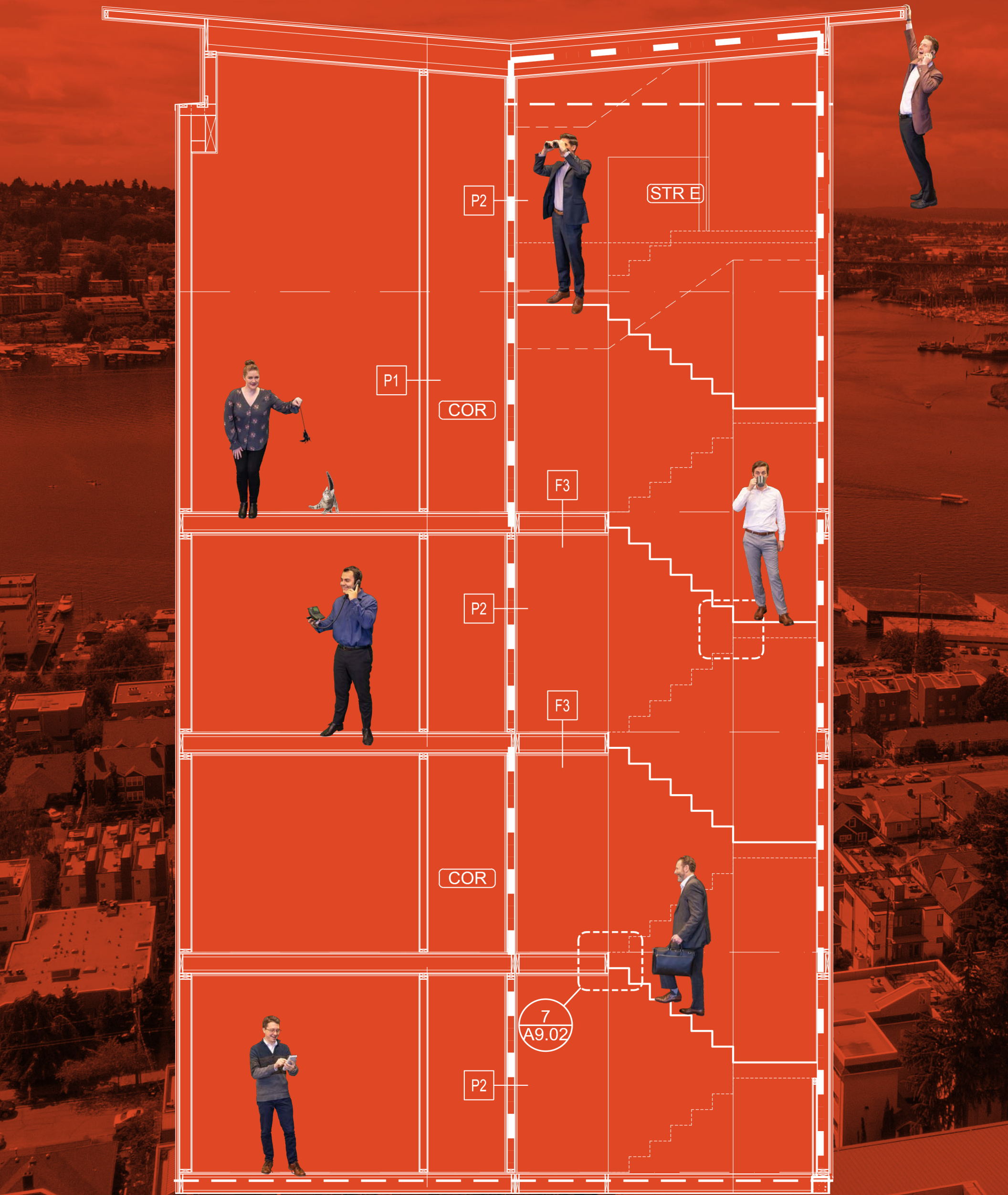


MICROHOUSING MARKET STUDY

November 2019 Special Report



A MACRO LOOK AT MICROHOUSING

Microhousing is by definition the smallest form of housing that developers can build in Seattle (see definitions below). Microhousing frequently tests building code limits, making this housing type challenging to develop for architects, developers, and building officials alike. Unsurprisingly, the regulatory environment for microhousing is always in flux to some degree. Over the past year, a number of policy changes altered both the letter of the code and how building officials interpret it.

