

Inflation

Apartment Brokers: Modest Job Growth Fuels 1Q Rentals Rebound; Rents Up Slightly

- *Relocating Workers Favor Renting Over Buying; Young People Especially Opt to Rent*
- *Landlords Negotiating Less, Giving Fewer Concessions, Raising Asking Rents*
- *Vacation Rentals Easily Beat Year Ago; Asking Prices Stay 'Flat' amid Less Discounting*

By Gary Rosenberger

MIAMI BEACH (EconoPlay) Mar. 11 – The slow jobs recovery has ushered in a solid rebound in apartment rentals at a time when home sales continue to languish – suggesting a demographic shift away from homeownership, brokers say.

At the same time, market power has begun to shift toward landlords, who just a year ago were loath to raise anyone's rent and offered a month or two free rent to draw new tenants.

Landlords are now offering fewer concessions (two weeks free instead of two months and no upgrade on appliances) – and are pushing for straight-out rent increases on renewals and turnovers as vacancies get filled.

Markets that were hit hard by the recession (like Florida, Michigan, and Ohio) are again seeing high occupancy rates that bode for rent increases down the road.

It is not clear what's driving the rebound – but it probably comes down to a combination of factors: the soft jobs rebound, more relocations, an aversion to investing in real estate, and the demographic bulge of echo boomers too busy paying off college loans to buy a home.

“The uncertainty in the sales market has certainly helped the rental market,” said Debbie Done, president of Apartment Search, a locator service in St. Louis. “It's a busier year overall. We're seeing a lot of bounce-back. People are so gun-shy about buying.”

People are relocating to St. Louis – but “not buying off the bat.” And people who move away are choosing not to sell in a weak market, and becoming first-time landlords.

So inventory is up, but there are also more people in the market for apartments – and more are staying put, “so there's not as much turnover,” Done noted.

“Apartment prices are creeping up and landlords are offering fewer concessions than they did a year or two ago,” she said. “We used to see one and two months free rent. Now we're seeing two weeks, if we see anything at all.”

Between fewer concessions and slightly higher rents, she estimates effective rents in St. Louis are increasing by around 5% over last year.

The cost of fuel and utilities has only become a topic of conversation in the last two weeks. Typically, fuel costs are the responsibility of tenants, so they wouldn't affect asking rents. But the price of gasoline does increase the cost of commuting, which could be a problem for the exurbs. "Fuel prices may prompt people to look for a home closer to work," Done said.

Tenants continue to make demands before moving in, but that too has been toned down. "I saw more demands for new appliances last year and the year before that. But the market was so soft then. There are still a lot of tenant demands. But that's dwindling because the market is tighter. There's not as much availability," she said.

What's truly unusual is that demands for upgrades and low rents have abated in the midst of a bad winter, when apartments just sit (nobody likes to move during a snowstorm).

"This was one of the toughest winters. We had enormous amounts of snow – and one storm after another. It was just a mess. But the fact that we're doing well bodes well for spring and summer," Done said.

Recovery

"Our feeling in all three of our markets is that things are getting better, absolutely – not worse," said Joy Anzalone, chief operating officer at Burton Carol Management in Cleveland with properties in Ohio, Michigan, and Florida.

It still takes "really aggressive" management to be profitable because rents aren't as high as they were. "But we are decreasing our specials and increasing rents. We are still trying to get rents back to where they were at the peak of the market [before the dotcom bubble burst] in 2000," she said.

Since that earlier burst, the market has been sporadic – a strong comeback track from 2003 to 2006 in Florida, and then the unwinding in 2008 and 2009. Michigan and Ohio have also climbed back in recent times.

Michigan is an especially impressive story. Vacancy rates for her properties now below 3%, which Anzalone describes as "outstanding."

"I'm very bullish on Michigan," she said. Her company is looking to buy more properties there, and recently closed on one in Novi outside Detroit (as well as in Westlake, Ohio).

So who are the new renters? "I don't sense that foreclosures have been a primary reason for increased occupancy," Anzalone said. "Apartments have become a lifestyle decision. People are so used to living on the edge, and not knowing when another shoe will drop, that they feel it's not a good time to buy a house."

The big surprise is “how many creditworthy people who could easily afford to buy a house in our markets choose to rent,” she said.

She didn’t specify a percentage increase in rents but the combination of fewer concessions and rent increases on renewals and turnovers adds up to “moderate” increases. “That’s better than zero, which is what was happening a couple years ago,” she said.

If rents are rising, so are costs. “Cities are going broke and they’re always looking for ways to charge assessments. Utility companies are raising rates, with water and sewer being the worst. We’ve experienced electric rates going up. Although natural gas has been steady,” she said.

The killer winter has also done a number on operating costs. “I’m sure the plow companies are thrilled this year,” Anzalone said. Her hardworking staff has been busy clearing snow since Dec. 1 – with another 10 inches or so expected before the weekend.

But weather aside, “our tomorrows are looking much better than they did over the last two years,” she said.

Coming to the Canyon

“This might be the busiest January, February, and March that we ever had,” said Mark Verge, owner of WestsideRentals.com, an apartment locator service in West Los Angeles.

People are migrating to Los Angeles hoping to land a job in the entertainment industry – or moving to West LA around Venice Beach, which is home to a growing tech sector, he said.

“Rents are solid. They haven’t moved very much, up at most 5 percent,” Verge said. “It’s the usual story: Price too high and your building is empty. Price it right and your building is full.”

Foreclosures might be part of the story, but it’s not a driving force anymore. “The quality of the tenants is very high,” he said.

On the other side of the coin are landlords – “still willing to negotiate but not too much,” Verge said. “I don’t see as many concessions here as I did before.”

