Orange County Multifamily

NORTHMARQ

Orange County Maintains Tight Vacancy Levels

Highlights

- The Orange County multifamily market showed signs of weakening in the third quarter for the first time since the pandemic struck. Asking rents recorded a notable pullback, while the vacancy rate held steady.
- In each of the first three quarters this year, the local vacancy rate has been 3.6 percent. Year over year, vacancy has tightened 30 basis points.
- Current asking rents are $1,958 per month, down 2 percent from the second quarter. The quarterly retreat shifted year-over-year measurements into negative territory; asking rents in Orange County have declined by 1.2 percent in the past 12 months.
- Sales velocity in Orange County is typically modest, and COVID-19 has further stalled activity in the investment market. In the few deals that have closed, prices and cap rates have remained relatively steady compared with last year's numbers.

Q3 Snapshot	Orange County Market
Market Fundamentals	
Vacancy	**3.6%**
- *Year Over Year Change*	**-30 bps**
Asking Rent	**$1,958**
- *Year Over Year Change*	**-1.2%**
Transaction Activity	
Median Sales Price Per Unit (YTD)	**$287,300**
Cap Rates (Avg YTD)	**4.0%**
Construction Activity	
Units Under Construction	**3,704**
Units Delivered YTD	**1,126**

Orange County Multifamily Market Overview

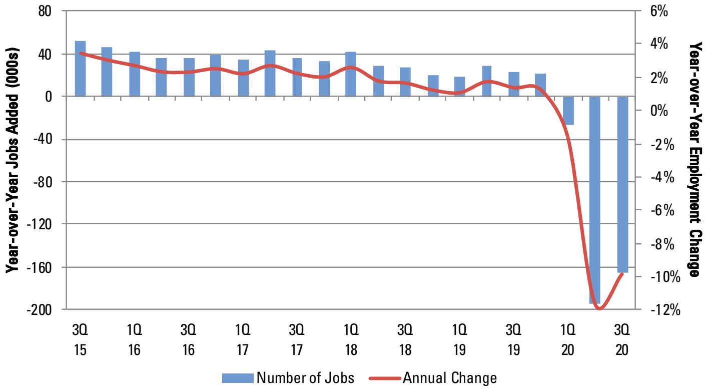
The Orange County multifamily market has posted mixed performance thus far in 2020. Vacancy has been very steady in recent quarters, and the rate has actually declined year to date and year over year. While apartment units have remained occupied, rental rates have declined as the pace of absorption has slowed. Declines in asking rents during the second quarter were fairly modest, but pricing pressure intensified during the past three months. Rents retreated more substantially during the third quarter, and current rents are lower than one year ago.

The investment market in Orange County largely paused during the second and third quarters, with transactions of properties consisting of 50 units or more slowing to a near crawl. There has been some activity in projects ranging from 20 units to 40 units in recent quarters, with private capital buyers active in sales less than $10 million. The current conditions are expected to be temporary, and as the local economy recovers, activity in institutional-grade properties is expected to stage a rebound.

Employment

- Employers in Orange County continued re-staffing efforts in the third quarter but at a slower pace than during the initial months of the recovery period. Employers added back approximately 31,000 jobs during the third quarter, but total employment in the area is still down 9.8 percent year over year.
- Orange County's large leisure and hospitality sector has been the source of approximately 40 percent of the total job losses in the area. Even after adding back nearly 40,000 jobs, employment in the sector is still down nearly 30 percent year over year.
- Local health officials recently gave clarity on reopening parameters for large theme parks such as Disneyland and Universal Studios, and an opening in 2020 is unlikely. Disneyland is the largest employer in Orange County with around 30,000 local workers prior to the health crisis.
- **Forecast:** Employment in Orange County is expected to contract by approximately 7 percent in 2020 before beginning to bounce back as a broader economic reopening occurs in 2021.

Employment Overview



Sources: NorthMarq, Bureau of Labor Statistics

Employers added back approximately 31,000 jobs during the third quarter

Vacancy

- Vacancy in Orange County has been consistent through the economic volatility. The local vacancy rate was 3.6 percent in the third quarter, matching the figure from each of the first two quarters of this year.
- The current vacancy rate is down 30 basis points from last year. This marked the fifth consecutive quarter in which vacancy rates in Orange County recorded a year-over-year decline.
- Vacancy in the Irvine submarket has declined 10 basis points year to date and is currently 5.5 percent. Irvine has been a particularly active submarket for new construction in recent years, and additional projects are forecast to come online in 2021.
- **Forecast:** The vacancy rate in Orange County is forecast to end 2020 at 4 percent, 30 basis points higher than at the end of last year. The year-end vacancy rate in 2018 was 4 percent.

