Fannie Mae

FEBRUARY 2024

2024 Outlook for Multifamily Affordability – Many Renters Remain Cost-Burdened

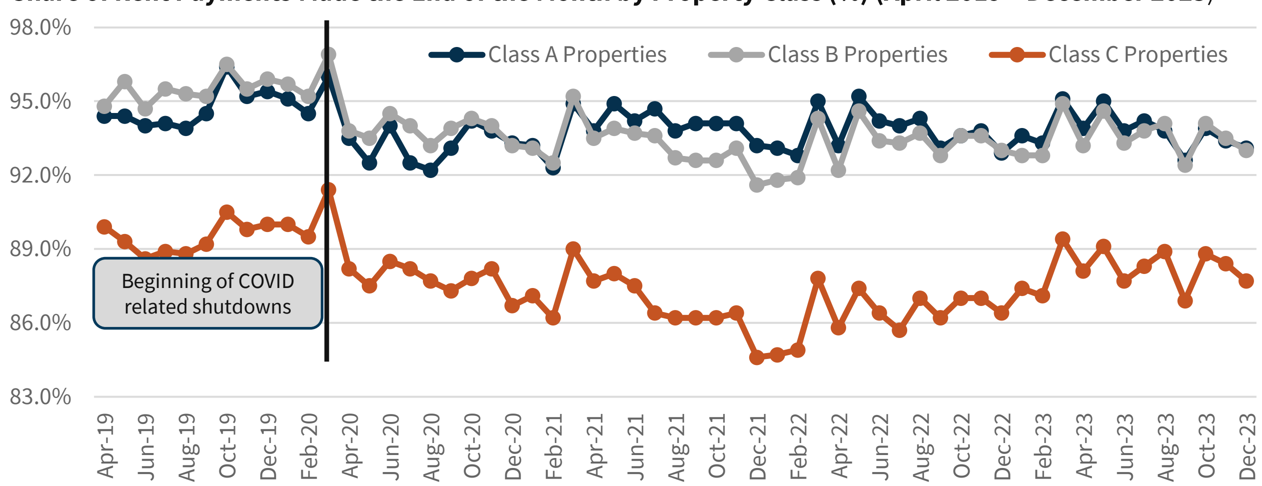
We believe that the vacancy rate rose by an estimated 0.25% in 2023 to 6.0%, as of December 31, 2023, and that year-over-year rent growth slowed to just 0.8% nationwide. Indeed, we estimate national rent growth turned negative in Q4 2023, falling by an estimated 0.7% in a single quarter to $1,500. While on the surface, these are positive trends in terms of multifamily rental affordability, they are not yet having much of an impact for many renters, especially lower-income renters.

On-Time Rent Collections Still Below Pre-Pandemic Averages

Even prior to the pandemic, some lower-income renters struggled to pay their rent. As shown in the chart below, typical Class C rent payments between April and December 2019 trailed collections in Class A and B properties by between 5 and 6 percentage points, according to data from RealPage, Inc. The share of rent payments made by the end of the month by Class C renters during this time was estimated to have averaged 89.4%, compared to about 94.7% for Class A units and 95.5% for Class B units.

From April 2020 through November 2021, just over 86% of Class C renters were able to pay their rent by the end of the month, compared to approximately 89% of all renters prior to the start of the pandemic. While not as stark, Class B renters also saw some erosion in payments over the same time period, to just over 93%, down from 95.5%.

Share of Rent Payments Made the End of the Month by Property Class (%) (April 2019 – December 2023)



Source: RealPage, Inc.

Some Lower Income Renters Still Behind on Rent

The share of renters making payments in any given month can vary. Despite eroding affordability, expired eviction moratoriums, and the end of federal rental assistance and income support, an improving economy meant most renters were able to pay their rent. The share of Class C renters able to pay their rent in the month it was due improved to 89.4% in March 2023, up from a low of 84.6% in December of 2021 and stayed above 87% through December 2023. Nevertheless, the share of Class C renters able to pay their rent was regularly above 89.0% and even above 90% in some months prior to the pandemic. Indeed, the ability of some Class C renters to pay their rent has not fully recovered.

