White Paper: Determining Market Area

June 2016

Introduction and Purpose

This White Paper is intended to serve as a resource for two categories of users: 1) market study providers to assist in the determination and documentation of a reliable market area and 2) users of market studies to understand the rationale in defining a market area and evaluating the appropriateness of the market area definition and description included in a market study.

The definition of a market area sets the context and tone of the entire market study. While a somewhat subjective judgment, a market area’s size and density has a profound impact on an analysis in terms of demographic trends, demand estimates, and the competitive environment.

Revised Primary Market Area Definition (Proposed): The primary market area is the geographic area that a proposed or existing housing community serves. The market area should consider both the proposed target market and the location of alternate housing opportunities that are similar in characteristics and linkage to employment centers, community facilities, and services. The subject property’s target market can include households who live, work, or have ties to the market area.

Secondary Market Area Definition: The portion of a market area that supplies additional support to an apartment property beyond that provided by the primary market area.

Factors to be Considered in Determination of a Market Area

The definition of a reasonable and reliable market area requires consideration of many factors, which may vary on a market by market basis. The market study should include a detailed narrative listing the factors considered and a discussion of how each factor affected the determination of the market area. Common factors used in market area determination, listed in alphabetical order, include:

- **Commuting Patterns and Drive-Time Analysis**: The time residents spend commuting and their employment destination often reveal distinct patterns. High percentages of residents with long commutes or working in neighboring jurisdictions are often indicators of a lack of available housing options near employment centers. Drive-time analyses can help define the areas that are within the commuter sheds of potential residents.

- **Employment Centers**: If the market area’s major employment centers have workers who live outside the primary market area, but have wages that are within the project’s price range, the primary market area may include non-market area residents working in the market area. These households should be considered in demand calculations in addition to households residing in the market area.
Housing Product Characteristics: The introduction of a unique product type (units with integrated garages, a mid-rise or high-rise building with ground floor commercial space, or single-family homes) may increase the draw to a particular site or submarket.

Jurisdictional and Local Agency Service Boundaries: Differences in the quality and services provided by school districts or municipalities often influence consumer location choices. The geographic areas covered by local agencies, such as housing authorities, senior citizen centers, community-based organizations, or churches can be a strong indicator of market area boundaries, especially when the project has a community-based sponsor or co-sponsor.

Location of Competitive Housing Alternative: The location of alternative housing opportunities addressing the same target population. The competitive properties should have similar access to jobs, services and community amenities, and transportation options as does the subject development and site.

Market Perceptions: Whether or not grounded in reality, market perceptions can be a significant determinant of market area boundaries. Social stigmas often exist within submarkets, with residents from one side of a submarket may not move to a close by neighborhood, regardless of housing opportunities. The construction of a new, attractive rental community may not necessarily alter this perception.

Natural Boundaries: Natural boundaries including rivers and mountains can restrict movement and travel within an area due to lack of transportation linkages. For example, a river with no nearby bridges would serve as a natural boundary of a market area.

Non-geographic Factors: Market areas can be determined by the target market the community will address rather than specifically by geography, such as employees expected to relocate to a submarket as a result of planned or existing job opportunities. Special needs households served by multi-jurisdictional agencies that have large service areas and often direct residents to different submarkets for housing.

Regional Amenities: The proximity of a site or submarket to regional amenities including large shopping centers, employers, healthcare providers, and/or colleges or universities often plays a role in the market area definition.

Target Market: Proposed developments targeting a special needs population such as seniors, generally draw from a larger geographic region. Given the smaller pool of qualified householders, the location and quantity of comparable stock is of additional importance. An acceptable market area for a general occupancy community may be too small for a special needs or senior oriented housing development.

Transportation Linkages: The proximity of transportation options including major traffic arteries and mass transit options can influence the size of the market. Mass transit can have a significant impact on projects addressing target markets for which transportation options may be limited.

Impact of a Market Area

Items directly impacted by the market area definition include:

Appropriate Pricing: The competitive and comparable housing stock included within a defined market area has a significant impact on the conclusion regarding appropriate pricing for housing at a specific location. The inclusion of competitive communities in non-comparable submarkets may result in an inaccurate conclusion regarding pricing.

Demand: Demand for new housing depends on the specific type of housing including tenure and target markets; however market area definition is one of the primary factors in a demand calculation. Too large of a market area may result in overstating demand for a proposed
development, while a conservative market area may discount the demand for new product, especially if a lack of quality housing currently exists.

- **General Demographics:** The socio-economic composition of a market area including income, household size, and tenure breakdown is a reflection of the geographic area included in a market area. An inaccurate market area will likely produce a demographic profile not consistent with the immediate area surrounding a proposed or existing site.

- **Population and Household Counts:** The geographic coverage of the market area determines the number of households in a market area. Total householders residing in a market area significantly influences demand estimates.

- **Supply Analysis and Competitive Stock:** The definition of the market area generally determines the competitive analysis and potential pipeline (anticipated new competitive units). The market area definition plays a role in the communities deemed most relevant and comparable. The market area definition also determines the pipeline communities used in the supply side of the demand estimate.

### Potential Market Area Red Flags

When reviewing a market area definition and the explanation of that market area, readers should look for potential red flags, which may indicate a questionable market area. While the following situations may be appropriate for a specific market area, they are often an indication of a potentially inaccurate market area definition.

- **Radii Market Area:** The use of concentric circles commonly referred to as a “ring analysis” to determine a market area is generally considered an arbitrary and antiquated technique. Easily obtainable analytic tools are now available to allow an analyst to tailor a market area to mirror development patterns. Field work should yield sufficient data and insight to eliminate the need to simply draw a circle around a site. In some cases, an accurate market area can resemble a circle; however the market study should include justification of the market area.

- **County-Wide or City-Wide Market Areas:** The use of an entire county or municipality as the market area is a common practice. A specific site’s location relative to the jurisdiction’s boundaries should be carefully considered before the jurisdiction is chosen as the market area. Often times, similar housing communities in neighboring counties are closer in both proximity and demographic/housing composition than the far side of the subject jurisdiction. The location of a proposed community within a particular jurisdiction does not necessarily mean that all jurisdiction residents will consider it a viable housing option; likewise, residents of neighboring jurisdictions will not necessarily ignore a housing alternative simply because it is not in their home jurisdiction.

- **Gerrymandered Market Areas:** A market area should be somewhat contiguous, following transportation networks, political and natural boundaries. An unusually shaped or sized market area should be justified by the analyst.

### Market Area Narrative

A market study should include a detailed narrative explaining how the market area was determined. The narrative should identify the project’s target market(s) and target population(s). It should discuss individual factors used in the determination of the particular market area. Narratives should be project-specific rather than general text with a litany of “factors considered” that could be included in any market study. For mixed-income, mixed-population, and/or mixed-use projects, the narrative should indicate if the individual components share the same market area or describe the reasons for different market areas.

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