MARKET REPORT | 2Q/2020

NORTHMARQ

Inland Empire Multifamily

Activity Forecast to Gain Momentum in the Second Half

Highlights

- The Inland Empire multifamily market posted healthy levels of absorption and rent growth in the first half of 2020, although an active period of deliveries drove the local vacancy rate higher.
- Multifamily vacancy rose 20 basis points in the second quarter, reaching 3.8 percent. Year over year, the rate is up 50 basis points.
- While vacancy has crept higher, the Inland Empire has still recorded some of the healthiest rent growth in the country. Asking rents ended the second quarter at $1,454 per month, 4.4 percent higher than one year earlier.
- The investment market cooled in the first half, repeating a trend that has occurred in recent years. The median price is up 5 percent from the 2019 figure, reaching approximately $230,200 per unit.

Q2 Snapshot	Inland Empire Market
Market Fundamentals	
Vacancy	**3.8%**
- Year Over Year Change	**+50 bps**
Asking Rent	**$1,454**
- Year Over Year Change	**+4.4%**
Transaction Activity	
Median Sales Price Per Unit (YTD)	**$230,200**
Cap Rates (Avg YTD)	**4.9%**
Construction Activity	
Units Under Construction	**922**
Units Delivered YTD	**1,661**

Inland Empire Multifamily Market Overview

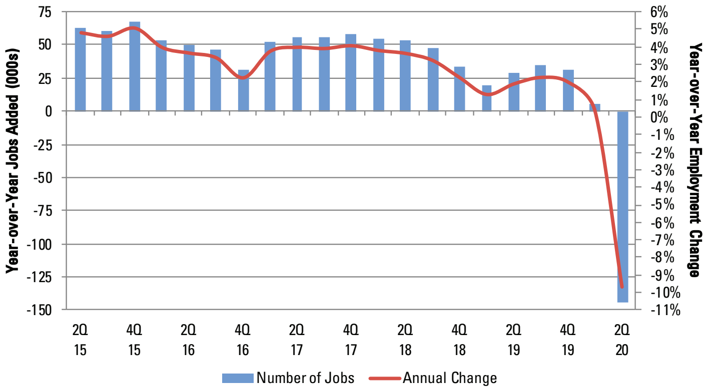
Apartment vacancy in the Inland Empire rose during the first half of the year, but the increase was more a result of inventory growth than a drop-off in renter demand. Net absorption of apartments was positive in the first half of 2020, totaling more than 1,000 units, ahead of the 2019 pace. While the market recorded job losses during the second quarter, the region's warehousing and distribution industry remains healthy. Amazon is the largest local employer, and the company has hired 3,700 workers in the Inland Empire thus far in 2020.

Multifamily investment activity in the Inland Empire got off to a slightly slower start to 2020, but in recent years, sales velocity has generally gained momentum as the year went on. During the first half of 2020, the COVID-19 outbreak likely pushed some transactions into the second half of the year. Pricing has continued to trend higher, despite a decline in the number of properties changing hands. The Inland Empire is typically the most active market in Southern California and will likely resume normal investment volume in the earlier stages of the recovery.

Employment

- The second quarter was a period of steep layoffs followed by re-staffing efforts in the Inland Empire. More than 190,000 jobs were cut in April, before nearly 50,000 jobs were added back to the market in the following two months. Year over year, local employment is down nearly 10 percent.
- While no industry has been insulated from the damage of the COVID-19 outbreak, the local construction sector has generally come back quickly. Local construction employment has recovered more than 85 percent of the industry jobs that were cut in the spring months.
- The Inland Empire's large warehousing and distribution industry continues to attract companies bringing jobs to the area. Sam's Club recently leased a 753,000-square-foot distribution facility in Perris, which will account for approximately 525 jobs. Amazon, the region's largest employer, continues to expand operations within the Inland Empire.
- **Forecast:** Employers are forecast to bring workers back to businesses in the second half of this year, but the exact pace of rehiring is uncertain. For the full year, net job losses of more than 3 percent are expected in the Inland Empire.

Employment Overview



Sources: NorthMarq, Bureau of Labor Statistics

The warehousing and distribution industry continues to attract companies, bringing jobs to the area

Vacancy

- Apartment vacancy rose 20 basis points during the second quarter, following an increase of 30 basis points in the first quarter. The rate ended the second quarter at 3.8 percent, 50 basis points higher than one year ago.
- Increases in 2020 follow an extended period of very stable vacancy. From the end of 2017 to the end of 2019, vacancy never rose above 3.5 percent or dipped below 3 percent.
- Additions to inventory drove the vacancy rate higher in Class A buildings during the first half of the year. The Class A vacancy rate rose 80 basis points in the first half of 2020, reaching 5.3 percent at midyear.
- **Forecast:** The local vacancy rate is expected to tick higher in the second half of the year, although the slowing pace of construction should limit supply-side pressures. Vacancy is forecast to end 2020 at 4.1 percent, an annual increase of 80 basis points.

