



Rental Housing

Although slowing, renter household growth continued to soar in 2013. The strength of demand has kept rental markets tight across the country, pushing up rents and spurring new construction. But supply and demand now appear to be coming into balance. With slower renter growth likely ahead and many new apartments in the pipeline, rent increases should begin to ease.

CONTINUED STRONG DEMAND

According to the Housing Vacancy Survey, the number of renter households was up by more than half a million in 2013. At the same time, the Current Population Survey reports that renter household growth was twice that pace. Regardless of this wide discrepancy, both surveys put renter growth well above the 400,000 annual average of the last few decades. Moreover, both sources also indicate that increases in renter households slowed as the homeownership rate declines eased at the end of 2013.

A variety of household types has shifted to rentals in recent years. Along with the groups that are most apt to rent—younger adults, low-income households, and single persons—many older households, higher-income earners, and families with children also contributed to the growth in renters. For example, while households under age 35 accounted for a quarter of renter growth in 2005–13, the share for 55–64 year olds is nearly as large (**Figure 23**). This reflects both the movement of the baby-boom generation into this age group and the drop in homeownership among these households. Meanwhile, households aged 35–44 and 45–54 each accounted for nearly a fifth of the growth in renters, driven largely by their sharply lower homeownership rates.

With the recession expanding the ranks of lower-income households, it is no surprise that this group accounted for much of the increase in renters. Indeed, more than a quarter of renter growth was among households earning under \$15,000 annually, and nearly 30 percent among those with incomes of \$15,000–29,999. At the same time, though, highest-income households accounted for nearly as large a share (23 percent) as lowest-income households. And while many new renters were single persons, families with children—including both single parents and married couples—were responsible for a slightly larger share of the increase because they experienced the biggest falloff in owning.

TIGHTER RENTAL MARKETS

With the continued strength of demand, the national rental market tightened further in 2013. According to Census Bureau estimates, the rental vacancy rate edged down to 8.3 percent

and stood at its lowest point since 2000. Even so, last year's decline was the smallest since vacancies began their retreat in 2010. Meanwhile, MPF Research reports that by the fourth quarter of 2013, the vacancy rate for professionally managed apartments was 5.0 percent, virtually unchanged since late 2011.

Rent increases have also remained fairly consistent. The consumer price index (CPI) for contract rents indicates that nominal rents were up 2.8 percent in 2013, little changed from 2012. Among professionally managed properties with five or more units, rent increases slowed from 3.7 percent in 2012 to 3.0 percent last year. But by either measure, rents still rose at a healthy clip, outpacing the overall inflation rate of 1.5 percent.

The tightening in rental markets was widespread, with 85 of the 93 metropolitan areas tracked by MPF Research reporting higher rents. In many metros, however, the pace of increases slowed. Rents in over 40 percent of these metro areas rose at least 3.0 percent in 2012, but that share was less than a third in 2013 (**Figure 24**). And in a quarter of metro markets, rent increases did not beat the national rate of inflation.

SUPPLY CATCHING UP WITH DEMAND

Construction of multifamily housing ramped up steadily from a low of 109,000 starts in 2009 to more than 300,000 in 2013—just 13 percent fewer starts than at the 2005 peak. Over 90 percent of these multifamily units are intended for the rental market, compared to just 50–60 percent during the peak years of the housing boom in 2005–06. As a result, the number of multifamily rental starts last year was at its highest level since 1998.

Gains in new construction may, however, be set to slow. The number of multifamily permits issued was up 59,000 in 2013—about half the increase in 2012. Even so, completions of new units should continue to ramp up because of the lengthy development process for multifamily properties. Indeed, multifamily completions totaled just 195,000 units in 2013, implying that many new units are still in the pipeline.

While multifamily construction activity has picked up across the country, the volume of new units remains below last decade's average in many markets. Overall, multifamily permits exceeded their 2000s averages in 47 of the 100 largest metro areas in 2013, but were less than half those levels in another 23.

