



RENTAL HOUSING



The share of US households that rent their housing now stands at a 20-year high. While most of the recent increase in the stock has come from conversion of owner-occupied single-family homes to rentals, multifamily construction has also picked up pace. Meanwhile, falling vacancy rates have lifted rents, improving the financial performance of rental properties but straining the budgets of millions of households unable to find units they can afford.

RECORD GROWTH IN DEMAND

Although estimates vary, the major Census Bureau surveys agree that 2014 marked the 10th consecutive year of robust renter household growth. By the Housing Vacancy Survey's count, the pace of growth accelerated to an average of 900,000 annually in 2010–14. This puts the 2010s on track to be the strongest decade for renter growth in history (**Figure 29**).

Part of the extraordinary growth in rental demand has come from households in certain age, income, and family groups that are traditionally more likely to own. While younger adults are most likely to rent their housing, the number and share of older renters have risen significantly over the last decade with the changing age distribution of the population. Although making up just 25 percent of renters in 2014, households aged 55 and over contributed fully 42 percent of renter household growth over the preceding decade (**Figure 30**). Within the 55–64 year-old age group, population growth drove more than half of the increase in renters while declines in homeownership were responsible for the remainder. Within the 65-and-over age group, however, population growth alone accounted for all of the growth in renter households.

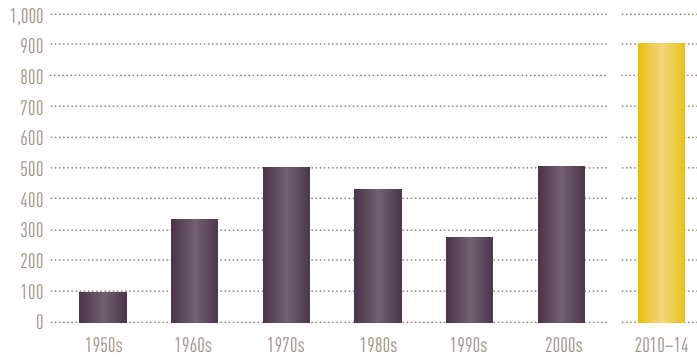
The income distribution among renter households is also shifting. After a net decline in 1994–2004, households in the highest income quartile accounted for almost one in five net new renters in 2004–14, and nearly one in three net new renters in 2011–14. While some of these upper-income renters may have faced economic challenges that prevented them from attaining or maintaining homeownership, more were simply opting to rent rather than own their housing. Even so, only 11 percent of renters were in the top income quartile in 2014, and nearly 40 percent were in the bottom income quartile.

While single persons still make up the largest share of renter households, the numbers of renters of all family types rose over the decade. The reasons for these increases differ, however. For example, growth in the number of single-person renters primarily reflects growth in the overall number of single-person households. In contrast, growth in the number of married-couple renters—particularly those with children—is due primarily to higher rentership rates. Regardless of the reasons, though, all

FIGURE 29

So Far in the 2010s, Annual Renter Household Growth Has Outstripped the Pace in Any Previous Decade

Average Annual Change in Renter Households (Thousands)



Source: JCHS tabulations of US Census Bureau, Decennial Censuses and Housing Vacancy Surveys.

of these changes in the characteristics of renters have served to increase the diversity of an already diverse set of households.

CONTINUED STRENGTH OF MULTIFAMILY CONSTRUCTION

With rental housing demand still on the rise, construction of multifamily units continued to ramp up last year. From a historic low of just under 110,000 in 2009, the number of multifamily starts rose steadily to nearly 360,000 units in 2014—more than in any year in the 1990s or 2000s. And in a marked shift, more than 90 percent of multifamily units started last year were intended for the rental market, up from less than 60 percent in the mid-2000s. Indeed, starts of multifamily rentals in 2014 hit their highest level since 1987 (Figure 31).

Meanwhile, the number of rental units completed last year was well below the number of starts, at just 280,000. With the long lag between starts and completions, the pipeline of new rental housing will continue to fill over the next few years. As a result, the number of new rental units brought to market will continue to rise even if starts level off.

