Yardi® Matrix

San Diego: Still In Expansion Mode

Multifamily Report Summer 2018

Development Accelerates

Rent Growth Outperforms US Average

Broad-Based Job Gains Continue to Fuel Demand

Market Analysis
Summer 2018

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Deliveries Slated for Cycle Peak

Strong demand and a relatively slow pipeline keep San Diego as one of the country's most stable multifamily markets. Rent growth, at 4.1% year-over-year as of April, continued to heavily outperform the U.S. rate, while the metro struggles with ongoing affordability.

Anchored by the U.S. Navy, prestigious universities, biotechnology clusters and tourism, San Diego's economy continues to diversify. While the construction sector expanded at the fastest rate, with several large-scale developments underway across the metro, the next spate of mega-projects is already lined up: Hines is planning a $2 billion repurposing of Riverwalk Golf Club in Mission Valley; the $1.5 billion Seaport San Diego is slated to break ground in a couple of years; and SDCCU Stadium is getting closer to redevelopment.

San Diego had roughly 8,300 units under construction as of April, and the metro is expected to add more than 5,000 units throughout 2018. This would mark a strong cycle peak, surpassing the 3,800 units delivered in 2016. In line with nationwide trends, occupancy in stabilized properties dropped 110 basis points in 12 months, to 96.1% as of March. Even so, as San Diego's housing crisis deepens and rental demand is poised to remain strong, Yardi Matrix expects rents to advance by 3.5% in 2018.

Recent San Diego Transactions

Carmel Pacific Ridge

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

Avion at Spectrum

City: San Diego
Buyer: Prime Group
Purchase Price: $140 MM
Price per Unit: $312,567

Olympus Corsair

City: San Diego
Buyer: Olympus Property
Purchase Price: $137 MM
Price per Unit: $379,167

Waterleaf

City: Vista, Calif.
Buyer: MG Properties Group
Purchase Price: $118 MM
Price per Unit: $257,675

On the cover: Photo by Art Wager/iStockphoto.com

Rent Trends

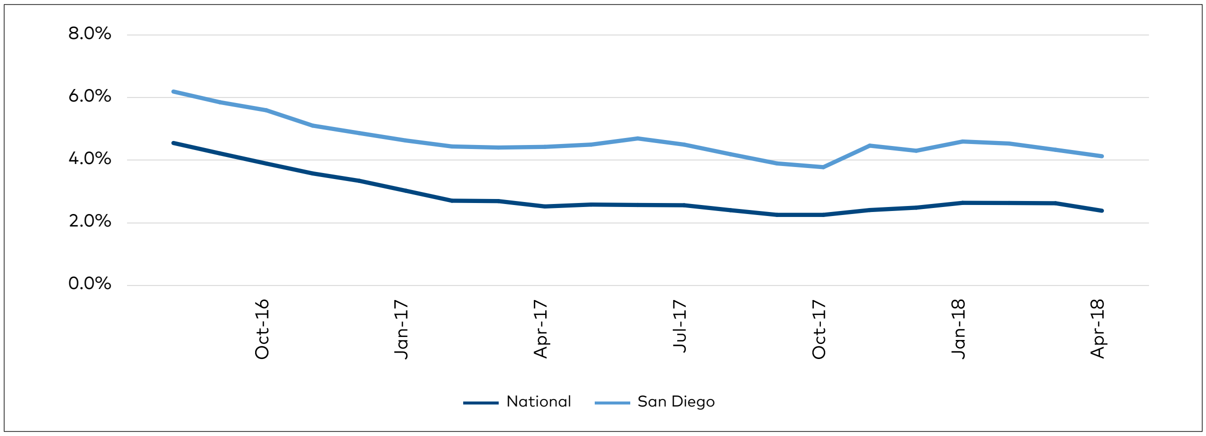
- San Diego rents rose 4.1% year-over-year through April, heavily outperforming the 2.4% U.S. rate. Due to its resilient and diversified economy, steady demographic growth and relatively restricted residential pipeline, the metro remained one of the country's most stable multifamily markets for the better part of the cycle. The average rent clocked in at $1,869 in April, well above the $1,377 U.S. figure.

