

2023 Q1

Mid-Atlantic Apartment

OUTLOOK

A Market Report for Multifamily Investors & Executives



Washington Metro Area First Quarter 2023 Trends



Class A absorption is near the long-term average, with 8,484 Class A units absorbed in the 12 months ending March 2023. Absorption including Class B product totaled 7,557 units.



Metro area Class A rents increased by 3.2% over the 12-month period ending March. For Class A and Class B combined, metro area rents increased by 3.8%.



The **stabilized vacancy rate for all classes of investment grade apartments increased by 70 basis points** over the past year and now stands at 3.2%; **Class A vacancy experienced a 110 basis-point increase to 4.3%**.



The **36-month development pipeline is up** from a year ago to 44,346 units, due to increases in Suburban Maryland and the District. Northern Virginia experienced a decrease.



14,404 units started construction over the 12-month period ending March 2023. During the first quarter, 2,080 units started construction.



Meanwhile, **10,848 units delivered in a 12-month span ending March 2023** and another 15,605 units are scheduled to deliver over the next year.

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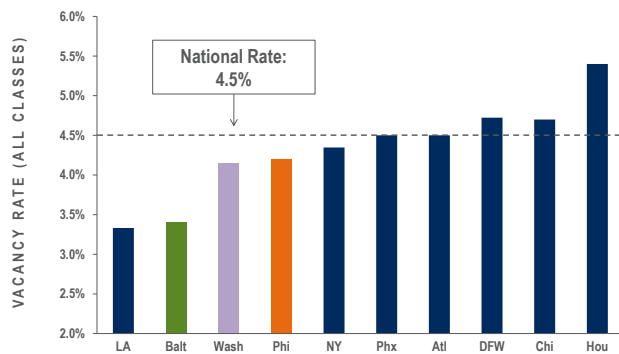
WASHINGTON METRO AREA CLASS A MARKET

STEADY ABSORPTION AMID A RISE IN CONCESSIONS AND HIGHER VACANCY

The highly-competitive Washington metro area Class A apartment market ended the first quarter of 2023 with below-average rent growth and rising vacancy, while absorption remained steady. Rent growth has softened some in recent months, especially in the District as concessions have become more prevalent. Meanwhile, vacancy is up across the metro in all substate areas. Net absorption met or surpassed deliveries in the suburbs over the past year while in the District, a wave of new deliveries has outpaced absorption. We expect competitive market conditions to persist as deliveries are expected to rise significantly in the suburbs over the next two years, similar to the heightened level of deliveries in the District over the past 12 months. Higher construction and financing costs have resulted in a slowdown in construction starts over the past several months; however, new starts were up in Suburban Maryland during the first quarter.

APARTMENT VACANCY RATES

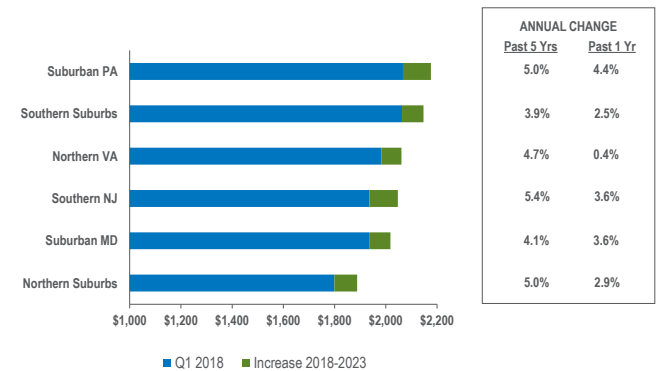
Major Apartment Markets | Q4 2022



Source: Reis, Delta Associates, March 2023.

ANNUAL AVERAGE EFFECTIVE RENT GROWTH

Mid-Atlantic Class A Low-Rise Apartments | March 2023



Source: Delta Associates, March 2023.

