Yardi® Matrix

Knoxville's Mending Ways

Multifamily Report Summer 2019

Employment Gains Improve

Limited Supply Sustains Rent Growth

Transaction Activity, Stock Additions Dwindle

Market Analysis

Summer 2019

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Tepid Supply Boosts Rent Growth

Knoxville's economy is steadily accelerating, strengthening the metro's multifamily fundamentals. The market's healthy demand, coupled with tepid construction activity, pushed up rent growth to 3.6% year-over-year through July, 20 basis points above the U.S. rate. The average Knoxville rent surpassed the $1,000 mark for the first time, reaching $1,023 as of July.

Employment growth saw a 1.9% uptick during the 12 months ending in June, outpacing the national rate for the first time since 2011. Trade, transportation and utilities led growth, following last year's nearly 2.2 million passengers that traveled through McGhee Tyson Airport. Manufacturing rose a solid 4.6% and is poised for sustained growth. There are several developments underway set to boost the area's economy, including the $6.5 billion Uranium Processing Facility at Y-12 National Security Complex in Oak Ridge, slated for completion in 2025. Meanwhile, three employment sectors contracted—including construction—losing a combined 800 jobs.

Transaction activity moderated considerably: Only three assets of 50 or more units traded in Knoxville this year through July. Deliveries also lagged, with just one property coming online during the first seven months. Mostly due to tepid supply, we expect the average Knoxville rent to continue rising, clocking in at 3.6% for the year.

Recent Knoxville Transactions

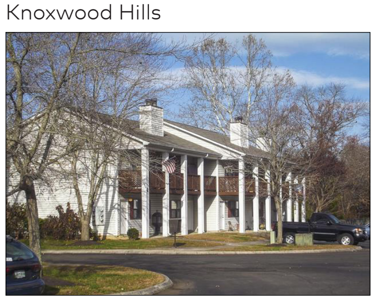
Steeplechase

City: Knoxville, Tenn.
Buyer: West Shore
Purchase Price: $40 MM
Price per Unit: $87,778

British Woods

City: Oak Ridge, Tenn.
Buyer: Prime Property Investors
Purchase Price: $8 MM
Price per Unit: $59,808

Knoxwood Hills



City: Knoxville, Tenn.
Buyer: CRE-PRO
Purchase Price: $4 MM
Price per Unit: $38,265

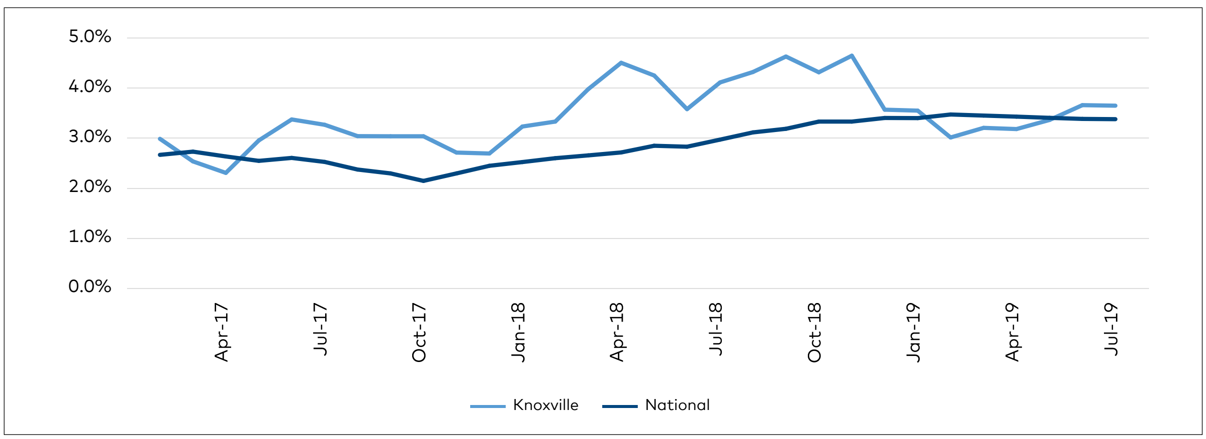
The Flats at Jackson Square

City: Oak Ridge, Tenn.
Buyer: Covenant Capital Group
Purchase Price: $4 MM
Price per Unit: $29,744

