Northmarq

CONSTRUCTION ACTIVITY

UNDER CONSTRUCTION	4,723
UNITS DELIVERED	235

MARKET FUNDAMENTALS

VACANCY RATE	3.5%
YEAR-OVER-YEAR CHANGE	-50bps
ASKING RENTS	$2,333
YEAR-OVER-YEAR CHANGE	+4.8%

TRANSACTION ACTIVITY (YTD)

MEDIAN PRICE PER UNIT*	$265,100

San Diego Multifamily
1Q 2023

MARKET INSIGHTS

Vacancy remains flat, rents inch higher

HIGHLIGHTS

- Property fundamentals in San Diego were mostly stable during the first quarter, as vacancy held steady and asking rents inched higher. Multifamily deliveries were limited to start the year but are forecast to pick up in the remainder of 2023.
- Area vacancy remained unchanged during the first quarter, finishing the period at 3.5 percent. The rate has improved by 50 basis points year over year.
- Asking rents inched higher at the start of the year, rising just 0.2 percent to $2,333 per month. Local apartment rents are up 4.8 percent from one year ago.
- The San Diego multifamily investment market experienced a slowdown as only a handful of properties changed hands in the first quarter. The median sales price to this point in 2023 is $265,100 per unit, down 26 percent from the median price last year.

SAN DIEGO MULTIFAMILY MARKET OVERVIEW

The San Diego multifamily market posted modest improvements during the first quarter, as vacancy levels stabilized and asking rents inched higher. The local market generally has fairly steady demand patterns, but the pace of absorption slowed in 2022. Absorption totals improved somewhat during the first quarter but still remain below trend. On the supply side, completions should pick up in the coming periods with projects totaling more than 4,700 units currently under construction throughout the region. While Downtown San Diego and Balboa Park account for the largest share of ongoing construction, developers are also active in Mission Valley and North County.

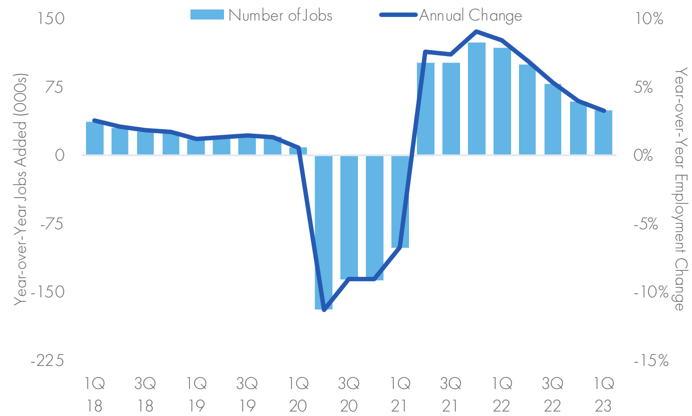
The multifamily investment market in San Diego slowed during the first quarter, falling to its lowest level of activity since 2020. The market remains in a period of price discovery as some owners are attempting to list properties at peak levels, which is not feasible for many buyers in the current high-interest rate market. As a result, bid-ask spreads have hampered deal flow across the region. Additionally, the San Diego City Council recently approved a host of strict, new renter protections intending to make it harder for landlords to evict tenants. While these policy changes have not yet been enacted, they have added a layer of uncertainty for many operators across the region.

EMPLOYMENT

- Area employers continued to add jobs at a steady pace at the start of 2023. Year over year, total employment advanced by 48,900 positions, a gain of 3.2 percent.
- San Diego's leisure and hospitality industry has been a major driver for the local economy in recent quarters. Year over year, this sector expanded by 10.3 percent with the addition of 18,900 workers. Despite the recent recovery, total employment in the sector still lags the mid-2019 peak, suggesting additional gains are likely in the coming quarters.
- Marriott International recently broke ground on the Gaylord Pacific Resort and Convention Center in Chula Vista. The 1.8 million-square-foot resort is anticipated to have 1,600 hotel rooms and nearly 420,000 square feet of convention center space. This project is expected to bring more than 10,000 construction jobs and 4,000 permanent jobs to the region.
- **FORECAST:** Total employment in San Diego is projected to expand by 1.3 percent in 2023 with the addition of roughly 20,000 jobs.

Year over year, total employment advanced by 48,900 positions.

