Avid Realty Partners

Avid Analytics

AVID ANALYTICS 01-02-25

"Our democracy must be not only the envy of the world but the engine of our own renewal. There is nothing wrong with America that cannot be cured by what is right with America."

— Bill Clinton

Avid Realty Partners Corporate Update

Avid Realty spent 2024 improving our assets, upgrading our corporate capabilities, and setting the stage for meaningful growth in 2025-2027. 2024 was by all accounts a transition year with most institutional investors still on the sidelines, but nevertheless a year of strong progress. The Avid Realty Partners Team spent the year focused on a few things:

1. <u>We meaningfully improved the operating performance of all of our assets, ending the year at a portfolio average 94% occupancy.</u> Our assets team was also focused on improved collections, rental rate optimization, and expense control, with these efforts flowing through to the bottom line. We did implement a master insurance policy that is driving meaningful cost savings versus prior spending levels. We are extremely focused on execution with the half-dozen assets that remain in our portfolio today and converting that into returns for our Investors;
2. <u>We spent time upgrading our corporate infrastructure and capabilities as we transition into a more institutional platform in 2025-2027.</u> Our Team has been very focused on upgrading our corporate capabilities this year including focusing on enhanced operational execution with our assets, enhanced

capital markets capabilities, and improved financial reporting and accounting functions, among others. The firm is readying to go through the FactRight process on a firm-wide basis to begin onboarding new classes of investors. The firm has made progress on corporate redundancy capabilities, succession contingency planning, and a host of other activities that grow Avid beyond any single individual. Avid has laid the groundwork for its first fund vehicle (though we have not yet launched). All of this work sets the stage for meaningful growth in 2025-2027 and beyond;

3. Avid Recapitalized one deal, co-sponsored a student housing two-pack, and is far down the path of recapitalizing another deal. On the transaction front, Avid did recapitalize one deal, paying investors out a 1.72x equity multiple (net) on a five-year hold transaction, and is far down the path of recapitalizing a second institutional asset in Texas (a roughly $54M transaction). We are generally pleased with these investment returns given the overall real estate environment. Further, we co-sponsored / co-GPed a student housing two pack, a nearly $50M total transaction. While overall transaction volumes are still low, we expect a solid uptick in 2025 and 2026 as market liquidity improves and institutional investors become more active again.

Overall, we are pleased with our Team's progress and hard work in a difficult operating environment, and look forward to harvesting the fruits of these efforts down the road.

2025 Economic and Multifamily Outlook: Our Top 10 List

2025 to be an exciting year of government reform, business growth, falling interest rates, and a comeback in illiquid asset classes like Real Estate and Private Equity; for multifamily, limited new supply will lead to a return to rent growth and stronger fundamentals. There are a lot of reasons Avid Realty's team is excited about 2025, including the prospects of meaningful Federal Government reform and shrinkage there, moving towards a smaller federal government deficit, and greater confidence in the overall economy. We also think that interest rates will fall, and that will spur greater confidence in illiquid asset class investments like Real Estate and Private Equity. For Multifamily in particular, we think very limited new supply and the digestion of rent growth over the past three years means that rents will begin to grow again, concessions will fall, and expense growth will moderate. **Here is Avid Realty Partners' Top 10 List of the forces that will shape the 2025 environment for multifamily apartment investing:**

1. **Trump Administration will begin to implement reform, though with much pushback from the Establishment and Democrats.** The Trump Administration has a once in a generation (or two) opportunity to shrink the federal government (which we think is way too bloated), secure the southern border, and bring fiscal sanity to federal deficits and spending. This is important if the US Dollar is

going to remain the world's reserve currency (bitcoin could take over this position from the US Dollar if spending is not eventually reined in). Obviously, there will be significant push back and obstruction from the DC establishment and far-left Democrats, but we think some of Trump's policy objectives will be successfully implemented. This will lead to enhanced optimism and investment/spending from businesses (in particular) and consumers regarding the overall economy;

2. **#TheFed will cut rates by 50-75 bps as we 'normalize' interest rates, with the 10-Year Treasury exiting 2025 at 3.25%-3.50%.** We think #TheFed will cut rates by another 50-75 bps in 2025 as we 'normalize' interest rates following the Covid-era rollercoaster. We expect the 10-Year Treasury to exit 2025 at 3.25%-3.50%, a decrease of roughly 100-125 bps versus current levels. In general, we think the 10-Year Treasury trades in a 'normal' range of 1.7%-3.0%, as it did from 2011-2019, a time period that is BC (before Covid), but after the Great Financial Crisis. Furthermore, we believe that Uncle Sam is effectively broke with total federal debt to GDP now at 124% versus only 30% in 1980, a QUADRUPLING of the USA's relative debt over the past 44 years! Given this, we do not think Uncle Sam can afford to pay 5% treasury rates anymore, or even 4% treasury rates, and will 'coordinate' with other high interest paying countries (Canada, Australia, UK, France) to lower global AAA-rated paper towards 2.5% over the coming years. In short, we expect lower interest rates from #TheFed to finally filter down to market interest rates, particularly once fears around Trump's tariff actions calm down;

