

A nighttime photograph of a cityscape in San Jose, California. The scene is illuminated by warm streetlights and building lights, creating a golden glow. In the foreground, there are several multi-story residential buildings, some with balconies and large windows. A prominent palm tree stands in the middle ground. In the background, a tall, modern building with a blue-lit top is visible against the dark sky. The overall atmosphere is urban and vibrant.

Yardi® Matrix

San Jose: Rents Down the Valley

Multifamily Report Summer 2017

Rents Continue to Decrease

High Prices, Lower Yields

Completions Soften

Market Analysis

Summer 2017

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Tech Scene Stays Hot, Rent Growth Cools

Silicon Valley is the nation's largest tech hub, a top-performing venture capital market and one of the most prominent locations for startups. The metro continues to thrive as an attractive destination for businesses and young, educated workers, as a result of consistent employment and wage growth. However, the rental market is cooling as San Jose becomes increasingly unaffordable, even for higher-paid workers. Rents dropped 1.3% year-over-year through May to \$2,675, more than double the national average.

Employment gains were led by professional and business services, which added 6,900 jobs. The construction sector also gained traction, as a result of the Bay Area Rapid Transit (BART) Silicon Valley Extension. The 10-mile, \$2.3 billion-dollar project is scheduled for completion in December and will create two additional metro stations: Milpitas and Berryessa. The project sparked investor interest, as Lyon Capital Ventures and Clayco Realty Group's two communities are already under construction in Milpitas, with more than 370 units each.

The total multifamily pipeline consists of roughly 39,000 units in different stages of development, with about 4,000 projected to come online by year-end. Because San Jose is among the most sought-after and competitive markets in the U.S., investor interest is expected to remain high. Rents, however, will stay flat, as Yardi Matrix forecasts only a 0.5% increase in 2017.

Recent San Jose Transactions

The Grove



City: San Jose, Calif.
Buyer: TIAA
Purchase Price: \$96 MM
Price per Unit: \$288,520

Sofi Berryessa



City: San Jose, Calif.
Buyer: Pacific Urban Residential
Purchase Price: \$56 MM
Price per Unit: \$330,357

The Vineyards



City: Gilroy, Calif.
Buyer: ABL Properties
Purchase Price: \$54 MM
Price per Unit: \$314,706

555



City: Milpitas, Calif.
Buyer: Interstate Equities Corp.
Purchase Price: \$46 MM
Price per Unit: \$335,766

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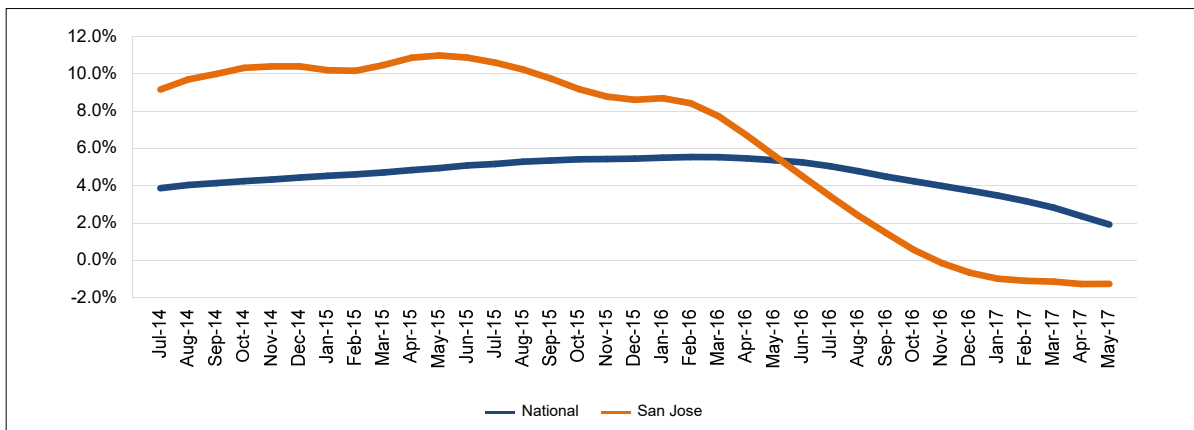
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Rent Trends