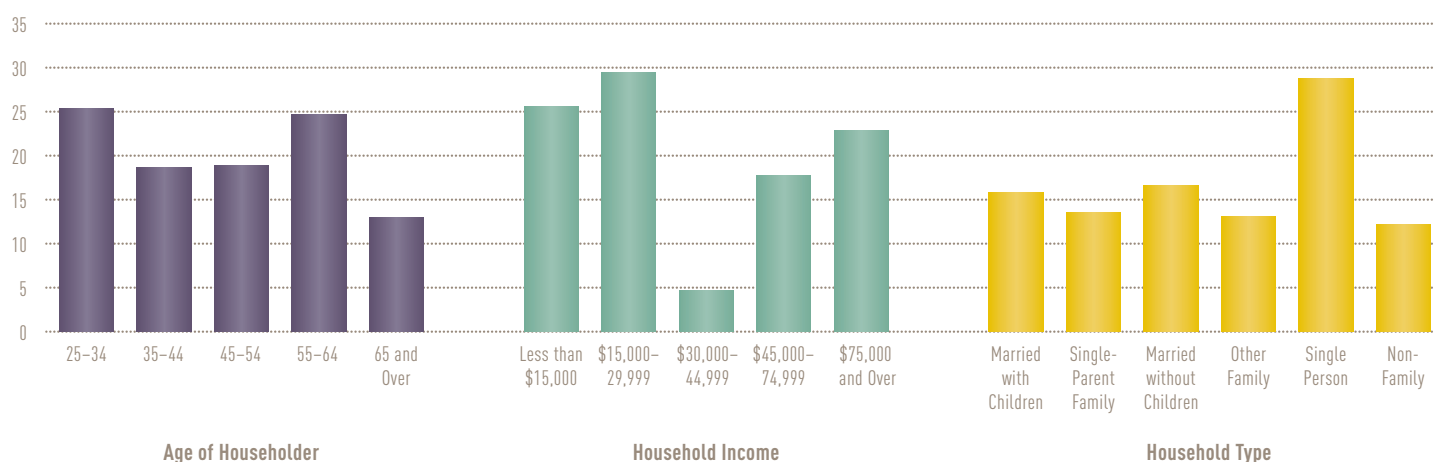
The extent of the rebound ranges widely even within the 15 markets averaging the most new multifamily units in the 2000s. At one extreme is Austin, where activity was twice as high as last decade's average (**Figure 25**). In six other markets, rental construction has exceeded average levels. Though not yet at their 2000s levels, New York, Miami, and Atlanta all experienced especially large gains in 2013. Meanwhile, other markets that had some of the biggest construction booms in the 2000s—including Tampa, Orlando, and Phoenix—have been slower to recover. Of these, Las Vegas trails farthest behind, with multifamily permitting lagging 80 percent below annual levels averaged in 2000–09.

Survey data from MPF Research suggest that demand and supply for investment-grade apartments are close to balance. From 2010 through 2012, increases in occupied apartments greatly outpaced the number of rental units coming on line, helping to drive down vacancy rates and push up rents. In 2013, however,

FIGURE 23

Households Across the Spectrum Have Fueled the Growth in Renters

Share of Renter Household Growth, 2005–13 (Percent)



Source: JCHS tabulations of US Census Bureau, Current Population Surveys.

the addition of new apartments accelerated while growth in renters moderated. With growth in demand and supply roughly equal at 160,000 units in 2013, occupancy rates were stable and rent gains more modest. Even if rental demand does not ease further, the expected increase in multifamily completions should create some slack in markets and slow the pace of rent increases.

FIGURE 24

Although Still Widespread, Rent Pressures in Many Metros Eased in 2013

Number of Metros



Notes: Estimates are based on a sample of investment-grade properties for the 93 metropolitan areas covered. Changes are measured fourth quarter to fourth quarter.
Source: JCHS tabulations of MPF Research data.

INFLUX OF SINGLE-FAMILY RENTALS

Although multifamily production has picked up substantially, newly constructed units have met just a fraction of the recent growth in renter households. From 2006 through 2012, multifamily completions totaled 1.6 million units while growth in renter households hit 5.2 million. While excess vacant units from the building boom helped to meet the surge in demand, conversions of owner-occupied single-family homes to rentals provided most of the new supply. Single-family homes have always made up a significant portion of the rental housing stock, but the recent increase is remarkable. The American Community Survey reports that the number of single-family homes rented during this period increased by 3.2 million, roughly twice the number of new apartments added, pushing the single-family share of all rentals from 30 percent in 2006 to 34 percent in 2012 (Figure 26).

