized properties remain healthy at 23%, showing that our renters have capacity for increased rent growth.

STRUCTURAL HOUSING DEFICIT CONTINUES TO EXIST

Despite increased starts of single-family and multifamily construction in 2021 and 2022, a structural housing deficit continues to exist. After 13 years of significant undersupply of new housing units, single-family inventories remain low, multifamily occupancies remain high, and demand should continue to outpace supply over the next decade (RealPage, 2023; JBREC, 2023).

2023 AND 2024 NEW SINGLE-FAMILY FOR SALE STARTS WILL DROP CONSIDERABLY

Due to higher values and rising interest rates, single-family housing starts are predicted to drop more than 25% from peak 2021 levels, adding to the structural U.S. housing deficit that will reveal itself again in late 2024 to 2026 as household formation returns, increasing demand (JBREC, 2023). Higher cost single-family housing resulting from the imbalance of supply and demand will likely drive more people to rent. The affordability gap (the cost of owning versus renting) has never been higher at over $1,100 per month (IPA, 2023).

While rents have increased over the past several years, they have not increased at the same level as homeownership cost due to increasing values and interest rates. The move in interest rates from 3.5% at the beginning of 2022 to 6.5% in early 2023 has effectively priced an estimated 16 million U. S. households out of homeownership (NAHB, 2023).

2023 AND 2024 NEW MULTIFAMILY FOR-SALE STARTS WILL DROP CONSIDERABLY

Construction debt is difficult to source as national banks have pulled back from construction lending and tightened their underwriting standards. Institutional development equity is severely restricted due to the market uncertainty and the “herd” mentality of the institutional capital community. Forecasters predict multifamily starts will fall 50% from 2022 levels to 2024 starts, reducing supply to the market in 2025, 2026, and 2027 (JBREC, 2023).

LOWER HOUSING STARTS CREATES A WINDOW OF OPPORTUNITY FOR THOMPSON THRIFT

Thompson Thrift has a **window of opportunity** to start projects when many developers cannot access capital. Our ability to source debt and equity during this period puts us in a unique position to start multifamily units during 2023 and 2024 to deliver in 2025, 2026, and 2027 when housing deliveries and supply are low.

VALUATIONS

Multifamily values skyrocketed in 2021 and the first half of 2022. Compressed cap rates, low-cost debt, and abundant capital seeking yield drove the market to aggressive underwriting standards. Values were driven up at an unsustainable pace. We were fortunate to sell many of our 2020 Fund projects ahead of schedule during peak valuations in 2022.

We have seen values retrace approximately 10-20% from their peak due to buyers sitting on the sidelines because of rising interest rates, lower leverage options, and market uncertainty.

Despite the drop from peak pricing, values remain attractive and offer good returns on cost. Apartment assets offer competitive yields for buyers compared to alternatives worldwide. Current projects in our 2020, 2021 and 2022 Funds are all in good standing with strong projected valuations in comparison to cost basis. We believe buyers sitting on the sidelines will return to the market during the second half of 2023 and 2024, anxious to deploy capital and seeing value opportunities in the market. The two remaining 2020 Fund properties are not projected to stabilize until late 2023, allowing us to be patient and evaluate the best time to go to market and optimize returns.

CONSTRUCTION COST INCREASES HAVE LEVELED OFF

We have real time knowledge of current construction pricing as we are contracting with subcontractors and suppliers in multiple markets across the U.S. We see a deceleration of construction cost increases. We do not expect an overall cost decrease in the future, but a flatlining of overall cost which benefits our 2023 and 2024 project starts.

TERRIFIC OPPORTUNITY

Given the decline in single-family and multifamily supply in 2025 and 2026, the fundamental strength of our underlying markets and strategy, our ability to start projects during this window, and our overall market outlook, we are optimistic about our existing portfolio and future development pipeline.

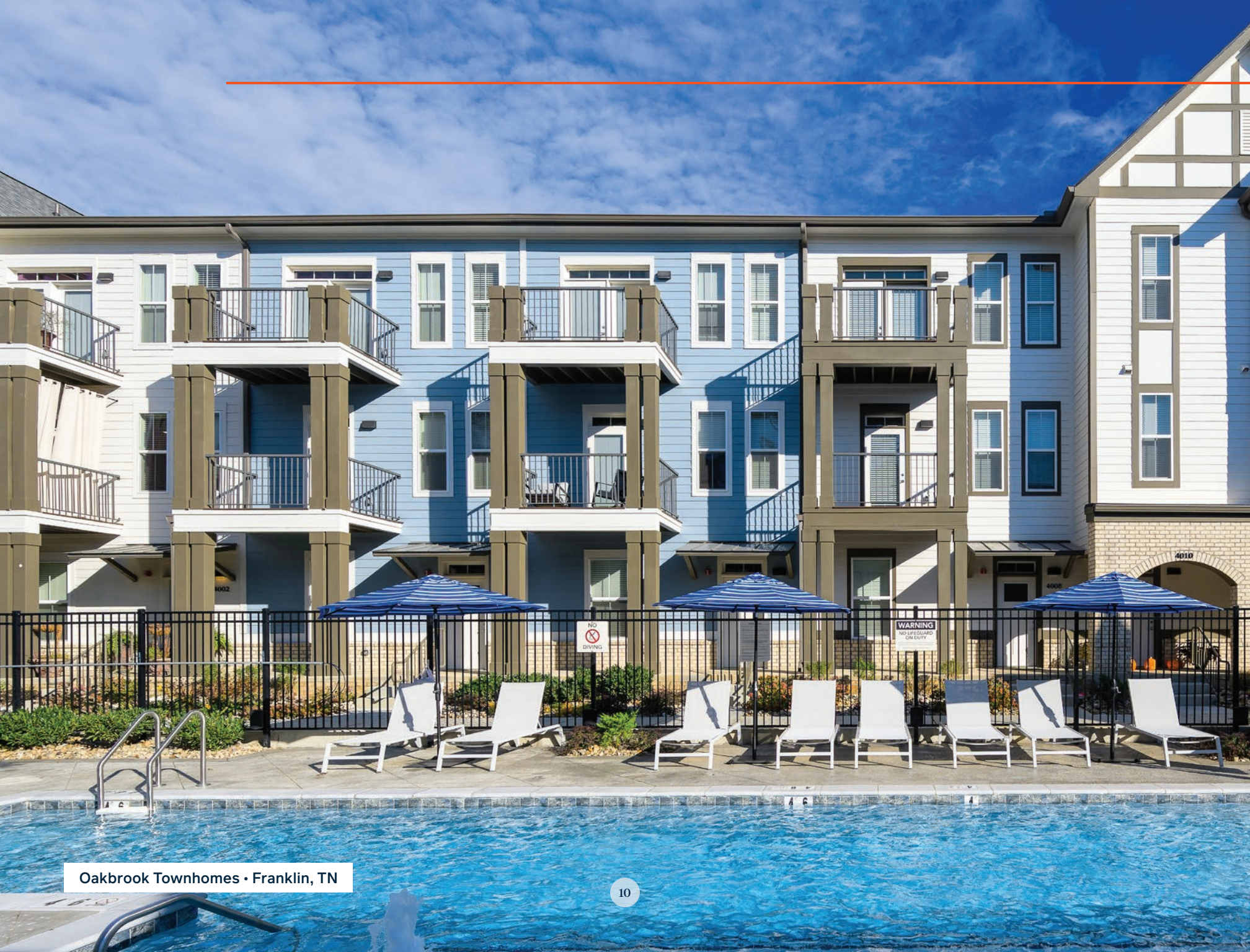
We continue to pursue strategically located sites in growth markets that meet our strict market and site criteria and exceed our projected performance standards. We are passionately dedicated to remaining disciplined in our underwriting standards. Based on our current projections, we expect to be in position to capture opportunities and create value through our proven ground-up multifamily development process.

