



Menifee Housing Study

Housing Market Impact Study | Inclusionary Housing Feasibility Study

Presented to Menifee City Council June 19, 2024

Prepared for:

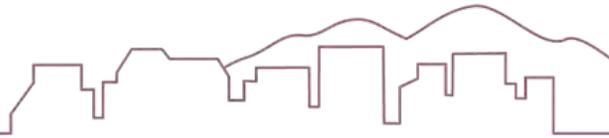


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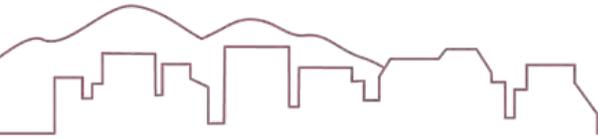
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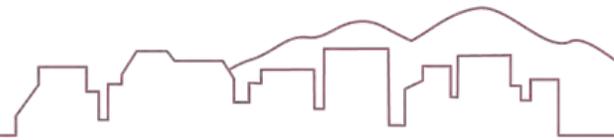
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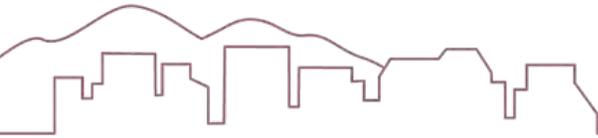
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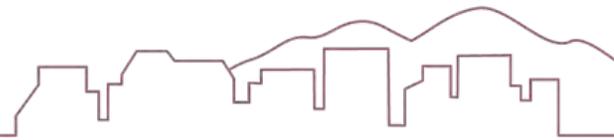


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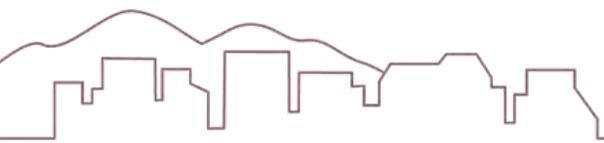


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Summary

The 6th Cycle Regional Housing Needs Assessment (RHNA) for Southern California brought significant changes from prior cycles. The number of housing units allocated to jurisdictions substantially increased, in part reflecting the need to alleviate overcrowding throughout the region. In addition, recent changes to state law require cities to rezone additional property if sites identified for affordable housing development in the general plan housing elements are developed without affordable housing. Many jurisdictions across the region have scrambled to designate sites for affordable housing development. Even more cities are exploring options to ensure that affordable housing gets built.

The aggressiveness of the 6th Cycle allocations highlights the pervasive problem of underbuilding housing—market rate and below market rate—regionally and nationally, as described in this report. This may appear to be somewhat at odds with the experience in Menifee, which has been steadily adding housing since its incorporation and before. Nevertheless, City wants to ensure that it continues to be a producer of housing as the region strives to address the critical shortfall.

It is within this context that the Menifee Housing Study has been prepared for the City. The first part of the report, the Housing Market Impact Study, assesses the overall demand for housing development in Menifee, the economic and market conditions underpinning that demand, and the types of housing that are needed. It also addresses constraints and barriers to affordable housing in the city.

The second part of this report is the Inclusionary Housing Feasibility Study. Local inclusionary housing ordinances require that new residential development

projects provide a set percentage of the units—typically, but not always, 5 to 15 percent of the total number of units—at a sales price or rent that is affordable to lower-income households. The report describes the requirements and considerations when adopting an inclusionary housing ordinance, analyzes the financial feasibility implications of inclusionary housing for six residential development prototypes, and provides recommendations for further consideration should the City Council be interested in pursuing an inclusionary housing requirement.

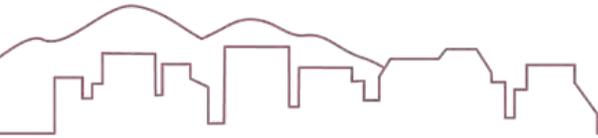
The following sections describe key findings presented in this report.

CHANGING DEMOGRAPHICS

Declining Household Sizes

Nationally, the average size of households steadily decreased from 3.14 persons per household in 1970 to 2.50 in 2022. In contrast, households in California continued to slowly increase, from 2.79 in 1990 to a high of 2.96 in 2017, and declining since then, reaching 2.77 in 2023. Household size is expected to continue to decline in California, in the Southern California region, and in Western Riverside County.

Because Menifee included several retirement communities when it was incorporated, it has a smaller average household size than nearby cities. Nevertheless, it exhibits the same basic trend in average household size: rising slightly from 2.78 in 2009 to 2.91 in 2017, and then declining slightly to 2.89 in 2023. The analysis presented in this report projects that Menifee's average



household size will decrease to 2.73 over the next 20 years, if present trends continue.

Fewer Married-couple Families with Children at Home

The number of households in the United States that are a married couple family with children at home decreased from 39 percent to 19 percent of all households from 1970 to 2021, declining from the most common type of household to the third most common type, after living-alone households and married-couple families without children living at home. Furthermore, only 28 percent of all households had children living at home.

In 2021, 27.8 percent of Menifee's households were married-couple families with children at home. However, across all household types, households with children at home increased slightly from 35.1 percent in 2012 to 36.8 percent in 2021. For 2021, among households that moved into their current home in the prior 12 months, the average household size was 3.3 persons per household for owner-occupied housing and 2.8 for renter households. For both owners and renters who moved in the prior 12 months, about 29 percent were two-person households, the most common household size among recent movers.

HOUSING CONSTRUCTION

Depressed Housing Production

The 2008/09 recession decimated the housing industry, and only in the last year has it returned to the average level of housing production from 1968 to the March 2006 peak. In the previous economic expansion, the economy produced almost twice as many units per year as it has in this expansion.

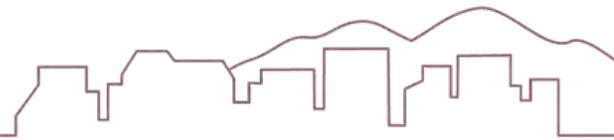
The underbuilding of housing during and since the 2008/09 recession is a national challenge, although some areas and regions have fared better than others. It is also a California problem. The average number of housing units constructed per year from 1990 to the 2008/09 recession was 128,300. Between that recession and the onset of the COVID-19 pandemic, the number of housing units constructed averaged only 72,600 per year, or 43 percent fewer. The market rebounded somewhat since then, averaging 118,100 units per year. Nevertheless, without the slowdown following the 2008/09 recession, the state would have an additional 669,000 housing units, or 4.5 percent more than there are today.

The underbuilding of housing nationally and in California is generally accepted as being a primary driver of rapidly escalating housing costs. The current challenges with high interest rates, lack of a sufficient labor force, and supply chain shortcomings still hamper the housing industry. Boosting housing production in Menifee may be limited by these national and regional housing industry constraints.

Prevalence of Single-Family Detached Housing

From 2012 to 2022, the number of housing units in Menifee and nearby cities increased by 20,645, growing 1.4 percent per year on average. Single-family detached housing accounted for 77.9 percent of that growth; single-family attached housing accounted for 3.7 percent; and multifamily provided the remaining 18.5 percent.

There are differences among cities in the types of housing that were developed in this period. However, in Menifee, single-family detached housing accounted for 98 percent of new housing constructed, higher than all neighboring market-area jurisdictions, except Canyon Lakes. Menifee accounted for 36.6 percent of



all market-area housing growth, but it accounted for 45.5 percent of the single-family detached housing growth.

However, as the demographics of the region continue to move to smaller households and fewer children, the market may adjust housing types over time. Nevertheless, a strength of the market in Menifee is affordable development costs that enable the production of housing that is attainable to middle-income households, and in the future it may be more successful than other cities with rising land and development costs.

Larger Houses and Higher Prices

From 1974 to 2022, the average inflation-adjusted price of a new single-family housing unit in the US increased 86.7 percent, but the cost per square foot only increased 22.4 percent. Roughly three-fourths of the inflation-adjusted increase housing cost was a matter of building larger housing units.

This suggests that one approach to encouraging the development of more moderately priced housing would be to facilitate the construction of smaller-size housing units. However, this is easier said than done. The financial incentive to the developer is to construct larger units to the degree that market demand will support such development. Furthermore, as costs for land, increased development standards, infrastructure and development fees increase, and financing costs remain high the financial incentive to the developer is to build larger, more expensive units, again, to the degree that the market will bear.

Multifamily Housing

The outstanding issue is that the market is not directing much investment into Menifee for single-family attached housing and multifamily housing. This may be a concern for the City. Attached and multifamily housing tends to be of a smaller size than detached housing, and thus, maybe be better suited to

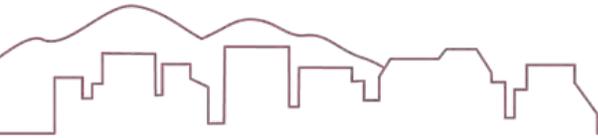
changing demographics of smaller household sizes. Smaller housing also translates into lower priced housing, which may be better suited to some people who work in Menifee but cannot afford to purchase a detached house. Such housing may also be a first step for people who grow up in Menifee and who are moving out of their parents' homes.

Based on the interviews with developers and other stakeholders, there is an expectation that the market will eventually produce attached and multifamily housing in greater numbers in Menifee. They indicated that rents may not yet be sufficient to support new construction and that sites remain available for such development in other nearby cities that are closer to higher concentrations of jobs.

BARRIERS TO HOUSING PRODUCTION

To prepare this report, the consultants interviewed a variety of market-rate and affordable-housing developers and reviewed the City's general plan and development regulations to identify barriers to housing production. There are many barriers—such as financing costs, mortgage rates, and market-rate sales values and rents—over which the City has no influence. The consultant's review identified little that the City can do to address these barriers.

The continued entitlement for and construction of single-family detached housing and interviews with developers indicate that the City imposes no undue barriers to this portion of the market. In contrast, the analysis indicates that the market produces only limited development of single-family attached and multifamily housing. The developer interviews suggest that this is a market effect, which the City can do little to address. However, there are two local factors that may influence the production of these types of housing.



Multifamily Development in the Economic Development Corridors

One potential barrier that was brought up in interviews was the City's limits or prohibitions on building stand-alone residential buildings and projects in the Economic Development Corridors (EDC). It is possible that allowing stand-alone residential in the EDC might facilitate multifamily development. Nevertheless, the development standards in the EDC are part of a long-term vision and comprehensive plan for development in these areas. Changes in EDC development regulations would need to weigh the possibility and likelihood that changes would actually generate new housing against the long-term and comprehensive vision that the City has adopted for the EDC.

Location of Sites Planned for HDR Development

The other potential barrier is a lack of HDR-zoned sites in proximity to the central economic activity centers of Menifee. Such locations are more attractive to market rate developers and more likely to sustain higher rents or sales values that are necessary to support new construction. Having more sites zoned for HDR development can help ensure that land can be available for multifamily development when the market is ready to invest in Menifee. Similarly, having sites zoned for HDR development near activity centers may entice more investment in multifamily development sooner than may be achieved with the current inventory of sites.

INCLUSIONARY HOUSING

The report analyzes the potential impact of an inclusionary housing requirement on the financial feasibility of residential development in Menifee. With an inclusionary housing ordinance (an amendment to the development code) the City can require new residential development projects to offer a specified percentage of the new housing units at sales prices or rents that are affordable to lower-income households. The City can also establish an in-lieu fee for

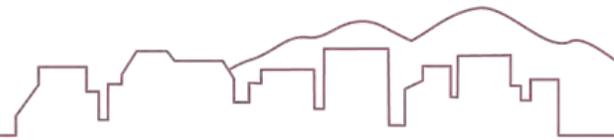
developers who do not want to provide onsite affordable housing or cannot accommodate it onsite.

The report analyzes the financial feasibility for four for-sale residential product types and for two for-rent product types. Current market conditions, primarily interest rates on construction loans and permanent financing, but also other cost factors, make much development financially infeasible. The analysis presented in this report is based on an assumption that interest rates will return to a more normal level over the next year or two. So, the financial feasibility findings represent the short-term future.

State law allows the CA Department of Housing and Community Development to review inclusionary housing requirements over 15 percent. So, the analysis first considered the impact of a 15 percent inclusionary requirement. It found that the provision of affordable housing should be financially feasible for medium-density townhouses and multifamily apartments. However, the other four residential development product types would not be financially feasible.

The analysis also considered lower inclusionary housing requirements. It found that a 5 percent inclusionary housing requirement should be financially feasible for most residential development product types, with the exception of vertical mixed-use, at this time.

The report also calculated an inclusionary housing in-lieu fee. It estimates that the cost to the City of Menifee to entice an affordable housing developer to build affordable housing in the City would be \$154,372 per affordable unit, assuming that the affordable housing developer is able to earn low-income housing tax credits and conventional bank financing. Finally, the analysis found that a \$154,372 in-lieu fee for required affordable housing units would also be financially feasible for all residential product types evaluated, with the



exception of large-lot single-family detached housing (the fee was about 25 percent too high at this point in time).

NEXT STEPS

Changing Demographics

The changing demographics discussed in this report do not rise to a specific action item. However, they will eventually fuel changes in the demand for housing—while many if not most cities in Western Riverside County want to attract new families with children, this is already a minority of the demand for housing, and it is decreasing. Not only housing, though, these demographic changes will affect the labor force and what kind of businesses can successfully operate in Menifee, consumer spending and the types of retailers that will find the city and attractive place to locate, and even the demand for public facilities and services. Thus, these characteristics of Menifee residents deserve monitoring, even though resulting actions may be in the future.

HDR Zoning

Expanding the land area zoned for high density residential development in proximity to activity centers in the city could spur more investment in multifamily housing before mixed-use development becomes financially feasible to develop. To move forward with this, the City could identify potential properties that could accommodate multifamily development projects of around 150 units, gauge property owner interest, and vet the selections with brokers and multifamily developers before moving on to community engagement and public hearings.

Inclusionary Housing

To move forward with consideration of inclusionary housing, the City will need to make three key decisions.

1. *Percentage of Affordable Units*

What percentage of new residential units should be affordable? The City would have a wide latitude in setting the inclusionary requirement. From a solely financial feasibility perspective, the analysis suggests an inclusionary requirement of 5 percent of housing units affordable to low-income and very low-income households.

2. *Minimum Project Size*

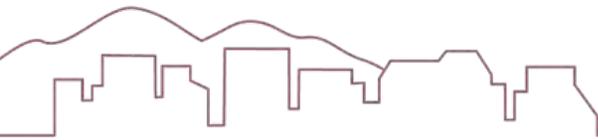
An inclusionary ordinance would need to establish a minimum project size to be subject to the inclusionary housing requirement. The analysis suggests that development projects with 10 or more housing units would have to provide affordable housing.

3. *Alternative Means of Compliance*

The City would need to identify one or more alternative means of compliance. The most common alternative is the payment of an in-lieu fee. The analysis suggests an in-lieu fee of \$154,372 per affordable housing unit required. This amount should provide the City with enough funding to leverage affordable housing developers to construct the required affordable housing units offsite, most likely in a fully affordable housing project. With a 5 percent affordability requirement, this fee would be \$7,719 per market rate unit, or \$3.23 per square foot of finished floor area (i.e., excluding garages).

4. *Housing Tenure Applicability*

As the Housing Market Impact Study portion of this report indicates, the market is not directing much investment into multifamily housing in Menifee. The City may want to consider exempting for-rent housing from the inclusionary requirement in order to create an incentive for multifamily housing.



HOUSING MARKET IMPACT STUDY





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2. Introduction

Broadly speaking, the housing market impact study is focused on the overall demand for housing development in Menifee, the economic and market conditions underpinning that demand, and the types of housing that are needed. The study also addresses constraints and barriers to affordable housing in the city. Based on the market demand and the constraints and barriers, the study provides recommendations for policies, strategies, and programs and an evaluation framework with which the city can track progress.

The study begins with an overview of the national and state context for housing development. This broad overview is important because many of the market factors that are analyzed for the residential market area reflect long-term national demographic and social changes. The decreasing average size of households, for example, has been occurring across the US for decades. This is not something that city policy can change, but rather, it is something that local policy must reflect.

Cities play a critical role in housing development: they regulate the locations where new housing can be developed and the density and other development standards with which new housing development must comply. In so doing, cities influence the price of land and the financial feasibility of new development. However, an individual city's influence and its ability to promote housing production are very limited relative to everything else that goes into making a housing development happen, such as the acceptable risk and necessary rate of return required by the equity investors and banks that fund new development, the availability of construction workers to do the actual construction, the availability and cost of construction materials, or the interest rates which determine how much households can pay to purchase new housing.

After the national context overview, the study provides detailed data and analysis about the factors that determine the long-term demand for housing and the types of housing. This section also looks at the difference in these market factors for households with incomes above moderate (i.e., above 120 percent of the area median income) and households with moderate incomes (i.e., 80 to 120 percent of the area median income) or below. In preparing this study, the consultants interviewed housing industry stakeholders, including market rate developers, affordable housing developers, lending providers, and real estate brokers. The market analysis section summarizes insights from these interviews.

The study presents a forecast and gap analysis for housing production, with projections for population, households, housing needs, and employment. The forecast demand for housing looks at needs based on tenure, price points based on affordability, and types of housing.

The final section of this study provides recommendations for potential policies, strategies, and programs that can help achieve the city's goals for housing. It also provides a framework for measuring and evaluating progress on achieving the city's goals.



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3. National and Regional Housing Market Context

The local demand for housing is driven by the regional demand for housing and the degree to which a home in the local market meets the needs of households moving to or relocating in the region. This chapter explores national and regional trends that can be expected to influence the types of housing that might be best suited to the needs for regional household growth.

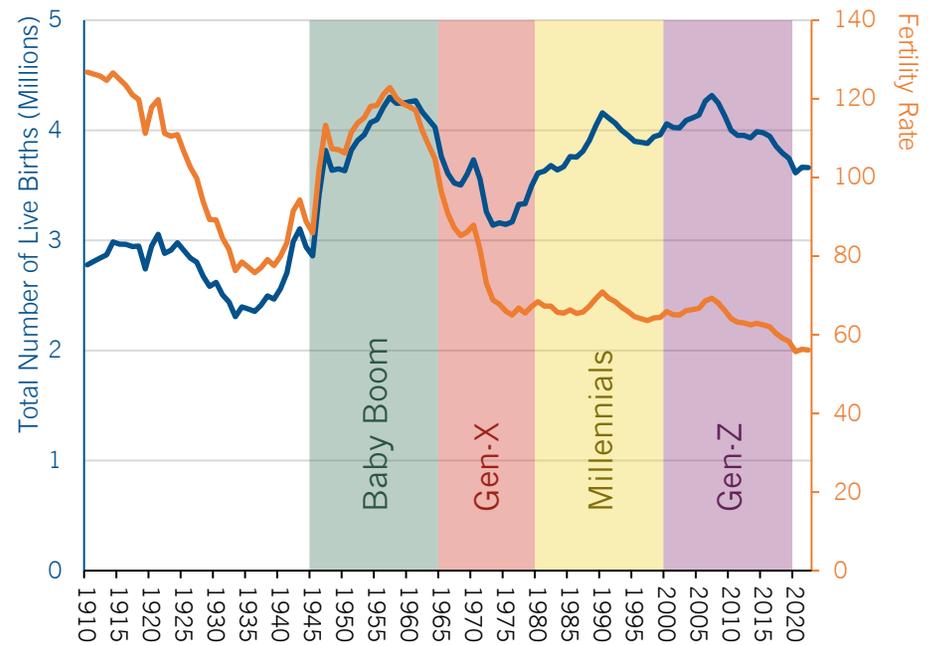
LONG-TERM DEMOGRAPHIC TRENDS

Generational Dynamics

One can regularly come across headlines and articles discussing differences among the generations, especially Baby Boomers and Millennials but also Gen-X and Gen-Z. While these discussions tend to debate the social and cultural differences among the different age groups, there are very real changes in the number of births (which affects the total population) and the fertility rate (which affects the average size of families).

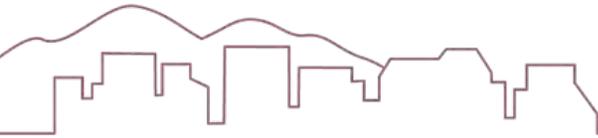
Figure 1 shows the number of live births and the fertility rate (the number of live births per woman aged 15 to 45) in the US for each year from 1910 to 2022. It also shows descriptive labels for the four most recent generations. There are alternative demarcations posited by different experts and pundits, but the boundaries for each generation shown in Figure 1 are aligned with five-year age cohorts, which simplifies the use of Census Bureau data. Thus, the Baby Boom began in 1945, Gen-X in 1965, the Millennials in 1980, and Gen-Z in 2000 and ending in 2019, with a new as-yet-to-be named generation beginning in 2020.

Figure 1: Number of Live Births, Fertility Rates, and Approximate Generational Labels; United States; 2009 to 2022



Source: PlaceWorks, 2024, using data from the US Centers for Disease Control, National Vital Statistics System (2022 data is preliminary).

What the data shows is that the total population has grown in waves, with the largest being the Baby Boom and the Millennials, and troughs or plateaus with Gen-X and Gen-Z. In contrast, their fertility rate, after a steep decline following



the introduction of the birth control pill¹, remained fairly constant from the mid-1970s until 2007. Since 2007, the number of births and the fertility rate have been declining.

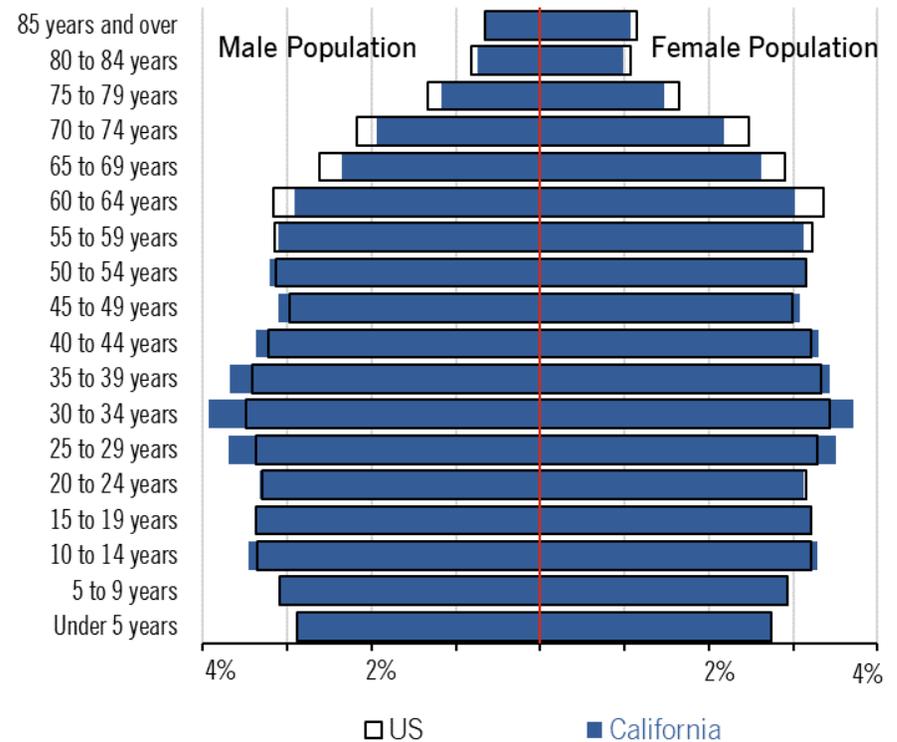
The waves of population have consequences for employment and the economy, housing demand, and even taxes and demands for public services. More importantly, the flatness and late decline in fertility rates suggests (and is shown to be the case below) that families are smaller than those during the Baby Boom and, have gotten even smaller in recent years.

One final demographic measure is total fertility rate, which is not shown in the chart. This measure is the expected number of lifetime births per 1,000 women given current birth rates by age. A total fertility rate of 2,100.0 births per 1,000 women is considered necessary to replace a population over time. The US total fertility rate in 2018 was 1,729.5 (and 1,632.0 in California). With the exception of 2007, the US total fertility rate has not exceeded 2,100 since 1971. Were it not for immigration, the US population would be declining over time.

Age Distribution in California

The resulting age distribution for the US population is quite similar to that in California, but not exactly the same. Figure 2 shows the population in California and across the US by age and sex, as a percentage of the total population.

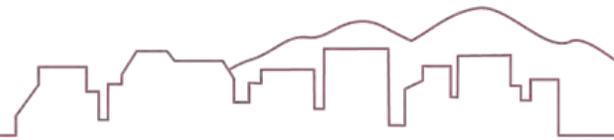
Figure 2: Population by Age Group and Sex as a Percentage of Total Population; California and the US; 2021



Source: PlaceWorks, 2024, using data from the US Census Bureau's 2021 American Community Survey, 1-Year Estimates.

¹ The decline is largely attributed to the introduction of the birth control pill. The FDA approved the pill to regulate menstruation in 1957, the year in which the fertility rate reached its highest level since 1916. In

1960 the FDA approved its use as an oral contraceptive. In 1965, the US Supreme Court effectively ended state and local laws limiting the use of the birth control pill to married couples.



For children and young adults under the age of 25, the share of total population is almost the same nationally as in the state. Then, the age groups from 25 to about 54 represent a larger share of California's total population than that in the US. These groups would include Gen-x and Millennials. Finally, the population aged 55 and older account for a smaller share of California's population and a larger share of the US population. This group includes Baby Boomers and those older.

These age differences reflect two long-term migration trends. California, for several decades, has had a net domestic out-migration, and previous analysis by the Public Policy Institute found that this out-migration was more prevalent among older residents than younger. More importantly, though, California also has a decades-long trend of foreign in-migration. In 2021, foreign-born residents accounted for 13.6 percent of the US population but 26.6 percent of California's population. Foreign migrants tend to be younger than the average age and they tend to have larger family sizes.

These age differences suggest that California's economy may have less challenges with an aging population. The differences also suggest that a larger portion of the state's population is in the age groups that are moving out of their parents' homes, those forming households, and those buying their first homes. The under-building of housing in the US discussed in US Housing Production section below can be expected to be more acute in California than in the US because of the age differences.

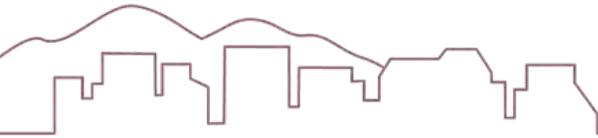
² The 2021 data are from the American Community Survey, which is conducted over the course of the calendar year. Thus, the 2021 data may reflect temporary shifts in living arrangements reflecting the impacts of the COVID-19 pandemic.

Household Changes

With the fertility rate leveling off in the early 1970s and the oldest Baby Boomers moving out of their parents' houses, the ways in which Americans live together in households began a decades-long transition. Figure 3 shows the percentage of total households by type of household for the US from 1970 to 2021².

During this period, the percentage of households that were married couples with children under the age of 18 at home declined from 39 percent to 19 percent, even though the number of babies being born was steadily rising from 1976 through 2007. This decline was slightly offset by an increase in the percentage of households that were single-parent families with children under the age of 18 at home, which increased from 5 percent in 1970 to 10 percent in 2020. Nevertheless, the percentage of households with children under the age of 18 at home, regardless of marital status, decreased to 29 percent of all households, down from 44 percent in 1970.

In contrast, the percentage of households that were married couples with no children at home hovered around 29 percent across five decades, declining to 28 percent in 2021. As mentioned above, the share of households that were a single parent with children increased from 5 percent to 10 percent, and the share that were single parents without children at home increased from 5 percent to 7 percent.



Perhaps the most dramatic change was the large increase in the share of households that were single people living alone, from 23 percent in 1980 (data were not published for 1970) to 28.3 percent in 2021, becoming the most prevalent type of household in the US. The two most common types of households—married couples without children living at home (28.1 percent) and single people living alone—account for 56 percent of all households.

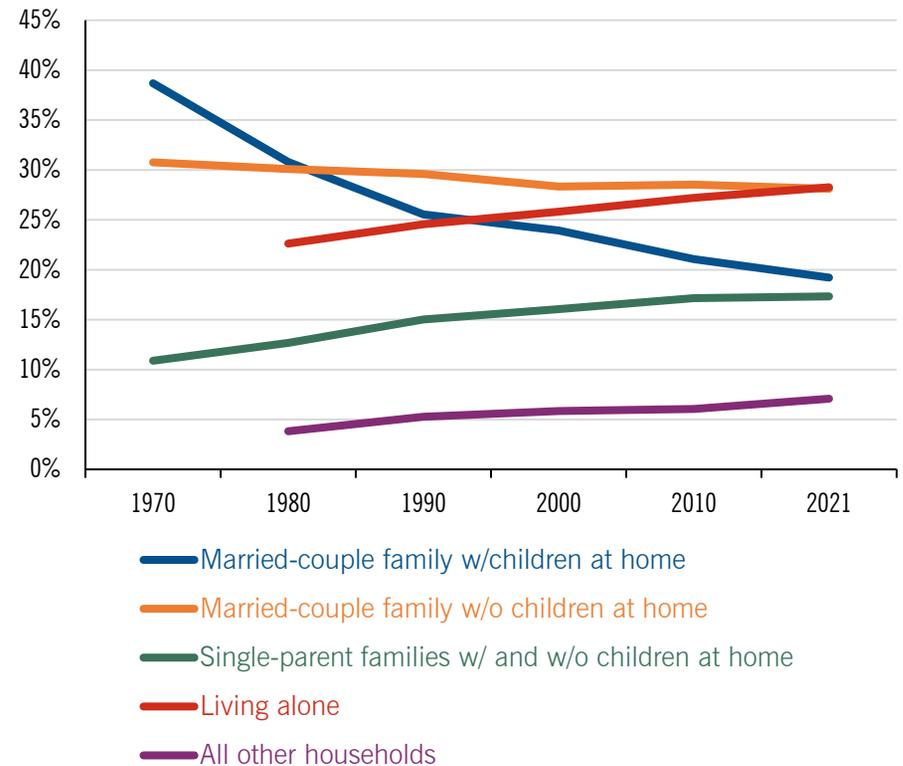
From 1980 to 2021, the number of households in the US increased by 47.1 million. Households with children, regardless of marital status, accounted for 14.6 percent of the total household growth. Households without children (married couple, single householders living with one or more relatives, and singles living alone) accounted for 72.8 percent of the increase. Nonfamily households accounted for the remaining 12.6 percent of the increase in households.

The household-type data show that the concept of the nuclear family, which plays a central role in how Americans view our society, really represents a minority of households. Furthermore, considering that only 28 percent of all households have children, the data raise the question of how well the housing market, which produces primarily single-family detached housing, is serving the needs of a majority of Americans.

Households by Size

The number of households in the US increased from 63,401,000 in 1970 to 131,202,000 in 2022. The increase of 67,801,000 households represents an annual growth rate of 1.4 percent per year. However, the growth in households was largest among one- and two-person households, and increasingly larger households have increasingly lower rates of growth. The number of households with six or more persons declined during this period. Table 1 provides data on the changes in the number of households based on household size.

Figure 3: Type of Household by Share of Total Number of Households; United States; 1970 to 2021



Source: PlaceWorks, 2024, using data from the US Census Bureau. Decennial Censuses (2007 to 2000) and American Community Survey (2010 and 2021).

Table 1: Change in the Number of Households by the Number of Persons in Household; United States; 1970 and 2022

Number of Persons in Household	Total Increase	Annual Rate of Change	Share of Total Household Growth	Share of Household, 1970	Share of Households 2022
One	27,036,000	2.4%	39.9%	17.1%	28.9%
Two	27,216,000	1.8%	40.1%	28.9%	34.7%
Three	8,865,000	1.1%	13.1%	17.3%	15.1%
Four	6,200,000	0.9%	9.1%	15.8%	12.3%
Five	746,000	0.2%	1.1%	10.3%	5.6%
Six	-714,000	-0.4%	-1.1%	5.6%	2.1%
Seven or more	-1,546,000	-1.3%	-2.3%	5.0%	1.3%
Total	67,801,000	1.4%	100.0%	100.0%	100.0%

Source: PlaceWorks, 2024, using data from the Census Bureau's Current Population Survey.

