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June Landscape Summary "SFR and BFR" May Be Emerging Asset Class"

BY Al DiNicola July 10, 2021

We continue to monitor emerging trends in the alternative real estate investment world. This is accomplished by participation in industry conferences and information exchanges. Over the past few years there has been great interest in the Single-Family Rental (SFR) investment space. There are public companies as well as private REITs that are investing in SFR assets in a variety of locations in the US. (We have already conducted due diligence in several of these offerings). However, there is a tremendous amount of dollars now being directed in this space. SFRs are generally a collection of existing homes, originally held by smaller investors, (referenced as mom and pop) that are being aggregated into larger portfolios of homes. Some of these portfolios are comprised of over 10,000 homes spread over different geographical areas and locations. You may also consider the SFR portfolio having a diversification because of the different locations. The industry has grown up in the past 10 years. It may not be too soon to predict that the current investment into SFRs will transition into DST offerings in the very near future. As an asset class the SFR is steady and with no correlation to the stock market. Basic focus for acquisition of homes will be to follow the jobs and rent growth. The Build For Rent (BFR) is an emerging trend where entire neighborhoods are being purpose built as rental communities. Recently a few fully leased up and stabilized communities in the southwest were sold to a large investment firm and repackaged as a DST offering. This repackaging has enabled smaller investors to take advantage of direct cash investment or 1031 tax deferred exchange investing. The popularity of the SFR rental housing stock continues to increase. Currently this asset class falls under the Multifamily offerings when we report in the Landscape Overview. Prior to student housing and manufactured housing being separated into their own asset classes both were under multifamily reporting.

Driving this SFR/BFR and other housing trends are some basic elements. Some experts believe there is a shortage of housing units as high as four million units and expecting to grow to six million units over the next 10 years. This tight inventory creates a big supply imbalance. This may create a structural housing deficit. For the large institutional investors this creates opportunity. Institutional money is entering the space with a large appetite for steady returns created by portfolios that are well managed. Institutions are risk adverse and continue to look for yields and steady income. Multifamily apartments continue to be a favorite asset class for investors. The SFR/BFR space may represent a "horizontal multifamily" asset class. The SFR/BFR assets operates similar to the multifamily in many ways. There is a property manager who handles the maintenance on the properties, leasing agents, and needed repairs are handled typically by service technicians. With technology today SFR that are spread out over a geographic area, maintenance and service calls are routed much like the Amazon or UPS delivery service. SFR may also benefit from longer tenancy and less move outs helping with down time. However with a 2- 3 year move out average this provides for rental bumps as much as 10% versus the average 3-4% annually. The BFR which are mainly purpose build and located in one neighborhood may have 50 to over 100 homes plus in one location and many have amenities designed for the rental demographic. Some of the newer communities are also gated adding to the popularity and rental demand.

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However, what is fueling the psychological demand of the individual renters for the SFR/BFR rentals? Who are the potential renters? Renters who are seeking locations outside of the urban areas are tired of the threat of crime and are seeking the safety SFR locations may provide. COVID also enabled some workers to move outside the urban areas and potentially work from home part of the week. This pushed the market to remote jobs. The original renters were those who must rent by economics. This workforce housing stock should continue to do well and create lower risk to investor because the asset is backed by rent paying tenants. The typical home may be a 1,500 square foot three-bedroom two-bathroom home in the midwest or southeast built after 1980. Once acquired by the sponsor or investment company, there is typically a capital improvement budget established to improve the living space as well as the structure if needed. The capital improvements also add to the value of the home. The SFR affords for a detached home, back yards and affordability as well as stability. The newer renters are interesting and could fall into two main groups. The BFR are attracting elder millennials (late 30's) who want yards, good schools for their children they expect to have and to be 'out of downtown'. A detached home with a small back yard may be one of the advantages providing a small area for your children or pet. The other group may be the older retired person who does not like living in an apartment and want some degree of separation from a typical apartment. The types of BFR neighborhoods will come in a variety of styles and offer homes as small as one bedroom up to three and four bedrooms. Some of the newer communities offer the same amenities as the Class A multifamily apartments. There is an additional advantage renting affords. Simply put the renters are not tied down to a specific location for a long time. If there is an opportunity to move to another part of the country for opportunity the renters can simply exit at the end of the lease period. If an individual homeowner needed to sell their home, there may be a delay in the sale of the home. Although there is a hot real estate market in many parts of the country that may not always be the case. Renting affords the flexibility for certain people.

As always, we will monitor this and other developing opportunities.

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