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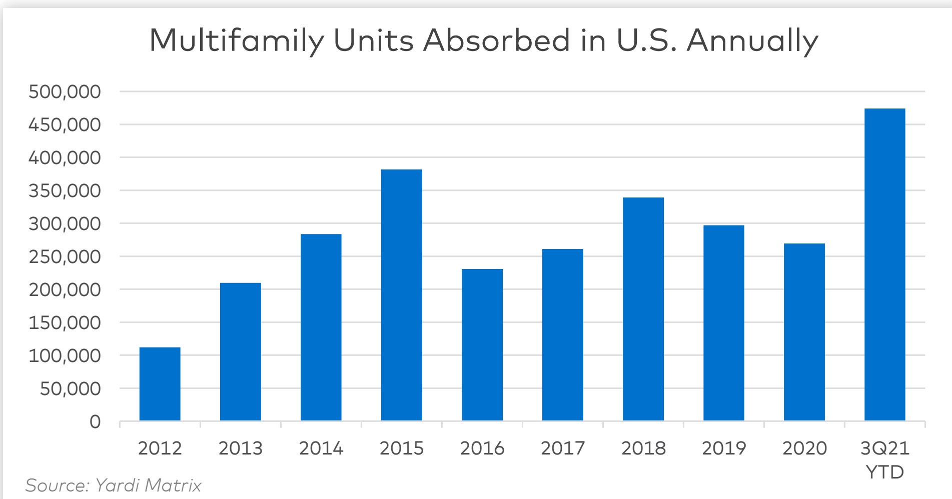
Gateway Market Rebound Heads Record-Setting Multifamily Absorption

After experiencing negative apartment absorption during the pandemic, gateway metros have roared back this year. Amid record-setting demand nationally, gateways led the nation in absorbing multifamily units through the first three quarters of 2021, according to Yardi Matrix.

The exodus of renters from gateway markets during the first few quarters of the pandemic prompted questions about the long-term future of urban markets. Though doubts about the prospects of large urban submarkets remain far from resolved, data indicates that demand for apartments returned as cities reopened services and amenities in 2021.

Demand for rentals in the U.S. this year has been extraordinary. Through three quarters in 2021, 475,000 apartment units have been absorbed in the U.S., already topping 2018's single-year high of 370,000 recorded by Matrix. Demand has also been relentless. At least 100,000 units have been absorbed in each of the last four quarters, which is also a first.



The absorption numbers explain the industry's stellar fundamentals performance. Asking rents nationally were up 11.4% year-over-year through September, while the occupancy rate of stabilized properties rose 110 basis points year-over-year to 95.9% as of August, per Matrix data on 140 markets.

Gateway Rebound

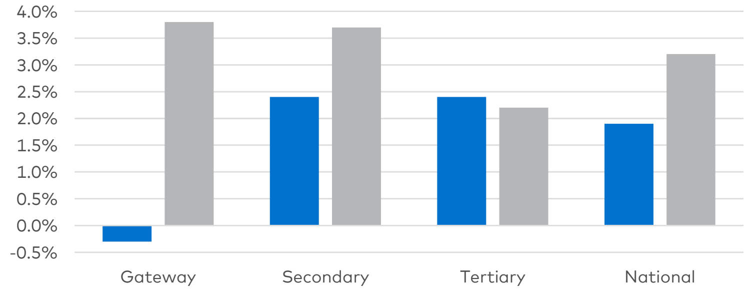
While the bullish apartment performance nationally has been well-documented in recent months, what is startling is the turnaround in gateway performance. Based on absorption as a percentage of stock by market size, gateway markets are on the verge of a "worst-to-first" turnaround. (Absorption is defined as the change in occupied units over time, encompassing move-ins minus move-outs.) Gateway metros (which we delineate as New York City, Boston, Washington, D.C., Miami, Chicago, Los Angeles and San Francisco) absorbed some 108,000 units through the first three quarters of 2021, after posting slightly negative (-7,000) absorption in 2020.

Put another way, gateways have had the most robust absorption in 2021 after being last by a significant margin in 2020. As a percentage of stock, gateway absorption was -0.3% in 2020, compared to 1.9% for the entire U.S. and 2.4% in secondary and tertiary metros. In other words, absorption was relatively normal in most non-gateway metros through the early stages of the pandemic, while gateways suffered occupancy losses.