Rent Trends

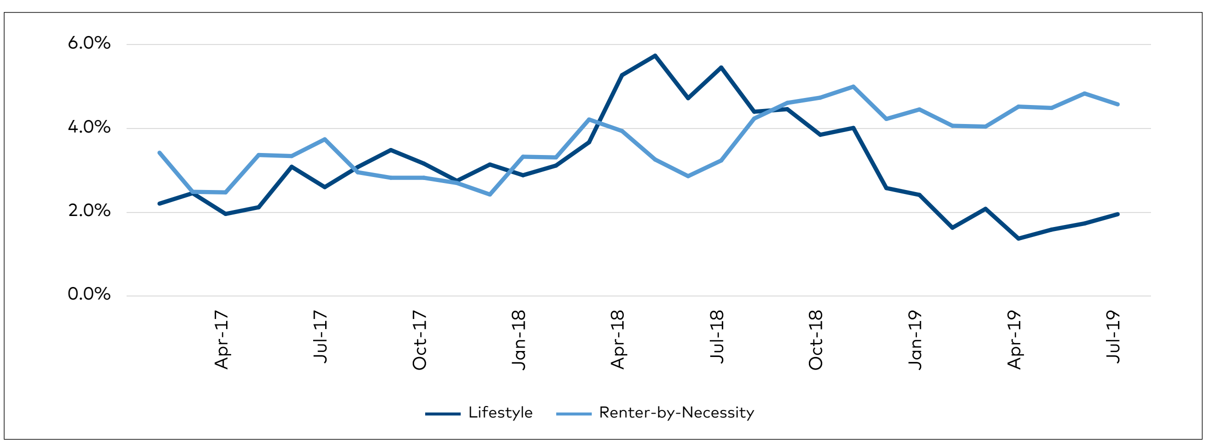
- Knoxville rents rose 3.6% year-over-year through July, 20 basis points above the national rate. The metro's rent performance has been irregular over the past couple of years, in part due to the 3,000 units delivered since the beginning of 2015. The average rent in the metro climbed to $1,023, continuing to trail the $1,469 U.S. figure.
- The working-class Renter-by-Necessity segment led rent growth in Knoxville, with the average rate up 4.6% year-over-year through July, reaching $868. Meanwhile, rents in the Lifestyle segment advanced 2.0%, to $1,359.
- The largest increases were recorded in the metro's second most affordable submarket, Oakridge (6.9% to $776), followed by Corryton (5.3% to $977). Half of Knoxville's submarkets posted average rents above the $1,000 mark, with Seymour (4.3% to $1,736) and Knoxville–West (4.5% to $1,307) remaining the most expensive.
- With the population and the metro's economy slowly but steadily rising, while multifamily development lags behind, we expect demand and supply in Knoxville to continue displaying the same dynamics in the foreseeable future. Yardi Matrix expects the average Knoxville rent to rise 3.6% in 2019.