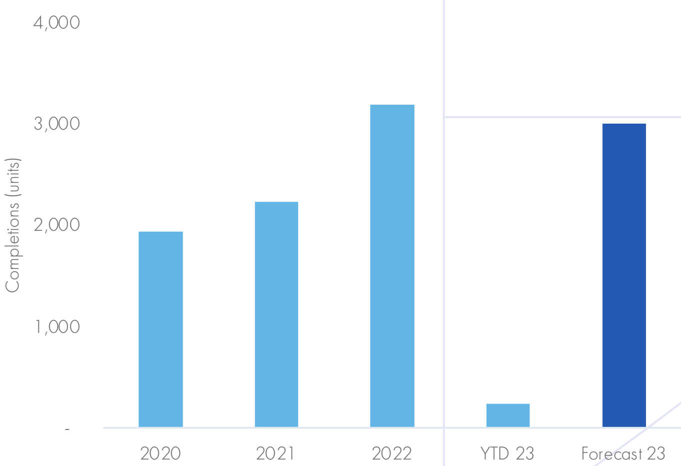
EMPLOYMENT OVERVIEW



Sources: Northmarq, Bureau of Labor Statistics

Projects totaling more than 4,700 units are under construction.

DEVELOPMENT TRENDS



Sources: Northmarq, CoStar

DEVELOPMENT & PERMITTING

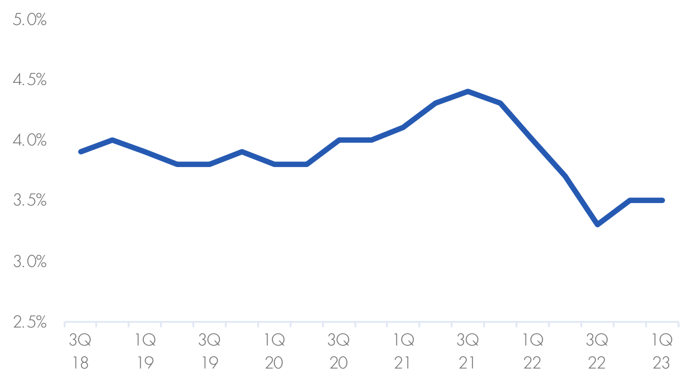
- Multifamily developers in San Diego completed 235 units in the first three months of 2023, the lowest quarterly total in two years. Following the lull, the pace of apartment completions should pick up significantly in the coming months.
- The development pipeline has thinned somewhat in recent quarters due to an acceleration of deliveries in 2022. Projects totaling more than 4,700 units are currently under construction throughout San Diego, down 20 percent from one year ago.
- Multifamily permitting picked up in the first three months of the year, as developers pulled permits for nearly 1,100 units in the first quarter, up 25 percent from the previous period. Despite the recent rise, annual permitting in 2023 is expected to slow from the last few years.
- **FORECAST:** After a slow start to the year, the pace of apartment deliveries is on pace to gain momentum in the coming periods. Projects totaling approximately 3,000 units are slated to come online in 2023.

VACANCY

The vacancy rate finished the first quarter at 3.5 percent.

- Vacancy in San Diego was stable in recent months; the rate finished the first quarter at 3.5 percent, matching the year-end 2022 figure. Vacancy improved by 50 basis points year over year.
- The submarkets in San Diego that record rents below the market average tend to have the tightest vacancy conditions. Some of these submarkets include El Cajon/Santee/Lakeside, San Diego/East of I-15, and Escondido/San Marcos, all with vacancies below 2 percent.
- Local vacancy has consistently been lowest in mid-tier and lower-tier properties. The combined vacancy rate in Class B and Class C units reached 1.7 percent in the first quarter. Class A vacancy was 5.6 percent in the first quarter, after lingering above 6 percent for much of the previous two years.
- **FORECAST:** Area vacancy is projected to inch slightly higher in the remainder of the year but remain near its long-term average. Vacancy is expected to rise 20 basis points in 2023, ending the year at around 3.7 percent. Vacancy in San Diego has remained between 3 percent and 4.5 percent since 2015.

