Five Themes for 2025

HALFTIME REPORT

As we entered 2025, we shared five themes impacting the multifamily sector. As we approach the midpoint of the year, it is time to evaluate the evolution of these trends and how they are materializing.

The property depicted is a representative example of the types of multifamily development properties Griffin Capital has been involved in. **This property is owned by Griffin Capital or its affiliates.**

THEME 1

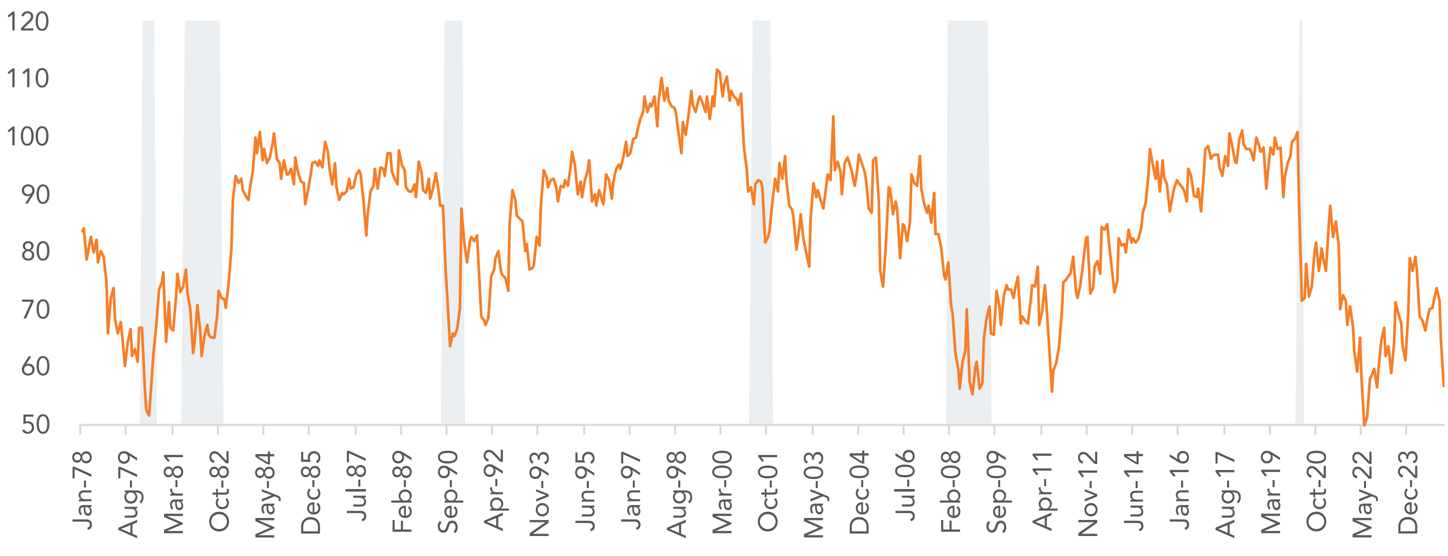
Red Sweep

The results are in. What was supposed to be a close election cycle was far from it, with Republicans prevailing in the House, Senate and White House.

While both parties talked on the campaign trail about the undersupply of housing and associated affordability issues, their stated approach to addressing these issues vastly differed. While the new government will focus first on getting nominations and appointments through the process and then shift focus to a reconciliation bill, policy discussions have already started to take shape. Depending on the extent of some of the proposed policies on immigration, trade, and tax, outcomes for the dynamics in the housing market are likely to be impacted. Policy to address housing supply is likely going to be accommodative to developers and investors, easing the red tape and regulatory burdens that have stymied housing creation. We expect an expansion of legislation like the "Investing in Opportunity Act" that spurred billions of private sector capital into Opportunity Zone Funds and see a path for further expansion of private sector incentives to develop affordable housing.

Conversely, trade policy could serve as a headwind for housing development depending on the scale and scope of tariffs and the associated cost of construction materials. The same can be said about immigration, as the construction industry relies heavily on the migrant labor pool. Higher materials and labor costs could be a counter-balance to new development but serve as a rent growth catalyst for existing supply. One of the important observations as it pertains to the incoming administration is that those who have been nominated to craft and implement housing policy have a background in the field of housing development and understand the nuanced issues that developers face and how to properly incentivize them to create the housing that Americans need.

