Yardi® Matrix

San Diego's Momentum

Multifamily Fall Report 2017

Legislators Back Affordability

Development Pipeline Expands

Rent Growth Remains Above-Trend

Market Analysis
Fall 2017

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SoCal Delivering for Investors

San Diego's multifamily market continues to attract robust investor demand, with transaction activity hot off 2016's cycle high and already at $1 billion year-to-date through July. The market boasts the fourth-highest occupancy rate among major U.S. metros. As a result, rents were up 4% year-over-year as of August, well above the national rate.

The metro benefits from a strong talent pool, renowned universities and its ever-growing biotechnology sector. Plans for several large-scale projects are being fast-tracked in order to satisfy a growing demand. SoccerCity and San Diego State University have their eyes on the Qualcomm site, while the $1.2 billion Seaport Village redevelopment is aiming at a 2020 groundbreaking. The $1.3 billion Manchester Pacific Gateway mixed-use project in the downtown area will serve as the U.S. Navy's new regional headquarters.

Inventory is expected to expand significantly in the coming years, given the city's robust multifamily pipeline and recent pro-development legislation. Roughly 9,000 units were underway as of August, and recent bills passed by state legislators are poised to spur additional development in San Diego. Bills passed in mid-September aim to secure funding for affordable housing and streamline the approval process, which should eventually boost supply. As deliveries have yet to catch up with demand, Yardi Matrix expects rent growth to end the year at 4.5%.

Recent San Diego Transactions

Carmel Pacific Ridge

City: San Diego
Buyer: American Assets
Purchase Price: $229 MM
Price per Unit: $429,747

BLVD63

City: San Diego
Buyer: TIAA
Purchase Price: $156 MM
Price per Unit: $469,880

Preserve at Melrose

City: Vista, Calif.
Buyer: MG Properties Group
Purchase Price: $134 MM
Price per Unit: $326,829

Dylan Point Loma

City: San Diego
Buyer: LaSalle Investment Management
Purchase Price: $90 MM
Price per Unit: $500,000

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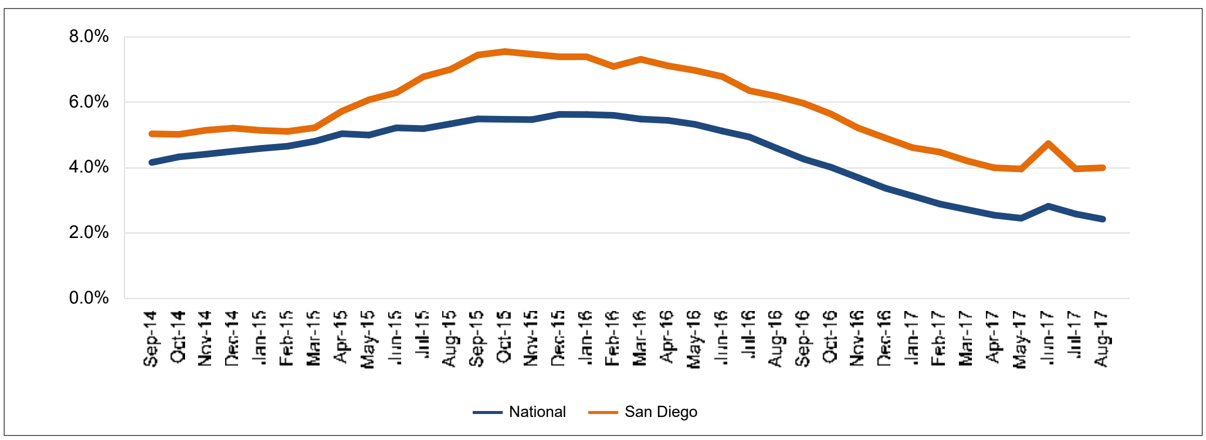
On the cover: Photo by Sean Pavone/iStockphoto.com

