March 2021

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Multifamily Absorption Surprises On the Upside in 2020

Despite a pandemic that restricted many routine activities and a recession that left millions jobless, demand for multifamily properties was unexpectedly positive in most parts of the country in 2020. Some 252,000 apartment units, or 1.7% of total stock, were absorbed in the U.S. in 2020, according to a review of Yardi Matrix's database.

The number of units absorbed in 2020 was only 12.0% less than the 286,300 units absorbed the prior year, and not too far off the average during the last cycle. Considering the economic and social calamity that befell the U.S., in many respects due to COVID-19, the fact that demand held up as well as it did is a relief for the apartment industry.

The positive multifamily absorption—which counts the net change in occupied units—was broadly distributed. Net absorption was in the black in 25 of the 30 largest metros, led by Dallas, Atlanta, Denver and Phoenix. Those top 25 metros accounted for 158,300 units absorbed, more than 60% of total U.S. net absorption.

Negative absorption was mostly limited to a handful of large markets, with the worst performance in the Bay Area and New York City, which combined for -22,100 units absorbed in 2020. By metro size, high-cost gateway metros had the worst performance, with net absorption of -0.3% (-7,600 units). Demand was much better in secondary (154,100 units, or 2.3% of total stock) and tertiary (96,200 units, or 2.0% of stock) markets.

On a regional level, renters continued to flock to the Southeast (96,700 units absorbed, or 2.4% of total stock), the Southwest (56,800 units, 2.1% of stock) and the West (57,100 units, 1.9% of stock). Meanwhile, demand was slightly positive in the Midwest (27,100 units, 1.1% of stock) and the Northeast (4,900 units, 0.2% of stock).

Market	Net Absorption 2020	Net Absorption % Stock 2020	Occupancy Rate Dec. 2020	Avg. Rent Dec 2020
National	252,013	1.7%	94.7%	$1,389
Secondary	154,112	2.3%	94.5%	$1,337
Tertiary	96,160	2.0%	95.4%	$1,183
Gateway	-7,599	-0.3%	93.9%	$2,201

Source: Yardi Matrix

Year of the Pandemic

COVID-19 roiled the multifamily industry, starting with the shelter-in-place orders in March 2020. The biggest impact on the segment emanated from the lack of mobility, the closing of entertainment venues and restaurants, and the change in work practices. Unemployment skyrocketed among low-wage service workers, while most professional service workers began working from home.

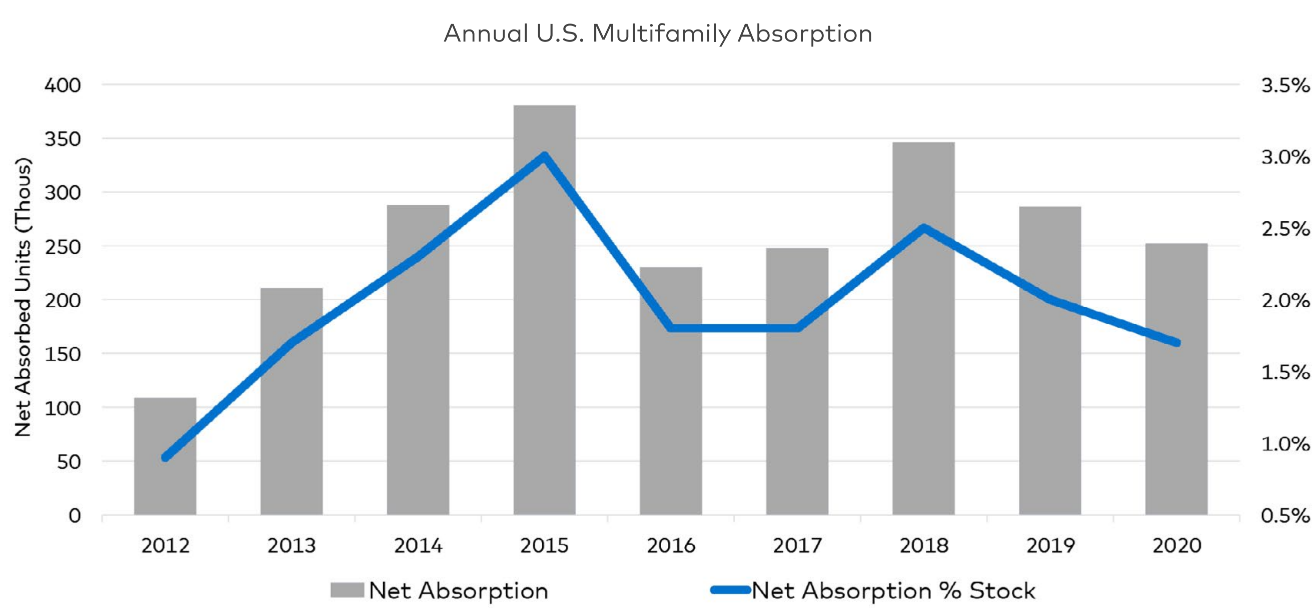
More than 22 million jobs were lost in the early months of the pandemic, before the recovery began in the second half of the year. As of January 2021, jobs in the U.S. totaled 142.7 million, still 9.8 million below the 152.5 million peak in February 2020. The unemployment rate as of January was 6.3%, though some Federal Reserve officials have suggested the real rate is closer to 10% because many workers dropped out of the workforce during the pandemic.

