Multifamily Investing After Coronavirus- Historical Resiliency Is Grounds for Optimism

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On March 11, 2020, the World Health Organization (WHO) shook the entire world when they publicly labeled the novel coronavirus (COVID-19) as a global pandemic.

Being at least a year away from a vaccine, the COVID-19 pandemic continues to alter every aspect of our personal and business lives. Here, we will discuss how real estate, specifically multifamily investing, will be affected by the COVID-19 pandemic.

COVID-19 and the Real Estate Industry

The U.S. housing industry is on a bit of a lockdown at the moment. The sales centers of many new developments are empty. Additionally, in the majority of states across the US, real estate agents can't even show properties due to state-wide shelter-in-place mandates. Inspectors and appraisers are currently not working. Even some cash buyers are having a hard time getting appointments, as homeowners are apprehensive about

letting people in their property because they fear getting exposed to the virus. Lastly, a majority of closings that were under contract before the COVID-19 pandemic are currently on hold**.**

Lower Interest Rates

Last month, the Federal Reserve lowered interest rates to zero in an attempt to stave off economic chaos and prevent disturbance in the financial markets. This decision had some multifamily investors rushing to refinance existing holdings.

So, with the lower interest rates, how exactly will the multifamily real estate market perform during the global COVID-19 pandemic? Well, even though real estate has a reputation for being recession-proof, the reality is that no investment, including real estate, is truly recession-proof; let's call it recession-resilient.

How will real estate survive COVID-19

Generally, real estate performs better than other investments during recessions.

For example, in the period Dec. 31, 2000, to Dec. 30, 2016, real estate outperformed the stock market approximately 2:1, returning 10.71% annually compared with the S&P 500 Index's 5.43% annual total return.

Many factors determine if your real estate investment portfolio can survive a recession. This includes the type of real estate investment, market, location, tenant base, amount of debt an investor carries, and the diversity of the portfolio.

The most significant negative real estate impact of the COVID-19 pandemic will undoubtedly be in the hospitality and retail industries. As for the hospitality industry, the short-term nature of bookings translates into immediate impacts when activity declines. Specifically, a substantial decrease in Asian tourism is likely to trigger a short-term decline in hotel occupancies in larger U.S. markets. Retail segments-- such as shopping centers, regional shopping malls, and free-standing retail malls-- are also extremely aware of a pandemic-induced slowdown. If consumers are forced to stay at home for extended periods, foot traffic and sales volume will suffer. Additionally, any economic slowdown might trigger organizations and customers to pull back or even shut down, significantly impacting the retail supply-demand characteristics.

Historically Multifamily Investments Perform Better during a Recession

Compared with other sectors of the real estate industry, expert expects multifamily properties to be impacted less in the immediate future. Multifamily investment properties generally have higher capital and returns on investment than a single-family house.

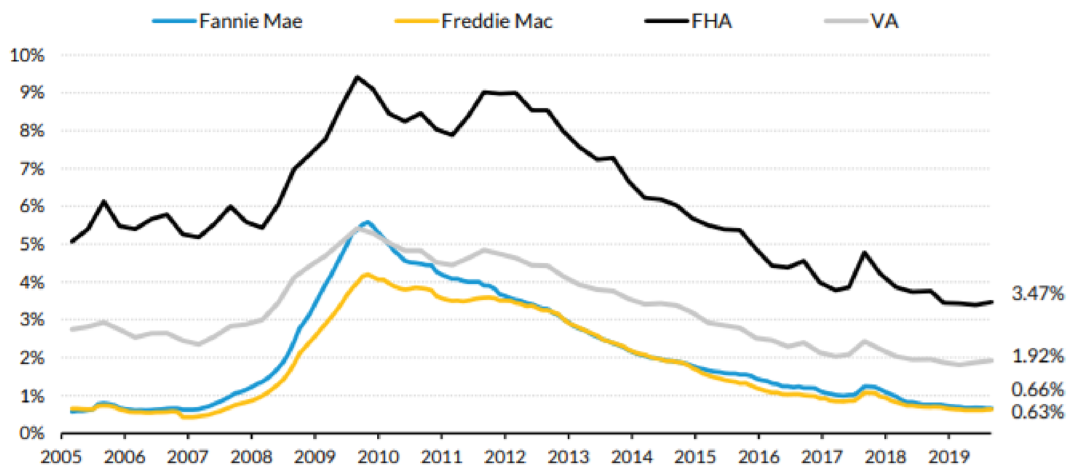
If you have 5 home loans on 5 single-family homes and one is empty, it may be harder to pay your expenses. However, if you have one mortgage on 5 or more units (5 is the minimum number of units to qualify for multifamily) and one is empty, your overall rental earnings will not be affected as much.

