

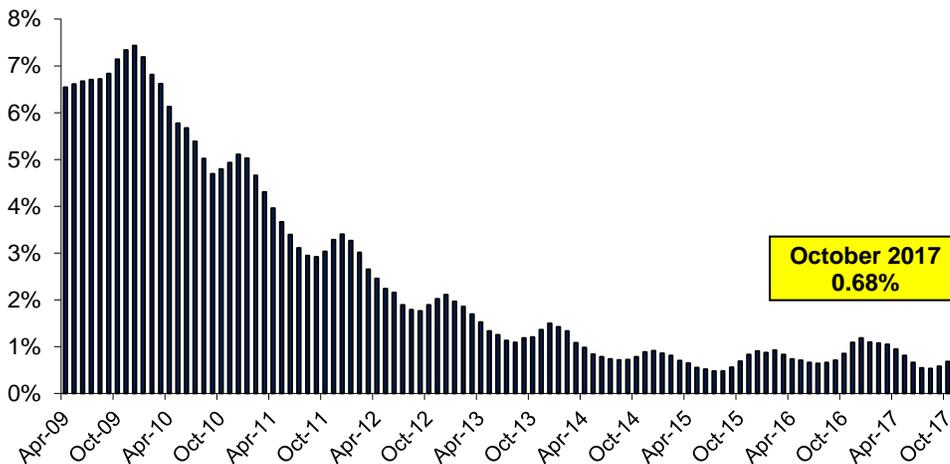


Multifamily Market Commentary – December 2017 Concessions Stay Low Amid Surge of New Supply

Over the past three years, apartment market fundamentals have been remarkably resilient with solid rent growth, strong net absorption, and low vacancy rates. The market has seen a significant volume of new supply come online again this year, which might have led property owners to reduce rents to keep units full. But ongoing demand from new rental household formations has kept that from happening in 2017, at least on a nationwide basis.

Offering concessions is one way property owners can attract tenants in a competitive market. Concessions are enticements with economic value for renters, such as periods of free rent, free utilities, or other amenities. Concessions data from RealPage’s Axiometrics, a Dallas-based commercial real estate researcher, shows that in most markets, property owners have not needed to use these methods to keep units occupied. As seen in the chart below, concessions remained near historically low levels over the last four years and have declined modestly from a year ago. In fact, the value of concessions has remained below 1 percent of annual asking rents for over two years. That’s down from more than 7 percent in 2009 – the equivalent of three to four weeks of annual rent.

National Multifamily Concession Rate

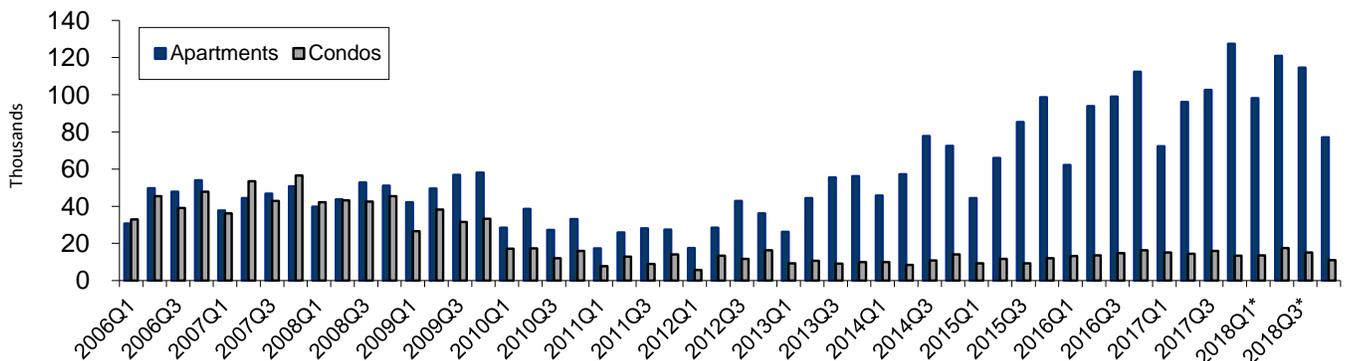


| Concession Magnitude | Rent Equivalent |
|----------------------|-----------------|
| 8.3% | 4 weeks |
| 6.2% | 3 weeks |
| 4.2% | 2 weeks |
| 2.1% | 1 week |
| 1.0% | ½ week |
| 0.9% | 3 days |
| 0.6% | 2 days |
| 0.3% | 1 day |

Source: Axiometrics, a RealPage company

The nation’s multifamily markets continue to see an exceptional surge in the supply of new apartments. In 2017, the industry expects to complete nearly 400,000 new apartment units, according to Dodge Data & Analytics. That’s after it added nearly 370,000 units in 2016, as seen in the chart below.

