Freddie Mac MULTIFAMILY

Las Vegas Fundamentals

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Luba Kim Reynolds [00:00:02] Las Vegas offers world class gaming, shopping, fine dining and entertainment, and is often referred to as the entertainment capital of the world. The leisure hospitality sector employs about one third of Las Vegas workers and represents 10 of the top 11 employers, according to Moody's Analytics. It's no surprise that we keep a close eye on this market, and it was a hot topic during covid pandemic. Today, we're taking a closer look at the market. We will discuss macro data, but also really looking to get into some of the on the ground information that will allow us to hear from our external clients. We have fantastic guests on today's podcast, our very own Sara Hoffman from in-house multifamily research team, and Ken Woolley, who is the founding director of The Farther West Development and the West Corp. Management Group. Welcome. So Ken we are so excited to have you on this podcast today. You have a very unique background and expertise. Nevada West does a lot of business in Las Vegas and also you have a lot of expertise in general that is very unique. We would love to hear a little bit more about you, but also will be really helpful for the listeners to get to know Las Vegas a little bit better. Any insight you can provide us on some markets and their main differences would be really helpful to us.

Ken Woolley [00:01:28] Very good. It's nice to be here Luba and Sara. Just for a brief introduction, I've been developing multifamily in Las Vegas since 1988 and have developed 18,000 units in that period, 50 projects continuously over the time frame. So I have a lot of experience in the market. With respect to the the market as a whole, Las Vegas has been growing except for the credit crisis of 2008 to 2012 and then again for a very brief period when the pandemic started, when we lost so many jobs. The submarket of Las Vegas are basically you have a very strong area to the south in the city of Henderson and to the southwest and to the west and the northwest of the valley. But the the middle of the city is old and is not doing well. North Las Vegas and the east side of town or areas where rents are lower and it's very difficult to develop and there's more difficulties with collections, etc.. The best submarkets are in the planned communities, Summerlong being one of the very best in our city. We also have Green Valley and we have Seven Hills and Anthem and now in Inspirata. All of these are large planned communities and these are the areas which are growing the fastest and these are the areas where the rent growth is the best in apartments.

Luba Kim Reynolds [00:02:58] Thank you, Ken. And Sara, would you mind to introduce yourself to the listeners here? And on the macro level, how does Las Vegas compare to the rest of the nation and what have we learned during the pandemic?

Sara Hoffman [00:03:11] Thanks Luba for having me. I'm happy to be here. I love talking about the different metros in the nation as a whole. I like to say is where we sit in Freddie Mac in the research side is we're kind of at the ten thousand foot view. We look at the top seventy five or so major metro areas across a number of different macroeconomic factors and multifamily fundamentals. Las Vegas has always been an interesting one. Historically, it has seen some volatility, as Ken was mentioning, leading up to the great financial crisis was a really strong market. But then we saw a steep decline and took many years for the Metro to then recover. And traditionally, as you said, Las Vegas has been very dependent on the overall nation's economic strength with nearly, as you said, over a third of the workforce dependent on that leisure, hospitality and tourism sector. You know, in the overall economy is healthy people spend a little bit more on travel, go out to eat, go to the shows, do some gambling and that always helps support the Vegas economy. However, during slower times, you know, traveling and tourism is one of the first thing that people cut out of their budgets. And that's when we kind of start seeing there to be a little more stress in the areas. And the onset of the pandemic, as everything was shutting down, our concern turned to the Las Vegas market, the concern being that we could see weakened multifamily fundamentals there. Just given the anticipation of large job loss numbers. However, as we kind of talk some more, that didn't necessarily play out for all of 2020. You know, we said it was a real quick, sharp hit. But, you know, as we kind of keep discussing, I think it kind of took us a little bit by surprise what the final numbers ended up being. But that's where it's great to be able to kind of look back at that and great to be able to talk with Ken, since you're there on the ground in Las Vegas and you can kind of give some more insight, kind of help with the numbers and the data that we see where we sit. So I think it's great, thanks for having me and looking forward to the conversation.

Luba Kim Reynolds [00:05:07] Perfect. This is a great setup. So let's switch gears. Ken let's talk about demographics. I know you mentioned in our pre-call there has been some interesting changes recently in the migration of the people to the submarket. Any any insights you can give us about what has been happening?