- Rents in the working-class Renter-by-Necessity segment were up 4.6%, reaching $1,615. Meanwhile, Lifestyle rents rose by 3.6%, to $2,283. Although demand is strong in both asset classes and the metro is generating jobs across the board, the area's affordable housing crisis continues to deepen, due to a slow pipeline and the lack of new workforce stock.

- All San Diego submarkets registered growth, with rents advancing slowly in more expensive areas such as Central San Diego (2.0% to $2,154), Coronado (2.4% to $2,501) and Del Mar (2.6% to $2,597). Non-core areas including Escondido (7.6%), Santee (6.6%) and San Marcos (6.6%) led growth.

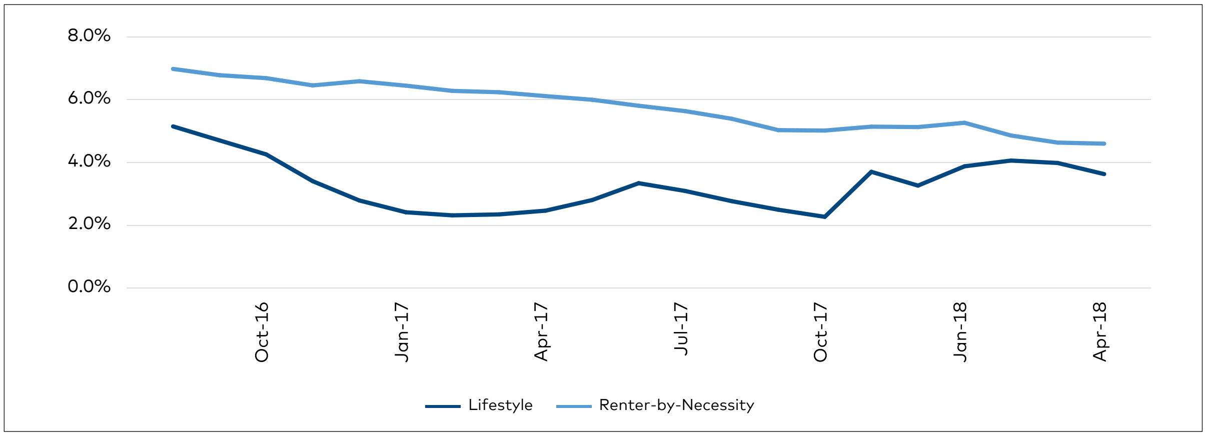
- Occupancy in stabilized properties dropped 110 basis points in 12 months, to 96.1% as of March, but still remains above the 94.9% U.S. average. Although the metro is set for a banner year in deliveries, demand should remain relatively strong, generating a 3.5% rent growth in 2018.

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)