Thank you for your continued confidence and support.



Paul Thrift

CEO



Oakbrook Townhomes • Franklin, TN



Market Data

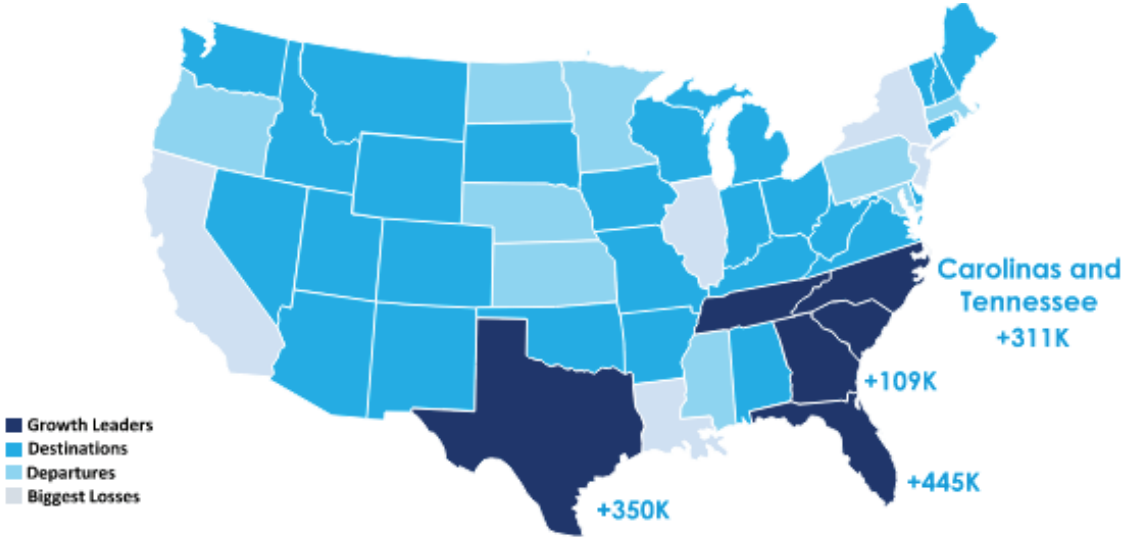
Multifamily Demand Drivers

MIGRATION TRENDS

Decades-long migration patterns from old growth markets to new growth markets in the West (Mountain and Desert) and Southeast continue to drive housing demand in select markets. The “Winning Cycle” continues for these markets as job creation follows lower-cost environments and a qualified workforce, with population following jobs.



POPULATION GROWTH: 2022



Annual net migration as of 2022
Sources: IPA Research Services, U.S. Census Bureau

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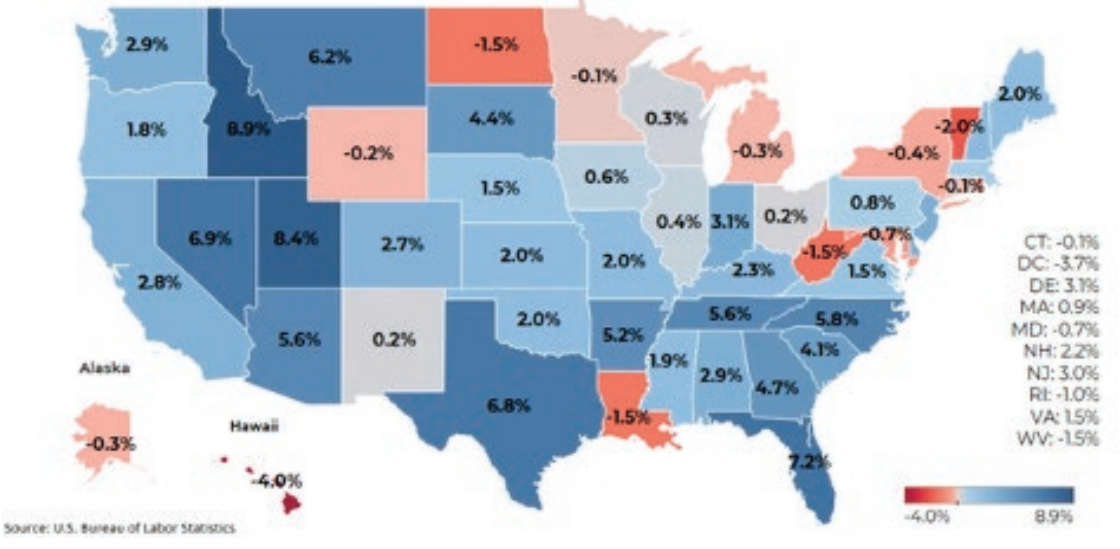
JOB GROWTH: MARCH 2020-JANUARY 2023

