

INITIATING MOTION: MARKET UPDATE AND LOOKING AHEAD

By Steve Sherwood
Founding Partner & Chairman

Dear Valued Partners,

As we reflect on our annual meeting two years ago, we want to revisit a forecast we shared at that time. Based on the supply then under construction and the historical demand patterns across our markets, we anticipated that a recovery would begin to take shape in 2025. While the ultimate direction of that outlook remains intact, the timing has proven more extended than our models suggested.

The absorption patterns we relied on—patterns that held consistently through prior cycles—did not repeat themselves in this cycle. As a result, the recovery is unfolding more slowly than expected. Based on current conditions, 2026 now appears to be a more realistic timeframe for improvement, though each market will follow its own distinct path. The first two quarters of 2026 should provide meaningful insight into the pace and strength of recovery across our portfolio markets.

Our confidence in the longer-term recovery remains strong. Demand fundamentals in the Sunbelt continue to be supported by job growth and population inflows, while the economics of new apartment development have become increasingly challenging. In many of our markets, rents would need to increase by more than 25% before new development would justify the time, cost, and risk required to assemble land, entitle sites, and secure financing. Not surprisingly, we are seeing a significant decline in new permits across all of our markets. While some markets—Austin, for example—continue to issue permits at a higher rate than others, markets such as San Antonio and Denver have experienced a much sharper pullback.

At the same time, the cost of homeownership relative to renting is at its highest level in more than 40 years. In certain markets, owning a home is now as much as 50% more expensive than renting. With median home prices near \$410,000, the income required to qualify for a typical mortgage approaches \$117,000—well beyond the reach of many young professionals.

As a result, renters are renting longer. Twenty years ago, the typical renter aged out in their early 30s; today that range extends into the late 30s. This demographic shift has a meaningful and lasting impact on apartment demand and reinforces our conviction in the long-term fundamentals of the asset class.

New apartment deliveries vary widely by market. Austin, Raleigh, and Nashville currently have elevated levels of properties in the lease-up phase, while other markets such as San Antonio and Denver are experiencing more limited new supply. Importantly, permit activity is declining across all markets, though not uniformly. This environment is creating opportunities to acquire well-located assets at prices below replacement cost—particularly in markets where new development is no longer economically feasible.

Identifying these opportunities requires experience, discipline, and a deep understanding of operating and construction costs. Our team applies its operating expertise and market

knowledge to recognize properties with the characteristics that position them to outperform their submarkets over time. This is where we believe our platform and long-standing operating focus should provide a meaningful advantage.

Periods like this are never easy, but they are often the most rewarding for patient and disciplined operators. Historically, our ability to remain patient and selective during downturns has allowed us to acquire a small number of high-quality opportunities that drive long-term performance. While competition remains strong and there are many capable operators in the market, our experience gives us confidence that patience and focus will once again serve us well in this cycle.

We deeply appreciate the trust you have placed in us—many of you for more than five decades—and remain committed to navigating the current environment with the same discipline and long-term perspective that has guided our firm throughout its 56-year history.