1. AFFORDABILITY REZONE LIMITS MOST AFFORDABLE UNITS

In October 2014, Seattle changed the zoning code for congregate housing, severely reducing the inventory of land where congregate development was permittable. In March 2019, new citywide Multifamily Housing Affordability legislation rezoned most of that land so that congregate housing is either no longer permitted or is unlikely to be economically feasible. We believe new congregate housing development will become exceedingly rare.

2. TAX EXEMPTION FEASIBLE FOR SEDUS IN CERTAIN NEIGHBORHOODS

The Multifamily Tax Exemption (MFTE) program was changed in September 2019 to raise the maximum rent for SEDUs from 40% to 50% of Area Median Income, which took effect on 10/24/2019. This rate is only available to projects where SEDUs are the only unit type in the building. Rates for congregate housing remain unchanged.

3. INCREASE IN BICYCLE PARKING REQUIREMENTS

Bicycle parking requirements were raised in 2018 to one bicycle space per unit. The code now requires that bicycle parking be accessible without the use of stairs. This poses major challenges for projects without elevator service. A new director’s rule is expected by the end of the year adding new access requirements and minimum dimensions.

4. NEW INTERPRETATION OF STORAGE REQUIREMENTS

In 2019, building officials made subtle alterations to how they interpret the rules for SEDU storage requirements, introducing new restrictions on the dimensions of closets and additional storage. This will not restrict unit sizes, but it hinders unit layout flexibility and livability.

5. INCREASED SEPA THRESHOLD SPEEDS UP PERMIT PROCESS

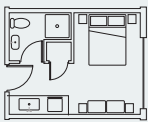
New legislation passed in October 2019 raised SEPA threshold to 200 units in all Urban Villages that have not exceeded their 2035 growth targets. Raising the SEPA threshold will speed up the permit process, remove requirements for historic review and traffic studies, and reduce overall entitlement timeline risks.



THIS LEGISLATIVE AND ZONING UPDATE WAS COMPILED
IN COLLABORATION WITH NEIMAN TABER ARCHITECTS

MICROHOUSING DEFINITIONS

CONGREGATE

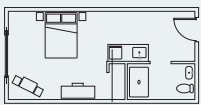


Std 140 - 200 SF
Avg 175 SF
Min 70 SF

A type of housing that has a private sleeping room and typically a bathroom, but is not a complete dwelling unit and may share a bathroom, common kitchen, dining room, and facilities with other units.

Allowed in
Certain Zones

MICRO

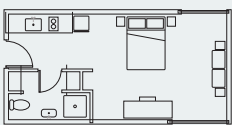


Std 150 - 250 SF
Avg 200 SF
Min 90 SF

An apartment or townhouse dwelling unit consisting of no more than eight sleeping suites (private room with private bath) and one common kitchen or kitchen/lounge.

Not Allowed
(Since 2014)

SEDU

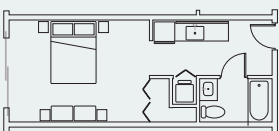


Std 240 - 320 SF
Avg 275 SF
Min 240 SF*

A very compact conventional studio apartment, complete with cooking and bathing facilities and closet space. The max gross floor area allowed is 320 SF – anything larger is an Efficiency Dwelling Unit (EDU).

Allowed

EDU



Std 321 - 400 SF
Avg 375 SF
Min 321 SF

A small conventional studio apartment with a main living space (“habitable space”) of no less than 220 SF.

Allowed

*THERE IS NO MINIMUM SEDU SIZE, JUST MINIMUM LIVING SPACE, WHICH IS 120 SF, YIELDING A 240 SF UNIT.

SEATTLE MARKET FUNDAMENTALS

2019 was the year of the micro, boasting seven micro apartment building sales and no SEDU sales. The premium location of the 2019 sales generated aggressive competition, pushing price per unit 15% higher than the three micro sales that occurred before 2019. However, cap rates for micros were stagnant at 5.2% on average, which is a 0.80% premium compared to market-rate apartment cap rates. We forecast strong cap rate compression once micros prove they can weather a recession. Until then, shrewd investors will be rewarded for their foresight in purchasing these rare investments.