SUPPLY/DEMAND AND RENT OUTLOOK

While the 36-month pipeline remains elevated across the metro area, absorption continues to moderate, resulting in an increase in vacancy. When the prior year's absorption is compared to the development pipeline at the submarket level, 14 low-rise submarkets in Northern Virginia and Suburban Maryland have less than four years of supply (or one year's worth of product overhang). Twelve of these submarkets have less than two years of supply and could be considered supply constrained. There are six high-rise submarkets with four years or less of supply and one with two years or less. This suggests development opportunities exist in submarkets throughout the metro area post-pandemic.

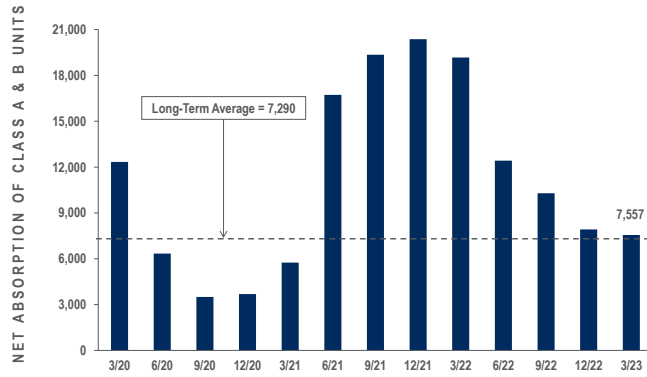
Another way of looking at the development pipeline at the submarket level is new supply relative to existing inventory. In 14 low-rise submarkets, the projected oncoming supply over the next 36 months represents less than 10% of existing inventory. Among high-rise product, no submarket has oncoming supply

representing 10% or less of existing inventory. In submarkets where new pipeline represents a relatively smaller increase in inventory, negative impacts on vacancy and rent growth will be less than in other locations.

Given projected absorption and the delivery schedule of projects currently under construction, we expect the region-wide vacancy rate for stabilized Class A apartment properties will increase by 80 basis points in three years compared to today - resulting in a metro-wide rate of 5.1%; we expect vacancy to fluctuate in the interim. We expect rent growth to continue moderating closer to the long-term average in 2023 and beyond. Rent growth will average between 3.2% and 4.2% in 2023 - 2025.

ANNUAL NET APARTMENT ABSORPTION

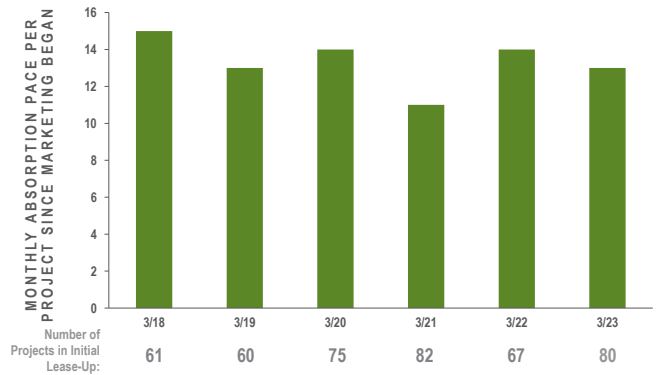
Class A & B Units | Washington Metro



Source: Delta Associates, March 2023.

ABSORPTION PACE PER PROJECT PER MONTH

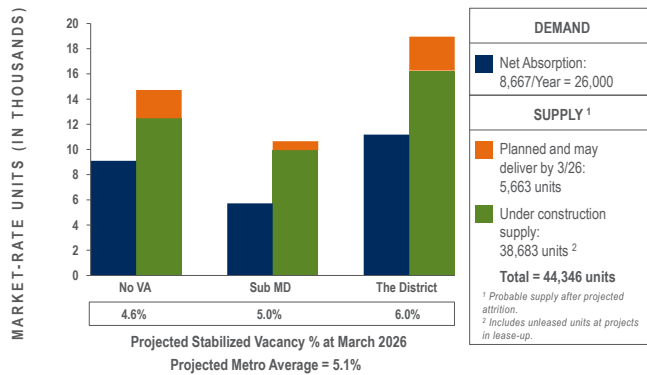
For Projects in Initial Lease-Up | Washington Metro



Source: Delta Associates, March 2023.

