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Hot Rents: Where the Growth Is

Secondary apartment markets pick up steam, point to broader recovery.

By: Chris Wood

What a report card! Another quarter, another round of impressive rent fundamental numbers in the apartment sector, with rent growth continuing, particularly increasing its pace in secondary markets as occupancies return to pre-recession highs. The inclusion of May and June—the beginning of peak rental season—in Q2 numbers makes mid-year data all the more significant, and reports from Carrollton, Texas-based MPF Research and Dallas-based Axiometrics show cause for optimism with continued buoyancy in effective rent growth and apartment occupancy across the country.

“There are some really good numbers in the second quarter, and by and large, the numbers came in as expected although with a little bit of shuffling in performance by product niche and also by metro,” says MPF Research vice president Greg Willett. MPF pegs total Q2 revenue lift for the apartment sector at 2.5 percent, driven by an average effective rent increase of 1.7 percent and an 0.8 percent occupancy increase that puts the national average at 94.3 percent, a substantial jump from the low of 91.8 percent recorded in late 2009, but still well below the 95.6 percent occupancy achieved just prior to the recession in 2008. “There’sa little bit of room there in occupancies for some additional absorption,” Willett says. “But a big chunk of the revenue growth is going to come on the rent side, except for a handful of markets—particularly in the Pacific Northwest—which are not all the way back to completely full.”

Looking at May numbers (Q2 not inclusive of June), Axiometrics reports an increase in the national apartment occupancy rate from 93.3 percent in April to 93.96 percent in May. Year to date, the occupancy rate has increased 86 basis points (bps), below the 136 bps increase for the same period in 2010, with the slowdown likely due to an increase in effective rents, which Axiometics estimates will rise 5.9 percent in 2011, the largest annual increase since 2005. “Effective rent growth is clearly stronger than it was over the same period last year,” says Axiometrics president Ron Johnsey. “However, some markets are showing a significant slowdown, including Washington, D.C.; Durham, N.C.; Greenville, S.C.; Nashville, Tenn.; and Raleigh, N.C., while others including Austin, Dallas, Houston, Oakland, San Diego, San Francisco, Santa Anna, and Seattle are showing major improvements.

Compared to a national annual effective rent gain of 4.9 percent through May, Axiometrics points to the following leaders and laggards with effective rent variances from the national average.

Leading Momentum, Effective Rent Variance
San Jose, Calif., 8.1%
San Francisco, 4.8%
Austin, Texas, 3.8%
Seattle, Wash., 3.6%
Boston, 2.5%
Dallas, 1.6%

Lagging Momentum, Effective Rent Variance
Las Vegas,-6.2%
W. Palm Beach, Fla., -3.2%
Los Angeles, -3.1%

Indeed, markets that were first to recover from the recession are seeing rent growth begin to slow as occupancies firm and renters show a reticence to relocate, particularly for single-family home purchases. Secondary markets are now following the rent and occupancy growth trajectory set by the core markets, though, pointing toward a broader recover across the multifamily sector. “Certainly, as we came into 2011, there was a huge premium for top-tier product versus the bottom end of the marketplace, but we’ve now have seen that momentum pick up in the bottom end,” Willett says. “The premium is still there, but it is meaningfully smaller than it was previously. That opens things up and is a good indicator of a broader overall recovery and is what you like to see as the cycle progresses. It is encouraging to see those numbers start to pop up now.”

According to MPF, the annual rent growth leaders at the mid-year point are:
1. San Jose, Calif.: 12.2%
2. San Francisco: 7.7%
3. Seattle: 7.1%
4. Oakland, Calif.: 6.6%
5T. Portland, Ore.: 6.4%
5T. Austin, Texas: 6.4%
7. Pittsburgh: 6.1%
8. Minneapolis: 5.8%
9. Chicago: 5.4%
10. Denver: 5.3%
11: Boston - 5.2% annual rent growth

As the year progresses, Willett expects additional secondary markets to enter the growth leaders chart as the stronger core markets follow the lead of metros such as Washington, D.C., and New York where recovery to 2007 highs has already occurred. “The markets that were first out of the gate with some meaningful rent growth early in 2010 are the places where you’ve gotten rents back up to previous highs, and there seems to be a little of a tendency once you reach that point to take your foot off of the gas,” Willett says. “Rents continue to go up, but not at the pace that they had been, so you are seeing a little slow down in the annual change numbers, but the reverse of that is also true: Some of the markets that had been lagging are where you are really starting to see some pick up in quarterly numbers, places like Phoenix and Southern California are starting to fare better at this point.”

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