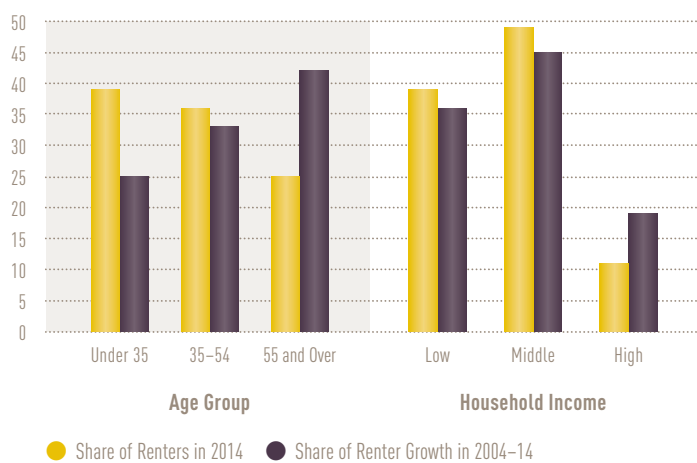
Although the growing supply of multifamily housing will help to meet soaring demand, new units are primarily built for the high end of the market. In 2013, the median asking rent for newly constructed multifamily units was \$1,290, equivalent to about half of the median renter’s monthly household income. At that rent level, over two-thirds of today’s renter households could not afford this new unit at the traditional 30-percent-of-income standard.

The rebound in multifamily construction activity is evident in markets across the country. Over the past year, 18 of the top 25 metros issued more multifamily permits than in an average year in the 2000s. The increases in Chicago, Houston, and Phoenix were particularly large, with permitting of at least 50 percent more multifamily units than in 2013. Over the past five years, however, Austin, San Jose, and Nashville have led the list of metros for growth, with annual permitting of at least 30 percent more units than the 2000s average.

FIGURE 30

Older and Higher-Income Households Have Increasingly Turned to Renting

Percent



Note: Low/middle/high household incomes are in the bottom/middle/top quartiles based on equal fourths of all households. Source: JCHS tabulations of US Census Bureau, Current Population Surveys.