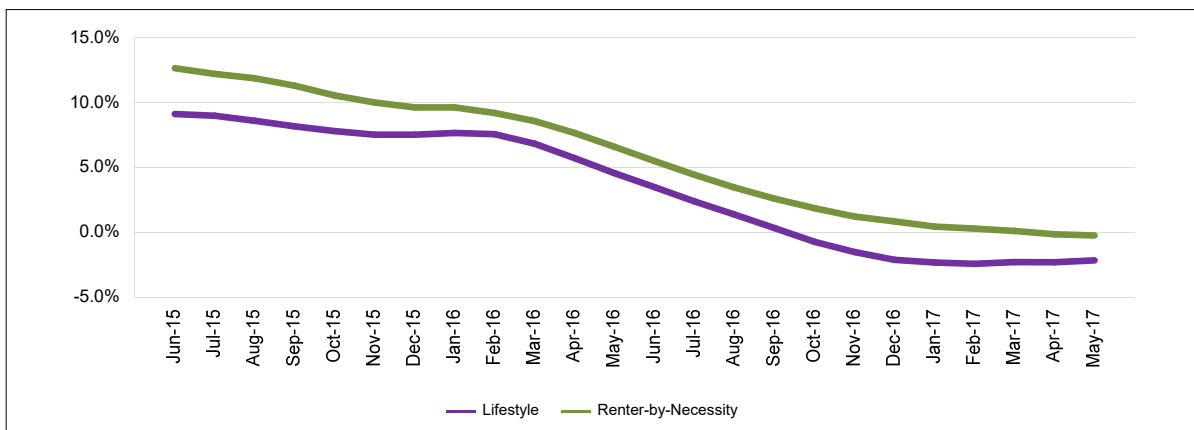
- Rent growth in San Jose has been decelerating since it reached double-digit levels in 2015. Growth fell to -1.3% in May 2017, well below the national growth rate of 1.5%. Affordability is proving to be a prime reason for the decline. The metro's \$2,675 average rent was more than double the national average of \$1,316.
- Gains in both asset classes have been decelerating, but the upscale Lifestyle segment (-2.2%) has been hit the hardest. The surge in supply in recent years is putting pressure on rent growth, particularly in the luxury segment, where most of the new deliveries have been concentrated. Rents in the working-class Renter-by-Necessity segment (-0.2%) are slightly down year-over-year.
- Out of the 20 San Jose submarkets, only four had rent increases: Gilroy (3.0%), East San Jose (1.5%), West San Jose (1.2%) and Milpitas (0.5%). The submarkets with the largest drop in rents were Central San Jose (-4.5%) and Central San Jose West (-3.0%).
- Although demand is expected to remain healthy, the affordability issue should keep rent growth to a minimum. Yardi Matrix forecasts rents to increase by 0.5% in 2017.

San Jose vs. National Rent Growth (Sequential 3 Month, Year-Over-Year)



Source: YardiMatrix

San Jose Rent Growth by Asset Class (Sequential 3 Month, Year-Over-Year)

