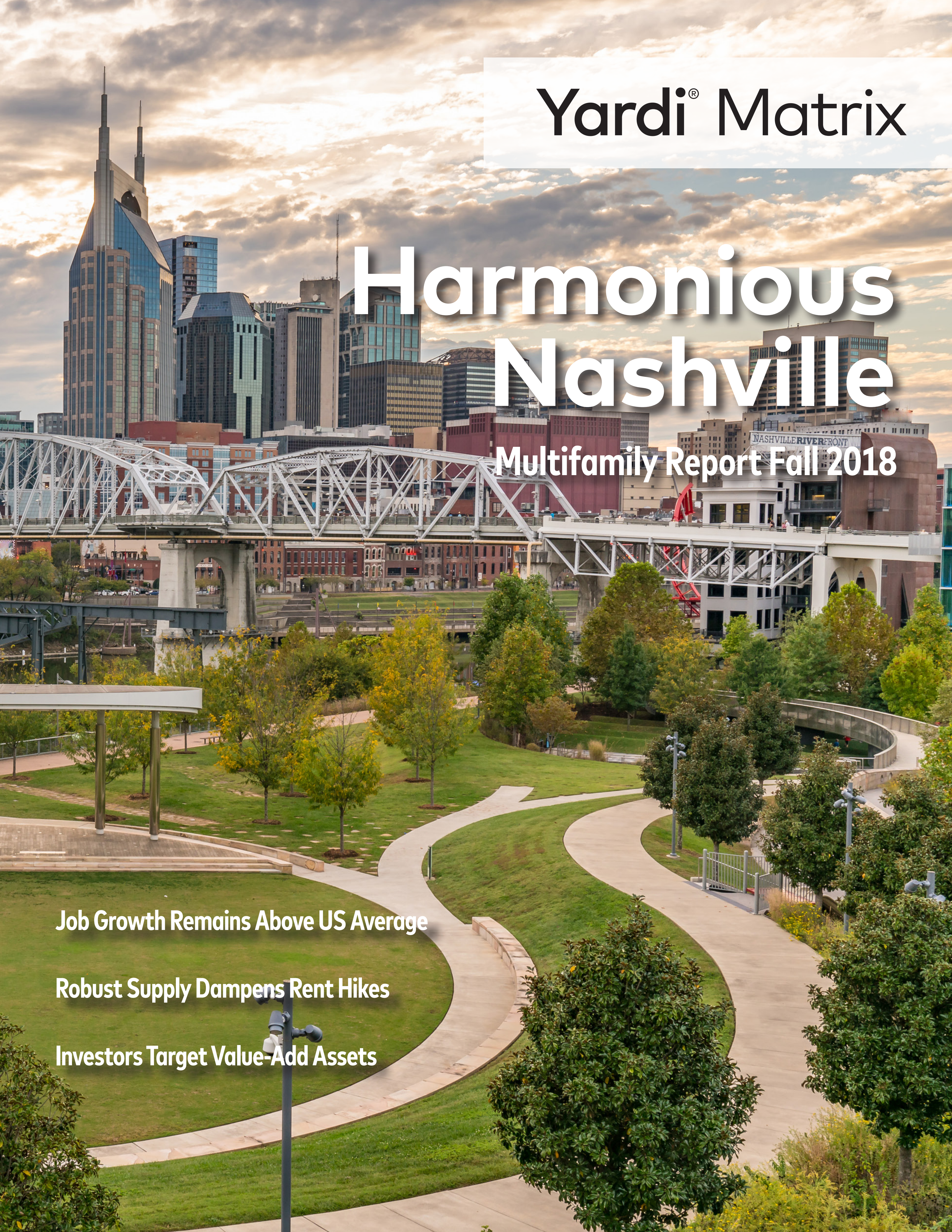
Yardi® Matrix

# Harmonious Nashville

## Multifamily Report Fall 2018




Job Growth Remains Above US Average

Robust Supply Dampens Rent Hikes

Investors Target Value-Add Assets

## Market Analysis

Fall 2018

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# Strong Supply Keeps Rent Growth in Check

Nashville has seen dramatic changes over the past decade, its strong employment and population growth placing the metro among the country's fastest-growing economies. Growth is decelerating, but rates continue to advance despite strong development, with the average rent reaching $1,216 as of August. However, as the bulk of the current development pipeline consists of upscale projects, rents at the upper end of the spectrum are likely to contract further, dampening overall growth.

Economic growth remains relatively strong but is spotty, with three employment sectors contracting by a total of 4,800 jobs. Professional and business services led gains by adding 8,700 positions, up 5.4% year-over-year through June. This is mainly due to corporate expansions and relocations—Philips signed a new lease for 107,700 square feet at Bank of America Plaza and AllianceBernstein is relocating its New York headquarters to Nashville, along with 1,050 employees.