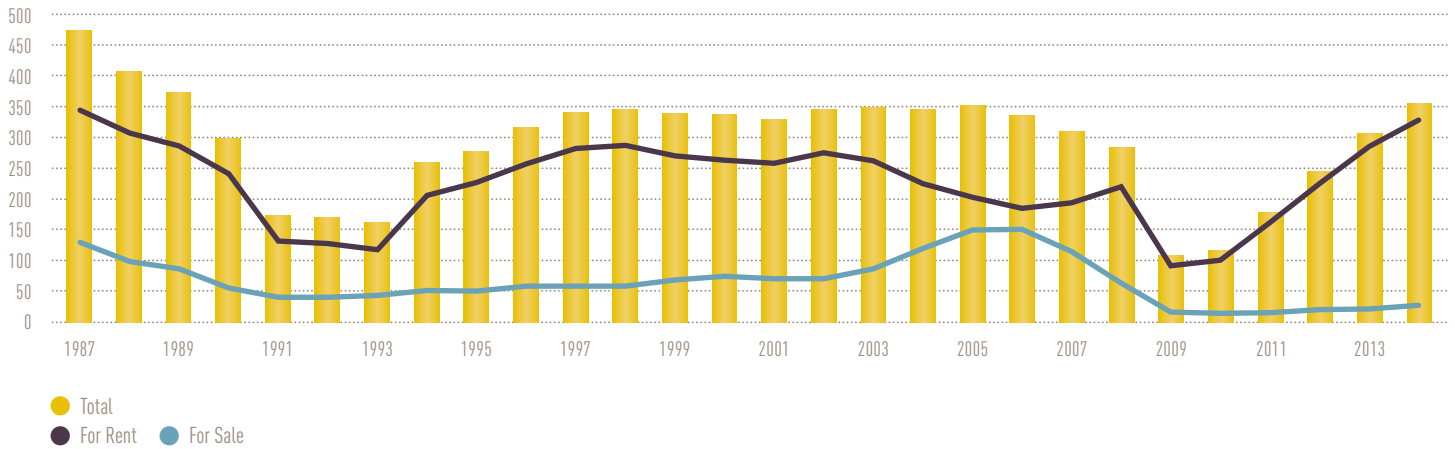
EXPANDED ROLE OF SINGLE-FAMILY RENTALS

Single-family rentals have absorbed an increasingly large share of renter household growth since the mid-2000s. Indeed, after averaging just 73,000 units annually in the 1990s, growth in the number of occupied single-family rentals accelerated to 138,000 units per year in the early 2000s. But by the end of the decade, the number of single-family rentals was increasing at an average annual rate of some 513,000 units (Figure 32). According to the American Community Survey, the number of renters in single-family detached homes increased by 3.2 million on net between the homeownership rate peak in 2004 and 2013, accounting for nearly half of the gain in rentals. In contrast, large multifamily buildings (with five or more units) housed about one-third of net new renters over this period, while attached single-family

FIGURE 31

Multifamily Construction Has Recovered to Pre-Crisis Levels, Driven Almost Entirely by Rentals

Multifamily Starts (Thousands of units)

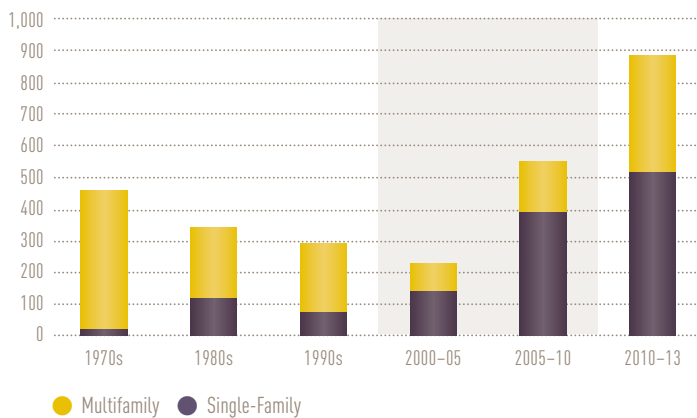


Source: JCHS tabulations of US Census Bureau, Surveys of Construction.

FIGURE 32

The Recent Growth of Single-Family Rentals Is Unprecedented

Average Annual Change in Occupied Rental Units (Thousands)



Note: Data exclude mobile homes.

Source: JCHS tabulations of US Census Bureau, Decennial Censuses and American Community Surveys.

units and small multifamily structures (with two to four units) accounted for another 13 percent.

A major factor behind the recent growth of single-family rentals is the surge in single-family development in the 1990s and 2000s. More than 12 million single-family homes were added in the 2000s alone, the highest level in any decade since the 1970s. When rental demand began to climb after the housing bust,

conversions of owner-occupied single-family homes to rentals accommodated much of this growth. These shifts also helped to stabilize for-sale markets, especially in the Sunbelt metros with the largest inventories of distressed and vacant single-family homes.

While the single-family sector has traditionally housed about 30 percent of the nation's renters, its share of the market now stands at 35 percent. This increase brings the number of households living in single-family rentals to 14.8 million. Including mobile homes, single-family housing makes up nearly 40 percent of the overall rental stock and provides homes for 16.7 million households. At the state level, the single-family share of rentals ranges widely from nearly half in Oklahoma, Kansas, and Idaho to less than a fifth in New York, Massachusetts, Rhode Island, and Washington, DC.

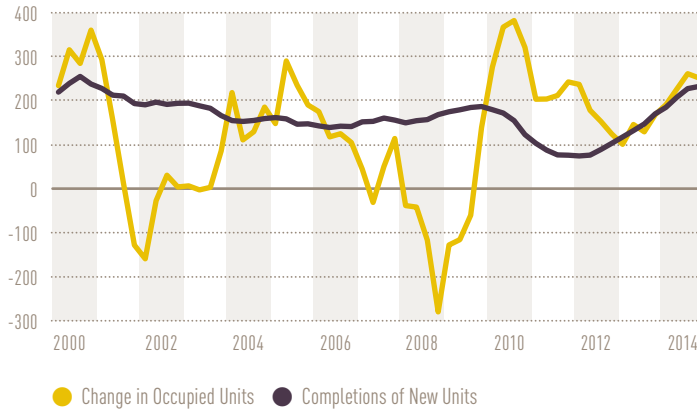
In general, the single-family rental stock differs from the owner-occupied inventory in age, size, and location. The typical single-family rental unit is 10 years older and 26 percent smaller than the typical owner-occupied home. Single-family rentals are also more likely to be found in urban neighborhoods, with more than 30 percent located in center cities, compared with about 20 percent of owner-occupied single-family homes.

