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Zacks Small-Cap Research

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Tom Kerr
312-265-9417
tkerr@zacks.com

scr.zacks.com
10 S. Riverside Plaza, Chicago, IL 60606

Harbor Custom Development (HCDI-NASDAQ)

UPDATE: Diversified and pioneering real estate development company reports 3rd quarter earnings which were below expectations due to a difficult real estate market and project sales timing.

Utilizing a DCF valuation process containing conservative estimates combined with other valuation methodologies, we believe HCDI could be worth $2.40 per share. An economic or real estate downturn may lower this value.

Current Price (11/17/22)	$0.67
Valuation	**$2.40**

OUTLOOK

Harbor Custom Development is a unique and diversified real estate development company involved in all aspects of the land development cycle including land acquisition, entitlements, permitting, development, construction of project infrastructure, single and multi-family vertical construction, marketing, sales, and management of various residential projects. The company operates in high growth market areas which currently includes locations in Washington, California, and Texas. The company went public in 2020 and has adequate liquidity and access to the capital markets at this time.

SUMMARY DATA

52-Week High	**$3.80**
52-Week Low	**$0.63**
One-Year Return (%)	**-67.8**
Beta	**0.53**
Average Daily Volume (sh)	**63,417**
Shares Outstanding (mil)	**14.3**
Market Capitalization ($mil)	**$10.0**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**13**
Insider Ownership (%)	**21**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**N/A**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2022 Estimate	**14.0**
P/E using 2023 Estimate	**9.3**
Zacks Rank	**N/A**

Risk Level	**Above Avg.**
Type of Stock	**Small-Growth**
Industry	**Real Estate**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2020					$50.4A
2021	$13.8 A	$14.1 A	$18.0 A	$26.3 A	$72.4A
2022	$28.6 A	$10.3 A	$11.7 A	$12.6 E	$63.2E
2023	$95.2 E	$68.0 E	$51.7 E	$57.1 E	$271.9E

EPS / Loss Per Share

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2020					-0.84 A
2021	-$0.12 A	$0.06 A	$0.17 A	$0.16 A	$0.41 A
2022	-$0.03 A	-$0.46 A	-$0.37 A	-$0.17 E	-$1.02 E
2023	$0.62 E	$0.33 E	$0.20 E	$0.19 E	$1.34 E

Quarterly revenues may not equal annual revenues due to rounding. Quarterly EPS may not equal annual EPS due to rounding, dilution or intangibles.

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WHAT'S NEW

Harbor Custom Development Inc. (NASDAQ:HCDI) reported 3rd quarter results and updated investors on the current state of the real estate market.

Financial Review

Sales for the 3rd quarter of 2022 decreased by 34.8% to $11.7 million, compared to sales of $18.0 million for the 3rd quarter of 2021. This decrease was largely due to a lower level of entitled land sales of $7.0 million, partially offset by an increase in home sales of $0.8 million and fee build revenues of $0.8 million.

Gross profit for quarter decreased to $0.4 million compared to $7.1 million in the prior year period. Gross margin decreased to 3.7% compared to 39.7% for the 3rd quarter of 2021. The $(6.7) million decrease in gross profit and (35.9)% decrease in gross margin were primarily due to the non-recurrence of higher margin entitled land sales in 2022 and a decrease in fee build gross profit due to significant cost overruns. The entitled land sales in the 3rd quarter of 2021 provided $5.9 million gross profit dollars at a gross margin of 57.0% that did not recur in the 3rd quarter of 2022.

Operating expenses during the quarter were $4.5 million compared to $3.3 million for the 3rd quarter of 2021. The increase in operating expenses was primarily due to $0.9 million of bad debt expense related to the sale of Winding Lane's developed lots in March 2022. Additionally, there was $0.5 million in pre-acquisition due diligence costs associated with the cancelation of the Westry Village project. These unusual project charges were partially offset by a reduction in 2022 incentive bonus compensation of $0.6 million. In addition, the company saw less significant increases in payroll expenses, marketing and advertising, right-of-use expense for a new corporate office, and depreciation expense.

EBITDA for the quarter decreased to a loss of ($3.2) million compared to positive EBITDA of $4.3 million in the prior year period. Adjusted EBITDA, which excludes the impact of stock compensation and other non-recurring items, decreased to a loss of ($3.1) million compared to adjusted EBITDA of $4.5 million for the third quarter of 2021.

