

# APARTMENT ADVISORY

SEPTEMBER 2021

The COVID-19 pandemic has accelerated a lot of pre-existing apartment market trends, as well as the discussion surrounding many of those trends and topics. One of those key topics has been the issue of housing affordability. Rental rates are growing at their fastest pace ever, so from that perspective, it may seem that affordability is becoming a big concern for the industry.

In the grand scheme, however, affordability challenges probably aren't as significant as some might fear. That isn't to say that affordability isn't a concern in specific instances. But the gold standard measurement for apartment affordability - the rent-to-income ratio - suggests pressure is less pronounced than advertised.

RealPage data collected from more than 12 million lease applications indicates the rent-to-income ratio for the U.S. overall is 22.6%. In other words, 22.6% of an applicant's income goes towards rent.

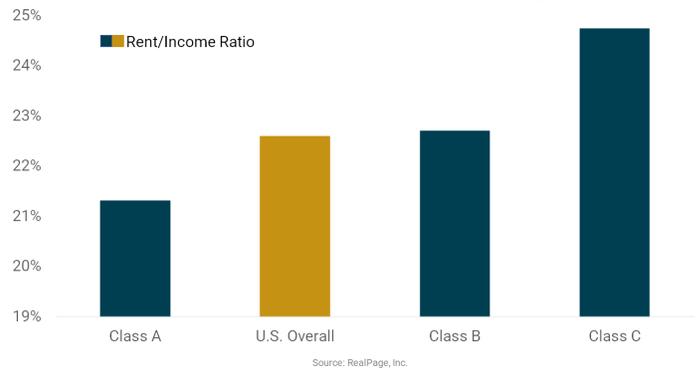
If rental rates are growing at their fastest pace ever, then how have rent-to-income ratios kept from becoming unbalanced? The answer is multifaceted but one of the key inputs is simply that renter incomes have grown considerably over the past year.

According to RealPage's proprietary research, the average renter income as of August 2021 sits around \$70,000. That's nearly 10% more than the \$63,800 average renter income last August.

The rise in renter incomes points to tight labor market conditions spurring wage growth. A growing amount of evidence points to the tight labor market such as help wanted signs everywhere and data suggesting that job openings today are well above pre-pandemic levels. With a mismatch in labor availability and employer need, wages have risen to combat employee turnover.

An ancillary yet still important trend with easing rent-to-income ratios points to migration trends over the past years. This primarily points to residents moving out of the expensive, coastal markets and into more

## Class A Rent/Income Ratio Lags



affordable areas. As renters keep their original income levels from their previous market - for example, San Francisco or Los Angeles - while relocating to a more affordable rental market - such as Phoenix or Las Vegas - those rent-to-income ratios are lessened as a result. There are questions how much of this migration is temporary versus permanent, but as it currently stands the migration movement shows up in the rent-to-income data.

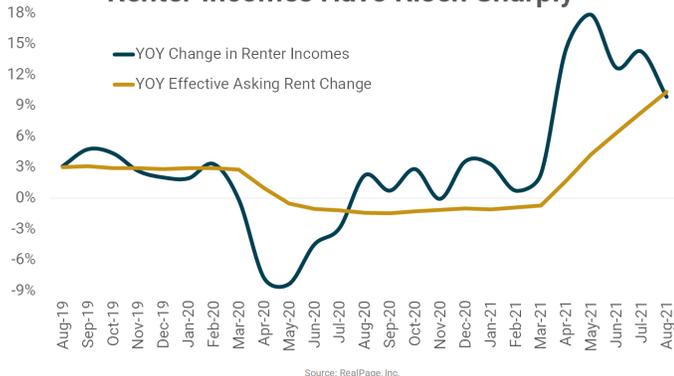
Rent-to-income ratios begin to show some difference when broken out by asset class. Class A rent-to-income ratios (21.3%) sit below the national average overall, which reflects that there are a lot of renters by choice living in those luxury properties. Class A rents as of August 2021 are about \$2,000, or \$450 more per month than Class B rents. In turn, that signals that Class A income levels above the Class B product tranche. Class B rent-to-income ratios closely align with the U.S. overall. Lastly, Class C assets have the highest rent-to-income ratio at 24.7%.

Breaking out these rent-to-income ratios by market shows there is some variance from place to place. Still, the overall variance - ranging from 19.6% on the low end to 26.5% on the high end - doesn't necessarily show a massive shift between metros.

The lowest rent-to-income markets are generally in the Midwest, with a few South region markets included. In fact, four of the five lowest rent-to-income markets are located in the Midwest or the Rust Belt. Pittsburgh, St. Louis, Kansas City, and Cincinnati - each with ratios around 20% to 21% - fit a similar profile of slower growth, mature economies with limited new construction. Further, these metros have some of the most affordable single-family home markets in the country which further limits upside potential for rent.

Altogether, this leads to a cluster of lower rent-to-income ratios in the region. The highest rent-to-income ratio among Midwest markets belongs to Cleveland - although the rent-to-income ratio of 22.0% is still below the U.S. norm.

