



YARDI® Matrix

San Diego: SoCal's Surge

Multifamily Winter Report 2017

**Millennial Influx
Boosts Rents**

**Biotech Accelerates
Hiring Pace**

**Supply Favors
Transit Adjacency**

Market Analysis

Winter 2017

Contacts

Paul Fiorilla

Associate Director of Research
Paul.Fiorilla@Yardi.com
(800) 866-1124 x5764

Jack Kern

Director of Research and Publications
Jack.Kern@Yardi.com
(800) 866-1124 x2444

Author

Bogdan Odagescu

Associate Editor

Rising Economic Tide Lifts Real Estate

Displaying solid job gains and above-average population growth, San Diego continues to offer healthy multifamily fundamentals, although it is suffering from an affordability crisis due to a prolonged housing shortage. With above-trend rent growth—220 basis points over the U.S. average—and outsize demand, the city continues to offer good prospects for both value-add investors and developers.

Benefiting from a deep talent pool and a major network of universities, colleges and research facilities, San Diego boasts not only the title of biotech capital of the West but also a reputation as a more affordable alternative to Silicon Valley. At the same time, the city's job market relies on several large and stable employers, including naval facilities, defense contractors, health-care providers, iconic tourist destinations and higher-education and research clusters. The \$2 billion trolley expansion project, which recently covered half of its cost through federal funding, is ready to reshape San Diego's multifamily market. Developers have already taken note, with construction heating up along the Interstate 5 corridor between Old Town and University. Other major projects include the \$1.3 billion Manchester Pacific Gateway and the \$1.2 billion Seaport Village redevelopment project.

With rents growing 6.6% in one year to an average of nearly \$1,700, multifamily supply in San Diego is barely keeping up with demand. The current pipeline of 30,800 units, coupled with a solid investment volume—roughly \$3 billion in the last two years—is rounding out San Diego's image as a dynamic and safe secondary market.

Recent San Diego Transactions

IMT Sorrento Valley



City: San Diego
Buyer: IMT Capital
Purchase Price: \$214 MM
Price per Unit: \$284,575

eaves Rancho San Diego



City: El Cajon, Calif.
Buyer: R&V Management
Purchase Price: \$158 MM
Price per Unit: \$233,728

Form 15



City: San Diego
Buyer: Essex Property Trust
Purchase Price: \$98 MM
Price per Unit: \$403,504

Pulse Millenia

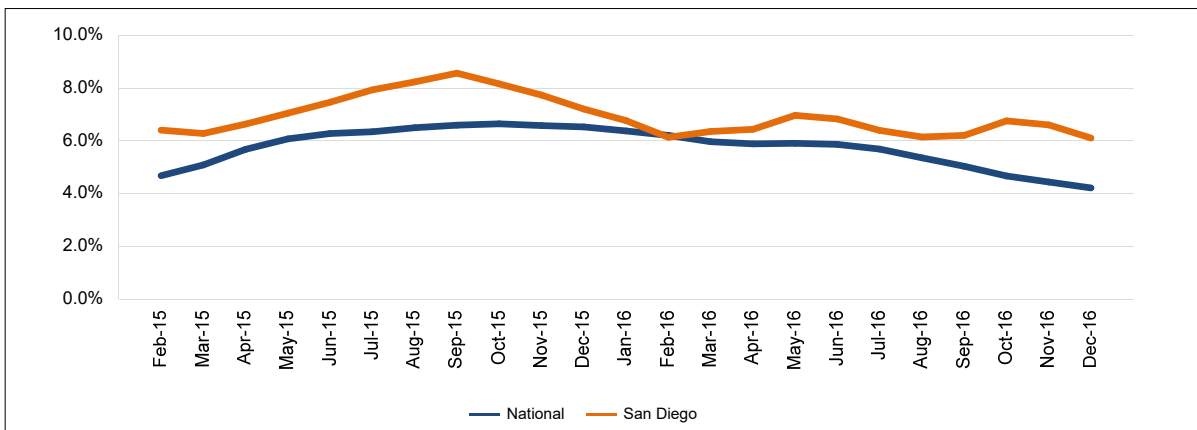


City: Chula Vista, Calif.
Buyer: Northwestern Mutual RE Investors
Purchase Price: \$94 MM
Price per Unit: \$343,590

