

Multifamily Market Commentary – January 2016

2016 Multifamily Outlook – Expect Continued Demand for Multifamily

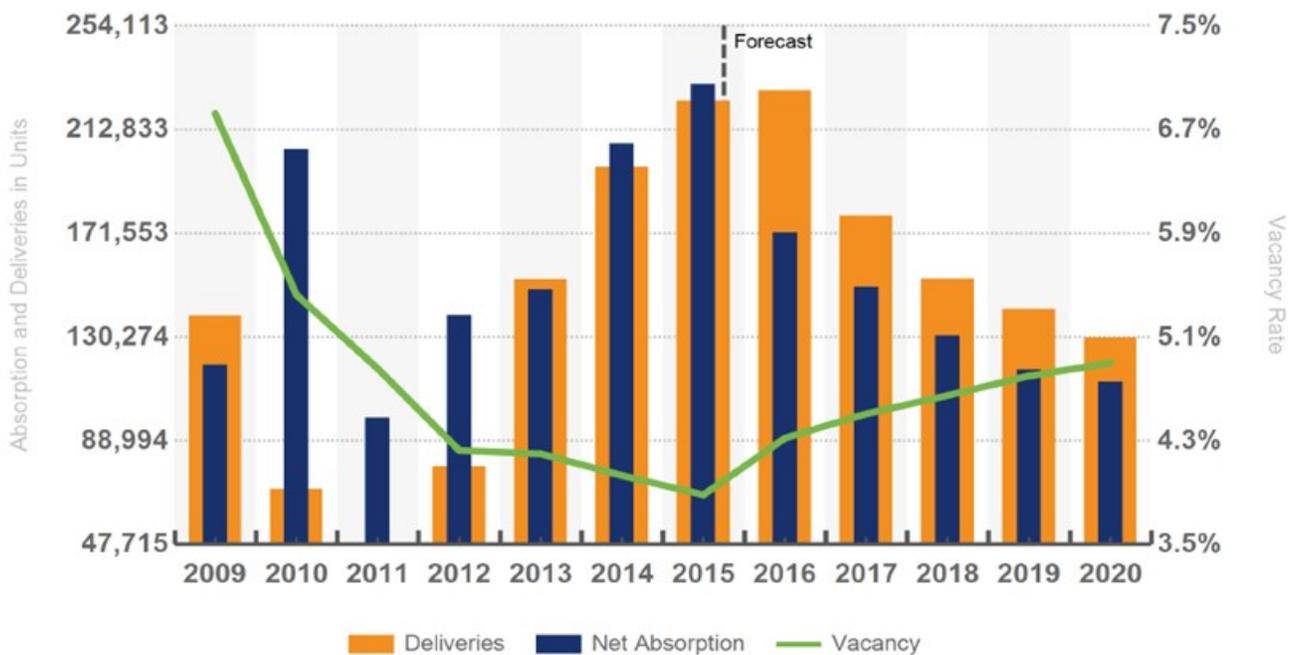
The multifamily sector continued to experience solid demand in 2015, and based on current data, 2016 is not expected to be significantly different despite the elevated amount of new construction underway. However, we do expect a slowdown in net absorption levels to lead to an uptick in vacancies, and rent growth could ease slightly.

We expect continued demand for multifamily rental units in 2016 based on a number of key fundamentals including positive job growth, solid demographic trends, and continued renter household formations.

The ongoing demand for multifamily rental units remained healthy throughout 2015, despite an estimated 276,000 new units coming online, according to Dodge Data & Analytics. Rent growth was not only positive but likely ended the year at about 3.0 percent, well above the pace of inflation, which was at just 0.5 percent at the end of November 2015.

Indeed, net absorption likely remained steady at an estimated 165,000 units, which is down from 2014’s estimated 169,000 units absorbed, according to Reis, Inc. We expect net absorption in 2016 to remain positive, although at a lower level than last year, possibly falling to fewer than 140,000 units absorbed based on 2015 trends.

