Rent Survey | December 2016

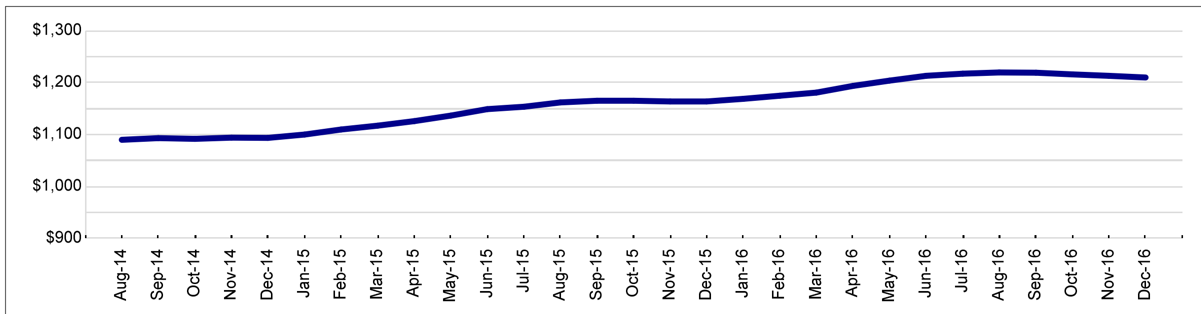
Multifamily Rents Finish 2016 Up 4%; Deceleration Continues

Average U.S. monthly rents dropped by $4 in December, as growth continues to cool. Rents fell to $1,210, according to Yardi Matrix's monthly survey of 124 markets. On a year-over-year basis, rents grew 4.0% nationwide in December, a 30-basis-point decline from November and a 270-basis-point drop from the recent high of 6.7% in October 2015.

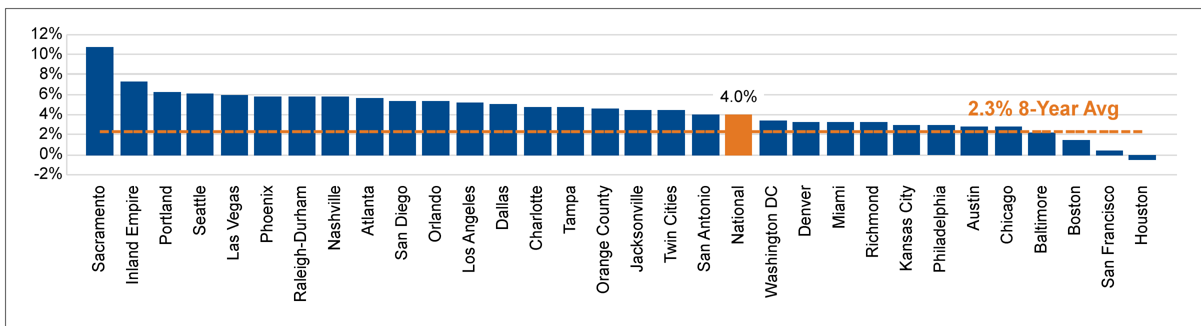
Rents have now dropped for four straight months, although the total decline is fairly minimal, only $10 total. Some of the drop can be attributed to normal seasonal factors, but it is clear that rents are in a period of deceleration after growing at high levels for the previous two years. Growth in some metros has flattened considerably—examples include Houston (-0.5% year-over-year), San Francisco (0.4%), Boston (1.5%), Austin (2.8%) and Miami and Denver (3.3%)—while in other metros it remains robust but not at the frothy levels of a year ago. Examples of metros in which growth has cooled but remains healthy include Portland (6.2% year-over-year), Seattle (6.1%), Atlanta (5.6%) and Dallas (5.1%).

As we have stressed in recent months, fundamentals remain sound and deceleration is not alarming, given that gains remain well above the long-term 2.3% average. The current level of growth is on par with our forecast for 3.9% increases in 2017. Clearly, this year remains difficult to predict, what with the prospect of major changes in taxes, tariffs, regulatory policy and foreign policy. That said, with the economy creating jobs at a 2 million-per-year rate and GDP growth showing strength, we expect no let-up in apartment absorption. We do expect rent growth to continue moderating during the first half of the year, as a large amount of new supply comes online and apartment owners must compete to maintain high occupancy levels. Growth should get a boost in the second half ,as the impact of economic stimulus takes effect and the increase in new supply begins to slow.

National Average Rents



Year-Over-Year Rent Growth—All Asset Classes



National averages include 119 markets tracked by Matrix, not just the 30 metros featured in the report. All data provided by YardiMatrix.