Multifamily was affected on many levels. Apartment demand and household formation are normally strongly correlated with the number of jobs. The loss of employment prevented many from starting new renter households. The desire on the part of some to avoid crowds restricted movement, which led to a decrease in tenants relocating and an increase in renewals.

The work-from-home phenomenon, although it has been surprisingly successful from a productivity point of view, reduced demand for units in and around large office-using employment centers. It enabled office workers to move to less expensive markets or stay with family or friends. The lack of entertainment also made 24-hour cities such as New York and San Francisco less appealing, leading to an exodus.

The loss of demand was not just out-migration. Large employment centers typically benefit from the inflow of new workers, such as college graduates starting careers in professional offices. With office work still being performed remotely, that typical inflow of residents to markets with a large employment base was interrupted.

About two-thirds of last year's net reduction in migration in the U.S. was due to a decline in in-migration, as opposed to out-migration, according



Source: Yardi Matrix

Market	Net Absorption 2020	Net Absorption % Stock 2020	Occupancy Rate Dec. 2020	Avg. Rent Dec 2020
National	252,013	1.7%	94.7%	$1,389
Dallas	19,233	2.4%	93.8%	$1,216
Atlanta	12,864	2.8%	94.7%	$1,357
Denver	11,552	4.0%	94.5%	$1,546
Phoenix	10,082	3.2%	95.5%	$1,266
Houston	8,377	1.3%	92.1%	$1,099
Austin	7,893	3.1%	93.3%	$1,361
Miami	7,721	2.5%	94.4%	$1,702
Tampa	6,196	2.8%	95.4%	$1,339
Charlotte	6,073	3.3%	95.1%	$1,233
San Antonio	5,836	2.8%	93.0%	$1,052
Inland Empire	5,793	3.7%	97.5%	$1,698
Las Vegas	5,279	3.0%	96.1%	$1,159
Orlando	5,175	2.3%	94.1%	$1,337
Philadelphia	4,960	1.6%	95.7%	$1,428
Twin Cities	4,546	2.1%	95.1%	$1,330
Raleigh–Durham	4,220	2.6%	94.5%	$1,228
Columbus	4,204	2.4%	95.0%	$1,019
San Diego	4,187	2.2%	96.1%	$1,998
Portland	4,018	2.5%	95.1%	$1,432
Washington DC	3,873	0.7%	94.1%	$1,758
Boston	3,863	1.6%	95.0%	$2,216
Seattle	3,260	1.3%	94.1%	$1,799
Los Angeles	3,080	0.7%	94.2%	$2,151
Sacramento	3,039	2.3%	96.9%	$1,631
Nashville	2,964	2.1%	94.2%	$1,279
Pittsburgh	-283	-0.3%	95.5%	$1,143
San Jose	-685	-0.5%	92.7%	$2,523
San Francisco	-2,736	-1.0%	92.2%	$2,461
Chicago	-2,816	-0.8%	90.9%	$1,528
New York	-18,603	-3.2%	94.0%	$3,184