The company's liquidity position remains stable with unrestricted cash of $13.7 million and $0.2 million available on the line of credit. Stockholders equity was $88.1 million, or $2.40 per share. Based on construction related loans of $92.2 million and total real estate values of $179.9 million, the company real estate leverage ratio was 51.2%.

Business Update & Recent News

Based on the 3rd quarter financial results, the company failed to meet a financial covenant on its senior secured revolving credit facility with BankUnited. The covenant requires the company to maintain an interest coverage ratio of 2.5x and based on the 3rd quarter financial results, that ratio stands at 1.4x. The company is working with the bank on this issue and there is no indication at this time the bank will call the loan.

On October 20th, the company announced it has contracted to sell 56.6 acres of land in Punta Gorda, Florida for $7,250,000. The property transaction is scheduled to close on or before December 20, 2022. Harbor Custom Development chief operating officer Jeff Habersetzer stated, *"The potential sale of our Punta Gorda property reinforces our stated business plan to monetize our assets at the most opportune time in the development cycle by taking into account current market dynamics and our planned capital allocation strategy."*

On October 31st, the company announced it has executed a letter of intent for the acquisition of 15 acres of land in Stanwood, Washington for $4,590,000. Located 53 miles north of Seattle in Snohomish County, the Stanwood site is suited for garden-style apartments. The property is located with easy access to the I-5 corridor, retail services, and approximately 20 minutes from the Cascade Industrial Center. Commencement of construction on the multi-family project is estimated to begin in the first quarter of 2024 following the completion of entitlements.

The company reiterated its strategic focus on developing and marketing multi-family housing projects which began in 2021. Multi-family properties have historically fared well in economic downturns and in addition, multi-family properties are usually a more affordable alternative for housing needs than purchasing a single-family home. This is more pronounced now due to high home prices, a slower economy, higher mortgage rates and low levels of single-family housing inventory in the company geographic markets. Multi-family housing projects comprise approximately 60% of real estate assets as of September 30, 2022

During the 2nd quarter, Harbor announced the listing of six multi-family properties in Western Washington. Those projects include Pacific Ridge, Mills Crossing, Belfair View, Wyndstone, Meadowscape (formally known as Tanglewilde) and Bridgeview Trails. The company's initial target was to have Mills Crossing, Pacific Ridge, Wyndstone and Belfair Phase 1 sold during the fourth quarter of 2022, but the closing of most of these projects will likely occur in 2023.

As of August 2022, the company announced it was in the process of developing additional multi-family projects which could total approximately 283 units. These will be located in the Puget Sound region of Washington in the cities of Silverdale, Port Orchard, Poulsbo, Bremerton, Tacoma and Edmonds. These projects are in various stages of the permitting and entitlement and should be completed during the 2024 calendar year.

Revised Guidance

Due to the items mentioned above, Harbor revised its annual 2022 guidance. Revenues for the year are now expected to be between $61 million and $65 million compared to previous guidance of $80 million to $90 million in revenues. Adjusted EBITDA is expected to be a loss of ($5.0) to ($7.0) million.

CEO Sterling Griffin stated, *"While our third quarter results were impacted by lower sales and higher operating expenses, we continued to make progress on our strategic initiatives to support future growth. I am pleased with the development we made in our transition to focus on multi-family projects and believe this strategy will enable us to drive additional value for our shareholders. Today's market environment remains unstable. The increases in interest rates to combat inflation, combined with affordability challenges and lower buyer sentiment, have weakened demand, particularly for land, lots, and single-family homes. These dynamics, along with their resultant uncertainty and inability to obtain cost-effective financing, as well as delays in the closing of certain multi-family projects and home sales, have caused us to revise our financial guidance downwards for the full year 2022. We continue to believe our unique portfolio positions us to deliver future financial growth through our multi-family offerings in 2023 and remain confident that the team we have in place will enable us to manage the changing market conditions and position us for long-term success."*

Estimate Change

We are adjusting our revenue and earnings numbers for the 4th quarter of 2022 and full year 2022 based on the year-to-date operating results, the current housing market environment and the timing of multi-family project closings. Our revenue estimate for 2022 is lowered to $63.2 million and EPS is lowered to ($1.02). Adjusted EBITDA is now estimated to be a loss of ($5.4) million.