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



Source: YardiMatrix

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



Source: YardiMatrix

Economic Snapshot

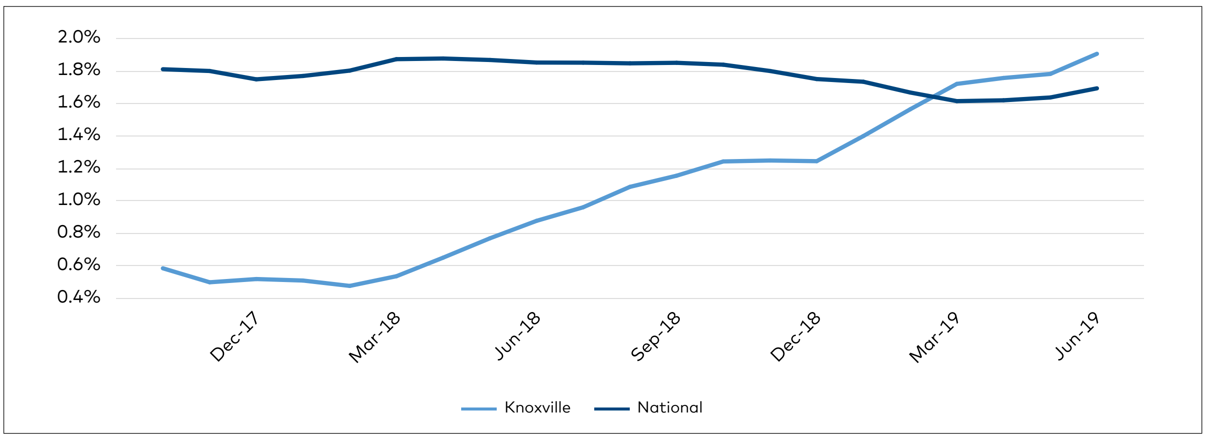
- Knoxville gained 7,900 jobs in the 12 months ending in June, a 1.9% uptick, above the 1.7% national rate. This is the first time since late-2011 that Knoxville job gains outpaced the U.S. figure. The metro's unemployment rate stood at 3.9% as of June, just 20 basis points above the national rate.

- The metro's economy is slowly regaining its footing: The number of employment sectors contracting dropped to three, accounting for 800 positions combined. Mining, logging and construction posted most of these losses, contracting by 600 jobs.

- Meanwhile, the trade, transportation and utilities sector led growth, gaining 2,600 positions. Last year, McGhee Tyson Airport handled nearly 2.2 million passengers, a record for Knoxville, while recently marking another milestone through the completion of a 10,000-foot runway.

- Leisure and hospitality and manufacturing rounded out the podium, gaining 4,300 jobs, with the latter expanding by a solid 4.6%. The sector is poised for continued growth, sustained by several developments underway, including a $6.5 billion uranium processing facility in Oak Ridge. Meanwhile, Fresenius Medical Care is building a new facility to support its nearby manufacturing plant. The new distribution center is set to become the company's largest such facility on the East Coast.

Knoxville vs. National Employment Growth (Year-Over-Year)



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

Knoxville Employment Growth by Sector (Year-Over-Year)

		Current Employment		Year Change	
Code	Employment Sector	(000)	% Share	Employment	%
40	Trade, Transportation and Utilities	81	20.0%	2,600	3.3%
70	Leisure and Hospitality	46	11.4%	2,500	5.7%
30	Manufacturing	41	10.1%	1,800	4.6%
65	Education and Health Services	56	13.8%	1,200	2.2%
80	Other Services	16	4.0%	400	2.6%
55	Financial Activities	20	4.9%	200	1.0%
50	Information	6	1.5%	-	0.0%
60	Professional and Business Services	65	16.0%	-100	-0.2%
90	Government	57	14.1%	-100	-0.2%
15	Mining, Logging and Construction	18	4.4%	-600	-3.2%

