MARKET REPORT | 3Q/2018

Inland Empire Multifamily

NorthMarq

Consistently Low Vacancy, Steady Demand Pushing Rents Higher

Highlights

- The Inland Empire multifamily market continued to post steady performance in the third quarter. The market is highlighted by low vacancy and rising rents. Looking ahead, apartment construction should accelerate, although employment growth should be sufficient to absorb much of the new inventory.
- Apartment vacancy in the Inland Empire has been very steady year to date. The rate ended the third quarter at 3.2 percent, identical to the vacancy rate in both the first and second quarters of 2018. Vacancy is up 30 basis points year over year.
- Local asking rents have posted consistent gains thus far in 2018. Asking rents ended the third quarter at $1,349 per month, 3.5 percent higher than one year ago.
- After a slow first half of the year, sales of apartment buildings accelerated during the third quarter. Prices and cap rates thus far in 2018 have closely tracked levels from last year.

Inland Empire Multifamily Market Overview

Multifamily fundamentals in the Inland Empire remain healthy. Renter demand for apartments is being fueled by a healthy pace of employment growth, particularly in the region's core industries. While the pace of employment is down slightly thus far in 2018, the dip has been largely concentrated in just the construction sector, which will likely regain momentum as housing starts accelerate. Overall employment growth remains above both the national and statewide averages, and the labor market remains a driver of local apartment demand. Supply growth has been modest year to date but is forecast to pick up in the fourth quarter, and 2019 will likely be a year of more robust construction activity.

Market Indicators

	3Q/2018
Vacancy	→
Rents	↑
Transaction Activity	↑
Price Per Unit	↑
Cap Rates	↓

Summary Statistics — Inland Empire Market

Summary Statistics	Inland Empire Market
Vacancy Rate	**3.2%**
- Change from 3Q 2017 (bps)	**0**
Asking Rents (per month)	**$1,349**
- Change from 3Q 2017	**+3.5%**
Median Sales Price (per unit YTD)	**$148,700**
Average Cap Rate (YTD)	**5.0%**

Inland Empire Multifamily Market Overview (cont.)

The local investment market remains healthy, although transaction activity thus far in 2018 is lagging the heightened levels recorded from 2015-2017. There has been no drop in activity at the top end of the market or in transactions changing hands below $10 million. There have been fewer transactions trading between $10 million and $20 million, which is likely a sign of fewer value-add opportunities available on the market than in recent years. Sales velocity picked up in the third quarter, setting the stage for what is likely to be a fairly active close to the year. Cap rates have inched lower, averaging approximately 5 percent in 2018, down 25 basis points from one year earlier.

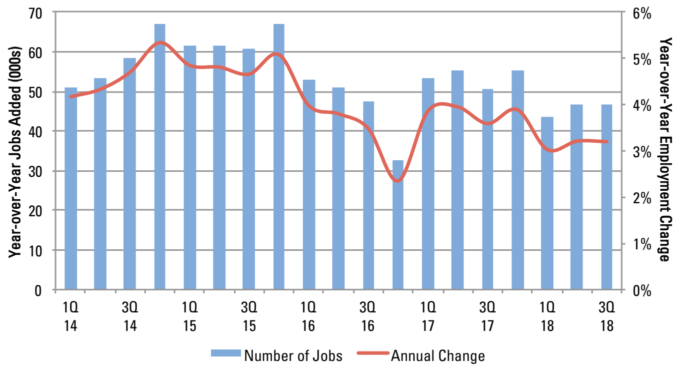
Submarket Statistics

Submarket Name	3Q 2018 Vacancy	3Q 2017 Vacancy	Annual Vacancy Change (BPS)	3Q 2018 Rents	3Q 2017 Rents
Fontana/Rialto	2.3%	2.0%	30	$1,171	$1,131
Upland	2.3%	2.4%	(10)	$1,319	$1,275
Rancho Cucamonga	2.4%	2.1%	30	$1,666	$1,607
Victorville	2.4%	2.6%	(20)	$1,030	$993
Perris	2.5%	2.4%	10	$1,259	$1,154
San Bernardino	2.5%	1.7%	80	$1,014	$984
Colton/Loma Linda	3.0%	2.9%	10	$1,423	$1,375
Indio/La Quinta/Coachella	3.1%	3.4%	(30)	$1,080	$1,043
Palm Springs/Palm Desert	3.1%	3.0%	10	$1,057	$1,034
University City/Moreno Valley	3.2%	2.3%	90	$1,374	$1,333
Hemet	3.4%	3.0%	40	$1,141	$1,053
North Ontario	3.6%	3.5%	10	$1,474	$1,435
Riverside/North Magnolia	3.7%	3.8%	(10)	$1,257	$1,219
South Ontario/Chino	4.3%	4.4%	(10)	$1,701	$1,635
Riverside County/Corona	4.8%	3.6%	120	$1,543	$1,510
SW Riverside County	5.0%	4.3%	70	$1,457	$1,402