The renters of single-family homes are much like renters everywhere, although they are more apt to be middle-aged. They are also more likely to be married couples with children, as well as married couples without children and single-parent families. Persons living alone, however, do make up a sizable share (21 percent) of single-family renters. Finally, white households are more apt to rent single-family homes than minority households. Indeed, 38 percent of white renters live in single-family units,

FIGURE 33

Apartment Supply and Demand Continue to Rise in Tandem

Annual Change (Thousands)

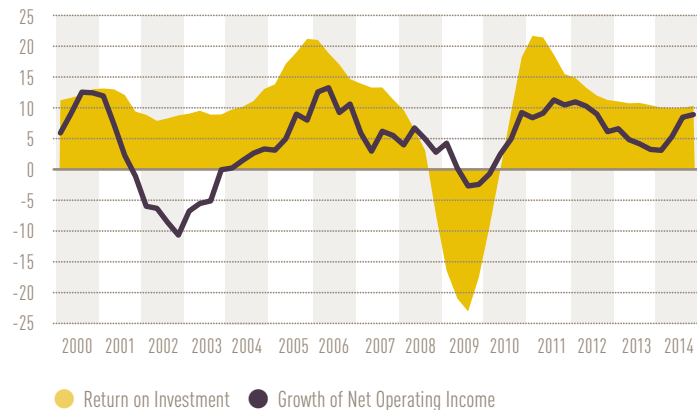


Note: Data are for investment-grade multifamily properties.
Source: JCHS tabulations of MPF Research data.

FIGURE 34

Rental Properties Have Generated Solid Returns Since Mid-2010

Annual Rate (Percent)



Notes: Data are for investment-grade multifamily properties. Net operating income is defined as gross rental income plus any other income less operating expenses.
Source: JCHS tabulations of National Council of Real Estate Investment Fiduciaries (NCREIF) data.

compared with 33 percent of Hispanic renters, 32 percent of black renters, and 28 percent of Asian/other renters.

TIGHTENING MARKETS

Rental markets tightened again in 2014 as the national vacancy rate fell by nearly a full percentage point to 7.6 percent—its lowest point in two decades. Data from MPF Research show that the vacancy rate for professionally managed properties with five or more apartments was even lower, averaging 4.6 percent for the year and running at a rate not seen since before the housing market downturn.

Rental markets are particularly tight at the low end. According to JCHS tabulations of Housing Vacancy Survey data, the number of vacant units with rents under \$800 per month dropped some 12 percent between 2013 and 2014—contributing more than 90 percent of the decline in rental vacancies.

Meanwhile, new construction of professionally managed apartments has not quite kept up with demand (Figure 33). At the end of 2013, new apartments were coming on line at an annual rate of 170,000 units, essentially matching the pace of growth in tenants. By the end of 2014, though, new apartment additions increased to 232,000 units a year while net growth in tenants hit 252,000.

With demand rising and vacancies declining, rents came under increasing pressure last year. The consumer price index for contract rents climbed 3.2 percent in 2014, the largest increase since 2008 and double the overall inflation rate of 1.6 percent. Rents for professionally managed properties were up even more sharply, with the annual increase rising from 3.0 percent in 2013 to 3.8 percent in 2014. Indeed, rent increases picked up pace in the fourth quarter, hitting a 4.6 percent year-over-year rate even as overall inflation cooled.

