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The Rise and Fall of Concessions: Is the Market Resetting?

- With multifamily demand diminished by job losses and social distancing measures imposed due to COVID-19, concessions rose sharply in the spring and fall of 2020. The impact varied widely between geographies and property types. Not surprisingly, the growth of concessions tracked other broad measures of multifamily performance, such as occupancy and rent growth.

- Concessions increased the most in the upper tier of the market: gateway metros and Class A and high-rise properties. Gateway markets had the largest percentage increase in concessions and the highest value of concessions as a share of monthly rent.

- Concessions grew the least in tertiary markets and in Class C and low-rise properties. The percentage of Class C and garden apartments that use concessions declined by the end of the year, a sign that demand shifted to low-cost properties.

- Strategies employed by owners to optimize income—such as offering concessions or lowering asking rent—are affected by competitive pressures, which may differ by metro. Metros with the highest percentage of properties offering concessions are those with a pandemic-driven drop in demand and those with copious amounts of supply coming online.

- Gateway markets have seen the biggest growth in concessions during the pandemic, but secondary metros are among the leaders in the percentage of properties that employ the tactic over time. Concessions are highest on a per-unit basis in metros with the highest average rents—particularly San Jose, San Francisco and New York—and the largest decline in occupancy rates and asking rents since the start of the pandemic.

- Concessions peaked in the middle of the year and then declined in the fourth quarter. This could be a sign that the market is stabilizing or that owners are shifting strategies to attract and retain tenants. The decline could signal that new asking-rent levels are being set that will be carried into the post-pandemic market.

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Concession Spike

COVID-19 was the dominant storyline for the multifamily market in 2020, as the shelter-in-place orders that began in March produced many short-term changes in demand. The most immediate impact was felt in employment: The U.S. labor market shrank by 22.4 million between March and May. Employment recovered to some extent through the rest of the year, but as of December the U.S.'s 142.6 million jobs were still 9.8 million short of pre-pandemic numbers.

The composition and geography of the lost jobs, not to mention health and safety considerations, wreaked havoc on multifamily demand. Many Americans, particularly low-wage service industry workers who were already stressed on housing costs, were forced to change plans. At the same time, business closures played out differently across the country. Cities with the densest populations and the earliest exposure to the virus enacted the strictest bans on travel and businesses.

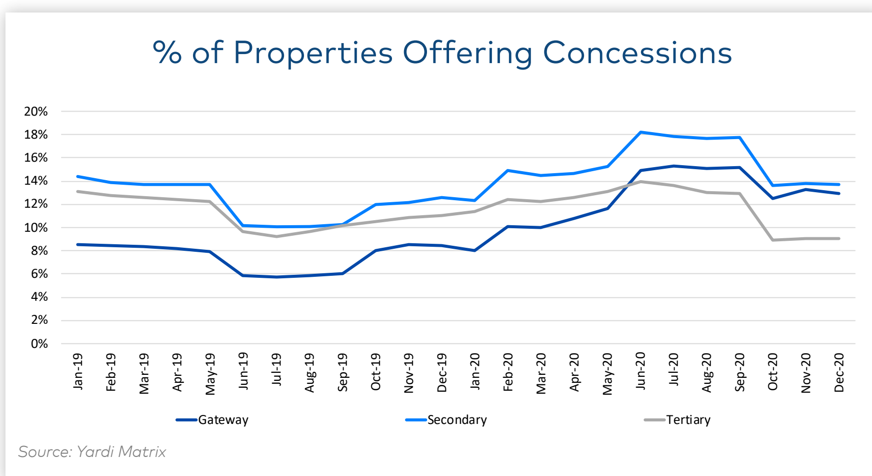
The resulting disruption hit the multifamily industry at the start of the traditional spring peak leasing season. Demand fell due to the loss of jobs and income and the safety issues that made people fearful to venture into public. To maintain occupancy rates, apartment owners employed strategies that included rolling over leases with no bump in rent and increasing use of concessions, mainly by offering periods of free rent. Concessions are predominantly—but not exclusively—used to attract new tenants.

The use of concessions increased dramatically during the spring and summer of 2020, according to a study by Yardi Matrix. On a national level, the percentage of properties that employed concessions increased by 4.6% to 15.8% in July, from 11.2% in January. As a percentage of rent, concessions increased to 6.4% in July from 5.5% in January.