The recovery for Class B renters also fell short. As shown in the chart on the prior page, the share of Class B renters able to pay their rent in the month it was due improved to just under 94.9% in March 2023, up from a low of 91.6% in December 2021 – and has generally stayed above 92% through December 2023. In comparison, the share of Class B renters able to pay their rent was regularly above 95.0% prior to the pandemic. The difficulty of a number of renters across all classes of units is not surprising given the gap between rent growth and wage growth over the past several years.

Wage Growth More Relevant for Renters

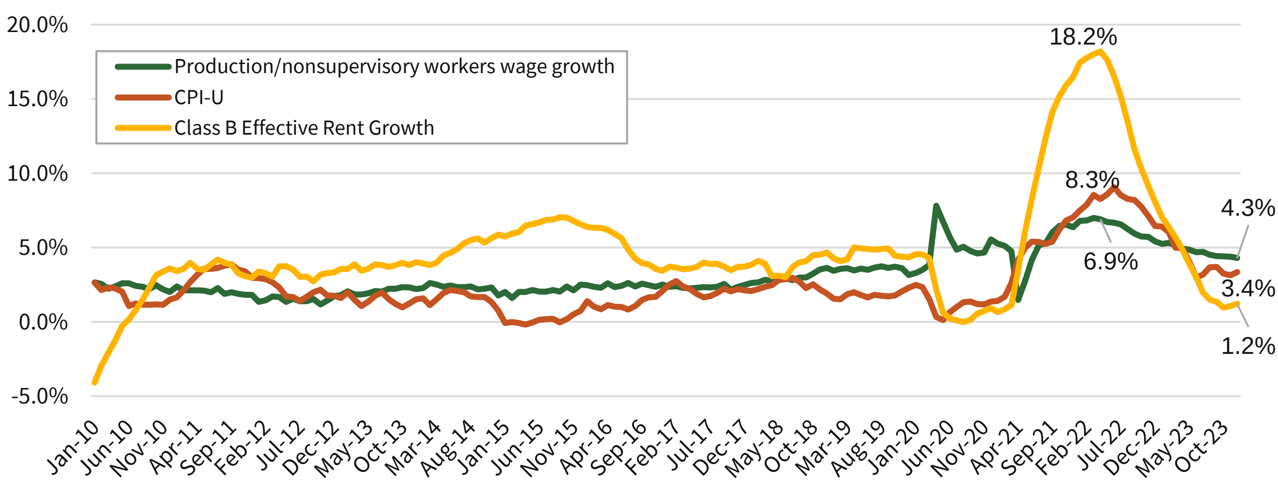
Wages measure earnings from work, while income can include non-work earnings such as interest and dividends. While growth in income will help with rental affordability, many renters rely solely on wages, making wage growth an important indicator of affordability.

Not Much Improvement in Renter Affordability

Improvement in rental affordability is primarily attained when wage growth meaningfully outpaces rent growth. Looking at Class B rents, defined here as those rents that fall between the top 20% and bottom 20% of the rent distribution for a given market and therefore in the mid-60% of the rent distribution, is a good indicator of trends in rental affordability. As shown in the chart below, since April 2023, many Class B renters are gaining back some lost ground as the rental market has softened. According to data from RealPage, as of December 2023, year-over-year Class B effective rent growth slowed to 1.2%, which was below the 4.3% recorded for wage growth for non-supervisory employees, and even slower than the 3.4% inflation rate.

However, many renters are still trying to make up for lost ground. For example, in April 2022, year-over-year wage growth was 6.9%, but Class B rent growth was a whopping 18.2%, while inflation was 8.3%. In fact, except for the 13-month period at the start of the pandemic, year-over-year rent growth for Class B units outpaced wage growth almost every month from August 2010 through March 2023.

