Multifamily Market Commentary – April 2016
Energy Metros and Low Oil Prices – A New Normal?

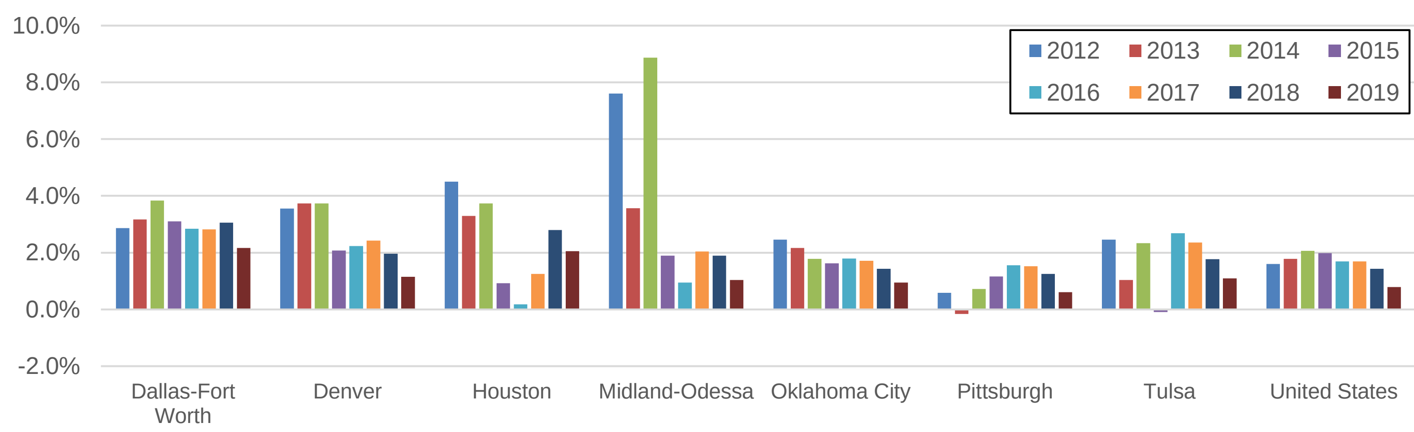
In mid-2014, a dramatic fall in oil prices brought a shock to global economic markets. Conditions stabilized with a modest price recovery through the first half of 2015, but by year's end we saw a repeat of 2014. The cause of the most recent decline was generally the same as the cause of the initial slump. An increase in North American oil production coupled with continued high levels of output from the traditional oil-producing nations was met by a slowdown in demand from China and a lackluster world economy, producing a global oil supply glut.

This time around, however, oil prices are not expected to rise dramatically anytime soon. The general consensus is that oil prices will recover modestly in 2016 – from a current price of about $40 per barrel – and perhaps rise to $50 per barrel over the next 12 to 24 months. Prices below $60 levels present more of a problem for North American producers than foreign producers, because the cost of extracting oil in North America is generally higher than in traditional oil-producing nations. While lower oil prices may make many commuters happy, they do raise concerns for some parts of the economy – including U.S. multifamily investors. Declining investment in oil exploration and a contraction in the number of oil-producing rigs have brought job losses, and they present a high likelihood of more losses to come.

What Happened to Energy Metro Job Markets in 2015?

Nationally, job market growth slowed slightly from 2.1 percent in 2014 to 2.0 percent in in 2015, according to Moody's Analytics. Houston, the metro with the largest energy-centric economy in the country, saw a more pronounced slowdown, though it did not experience net job losses. As the chart below shows, its total job growth declined to 0.9 percent in 2015 from 3.7 percent in 2014.

Moody's Annual Job Growth (Historical and Forecast) - Select Energy Metros



Source: Moody's Analytics

Among the larger energy metros, only Tulsa experienced a net job loss in 2015 – a slight 0.1 percent decrease. Smaller energy metros, however, felt a greater impact. As the table on the next page shows, Lafayette, LA, lost the highest number of jobs among metros with a concentration of mining jobs. But many metros with mining job concentrations – including Houston, Dallas, and Oklahoma City – actually managed to post positive job growth results despite the impact of falling oil prices late in the year. Of the many cities whose job markets did weaken in 2015, only a small number have larger-than-average apartment markets. Nationally, about 18 percent of housing units are in buildings with five or more units. The table on the next page shows that only eight of the 50 metros with mining job concentrations have an above-average concentration of multifamily housing units.

