Northmarq

MARKET INSIGHTS

Sales activity limited to Class C assets to start 2023

CONSTRUCTION ACTIVITY

UNDER CONSTRUCTION	6,461
UNITS DELIVERED	439

MARKET FUNDAMENTALS

VACANCY RATE	3.1%
YEAR-OVER-YEAR CHANGE	+10bps
ASKING RENTS	$1,809
YEAR-OVER-YEAR CHANGE	+0.1%

TRANSACTION ACTIVITY (YTD)

MEDIAN PRICE PER UNIT	$240,600

Inland Empire Multifamily
1Q 2023

HIGHLIGHTS

- Apartment operating conditions in the Inland Empire softened slightly in the first quarter, as asking rents inched lower, and vacancy ticked higher. Still, most current performance metrics are closely tracking levels from one year earlier.
- Local vacancy inched up at the start of the year but remained in its recent range. The rate rose 10 basis points during the first quarter to 3.1 percent and is also just 10 basis points higher than one year ago.
- Asking rents dipped lower during the first quarter, falling 0.5 percent to $1,809 per month. Average rents are up just $2 per month from one year ago.
- Investment activity in the first quarter was limited to a handful of Class C properties. The median sales price was $240,600 per unit, while cap rates averaged 4.1 percent to start the year.

INLAND EMPIRE MULTIFAMILY MARKET OVERVIEW

Operating conditions in the Inland Empire multifamily market were fairly consistent from the end of 2022 through the beginning of this year, highlighting the traditional stability that is a prevailing feature of the area. Vacancy has remained in a tight range, and the current rate is only 10 basis points higher than one year ago. Rent trends have been mixed, declining in each of the past two quarters after significant gains in 2021 and 2022. With vacancy consistently low and forecasts calling for continued population growth, multifamily developers are increasing activity. While the bulk of the development pipeline consists of garden-style and low-rise apartments, there are a handful of single-family rental communities under construction, including developments that will be completed later this year in Perris and La Quinta.

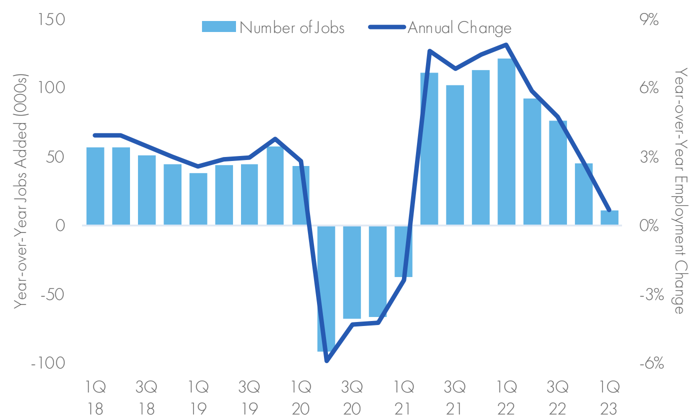
Multifamily sales activity in the Inland Empire has been fairly limited during the past 12 months, as only a handful of properties changed hands in each quarter. With only a small number of deals in the first three months of 2023, pricing crept lower as a result of the older mix of properties that sold. Nearly all the properties that traded in the first quarter were Class C assets. This is in contrast to recent years, when Class A and Class B assets accounted for between 50 percent and 65 percent of transactions per year. Cap rates continued to tick higher to this point in the year, averaging 4.1 percent during the first quarter. Cap rates are up roughly 35 basis points from the previous quarter with further increases expected in the coming periods.

EMPLOYMENT

- The labor market in the Inland Empire continues to expand but at a slower pace. During the 12-month period ending in the first quarter, area employers added 11,000 positions, a gain of 0.7 percent.
- While growth has slowed in many industries, the healthcare and social assistance sector continued to add workers. Growth totaled 3.9 percent during the past 12 months with the addition of 9,500 healthcare positions.
- The 2,600-acre, 40-million-square-foot World Logistics Center is scheduled to break ground in Moreno Valley by the end of 2023. The project is expected to deliver approximately 6 million square feet of industrial space per year through 2030, supporting construction jobs and logistics positions. Skechers has committed to 1.8 million square feet in the first phase.
- **FORECAST:** Local employers are projected to add jobs in the coming periods, but the pace of growth will be fairly modest. Total employment is forecast to grow by 0.6 percent in 2023 with the addition of 10,000 workers.