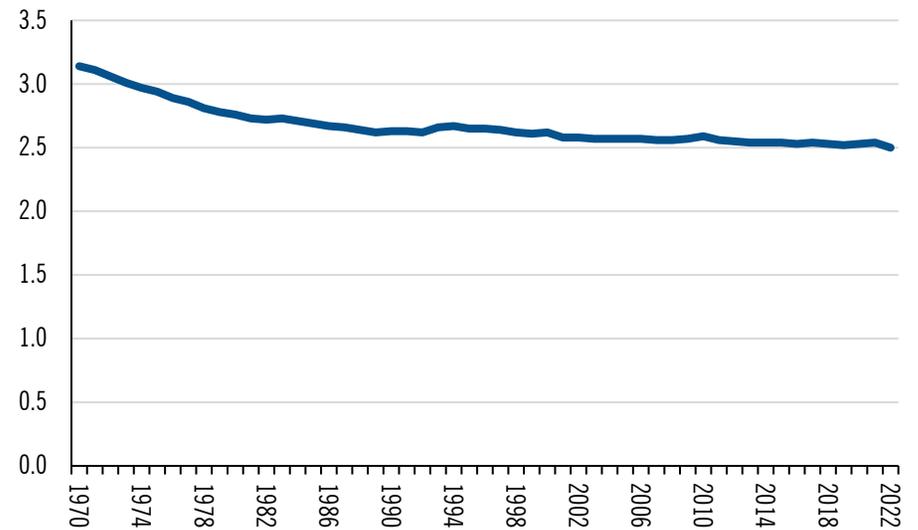
One- and two-person households accounted for 80 percent of household growth over the five decades and increased from 46 percent of the total number of households in 1970 to 64 percent of all households in 2022. In contrast, all larger household sizes experienced a decline in the share of total households.

Average Household Size

Reflecting the higher growth in one- and two-person households and the decline in the number of households with six or more people, the average size of households has decreased. In 1970, the average household had 3.14 people.

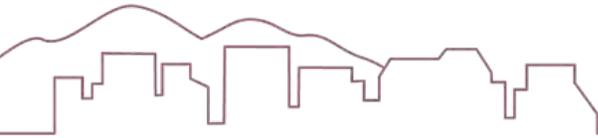
By 2022, the average household size had decreased to 2.50 persons per household. Figure 4 shows the average household size from 1970 to 2022.

Figure 4: Average Number of Persons per Household; United States; 1970 to 2022



Source: PlaceWorks, 2024, using data from the US Census Bureau, Current Population Survey

The largest decrease in average household size occurred in the 1970s and 1980s, with a brief pause during and after the 1982 recession. In large part, this reflects Baby Boomers leaving their parents' homes and moving out on their own. Nevertheless, the average household size has generally decreased over the entire period, with brief pauses during and immediately after other recessions.



Life Transitions

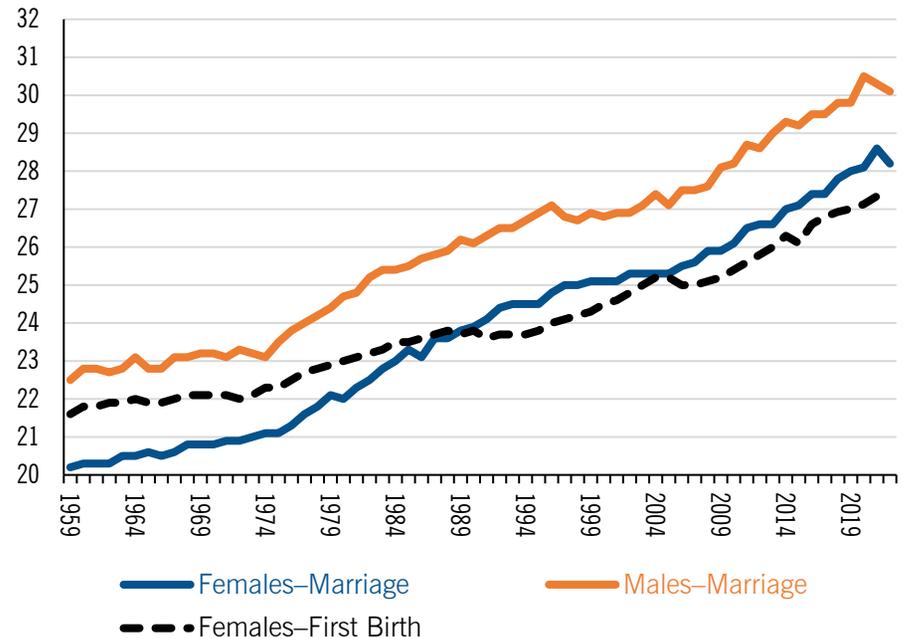
The age at which women first give birth and the age at which people first marry has been increasing for many decades. The delay in forming families has implications for the demand for housing. Indeed, one can surmise that the long-term increase in households with single people living alone results, in part, from the trend of people spending more of their lives between becoming adults and first forming families. Figure 5 shows the median age at marriage for men and woman and the mean age for women at first birth.

The median age at marriage was steadily increasing for men and women but began a more rapid increase beginning in 1975 for men and 1976 for women. The rate of increase slowed down in the late 1990s and then grew again starting in 2006. There was a decline from 2021 to 2022. For men, the median age at marriage increased from 23.2 in 1970 to 30.1 in 2022, an increase of 30 percent. For women, the median age at marriage increased from 20.8 in 1970 to 28.2 in 2022, an increase of 36 percent.

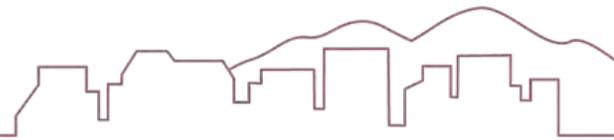
The mean age of women at first birth has been increasing since 1959, but the rate of increase was lower than the rate of increase in the median age at marriage. From 1959 to 1988, the mean age at first birth was higher than the median age at marriage. The mean age of women at first birth increased from 22.1 in 1970 to 27.3 in 2021, an increase of 24 percent.

The data for age at first marriage and age at first birth show that Americans are spending a larger portion of their life as single adults without children before they move into the family-forming stage of life and that this is a decades-long trend.

Figure 5: Median Age at First Marriage and Mean Female Age at First Birth; United States; 1959 to 2021 (Birth) and 2022 (Marriage)



Source: PlaceWorks, 2024, using marriage data from the US Census Bureau's Current Population Survey and birth data from the US Centers for Disease Control, National Vital Statistics System.



RESIDENTIAL DEVELOPMENT TRENDS

US Housing Production

Since the end of the recession related to the COVID-19 pandemic, the US housing market completed about 1.3 million new housing units. By previous economic expansions standards, this is slightly below average (1.4 million per year during economic expansions starting in December 1970), but somewhat remarkable given the supply-chain disruptions, high inflation, and the increase in interest rates over the past year. What is more remarkable, however, is that during the previous economic expansion, running from July 2009 to February 2019, the housing market produced only an average of 879,000 total new housing units per year. This is 38 percent below the annual average for economic expansions. Over the more than nine years of this economic expansion, this resulted in 5 million fewer housing units having been built. Figure 6 on the following page shows the number of housing units completed each month at a seasonally adjusted annual rate. Table 2 provides the average annual housing production during each economic expansion since December 1970. When viewed in tandem, Table 2 and Figure 6 illustrate the monthly and average annual housing unit construction since 1970.

During the previous ten years, the housing market completed an average of 868,642 housing units per year. At the beginning of this period, 2009, the Millennials were between 10 and 29 years old. At the end of this period, 2018, the Millennials were between 19 and 38 years old. For Baby Boomers, the corresponding age ranges represent the years 1974 to 1983. During this time period, the housing market completed an average of 1,497,850 housing units per year. The housing market produced 72 percent more housing units for the period when Baby Boomers were forming families than it produced

when Millennials were forming families, even though there were only 3.5 percent more babies born during the Baby Boom as were born for Millennials. It is no wonder that there is a housing crisis.

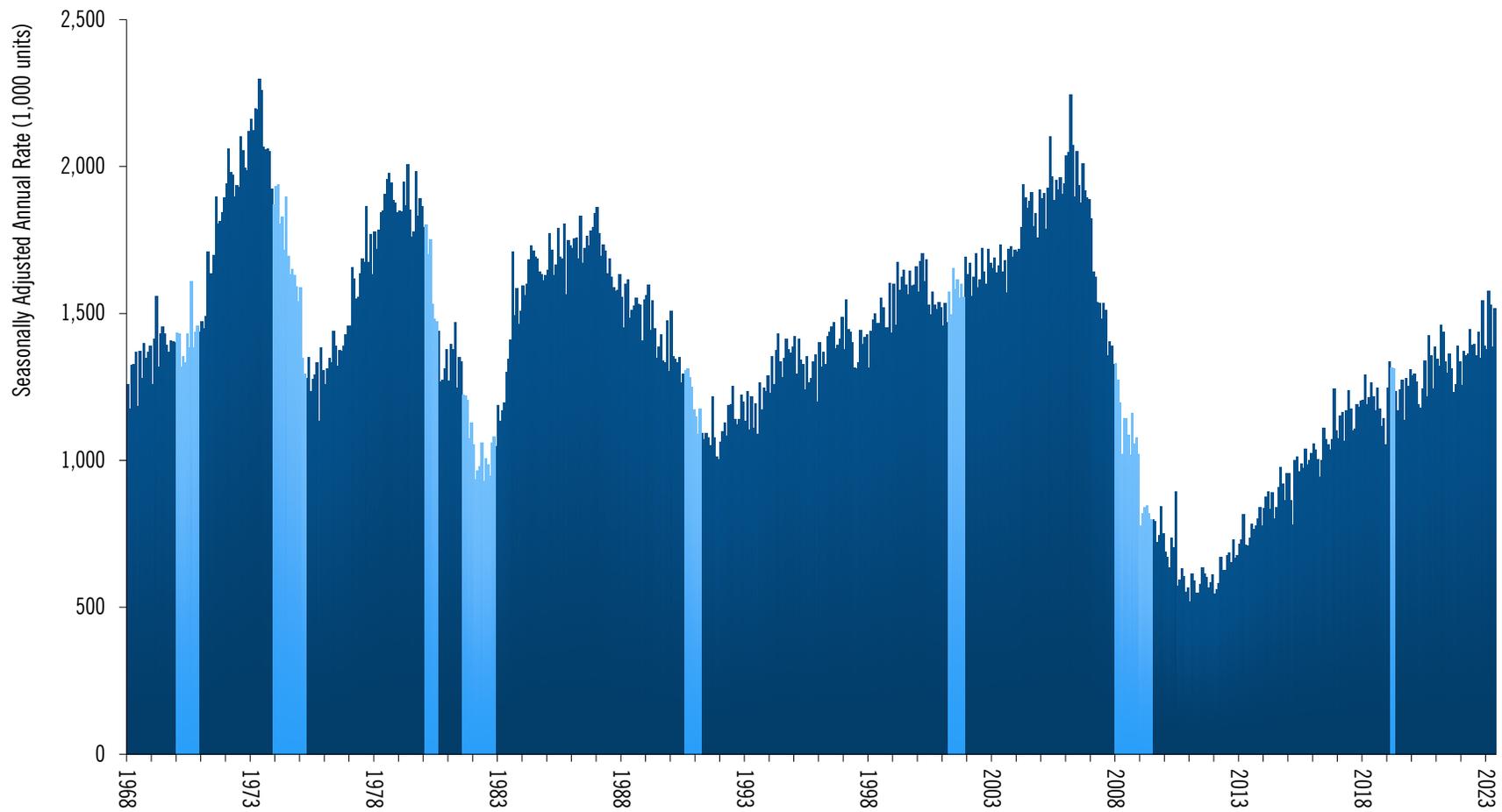
Table 2: Average Annual Housing Unit Production During Economic Expansions; United States; December 1970 through May 2023

Economic Expansion		Average Annual Housing Units Completed
Begin	End	
December 1970	November 1973	1,920,750
April 1975	January 1980	1,627,690
August 1980	July 1981	1,342,833
December 1982	July 1990	1,563,880
April 1991	March 2001	1,365,175
December 2001	December 2007	1,763,890
July 2009	February 2019	878,793
May 2019	May 2023	1,335,694

Source: PlaceWorks, using housing production data from the US Census Bureau's Building Permits Survey and Survey of Construction, and economic expansion/contraction data from the National Bureau for Economic Research.



Figure 6: Monthly Number of Housing Units Completed; United States; January 1968 to May 2023



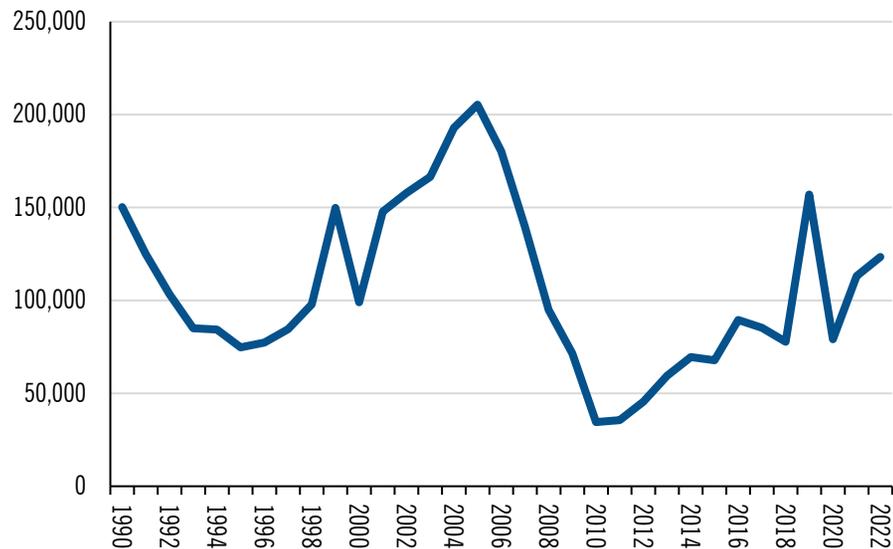
Note: Lighter-shaded areas indicate recessions.

Source: PlaceWorks, 2019, using data from the US Census Bureau.

California Housing Production

It is a similar story in California, as shown in Figure 7. The average number of housing units constructed per year from 1990 to the 2008/09 recession was 128,300. Between that recession and the onset of the COVID-19 pandemic, the number of housing units constructed averaged only 72,600 per year, or 43 percent fewer. The market rebounded somewhat since then, averaging 118,100 units per year. Nevertheless, without the slowdown following the 2008/09 recession, the state would have an additional 669,000 housing units, or 4.5 percent more than there are today.

Figure 7: Net Annual Increase in the Total Number of Housing Units Housing; California; 1990 to 2023



Source: PlaceWorks, 2024, using data from the CA Department of Finance.

Housing Unit Size

The size of housing units, both single-family detached and multifamily, have been increasing over time. Figure 8 shows the average unit size for each year, from 1971 to 2022.

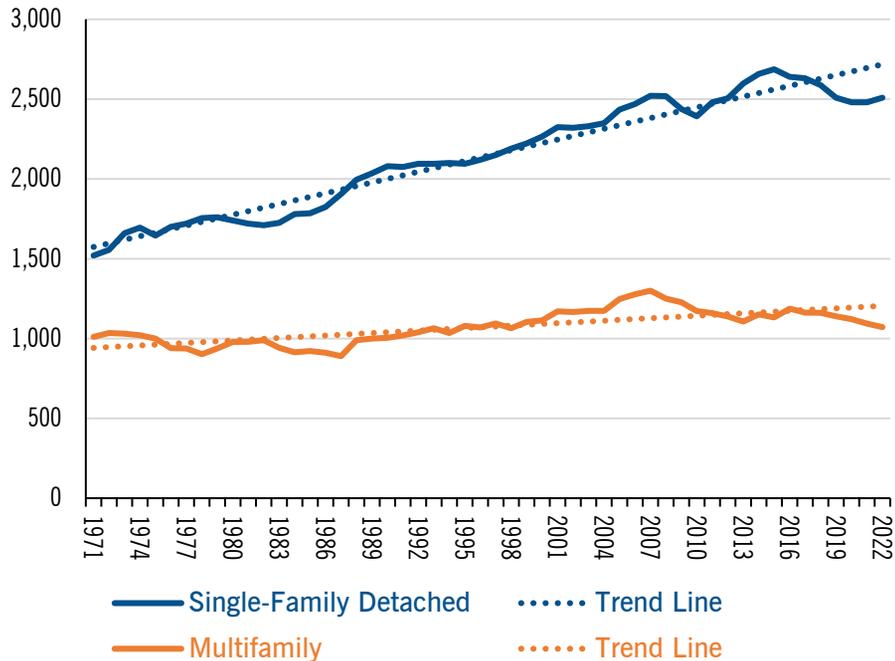
The size of the average single-family housing unit has increased 77 percent, growing from 1,520 square feet in 1971 to a high of 2,687 square feet in 2015, before declining slightly to 2,509 in 2022. Over the past four and a half decades, the average house increased in size by about 25 square feet per year.

In contrast, the average unit size across multifamily housing units increased over this period by 29 percent, growing from 1,011 square feet in 1971 to a high of 1,300 square feet in 2007, or an increase of 8 square feet per year. The average unit size declined to 1,162 square feet in 2017.

Starting in 1999, the Census Bureau began reporting multifamily unit size for units intended for rental and those intended for-sale. Since then, the average size of multifamily units intended for rental increased by 80 square feet, or 7.6 percent, to 1,130 square feet, which is only 119 square feet larger than the average size for all new multifamily units in 1971. In contrast, the average size of new multifamily units intended for sale, increased by 265 square feet, or 19 percent, from 1,360 square feet in 1999 to 1,625 square feet in 2017.



Figure 8: Average Unit Size for Single-family Detached Housing and Multifamily Housing Completions, Actual and Trend; United States; 1971 through 2022



Source: PlaceWorks, 2024, using data from the US Census Bureau.

Sales Price for New Single-family Houses

Over time, the sales price for new single-family housing has increased, even when adjusted for inflation. Figure 9 illustrates the inflation-adjusted sales price and sales price per square foot increase between 1974 and 2022. From 1974

to 2022, the real (inflation-adjusted) average sales price increased about \$6,350 per year. However, much of that increase results from the high inflation of the past few years; from 1971 to 2019, the average increase was \$4,450. The average price of a new single family housing unit in the US in 2022 was \$530,000, compared to the inflation-adjusted price of \$231,00 in 1974 (unadjusted value of \$38,000) and \$432,000 in 2019 (unadjusted value of \$373,000). How did the price for new single-family housing increase so much? In large part, the price increase is a direct result of the market producing larger housing units.

The average sales price increased from \$148.42 per square foot (in inflation-adjusted 2022 dollars) in 1974 to \$211.12 per square foot in 2022. And again, this is partially affected by the high inflation of the past few years. The average sales price per square foot in 2019 was \$172.00 per square foot, in 2022 dollars.

From 1974 to 2022, the average inflation-adjusted price of a new single-family housing unit increased 86.7 percent, but the cost per square foot only increased 22.4 percent. Roughly three-fourths of the inflation-adjusted increase housing cost was a matter of building larger housing units.

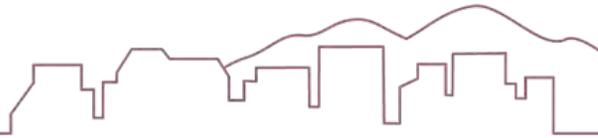
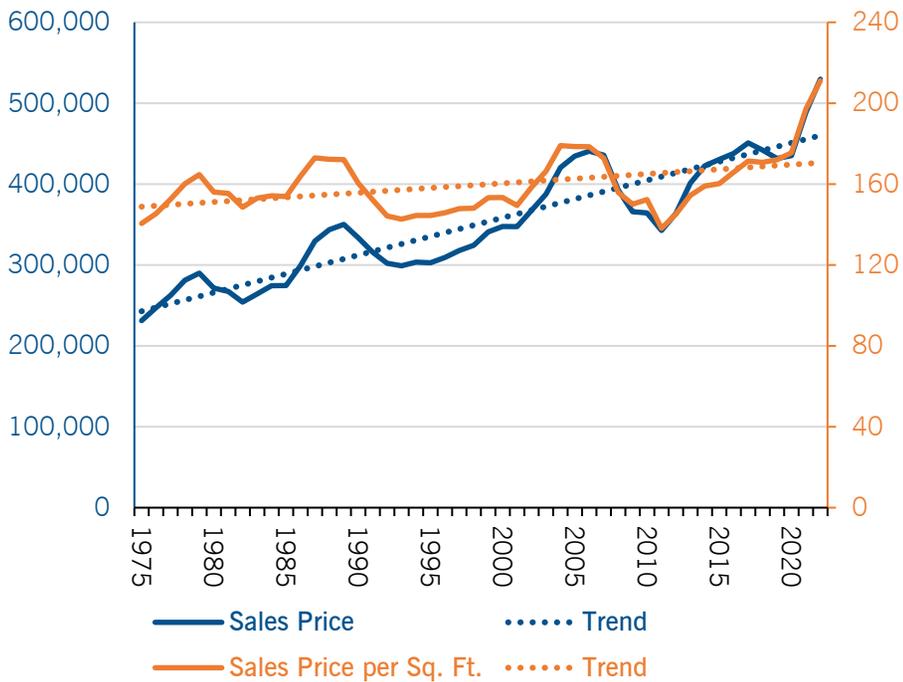


Figure 9: Real Average Sales Price and Real Average Sales Price per Square Foot for New Single-family Housing; United States; 1971 to 2022



Source: PlaceWorks, 2024, using sales price and floor area data from the US Census Bureau's Characteristics of New Housing and the consumer price index for all urban consumers data from the US Bureau of Labor Statistics.

IMPLICATIONS OF LONG-TERM NATIONAL TRENDS

The trends discussed in this chapter have implications for housing supply and demand in general and for housing production in Southwest Riverside County and Menifee.

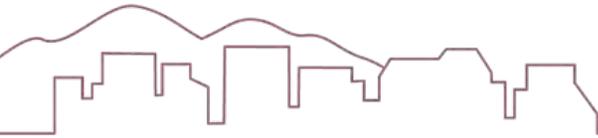
Generational Waves

The large number of people born between 1945 and 1964, the Baby Boomers, are in or entering retirement. Home ownership rates are highest among this group. Over time, however, as they age, a portion of them can be expected to trade in their single-family housing for smaller housing, senior condos, or assisted living homes, thus increasing the supply of existing housing for sale.

The next large wave of population, the Millennials, were born, roughly, between 1990 and 2000. Many of those in this wave are well into the home-buying stage of life or about ready to enter those ages. With many Baby Boomers still living in their homes, this next wave of homebuyers is pushing the market and, in part, helping to support or drive up the cost of housing because the market has underbuilt housing since the 2008/09 recession.

Mismatch Between Household Living Arrangements and Housing Production

Since at least the 1970s, Americans have waited longer to marry and have children, fewer and fewer households even have children, more people live alone and in two-person households, and the average household size has declined. However, the housing market has continued to produce predominantly single-family detached housing and has continued to build larger and larger houses. Perhaps one- and two-person households would continue to choose to live in larger single-family housing, but the data suggests that the growing



number of small households has less and less of an opportunity to choose smaller new housing units, especially in the ownership market.

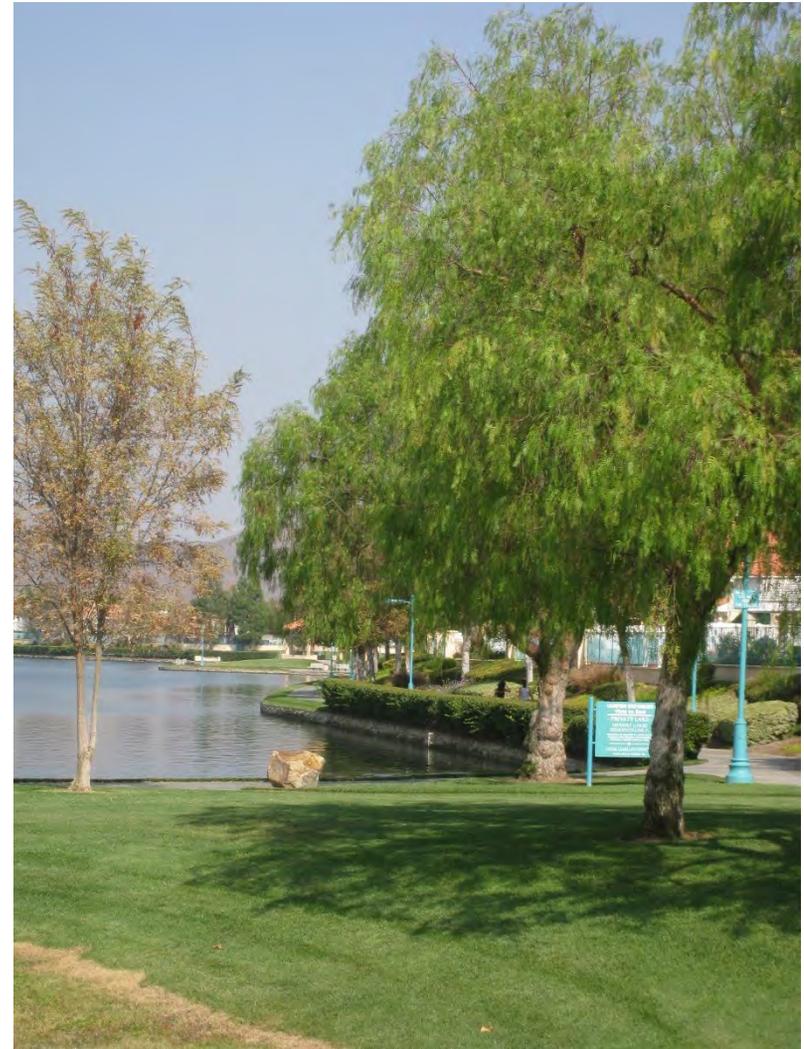
Housing Market Not Producing Enough Housing

The 2008/09 recession decimated the housing industry, and it has only just in the last year returned to the average level of housing production from 1968 to the March 2006 peak. In the previous economic expansion, the economy produced almost twice as many units per year as it has in this expansion.

The underbuilding of housing during and since the 2008/09 recession is a national challenge, although some areas and regions have fared better than others. It is also a California problem. The current challenges with high interest rates, lack of a sufficient labor force, and supply chain shortcomings still hamper the housing industry. Boosting housing production in Menifee may be limited by these national and regional housing industry constraints.

Larger Housing Units Increase Housing Costs

Much of the long-term growth in inflation-adjusted prices for single-family housing correlates with the long-term increase in unit sizes. This would suggest that one approach to encouraging the development of more moderately priced housing would be to facilitate the construction of smaller-size housing units. However, this is easier said than done. The financial incentive to the developer is to construct larger units to the degree that market demand will support such development. Furthermore, as costs for land, increased development standards, infrastructure and development fees increase, the financial incentive to the developer is to build larger, more expensive units, again, to the degree that the market will bear.



4. Menifee Housing Market

MARKET AREA ANALYSIS

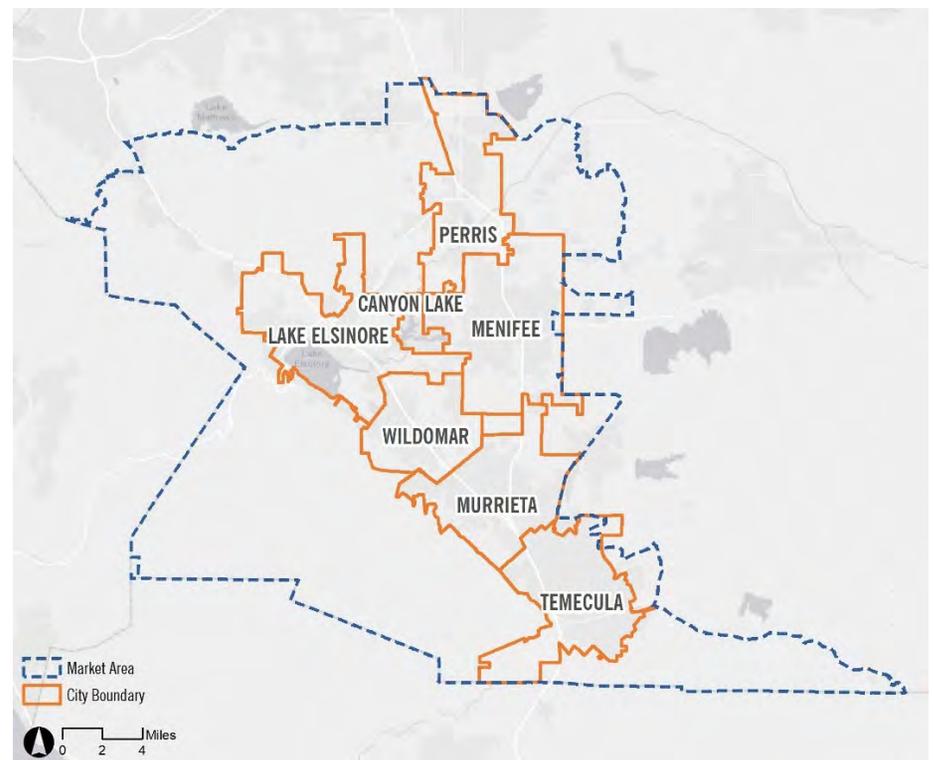
There are unique characteristics that influence the housing market in one city versus another, and even in one neighborhood versus another. However, the housing market is truly a regional market. Regions with growing economies are better able to retain existing residents and attract migrants from other regions, if not other nations. Conversely, regions with stagnant or declining economies find it challenging to retain existing residents, let alone attract migrants. The local housing market is a function of overall regional growth or stagnation or decline.

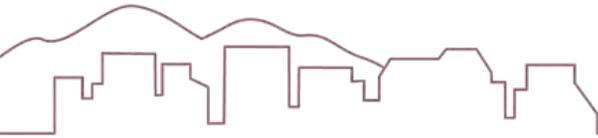
This chapter examines various factors that influence the demand for housing in Southwest Riverside County and in Menifee. The housing market area used in the first half of this analysis consists of the US Census Bureau boundary that includes the seven cities along the I-15 and I-215 corridors in southwest Riverside County: Canyon Lake, Lake Elsinore, Menifee, Murrieta, Perris, Temecula, and Wildomar; as shown in Figure 10. There is a rich amount of data available for this Census Bureau boundary, especially regarding detailed household income, occupancy characteristics, and length of tenure at current residence. In addition, a smaller market subarea is used in the second half of this analysis, and it includes only Menifee, Murrieta, Perris, and Temecula.

This chapter describes the characteristics of households in Western Riverside County. It compares households earning a moderate income or less, defined as less than 120 percent of the area median income, to households earning an above moderate income, defined as 120 percent or more of the area median income. Households earning a moderate income or less are faced with realities

not experienced by those earning an above moderate income, which manifest in housing choice and household demographics.

Figure 10: Market Area Extent



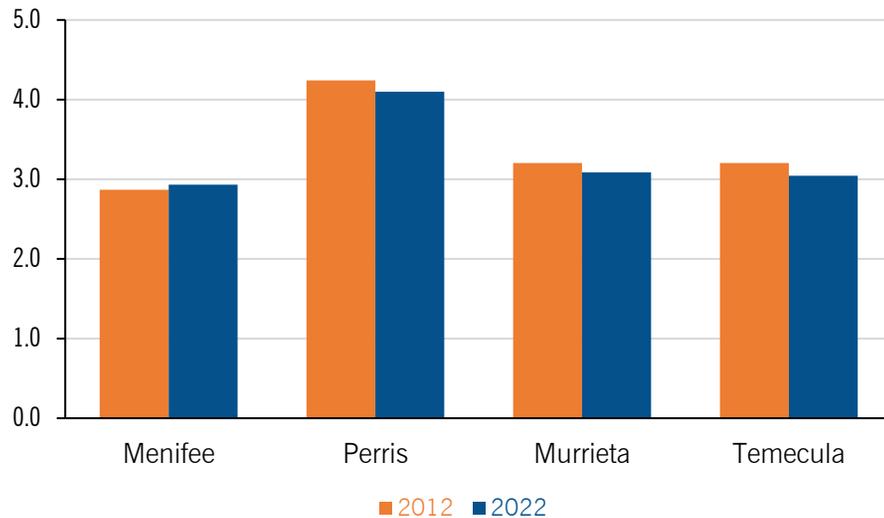


HOUSEHOLD CHARACTERISTICS

Household Size

Menifee has the smallest average household size when compared to other cities in the market area based on California Department of Finance Data, as shown in Figure 11. Between 2012 and 2022, only Menifee experienced a marginal increase in average household size, rising from 2.87 to 2.9, while average household sizes in neighboring jurisdictions decreased.

