Fannie Mae

Multifamily Market Commentary – March 2018

Seniors Rental Housing: Fundamentals Eased Modestly in 2017

Seniors rental housing fundamentals eased modestly over the course of 2017, with occupancy levels declining slightly from the prior year's levels and rent growth rates slowing, based on data from the National Investment Center for Seniors Housing & Care (NIC), a leading industry provider of seniors housing data. These indicators softened in the first half of 2017 but were remarkably steady in the fourth quarter of 2017, with occupancy levels and rent growth rates virtually unchanged from the prior quarter. There is still ongoing demand for seniors housing, but the surge of new inventory appears to be preventing occupancy levels from rising. Rent growth rates remained positive in 2017 but were below the above-average levels achieved in 2016. Continued deliveries of new units is likely a long-term condition for seniors rental housing, and in late 2017 the number of new units under construction began to rise again, albeit just slightly.

Most Primary Markets Continued Steady Performance in 2017

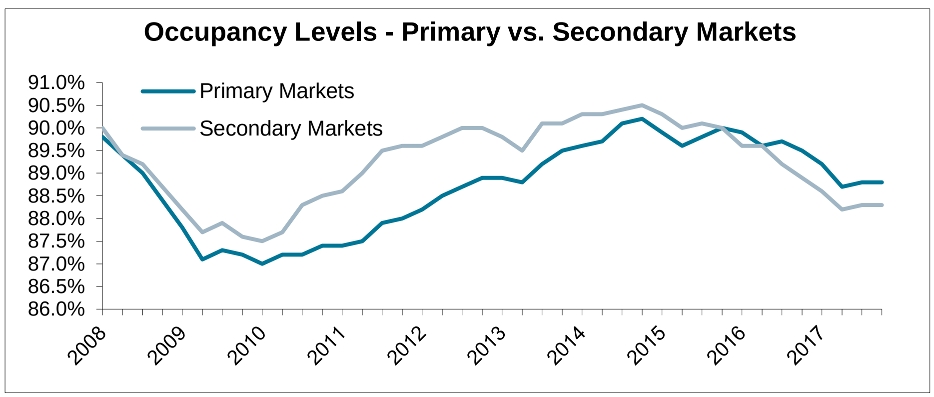
For the second consecutive quarter, year-over-year rent growth was positive in all but one of NIC's 31 primary markets in the fourth quarter of 2017. Overall, 17 of the 31 primary markets had lower rent growth in the fourth quarter than they did in the prior quarter, which was a slight improvement compared to the third quarter.

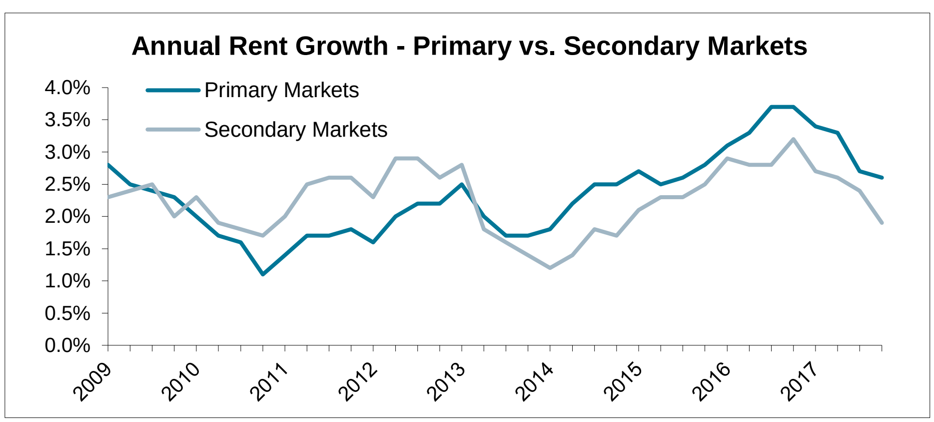
San Jose's reign as the strongest seniors housing market continued throughout 2017, after reporting the highest occupancy level and rent growth rate among the 31 primary markets at year end. In the fourth quarter, Seattle and Los Angeles also led the way in rent growth compared to a year ago, with Los Angeles reporting one of the stronger improvements compared to the prior year. Kansas City underperformed in the fourth quarter, as it experienced its second consecutive decline in rent growth, resulting in a minor contraction for the quarter. It continued to be among the five least-occupied primary markets. San Antonio had the weakest occupancy among the primary markets throughout 2017, likely resulting in the market's below average rent growth, which is likely attributable to the metro's ongoing supply surge.

