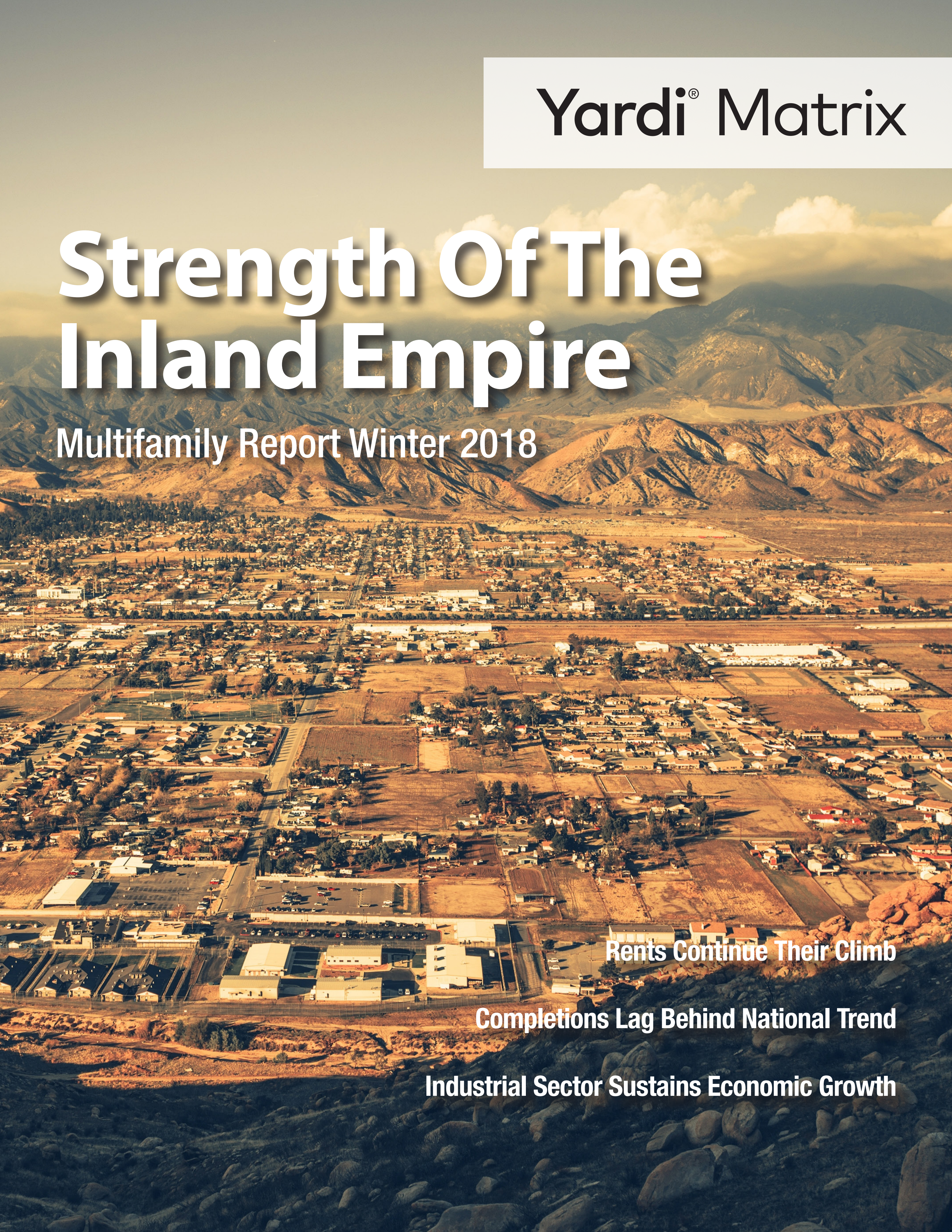
Yardi® Matrix

# Strength Of The Inland Empire

## Multifamily Report Winter 2018



Rents Continue Their Climb

Completions Lag Behind National Trend

Industrial Sector Sustains Economic Growth

## Market Analysis

Winter 2018

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# The Market Shows Its Sprawl

Riverside and San Bernardino counties are in the midst of a housing boom. Rents continue to grow at a solid rate throughout the Inland Empire, a direct result of steady job gains, at a time when the area's economic cornerstone—its industrial sector—is surging in all major metrics. Meanwhile, multifamily transactions have slightly tempered, due to an ongoing single-family housing wave, which has inflated construction activity and property values to new highs. Area rents grew the fastest in the Renter-by-Necessity segment, as the bulk of demand is in low- to middle-income housing.

