Multifamily Market Commentary – February 2015
Demand for Multifamily Expected to Stabilize in 2015

The multifamily sector continued to experience solid demand in 2014, and based on current data, the forecast for 2015 is not significantly different despite the big increase in new construction supply underway. Although there is an expectation of slowing rent growth and an uptick in vacancy levels, we expect there will be continued demand for multifamily housing in 2015 based on positive job growth, solid demographic trends, an increasing number of renter household formations, and rising for-sale home prices.

The ongoing demand for multifamily rental units remained healthy throughout all of 2014, despite the estimated national vacancy rate ticking up to 5.0 percent at the end of the fourth quarter of 2014. More importantly, rent growth appears to have been positive despite new additions to existing supply coming online throughout the year. We expect net absorption in 2015 to remain positive, although at a lower level than last year.

Vacancy Levels Expected to Rise Modestly

The national multifamily vacancy trend is expected to remain fairly stable over the forecast despite the influx of new completions likely outpacing demand, especially over the next few years. It is expected that the estimated national vacancy rate will actually increase to 5.25 percent sometime early in the year, perhaps by the end of the first half, and then climb to 5.5 percent by year-end 2015.

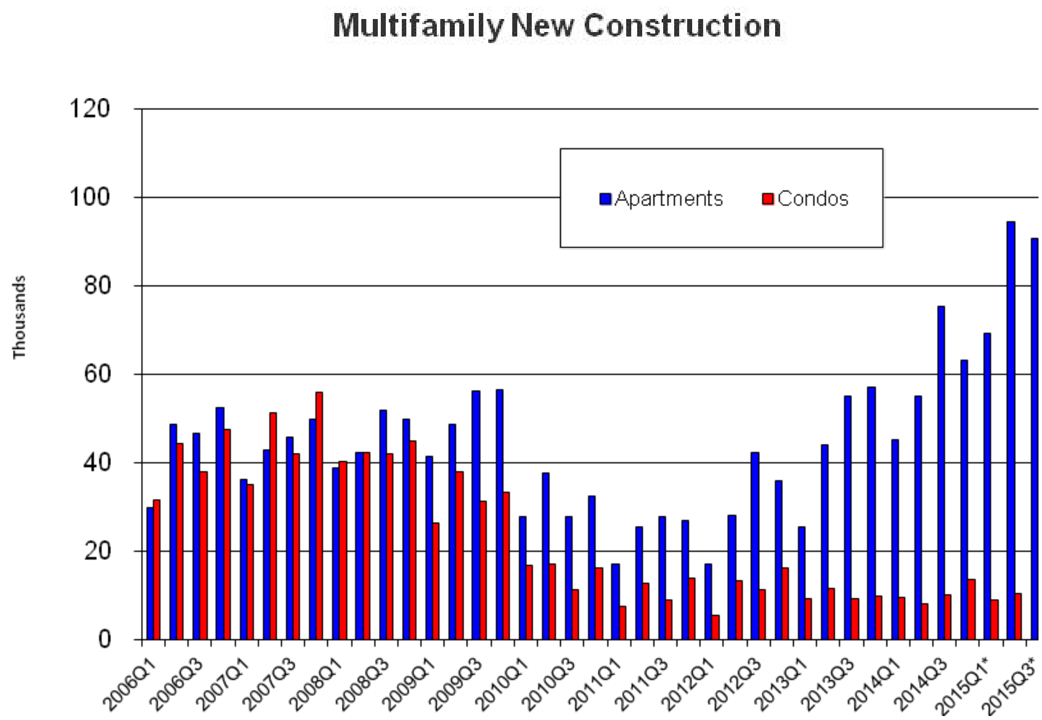
Multifamily Construction Surging – All in the Same Places

As seen in the chart on the following page, the amount of multifamily new construction has been increasing rapidly, especially over the past few years. According to the Dodge Data & Analytics Construction Pipeline, which distinguishes between apartment and condo multifamily units, approximately 239,000 apartment units were completed in 2014, with another 441,000 underway – 340,000 of which are expected to come online in 2015.

