MARKET REPORT | 4Q/2018

Orange County Multifamily

NORTHMARQ

Prices Rise, Cap Rates Compress to Close 2018

Highlights

- The Orange County multifamily market ended 2018 with strong market conditions. Absorption has been active, allowing vacancy to remain flat for the past few quarters despite heightened levels of new construction.
- Vacancy was 4 percent in both the third quarter and in the fourth quarter. The vacancy rate rose 20 basis points in 2018.
- Rents rose to close the year. Asking rents pushed up 3.5 percent in 2018, reaching $1,948 per month. Annual rent growth has averaged 3.6 percent since 2014.
- Transaction velocity was flat from the third quarter to the fourth quarter, but dollar volume spiked as larger properties changed hands. The median price in the fourth quarter was $374,300 per unit. For the year, the median price was $339,700 per unit, and cap rates averaged 4 percent.

Orange County Multifamily Market Overview

The Orange County multifamily market was marked by both strong renter demand and healthy supply growth in 2018. These trends persisted during the fourth quarter, holding the vacancy rate flat. While supply and demand trends were positive in 2018, the larger economy cooled. Employment growth in Orange County had averaged nearly 40,000 new jobs annually from 2012 to 2017, but a weak fourth quarter caused the local labor market to record net job losses for 2018. While growth has stalled in a few segments of the economy, a few of the core industries—led by leisure and hospitality—in Orange County expanded at healthy paces in 2018, and more widespread additions are likely in 2019.

Market Indicators

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

Summary Statistics — Orange County Market

Vacancy Rate	4.0%
- Change from 4Q 2017 (bps)	+20
Asking Rents (per month)	$1,948
- Change from 4Q 2017	+3.5%
Median Sales Price (per unit YTD)	$339,700
Average Cap Rate (YTD)	4.0%

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Orange County Multifamily Market Overview (cont.)

Investment for multifamily properties in Orange County slowed in the second half of 2018, but prices rose and cap rates compressed, highlighting the strength of demand for the modest supply of properties available for acquisition. While the number of transactions was flat from the third quarter to the fourth quarter, dollar volume increased significantly as more units sold and per-unit prices spiked. The median price reached an all-time high in 2018, approaching $340,000 per unit. As prices rose, cap rates compressed and averaged approximately 4 percent in 2018.