Cargo volumes have grown in the nearby ports of Los Angeles and Long Beach, leading to further expansion in the trade, transportation and utilities sector. Employment growth has been diverse, as all but two sectors improved year-over-year through September. Continued economic development will soon present the area with a need to refurbish its transportation grid, as increased freighting will require improvement in infrastructure across the two counties. Riverside is looking to cash in on the effect of California Senate Bill 1, which should result in roughly $430 million in aid for the county as it looks to improve its aging infrastructure.

Multifamily development in the Inland Empire is tepid, in line with the broader, post-recession trend, with 3,200 units underway as of November. Another 12,000 are in the pipeline, as inflating home prices slowly push up demand for rentals.

### Recent Inland Empire Transactions

Avana Rancho Cucamonga

City: Rancho Cucamonga, Calif.
Buyer: Greystar
Purchase Price: $122 MM
Price per Unit: $1,124,011

Victoria Arbors

City: Rancho Cucamonga, Calif.
Buyer: Sares-Regis Group
Purchase Price: $94 MM
Price per Unit: $612,647

The Highlands at Grand Terrace

City: Grand Terrace, Calif.
Buyer: TruAmerica Multifamily
Purchase Price: $92 MM
Price per Unit: $490,698

Angelica

City: Rancho Cucamonga, Calif.
Buyer: Mesirow Financial
Purchase Price: $84 MM
Price per Unit: $328,859

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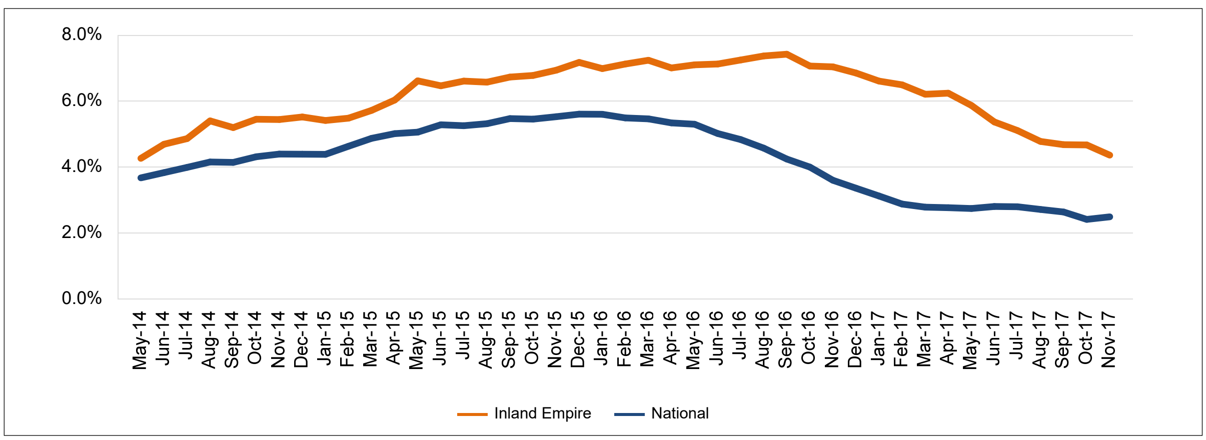
## Rent Trends