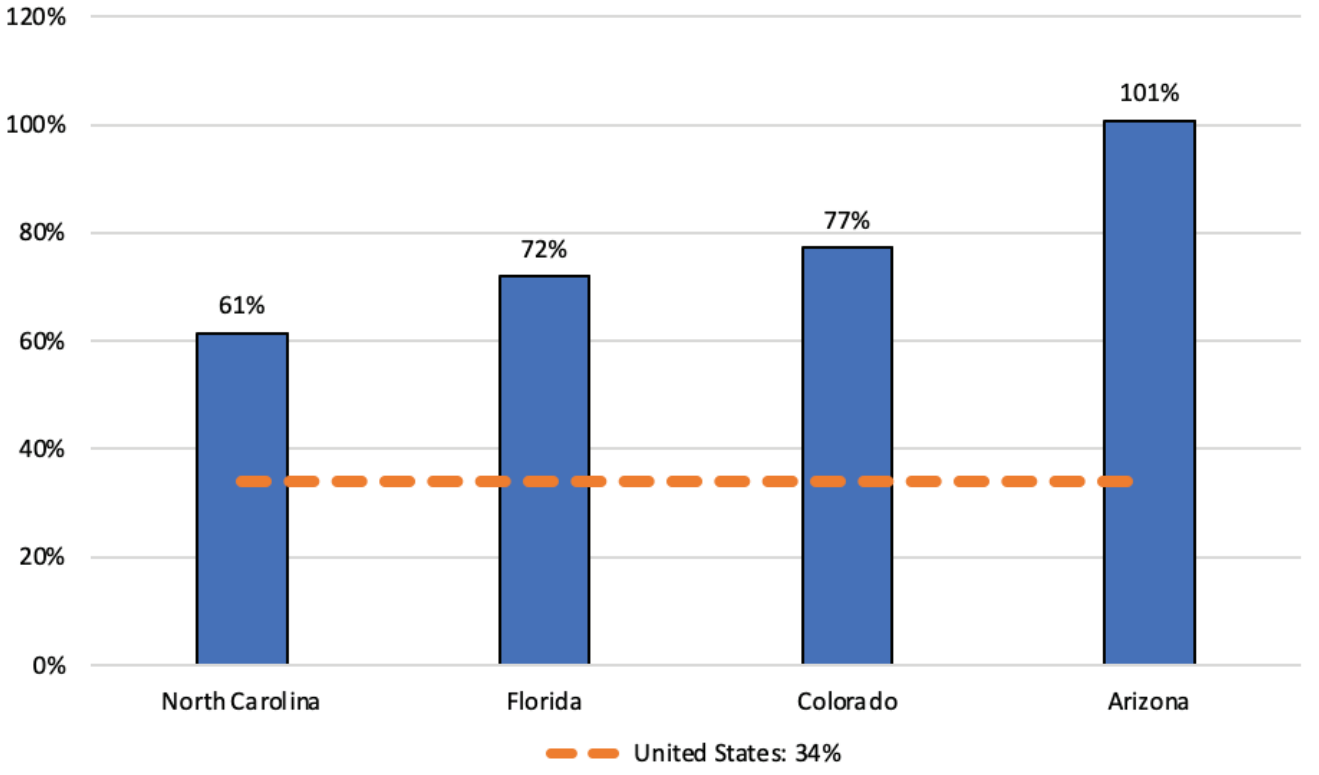


Source: U.S. Bureau of Labor Statistics

Multifamily Demand Drivers GROWTH MARKETS

We develop properties in high in-migration markets that are creating jobs and attracting a highly qualified workforce. The markets we focus on have a decades-long history of population growth and are seeing an enormous amount of capital investment and job creation (Census Bureau, 2023; BLS, 2023).