Sources: YardiMatrix, Bureau of Labor Statistics

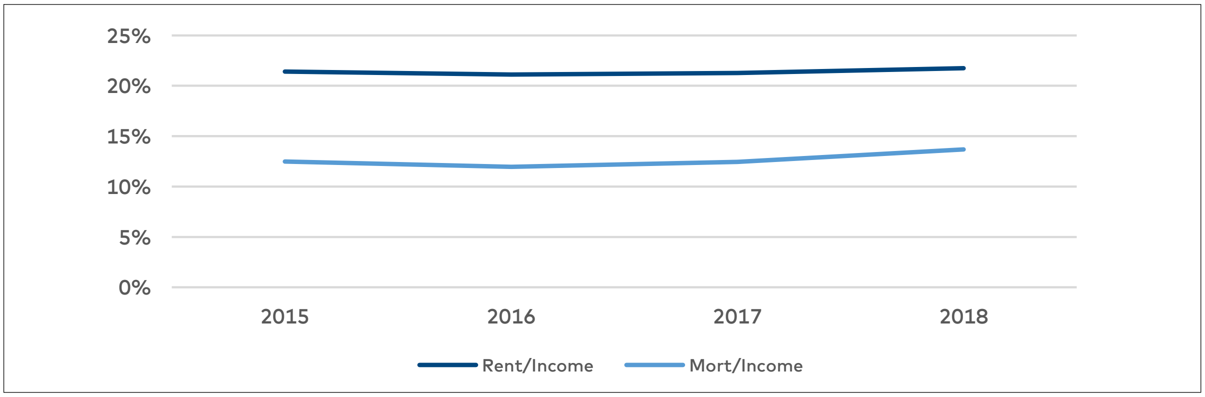
Demographics

Affordability

- The Knoxville median home value rose 8.0% in 2018, to $151,638. That marked a 26.8% hike in a decade. The metro remains relatively affordable, even at a regional level, as owning continues to be the significantly cheaper alternative. Last year, the average mortgage payment accounted for only 14% of the area median income, while the average rent equated to as much as 22% of the same amount.

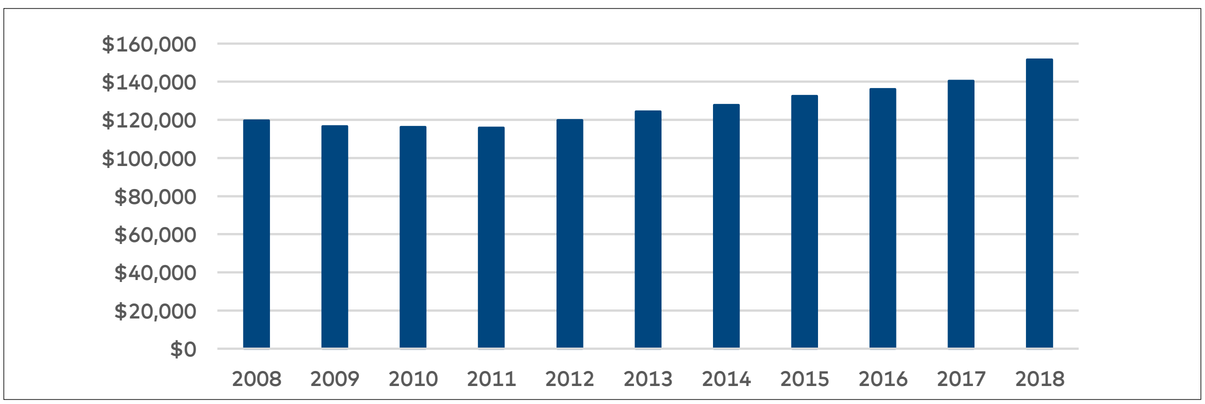
- The metro remains more affordable when compared to nearby cities such as Nashville, but a portion of the development pipeline continues to cater to lower-income households. As of late-August, nearly 20% of all units in underway, planned and prospective communities were part of fully affordable projects.

Knoxville Rent vs. Own Affordability as a Percentage of Income



Sources: YardiMatrix, Moody's Analytics

Knoxville Median Home Price



Source: Moody's Analytics

Population

- Knoxville added 9,234 residents in 2017, a 1.1% uptick, 40 basis points above the U.S. rate.
- The metro gained more than 38, 000 residents between 2010 and 2017, for a 4.8% demographic expansion.

Knoxville vs. National Population

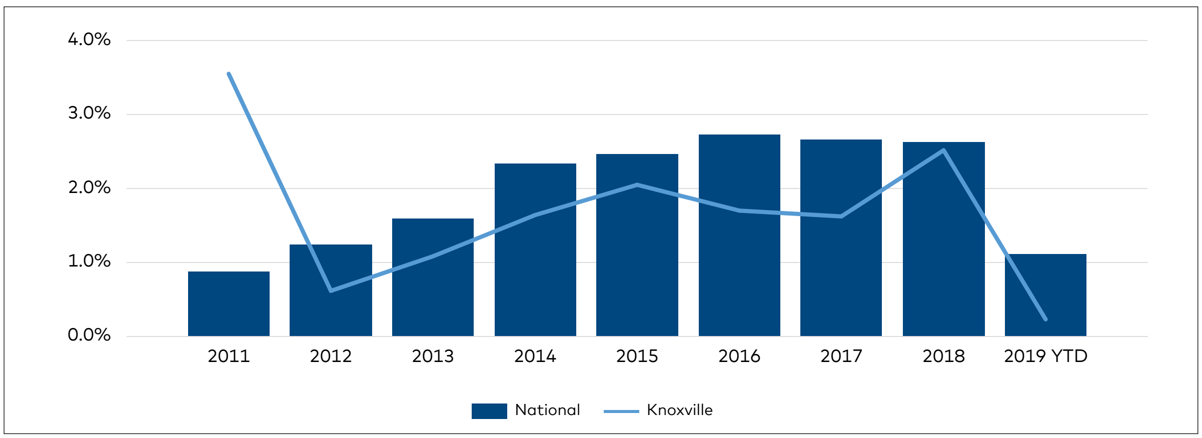
	2013	2014	2015	2016	2017
National	316,234,505	318,622,525	321,039,839	323,405,935	325,719,178
Knoxville Metro	851,377	855,695	860,398	867,870	877,104