DEMAND AND SUPPLY PROJECTIONS

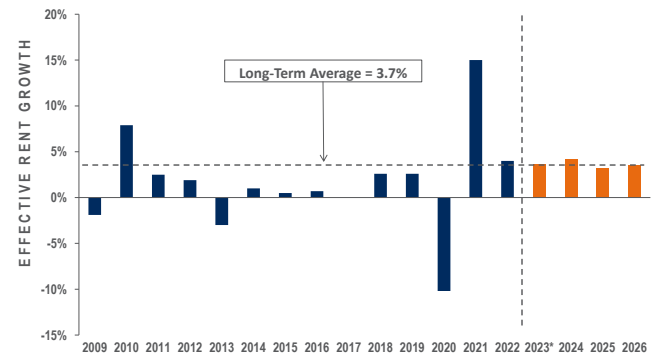
Washington Metro Class A Apartment Market
March 2023 – March 2026



Source: Delta Associates, March 2023.

ANNUAL CLASS A APARTMENT RENT GROWTH

Washington Metro | 2009 - 2026



Source: Delta Associates, March 2023.

*Annual rent increase of 3.2% as of Q1 2023.

DEMAND NORMALIZING

Class A apartment absorption in the Washington area was 8,484 units over the year ending March 2023. About 42% of the units absorbed over the past year were in the District, which recorded 3,532 units. Absorption was down significantly in all three substate areas, with the District recording the highest demand of its counterparts, although a decrease of 53% over the year. While absorption is down significantly from the prior year, demand is normalizing after setting a record in 2021.

We project annual demand averaging about 8,650 Class A units over the next three years with stronger absorption over the next year as the apartment market continues to recover, then moderating some.

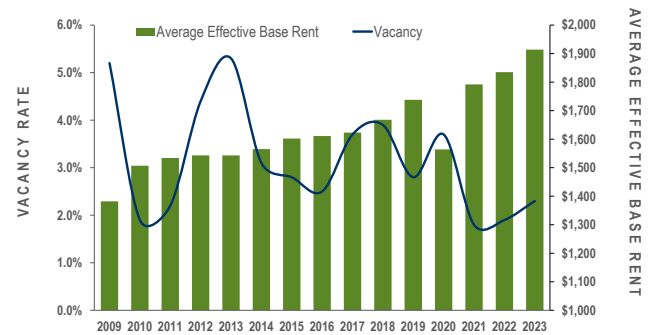
WASHINGTON METRO AREA CLASS B MARKET

RENT GROWTH REMAINS ABOVE-AVERAGE, VACANCY STARTS TO RISE

The Washington metro area Class B multifamily market has continued to stabilize in recent months as vacancy remains at low rates and rent growth stays elevated. Annual rent growth was positive in all but three submarkets in the Washington metro area. Metro-wide, Class B rents are up 4.4% in the 12-month period ending March 2023. Class B rents on average have fully recovered from the effects of the pandemic as they are now 11.0% higher than they were at the beginning of the crisis back in March 2020; with Suburban Maryland rents up 13.0%, Northern Virginia rents up 8.8%, and District rents up 5.7%. Meanwhile, vacancy increased in two sub-state areas from a year prior: in Northern Virginia by 50 basis points and in Suburban Maryland by 40 basis points. The District saw no change in vacancy year-over-year. Despite the slight increase in Northern Virginia and Suburban Maryland, all three sub-state vacancy rates remain well below their respective historical averages.

EFFECTIVE RENT AND VACANCY RATE

Class B Apartments | Washington Metro Area | 1st Quarter 2009 – 2023



Source: Delta Associates, March 2023.

