Hurricane Harvey: Multifamily Analysis

Storm Accelerates Lease Cycle; Effective Rents on the Rise



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- Pre-Harvey, multifamily absorption exceeded deliveries by almost 2,000 units, driving market-wide occupancy gains through August 2017.
- Hurricane Harvey coming ashore August 25th accelerated the multifamily lease cycle by approximately 18 months. According to a press release by Apartment Data Services (ADS) on September 15th, occupancy has tightened by 120 basis points (bps) while net effective rents have risen by 1.5% since the passing of the storm.
- A quickly draining construction pipeline—with less than 7,700 units underway—and reduced inventory due to flooding will cause supply to tighten while demand from displaced single-family residents, contract workers, and natural growth will orient leasing toward landlords.
- The storm will have acute, albeit brief, effects on the Houston area economy. Though job growth and economic growth will experience minor interruptions, a full employment recovery is expected by late-October, according to the Greater Houston Partnership, largely because Houston's economic base emerged from the storm almost completely unscathed.
- Housing was acutely affected in some areas, with an estimated 72,000 single-family homes damaged or destroyed. Houston's apartment market was significantly less affected than initial estimates, with approximately 10,600 units reported to be damaged according to ADS, with an 81% landlord response rate.
- CBRE Research will continue to monitor changing market conditions during the recovery period and will be releasing updates accordingly.

PRE-HARVEY: FUNDAMENTALS TIGHTEN AS DEMAND PLAYS CATCH-UP

Market-wide recovery of Houston's apartment fundamentals over the past 8 months has been solid. For example, year-to-date net absorption in 2017 stands at over 14,400 units, compared to a total of 4,500 units last year. This year's high-demand has been accompanied by a rapid draw-down in the construction pipeline, as the current development cycle is quickly winding down. A pre-Harvey supply and demand analysis indicates only 3,100 units are scheduled for delivery during 2018, with pre-Harvey demand forecasted at over 11,300 units for the same year.

CBRE occupancy models prior to Harvey's impact indicated a steady rebound in occupancy through 2020, with occupancy reaching the 90% threshold between 2018 and 2019. Pre-Harvey estimates signaled a market in equilibrium during 2018, with a full transition to a landlord-favored market the following year. A number of metro Houston economic indicators contributed to the strength of multifamily demand over the 12 months preceding Hurricane Harvey (Figure 1).

Figure 1. Houston Economic Indicators, Pre- and Post-Harvey

	Pre-Harvey	Post-Harvey
Job Growth, Unemployment	53,500 Aug. T-12 5.2% unemployed	Avail. 10/20/17
Home Sales	95,276 July T-12 All-time record	92,967 Aug. T-12 "Screeching halt before Harvey"
Houston PMI	51.8 in July 10 consecutive months >50	46.5 in Aug. Last week of Aug. surveyed
Population Growth	125,000 in 2016 2nd in the U.S.	N/A Minimal effects expected

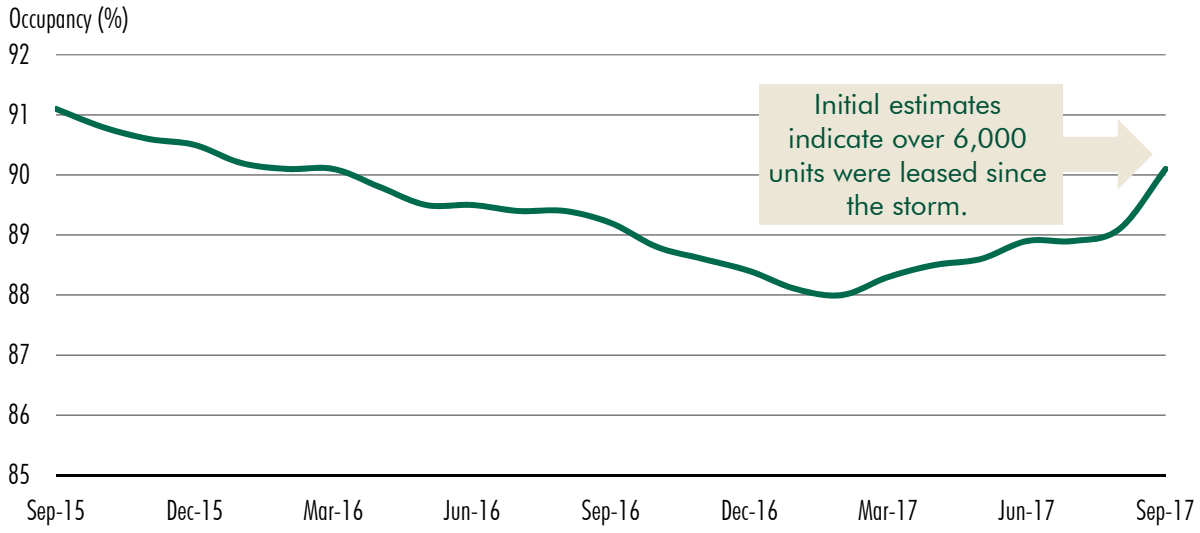
Source: BLS, ISM, MLS, September 2017.