Some $541 million in multifamily assets traded in 2018 through July. More than three-quarters of sold communities were value-add, which has pulled down the average per-unit price to $121,299. As the 4,000 units delivered by August and another 10,000 underway are bound to keep demand in check, we expect the average Nashville rent to rise 1.8% this year.

### Recent Nashville Transactions

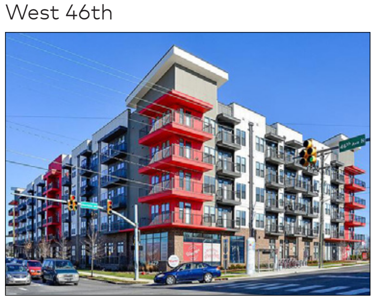
Panther Creek Parc

City: Murfreesboro, Tenn.
Buyer: Michelson Organization
Purchase Price: $58 MM
Price per Unit: $166,236

The Hamptons at Woodland Pointe

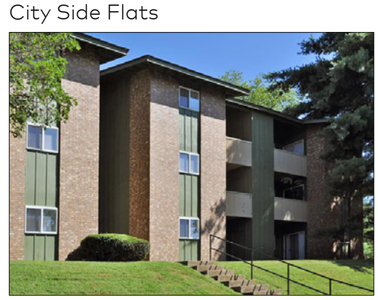
City: Nashville, Tenn.
Buyer: Security Properties
Purchase Price: $45 MM
Price per Unit: $188,646

West 46th



City: Nashville, Tenn.
Buyer: Venterra Realty
Purchase Price: $34 MM
Price per Unit: $198,830

City Side Flats



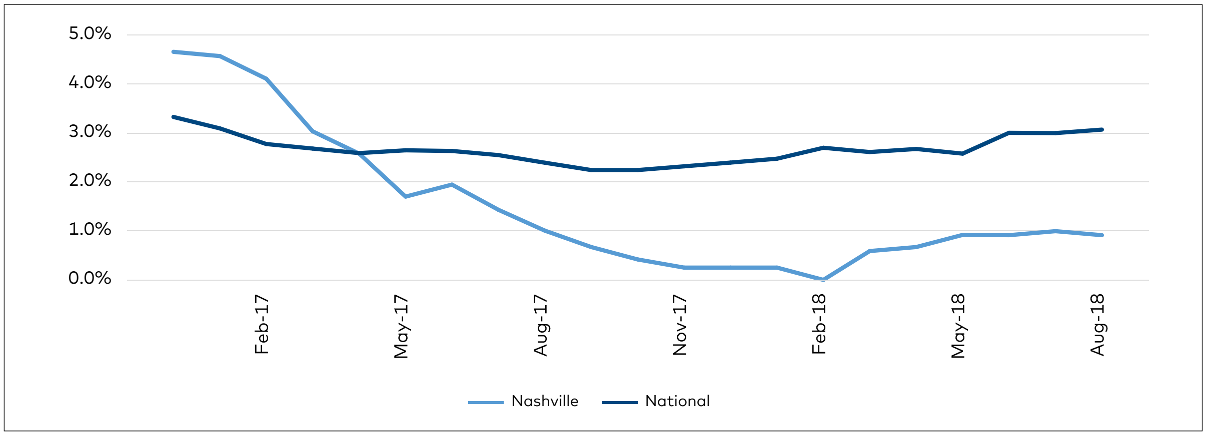
City: Nashville, Tenn.
Buyer: Emma Capital
Purchase Price: $25 MM
Price per Unit: $122,139