Year over year, area employers added 11,000 positions.

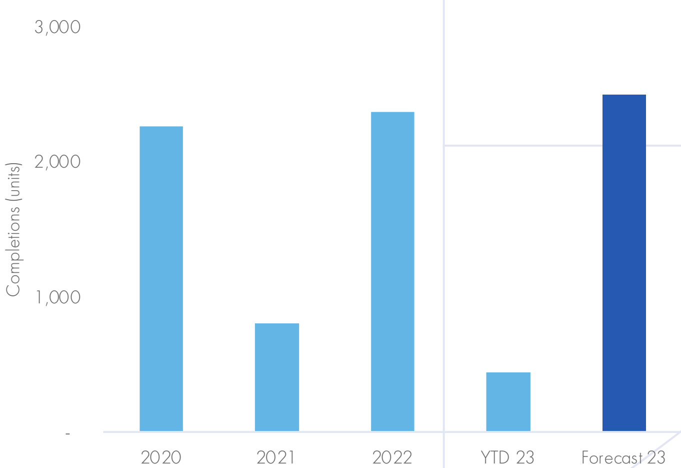
EMPLOYMENT OVERVIEW



Sources: Northmarq, Bureau of Labor Statistics

Approximately 440 units were completed during the first quarter.

DEVELOPMENT TRENDS



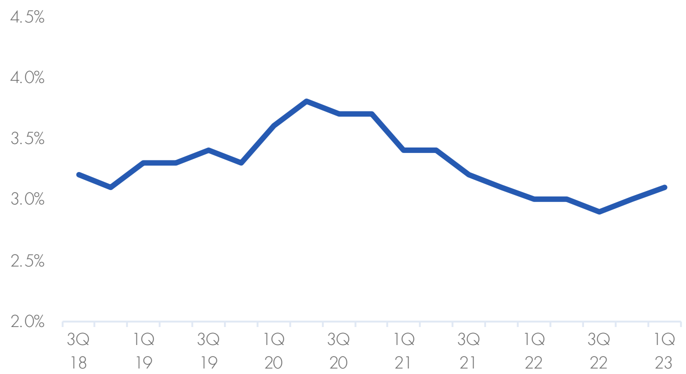
Sources: Northmarq, CoStar

DEVELOPMENT & PERMITTING

- Multifamily developers continue to bring new projects online as approximately 440 units were completed during the first quarter. The pace of deliveries is scheduled to accelerate in the coming months, and completions in 2023 should closely track levels from last year.
- The development pipeline expanded in recent quarters. Projects totaling 6,461 units are currently under construction throughout the Inland Empire, up nearly 45 percent from the same period last year.
- Developers pulled permits for roughly 1,930 multifamily units in the first quarter, more than double the levels from the same period in 2022. Multifamily permitting levels have likely peaked, and activity is expected to cool in the coming quarters.
- **FORECAST:** Apartment construction activity is set to gain momentum in the remainder of the year with projects totaling nearly 2,500 units slated to come online in 2023.

Class A vacancy ended the first quarter at 2.1 percent.

VACANCY TRENDS



Sources: Northmarq, REIS

VACANCY

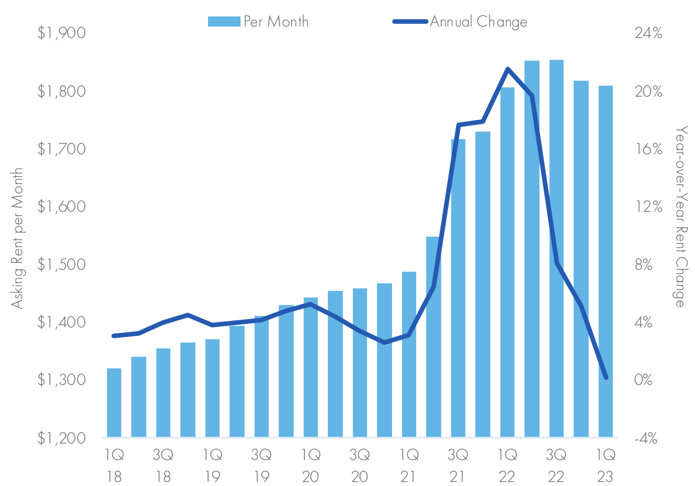
- The vacancy rate inched higher, rising 10 basis points in the first quarter to 3.1 percent. This was the second consecutive quarter when the rate inched up 10 basis points, following declines in four of the past five quarters.
- Year over year, the local vacancy rate increased by just 10 basis points. Despite some quarterly movement, vacancy in the Inland Empire typically operates in an extremely tight range between 3 percent and 3.5 percent.
- Absorption levels continue to be heavily concentrated in newer, Class A properties. The vacancy rate in upper-tier units fell 150 basis points in the past year, ending the first quarter at 2.1 percent.
- **FORECAST:** Vacancy is projected to tick higher in the coming quarters as construction activity picks up. Area vacancy is expected to rise 30 basis points in 2023 to 3.3 percent. The rate tightened in both 2021 and 2022.