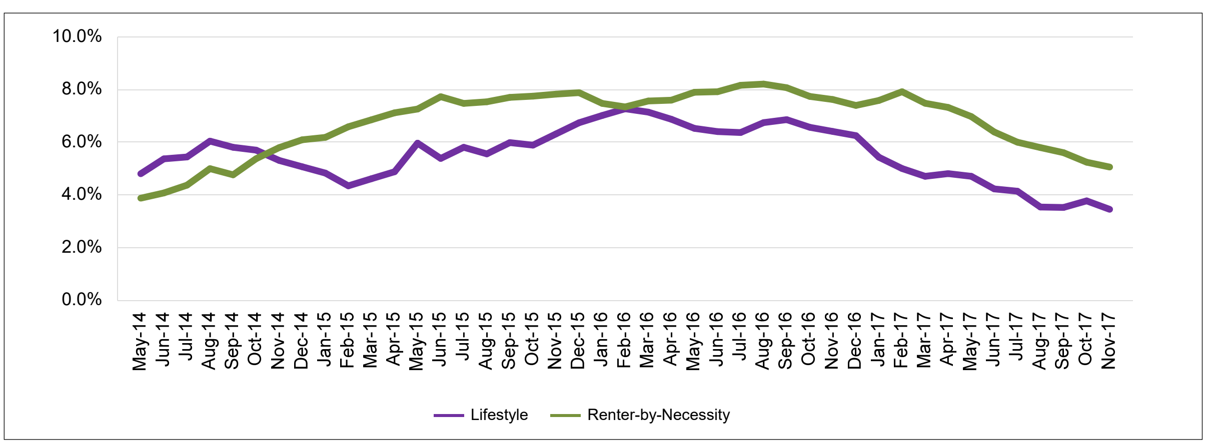
- Rents in the Inland Empire were up 4.4% year-over-year as of November 2017, 190 basis points above the national rate. The overall average rent stood at $1,412, matching the historic high reached in October and more than $50 above the U.S. average. San Bernardino and Riverside counties have enjoyed a solid spell of rent growth for the past few years, as strong employment gains and a limited rate of delivery have pushed up demand in the area.
- Working-class Renter-by-Necessity assets appreciated at the highest rate, capping off 5.1% year-over-year growth, at $1,247 in November. Occupancy in stabilized properties in the RBN segment was 96.5% in October, a 40 basis-point slide year-over-year. Rents in the Lifestyle segment rose 3.4%, to $1,650. Accelerated demand in single-family housing and favorable prices compared to Orange County and Los Angeles continued to push the local market, affecting multifamily development and occupancy.
- Rents grew at the fastest rates in Beaumont/Banning (9.2%), White Water/Desert Hot Springs (7.8%), Highlands (7.4%), West Riverside (7.0%) and Hemet/San Jacinto (7.0%). The five submarkets are made up of 86% Renter-by-Necessity units, where the bulk of growth is occurring.

**Inland Empire vs. National Rent Growth** (Sequential 3 Month, Year-Over-Year)




Source: YardiMatrix

**Inland Empire Rent Growth by Asset Class** (Sequential 3 Month, Year-Over-Year)




Source: YardiMatrix

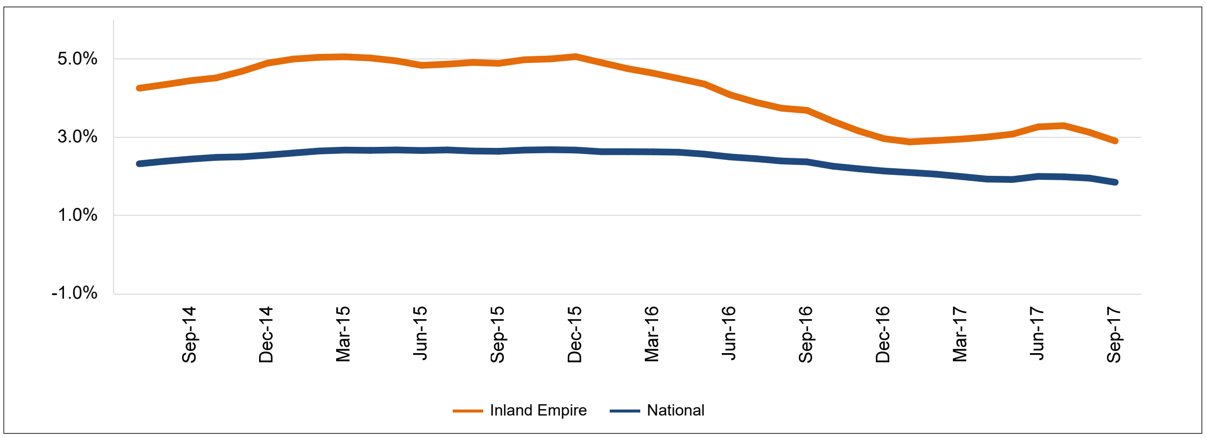
## Economic Snapshot

- In the 12 months ending in September, the Inland Empire added 35,000 jobs, up 2.9% year-over-year. The rate of employment growth is 100 basis points higher than the national average. San Bernardino and Riverside counties continue to heavily rely on their strong presence in the warehousing and distribution industries, with trade, transportation and utilities adding 3,100 jobs. Earlier this year, the ports of Los Angeles and Long Beach saw near-record levels of traffic. With more than a third of all U.S. imports coming through the two waypoints, improvement there brings positive influence to the Inland Empire.