Ken Woolley [00:05:29] Well, let me first start by saying when the pandemic started, we were really worried. You know, within the first six weeks, there was 30 percent unemployment in the Las Vegas Valley, which is a very dramatic downturn. And people were not able to pay their rents. We had properties lease up, renting was was slow, obviously. And then something happened. We started getting people coming from primarily California, but also other states moving into the state. And we started seeing our new properties, having very rapid leasing. And this was by last June and July. Our leasing pace was much faster than it had been in previous periods. And as you drive through the parking lots now, you'll see somewhere between 15 percent to 20 percent of the cars are from California and other states, but mostly California. And this is unusual. But in the past, we had some people from out of state, but not so many. This has led up to where we are today, which is our occupancies are 100 percent. And this is in six properties that we own and they're very high in the properties we operate. In the 40 years I've been in the market, I have never seen 100 percent occupancy and rates going up like they have. The demographics of the people are basically it's millennials and the average age is in the range of 40 to 42. We have some older people, but not very many. Our apartment dwellers primarily are without children. So even though we have two and three bedroom apartments, we don't have very many children. So we're not seeing a lot of families per say. We're seeing a lot of young single adults or young married single adults moving into our properties. Also, the income levels are quite high. The household income levels are kind of 80 to 90 thousand, which is high, really. So we have people with money. And then you say, well, what happened? We still have high unemployment in our city. I think it's still in the range of eight, nine percent, but it's coming down very rapidly as the casinos open back up.

Sara Hoffman [00:07:56] That's great to hear. You know, the population moves because that's one thing that we were looking at, too. And we actually saw a report by CBRE that analyzed the USPS change of addresses, this would be excluding temporary changes. And so I looked at the difference, 2019 to 2020 and it shows similar patterns, as you mentioned, that the moves from California, just the state of California into Las Vegas increased 13.6% year over year. So you'd expect some increase just as general population increases. But then they broke out the share. And so the share increased from a 9.6% share of total moves into Las Vegas came from California in 2019. And in 2020 that jumped up to 10.4%. So the overall piece of the pie of moves was much higher. Now those numbers might sound kind of low, like about 10%, but that's taking over all the moves. And as we know, the majority of moves or change of addresses are going to be within the metro area. It's almost about 75-80% are within the Las Vegas metro area. Southern California is the next highest.

Ken Woolley [00:09:02] So what you're saying is that if you look at the moves into the valley, a much higher percent than 10% are coming from California. I don't know the percentage. You may have the data. I'm just giving you anecdotal information about what we're seeing at our apartment rentals.

Sara Hoffman [00:09:17] And that's why I like talking to you. Can you see the car license plates, as you said, and we can match that up to the data. So I guess the differentials might sound kind of small, but just looking at the change like that, 13.6% increase equated to about thirty five hundred address changes. If you kind of just assume one household to an address change. And that's an additional just thirty five hundred from from California coming in.

Ken Woolley [00:09:43] We've always had a pretty good apartment production, but if you look at the production of apartments as compared to the in-place number of apartments, we're only running about 1.5% of employees apartment stock, which is not very high compared to other cities. For example, this is this is data from Yardie, the city of Austin in the past year has a 5% increase in the number of apartments. Denver 4%, Raleigh, North Carolina 4%. Las Vegas was only 1.5%. So we're having a huge influx of people. We're not having as much production. And so that's causing rent growth, which is pretty high right now.

Luba Kim Reynolds [00:10:30] Let's touch on supply. Sarah, when we look at the historical completion of the units. It looks like they have picked around early 2000s and then started to decline with just some modest growth in the recent years. Can you tell us what you have observed in the market?

Sara Hoffman [00:10:46] Yes, I mean, that's a great point. So when we kind of start getting questions on different markets or, you know, like I said, Las Vegas is a unique one to us because we all had expectations of what could happen last year at the onset of the pandemic and we thought we seem to have seen the opposite. So then we kind of start digging in and so one of the first things we go to supply and demand story. Demands a little harder, I know it's great being able to talk with Ken about what he's actually seeing, but it's hard to get the demand numbers. But the supply numbers, you know, those those are more readily available. And what we do is we took a look historically and as we've been saying, it's no surprise we saw it, we all know what happened in the early 2000s leading up to the great financial crisis with really strong household household construction. So a lot of completions and that was both in the Single-Family and Multifamily space. And so then when you talk about like post the great financial crisis, a steep drop off, and then we kind of look at how it's been recovering. It's hard to kind of really say where equilibrium is, it's hard to kind of draw a line in the sand of this is where it needs to get back to. There's a lot of different factors that can influence how much housing is needed in an area. But we kind of just looked at where construction was compared to its peak that was seen in the '06 timeframe. And we compare that to kind of the national level. And then at the national level, total housing completions has bounced back to about 65% of that pre-crisis peak. Again, we're not saying housing needs to go back to the peak, but it's just the way to kind of benchmark. In Las Vegas it's only at about 36%, so it's really not kind of following that same trend as the nation. And at the same time, when you look at just the past couple of years, while the nation still continuing to grow on an upward trend, the Las Vegas is actually shown flat. So the total housing completions has remained flat over the past couple of years instead of that continuing upward growth. So we're not kind of really seeing where the market needs to be, but just kind of seeing those construction trends compared to the national level.