Year-over-Year Change in Private Sector Nominal Average Hourly Earnings and Effective Rent (Jan. 2010– Dec. 2023)

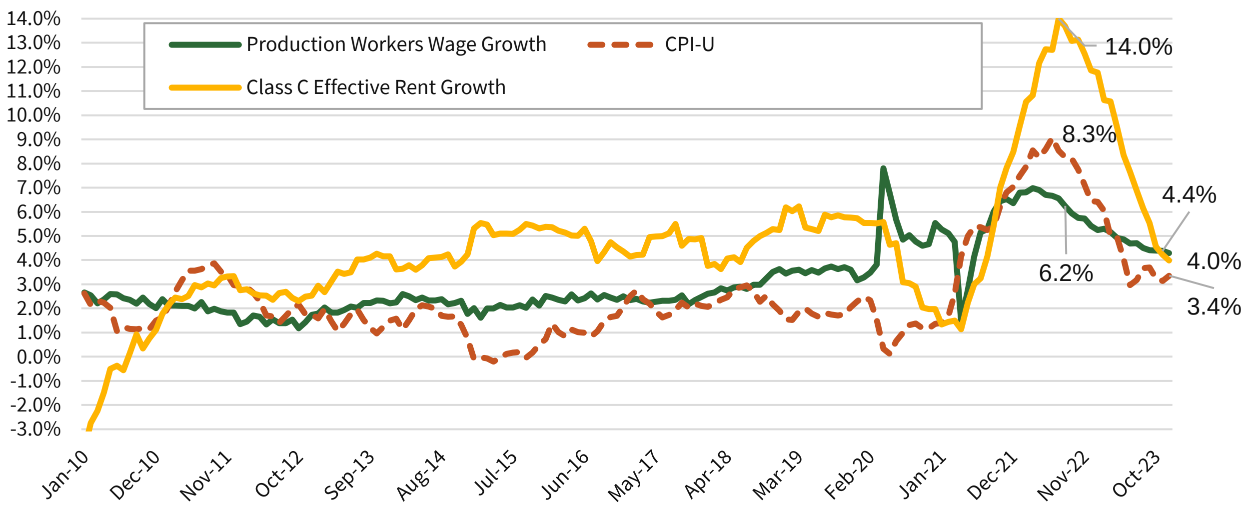


Source: Moody's Analytics, RealPage

Class C Affordability Not Improving

Class C rents, defined as those that are in the bottom 20% of the rent distribution for a given market, are some of an area's most affordable rents. These are also the type of units that tend to be affordable for production and non-supervisory employees. However, as shown in the chart below, Class C renters are making even less headway than Class B renters. According to RealPage, as of December 2023, year-over-year Class C rent growth slowed substantially to 4.0% from a high of 14.0% recorded in August 2022. Even so, year-over-year December 2023 rent growth was just barely below the 4.4% recorded for wage growth for non-supervisory employees and still above the 3.4% inflation rate. As a result, many Class C renters are unlikely to have seen any real benefit from slowing rent growth to date.

Year-over-Year Change in Private Sector Nominal Average Hourly Earnings and Effective Rent (Jan. 2010– Dec. 2023)