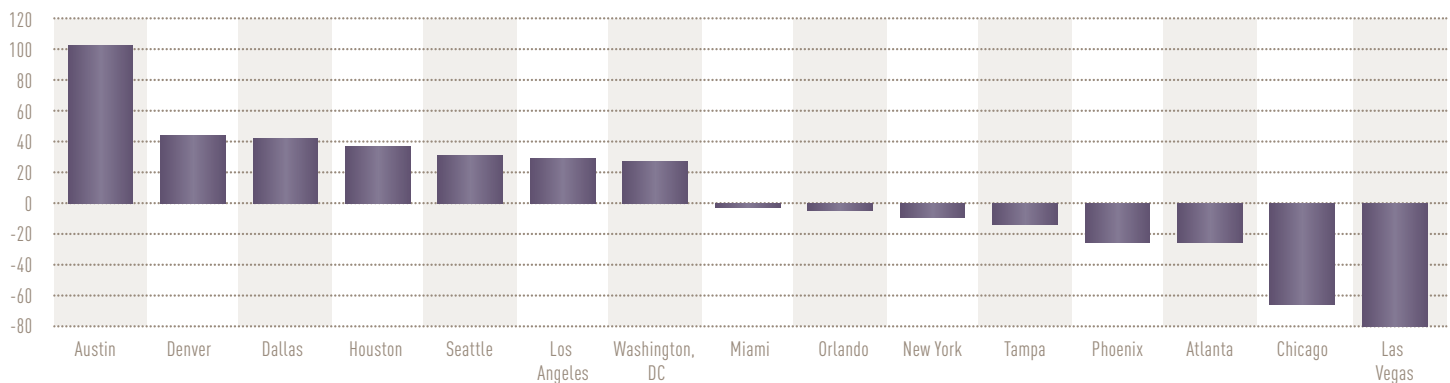
Although individuals have traditionally owned the vast majority of single-family rentals, institutional investors were enticed into the market by a unique set of conditions following the recession: a high volume of distressed homes for sale, weak demand from owner-occupants, and high rent-to-price ratios. While precise numbers are hard to come by, estimates suggest these investors have amassed more than 200,000 single-family units from 2012 through early 2014, concentrating most of their purchases in selected markets. Now that distressed home sales have slowed and home prices have risen sharply, however, most of the largest investors have indicated that they will limit future acquisitions.

The experience of managing and financing large portfolios of single-family rentals may provide new business models for this segment of the market. Over the past year, several institutional investors issued securities backed by the cash flow from their

FIGURE 25

The Recovery in Multifamily Construction Varies Significantly Across Metros

Multifamily Units Permitted in 2013 Relative to 2000-09 Annual Average (Percent)

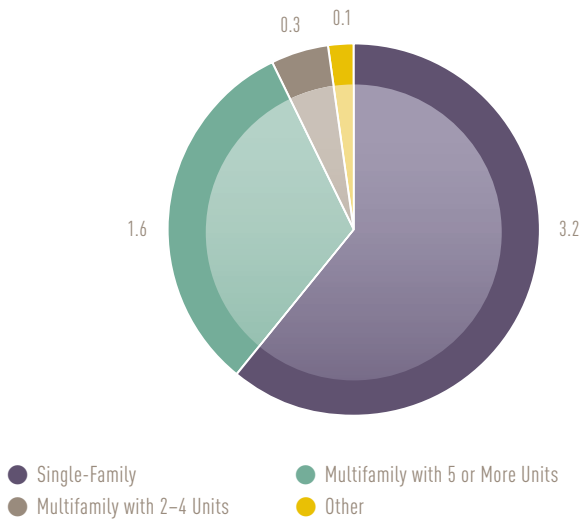


Source: JCHS tabulations of US Census Bureau, Building Permits Survey data.

FIGURE 26

Most of the Recent Increase in Rental Supply Has Come from Single-Family Homes

Growth in Occupied Rental Units, 2006–12 (Millions)



Note: Other units include mobile homes, trailers, boats, recreational vehicles, and vans.
Source: US Census Bureau, 2006 and 2012 American Community Surveys.

single-family properties, which may open new avenues for debt financing. This may foster further consolidation of investor activity in the single-family market, although the profitability of managing large portfolios of geographically scattered properties remains in question. Regardless, these decisions have important implications for the communities with large concentrations of investor-owned properties as the management and eventual sale of these homes will have a significant impact in these areas.