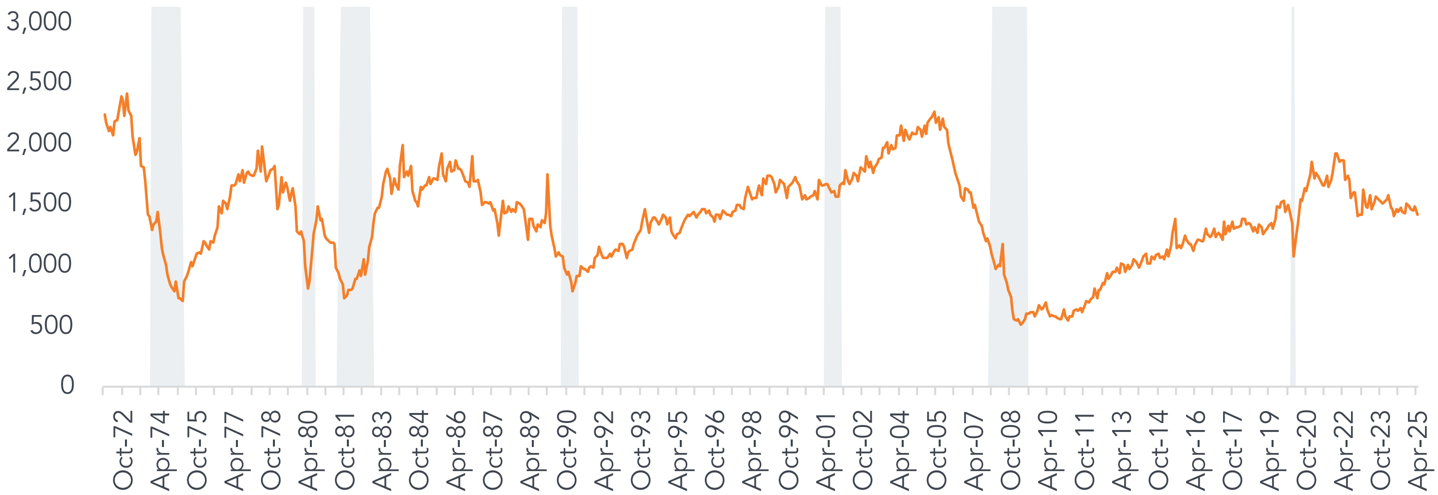
Consumer Sentiment



Source: University of Michigan: Consumer Sentiment (UMCSENT) https://fred.stlouisfed.org/series/UMCSENT

Past performance is no guarantee of future results.

Total Housing Units Authorized



Source: New Privately-Owned Housing Units Authorized in Permit-Issuing Places: All Residential Units (PERMIT5) https://fred.stlouisfed.org/series/PERMIT5

Halftime Report

While immigration policy is clear, its impact on the labor force so far has been minimal. Builders are not reporting observable increases in labor costs, and the availability of skilled labor remains sufficient to support what is presently a muted development pipeline. Trade policy, however, presents a different dynamic, as clarity is still lacking. Impacts of this uncertainty have rippled through public equity markets, reminding investors of the benefits of portfolio diversification. The knock-on impacts of aggressive tariffs, such as a slower growth outlook and heightened probability of recession, have pushed down interest rates in some respects and increased the prospects of future rate cuts, but volatility in the bond market has created complexities for real estate investors seeking access to debt capital.

What is evident regarding trade policy thus far is that consumer sentiment has weakened, leaving business leaders somewhat confounded. This is limiting investment in the near-term at both the consumer and corporate level as indicated by an incredibly anemic start to the Spring home-buying season and M&A activity year-to-date.[1,2] Trade policy has not yet significantly impacted construction costs,[3] and in several cases, such as lumber and drywall, major construction materials have been exempted from more restrictive policies. This supports the view that the administration acknowledges that housing affordability is best addressed by reducing barriers to expanding supply. Should some of the more draconian macroeconomic outlooks materialize, we know that housing construction historically contracts during recessions, but household formation continues.

Tax Policy remains a work in progress but is gaining momentum rapidly. The House and Senate have elected to approach reconciliation through a single omnibus bill, which is the preferred approach of the Executive Branch. This legislation is likely to include extensions of key provisions from the Tax Cuts and Jobs Act (TCJA). Opportunity Zones, created as part of the TCJA and championed by influential members of Congress, are likely to be extended and potentially expanded, paving the way for additional catalysts to housing creation and expanding upon what has proven to be a very successful program.

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THEME 2

The Supply Cliff

In 2024, we had the largest spread between new apartment deliveries and new starts since 1975, a continuation of a trend from 2023.[4]

The easiest thing to predict is new apartment deliveries; one must only look at new starts and extrapolate the construction timeline to completion to understand the future of supply. New starts and future deliveries are highly correlated, and what we know for certain is that new starts have declined dramatically. In many of the high-growth markets, peak-to-trough starts are down more than 60%,[5] driven by less liquid debt markets, uncertainty around valuations as interest rates were rising, higher costs of construction and capital rotating away from real estate over the past 24 months to less interest rate sensitive sectors. As we look at the delivery pipeline, we see a dramatic fall-off starting in the second half of 2025. We expect this to lead to improved operating fundamentals for landlords, which will be realized through fewer leasing concessions and higher rental rates on renewals and new leases.

