NEWS CoStar

Developers Expanding Single-Family Build-for-Rent Market

Forecasters Expect Influx of Residential Builders into Single-Family Rental Space

By Randyl Drummer
March 10, 2016

AHV Communities' recent acquisition of a 92-lot site near Austin, the first project in a $100 million commitment to build single-family rental communities in major Sunbelt markets in 2016, underscores a rising trend by residential developers: construction of single-family homes tracts targeted specifically at renters.

The Village at Vickery Grove in San Antonio is the first single-family rental community developed by AHV Communities. AHV announced that Park on San Gabriel near Austin will kick off a $100 million commitment to single-family rentals.

Build-to-rent development has emerged over the last year to become one of the hottest new segments of real estate development, with privately held companies as well as the largest publicly traded developers and acquirers of single-family rentals jumping into the market.

Multifamily builders and investors frustrated at high apartment prices and shrinking yields appear to be helping drive the nascent build-to-rent trend.

Mark Wolf is a prime example. Wolf, who serves as CEO and co-founder of Newport Beach, CA-based AHV Communities, is a veteran apartment investor and developer who has been involved in buying or building 12,000 apartments units totaling $3 billion over the last 20 years in his previous positions at Newport Beach-based Greenlaw Partners and capital provider Sicuro Realty Partners.

"I got sick of trying to buy apartments at 4.5% and 5% caps and losing out to big institutions that were parking money in large portfolios," Wolf tells CoStar, explaining why he and partner Spencer Rinker formed the company in 2013. "I figured I can build single-family rentals myself and get better yields on a risk adjusted basis, versus apartments," he said.

While AHV is a pioneer in the emerging buiuld-to-rent market, a few merchant homebuilders have also entered the single-family rental market over the last year, led by the nation's second-largest residential developer, Lennar Corp., which opened its 80-home Frontera rental community in a suburb of Reno, NV, in March of last year.

Lennar Corp. CEO Stuart Miller told investors last month "we're still in the experimentation phase" of offering single-family rental masterplans, which he described as a hybrid between Lennar's for-sale and multifamily apartment communities.

"We expect to expand on that platform as we go forward, though there are still some complications in terms of the financing of those kinds of communities," Miller said. "But we think it's a really unique opportunity that rides right between our for-sale single-family operations and our multifamily rental operations."

Lennar, D.R. Horton and KB Homes are among at least a dozen residential builders to get into the business, in some cases selling rentals to the largest publicly-traded single-family rental owners, including Starwood Waypoint Residential Trust, which merged with Colony American Homes on Jan. 5 to create the $7.7 billion Colony Starwood Homes (NYSE: SFR).

AHV, however, is one of the few developers to focus entirely on single-family rental construction, though Wolf and other industry observers expect an influx of investors into the space in coming years due to the large and rising demand for rental homes by millenial families and others unable or unwilling to assume a home mortgage.

"We're the only ones building fairly large tracts of cohesive, continuous units with amenities," Wolf said. "We're taking a very multifamily-centric approach, providing community, value, amenities and service similar to what renters get in an apartment community."

Wolf expects more investors will gravitate to single-family development.

"It's no different that the apartment market, where investors have tried to buy current cash flow, but the cap rates are so low they can get better yield by building new," he said. "The same thing is happening now in the single-family market."

For years, home builders ignored the rental market, which makes up 10% of all single-family housing demand, according to John Burns of John Burns Real Estate Consulting. Burns noted that 29% of the nation's 44.3 million renter households rent a detached single-family dwelling, with another 6% leasing condominiums or townhouses.

"These 12.7 million detached home renters have largely been ignored by builders and developers for years as both supply and demand steadily grew over many decades," Burns said in a recent report.

That's changing as developers identify and seek to meet rising SFR demand as sales of existing homes shrink the inventory of homes available for rent.

"In 2014 approximately 25,000 detached homes were built for rent. We believe that number will increase significantly over the next several years," Burns said. "We expect detached homes for rent to become an important segmentation opportunity for the top masterplans in the country, who will no longer ignore 10% of housing demand."

In addition to its Park on San Gabriel, a community of 92 luxury detached rental residences in Georgetown, TX, near Austin. AHV Communities is targeting high-growth, low-barrier markets such as San Antonio, Nashville, Charlotte and Denver.

The value proposition of SFR development is more challenging in larger, more expensive housing markets, including Southern California, Wolf said. Land and carrying costs are prohibitively high in the coastal markets, where it can take from two to four years to move a project from the entitlement stages to construction.

"It's not easy task to underwrite land for single-family rentals that pencils out," Wolf said. "In some cases, rents would have be $5,000 a month to achieve a yield of 4.5% to 5%."