Trepp®

CMBS & CRE Research

October 2016

High Demand and Dwindling Delinquencies Drive the Multifamily Market

According to Freddie Mac's 2016 Multifamily Outlook report, last year produced the greatest amount of new supply to hit the multifamily sector in a single year since 1989. High demand kept up with the supply of 381,000 new units, which boosted rent prices and kept vacancy rates low. This year, the level of new supply has continued to rise, although it appears to be decreasing from the boom in 2015. An increased number of new multifamily construction permits were issued last year, but supply is hitting the market at a slower pace. According to Fannie Mae's July report, 80,000 new apartment units had begun construction in Q1 2016. This compares to 109,000 in Q2 2015, which was the highest number in a decade.

Fitch Ratings reports that construction, particularly in the Class A and student housing sectors, is still escalating. However, these segments may be at risk of overbuilding. According to Fannie Mae, new multifamily developments are disproportionately concentrated in major markets such as New York, Denver, Seattle and Boston. National job growth has become more evenly distributed, so supply might outpace demand in those major markets. However, current multifamily occupancy is strong across the board and has remained near historic highs thanks to the flourishing rental market.

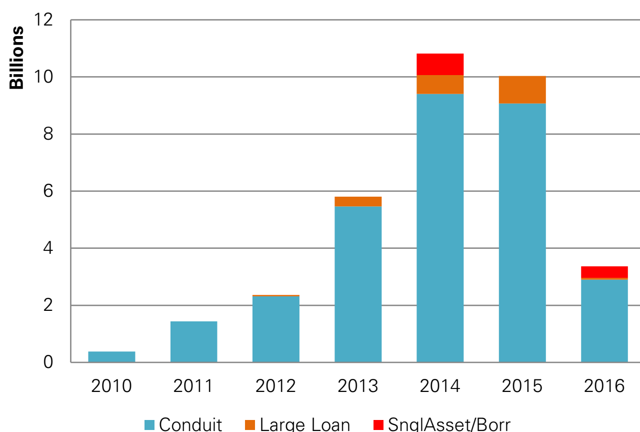
The momentum of month-to-month rent growth has started to decelerate this year, suggesting that the market has passed the peak of this growth spurt. Average monthly rent dropped from $1,220 to $1,219 in September 2016, marking the first such decrease since November 2015. A September report from Yardi Matrix shows that year-over-year rent growth remains solid at 4.7%, which indicates that the slowdown in multifamily rent is an adjustment to more sustainable levels for long-term growth.

CMBS Issuance

Trepp data shows that multifamily CMBS issuance in 2016 has dropped sharply from the huge volume originated in 2014 and 2015, though it is not the only property sector to experience this sort of decrease. Private-label CMBS lenders have scaled back origination due to rising concerns over market volatility and the implementation of risk retention rules. According to Trepp, CMBS issuance through the first half of 2016 only accounted for 7% of the overall CRE lending market, compared to 18% last year.

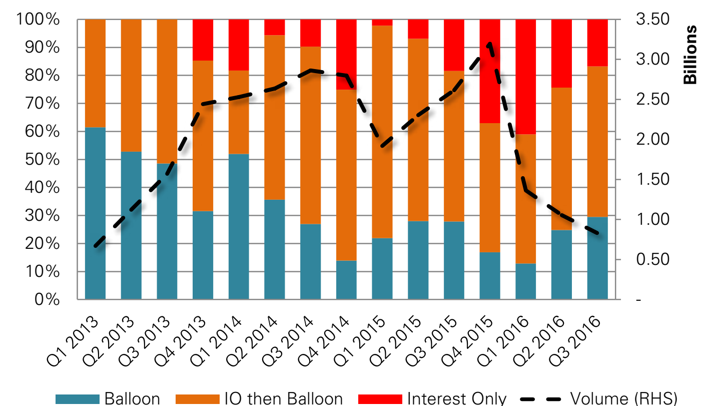
Many in the commercial markets have December circled on their calendar for two reasons: there could be an interest rate hike announced that month, and the new

