# Market Insights

San Diego Multifamily 4Q 2021

Northmarq

## Construction Activity

**4,649**
Units under construction

**1,249**
Units delivered (YTD)

## Market Fundamentals

**4.3%**
Vacancy

**+30bps** | Year over year change

**$2,155**
Asking Rent

**+15.9%** | Year over year change

## Transaction Activity

**$321,000**
Median sales price per unit (YTD)

# Sales Activity Accelerates as the Local Labor Market Rebounds

## Highlights

- The San Diego multifamily market posted improving conditions to close out the year, building on gains recorded during the third quarter. Asking rents advanced at an unprecedented rate in recent months while the local labor market recorded an ongoing recovery. Renter demand is expected to remain elevated in the year ahead.
- Vacancy dipped 10 basis points during the fourth quarter, and the rate ended the year at 4.3 percent. While the rate inched lower in the final few months of the year, vacancy rose 30 basis points for the full year. With the exception of Downtown, most submarkets across San Diego posted vacancy rates between 2.5 percent to 4.5 percent.
- Asking rents jumped 6.2 percent during the fourth quarter and spiked 15.9 percent for the full year. After the steep increases, asking rents ended 2021 at $2,155 per month.
- Transaction velocity gained momentum in the last few months of the year, outpacing levels recorded in recent periods. The median sales price trended higher during 2021, ending the fourth quarter at $321,000 per unit. As prices rose, cap rates compressed, averaging approximately 3.1 percent during the fourth quarter.

## San Diego Multifamily Market Overview

The San Diego economy gained momentum in 2021, particularly late in the year, leading to healthy operational performance in the local multifamily market. While the local vacancy rate is above the region's long-term trend, renter demand has been strong enough to result in rapid rent growth. The year ahead should be an active one in terms of both new supply and accelerating renter demand. The pace of rehiring should remain elevated, and new projects are set to deliver in a handful of submarkets. The additions to supply growth could result in some modest increases in the Class A vacancy rate, but conditions are expected to remain extremely tight in the region's Class B and Class C units, where vacancies routinely hover around 2.5 percent.

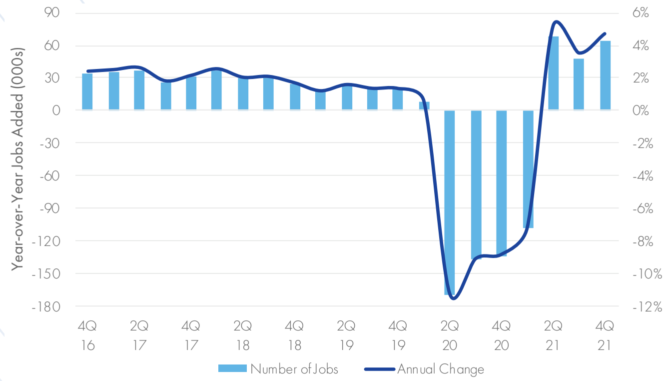
The accelerating pace of rent growth in the second half of 2021 was reflected in the multifamily investment market, as sales velocity gained momentum during the fourth quarter. The number of properties that changed hands in the final months of the year nearly matched the combined levels recorded from the preceding six months. While Class B and Class C properties continue to account for the bulk of transactions in the San Diego market, there has been a surge in larger transactions. During the fourth quarter, more than one-third of the transactions sold for more than $75 million. Cap rates averaged 3.1 percent during the fourth quarter with several properties transacting at cap rates between 2.5 percent to 3 percent.

## Employment

- Employers in San Diego brought back workers at a steady pace throughout 2021, including the addition of more than 21,000 jobs in the fourth quarter. The local labor market expanded by nearly 65,000 positions for the year, advancing 4.7 percent during 2021.
- The labor market was propelled forward by gains in the professional and business services sector in 2021. Professional employment expanded by 13,500 jobs in the past year, a 5.3 percent growth rate.
- The technology industry in San Diego has been growing over the past several years as high-tech companies relocated from the Bay Area. San Francisco-based software company Groove expanded in San Diego during the past year and added 50 positions Downtown. The company plans to double its local workforce in the year ahead, adding positions in sales, marketing, and engineering.
- **Forecast:** Despite strong gains in 2021, total employment in San Diego is still down more than 5 percent from its pre-pandemic high, allowing for additional recovery. Area employment is forecast to expand by an additional 3.5 percent in 2022, with employers bringing back more than 50,000 workers.

"The local labor market expanded by 4.7 percent during 2021."

