Manufactured Housing

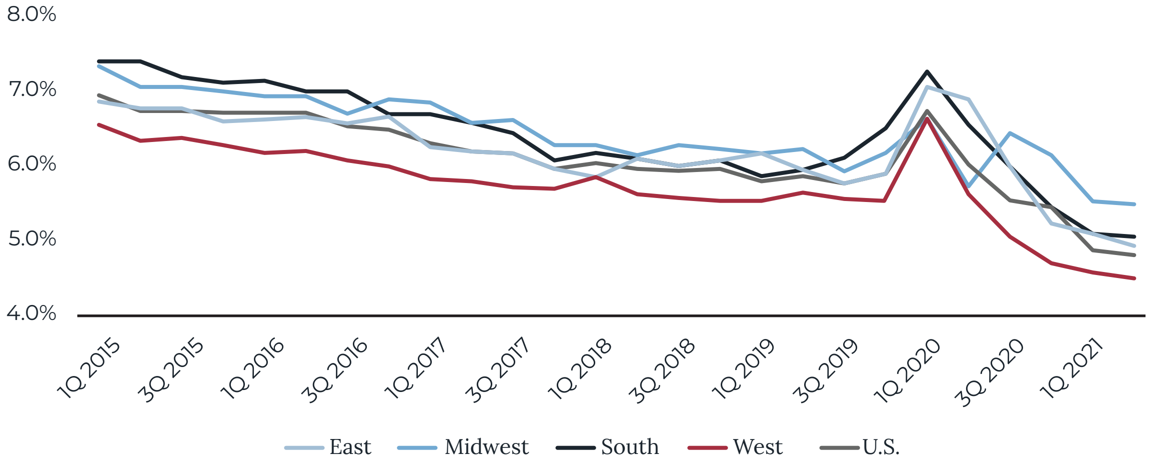
Fueled by demand for affordable housing in today's uneven economic climate, the manufactured housing sector has emerged as a strong performer in the investment sphere. The nation's current inflationary environment has encouraged many people to reassess their spending habits and search for more affordable housing options.

At an average price of $108,100 (excluding land), compared to an average price of $365,904 (excluding land) for site-built housing, manufactured housing strikes a balance for those who seek both the stability of home ownership and the affordability of factory-built housing.[1] In manufactured housing communities, residents typically own the homes themselves, but pay rent for the land they rest upon. With 22 million residents, the sector boasts more than 43,000 land-lease communities nationwide and 4.3 million lot sites.[2] However, despite the sector's designation as one of the most affordable housing options, manufactured housing residents are not immune to the economic implications of supply and demand.

SUPPLY SHORTAGES

Since its downward plunge in the immediate aftermath of the COVID-19 pandemic, the American labor market has boasted a remarkable recovery. The national unemployment rate has fallen to historically low levels, while the American workforce has risen to within 2% of its pre-pandemic high.[3] With a surplus of openings in the national job market, wages for both salaried and hourly positions have faced upward pressure. Higher incomes have translated to increased demand for residential housing and higher housing prices. The uptick in housing prices has driven many middle-income households out of the market for traditional housing opportunities and prompted them to consider manufactured housing as an affordable alternative. However, as demand has climbed within the sector, supply has struggled to keep pace. John McLaren, CEO of Sun Communities, asserts that the lack of new supply can largely be attributed to what he dubs "NIMBYism" — or a "not in my backyard" sentiment.[4] With the sector's somewhat negative public perception, many traditionally housed residents are wary of manufactured housing communities being constructed in their neighborhoods. Highlighting the extent of the supply shortage, McLaren reveals that in the last five years, Sun Communities has built only ten communities nationwide. The limited availability of manufactured housing translates to rising rents, with few states currently offering legal protections against drastic increases. Also, while the sector carries a connotation of mobility, the steep cost of transporting a home, often as much as $15,000, renders relocation infeasible for many low-income homeowners.[5] McLaren asserts that the average resident remains in their manufactured housing community for 14 years, highlighting the steady revenue streams available for capture within the sector. As manufactured housing rents continue to follow the upward trajectory of the traditional housing market, residents must decide if they will pay rising rental rates, absorb the significant costs that come with moving their home to a less expensive location, or sell their home altogether.