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

Supply

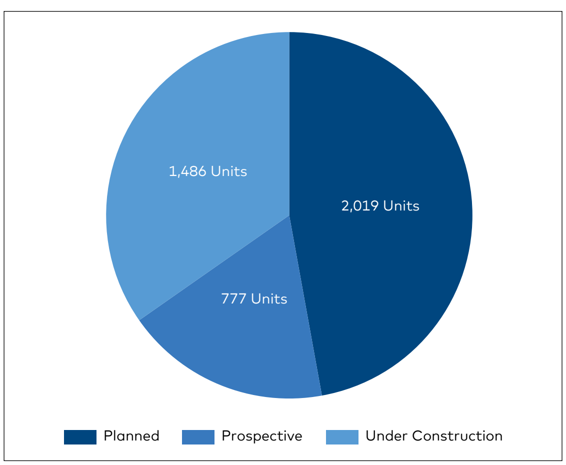
- Some 1,500 units in seven properties were under construction as of July, nearly half of them in fully affordable projects. With the construction sector losing 600 positions over 12 months in the context of a tight labor market, further development delays are likely to occur, a more-than-apparent trend across many U.S. metros. We expect some 750 units to be delivered in Knoxville this year.
- Developers added just 92 units in 2019 through July, a mere 0.2% of stock, trailing the 1.1% U.S. rate. This comes after 986 units were delivered last year, the highest volume since 2011. Laurel Branch, the only property of 50 or more units delivered in the first seven months of the year, is a fully affordable community owned by Hall Housing Investments and located in an Opportunity Zone south of Knoxville. Last year's deliveries left a mark on occupancy, with the rate in stabilized assets dropping 120 basis points over 12 months, to 95.1% as of June.
- Just four Knoxville submarkets had multifamily developments underway as of July. Hardin Valley had 597 units under construction in two projects, followed by South Knoxville (487 units), Northshore (240 units) and Knoxville–East (162 units).

Knoxville vs. National Completions as a Percentage of Total Stock (as of July 2019)



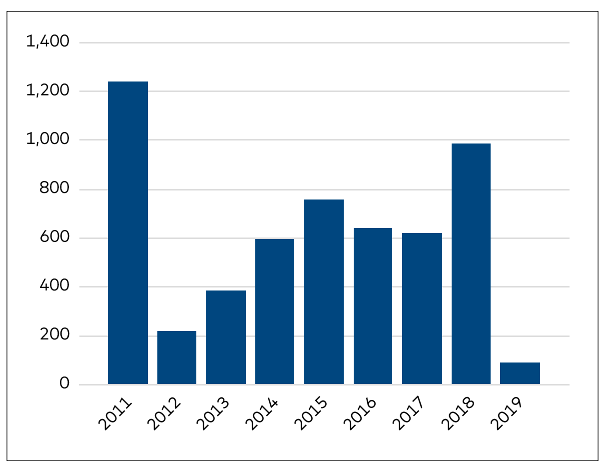
Source: YardiMatrix

Development Pipeline (as of July 2019)



Source: YardiMatrix

Knoxville Completions (as of July 2019)