Multifamily Construction Pipeline – Condos and Apartments Completed and Underway



Source: Dodge Data & Analytics – November 2017

* Anticipated

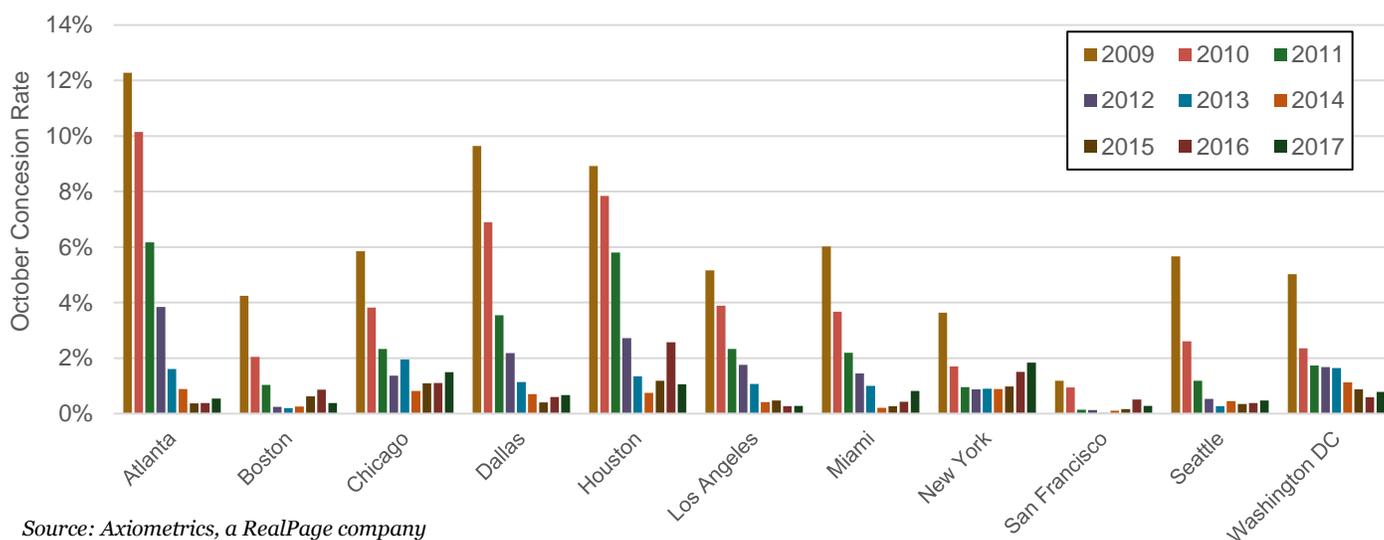


Concessions Rise Slightly in a Few Major Markets

While nearly 400,000 new apartment units are expected to be completed in 2017, these units are not evenly distributed on a national basis. In fact, the majority of the new apartment supply is concentrated in approximately 12 metropolitan areas, and mostly in an even smaller set of submarkets within those metropolitan areas. The most active metropolitan areas in the country for apartment development continue to be New York, Dallas, Washington, and Los Angeles. New York has more than 63,000 units under way, while the other three exceed 20,000 each. Atlanta, Seattle, and Denver follow with slightly fewer units, and Boston, Chicago, and Miami round out the top 10. Miami has been more active this year and joined the top 10 metropolitan areas, unlike in 2016 when Houston was on the list.

These 10 major metropolitan areas have seen remarkable levels of new supply over the past few years, but pent-up demand has helped absorb this wave without property owners having to greatly increase concessions, as seen in the chart below.

Multifamily Concession Rate by Market – Select Metropolitan Areas



Source: Axiometrics, a RealPage company

Previously, the Houston apartment market was an exception to the low concession rate trend. Its overall level of concessions reached a low of 1.4 percent in October 2013. However, following Hurricane Harvey, the area lost many rental units and the apartment market tightened. The change in market conditions led to a drop in concessions to 1.1 percent as of October 2017, after hitting 2.6 percent in 2016. Houston's apartment market had been going through a volatile period before it was impacted by the storm, including dealing with falling oil prices and related weakness in the area's job growth. Now, it has to adjust to the shock of the units lost due to flooding.

Among other metropolitan areas experiencing a surge in supply, Miami has seen a rise in concession rates compared with the prior two years, but the overall concession rate still remains low at 0.8 percent as of October 2017, and is well below its peak concession levels of 2009 through 2010, as seen in the chart above. Atlanta, Chicago, New York, and Washington DC have also seen a small but noticeable rise in concessions over the past year.

