Northmarq

MARKET INSIGHTS

Rent growth resumes, even as vacancies push higher

CONSTRUCTION ACTIVITY

UNDER CONSTRUCTION	37,475
UNITS DELIVERED	7,475

MARKET FUNDAMENTALS

VACANCY RATE	3.8%
YEAR-OVER-YEAR CHANGE	+20bps
ASKING RENTS	$2,380
YEAR-OVER-YEAR CHANGE	+2.9%

TRANSACTION ACTIVITY (YTD)

MEDIAN PRICE PER UNIT	$283,300

Southern California Multifamily
2Q 2023

HIGHLIGHTS

- Operating conditions in Southern California were mixed through the first half of 2023 as vacancy conditions ticked higher and asking rents rose. Developers remain active with projects totaling 37,475 units currently under construction throughout the region.
- Asking rents in Southern California trended higher during the second quarter; rents in the region rose 1.6 percent to $2,380 per month. Year over year, average rents are up 2.9 percent. Rent trends in Class A properties have been mixed. Class A asking rents in San Diego have posted healthy gains, but top-tier rents in the other Southern California markets have recorded minimal increases or modest declines during the past year.
- Overall vacancy conditions inched higher in recent months, rising 20 basis points during the second quarter to 3.8 percent. The current vacancy rate is also up 20 basis points year over year. Operating conditions in Class B and Class C properties remain very tight, with vacancy averaging about 2 percent. Class A vacancies reached 5.6 percent at midyear, with Los Angeles and San Diego having the highest rates.
- Fewer multifamily properties sold in Southern California during the second quarter than in the first three months of the year. Cap rates have edged higher in recent quarters, and prices have dipped. The median sales price year to date is $283,300 per unit, while most properties are selling with cap rates between 4 percent and 5.5 percent.

SOUTHERN CALIFORNIA MULTIFAMILY MARKET OVERVIEW

Property fundamentals in Southern California were generally mixed during the second quarter with vacancy ticking higher and asking rents also rising. The regional vacancy rate reached 3.8 percent, 20 basis points higher than in the first quarter. The lowest vacancy rates are being recorded in the Inland Empire, where the rate held steady at 3.1 percent during the second quarter. While vacancy conditions softened a bit, rents trended higher across the region. Asking rents in Southern California rose 1.6 percent in the second quarter to $2,380 per month. Apartment developers ramped up activity in recent months with projects totaling 7,475 units delivered in the first half of the year. The trend of accelerating supply growth will continue through the second half of this year and into 2024, with more than 37,000 units currently under construction.

While multifamily properties throughout much of Southern California are generally posting healthy operational performance, sales velocity has continued to slow during the past few quarters. The number of transactions during the second quarter fell 50 percent from the first three months of the year and is down 70 percent from one year ago. Investment activity is being hindered by an environment where interest rates have pushed higher at a faster rate than cap rates have increased. In transactions that have executed, most properties traded with cap rates between 4 percent to 5.5 percent after averaging closer to 3.5 percent one year ago. The combined forces of rising cap rates and fewer transactions have resulted in a decline in prices; the median sales price thus far in 2023 is $283,300 per unit, down 15 percent from the median price last year.

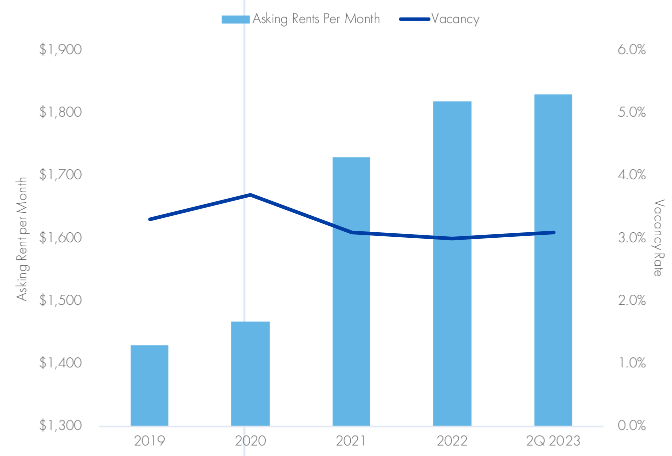
INLAND EMPIRE

CONSTRUCTION/VACANCY/RENTS

- Apartment development activity in the Inland Empire has been fairly light in the first half of 2023 with 660 units coming online year to date. The pace of completions should accelerate in the coming periods with projects totaling 6,887 units currently under construction, up 42 percent from one year ago.
- Vacancy conditions in the Inland Empire typically operate in a tight range, a trend that has continued to this point in 2023. The local vacancy rate finished the second quarter at 3.1 percent, matching the figure from the first three months of the year.
- Apartment rents trended higher during the second quarter, after retreating for two consecutive quarters. Asking rents rose 1.1 percent in the last three months to $1,830 per month. Despite the recent uptick, asking rents in the Inland Empire are down 1.2 percent from one year ago.
- **FORECAST:** Apartment construction activity is set to gain momentum in the second half of the year with projects totaling nearly 2,500 units slated to come online in 2023. As construction activity picks up, area vacancy is expected to inch higher, reaching 3.3 percent. Rents in the Inland Empire are projected to end the year at $1,855 per month.