3. **Inflation will continue to modestly decline, despite potential Tarriff actions, and will exit 2025 at 'normal' levels of 2%-3%.** We think that the inflation battle has already been won for the most part, and will be fully won in coming quarters (note, Producer Price Index has been falling the past four months). While Trump's potential Tariff actions do represent a risk, we think these actions will be highly targeted, and will have modest impacts on the overall economy and inflation. We do still see some inflationary pressure in Wages and Rents. Wages continue to 'catch-up' with the overall cost of living, and that could continue for some time still. Rents at some laggard properties have been 'catching up' with big gains seen during Covid in 2021-2022. Also, we expect Rents to generally start growing again after digesting in high-supply markets over the past three years. We expect the takeover of the family farm by private equity shops and other institutional investors could drive some longer-term inflationary pressures in farm products. Net, we think the overall inflation battle has been won, and that The Fed's efforts to shrink its balance sheet via QT will have the intended consequences of keeping inflation low for the foreseeable future.

4. **The stock market will grind higher, though much of the market gains are already behind us.** The US stock market indices are close to all-time highs after running very meaningfully in 2024…nobody can stop that freight train! Indeed, the S&P 500 is now +157% versus its Covid lows of Mar'20 and is +65% versus its rate cycle lows of Oct'22. Meanwhile, the NASD is up even more and is now +184% versus its Covid lows of Mar'20 and is +94% versus its rate cycle lows of Oct'22…wow! While I think equity market valuations are off the charts high, there is nothing on the immediate horizon to derail future gains given Trump is coming into office with business-friendly policies, given interest rates are likely moving lower, and given the inflation battle is largely won. We think corporate profits move higher in this environment, and the stock market will move modestly higher as well, though it is unlikely to see another 20%-25% gain year in 2025.

5. **Institutional Investors will get further off the sidelines and re-enter the investment markets.** With interest rates likely moving lower in 2025, and the stock market at eyebrow-raising valuation levels, we think that bargain hunting in the real estate sector will move a solid number of institutional investors off the sidelines. We think transaction volumes will increase further in 2025 given that there is less uncertainty into the economy and interest rates than there was just one year ago, and given that the world has returned to a more normal working environment. With so many institutional investors still 'on the beach' in 2024, transaction volumes remained low, prices were low, and there was limited demand for new investments. We expect these factors to transition to a more normal capital markets environment in 2025.

6. **Small- and medium-sized operators, and those who overpaid for too much product in 2020-2022, will continue to struggle and lose properties.** Yes, many multifamily buyers purchased over-priced multifamily deals in 2H'20 – 1H'22 when cheap money was plentiful. In fact, nearly anyone that purchased a deal in 2021 or early 2022 overpaid for their deal! Those firms with limited balance sheets, those who were overly aggressive in purchasing deals, and those with a plethora of highly-leveraged bridge debt deals will continue to struggle as interest rate caps expire and 'cash-in' refinances are required. Some of these buyers have used or will use Pref Equity to kick the can down the road (Pretend and Extend) until multifamily prices are at higher levels, while others have given up properties outright. This dynamic has created some buying opportunities, particularly in older vintage assets. Well-capitalized buyers with on-balance sheet cash have generally stepped in to take advantage of this buying opportunity. In short, there is financing distress, bridge debt-related distress, interest rate cap-related distress, and opportunities will continue to present themselves in 2025 at relatively attractive prices.

7. **Multifamily supply growth will fall to a slow trickle.** There has been a LOT of multifamily supply that delivered in 2022-2024, which has impacted top line performance in high supply markets quite meaningfully. In fact, multifamily supply deliveries have been at 50-year highs for most of the past two years. That said, new construction deliveries are now falling to a slow trickle across the country as the construction pipeline delivers the last starts before the interest rate spike of 1H'22. There are still opportunities to purchase brand new construction core-plus multifamily deals at (and occasionally below) cost, and acquisitions at today's prices will look very smart three to five years from now in hindsight. Indeed, this is one of Avid Realty Partners' focus areas for 2025.