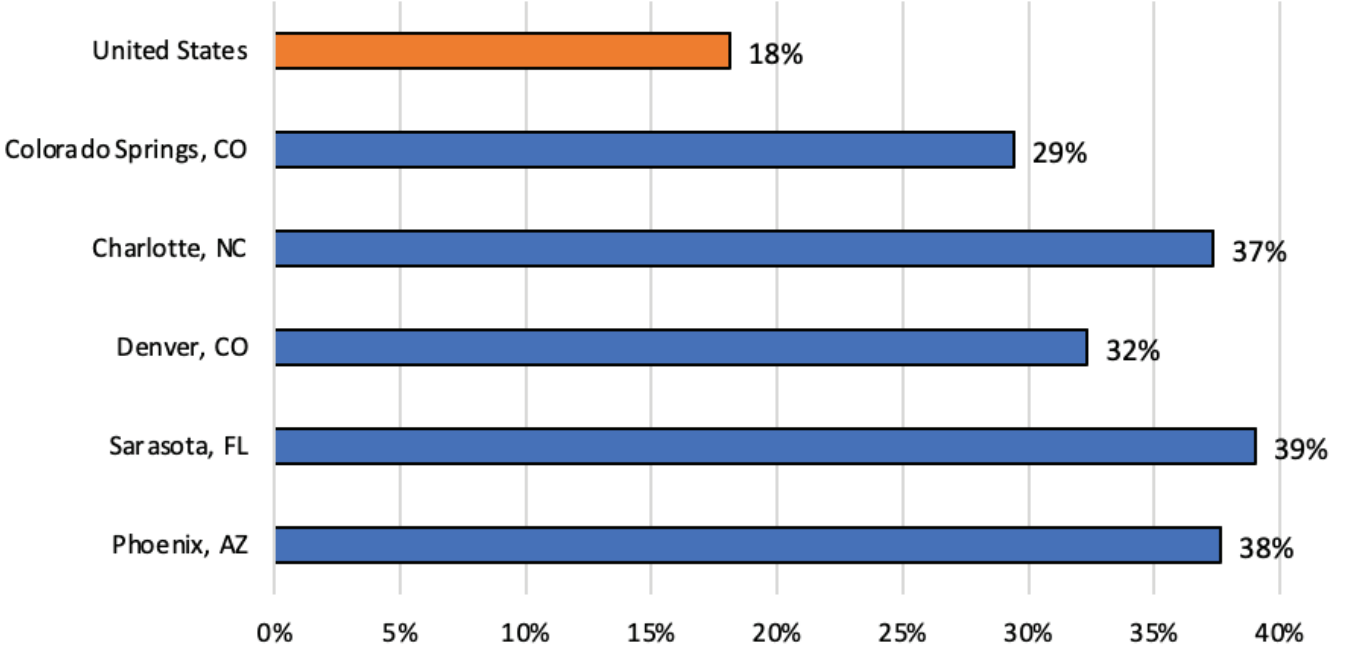
1990-2022 POPULATION GROWTH



Multifamily Demand Drivers

GROWTH MARKETS

2010-2022 EMPLOYMENT % CHANGE

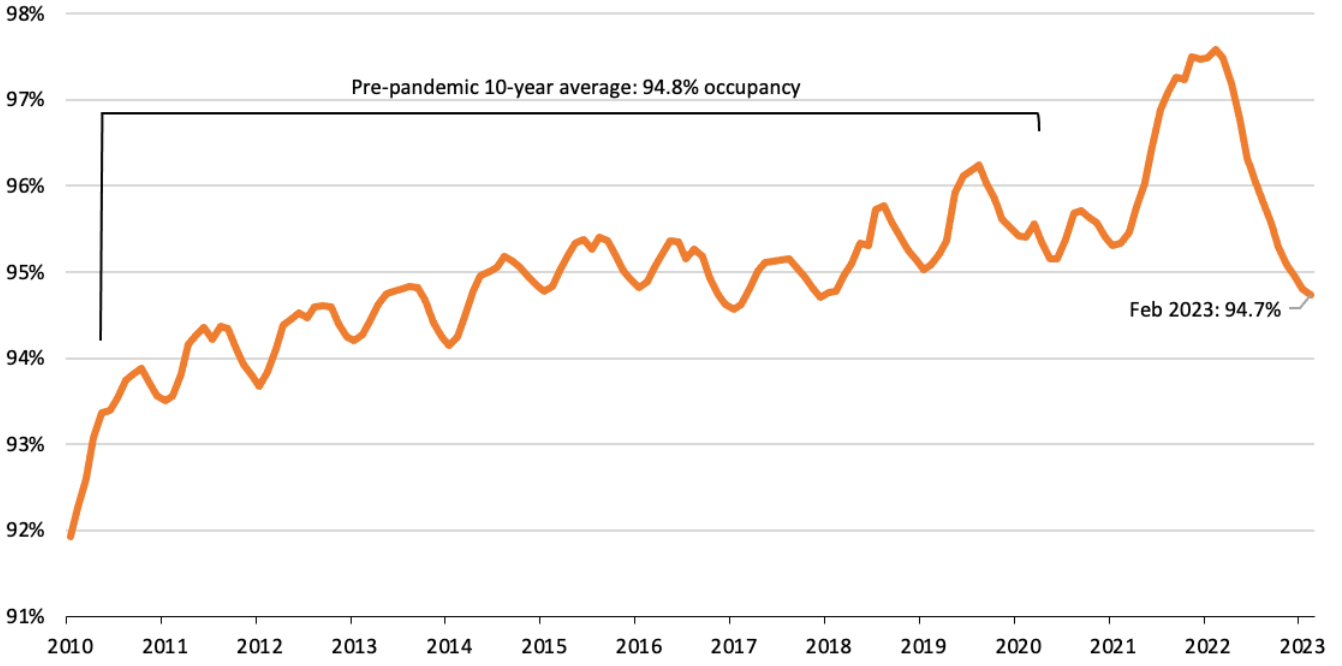


Housing Supply and Demand

MULTIFAMILY OCCUPANCY

U.S. multifamily occupancy remains at the pre-pandemic 10-year average. Multifamily occupancy is now 94.7% as of February 2023. Despite high multifamily deliveries in 2023 and 2024, respected industry sources forecast occupancy to remain within a healthy range of 94-95% through 2024 (RealPage, 2023).

U.S. MULTIFAMILY OCCUPANCY RATE

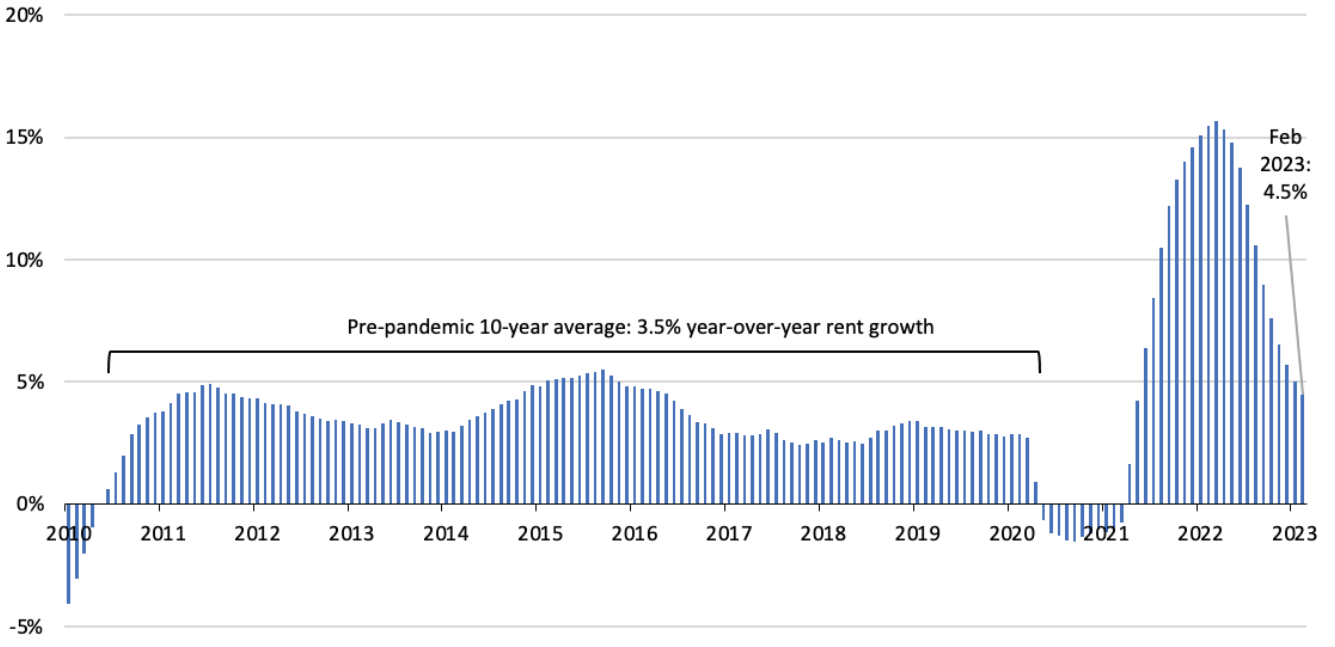


Housing Supply and Demand

MULTIFAMILY RENT GROWTH

Year-over-year national multifamily rent growth is 4.5% as of February 2023. Forecasted average rent growth for 2023 and 2024 ranges between 2-4% nationally, across asset classes, with continued projected growth thereafter (RealPage, 2023).

