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"America as a Special Bargain for Europeans"

Why rental apartments could profit from the misery in the US housing market

nks. NEW YORK, April 4. In general, the news emanating from the US real estate market would currently tend to have a depressing effect on investors. The price of homes is declining and ever more homeowners are no longer able to make their mortgage payments, leading to foreclosures. As a chain reaction, the mortgage crisis that began with so-called sub-prime loans to less than creditworthy debtors has spawned a global financial crisis.

That wretched situation notwithstanding, there appear to be segments in the US housing market that are disengaging themselves from the general downtrend. As a case in point, the stock prices of real estate companies that invest in rental apartments have so far this year climbed significantly in relation to the general market trend. By contrast, as a result of the financial crisis and the investors' fear of a recession in the United States, the market-wide American S&P 500 stock index has weakened.

This time around, in the opinion of Christopher Finlay, president of Mission Residential, an American real estate investment company that is not listed on the stock exchange, rental apartments will buck even an economic downturn. "This is the best time in 30 years to invest in apartments", Finlay, whose business focuses on multifamily projects in the medium price range, has told us. That, he says, is particularly true for European investors. "The United States is a special bargain for Europeans", says Finlay, referring to the strong Euro as compared to the dollar.

The argument in favor of rental apartments is simple enough: People have to live somewhere. Accordingly, the occupancy rate of rental apartments in the United States has been holding steady in recent years at approximately 95 percent. By contrast, since 2004 the percentage of homeowners has declined from its peak of 69.2 percent at the time to 67.8 percent today. That number, estimates Richard Moody, chief economist at Mission Residential, is going to drop further due to the expected increase in foreclosures. Normally, says Moody, an economic downswing is accompanied by a broad-based slowdown in new home construction. Job losses often cause families to move together or children will delay moving out of their parental nest. Still, Moody expects that in the times ahead an increasing number of Americans will become apartment dwellers. "The turbulences in the home buyers market will force more dispossessed homeowners back into the rental market", says Moody. At the same time, mortgage loan standards now stiffened as a result of the sub-prime debacle make it more difficult for renters to buy a home, which on its part boosts the demand for rental apartments.

Concurrently, fewer apartment complexes were built in recent years than during past phases of economic upturn. That, too, was in part a result of the boom in the home buying market. The loose mortgage granting policies of recent years made buying a single-family home or condominium easy enough. Real estate developers therefore were more restrained when it came to building apartment complexes.

In view of the limited supply and the growing demand, apartment rents will continue to rise, according to the prognosis of Mr. Finlay, Mission Residential's CEO. The prices of multi-family rental properties as well, he says, have been steadily rising.

But then there are skeptics as well, such as Ross Smotrich, analyst at the Bear Stearns investment bank which in spite of its mortgage investments had run into trouble. Smotrich is worried because of the enfeebled labor market which could impact the demand for apartments. Besides, he feels, apartments are competing with unsaleable single-family homes and condos which would now be rented out by their owners. This, he says, is particularly true for regions hit hard by the real estate crisis, such as southern Florida, the area around Phoenix in Arizona as well as Las Vegas. “The landlords in those areas”, says Smotrich, “don’t have much leeway for charging high rents”.

To minimize that risk, Mission Residential is concentrating on growth regions that appear to have disengaged themselves from the general downtrend. These include medium-sized conurbation centers like Raleigh/Durham or Charlotte in the state of North Carolina. Even Austin, the capital of Texas, and Nashville, Tennessee, are considered to be areas of vigorous growth. According to Finlay, “a general economic downturn in the United States does not spell negative growth in Nashville”. So far, Mission Residential has targeted mostly private American investors who have to come up with at least 25,000 dollars to participate in an apartment complex. Finlay wants to expand the percentage of European investors. According to his own statement he is talking to Deutsche Bank and UBS in an effort to reach their well-heeled clientele.

Mission Residential’s planning goes beyond the current crisis stage. In about seven years, says Finlay, the children of the Baby Boomer generation – one of its best-known members being former president Bill Clinton – after graduating from high school and college, will have crowded the job market, and there is also the influx of immigrants, adding to the demand for rental apartments. On his investments in rental property, Finlay expects an average return of 15 percent over a five-year span, which includes rental income as well as the resale of the property. The bottom line for Finlay: “There are US real estate niche markets that continue to be attractive”.

Caption:

New York housing project

Photo by Bloomberg

Author(s): Norbert Kuls (nks)