

VIEWPOINTS



MULTIFAMILY

Five Steps to Smart Multifamily Investments

Opting for class-B and -C properties might be a smarter bet than investment in new luxury buildings.

Swapnil Agarwal | Oct 10, 2018

Home ownership rates have fallen in recent years due to rising home values and stricter underwriting standards. As a result of this and the increase in the number of people 34 and under—the prime rental age—more U.S. households are renting than at any point in 50 years, according to a study done by the Pew Research Center.

The signs all point to an excellent opportunity for investment in multifamily rental properties. But while the overall outlook may be favorable, it's important to dig a bit deeper to find the most profitable properties for long-term investment. Here are five things to consider before you make a decision:

- 1. A growing market.** Who are the renters? Working-class individuals have traditionally been a mainstay of apartment living, but we now have to consider the millennial generation, consisting of 85 million U.S. citizens born between 1977 and 1996. Whether due to student debt or the delay in starting a family, this large segment of the population is a big factor in the increasing demand for apartments nationwide.
- 2. Investing in a new complex.** In response to the growing number of people who prefer to rent rather than buy a home, new, shiny apartment communities are being built in cities across the nation. However, a survey done by RealPage found that retention rates for these upscale buildings tend to be low, with less than half of the tenants opting to stay when their lease expires. Such turnover results in high expenditures for marketing and unit make-ready in order to attract new tenants. In short, net operating income is low if vacancies are high.
- 3. Increased demand for class-B and -C apartments.** With minimal investment in upgrades and amenities, the older class-B and -C complexes can attract a wide demographic, including working-class individuals and millennials. For one thing, they are generally located in established middle-income neighborhoods. In addition, these apartment complexes are essentially recession-proof, which is important for tenant retention when the economy heads south.
- 4. Lower initial costs lead to greater long-term returns.** Older complexes are often undervalued or overlooked by institutional buyers due to the significant investment in time and resources required to reposition the property. A smart investor will see the opportunity here, since by investing in the right kinds of upgrades and addressing maintenance and safety issues, these buildings can yield greater returns, significant NOI growth and overall capital appreciation.
- 5. The importance of professional management.** Many of these older units suffer from absentee ownership, misalignment between owner and property manager or unsophisticated owners/operators who lack professionalism and an institutional approach. Simply upgrading the units is not enough to improve value; professional property management is essential to protecting your investment. These days, that means more than simply keeping the property clean and attractive, although those things are important; it also means working to make your tenants feel like part of a community. That takes an experienced, professional management team.

Coupling an institutional investment approach with active, hands-on property management is what makes for a successful multifamily investment. Ultimately, if people feel safe and comfortable in their apartment community, they will want to stay—and that benefits everyone.

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