THE DIMINISHING LOW-COST SUPPLY

New multifamily construction typically adds units at the upper end of the rent distribution, well out of reach for households with limited incomes. The 2011 American Housing Survey reports that the median monthly gross rent for units built in the preceding four years was \$1,052—affordable at the 30-percent-of-income standard only to households earning at least \$42,200 a year. Just 34 percent of new units added in that period rented for less than \$800 per month or roughly the amount the median renter earning \$28,000 could afford. Among the many factors contributing to the difficulty of building new low-cost rentals are the high costs of land zoned for higher-density housing, financing for acquisition and development, and construction materials and labor.

At the same time, owners of existing low-rent properties have little revenue to cover operating and maintenance costs,

leaving these units at risk of removal. Of the 34.8 million rentals that existed in 2001, some 1.9 million (5.6 percent) were demolished by 2011. The loss rate for units renting for less than \$400 was more than twice as high at 12.8 percent. Although making up only a small share of the overall supply, these units thus accounted for more than a third (650,000) of total removals. Losses of units with rents between \$400 and \$600 were also relatively high at 6.7 percent. Removal rates decline as rents increase, falling to just 3.0 percent for units renting for \$800 or more.

Across the country, rental loss rates are particularly high in rural areas. Indeed, fully 8.1 percent of rentals in non-metro areas were lost in 2001–11, compared with 5.7 percent in central cities and 4.7 percent in suburbs. High rural loss rates reflect the greater presence of mobile homes in these areas, particularly in the South and West where they account for more than 10 percent of the rental stock. Mobile homes have by far the highest loss rates of any structure type, with more than one in five removed from the stock between 2001 and 2011.

PERFORMANCE OF APARTMENT PROPERTIES

With vacancy rates at their lowest point in more than a decade and rent increases consistently outpacing inflation, apartment properties continue to perform well. The National Council of Real Estate Investment Fiduciaries reports that the net operating income of commercial-grade apartments was up 3.1 percent in 2013. While well below the 6–11 percent growth in 2011–12, last year's increase was still healthy and nearly matched the 3.3 percent annual average of the last three decades.

Meanwhile, apartment property values continued to climb at a remarkable pace. According to Moody's/RCA Commercial Property Price Index, apartment prices shot up 14 percent on average in 2012–13. Indeed, rental property values hit a new high last year, exceeding their 2007 peak by 6 percent and far outpacing the recovery in owner-occupied home prices (Figure 27).

With rapidly appreciating property values and stable cash flows, commercial-grade properties posted a 10.4 percent annual rate of return last year. This nearly matches the 11.5 percent average level in the ten years preceding the housing bubble and bust (1995–2004), suggesting that growth is settling down to more sustainable rates.

Although their definitions are not strictly comparable, all measures of multifamily loan delinquencies are on a downtrend. In the latter half of 2013, the share of multifamily loans at FDIC-insured institutions that were at least 90 days past due dipped below 1.0 percent for the first time since early 2008. The share of multifamily loans held in commercial mortgage backed securities (CMBS) that were at least 60 days delinquent or had been repossessed by the lender also dropped sharply last year,

but remained high by historical standards. Multifamily loans backed by Fannie Mae and Freddie Mac continued to perform well, with delinquencies of at least 60 days at both institutions down to 0.1 percent or less at year-end.

FIGURE 27

Prices of Apartment Properties Have Recovered Much Faster than Those of Single-Family Homes and Now Exceed Their Recent Peak