Rent Trends

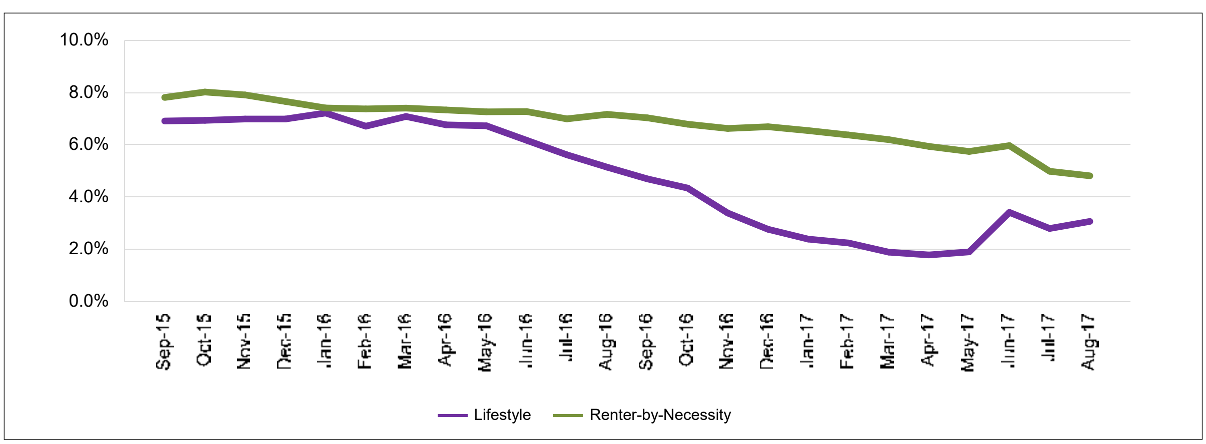
- Rents in San Diego rose 4% year-over-year through August, 160 basis points higher than the national rate. The average rent was $1,820, $468 above the national average. The average occupancy rate in stabilized properties was at 96.8%, one of the highest rates among major metros and a primary cause of continued rent growth.
- Rents in the Renter-by-Necessity segment grew by 4.8% year-over-year to $1,567, 170 basis points over those in the Lifestyle segment. This reflects the shortage of working-class housing, deepened by the fact that 94% of all units currently under construction cater to the higher-end segment, where rents average $2,253.
- Rents grew at the fastest rates in Spring Valley (7.1%), El Cajon (6.8%), Fallbrook (6.5%) and Mid-City (6.4%), submarkets with few units in development. Meanwhile, rents are kept in check in Central San Diego, where year-over-year growth topped out at 1.5%, as this area has the greatest activity levels. Although rents in Del Mar contracted this year, the submarket still has the highest average rent at $2,609, followed by Coronado, University and Carlsbad, all with average rents above the $2,000 mark.
- Although supply is beginning to pick up after years of under-development, we expect a strong demand to support rent growth at an above-trend 4.5% for the year.

