

U.S. Multifamily Outlook

Winter 2022

Another Strong Year Expected For Multifamily in 2022

Healthy Economic Growth
Rising Apartment Occupancy
Capital Flowing to Multifamily

Market Analysis

Winter 2022

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Another Year of Bullish Conditions on Tap for Multifamily

- The multifamily market appears poised for another solid year in 2022, although it is not likely to match 2021's unexpected exceptional performance. We anticipate demand for apartments will remain robust, highlighted by strong economic growth and household formation. Meanwhile, capital conditions will be favorable, driven by investors' insatiable appetite for stable income and low mortgage rates.
- U.S. economic growth in 2022 will decelerate from its decade-long high of roughly 6% in 2021 but should remain above trend. The economy is benefiting from lingering monetary stimulus, job growth, higher wages and consumer wealth, while supply-chain issues have continued into 2022. Inflation and the labor shortage are the biggest headwinds, but most of the negative ramifications from those matters won't be felt until 2023 or later.
- After asking rents rose 13.5% nationally in 2021, it's an easy call to forecast a moderation in rent increases. However, we still expect overall U.S. rent growth to reach 4.8% in 2022, well above the long-term 2.7% average. The conditions that drove higher rents in 2021—including pent-up demand coming out of the pandemic, strong job growth, soaring home prices and healthy consumer savings—have not fully subsided.
- Absorption hit record levels in 2021, prompting occupancy rates to flirt with all-time highs. In that light, concerns about oversupply have become moot and builders are ramping up projects. As of the beginning of 2022, more than 750,000 market-rate apartment units were under construction. After 350,000 units delivered in 2021, we expect about 385,000 to 400,000 more in 2022.
- The amount of investment capital chasing multifamily, both equity and debt, is enormous. Property values are rising rapidly, driven by lower acquisition yields and increases in net income as asking rents shoot higher. Some \$166 billion of multifamily transactions were completed in 2021, up 75% from 2020, and the only limit is the number of properties put up for sale. Debt availability is also robust, led by Fannie Mae and Freddie Mac, which have increased capital allocations in 2022. Multifamily debt has also driven record levels of lending by private equity funds.

Healthy Economic Outlook

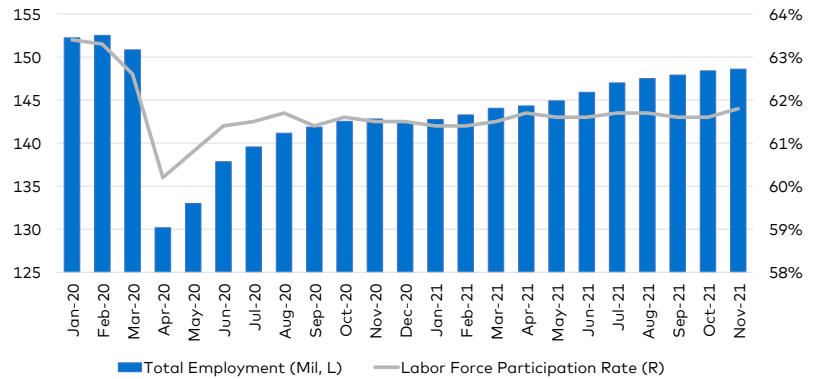
Underpinning multifamily performance is the economy, which grew by 6% in 2021, the highest rate in 40 years, driven by federal government stimulus and the increase in consumer wealth. While growth will almost certainly decelerate in 2022, the outlook for the economy remains bullish.

Evercore ISI, for example, forecasts real GDP growth of about 4.0% in 2022 (with some omicron-induced choppiness in Q1), which would be among the best performance in recent decades. Evercore's growth forecast is based on factors that include ongoing massive monetary stimulus, higher wages, the unprecedented surge in consumer wealth and savings, the economy continuing to reopen, the easing of supply chain issues, and strong corporate profits. The U.S. economy added 6.4 million jobs in 2021, putting the country on track to reach its pre-pandemic job totals in late 2022 or 2023.

