MARKET REPORT | 4Q/2020

Orange County Multifamily

Investors Close a Wave of Deals to End 2020

Highlights

> The Orange County multifamily market delivered a mixed performance in 2020. Asking rents registered their first decline since 2009, while vacancy was stable as apartment demand stayed resilient.

> The local vacancy rate was steady throughout the year, finishing 2020 at 3.7 percent, unchanged from 2019.

> After briefly surpassing $2,000 per month in the first quarter, rents dipped during the remainder of the year. During 2020, apartment rents contracted 2.3 percent to $1,954 per month; most of the decline occurred in the third quarter.

> The investment market in Orange County was limited for the majority of 2020 by COVID-19. Things shifted at the end of the year, and the fourth quarter was the most active period since the first quarter of 2017. Sales prices and cap rates held relatively consistent to figures from 2019.

Q4 Snapshot	Orange County Market
Market Fundamentals	
Vacancy	**3.7%**
- *Year Over Year Change*	**0 bps**
Asking Rent	**$1,954**
- *Year Over Year Change*	**-2.3%**
Transaction Activity	
Median Sales Price Per Unit (YTD)	**$309,400**
Cap Rates (Avg YTD)	**4.0%**
Construction Activity	
Units Under Construction	**4,384**
Units Delivered YTD	**1,928**

Orange County Multifamily Market Overview

The Orange County local multifamily market maintained tight vacancy conditions in 2020, although rents dipped as operators focused on tenant retention. The local labor market softened in 2020, but performance varied. Orange County's large, high-wage professional and financial sectors recorded modest softening and will likely bounce back quickly when the economy more fully reopens. The parts of the economy that are more dependent on travel and tourism—including leisure/hospitality and retail—suffered steeper losses. These industries present the greatest upside potential for 2021, especially if vaccination efforts gain momentum, the area's popular attractions resume operations, and leisure travel resumes.

Multifamily sales activity was minimal throughout the first nine months of 2020, but transactions picked up significantly in the fourth quarter. The spike in transactions at the end of the year brought sales activity in 2020 to very closely resemble investment trends from 2019, highlighting the stability of investor demand for rental properties in Orange County. Pricing in 2020 closely tracked figures from 2019, and cap rates of approximately 4 percent were nearly identical. Active submarkets for transactions in 2020 included Anaheim and Santa Ana, similar to where activity was concentrated in 2019.

Employment

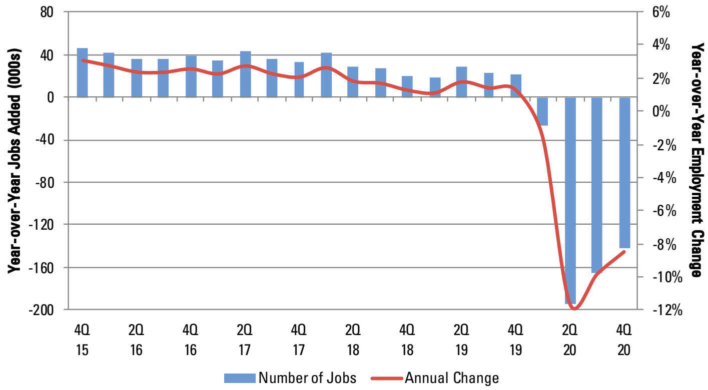
> Employers added approximately 27,000 net jobs during the fourth quarter, building on a similar gain during the third quarter. Year over year, employment in Orange County contracted 8.5 percent, with the loss of roughly 142,000 net jobs.

> Local construction employment expanded in 2020, despite turbulence in the larger economy. Construction employment grew 1.8 percent in 2020 with the addition of nearly 2,000 jobs, the only sector in Orange County to record an annual gain during the year.

> Disneyland, Orange County's single-largest employer, recently announced plans to launch a limited-time dining experience around mid-March, bringing back roughly 1,000 local workers. The new event will operate multiple days a week with limited capacity. A broader reopening of the park would support local employment, but a schedule for that has not been announced.

> **Forecast:** After significant layoffs in 2020, a more robust rebound is forecast for 2021, especially during the second half. In 2021, employment in Orange County is forecast to advance 3.2 percent, with the addition of nearly 50,000 net new jobs.

Employment Overview



Sources: NorthMarq, Bureau of Labor Statistics

Employers added approximately 27,000 net jobs during the fourth quarter, building on a similar gain during the third quarter

Vacancy

> Apartment vacancy was stable throughout much of 2020, although the rate inched higher at the end of the year. Vacancy ticked up 10 basis points from the third quarter to the fourth quarter, reaching 3.7 percent.

> Renter demand closely tracked apartment construction in 2020, and the local vacancy rate was unchanged from the end of 2019. The current vacancy rate is down 30 basis points from two years ago.