Rent Trends

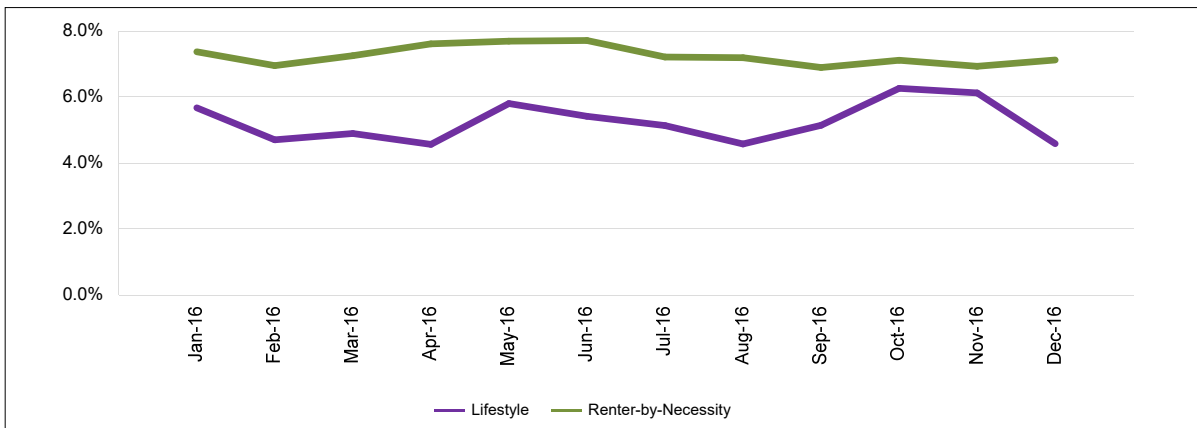
- Rents in San Diego grew 6.6% year-over-year through November, 220 basis points above the U.S. rate. Rents reached \$1,681, well over the \$1,214 national average. Like most large U.S. metro areas, San Diego recorded rent growth deceleration during the past quarter, though it still outperforms the national rate.
- Rents in the Lifestyle sector grew 6.0% year-over-year to \$2,115. Working-class Renter-by-Necessity properties average \$1,503, a 6.9% rise. These strong numbers reflect the city's healthy level of demand, influenced by population growth, the rising number of higher-paid jobs, an influx of highly skilled Millennials prone to renting, as well as an underperforming level of new stock.
- Core submarkets are leading growth, with Mid-City (13.8%), El Cajon (9.8%) and La Mesa (8.8%) topping the list. Affluent northern areas are also recording above-trend rent surges, especially Vista (8.5%) and Oceanside (8.2%). Developers, however, are focusing on different opportunities: The five submarkets leading growth have fewer than 350 units under construction.
- Five upscale submarkets, all of them north of Kearny Mesa, have average rents above the \$2,000 mark. Del Mar (\$2,833) is followed by University (\$2,167), Poway (\$2,129), Carlsbad (\$2,006) and San Dieguito (\$2,003). All five have recorded rent growth levels below the metro's 6.6% average, a sign of oversaturation.

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)

