AvalonBay COMMUNITIES

Fourth Quarter 2016 Management Letter

- **Q4 2016 Core FFO per share was $2.12, 6.5% above Q4 last year**
- **Full year 2016 Core FFO per share increased 8.5%, and is up more than 105% over the last six years**
- **Q1 2017 dividend increased 5.2%, and is up nearly 60% over the last six years**
- **2017 Core FFO per share expected to increase 5.5%**

Review of Full Year and Q4 2016 Results

2016 was another strong year for AvalonBay. Our stabilized portfolio delivered a sixth consecutive year of healthy operating results. We completed eight new development communities and acquired five stabilized communities. In addition, we raised $1.35 billion of attractively priced capital to fund ongoing investment and refinancing activity. Based on these achievements and our expectations for 2017, concurrent with our Q4 earnings release we announced an increase in our quarterly dividend to $1.42 per share, which represents a 5.2% increase over our 2016 dividend. Since 2011, our quarterly dividend has increased nearly 60%.

For the fourth quarter of 2016, Core FFO per share was $2.12. For the full year, Core FFO per share increased 8.5%, driven by a 4.8% increase in same-store NOI and contributions from new investment activity. Over the last six years, Core FFO per share has more than doubled to $8.19 per share from $3.98 per share.

We continued to enjoy healthy same-store revenue and NOI growth in 2016; however, the rate of growth moderated throughout the year. This deceleration was driven by demand and supply coming into equilibrium. Same-store like-term rent change for the seasonally slow fourth quarter was 1.3%, down 290 basis-points from the prior-year period. For the full year, same-store, like-term rent change was 3.2%, or 260 basis-points below the rate achieved in 2015.

Development continued to contribute meaningfully to both NAV and Core FFO per share growth in 2016. For the year, we completed eight development communities, representing a total capital investment of approximately $510 million. These new communities are projected to generate a weighted average initial stabilized yield of 6.7% and were completed at a cost basis under $300,000 per apartment home, roughly $100,000 per apartment home below the market value of our existing 19 year-old portfolio. In addition, we started nine development communities in 2016 that are projected to contain over 2,700 apartment homes and approximately 100,000 square feet of retail space, and represent $1.6 billion (at share) in projected total capital cost.

We also increased our acquisition activity in 2016 by purchasing five stabilized communities for $530 million, which were funded through increased disposition activity. In doing so, we successfully recycled

This Management Letter provides management commentary regarding recent Company activity and expectations. See pages 6, 7 and 8 of this Management Letter, and our 4th Quarter 2016 Earnings Release, for important information concerning forward-looking statements and certain non-GAAP and other financial terms and information, including a reconciliation of Net Income attributable to common stockholders to FFO and Core FFO.

capital from communities developed in prior cycles into newer properties located in attractive, infill submarkets.

The unsecured debt and transaction markets provided a cost-effective way to finance our business in 2016. During the year, we raised $1.35 billion of new capital by borrowing approximately $1.1 billion in unsecured debt at an average rate of 3.4%, inclusive of the effect of interest rate hedges, and by sourcing the balance through wholly owned dispositions and distributions from unconsolidated real estate entities.

Economic & Apartment Market Update

Looking ahead, we expect the economic landscape in 2017 to be similar to last year. Our business plan assumes that job and income growth, favorable demographics and delays in family formation (e.g. marriage, children) will produce another year of healthy apartment demand. However, we believe an increase in new apartment deliveries in 2017 will temper rental revenue growth across many of our regions.

Accordingly, we project Core FFO per share to increase 5.5% in 2017. Core FFO per share growth is expected to be driven by 2.8% same-store NOI growth and the lease-up of over 4,000 new apartment homes, which are anticipated to contribute approximately $65 million of new NOI in 2017.

Economy

We believe a 2017 consensus outlook calling for moderate economic growth this deep into an expansion is encouraging, and it is consistent with the expectation that this economic cycle will rival the durability of the 1990s expansion.

Consumer fundamentals are healthy. In recent months, the rate of job growth stabilized, job openings hit new highs, the unemployment rate fell to a nine-year low, and wage growth began to accelerate. This backdrop, supported by low household debt burdens, has driven consumer confidence to its highest level in more than 15 years, which is prompting a rebound in household formation.

