Multifamily Market Commentary – April 2015
Lower Oil Prices and Multifamily Housing Sector – More Winners than Losers

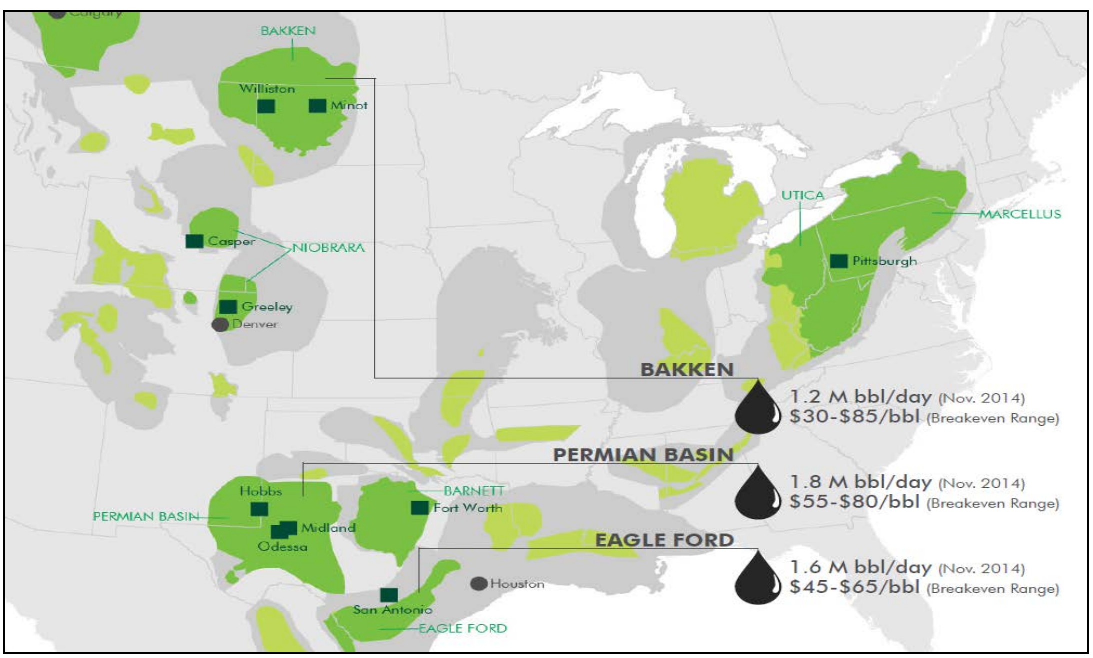
The recent drop in oil prices has been an unanticipated shock—or a welcome development—to both local and national economies. The rise in North American oil production and a continued high level of output from traditional overseas oil producers, coupled with an expected lull in international oil demand this year, has resulted in a worldwide supply glut. This glut has resulted in oil prices dropping to around $50 per barrel as of February 2015, down significantly from around $90-$100 per barrel during most of 2014. While prices have recently inched up from their nadir, market forecasters expect that prices should rise and settle at around $65 a barrel for the remainder of 2015.

Unfortunately, at $65 per barrel many North American drilling locations become uneconomical. In fact, a number are already being shuttered, most notably in North Dakota. At first glance, this might appear to potentially be alarming for multifamily investors as recent economic growth—and, in turn, household growth—in several metros has been fueled by oil exploration and production via hydraulic fracturing, or "fracking." In reality, these low oil prices will probably have more of an immediate and negative impact on the more volatile office and industrial sectors, since those property types will endure the brunt of rig closures and production slowdowns first, before the multifamily housing sector begins suffering from adverse demographic trends.

Fracking Created an Oil Boom in Certain Areas

The vast majority of recent U.S. oil production has come out of two states: North Dakota and Texas. The Bakken formation in the region surrounding Williston and Minot, ND has been producing an estimated 1.2 million barrels of oil per day for the past several years, although that is expected to decline considerably this year. In Texas, the Permian, Eagle Ford, and Barnett formations have been producing around 3.4 million barrels per day. In comparison, the Marcellus and Utica formations in the greater Pittsburgh region, combined with the Niobrara formation in the greater Denver area, together produce fewer than 350,000 barrels per day, instead relying primarily on producing natural gas.

