BRIDGE INVESTMENT GROUP

APRIL 2025

RESIDENTIAL RENTAL MARKET OVERVIEW

Summary

- Current market valuations at the start of a new cycle present a compelling entry point.
- The long-term supply-demand imbalance in the rental housing market underpins a strong investment thesis across prime segments of residential rental.
- Strategic investments in high-growth markets and robust asset types including but not limited to market rate Multifamily, Workforce and Affordable Housing, and Single-Family Rentals offer strong positioning in an increasingly supply-constrained environment.
- Affordability constraints and demographic shifts are expanding the renter pool, reinforcing resilient demand fundamentals.

With shifting demographics and persistent affordability challenges, we believe investors who act now to acquire high-demand residential assets—multifamily, workforce housing, and single-family rentals—can capitalize on a rare pricing reset and position for significant long-term upside. Increasingly, asset values are being marked below replacement cost, offering an attractive entry point not seen in over a decade. In a high interest rate environment, unlevered cap rates have become a more reliable gauge of intrinsic value—helping to strip out capital structure noise and focus attention on the core earnings power of assets. These dynamics underscore the importance of underwriting at the asset level, where incremental differences in location, quality, and operational performance can drive meaningful risk-adjusted outperformance, in our view.

Why Residential Real Estate Now?

Residential real estate has demonstrated remarkable resilience through multiple economic cycles. Housing is a needs-based asset class driven by enduring demand dynamics, such as:

- Household formation,
- Job growth, and
- Affordability constraints that persist regardless of short-term economic disruptions.

At its core, demand for housing remains largely insulated from short-term economic fluctuations. People need a place to live, making it one of the more stable asset classes across market cycles. As such, one key characteristic of residential rental is the ability to offer a hedge against economic uncertainty. Two core elements of this hedge include:

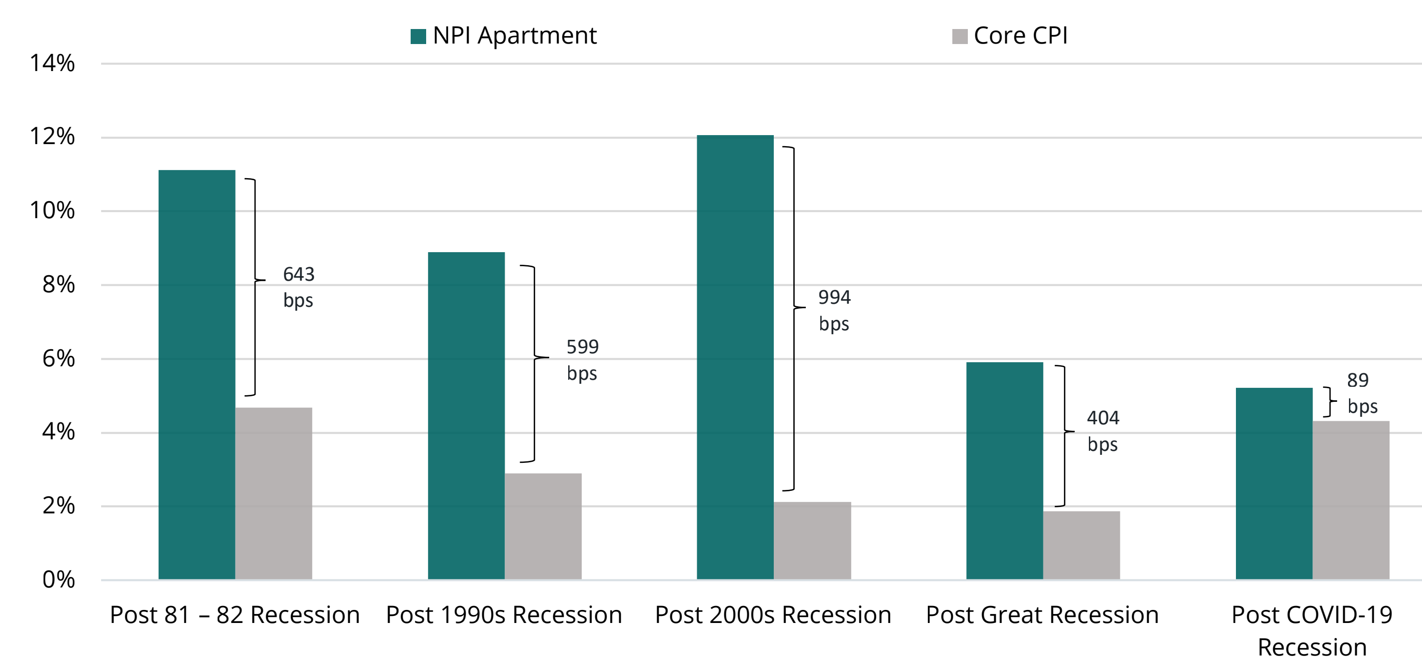
- Shorter lease terms allow for mark-to-market adjustments, which enables active revenue management in response to shifting market conditions.
- Low volatility in occupancy relative to many other real estate sectors, which contributes to durable cash flows that support long-term value creation.