Halftime Report

The looming supply cliff is real. New starts remain muted, and the number of new deliveries will continue to decline over the next 24 months.[6] We currently find that it takes an average of 17 months to start and complete a multifamily community, a timeline that continues to extend, not including the 12 or more months required for zoning and permitting. Construction costs remain elevated, and access to debt capital for developers is only available for a select subset of market participants. However, we are already seeing operating fundamentals improving and expect this trend to continue as strong demand meets limited new supply.

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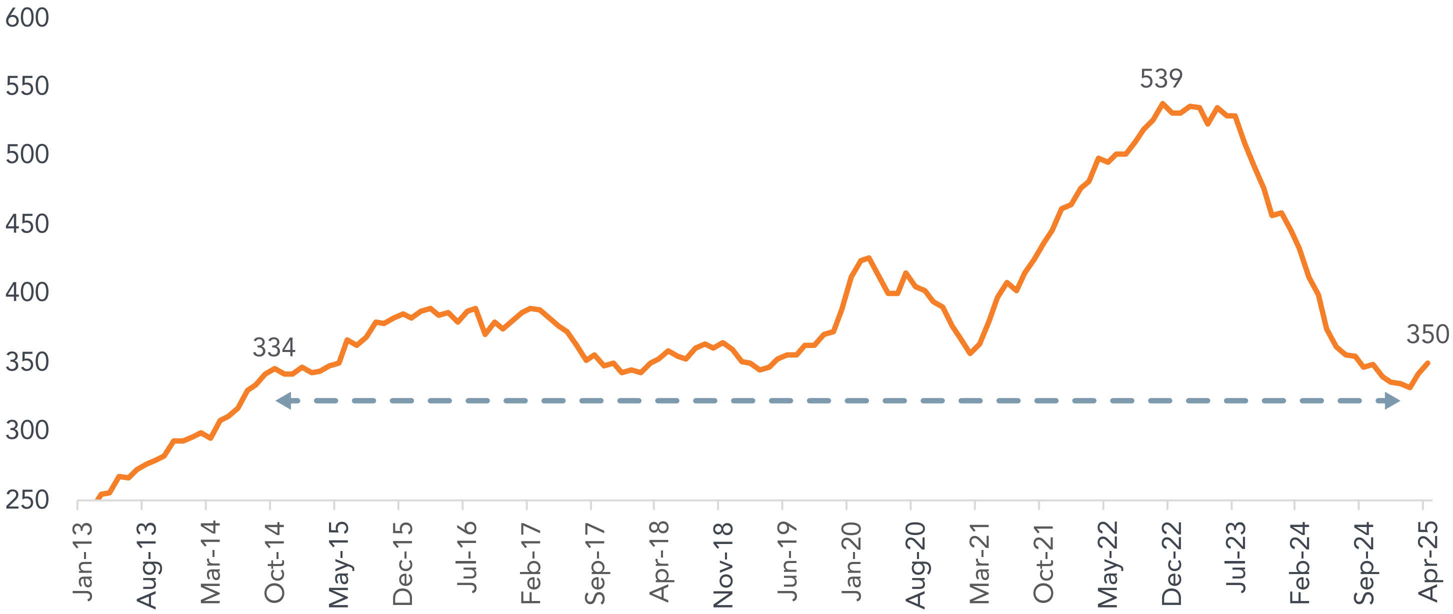
U.S. Multifamily Housing Starts Plunge to 10-Year Low