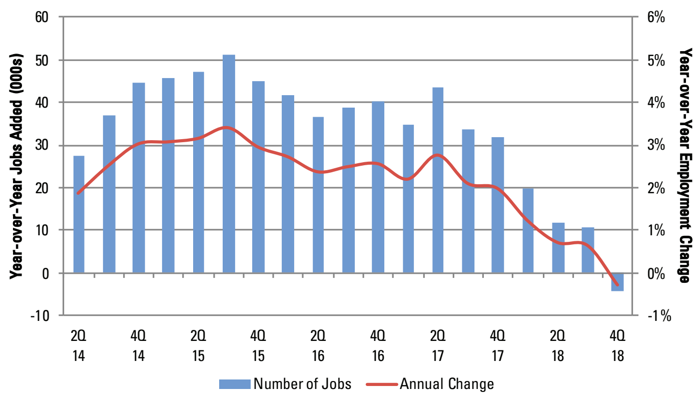
Submarket Statistics

Submarket Name	4Q 2018 Vacancy	4Q 2017 Vacancy	Annual Vacancy Change (BPS)	4Q 2018 Rents	4Q 2017 Rents
Buena Park	1.6%	1.9%	(30)	$1,557	$1,514
Orange	2.1%	2.0%	10	$1,922	$1,861
Costa Mesa	2.3%	2.2%	10	$1,887	$1,910
Tustin	2.3%	2.4%	(10)	$1,978	$1,881
Westminster/Fountain Valley	2.4%	2.3%	10	$1,602	$1,555
Placentia/Northeast Anaheim	2.6%	2.7%	(10)	$1,495	$1,483
North Anaheim	3.0%	2.8%	20	$1,489	$1,459
Laguna Beach/Dana Point	3.1%	3.5%	(40)	$2,021	$1,992
Fullerton	3.7%	4.0%	(30)	$1,628	$1,587
Huntington Beach	4.0%	4.1%	(10)	$1,954	$1,754
Mission Viejo	4.0%	3.3%	70	$1,911	$1,859
Newport Beach	4.1%	5.0%	(90)	$2,787	$2,748
South Santa Ana	4.9%	3.8%	110	$1,970	$1,932
Brea	5.1%	3.4%	170	$1,747	$1,655
North Santa Ana	5.1%	3.2%	190	$1,612	$1,504
Laguna Hills	5.2%	7.1%	(190)	$2,011	$1,975
Irvine	6.2%	5.5%	70	$2,578	$2,476
South Anaheim	6.2%	6.9%	(70)	$1,817	$1,776

Employment

- Employment in Orange County slowed in the fourth quarter. Total employment in Orange County contracted by 0.3 percent in 2018 with net losses of 4,300 jobs. This followed a four-year run of strong growth, where an average of more than 40,000 jobs were added annually.
- The leisure and hospitality sector plays a prominent role in the local economy. The sector expanded by 3.2 percent in 2018 with the addition of 7,100 workers.
- The healthcare and social assistance sector has been expanding at a rapid pace. In 2018, approximately 5,000 jobs were added in this sector, a growth rate of 2.6 percent.
- **Forecast:** After a decline in 2018, businesses are expected to return to expansion mode in the year to come. Employers are forecast to add approximately 17,000 jobs in 2019, for growth of 1 percent.

Employment Overview



Sources: NorthMarq, Bureau of Labor Statistics

Total employment in Orange County contracted by 0.3 percent in 2018

Vacancy

- The Orange County multifamily vacancy rate held steady at 4 percent in the final three quarters of 2018 after inching higher at the beginning of the year. The rate crept up 20 basis points in 2018.
- Vacancy in Class A units inched up 10 basis points in the fourth quarter, reaching 5.2 percent. The Class A vacancy rate crept up 20 basis points due to the delivery of nearly 4,000 new units in 2018.
- While vacancy has crept higher in recent years, net absorption of units has remained positive. During the fourth quarter, net absorption totaled nearly 1,000 units, and for the full year, renters moved into a net of nearly 3,400 units.
- **Forecast:** Vacancy is forecast to tick higher in 2019, with the rate expected to end the year at approximately 4.2 percent.

Vacancy Trends

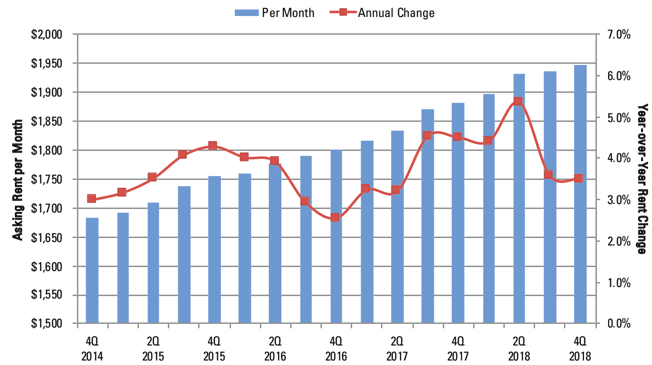
Sources: NorthMarq, Reis

While vacancy has crept higher in recent years, net absorption of units has remained positive

Rents

- Asking rents pushed higher in the fourth quarter, ending the year at $1,948 per month. Rents rose 3.5 percent in 2018, following a gain of 4.5 percent in the preceding year.
- Rents in Laguna Hills topped $2,000 per month during the fourth quarter, joining three other submarkets where rents have exceeded this figure. Asking rents in the Laguna Hills submarket rose 1.8 percent in 2018 to $2,011 per month.
- Rent growth was strongest in Class A properties, where asking rents advanced 3.7 percent in 2018 to $2,258 per month. Asking rents in Class A properties have increased at an average rate of 3.5 percent annually during the past five years.
- **Forecast:** Asking rent growth in Orange County is forecast to total approximately 3.5 percent again in 2019, ending the year at more than $2,000 per month.