2023 revenue estimates have been raised to $271.9 million as we expect many of multi-family projects currently listed for sale to close during the year. Based on this level of sales, EBITDA is estimated to be approximately $38.6 million and we expect annual EPS of $1.34. These estimates assume a normalized housing market, receding inflationary pressures, and the absence of any unusual cost overruns.

Valuation

Our primary valuation methodology is now focused on Price/Book value. Currently, HCDI is selling at 31.0% of stockholders equity which uses total common shares outstanding of 36.9 million. On a more conservative basis utilizing fully diluted shares which includes warrants and converted preferred stock and totals 55.0 million shares (as of 9/30/22), the stock is trading at approximately 46.0% of book value. The home builder industry Price/Book ratio has declined year-to-date due to higher interest rates and recessionary fears, yet still trades at an average Price/Book value of approximately 1.0x currently. We lower our valuation target to $2.40 as we believe that once steady profitability is achieved in 2023, the company can trade close to book value per share.

We believe even with volatile earnings that may be associated with real estate development companies, Harbor can continue to add earnings to shareholders equity and increase book value over time.

KEY POINTS



Source: HCDI Investor Presentation

- Founded in 2014, Harbor Custom Development Inc. (HCDI) is a real estate developer that is active in all phases of the land-to-home development cycle. The company's uncommon business model provides flexibility for the monetization of land and properties at various stages of development.

- Harbor acquires land, entitles and permits the property, develops the land with horizonal infrastructure, constructs home, condos, or apartment buildings, then monetizes the real estate assets at different stages to take advantage of prevailing market conditions.

- The company builds superior homes built with quality materials and exceptional craftsmanship, carefully designed floor plans, and are located with a 20-to-60 minute commute from a major metropolitan area. The homes are designed for energy-efficiency which reduces the homeowner's environmental impact and energy costs.

- The business model is flexible in that the company facilitates partnerships with regional companies that specialize in their local markets, including residential builders, general contractors, and land developers.

- Harbor is currently operating in three high growth markets in Washington, Texas, and California and seeking opportunities in other high growth markets around the country.

- The company is led by an experienced management team with the CEO and founder having 37 years of experience in land acquisition and development, residential construction, and syndication of apartment properties.

- The company has adequate liquidity as of the end of the 3rd quarter ending September 2022 with $13.7 million in unrestricted cash and equivalents and $0.2 million available on its revolving line of credit.

OVERVIEW

Harbor Custom Development is a unique and diversified real estate development company involved in all aspects of the land development cycle including land acquisition, entitlements, permitting, development, construction of project infrastructure, single and multi-family vertical construction, marketing, sales, and management of various residential projects. The company operates in high growth market areas which currently includes locations in Washington, California, and Texas. As a land developer and builder of single-family homes, luxury homes, townhomes, condominiums and apartments, the core business strategy is to acquire and develop land strategically based on an understanding of population growth patterns, entitlement restrictions, land use evaluation, infrastructure development, and geo-economic forces.

The company strives to acquire land with scenic views to develop and sell residential lots, new home communities, townhomes and multi-story condominium or apartment properties within a 20-to-60 minute commute of some of the country's fastest-growing metro employment corridors such as Austin, Texas or Seattle, Washington.

The company is believed to be the first national land developer and home builder accepting payment in the form of cryptocurrency for their properties. This offering has been active since January 2022 and is done in partnership with BitPay. Harbor takes no volatility risk with regard to accepting cryptocurrency due to the arrangement and processes with BitPay.

Harbor's portfolio of land, lots, home plans, and finishing options, coupled with a historic low inventory of residential and multi-family housing in their principal geographic areas of operation provides an opportunity to increase revenue and overall market share. In addition to single-family residential projects, the company plans to build and sell townhomes, condominiums, and apartments and anticipate commencement of land development and construction on six multi-family sites in Washington.

The company's infrastructure development division constructs a diverse range of residential communities and improved lots in a cost-effective manner. Harbor owns and leases heavy equipment which is used to build and develop residential subdivisions and multi-family communities. The equipment is primarily used for land clearing, site development, public and private road improvements, installation of wet utilities such as sewer and, water sewer lines in addition to construction of dry utility lines for power, gas, telephone, and cable service providers. The company typically acts as a general contractor to construct single-family homes, townhomes, condominiums, and apartments utilizing a base of employees in conjunction with third-party subcontractors.

