UBS

Global Research

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Powered by UBS Evidence Lab

UBS Evidence Lab: US Housing Intentions

From "Doubled Up" to "Singled Out": Survey Supports Increased Household Formation

Equities

Americas
Real Estate

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Second wave of survey supports above consensus housing starts forecast

As a follow up to our inaugural survey, Who's Moving On Up & Out?, UBS's Economics, Homebuilding & Building Products, Multifamily REITs, and Hardline Retail teams collaborated with UBS Evidence Lab in a survey of US consumers to better understand their intentions regarding their housing situation in the near term and further out. From a macro perspective, our Chief US Economist is encouraged by the substantial portion of respondents (just over half) that are currently "doubled up" but citing plans to buy or rent a home in the next year. This is in line with the improvement in household formation in 4Q14, a trend he expects will continue this year. Moreover, it supports his 2015 estimate for total housing starts at 1.25mn, ahead of consensus at 1.16mn.

Multifamily REITs will continue to benefit as doubled-up households separate

Survey results show an increase in pent-up rental demand from doubled-up millennials. While some of this could be due to seasonal factors, 52% in wave 2 vs. 40% in wave 1 said they hope to rent in the next 12 months. Financial constraints remain the predominant reason why young people are doubled-up, with only 33% employed full time. As job and wage growth improves, we expect rental demand to be unlocked further in 2015, benefitting Multifamily REITs. AVB, EQR, and AIV are our top picks.

Financial constraints continue to inhibit the pace of housing recovery

Reflecting millennials' positive outlook on housing, we found those who plan to buy a home in the next year financed with a mortgage, have saved an ~11% down payment on average. Although stringent underwriting remains an issue among this cohort, as this eases, we look for increased home ownership among them. We highlight top pick PHM.

HD and LOW remain poised to benefit from home improvement spending

Notably, a greater percentage of homeowners surveyed plan to do a HI project in the next 3 months (53% vs 47% prior), which should benefit HD & LOW. Approx. 40% expect to purchase materials from HD & 26% from LOW. Homeowners with properties valued $400k+ favored HD over LOW. Interestingly, 5% of homeowners indicated they would buy most of their materials for DIY projects from AMZN, ahead of WMT at 4%.

Contents

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** **UBS Evidence Lab** provides our research analysts with rigorous primary research. The team conducts representative surveys of key sector decision-makers, mines the Internet, systematically collects observable data, and pulls information from other innovative sources. They apply a variety of advanced analytic techniques to derive insights from the data collected. This valuable resource supplies UBS analysts with differentiated information to support their forecasts and recommendations—in turn enhancing our ability to serve the needs of our clients.*

For this report, UBS Evidence Lab conducted surveys of US consumers to better understand their intentions to buy, rent, or sell a home in the coming year as well as the drivers of those decisions. To better understand how intentions and motivations vary among different key demographic segments, the survey was simultaneously conducted among a large representative sample of over 2,000 adults who speak English.

UBS Housing Intentions Survey

Executive Summary

Report overview. Since the housing recovery took hold in 2011-12, factors contributing to its unevenness have been much discussed. To gain understanding of the longer-term pace and path of improvement, we believe the bigger questions should focus on the demand side of the equation. This is especially evident when looking at: 1) the lack of participation among entry-level homebuyers; 2) the muted increase in the formation of new households; and 3) the decline in the homeownership rate to 64% in 4Q14 from a peak of approximately 69% in 2006. This report seeks to better understand the attitudes and mind-sets of current and potential homebuyers, apartment renters, and consumers of housing-related building products.

This is a follow up to our inaugural survey, Who's Moving On Up & Out? Despite the numerous macro related and geopolitical events that have been in the headlines since our first iteration (declining oil prices, tensions in the Middle East), we found respondents continue to have an optimistic outlook regarding their housing situation. This is reflected in the substantial portion of those surveyed who are currently "doubled up" (44% in the 1st and 55% in the 2nd survey) that cite plans to buy or rent a home in the next 12 months. As we detail in this report, these findings have implications for homebuilders, multifamily REITs and hardline retailers. Therefore, we strive to provide greater insights from several industry and sector perspectives.

More to come. We will repeat this survey on a quarterly basis over time, keeping the questions consistent to gain valuable insights to changes in thoughts and attitudes surrounding homeownership and the homebuying process. In our view, the time series will allow us to better understand the path of housing and related demand trends. Further, as that these decisions are largely influenced by life changes (ie, marriage, children), financial situations, and economic outlooks, we will aim to decipher the psyche of those surveyed to understand the changing roles these factors play in their decision-making process.

Whom Did We Survey?

The views considered in this report are based on a survey of 2,090 adults age 21 and older that was commissioned by UBS Evidence Lab. The survey was conducted between February 2-17, 2015, utilizing a questionnaire covering a range of topics such as respondents' household characteristics, financial situation, and attitudes and thoughts towards their current housing and ability to change it.

Our sample reflects a cross-section of the US population with respondents from different regions and a variety of economic statuses and demographic profiles. Since our survey was conducted online, it is true that there is a bias in our sample, as it does not capture those who are less likely to use the web for reasons such as access, interest, or understanding. Nonetheless, it should provide a useful picture of the thoughts and attitudes of current and potential homeowners.

For further details regarding our survey methodology, see page 46.

Key Takeaways

We highlight the following high-level takeaways from our study regarding respondents' intentions around housing:

- **Second UBS survey suggests less "doubling up".** From a macro perspective, our Chief US Economist is encouraged by the improving trends in household formations. Given a substantial portion of those surveyed (44% in the 1st and 55% in the 2nd survey) citing plans to buy or rent in the next 12 months, these results suggest that moving out of doubled up residences could be considerable and have an important economic impact over time.

- **Financial constraints will limit the pace of improvement in housing.** Overall, respondents remain optimistic about purchasing a home. Further, those planning to buy in the next year and finance the transaction with a mortgage have a ~13% down payment saved on average. Although this is encouraging, we believe the tighter underwriting standards remain a key obstacle to homeownership and expect this will take time to ease meaningfully. As such, we continue to believe a moderate recovery is unfolding.

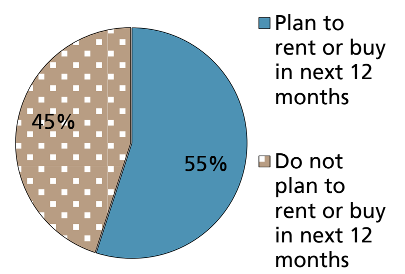
- **Millennials' desire for mobility should benefit Multifamily REITS.** This group had a material increase (52% from 40%) in plans to rent, with "move to a place where there are more job opportunities" rising in importance from #7 to #2. Further, pent-up demand from millennials still living at home is substantial and we view many as being future renters. With an improving labor market, we expect demand trends to pick up in 2015 for the Multifamily REITs.

- **Despite decline, home improvement spending intentions remain robust.** On average, those who are planning a project within the next three months expect to spend $4,334 on materials and labor, a decrease of 8% from 4Q14. That said, the leading home improvement retailers remain prime beneficiaries of this demand. Approximately 66% of respondents who intended to complete a project themselves indicated Home Depot and Lowe's were where they would purchase materials.

- **What's on the to-do list?** The most frequently cited home improvement projects (painting and repair/replace sinks and toilets) were broadly aligned with the previous iteration of our survey, suggesting homeowners have fairly consistent intentions for projects over the next few months.

We consider key findings as they relate to various sectors more specifically below.

Figure 1: Living arrangement plans of adults living with relatives or friends, wave 2



Source: UBS Evidence Lab Survey (February 2015)

Macro Economics

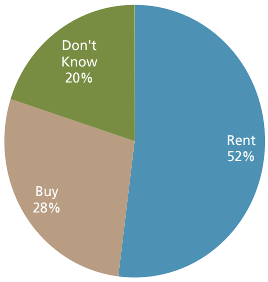
Household formation finally appears to be picking up after a disappointing first three quarters of 2014 (figure 6 and explanation in box on page 9). The change from a year earlier in the four-quarter moving average of households rose in Q4(14) to 792,000 from 467,000 a quarter earlier. This pickup was in line with results from our November 2014 UBS Evidence Lab survey in which almost half of adults living with relatives reported plans to either rent or buy in the coming year (figures 8 and 9). These earlier findings have been corroborated in a more recent February 2015 UBS Evidence Lab Survey. Just over half of sampled adults living with relatives or friends report planning to either rent or buy in the next twelve months. While plans may overstate actual moving, the results are consistent with rising household formation, which we see at close to a million units in 2015.

Multifamily REITs

Using the same approach as the first wave, we analyzed respondent data (1) in aggregate, (2) by age segment, and (3) by living situation. The results, on the whole, were largely similar between the two waves, but there were a handful of results and trends that caught our attention. This includes the following:

- **Renters – continue to rent:** An equally high percentage of renters (52% vs. 50%) say they will continue to rent for their next residence. If excluding "don't know" responses, we see a likely shift in the preference to rent for one's next residence, with the proportion increasing from 5:3 in wave 1 to 5:2 in wave 2.
- **Millennials – can't afford to buy**: Intentions to buy stayed at 43%, but this demographic continues to encounter financial difficulties in affording a home. Roughly ¼ of millennials agree they will never be able to afford a home due to down payment requirements and/or ownership expenses.
- **Doubled-Up Millennials – improving employment and stronger preference to rent:** While still low in comparison to other age groups, full-time employment increased to 33% from the high-20% in wave 1. Further, we noticed a material increase (52% from 40%) in plans to rent. One of the top reasons for renting is "move to a place where there are more job opportunities," which rose in importance from #7 to #2.
- **Unleashing pent-up demand:** Demand from millennials still living at home or with friends is substantial and we view many as being future renters. While employment trends are accelerating, only 33% of this segment is employed full-time. **With an improving labor market, we expect demand trends to pick up in 2015 for the Multifamily REITs.**

Figure 2: W2 Doubled-Up Millennial Living Plans, NTM



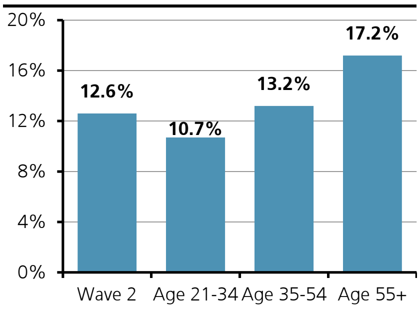
Source: UBS Evidence Lab

Homebuilding

In reviewing the findings from the second wave of our survey, we found respondents' overall attitudes and desires toward homeownership were essentially unchanged from the first (22% of total planning to buy versus 23% in 4Q14). This is in line with our view that a moderate recovery in housing is unfolding. That said, the pace of improvement will be limited by financial—as well as psychological—constraints. This time, we focused on respondents' financial situation, including savings, especially for millennials, in order to better understand this issue. More specifically, we note the following:

- On average, all the respondents planning to buy a home in the next year, and finance the purchase with a mortgage, have an approximate 13% down payment saved. That said, we believe potential buyers' ability to qualify for a loan—given the stringent underwriting—remains a significant impediment to improving demand and any easing will be gradual.
- More specifically, millennials (those aged 21-34) have an average down payment of 11% saved. Although this is encouraging, considering the availability of loans with as little as 3% down at the FHFA, we caution that this is likely partially offset by their overstated ability to get a loan given their limited credit history and lower incomes.
- Surprisingly, 36% of those surveyed said they would postpone purchasing a home—up from 29% in the first survey—if they are unable to qualify for a mortgage as opposed to looking for something more affordable. Given the

Figure 3: Avg. % Saved for Downpayment



Note: Represents respondents who are looking to buy in the next year and would use a mortgage to finance
Source: UBS Evidence Lab

importance of this issue to the broader recovery, we will closely monitor this data point in future surveys.

- Overall, the 1Q15 survey results support our view that the recovery in housing will be gradual. As such, we recommend investors take caution in selecting entry points and focus on company specific stories where earnings can grow at an accelerated rate even in a less supportive operating environment. As such, we highlight Buy rated PHM, RYL, HOV, and BZH.

Hardline Retail

Homeowners' responses to home improvement questions revealed some key insights into their thinking about spending in the category.

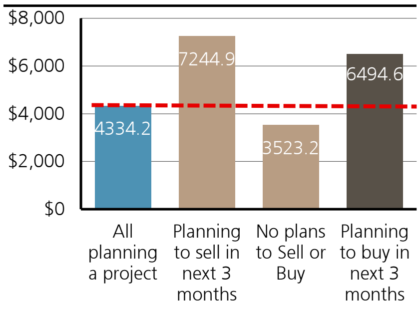
- On average, those who are planning a project within the next three months expect to spend $4,334 on materials and labor. This compares with the $4,720 amount from the 4Q'14 edition of our survey. We found that while renters intend to spend materially less than homeowners on home improvement projects, the average renter still intends to spend $2,627 over the next three months.

- From our sample of over 1,400 homeowners, 13% indicated they would re-paint on the inside of their home, with 7% planning to re-paint outside. Another popular upcoming project was related to sinks and toilets. Specifically, 9% of respondents indicated they were planning to replace a sink or toilet, with another 9% planning to repair a sink or toilet. These results were broadly aligned with the previous iteration of our survey, suggesting that the homeowners surveyed have fairly consistent intentions for home improvement projects over the next few months.

- Approximately 66% of survey respondents who intended to complete a project themselves indicated Home Depot and Lowe's were where they would purchase materials. This is broadly in line with the results from our previous survey. The two retailers continue to retain material share in the HI market. Homeowners planning to do at least one HI project by themselves indicated that they would purchase materials from HD (40%) and LOW (26%). Home Depot and Lowe's dominated the responses, as all other retailers received 5% or less consideration. Out of the two, indications of heavy spending were skewed toward HD over LOW. Homeowners with properties valued over $400k disproportionately indicated that they would buy their materials from HD over LOW. Interestingly, 5% homeowners indicated they would purchase most of their materials for DIY projects from AMZN, ahead of WMT & Ace Hardware. Overall, HD & LOW continue to grab the lion's share of HI spending.

- Homeowners that plan to sell within the next three months expect to spend $7,245 on home improvement projects (including materials and labor), or 67% more than average. This is a narrower gap from the 90% difference from the average spend in the previous iteration of our survey. Further, those intending to buy a home within the next three months plan on spending $6,495 on projects, or 50% more than average, which is also a much more narrow gap from the previous iteration of our survey. Those with no intention to sell or buy anticipate spending -14% and -24% less than average, respectively.

Figure 4: HI spending intentions - selling/buying vs not selling/buying



Source: UBS Evidence Lab

Top Stock Picks & Valuation

Figure 5: Top Stock Picks

Homebuilding	Ticker	Rating	PT	Target P/BV	Current P/BV
Pulte	PHM	Buy	$25	2.4x	2.2x
Ryland	RYL	Buy	$50	1.9x	1.9x
Beazer	BZH	Buy	$28	1.5x	1.0x
Hovnanian	HOV	Buy	$5	NA	NA
				FFO Multiple	
Multifamily REITs	**Ticker**	**Rating**	**PT**	**'15E**	**'16E**
AIMCO	AIV	Buy	$42	17.9x	17.4x
AvalonBay	AVB	Buy	$194	24.0x	22.0x
Equity Residential	EQR	Buy	$88	22.7x	21.3x
Hardline Retail	**Ticker**	**Rating**	**PT**	**Target CY15E P/E**	**Target CY16E P/E**
Home Depot	HD	Buy	$129	25x	22x
Lowe's	LOW	Buy	$83	25x	21x

Note: PHM PT is based on 10x 2017E EPS & HOV PT is based on 10x 2016E EPS (discounted back).
Source: Company reports and UBS estimates

Macro Economics

New Survey On Faster Household Formation

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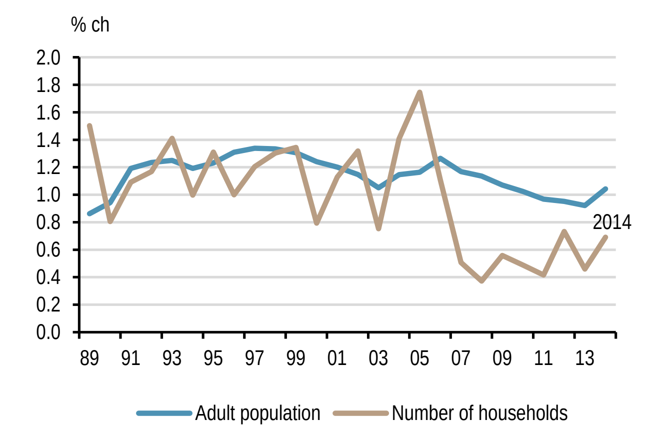
Second UBS Survey Suggests Less "Doubling Up"

Household formation finally appears to be picking up after being disappointing through the first three quarters of 2014. (See Figure 6 and explanation in box on following page.) The change from a year earlier in the four-quarter moving average of households rose in Q4(14) to 792,000 from 467,000 a quarter earlier. This pickup was in line with results from a November 2014 UBS Evidence Lab survey in which almost half of adults living with relatives reported plans to either rent or buy in the coming year. (See Figures 8 and 9.)

Expanded coverage of "doubled up" adults in second UBS survey

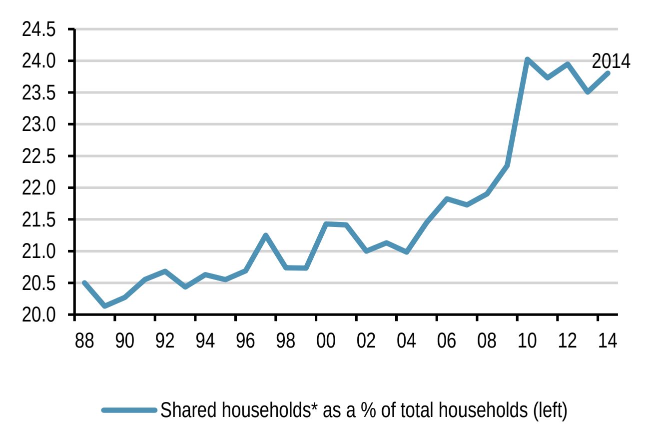
Compared to the earlier November 2014 survey, the February 2015 survey included adults living with friends and as well as adults living with relatives—the scope of the earlier survey. The more comprehensive coverage of "doubled up" adults, in principle, should generate a more accurate picture. That said, the two samples are not strictly comparable. However, the results of the second survey re-enforce our confidence in the conclusions from the initial survey.

Figure 6: Household formation picked up a bit last year



Note: Census estimates for 2014 population growth.
Source: Census Bureau and UBS

Figure 7: Less "doubling up" to raise household formation



Note: The households data are as of March each year. * Includes cohabiting households.
Source: "Poverty and Shared Households by State: 2011", Suzanne Macartney and Laryssa Mykyta, November 2012, Census Bureau and UBS

"Doubled up" adults still planning on changing residences

A substantial portion (44% in the 1st survey and 55% in the 2nd survey) of surveyed adults cite plans to buy or rent in the next 12 months. (Adults living with friends may feel less attached (or welcome) as "guests" than those living with relatives.) While we don't have consecutive fully comparable reports much less than a time series yet, these results suggest that moving out of doubled up residences could be considerable and have an important economic impact. For instance, last year there were 27-28 million shared households among the 116 million households. Each one percentage point decline in net shared households would add around 275,000 to overall household formation that was around 792,000 last year. (Note in Figure 7 that a one percentage point decline in the fraction of households that are shared would represent only a partial reversal of the rise in the household sharing percentage since the Great Recession.)

