MULTIFAMILY PROPERTY INVESTMENT
KEYS TO HGI'S CORE SEGMENT: A WHITE PAPER

CONTENTS

HARBOR GROUP INTERNATIONAL

Real estate in the United States is typically divided into several classes: Multifamily, office, retail, industrial, mixed-use, hotels, storage and land.

1. WHAT IS MULTIFAMILY?

Moody's Analytics defines multifamily as "a classification of housing where multiple separate housing units for residential inhabitants are contained within one building or several buildings within one complex."

According to that definition, there can be a wide variety of properties under the multifamily umbrella, from a small duplex house to an entire high-rise apartment tower. This variety also makes the multifamily sector a viable investment vehicle for many different types of investors.

One of the more common property types in the multifamily sector is the garden-style apartment community. These properties provide the most flexibility to people looking for housing at a price that matches their income in a location convenient to their needs.

Garden-style apartment communities consist of one or more buildings containing multiple apartment units. Size varies significantly, with some properties containing less than 50 units and some containing more than 2,000.


Garden Style

Garden-style apartment properties often feature wood-frame construciton with a concrete foundation, as well as breezeways with concrete stairs and wood landings.


High-Rise

These properties often provide residents with conveniences including parking, recreation, and other amenities. They can be found in nearly any market in the United States and tailored to nearly any income level.

Often found in urban locations, multifamily **high-rise properties** are also common. These properties consist of one or more towers with multiple units. These are often associated with luxury communities, with penthouse units commanding the highest rents.

Mid-rise properties have attributes of high-rise and garden-style apartment communities, with most of the units contained in a single building but more outdoor amenity space than a high-rise. Mid-rise properties are usually 4-12 stories, but that can vary depending on the market. Construction style for mid-rise involves poured reinforced concrete footings with concrete slab at grade.


Mid-Rise

Mixed-use properties can be garden-style mid-rise or high-rise. These properties contain housing units and additional components, often retail or office, located on the same property.

2. RESIDENT TYPES

Multifamily properties cater to residents from a variety of income levels and backgrounds.

"Traditional" multifamily properties are open to any qualified residents who can afford the rental rates. These are the most common type of multifamily properties and they provide the most flexibility when it comes to setting rental rates and getting a good return on a "value add" capital improvement plan.

Other classes of multifamily properties are specifically geared towards residents who may require financial or physical assistance.

Student housing, located near a college or university, is housing created to meet the requirements of people attending the nearby school. These properties often have rental restrictions based on the requirements of the school or government.

Senior housing is limited to people who meet an age requirement. In the United States, HUD (The U.S. Department of Housing and Urban Development), sets requirements for housing for people aged 55 or older. These properties are available only to seniors and many meet HUD's affordability and accessibility requirements.

Affordable housing includes any property that targets low income residents. This can be further broken down into affordable properties that are simply inexpensive to maintain and rent, as well as "subsidized" properties where renters receive assistance, usually from a government program, to maintain an affordable rental rate.

3. MULTIFAMILY CLASSES

Harbor Group International, LLC ("HGI") is one of the top owners and managers of multifamily real estate in the United States, consistently ranking among NMHC's top 50 owners in the country.

Multifamily real estate in the United States spans a wide variety of property types, markets and geographies, where the key to success lies in research and discipline.

Multifamily apartment communities are a core asset class for HGI, including garden style, high rise apartment buildings, mid-rise and mixed-use properties.

Like all real estate types, multifamily properties are often referred to as Class A, B or C.

Class A properties generally benefit from a prime location and are often recently built or newly developed. These properties also feature plenty of high-end amenities for residents.

Class B properties may be older, in a less desirable location or less amenity-rich, but still provide opportunities for making improvements to be more competitive.

Class C properties often cater to residents in need of affordable housing. They lack comprehensive amenities and feature more basic finishes inside and out. Some are much older properties in need of maintenance. They may be poorly located or poorly managed. These properties may still provide opportunities for improvement to the opportunistic investor.

Classes may be further broken down to + or - subsections depending on the properties position among its competitors.

4. THE MULTIFAMILY UNIVERSE

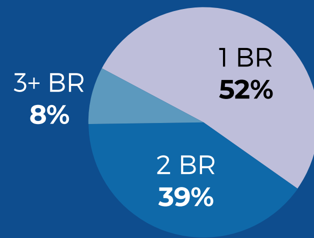
Multifamily is a sector that continues to grow. Housing is a basic need required by everyone, and with population increases across the U.S., the sector must grow in order to meet that demand. According to the National Multifamily Housing Council (NMHC), there are 23 million apartment units in the U.S.