### Employment Overview



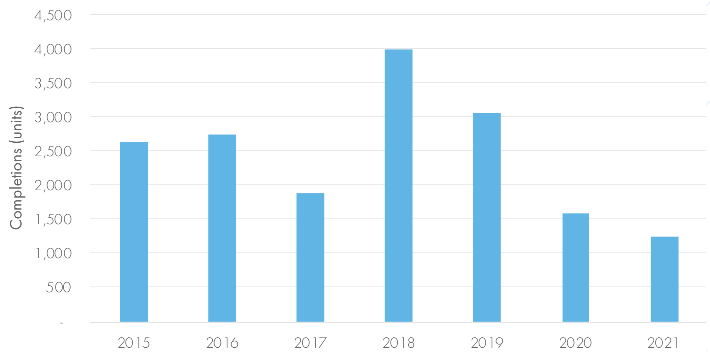

Sources: Northmarq, Bureau of Labor Statistics

## Development and Permitting

- Construction activity slowed during the final months of the year with no significant projects coming online during the fourth quarter. Projects totaling 1,249 units were delivered in 2021, the lowest annual total for deliveries since 2011.
- More than 4,600 units are currently under construction in San Diego, down about 10 percent from the total one year ago. The most active submarkets for future construction include Downtown and Clairemont/Linda Vista.
- Multifamily permitting remained active in 2021 with developers pulling permits for more than 5,700 units during the year. Multifamily permitting activity has remained in a fairly tight range for the past five years.
- **Forecast:** With more than 4,600 units currently being developed, apartment completions are expected to accelerate in 2022. Projects totaling approximately 3,100 units are forecast to be delivered in the year ahead.

"More than 4,600 units are currently under construction."

### Development Trends



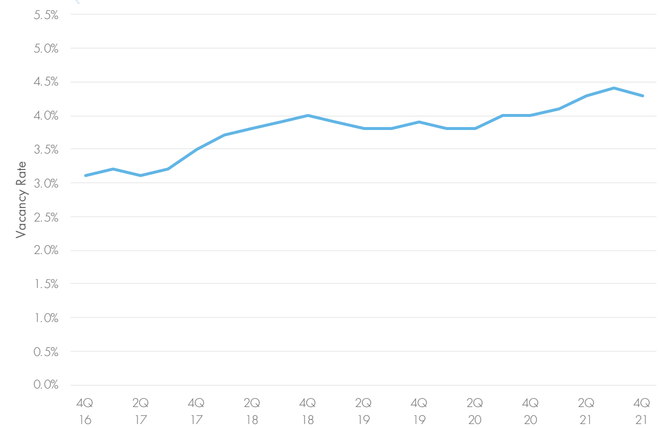

Sources: Northmarq, Reis

# Vacancy

- Vacancy dipped slightly in the final months of 2021, declining 10 basis points during the fourth quarter to 4.3 percent. The vacancy rate had been slowly trending higher since 2014, as developers have been more active in bringing new apartment projects into the market.
- In 2021, vacancy rose 30 basis points in San Diego. Despite a recent uptick across the county, vacancy remains extremely tight in the submarkets on the eastern portions of the county, with average rates of around 1.5 percent in Escondido/San Marcos and El Cajon/Santee/Lakeside.
- The vacancy rate in Class B and Class C properties has remained consistently low during the past several years. In 2021, vacancy in Class B and Class C units declined 10 basis points to end the year at 2.4 percent.
- **Forecast:** With an elevated number of units forecast to come online in the year ahead, vacancy is expected to inch higher. The rate is expected to rise 20 basis points in 2022, ending the year at 4.5 percent.

> Vacancy dipped slightly during the fourth quarter to 4.3 percent.

### Vacancy Trends



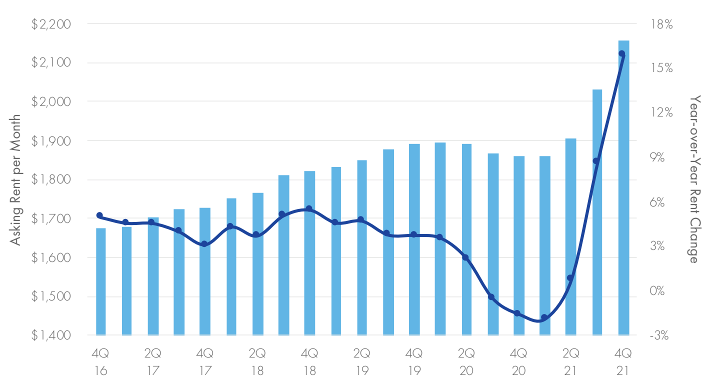

Sources: Northmarq, Reis

# Rents

- Asking rents in San Diego recorded rapid gains in 2021, particularly during the second half of the year. Rents jumped 6.2 percent from the third quarter to the fourth quarter to $2,155 per month.
- Area asking rents rose 15.9 percent in 2021, the largest annual rent growth on record in San Diego. The latest year of growth was well above trend; the market has averaged a growth rate of nearly 3.5 percent annually during the past decade.
- Rents advanced at an accelerated pace across all property classes during 2021 with significant growth occurring in Class A properties. Asking rents in Class A units expanded more than 15 percent in 2021, reaching $2,622 per month.
- **Forecast:** Asking rents in San Diego are expected to continue to rise in the coming quarters, though the pace of growth will likely taper off from 2021 levels. Average rents are forecast to end 2022 at $2,290 per month, up 6.3 percent from levels at the end of 2021.

