MARKET REPORT | 4Q/2018

Inland Empire Multifamily

NORTHMARQ

Investment Activity Surges to Close 2018

Highlights

- The Inland Empire multifamily market strengthened a bit in the fourth quarter, with vacancy ticking lower, rents rising and investment activity recording a spike.
- Apartment vacancy fell 10 basis points during the fourth quarter, ending the year at 3.1 percent. Vacancy fell 20 basis points for the year. The long-term trend is for flat vacancy, which has averaged approximately 3 percent since 2013.
- Local asking rents ended the fourth quarter at $1,365 per month, a 4.4 percent increase from the preceding year. A similar rise is forecast for 2019.
- Sales activity spiked late in the year as demand accelerated. The average cap rate was below 5 percent in 2018, and the median price topped $200,000 per unit.

Inland Empire Multifamily Market Overview

The Inland Empire multifamily market had a strong fourth quarter, closing out a year where vacancy inched lower and rents pushed higher. These market measurements were favorable to apartment owners, even as the pace of local employment growth slowed late in the year. The pace of job growth in 2018 was in-line with the national rate of expansion, following several years of outperforming the country's growth rate. Looking ahead, employment growth in 2019 is expected to accelerate, supporting local renter demand for apartments. One reason the vacancy rate improved even as job growth slowed was the easing of supply-side pressures. Completions in 2018 were roughly half of the average figure from recent years, but construction is likely to accelerate in 2019.

Market Indicators

	4Q/2018
Vacancy	↓
Rents	↑
Transaction Activity	↑
Price Per Unit	↑
Cap Rates	↓

Summary Statistics — Inland Empire Market

Vacancy Rate	**3.1%**
- *Change from 4Q 2017 (bps)*	**-20**
Asking Rents (per month)	**$1,365**
- *Change from 4Q 2017*	**+4.4%**
Median Sales Price (per unit YTD)	**$208,000**
Average Cap Rate (YTD)	**4.9%**

Inland Empire Multifamily Market Overview (cont.)

The local investment market strengthened at the end of 2018, with more properties changing hands, prices rising and cap rates compressing. The surge in sales velocity drove the total activity in 2018 above the 2017 level, outperforming the national trend. The high end of the market recorded the strongest increase in activity during the fourth quarter.

More than half of the transactions that occurred during the fourth quarter topped $50 million; during the first nine months of 2018, the bulk of the transaction activity consisted of 1980s-vintage product selling in the $20-million to $40-million range. With newer properties selling late in the year, average cap rates compressed below 5 percent.

Submarket Statistics

Submarket Name	4Q 2018 Vacancy	4Q 2017 Vacancy	Annual Vacancy Change (BPS)	4Q 2018 Rents	4Q 2017 Rents
Fontana/Rialto	2.1%	2.0%	10	$1,167	$1,136
Perris	2.2%	2.6%	(40)	$1,271	$1,179
Upland	2.2%	2.3%	(10)	$1,318	$1,274
Rancho Cucamonga	2.3%	2.4%	(10)	$1,660	$1,627
Victorville	2.3%	2.7%	(40)	$1,041	$998
Colton/Loma Linda	2.6%	3.2%	(60)	$1,428	$1,372
San Bernardino	2.7%	2.8%	(10)	$1,021	$980
Indio/La Quinta/Coachella	2.8%	3.1%	(30)	$1,118	$1,043
Palm Springs/Palm Desert	2.9%	3.3%	(40)	$1,070	$1,037
University City/Moreno Valley	3.2%	2.8%	40	$1,434	$1,335
Riverside/North Magnolia	3.4%	3.8%	(40)	$1,275	$1,209
Hemet	3.6%	3.0%	60	$1,138	$1,045
North Ontario	3.8%	3.7%	10	$1,472	$1,430
Riverside County/Corona	4.4%	5.5%	(110)	$1,557	$1,510
South Ontario/Chino	4.4%	4.4%	-	$1,715	$1,653
SW Riverside County	4.8%	4.8%	-	$1,498	$1,420

Employment

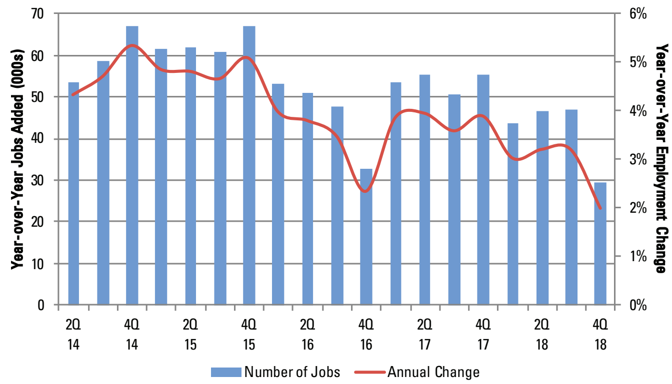
> Employment in the Inland Empire expanded in 2018, although the pace of growth was more modest than in recent years. Employers added 29,500 net new jobs in 2018, a 2 percent increase. Growth had averaged more than 4 percent per year for the five years leading up to 2018.

