

Residential REITs

BofA Apartment REITs cap rate analysis

Industry Overview

Cap rate analysis for Apartment REITs

In this report, we track private market cap rates for apartments using Real Capital Analytics (RCA) transaction data by MSA. We then overlay these cap rates onto each Apartment REIT's geographic exposure to build up to a portfolio wide private market cap rate. We then compare this private market cap rate with BofA's applied cap rate and the market's implied cap rate.

Our Apartment models reflect a rise in cap rates

Since October 2022, we have increased our applied cap rates by +156bp on average. Since October 2022, the market implied cap rates on Apartment REITs have increased +120bp on average. We note that 3Q23 private market cap rates are +77bp higher than 3Q22.

Public vs private market cap rates have disconnected

The spread between private market and market implied cap rates has widened significantly since 2022. Across our REIT coverage the average spread is +219bp. That compares to the average spread of -3bp from 2011-19.

The spread over the 10-year Treasury has narrowed

The spread between private market cap rates and the 10-year Treasury has narrowed significantly. The narrowing spread has been driven by rising interest rates. Private market cap rates have adjusted by a much smaller degree. Across our REIT coverage, the average spread is +8bp. That compares to the average spread of +300bp from 2011-19.

Private market cap rates remain sticky

The latest commentary from REIT management teams supports cap rate ranges of mid 5s. Please see inside for cap rate quotes from the 3Q earnings calls.

Summary table of Apartment REIT cap rates

Exhibit 1: Private market cap rates vs implied cap rates

The public market assures private market cap rates will increase

Ticker	BofA Applied cap rate	Public market Implied cap rate	Private market cap rate			Spread
			October	3Q23	2022	
AVB	6.5%	6.8%	5.2%	5.2%	4.2%	158bps
AIRC*	n.a.	7.0%	4.8%	4.8%	4.3%	220bps
CPT	7.2%	7.7%	4.9%	4.9%	4.3%	285bps
EQR	6.3%	7.2%	5.1%	5.1%	4.2%	210bps
ESS	6.3%	6.4%	4.5%	4.6%	3.8%	190bps
IRT*	n.a.	8.1%	4.9%	4.7%	4.3%	325bps
MAA	7.2%	7.2%	4.7%	4.6%	4.0%	251bps
UDR	6.7%	6.9%	5.2%	5.1%	4.2%	170bps
VRE	6.5%	7.6%	6.0%	5.9%	5.0%	164bps
Avg	6.7%	7.2%	5.0%	5.0%	4.3%	219bps

Source: RCA analytics, company filings, S&P Global

Note: *Cons implied cap rates for REITs not covered. Spread is public market implied cap rates minus the latest private market cap rates

BofA GLOBAL RESEARCH

28 November 2023

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United States
REITs

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Key terms used:

Applied cap rate: The cap rate we apply to a REIT's NOI stream to build up to our Net Asset Value (NAV).

BP: basis points

Cap Rate: capitalization rate

Implied cap rate: The public market's implied cap rate based on the equity market capitalization.

MSA: Metropolitan statistical area

RCA: Real Capital Analytics

10 TSY: 10-year Treasury yield

Definition: Private market cap rates are calculated using the Apartment REITs' 2Q23 portfolio geographic exposure by MSAs and RCA's latest private market cap rates by MSAs. Using the geographic exposures as weights, we calculated a weighted average by overlaying the private market cap rates from RCA.

What you will find inside the report: (1) REIT portfolio cap rate analysis, (2) Gateway market cap rate analysis and (3) Sunbelt cap rate analysis.

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Timestamp: 28 November 2023 12:01AM EST

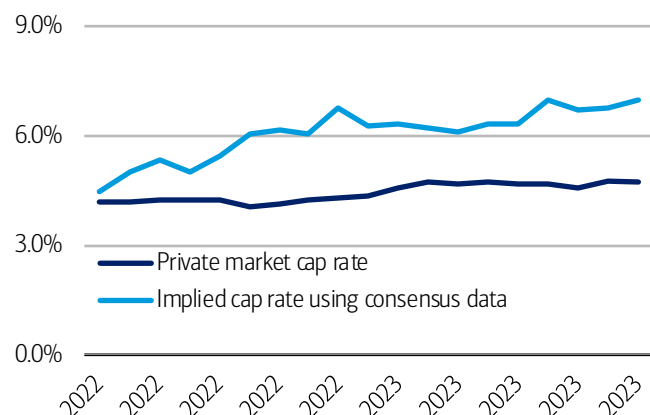
Latest cap rate commentary from REITs

- **EQR:** "So it seemed like over the summer, things were settling down to, say, 5.25%, maybe even a 5.5% cap. The last 60 days have changed that a lot. With the spike in the tenure, it's really uncertain what the market is doing right now. So you hear about transactions closing, but those reflect pricing from the summer, not from right now. So we're all feeling it out. So there are properties -- limited number of properties on the market. No one knows exactly what cap rate reflects what the seller is willing to give up and what a buyer thinks is appropriate returns. So it's definitely upward pressure on cap rates."
- **MAA:** "And while closed transactions are limited in number. We continue to see some upward pressure on cap rates on projects we track. With cap rates up by roughly 15 basis-points from 2Q." "And so and we're still seeing cap rates in the low 5% range for those well-located assets."
- **UDR:** "Today, cap rates are in kind of that mid-to-high 5s range based off a limited transaction volume that is out there in the market."

