Newmark Knight Frank

NKF PERSPECTIVES
PHILADELPHIA MULTIFAMILY

HOW HAS THE MARKET WEATHERED THE PANDEMIC?

As a new decade dawned, the Philadelphia multifamily market was flourishing, with low vacancy, strong demand, rising rents, new supply delivering and more in the pipeline. Since March 2020, the spread of COVID-19 and ensuing disruption has caused unprecedented swings in economic conditions. This will undoubtedly challenge the region's multifamily sector in the short- to intermediate-term as many renters face loss of income. However, multifamily rent collections since March have proven to be better than expected, only slightly lower than collections a year ago. Further supporting a cautiously positive outlook for future multifamily collections: as personal consumption expenditures have plummeted, the national Personal Saving Rate skyrocketed from 8.0% in February to a whopping 33% in April, its highest point recorded since the Bureau of Economic Analysis started tracking the measure in 1959. This indicates that people will have more money saved for essentials – like shelter – going forward into the reopening of the economy.

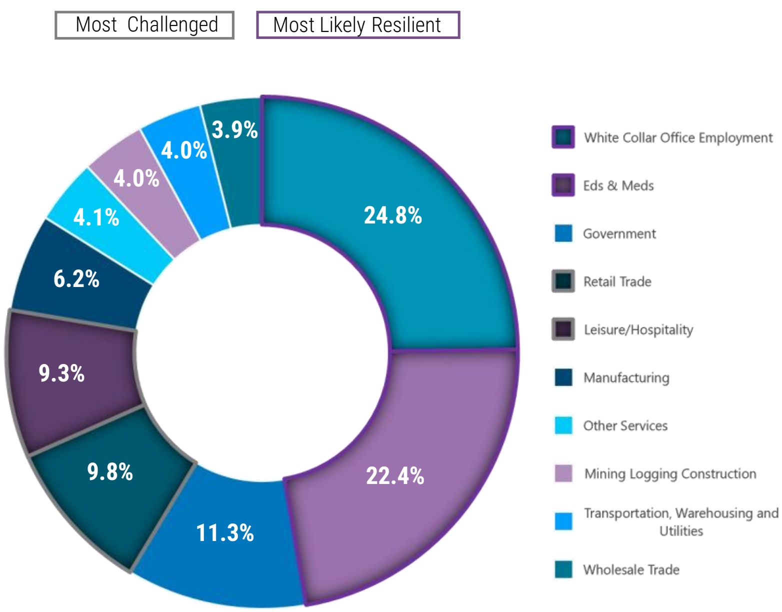
Greater Philadelphia as a whole is well-poised to withstand this shock to the system and return to the stability that has characterized the market for decades. This stability is and will be supported by three core factors:

- The bulk of the regional economy comprises industries that are more resilient and adaptable to the unique obstacles social distancing mandates have created.
- Greater Philadelphia has less economic exposure to the industries most impacted in this disruption and has already seen the bulk of job losses that are likely to be sustained during this economic downturn.
- Supply additions have remained modest for years, leading to pent-up demand that developers have started to react to only relatively recently. While individual submarkets may grapple with supply additions outpacing demand, the overall market is facing less potential oversupply than other comparable markets.

A DIVERSE ECONOMY ANCHORED BY RESILIENT SECTORS

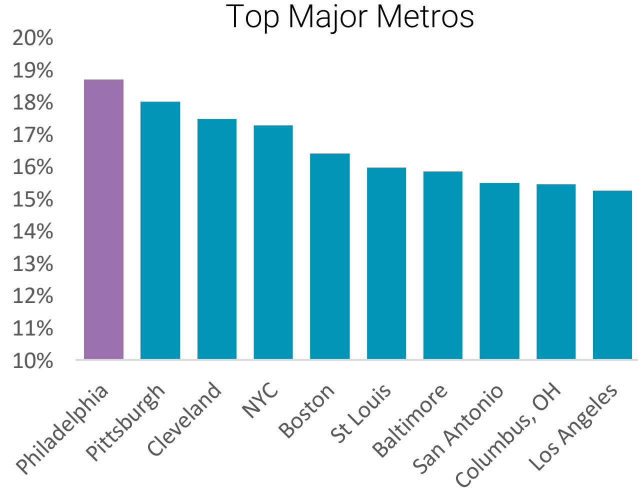
Multifamily market stability is fundamentally predicated on the job security of its residents. Nearly half of the workforce in the Philadelphia MSA is employed in either "eds & meds" (education and medicine) or white collar industries (professional & business services, financial services and tech), typically higher-

