The Strength of Multifamily as a Long-Term Investment

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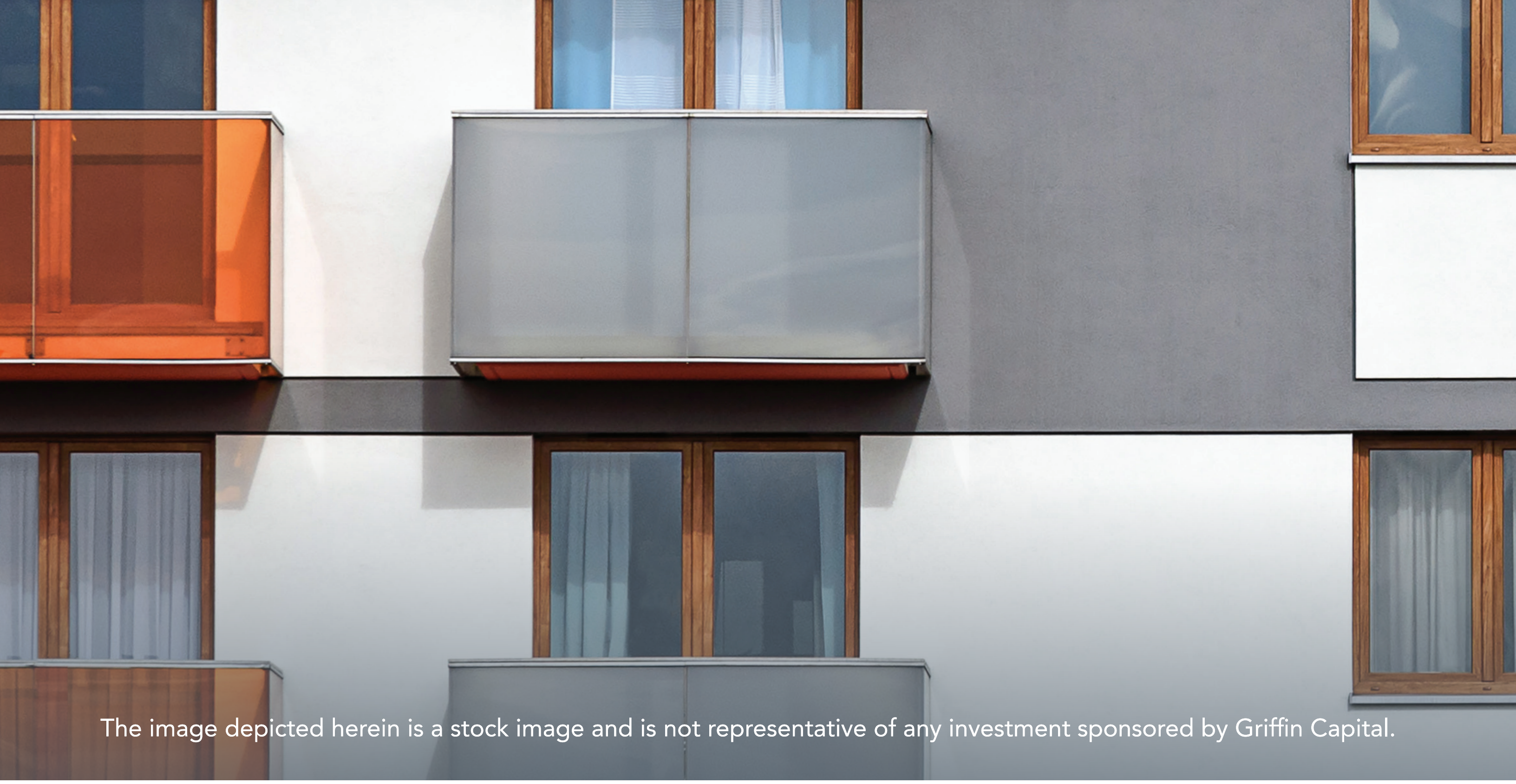
