

# Will Boston property market absorb new luxury rental apartments?

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By Dr. Tina M. Bacci

With so many new apartments entering the Boston real estate market, we are continually asked whether the supply of luxury apartments will far exceed the demand. Given the current market conditions, the answer is still no. Vacancy rates are low across the Boston apartment market, which is a solid indicator that demand is still strong and the new apartments will continue to be absorbed. Even with hundreds of new units entering the market last year, Downtown Boston closed 2013 with an overall 3.9% apartment vacancy rate, which is lower than the five year average of 4.4%.

It is true that many new luxury apartments in the new buildings are vacant at this moment and buildings that opened in 2009 or later carry a collective 70% vacancy rate, however the overall vacancy rate continues to remain low because the new inventory accounts for less than 10% of the overall rental market, a relatively small segment.

Market Conditions: Low condo inventory, old apartment inventory

The Boston housing market is well positioned for the absorption of the newly opened luxury rental buildings, as well as the additional hundreds of luxury apartment units expected to be delivered in the next year, because the overall housing supply is still tight. It might seem unusual that the new apartments are entering the market in quick successive order, and indeed it is. However, given the scarcity of inventory in the Boston condo market and the metro areas surrounding Boston, the new onslaught of apartment inventory provides much needed housing supply. The Boston condominium market currently has less than a month's supply of inventory and very little new construction condos are in the immediate pipeline. Similarly, Cambridge and Somerville condo markets are below a one month's supply of inventory.

The demand for housing in Boston is evident. Last year's condominium market set a record with \$2.79 Billion in condo sales. The number of sales transactions exceeded 3,600 and 60% were over \$500,000. 2013 was one of the top three years for the number of sales transactions in the last 10+ years. In an unusual twist, last year's market was fueled almost entirely by a strong re-sale market. In previous years with a high number of sales transactions, new construction closings drove the number of transactions up because many of the units were put under agreement in the year or two before they actually closed. In 2013, there was a very limited amount of new construction closings taking place and many of the new construction closings that did occur were units that went under agreement and closed within the same year. This surging re-sale market shows indication of pent-up demand for housing in Boston.

Low condo inventory coupled with high demand for housing helps the apartment market in two important ways.

Regardless of the condo supply, life still goes on. Job transfers, expanding households, emptying nests, and other factors require moves whether the market conditions are ideal or not. If the condo market can't suit the needs of Boston's residents, the luxury apartment market will try to make the most of the opportunity.

The Spring condominium market is already flooded with people who have to find new housing and many of them won't be able to find a condominium that suits their needs or budget. Inventory is just too tight. After these hopeful homebuyers spend a few weeks or months searching, they may realize a rental apartment can suit their immediate needs for the location and lifestyle they want. That decision may end up being a long-term decision if the building they choose ends up working for them.

The new luxury apartments provide a lifestyle that is very attractive and, in many cases, very comparable to condominium living. For would-be buyers who are now turning to renting when faced with limited options for buying, the new luxury apartments offer a pleasant alternative and a lifestyle experience that is more akin to condo living than what previous rental buildings offered. Boston has needed new rental inventory for some time now, given that 60% of the existing apartment inventory was built prior to 1980. Many of the new luxury buildings feature condo-style finishes, state of the art amenities and services, windows that open, high ceilings, and updated systems. These new buildings are also designed to offer more variation in the stock of luxury apartment inventory.

More unit variation

The new luxury apartment inventory brings unit types and sizes that offer the rental market more variety in floorplan options as well as pricing options. As one example, many of the existing luxury apartment buildings were designed with little to no studio apartments. The Devonshire, The Colonnade, The Greenhouse, 1330 Back Bay Fens, Exeter Towers, Mandarin Oriental Apartments, etc. have no studios and there are less than twenty studios combined in Archstone Boston Common, Archstone Avenir, One Back Bay, West End Residences, and the Lofts at Atlantic Wharf.

The new inventory coming into the market brings more studios and small 1-bedroom units to the market. The Victor alone, for example, adds 44 studios to the inventory pool and approximately 75% of its units are of the studio or 1-bedroom type. Similarly, at The Radian at 120 Kingston Street, 80% of the 240 units are programmed as studios and 1-bedroom units. These new unit types will offer more housing

options for single professionals.

#### Race to the finish line

While the overall market is still very much in favor of these new luxury rental communities, the battle for each building to achieve a timely and profitable lease-up will be won or lost on the leasing floor, one renter at a time. The question is not whether these new rental buildings will be leased up. Rather, the question is which building will lease up first and who will achieve maximum profitability versus the competition. Overall vacancy is low, but for each individual renter looking to lease a new luxury apartment there is a variety of building options and there are several vacant units to choose from. The battle is won or lost by the leasing team.

Creating a distinct lifestyle experience and a unique value proposition will be critical to the success of any lease-up in the current market setting. Properly identifying the target audience and reaching that target audience with the right message will also be key to success. The number one most important tool for the successful lease up of any new luxury apartment building, however, will be the strategy to create value and build momentum as the lease program progresses.

At RESIS we strongly believe you should never lease or sell the first unit until you know how you will lease or sell the last unit, and that principle will be more important now than ever for these new luxury apartments.

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