However, the use of concessions varied. Concessions rose more in 2020 in gateway, high-rise and Class A properties, and the least in low-rise properties and tertiary metros. That finding is consistent with rent and occupancy data that show that demand has fallen the most in high-cost gateway and urban markets, as tenants seek out more affordable and spacious housing while most amenities and offices in dense cities remain closed.

Biggest Increase in Gateways

The growth in concessions has the biggest impact in gateway metros, which include New York, San Francisco, Chicago, Boston, Washington, D.C., and Los Angeles. Gateway markets were among the nation's hottest markets during the last cycle, as job growth in technology and other office-using sectors was concentrated in urban coastal markets that benefited from the growing preference for the live-work-play lifestyle. But as the pandemic shut down urban amenities and most corporations closed offices and focused on working from home, residents shifted to lower-cost areas and suburbs where they have more space.

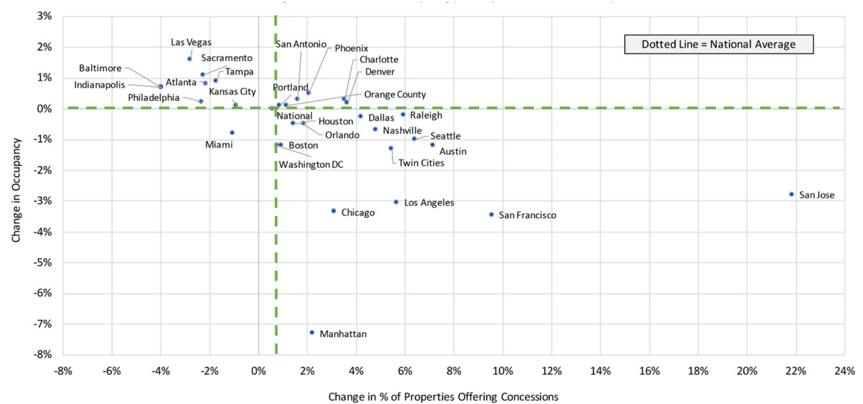


Source: Yardi Matrix

Consequently, rent growth, occupancy and demand deteriorated

the most in gateway markets. U.S. metros with the largest declines in occupancy rates last year were Manhattan (-7.3%), San Francisco (-3.4%), Chicago (-3.3%), Los Angeles (-3.1%) and San Jose (-2.8%), according to Matrix, and those numbers probably don't reflect the entirety of the falloff. The largest declines in rent year-over-year as of December 2020 were in San Jose (-13.7%), New York (-11.7%), San Francisco (-9.4%), Seattle (-6.2%), Washington, D.C. (-4.9%) and Boston (-3.7%).

Change in Concessions and Occupancy
(January 2020-December 2020)



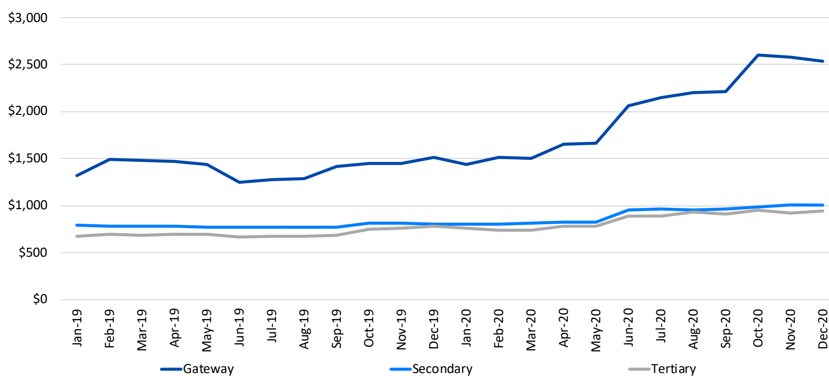
Source: Yardi Matrix

Considering the drop-off, it's no surprise that the percentage of properties offering concessions in gateway metros almost doubled between January and July—from 8.0% in January to 15.3% in July. Concessions shrank in the fourth quarter in gateway metros, ending the year at 13.0%.

Secondary and tertiary metros traditionally have had a higher overall rate of concessions, but they saw a much smaller rate of growth during the pandemic. Concessions for multifamily properties in secondary metros rose from 12.3% in January, peaking at 18.2% in June and ending the year at 13.7%. Concessions for properties in tertiary markets started the year at 11.3% in January, peaked at 13.9% in June and ended the year at 9.1%. The data is consistent with the trend that apartment demand shifted from high-cost urban markets to less-expensive markets across the country.