Where Is Multifamily in the Cycle?

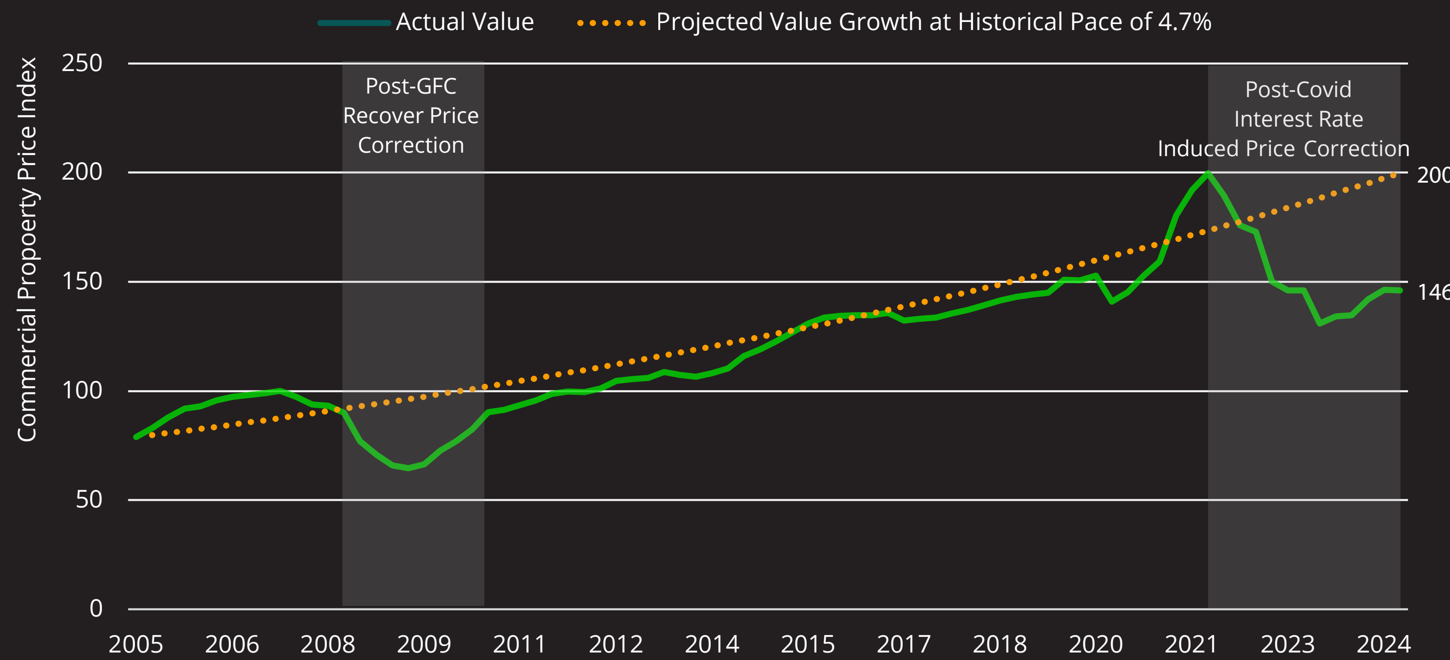
We believe today's environment presents a compelling opening for both current yield and asset appreciation as fundamentals are resetting and stabilizing. Following one of the longest real estate cycles in history, multifamily asset values have declined approximately 27% from the recent peak,[2] a scale of pricing reset experienced only twice in the past four decades.[3] This correction—driven by elevated supply, downward pressure on rent growth, expense inflation, and higher debt service costs—is similar to previous late cycle conditions that offered unique opportunities to acquire assets at discounted valuations early in the recovery stage.