*ALL MICRO BUILDINGS SOLD IN 2019 PARTICIPATED IN THE MULTIFAMILY TAX EXEMPTION PROGRAM (MFTE), WHICH ARTIFICIALLY INFLATES GOING-IN CAP RATES RELATIVE TO PROPERTIES THAT DO NOT PARTICIPATE IN THE PROGRAM. WE ESTIMATE THE AVERAGE EFFECT ON GOING-IN CAP RATES AT ABOUT 0.30%, MEANING THAT THE TRUE AVERAGE CAP RATE FOR MICROS IS ABOUT 4.9% AFTER ADJUSTING FOR THE PROPERTY VALUE ATTRIBUTABLE SOLELY TO PARTICIPATION IN THE MFTE PROGRAM.

MICROS

\$1,051	\$5.22	4.0%	\$145K	\$710	5.2%
AVG RENT	AVG RENT/SF	AVG VACANCY	AVG SALES PRICE/UNIT	AVG SALES PRICE/NRSF	CAP RATE

SEDUS

\$1,319	\$4.85	6.0%	\$205K	\$758	4.7%
AVG RENT	AVG RENT/SF	AVG VACANCY	AVG SALES PRICE/UNIT	AVG SALES PRICE/NRSF	CAP RATE

MARKET-RATE APARTMENTS

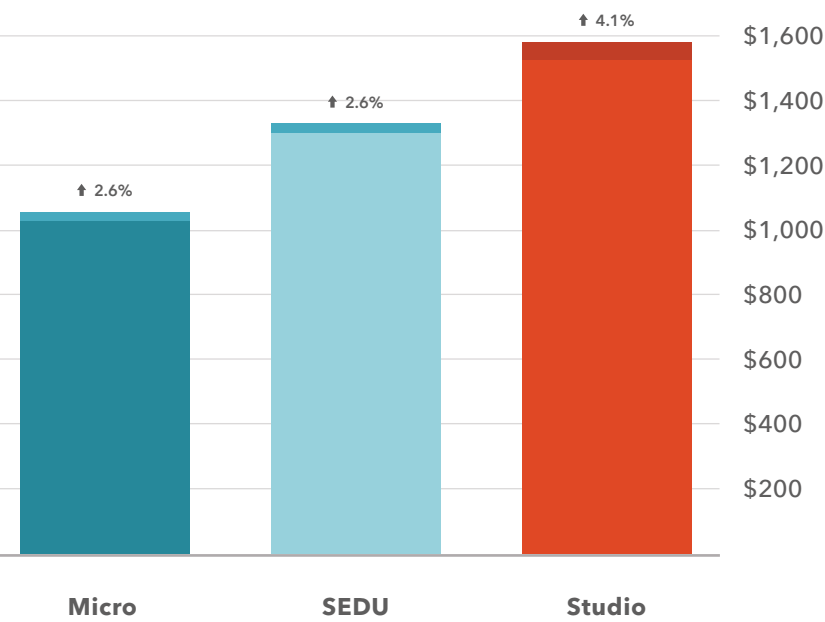
\$1,584	\$3.72	8.0%	\$434K	\$547	4.4%
AVG STUDIO RENT	AVG STUDIO RENT/SF	AVG STUDIO VACANCY	AVG SALES PRICE/UNIT	AVG SALES PRICE/NRSF	CAP RATE