Vacancy Trends

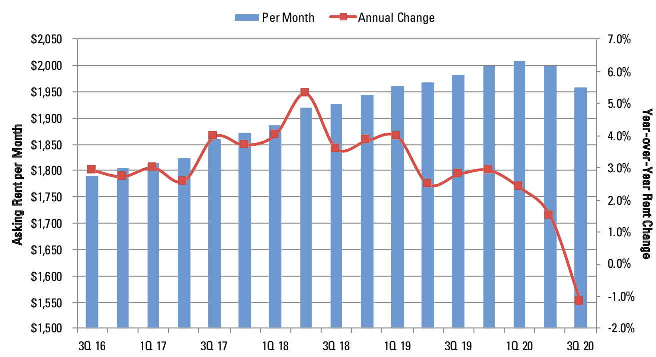
Sources: NorthMarq, Reis

The local vacancy rate was 3.6 percent in the third quarter

Rents

- Following a minor dip in the second quarter, rents fell at a steeper clip in the third quarter. Asking rents declined 2 percent from the second quarter to the third quarter, finishing at $1,958 per month.
- The recent quarterly declines have pushed current rents lower than levels from one year earlier. Year over year through the third quarter, asking rents are down 1.2 percent.
- Rents in some of the more expensive parts of Orange County have recorded more significant declines in recent periods. In the Newport Beach submarket, rents have declined 8.6 percent in the last 12 months and are currently $2,642 per month.
- **Forecast:** Asking rents in Orange County are forecast to decline approximately 2.5 percent in 2020, ending the year at $1,950 per month. Rents briefly topped $2,000 per month in late 2019 and early 2020.

Rent Trends



Sources: NorthMarq, Reis

Asking rents ended the third quarter at $1,968 per month

Development and Permitting

- New construction remained modest in the third quarter, and developers completed 290 apartment units, bringing the year to date total to more than 1,100 units. Apartment deliveries through the first three quarters are down 23 percent from the same period in 2019.
- There are significant projects in the future development pipeline. Multifamily projects totaling approximately 3,700 units are currently under construction in Orange County, up nearly 30 percent from one year earlier.
- Following consecutive years in 2018 and 2019 with no inventory additions, the Laguna Hills submarket accounted for nearly 50 percent of Orange County's total development this year, with more than 500 apartment units delivering in the region to this point in 2020.
- **Forecast:** Projects totaling approximately 2,000 units are scheduled to come online in 2020. This is nearly identical to the inventory growth recorded in 2019.

Development Trends

Sources: NorthMarq, Reis

The Laguna Hills submarket has accounted for nearly 50 percent of the county's total development this year

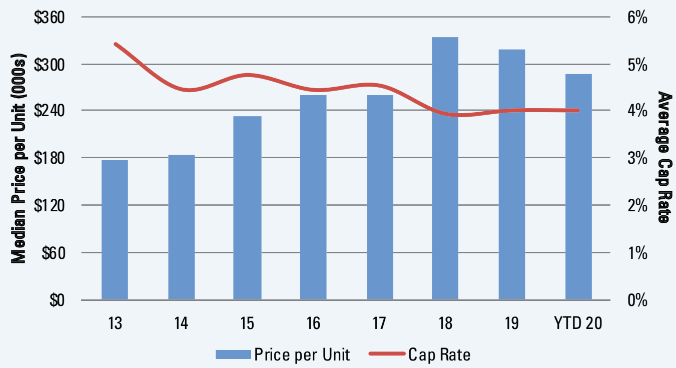
Multifamily Sales

> Sales velocity in Orange County is generally limited, and the recent economic volatility has further slowed deal flow in the market. No significant transactions took place in the third quarter, and only a few properties have changed hands this year.

> In the few deals that have closed thus far in 2020, the median price was $287,300 per unit, 10 percent below the figure from 2019.

> Cap rates have averaged approximately 4 percent year to date, similar to levels recorded during the past few years.