The U.S. business sector is also healthy. Corporate profits improved in two of the last three quarters and business confidence has been on a steady ascension since September. Further, businesses are poised to benefit from potential regulatory and tax reform, although the lack of clarity surrounding policy proposals may affect business investment in the near-term.

Overall, we believe U.S. consumers and businesses enter 2017 with renewed optimism in a favorable economic environment.

Apartment Market

We expect economic trends will support healthy apartment demand during 2017. In our markets, we project job growth of 1.7%, 20 basis-points below last year’s pace, and a more even distribution of job growth across our markets in 2017 than in prior years. We forecast personal income growth to accelerate to 5.0%, from 3.6% in 2016, as the labor market continues to tighten.

Demographic trends will continue to support apartment demand over the next several years. According to U.S. Census Bureau projections, the key 25 – 34 year-old cohort will increase by over 600,000 individuals in 2017, and by nearly 1.7 million individuals by the end of the decade. Moreover, many within this cohort are delaying marriage and children, which continues to extend rental tenures.

Over the last few years, supply has responded to strong apartment demand. We expect new apartment deliveries as a percentage of existing inventory in our markets to peak at 2.1% in 2017, up approximately 50 basis-points from 2016. Within our regions, we project new apartment supply in our urban submarkets (defined as submarkets with more than 3,500 households per square mile) will be approximately 2.8% of existing apartment stock, while our suburban submarkets will see an increase in existing apartment stock of roughly half that rate. Among our regions, we expect the Seattle metro area to experience the largest increase in existing apartment stock, at 3.7%; conversely, we project Southern California will remain our most supply-constrained region, with new apartment deliveries equal to approximately 1.5% of existing stock. Looking further ahead, in 2018 and 2019, we expect new apartment deliveries to decline from 2017 levels due to a strengthening for-sale market and a reduction in financing available to multifamily development.

AVB Outlook

Property Operations

For 2017, we expect same-store rental revenue growth of 2.0 to 3.0%. We believe quarterly year-over-year same-store rental revenue growth will continue to moderate through the third quarter before stabilizing in the second half of the year.

We expect our West Coast portfolio to outperform our East Coast portfolio, but anticipate performance between the two coasts will continue to converge in 2017. We forecast same-store rental revenue growth in the Seattle metro area and Southern California to lead the portfolio at 4.0 and 5.0%, while Northern California is projected to lag with same-store rental revenue growth of approximately 1.5%. On the East Coast, we expect same-store rental revenue growth of 2.0 to 2.5% in the New England and Mid-Atlantic regions, while Metro New York/New Jersey is projected to produce same-store rental revenue growth of 1.5 to 2.0%.

We anticipate same-store operating expense growth of 1.5 to 2.5% in 2017, which in turn is expected to generate same-store NOI growth of 2.0 to 3.5%.

Development

Development continues to be an attractive source of NAV and Core FFO per share growth. We expect to break ground on ten developments in 2017, representing $900 million in projected total capital cost. All ten of our 2017 projected development starts are located in more supply-constrained, infill suburban submarkets where development economics are currently most attractive. We are expecting to complete a Company-record $1.7 billion of new development in 2017, which will reduce development under construction as a percentage of Total Enterprise Value from nearly 13% at the end of 2016 to 10% at year-end 2017 (based on our year-end 2016 Total Enterprise Value).

We continue to maintain a disciplined approach to the structuring of new development opportunities. At year-end 2016, we had just $85 million in land held for development on the balance sheet, the lowest amount in over a decade. We plan to continue to structure new development opportunities primarily as longer-term purchase contracts with modest at-risk deposits to preserve flexibility.

Capital Activity & Balance Sheet

We enter 2017 with a very strong balance sheet and continue to enjoy excellent access to liquidity. At year-end 2016, Net Debt-to-Core EBITDA was 5.0x, 80% of NOI was unencumbered and Interest Coverage was 6.8x. We were 80% match-funded on our $4.0 billion of development activity underway or recently completed, which is calculated using $1.4 billion that is remaining to be invested less the sum of (i) approximately $215 million in unrestricted cash and (ii) approximately $350 million in cash from operations available for investment, annualized (based on fourth quarter 2016 results). In addition, we currently maintain $800 million of interest rate protection agreements that will hedge against unfavorable changes to interest rates for anticipated 2017 debt issuance activity.

Our 2017 capital plan contemplates sourcing $1.7 billion of external capital primarily from new debt and asset sales. However, the amount, timing and form of new capital will depend on capital market conditions and pricing throughout the year.

