MARKET REPORT

Multifamily

Sacramento Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

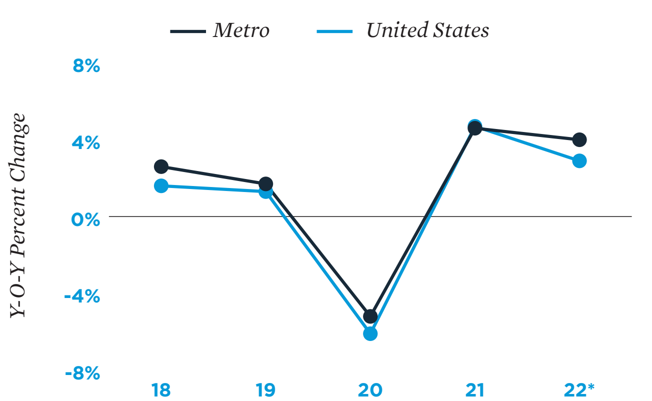
3Q/22

Multi-Decade Construction Record Lifts Vacancy; Rate Still Low by Historic Standards

Demand reaches an inflection point. Across 2020 and 2021, more units were absorbed on a net basis than in the previous six years combined. This allowed vacancy to breach the sub-2 percent threshold at the turn of the calendar, the first time this has happened since 2001. The tides shifted during the opening six months of 2022, however, as net absorption was measured at negative 670 units — the weakest two-quarter span in almost five years. Sacramento is experiencing a demand normalization, after a historic stretch that resulted in fewer than 3,000 rentals being available throughout the entire metro earlier this year. Even with the reversal during the first half, the number of vacant units held below the 2019 year-end level, which will continue to drive competition between prospective tenants and facilitate rent growth. The average effective monthly rate is expected to eclipse $2,000 by the culmination of 2022, but Sacramento remains the most affordable of the major California markets.

Slower household creation will be partially offset. Amid widespread inflation and fast rent growth, fewer households are being formed as some residents cut costs by finding roommates or moving back in with family. This contributed to the rise in rental vacancy during the first half of 2022; however, future losses are expected to be counterbalanced by homeownership barriers. The affordability gap, or the difference between a monthly payment on a median priced home compared to a rent obligation, tripled in the span of just seven quarters, surpassing $1,500 in the most recent period.

Employment Trends



** Forecast*

Sources: BLS; CoStar Group, Inc.; RealPage, Inc.

Multifamily 2022 Outlook

40,500 JOBS
will be created

EMPLOYMENT:

Through the first half, Sacramento's job count grew by the slowest pace year-over-year of the major California metros. By the end of 2022, however, the number of workers will exceed the 2019 tally by the second-largest margin among the eight markets.

3,000 UNITS
will be completed

CONSTRUCTION:

Responding to three consecutive years of vacancy compression totaling 180 basis points, developers are stepping on the gas. The 2022 delivery volume will be the largest in more than 20 years, with a high concentration in the urban core.

110 BASIS POINT
increase in vacancy

VACANCY:

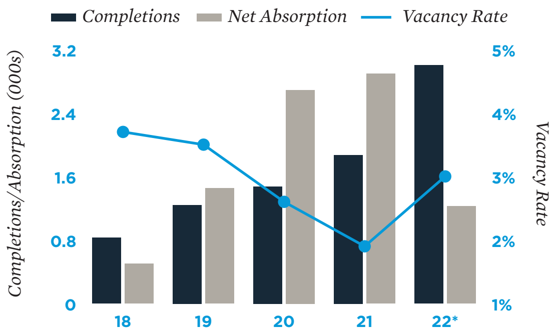
Slower household creation amid inflationary pressures and a record-setting pipeline result in a notable vacancy climb. Still, Sacramento's rate ends the year 50 basis points below 2019's recording at 3.0 percent.

8.7% INCREASE
in effective rent

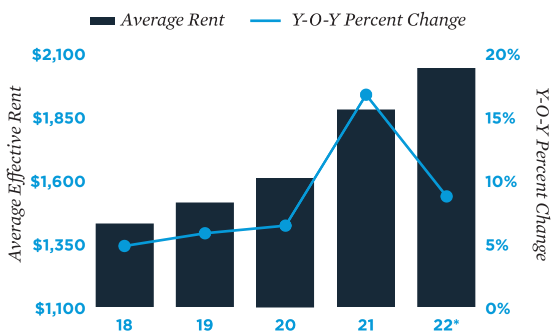
RENT:

While vacancy is expected to rise, renters will still be competing for a low number of available units compared to years past. This, along with lease turnover from pandemic rates, help move the average effective rent up to $2,040 per month.

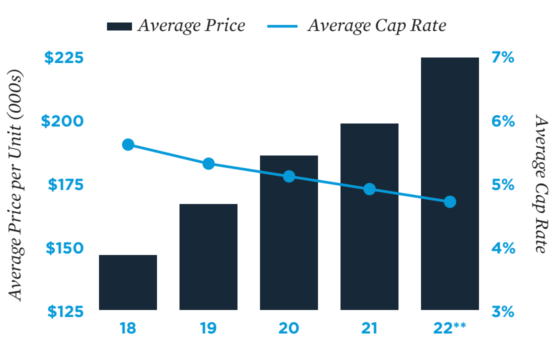
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 2Q*

Sources: CoStar Group, Inc.; Real Capital Analytics; RealPage, Inc.

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Price: $250

2Q 2022 - 12-Month Period

CONSTRUCTION

2,567 units completed

- The pace of supply growth during the 12-month period ended in June more than doubled the previous year's 0.7 percent rise. Central Sacramento added over 1,000 new rentals, compared to just 60 units in the prior year.
- Of the 11 suburban areas, only Woodland-West Sacramento and North Sacramento-North Highlands had inventory gains of at least 2 percent.

VACANCY

90 basis point increase in vacancy Y-O-Y

- Davis has been a bright spot in the market, as the university produces consistently strong demand for campus-adjacent rentals. Vacancy in the submarket plunged 550 basis points year-over-year to 2.0 percent in June.
- Excluding Davis, only one other submarket had a vacancy decline. The rate fell 50 basis points in Carmichael to a marketwide low of 1.5 percent.

RENT

13.5% increase in the average effective rent Y-O-Y

- Class A posted an 11.1 percent gain to $2,288 per month, while the Class B segment registered a 15.6 percent rise to $1,882 per month. In the prior year, the luxury segment outpaced the mid-tier improvement.
- Annual rent growth exceeded 10.0 percent in all but one submarket, and surpassed 15.0 percent in three different suburban pockets of Sacramento.

Investment Highlights

- Apartment assets that transacted during the four-quarter frame ended in June carried an average sale price of $224,200 per unit, nearly 17 percent above the prior year's measure. This level of growth is not particularly unusual for the market in recent periods, with annual rises eclipsing 10 percent in four of the past five years, including jumps of at least 17 percent in two of those intervals. Sacramento's average entry cost per unit is now more than twice as high as it was in 2016, an acceleration that ranks as the fastest among the eight major California markets during that span.
- Sacramento retained the highest average cap rate of the state's major markets, at 4.7 percent during the yearlong span ended in the second quarter. The potential for higher yields alongside a robust sale price growth trajectory is generating greater attention from regional institutions, as well as investment groups typically focused on other regions of the U.S.
- Nearly 800 rentals finalized in Central Sacramento during the first half of 2022, and an additional 2,000 units are scheduled to deliver before the end of next year. New supply entering the urban core will present future opportunities for investors to acquire institutional-grade product. Class A/B assets here often trade for more than $600,000 per unit.