Marcus & Millichap Capital Corporation

Cap Alert

LATEST DEBT MARKET INFORMATION

July 17, 2020

Assessing the Impact of COVID-19 on Multifamily Assets, Now and Long-Term

Coronavirus infections have risen in 41 states over the past two weeks, with Florida, Texas and Arizona especially hard-hit. States and cities are returning to partial lockdowns and issuing new rules to prevent the spread of COVID-19, threatening a shaky economy. Meanwhile, a difficult deadline looms: The CARES Act federal unemployment assistance of $600 a week, which made it possible for more than 30 million jobless Americans to pay their rents, expires on July 31.

In addition, funds used to support workers' salaries, distributed through the Paycheck Protection Program (PPP), are burning off. Some 84 percent of small business owners who received PPP funds say they will run out by the end of this month, according to a survey released this week by Goldman Sachs. Only 37 percent of respondents said their businesses could survive another wave of shutdowns caused by the virus. Congress returns to work next week to consider an extension of benefits.

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In the near-term, these trends portend a bumpy ride for the multifamily asset class, which has been the darling of investors for nearly a decade. Through April and May, asking rents fell 0.4 percent across the U.S., according to a new report by Yardi. Rents fell in 71 metros, with market-specific issues affecting demand: Las Vegas and Houston were hard hit by slowdowns in the energy sector and entertainment; Nashville and Denver are suffering from a glut of new inventory; and densified cities like New York, Los Angeles, Boston and San Francisco are seeing renters flee for more open spaces, either temporarily or permanently. As demand softens for market-rate luxury units, more owners are reducing rents or offering concessions, the report found. On the upside, rents rose in 35 markets, with smaller towns such as Portland, Maine and Mobile, Alabama leading the growth.

Meanwhile, July rent payments were holding relatively steady. Some 87.6 percent of renters living in professionally managed units made a rent payment as of July 13, down just 2.5 percentage points from a year ago, according to research by RealPage and the National Multifamily Housing Council.

Multifamily is feeling the effects of younger renters moving back in with mom and dad to wait out the COVID-19 crisis. As we move into the fourth quarter, we could see a national vacancy rate as high as of 8 percent, with urban, dense, vertical cities that rely heavily on public transportation bearing the brunt of the exodus. Expiration of eviction moratoriums will likely exacerbate the trend. But longer-term, COVID-19 may be a temporary disruption rather than a fundamental shift for multifamily, according to a Marcus & Millichap special report, part of its series "Beyond the Global Health Crisis." Several key trends continue to support momentum the multifamily asset class, including:

- Americans age 20 to 34 cohort, who make up roughly one-fifth of the population, will continue to have a high propensity to rent.

NMLS: 164121 | AZ Lic: BK-903255 23975 Park Sorrento | Suite 400 | Calabasas, CA 91302 | Telephone: (818) 212-2250

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- The affordability gap between renting and owning remains substantial, making renting a more viable option for many. The softened economy, unsettled housing market, and tighter mortgage standards may delay home buying plans by older millennials.
- As living in a small unit in central business districts becomes less appealing and remote work becomes a norm, suburbanization will likely accelerate. Downtown apartment vacancy rates recently surpassed suburban rates for the first time in 20 years. With a dearth of inventory, potential buyers in suburban markets near major metros are confronting bidding wars.
- Secondary markets are on the rise. Pittsburgh and Richmond and in the Midwest Louisville and Columbus and St. Louis and on the west Denver, Salt Lake, Phoenix and Austin – but a year from now there will be many parts of the country that are doing extremely well and other parts have much higher vacancy.
- The housing market remains undersupplied, even with slowdown in household formations. As the job market bounces back in 2021, the nation will still lack sufficient housing to meet demand.
- As much as $100 billion is sitting on the sidelines awaiting investment in distressed assets. Liquidity is quite strong. Watch for velocity pick up in the fourth quarter. Where we do see price adjustments, it will be driven by net operating income rather than cap rates.

As for the capital markets, we are seeing national banks, life companies, regional banks and credit unions maintaining current levels of lending activity. CMBS is edging back into the market, though price discovery remains challenging. Terms have loosened up a bit for strong borrowers and quality assets in good locations. Lenders continue to favor multifamily, industrial and select retail assets, including centers focused on grocery, banks, pharmacy and quick-service restaurants. Hospitality remains challenging, and senior housing is beginning to pick up. Rates are generally ranging from 3.25 to 4 percent with DSCs of 130 to 135; LTVs are typically 60 to 65 percent, though the agencies are offering up to 80 percent for the right assets.

As more lenders re-enter the market offering historically low rates, MMCC continues to partner with clients and agents to provide the best options for their commercial real estate needs. Contact your MMCC advisor for the latest updates.

RECENT TRANSACTIONS

MULTIFAMILY PORTFOLIO

New Haven, CT
$17,500,000
4.45% Fixed
3-yrs I.O.
10-yr term/30-yr amort.

MULTIFAMILY

Los Angeles, CA
$15,500,000
4.00% Fixed
30-yr term/30-yr amort.
No Reserves

MULTIFAMILY

Sherman, TX
$4,248,000
3.49% Fixed
12-yr term/30-yr amort.
Non-Recourse
Cash-Out Refinance