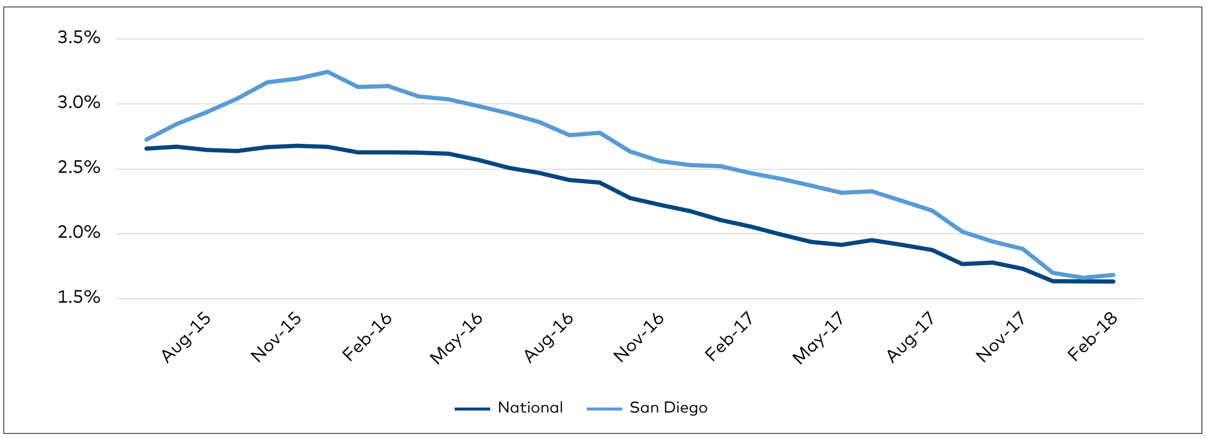


Source: YardiMatrix

Economic Snapshot

- San Diego added 27,900 jobs in the 12 months ending in February for a 1.7% uptick year-over-year, roughly on par with the U.S. rate. Continuing to add positions across the board—albeit at a decelerating pace—the metro is attracting highly skilled Millennials, due to its strong job market and relative affordability compared to other major metros in the state.
- Professional and business services led gains, with the addition of 8,700 positions. The sector's steady expansion continues to fuel demand in the office sector. According to Yardi Matrix data, San Diego had more than 2.2 million square feet of office space underway as of mid-May, nearly double the figure recorded at the start of 2018.
- The construction sector added 5,200 positions and recorded the highest expansion rate—6.8%—as the metro's development pipeline continues to add large projects at a fast pace. Manchester Financial Group secured financing for its $1.5 billion, 3 million-square-foot Manchester Pacific Gateway; the eight-block mixed-use development is slated for full completion by 2021. Other large-scale projects are also moving forward, including the 210-acre Millenia Master Plan in Chula Vista and the $2.1 billion, 11-mile trolley expansion that will connect downtown to University City.

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	%
60	Professional and Business Services	240	16.4%	8,700	3.8%
65	Education and Health Services	208	14.2%	5,200	2.6%
15	Mining, Logging and Construction	82	5.6%	5,200	6.8%
30	Manufacturing	111	7.6%	3,600	3.3%
90	Government	252	17.2%	2,900	1.2%
40	Trade, Transportation and Utilities	228	15.6%	1,300	0.6%
55	Financial Activities	74	5.1%	700	1.0%
80	Other Services	54	3.7%	400	0.7%
50	Information	24	1.6%	-	0.0%
70	Leisure and Hospitality	190	13.0%	-100	-0.1%

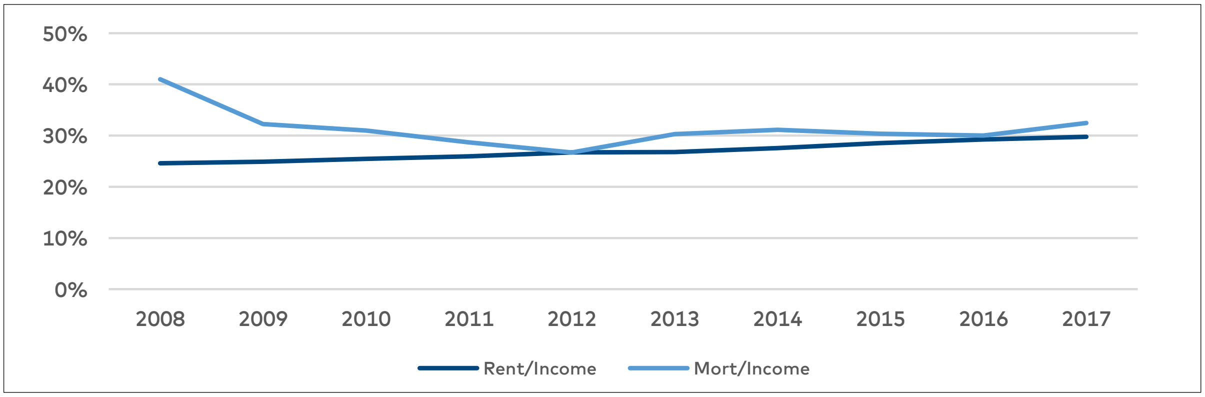
Sources: YardiMatrix, Bureau of Labor Statistics