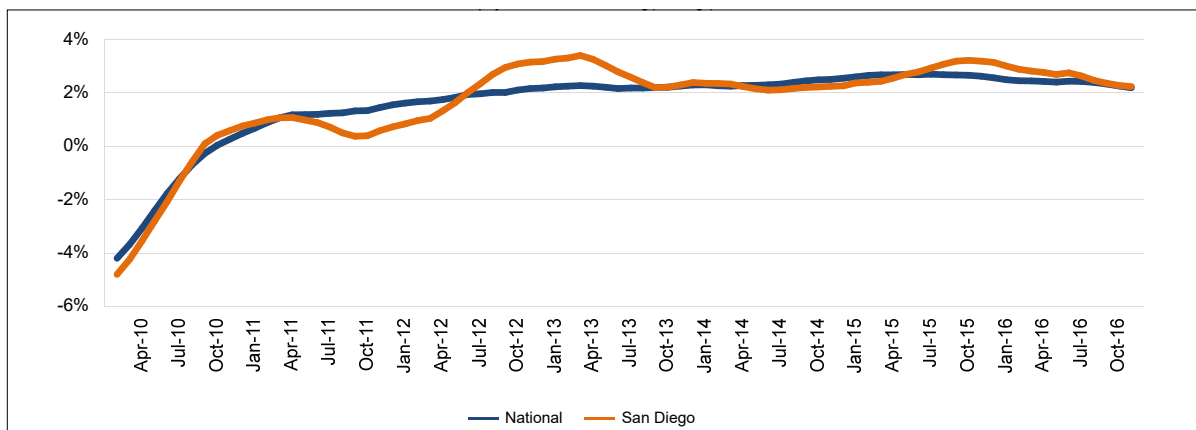


Source: YardiMatrix

Economic Snapshot

- San Diego added 30,900 jobs in the last year, on par with the 2.3% national growth rate. The city's job market relies on a wide range of large employers, including naval facilities, defense contractors and higher-education and research clusters.
- The education and health-services sector leads growth, contributing 8,100 jobs. Boosted by a strong network of universities and research centers, San Diego's biotechnology industry continues to draw highly skilled Millennials. The leisure and hospitality sector added 7,100 jobs year-over-year. Aided by the area's climate, beaches, convention center and iconic attractions, year-round tourism remains a San Diego staple.
- San Diego's tech- and research-and-development-driven office market continues to thrive. During the past year, the professional and business services and the information sectors added a combined 7,400 jobs. According to CBRE, San Diego's office market is in its expansion phase, with rents rising and vacancy rates compressing. This trend contrasts with most West Coast metros that have a strong tech component, including the San Francisco Bay Area and Portland, Ore., which are currently in the maturation phase of the cycle.
- Due to its economic stability, the city has no shortage of large developments. The trolley expansion project recently secured \$1 billion in federal financing and is slated for completion by 2021; the \$1.3 billion waterfront Manchester Pacific Gateway is on track; and the \$1.2 billion Seaport Village redevelopment project only recently received the port's green light.

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)

Code	Employment Sector	Current Employment		Year Change	
		(000)	% Share	Employment	%
65	Education and Health Services	202	14.2%	8,100	4.2%
60	Professional and Business Services	239	16.8%	7,100	3.1%
70	Leisure and Hospitality	195	13.7%	7,100	3.8%
90	Government	238	16.7%	6,200	2.7%
40	Trade, Transportation and Utilities	221	15.5%	3,000	1.4%
55	Financial Activities	73	5.1%	900	1.3%
50	Information	24	1.7%	300	1.3%
30	Manufacturing	106	7.4%	-200	-0.2%
15	Mining, Logging and Construction	72	5.1%	-700	-1.0%
80	Other Services	53	3.7%	-900	-1.7%

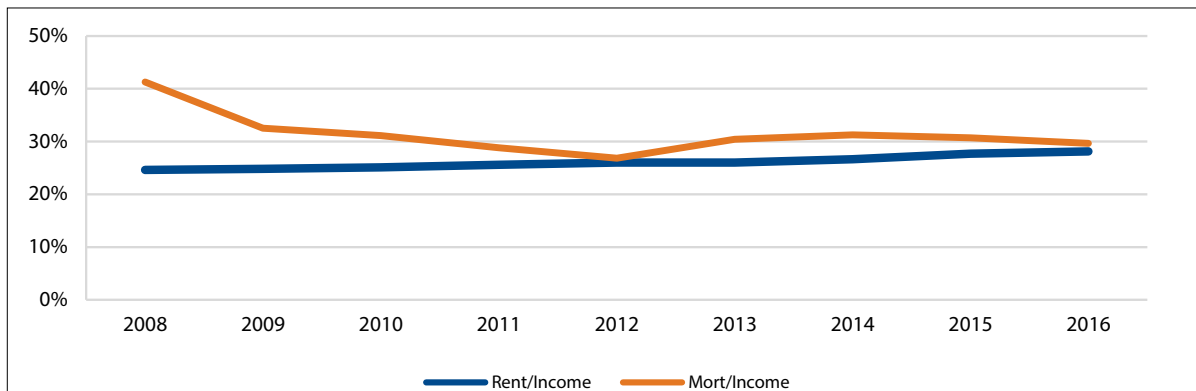
Sources: YardiMatrix, Bureau of Labor Statistics