- Multifamily demand and a continuously expanding industrial development pipeline have pushed construction to record growth. The sector added 16,200 jobs, up 17.0% year-over-year. With a residential pipeline totaling 15,500 units in all stages of development and roughly 29 million square feet of industrial space under construction as of 3Q17, further growth is in store. Vacancy in the industrial sector is at cycle lows, while asking rents are moving closer to the $0.60 mark.

- Going forward, the challenge rests on the area's infrastructure, as growing freighting and accelerated expansion in both the commercial and residential sectors will exact pressure on the area's existing transit grid. An estimated $420 million from 2017's landmark SB 1 bill will be dedicated to fixing Riverside County's infrastructure woes.

### Inland Empire vs. National Employment Growth (Year-Over-Year)




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

### Inland Empire Employment Growth by Sector (Year-Over-Year)

| | | Current Employment | | Year Change | |
|---|---|---|---|---|---|
| Code | Employment Sector | (000) | % Share | Employment | % |
| 15 | Mining, Logging and Construction | 112 | 7.8% | 16,200 | 17.0% |
| 70 | Leisure and Hospitality | 163 | 11.4% | 5,100 | 3.2% |
| 65 | Education and Health Services | 220 | 15.3% | 4,600 | 2.1% |
| 90 | Government | 240 | 16.7% | 3,400 | 1.4% |
| 40 | Trade, Transportation and Utilities | 350 | 24.4% | 3,100 | 0.9% |
| 30 | Manufacturing | 101 | 7.0% | 1,600 | 1.6% |
| 80 | Other Services | 46 | 3.2% | 1,000 | 2.2% |
| 55 | Financial Activities | 46 | 3.2% | 700 | 1.5% |
| 50 | Information | 11 | 0.8% | -100 | -0.9% |
| 60 | Professional and Business Services | 147 | 10.2% | -500 | -0.3% |

Sources: YardiMatrix, Bureau of Labor Statistics

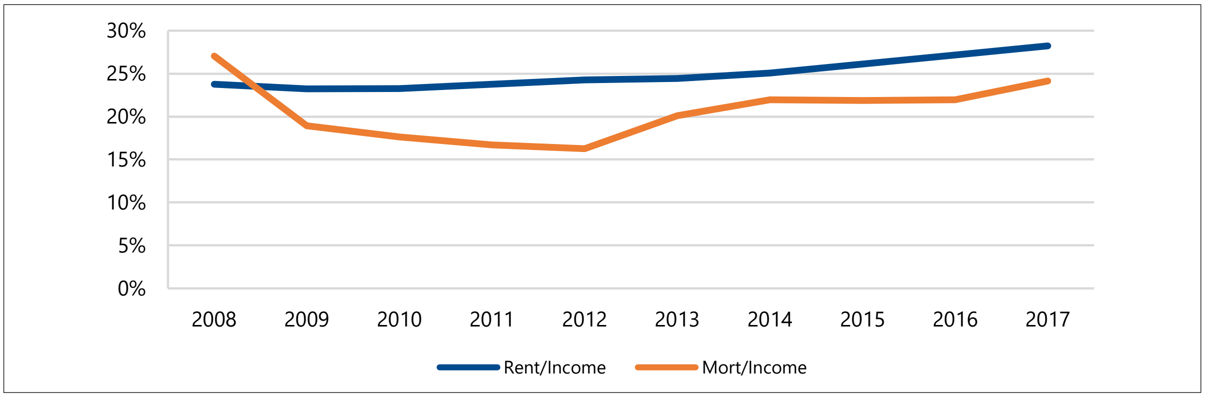
## Demographics

### Affordability

- The median home price in Riverside and San Bernardino counties hit $309,537 during the year's first half, 71% higher than in 2011, when the market bottomed out. With the area's economic makeup still dominated by the rise of its industrial sector, the metro relies on growth in low-paying sectors, which may dent affordability in the coming years.