RENT & VACANCY

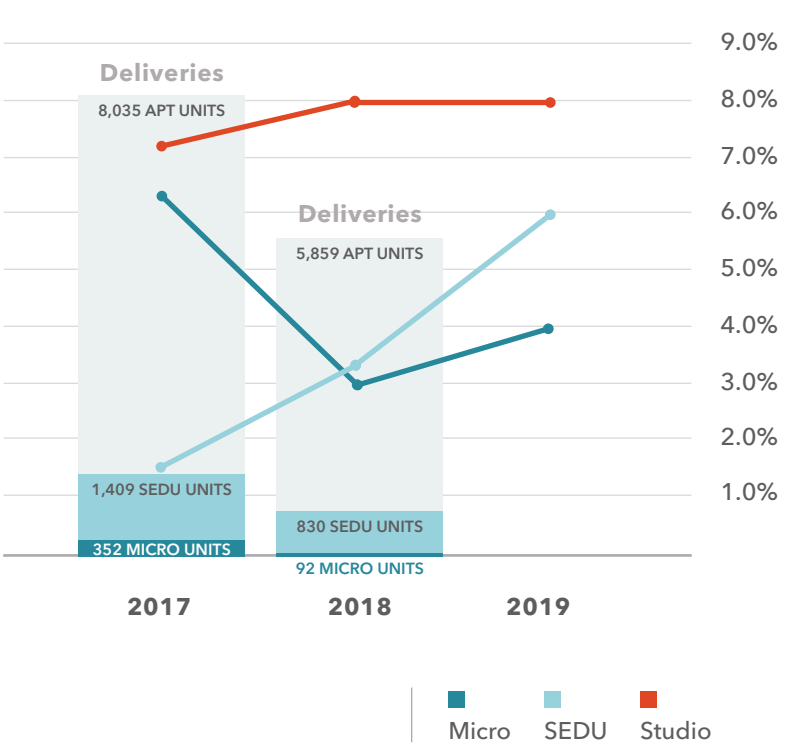
Rent growth in new market-rate studios outpaced micros and SEDUs for the first time in three years. We presume the leading cause for slowed growth in microhousing is an oversupply of small units near future light rail stations, causing a short-term imbalance in the supply and demand around these transit hubs. In 2020, we will be watching how the compressed delta between SEDU and studio rents impacts SEDU absorption. In the near term, we expect smaller, more affordable units will experience stronger rent growth and lower vacancy than larger SEDUs with asking rents over \$1,350.

MICRO		
\$1,051	\$5.22	4.0%
AVG RENT/UNIT	AVG RENT/SF	AVG VACANCY
SEDU		
\$1,319	\$4.85	6.0%
AVG RENT/UNIT	AVG RENT/SF	AVG VACANCY

RENT



VACANCY



	Rent / Unit			Rent / SF			Vacancy		
	2017	2018	2019	2017	2018	2019	2017	2018	2019
MICRO*	\$998	\$1,024	\$1,051	\$5.38	\$4.91	\$5.22	6.4%	3.0%	4.0%
SEDU*	\$1,275	\$1,286	\$1,319	\$4.80	\$4.83	\$4.85	1.5%	3.3%	6.0%
STUDIO†	\$1,523	\$1,521	\$1,584	\$3.86	\$3.85	\$3.72	7.2%	8.0%	8.0%

*DATA SOURCE: ASKING RENTS AND SURVEYED VACANCY
†DATA SOURCE: COSTAR - ASKING RENT, STUDIOS BUILT 2010+; COSTAR - Q2 GROSS VACANCY, STUDIOS BUILT 2010+
NOTE: VACANCY IMPACTED BY PROPERTIES IN LEASE-UP.