Change in Total Job Market Among Metros with Mining Job Concentrations - 2015

Metro Area	2014 Total Jobs (000s) Total	2014 Total Jobs (000s) Mining	Mining % of Total Jobs	2015 Total Metro Area Jobs (000s)	2014-15 % Change	2015 Net Job Change (000s)	2014 Housing Units (000s) Total	2014 Housing Units (000s) 5+ Units	Multifamily (5+) % of Total Units
Midland, TX	97.9	25.2	25.7%	99.6	1.7%	1.6	60.2	10.9	18.1%
Odessa, TX	81.2	13.1	16.1%	82.9	2.2%	1.8	56.5	11.1	19.6%
Farmington, NM	53.3	7.3	13.8%	52.4	-1.6%	(0.9)	49.6	1.6	3.2%
Casper, WY	42.9	4.7	10.9%	41.9	-2.4%	(1.0)	35.8	5.0	14.0%
Lafayette, LA	222.0	23.6	10.6%	217.0	-2.3%	(5.0)	201.9	20.0	9.9%
Victoria, TX	45.2	4.5	9.9%	46.3	2.4%	1.1	39.7	4.8	12.1%
Greeley, CO	101.1	9.4	9.3%	105.0	3.8%	3.8	100.1	11.4	11.4%
Wheeling, WV	68.6	6.0	8.7%	68.3	-0.4%	(0.3)	69.1	6.0	8.7%
Longview, TX	105.0	7.8	7.4%	105.7	0.6%	0.7	89.5	6.7	7.5%
Houma-Thibodaux, LA	101.5	7.0	6.9%	98.5	-2.9%	(3.0)	84.2	4.7	5.6%
Beckley, WV	47.4	2.8	6.0%	47.4	0.1%	0.0	57.5	3.2	5.5%
Grand Junction, CO	61.7	3.4	5.5%	61.6	-0.2%	(0.1)	63.8	5.3	8.3%
Corpus Christi, TX	196.8	9.0	4.5%	199.9	1.6%	3.1	187.5	24.8	13.2%
Williamsport, PA	56.5	2.4	4.3%	54.8	-3.1%	(1.7)	52.6	4.7	8.9%
Bakersfield, CA	260.9	10.5	4.0%	262.4	0.6%	1.5	291.5	27.4	9.4%
Fairbanks, AK	38.5	1.5	3.9%	38.6	0.1%	0.0	41.7	5.8	13.8%
Houston, TX	2,968.5	113.3	3.8%	2,996.0	0.9%	27.4	2,441.2	645.2	26.4%
Charleston, WV	123.6	4.6	3.7%	122.8	-0.6%	(0.7)	107.5	10.3	9.6%
Wichita Falls, TX	58.3	2.1	3.6%	57.2	-2.0%	(1.2)	65.3	6.8	10.4%
Oklahoma City, OK	623.0	22.7	3.6%	633.2	1.6%	10.1	557.4	83.0	14.9%
San Angelo, TX	49.1	1.8	3.6%	49.1	0.1%	0.1	48.6	7.5	15.4%
Abilene, TX	68.6	2.2	3.2%	69.0	0.6%	0.4	70.5	8.5	12.1%
Laredo, TX	99.3	3.2	3.2%	101.3	2.1%	2.1	78.1	10.4	13.4%
Tuscaloosa, AL	103.7	3.2	3.1%	106.1	2.4%	2.5	104.4	20.7	19.8%
Shreveport-Bossier City, LA	183.8	5.3	2.9%	181.5	-1.2%	(2.2)	198.6	23.7	11.9%
Tyler, TX	99.2	2.8	2.8%	99.8	0.6%	0.6	88.4	10.6	12.0%
Duluth, MN-WI	134.5	3.6	2.7%	135.5	0.8%	1.0	141.9	15.8	11.1%
College Station-Bryan, TX	105.7	2.7	2.6%	106.7	0.9%	0.9	100.1	20.0	19.9%
Fort Smith, AR-OK	113.2	2.6	2.3%	112.0	-1.1%	(1.2)	123.0	10.0	8.2%
Prescott, AZ	60.5	1.4	2.3%	61.7	1.9%	1.2	112.5	6.0	5.3%
Anchorage, AK	180.2	3.8	2.1%	181.5	0.7%	1.3	155.6	22.4	14.4%
Tulsa, OK	443.5	8.8	2.0%	443.1	-0.1%	(0.4)	421.1	60.8	14.4%
Carbondale, IL	54.8	1.1	2.0%	53.9	-1.6%	(0.9)	59.4	7.9	13.3%
Amarillo, TX	116.6	2.1	1.8%	117.5	0.7%	0.8	107.5	14.2	13.2%
Pine Bluff, AR	34.1	0.6	1.7%	31.7	-7.0%	(2.4)	42.6	4.3	10.0%
Terre Haute, IN	70.5	1.1	1.5%	70.0	-0.7%	(0.5)	73.9	7.5	10.2%
New Orleans, LA	564.5	8.3	1.5%	563.7	-0.1%	(0.8)	553.4	82.9	15.0%
Morgantown, WV	69.8	0.9	1.3%	69.3	-0.7%	(0.5)	59.5	9.9	16.6%
McAllen-Edinburg-Mission, TX	245.0	3.1	1.3%	251.4	2.6%	6.5	261.2	21.3	8.1%
Parkersburg-Vienna, WV-OH	42.8	0.5	1.3%	42.7	-0.3%	(0.1)	43.3	2.7	6.3%
Beaumont-Port Arthur, TX	168.4	2.1	1.2%	173.1	2.8%	4.7	174.7	24.3	13.9%
Lake Havasu City-Kingman, AZ	46.6	0.5	1.2%	46.0	-1.4%	(0.6)	112.3	6.7	5.9%
San Antonio, TX	959.0	10.8	1.1%	994.7	3.7%	35.8	862.0	165.3	19.2%
Dallas-Fort Worth-Arlington, TX	3,326.0	37.4	1.1%	3,429.2	3.1%	103.2	2,645.5	662.2	25.0%
Denver-Aurora-Broomfield, CO	1,362.7	15.3	1.1%	1,390.9	2.1%	28.2	1,114.1	295.7	26.5%
Pittsburgh, PA	1,164.5	11.8	1.0%	1,178.0	1.2%	13.5	1,106.0	138.0	12.5%
Elmira, NY	39.2	0.4	1.0%	39.1	-0.2%	(0.1)	38.4	3.7	9.5%
Hanford-Corcoran, CA	37.6	0.3	0.8%	37.8	0.7%	0.3	44.9	4.6	10.2%
Huntington-Ashland, WV-KY-OH	141.0	1.2	0.8%	141.1	0.1%	0.1	165.6	13.0	7.8%
Johnstown, PA	57.5	0.4	0.6%	56.8	-1.3%	(0.7)	65.3	5.4	8.2%

