

APARTMENT ADVISORY

JULY 2021

While concession usage increased somewhat during the COVID-19 pandemic downturn, discounts were significantly below the levels seen during the Great Financial Crisis of 2007 to 2009. The difference today is that more and more operators and asset managers are realizing that costs outweigh the perceived benefits when it comes to concessions.

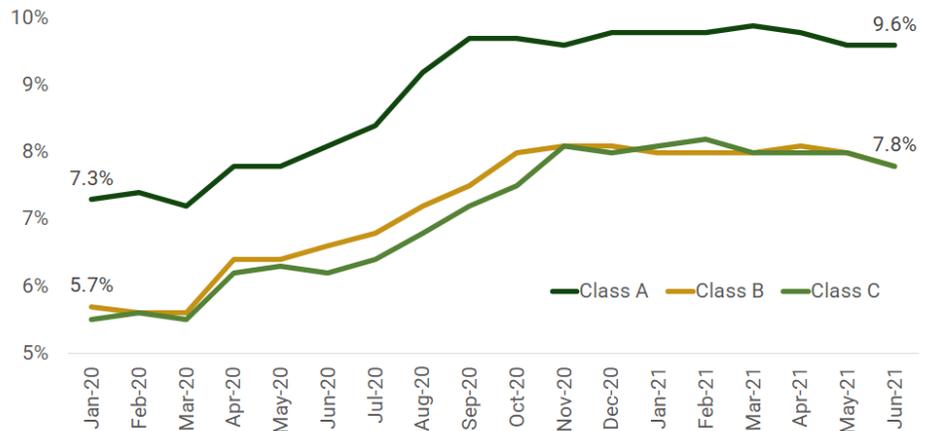
Rental concessions are a pricing strategy used to accelerate the lease-up of new properties as well as to fill vacant units in existing properties. Some units may be harder to lease because of market oversupply in a specific unit type, less desirable floor plan, location or access, view, and so forth. Concessions also tend to be used more heavily when overall market conditions become more competitive or challenging, such as during economic recessions. That was certainly the case during the Great Financial Crisis of 2007 to 2009. But with the COVID-19-driven recession, that wasn't the case - and rightly so.

RealPage data shows that use of concessions in the COVID-19 era peaked in May of last year when discounts were offered for 16.1% of the vacant available units. The giveaways have lessened since then, to 8.6% in June 2021. For comparison, going back to the

recession of 2007 to 2009, use of concessions spread to a stunning 54.7% of the available product. That's a big difference.

ushering in a shift toward effective pricing and away from free rent in properties where occupancy is stabilized.

Class A Concessions Dominate



Source: RealPage, Inc.

Influencing the much more limited use of concessions this time around, occupancy has stayed much, much higher than it was in 2007 through 2009. In fact, U.S. apartment occupancy reached a decade high of 96.5% in June. Also, the use of revenue management pricing is much more common these days, with revenue management systems

Further, market conditions were quite different between the two recessions. The Great Financial Crisis of 2007 to 2009 was brought on by underlying structural weakness in the U.S. economy, while the recent economic downturn was brought on by a worldwide health crisis. As such, government-mandated business closures and stay-in-place orders resulted in many apartment residents staying put wherever they were currently renting. Leasing activities were largely put on pause, further limiting renter movement and concession shopping among prospective renters, thereby making concession usage less common.

Add to that, over the past decade the use of revenue management software has become much more prevalent. As more properties use revenue management systems, that essentially negates the need for a bulk discount up front in the form of rental concessions. Instead, revenue management can take incremental cuts over the term of a lease to make smarter

Fewer Operators Offering Concessions



Source: RealPage, Inc.

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adjustments to smooth out cash flow for the operator and to avoid sticker shock when it comes time for a resident to renew.

Looking at average concession value as a percent of asking rent over roughly the past year and a half, Class A concessions have generally run higher than those for the rest of the nation's stock. This makes sense, as concessions remain a common strategy used by apartment operators to encourage lease-up of new properties. Accordingly, the more new supply seen in a particular market, the more likely pricing pressure will result in concessions being offered on new units as they become available. However, concessions offerings in this luxury product space didn't spike with the onset of COVID-19.

As of June 2021, concessions as a percentage of asking rent registered 9.6% in Class A units and were at 7.8% in both Class B and C units. The percentage increase from before the pandemic downturn in February 2020 to June 2021 for each of the three product classes was just over 2%, meaning that for the units offering concessions as

Deepest Class A Concessions



of June, the concession amount wasn't that much higher than it was before the arrival of COVID-19 in the U.S.

It's no surprise that many of the individual apartment markets resorting to the largest concessions in the COVID-19 era were among the hardest hit from job losses from the pandemic-induced economic decline. The list of the top 10 largest concession markets was comprised almost

entirely of the more expensive coastal gateway markets. In June, New York City topped the list with a 13.7% discount on asking rents. Other markets with double-digit concessions included San Francisco (12.2%), Portland (10.9%), Newark and Seattle (each at 10.5%), and Boston (10.3%).

The use of concessions in some markets is relatively commonplace even during normal economic conditions, so it's interesting to look at which of these markets are currently offering concessions above their normal discounts. Again, New York tops the list – the current discount is about 6% higher than the pre-pandemic norm. The Bay Area is next in line, with concessions running about 5% higher than before COVID-19. San Jose and Oakland are offering concessions about 4% higher than usual. Most of the other high concession markets are running closer to 3% above average.

Diving deeper into markets with the deepest concession discounts on Class A product in June, the list is once again dominated by coastal gateway cities. However, this time a few other markets are sprinkled in, including Columbus, Cleveland and Greensboro/Winston-Salem.

Gateway Markets Log Big Concessions



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