> Transportation and warehousing employment continues to expand as tenant demand for the Inland Empire's industrial market remains robust. Approximately 7,500 jobs were added in the transportation and warehousing sector in 2018, a 3.8 percent increase.

> The leisure and hospitality sector, which is generally an indicator of the overall health of the economy, posted strong gains for the seventh straight year. In 2018, growth in the leisure and hospitality sector totaled nearly 3.5 percent with 5,800 new jobs.

> **Forecast:** Following a slowdown in 2018, job growth is forecast to accelerate in 2019. Employers are expected to add approximately 44,000 new positions in the year ahead, a 2.9 percent increase.

Employment Overview



Sources: NorthMarq, Bureau of Labor Statistics

The leisure and hospitality sector posted strong gains for the seventh straight year

Vacancy

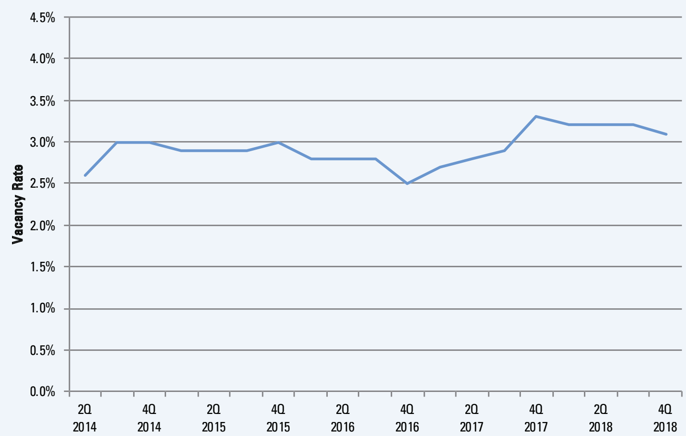
> After holding steady in the middle part of the year, vacancy in the Inland Empire declined by 10 basis points in the fourth quarter, dipping to 3.1 percent.

> Multifamily vacancy fell 20 basis points from 2017 to 2018. This marked the seventh year since 2010 where the vacancy rate declined.

> The vacancy rate in Class A properties dipped 10 basis points during the fourth quarter, reaching 4.2 percent. The rate fell 30 basis points in 2018, after rising in 2017.

> **Forecast:** Apartment construction is expected to accelerate in 2019, putting upward pressure on the vacancy rate. Vacancy is forecast to end 2019 at 3.5 percent, up 40 basis points for the year.

Vacancy Trends



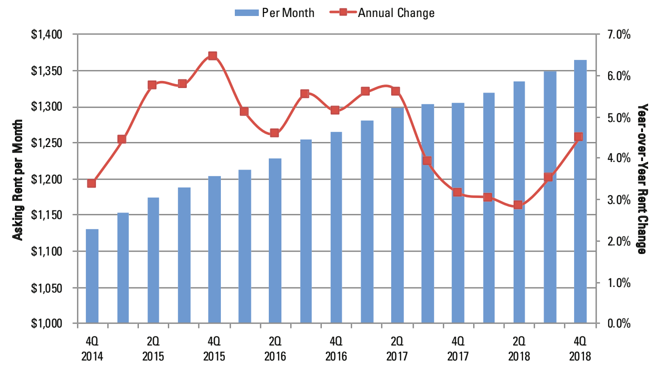
Sources: NorthMarq, Reis

Multifamily vacancy fell 20 basis points from 2017 to 2018.

Rents

- Rents in the Inland Empire continued to post steady gains during the fourth quarter. Asking rents ended the fourth quarter at $1,365 per month, up 4.4 percent from one year ago.
- The strongest rent growth is occurring in Class B and Class C properties, where vacancies are quite tight and renter demand is high. Average asking rent in Class B and Class C units is $1,188 per month, up 4.8 percent year over year.
- Rents in the University City/Moreno Valley submarket posted some of the strongest increases in the Inland Empire in 2018. Asking rents in this market spiked more than 7 percent in 2018, reaching $1,434 per month.
- **Forecast:** In 2019, asking rents are forecast to tick up approximately 4 percent to $1,420 per month, following a 4.5 percent in 2018.