However, there are headwinds, among them that labor force participation remains weak in part due to the "Great Resignation." Getting a taste of being home, some workers retired early, while others have remained out of the workforce due to fear of COVID, or the need to care for a child or elderly relative.

Others decided to quit low-paying jobs with poor working conditions. Combined with reduced immigration in recent years, that has created a shortage of workers in many industries, including technology, construction and services. The number of job openings topped 10 million in late 2021. Growth will slow rather quickly unless companies can find workers to fill positions.

Total U.S. Employment, Labor Participation



Source: Bureau of Labor Statistics

Another consequence of the labor shortage is that employers have been forced to raise wages significantly to attract workers. The U.S. unemployment rate dropped to 3.9% in December 2021, and wages increased by a hearty 4.7% for the year. Higher wages put money in consumers' pockets, helping them to afford rapidly rising rents.

How much of a good thing is too much, though? The soaring economic growth brought with it an outbreak of inflation that could prove damaging to the economy over the long haul. Inflation rose about 7% in 2021, the highest level since the early 1980s. Inflation skyrocketed in goods and services. As the economy reopened in 2021, consumers had several trillion dollars of excess savings and pent-up demand to buy durable goods and services. The resulting explosion of spending—core retail sales were up 16.5% year-over-year in November 2021—strained the supply chain, leading to backlogs at ports and shipping delays.

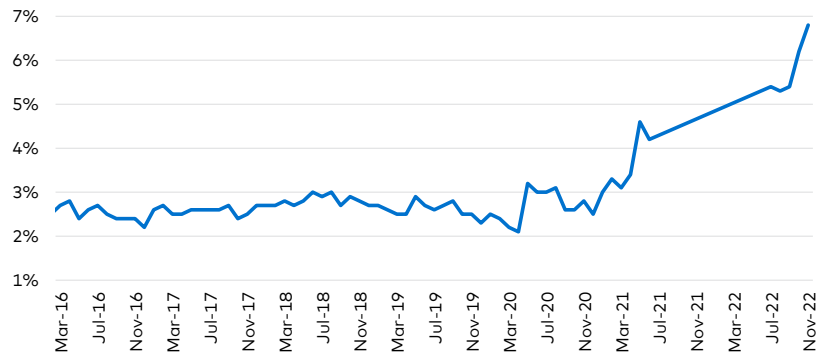
Given that inflation was below the Federal Reserve's 2% target through most of the last economic cycle, a short bout of higher costs would not be alarming. But the level and persistence of inflation have moved beyond the so-called transitory stage, leading to worries that prices will spiral out of con-

control, or that the Fed will be prompted to take action that would choke growth and lead to a recession. After trying to downplay the inflationary environment for most of the year, Fed chairman Jerome Powell in December announced steps to reduce growth that include a tapering of asset purchases to lower the agency's \$9 trillion balance sheet and plans to hike the federal funds rate three times in 2022. It remains to be seen whether these actions can produce the desired inflationary soft landing.

While few expect inflation to recede to the Fed's target level soon, the prognosis and severity are debated. Optimists say that inflation will gradually ease. In this view, the impact of the stimulus is abating, while energy prices will level off or decline. Meanwhile, the supply-chain disruptions are receding, and consumer spending will normalize as the pent-up spending runs its course. Finally, wage growth will moderate as people who left the labor force during the pandemic return and ease the shortage of workers, especially for service jobs.

When inflation does run high, commercial real estate is arguably one of the better investment

Consumer Price Index (% Change YoY)



