MARKET REPORT | 3Q/2018

Orange County Multifamily

NorthMarq

Employment Gains Driving Rental Demand, Low Vacancy Rates

Highlights

- The Orange County multifamily market was steady during the third quarter. Renter demand for apartments is strong, keeping the vacancy rate unchanged from the second quarter to the third quarter at 4 percent.
- More than 2,600 units have come online to this point in 2018, and nearly 5,000 apartments are currently under construction.
- Rents have generally been on an upswing, but there was a modest dip during the third quarter. Current asking rents are $1,922 per month, 2.8 percent higher than one year ago.
- Sale prices have been posting robust gains, particularly as some newer properties have been changing hands. The median price has spiked nearly 30 percent from 2017 to 2018, reaching approximately $340,000 per unit. Cap rates have compressed to an average of about 4.3 percent.

Orange County Multifamily Market Overview

The Orange County multifamily market remained healthy during the third quarter. Orange County has the highest median single-family home price of any county in Southern California, making renting the only reasonable option for a significant segment of the local population. These elevated home prices, which topped $725,000 during the third quarter, support a consistent base of renters for apartments, and the Orange County multifamily vacancy rate has remained in the 3-4 percent range since 2015. Vacancy has remained tight even as new projects have come through the development pipeline. This is most clearly evident in the Irvine submarket, which has been the location of the most new development since 2015. Vacancy in Irvine has declined in recent years, even as new projects have been delivered.

Market Indicators

	3Q/2018
Vacancy	→
Rents	↓
Transaction Activity	↓
Price Per Unit	↑
Cap Rates	→

Summary Statistics — Orange County Market

Summary Statistics	Orange County Market
Vacancy Rate	4.0%
- Change from 3Q 2017 (bps)	+40
Asking Rents (per month)	$1,922
- Change from 3Q 2017	+2.8%
Median Sales Price (per unit YTD)	$340,700
Average Cap Rate (YTD)	4.3%

Orange County Multifamily Market Overview (cont.)

The investment climate for multifamily buildings in Orange County remains quite strong. The median price has surged to more than $340,000 per unit thus far in 2018, with a few newer projects changing hands for more than $400,000 per unit. While sales velocity thus far in 2018 has lagged levels from last year, the projects that are selling generally include larger properties at higher dollar amounts. During the first three quarters of 2018, four projects traded for more than $100 million; in all of 2017 only one sale topped $100 million. Cap rates are low and have compressed year to date; average cap rates in 2018 are approximately 4.3 percent, down 30 basis points from one year earlier.

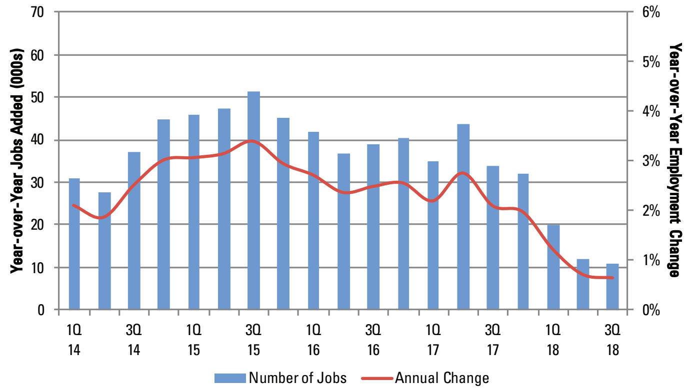
Submarket Statistics

Submarket Name	3Q 2018 Vacancy	3Q 2017 Vacancy	Annual Vacancy Change (BPS)	3Q 2018 Rents	3Q 2017 Rents
Buena Park	1.5%	1.2%	30	$1,545	$1,515
Costa Mesa	2.2%	2.3%	(10)	$1,880	$1,932
Westminster/Fountain Valley	2.4%	2.3%	10	$1,589	$1,540
Tustin	2.5%	2.1%	40	$1,939	$1,881
Placentia/Northeast Anaheim	2.6%	2.6%	-	$1,482	$1,495
North Anaheim	2.9%	2.5%	40	$1,502	$1,464
Laguna Beach/Dana Point	3.4%	3.5%	(10)	$2,012	$1,957
Fullerton	3.7%	4.5%	(80)	$1,628	$1,591
Huntington Beach	3.9%	3.9%	-	$1,841	$1,777
Orange	3.9%	1.8%	210	$1,932	$1,898
Mission Viejo	4.1%	2.6%	150	$1,892	$1,861
Laguna Hills	4.4%	7.5%	(310)	$1,913	$1,974
North Santa Ana	4.5%	2.7%	180	$1,560	$1,507
Newport Beach	4.6%	4.8%	(20)	$2,509	$2,754
Irvine	5.0%	5.4%	(40)	$2,596	$2,397
South Santa Ana	5.1%	3.9%	120	$1,991	$1,945
Brea	6.2%	2.2%	400	$1,748	$1,586
South Anaheim	7.9%	6.6%	130	$1,843	$1,750