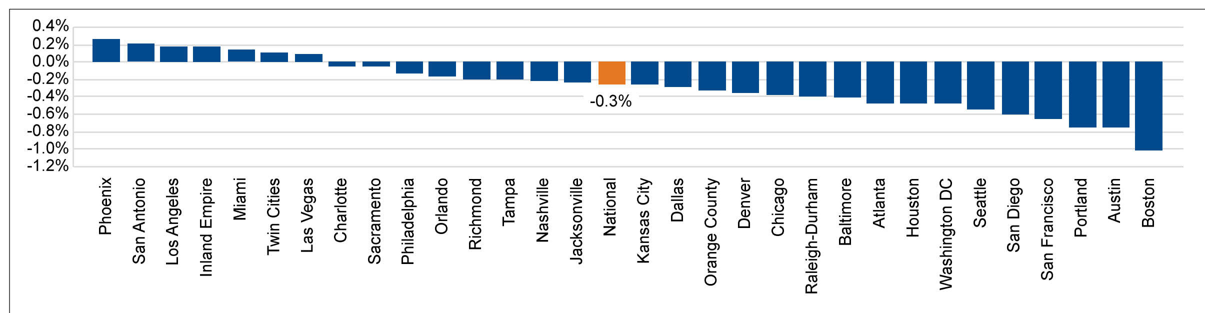
Trailing 3 Months: Seasonality Hits Short-Term Rent Growth

Nationally, multifamily rents fell 0.3% on a trailing three-month (T-3) basis in December, marking a 10-basis-point decline from November. The decline was concentrated in higher-end Lifestyle properties, where rents dropped 0.4%. Rents in the working-class Renter-by-Necessity (RBN) segment fell by 0.1%. The T-3 survey captures short-term changes in rents that may or may not be indicative of future trends. Seasonality has been less of a factor in recent years due to the atypical strength of the multifamily industry, so the end-of-year deceleration in 2016 seems to indicate a more normal environment.

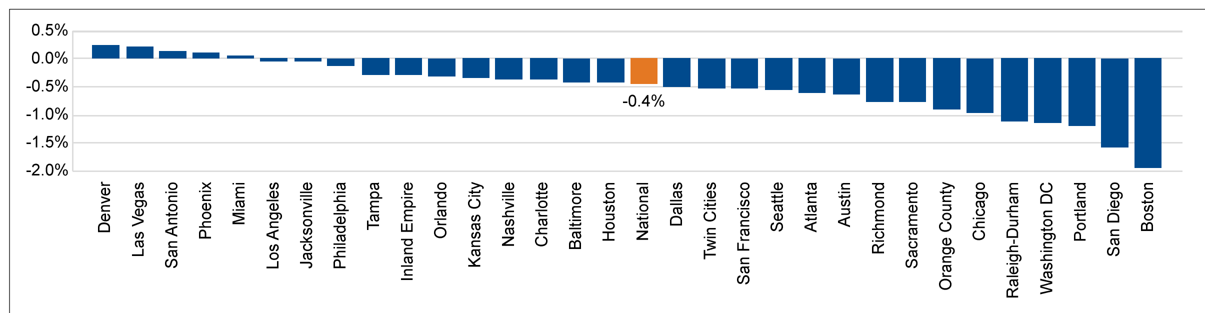
Leading T-3 markets were once again Sunbelt areas such as Phoenix (0.3%), San Antonio and Los Angeles (both 0.2%). The fastest-declining markets were Boston (-1.0%), Austin and Portland (both -0.8%), all markets that have had significant supply increases of late.

Comparing Lifestyle to RBN, Denver sticks out as the fastest-growing Lifestyle market in the country on a T3 basis (0.3%), while also being the fastest-declining market for RBN (-0.8%). Over the past year, Denver has seen significant rent growth among RBN units while Lifestyle units have flattened, and the recent reversal in the T3 data may be signs of a reversion to the mean for the whole market.

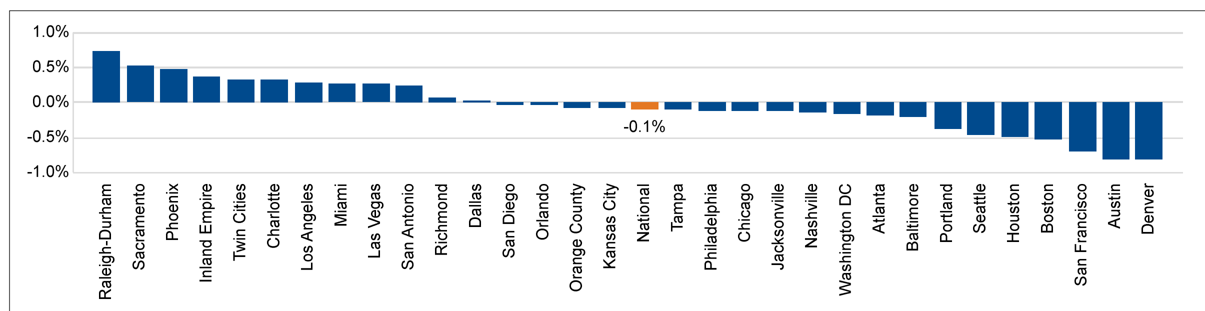
Trailing 3 Months Sequential—All Asset Classes