Source: Moody's Analytics, Bureau of Labor Statistics, per Fannie Mae's Economic & Strategic Research Group – metro areas include coal mining concentrated MSAs

National Outlook – Pain in Energy Metros, Steady National Economy

Moody's expects national job market growth to slow moderately in 2016 – to 1.7 percent, down from 2.0 percent for 2015. Even so, as they did last year, low oil prices should provide a net benefit to the national economy. They provide consumers with more disposable income every time they go to the gas pump. And in the business sector, low oil prices reduce operating costs and create a more profitable industrial production process.

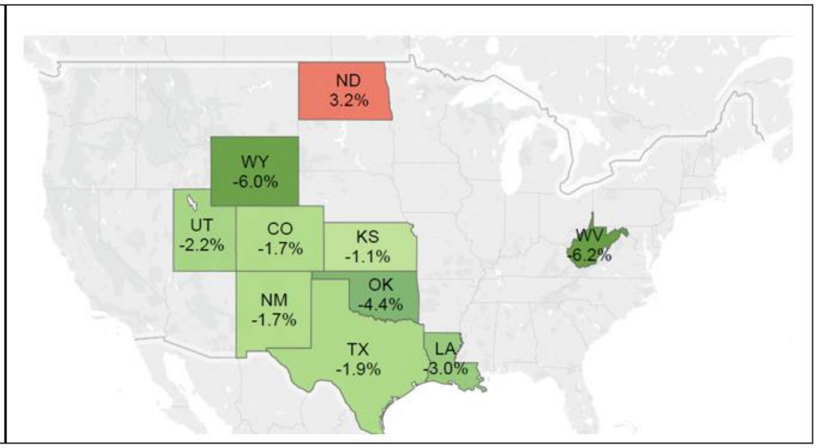
Moody's expects oil prices to rise modestly during 2016. However, it says that if prices stayed at the $35-a-barrel level, the national economy would actually produce 280,000 more jobs this year than if prices rose modestly. Using the general ratio of five new jobs producing demand for one additional apartment rental unit, lingering $35 per barrel oil prices could possibly increase the demand for new apartments nationally by as many as 56,000.