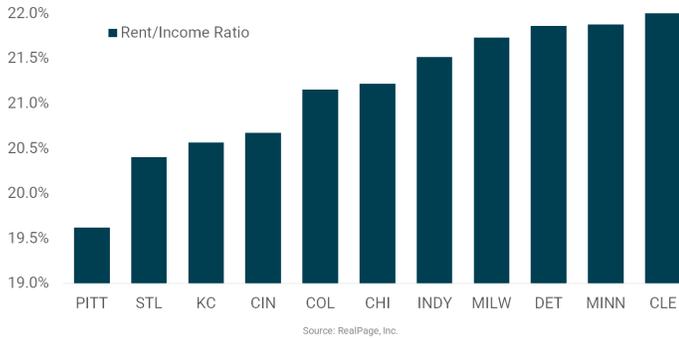
## Renter Incomes Have Risen Sharply



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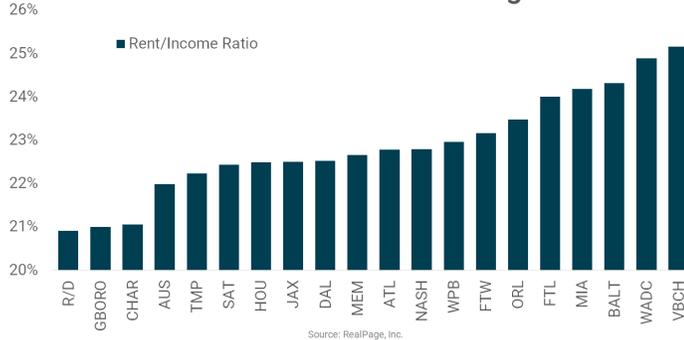
## Midwest Region Rent/Income Ratios Run Behind the U.S. Average



Three South region metros make the list for most affordable rent-to-income ratios, all three being the primary North Carolina markets: Raleigh/Durham, Greensboro/Winston-Salem, and Charlotte. Rent-to-income ratios there are closely aligned, ranging from 20.9% to 21.1%.

The next most affordable South region market based on rent-to-income levels is Austin. Austin is a great example of a metro that's likely benefited from recent in-migration from higher income states like California. Austin boasts one of the South region's highest rental rates, but as residents have moved into Austin from higher-income areas, that has at least partially informed a falling rent-to-income ratio.

## South Region Rent/Income Ratios Have More Variance Than Other Regions

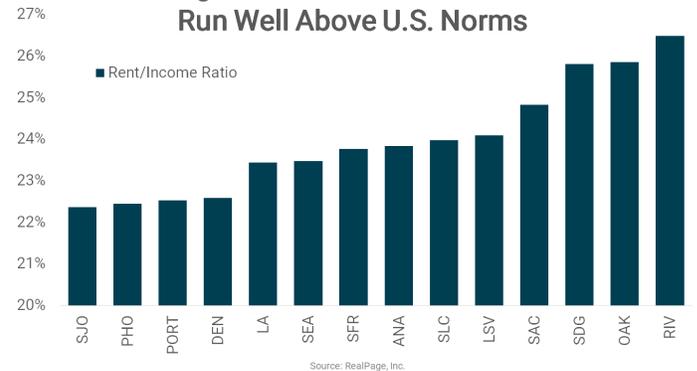


While Washington, D.C.'s rank as one of the nation's least affordable markets probably isn't too surprising, it may come as a surprise that Virginia Beach is actually the region's least affordable with a rent-to-income ratio of 25.2%. In fact, it's the fourth highest in the country and one of only four markets with rent-to-income above 25%.

Shifting focus to the West region, it's probably not too much of a surprise that the nation's least affordable metros are often found out west. The rank of those markets, however, may be somewhat surprising.

Remarkably, the West region's most affordable market is San Jose, which has one of the nation's highest average rental rates but a rent-to-income of just 22.4%. But San Jose's Silicon Valley boasts a cluster of many of the nation's highest paying industries with its technology presence. Also the hefty rent cuts that have affected the market over the past year have likely caused that rent-to-income figure to come down as well.

## West Region Rent/Income Ratios Tend to Run Well Above U.S. Norms

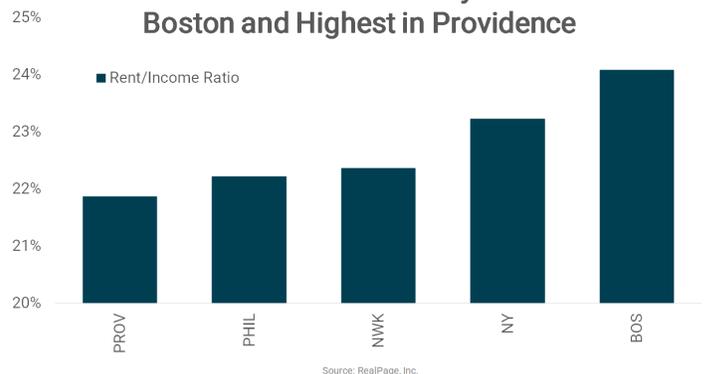


By comparison, neighboring San Francisco (rent-to-income of 23.8%) ranks middle-of-the-pack by regional standards. But Oakland's rent-to-income ratio of 25.9% is actually second highest both regionally and nationally. In the case of Oakland, that likely reflects lower incomes levels than its neighbors.

The nation's least affordable market by rent-to-income standards is Riverside at 26.5%. Riverside's rent-to-income ratio reflects a very blue-collar economy by regional standards, alongside exceptionally rapid rent growth throughout much of the past two years despite the pandemic.

Lastly, the Northeast region features a slate of metros where rent-to-income ratios run roughly in line to slightly above the U.S. norm. Boston leads the region with a 24.1% rent-to-income ratio while Providence, RI comes in with the lowest (21.9%).

## Northeast Market Affordability is Lowest in Boston and Highest in Providence



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