Employment

- The Inland Empire continued to add workers in the third quarter. Year over year, local employment has expanded by 3.2 percent, with the addition of 46,800 jobs. While the current pace of payroll expansion is among the top markets in the country, the pace of growth was somewhat stronger last year at this time.
- The construction sector is recording more modest growth following a steep upward climb in recent years. From 2013-2017, construction employment expanded at a pace of approximately 9 percent per year as the sector grew by nearly 35,000 employees. In the 12-month period ending in the third quarter, construction employment had expanded by just 0.9 percent, with the addition of 900 jobs.
- One sector where the economy continues to expand is in trade, transportation and warehousing, which has grown by more than 4 percent in the past year with the addition of 8,000 net new jobs.
- **Forecast:** After a gain of more than 55,000 jobs in 2017, employment growth in the Inland Empire is on pace to slow to approximately 45,000 new workers this year, a 3 percent gain.

Employment Overview



Sources: NorthMarq, Bureau of Labor Statistics

The current pace of payroll expansion is among the top markets in the country

Vacancy

- After gradually inching higher for most of 2017, apartment vacancy in the Inland Empire has been very steady year to date. The rate ended the third quarter at 3.2 percent, identical to the vacancy rate in both the first and second quarters of 2018.
- The multifamily vacancy rate is up 30 basis points from one year ago, even as construction of new units has slowed. Despite rising a bit during the past 12 months, the local vacancy rate has been consistently low; vacancy in the Inland Empire has not topped 3.5 percent in nearly five years.
- At just 2.4 percent, the Rancho Cucamonga submarket has one of the lowest vacancy rates in the Inland Empire. Supply-side pressures could push the vacancy rate higher in the coming years, with projects totaling nearly 1,200 units scheduled to come online during the next 24 months.
- **Forecast:** Vacancy is forecast to hold steady at 3.2 percent in the fourth quarter. This would represent a decline of 10 basis points from the year-end 2017 rate.

Vacancy Trends

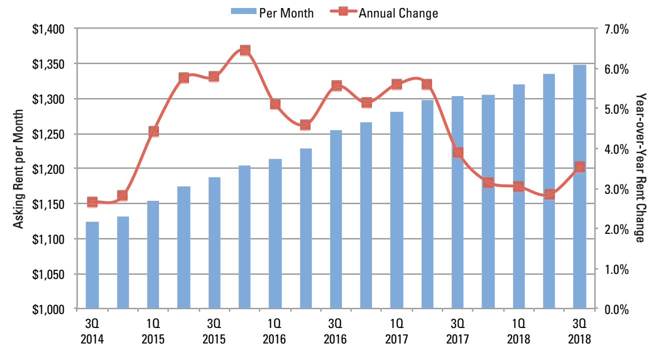
Sources: NorthMarq, Reis

Vacancy in the Inland Empire has not topped 3.5 percent in nearly five years

Rents

- After slowing late last year, rents in the Inland Empire have been on a steady upward climb in 2018. Asking rents ended the third quarter at $1,349 per month, 3.5 percent higher than one year ago.
- Class A asking rents have increased by 3 percent in the past year, with some of the strongest growth in the past two quarters. Average asking rents in Class A properties were $1,578 per month in the third quarter.
- Rents in the Rancho Cucamonga submarket are among the highest in the Inland Empire. Asking rents in the submarket were $1,666 per month as of the third quarter, up 3.7 percent from one year earlier.
- **Forecast:** Rent growth should remain on an upward trajectory, with asking rents ending 2018 at $1,365 per month, 4.5 percent higher than at the end of last year.