> Asking rents rose 15.9 percent in 2021.

### Rent Trends



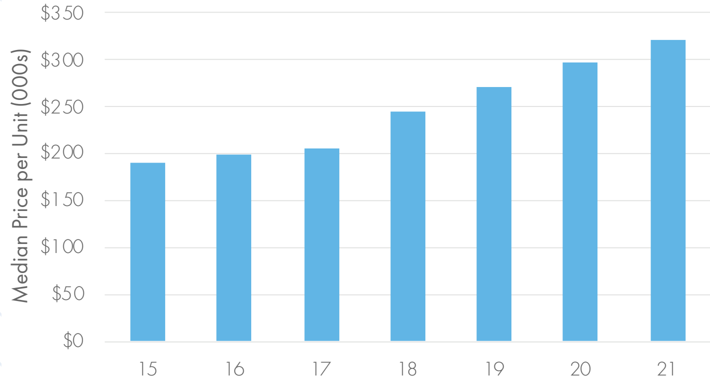

Sources: Northmarq, Reis

# Multifamily Sales

- The San Diego investment market gained momentum in recent months with transaction activity increasing nearly 70 percent from the third quarter to the fourth quarter. Total sales volume for the year more than doubled the number of transactions in 2020.
- The median sales price in 2021 was approximately $321,000 per unit, up nearly 8 percent from the median price in 2020. Although transactions occurred across the entire San Diego metro, some of the most active regions included Escondido and El Cajon, which also feature the tightest vacancies in the county.
- The rapid rent growth recorded in San Diego led to cap rate compression late in the year. During the fourth quarter, cap rates compressed to an average of just 3.1 percent.

> The median sales price in 2021 was $321,000 per unit.

### Investment Trends




Sources: NorthMarq, CoStar

## Recent Transactions

### Multifamily Sales Activity

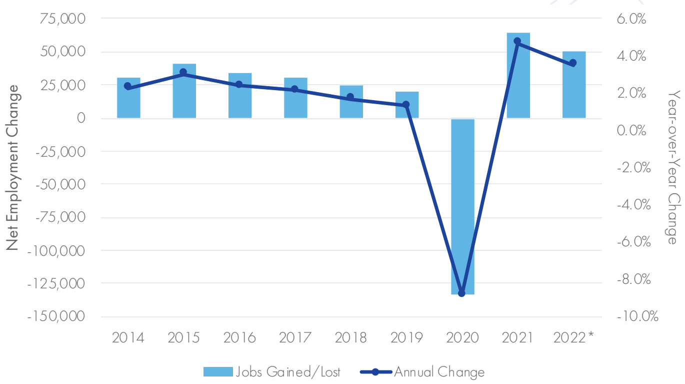
| Property Name | Street Address | Units | Sales Price | Price/Unit |
|---|---|---|---|---|
| The Merian | 601 11th Ave., San Diego | 426 | $300,000,000 | $704,225 |
| Sofi Ocean Hills | 3500 Windrift Way, Oceanside | 404 | $196,000,000 | $485,149 |
| Palomar Station | 1257 Armorlite Dr., San Marcos | 386 | $195,000,000 | $505,181 |
| Gravity | 4560 Mission Gorge Pl., San Diego | 325 | $177,500,000 | $546,154 |
| Escondido Portfolio | Multiple | 314 | $157,000,000 | $500,000 |
| Jefferson Pacific Beach | 4275 Mission Bay Dr., San Diego | 172 | $113,000,000 | $656,977 |
| Sunterra | 3851 Sherbourne Dr., Oceanside | 240 | $97,500,000 | $406,250 |
| EV Lofts | 688 13th St., San Diego | 208 | $85,250,000 | $409,856 |
| Latitude at Mission Valley | 4580 Zion Ave., San Diego | 146 | $47,525,000 | $325,514 |

# Looking Ahead

Following a year of healthy economic recovery and rapid rent growth, the San Diego multifamily market is expected to post additional gains in 2022. The ongoing additions in the labor market should support demand, while the pace of new supply growth should accelerate. The past two years have been below trend for new apartment deliveries, but developers are expected to ramp up activity levels in 2022. With more than 3,000 units expected to come online by the end of next year, vacancy will likely inch higher, especially in the areas where construction is more concentrated including the Clairemont/Linda Vista submarket. Even if new supply growth outpaces absorption, rents should continue to trend higher in the coming year, although gains are expected to more closely track historical levels.