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



Source: YardiMatrix

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

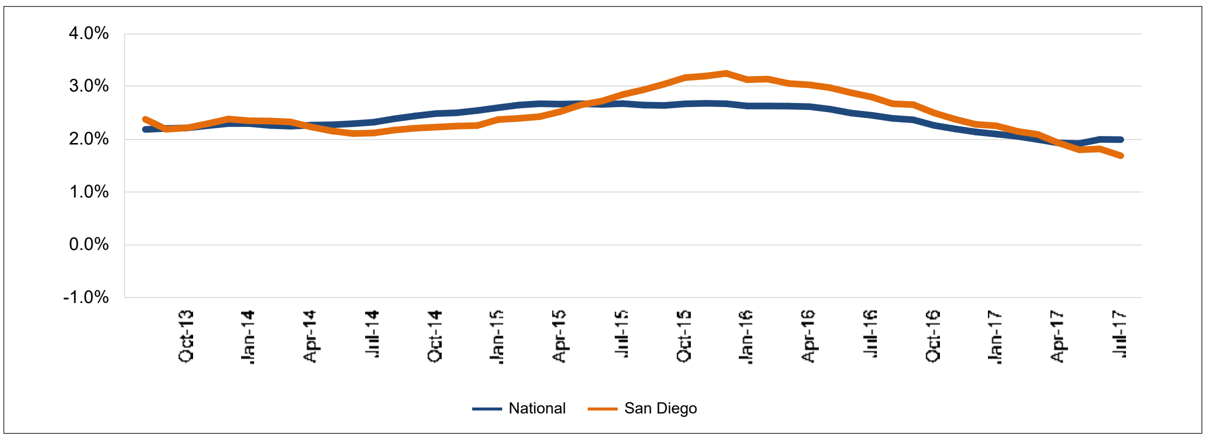


Source: YardiMatrix

Economic Snapshot

- San Diego added 20,400 jobs in the 12 months ending in July, up 1.7% year-over-year. That's 30 basis points below the national rate. The metro benefits from a strong, well-educated talent pool that feeds into the market's prominent biotech sector, but some cuts in education and the contraction of sectors such as manufacturing, professional and business services and trade, transportation and utilities have limited job gains.
- Leading the way was the public sector, which added 9,100 jobs and accounts for 16.7% of current employment. Education and health services added 5,000 positions, despite the nearly 2,000 jobs that were cut from teaching and support staff announced by the San Diego Unified School District Board of Education earlier this year. In 2018, UC San Diego will break ground on a $608 million mixed-use project, which will provide housing for 2,000 students by 2020.
- Office space in San Diego's primary urban areas remains in high demand, with vacancy rates now below the 5% mark. The $1.3 billion Manchester Pacific Gateway mixed-use project in downtown San Diego occupies a 12-acre site and will serve as the new regional headquarters for the U.S. Navy. The development is slated for completion in 2020. Other large projects include Protea Waterfront's $1.2 billion redevelopment of Seaport Village, set to break ground in 2020.

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



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

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

		Current Employment		Year Change	
Code	Employment Sector	(000)	% Share	Employment	%
90	Government	240	16.7%	9,100	3.9%
65	Education and Health Services	201	13.9%	5,000	2.5%
80	Other Services	60	4.2%	4,900	8.8%
15	Mining, Logging and Construction	80	5.6%	2,400	3.1%
55	Financial Activities	76	5.3%	1,900	2.6%
70	Leisure and Hospitality	200	13.9%	1,800	0.9%
50	Information	24	1.7%	-100	-0.4%
30	Manufacturing	108	7.5%	-1,100	-1.0%
60	Professional and Business Services	234	16.2%	-1,600	-0.7%
40	Trade, Transportation and Utilities	219	15.2%	-1,900	-0.9%

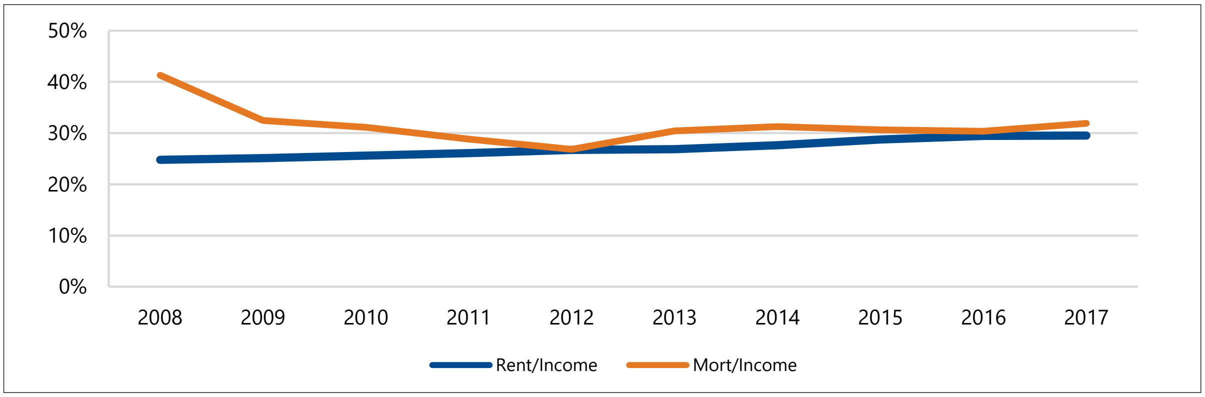
Sources: YardiMatrix, Bureau of Labor Statistics

