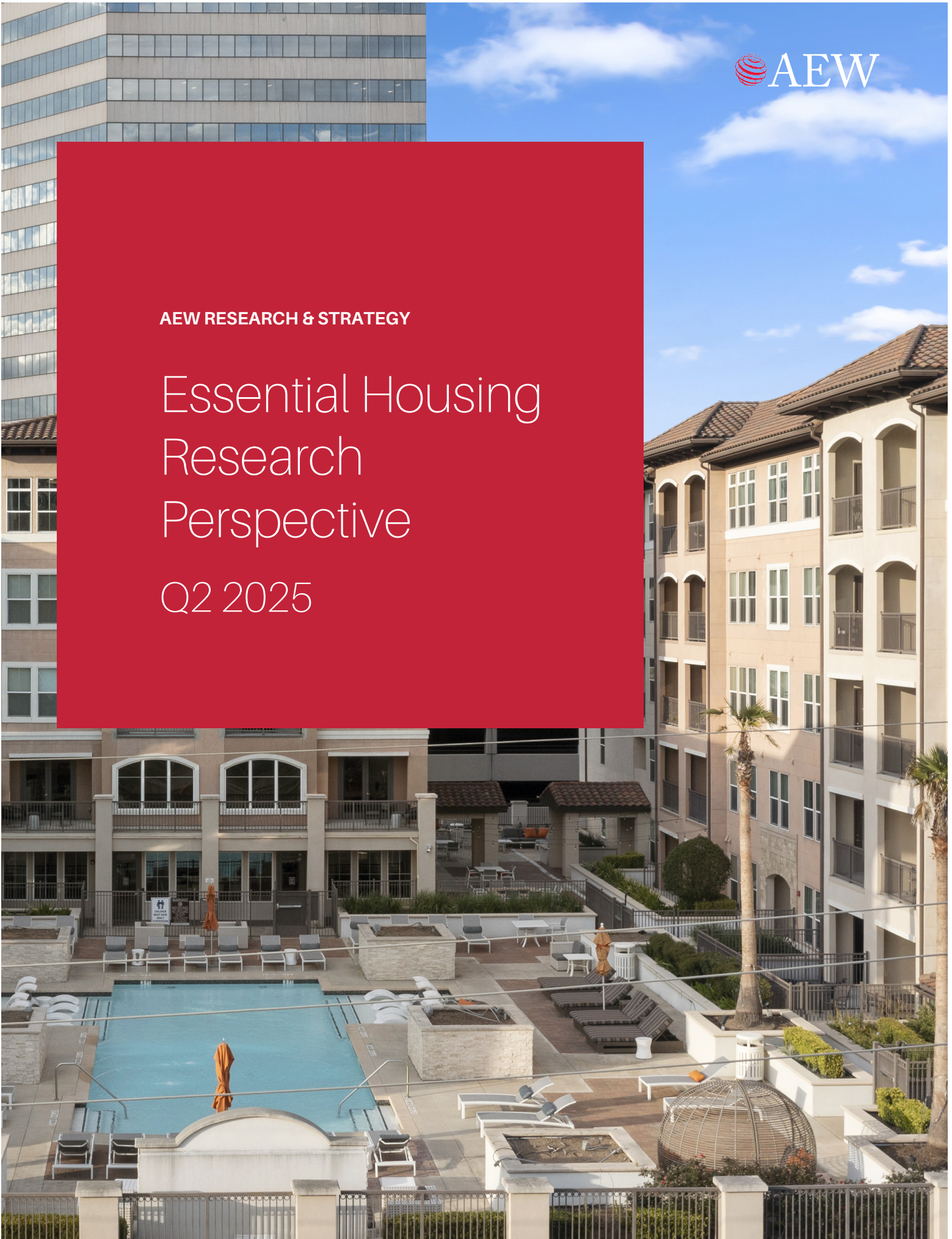


**AEW RESEARCH & STRATEGY**

# Essential Housing Research Perspective

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# Essential Housing

The 90+ days stretching from April 2<sup>nd</sup> Liberation Day through the July 4<sup>th</sup> signing of the One Big Beautiful Bill (OB BB) represents one of the most consequential periods of federal government policy change in many years. When taken together, these policy changes are, at best, mixed and in some ways negative for both future essential housing development and the financial wellbeing of essential housing renters.