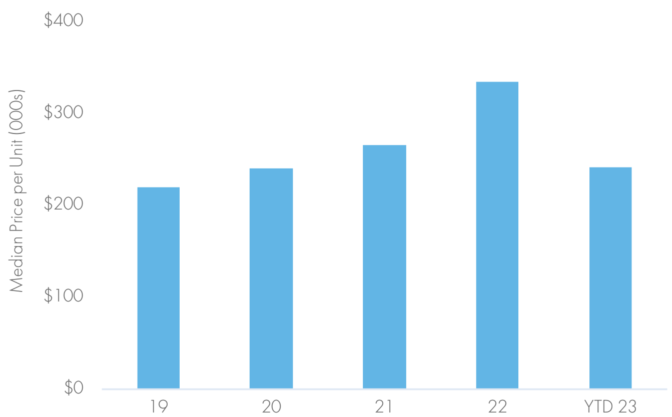
The vacancy rate finished the second quarter at 3.1 percent.

VACANCY & RENT TRENDS



Sources: Northmarq, Reis

SALES TRENDS



The median sales price to this point is $240,600 per unit.

MULTIFAMILY SALES

- Although sales activity accelerated slightly from the first quarter to the second quarter, overall deal volume remains limited in the Inland Empire. The number of transactions in the first half of 2023 fell 50 percent from the same period last year.
- The median sales price to this point in the year is $240,600 per unit, down 28 percent from the 2022 figure. In the second quarter, prices rose; the median price was more than $323,000 per unit in the handful of transactions that closed in the second quarter.
- Cap rates continued to edge higher, averaging 4.5 percent during the second quarter. Cap rates have increased by approximately 40 basis points from earlier this year.

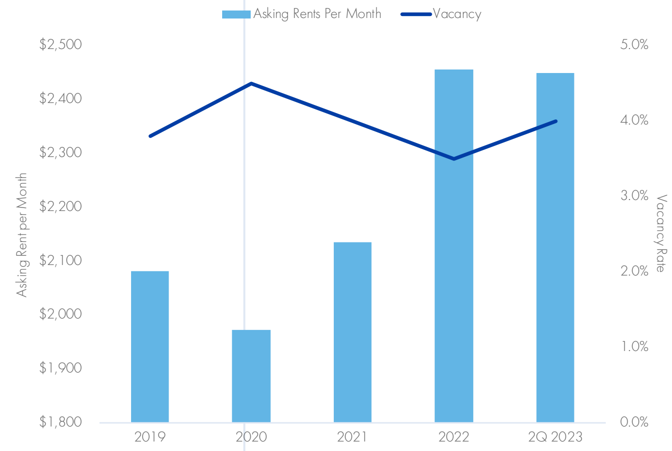
LOS ANGELES

CONSTRUCTION/VACANCY/RENTS

- Multifamily developers completed nearly 3,200 units during the second quarter bringing the year-to-date total to 4,935 units. Projects totaling more than 19,500 units are currently under construction throughout Los Angeles with the Downtown area accounting for approximately 45 percent of the development pipeline.
- Vacancy conditions softened slightly during the second quarter as the rate rose 20 basis points to 4 percent. Year over year, the rate increased by 40 basis points. While most submarkets are recording vacancy rates around 4 percent or lower, vacancy in Downtown rose 110 basis points in the past year to 6.6 percent.
- Asking rents in Los Angeles rose 2 percent during the second quarter, reaching $2,449 per month. Year over year, average rents in Los Angeles have advanced 4.1 percent.
- **FORECAST:** Projects totaling roughly 9,500 units are scheduled to come online in 2023, outpacing the average annual delivery totals in the previous two years by about 50 percent. With construction on the rise, local vacancy is forecast to finish 2023 at 4.3 percent, up 80 basis points for the full year. Apartment rents in Los Angeles are projected to reach $2,500 per month, an annual gain of around 2 percent.

