Residential Real Estate

Homebuilders turn to incentives to draw in priced-out buyer pool

In August, 31% of the nation's homes available for sale were new construction. That's more than twice the historical average, which falls in the 12% to 14% range, according to the National Association of Home Builders, underscoring how little inventory is on the market.

BYRON E. SMALL

By Ashley Fahey – Editor, The National Observer: Real Estate Edition, The Business Journals
Oct 25, 2023

Homebuilders continue to see sales momentum — despite surging mortgage rates and persistent affordability challenges — in part because they're pulling out the stops to lure buyers and ensure deals cross the finish line.

While a growing share of buyers have been locked out of the housing market because of rising mortgage rates, persistent home-price appreciation and a lack of existing-home inventory, the current environment also is creating some tailwinds for builders that can offer more competitive financing.

Housing starts increased 7% in September to a seasonally adjusted annual rate of 1.36 million units, according to the Department of Housing and Urban Development and U.S. Census Bureau data.

In fact, 31% of homes available for sale in August were new construction, compared to a historical average in the 12% to 14% range, according to the National Association of Home Builders — underscoring how little inventory is on the market right now.

Still, the association noted, higher interest rates are affecting builders' ability to move forward with their projects, as the number of single-family homes under construction in September was 674,000, about a 15% decline from a year ago.

The most recent National Association of Home Builders/Wells Fargo Housing Market Index, a monthly survey of U.S. homebuilders, found builders are using a range of incentives to lure buyers and avoid sale cancelations. The most prominent incentive is to pay closing costs or fees, which 34% of respondents said in the October survey they were currently doing.

Other popular incentives being used by builders include offering options or upgrades at no or reduced cost (32%); discounted home prices or reduced margins (31%); mortgage rate buydowns (29%); and absorbing financing points for buyers (21%).

Among the 32% of builders who said they've reduced home prices to bolster sales volume or limit cancelations, the biggest share — 38% — said they reduced prices by 6% or more.

Builders draw in new business

Some of the nation's biggest builders employing incentives are seeing their bets pay off.

Atlanta-based Pulte Group Inc. (NYSE: PHM) in its recent third-quarter earnings call said new home orders during the three months ending Sept. 30 increased 43% compared to the same period in 2022, reports the *Atlanta Business Chronicle*. Specifically, orders from first-time homebuyers increased 53% year-over-year, Bob O'Shaughnessy, the builder's chief financial officer, said during the call.

"[T]he permanent 30-year buydown is probably a most powerful incentive," said Ryan Marshall, president and CEO of Pulte, during the call. "Right now, we've got national incentives that offer 5.75% on a 30-year fixed [rate]."

He called that offer a "pretty powerful" option for buyers because of the 8% mortgage rate that's typical right now and the ability for buyers to buy a new home at a lower rate. He said Pulte is redistributing concessions that've historically been offered toward countertops and cabinets to interest-rate incentives.

At Miami-based Lennar Corp. (NYSE: LEN), executives during the company's third-quarter earnings call in September said they're using mortgage concessions in every market where the builder operates, but there are differences by region.

In Florida, the Carolinas, parts of Texas and other markets with immigration and strong job growth, concessions aren't needed as much, said Jon Jaffe, Lennar's co-president and co-CEO. But in places that've seen a bigger housing-market shift — Jaffe pointed to Austin, Texas; Boise, Idaho; and parts of California — they've had to use incentives more frequently.

"[W]e're able to achieve our desired pace by managing those levers with each individual buyer at each community, home-by-home basis, to find the right monthly payment for them to deal with their mortgage qualification issues, get them locked into a loan and to hit our production levels," Jaffe said.

Even builders that don't frequently offer rate buydowns are offering them in select cases to give buyers certainty on the cost of their home at closing amid surging mortgage rates.

At Los Angeles-based KB Home (NYSE: KBH), which reported its third-quarter earnings in late September, new orders in the third quarter grew by 7%, to 4,746 units. The average sales price of new orders in the third quarter was $456,100, an increase of 1% from the third quarter of 2022.

Within KB Home's built-to-order business, there aren't many financing concessions, said Jeff Mezger, chairman, president and CEO of KB Home, during the company's earnings call. But for what the builder calls "inventory" homes, ones farther along in the development cycle and closer to closing, they've continued to offer incentives, he said.