The post-Global Financial Crisis (GFC) period (2010-2012) provides a prime example of early-cycle opportunity when new vintages of multifamily value-add funds capitalized on similar resetting values seen today. These early cycle funds achieved a median net IRR of 19.3%, meaningfully higher than the median of 12.2% for funds launched shortly afterward (2013-2015).[4] Some dissimilarities exist as well: while the post-GFC era was defined by a protracted period of near-zero rates, we acknowledge that the residential sector continues to grapple with multi-decade highs in interest rates. In our view, this reinforces the emphasis on a *fundamentals first* approach to disciplined underwriting at this point in the cycle.

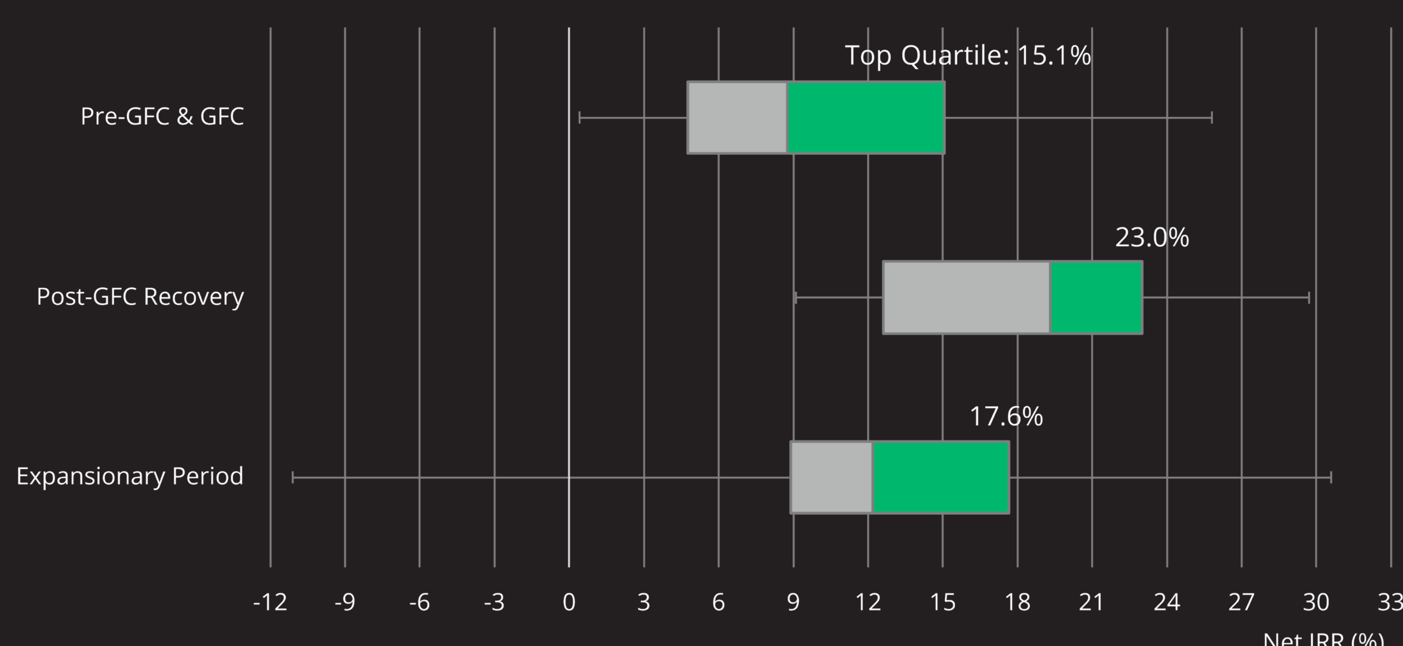
Strong Returns Through Economic Cycles[1]