8. **Low multifamily supply deliveries will drive improving top line results with better Occupancy, Rental Rates, and Concessions.** The above-referenced supply-boom pressured occupancy rates, rental rates, and concessions in 2023-2024 quite meaningfully in high supply growth markets across TX, FL, AZ, NC, SC, and others. With new supply deliveries slowing to a trickle, we expect that top line performance will improve noticeably in these markets, with improving trends seen in Occupancy Rates, Rental Rates, and Concessions. This will come as a relief to those owners that have been dealing with adverse conditions on the ground (street-fight conditions) for two plus years now.

9. **Improving top-line plus moderating expense growth means that multifamily cap-rates will increase and 'grow into' current pricing.** With the aforementioned improvement in top-line results in 2025, and with inflationary pressures moderating meaningfully, we expect multifamily cap-rates to improve

from current levels (generally in the 4.0%-5.0% range for performing properties on T3 revenues when adjusted for taxes, insurance, real expenses, and replacement reserves) by roughly 50bps. That said, if multifamily pricing starts to move higher then that could be a slight offset to this higher NOI trend. Regardless, in a ‘normal’ operating environment void of the huge Covid-driven swings in supply, revenues, expenses, and interest rates, we generally expect institutional-quality multifamily deals to trade in a 4.0%-5.0% cap rate range over the long-term.

10. **Multifamily prices will begin to move higher, though compelling buying opportunities remain.** We believe that multifamily prices put in a low during late 2023 and 2024, and will begin to tick higher in 2025 as topline performance improves, 10-Year Treasury Rates begin to fall more meaningfully, and institutional investors re-enter the market in greater numbers. We still believe 2025 will present compelling buying opportunities, though generally we believe a bottom has been put in place for multifamily assets already. **Overall, we expect multifamily prices to tick modestly higher, inflation is normalizing in the 2%-3% range, interest rates will move lower during 2025, institutional investors are re-entering the investment market, and NOW is a tremendous and unique opportunity to purchase multifamily apartment deals at attractive prices.**

Inflation Status Check: Much Progress Made, a Bit More Work to be Done

Inflation numbers look good, with only Wages and Rents trending modestly above 3% inflation levels in 2024; PPI index now falling. Overall, we think that inflation trends are quite tame, a positive for lower interest rates and higher real estate valuations in the not-to-distant future. Indeed, we really only see modestly elevated inflation levels in Wages (~4% growth YTD) and Rents (+4.3% growth YTD), with core CPI trending +3.3% YTD. Looking at Producer Prices we see that PPI is +3.2% YTD, however it is actually down ~3% over the past four months which suggests that overall inflation metrics could cool further in the near future. Overall, these numbers are pretty encouraging, which leads us to believe that the battle against inflation has largely been won. Given this, we expect some further normalization of the #FedFunds rate in 2025, which we expect will translate to lower Treasury rates as well.

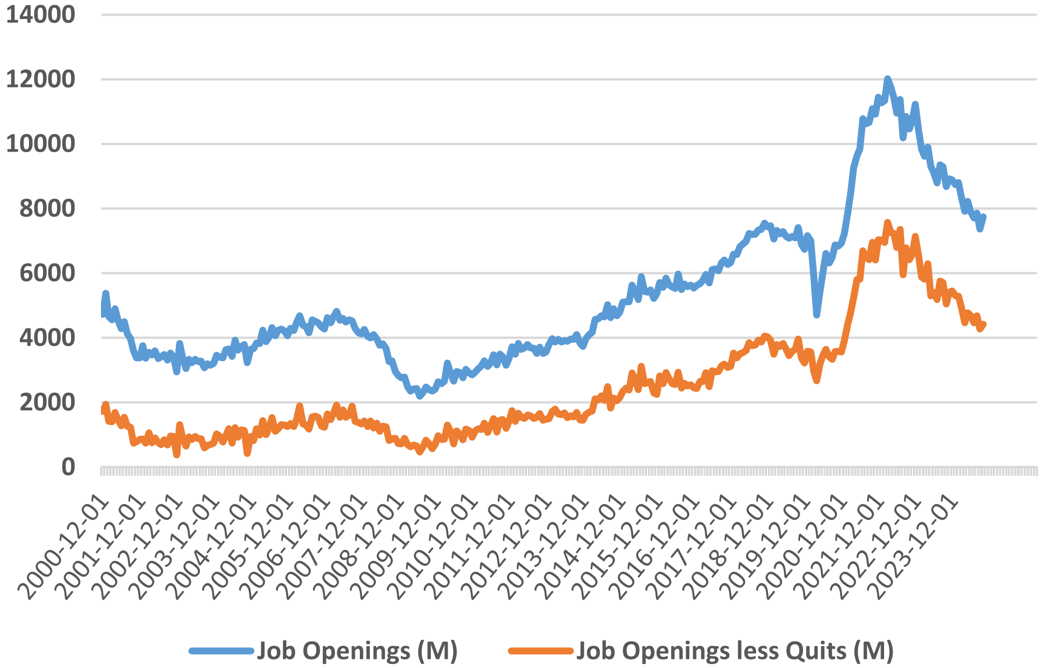
Figure 1. Various Inflation Metrics: Mostly Normal Readings with Wages and Rents Still High

