MARKET REPORT

Multifamily

Houston Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

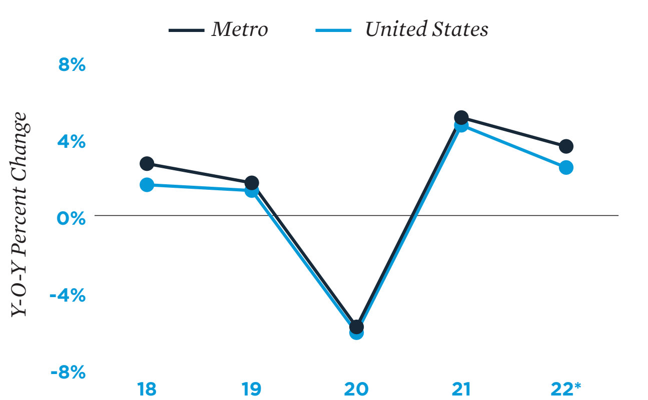
2Q/22

Widening of Rents Between Tiers Insinuates Brewing Tailwinds for Lower-Cost Units

Cost considerations will enhance lower-tier demand. Production and exports of energy goods accelerated in recent months, after sanctions were placed on Russia, supporting job gains in Houston's central industry. Elements of the supply chain for energy, as well as a multitude of other products, constitute a significant portion of employers in the market. The trade, transportation and utilities sector, as well as the manufacturing sector, comprise about 28 percent of total workers in Houston — a larger share than the national proportion. Many of these personnel traditionally receive wages in-line with costs for mid-tier apartment rentals, but conditions are changing. More residents in Houston will prioritize cost factors when searching for apartments in the coming quarters, after the rent spread between property tiers swelled last year.

Tight housing market facilitates momentum. Demand for higher-quality rentals is notable amid soaring home costs, with the difference between a rent obligation and a mortgage payment in Houston stretching to $1,100 per month in the first quarter of this year. Rentals also offer greater flexibility and amenities, while requiring minimal upkeep. Both the Class A and Class B segments logged vacancy rates of 3.8 percent or lower entering April, with each tier noting annual rent growth of at least 15 percent. Meanwhile, lower-tier rates increased marginally, thus the gap between Class C and Class B rates extended by roughly $150 per month.

Employment Trends



* Forecast

Sources: BLS; CoStar Group, Inc.; RealPage, Inc.

Multifamily 2022 Outlook

115,000 JOBS
will be created

EMPLOYMENT:

In March of this year, the employment total was about 24,000 roles below the February measure in 2020, before the onset of the health crisis. A full recovery, and then some, is achieved this year as Houston's worker count grows by 3.6 percent.

18,200 UNITS
will be completed

CONSTRUCTION:

For the fourth time in seven years, developers bring more than 18,000 rentals to market. Construction is heaviest in the CBD, as well as fast-growing suburbs like Rosenberg-Richmond and Spring-Tomball.

60 BASIS POINT
decrease in vacancy

VACANCY:

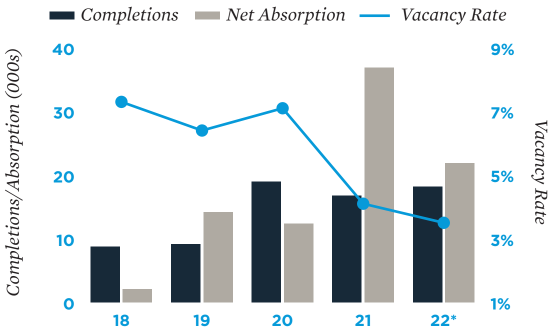
Houston's vacancy reduction in 2022 will rank second among major Texas metros, behind only San Antonio. Nonetheless, the projected rate of 3.5 percent at year-end will be 80 to 110 basis points higher than the three other Lone Star markets.

8.3% INCREASE
in effective rent

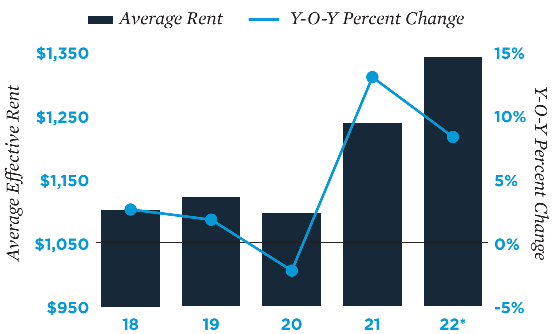
RENT:

The average effective rent climbs to $1,341 per month as vacancy falls and in-migration bolsters demand. Faster rent hikes in other areas of the Sun Belt could boost the appeal of Houston, which has a mean rent lower than at least 35 major U.S. metros.

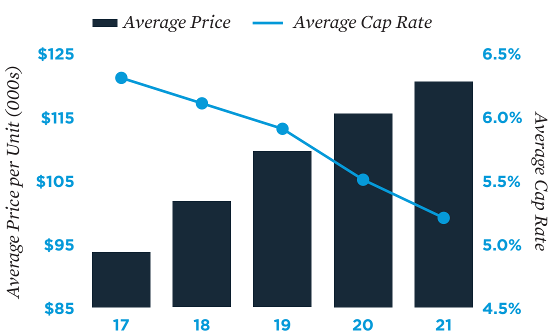
Supply and Demand



Rent Trends



Sales Trends



** Forecast*

Sources: CoStar Group, Inc.; Real Capital Analytics; RealPage, Inc.

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Price: $250

1Q 2022 - 12-Month Period

CONSTRUCTION

17,164 units completed

- Development was scattered in 2021. Seven submarkets added 1,000 to 2,500 rentals, and six other areas gained 400 to 1,000 units. The dispersed nature of construction mitigates localized supply headwinds.
- The average project in the pipeline has almost 300 units, and most are garden-style, as land constraints in Houston remain minimal.

VACANCY

390 basis point decrease in vacancy Y-O-Y

- In the first quarter of 2022, all 35 submarkets recorded year-over-year vacancy declines of at least 150 basis points, with drops exceeding 300 basis points in 28 of those areas.
- Metrowide, vacancy was measured at 3.7 percent in March. The number of available rentals shrunk by 27,200 units over the past year.

RENT

14.9% increase in the average effective rent Y-O-Y

- Top areas for rent growth over the past 12 months included rapidly growing suburbs like The Woodlands and urban corridors that appeal to young professionals, such as Greater Heights-Washington Avenue.
- Rent gains are slowest in submarkets with a greater share of Class C stock, where average rents are below $1,000 per month.

Investment Highlights

- Last year was the strongest for multifamily trading since 2018, with deal flow practically doubling the previous year's volume. The steep rise in $20 million-plus assets changing hands can be attributed to several factors. Institutions are active in Sun Belt markets like Houston, where elevated in-migration supports a positive outlook. At the same time, the market contains a swath of 200-plus unit properties, many of them built within the past decade. Newer apartments of this size command offers above $50 million, while an overall rise in per-unit prices, driven by competition, means large Class B/C properties are increasingly transacting for prices above $20 million, lifting dollar volume in the market.
- The average cap rate slid into the low-5 percent band last year, but returns above 6 percent are obtainable in pockets of the metro. Southeast Houston and Brazoria County are the predominant targets for higher yields and prices under the metro mean of $120,500 per unit.
- Local transaction velocity tripled annually in a handful of submarkets, headlined by suburbs like Sugar Land-Stafford, Cinco Ranch and neighborhoods surrounding Lake Houston. Higher-quality assets are attractive here amid a large-scale millennial shift to the suburbs.