On the cover: Photo by pabradyphoto/iStockphoto.com

## Rent Trends

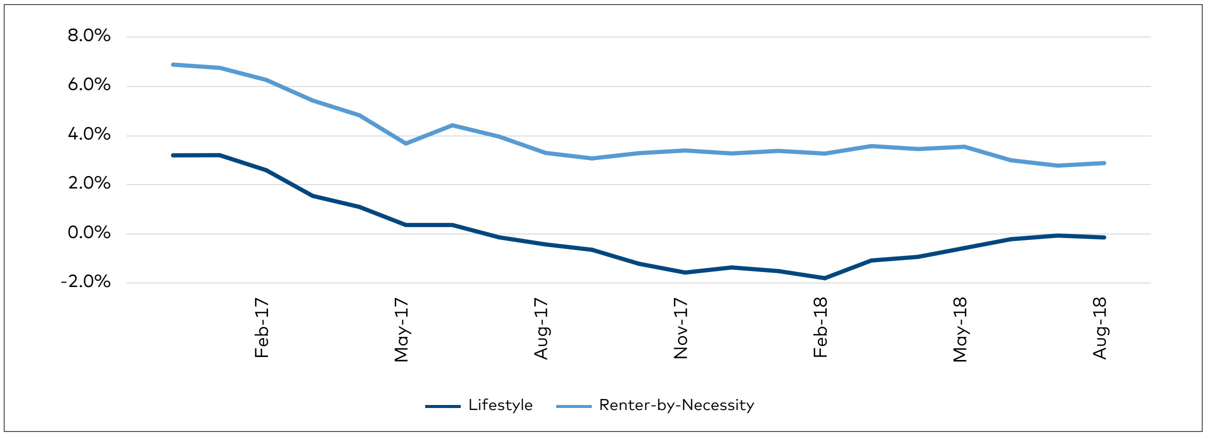
- Nashville rents rose 0.9% year-over-year through August to $1,216, nearly $200 below the national average. Rent growth in the metro decelerated and remained tepid over the past year and a half, mostly due to the robust inventory injected in the housing stock—almost 17,000 new units since January 2016.
- Rents in the working-class Renter-by-Necessity segment led growth, up 2.9% year-over-year to $1,001. Rates for Lifestyle assets contracted 0.1%, to $1,391. As the development pipeline consists mainly of lifestyle projects, this trend is likely to continue.
- Rent growth was spotty, with rates contracting in about a quarter of the metro's submarkets over the 12 months ending in August. Downtown–South registered the steepest drop (-8.5% to $1,253), followed by distant Ashland City (-3.8% to $1,018) and Midtown/Music Row (-3.4% to $1,740). Southeast–West, where all communities were developed before 2000, is the metro's most affordable submarket, with an $860 average rate. The most expensive areas in Nashville are Downtown–North ($1,741) and Midtown/Music Row ($1,740). Rents stayed flat in Murfreesboro–South, at $1,026.
- As population and job growth continue to fuel demand while heavy levels of new supply are keeping rent hikes in check, we expect Nashville rates to appreciate 1.8% in 2018.

**Nashville vs. National Rent Growth** (Sequential 3 Month, Year-Over-Year)




Source: YardiMatrix

**Nashville Rent Growth by Asset Class** (Sequential 3 Month, Year-Over-Year)




Source: YardiMatrix

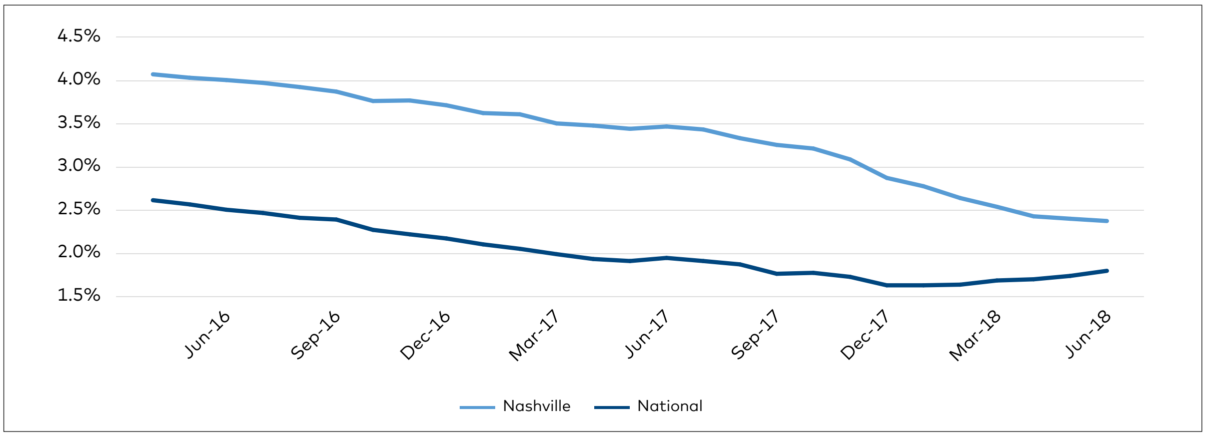
## Economic Snapshot

- Nashville's employment growth is decelerating but is far from stopping. The metro added 20,600 jobs in the 12 months ending in June, up 2.4% year-over-year and 60 basis points above the national rate. The unemployment rate rose to 3.2% in June but remained significantly below the U.S average.

- Growth was uneven, with three sectors—information, manufacturing and mining, logging and construction—contracting by 4,800 jobs combined. The professional and business services sector led growth, adding 8,700 positions.

- The sector is fueled by corporate expansions and relocations brought by the metro's solid pipeline of talent, favorable business costs and overall quality of life. Philips signed a new lease for 107,700 square feet at Bank of America Plaza, Southwestern Investment Services leased nearly 30,000 square feet at Five Corporate Center in Cool Springs and AllianceBernstein is relocating its New York headquarters to Nashville, along with 1,050 employees.