Trailing 3 Months Sequential—Lifestyle Asset Class



Trailing 3 Months Sequential—Renter-by-Necessity Asset Class

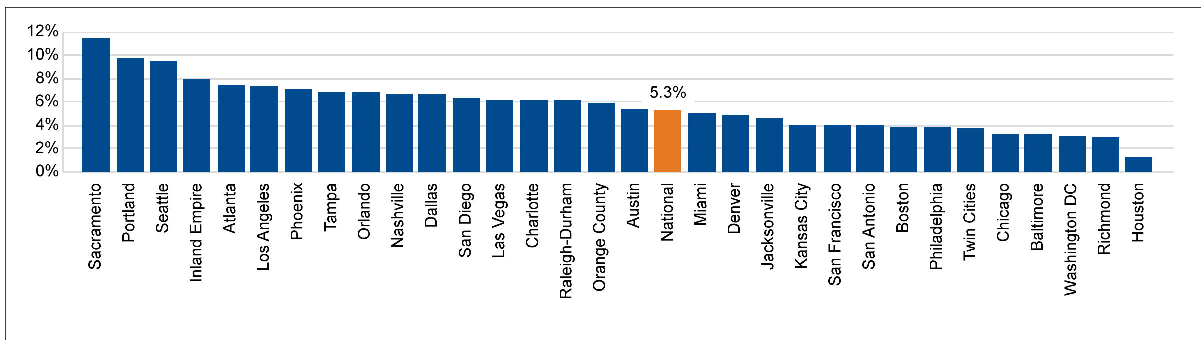


Trailing 12 Months: Growth Drops Another 20 Basis Points in T-12

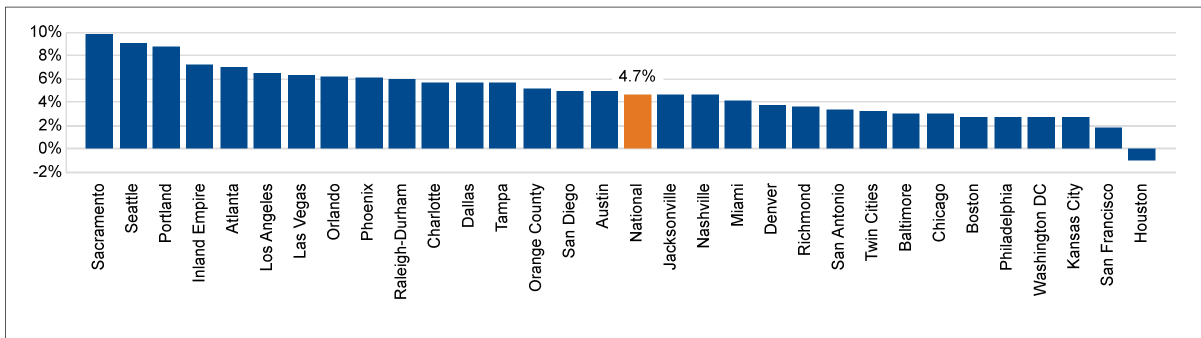
Rents grew at 5.3% on a trailing 12-month (T-12) basis in December, down 20 basis points from the previous month. Working-class Renter-by-Necessity properties once again led the gains, with 5.6% growth, compared to 4.7% for high-end Lifestyle assets. The T-12 survey represents the change in the average rent during the preceding one-year period compared to the previous one-year period.

Sacramento, with its limited supply and strong demand, continues to lead rent growth, increasing 11.4% on a T-12 basis. California's capital was also the best-performing market for Lifestyle (9.9%) and RBN (12.7%). Other West Coast markets round out the top 4 for overall T-12 rent growth, including Portland (9.8%), Seattle (9.5%) and the Inland Empire (8.0%). Houston remains at the bottom of the T-12 rankings, as the drop in energy employment that began in the fourth quarter of 2014 and the heavy supply pipeline continue to dampen rent growth. We expect the deceleration to continue in 2017, with forecast rent growth of 3.9%.

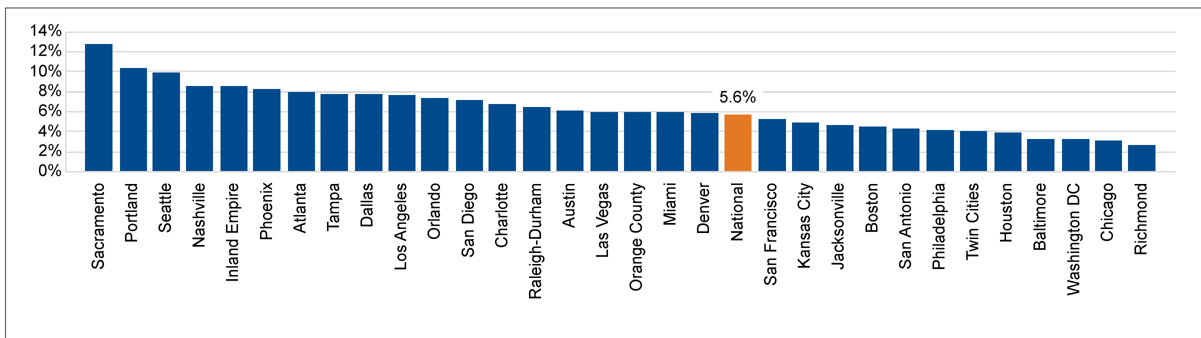
Trailing 12 Months Year-Over-Year—All Asset Classes



Trailing 12 Months Year-Over-Year—Lifestyle Asset Class



Trailing 12 Months Year-Over-Year—Renter-by-Necessity Asset Class



Employment, Supply and Occupancy Trends; Forecast Rent Growth

Changes in economic policy will no doubt be a major story in 2017, but as it applies to impact on multifamily property values, policy will take a back seat to the rise in interest rates. The 10-year Treasury rate increased nearly 70 basis points between the election and Christmas, as investors expect higher economic growth and more aggressive rate hikes from the Federal Reserve. Commercial real estate—both debt and equity—is benchmarked off the 10-year rate, so the change has major implications.