With respect to supply, various OB BB provisions are designed to encourage more investment in affordable housing through expansion of various aspects of low-income housing tax credits (LIHTC), more predictable funding of new market tax credits (NMTC), and enhancements to the opportunity zone programs introduced in the 2017 precursor to the OB BB. The OB BB also restores 100% bonus depreciation for furniture, fixtures, equipment, and landscaping in LIHTC and other projects.

**TABLE 1**  
**OB BB PROVISIONS LIKELY IMPACTING AFFORDABLE HOUSING DEVELOPMENT**

Permanent 12% increase in each state's annual allocation of 9% LIHTCs.
Lower bond financing threshold for 4% credits, with the "50% test" for private activity bond financing permanently reduced to 25%.
Expanded GSE investment cap, Fannie Mae and Freddie Mac can now each invest up to \$2 billion annually in LIHTC properties (up from \$1 billion), totaling \$4 billion per year.
Permanent extension of the New Markets Tax Credit (NMTC), with \$5 billion annual allocation authority.
Permanent extension of the OZ Program, with rolling 10-year new OZ census tracts.
Census tracts must now meet tighter definitions of "low-income community," with poverty rate $\geq 20\%$ and median household income $\leq 125\%$ of statewide or metro median income.
Capital gains invested in Qualified Opportunity Funds (QOFs) can now be deferred for 5 years from the investment date with investors receiving 10% basis step-up after 5 years and 30% step-up for investments in rural OZs.

Source: Novogradac

At the same time, however, significant changes to existing tariff rates on products and countries introduce potentially higher and more variable future costs for a wide range of building materials, appliances, furniture and fixtures, making the overall impact on all future development, including affordable housing, less clear.

In terms of demand and renter household financial wellbeing, particularly for below median income households, the impacts of tariffs and the OB BB are mixed at best and negative in some specific dimensions. Most significantly, tariffs are a tax on consumption and the current average effective tariff rate of nearly 20% represents one of the largest consumption tax increases in U.S. history. The Budget Lab at Yale estimates this new tariff rate will increase the average cost of goods currently purchased by U.S. households by approximately \$2,400 per year, an amount that many households, particularly below median income households simply cannot absorb into existing budgets. Historically, federal tax policy generally eschewed consumption-based tax schemes as regressive, disproportionately impacting lower income households, particularly with respect to non-discretionary items such as food and clothing.

With respect to the OB BB, most households will see modest tax relief, primarily through an increase of \$750 in the standard deduction for single filers (\$1,500 for married filing jointly) and the increase in the child tax credit from \$2,000 to \$2,200<sup>1</sup>.

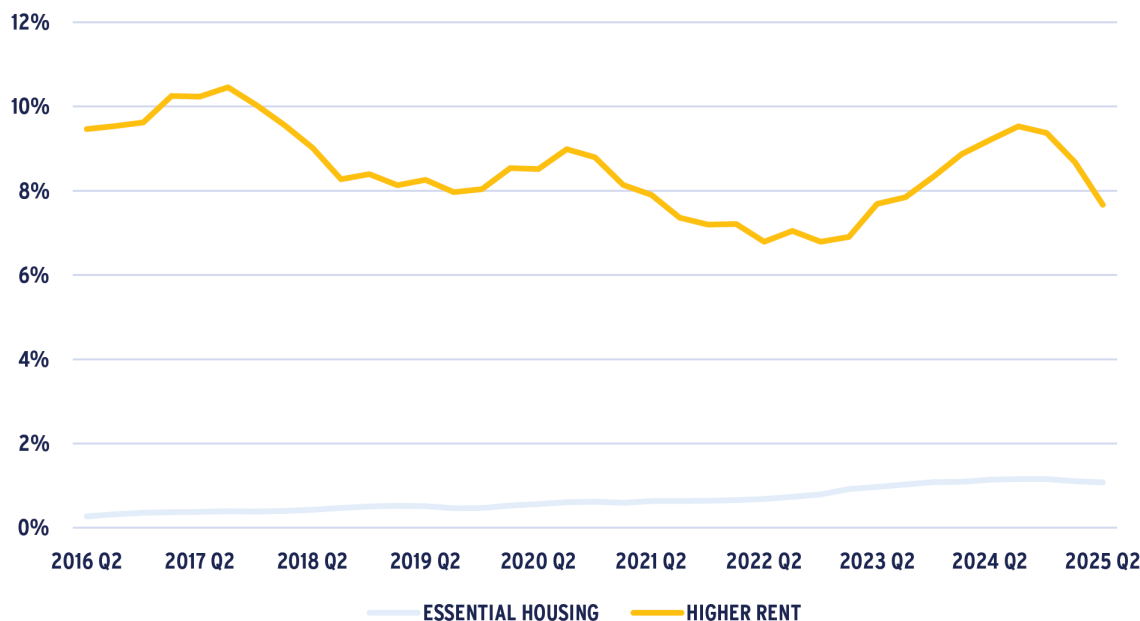
<sup>1</sup> Note, the refundable portion of the child tax credit remains capped at \$1,700 thereby capping the benefit to families with little or no federal tax liability.