Demographics

Affordability

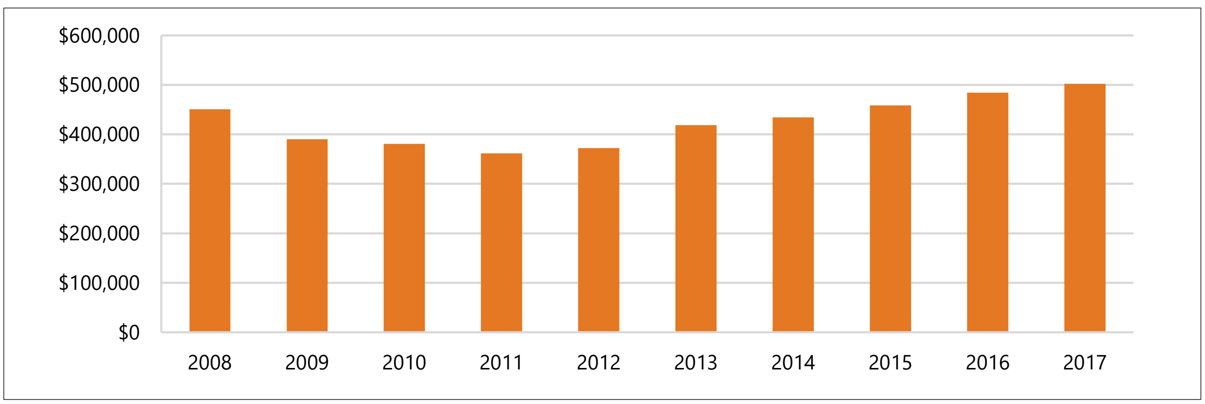
- San Diego is one of the most expensive U.S. metros. The median home value hit $502,191 in mid-2017, a cycle high, up 38.9% from 2011. Rents accounted for 30% of the median income, while mortgages equated to 32%.
- Recent legislation addresses California's affordability crisis, pointed out in a recent Census report, which revealed that about one in five state residents lives under the poverty line, mainly due to housing costs. Senate Bill 2 will impose a $75 fee on certain real estate transactions and is expected to raise $250 million per year for affordable housing, while SB 3 will put a $4 billion bond before voters in 2018 for affordable and veteran housing. SB 35 aims to fast-track construction approvals and boost supply.

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



Sources: YardiMatrix, Moody's Analytics

San Diego Median Home Price



Source: Moody's Analytics

Population

- San Diego added 27,504 residents in 2016, a growth rate of 0.8%, slightly above the national rate of 0.7%.
- From 2012 to 2016, the metro expanded by 4.3%, 140 basis points above the national rate.

San Diego vs. National Population

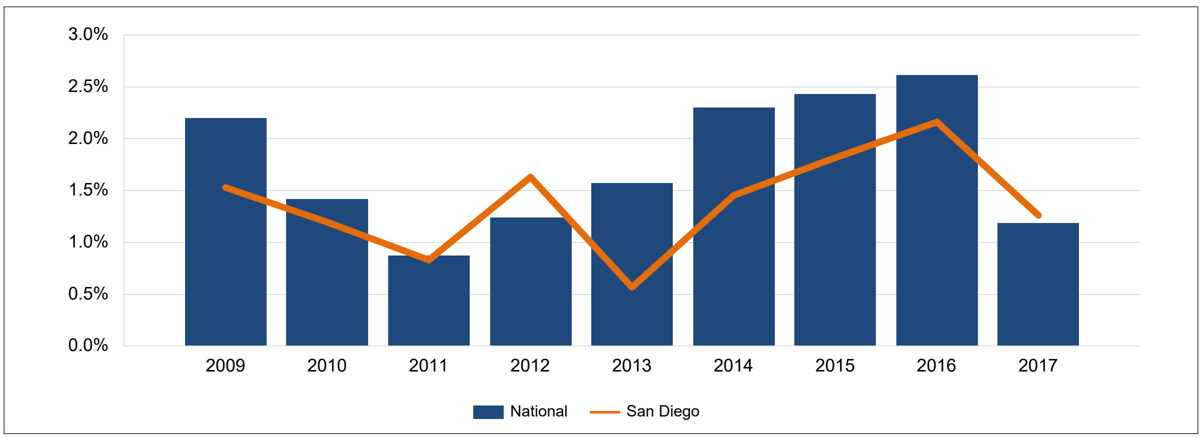
	2012	2013	2014	2015	2016
National	313,998,379	316,204,908	318,563,456	320,896,618	323,127,513
San Diego Metro	3,181,513	3,218,419	3,258,856	3,290,245	3,317,749