**Nashville vs. National Employment Growth** (Year-Over-Year)




Sources: YardiMatrix, Bureau of Labor Statistics (not seasonally adjusted)

**Nashville Employment Growth by Sector** (Year-Over-Year)

| | | Current Employment | | Year Change | |
|---|---|---|---|---|---|
| Code | Employment Sector | (000) | % Share | Employment | % |
| 60 | Professional and Business Services | 170 | 17.1% | 8,700 | 5.4% |
| 40 | Trade, Transportation and Utilities | 191 | 19.2% | 6,100 | 3.3% |
| 65 | Education and Health Services | 151 | 15.1% | 3,900 | 2.7% |
| 70 | Leisure and Hospitality | 116 | 11.6% | 2,600 | 2.3% |
| 90 | Government | 110 | 11.0% | 2,400 | 2.2% |
| 55 | Financial Activities | 68 | 6.8% | 1,200 | 1.8% |
| 80 | Other Services | 42 | 4.2% | 500 | 1.2% |
| 50 | Information | 24 | 2.4% | -300 | -1.2% |
| 30 | Manufacturing | 83 | 8.3% | -2,200 | -2.6% |
| 15 | Mining, Logging and Construction | 41 | 4.1% | -2,300 | -5.3% |

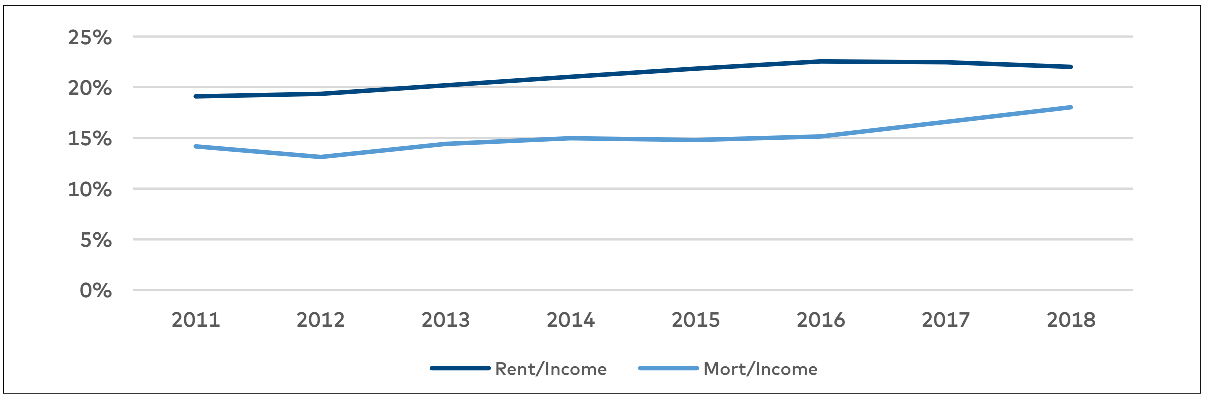
Sources: YardiMatrix, Bureau of Labor Statistics

## Demographics

### Affordability

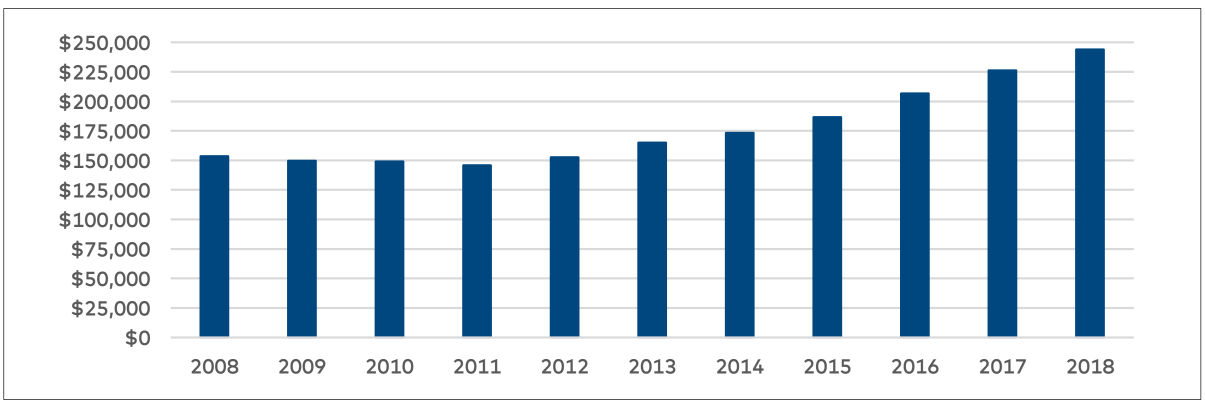
- Nashville's hot job market is boosting real estate values, and thanks to the influx of higher-wage workers, communities in once lower-rent neighborhoods are being revitalized. Housing remains relatively affordable in Nashville compared to the nation, although the median home price rose another 7.9% in the first half of 2018, reaching $244,069. However, owning remains the more affordable option, accounting for 18% of the area median income, while the average rent of $1,216 equates to 22%.
- There are 1,300 affordable units under construction in Nashville in fully and partially affordable communities, with nearly 600 slated for completion by the end of the year.