Luba Kim Reynolds [00:13:02] Right. And that's what's very interesting, right? So on the one hand, you have all these people moving into the states. So it would sounds like the construction really should be accelerating and picking up, but it doesn't seem that way. Can any insights what's going on in the market? Why we don't see more cranes in Las Vegas?

Ken Woolley [00:13:24] There's two or three factors. I'd say the first factor is there has been a seat change in the politics here in the Las Vegas Valley. The two main jurisdictions are Clark County and the city of Henderson. Both these jurisdictions have tightened up and made it very much more difficult for developers to get approvals, to build apartments and approvals to build Single-Family. So that's those two factors have slowed down the process dramatically. It's becoming a little more like California, not so much like Texas. It used to be more like Texas. So that's one factor. Second factor in the apartment side was and to some degree, the Single-Family, when the Great Depression/Recession happened, Las Vegas was hit harder almost than any metropolitan market. And many of the developers went under and many projects were foreclosed on. Our company, we were fortunate, we had sold everything, we didn't own anything when it all happened. And we actually started construction again on a new project in the summer of 2009 and we started another one in 2010. And we were able to build apartments at very low cost and they were very profitable because people always want to move into new apartments even when there's vacancy. So we have high vacancy, lower...rents have gone down since then. It taken a long time to sort of people to get geared back up. And I think for national developers, our market has been looked at with concern as to it being too risky. Now it's happening. We're seeing people or companies from other parts of the country come here and build. Another factor that has kept the production or the supply low has been the lack of land. Much of the land here in this valley is owned by the Bureau of Land Management. And in past years, the BLM has released land in auctions so that land could be available to develop. In the last few years, they've been much more stingy about that. So new land does not come on the market for the possibility of new development. So it's constraining the supply of land, even though, as you think about Las Vegas, there's plenty of desert all around it's not very much in private hands. So that that constrains the the growth further. So those three factors going back - number one, the politics of change is much more difficult to permit. Number two, there's a shortage in the supply of land due to the lack of new auctions from the BLM. And number three, the devastation, the financial devastation of many of the local developers who are just sort of coming out of it now. Those are all supply limiters.

Luba Kim Reynolds [00:16:16] This is very interesting, it'ss such a great insight, Ken. And I love how we're going back and forward between the macrodata that Sarah's providing and all the color that you have from the ground. So let's continue this and I think now we are jumping to actually one of the most interesting and complicated topics which relates to rent growth, rent collections, vacancies in the market. So maybe let's do the same thing. Sara, you start off with giving us a little bit of a macro overview of the trends and Ken then we'll jump over to you to see what's what's really going on in the market and what you see on the ground.

