MARKET REPORT | 3Q/2019

San Diego Multifamily

NorthMarq

Job Growth Fueling Absorption of New Units

Highlights

- The San Diego multifamily market continues to post strong performance. The market is proving it can absorb the new inventory that has been delivered in recent years, keeping overall vacancy low.
- Vacancy held steady at 3.8 percent, and the rate has dropped 10 basis points year over year. Vacancy in Class B and Class C units averages just 2.2 percent.
- Current asking rents are $1,878 per month, 3.8 percent higher than one year ago. Rents have trended higher at a fairly steady pace since 2016.
- The favorable market performance supported investment sales activity in recent quarters. Year-to-date sales velocity has mirrored levels from 2018, while prices have pushed higher and cap rates have remained flat.

Q3 Snapshot	San Diego Market
Market Fundamentals	
Vacancy	**3.8%**
- Year Over Year Change	**-10 bps**
Asking Rent	**$1,878**
- Year Over Year Change	**+3.8%**
Transaction Activity	
Median Sales Price Per Unit (YTD)	**$270,900**
Cap Rates (Avg YTD)	**4.5%**
Construction Activity	
Units Under Construction	**4,007**
Units Delivered YTD	**2,155**

San Diego Multifamily Market Overview

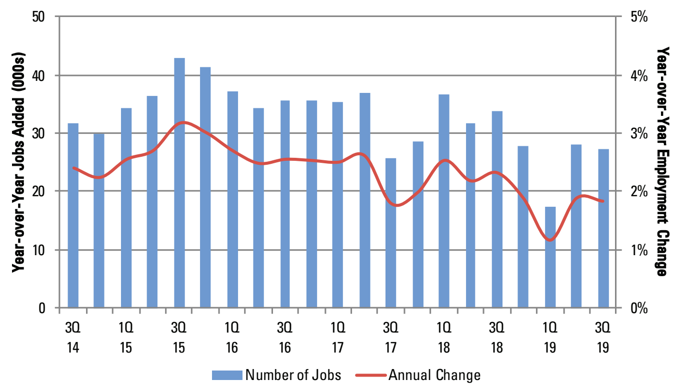
The San Diego multifamily market is posting some of the steadiest operating results in the country, with vacancy remaining in a consistently tight range and rents posting repeated increases. While construction of new units has accelerated since the beginning of 2018, demand has also gained momentum, fueled by a healthy pace of new job growth. Absorption of apartments is forecast to remain elevated, allowing for continued operational health in the local multifamily market.

Investment activity accelerated during the third quarter, after a slower start to the year, and sales velocity continued into the fourth quarter. Activity levels for 2019 were on pace to closely track levels from the preceding year. Prices rose, and the average deal size spiked by approximately 20 percent in 2019. Cap rates have remained fairly steady from 2018 to 2019, averaging approximately 4.5 percent, although some properties are trading with cap rates below 4 percent.

Employment

- After a spike in the second quarter, the pace of job growth in San Diego cooled slightly in the third quarter. Year over year through the third quarter, total employment in San Diego is up 1.8 percent, with the addition of 27,400 net new jobs.
- Construction employment in San Diego is expanding at one of the fastest rates in Southern California. During the past 12 months, employers have added more than 5,000 construction positions, a 6.3 percent expansion.
- The professional and business services sector continues to expand, although gains in professional jobs have been a bit slower this year than in previous years. Growth in the 12-month period ending in the third quarter totaled 7,700 positions, down from an expansion of 9,400 jobs one year earlier.
- Fueled by strong growth in the construction sector, total employment in San Diego is on pace to expand 2.1 percent in 2019, with the addition of 32,000 net new jobs.

Employment Overview



Sources: NorthMarq, Bureau of Labor Statistics

Construction employment in San Diego is expanding at one of the fastest rates in Southern California

Vacancy

- After inching lower in the second quarter, apartment vacancy in San Diego held steady at 3.8 percent in the third quarter. The rate has remained between 3.7 percent and 4.0 percent since the beginning of 2018.
- Vacancy has improved 10 basis points during the past 12 months, as the net absorption of units has outpaced the previous 12-month period by approximately 4 percent.
- Vacancy in Class A units is above the market average, reaching 5.8 percent as of the third quarter. In Class B and Class C units, conditions are consistently tight, with the vacancy rate generally in the low-2-percent range.
- The local vacancy rate was forecast to end 2019 at 3.9 percent, 10 basis points lower than one year earlier. Vacancy in the market has generally ranged between 3 percent and 4 percent since 2015.

