Doubling Down on Single-Family Build-to-Rent

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IN SEPTEMBER 2022, WE PUBLISHED A PAPER TITLED "WHY WE'RE BETTING ON SINGLE-FAMILY BUILD-TO-RENT." The paper adopted a historical perspective to analyze the factors contributing to the success of multifamily investments over the past decade and then extrapolated these insights to articulate our conviction going forward for single-family build-to-rent. Our thesis was simple. **With the growing housing shortage, Millennials entering family-forming age, affordability issues in for-sale housing, and institutional interest in single-family rentals, single-family build-to-rent is poised to be a leading real estate investment opportunity of the 2020s.**

More than a year has passed since that initial publication, all the key drivers remain intact, and our thesis is now bolstered further with data and analytics. With this second paper, we aim to outline how recent performance data aligns with and reinforces the investment thesis presented in 2022.

1 Accelerating Demographic Tailwinds

In our September 2022 white paper, we discussed aging Millennials which held a median age of 33 at the end of 2021. Today that median age is approaching 36. 25–34-year-olds in the U.S. are projected to grow more slowly at an annual rate of ‹ 0.5% per annum through 2025, and to decline as a percentage of the total population after that[1]. According to Harvard's "The State of The Nation's Housing 2023" report, "growth in households headed by people ages 35–44 more than doubled from 210,000 per year in 2017–2019 to 560,000 per year in 2019–2022." As these younger Americans get older, their housing preferences are likely to transition from prioritizing walkable amenities over space and security, to larger homes in suburban locations more traditionally attractive to family households.

Source: (1) Green Street

2 Accelerating Capital Deployment

In 2019, John Burns Research tallied approximately $3 billion in total announced equity capital commitments to single-family rental equity investment strategies. By 2022 that number was $27 billion. Since then, build-to-rent investment volume has outperformed other real estate asset classes with 2023 total sales volume outpacing 2019 levels by approximately 40%, while multifamily sales volume in 2023 declined by 65%[2]. Further highlighting this trend of institutional capital flows into single-family rental housing strategies, Blackstone announced January 19th that it is acquiring Tricon Residential, a public company primarily invested in single-family rental homes, valuing the company at a $3.5 billion equity value and $7.5 billion enterprise value. Together with its all-cash purchase of Home Partners of America in mid-2021, **Blackstone has invested more than $9.5 billion cash into single-family rentals in the last ~30 months.** Investor demand for high-quality single-family rental communities continues to escalate, and finite assets available for investment creates an attractive capital markets supply/demand dynamic for property valuations.

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Source: (2) Cushman & Wakefield – The State of Build-to-Rent – December 2023

3 Separation from Multifamily Fundamentals

In the headline metric of revenue growth, single-family rentals in NewStar's primary Sunbelt markets (Atlanta, Charlotte, Jacksonville, Nashville, Orlando, Raleigh and Tampa) are projected to grow 4.7% annually through 2027, compared to apartment revenue growth forecasted to grow 0.9% annually[3]. **The cumulative total forecast for single-family rental revenue growth for 2024–2027 is 19%, compared to 4% for apartments (5x higher). A single-family rental community averaging 4.7% revenue growth for four years, purchased at the same cap rate as a multifamily community averaging 0.9% revenue growth, would deliver a 20% levered IRR compared to the multifamily community investment returning a 3% levered IRR, all else equal[4].**

Beyond revenue growth and IRR's, Cushman & Wakefield's December 2023 "The State of Build-to-Rent" notes build-to-rent communities are averaging substantially more absorption than traditional multifamily measured as a percentage of total inventory: "Since 2020, BTR product has averaged about 3% absorption, topping out at nearly 5% earlier this year, whereas (traditional multifamily) product has averaged 0.6% of its inventory and topped out at less than 2% at the peak in 2021." **Cushman & Wakefield estimates it would take just a year and a half to absorb all of the new BTR construction, compared to approximately four years to absorb new multifamily construction.**

Sources: (3) Green Street market forecasts; (4) NewStar estimates; (5) U.S. Census

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Retention rates are also proving to be superior, with Yardi reporting a 64% average renewal rate for single-family rental homes, which is approximately 10% higher than traditional multifamily. Less frequent turnover of our residents provides savings to maintenance expenses like carpet replacement and painting, as well as reduced downtime vacancy, and supports more stable cash flow for our investors.

Finally, Cushman & Wakefield reports that across their 8,000-home single-family rental portfolio they observe a 2% lower delinquency rate compared to traditional multifamily. This is likely attributable to older, family formation and retirement demographics that typically target single-family rental communities compared to younger demographics that traditionally target apartments.

None of this is particularly surprising when we consider the magnitude of the supply deficit facing single-family housing: more new single-family homes were built and sold in 2001 than in 2022 despite the U.S. population adding approximately 65 million people[5].

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4 Public Markets Signaling

Public REITs often provide an early glimpse to where private real estate values may be headed. Today we see apartment REITs trading at 6% - 7% implied cap rates (6.5% average / 6.7% median across Green Street's apartment REIT coverage universe as of December 2023), compared to single-family rental REITs trading at sub-6% implied cap rates (5.6% average and median). **Further, Green Street estimates Blackstone's acquisition of Tricon implies a cap rate of approximately 5.0%, which would represent a 170 bps / 34% valuation premium to the median multifamily REIT in their coverage.** All else equal, a lower implied cap rate implies that investors have a higher expectation for earnings growth.

Source: (5) U.S. Census

MORE THAN HALF OF U.S. RENTER HOUSEHOLDS ARE NOT IN APARTMENTS. 24 million Americans rent "scattered site" single-family homes, townhomes, manufactured housing, and other rentals[6]—distinctly different from newly constructed, build-to-rent communities—which are typically older vintage (according to the Joint Center for Housing Studies at Harvard, the median home in 2021 was the oldest is has ever been, at 43 years old) and managed by individual mom and pop investors. **Through 2023 only 1,231 build-to-rent communities were operational across the entire country, comprising just 156,981 homes[7]**. As a percentage of apartments, this is less than 1%[8]. As families, individuals, and retirees alike recognize a new and improved rental housing alternative, we believe there will be exceptional demand flows to our single-family rental communities. NewStar invests across the single-family housing continuum, from land development, to build-to-rent development, to our long-term portfolio under Stella Homes.

For information on how to invest with us across our reg D development and 1031 DST offerings, please contact sales@pcsalts.com or 855.330.6594.

Sources: (6) Green Street – 2023 U.S. Single-Family Rental Outlook – January 2023; (7) John Burns Research and Consulting estimates

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About the Author

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Mr. DuPree is Chief Executive Officer for NewStar Asset Management, parent company of NewStar Exchange, which he founded in 2021. Prior to forming NewStar, Mr. DuPree most recently served as an executive for Preferred Apartment Communities, Inc. ("PAC"), a publicly-traded real estate investment trust that was acquired by Blackstone in 2022. From its initial public offering through the company's sale to Blackstone, PAC issued more than $2.6 billion of non-listed preferred stock and paid more than $675 million in preferred dividends, while delivering more than a 3.3x multiple to common stockholders.

Mr. DuPree is a graduate and member of the Urban Land Institute's Center for Leadership and a member of the Young Presidents Organization (YPO). He holds a B.S. in Finance from Wake Forest University in Winston-Salem, North Carolina.

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