Investment Trends



Sources: NorthMarq, CoStar

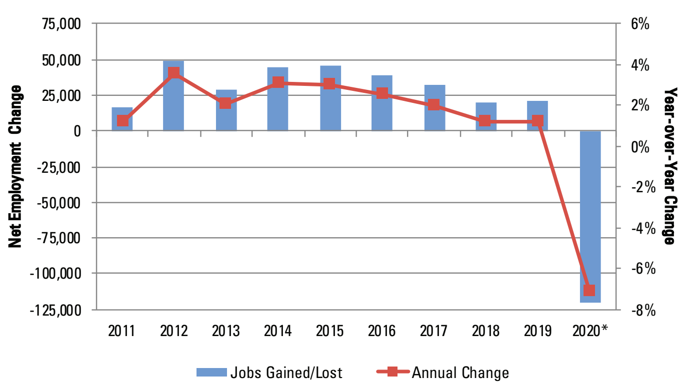
Cap rates have averaged approximately 4 percent year to date

Looking Ahead

The long-term demand drivers that support the Orange County multifamily market, including elevated home prices and a favorable quality of life, will remain in place through the remainder of this year and into 2021. These forces should support the market while the local employment outlook improves. While job losses have been severe and will linger into 2021, vacancy has remained in a tight range and local rent collections have generally outpaced national and statewide averages.

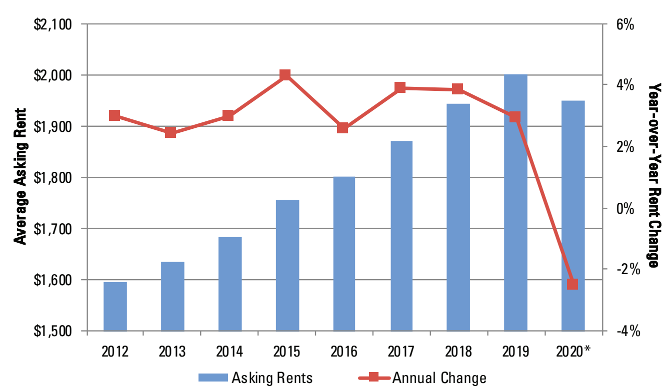
The same factors that are expected to support occupancy levels in Orange County should also stimulate investment demand going forward, but it may take a few more quarters. Investors will likely take a few more months to fully evaluate the impact of the coronavirus on property fundamentals, and a broader reopening of some of Orange County's hospitality businesses would strengthen investor sentiment. A lifting of economic uncertainty, perhaps aided by the passage of a second stimulus package, would likely allow local investment activity to gain momentum.

Employment Forecast



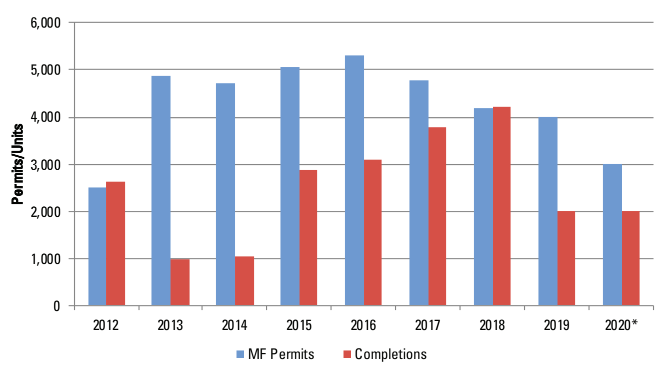
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



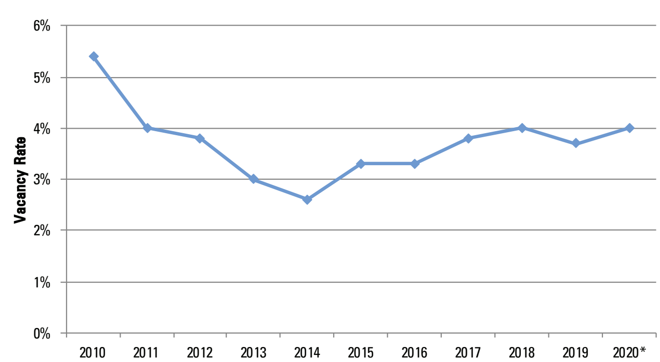
* Year End Forecast
Sources: NorthMarq, Reis

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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