Northmarq

CONSTRUCTION ACTIVITY

UNDER CONSTRUCTION	6.829
UNITS DELIVERED	2,368

MARKET FUNDAMENTALS

VACANCY RATE	3.0%
YEAR-OVER-YEAR CHANGE	-10bps
ASKING RENTS	$1,818
YEAR-OVER-YEAR CHANGE	+5.1%

TRANSACTION ACTIVITY (YTD)

MEDIAN PRICE PER UNIT	$334,500

Inland Empire Multifamily
4Q 2022

MARKET INSIGHTS

Tight operating conditions and ongoing demand fueling new development

HIGHLIGHTS

- Operating conditions cooled during the fourth quarter with rents declining and vacancy inching higher. After a slowdown in apartment deliveries in 2021, developers were more active in 2022 with the completion of roughly 2,370 units for the year. New construction will accelerate again in 2023.
- Local vacancy ticked higher before the end of 2022, rising 10 basis points during the fourth quarter to 3 percent. Despite the minimal increase at the end of the year, the rate still declined 10 basis points in 2022, the second consecutive year where conditions tightened.
- Rent trends were also mixed in 2022. For the full year, asking rents rose 5.1 percent to $1,818 per month. During the fourth quarter, however, rents dipped nearly 2 percent, offsetting some of the year's earlier gains.
- The multifamily investment market slowed in the final few months of the year even as pricing remained well above the 2021 figure. The median sales price in 2022 was $334,500 per unit, up 26 percent from the median price in 2021. Cap rates averaged around 3.75 percent during the fourth quarter.

INLAND EMPIRE MULTIFAMILY MARKET OVERVIEW

Following a very strong first three quarters of the year, operating conditions in the Inland Empire multifamily market softened a bit to close out 2022, with asking rents declining and the vacancy rate inching higher. Although vacancy ticked higher at the close of the year, the rate is in line with the long-term trend in the region. After more than 10 years of consistent rent increases, local apartment rents dropped during the final three months of 2022. Class A properties have recorded the strongest performance in recent periods, accounting for nearly all of the net absorption in recent quarters. The healthy renter demand, tight vacancies, and rising rents have continued to encourage developers to bring new units to the market.

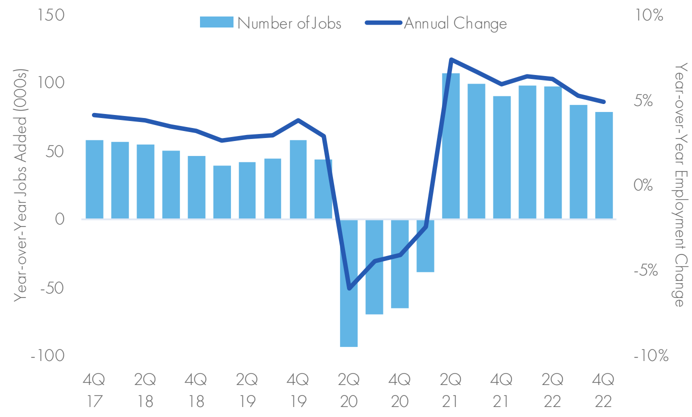
Multifamily sales activity slowed during the fourth quarter while deal volume for the full year fell nearly 40 percent from the 2021 total. Although the pace of deals slowed significantly in recent months, prices have remained elevated. The median sales price was $334,500 per unit, up 26 percent from the median price in 2021. While only a handful of properties changed hands during the fourth quarter, the transaction mix consisted almost entirely of Class B properties in San Bernardino. This followed a first half of the year where several properties changed hands throughout the region. Cap rates began to tick higher during the fourth quarter, averaging around 3.75 percent. Further increases may be necessary to stimulate deal flow.

EMPLOYMENT

- Employers continued to add workers to payrolls at a healthy pace throughout 2022. The local labor market grew by 11,600 positions in the fourth quarter, and for the full year, total employment advanced 4.8 percent with the addition of 78,500 jobs.
- The professional and business services sector was one of the strongest-performing industries in the past year. During the past 12 months, this sector added 13,700 jobs, an annual gain of 8 percent.
- Ongoing population growth in the region continued to support demand for health services. The Inland Empire's healthcare and social assistance sector expanded by 16,800 workers in 2022 and grew by nearly 7.2 percent.
- **FORECAST:** The local labor market is expected to continue to add workers in the year ahead, although the pace of growth will taper off from recent periods. Total employment is forecast to rise 1.2 percent in 2023 with the addition of 20,000 jobs.

The local labor market grew by 11,600 positions in the fourth quarter.

