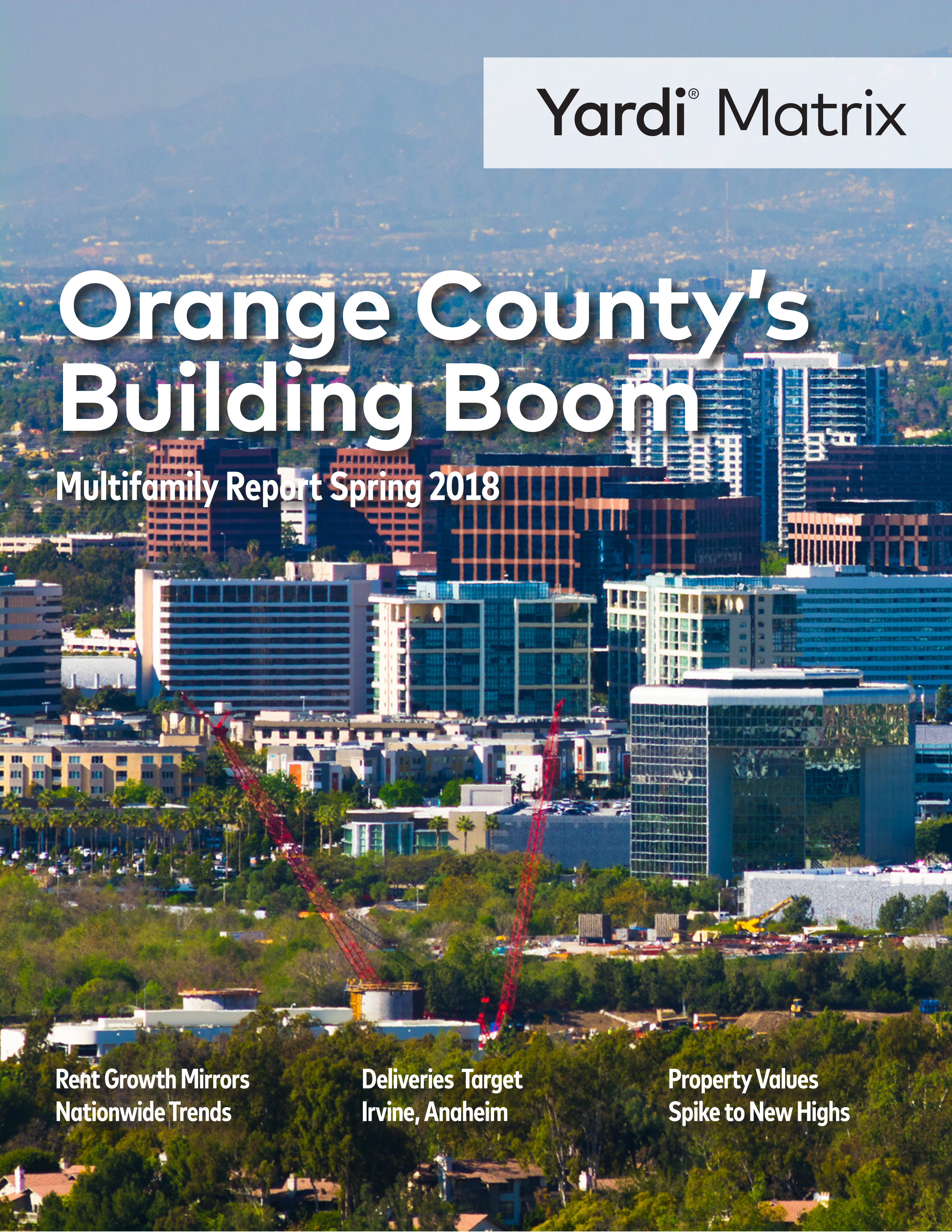

Yardi® Matrix

Orange County's Building Boom

Multifamily Report Spring 2018

Rent Growth Mirrors Nationwide Trends

Deliveries Target Irvine, Anaheim

Property Values Spike to New Highs

Market Analysis
Spring 2018

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Demand Eclipses Rising Supply

Apartment demand remains strong in Orange County, spurred by robust hiring in high-earning sectors and a high barrier to homeownership, which steers residents toward renting while giving landlords leverage to lift rents.