Additionally, some households will benefit from limited tax relief for tipped income and overtime pay, though currently these benefits are not expected to be realized until households file for and receive tax rebates next year. Importantly, the newly created tax relief for tip income, overtime and the new special deduction for seniors all expire at the end of 2028 unless extended by the next administration<sup>2</sup>. Overall, the Tax Policy Center estimates that 70% of American households will experience no additional tax cut benefit after the end of the 2028 tax year. For the essential housing renter, the Tax Policy Center also projects limited after-tax income gains for the median income (and below) household, approximately \$1,000 for households earning between \$50,000 and \$75,000. Overall, any after tax-income gains for below median income households is likely to be more than offset by higher costs of goods related to new tariffs.

Future tariffs and OBBB impacts aside, assessment of the status and direction of the current U.S. apartment market remains complicated. Data from CBRE-EA continues to show steady improvement in the overall vacancy rate, but CBRE-EA includes very few non-stabilized properties (i.e., properties still in lease up). Using data from CoStar, the total vacancy rate for higher rent units modestly improved over the first half of 2025 but remains high by historical standards at slightly more than 11%. When the higher rent segment is adjusted to exclude properties that are not yet stabilized, the vacancy profile reverts to levels much closer to the typical vacancy of essential units<sup>3</sup>. For essential units, the differences between the vacancy rate for stabilized properties and properties that are not yet stabilized are quite small, largely because there are typically much fewer new units delivered within the essential segment of the market, despite it representing a much larger share of total stock. To this point, Figure 1 illustrates the year-over-year growth in rental stock over the past decade. While the new supply (growth in stock) is slowing in the higher rent segment, it remains multiples above the long observed lower growth rate of the essential stock.