Secondary Markets Eased More than Primary

Occupancy levels in secondary markets (32nd to 100th in size) were unchanged from the third quarter at 88.3 percent in the fourth quarter of 2017, after falling steadily in most quarters since 2014. Occupancy remained lower in secondary markets than in the primary markets, as seen in the chart to the right. Compared to a year ago, occupancy in the smaller markets was down 0.6 percent in the fourth quarter.

Rent growth in the secondary markets in fourth quarter fell more than in the primary markets, with the secondary markets falling 0.5 percent compared to the third quarter to 1.9 percent, as seen in the chart to the right. Compared to a year ago, fourth quarter 2017 rent growth declined more significantly in the secondary markets than in the primary ones, falling 1.3 percent compared to 1.1 percent in the primary markets.

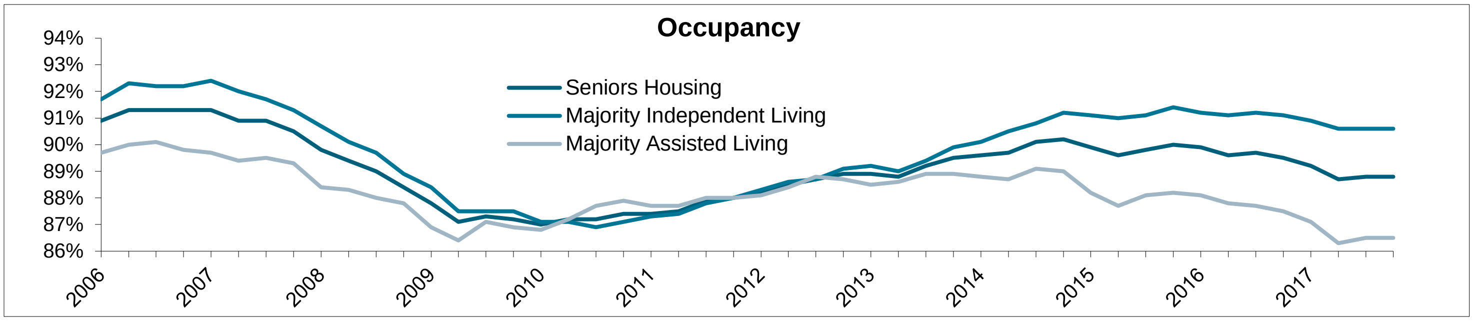




Source: NIC MAP Data Service

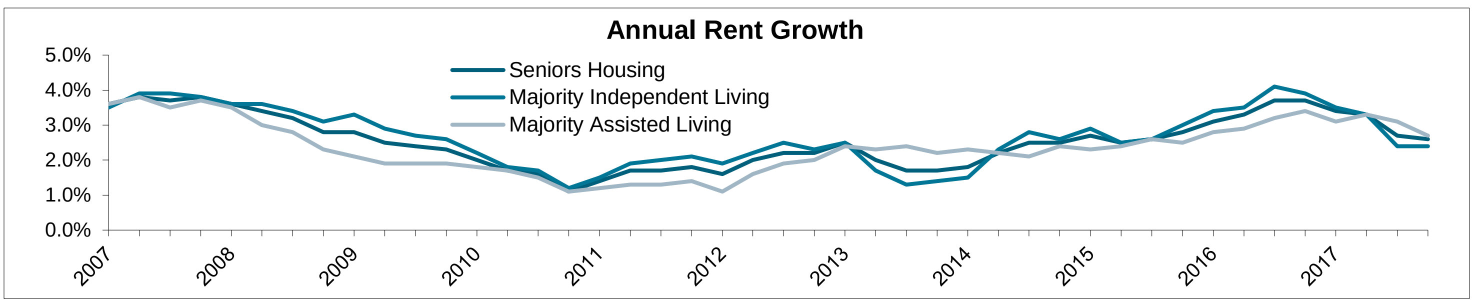
Steady Rent and Occupancy in Second Half of 2017

After declining in late 2016 through mid-2017, occupancy for seniors rental housing properties was unchanged in the fourth quarter of 2017 at 88.8 percent, but remained 0.7 percent down from the prior year, as seen in the chart below. Majority Independent Living (IL) was unchanged from the prior quarter at 90.6 percent, but down 0.5 percent from a year ago. Majority Assisted Living (AL) occupancy was also unchanged from the prior quarter at 86.5 percent, a 1.0 percent decrease from the fourth quarter of 2016.