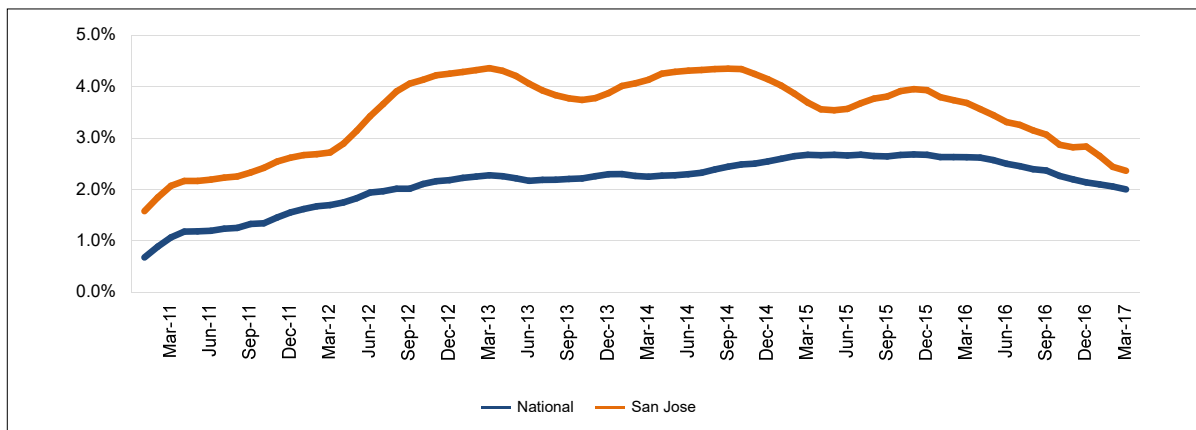


Source: YardiMatrix

Economic Snapshot

- San Jose added a total of 24,200 jobs year-over-year through March, a 2.3% increase and 30 basis points above the national average.
- Professional and business services drove employment gains with 6,900 jobs added in the 12 months ending in March 2017. Innovation and technology define Silicon Valley, and with the recently opened Apple Park, Nvidia's new headquarters and Google's upcoming canopy campus, San Jose will likely continue through 2017 with consistent job gains in this sector.
- The tech industry accounts for the bulk of the office space occupied in San Jose. This is the fifth year in a row that the office market has had positive net absorption, bringing total occupancy in Silicon Valley to more than 11 million square feet. The largest deal of the first quarter was Amazon's 214,000-square-foot lease of a newly constructed building in East Palo Alto for its A9 division. Asking rates continue on an upward trend, and are about \$4.30 per square foot.
- Health-care businesses had the highest percentage of new investment in the first months of 2017, collecting more than \$1.1 billion, more than 40% of all venture capital invested in the region. The sector added 4,200 jobs year-over-year.

San Jose vs. National Employment Growth (Year-Over-Year)



Sources: YardiMatrix, Bureau of Labor Statistics (not seasonally adjusted)

San Jose Employment Growth by Sector (Year-Over-Year)

Code	Employment Sector	Current Employment		Year Change	
		(000)	% Share	Employment	%
60	Professional and Business Services	228	21.1%	6,900	3.1%
70	Leisure and Hospitality	103	9.5%	6,300	6.5%
65	Education and Health Services	166	15.4%	4,200	2.6%
50	Information	76	7.0%	3,400	4.7%
15	Mining, Logging and Construction	48	4.4%	2,500	5.4%
80	Other Services	28	2.6%	900	3.3%
30	Manufacturing	164	15.2%	800	0.5%
90	Government	96	8.9%	400	0.4%
55	Financial Activities	35	3.2%	-100	-0.3%
40	Trade, Transportation and Utilities	137	12.7%	-1,100	-0.8%

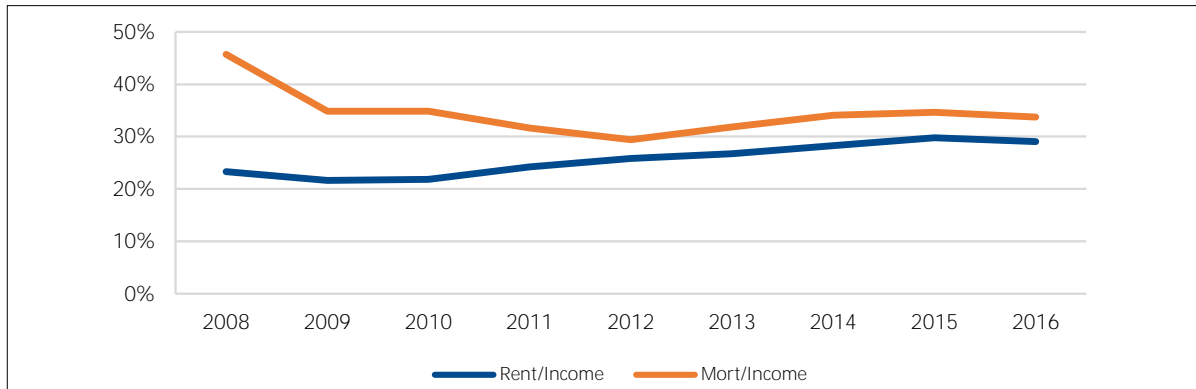
Sources: YardiMatrix, Bureau of Labor Statistics