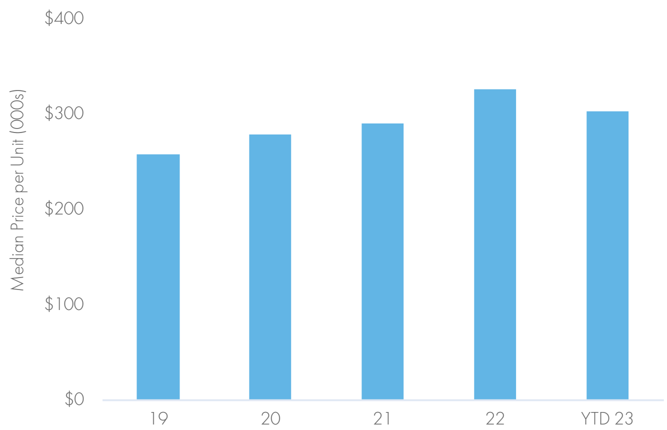
More than 19,500 units are currently under construction.

VACANCY & RENT TRENDS



Sources: Northmarq, Reis

SALES TRENDS



Cap rates averaged approximately 4.8 percent.

MULTIFAMILY SALES

- Sales velocity in Los Angeles recorded a steep decline from the first quarter to the second quarter, as investors weighed the impact of increasing concessions, rising insurance costs, and cooling demand on property performance. The number of transactions dropped 57 percent from the first quarter to the second quarter. Sales activity through the first half of 2023 is down nearly 50 percent from the same period last year.
- Some of the operational challenges facing the market have spilled over into pricing. The median sales price thus far in 2023 is $303,500 per unit, down 7 percent from the 2022 figure.
- During the second quarter, cap rates averaged approximately 4.8 percent across Greater Los Angeles, 50 basis points higher than at the beginning of the year. Generally, cap rates were lowest in West Los Angeles and in the South Bay, and a bit higher in Downtown and in the San Fernando Valley.

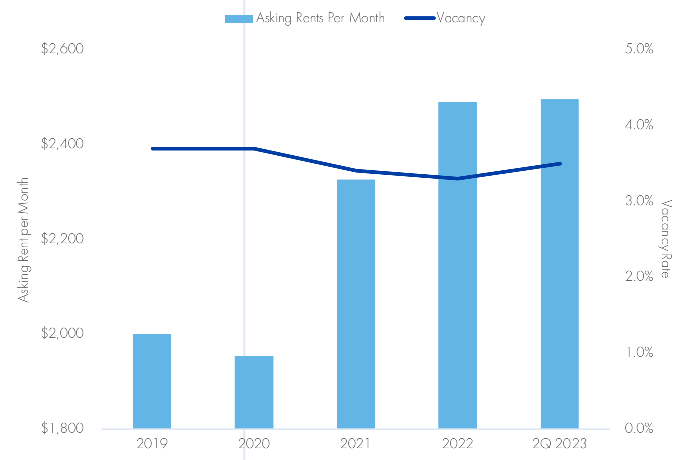
ORANGE COUNTY

CONSTRUCTION/VACANCY/RENTS

- Apartment developers in Orange County delivered 590 apartment units in the second quarter, bringing the first half total to nearly 1,200 units. Projects totaling approximately 5,500 units are currently under construction throughout the region, up 40 percent from one year ago.
- Vacancy ticked higher during the second quarter, rising 20 basis points to 3.5 percent. During the past 12 months, vacancy has risen 40 basis points. Vacancy in Orange County had reached a five-year low in 2022, but the rate has inched higher in subsequent quarters.
- After dipping slightly in the previous two quarters, local asking rents rose 1.1 percent in the second quarter to $2,495 per month. The region recorded steep rent increases in 2021 and during the first half of last year before rents began to plateau. Asking rents in Orange County have increased by just 1.2 percent year over year.
- **FORECAST:** Projects totaling nearly 3,000 units are slated to come online in 2023, the largest annual delivery total in Orange County since 2018. As new supply is on track to slightly outpace renter demand, the vacancy rate is expected to finish 2023 at around 3.6 percent, up 30 basis points for the year. Local asking rents are projected to rise 2.5 percent to $2,550 per month.

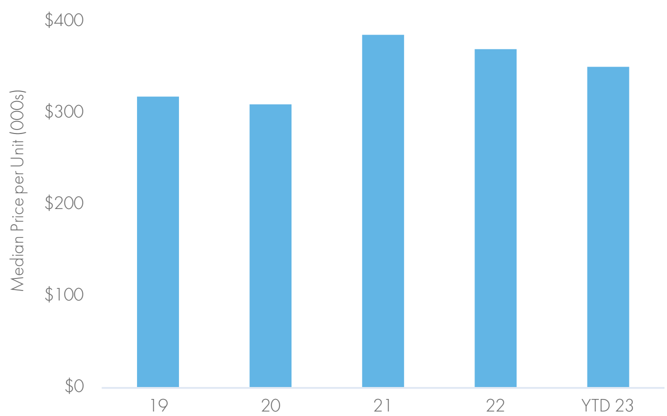
Approximately 5,500 units are under construction.

