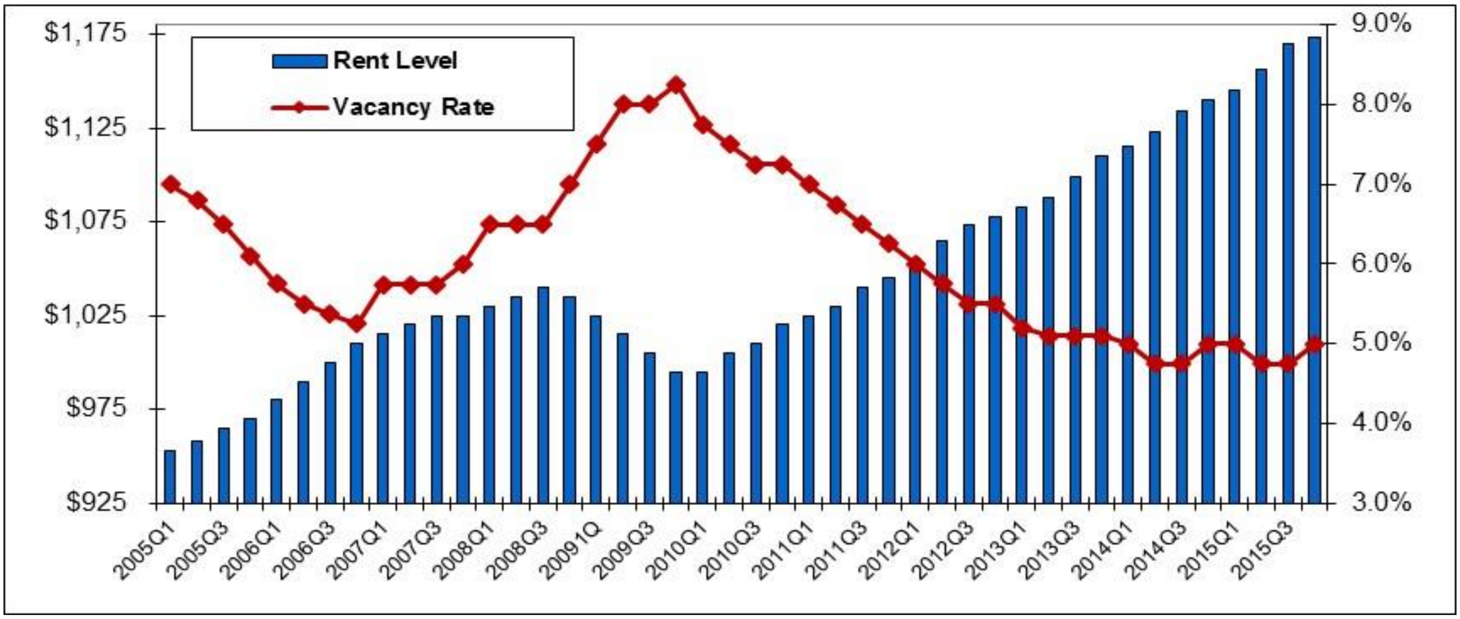
Multifamily Market Commentary – February 2016

Trends Show Some Seasonal Softening at End of 2015

National multifamily fundamentals reflected ongoing healthy demand during the fourth quarter of 2015. While there definitely were signs of softening late in the year, this can be attributed to typical year-end seasonality. The preliminary estimated national vacancy level inched up to 5.0 percent from 4.75 percent in the third quarter of 2015. As shown in the chart below, preliminary estimated effective rents continued to climb in the final quarter, although at a much slower pace than in the previous quarter. This was the 23rd consecutive quarter of rising rents. Despite an increase in new apartment construction starting to come online in a number of submarkets across the country, underlying fundamentals have remained steady, supporting demand.

Estimated National Multifamily Rent and Vacancy Levels



Source: Fannie Mae Multifamily Economics and Market Research

Demand Positive but Slowing Down

Preliminary third-party data for the fourth quarter of 2015 suggest that the vacancy rate for institutional investment-type apartment properties rose to an estimated 5.0 percent, up from an estimated 4.75 percent during the third and second quarters and returning to the estimated 5.0 percent in the year's first quarter.

Estimated rents continued to rise in the fourth quarter, but only by 0.25 percent, the slowest growth of the year compared to 1.25 percent in the third quarter, 1.0 percent in the second quarter, and 0.5 percent in the first. Rents grew at an estimated 3.0 percent in 2015, in line with the Multifamily Economic and Market Research team's multifamily rent growth forecast of between 3.0 and 3.5 percent.