Rent Trends



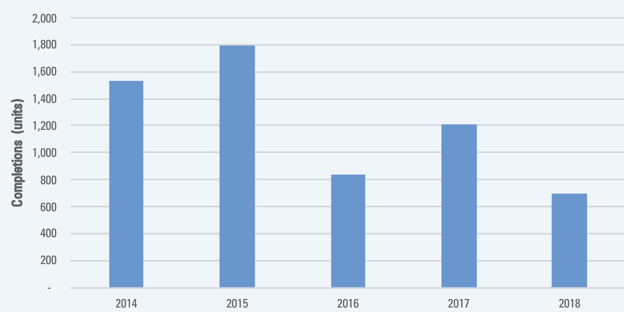
Sources: NorthMarq, Reis

Asking rents ended the fourth quarter up 4.4 percent from one year ago

Development and Permitting

- Projects totaling approximately 700 apartment units delivered in 2018, down from more than 1,200 units that came online in 2017. This marked the lowest level of new multifamily development since 2013.
- Apartment construction is gaining momentum, with more than 3,300 units currently under construction in the Inland Empire. The bulk of these projects are forecast to be delivered in 2019.
- Permitting activity slowed in the fourth quarter. Permits for fewer than 600 multifamily units were pulled in the final three months of the year, bringing the total for 2018 to approximately 3,000 permits, a dip of 10 percent from 2017.
- **Forecast:** Following a lull in deliveries in 2018, apartment construction will accelerate this year. Developers are expected to bring approximately 2,500 new apartments to the Inland Empire in 2019.

Development Trends



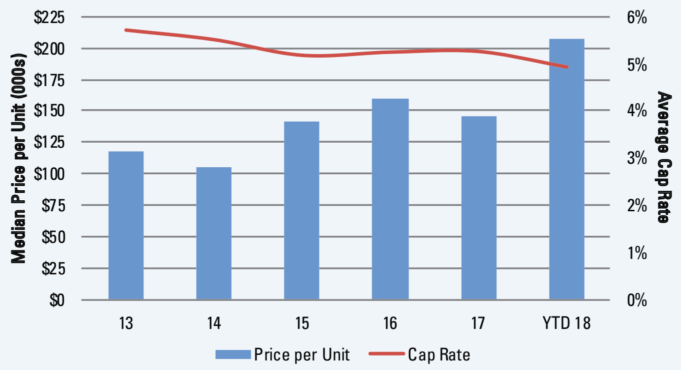
Sources: NorthMarq, Reis

Permitting activity slowed in the fourth quarter

Multifamily Sales

- Sales velocity accelerated to close 2018. Sales in the fourth quarter doubled the number of transactions from the third quarter, and the number of deals in the final three months of the year accounted for half of the total for all of 2018. The number of properties that sold in 2018 was up 11 percent from the preceding year.
- Prices rose at the end of the year, with the median price reaching $226,000 per unit in the fourth quarter. The median price for the full year rose by more than 40 percent from 2017, reaching $208,000 per unit.
- Cap rates averaged 4.9 percent in the fourth quarter, and that was the average for the year as well. Cap rates declined by about 40 basis points on average in 2018.

Investment Trends



Sources: NorthMarq, CoStar

Sales in the fourth quarter doubled the number of transactions from the third quarter

Recent Transactions in the Market

MULTIFAMILY SALES ACTIVITY

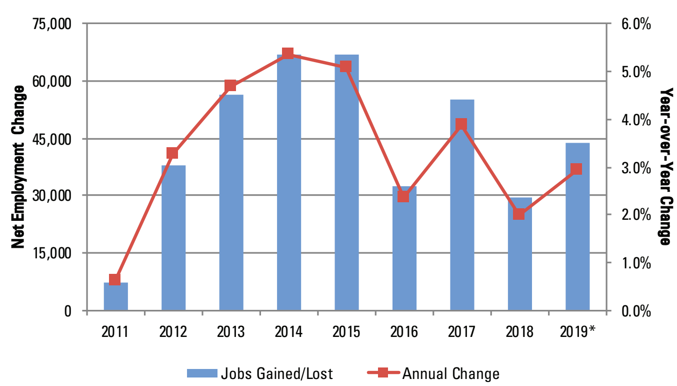
Property Name	Street Address	Units	Sales Price	Price/Unit
Parkview Terrace	1601 Barton Rd., Redlands	558	$130,600,000	$234,050
Capriana at Chino Hills	16301 Butterfield Ranch Rd., Chino Hills	286	$95,500,000	$333,916
Solana Ridge	41754 Margarita Rd., Temecula	312	$90,000,000	$288,462
Sierra Heights	10801 Lemon Ave., Alta Loma	265	$76,500,000	$288,679
Alvista Canyons	600 Central Ave., Riverside	288	$63,100,000	$219,097
The Benson	850 N Benson Ave., Upland	235	$48,900,000	$208,085