Figure 11: Average Household Size; Market Area Cities; 2012 and 2022



Source: PlaceWorks, 2024, using data from the California Department of Finance, Table E-5.

Census Bureau data indicates that the increase was largely fueled by growth in owner-occupied units, which increased from 2.87 to 3.14 persons per household between 2012 and 2021 (the most recent Census Bureau data available). Renter-occupied households contributed a lesser amount, increasing slightly, from 3.0 to 3.05 persons per household, during the same period.

Household Size and Household Income

Throughout the market area, households earning an above moderate-income have a higher average household size compared to households earning a moderate income or less. The percentage of households that have only one person accounts for most but not all of the differences in average household size across the income categories. Approximately 24 percent of households earning a moderate-income or less are comprised of a single individual, compared to only 6 percent of above moderate-income households. The percentage of two- and three- person households is comparable across both income categories; however, the percentage of four-person and larger households earning above moderate income (50 percent) is noticeably larger than comparably sized households earning a moderate income or less (31 percent).

Table 3 summarizes household size data for middle-income households. Figure 12 shows the percentage of each income category's households by the number of persons per household. Three or fewer person households account for 69 percent of households earning a moderate income or less, and 85 percent of households are made up of four or fewer persons. This suggests that the vast majority of the market area's housing needs can be accommodated with housing units with three or fewer bedrooms. Furthermore, housing units with two or fewer bedrooms should accommodate the majority of households with three or fewer people.

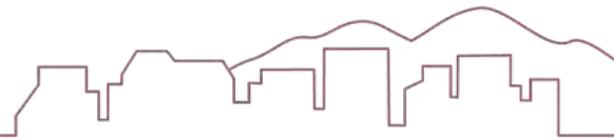
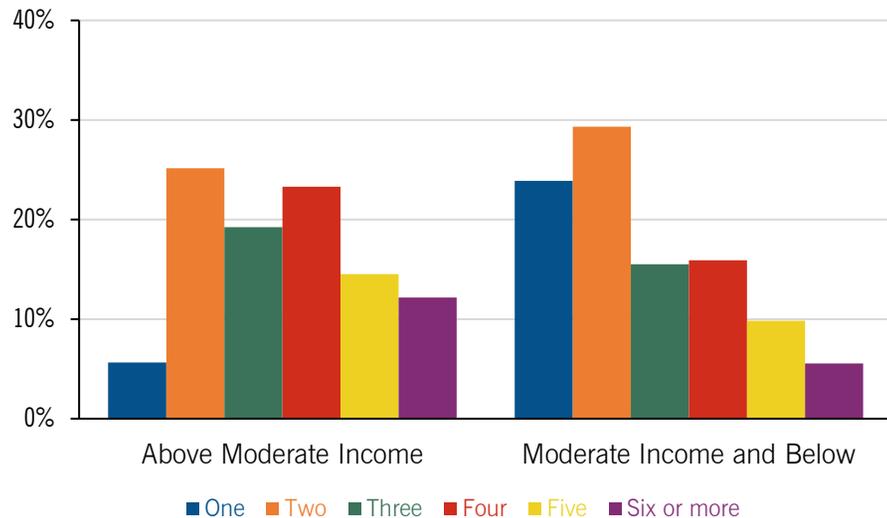


Table 3: Household Size by Income Category; Market Area; 2021

	Above Moderate Income	Moderate Income and Below
Average Household Size	3.6	2.8
One-person households	5.6%	23.9%
Two-person households	25.2%	29.3%
Three-person households	19.2%	15.5%
Four-person households	23.3%	15.9%

Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set.

Figure 12: Percentage of Income-Category Households by Number of Persons per Household; Market Area; 2021



Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set.

Household Type

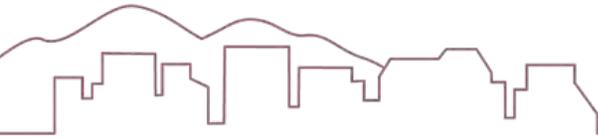
Household type varies by household income. Table 4 provides data on household type by income category for the market area.

Households across both income categories are more likely to be married-couple families, and more likely to have no children at home. As stated under the household size discussion above, approximately one-quarter of households earning a moderate income or less are individuals living alone. Regardless of household type, the majority of households in each category do not have children living at home. Above moderate-income households are less likely to be single-parent households, and single heads of household are more likely to not have children at home than to have children at home.

Table 4: Household Type and Presence of Children under the Age of 18 by Income Category; Market Area; 2021

	Above Moderate Income	Moderate Income and Below
Living alone	5.6%	23.9%
Married couple w/o children at home	38.6%	26.7%
Married couple with children at home	36.9%	23.3%
Other household w/o children at home	13.0%	14.4%
Other household with children at home	2.5%	3.0%
Single parent with children at home	3.3%	8.7%
All households with children at home	42.8%	35.0%
All households w/o children at home	57.2%	65.0%

Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set



Multigenerational Households

The US Census Bureau defines a multigenerational household as a household with two or more adult generations. Although demographers often include grandparents raising grandchildren, these households are not included in the Census Bureau data. Table 5 provides multigenerational household data for the market area.

The Pew Research Center published a 2018 report that noted that the national population living in multigenerational households decreased from 21 percent in 1950 to 12 percent in 1980, and it has steadily increased since then, reaching 20 percent in 2016. Multigenerational households are not as common in the market area compared to national trends. Nevertheless, approximately 10 percent of above moderate-income households are multigenerational, and 5 percent of households earning a moderate income or less are multigenerational.

Table 5: Multigenerational Households as a Share of Total Households and Share of Population by Income Category; Market Area; 2021

	Above Moderate Income	Moderate Income and Below
Percent of Households	9.8%	4.8%
Percent of Household Population	16.0%	10.0%

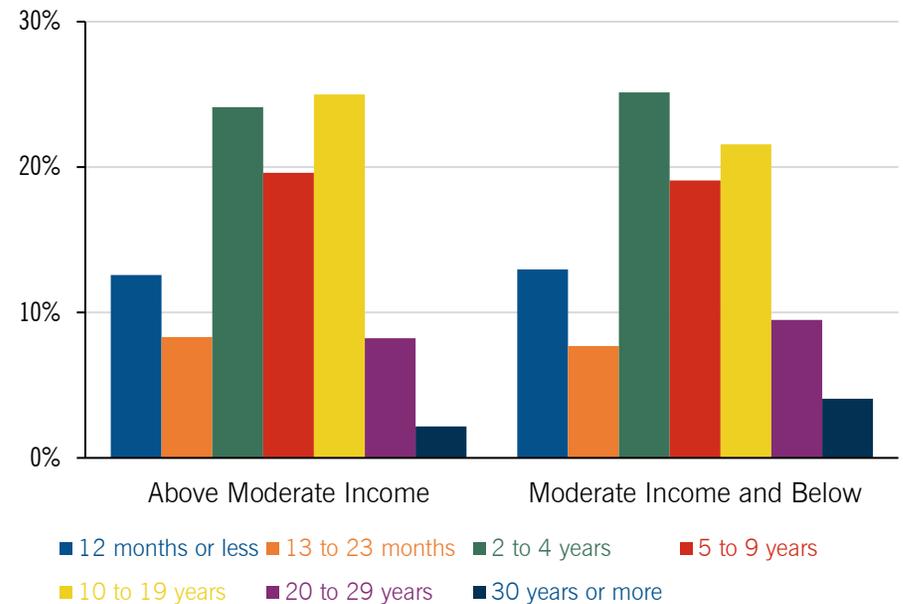
Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set

Length Of Time at Current Residence

How long the typical household has lived at its current residence is typically correlated with household income. Generally, the higher the household income, the longer the household has lived at the current home.

For households in the market area, however, residency lengths are comparable across both income categories, with 65 percent of households in both categories having occupied their current residence for less than 10 years. Figure 13 shows the length of time households have resided at their current residence.

Figure 13: Length of Time at Current Residence by Income Category; Market Area; 2021



Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set

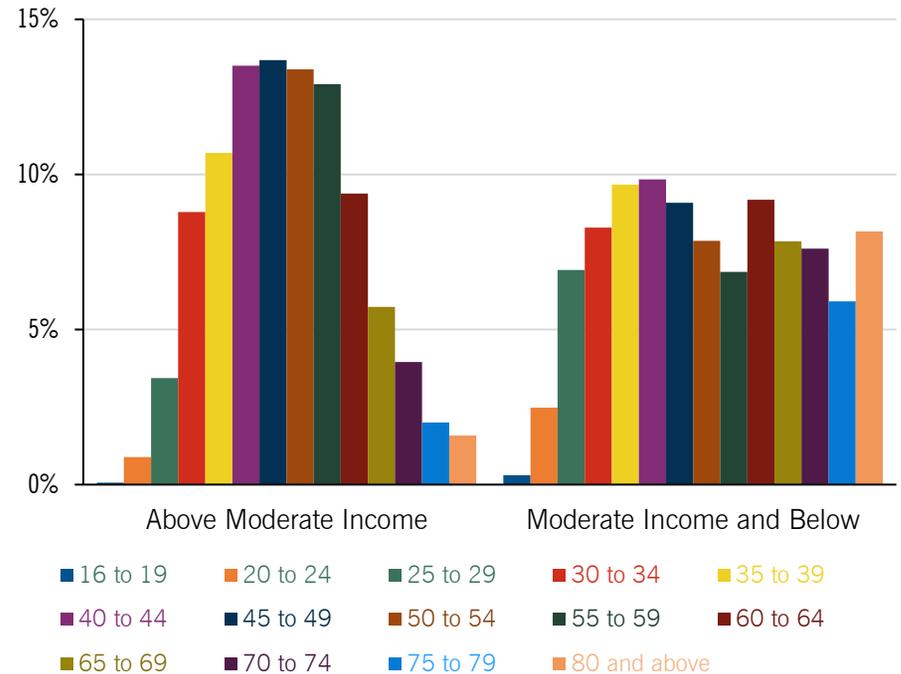
Age Of Householder

The average age of householders varies slightly between the income categories: 50 years old for above moderate-income households and 52 years old for households earning a moderate income or less. However, there are large variations across income categories when looking at age cohorts. Figure 14 shows the age distribution for householders by income categories.

The age distribution for households earning above moderate income is representative of a bell curve, with the median shifted slightly left. The four largest cohorts are householders between the ages of 40 to 44, 45 to 49, 50 to 54, and 55 to 59, which logically tracks prime earning years.

For households earning a moderate income or less, the average householder age skews slightly higher. The respective share for cohorts with a householder aged 35 years or older is fairly consistent, which suggests that new housing targeting households earning a moderate income or less will need to accommodate various stages of life, particularly empty-nesters and retirees.

Figure 14: Age Distribution of Householders by Income Category; Market Area; 2021



Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set

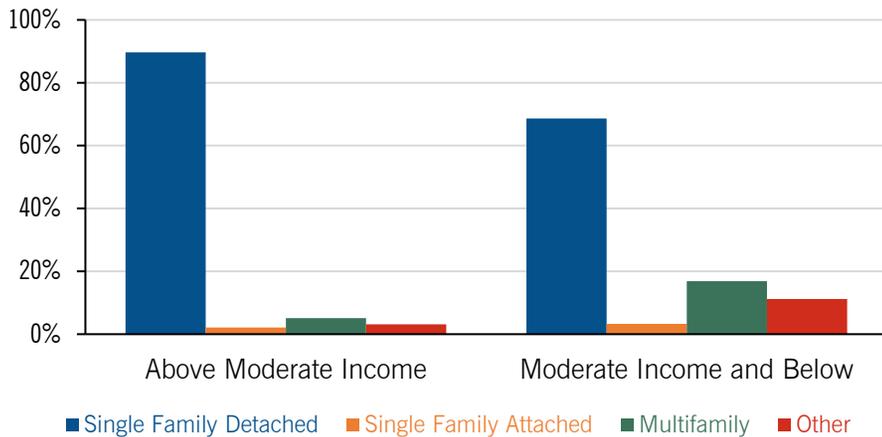
HOUSING CHARACTERISTICS

Type Of Housing

Single-family detached dwellings are the most prevalent form of housing in the market area and the Western Riverside County region (56 percent). Occupancy of a single-family dwelling is correlated with income. Figure 15 shows the data on housing type by income category.

In the market area, approximately 90 percent of households earning above moderate income live in a single-family detached dwelling. This figure drops to 69 percent for households earning a moderate income or less, with more households occupying single-family attached, multifamily units, and other dwelling types.

Figure 15: Percentage of Households by Income Category and by Type of Housing; Market Area; 2021

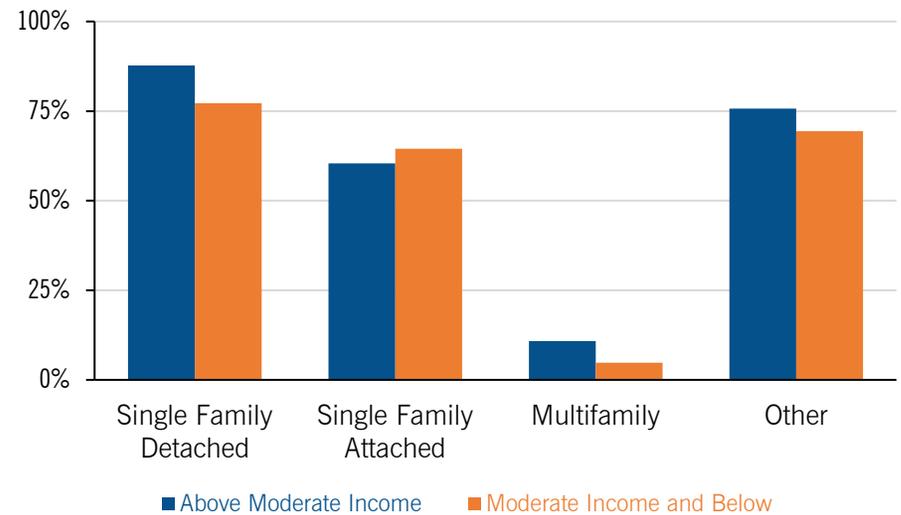


Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set.

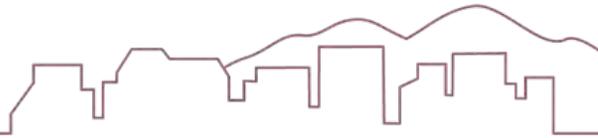
Tenure

Housing tenure describes whether a housing unit is occupied by the owner or by a renter and, much like the type of housing unit occupied, is generally correlated with household income. Figure 16 shows ownership rates across product types by income category. Across the board, the majority of households residing in single-family attached and detached housing are homeowners. The rate of ownership is similarly high for households living in “Other” housing types, which include mobile homes and park model units. The vast majority of households living in multifamily housing are renters; however, some households do own and occupy multifamily units in condominium developments.

Figure 16: Homeownership Rate by Housing Unit Type and Income Category; Market Area; 2021



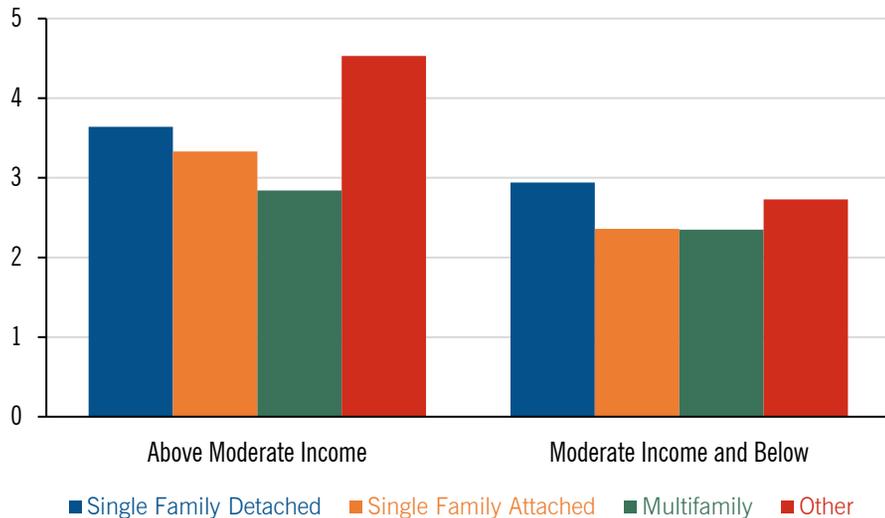
Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set.



Household Size

The average household size for each type of housing increases with income. For above moderate-income households, household size decreases slightly from 3.6 for households residing in single-family detached housing, to 3.3 for single-family attached housing, to 2.8 for multifamily housing. Average household size for households earning a moderate income or less is more consistent, decreasing slightly from 2.9 for single-family detached housing to approximately 2.4 for single family attached and multifamily units. Figure 17 shows the average household size data.

Figure 17: Average Household Size by Housing Type and Income Category; Market Area; 2021

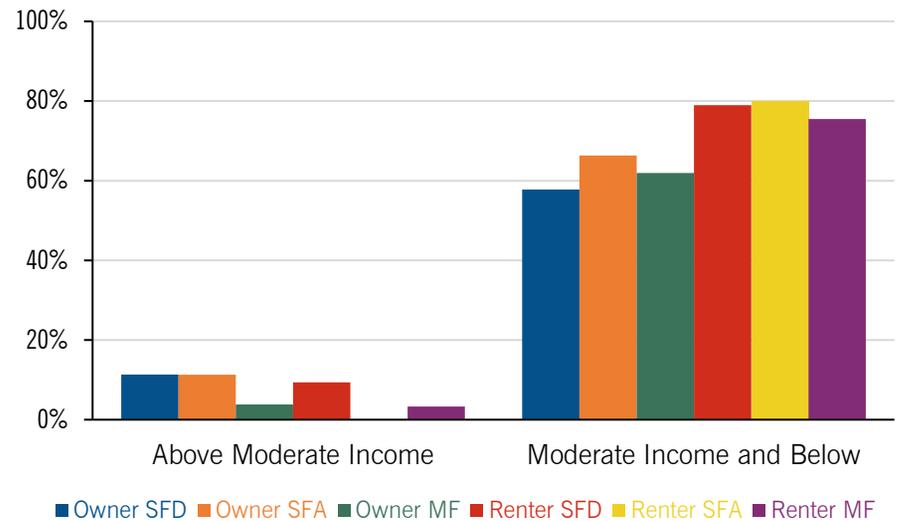


Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set.

Housing Overpayment

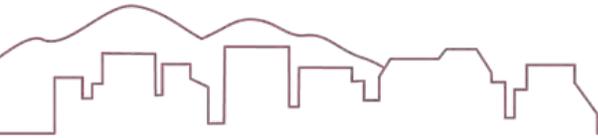
Housing overpayment represents households that pay more than 30 percent of their household income for housing costs. For renters, housing cost includes rent and utilities, commonly referred to as gross rent. For owners, housing cost includes mortgage payments, PMI and property, insurance, taxes, and CFD/HOA fees. Figure 18 shows housing overpayment in the market area.

Figure 18: Housing Overpayment by Housing Unit Type, Tenure, and Income Category; Market Area; 2021



Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set.

Few above moderate-income households experience housing overpayment, whereas the majority of households earning a moderate income or less



experience housing overpayment. Across the three most prevalent housing unit types—single-family detached, single-family attached, and multifamily—renter households earning a moderate income or less experience housing overpayment at a higher rate than owner households in the same income bracket.

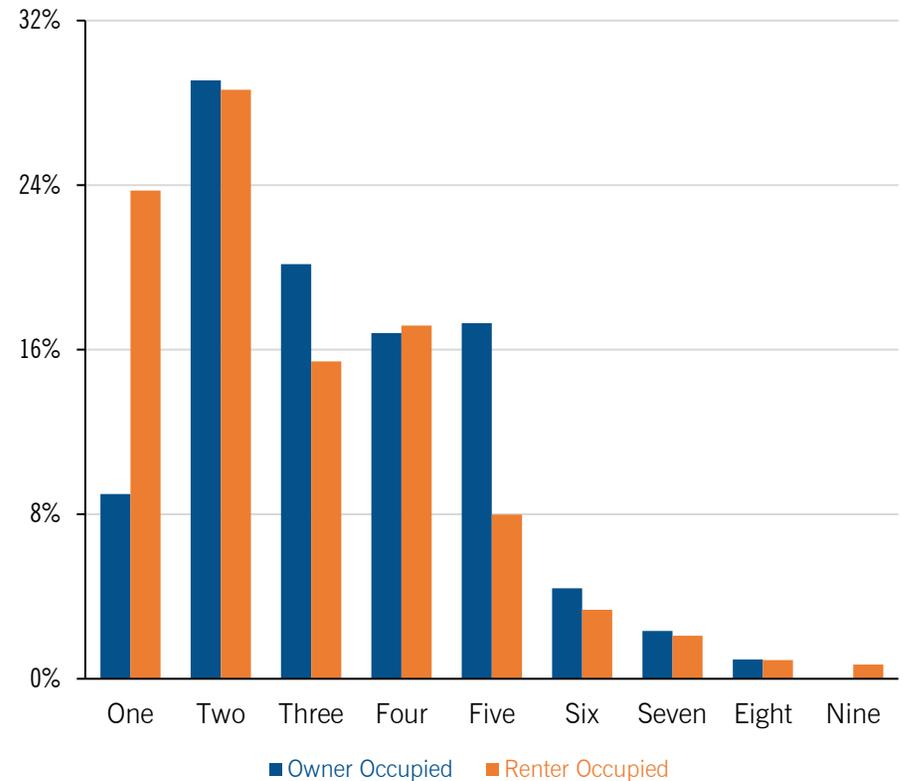
CHARACTERISTICS OF HOUSEHOLDS THAT MOVED TO THE MARKET AREA IN THE PRIOR YEAR

An important question is whether the characteristics of those moving into the market area in the past year are similar to the characteristics of those who were already living here: the question being, who is moving here? Approximately 57 percent purchased a home, while the remaining 43 percent moved into for-rent products. This section highlights relevant socioeconomic characteristics for the owner and renter households.

Household Size

Owner-occupied households that moved into the market area in the prior year, averaged 3.3 persons per household. Renter-occupied households were not far behind at 2.8 persons per household. Figure 19 shows the proportion of households by number of people for both owner- and renter-occupied units. For both tenure types, two person households are the most prevalent. Owner-occupied units have a higher proportion of households with three or more people, although renter households do not trail far behind. However, a noticeably higher proportion of renter households consist of only one person, which is reflected in the smaller average household size.

Figure 19: Tenure by Number of Persons in a Household; Market Area; 2021

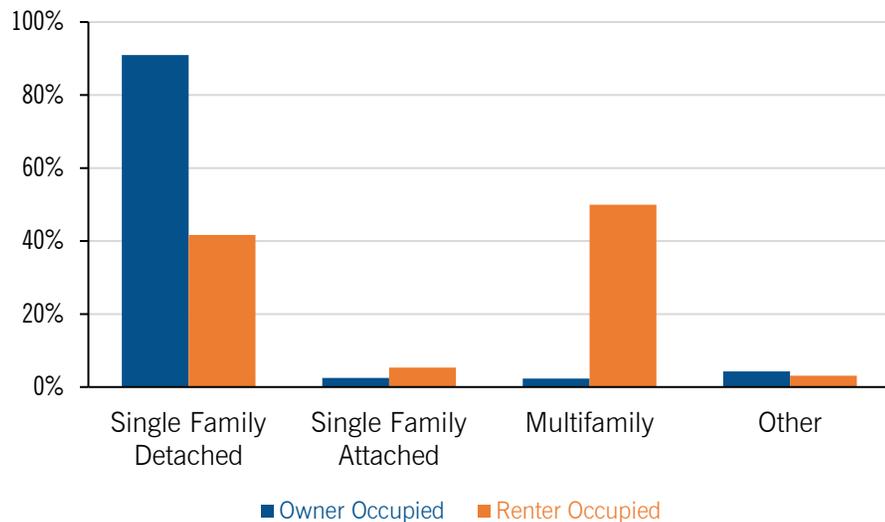


Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set

Housing Type

Approximately 91 percent of households that recently bought a home in the market area purchased a single-family detached unit. Renter households were split between single-family detached and multifamily units at 42 percent and 50 percent of households, respectively. Single-family attached units and mobile homes were the least popular categories, combining for less than 10 percent of both owner- and renter-occupied units. Figure 20 illustrates the proportion of housing types by tenure.

Figure 20: Tenure by Housing Unit Type; Market Area; 2021

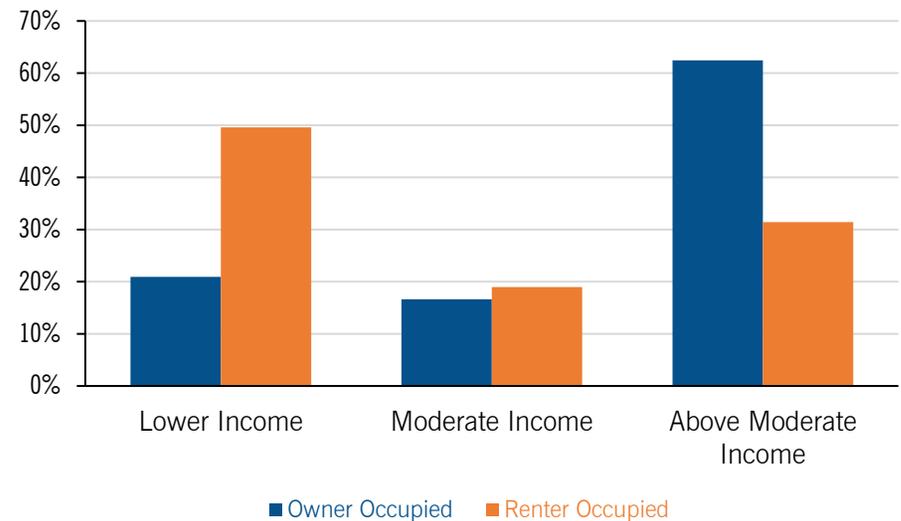


Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set

Household Income

In the prior year, approximately 63 percent of households that purchased a home in the market area earn an above moderate income (more than 120 percent of the area median income). By comparison, approximately 31 percent of renter households that recently moved to the market area earn an above moderate income. A comparable proportion of owner and renter households earn a moderate income (80 to 120 percent of the area median income), but a larger proportion of renter households qualify as lower income (less than 80 percent of the area median income). Figure 21 shows the proportion of households broken down by income category and tenure.

Figure 21: Tenure by Household Income Category; Market Area; 2021



Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 Public Use Microdata Set

CITY-LEVEL CHANGES

Housing Type

From 2012 to 2022, according to data from the California Department of Finance, the number of housing units in the major market area cities increased by 20,645, growing 1.4 percent per year on average. Single-family detached housing accounted for 77.9 percent of that growth; single-family attached housing accounted for 3.7 percent; and multifamily provided the remaining 18.5 percent. In contrast, the comparable data for the county as a whole were: single-family detached, 82.5 percent; single-family attached 2.4 percent; and multifamily 15.1 percent.

There are differences among cities in the types of housing that were developed in this period. In Menifee, single-family housing accounted for 98 percent of new housing constructed, higher than all neighboring market area jurisdictions, except Canyon Lakes.

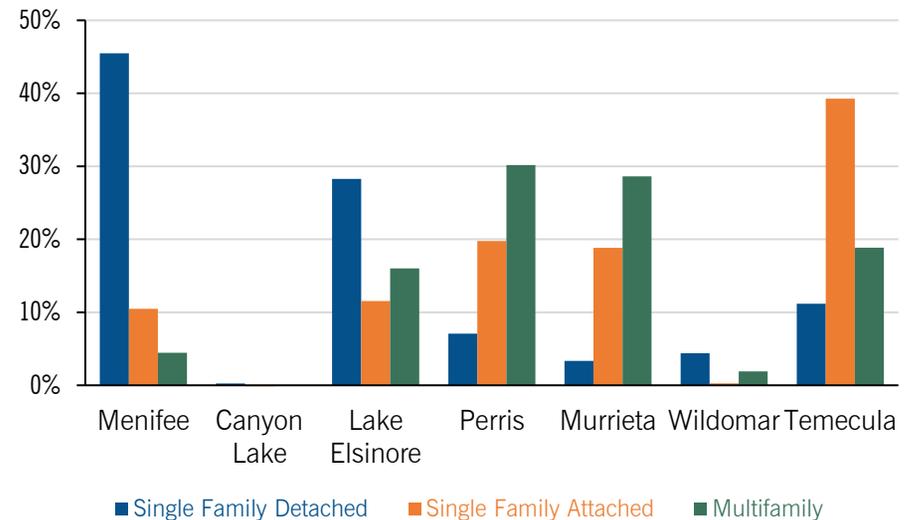
Menifee accounted for 36.6 percent of all market area housing growth. More specifically, it accounted for 45.5 percent of the single-family detached housing growth, 10.5 percent of single-family attached housing growth, and 4.5 percent of the multifamily housing growth. In absolute numbers, Menifee provided 79 single-family attached dwellings, 7,312 single-family detached dwellings, and 170 multifamily units. The data in Figure 22 suggests that Temecula is a single-family-attached housing powerhouse, but there were only 754 units of single-family attached housing developed in the market area during between 2012 and 2022.

Average Household Size

From 2012 to 2022, the average household size decreased slightly in all market area cities, except for Menifee, which remained constant at 2.9 persons.

Temecula experienced the largest decrease, 5 percent during the period. Nevertheless, Menifee's average household size remains smaller than neighboring major market area cities Murrieta, Perris, and Temecula.

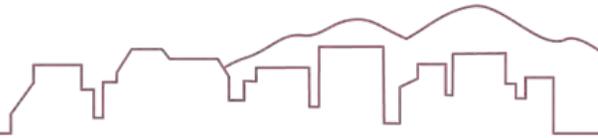
Figure 22: Share of Each Market-Area City Housing Growth by Type of Housing; Market Area Cities; 2012 to 2022



Source: PlaceWorks, 2024, using data from the California Department of Finance, Table E-5.

Overcrowding

Occupancy by more than one person per room is used as a general proxy for overcrowding. Between 2012 and 2021, the proportion of Menifee households that were overcrowded decreased from 4.3 percent to 3.5 percent. As a whole,

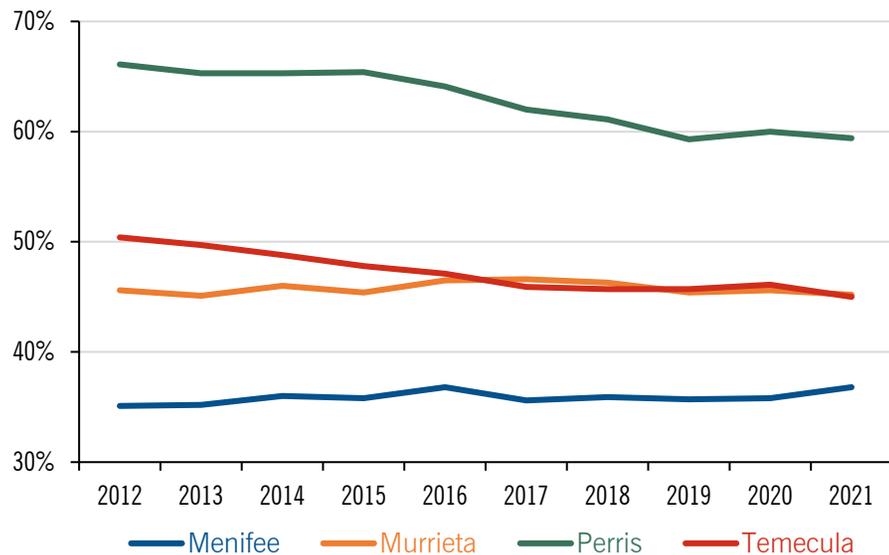


the proportion of overcrowded households in the market area cities increased slightly from 5.2 percent to 6.2 percent.

