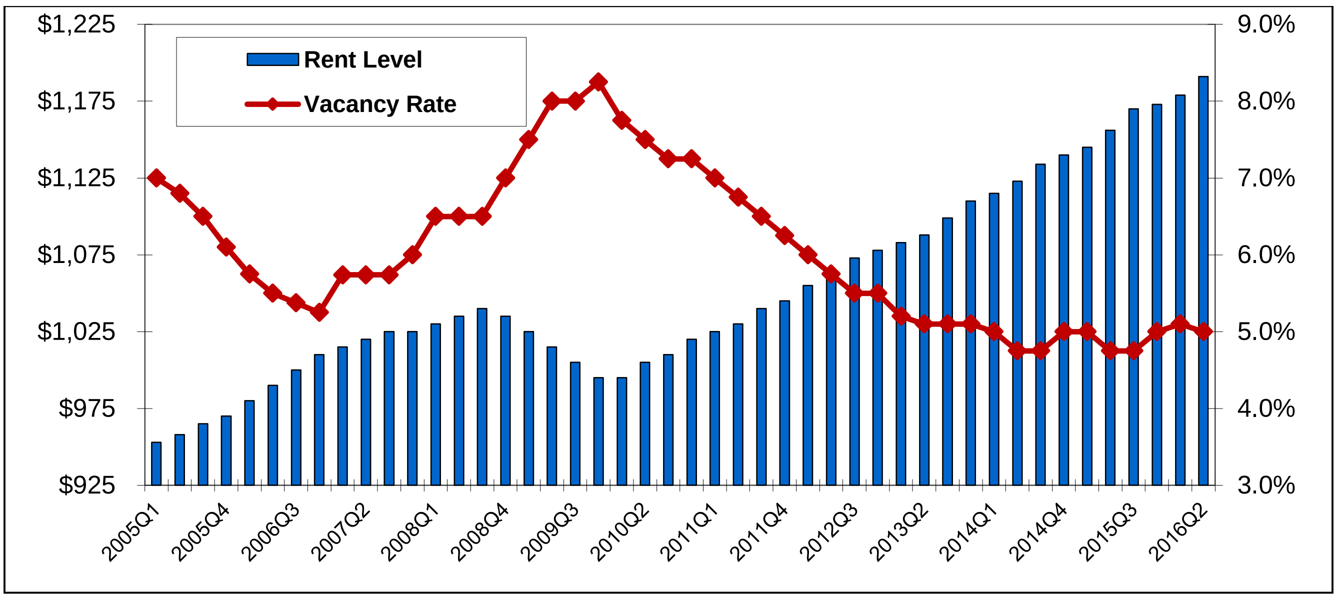
Multifamily Market Commentary – August 2016

Continued Demand for Multifamily in First Half of 2016

During the first half of 2016, the multifamily sector exhibited resiliency despite slowing fundamentals, according to preliminary third-party data. While low compared to the historical trend, the estimated 5.0 percent national multifamily rental vacancy level at the end of the first six months of the year was up from 4.75 percent one year earlier.

Estimated effective rents increased during the first six months of the year – by 1.5 percent. Rents have risen for 25 consecutive quarters. As newly constructed apartments coming online have increased in a number of submarkets across the country, demand has remained relatively healthy overall. However, it is important to note that demand is slowing.

Estimated National Rent Level and Vacancy Rate



Source: Fannie Mae Multifamily Economics and Market Research

First-Half Trends Reflect Slowing but Positive Demand

The vacancy rate rose somewhat during the first six months of 2016 and was higher year-over-year, while demand remained largely positive. Vacancies among institutional investment-type apartment properties declined slightly to an estimated 5.0 percent for the second quarter of 2016 – from 5.10 percent in this year's first quarter and returning to where they were in the fourth quarter of 2015.

Estimated rents rose by 1.0 percent in the second quarter of 2016 – the same rate as a year earlier. This was double the 0.5 percent estimate for the first quarter and a significant improvement from the 0.25 percent estimate for the fourth quarter of 2015. This resurgence in rent growth was somewhat of a surprise but reflects seasonal factors, such as people tending to move more in the spring and summer.

Trending suggests that multifamily rent growth could reach 3.0 to 3.5 percent by the end of 2016.

Net Absorption Also Slowing

Estimated net absorptions – indicating the net change in occupied rental units – were positive during the first half of the year, but at a lower level than one year earlier. For example, Reis estimated net absorption of 69,000 units during the first half of 2016 compared to an estimated 97,000 units during the first half of 2015.

The decrease in net absorption clearly indicates that demand has slowed. Dodge Data & Analytics construction pipeline data project an estimated 388,000 new multifamily rental units coming online this year, which would far exceed expected demand.

Vacancy Rates Still Declining in Some Metros, but Rising in Others

While demand for all types of rental housing has been healthy overall this year, demand is slowing in a number of metros. The number of metros with rising vacancy rates is on the rise, according to preliminary data from CBRE Econometric Advisors. The real estate research firm estimates that the vacancy rate fell in 33 out of 66 metros in this year's second quarter, while 28 metros saw vacancies rise and five metros remained the same.

Metros with the biggest declines in year-over-year vacancy rates in the second quarter, according to CBRE Econometric Advisors, included Norfolk, VA; Tucson, AZ; San Diego, Memphis, TN; Providence, RI; Richmond, VA; Birmingham, AL; and Louisville, KY. Metros with below 4.0 percent vacancy rates include Detroit; Oakland, CA; New York City; Newark, NJ; Long Island, NY; and Providence, which had the overall lowest rate of 2.7 percent.

The metros CBRE Econometric Advisors found had the most significant increases in vacancies in the second quarter included Denver; Hartford, CT; Honolulu; Oklahoma City; Pittsburgh; and San Jose, CA. All saw year-over-year increases of 100 basis points or higher.

Multifamily Demand Still Viable

We expect fundamentals to remain positive for the multifamily sector during the remainder of 2016. However, continued slowing in the pace of rent increases, softening net absorptions, and increased vacancy rates are likely. Fortunately, this scenario is not expected to last for very long – perhaps only 18 to 24 months. On a national level, we expect employment growth, solid demographic trends, and low homeownership rates to keep rent growth positive – at about 3.0 percent this year. We also expect the national multifamily rental vacancy rate will likely rise and possibly reach 5.5 percent by year's end.

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