Apartment Values Back at 2019 Levels[5]

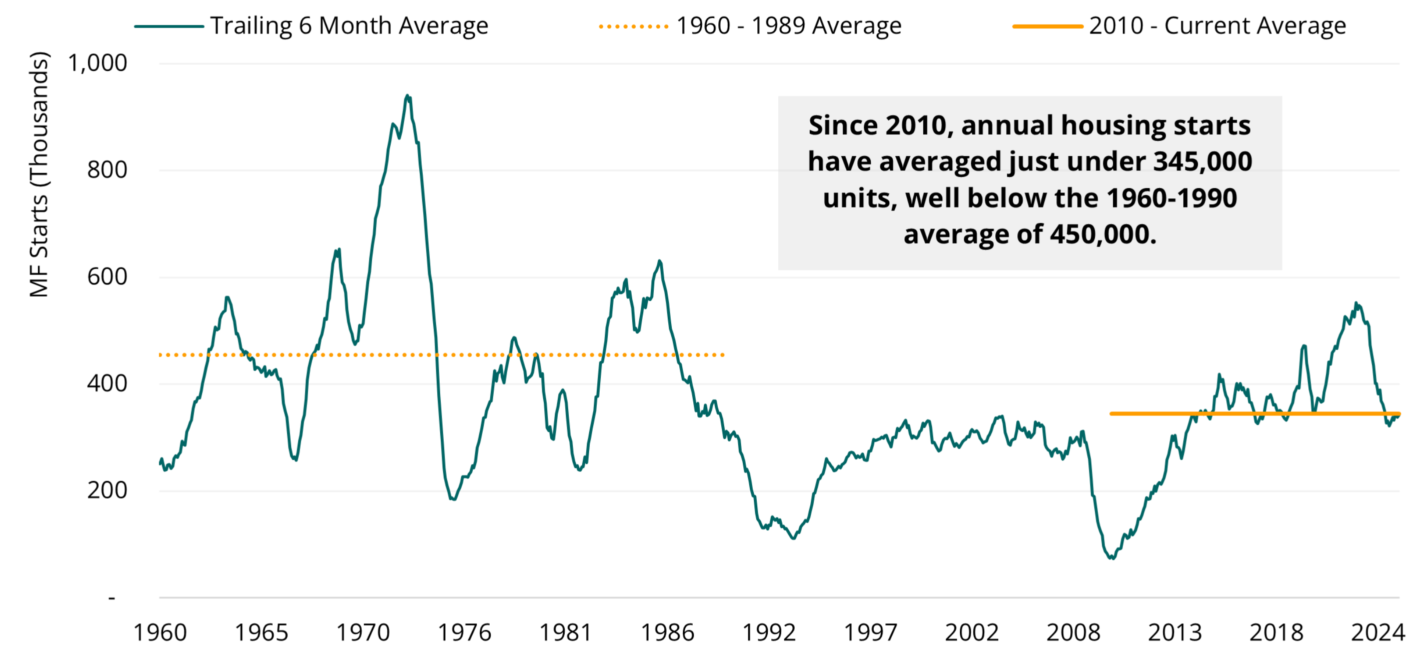


Outsized Returns for Multifamily Value-Add Funds Formed in the Immediate Aftermath of the GFC[6]