EMPLOYMENT BY INDUSTRY
Philadelphia MSA, Annual Average, 2019



Source: US Bureau of Labor Statistics

HEALTHCARE AS A PERCENTAGE OF OVERALL EMPLOYMENT
Top Major Metros



Source: US Bureau of Labor Statistics, JobsEQ paying industry sectors. In past recessions, local and national white collar employment has suffered, particularly financial services, but with this recession spurred by a health crisis, many white collar office-using firms have successfully transitioned to work from home strategies and have been insulated from sharp job losses. White collar office-using industries represented just 10% of the metro's total job losses in March and April 2020. As for eds & meds, Greater Philadelphia's bulwark sector, healthcare in particular has proven to be an unparalleled economic driver, growing strongly for decades, even through recessions. The healthcare industry is undeniably facing unique challenges in this health-driven crisis and has been hit hard with job losses, but is expected to rebound when the economy reopens, as healthcare is a basic human need. As of May, some Philadelphia-area medical systems resumed elective procedures, and as virus cases continue to decline, non-life-sustaining medical care will expand, likely restoring job losses sustained in this sector.

Further supporting a cautiously optimistic view of the Philadelphia economy's resilience: less than 20% of Philadelphia's economy is exposed to the hardest-hit industries of retail trade and leisure/hospitality, contrasted with Florida metros like Orlando and Miami with outsized economic dependence on tourism, where those two industries total 32% and 25%, of the economy, respectively.