AVERAGE CAPITALIZATION RATE BY REGION



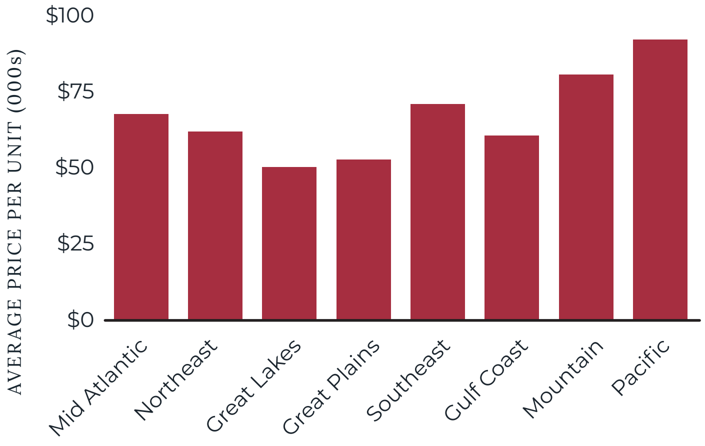
Source: JLL Research, JLL Property Intelligence Exchange (PIX)

SECTOR PERFORMANCE AND RETURNS

As rents climb and vacancy sits near historic lows, the manufactured housing industry continues to deliver strong returns to its investors. Led by Sun Communities, Equity LifeStyle Properties (ELS), and RHP properties, who collectively own over 400,000 home sites in communities nationwide, institutional capital accounted for 22% of transaction volume in 2021.[6] Total volume for the trailing four-quarters ending 3Q21 was $4.5B and as investor confidence in the sector has increased, sale prices have risen and cap rates have fallen.[7] Manufactured housing cap rates fell to 4.8% in 2Q21, a decline of 121 bps YOY.[8] While the downward trajectory of cap rates is a nationwide trend, the decline is most prominent in the West, where cap rates fell below 5% in both 1Q21 and 2Q21.[9] Inversely, since 3Q20, the Midwest has reported the highest cap rates nationally, with the average figure resting about 100 bps above all other regions.

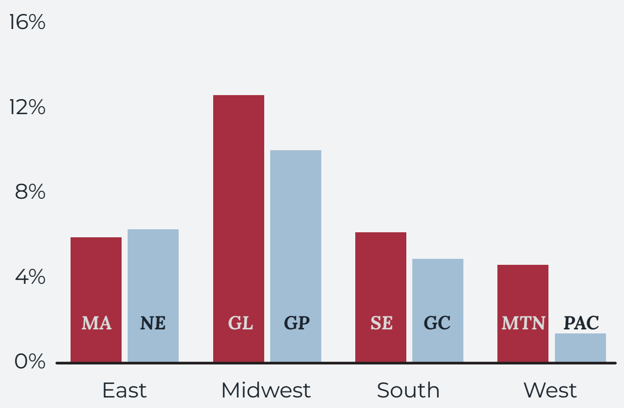
As both resident and investor demand has risen, sale prices of manufactured housing communities have followed the upward pressure, with the average manufactured home selling at $108,100 in 2021, excluding land.[10] Communities within the Great Lakes and Great Plains regions report the lowest lot rents for manufactured housing and sale prices within the region also sit below the national average.[11] In contrast to those areas, manufactured housing communities within the Pacific and Mountain regions, both located in the broader Western region, trade at much higher prices than the national average.

2021 SALES



Source: Marcus & Millichap. National Report. Manufactured Home Communities. 1H22.

2021 VACANCY RATE



Regions

East: Mid-Atlantic, Northeast

Midwest: Great Lakes, Great Plains

South: Southeast, Gulf Coast

West: Mountain, Pacific

Source: Marcus & Millichap. National Report. Manufactured Home Communities. 1H22.

VACANCY

Vacancy figures within the sector continued to decline in 2021, with multiple markets reporting drops of more than 200 bps.[12] In the Midwest, where the low cost of traditional home ownership shifts demand away from the manufactured housing sector, vacancy is highest in the nation. Inversely, at 1.3%, vacancy along the Pacific Coast is the lowest in the country. This figure can largely be attributed to the sub-1% vacancy rates in many California submarkets, including Orange County and San Diego County. On the East coast, the Miami-Dade submarket reported the lowest vacancy rate, with Florida's tax incentives and warm climate enticing new residents.

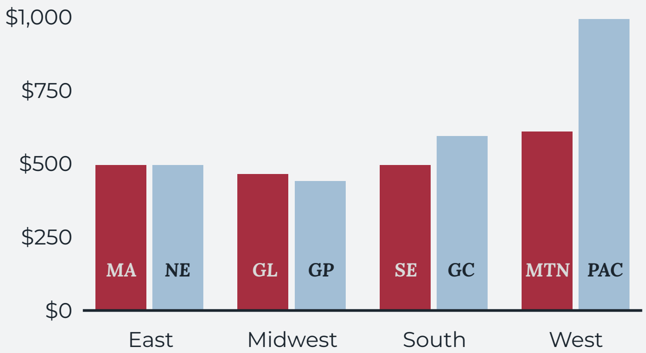
Manufactured housing is a popular choice for senior citizens, many of whom live on a fixed income. Since 2020, the number of Americans over the age of 55 has increased by nearly 3 million, representing an increase of 3%.[13] As the cost of living continues to rise, a growing number of these individuals are likely to consider purchasing manufactured homes in age-restricted communities. In communities with an age minimum of 55, the national average vacancy rate in 2021 was 3.5%, less than half the rate for non-age-restricted manufactured housing communities.[14]

The uptick in housing prices has driven many middle-income households out of the market for traditional housing opportunities and prompted them to consider manufactured housing as an affordable alternative.