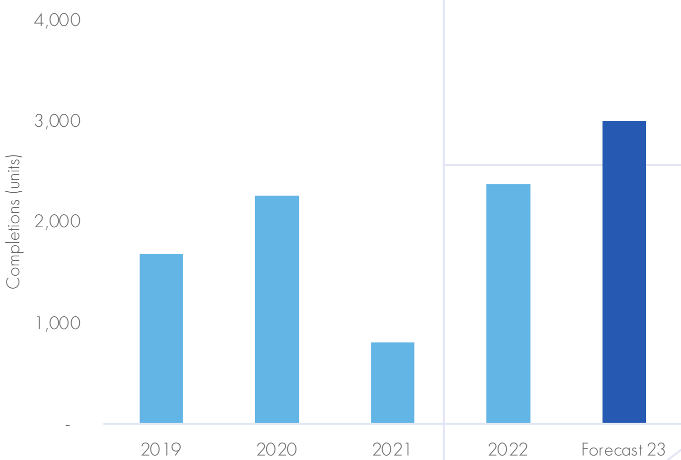
EMPLOYMENT OVERVIEW



Sources: Northmarq, Bureau of Labor Statistics

Projects totaling roughly 2,370 units were completed in 2022.

DEVELOPMENT TRENDS



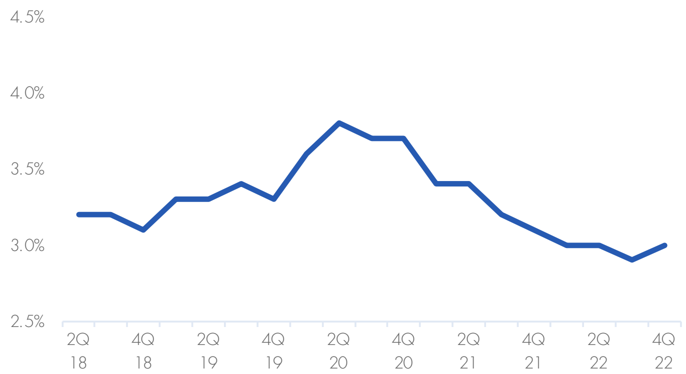
Sources: Northmarq, CoStar

DEVELOPMENT & PERMITTING

- Multifamily developers remained active in the final months of the year, completing more than 1,000 units during the fourth quarter. Projects totaling roughly 2,370 units were delivered in 2022, about 85 percent higher than the region's trailing five-year average.
- The construction pipeline has been expanding, with developers breaking ground on new projects in response to continued renter demand. At the end of 2022, more than 6,800 units were under construction, up 68 percent from one year earlier. Some of the more active areas for new development include Murrieta, Fontana, and Rancho Cucamonga.
- Multifamily permitting picked up in the final months of the year as developers pulled permits for more than 1,450 units during the fourth quarter, more than double the level of issuance in the previous period. Approximately 3,650 permits were issued in 2022.
- **FORECAST:** Apartment development activity is projected to remain elevated in the coming quarters. Projects totaling roughly 3,000 units are slated to come online in 2023.

Year over year, the vacancy rate is down 10 basis points.

VACANCY TRENDS



Sources: Northmarq, REIS

VACANCY

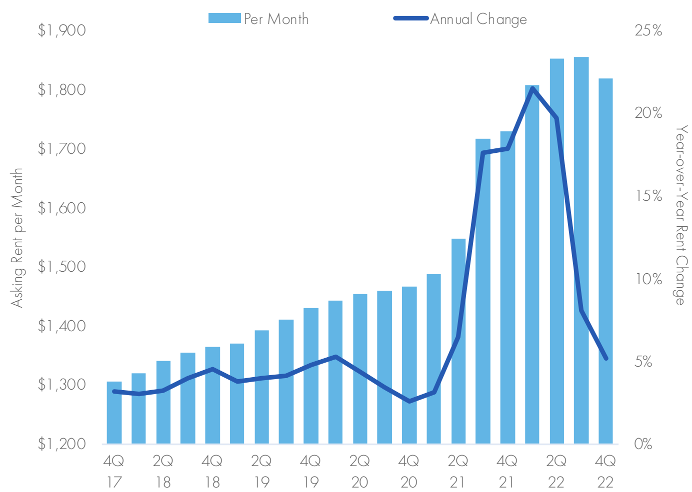
- The vacancy rate in the Inland Empire inched higher at the close of the year, rising 10 basis points during the fourth quarter to a still-tight 3 percent. The region's vacancy rate has averaged 3.3 percent during the past five years.
- Year over year, the rate is down 10 basis points. Some of the tightest vacancy rates are being recorded in the northern portion of the region including North Ontario and Fontana/Rialto, where rates are 1.6 percent and 1.7 percent, respectively.
- Renter demand continues to be concentrated in top-tier properties; the vacancy rate in Class A units fell 140 basis points in 2022 to 2.8 percent.
- **Forecast:** Local vacancy is projected to inch higher in 2023 as delivery activity picks up. The vacancy rate is projected to rise 20 basis points, finishing the year at 3.2 percent.