> There are several high-demand areas in Orange County with a vacancy rate below 2 percent. Submarkets with the lowest vacancy rates include Buena Park, Costa Mesa, and Tustin.

> **Forecast:** Apartment demand is expected to outpace the rate of new construction in 2021, pushing the vacancy rate lower. The rate is forecast to decline 20 basis points, reaching 3.5 percent by the end of the year.

Vacancy Trends

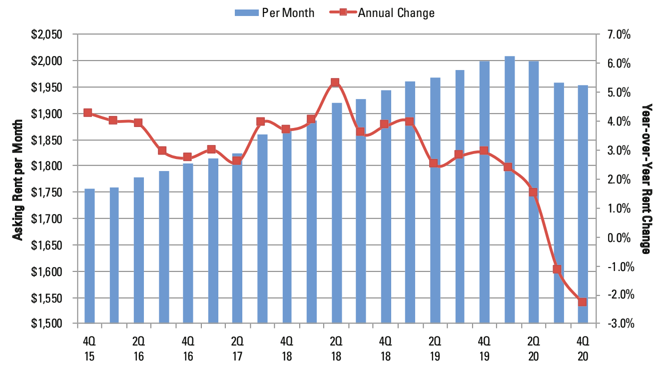
Sources: NorthMarq, Reis

Renter demand closely tracked apartment construction in 2020

Rents

- After a sharp pullback in the third quarter, rents recorded a minimal dip in the fourth quarter. Apartment rents decreased just 0.2 percent from the third quarter, finishing 2020 at $1,954 per month.
- Year over year, local asking rents contracted 2.3 percent. Before this year's loss, rents in Orange County had been on an extended upswing, increasing at an average rate of 3 percent per year since 2010.
- The Laguna Beach/Dana Point submarket was one of the few areas in Orange County where rents gained ground in 2020. Asking rents in the submarket expanded 2.6 percent year over year to $2,237 per month. Even after the recent increase, rents in the submarket are still 12 percent lower than in neighboring Newport Beach.
- **Forecast:** Rents in Orange County are expected to resume growth in 2021. Asking rents are forecast to rise approximately 2.5 percent, with rents ticking up above $2,000 per month by year end.

Rent Trends



Sources: NorthMarq, Reis

Rents in Orange County are expected to resume growth in 2021

Development and Permitting

- After peaking in 2018 with 4,250 units delivered, apartment construction has declined in the consecutive years. In 2020, developers brought more than 1,900 units online, down 18 percent from 2019.
- The number of units that are in the development pipeline has been on the rise in recent quarters. Projects totaling nearly 4,400 multifamily units are currently under construction, up more than 50 percent from one year earlier.
- Irvine has been one of the fastest-growing cities in Orange County, and developers remain active in the area to meet demand. The Irvine submarket accounts for more than 60 percent of the ongoing construction, and approximately 2,750 multifamily units are under construction in the city.
- **Forecast:** Apartment deliveries are forecast to slow for the third consecutive year in 2021. Developers are forecast to bring nearly 1,700 multifamily units to the market in the next year. From 2016 to 2019, apartment deliveries averaged roughly 3,900 units per year.

Development Trends

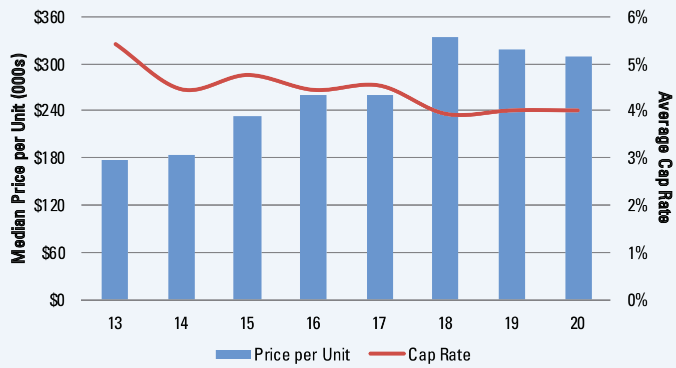
Sources: NorthMarq, Reis

Developers brought more than 1,900 apartment units online in 2020

Multifamily Sales

- After minimal transaction activity in the first three quarters of the year, the number of properties changing hands more than tripled at the end of the year. With the late activity surge, sales velocity in 2020 nearly matched the figure from 2019.
- The median sales price in deals recorded during 2020 was $309,400 per unit, down just 3 percent from 2019.
- Pricing varies significantly by building class. In Class A properties that sold in 2020, the median price exceeded $450,000 per unit. The median price in Class B sales was approximately $330,000 per unit, and in older, Class C properties, the median was $272,000 per unit.
- Cap rates in Orange County held steady from 2019 to 2020, averaging 4 percent each year.