Demographics

Affordability

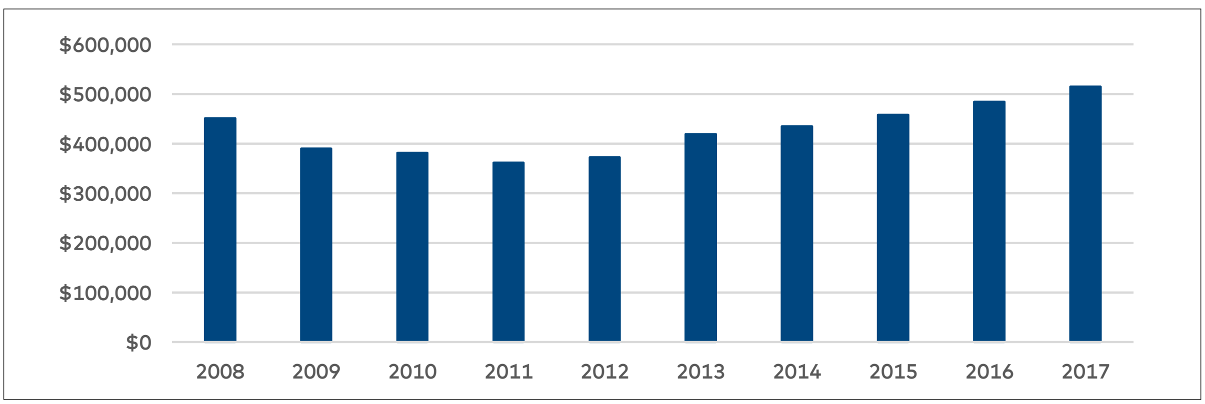
- The San Diego median home price reached $514,502 in 2017, a 6% uptick year-over-year and 42% over the 2011 figure. Surging values are elevating the barrier for first-time buyers even further and boosting rental demand along the way. Renting is slightly more affordable, with the average rent accounting for 30% of the area median income, while the average mortgage payment equates to as much as 32%.
- With the Affordable Housing Act close to this November's State ballot and other similar initiatives just passed or in the works, California's housing crisis could find some relief in the long run. For the time being, however, issues continue to deepen in San Diego and other metros across the state.

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 20,000 residents in 2017 for a 0.6% expansion, just 10 basis points under the national average.
- The metro gained more than 120,000 people since 2013, marking a 3.8% rise, some 80 basis points over the U.S. rate.

San Diego vs. National Population

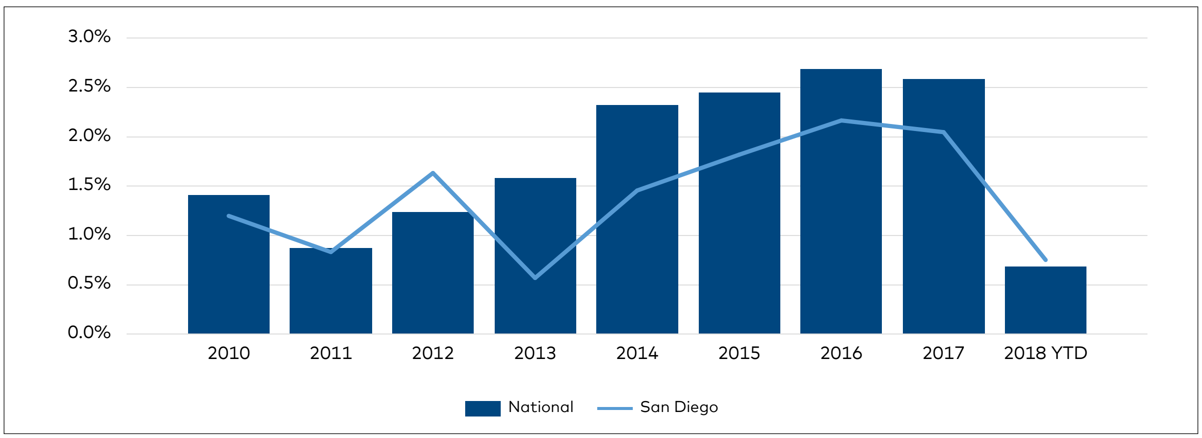
	2013	2014	2015	2016	2017
National	316,234,505	318,622,525	321,039,839	323,405,935	325,719,178
San Diego Metro	3,216,522	3,256,875	3,290,044	3,317,200	3,337,685