Despite Diversification, Impact on Energy-Dependent Regions Still Negative

Nevertheless, persistently low oil prices would certainly have a negative impact on several energy-dependent economies around the country. But it is important to recognize that today's energy markets are not the same places they were during the oil bust of the 1980s. Since then, the national economy has diversified in many important ways, and so have these metros.

Change in Mining Share of State Payrolls 1982 vs. 2014

	Mining Share of Payrolls	
	1982	2014
WY	15.2%	9.2%
ND	3.6%	6.8%
AK	5.8%	5.3%
WV	10.2%	4.0%
OK	8.2%	3.8%
NM	5.1%	3.4%
TX	4.6%	2.7%
LA	5.6%	2.6%
CO	3.1%	1.4%
UT	3.1%	0.9%
KS	1.9%	0.8%



Source: Bureau of Labor Statistics, per Fannie Mae's Economic & Strategic Research Group

As the table above shows, all of the states except North Dakota have seen a significant decrease in the portion of their jobs that are in the mining sector – which includes oil exploration and extraction, and the mining of coal and other natural resource, but not office support services and equipment manufacturing.

Taking a closer look at Houston – the nation's energy capital – shows that it too has seen a significant decrease over the past three decades in the importance of oil to its overall economy. For example, in 1982, mining and manufacturing jobs (including non-oil and energy-related jobs in those sectors) accounted for a combined 20 percent of Houston's job market. At the end of 2013, that portion was just 12.5 percent. More importantly, Houston can expect continued diversification over the next decade. And Houston is not alone. Dallas has seen an even more pronounced change in its local economy. In 1982, mining and manufacturing jobs accounted for 21 percent of the jobs in the Dallas metro. By 2013, they had declined by more than half, accounting for just 9.1 percent.

Overall, Texas has managed to slog through the fall in oil prices better than would have been expected. In 2015, total job growth in the state was 1.5 percent, only slightly below the 2.0 percent national rate. Texas still has very solid demographics supporting its housing markets. Its population grew 1.8 percent in 2015 – well above the 1.0 percent national average. According to Moody's, home prices are rising in all of the state's major metro areas.

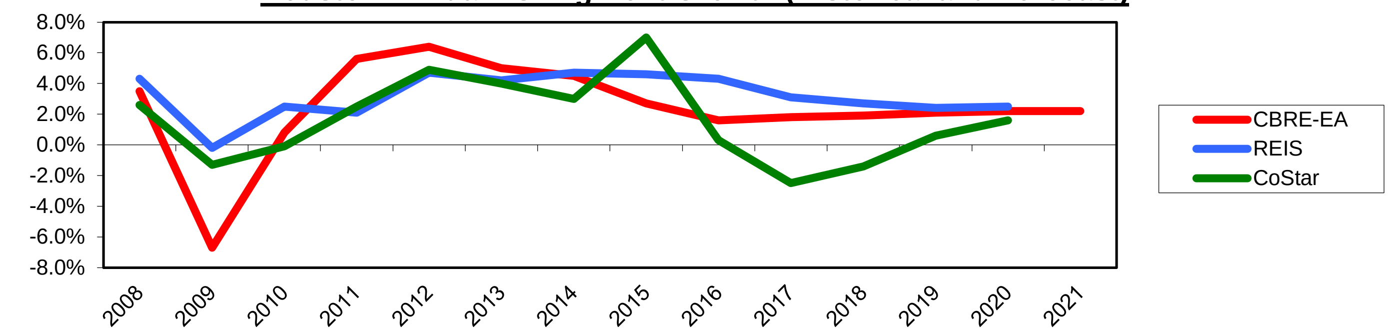
In Louisiana, by contrast, low oil and natural gas prices have weakened economic conditions. In 2015, while regional construction kept Baton Rouge steady, job markets were weak in Shreveport and Lafayette, though not as weak as in 2014.

