

San Diego Multifamily




Employment Outlook Strengthens as Apple Announces Expansion

Highlights

- > The San Diego multifamily market proved fairly resilient in the opening quarter of 2021. Apartment rents held steady following several months of modest declines, while the vacancy rate inched higher.
- > Vacancy rose 10 basis points from the fourth quarter to the first quarter, finishing the period at 4.1 percent. Several submarkets where rents are lower and new development has been limited have vacancy rates under 2.5 percent.
- > After trending lower in the final three months of 2020, rents were essentially flat during the first quarter. Asking rents ended the quarter at \$1,859 per month. Year over year, asking rents are down 1.9 percent.
- > Sales of apartment properties in San Diego got off to a healthy start in 2021. Sales velocity was ahead of last year's pace, and cap rates compressed to just 3.9 percent, while the median price dipped to \$256,500 per unit as more Class C properties sold.

San Diego Multifamily Market Overview

The San Diego multifamily market was mostly stable at the beginning of 2021. The vacancy rate recorded a minimal uptick, while rents stabilized after ticking lower for much of 2020. One factor fueling the stable property performance in the first quarter was a break in new development. No significant new projects were delivered at the start of the year, although several projects are scheduled to come online through the remainder of 2021. Rent trends have been mixed, with rents creeping lower in the most expensive areas, but ticking higher in more affordable submarkets. The most noteworthy economic development from the beginning of 2021 was Apple's announcement to add 5,000 new jobs in the area over the next five years.

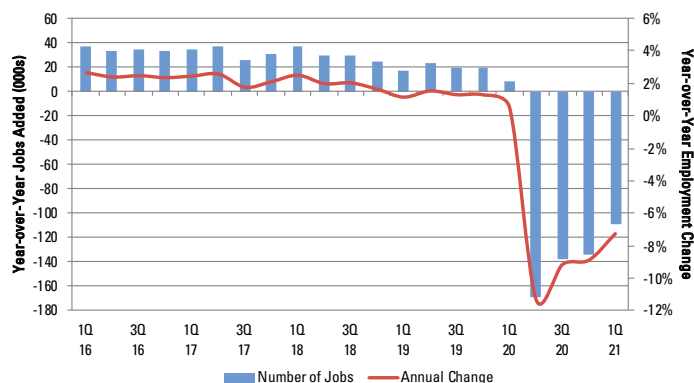
Q1 Snapshot	San Diego Market
	Market Fundamentals
	Vacancy 4.1%
	- Year Over Year Change +30 bps
	Asking Rent \$1,859
	- Year Over Year Change -1.9%
	Transaction Activity
	Median Sales Price Per Unit (YTD) \$256,500
	Cap Rates (Avg YTD) 3.9%
	Construction Activity
	Units Under Construction 5,087
	Units Delivered YTD 0

The investment market in San Diego started out 2021 in a stronger position than one year ago, with more properties changing hands. Sales velocity in the first quarter of this year was more active than in three of the four quarters in 2020, eclipsed only by the volume of transactions at the end of last year. While the bulk of the transactions that closed during the first quarter were older Class C properties, cap rates still compressed, dipping below 4 percent on average. Lower cap rates reflect the competitive investment landscape in the market, as well as expectations that property rents will trend higher as the local economy regains momentum this year.

Employment

- > The San Diego employment market is recovering slowly. During the first quarter, employers added 17,500 positions to payrolls, nearly doubling the gains recorded in the fourth quarter of last year. Despite the recent boost, local employment is still down 7.2 percent from one year ago.
- > San Diego's high-wage employment sectors have mostly recovered from the volatility recorded last year. Year over year through the first quarter, employment in the local professional and business services sector has crept higher by approximately 1,000 jobs.
- > Apple recently announced plans for a significant nationwide expansion, with San Diego being one of the markets that will grow considerably. Apple plans on expanding its current San Diego workforce of around 1,000 people to more than 5,000 workers by 2026.
- > **Forecast:** San Diego's labor market should continue to outperform as pent-up demand is anticipated to boost economic activity in the next few quarters, especially in the hardest-hit markets. Total employment is expected to expand 3.6 percent, with the hiring of around 50,000 workers.

Employment Overview



Sources: NorthMarq, Bureau of Labor Statistics

Apple plans on expanding its current San Diego workforce to more than 5,000 workers by 2026

Vacancy

- > Apartment vacancy inched higher in the first quarter, rising 10 basis points to 4.1 percent. Vacancy has recorded some moderate upward pressure since the beginning of 2020, but San Diego's vacancy rate remains one of the lowest in the country.
- > Year over year, vacancy in San Diego has increased 30 basis points. Renter demand for apartments has been mostly steady, and the modest rise in vacancy is largely the result of new supply coming online.
- > After spiking to over 10 percent during the pandemic, vacancy in Downtown San Diego has been improving in recent periods. The vacancy rate in the Downtown submarket has declined 120 basis points in the last two quarters and is currently 8.9 percent.
- > **Forecast:** Apartment construction is forecast to accelerate in the coming months, and the additions to inventory will likely outpace renter demand growth. Vacancy is forecast to rise 40 basis points in 2021, with the rate ending the year at 4.4 percent.