Source: Bureau of Labor Statistics

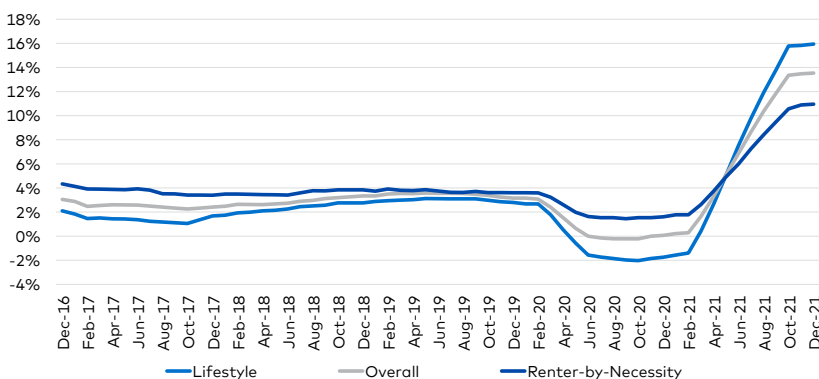
vehicles. Commercial and multifamily property are believed to serve as a hedge against inflation, because rents and values tend to rise in an inflationary environment. A recent study by the Pension Real Estate Association found that commercial real estate performance has been good during periods of high inflation and that returns are much more closely correlated to growth than inflation. The full impact of inflation on the U.S. economy will depend on how severe it remains and how long it persists. Whatever the eventual impact, multifamily investors should prepare and act accordingly.

Rent Growth to Moderate

Following what has been a banner year for the multifamily industry, when national asking rents were up 13.5%, 2021 ended on a note of much-expected deceleration. Although growth will moderate in 2022, we expect that gains will remain above trend, with average asking rents increasing by 4.8% nationally during the year.

Growth has been driven by extraordinary demand, as more than 400,000 multifamily units were

U.S. Multifamily Rents



Source: Yardi Matrix

absorbed in 2021, about 50% more than recorded by Yardi Matrix in any previous year. Dynamic demographic trends due to increased mobility amid widespread availability of work-from-home options have pushed absorption to new highs. Despite a solid year for deliveries nationwide, occupancy levels increased in 2021, topping 96.0% through the second half of the year.

Demand should remain robust in 2022. More than 10 million jobs are still unfilled, so job growth should stay strong. Wage growth is high, and consumer balance sheets are healthy, which provides the financial wherewithal to create distinct households and pay higher rents. Some households will continue to be frozen out of homeownership by house prices, which increased by 20% in 2021. Mortgage rates are likely to rise in 2022, which also makes renting more competitive. Plus, the ongoing migration of population to secondary and tertiary markets in the South and West will funnel demand into areas that have grown rapidly in recent years.

At the same time, there are factors that will restrain rent growth to more moderate levels. Most of the pent-up demand from 2020, when people sheltered in place, was expended in 2021. Another moderating factor is inflation, as rents and other expenses have risen faster than wages. A wild card is new waves of the COVID-19 virus, which limit economic growth and mobility.

Rents nationally rose by record levels in 2021, but on a metro level, growth was driven by affordable secondary markets in the Southeast and Southwest—Phoenix, Tampa, Jacksonville, Orlando—that drew from migration during the pandemic.

Residents moving between metros looking for more cost-effective options and more value for their dollar have exacerbated what had already been a significant boost for Sun Belt metros, which

2022 Forecast Rent Growth by Metro

Metro	YoY Rent Forecast 2022	Average Rent as of December 2021
National	4.8%	\$1,594
Tampa–St. Petersburg	6.6%	\$1,676
Raleigh-Durham	6.5%	\$1,493
San Francisco	6.5%	\$2,647
Atlanta	6.2%	\$1,627
Phoenix	6.2%	\$1,618
Orlando	6.1%	\$1,665
Denver	5.9%	\$1,784
Miami	5.8%	\$2,133
Los Angeles	5.6%	\$2,402
San Jose	5.5%	\$2,790
Charlotte	5.4%	\$1,481
Jacksonville	5.4%	\$1,447
Charleston	5.1%	\$1,516
Seattle	5.1%	\$2,048
Austin	5.0%	\$1,677
Chicago	4.7%	\$1,697
New York	4.7%	\$3,905
Boston	4.3%	\$2,514
Houston	4.3%	\$1,243
Richmond	4.0%	\$1,345
Dallas	3.6%	\$1,424
Kansas City	3.6%	\$1,102
Philadelphia	3.5%	\$1,595
Washington, D.C.	3.4%	\$1,958
Twin Cities	3.3%	\$1,415

Source: Yardi Matrix

will continue to drive rent improvement in these markets, albeit at a more sustainable rate than in 2021.