	2019	2020	2021	2022	2023	2024 YTD	Last 4 Months Annualized	Last 3 Months Annualized	Pricing Vs Peak Levels
Headline PPI	1.7%	-0.8%	12.3%	8.9%	0.1%	3.2%	-2.6%	-3.2%	-1.8%
Headline CPI	2.3%	1.3%	7.2%	6.4%	3.3%	2.7%	2.8%	3.0%	Peak
CPI Less Food & Energy	2.3%	1.6%	5.5%	5.7%	3.9%	3.3%	3.6%	3.6%	Peak
CPI - Urban Wage Earners	2.3%	1.4%	7.8%	6.3%	3.3%	3.0%	0.5%	0.5%	-0.1%
Avg Hourly Earnings - Manufacturing	3.1%	2.8%	4.4%	3.7%	5.7%	3.7%	1.8%	3.8%	Peak
Avg Hourly Earnings - Total Private Jobs	3.0%	5.4%	5.0%	4.9%	4.3%	4.0%	4.6%	4.4%	Peak
Rents (Primary Residence)	3.7%	2.3%	3.3%	8.3%	6.5%	4.3%	4.3%	4.2%	Peak
Gasoline (SA)	13.6%	-18.7%	69.4%	-4.5%	-4.0%	-12.2%	-16.9%	-23.2%	-43.2%
Crude Petro (NSA)	19.1%	-24.7%	60.8%	6.5%	-8.0%	-1.7%	-45.9%	-44.6%	-41.7%
No. 2 Diesel (SA)	-0.2%	-2.9%	54.3%	21.0%	-18.5%	-13.6%	-34.7%	-52.3%	-54.2%
Steel Scrap (NSA)	-27.4%	41.6%	37.0%	-30.2%	21.0%	-15.5%	5.7%	8.0%	-37.6%
Steel Mill Products (NSA)	-16.0%	5.2%	128.0%	-29.8%	-3.3%	-10.1%	-6.6%	2.3%	-38.4%
Lumber (SA)	-0.7%	39.1%	18.9%	-23.8%	-7.6%	9.4%	24.3%	25.9%	-39.6%
Industrial Chemicals (NSA)	-5.9%	-2.8%	39.8%	-1.0%	-9.0%	-0.3%	-10.0%	-12.5%	-20.6%
Pharma Chemicals (SA)	1.8%	1.8%	1.3%	1.9%	2.8%	1.7%	3.1%	2.0%	Peak
Meats (SA)	5.9%	-1.6%	21.0%	-0.8%	12.2%	2.8%	5.7%	24.4%	0.0%
Dairy - Whole Milk	11.7%	10.9%	5.9%	12.5%	-4.8%	3.5%	11.7%	9.3%	-1.9%
Farm Products - Grains (NSA)	1.3%	14.6%	43.7%	9.7%	-29.6%	-12.4%	10.8%	34.5%	-47.6%
Animal Feeds (NSA)	0.2%	8.6%	10.5%	14.3%	-6.3%	-5.8%	-5.5%	-3.3%	-12.4%
Motor Vehicles (SA)	-0.1%	0.8%	2.6%	4.7%	0.6%	1.8%	2.8%	3.0%	Peak
Average of Averages	1.1%	4.3%	26.9%	1.2%	-1.4%	-1.4%	-2.0%	-0.5%	-26.1%

Source: Avid Realty Partners

Jobs market and wages have cooled, now helping the inflation fight. Inflation readings on Labor and Wages have cooled over the past 18 months, a plus. But wage pressures are still running slightly hotter than targeted levels given the delayed impact of annual raises and a still relatively tight labor market. The jobs market has weakened somewhat since peaking in early 2022 with Job Openings down 36% from peak levels, a plus for the cooling of the economy and the fight against inflation (where good news is bad news and bad news is good news), but there remains relative strength in the jobs market 33 months into the Fed's efforts to cool the economy. Remaining strength in the jobs market likely supports a 'soft landing' scenario, though many will feel this economy is 'bumpy' nonetheless.