Comparison Of The Two Surveys

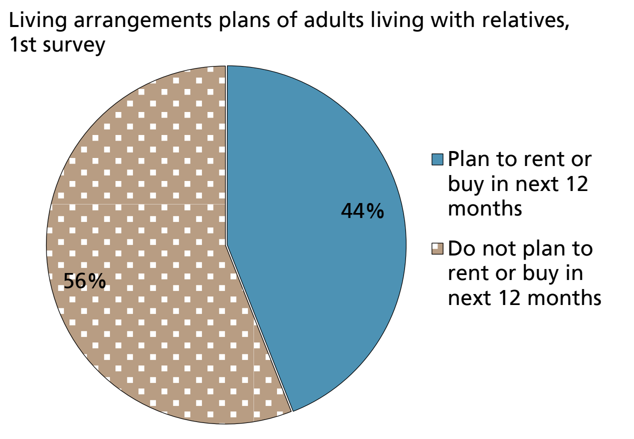
Key results from the two surveys are compared in Figures 8-21. The surveyed financial conditions of adults living with friends or relatives in the 2nd survey was about the same as the financial conditions of adults living with relatives in the 1st survey. However, adults living with friends and relatives were less likely to be employed and were more likely to cite insufficient funds for independent living as a reason for not planning to leave their current shared living arrangements in the next year. Also, adults living with friends or relatives cited more perceived difficulty in finding a residence to buy.

Household Formation

Household formation is the net change in outstanding occupied residences, whether rented or owned. Government statisticians estimate the number of outstanding occupied residences as follows. The vacancy rate for rented and non-rental units is estimated in a quarterly survey. The estimated overall vacancy rate is then applied to the estimated outstanding number of residences to derive an estimate of the number of occupied residential units.

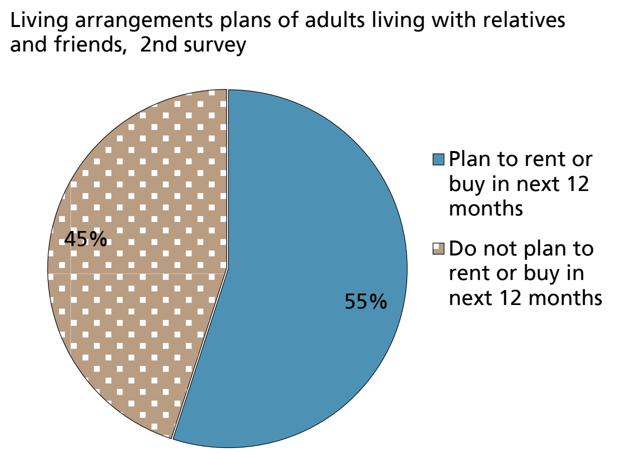
The number of outstanding residential units is estimated by adding to earlier estimated levels the number of new housing units completed minus estimated units becoming no longer habitable. For instance, the increase in the number of habitable units in 2015 depends on the 884,000 completed housing units in 2014 minus the estimated units no longer being habitable. In this setting, for 2015 household formation to reach our one million projection, there needs to be further vacancy rate declines.

Figure 8: Wave 1



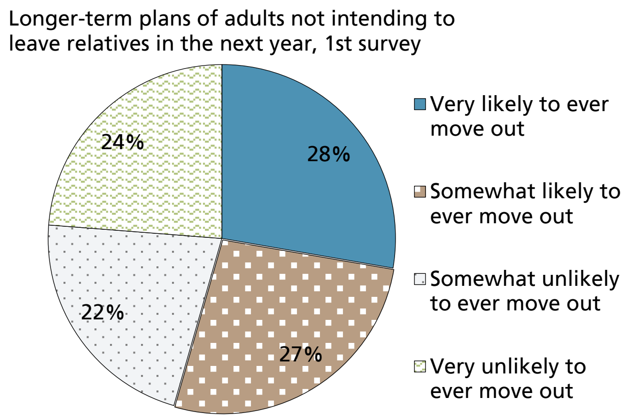
Source: UBS Evidence Lab Survey (November 2014)

Figure 9: Wave 2



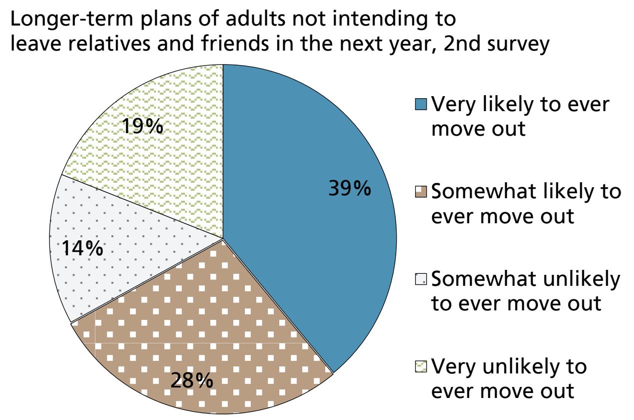
Source: UBS Evidence Lab Survey (February 2015)

Figure 10: Wave 1



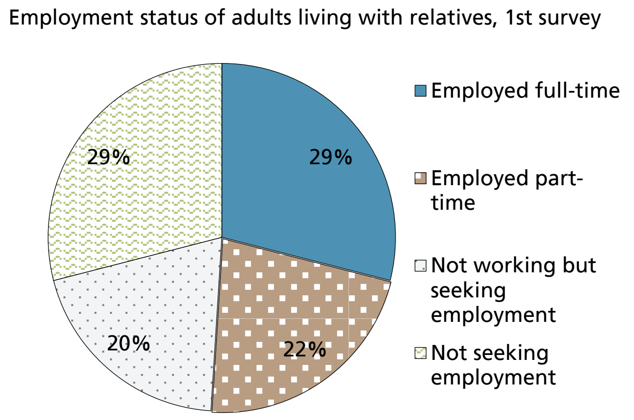
Source: UBS Evidence Lab Survey (November 2014)

Figure 11: Wave 2



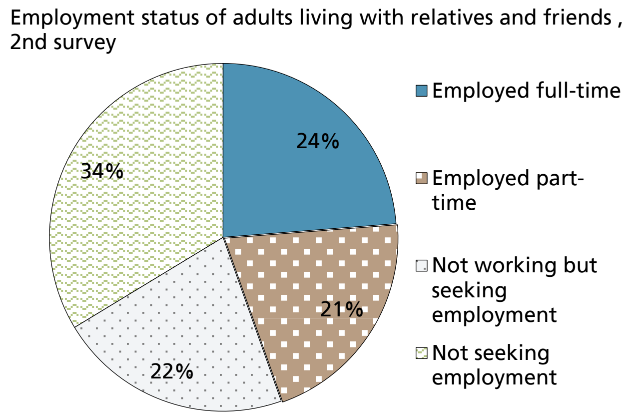
Source: UBS Evidence Lab Survey (February 2015)

Figure 12: Wave 1



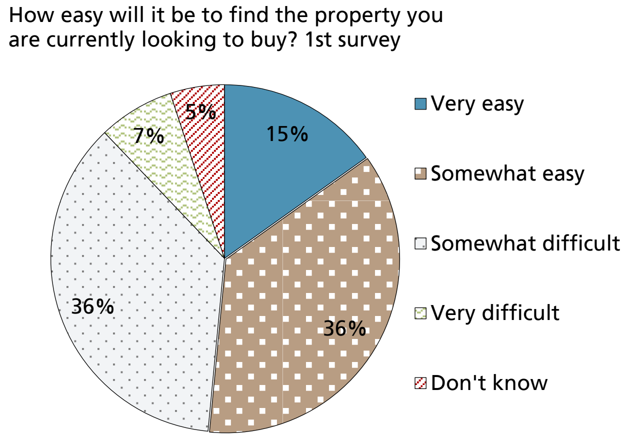
Source: UBS Evidence Lab Survey (November 2014)

Figure 13: Wave 2



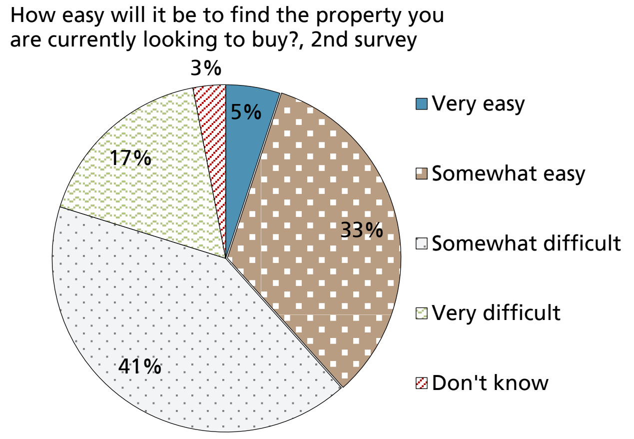
Source: UBS Evidence Lab Survey (February 2015)

Figure 14: Wave 1



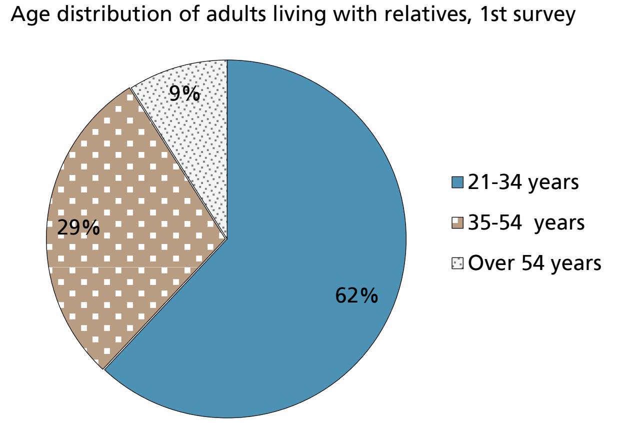
Source: UBS Evidence Lab Survey (November 2014)

Figure 15: Wave 2



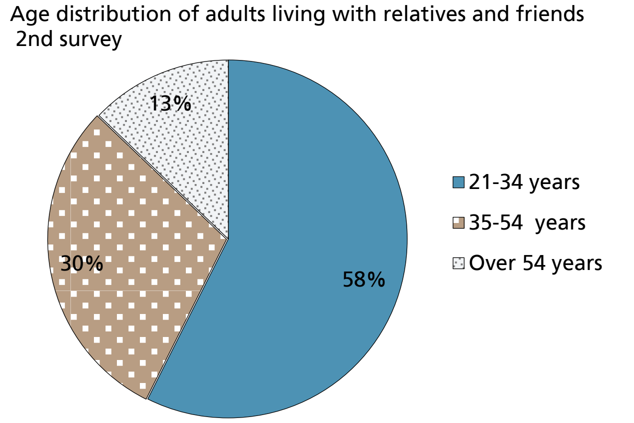
Source: UBS Evidence Lab Survey (February 2015)

Figure 16: Wave 1



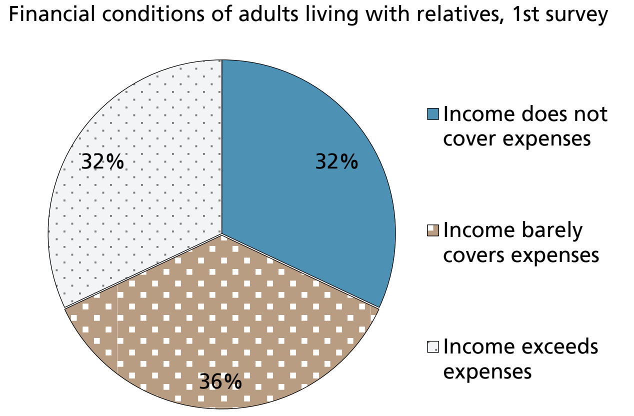
Source: UBS Evidence Lab Survey (November 2014)

Figure 17: Wave 2



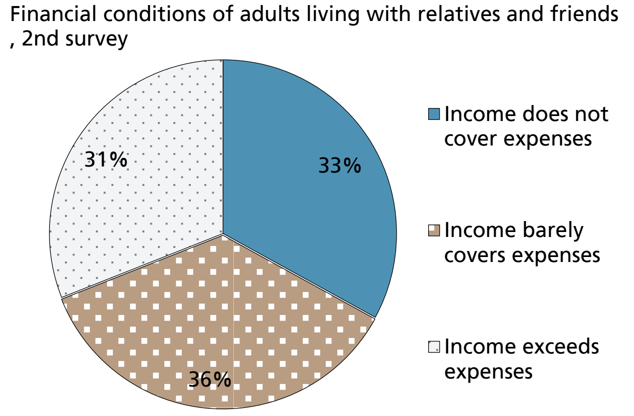
Source: UBS Evidence Lab Survey (February 2015)

Figure 18: Wave 1



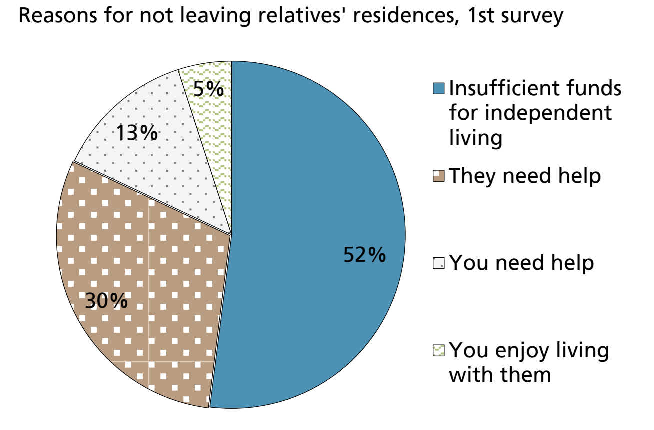
Source: UBS Evidence Lab Survey (November 2014)

Figure 19: Wave 2



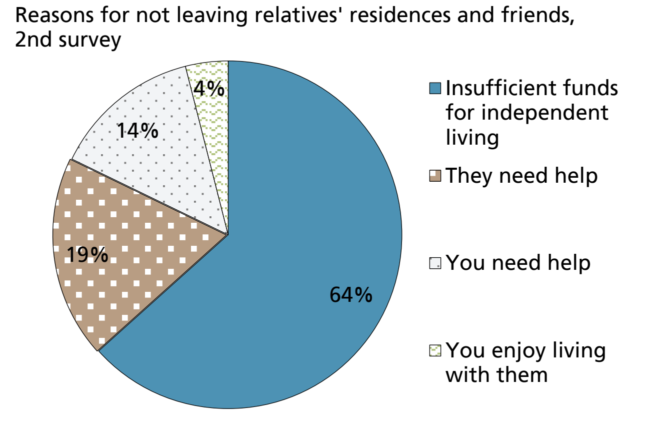
Source: UBS Evidence Lab Survey (February 2015)

Figure 20: Wave 1



Source: UBS Evidence Lab Survey (November 2014)

Figure 21: Wave 2



Source: UBS Evidence Lab Survey (February 2015)

Multifamily REITs

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Survey Takeaways for Multifamily REITs

The UBS Evidence Lab U.S. Housing Intentions Survey includes information that applies directly to the U.S. Multifamily REIT sector. From the results, we seek to understand (1) intentions of buying versus renting as an indication of demand, (2) the rationale for choosing to rent, and (3) trends that indicate new household formation, particularly among millennials.

Since the survey is meant as a sample of the national population (and not certain MSAs), the direct inferences mostly apply to the broader U.S. apartment market. The survey results reinforce what we already view to be strong demographic trends for the Multifamily sector.

- **Renters – continue to rent:** An equally high percentage of renters (52% vs. 50%) say they will continue to rent for their next residence. If excluding "don't know" responses, we see a likely shift in the preference to rent for one's next residence, with the proportion increasing from 5:3 in wave 1 to 5:2 in wave 2.

- **Millennials – can't afford to buy**: Intentions to buy stayed at 43%, but this demographic continues to encounter financial difficulties in affording a home. Roughly ¼ of millennials agree they will never be able to afford a home due to down payment requirements and/or ownership expenses.

- **Doubled-Up Millennials – improving employment and stronger preference to rent:** While still low in comparison to other age groups, full-time employment increased to 33% from the high-20% in wave 1. Further, we noticed a material increase (52% from 40%) in plans to rent. One of the top reasons for renting is "move to a place where there are more job opportunities," which rose in importance from #7 to #2.

- **Unleashing pent-up demand:** Demand from millennials still living at home or with friends is substantial and we view many as being future renters. While employment trends are accelerating, only 33% of this segment is employed full-time. **With an improving labor market, we expect demand trends to pick up in 2015 for the Multifamily REITs.**

While MSA level responses were not part of this survey, we would expect coastal areas such as New York City and San Francisco to show even stronger preferences than the national population for renting versus owning given the large expense (and down-payment) of for-sale housing in such markets. There is still a strong preference (among all age types) for owning versus renting, but financially many cannot afford owning. **We think this points to more risk for Multifamily REITs exposed to lower cost housing markets such as the Sunbelt (e.g. CPT and PPS), rather than the Coasts, where move-outs to buy a home could increase in 2015-16. This is one of the major reasons we have a coastal preference for our Buy rated Apartment REIT picks: AVB; EQR; and AIV.**

We break down the survey to show preferences of the 4 key groups:

1) Current Renters (any age level)

2) Millennials (age 21-34) – Current Renters

3) Millennials (age 21-34) – Current Renters & Owners

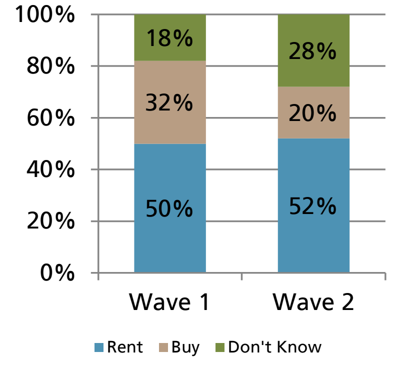
4) Millennials (age 21-34) – Living with Parents / Relatives / Friends

Survey Says: Buy or Rent?

Current Renters (any age level)

- **More to stay renters:** Compared to wave 1, we saw a similarly high percentage in those saying their next residence is likely to be a rental (52% vs. 50%) rather than a purchased for-sale home (20% vs. 32%). While the overall affirmative response to rent was only 2% higher, the lower response rate to for-sale housing and a higher rate of indifference (28% vs. 20%) resulted in a notably higher rental preference proportion of 5:2 vs. 5:3.
- **No change in plans over the next 12 months:** No material change in the decision plans for the next 12 months with 31% still looking to buy a home and 34% (up from 33%) looking to rent.
- **Buying is an investment decision:** For those current renters looking to buy, the top reasons remain "owning a home is better than renting one" and "buying a home is a good investment."
- **Breaking the bank:** For those current renters who are not looking to buy, the top reasons for renting are still financially driven, citing the inability to afford a down payment or the expenses affiliated with owning home.

Figure 22: Renters Stay Renters

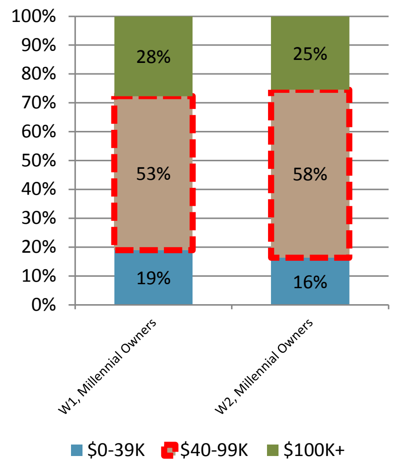


Source: UBS Evidence Lab

Millennials (age 21-34) – Current Renters

- **Incomes improve for millennials:** Millennial renters still have far lower household incomes than millennial owners. Among millennial renters, 54% (vs. 56%) have income under $40K, while 38% (vs. 36%) fall between $40-99K and 8% (flat) have income over $100K. However, among millennial owners, 16% (vs. 19%) have income under $40K, while 58% (vs. 53%) fall between $40-99K and 25% (vs. 28%) have income over $100K. While the percentage of high-income earners declined, we see fewer low-income earners and more middle-income earners, indicating rising wages & improving financial situations.
- **Saving for later:** Those looking to stay renters continue to do so because of financial considerations (can't afford to buy a home). The lifestyle preference of renting was a lower consideration (23% saying renting is more flexible based on life changes).