U.S. MULTIFAMILY RENT GROWTH, YEAR-OVER-YEAR

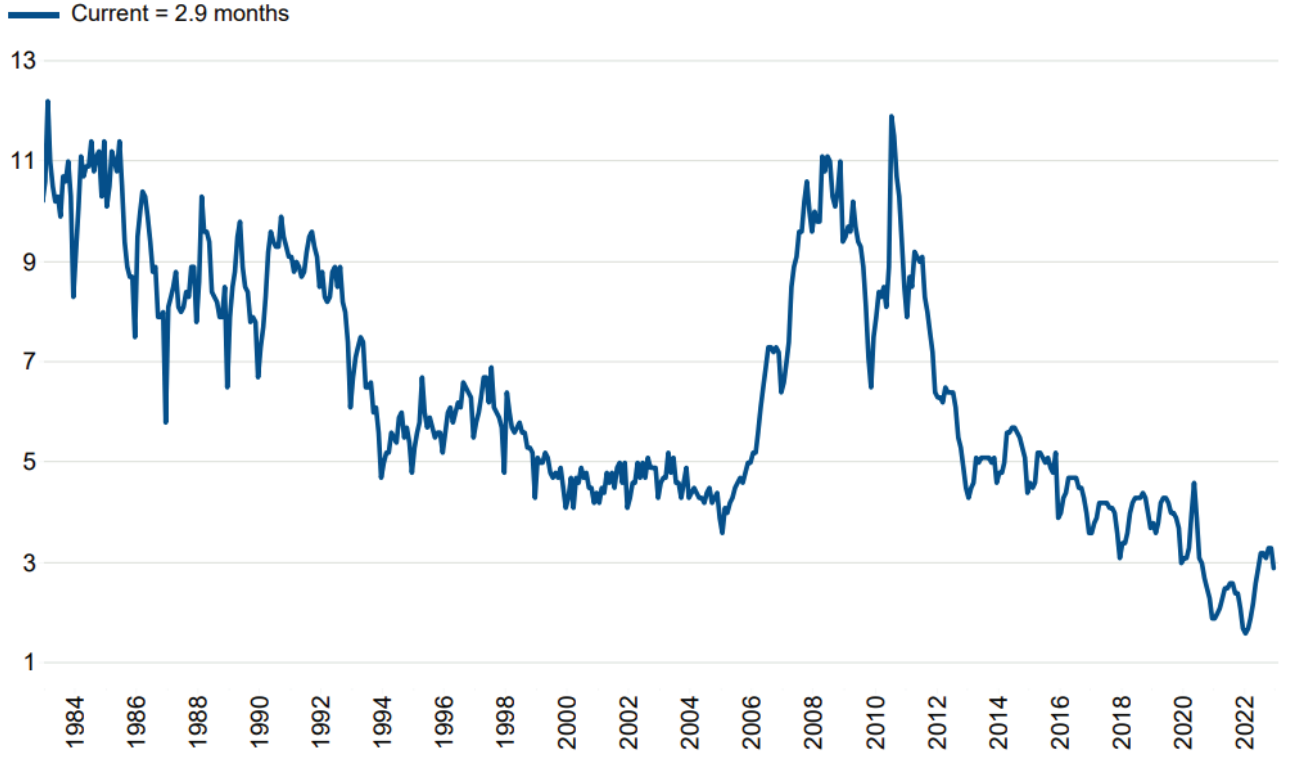


Housing Supply and Demand

U.S. SINGLE-FAMILY INVENTORY

The U.S. continues to experience a structural deficit in both single-family and multifamily housing. With 2.9 months of supply, the U.S. supply of existing single-family homes for sale remains near record lows (JBREC, 2023).

EXISTING HOME MONTHS OF SUPPLY



Sources: NAR; John Burns Real Estate Consulting, LLC (Data: Dec-22, Pub: Feb-23)

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Prepared exclusively for Thompson Thrift: Mike Morgan

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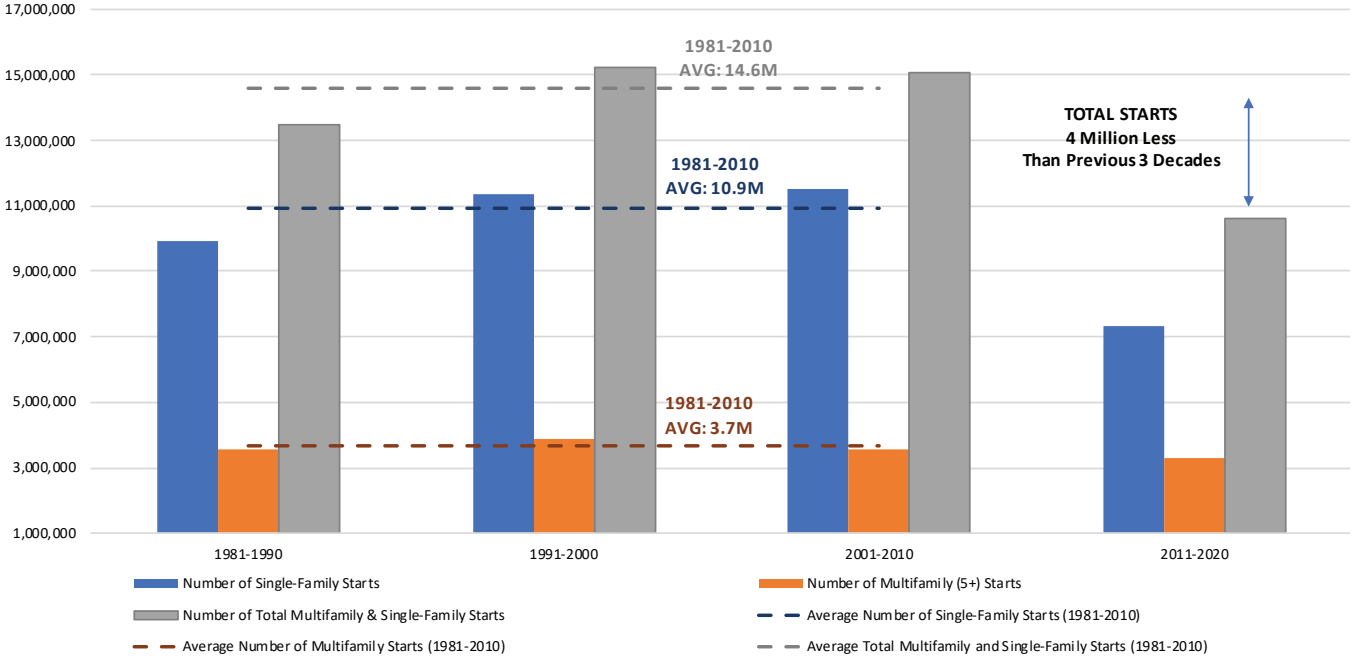
Housing Supply and Demand

U.S. HOUSING UNDERSUPPLY

Between 2011 and 2020, a total of 10.6 million units were started in the U.S. This is 27% below the average of the previous three decades (14.6 million) and further contributed to the national housing undersupply (Census Bureau, 2023).

NUMBER OF SINGLE-FAMILY AND MULTIFAMILY HOUSING STARTS



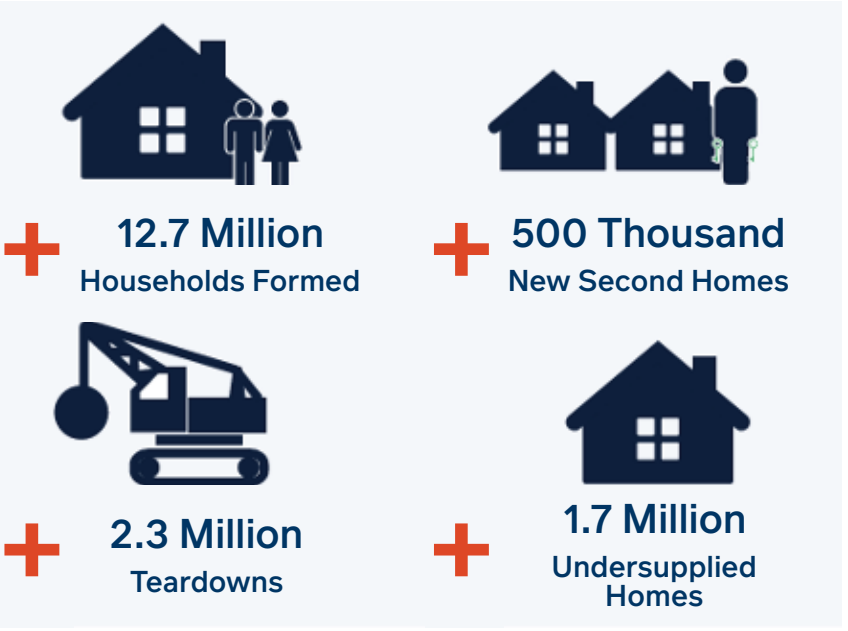
Source: U.S. Census, Compares Rolling 10-Year Periods of SF & MF Starts

Housing Supply and Demand

U.S. HOUSING SUPPLY

According to John Burns Real Estate Consulting, U.S. housing demand will continue to outpace supply. An estimated 17.2 million new housing units will be needed over the next decade (2020-2030) to satisfy long-term demand (1.7 million annually) (JBREC, 2022). By contrast, just 1.3 million units are projected to start in 2023 and 1.1 million in 2024, well below the number needed to satisfy long-term demand (JBREC, 2022).