Source: Yardi Matrix

Market	Net Absorption 2020	Net Absorption % Stock 2020	Occupancy Rate Dec. 2020	Avg. Rent Dec 2020
National	252,013	1.7%	94.7%	$1,389
Southeast	96,740	2.4%	94.7%	$1,316
West	57,103	1.9%	95.2%	$1,796
Southwest	56,818	2.1%	93.5%	$1,134
Midwest	27,131	1.1%	94.6%	$1,111
Northeast	4,882	0.2%	95.5%	$2,024

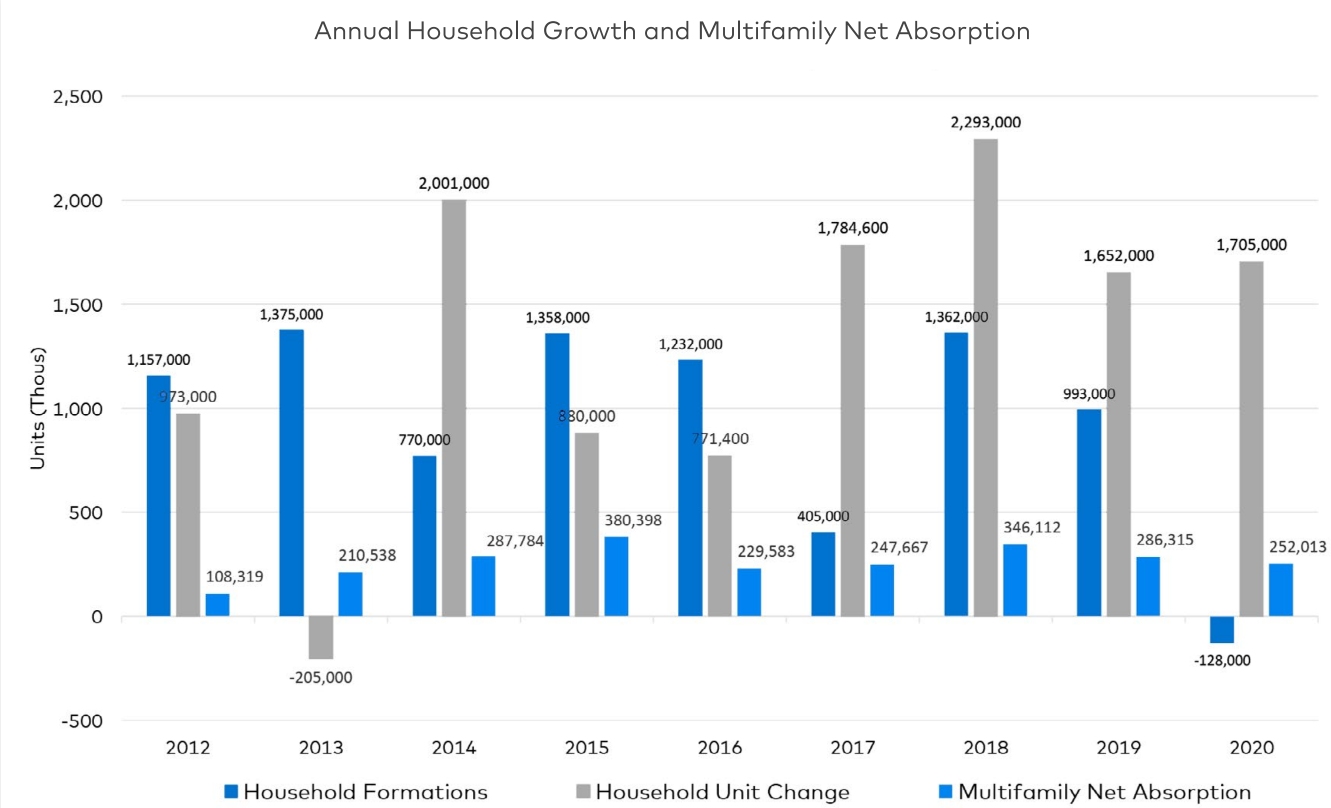
Source: Yardi Matrix

to a February 2021 study by policy economist Stephan Whitaker of the Federal Reserve Bank of Cleveland. The reduction in inflow was particularly acute in rapidly growing employment centers such as San Jose, Seattle, Washington, D.C., Los Angeles, Denver and New York, according to the study, titled *"Did the COVID-19 Pandemic Cause an Urban Exodus?"*