Vacancy Trends

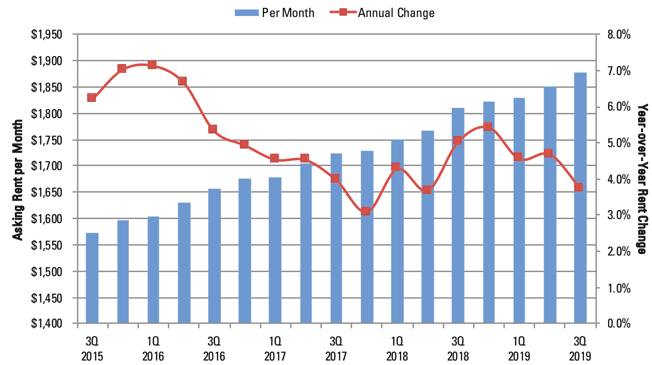
Sources: NorthMarq, Reis

Vacancy has improved 10 basis points during the past 12 months, fueled by a rise in absorption

Rents

- Asking rents in San Diego rose 1.5 percent during the third quarter, building on a 1.1 percent increase in the preceding three months. This was the strongest quarter of rent growth since the third quarter of last year.
- During the past 12 months, local asking rents have advanced 3.8 percent, ending the third quarter at $1,878 per month. One year ago, annual rent growth in the area was 5 percent.
- Class A asking rents ended the third quarter at $2,300 per month, 3.6 percent higher than one year earlier. Class A asking rents have been rising at an annual rate of approximately $100 per month.
- Annual rent growth in 2019 was estimated to total approximately 4.3 percent, with asking rents reaching $1,900 per month.

Rent Trends



Sources: NorthMarq, Reis

Asking rents rose 1.5 percent during the third quarter, building on a 1.1 percent increase from the preceding quarter

Development and Permitting

- Developers delivered 1,100 apartment units in San Diego during the third quarter, bringing the total for the year to more than 2,100 units. Through the first three quarters of the year, completions in 2019 are down 33 percent when compared to 2018 levels.
- The development pipeline has thinned slightly in recent quarters as projects have been delivered. Approximately 4,000 units are currently under construction, down nearly 20 percent from one quarter ago.
- Permits for approximately 1,450 multifamily units were pulled during the third quarter, doubling the total from the third quarter of last year. Year to date, developers have pulled permits for nearly 3,800 multifamily units.
- Multifamily developers were expected to deliver approximately 4,000 apartment units in 2019, a slight increase from the 2018 total.

Development Trends

Sources: NorthMarq, Reis

The development pipeline has thinned slightly as projects have been delivered

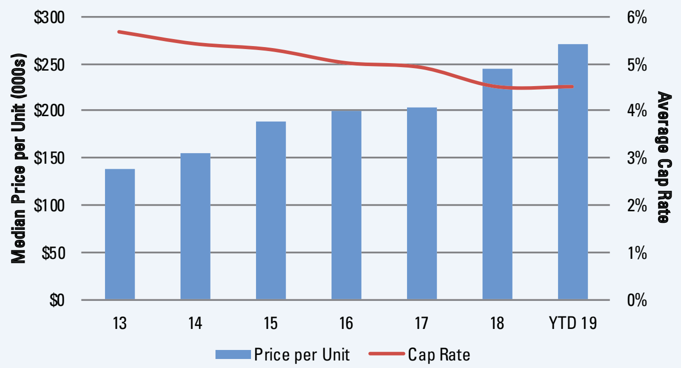
Multifamily Sales

> Transaction activity gained momentum during the third quarter, doubling the number of sales from the second quarter. Activity levels from the first three quarters of the year were nearly identical from the same period in 2018.

> Prices rose during the third quarter, bringing the median price for the first nine months of the year to $270,900 per unit.

> Cap rates have averaged approximately 4.5 percent in 2019, with a handful of properties trading with cap rates below 4 percent. On average, cap rates in 2019 are nearly identical to cap rates from 2018.