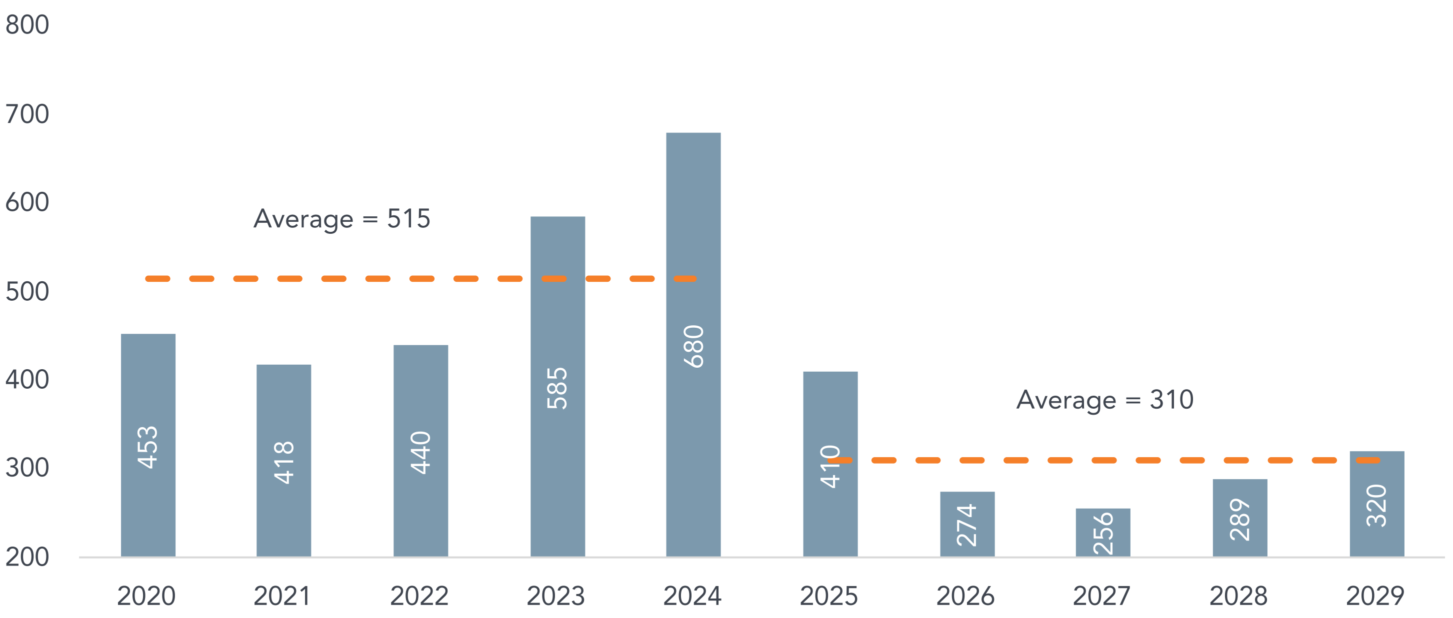
T-12 Multifamily Housing Starts (NSA), in thousands of units



Source: U.S. Census Bureau and U.S. Department of Housing and Urban Development, New Privately-Owned Housing Units Started: Units in Buildings with 5 Units or More [HOUST5FNSA], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/HOUST5FNSA, May 21, 2025.

Multifamily - Gross Delivered Units

History & Forecast, in thousands of units



Source: CoStar.

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THEME 3

The Demand Story Continues

Housing selection is a binary choice between owning and renting.

Inadequate single-family housing production dating back to the GFC and limited for-sale inventory created a significant increase in home values over the past three years that has remained sticky. Only 9% of the single-family housing supply being developed is "entry-level,"[7] creating challenges for those who wish to leave the rental pool. With consumer debt rising, personal savings rates declining, and more significant components of our population skewing younger, we anticipate continued strong demand for rental housing. In Q4 2023, Q1 2024, and Q2 2024, the rental market had double the normalized demand, a trend we expect to continue to be elevated over the next several years. Given the decline in new deliveries starting in the second half of 2025, if demand persists as we expect it will, the operating environment for multifamily owners should be advantageous.

Halftime Report

The demand side of the equation has outperformed expectations. We experienced the second strongest leasing season for a Q1 in history. Anecdotally, the prime season for leasing, which is the Spring, is also off to a very promising start. The average age of first-time homebuyers is now 38 years,[8] prolonging the rental journey for a significant portion of the population. We expect continued strong demand through 2025, and as new deliveries continue to decline, we forecast rent growth to accelerate.

