Reports show rental cooloff for Silicon Valley

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Multifamily housing is in high demand in Silicon Valley, but a new real estate forecast by Allen Matkins and the UCLA Anderson School of Management shows that developers' desire to build new units may be waning.

The recently released report shows that for the first time since Allen Matkins and UCLA began tracking multifamily market optimism among developers four years ago, respondents were less confident they could fill new units or get higher rents for those apartments in the coming years.

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That was a surprise to John Tipton, a partner in the real estate department at Allen Matkins.

"Multifamily, like industrial, had pretty much just been positive, positive, positive," he said. "Literally all of a sudden in this survey there was a pretty big shift."

The survey responses that helped shape the report show that more than 50 percent participants don't plan to build new apartment buildings in the coming year. That's up from 2015, when only 39 percent said they wouldn't start a new apartment project in 2016.

So, has the multifamily market in the valley topped out? That's not a simple yes or no answer, Tipton said.

"There was real demand for [luxury housing] and demand seems to be met," he said. "But clearly, there does remain some demand for lower price point housing."

In 2016 alone, more than 11,260 units wrapped up construction in the Bay Area – more than double the region's 15-year average of about 5,250 units annually, according to a recent report by Richardson, Texas-based RealPage, Inc.

Apartment owners throughout the Bay Area are starting to offer new deals to attract new tenants, like a free month – or sometimes more – of rent for signing a lease in a more competitive market.

In the coming year, property owners may also start to forego or reduce the large annual rent hikes that became standard practice between 2013 and 2015, said Ron Granville, CEO at Belmont-based Woodmont Real Estate Services.

That estimate matches up with RealPage data that shows that in 2016, rents in some parts of the Bay Area were down slightly from the year before. In San Jose, for instance, rents trended downward by around 1 percent last year – a significant change from 2015, when rents grew by 6.7 percent, according to the data.

But these trends are not a cause for panic, Granville says.

“Certainly a building coming to market right now is renting up in a more competitive market than those that came to market 18 months ago,” he said. “But from a developer standpoint, we are still seeing very good rents.”

And while there may be some trickle-down effects from the Class A cool down to Class B and C apartment rent rates, the market is still strong, RealPage notes in a Feb. 1 report when it says: “The recent pullback seems more like an overreaction from apartment operators than a structural shift in the market. Operators have been able to push rents so hard for so long that, as the economy has normalized as anticipated, they slammed on the brakes. The structural underpinnings of the Bay Area remain healthy and intact.”

The Allen Matkins/UCLA survey agrees, adding that this may be an opportunity for developers to dive into the lower-cost apartment market, where demand is still strong.

The barriers to doing that – like high land prices and construction costs – may have builders waiting a year or so before digging in, but Tipton predicts that shift will come.

“Typically speaking, entrepreneurs will follow where there are returns to be had,” he said. “Most likely they will not decide to do nothing.”