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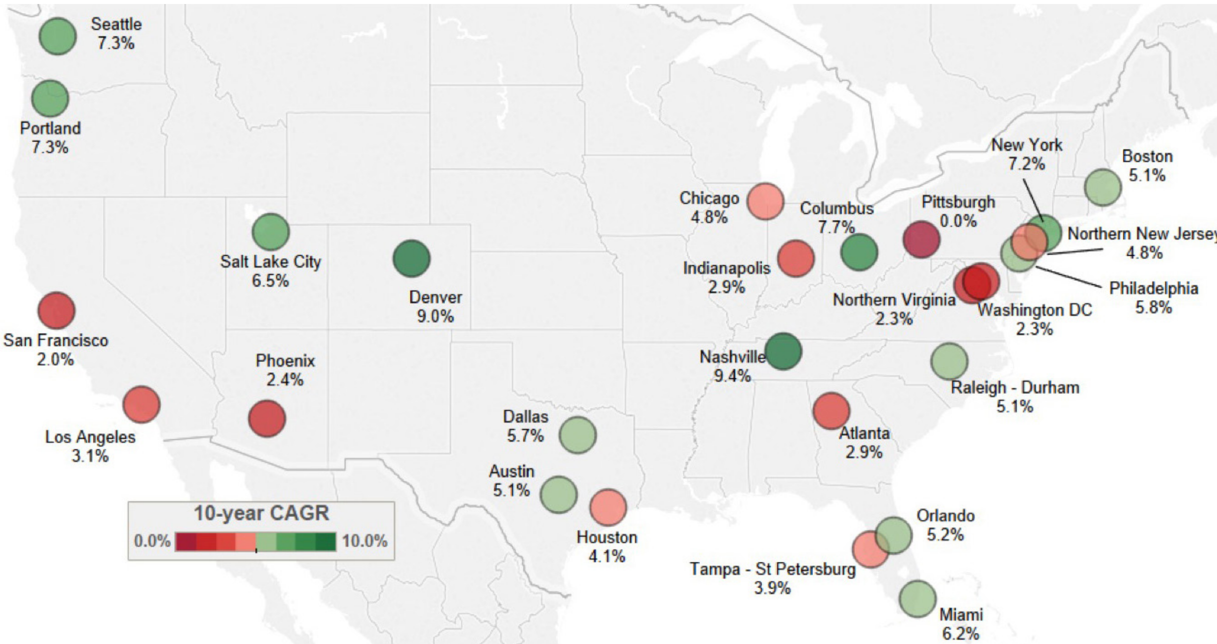
Today's Multifamily: A Game for Sharpshooters

Yardi Matrix Vice President Jeff Adler, joined by host Jack Kern, director of institutional research, presented the semiannual Multifamily Market Update webinar Thursday afternoon. The webinar addressed how the commercial real estate industry is performing, what can be expected over the next couple of years, and why.

Key Points:

- The U.S. economy is in very good shape
- Wages are rising and the labor market is tight
- Inflation is rising, but slowly, and short-term interest rates are up
- A downturn could come around 2020-2021; watch the yield curve
- Multifamily demand is strong and shifting to lower-cost cities
- Tech hubs are emerging both in formerly non-tech metros and traditionally overlooked cities
- There are a handful of markets at risk of oversupply over the next two years

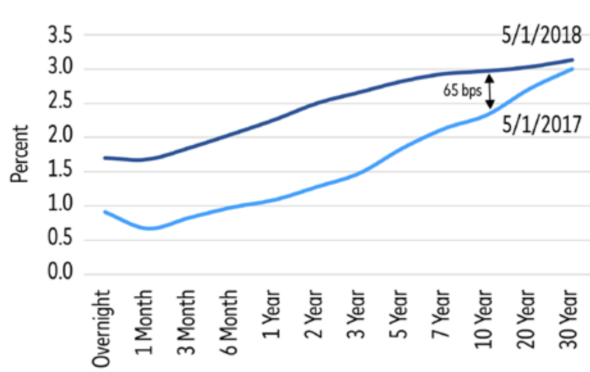
Long-Term Valuations Outperformed in Secondary Markets Since 2008



**Multi-family sales price per unit CAGR: 2008-2017. Values are not "same-store" sales; subject to mix shifts. Source: Yardi Matrix; Tableau*

According to Adler, the U.S. economy is in very good shape. GDP growth has been decent, and factors driving GDP show further signs of growth to come. Employment is up, and with such a tight labor market, people are being pulled off the sidelines. Inflation is rising but unlikely to break 2.5 percent, and short-term interest rates are up, as well. Adler outlined five signs that presage a recession, but concluded that until the yield curve inverts, there is no need to worry, and he doesn't anticipate this happening until 2020-2021.

U.S. Treasury Yield Curve



Source: U.S. Department of the Treasury

As Adler narrowed his focus to the multifamily market, he noted that the sector is now facing increasing crosswinds. Demand remains strong, but this late in the cycle it is shifting to lower-cost cities driven by job and population growth. As Adler put it: "It's a sharpshooter's game for the next few years."

Secondary markets, particularly those with a known tech presence, have been outperforming gateway markets. Cost advantages and emerging intellectual hubs are shifting the geography of jobs, and tax reform will likely accelerate these trends. Although it takes time to become an established tech city, a number of markets are in the early stages of this process now and were noted by Amazon as dark horse options for the company's second headquarters.

New supply, said Adler, will be the key variable to pay attention to over the next few years. New supply is flattening but not declining as much as he previously thought. A handful of markets—including Denver, Seattle, Charlotte, Dallas, Phoenix and Miami—are at risk of oversupply in the short term, and as supply outpaces demand in some markets, the importance of location selection within markets and submarkets will increase.

Overall, Adler's point of view is that the economy is in very good condition, and although multifamily fundamentals are favoring secondary and tertiary markets, these locations are more volatile during downturns, which may be coming in a few years. Supply-demand imbalances in a handful of markets are points of concern, increasing the importance of location selection and indeed making the multifamily market a "sharpshooter's game" over the next few years.

—**Meeghan Fuhr,** *Senior Research Analyst*