

Houston Multifamily




Apartment Fundamentals to Stabilize as Job Market Bounces Back

Highlights

- > The Houston multifamily market posted a mixed performance during the first quarter. Rents rose but are still lower than year-earlier levels. The vacancy rate ticked higher but absorption was positive, and the uptick in the rate was a result of an active period of new development.
- > Vacancy in Houston rose 20 basis points in the first quarter, reaching 6.2 percent. The rate is up 80 basis points year over year.
- > Asking rents are down 1.6 percent year over year but did tick up at the start of 2021. During the first quarter, asking rents rose 0.4 percent, ending the quarter at \$1,086 per month.
- > Future multifamily development will remain active. At the end of the first quarter, more than 50 apartment properties were under construction, totaling approximately 17,500 units.
- > In transactions where sales prices are available, the median price in the first quarter was \$142,500 per unit. Cap rates continued to trend lower, dipping 25 basis points to approximately 5 percent.

Houston Multifamily Market Overview

The Houston multifamily market began to show signs of stabilizing in the first quarter. The vacancy rate inched higher again, but absorption was positive, and rents reversed course and began to creep up after trending lower at the end of last year. Employers in the area have been bringing back workers, although the local economy has a deeper hole to dig out of than the other major Texas markets. Renter demand for apartments should gain momentum as the economy improves. Construction of new units continues, and developers have approximately 17,500 units in the construction pipeline.

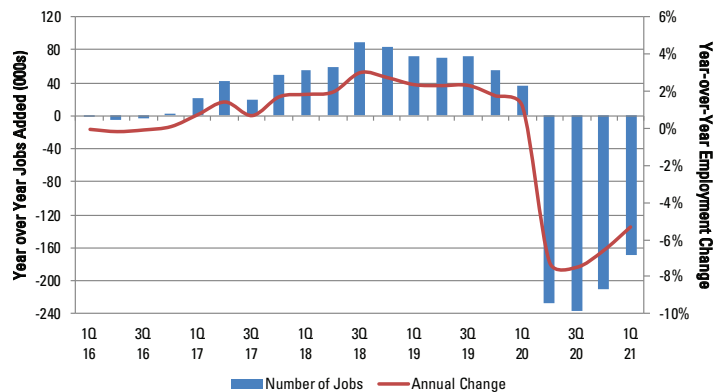
Q1 Snapshot	Houston Market
	Market Fundamentals
	Vacancy 6.2%
	- Year Over Year Change +80 bps
	Asking Rent \$1,086
	- Year Over Year Change -1.6%
	Transaction Activity*
	Median Sales Price Per Unit (YTD) \$142,500
	Cap Rates (Avg YTD) 5.0%
	Construction Activity
	Units Under Construction 17,568
	Units Delivered YTD 1,257
	<small>*In transactions where pricing is available</small>

The local investment market gained momentum at the end of last year, and healthy conditions persisted at the start of 2021. Multifamily property sales outpaced year-earlier levels, the median price rose, and cap rates compressed. One segment of the market where pricing trends have been inconsistent has been in Class A properties. The bulk of the newer Class A projects that have sold to this point in 2021 are generally in some of Houston's sprawling suburbs such as The Woodlands, Katy, and Sugar Land. The 2021 median sales price in Class A properties is approximately \$150,000 per unit, lower than the price in 2020 when more close-in assets traded.

Employment

- > Year over year through the first quarter, total employment in Houston has contracted by 5.3 percent, with the loss of approximately 168,000 jobs. All of the losses occurred in 2020, when total losses topped 200,000 positions, a decline of 6.6 percent.
- > During the first quarter of 2021, area employers added nearly 35,000 jobs, building on the addition of 37,000 jobs in the fourth quarter of last year. Employers have added back 180,000 of the 370,000 jobs that were slashed during the spring of 2020.
- > The construction sector was quick to shed workers last year, but as the economy strengthens, it should be a source of additions in 2021. Year over year through the first quarter, area construction employment is down 13 percent with the loss of 31,000 jobs. Rapid construction hiring is common in Houston; the market added 15,500 construction jobs in 2018 and nearly 20,000 construction jobs in 2014.
- > **Forecast:** Area employment in Houston is forecast to expand by 4.2 percent in 2021, as employers add back approximately 125,000 jobs.