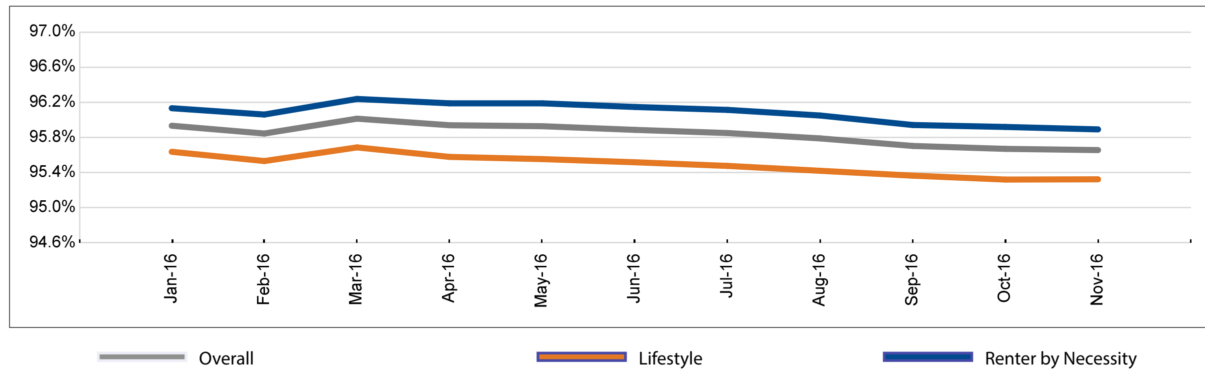
In order to quantify the effect on property values, Yardi Matrix conducted a study of the impact of higher interest rates on yields. The study examined the effect that the increased cost of debt (assuming loan spreads remain constant) would have on the cash flow and returns of different properties. What we found was that if cash flow and debt levels remain constant, a 50-basis-point increase in interest rates would reduce property values by nearly 6% and a 100-basis-point increase by 11%. However, the impact on values is mitigated by increases in cash flow. For example, a 50-basis-point increase in debt costs would be canceled out by a 5% increase in net income. The full details of the study will be published shortly, but the upshot is that rising rates will likely cut short the robust run-up in values that began in 2010, although the impact will be mitigated to the extent that fundamentals continue to improve. Our view is that the growth in multifamily values will be curtailed by the higher interest rate trend, but the market will benefit from ongoing moderate rent growth and continued demand from investors looking for safety and liquidity.

Market	Y-o-Y Job Growth (6-mo. moving avg.) as of October 2016	Completions as a % of Total Stock as of December 2016	Occupancy Rates as of October 2016	Occupancy Rates as of November 2016
Sacramento	2.6%	0.7%	96.7%	96.6%
Atlanta	2.8%	1.8%	95.1%	95.2%
Seattle	3.7%	4.9%	96.0%	95.9%
Inland Empire	2.5%	1.7%	96.5%	96.5%
Dallas	3.5%	2.2%	95.8%	95.8%
Portland	2.9%	3.0%	95.9%	95.8%
Orange County	2.8%	1.4%	96.8%	96.9%
San Diego	2.3%	2.3%	97.0%	97.0%
Las Vegas	2.4%	1.1%	95.1%	95.1%
Nashville	3.0%	3.9%	96.2%	96.3%
Raleigh-Durham	2.6%	2.0%	NULL	NULL
Charlotte	2.4%	5.2%	96.1%	96.0%
Phoenix	2.7%	2.9%	95.1%	95.0%
Orlando	3.9%	3.3%	96.0%	96.0%
Austin	3.3%	5.3%	95.4%	95.4%
Los Angeles	2.0%	2.3%	96.8%	96.8%
Tampa	2.9%	1.4%	95.3%	95.3%
Washington, D.C.	2.3%	2.4%	96.0%	96.0%
Richmond	1.7%	0.9%	95.3%	95.3%
Jacksonville	3.9%	1.3%	95.1%	95.0%
Twin Cities	1.7%	1.4%	97.8%	97.7%
Denver	3.3%	4.4%	95.4%	95.4%
Kansas City	1.2%	2.0%	95.3%	95.3%
Chicago	1.2%	2.2%	95.7%	95.7%
San Antonio	2.1%	3.9%	94.5%	94.5%
Miami	2.5%	3.2%	95.6%	95.6%
Philadelphia	2.1%	1.5%	96.1%	96.2%
Baltimore	2.0%	1.4%	95.4%	95.4%
Boston	1.8%	2.7%	96.7%	96.7%
San Francisco	2.9%	1.7%	96.2%	96.2%
Houston	0.4%	3.0%	93.5%	93.5%

Occupancy and Asset Classes

The occupancy rate for stabilized properties nationally was unchanged at 95.7% in November. Renter-by-Necessity properties remained at 95.8%, while Lifestyle occupancy was unchanged at 95.5%. Occupancy has remained stable for the past year, although it has declined by about 30 basis points in all three categories since peaking in March 2016.