Employment

- Employment in Orange County is expanding, but at a fairly modest pace. During the past 12 months, employers have added 10,800 jobs, a 0.7 percent increase. Last year at this time, growth was far stronger, having topped 2 percent.
- Leisure and hospitality, one of the largest employment sectors in Orange County, has been expanding in recent years. In the past year, employment in the sector has grown by 3.2 percent, with the addition of 7,100 new positions.
- One of the drags on the local employment market has been the manufacturing sector, which has contracted by 3.5 percent year over year with the loss of 5,500 jobs.
- **Forecast:** Employers are forecast to add approximately 15,000 jobs in 2018, down from more than 30,000 net new positions created last year. The pace of growth will be approximately 0.9 percent this year.

Employment Overview



Sources: NorthMarq, Bureau of Labor Statistics

During the past 12 months, employers have added 10,800 jobs, a 0.7 percent increase

Vacancy

- Vacancy in Orange County held steady at 4 percent from the second quarter to the third quarter. The rate is up 40 basis points from one year ago.
- One driver of the upward trend in vacancy has been the delivery of new, high-end units. The Class A vacancy rate ended the third quarter at 5.1 percent, up 20 basis points year over year. After averaging 4.2 percent from 2014-2017, the Class A vacancy rate has been above 5 percent for each of the past two years.
- While the Class A vacancy rate has pushed higher, renter demand for high-end units remains strong. Net absorption in Class A units in Orange County thus far this year is nearly 2,500 units, accounting for nearly all of the market total.
- **Forecast:** Vacancy is likely to inch higher at the end of the year as new units come online. Vacancy is forecast to post a 40-basis-point annual increase in 2018, with the rate reaching 4.2 percent.

Vacancy Trends

Sources: NorthMarq, Reis

Renter demand for high-end units remains strong

Rents

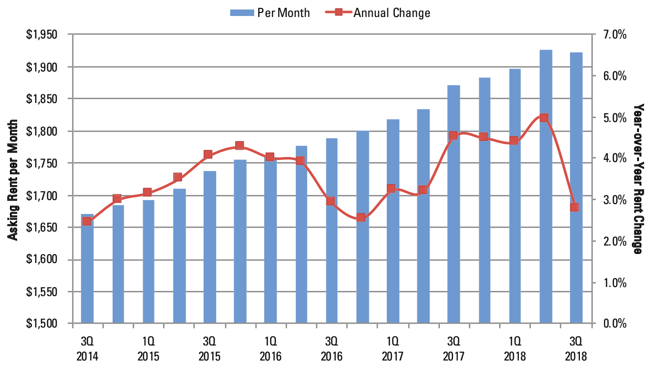
> Asking rents softened a bit during the past three months, the first quarterly decline in more than five years. Asking rents are $1,922 per month, 2.8 percent higher than one year ago.

> Vacancies in Class B and Class C properties in Orange County are often quite low, allowing for steady rent gains in these buildings. The combined average asking rent in Class B and Class C apartments is $1,696 per month, up 2.9 percent from one year ago.

> The Irvine submarket has the largest inventory total in Orange County and some of the highest rents. Asking rents in the Irvine submarket ended the third quarter at $2,596 per month, up 8.3 percent from one year ago.

> **Forecast:** Rents in Orange County are expected to remain on a fairly steady upward trajectory. Asking rents are forecast to end 2018 at $1,950 per month, 3.6 percent higher than one year earlier.