Households With Children

Between 2012 and 2021, the total number of Menifee households with children increased by 27 percent, and the number of households without children increased by 18 percent. Thus, the share of households with children increased only from 35.1 to 36.8 percent.

Figure 23: Percentage of Households with Children under the Age of 18; Market Area Cities; 2012 to 2021



Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 American Community Survey 5-Year Estimates.

By contrast, other cities in the market area saw a decrease in the proportion of households with children, largely due to greater growth in households without children. Only Temecula recorded a net loss of total household with children during the same period. Figure 23 shows the trend in percentage of households with children for each city.

Household Type

The majority of households, 51.5 percent, in Menifee in 2021 were one- and two-person households, a decrease from 57.5 percent in 2012. Figure 24 shows the percentage of three- or more person households in each of the cities in 2012 and 2021. Compared to other jurisdictions in the market area, Menifee has the lowest proportion of 3 or more person households; however, the recent influx of families with children suggests that may change. Murrieta and Perris experienced a slight increase in the proportion of 3 or more person households, while Temecula experienced a slight decline.

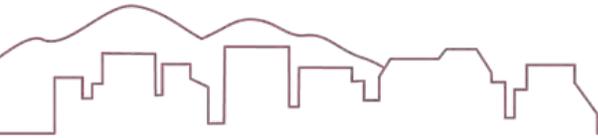
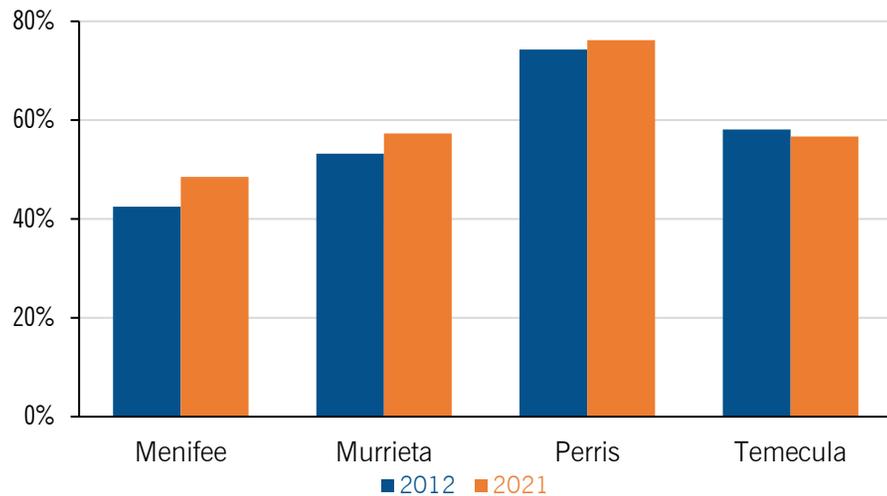


Figure 24: Three or More Person Households as a Share of Total Households; Market Area Cities; 2012 and 2021



Source: PlaceWorks, 2024, using data from the US Census Bureau, 2021 American Community Survey 5-Year Estimates

STAKEHOLDER INTERVIEWS

In preparing this report, the consultants interviewed a number of stakeholders about their perceptions of the housing market, market demand, and increasing housing production. The key issues and concerns raised in these interviews is summarized below.

Market Rate Housing Development

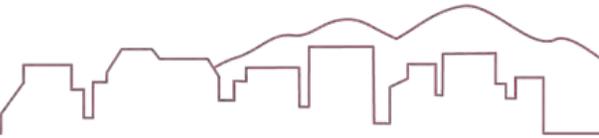
The market is geared towards single-family housing. It does not appear that higher density housing is necessarily financially feasible in Menifee currently. As discussed previously, there is a growing need in the market area for smaller housing units and multifamily housing. However, multifamily developers are investing in gateway areas that are more developed than Menifee and where the developers are more confident that they can charge rents that will make development financially feasible. Nevertheless, there appears to be consensus that it is just a matter of time before more investment in multifamily housing starts to flow to Menifee.

It was also noted that the pandemic has drawn more people to live in the suburbs and is changing some of the residential markets throughout Southern California.

The largest segment of the market demand for new housing is 28- to 45-year-olds, typically families with 1 to 3 children. These are often upwardly mobile families relocating to Menifee for a nicer home, at a good value.

Current market conditions are a bit of an unknown, between rising interest rates and tighter bank lending standards to continuing challenges with supply chains. Developers also noted some challenges with securing funding because banks are lending less than before. Nevertheless, developers are still seeing strong demand for housing, even with rising mortgage rates.

The developers interviewed were generally very complimentary of Menifee's staff and development processing, noting that it was less problematic than in other cities. Nevertheless, they did indicate that there could be improvements in permit tracking and review timelines. There was discussion about the mixed-



use zoning as well as design requirements and development standards, specifically challenges and limitations to multifamily housing development in the Economic Development Corridors.

Affordable Housing Development

Interviewed stakeholders noted that the gap between affordable rent and market rent is growing, and the demand for affordable housing is ever present. Low-income housing tax credits (LIHTCs) remain the key subsidy for developing affordable housing, but LIHTC funds are highly competitive. Many of the remaining funding sources are set up for specific populations (homeless, veteran, etc.), or preclude certain households, such as those with 2 earners.

Several stakeholders also noted the market-rate developers are not always set up to manage affordable inventory. Even though that can and do use non-profit partners to manage affordable housing in mixed-income developments, this can be, at times, inefficient as managers must work over many small, scattered sites. It was suggested that market-rate developers might prefer an alternative for in-lieu fees. The city could use in-lieu funds to support an affordable housing project. In addition, cities can partner with affordable housing developers to find and secure land for affordable housing projects.

Lending Providers

Assisting low- and moderate-income households to move into home ownership has its own unique set of challenges. Downpayment assistance through Neighborhood Partnership Housing Services (NPHS), which contributes up to \$100,000, has so far only been successful in desert communities. In June 2023, Menifee City Council increased the city's maximum down payment assistance to \$100,000.

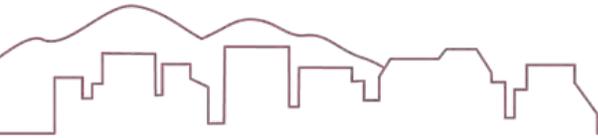
Many low-income households only qualify for mortgages for homes less than \$365k, which are scarce in the area, and increasing interest rates will likely reduce that amount further. A potential inclusionary ordinance could have a positive impact on the gap for principal reduction and closing costs such as downpayments. Conventional lenders approve mortgages for subsidized ownership, but subsidies must meet an institution's investment criteria and deals must be structured appropriately throughout the entire process.

During the interview, two successful programs were mentioned:

- + City of Riverside, a 34-unit subdivision with 7 guaranteed affordable units. The city sold land to National Core (affordable housing developer) and provided downpayment assistance, and when market rates rose, NPHS and National Core worked together on additional funding.
- + City of Dana Point land trust model. This model maintains affordability but does not build equity.

Real Estate Brokers

Real estate brokers characterized the most common purchaser of new and existing houses as young families with children from Los Angeles, Orange, and San Diego counties. In addition, they are seeing Baby Boomers following adult children and grandchildren to the area. Residential investment by foreign nationals, which is prevalent in some parts of Southern California, is not a meaningful segment of the market in Menifee. They characterized the most common sellers as long-time homeowners selling due to a life event(s). However, they are also noticing retirees getting priced out of the market.



The brokers discussed several trends in the market. First, Menifee is no longer the “affordable” option. The price gap between Menifee and the Murrieta/Temecula market is closing, and builders are starting to move to the north-east in search of affordable land. Multigenerational housing, whether single structure or ADUs, are becoming increasingly popular. After a short cooldown due to rate hikes, demand has returned, and the resale market supply is slowing, giving new homebuilders an advantage, largely due to lower interest rates compared to resale homes.

MARKET CONDITIONS

For-Sale Housing

Between January 2022 and April 2023, newly constructed single-family homes accounted for almost 95 percent of all transactions, with condominiums making up the remaining 5 percent. For the purposes of this analysis, “new” refers to a dwelling unit constructed in 2021 or 2022 but not recorded on the market until 2022 or 2023.

Single Family Detached Housing

Approximately two thirds of the new construction single-family sales had four or more bedrooms. Four-bedroom homes made up half of all transactions, with three-bedroom homes accounting for approximately 30 percent of the total sales. Homes with five bedrooms were less common, constituting 16 percent of sales, while two-bedroom and six-bedroom homes made up fewer than 3 percent of all new sales combined.

Overall, the average home new home price increased as home size and number of bedrooms increased. The average size of a 2-bedroom home was 1,544 square feet and sold for an average of \$546,000. Three-bedroom homes

averaged 2,170 square feet and sold for an average of \$585,000. Four-bedroom homes averaged 2,419 square feet and sold for an average of \$608,000. Five-bedroom homes averaged 2,948 square feet and sold for an average of \$675,000. Six-bedroom homes averaged 4,124 square feet and sold for an average of \$788,000.

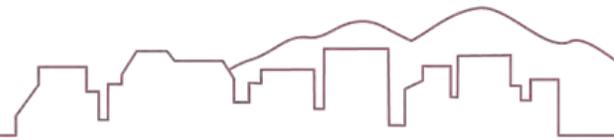
Condominiums

Of the newly constructed condominium sales recorded between January 2022 and April 2023, more than two-thirds were three-bedroom units. The remaining sales were two-bedroom units, averaging 1,396 square feet and a sale price of \$427,000. The more popular three-bedroom units averaged 1,580 square feet and a sale price of \$475,000.

For-Rent Housing

Although the vast majority of Menifee’s housing stock is comprised of single-family detached units, there has been a slight uptick in the development of multifamily for-rent products since the turn of the millennia. Prior to 2000, only 644 apartments were built across six complexes of varying sizes. Between 2000 and 2019, five apartment complexes added 1,072 units, more than doubling the City’s supply. The pace of development appears to be increasing, as two new apartment complexes, completed in 2020 and 2021, added 470 more units. Interestingly, all multifamily units developed in Menifee fall under the umbrella of garden-style apartment complexes, which are characterized by medium-density, low-rise structures surrounded by landscaped common areas.

The increase in production is undoubtedly a response to rising market demand, which can be seen in average occupancy / vacancy rates. Traditionally, a market area vacancy rate of 5 percent is considered healthy, and accounts for normal turnover. On average, multifamily products in Menifee have a vacancy rate of



3.8 percent, indicating that demand is outpacing supply. Low vacancy rates are consistent across product types and physical structure age, suggesting that demand is coming from multiple market segments.

The average asking rent for a market-rate multifamily unit in Menifee currently sits at \$2,177. Products built since 2010 command a higher rent, on average, compared to units built in 2009 or earlier. This tends to align with the general consensus that a newer product is inherently more valuable, but it must also be mentioned that the trend of increasing unit size, and the inclusion of more lifestyle amenities, also factor into the rent difference.

The average asking rent for affordable or age-restricted multifamily units in Menifee currently sits at \$2,900; however, there are significant differences between the types of products offered. At one end of the spectrum, age-restricted, affordable communities with smaller units and fewer lifestyle amenities have an average asking rent of \$969. At the opposite end of the spectrum, age-restricted, market-rate communities offer a full range of lifestyle amenities and units that cater to residents at various stages of life. These units command a significantly higher asking rent, \$4,830, compared to affordable, age-restricted products.

BARRIERS ANALYSIS

As part of this market study, the consultant reviewed the barriers analysis included in Menifee's adopted 6th Cycle Housing Element. The consultant also interviewed developers and other stakeholders and reviewed the City's development regulations and planning documents.

One of the key issues arising from this market study is that the market is producing little multifamily housing, and it is worth considering whether this is due to market conditions and/or regulatory hinderances. There are two primary zoning

districts and land use designations that would accommodate multifamily housing. These are discussed below.

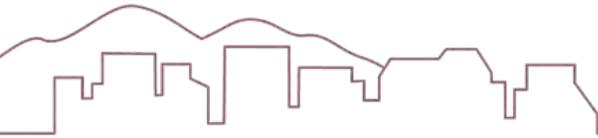
Multi-Family Residential (HDR) Zone

The consultant reviewed the City's zoning code to better understand the development standards governing multifamily and mixed-use development. We agree with the City's assessment, described in the adopted 6th Cycle Housing Element, that the standards are not onerous and therefore do not restrict or otherwise disincentivize the development of multifamily units. We found that for the HDR zone, it is possible to achieve the maximum allowed density on a variety of parcel sizes, even those as small as 3,200 square feet. The resulting units would range in size from approximately 500 square feet to 1,000 square feet, which would allow a developer ample room to mix unit types within a project.

Economic Development Corridor

Resulting from the 2013 General Plan, five Economic Development Corridor (EDC) subareas encapsulate Menifee's vision for the future. The EDC is intended to develop primarily as nonresidential uses with some supporting residential in a mixed-use project; however, each subarea has a different proportionality for these uses. The special development standards applied to residential projects proposed in the EDC, regardless of subarea, likely impact the feasibility of residential development for the near-term, before market demand for mixed-use development materializes. However, as the non-residential portions of the subareas continue to intensify, as well as other areas in the city, housing demand will likely increase to a degree that mixed-use residential projects become feasible.

If the intent remains to follow through with the original vision for the EDC subareas, it should simply be a matter of time until the market supports the envisioned housing components. Should the City wish to encourage housing, PlaceWorks recommends revisiting the special development standards and reducing or



removing sections that currently present a challenge to residential development. For example, the City may determine that the requirement for residential developments to include a minimum amount of non-residential uses may be too restrictive, and either reduce the dedication, temporarily suspend, or remove the requirement altogether.

IMPLICATIONS OF HOUSING MARKET FACTORS

Attainable Housing.

The label “attainable housing” is used to refer to housing that is broadly affordable to middle-income households, which would include some moderate-income households and some above-moderate-income households.

Menifee has been considered a good place for developing attainable housing, in part because land costs have been reasonable. Market conditions have pushed sales prices higher, however, and the median sales price for new single-family detached housing has climbed to \$609,000.

The median sales price would be affordable to a household with an income of around \$170,000 or higher. The median household income in Riverside County is \$87,400. The median incomes are not much higher in Orange County, \$100,559, and San Diego County, \$91,003. Thus, even in Menifee, much new single-family housing is not affordable to middle-income households, at least not as first-time homebuyers.

It may be that the market will eventually price new homes in Menifee out of reach for middle-income first-time home buyers. Nevertheless, it is the strength of the local market today. In considering policies and programs to promote housing production and increase the provision of affordable housing in Menifee, the city may need to balance tradeoffs between maintaining housing prices that are

attainable to middle-income households and being able to invest in and maintain public facilities and services that would support higher housing prices.

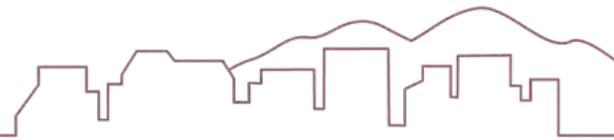
Households Without Children Under the Age of 18

Similar to the national context, a large majority of households in Southwest Riverside County do not have children. This applies across income categories, with 61.5 percent of above-moderate-income market-area households and 71 percent of moderate-income households and below having no children under the age of 18 at home.

Just as this is an increasing trend nationally, the share of market-area households with children at home has been decreasing over time. It is a bit of a complicated story in a growing region like Southwest Riverside. In Temecula, the number of households with children at home decreased from 2012 to 2021. In Murietta and Perris, there was growth in the number of households with children, but there was larger growth in the number of households without children. Thus, in these two cities, the percentage of households with children decreased.

In contrast, the number of households with children in Menifee increased by 27 percent from 2012 to 2021. However, there was an almost proportional increase in the number of homes without children. Thus, the percentage of homes with children increased only slightly. Even still, the majority of growth in households in Menifee was those without children.

The region’s growth in households with children is strongest in Menifee. And as long as Menifee continues to be a place where developers can provide attainable housing, this trend may well continue. Nevertheless, the market area’s share of households with children is likely to continue to decrease over time.



Smaller Households

In the market area, 49 percent of households have one or two people, 65 percent have three or fewer people. Strikingly, the percentages are nearly identical (47 and 65 percent) among the households that moved to their current home in the previous year. There are slightly fewer households with one person and slightly more with three among owners relative to renters.

It is more likely for larger households to move into new housing and for smaller households into existing housing. Furthermore, it is possible that even smaller households choose larger homes when their incomes can accommodate the price. Nevertheless, the magnitude of one- and two-person households among those moving in the last year suggests that there is a market for smaller-sized housing units.

Single-Family Housing

Single-family housing is the dominant form of housing in the market area. Even though only 56 percent of households in the WRCOG region reside in single-family housing, in the market area, 90 percent of households with incomes above moderate and 70 percent of households with moderate or below incomes reside in single-family housing. In Menifee, 87 percent of the existing housing is single-family detached housing.

Single-family housing is also the dominant type of housing being constructed. Among the cities in the market area, 78 percent of the increase in housing from 2012 to 2021 was single-family detached housing. However, in Menifee, single family detached housing accounted for 98 percent of housing growth. Menifee accounted for 37 percent of the market area's growth in housing but 46 percent of the increase in single-family detached housing. During the previous year, two-thirds of the new single-family housing sold had four or more bedrooms, and 30 percent had three bedrooms.

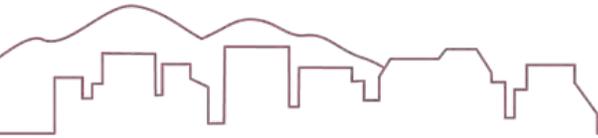
The strength of the Menifee housing market is single-family housing development. In part, this strength rests on a foundation of development costs that allow for the construction of attainable housing. A substantial portion of this market serves the needs of households in other counties relocating to Menifee, where they are able to afford to purchase a new house and live in a community with a desirable quality of life. Because this is the core strength of the Menifee housing market, new and revised policies should take into consideration the impacts to this market. Nevertheless, it may be the case that forces beyond the influence of the city—such as interest rates, construction labor, regional infrastructure and school fees, and the price landowners expect—have a much larger impact.

At the same time, it may be the case that the housing market is not building enough housing suited for a segment of the regional housing market, smaller households. Recent state legislative changes relating to accessory dwelling units (ADUs) may alter the housing development market. However, ADUs will mostly be for rent and not serve the potential demand for smaller for-sale housing units. Thus, the city may want to explore whether there are policies that could encourage or incentivize the development of smaller for-sale housing units.

Attached and Multifamily Housing

While Menifee accounted for 37 percent of the market area's growth in housing from 2012 to 2021, it only provided 10.5 percent of the new single-family attached housing and 4.5 percent of the multifamily housing.

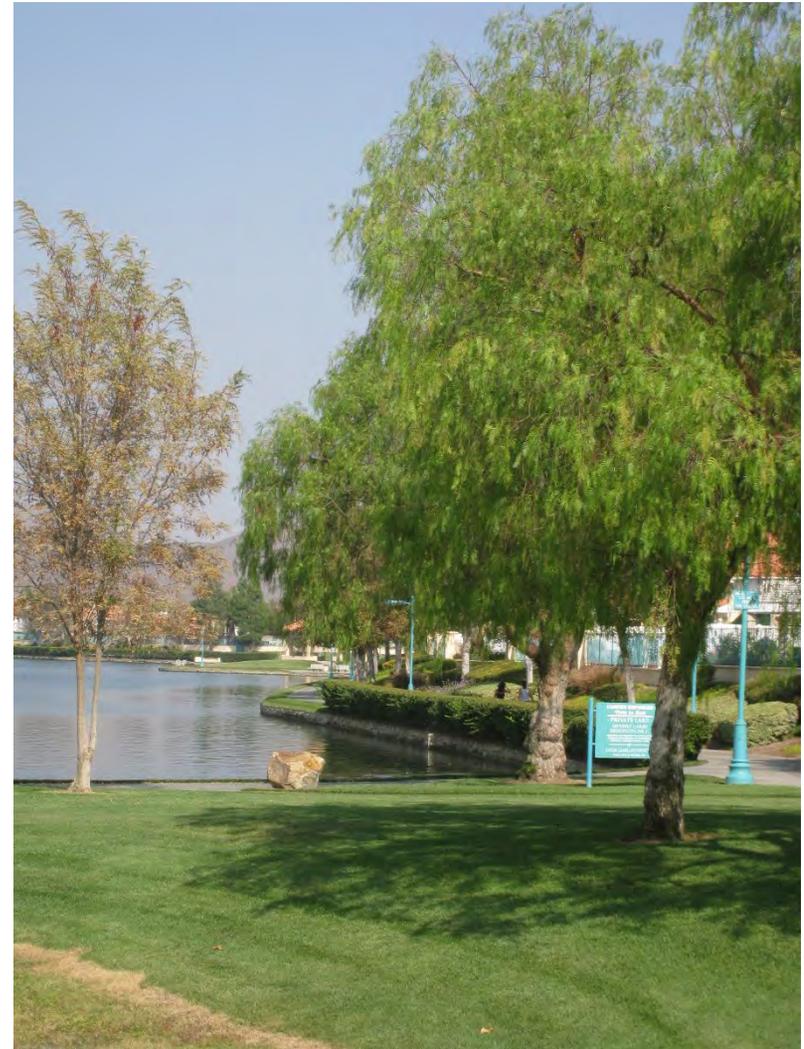
It may be the case that it is a matter of time before more investment in multifamily housing flows to Menifee. Developers suggested that multifamily development is more financially feasible in the gateway communities, such as Temecula and Murrieta to the south, and the cities along and closer to the CA-91 freeway to the north, and that there are still development opportunities in these communities.



However, developers also questioned whether Economic Development Corridor designation complicated the prospects for developing multifamily housing in areas close to the freeway. They also questioned whether there were a sufficient number of properties zoned for high density residential uses in areas closest to the freeway and services, the areas in which multifamily housing developers tend to prefer.

Multifamily housing is an important component of the housing market. It tends to be the most affordable housing option, and it can provide a substantial portion of a community's workforce housing. In Menifee, 57 percent of renters (which include single-family and multifamily housing) pay more than 30 percent of their income for their housing costs, and 36 percent pay more than 50 percent. This suggests that there is a need for and market demand for more multifamily housing in Menifee.

The city should consider whether zoning and land use changes are warranted and whether policy changes to provide incentives for multifamily housing are warranted to hasten investment in new multifamily housing development.



5. Forecasts and Gap Analysis

LOCAL AND REGIONAL POPULATION PROJECTIONS

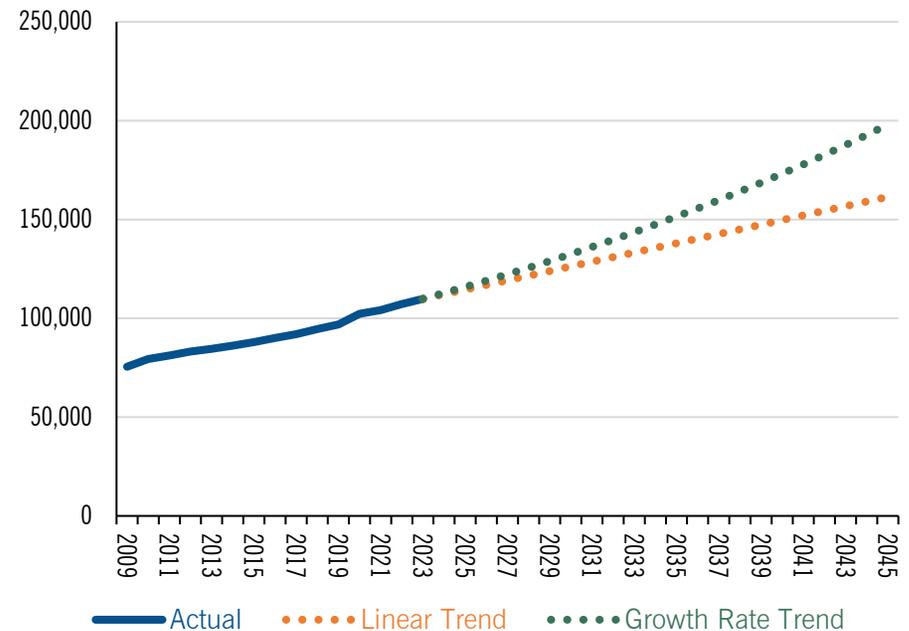
From 2009 to 2023, the population of Menifee grew by 2,450, increasing from 75,500 to 109,800. If the city were to continue growing by 2,450 new residents each year, the 2045 population would be 161,400, an increase of 51,600 people. This is called a “linear trend” because the population in each year forms a straight line. Figure 25 shows the actual population and the projected population with a linear trend.

The city’s population increase from 2009 to 2023 represents an annualized growth rate of 2.7 percent per year. Although the actual increase each year varies, if the 2009 population of 75,500 increased by 2.7 percent the next year and each year after, it would have been 109,800 in 2023. This is called a “growth rate trend.” Each year, the population increases by the same percentage, but because each year the population is a little bit larger than the previous year, the total number of new people is slightly larger each year, and the population forms a curve that gently slopes upward. With an annual growth rate of 2.7 percent, the city’s 2045 population would be 198,000, an increase of 88,200 people. Figure 25 shows the actual population and the projected population with a linear trend.

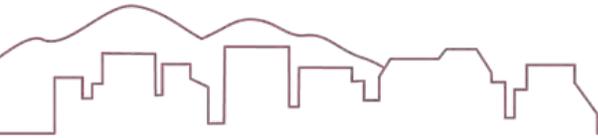
The Southern California Association of Governments (SCAG) forecasts population as part of its planning process for the regional transportation plan. Its most recent, based on its estimated population for Menifee in 2019, is for the population to increase to 129,800 in 2045, which represents linear growth of 1,400 people each year or an annualized growth rate of 1.3 percent per year. This is substantially lower than both the linear and growth rate trends. The

following sections explore several other projections before presenting a forecast for future growth and the demand for housing to accommodate the growth.

Figure 25: Actual Population, 2009 to 2023, and Two Population Projections, 2023 to 2045; Menifee



Source: PlaceWorks, 2024, using data from the CA Department of Finance.



Comparing Menifee’s population growth to that of the major nearby cities provides some helpful context. Menifee had a larger annualized rate of growth from 2009 to 2023, 2.7 percent, than did Murrieta (0.5 percent), Perris (1.4 percent), and Temecula (0.8 percent). However, this is, in part, due to these cities growing more rapidly prior to the 2008/09 recession. The annualized rate of growth for these cities from 1990 to 2023 (1992 for Murrieta, which did not incorporate until that year) is 5.0 percent in Murrieta, 4.0 percent in Perris, and 4.3 percent in Temecula.

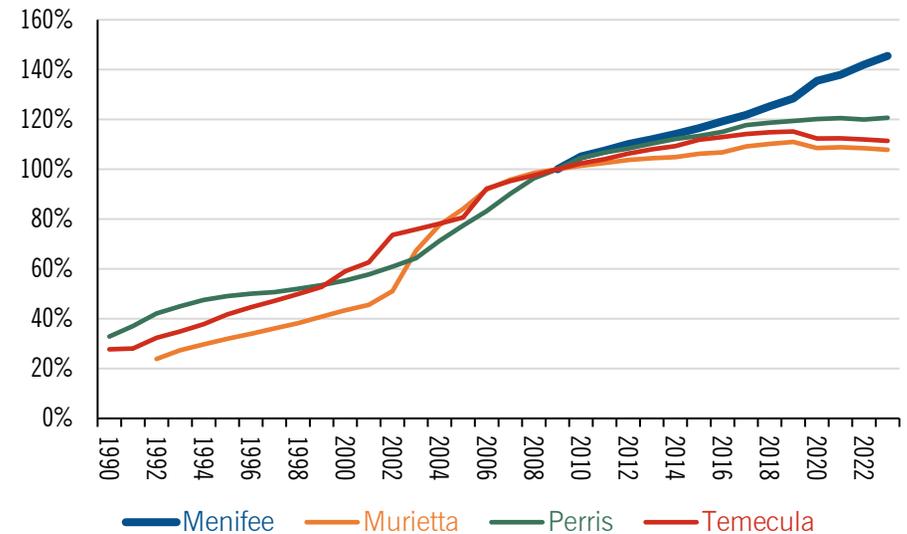
Figure 26 shows the population in Menifee and the three major nearby cities as a percentage of their 2009 populations. The data illustrate the relative rate of growth in each city, with the three nearby cities having faster growth in the early 2000s, then slowing as the overall housing market began to slow in 2006. The three cities have continued to grow, but at a slower rate after the 2008/09 recession than the rate prior to the recession. The experience in these three cities suggests that, at some point, Menifee’s rate of population growth will also slow.

Given the lower population forecast from SCAG and the population growth experienced in Murrieta, Perris, and Temecula, it is reasonable to assume that Menifee’s long-term population growth potential will be closer to the linear growth trend than the growth rate trend. However, the city’s population may well increase at the growth rate trend through the end of the current economic expansion, if not longer, before slowing.

HOUSEHOLD POPULATION PROJECTION

The driver for housing demand is the number of households. Thus, the projection for the household population—which excludes incarcerated individuals, those living in on-campus student housing and assisted living facilities, and

Figure 26: Population as a Percentage of 2009 Population; Menifee, Murrieta, Perris, and Temecula; 1990 to 2023



Source: PlaceWorks, 2024, using data from the CA Department of Finance.

military personnel stationed elsewhere—is important for forecasting housing demand over the long term. In Menifee, the share of the population living in households remained nearly constant, increasing from 99.7 percent in 2009 to 99.8 percent in 2023. Other nearby cities have similarly low percentages of population residing in households.

Because there are few residents not living in households, Menifee’s household population had nearly identical growth as the total population, adding an

average of 2,450 people per year or growing at an annualized rate of 2.7 percent per year. However, as shown in Figure 26, Menifee has been growing more quickly than other nearby cities. The city's share of the total household population in the market-area cities increased from 17.5 percent in 2009 to 20.9 percent in 2023.

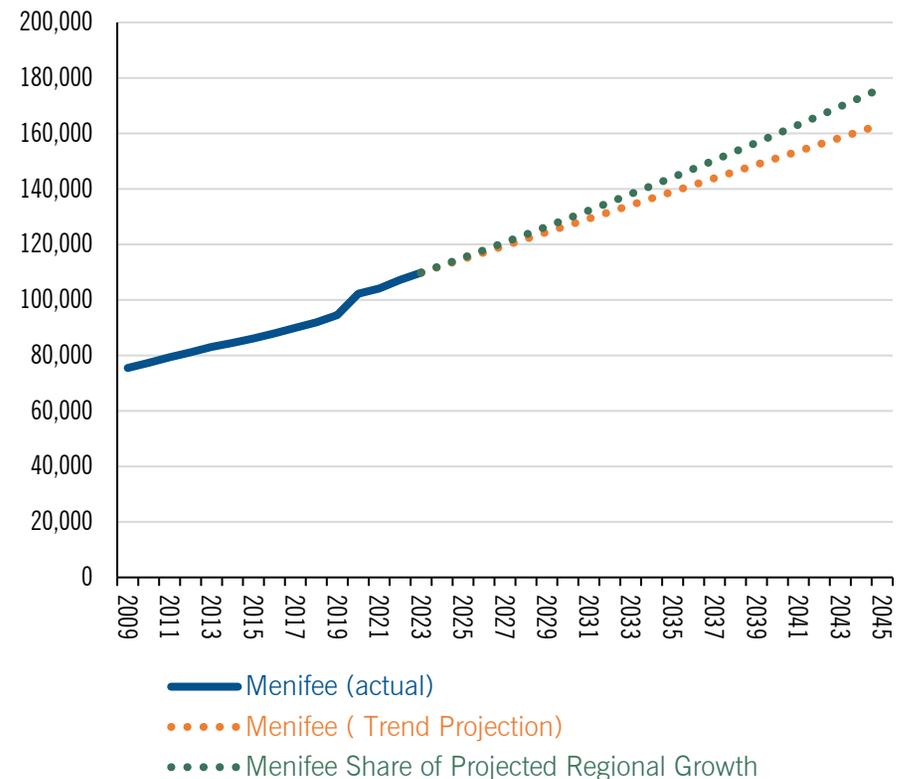
Figure 27 shows two projections for the household population in Menifee. One is the linear trend projection, based on the city's household population in each year from 2009 to 2023. This projection is nearly identical to the trend projection for total population, discussed above. The second projection is derived from applying the linear trend projection of Menifee's percentage share of the region's household population (which is increasing from 2009 to 2023) to the linear trend projection for the region's household population. Because the city's share of the region's household population has increased over time, this projection results in a higher population in 2045 than does the projection of just the city's household population. These two projections provide the basis for the forecast for long-term housing demand below.