At a national level, that amount of new multifamily units added to the existing stock is not unreasonable. That is because 2015 is expected to see job growth of approximately 2.5 percent, according to Moody's Analytics, which would be an addition of more than 3 million new jobs.

Based on expected job growth, multifamily rental demand is estimated at 530,000 units, however this level of absorption is unlikely given that a significant portion of the new supply is located in roughly 12 metro areas, and most of that is further concentrated in certain submarkets. National estimated job growth and accompanying demand is not expected to be concentrated in just 12 metros, which is why we anticipate that supply will outpace demand over the next few years.

Fortunately, because the U.S. population includes approximately 45 million people between the ages of 20 and 29 – which is the cohort most likely to rent an apartment – overall demand is expected to remain in place, and as a result, the estimated national vacancy rate is not expected to increase significantly.

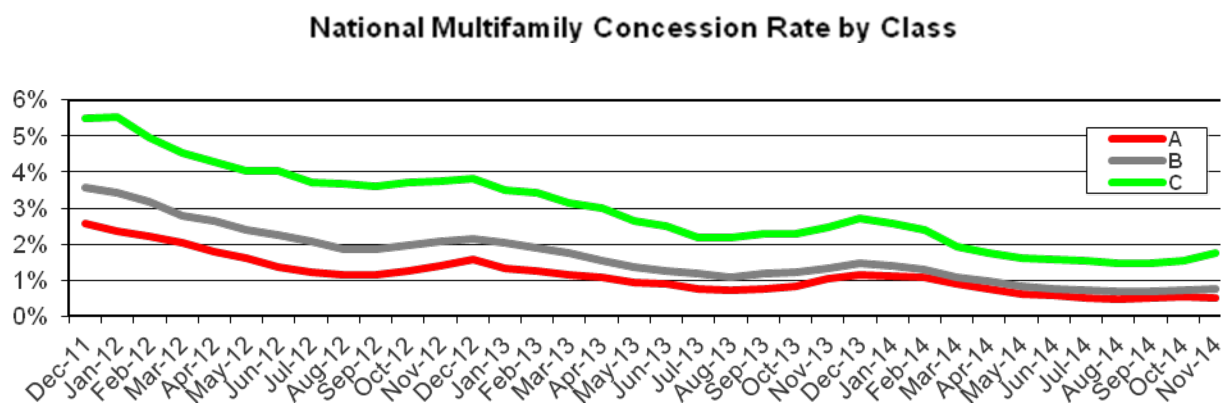


Source: Dodge Data & Analytics Construction Pipeline, January 2015 ** Anticipated completion date*

Rent Growth Will Likely Taper Off but Remain Positive

We expect the same to be true for rent growth, as well. Rent growth has been exceptionally strong over the past few years and only started slowing down slightly in 2014. The expectation for 2015 is that rent growth will be positive, but will likely slow to a range of about 2.0 percent to 2.5 percent, compared to 3.0 percent in 2014.

As seen in the chart below, multifamily concessions for all property types are at historic lows, which suggests that supply and demand have been out of balance for some time. With the advent of new supply, it is expected that concession rates should return to more normalized levels and likely to above average levels in those metros with concentrated supply. Indeed, there are already anecdotal reports that concessions in certain metros are already in use.



Source: Axiometrics

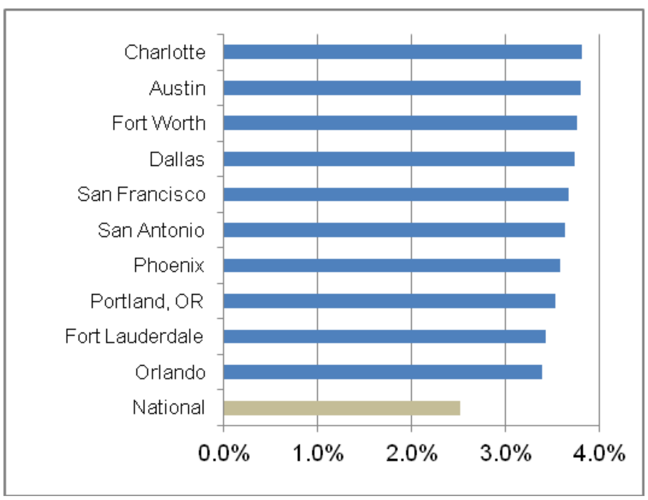
Job Growth Forecasts Mixed Depending Upon Metro