Despite a slowdown beginning in 2016, the metro's labor pool continues to expand, with the highest employment growth occurring in leisure and hospitality (9,800 jobs), followed by professional and business services (7,800). Construction hiring is also strong, due to office and housing development booms. Notable projects underway include JPI's Jefferson Stadium Park, which is set to bring more than 1,000 luxury apartments, a public park and retail to the Platinum Triangle.

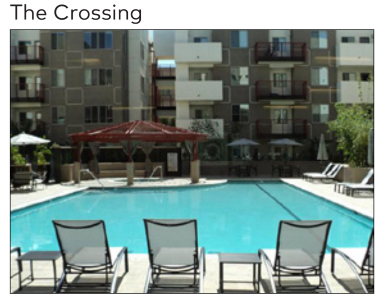
High costs are not discouraging multifamily developers, however. Rents continue to rise, maintaining attractive yields. In 2017, the apartment construction surge brought more than 5,100 units to the market, marking a post-recession high and nudging occupancy down to 96.0% as of January—a decline of 90 basis points over 12 months. The pipeline is also significant, with more than 8,200 units under construction as of February, most of them located in West Irvine, Anaheim, South Orange County and Santa Ana. Yardi Matrix expects demand to remain strong, pushing rents up 3.1% in 2018.

Recent Orange County Transactions

Surf at 39

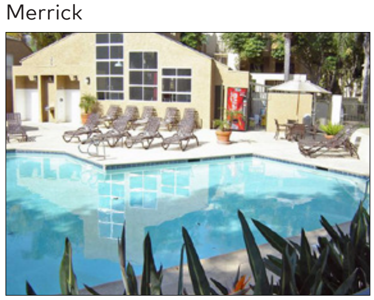
City: Huntington Beach, Calif.
Buyer: Interstate Equities Corp.
Purchase Price: $134 MM
Price per Unit: $335,000

The Crossing



City: Anaheim, Calif.
Buyer: RedHill Realty Investments
Purchase Price: $106 MM
Price per Unit: $339,744

Merrick



City: Placentia, Calif.
Buyer: Fairfield Residential
Purchase Price: $104 MM
Price per Unit: $250,962

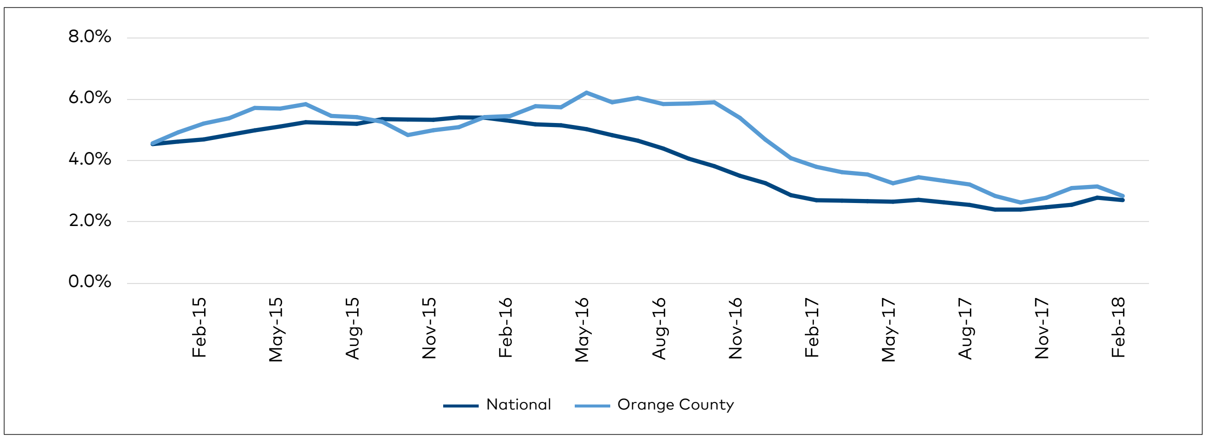
The Villas at Tustin

City: Santa Ana, Calif.
Buyer: Bascom Group
Purchase Price: $94 MM
Price per Unit: $231,527

