

## **South Bay Apartment Market Update by Hendricks & Partners**

While its extent of decline was considerable, and a return to health is still distant, several key indicators show the South Bay rental market has turned the corner to recovery. Crippling job losses stemming from the Tech Crash that trimmed area payrolls by over 200,000 positions have ended, as evidenced by the 6,700 jobs added over the most recent 12 months. Santa Clara County reported the second largest increase in the total value of non-residential construction activity among California's 28 metro areas through the first half of 2005. Commercial and residential activity combined reached a four-year high for the area and a 50% increase over last year.

For the first time since 2001, the local average rental rate showed growth in comparison to its year-ago value in the second quarter.

In a further sign of optimism for the area's economy, the most recent Business Confidence Survey indicates roughly 34% of local surveyed executives plan hiring in the next six months, while an improved 15% indicate they expect layoffs. Though Palo Alto tech giant Hewlett Packard announced plans in July to layoff 14,500 people worldwide (some of which could occur locally), weakness appears limited to this sector, with South Bay's overall employment figures likely to see continued, gradual improvement in the months ahead.

- Aided by an improved economic environment, year-to-date apartment demand – measuring 860 units as of the second quarter – stands nearly 20% ahead of last year.
- New construction brought a total of 465 rental units online in the second quarter, roughly split between a property in San Mateo and a property in the N/NE Valley. An examination of projects slated for completion over the rest of the year shows a moderate 800 or so units coming online, a level likely to delay substantial improvement to vacancy over the near term.
- Multifamily construction permits (apartments and condominiums) were issued for a sizable 1,182 multifamily units in the second quarter. Year-to-date volume stands at more than 1,900 units, already closing in on last year's annual total of 2,260 units.
- Improved demand reeled in the South Bay's overall average apartment vacancy rate from 5.4% in the second quarter of 2004 to 5.0% this year, its lowest level since third quarter 2002.
- Perhaps the quarter's most notable news emerged within rental rates. After shedding roughly 25% of their value in recent years, rental rates have regained forward momentum. The South Bay's overall average rent rose a miniscule but nonetheless positive 9.5% over the year ended in June, its first year-over-year gain in nearly four years. Twelve months earlier, rents contracted an average of 2.8%.

Representing perhaps the largest corporate campus project in Palo Alto for roughly a decade, software maker VMware, Incorporated has announced plans to build a 1,400 employee corporate headquarters in the city. The site, which will house 460,000 square feet of office space, lies along Hillview Avenue near Foothill Expressway in south Palo Alto. Already partway through the approval process, groundbreaking at the site could take place later this year. While the project's immediate effect on the local high-tech sector remains unknown, the project foretells recovery within Palo Alto's commercial real estate market, which is often viewed as a bellwether for other South Bay markets.

*Reprinted with permission of Hendricks & Partners, the nation's largest apartment sales and research firm. Second Quarter 2005. For more information, please call (510) 444-2787 or visit [www.hendrickspartners.com](http://www.hendrickspartners.com).*