Vacancy Trends

Sources: NorthMarq, Reis

Vacancy ended the second quarter at 3.8 percent, 50 basis points higher than one year ago

Rents

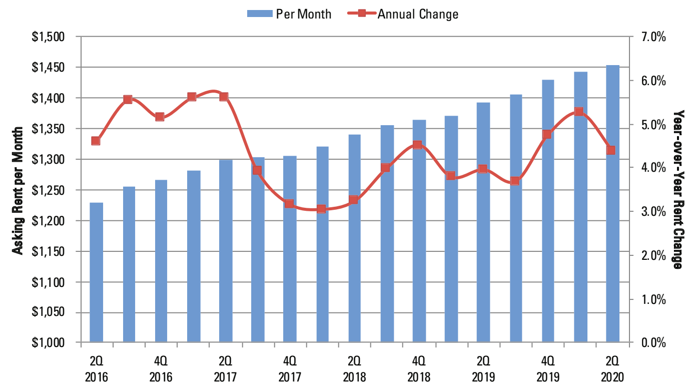
> Apartment rents in the Inland Empire have continued to rise, due in part to the influx of newer, more expensive units coming to the market. Asking rents rose 0.8 percent in both the first and second quarters, while rents in many markets contracted.

> Asking rents are up 4.4 percent year over year, ending the second quarter at $1,454 per month. This represents some of the strongest annual rent growth of any major market in the country.

> Rents have been rising in the lower property tiers, with renters seeking less expensive units finding few options. The average combined asking rents in Class B and Class C properties ended the second quarter at $1,279 per month, 4.2 percent higher than one year earlier.

> **Forecast:** Rents in the Inland Empire will likely level off in the second half, but gains in the first half should be maintained. Rent growth for 2020 should total approximately 1.5 percent to 2.0 percent.

Rent Trends



Sources: NorthMarq, Reis

Year over year through June, asking rents have expanded 4.4 percent

Development and Permitting

> Apartment deliveries spiked in the first six months of this year. Developers delivered approximately 1,660 units through the first two quarters, the fastest start to a year in more than a decade. Deliveries in the first half of 2020 nearly matched the total for the full year in 2019.

> The high volume of deliveries during the first half of 2020 thinned out the development pipeline. Projects totaling approximately 925 units are currently under construction, down more than 70 percent from last year.

> Multifamily permitting has been minimal in 2020. Developers pulled permits for fewer than 350 multifamily units in the first half of this year, lagging levels from the same period in 2019 by nearly 80 percent.

> **Forecast:** Developers are forecast to deliver projects totaling approximately 2,400 units in 2020, a figure that comes close to the combined total of new construction for the past two years. The bulk of the deliveries came online in the first half.

Development Trends

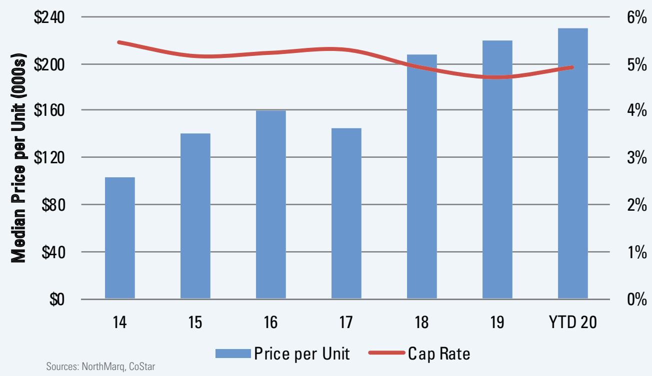
Sources: NorthMarq, Reis

Developers delivered approximately 1,660 units through the first two quarters

Multifamily Sales

- Since 2018, apartment sales in the Inland Empire have been concentrated in the second halves of years. That trend continued in 2020, with fewer than 10 significant properties changing hands. Sales velocity in the first half of this year lagged levels from the same period in 2019 by 23 percent.
- The median price in sales during the first half was approximately $230,200 per unit, up 5 percent from the median price in 2019.
- In the handful of deals that closed during the first half of the year, cap rates averaged approximately 4.9 percent, up 20 basis points from the 2019 average.