VACANCY & RENT TRENDS



Sources: Northmarq, Reis

SALES TRENDS



During the second quarter, the median price was $377,900 per unit.

MULTIFAMILY SALES

- Multifamily investment activity continued to slow in Orange County as deal volume fell 50 percent from the first quarter to the second quarter. This was a continuation of a more modest pace of transactions that began to take shape in the second half of 2022. The number of sales in the first half was down 60 percent from the same period last year.
- The median sales price year to date is $350,800 per unit, down 5 percent from the median price in 2022. Investors in Orange County have shown a preference for small and mid-sized properties in recent months. Nearly all the activity this year has been in properties with fewer than 100 units, while in past years, transaction sizes averaged about 200 units.
- Cap rates in Orange County have pushed higher in recent quarters but remain low compared to many other markets across the country. Most properties are selling with cap rates around 4.75 percent, after rising during the second quarter. With current cap rates considerably lower than prevailing lending rates, underwriting acquisitions is proving to be a challenge.

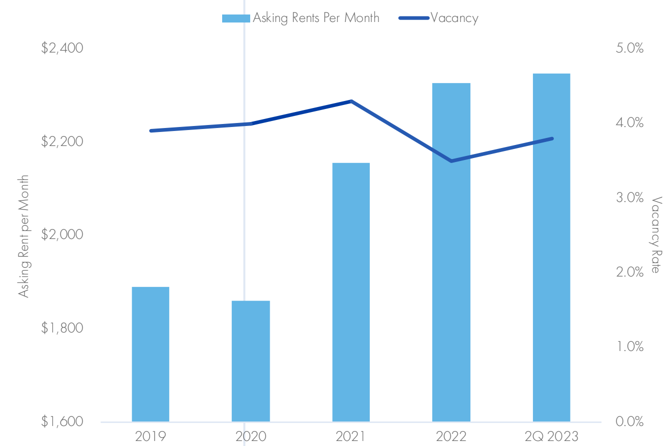
SAN DIEGO

CONSTRUCTION/VACANCY/RENTS

- Developers in San Diego completed roughly 685 apartment units in the first half of 2023, a slowdown from recent years. With projects totaling 5,580 units currently under construction throughout the region, the pace of deliveries will accelerate in the coming quarters.
- Vacancy in San Diego crept higher during the second quarter, rising 30 basis points to 3.8 percent. Despite the recent uptick, the rate is up just 10 basis points year over year.
- Average rents in San Diego inched higher by 0.6 percent during the second quarter to $2,348 per month, marking the ninth consecutive quarterly increase in the region. Recent advances have been slow, but steady; rents are up 3.2 percent in the past 12 months.
- **FORECAST:** Apartment projects totaling approximately 3,000 units are scheduled to come online in 2023, slightly lower than the total deliveries in 2022. Vacancy is expected to increase 50 basis points in 2023, reaching 4 percent, while asking rents are on pace to rise 2.5 percent to $2,385 per month.

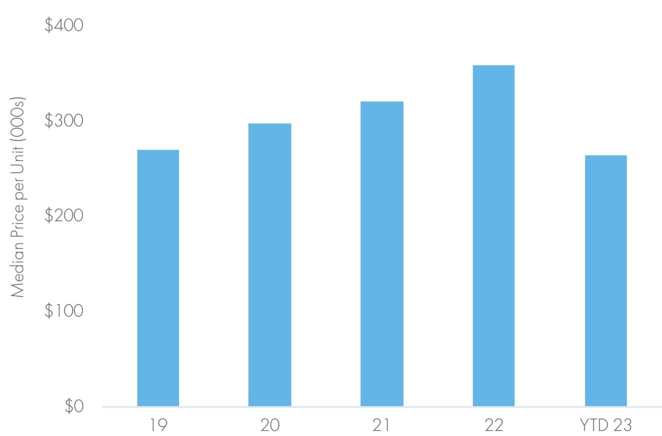
Rents are up 3.2 percent in the past 12 months.

VACANCY & RENT TRENDS



Sources: Northmarq, Reis

SALES TRENDS



The median sales price in 2023 is $264,900 per unit.

MULTIFAMILY SALES

- Multifamily investment activity continued to slow in recent months as the number of sales fell 30 percent during the second quarter. Deal volume year to date is down more than 50 percent compared to levels in the first half of 2022. Many of the transactions that closed during the second quarter were between 30 and 65 units.
- The median sales price thus far in 2023 is $264,900 per unit, down 26 percent from last year's figure. This followed an extended period where prices rose by an average of 10 percent per year.
- Cap rates continued to drift higher during the last three months, averaging between 4.5 percent to 5.5 percent. Recent cap rates are about 150 basis points higher than one year ago.

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