

Why We're Betting on Single Family Build-to-Rent



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with

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The last ten years have been a true golden era for multifamily investing. Operating fundamentals have performed exceptionally well, driven by demographic tailwinds and a strong economy, and capital flows to the sector have increased investor demand for these properties, compressing sale cap rates and driving up values.

We enjoyed these tailwinds throughout the launch, scaling, and recent sale of Preferred Apartment Communities, a publicly-traded REIT led by many of the NewStar team. Herein we analyze the factors that supported this historic run of performance for multifamily, and share our outlook on the opportunity ahead, and why we are going “all-in” on single family build-to-rent.

The Millennial Factor

Millennials are the largest U.S. population cohort since the Baby Boomers, and for 2012 – 2021 the median age of a Millennial was 23 – 33.* According to the U.S. Census, the median age of first marriage for a male in 2021 was 30, and the median age of first marriage for a female was 28. Millennials are marrying and forming households more than five years later than the Baby Boomers before them.

The delay in family formation drove demand for multifamily apartments over the last decade, with many Millennials opting to rent as opposed to owning a home, preferring urban environments and walkable amenities over family-oriented attributes like space, privacy, and security.

Extraneous Drivers

More recently, as Millennials have reached and surpassed the median age of first marriage, several less predictable factors extended this decade of exceptional multifamily performance:

1

COVID delayed planned moves, and for those that did relocate it was often in favor of our Sun Belt markets, creating a fresh wave of renter demand.

2

The median U.S. home price appreciated 34%** since the start of COVID, forcing many to remain in apartments even as they entered prime family formation years.

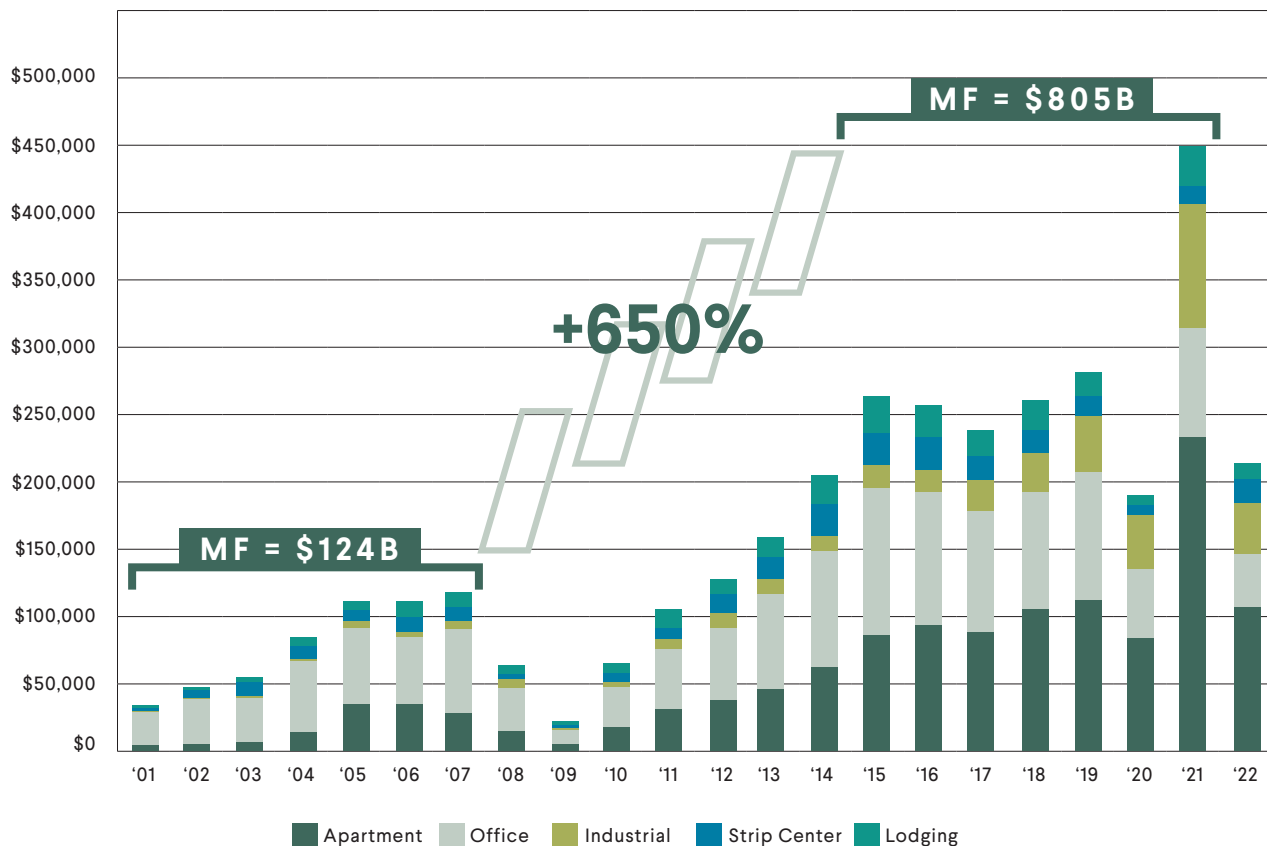
* Source: <https://www.pewresearch.org/fact-tank/2020/04/28/millennials-overtake-baby-boomers-as-americas-largest-generation/>