Rent Trends

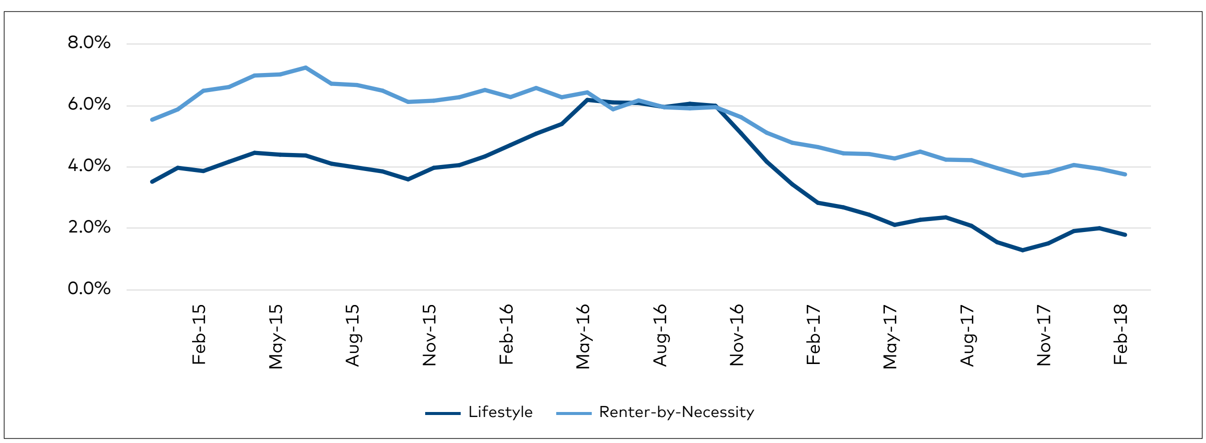
- Mirroring the national trend of deceleration, rents in Orange County rose 2.8% year-over-year through February, slightly above the 2.7% U.S. rate. The average rent stood at $2,024, well above the $1,364 national figure. Amid a surge of new supply, occupancy in stabilized properties slid to 96.0% as of January, a drop of 90 basis points from 12 months prior.
- Rents in the working-class Renter-by-Necessity segment rose 3.8% to $1,821, while Lifestyle rates increased by 1.8% to $2,324. Boosted by robust hiring in high-earning sectors—with single-family housing remaining out-of-reach for many residents—demand for rentals is strong, maintaining the metro's multifamily market as one of the most expensive in the country. Consequently, a large number of middle-income families are being priced out, according to the most recently available IRS data, which shows net population losses from people in the 35 -54 age bracket. Moving forward, absorption is expected to keep up with the surge in construction, pushing rents up by 3.1% in 2018.
- Submarkets with sharper rent growth include Fountain Valley (up 5.7%, to $1,882), Placentia (5.4%, to $1,804) and Tustin (4.9%, to $2,002). The highest rents are in Newport Beach ($2,702), South Irvine ($2,530), North Irvine ($2,291) and West Irvine ($2,307). A spate of deliveries this year may put further pressure on occupancy rates and restrict rent gains in West Irvine and Anaheim–Central ($1,879).

Orange County vs. National Rent Growth (Sequential 3-Month, Year-Over-Year)



Source: YardiMatrix

Orange County Rent Growth by Asset Class (Sequential 3-Month, Year-Over-Year)



