

Apartment Resources is a monthly publication designed for apartment developers, lenders, and builders involved in all forms of multifamily housing.

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Section:

Market Hotline! takes a look at 1989.

*We've expanded our **Market Hotline!** this month to discuss our predictions for multifamily vacancy rates in 1989. Why haven't vacancy rates gone up as quickly as predicted? Where will they be going this year?*

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"Based on this information, we believe that vacancies, although stable in 1988, will increase slightly in the summer and fall of 1989."

The Future of Multifamily Housing—Part 2.

*Our special series on what's happening to multifamily housing continues this month with a special **Market Support Matrix (MSM)** showing national averages for new move-ins. You now have the ability to determine how your complex compares to the national average, and target your marketing expenditures more effectively.*

2

"In general, you should expect between 50% and 70% of your tenants from the Effective Market Area (EMA), with the typical average being around 60%."

Exciting new additions to REAL/LINE!

New market areas added on-line. And a redesigned and expanded REAL/LINE report gives you more vital information than ever before!

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Market Hotline! takes a look at 1989.

What lies ahead in multifamily vacancy rates?

- Developers often ask us about the overbuilding that has occurred in a number of multifamily markets for the past several years. From many of these developers, we hear two questions most often: If so much overbuilding has occurred, why have vacancy rates gone up only marginally in most areas? And, what impact will previous overbuilding have on the 1989 market?

To answer these questions, one needs to look both at multifamily development trends since 1986, and the outside forces that influenced them.

Since 1970, analysts at Kenneth Danter & Company have been examining multifamily development trends throughout the US by comparing area household growth and internal mobility to housing starts.

Our analysis bases housing starts in a given year on building permits issued the previous year, since in most cases the approximate time difference between a project's permit issue and preparedness for occupancy is a year.

- Developers first began to express concern when overall vacancy rates rose in 1987. Principally, that increase in vacancies was the result of the multifamily overbuilding which occurred that year.

The impact on multifamily development could have been greater, but, fortunately, the level of multifamily construction during the middle part of the decade fell below support levels, creating

multifamily deficits. Therefore, even in the face of overbuilding, most market areas found overall vacancies increasing only slightly. Without these prior deficits, the overall vacancy rate would have been much higher.

As a result, many developers in 1987 were concerned about what would happen in 1988. But again, these developers were fortunate in that building activity (according to 1987 building permits data) declined greatly. Some of this decline can be attributed to the Tax Reform Act of 1986, which chased many developers to the sidelines to wait out its impact. The result was a stabilization of vacancies in most areas.

- As 1989 building activity swings into full gear, however, there is much speculation on the continued impact of previous overbuilding. Although the 1988 building permits final report is yet to be issued, a review of permit activity through November finds that both single- and multi-family permits in a number of critical markets are running higher than for the comparable period in 1987.
- As we noted above, this trend is significant because permits issued in 1988 become housing starts in 1989. Based on this information, we believe that vacancies, although stable in 1988, will increase slightly in the summer and fall of 1989. A contributing factor is the current lack of prior development deficits. These deficits dampened the impact of overbuilding in 1986.

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This is not particularly good news for apartment owners and developers, but it is important to note that pockets of opportunity exist in most markets—for product that competitively addresses market demand in location, concept, and price. Further, developers who have learned from mistakes made in disasterously overbuilt markets are tending to diversify their development strategies into previously underserved areas.

- Another factor controlling the vacancy rate is the diversity of product. Although there is an increasingly large group of apartment tenants ready to jump to a single-family alternative, new multifamily developments that offer design, amenities, and features (along with the increasing cost of single-family home ownership) have kept this group “locked” into multifamily rental.

A concern of Kenneth Danter & Company is that government-sponsored housing programs may be initiated in the coming year that provide this market component with a pathway to single-family ownership.

Households in this component are typically characterized by high incomes, but little net worth. Usually childless, they have become accustomed to the lifestyle afforded to them in the newer upscale developments. We see the possibility of government programs being created that reduce the cash requirements necessary to move into single-family homes. Should this happen, vacancies could increase significantly.

- In summary, it is inevitable that vacancies will increase, possibly in excess of the rate experienced in 1986 and 1987. In most markets, the diversification of product and location will cause vacancies not to be concentrated in any one area. However, developers, project owners, and managers must keep a wary eye on their upscale, very mobile tenants.

What is REAL/LINESM, and what can it do for me?

