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Bay Area Multifamily

November 2023

Prospects of Bay Area Apartments Stronger Than Media Suggests

There is a solid case to be made for the future performance potential and investment appeal of the multifamily sector in the San Francisco Bay Area, despite media reports that tend to emphasize the local economy's recent challenges. Three key factors underlie why the need for apartment rentals in the region is not only robust, but growing.

Economic Resilience. Total employment combined across the San Francisco, East Bay and South Bay metro areas is approaching 3.6 million jobs. That tally is nearly 50,000 positions ahead of the early 2020 pre-pandemic count, setting the stage for the sort of comeback that has been recorded after previous downcycles, including the Dot-com Bubble of the early 2000s and the Global Financial Crisis of the late 2000s. The job base is heavy on high-paying positions, reflecting the importance of the technology sector, as well as the region's capture of venture capital investments. Innovation remains a key advantage for Northern California. Silicon Valley should account for a quarter of U.S. job creation driven by new artificial intelligence capabilities.

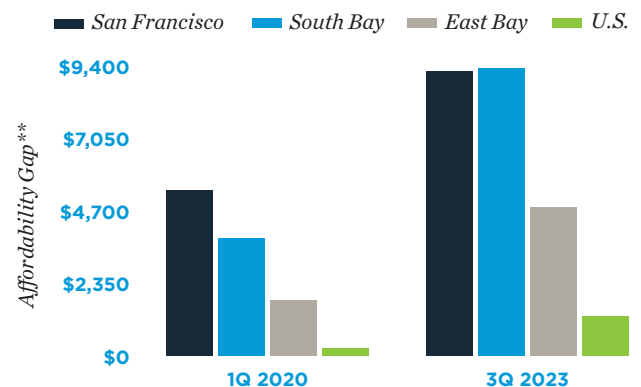
Lofty For-Sale Residential Prices. As the Bay Area's population expands amid new job opportunities, stunningly expensive for-sale home prices will steer much of the local housing demand to rentals. A shortage of for-sale product is pushing up home prices across the country, while financing costs are registering a drastic impact from elevated mortgage interest rates that have recently touched the 8 percent mark. The national premium to buy the typical, median-priced single-family home versus rent the average apartment is at a record \$1,291 per month. That gap in affordability is even wider in the Bay Area, exceeding \$4,800 per month in the East Bay and \$9,200 per month in San Francisco and the South Bay.

Limited Apartment Construction. Chronic apartment shortages continue in the Bay Area, in sharp contrast to a wave of new supply arriving in some other parts of the country. The 17,400 units regionally under construction going into the final quarter of 2023 will yield inventory growth of just 2.6 percent, only half the 5.2 percent expansion on the way nationally. Moreover, the apartments currently in development in the Bay Area likely reflect the peak in activity that will be seen for quite a while. Local construction starts came to a near standstill during the past few months.

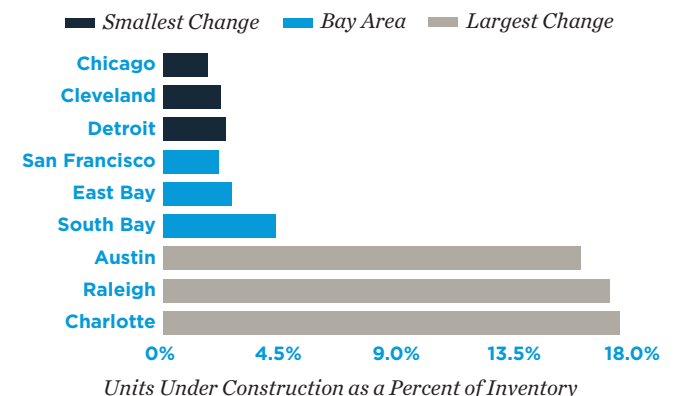
Bay Area Employment Rebound Trend



Bay Area Single-Family Home Costs Surge



Bay Area Has Comparatively Slow Stock Growth



* As of 3Q

** Gap between average effective apartment rent and mortgage payment on a median-priced home

Sources: IPA Research Services; BLS; CoStar Group, Inc.; Moody's Analytics; RealPage, Inc.

East Bay and South Bay Neighborhoods Outperform

The Bay Area's apartment vacancy rate stood at 5.3 percent at the end of the third quarter. While that vacancy figure has inched above the historical average, it is a healthy reading that is under previous highs from both the Dot-com Bubble and the worst part of the pandemic. This measure is influenced by the region's big-picture supply shortfall. The existing inventory remains essentially full across much of the region, with undermet long-term housing needs evident, even in the neighborhoods that are registering the most momentary stress.