RENTS

- Apartment rents in the Inland Empire dipped 0.5 percent in the last three months to $1,809 per month. Following robust rent growth in recent years, asking rents have now inched lower in each of the past two quarters.
- With the recent declines, current asking rents are nearly identical to levels from one year ago. Year over year, average rents are up just $2 per month, an annual growth rate of just 0.1 percent.
- Rents in the region's most expensive submarket, South Ontario/Chino, have continued to push higher in the past year. Average asking rents in this submarket rose nearly 1.5 percent in the past 12 months to $2,398 per month.
- **FORECAST:** Local apartment rents are forecast to inch higher in the remainder of the year. Asking rents are expected to rise 1.5 percent in 2023, ending the year at around $1,845 per month. Historically, rent growth in the region has averaged closer to 3.5 percent to 4 percent per year.

Asking rents are expected to rise 1.5 percent in 2023.

RENT TRENDS



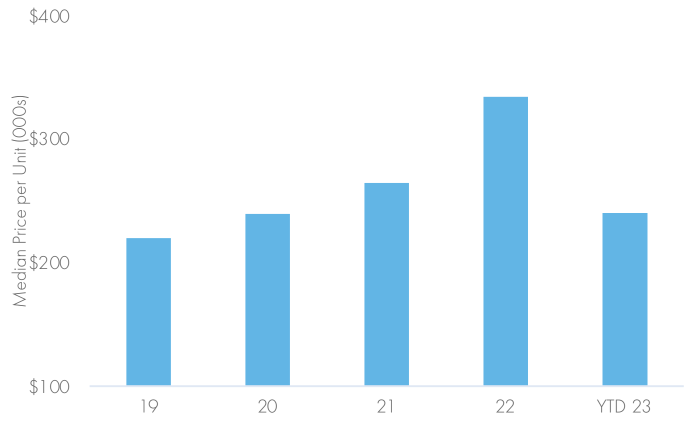
Sources: Northmarq, REIS

MULTIFAMILY SALES

- After a significant drop in the number of transactions last year, multifamily sales activity continues to be fairly limited to this point in 2023. Only a handful of properties changed hands during the first quarter, closely tracking levels recorded at the end of last year.
- The median sales price in the small number of deals during the first quarter was $240,600 per unit, after prices topped $330,000 per unit in 2022. Current pricing is closer to levels recorded from 2019 to 2021.
- The mix of properties that have changed hands to this point in the year has heavily influenced pricing. During the first quarter, Class C properties accounted for nearly all of the sales, which was a switch from prior periods. In recent years, Class A and Class B properties have combined to account for more than half of the annual transaction activity.
- Cap rates continued to tick higher in recent months, averaging 4.1 percent during the first quarter. Cap rates are up roughly 35 basis points from the end of last year.

Cap rates averaged 4.1 percent in the first quarter.

INVESTMENT TRENDS



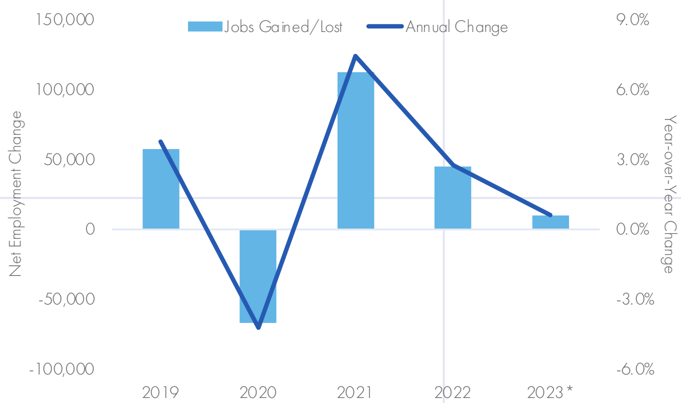
Sources: Northmarq, CoStar

LOOKING AHEAD

Despite some softening property fundamentals in recent quarters, the Inland Empire is expected to remain one of the top-performing markets in the West for the next few years. Optimism is fueled by the region's more favorable growth profile than nearby markets. Current operators are confident that the extremely tight occupancy conditions will eventually push rents higher, although gains in the near term will be modest. The region routinely has one of the lowest and steadiest vacancy rates in Southern California, while also featuring the fastest population growth in the region. Developers will move to meet the demand, with projects totaling approximately 2,500 units slated to come online in 2023, a slight increase from the delivery total last year.