With multifamily properties, the cost per apartment will constantly be more affordable than a single-family home in the exact same location. The total purchase price might be higher, but the price per unit will be almost always less than a single-family house.

Overall, multifamily homes are currently cost-effective because they have numerous earnings streams in one place/property. Multifamily homes act like stand-alone businesses. Because there are several income streams, if one tenant is not paying or if one unit is briefly empty, the entire business might still be profitable

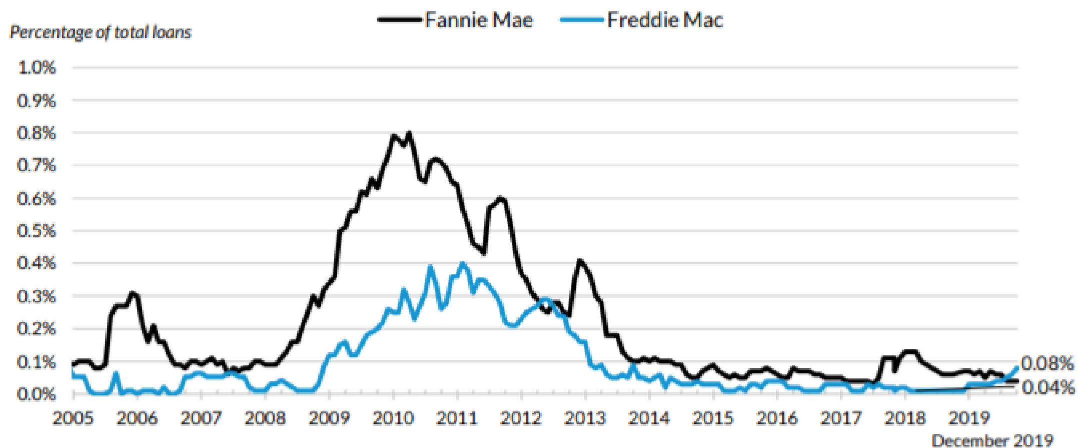
As the economic crises deepen, some property owners will be forced to leave single-family units and move into multifamily properties. Others who were previously planning on vacating a parents' house may also forestall their first single-family house purchase and instead might be looking for an apartment. Overall, you can expect your occupant pool to broaden. In a recession, you might have more overall candidates for empty units.

Serious Delinquency Rates–Single-Family Loans



Sources: Fannie Mae, Freddie Mac, MBA Delinquency Survey and Urban Institute. **Note:** Serious delinquency is defined as 90 days or more past due or in the foreclosure process. Not seasonally adjusted. FHA and VA delinquencies are reported on a quarterly basis, last updated November 2019. GSE delinquencies are reported monthly, last updated February 2020.