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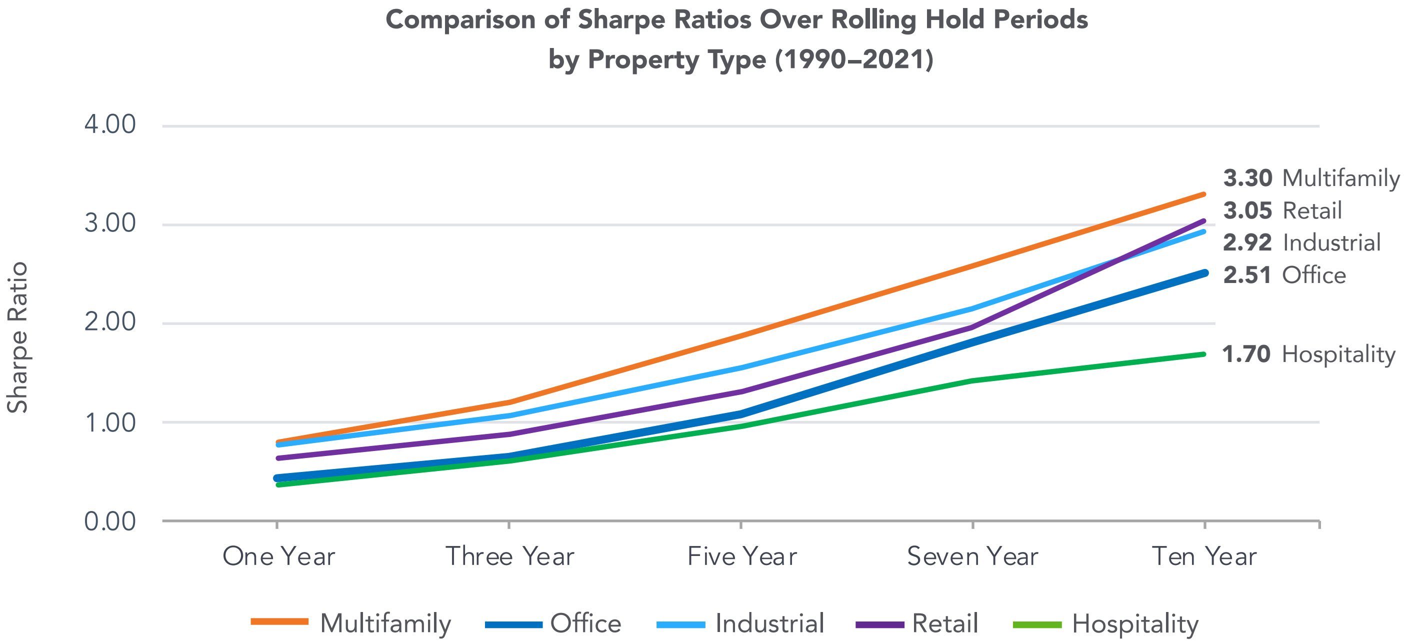
The Continued Case For Multifamily