PROJECTED HOUSING DEMAND: JULY 1, 2020 - JULY 1, 2030



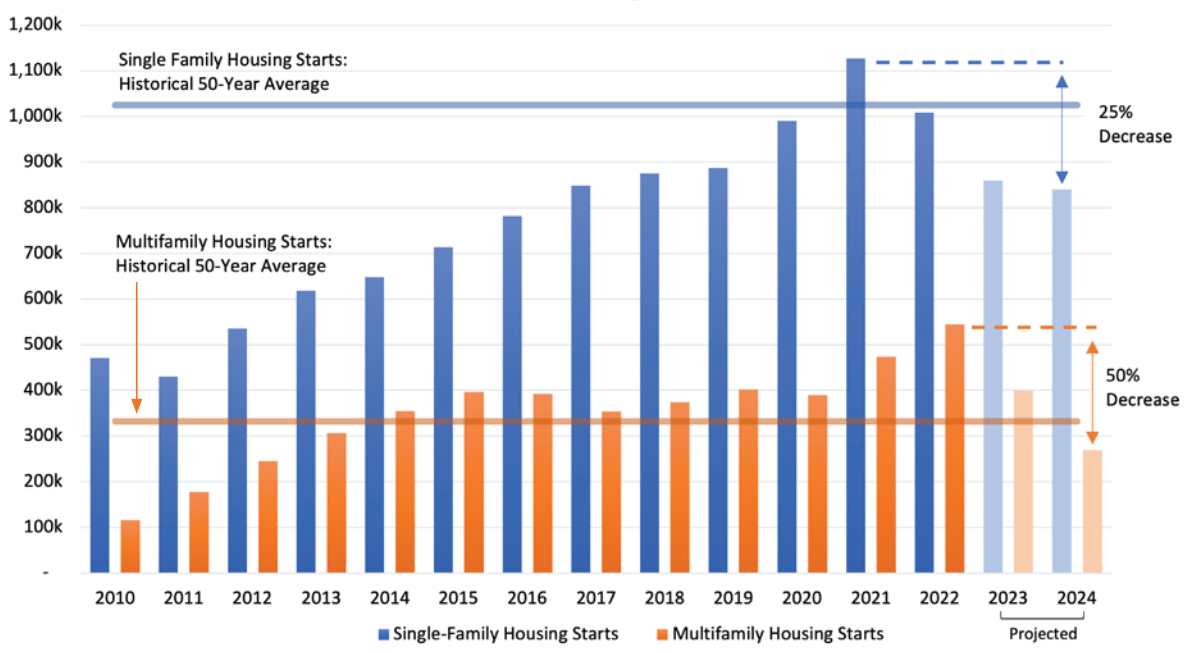
Housing Supply and Demand

U.S. HOUSING STARTS

Nationally, total housing starts will decline over the next two years as construction slows in response to recent rate increases and reduced access to capital. According to John Burns Real Estate Consulting, single-family starts could drop over 25% from peak 2021 levels (JBREC, 2023).

Multifamily starts are projected to decline 50% from peak 2022 levels through 2024, reducing supply coming to market in 2025, 2026, and 2027. The slowdown in starts will contribute to the undersupply of housing in 2025 and 2026 as the economy recovers from an anticipated recessionary period, and demand growth resumes (JBREC, 2023). In the near-term, projects starting in 2023 and 2024 will have a window of opportunity to deliver during this anticipated low-supply period.

NUMBER OF SINGLE-FAMILY AND MULTIFAMILY HOUSING STARTS

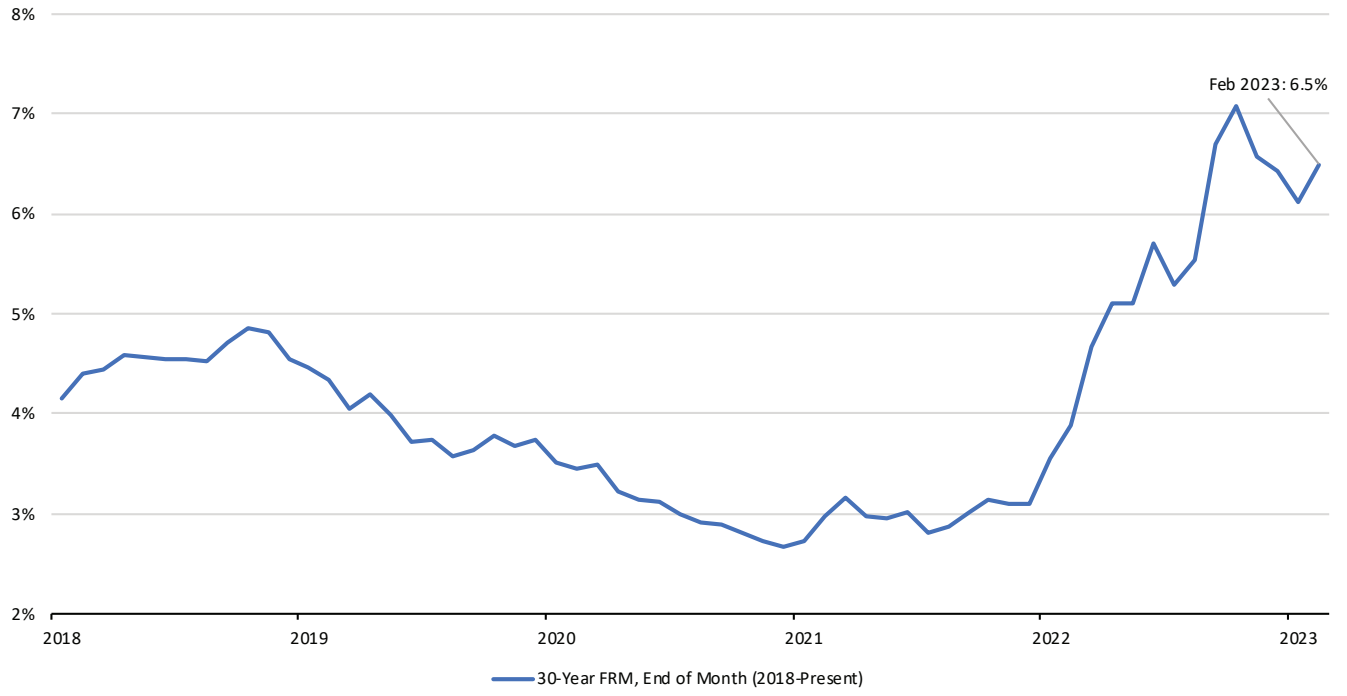


Housing Supply and Demand

INCREASING MORTGAGE RATES

Higher mortgage rates have impacted affordability and demand for single-family housing, contributing to a reduction in single-family starts. After rising sharply in 2022, rates for a 30-year fixed rate mortgage have eased to a rate of 6.50% as of February 2023 (Freddie Mac, 2023).