Ralph Barocas, owner of RDNY.com (Rent Direct New York), the internet-based rental locator, is looking forward to the summer selling season for the first time since the collapse of Lehman Brothers.

For one, vacancy lists are shrinking, adding urgency to the apartment hunt. “Wall Street was bailed out and is now solvent again. So, hopefully, all the college kids that that were not getting Wall Street jobs the last two years will be getting jobs this year,” he said.

Business also came back “a bit” despite one of the harshest winters in the city’s history. “We’ve seen an increase in business the past month or so, which means there *could* be a season this year, unlike last year and two years ago,” Barocas said.

One sign that things have improved for landlords is they have pulled back on “OPs” (where *owners pay* the broker fees). “They feel they no longer have to offer incentives to brokers to bring in tenants,” he said. One building he lists went from 17 rentals to two.

Rents have stabilized or, in some cases, are still dropping – with more play at the higher end. And the bad winter also prompted slight rent decreases at the lower end. But once the season begins to heat up again by summer, he expects rents to rise again.

The big wildcard is still jobs. “Companies that survived the downturn, and I include my own company, are more efficient. Even if the economy does come back to where it was, they’ll never go back to the same amount of staff,” he said. “I used to have 20 support staff. Now I’m down to seven. Will I hire a couple people more? Yes, but I’ll never go back to 20.”

The suburbs of New York City are still glutted with unsold homes and landlords face stiff competition for renters.

“Houses are renting, but it is still a price-sensitive market,” said a Larchmont broker. “There is a lot of inventory. Tenants have become very picky. They want new appliances, updated kitchens and baths. They want a lot for little money.”

A Demographic Shift

In Atlanta, where the jobs recovery has been near nil, occupancy and rents have managed to rise anyway, said Dale Henson of Dale Henson Associates, market advisors to the multifamily industry. (The information below is culled from his latest year-end Atlanta Apartment Market Tracker and Pipeline Report.)

The 22,300 new units delivered during 2007 to 2010 coincided with plunging employment levels that have yet to begin recovery, resulting “in a pit much too deep to detect any strong evidence of overall recovery during 2010,” he said.

Atlanta occupancy levels advanced only 130 basis points from 88.3% at the end of 2009 to 89.6% at the end of 2010. At the same time, effective rents barely budged, moving from \$761 to \$763, according to his report.

Bringing down those numbers is a huge inventory of outlying garden apartments that can’t compete with the amenity-laden urban apartments closer to downtown. Those urban properties “easily out-performed” in 2010, registering 4.1% effective rent increases with occupancy up 270 basis points to 94.0%, Henson said.

Henson looks to 2011 as a “recovery year.” Only 168 new units are starting construction, down from 9,000 in 2009! But can the market recover without jobs? Apparently so.

“Employment growth, long the primary demand indicator for apartments, has apparently lost its predictive powers – at least for this period, in Atlanta,” he said.

Delaying home purchases and moving from single-family homes to apartments, along with the onslaught of the 25 to 35 year-old demographic – a group that seemingly prefers to rent – are the primary sources of new rental demand, Henson said.

The Hamptons Life

It might be too early to get a handle on summer vacation home bookings. But so far they look to be much better than last year. The Hamptons almost certainly illustrate how Wall Street, which arguably caused the recession, got off scot-free.

“The summer vacation rental market has been extremely busy this year,” said Meg Salem, vice president at Saunders & Associates, a Bridgehampton brokerage.

“We had a lot of activity around the New Year and then it died off when the snow came. But now that the snow has melted, the warmer weather and sunshine is bringing customers out again,” she said. “Everybody remembers the beautiful weather we had last summer and is getting ready for another great season.”

Owners are “pretty much” listing for similar prices as last year. “But there’s less negotiation. Many of my renewals have been at slightly higher prices – less than 5 percent,” Salem said.

Bookings in Martha’s Vineyard are “amazingly better” but still have not caught up to the 2008 peak, said Ann Floyd, owner of Sandcastle Realty in Edgartown, Massachusetts.

“But we’re getting close,” she said. Floyd credits a broadened internet presence and a better consumer mood. “I also think people are just tired of the winter.”

While nobody has raised rents, discounts are harder to come by – and one of her best booking weekends came when the Middle East and oil prices monopolized the news channels.

Rick Elliott, president of Elliott Beach Rentals in Myrtle Beach, South Carolina, foresees a “very good season, overall” this summer.

But he is spotting an impact from higher fuel prices. There has been a lull in bookings in the last two or so weeks – “so we’re going back to the days of cash for gas deals.”

Advanced bookings are “on par” with last summer – when the Myrtle Beach area grabbed market share from Gulf Coast beaches following the BP oil spill.

But people also come to play golf and eat out in the winter months – so January, February, and March have been “three of our biggest booking months.”

He is intent on raising rents to make more revenue for owners this year – particularly for top-end units that he feels were underpriced. The majority of those increases will come by way of reduced discounts – with increases for those top properties.

In California’s Wine Country, the state’s economy and competition among landlords do not allow for rent increases, said Ellen DeProto, vacation rental manager at Russian River Vacation Homes near Napa.

“I don’t see any difference in the level of bookings from the last couple of years,” she added. “Where I have noticed a change is in the demand for some of our larger properties – for family reunions and corporate events. That’s something that we haven’t seen in the last two years.”

She does not worry too much about fuel prices. “We’re a destination for the Bay Area and an easy drive, so high gas prices this summer could help us as much as hurt us. It will certainly help us if people decide to stay close to home,” DeProto said.

The U.S. Labor Department is scheduled to release PPI data for February on Wednesday, March 14 and CPI data on Thursday, March 15, both at 8:30 a.m. ET.

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