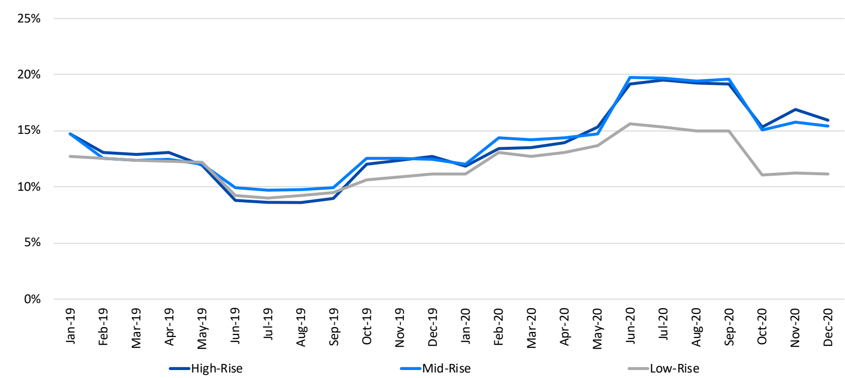
Not only did the number of properties offering concessions increase more in gateway metros but the value of the concessions is higher and rose by a greater amount in those markets during the pandemic. The average concession in gateway markets grew from $1,444 in January to $2,533 in December, up 75.4% during the year. In secondary markets, the average concession rose from $806 in January to $1,007 in December, up 24.9%. In tertiary markets, the average concession rose from $759 in January to $941 in December, up 24.0%.

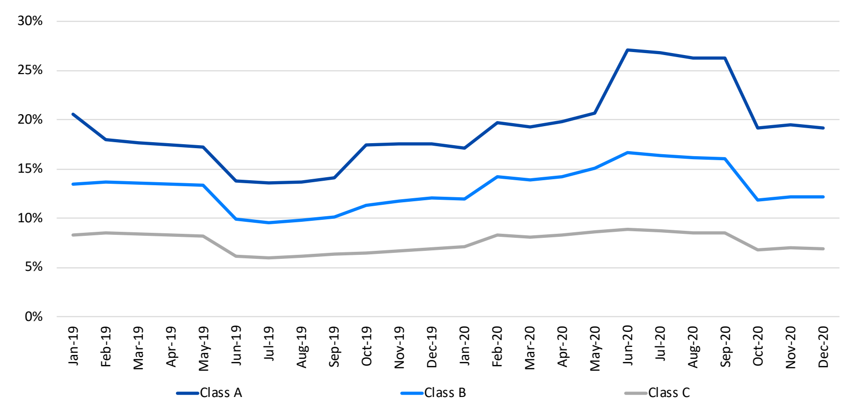
Average Concession by Metro Size ($)



Source: Yardi Matrix

Other metrics of property quality and location showed a similar pattern. In high-rise properties, which correspond to urban submarkets, the percentage of properties using concessions was 11.8% in January, peaked at 19.5% in July and fell to 16% in December. In mid-rise properties, which are associated with





inner-ring suburbs, concessions were 12% in January, peaked at 19.8% in June and fell to 15.4% in December. For low-rise properties, associated with suburban garden apartments, concessions were 11.2% in January, peaked at 15.6% in June and fell to 11.2% in December.

Among Class A properties, the percentage offering concessions was 17.1% in January, 27.1% in June and 19.1% in December. For Class B, it was 12% in January, 16.7% in June and 12.2% in December. For Class C, it was 7.1% in January, 8.9% in June and 6.9% in December.

Occupancy, Supply Drive Concessions

Many metros that have seen the largest occupancy declines since January are also among the metros that have the largest increase in percentage of properties offering concessions. San Jose saw the greatest increase in the percentage of all properties offering concessions since January, growing from 17.1% in January to 39.0% in December, a 21.9 percentage point jump. San Jose was also among the top five markets for the largest declines in occupancy since January, declining by 2.8 percentage points. Other metros in the top five for concession increases include San Francisco (9.6 percentage point increase in concessions and 7.3% decline in occupancy), Austin (7.2%, -1.2%), Seattle (6.4%, -1.0%) and Raleigh (5.9%, -0.2%).