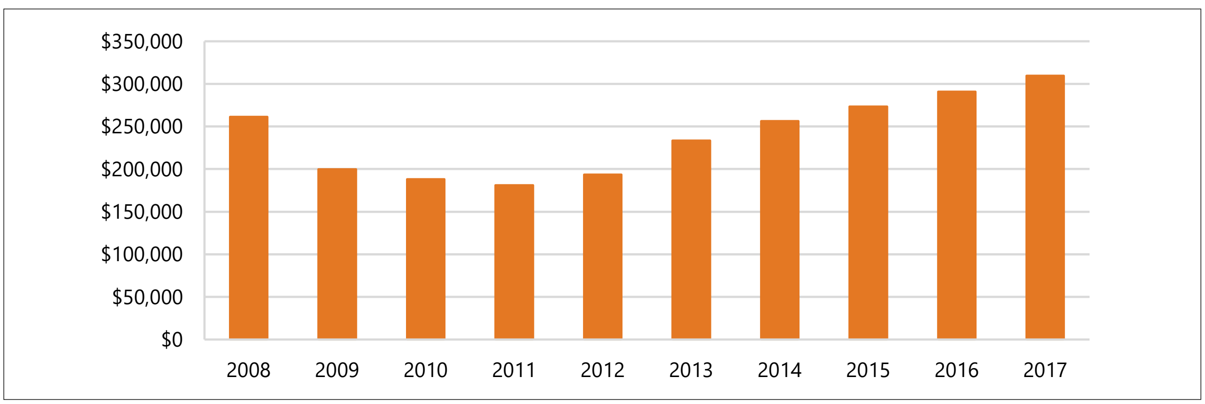
- Although both rents and mortgages in the Inland Empire are affordable compared to other markets in Southern California, continued property appreciation is affecting incomes. Rents accounted for 28% of median income, while home prices have rebounded to a point where the average mortgage payment equated to 25%.

**Inland Empire Rent vs. Own Affordability as a Percentage of Income**




Sources: YardiMatrix, Moody's Analytics

**Inland Empire Median Home Price**




Source: Moody's Analytics

### Population

- The Inland Empire's population grew at a rate of 1.2% in 2016, double the average U.S. rate. The metro added 52,400 residents.

- Population growth continues, spurred by affordability and employment opportunities.

**Inland Empire vs. National Population**

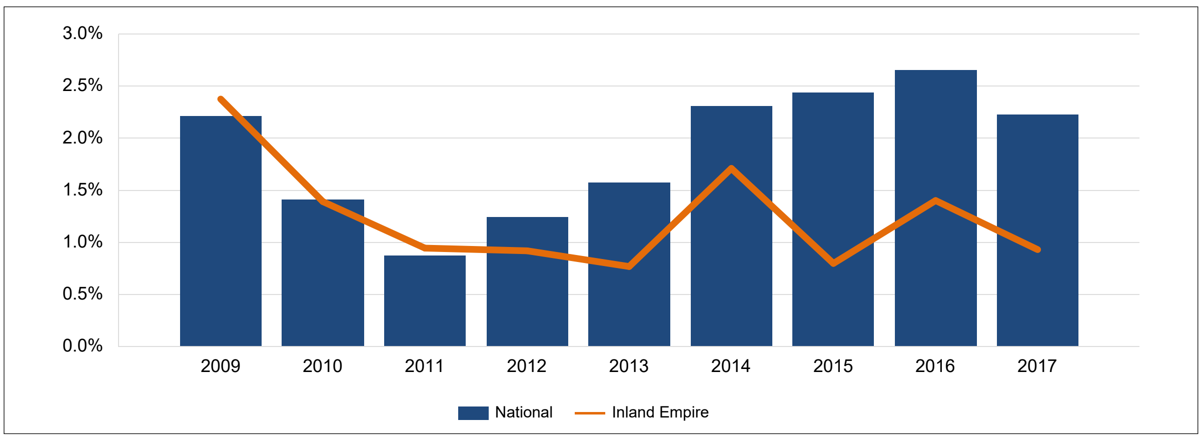
| | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|
| National | 313,998,379 | 316,204,908 | 318,563,456 | 320,896,618 | 323,127,513 |
| Inland Empire Metro | 4,342,166 | 4,379,397 | 4,428,390 | 4,475,437 | 4,527,837 |

