



KEYSER MARSTON ASSOCIATES™
ADVISORS IN PUBLIC/PRIVATE REAL ESTATE DEVELOPMENT

MEMORANDUM

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To: Lucia Hughes, City of Fremont
From: Keyser Marston Associates, Inc.
Date: October 6, 2020
Subject: Update on Residential Market Trends During Pandemic

Keyser Marston Associates, Inc. (KMA) prepared the following two studies to support updates to the City's Affordable Housing Ordinance:

- Affordable Housing Nexus Analysis ("Nexus Analysis") and
- Financial Feasibility Analysis ("Feasibility Analysis").

The market rents and sales prices for new residential developments in Fremont are an important input for both studies. As the studies were prepared prior to the coronavirus pandemic, they reflect pre-pandemic market conditions. This memorandum provides an update on residential market trends since the pandemic began and evaluates whether the rent and sales price estimates incorporated into the studies still hold.

Conclusion

Based on the market data summarized in this memorandum, the home price and rent estimates used in the Nexus Analysis and Feasibility Analysis continue to reflect the near-term development economics of residential development projects in Fremont and remain valid estimates for purposes of the two studies.

- Home price estimates used in the studies are consistent with current sale and listing prices for new homes in Fremont.
- Rent estimates remain appropriate for purposes of the studies. Rents have decreased during the pandemic to a level that would not support development feasibility if reduced rents were to hold longer term based on sensitivity testing of the apartment pro forma model presented in the Feasibility Analysis. However, apartment projects continue to advance entitlement applications, suggesting

developer optimism that declines in rent are temporary in nature and will reverse as the pandemic subsides and the work-from-anywhere flexibility provided by many employers begins to phase out. Pre-pandemic rents are likely a better reflection of medium to longer-term market conditions and underwriting assumptions being used by developers with apartment projects in the pipeline than asking rents during the pandemic.

Notwithstanding the conclusion that the rent and sales price estimates remain valid for purposes of the studies, the pandemic obviously adds an additional element of uncertainty and conditions will continue to evolve.

Analysis

To help understand the near-term effects of the pandemic on home prices and apartment rents in Fremont, KMA reviewed local market data for the second and third quarters of 2020. The market data indicates that the local for-sale housing market has been resilient during the pandemic with home prices remaining stable or even increasing in certain cases. The rental market has weakened during the pandemic, particularly for newly built, Class A projects. Developers of rental projects are still moving forward with entitlement applications, suggesting optimism that rents will return to feasible levels in the near term.

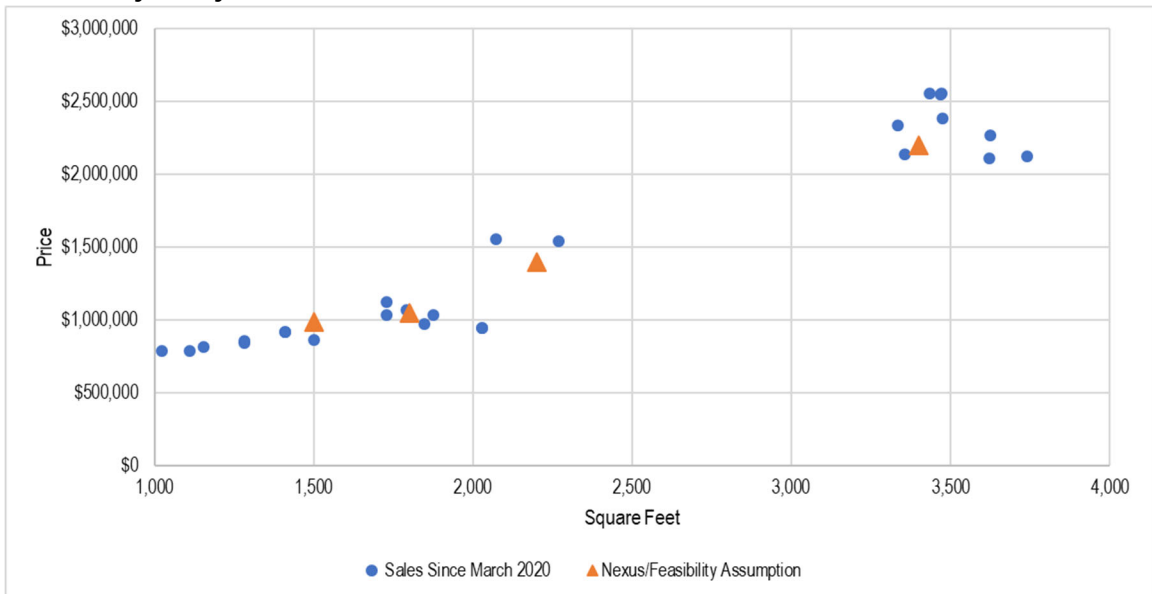
For-Sale Market Conditions as of Q3 2020

- *Existing home prices trending higher* – In August 2020, the median price of existing single-family detached homes sold in Alameda County was approximately 14% greater than the prior year, while the median price of existing condos and townhomes was approximately 5% greater than the prior year, according to data from the California Association of Realtors. The resilience of for-sale home prices during the pandemic is potentially explained in part by the limited supply of homes on the market, strong demand from households relocating from elsewhere in the Bay Area, and historically low interest rates.
- *Prices of newly built homes support Nexus Analysis and Feasibility Analysis estimates* – The per square foot pricing of newly built homes in Fremont estimated in the Nexus Analysis and Feasibility Analysis is consistent with the prices of new homes that have been sold since the pandemic began. As shown in Figure 1, the Nexus Analysis and Feasibility Analysis estimates generally fall within the price range of homes built since 2019 and sold since March 2020. Some variation between KMA's estimates and actual sales is expected given the limited number of recorded sales.