STRATEGY

The company's operating and long-term strategy is driven by a number of factors and strategic goals.

The company's expertise allows for a diversified product strategy that enables them to better serve a wide range of buyers, adapt quickly to changing market conditions, and optimize performance and returns while strategically reducing overall portfolio risk. The company has the resources and skills to build to the surrounding communities' needs, including single family homes, townhomes, condominiums, and apartments. This flexible business model allows for the targeting of a wide and diverse range of customers including those looking at lower income housing options through condominiums and apartments, to those seeking to buy high-end luxury single-family homes.

The company stated goal is to provide a "positive and memorable" experience to homeowners and residents. Homes are built with quality materials and advanced craftsmanship, thoughtfully designed floor

plans, and located with a 20-to-60 minute commute from major metropolitan areas. The company engineers the homes to be energy-efficient which reduces the homeowner's environmental impact and overall energy costs. The company's competitive advantage in the selling process focuses on the home's features, design, and premium locations with scenic views. New homebuyers' needs are met across multiple communities and price points by maintaining a substantial inventory of ready-to-build lots and designer home plans.

The significant appreciation in rental rates over the past year, combined with moderate capitalization rates and low inventory of rental housings in the company's target markets, have created a substantial opportunity to expand the company's product portfolio within the multi-family vertical space. A product agnostic building model provides the flexibility to accommodate the current rapidly changing market conditions.

The company is very focused on cost control through a disciplined planning process. Detailed budgets are prepared for all cost categories. Budgets are closely monitored throughout the building process as budgets are revisited and update on an ongoing basis. Many development components are provided by subcontractors and significant efforts are made to assure that scopes of work are complete and satisfactory. Contract variances and change orders are closely scrutinized for appropriateness.

At the sale and closing of each home in a project, the estimated and final margins are compared and variances are identified and investigated to better control future project costs. The company believes their disciplined process of setting realistic budgets and expectations, monitoring, and evaluating them and making any necessary adjustments to correct deviations going forward enables us to prudently control costs.

The business model is flexible and facilitates partnering with companies that specialize in their local markets, including residential builders, general contractors, and land developers. By partnering with these specialists, the overall cost structure can be closely managed. Further, all internal shared services are centralized at corporate office in Washington state. Centralized functions include purchasing, accounting, finance, operations, legal, human resources, transaction coordination, and permitting. Centralizing these important functions keeps infrastructure costs under tight control.

REAL ESTATE PORTFOLIO

Harbor operates in three distinct high growth regions at this time, Washington, California, and Texas. As of March 2022, the company owns or controls 26 communities in these states. The company engages in comprehensive research to identify prime markets to make real estate investments. Some of these factors include population growth, employment growth, a reasonable proximity to major shipping and rail transportation hubs, diversified employment base, and above average household income.

Washington

The company owns or controls 2,160 units or lots in the state of which 41% are owned by the company and 59% are controlled. The controlled properties are those that are under contract to be purchased and the company is typically engaging in due diligence on these assets.

The real estate is diverse across most of the company's offerings and includes developing and selling lots, building and selling apartment complexes, building and selling townhomes, selling entitled land and building homes. The communities are principally based in the cities of Blaine, Belfair, Bremerton, Tacoma, Olympia, Port Orchard, Poulsbo and Yelm.





Source: HCDI Investor Presentation

California

Operations in this state are focused on developing and entitling residential lots to be sold to the public. The company is not building homes in this community. The Darkhorse community is located in the city of Auburn, a growing city located approximately 30 miles northeast of Sacramento, which is California's state capital. The company originally purchased 68 lots for this project and as of August 17th, 2022, 63 remain unsold.





Source: HCDI Investor Presentation

Texas

The company operates in various communities in the Austin metropolitan area and is involved in all aspects of the residential real estate life cycle including building and selling residential homes. The original project purchased 242 lots on which the company will develop the land and construct homes. The company will sell both lots and completed homes. Of the 242 original lots or homes, 203 remain unsold as of August 17th, 2022.

Cities in which the company operates development projects include Austin, Driftwood, Horseshoe Bay, Dripping Springs, and Georgetown. The company has indicated that luxury homes in this region started closing during the 1st quarter with sales prices of approximately $400 per square foot.

