INVESTMENT FORECAST

Multifamily

San Jose

IPA | INSTITUTIONAL PROPERTY ADVISORS

2020

Transit Networks Increasingly Key for Development and Investment Strategies

Mountain View captivating builders, driving development to record high. Apartment construction will be abundant this year as 5,500 units are slated for delivery — the highest total this millennium. Northern sections of Sunnyvale will get much-needed supply amid sub-3 percent vacancy, while downtown San Jose will also witness significant development as builders focus on areas that align with public transit routes. Mountain View will post the strongest supply growth, adding more than 1,500 units, as developers seek to keep pace with the steady job creation of nearby tech firms. The influx of supply will outstrip the expected absorption of 3,700 apartments, putting short-term pressure on marketwide vacancy as it's pushed to the low-4 percent range. Some areas such as East San Jose will retain limited apartment availability, keeping local rent growth among the strongest in the market. Over the past five years, the average effective rent in East San Jose has risen 29 percent, the most of any submarket within the metro.

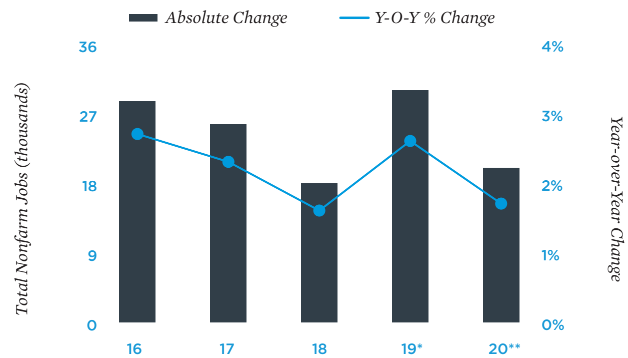
Rent-control caps causing investors to adjust underwriting. Over the past few years, as its neighbor to the north saw a huge imbalance between investment demand and properties trading hands, San Jose enjoyed a more reasonable balance between investor capital and the supply of properties for purchase. However, in the second half of 2019 the San Jose market registered a deceleration in sales activity that could carry over into the new year. The recent passage of statewide rent control regulations has caused confusion and uncertainty regarding current valuations. A potential silver lining, however, exists in the new rent law exempting properties less than 15 years old. Developers with recently or soon-to-be completed projects could leverage this loophole by pointing out that rental increase restrictions would not kick in for years and list their properties for disposition. This would then take advantage of the strong demand for core assets by institutional capital or REITs. Meanwhile, private capital's search for higher-yielding value-add opportunities will require creativity and patience in the coming year as the rental rate caps could hamper the ability to fully raise rents to cover the renovation costs of updated properties. Value-add owners may need to scale back the scope and depth of rehab plans in order to make sure that the capped rental increases will be able to hit their project returns.

22.3% *2019 share of local population between 20 and 34 years old*

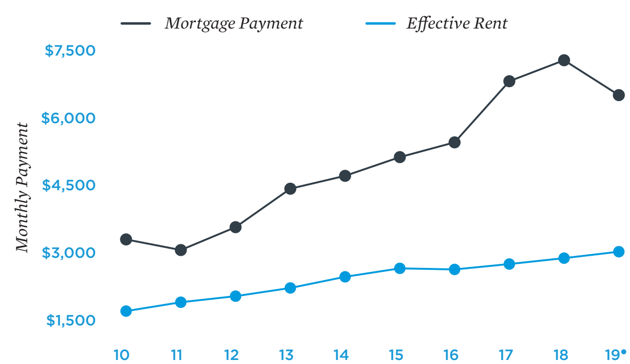
48.4% *of local population hold bachelor's degree or higher*❖

$1,294,696 *2019 median home price*

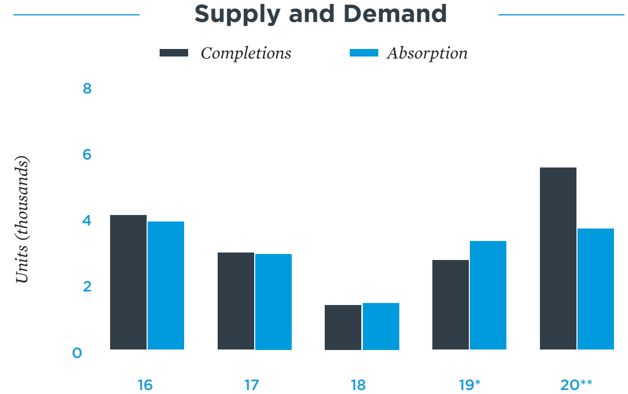
Employment Trends



Housing Affordability Gap



Supply and Demand



* Estimate ** Forecast • Through 3Q
❖ 2019: 25+ years old
Sources: Marcus & Millichap Research Services; RealPage, Inc.