Figure 23: Better Financial Situation



Source: UBS Evidence Lab

Millennials (age 21-34) – Current Renters & Owners

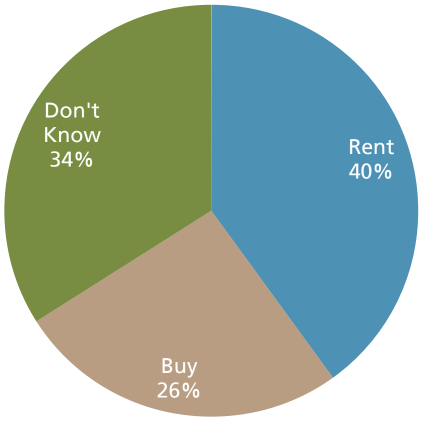
- **Stable buying intentions:** 43% (flat) plan to buy in the next 12 months.
- **BUT it's simply unaffordable:** roughly ¼ of those surveyed (flat from prior survey) either agree or strongly agree they will never be able to afford to buy a home.
- **AND owning is expensive:** The top reasons for not buying remain mostly financial (e.g. not enough saved for down payment, can't afford expenses of owning a home).

Millennials (age 21-34) – Living with Parents / Relatives / Friends

- **Improving employment:** Full-time employment increased to 33% (from high-20%). Part-time employment decreased to 19% (from low-20%); unemployed but looking stayed virtually flat (26%); unemployed and not looking dropped to 6% (from double-digits); students increased to 16% (from 13%).

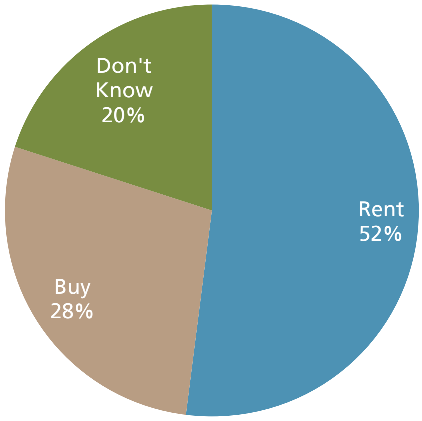
- **Propensity to rent:** In the next 12 months, 52% (vs. 40%) plan to rent, 28% (vs. 26%) plan to buy, and 20% (vs. 34%) don't know.

Figure 24: W1 Doubled-Up Millennial Living Plans, NTM



Source: UBS Evidence Lab

Figure 25: W2 Doubled-Up Millennial Living Plans, NTM



Source: UBS Evidence Lab

- **Birds leaving the nest:** 75% say they are likely to move out of their parents' / relatives' / friend's homes at some point in the future.

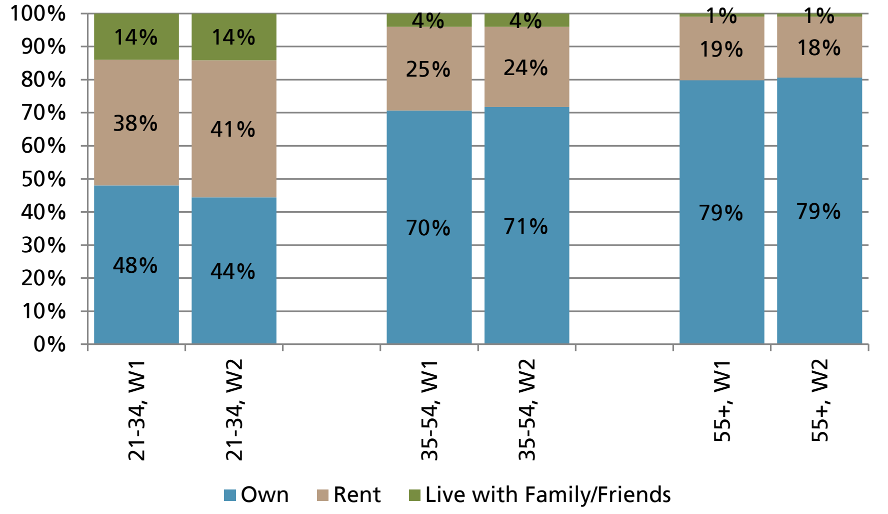
- **Finances prevent moveouts:** For those *not* looking to move out in the next 12 months, an increasing majority (66% vs. 58%) say this is because they do not have enough money to live on their own.

A Bird's Eye View: Results by Demographic

While millennials are of particular interest, we will explore this segment in further detail later. First, we will start with the aggregate results that apply to the choice of renting vs. buying.

Consistent with the first wave, the highest percentage of renters are millennials, defined as adults age 21-34. While this group still accounts for the vast majority of those who live with parents, relatives, or friends, we note a rising percentage of renters vs. owners.

Figure 26: Living Situation by Age Group



Source: UBS Evidence Lab

Nearly ¼ of those surveyed (same as in wave 1) indicated an intention to purchase a home within the next 12 months, which coincides with 27% (vs. 25% in wave 1) saying now is a good time to buy a home where they live. However, also consistent with wave 1, nearly 33% of these respondents believed they would face difficulties in being approved for the house they want (either not having enough money for a down payment or not believing they will qualify for a mortgage). As a result, more than 60% of the buying population facing difficulty stated they would either postpone the purchase decision or would look for a smaller or less expensive home as an alternative to the intended purchase. This, in turn, could at the least boost short term demand for rentals as searches are extended.

Figure 27: Intention to Purchase a Home by Age Group

Source: UBS Evidence Lab

The reasons for buying instead of renting showed little variance between wave 1 and wave 2. Reasons are heavily shifted towards sentiment, with "owning a home is better than renting one" and "buying a home is a good investment" trumping the financial reasons of affordability and having the money for a down payment.

Figure 28: Top Reasons for Buying Instead of Renting (for those planning to buy), by Age Group

Rationale	Total	21-34	35-54	55+
Owning a home is better than renting one	1	1	2	1
Buying a home is a good investment	2	2	1	2
Can afford the expenses of owning a home (maintenance, utilities, etc.)	3	4	8	3
You believe you will qualify for a mortgage	4	5	4	4
Don't mind being tied down to owning a home right now	5	3	6	8
Now is a good time to buy a home where you live	6	8	3	5
Have the money to afford a down payment	7	7	7	6
Can afford the house you want right now	8	10	5	7
You have security in your job situation	9	6	10	9
You are comfortable taking on more debt right now	10	8	9	10
Any other reason	11	11	11	11
Bad experience with previous landlord	12	12	12	12

Source: UBS Evidence Lab

Although 65% of the renter population (an increase from 60% in wave 1) believed owning is better than renting, this group continues to rent instead of buy due to factors relating to affordability (expenses and debts) and ownership (down payment and mortgage qualification), which would likely be magnified in the coastal areas due to higher housing costs. In our survey, 31% of current renters (same as wave 1) plan or aspire to buy a home in the next 12 months, which compares to the typical 20% move-out rate due to homebuying as reported by Multifamily REITs. This indicates optimism among renters that increased wages or job stability will allow them to afford a house.

Figure 29: Top Reasons for Renting Instead of Buying (for those planning to rent), by Age Group

Rationale	Total	21-34	35-54	55+
Can't afford down payment	1	2	1	2
Renting a house is more flexible if your life changes	2	4	1	1
Can't afford the house you want right now	3	1	8	8
Can't afford the expenses of owning a home (maintenance, utilities, etc.)	4	3	4	4
Don't think you will qualify for a mortgage	5	4	3	3
You have too many other debts right now	6	6	7	6
Don't want to be tied down to owning a home right now	7	7	5	5
Don't have security in your job situation	8	9	5	10
Buying a house is a very risky investment	9	8	9	9
Now is not a good time to buy a home where you live	10	10	10	11
Don't think owning a home is a good idea	11	11	11	7

Source: UBS Evidence Lab

Why Do Millennials Choose to Rent vs. Buy?

Similar to the reasons cited above for those not looking to buy (across all age groups), and in-line with the results of wave 1, millennials are delaying home purchasing decisions and opting to rent for financial reasons, primarily because they either cannot afford the down payment or need to pay off debt.

Figure 30: Top 5 Reasons Millennials are Delaying Buying a Home

Rationale	% of Respondents
Until you are able to pay off more of your debt	27%
Until you have enough money saved up for a down payment	25%
Until you get a higher-paying job	23%
Until you have more steady income	22%
Until you get a more stable job	17%

Note: Respondents could select multiple reasons among 15 choices, so the sum of responses is >100%
Source: UBS Evidence Lab

The financial burden of home ownership also applies to current millennial renters. As shown below, the predominant reason that millennial renters continue to rent is due to the inability to afford a down payment, the expenses of home ownership, or the belief they will not qualify for a mortgage.

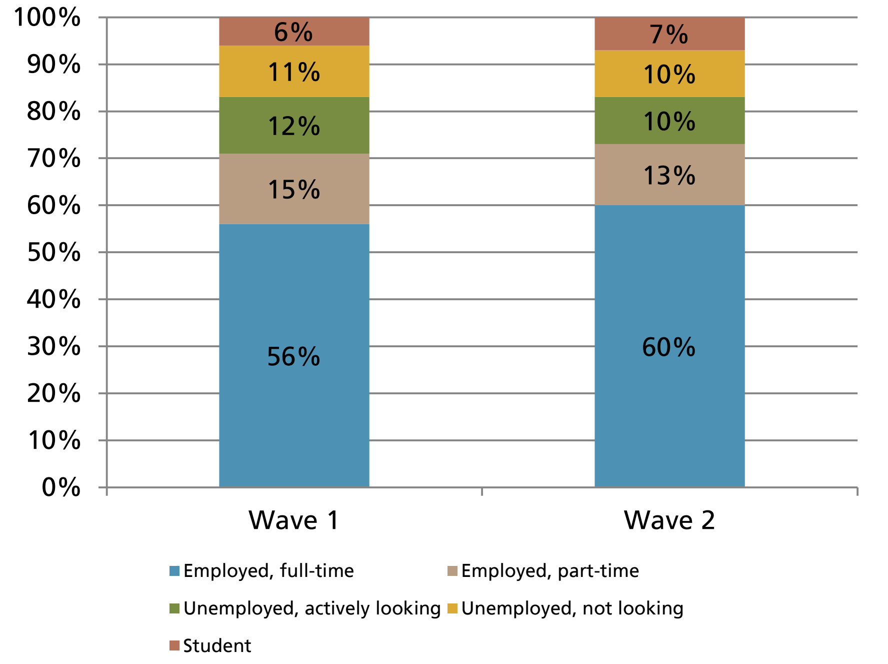
Figure 31: Top Reasons Why Millennial Renters Choose to Stay Renters

Rationale	Renters
Can't afford down payment	1
Don't think you will qualify for a mortgage	2
Can't afford the expenses of owning a home (maintenance, utilities, etc.)	3
Renting a house is more flexible if your life changes	4
Can't afford the house you want right now	5
You have too many other debts right now	6
Don't want to be tied down to owning a home right now	7
Don't have security in your job situation	8
Buying a house is a very risky investment	9
Now is not a good time to buy a home where you live	10
Don't think owning a home is a good idea	11

Source: UBS Evidence Lab

Furthermore, millennials remain less likely to be employed on a full-time basis than adults age 35-54. While the sequential survey data of improved full-time employment is encouraging, the lower relative employment rate could explain the relatively high percentage of lower-income earners among millennials and the potential difficulties in achieving homeownership. Recent job growth trends are promising but we need to see an improving employment situation for millennials to support a strengthening housing market (both for rentals and purchases).

Figure 32: Employment Situation for Millennials



Source: UBS Evidence Lab

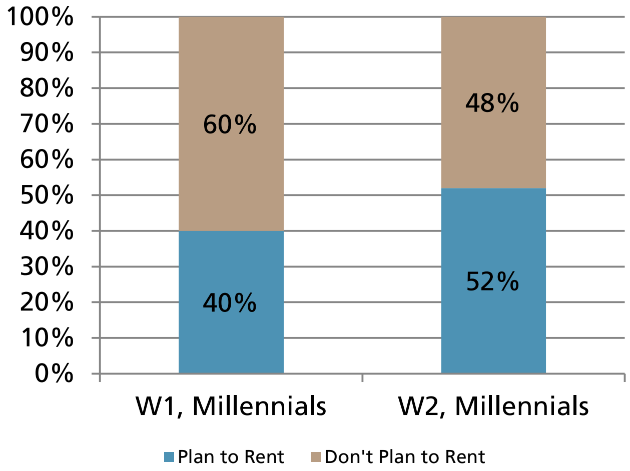
Doubled-Up Millennials Want to Move Out

As indicated earlier, millennials constitute the majority (two-thirds) of those still living at home with family. Although 75% of millennial respondents currently living at home say they are likely to move out, when digging further into the data we found that the #4 reason for delaying buying a home (waiting for a more steady income) remains the top factor (by a wide margin) preventing doubled-up millennials from making this transition. With improving U.S. job growth, we see a trend of millennials gaining a stronger foothold in the employment market and moving out of their family homes into rental housing.

Importantly, compared to our inaugural survey, there are more respondents currently living with family or friends that plan to rent. As shown in the following figure, those planning to rent among this population increased from 35% in wave 1 to 44% in wave 2. This increase is primarily due to more respondents looking to rent 4-12 months from now. Doubled-up millennials, in particular, expressed a material increase in plans to rent, with over half of the population now indicating rental plans, with most of the gain in the 4-12 month timeframe.

NOTE: With regard to these findings, we caution that two data points does not necessarily make a trend. Given that our first two surveys were done in November 2014 and February 2015, we are not yet sure whether seasonality or other factors may be playing into the survey responses.

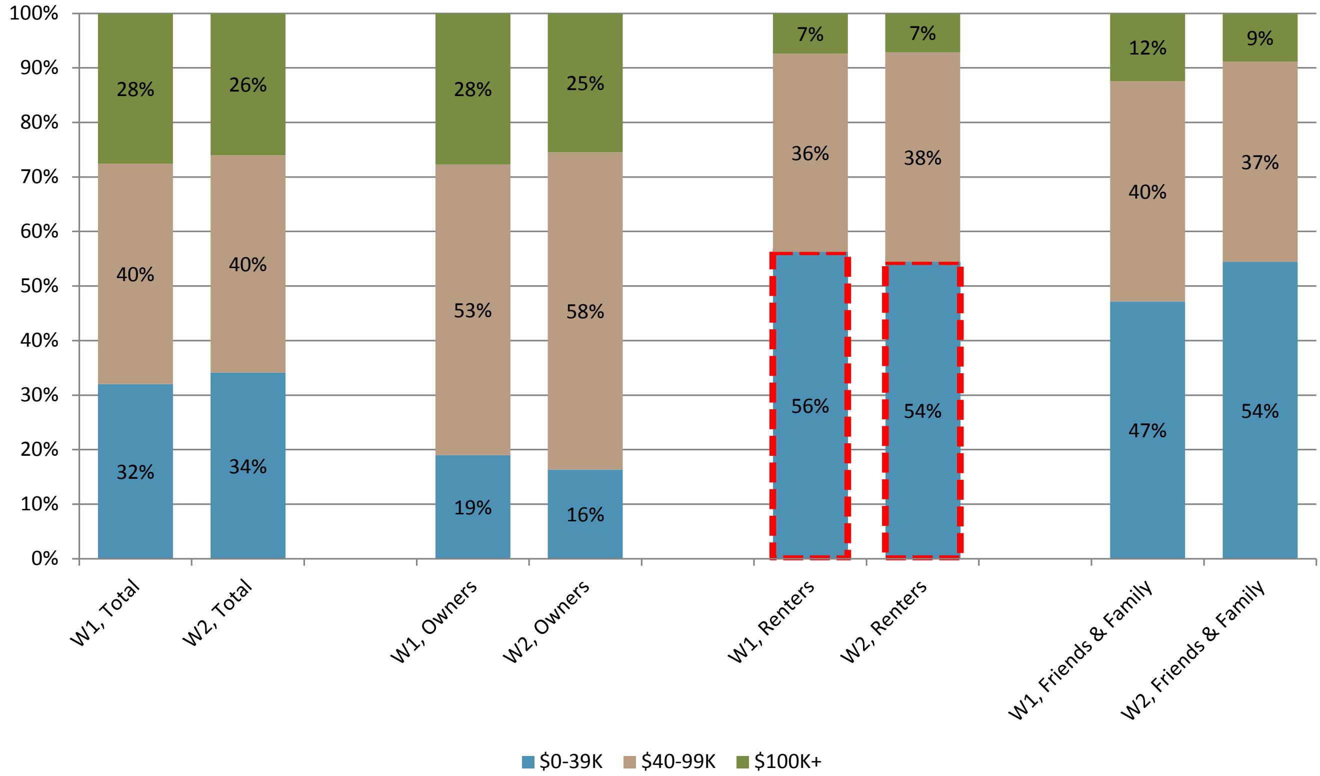
Figure 33: Plans to Rent Increasing Among Doubled-Up Millennials



Source: UBS Evidence Lab

Wage growth may spur millennial renters to become home owners, but we believe the reported preference to rent over buy should continue to support the Multifamily sector. Coupling this with the concept that wage growth may be necessary just to keep pace with rental rate growth, this lends support to the idea of "permanent renters" among millennials.

Figure 34: Income Disparities Among Millennials, by Living Situation



Source: UBS Evidence Lab

Piecing the Puzzle Together for Multifamily REITs

We see a healthy fundamental picture for the Multifamily REITs sector. Demand, driven by increased levels of household formation and job growth, continues to exceed supply except in limited markets such as Washington D.C. Supply has been growing in parts of Texas and California, mostly in response to strong job growth trends there. We expect supply deliveries to remain heightened in certain metro areas (e.g. Washington D.C., Houston, Dallas, Austin and the San Francisco Bay Area), but total U.S. supply deliveries should begin to moderate in 2015.

To this end, the most recent U.S. Census data showed the rate of Multifamily permit growth is hopefully slowing, which suggests starts could peak in early 2015. In February the 6-month trailing average for Multifamily permits was 392K, which was up 7% y/y but well below the 40-50% y/y growth rates in 2012-2013.

With this backdrop, and as we describe in our recent note from our Houston tour (**click here for the full report**), **we reiterate our concerns about growing supply pressures impacting Sunbelt markets more than coastal markets. Consequently, we continue to have a coastal bias and our top picks remain AVB, EQR, and AIV.**

Our Buy-rated stocks in the sector:

The results from the Housing Intentions Survey as well as MSA-level data support our coastal-developer bias (AVB and EQR). However, with these blue-chip Multifamily REITs trading at sub-5% implied cap rates, we think investors should also own AIV for its Class B exposure (as these assets have less new supply threats and will likely benefit from some cap rate compression vs. Class A assets at this point in the cycle).

AvalonBay (AVB) – We think AVB has the biggest potential upside to NAV and earnings estimates from an improving economy because it has the largest development pipeline in the sector and the heaviest exposure to the Northeast (Boston and metro NYC account for 50% of its NOI). This region has seen lagging rent and jobs growth vs. the national average but is now improving. The math on the company's development pipeline continues to look compelling: every $1 billion delivered at a 7% yield (assuming 5% cap rate) creates $3 per share of NAV growth. Thus, we calculate the current pipeline under way creates $12 per share of NAV growth. With another $1.0-1.5bn being started in 2015, AVB continues to be one of the top growing Multifamily REITs in terms of adding shareholder value, in our estimate. Our $194 price target is based on a 5% premium to our forward NAV estimate.

Equity Residential (EQR) – EQR trades at an attractive discount to our NAV estimate, making it a particularly attractive blue-chip with the best Class A assets among the Multifamily REITs we cover. Our $88 price target is based on a 5% premium to our forward NAV estimate.

