Multifamily Looks Forward to Increased Deal Flow

Lower rates will provide relief for underwater multifamily loans.

By Philippa Maister

Current trends point to a case for "moderate optimism" about the health of the multifamily sector and the likelihood of increased deal flow, according to Yardi Matrix's August 2024 national multifamily report.

The main reason for this optimism is the Fed's stated intention to begin cutting interest rates. The report noted that there is plenty of dry powder already sitting around with money ready to move into multifamily. However, high rates have discouraged investors from making many moves.

"The increased cost of debt since mid-2022 has produced a large bid-ask spread between buyers and sellers," the report stated. "But 4% yields don't work when mortgage rates are 6%-7%. Buyers generally avoid negative leverage and sellers held on to properties rather than selling at reduced prices."

Even though sales volume was essentially flat at around $33.8 billion in the years ending July 2023 and July 2024, that level was well below the $230 billion recorded in 2021 and the $200 billion recorded in 2022.

However, Yardi cited signs of recovery, like KKR's $2.1 billion acquisition of a Class A portfolio of 18 newly built multifamily assets in growing coastal and Sunbelt markets from a closed-ended fund sponsored by Quarterra Multifamily. Another example is Equity Residential's agreement to acquire 11 apartment properties from Blackstone Real Estate Debt Strategies for $964 million.

Yardi noted that many deals have implied initial yields of around 5%, "which means negative leverage but also a sign that buyers are confident of income growth in the medium to long term." Even though many investors anticipate weak rent growth for another year because of the surplus of multifamily supply in the Sunbelt, they also expect rents to rise again by late 2025 or 2026. Yardi predicted that more deals are likely if rates drop further to align with equity yields.

"Lower rates will also provide relief for some multifamily loans that are underwater due to looming maturity defaults and now have a path forward with five-year fixed agency or CMBS loans. The more rates recede, the less distress there will be," Yardi commented.