VACANCY TRENDS



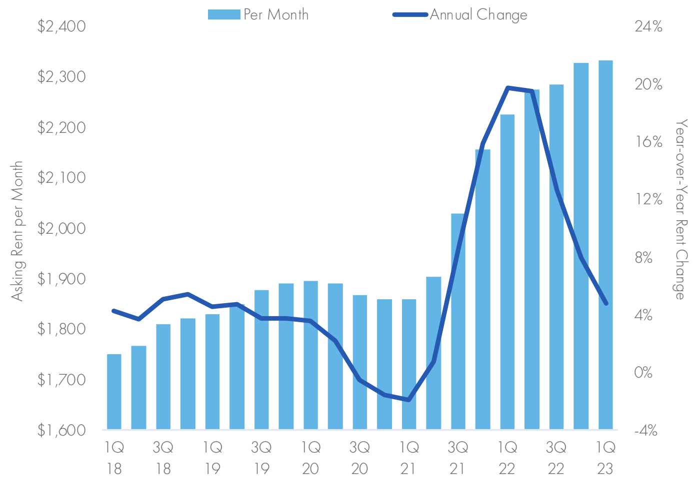
Sources: Northmarq, REIS

RENTS

- Asking rents in San Diego inched higher at the start of the year, rising just 0.2 percent in the first quarter to $2,333 per month. Local apartment rents have now risen for eight consecutive quarters, although this latest uptick was the smallest gain in that period.
- Year over year, average rents rose 4.8 percent, faster than the region's long-term trend. Annual rent growth averaged 3.8 percent from 2015 to 2020, before rents spiked in 2021 and 2022.
- After recording some of the strongest rent growth in the region last year, the La Mesa/Spring Valley/Lemon Grove submarket posted the largest decline in rents in the past three months. Average rents in this submarket fell 1.8 percent in the first quarter to $2,111 per month.
- **FORECAST:** Annual rent growth is projected to continue to cool in 2023. Asking rents in San Diego are forecast to reach $2,400 per month by the end of the year, roughly a 3 percent annual increase.

Year over year, average rents rose 4.8 percent.

RENT TRENDS



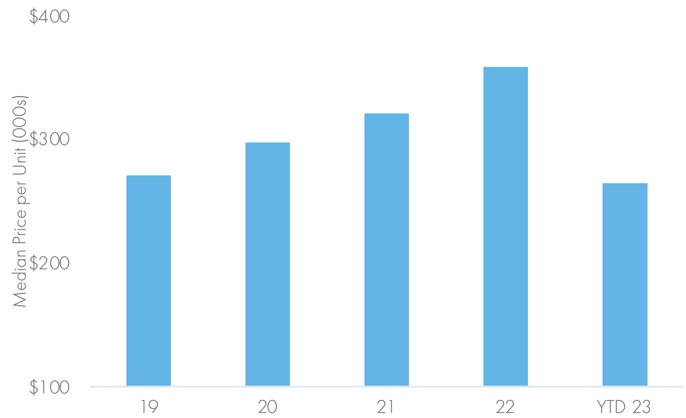
Sources: Northmarq, REIS

MULTIFAMILY SALES

- Multifamily sales activity slowed significantly at the start of 2023, as the number of deals during the first quarter fell nearly 70 percent from the previous period. Additionally, transaction volume in the last three months is down 50 percent from the same period last year.
- With fewer properties selling, prices also trended lower at the outset of this year. The median sales price thus far in 2023 is $265,100 per unit, down 26 percent from the median price in 2022.
- Cap rates continued to trend higher in the early months of the year. Cap rates averaged around 4.25 percent in the first quarter, up roughly 125 basis points from one year ago.

The median sales price thus far in 2023 is $265,100 per unit.

INVESTMENT TRENDS



Sources: Northmarq, CoStar

RECENT TRANSACTIONS MULTIFAMILY SALES ACTIVITY

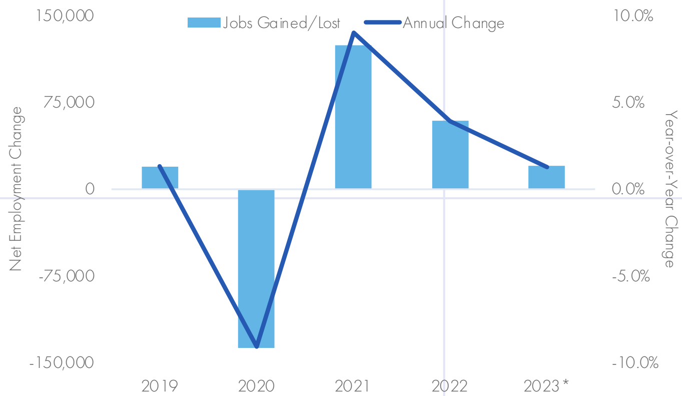
PROPERTY NAME	STREET ADDRESS	UNITS	SALES PRICE	PRICE/UNIT
San Diego Portfolio	3454 Ruffin Rd., San Diego & 6363 Beadnell Way, San Diego	520	$163,567,500	$314,553
Ballpark Place	229 16th St., San Diego	100	$21,000,000	$210,000
El Cajon Portfolio	966 & 948 S Sunshine Ave., El Cajon & 1018 E Lexington Ave., El Cajon	61	$16,170,000	$265,082
Easter Manor Apartments	1113 Greenfield Dr., El Cajon	28	$8,128,000	$290,286
Royal Apartments	5101 Towle Ct., San Diego	48	$7,000,000	$145,833
Chula Vista Apartments	175 E St., Chula Vista	25	$5,965,000	$238,600