AIMCO (AIV) - Despite outperformance for the stock in 2014, we think AIV's valuation still does not reflect the attractive portfolio upgrades completed since 2009. AIV trades at an attractive discount to our $43 1-year forward NAV estimate, with the market pricing the stock as if it still owned its lesser-quality 2008-era portfolio. We expect AIV to post 4.6% annual SSNOI growth in 2015, similar to heavier Class A peers like EQR and UDR, which trade at lower implied cap rates. AIMCO's heavy mix of Class B/C assets (55% of NOI, with the remainder

Class A) provides a hedge against new supply threats to the sector. Our $42 price target is based on a 2% discount to our forward NAV estimate.

Figure 35: Multifamily REIT Comps

Ticker	Rating	Target Price	Price 2-Apr	FFO Multiple '15E	FFO Multiple '16E	AFFO Multiple '15E	AFFO Multiple '16E	Implied Cap Rate	Prem/(Disc) to NAV 4Q14	Prem/(Disc) to NAV 4Q15	Div Yld	Market Cap ($000)	AFFO Y/Y 2015E	AFFO Y/Y 2016E
AIV	Buy	$42.00	$38.96	17.9x	17.4x	23.5x	20.5x	5.79%	-5.0%	-9.0%	2.7%	$6,346	2.1%	14.7%
AVB	Buy	$194.00	$174.74	24.0x	22.0x	27.0x	25.1x	4.49%	2.1%	-5.8%	2.8%	$23,748	7.0%	7.7%
CPT	Neutral	$79.00	$78.52	17.8x	17.1x	21.7x	20.4x	5.52%	-0.9%	-6.0%	3.5%	$7,136	4.5%	6.5%
EQR	Buy	$88.00	$78.31	22.7x	21.3x	26.5x	24.6x	4.50%	-0.9%	-6.4%	2.5%	$30,825	8.2%	7.5%
ESS	Neutral	$223.00	$229.15	23.9x	21.7x	29.8x	26.5x	3.87%	19.8%	8.7%	2.4%	$15,849	15.3%	12.4%
HME	Neutral	$68.00	$69.97	15.2x	14.6x	16.4x	15.8x	5.82%	7.6%	1.1%	4.2%	$4,875	8.7%	4.3%
PPS	Neutral	$61.00	$56.90	19.8x	19.4x	23.5x	23.4x	5.29%	-1.5%	-6.5%	2.7%	$3,194	1.2%	0.4%
UDR	Neutral	$33.00	$33.98	20.8x	19.8x	23.0x	21.3x	4.75%	7.2%	-1.0%	3.0%	$9,230	8.1%	8.0%
Multifamily REIT Average				**21.9x**	**20.5x**	**25.7x**	**23.7x**	**4.66%**	**3.9%**	**-3.2%**	**3.0%**		**8.2%**	**8.4%**
Total REIT Average				**19.3x**	**18.0x**	**24.1x**	**22.1x**	**5.13%**	**14.6%**	**7.7%**	**3.3%**		**9.6%**	**8.9%**

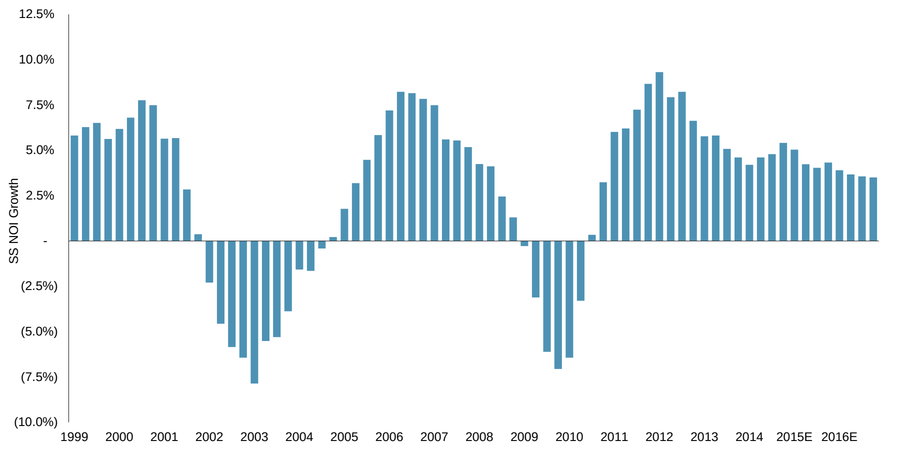
Source: UBS Investment Research, Factset

Expectations for 2015

The U.S. Multifamily REIT sector is now in its 5th consecutive year of positive SSNOI growth, already beating the most recent recovery: The growth cycle lasted just 4 years in the 2005-2008 period, sandwiched between two U.S. recessions in that decade. We see the current recovery cycle lasting at least through 2016 absent another U.S. recession (with possible re-acceleration in Multifamily fundamentals coming in late 2015 if new supply peaks and U.S. job formation accelerates, given what we view to be a strong demand backdrop).

We expect the Multifamily REITs to post 4.4% SSNOI growth in 2015, down from 4.7% in 2014, 5.3% in 2013 and 7.8% in 2012. Such a slowdown to a more normalized pace is natural, given the sharp recovery off the bottom in 2010. We think private market valuations remain supportive of Multifamily REIT NAVs, with possible additional M&A in the next year providing further valuation support.

Figure 36: Multifamily REITs - Industry Same-Store NOI Growth & UBS Estimates



Source: Company Reports, UBS Investment Research

Homebuilding

Current View on Housing

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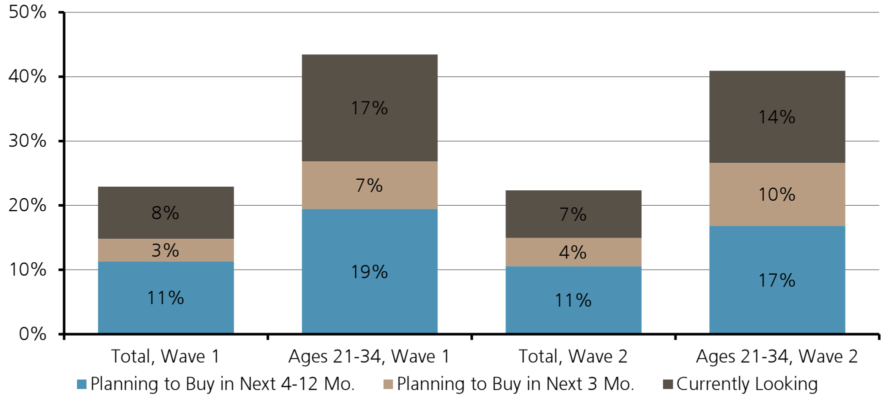
Demand Trends Positive Even With Underlying Constraints

In comparing responses from the second wave of the US Housing Intentions Survey to the first, data continues to support our view for a moderate recovery. Specifically, while interest in buying a home in the next year remains strong, financial and psychological headwinds persist. In our view, these constraints are likely to continue due to limited wage inflation and pro-cyclicality in the mortgage market which will constrain the pace of improvement.

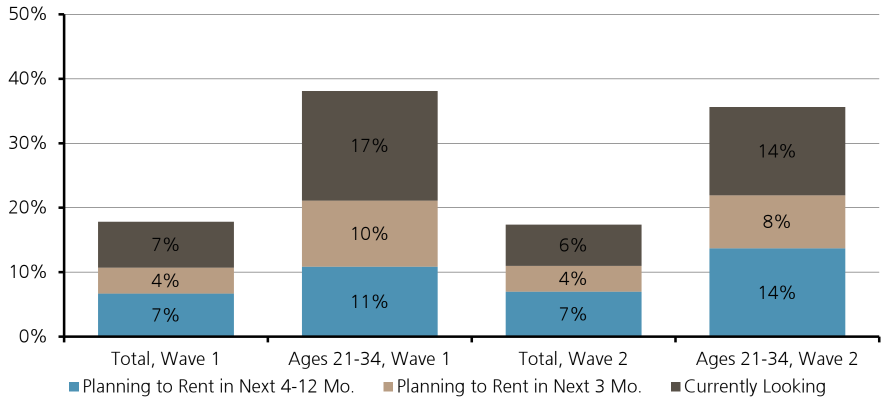
While buying is still favored to renting, we did not see any movement in the relative attractiveness of homeownership (as measured by hopes to buy vs. rent), most likely related to the uncertainty buyers are facing in the market currently. That said, we would expect to see this trend gradually revert to historical norms as conditions in the housing market improve.

Figure 37: Plans to Buy a Residential Property



Source: UBS Evidence Lab

Figure 38: Plans to Rent as Primary Residence

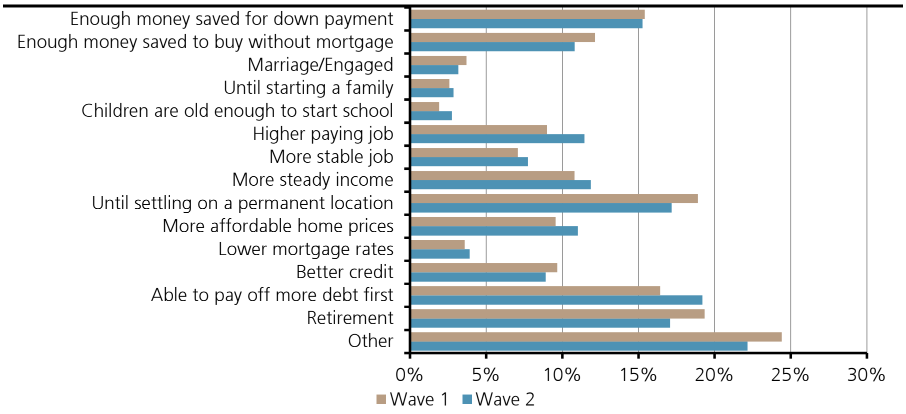


Source: UBS Evidence Lab

So What's Holding Us Back?

While we know that interest in homeownership exists, there are a number of reasons to believe that this recovery will continue to be one of moderate growth, as opposed to a more robust upcycle.

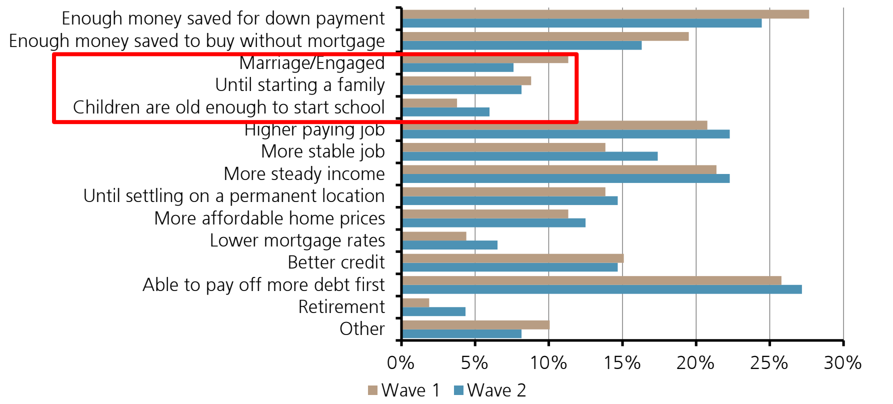
Figure 39: What are you waiting for to buy a home? (Total)



Note: Represents respondents who are planning to buy a home in the future.
Source: UBS Evidence Lab

More specifically for millennials, in addition to financial constraints, life cycle events play a significant role in their decision making process.

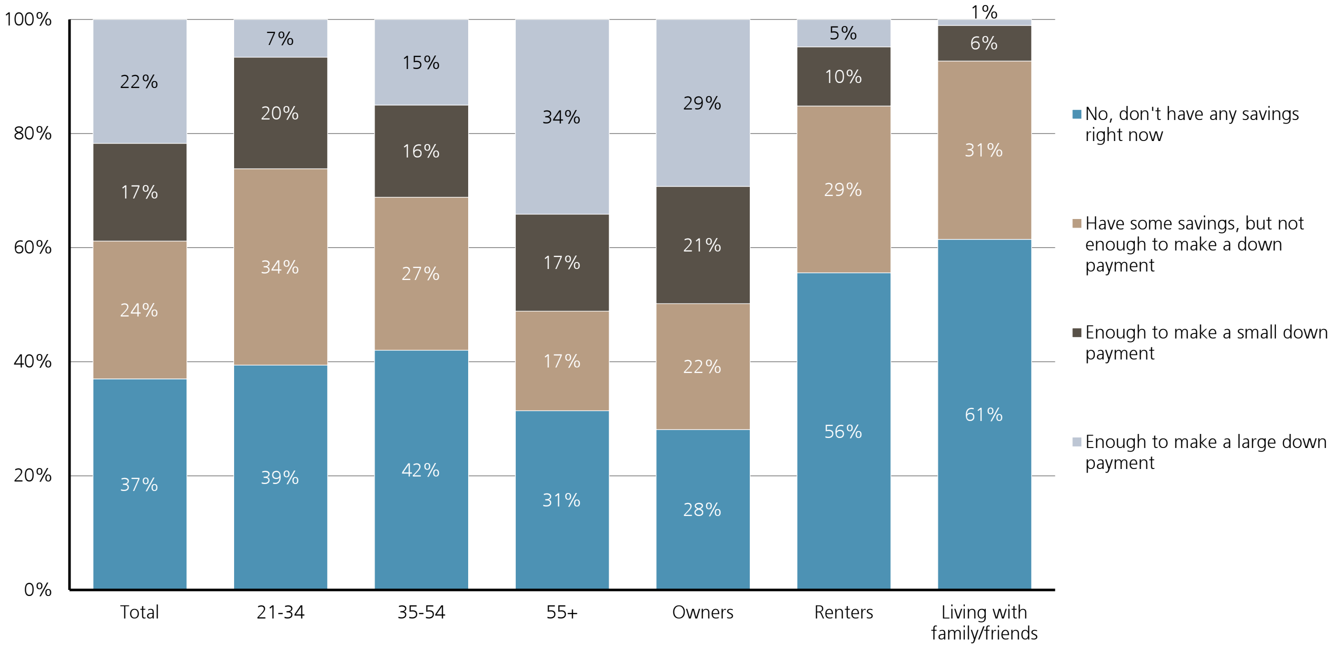
Figure 40: What are you waiting for to buy a home? (Age 21-34)



Note: Represents respondents who are planning to buy a home in the future.
Source: UBS Evidence Lab

To better understand the degree to which financial constraints are limiting growth, specifically within the millennial generation, we asked about level of savings. Of respondents who are not planning to buy a home in the next 12 months, just 7% of those ages 21-34 and 5% of renters believe they currently have enough saved to make a large downpayment if they decided they wanted to purchase a home.

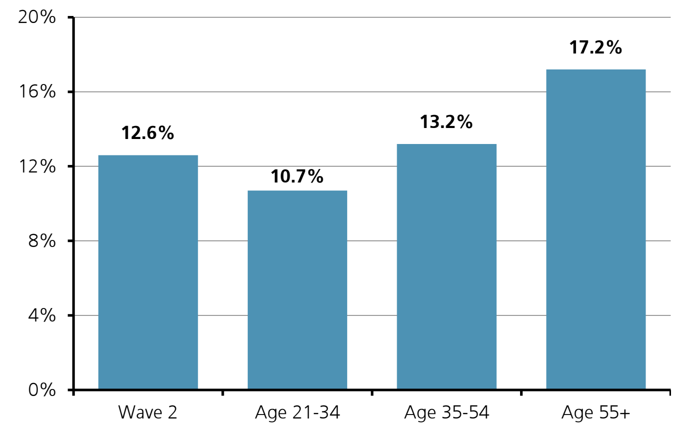
Figure 41: Current Savings For Downpayment



Note: Represents respondents who don't plan to buy a home in the next 12 months.
Source: UBS Evidence Lab

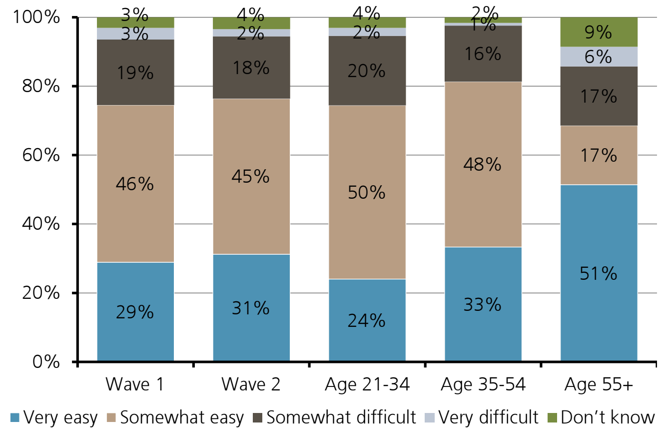
That said, of those respondents ages 21-34 that are planning to buy a residential property in the next 12 months and finance with a mortgage indicated that they have an ~11% downpayment saved on average. While this is encouraging considering the availability of mortgages with as little as 3% down at the FHFA, we would note that 1) this age cohort's view on their ability to get mortgage approval is likely overly optimistic given limited credit history and lower incomes and 2) the majority (approximately 60%) of millennial respondents do not plan to buy a home in the next 12 months, consistent with the first wave of our survey.

Figure 42: Avg. % Saved for Downpayment



Note: Represents respondents who are looking to buy in the next year and would use a mortgage to finance
Source: UBS Evidence Lab

Figure 43: Ease of Mortgage Approval

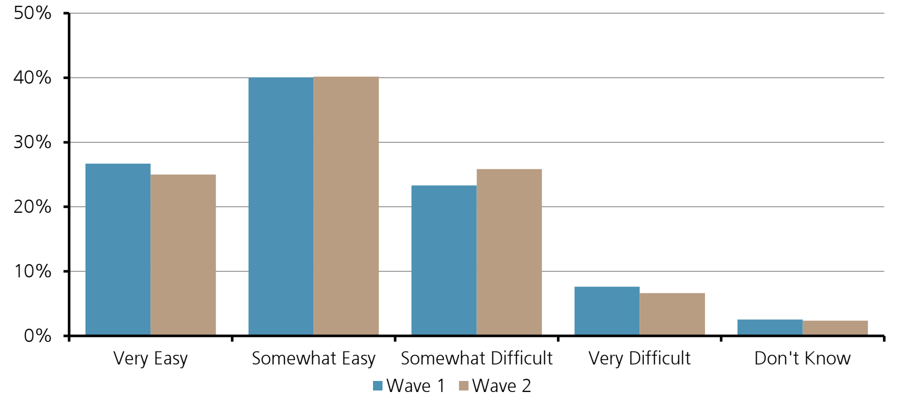


Note: Represents respondents who are looking to buy in the next year and would use a mortgage to finance
Source: UBS Evidence Lab

While the percentage of those surveyed who believe it will be easy/somewhat easy to get approved for a mortgage is roughly unchanged, we were surprised to see an increase in the percentage of respondents who would postpone their buying decision should they have difficulty getting a mortgage. Given this shift in preference from looking to buy a smaller/less expensive home, we are interested to see how the willingness of potential buyers to be flexible in their search changes in future iterations of this survey.

