WHITE OAK
PARTNERS

4960 E Dublin Granville Rd, Suite 500
Westerville, OH 43081

whiteoakpartners.com

THE STATE OF HOUSING IN TODAY'S INFLATIONARY ENVIRONMENT:

"HOUSE RICH VS. HOUSELESS"

White Oak Partners Research Team | April 2022

- *Homeownership is out of reach for many Americans due to rising mortgage rates and increasing construction costs.*
- *Home prices are up 30% since March 2020 according to the Fed.*
- *Construction materials and labor costs are significantly higher today than before the pandemic and the increases are expected to continue, which will drive up the price of newly built homes.*
- *Desirable suburban locations with access to good schools, employment, and lifestyle amenities are priced well above the market averages.*

Inflation is a top economic concern today as we emerge from the pandemic. According to the Fed, home prices have increased by 30% since March 2020.[1] While price increases for some goods and services have proven to be transitory, housing appears poised for further price increases due to demographic tailwinds and growing construction costs. As Millennials now comprise both the prime renter age group and the peak family formation ages, the growing demand for housing is expected to continue into the foreseeable future, with an emphasis on suburban living and the good schools, lower density, and low crime that comes with it. Housing attainability, especially for first-time buyers, continues to be a difficult hurdle to overcome and the increasing home prices have an outsized impact on buyers who cannot benefit from selling an existing home. Together, these factors suggest that difficulty in purchasing a home will continue to increase for potential buyers. As such, the next decade is poised to become a "House Rich vs. Houseless" period that leads to a growing demand for suburban multifamily rentals in lieu of entry-level homes.

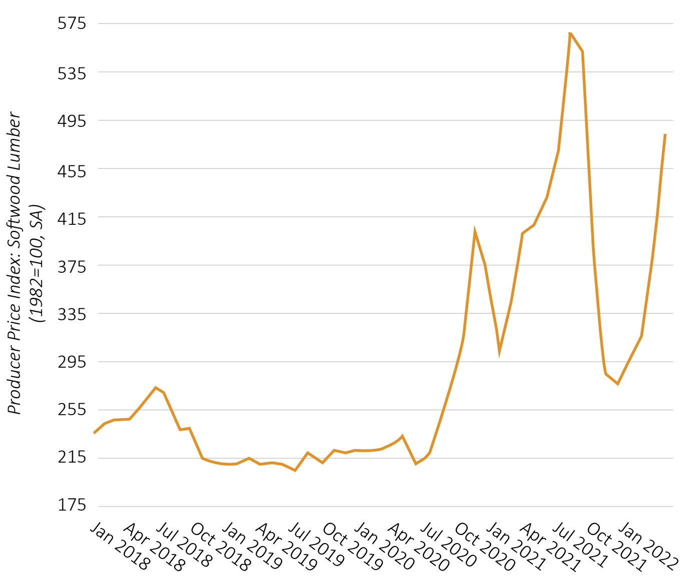
HINDRANCE TO HOMEOWNERSHIP

Buying a home has long been referred to as the American Dream. However, a combination of factors has prevented many from making this dream a reality. The average sale price for a home today has increased $90,000 since the start of the pandemic to more than $400,000, according to Fed data.[1] The pandemic drove a portion of the population to move up their timeframe for buying a home to take advantage of the privacy and lower density features of ownership. In a recent interview, Ivy Zelman of the housing research firm Zelman & Associates, reported that 70% of existing mortgages today have interest rates below 4%, compared to 39% in 2018.[2] As mortgage rates now begin to increase, the "House Rich" who are locked in at a low rate may choose to stay put and improve their current home instead of moving up to something more expensive. This stagnation of move-up buyers will reduce the number of entry-level homes on the market and prevent a greater share of first-time buyers from homeownership.

The imbalance between supply and demand for housing has been driven by demographic trends and lower than average housing additions over the past decade. Inflation has hit the construction market hard, with building material prices up nearly 30% since the start of 2020.[3] Lumber prices alone are up 74% since mid-2021, according to a report by the National Association of Home Builders (NAHB).[3] According to NAHB's analysis, average lot values for single-family homes have increased 18% to a record high of $53,000.[4] Additionally, wages for construction workers have increased nearly 10% since the start of the pandemic.[5] The increasing costs of construction has made it difficult for developers to build entry-level priced homes, which has resulted in a growing imbalance between supply and demand for the "Houseless".