POST-HARVEY: MARKET ACCELERATES, TRENDS TOWARD LANDLORDS

The demand from displaced renters and residents seeking temporary housing spiked dramatically after the storm—ADS estimates specify over 6,000 units have been leased in the weeks following Harvey's landfall. Houston's multifamily occupancy rose 120 basis points to 90.1% (adjusted for out-of-commission units) based on preliminary estimates from ADS (Figure 2). Harvey effectively accelerated the multifamily recovery timeline, propelling Houston into a landlord-favored market approximately 18 months ahead of schedule.

The spike in occupancy driven by Harvey related to leasing activity is expected to stay. In addition, a majority of rental concessions expired. A subdued development pipeline along with sustained recovery-driven demand is expected to pull down vacancy. These factors, buttressed by natural growth in Houston's demographics will drive demand for new supply during the recovery period.

Figure 2. Initial Data Shows Uptick In Multifamily Demand & Occupancy



Source: Apartment Data Services, September 15, 2017.

Given the risk of possible future flooding and the potential loss of equity in the event of another similar storm, a new segment of permanent renters could emerge. For example, older homeowners contemplating apartment living now have an additional motivation to shift from owning to renting. This housing change comes with a number of advantages such as the potential to reduce tax liabilities, lower maintenance burdens and several physical stories of separation from any future impeding floodwaters.

RAPID RECOVERY, ECONOMIC BASE INTACT

Hurricane Harvey is expected to have an acute, albeit brief, impact on Houston employment and economic base. Houston's main economic drivers—Port Houston, downstream petrochemicals, upstream energy, and healthcare—all emerged from the storm almost completely unscathed. CBRE Research estimates that less than 0.5% of Houston's office inventory was directly damaged by the storm, evidenced by the fact that upwards of 90% of employers reopened September 5, the Tuesday after Labor Day, and 95% were open the following Monday. While a brief dip in area employment and economic growth is expected, local economists estimate pre-Harvey employment levels to return as soon as this October and overall job losses to be minor.

The single-family housing market—Houston's most severely impacted property type—is estimated to have suffered approximately 72,000 damaged or destroyed homes, well below initial estimates which numbered in the hundreds of thousands. Texas Department of Public Safety estimates that approximately 3.3% of the Houston metro's inventory suffered minor damage (residences that are habitable within 30 days after repairs), while destroyed homes represent 0.1% of inventory.

MULTIFAMILY DAMAGE LOCALIZED

The multifamily market fared considerably better in some submarkets versus others, while market-wide damage was to limited to approximately 10,600 units, or 1.7% of Houston's total market inventory, according to an ongoing, but 81% complete, survey by Apartment Data Services. This survey-based figure, sourced directly from landlords, is expected to be a durable estimate of physically damaged units. Early third-party estimates were considerably higher, based on flood map analyses of impacted areas which vastly overestimated damaged inventory created solely on geography.

Based on preliminary damage reports, the multifamily submarkets most severely impacted are situated in the Northeast cluster, a collection which experienced damage in approximately 5.1% of its total inventory (Figure 3). Particularly hard hit were the Greenspoint, Lake Houston/Kingwood, Northeast Houston/Crosby, and I-10 East submarkets (Figure 4). Other submarkets experiencing substantial damage were those with significant exposure to Houston's extensive bayou system—the Med Center/Braes Bayou, Almeda/South Main, Energy Corridor, and Bear Creek submarkets all experienced above trend flood damage.