Lafayette's economy swung from a 2.5 percent contraction in 2014 to a net gain of 1.0 percent in 2015. Shreveport saw more significant trouble in 2013 when natural gas prices declined precipitously and its economy contracted by 5.8 percent. The area managed to find its way back to positive territory in 2015 when it experienced 2.0 percent economic growth. The economies of both metros – as well as the state's – is expected to continue to lag in 2016.

Houston – Softening, Not Collapsing

Houston is among the metros that will likely be seeing new multifamily housing supply increase significantly in 2016, just as its economy slows noticeably from recent trends. Planning for these new developments occurred when Houston was growing at twice the national average, and before declining oil prices took their toll. As a result, Houston should expect to see softening of its apartment market. This year, it is expected that Houston will have no appreciable rent growth and its vacancy rate could potentially increase by 200 basis points.

Houston Annual Asking Rent Growth (Historical and Forecast)



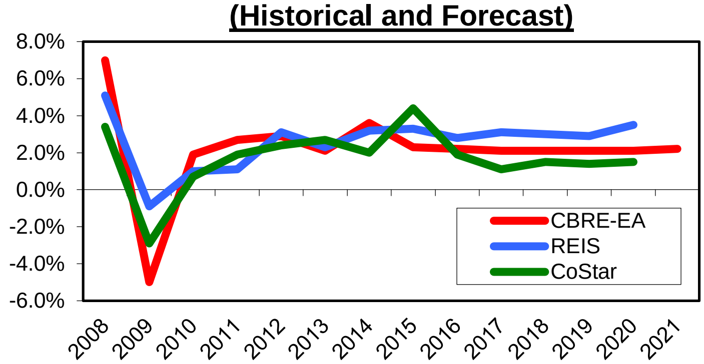
Source: CoStar, CBRE Econometric Advisors, and REIS

Houston was already poised for a slowdown this year – even before falling oil prices muted prospects for the metro's job market. Now, a surge in new rental supply will be coming online at a time when there is weaker-than-expected market demand. Once these conditions subside, Houston's multifamily market is expected to start growing again – but that should occur further out in the forecast, as noted the chart above.

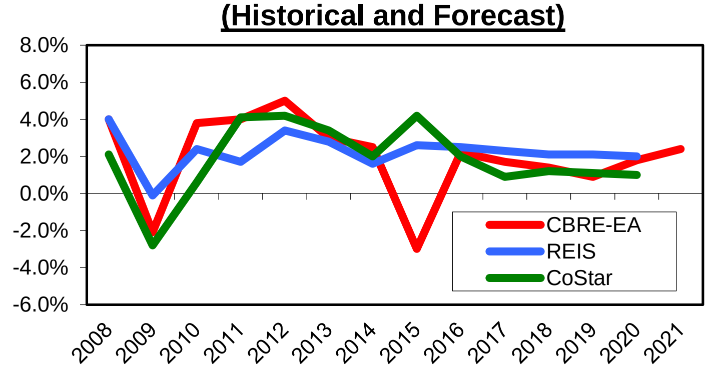
Oklahoma – Slowing but Not Breaking

Oklahoma's two largest metropolitan areas – Tulsa and Oklahoma City – both benefitted from the oil boom, but Tulsa felt more pain from 2015's drop in oil prices than Oklahoma City. Job growth plummeted to essentially zero last year in Tulsa from a quite healthy 2.3 percent increase in 2014. In Oklahoma City, by comparison, the slowdown was modest, with job growth falling slightly to 1.6 percent from 1.8 percent in 2014. The apartment markets in both metros are expected to remain fairly stable – with a slight increase in vacancies and positive, though slightly slower rent growth, as noted in the charts below. While the two metros face more modest growth in oil and mining jobs going forward, both are expected to see their education, health and professional and business services jobs grow at above national average rates over the next five years, supporting apartment demand.