Conclusion

2016 was another strong year for AvalonBay. Favorable apartment fundamentals helped us deliver a sixth consecutive year of healthy operating results. We continued to invest in profitable development opportunities; we improved the quality of our portfolio through the transaction market; and we enhanced our financial flexibility.

In 2017, we expect apartment demand to remain healthy but anticipate that elevated apartment deliveries, particularly in our urban submarkets, will temper growth in same-store revenue. We believe our accretive investment platform will continue to contribute to Core FFO and NAV per share growth, and we believe we remain well positioned to pursue accretive investment opportunities.

Timothy J. Naughton	Kevin P. O'Shea
Chairman & CEO	Chief Financial Officer

This Management Letter and the related presentation dated February 1, 2017 contain forward-looking statements, which are indicated by the use of words such as “expects,” “projects,” “forecast,” “outlook,” “estimate,” “anticipate” and other words that do not relate to historical matters. Actual results may differ materially. For information concerning risks and other factors that could cause such differences, see “Forward Looking Statements” in AvalonBay’s earnings release dated February 1, 2017. The Company does not undertake a duty to update the projections and expectations stated in this letter, which speak only as of the date of this letter. Non-GAAP financial measures and certain other terms used in this letter are defined, reconciled and further explained in Attachment 15 to the Company's earnings release dated February 1, 2017.
This Management Letter and the related presentation are provided in connection with AvalonBay’s fourth quarter 2016 earnings conference call held on February 2, 2017. This Management Letter and the related presentation are intended to accompany the earnings release, and should be read in conjunction with the earnings release. AvalonBay does not intend to update any of these documents, which speak only as of their respective dates.

The earnings release is available on AvalonBay’s website at www.avalonbay.com/earnings

Reconciliations of Net Income attributable to common stockholders to FFO and to Core FFO for Q4 2016, Q4 2015 and full year 2016, 2015 and 2010 are as follows (dollars in thousands):

	Q4 2016	Q4 2015	Full Year 2016	Full Year 2015	Full Year 2010
Net income attributable to common stockholders	$ 242,235	$ 155,428	$ 1,034,002	$ 742,038	$ 175,331
Depreciation - real estate assets, including discontinued operations and	140,773	126,824	538,606	486,019	237,041
Distributions to noncontrolling interests, including discontinued	10	9	41	38	55
Gain on sale of unconsolidated entities holding previously depreciated	(4,897)	(2,633)	(58,069)	(33,580)	-
Gain on sale of previously depreciated real estate	(90,041)	(9,474)	(374,623)	(115,625)	(74,074)
Casualty and impairment (recovery) loss, net on real estate (1)(5)	-	-	(4,195)	4,195	-
FFO attributable to common stockholders	$ 288,080	$ 270,154	$ 1,135,762	$ 1,083,085	$ 338,353
Adjusting items:					
Joint venture losses (gains) (2)	$ 268	$ (388)	$ 6,031	$ (9,059)	$ -
Impairment loss on real estate (3)(5)	-	-	10,500	800	-
Casualty loss (gain), net on real estate (4)(5)	-	125	(10,239)	(15,538)	-
Business interruption insurance proceeds	(143)	(998)	(20,565)	(1,509)	-
Lost NOI from casualty losses covered by business interruption	1,786	2,790	7,366	7,862	-
Loss (gain) on extinguishment of consolidated debt	4,614	-	7,075	(26,736)	-
Acquisition costs	959	352	3,523	3,806	-
Severance related costs	(55)	215	852	1,999	(1,550)
Development pursuit and other write-offs	(107)	766	3,662	1,838	-
Joint venture promote (7)	(4,538)	-	(7,985)	(21,969)	-
Loss (gain) on sale of other real estate	697	-	(10,224)	(9,647)	-
Legal settlements	(417)	-	(417)	-	(927)
Income taxes	-	106	-	1,103	
Federal excise tax	-	-	-	-	(235)
Severe weather costs	-	-	-	-	672
Investment management fund transaction costs, net (8)	-	-	-	-	811
Core FFO attributable to common stockholders	$ 291,144	$ 273,122	$ 1,125,341	$ 1,016,035	$ 337,124
Average shares outstanding - diluted	137,519,045	137,349,671	137,461,637	134,593,177	84,632,869
Earnings per share - diluted	$ 1.76	$ 1.13	$ 7.52	$ 5.51	$ 2.07
FFO per common share - diluted	$ 2.09	$ 1.97	$ 8.26	$ 8.05	$ 4.00
Core FFO per common share - diluted	$ 2.12	$ 1.99	$ 8.19	$ 7.55	$ 3.98