Rent Trends



Sources: NorthMarq, Reis

Asking rents softened a bit, having their first quarterly decline in more than five years

Development and Permitting

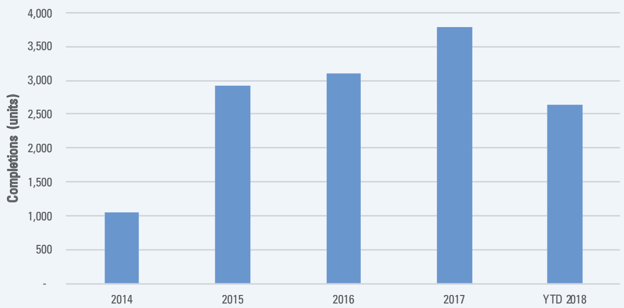
> After deliveries peaked in the second quarter, completions of new units slowed in the third quarter. Approximately 250 apartment units were delivered in the third quarter, and more than 2,600 units have come online through the first nine months of the year.

> Projects totaling nearly 5,000 units are currently under construction, with the bulk of these projects scheduled to deliver in 2019.

> Nearly half of the units currently under construction are located within the Irvine submarket. Inventory growth in Irvine has been expanding at an average pace of approximately 1,000 units per year since 2012, while vacancy remained flat.

> **Forecast:** After nearly 3,800 apartment units were delivered in 2017, developers are forecast to complete approximately 4,200 units in 2018. This will mark the strongest single year of new apartment construction in more than a decade.

Development Trends



Sources: NorthMarq, Reis

Nearly half of the units currently under construction are located within the Irvine submarket

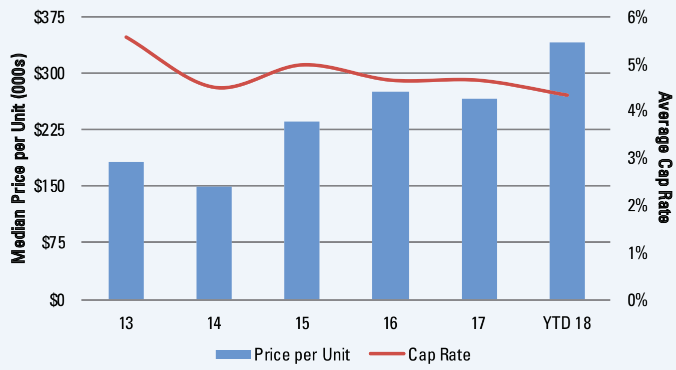
Multifamily Sales

> Sales velocity was fairly steady in the first half of the year but slowed during the third quarter. Transaction counts through the first nine months of 2018 were down about 15 percent from the same period in 2017.

> Prices have been on an upward trajectory throughout 2018. The median price thus far this year has been approximately $340,000 per unit, up nearly 30 percent from the median price in 2017. Some of the increase is likely due to increased activity among newer assets; approximately 30 percent of the properties that have been sold thus far in 2018 have been built in the past 10 years.

> Cap rates are low and have compressed thus far in 2018. Year to date, the average cap rate is 4.3 percent, 30 basis points lower than the 2017 average.

Investment Trends



Prices have been on an upward trajectory throughout 2018

Recent Transactions in the Market

MULTIFAMILY SALES ACTIVITY

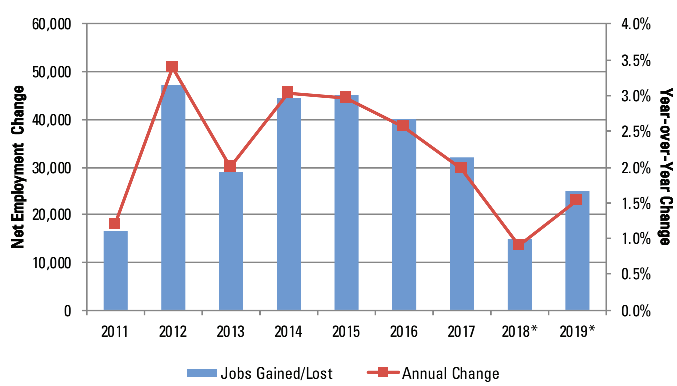
Property Name	Street Address	Units	Sales Price	Price/Unit
Corte Bella	9580 El Rey Ave., Fountain Valley	251	$85,750,000	$341,633
Bellecour Way	21041 Osterman Rd., Lake Forest	131	$56,250,000	$429,389
Pacific Pointe South	13922 Tustin East Dr., Tustin	92	$33,300,000	$361,957
Cypress Village	6343 Lincoln Ave., Buena Park	88	$26,500,000	$301,136
Las Palmas	317 E La Palma Ave., Anaheim	61	$12,755,000	$209,098

Looking Ahead

Many of the current trends in the Orange County multifamily market are expected to continue through the remainder of this year and into 2019. Employment gains are a bit more modest than in recent years, and new supply growth is gaining momentum, so there will likely be a short-term uptick in the local vacancy rate. Despite a bit of a supply-demand imbalance in the coming months, the overall nature of the Orange County multifamily market should remain favorable. Vacancy is expected to stay fairly tight in the low to mid-4 percent range, and rents will likely continue to tick higher, although there could be a slight increase in concessions.