RENTS

- Following more than a decade of consistent rent growth, asking rents declined during the fourth quarter. Local apartment rents fell nearly 2 percent in the final months of 2022 to $1,818 per month.
- Despite the decline in the final quarter, asking rents advanced 5.1 percent in 2022. This pace of growth is consistent with the market's long-term rate; during the past decade, local rent growth has averaged 5.2 percent per year.
- Local apartment rents trended higher at a healthy pace across all asset classes during the past year. The largest gains occurred in upper-tier properties where asking rents in Class A units rose 5.8 percent in 2022 to $2,175 per month.
- **Forecast:** Apartment rents are projected to tick higher in the coming quarters, although annual rent growth in 2023 will be much more modest than in recent years. Asking rents are forecast to rise 2.6 percent in 2023, finishing the year at around $1,865 per month.

Asking rents advanced 5.1 percent in 2022.

RENT TRENDS



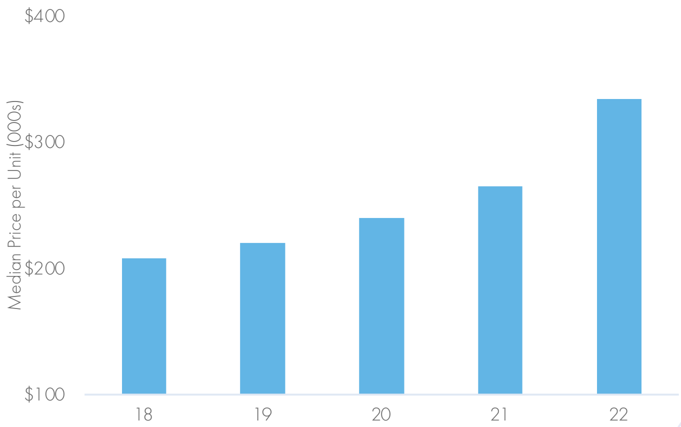
Sources: Northmarq, REIS

MULTIFAMILY SALES

- Deal volume slowed significantly during the fourth quarter as only a handful of properties traded in the final months of the year. The number of sales in 2022 declined nearly 40 percent from the 2021 total. Activity levels above $100 million were fairly consistent from 2021 to 2022, although the bulk of these sales occurred in the first half of the year.
- While fewer properties are changing hands, per-unit pricing rose significantly during the past 12 months. The median sales price through the end of 2022 was $334,500 per unit, up 26 percent from the 2021 figure.
- Cap rates have trended slightly higher during the final quarter of 2022 but remain low compared to bond yields. Most of the properties that sold during the last three months of 2022 recorded cap rates between 3.5 percent and 4 percent.

The median sales price was $334,500 per unit.

INVESTMENT TRENDS



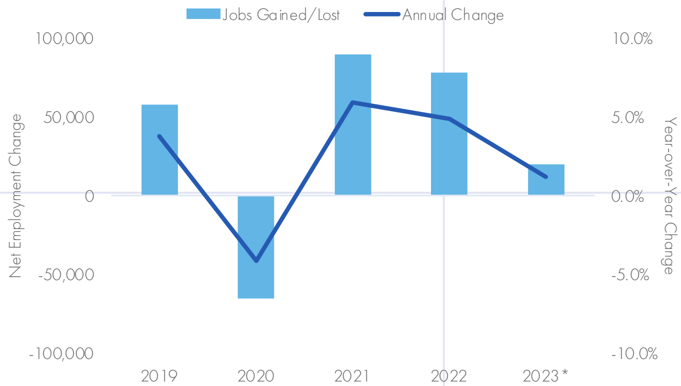
Sources: Northmarq, CoStar

LOOKING AHEAD

Supported by a strong local economy and consistent population growth, property fundamentals in the Inland Empire are set for healthy performance in 2023. After declining in recent months, asking rents should tick higher by the end of the year with expected annual gains of around 2.5 percent. Following a spike in multifamily permitting and an expanding construction pipeline in the last few quarters, apartment developers are expected to be extremely active in 2023. Projects totaling nearly 3,000 units are scheduled to come online in the year ahead, an annual increase of about 25 percent. As the pace of supply growth picks up, vacancy should inch marginally higher but will remain in the low-3 percent range.