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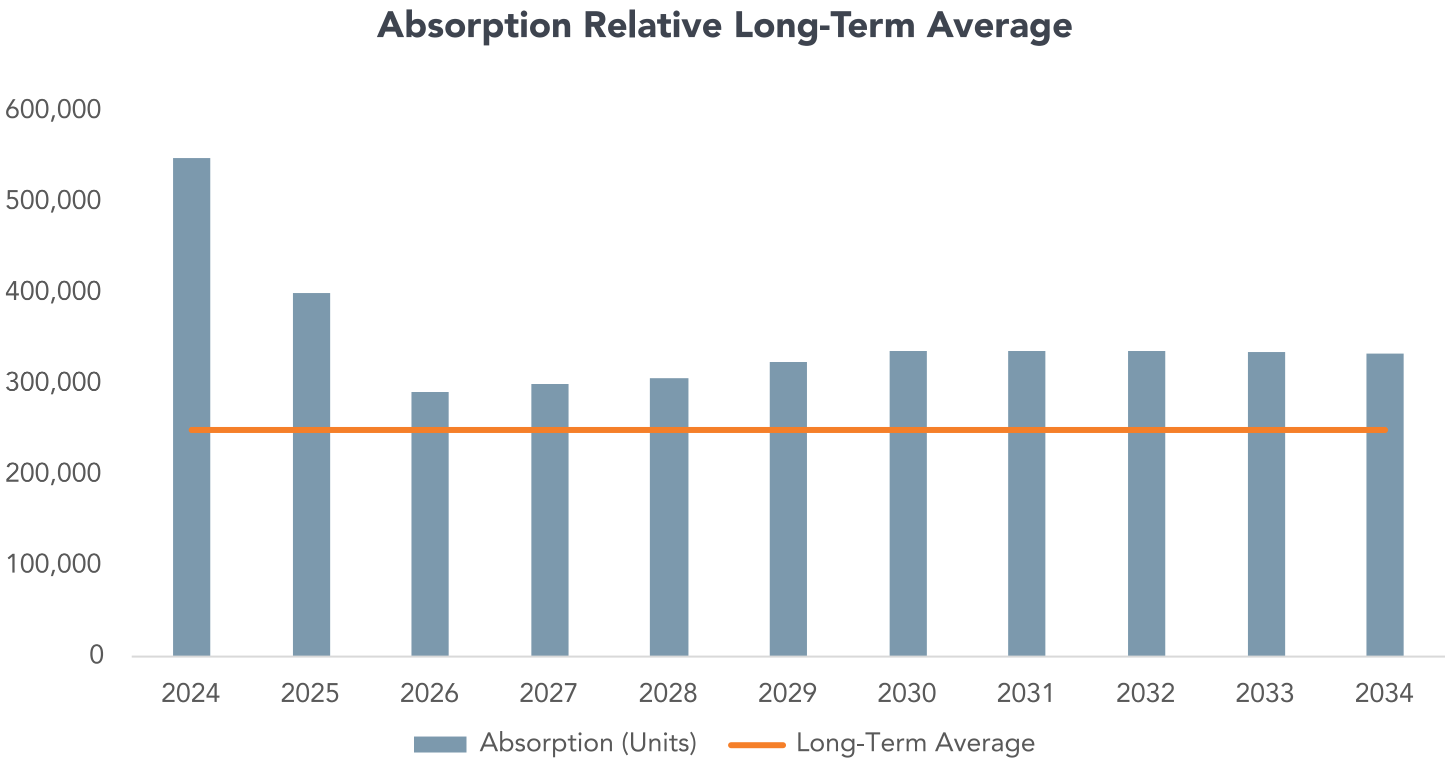
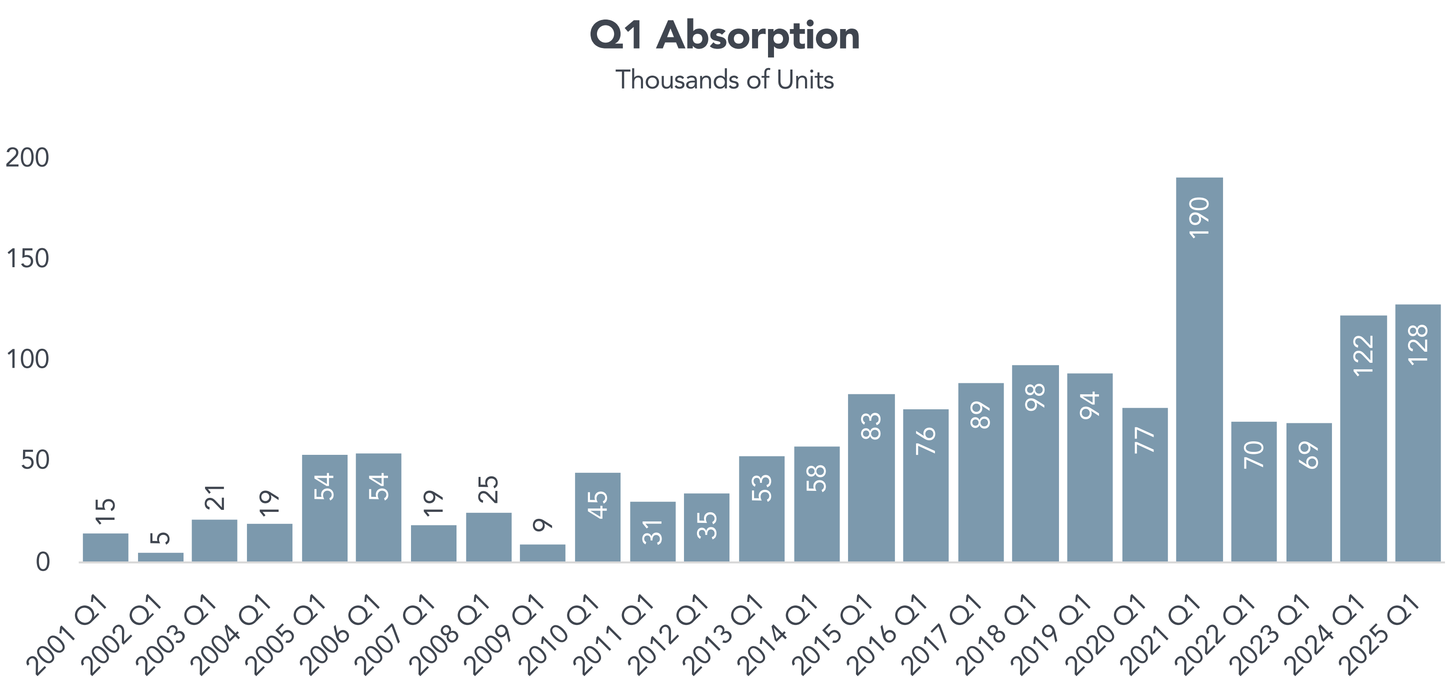