AVERAGE HOUSEHOLD SIZE PROJECTION

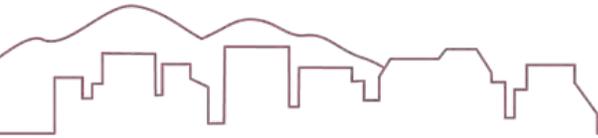
As discussed previously, the average household size in the US has been steadily declining for several decades. This has not been the case in Southern California, until recently. Although household sizes declined in conjunction with the pandemic, SCAG projects that the Riverside County's average household size will decline by 0.36 persons per household over the long term.

As discussed above, Menifee's average household size is lower than that in other nearby cities, but it increased slightly over the past ten years, while the size in other cities has begun to decline. Because most of the housing built in Menifee and the vast majority of entitled but not yet built housing is single

Figure 27: Household Population, Actual and Projections; Menifee; 2009 to 2023 (actual) and 2023 to 2045 (projections)



Source: PlaceWorks, 2024, using data from the CA Department of Finance.



family, the city may not experience a decline in household size in the near term. However, over the long term, the city can expect to experience some of the regional trend to smaller household sizes.

The average household size in Menifee generally increased from 2.77 persons per household in 2009 to 2.83 in 2019. After a jump to 2.95 persons per household in 2020, reflecting the COVID-19 pandemic, the average size decreased slightly to 2.89 in 2023.

If the average household size were to continue the linear trend of growth from 2009 to 2023, the average size would reach 3.05 persons per household in 2045. This projection is shown as Menifee (trend) in Figure 28. If the average size were to follow the decrease expected for Lake Elsinore, Murrieta, Perris, and Temecula, it would decline to 2.62 in 2045.

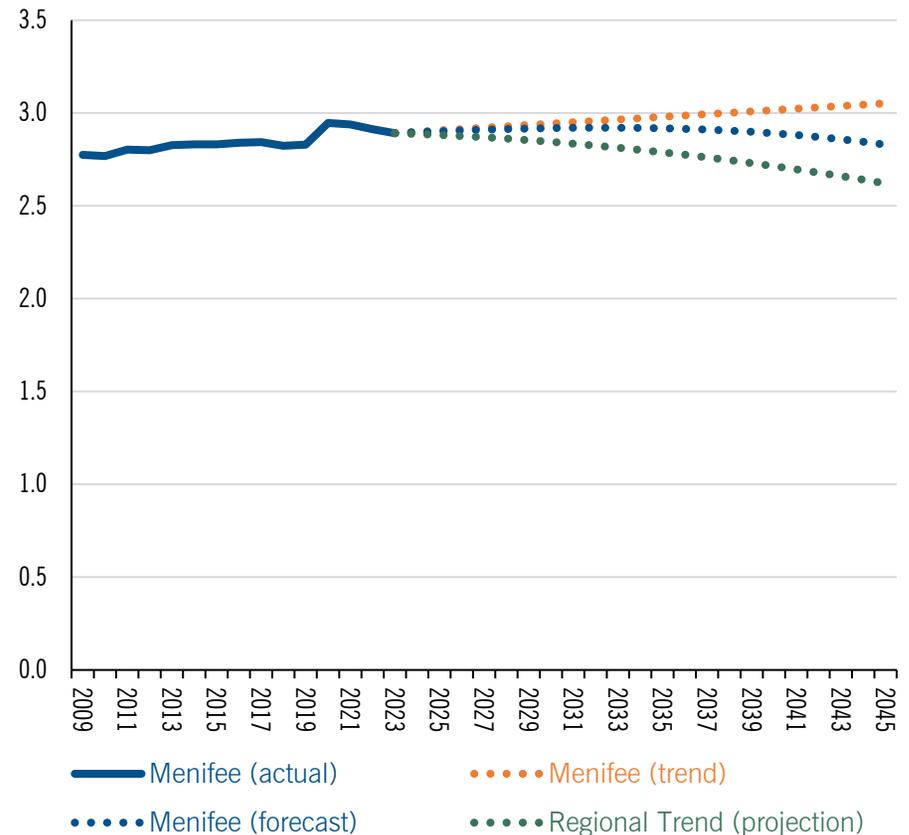
The analysis forecasts that the average household size in Menifee will increase at its linear trend rate for the next four years and then slowly transition to the rate of decline expected regionally. The resulting forecast indicates that the average size would increase to 2.92 persons per household in 2032 and then decrease to 2.83 in 2045.

These might appear to be very small changes, but when applied to a household population expected to be near or over 170,000, they result in differences of thousands of housing units.

PROJECTED NUMBER OF HOUSEHOLDS

Menifee had 27,200 households in 2009 and grew to 38,000 in 2023. This growth represents an average of about 770 new households each year or an annualized growth rate of 2.4 percent per year.

Figure 28: Average Household Size, Actual and Projections; Menifee; 2009 to 2023 (actual) and 2023 to 2045 (projections)



Source: PlaceWorks, 2024, using data from the CA Department of Finance.

To develop a forecast for future household growth, the analysis considered a low projection, as shown in Figure 29. The low projection is based on the low projection for household population in Figure 27, and assumes that the average household size will continue increasing at its current rate, which is the linear Menifee trend in Figure 28. With this projection, the city would grow to 53,500 households by 2045.

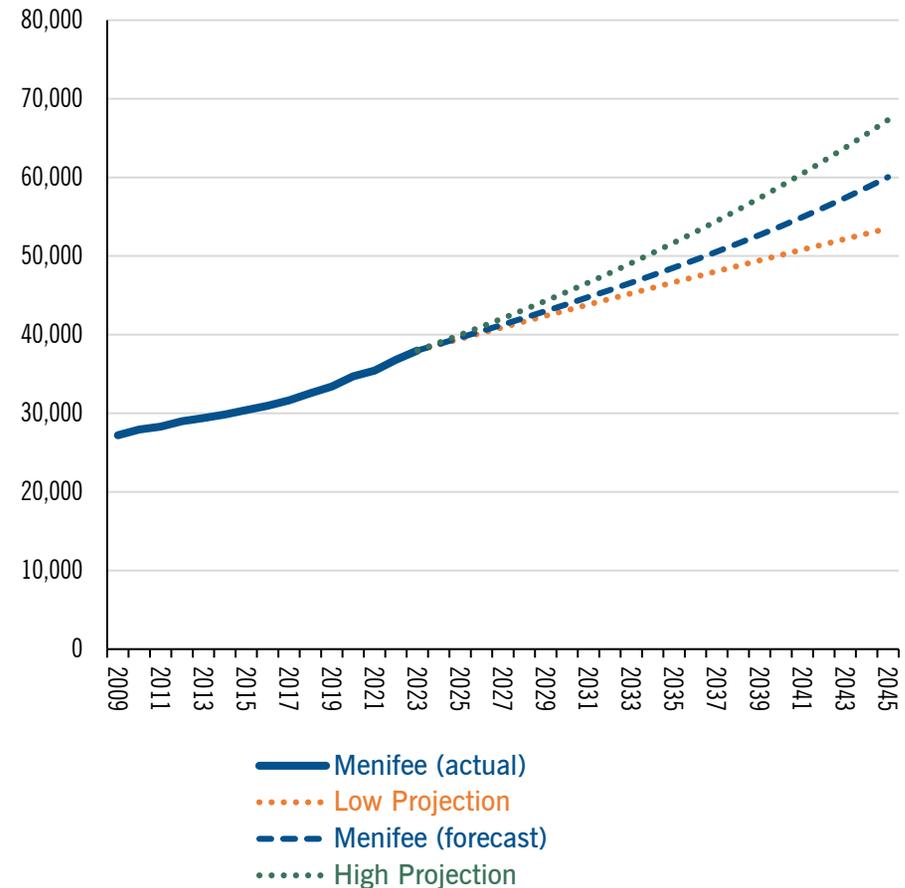
The analysis also considered a high projection, also shown in Figure 29. This projection is based on the high projection for the household population and the regional trend projection for the average household size. This would result in a total of 67,300 households in 2045.

The analysis' forecast for the number of households is based on the average of the two projections for household population and the forecast for the average household size. The forecast is for Menifee to add 22,100 households, growing to a total of 60,000 in 2045. This increase would be an average of 1,000 households per year. This is more than the annual average since 2009, but slightly less than the average from 2018 to 2023. Because the starting point for the forecast, 2023's household count, is higher than that in 2009, the annualized rate of change for the forecast for household growth, 2.1 percent per year, is lower than the growth rate since 2009, 2.4 percent per year.

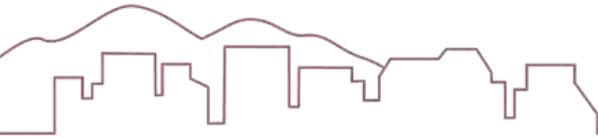
HOUSING UNIT FORECAST

Menifee incorporated during the 2008/09 recession. The CA Department of Finance estimated that over 9 percent of the city's housing stock was vacant in 2009, and the vacancy rate didn't fall below that until 2013. The rate declined steadily, reaching 5 percent in 2020 and has stayed at about that level since. To forecast the number of housing units, the analysis applies the 5 percent vacancy rate to the forecast increase in the number of households in each year.

Figure 29: Number of Households, Actual and Projections; Menifee; 2009 to 2023 (actual) and 2023 to 2045 (projections)



Source: PlaceWorks, 2024, using data from the CA Department of Finance.



The vacancy rate can be expected to rise and fall with changing economic conditions. Nevertheless, a five percent vacancy rate can generally be considered a marker of a healthy residential development market, and it is reasonable to assume this rate for the long-term housing development potential.

Table 6 provides the forecast for the total number of housing units from 2023 to 2045, broken down into five-year increments. It also provides the average annual number of new housing units for each period and the annualized rate of growth.

Table 6: Total Number of Housing Units Forecast; Menifee; 2023 to 2045

Year	Total Number of Housing Units	Average Annual Increase from Previous	Annualized Rate of Growth from Previous
2009	29,900		
2023	40,000	720	2.1%
2025	41,700	860	2.1%
2030	46,200	900	2.1%
2035	51,100	980	2.0%
2040	56,600	1,110	2.1%
2045	63,200	1,310	2.2%
2023 to 2045		1,060	2.1%

Source: PlaceWorks, 2024.

The analysis forecasts that Menifee will add 23,200 housing units, increasing from 40,000 units in 2023 to 63,200 units in 2045. The combination of a slightly increasing rate of growth in household population over time and the

steady and then decreasing rate of change in the average household size results in a housing forecast that generally produces an increasing number of housing units each year through 2045.

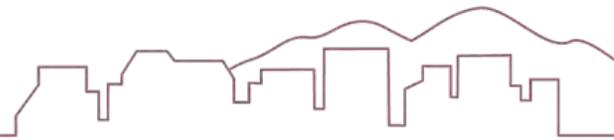
Residential buildout under Menifee’s current General Plan would result in a total of 70,800 housing units. The forecast indicates that in 2045, the city will not have reached full residential buildout and would have another 7,700 units to be built. The higher range projection would reach full residential buildout in 2045, while the low-range projection would still be 14,500 units short of buildout.

PRODUCT TYPE AND GAP ANALYSIS

As discussed previously, the market has produced predominantly single-family detached housing in Menifee. From 2010 to 2023, single-family detached housing accounted for nearly 95 percent of the increased housing in Menifee. In the remainder of the market area outside of Menifee, single-family detached housing was also the largest part of the market, but it accounted for about 75 percent of new housing.

Table 7 provides the data on the number and types of housing that the regional market would demand from 2023 to 2045. Single-family detached housing would decrease from 94.8 percent of new construction to 73.3 percent over the long term. Single-family attached housing (primarily townhouses and multi-plexes) would increase from 1.3 percent to 6.6 percent, and multifamily housing (for-rent apartments and for-sale condos) would increase from 4.2 percent to 20.1 percent.

In terms of the number of units, this shift to address regional demand would mean 1,530 single-family attached units and 4,700 multifamily units, instead



of 338 single-family attached and 615 multifamily units under current construction trends.

Table 7: Menifee Housing Mix by Type of Housing Based on Regional Demand; 2023 to 2045

Housing Type	Menifee New Housing Mix, 2009 to 2023	Projected Market Area Demand 2023 to 2045	Menifee Housing Mix to Meet Market Area Demand	Menifee Existing Housing Stock, 2023	Total Menifee Housing Stock in 2045
SF Detached	94.8%	73.3%	17,026	31,395	48,421
SF Attached	1.3%	6.6%	1,533	1,056	2,589
MF 2 to 4 Units	0.3%	2.5%	577	481	1,058
MF 5+ Units	3.9%	17.6%	4,077	1,079	5,156
Mobile Homes	-0.3%	0.0%	0	2,515	2,515
Total	100.0%	100.0%	23,213	36,526	59,739

Source: PlaceWorks, 2024, using data from the CA Department of Finance.

IMPLICATIONS OF THE GAP BETWEEN CURRENT TRENDS AND MARKET-AREA DEMAND

The market gap is not about curtailing single-family detached housing development. The 17,026 detached housing units identified in Table 7 represents a long-term average annual production that is higher than that from 2010 to 2023. Rather, the gap is about capitalizing on the regional demand for

attached and multifamily housing and accelerating its development in Menifee. It is about the additional 5,300 attached and multifamily housing units that the regional market could direct to Menifee and the households that could reside in those units.



6. Recommendations

The market currently directs substantial investments into Menifee for the development of single-family detached housing. Relative to other cities in Western Riverside County, the cost to develop in the city still allows for the market to produce what some developers refer to as “attainable housing.” This study has identified no reasons to interfere with the production of attainably priced single-family detached housing.

The outstanding issue is that the market is not directing much investment into Menifee for single-family attached housing and multifamily housing. This may be a concern for the City. Attached and multifamily housing tends to be of a smaller size than detached housing, and thus, maybe be better suited to changing demographics of smaller household sizes. Smaller sizes also translate into lower priced housing, which may be better suited to some people who work in Menifee but cannot afford to purchase a detached house. Such housing may also be a first step for people who grow up in Menifee and who are moving out of their parents’ homes.

Based on the interviews with developers and other stakeholders, there is an expectation that the market will eventually produce attached and multifamily housing in greater numbers in Menifee. They indicated that rents may not yet be sufficient to support new construction and that sites remain available for such development in other nearby cities that are closer to higher concentrations of jobs. However, they also indicated that it is too difficult to try to entitle stand-alone multifamily projects in the EDC and that the sites zoned HDR are generally not close enough to shopping, entertainment, and other economic activity centers in the city.

In the March 2023 update of the City’s Strategic Plan, the City identifies a Community Value for Balanced Growth, “We value our ability to provide a

broad range residential housing types for our residents’ life stages and lifestyles.” The limited amount of attached and multifamily housing may hinder this value. However, solutions to address this lack of development will be weighed against other values in the Strategic Plan. Nevertheless, under the State-mandated Housing Element, the City is committed to the goal of a diverse housing stock that offers a full range of housing opportunities for Menifee residents and supports the local economy.

Additional HDR-zoned Sites

There are sites currently zoned for higher density housing types, and some of these are being pursued by developers for attached or multifamily housing development. However, others have site constraints, such as slopes and drainage that limit their development capacity. Furthermore, there is a lack of HDR-zoned sites in proximity to the central economic activity centers of Menifee. These are much more attractive to market rate developers, and such sites are more likely to sustain higher rents or sales values that are necessary to support new construction.

Collaborating with the community and with property owners who might be interested in developing their property or selling it for development, the City could consider a limited number of targeted HDR rezonings for sites near existing activity centers and existing infrastructure.

INCLUSIONARY HOUSING FEASIBILITY STUDY





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7. Introduction

As part of the process of adopting a Housing Element and having it certified by the CA Department of Housing and Community Development, the City included in its Housing Element an implementation program to assess the feasibility of an inclusionary housing ordinance. This study estimates the impact of requiring new market-rate housing development to include income-restricted housing units on the financial feasibility of new residential development, estimates the amount an in-lieu fee would need to be set at to enable the City to support the development of income-restricted affordable housing, and the impact of an in-lieu fee on new residential development.

Two key factors to be considered in the creation of an inclusionary housing requirement are:

1. The requirements should balance the interests of developers against the public benefit created by the production of affordable units.
2. The inclusionary housing requirements should not deprive housing developers of a fair and reasonable return on their investment.

FEASIBILITY STUDIES VERSUS NEXUS STUDIES

Feasibility studies and nexus studies are related yet serve different purposes. As explained further below, inclusionary housing ordinances are adopted as local land use regulations via a jurisdiction's use of its police power. Feasibility studies for inclusionary housing ordinances consider the quantity of affordable housing that new residential development projects can bear while remaining financially feasible to develop.

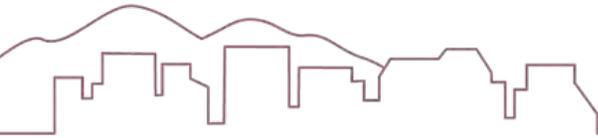
In contrast, nexus studies need not assess project financial feasibility. Nexus studies are used to quantify impacts of new development, calculate the cost of this impact, and determine the fees to be imposed as a development condition. In the case of affordable housing, nexus studies document how much a development project (including residential and non-residential) contributes to the need for affordable housing and determine a legally defensible impact fee. Nexus studies demonstrate that a new development project would create the need for affordable housing; the jurisdiction may, but is not required, to consider financial feasibility when establishing the amount of the development impact fee.

For development impact fees, nexus studies determine the maximum fee that is legally defensible. However, the jurisdiction can charge any fee up to that amount. Oftentimes, for affordable housing, cities account for financial feasibility and impose a fee lower than the maximum amount.

It is important to note that this study is only for an inclusionary housing requirement that could be adopted into the City's Municipal Code; it is not a nexus study for a development impact fee.

LIMITS OF FEASIBILITY STUDIES

The results of all feasibility studies should be understood as approximate. Feasibility studies are different from real estate appraisals, which establish a value for a specific property based on data from comparable properties and projects. Feasibility studies involve more complex calculations based on a wider variety of data. While market data on home sales prices and rents is available,



feasibility studies also rely on data and assumptions about land values, construction costs, operating costs, unit sizes, parking costs, and other factors.

The primary difference between an appraisal and a feasibility study is the scope. An appraisal is focused on a single property and is intended to provide an accurate estimate of the value of that property. In contrast, a feasibility study is intended to represent an approximate typical value for a type of development that could occur on many different properties within a jurisdiction. The values of that theoretical development may vary greatly across different properties and with different developers.

Feasibility studies depend on specific input assumptions and are more open to interpretation than appraisals. While two certified appraisers are likely to return very similar property value estimates in most cases, two well-conducted feasibility studies may still draw varying conclusions about the impact of inclusionary housing requirements on project feasibility.

LEGAL BACKGROUND

Article XI, section 7 of the California Constitution grants each city and county the power “to make and enforce within its limits all local, police, sanitary and other ordinances and regulations not in conflict with general laws.” This is referred to as the police power of local governments. California Planning and Zoning Law (Government Code, Sections 65000 to 66035) establishes the Legislature’s intent to “provide only a minimum of limitation in order that counties and cities may exercise the maximum degree of control over local zoning matters.”

Approximately 200 jurisdictions in California, pursuant to their police power, have adopted inclusionary housing ordinances that require developers to ensure that a certain percentage of housing units in a new development be affordable to moderate- and lower-income households. The majority of these include requirements for both for-sale and rental residential development projects.

A series of legal cases and legislation adopted by the State of California Legislature guide the creation and implementation of inclusionary housing programs. A chronological summary of the relevant issues follows.

Court Cases

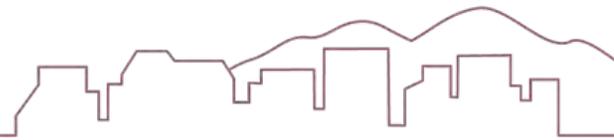
Palmer/Sixth Street Properties L.P. v. City of Los Angeles (2009) 175 Cal.App.4th 1396

In 2009, the California Court of Appeal ruled that the local affordable housing requirements imposed by the City of Los Angeles violated the Costa-Hawkins Rental Housing Act (Costa-Hawkins). Costa-Hawkins allows landlords to set the initial monthly rent for a new unit, and then to increase the monthly rent to the market level each time a unit is vacated. The Court found that the imposition of long-term income and affordability restrictions on rental apartment units is a violation of this provision.

After the Palmer decision, most jurisdictions with inclusionary housing ordinances that included rental housing stopped applying the rental requirement. Some jurisdictions replaced affordable housing production models with a linkage or impact fee methodology.

California Building Assn. V. of San Jose (2015) 61 Cal.4th 435

In 2010, the City of San Jose adopted an inclusionary housing ordinance that applied a 15 percent inclusionary requirement. The California Building Industry



Association (CBIA) filed a lawsuit alleging that the requirements constituted an “exaction” that needed to be justified by the impact of the project. In 2015, the California Supreme Court ruled that inclusionary requirements are not exactions, stating that they are “constitutionally legitimate” so long as the enforcement “bears a real and substantial relationship to the public interest.” The court cited the need to increase the number of affordable units in California and the desirability of economically diverse communities.

This case has been widely interpreted to mean that an in-lieu fee payment option in an inclusionary housing program is not subject to the requirements of California Government Code Section 66000, the “Mitigation Fee Act.”

Assembly Bill 1505

Assembly Bill 1505 (AB 1505) was passed in 2017 in response to the Palmer case. AB 1505 amends Section 65850 of the California Government Code and adds Section 65850.01. It supersedes the holding in Palmer, to the extent that the decision conflicts with a local jurisdiction’s authority to adopt inclusionary housing programs on residential rental developments. AB 1505 reaffirms the authority of local governments to include inclusionary rental requirements. It provides for limited, circumstantial California Department of Housing and Community Development (HCD) review of economic feasibility studies to demonstrate that inclusionary housing programs do not “unduly constrain” the production of housing.

Per AB 1505, HCD is not required to evaluate financial feasibility studies. Local governments are only required to submit the studies upon HCD’s request. AB 1505 gives HCD the authority to review the restrictions imposed by an inclusionary housing program on rental projects if the program requires more

than 15 percent of units to be restricted to households earning less than 80 percent of the area median income (AMI), and if one of the following applies:

- + The jurisdiction has failed to meet at least 75% of its RHNA allocation for above moderate income units. This test is measured on a pro-rated basis over the planning period, which is set at a minimum of five years; or
- + HCD finds that the jurisdiction has not submitted their Housing Element report for at least two consecutive years.

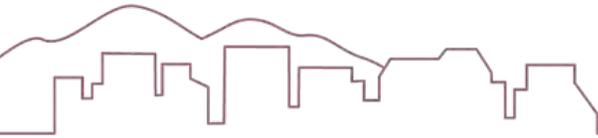
HCD may request evaluation based on information in the jurisdiction’s Housing Element, Annual Progress Report, stakeholder comment letter, phone call, news article, or at the request of a third-party.

Finally, HCD will not review the actual inclusionary housing program pursuant to AB 1505. HCD’s review is limited to a review of the financial feasibility study.

This study analyzes the potential impacts of a requirement for new residential development to restrict 15 percent, or less, of the units to occupancy by income-qualified households. Because the inclusionary requirement that is assessed does not exceed 15 percent, the provisions of AB 1115 would not apply and, thus, are not addressed in the study.

INCLUSIONARY HOUSING ORDINANCE COMPONENTS

The majority of inclusionary housing ordinances in California are comprised of a series of components that establish eligible developments, specific affordability requirements and alternative compliance options.



Threshold Project Size

Most inclusionary housing programs include a minimum threshold project size below which projects are not subject to the affordable housing production requirements. Common size thresholds range from three to ten units. This analysis is based on typical recent development projects in Menifee, which are larger than the typical threshold size. Thus, this study does not address this issue, and if the City were to move forward with an inclusionary housing ordinance, a threshold project size would need to be determined.

Applicable Geography

Some jurisdictions with a diverse real estate landscape impose varying inclusionary requirements for unique subareas. Others apply a single inclusionary housing requirement across the entire jurisdiction. The study discusses the appropriate geography in the recommendations section.

Income and Affordability Requirements

Income and housing affordability requirements are the key components of inclusionary housing. They vary throughout California. Most ordinances require that eligible projects include 10 to 20 percent affordable units. The following variations are common:

- + The inclusionary requirements vary for different levels of household affordability.
- + A sliding scale of inclusionary requirements for projects of varying size, developed to reduce the potentially disproportionate impact of inclusionary housing requirements on smaller projects.

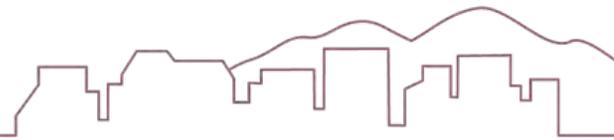
- + The length of the covenant period imposed on inclusionary units varies from jurisdiction-to-jurisdiction. However, the standards of 45 years for ownership housing units and 55 years for rental units set by California Health and Safety Code (H&SC) Section 33413 are commonly used.

Inclusionary Compliance Alternatives

According to California Government Code Section 65850 (g), jurisdictions may adopt inclusionary housing ordinances applicable to rental development, but the ordinance must offer developers alternative means of compliance. Common options for alternative means of compliance include:

- + Construction of a defined percentage of income restricted units within new market-rate residential projects.
- + Construction of a defined percentage of income restricted units in an off-site location.
- + Payment of a fee in lieu of producing affordable housing units that will subsequently be used by the jurisdiction to assist in the development of affordable housing units within the community.
- + The dedication of land to the jurisdiction that is appropriate for the development of affordable housing.
- + The acquisition and rehabilitation of existing units.

Some communities prefer an in-lieu fee as an alternative means of compliance because it provides a funding stream that allows the city to be more actively involved in affordable housing. The fee facilitates the transfer of affordable



requirements to developers that specialize in affordable housing development and operation. Dedicated affordable housing developments also have access to local, state and federal public funding sources that may support a greater number of affordable housing units. At the same time, there are other communities that prefer to not use in-lieu fees as an alternative means of compliance because they want affordable housing to be integrated in mixed-income buildings and neighborhoods rather than be concentrated.

STATE DENSITY BONUS AND INCLUSIONARY HOUSING

California’s Density Bonus Law (California Government Code Sections 65915 – 65918) provides developers with tools to build affordable housing. The law requires jurisdictions to provide density bonuses based on a sliding scale, including up to a 50 percent increase in project densities depending on the percentage of affordable housing provided and the income limits to which the affordable units are restricted.

The density bonus provides one method for developers to improve the feasibility of their project while still complying with an inclusionary housing ordinance. A 2013 case, *Latinos Unidos Del Valle De Napa Y Solano v. County of Napa* (2013) 217 Cal.App.4th 1160., has been broadly interpreted to hold that inclusionary units qualify as affordable units for the purposes of the DBL. Developers can use the same affordable units to fulfill both inclusionary housing requirements and density bonus requirements. However, to exercise this option, the more stringent of the two programs’ requirements must be applied.

The case confirmed that the density bonus is a financial tool available to help developers achieve inclusionary housing requirements. It should be noted,

however, that developments using an in-lieu fee to meet inclusionary housing requirements do not qualify for the density bonus.

Table 8 shows the scale of the state density bonus for increasing percentages of affordable units, up to 20 percent. Note that there is no bonus for either low- or moderate-income affordable units if they comprise less than 10 percent of the total number of units. Thus, with an inclusionary requirement below ten percent, the density bonus would only provide an incentive for housing affordable to very low-income households.

Table 8: Density Bonus Percentage Under State Density Bonus Law

Affordable Unit Percentage (Of Pre-Bonus Unit Total)	Very Low-Income Density Bonus	Low-Income Density Bonus	Moderate-Income Density Bonus (For-Sale Projects Only)
5%	20%	-	-
6%	22.5%	-	-
7%	25%	-	-
8%	27.5%	-	-
9%	30%	-	-
10%	32.5%	20%	5%
11%	35%	21.5%	6%
12%	38.75%	23%	7%

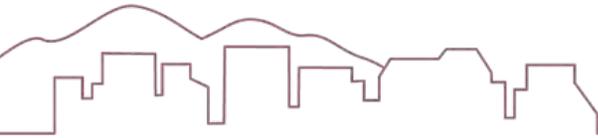


Table 8 continued

Affordable Unit Percentage (Of Pre-Bonus Unit Total)	Very Low-Income Density Bonus	Low-Income Density Bonus	Moderate-Income Density Bonus (For-Sale Projects Only)
13%	42.5%	24.5%	8%
13%	42.5%	24.5%	8%
14%	46.25%	26%	9%
15%	50%	27.5%	10%
16%	50%	29%	11%
17%	50%	30.5%	12%
18%	50%	32%	13%
19%	50%	33.5%	14%
20%	50%	35%	15%
...			
100%	80%	80%	80%

Source: California Government Code Sections 65915 – 65918.

Mixing Income Levels for Affordable Housing

The differing amounts of density bonus for each income category and the fact that two of the categories provide no density bonus units when providing less than 10 percent of a project’s total number of units creates challenges in determining a financially feasible incentive for affordable housing for a 15-percent inclusionary housing requirement.

Because the density bonus for low-income and moderate-income households does not commence until they account for 10 percent, or more, of the total units, there is a reduced incentive to provide low *and* moderate income units with a 15 percent inclusionary requirement—the developer could obtain a density bonus for 10 percent of one category and no bonus for the five percent of the other; there would be no density bonus with 7.5 percent of the housing in each category.

Moderate-income affordable housing only qualifies for a density bonus with for-sale housing. A for-sale housing project might provide fully 15 percent of the units as moderate income to minimize the total amount of subsidy in sales value or might provide up to five percent of the units as very low income to increase the total number of density bonus units.

A for-rent project might maximize the density bonus by providing 15 percent of the units as very low income or else provide at least ten percent of the units at low income and up to five percent as very low income.

As discussed in subsequent sections, it is possible that the density bonus cannot be achieved on a site without fundamentally changing the type of housing (e.g., having to provide some units as single-family attached housing in a development that is otherwise all single-family detached housing). Allowing a developer to select the mix of income categories increases the likelihood that the developer can find a financially feasible mix and will construct the inclusionary housing rather than pay an in-lieu fee. However, allowing the developer to determine the mix might also result in a disproportionate amount of one income category of housing being built in Menifee.



Even though the Density Bonus Law requires a minimum of 10 percent low- or moderate-income affordable housing in order to receive a density bonus and requires moderate-income housing be owned rather than rented, a local inclusionary housing ordinance can provide a density bonus for rental moderate-income housing units or for less than 10 percent low- or moderate-income units. Reducing these thresholds through a local ordinance can provide an additional incentive for the developer to include affordable housing in their residential project rather than paying an in-lieu fee.

