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WESTERN REAL ESTATE BUSINESS

MARKET HIGHLIGHT, MAY 2012

LOS ANGELES
By Paul Daneshrad

Los Angeles is always a popular market, but the question is, just who is it popular with? The city is always a beacon for tourists and the entertainment industry, but luckily investors are once again turning toward the City of Angels as well. A few key industries are keeping the city's office market buoyed, while the industrial sector continues to profit from the area's port-adjacent location. Like most of the nation, multifamily properties in Los Angeles are trading at a healthy level, while retail activity is slowly returning.

MULTIFAMILY


Daneshrad

Where is the multifamily market headed? Up. Currently, it is the strongest product type for an investment dollar, and there are a substantial amount of opportunities available. What's the driving force? Multifamily has a strong set of fundamentals that are particularly attractive when compared to other product types such as retail and office on the national front. This market is currently seeing a rental growth in about 70 percent to 80 percent of the nation — with the West Coast and Los Angeles seeing significant growth as well.

In fact, according to the 2012 Casden Multifamily Forecast from USC's Lusk Center for Real Estate, average rents in Los Angeles will increase 7.9 percent this year, with a total growth of 9.6 percent through the end of 2013. Vacancy rates are predicted to rise slightly, with further increases expected next year as rent growth slows.

In California, most of the coastline has seen rental growth from 4 percent to 8 percent, making it a relatively healthy sector. Additionally, we're expecting to do about $150 million to $250 million in multifamily acquisitions in 2012 and tailing into 2013. Although this is on the lighter side for us, it is expected because of precautions we are taking against possible risks.

The greatest opportunities in the Los Angeles market can be found in the value-add sector. Although some have strayed away from value-adds in favor of core products that may be more stable, the multifamily and value-added side of the business is actually where one can get double-digit internal rates of return.

These fundamentals are expected to remain strong. Demographics are showing a shift in a certain cohort of 19- to 35-year-olds moving into the renters' stream. This trend is expected to continue. This indication is a very positive force for multifamily. It's also a good sign of not only stability, but of demand moving forward. Another demographic shift we're seeing is the buyer-owners transitioning into renters. There is definitely a segment of the population from the Great Recession that has realized that maybe the American Dream is not owning a home, but instead enjoying the freedom, comforts and flexibility that renting allows.

What does that mean for the real estate investor? When you have those kinds of demographic shifts, it creates demand and stability that ultimately generate a higher rate of return than some of the other product types. These two demographic shifts can add anywhere between 300 to 400 basis points to the internal rate of return of a multifamily asset, which is unlikely to happen in office or retail. The end result is that multifamily product will remain a strong asset for the investor.

— Paul Daneshrad, CEO, StarPoint Properties in Beverly Hills