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

## Supply

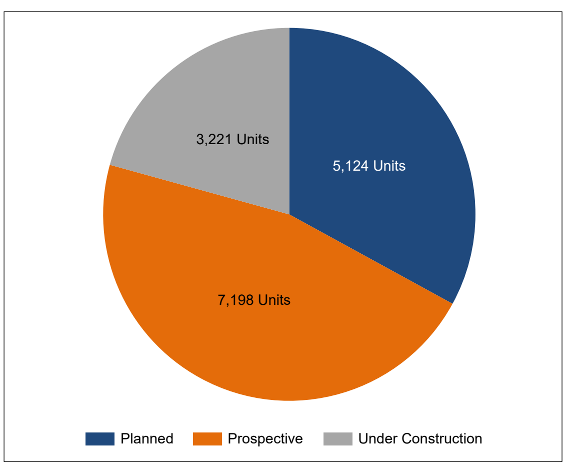
- Roughly 1,400 units were delivered in 2017 through November, 0.9% of total stock. The rate of completions was about half the national average, consistent with the generally tepid pace of deliveries in the Inland Empire this cycle.
- About 3,200 units were under construction in San Bernardino and Riverside counties, while another 12,300 were in the planning and permitting stages. As employment growth continues at above-average levels, and the area maintains its appeal as an affordable alternative to the increasingly prohibitive markets of Los Angeles and Orange counties, development is likely to continue at a consistent pace.
- Limited inventory growth in the Renter-by-Necessity segment has maintained the average occupancy rate in stabilized properties at 96.5% as of October. Although 40 basis points lower than it was 12 months prior, the occupancy rate remained relatively high.
- Developers are set to add units in Montclair/North Ontario (800 units under way), East Riverside (553 units) and Redlands/Yucaipa (340 units). The Paseos at Ontario is the largest community being constructed in the two counties, and is scheduled for completion at the end of 2018.

