MARKET REPORT

MULTIFAMILY

San Diego Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

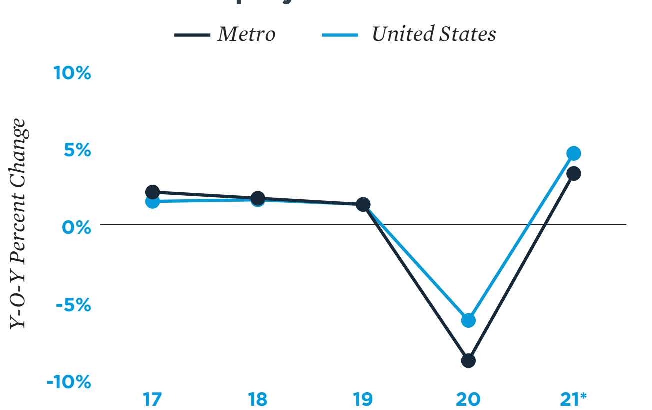
3Q/21

San Diego's Extremely Tight Suburban Vacancy Rate Revives Class B/C Investment Activity

Renters flock to lower-cost submarkets. After a historically strong second quarter the metro entered July with its lowest vacancy rate in nearly 20 years, highlighted by the performance of locales outside the city of San Diego. Over the past 12 months ended in June, six submarkets in South County, East County and along the 78 Corridor saw vacancy fall below 2 percent. Each area noted positive absorption in all four quarters, which supported an average annual rent gain of 8 percent. Despite this increase, average monthly rates in these submarkets are $100 to $450 per month below the metro mean. The lower costs of housing will continue to fuel robust demand for available units in these areas, potentially steering renters to more centrally located submarkets where vacancy is higher.

Development unable to keep pace with high-end demand. Surging home prices, limited single-family construction, and higher earning households' desire for flexibility have heightened luxury apartment demand in the county, placing Class A vacancy below 4 percent for the first time since 2008. This rate is positioned to remain tight in the near term, as most markets outside the city of San Diego, apart from Vista and Chula Vista, lack notable apartment pipelines. In the urban core, Downtown San Diego will add just 450 units in the second half. This lull in supply additions bodes well for the submarket as it was the only locale to record an increase in overall vacancy over the past year.

Employment Trends



* Forecast

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

Multifamily 2021 Outlook

46,000 JOBS
will be created

EMPLOYMENT:

San Diego records employment growth of 3.3 percent in 2021, allowing the metro to recapture roughly one-third of the 133,800 positions lost last year. This hiring activity will trail the national pace of increase, keeping unemployment slightly above the U.S. rate.

3,600 UNITS
will be completed

CONSTRUCTION:

For a fourth consecutive year developers complete more than 3,000 units, expanding the metro's rental inventory by 1.2 percent. Supported by completions in Mission Valley, Northeast San Diego adds more than 1,500 apartments.

70 BASIS POINT
decrease in vacancy

VACANCY:

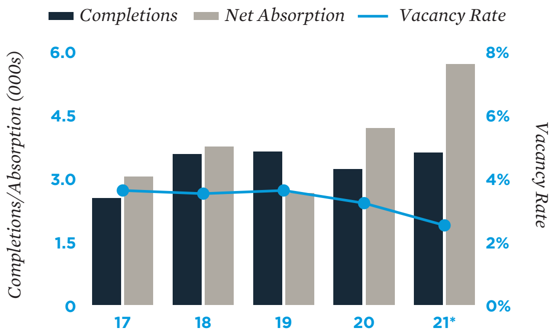
On net absorption of 5,700 units vacancy compresses to 2.5 percent, the lowest rate since 2000. By year-end, more than half of the metro's 13 submarkets could boast sub-2 percent vacancy, driven by strong demand for lower-cost rentals.

7.6% INCREASE
in effective rent

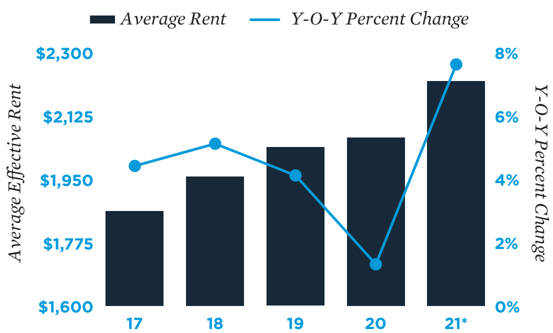
RENT:

Extremely tight vacancy outside Downtown San Diego will provide the impetus for strong rent growth. The metro's average effective rate will reach $2,220 per month by year-end, extending a stretch of positive rent growth that began in 2010.

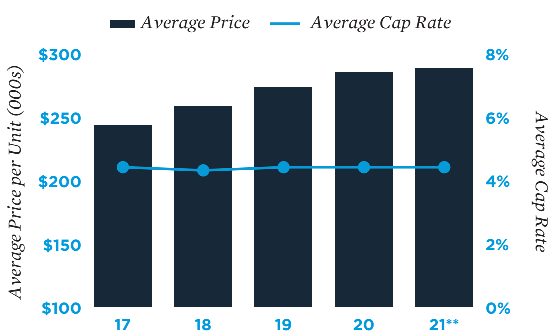
Supply and Demand



Rent Trends



Sales Trends



** Forecast; ** Through 2Q*

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

2Q21 — 12-Month Period

CONSTRUCTION

3,430 units completed

- The metro's rental inventory expanded by 1.1 percent over the past year ending in June. Roughly 1,520 units were completed during the second quarter, including 617 apartments at Diega in Downtown San Diego.
- Construction was underway on an additional 10,200 units at the onset of July with delivery dates extending into the first half of 2024.

VACANCY

160 basis point decrease in vacancy Y-O-Y

- Renters absorbed more than 8,300 units over the past 12 months, lowering vacancy to 2.6 percent. Ten of the metro's 13 submarkets recorded triple-digit compression during the yearlong stretch.
- Vacancy fell by more than 100 basis points in every apartment building tier, highlighted by a 190-basis-point drop in the Class B sector.

RENT

7.6% increase in the average effective rent Y-O-Y

- Positive rent growth was recorded across all submarkets over the past four quarters, lifting the average effective rate to a $2,164 per month.
- Rent growth was strongest along the 78 Corridor as Oceanside and Vista-San Marcos noted gains of 11.7 and 8.1 percent, respectively. Entering July, vacancy in both submarkets was 1.5 percent.

Investment Highlights

- Deal flow fell by 20 percent over the annual period ended in June as sales activity slowed notably during the third quarter of last year. Since, investor confidence and transaction velocity have improved. Driven by a rise in Class B/C executions, the January through June span was the strongest first half for closings in the past four years,
- Heightened competition for properties in areas of sparse vacancy pushed average pricing up 3 percent to $288,300 per unit. Despite this rise, the mean cap rate held at 4.4 percent, with maximum returns in most submarkets reaching the high-5 percent band.
- North Park and other neighborhoods near Balboa Park that are popular among millennials accounted for one-fourth of all closings over the past year. Here, smaller Class C complexes trade for an average of $320,000 per unit, with high-3 to mid-4 percent yields common.
- Buyers targeting comparable properties at lower price points and higher returns are most active in areas near San Diego State University and East County cities including El Cajon. The average price in this submarket is roughly $40,000 per unit below the metro average.

IPA Multifamily

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