Occupancy—All Asset Classes by Month

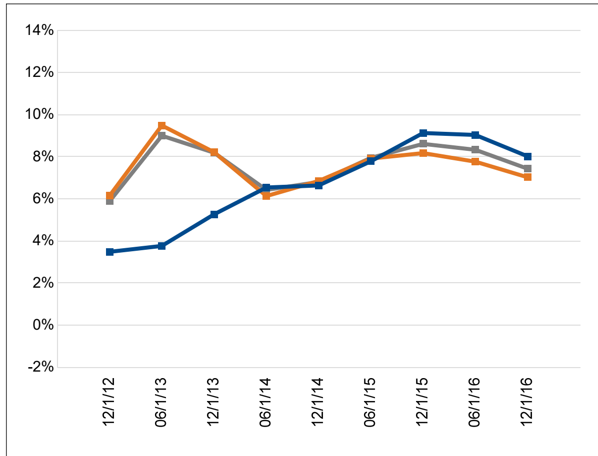


Year-Over-Year Rent Growth, Other Markets

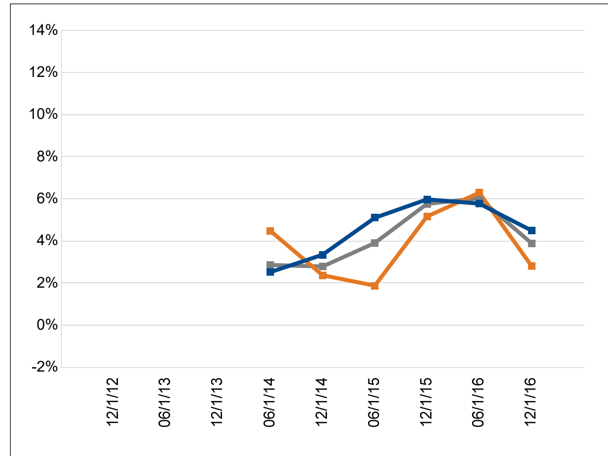
Market	December 2016		
	Overall	Lifestyle	Renter by Necessity
Tacoma	12.9%	13.7%	11.6%
Reno	9.6%	10.9%	8.1%
Colorado Springs	8.9%	9.9%	7.7%
Central Valley	7.6%	8.3%	3.6%
San Fernando	6.0%	6.1%	7.0%
Tucson	4.5%	3.7%	7.3%
Long Island	4.1%	4.0%	5.2%
Northern New Jersey	3.9%	2.9%	5.1%
SW Florida Coast	3.9%	4.6%	3.1%
NC Triad	3.8%	4.4%	3.1%
Indianapolis	2.9%	3.2%	2.6%
St. Louis	2.9%	2.8%	3.7%
Albuquerque	2.7%	3.2%	2.1%
Louisville	2.3%	2.3%	2.7%
Central East Texas	2.2%	2.0%	3.9%
Bridgeport - New Haven	1.1%	1.9%	-0.3%
El Paso	0.0%	0.0%	-0.1%

