The Large Amount of Units Entering the Market is Being Absorbed by Apartment Renters

Meanwhile inventory will rise by 3.2% over the next 12 months.

Renters are quickly absorbing the unprecedented influx of apartments that hit the market in the first half of 2023, according to Newmark's U.S. multifamily capital markets report for 2Q 2023. This trend is expected to continue through mid-2024, creating new opportunities for real estate investors.

The report found that renters absorbed 98,249 units in the first half of 2023, about four times as many as they did in the same period in 2022. This is due in part to the strong economy and job growth, which is driving demand for housing.

The median market's inventory is forecast to increase by 3.2% over the next 12 months, up from 2% over the previous 12. However, this increase in supply is expected to be met by strong demand from renters, particularly in markets with strong population growth and job markets.

Real estate investors can capitalize on this trend by investing in apartments in these markets. They should also consider investing in lower-income communities, as Class C properties have experienced the largest rent growth gains in recent years.

However, investors should be aware of the rising expenses that landlords are facing, such as insurance costs and property taxes. Despite these expenses, multifamily net operating income is expected to rise slightly above its long-term growth average in 2027.

Overall, the news is positive for real estate investors who are looking to invest in multifamily properties. The high demand for apartments and the projected growth in the median market's inventory are both favorable trends. However, investors should be mindful of the rising expenses that landlords are facing, and they should focus on investing in markets with strong demand and lower-income communities.

For INVESTORS:

Focus on markets with strong population growth and job markets, as well as lower-income communities. Be mindful of rising expenses such as insurance costs and property taxes. Consider investing in Class C properties, which have experienced the largest rent growth gains in recent years.

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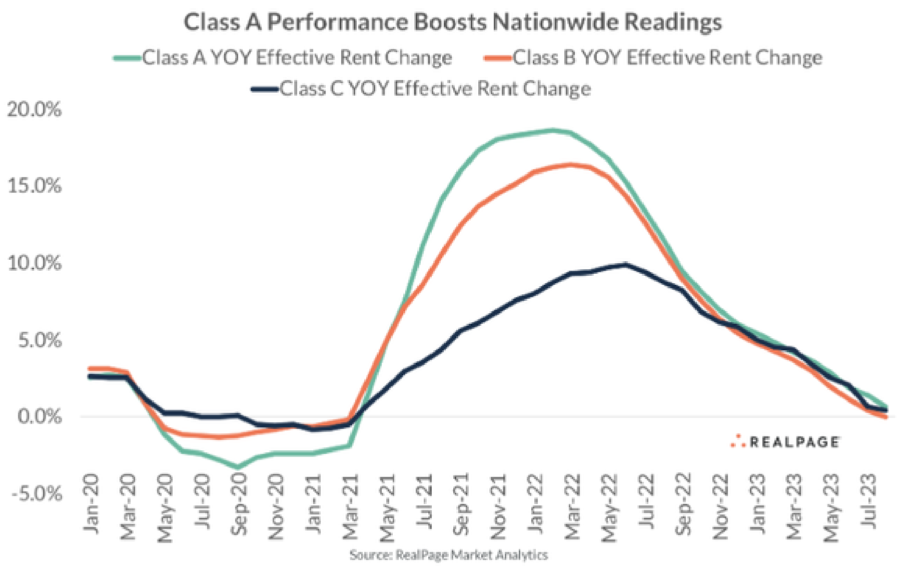
Some apartment markets are suffering from
Class A Rent Performance

Though market-level figures varied, nationwide apartment rent growth almost stopped in August.

However, the Class A rent change improved overall national performance. As of August, Class A space had an increase in yearly effective rent of 0.7%, while Class B and Class C saw stable rent growth of 0.0% and 0.4%, respectively. In the United States as a whole, the yearly effective asking rent change was only 0.3% as of August, according to data from RealPage Market Analytics.



In some markets, however, that storyline runs counter to current rent performance by product class. In several of the nation's largest apartment markets, rent change in Class A units – often a proxy for new supply – is weighing down marketwide readings. In some markets, Class A rent change runs 700-plus basis points (bps) below Class B and C readings and as deep as 300-plus bps below market averages.