Eric Kaplan, President, Griffin Capital Private Equity

The COVID-19 pandemic spurred a series of new trends and widespread rethinking of historical norms. For many real estate investors, such evolutions raise the question as to whether the post-pandemic outlook of different property sectors will change meaningfully from their pre-pandemic performance. While many are left to question the resiliency of sectors like office and retail, one sector appears to be well-positioned to continue generating strong risk-adjusted returns: multifamily.

For the past several decades, multifamily investors enjoyed attractive risk-adjusted returns relative to other major property sectors for a variety of reasons, including its necessity-based nature (the need for shelter), greater affordability versus single-family homes, enhanced liquidity relative to other asset classes, the programmatic nature of expenses, the ability to diversify across several tenants and a sustained trend towards delayed household formation amongst younger cohorts. The pandemic not only confirmed these factors but created additional demand drivers, such as the rapid acceleration of single-family home prices and a shift in population mobility towards certain markets that are expected to support multifamily performance for decades to come. These were among the many reasons why average multifamily rent collections remained robust during the pandemic.

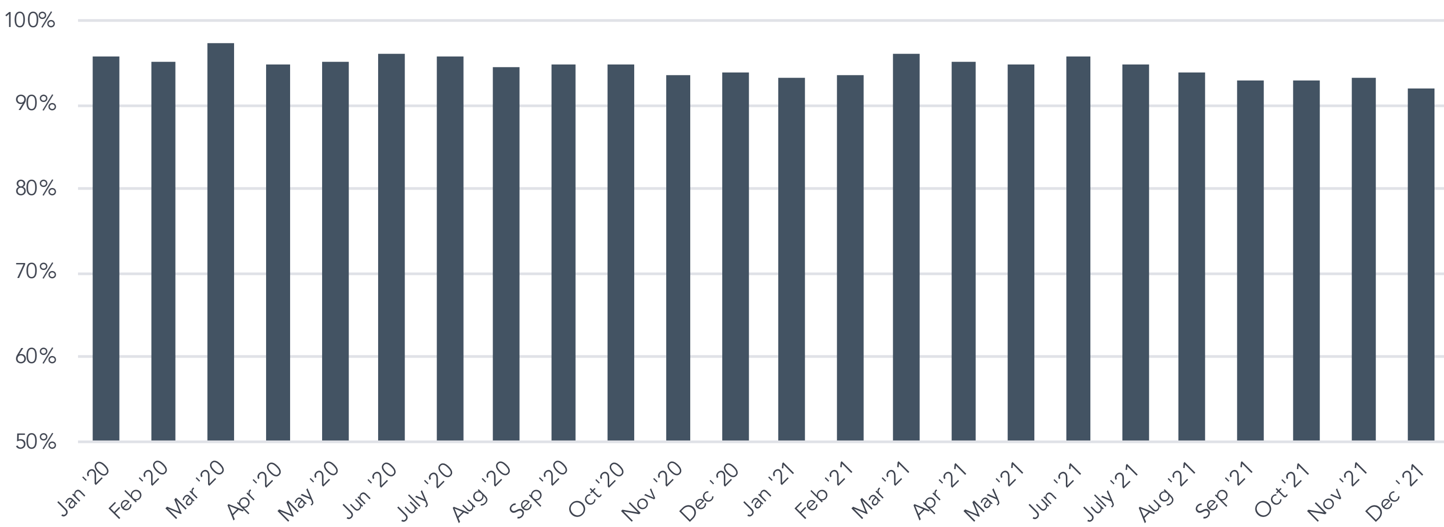


Sharpe Ratio: A ratio used to compare risk-adjusted returns, which shows an investment's excess return (above the risk-free rate) per unit of risk (standard deviation). The higher the ratio, the better the risk-adjusted return. The average three-month U.S. Treasury T-bill auction was used as the risk-free rate in this analysis.

Source: National Council of Real Estate Investment Fiduciaries (NCREIF) through December 31, 2021. Returns were calculated as the average for each specified holding period on a rolling quarterly basis between 1Q 1990 and 4Q 2021.

Past performance is no guarantee of future results. This chart is for illustrative purposes only and not indicative of any investment. The data used to create the chart was provided by NCREIF.

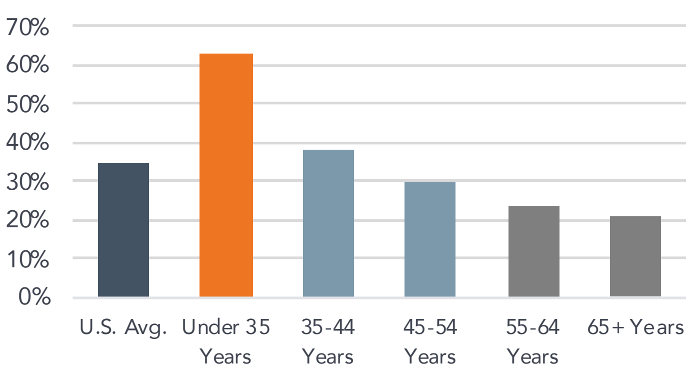
AVERAGE U.S. MULTIFAMILY RENT COLLECTION[1]



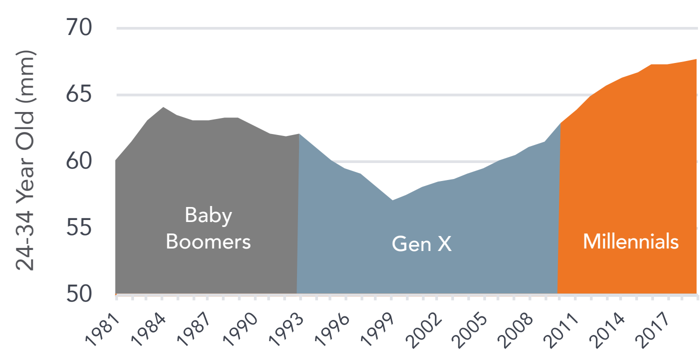
DEMOGRAPHIC TRENDS[2]

While demand for multifamily has long been supported by an inherent need for housing in response to a growing population, it has benefited from additional tailwinds over the past two decades as a result of the shifting preferences of various generations. Most notable is the increasing percentage of young adults that are delaying household formation. Millennials, with a median current age of 32, are the largest age demographic in U.S. history and are overwhelmingly showing a preference to rent with an average rentership rate of over 60% for individuals under 35 years old.