** Source: <https://fred.stlouisfed.org/series/MSPUS>

The Result

The result of these positive market forces was long-term low vacancy and all-time high rental rates, particularly in the Sun Belt. Strong operating fundamentals attracted more investment in the sector, and capital markets for multifamily investment experienced a transformative institutionalization, leading to expanded liquidity, which in turn reduced borrowing costs, compressed sale cap rates, and drove higher values and investor returns. **We saw firsthand the consequence of this wave of liquidity. Class A apartments we acquired ten years ago priced to initial yields of 6.5% sold later priced to yields of 3.75%. Expanding a sale multiple from 15x to more than 25x is very clearly, and very significantly, accretive.**

TRANSACTION VOLUME BY SECTOR (\$MM)



Source: Green Street

What's Next

It was a great run, but markets move, and our job is to move with them.



The Aging Millennial

Today we look ahead, and the demographic story has evolved, with the median Millennial age now 33 and **100% of Millennials turning 30 by 2026.*** Housing demand is shifting quickly to suburban communities offering more spacious homes that reflect prioritization of those family-oriented attributes – space, privacy, and security – that were secondary through the 2010's.

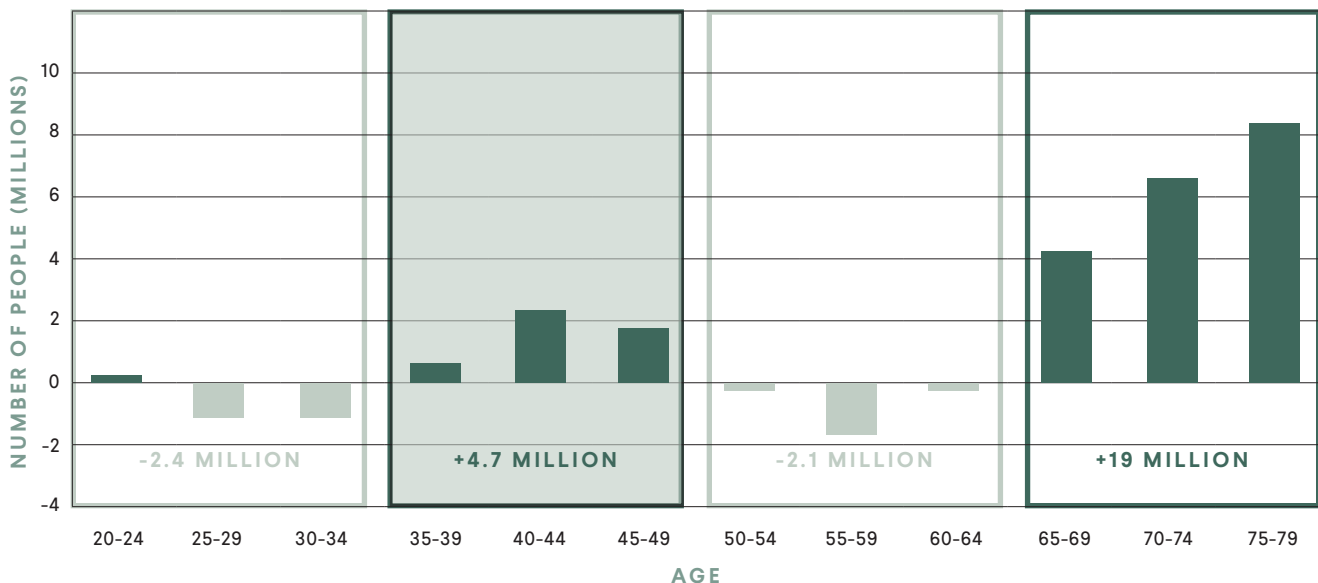
CHANGE IN POPULATION BY AGE 2020-2030

Groups in their 20s will shrink in size, these groups tend to live more urban lifestyles.

Groups in their family-formation years will grow. These groups live a more suburban lifestyle.

A portion of the empty-nester population will go urban. This group is shrinking.

Retirement-age groups will surge. These groups are likely to live a suburban lifestyle.