Source: CoStar.



Source: CoStar.

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THEME 4

Liquidity Returns

As interest rates were rising, valuations were adjusting.

Consequently, transaction markets were muted with buyers and sellers unable to come to a consensus. The Green Street Property Index indicates that values troughed in Q4 2023 and have rebounded ever so slightly over the course of 2024. The NCREIF Property Index, which is a diversified Core Real Estate Index comprised of Institutional Funds, reported a positive total return in Q4 2024, with both income and appreciation components of returns skewing positive. The biggest players have begun to step back into the market with sizeable transactions recorded in the second half of 2024, including Blackstone, KKR, Brookfield, and Equity Residential. This is just the beginning. Market participants are under-allocated to private real estate relative to their target allocations, have significant dry powder earmarked, and multifamily remains a favored sector. As interest rates have stopped rising and fundamentals such as demand remain clearly enduring, 2025 will likely be a year in which transaction volume accelerates meaningfully. Multifamily exposure offers investors portfolio diversification, defensive income, stability, and tax efficiency, all attributes we expect investors to want more exposure to if they are confident valuations have stabilized.

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Halftime Report

Liquidity in the debt capital markets is improving, predominantly for stabilized assets. Debt funds that raised significant capital over the 2022-2024 period are now compelled to put capital to work in an increasingly competitive environment, which is compressing spreads and benefiting borrowers. Traditional debt providers are also more active, encouraged by improving fundamentals.[9]

However, despite the increased liquidity, transaction activity has been tepid to start the year. While valuations have troughed, broader economic uncertainty remains a hindrance to normalized activity. With more clarity as we move through the year, we expect transaction volume to accelerate.

