

Written by NMHC

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Best Practices in Research

Since 2002, NMHC's annual Research Forum has been the place for those who specialize in real estate research to discuss best practices and industry trends as well as to network with colleagues.

This year's Research Forum was in Dallas, and the mood was upbeat. In fact, Equity Residential's Jay Lybik, Chair of NMHC's Research Committee, cautioned against getting too "fat, happy and stupid" simply because the apartment industry is prospering now. "I know everything looks great, but let's focus on what our research proves has worked well, not get crazy because everything looks great right now. We should be happy, but don't get too happy."

This special NMHC Update newsletter reviews the key themes and takeaways from this recent forum.

In addition to this newsletter, presentations from the Research Forum are available. If you missed this forum, visit www.nmhc.org/goto/meetings for information on upcoming NMHC meetings that you'll enjoy.

Property Managers' Panel---Turnover, Revenue Management and Upgrades

MPF Research's Greg Willett moderated a high-level property managers' panel, including Sue Ansel from Gables Residential, Berkshire Property Advisors' Alan King and Steve Lamberti from Milestone Management.

Sue Ansel reported that Gables' turnover in 1Q 2011 was less than in 1Q 2010: "All of 2010 turnover is down from 2009's. Traffic varied by market but was up slightly."

Berkshire Property Advisors' Alan King agreed: "We anticipated higher turnover but it didn't occur. Traffic is up 10 percent to 20 percent across markets. We were somewhat sensitive to being over-aggressive in the first quarter but renewal and market rate increases have been achieved."

"Rents are up, traffic is up, turnover is down" for Milestone, Steve Lamberti reported, but, he added, "at some point we'll start to get resistance on renewals and on new leases."

Residents departing to a single-family house is not a significant threat at the moment: "We're not seeing a huge movement to home buying," said Lamberti. Ansel added that moving out to purchase a house has always been the main reason residents gave when leaving a Gables property: "But that data was the lowest level ever seen in 1Q 2011. 2009 and 2010 were low, and 2011 is following that trend."

"We went into 2011 expecting to give up a bit on occupancy to focus on the rent number," said moderator Greg Willett. "Is that still the expectation?" Lamberti responded, "The rents we're

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getting today are trying to get us back to 2007 and 2008 ranges---it's not raising rents, it's recovering them."

Gables is "giving our associates the confidence that they could push rates. We created incentive plans to raise revenue. If they move the needle for rental rates beyond what was expected, they are rewarded," according to Ansel.

Alan King reported that Berkshire's revenue management model is being very aggressive, using renewal protection and pushing the parameters: "The mindset has changed and we're seeing success." He says a bonus program at Berkshire measures property managers' performance to rent increases.

Regarding renovations Ansel said, "Now is the right time to be doing renovations. Kitchens and baths are the key. Even if all the resident does is put their sweaters in the oven, they want to have a beautiful kitchen," according to Gables' Ansel.

Lamberti agreed that kitchen and bath upgrades are key, asking "but what is the second-generation upgrade? Raised panel doors? New ceilings? Do you get paid for those? It will be very interesting to follow over the next 12-24 months."

The View from the Executive Office

Jay Lybik (Equity Residential) asked executives how their firms use research. Scott Wilkerson, Ginkgo Residential, said Ginkgo does not have a large in-house research department, so "I come to NMHC meetings and pay attention, I do Internet research and I use the Census Bureau's American Fact Finder. That will soon be able to go to the block level. We have also bought research from large firms."

Wilkerson added that he also likes to watch what retailers do and what firms with big research budgets are doing. "I also do things the oldfashioned way: I drive around and look around. I'll go on a Friday night, count the cars in the parking lot. It's an indicator; it's data."

He added that he also watches what his competitors do. "We found firms doing mandatory renters' insurance a few years ago, so we tested it on some properties, then rolled it out portfolio-wide. We tested out non-smoking apartments; rolled it out to 36 properties and will roll it out to more. These are some of the things where using research helps us."

Lybik volunteered that Equity likes to use Google Street View to aid in its research. "We can 'walk' around the property in our office. We save thousands in travel costs." Wilkerson agreed: "The resolution is incredible; these are phenomenal tools we didn't have when I started in this business in the mid-80s."

Pinnacle's Rick Graf added that it's important to have a realistic view of what a particular submarket you are considering is going to do: "If one employer dominates in that area, be sure to see if that employer is going up or down."

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Lybik reflected on the importance of data rather than anecdotes: "I don't care what the rents are; I want to know what we are collecting every month. If you're not looking at your own properties yet, then you really need to look at it. You can utilize that information and get away from simply asking the property manager for their profile; that's meaningless. You have the information there; you've got to use it. The power of information really is amazing."

Homeownership: "Rocky Bottom"

Eric Belsky, Managing Director of Harvard's Joint Center for Housing Studies, (which just released a new report, America's Rental Housing: Meeting Challenges, Building on Opportunities), analyzed the worst homebuilding downturn since World War II. Belsky reported that the National Association of Realtors' median existing house price to per-capita income ratio is at record lows (dating back to 1975) and the Case-Shiller Index finds the house price to per-capita income ratio is at 25-or-more-year lows in IL, FL, CA, NV and AZ.