U.S. Oil Producing Regions and Well Breakeven Costs



Source: CBRE Research, December 2014

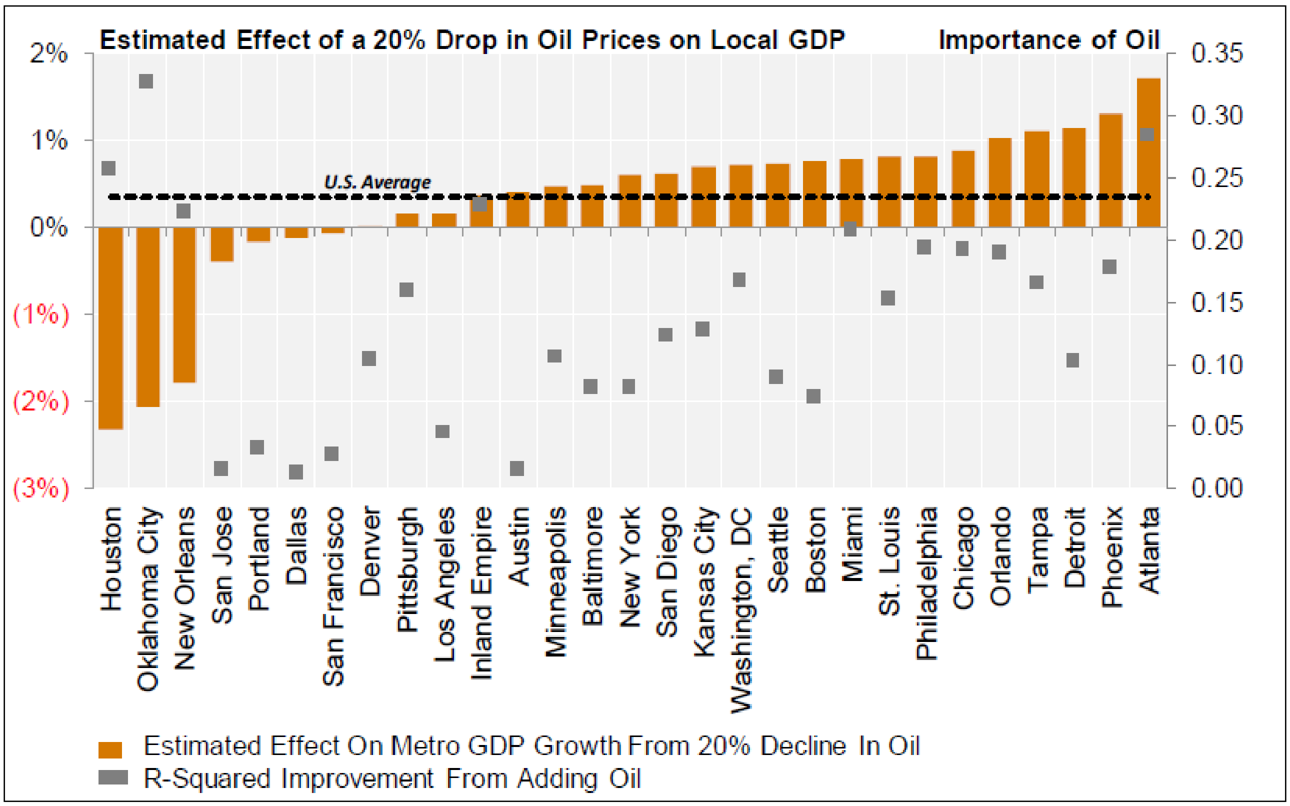
Lower Energy Prices = Good News for the National Economy

Lower oil prices are actually a net stimulus to the national economy, particularly for energy-importing metros. Because lower fuel prices allow consumers to enjoy more immediate disposable income, Moody's Analytics estimates that the recent oil price decline will add anywhere from 0.25 percent to 0.75 percent to this year's Gross Domestic Product, meaning that an impressive $165 billion is now available for consumers to spend in ways other than filling up the tank.

Potential Winners from Low Oil Prices

As seen in the chart below, the metro areas that are expected to benefit from lower oil prices are a diverse set. Some metros, including Atlanta, Philadelphia, and Boston should benefit because it will be less expensive to heat and/or cool buildings and homes. Other metros should benefit because consumers will now have more disposable income, allowing for a stimulus in tourism, in places like Phoenix, Tampa, and Orlando.

