

TUVIA MULTIFAMILY MEMO

Los Angeles Multifamily Market Shift Update

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By: Jason Tuvia

The past 30 days or so marked the beginning of a market shift. Every investor is trying to understand how the Fed's aggressive stance increasing rates affects values and what route to take next. As of this writing most lenders are quoting local multifamily loans in the low to mid 4% range while the 10-year treasury is around 3%. By the Fed's next meeting multifamily loans may be closer to 5%.

How can I adjust my real estate portfolio to combat inflation?

Rent control, especially Los Angeles rent control hurts equity values and cash flow much more when it comes to inflation. This is due to the minimal or nonexistent rent increases rent control enforces. With the inflation rate at 8% and the typical rent control apartment building in LA with flat or low rent growth the net real return is negative.

The best moves to make now would be to refinance any debt that is adjusting in the next few years while rates are not in the 5% range yet. Additionally, exchanges out of rent control into non rent control are very popular trades. They are also proven, with one recent case which we just closed for a client. The client exchanged out of a low return rent control building and exchanged into a 90's construction non-LA rent control building with plenty of remaining upside. This can be done through an exchange into out of state multifamily in markets that do not have rent control, as well as locally into properties that do not fall under RSO. Non rent control buildings ensure investors are keeping up with rent growth and likely inflation while keeping equity growth in the right direction.

Is There a Recession Looming?

There is a possibility of a recession in the near term, however there are many bright spots in our economy today. Some of the bright spots are US corporate profit growth is very positive and there has never been a recession while there is corporate profit growth. Additionally, employment is extremely strong with around 1.7 unfilled jobs for every unemployed individual. The number of people filing for first time unemployment is at historical lows, not seen in over 60 years. This all bodes well for multifamily rent growth.

What are the reasons to keep buying LA multifamily now?

The Los Angeles metro has seen an incredible rent growth over the past year increasing nearly 17 percent. Additionally, renters absorbed over 43,000 units bringing the vacancies down to under 2 percent. Developers finished around 10,000 units for the third consecutive year which has increased rental inventory by only .9 percent and are getting absorbed by tenants at a very healthy clip.

As interest rates on single family homes continue to increase at a faster rate than multifamily loans, home affordability remains at a low for many, keeping most of the tenant base in place. This will continue the demand for Class A and B multifamily.

Who are buying apartments today?

As inflation turns many real returns negative, keeping cash in the bank is the last place to earn a return. While many banks are offering more than 0% now, most offer less than 1%. Today's cap rates are slowly increasing to the mid 4% range, slightly above the cost of capital. There are still multiple bidders on most of our listings who are realizing the compelling reason to stay in the market while they can get positive leverage and keep continue their equity & rent growth through turnover.

Is Inventory Up?

One of the biggest shifts over the past 30 days is the number of available multifamily listings. At the time of writing there are 690 apartment buildings on the market in LA County, which is high in comparison to the past five years. For example, the Hollywood submarket currently has 54 active listings which would normally have 20 -30. As the number of sellers increase in the marketplace there will be certain sellers meeting the market and understanding there is somewhat of a shift while other sellers will hold out for top pricing and more than likely miss out on the market. Most of the sellers today are still doing a 1031 exchange and exchanging back into the same environment albeit out of state or different product type.

Is now the time to exchange into net lease?

Net lease has already seen the start to a repricing which will more than likely continue as the product is heavily tied to interest rates. Their cap rates fell in 2020 and 2021 while rates fell, and demand rose. Now with rates in the 4s and approaching the 5s on net lease, there may be a good entry point soon for multifamily owners wanting a passive avenue out of multifamily. Many of the net lease exchanges I have assisted clients with out of multifamily increased their net cash flow by over 30%. As cap rates trend higher at a faster pace than local multifamily, diversifying into net lease can make sense for certain investors.

Over the next few months, we will be seeing many investors sift their strategy and figure out ways to take a more aggressive stance against inflation. Currently the Fed funds rate is between 0.75% - 1% and the market is expecting the rate to rise between 2.75% - 3% by years end. This alone will get many investors to figure out how to get a net positive return through 1031s, refinancing, or adjusting from value-add capital intensive multifamily to turnkey assets with attractive cap rates.



JASON TUVIA

Senior Vice President Investments
Senior Director - National Multi Housing
Group
Encino Office
Tel: (818) 212-2735
Cell: (818) 448-4415
Fax: (818) 698-8372
jason.tuvia@marcusmillichap.com
License: CA 01772495



Marcus & Millichap
TUVIA GROUP
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TUVIA GROUP RECENT CLOSINGS



325 S WESTLAKE AVENUE
Los Angeles, CA 90057
Submarket: Westlake

PRICE: \$2,400,000
UNITS: 10
PRICE PER UNIT: \$240,000
PRICE PER SF: \$300.00
GRM: 15.16
CAP RATE: 3.77%



639 N CORONADO STREET
Los Angeles, CA 90026
Submarket: Silver Lake

PRICE: \$1,650,000
UNITS: 6
PRICE PER UNIT: \$275,000
PRICE PER SF: \$333.47
GRM: 15.30
CAP RATE: 3.88%



4438 VESPER AVENUE
Sherman Oaks, CA 91403
Submarket: Sherman Oaks

PRICE: \$2,900,000
UNITS: 7
PRICE PER UNIT: \$414,286
PRICE PER SF: \$460.90
GRM: 16.30
CAP RATE: 3.77%



606 & 330 N SPAULDING AVENUE
Los Angeles, CA 90036
Submarket: Melrose / Fairfax

PRICE: \$4,500,000
UNITS: 8
PRICE PER UNIT: \$562,500
PRICE PER SF: \$432.24
GRM: 17.95
CAP RATE: 3.76%



1435 NORTH AVENUE 47
Los Angeles, CA 90042
Submarket: Eagle Rock

PRICE: \$3,800,000
UNITS: 11
PRICE PER UNIT: \$345,455
PRICE PER SF: \$440.43
GRM: 14.28
CAP RATE: 4.61%



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