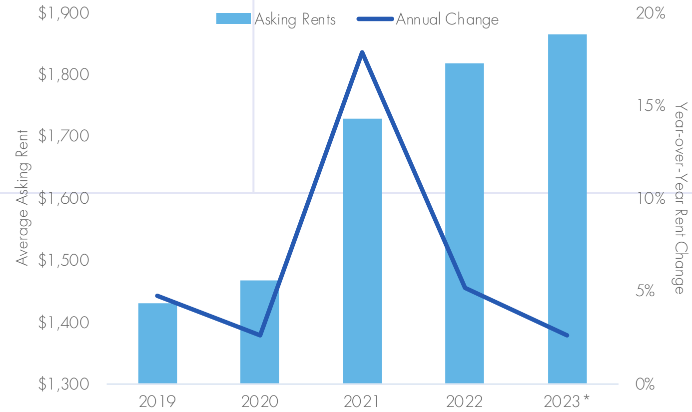
Investment activity is projected to be limited in the first half but should eventually gain momentum in 2023. The factor likely to have the greatest impact on sales velocity is the cost of financing, which has pushed higher throughout the past several months, while cap rates have been slower to trend higher. This disconnect has hampered transactions, despite a favorable outlook for the Inland Empire region as a whole. Overall property fundamentals remain strong, and with modest gains expected in the coming quarters, investor sentiment should be positive. As buyers and sellers adjust expectations, cap rates are projected to trend closer to 4 percent or higher.

EMPLOYMENT FORECAST



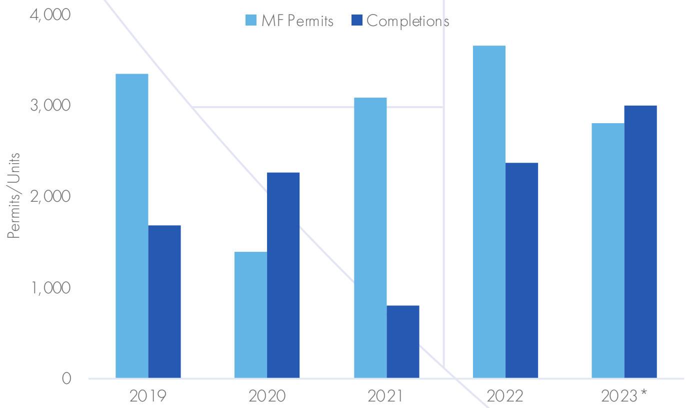
* *Year End Forecast*
Sources: Northmarq, Bureau of Labor Statistics

RENT FORECAST



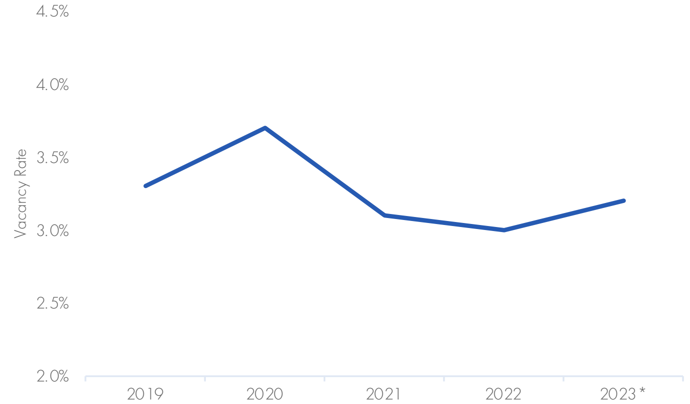
* *Year End Forecast*
Sources: Northmarq, REIS

CONSTRUCTION & PERMITTING FORECAST



* *Year End Forecast*
Sources: Northmarq, Census Bureau, CoStar

VACANCY FORECAST



* *Year End Forecast*
Sources: Northmarq, REIS

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FOR MORE INFORMATION, PLEASE CONTACT:

SHANE SHAFER
SVP, Managing Director–Investment Sales
949.270.3690
sshafer@northmarq.com

DAVID BLUM
SVP, Managing Director–Debt & Equity
949.717.5215
dblum@northmarq.com

JOE GIORDANI
Managing Director–Debt & Equity
949.717.5208
jgiordani@northmarq.com

PETE O'NEIL
Director of Research
602.508.2212
poneil@northmarq.com

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