AVERAGE RENT BY NEIGHBORHOOD

NORTH SEATTLE

MICRO	\$1,035	\$4.77/SF
SEDU	\$1,084	\$3.60/SF

496

BALLARD

MICRO	\$1,000	\$5.53/SF
SEDU	\$1,283	\$4.66/SF

491

GREEN LAKE, FREMONT, WALLINGFORD

MICRO	\$968	\$4.47/SF
SEDU	\$1,265	\$5.17/SF

293

EASTLAKE

MICRO	\$1,218	\$5.25/SF
SEDU	\$1,432	\$5.20/SF

263

QUEEN ANNE, BELLTOWN, SOUTH LAKE UNION

MICRO	\$1,090	\$5.96/SF
SEDU	\$1,416	\$4.78/SF

205

DOWNTOWN, FIRST HILL, YESLER

MICRO	\$1,033	\$5.36/SF
SEDU	\$1,477	\$5.32/SF

457

WEST SEATTLE

MICRO	\$966	\$5.04/SF
SEDU	\$1,352	\$4.77/SF

388

ROOSEVELT, RAVENNA

MICRO	\$1,181	\$5.83/SF
SEDU	\$1,234	\$4.96/SF

815

UNIVERSITY DISTRICT

MICRO	\$984	\$5.10/SF
SEDU	\$1,259	\$4.51/SF

1,301

CAPITOL HILL

MICRO	\$1,049	\$5.40/SF
SEDU	\$1,366	\$4.86/SF

1,388

EASTSIDE

MICRO	\$1,045	\$4.46/SF
SEDU	-	-

482

CENTRAL DISTRICT

MICRO	\$1,042	\$5.42/SF
SEDU	\$1,338	\$5.51/SF

459

BEACON HILL, RAINIER VALLEY

MICRO	-	-
SEDU	\$1,228	\$4.36/SF

209

Total existing stock of microhousing units by neighborhood

#

SALES & DEVELOPMENT

SALES

MICROS

	Property Name	Address	Year Built	Units	Avg Unit Size (SF)	Price	Sale Date	\$/Unit	\$/NRSF	Cap Rate	NOI/NRSF
1	Footprint Phinney	8727 Phinney Ave N	2014	79	152	\$10,550,000	6/28/19	\$133,544	\$877	5.2%	\$45.60
2	Footprint Greenwood	143 N 85th St	2014	38	235	\$5,300,000	6/28/19	\$139,474	\$593	5.2%	\$30.82
3	Footprint Wallingford	4516 Meridian Ave N	2013	40	274	\$7,150,000	6/21/19	\$178,750	\$651	5.4%	\$35.18
4	Footprint Madison	1806 23rd Ave	2013	61	172	\$7,900,000	2/28/19	\$129,508	\$754	5.2%	\$39.19
5	Footprint Eastlake	2371 Franklin Ave E	2013	35	185	\$4,700,000	1/24/19	\$134,286	\$725	4.8%	\$34.80
6	Footprint Cal Park	1806 12th Ave	2014	78	274	\$14,500,000	1/24/19	\$185,897	\$679	5.2%	\$35.33
7	Footprint Capitol Hill	422 11th Ave E	2013	54	209	\$9,200,000	1/24/19	\$170,370	\$817	4.9%	\$40.01
8	Emerald 10	315 10th Ave	2012	36	176	\$5,000,000	6/27/17	\$138,889	\$790	5.2%	\$41.09
9	Footprint Delridge	4546-4548 Delridge Way SW	2013	16	187	\$2,000,000	5/31/17	\$125,000	\$667	4.9%	\$32.70
10	Sedona Micros	8520 20th Ave NE	2015	80	207	\$9,000,000	6/10/16	\$112,500	\$545	5.6%	\$30.50
Average			2013	52	207			\$144,822	\$710	5.2%	\$36.52