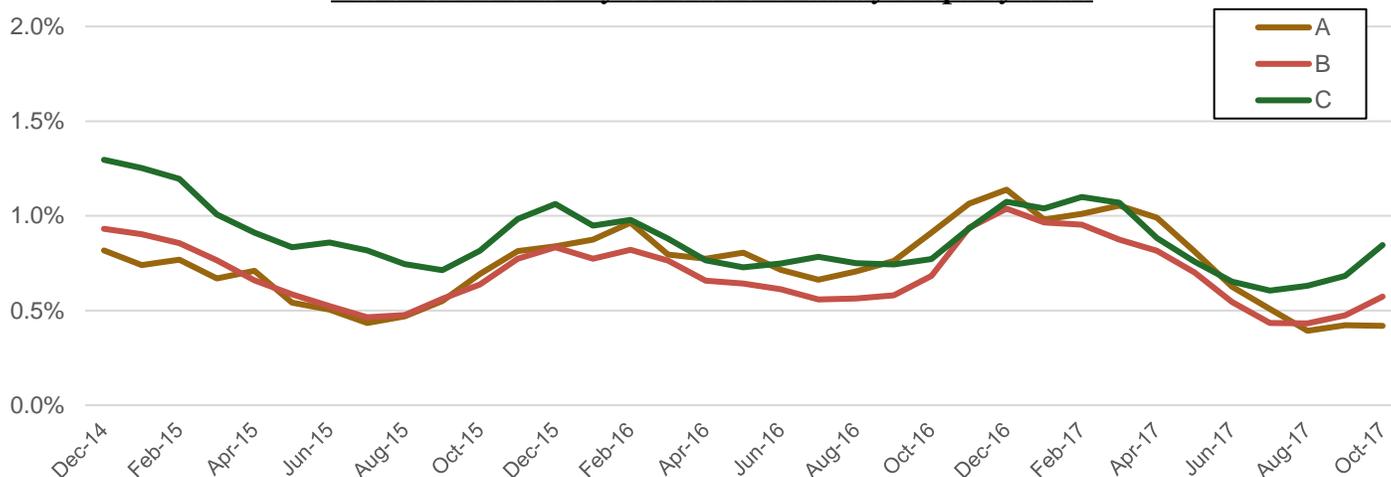
All Property Types Seeing Very Low Concession Rates

The recent surge of new apartments has generally occurred among higher quality buildings, which offer more amenities and higher-end finishes and appliances. Under pressure from increased competition among these Class A properties, owners ordinarily might have to offer higher concessions to fill units. However, with demand for apartments remaining robust, most Class A properties appear to have navigated the supply surge without having to significantly increase concessions.



As with the overall market, concessions for Class A properties have declined over the past year. Class A concessions fell from 0.9 percent in October 2016 to 0.4 percent in October 2017, the lowest current concession rate among the classes. This is remarkable, considering that the 400,000 or so apartment units added to the nation's housing stock during this period consisted primarily of Class A properties.

National Multifamily Concession Rate by Property Class



Source: Axiometrics, a RealPage company

Over the past several years, concessions for Class B and C properties have generally remained below 1 percent, which is noteworthy considering the overall level of new supply. Possibly as the result of competitive pressures, in the past few months both of these classes have experienced a slight rise in concessions. Class C has experienced the largest rise, as its concession level reached 0.85 percent, though that is still below its peak of 1.1 percent at the beginning of the year.

Will the Next Part of the Real Estate Cycle See Rising Concessions?

Although net absorption levels have slowed relative to last year, there has been no significant change in concessions. Considering the large volume of units that are currently underway and expected to be completed in 2018, it is possible that supply will outpace demand as new units continue to be rolled out. If this happens, property owners may be inclined to increase concessions to entice tenants and keep vacancy rates from increasing. Even with this possibility, it is expected that vacancy rates will remain healthy from a historical perspective, remaining near the long-term average rate of about 6.0 percent.

Rising concession rates have begun to appear in certain submarkets in more expensive metropolitan areas, including in New York, Miami, and Chicago. With more competition on the way, it's possible that national concession rates could start to rise over the next few quarters, particularly for higher-end, Class A projects. However, the low concession rate for Class A properties — which currently account for a huge proportion of the units underway and coming online — suggests strong underlying demand. The minor rise in recent concession rates for Classes B and C could be a harbinger of competitive pressures impacting the market, thereby leading to lower rent growth. Considering that all classes of properties have seen remarkably low concession rates for an extended period, we expect the apartment market will likely see concessions start to rise in 2018 as the overall apartment market begins to soften.



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Multifamily Economics and Market Research
December 2017

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