- *Listing prices for new condos are stable* – While some real estate professionals have speculated that the pandemic could adversely impact the market appeal of higher density condo development, listing prices for new condo projects in Fremont, including Theory at Innovation and Metro Crossing, have not changed significantly since the pandemic began. Recorded sales suggest that new condos are generally being sold at or near their listing price.

In conclusion, the home price estimates incorporated into the Nexus Analysis and Feasibility Analysis remain valid and consistent with current sale and listing prices of for-sale projects in Fremont.

Figure 1. Prices of New Homes Sold in Fremont Since March 2020 vs. Nexus and Feasibility Analysis Estimates



Source: Redfin

Rental Market Conditions as of Q3 2020

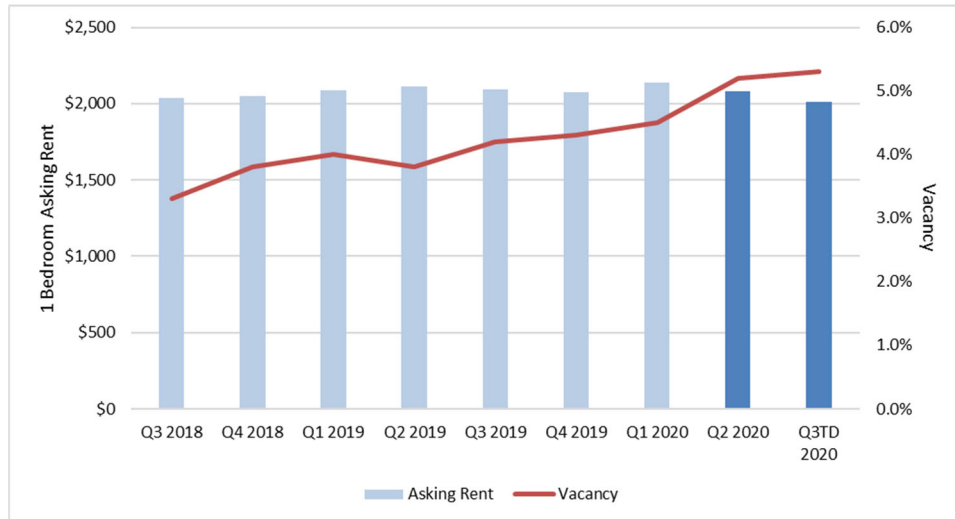
- *Apartment rents have declined during the pandemic* – The average asking rent for a one-bedroom apartment unit in Fremont has decreased by 4% from one year ago, according to Costar (see Figure 2). The apartment vacancy rate is also trending higher. Newer apartment buildings with premium amenities have been the most adversely impacted by the pandemic. The average asking rent for a one-bedroom unit at Artist Walk, completed in 2018, is down by approximately 10% versus the prior year. Two apartment projects built in 2020, Aya and the Asher, are leasing up during the pandemic. Both projects are offering up to two

months of free rent and a potential leasing bonus of \$1,000 to \$2,000 for new tenants. These concessions are more generous than what new apartment projects typically offered prior to the pandemic.

- *Nexus Analysis and Feasibility Analysis rent estimates exceed current rents in newer buildings* – The average effective rents (net of concessions) at Artist Walk, Aya and the Asher currently range from \$3.15 to \$3.25 per square foot, compared to the Nexus Analysis and Feasibility Analysis apartment rent estimates based on pre-pandemic market data of \$3.44 to \$3.60 per square foot. If these pandemic-affected rents were assumed to hold over a longer time horizon, as opposed to representing a temporary market condition, apartment development would be estimated as infeasible based on sensitivity testing of the apartment pro forma model presented in the Feasibility Analysis, holding constant all other pro forma inputs such as development costs and return requirements.
- *Entitlement activity remains strong* – Despite weaker apartment rents, City staff report that multifamily projects proposed before the pandemic continue to advance entitlement applications, suggesting optimism that apartment rents will return to feasible levels reflected in the Nexus Analysis and Feasibility Analysis.

The current underperformance of the rental housing market is likely not representative of what the post-pandemic rental market might look like. Multifamily projects that proceed with development in the near term will likely do so based on the expectation that rents will recover to feasible levels that meet the return requirements of developers and investors. The Nexus Analysis and Feasibility Analysis apartment rent estimates, which capture pre-pandemic market conditions, provide a reasonable baseline for the rents targeted by multifamily projects intending to proceed with development in the near term.

Figure 2. One-Bedroom Asking Rent and Vacancy of Fremont Apartment Buildings Completed Before 2020



Source: Costar

Even without a pandemic, real estate development economics are fluid and are impacted by constantly changing conditions with regard to rent potential and sale prices, construction costs, land costs, and costs of financing. The pandemic adds additional uncertainty and it is possible that its economic fallout will produce longer-term impacts on Fremont’s housing market that are not yet apparent from two quarters of market data. As always, it will be important to monitor the health of the housing market over time to help ensure the City’s affordable housing policies remain effective and responsive to local market conditions.