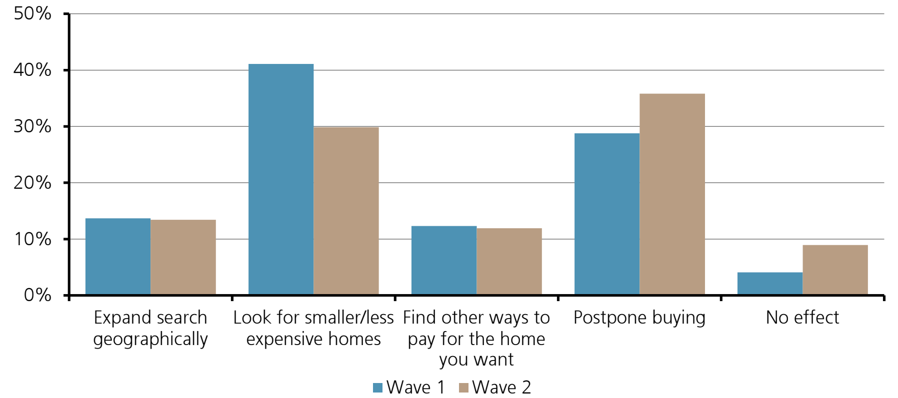
That said, we note that approximately one-third of respondents believe it will be very to somewhat difficult to find a home within their price range. This is encouraging given the level of price increases being realized across many of the country's housing markets and the largest builders' continued interest in achieving greater profitability as opposed to volume growth. This is a bigger issue with millennials, in line with their more limited incomes and financial strength. Over time, as the recovery progresses, we expect new construction to move further to the periphery, where price appreciation will ease, allowing the entry level buyer more opportunity.

Figure 44: How easy do you think it will be to find homes that you like and can afford?



Note: Represents respondents who are currently looking to buy a property or are planning to look for a property to buy in the next 3-12 months.
Source: UBS Evidence Lab

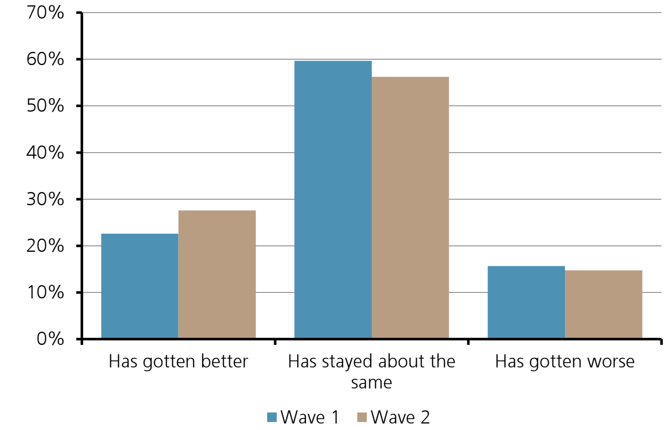
Figure 45: If you have difficulty getting a mortgage, how will it alter your plan?



Note: Represents respondents who 1) said it would be "somewhat difficult" or "very difficult" to get approved for a mortgage or 2) said they have already applied and been rejected for pre-approval
Source: UBS Evidence Lab

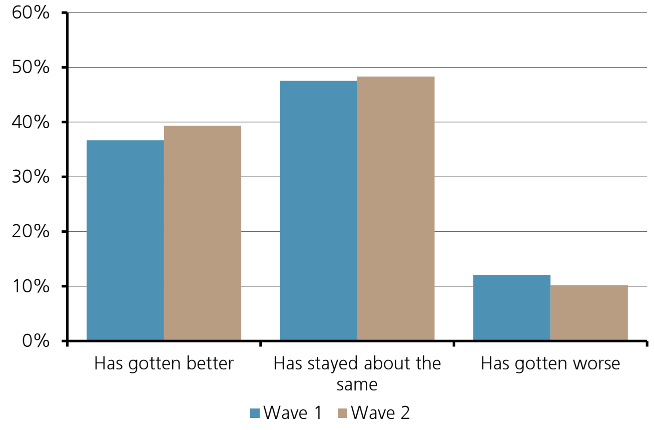
In our view, job growth and wage inflation will be primary factors that enable the housing recovery to move forward. While there was marginal improvement compared to the first wave, the majority of respondents continue to report stagnant wages over the past 6 months.

Figure 46: Over the past 6 months, would you say your household's financial condition…(Total)



Source: UBS Evidence

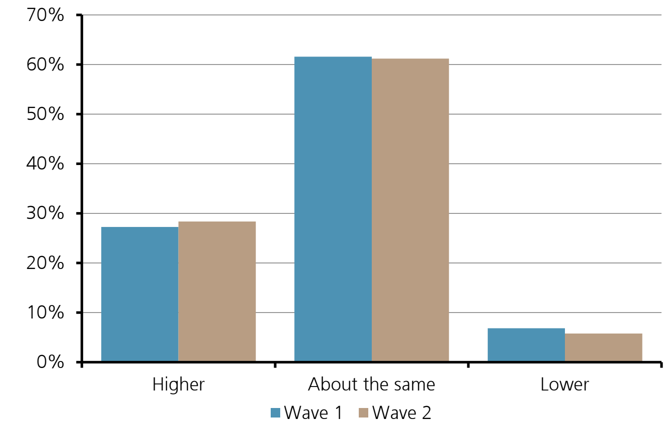
Figure 47: Over the past 6 months, would you say your household's financial condition…(Ages 21-34)



Source: UBS Evidence

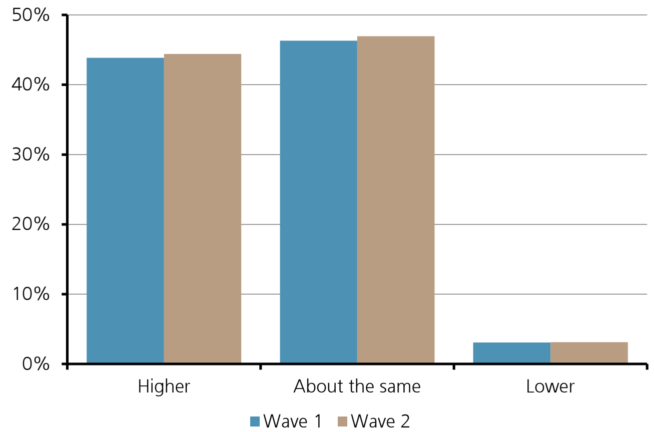
Further, the outlook on financial condition over the next 6 months remains one of caution, with 61% of total respondents expecting their incomes to stay flat versus 28% expecting higher incomes. Millennials are more optimistic about their future financial position.

Figure 48: In 6 months, do you think your household's income will be higher or lower than today? (Total)



Source: UBS Evidence Lab

Figure 49: In 6 months, do you think your household's income will be higher or lower than today? (Ages 21-34)



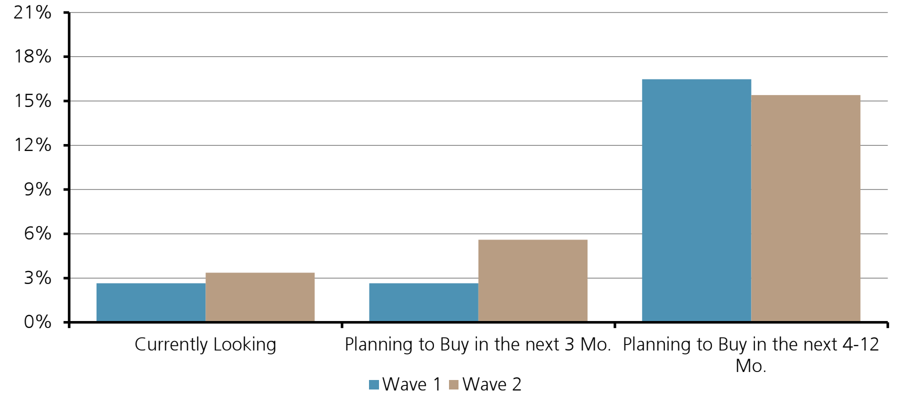
Source: UBS Evidence Lab

Respondents Living With Parents or Relatives

We believe millennials will play an increasingly important role in the next leg of the housing recovery, specifically those who are "doubled up" and will eventually move out. To gain a better understanding of this trend, we surveyed an additional ~240 English-speaking adults currently living with parents, other relatives or friends. The following results are based on the inclusion of this oversample.

Optimism continues to exist among those living at home as 24% plan to buy a house in the next 12 months.

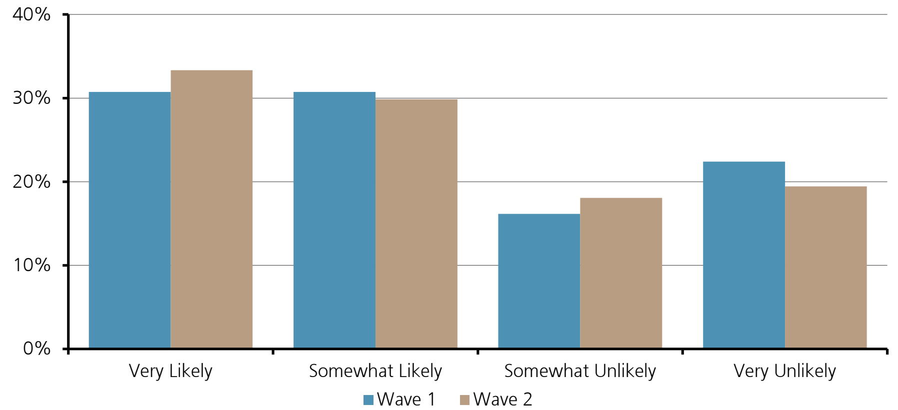
Figure 50: Plans of Those Living at Home to Buy a Residential Property



Source: UBS Evidence Lab

Furthermore, those who do not plan to move out within the year are confident that they will in time. Millennials among this group are especially confident as 77% believe that it is either very or somewhat likely to occur.

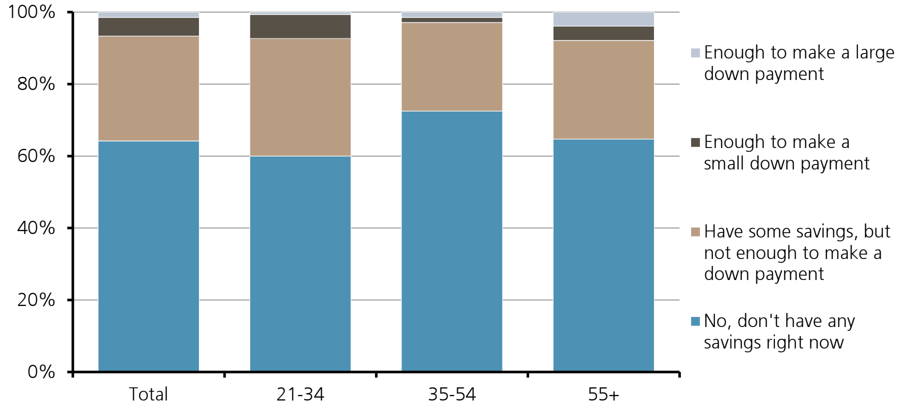
Figure 51: How likely are you to ever move out of parent's/relative's home?



Note: Represents respondents who currently live with parents/relatives and are not planning to buy or rent a home in the next year.
Source: UBS Evidence Lab

That said, the majority of these respondents indicated that they either do not have any savings currently or only a small amount. Additionally, respondents in this group face the burden of student loan debt, with 21-34 year olds and 34-54 year olds holding an outstanding balance of ~$18,000 and ~$23,500 on average, respectively.

Figure 52: Current Savings For Downpayment



Note: Represents respondents who do not plan to buy a home in the next 12 months.
Source: UBS Evidence Lab

While the level of optimism is encouraging to see, we believe that due to the financial constraints many of these people currently face, the path to homeownership will likely take time.

Homebuilding Top Picks

We continue to believe a moderate recovery in housing is unfolding. This reflects the benefits of an improving economic backdrop, mortgage rates that remain historically low, and the government's willingness and commitment to help the industry. More specifically, we look for the market to slowly transition to the next stage of improvement, where activity moves to peripheral locations and encompasses more entry-level buyers. Given these underlying trends, we expect volume growth to accelerate in 2015 (although this will be back-end weighted) and beyond. At the same time, pricing power will be diminished in these areas, reflecting payment sensitivity among these buyers and the less pro-cyclical nature of mortgage markets relative to previous recoveries.

Given this scenario, we would view increased concerns from investors as an opportunity to selectively add exposure to the group. That said, we expect valuations to be range-bound in 2015, much as they have been in the past year. In turn, we recommend focusing on company-specific stories where earnings can grow at an accelerated rate even in a less supportive operating environment. Accordingly, we highlight Buy-rated PHM, RYL, BZH and HOV.

More specifically, we focus on Pulte, our Key Call. Our view considers the following:

(1) **The leverage inherent in Del Webb.** We have been impressed by the improvements already witnessed here and expect them to continue, given favorable underlying demographic trends. Reflecting this, although the sales pace was about 3.2 homes per month in the third quarter, it would have to double to hit the lower bound of a more normal range. Further, Del Webb communities tend to be longer-lived, which will help drive greater margin expansion as price appreciation improves. Finally, we look for neighborhood growth in this segment in 2015, off recent land acquisitions.

(2) **Benefits from Value Creation in operations.** This strategy addresses how to improve the cost and revenue aspects of the homebuilding process. In terms of maximizing revenue, the company has become increasingly focused

on driving greater lot premiums and option revenue and controlling the level of spec construction, while limiting incentives. The strategy also includes efforts made under its Common Plan Management system, which has allowed Pulte to better compare costs across products and geographies. Year-to-date through September 2014, approximately 40% of closings have been from homes that have undergone this process. As an increasing number of divisions adopt these practices, we would look for further gains across metrics, including asset turnover (land and homes) as well as increased profitability from options and land premiums.

(3) **Commitment to maximizing risk-adjusted returns over growth and returning capital to shareholders.** As the recovery has taken shape, Pulte has taken a more balanced approach to capital allocation. As it outlined at its December investor day, the company's priorities for cash and investments are: 1) invest in order to support and grow its position within local markets; 2) support an increase in the dividend (it is ultimately targeting a 2-3% dividend yield); 3) pursue advantageous acquisitions; and 4) return remaining cash to shareholders through repurchases. In line with this, it announced a $750 million authorization in October and we look for a relatively consistent pace of approximately $100 million per quarter for the foreseeable future.

Hardline Retail

Gaining Insight into the Home Improvement Cycle

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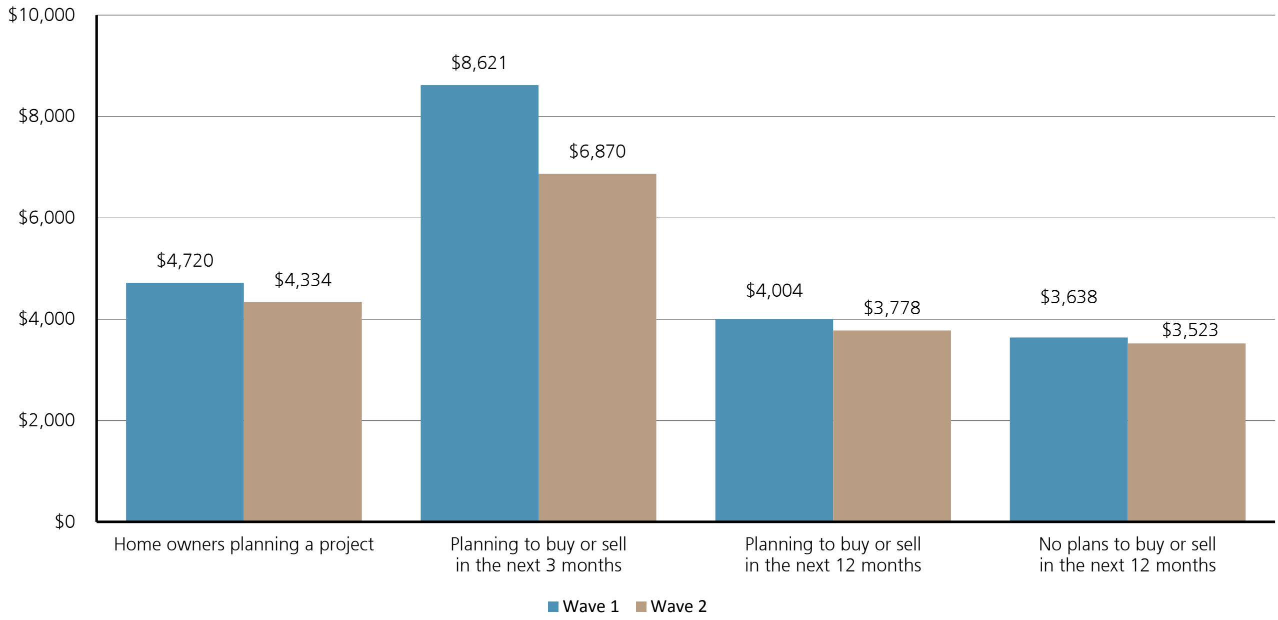
The home improvement retailers have been the beneficiaries in recent years as consumers re-engage with this category. In particular, Home Depot and Lowe's have both trended positively as the home improvement cycle continues to unfold. Our UBS Housing Intentions Survey gathered an immense amount of data which supports the notion that the home improvement cycle still stands to gain as more than half of homeowners expect to do a home improvement project over the next three months. We note that since the previous iteration of our survey published in January, there is a slightly greater percentage of homeowners surveyed who indicated that they plan on doing a home improvement project within the next three months (53% vs 47% in our previous survey).

On average, those who are planning a project within the next three months expect to spend $4,334 on materials and labor. This compares with the $4,720 amount from the 4Q'14 edition of our survey. While this metric is down from the previous iteration of our survey, we will get a better read on the impact of seasonality as we anniversary the baseline metrics of the survey.

Also, we wanted to size the difference between homeowner and renter home improvement spending intentions. We found that while renters intend to spend materially less than homeowners on home improvement projects, the average renter still intends to spend $2,627 over the next three months.

One item of note from a category specific perspective is that 17% of the respondents indicated that they planned to replace or add major appliances as one of their projects over the next four to twelve months. This compares to 15% of the respondents in our previous survey. The survey shows that the composition of those who expect to complete a home improvement project is diverse across geographies, age ranges, and socio-income demographics. The leading home improvement retailers should be prime beneficiaries of this intended spending, as they were cited more often than not as the locations to source materials for these projects. In particular, HD stood out. It was cited 54% more often than LOW as the retailer where most of the materials would be purchased.

Figure 53: How much do homeowners expect to spend on their home improvement projects (materials and labor)?



Source: UBS Evidence Lab

This survey was completed in partnership with the UBS Evidence Lab and is part of a broader study on housing intentions. As part of the survey, over 2,000 English-speaking adults were asked questions about their overall views on housing. From this population, approximately 1,400 identified themselves as homeowners and were further queried on their anticipated home improvement projects. Within this subset, ~750 homeowners expected to perform a home improvement project in the next 3 months. It is from this group that we derive home improvement spending intentions.

Our first iteration of our survey was published in January of this year. As this survey is repeated on a regular basis, it will provide an extensive look at the breadth and scope of home improvement spending. Just as importantly, it should shed light on why these expenditures are being made. As we see it, this will help determine the shape and length of the cycle.

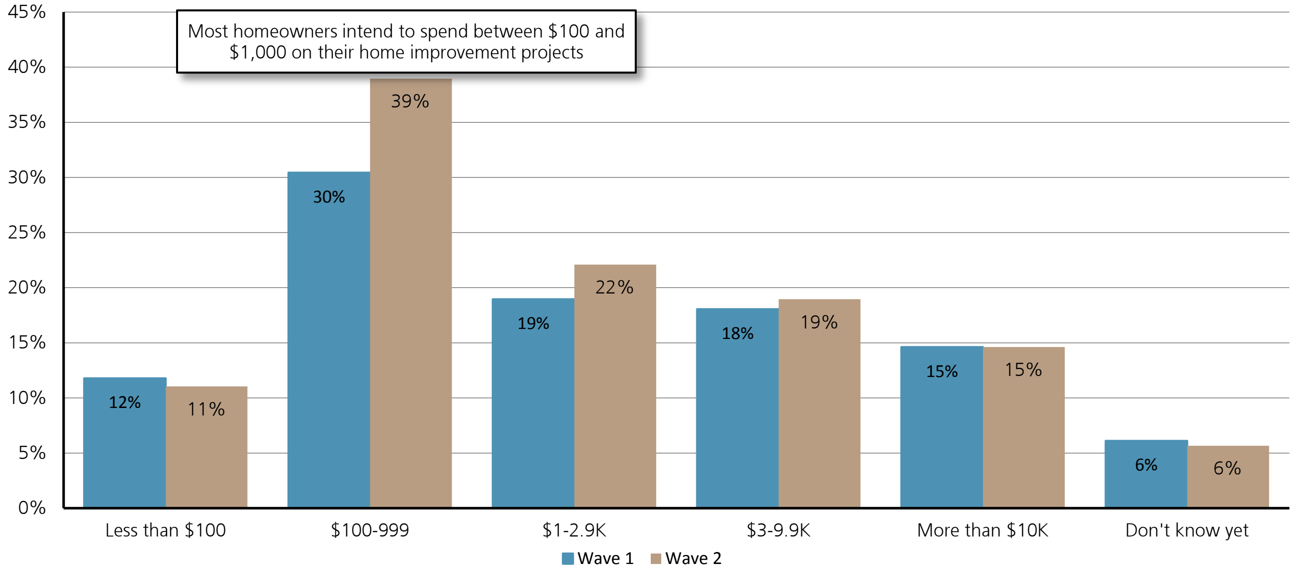
What Drives Higher Home Improvement Spending?