Demographics

Affordability

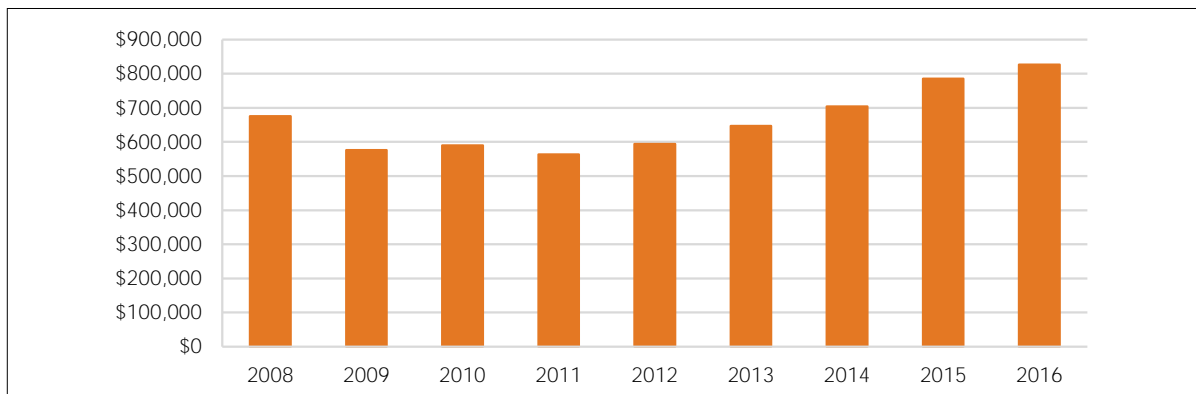
- San Jose's median home price is among the highest in the nation, surpassing \$826,700 in 2016. Renting is still more affordable than owning, with the average rent accounting for 29% of the area's median income, while the average mortgage payment comprises 34%.
- The lack of low-cost housing is a growing problem in San Jose. SV@Home—a nonprofit organization that works with other organizations, companies, developers and banks—recently collaborated with the Santa Clara Valley Transit Authority to approve a policy where 20% of all housing built on the authority's territory would be affordable. Facebook also pitched in, providing \$20 million to help fund the affordable housing cause.

San Jose Rent vs. Own Affordability as a Percentage of Income



Sources: YardiMatrix, Moody's Analytics

San Jose Median Home Price



Source: Moody's Analytics

Population

- The San Jose-Sunny Vale-Santa Clara MSA's population rose by 0.5% in 2016, 20 basis points below the national average.
- The metro added 10,238 residents in the past year and 83,029 since 2012.