With rapid population growth and robust economic development, the Southeast placed many metros near the top of our 2022 rent forecast, including Tampa (6.6%), the Southwest Florida Coast (6.6%), Raleigh-Durham (6.5%), Atlanta (6.2%) and Orlando (6.1%).

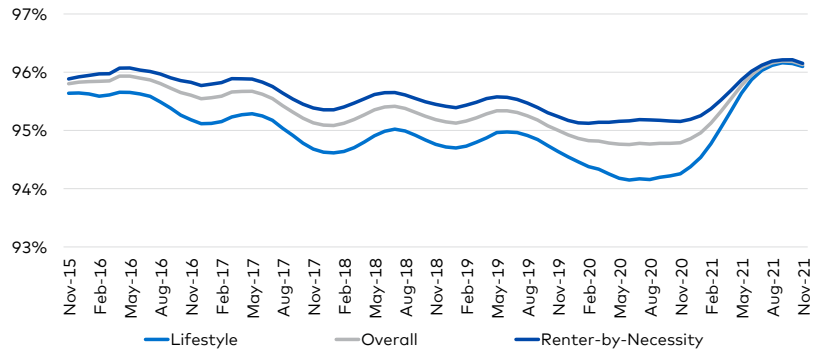
The Bay Area is expected to turn a corner in 2022: San Francisco (6.5% rent forecast) and San Jose (5.5%) are two of only six metros nationally in which average asking rents declined during the pandemic. Demand is recovering in both markets, as the occupancy rate of stabilized properties rose 2.5 percentage points year-over-year through November in San Jose and 2.0 percentage points in San Francisco.

Other Western metros among the top for 2022 forecast rent growth include Las Vegas (6.5%), San Diego (6.4%), Phoenix (6.2%), the Inland Empire (6.1%), Sacramento (6.0%), Los Angeles (5.6%) and Salt Lake City (5.6%). Major secondary markets will continue to perform well, but more sustainable growth will be the name of the game in 2022, as the rental market settles.

Demand to Boost Supply Growth

After a very strong start in 2021, due in part to delays in projects that were slated to come online in 2020, the market ended 2021 with more than 350,000 units delivered. With 2022 set to continue multifamily development's hot streak, we expect some 380,000 units to come online by year's end, increasing inventory by 2.5%.

U.S. Occupancy Rate



Source: Yardi Matrix

Extended construction timetables have been a fixture for the industry, as labor shortages and continued cost increases have prolonged development timelines during the second half of the cycle. Coupled with pandemic-driven restrictions and supply-chain disruptions, construction was expected to be a problematic topic for the industry. Instead, increased resident mobility and job recovery have pushed demand in Sun Belt markets, keeping developers in these markets active throughout the pandemic.

As we begin 2022, more than 800,000 multifamily units of all types are under construction in the U.S., and we expect starts to be maintained at a steady rate. While demand for more exists and capital is available, continuing supply constraints (rising costs, labor/material disruptions and regulation) will limit expansion, and thus enable the multifamily growth in rents to continue.

Concerns about overbuilding in some metros have been alleviated by the significant increase in demand. Despite a consistent rate of deliveries over the past few years and supply concerns in several markets, occupancy rates of stabilized properties have risen to near all-time highs. The national occupancy rate in stabilized properties rose by nearly 100 basis points last year, leading to skyrocketing rents and the addition of several projects to the pipeline.

The gap in occupancy rates between Lifestyle and Renter-by-Necessity assets began 2021 at 70 basis points, but the strong demand for up-scale units throughout the year had almost nullified the difference, which shrank to 10 basis points as of November. However, with most projects in the pipeline geared at the upscale segment, that gap may widen again.

On a metro basis, Dallas is once again likely to lead multifamily development, with nearly 20,000 units expected to come online in 2022, a 2.4% increase in stock. The metro also led all markets in 2021 deliveries with 23,000. Austin (17,800 units, 6.5%) and Phoenix (15,800 units, 4.8%) round out the top 3 U.S. metros for expected completions due to migration and corporate relocations into the Southwest, coupled with easier development approvals. At 6.5%, Austin is projected to have the highest increase in stock in 2022. Charlotte, another fast-growing secondary market, is set to add 9,400 units this year, accounting for 4.8% of existing stock.