Perhaps the most dramatic instance of this Class A underperformance is Cincinnati. In Cincinnati, Class A rent growth was under 0.5% annually as of August, but Class B and Class C unit growth was above 5%. Cincinnati, one of the top rent increase performers in the country in August, came in second place among the 50 largest markets in the country, behind only Newark, with an annual rent growth rating of 3.8%.

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Class A Performance Weighing Down Marketwide Rent Change

Market	Class A	Class B	Class C	Market Total
Cincinnati	0.5%	5.1%	6.1%	3.8%
Columbus	0.9%	3.1%	4.0%	2.7%
San Diego	-0.1%	1.1%	6.1%	1.3%
Memphis	-0.4%	0.4%	3.2%	0.8%
Chicago	2.0%	4.5%	3.5%	3.2%
Miami	1.3%	1.1%	8.7%	2.4%
Los Angeles	-1.8%	-0.4%	0.3%	-0.7%
Nashville	-3.1%	-1.8%	-1.3%	-2.1%
Indianapolis	2.0%	2.7%	4.3%	2.9%

*YoY Rent Change as of August 2023

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Source: RealPage Market Analytics

A similar tendency can be seen in almost half of the markets on this list. In the year ending in August, Columbus, Chicago, Miami, and Indianapolis all placed among the top 10 markets nationwide for rent change. Additionally, the Midwest markets on this list often have minimal supply pressure, which tends to have a greater influence on Class A rentals than cheaper rents.

The findings from the remaining markets are inconsistent. Although San Diego continues to fare well by regional norms, the West Coast continues to have the largest percentage of markets with rent reductions. With an average rent of $2,861 in August, San Diego is one of the most expensive apartment markets in the country. San Diego's typical Class A rent is $3,303, which is over $1,200 more expensive than the city's typical Class C rent of $2,187. As a result, San Diego may be better described as a market where Class C units do better than Class A units do.

In Miami, where average Class C rents ($1,778) are around 45% less expensive than Class A equivalents ($3,208), the same may be stated.

Nashville could appear to be a wild card on this list before the context of its incredibly large supply chain is included. Nashville added approximately 10,000 new units in the second quarter of 2023, increasing the current inventory by over 6%. Additionally, Music City is now building another 29,000 apartments, with 13,000 of those slated to be completed in the upcoming four quarters. Operators maintaining occupancy in the face of demand from new product to lease up were likely the cause of the 3.1% decrease in Class A rent in August.

A few markets, however, present the other narrative. Class B and C product classes in Sacramento, Tampa, and West Palm Beach recorded yearly rent decreases in August, whereas Class A product classes reported rent increases, significantly enhancing market-wide rent performance.

Rent Growth Under Pressure from Florida Apartment Supply

Region	YoY Effective Asking Rent Change (Aug. 2023)	YoY Net Inventory Growth (2Q23)
Carolinas	-0.5%	**3.6%**
Mountains/Desert	-2.1%	**3.2%**
Florida	-0.7%	**3.0%**
Southeast	-0.2%	**2.6%**
Texas	-0.3%	**2.3%**
Midwest	3.1%	**1.4%**
East Coast	2.5%	**1.2%**
West Coast	-0.8%	**1.1%**

Source: RealPage Market Analytics

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Florida is one of the nation's fastest growing apartment regions, and all that new supply is putting downward pressure on rent growth. Among the eight geographic regions defined by RealPage, Florida is the third-fastest growing area, with net inventory growth of 3% in the year-ending 2nd quarter 2023. This performance followed the Carolinas and the Mountains/Desert region, but not by much.

While Florida has seen some of the nation's strongest apartment demand in recent years, even solid absorption has not been enough to keep up with big volumes of new supply. And those intense completions volumes are putting downward pressure on rents. Just a year ago, annual effective asking rent growth in the Sunshine State reached into the double digits, but prices are now in decline, falling 0.7% year-over-year as of August.

This decline in rent growth is likely to continue in the coming months, as more new apartments come online. However, it is important to note that Florida still has a strong rental market, and demand is still outpacing supply in many areas. As a result, rents are still expected to be higher than they were pre-pandemic.

Implications for Investors

The decline in rent growth in Florida has implications for investors who own or are considering investing in apartment buildings in the state. Investors should be aware that the market is becoming more competitive, and that they may need to offer lower rents or concessions in order to attract tenants. However, the long-term outlook for the Florida apartment market is still positive, due to the state's strong population growth and job market.