On the other end of the spectrum, some metros that have outperformed the national average this year in occupancy rate change have seen a decline in the percentage of properties offering concessions. The Inland Empire saw a 5.1% decline in the percentage of properties offering concessions and a 1.8% increase in occupancy. Baltimore (-4.0%, 0.7%), Indianapolis (-3.9%, 0.7%) and Las Vegas (-2.8%, 1.6%) followed behind—these metros were among the leaders in rent growth for 2020, as well.

While the use of concessions as a tactic to maintain occupancy rates grew the most in gateway metros during the pandemic, most of the metros with the highest percentage of properties offering concessions are secondary and tertiary markets. San Jose led the nation in percentage of properties offering concessions as of December 2020, with 40% of Class A and B properties offering an average concession of $3,500. San Francisco (20.8%)

Highest % of Properties Offering Concessions (Dec 2020)

Metro	% of A + B Properties Offering Concessions	Average Concession
San Jose	40.2%	$3,542
San Antonio	26.4%	$743
Austin	24.8%	$1,049
Dallas	22.5%	$913
Denver	21.5%	$1,262
Houston	21.2%	$860
Nashville	21.0%	$1,074
San Francisco	20.8%	$3,595
Los Angeles	20.1%	$2,427
Seattle	19.4%	$1,993
Raleigh	19.0%	$939
Chicago	17.5%	$2,014
Orlando	17.4%	$1,080
Charlotte	17.3%	$1,036
Kansas City	16.5%	$782

Source: Yardi Matrix

Lowest % of Properties Offering Concessions (Dec 2020)

Metro	% of A + B Properties Offering Concessions	Average Concession
Orange County	14.7%	$1,350
Portland	14.4%	$1,344
Phoenix	13.1%	$727
Twin Cities	12.9%	$1,162
Tampa	12.8%	$1,026
Las Vegas	12.2%	$582
Atlanta	12.1%	$955
Miami	12.0%	$2,433
Philadelphia	11.1%	$1,427
Boston	10.4%	$2,505
Washington DC	9.3%	$1,451
Indianapolis	8.6%	$570
Manhattan	7.7%	$6,220
Sacramento	3.3%	$1,114
Inland Empire	2.7%	$1,581

Source: Yardi Matrix

and Los Angeles (20.1%) also made the top 10 among metros that offer the most concessions.

However, concessions in many cases are most prevalent in secondary metros with strong economies and growing populations. After San Jose, the metros offering the most concessions are all in Texas: San Antonio (26.4% of Class A and B properties), Austin (24.8%), Dallas (22.5%) and Houston (21.2%). Other high-growth metros with large percentages of Class A and B properties offering concessions include Denver (21.5%), Nashville (21.0%), Seattle (19.4%), Raleigh (19.0%), Orlando (17.4%) and Charlotte (17.3%).

While demand is strong, each of these metros is among the leaders in deliveries. Over the long term, fundamental drivers are strong, but at the same time the easy ability to build new supply adds to the competition for renters within the market.

Market Reset?

The data shows a pattern of apartment demand shifting from more expensive properties and metros to lower-cost properties and metros, which makes sense given the economic situation. More owners are choosing concessions to attract renters in the hope of returning to pre-COVID-19 levels of rent when the economy rebounds. Concessions, however, are but one tactic for apartment owners trying to maximize revenue. Other options include lowering rent. Differences in metro-level data could mean that concession strategies depend in part on what competitors are doing.

Why has the use of concessions declined after peaking in the summer? There could be several explanations: The job market and consumer sentiment gained in recent months as businesses in parts of the country reopened and the COVID-19

vaccine was developed, which has created optimism about reopening the economy and boosted demand somewhat.

Another factor is that the natural leasing cycle was delayed for several months. Concessions tend to rise and fall with the season, increasing during the winter, when demand is weak, and decreasing in the spring, when demand is at its highest. The pandemic may not have eliminated the 2020 leasing cycle so much as pushed it back a few months.

Although it is still too soon to draw firm conclusions, the recent decline in concessions might also indicate that in some metros the dominant trend is to reset rents at lower levels rather than using incentives. Moving forward, the big question facing multifamily is how much employment trends such as work-from-home and lifestyle preferences for city versus suburbs have changed the demand equation. The answer will determine the use of concessions and whether rents reset at new levels.

—Paul Fiorilla, Director of Research, and Maddie Harper, Senior Research Analyst

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