Market Rent Growth by Asset Class

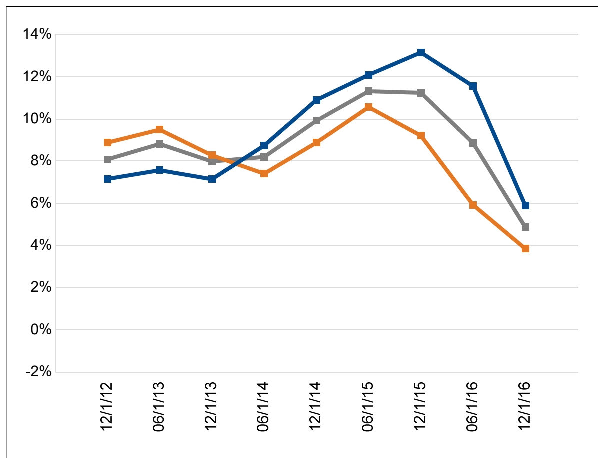
Atlanta



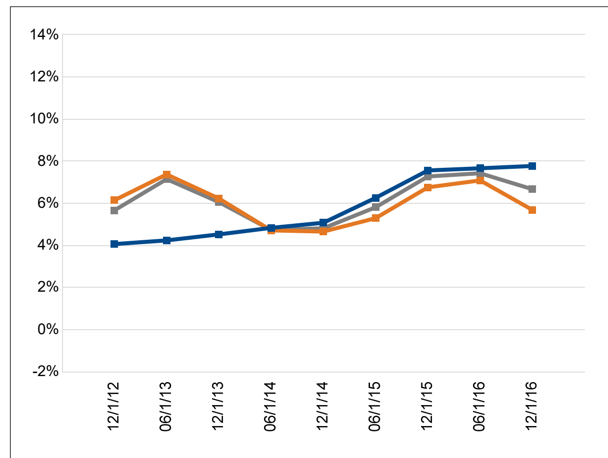
Boston



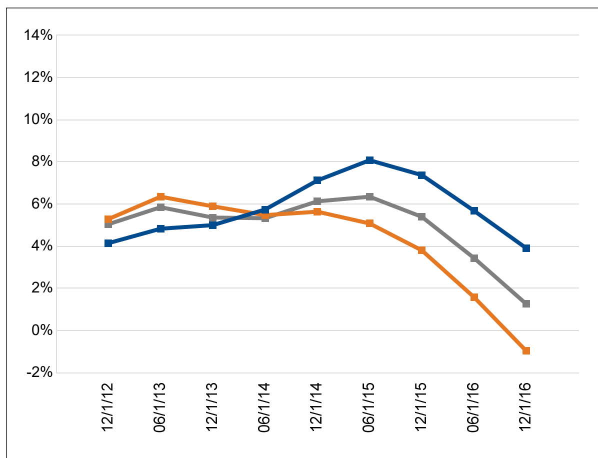
Denver



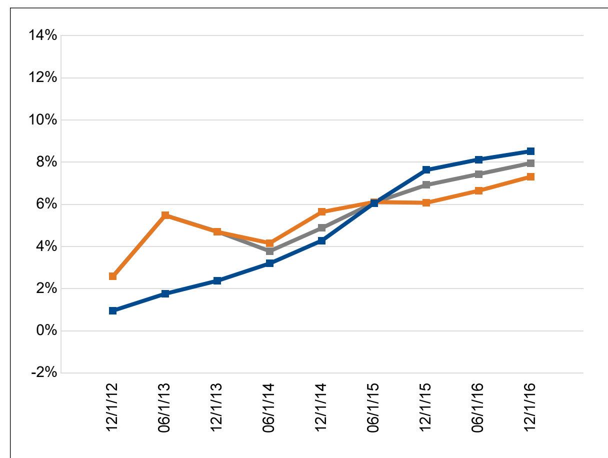
Dallas



Houston

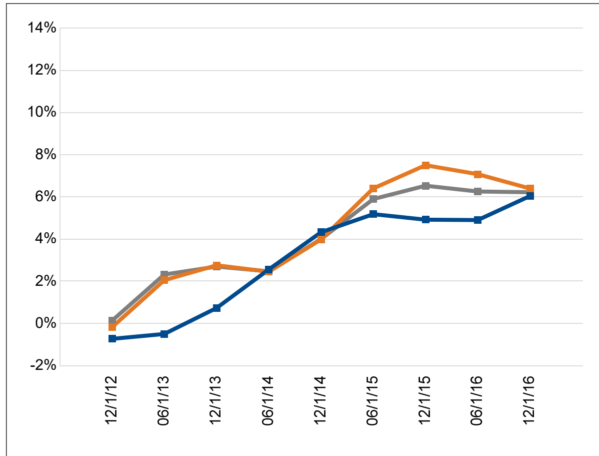


Inland Empire

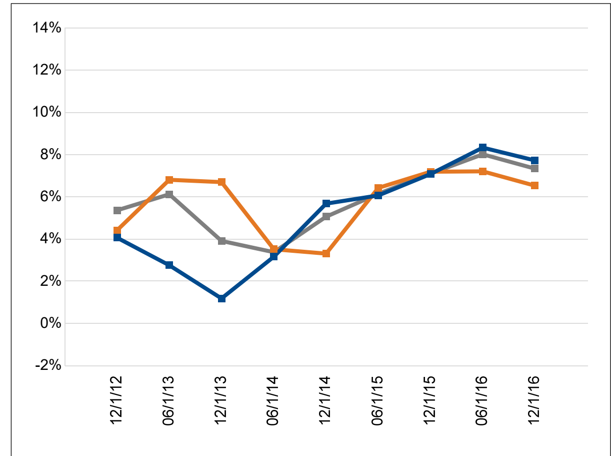


Trailing 12 Months Overall Trailing 12 Months Lifestyle Trailing 12 Months Renter by Necessity