"[T]hat's where you fall into that situation where you typically have to offer some type of financing concessions or mortgage concessions ... to move that inventory," Mezger said.

Rob McGibney, executive vice president and chief operating officer at KB Home, estimated the builder's mortgage concessions rate was flat quarter-over-quarter, at about 1.6%.

Despite only offering incentives on a small percentage of its inventory, KB Home raised prices in 65% of its communities and decreased prices in only 10% in the third quarter, McGibney said.

"We offered mortgage concessions as needed, primarily in cases where the buyer did not qualify," he said. "Anecdotally, we hear from our teams in the field that buyers are compelled by the combination of the best price and value, not just the best interest rates."

Commercial Real Estate

Build-to-rent, single-family rental markets shift gears in unique housing market

Across the country, some 6,600 build-to-rent units delivered in the first half of 2023, 50,000 of those units are underway currently, and another 36,000 are in the planning stage, according to Yardi Matrix.

JIM POULIN | PHOENIX BUSINESS JOURNAL

By Ashley Fahey – Editor, The National Observer: Real Estate Edition, The Business Journals
Nov 1, 2023

The nation's apartment market is slowing and for-rent housing continues to be a challenge, with surging interest rates and a dearth of inventory, but current market forces could combine to create a unique opportunity for the related sectors of single-family rental and build-to-rent properties.

The Urban Land Institute has estimated that as of June 2022, large institutional investors owned 574,000 homes across the U.S., thanks in part to a buying spree during the Covid-19 pandemic. Similarly, the build-to-rent sector skyrocketed in popularity during the pandemic, with a record $2.67 billion in sales among build-to-rent communities in 2021 and $2.1 billion in 2022, according to Yardi Matrix and RSM data.

Developers within the build-to-rent space — which includes for-sale homebuilders and traditional apartment developers, among other groups — are disproportionately building them in the South, where BTR development is outpacing the next closest geography, the West, by more than 2 to 1, according to RealPage Inc.

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Gene Garcia, a real estate senior analyst and principal at RSM, said single-family rentals became particularly attractive to millennials during the pandemic, and as work-from-home and other trends have held steady, demand for those units has remained "sticky."

For many would-be homebuyers, a single-family rental home is one of the only viable options for households seeking more space. With interest rates hovering above 8% and home-price appreciation having hit record levels in recent years, the combination has locked out a lot of people from being able to afford a home.

Garcia said the build-to-rent sector in particular remains a young market, but even with a slowdown in the broader rental market, there's still a lot of demand for the units.

"The data suggests there is real need for this due to the housing crisis and the gap between ownership and rentership right now," Garcia said. "It's definitely a market that's able to take advantage of what's happening due to the decrease in home sales going on and the housing shortage."

Will SFR buyers pivot to BTR?

Despite being perhaps sturdier than other sectors right now, single-family rental investors have pulled back since their buying sprees at the height of the pandemic, when mortgage rates were ultra low.

Nationally, the market share for large institutional operators — those that own 1,000 or more homes — peaked in the second quarter of 2022, at 2.4% of all U.S. home purchases, according to John Burns Research and Consulting. In the second quarter of this year, that declined to 0.4% of all homes purchased.

For groups that've traditionally only purchased single-family rental homes, some are now pivoting to BTR homes or purchasing those properties directly from builders.

Others are actually offloading some inventory, according to John Burns Research and Consulting.

But as the housing market remains in a unique situation — and more builders are having to offer concessions to lower mortgage rates and get home sales across the finish line — there's potential opportunity for investors to purchase excess inventory from a for-sale builder, Garcia said.

"There's also a lot of cash on the sidelines waiting to find an investment to get yields they've been accustomed to," Garcia said, adding home appreciation has been significant in the past three years. "[There are] no data points to suggest there would be a big decline in home values at this point."

Dallas Tanner, president and CEO of Dallas-based Invitation Homes Inc. — one of the largest single-family rental landlords in the country — referenced this during the company's Oct. 27 third-quarter earnings call, saying Invitation "remains committed to bringing new supply to the marketplace through our extensive homebuilding relationships."

But where rental units are being bought and built is shifting, in response to robust construction pipelines in places like the Sun Belt.

Garcia said the top 10 BTR markets change on almost a daily basis, but markets like Baltimore, Pittsburgh and Philadelphia are becoming more popular. Those places didn't see the breakneck rental growth like the Sun Belt and other markets did during the pandemic, Garcia said, and therefore are still seeing modest gains today.

