NATIONAL APARTMENT ASSOCIATION
We Lead the Way Home

Mass Appeal

By Barbara Ballinger |
November 27, 2023 |
Updated November 28, 2023

Secondary and tertiary markets attract multifamily housing development for affordability, job opportunities, amenities, space and easy living.

If the pandemic and recovery have taught any lessons about what constitutes an appealing multifamily housing location, it’s that there’s no single answer.

Being in the heart of a downtown metro used to represent the epitome of convenience and cachet and led to high occupancy rates, although land and labor in such markets was costly.

The trend of building outside these primary markets didn't begin with the pandemic, but the pandemic triggered more construction as many exited crowded urban cores when employers permitted remote work, followed by hybrid solutions. Renters headed to secondary and farther out tertiary market locations. Developers quickly recognized the opportunity to buy more readily available, affordable land on sites where they could build from the ground up or rehab existing structures and sometimes adapt vacant industrial and commercial spaces.

From our firm's prior work in second tier gateway cities, we had experienced the advantages of outlying markets, such as less bureaucracy to comply with zoning codes, which can be onerous in primary markets," says architect Tom Schultz, AIA, Associate with Boston-area-based The Architectural Team (TAT). In downtown Boston, projects can take anywhere from three to eight years to get off the ground versus in markets northwest of Boston like in Chelmsford, or in Revere just six miles from Boston, where it takes less time – even half as long.

Architects and developers have also found they can build more economically in smaller markets where instead of high-rises they construct low- and mid-rise wood-framed structures, buildings atop podiums or wrapped around garages, walk-ups and garden-style horizontal designs.

To retain residents who might resent long commutes over time or miss city life, developers and managers have also learned what residents care about most, as well as how they can achieve the best financial results. Though land and building costs are less than in primary markets, they're increasing. Rents they can charge are also less, says Levi Kelman, CEO of Clifton, N.J.-based Blue Onyx Properties, which has long focused on attainable market-rate secondary and tertiary New Jersey sites.

Kelman has also seen changes as these outlying markets grow. Over time, some become too expensive for those who relocated, the case now in Jersey City, which last year was cited as having the highest rent in the country at an average of $5,500 a month, according to the New Jersey Digest. This year, according to news outlet PIX11, it slipped to second, tied with San Francisco, following New York City, but its still-high rents pushed some to move to less expensive Harrison, Weehawken and Bloomfield, N.J., Kelman says.

Here's what developers are doing to make secondary and tertiary markets a strong alternative, particularly to meet work-life-play objectives, Schultz says.

Most expect the trend will continue, though probably at a slower pace as migration slows, supply increases and employers mandate more frequent returns to offices, says Adam Rosenkranz, CIO with Christina, which is focused on exclusive submarkets like Beverly Hills and West Hollywood on Los Angeles' West Side.

Location

The key criteria that make outer market locations appeal are a growing population, healthy job market, low taxes, strong infrastructure with retail, restaurants, medical care and technology and mass transit. The variety of locations and their different demographics has led to slight differences, including how far they are from a primary market. Most residents still want easy access and not to be on a train, bus or subway for too long. Kelman prefers locations with public transport options that can get residents to Manhattan in under an hour such as East Orange, N.J., and where rent is half the cost of the average Jersey City or New York City building. He also favors regions that have fairly developed infrastructure, including a robust commercial/office corridor, rather than waiting for facilities to move in after residents arrive.

Doug Faron, Managing Partner at WestPalm Beach, Fla.'s Shoreham Capital, concurs with that approach as it develops apartment communities, single-family rentals and build-to-rent communities in the Sun Belt. Jay Remillard, Managing Director of New York City-based CP Capital US, also focuses on smaller markets with their own infrastructure. "We don't want residents in Des Plaines, Ill., to have to rely on Chicago or those in Covington, Ga., to have to go regularly to Atlanta. A lot of these suburban markets mimic an urban feel," he says. Yet, his firm still wants locations to be no more than 20 miles or so, if possible.