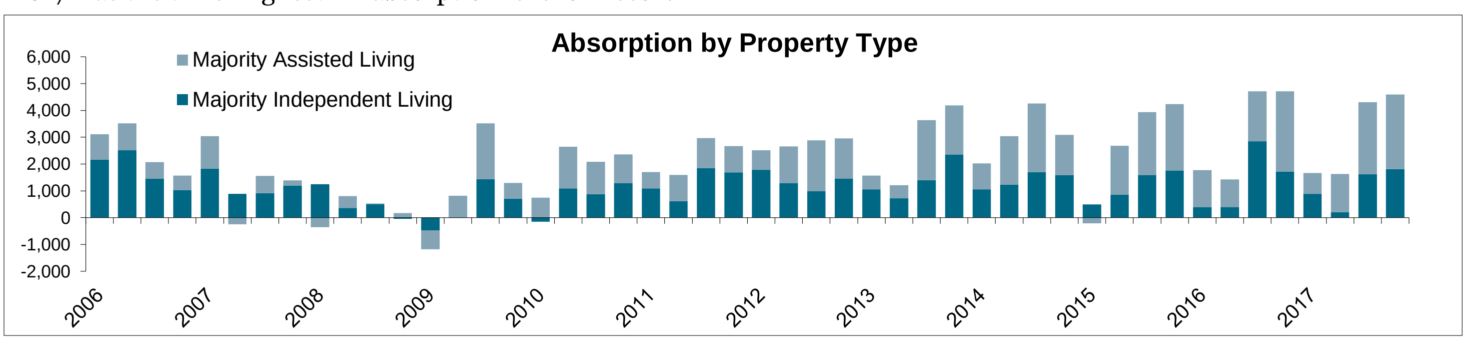
Source: NIC MAP Data Service

Rent growth for seniors housing was down slightly in the fourth quarter of 2017, declining to 2.6 percent, 0.1 percent below the prior quarter and 1.1 percent below year-ago levels, as seen in the chart below. The underlying trends for IL and AL diverged slightly: Majority IL rent growth was unchanged at 2.4 percent for the fourth quarter of 2017, while Majority AL rent growth slowed more measurably, declining 0.4 percent to 2.7 percent.



Source: NIC MAP Data Service

Total seniors rental housing absorption in the fourth quarter of 2017 was 4,589 units, the third-highest level on record, as seen in the chart below. Results for the underlying segments were similar during the quarter: Majority IL absorption was up 12.0 percent compared to the third quarter, and Majority AL absorption was up just 4.0 percent, although fourth quarter 2017 was the third-highest AL absorption level on record.