LOOKING AHEAD

Multifamily property performance metrics in San Diego have leveled off in recent months, following heightened rent growth and strong renter demand since 2021. Going forward, the local market is projected for a moderate performance in 2023. Asking rents are forecast to rise about 3 percent this year. This is a slower pace of growth than is typical in the region where conditions are tight and housing affordability is a persistent challenge. Construction has been elevated in recent years, but the development pipeline has thinned in recent quarters. Still, multifamily permitting rose to start 2023, and the vacancy rate is expected to record modest upticks in the remainder of the year.

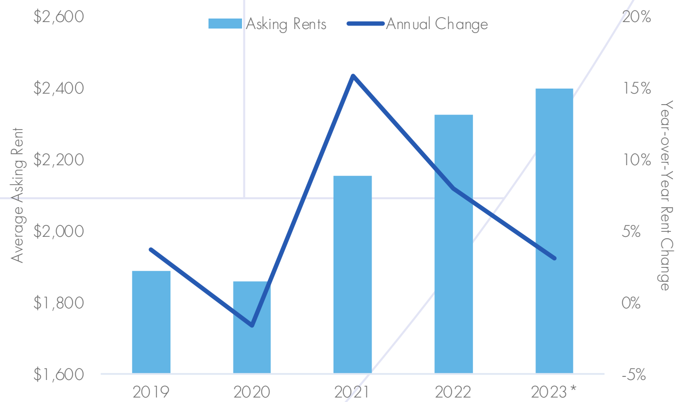
Investors will likely remain attracted to San Diego for the region's stable property fundamentals and strong local economy. While the elevated cost of financing has limited sales activity in recent months, transaction volume is projected to accelerate in the second half of the year. Investors may find new opportunities in submarkets where construction is more concentrated, including Downtown San Diego and Balboa Park. Cap rates in the market generally do not trend much above 4.5 percent or 5 percent, even when yields on Treasury bonds push higher. While cap rates may inch higher in the near term, any additional increases will likely be modest.

EMPLOYMENT FORECAST



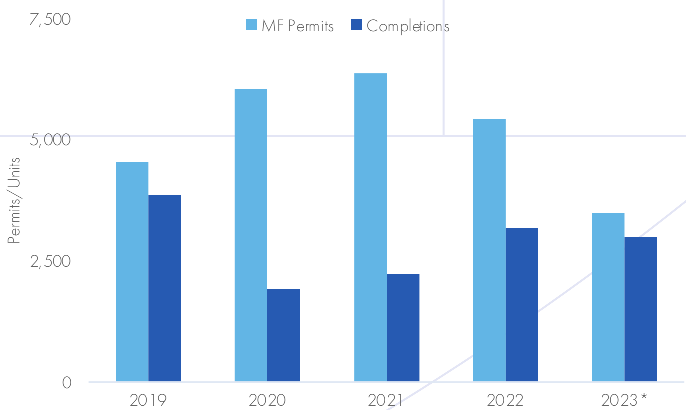
* Year End Forecast
Sources: Northmarq, Bureau of Labor Statistics

RENT FORECAST



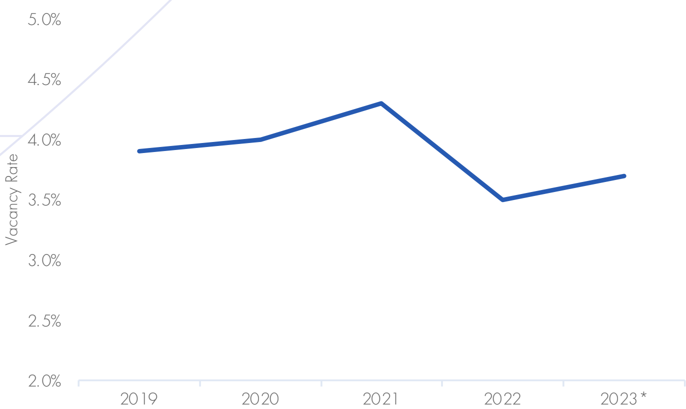
* Year End Forecast
Sources: Northmarq, REIS

CONSTRUCTION & PERMITTING FORECAST



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

VACANCY FORECAST



* Year End Forecast
Sources: Northmarq, REIS

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