MARKET REPORT

MULTIFAMILY

San Jose Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

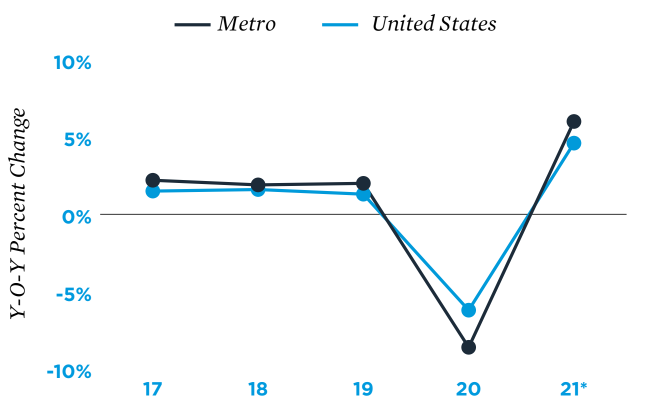
3Q/21

Apartment Market Turned Corner in Spring; Big Tech to Return in Fourth Quarter and Early 2022

Ongoing health crisis flattens multifamily recovery trajectory. The apartment market in the South Bay had a strong second quarter and was poised for continued momentum as Apple, Facebook and Google made plans to have their employees return to their campuses. However, the emergence of the delta variant and the rise in COVID-19 cases encouraged both Apple and Facebook to delay recalling employees until January of next year and Google to push back its full office opening until mid-October while also mandating vaccines for workers. Although the extensions will make the improvement in vacancy and rents more measured in the second half of 2021, the eventual return of employees to these economic anchors will prompt smaller firms to bring workers back to their offices.

Construction cycle looms as concern. Supply additions reach a peak this year and deliveries are anticipated to remain brisk again in 2022. The introduction of new Class A units will necessitate some concessions in areas with a high concentration of new inventory. This year, Central San Jose is the most supply burdened with projects such as the 28-story Miro towers being completed next to City Hall. Looking forward to 2022, development moves back toward the tech campuses. Mountain View-Palo Alto-Los Altos is scheduled to receive more than 1,400 doors and North Sunnyvale deliveries will approach 1,000 apartments. A return of workers to the nearby Google and Apple campuses could go a long way in reducing lease-up times.

Employment Trends



* Forecast

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

Multifamily 2021 Outlook

64,000 JOBS
will be created

EMPLOYMENT:

The employment base is anticipated to grow 6.0 percent this year as some of the major tech firms with campuses in the South Bay recall workers. The total number of jobs will be approximately 3 percent below the previous peak set in the fourth quarter of 2019.

5,350 UNITS
will be completed

CONSTRUCTION:

Led by additions in Central San Jose, apartment stock expands 3.0 percent this year as construction stays robust. In 2020, the delivery of nearly 4,200 units resulted in a 2.2 percent rise in South Bay inventory.

130 BASIS POINT
decrease in vacancy

VACANCY:

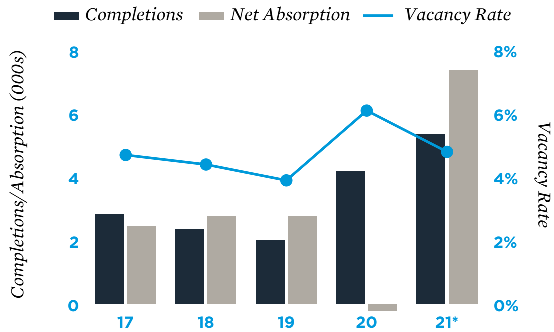
By year-end, the average vacancy rate will dip to 4.8 percent as conditions continue to improve. Vacancy is lower in submarkets farther away from Big Tech firms, a trend that should reverse in the coming quarters.

3.7% INCREASE
in effective rent

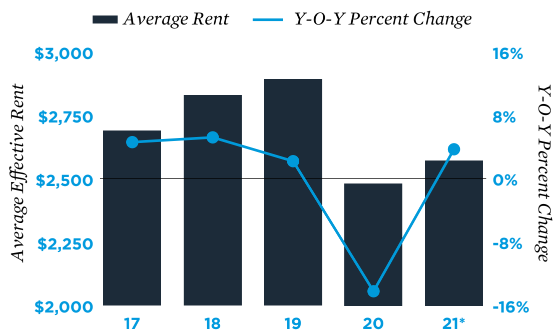
RENT:

The average effective rent is anticipated to finish the year at $2,572 per month, still 12.7 percent below the rate preceding the health crisis. Rents should record broader gains next year as the market inches closer to economic stabilization.

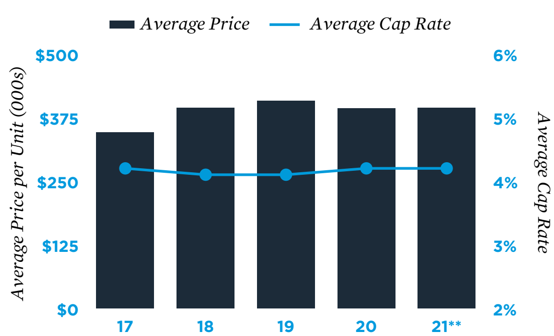
Supply and Demand



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

4,581 units completed

- Apartment development remains elevated in the South Bay as inventory climbed 2.6 percent in the yearlong period ending in the second quarter. In the prior 12 months, stock expanded by 1.6 percent.
- Construction will likely remain a challenge to fundamentals as nearly 8,500 units are underway, or 4.8 percent of inventory.

VACANCY

50 basis point increase in vacancy Y-O-Y

- In the second quarter, apartment vacancy plunged 100 basis points to 5.2 percent as job gains resulted in household creation.
- After peaking in this year's opening quarter, Class A vacancy tightened 150 basis points in the second quarter to 6.2 percent. The rate remains 180 basis points above the pre-pandemic level.

RENT

10.1% decrease in the average effective rent Y-O-Y

- Although rent is below the year-ago level, the average effective rate has reversed course and is climbing again. In the second quarter, renters paid an average of $2,545 per month, up 3.2 percent for the quarter.
- Submarkets near tech employers, including Mountain View-Palo Alto-Los Altos, recorded the largest decline in effective rent year over year.

Investment Highlights

- Investors expressed much greater confidence in the South Bay relative to San Francisco over the past year largely because of the more wide-open nature of the market. Deal flow declined approximately 10 percent during the recent 12-month period ending in June, relative to a 50 percent decline in neighboring San Francisco.
- Buyers paid an average price of $394,300 per unit during the yearlong period ending in June, approximately 2 percent lower than the prior four-quarter average. A portion of the decline in the average price is due to the decrease in Class A and B transactions. The number of Class C properties that changed hands remained constant year over year.
- The cap rates investors are willing to accept have remained consistent in the low-4 percent range since 2016. During the most recent 12-month period, the average first-year return was 4.2 percent, unchanged from the prior year. Thus far in 2021, some compression toward an average of 4.1 percent has been observed.