Forecasted National Multifamily Trends



Source: CoStar

Vacancy Levels Expected to Rise

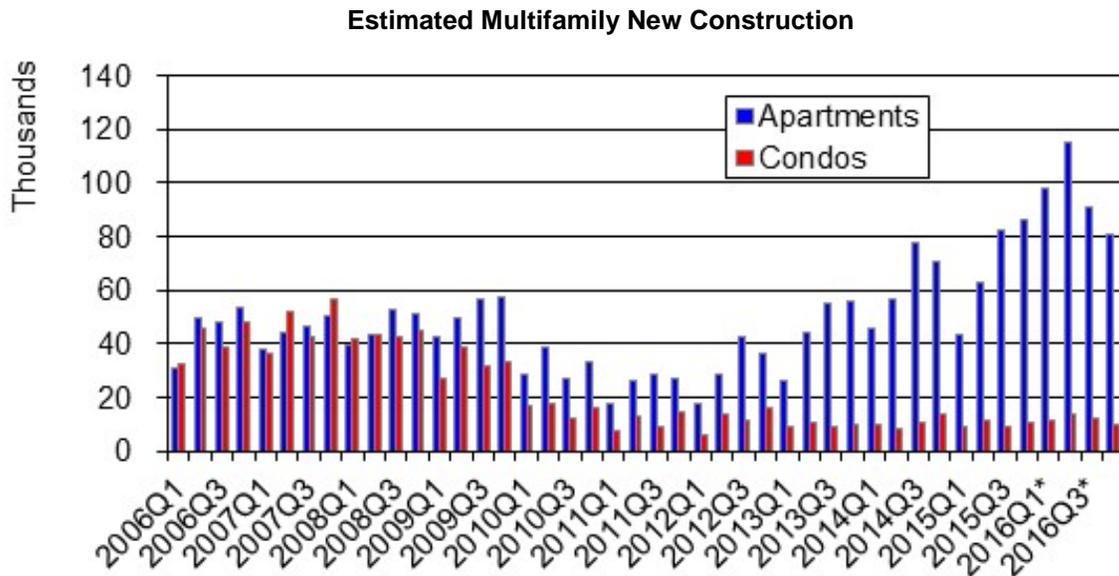
National multifamily vacancies should rise as the supply from an influx of new completions outpaces demand, especially over the next few years. For example, as illustrated in the above chart, real estate research firm CoStar shows the national vacancy rate beginning to increase this year and the upward trend continuing until 2020.

The Fannie Mae Multifamily Economic and Market Research team also believes that the national vacancy rate is likely to rise, but to 5.25 percent sometime during the first half of 2016 and climb further, perhaps to 5.5 percent, by the end of the year.

Multifamily Construction Surging – All in the Same Places

As seen in the chart below, the amount of new multifamily construction has been increasing rapidly, especially over the past few years.

According to the Dodge Data & Analytics Pipeline, which distinguishes between apartment and condo units, there were around 276,000 apartment unit completions in 2015, with another 500,000 units underway, of which about 384,000 are expected to come online in 2016.



Source: Dodge Data & Analytics/CBRE-EA
 Note: Pipeline data is not an actual forecast of activity, it is a monitor of activity reported on to-date. As more projects are planned and tracked, figures in future periods might go up.

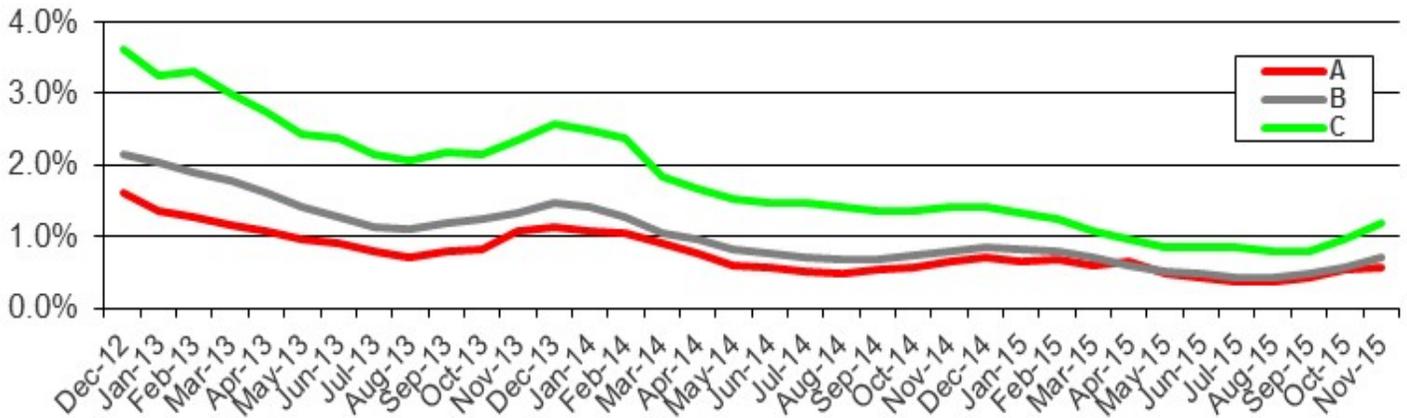
At a national level, the addition of that amount of new multifamily units to the existing stock is not unreasonable. Moody’s Analytics expects to see job growth of 1.9 percent in 2016, or the addition of 2.6 million new jobs. That amount of job growth could suggest multifamily rental demand closer to 520,000 units, but we believe that amount of absorption is not likely to happen because most of the new supply is located in only about 12 metros, and most of that is further concentrated in certain submarkets. This year’s job growth and accompanying demand is not expected to be concentrated in just those 12 metros, which is why we expect supply to outpace demand.