Source: YardiMatrix

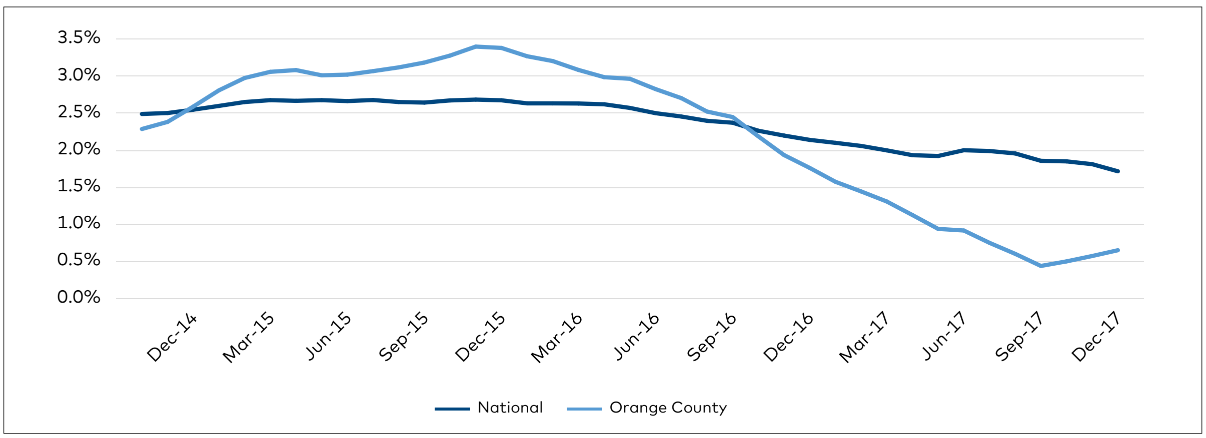
Economic Snapshot

- Orange County added 23,600 jobs in 2017 for a 0.7% uptick, trailing the 1.7% national average. Unemployment dropped to 2.8% during the same month, well below the 4.1% national rate, once again emphasizing the area's tight job market. Across the state, only San Francisco, Marin, Santa Clara and San Mateo had lower joblessness rates, mostly due to the Bay Area's ongoing technology boom.

- Growth remains bifurcated between low-paying jobs in segments such as leisure and hospitality (9,800)—thanks to a strong tourism industry—and high-paying professional and business services jobs (7,800). Construction is also expanding, boosted by large mixed-use projects and a multifamily supply surge, which peaked in 2017. Manufacturing lost 5,400 jobs, which could continue as some employers may be affected, in the long run, by the new tariffs on steel and aluminum imports.

- Office-using job creation continues to underpin demand for office space across the metro, where deliveries hit a post-recession high in 2017, according to Marcus & Millichap. Fewer projects are scheduled to come online this year, which may divert interest to existing space and bolster rent gains. The largest new developments include the 38-acre Flight at Tustin Legacy creative office campus, rising within the 1,600-acre master-planned community of Tustin Legacy, at the site of the former Marine Corps Air Station. Lincoln Property Co. and Alcion Ventures are building the two-phase project.

Orange County vs. National Employment Growth (Year-Over-Year)



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

Orange County Employment Growth by Sector (Year-Over-Year)

		Current Employment		Year Change	
Code	Employment Sector	(000)	% Share	Employment	%
70	Leisure and Hospitality	221	13.6%	9,800	4.6%
60	Professional and Business Services	308	19.0%	7,800	2.6%
15	Mining, Logging and Construction	105	6.5%	7,400	7.6%
65	Education and Health Services	209	12.9%	5,000	2.4%
80	Other Services	54	3.3%	3,700	7.4%
50	Information	26	1.6%	300	1.2%
40	Trade, Transportation and Utilities	271	16.7%	-200	-0.1%
55	Financial Activities	118	7.3%	-1,100	-0.9%
90	Government	160	9.9%	-3,700	-2.3%
30	Manufacturing	152	9.4%	-5,400	-3.4%

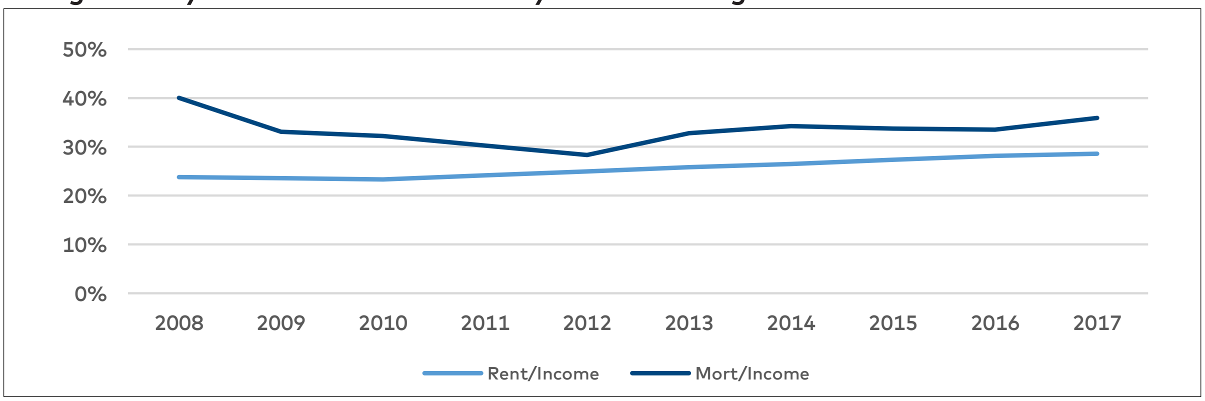
Sources: YardiMatrix, Bureau of Labor Statistics