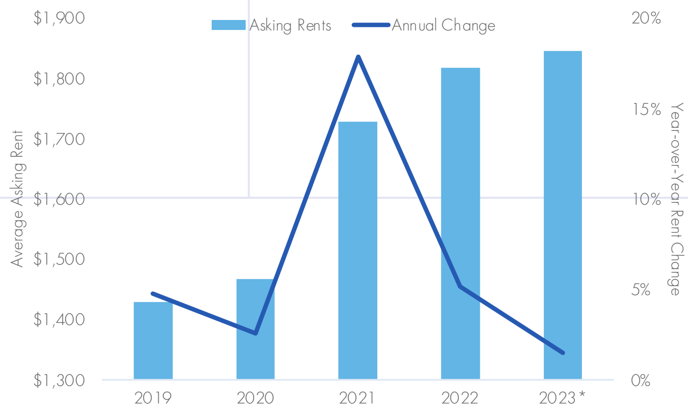
Multifamily investment activity in the Inland Empire will likely remain measured in the next few months before picking up sometime in the second half of the year. With the cost of capital on the rise and lenders tightening standards, there may not be an in-place driver fueling transaction volume in the near term. Still, the region has a growth trajectory that will appeal to investors, and the Inland Empire often records the fastest rate of multifamily sales velocity in Southern California. Cap rates are trending higher, and additional increases could reach levels that entice some buyers to move off the sidelines before year end. Investors waiting for a wave of distress to come to the market are not expected to find many opportunities in 2023.

EMPLOYMENT FORECAST



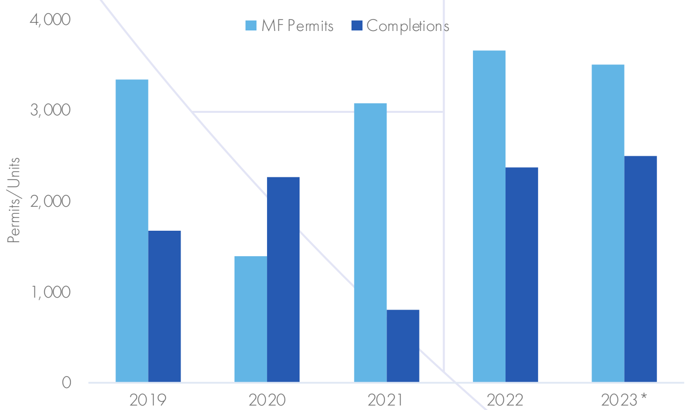
* Year End Forecast
Sources: Northmarq, Bureau of Labor Statistics

RENT FORECAST



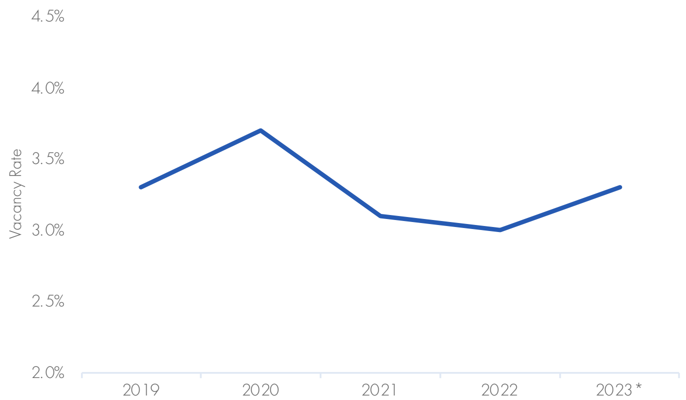
* Year End Forecast
Sources: Northmarq, REIS

CONSTRUCTION & PERMITTING FORECAST



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

VACANCY FORECAST



* Year End Forecast
Sources: Northmarq, REIS

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