San Jose vs. National Population

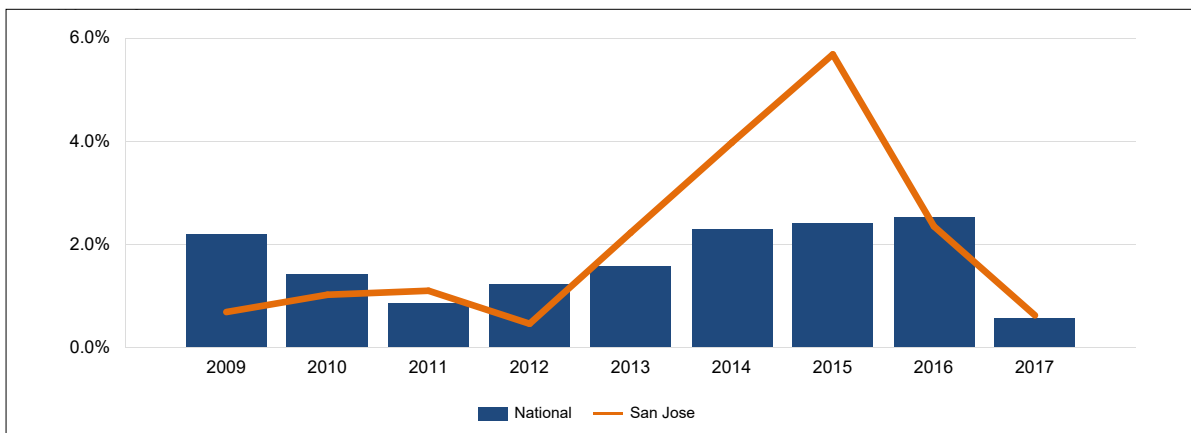
	2012	2013	2014	2015	2016
National	313,998,379	316,204,908	318,563,456	320,896,618	323,127,513
San Jose Metro	1,895,787	1,924,432	1,947,922	1,968,578	1,978,816

Sources: U.S. Census, Moody's Analytics

Supply

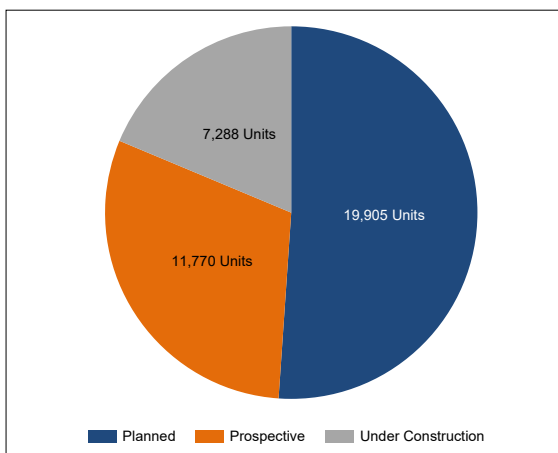
- Multifamily development in San Jose is tepid. By the end of 2017's second quarter, only 400 units came online. In 2016, about 2,800 units were completed, a significant drop compared to 2015's numbers. Last year's completions represented a 2.4% increase in stock, 10 basis points below the national average.
- Completions are expected to pick up, as more than half of the total 7,000 units under construction are scheduled for delivery by year-end. Of the 39,000 units that were in the development pipeline as of May, about 20,000 were in the planning phase and 12,000 were prospective projects.
- The tight supply and high demand are making San Jose increasingly unaffordable for residents, particularly in well-located neighborhoods near corporate campuses. As of April, occupancy for stabilized properties was 95.4%.
- Submarkets with the most construction activity were Central San Jose West (1,138 units) and Santa Clara (1,011). Irvine Co.'s 825-unit Monticello in the Santa Clara submarket ranks as the largest project scheduled to come online in 2017. As of January, the property was already 44% pre-leased.

San Jose vs. National Completions as a Percentage of Total Stock (as of May 2017)



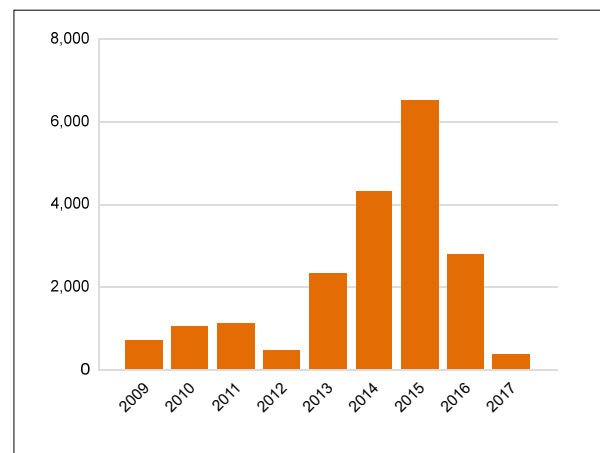
Source: YardiMatrix

Development Pipeline (as of May 2017)