Figure 2. Labor Market Strength Supports Soft Landing Scenario



Source: Avid Realty Partners and fred.stlouisfed.org

__**Fed's inflation target of 2% may or may not be achievable.**__ We do think we have largely won the battle against inflation. That said, the economy may not get to the Fed's 2% targeted inflation levels, we may not even want it to by the way, and inflation may remain in the 2.5%-3.0% range for some time to come. Overall, we see some of the data (Wages, Rent, some farm goods) presenting some ongoing headwinds in the fight against inflation, with a continuing reduction in Fed balance sheet assets and overall government spending levels necessary to really 'win' this fight. As real estate investors operating during a credit contraction cycle, we are hunkering down for the long haul, should it prove to be necessary.

2024 Outlook Scorecard: What We Got Right and Wrong from One Year Ago

2024 a wrap, checking on the status of our predictions from one year ago. 2024 was a continuation of 2023 in many ways with multitudes of institutional investors still on the sidelines awaiting stability and better economic visibility, and with price discovery still very much front and center. Looking back at our 2024 outlook piece from one year ago, we got a number of things right and a few things wrong. Overall we are grading ourselves at a respectable 8.5 out of a possible score of 10, including the following:

1. Correct. **Presidential and Congressional politics will remain highly partisan and nasty, and will suck up much of the oxygen in the room this year.** We are glad America got a president-elect on election night and did not have to wait out some grueling recount process in a number of states. But, absolutely, the election did keep many on the sidelines this past year.

2. Half-Correct: **TheFed will cut rates by 100-125 bps to aid in a 'soft-landing' scenario, with the 10-Year Treasury exiting 2024 at 2.75%-3.25%.** We were correct in predicting 100bps of rate cuts, but were wrong about the market's reaction to these rate cuts, and to Trump winning the presidential election (with the tariffs chatter pressuring rates higher). We were probably 12 months early predicting the 10-year at 2.75%-3.25%. That said, we think the 10-Year Treasury trades in a 'normal' range of 1.7%-3.0%, as it did from 2011-2019, a time period that is BC (before Covid), but after the Great Financial Crisis, and we think the 10-year Treasury is going back to this range in coming years.

3. Correct: **Inflation will mostly be beaten back, but pressures will remain in wages, energy, farm products, and possibly rents.** This is essentially correct, with inflation in the 3.0%-3.5% range, which we consider normal. Wages have been an area of increased pressures as peoples' salaries 'catch-up' to the cost of living. While we do not expect dis-inflation, or falling prices, we generally think prices have stopped going up at an unusual rate, and have essentially leveled-off.

4. Half-Correct: **The stock market will grind higher, though many of the gains are already behind us.** The stock market did move higher, but it moved solidly higher, which is why we are grading ourselves only half-correct on this one. Year-to-date, the S&P500 is up 26%, the NASDAQ is up 33%, and the Russell 2000 (small cap index) is up 11%. Just when I think the stock market is fully valued, it continues to run higher, meanwhile illiquid asset classes like Real Estate, Private Equity, and Venture Capital remain stuck in the mud with capital calls and a lack of recent liquidity events holding investors back.

5. Half-Correct: **Institutional Investors will slowly get off the sidelines and re-enter the investment markets.** More investors did get off the sidelines in 2024, with transaction volumes up versus 2023, but the level of increase was not meaningful enough in many cases. Too many institutional investors still lack conviction, are avoiding taking on any risks, remain in price discovery mode, or simply do not have enough capital and liquidity to be very active even now as we head into 2025.

6. Correct: **Many investors purchased over-priced multifamily in 2021 and 2022, and those with limited balance sheets and deals with bridge debt will feel the pain.** This is correct, with many smaller players or over-leveraged players feeling substantial pain. We have all seen the headlines about Tides Equities or GVA, but there are many other shops that do not make the headlines that are feeling similar pain.

7. Correct: **Distressed debt deals and Pref Equity will see the most activity in 2024, but plain vanilla investment opportunities will make a comeback too.** Pref Equity continues to be the most active form of institutional equity out there for all multifamily deals. Also, many investors have shifted into the credit market as well. As mentioned, plain vanilla equity investments made somewhat of a comeback in 2024, but not nearly as much as we expected.

8. Correct: **Multifamily supply will continue to deliver at a meaningful rate, especially in 1H'24, creating a unique opportunity to buy attractively-priced new construction core-plus multifamily deals.** There definitely has been a LOT of multifamily supply that delivered in 2022-2024, though it has begun to

tail off quite meaningfully in 2H’24 and certainly into 2025. There have been some good opportunities to buy new construction assets at or below cost, though frankly we would have expected to see even more of this product than we did.

9. Correct: **Increased multifamily supply will continue to pressure Occupancy, Rental Rates, and overall financials, while insurance and inflation-driven expenses will compress the bottom line, thus leading to overall asset price rationalization.** This was correct. Many properties have struggled (and are struggling) with both the top- and bottom-lines, with top-line impacts particularly felt in fast supply-growth markets. But, price compression did not match net income compression, leading to too many multifamily deals priced in the 3%, 4% or (if you’re lucky) 5% cap-rate range. As top line trends improve and expenses stabilize, we expect multifamily cap-rates to grow into current pricing levels and more often trend towards 4.5%-5.5% cap rates.