**FIGURE 1**  
**YEAR-OVER-YEAR GROWTH IN RENTAL STOCK**



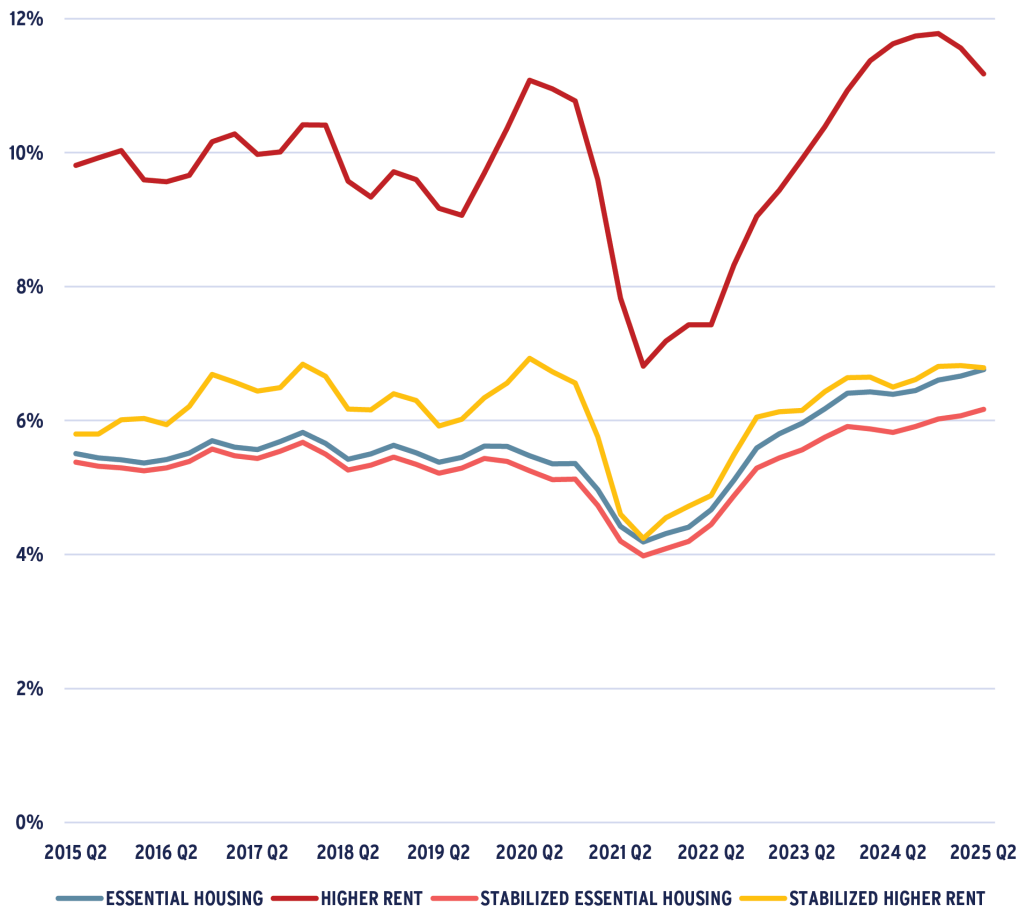
Source: CoStar, AEW Research

<sup>2</sup> Other new tax cuts that also expire at the end of the 2028 tax year include the newly increase SALT deduction and the deduction for interest expense on newly purchased American produced automobiles.

<sup>3</sup> For the various exhibits included, Essential Housing is defined as the inventory weighted average aggregate for the various “star rating” segments calculated by CoStar. Specifically, essential housing here is defined as the weighted average of 1-star, 2-star and 3-star apartment units. Higher rents units are similarly calculated for 4-star and 5-star units.



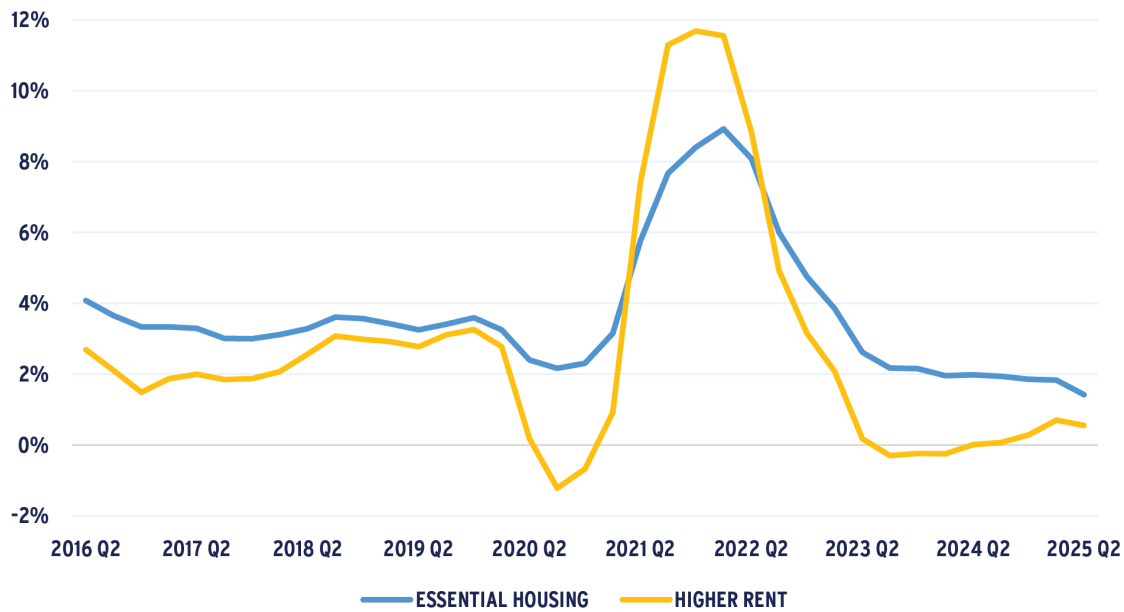
**FIGURE 2**  
**APARTMENT VACANCY RATE**