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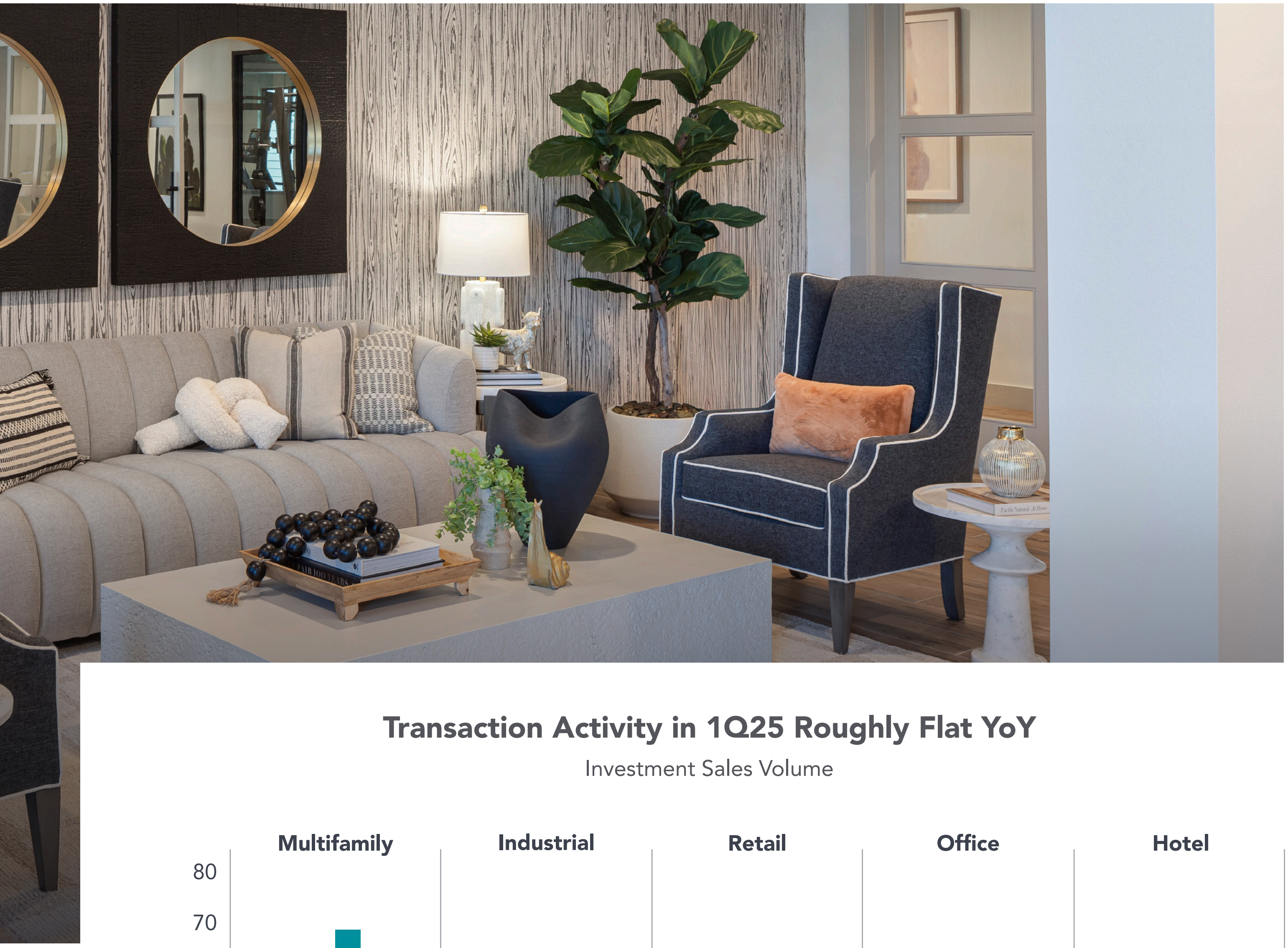
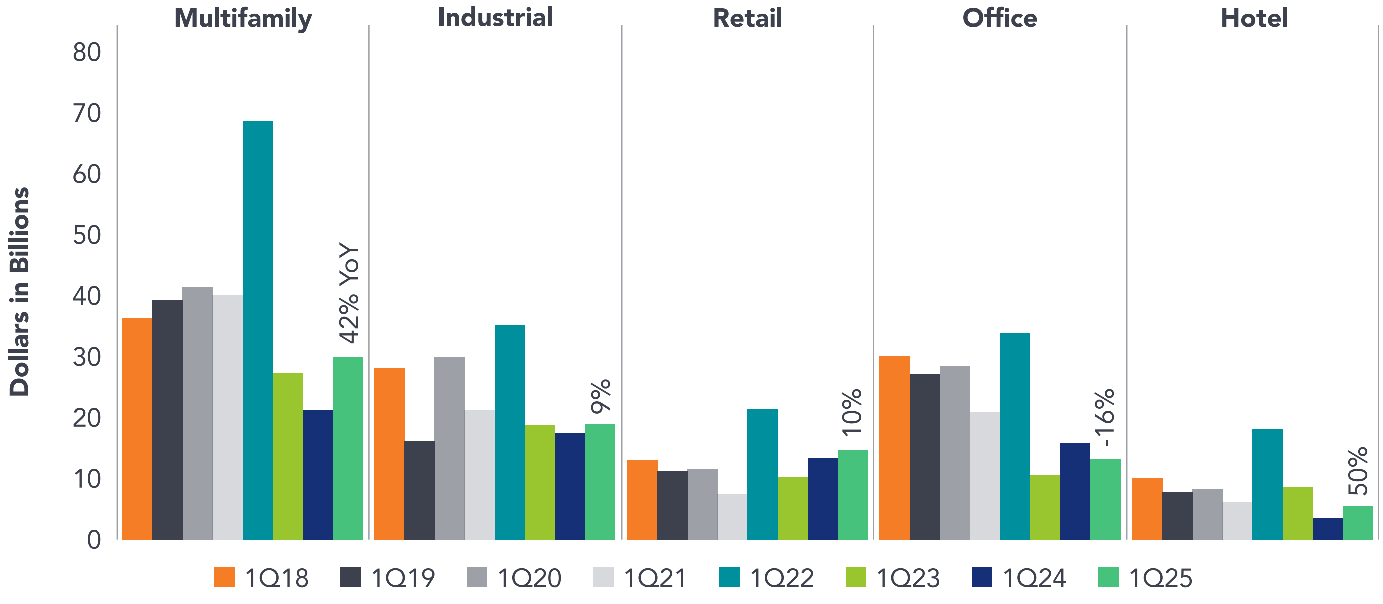


Transaction Activity in 1Q25 Roughly Flat YoY

Investment Sales Volume



Source: RCA, Newmark Research as of April 21, 2025.