Investment Trends



Sources: NorthMarq, CoStar

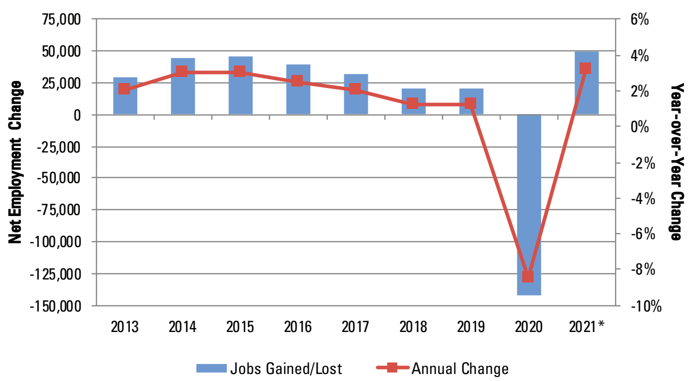
In Class A properties that sold in 2020, the median price exceeded $450,000 per unit

Looking Ahead

The Orange County multifamily market is forecast to strengthen in 2021, after posting mostly steady performance during a tumultuous year in 2020. Deliveries of new units should slow in the coming years, and demand should receive a boost as the economy normalizes. With supply growth in check, vacancy is forecast to tighten and rents should rise. Property performance is expected to be strongest in the second half of the year, particularly if the economy has opened enough for increased visitor volume for the summer travel season.

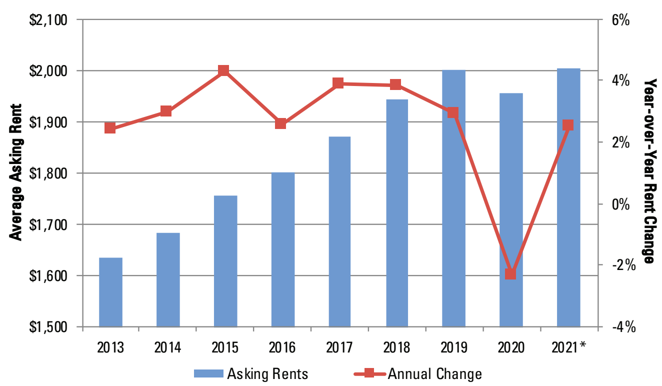
The investment trends that have prevailed in recent years should repeat again in 2021. Investors returned to the market late in 2020, and a handful of properties have already traded in the first few weeks of 2021. Cap rates have averaged around 4 percent in each of the last three years and are not likely to move significantly off of that average unless interest rates were to rise unexpectedly. Only a few of the recently completed apartment complexes have sold to this point, but activity will likely pick up in that segment of the market as properties are leased up.

Employment Forecast



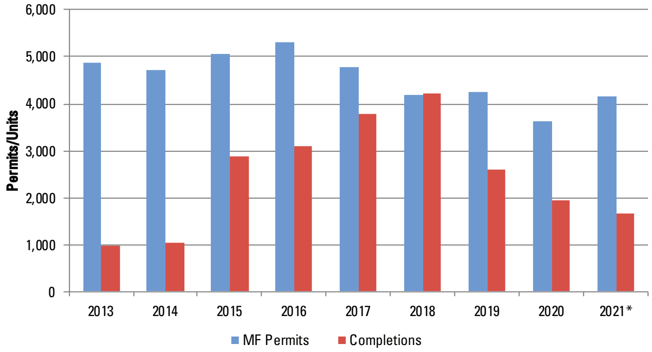
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



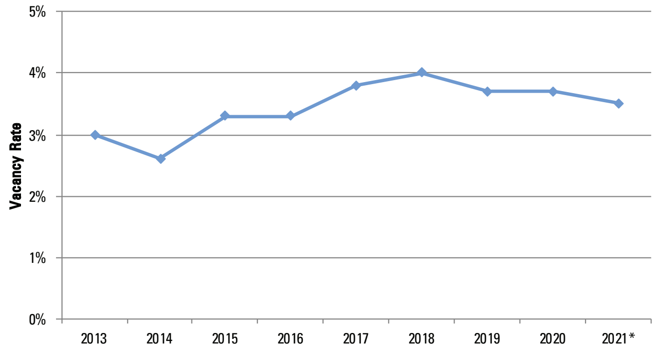
* Year End Forecast
Sources: NorthMarq, Reis

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 $14 billion, loan servicing portfolio of more than $61 billion and the multi-year tenure of our nearly 600 people.

For more information, contact:

Shane Shafer
SVP, MANAGING DIRECTOR – INVESTMENT SALES
949.270.3690
sshafer@northmarq.com

Kyle Pinkalla
MANAGING DIRECTOR – INVESTMENT SALES
858.675.7865
kpinkalla@northmarq.com

Michael Elmore
EVP, MANAGING DIRECTOR – DEBT & EQUITY
949.717.5213
melmore@northmarq.com

Pete O'Neil
DIRECTOR OF RESEARCH
602.508.2212
poneil@northmarq.com

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