Source: YardiMatrix

San Jose Completions (as of May 2017)

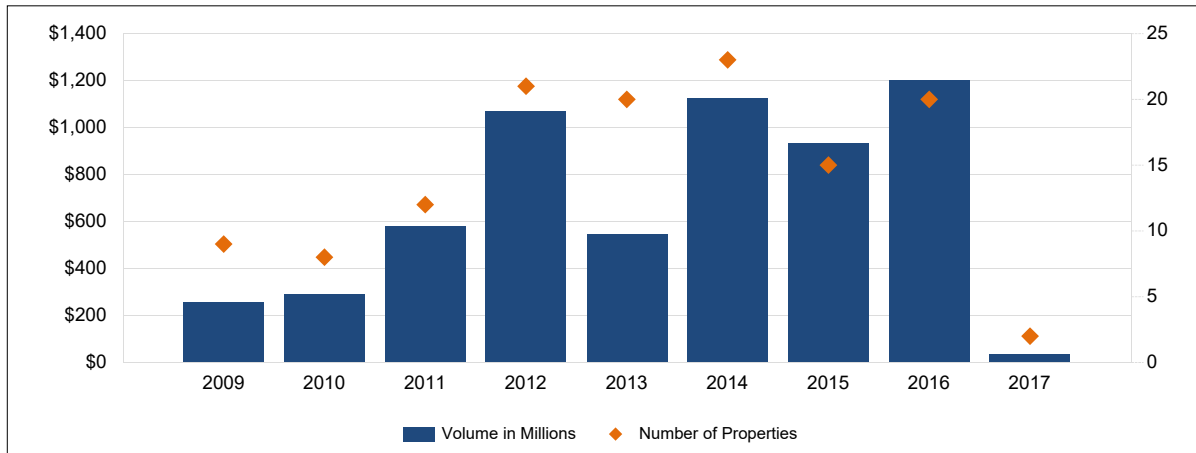


Source: YardiMatrix

Transactions

- Roughly \$38 million worth of multifamily assets changed hands through the end of the second quarter. The tech industry continues to make Silicon Valley a prime region for multifamily investments, and San Jose is benefiting from the capital inflow from both domestic and international investors.
- Acquisition yields are in the low 4.0% range for stabilized Class A properties and hover between 3.7% and 4.7% for Class B and C assets. As of May 2017, the average price per unit was \$186,567, well above the national average of \$130,839.
- The most sought-after submarkets were Santa Clara (\$295 million traded), Central San Jose West (\$153 million) and Far South San Jose (\$150 million). TIAA's \$96 million purchase of The Grove was the largest deal over the past 12 months. Kennedy Wilson sold the asset for 48% above the 2007 purchase price.

San Jose Sales Volume and Number of Properties Sold (as of May 2017)



Source: YardiMatrix

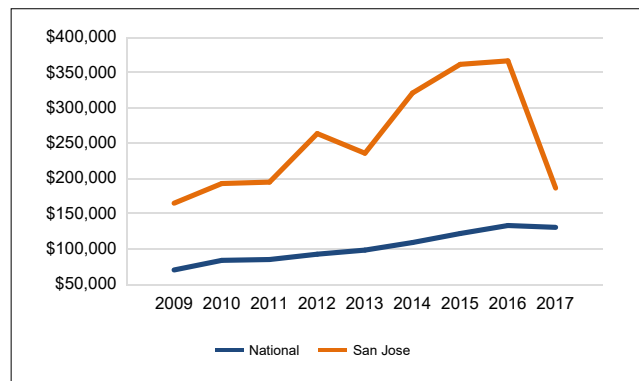
Top Submarkets for Transaction Volume¹

Submarket	Volume (\$MM)
Santa Clara	295
Central San Jose West	153
Far South San Jose	150
East San Jose	56
Gilroy	54
Milpitas	46
Campbell	45
Central San Jose	38

Source: YardiMatrix

¹ From June 2016 to May 2017

San Jose vs. National Sales Price per Unit



Source: YardiMatrix

Read All About It!