Rent Trends



Sources: NorthMarq, Reis

Rents in the Inland Empire have been on a steady upward climb in 2018

Development and Permitting

- The pace of deliveries has slowed considerably in the Inland Empire thus far in 2018. Year to date, projects totaling fewer than 200 units have come online. Last year, more than 1,200 apartment units were delivered.
- Development is on pace to gain momentum after a lull during much of 2018. Projects totaling approximately 3,500 units are currently under construction, with the bulk of these projects expected to be completed in 2019.
- After permits for more than 1,100 multifamily units were issued in the second quarter, activity slowed in the third quarter, with only about 700 multifamily permits pulled. Year to date, approximately 2,400 multifamily permits have been issued, down approximately 2 percent from the levels recorded in the same period in 2017.
- **Forecast:** Construction is expected to accelerate in the fourth quarter, and the completions for 2018 will total nearly 1,300 units. Development will likely also pick up in 2019.

Development Trends

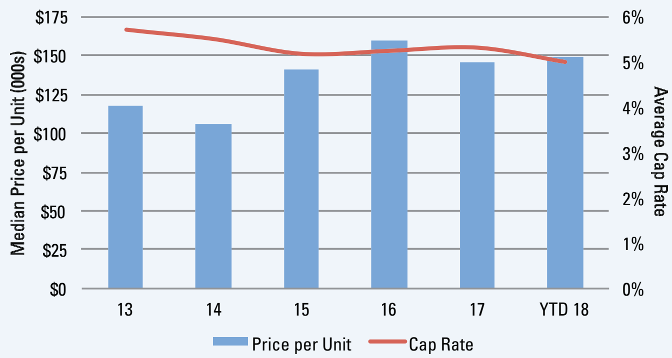
Sources: NorthMarq, Reis

Development is on pace to gain momentum after a lull during much of 2018

Multifamily Sales

- Sales velocity accelerated during the third quarter, posting a 25 percent increase over second quarter's number of transactions. Thus far in 2018, investment activity is lagging levels from previous periods; the number of properties sold year to date is down approximately 30 percent from the same period in 2017.
- The median price rose during the third quarter, reaching nearly $155,000 per unit. In transactions closed year to date, the median price is $148,700 per unit, about 3 percent higher than in 2017.
- Cap rates have been very consistent throughout this year, averaging approximately 5 percent in 2018 and also in the third quarter. Cap rates averaged approximately 5.25 percent in 2017.

Investment Trends



Sources: NorthMarq, CoStar

Cap rates have been very consistent throughout this year

Recent Transactions in the Market

MULTIFAMILY SALES ACTIVITY

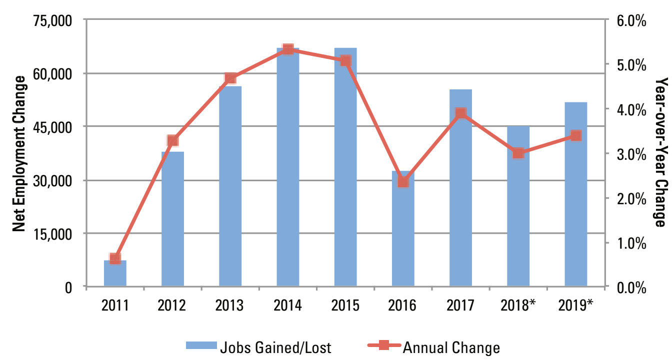
Property Name	Street Address	Units	Sales Price	Price/Unit
Foothill Ridge	1334 W Foothill Blvd., Upland	232	$48,250,000	$207,974
Dakota	34875 Pourroy Rd., Winchester	174	$42,000,000	$241,379
Laurel Heights	8655 Arlington Ave., Riverside	176	$27,250,000	$154,830
ReNew Riverside	6195 Pegasus Dr., Riverside	128	$22,100,000	$172,656
ReNew Diamond Valley	1025 S Gilbert St., Hemet	137	$15,050,000	$109,854
Montara	1900 Dill Rd., Barstow	158	$10,000,000	$63,291

Looking Ahead

The multifamily market in the Inland Empire is expected to remain healthy in the coming quarters, although an increase in new construction could push the vacancy rate a bit higher. While there are construction projects located throughout the market, more new units are slated to be delivered in San Bernardino County, with projects in Ontario and Chino Hills coming online during the next 12 months. Over the longer-term, the redevelopment of the Empire Lakes golf course is slated to bring approximately 650 new apartments to Rancho Cucamonga in the coming years. In Riverside County, the bulk of the construction will be delivered in the city of Riverside, where there are more than 1,000 apartments currently under construction. As these projects are completed, the inventory in the University City/Moreno Valley submarket could increase by more than 5 percent, potentially causing a short-term rise in the local vacancy rate.