Source: CoStar, AEW Research

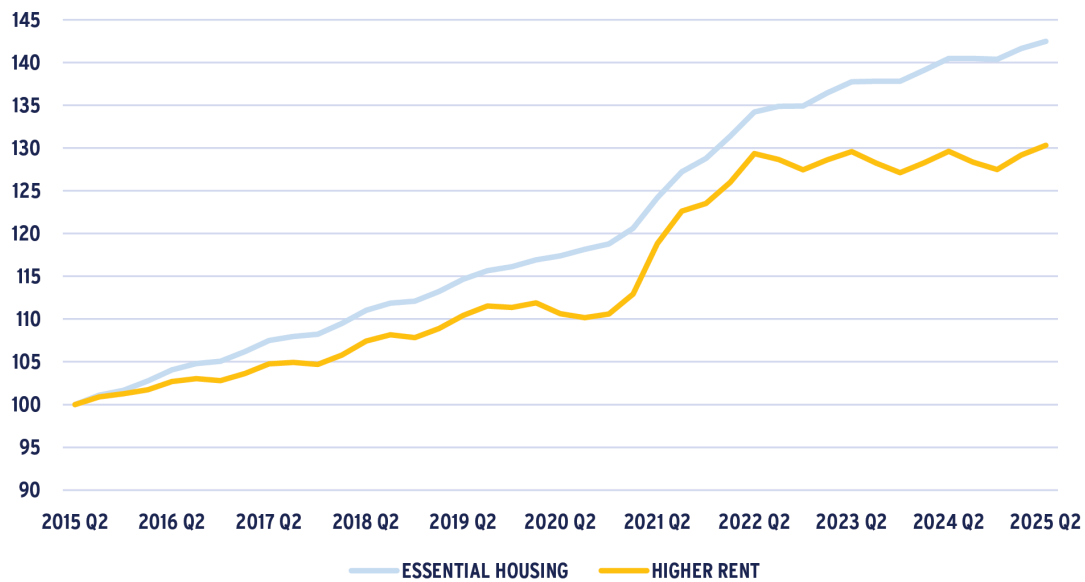
Reflecting the differences in overall vacancy, the slowdown in effective rent growth within the higher rent segment has been more pronounced than in the essential segment. On a year-over-year basis, rent growth in the higher rent segment moved into positive territory over the first half of this year while the essential segment has seen a slight deceleration from the stable 2% range of the past two years. When we examine the compounded impacts of the differences in rent growth we find, on average, 11% higher rent gain in essential housing over the past ten years, slightly more than one hundred basis points per year (4.8% CAGR vs 3.8%).