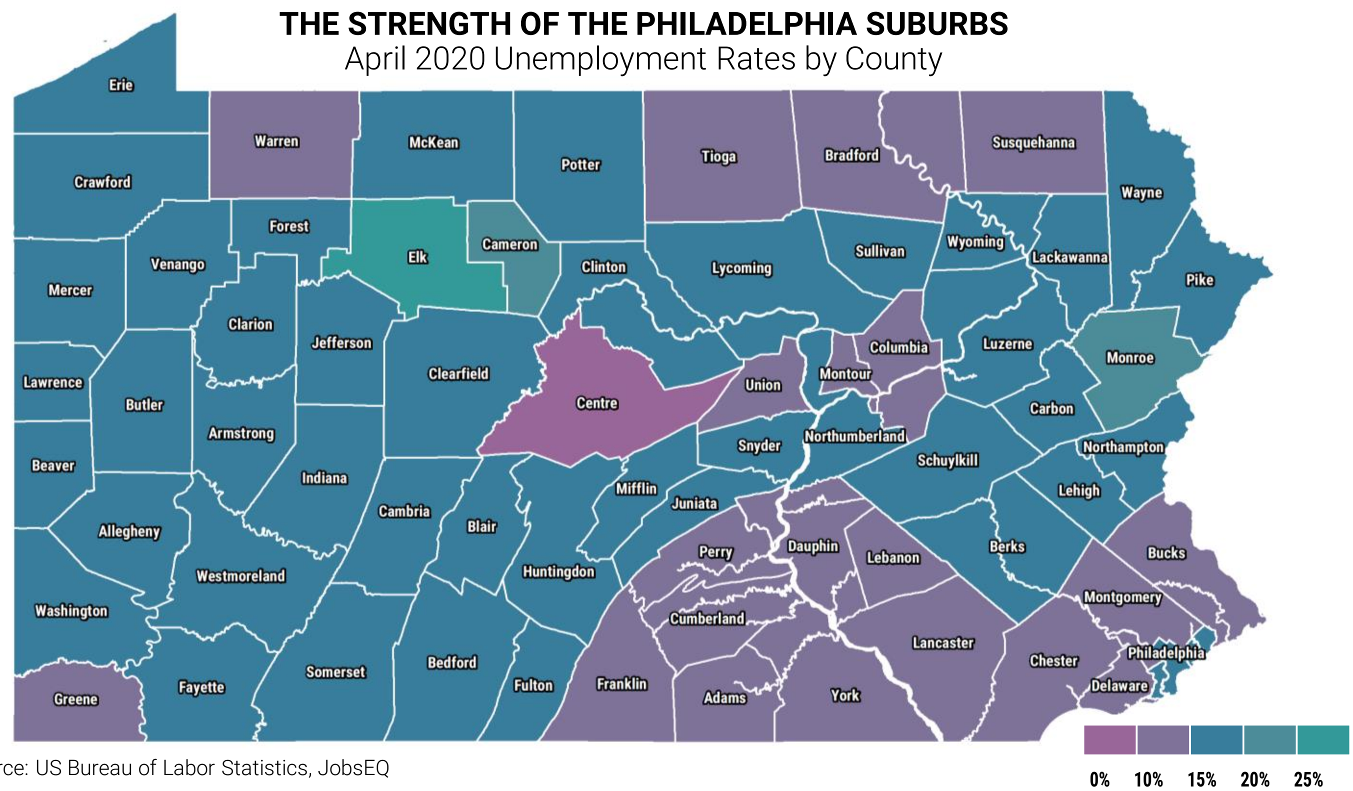
GREATER PHILADELPHIA'S PERFORMANCE WITHIN A HARD-HIT STATE

Pennsylvania was one of the first in the nation to declare a state of emergency and implement aggressive lockdown guidelines to curb the spread of COVID-19, which has contributed to an economic disruption of longer duration and a higher number of unemployment claims relative to other states. From a position of pre-COVID-19 strength in February, the state's unemployment rate shot up from 4.7% to 15.1% in April, in a tie with Massachusetts for the 16th highest unemployment rate in the nation. Yet, new jobless claims in Pennsylvania have steadily decreased every week since the end of March, in contrast to fluctuating performance in many other states - indicating the bulk of job losses related to COVID-19 disruption has already hit.

While no county has remained immune from a staggering increase in unemployment, among the counties that realized the lowest unemployment rates in April were those in Greater Philadelphia, particularly the suburban counties. Chester County had the third lowest unemployment rate in the state at 11.3%. Bucks, Delaware and Montgomery counties also fared better than 73% of the state in terms of April unemployment rates. In Philadelphia County, where unemployment exceeded the state average, rising to 16.5% in April, half of all job losses were concentrated in hospitality and trade alone – industries that will unfortunately continue to struggle throughout the rest of the year. However, as the local economy reopens in June, Greater Philadelphia has more jobs intact than most of the state and therefore is on better footing for the path to recovery.

THE STRENGTH OF THE PHILADELPHIA SUBURBS

April 2020 Unemployment Rates by County



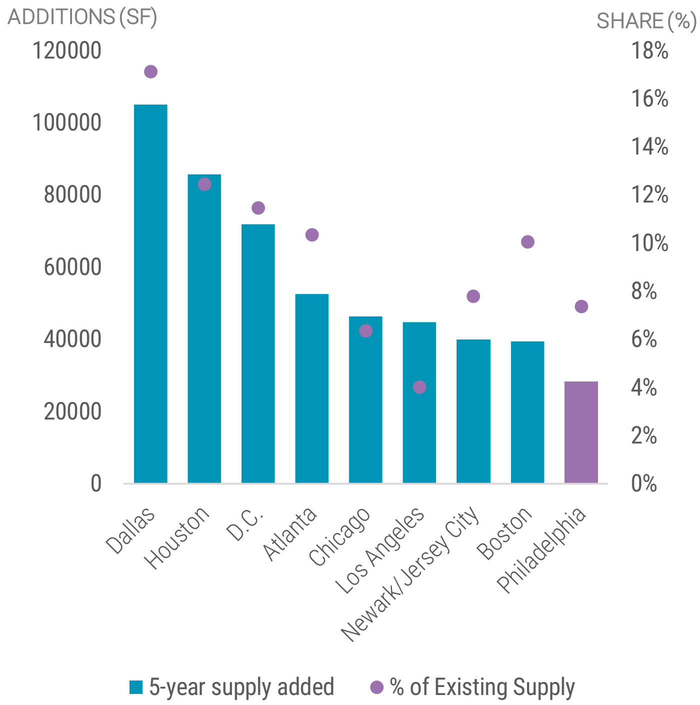
Source: US Bureau of Labor Statistics, JobsEQ