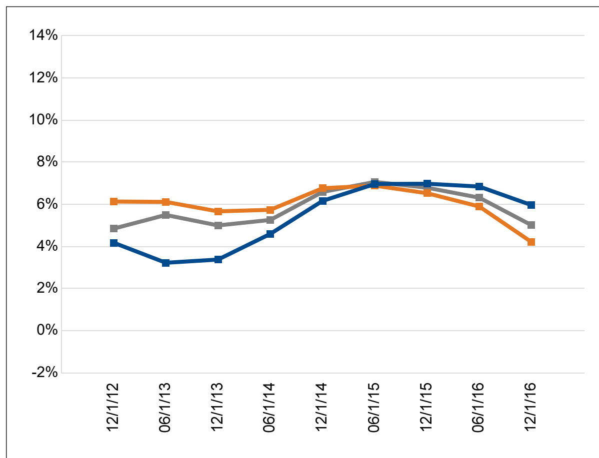
Las Vegas



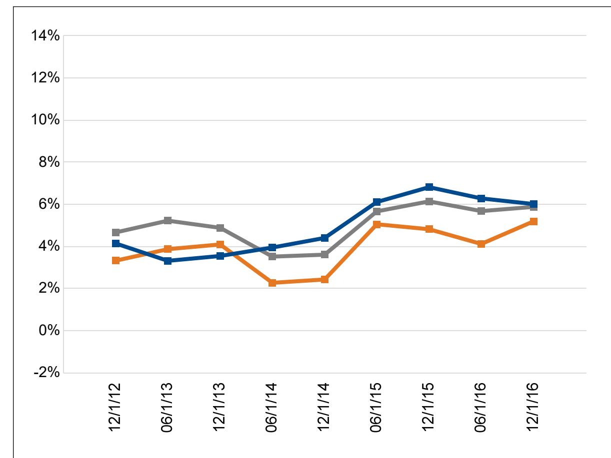
Los Angeles



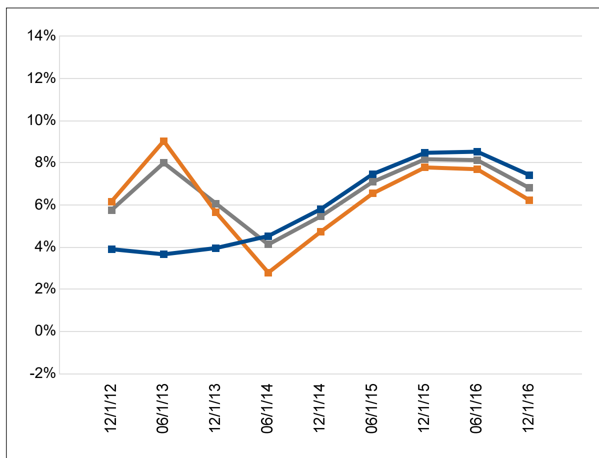
Miami



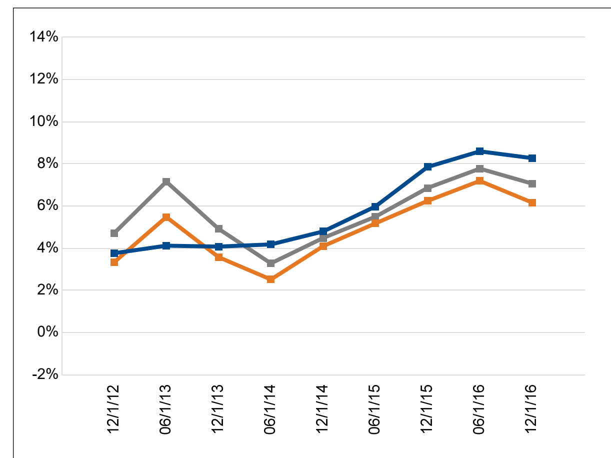
Orange County



Orlando

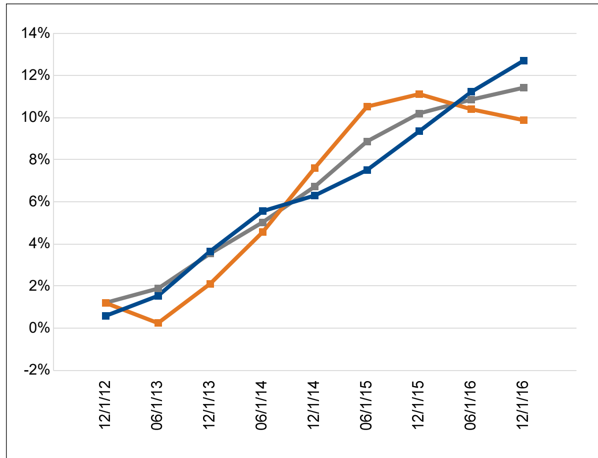


Phoenix

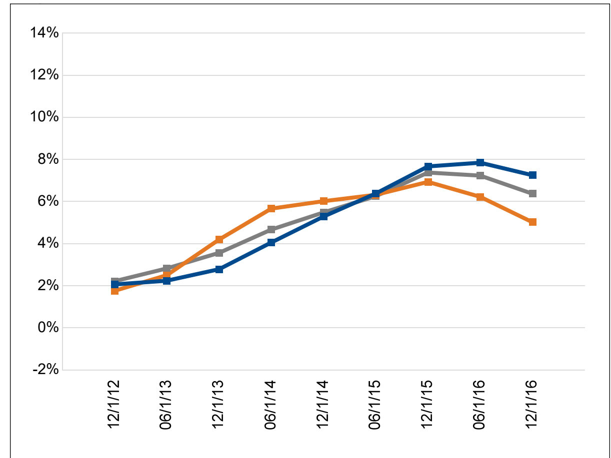


Trailing 12 Months Overall
Trailing 12 Months Lifestyle
Trailing 12 Months Renter by Necessity