Mark Alexander, President and Principal of Alexander Development, has also focused on secondary markets, but in New York's suburban Westchester County such as White Plains, N.Y., and tertiary markets a bit beyond like Tuckahoe and Tarrytown. He favors locations no more than 35 minutes by train to Manhattan. Unlike Kelman, whose properties are Class B and C categories, Alexander builds Class A to attract affluent Millennials and empty nesters—who want the feeling of a Manhattan building but without congestion. In such sites, he can build for as much as $100 less per square foot than in New York, in part because they're often stick atop podium construction, and charges rents generally $10 to $20 less a square foot than newer properties in New York City.

The Southeast has also become a popular destination for developers pursuing this strategy. The Beach Co., headquartered in Charleston, S.C., has recognized the value that smaller markets can offer, says Alan McMahon, Senior Development Manager. Since the company's founding in 1945, it has grown along with Charleston, but has also expanded into more than 25 other cities in six other Southeastern states. Doing so has given it strong brand recognition and fewer competitors than it might have in larger markets. While it focuses on Class A, it also buys B and C assets and adds value. In Wilmington, N.C., it chose a suburban infill site to build a multifamily property that's part of a lifestyle center with hotel, 100,000-square-feet of retail and nearby mass transit.

Also in the Southeast, developer Jeff Klotz, CEO of Jacksonville, Fla.-based The Klotz Group of Companies, picks sites in cities with a population of between 250,000 and 2 million where housing costs have put them out of the reach of many, who instead want to rent in highly amenitized Class A buildings for quality of life, he says. Sites that appealed are in Florida's Pensacola, Panama City and Santa Rosa Beach, Alabama's Huntsville and Georgia's St. Marys. So far, Klotz hasn't seen migration back to bigger cities but has heard the challenge is to make money remotely and in the gig economy.

Not everyone is going after mimicking big city high-rises on a smaller scale. Joe Morrison, CEO of Myrtle Beach, S.C.-based Sands Companies, favors sites about 15 minutes from secondary and tertiary centers where there's land to construct 250 to 325 of its build-to-rent detached, single-family homes and clubhouses with land left for outdoor activities. "We don't want anyone to feel isolated, but we also don't want residents dealing with congestion," he says. Examples are its Argent Cottage Apartment Homes near Savannah, Ga., and Cape Cottages in Leland, N.C., near Wilmington.

And sometimes, secondary or tertiary markets may be almost in a major market's backyard. That's the case with Miami-based The Astor Companies' choice of where it constructs its attainable multifamily buildings. While downtown Miami demands higher rents, right beyond has offered opportunity to construct the Douglas Enclave near a casino that was refurbished and is attracting growth and also near mass transportation to downtown. Ten blocks away in what CEO Henry Torres describes as a tertiary market, his company is building its Flagler Enclave 1 and 2 workforce housing. It's begun to look farther on the state's West Coast where population is growing, insurance costs are half the price and rents are a quarter of those on the East Coast.

Amenities

For many developers, amenity choices help curate a sense of community, key for those who relocate, especially from a bustling city, Kelman says. Due to availability of more land in many cases, outdoor and indoor space may be larger than in primary markets, depending on budget and price. In many of Kelman's affordable buildings, he includes a fitness center, lounge, workspace and pet wash but no swimming pool. His firm also makes buildings service oriented by offering free Friday morning coffee at locations where residents are interested in community engagement initiatives.

Morrison's communities include enough land for resort features like bocce ball, firepits, grilling stations, volleyball and walking and bicycle trails. The company offers free bicycles to borrow. But the biggest perk, he says, is that the detached style of its units means nobody's living above or next door since noise is the biggest resident complaint, he says. The apartment homes also have private porches.

Schultz agrees about the importance of noise containment and says TAT designs spaces to mitigate noise and adds sound absorption materials to soundproof units and workstations. "Nobody wants to conduct a conference call with a noisy dog in the next apartment," he says. His firm also strategically programs outdoor pools in optimal spaces so that in colder climates residents aren't looking at an unattractive cover for nine months of the year. "We design so that the pool is a backdrop rather than primary view," he says

To conserve space and allow for flexibility, TAT architects and interior designers create zones that are multifunctional by having an area serve as a coffee-croissant gathering spot in the morning, then a pizza-beer hub at night, or by situating a leasing office out in the open so that tables and chairs can be used for other functions, too, he says. Amenities outside a building, which are part of the neighborhood's existing fabric also work as resident amenities such as breweries in Everett, Mass., where his firm is working on 35 Garvey Street, led by Greystar, and a multifamily community Artemas, led by LMC; each adjacent to a brewery.