* Source: US Census



Housing Shortage and Affordability Crisis

Housing supply in these suburban communities has not kept up with the rising demand – **Freddie Mac estimated in 2020 a nearly four-million-unit housing deficit, most acute within the single family category** – and this imbalance continues to grow. **Fallout from the Great Financial Crisis drove key labor and capital out of the single family housing economy. Construction costs are high and zoning boards are increasingly tough on for-rent single family approvals.**

Furthermore, the supply deficit, together with higher mortgage rates, is causing a generational for-sale housing affordability crisis, with the **Wall Street Journal reporting in June 2022 “the worst housing affordability since 1989”**.

The Joint Center for Housing Studies at Harvard University estimated that based on the average down payment required for the median-priced U.S. home in April 2022, **92% of renters could not qualify.**

For-sale affordability challenges drive would-be homeowners to rent single family homes, while costs and entitlement barriers are restricting new supply of that product. We have a long way to go to meet the market need.

Institutional Capital Flows

MetLife Investment Management estimated in a November 2021 white paper that to increase institutional ownership of single family rental property from 2% to 10% would require nearly **\$300 billion** in additional capital to the sector. That feels conservative when considering that by comparison, Altus Group estimates institutions own 50% - 55% of all U.S. multifamily units.* Extrapolating MetLife's methodology, **for institutions to own an equivalent percentage of single family rental units would require over \$2 trillion in additional capital flows.**

Major institutional capital allocators are committing to this new sector – including Blackstone, JP Morgan, Invesco, CalSTRS, Bain and Pacific Life – and since 2020 have announced approximately \$40 billion in new single family rental joint-ventures.** But most of these partnerships remain in the early stages of deploying capital, and relative to the magnitude of the overall capital allocation opportunity, in the hundreds of billions, \$40 billion is a small early dent.

As we've seen before, most recently in the multifamily market, more capital chasing investment drives pricing.

*Source: <https://www.altusgroup.com/insights/single-family-rentals-a-source-of-predictable-cash-flows/>

**Source: John Burns Real Estate Consulting - June 2022

Conclusion

Markets afford investors different opportunities at different times. Multifamily real estate experienced a historic run of performance for the last decade, but successful investing is dependent upon adapting with the market. With a single family housing shortage, Millennials entering prime family formation age, historically challenging for-sale housing affordability, high costs to build and limited labor to build it, and the very early innings of a major institutionalization of the single family rental sector, NewStar, our team and partners, and our 1031 exchange business, NewStar Exchange, are betting that build-to-rent single family rental will be the leading real estate investment opportunity of the 2020's.

NEWSTAR
EXCHANGE

BOONE DUPREE

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.

DANIEL M. DUPREE

Dan DuPree is Chairman of NewStar Exchange. He most recently served as Executive Chairman of the Board of Directors for Preferred Apartment Communities, Inc. from April 2018. Previously, he served as Chief Executive Officer of PAC from April 2018 to December 2019, as Vice Chairman of the Board from August 2012 to April 2018, and as Chief Investment Officer from January 2014 to April 2018. Mr. DuPree has over 45 years of commercial real estate experience in development, leasing and property management. From 1992 to March 2009, Mr. DuPree was President and Chief Operating Officer for Cousins (NYSE: CUZ). From 1982 to 1992, he served as Chief Executive Officer of New Market Development Company, a shopping center management and development company which he founded in 1982.

Mr. DuPree currently serves as Chairman of the Board of Park Holding, Inc., as a board member of the University of Florida College of Business Administration and as a current member and former Board Chair of the Executive Committee of Atlanta Midtown Alliance. He is a member emeritus of the Board of Trustees for The Lovett School as well as the Board of Directors of Breakthrough Atlanta, a nationwide supplemental education program for inner city children. Mr. DuPree has served as an advisory board member of the Wake Forest University Schools of Business and on the Emory University Board of Visitors. He has also served as Capital Campaign Chair of the Atlanta Community Food Bank and Transportation Committee Chair for the Metropolitan Atlanta Chamber of Commerce.

Mr. DuPree received his B.S. in Business Administration from the University of Florida.

JOE GIBSON

Mr. Gibson is a founding partner of NewStar Asset Management and serves as Chief Investment Officer for NewStar and its subsidiaries, including NewStar Exchange. Previously, Mr. Gibson served as Senior Vice President of Investments for Preferred Apartment Communities. At PAC he led the acquisition of more than \$640 million of real estate across the Southeast. Before PAC, Mr. Gibson served as a Vice President at Eastdil Secured, a leading real estate investment bank, where he was involved in the marketing of more than \$4 billion of commercial property across the Southeast. Prior to Eastdil Secured, Mr. Gibson worked for Atlanta-based investment bank VRA Partners.

Mr. Gibson holds a B.A. in Economics from Washington & Lee University in Lexington, Virginia.