Before answering this question, we must understand how much homeowners are spending on their home improvement projects and the composition of homeowners. First, we asked homeowners if they had plans to perform a project in the next three months. Further, from the population that answered yes to this question, we asked how much they were planning to spend on materials and labor. From there, we drilled into characteristics.

On average, those who are planning a project within the next three months expect to spend $4,334 on materials and labor. The most common response from those surveyed was in the $100-$1,000 bucket, representing 39% of those homeowners with an imminent project. When including renters into this metric, the average intended spend on materials and labor declines to $4,083 and 39% of respondents planning a project within the next three months expect to spend within the $100-$1,000 bucket. Interestingly, there is not as huge a gap between those planning projects in the $1,000 and $3,000 cost range, the $3,000 and

$10,000 cost range, and those costing more than $10,000. However, 50% of homeowners are planning projects that cost under $1,000, whereas 42% of homeowners expect to do a project costing under $1,000 in the previous edition of our survey.

Figure 54: For those planning on a project in the next 3 months, how much are you likely to spend on these projects in total, including materials and labor?

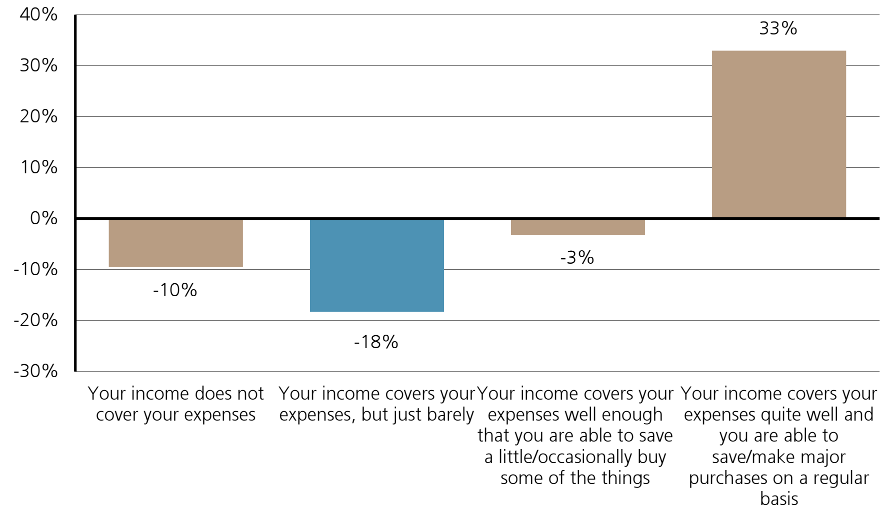


Source: UBS Evidence Lab

Notably, in these kinds of surveys, respondents have a tendency to overstate expected spending on an annualized basis. As we develop a time series of data, we will be able to better understand the gap between intended and actual spending. In the meantime, we can dig in on the demographics of the homeowners, their financial condition, and the characteristics of the home that they own.

First, we looked at how the homeowners' income levels affected their home improvement intentions. Recall that 53% of homeowners plan to do a home improvement project in the next 3 months and plan on spending an average of $4,334 on materials and labor. When examining the difference in home improvement project spending relative to expenses between homeowners of different income levels, we noticed that those whose income 'just barely covers their expenses' believed they would spend approximately -18% less than average on home improvement projects in the next three months. This compares to those whose income covers their expenses 'quite well and are able to save or make major purchases on a regular basis,' who indicated they would spend 33% more than average on home improvement projects in the next three months.

Figure 55: Homeowner HI spending intentions by income level versus average

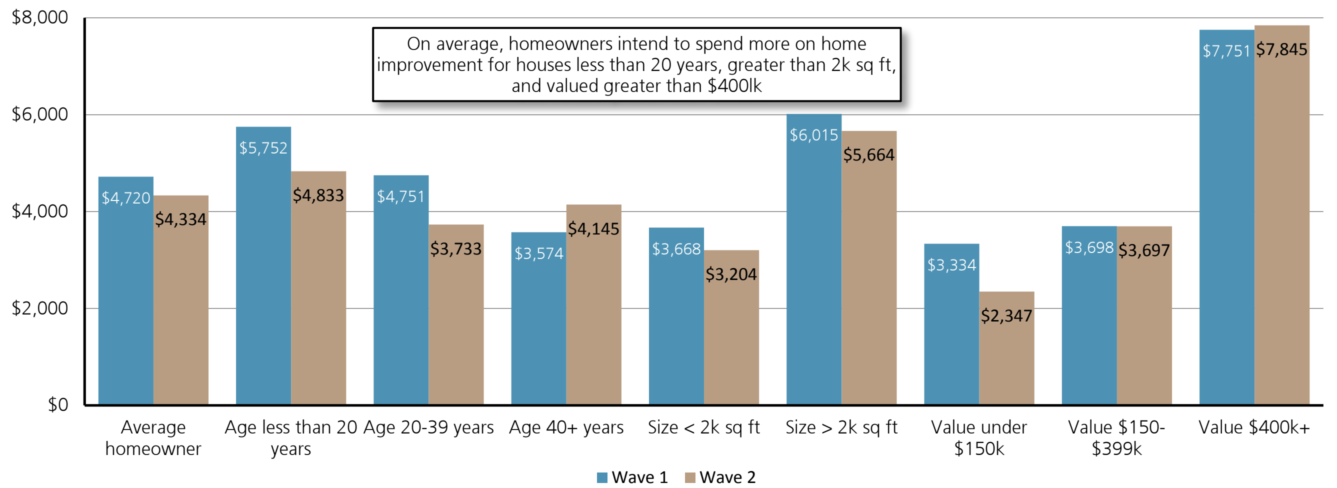


Source: UBS Evidence Lab, UBS estimates

Further, we examine how home characteristics impact homeowner spending. Respondents indicated that those with houses less than 20 years old expected to spend almost 12% more than average. Likewise, homeowners living in homes older than 40 years old anticipated spending -4% less on their home improvement projects.

Further, those living in homes in excess of 2k square feet indicated that they would spend $5,664 on their projects, or 31% more than average (27% more than average in the previous iteration of our survey). Finally, there was a clear disparity on anticipated home improvement spending based on the value of the home. In particular, homeowners living in homes with values in excess of $400k expected to spend $7,845 on home improvement, or 81% more than average, which is a greater percentage increase than in our previous survey.

Figure 56: For those planning on a project in the next 3 months, how much are you likely to spend on these projects in total, including materials and labor, depending on home characteristics?



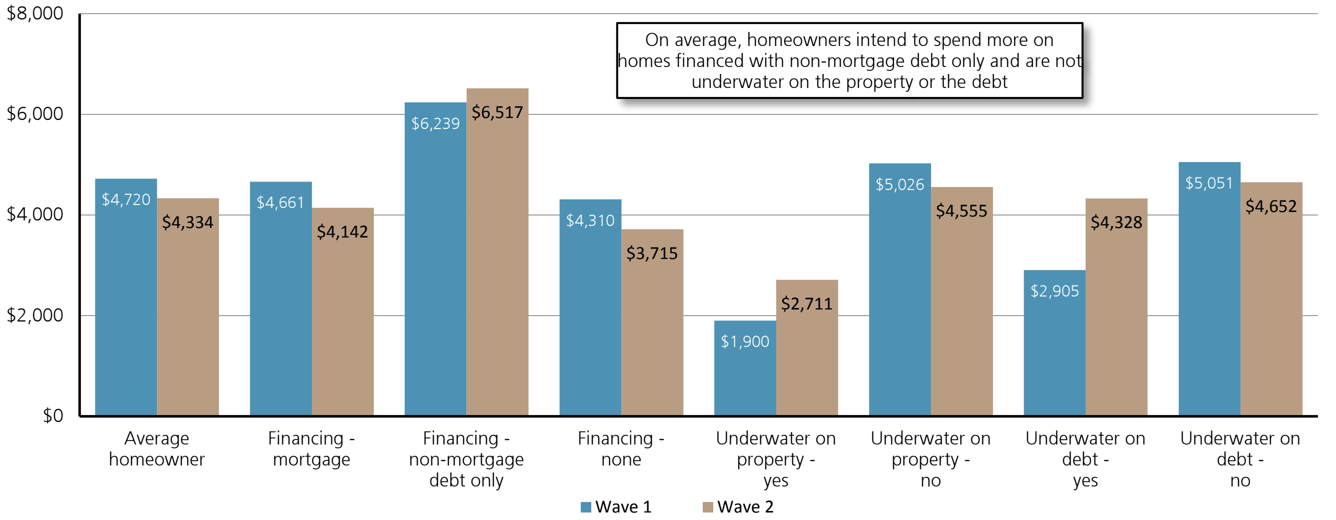
Source: UBS Evidence Lab

This is likely due to the lower average dollar spend by homeowners in this edition. To the contrary, projects at homes valued under $150k and those between $150k to $399k were -46% and -15% below the average, respectively. In essence, there is increased home improvement spending on homes under 20 years old, homes that are larger than 2k square feet, and homes with a value greater than $400k.

In addition, we looked at how the financial condition and situation of homeowners impacted their home improvement spending. Notably, homeowners underwater on their properties intended to spend $2,711 (including materials and labor) on home improvement projects, or -37% less than the average project spending. This is materially smaller than the -60% gap from the average project spending during the last iteration of our survey.

Also, homeowners underwater on debt planned on spending $4,328 on home improvement projects, which is in line with the average homeowner spending intentions and much less than the prior spending gap in the category of -38% below average.

Figure 57: For those planning on a project in the next 3 months, how much are you likely to spend on these projects in total, including materials and labor, depending on financial characteristics?



Source: UBS Evidence Lab

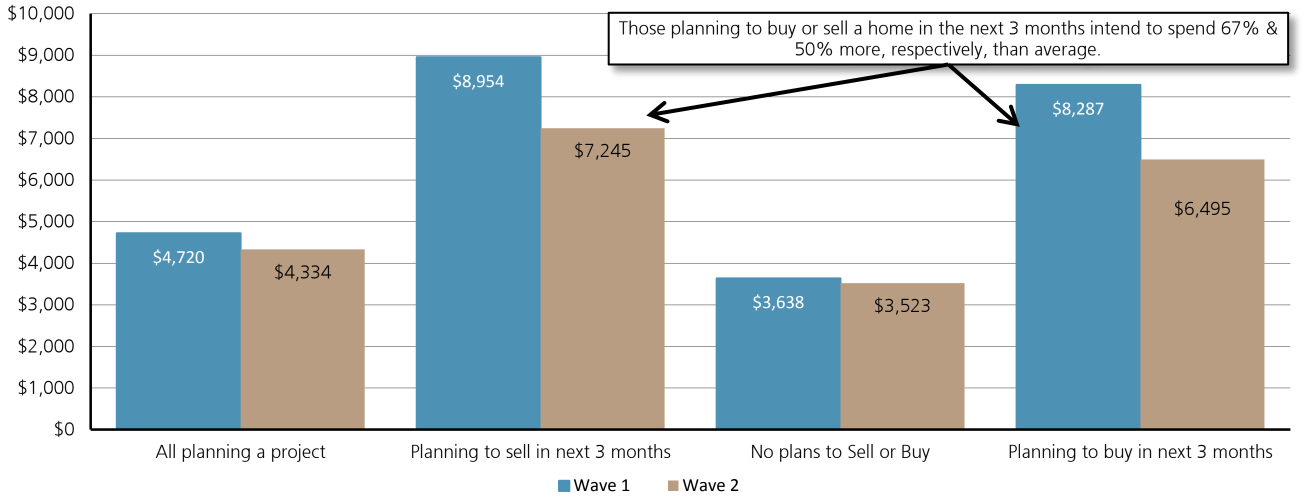
We believe this highlights the importance of the home price appreciation for Home Depot, Lowe's, and other home improvement retailers. Keeping homeowners above water directly impacts their intentions to spend. Further, the narrower gap between average spending intentions and those underwater on their property or debt may reflect recognition by consumers that spending on home improvement projects may be a suitable way to increase the value of their home and their overall net worth.

Furthermore, we studied the impact of homeowner intentions to buy or sell their homes on home improvement spending. The results indicate that homeowners that plan to sell within the next three months expect to spend $7,245 on home improvement projects (including materials and labor), or 67% more than average. This is a narrower gap than the 90% difference in average spend from the previous iteration of our survey. Further, those intending to buy a home within the next three months plan on spending $6,495 on projects, or 50% more than average, which is also a much more narrow gap from the previous iteration of our

survey. Those with no intention to sell or buy anticipate spending -14% and -24% less than average, respectively.

Overall, we think these results illustrate the benefit that housing turnover has on home improvement retailers. Those intending to buy or sell spend about twice as much on projects than those without intentions to buy or sell.

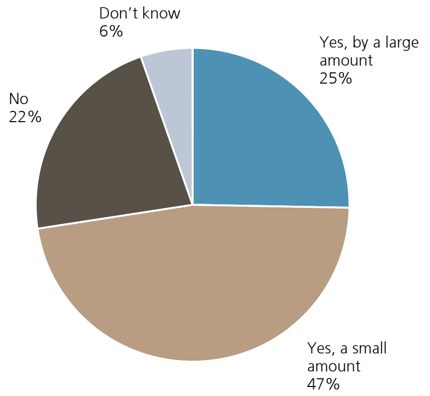
Figure 58: For those planning on a project in the next 3 months, how much are you likely to spend on these projects in total, including materials and labor, depending on intention to buy or sell?



Source: UBS Evidence Lab

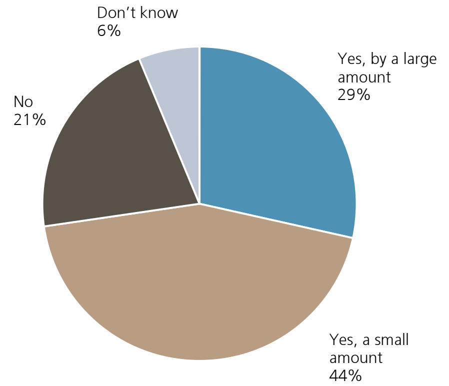
Not surprisingly, homeowners generally view their home improvement projects as investments. In particular, 73% of respondents indicated they believe their home improvement project would add value to their home. Further, 25% believe they will add a large amount of value. These results were pretty much in line with the previous iteration of our survey.

Figure 59: Do you expect the projects you're doing in the next 3 months will add to the value of your home? (Wave 2)



Source: UBS Evidence Lab

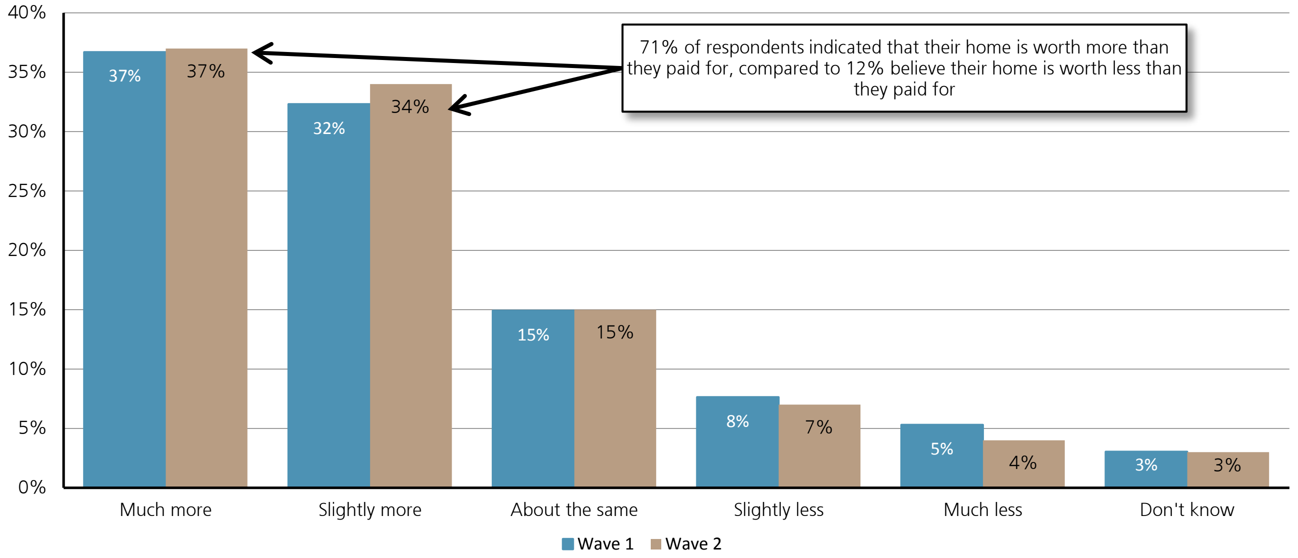
Figure 60: Do you expect the projects you're doing in the next 3 months will add to the value of your home? (Wave 1)



Source: UBS Evidence Lab

Overall, 71% of homeowners indicated that their home is worth more than what they paid for it. This is slightly greater than the 69% of homeowners that made the same indication in the previous edition of our survey. As we revealed earlier, home appreciation is an important contributor to home improvement sales.

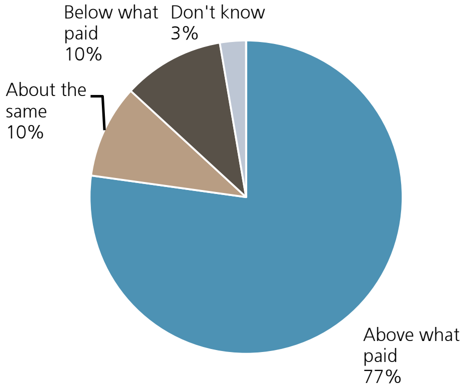
Figure 61: Is your home worth more or less than what you paid for it?



Source: UBS Evidence Lab

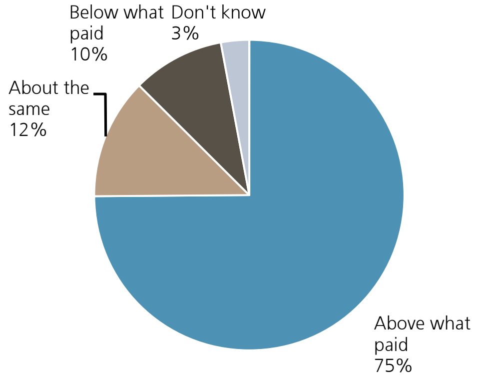
These results indicate that while a strong percentage of homeowners have seen their home prices appreciate since their purchases, a number have homes that are still valued below what they paid for them or the debt owed on them. As prices appreciate, owners should be more likely to invest in their home.