MF Rentership Rate by Age



Size of U.S. Age Group by Generation



1. Source: https://www.nmhc.org/research-insight/nmhc-rent-payment-tracker/.
2. Sources: U.S. Census Bureau, Bureau of Labor Statistics, and Zelman and Associates. As of Q1 2021.

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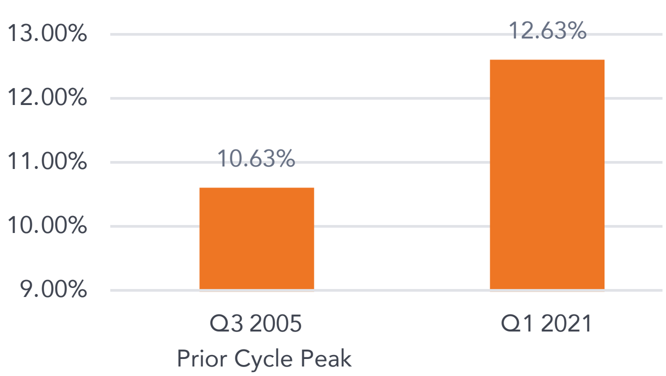
As noted by the Housing Finance and Policy Center, one of the primary reasons these individuals elect to rent is their enhanced desire to delay household formation. For example, in the year 2000, 42.7% of individuals aged 18–34 had never been married and 32% were married with children. By 2015, the percentage of individuals in this age cohort that had never been married increased to 53.9% and the percentage that were married with children shrank to 25.7%.[3]

Millennials aren't the only generation showing an increased propensity to rent. Baby boomers, the second largest age group in U.S. history, are increasingly looking to rent as well. As noted by the U.S. Census Bureau figures, from 2007 to 2017 the number of renters aged 55 and older rose 38% and those over the age of 65 rose 43%.[4] The combination of rising life expectancies and higher medical costs makes the convenience and affordability of renting an attractive option for those entering their retirement years; with a median age of 66, the majority of baby boomers are either at or near the time when they will need to start evaluating such considerations.

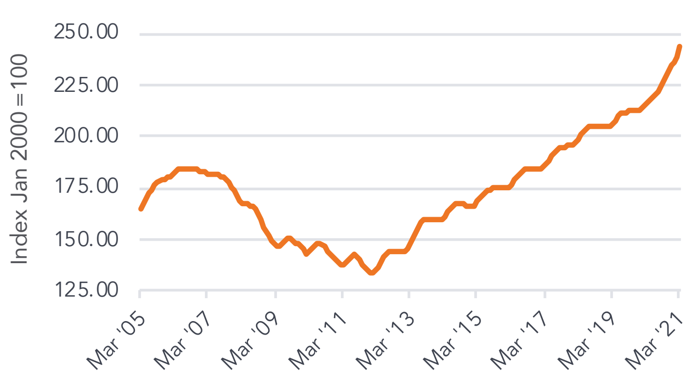
HOUSING AFFORDABILITY

Single-family home prices have grown significantly relative to wages, driving the American dream of homeownership farther out of reach for many younger Americans. Work from home and a desire for more space caused buyers to flee high-cost urban nodes such as San Francisco and New York and purchase homes in lower-cost states and suburbs. This in turn drove home prices to record highs, culminating most recently with the Federal Housing Finance Agency's ("FHFA"), seasonally adjusted home price index booking its highest trailing one-year increase on record at 12.63%.

Trailing Four Quarters Growth in U.S. Home Prices[5]



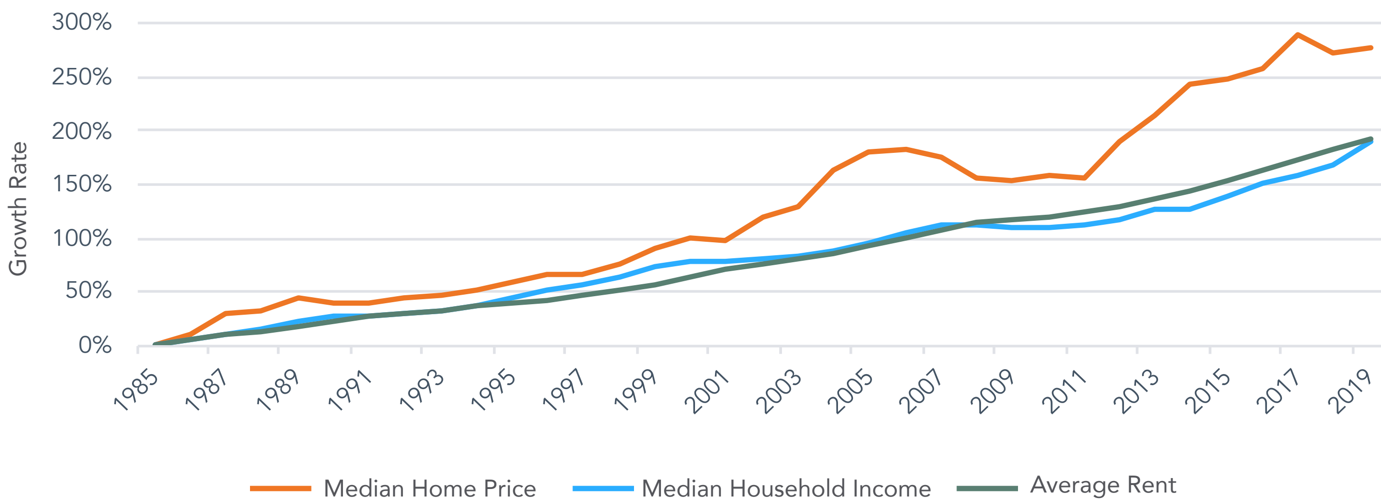
Case-Shiller U.S. Home Price Index[6]