Estimated Change in Local GDP Due to Lower Oil Prices



Source: CoStar; R-Squared reflects the magnitude of the importance of oil in a metro's economy

Potential Losers from Low Oil Prices

Among major U.S cities, Houston has the most to lose from lower oil prices and is the only primary metro in the U.S. that is expected to be negatively impacted in a meaningful way. As the energy capital of North America, its economy will be hit with the most direct impact of the shock. Fortunately, that hit is not expected to be devastating since Houston has diversified its local economy in very important ways since the oil bust a few decades ago, which should end up blunting the anticipated drag on overall job growth.

There are several smaller metros that may not be so lucky and are expected to encounter significant economic turbulence and out-right job losses. These metros include Williston, ND; Oklahoma City; and Midland-Odessa, TX; which have been among the fastest growing metros in the country over the past several years, as they have been riding the wave of growth related to new oil well drilling. In addition, New Orleans will likely be negatively impacted, albeit to a lesser extent.

As seen in the table below, there are several metros with nominally large but proportionally small oil industry operations—like Denver, Dallas, and Williamsport, PA—that could see a negative impact on their local economies. However, the positive aspects of low oil prices, like enhanced consumer spending and marginal expansion of manufacturing due to lower energy costs, are expected to balance out any negatives in these metros.

Oil/Gas Industry Employment (Including Support Businesses) and Multifamily Housing

	Jobs (000s)		Oil/Gas	Housing Units (000s)		MF Unit
Metro Area (MSAs)	Oil/Gas	Total	Share	Multifamily	Total	Share
Midland, TX	18.5	74.5	24.8%	10.0	55.2	18.1%
Odessa, TX	7.3	57.5	12.6%	7.1	54.3	13.0%
Farmington, NM	3.4	38.0	8.9%	2.4	49.6	4.9%
Lafayette, LA	13.3	190.6	7.0%	14.4	117.3	12.3%
Casper, WY	2.4	35.0	6.8%	3.6	34.9	10.3%
Houma-Thibodaux, LA	5.3	77.5	6.8%	5.6	83.2	6.7%
Longview, TX	4.5	83.4	5.4%	7.8	88.1	8.9%
Grand Junction, CO	2.4	49.9	4.8%	5.3	63.2	8.4%
Greeley, CO	3.1	69.8	4.4%	11.6	97.5	11.9%
Corpus Christi, TX	6.5	151.2	4.3%	29.8	185.3	16.1%
Victoria, TX	1.3	32.5	4.1%	5.8	50.1	11.6%
Shreveport-Bossier City, LA	6.6	161.9	4.0%	22.1	176.2	12.6%
Bakersfield, CA	7.7	190.0	4.0%	26.2	285.9	9.2%
Abilene, TX	2.1	57.5	3.7%	7.2	70.6	10.2%
Anchorage, AK	5.9	162.4	3.7%	23.1	155.0	14.9%
Oklahoma City, OK	16.8	478.6	3.5%	81.5	544.6	15.0%
Wichita Falls, TX	1.6	48.5	3.2%	8.5	65.0	13.0%
San Angelo, TX	1.0	37.5	2.6%	8.0	47.7	16.8%
Williamsport, PA	1.2	47.2	2.5%	3.3	52.5	6.3%
Houston, TX	49.9	2,334.7	2.1%	602.6	2,363.5	25.5%
Tulsa, OK	8.1	382.4	2.1%	62.5	414.8	15.1%
Laredo, TX	1.5	70.0	2.1%	8.4	75.1	11.2%
Tyler, TX	1.5	86.2	1.8%	10.6	87.8	12.1%
College Station-Bryan, TX	1.1	60.4	1.7%	20.1	96.3	20.9%
Morgantown, WV	0.7	48.6	1.4%	10.8	58.9	18.4%
Fort Smith, AR-OK	1.3	98.2	1.3%	9.0	130.2	6.9%
Charleston, WV	1.1	95.9	1.2%	11.8	142.8	8.3%
New Orleans-Metairie, LA	5.2	470.0	1.1%	86.4	541.3	16.0%
Parkersburg-Vienna, WV	0.3	33.7	0.9%	5.2	75.6	6.8%
Dallas-Fort Worth-Arlington, TX	21.9	2,680.7	0.8%	638.1	2,546.6	25.1%
Denver-Aurora-Lakewood, CO	7.6	1,088.7	0.7%	289.8	1,086.3	26.7%
McAllen-Edinburg-Mission, TX	1.2	175.2	0.7%	20.1	254.8	7.9%
Wichita, KS	1.6	247.8	0.7%	36.0	264.3	13.6%

Source: Fannie Mae Economics & Mortgage Market Analysis, Moody's Analytics, ACS; counts as of 2012.