The story was far different in the first three quarters of 2021, with gateway metro absorption at 3.8% of total stock, compared to 3.2% for all metros. Secondary market absorption was also extremely strong, at 3.7% of stock, while tertiary metros trailed at 2.2% of stock. The data denotes a strong turnaround in gateway metros, while demand never flagged in secondary and tertiary markets.

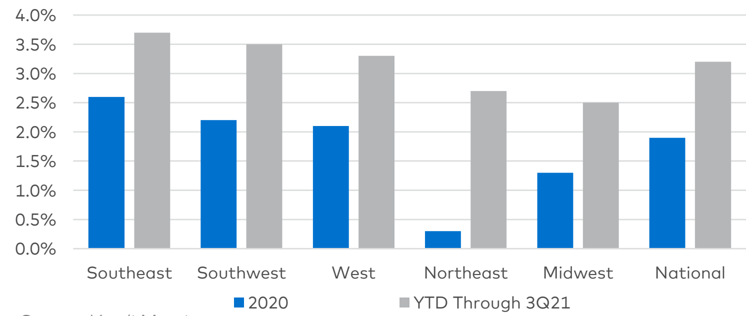
Robust multifamily absorption is driven by a confluence of factors. The economy

Multifamily Absorption as % of Stock by Market Size



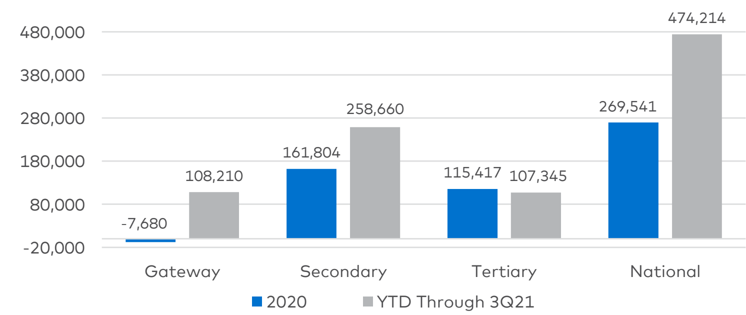
Source: Yardi Matrix

Multifamily Absorption as % of Stock by Region



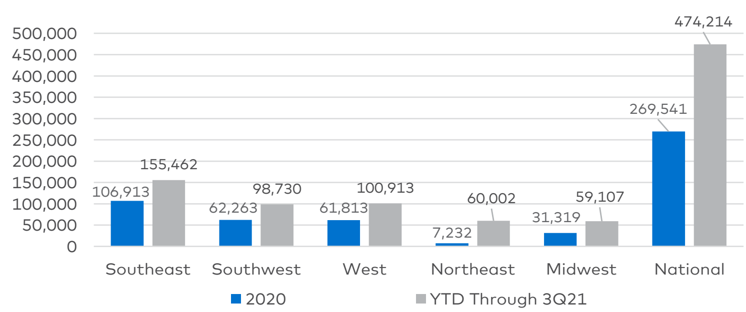
Source: Yardi Matrix

Multifamily Units Absorbed, 2020 vs. 3Q21



Source: Yardi Matrix

Multifamily Units Absorbed, 2020 vs. 3Q21



Source: Yardi Matrix

is set to post its highest GDP numbers in decades, at about 6% for the year. Nearly five million jobs have been added since January, even though total employment remains nearly five million below pre-pandemic levels. There is pent-up demand coming out of the pandemic, and households have strong balance sheets after a year of reduced spending and banking government stimulus checks. Young adults are moving out of their parents' homes and forming their own households.

Plus, there remains a long-term shortage of housing supply, as new construction was stifled for several years coming out of the Great Recession. Single-family home prices have also soared. The 20-city S&P/Case-Shiller Index was up nearly 20% year-over-year through July. A growing number of single-family homes—upwards of 15%, according to some estimates—are being purchased by investors for rental properties and by buyers of second homes.

Amid overall healthy demand for housing, renters are returning to gateway markets. During the pandemic, gateway markets lost some Millennial renters with children looking for housing with more space and/or better schools, renters who work remotely looking for lower-cost housing and those seeking a more suburban or rural lifestyle.

Now units are being backfilled, largely by young workers seeking the experience of city life and downsizing retirees. Although office workers have been slow to return due to the Delta variant, residential sections of the gateway cities are returning to normal faster than business districts as recreation and entertainment open back up.