Downtown San Jose Revival:
From Historic YMCA
Building to Hotel



Will San Jose's New Rules
Hobble Its Market?



San Jose Office Building
Trades for \$82M

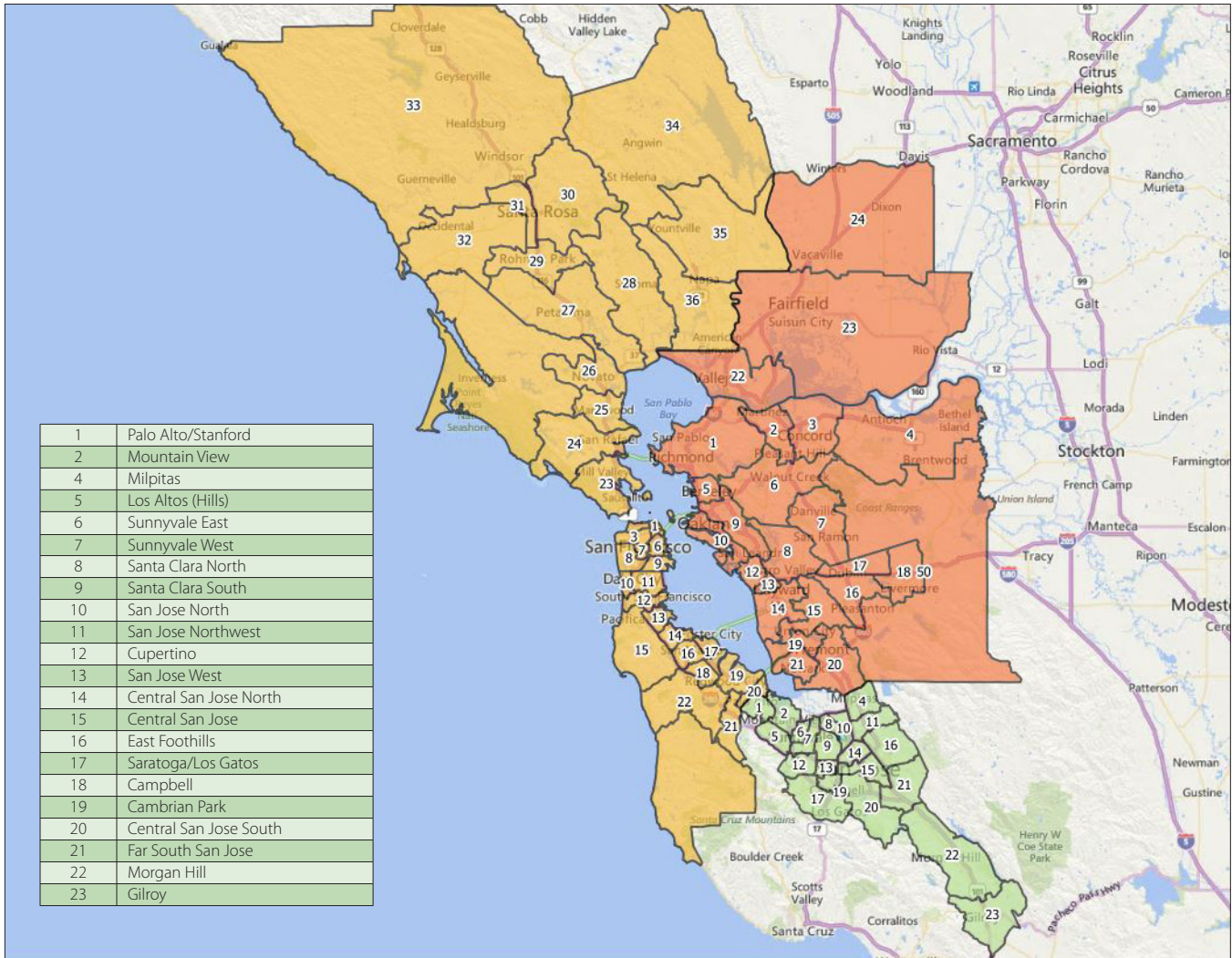


Mammoth 1 MSF San Jose
Office Project in Talks

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Area #	Submarket
1	Northeast San Francisco
2	Northwest San Francisco
3	Golden Gate Park
4	Market Street
5	China Basin
6	Eastern San Francisco
7	Central San Francisco
8	Southwest San Francisco
9	Southeast San Francisco
10	Broadmoor/Daly City
11	Colma/Brisbane
12	South San Francisco
13	Millbrae
14	Burlingame
15	Moss Beach
16	San Mateo
17	Foster City
18	Belmont/San Carlos

Area #	Submarket
19	Redwood City
20	East Palo Alto
21	Atherton/Portola
22	Woodside
23	Tiburon/Sausalito
24	San Rafael
25	Lucas Valley
26	Novato
27	Petaluma
28	Sonoma
29	Rohnert Park
30	Santa Rosa
31	Roseland
32	Sebastapol
33	Northern Marin County
34	Deer Park/St. Helena
35	Napa North
36	Napa South

Area #	Submarket
1	NW Contra Costa (Richmond)
2	Pleasant Hill/Martinez
3	Concord
4	Antioch/Oakley
5	Berkeley
6	Walnut Creek/LaFayette
7	San Ramon/Danville
8	Castro Valley
9	Oakland East
10	Oakland West
11	Alameda
12	San Leandro

Area #	Submarket
13	San Lorenzo
14	Hayward
15	Union City
16	Pleasanton
17	Dublin
18	Livermore
19	Fremont East
20	Fremont West
21	Newark
22	Vallejo/Benicia
23	Fairfield
24	Vacaville
50	East Bay

Definitions

Lifestyle households (renters by choice) have wealth sufficient to own but have chosen to rent. Discretionary households, most typically a retired couple or single professional, have chosen the flexibility associated with renting over the obligations of ownership.

Renter-by-Necessity households span a range. In descending order, household types can be:

- *A young-professional, double-income-no-kids household* with substantial income but without wealth needed to acquire a home or condominium;