Not Much Multifamily in Impacted Metros

While housing may be in for a period of decline in fundamentals in certain metros with a disproportionate dependence on oil extraction, in truth, few of these metros have any significant concentration of multifamily housing. Nationally, approximately 18 percent of housing units are in multifamily structures. As seen in the table above, of the 33 metros listed that have a higher-than-average concentration of jobs in the oil and gas industry, just six metros have a concentration of multifamily housing exceeding 18 percent. And of those six metros, the only one with both an unusually high concentration of oil and gas jobs (24.8 percent) as well as a high concentration of multifamily housing (18.1 percent) is Midland, TX.

What's Ahead for Houston?

Houston is headed for a slowdown, no doubt about it. However, there is little agreement about the severity of the slowdown. Fortunately, none of the major macroeconomic and commercial real estate data providers expect the Houston economy to fall into recession. The general consensus is that Houston's job market will slow from being one of the fastest-growing in the nation, to one that achieves just national average growth rates. For example, Moody's Analytics is forecasting that Houston's 2015 job growth will be about half of what was previously expected, but still viable enough to produce an estimated 63,000 new jobs in 2015. Commercial real estate data provider Axiometrics has a slightly more optimistic forecast: 73,000 new jobs in 2015, down from 93,000 prior to the oil price decline, or about 20 percent fewer jobs than previously expected.

Prior to the recent decline in oil prices, the apartment supply surge was well on its way in Houston. After several years of apartment market tightening, Houston was already expected to see some easing in rent growth and occupancy levels this year, as new supply hits the market. Now, with the anticipated slowing down of job growth, there is likely to be a short-term oversupply of units over the next 12 to 24 months.

Previous Undersupply Will Help Houston Now

There are about 18,000 new apartment units underway in Houston, with expected completions occurring over the next two years. With job growth anticipated at about 2 percent, that should produce demand for about 13,000 units, which would appear to create a supply/demand imbalance. Mitigating this condition, however, is the fact that Houston has been undersupplied over the past several years: Only 22,500 units were completed since 2011 but more than 250,000 jobs were added, creating estimated demand for about 50,000 multifamily rental units.

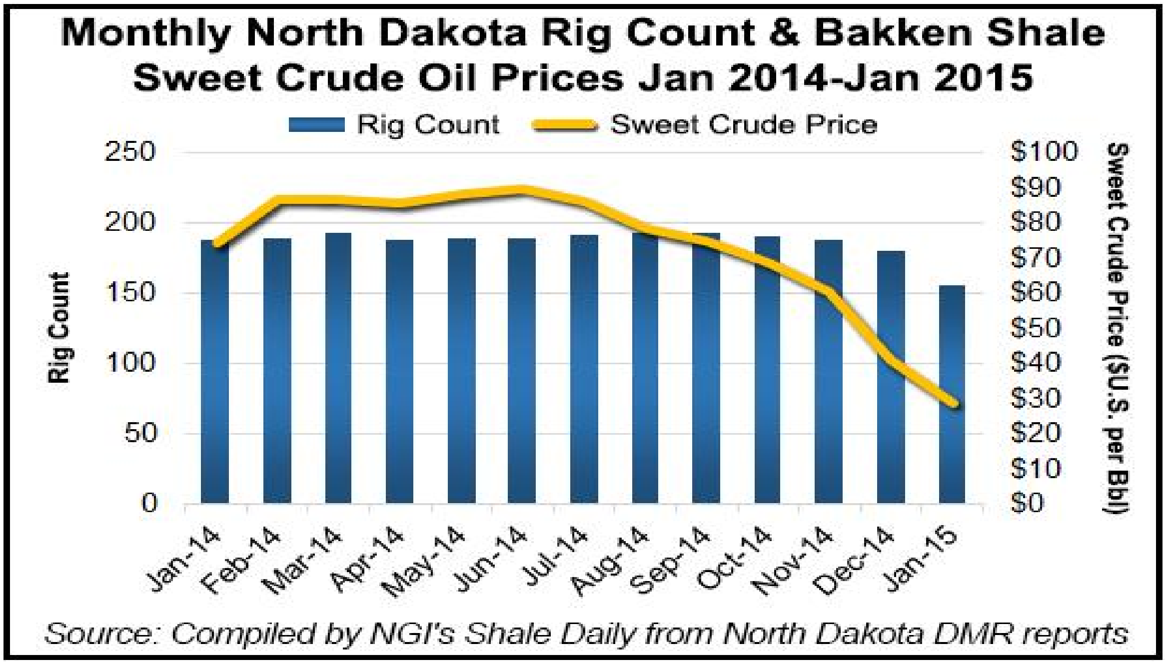
Worthy of note is that sections of Houston will actually *benefit* from low oil prices. The metro's east side submarket has been seeing a surge in construction of chemical and manufacturing plants that are taking advantage of low natural gas prices. This is expected to continue, and possibly expand, if oil prices remain low.