10. Correct: **Multifamily prices will find a bottom, with higher transaction volumes versus 2023, creating a compelling buying opportunity ahead of growth in 2025-2027.** We think transaction volumes did grow in 2024 versus 2023, and that pricing found a bottom in 2H’23 and 1H’24. While prices seem to be up modestly off the bottom, a buying opportunity remains for sizable price gains in 2026-2027.

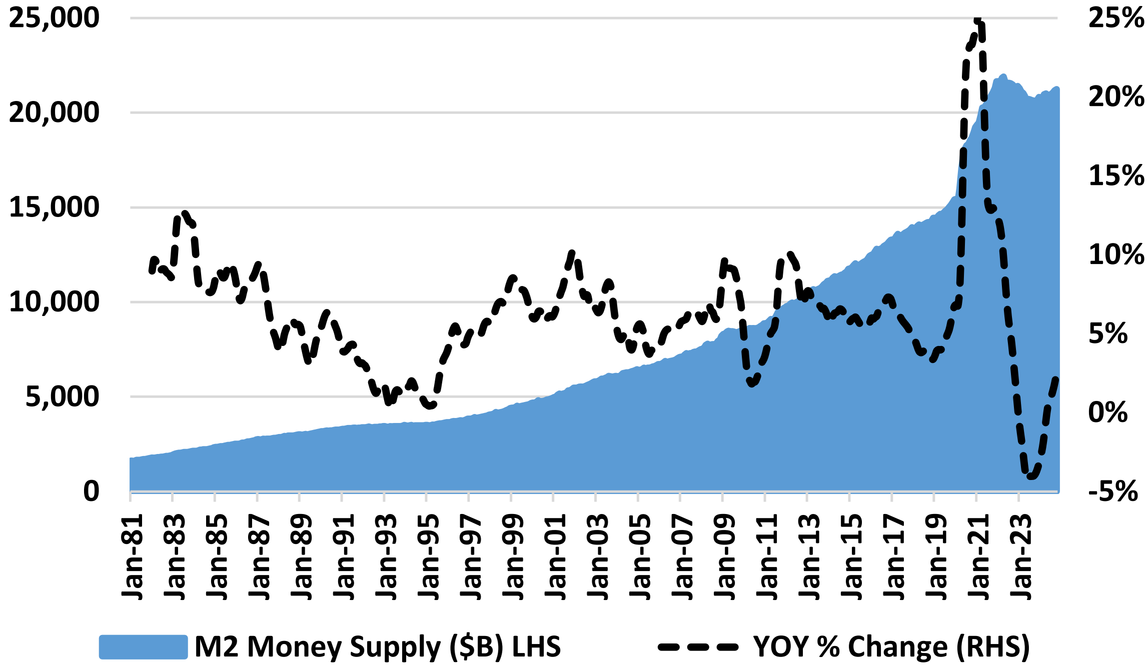
Revisiting the Root Causes of Inflation

Excessive Quantitative Easing and too much Government Stimulus (vote buying) money. We believe that 70%-80% of the root cause in inflation was due to the Federal Reserve’s out-of-control Frankenstein experiment known as Quantitative Easing (QE). As shown below, #TheFed egregiously grew the US’ M2 Money Supply by 43% from the onset of Covid in February 2020 through early 2022. That is 43% growth in US M2 Money Supply in 23 months!! Well, it is no wonder we have had 43% inflation over the past few years!! Other causes of inflation include repeated Federal & State Government stimulus programs, including many that were not needed, and to more affluent people that did not need the funds (some twisted form of politician-driven voter appeasement or vote buying). We think that supply chain bottlenecks accounted for less than 10% of the overall cause of inflation, and the Russia/Ukraine war less than 2% of the overall cause of inflation.