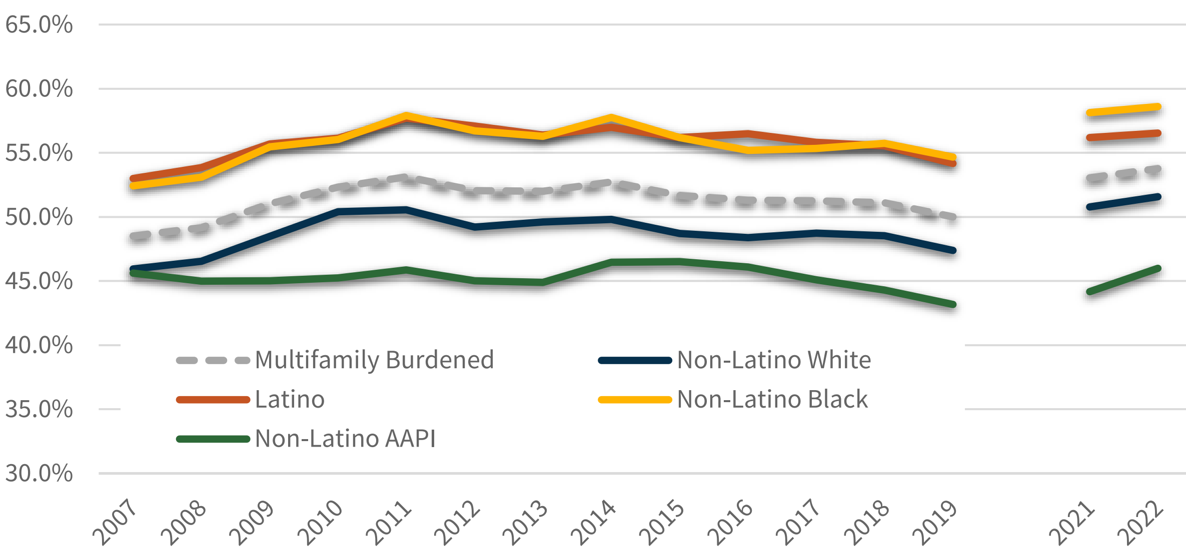
Source: Moody's Analytics, RealPage

More Multifamily Cost-Burdened Renters

With rent growth outpacing income growth, it is not surprising that there has been a significant increase in the share of cost-burdened renters, defined as those spending more than 30% of their household income on rent and utilities. As shown in the chart on the next page, there has been a significant jump in cost-burdened renter households in just the past three years. According to the 2022 American Community Survey, 53.8% of multifamily renters were cost-burdened, representing an estimated 11.4 million renter households. That is an increase of more than 1.4 million multifamily renter households from three years prior, when 50.0% were cost-burdened (in 2019).

Further, the share of cost-burdened multifamily renter households is even higher than it was during the Great Recession, when 48.5% of households were cost-burdened, representing 7.8 million multifamily renter households.

Share of Cost-Burdened Renters (2007-2022)



Source: Fannie Mae tabulations of 2022 American Community Survey Data

Minority Renters Also Experienced Increase in Cost Burdens

As shown in the chart above, Black and Latino multifamily renter households have had a higher overall level of cost burden since at least 2007 when their levels reached 52.4% and 53.0%, respectively, compared to an average cost-burdened rate of 48.5% for all multifamily renter households.

But there has also been an increase in minority cost-burdened renter households in just three years. Black multifamily renter households showed the greatest jump, at 3.9 percentage points. Data from the 2022 American Community Survey shows that 2.5 million Black multifamily renter households were cost-burdened in 2022, representing 58.6% of Black multifamily renter households, an increase from 54.7% in 2019.

Similarly, 2.4 million Latino multifamily renter households were cost-burdened in 2022, representing 56.5% of all Latino multifamily renter households. This is up from 54.2% in 2019.