REAL/LINE is the fastest way to evaluate a market area’s multifamily development potential. Users can access information on rents, vacancies, and market absorption—and a comprehensive analysis of the comparable market rents for projects based on their “amenity index.”

If you subscribe to this publication, you’ve already paid your system access fees. See the access summary below to learn how to sample REAL/LINE today!

Also, be sure to see this month’s **REAL/LINE Connection** for the latest updates on system features and additions.

REAL/LINE access summary

REAL/LINE is available 24 hours a day, seven days a week. Anyone is welcome to access REAL/LINE at any time, as our guest.

system prompts as follows:

First Name: **NEW**
Last Name: **USER**
Password: **DANTER**

To access the system, you need (1) a computer with modem attachment, (2) a terminal program for your computer (popular ones include Crosstalk, Smartmodem, and ProComm), and (3) the REAL/LINE phone number and password.

You’ll be given access to nearly every system feature, except the ability to download market reports. Of course, if you’re an *Apartment Resources* subscriber, you are entitled to a free subscription with full access to the system. For more information, call 1-(614)-221-9096 and ask for the REAL/LINE coordinator.

The REAL/LINE phone number is 461-8980. To enter the system, respond to the opening

REAL/LINE system defaults

To access REAL/LINE, you’ll need to make sure your terminal program is set up properly. You don’t really need to know what the following terms mean—just make sure they are set as listed:

Parity: **N**
Stop Bits: **1**

Duplex: **Full** (Or **Echo: Off**—depending on the terminal program)

Baud: **300 or 1200**
Data Bits: **8**

Also, most programs offer a *Filter or Strip 8th Bit* function. This should be turned OFF, although it is not critical.

The Future of Multifamily Housing—Part 2.

The Market Support Matrix (MSM)SM—National Comparisons.

Special Report Executive Summary

This report contains national comparisons for the nine “boxes” in our *Market Support Matrix (MSM)* analysis.

The comparisons are based on nationwide research of apartment markets throughout the US by Kenneth Danter & Company.

As introduced in the January 1989 issue of *Apartment Resources*, the MSM analyzes incoming apartment tenants by both *household* composition and *geographic* origin, and places these tenants in one of nine possible categories. By establishing the percentage distribution among these categories, developers and managers can target their marketing and development strategies to the most critical categories.

Tenants coming from within the Effective Market Area (EMA)SM account for approximately 60% of a project’s absorption. When tenants in this category are further distributed by household origin (basing percentages on total tenants), 6% come from new household formations, 9% are former homeowners, and 45% come from other apartments.

Tenants coming from outside the EMA, but within the immediate area, account for approximately 20% of a project’s absorption. When tenants in this category are further distributed by household origin (basing percentages on total tenants), 2% come from new household formations, 3% are former homeowners, and 15% come from other apartments.

Tenants coming from beyond the immediate area also account for approximately 20% of a project’s absorption. When tenants in this category are further distributed by household origin (basing percentages on total tenants), 2% come from new household formations, 3% are former homeowners, and 15% come from other apartments.

Considering geographic origin alone, 60% of new tenants come from within the EMA. 20% from beyond the EMA but within the immediate area, and 20% from outside the immediate area.

Considering household origin alone, 10% of new tenants come from new household formations, 15% from home ownership, and 75% from other apartments.

In nearly two decades of market analysis, Kenneth Danter & Company has analyzed multifamily housing support throughout the United States. Based on these analyses, and our continual in-house tenant profile surveys, we’ve developed numerous overviews of support characteristics in multifamily housing.

As a basis for comparison with your development interests, we’ve included in this issue of *Apartment Resources* a typical distribution of tenants in the Market Support Matrix as it applies to new tenants moving into a modern, market-rate housing complex.

A Summary of Market Support Matrix (MSM) Analysis. A complete introduction to Market Support Matrix (MSM) analysis appears in *Apartment Resources* Vol 3, No. 1 (January 1989). Space doesn’t permit reprinting that introduction here, but the following paragraphs outline the principles of this analytical technique.

Market Support Matrix analysis works by drawing a comparison between the type of housing (here called *tenure*) tenants are coming from, and the location (here called *geographic origin*) they are coming from.

Each of these two factors is subdivided into three categories.

When considering the *area* tenants are coming from (with respect to a project’s EMA), the tenants are either coming from *within* the EMA, *outside the EMA but within* the immediate area, or *outside* the immediate area.

When considering the *type of housing* tenants are coming from, they are either a *new household* formation, current *homeowners*, or currently occupying an *apartment*.