RENTAL RATES AND ESCALATION

While demand and inflation push rents upward, manufactured housing is still relatively affordable. Roughly 95% of markets reported higher monthly rents in the sector in 2021 than in previous years, with the majority of markets reporting average annual rent growth below 10%.[15] In Matt Slepin's "Leading Voices in Real Estate" podcast, Sun Communities CEO John McLaren stated that the weighted average rent escalation figure for the REIT's portfolio through the first half of 2022 was 4.2%.[16] In contrast, average monthly rents within the traditional multifamily sector climbed 15.5% in 2021.[17] In 2021, average rents within manufactured housing communities across the country ranged between $457 to $840 in the Midwest and West, respectively. As depicted in the accompanying table, the Great Plains region offers the lowest rental rates for manufactured housing in the nation, with an average monthly rent of $439. Ranking just below in affordability, the Great Lakes and Gulf Coast subregions boast average monthly rents of $460 and $488. Meanwhile, on the other end of the spectrum, residents pay an average of $981 per month to station their houses within the Pacific region. In terms of rent growth, Charlotte, NC led the country with an average of 15% YOY, while communities in Tulsa, Greenville, and Port Huron saw rental rates escalate by 14% YOY.[18]

2021 AVERAGE RENT



Regions

East: Mid-Atlantic, Northeast

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Source: Marcus & Millichap. National Report. Manufactured Home Communities. 1H22.

ETHICAL AND REPUTATIONAL CONCERNS

While the manufactured housing sector has proven itself to be a strong performer for investment returns, some media outlets have remarked that there can be ethical considerations in the space. For example, a recent Washington Post article commented on residents' fears of losing their homes due to large rent increases.[19] Of the manufactured housing community members interviewed by The Washington Post, the majority reported that their rents had increased by 10-25% in the last year, while some claimed that their monthly rent had doubled or tripled in the same timeframe.[20] With the lack of regulations in place to protect residents in manufactured housing communities, some argue that private equity investors are taking advantage of strong resident demand for these properties to increase lot rents to unreasonable levels. The ability to substantially escalate rents without providing additional value to a tenant can raise ethical considerations. While fulfilling their obligations as fiduciaries, manufactured housing investors should also strive to adhere to core ESG principles by being cognizant of ethical concerns related to their investments and by thoughtfully addressing these concerns as they make business decisions.

ENDNOTES

1 *Manufactured Housing Institute. (2022). 2022 Manufactured Housing Facts. Industry Overview. August 2022.*
2 *Manufactured Housing Institute. (2022). 2022 Manufactured Housing Facts. Industry Overview. August 2022.*
3 *Marcus & Millichap. (2022). Manufactured Home Communities. National Report. 1H22.*
4 *Slepin, Matt. "John McLaren | President & COO Sun Communities." Leading Voices in Real Estate Podcast. June 20, 2022. www.applepodcasts.com.*
5 *Bhattarai, Abha. "'We're all afraid': Massive rent increases hit mobile homes." The Washington Post. June 6, 2022.*
6 *JLL. (2021). Manufactured Housing Communities. Market Trends and Valuation Index Report.*
7 *JLL. (2021). Manufactured Housing Communities. Market Trends and Valuation Index Report.*
8 *JLL. (2021). Manufactured Housing Communities. Market Trends and Valuation Index Report.*
9 *JLL. (2021). Manufactured Housing Communities. Market Trends and Valuation Index Report.*
10 *Manufactured Housing Institute. (2022). 2022 Manufactured Housing Facts. Industry Overview. August 2022.*
11 *Marcus & Millichap. (2022). Manufactured Home Communities. National Report. 1H22.*
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13 *Marcus & Millichap. (2022). Manufactured Home Communities. National Report. 1H22.*
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16 *Slepin, Matt. "John McLaren | President & COO Sun Communities." Leading Voices in Real Estate Podcast. June 20, 2022. www.applepodcasts.com.*
17 *Marcus & Millichap. (2022). Manufactured Home Communities. National Report. 1H22.*
18 *Marcus & Millichap. (2022). Manufactured Home Communities. National Report. 1H22.*
19 *Bhattarai, Abha. "'We're all afraid': Massive rent increases hit mobile homes." The Washington Post. June 6, 2022.*
20 *Bhattarai, Abha. "'We're all afraid': Massive rent increases hit mobile homes." The Washington Post. June 6, 2022.*

FOR ADDITIONAL INFORMATION

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