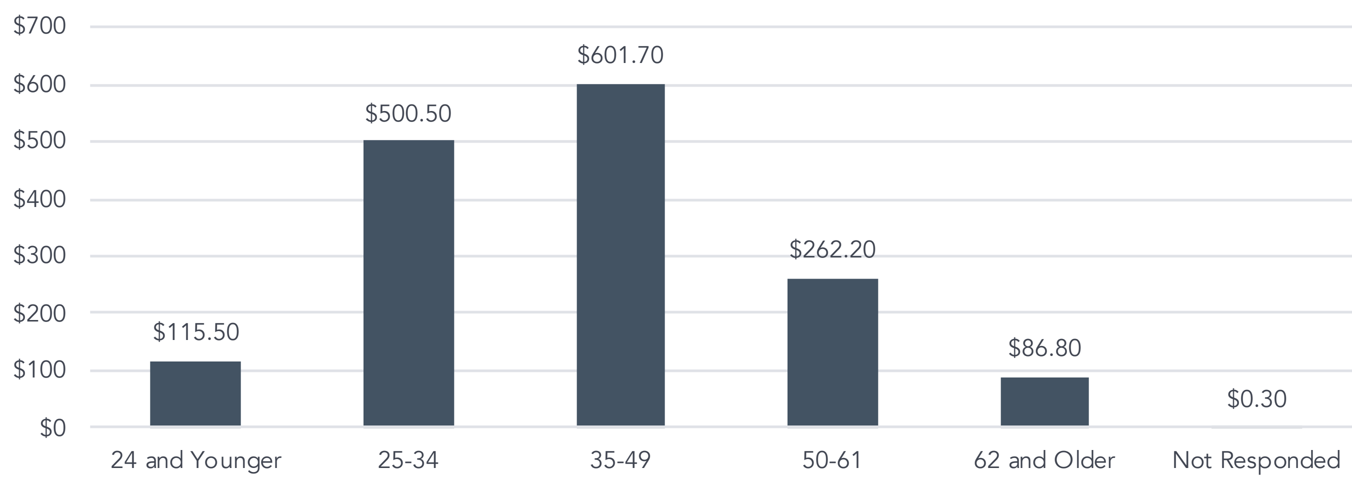
3. Source: https://www.urban.org/sites/default/files/publication/98729/millennial_homeownership.pdf.
4. Source: https://www.forbes.com/sites/nextavenue/2019/10/22/moving-back-to-the-city-in-midlife/?sh=383e63457db9.
5. Source: FHFA Seasonally Adjusted, Purchase-Only Index. https://www.fhfa.gov/DataTools/Downloads/Pages/House-Price-Index-Datasets.aspx#mpo.
6. Source: Retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/CSUSHPINSA.

As home prices have risen, incomes have failed to keep up. When combined with the increasing burden of student debt that many face, renting becomes not just one of the options available but the most attractive option.