Employment Overview



Area employment in Houston is forecast to expand by 4.2 percent in 2021

Vacancy

- > During the first quarter, apartment vacancy in Houston rose 20 basis points, reaching 6.2 percent. The local vacancy rate trended lower from mid-2017 until mid-2020 but has crept higher in recent quarters.
- > Year over year, vacancy is up 80 basis points, and the current rate is at its highest point since the first quarter of 2018.
- > Absorption in the Class A segment of the market totaled nearly 10,000 units in 2020 but reached only about 1,000 units in the first quarter of this year. Class A vacancy ended the first quarter at 6.9 percent.
- > **Forecast:** This year should be an active one for both supply growth and an expansion of renter demand for units. New supply is expected to outpace absorption in 2021, pushing the vacancy rate up 50 basis points to 6.5 percent.

Vacancy Trends

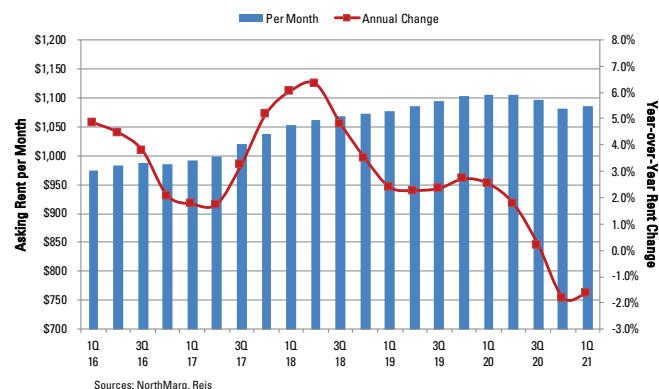


During the first quarter, vacancy rose 20 basis points, reaching 6.2 percent

Rents

- > Apartment rents inched lower in the second half of 2020 but began to reverse course at the start of this year. Asking rents rose 0.4 percent in the first quarter, creeping up to \$1,086 per month.
- > Despite some upward momentum in the first few months of 2021, current rents are still lower than levels from one year ago. During the past 12 months, the average asking rent has dropped 1.6 percent.
- > The Montrose/River Oaks submarket has been one of the fastest-growing areas in recent years, and the delivery of new, Class A units has pushed rents higher. During the first quarter, asking rents in the submarket rose 1.7 percent to \$1,543 per month.
- > **Forecast:** Rents should gain momentum as economic growth accelerates. Asking rents are forecast to rise 3 percent in 2021, reaching approximately \$1,115 per month.

Rent Trends

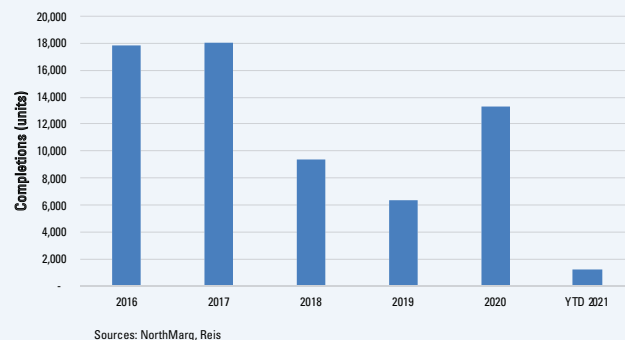


Asking rents are forecast to rise 3 percent in 2021, reaching \$1,115 per month

Development and Permitting

- > The pace of completions cooled a bit during the first quarter, with developers bringing approximately 1,250 units online. The pipeline remains full, and this is expected to be a short-term lull in the pace of deliveries of new units.
- > As of the end of the first quarter, more than 50 apartment properties were under construction, totaling approximately 17,500 units. Development is widespread throughout the market, with more than a dozen Houston-area submarkets having at least one project under construction.
- > Multifamily permitting slowed at the beginning of 2021, with developers pulling permits for approximately 2,000 multifamily units in the first quarter. This was the lightest period of multifamily permitting in Houston since the first quarter of 2018. One year ago, developers pulled permits for nearly 6,700 multifamily units.
- > **Forecast:** Developers are forecast to deliver approximately 16,000 units to the market in 2021, after completing 13,300 units in 2020