REIT cap rate analysis

Exhibit 2: AIRC: private market vs implied cap rates

Private market and implied REIT cap rates typically track each other

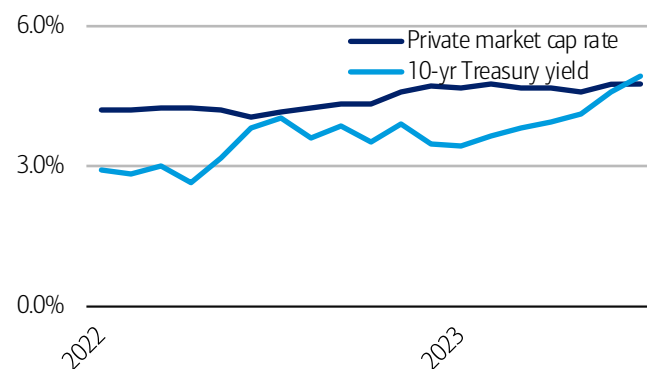


Source: RCA analytics, S&P Global for consensus implied cap rates

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Exhibit 3: AIRC: private market cap rates vs 10-yr Treasury

Private market cap rate spreads over the 10yr averaged 301bps (2011-2019)



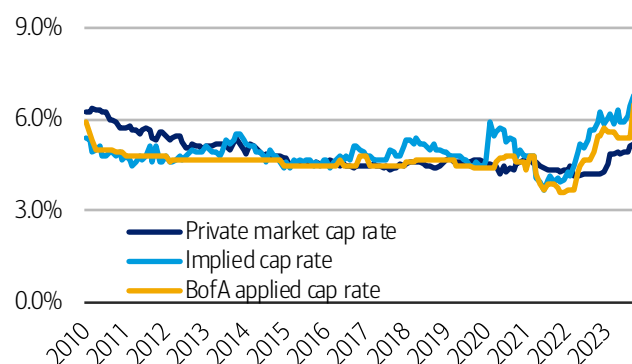
Source: RCA analytics, company filings, Bloomberg

AIRC split off on 12/3/20. We show the private market cap rates before the split off to highlight cap rate compression across their market

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Exhibit 4: AVB: private market, implied and applied cap rates

Private market and implied REIT cap rates typically track each other

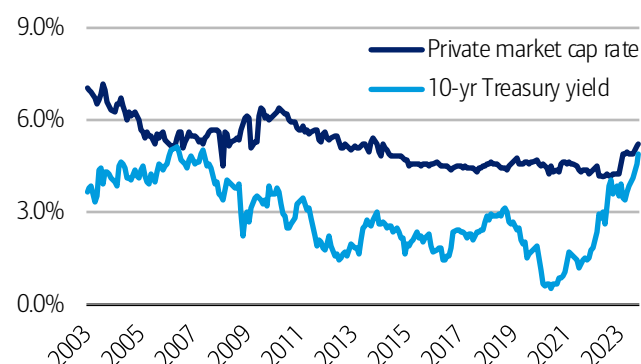


Source: RCA analytics, company filings

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Exhibit 5: AVB: private market cap rates vs 10-yr Treasury

Private market cap rate spreads over the 10yr averaged 258bps (2011-2019)

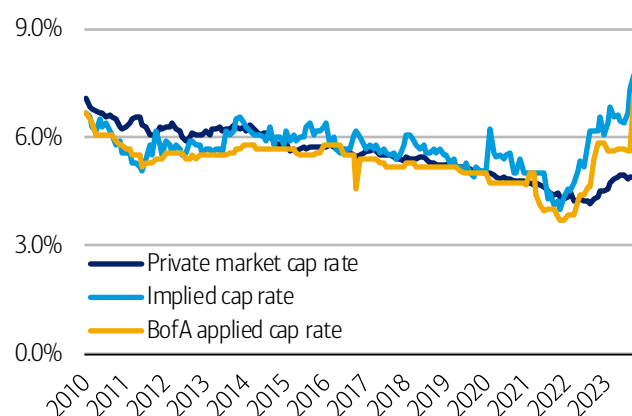


Source: RCA analytics, company filings, Bloomberg

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Exhibit 6: CPT: private market, implied and applied cap rates

Private market and implied REIT cap rates typically track each other

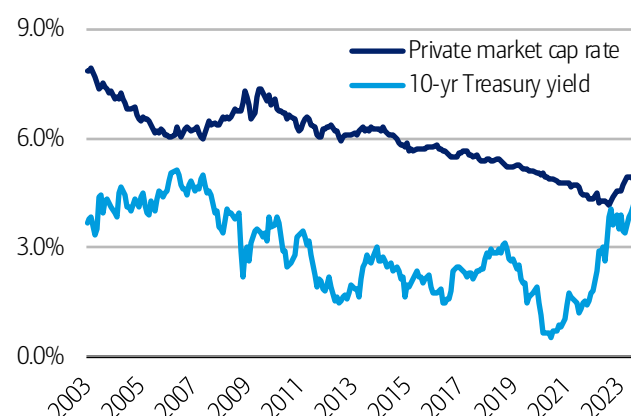


Source: RCA analytics, company filings

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Exhibit 7: CPT: private market cap rates vs 10-yr Treasury