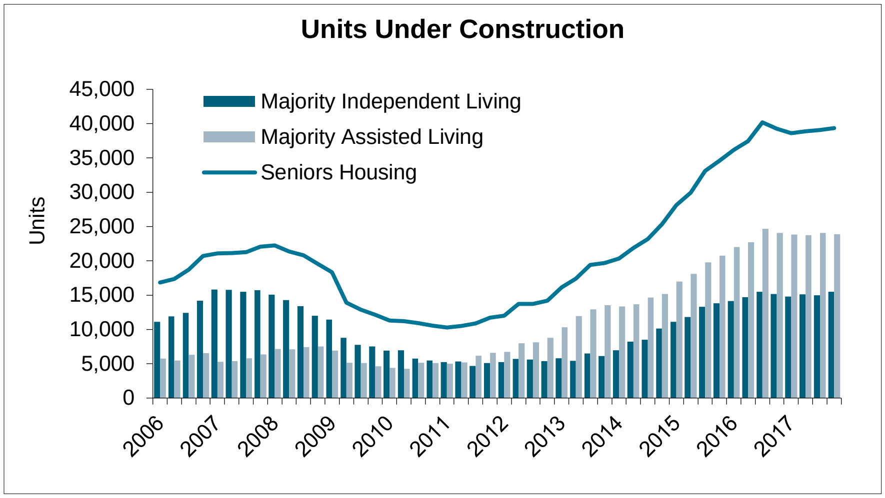


Source: NIC MAP Data Service

Construction Activity Level Steadied

After decreasing earlier in 2017, the number of seniors rental housing units under construction rose slightly in the fourth quarter of 2017 to 39,354 units, the second-highest level on record, as seen in the chart to the right. The number of units under construction was up just 0.3 percent from a year ago. Compared to the fourth quarter of 2016, the number of AL units under construction was down 0.9 percent in the fourth quarter of 2017, while the number of IL units under construction was up 2.1 percent.

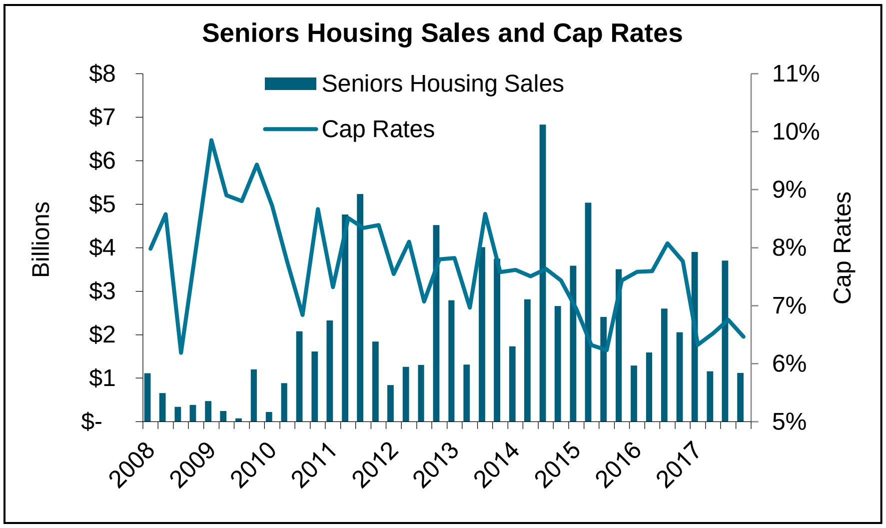
The number of units added to inventory in the fourth quarter declined to 5,127, up 17.2 percent from a quarter ago but down 16.7 percent from the fourth quarter of 2016.



Source: NIC MAP Data Service

Sales Fell in Fourth Quarter

Total seniors rental housing sales volume in the fourth quarter of 2017 was down 70 percent from the third quarter to $1.1 billion, but annual volume of $9.9 billion for 2017 was up 31 percent from 2016, as seen in the chart to the right. Fourth quarter's sales involved 72 properties, the fewest since the first quarter of 2010. NIC attributed the slow sales to hesitation by investors waiting for resolution of tax reform. Cap rates fell from the prior quarter to 6.5 percent in the fourth quarter, down modestly from (the revised) 6.8 percent in the third quarter.



Source: NIC MAP Data Service

Industry Outlook Remains Positive in 2018

Seniors rental housing market conditions remained generally stable in 2017. The continued delivery of new units into the market was once again met with steady demand, though these new units were likely the cause of the minor easing of rent growth later in the year. Rent growth in 2017 slowed from the rapid growth in 2016; the slowdown was difficult to avoid after so many quarters of remarkably strong performance. Over the next year, inventory growth is expected to outweigh absorption, resulting in modest easing of occupancy levels, particularly for Majority AL units. However, the solid performance of absorption levels indicates steady underlying demand, with the potential for rent growth to stay positive. The overarching caveat for this sector remains economic conditions. As long as there is a generally healthy economy coupled with a stable single-family housing sales market, seniors housing demand is expected to remain steady over the near term.

It is important to note that the seniors rental housing sector is expected to experience robust levels of new supply for the foreseeable future to meet the needs of the nation's expanding older population. The solid performance since 2012 has shown that rent growth can be attained even when new supply results in rising levels of inventory and softening occupancies. Supply growth may prevent further occupancy tightening in the long term, but continued positive rent growth appears to be sustainable as long as the national economy remains stable.

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