Figure 62: Is your home worth more or less than the amount of debt you still owe on it? (Wave 2)



Source: UBS Evidence Lab

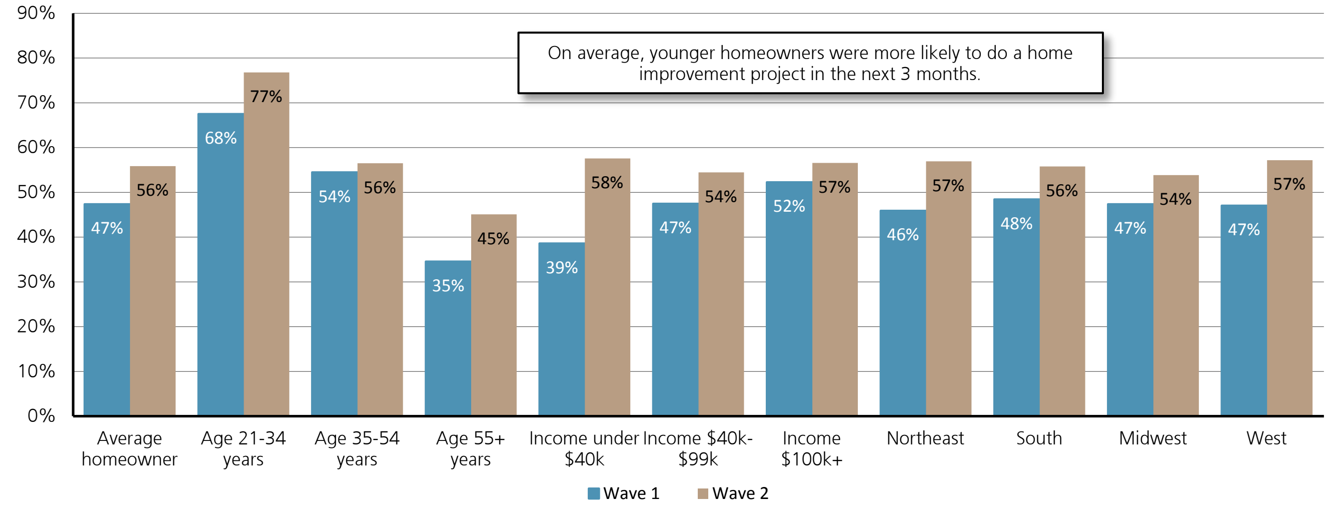
Figure 63: Is your home worth more or less than the amount of debt you still owe on it? (Wave 1)



Source: UBS Evidence Lab

Approximately 56% of homeowners indicated they intended to perform a home improvement project in the next three months. Younger homeowners were more likely to expect a project by 21% than the average homeowner, while those over the age of 55 were 12% less likely than average.

Figure 64: Are you planning to do any projects on your home? (homeowner characteristics)

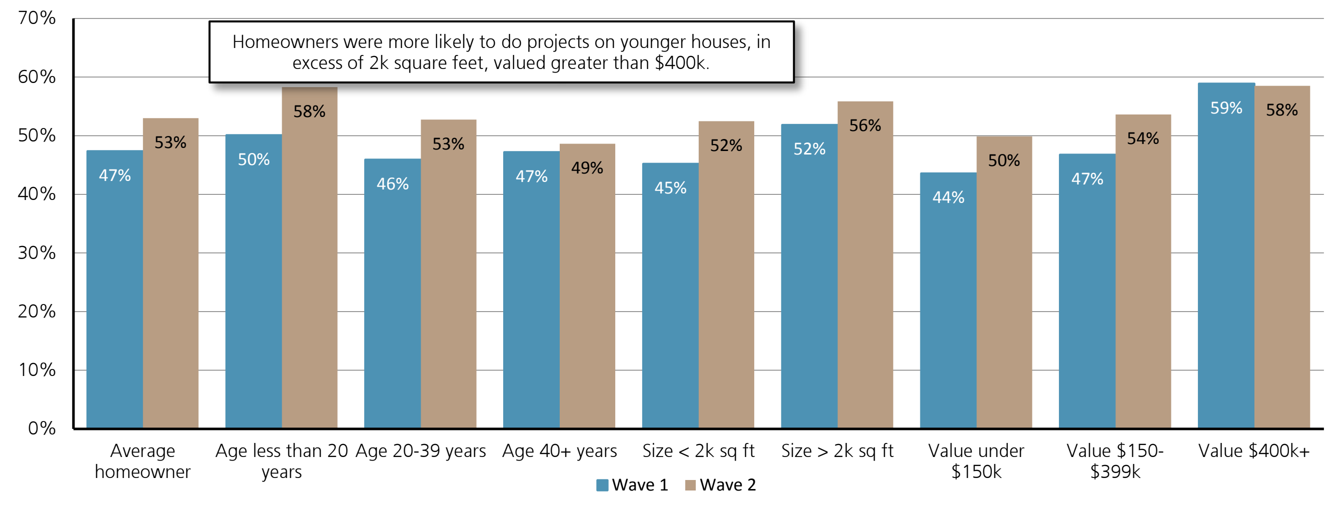


Source: UBS Evidence Lab

The results in regional and age categories were directionally aligned with the previous iteration of our survey. However, the income skews in this iteration of our survey did not show a substantial preference for home improvement intentions, while there was more income bias in the previous iteration of our survey.

When considering the characteristics of the actual home the projects would be performed on, homeowners are most likely to do projects on homes valued in excess of $400k and homes bigger than 2k square feet. While there was a little less variability in the habits of homeowners based on the age of the home, homes under 20 years old were the most likely to have projects planned in the next three months.

Figure 65: Are you planning to do any projects on your home? (home characteristics)



Source: UBS Evidence Lab

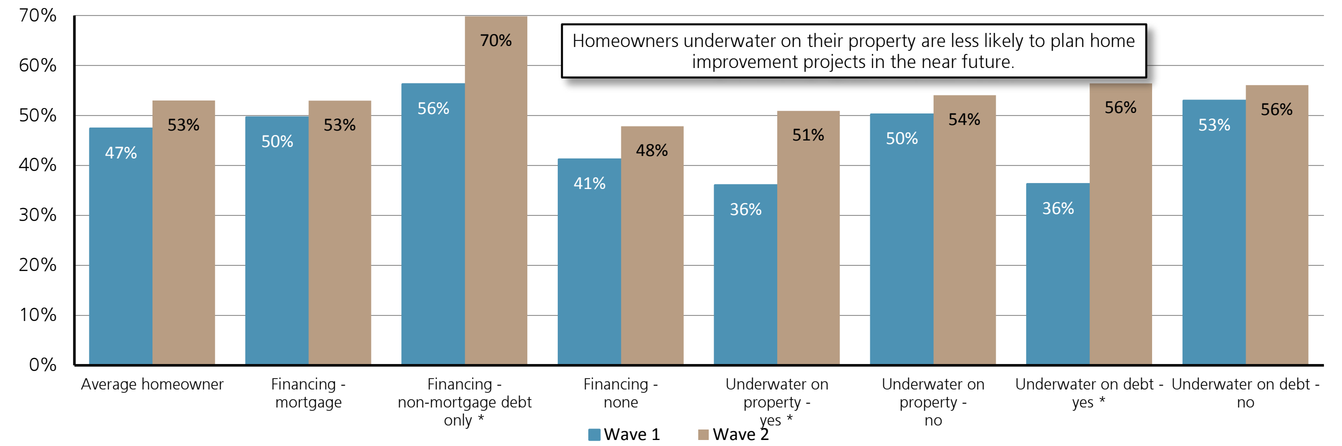
Compared to our last survey, the results in this iteration of our survey reflect greater home improvement project participation in houses aged 20 years or more as well as in houses under $400k in value.

Homeowners who financed their homes through non-mortgage debt only were the most likely to plan on home improvement projects, although the sample size is

small. Likewise, homeowners who are underwater either on their property are less likely to conduct a home improvement project in the next three months.

However, compared to the results of our pervious iteration of the survey, homeowners who are underwater on their property are more likely to do a home improvement project.

Figure 66: Are you planning to do any projects on your home? (financial characteristics)

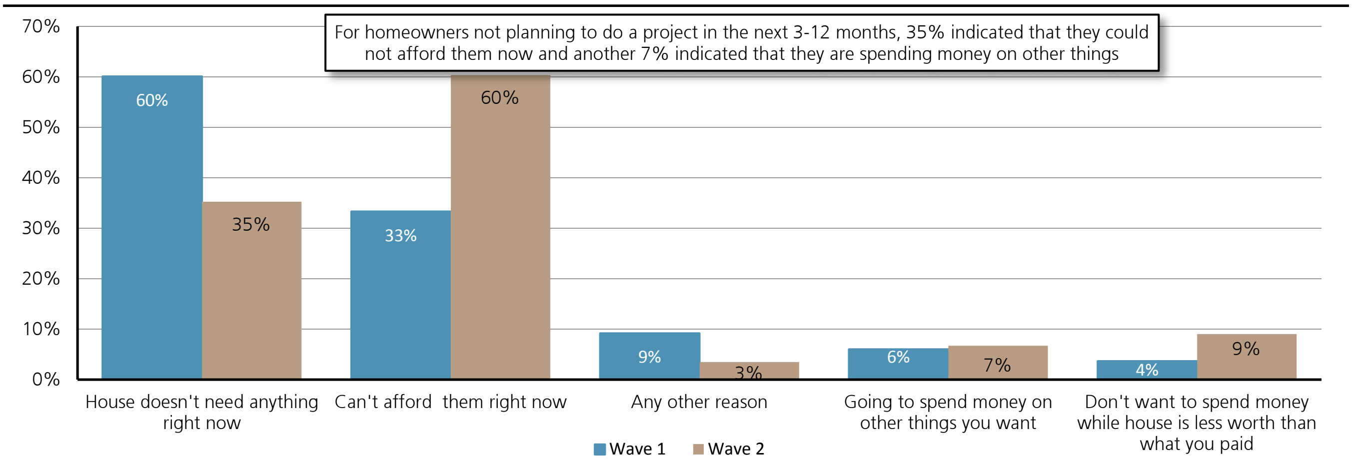


Note: Categories designated with * have a smaller base size.
Source: UBS Evidence Lab

Taking a look from an opposing view, we asked those who indicated they did not have any home improvement projects planned in the next 12 months why they do not intend to do so.

In the previous iteration of our survey, an overwhelming majority indicated their homes did not need anything at the moment. However, the majority of respondents (60%) in this iteration of our survey said that affordability was the primary reason. This compares to 33% of respondents indicating that they couldn't afford the projects right now in the previous iteration of our survey.

Figure 67: Why are you not planning to do any home improvement projects in the next 12 months?



Source: UBS Evidence Lab

Separately, 7% indicated they were going to spend money on other things that they want. This should be something to watch. If the economy shows material

improvement, it could spark acceleration in home improvement for homeowners in this bucket. Another 9% indicated that they did not want to invest in a home worth less than what they paid. This small but meaningful portion of the population could look to initiate home improvement projects should home prices appreciate meaningfully.

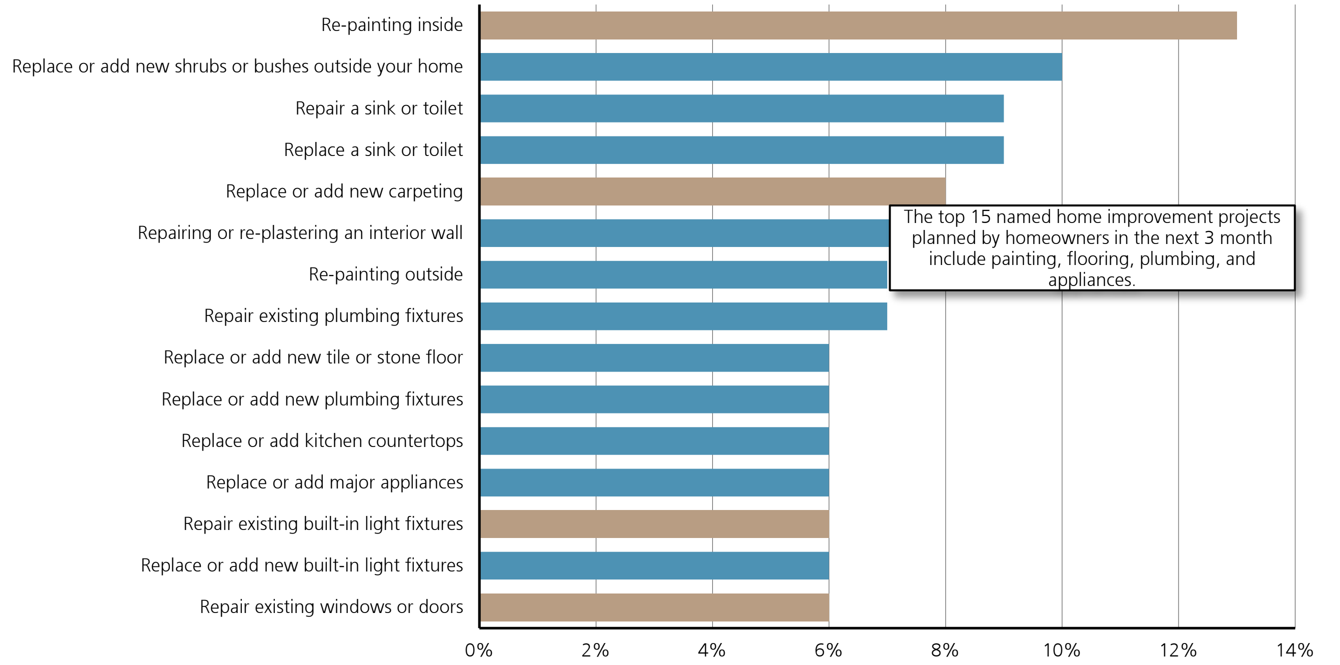
What Projects Are on the Agendas of Homeowners?

Shoppers visit home improvement retailers to purchase materials for a number of different projects. To better understand what projects are on the minds of homeowners, we asked them "are you planning to do any of the following to your home in the next three months?" and listed a number of projects.

From our sample of 1,408 homeowners, 13% indicated they would re-paint on the inside of their home, with 7% planning to re-paint outside. Another popular upcoming project was related to sinks and toilets. Specifically, 9% of respondents indicated they were planning to replace a sink or toilet, with another 9% planning to repair a sink or toilet. These results were broadly aligned with the previous iteration of our survey, suggesting that the homeowners surveyed have fairly consistent intentions for home improvement projects over the next few months.

Notably, appliances were a popular category for home improvement projects. In particular, 6% of those surveyed indicated they intend to replace or add major appliances, with another 4% revealing that they planned to repair existing major appliances.

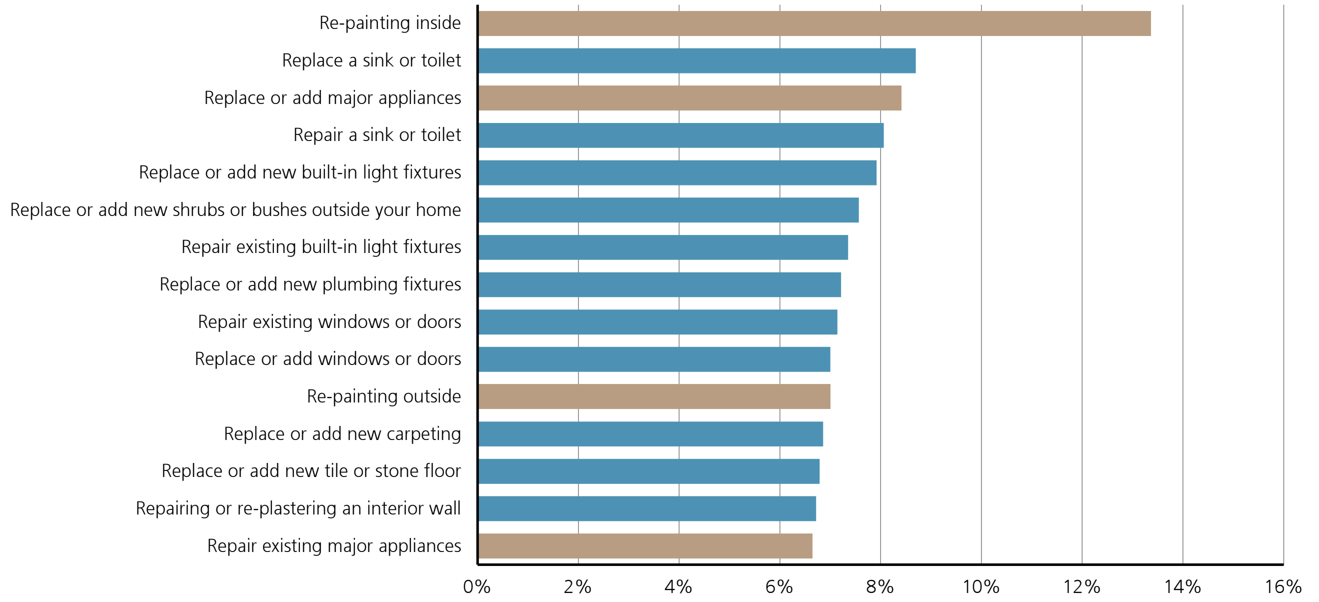
Figure 68: Are you planning to do any of the following to your home in the next 3 months? (Wave 2)



Source: UBS Evidence Lab

Notably, replacing or adding major appliances fell in ranking from its third place position in the previous iteration of our survey. At the same time, categories such as replacing new shrubs or bushes, and adding a new carpet rose in ranking between surveys.

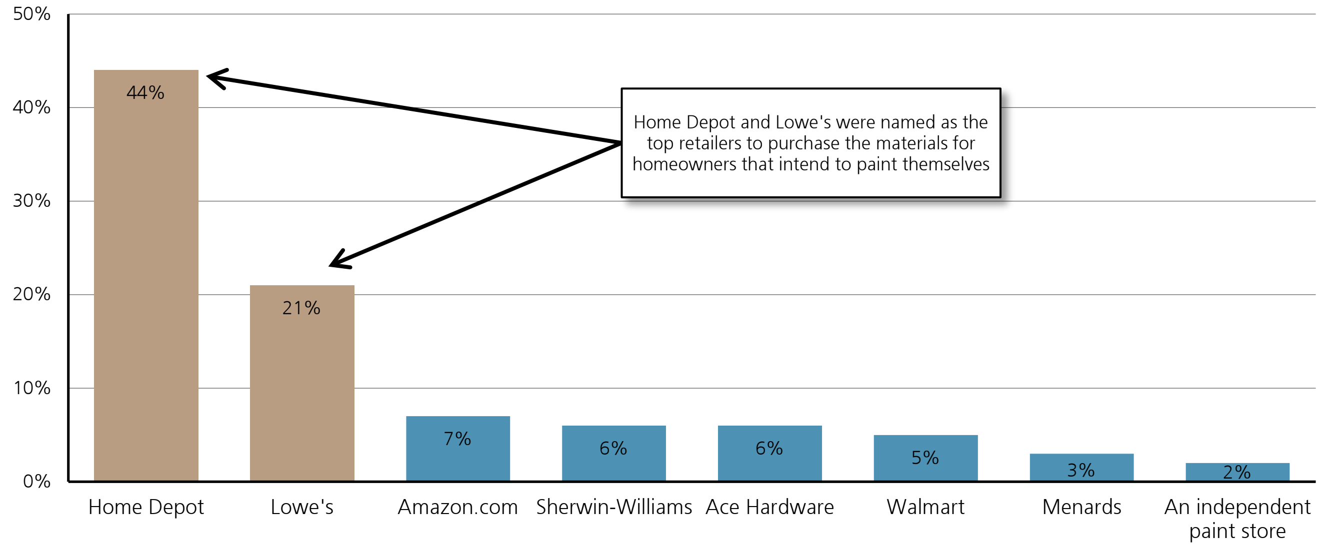
Figure 69: Are you planning to do any of the following to your home in the next 3 months? (Wave 1)



Source: UBS Evidence Lab

As indoor painting was the most common home improvement project noted by respondents, and painting outside another popular response, we dug in to see where shoppers intended to purchase materials for this project. Notably, both Home Depot and Lowe's were the top two retailers of choice for buying paint. Further, 68% of the respondents who planned to repaint indoors planned to do so themselves while 17% of respondents will depend entirely on a hired professional to do the entire job.