- > Suburban Maryland up 4.2%
- > Northern Virginia up 3.9%
- > District up 9.1%
- > Metro-wide low-rise up 4.6%
- > Metro-wide mid and high-rise up 4.0%

AN OVERVIEW OF THE CLASS B APARTMENT MARKET AT FIRST QUARTER 2023 BY SUB-STATE AREA:

The Trend Since First Quarter 2022

NORTHERN VIRGINIA



EFFECTIVE RENTS

▲ 3.9%

SUBURBAN MARYLAND



EFFECTIVE RENTS

▲ 4.2%

THE DISTRICT



EFFECTIVE RENTS

▲ 9.1%

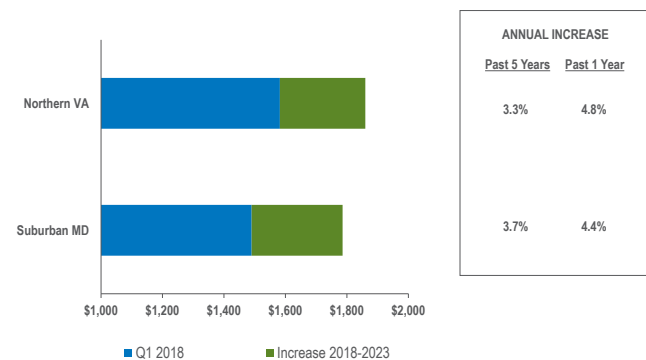
OUTLOOK FOR CLASS B APARTMENTS

Class B year-over-year rent growth (4.4%) continues to outpace Class A growth (3.2%). While vacancy in Class B product (2.3%) increased 40 basis points from a year ago, it is still lower than Class A vacancy (4.3%). Several contributing factors will continue to impact vacancy and rents going forward:

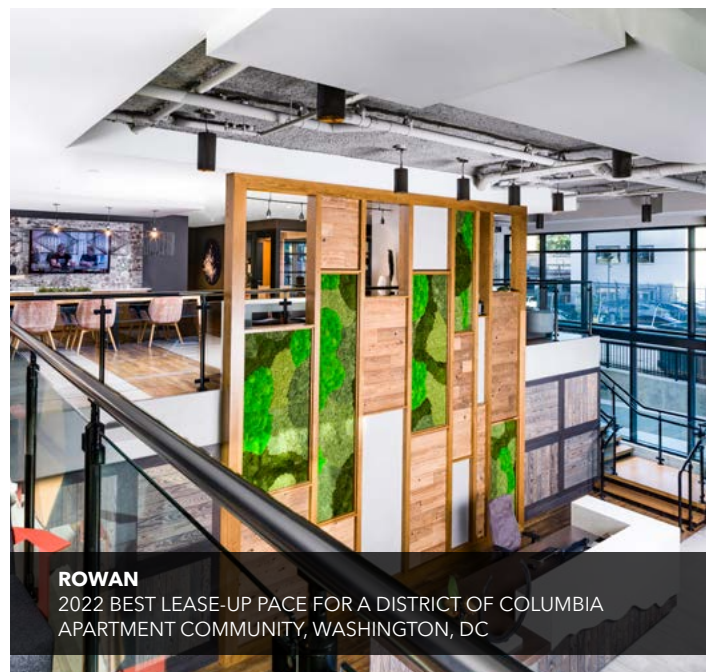
- 1. The Washington metro area job market has improved significantly since the beginning of the pandemic, providing opportunity for Class B apartment market demand.** Metro-wide job growth supported a sturdy Class B apartment market prior to the pandemic. In the Spring of 2020, many industries saw devastating job losses, but rebounded a year later as vaccinations were widely administered and confidence in the economy returned, including in sectors which support demand for Class B apartments. The greatest share of jobs in the region remains in the Professional/Business Services sector. Entry level positions in this sector do not pay enough to afford Class A apartment rents, making newly employed professionals search for Class B options with rents within their budgets. Many Professional/Business Services jobs can be done remotely, which has helped to shelter employment fluctuations in the sector during the pandemic.
- 2. Interest rate hikes aim to cool inflation.** The Federal Reserve lowered interest rates in the first quarter of 2020 to help stimulate the economy as the COVID-19 pandemic influenced employment and consumer confidence over the course of 2020 and 2021. As high inflation and lower consumer confidence threaten another economic recession, the Fed has been swiftly hiking interest rates. In 2022, seven rate hikes were implemented, including four large hikes of 0.75% over the summer and early fall and a 0.5% increase in December. This trend has continued in 2023 with a 0.25% rate hike implemented in February and a 0.25% increase in March. These rate hikes have pushed the average 30-year fixed mortgage rate above 6% for the first time in over a decade, which will dampen demand for homebuying and result in a larger pool of renters.
- 3. Prices keep homeownership out of reach for first-time homebuyers.** Metro-wide housing prices remain high, with the average sales price reaching record highs during the pandemic. Washington’s home ownership rate increased by 3.2% in 2020 to 67.9% and exceeded the national average of 66.6% as many residents opted to become homebuyers further from the core of the region in search of more spacious living. Since then, the regional homeownership rate has dipped back below the national average. Many residents in the region are renters by choice, so even those who may be able to afford to buy have a preference to rent instead.
- 4. Renovation activity shows a yearly improvement.** About 13,900 Class B units are under renovation in the metro area, up from 8,895 in March 2022. While this figure is more than last year’s total it is still slightly lower than the 14,500 units the Class B market averaged in the year leading up to the pandemic. Several projects were undergoing renovations before the pandemic temporarily halted plans until the full economic effects of COVID-19 came to light. We expect renovation activity to continue to rebound in 2023, approaching pre-pandemic levels. Nevertheless, properties that do move forward with these improvements are achieving premium rents, which we continually expect to see in those still undergoing renovations.