The loss of demand, both in-migration and out-migration, had a large impact on multifamily performance, even in metros where overall demand was positive. Rent growth in 2020 was negative in most major urban centers, led by those with negative total absorption: San Jose (-13.4%), New York (-11.2%), San Francisco (-9.6%) and Chicago (-3.3%) all saw poor performance.

But negative rent growth wasn't limited to metros with negative absorption; many of the secondary metros with strong employment metrics and positive net migration also saw rents drop in 2020, including Seattle (-6.2%), Washington, D.C. (-5.1%), Austin (-3.3%), Los Angeles (-2.9%) and Denver (-1.6). In these metros, the combination of a large amount of new supply and lower-than-expected in-migration forced property owners to reduce rents to fill new product while trying to maintain occupancy in existing assets.

Metros with the strongest net absorption in 2020 include Denver (4.0% of stock), the Inland Empire (3.7%), Charlotte (3.3%), Phoenix (3.2%), Austin (3.1%) and Las Vegas (3.0%). On an absolute basis, Dallas led with 19,200 units absorbed, followed by Atlanta (12,900), Denver (11,600) and Phoenix (10,100). These metros have seen an increase in jobs and population that has been exacerbated by the exodus from gateway metros.



Sources: U.S. Census Bureau, Yardi Matrix

Despite Worries, Encouraging Signs

Demand for multifamily held up surprisingly well during the pandemic. At the beginning, it seemed as if the industry would face a bear market from negative economic growth, the loss of millions of jobs, sheltering in place, shutdown of urban offices and more. Data from the U.S. Census Bureau suggests that the pandemic reduced household formation in 2020, although the data was mixed.

Household formation in the U.S. was -128,000 in 2020, after averaging 1.2 million per year in the previous two decades, per the Census Bureau. That number seems reasonable, based on the recession and decline in personal movement, but it is hard to square with the experience of the housing industry in 2020. Not only was multifamily absorption healthy but homeownership rose as people took advantage of low interest rates and moved out of cities for more space. The U.S. homeownership rate in the fourth quarter of 2020 was 65.6%, 30 basis points higher than the first quarter and the highest it has been since the second quarter of 2012.

Another Census Bureau measure called "household estimates," based on a survey of housing vacancy, tells a different story than formations data. The household estimates survey reports that the number of U.S. households grew by 1.7 million in 2020, which is in line with the average of the last four years. The truth is likely somewhere between the two Census numbers, which may be subject to revision. COVID-19 forced the agency to suspend in-person interviews at points during the year, so the 2020 data may be less accurate compared to previous years. Whatever the case, multifamily demand grew less than it would have absent the pandemic, and extreme consequences were limited to a handful of major urban centers.

Even though demand was better than expected through the pandemic, and the industry mood as measured by fundamental performance and pricing remains optimistic, multifamily has a plethora of issues to face in 2021. These include, but are not limited to:

- Renter support. Industry trade groups estimate that renters are behind on payments by as much as $70 billion. Some tenants will make up the payments over time, and some property owners will be reimbursed through a $25 billion federal renter subsidy passed by Congress, but many owners will have to deal with payment shortfalls.

- Multifamily delinquency rates remain low, but in some cases that is because of forbearance by lenders that will be dealt with after the pandemic.

- Some state and city-level jurisdictions have implemented eviction bans that increase the difficulty of collecting rents.