All but 2 of the 93 metro areas tracked by MPF Research saw rents rise last year. Increases were at least 4 percent in more than a third of metros and at least 3 percent in just under half. At the high end, rents in San Jose, Honolulu, San Francisco, and Denver rose 10 percent or more in 2014.

The 20 hottest rental markets (where rents rose more than 5 percent last year) were all located in the West or South. Rent increases in metros of the Northeast and Midwest were more modest, with only a few major areas—including Boston and Chicago—registering a rise of more than 3 percent.

Occupancy rates were high in the majority of markets where rents were increasing the fastest. At year end, the rental occupancy rate in 2014 exceeded 95 percent in well over half of the 20 hottest markets. Occupancies edged up slightly in the already tight New York and Portland markets, to the 97–98 percent range, but jumped by more than a percentage point in Indianapolis, Cleveland, Phoenix, and Sacramento. In contrast,

rental occupancy rates in Charlotte, Austin, and Miami fell slightly despite a solid increase in rents.

STRONG PERFORMANCE OF APARTMENT PROPERTIES

Apartment properties performed well again in 2014. The National Council of Real Estate Investment Fiduciaries reports that the net operating income of commercial-grade apartment buildings rose an impressive 9 percent last year, far exceeding the 6 percent annual average over the preceding decade (Figure 34).

Apartment prices, as measured by Moody's/RCA Commercial Property Price Index, also rose 15 percent in 2014—the fifth consecutive year of strong growth. These consistent price gains make 2011–14 comparable in strength to 2004–05, the height of the last real estate cycle. Based on changes in net operating incomes as well as property values, the annual rate of return for commercial-grade properties came in at 10 percent last year, much the same as in 2013.

Strong market fundamentals and low interest rates helped to drive growth in multifamily lending, pushing the Mortgage Bankers Originations Index up 15 percent for 2014 as a whole and 39 percent in the fourth quarter alone. Total loans outstanding (including both originations and repayment/writeoffs of existing loans) rose by \$60 billion, led by a \$35 billion jump in loans held by banks and thrifts. While this increase brought the bank and thrift share back to its pre-crisis average of 30 percent, federal sources still hold or guarantee fully 44 percent of mortgage debt outstanding.

Meanwhile, multifamily loan delinquencies continue their decline. In the fourth quarter of 2014, the share of seriously delinquent multifamily loans (at least 90 days past due) at FDIC-insured institutions dipped below 0.5 percent, approaching average levels before the mortgage crisis. The delinquency rate for commercial/multifamily loans held by life insurance companies was even lower, at less than 0.1 percent.

The share of multifamily loans held in commercial mortgage backed securities (CMBS) that were at least 60 days past due, in foreclosure, or REO also fell in 2014. But even after four consecutive years of declines, the share still stood at 8.6 percent—well above the pre-crisis average of less than 1.0 percent. Similarly, delinquency rates for multifamily loans backed by Freddie Mac and Fannie Mae also declined last year, but to levels that were even below average in the early 2000s.

THE OUTLOOK

Rental markets continue to adapt to the unprecedented surge in demand that began in the mid-2000s. Although initially ignited by the bust in housing and mortgage markets, rental growth is likely to remain strong as members of the huge millennial population enter the housing market. According to the latest JCHS projections, individuals that are currently under age 30 will form over 20 million new households between 2015 and 2025, and most of these households will be renters. There will also be a large increase in renters over age 65 as more members of the large baby-boom generation cross this threshold over the coming decade.

To keep rents from rising even more sharply, it will be essential to ensure that an adequate supply of rental housing is available to accommodate this upcoming wave of demand. To that end, the growing pipeline of new multifamily rentals is a positive trend. Of course, some markets could face an oversupply of rental units if the ramp-up in multifamily construction goes on for too long. So far, though, there is no evidence that this is an imminent threat.

The rental market plays a critical role in meeting the housing needs of an expanding mix of households. Even so, rental housing continues to be home to a large majority of the nation's low-income households, challenging the market's ability to provide good-quality units that are within financial reach of renters of modest means. Closing the gap between what it costs to produce this housing and what economically disadvantaged households can afford to pay requires the persistent efforts of both the public and private sectors.