Multifamily Issuance by Deal Type



Source: Trepp

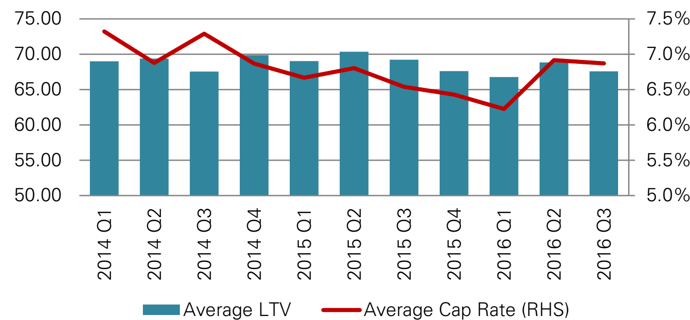
Multifamily Issuance by Loan Type



Source: Trepp

risk retention regulations will become effective. Risk retention requires CMBS lenders to hold a 5% slice of each deal they issue for five years. Concerns regarding these two events explain the steep drop in issuance. Trepp data reflects that conduit, single-borrower, and large loan CMBS issuance for multifamily properties totaled $10.8 billion in 2014 and $10 billion in 2015. The 2016 year-to-date total comes in well below those numbers at just $3.2 billion.

Conduit Multifamily LTV & Cap Rates



Source: Trepp

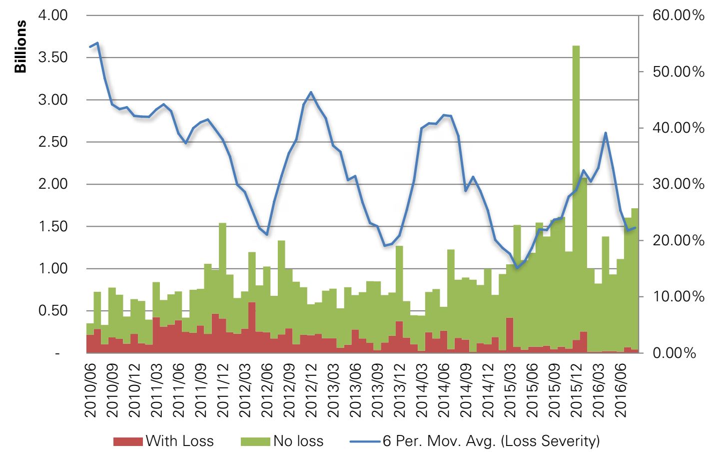
The increased use of interest-only loan structures over the past several years indicates a competitive lending market. The proportion of full- and partial-term IO loans in new multifamily issuance has grown from 56.1% in 2013 to 78.9% thus far in 2016.

According to Trepp, LTVs remain relatively flat, fluctuating between 66% and 71% since 2014. Looking more closely between this year and last year, average LTVs are slightly lower in 2016. Coupled with a drop in overall issuance, this suggests that credit standards have begun to tighten. The average conduit LTV for 2015 was 69.1%, and the average thus far in 2016 is 67.7%. Cap rates for conduit multifamily loans have been compressing since Q2 of 2015, signifying market heat and a bidding up of multifamily property values. The weighted average cap rate dropped from 6.5% in Q2 2015 to 5.3% in Q2 2016. This number may have stabilized as the Q3 2016 produced an average cap rate of 5.2%.

Losses & Delinquencies

Average loss severity for disposed multifamily loans has fluctuated around 30% since 2011, and has continued

Losses on Disposed Multifamily Loans



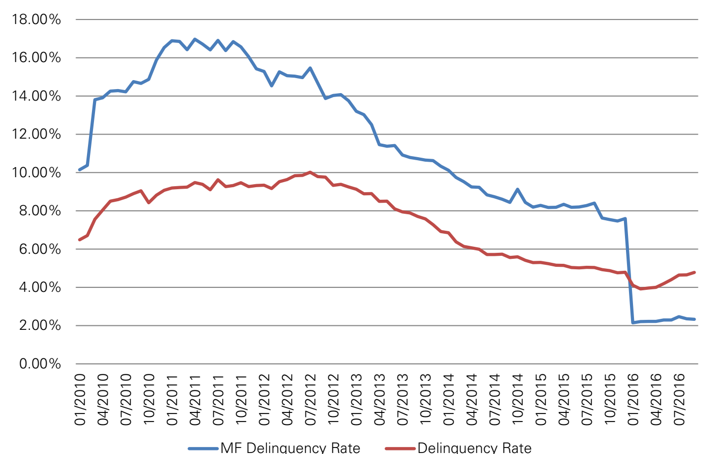
Source: Trepp

on that pattern in 2016. However, the volume of loans disposed with losses has decreased from 17.6% in 2014 to 7.6% in 2015, and now 4.4% this year.