Private market cap rate spreads over the 10yr averaged 353bps (2011-2019)

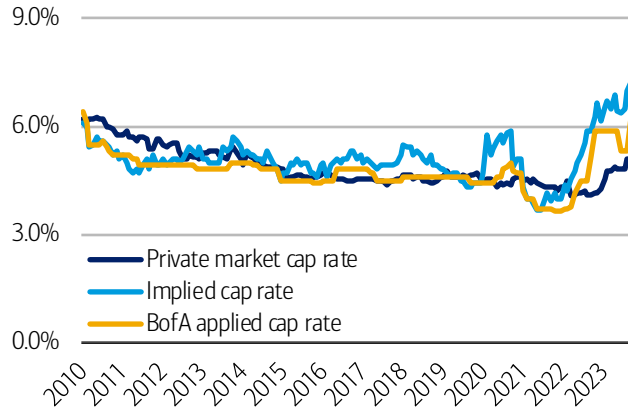


Source: RCA analytics, company filings, Bloomberg

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Exhibit 8: EQR: private market, implied and applied cap rates

Private market and implied REIT cap rates typically track each other

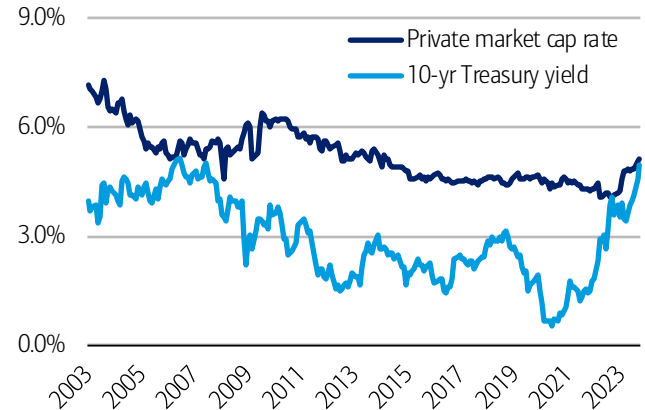


Source: RCA analytics, company filings

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Exhibit 9: EQR: private market cap rates vs 10-yr Treasury

Private market cap rate spreads over the 10yr averaged 262bps (2011-2019)

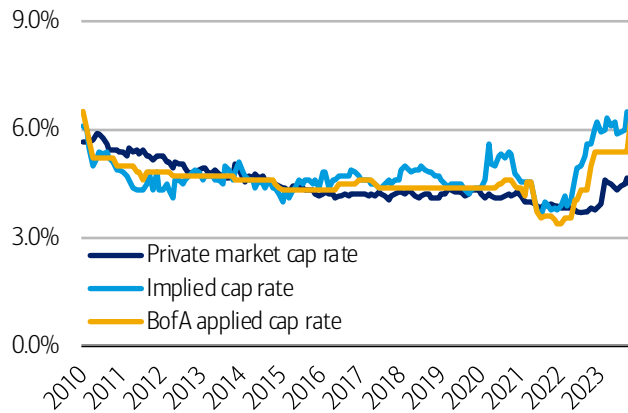


Source: RCA analytics, company filings, Bloomberg

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Exhibit 10: ESS: private market, implied and applied cap rates

Private market and implied REIT cap rates typically track each other

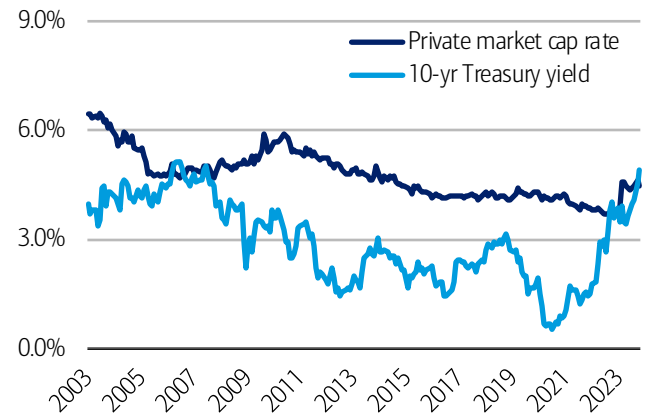


Source: RCA analytics, company filings

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Exhibit 11: ESS: private market cap rates vs 10-yr Treasury

Private market cap rate spreads over the 10yr averaged 227bps (2011-2019)