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

Supply

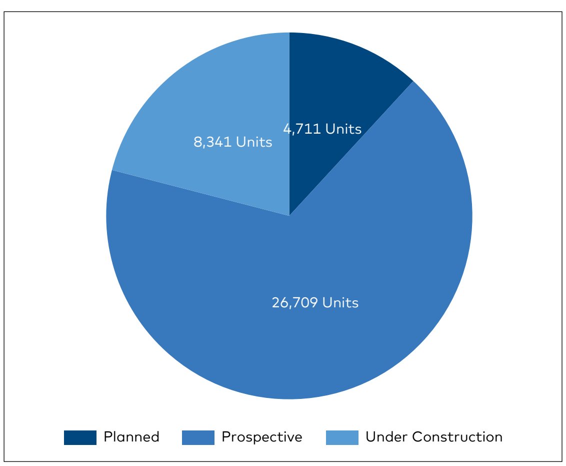
- Seven properties adding as many as 1,356 units were delivered in 2018 through April, three of them located in the Central San Diego submarket. This comes on the heels of several years when construction activity was heavily focused on upscale assets. Since 2015, more than 11,000 have been completed, less than a quarter of which were in fully affordable communities.
- Roughly 8,300 units were underway in the metro as of April, almost half of which were being built in Central San Diego. The core submarket leads the multifamily pipeline by far (3,677 units), followed by University (860), Mira Mesa (810) and Kearny Mesa (553). The total San Diego pipeline counts nearly 40,000 units.
- Although San Diego's inventory expansion underperformed against the U.S. average for the better part of the cycle, while its population rose at a rapid pace, the metro is set for a banner construction year. Yardi Matrix expects the delivery of 5,221 units for the year, which is set to mark a new cycle peak. That is expected to result in a slight dampening of rent growth and partial alleviation of some of the metro's affordability issues.

San Diego vs. National Completions as a Percentage of Total Stock (as of April 2018)



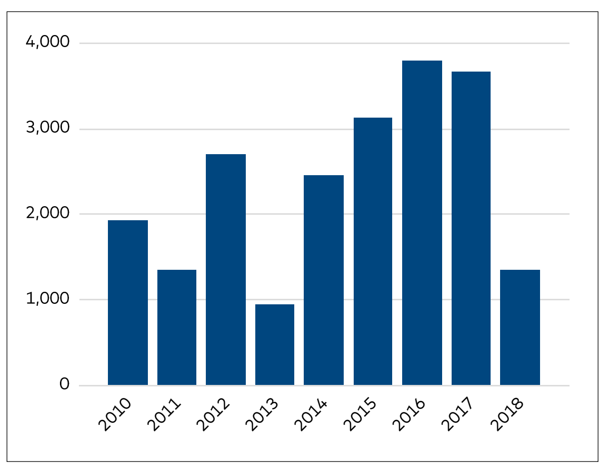
Source: YardiMatrix

Development Pipeline (as of April 2018)



Source: YardiMatrix

San Diego Completions (as of April 2018)