For Klotz's communities, there's an emphasis on community gardens and outdoor exercise places to stay fit, as well as lots of programmed classes to enjoy wine, music and art. Experts also come to the properties to perform services such as trimming residents' hair and grooming pets. Some properties may have fewer amenities than comparable big city sites because they have fewer units to amortize the cost, Klotz says. In his tertiary markets, there may be 50 to 125 units, and a small gym but no clubhouse or staff. In contrast, his larger communities in secondary markets try to keep up with the Joneses in primary markets. “We all shop each other’s buildings to compare,” he says. To compete, some may offer a busy street scene on the ground floor with coffee shop and organic food store, mail and package rooms for more interaction and lots of community programs. “Vibrancy is the secret sauce that provides magic,” he says.

And even with Astor’s more modest buildings, room is set aside for amenities. “They’re greatly appreciated since many of our competitors don’t include any. We usually have a pool and gym, with at least 15 machines while many competitors only have perhaps three,” Torres says.

Sustainability surge

The growing interest in sustainability has made it the equivalent of a sought-after amenity, Schultz says. Residents want to feel they’re doing good by prioritizing living in a sustainable environment, in response, more buildings are seeking LEED or Fitwel certifications, he says. “Today’s residents are increasingly eco-conscious and well versed in the latest green design strategies. They look for everything from Energy Star-rated appliances and water efficient or low-flow fixtures to occupancy sensors that control lighting and energy-efficient windows and solar panels and shades,” he says. Especially post-pandemic, they consider indoor air quality important with low- or no-VOC paints and upcycled materials. Buildings feature additional recycling areas for a range of products and regularly scheduled pickups for donated items. EV charging stations and bicycle storage are the norm.

Configuration and size

Apartment unit sizes vary depending on the site and economics of construction costs and rents desired. Kelman’s buildings typically include mostly one-bedrooms since more residents favor them over studios for room to work. But he also includes studios and two bedrooms. Morrison’s detached apartment homes include one, two and three bedrooms on one or two levels. Klotz is finding that more residents opt for two bedrooms to use one as an office but want just one bathroom for a lower rent. Faron’s Shoreham Capital’s Siesta Lakes in Cape Coral, Fla., will feature 412 units with one, two or three bedrooms and each with a private balcony, open-concept plan and high-end finishes. Construction is slated to begin later this year.

What's the investment strategy?

Smaller markets are the ones that registered the best investment growth over the last year out of 150 markets studied, according to RealPage. At the top of the list was Midland/Odessa, Texas, with more than $125 million in apartment transactions and a 2,672% increase year-over-year (YoY) due to its energy-centric economy. Number two was Salisbury, Md., close to Washington, D.C., and Baltimore with a 609% growth YoY and $58.5 million of apartment deals transacted. For now, these outlying markets are experiencing great demand with strong occupancy rates in the mid-90s, even as rents increase. The key, Jay Remillard, Managing Director of New York City-based CP Capital US says, is to recognize when a market is overbuilt and doesn't hit the desired rent velocity. "We don't want to be the 18th development when only 17 were needed," he says. —B.B.

What's the difference between primary, secondary and tertiary markets?

Definitions vary but at The Katalyst Team, based in Des Moines, Iowa, it defines a primary real estate market as the largest housing markets in the country with dense population centers with long-established commerce and industry such as New York, Los Angeles, Chicago, Miami and Seattle. The firm defines a secondary market as slightly smaller cities with populations between 1 and 5 million with slightly less economic activity but growing in both residents and business such as Denver, Las Vegas, Minneapolis and Austin. It next defines a tertiary market as a still smaller location with fewer amenities and a growing population but one under 1 million such as Kansas City, Charleston and Nashville. According to InvestNext, secondary markets are growing due to their affordability and job opportunities for younger demographics, and tertiary markets have less industry and people and their lines with suburban areas may blur at times. Because they also have less infrastructure and development, some developers may view investment in them as riskier. —B.B.

Barbara Ballinger is a frequent contributor to units.