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2015 Forecast

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Multi-family investment outlook: White-hot investor demand to set new benchmarks

Pre-recession pricing, abundant retrofit opportunities, historically low interest rates and free-flowing capital – these are a few of multi-family investors' favorite things. Just like the years since the Great Recession leading up to 2015, unprecedented investor demand will continue to be fed by falling cap rates and rising prices per unit. This white-hot environment and widespread shortage of supply, however, are breeding competition. Gaining entry can be challenging, at best, and off-market transactions have become the norm. Now more than ever, it is imperative to partner with an investment brokerage firm with decades of experience, depth of market expertise and long-term owner relationships.

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In both suburban and urban areas, older, post-World War II garden-style and mid-rise apartments will outpace their newer counterparts in the coming year. This is due to supply constraints and the high-barrier-to-entry of Class-A product. Age allows investors the greatest opportunity to breathe new life into an outdated building through unit renovations and modernization of common area features. Both have proven to increase revenue and decrease turnover rates, while also reducing maintenance costs following the initial upgrade investment. Kitchens, bathrooms and common area renovations have become the "standard" for capital improvement programs.

These repositioned properties, along with a weak single-family home market, have contributed toward a steady rental uptick that peaked in November at its highest point nationally since August 2011, according to Zillow. The same study reports a 3.6% and 4.4% increase in the New York/New Jersey and Philadelphia MSAs, respectively. Major strides are expected to be the theme in 2015 as well, with asking rents advancing at a pace commensurate with 2014.

Even if the job market makes miraculous strides this year, occupancy rates will not waver. In-place tenants, the majority of whom are hard-working families unable to qualify for a residential mortgage and/or don't have access to ready cash for a down payment, will stay put while a strong renter-base pipeline builds.

From Millennials to Baby Boomers, rental living has gained greater momentum as the lifestyle of choice. Retirees are shedding their empty nests at a faster pace now that housing prices are no longer significantly undervalued. Simultaneously, the 25- to 35-year-old demographic continues to reject homeownership altogether, based on their parents' losses during the mortgage crisis, lack of creditworthiness and disinterest in home maintenance. Despite the 30+ year age gap between Millennials and Baby Boomers, both want the same thing – a live/work/play rental lifestyle.

While multi-family construction starts are on the rise, there is no immediate "health" threat to existing properties in the Mid-Atlantic region. Largely confined to cities implementing more efficient urban planning and mass transit infrastructure improvements, many abandoned industrial properties are now being converted to residential Class-A properties.

Existing class B+ or value-add-opportunity B and C property investors need not be concerned. Historically, these properties are in greatest demand among workforce tenants. And by rendering older buildings more competitive, owners are leveraging city-wide gentrification associated with new construction in the neighborhood.

Even in suburban locales like densely populated Northern New Jersey, mixed-use projects that have been stalled for years are now underway with positive rippling effects. This holds true in Passaic and Bergen County, which coincidentally is one of the highest-barrier-to-entry markets in the region.

While 2014 was the strongest post-Great Recession year for multi-family investments on record, with firms like Gebroe-Hammer recording more than 105 deals involving 7,200+ units, 2015's theme will be major rent growth. Among the top markets to watch are Pennsylvania and New Jersey. The housing market will continue to lag while multi-family investment and rents are prime for expansion. Barring a major interest rate increase, which is unlikely, multi-family will continue its meteoric rise and secure its rightful spot as the past decade's leading commercial real estate asset.

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