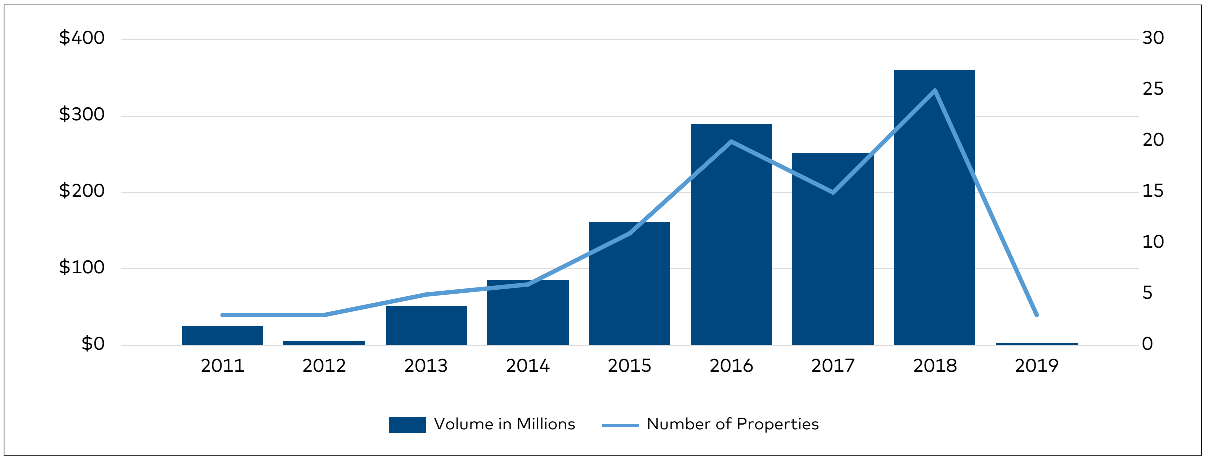
Source: YardiMatrix

Transactions

- After last year's cycle peak, when $360 million in multifamily assets traded in Knoxville at an average per-unit price of $100,314, transaction activity shifted down a couple of gears. By July, only three properties of 50 or more units changed ownership in the metro, all value-add assets. Nearly $1.3 billion in communities traded across Knoxville since the beginning of 2010.

- Of the three assets of 50 or more units trading through July, only one had a recorded price tag: The 98-unit Knoxwood Hills, located in the Knoxville–East submarket, which was acquired by CRE-PRO in an REO sale for nearly $4 million. The transaction is subject to a $2.7 million loan held by Highlands Union Bank. The other two assets changing hands are also subject to loans—$13.4 million in HUD financing on LHP Capital's 109-unit, fully affordable Tillery Ridge, and a total of $20.7 million in Fannie Mae financing for The Heights of Knoxville, a 204-unit student community owned by Saban Capital Group.

Knoxville Sales Volume and Number of Properties Sold (as of July 2019)



Source: YardiMatrix

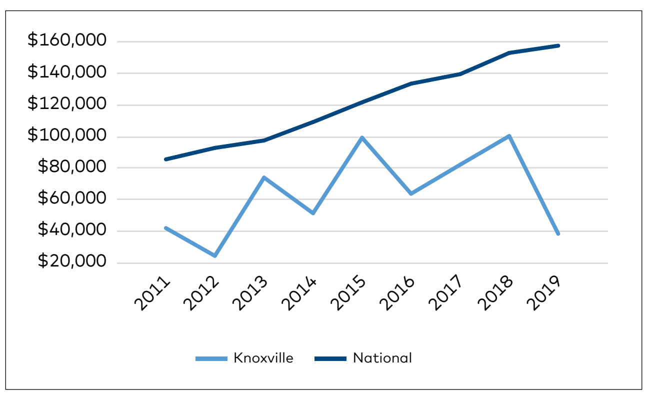
Top Submarkets for Transaction Volume[1]

