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Apartment investments still remain center stage among real estate markets

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Review of several real estate benchmarks indicate that the apartment sector remains one of the best performing sectors in the industry. The recovering economy and increasing employment benefits the apartment sector by creating immediate demand for occupancy, which is being driven, to a large extent, by two key sectors of the population: ex-homeowners and echo boomers.

Due to the recent downturn in the economy, many ex-homeowners have been forced into a rental situation as their home mortgages became impossible to pay. Apartment owners report high interest for two and three bedroom apartments, as couples relocate families from single-family residences. Additionally, a large number of homeowners turned over the keys to their residences, as property values dipped far below their mortgage loan balances. While home mortgage interest rates hover around 3.0 percent, many ex-homeowners simply do not have the ability to secure a new mortgage, and apartment investors are benefiting from this situation. As the economy continues to strengthen, ex-homeowners will potentially begin to transition back to home ownership.

The "Echo Boom" generation has a profound influence on the Apartment Sector as a whole. Broadly defined as persons born between the latter 1970s and the early 2000s, this group is one of the single largest generations that exists today. Interestingly, relative to prior generations, the group demographics indicate a lower marriage rate, minimal savings as a result of high education costs and a lackluster economy, a desire to live close to work and a stronger bias toward renting vs. home ownership. The higher educated within the generation value urban locations with a high quality of life, and typically seek cities such as New York, Hoboken and Jersey City. In the Metro New York area, the rental market for three bedroom apartments is in demand by Eco Boomer families who have decided to remain in the city after marriage and children. Historically, New Yorkers would have moved into suburbia and the next generation would have transitioned into the city. As a result of this new trend to stay put in New York City even with a growing family, developers are incorporating daycare facilities into new construction.

Due to peak demand, apartment vacancy rates are expected to remain near five percent nationwide, with lower rates of between 3 - 4% in key markets like New York. Aware of this demand, Urban Core development in key gateway cities such as New York and New Jersey's Gold Coast are receiving the majority of interest for apartment development. Investors and developers favor these areas, as higher income levels support the upscale product typically constructed in these infill locations. Recently, a developer in Hoboken, who is completing a 40-unit boutique apartment project, received over 500 inquiries, as evidence of continued demand. We expect the speculative development to eventually reach a crossover point with demand. Investors active in speculative residential construction are still optimistic but aware of potential overbuilding. They are closely monitoring portfolio rental rates and occupancy statistics to identify any saturation of the market.

In select urban markets, rent growth has exceeded ten percent per annum. This rental increase is not sustainable over the long term as much of the recent rent growth was a result of increasing rents back to pre-2008 levels. An annual growth rate of four to five percent is projected over the next several years.

While the apartment sector is still one of the preferred targets for institutional and private investment, speculative construction and non-sustainable rental increases will temper appreciation. Still, relative to several alternative real estate investments, the apartment sector remains a safe choice for investors.

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