30-YEAR FIXED RATE MORTGAGE

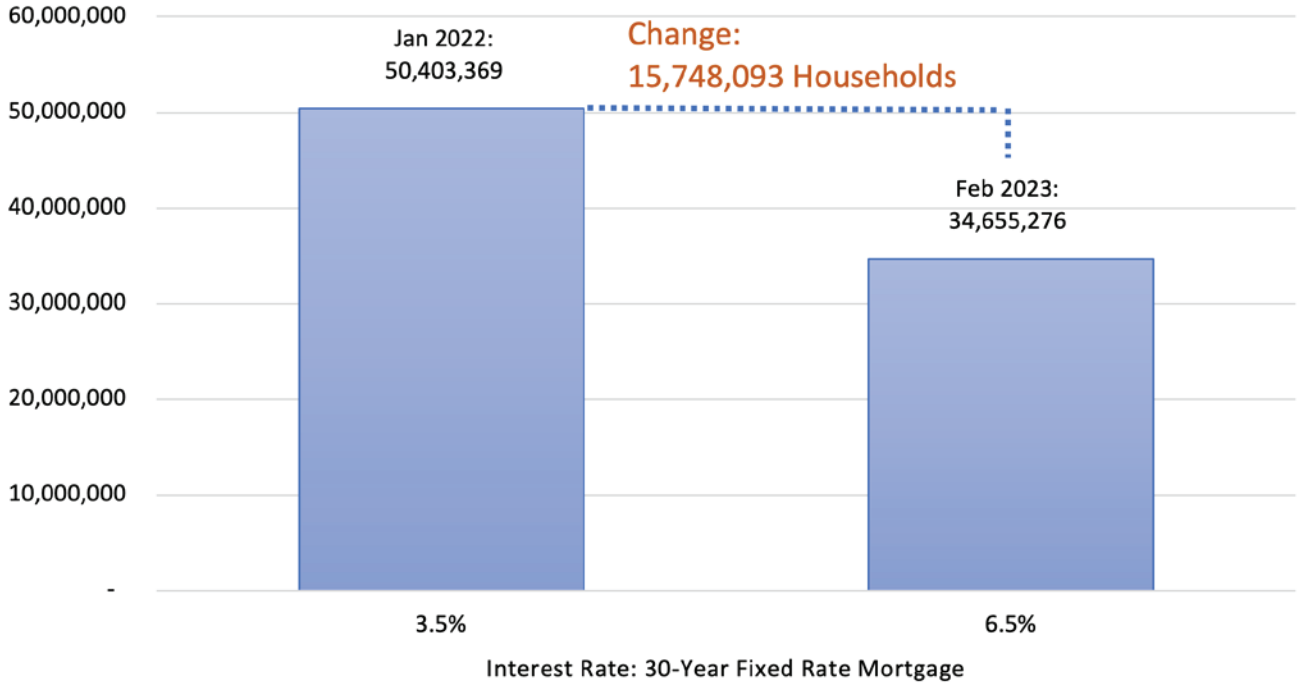


Housing Supply and Demand

INCREASING MORTGAGE RATES

As interest rates continue to climb, an increasing share of U.S. households are unable to afford a median-priced home. The recent runup in mortgage rates has effectively priced out an additional 16 million households (NAHB, 2023).

US HOUSEHOLDS THAT CAN AFFORD A MEDIAN-PRICED HOME

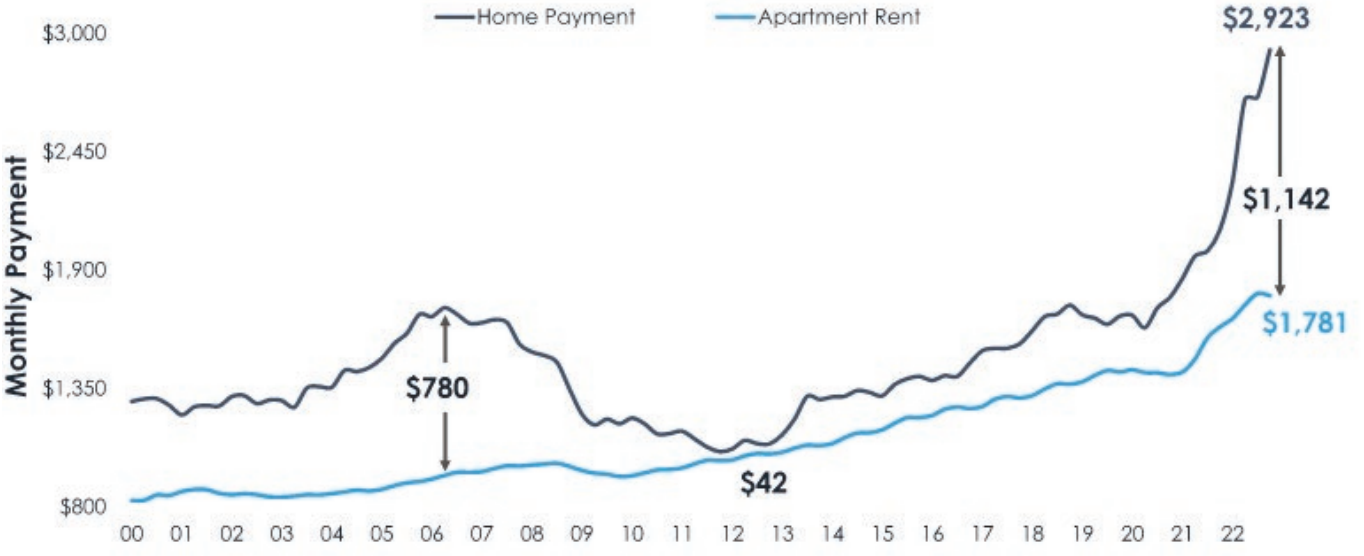


Housing Supply and Demand

AFFORDABILITY

The affordability gap measuring the cost difference between owning and renting has never been higher. It is now over $1,100 more expensive per month to own a single-family home than to rent an apartment (IPA, 2023).