- *Students*, who also may span a range of income capability, extending from affluent to barely getting by;
- *Lower-middle-income (“gray-collar”) households*, composed of office workers, policemen, firemen, technical workers, teachers, etc.;
- *Blue-collar households*, which may barely meet rent demands each month and likely pay a disproportionate share of their income toward rent;
- *Subsidized households*, which pay a percentage of household income in rent, with the balance of rent paid through a governmental agency subsidy. Subsidized households, while typically low income, may extend to middle-income households in some high-cost markets, such as New York City;
- *Military households*, subject to frequency of relocation.

These differences can weigh heavily in determining a property’s ability to attract specific renter market segments. The five-star resort serves a very different market than the down-and-outer motel. Apartments are distinguished similarly, but distinctions are often not clearly definitive without investigation. The Yardi® Matrix Context rating eliminates that requirement, designating property market positions as:

Market Position	Improvements Ratings
Discretionary	A+ / A
High Mid-Range	A- / B+
Low Mid-Range	B / B-
Workforce	C+ / C / C- / D

The value in application of the Yardi® Matrix Context rating is that standardized data provides consistency; information is more meaningful because there is less uncertainty. The user can move faster and more efficiently, with more accurate end results.

The Yardi® Matrix Context rating is not intended as a final word concerning a property’s status—either improvements or location. Rather, the result provides reasonable consistency for comparing one property with another through reference to a consistently applied standard.

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