Finally, the City can provide additional incentives beyond the density bonus to encourage developers to provide affordable housing. For example, some cities reduce or waive development impact fees for affordable housing units. However, the majority of the cost of residential impact fees applicable to residential development in Menifee are required by other public agencies, such as school districts, the water district, and the regional transportation fee. Reducing or waiving fees can provide a direct financial incentive, but affordable housing units do not necessarily result in less demand for the infrastructure funded by impact fees. Thus, that cost still needs to be funded from another source.

HOUSING NEED IN MENIFEE

This feasibility analysis was prepared after adoption and certification of the City's 6th Cycle, 2021-2029 Housing Element. For RHNA allocation, the City had to plan for the construction of 6,609 housing units, with 1,761 units affordable to very low-income households, 1,051 units affordable to low-income households, 1,106 units affordable to moderate-income households and the remaining 2,691 affordable to above-moderate-income households.

As of the preparation of this analysis, there were approximately 40,000 existing residential dwelling units in Menifee. There are about 8,000 residential dwelling units that have been entitled but not yet constructed. The General Plan is estimated to accommodate a total of 70,800 residential dwellings at full buildout. Thus, there is a planned capacity for about 22,800 additional residential dwelling units to be entitled and constructed. The Housing Market Impact Study forecasts that the city will not reach full residential buildout by 2045. If the growth rate trends continue, full buildout could occur in 2050, although growth tends to slow as cities approach buildout and less land is available on the market to be developed.

If the City were to adopt an inclusionary housing requirement, it would not apply to the 8,000 entitled but not yet constructed dwelling units; it would apply to the 22,800 estimated units neither constructed nor entitled. A new inclusionary housing requirement may have only a limited effect in generating new affordable housing in the short term as the existing inventory of entitled housing gets constructed. An inclusionary housing requirement can be expected to increasingly generate affordable housing, directly or through the payment of in-lieu fees, over time. Even if an inclusionary housing requirement does not generate the City entire RHNA allocation of affordable housing in the current cycle, there will be new RHNA allocations with subsequent housing element cycles before the city reaches buildout.



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8. Methodology

The financial feasibility impact of an inclusionary housing requirement on a market-rate project is the difference between financial performance of a fully market rate development project and one that provides the required number of below-market rate (BMR) units along with any density bonus and other incentives. Most commonly, this difference is measured as the difference in the rate of return that the developer would expect for the equity invested in the project. However, the difference can also be expressed as the difference in the market-rate sales values or rents for units in the market-rate only project and the sales values or rents in the inclusionary project (i.e., for the same return on investment and same land cost, what would be the change in price for market rate units need to be for the inclusionary project to be feasible). It can also be measured as the difference in the residual land value (how much the developer can afford to pay to acquire the development site) between the market-rate and the BMR development projects, keeping the rate of return and the sales prices or rents equal.

ANALYTICAL APPROACH

The basic structure of the analysis is the development and application of financial feasibility pro formas for a set of housing development scenarios reflecting current development trends in Menifee and the region. The analyses include:

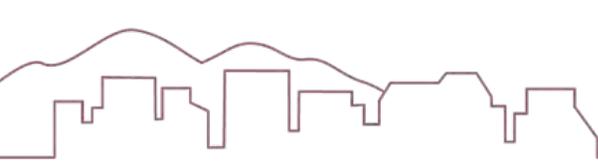
- + Creation of residential development prototypes that are representative of new and planned market-rate development in Menifee.

- + Estimation of typical market-rate sales prices and rents for the product types in these scenarios.
- + Calculation of the sales prices and rents reflecting affordable housing payments for the inclusionary units.
- + Calculation of the percentage of units that could be designated as inclusionary housing units while maintaining project financial feasibility.
- + Calculating the rate of return with the payment of in-lieu fees rather than constructing inclusionary units.

Development Prototypes

PlaceWorks developed for-sale and for-rent housing development prototypes that reflect recent development patterns in Menifee. The prototypes were created using multiple inputs to ensure they are representative of local development patterns and provide for the most accurate analysis within the limitations of a financial feasibility assessment. These inputs include:

- + Ongoing consultation with City staff regarding current project applications to the City, desired housing development types, and local policies related to housing production.
- + Evaluation and integration of recently constructed and approved single- and multi-family for-sale projects and rental projects.



- + Interviews with market rate and affordable housing developers with current or recent development projects in the city.
- + Results of the Housing Market Impact Study prepared in conjunction with this analysis and report.

Market Survey

PlaceWorks completed a market survey of home sales and rent prices to estimate achievable values for the development scenarios. The survey included rental apartments rates listed online or gathered from phone calls, data about rental prices in Menifee from real estate aggregators Zillow and Trulia, and sales data purchased from ListSource/CoreLogic.

Calculation Of Affordable Home Prices and Rents

PlaceWorks calculated affordable home values and rental process for inclusion in the pro forma process. These values were calculated using the Department of Housing and Community Development calculation methodology for income and number of bedrooms based on household size, based on California Health and Safety Code (H&SC) Section 50052.5.

Pro Forma Analyses

PlaceWorks prepared a series of dynamic pro formas for each development scenario to identify whether, and how, a 15-percent inclusionary requirement could be supported by market-rate housing projects. For development scenarios that were found not to be financially feasible, lower inclusionary rates were also evaluated.

Unlike static pro formas, dynamic pro formas rely on multi-year cash flow projections. This type of modeling requires a greater number of assumptions and

inputs than static modelling. It allows for the most accurate evaluation of the feasibility of real estate projects. This approach facilitated calculation of the following metrics:

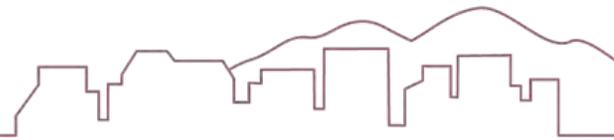
Internal Rate of Return

PlaceWorks calculated Internal Rate of Return (IRR) to assess the feasibility of the for-sale development scenarios. IRR measures the developer's return on investment with a discounted cash flow model. It is more complex and more accurate than a simple return on cost metric. It is based on the net cash flow for each year during the planning, construction, and sale. Equity investors typically use IRR because it allows them to compare different investment opportunities.

In the initial years, a developer invests money into a project and then, in later years, receives return in the form of the sales value of the residential dwelling units, after repaying the construction loan. The IRR is essentially the rate that generates a \$0 net present value for the series of cash flows. For real estate investments, an IRR of 15 percent is generally considered the threshold for a proposed project to be considered financially feasible.

Unleveraged Cash-on-Cash Yield

The analysis calculates the unleveraged cash-on-cash yield to assess the financial feasibility of for-rent development scenarios. With for-rent residential projects, the developer may own and operate the project for an indeterminate number of years. The cash-on-cash yield is an industry standard metric for rental projects, and it measures the annual net operating income (before taking into account debt service and taxes) relative to the total development cost. A 6 percent yield is generally considered the threshold for a proposed for-rent project to be financially feasible.



The leveraged yield is another return-on-investment metric used with for-rent projects. The leveraged yield measures the net operating income after debt service and taxes against the equity investment that the developer has to provide. In the current market—with banks hesitant to lend for real estate projects and high interest rates—it will be very difficult to begin a new for-rent development project. When measured by the leveraged yield, the for-rent projects analyzed in this report are not financially feasible, but this reflects lending conditions rather than the inherent value of the projects.

Thus, this analysis uses the unleveraged yield rather than making assumptions about when and how lending conditions will return to a more normal environment that supports real estate development. The unleveraged yield provides an indication of what scale and intensity of development will be financially feasible when lending conditions become supportive of development.

Residual Land Value

Residual land value is the amount that a developer can afford to pay to acquire a site for development and achieve a financially feasible rate of return. Residual land value is most often used to compare two or more alternatives for a development site or two or more land use regulations by determining which generates the highest residual land value. However, a portion of the financial impact of inclusionary housing requirements can be absorbed by landowners in the form of lower residual land values (RLV). As detailed further in subsequent sections, the methodology used in this analysis assumes that the residual land value would remain the same.

Scenario Analysis

The financial feasibility of each development scenario was analyzed under two scenarios:

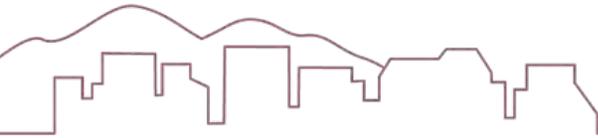
Base Scenario

This scenario consists of the density, number of units and unit type allowed under current General Plan and Development Code requirements. All of the units are sold or rented at market rates. The inclusionary scenario is derived from the base scenario, and the feasibility of the in-lieu fee is evaluated for the base scenario.

Inclusionary Scenario

Most of the housing being built in Menifee today is owner-occupied. With ownership housing, the primary affordable housing challenge is that, even at a reduced price, each household must still have the ability to pay (a down payment and meet debt-to-income limits) and the willingness to pay (credit score) to qualify for a conventional mortgage. Inclusionary housing programs tend to set the requirements for for-sale housing development for moderate-income households.

In addition, there is no state density bonus for low-income or moderate-income affordable units if they comprise less than ten percent of the total number of units in a project. Some inclusionary housing programs leave it to the developer to balance the number of affordable units by income classification in order to obtain the density bonus that best fits the site and supports financial feasibility. Table 9 shows the density bonus that each income-category of housing would receive at three different percentages of the total number of housing units. In the absence of a specific requirement for each income category, a developer



would weigh the required subsidy (in reduced rent or sales value) against the increased project return from bonus market rate units when deciding how many units to provide in each income category to achieve an overall project inclusion of 15 percent affordable units.

Table 9: Density Bonus (Percent Increase in Total Number of Units) for 5, 10, and 15 Percent Inclusionary Affordable Unit Requirements

	Percentage of Affordable Units Provided		
	15% Affordable	10% Affordable	5% Affordable
Very Low Income	50%	32.5%	20%
Low Income	27.5%	20%	0%
Moderate Income	10%	5%	0%

Source: California Government Code Sections 65915 – 65918

For this analysis, the inclusionary scenario includes the base scenario with the required number of affordable inclusionary units plus the additional density bonus market-rate units. The for-sale development scenarios are evaluated with at ten percent of the units affordable to moderate-income households and five

Table 10: HCD Income Limits by Household Size and Income Classification; Riverside County; 2023

Number of People:	1	2	3	4	5	6	7	8	9
Income Classification									
Very low-income household	32,650	37,300	41,950	46,600	50,350	54,100	57,800	61,550	65,278
Low-income household	52,200	59,650	67,100	74,550	80,550	86,500	92,450	98,450	104,414
Moderate-income household	79,400	90,700	102,050	113,400	112,450	131,550	140,600	149,700	158,772

Source: PlaceWorks, 2024, using data from the CA Department of Housing and Community Development.

percent affordable to very low-income households. Similarly, the for-rent development scenarios are evaluated with ten percent of the units affordable to low-income households and five percent affordable to very low-income households.

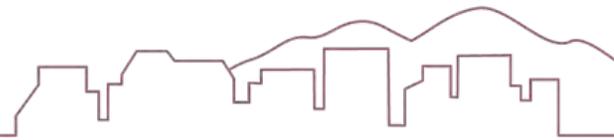
Sensitivity Analysis

The pro forma modelling includes sensitivity analyses that test the impact of a range of changes to key inputs. This type of analysis looks at the extent to which feasibility would be impacted under changing market or other assumptions. Inputs altered as part of the sensitivity analysis include:

- + Rental rates
- + Sales values
- + Residual land value
- + Project densities and combinations of housing project product types

AFFORDABLE HOUSING PAYMENTS

The housing payment considered to be affordable for a given household is determined by household size and income. The calculated affordable housing



payment is unrelated to the size (square footage) of the dwelling units (provided it has the appropriate number of bedrooms), the type of housing (single-family detached, townhouse, condo, or apartment), or the market-rate price of the unit. The calculated affordable housing payments used in the analysis are provided below.

Housing Income Classifications

There are several related but distinct income classifications used for public programs. This analysis is based on the most common classification for housing programs, the state Department of Housing and Community Development (HCD) Income Limits. Table 10 provides the HCD income limits for Riverside County for 2023. The income levels are based on the area median income (AMI) which is calculated on a countywide basis. The data indicate that maximum income that a household with a given number of people can earn and be included in each income classification.

Thus, a 3-person household with an annual income of \$40,000 would be classified as very low income, while a 3-person family with an annual income of \$60,000 would be classified as low income. When purchasing a home with some sort of public subsidy, support, or write-down, the household's actual income is used to determine the affordable housing payment. For planning purposes, the maximum income for each income classification is used to determine the affordable housing payment and, thus, the affordable sales price.

Affordable-Housing Sales Prices and Rents

The price at which affordable owner-occupied housing can be sold is based on annual income and household size. The affordable sales prices are calculated in Table 11 for very low-income, low-income, and moderate-income households. Similarly, the rent which may be charged for affordable renter occupied

housing is based on income and household size. The affordable rents are calculated in Table 12, starting on page 61.

For a 3-person low-income household, for whom HCD would require a 3-bedroom home, the affordable purchase price is \$107,281, inclusive of a \$6,860 down payment. The affordable rent for this household would be \$1,482 per month.



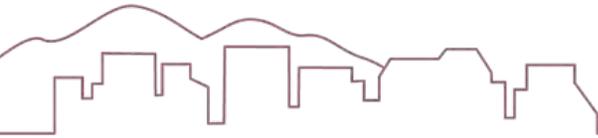


Table 11: Calculation of Affordable-Housing Sales Price by Household Size and Income Classification; Menifee; 2023

Household Size	1	2	3	4	5	6	7	8	9
Very Low-Income Households									
Annual income ¹	32,650	37,300	41,950	46,600	50,350	54,100	57,800	61,550	65,278
Affordable housing cost (@30%) ²	9,795	11,190	12,585	13,980	15,105	16,230	17,340	18,465	19,583
Utility allowance ³	1,962	2,028	2,352	2,676	2,676	2,988	3,336	3,336	0
Annual housing affordable payment ⁴	7,833	9,162	10,233	11,304	12,429	13,242	14,004	15,129	19,583
Monthly housing affordable payment ⁴	653	764	853	942	1,036	1,104	1,167	1,261	1,632
Present value of payments	103,380	120,920	135,055	149,190	164,037	174,767	184,824	199,672	258,461
Other housing costs ⁵	274	320	358	395	435	463	490	529	685
Mortgage amount	60,006	70,187	78,392	86,596	95,215	101,443	107,280	115,898	150,022
Mortgage payment ⁶	379	443	495	547	601	641	677	732	947
Total monthly payment	653	764	853	942	1,036	1,104	1,167	1,261	1,632
Affordable purchase price⁶	63,164	73,881	82,518	91,154	100,226	106,782	112,926	121,998	157,918

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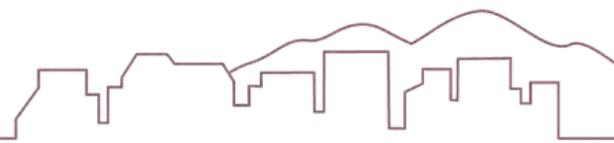


Table 11 continued

Household Size	1	2	3	4	5	6	7	8	9
Low-Income Households									
Annual income ¹	52,200	59,650	67,100	74,550	80,550	86,500	92,450	98,450	104,414
Affordable housing cost (@30%) ²	15,660	17,895	20,130	22,365	24,165	25,950	27,735	29,535	31,324
Utility allowance ³	1,962	2,028	2,352	2,676	2,676	2,988	3,336	3,336	0
Annual housing affordable payment ⁴	13,698	15,867	17,778	19,689	21,489	22,962	24,399	26,199	31,324
Monthly housing affordable payment ⁴	1,142	1,322	1,482	1,641	1,791	1,914	2,033	2,183	2,610
Present value of payments	180,786	209,412	234,633	259,855	283,611	303,052	322,017	345,773	413,416
Other housing costs ⁵	479	555	622	688	751	803	853	916	1,095
Mortgage amount	104,936	121,552	136,191	150,831	164,620	175,904	186,913	200,702	239,965
Mortgage payment ⁶	663	767	860	952	1,039	1,111	1,180	1,267	1,515
Total monthly payment	1,142	1,322	1,482	1,641	1,791	1,914	2,033	2,183	2,610
Affordable purchase price⁶	110,459	127,949	143,359	158,769	173,284	185,163	196,750	211,265	252,594

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Table 11 continued

Household Size	1	2	3	4	5	6	7	8	9
Moderate-Income Households									
Annual income ¹	79,400	90,700	102,050	113,400	112,450	131,550	140,600	149,700	158,772
Affordable housing cost (@30%) ²	23,820	27,210	30,615	34,020	33,735	39,465	42,180	44,910	47,632
Utility allowance ³	1,962	2,028	2,352	2,676	2,676	2,988	3,336	3,336	0
Annual housing affordable payment ⁴	21,858	25,182	28,263	31,344	31,059	36,477	38,844	41,574	47,632
Monthly housing affordable payment ⁴	1,822	2,099	2,355	2,612	2,588	3,040	3,237	3,465	3,969
Present value of payments	288,481	332,351	373,014	413,677	409,916	481,422	512,662	548,692	628,640
Other housing costs ⁵	764	880	988	1,096	1,086	1,275	1,358	1,454	1,665
Mortgage amount	167,447	192,911	216,514	240,116	237,933	279,438	297,571	318,485	364,890
Mortgage payment ⁶	1,057	1,218	1,367	1,516	1,502	1,764	1,879	2,011	2,304
Total monthly payment	1,822	2,099	2,355	2,612	2,588	3,040	3,237	3,465	3,969
Affordable purchase price⁶	176,260	203,064	227,909	252,754	250,456	294,146	313,233	335,247	384,095

Source: PlaceWorks, 2024, using data from the CA Department of Housing and Community Development and the Riverside County Housing Authority.

Notes to Table 11:

1. Data for annual income limit by household size and income classification is from Table 10.
2. The total payment for housing costs is considered to be affordable at 30 percent of household income.
3. Annual utility allowance data are based on the Riverside County Housing Authority Utility Allowances.
4. The annual housing affordable payment is the affordable housing cost less the utility allowance. The monthly housing affordable payment is the annual payment divided by 12.
5. Other housing costs assume a 5 percent down payment and a 95 percent loan to value ratio and include 1 percent taxes, 1 percent annual private mortgage insurance, and 0.57 percent annual homeowners' insurance.
6. The mortgage payment is the monthly housing affordable payment less other housing costs. The affordable purchase price is based on the mortgage payment and assumes a 30-year fixed rate mortgage with a 5 percent down payment and a 6.5 percent annual percentage rate.

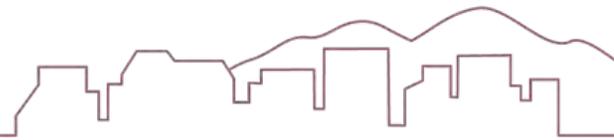


Table 12: Calculation of Affordable-Housing Rent by Household Size and Income Classification; Menifee; 2023

Household Size	1	2	3	4	5	6	7	8	9
Very Low-Income Households									
Annual income	32,650	37,300	41,950	46,600	50,350	54,100	57,800	61,550	65,278
Affordable housing cost (@30%)	9,795	11,190	12,585	13,980	15,105	16,230	17,340	18,465	19,583
Utility allowance	1,962	2,028	2,352	2,676	2,676	2,988	3,336	3,336	0
Annual housing affordable payment	7,833	9,162	10,233	11,304	12,429	13,242	14,004	15,129	19,583
Monthly Affordable Rent	653	764	853	942	1,036	1,104	1,167	1,261	1,632
Low-Income Households									
Annual income	52,200	59,650	67,100	74,550	80,550	86,500	92,450	98,450	104,414
Affordable housing cost (@30%)	15,660	17,895	20,130	22,365	24,165	25,950	27,735	29,535	31,324
Utility allowance	1,962	2,028	2,352	2,676	2,676	2,988	3,336	3,336	0
Annual housing affordable payment	13,698	15,867	17,778	19,689	21,489	22,962	24,399	26,199	31,324
Monthly Affordable Rent	1,142	1,322	1,482	1,641	1,791	1,914	2,033	2,183	2,610
Moderate-Income Households									
Annual income	79,400	90,700	102,050	113,400	112,450	131,550	140,600	149,700	158,772
Affordable housing cost (@30%)	23,820	27,210	30,615	34,020	33,735	39,465	42,180	44,910	47,632
Utility allowance	1,962	2,028	2,352	2,676	2,676	2,988	3,336	3,336	0
Annual housing affordable payment	21,858	25,182	28,263	31,344	31,059	36,477	38,844	41,574	47,632
Monthly Affordable Rent	1,822	2,099	2,355	2,612	2,588	3,040	3,237	3,465	3,969

Source: PlaceWorks, 2024, using data from the CA Department of Housing and Community Development and the Riverside County Housing Authority.



Notes to Table 12:

1. Data for annual income limit by household size and income classification is from Table 10.
2. The total affordable housing payment is considered to be 30 percent of household income.
3. Annual utility allowance data are based on the Riverside County Housing Authority Utility Allowances.
4. The annual housing affordable payment is the affordable housing cost less the utility allowance. The monthly housing affordable payment is the annual payment divided by 12.

9. In-Lieu Fee

An inclusionary housing ordinance is commonly included in inclusionary housing programs as a method of compliance as an alternative to the developer providing the required number of affordable units on the same site as a new residential development project. State law requires that payment of an in-lieu fee be an alternative for residential for-rent projects, but it is often allowed on for-sale residential projects too.

This section provides a rationale for setting the amount of the fee. It is presented before the financial feasibility analysis of the development scenarios so that it can be evaluated with each scenario.

METHODOLOGY

General Approach

The general approach is to determine the typical cost for the City to have an affordable housing unit built. The in-lieu fee would then be set at a level that would generate sufficient revenue to have the required number of affordable units built.

Example

Take, for example, a hypothetical residential subdivision that would have 100 lots. The inclusionary housing provisions would require that 15 of the units (15 percent of the total) be Below Market-Rate units (BMR) that are restricted to income-qualified households. The remaining 85 units would be sold at market rate (MR) prices.

If, instead of a mixed-income development project (i.e., 15 BMR and 85 MR units), the developer chose the alternative of paying an in-lieu fee, the

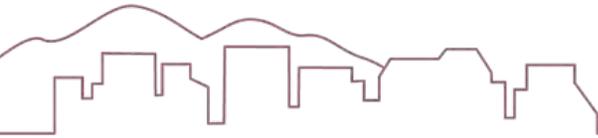
proposed project would have 100 MR units, and the total amount of in-lieu fees paid should be sufficient to have 15 affordable housing units constructed elsewhere in Menifee.

If that cost were \$200,000 per affordable unit, then the in-lieu fee for the project should be at least \$3 million (15 BMR units X \$200,000 per unit = \$3 million). Because the developer's proposed project has 100 MR houses, the in-lieu fee, on a per unit basis, would be \$30,000 (\$3 million total ÷ 100 MR units = \$30,000 per unit).

Affordable Housing Development Finance

Most affordable housing is constructed and operated by specialized affordable housing developers. They have expertise in accessing a variety of funding sources, and they have expertise in qualifying income-eligible households. The recommended fee derived in subsequent sections is based on five Riverside County affordable housing projects that the state awarded tax credits to in 2021 and 2022.

There are three important types of funding for the permanent financing of affordable housing developments. First and foremost are Low-Income Housing Tax Credits (LIHTC). These are tax credits that the federal government annually provides to states to distribute to affordable housing development projects. In California, the Tax Credit Allocation Committee awards tax credits on a competitive basis annually. Affordable housing developers have indicated that it is not uncommon for an application to take up to three rounds before being successful. However, they have also indicated that they are rather confident in



their ability to eventually receive tax credit funding for projects.³ For the five Riverside County affordable housing projects, tax credits accounted for 51 percent to 64 percent of the total permanent financing.

Affordable housing projects also rely on conventional bank financing for permanent funding, just as market rate developers do. Residents of affordable housing projects pay rent—albeit a reduced rent that is affordable. These rent payments cover the operation and maintenance expenses. The amount of rent in excess of operation and maintenance costs is used to repay the conventional bank financing.

Finally, there are all the other sources of funding. Part of the art of affordable housing development is being able to piece together a variety of other funding sources to fully fund a development. Part of the challenge is timing these other sources to coincide with the awarding of tax credit funding.

Fee Basis

Affordable housing developers have indicated their confidence in obtaining tax credits and conventional bank financing. If funding from in-lieu fees can make up the difference from all the other funding sources they usually piece together, they should be able to develop affordable housing in Menifee. Thus, the basis for the in-lieu fee is the gap between the development cost and the tax credit funds plus bank financing. This amount is calculated below.

³ There are two types of LIHTC, commonly referred to as 4 percent credits and 9 percent credits. The affordable housing developers interviewed for this report say that the 9 percent credits are very challenging

AFFORDABLE HOUSING GAP CALCULATION

Based on a breakdown of the development costs for each of the five Riverside County affordable housing projects, Table 13 provides the total development cost for all five projects combined, and the weighted average development cost per unit. The data indicated that, on average, each unit of affordable housing costs \$405,000.

Table 13: Weighted Average Development Cost per Unit for Recent Affordable Housing Projects; Riverside County; 2022

Total Development Cost	\$260,920,803
Total Number of Units	644
Average Development Cost per Unit	\$405,157

Source: PlaceWorks 2023, using data from the CA Tax Credit Allocation Committee.

Based on a review of the funding sources used for permanent financing of the five Riverside County affordable housing projects, Table 14, on the following page, shows the total permanent bank financing and the total federal tax credit equity as well as the weighted average per unit. The data indicate that, on average, the typical affordable housing unit is funded with \$81,200 in conventional bank financing and \$175,300 in federal tax credits.

to get but that they are confident that they can obtain 4 percent tax credits for affordable housing projects. References to tax credits in this report refer to the 4 percent tax credits.

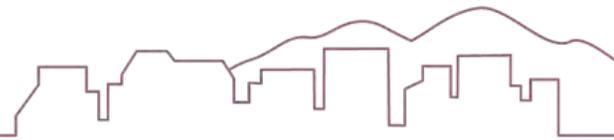


Table 14: Weighted Average Bank Financing and Federal Tax Equity per Unit for Recent Affordable Housing Projects; Riverside County; 2022

Total Number of Units	644
Total Permanent Bank Financing	\$52,306,087
Average Bank Financing per Unit	\$81,221
Total 4% Federal Tax Credit Equity	\$112,904,222
Average Tax Credit Equity per Unit	\$175,317

Source: PlaceWorks 2023, using data from the CA Tax Credit Allocation Committee.

The affordable housing financing gap—which is the amount that the inclusionary housing in-lieu fee would cover—is the difference between the development cost and the two types of permanent financing that affordable housing developers can reliably access. As shown in Table 15, the average affordable housing financing gap in Riverside County in 2022 was \$148,600.

Table 15: Average Affordable Housing Financing Gap for Recent Affordable Housing Projects; Riverside County; 2022

Average Development Cost per Unit	\$405,157
Less Average Bank Financing per Unit	-\$81,221
Less Average Tax Credit Equity per Unit	-\$175,317
Affordable Housing Gap per Unit	\$148,619

Source: PlaceWorks 2023, using data from the CA Tax Credit Allocation Committee.

The financial data used in the analysis above were reported by the CA Tax Credit Allocation Committee in June 2022. Since then, inflation has increased costs.

While there are construction cost indices and other inflation adjustments, the US Bureau of Labor Statistics' reported Consumer Price Index is often used to adjust for inflation over time for many planning and building fees and charges. Table 16 shows the current subsidy required per affordable unit, adjusted for inflation to June 2023 dollars. Thus, a fee adopted today would need to generate \$154,372 per affordable unit to overcome the expected financing gap.

Table 16: Average Affordable Housing Financing Gap, Adjusted for Inflation; Riverside County; September 2023

	Required Subsidy per Affordable Unit	CPI
Value in June 2022	\$148,619	165.553
Value in June 2023	\$154,372	171.962

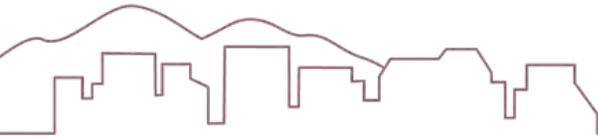
Source: PlaceWorks 2023, using data from the US Bureau of Labor Statistics, Consumer Price Index, All items in U.S. city average, all urban consumers, chained, not seasonally adjusted (C-CPI-U).

FEE CALCULATION

The city could adopt a fee of \$154,372 per affordable housing unit that is required under an inclusionary housing ordinance when the developer chooses to forego construction of those units onsite. The financial feasibility analysis in the next section of this report evaluates the impact of this fee as applied to the number of required inclusionary housing units.

Fee per Market Rate Unit

However, to facilitate an easier application of the in-lieu fee in practice, most cities structure the fee on the basis of the number of market rate units being



constructed. The financial feasibility analysis below evaluates a 15 percent inclusionary housing requirement, although other levels are also considered. With a 15-percent inclusionary requirement, each group of 20 new dwelling units would need to include 3 affordable units and 17 market rate units. If the developer chooses not to build the affordable units, then all 20 units would be market rate, and the in-lieu fee across all 20 units would need to add up to the affordable housing financing gap for three affordable units, \$463,117 ($\$155,372 \times 3$). This works out to \$23,156 per market rate unit ($\$463,117 \div 20$ market rate units).

With a 5-percent inclusionary requirement, each group of 20 new dwelling units would need to include 1 affordable unit and 19 market rate units. If the developer chooses not to build the affordable units onsite, then all 20 units would be market rate, and the in-lieu fee across all 20 units would need to add up to the affordable housing financing gap for one affordable housing unit, \$155,372. This works out to \$7,769 per market rate unit, as shown in Table 17.

Table 17: In-Lieu Fee per Market Rate Unit with a 5% Inclusionary Requirement

Affordable Housing Gap per Affordable Unit	\$154,372
Number of Market Rate Units per Affordable Unit	20
In-Lieu Fee per Market Rate Unit	\$7,719

Source: PlaceWorks, 2024.

Fee per Square Foot

Finally, some cities decide to establish their fee on a per square foot basis, by dividing the fee per market rate unit by the average size of new housing. In this case, larger than average housing units pay a higher fee, and smaller than average units pay a smaller fee. Over time, however, the total fee collected should average out to generate the same amount of funding as a per market rate unit fee would generate. A per square foot-based fee has the effect of creating a sliding scale. Higher density types of housing tend to have smaller unit sizes than lower density housing types. Thus, the total fee paid by higher density development may still be more on a per acre basis, but it would be less on a per unit basis than the fee for lower density housing.

For the housing sales data used in the financial feasibility analyses in the next section of this report, the average finished floor area (i.e., excluding garages) was 2,389.7 square feet. For a 15-percent inclusionary housing requirement, the in-lieu fee would be \$3.23 per square foot, as shown in Table 18.

Table 18: In-Lieu Fee per Square Foot with a 5% Inclusionary Requirement

Affordable Housing Financing Gap per MR Unit	\$7,719
Average Unit Size	2,389.7 sq. ft.
Fee per sq. ft.	\$3.23/sq. ft.

Source: PlaceWorks, 2024.

10. Development Scenarios

This section of the report describes each development scenario, estimates the development costs and project income, and evaluates the financial feasibility. The scenarios reflect generalized development patterns that are typical and/or allowable under current planning and zoning and to provide a generalized indication of the financial feasibility impacts of a 15 percent inclusionary housing requirement. The scenarios do not reflect any particular lot or parcel nor location in the city. The financial feasibility of any prototypes on a specific site should be expected to vary from the generalized analysis provided below.

SCENARIO 1: LARGER LOT SINGLE-FAMILY DETACHED HOUSING

Scenario Description

This scenario reflects a theoretical larger-lot single-family detached housing subdivision development. The analysis assumes that the base development scenario would provide 220 3- to 6-bedroom houses on a 55-acre site. This represents a gross density of 4.0 units per acre, before taking streets and open space out of the calculation. For the inclusionary housing scenario, 10 percent of the 220 units (22 units) would be moderate-income units. Five percent of the total number of units (11 units) would be very-low-income units. The inclusionary housing scenario receives a 25 percent density bonus, an additional 55 market rate units, for a total of 275 units. Thus, from the base scenario of 220 units, the inclusionary scenario has 242 market rate units and 33 affordable units. With this number of housing units, the gross density increases to 5.0 units per acre. This increase in density does not require any fundamental change in product type to be physically accommodated on the site.