Demographics

Affordability

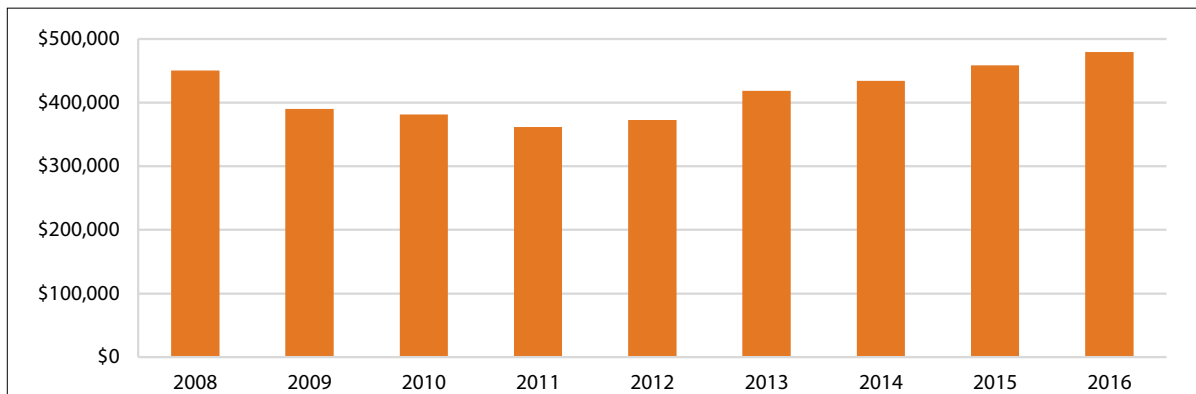
- San Diego's median home price reached \$479,279 in 2016, the highest point in the current cycle and more than double the national average. The city continues to be one of the most expensive in the U.S., with the widening disparity predominantly impacting lower-income households.
- When it comes to affordability, there is little difference between renting and owning in San Diego. The average mortgage payment is 30% of the metro's median income, while renting comprises around 28%. The city is in the middle of a housing crisis, and thin supply during the current cycle is one of the main drivers.

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

- From 2011 to 2015, San Diego's population grew by 5.0%, more than 2.0% above the national rate.
- The MSA expanded by 1.0% in 2015, 20 basis points in excess of the U.S. average.

San Diego vs. National Population

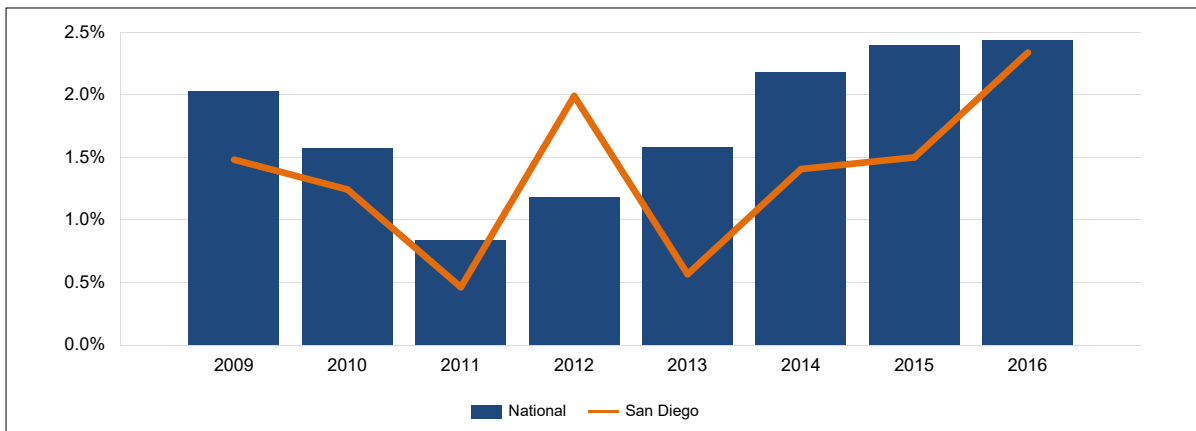
	2011	2012	2013	2014	2015
National	311,718,857	314,102,623	316,427,395	318,907,401	321,418,820
Metropolitan Statistical Area	3,142,256	3,184,358	3,223,645	3,265,700	3,299,521