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THEME 5

A Tale of Two Halves but a Good Whole

The first half of 2025 is likely to be markedly different than the second half. In the first half, rent growth will remain muted as the last of the new deliveries from the cyclical peak of new supply get absorbed. Housing, trade, and tax policy will be a moving target and have implications relative to interest rates that property market investors will seek to gain clarity on before jumping in with both feet. The headline narrative around real estate will shift slowly from cautious optimism to full-fledged conviction. Investors who place capital in advance of that sea change will likely benefit the most as we move through the cycle, but the dispersion of returns across the 2025 entry point will likely not have a dramatic impact on investors. We expect 2025 will be viewed in a historical context as an attractive vintage for capital deployment.

Halftime Report

We maintain our conviction that the first and last six months of 2025 will be different, for the reasons outlined. We anticipate that capital deployment in 2025 will be rewarded over the intermediate and long-term. While we expect valuations will not adjust meaningfully over the entire 12-month period, we believe that multifamily operations will begin to improve, which is already starting to materialize.

As trade policy becomes more clear and the tax policy framework is established, investor confidence is likely to increase. With that clarity, the capital deployment cycle will begin in earnest. Investors seeking portfolio diversification strategies may find it beneficial to begin increasing their allocations to private real estate over the ensuing 24 months.

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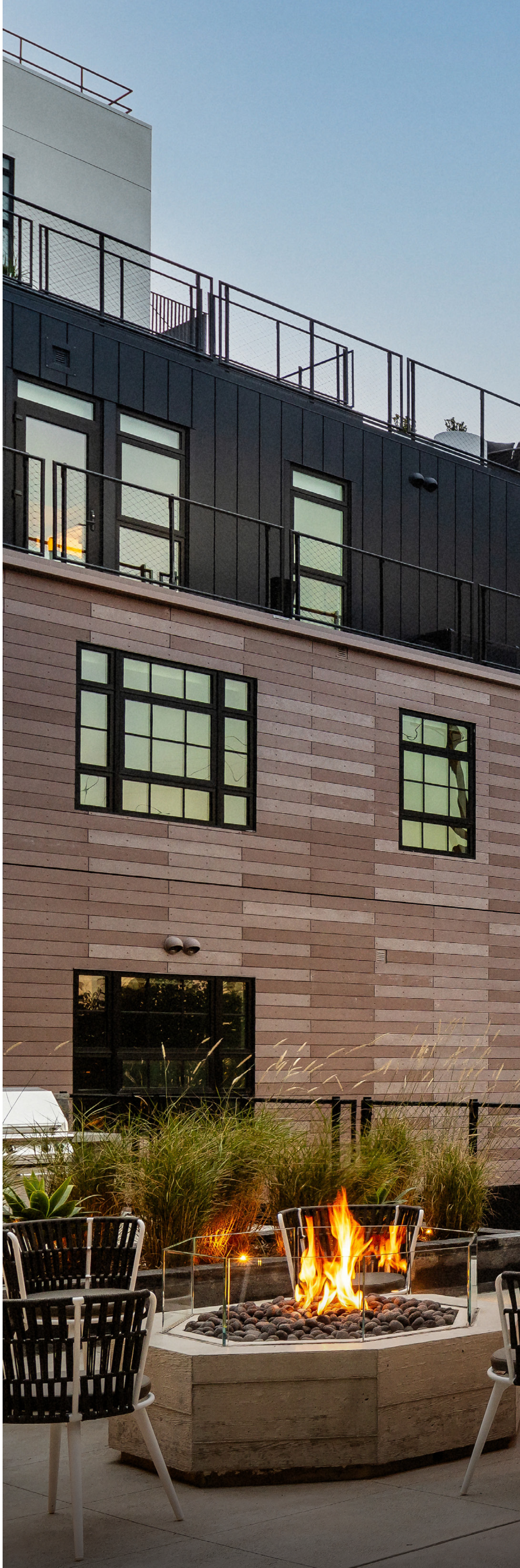

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ENDNOTES

1. https://www.newsweek.com/housing-market-gets-worrying-sign-spring-2025-2064152.
2. https://www.reuters.com/business/ma-deal-signing-hits-20-year-low-after-trumps-liberation-day-2025-05-06/.
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4. U.S. Census Bureau and U.S. Department of Housing and Urban Development, New Privately-Owned Housing Units Started and Completed: Units in Buildings with 5 Units or More [COMPU5MUSA], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org, December 19, 2024.
5. CoStar.
6. https://www.yardimatrix.com/Publications/Download/File/7225-MatrixMultifamilyNationalReport-April2025?signup=false.
7. U.S. Census Bureau. Percentage of entry-level housing defined as units less than 1,400 square feet completed as a percentage of total homes completed for the year ended December 31, 2023.
8. https://www.nar.realtor/newsroom/in-the-news/the-average-age-of-first-time-u-s-homebuyers-is-38-an-all-time-high-cnbc.
9. https://mktgdocs.cbre.com/2299/d2326b89-d7af-4f3c-adc3-6efd270307b3-2034954235/Q1_2025_U.S._Capital_Markets_F.pdf