STRONG MULTIFAMILY FUNDAMENTALS

One of the defining factors of Philadelphia's multifamily market stability is a lack of overdevelopment. Although development has significantly picked up over the past few years on the heels of population growth and in particular, in-migration of younger professionals from fellow Northeast Corridor metros like New York and Washington, D.C., the last five years have only added only about 28,000 new units to the market, the lowest supply volume of any of the top major metros (excluding San Francisco). This has kept demand in line with supply and has pushed vacancy down to 3.5% in 1Q20. In addition, the Philadelphia market has seen limited exposure to recent trends yet-untested by market shifts and downturns, like the rise of short-term rental operators leasing multifamily units (See NKF's report on this trend, "Flexible Flats", from January 2020).

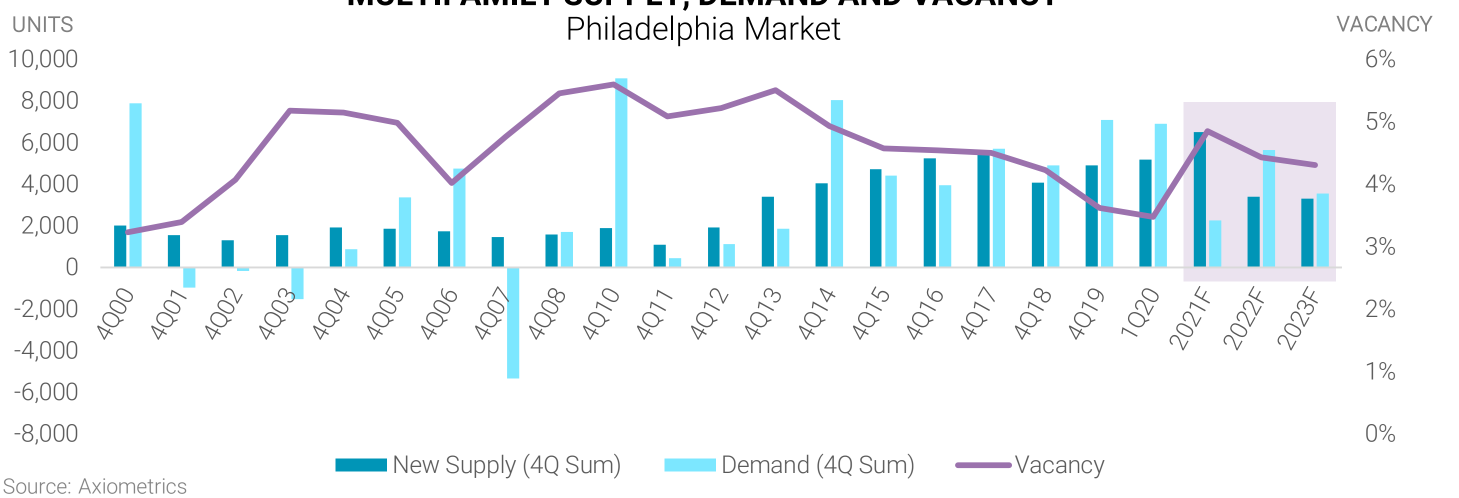
Looking forward, there is certain to be some measure of volatility in the multifamily market. As of 1Q20, the supply pipeline measured 10,100 market-rate rental units, and new supply is forecasted to take longer to lease up – especially luxury product. This will likely lead to an increase in market vacancy, as forecasted by Axiometrics in the figure below. The post-COVID-19 environment may keep future development muted – projects in planning could be sidelined due to equity issues or simply because, with shifting underwriting assumptions, they no longer pencil out. This potential pause in new development coupled with the resiliency in Greater Philadelphia's diverse economy is expected to help buoy market stability in the mid-term.

5-YEAR MULTIFAMILY SUPPLY ADDITIONS AND SHARE OF CURRENT INVENTORY
By Major Market



Source: Axiometrics

MULTIFAMILY SUPPLY, DEMAND AND VACANCY
Philadelphia Market



Source: Axiometrics

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