Figure 70: For those indicating that they were doing painting projects themselves, where are you most likely to purchase the paint?



Source: UBS Evidence Lab

One category that has gained attention at the home improvement retailers is appliances. In particular, the competition for this category has picked up, as HD and LOW, as well as BBY, attempt to draw share away from SHLD. Overall, 6% of

homeowners intending to do a project in the next three months indicated they would replace or add major appliances.

Interestingly, 17% of homeowners between the ages of 21 and 34 who expect a project in the next three months intend to replace or add major appliances, compared to 7% from the 25 to 54 year old age group and 3% in the 55+ age bracket. Perhaps most surprisingly, the size of the home did not have a huge impact on the demand for appliances. Specifically, there was only a 100 bp difference from the 7% in houses in excess of 2k square feet who planned on installing appliances and the 6% in houses less than 2k square feet.

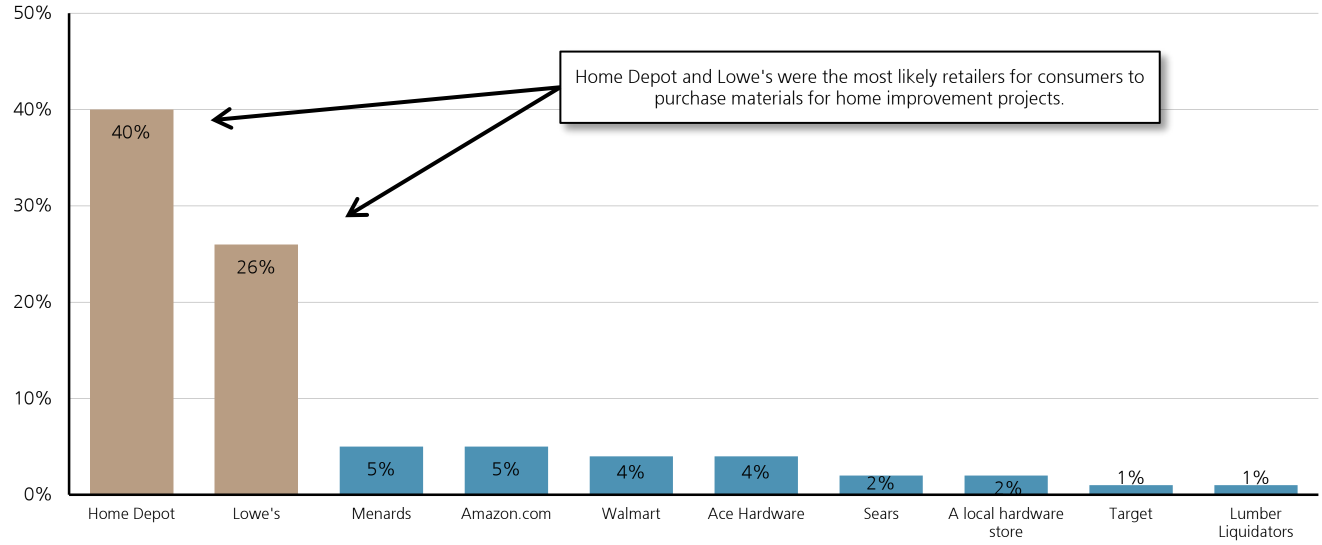
Kitchen is the largest product category at Home Depot with $8,403 million in sales, accounting for 10.1% of sales in FY'14. Approximately 5% of homeowners indicated that they would replace or add kitchen cabinets in the next 3 months. Further, another 4% revealed that they would repair their kitchen cabinets within the same time frame. These results are consistent with the previous edition of our survey. In addition, 6% of homeowners noted that they would replace or add kitchen countertops in the next 3 months, while another 4% specified that they would repair their countertops.

Flooring is another category that represents a sizable percentage of sales at home improvement retailers, with 7.2% of HD's sales in FY'14 coming from the segment. Nearly 5% of homeowners surveyed indicated that they were expecting to replace or add a new wood floor. Further, 6% of homeowners indicated that they intended on replacing or adding a new tile or stone floor in the next three months.

Which Retailer Is Best Positioned to Capture These Sales?

Approximately 66% of survey respondents who intended to complete a project themselves indicated Home Depot and Lowe's were where they would purchase materials. This is broadly in line with the results from our previous survey. Notably, these two retailers have comprised roughly 40% of the category's US Census Bureau Retail sales in recent quarters. Home Depot and Lowe's dominated the responses, as all other retailers received 5% or less consideration. These results highlight the strength of the market position that these companies have in the industry.

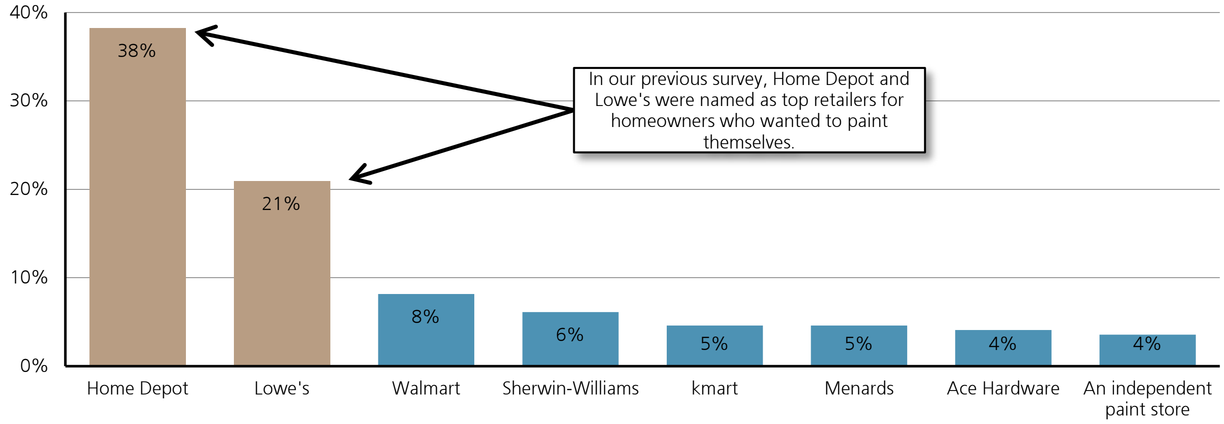
Figure 71: Where are you most likely to purchase most of the materials for the projects you intend to do yourself? (Wave 2)



Source: UBS Evidence Lab

Notably, Amazon.com made its first appearance during this iteration of our survey with a 5% consideration. It will be interesting to see how the online retailer is considered through future iterations of this survey and how brick and mortar retailers will strengthen their online presence down the road. In the last iteration of our survey, Walmart and Sherwin-Williams were the next most popular retailers chosen by respondents after HD and LOW.

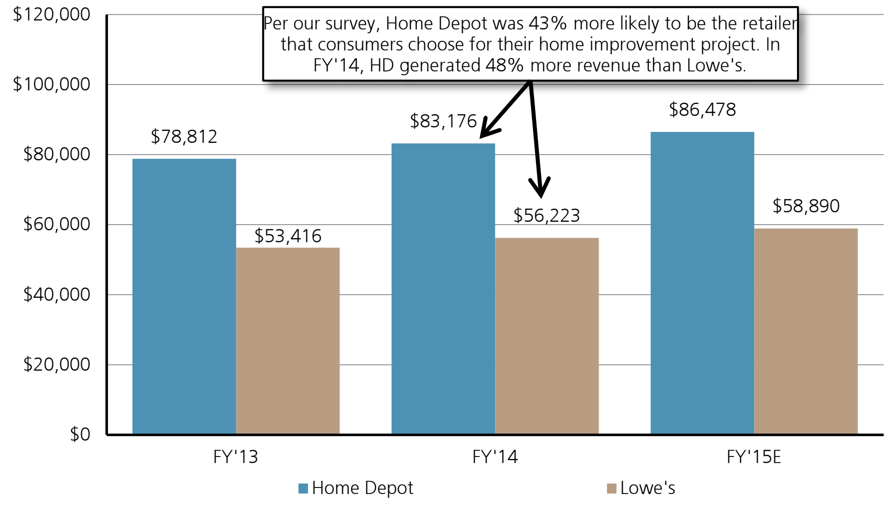
Figure 72: For those indicating that they were doing painting projects themselves, where are you most likely to purchase the paint? (Wave 1)



Source: UBS Evidence Lab

We compared our survey respondents' preferences to Home Depot and Lowe's actual sales figures to examine the difference between intentions and actual spending habits. In this iteration of our survey, the disparity between homeowner spending intentions and the sales results at Home Depot and Lowe's has narrowed as 43% more respondents indicated they would purchase their materials at Home Depot over Lowe's while Home Depot's sales in FY'14 were 48% greater than Lowe's. In the previous iteration of our survey, the gap was much wider, with 65% more respondents indicating they would purchase their materials at Home Depot over Lowe's.

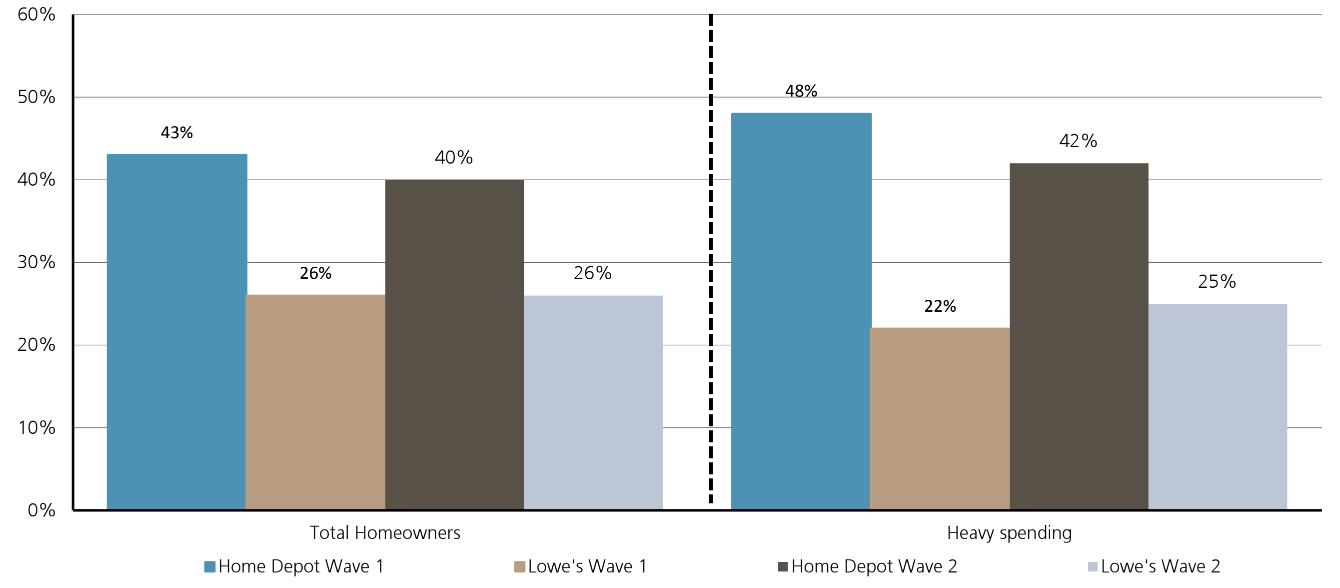
Figure 73: HD and LOW Sales, FY13-FY15E



Source: Company reports, UBS estimates

In addition, we looked at how the spending of the project would affect the retailer chosen. Respondents indicated that the more expensive the project, the more likely they were to choose Home Depot to make their purchases. Inversely, respondents signified that for projects that require lighter overall spending, they were more likely to make the purchase at Lowe's than Home Depot. These results were pretty much in line with the previous iteration of our survey.

Figure 74: Where are you most likely to purchase most of the materials for the projects you intend to do yourself, by amount of spend?

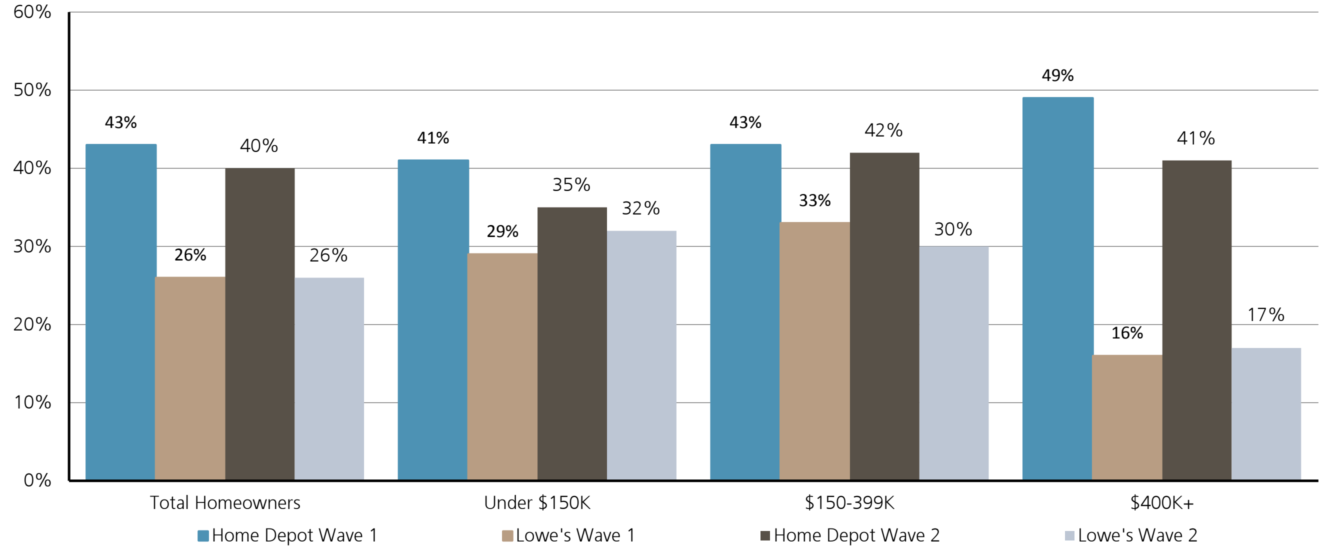


Source: UBS Evidence Lab

Further, we also look at the cost of the consumer's home and how that affects their choice of home improvement retailer. The data shows a material pickup in the likelihood of purchasing intentions at Home Depot from homeowners whose home value was above the $150k level. At the same time, homeowners' intention on purchasing materials from Lowe's began to decline above the $150k mark. The disparity between the two retailers was largest among homeowners whose home

value was above the $400k level with 40% indicating intentions to make their purchases at Home Depot as opposed to 17% at Lowe's. In the previous edition of our survey, there was a larger gap between HD and LOW from homeowners whose homes were under $150k in value. Otherwise, the results from our latest survey were similar to the previous iteration of our housing intentions survey, giving further support to the consistency of these intentions.

Figure 75: Where are you most likely to purchase most of the materials for the projects you intend to do yourself, by value of home?



Source: UBS Evidence Lab

We think that **Home Depot (HD)** and **Lowe's (LOW)** are poised to appreciate, with a conducive macro environment featuring expected ~3% GDP growth, rising home prices, and increasing wages all working in their favor. Further, Home Depot has developed one of the best supply chains in the industry, which, combined with premium store locations, should allow it take advantage of improving conditions. Home Depot management has commented that many of its selling categories have not reached the peak sales level experienced during the housing boom, reinforcing the view that it has more room to run. Further, in the past couple of years LOW has invested in initiatives related to merchandising, store layout, and omni-channel, which continue to benefit the company. We have Buy ratings on both HD and LOW. For HD, our $129 price target equates to 21.5x our CY'16 EPS estimate and is based on a DCF/multiple blend analysis. For LOW, our $83 price target equates to 21.4x our CY'16 EPS estimate and is based on a DCF/multiple blend analysis.

Survey Methodology Detail

UBS Evidence Lab conducted a survey among 2,090 adults age 21+ who live in the US. The main sample was recruited and weighted to be representative of the English-speaking population on age, gender, income, Census region, race, and Hispanic origin. In addition, we collected responses from an extra ~240 English-speaking respondents who currently live with parents, relatives or friends. All of the surveys were fielded using an Internet methodology from February 2-17, 2015. Conclusions based on the total representative sample of adults have a potential sampling error of 1.8 percentage points, at a 90% confidence level.

We'd note that differences between findings of wave 1 and wave 2 could also be driven by sampling differences and seasonality. As further waves of this survey are conducted, it would establish a more robust database to assess difference based on random variations versus those driven by seasonality or other factors.

Statement of Risk

Homebuilders: The primary risk facing homebuilders currently is that recent improvements slow or reverse, driven by: 1) a weaker macroeconomic backdrop and related lower level of job creation; or 2) the impact of recent increases in mortgage rates. Additional risks include increased costs for land, labor or materials and the potential for the more limited availability of mortgage financing to negatively impact demand.

Hardline Retail: Investing in retail stocks entails certain risks, including but not limited to, changes in consumer spending and its components, retail industry competition and general market risk.

Multifamily REITs: REITs continue to be exposed the cost and availability of capital. If economic and job growth accelerates faster and/or earlier than expected, property level fundamentals could exceed our forecasts, leading to higher than expected earnings. Conversely, if the economy and service sector job market continue to deteriorate, earnings could be at risk.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	45%	37%
Neutral	FSR is between -6% and 6% of the MRA.	43%	33%
Sell	FSR is > 6% below the MRA.	12%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	less than 1%	less than 1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	less than 1%	less than 1%

Source: UBS. Rating allocations are as of 31 March 2015.
1:Percentage of companies under coverage globally within the 12-month rating category. 2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
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UBS Securities LLC: Nick Yulico, CFA; Ross T. Nussbaum; Susan Maklari; Michael Lasser.

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Apartment Investment & Management Comp.[16]	AIV.N	Buy	N/A	US$38.78	07 Apr 2015
AvalonBay Communities, Inc.[2, 4, 6, 16]	AVB.N	Buy	N/A	US$172.59	07 Apr 2015
Beazer Homes[4, 6, 16, 20]	BZH.N	Buy (CBE)	N/A	US$17.85	07 Apr 2015
Camden Property Trust[16]	CPT.N	Neutral	N/A	US$78.50	07 Apr 2015
Equity Residential[2, 4, 6, 16]	EQR.N	Buy	N/A	US$77.70	07 Apr 2015
Essex Property Trust, Inc.[1, 2, 4, 6, 8, 16]	ESS.N	Neutral	N/A	US$227.18	07 Apr 2015
Home Depot Inc.[16]	HD.N	Buy	N/A	US$114.30	07 Apr 2015
Home Properties, Inc.[16]	HME.N	Neutral	N/A	US$68.74	07 Apr 2015
Hovnanian Enterprises[16, 20]	HOV.N	Buy (CBE)	N/A	US$3.67	07 Apr 2015
Lowe's Companies, Inc.[16]	LOW.N	Buy	N/A	US$74.11	07 Apr 2015
Post Properties Inc.[16]	PPS.N	Neutral	N/A	US$56.39	07 Apr 2015
PulteGroup, Inc.[4, 6, 16, 20]	PHM.N	Buy (CBE)	N/A	US$22.17	07 Apr 2015
Ryland Group[16, 20]	RYL.N	Buy (CBE)	N/A	US$48.13	07 Apr 2015
UDR Inc.[16]	UDR.N	Neutral	N/A	US$33.64	07 Apr 2015

Source: UBS. All prices as of local market close.
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