AFFORDABILITY GAP BETWEEN AVERAGE MORTGAGE PAYMENT AND AVERAGE MONTHLY RENT HAS GROWN



Mortgage payments based on quarterly median home price for a 30-year fixed rate mortgage, 90% LTV, taxes, insurance, and PMI
Sources: IPA Research Services, RealPage, Inc., Freddie Mac, National Association of Realtors

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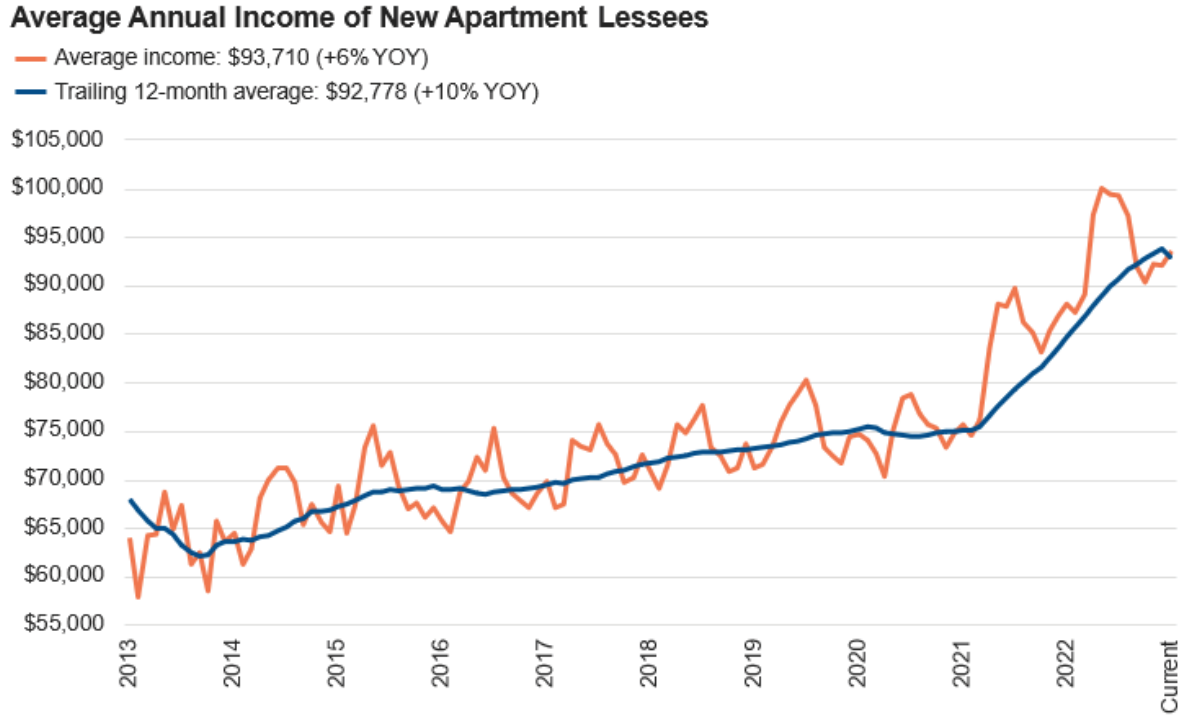
Housing Supply and Demand

AFFORDABILITY

The income profile of new U. S. renters continues to increase with annual income now more than $93,000, representing a 6% annual increase and nearly 25% higher than in 2021 (JBREC, 2023). Rent-to-income ratios (renter's percentage of income paid on housing) for Thompson Thrift stabilized properties remain healthy at 23%, showing that our renters have capacity for increased rent growth.

NEW U.S. APARTMENT RENTER INCOMES HAVE JUMPED SHARPLY IN THE POST-PANDEMIC ERA



Sources: RealPage, Inc.; John Burns Real Estate Consulting, LLC (Data: Jan-23, Pub: Mar-23)

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Data includes all asset classes

Property Values and Cap Rates

APARTMENT CAP RATES

Apartment cap rates have increased from lows in 2021 and early 2022, remaining below the long-term average (Marcus & Millichap, 2023). Despite the drop from peak pricing, values remain attractive and offer good returns on cost. Apartment assets offer competitive yields for buyers compared to alternatives worldwide.

U.S. APARTMENT CAP RATE YIELD SPREAD TIGHTENING; AVERAGE CAP RATE VS. 10-YEAR TREASURY



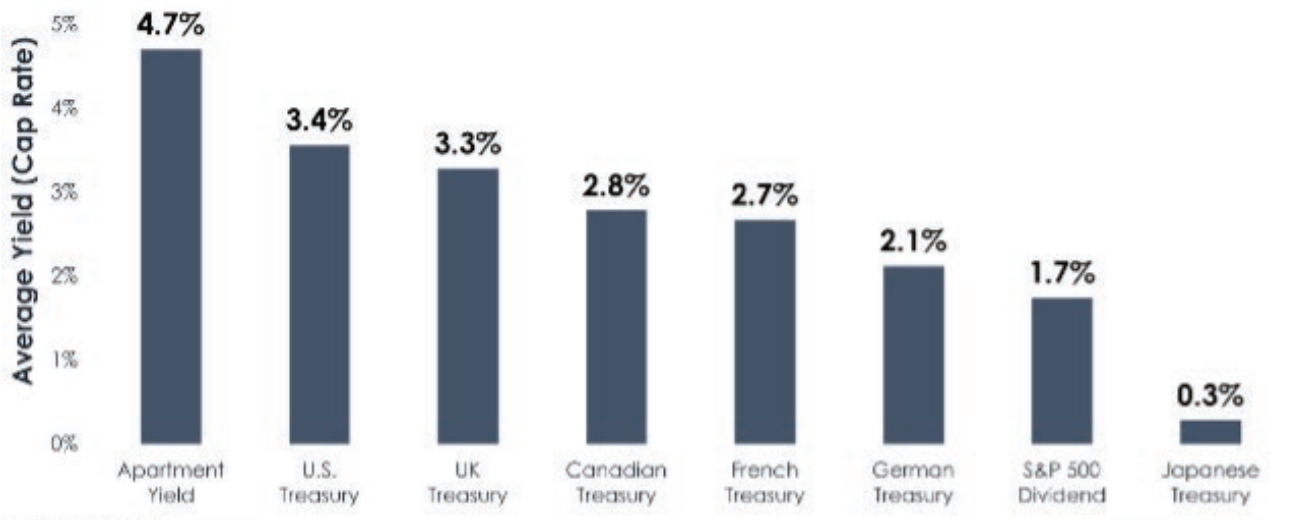
* Through December 2022
Includes sales $2.5 million and greater from RCA's Hedonic series
Sources: Marcus & Millichap Research Services, Real Capital Analytics, Federal Reserve

Marcus & Millichap

Property Values and Cap Rates

APARTMENT CAP RATES

APARTMENTS OFFER COMPETITIVE YIELDS COMPARED TO ALTERNATIVES



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