Rent Trends



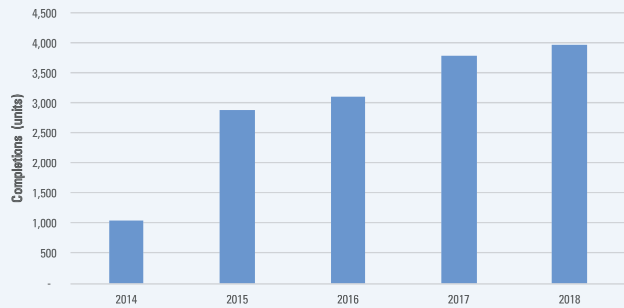
Sources: NorthMarq, Reis

Rent growth was strongest in Class A properties

Development and Permitting

- Construction of new apartments has been particularly active in Orange County in recent years. In 2018, approximately 4,000 units were delivered, the highest annual total in more than 20 years. Since 2015, completions have averaged more than 3,400 units per year.
- Projects totaling more than 4,600 units are currently under construction, with the bulk of these projects scheduled to deliver in 2019.
- Approximately 750 units are under construction in the South Anaheim submarket. In 2018, more than 950 new apartments were delivered in this submarket, the third straight year of active construction.
- **Forecast:** The year ahead is expected to be an active one for multifamily construction. Projects totaling approximately 4,000 apartments are forecast to come online in 2019.

Development Trends



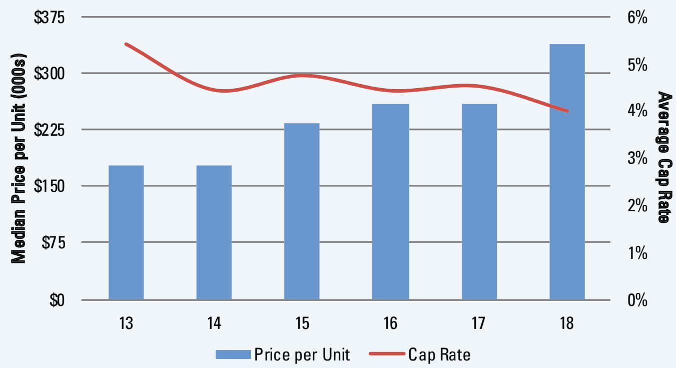
Sources: NorthMarq, Reis

Projects totaling more than 4,600 units are currently under construction

Multifamily Sales

- The number of multifamily sales in the fourth quarter was nearly identical to activity in the third quarter, but activity in the second half of the year was down about 30 percent from the first half. Sales velocity in 2018 was down 13 percent from 2017 levels.
- Prices rose throughout 2018, peaking at the end of the year. The median price in sales during the fourth quarter was $374,300 per unit. For the full year, the median price was $339,700 per unit, an increase of more than 30 percent from the preceding year.
- Cap rates compressed in 2018, averaging approximately 4 percent in 2018. Most transactions closed with cap rates in the mid-3 percent to mid-4 percent range.

Investment Trends



Prices rose throughout 2018, peaking at the end of the year

Recent Transactions in the Market

MULTIFAMILY SALES ACTIVITY

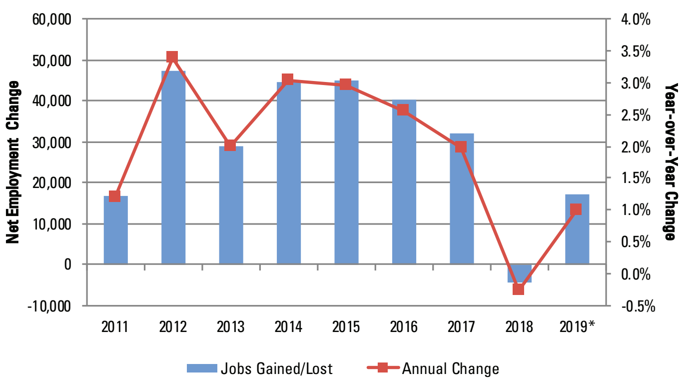
Property Name	Street Address	Units	Sales Price	Price/Unit
Seacrest	240 Avenida Vista Montana	368	$137,730,000	$374,266
Fusion	17321 Murphy Ave., Irvine	280	$118,500,000	$423,214
Rancho Del Mar	1100 Calle Del Cerro, San Clemente	250	$92,600,000	$370,400
Dover Heights	1630 Bedford Ln., Newport Beach	60	$30,554,000	$509,233
Cypress Village	6343 Lincoln Ave., Buena Park	88	$28,850,000	$327,841

