

Commercial Real Estate Debt

The Rising Cost of Housing



Jennifer A. Marler
Senior Managing Director



William Bennett
Managing Director



Ted Jung
Director

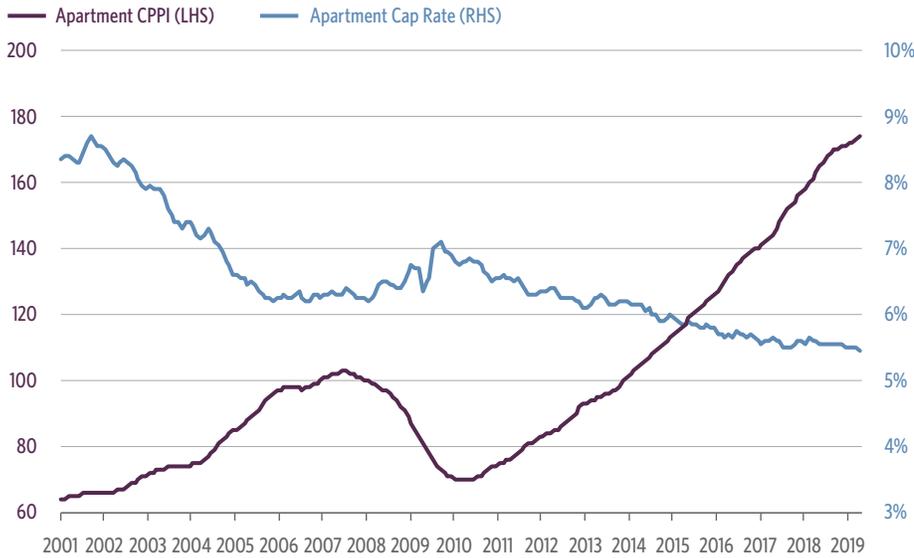
Real estate investors mull the ramifications of rent control.

Over the last 10 years, the multifamily sector has had an impressive run, with asset prices increasing over 100 percent and cap rates falling nearly 2 percentage points (see chart, top right). As multifamily investors evaluate when the current growth cycle for the sector may close, they have another concern beyond the market: rent control initiatives.

Oregon recently became the first state to mandate statewide rent control, capping owners' ability to increase rents annually at inflation plus 7 percent. California, Maryland, New Jersey, New York, and the District of Columbia all mandate some level of state or local rent restrictions, and industry experts predict that other jurisdictions will follow suit. Although many states have laws that prohibit municipalities from controlling rents (see map, bottom right), there is increasing pressure to address the demand for more affordable housing by restricting investors' ability to increase market rents.

In addition to restrictions on increasing rents, some jurisdictions such as New York, which recently made its sweeping rent control provisions permanent, are closing loopholes. In the past, these loopholes allowed a multifamily property owner to bring rents up to market rents when a unit became vacant (vacancy de-control) when the owner invested equity to make improvements to the property, or when a tenant's income rose to a designated "high-income" level. With these changes, the Real Estate Board of New York predicts that owners will no longer have an incentive to invest in rent-regulated units. With uncertainty around how the new restrictions will impact property values, S&P Global Market Intelligence noted that multifamily loan originations in New York declined by nearly 30 percent year-over-year in early 2019. Access to affordable rental housing has become a rallying cry for a number of the 2020 presidential hopefuls, thus rent control is expected to remain a risk factor for multifamily investors. It is also a mandate that is unlikely to solve the fundamental market disconnect when the demand for housing exceeds the existing supply.

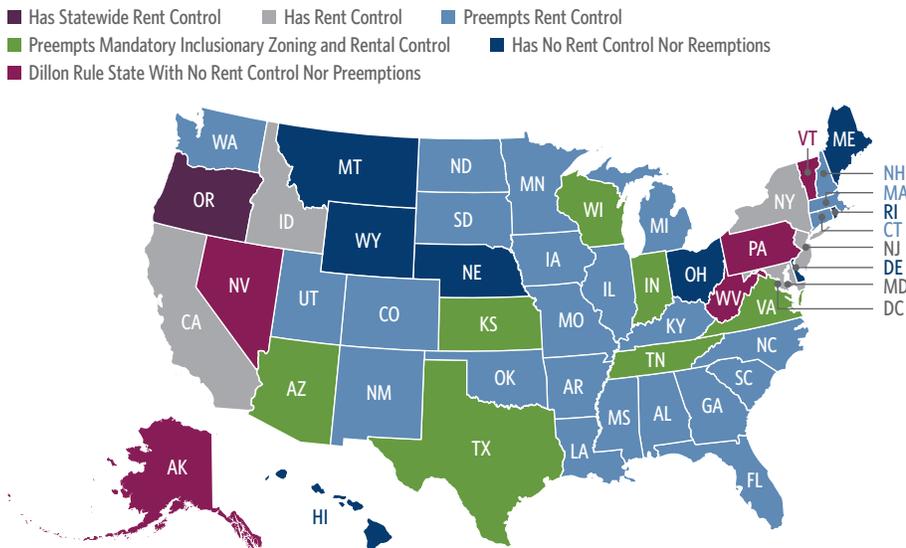
Multifamily Sector Asset Prices Have Doubled in 10 Years



Source: Real Capital Analytics. Data as of 4.30.2019. CPPI: Commercial Property Price Index.

Over the last 10 years, the multifamily sector has had an impressive run, with asset prices increasing over 100 percent and cap rates falling nearly 2 percentage points.

Demand for More Affordable Housing Is Leading to More Rent Control Legislation



Source: National Multifamily Housing Council. Data as of 3.13.2019.

Although many states have laws that prohibit municipalities from controlling rents, there is increasing pressure to address the demand for more affordable housing by restricting investors' ability to increase market rents.

Investing involves risk. In general, the value of fixed-income securities fall when interest rates rise. High-yield securities present more liquidity and credit risk than investment grade bonds and may be subject to greater volatility. Asset-backed securities, including mortgage-backed securities, may have structures that make their reaction to interest rates and other factors difficult to predict, making their prices volatile and they are subject to liquidity risk. Investments in floating rate senior secured syndicated bank loans and other floating rate securities involve special types of risks, including credit risk, interest rate risk, liquidity risk and prepayment risk. Guggenheim Investments represents the following affiliated investment management businesses of Guggenheim Partners, LLC: Guggenheim Partners Investment Management, LLC, Security Investors, LLC, Guggenheim Funds Investment Advisors, LLC, Guggenheim Funds Distributors, LLC, GS GAMMA Advisors, LLC, Guggenheim Partners Europe Limited and Guggenheim Partners India Management. ©2019, Guggenheim Partners, LLC. No part of this article may be reproduced in any form, or referred to in any other publication, without express written permission of Guggenheim Partners, LLC.