Growth Rate of Median Home Prices vs. Median Household Incomes vs. Average Rents Nationwide[7]



Student Debt Dollars Outstanding (in Billions)[8]

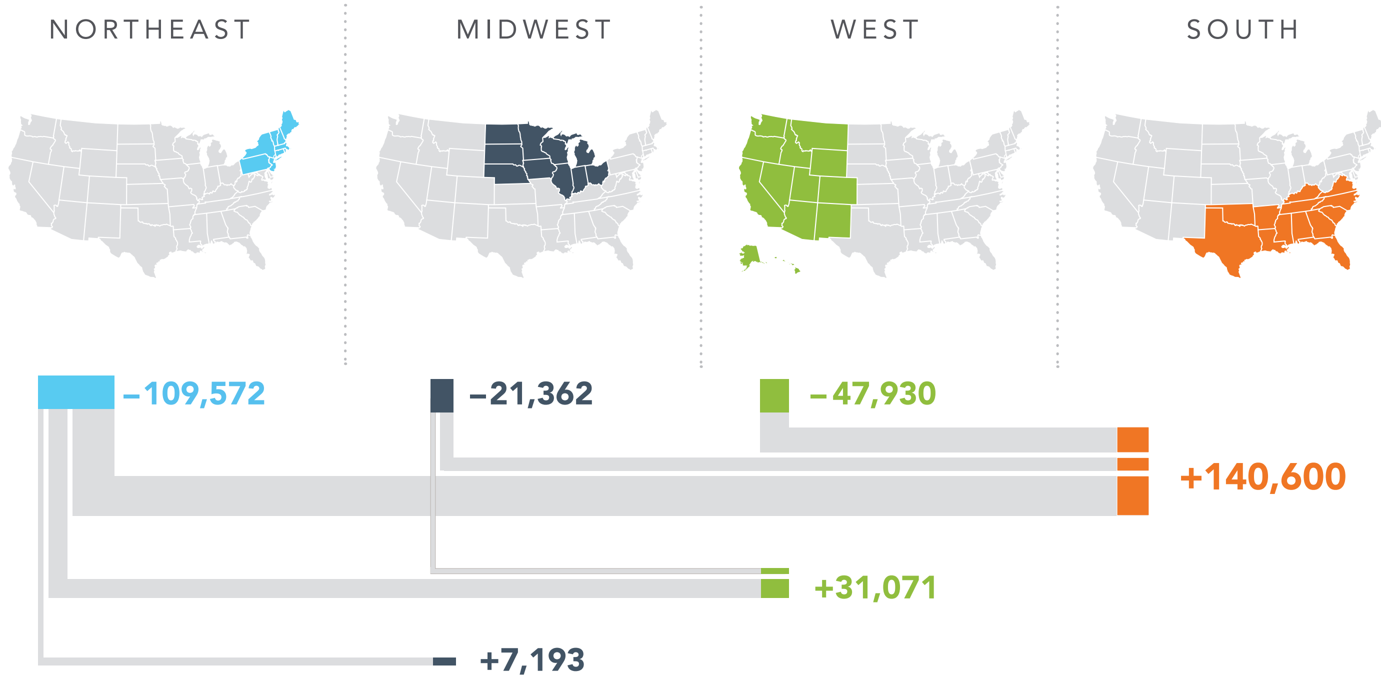


7. Source: Retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org.
8. Source: https://www.cnbc.com/select/average-student-loan-debt-by-age/.

POPULATION MOBILITY

Population mobility has increased significantly through the pandemic across multiple age demographics. Similar to the rise in single-family home prices, the widespread adoption of work from home caused a surge of movement not only within states but across states. While some speculate this trend may reverse as offices reopen, the rapid adoption of remote work technology and other factors have granted workers increased flexibility to dictate where they want to live and work. They are choosing markets that are lower cost, that provide better opportunities for a work/life balance, where they can spend more time recreating outdoors and keep more of what they earn. Baby boomers similarly are moving to lower-tax states with better weather and lower costs of living. Employers have followed suit in pursuit of this migrating talent pool while also enjoying lower operating costs. Growth markets like Nashville, Tampa, Dallas, Austin, Phoenix and Denver, as well as other markets across the Southeast and Southwest have been the beneficiaries of population mobility fueling some of the strongest rental growth in the country as demand exceeds supply.

2020 Net Flow of Households Between Regions[9]



The result of rising home prices, population mobility, and strong demographic-driven pent-up demand portends a very constructive outlook for multifamily developers and owners. There is a housing shortage, a housing affordability issue, and a changing view on what is most important to individuals when it comes to location desirability, fueling secular demand for rental housing, specifically in growth markets across the Southern United States that is likely to endure. The speed by which demand is shifting to many markets has made it difficult for supply to keep up. Therefore, experienced and knowledgeable developers and investors are well-positioned to take advantage of the opportunity.

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9. Source: https://www.wsj.com/articles/pandemic-supercharged-changes-in-where-americans-live-11619536399.

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