

MARKET REPORT

MULTIFAMILY

San Francisco Metro Area

IPA

INSTITUTIONAL
PROPERTY
ADVISORS

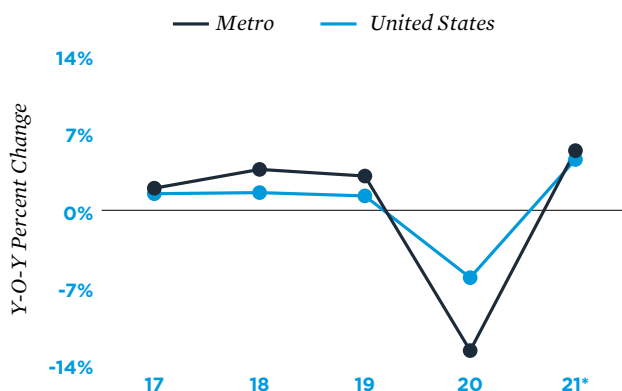
3Q/21

San Francisco Apartment Market Improves; Future Gains Will Be More Difficult

Late reopening drives recent apartment gains. Many of the big tech companies have asked workers to return to offices, though mandates are less widespread relative to Silicon Valley. Multifamily fundamentals improved faster than most expectations during the first half of the year, bringing the number of occupied units to within 1,500 apartments of the pre-pandemic level. The initial stages of the recovery were always going to be less challenging en route to the tight apartment market that existed prior to the recession. Gains should persist, but consistent new construction will generate pockets of weakness. More than half of the units underway are in SoMa, encouraging some operators to remain aggressive with concessions until apartment vacancy declines further.

Some clouds form on the horizon. Policy decisions could hamstring the rapid improvement in the apartment market. San Francisco has issued a vaccine mandate to visit most indoor establishments, including eating and drinking places, gyms, museums, theaters and entertainment venues. If the mandate ultimately hampers business activity, the need for workers in these establishments could slow the increase in apartment demand. Although more than 70 percent of eligible residents are fully vaccinated, San Francisco relies heavily on tourism. Between low international tourism and avoidance by unvaccinated visitors, new jobs for leisure and hospitality workers could grind to a crawl, slowing household formation until after restrictions are lifted.

Employment Trends



* Forecast

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

Multifamily 2021 Outlook



**56,000
JOBS**

will be created

EMPLOYMENT:

Following a 12.7 percent decline in 2020, employers will expand payrolls 5.4 percent in 2021. Many of those spots will be in the leisure and hospitality sector, which accounts for more than half of the unrecovered positions.



**3,250
UNITS**

will be completed

CONSTRUCTION:

Due to the prolonged nature of construction in the area, projects that were started prior to the health crisis will be completed this year, lifting inventory 1.4 percent in 2021. Last year, supply increased 1.8 percent.



**310
BASIS POINT**

decrease in vacancy

VACANCY:

The relatively rapid recovery in the local economy should continue in the second half of this year, pulling vacancy down to 7.5 percent. The rate more than doubled to 10.6 percent during 2020.



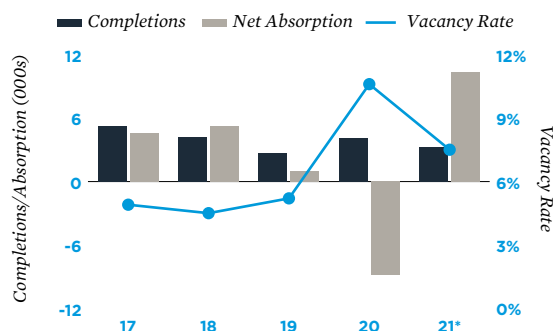
**8.4%
INCREASE**

in effective rent

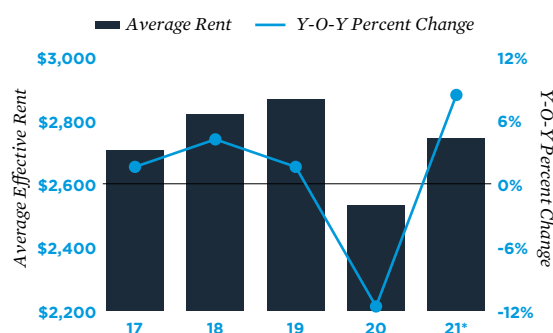
RENT:

Managers will lift the average effective rent to \$2,745 per month by year-end, only 4 percent below the pre-pandemic level. A rebound in Class A rent will be the primary driver in gains as employees return from remote work during the health crisis.

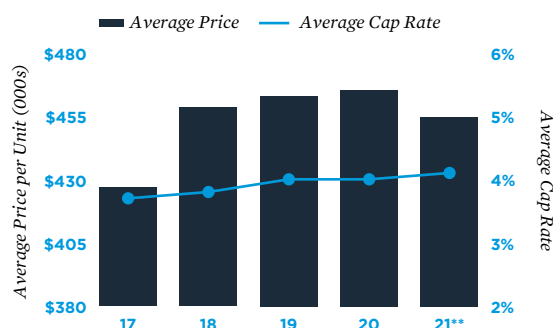
Supply and Demand



Rent Trends



Sales Trends



* Forecast; ** Through 2Q

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

IPA Multifamily

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Price: \$250

2Q21 — 12-Month Period



CONSTRUCTION

2,497 units completed

- Inventory only climbed 1.1 percent during the 12-month period ending at midyear. The completion of new units slowed dramatically during the first half of 2021 as just 419 doors were completed.
- Builders are taking a wait-and-see approach. In the first half of this year, new starts were roughly half the level at the same time in 2020.



VACANCY

20 basis point decrease in vacancy Y-O-Y

- The vacancy rate fell 150 basis during the second quarter to 7.9 percent as workers returned and development plummeted.
- Vacancy fell across all classes in the spring period, including a 280-basis-point decline at Class A properties. Class B and Class C recorded drops of 120 and 130 basis points, respectively.



RENT

1.0% decrease in the average effective rent Y-O-Y

- Although the average effective rent of \$2,727 per month is down from the same point last year, 2021 has been strong. Through the first six months of this year, the average effective rent jumped 7.7 percent.
- The return of many white-collar office positions pushed up Class A's average effective rent 17.5 percent in the opening half of 2021.

Investment Highlights

- Sales velocity declined by approximately 50 percent during the 12-month period ending at midyear. Much of the decline can be attributed to the uncertainty surrounding the pace of recovery along with an unwillingness of owners to list assets at prices that reflected the significant decrease in revenue during the health crisis.
- Year over year, the average per door price for San Francisco apartments dipped 2 percent to \$454,500, reflecting the lack of discounting over the past 12 months. Following healthy gains in fundamentals during the first half of 2021, price discovery may remain challenging in the coming months as valuations and operations remain disconnected.
- First-year returns were modestly trending higher even before the health crisis as underwriters considered the impact of new construction and a rent ceiling that was emerging. Since the trough in 2017, the average cap rate has climbed 40 basis points to a still-low 4.1 percent. Year over year, the rate inched up 10 basis points, partially reflecting the greater percentage of Class C properties that changed hands.

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. Note: Metro-level employment growth is calculated based on the last month of the quarter/year. Sales data includes transactions sold for \$1 million or greater unless otherwise noted. 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.; Real Capital Analytics; RealPage, Inc.

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