Vendor Estimates in Vacancy Reflect the Same Trend – Finally

For the fourth quarter, all of our data vendors' estimated vacancy directional trends were in agreement – the first time in a while – although there were variations in estimates of how much vacancies rose. One vendor estimates an increase of only 10 basis points, one an increase of about 30 basis points, and two a 40-basis-point increase.

Axiometrics estimates the fourth-quarter vacancy rate rose 40 basis points, to 5.1 percent, compared to 4.70 percent in the third quarter and 5.22 percent in the first. Among our vendors, this was the largest estimated increase for the fourth quarter.

CBRE Econometric Advisors estimates that vacancy levels rose about 30 basis points in the fourth quarter to 4.7 percent, up from a revised 4.3 percent in the third quarter and the same as its revised estimate of 4.7 percent for the first quarter.

Reis, Inc. estimates a 10-basis-point increase to 4.4 percent in the fourth quarter, higher than its 4.2 percent estimates for the first and second quarters. Among our vendors, this was the smallest increase in fourth-quarter vacancies.

Lastly, CoStar estimates a vacancy level of 3.9 percent, up 30 basis points from its revised estimates of 3.6 percent for the third and second quarters of 2015 and very close to its revised first-quarter estimate of 4.0 percent. This was the lowest estimated vacancy level for the final quarter of 2015.

Positive Net Absorption

Reis is reporting that net absorption – the net change in occupied rental units – remained positive, if a bit slower, in fourth quarter 2015 at about 34,000 units, compared to 37,000 units in the third quarter. Net absorption rose by a revised 49,810 units in the second quarter and 33,309 units in the first. Despite an increase in new construction and supply coming online, the pace of net absorption has held firm, reflecting ongoing demand for multifamily housing nationwide. While the number of completions have slowed over the past few months, there were still an estimated 276,000 new units completed last year, according to Dodge Data & Analytics construction pipeline data. This is well above Reis' estimated absorption rate of 165,000 units for 2015 but in balance when factoring in typical annual obsolescence of about 120,000 units.

Rent Growth Slips in 4Q2015

Multifamily rent growth tends to slow, or even turn negative, during the last quarter of the year due to seasonal factors. Indeed, two of the data vendors estimate that rent growth turned negative during the fourth quarter of 2015. Axiometrics estimates that effective rent growth declined by 0.46 percent in the fourth quarter from the third quarter, although the year-over-year effective rent growth rate was a very solid 4.59 percent. CBRE Econometric Advisors, while estimating an even larger quarter-over-quarter decline, estimates year-over-year growth of 4.6 percent, almost the same as Axiometrics' estimate. CoStar estimates essentially no change (-0.1 percent) during fourth quarter 2015, but estimates robust year-over-year rent growth of 6.0 percent. Reis is the contrarian, estimating an increase of just 0.80 percent for the fourth quarter of 2015, but it estimates a 4.5 percent rent increase for all of 2015, in line with some of the other vendors. The Multifamily Economics and Market Research team estimates only 3.0 percent rent growth for 2015, but it tries to include all classes of multifamily properties, including class B and C. The team's estimate of 0.25 percent growth for the fourth quarter of 2015 falls between the estimates of Reis and CoStar, both of which have data on a larger number of rental units than the other vendors.

Vacancy Rates Still Declining in Some Metros but Rising in Others

Clearly, demand for rental housing of all types remained healthy in the fourth quarter 2015, but there was an increase in the number of metros with rising vacancy rates, according to preliminary data from CBRE Econometric Advisors. The firm estimates that the vacancy rate fell in just 36 out of 62 metros in the fourth quarter, compared to 39 metros in the third quarter, 43 in the second, and 51 (out of 61 metros) in the first. Vacancy rates rose in 24 metros in the fourth quarter, compared to 18 in the third quarter, 15 in the second, and only seven in the first. By CBRE Econometric Advisors' estimates, some of the metros with the biggest declines in the year-over-year vacancy rate include Detroit; Cincinnati; Providence, RI; Jacksonville, FL; Kansas City, MO; Richmond, VA; and Tampa, FL. Metros with vacancy rates below 4.0 percent include Detroit; New York City; Newark, NJ; Los Angeles; Miami; and Long Island, NY. The metros with the most significant increases included Hartford, CT; San Jose, CA; and Oklahoma City. These metros saw year-over-year increases of 100 basis points or more in the fourth quarter.

Expect Multifamily Demand to Remain Positive but Vacancy Will Likely Rise

We expect to see solid fundamentals for the multifamily sector continuing in the year ahead, while rent increases slow and softening net absorption leads to slightly higher vacancy levels. On a national level, we expect employment growth, solid demographic trends, and low homeownership rates to keep rent growth between 2.5 percent and 3.0 percent this year, with the vacancy rate expected to climb to just 5.5 percent by the end of 2016.

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