SEDUS

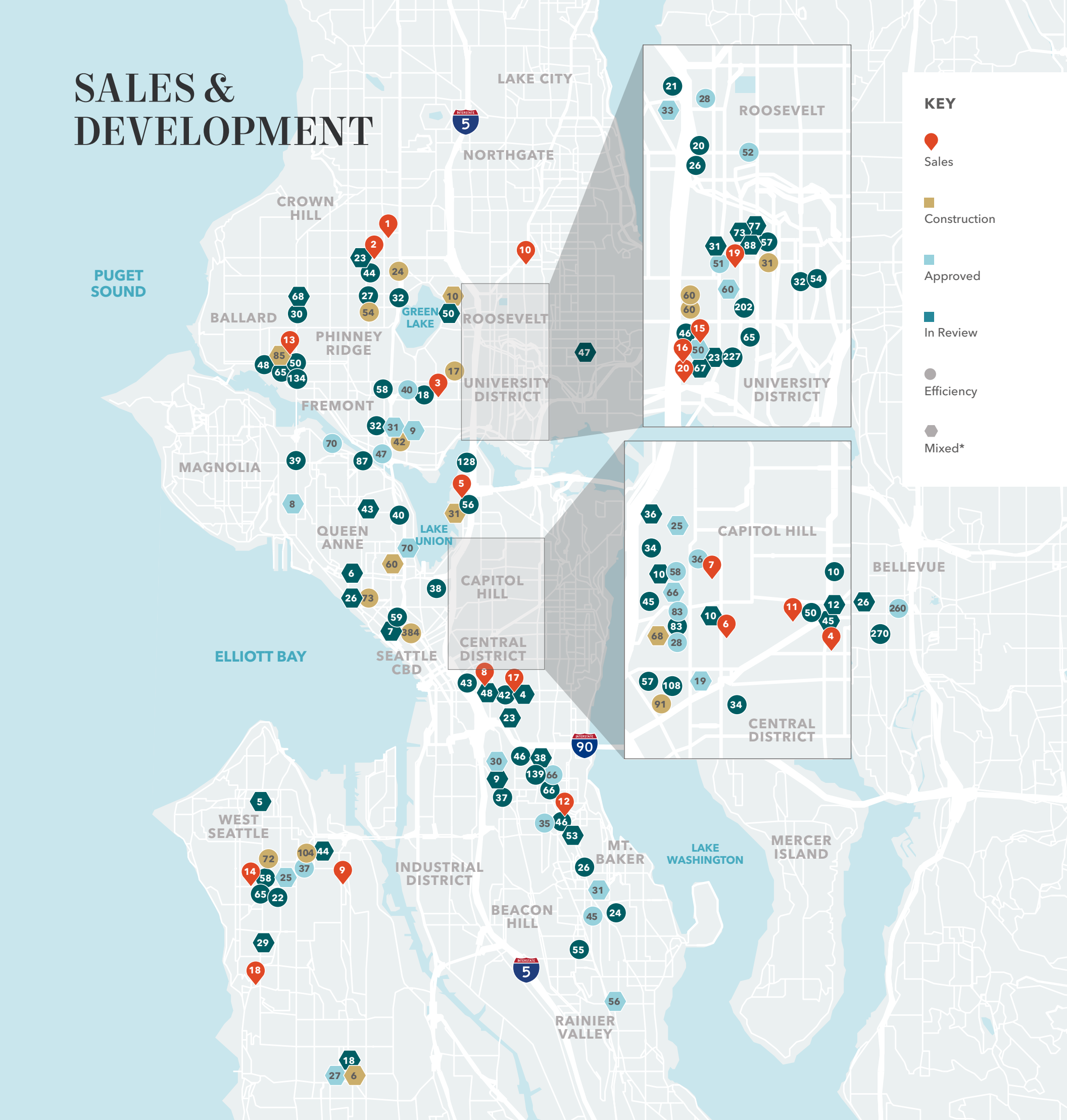
	Property Name	Address	Year Built	Units	Avg Unit Size (SF)	Price	Sale Date	\$/Unit	\$/NRSF	Cap Rate	NOI/NRSF
11	The Redwood	111 21st Ave E	2017	75	280	\$17,500,000	12/18/18	\$233,333	\$832	4.5%	\$37.45
12	Link Studios	2939 S Mt Baker Blvd	2015	60	206	\$7,478,753	8/30/18	\$124,646	\$604	5.1%	\$30.79
13	Ballard 57	1731 NW 57th St	2016	48	275	\$11,000,000	8/16/18	\$229,167	\$833	4.5%	\$37.49
14	Lofts at the Junction	4535 44th Ave SW	2015	38	337	\$9,500,000	7/26/18	\$250,000	\$742	4.6%	\$34.14
15	Willet	4252 8th Ave NE	2017	20	323	\$5,450,000	4/27/18	\$272,500	\$843	4.4%	\$37.10
16	Pomelo Heights	4229 7th Ave NE	2017	23	246	\$4,950,000	4/24/18	\$215,217	\$876	4.3%	\$37.66
17	Jupiter	155 17th Ave	2015	20	252	\$3,846,500	9/12/17	\$192,325	\$764	5.0%	\$38.22
18	Viridian	6917 California Ave SW	2015	30	204	\$5,030,000	6/30/17	\$167,667	\$821	5.4%	\$44.35
19	Den on Brooklyn	5043 Brooklyn Ave NE	2013	50	262	\$8,825,000	2/28/17	\$176,500	\$674	4.4%	\$29.65
20	Studio 7	4029 7th Ave NE	2013	75	327	\$14,450,000	6/30/16	\$192,667	\$589	4.7%	\$27.70
Average			2015	44	271			\$205,402	\$758	4.7%	\$35.45