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

Supply

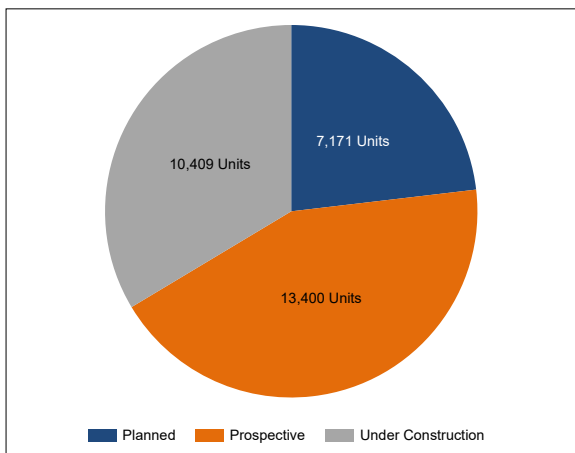
- San Diego added 4,104 units in the first 11 months of 2016, establishing a cyclical high and partially addressing the area's strong level of demand. Almost all of the properties coming online in 2016 fall at the upper end of the quality scale.
- With roughly 30,800 units in different stages of construction, San Diego is getting closer to balancing supply and demand. More than 10,000 units are currently under construction, almost half of them slated to come online in 2017.
- The pipeline is dominated by submarkets along the future extension of the Trolley Blue Line, which is opening up opportunities for transit-oriented, walkable communities and mixed-use developments. Just five submarkets—Central San Diego, Mira Mesa, University, Del Mar and Kearny Mesa—have a total of more than 8,000 units under construction.
- Mesa Nueva, UC San Diego's 1,080-unit student housing development, will be the largest project to come online in 2017. The Rey, a 484-unit luxury residential tower in Central San Diego, and Intracorp's 416-unit MARC San Marcos are also slated for completion during the next two quarters.

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



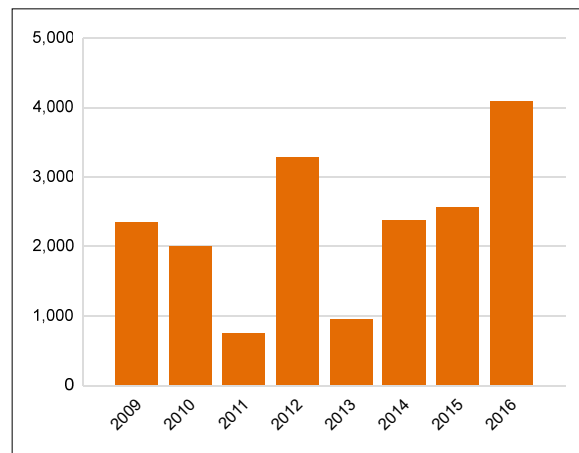
Source: YardiMatrix

Development Pipeline (as of January 2017)



Source: YardiMatrix

San Diego Completions (as of January 2017)