**Inland Empire vs. National Completions as a Percentage of Total Stock** (as of November 2017)



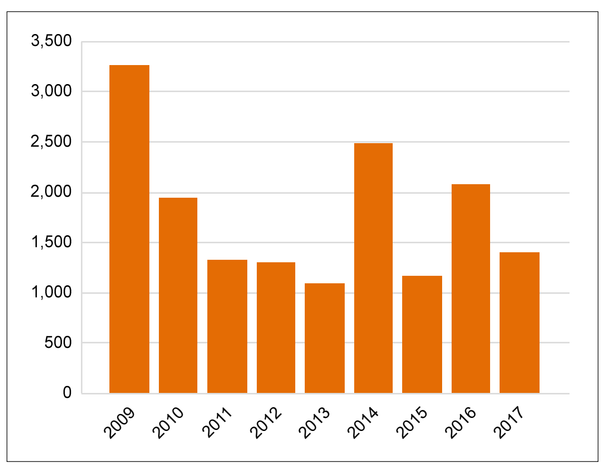

Source: YardiMatrix

**Development Pipeline** (as of November 2017)




Source: YardiMatrix

**Inland Empire Completions** (as of November 2017)

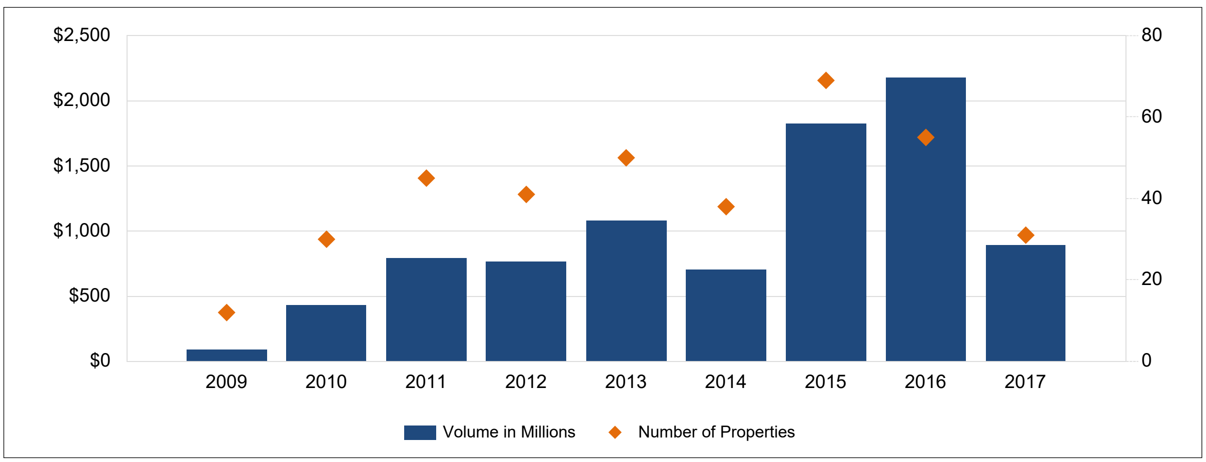



Source: YardiMatrix

## Transactions

- Roughly $900 million in multifamily properties traded in the Inland Empire in 2017 through October. Investment activity has somewhat tapered in Riverside and San Bernardino counties, following a banner year in 2016, when $2.2 billion in assets changed hands.
- The average per-unit price in 2017 was $165,341, a $6,000 slide compared to 2016. Two thirds of multifamily deals completed this year involved assets in the Renter-by-Necessity segment. Demand has pushed acquisition yields for stabilized Class A properties below the 5.0% mark.
- Although overall volumes are waning, properties in San Bernardino County traded for $700 million, while Riverside County assets claimed $500 million in the 12 months ending in October. Greystar's purchase of Avana Rancho Cucamonga for $122 million—or $195,192 per unit—was the largest deal of 2017 through October.

**Inland Empire Sales Volume and Number of Properties Sold** (as of October 2017)




Source: YardiMatrix

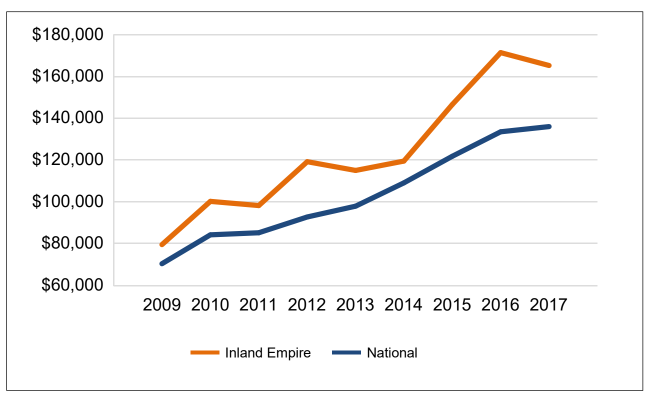
**Top Submarkets for Transaction Volume**[1]

| Submarket | Volume ($MM) |
|---|---|
| Rancho Cucamonga | 299 |
| Colton/Grand Terrace | 125 |
| Moreno Valley | 117 |
| Redlands/Yucaipa | 83 |
| Murrieta/Temecula | 75 |
| Upland/Alta Loma | 65 |
| North San Bernardino | 64 |
| Hemet/San Jacinto | 54 |