(1) In 2015, the Company recognized an impairment on depreciable real estate of $4,195 from the severe winter storms that occurred in the Company's Northeast markets. The Company received insurance proceeds in 2016, net of additional costs incurred, of $5,732 related to the winter storms. $4,195 of this recovery is recognized in Full Year 2016 as an offset to the loss incurred in the prior year period. The balance of the net insurance proceeds received in 2016 of $1,537 is recognized as a casualty gain in Full Year 2016 and is included in the reconciliation of FFO to Core FFO.

(2) Amount for Full Year 2016 is primarily composed of the Company's portion of yield maintenance charges incurred for the early repayment of debt associated with joint venture disposition activity and the write-off of asset management fee intangibles primarily associated with the disposition of communities in the U.S. Fund. Amount for Full Year 2015 is primarily composed of the Company's proportionate share of gains and operating results for joint ventures formed with Equity Residential as part of the Archstone acquisition.

(3) Amounts include impairment charges relating to ancillary land parcels.

(4) Amount for Full 2016 includes $8,702 in property damage insurance proceeds for the Edgewater casualty loss, and $1,537 in property damage insurance proceeds in excess of the total recognized loss related to severe winter storms in the Company's Northeast markets that occurred in 2015. Amount for Q4 2015 consists of demolition and additional incident expenses for the Edgewater casualty loss and amount for Full Year 2015 includes $44,142 of Edgewater insurance proceeds received partially offset by $28,604 for the write-off of real estate and related costs.

(5) Aggregate impact of (i) Casualty and impairment (recovery) loss, net on real estate, (ii) Impairment loss on real estate and (iii) Casualty loss (gain), net on real estate for Full Year 2016, is a gain of $3,935 as shown on Attachment 1 - Detailed Operating Information.

(6) Amounts relate to a casualty event at Edgewater in Q1 2015, for which the Company received $20,306 in business interruption insurance proceeds in Q1 2016.

(7) Amounts for Q4 and Full Year 2016 are composed of the Company's recognition of its promoted interest in Fund II. Amount for Full Year 2015 is primarily composed of a joint venture partner's buyout of the Company's promoted interest in future distributions of MVP I, LLC.

(8) Represents the Company's proportionate share of the investment management fund activity.

A reconciliation of the ranges provided for Projected Core FFO to the ranges provided for projected EPS (diluted) are as follows:

	Low Range	High Range
Projected EPS (diluted) - Full Year 2017	$ 6.42	$ 6.82
Depreciation (real estate related)	4.09	4.29
Gain on sale of communities	(1.92)	(2.12)
Projected FFO per share (diluted) - Full Year 2017	$ 8.59	$ 8.99
Joint venture income, development pursuit and other write-offs, and severance related items	(0.14)	(0.14)
Lost NOI from casualty losses covered by business interruption insurance	0.03	0.03
Gain on extinguishment of consolidated debt	(0.04)	(0.04)
Projected Core FFO per share (diluted) - Full Year 2017	$ 8.44	$ 8.84

Q4 2016 cash from operations available for investment, annualized is the Company's fourth quarter 2016 Core FFO, less (i) fourth quarter 2016 dividends declared – common and (ii) fourth quarter 2016 non-rev capex, annualized. Q4 2016 cash from operations available for investment, annualized does not represent the Company's Net cash provided by operating activities as presented in the Company's consolidated financial statements. A reconciliation of Q4 2016 cash from operations available for investment, annualized to Core FFO is as follows (dollars in thousands):

	Q4 2016
Core FFO	$ 291,144
Dividends declared - common	(185,397)
Non-rev capex (1)	(19,242)
Q4 2016 cash from operations available for investment	$ 86,505
Q4 2016 cash from operations available for investment, annualized	$ 346,022

(1) Non-Rev Capex per Home as disclosed on Attachment 3 of the Company's Fourth Quarter 2016 Earnings Supplemental was $305 and represents Non-Rev Capex for the Company's Established and Other Stabilized community buckets ($305 per Home multiplied by 63,087 apartment homes).