Development Trends

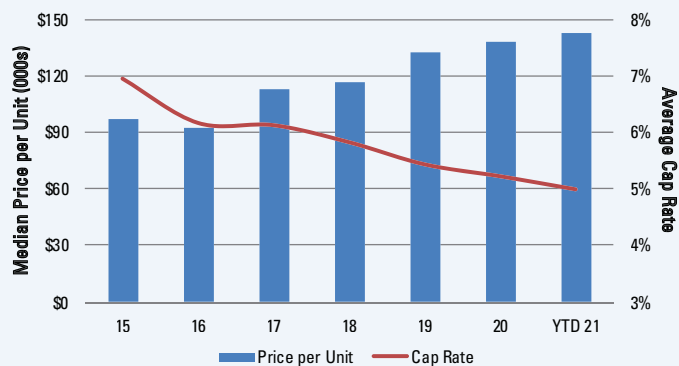


Developers pulled permits for approximately 2,000 multifamily units in the first quarter

Multifamily Sales

- > The pace of transaction activity picked up at the end of last year and that trend has carried over into 2021. Sales velocity in the first quarter was up approximately 5 percent from the same period one year earlier.
- > In transactions where sales prices are available, the median price in the first quarter was \$142,500 per unit, up 3 percent from the median price in 2020.
- > Cap rates have gradually trended lower in Houston in recent years. Cap rates averaged approximately 5 percent in the first quarter, 25 basis points lower than the 2020 average.

Investment Trends



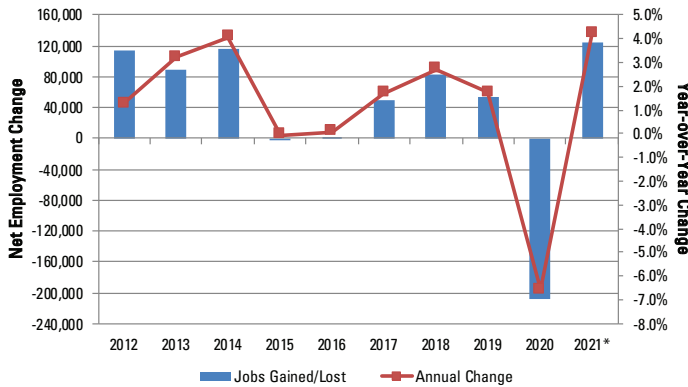
Cap rates averaged approximately 5 percent in the first quarter

Looking Ahead

The Houston economy is forecast to sustain the positive momentum that has been building in recent quarters. Employers have been adding back workers at a fairly aggressive pace since the final few months of 2020. The recovery should continue through the next several months. The energy sector should be a source of growth through the remainder of the year. In the second quarter, oil prices topped \$70 per barrel, the highest price since early 2019. Rising oil prices are being fueled by increased global demand, which could support an accelerating pace of hiring in the energy sector.