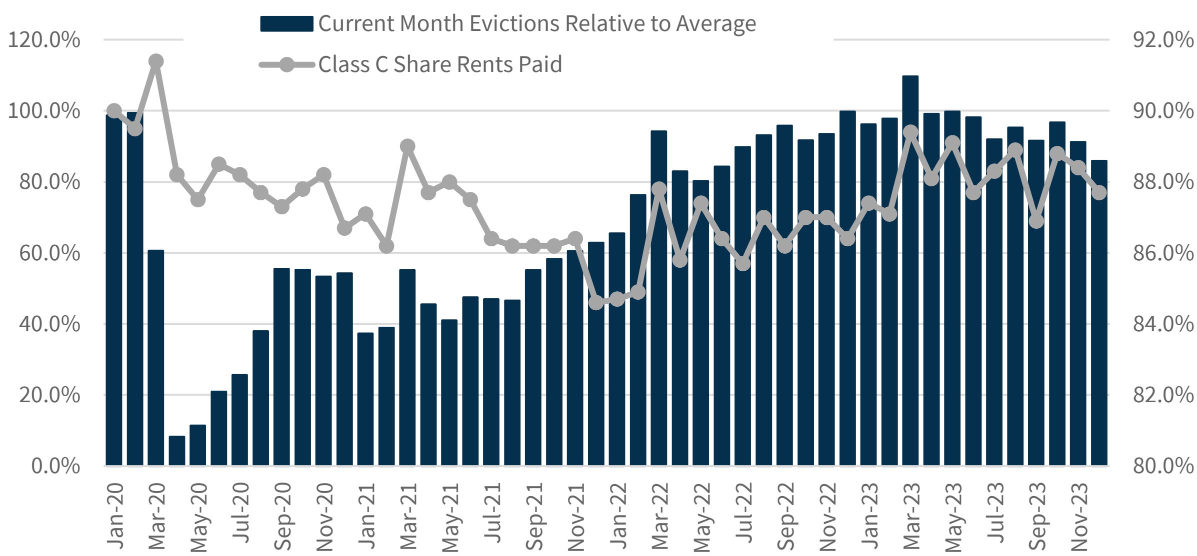
Non-Latino White multifamily renter households saw the highest increase in cost-burdened multifamily rental households. In 2022, 5.2 million non-Latino White multifamily renter households were cost-burdened, representing 51.6% of all non-Latino White multifamily renter households, an increase from 47.4% in 2019. However, even with this increase, the share of non-Latino White cost-burdened households remained 2.2 percentage points below the national average in 2022.

With the increase in all types of cost-burdened renter households since 2019, it is not surprising that evictions have also risen.

Evictions have Returned to Historic Levels…

The Eviction Lab at Princeton, which monitors eviction filings in 34 cities and 10 states across the country, has indicated that eviction levels have been rising since the lifting of the Centers for Disease Control's eviction moratorium in August 2021. As shown in the chart below, eviction filings reached parity with the pre-pandemic historic average in December 2022 and remained near this level through June 2023. According to the Eviction Lab, 1.1 million evictions were filed in 2023, in line with pre-pandemic filings.

Eviction Filings Relative to the Historic Average



Source: Jacob Haas, Jasmine Rangel, Juan Pablo Garnham, and Peter Hepburn, Preliminary Analysis: Eviction Filing Trends After the CDC Moratorium Expiration, Princeton University, December 9, 2021; Class C rent data from RealPage, Inc.,

…But Have Been Trending Downward

It is interesting to note that the level of evictions relative to the pre-pandemic historic average in the same month has declined a small amount since June 2023, generally ranging from 91% to 97%. We believe this is in part due to ongoing steady job growth and the easing of rent growth experienced in certain markets.

However, it may also be due to additional resources available to renters. During the pandemic, some local jurisdictions implemented eviction diversion courts. In addition, some municipalities like New York City and Philadelphia started to fund legal representation for renters receiving eviction filing notices. According to the Eviction Lab, as of December 2023, 6,690 New York City renters were subject to eviction filings, down from more than 18,000 on average in the month of December 2019, accounting for a 64% decline in eviction filings. Similarly, there were an estimated 970 filings in Philadelphia in December 2023, down from 1,680 in December 2019, representing a 42% decline in eviction filings.

Nevertheless, the share of Class C renters able to pay their rents by the end of the month appears to have declined over the past three months, as shown in the chart above. This may soon increase the level of eviction filings, as there is a lag between non-payment of rent and the filing of an eviction notice.