"This is one of the slowest job recoveries we've had," Belsky said, and low consumer confidence is constraining demand. Private payroll employment is needed for sales recovery to happen; employment growth has been key to the strength of past demand rebounds.

Right now, conditions don't look poised for a big bounceback in the single-family market, Belsky concluded, but if employment improves it could turn around faster.

It's no coincidence that the unemployment rate correlates to negative equity: people find it hard to move to find a job. Fleming added that negative equity could last for seven to 10 years in some markets.

This can lead to "strategic default"---where people who are able to make their mortgage payment voluntarily decide to stop paying. The three best indicators of strategic default are:

1. The borrower is deeply---not just slightly---underwater on their loan
2. The borrower is an investor; the house is not their primary residence
3. The borrower knows other people who have strategically defaulted: "This is unlikely if they live in New York City, but if they live in Nevada, they likely know someone else who had strategically defaulted."

2010 Census: "The mark of a truly educated man is to be moved deeply by statistics"

Demographer Steve Murdock, former Director of the U.S. Census Bureau, said that the U.S. is experiencing the second-slowest growth rate in our history; only the 1930s were slower. Despite this, he expects the U.S. population to grow to 439 million by 2050. And he added that two of every three people added to our population will come through births, not through immigration. Of our immigration, he added, most of it is legal, documented immigration.

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Census data show a long-term pattern, Murdock added: "The Northeast is no longer where everybody lives." Eighty-five percent of our growth between 1910 and 2010 occurred in the South and the West and "no data suggests that that will change much."

Murdock added that "central cities have continued to struggle relative to suburbs; the ten largest American cities did not have booming growth between the 2000 and 2010 Censuses." NMHC's Mark Obrinsky suggested that "the term 'suburbs' doesn't mean what it once meant. In the 1950s it meant a 'bedroom community' for a city. Today, some suburbs are bedroom communities, but others are actual cities that grew near a city but have a totally different character. Our vocabulary hasn't grown sufficiently." He added, "Maybe we need to talk to more geographers to figure out how to work on that."

Murdock also looked at changes in the demographics of renters. Demographers use a country's birth-to-death ratio, he said: "If you discount immigration, if a country has more births than deaths the ratio increases. In the first half of 2000- 2010, the birth-to-death ratio for the overall U.S. population was 1.3 to 1, but for Hispanics that ratio was 8 births to 1 death. Thus, he said, "unless people who rent drastically change characteristics, people who have those characteristics will be Hispanic."

Issue in Apartment Investment: Prices and Property Types

Mike Sobolik of Invesco Real Estate moderated an apartment investment discussion. First, AXIOMetrics President Ronald Johnsey examined whether Class A properties have outperformed Class B and Class C properties. Examining data from 3Q 2003 to 4Q 2010, he found that the Class A did indeed outperform the other classes in some markets, including Atlanta, Boston, Chicago and Houston. In other markets, though, such as Austin, West Palm Beach, Fort Lauderdale and Miami, Classes B and C rather consistently performed better than Class A properties.

Melissa Reagen of LaSalle Investment Management analyzed 33 apartment markets across the U.S. to find that some markets never delivered the NOI growth needed to justify the prices paid. She found a weak relationship between apartment NOI growth and cap rate spreads; while some markets, such as Los Angeles, New York, Washington, DC and Chicago look reasonably priced, others, including San Francisco, Houston and Charlotte, are not.

Jeannette Rice of Verde Realty added: "We should add Psychology to the list of variables. We who work in Research hear and look at research that should drive investment decisions, but investment decisions are driven by many other things that might not make sense to researchers in this room. Since investment decisions are driven by factors other than cash flow, we'd like to see more research on this."

Federal Multifamily Data Workshop: "Characteristics, not Counts!"

At a special workshop, Jay Lybik (Equity Residential) explained that the annual American

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Community Survey (ACS) is in some ways a better tool for apartment researchers than the decennial Census, which is updated once every ten years.

"The ACS uses Permanent Census interviewers, always in the field gathering data," said Lybik. "This helps ACS data to be a good quality source, with lower error percentages in this data." The downside: there is a smaller sample size compared to the decennial Census, so there is greater sampling error. The ACS does provide income data and asks for marital status, language spoken, number of rooms in residence, bedrooms, etc.

"The key point I want people to take away is the ACS is not about counts; it's about characteristics. There will be population data embedded in it, but the ACS is not developed for counts. That's what the Current Population Survey is for," Lybik said.

Mark Obrinsky (NMHC) agreed, adding that, "One problem I see is that lots of people like to use the ACS, the American Housing Survey and other Census survey data to get a time series. The Census Bureau would prefer that they didn't do that, but people do use it that way." Lybik concluded, "My biggest fear from a research standpoint is that Wall Street researchers will take ACS data, see that it includes population numbers and start doing time series. It's not supposed to be used like that."

The Census Bureau Needs You

Richard Levy of the Census Bureau discussed the Rental Housing Finance Survey, an important new Census initiative that will benefit the apartment industry.

The Rental Housing Finance Survey will collect data on multifamily characteristics, operating expenses and debt financing. Responses will be kept confidential.

The multifamily survey will be conducted January-April 2012; data will be available to the industry in late 2012 or early 2013.