Gateway markets will enjoy varying levels of deliveries in 2022. Miami, which added 16,000 units in 2021, is projected to add another 15,000 units in 2022. Los Angeles (13,200 units) and New York City (11,900 units) have significant pipelines for 2022. Chicago, with 4,700 units set to come online this year, or 1.3% of stock, trails its gateway peers, even though demand rebounded in 2021. Year-over-year through November, New York's occupancy rate increased by 3.2 percentage points while Chicago's increased by 2.9 percentage points.

2022 Forecast Supply Growth by Metro

Metro	2022 Forecast Deliveries	2022 Forecast Deliveries as a % of Inventory
National	378,720	2.5%
Dallas	19,927	2.4%
Austin	17,824	6.5%
Phoenix	15,893	4.8%
Miami	15,053	4.6%
Houston	13,651	2.0%
Los Angeles	13,243	2.9%
New York	11,920	2.1%
Washington, D.C.	11,842	2.1%
Orlando	11,373	4.7%
Denver	11,345	3.8%
Seattle	10,522	3.9%
Boston	9,562	3.9%
Charlotte	9,410	4.8%
San Francisco	8,348	3.0%
Atlanta	8,058	1.7%
Twin Cities	7,978	3.4%
Tampa-St. Petersburg	7,693	3.3%
Richmond	6,656	2.9%
Raleigh-Durham	5,516	3.3%
Jacksonville	5,219	4.8%
Philadelphia	4,862	1.6%
Chicago	4,787	1.3%
Kansas City	3,896	2.3%
San Jose	3,441	2.6%
Charleston	2,396	3.2%

Source: Yardi Matrix

Capital Markets: Favorable Conditions

Multifamily's capital conditions could scarcely be more favorable as we enter 2022. After a brief dip in commercial real estate market activity in the spring of 2020, the market came roaring back in 2021 and has resumed its place as a favorite asset class of investors. Transaction activity and pricing have reached all-time highs, while debt is plentiful and cheap. The biggest worry is that prices are rising too much, too fast, but the positive performance mitigates some of those concerns.

Multifamily transaction activity reached \$166.8 billion in 2021, on track to top 2019's pre-pandemic high-water mark of \$128.6 billion, according to Matrix. Price per unit also reached an all-time high, at \$188,000 surpassing the previous high of \$157,000 in 2020. Practically the only limit to deal flow is how many sellers are willing to put properties on the market.

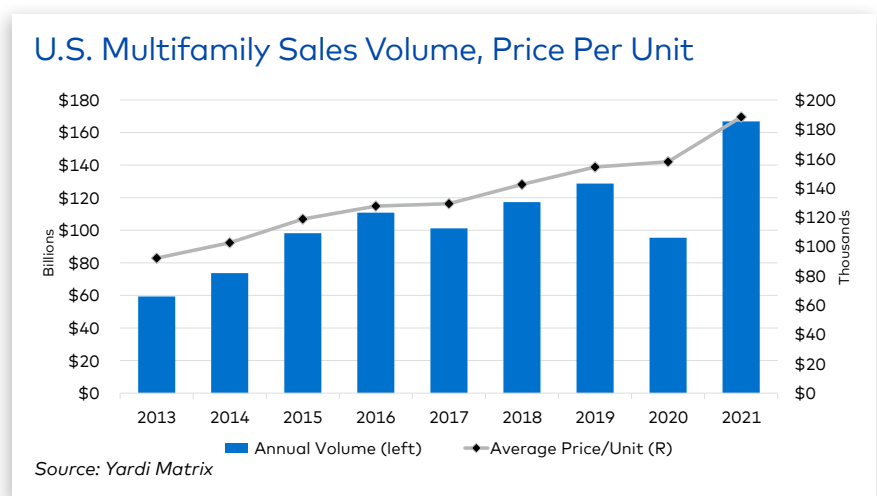
On the debt side, the story is much the same. The multifamily government-sponsored enterprises Fannie Mae and Freddie Mac floated a record \$130 billion of CMBS, according to "Commercial Mortgage Alert" (CMA), while other types of lenders are also actively competing for multifamily originations.