**Nashville Rent vs. Own Affordability as a Percentage of Income**




Sources: YardiMatrix, Moody's Analytics

**Nashville Median Home Price**




Source: Moody's Analytics

### Population

- Nashville had one of the highest growth rates among larger metro areas last year, up 1.8%, more than double the national rate.
- In 2017, Nashville added more than 34,000 residents, 13.9% over the 2010 census figure.

**Nashville vs. National Population**

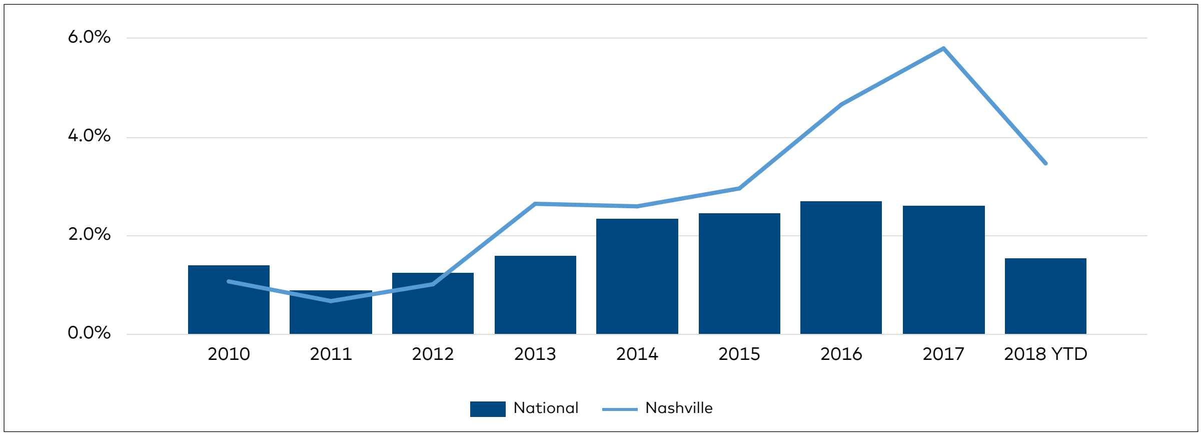
| | 2013 | 2014 | 2015 | 2016 | 2017 |
|---|---|---|---|---|---|
| National | 316,234,505 | 318,622,525 | 321,039,839 | 323,405,935 | 325,719,178 |
| Nashville Metro | 1,757,891 | 1,792,756 | 1,829,513 | 1,868,855 | 1,903,045 |

Sources: U.S. Census, Moody's Analytics

## Supply

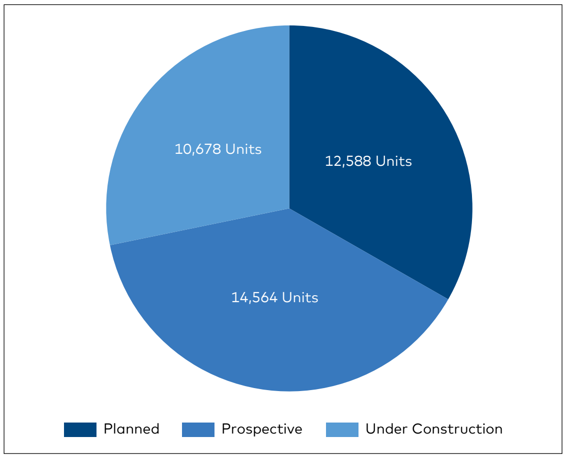
- More than 4,000 units in 18 properties were delivered across the metro this year through August, with the bulk being in core submarkets. This comes after the 2017 cycle high, when some 7,100 units came online. Last year's Nashville deliveries accounted for 5.8% of the total multifamily stock, second only to Seattle among major U.S. metros and more than double the national average.
- As of August, the metro had 10,600 units under construction and an additional 27,000 apartments in the planning and permitting stages. Despite the ongoing development boom, the occupancy rate in stabilized properties slid only 30 basis points year-over-year, to 95.1% as of July. However, the pipeline continues mainly to comprise Lifestyle communities, which is set to further deepen the gap across the quality spectrum.
- Construction activity is most intense in Downtown–North (2,267 units), Franklin (2,179 units) and Hendersonville (954 units). The largest multifamily development underway is the 444-unit The Revere at Hidden Creek in Hendersonville. The community, owned by Gross Builders, started pre-leasing in January and is slated for delivery in March 2019.