Submarket	Volume ($MM)
Powell	40
Middlebrook	11
Oakridge	11
Knoxville–East	9

Source: YardiMatrix

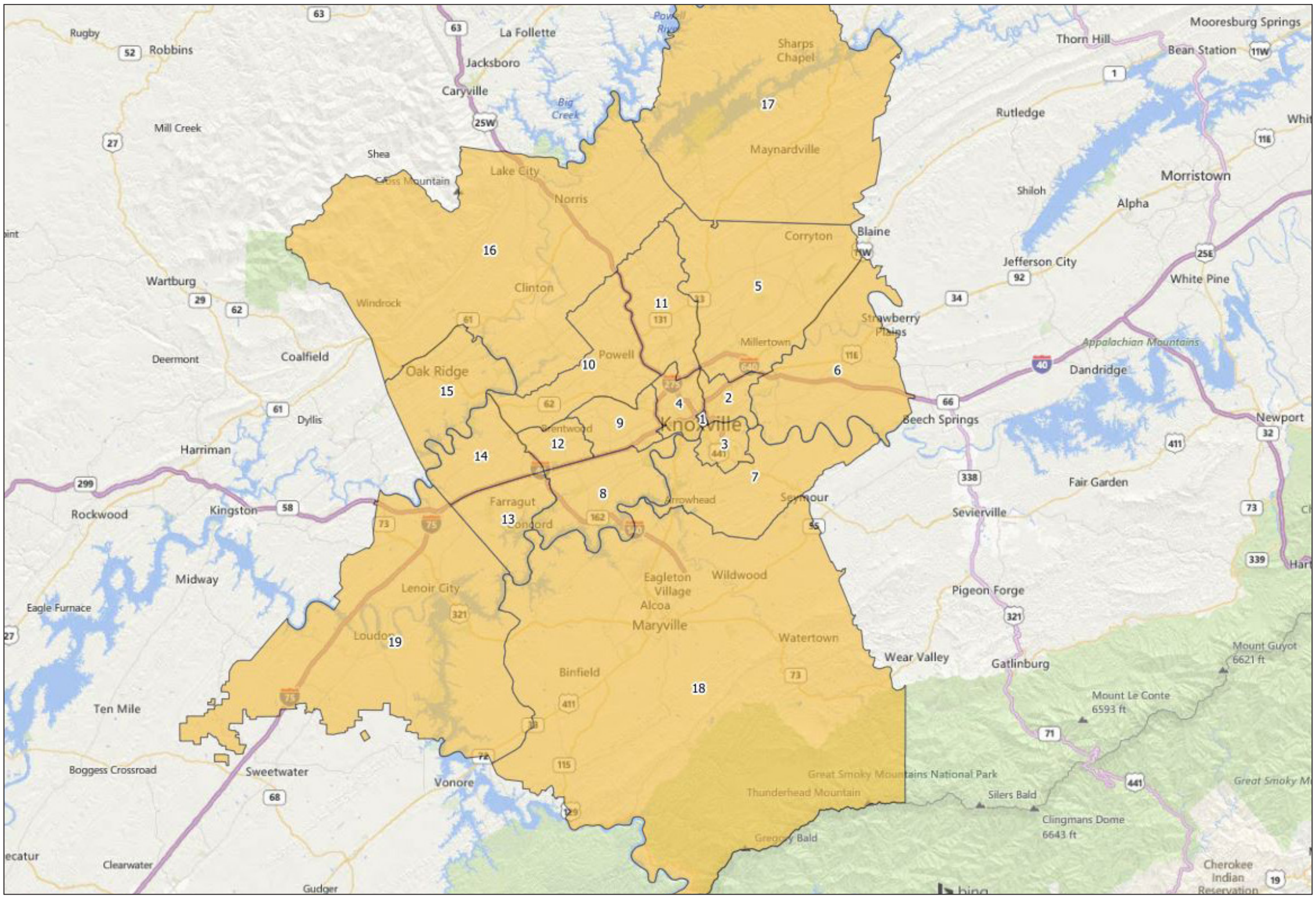
[1] From August 2018 to July 2019

Knoxville vs. National Sales Price per Unit



Source: YardiMatrix

Knoxville Submarkets



Area #	Submarket
1	Knoxville–Downtown
2	Knoxville–East
3	South Knoxville
4	Knoxville–West
5	Corryton
7	Seymour
8	Northshore
9	Middlebrook
10	Karns

Area #	Submarket
11	Powell
12	Cedar Bluff
13	Farragut
14	Hardin Valley
15	Oakridge
16	Anderson
18	Maryville
19	Loudon

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.