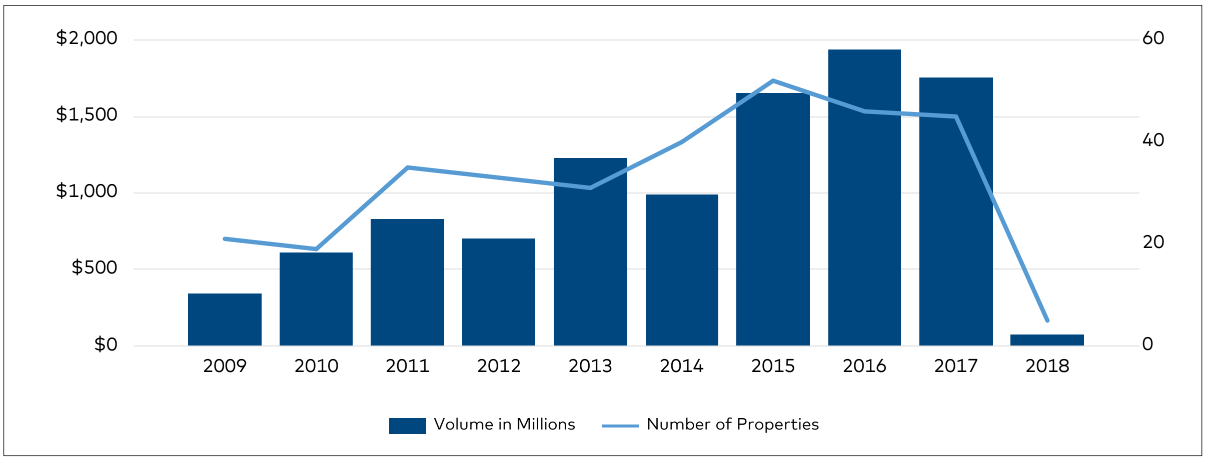


Source: YardiMatrix

Transactions

- Following three years of intense investor activity, only $73 million in multifamily assets traded in San Diego in 2018 through April. Roughly $5.3 billion in rental properties traded between 2015 and 2017, with investors heavily targeting value-add opportunities.
- All assets sold during the year's first four months were workforce housing, which pushed down the per-unit price to $217,507—significantly less than 2017's $256,650. Even so, prices remain well above the $146,694 U.S. average. The metro offers some of the lowest U.S. acquisition yields, starting at about 3.5% for stabilized Class A assets and reaching between 5.0% and 6.0% for value-add properties.
- Kearny Mesa attracted the most capital in the 12 months ending in April. During this time, six assets traded in the submarket for $597 million, at an average price of about $350,000 per unit.

San Diego Sales Volume and Number of Properties Sold (as of April 2018)



Source: YardiMatrix

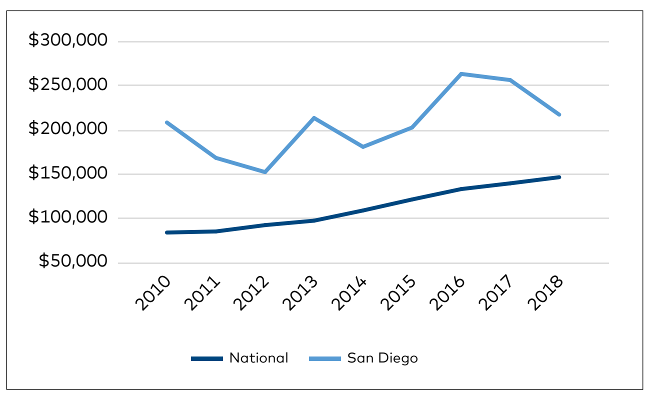
Top Submarkets for Transaction Volume[1]

Submarket	Volume ($MM)
Kearny Mesa	597
Oceanside	288
Mira Mesa	151
El Cajon	108
Escondido	108
Mid-City	65
La Mesa	55
Del Mar	55

Source: YardiMatrix

[1] From May 2017 to April 2018

San Diego vs. National Sales Price per Unit



Source: YardiMatrix

News in The Metro

Brought to you by: MULTI-HOUSING NEWS

San Diego Mixed-Use Tower Tops Out

The Richman Group of California Development Co. and Level 10 Construction have topped out K1, which includes 220 units and 7,000 square feet of commercial space.

Sunrise Management Strengthens Small Property Division

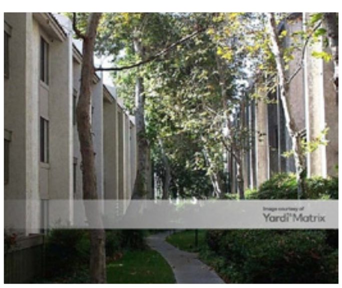
Peyton Hoban will serve as director of the company's small property department and Eric Paulin will be regional manager of the same branch.

Pathfinder Partners, Lanshire Complete CA Townhomes

Bahia Vista II in Chula Vista offers 16 townhomes and a tot lot, a paved trail and private patios. The community is scheduled for completion by August 2018.

Mazis Family Trust Buys 19-Unit San Diego Community

Located at 4560 Florida St., in the University Heights neighborhood, the 1970-built property features a mix of 13 two-bedroom and six one-bedroom units.