The multifamily delinquency rate has also undergone a consistent decline since its peak in 2011. In the second quarter of 2011, the multifamily delinquency rate topped off at 16.7%, making the multifamily sector the worst-performing major property type that year. By 2015, multifamily delinquencies shrank to about half that size, hovering between 7.5% and 8.4% consistently throughout the year.

The massive debt behind the Stuyvesant Town-Peter Cooper Village Complex in New York City made up

Multifamily Delinquencies



Source: Trepp

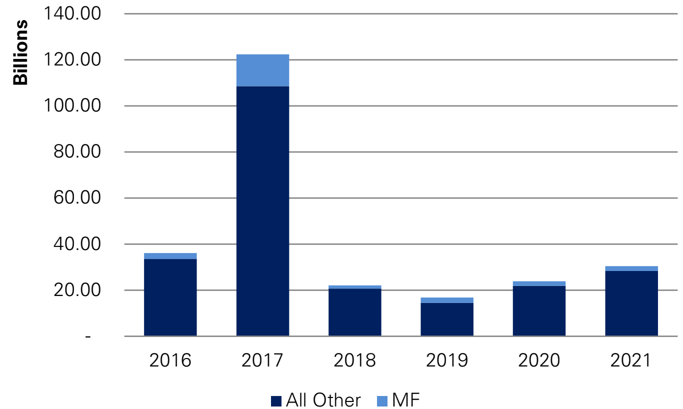
$3 billion of that delinquent balance, until its sale to Blackstone last December. The sale paid off debt behind five different CMBS deals and caused an almost-vertical drop in the multifamily delinquency rate from 7.6% to 2.15% in January 2016. The rate has remained relatively steady throughout the year, and came in at 2.3% for September 2016. The multifamily delinquency rate fell below the national delinquency rate (4.8%) for the first time since 2008 following the StuyTown resolution.

Outlook: Upcoming Mass of Maturing Loans

The "wave of maturities" will continue to wash up an immense amount of CMBS debt over the next 14 months. About $36 billion outstanding in private-label CMBS debt is due to mature over the remainder of 2016. Multifamily debt represents about $2.6 billion, or 7.2% of that total. Over $120 billion in non-agency CMBS debt is slated to mature in 2017, $13.9 billion (11.3%) of which is comprised of multifamily loans.

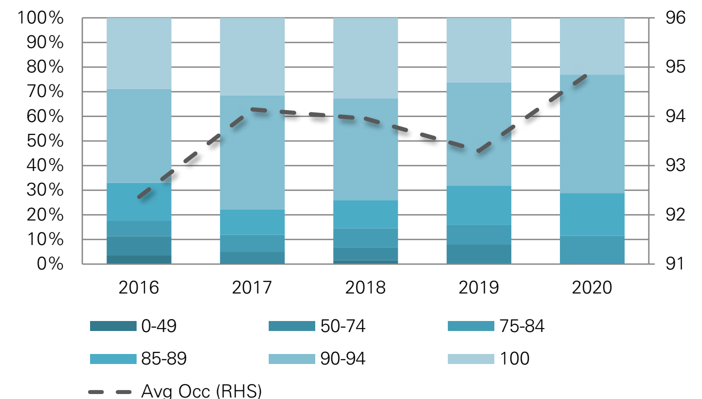
For loans maturing in the next five years, occupancy exceeds more than 90% in over half of the backing properties. Less than 20% of the properties have reported occupancy levels lower than 85%. The steep demand for multifamily housing is expected to last, as the millennial demographic will continue to drive the rental market forward and keep occupancy levels high.

Maturing Multifamily Loans



Source: Trepp

Maturing Multifamily Loan Occupancy



Source: Trepp

For inquiries about the data analysis conducted in this research, contact press@trepp.com or 212-754-1010.
For more information about Trepp's commercial real estate data, contact info@trepp.com

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