North Dakota: A Slippery Slope

North Dakota has been one of the primary beneficiaries of the North American fracking boom and Williston, in particular, has been the center of that activity. Williston has grown tremendously over the past few years, to nearly 30,000 people, and is the nation's fastest growing micropolitan area. It has seen its population increase by an average 7.0 percent per year since 2010, compared to just 0.7 percent growth at the national level. Needless to say, this extraordinary growth has occurred specifically because of drilling activity in the area.

Now with an extended period of low oil prices, the Williston metro area and the entire state could fall into a recession. While extraction costs are estimated to be lower here than in some areas, the combined cost of construction of new wells and transportation of crude oil to refineries located on the coasts of the Gulf of Mexico and the Mid-Atlantic will likely make new investments in the area uneconomical.

As seen in the chart below, as the price of oil declines, the state's active rig count also declines—and as of February 2015, it has only worsened. The state's active rig count has declined to 121, down from 190 a year ago, according to data from the North Dakota Department of Mineral Resources. This means that the state is now unable to produce its previous output level of about 1.2 million barrels per day. In addition, of these active rigs 115 are concentrated in just four counties—Dunn, McKenzie, Mountrail, and Williams—all of which are located in the most prolific section of the Bakken formation.



Williston's Multifamily Sector Likely Impacted

Williston has a fairly large multifamily inventory considering its rural setting and relatively small population size. The influx of workers coming to the oil fields has resulted in a significant housing shortage and a sizeable inventory of temporary housing. As of 2013, there were about 6,000 multifamily housing units in Williston, according to a recent City of Williston/NDHFA Housing Study. Multifamily housing, which likely includes this sizable inventory of temporary dwellings, represents 49 percent of all housing stock, with about 9 percent consisting of mobile homes and another 40 percent consisting of single-family homes.

Rents already appear to be declining and concessions commonplace. For instance, a review of one rental apartment website reveals concessions of $550 being offered on a $1,800 monthly rental, or about -2.5 percent—significantly above the national average of just -0.9 percent. Williston's multifamily sector is expected to see further decreases in rent and higher concession rates if the rig counts continue declining over the next few months—a likely scenario, we believe.