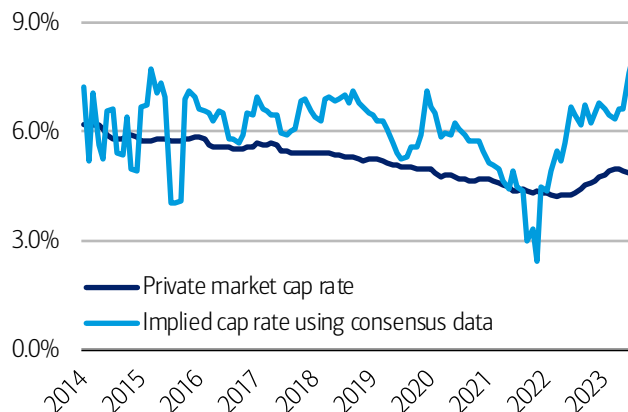


Source: RCA analytics, company filings, Bloomberg

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Exhibit 12: IRT: private market vs implied cap rates

Private market and implied REIT cap rates typically track each other

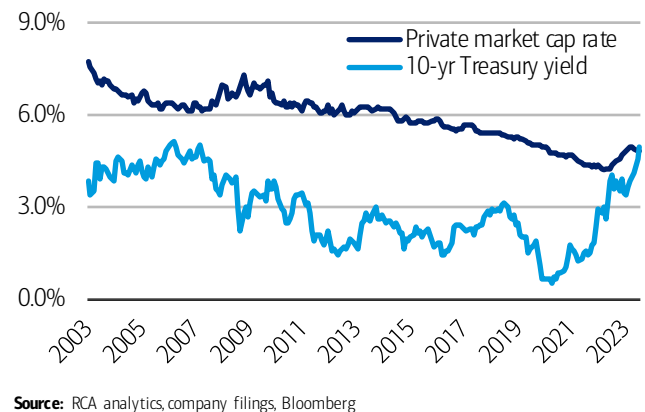


Source: RCA analytics, S&P Global for consensus implied cap rates

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Exhibit 13: IRT: private market cap rates vs 10-yr Treasury

Private market cap rate spreads over the 10yr averaged 355bps (2011-2019)



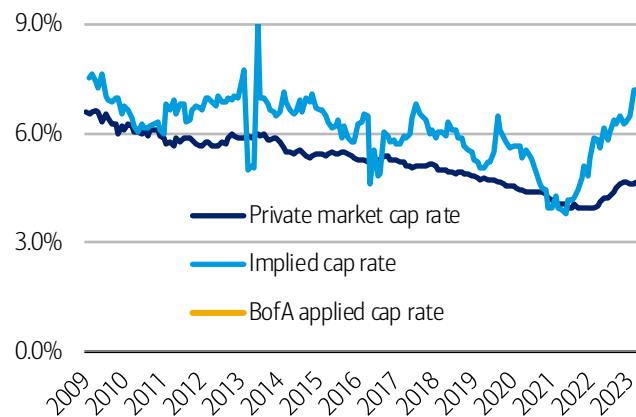
Source: RCA analytics, company filings, Bloomberg

IRT IPO-ed on 8/13/13. We show the private market cap rates before the IPO to highlight cap rate compression across their market

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Exhibit 14: MAA: private market vs implied cap rates

Private market and implied REIT cap rates typically track each other

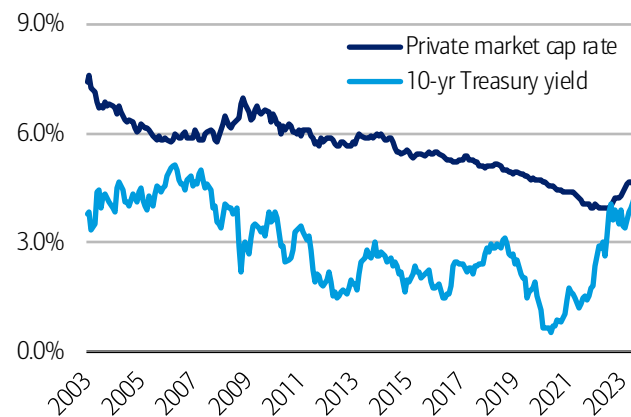


Source: RCA analytics, S&P Global for consensus implied cap rates

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Exhibit 15: MAA: private market cap rates vs 10-yr Treasury

Private market cap rate spreads over the 10yr averaged 321bps (2011-2019)

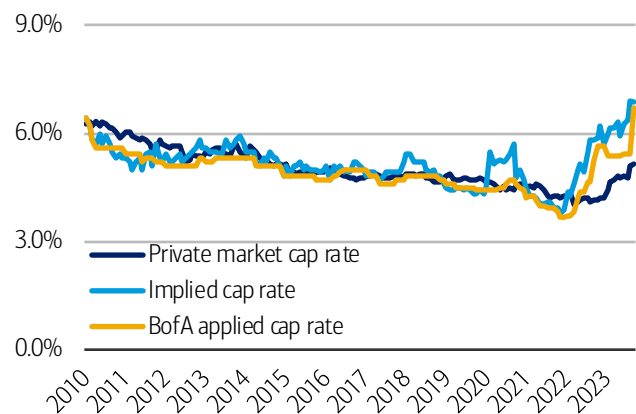


Source: RCA analytics, company filings, Bloomberg

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Exhibit 16: UDR: private market, implied and applied cap rates