MARKET-RATE APARTMENTS*

		Year Built	Units	Avg Unit Size (SF)	Price	Sale Date	\$/Unit	\$/NRSF	Cap Rate	NOI/NRSF
Average (Built 2012 & Newer)		2016	129	624		6/2016 - Present	\$433,945	\$547	4.4%	\$30.87

*BASED ON 60 URBAN KING COUNTY SALES (7,758 TOTAL UNITS) FROM JUNE 2016 - PRESENT

SALES & DEVELOPMENT



INVENTORY & PIPELINE

Only 950 of the 1,700 micro units and SEDUs forecast to be delivered in 2019 were completed as of November. Construction delays, oversupply concerns, and escalating construction costs are the leading causes of fewer building completions. Additionally, the citywide upzone adopted in April 2019 made new development of micro units nearly impossible, with only two projects currently under construction and two in permitting. In contrast to the anemic growth of micro apartment supply, there are nearly 3,000 SEDUs under construction or approved, which will effectively double the existing stock of SEDUs in the next 24 months.

Existing	Construction	Approved	In Review	Total Pipeline
7,247	1,272	1,476	4,134	6,882
% Inventory	18%	20%	57%	95%

7,247 UNITS

1,272

1,476

4,134

*MIXED DEVELOPMENTS INCLUDE BOTH MICROHOUSING AND STANDARD APARTMENT UNITS. THE NUMBER WITHIN THE HEXAGONS INDICATES MICROHOUSING UNITS ONLY IN THE MIXED DEVELOPMENTS.

FINANCING

OVERVIEW OF PERMANENT DEBT FOR MICROHOUSING – MARKET TERMS

Loan Structures	Hybrid fixed-to-float loans with 5, 7, and 10-year fixed rates and adjustable tails are widely available.
Minimum DSC	Typically 1.25, with some lenders able to underwrite to 1.20 (comparable to market-rate apartments)
Maximum Loan-to-Value	Typically 75% (comparable to market-rate apartments)
Amortization	30 years universally available
Interest-Only	One to two years of interest-only is possible on high-leverage requests. Full-term interest-only is achievable on loans with DSC over 1.35.
Term	10–30 years
Prepayment Penalties / Exit Cost	Stepdown prepayment penalties are widely available
Personal Recourse	Being open to personal recourse significantly expands the number of available lenders, but nonrecourse loans are available.
Reporting	Annual reporting of property financials in addition to personal financial information is usually required.
Rate Lock	Early rate lock available with most lenders
Transaction Cost	Indistinguishable from market-rate apartments. Lender fees, third-party reports, title and escrow, legal, and miscellaneous costs totaling up to 0.5% of the loan amount are common.

SAMPLE LOAN TERMS – PERMANENT FINANCING

Sample Loan Amount	\$10,000,000		
Loan Type	5-Year Hybrid	7-Year Hybrid	10-Year Hybrid
Pricing Index	5-Year Treasury	7-Year Treasury	10-Year Treasury
Index	1.75%	1.85%	1.95%
Estimated Pricing Spread	2.00%	2.00%	2.00%
Note Rate	3.75%	3.85%	3.95%
Amortization	30 Years	30 Years	30 Years
Amortizing Monthly Payment	\$46,312	\$46,881	\$47,454
Interest-Only Payment	\$31,250	\$32,083	\$32,917
Estimated Transaction Cost	\$25,000	\$25,000	\$25,000
Prepayment Penalty	5-4-3-2-1	5-5-4-4-3-2-1	5-5-4-4-3-3-2-2-1-1

MICROHOUSING SALES EXPERTS

We don’t just sell microhousing—we’ve created an entire division specializing in its valuation, acquisition, and sale.

We believe microhousing is the most innovative way to diversify and improve downturn resilience in your apartment portfolio while providing safe, affordable homes for residents.

Residents have spoken: they’ll trade square footage for location and great access to the city. That’s why we’ve made it our mission to sell and educate the world on microhousing.

23

MICROHOUSING INVESTMENTS SOLD AND UNDER CONTRACT

100%

MICROHOUSING INVESTORS, OWNERS, AND DEVELOPERS IN OUR DATABASE

\$272,500

RECORD MICROHOUSING PRICE PER UNIT

\$877

RECORD MICROHOUSING PRICE PER SQUARE FOOT

4.3%

RECORD MICROHOUSING CAP RATE

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