More than 30% of these apartment units were built in the year 2000 or later, again showing the need to continue to add supply to meet increased demand. More recently, increased building costs and restrictions on development have made it more difficult to build new properties. These restrictions make existing multifamily real estate more valuable.

Multifamily properties are desireable to investors as they can be improved upon, and the lease terms of residents are short comparable to other sectors, allowing ownership to benefit from increases in market rents as residents renew or new residents lease apartments at the property.

U.S. APARTMENTS BREAKDOWN

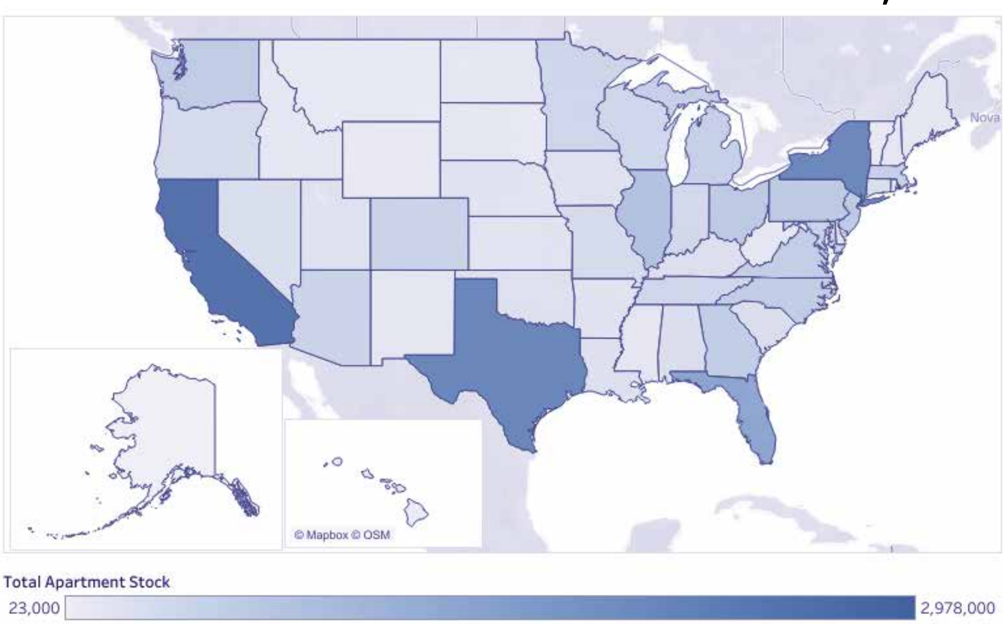
23 million
apartment units in the U.S.



Apartment Inventory by number of bedrooms

Source: NMHC tabulations of 2022 American Community Survey microdata, US Census Bureau. Updated 11/2023.

STATE DISTRIBUTION OF APARTMENT STOCK, 2022



Source: NMHC tabulations of 2022 American Community Survey microdata, US Census Bureau. Updated 11/2023. An apartment is defined as a unit occupied by renters, a vacant unit, or a rented unit not yet occupied, all located in a structure with 5 or more units.

5. MULTIFAMILY KEY STRATEGIES

When it comes to multifamily real estate investment, HGI focuses on a few primary strategies that bring the greatest opportunity for success given market conditions. Each one depends on backup from market research and extensive due diligence. Here is an overview of HGI's key strategies.

1. Newly Developed

A newly developed or recently built multifamily property, given the right market conditions, can provide a unique opportunity for success in a competitive market. New properties are highly desirable in markets where housing supply is low and there are barriers to developers trying to add more units to the market.

New property developers also face unique challenges as a property nears completion. Development loans often mature on a short timeline, leaving a narrow window to lease the newly built property.

Owners like HGI are uniquely positioned to acquire the new property from the developer with more favorable financing, giving adequate time to lease the property to residents who are qualified to pay market rental rates.

2. Value Add

The value-add strategy can be distilled down to the basic principal of "Buy it, fix it, sell it."

Value-add investment strategies are in reality much more complicated. Class A, B and C properties can provide opportunities to add value through renovations, new amenities and better management. Again, this strategy requires a significant amount of market research and due diligence.

If a property is achieving rents below market rates and there is an opportunity to improve upon it in order to increase revenue, a value-add opportunity can improve both the physical asset and income metrics.

3. Portfolio

Few real estate investors have the capability to "buy wholesale" when it comes to entire portfolios of multifamily properties but the advantages are many.

Properties are often sold as portfolios because the previous ownership tied them together with existing debt or is looking to sell assets in a group for a reason such as exiting a market.