Table 19: Scenario 1, Development Description

Unit Type	Base Development Scenario	Inclusionary Housing Scenario		
	Total Number of Units	Below Market-Rate Units	Market-Rate Units	Total Number of Units
3-Bedroom	70	10	77	87
4-Bedroom	70	10	77	87
5-Bedroom	50	8	55	63
6-Bedroom	30	5	33	38
Total	220	33	242	275
Site Area (acres)	55.0			55.0
Gross Density (du/ac)	4.0			5.0

Source: PlaceWorks, 2024.

Project Income

In a for-sale development, the project income is derived from the sale of housing units. Table 20 provides the unit types, sizes, and expected sales values for market-rate and below market-rate units. As discussed below, this scenario incorporates Mello Roos funding for water, sewer, and roads. The property owner payments for the Mello Roos fees for the below market-rate units are deducted from the affordable housing payment. Thus, the average sales price for these units is lower than presented in Table 11.

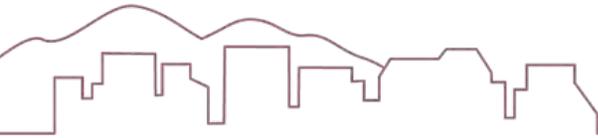


Table 20: Scenario 1, Average Unit Sizes and Average Sales Values (in current dollars)

	3-Bedroom	4-Bedroom	5-Bedroom	6-Bedroom
Size (sq. ft.)	1,480	1,970	2,270	3,470
Market Rate Price	689,000	713,000	728,000	786,000
Below-Market Rate Price	135,500	186,000	190,200	207,000
Difference	553,000	527,000	538,000	580,000
	80.3%	73.9%	73.9%	73.7%

Source: PlaceWorks, 2024.

Notes to Table 20:

- Unit types, sizes, and market-rate sales values are PlaceWorks assumptions based on our assessment of the current market, including an assessment of home sales values in 2022, adjusted for inflation into 2023 dollars.
- Below market-rate sales values are based on the data in Table 11 and Table 12, assuming that 3-bedroom units are a mix of 3- and 4-person households, 4-bedroom units are 5-person households, 5-bedroom units are a mix of 7- and 8-person households, and 6-bedroom units are 9-person households. In this scenario, the affordable housing price has been reduced to account for the payment of CFD/HOA fees for the cost for road, water, and sewer infrastructure.

Based on the number of units provided in Table 19 and the sales values provided in Table 20, the resulting gross sales value and the net sales value after sales commissions for the base development scenario and the inclusionary housing scenario are provided in Table 21.

The average sales value across all units are 9.1 percent lower for the inclusionary housing scenario, due primarily to the decrease in affordable purchase price resulting from the Mello Roos fees; even the additional income from bonus

market rate units is insufficient to ameliorate this decrease. Nevertheless, the gross and net sales values are 13.7 percent higher under the inclusionary housing scenario.

Table 21: Scenario 1: Project Income

	Base Development Scenario	Inclusionary Housing Scenario
Average unit sales value	719,000	653,000
Gross sales value	158,000,000	180,000,000
Less sales commission	-7,904,000	-8,983,000
Total Net Sales Value	150,000,000	171,000,000

Source: PlaceWorks, 2024.

Project Costs

Estimated project costs are provided in Table 22. The overall cost increases with additional units, from \$129 million for the base development scenario to \$154 million for the inclusionary housing scenario. However, the cost per unit decreases with fixed costs, such as land acquisition, spread across more units, and smaller lots with smaller frontages resulting in less roadway, water, and sewer per unit. The analysis estimates that the total development cost (before financing costs are added in) would increase by 19 percent with the inclusionary housing scenario, but the per unit cost would decrease by 4.9 percent.

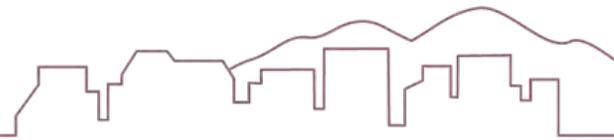


Table 22: Scenario 1: Project Costs

	Base Development Scenario	Inclusionary Housing Scenario
Estimated Land Cost	22,660,000	22,660,000
Hard Costs		
Site work (w/water & sewer)	11,590,000	14,940,000
Building construction	76,900,000	93,300,000
Circulation and parking	5,040,000	6,300,000
Landscaping	8,290,000	7,370,000
Hard cost subtotal	101,800,000	122,000,000
Soft Costs		
Design, entitlement, contingency, and other	15,270,000	18,290,000
Development Impact Fees	12,100,000	13,310,000
Soft costs subtotal	27,400,000	31,600,000
Total Development Cost		
Total cost (before financing)	129,200,000	153,600,000
- per unit	587,000	558,000

Source: PlaceWorks, 2024.

Notes to Table 22:

1. The estimated land cost is a PlaceWorks estimate based on our analysis of sales data, asking prices, and residual land values. There are few land sales, and reported prices vary, likely reflecting current zoning and existing entitlements, expectations for rezonings, topography, proximity to existing infrastructure and other factors. The analysis assumes a 5 percent land cost allowance for due diligence activities related to land acquisition. The cash flow model

assumes monthly option payments of 1 percent of the estimated property value during the entitlement period, but the option payments are part of the overall payment for land acquisition rather than an additional cost.

2. Building construction costs are calculated on a per square foot basis for finished floor area and a separate square foot basis for garages. The per square foot costs are taken from Craftsman Book Company's 2023 National Building Cost Manual, with the source's recommended adjustments for local cost differential. As noted in the source, the per square foot cost estimates include all construction costs: labor, materials, equipment, plans, building permit, supervision, overhead, and profit.
3. Development impact fees are calculated at approximately \$55,000 per dwelling unit. The analysis assumes that development impact fees are charged to market-rate units but not below market-rate units.

Financial Feasibility

Table 23 summarizes the financial feasibility of Scenario 1. The analysis finds that the base development scenario is financially feasible, generating an IRR of 17.9 percent. In contrast, the inclusionary housing scenario, as analyzed, would generate an IRR of 6.4 percent. Because this return is below the 15 percent threshold, this scenario is not financially feasible to develop.

Simply requiring 15 percent inclusionary housing and relying on the State Density Bonus Law to provide the incentive is not financially feasible with the assumed income-class distribution of affordable housing. This inclusionary housing scenario would require an additional \$4.1 million subsidy in order to be feasible.

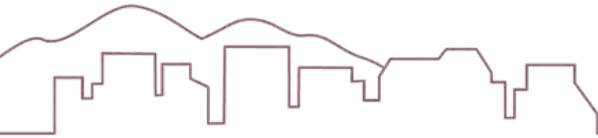


Table 23: Scenario 1: Financial Feasibility Summary

	Base Development Scenario	Inclusionary Housing Scenario
Development cost	129,200,000	153,600,000
Financing cost	12,180,000	13,290,000
Total project cost	141,000,000	167,000,000
Construction loan amount	107,100,000	128,200,000
Required equity	34,200,000	38,600,000
Net project income	9,920,000	3,800,000
Project IRR	17.9%	6.4%
Surplus/(Gap) w/15% IRR	1,300,000	-4,140,000
Residual land value w/15% IRR	23,264,000	17,857,000

Source: PlaceWorks, 2024.

Notes to Table 23:

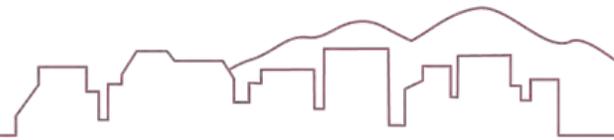
1. Financing cost includes construction loan fees of 2.5 percent and an interest rate of 8.6 percent. The current interest rate report by realtyrates.com for residential construction loans of 10.6 percent. The analysis assumes that interest rates will decline by two percentage points over the next two years. The total project costs are the development cost, from Table 22, plus the financing cost.
2. The construction loan amount is based on 50 percent of land acquisition and 84 percent of other construction costs, based on data from realtyrates.com.
3. The IRR is an annual rate of return based on monthly cash flow, assuming a 6-month entitlement period, 4 months of site work, 18 months of construction, and 3 months to complete sales. This is a somewhat simplified phasing schedule from what should be expected for actual development projects.

Sensitivity Analysis

The analysis considered other alternatives to achieve financial feasibility. First is the in-lieu fee. The base development scenario is estimated to generate a surplus residual land value of \$1.3 million. The in-lieu fee being evaluated in this report is \$154,372 per inclusionary unit. With a 15 percent inclusionary requirement, this project could comply with the inclusionary requirement with payment of a total in-lieu fee of \$5,094,283 (154,372 \$/inclusionary unit X 33 required inclusionary units). This fee is more than the estimated surplus residual land value, indicating it would not be financially feasible to develop this project as a fully market-rate development and pay the in-lieu fee. However, there could be other site designs and product mixes that would generate a sufficiently high rate of return to make the fee financially feasible.

Reducing the inclusionary requirement to 10 percent affordable units, with all moderate-income households, results in total development costs, including financing, that exceed the project income, and thus, is not feasible. In contrast, lowering the requirement to five percent affordable units, with all very-low-income households (because there are no density bonus units granted for five percent inclusionary housing with low-income or with moderate-income households) generates an IRR of 15.9 percent. This is not as lucrative, from a financial feasibility perspective, as the base development scenario, but it is more lucrative than achieving the inclusionary requirement through the payment of an in-lieu fee.

Finally, the analysis assesses changes in market-rate sales value. The sale values would have to increase by 3.2 percent for the inclusionary housing scenario in Table 23 to be financially feasible. However, with this increase, the inclusionary housing project is not as lucrative as the base development scenario and paying the in-lieu fee.



SCENARIO 2: SMALL LOT SINGLE-FAMILY HOUSING

Scenario Description

This scenario incorporates small lots with single-family detached houses and a smaller number of single-family attached units. The analysis assumes that the base development scenario would provide a total of 303 housing units, with 211 single-family detached units and 92 single-family attached duplex units. Situated on a site of 28.4 acres, the base development scenario results in a gross density of 10.7 units per acre.

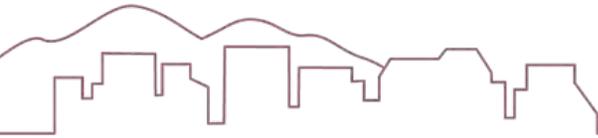
The inclusionary housing scenario, with 10 percent moderate-income units and 5 percent very-low-income units, would be eligible for a 25 percent density bonus, or an increase of 76 units. With a total of 379 housing units on the site, the gross density would increase to 13.3 units per acre. It does not appear that the original types of housing could be simply reconfigured to achieve this density. Therefore, the analysis evaluates an alternative development in which the number of single-family detached units is decreased, and the majority of the housing is single-family-attached townhouses. There are other types of development that could be considered, each of which could generate a different financial feasibility result.

This points to one of the challenges with using density bonus to offset the costs of inclusionary housing. Achieving the density bonus can, at times, result in the need to switch to a denser product type, for which there may or may not be the same market demand. In this example, there are 211 single-family detached units out of 303 total units in the base development scenario, and there are 166 single-family detached units out of 379 total units in the inclusionary housing scenario, with townhouses accounting for the other 213 units.

Table 24: Scenario 2, Development Description

Unit	Base Development Scenario	Inclusionary Housing Scenario		
	Total Number of Units	Below Market-Rate Units	Market-Rate Units	Total Number of Units
SFD-A	39	0	31	31
SFD-B	47	0	37	37
SFD-C	39	0	31	31
SFD-D	33	0	26	26
SFD-E	31	0	24	24
SFD-F	22	0	17	17
SFA-G	18			
SFA-H	18			
SFA-I	28			
SFA-J	28			
TH-1		9	33	42
TH-2		24	83	107
TH-3		14	50	64
Total	303	47	332	379
Site Area (acres)	28.4			28.4
Gross Density (du/ac)	10.7			13.3

Source: PlaceWorks, 2024.



Project Income

In a for-sale development, the project income is derived from the sale of housing units. Table 25 provides the unit types, sizes, and expected sales values for market-rate and below market-rate units. As discussed below, this scenario incorporates Mello Roos funding for water, sewer, and roads. The property owner payments for the Mello Roos fees for the below market-rate units are deducted from the affordable housing payment. Thus, the average sales price for these units is lower than presented in Table 11.

As shown in Table 25, the townhouse units are generally smaller and less costly than the single-family detached and most of the single-family attached units that they replace for the inclusionary housing scenario.

Based on the number of units provided in Table 24 and the sales values provided in Table 25, the resulting gross sales value and the net sales value after sales commissions for the base development scenario and the inclusionary housing scenario are provided in Table 26 on page 73.

The average sales value across all units is 12.2 percent lower for the inclusionary housing scenario. The average price is lower due to the decrease in affordable purchase price resulting from the Mello Roos fees and due to the substitution of 213 townhouses with slightly lower average prices. Nevertheless, the gross and net sales values are 9.8 percent higher under the inclusionary housing scenario.

Table 25: Scenario 2, Average Unit Sizes and Average Sales Values (in current dollars)

	Size (sq. ft.)	Market-Rate Price	Below Market-Rate Price	Difference	
SFD-A	1,460	624,000			
SFD-B	1,510	626,000			
SFD-C	1,670	633,000			
SFD-D	1,680	634,000			
SFD-E	2,090	652,000			
SFD-F	1,970	647,000			
SFA-G	1,460	563,000			
SFA-H	1,510	569,000			
SFA-I	1,670	594,000			
SFA-J	1,680	595,000			
TH-1	1,230	520,000	200,000	321,000	-38.4%
TH-2	1,460	547,000	189,000	357,000	-34.6%
TH-3	1,760	580,000	196,000	384,000	-33.8%

Source: PlaceWorks, 2024.

Notes to Table 25:

1. Unit types, sizes, and market-rate sales values are PlaceWorks assumptions based on our assessment of the current market, including an assessment of home sales values in 2022, adjusted for inflation into 2023 dollars.
2. Below market-rate sales values are based on the data in Table 11 and Table 12. In this scenario, the affordable housing price has been reduced to account for the payment of CFD/HOA fees for the cost for road, water, and sewer infrastructure.

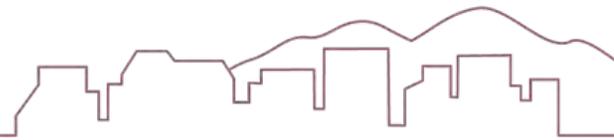


Table 26: Scenario 2: Project Income

	Base Development Scenario	Inclusionary Housing Scenario
Average unit sales value	619,000	543,000
Gross sales value	187,000,000	206,000,000
Less sales commission	-9,375,000	-10,293,000
Total Net Sales Value	178,000,000	196,000,000

Source: PlaceWorks, 2024.

Project Costs

Estimated project costs are provided in Table 27. The overall cost increases with additional units, from \$155 million for the base development scenario to \$178 million for the inclusionary housing scenario. However, the cost per unit decreases with fixed costs, such as land acquisition, spread across more units, and smaller lots with smaller frontages resulting in less roadway, water, and sewer per unit. The analysis estimates that the total development cost (before financing costs are added in) would increase by 15 percent with the inclusionary housing scenario, but the per unit cost would decrease by 7.8 percent.

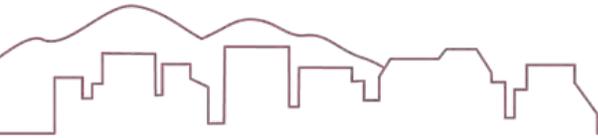
Table 27: Scenario 2: Project Costs

	Base Development Scenario	Inclusionary Housing Scenario
Estimated Land Cost	11,700,000	11,700,000
Hard Costs		
Site work (w/water & sewer)	9,110,000	10,930,000
Building construction	102,400,000	120,500,000
Circulation and parking	6,430,000	5,340,000
Landscaping	3,500,000	4,400,000
Hard cost subtotal	121,400,000	141,200,000
Soft Costs		
Design, entitlement, contingency, and other	18,210,000	21,180,000
Development Impact Fees	15,200,000	16,130,000
Soft costs subtotal	33,400,000	37,300,000
Total Development Cost		
Total cost (before financing)	154,800,000	178,500,000
- per unit	511,000	471,000

Source: PlaceWorks, 2024.

Notes to Table 27:

- The estimated land cost is a PlaceWorks estimate based on our analysis of sales data, asking prices, and residual land values. There are few land sales, and reported prices vary, likely reflecting current zoning and existing entitlements, expectations for rezonings, topography, proximity to existing infrastructure and other factors. The analysis assumes a 5 percent of land cost allowance for due diligence activities related to land acquisition. The cash flow model



assumes monthly option payments of 1 percent of the estimated property value during the entitlement period, but the option payments are part of the overall payment for land acquisition rather than an additional cost.

2. Building construction costs are calculated on a per square foot basis for finished floor area and a separate square foot basis for garages. The per square foot costs are taken from Craftsman Book Company's 2023 National Building Cost Manual, with the source's recommended adjustments for local cost differential. As noted in the source, the per square foot cost estimates include all construction costs: labor, materials, equipment, plans, building permit, supervision, overhead, and profit.
3. Development impact fees are calculated at approximately \$55,000 per dwelling unit. The analysis assumes that development impact fees are charged to market-rate units but not below market-rate units.

Financial Feasibility

Table 28 summarizes the financial feasibility of Scenario 2. The analysis finds that the fully market rate project is financially feasible, generating an IRR of 18.7 percent. In contrast, the inclusionary housing scenario, as analyzed, would generate an IRR of 10.5 percent. This is a better financial performance than Scenario 1, but it still is below the 15 percent threshold to be financially feasible to develop.

Simply requiring 15 percent inclusionary housing and relying on the State Density Bonus Law to provide the incentive is not financially feasible with the assumed income-class distribution of affordable housing. This inclusionary housing scenario would require an additional \$2 million subsidy in order to be feasible.

Table 28: Scenario 2: Financial Feasibility Summary

	Base Development Scenario	Inclusionary Housing Scenario
Development cost	154,800,000	178,500,000
Financing cost	13,200,000	14,170,000
Total project cost	168,000,000	193,000,000
Construction loan amount	133,800,000	153,800,000
Required equity	34,200,000	38,900,000
Net project income	9,460,000	5,780,000
Project IRR	18.7%	10.5%
Surplus/(Gap) w/15% IRR	1,500,000	-2,050,000
Residual land value w/15% IRR	12,846,000	9,307,000

Source: PlaceWorks, 2024.

Notes to Table 28:

1. Financing costs include construction loan fees of 2.5 percent and an interest rate of 8.6 percent. The current interest rate report by realtyrates.com for residential construction loans of 10.6 percent. The analysis assumes that interest rates will decline by two percentage points over the next two years. The total project costs are the development cost, from Table 27, plus the financing cost.
2. The construction loan amount is based on 50 percent of land acquisition and 84 percent of other construction costs, based on data from realtyrates.com.
3. The IRR is an annual rate of return based on monthly cash flow, assuming a 6-month entitlement period, 4 months of site work, 18 months of construction, and 3 months to complete sales. This is a somewhat simplified phasing schedule from what should be expected for actual development projects.

Sensitivity Analysis

The analysis considered other alternatives to achieve financial feasibility. First is the in-lieu fee. The base development scenario is estimated to generate a surplus residual land value of \$1.5 million. The in-lieu fee being evaluated in this report is \$154,372 per inclusionary unit. With a 15 percent inclusionary requirement, this project could comply with the inclusionary requirement with payment of a total in-lieu fee of \$7,255,484 (154,372 \$/inclusionary unit X 47 required inclusionary units). This fee is more than the estimated surplus residual land value, indicating it would not be financially feasible to develop this project as a fully market-rate development and pay the in-lieu fee.

Reducing the inclusionary requirement to 10 percent, with all moderate-income households, results in a development project that would generate an IRR of 18.3 percent, which would be financially feasible. Similarly, lowering the requirement to five percent, with all very-low-income households (because there are no density bonus units granted for five percent inclusionary housing with low-income or with moderate-income households) generates an even larger IRR, 22.3 percent. This is even more lucrative, from a financial feasibility perspective, than the base development scenario.

Finally, the analysis assesses changes in market-rate sales value. The sale values would have to increase by 2.6 percent for the inclusionary housing scenario to be financially feasible. With such an increase in sales values, the base development scenario would not be profitable enough for the payment of the in-lieu fee to be financially feasible.

SCENARIO 3: TOWNHOUSES

Scenario Description

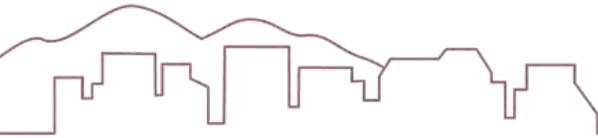
This scenario provides two-story, 2- and 3-bedroom townhouses, and attached two-car garages. The analysis assumes that the base development scenario would provide a total of 350 housing units. The size of the development site is 24.3 acres, which results in a gross density of 14.4 units per acre.

Table 29: Scenario 3, Development Description

Unit	Base Development Scenario	Inclusionary Housing Scenario		
	Total Number of Units	Below Market-Rate Units	Market-Rate Units	Total Number of Units
2-Bed/2_Bath	70	11	77	31
3-Bed/3-Bath	175	26	192	37
3-Bed/3.5 Bath	105	16	116	31
Total	350	53	385	438
Site Area (acres)	24.3			24.3
Gross Density (du/ac)	14.4			18.0

Source: PlaceWorks, 2024.

The inclusionary housing scenario, with 10 percent moderate-income units and 5 percent very-low-income units, would be eligible for a 25 percent density bonus, or an increase of 88 units. With a total of 438 housing units on the site, the gross density would increase to 18.0 units per acre. In the base



development scenario, the housing units would be two stories in height. To accommodate the density bonus and achieve the 18.0 units per acre density, the analysis assumes that the townhouses in the inclusionary housing scenario would be three stories in height. While the inclusionary housing scenario might be taller and have somewhat less landscaped open space, it is not a fundamentally different type of housing product.

Project Income

In a for-sale development, the project income is derived from the sale of housing units. Table 30 provides the unit types, sizes, and expected sales values for market-rate and below market-rate units.

Table 30: Scenario 3, Average Unit Sizes and Average Sales Values (in current dollars)

	Size (sq. ft.)	Market-Rate Price	Below Market-Rate Price	Difference	
2-Bed/2-Bath	1,225	614,000	127,100	486,000	-20.7%
3-Bed/3-Bath	1,460	624,000	153,800	470,000	-24.6%
3-Bed/3.5 Bath	1,755	637,000	158,900	478,000	-25.0%

Source: PlaceWorks, 2024.

Notes to Table 30:

- Unit types, sizes, and market-rate sales values are PlaceWorks assumptions based on our assessment of the current market, including an assessment of home sales values in 2022, adjusted for inflation into 2023 dollars.
- Below market-rate sales values are based on the data in Table 11 and Table 12. In this scenario, the affordable housing price has been reduced to account for the payment of CFD/HOA fees for the cost for road, water, and sewer infrastructure.

With a higher density, there is less water, sewer, and road infrastructure per unit. This development scenario can be developed without using Mello Roos / CFD financing. Accordingly, the affordable house price for income-qualified households is higher than in the previous scenarios, and the difference between market-rate sales values and below market-rate sales values is less.

Based on the number of units provided in Table 29 and the sales values provided in Table 30, the resulting gross sales value and the net sales value after sales commissions for the base development scenario and the inclusionary housing scenario are provided in Table 31. The average sales value across all units is 9.2 percent lower for the inclusionary housing scenario. Nevertheless, the gross and net sales values are 13.6 percent higher under the inclusionary housing scenario, reflecting added density bonus units.

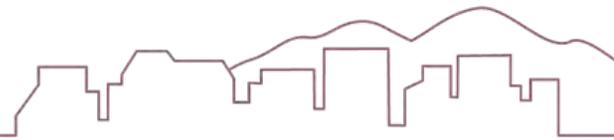
Table 31: Scenario 3: Project Income

	Base Development Scenario	Inclusionary Housing Scenario
Average unit sales value	626,000	568,000
Gross sales value	219,000,000	249,000,000
Less sales commission	-10,951,000	-12,444,000
Total Net Sales Value	208,000,000	236,000,000

Source: PlaceWorks, 2024.

Project Costs

Estimated project costs are provided in Table 32. The overall cost increases with additional units, from \$155 million for the base development scenario to \$178 million for the inclusionary housing scenario. However, the cost per unit decreases with fixed costs, such as land acquisition, spread across more units, and street frontage per unit, resulting in less roadway, water, and sewer per



unit. The analysis estimates that the total development cost (before financing costs are added in) would increase by 15 percent with the inclusionary housing scenario, but the per unit cost would decrease by 7.8 percent.

Table 32: Scenario 3: Project Costs

	Base Development Scenario	Inclusionary Housing Scenario
Estimated Land Cost	11,700,000	11,700,000
Hard Costs		
Site work (w/water & sewer)	9,110,000	10,930,000
Building construction	102,400,000	120,500,000
Circulation and parking	6,430,000	5,340,000
Landscaping	3,500,000	4,400,000
Hard cost subtotal	121,400,000	141,200,000
Soft Costs		
Design, entitlement, contingency, and other	18,210,000	21,180,000
Development Impact Fees	15,200,000	16,130,000
Soft costs subtotal	33,400,000	37,300,000
Total Development Cost		
Total cost (before financing)	154,800,000	178,500,000
- per unit	511,000	471,000

Source: PlaceWorks, 2024.

Notes to Table 32:

1. The estimated land cost is a PlaceWorks estimate based on our analysis of sales data, asking prices, and residual land values. There are few land sales, and reported prices vary, likely reflecting current zoning and existing entitlements, expectations for rezonings, topography, proximity to existing infrastructure and other factors. The analysis assumes a 5 percent of land cost allowance for due diligence activities related to land acquisition. The cash flow model assumes monthly option payments of 1 percent of the estimated property value during the entitlement period, but the option payments are part of the overall payment for land acquisition rather than an additional cost.
2. Building construction costs are calculated on a per square foot basis for finished floor area and a separate square foot basis for garages. The per square foot costs are taken from Craftsman Book Company's 2023 National Building Cost Manual, with the source's recommended adjustments for local cost differential. As noted in the source, the per square foot cost estimates include all construction costs: labor, materials, equipment, plans, building permit, supervision, overhead, and profit.
3. Development impact fees are calculated at approximately \$55,000 per dwelling unit. The analysis assumes that development impact fees are charged to market-rate units but not below market-rate units.

Financial Feasibility

Table 33 summarizes the financial feasibility of Scenario 3. The analysis finds that both scenarios are financially feasible, with base development scenario generating an IRR of 27 percent and the inclusionary housing scenario generating an IRR of 25.2 percent. The return for the base development scenario, when applying an in-lieu fee, decreases to an IRR of 20 percent, which suggests that the density bonus creates an incentive to the developer to provide the inclusionary housing units rather than paying the in-lieu fee.

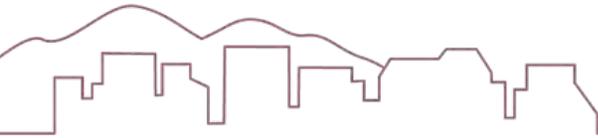


Table 33: Scenario 3: Financial Feasibility Summary

	Base Development Scenario	Inclusionary Housing Scenario
Development cost	154,800,000	178,500,000
Financing cost	13,170,000	14,110,000
Total project cost	168,000,000	193,000,000
Construction loan amount	133,800,000	153,700,000
Required equity	34,200,000	38,900,000
Net project income	14,090,000	14,590,000
Project IRR	27.0%	25.2%
Surplus/(Gap) w/15% IRR	5,000,000	4,740,000
Residual land value w/15% IRR	16,384,000	16,097,000

Source: PlaceWorks, 2024.

Notes to Table 33:

1. Financing costs include construction loan fees of 2.5 percent and an interest rate of 8.6 percent. The current interest rate report by realtyrates.com for residential construction loans of 10.6 percent. The analysis assumes that interest rates will decline by two percentage points over the next two years. The total project costs are the development cost, from Table 32, plus the financing cost.
2. The construction loan amount is based on 50 percent of land acquisition and 84 percent of other construction costs, based on data from realtyrates.com.
3. The IRR is an annual rate of return based on monthly cash flow, assuming a 6-month entitlement period, 4 months of site work, 18 months of construction, and 3 months to complete sales. This is a somewhat simplified phasing schedule from what should be expected for actual development projects.

Sensitivity Analysis

The analysis considered other alternatives to achieve financial feasibility. First is the in-lieu fee. As mentioned above, it is financially feasible for this development scenario to comply with an inclusionary housing requirement by paying an in-lieu fee.

Reducing the inclusionary requirement to ten percent, with all moderate-income households, results in a development project that would generate an IRR of 30.8 percent. Similarly, lowering the requirement to five percent, with all very-low-income households generates an even larger IRR, 44.8 percent.

SCENARIO 4: CONDOS

Scenario Description

This scenario provides for-sale multifamily housing in buildings with 10 to 12 units that includes some multilevel townhouse units and some flats. The buildings include at least one tuck-under garage parking space for each unit, with additional parking in surface parking spaces. The analysis assumes that the base development scenario would provide a total of 192 housing units. The size of the development site is 9.2 acres, which results in a gross density of 20.9 units per acre.

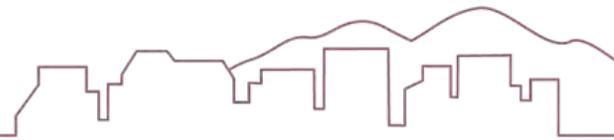


Table 34: Scenario 4, Development Description

Unit	Base Development Scenario	Inclusionary Housing Scenario		
	Total Number of Units	Below Market-Rate Units	Market-Rate Units	Total Number of Units
2 Bedrooms	114	18	125	143
3 Bedrooms	78	12	85	97
Total	192	30	210	240
Site Area (acres)	9.2			9.2
Gross Density (du/ac)	20.9			26.1

Source: PlaceWorks, 2024.

The inclusionary housing scenario, with 10 percent moderate-income units and 5 percent very-low-income units, would be eligible for a 25 percent density bonus, or an increase of 48 units. With a total of 240 housing units on the site, the gross density would increase to 26.1 units per acre. In the base development scenario, the housing units would be three stories in height, with garage parking and a few units on the ground floor. To accommodate the density bonus and achieve the 26.1 units per acre density, the analysis assumes that a fourth story would be added to the buildings. To achieve this density, not all units would have a garage parking space and the minimum parking allowed under the density bonus provisions would be used. It is not clear that there is yet market demand in Menifee for condos at the density and with the limited parking needed to accommodate the density bonus units.

Project Income

In a for-sale development, the project income is derived from the sale of housing units. Table 35 provides the unit types, sizes, and expected sales values for market-rate and below market-rate units.

Table 35: Scenario 4, Average Unit Sizes and Average Sales Values (in current dollars)

	Size (sq. ft.)	Market-Rate Price	Below Market-Rate Price	Difference	
2 Bedrooms	1,160	427,000	131,000	296,000	-30.7%
3 Bedrooms	1,270	455,000	156,000	299,000	-34.3%

Source: PlaceWorks, 2024.

Notes to Table 35:

- Unit types, sizes, and market-rate sales values are PlaceWorks assumptions based on our assessment of the current market, including an assessment of home sales values in 2022, adjusted for inflation into 2023 dollars.
- Below market-rate sales values are based on the data in Table 11 and Table 12.

Based on the number of units provided in Table 34 and the sales values provided in Table 35, the resulting gross sales value and the net sales value after sales commissions for the base development scenario and the inclusionary housing scenario are provided in Table 36. The average sales value across all units is 8.5 percent lower for the inclusionary housing scenario. Nevertheless, the gross and net sales values are 14.4 percent higher under the inclusionary housing scenario, reflecting added density bonus units.