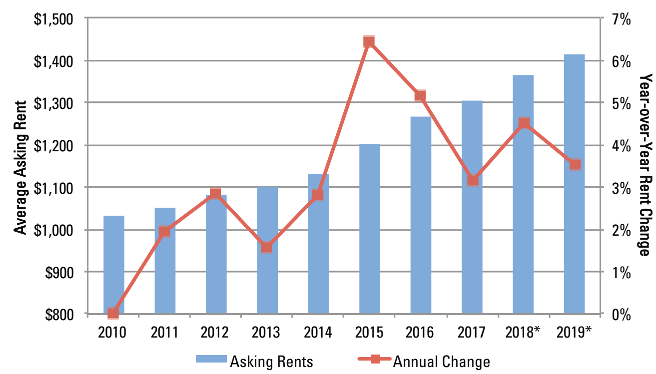
With the local economy continuing to expand, investment conditions are expected to remain strong in the coming quarters. The pace of employment growth has slowed, but that is due almost entirely to a more sustainable rate of expansion in the construction sector, while the core warehousing/distribution industry continues to grow at a robust pace. More than 20 million square feet of industrial space is currently under construction. As these projects are delivered and secure tenants, thousands of new jobs will be added to the sector. This continued growth in a core sector of the local economy should strengthen investor sentiment for rental properties in the Inland Empire.

Employee Forecast



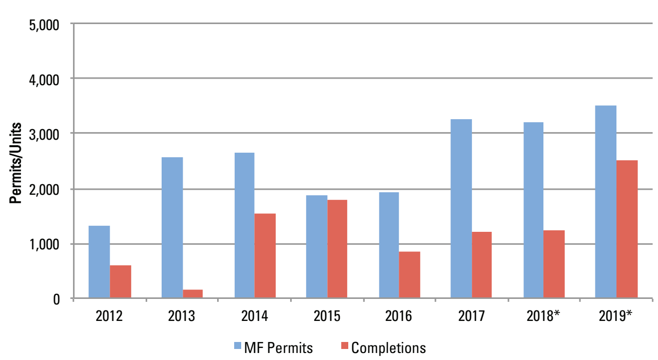
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



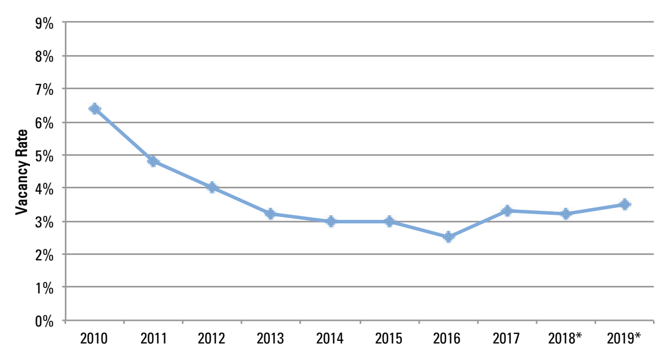
* Year End Forecast
Sources: NorthMarq, Reis

Construction & Permitting Forecast



* Year End Forecast
Sources: NorthMarq, Census Bureau, Reis

Vacancy Forecast



* Year End Forecast
Sources: NorthMarq, Reis

About NorthMarq Multifamily

NorthMarq Multifamily has a market-leading position in multifamily property sales in markets across the U.S., offering commercial real estate investors a personalized approach to buying and selling multifamily and manufactured housing properties. These teams collaborate with NorthMarq Capital's debt and equity experts nationwide to provide a full range of capital markets services, developing innovative solutions for real estate investments.

NorthMarq Capital, the largest privately held commercial real estate financial intermediary in the U.S., provides debt, equity and commercial loan servicing through over 300 mortgage banking professionals in regional offices coast-to-coast and services a loan portfolio of more than $53 billion. For more information, please visit www.northmarq.com.

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