M2 Money Supply and the Federal Reserve’s Balance Sheet are the monetary tails wagging the inflation dog. Did you know that the Federal Reserve grew M2 Money Supply by a reckless 7.75% annually for 15 years running from July 2007 – July 2022? ***Wow, those Fed Governors should not only be fired, but prosecuted for Treason!!*** The below graph shows a couple of things: 1) Growth in M2 Money Supply has been out of control, fell below historically normal year-over-year growth levels for about 26 months with Quantitative Tightening, and is now ramping back towards 3%-4% annual growth as the Fed works to undo some of the damage it has done; 2) #TheFed probably needs to shrink its balance sheet and overall M2

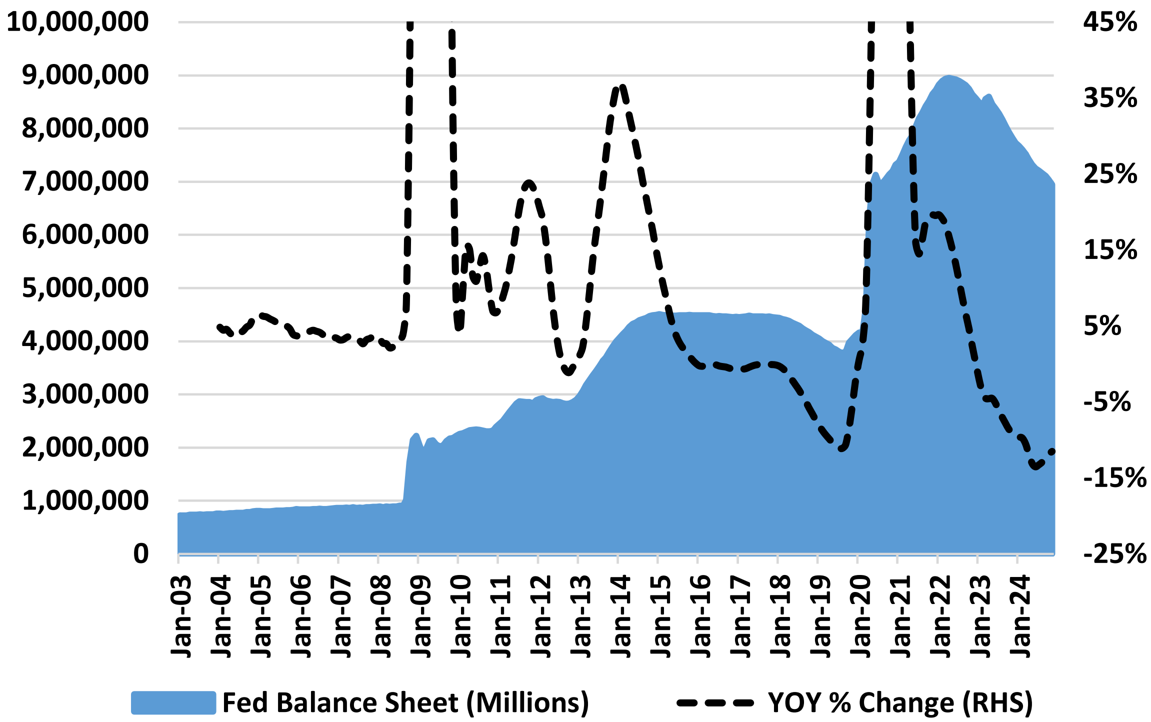
Money Supply aggressively, not just prevent it from growing further if it truly wants to get inflation to its 2% target levels; and 3) The last time growth in M2 Money Supply was over 10% was in the early-to-mid 1970s (through 1977), which spurred its own inflation nightmare in the late 1970s and early 1980s. We note that the Fed has shrunk M2 Money Supply by a somewhat-paltry 3.1% since its peak in Apr'22, and has shrunk it's overall Balance Sheet by a slightly more respectable 22.4% since its peak in Apr'22. This is a reduction of $2.00 Trillion in Fed Assets from peak levels, which is somewhat meaningful, but not really enough considering Congress and the President gave those sums away to affluent voters who did not need it, undocumented immigrants, student loan borrowers, the war effort in Ukraine, and others with the strike of a pen…the Fed needs to do more, and Congress must reign in these spending mishaps!

Figure 3. Growth in M2 Money Supply the Cause of Inflation…QE The Fed's Frankenstein Baby



Source: Avid Realty Partners and fred.stlouisfed.org

Figure 4. The Fed's Balance Sheet Grew Recklessly Fast; Has Fallen 22.4% From Peak of Apr'22