Private market and implied REIT cap rates typically track each other

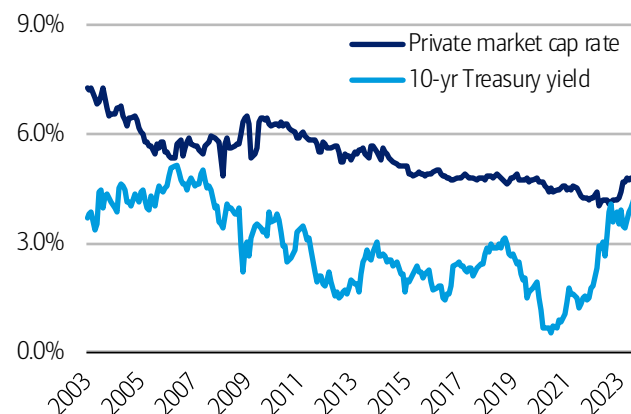


Source: RCA analytics, company filings

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Exhibit 17: UDR: private market cap rates vs 10-yr Treasury

Private market cap rate spreads over the 10yr averaged 286bps (2011-2019)

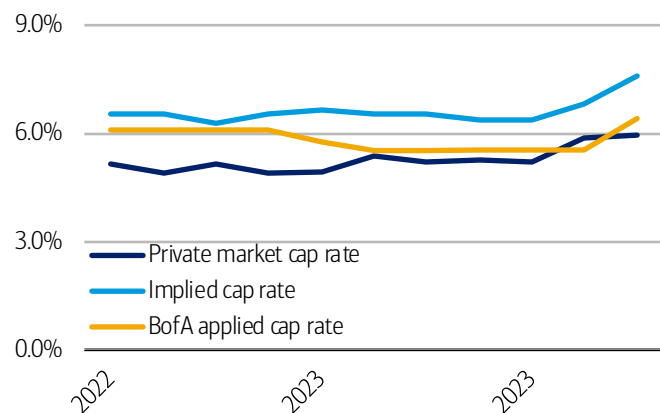


Source: RCA analytics, company filings, Bloomberg

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Exhibit 18: VRE: private market, implied and applied cap rates

Private market and implied REIT cap rates typically track each other

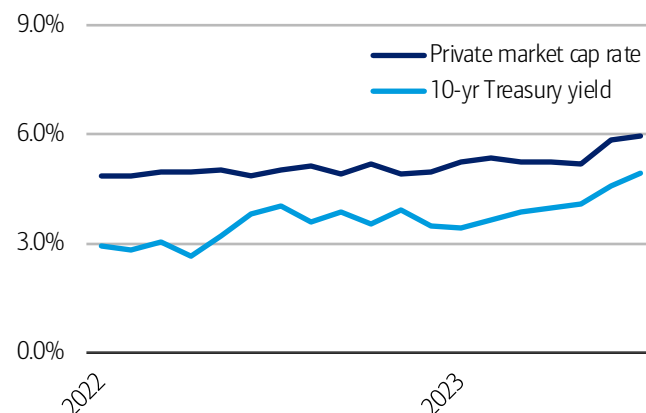


Source: RCA analytics, company filings

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Exhibit 19: UDR: private market cap rates vs 10-yr Treasury

Private market cap rate spreads over the 10yr averaged 286bps (2011-2019)



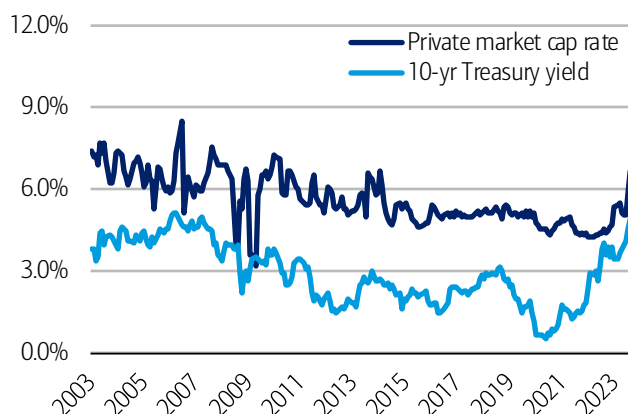
Source: RCA analytics, company filings, Bloomberg

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Cap rates in Gateway markets

Exhibit 20: Boston private market cap rates

Private market cap rate spreads over the 10yr averaged 306bps (2011-2019)

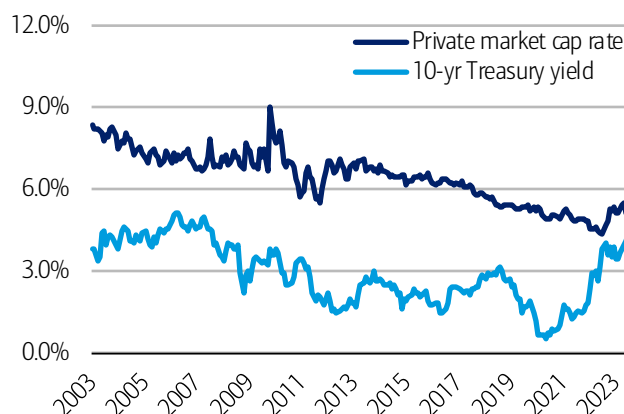


Source: RCA analytics, Bloomberg

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Exhibit 21: Houston private market cap rates