The red-hot market reflects the cascade of capital looking to invest in commercial properties, with multifamily and industrial as the most favored. Investor demand is driven by the impressive fundamental performance of multifamily, along with the belief that supply-demand balance is likely to remain robust in coming years.

Strong capital conditions are not new. Indeed, the capital markets have been healthy for most of the post-Global Financial Crisis economic cycle. Multifamily sales volume and pricing rose steadily for years until the spring of 2020, when COVID-19 lockdowns started. After a few tepid months, deal flow began picking up again in many regions, with gateway metros the slowest to recover.

Apartment demand, however, came back full steam in 2021, leading to a surge in transactions. Buy-and-hold investors see multifamily as a stable asset class with potential growth in net operating income as rents continue to rise. Value-add investors are on the prowl for B- and C-level assets that can be renovated and re-leased at higher rates and then resold. Investors are particularly looking for assets in growing secondary and tertiary markets that are poised to see outsize growth in population and employment in coming years. Although demand for stable assets in gateway markets remains strong, many institutional investors are broadening their geographic scope and outbidding local investors for assets in secondary and even tertiary markets.

The fierce competition for assets means that prices are on the rise. Acquisition yields, or capitalization rates, continue to decline. Acquisition yields



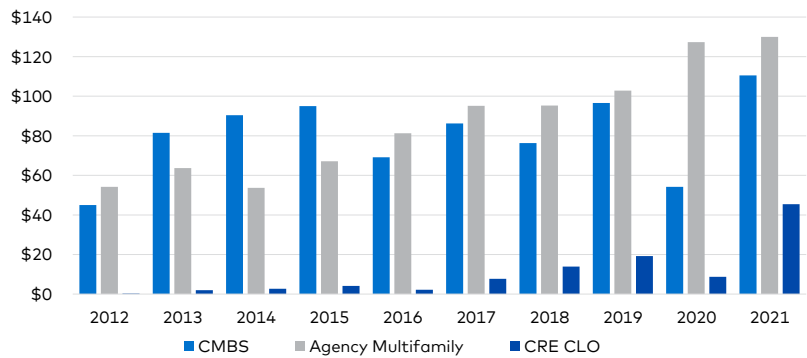
for all multifamily properties average sub-5%, and Class-A assets in in-demand markets are selling in the 4% range, or sometimes the 3% range.

Low-cost debt is one of the drivers of the price appreciation. Mortgage coupons are in the 3% range for most properties. Mortgage demand is high. Borrowers want to take advantage of rock-bottom interest rates (that are bound to rise as the Federal Reserve hikes policy rates in 2022). Plus, there is a rush to finance value-add multifamily properties.

Fannie Mae and Freddie Mac continue to be the leading multifamily financing vehicles. The agencies securitized a combined record \$129.6 billion of mortgages in 2021, topping 2020's record \$127.3 billion, per CMA. Fannie and Freddie each received an extra \$8 billion in allocations this year, bringing their total to \$78 billion apiece. With an administration more favorable to their mission in charge, talk of reform has died down, although the agencies are required to focus half of their allocations on financing properties with an affordable component.

One of the surprising developments in multifamily in 2021 was the growth of private equity floating-rate mortgages that were originated via collateralized loan obligation (CLO) vehicles, which encompass pools of short-term loans on non-stabilized properties. CLO volume of \$44.5 billion

CRE Securitization Volume (Bil)



Source: Commercial Mortgage Alert

in 2021 far surpassed the previous annual high-water mark of \$19.2 billion, set in 2019, according to CMA. Some 70% of CRE CLO volume (\$31.7 billion) was backed by multifamily.