Rent Growth Expected to Ease Slightly

Rent growth has been exceptionally strong since 2011 and has remained in the 3.0 percent range over the past two years, only starting to slow down slightly in 2014. Rent growth is expected to be positive once again in 2016, but it is expected to ease slightly into the 2.5 to 3.0 percent range, down slightly from 2015.

As seen in the chart below, multifamily concessions for all property classes remain at very low levels, which suggests that supply and demand have been out of balance for a while now. With the advent of new supply, concession rates should return to more normalized levels and to even higher levels in those metros with concentrated supply.

National Multifamily Concession Rate by Class

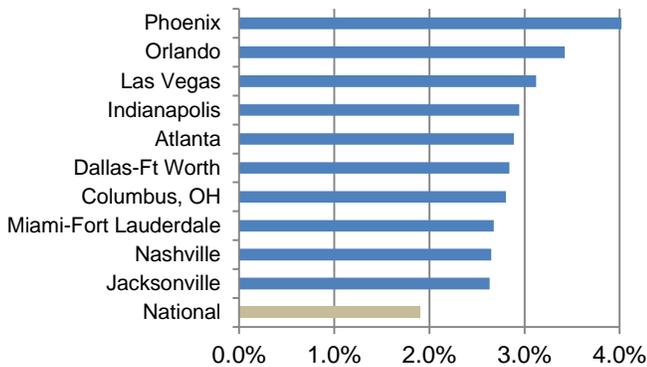


Source: Axiometrics

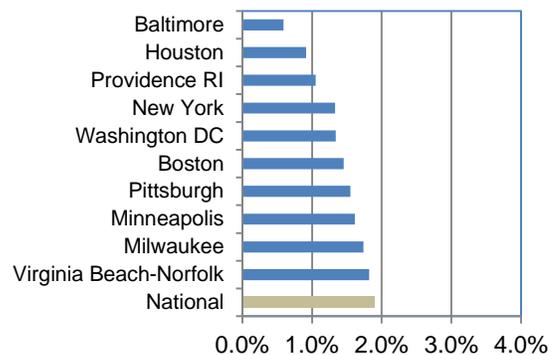
Job Growth Forecasts Mixed Depending Upon Metro

Although all of the nation’s major metros are expected to see positive job growth this year, not all of them are expected to experience the same level of employment growth, as illustrated in the two charts below. Although Moody’s Analytics’ baseline 2016 forecast is for a national employment growth rate of 1.9 percent, a number of metros are not expected to come close to the national estimate, including **Baltimore**, **Houston**, **Boston**, and even **New York** and **Washington, DC**.

Markets with Highest Expected 2016 Employment Growth



Markets with Lowest Expected 2016 Employment Growth



Source: Moody’s Analytics

Fortunately, for some of the metros with the lowest projected employment growth in 2016, such as **Providence**, **Milwaukee**, and even **Pittsburgh**, there isn’t a large amount of new multifamily supply on the horizon. Others, however, such as **Baltimore** with more than 6,300 units underway, or even more concerning, **Houston** with nearly 20,000 units underway, are likely to see diminished rent growth, particularly in certain submarkets, over the next 12 to 24 months.

Metros with high employment growth, as seen above, are poised to fare better. Some Florida metros, including **Orlando**, **Miami**, and **Jacksonville**, are expected to far surpass national average job growth. Dallas, one of the Texas metros not dependent upon the oil and gas sector, is expected to see about 3.0 percent job growth from expansion in its professional services, healthcare, and transportation sectors. **Phoenix** is poised to see the best job growth in the nation this year, at 4.2 percent, thanks to growth in its professional services, healthcare, and tourism sectors.



2016 Outlook: Continued Demand but Slower Absorption

The outlook for the multifamily sector in 2016 is one of slower absorption despite ongoing demand. The concern is not just over the amount of new supply coming online this year but, more importantly, that most of this supply will be concentrated in submarkets in about 12 metros. While healthy job growth should spur continued rental household formations, we believe this concentration of supply – consisting primarily of Class A luxury units – will disrupt underlying fundamentals, producing an increase in vacancy levels and reduction in rent growth trajectories in certain submarkets, thereby negatively 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 2016 should keep average asking rent growth in the 2.5 percent to 3.0 percent range. The new supply should also push vacancy rates up modestly, likely to 5.25 percent in the first half of 2016 and perhaps as high as 5.5 percent by the end of the year.

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