Tulsa Annual Asking Rent Growth (Historical and Forecast)



Oklahoma City Annual Asking Rent Growth (Historical and Forecast)



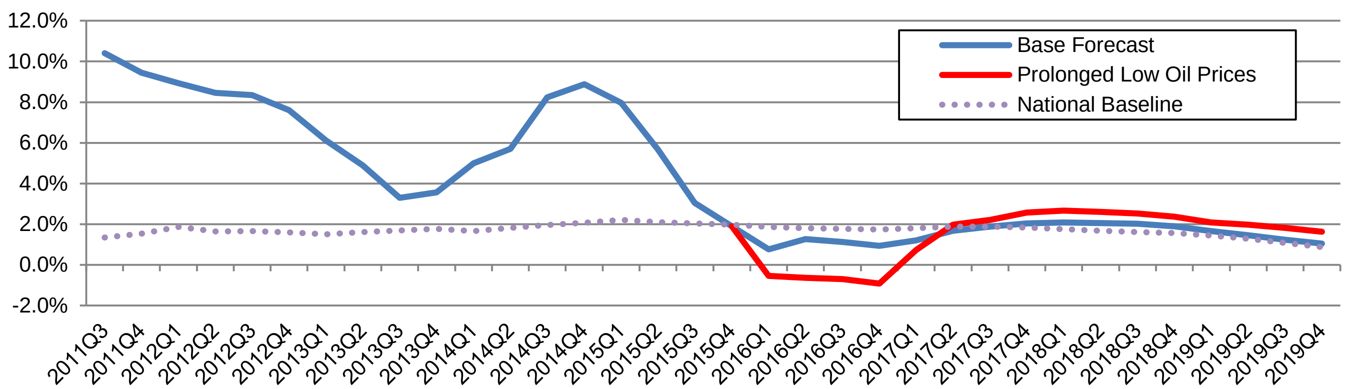
Source: CoStar, CBRE Econometric Advisors, and REIS

Midland-Odessa – The Worst May Be Over

Midland-Odessa – probably the largest beneficiary of the Texas oil drilling boom – experienced exceptional job growth in 2012 through 2014. New jobs grew at astounding double-digit rates during the period, before the market came back down to earth in 2015. While the metro did not sustain a net loss in jobs, job growth was down significantly – falling from an eye-popping 8.9 percent in 2014 to a still very respectable 1.9 percent in 2015. According to Reis, Inc., this has resulted in a stunning rise in vacancies. From a low of less than 3.0 percent in 2012, the vacancy rate soared to just over 10 percent by the end of 2015. Rents have been volatile, but have not declined dramatically. Reis estimates that rents grew more than 20 percent in both 2011 and 2012. In 2015, they contracted by approximately 5.0 percent.

The good news for Midland-Odessa is that the worst is probably over. A dramatic decline in oil prices brought similarly dramatic change in the local economy, but further deterioration should only be minor. Moody's forecasts that the area could have 0.9 percent job growth in 2016, and 2.0 percent the following year. While these levels may be disappointing, the area's exceptional growth of 2012 through 2014 was unsustainable over the long term. However, even if low oil prices persist for more than three years, Moody's expects the area's job growth rates to exceed the national average, although at a much slower pace than in the earlier period, as noted in the chart below.

Midland-Odessa Job Growth (Historical and Forecast) (YoY)



Source: Moody's Analytics

North Dakota Adjusting to Its New Normal

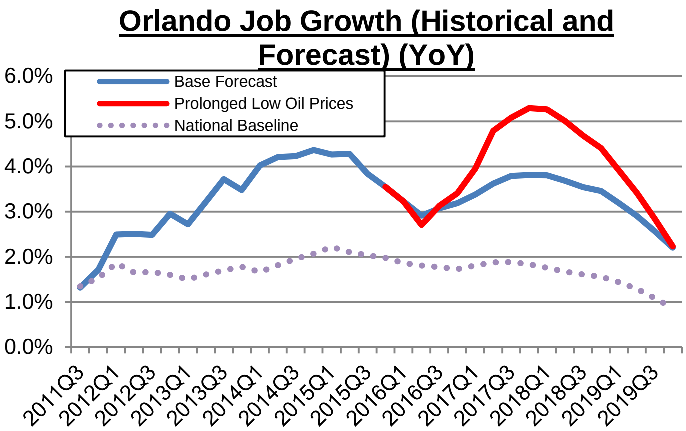
North Dakota continues to adjust to the new reality of oil prices below $40 a barrel. In 2016, more than anywhere else in the country, the state is expected to feel the pain of exploration and drilling job losses. As of early March 2016, there were just 32 exploration and production rigs operating in the state – compared to more than 200 as recently as 2012. As of this March, rigs in operation were down 70 percent from a year earlier. The number of jobs in North Dakota contracted by 1.6 percent in 2015.