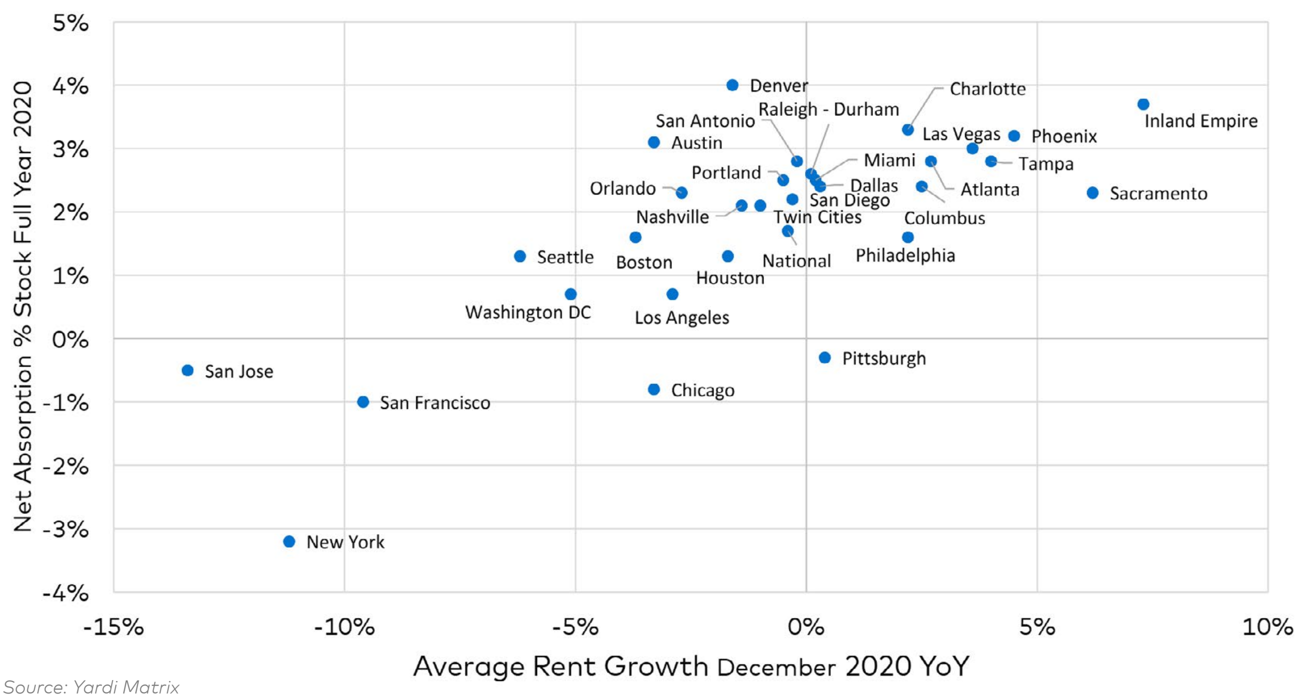
- The shortage of affordable housing and local regulatory efforts stymie needed development.

By and large, though, the signs going forward are encouraging. The availability of COVID-19 vaccines makes it likely that normal activity will be possible by the end of 2021, or maybe in 2022. When downtown office buildings and urban entertainment venues reopen, some of those who left are sure to return. Another positive sign is that apartment absorption accelerated to 160,400 in the second half of 2020, up 75% and above the long-term average. Whatever "normal" means post-COVID-19, it could be on its way before too long.