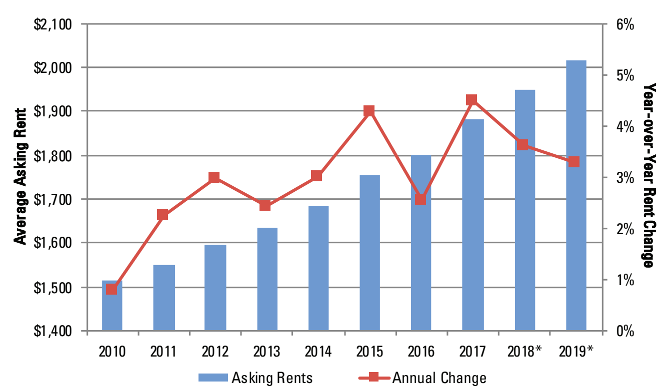
The investment climate for Orange County multifamily buildings is expected to remain healthy in the coming quarters. Even at a time when interest rates have generally trended higher, cap rates in Orange County have compressed a bit and prices have pushed higher. This reflects both the strong investor demand for apartment properties, as well as the mix of newer assets that have sold in recent quarters. Pricing and cap rates will likely be influenced by the mix of assets that are available for sale and ultimately sell. The recent increase in new development could influence the mix of properties that come to the market.

Employee Forecast



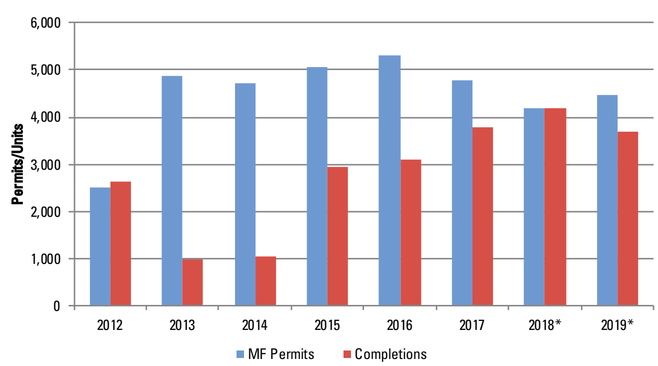
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



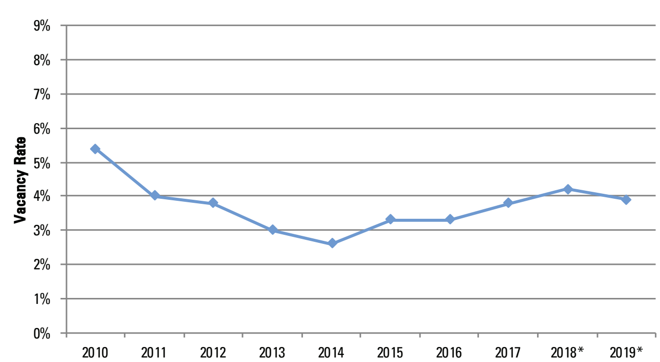
* Year End Forecast
Sources: NorthMarq, Reis

Construction & Permitting Forecast



* Year End Forecast
Sources: NorthMarq, Census Bureau, Reis

Vacancy Forecast



* Year End Forecast
Sources: NorthMarq, Reis

About NorthMarq Multifamily

NorthMarq Multifamily has a market-leading position in multifamily property sales in markets across the U.S., offering commercial real estate investors a personalized approach to buying and selling multifamily and manufactured housing properties. These teams collaborate with NorthMarq Capital's debt and equity experts nationwide to provide a full range of capital markets services, developing innovative solutions for real estate investments.

NorthMarq Capital, the largest privately held commercial real estate financial intermediary in the U.S., provides debt, equity and commercial loan servicing through over 300 mortgage banking professionals in regional offices coast-to-coast and services a loan portfolio of more than $53 billion. For more information, please visit www.northmarq.com.

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