Private market cap rate spreads over the 10yr averaged 397bps (2011-2019)

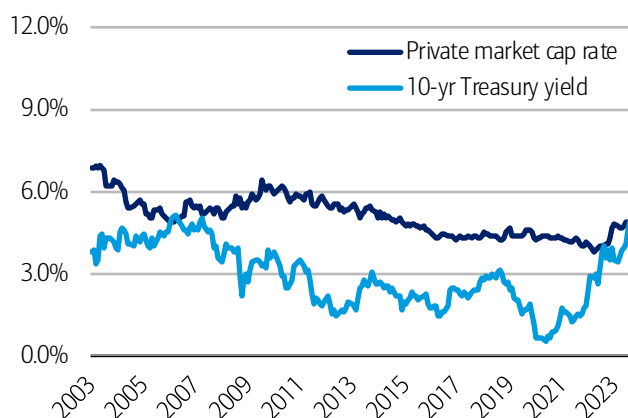


Source: RCA analytics, Bloomberg

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Exhibit 22: Los Angeles private market cap rates

Private market cap rate spreads over the 10yr averaged 262bps (2011-2019)

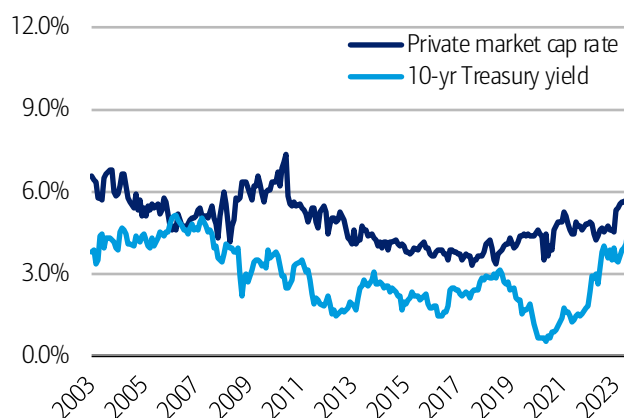


Source: RCA analytics, Bloomberg

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Exhibit 23: New York City private market cap rates

Private market cap rate spreads over the 10yr averaged 196bps (2011-2019)

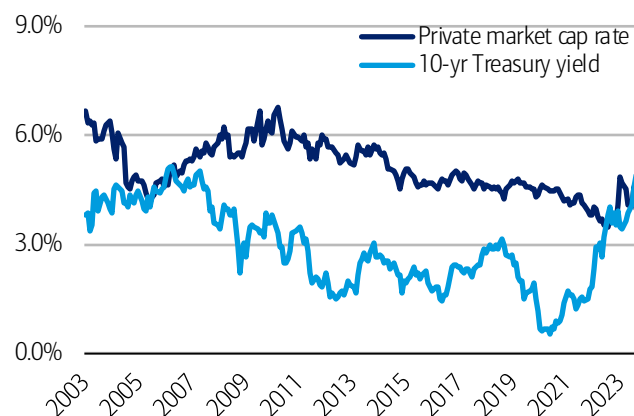


Source: RCA analytics, Bloomberg

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Exhibit 24: San Diego private market cap rates

Private market cap rate spreads over the 10yr averaged 279bps (2011-2019)

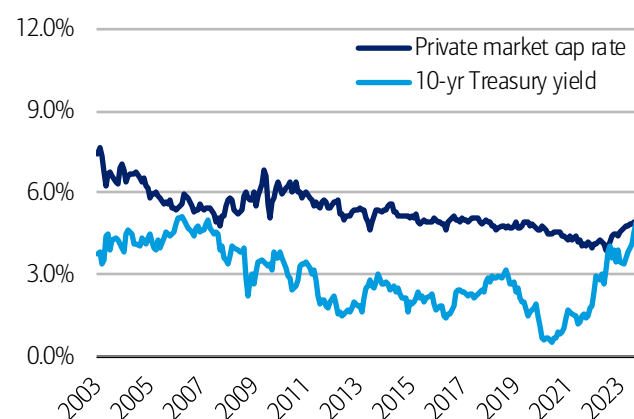


Source: RCA analytics, Bloomberg

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Exhibit 26: Seattle private market cap rates

Private market cap rate spreads over the 10yr averaged 287bps (2011-2019)

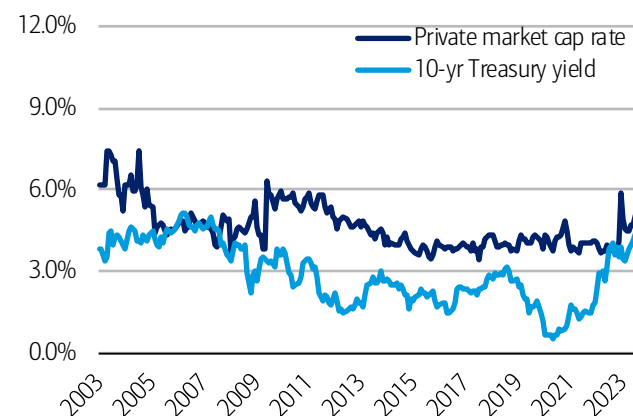


Source: RCA analytics, Bloomberg

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Exhibit 25: San Francisco private market cap rates

