APARTMENT INDEX

LAGGING APPRECIATION IS A DRAG ON APARTMENT RETURNS

Decreased property appreciation led to a nationwide slowing of total apartment returns in 3Q19, with year-over-year appreciation of only 1.08%. This continues a downward trend and reflects a level that is nearly one-third of the 20 year average. Apartment performance is best characterized as steady, but slowing. Investors are still actively pursuing the asset type, as indicated by total transaction volume remaining near 10-year high levels in 3Q19 according to CoStar. As the second largest property sector within the NCREIF Index in both property count and total market value, apartments weigh heavily on the Index. Apartment returns lag those of office and industrial properties, which have outperformed apartments in both income and appreciation metrics.

Although total returns remain positive in all regions due to continued income growth, they slowed to 1.18% in the most recent quarter and 5.39% for the year ending 3Q19. The West and South regions continue to lead the sector, with one-year returns of 6.50% and 6.15%, respectively. The Mountain division of the West region provided returns at nearly double the national average; yielding 2.63% in 3Q19 and 9.35% over the past year.

Appreciation returns are the driver behind the slow-down in total returns. The nationwide property appreciation rate has decreased from 0.36% to 0.13% over the past quarter, with the East region indicating the most dramatic shift quart-over-quarter. The East recorded a 54 basis point swing quarter-over-quarter, yielding negative appreciation of 0.40%. However, it is noted the East remains positive on the year and only the Midwest region is negative over this time period.

Of note is the continued strong performance of garden apartments in comparison to high-rise developments. Garden developments indicate 8.05% total returns over the past year, with appreciation returns exceeding 3%. This is in contrast to 4.15% total returns for high-rise projects, with 0.13% attributed to appreciation. As high-rise projects remain a desirable vehicle in which to place significant funds with less perceived risk, we believe the returns will remain compressed for this subsector.

Income returns remain steady on a national level and are relatively consistent among all regions, with a tight range of 1.03% to 1.07%. Occupancy remains strong within most major markets, with nationwide vacancy remaining below 6% according to 3Q19 CoStar data. The number of units under construction decreased 3% over the past year, but trailing 12 month absorption fell to its lowest level since 1Q18. The true impact of recent rent control laws and other legal implements aimed at creating more affordable housing are not yet known. However, such restrictions and requirements are likely to lead to decreased income growth over time.

Jim Newell, MAI
Executive Managing Director
Qval Property Advisors

APARTMENT TOTAL RETURNS

	Total NPI	Total Apartment	East	Midwest	South	West
3rd Q 2019	1.41	1.18	0.64	0.78	1.52	1.52
2nd Q 2019	1.51	1.42	1.20	1.24	1.52	1.61
One Year	6.24	5.39	4.32	2.85	6.15	6.50
Three Years	6.76	5.99	4.75	3.71	6.31	7.50
Five Years	8.57	7.66	5.88	5.92	7.83	9.79
Ten Years	9.77	9.83	8.20	9.33	10.17	11.44
Twenty Years	8.80	8.65	8.01	7.69	8.79	9.85

APARTMENT INCOME RETURNS

	Total NPI	Total Apartment	East	Midwest	South	West
3rd Q 2019	1.11	1.05	1.03	1.07	1.06	1.04
2nd Q 2019	1.12	1.06	1.05	1.09	1.09	1.05
One Year	4.53	4.28	4.20	4.32	4.45	4.21
Three Years	4.60	4.34	4.20	4.35	4.57	4.32
Five Years	4.75	4.49	4.30	4.48	4.80	4.46
Ten Years	5.37	4.95	4.66	5.10	5.35	4.88
Twenty Years	6.25	5.57	5.39	5.68	5.91	5.48

APARTMENT APPRECIATION RETURNS

	Total NPI	Total Apartment	East	Midwest	South	West
3rd Q 2019	0.30	0.13	-0.40	-0.28	0.46	0.48
2nd Q 2019	0.38	0.36	0.14	0.14	0.43	0.56
One Year	1.65	1.08	0.12	-1.43	1.64	2.23
Three Years	2.09	1.59	0.53	-0.62	1.68	3.09
Five Years	3.69	3.07	1.53	1.40	2.93	5.16
Ten Years	4.23	4.71	3.43	4.08	4.64	6.34
Twenty Years	2.44	2.95	2.53	1.93	2.76	4.20

APARTMENT INDEX—QUARTILE RANGE OF RETURNS