Demographics

Affordability

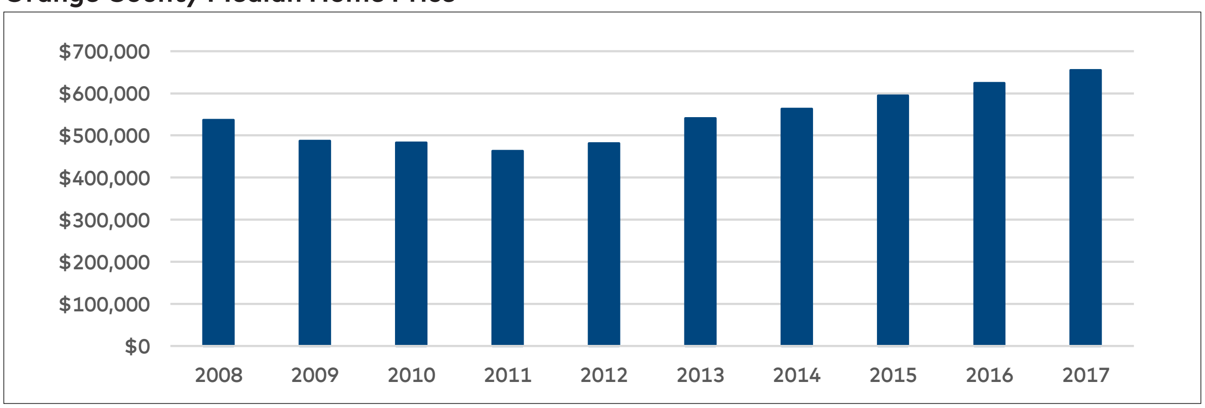
- The median home price in Orange County climbed to $655,282 in 2017, representing a new cycle high, but remained below the $700,000 historic peak recorded in 2007. The average mortgage payment accounted for 36% of the area's median income, while the average rent, albeit high in a national context, remained the more affordable option, comprising 29%.
- Orange County's overall cost of living was 87% higher than the national average, while the metro's median family income was only 41% higher than the U.S. median income, as per Orange County Community Indicators 2017. This gap is higher only in Los Angeles, San Francisco and San Diego.

Orange County Rent vs. Own Affordability as a Percentage of Income



Sources: YardiMatrix, Moody's Analytics

Orange County Median Home Price



Source: Moody's Analytics

Population

- Orange County added 15,959 residents in 2016 for a 0.5% uptick, trailing the 0.7% national rate.
- The metro grew by 97,600 people between 2012 and 2016 for a 2.8% rise, roughly on par with the U.S. average.

Orange County vs. National Population

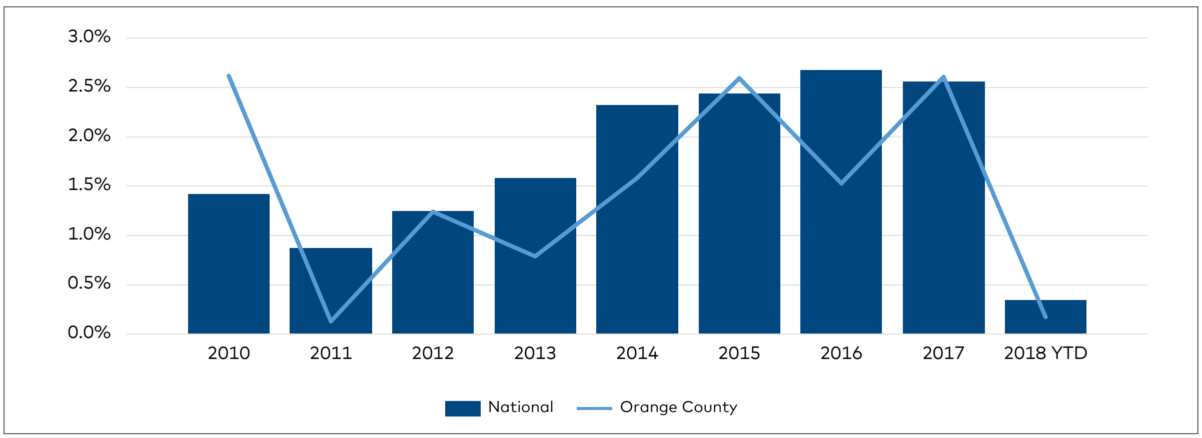
	2012	2013	2014	2015	2016
National	313,998,379	316,204,908	318,563,456	320,896,618	323,127,513
Orange County Metro	3,084,935	3,112,576	3,134,438	3,156,573	3,172,532