This region is known as the Hill Country of Texas and remains one of the fastest growing metro areas in the nation. It is considered one of the most beautiful regions in Texas with its rolling hills, spring-fed rivers, and many lakes. Many of Harbor's communities are close to prestigious golf courses, prominent wineries, and unique shopping. The Hill Country is home to the state's capital, Austin.

Harbor closed on the sale of its first two single-family homes in the Driftwood community of La Ventana in March 2022. The company followed that sale with nine additional homes under contract that are expected to close later this year. There are currently 23 other lots in various stages of construction throughout the Hill Country and nearby Horseshoe Bay.

A detailed portfolio breakdown of the original lots includes the following communities in the Austin MSA:

- Bunker Ranch, Dripping Springs (4 lots)
- Cimarron Hills, Georgetown (5 lots)
- Creek's Edge, Austin (2 lots)
- Flintrock Falls, Austin (1 lot)
- La Ventana, Driftwood (9 lots)
- Siena Creek, Horseshoe Bay (35 lots)
- Stone House, Horseshoe Bay (68 lots)
- Summit Rock, Horseshoe Bay (108 lots)
- The Trails of Horseshoe Bay, Horseshoe Bay (10 lots)

Harbor's luxury homes in this region range from 2,200 to 4,200 square feet, with prices ranging from $900,000 to more than $2,000,000. Most homes feature four-five bedrooms, three-four bathrooms, and two-three car garages. The design encompasses styles of that region with contemporary modern farmhouse elements reminiscent of Hill Country, such as vaulted ceilings, accent beams, stone and natural wood tones, modern light fixtures, barn doors, metal or tile roofing, quartz countertops, and high-end appliances.





Source: HCDI Investor Presentation

The company further breaks down revenues and gross profit by five reportable segments:
1) Homes, 2) Developed lots, 3) Entitled land, 4) Multi-Family and 5) Fee build.

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2022	2021	2022	2021
Revenue by segment				
Homes	$ 4,693,900	$ 3,929,300	$ 25,758,100	$ 14,277,700
Developed lots	—	770,000	9,080,000	7,770,000
Entitled land	3,400,000	10,440,000	7,880,000	19,750,000
Multi-family	27,200	—	27,200	—
Fee Build	3,623,500	2,871,300	7,825,300	4,219,500
Other	3,900	—	45,400	—
	$ 11,748,500	$ 18,010,600	$ 50,616,000	$ 46,017,200
Gross profit (loss) by segment				
Homes	$ 888,900	$ 431,300	$ 4,297,000	$ 1,899,500
Developed lots	(87,300)	274,600	935,700	228,300
Entitled land	52,100	5,947,400	3,819,200	8,300,600
Multi-family	2,100	—	(100)	—
Fee Build	(167,700)	491,100	(3,185,300)	650,500
Other	(250,400)	—	(1,305,900)	—
	$ 437,700	$ 7,144,400	$ 4,560,600	$ 11,078,900

Source: HCDI SEC filings

MANAGEMENT TEAM

Sterling Griffin
Chief Executive Officer

Mr. Griffin began his career at James S. Griffin Co. in January 1985 as a principal and Vice President of Marketing, where he focused on the syndication of apartment properties, raw land, and retirement home facilities in the Puget Sound region of Washington State. Beginning in June 1989, Mr. Griffin co-founded several businesses over a 12-year period, while actively self-employed as a real estate broker, investor, and developer. In January 2012, he became the Chief Operating Officer for Hudson Homes LLC, a Washington-based residential builder and developer focused on construction of upscale homes in Pierce and Kitsap Counties, where he was responsible for land acquisition, construction, marketing, and sales. In 2014, Mr. Griffin founded the Company. Mr. Griffin is a lifelong Washington resident who graduated from Colorado College with a Bachelor of Arts degree in History in 1984.

Jeff Habersetzer
Chief Operating Officer

Mr. Habersetzer is the Chief Operating Officer and also serves as General Counsel and Corporate Secretary. Mr. Habersetzer has vast legal experience forming and managing corporations, business contracts, litigation, disputes, and representing lenders in real estate closings and debt agreements. Mr. Habersetzer has served as General Counsel since 2019, playing an integral role in four successful capital raises for the company, as well as quarterly and annual SEC reports. Mr. Habersetzer holds a Bachelor's degree from the University of Washington and both a law degree and MBA from Seattle University.