South, West Metros Lead Growth

Regionally, the Southeast continues to attract the most renters, with 155,000 units absorbed year-to-date, constituting 3.7% of stock. Metros in the West (101,000, 3.3% of stock) and Southwest (98,000, 3.5% of stock) are also attracting a high number of households. The Northeast (60,000, 2.7% of stock) and Midwest (59,000, 2.5% of stock) trail in total absorption, though that performance is healthy compared to historical standards.

Dallas (31,450), Houston (24,891) and Washington, D.C. (20,845) posted the highest number of units absorbed year-to-date through September. Six of the top 10 metros in the country based on 2021 absorption are gateways, illustrating the extent of the rebound. The only gateway not in the top 10 is Boston, which at 4.6% is among the top 10 metros for absorption as a percentage of stock. Six metros posted 5.0% or higher absorption as a percentage of stock year-to-date through September, led by Miami (6.0%), Austin (5.5%), San Jose (5.2%) and San Francisco, Orlando and Charlotte (all 5.0%).

The bounceback in the Bay Area is particularly encouraging. San Francisco and San Jose were—along with Manhattan—the markets that saw the biggest drop in performance during the pandemic. Those three metros share some commonalities. They are among the highest-priced markets in the country, with concentrations of highly paid knowledge workers in the types of jobs that are easiest to perform remotely. New York and San Francisco are among cities with a lag in workers returning to the office.

But the similarities only go so far. Companies that form the bedrock of New York City's economy—the financial industry—have made it clear that they plan to require most employees to work from offices when concerns about health recede. Surveys indicate that the technology industry, which is the dominant industry in the Bay Area, may not be as demanding about bringing employees back to the office full time. In part that's because technology workers are less eager to work in an office, with many feeling they can be just as productive at home.

Absorption by Metro
YTD Through Sept. 2021

Metro	# of Units	% of Stock
Dallas	31,458	3.9%
Houston	24,891	3.7%
Washington DC	20,845	3.8%
New York	19,582	3.4%
Miami	19,134	6.0%
Atlanta	16,988	3.7%
Chicago	16,584	4.6%
Los Angeles	15,891	3.6%
Austin	14,281	5.5%
San Francisco	13,646	5.0%
Seattle	12,144	4.6%
Orlando	11,699	5.0%
Denver	11,530	3.9%
Boston	11,164	4.6%
Phoenix	10,558	3.2%
Twin Cities	10,368	4.5%
Charlotte	9,587	5.0%
San Antonio	8,714	4.1%
Philadelphia	8,203	2.7%
Tampa	7,853	3.4%
Raleigh	7,752	4.6%
Portland	7,198	4.3%
San Jose	6,882	5.2%
Nashville	6,776	4.7%
San Diego	5,378	2.8%
Columbus	4,717	2.6%
Las Vegas	3,921	2.2%
Inland Empire	2,214	1.4%
Pittsburgh	1,401	1.5%
Sacramento	1,301	1.0%

Source: Yardi Matrix

The long-term recovery and growth of gateway markets requires all parts of the cities to be functioning. Lifestyle amenities and employment have worked hand-in-hand to create vibrant 24-hour economies that fueled growth in recent decades. It's still too early to say all is back to normal, though the bounceback in 2021 proves that gateway metros retain appeal as places to live for many demographic groups.

Durable Demand Drivers

Multifamily has benefited from a confluence of factors to produce outstanding fundamental performance in 2021. Some of those factors, such as the above-trend stimulus-fueled economic growth and pent-up demand after a year spent in quarantine, are not sustainable, and the impact will fade in coming quarters.

Other factors, however—including the long-term supply-demand imbalance, an increasing propensity by older and wealthier households to choose to rent instead of owning a house, women having fewer children and giving birth later in life, lifestyle choices of seniors who want to live in urban centers—represent changing social and demographic forces that are likely to drive demand for years to come. There remain many wildcards that include how companies handle work-from-home and flexible office policies, and preferences of younger workers. Although it is far from clear how those trends will be resolved, they hold enormous implications for apartment demand.

On balance, we expect that demand and absorption will moderate in coming quarters as some of the short-term drivers begin to wane, but overall demand is likely to remain elevated through 2022 and beyond due to long-term factors that will continue to drive growth.

Paul Fiorilla, Director of Research

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