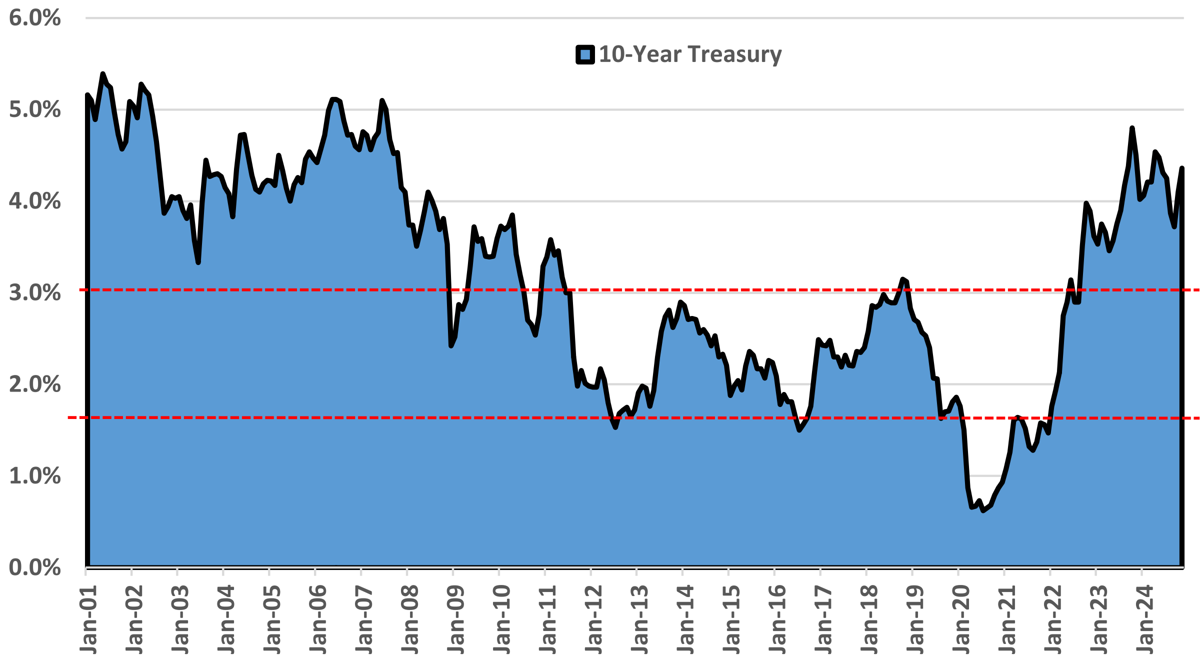


Source: Avid Realty Partners and fred.stlouisfed.org

Interest Rates Likely Going Lower with a 'Normal Range' of 1.7% - 3.0%

So, where are interest rates going? We think lower. As seen below, 10-year Treasury Bonds have traded between 0.6% and 5.3% over the past 21 years. Yes, we know that Treasury Bonds traded at much higher rates in the 1970s-1990s, however, we believe structural changes to the global fiscal and economic system means that society is not going back to those rates any time soon. During the past 22 years, we believe the years from 2012 to 2019 represent 'the new normal' in Treasury Bond pricing, with normalized yields ranging between 1.7% - 3.0%. We think these rates are what Uncle Sam can afford given the USA's growing annual deficits and mounting fiscal debt from entitlements and general over-spending. While the USA's fiscal and monetary policies and positions are not buttoned up, this country is still one of the best houses on a bad block, leaving global investors few choices of better investment alternatives than low-risk US Treasuries. So, in short, we think 10-year Treasury Bonds are going to trade higher, resulting in yields that trend in this 1.7% - 3.0% in coming years. We believe this range is 'the new normal' that will come into effect once we put this inflation debacle further in the rearview mirror.

Figure 5. Treasury Rates Should Now Trade in a 'New Normal' Range of 1.7% - 3.0%



Source: Avid Realty Partners and fred.stlouisfed.org

What does this mean for real estate and multifamily trends? Normalized cap-rates will trend flattish from here. We believe that Treasury Bond rates set the cost of Fannie Mae and Freddie Mac agency borrowing rates, which in turn help set the cap-rates that multifamily deals trade at. So, we think that Multifamily agency borrowing rates are 150bps-200bps higher than 10-Year Treasury Bond rates, which equates to a normalized borrowing rate of 3.2% - 5.0%, with a likely normalized agency borrowing rate in coming years of around 4.2%, give or take. Generally, we think that institutional quality multifamily deals trade in a cap-rate range of Agency borrowing rates +0-75 bps. ***This means that institutional quality multifamily deals will trade in a cap-rate range of 4.0% - 4.8% in coming years.*** Too many investors are underwriting a 6.0% exit cap rate, which we think is too high for institutional multifamily product. If multifamily owners can grow their yield on total cost to 6.5%-7.0% on a five-year hold deal, and then sell near a 4.5% exit cap rate, then we think these deals will be an absolute homerun in retrospect. We continue to think that multifamily prices will go up over the long-term, buoyed by rising construction costs and growing rental rates, and that buying quality deals at a good price during periods of volatility and price contraction (like what we are seeing today), will lead to above average returns over time.

<u>Thank you for reading, Happy New Year, and let us know if you have any questions or thoughts.</u>

---- Craig, James, Mary, Jim, Eddy, Jeff, Luis, Omar, and Sebastian

The Avid Realty Partners Team: Integrity and Experience


HAPPY NEW YEAR
2025