—Paul Fiorilla, Director of Research, and
Casey Cobb, Senior Analyst

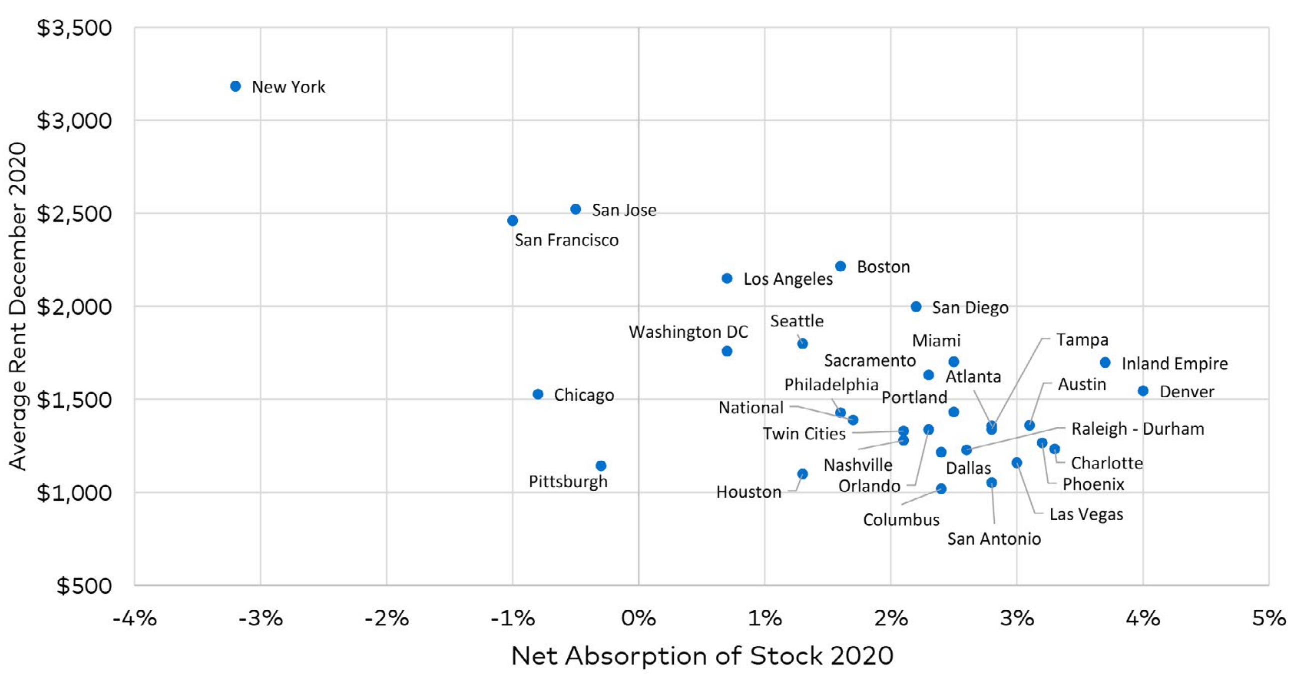
Appendix

Rent Growth vs Net Absorption % Stock

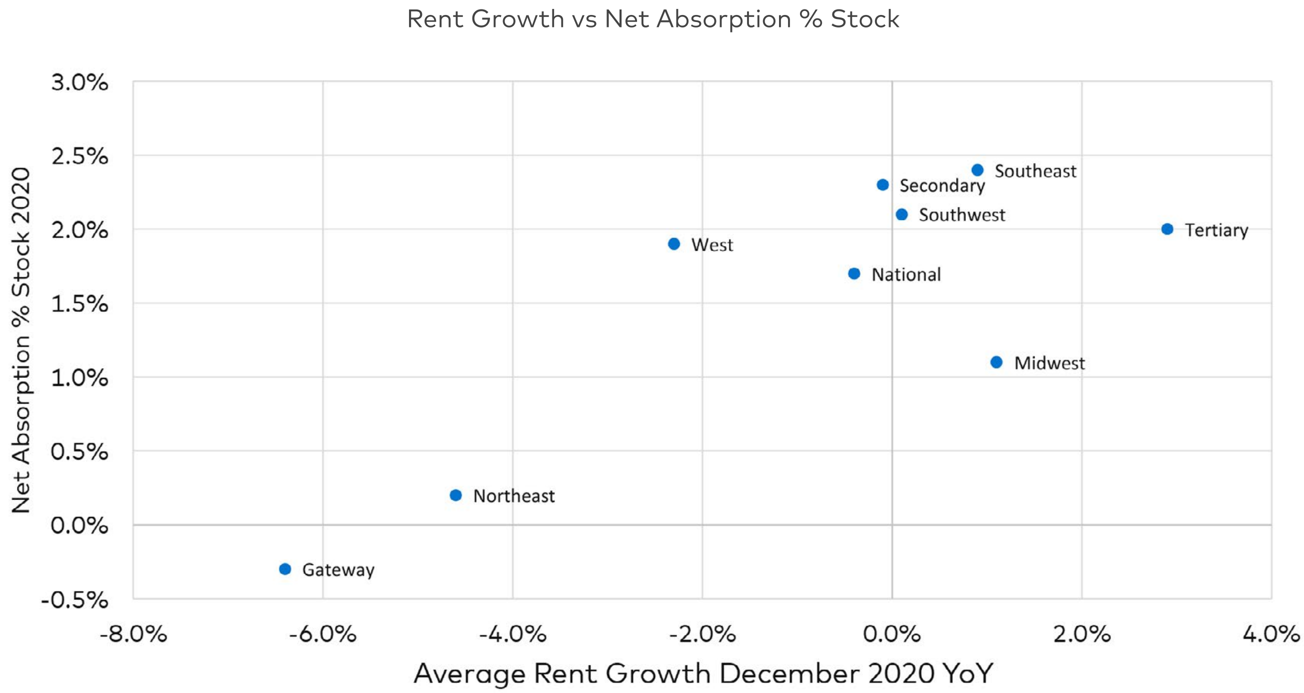