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

Supply

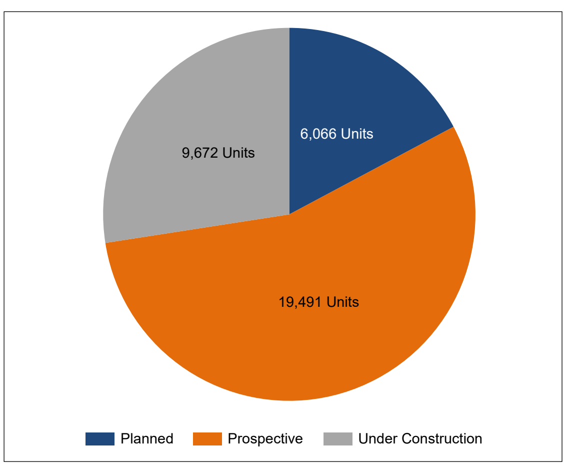
- Developers added 2,246 units year-to-date through August, with nearly 4,500 more expected to come online this year. Multifamily construction has been ramping up throughout the second half of the economic cyle, and legislation aims to streamline approvals. Senate Bill 35, introduced last year and passed in mid-September, will spur construction of affordable housing going forward.
- Roughly 10,000 units were underway in San Diego as of August, with more than 25,500 units in various stages of development. Central San Diego accounts for more than a third of the number of units under construction, followed by the University submarket, where the University of California–San Diego is adding 1,080 student residences later this year and another 2,000 by 2020.
- Construction activity is highest in the Mission Valley submarket, where many redevelopment projects are on the drawing board, seeking approval. Hines is planning a revamp of the Riverwalk Golf Club that would add 4,000 units upon completion. The SoccerCity development proposal at the Qualcomm Stadium would add another 4,800 units to the area, if approved.

San Diego vs. National Completions as a Percentage of Total Stock (as of August 2017)



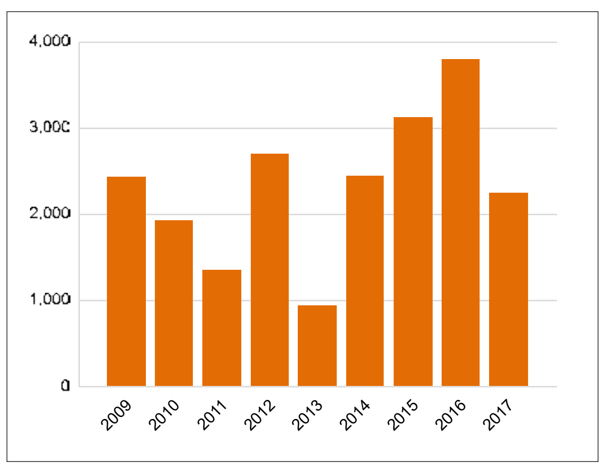
Source: YardiMatrix

Development Pipeline (as of August 2017)



Source: YardiMatrix

San Diego Completions (as of August 2017)