**Nashville vs. National Completions as a Percentage of Total Stock** (as of August 2018)



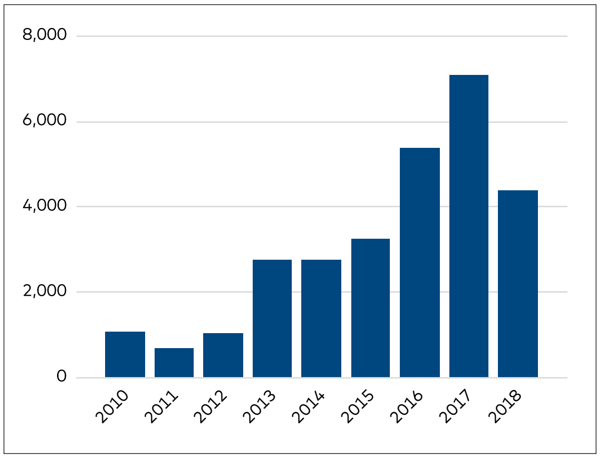

Source: YardiMatrix

**Development Pipeline** (as of August 2018)




Source: YardiMatrix

**Nashville Completions** (as of August 2018)

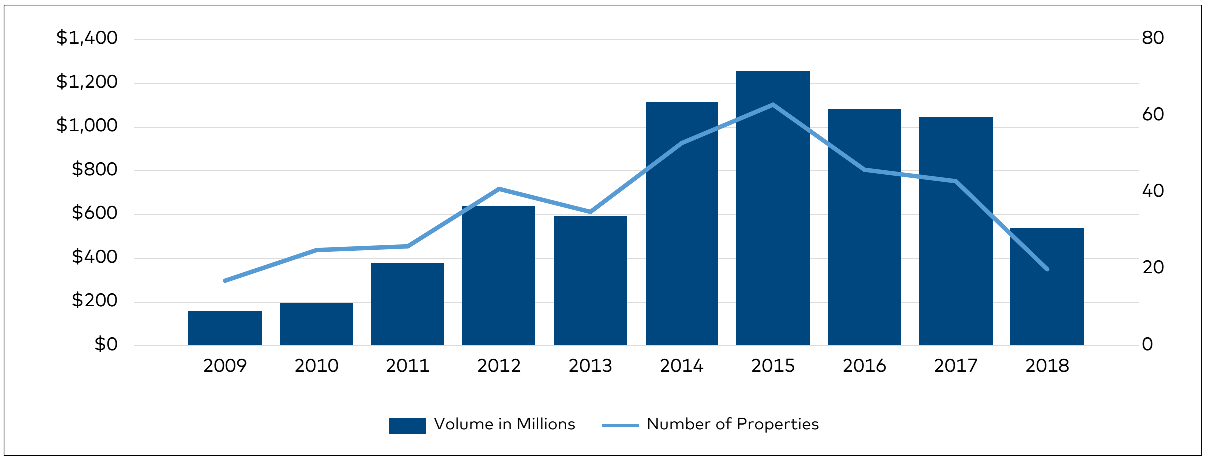



Source: YardiMatrix

## Transactions

- Transaction activity maintained last year's pace in the first half of 2018, with $541 million in multifamily assets trading through July. Investors mainly focused on value-add plans, with 14 of the 20 assets changing hands in the first seven months being Renter-by-Necessity. The metro's healthy demand pushed cap rates down to the low-5.0% range for Class A assets, according to an analysis by Cushman & Wakefield. At the same time, the share of Class A transactions is bound to rise, as value-add deals are becoming increasingly harder to come by.
- This year's drop in per-unit values also reflects the shift to value-add: The average Nashville unit traded for $121,299 in the first seven months of the year, down 18.7% compared to the 2017 figure. Meanwhile, the national per-unit average continued its ascension, up 5.7% to $147,630. Franklin remained the most active Nashville submarket in the 12 months ending in July, with sales totaling roughly $120 million.

**Nashville Sales Volume and Number of Properties Sold** (as of July 2018)




Source: YardiMatrix

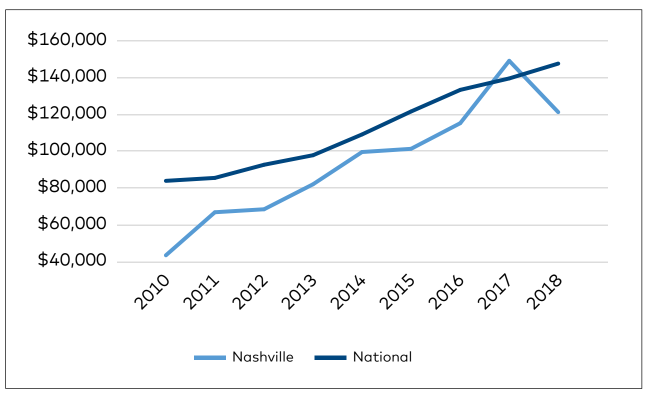
**Top Submarkets for Transaction Volume[1]**

| Submarket | Volume ($MM) |
|---|---|
| Franklin | 120 |
| Murfreesboro–West | 102 |
| Downtown–North | 76 |
| Midtown/Music Row | 72 |
| Bellevue | 70 |
| East End | 67 |
| West Nashville | 48 |
| Donelson/South Hermitage | 42 |