Rent growth momentum varies significantly across Bay Area neighborhoods, with several areas recording noteworthy gains. In general, rent growth since the pre-pandemic period is stronger in the lower-priced submarkets than in the more expensive zones. While employers pushing for workers to return to offices are making some progress, more stringent enforcement tactics will result in high leasing demand and upward rent momentum, particularly for luxury product in the South Bay, Peninsula and San Francisco.

The most robust rent increases are generally seen in areas where average monthly rents are under \$3,000, with several East Bay submarkets faring the best. Compared to pre-pandemic early 2020 rents, monthly payments are up at least 6 percent in almost every suburban East Bay neighborhood. Increases reach about 15 percent in outlying Northeast Contra Costa County, 13 percent in the Livermore and Pleasanton areas, and 11 percent in Concord, Martinez and Fremont. The neighborhoods with the lowest rents in the South Bay are also registering double-digit growth rates from early 2020 levels. Effective rates are up 13 percent in both the South and East San Jose submarkets.

Downtown San Francisco and the adjacent South of Market area are interesting investment counterplays at this point. Average rents in those neighborhoods ranged from \$3,200 to \$3,400 in September, well below past highs. Yet, urban core areas have traditionally been very popular with young adult renters, and the comparative drop in monthly rates could help restore their appeal.

The information contained in this report was obtained from sources deemed to be reliable. Every effort was made to obtain accurate and complete information; however, no representation, warranty or guarantee, express or implied, may be made as to the accuracy or reliability of the information contained herein. Sales data includes transactions sold for \$1 million or greater unless otherwise noted. Mortgage payment is based on the quarterly median home price at a 30-year fixed rate mortgage, 90% LTV, taxes, insurance and PMI. This is not intended to be a forecast of future events and this is not a guaranty regarding a future event. This is not intended to provide specific investment advice and should not be considered as investment advice.

Sources: IPA Research Services; Bureau of Labor Statistics; CoStar Group, Inc.; Moody's Analytics; RealPage, Inc.

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Top 15 Bay Area Submarkets by Rent Growth:

1Q 2020 to 3Q 2023

| Submarket | Metro | Rent Change 1Q20-3Q23 | Average Effective Rent 3Q23 | Vacancy Rate 3Q23 | Inventory Change 1Q20-3Q23 |
|---------------------------------|------------------|-----------------------|-----------------------------|-------------------|----------------------------|
| NE Contra Costa County | East Bay | 14.9% | \$2,191 | 6.4% | 4.9% |
| Livermore-Pleasanton | East Bay | 12.9% | \$2,823 | 5.5% | 1.8% |
| South San Jose | South Bay | 12.7% | \$2,911 | 4.2% | 3.7% |
| East San Jose | South Bay | 12.5% | \$2,709 | 6.4% | 0.7% |
| Concord-Martinez | East Bay | 11.1% | \$2,314 | 5.6% | 2.7% |
| Fremont | East Bay | 10.8% | \$2,732 | 4.3% | 7.5% |
| Hayward-San Leandro-Union City | East Bay | 9.5% | \$2,428 | 5.1% | 2.2% |
| San Ramon-Dublin | East Bay | 9.5% | \$2,709 | 3.6% | 3.2% |
| NW Contra Costa County | East Bay | 9.2% | \$2,477 | 6.2% | 4.2% |
| West San Jose-Campbell | South Bay | 6.9% | \$2,862 | 4.2% | 4.0% |
| North San Jose-Milpitas | South Bay | 6.8% | \$3,141 | 3.4% | 7.7% |
| Walnut Creek-Lafayette | East Bay | 6.3% | \$2,569 | 4.5% | 8.3% |
| Santa Clara | South Bay | 5.3% | \$3,182 | 4.9% | 7.6% |
| Marina-Pacific Heights-Presidio | San Francisco | 5.3% | \$3,682 | 4.8% | 0.8% |
| Daly City-Brisbane | S.F. - Peninsula | 4.9% | \$2,568 | 6.9% | 5.4% |
| Bay Area | | 3.4% | \$2,829 | 5.3% | 6.0% |

Sources: IPA Research Services; CoStar Group, Inc.; RealPage, Inc.

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