Although all of the nation's major metros are expected to see positive job growth this year, not all metros are expected to experience the same level of employment growth, as illustrated in the two charts below. While Moody's is forecasting national job growth of approximately 2.5 percent, they expect a number of metros to not come close to that amount, including **Washington, DC, Chicago, Philadelphia**, and **New York**.

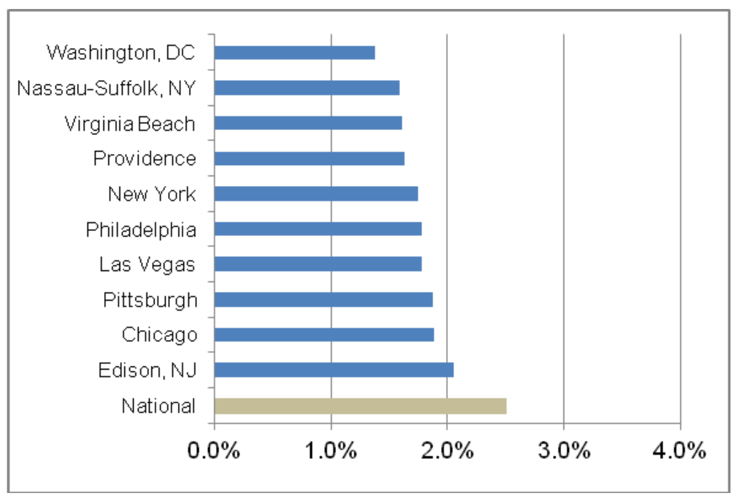
Fortunately for some of these metros, such as **Las Vegas, Providence,** and **Pittsburgh**, there isn't a large amount of new multifamily supply on the horizon. While this should not be a significant problem for the multifamily sector in some of these metros, others such as **Philadelphia** – with nearly 6,200 units underway – are likely to see diminished rent growth, particularly in certain submarkets, over the next 12 to 24 months.

Other metros will likely fare better. Some of the major Texas metros, such as **Dallas** and **Fort Worth**, are expected to continue seeing above-average job growth, albeit at a slower pace than over the past few years due to the continuing price declines occurring in the oil and gas sector. But other metros, such as **Charlotte**, **Phoenix**, and some of the Florida metros, including **Fort Lauderdale** and **Orlando**, also are expected to have above-average job growth this year, helping to keep their expected rent growth and vacancy levels healthy.

Markets with Highest Expected 2015 Employment Growth



Markets with Lowest Expected 2015 Employment Growth



Source: Moody's Analytics

2015 Outlook: Stabilizing Trends Despite New Supply

The outlook for the multifamily sector in 2015 is one of stabilization. Rent growth is expected to remain positive, albeit at a lower level than has been the case over the past few years. The concern lies with new supply and that most of it is concentrated in a number of submarkets in about 12 metros. While there should be healthy job growth spurring continued rental household formations, there is no denying that this concentrated amount of supply – consisting primarily of Class A luxury supply – will likely cause a disruption in the underlying fundamentals, producing an increase in vacancy levels and reduction in rent growth trajectories affecting the overall metro trend.

Nevertheless, the nation's multifamily sector should see another year of positive rent growth. Ongoing demand combined with the higher rent levels of these new Class A units coming online in 2015 is expected to push average asking rent up by 2.0 percent to 2.5 percent. The new supply also will push vacancy rates up modestly, rising to 5.25 percent in the first half of the year and perhaps as high as 5.5 percent by year-end.

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