Investment Trends



Sources: NorthMarq, CoStar

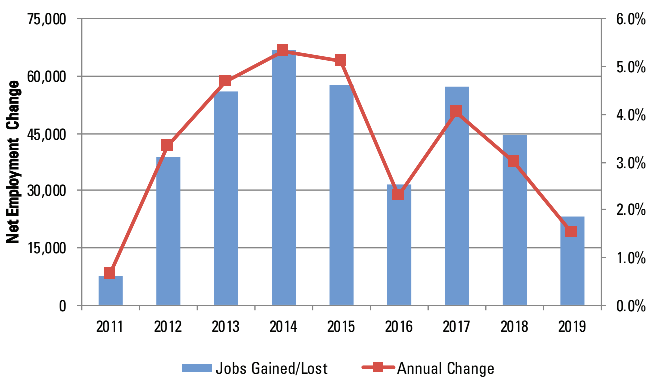
The median price in sales during the first half was approximately $230,200 per unit

Looking Ahead

The Inland Empire is consistently one of the stronger performing multifamily markets in the country, a trend that is likely to continue in the coming quarters. The local vacancy rate is expected to end 2020 slightly higher than the market's long-term average, the result of a short-term supply-demand imbalance brought about by a rise in deliveries and job losses related to the COVID-19 pandemic. Both of these trends are forecast to reverse course in the second half of the year. Employers are expected to bring back temporarily laid-off workers, while the pace of new apartment deliveries will cool.

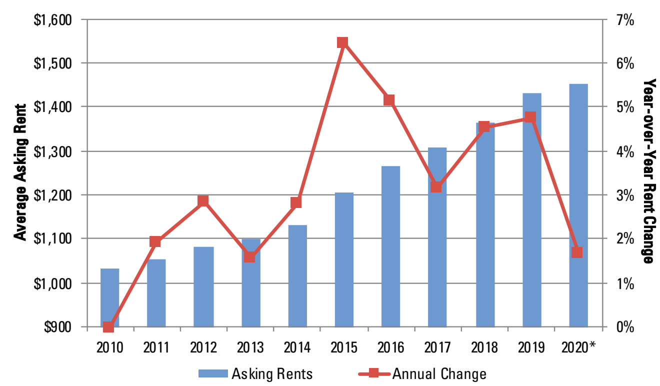
As operating conditions steady, sales velocity is expected to more closely resemble historical levels. In recent years, investment activity has been more robust in the third and fourth quarters, and that trend is likely to repeat in 2020, after a more modest start to the year. Assuming newer properties lease up successfully, this could produce an additional source of transaction activity in the second half of this year and into 2021. The local investment market will likely benefit as businesses bring employees back to work.

Employment Forecast



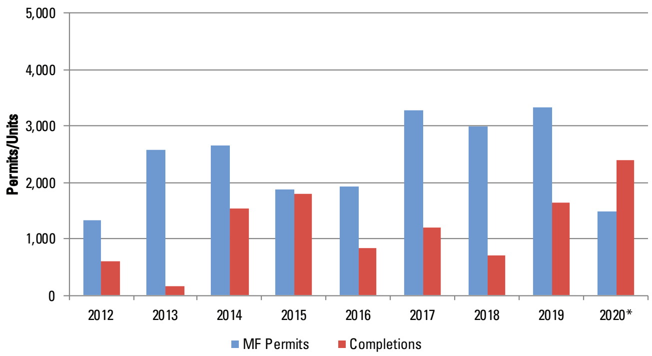
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



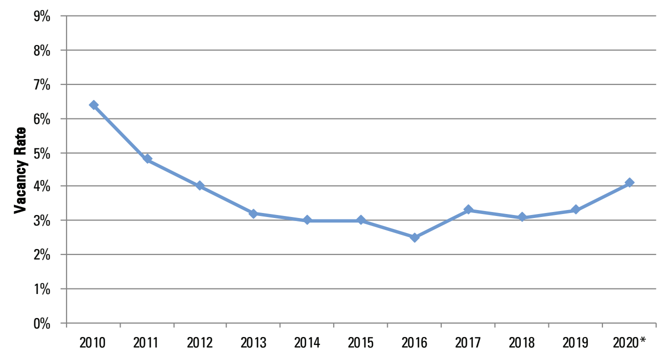
* Year End Forecast
Sources: NorthMarq, Reis

Construction & Permitting Forecast



* Year End Forecast
Sources: NorthMarq, Census Bureau, Reis

Vacancy Forecast



* Year End Forecast
Sources: NorthMarq, Reis

About NorthMarq

As a capital markets leader, NorthMarq offers commercial real estate investors access to experts in debt, equity, investment sales, and loan servicing to protect and add value to their assets. For capital sources, we offer partnership and financial acumen that support long- and short-term investment goals. Our culture of integrity and innovation is evident in our 60-year history, annual transaction volume of $14 billion, loan servicing portfolio of more than $61 billion and the multi-year tenure of our nearly 600 people.

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