ANNUAL AVERAGE EFFECTIVE RENT GROWTH

Class B Low-Rise Apartments | Washington Metro Area
First Quarter 2023



Source: Delta Associates, March 2023.



ROWAN
2022 BEST LEASE-UP PACE FOR A DISTRICT OF COLUMBIA
APARTMENT COMMUNITY, WASHINGTON, DC

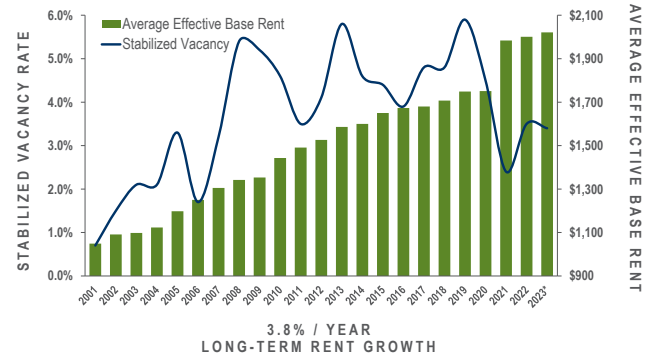
BALTIMORE METRO AREA CLASS A MARKET

LARGE DECREASE IN ABSORPTION AS FEW UNITS DELIVER

Absorption dropped across the Baltimore metro area significantly by 87%. A year ago, annual absorption was quite strong with 2,205 units compared to just 284 units over the past 12 months. Absorption was abnormally high in 2021 due to the effects of the pandemic, but the rapid drop in absorption over the past year was caused by a lack of new product and an increase in vacancy. There are only 984 units that came on the market over the year. Meanwhile, annual rent growth is low at 1.4% across the metro area.

EFFECTIVE RENT AND VACANCY RATE

Class A Apartments | Baltimore Metro

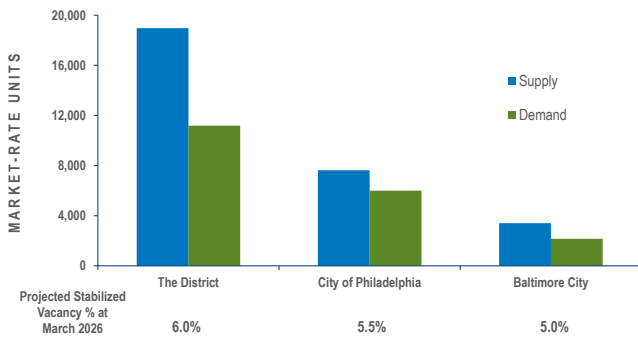


Source: Delta Associates, March 2023.