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

Supply

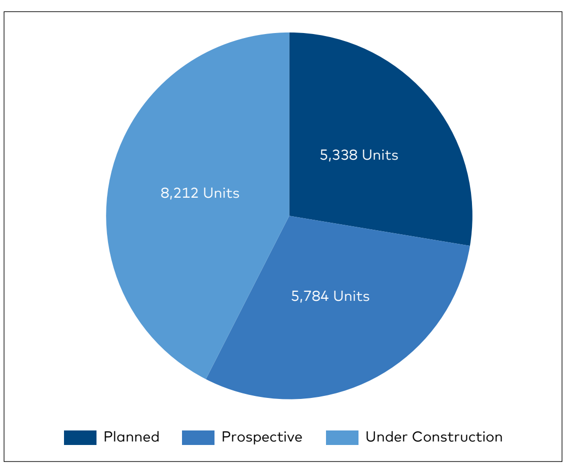
- More than 5,100 units came online in 2017, marking a post-recession high and accounting for 2.6% of total stock, in line with the national average. Despite the wave of new deliveries, the area's strong demand for apartments ensures steady absorption, boosting rent growth.
- Some 8,200 units were under construction as of February, more than 4,500 of which are expected for delivery by the end of 2018, while another 11,122 were on the drawing board. High construction costs are not discouraging developers, as rents continue to rise, keeping yields at attractive levels.
- The submarket with the highest number of units underway was West Irvine (1,738), which is luring an growing number of new residents, including people drawn by the area's renowned schools. Developers are also targeting Anaheim–Central, especially the flourishing Platinum Triangle, which is expected to reach 28,000 residents within two decades.
- The first two phases of Jefferson Stadium Park, JPI's development in the Platinum Triangle, are set to bring 647 luxury units by the fall of 2018. Plans also call for another 432 units, a public park and retail.

Orange County vs. National Completions as a Percentage of Total Stock (as of February 2018)



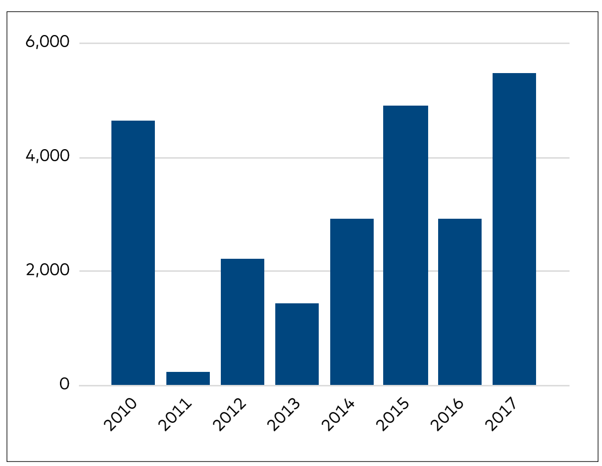
Source: YardiMatrix

Development Pipeline (as of February 2018)



Source: YardiMatrix

Orange County Completions (as of February 2018)