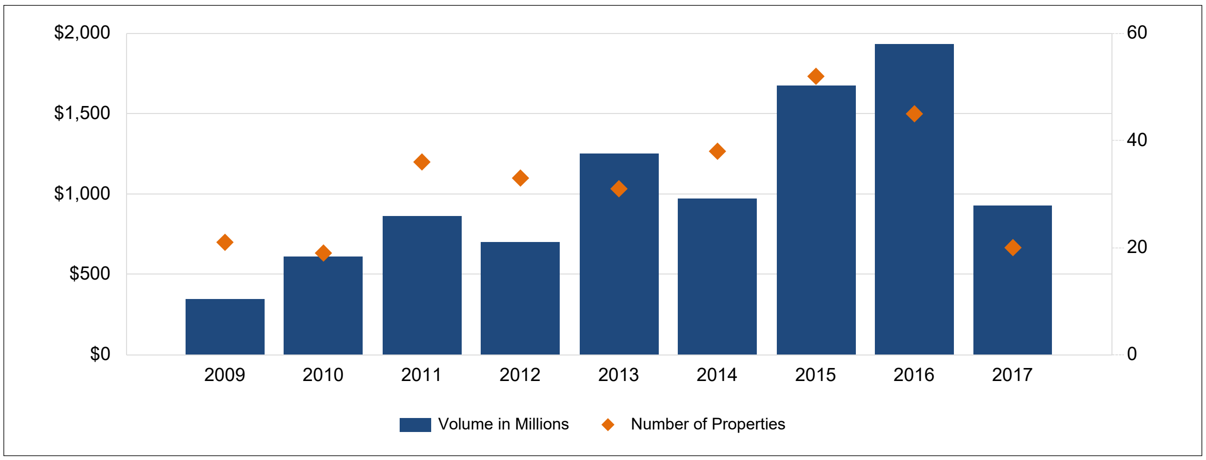


Source: YardiMatrix

Investment Transactions

- Nearly $1.7 billion in multifamily properties traded in the 12 months ending in July. Acquisition yields for Class A infill stabilized properties were in the 4% range, with some even lower, roughly on par with core investment markets in California, such as San Francisco, San Jose and Los Angeles.
- A robust development pipeline is keeping prices in check. The average per-unit price was $260,653 in 2017 through July, a 1.5% decrease from the previous year, but nearly double the national average of $133,537. Deals for assets in the Lifestyle segment accounted for nearly one-third of overall investment activity.
- Kearny Mesa, Oceanside and Mid-City accounted for nearly half the transaction volume, led by American Assets' $229 million purchase of Carmel Pacific Ridge, a 533-unit Lifestyle community with 30 affordable units. Seller Carmel Partners netted a per-unit price of $429,746 for the asset.

San Diego Sales Volume and Number of Properties Sold (as of July 2017)



Source: YardiMatrix

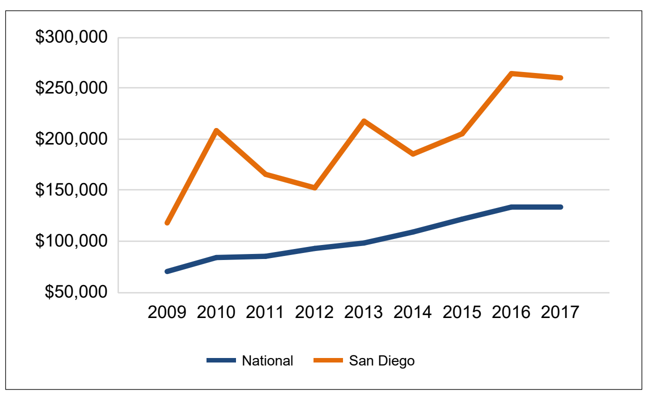
Top Submarkets for Transaction Volume[1]

Submarket	Volume ($MM)
Kearny Mesa	294
Oceanside	244
Mid-City	239
Mira-Mesa	151
Escondido	150
Peninsula	118
Santee	69
El Cajon	56