Economies of scale create opportunity in any line of business and multifamily real estate is no different. The challenge when it comes to a portfolio acquisition is to view each property with an individual business plan and execute on each property with the ultimate goal of "buy wholesale, sell retail."

When HGI acquires a portfolio, each property is looked at as an individual investment with its own business plan that must be realized to achieve projected results.

4. Credit Investments

Often, multifamily investors are able to participate in the upside of an investment without assuming the risk of ownership.

> "If a property is achieving rents below market rates and there is an opportunity to improve upon it in order to increase revenue, a value-add opportunity can improve both the physical asset and market income metrics."

5. MULTIFAMILY KEY STRATEGIES

The same market research and due diligence process HGI uses when acquiring properties also applies when HGI takes a credit position in a property being acquired by a qualified sponsor.

Through a senior mortgage, preferred equity investment, a mezzanine loan or a bond purchase, HGI is able to reap the benefits of another owner's investment in a position that allows the company to take control if the sponsor is unable to meet its obligations.

Why Focus on Multifamily?

Multifamily real estate fills a need that will never go away. People need a place to live. Populations grow.

Housing is a fundamental component of human life and rental housing provides the most options for people at various stages in life while giving them the flexibility to move more quickly from one location to another.

Historically, multifamily investment markets have grown, especially among Class A residents, as successful people look for housing with proximity to an urban environment, transportation access, and a growing suite of amenities that more resemble a resort than a typical apartment home.

Opportunities may be found across all income and market types. As an investor, it's important to be discerning. HGI enters markets where thorough research has been done. Each property goes through an exhaustive screening process.

Risk always exists in any investment, and multifamily real estate does bring with it a share of risks, which may include: Changes to interest rates, increased costs, taxes, market job loss, overbuilding in the area, and more. An experienced owner and operator works to anticipate and plan for multiple situations or major changes to the market.

Furthermore, these investments lack liquidity. A multi-year investment term is typical and must be anticipated.

Risk aside, multifamily has proven to be a stable asset class across multiple economic cycles and in various markets.

6. MULTIFAMILY TODAY

The multifamily market faces a number of pressures today that create opportunities for savvy investors.

A key factor is the historically high cost of homeownership. The price to own a home has been driven up by increased construction costs. Additionally, higher interest rates mean the monthly cost of ownership is now much higher than the cost of renting - even with today's increased rental rates.

While interest rates have shown a slight drop recently, there is still a lack of supply in many markets across the U.S., and fewer permits have been granted to developers looking to fill that gap.

Millennials and Gen Z are leading the charge in the renter nation, with 52% of Gen Z stating they prefer renting to buying a home, compared to 40% of millennials. (Source: National Multifamily Housing Council)

While multifamily fundamentals appear to indicate a stable asset class, many owners of these properties are facing pressure due to changes in the capital markets.

Owners who financed acquisitions using floating rate debt are now facing significant cost increases to their monthly debt service and many of these loans mature in the near term.

These impending loan maturities create opportunities for investors like HGI to acquire stable multifamily properties with the potential for attractive returns.

DECADES OF MULTIFAMILY EXPERIENCE

Harbor Group International has a multi-decade track record of success as an owner and operator of multifamily investment real estate throughout the United States, starting from its origins in 1985 as a property management company.

Since inception, HGI affiliates have acquired, operated and realized multifamily investments in markets across the entire United States covering all classes of multifamily investment real estate.

HGI has a track record of success stretching across multiple market cycles, weathering the dot-com bubble burst of 2000, the financial crises of 2007-2008 and 2015 and the recent pandemic.

Following the Great Financial Crisis of 2007-2008, HGI concluded that fundamentals in the multifamily sector were likely to remain strong for the foreseeable future and that the sector would offer the best risk adjusted real estate returns. As a result, HGI allocated 80% or more of its capital to multifamily investments, either direct owned or credit.

HGI continues to actively invest in multifamily, leveraging its experience in the sector along with proprietary market data from its extensive credit investments to identify markets and trends that provide the best possible risk adjusted returns to investors.

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HARBOR GROUP INTERNATIONAL, LLC

HGI and its affiliates control an investment portfolio of ~$19 billion[1] including 5 million square feet of commercial space throughout the United States and the United Kingdom and 56,000 apartment units[2] in the United States. In addition to its corporate headquarters in Norfolk, Virginia, HGI maintains offices in New York City, Baltimore, Los Angeles, and Tel Aviv.

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[1]As of 3/31/2024. AUM represents the total capitalized value of underlying assets, which includes direct and indirect real estate and real estate related investments, and the AUM of HGI's affiliate, HGI Capital Management, LLC.
[2]Includes multifamily direct and preferred equity investments.