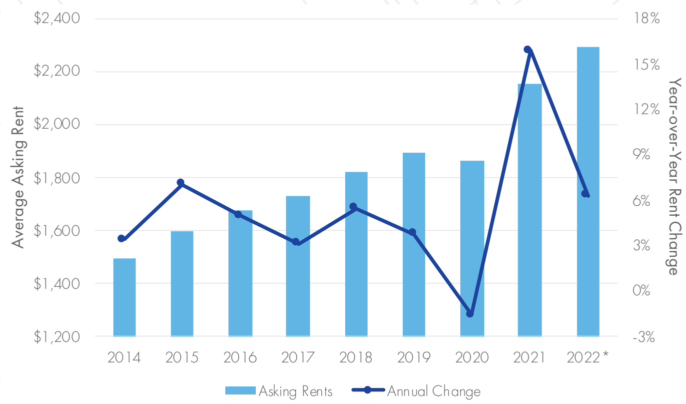
The multifamily investment market gained momentum during the fourth quarter, signaling a return to normalcy in the year ahead. Building upon the recent spike in sales velocity, the investment market is expected to remain active and competitive in 2022. Following an unprecedented pace of rent growth in 2021, sales prices will likely continue to trend higher in the next several quarters, even if future rent increases do not keep pace with levels achieved in 2021. A growing number of opportunities should open up for investors in the next few years, as dozens of projects are currently in the development pipeline. Cap rates have crept lower in recent months and will likely remain compressed.

## Employment Forecast



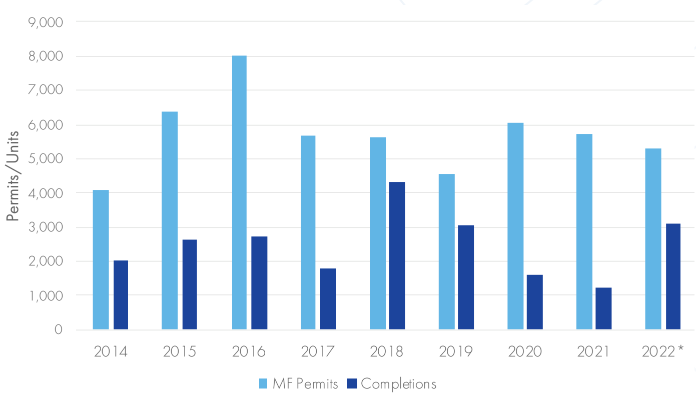

* Year End Forecast
Sources: Northmarq, Bureau of Labor Statistics

## Rent Forecast



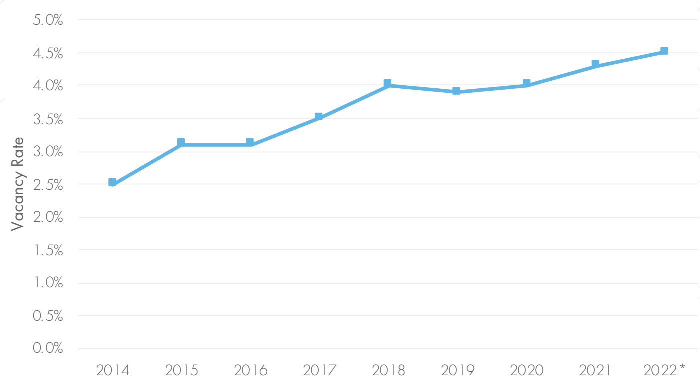

* Year End Forecast
Sources: Northmarq, Reis

## Construction & Permitting Forecast




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

## Vacancy Forecast




* Year End Forecast
Sources: Northmarq, Reis

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## For more information, please contact:


Kyle Pinkalla
Managing Director – Investment Sales
858.675.7865
kpinkalla@northmarq.com

Erik Anderson
Associate Vice President – Investment Sales
858.675.7641
eanderson@northmarq.com

Tobin Hecker
Associate – Investment Sales
858.401.9335
thecker@northmarq.com

Eric Flyckt
SVP, Managing Director – Debt & Equity
858.675.7640
eflyckt@northmarq.com

Aaron Beck
SVP, Senior Director – Debt & Equity
858.675.7862
abeck@northmarq.com

Conor Freeman
Vice President – Debt & Equity
858.675.7661
cfreeman@northmarq.com

Wyatt Campbell
Vice President – Debt & Equity
858.675.7860
wcampbell@northmarq.com

Pete O'Neil
Director of Research
602.508.2212
poneil@northmarq.com


## About Northmarq

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