MARKET REPORT

Multifamily

Philadelphia Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

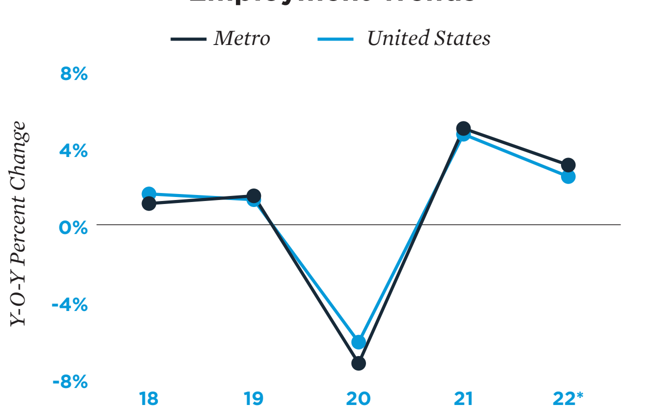
2Q/22

Supply Wave Hits Urban Core; Tax Amendments to Influence Future Builds

Gap narrows between suburban and urban assets. The average effective rent in the urban core ended last year just $700 above the suburban equivalent, down from a $1,000 difference prior to the pandemic. Development trends may see this gap continue to narrow. Additions slated for Center City and adjacent zones in 2022 could translate to more muted rent gains here. This continues the high rate of stock expansion observed last year, when Center City's supply expanded by 3.8 percent. Still, much of this supply pressure will likely be offset by a return to the urban core. In Center City, a year-over-year vacancy compression totaling 480 basis points was observed in March 2022, the highest of any submarket. Additionally, job growth in office-using sectors should support leasing in existing properties.

Policy change potentially impacts metro's long-term pipeline. Effective January 2022, the city of Philadelphia's previous 10-year, 100 percent tax abatement on new residential construction was amended to waive all fees for just one year after completion, with the abatement decreasing by 10 percent each subsequent annual. The multifamily permit volume surged at the end of 2021 as developers rushed to take advantage of the previous tax structure, so starts now look likely to balloon this year, setting the stage for delivery acceleration in 2023-2024.

Employment Trends



** Forecast*

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

Multifamily 2022 Outlook

90,000 JOBS *will be created*

EMPLOYMENT:

Expanding at a 3.1 percent clip, Philadelphia's employment base will outpace the national rate of expansion. Diverse job creation allows the metro's labor market to end 2022 on the cusp of full recovery, just 2,000 jobs under the pre-COVID-19 mark.

7,500 UNITS *will be completed*

CONSTRUCTION:

Developers are set to achieve a multidecade record for annual completions this year as metro inventory expands by 1.9 percent. Nearly 5,000 units are set to come online in the Philadelphia city limits.

0 BASIS POINT *change in vacancy*

VACANCY:

Despite rapid stock growth, metro vacancy is expected to hold at 1.9 percent. An uptick in unit availability may occur in Center City, due to scheduled deliveries here. This submarket is currently the single locale with vacancy above 3.0 percent.

8.5% INCREASE *in effective rent*

RENT:

While rent growth will decelerate from the 13.0 percent jump recorded in 2021, robust gains should continue as the average effective rent hits $1,744 per month. Tight conditions in suburban New Jersey locales could result in higher rent growth here.

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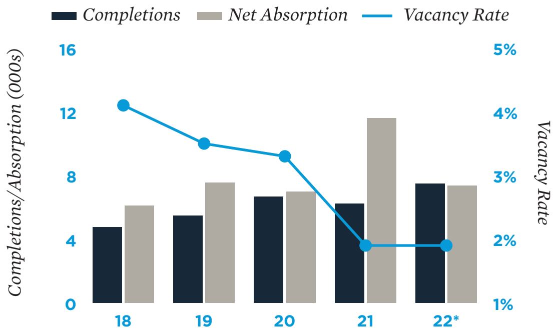
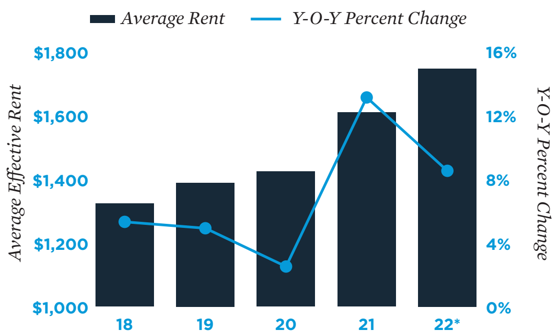
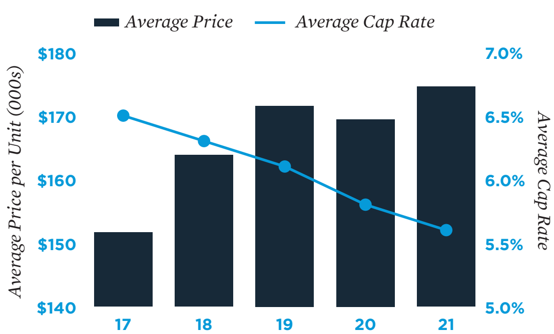
Supply and Demand



Rent Trends



Sales Trends



* Forecast

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

IPA Multifamily

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Price: $250

1Q 2022 - 12-Month Period

CONSTRUCTION

5,835 units completed

- Completions during the 12-month period ending in March trailed the prior yearlong span by 400 units. Still, rental stock grew by 1.5 percent.
- Center City, Chester County and Southwest Philadelphia underwent the greatest inventory transformations in 2021, with supply additions expanding these submarkets' apartment stocks by over 3.0 percent.

VACANCY

180 basis point decrease in vacancy Y-O-Y

- Frenetic leasing activity pushed metrowide vacancy down to 1.7 percent, the lowest rate of availability posted since before 2000.
- All apartment tiers closed out 2021 with sub-3 percent vacancy rates. Class A units observed the highest availability, though vacant units in this segment comprised just 2.8 percent of the market's luxury stock.

RENT

14.7% increase in the average effective rent Y-O-Y

- Tight availability translated to a multidecade record for rent growth, with effective rents closing March at $1,642 per month on average.
- While suburban rents observed consistent gains during the health crisis, the CBD did not surpass late-2019 highs until the first quarter of 2022. Low concessionary activity should drive rents higher here moving forward.

Investment Highlights

- Following a 2020 slump, renewed investor confidence brought last year's transaction velocity above the previous deal flow record set in 2018. Coinciding with improving fundamentals, last year also marked the return of positive pricing growth to the market, after a 1.2 percent dip the year prior. The average per-unit price ended 2021 at a new high of $174,600.
- Additional out-of-state capital was observed last year as Northeast-based investors combed the market for yields elevated above certain nearby metros. Buyers in this category are targeting Class B properties, which have been known to trade at high-4 to low-5 percent cap rates, although first-year returns can range lower for some assets with growth potential.
- Trades involving Class C properties continue to account for the bulk of sales activity. A drop in the average number of units in assets of this category traded last year indicates investors targeted smaller properties. Amid the large share of lower-tier transactions, a considerable jump in per-unit pricing is occurring across the property tier, narrowing the yield gap between Class B assets and this segment.