2020 Annual Report Letter: Discipline

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The Greek myth of Icarus and Daedalus is the ultimate lesson in moderation. CWS prides itself in having the discipline to fly at a height that is just right. In real estate, this means making sure that we have the resources available to reinvest in our assets, people, and systems over the long term so those assets can continue to perform at their best.

The chart that follows outlines the annual financial performance for our same store portfolio of stabilized assets which we owned continuously starting in 2018, which is a total of 83 assets and 23,230 units. While you as investors are invested in individual assets or in funds that are invested in small pools of assets, many characteristics of our individual assets are reflected in our overall portfolio. A couple of highlights:

- Total revenues were essentially flat for 2020 relative to 2019. In the face of COVID, we are pleased with this outcome. While new leases were down slightly from the leases they replaced, our renewals made up for this drop.
- Operating Expenses increased just over 3%. We experienced considerable expense savings in Marketing (reduced locators) and also G&A (travel, training, and renegotiating an extensive software operating system package with our provider). We did have significant expense increases in insurance premiums as insurance companies are reacting to the poor loss history that they have experienced in multifamily assets over the last number of years. Professional services also were up considerably due in part to increased security spending at our properties.
- As a result of the above, Net Operating Income was down a little over 2%.
- On the positive side, due to our variable-rate loan strategy, our interest payments were down over 37%, a savings of over $39 million in 2020 relative to 2019.
- Along with some COVID related postponements of planned capital expenditures, these interest savings resulted in an increase in Operating Cash Flow to $96.5 million in 2020, which was a 62% increase over the previous year.

* Figures shown in dollars million	2018	2019	'19 v '18 % Change	2020	'20 v '19 % Change
Net Rental Income	347.3	364.2	4.8%	365.9	0.5%
Other Income	39.8	38.2	-4.1%	37.3	-2.2%
Total Revenues	387.1	402.3	3.9%	403.2	0.2%
Salaries	34.1	35.7	-4.5%	37.4	-4.7%
Marketing/Advertising	7.4	6.2	15.6%	5.4	13.1%
Turnover	6.1	6.1	0.3%	6.0	0.9%
Repair and Maintenance	5.0	5.1	-1.9%	5.1	0.1%
Professional Services	8.6	8.8	-1.7%	9.8	-11.7%
General & Administrative	6.3	6.9	-9.9%	5.1	25.3%
Utilities	23.6	24.5	-3.7%	25.1	-2.7%
Taxes	71.3	69.6	2.4%	72.6	-4.4%
Insurance	5.4	5.9	-9.6%	7.4	-24.8%
Mgmt Fees	12.3	12.8	-4.3%	13.1	-2.2%
Retail Expenses	0.8	0.8	3.8%	0.8	-1.4%
Total Expenses	180.8	182.3	-0.8%	187.9	-3.1%
Net Operating Income	206.3	220.0	6.7%	215.3	-2.1%
Interest Payments	98.5	103.9	-5.5%	64.8	37.6%
Principal Amortization	10.4	9.5	8.8%	9.0	5.4%
Other Expenses	9.3	10.1	-8.5%	12.7	-25.0%
Capital Expenditures	36.7	37.0	-0.8%	32.4	12.5%
Operating Cash Flow	51.4	59.6	15.9%	96.5	62.0%

SAME STORE PORTFOLIO

Our results in 2020 demonstrate our discipline in several ways:

First, over the last several years we maintained our variable-rate strategy in the face of rising interest rates, rates that have now cratered to our benefit in the wake of COVID, and which are predicted to stay very low for at least through 2023 based on Federal Reserve statements. We correctly assessed that the risks of an economic downturn in a highly indebted and aging world would create a greater probability of rates dropping and staying lower versus rising and remaining there as a result of inflation. We had the discipline to stick with our strategy, even as rates were climbing higher in 2017 and 2018 and stayed there through much of 2019. By believing in our hypothesis and keeping a strong backbone, we were able to weather a couple of years of higher interest costs to now be basking in the sun of lower interest rates for at least the next few years. And unlike Icarus, our wings are still very much intact.

Secondly, we are exercising discipline by not converting this increased cash flow instantly into higher distributions. While we have selectively increased distributions at some assets and plan to increase it at others this year, our goal is to be able to consistently produce distributions and grow them <u>over the long term</u>. As a result, we are reinvesting a significant portion of the increased Operating Cash Flow into our assets. Our plan is to spend over $55.2 million in capital expenditures next year, a significant increase over the $32.4 million we spent this year. Our ability to prudently maintain and improve our asset base during these times will enable our assets to better compete and to continue to produce healthy cash flows over the long term. Furthermore, we are taking this opportunity to judiciously build up working capital balances at certain assets that had been depleted over the last several years, due in part to rising interest rates. This strategy should help us maintain our current level of distributions in the event of a further economic downturn or perhaps an unexpected hailstorm, which now requires payment of a significant deductible before insurance proceeds kick in to repair the roofs and siding.

CWS will maintain our discipline in picking the right investment and financing strategies coupled with prudent capital spending that will benefit our investors over the long term. We will continue to work hard and produce results that earn your trust and confidence.