Source: Yardi Matrix

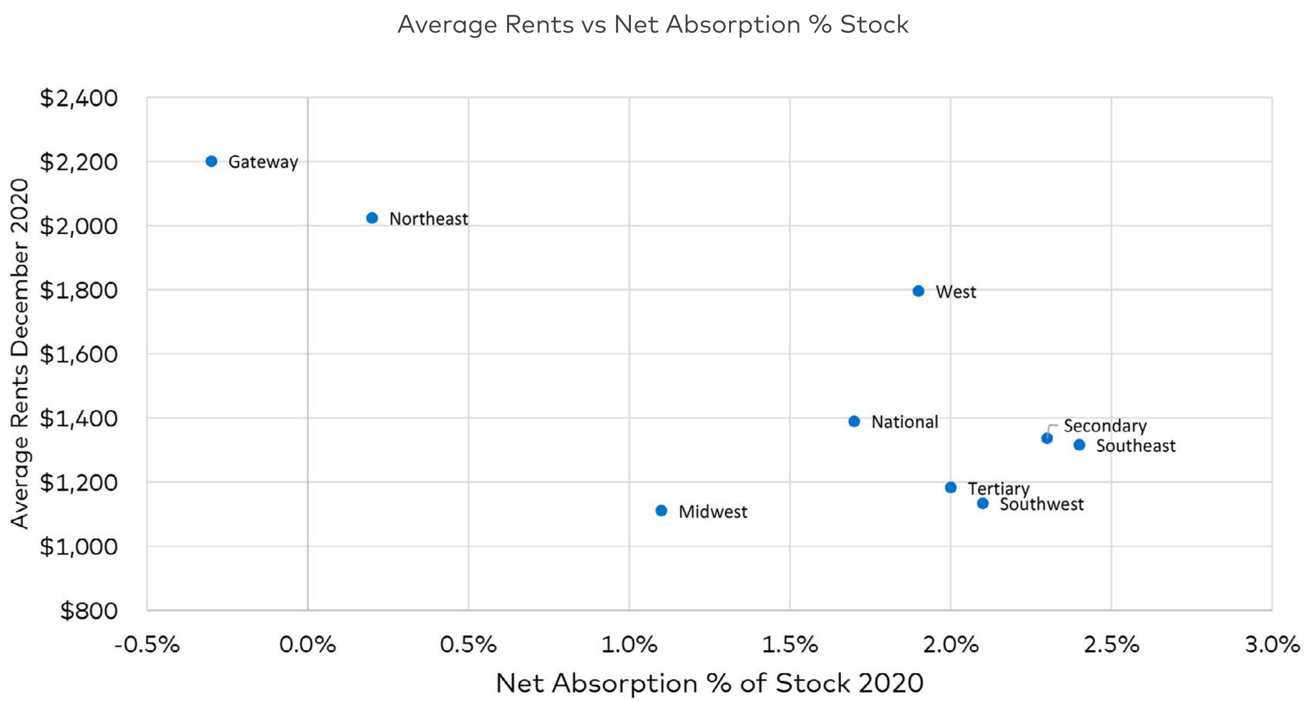
Average Rents vs Net Absorption % Stock



Source: Yardi Matrix



Source: Yardi Matrix



Source: Yardi Matrix