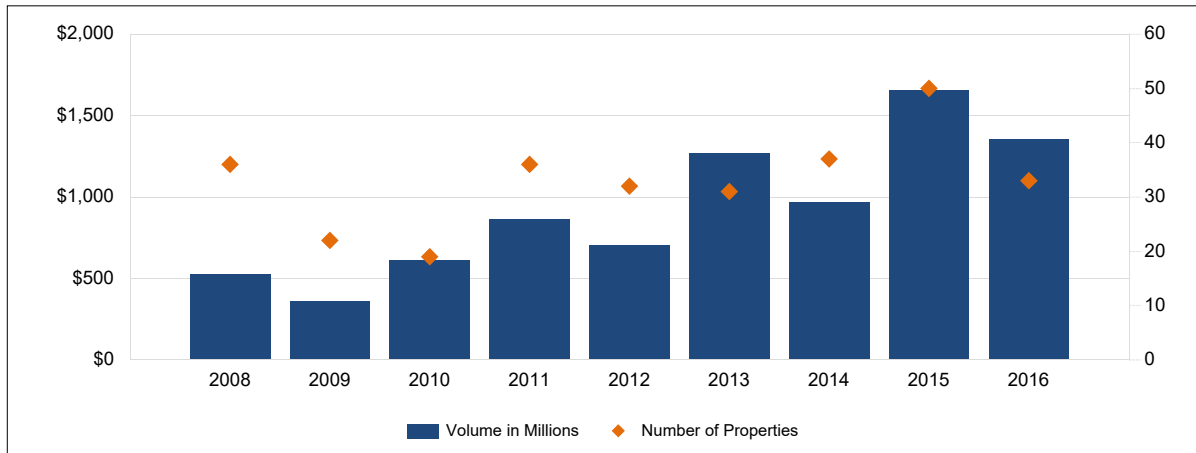


Source: YardiMatrix

Transactions

- Demand for San Diego properties continues to be strong, as more than \$1.3 billion worth of multifamily assets traded in the first 11 months of 2016. This keeps investor appetite on par with 2015, which saw \$1.6 billion worth of transactions.
- Value-add strategies are driving the San Diego market, as more than 60% of 2016's investment volume was dedicated to working-class Renter-by-Necessity assets. This tendency has been apparent throughout the cycle; since 2008, just 20% of the properties changing hands in San Diego have been luxury Lifestyle assets.
- Strong investor appetite translates into a surge in per-unit prices, which peaked at roughly \$258,000 in 2016, a 25% increase over the previous year. This average is nearly double the national average of \$134,575. The 752-unit IMT Sorrento Valley in Mira Mesa, which sold for \$214 million, was the largest transaction of the year.

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



Source: YardiMatrix

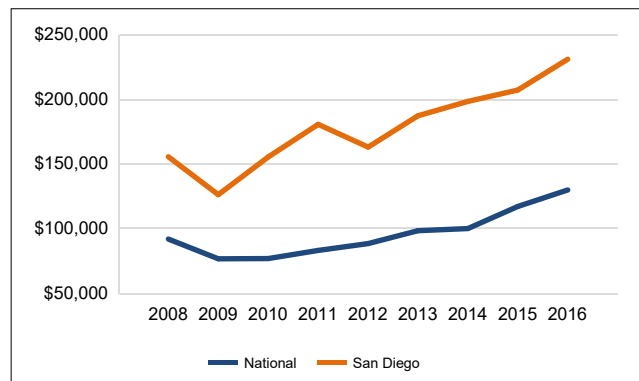
Top Submarkets for Transaction Volume¹

Submarket	Volume (\$MM)
Mira Mesa	214
La Mesa	159
Spring Valley	158
Oceanside	156
Central San Diego	114
Sweetwater	94
Peninsula	90
Mid-City	70

Source: YardiMatrix

¹ From December 2015 to November 2016

San Diego vs. National Sales Price per Unit



Source: YardiMatrix

Read All About It!



