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Inflation

Apartment Brokers: Amid Housing Recovery, Demand for Rental Units Still Robust

- *But Rent Increases Begin to Flatten After an Explosive Year-Long Surge*
- *Rents on Par With Cost of Ownership, but a Mobile Workforce Favors Renting*
- *A Captive Audience of Ex-Homeowners Also Keeps Occupancy Rates High*

By Gary Rosenberger

NEW YORK (EconoPlay) Oct. 11 – Demand for rental units remains strong, but rent increases may have hit a wall after a year of explosive growth – and are likely to plateau well into 2013, say brokers, landlords, and relocation specialists.

Pushback from consumers and growing inventories (in the way of new construction and old foreclosures) are putting a lid on those catapulting rent increases, which began last fall and had another burst in spring and summer.

Neither the housing recovery nor the fact that the cost of renting and ownership are now largely on par seems to weigh on the rental market.

That’s because there are a number of lifestyle and demographic factors that continue to favor the rental market. (Homebuilders are noticing and continue to build for the rental market – more on this in tomorrow’s housing outlook.)

The most reliable customers are the victims of the housing bust, who still have years to go before their credit histories become clean – and many are permanently turned off from ownership anyway.

A second factor favoring rentals lies in the nature of today’s job market, which is far more mobile than it has ever been – especially in technology, where contractors move from project to project, often crossing municipal, state, and international boundaries.

If you’re young, there’s also something inherently appealing in a vibrant downtown apartment – in contrast to the relative isolation behind a white-picket fence in some suburb, pegged down by a 30-year mortgage.

“Last year we were filled with exuberance. Things were on the mend and the rental market was picking up,” said Larry Rosenberg, president of RDNY (Rent Direct New York), the internet-based rental locator covering New York’ five boroughs and a bit beyond.

The market stayed “hot” through this past summer. “We saw rents go back up to damn near their high points,” he said. “I didn’t think we’d get there so quickly. But sure enough, it happened.”

But now, in October, he is beginning to see a “more cautious” market. “There are still plenty of people looking for apartments, but the willingness to commit has slowed down,” he said.

The Summer Rush Ends

Part of the problem is seasonal. “To be more specific, it’s a student thing,” Rosenberg said. “Right now we’re seeing the normal slowdown that happens after the summer.”

Newly minted grads “rush to New York City in the summer to find apartments ahead of job offers that begin in September,” he explained. And by now, upper classmen are settled in off-campus housing – so it’s two rushes with similar deadlines.

Anyone else looking for an apartment is probably hedging – waiting for rents to come back down. “I had been advising people that unless they need an apartment with some urgency, they better hold off until October,” Rosenberg said.

During that summer rush, he saw New York rents spike by as much as 15%, with the greatest increases in Manhattan (particularly for smaller one-bedroom units and studios). The softest increases were in Queens.

“But rents always do come down a bit as we approach winter,” he said. “How soon they start to decline, I can’t tell you. It usually happens in October or November. But by December, prices will be down.”

So what gave New York City that little extra kick last summer? Rosenberg thinks the rent increases and the added urgency reflect an accelerated economic recovery in the city. “New York is once again a magnet for recent grads,” he said.

He doesn’t query into people’s lines of work but suspects that advertising, technology, and marketing are making up for any stumbles on Wall Street or law.

“It’s still an upward trajectory. Upward, upward, upward,” said Kevin Miller, president of Westside Rentals, with seven offices between Santa Barbara and San Diego.

“Demand is through the roof. I thought demand six months ago was big. It’s flat out going nuts now,” he said.

Part of it is those foreclosures that created a generation of renters. "But lately there's been a major shift from Silicon Valley to Silicon Beach. And with not much new supply, you know what happens to rents," Miller said.

Rents in West LA have climbed "another 8 or 10 percent" since April, "which is massive," he said.

But LA is a big place with all kinds of neighborhoods and varying degrees of desirability. So he puts the average rent increase at "closer to 2.5 percent."

A Tech Hotbed

But Silicon Beach, a swath roughly encompassing Santa Monica, Venice Beach, and Manhattan Beach is a technology hotbed. "It's tech people coming down from San Francisco. Companies are opening up massive offices. Facebook, YouTube, Google are opening up 100,000-square foot offices and hiring like crazy. The influx has been unbelievable," Miller said.

"You hear about the southern California economy sucking. But when it comes to technology, it's far from sucking," he said. "We have so many advantages over Silicon Valley. We have 340 days of sunshine. Office rents are cheaper. But probably the biggest thing is an employment pool of 10 million people, which is 10 times the employment pool they have in Silicon Valley."

It's not just the big companies. "A ton of smaller startups are moving in to be near the likes of Facebook without the San Francisco rents," he said. "It's booming here. Commercial rents are rising, but people coming down from San Fran just see a bargain."

This is the kind of jobs recovery that probably doesn't appear on the BLS radar. "So many of my friends don't get a paycheck, but they're trying to build a company and build a brand," Miller said. "They work and share office space – you'll see 30 companies under one roof that allow young entrepreneurs to have an office where they can be creative at one tenth the cost."