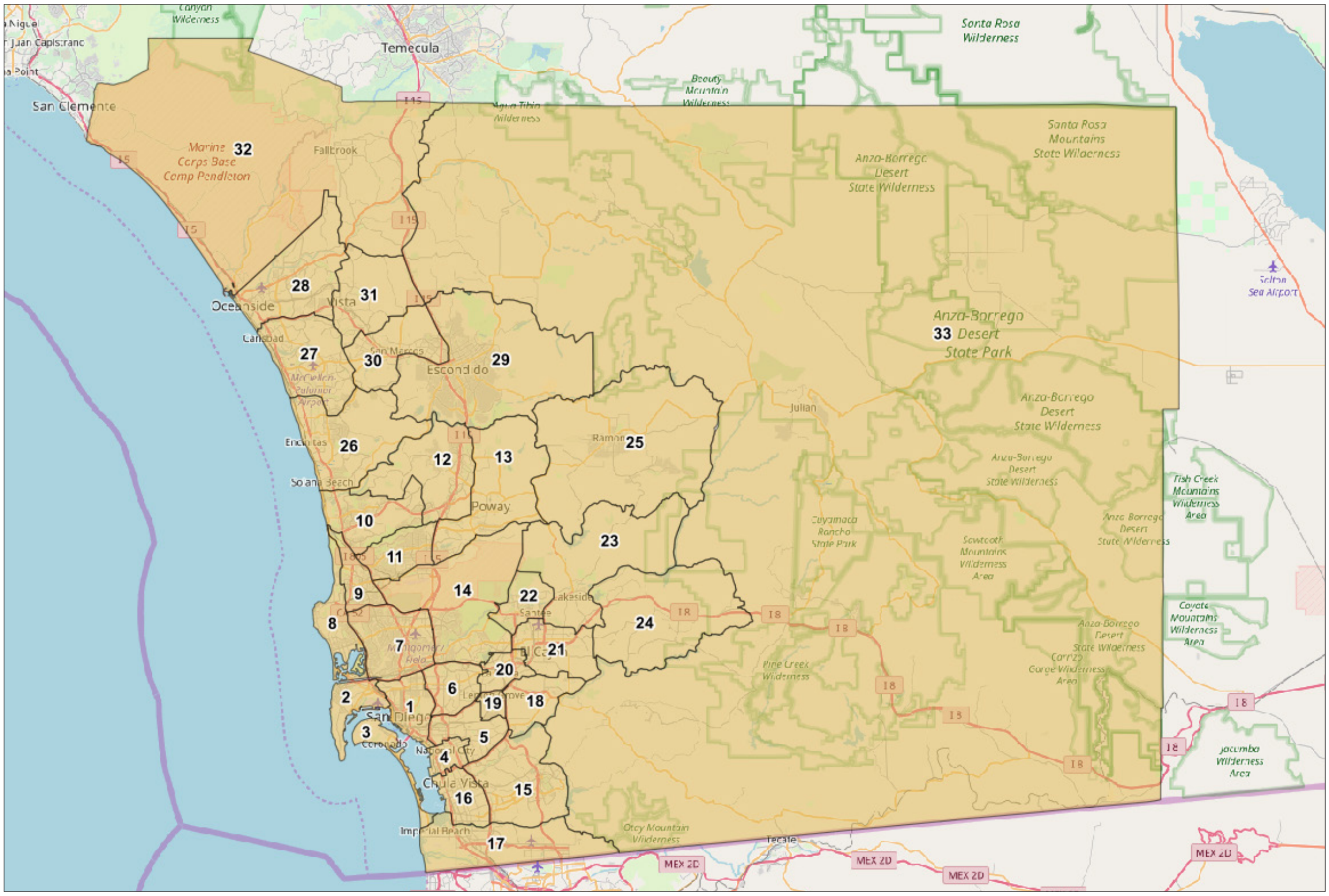
Sares Regis Picks Up San Diego Asset

The company financed the acquisition of the 344-unit property with an $80 million loan, which will also be used to fully redevelop it.

San Diego Community Opens, Lands New Management

The 97-unit multifamily property in the city's southern suburbs, 15 miles from downtown, contains a mix of one- and two-bedroom apartments.

San Diego Submarkets



Area #	Submarket
1	Central San Diego
2	Peninsula
3	Coronado
4	National City
5	Southeast San Diego
6	Mid-City
7	Kearny Mesa
8	Coastal
9	University
10	Del Mar
11	Mira Mesa
12	North San Diego
13	Poway
14	Elliot–Navajo
15	Sweetwater
16	Chula Vista
17	South Bay

Area #	Submarket
18	Spring Valley
19	Lemon Grove
20	La Mesa
21	El Cajon
22	Santee
23	Lakeside
24	Alpine
25	Ramona
26	San Dieguito
27	Carlsbad
28	Oceanside
29	Escondido
30	San Marcos
31	Vista
32	Fallbrook
33	Outlying San Diego County

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.