Figure 3: Estimated Units Damaged

	Units Damaged	Total Inventory	% of Cluster Damaged
Central	1,060	69,569	1.5
Southwest	2,591	197,642	1.3
Northwest	2,180	182,506	1.2
Northeast	3,172	62,598	5.1
Southeast	1,568	126,288	1.2
Total	10,571	638,603	1.7

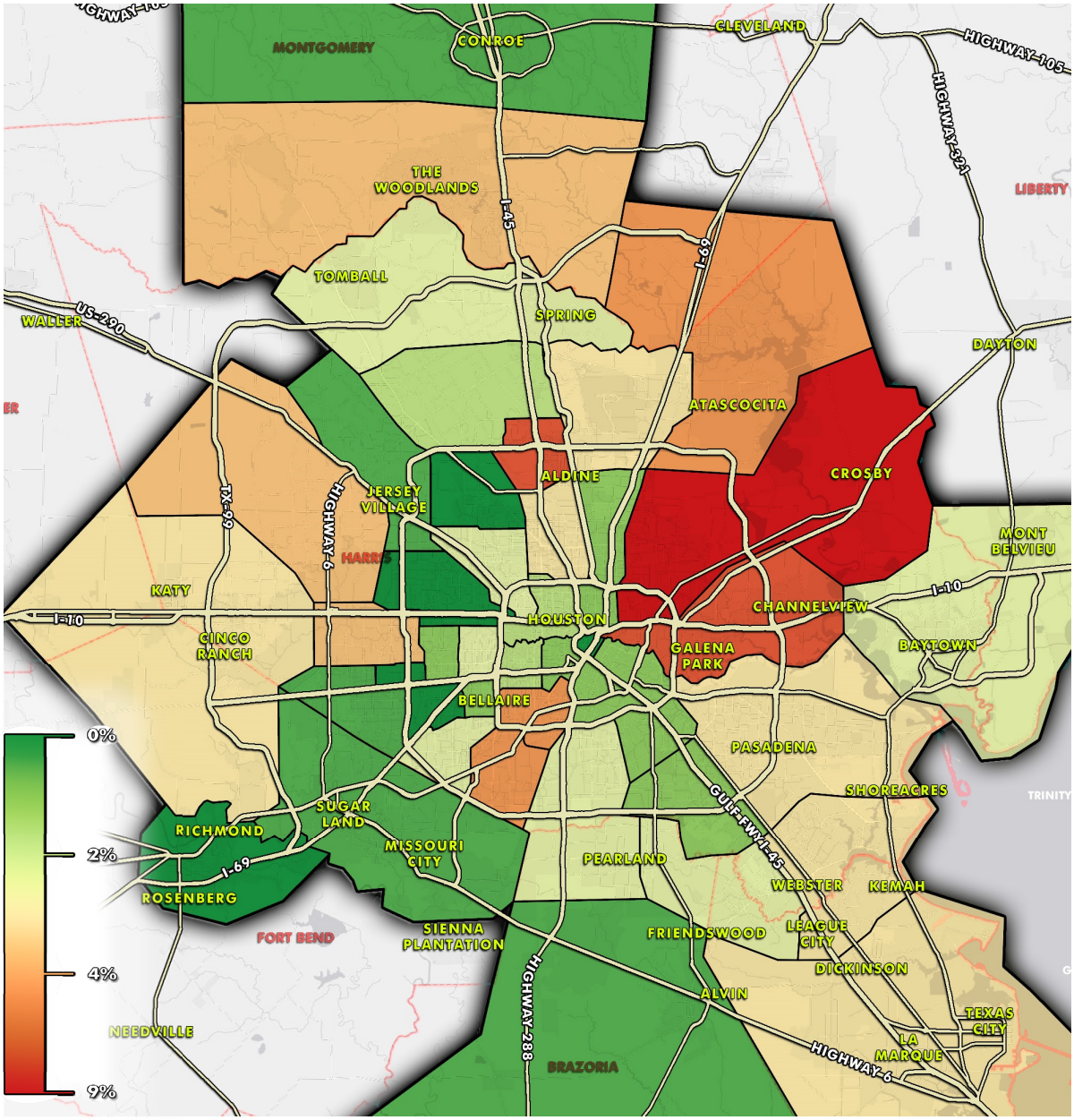
Source: Apartment Data Services, September 15, 2017.