Sara Hoffman [00:16:56] Yeah, I think that sounds great. So as we were talking about kind of total housing construction, maybe I'll kind of start there by looking at overall housing vacancy rates. And we found that leading up to the great financial crisis, total vacancy rates in Las Vegas was actually slightly below the national level, which was at about 10%. And then after or during the crisis, in the years after, vacancy rates in Las Vegas increased up to peaks about 16% and well above the national level. Since 2015 it's come back in line with the national average and is actually then followed, it's kind of bounced around the national trend line which is a downward sloping line. So when we compared it back to the total construction, when we compare now with vacancy, you know, vacancy rates are following the national trend, whereas we were mentioning earlier the construction trends weren't. So I think that kind of goes to Ken's point that there is strong demand there and a lot of the vacancy rate remains tight so the housing supply remains tight. Now, when we look at then the Multifamily side of it, like I said last year, kind of threw us for a curveball. We all anticipated that Vegas was going to be one of the harder hit metros, but then at the end of the year, we actually saw the opposite. You know, it had very strong occupancy, as reported by Reise, the vacancy rate actually declined throughout the year instead of increased. It's about 3.9% as of the fourth quarter at year end. And and to put in perspective, the average that Reise reported going back to the 80s is about 5.5%. So that's very pretty well below its long term average there. Likewise, the rent growth was pretty strong, around 3% compared, according to Reese. And then RealPage had a little bit higher, about 3.5%. And these numbers maybe in 2015, wouldn't be too much to blink an eye at but in 2020 when national rent growth was negative or at least flat, depending on the data provider, that's very robust rent growth. And again, not what we were expecting at all with an economy that was tied so heavily to tourism and seeing that completely stopped that you were still able to get get that demand in to help boost rents. Our expectations for for going into this year is for that trajectory to continue and continue to see strong rent growth in the metro, maybe upwards of about 4%. And that's a little bit on the overall economy also recovering and we expect that to help boost in many metro areas, especially Las Vegas. So on the flip side, though, when we talk about, you know, rents and vacancies looking strong when we look at the rent collection, so this is the amount of rent that is collected by the, you know, at a property level in the tenants. RealPage breaks it out nicely across different Metro areas and Las Vegas does see a bit of a bigger gap in the rent collections currently compared to pre pandemic levels, and that's on a month to month basis. So we compare, say, May rent collections in 2021 to neighboring collections in 2019. So we kind of try to, try to keep the seasonality impacts muted there. But there is a bit of a larger gap there in Las Vegas compared to some of the other metro areas. In general, we've not really seen a strong correlation between rent growth and rent collections at the metro level. Meaning, you know, intuition would be that maybe those with weaker rent growths would have also seen weaker rent collections. But that's not necessarily the pattern that we've seen with the with the limited amount of data that we have. So that was kind of one of our interesting when we looked at all the data pulling it all together, know those two things didn't quite go hand in hand, which made us kind of want to deep dive into Las Vegas a little bit more.

Ken Woolley [00:21:09] Well, yeah, it's it's interesting. You know, if you classify apartments between sort of A, B and C, we're primarily in the A category. And CBRE does a, you know, they do a study of Las Vegas and right now they're their analysis is that the vacancy rate is 2.92% in class A. And having come down from the pre pandemic rate, which was more in the 5% range, which is very unus-... 5.5%, right, in April or February of 2020.

Luba Kim Reynolds [00:21:42] Thank you both. It looks like Vegas is recovering very well - shows opening up, hotels have fully booked, what do you see for Vegas in the next few months?

Ken Woolley [00:21:52] I see nothing but good here in the apartment business because you have the hotels coming back to full occupancy. The airport is back to basically 100% of what it was before the pandemic. And then you have all this influx of people coming from high tech states to Nevada where we don't have an income tax. So you have that additional pressure on the move inside. So I think we're going to see a lot more inflation in the house prices and in rents and costs are going to go up here. So it's a good place to be right now.

Luba Kim Reynolds [00:22:30] Got it all very positive. Sara, internally, how do we feel about Las Vegas right now? Anything that we need to be mindful of or still on your watch list? How do we treat it?

Sara Hoffman [00:22:43] So I think I mean, these have all been great points. And as we kind of look through and think about future, we can see a lot of people from California are moving there. Like I said, the data we had from that CBRE report wasn't temporary addresses. So it wasn't just people like, "OK, I got a few months, let me go somewhere warmer where I can be outside more." But it will be interesting once things start moving back to normal, are people going to go back into the workplace or are these people who move...you know, we don't know the reason why these people moved. Did they move because they can work remotely, but are they going to be called back in? And even if it's partial back in, do they want to still be closer to their to their workplace? I know there's been some talk about, you know, the financial institutions are showing a lot more people moving back to be close to work because the banks are asking people to be in the office. Tech companies might might be a little bit different. And, you know, just to generalize, the type of industries in California, is that is that what we saw move to Las Vegas? So that that level of detail, I don't think we can really get our hands around and know. But, you know, that's just kind of what we think through as the long term impacts. But I think relative to the supply story that we've been talking about there, we can see that there does seem to be lower supply in the Las Vegas metro, especially after the Great Recession. A lot of that's been absorbed, even the shadow supply from the Single-Family market after after the Great Recession. So we can definitely see that there's lower supply there. And with higher demand, whether it's all going to be permanent or some move back, it's a good amount of demand that's going to keep the market strong in the in the short term over the next couple of years.

Luba Kim Reynolds [00:24:25] Thank you Sara and Ken for joining me today. I loved our conversation about Vegas and it's really helped to understand some of the nuances of this very interesting market. I'm looking forward to Vegas continuing to recover and perform its historical levels.