And all these people, while they're maxing out their credit cards, have to live somewhere. "You can get a beautiful house in Santa Monica for $3,500 a month," he noted. "What's putting us in such a good spot is that nobody can get a loan. Even if you have a job and good credit, you just can't get a loan. Banks are so tight. They won't even refinance. It's brutal. So they rent."

And then there's one last thing to consider. In the tech world, jobs are very mobile. Contractors jump from assignment to assignment, from city to city. "These tech jobs come and go. You can't be locked into a 30-year-mortage," Miller said.

“We stayed pretty steadily up, up, up through May,” said Jeff Rowe, vice president at CORT Destination Services in Cincinnati, Ohio, a national relocation service provider.

“We had a strong year all the way through. But we saw things tail off somewhat over the last few months. It’s hard to say why,” he said.

He recently attended an employee relocation conference where there was widespread agreement that, after a strong year, the growth potential is dissipating.

“Our competitors and our customers anticipate very small growth in 2013, most are saying a flat year,” Rowe said. “Some blame the election and the economic uncertainty ahead. But it looks like a flat year for everybody out there.”

A Flatter Horizon

At a separate conference on the multifamily housing industry, many executives felt that rent increases are likely to plateau going forward. “Last year vacancies were so low. We had 97 percent occupancy and were seeing rents growing, in some cases 10 to 20 percent,” Rowe said.

But at some point you run into the laws of diminishing returns and no matter how high those occupancy rates remain, that level of rent increases can’t be sustained.

For one, he explains, there’s that ever-present shadow inventory of single-family and condo foreclosures that tend to become rental units – prompting an excess of supply.

“When they had very low vacancy, landlords got aggressive with rents. But there’s an enormous amount of single-family homes coming online to compete for the renter – I’ve heard estimates of 2.5 million foreclosures that have yet to hit the market,” he said.

Even if the cost of renting is now on par with owning, he is not seeing a swing to buying among transferees.

Rowe argues that renting is an accepted lifestyle with benefits over ownership. Renting removes the fuss and bother of ownership (property taxes, maintenance, roller coaster valuations) and offers amenities (fitness centers, Wi-Fi, a social network) that don’t come as easily in the white-picket-fence suburbs.

“Mobility is another big thing for a lot of people. If you want to thrive in today’s job market, you have to have the ability to be mobile and not be tied down from a real estate standpoint,” Rowe said. “Interest rates at an all-time low – no question there are values out there. But most of the transferees that we are helping to relocate, including those coming from abroad, choose to rent.”

Indeed, the desire for job flexibility is so great these days that corporations are insisting on “break-lease” clauses in the event of a new assignment (or worse).

“From 2011 to 2012, things were looking phenomenal,” Rowe said. “But from a relocation standpoint, we’re no longer seeing the explosive growth. From 2012 to 2013 it’s plateauing. It had to happen at some point.”

Great, Good, and So-So

Joy Anzalone, chief operating officer at Burton Carol Management in Cleveland with properties in Ohio, Michigan, and Florida, continues to see a broad recovery, especially in places that were once written off as economic basket cases.

“The Detroit suburbs continue to be awesome. Occupancy is great and has been the entire year,” she said.

“We’ve had waiting lists all year,” she said. Physical vacancies are at 3% in her Detroit properties, mostly from natural turnover – but that goes down to virtually zero when counting approved applicants waiting to move in.

“The Cleveland area continues to be better than it has been in many years, and we feel that occupancy is strong,” Anzalone noted.

“Obviously at this time of year, traffic becomes less. But we are moving into winter in better shape than in previous years. Rent increases continue to be modest, but at least they are moving in the right direction,” she said.

Vacancy rates in her Cleveland properties are about 5%, but when counting approved applicants, the reality is closer to 3%.

Florida, while improving, “brings up the rear,” she said. It still suffers from stubborn supply issues. Too many houses that went bust are now rentals (including condo reconversions to rental units). “Buyers are chasing apartment deals in Florida,” she said.

“The apartment market continues to be great for investors who take care of their properties because renters always look for well-managed and maintained properties,” Anzalone said.

“This is a very good time to be in this business,” she added. “Renting is a lifestyle choice. The last four years have taught us that owning a home is not a be-all and end-all.”

"The rental market in our area is very strong," said Dick Dohack of the Dohack Group in Fort Myers, Florida. "Many homeowners have been displaced due to a foreclosure or short sale and need to rent for two to seven years until their credit is restored."

On top of that, seasonal rentals are getting a lift from economic uncertainty. "Many people who would be buyers decide to rent for a time until they have more peace of mind about the economy," he said.

But inventory is now in short supply, which creates more demand for rentals. "All of this is working out for the investors that snapped up bargains at the bottom of the market," he said.

But despite all that, "rents are unchanged," he said.

The U.S. Labor Department is scheduled to release PPI data for September on Friday, Oct. 12 and CPI on Tuesday, Oct. 16 both at 8:30 a.m. ET.

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