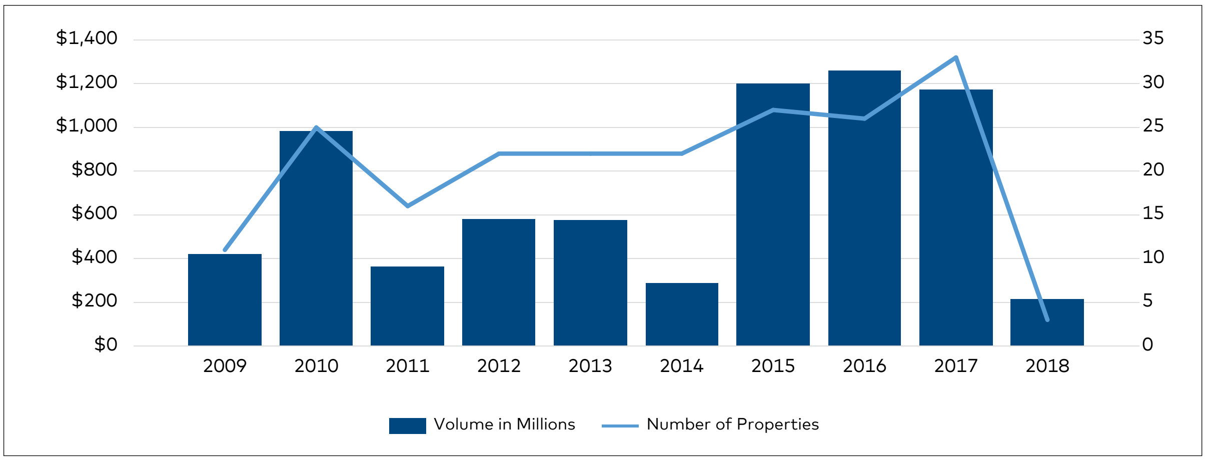


Source: YardiMatrix

Transactions

- Nearly $1.2 billion in multifamily assets traded last year, at an average per-unit price of $257,125. Three properties worth a combined $215 million changed hands in the first two months of 2018, at an average price per unit of $342,903, more than double the national average of $151,681.
- Orange County apartments are a hot commodity, having pushed transaction volumes above the $1 billion mark each of the past three years. This trend is set to continue, as rising rents and a high barrier to homeownership will continue to encourage investors, especially those looking for value-add opportunities.
- Interstate Equities' $134 million acquisition of the 400-unit Surf at 39 in Huntington Beach ranks as the largest deal of the 12 months ending in February. The company bought the workforce asset from Lone Star Funds in December, on behalf of a fund targeting value-add assets throughout coastal California.

Orange County Sales Volume and Number of Properties Sold (as of February 2018)



Source: YardiMatrix

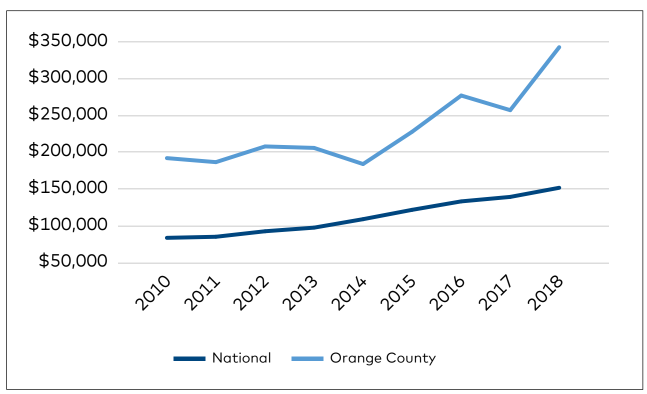
Top Submarkets for Transaction Volume[1]

Submarket	Volume ($MM)
Huntington Beach	276
Santa Ana	150
Anaheim–Central	111
Anaheim Hills	106
Placentia	104
Mission Viejo–Lake Forest	98
Garden Grove	84
Tustin	62