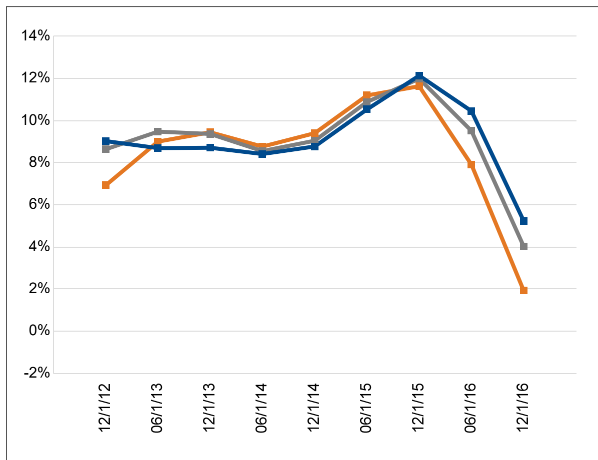
Sacramento



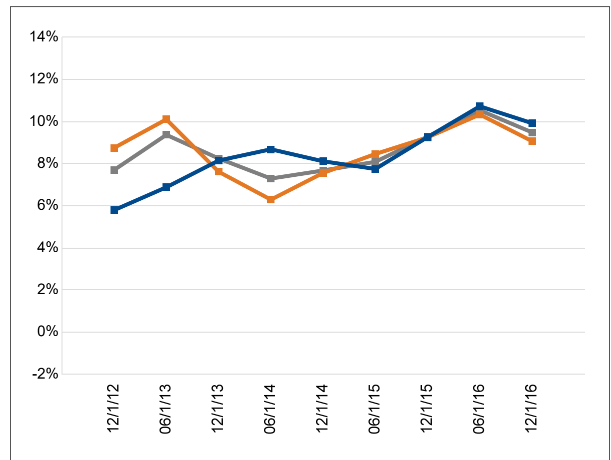
San Diego



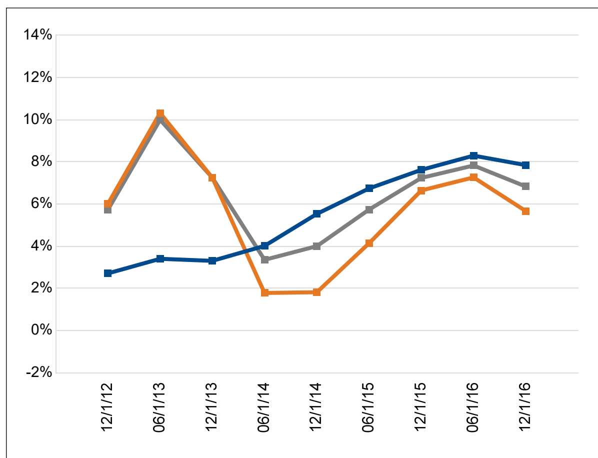
San Francisco



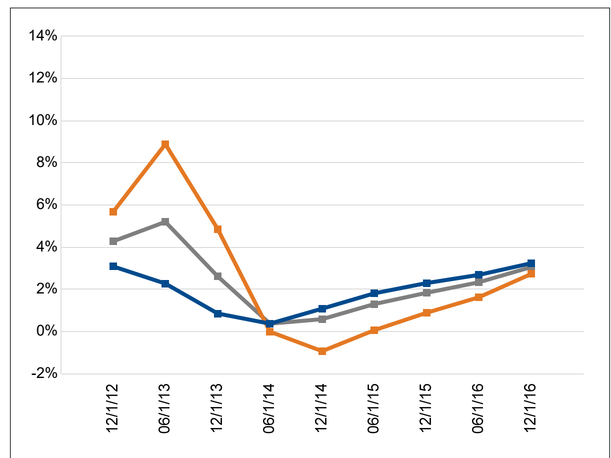
Seattle



Tampa



Washington, D.C.



Trailing 12 Months Overall — Trailing 12 Months Lifestyle — Trailing 12 Months Renter by Necessity

Definitions

Lifestyle households (renters by choice) have wealth sufficient to own but have chosen to rent. Discretionary households, most typically a retired couple or single professional, have chosen the flexibility associated with renting over the obligations of ownership.

Renter-by-Necessity households span a range. In descending order, household types can be:

- *A young-professional, double-income-no-kids household* with substantial income but without wealth needed to acquire a home or condominium;
- *Students*, who also may span a range of income capability, extending from affluent to barely getting by;
- *Lower-middle-income ("gray collar") households,* composed of office workers, policemen, firemen, technical workers, teachers, etc.;
- *Blue-collar households*, which may barely meet rent demands each month and likely pay a disproportionate share of their income toward rent;
- *Subsidized households*, which pay a percentage of household income in rent, with the balance of rent paid through a governmental agency subsidy. Subsidized households, while typically low income, may extend to middle-income households in some high-cost markets, such as New York City;
- *Military households*, subject to frequency of relocation.

These differences can weigh heavily in determining a property's ability to attract specific renter market segments. The five-star resort serves a very different market than the down-and-outer motel. Apartments are distinguished similarly, but distinctions are often not clearly definitive without investigation. The Yardi® Matrix Context rating eliminates that requirement, designating property market positions as:

Market Position	Improvement Ratings
Discretionary	A+ / A
High Mid-Range	A- / B+
Low Mid-Range	B / B-
Workforce	C+ / C / C- / D

The value in application of the Yardi® Matrix Context rating is that standardized data provides consistency; information is more meaningful because there is less uncertainty. The user can move faster and more efficiently, with more accurate end results.

The Yardi® Matrix Context rating is not intended as a final word concerning a property's status—either improvements or location. Rather, the result provides reasonable consistency for comparing one property with another through reference to a consistently applied standard.

To learn more about Yardi® Matrix and subscribing, please visit www.yardimatrix.com or call Ron Brock, Jr., at 480-663-1149 x2404.

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