What is driving the rush to CLO financing? With interest rates so low and risk spreads so tight, borrowers might normally want to lock in low rates for long periods at fixed coupons, but many are opting to take out short-term floating-rate loans with the expectation that rates will remain low and they can refinance with higher proceeds. Others are choosing variable-rate loans while properties recover from the pandemic.

We have every reason to believe, and expect, another two years of growth, until interest rate and monetary policy tightening designed to rein in inflation induce a recession in either 2024 or 2025.

Definitions

Lifestyle households (renters by choice) have wealth sufficient to own but have chosen to rent. Discretionary households, most typically a retired couple or single professional, have chosen the flexibility associated with renting over the obligations of ownership.

Renter-by-Necessity households span a range. In descending order, household types can be:

- A young-professional, double-income-no-kids household with substantial income but without wealth needed to acquire a home or condominium;
- Students, who also may span a range of income capability, extending from affluent to barely getting by;
- Lower-middle-income (“gray-collar”) households composed of office workers, policemen, firemen, technical workers, teachers, etc.;
- Blue-collar households, which may barely meet rent demands each month and likely pay a disproportionate share of their income toward rent;
- Subsidized households, which pay a percentage of household income in rent, with the balance of rent paid through a governmental agency subsidy. Subsidized households, while typically low income, may extend to middle-income households in some high-cost markets, such as New York City;
- Military households subject to frequency of relocation.

These differences can weigh heavily in determining a property’s ability to attract specific renter market segments. The five-star resort serves a very different market than the down-and-outer motel. Apartments are distinguished similarly, but distinctions are often not clearly definitive without investigation. The Yardi® Matrix Context rating eliminates that requirement, designating property market positions as:

Market Position	Improvements Ratings
Discretionary	A+ / A
High Mid-Range	A- / B+
Low Mid-Range	B / B-
Workforce	C+ / C / C- / D

The value in application of the Yardi® Matrix Context rating is that standardized data provides consistency; information is more meaningful because there is less uncertainty. The user can move faster and more efficiently, with more accurate end results.

The Yardi® Matrix Context rating is not intended as a final word concerning a property’s status—either improvements or location. Rather, the result provides reasonable consistency for comparing one property with another through reference to a consistently applied standard.

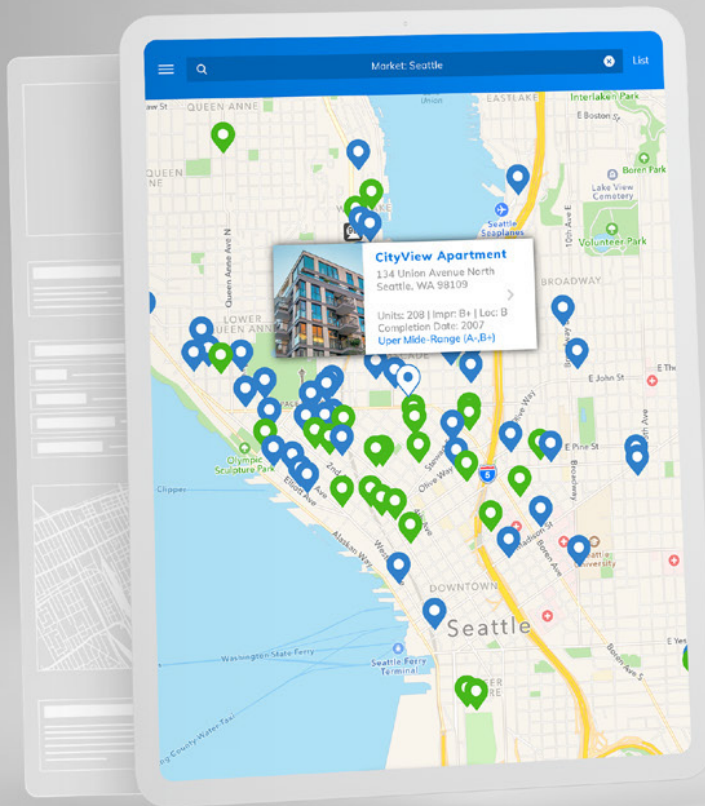
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