Receding Headwinds: Oncoming Supply Constraints

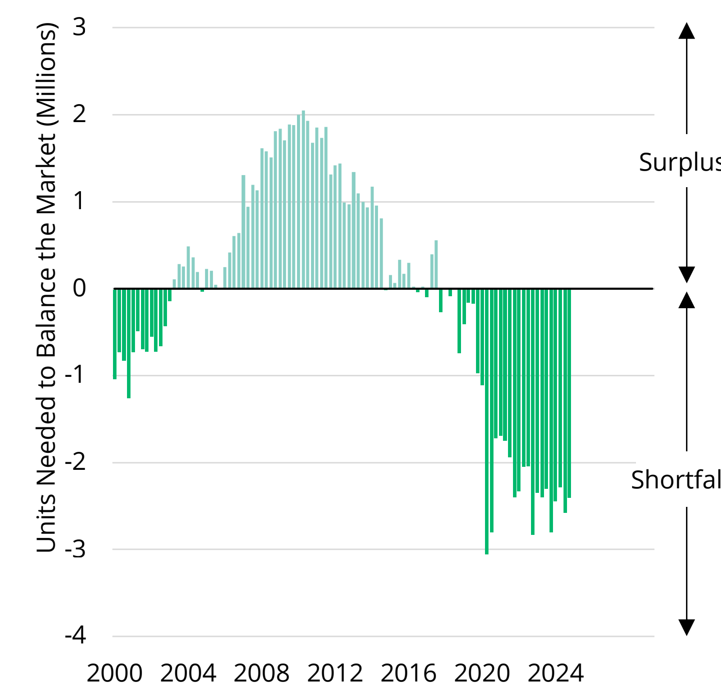
Multifamily Starts Are Sharply Down from the Mid-2022 Peak[9]



As multifamily prices stabilize, the multifamily sector is transitioning from temporary supply-demand imbalance to the next phase of early expansion. The latest data indicate that US occupancies are already on the path to recovery, rebounding 60 bps during 2024 despite the surge in supply that saw deliveries reach the highest annual total in over 25 years.[7] Demand-side forces have fueled the occupancy gains, with net absorption reaching 667,000 units in 2024—the second-highest annual total on record since 2000 and outpacing new supply by 78,000 units.[8] With multifamily starts falling 37% from the recent cyclical peak, we anticipate a sharp deceleration in the forward pipeline. As deliveries decline and absorption continues to rise, market dynamics are resetting, setting the stage for an increasingly favorable multifamily landscape.

Our analysis suggests an additional 2.4 million vacant units are still needed to bring housing vacancy in line with long-term historical trends—and our base case likely underestimates the true deficit as it does not account for ongoing household formation. With supply now receding, we believe the housing shortfall is likely to persist and continue to exert a stabilizing influence on sector fundamentals.[10]

An Estimated 2.4 Million Housing Units Needed to Balance the Housing Market[11]



Rising Tailwinds: Deeper, Broader Renter Pool

With fundamentals stabilizing, we maintain conviction that the rental sector is entering a new phase of expansionary activity, propelled by a substantial acceleration in demand tailwinds. Over the past five years, the US has added 2.3 million rental households, a striking 2.7x leap in net renter household formation compared to the preceding five-year period.[12]