Lance Brown
Chief Financial Officer

Mr. Brown serves as Chief Financial Officer. Prior to joining Harbor, Mr. Brown was Vice President and Chief Accounting Officer at Select Interior Concepts where he was responsible for Finance, Accounting, SEC Reporting, and Tax. Mr. Brown developed the public company accounting and reporting infrastructure, was extensively involved in the diligence and integration for multiple completed acquisitions, assisted with divestitures, and provided support for the sale and go private transaction of SIC. Mr. Brown started his career in public accounting at PricewaterhouseCoopers. He holds a Bachelor of Business Administration degree from the University of Georgia and a Master of Accountancy from Auburn University. Mr. Brown is a Certified Public Accountant.

RISK FACTORS

- The housing market may not continue to grow at the same rate as it has in the past, or may decline, and any decline in the company's markets or for the homebuilding industry in general may materially and adversely affect the business and financial condition. Other areas of unpredictability include regional difficulties, mortgage rates, land costs, construction costs, consumer lending, reduced consumer income, tighter bank requirements, and the effect of pandemics.

- Substantially all of the company's home buying customers finance their home purchases through lenders that provide mortgage financing. Mortgage interest rates have generally trended downward for the last several decades and reached historic lows in 2020 and 2021, which made the homes the company sold more affordable. Starting in the 1st quarter of 2022, mortgage lending rates began to rise as the U.S. Federal Reserve began raising short-term rates to fight inflation. Higher mortgage rates may negatively affect the company's financial results.

- Real estate is an illiquid asset and typically cannot be sold quickly. The capitalization rates at which properties may be sold could be higher than historic rates, thereby reducing the potential proceeds from sale. Consequently, the company may not be able to change real estate or land inventory promptly in response to changes in economic or other conditions. These factors could adversely affect the company's core business, financial condition, and operating results.

- Inflation could adversely affect the real estate business and the company's financial results by increasing the costs of land, raw materials and labor needed to operate the business. If the markets in which the company operates have an oversupply of homes, relative to demand, the company may be unable to offset any such increases in costs with corresponding higher sales prices for home sales.

- The company operates in a very competitive environment that is characterized by competition from a large number of other homebuilders and land developers in each geographical market in which the company has operations. There are relatively low barriers to entry into the homebuilding business and the company competes with numerous large national and regional homebuilding companies as well as smaller local homebuilders and land developers.

- The company's operations are located in many areas that are subject to natural disasters, severe weather or adverse geological conditions such as hurricanes, tornadoes, droughts, floods, brushfires, wildfires, prolonged periods of precipitation, landslides, soil subsidence, and earthquakes. The occurrence of any of these events could damage land parcels and projects, cause delays in completion of certain projects, or reduce consumer demand for housing or land.

- The homebuilding and land development industry is capital-intensive and requires significant up-front expenditures to acquire land parcels and begin development. If internally generated funds are not sufficient, the company would need to seek additional capital in the form of equity or debt financing from a variety of potential sources, including additional bank financings and/or securities offerings. These sources of capital may not be available during times of economic distress.

SUMMARY

The company's recent strategic shift to focus on multi-family projects will likely payoff in the near-to-mid term as a difficult single-family housing market may drive consumers to rental properties as opposed to home purchases. This will increase activity in the multi-family development industry, a trend in which Harbor can capitalize on due its current listed projects, new projects under development, and overall flexible business model.