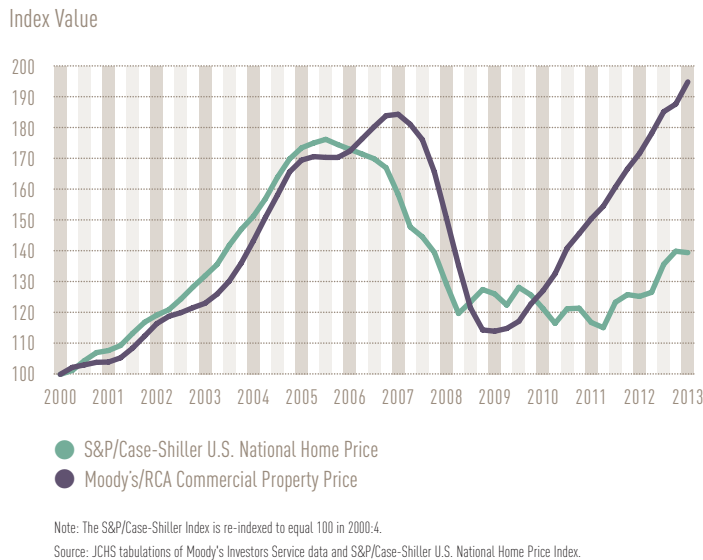
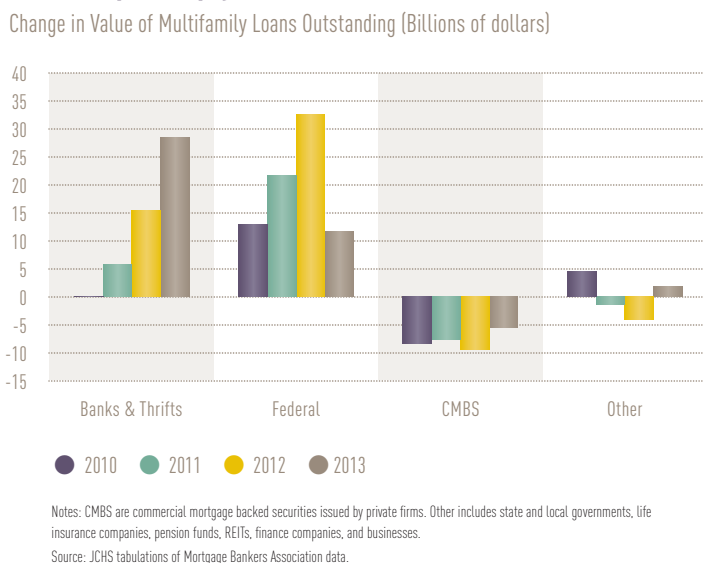


FIGURE 28

Multifamily Lending Activity at Banks and Thrifts Picked up Sharply in 2013



PRIVATE LENDING ON THE RISE

The strong financial performance of the apartment market has fueled a rebound in multifamily lending. A Mortgage Bankers Association survey indicates that originations of multifamily loans were up 13 percent in 2013, following outsized gains of 36 percent in 2012 that had pushed annual multifamily originations above their mid-2000s peak.

Of particular note is the changing source of these loans. Based on estimates of total loans outstanding (including both new originations and repayment or writeoffs of existing loans), federal sources accounted for much of the increase in lending early in the multifamily recovery. In 2010, the volume of loans backed by the GSEs and FHA increased by \$13 billion, loans held by banks and thrifts were essentially flat, and those held in CMBS fell \$9 billion. As the rental recovery gained traction, however, private lenders began to step up their presence in the market. By 2013, net lending by banks and thrifts jumped by \$29 billion—more than twice the increase in the volume of government-backed loans (Figure 28).

As long as they continue to perform well, multifamily properties should attract an increasing level of private funding. In the meantime, plans to shrink the federal footprint in the multifamily sector have been put on hold to help meet the rising demand for rental properties and to address renter affordability challenges.

THE OUTLOOK

Predicting the course of homeownership rates, and therefore rentership rates, is difficult because it depends on a host of economic factors as well as consumer attitudes. But given recent signs that the homeownership rate may be stabilizing and that new rental units will continue to come on line, market conditions should come more into balance.

Assuming homeownership remains at today's rates, the Joint Center estimates that demographic forces alone would lift the number of renter households by 4.0–4.7 million in 2013–23. While considerably slower than the recent pace of growth, these increases would still exceed the long-run average over the past several decades.

Two broad trends will drive future growth in renters: the imminent surge in the number of older households and the increasing racial/ethnic diversity of younger age groups. Over the coming decade, the number of renters aged 65 and older is projected to rise by about 2.2 million and account for roughly half of all renter growth. The aging of the population also means that the share of renters that are single persons or married couples without children will soar. Meanwhile, Hispanics will account for slightly more than half of all new renters while other minorities will make up the remainder. Meeting this diverse demand will require a range of new rental options in a variety of community settings.