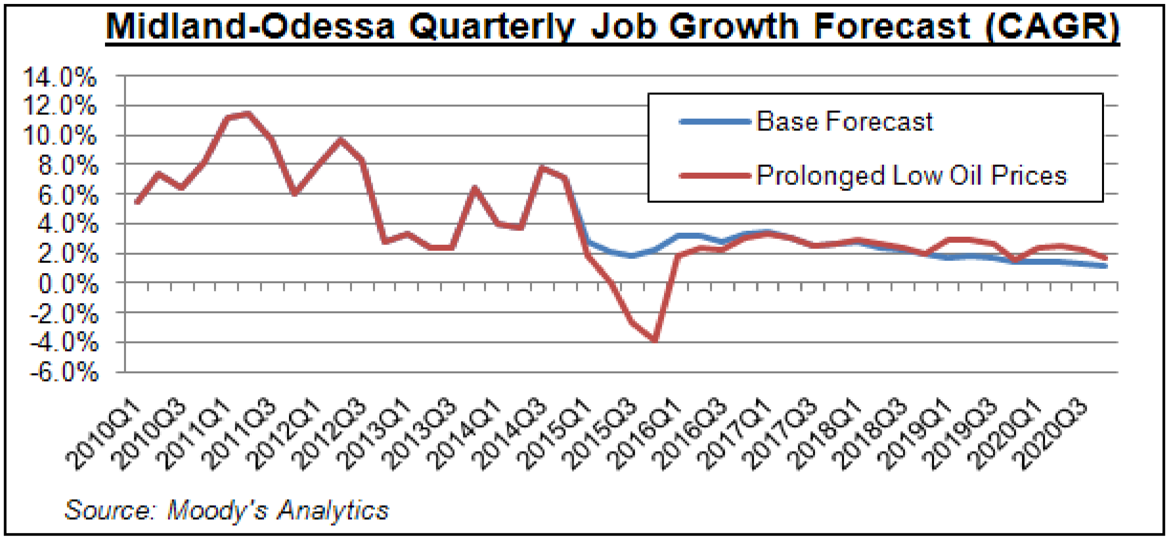
Slowdown in Midland-Odessa, Texas

Midland-Odessa has the highest concentration of oil and gas industry jobs in the country and, as a result, has been in the midst of an exceptional expansion for the past several years. The area's job market has grown by an average 6.4 percent per year since 2009—more than four times the national average.

This has been driven by the oil economy in the region, which has accounted for an estimated 40 percent of the 45,000 jobs created since 2009. Yet, during this period, apartment development has been unexpectedly muted. Since 2009, just 10 apartment projects have come online, accounting for 2,400 units. For context, there are an estimated 20,000 multifamily units in the Midland-Odessa area.

With falling oil prices, Midland-Odessa is poised for a significant slowdown, though calamitous conditions in the job and apartment markets are not expected. Moody's Analytics estimates that job growth in the area will remain positive, slowing to a still-respectable 2.2 percent this year compared to an enviable 5.6 percent in 2014, as seen in the chart below. Moody's Analytics provides an additional forecast that keeps oil prices low longer than expected, and even in that forecast Midland-Odessa's job market is forecasted to contract by just -1.2 percent in 2015, with job growth rebounding to 2.4 percent in 2016.

The base forecast for Midland-Odessa's job market results has real estate research firm Reis, Inc., anticipating that the metro's apartment market will see vacancy rise to 7.0 percent by year-end 2015, up from 6.1 percent in 2014, and rent growth remaining positive—though slowing—to an enviable 6.8 percent for 2015, down from 7.8 percent for 2014.



Keeping an Eye on Some Metros

Other mid-sized metro areas that have a concentration of oil jobs and could have some more trying times ahead include Lafayette, LA; Corpus Christi, TX; Oklahoma City; Shreveport, LA; and Bakersfield, CA. All of these metro areas have seen oil drilling jobs enhance their local economies over the past several years, and are poised to see that additional job growth diminish if oil prices remain low, especially over the long-term.

From a multifamily rental sector perspective, these metros are likely to see some softening conditions ahead but none of these locations have been hotbeds of apartment development activity, and the impact of a slowdown in oil jobs should not obliterate local apartment sector demand.

National Benefits and the Multifamily Sector

The rise in North American oil production and the recent drop in worldwide oil prices should be a benefit to consumers across the country. Greater disposable income would stimulate tourism, retail sales, and a diverse set of industries, allowing the national economy to potentially grow more than previously forecast, in turn bolstering a generally healthy national apartment market.

The fall in oil prices would be felt more acutely in just a few geographical areas and in certain local jobs. Fortunately, for most of these areas, the stimulus from oil production has simply enhanced an already healthy economy. The slowdown resulting from the drop in oil prices should not result in large-scale, metro-wide job losses, but rather should impact clusters of oil-dependent jobs. Local apartment markets, many of which were already poised for a rise in vacancy and an easing of rent growth, will likely see some additional softening, but this is not expected to be a significantly negative event for the nation's multifamily sector.

Kim Betancourt
Director of Economics

Tim Komosa
Economist Manager

Multifamily Economics and Market Research
April 2015

Opinions, analyses, estimates, forecasts and other views of Fannie Mae's Multifamily Economics and Market Research Group (MRG) 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 MRG 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 MRG represent the views of that group as of the date indicated and do not necessarily represent the views of Fannie Mae or its management.