Carrier Johnson + CULTURE-Designed Tower Planned For San Diego



MG Properties Buys SD-Area Apartments for \$45M



Voit Real Estate Sells Miramar Assets for \$24M

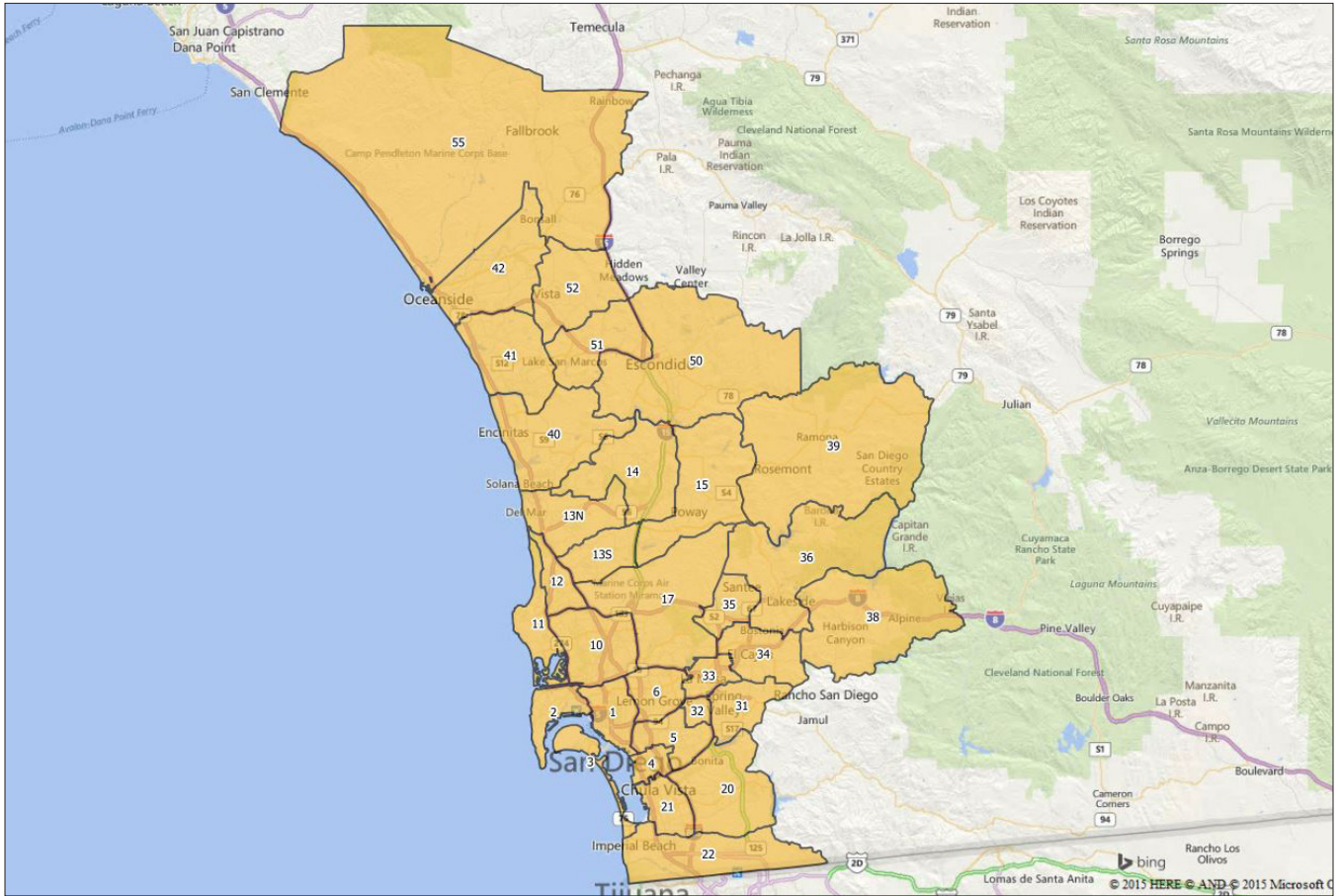


RAF Pacifica Spec Development Hits Pre-Leasing Milestone

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San Diego Submarket Map



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
22	South Bay

Area #	Submarket
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.

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