Vacancy Trends



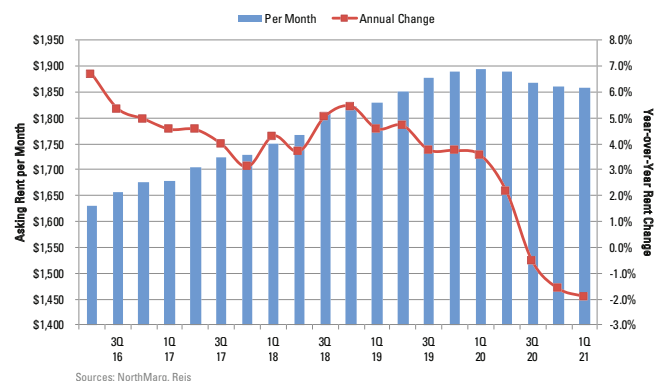
Sources: NorthMarq, Reis

Vacancy inched higher in the first quarter, rising 10 basis points to 4.1 percent

Rents

- > After contracting for three consecutive quarters, apartment rents in San Diego seem to have found a floor. Asking rents were essentially flat from the fourth quarter to the first quarter, ending the period at \$1,859 per month.
- > Local asking rents are down 1.9 percent in the last 12 months. After leveling off to start 2021, rents are forecast to creep higher as the economy expands in the upcoming quarters.
- > Rent declines have been most pronounced in the costlier areas of San Diego, consistent with nationwide trends. The La Jolla/University submarket has recorded the most significant rent drops; asking rents in the area retreated 9.7 percent year over year to \$2,282 per month.
- > **Forecast:** After steadying in the first quarter, rents are expected to trend higher throughout the rest of this year. Asking rents are forecast to advance approximately 2.5 percent in 2021, ending the year above \$1,900 per month.

Rent Trends

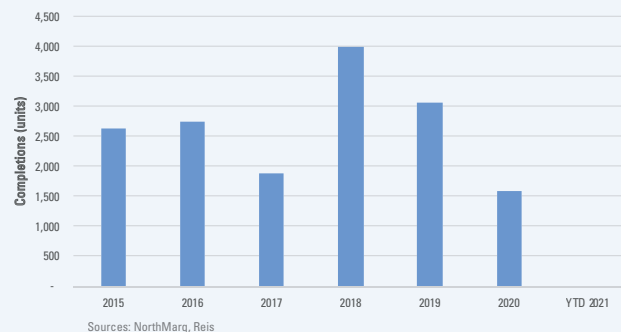


Asking rents were essentially flat from the fourth quarter to the first quarter, ending the period at \$1,859 per month

Development and Permitting

- > New multifamily construction has been tapering off in recent years after peaking in 2018 and 2019. During the first quarter, no significant new apartment projects came online, but deliveries are forecast to accelerate in the coming quarters.
- > Roughly 20 multifamily projects totaling nearly 5,100 units are currently under construction in San Diego. The Mission Valley area is a popular spot for new development, with more than 1,700 units expected to be delivered by the end of 2022. The Society is an 840-unit, four-building project that is scheduled to come online this year.
- > Multifamily permitting in San Diego strengthened at the end of 2020 and remained active to start this year. Developers pulled permits for nearly 1,800 multifamily units during the first quarter, up 82 percent from the same period in 2020.
- > **Forecast:** Apartment construction is forecast to ramp up through the remainder of 2021. Projects totaling more than 3,300 units are scheduled to be delivered this year, doubling the number of units that came online in 2020.

Development Trends

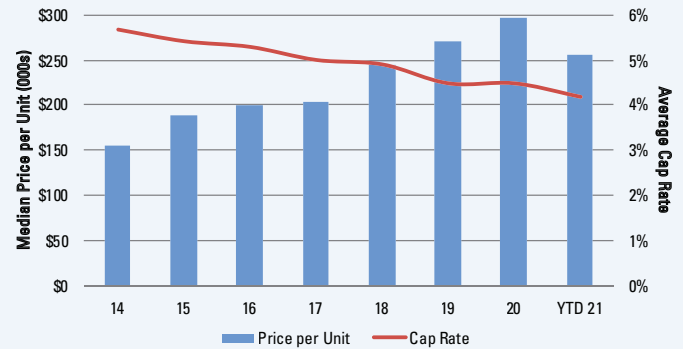


Multifamily projects totaling nearly 5,100 units are under construction in San Diego

Multifamily Sales

- > Investment activity got off to a strong start to 2021. Sales velocity during the first quarter was up 40 percent compared to levels from the same period, one year earlier.
- > The median price in sales during the first quarter of 2021 was approximately \$256,500 per unit, about 14 percent lower than the median price in 2020. Several of the transactions that closed at the beginning of the year were older Class C properties that traded at the lower end of the market's pricing range.
- > Cap rates dipped below 4 percent at the start of 2021. The average cap rate at the beginning of this year reached 3.9 percent, 30 basis points lower than the average in 2020.