Private market cap rate spreads over the 10yr averaged 203bps (2011-2019)

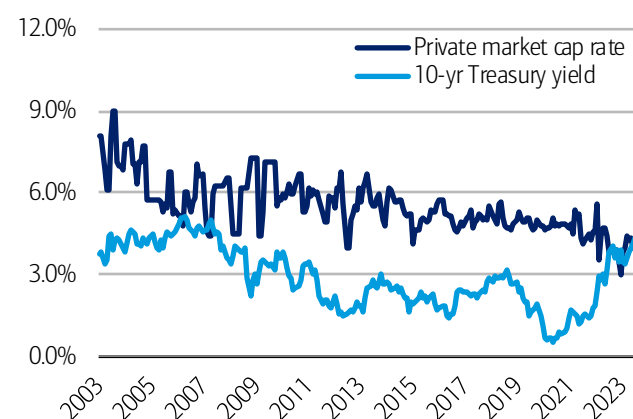


Source: RCA analytics, Bloomberg

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Exhibit 27: Washington DC private market cap rates

Private market cap rate spreads over the 10yr averaged 305bps (2011-2019)



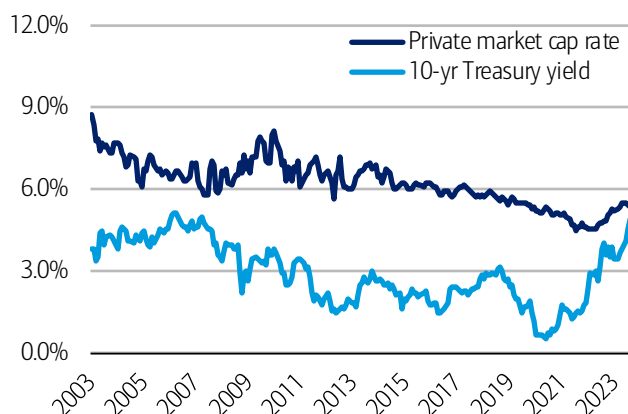
Source: RCA analytics, Bloomberg

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Cap rates in Sunbelt markets

Exhibit 28: Atlanta private market cap rates

Private market cap rate spreads over the 10yr averaged 389bps (2011-2019)

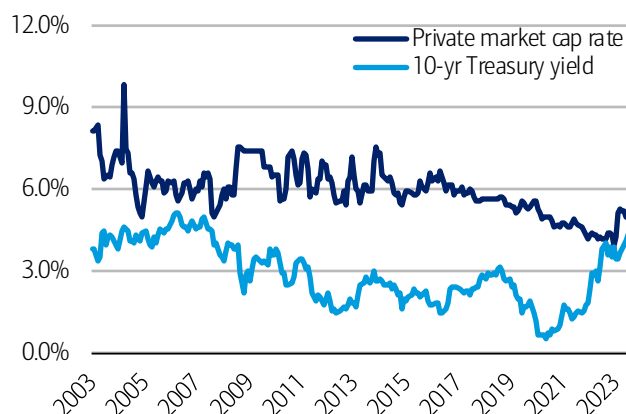


Source: RCA analytics, Bloomberg

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Exhibit 29: Charlotte private market cap rates

Private market cap rate spreads over the 10yr averaged 379bps (2011-2019)

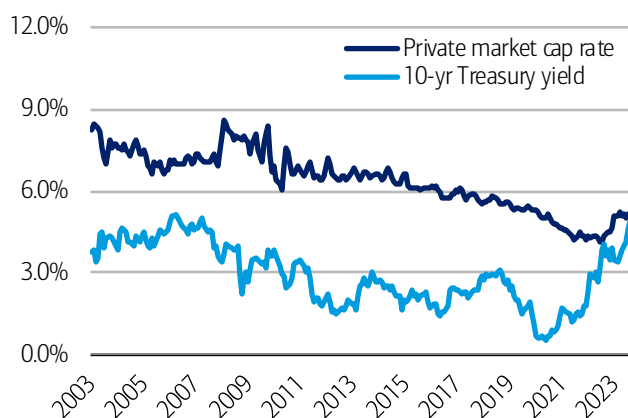


Source: RCA analytics, Bloomberg

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Exhibit 30: Dallas private market cap rates

Private market cap rate spreads over the 10yr averaged 390bps (2011-2019)

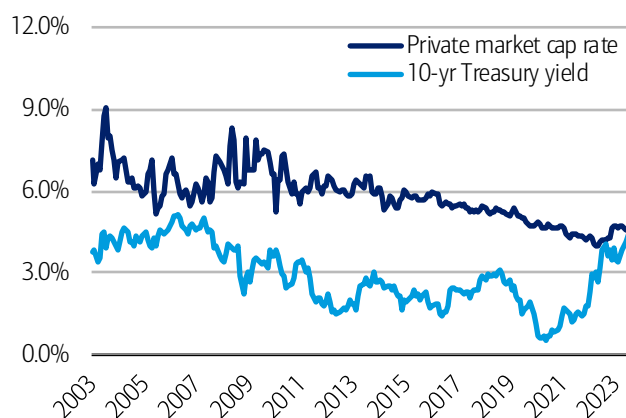


Source: RCA analytics, Bloomberg

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Exhibit 31: Denver private market cap rates