**FIGURE 3**  
**YEAR-OVER-YEAR RENT GROWTH**



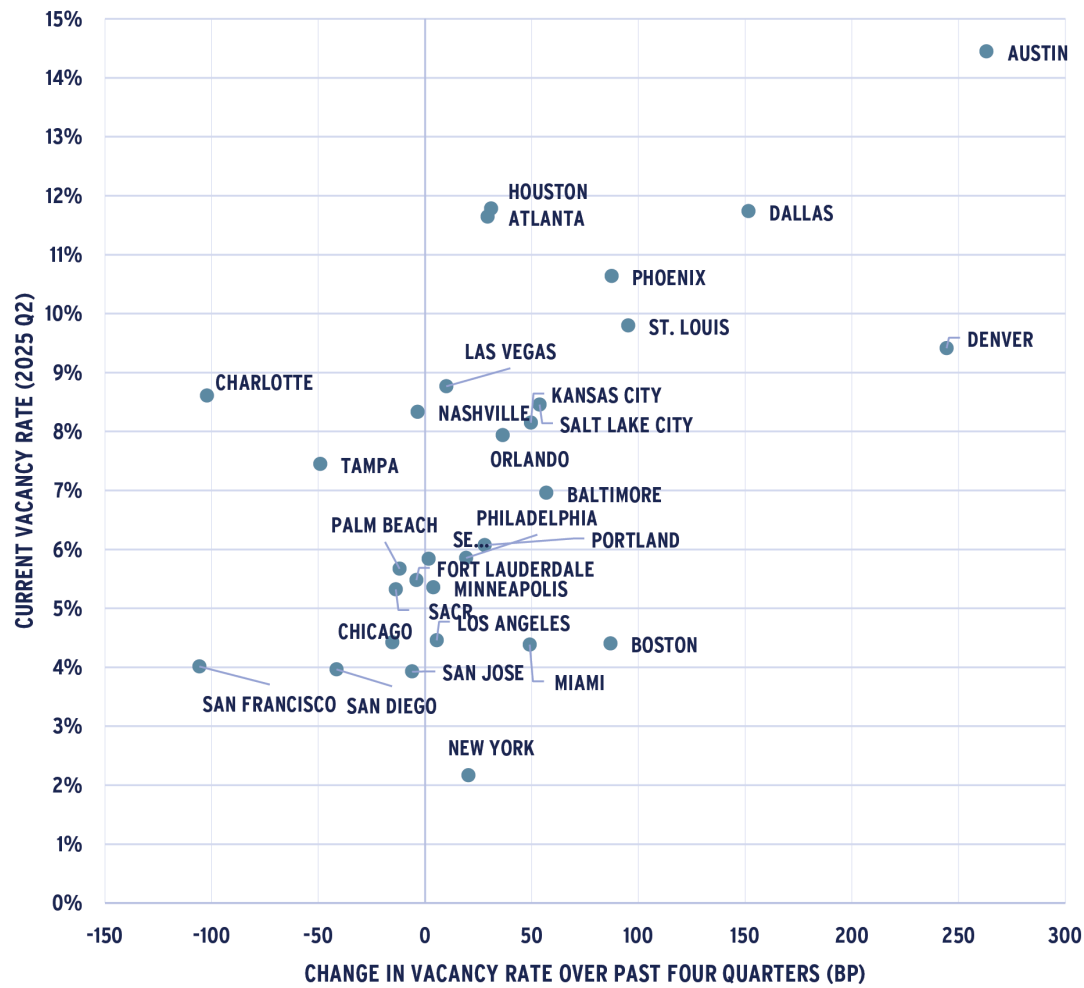
Source: CoStar, AEW Research

**FIGURE 4**  
**AVERAGE EFFECTIVE RENT INDEX, 2015 Q1 = 100**



Source: CoStar, AEW Research

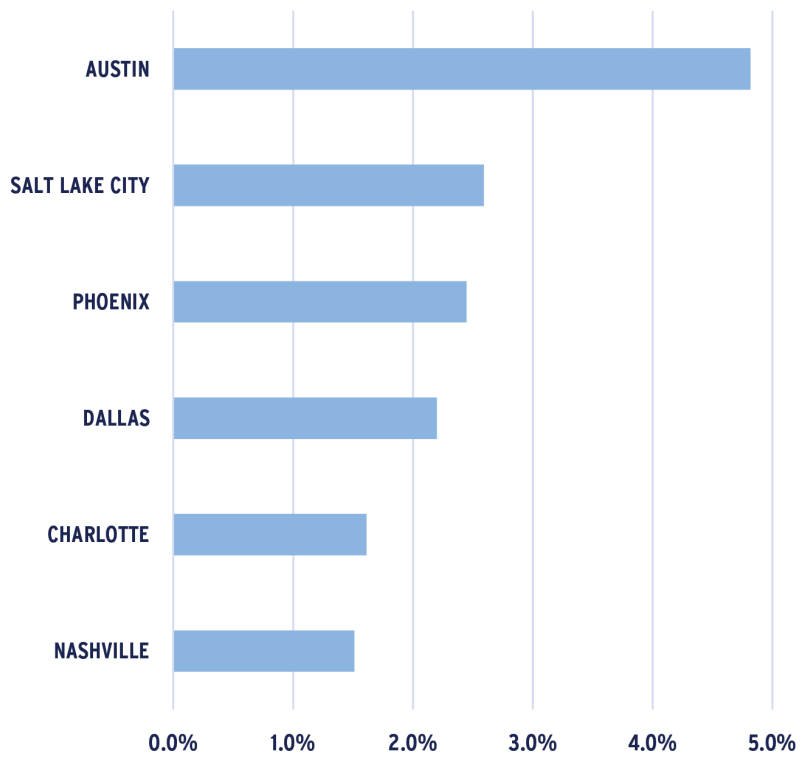
**FIGURE 5**  
**CURRENT ESSENTIAL HOUSING VACANCY RATE AND CHANGE OVER PAST FOUR QUARTERS**



Source: CoStar, AEW Research, 2025 Q2



**FIGURE 6**  
**YEAR-OVER-YEAR GROWTH IN ESSENTIAL HOUSING INVENTORY**



Source: CoStar, AEW Research 2025Q2