Investment Trends



Sources: NorthMarq, CoStar

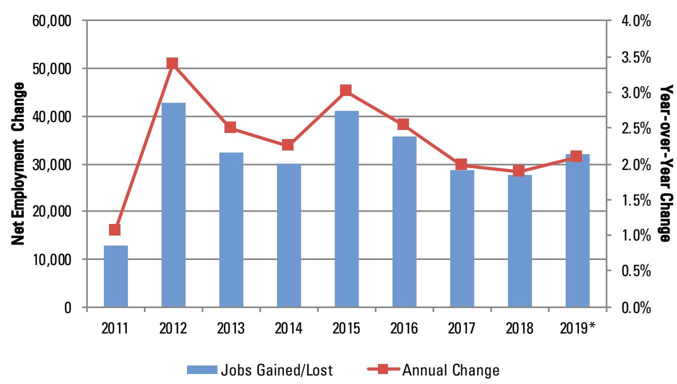
Transaction activity gained momentum during the third quarter

Looking Ahead

The San Diego multifamily market is expected to continue to post strong performance. Beginning in 2020, the market will benefit from a slower pace of new multifamily development. While net absorption of units has been healthy in recent years, an accelerated rate of supply growth has prevented the vacancy rate from tightening, particularly in the Class A segment. With deliveries in the year ahead anticipated to slow by nearly half the 2018-2019 levels, vacancy is forecast to dip and rent growth could gain momentum.

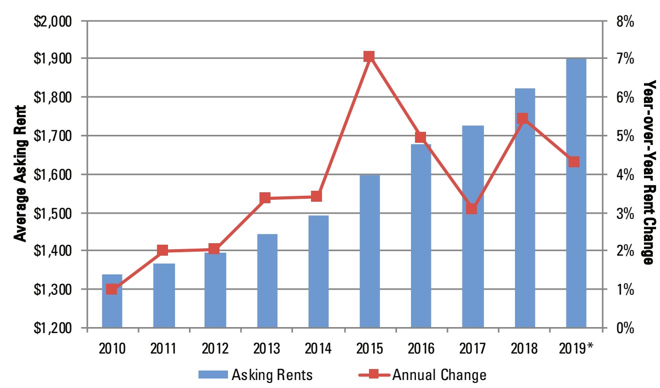
The investment market has performed at a steady pace over the past several years, a trend that is likely to repeat in the year to come. The supply of properties available for sale is generally limited, and demand for those properties that become available is strong. This will continue to keep cap rates low, especially if interest rates remain near their current ranges. The passage of rent control legislation in California is not expected to slow transactions, as the allowed rate of growth of 5 percent plus inflation will allow for healthy rent increases.

Employment Forecast



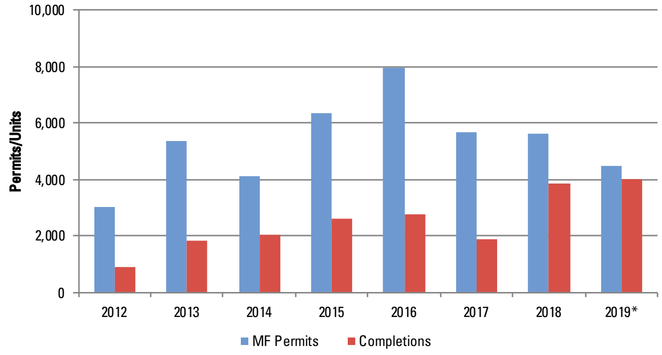
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



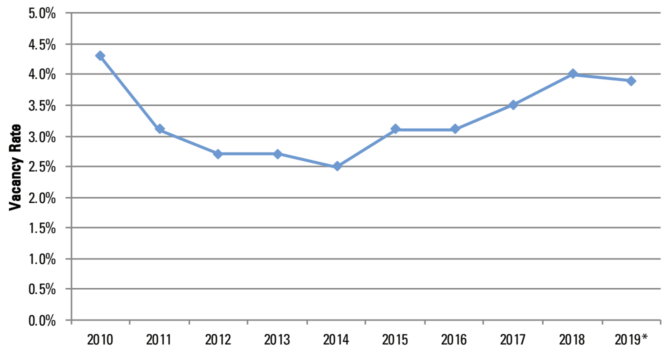
* Year End Forecast
Sources: NorthMarq, Reis

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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