Source: YardiMatrix

[1] From March 2017 to February 2018

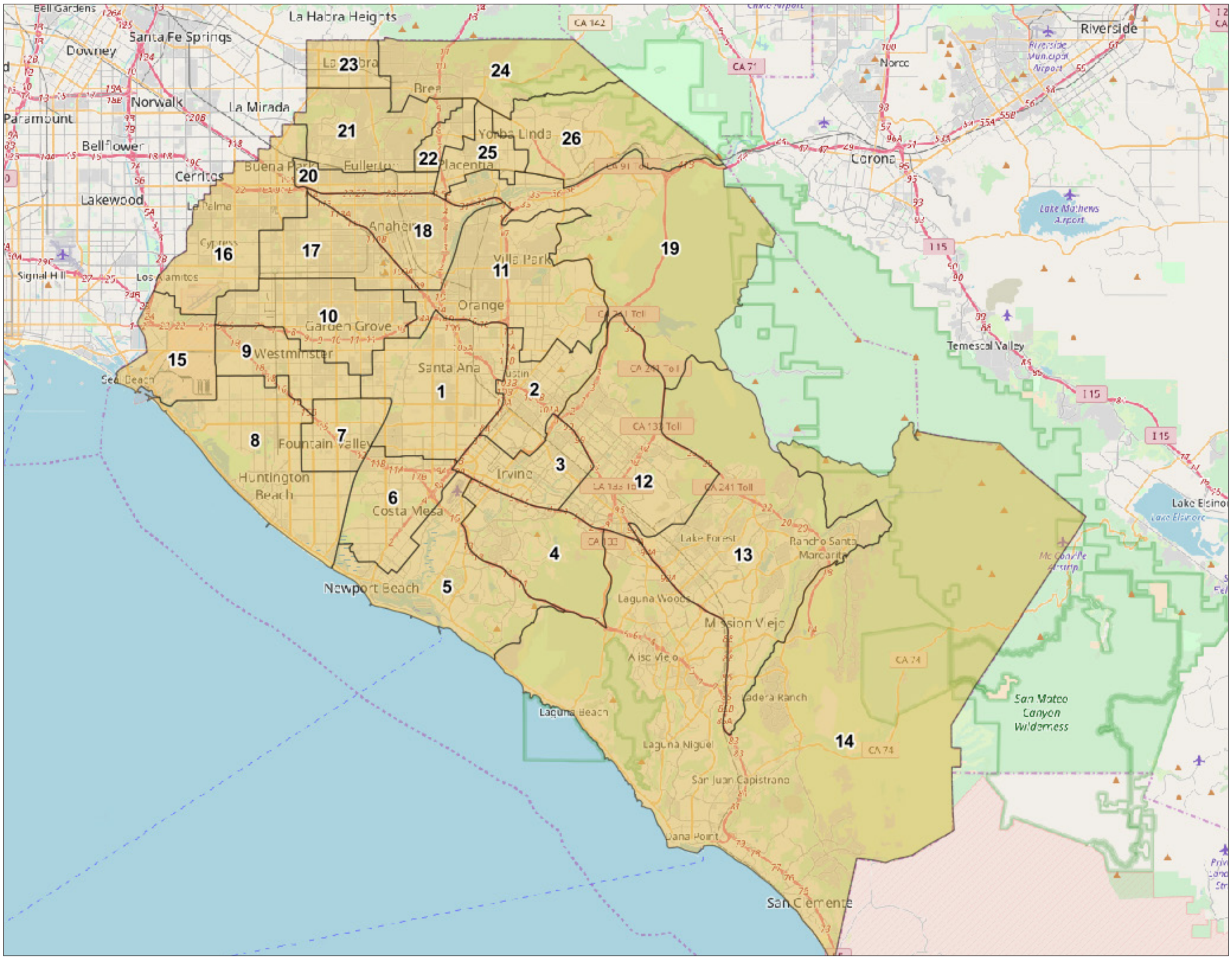
Orange County vs. National Sales Price per Unit



Source: YardiMatrix

Photo by Lagunatic Photo/iStockphoto.com

Orange County Submarkets



Area #	Submarket
1	Santa Ana
2	Tustin
3	Central Irvine
4	South Irvine
5	Newport Beach
6	Costa Mesa
7	Fountain Valley
8	Huntington Beach
9	Westminster
10	Garden Grove
11	Orange
12	West Irvine
13	Mission Viejo–Lake Forest

Area #	Submarket
14	South Orange County
15	Seal Beach
16	Buena Park–Cypress
17	Anaheim–West
18	Anaheim–Central
19	Anaheim Hills
20	Fullerton–South
21	Fullerton–North
22	Fullerton–University
23	La Habra
24	Brea
25	Placentia
26	Yorba Linda

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.

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