*As of March 2023.

SUPPLY/DEMAND RELATIONSHIP

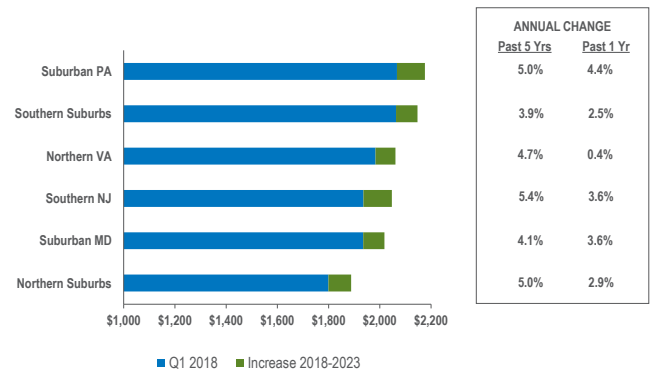
Mid-Atlantic Central City Class A Apartment Markets
Next 36 Months: Period Ending March 2026



Source: Delta Associates, March 2023.

ANNUAL AVERAGE EFFECTIVE RENT GROWTH

Mid-Atlantic Class A Low-Rise Apartments | March 2023



Source: Delta Associates, March 2023.

FIRST QUARTER 2023 HIGHLIGHTS

- > **Stabilized vacancy** in the Baltimore metro area increased 60 basis points from 2.8% a year ago to 3.4%. The vacancy rate in the suburbs is up by 50 basis points from 2.3% a year ago to 2.8%.
- > **Average effective rents** in the metro area are \$2,021 (\$2.13 per SF). Rents are up over the year by 1.4% metro-wide. Rent growth was strongest in the Southern Suburbs – up by 2.5%, followed by Baltimore City with a 0.8% increase. Rent growth in the Northern Suburbs was up 0.4% over the year ending March 2023.
- > **Absorption** over the year was just 284 units, which was 87% lower than a year ago. This significant drop in absorption is due to the lack of deliveries over the year in the market and a rise in vacancy.
- > **Deliveries** metro-wide stands at 984 units over the past 12 months. The number of deliveries in the 12-month period ending March 2023 compares to 275 units in the prior year.
- > **The supply pipeline** metro-wide experienced a 42% increase over the year. There are 6,188 unleased units under construction or planned for delivery in the next 36 months in the metro area after attrition. In Baltimore City, the 36-month development pipeline is up by 51%.
- > **Per project lease-up pace** for the five actively marketing projects in the Baltimore metro area currently averages 12 units per month, down six units from the same period last year.
- > **Apartment building sales** in 2022 included four transactions in low-rise buildings valued at \$238.2 million (\$322,260 per unit) and three transactions in mid-/high-rise buildings valued at \$223.2 million (\$266,250 per unit). As of March 2023, there are no recent transactions to report.

Of the 10 submarkets we track in the Baltimore metro area, three have less than four years of apartment supply based on absorption over the past 12 months (of these two have less than two years of apartment supply). In addition, five submarkets will add less than 10% of existing inventory over the next 36 months. Baltimore's supply/demand relationship indicates that vacancy rates will increase 70 basis points to 4.1% by the first quarter of 2026; however, we expect vacancy to fluctuate during this three-year period. Rents are expected to grow below the long-term average during this three-year period.



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2022 BEST OVERALL WASHINGTON/BALTIMORE APARTMENT COMMUNITY,
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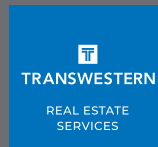
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