Investment Trends



Sources: NorthMarq, CoStar

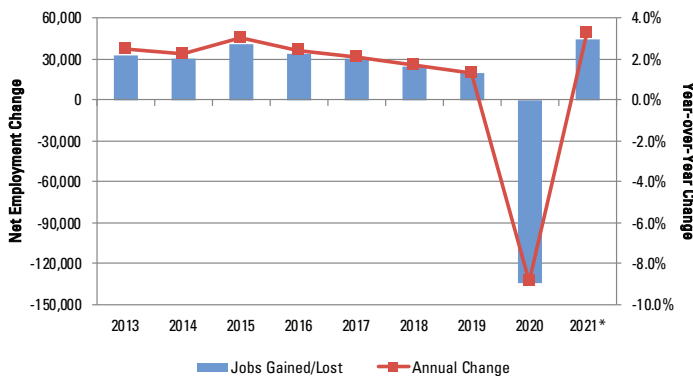
The average cap rate at the beginning of this year reached 3.9 percent

Looking Ahead

The San Diego multifamily market will likely record a mixed performance in 2021, even as the local labor market bounces back as the economy reopens. Renter demand for apartments should gain momentum throughout the year, as employers bring back workers at a healthy pace. While demand will pick up, there will also be significant supply growth, as developers are scheduled to deliver more than 3,000 units, the highest annual total since 2018. The result will likely be a modest increase in the area vacancy rate, coupled with a rise in the average market rent.

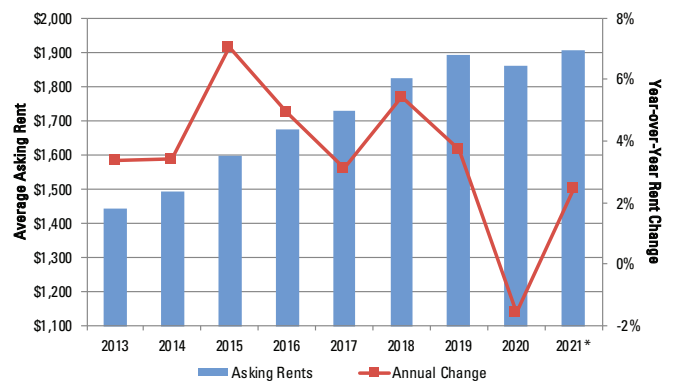
Investor demand for local apartment properties is expected to remain elevated in 2021, and transaction activity has already gotten off to an active start to the year. The properties that changed hands at the beginning of the year generally involved older Class C complexes, but as a more diverse mix of properties sells, prices should tick higher. This trend began to emerge during the first few weeks of the second quarter. Cap rates have compressed as investors underwrite acquisitions with the expectation of future rent increases.

Employment Forecast



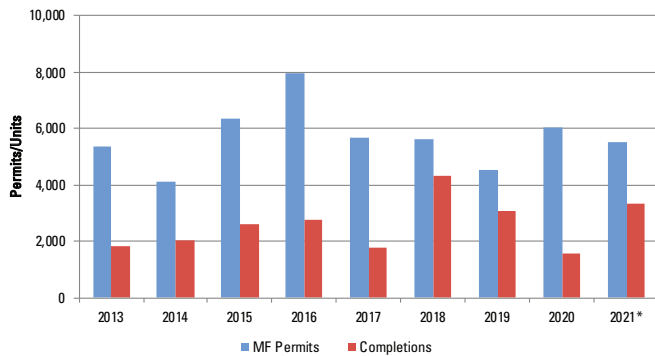
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



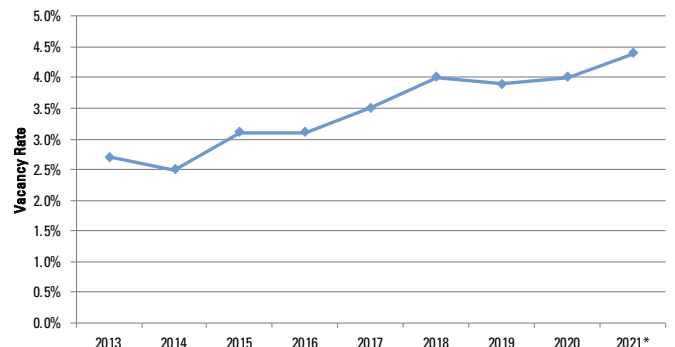
* Year End Forecast
Sources: NorthMarq, Reis

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 more than \$16 billion, loan servicing portfolio of more than \$65 billion and the multi-year tenure of our nearly 600 people.

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