Private market cap rate spreads over the 10yr averaged 344bps (2011-2019)

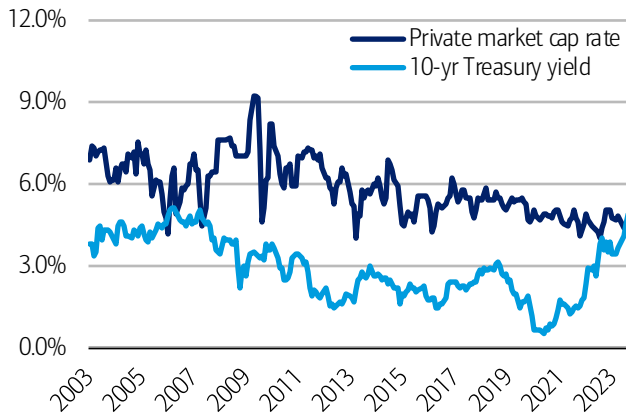


Source: RCA analytics, Bloomberg

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Exhibit 32: Miami private market cap rates

Private market cap rate spreads over the 10yr averaged 340bps (2011-2019)

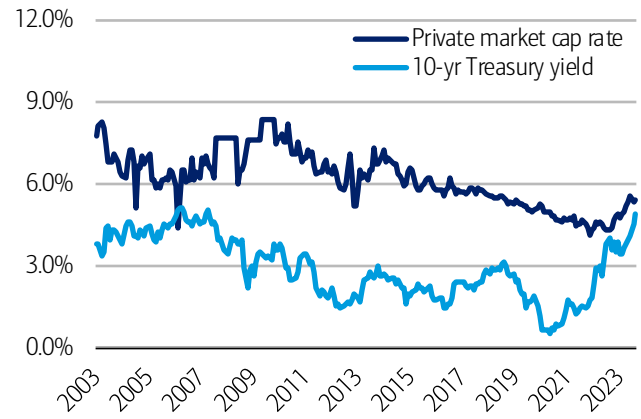


Source: RCA analytics, Bloomberg

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Exhibit 33: Orlando private market cap rates

Private market cap rate spreads over the 10yr averaged 379bps (2011-2019)

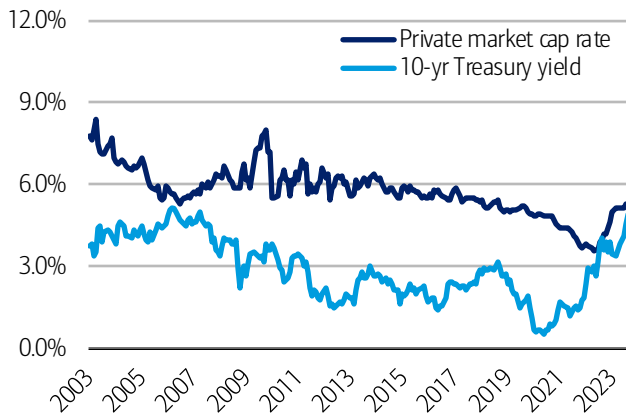


Source: RCA analytics, Bloomberg

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Exhibit 34: Phoenix private market cap rates

Private market cap rate spreads over the 10yr averaged 347bps (2011-2019)

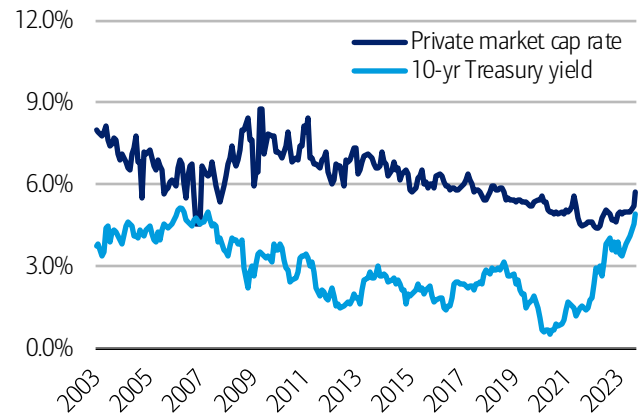


Source: RCA analytics, Bloomberg

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Exhibit 35: Tampa private market cap rates

Private market cap rate spreads over the 10yr averaged 400bps (2011-2019)



Source: RCA analytics, Bloomberg

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Exhibit 36: Companies mentioned

Full company names below

Ticker	Company name
AIRC*	Apartment Income REIT Corp
AVB	AvalonBay Communities, Inc.
CPT	Camden Property Trust
EQR	Equity Residential, Inc.
ESS	Essex Property Trust, Inc.
IRT*	Independence Realty Trust, Inc.
MAA	Mid-America Apartment Communities, Inc.
UDR	UDR, Inc.
VRE	Veris Residential, Inc.

Note: * for companies that are not under our coverage

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R1}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R1} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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