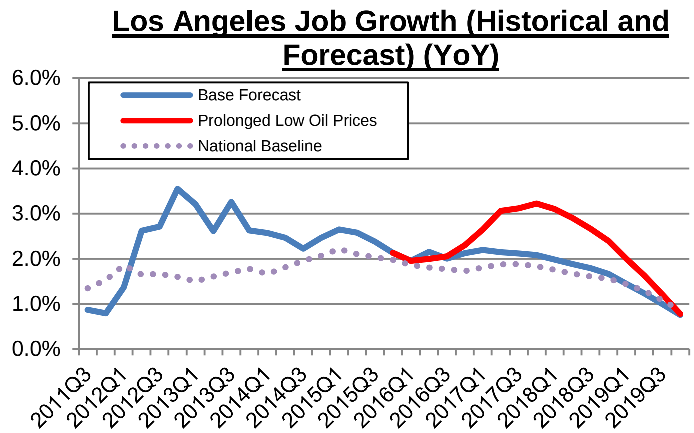
The largest cities in North Dakota – Bismarck, Fargo, and Grand Forks – all reported positive job growth for 2015. That puts the primary oil metro in the state – Williston – on the receiving end of the largest negative fallout. Axiometrics, Inc. estimates that asking rents in Williston fell by more than 34 percent in 2015, as the occupancy rate plummeted 10 percentage points to 84 percent. Without a significant recovery in oil prices, it is likely that Williston – along with most of North Dakota – will continue to languish for the next several years.

Oil exploration activity is not significant in Fargo, which is the most populous area of the state. But the metro has definitely experienced the impact of falling oil prices. Fargo's apartment market has felt the pain acutely, though it possibly has seen the worst. Reis reports a rapid rise in the metro's apartment vacancy rates – to 9.0 percent at the end of 2015 from a low of 4.6 percent just two years earlier. Expectations are for only an additional one percentage point increase in the vacancy rate over the next two years.

Many Metros Benefit from Low Energy Prices

As most people can appreciate, lower gas prices are a positive. And they're not only positive for individuals, but also for many local economies. Low oil prices will likely provide an economic stimulus to metro areas that rely not on the energy sector, but on such industries as logistics, manufacturing, transportation, and tourism. For example, Orlando and Los Angeles would expect to see significantly stronger job growth through 2019 if oil prices stayed below $40 a barrel for the next three years. That could give their economies an additional 35,000 and 129,000 jobs, respectively – loosely translating into possible demand for as many as 7,000 additional apartments in Orlando and as many as 25,800 additional apartments in Los Angeles. Most metros across the country whose economies will be stronger as the result of lower energy prices can expect to see increases in job growth and apartment demand.





Source: Moody's Analytics

Softening Conditions Nationally in 2016, Slightly Worse in Energy Metros

Nationally, the multifamily sector can expect to see some softening of fundamentals in 2016. Rent growth has been exceptionally strong since 2011. It has remained in the 3.0 percent range over the past two years, starting to slow down slightly in 2014. The expectation for 2016 is that rent growth will once again be positive, but that it will ease slightly into the 2.5 to 3.0 percent range. A large amount of new supply should come online in 2016. Importantly, much of the supply will be concentrated in submarkets in about 12 metros. Healthy job growth should spur continued rental household formations, but there is no denying that the added apartment supply will likely produce an increase in vacancy levels, particularly in those submarkets across the country where it is concentrated.

Continued low oil prices are likely to be painful in a few places, but a welcome stimulus in many others. It's true that we did not see a dramatic increase in consumer spending nationwide in 2015 as a result of lower oil prices. But we also didn't see any cataclysmic eruptions in the economies of energy-focused metros. This state of relative equanimity is expected to continue in 2016 for the national economy, local economies, and apartment markets. A rising vacancy rate and softening rate of rent growth is expected for the national apartment market, after consecutive years of extremely tight vacancies and an extended period of unabated rent growth. Energy-focused markets will obviously experience softening as well. Although most have seen the majority of the job losses to be expected during this phase of the oil cycle, weaker-than-expected job creation and housing demand should somewhat exacerbate results in their apartment markets.

The question is, how long will the oil glut last and how will it affect the economy? If oil prices would remain at around $40 per barrel for the next three years, there would likely be a disproportionate impact on Houston, one of the nation's largest metros. And many of the smaller energy metros would likely endure a prolonged contracted economy. The rest of the nation would probably benefit, making many consumers, and especially commuters, quite happy.

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