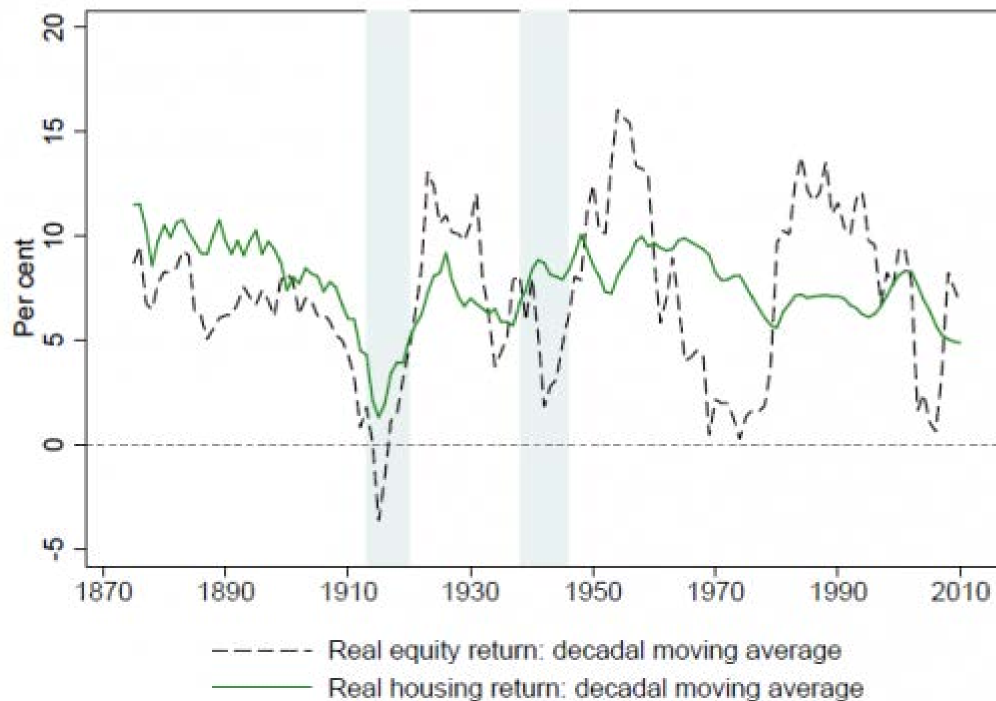
Serious Delinquency Rates–Multifamily GSE Loans



Sources: Fannie Mae, Freddie Mac and Urban Institute.
Note: Multifamily serious delinquency rate is the unpaid balance of loans 60 days or more past due, divided by the total unpaid balance.

Throughout modern history, [residential real estate has enjoyed an extremely high rate of return with low risk](). Notably, at the height of the last recession, multifamily properties had less than .5% serious delinquency rate vs. over 9% for single-family. This could a large majority of single-family loans are FHA.

Take a look at volatility for real estate vs. stock for the past 145 years:



Note: Mean returns for 16 countries, weighted by real GDP. Decadal moving averages.

Overall, the housing condition bodes well in the long term. Job growth and employment rates are significant factors that influence multifamily real estate investing. Thus, if the global pandemic continues for a long time, continued economic turmoil would likely create more financial challenges for multifamily investments as well.

Should you Keep Your Faith in Multifamily Investing?

While cash is king with multifamily real estate investing under normal financial conditions, during a recession, cash flow is even more important. The more income a property can generate only helps to cover its mortgage payments and other property-related expenses.

Diversification in your multifamily investment portfolio can also lessen your financial risk during the COVID-19 pandemic and beyond. Owning assets across multiple markets, industries, and property classes will reduce your risk exposure substantially.

Without a doubt, investors should continue to invest in multifamily properties by focusing on undervalued, value-add opportunities. Smart investors are responding to the COVID - 19 pandemic by positioning their properties through improvements, amenities, and marketing to the best tenants and those who can afford the highest lease rates. This strategy is especially important given the fact that there is a current shortage in housing, where new home starts are not keeping pace with demand.

To charge the highest market rates, investors should diversify investment portfolios by choosing multifamily properties in markets that show population growth, job growth, and employment rates to support higher than average occupancy rates.

The Market will Rebound Eventually

History tells us that the financial markets will eventually recover. And, while it's still too early to assess the full economic impact of the COVID-19 pandemic, during past recessions, the markets stabilized within three to six months on average. The beautiful thing about multifamily investing is that there is a constant demand for housing in growing markets. This is even true for multifamily properties located in lukewarm markets. In secondary markets, investors can still make substantial profits by optimizing their operating strategies to maintain high occupancy rates, reduce vacancies, and lower operating expenses.

With that being said, while it is true that not all real estate investments will survive the COVID-19 pandemic, notably, the hotel and tourism industry, history tells us that the multifamily real estate market will not only survive but may quite possibly come out ahead once the dust settles.

For a video presentation that covers this in even more detail, please check out this YouTube video: https://youtu.be/ZFO98WGuQpY and don't forget to subscribe/like/share!

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