GROWTH & TRANSPORTATION

By Tyler Wilkins | Reporter

POINT

What's driving the build-to-rent surge

Atlanta is a top market for the asset class, buoyed by steep home prices

From outlying suburbs to far-flung exurbs, metro Atlanta is a target for large housing developments.

New communities with single-family homes and townhomes are rising along major highways. Sometimes, rows of residential units are peppered with dog parks, co-working space and other on-site amenities. But there's a key difference between many of these communities and subdivisions from the past: residents are renting the homes from the get-go instead of buying them.

Atlanta is a top market for build-to-rent, a fast-growing asset class buoyed by the dearth of attainable homeownership opportunities. Elevated home prices and steep mortgage rates have priced out would-be buyers, so much so the U.S. is now experiencing its least affordable buying market in recent history, according to real estate services firm Berkadia.

In turn, some couples and young families are trading traditional apartment buildings for rentable homes with larger footprints in suburban settings. Build-to-rent communities are also an option for empty-nesters. Limited for-sale inventory is a challenge faced by those hoping to downsize, while others prefer the maintenance-free lifestyle achieved by renting.

TWO CAPITAL PARTNERS

Two Capital Partners and RAM Partners are rolling out build-to-rent communities across the Southeast, including in metro Atlanta.

▸ BY THE NUMBERS

2,156

The number of build-to-rent units planned in the Atlanta suburbs, which only trails behind Fort Worth, Texas.

409

The number of build-to-rent units under construction in Atlanta's urban core, which represents 223.5% of existing inventory.

twilkins@bizjournals.com
404-249-1042
@tydawi

COUNTERPOINT

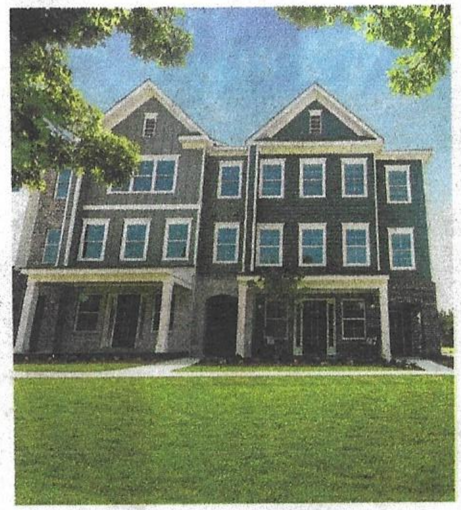
Why local leaders are pushing back

Some are soured by institutional investors who flip homes

As build-to-rent developers plop down homes in metro Atlanta, some suburban officials have blocked the efforts by rejecting rezoning requests, enacting lengthy moratoriums and adopting new regulations.

Last year, a new Stonecrest City Council ordinance restricted where rental units can be built and required developers to indicate on applications whether homes will be rented or sold.

Developers attribute the resistance to an ongoing stigma, in which renters are cast as "transients" with less of an incentive to invest in communities. Local leaders are also soured by institutional investors flipping for-sale homes



PARKLAND COMMUNITIES

into rentals, a widespread occurrence during the subprime mortgage crisis that continues to this day.

Institutional investors own 23% of single-family rentals in Atlanta, the most of any major metro area, according to Berkadia. Most of the purchases are concentrated in predominately Black communities.

Real estate pros say BTR communities are not the same as the purchase of homes en masse to rent them out.

Stonecrest crafted restrictions after Parkland Communities pitched plans for one of the largest BTR communities in the state. Residential developers anticipate a spike in housing demand as industrial jobs spread along the Interstate 20 corridor. It will be a rentable option for workers who desire a home with a private yard and garage, said Jim Jacobi, president of the firm.

"It's still the belle of the ball," Jacobi previously told the Chronicle. "Build-to-rent is here to stay … and it is going to become a bigger, necessary component of the housing stock."

▸ QUOTABLE

"We're renting to first-time homebuyers, [who] were traditionally apartment renters and now it's time to buy a house. But they can't afford to buy because interest rates make it cost-prohibitive. So, this is their next step."

BRENDA LINDNER, executive vice president and managing partner at RAM Partners, which will manage the build-to-rent units underway by Two Capital Partners.