Looking Ahead

The Inland Empire is expected to be one of the highest-growth areas in California and in the United States again in 2019, supporting the local apartment market. Renter demand for units will likely top the 2018 total, although the vacancy rate should inch higher in response to an accelerating pace of new construction. Rises in development are common in high-growth/high-demand markets such as the Inland Empire and do not present any kind of sustained threat to the overall health of the market.

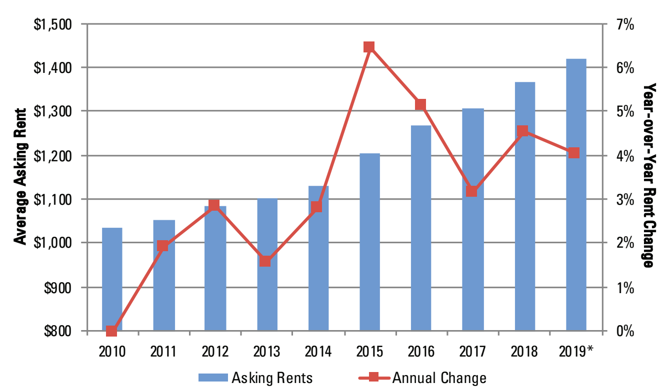
Investment activity in the Inland Empire is expected to have a slightly slower start in 2019, repeating the trend that occurred in 2018. This is the likely result of the surge in activity that occurred at the close of 2018, leaving fewer properties available for acquisition at the beginning of the following year. Activity should gain momentum in the second half of 2019. With rents continuing to push higher and interest rates coming down slightly, cap rates should remain near current ranges, and per-unit prices could push higher.

Employee Forecast



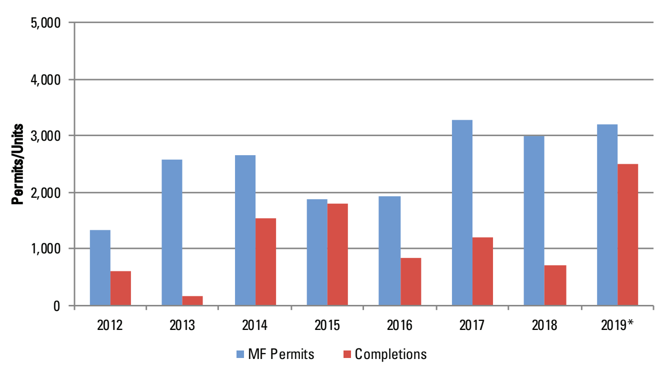
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



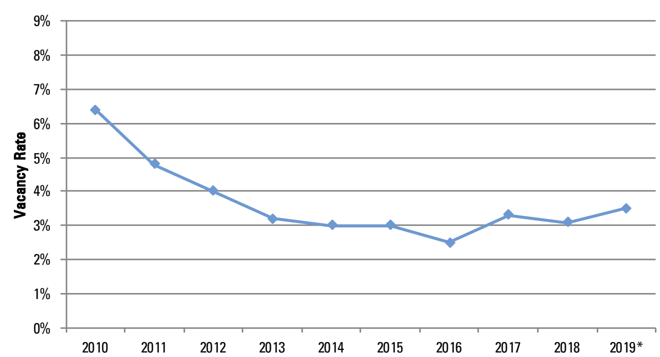
* Year End Forecast
Sources: NorthMarq, Reis

Construction & Permitting Forecast



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

Vacancy Forecast



* Year End Forecast
Sources: NorthMarq, Reis

About NorthMarq

As a capital markets leader, NorthMarq offers commercial real estate investors access to experts in debt, equity, investment sales, and loan servicing to protect and add value to their assets. For capital sources, we offer partnership and financial acumen that support long- and short-term investment goals. Our culture of integrity and innovation is evident in our 60-year history, annual transaction volume of $13 billion, loan servicing portfolio of more than $55 billion and the multi-year tenure of our more than 500 people.

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