SOFTWOOD LUMBER PRICES

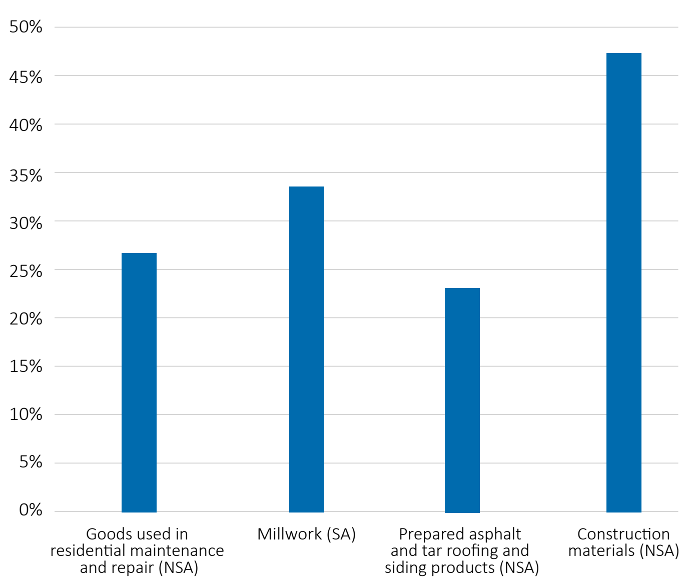
January 2018 - January 2022



Source: U.S. Bureau of Labor Statistics

CHANGE IN PRICES, OTHER INDEXES

January 2020 - January 2022



Source: National Association of Home Builders

"HOUSELESS" CLASS A RENTERS

The demographic makeup of the population supports the growing demand for suburban housing as there are 83 million Millennials in the mid-20's through early 40's age range. Married couples comprise 60% of first-time home buyers today and the average age at which people first marry is the highest on record at 30 and 28 for men and women, respectively.[6,7] The age of first-time homebuyers is the highest ever recorded by the National Association of Realtors (NAR) at 33 years. Similarly, the median age of repeat buyers is also the highest ever at 56.6. Based on these trends, it seems likely that the "Houseless" population will remain renters longer than previous generations.

Demand for suburban multifamily living is driven by the growing need for housing that caters to newly formed households, families, and residents who are moving from other cities. These high-quality apartment communities can serve as a replacement for a starter home or a suburban "test drive" prior to a home purchase. As buying a home becomes more expensive, many families with moderate to high skilled jobs will choose to rent in the most desirable suburbs as opposed to buying a home in a lower-quality location. Class A multifamily communities offer families access to a lifestyle they may want to adopt long-term if they can't afford a home purchase at today's prices. Additionally, these communities are typically equipped with luxury amenities like resort-style pools, professional quality fitness centers, and other features that many could otherwise only experience while on vacation.

The practice of renting a luxury lifestyle that features a mix of location and property-based amenities, which has been common in the large urban gateway markets for years, is spreading to the suburbs. With increasing home prices and declining purchasing power, the "Houseless" appear likely to remain renters of suburban luxury apartments longer than prior generations. There is a range of growth outcomes between markets, and some locations have experienced demographic dividends as strong population migration and economic growth have generated the additional need for services—recent growth driving future growth. Home prices in these markets have grown at rates above the national average and, as home prices continue to grow, many residents will need to put off homeownership.

INVESTORS: FLIGHT TO QUALITY

Multifamily has exhibited resilient performance throughout the pandemic and, as such, the asset class was responsible for 41.5% of all real estate investments in 2021.[8] Investors have been following the population and economic growth and investing in markets throughout the "Smile States", as 81.3% of the total multifamily investment were in these markets.[8] As we move into an inflationary environment, demand for multifamily investment is projected to continue to increase and may cause cap rates to remain steady or further compress in some markets. Multifamily has historically outperformed other real estate asset classes during times of inflation. Apartments, given the short duration of typical leases and staggered lease expirations, are uniquely positioned to re-price their rents to keep up with inflation.[8] Although interest rates are increasing today, a recent

*Examples Of Luxury Amenities

study from the National Multifamily Housing Council asserted that even with increasing borrowing costs, cap rates may remain unchanged due to the ability to grow rents.[9]

EYES ON RISK

Despite the favorable demographic and economic trends supporting multifamily, there are also some risks to consider. The institutionally owned single-family rental market continues to grow and offers residents the privacy of homeownership with the freedom and affordability of a rental. However, these communities are typically located several miles outside established locations and the extra commute time may diminish the desirability while gas prices are elevated. Lenders are starting to offer programs that cater to potential home buyers who do not have the down payment typically needed to purchase a home. While these lending programs will help some, bidding wars for homes will continue to hinder the ability of the "Houseless " to compete with the "House Rich" to buy a home. Inflation for commodities like food and gas acts as an additional tax burden on the lower-income portion of the population, and many in this group may struggle to absorb rent increases.

PAYOFF

As the imbalance between housing supply and demand continues to grow, buying a home becomes less attainable for many families. Renters in Class A multifamily communities are likely to remain "Houseless" longer than prior generations and choose to rent a luxury lifestyle in a desirable suburb instead of building equity and buying a home in a less desirable part of town. As such, demand for well-located suburban apartment communities appears poised to benefit from both demographic trends and the challenges facing would-be home buyers today.

Resources

1. *Fed - Median Sales Price of Houses Sold for the United States*
2. *Moody's Podcast - Higher Rates and House Price Angst*
3. *NAHB - Lumber and Paint Lead Building Materials Price Increases in January*
4. *Eye on Housing - Lot Values Surge at Record Breaking Pace*
5. *Fed - Average Hourly Earnings of All Employees, Construction*
6. *Money - Here's How Old the Typical Homebuyer Is Today*
7. *RealPage*
8. *Newmark US Multifamily Capital Markets Report 4Q21*
9. *NMHC - What Rising Interest Rates Mean for Apartment Cap Rates*

CONTACT US

MICHAEL MENZER
Chief Executive Officer
mmenzer@whiteoakpartners.com
614-741-7790

JAMES CRAMER
Partner, President
jcramer@whiteoakpartners.com
614-741-7797

ANDREW CARR
Partner, Head of Capital Markets
acarr@whiteoakpartners.com
614-741-7736

BENJAMIN BARNES
Partner, Chief Investment Officer
bbarnes@whiteoakpartners.com
614-741-4628

4960 E. Dublin Granville Road,
Suite 500
Westerville, OH 43081

whiteoakpartners.com