Looking Ahead

The Orange County multifamily market is positioned for another steady year of property performance in 2019. Apartment fundamentals remained healthy in 2018, overcoming a modest economic drag caused by net job losses in Orange County. In 2019, job growth is forecast to turn in a positive direction, which should provide a bit of a spark to renter demand for apartments. On the supply side, 2019 should mark another year of active construction. Approximately 4,000 apartment projects are scheduled to come online, marking the fifth consecutive year of above-average inventory growth.

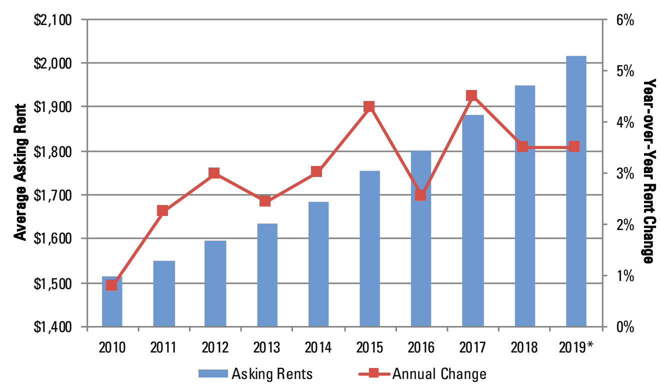
Investor demand for multifamily properties is expected to remain elevated in the year ahead. Prices for apartments spiked in 2018 and cap rates compressed, highlighting the competitive investment environment present in the market. The investment climate should remain healthy going forward, as the market has demonstrated an ability to absorb the new units coming online and rents have continued to trend higher. Cap rates will likely remain low after averaging just 4 percent in 2018. Cap rates have compressed in each of the past few years, but a dip below 4 percent on average seems unlikely.

Employee Forecast



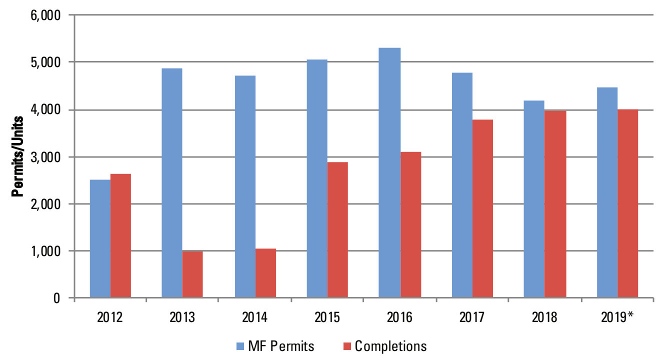
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



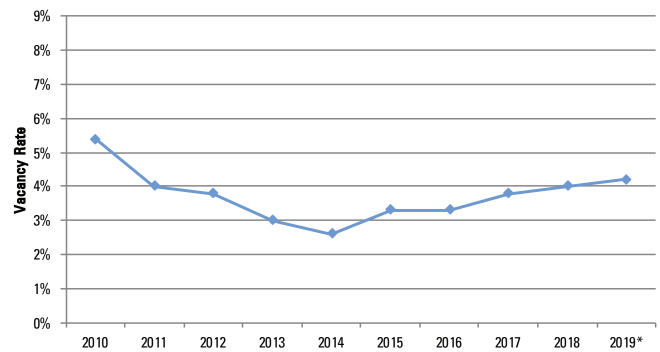
* Year End Forecast
Sources: NorthMarq, Reis

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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