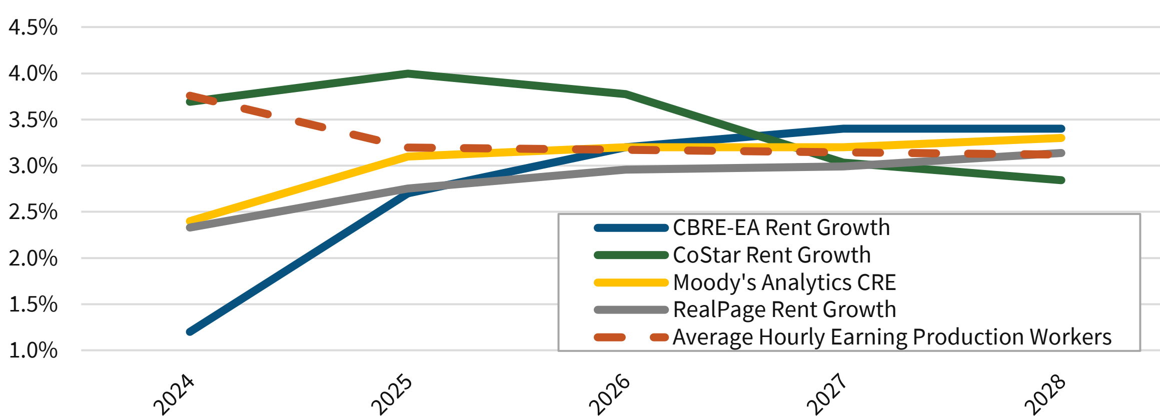
Moderating Rents Not Expected to Last Long

While rent growth has moderated considerably from recent highs, it is expected to increase again, as shown in the chart below. While CBRE Econometric Advisors, Moody's Analytics CRE and RealPage project slower rent growth for 2024 at between 1.2% and 2.4%, CoStar has a higher estimate of 3.8%. The slower rent growth expected in the short term is due to elevated deliveries of new multifamily rental units.

According to preliminary data from Dodge Data & Analytics Supply Track, which distinguishes between multifamily properties consisting of apartment and condominium units, more than 500,000 apartment units were likely completed in 2023, up notably from 2022's 475,000 units – the most recent peak year for new deliveries. And although Dodge Data & Analytics is currently tracking nearly 685,000 multifamily rental units slated for completion in 2024, we believe it is very unlikely that all those units will be completed before year end, due primarily to ongoing construction labor shortages, rising material costs, economic uncertainty, and delays, notably permitting and financing delays.

Further, delivery of new multifamily units is expected to slow after 2024 due to a decline in permitting and starts in 2023. According to the Census Bureau, the seasonally adjusted annual rates for multifamily permitting and construction starts were down 27% and 10% respectively from December 2022. As a result, most vendors are projecting rent growth will pick up steam starting in 2025. In fact, as shown in the chart below, all four vendors project annual rent growth of at least 2.7% or higher annually from 2025-2028.

Year-over-Year Change in Rents and Average Hourly Earnings of Production Workers 2024 and Beyond



Source: RealPage, CBRE-EA, Moody's Analytics CRE, CoStar, Moody's Analytics

Wage Growth is Expected to Moderate Affordability Improvement

While the growth of average hourly earnings of non-supervisory and production workers has improved substantially since April 2021, Moody's Analytics is projecting a slowdown starting in 2025 with wage growth returning to more normal levels. As shown on the chart above, Moody's Analytics is projecting an annual increase of around 3.1% starting in 2025. This is in line with the rent growth projections for CBRE, Moody's Analytics CRE, and RealPage that are also projecting rent growth in the range of 3% over this timeframe, but less than CoStar's projection above 3.0% annually until 2028. As a result, we do not expect any gains in affordability in 2023 and 2024 to overcome a decade where rent growth has mostly outpaced wage growth for many Class B and C renters.

Tanya Zahalak

Multifamily Economics and Strategic Research – Economics

Advisor Economist

Multifamily Economics and Strategic Research

February 2024

Opinions, analyses, estimates, forecasts, and other views of Fannie Mae's Economic and Strategic Research (ESR) Group included in these materials should not be construed as indicating Fannie Mae's business prospects or expected results, are based on a number of assumptions, and are subject to change without notice. How this information affects Fannie Mae will depend on many factors. Although the ESR Group bases its opinions, analyses, estimates, forecasts, and other views on information it considers reliable, it does not guarantee that the information provided in these materials is accurate, current, or suitable for any particular purpose. Changes in the assumptions or the information underlying these views could produce materially different results. The analyses, opinions, estimates, forecasts, and other views published by the ESR Group represent the views of that group as of the date indicated and do not necessarily represent the views of Fannie Mae or its management.