ONGOING ANALYSIS THROUGH THE RECOVERY

Given the dynamic and complex nature of the area economy through the recovery efforts, CBRE Research will be providing ongoing analysis as more facts and data become available, chronicled in periodic updates to this current Viewpoint. Because of the reality of an evolving situation, CBRE Research will be paying particular attention to the issues outlined below:

- Information **projecting when offline units will return** to the market. Future editions of CBRE's supply and demand analysis will include such units in the 2018 supply, with some permanent removals expected.
- Reports of **labor shortages and rising construction costs will impact the pace of rebuilding**—we will look for quantifiable evidence demonstrating this effect.
- CBRE Research will consult with our brokerage professionals and report on aggregate data for **office and industrial users in the market**.
- CBRE Research will **listen to multifamily owners, landlords and industry experts** to collect real time market intelligence such as those recently suggesting that some homeowners will transition to permanent renters by choice.

Figure 4: Units Damaged as a Percentage of Submarket



Source: Apartment Data Services, September 15, 2017.

As of August 31st

Houston Apartment Market

Figure 5: Houston Metro Multifamily Supply/Demand Analysis

Houston Multifamily Supply vs. Demand Analysis for 2017 - 2020

	2016	2017	2018	2019	2020	Total
Projected Population Growth	130,800	132,000	133,100	130,800	126,700	522,600
(Source: Moody's Analytics | Economic & Consumer Credit Analytics 7/31/17)						
SUPPLY						
Number of Units Under Construction (Source: ADS; September 5, 2017)	0	4,166	3,135	357	0	7,658
Number of Units Recently Opened (Source: ADS; EOM August 2017)	0	12,476	-	-	-	12,476
Total New Supply 2017-2020:	0	16,642	3,135	357	0	20,134
DEMAND						
Multifamily Demand (1 unit / addtl 11.7 forecasted population)	11,141	11,244	11,337	11,141	10,792	*44,514
Projected Year End Occupancy	90.3%	88.0%	89.3%	91.0%	92.6%	90.0%
Net addition to inventory that would result in 90.0% occupancy						18,893

* Demand correlated with Moody's July 2017 job forecast is 47,880 units (based on 1 unit / 5 additional jobs)

Houston Population vs. Absorption

Year	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Total
Population	5,233,729	5,423,615	5,540,882	5,676,381	5,826,108	5,920,416	6,057,800	6,181,700	6,326,200	6,489,600	6,647,400	6,770,700	
Y-O-Y Δ	101,127	189,886	117,267	135,499	149,727	94,308	137,384	123,900	144,500	163,400	157,800	123,300	1,638,098
Absorption	34,860	-3,058	5,133	8,425	1,556	13,940	13,655	14,732	16,168	15,958	14,152	4,354	139,875
	2.90	-62.09	22.85	16.08	96.23	6.77	10.06	8.41	8.94	10.24	11.15	28.32	
	Total Population Increase Req'd to Absorb 1 Apartment Unit (Total YOY change / Total Absorption)												11.71

Total Number of Operating Units as of September 5, 2017	638,603 units
Occupancy as of September 5, 2017	89.1%
Class-A Stabilized Occupancy as of September 5, 2017	90.3%
Number of Units Absorbed YTD through August 31, 2017	14,437 units
Number of Units Proposed as of September 5, 2017	16,786 units
2017 Projected Deliveries	
Number of Units Recently Opened through EOM August 2017	12,476
Number of Units Under Construction Projected to Open by YE 2017	4,166
Total 2017 Deliveries	**16,642**
Number of Units Opened 2016	20,075
2016 Absorption (# of Units)	4,482

Population Forecast

Year	2017	2018	2019	2020
Population	6,904,500	7,037,600	7,168,400	7,295,100
Y-O-Y Δ	132,000	133,100	130,800	126,700
Absorption	11,244	11,337	11,141	10,792

Source: Moody's Analytics Forecast (July 2017)

**Data captures partial post-Harvey activity, as the majority of flooding occurred from August 27th to August 31st.*

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