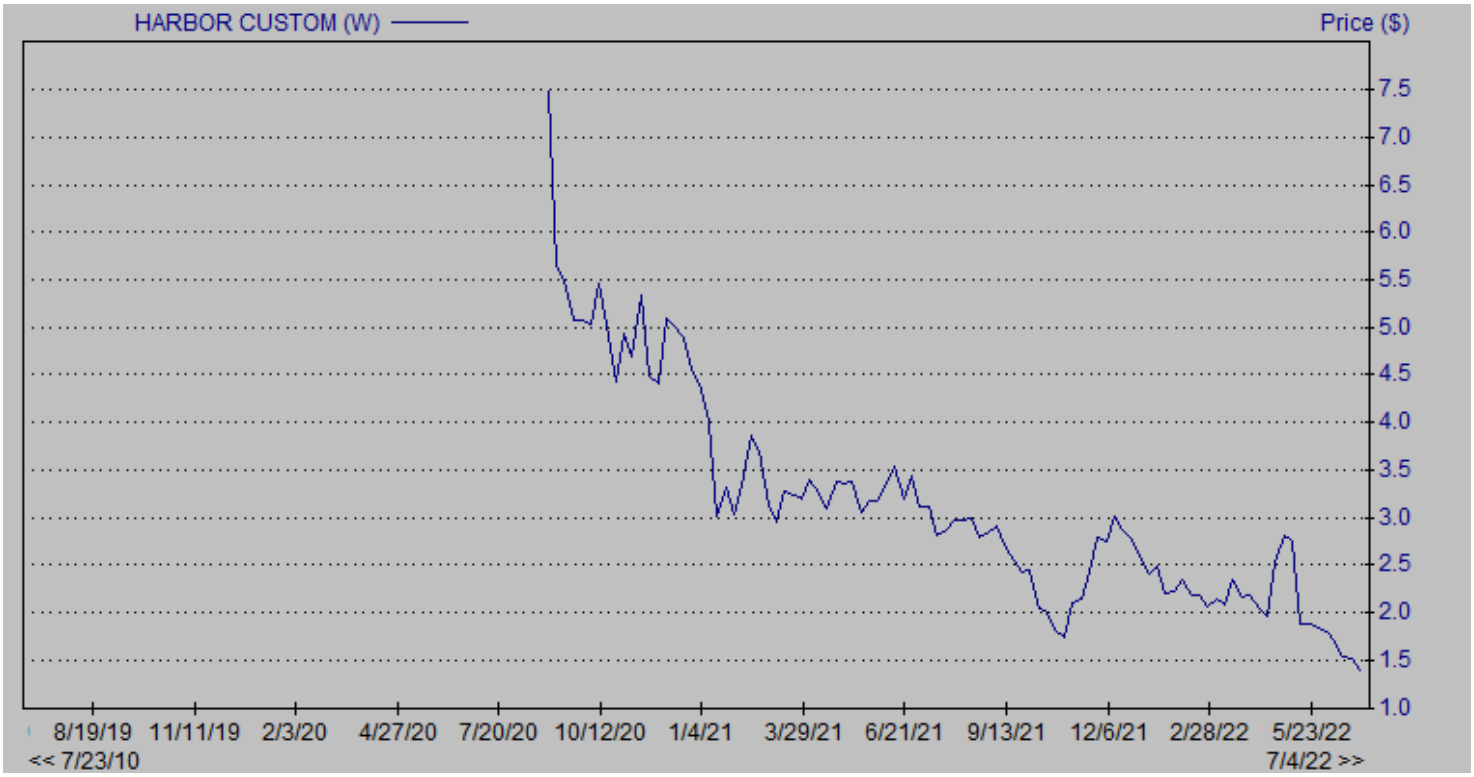
The recent increase in mortgage rates may affect the company negatively to some degree, however we feel Harbor may be well positioned to manage a rising rate environment. In certain markets such as Texas, there exists a very strong supply/demand imbalance which could support home sales going forward. In addition, many buyers in Texas markets come from high real estate value states such as California in which cash purchases are common. Further, if a high mortgage rate environment does eventually affect home or lot sales, this may drive individuals and families to rental situations in which the company also participates through multi-family projects in certain regions in which the company operates.

From a longer-term perspective, the home ownership sector does have positive tailwinds due to the demographics of the millennial population. Aging millennials are expected to drive home ownership rates higher from the 30% range for those in their late 20's to over 60% once they reach the age of 30 or above.

In addition, there still appears to be a shortage of homes in the country based on current needs and population growth. Mark Zandi, chief economist at Moody's Analytics, estimates there could be a shortfall of close to 1.6 million homes. The biggest culprit in the recent phenomenon of rising home prices is the historic housing shortage. There is also a shortage in multi-family rental properties due to years of underinvestment in the sector.

Currently, investor sentiment remains very low on homebuilder stocks due to rising mortgage rates and investor fears about a potential recession in 2022 or 2023. Homebuilder stocks tend to underperform the market during periods of rising rates and ahead of recessions, however this effect may already be priced in for real estate related equites.

HISTORICAL STOCK PRICE



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