From these categories, a matrix is created with the three possible *tenure* characteristics down the left side and the three possible *geographic* characteristics across the top—nine “boxes” which can describe the origin of the tenant.

More important, by surveying your tenants or potential tenants for their origin characteristics, you can assign percentages to each of these “boxes,” which will tell you where you should be concentrating your marketing efforts. In addition, you will be better able to estimate the type of unit and project amenities your potential market requires or desires.

How does your project compare?

Although the MSM was developed to identify tenant mobility patterns and their impact on absorption projections for new projects, comparing the results of your analysis with national averages can help you identify local trends that are influencing the way your units are being absorbed in the market.

The national average Market Support Matrix appears on the following page. Details on each category follow.

Internal Mobility. New tenants moving into an apartment complex will come mostly from the complex’s Effective Market Area (EMA)SM. In general, you should expect between 50% to 70% of your tenants from this area, with the typical average being around 60%.

Within this tenant group, approximately 10% (6% of total tenants) will come from new household formations. Details of the possible sources for new household formations are given in Part 2 in this series (in last month’s issue of *Apartment Resources*).

Another 15% (9% of total tenants) will be former homeowners (or former residents of “other than modern rental” units). For various reasons, these tenants have sold their homes and turned (or returned) to rental housing.

But the greatest share in this section (and the largest of the nine possible categories) are tenants who are coming from other apartments. These tenants may comprise approximately 75%

(45% of total tenants) of the internal mobility tenant population.

External Mobility. As discussed in Part 2 of this series, external mobility is usually subdivided into two parts: tenants coming into the EMA from the immediate surrounding area, and tenants coming into the EMA from outside the immediate area.

Tenants in the “Beyond the EMA, but within the area” category will comprise between 15% and 25% of your tenant population, with an average being 20%.

Of these tenants, approximately 10% (2% of total tenants) are from new household formations, 15% (3% of total tenants) are former home owners, and 75% (15% of total tenants) will come from other apartments.

Tenants in the “Outside of immediate area” category will comprise another 15% to 25% of your complex, with the average once again around 20%. Of these tenants, approximately 10% (2% of total tenants) are from new household formations, 15% (3% of total tenants) are former home owners, and 75% (15% of total tenants) will come from other apartments.

The big picture. Notice that in the outer rows of the matrix, totals for each component of the matrix are given. As discussed above, in the *Geographic Origin Characteristics*, approximately 60% of your tenants will have come from within the EMA, 20% from outside the EMA, but within the immediate area, and 20% from outside the immediate area.

Under the *Tenure Origin Characteristics*, 10% of your tenants will have come from new household formations, 15% from home ownership, and 75% from other apartments. (For details on the impact of step-up support from other apartments, see “No-growth markets: A moving experience.” in the September 1987 issue of *Apartment Resources*.)

Of course, the figures given in this example are based on national averages. The actual figures for any housing development will vary depending on the type of housing offered and factors unique to the market area.

Market Support Matrix (MSM)* Housing Absorption (To Apartments)

GEOGRAPHIC ORIGIN CHARACTERISTICS

TENURE ORIGIN CHARACTERISTICS	Internal	External		
	Within EMA (50-70%)	Beyond EMA Within Area (15-25%)	Outside Area (15-25%)	
From New H-H Formations	6%	2%	2%	10%
From Ownership	9%	3%	3%	15%
From Apartments	45%	15%	15%	75%
	60%	20%	20%	100%

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Using the Market Support Matrix (MSM)SM Analysis

The Market Support Matrix (MSM) analysis looks at tenant mobility from two different perspectives—geographic origin and household origin.

Possible household origins (here called Tenure Origin Characteristics) appear down the left side of the matrix. Possible geographic origins (Geographic Origin Characteristics) appear across the top.

The matrix formed from these two perspectives creates nine “boxes” of tenant support. The percentages displayed in the nine boxes are based on the total tenant population.

On the outer edges of the matrix are subtotals and totals for each of the categories. Together, these percentages give you an at-a-glance analysis of the actual support components for your existing or proposed multifamily development.

Coming up in future articles. Now that we have established our methodology for analyzing tenant movement, and noted national trends for each of our nine “boxes,” our next issue of *Apartment Resources* will go one step further.

In our next special report, we’ll take a closer look at demographic statistics as they relate to the Market Support Matrix. We’ll dig deeper into

the component profiles of tenants in each category, and identify the market trends that created the national distribution discussed here.

We’ll also take a look at the how future trends are going to affect each component—and how your absorption and vacancy rates will be affected by them in the months to come.