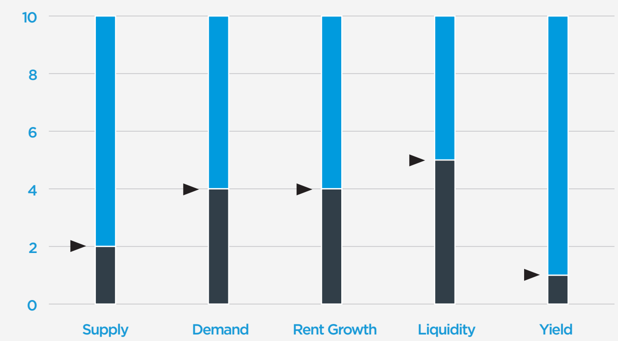
2020 Investment Outlook

Decreases in the demand and rent growth indexes during the second half of 2019 dented the fundamentals of the Key Performance Index but the downside impacts could be short lived as San Jose's new housing additions will likely not meet ultimate demand. The supply index held firm and might also aid in the rent growth index rebounding quickly.

No expansion in capital inflows in the past six months kept liquidity capped at 5 in the transaction section as the number of listed assets has not grown. However, for those deals that do come to market, pricing remains aggressive, which pushed down yield down back to 1.

Note: The Key Performance Index provides a metro-level relational benchmark scaled from 1-10 for five key metrics.

Key Performance Index



2020 Market Forecast

Employment
20,000 jobs
Metro **1.7%**
U.S. **1.0%**

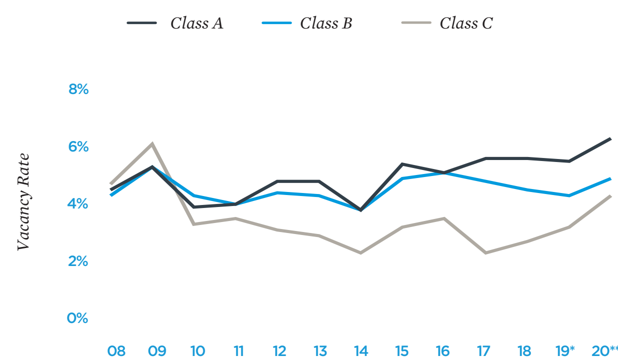
Construction
as % of inventory❖
Metro **3.1%**
U.S. **1.7%**

Class A Vacancy
Up 80 bps
Metro **6.2%**
U.S. **5.3%**

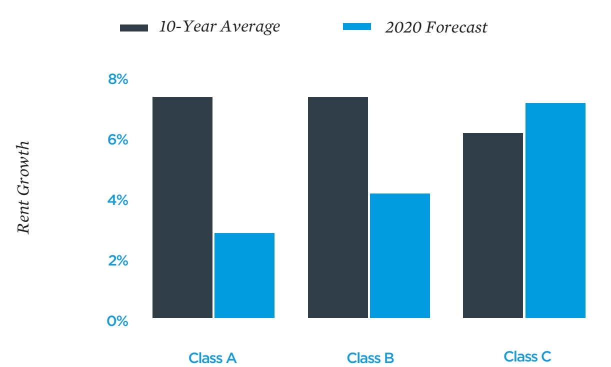
Class A Rent
$3,670 per month
Metro **2.8%**
U.S. **3.3%**

Investment
3-yr. avg. activity
$20+ million
Deals: **13**
Volume: **$1.1 billion**

Vacancy By Class



Rent Growth By Class



Jeffery J. Daniels
Senior Vice President
National Director IPA Multifamily
(212) 430-6127 | jdaniels@ipausa.com

** Estimate ** Forecast*
❖ Arrow reflects completions trend compared with 2019
Sources: Marcus & Millichap Research Services; CoStar Group, Inc.; RealPage, Inc.; Real Capital Analytics