The Institutionalization of the SFR Niche

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The single-family rental template is maturing as more large investors buy in.

A new wave of institutionalization is sweeping the single-family rental sector today—a wave that shows no signs of slowing down.

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SFR investing is growing dramatically, as some of the world's largest asset managers dive in or expand their footholds. Major equity investments and commitments totaled $6.3 billion in the first quarter, according to CBRE—dwarfing the $2.6 billion recorded in all of 2020 and $1 billion in 2019. The second quarter of 2021 saw even more activity, with two heavyweights—Blackstone Real Estate Income Trust Inc. and Invesco Real Estate—announcing deals worth a total of $11 billion in June alone.

Why SFR? For starters, millennials are maturing into their prime family-formation years, but home prices continue to outpace incomes. The pandemic, meanwhile, boosted demand for larger homes that can accommodate remote work and placed a premium on flexibilty.

"We're probably in the early innings of institutions looking at this as a real asset class," said Doug Brien, co-founder & CEO of SFR company Mynd, during a recent virtual panel. Mynd, which manages about 8,000 SFR units across 16 U.S. markets, partnered with global real estate investment manager Invesco Real Estate in June with the aim of deploying up to $5 billion to acquire 20,000 homes.

Most analysts believe there is ample room for growth. Institutional ownership—defined as portfolios with more than 2,000 properties—is estimated to account for between 2.1 and 2.5 percent of total SFR units, or 350,000 to 400,000 homes, according to a report published last November by the Altus Group. In multifamily, by contrast, institutions own 50 to 55 percent.

"SFR is in high demand right now and it looks to be in high demand for some time to come," said Jenette Rice, head of multifamily research for the Americas at CBRE. "For investment capital, it's an alternative but something they are very familiar with. It operates like a multifamily property and has professional management, like multifamily."

Rice estimates the SFR market encompasses 15 million homes or 22 million including townhouses. Most of the market is owned by small or mom-and-pop investors, creating a huge opportunity for consolidation and yet a significant challenge for institutions that want to scale up quickly.

Christopher Todd Communities At Stadium, a 313-home property in Phoenix that BTR leader Christopher Todd Communities sold last November, highlights the developer's preference for detached homes that are similar in size to typical multifamily units. *Image courtesy of Christopher Todd Communities*

Booming BTR

Some investors choose the more direct route of investing in portfolios or build-to-rent communities, purpose-built collections of SFR homes that offer on-site management and maintenance. The BTR subtype is growing exponentially, with Rice predicting that inventory will double in the next two years. The vast majority of existing BTR product was built in the last three years, she added.

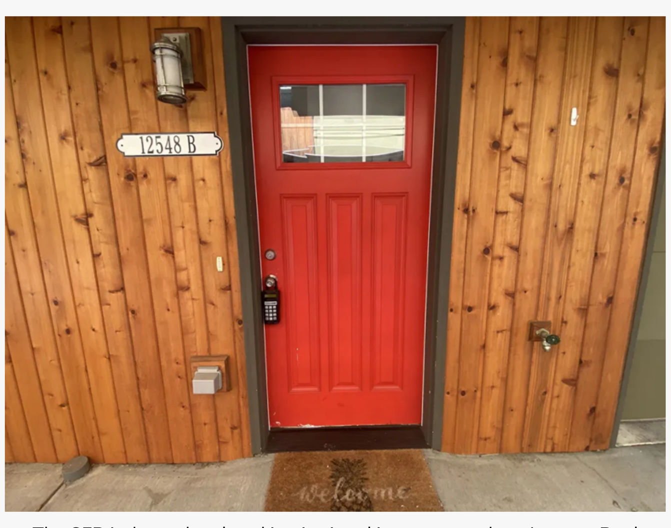
Major players in the space include Toronto-based Tricon Residential, which partnered with Pacific Life Insurance Co. and a global institutional investor in February to purchase about 5,000 newly built homes in the U.S. Sun Belt. The $1.5 billion joint venture aims to acquire finished BTR communities and scattered-site homes.

GTIS Partners, a pioneer in SFR investing after the global financial crisis, has also turned to BTR. It hired new executives for its BTR development platform in June, after breaking ground on a 197-unit single-family, build-to-rent community in Meza, Ariz., last December. The project is part of Cadence, the master-planned development owned by GTIS and Harvard Investments.

"People initially didn't think we were the right way to go and now everyone says this is the best way to go," said Mark Wolf, co-founder & CEO of San Antonio-based AHV Communities, a first-mover in BTR.

Work in progress

Because of the relative novelty, investors and developers often face a steep learning curve. "Like any new alternative, the product type is still evolving, and developers are still trying to figure out what works," Rice noted. "Do you put in really fancy pools?"



The SFR industry has lured institutional investors such as Invesco Real Estate, which recently forged a $6 billion partnership to acquire 20,000 homes across the country. Oakland, Calif.-based Mynd currently manages about 8,000 units in 16 markets from Seattle to Orlando, Fla. *Image courtesy of Mynd*

Strategies vary widely. NexMetro Communities and Christopher Todd Communities, for example, tend to build homes that are similar in size to traditional multifamily units, according to a CBRE research brief. But most other BTR developers offer larger homes averaging closer to 2,000 square feet.

One common pitfall in the industry is "a lack of fundamentals in location," according to Wolf, who noted that many communities are being built a 45-minute drive from the nearest employment hub. "Just because you can build it doesn't mean they're going to come."

Compounding the problem, some participants fail to offer luxury amenities and full-time management and maintenance that might help compensate for a long commute. "A lot of people aren't committed to that execution," said Wolf. "So, it gives you even less of a reason to drive that far out."

Land prices and other development costs also pose challenges, as they do for home builders. Capital requirements are typically higher for SFR properties than for traditional multifamily. Growing competition among investors has also driven down yields over the past year. Cap rates, which hovered about 20 to 50 basis points above multifamily historically, are now in line with multifamily in many cases, according to a presentation by RCLCO Real Estate Consulting.

But competition will also ulimately force the industry to become more sophisticated.

"We're trying to create a positive experience where people can find homes," said Brien. "They can use technology to find it more easily, have lots of choices, streamline the process with self-showings and really make that experience better."

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CBRE, GTIS Partners, Tricon Residential

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