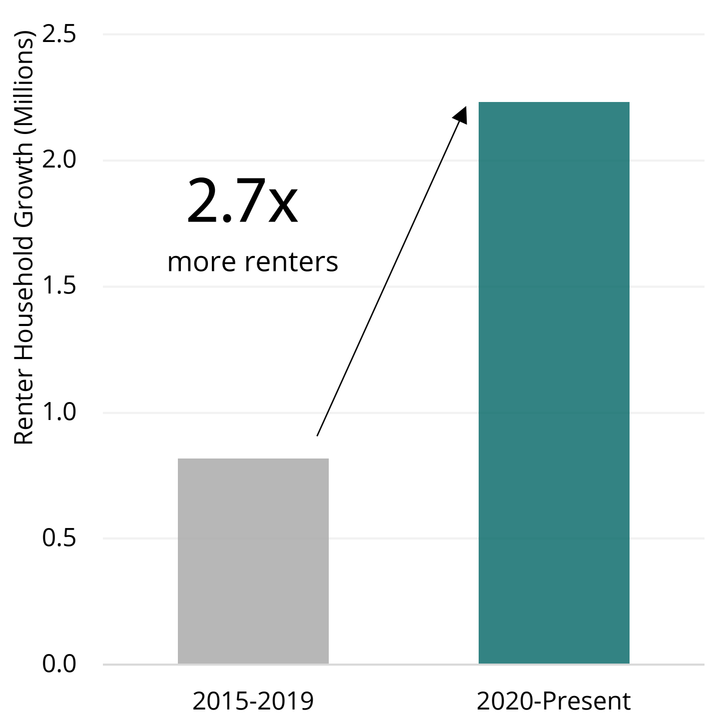
Demographic Shifts Expanding the Renter Pool

Amid these broad shifts in the housing market, the profile of the US renter pool is diversifying, which we believe is likely to provide meaningful uplift to demand in the next cycle. We see a broader range of household incomes compared to historic trends, with increasingly affluent households that we believe are catalyzing renter household growth. Illustrating this point, the number of renters earning $50,000+ has more than doubled between 2010 and 2023, and in the same period there was also a sharp increase in the over $100,000 income band.[15] These higher-income renters reflect a growing preference for renting as affordability challenges manifest across every housing segment.

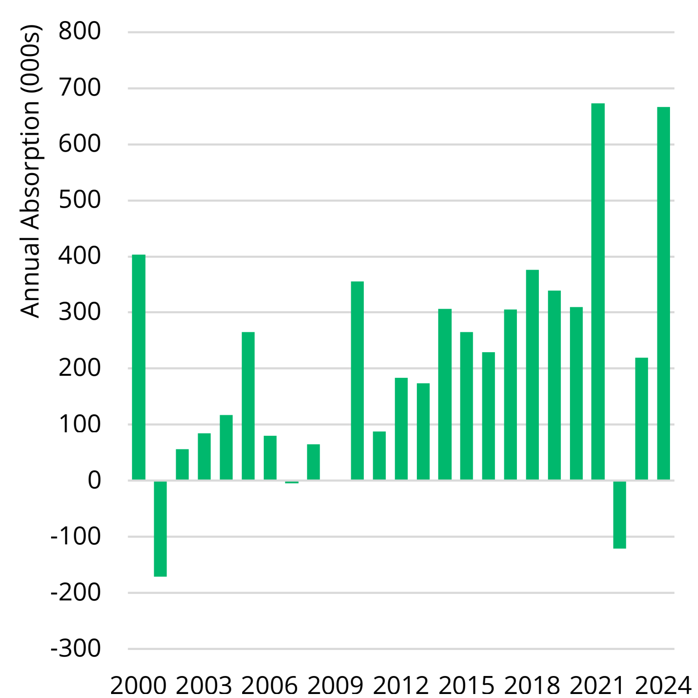
We are also seeing a more diverse range of renters by age. In the previous cycle, younger age cohorts, particularly the Millennial generation, accounted for the core base of renters across markets. In the coming cycle, while these younger cohorts are likely to remain the primary drivers of rental demand, we observe an increasing trend of older adults that are opting to rent. This is particularly notable as the renter population aged 55+ has grown 42% since 2010, far outpacing the 7.4% growth of younger renters during the same timeframe.[17] These older renters tend to favor the flexibility and reduced maintenance responsibilities of renting, generating incremental rental demand, particularly for communities that cater to their lifestyle preferences.