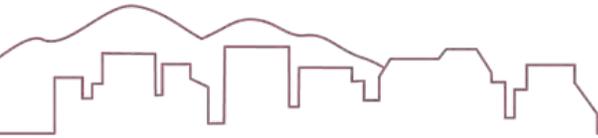


Table 36: Scenario 4: Project Income

	Base Development Scenario	Inclusionary Housing Scenario
Average unit sales value	438,000	401,000
Gross sales value	84,000,000	96,000,000
Less sales commission	-4,209,000	-4,814,000
Total Net Sales Value	80,000,000	91,000,000

Source: PlaceWorks, 2024.

Project Costs

Estimated project costs are provided in Table 37. The overall cost increases with additional units, from \$65.2 million for the base development scenario to \$78.8 million for the inclusionary housing scenario. However, the cost per unit decreases with fixed costs, such as land acquisition, spread across more units, and street frontage per unit, resulting in less roadway, water, and sewer per unit. The analysis estimates that the total development cost (before financing costs are added in) would increase by 21 percent with the inclusionary housing scenario, but the per unit cost would decrease by 3.3 percent.

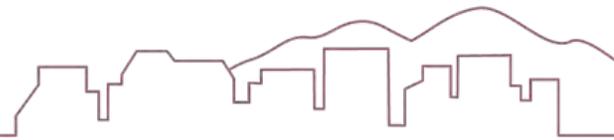
Table 37: Scenario 4: Project Costs

	Base Development Scenario	Inclusionary Housing Scenario
Estimated Land Cost	3,680,000	3,680,000
Hard Costs		
Site work (w/water & sewer)	2,230,000	2,750,000
Building construction	45,500,000	56,000,000
Circulation and parking	1,030,000	1,480,000
Landscaping	480,000	400,000
Hard cost subtotal	49,300,000	60,600,000
Soft Costs		
Design, entitlement, contingency, and other	7,390,000	9,090,000
Development Impact Fees	8,540,000	9,140,000
Soft costs subtotal	15,900,000	18,200,000
Total Development Cost		
Total cost (before financing)	65,200,000	78,800,000
- per unit	339,000	328,000

Source: PlaceWorks, 2024.

Notes to Table 37:

1. The estimated land cost is a PlaceWorks estimate based on our analysis of sales data, asking prices, and residual land values. There are few land sales, and reported prices vary, likely reflecting current zoning and existing entitlements, expectations for rezonings, topography, proximity to existing infrastructure and other factors. The analysis assumes a 5 percent of land cost allowance for due diligence activities related to land acquisition. The cash flow model



assumes monthly option payments of 1 percent of the estimated property value during the entitlement period, but the option payments are part of the overall payment for land acquisition rather than an additional cost.

2. Building construction costs are calculated on a per square foot basis for finished floor area and a separate square foot basis for garages. The per square foot costs are taken from Craftsman Book Company's 2023 National Building Cost Manual, with the source's recommended adjustments for local cost differential. As noted in the source, the per square foot cost estimates include all construction costs: labor, materials, equipment, plans, building permit, supervision, overhead, and profit.
3. Development impact fees are calculated at approximately \$55,000 per dwelling unit. The analysis assumes that development impact fees are charged to market-rate units but not below market-rate units.

Financial Feasibility

Table 38 summarizes the financial feasibility of Scenario 4. The analysis finds that the base development scenario is financially feasible, generating an IRR of 16.5 percent. However, the inclusionary housing scenario, with an IRR of 10.3 percent is not feasible. The analysis also indicates that the base development scenario would not be financially feasible when paying the in-lieu fee to comply with a 15 percent inclusionary housing requirement.

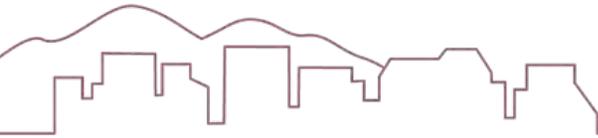
Table 38: Scenario 4: Financial Feasibility Summary

	Base Development Scenario	Inclusionary Housing Scenario
Development cost	65,200,000	78,800,000
Financing cost	5,880,000	6,520,000
Total project cost	71,000,000	85,000,000
Construction loan amount	56,800,000	68,400,000
Required equity	14,300,000	17,000,000
Net project income	3,410,000	2,420,000
Project IRR	16.5%	10.3%
Surplus/(Gap) w/15% IRR	250,000	-920,000
Residual land value w/15% IRR	3,930,000	2,760,000

Source: PlaceWorks, 2024.

Notes to Table 38:

1. Financing costs include construction loan fees of 2.5 percent and an interest rate of 8.6 percent. The current interest rate report by realtyrates.com for residential construction loans of 10.6 percent. The analysis assumes that interest rates will decline by two percentage points over the next two years. The total project costs are the development cost, from Table 37, plus the financing cost.
2. The construction loan amount is based on 50 percent of land acquisition and 84 percent of other construction costs, based on data from realtyrates.com.
3. The IRR is an annual rate of return based on monthly cash flow, assuming a 6-month entitlement period, 4 months of site work, 18 months of construction, and 3 months to complete sales. This is a somewhat simplified phasing schedule from what should be expected for actual development projects.



Sensitivity Analysis

The analysis considered other alternatives to achieve financial feasibility. First is the in-lieu fee. The base development scenario is estimated to generate a surplus residual land value of \$250,000. The in-lieu fee being evaluated in this report is \$154,372 per inclusionary unit. With a 15 percent inclusionary requirement, this project could comply with the inclusionary requirement with payment of a total in-lieu fee of \$4.6 million (154,372 \$/inclusionary unit X 30 required inclusionary units). This fee is more than the estimated surplus residual land value, indicating it would not be financially feasible to develop this project as a fully market-rate development and pay the in-lieu fee.

Reducing the inclusionary requirement to 10 percent, with all moderate-income households, results in a lower IRR, 8.3 percent, than the 15 percent inclusionary requirement that was analyzed above. The five percent density bonus is not sufficient to offset the difference in sales values between the market-rate and the below market-rate units. In contrast, lowering the requirement to five percent, with all very-low-income households generates an IRR of 21.6 percent. This is more lucrative than the base development scenario even without paying an in-lieu fee.

Finally, the analysis assesses changes in market-rate sales value. The sale values would have to increase by 1.3 percent for the inclusionary housing scenario to be financially feasible. However, with this increase, the inclusionary housing project is not as lucrative as the base development scenario and paying the in-lieu fee.

SCENARIO 5: FOR-RENT MULTIFAMILY APARTMENTS

Scenario Description

This scenario is a conventional multifamily apartment development, with 14 individual three-story buildings. Each apartment is accessed through a doorway in an interior common hallway. A portion of the ground floor in each building is used for individual garages, without about 43 percent of the required residential parking spaces provided in these garages. The remaining spaces are provided in surface parking.

The analysis assumes that the base development scenario would provide 237 1-, 2-, and 3-bedroom units on an 8.8-acre site. This represents a gross density of just under 27 units per acre. For the inclusionary housing scenario, 10 percent of the 237 units (24 units) would be low-income units (moderate-income housing is not eligible for a density bonus when offered for rent, and 10 percent is the minimum percentage for low-income housing units to be eligible for a density bonus). Five percent of the total number of units (12 units) would be very-low-income units. The inclusionary housing scenario also receives a 40 percent density bonus, or an additional 95 market rate units, for a total of 332 units. Thus, from the base scenario of 237 units, the inclusionary scenario has 296 market rate units and 36 affordable units. With this number of housing units, the gross density increases to 33.7 units per acre. The analysis assumes that the additional units can be accommodated by increasing the height of the buildings from three stories to four stories. However, it is not clear without detailed site planning, that the inclusionary scenario could be developed without a substantial waiver to parking requirements, above and beyond the reduced parking to which the affordable units are entitled.

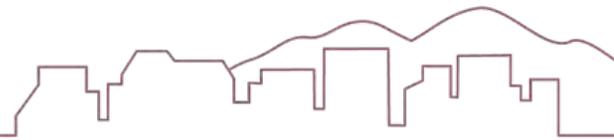


Table 39: Scenario 5, Development Description

Unit Type	Base Development Scenario	Inclusionary Housing Scenario		
	Total Number of Units	Below Market-Rate Units	Market-Rate Units	Total Number of Units
1-Bedroom A	54	8	68	76
1-Bedroom B	48	7	60	67
2-Bedroom A	50	8	62	70
2-Bedroom B	24	4	30	34
2-Bedroom C	43	6	54	60
3-Bedroom A	18	3	22	25
Total	237	36	296	332
Site Area (acres)	8.8			8.8
Gross Density (du/ac)	26.9			37.7

Source: PlaceWorks, 2024.

Project Income

In a for-rent development, the project income is derived from the monthly rent. In practice, multifamily developments may also generate ancillary income from laundry facilities and other fees. For simplicity, this analysis only considers income from monthly rent. Table 40 provides the unit types, sizes, and expected rents for market-rate and below market-rate units.

Table 40: Scenario 5, Average Unit Sizes and Average Monthly Rents (in current dollars)

	Size (sq. ft.)	Market-Rate Price	Below Market-Rate Price	Difference	
1-Bedroom A	760	1,470	950	520	-35.5%
1-Bedroom B	780	1,570	990	570	-36.6%
2-Bedroom A	1,040	2,780	1,130	1,650	-59.4%
2-Bedroom B	1,130	3,070	1,200	1,860	-60.7%
2-Bedroom C	1,220	3,350	1,150	2,200	-65.5%
3-Bedroom A	1,410	4,320	1,330	2,990	-69.3%

Source: PlaceWorks, 2024.

Notes to Table 40:

- Unit types, sizes, and market-rate rent values are PlaceWorks assumptions based on our assessment of the current market.
- Below market-rate rent values are based on the data in Table 11 and Table 12, assuming that 1-bedroom units are a mix of 1- and 2-person households, 2-bedroom units are 3-person households, and 3-bedroom units are a mix of 4- and 5-person households.

Based on the number of units provided in Table 39 and the rent values provided in Table 40, the resulting gross monthly rent and the annual net operating income for the base development scenario and the inclusionary housing scenario are provided in Table 41.

The average rent per unit is 6.2 percent lower for the inclusionary housing scenario. Nevertheless, the gross rent and net operating income are 31.3 percent higher under the inclusionary housing scenario.

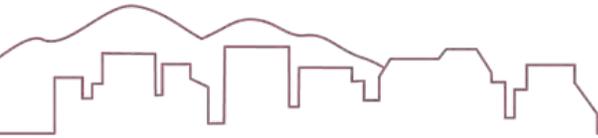


Table 41: Scenario 5: Project Income

	Base Development Scenario	Inclusionary Housing Scenario
Average monthly rent per unit	2,490	2,330
Gross monthly rent	589,000	774,000
Less vacancies and operations	-165,400	-217,200
Annual net operating income	5,080,000	6,680,000

Source: PlaceWorks, 2024.

Project Costs

Estimated project costs are provided in Table 42. The overall cost increases with additional units, from \$72 million for the base development scenario to \$95 million for the inclusionary housing scenario. However, the cost per unit decreases with fixed costs, such as land acquisition, spread across more units. The analysis estimates that the total development cost (before financing costs are added in) would increase by 32 percent with the inclusionary housing scenario, but the per unit cost would decrease by 5.8 percent.

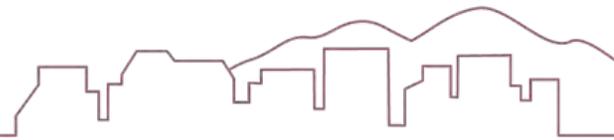
Table 42: Scenario 5: Project Costs

	Base Development Scenario	Inclusionary Housing Scenario
Estimated Land Cost	3,790,000	3,790,000
Hard Costs		
Site work	5,180,000	5,220,000
Building construction	45,400,000	63,700,000
Circulation and parking	1,380,000	2,090,000
Landscaping	1,500,000	420,000
Hard cost subtotal	53,500,000	71,400,000
Soft Costs		
Design, entitlement, contingency, and other	8,020,000	10,720,000
Development impact fees	10,310,000	12,600,000
Soft costs subtotal	18,300,000	23,300,000
Total Development Cost		
Total cost (before financing)	71,800,000	94,800,000
- per unit	303,000	285,000

Source: PlaceWorks, 2024.

Notes to Table 42:

1. The estimated land cost is a PlaceWorks estimate based on our analysis of sales data, asking prices, and residual land values. There are few land sales, and reported prices vary, likely reflecting current zoning and existing entitlements, expectations for rezonings, topography, proximity to existing infrastructure and other factors. The analysis assumes a 5 percent land cost allowance for due diligence activities related to land acquisition. The cash flow model



assumes monthly option payments of 1 percent of the estimated property value during the entitlement period, but the option payments are part of the overall payment for land acquisition rather than an additional cost.

2. Building construction costs are calculated on a per square foot basis for finished floor area and a separate square foot basis for garages. The per square foot costs are taken from Craftsman Book Company's 2023 National Building Cost Manual, with the source's recommended adjustments for local cost differential. As noted in the source, the per square foot cost estimates include all construction costs: labor, materials, equipment, plans, building permit, supervision, overhead, and profit.
3. Development impact fees are calculated at approximately \$55,000 per dwelling unit. The analysis assumes that development impact fees are charged to market-rate units but not below market-rate units.

Financial Feasibility

Table 43 summarizes the financial feasibility of Scenario 5. Because this development scenario is analyzed as a for-rent project, the analysis uses the unleveraged yield to measure financial feasibility. The analysis finds that the base development scenario should be financially feasible, generating a yield of 6.21 percent. This scenario would generate a surplus value of \$2.5 million, which, if used to pay an in-lieu fee, would support a fee of \$69,400 per inclusionary unit.

The inclusionary scenario is also financially feasible, with a yield of 6.27 percent. This suggests that a market rate developer would have an incentive to provide inclusionary housing units and capitalize on the density bonus if the in-lieu fee is set at an amount larger than \$69,400. The surplus value with the inclusionary housing scenario would allow the project to be built on a larger site if needed to accommodate additional parking.

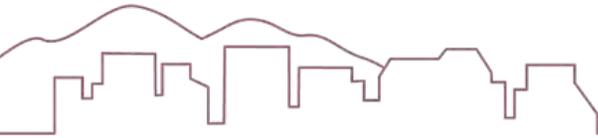
Table 43: Scenario 5: Financial Feasibility Summary

	Base Development Scenario	Inclusionary Housing Scenario
Development cost	71,800,000	94,800,000
Financing cost	6,360,000	8,050,000
Total project cost	78,000,000	103,000,000
Construction loan amount	62,700,000	82,900,000
Required equity	15,500,000	19,900,000
Unleveraged yield (6% target)	6.21%	6.27%
Surplus/(Gap) w/6% Yield	2,500,000	4,230,000
Residual land value w/6% Yield	6,020,000	7,750,000

Source: PlaceWorks, 2024.

Notes to Table 43:

1. Financing costs include construction loan fees of 2.5 percent and an interest rate of 8.6 percent. The current interest rate report by realtyrates.com for residential construction loans of 10.6 percent. The analysis assumes that interest rates will decline by two percentage points over the next two years. The total project costs are the development cost, from Table 42, plus the financing cost.
2. The construction loan amount is based on 50 percent of land acquisition and 84 percent of other construction costs, based on data from realtyrates.com.
3. The IRR is an annual rate of return based on monthly cash flow, assuming a 6-month entitlement period, 4 months of site work, 18 months of construction, and 3 months to complete sales. This is a somewhat simplified phasing schedule from what should be expected for actual development projects.



Sensitivity Analysis

Because both scenarios are estimated to be financially feasible, additional sensitivity analysis is not warranted. However, it is worth noting that the analysis estimates that the base scenario could afford to pay an in-lieu fee of up to \$69,400, which is substantially less than the fee being evaluated in this report is \$154,372 per inclusionary unit. This suggests that the density bonus provides an incentive for the developer to construct the inclusionary units rather than pay a fee for multifamily rental housing, provided that the developer can accommodate the increased density on the site.

SCENARIO 6: FOR-RENT MIXED-USE MULTIFAMILY APARTMENTS AND STAND-ALONE COMMERCIAL

Scenario Description

This scenario is a conventional multifamily apartment development, with two stand-alone commercial buildings. The apartments are provided in eight three-story buildings. Each building has two ground-floor apartments at each end, with the remainder of the ground floor being used for parking. The two commercial buildings would be served entirely by surface parking spaces.

The analysis assumes that the base development scenario would provide 200 1-, 2-, and 3-bedroom units on about 8.1 acres of the 8.8-acre site. This represents a gross density of 24.6 units per acre. For the inclusionary housing scenario, 10 percent of the 200 units (20 units) would be low-income units (moderate-income housing is not eligible for a density bonus when offered for rent, and 10 percent is the minimum percentage for low-income housing units to be eligible for a density bonus). Five percent of the total number of units (10 units) would be very-low-income units. The inclusionary housing scenario also

receives a 40 percent density bonus, or an additional 80 market rate units, for a total of 280 units. Thus, from the base scenario of 200 units, the inclusionary scenario has 250 market rate units and 30 affordable units. With this number of housing units, the gross density increases to 34.4 units per acre. The analysis assumes that the additional units can be accommodated by increasing the height of the buildings from three stories to four stories. However, it is not clear without detailed site planning, that the inclusionary scenario could be developed without some provisions for shared parking and/or a substantial waiver to parking requirements, above and beyond the reduced parking to which the affordable units are entitled.

Table 44: Scenario 6, Development Description

Unit Type	Base Development Scenario	Inclusionary Housing Scenario		
	Total Number of Units	Below Market-Rate Units	Market-Rate Units	Total Number of Units
1-Bedroom	96	14	120	134
2-Bedroom A	40	6	50	56
2-Bedroom B	48	8	60	68
3-Bedroom	16	2	20	22
Total	200	30	250	280
Est. Residential Area	8.1			8.1
Gross Density (du/ac)	24.6			34.4

Source: PlaceWorks, 2024.

Project Income

In a for-rent development, the project income is derived from the monthly rent. In practice, multifamily developments may also generate ancillary income from laundry facilities and other fees. For simplicity, this analysis only considers income from monthly rent. Table 45 provides the unit types, sizes, and expected rents for market-rate and below market-rate units.

Table 45: Scenario 6, Average Unit Sizes and Average Monthly Rents (in current dollars)

	Size (sq. ft.)	Market-Rate Price	Below Market-Rate Price	Difference	
1-Bedroom	680	1,170	1,040	130	-11.0%
2-Bedroom A	1,010	2,670	1,270	1,400	-52.3%
2-Bedroom B	1,175	3,220	1,250	1,970	-61.3%
3-Bedroom	1,190	3,620	1,350	2,270	-62.7%

Source: PlaceWorks, 2024.

Notes to Table 45:

- Unit types, sizes, and market-rate rent values are PlaceWorks assumptions based on our assessment of the current market.
- Below market-rate rent values are based on the data in Table 11 and Table 12, assuming that 1-bedroom units are a mix of 1- and 2-person households, 2-bedroom units are 3-person households, and 3-bedroom units are a mix of 4- and 5-person households.

Based on the number of units provided in Table 44 and the rent values provided in Table 45, the resulting gross monthly rent and the annual net operating income for the base development scenario and the inclusionary housing scenario are provided in Table 46.

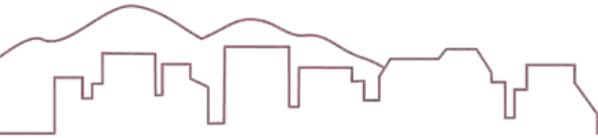
The average rent per unit is 4.9 percent lower for the inclusionary housing scenario. Nevertheless, the gross rent and net operating income are 33.1 percent higher under the inclusionary housing scenario.

Table 46: Scenario 6: Project Income

	Base Development Scenario	Inclusionary Housing Scenario
<i>Residential</i>		
Average monthly rent per unit	2,160	2,050
Gross monthly rent	432,000	575,000
Less vacancies and operations	-121,200	-161,300
Annual net operating income	3,730,000	4,960,000
<i>Nonresidential</i>		
Gross leasable floor area (sq. ft.)	27,174	27,174
Gross monthly rent	67,900	67,900
Less vacancies and operations	-31,600	-31,600
Annual net operating income	436,000	436,000
<i>Total Project Income</i>		
Annual net operating income	4,162,424	5,395,475

Source: PlaceWorks, 2024.

Table 46 also provides the estimated income from the non-residential development. This portion of the development does not change with the addition of inclusionary housing. The analysis estimates that the total project would generate



a net annual operating income of \$4.16 million for the base scenario and \$5.4 million for the inclusionary housing scenario, for the first year of full occupancy.

Project Costs

Estimated project costs are provided in Table 47. The overall cost increases with additional units, from \$76 million for the base development scenario to \$100 million for the inclusionary housing scenario. However, the cost per unit decreases with fixed costs, such as land acquisition, spread across more units. The analysis estimates that the total development cost (before financing costs are added in) would increase by 31 percent with the inclusionary housing scenario, but the per unit cost would decrease by 6.4 percent.

Table 47: Scenario 6: Project Costs

	Base Development Scenario	Inclusionary Housing Scenario
Estimated Land Cost	4,180,000	4,180,000
Hard Costs		
Site work	5,910,000	5,950,000
Building construction	51,100,000	67,900,000
Circulation and parking	1,480,000	1,860,000
Landscaping	910,000	1,500,000
Hard cost subtotal	59,400,000	77,200,000

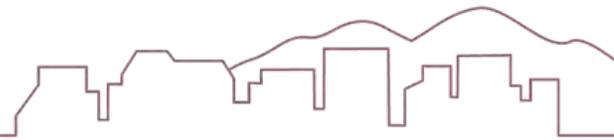
Table 47 continued

	Base Development Scenario	Inclusionary Housing Scenario
Soft Costs		
Design, entitlement, contingency, and other	8,900,000	11,590,000
Development impact fees	7,870,000	10,910,000
Soft costs subtotal	16,800,000	22,500,000
Total Development Cost		
Total cost (before financing)	76,100,000	99,700,000
- per unit	381,000	356,000

Source: PlaceWorks, 2024.

Notes to Table 47:

1. The estimated land cost is a PlaceWorks estimate based on our analysis of sales data, asking prices, and residual land values. There are few land sales, and reported prices vary, likely reflecting current zoning and existing entitlements, expectations for rezonings, topography, proximity to existing infrastructure and other factors. The analysis assumes a 5 percent land cost allowance for due diligence activities related to land acquisition. The cash flow model assumes monthly option payments of 1 percent of the estimated property value during the entitlement period, but the option payments are part of the overall payment for land acquisition rather than an additional cost.
2. Building construction costs are calculated on a per square foot basis for finished floor area and a separate square foot basis for garages. The per square foot costs are taken from Craftsman Book Company's 2023 National Building Cost Manual, with the source's recommended adjustments for local cost differential. As noted in the source, the per square foot cost estimates include all construction costs: labor, materials, equipment, plans, building permit, supervision, overhead, and profit.



- Development impact fees are calculated at approximately \$55,000 per dwelling unit. The analysis assumes that development impact fees are charged to market-rate units but not below market-rate units.

Financial Feasibility

Table 48 summarizes the financial feasibility of Scenario 6. Because this development scenario is analyzed as a for-rent project, the analysis uses the unleveraged yield to measure financial feasibility. The analysis finds that neither the base development scenario nor the inclusionary housing scenario would be financially feasible. Even if the land were provided free, this mixed-use development would not be feasible.

Table 48: Scenario 6: Financial Feasibility Summary

	Base Development Scenario	Inclusionary Housing Scenario
Development cost	76,100,000	99,700,000
Financing cost	6,370,000	7,660,000
Total project cost	83,000,000	107,000,000
Construction loan amount	66,100,000	86,600,000
Required equity	16,400,000	20,800,000
Unleveraged yield (6% target)	4.8%	4.84%
Surplus/(Gap) w/6% Yield	n/a	n/a
Residual land value w/6% Yield	n/a	n/a

Source: PlaceWorks, 2024.

Notes to Table 48:

- Financing costs include construction loan fees of 2.5 percent and an interest rate of 8.6 percent. The current interest rate report by realtyrates.com for residential construction loans of

10.6 percent. The analysis assumes that interest rates will decline by two percentage points over the next two years. The total project costs are the development cost, from Table 47, plus the financing cost.

- The construction loan amount is based on 50 percent of land acquisition and 84 percent of other construction costs, based on data from realtyrates.com.
- The IRR is an annual rate of return based on monthly cash flow, assuming a 6-month entitlement period, 4 months of site work, 18 months of construction, and 3 months to complete sales. This is a somewhat simplified phasing schedule from what should be expected for actual development projects.

Scenario 6 is similar to Scenario 5: they have a similar residential density, and they have similar unit sizes. The substantial difference in the estimated return on investment suggests that the commercial development portion included in Scenario 6 is the primary challenge to the feasibility.

Sensitivity Analysis

Because neither scenario is financially feasible, even with the land cost reduced to zero, no additional sensitivity analysis is warranted.

FINANCIAL FEASIBILITY SUMMARY

The financial feasibility analyses are summarized in Table 49. Only two of the scenarios are financially feasible to develop with a 15 percent inclusionary requirement: Scenario 3, townhouses, and Scenario 5, for-rent multifamily apartments. If the inclusionary requirement were reduced to 10 percent, then Scenario 2, small lot single-family housing would become financially feasible. Finally, if the inclusionary requirement were reduced to 5 percent, then all the scenarios would be financially feasible, with the exception of Scenario 6, mixed use.

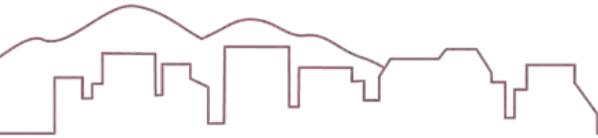
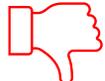
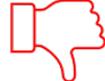
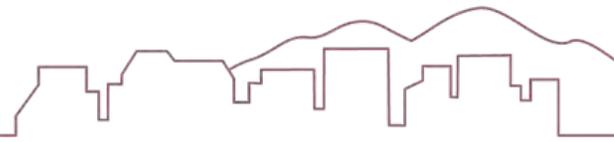


Table 49: Financial Feasibility Summary

	With No Inclusionary	15% Affordable		5% Affordable	
		On-site Inclusionary Housing	In-Lieu Fee	On-site Inclusionary Housing	In-Lieu Fee
Scenario 1: Larger Lot Single-Family Detached Housing					
Scenario 2: Small Lot Single-Family Housing					
Scenario 3: Townhouses					
Scenario 4: Condos					
Scenario 5: For-Rent Multifamily Apartments					
Scenario 6: For-Rent Mixed-Use MF Apartments and Commercial		N/A	N/A	N/A	N/A



Previously this report indicated that the city would need to collect \$154,372 per inclusionary unit that does not get built in order to be able to incentivize affordable housing developers to build that unit. The analysis finds that only one scenario, Scenario 3, townhouses, could afford to pay the full fee. If the inclusionary requirement were reduced to 10 percent, then Scenario 2, small lot single-family housing would be able to pay the fee. Finally, if the inclusionary requirement were reduced to 5 percent, then Scenario 5, for-rent multifamily apartments would be able to pay the in-lieu fee.

If the City adopts a 15 percent inclusionary requirement, developers would need to raise the price of new market rate housing from 1.3 percent, for condos, to 3.1 percent, for larger lot single-family housing. However, there is no guarantee that the market would simply absorb the price increase. Similarly, developers could reduce the price they pay for land to offset the feasibility gap, but there is no guarantee that property owners would be willing to sell their property at a reduced price.

With an estimated 22,800 housing units yet to be entitled and built, a 15 percent inclusionary requirement could generate 3,420 affordable housing units. A 10 percent requirement would generate 2,280 units, and a 5 percent requirement would generate 1,140 units.

Because there are already 8,000 entitled but not yet constructed housing units, a new inclusionary housing requirement would be unlikely to generate a substantial portion of the RHNA-allocated 2,800 lower-income housing units or the 1,100 moderate-income housing units, during the time horizon of the City's current Housing Element. Indeed, a 15 percent inclusionary housing requirement could, by 2050, generate 3,420 affordable housing units, which is less

than the 3,900 affordable housing units that the City's has had to plan for by 2029 (the horizon year for the current Housing Element). Thus, an inclusionary housing requirement, if adopted, would need to be augmented with other tools and strategies, such as the City's current funding for down payment assistance.

NEXT STEPS

Should the City decide to explore an inclusionary housing requirement, there will be several key decisions to make in order to prepare a draft ordinance.

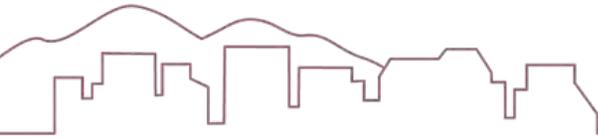
Key Decisions for an Inclusionary Housing Ordinance

Inclusionary Percentage

The City would be free to establish any percentage of units that must be affordable for any of the income groupings, although HCD may review any requirement that is over 15 percent.

Based on the financial feasibility analysis, we would suggest consideration of a 5 percent inclusionary requirement. The analysis suggests that this would be financially feasible for the residential prototypes described above once lending rates return to normal, or at least to a new normal.

We would also suggest that the 5 percent requirement apply to any combination of low-income and very low-income households. There is no density bonus for providing less than 10 percent affordable units with low-income housing, but there is no reason to preclude a developer from satisfying the inclusionary requirement with housing affordable to low-income households. In addition, the City may consider providing a local density bonus for 5 percent low-income housing to maintain an incentive for this level of affordability.



Once the City has some experience implementing the inclusionary housing ordinance, the specific requirements can be revisited and adjusted to ensure that the inclusionary housing program results in affordable housing being built.

As discussed previously, the market is not directing much investment into multifamily housing development in Menifee. As part of an inclusionary housing ordinance, the City could exempt new housing that will be rented rather than sold. This would create an incentive for multifamily housing development.

Threshold Project Size

Most ordinances establish a threshold project size and exempt projects smaller than the threshold size from the inclusionary requirement. With a 5 percent inclusionary requirement, any project with less than 20 units would be required to provide a fraction of an affordable unit (most ordinances require all fractional units to be rounded up, or fractions of 0.5 or higher to be rounded up, or something similar). Nevertheless, for a project with less than 20 units, there are fewer and fewer market rate units to spread the cost of the affordable unit across; the smaller the less-than-20-unit project is, the less financially feasible the inclusionary requirement becomes.

The City may make the inclusionary requirement applicable to all new residential development regardless of size. If the ordinance will provide for an in-lieu fee as an alternative means of compliance, it could allow the in-lieu fee on a proportionate basis for projects with less than 20 units.

With the 5 percent inclusionary requirement, we would suggest a threshold project size of 10 or more dwelling units.

Alternative Means of Compliance

An inclusionary housing ordinance is required to provide for at least one alternative means of compliance. Examples were provided in Section 7, the Introduction to the Inclusionary Housing Feasibility Study.

An in-lieu fee is the most common alternative means of compliance. We would suggest that the City provide for an in-lieu fee of \$154,372 per required inclusionary housing unit. We would also suggest that an inclusionary housing ordinance allow a developer to satisfy part of the inclusionary requirement with on-site units and the remainder with an in-lieu fee.

An alternative allowing the developer to construct the affordable units offsite is also worthy of consideration. However, this alternative has the potential to inhibit mixed-income neighborhoods and to concentrate affordable units. The dedication of land alternative can be used, but we would suggest that the value of the land be at least the same, or more, than the in-lieu fee would generate. Otherwise, the City may not be able to leverage the dedicated land to have the same number of affordable housing units built. Finally, the alternative for acquisition and rehabilitation of existing affordable units is probably of limited utility in Menifee.

Inclusionary Housing Ordinance

An inclusionary housing ordinance can be drafted once the key decisions have been settled. The ordinance would represent an amendment to the City's development code. Typically, when an in-lieu fee is included, the ordinance identifies the fee as an alternative means of compliance, but the fee is set by a separate resolution. This allows the City to update the fee each year without going through an amendment to the development code.