Source: YardiMatrix

[1] From August 2016 to July 2017

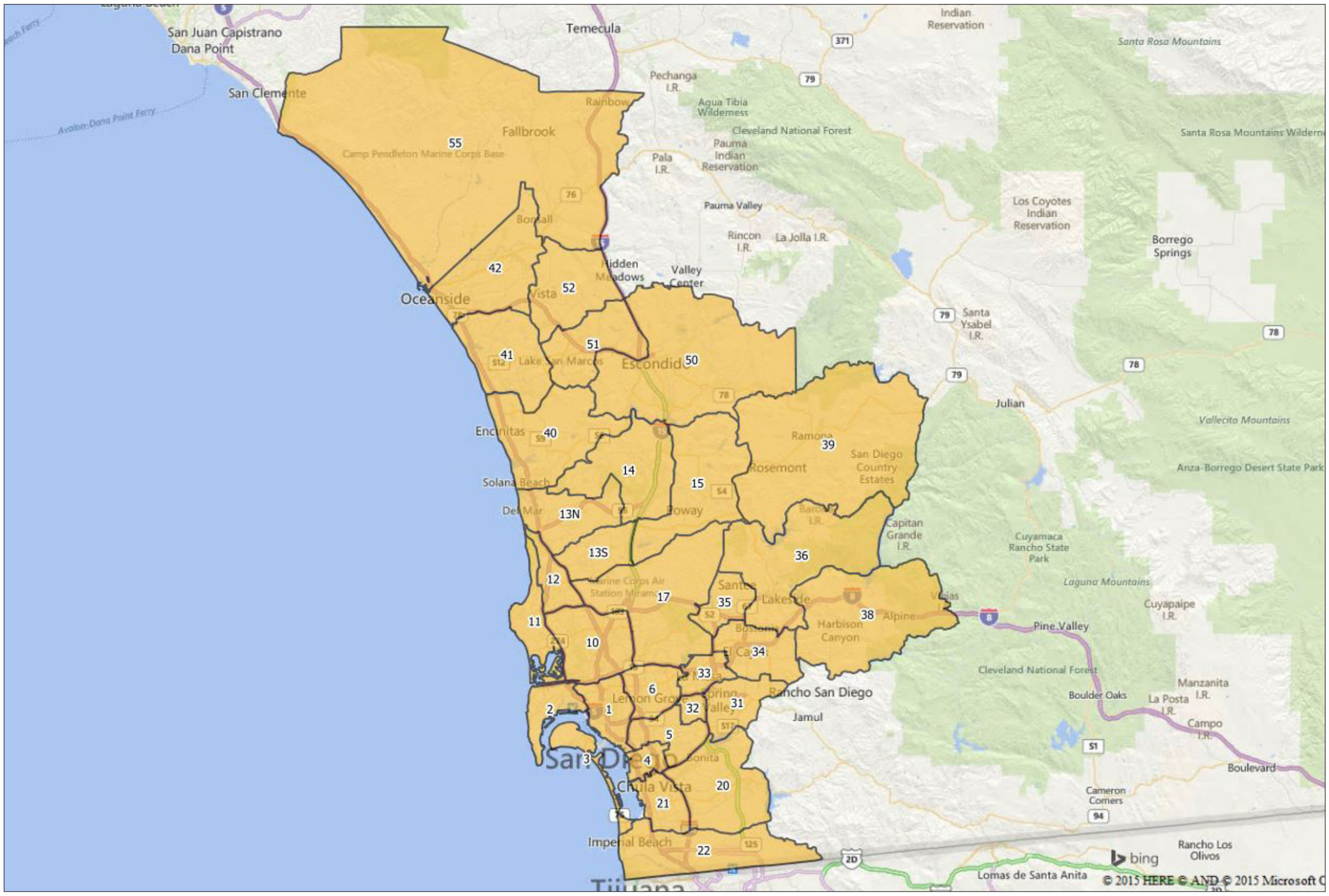
San Diego vs. National Sales Price per Unit



Source: YardiMatrix

Photo by photoquest7/iStockphoto.com

San Diego Submarkets



Area #	Submarket
1	Central San Diego
2	Peninsula
3	Coronado
4	National City
5	Southeast San Diego
6	Mid-City
10	Kearny Mesa
11	Coastal
12	University
13N	Del Mar
13S	Mira Mesa
14	North San Diego
15	Poway
17	Elliot-Navajo
20	Sweetwater
21	Chula Vista

Area #	Submarket
22	South Bay
31	Spring Valley
32	Lemon Grove
33	La Mesa
34	El Cajon
35	Santee
36	Lakeside
38	Alpine
39	Ramona
40	San Dieguito
41	Carlsbad
42	Oceanside
50	Escondido
51	San Marcos
52	Vista
55	Fallbrook

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.

To learn more about Yardi® Matrix and subscribing, please visit www.yardimatrix.com or call Ron Brock, Jr., at 480-663-1149 x2404.