Source: YardiMatrix

[1] From August 2017 to July 2018

**Nashville vs. National Sales Price per Unit**




Source: YardiMatrix

## News in The Metro

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### Lion Real Estate Roars Into Nashville

The company acquired the 1973-built Highland Cove, a 206-unit property that traded for $16.6 million in an off-market transaction.

### Nashville Community Changes Hands For $27M

The Benoit Group sold the 210-unit Class B property to NexPoint Residential Trust, which financed the acquisition with a $17 million Freddie Mac loan.

### MACC JV Acquires TN Portfolio

Hyde Capital Group traded the two communities, totaling 456 units, for more than $32 million. The new owner plans to renovate both assets.

### TN Apartments Land $17M Refi

CBRE Capital Markets originated the Freddie Mac mortgage, which retires a prior fixed-rate CMBS loan of $10.6 million taken in 2012.

### Walker & Dunlop Secures $20M Loan For Affordable Asset

Vice President Rob Rotach lined up the financing for the 153-unit Dandridge Towers, an age-restricted property in southern Nashville, through the HUD program.

### Raskin Holdings Sells Nashville Apartments For $50M

Covenant Capital Group picked up the 57-building, 379-unit community, funding the purchase with a five-year, $35 million Freddie Mac loan.

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## Executive Insight

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MULTI-HOUSING NEWS

### Music City's Multifamily Build-Up

Following last year's historic number of deliveries across the metro, Nashville's rent growth has begun to slow down. At the same time, as the city's major employers continue to generate new jobs, population growth is soaring—by one estimate, between 75 and 100 people are moving to the area each day.

Southeast Venture has been doing business in Nashville since its inception in 1981, offering a mix of brokerage, development and design services. Wood Caldwell, principal at the company and a 40-year veteran of the metro's real estate industry, shares his insights into the metro's development boom and investment opportunities.

***Given the unprecedented number of multifamily units in Nashville's development pipeline, what does it take for a project to stand out?***

Location, location, location. The key is not to go where the competition is. There wasn't much going on in areas like East Nashville, The Nations and MetroCenter before we started developing there. You have to watch the trends for a while and see where the market is going.

***How has the market's rent growth deceleration affected Southeast Venture's business strategy?***

It has slowed, but it's still high—it hasn't affected us yet. In 2018, the number of units that came online was unprecedented, so you're seeing some projects giving one to two months of free rent to attract tenants, but we expect demand to catch up to supply next year.

***Tell me about a recent development you were involved in. In what ways does it reflect the current housing trends in Nashville?***

Silo Bend is the biggest example (of a recent development). In total, 105 condo units are going in there, and 65 have already been sold before they even dug the foundation.

We've found that if you hit the $250,000 to $300,000 price point, or $175 to $200 per square foot, the units go quickly.

***How are the needs of today's renter different than those of a decade ago?***

They want more amenities. They're not looking for the largest unit, but the ones with nice amenities. They're not doing much besides sleeping there, anyway, because they're going out and spending their free time in communal and public spaces with friends.

