Workforce Housing Forecasted to Outperform Multifamily

There is a strong demand for workforce housing apartments with the shortage expected to continue in 2019.

By **Tanya Sterling** | January 03, 2019

(https://images.globest.com/contrib/content/uploads/sites/304/2019/01/
Jeanette Rice

Los Angeles, CA– Workforce housing has consistently outperformed the multifamily market for the last four years with low vacancy rates and above-average rent growth, says the latest research from CBRE, "The Case for Workforce Housing." Slow wage growth over the past decade has contributed to a high number of potential renters and an extreme lack of new supply. Plus the limited alternative lending options translates into a strong demand for workforce housing apartments with the shortage expected to continue in 2019.

Defining Workforce Housing

"We define workforce housing as the housing where individuals and families making between 60% and 100% of area median income (AMI) live. In some markets, especially high-cost markets like California, the definition could be extended to 120%. In our research, we focus on market-rate multifamily product. The way that we define workforce housing is in line with most industry participants," says Jeanette Rice, Head of Multifamily Research, Americas, CBRE. "However, in the broadest definition of workforce housing, it would include some government-sponsored housing targeted at families earning between 60% and 100% of AMI as well as both single-family rentals and owned single-family. For families in this income range of 60% to 100%, there are many housing options, but the most common is market-rate multifamily housing."

Rice continues, "when we think of affordable housing at CBRE, we're usually focusing on subsidized housing targeted at families making less than 60% of AMI. That definition is fairly standard in the industry, but it's true that the term "affordable housing" is often used to connote housing for a wider-range of incomes. (Colloquially, we often refer to the first definition of affordable housing as "Affordable" with a capital A and the second definition as "affordable" with a lower-case A.)

Attracting $375B In Investment

The robust market performance of workforce housing has attracted major investments of approximately $375 billion over the past five years, a total of 51.3% of all multifamily assets. This capital is increasingly coming from unlikely sources, including institutional and cross-border investors, says CBRE's report.

Investor interest in workforce housing began to grow a couple of years ago when market performance in Class A began to show some softness from the large quantity of new supply, but not from any let-up in demand, Rice says. Class B & C product market metrics were improving — rent growth rising, vacancy falling more than previous years — and also outperforming Class A. That shift came about three years ago, she says.

As we enter a new year, the high supply/low demand balance in workforce housing is still working in its favor.

“Class B and C space will outperform Class A through the year,” Rice says. There’s no let-up this year on construction deliveries — which will continue to impact Class A sector, but not Class B and C. Meanwhile, wage growth is improving, but not enough to allow most workforce housing residents to move out into Class A product or to homeownership or rentals, explains Rice.

“Yet, also job growth and wage growth are sufficient to keep consumer confidence relatively high and household formation high. So demand will remain strong.

Growing Risks

But while the industry will continue to try to figure out how to deliver new workforce housing product, the obstacles on that front, such as high construction costs, high land costs, regulatory environment, are daunting, Rice says.

There are other risks as well. Workforce housing affordability has begun to create some resistance to rent increases and may limit them even further in the future. More than 35% of workforce renter households were considered “rent burdened” last year meaning that their rents represented 30% or more of their incomes versus 21% in 2006. Proposed rent control policies could also limit rent growth, while the wide array of public and private programs focused on trying to improve housing affordability may improve the supply/demand situation for renters at the expense of owners.

“In 2019, there are two challenges for investment. The first is finding scale. That’s not a problem for many private buyers, but institutional capital typically prefers larger deals, including portfolios, and there may be fewer of those in 2019,” explains Rice. “The second is pricing. While cap rates are not likely to fall further in 2019, they are low, and the premium over Class A product may be the tightest ever. So buyers will definitely need to continue to do their homework.”