Source: YardiMatrix

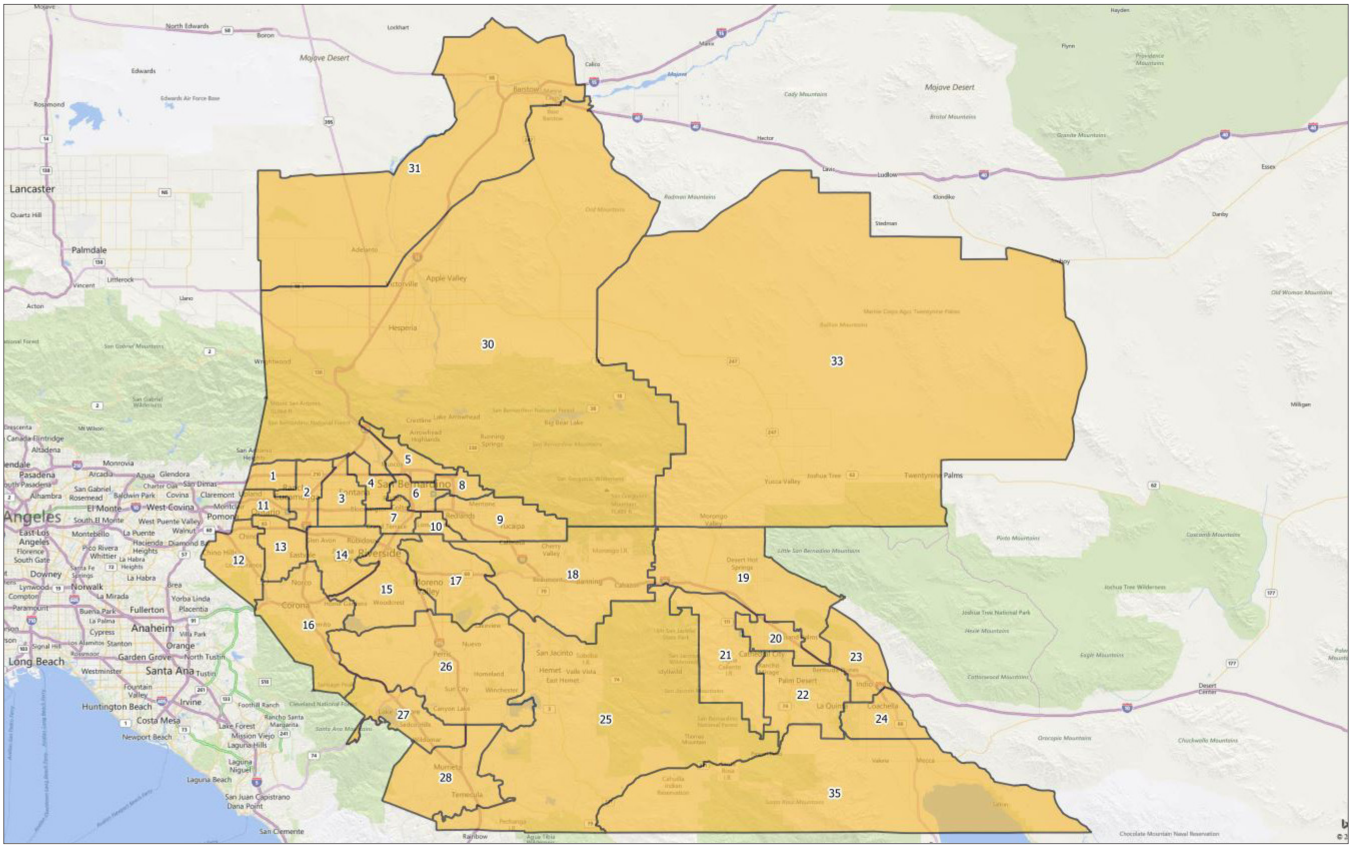
[1] From November 2016 to October 2017

**Inland Empire vs. National Sales Price per Unit**




Source: YardiMatrix

## Inland Empire Submarkets




| Area # | Submarket |
|---|---|
| 1 | Upland/Alta Loma |
| 2 | Rancho Cucamonga |
| 3 | Fontana |
| 4 | Rialto |
| 5 | North San Bernardino |
| 6 | South San Bernardino |
| 7 | Colton/Grand Terrace |
| 8 | Highlands |
| 9 | Redlands/Yucaipa |
| 10 | Loma Linda |
| 11 | Montclair/North Ontario |
| 12 | Chino/Chino Hills |
| 13 | South Ontario |
| 14 | West Riverside |
| 15 | East Riverside |
| 16 | Corona |

| Area # | Submarket |
|---|---|
| 17 | Moreno Valley |
| 18 | Beaumont/Banning |
| 19 | White Water/Desert Hot Springs |
| 20 | Thousand Palms/Cathedral City |
| 21 | Palm Springs |
| 22 | Palm Desert/La Quinta |
| 23 | Indio |
| 24 | Coachella |
| 25 | Hemet/San Jacinto |
| 26 | Nuevo/Perris/Menifee |
| 27 | Lake Elsinore |
| 28 | Murrieta/Temecula |
| 30 | Victorville/Apple Valley/Big Bear |
| 31 | Adelante/Oro Grande |
| 33 | Yucca Valley/Morongo Valley |

## 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.