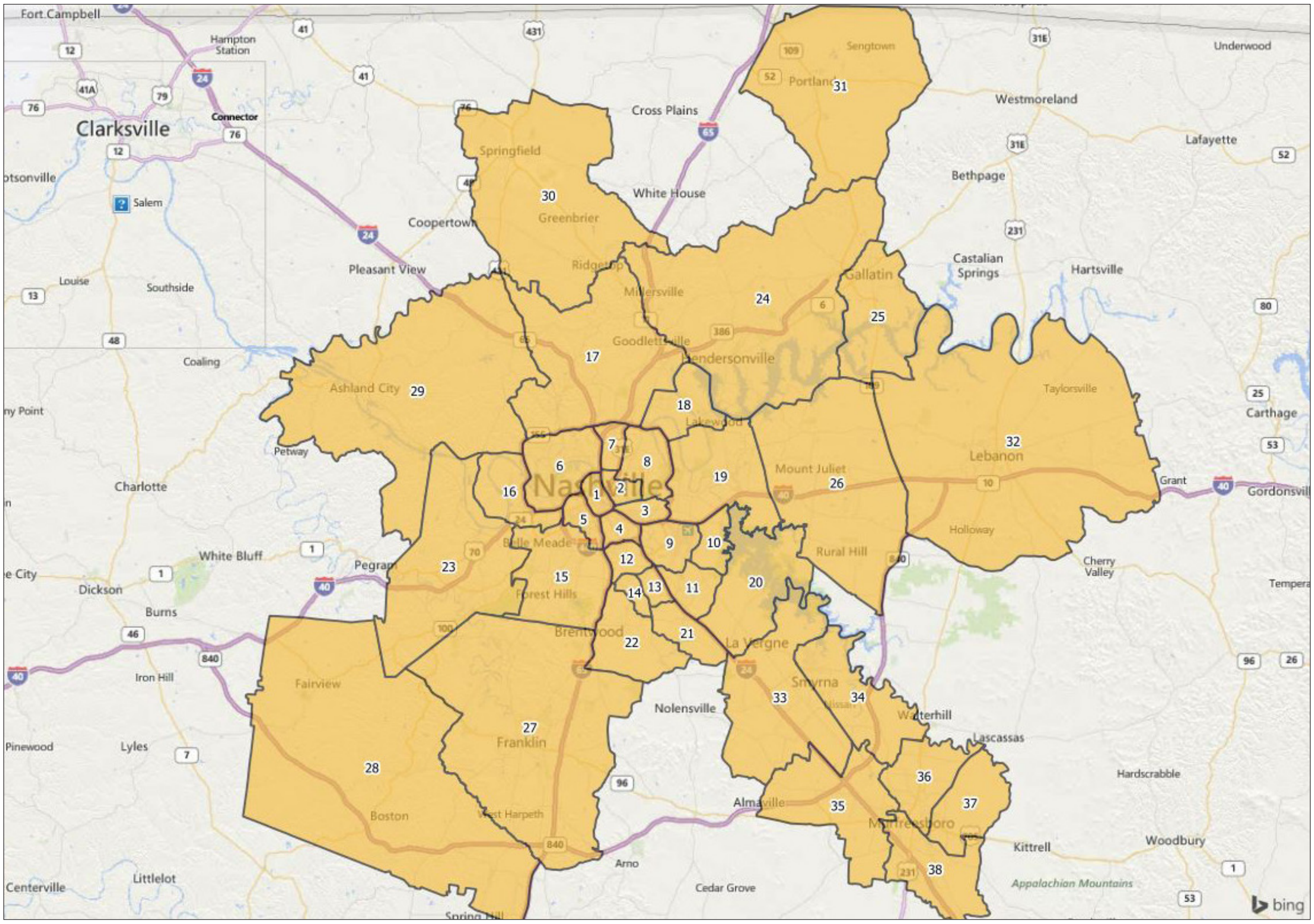
***What can an owner of an existing property do to stay competitive with the flood of new communities?***

They can keep rents lower than what the newer properties are offering, based on the market price, and they'll keep the units full. If they go for a buyout deal, though, the rents will go up again and people will go for the newer places at the same price.

***What insights can you provide about the main opportunities and challenges in Nashville's multifamily market right now?***

You have to go where the markets are trending. Job growth is still booming, so plenty of young people are still coming to town and looking to rent. The challenge is keeping up with that demand while keeping housing affordable. That's not just a developer's problem, but (a problem for) the whole city of Nashville.

## Nashville Submarkets




| Area # | Submarket |
|---|---|
| 1 | Downtown–North |
| 2 | East End |
| 3 | Clovernook |
| 4 | Downtown–South |
| 5 | Midtown–Music Row |
| 6 | North Nashville–Bordeaux |
| 7 | Northeast Nashville |
| 8 | East Nashville–Inglewood |
| 9 | South Nashville |
| 10 | Donelson–South Hermitage |
| 11 | Antioch–West |
| 12 | Elm Hill–Woodbine |
| 13 | Southeast–East |
| 14 | Southeast–West |
| 15 | West End–Green Hills |
| 16 | West Nashville |
| 17 | Goodlettsville–North |
| 18 | Goodlettsville–South |
| 19 | Nashville Shores–Hermitage |

| Area # | Submarket |
|---|---|
| 20 | Antioch–East |
| 21 | Antioch–South |
| 22 | Southeast–Brentwood |
| 23 | Bellevue |
| 24 | Hendersonville |
| 25 | Gallatin |
| 26 | Mount Juliet |
| 27 | Franklin |
| 28 | Fairview |
| 29 | Ashland City |
| 30 | Springfield–Greenbrier |
| 31 | Portland |
| 32 | Lebanon |
| 33 | La Vergne–Smyma |
| 34 | Smyma–East |
| 35 | Murfreesboro–West |
| 36 | Murfreesboro–North |
| 37 | Murfreesboro–East |
| 38 | Murfreesboro–South |

## 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.

To learn more about Yardi® Matrix and subscribing, please visit www.yardimatrix.com or call Ron Brock, Jr., at 480-663-1149 x2404.