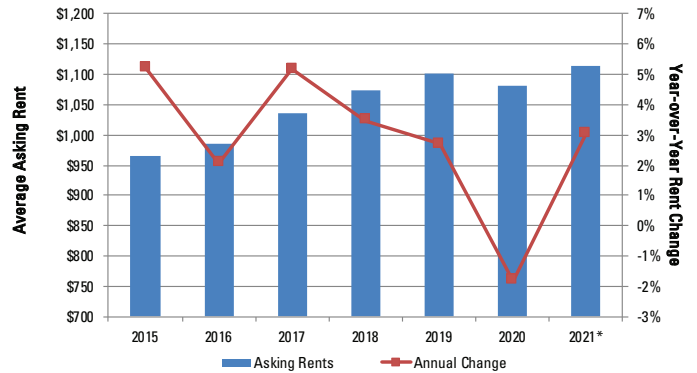
Multifamily investment activity in Houston should strengthen as 2021 progresses, with investors responding to the improving economic outlook. One potential area for concern will be the rise in new apartment development, which could affect property sales in submarkets where new development is most active. Class B and Class C properties, which do not directly compete with the newer high-end product coming to the market, may become a preferred investment option for some buyers. Value-add strategies in these properties could prove profitable as the local labor market expands at a rapid pace in 2021.

Employment Forecast



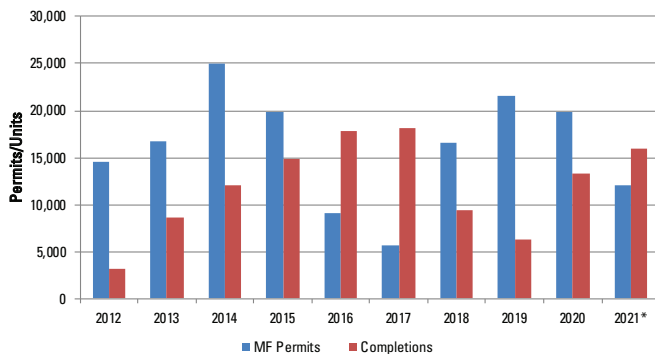
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



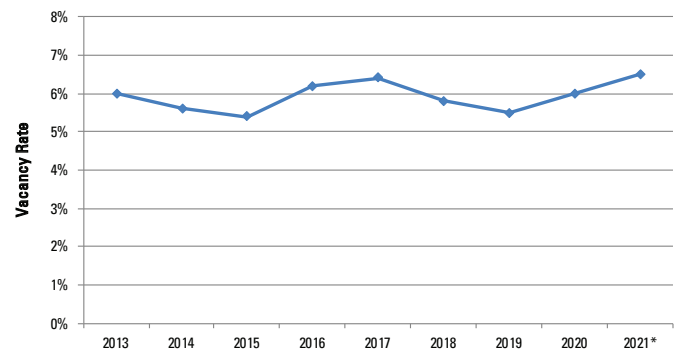
* Year End Forecast
Sources: NorthMarq, Reis

Construction & Permitting Forecast



* Year End Forecast
Sources: NorthMarq, Reis, Census Bureau

Vacancy Forecast



* Year End Forecast
Sources: NorthMarq, Reis

About NorthMarq

As a capital markets leader, NorthMarq offers commercial real estate investors access to experts in debt, equity, investment sales, and loan servicing to protect and add value to their assets. For capital sources, we offer partnership and financial acumen that support long- and short-term investment goals. Our culture of integrity and innovation is evident in our 60-year history, annual transaction volume of more than \$16 billion, loan servicing portfolio of more than \$65 billion and the multi-year tenure of our nearly 600 people.

For more information, contact:

John Burke

MANAGING DIRECTOR – DEBT & EQUITY
713.333.8824
jburke@northmarq.com

Ray Driver

MANAGING DIRECTOR – DEBT & EQUITY
713.871.5801
rdriver@northmarq.com

Tony Gray

MANAGING DIRECTOR – DEBT & EQUITY
713.622.6300
tgray@northmarq.com

Trevor Koskovich

PRESIDENT – INVESTMENT SALES
602.952.4040
tkoskovich@northmarq.com

Pete O'Neil

DIRECTOR OF RESEARCH
602.508.2212
poneil@northmarq.com

Copyright © 2021 NorthMarq Multifamily, LLC.

The information contained herein has been obtained from sources deemed reliable. While every reasonable effort has been made to ensure its accuracy, we cannot guarantee it. No responsibility is assumed for any inaccuracies. Readers are encouraged to consult their professional advisors prior to acting on any of the material contained in this report.