The broadening of the US renter base across both income bands and age cohorts, in our view, can be tied back to the rising cost of homeownership. A confluence of record home prices, high mortgage rates, and limited available supply has eroded homeownership affordability to a 30-year low. These cost constraints have pushed the median age of first-time homebuyers from 35 in 2023 to 38 in 2024—an all-time high[19]—as the mortgage payment for the median-priced home has doubled since the beginning of 2020, equivalent to over $1,100 in added household expenses each month.[20] Consequently, we believe many higher-income and mature households are either choosing to rent out of necessity or view renting as the more financially prudent option.

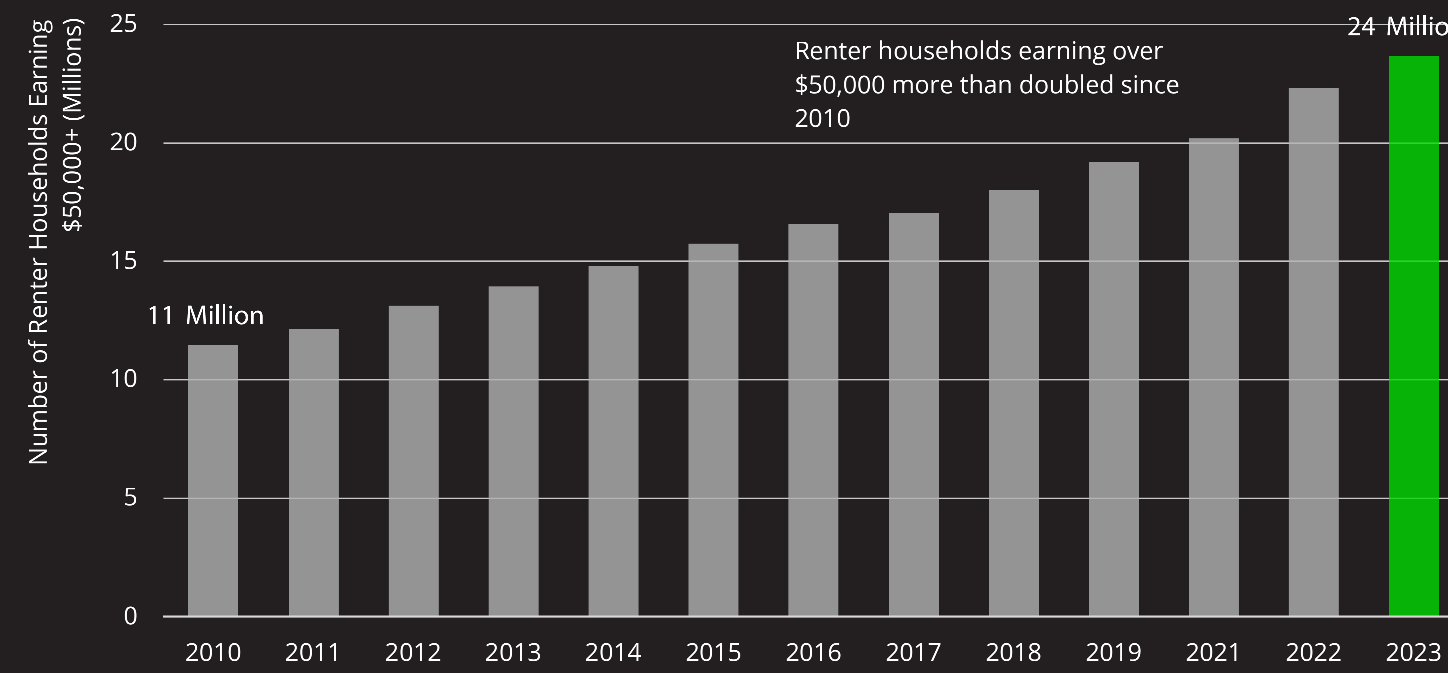
Renter Household Formation is Accelerating[13]



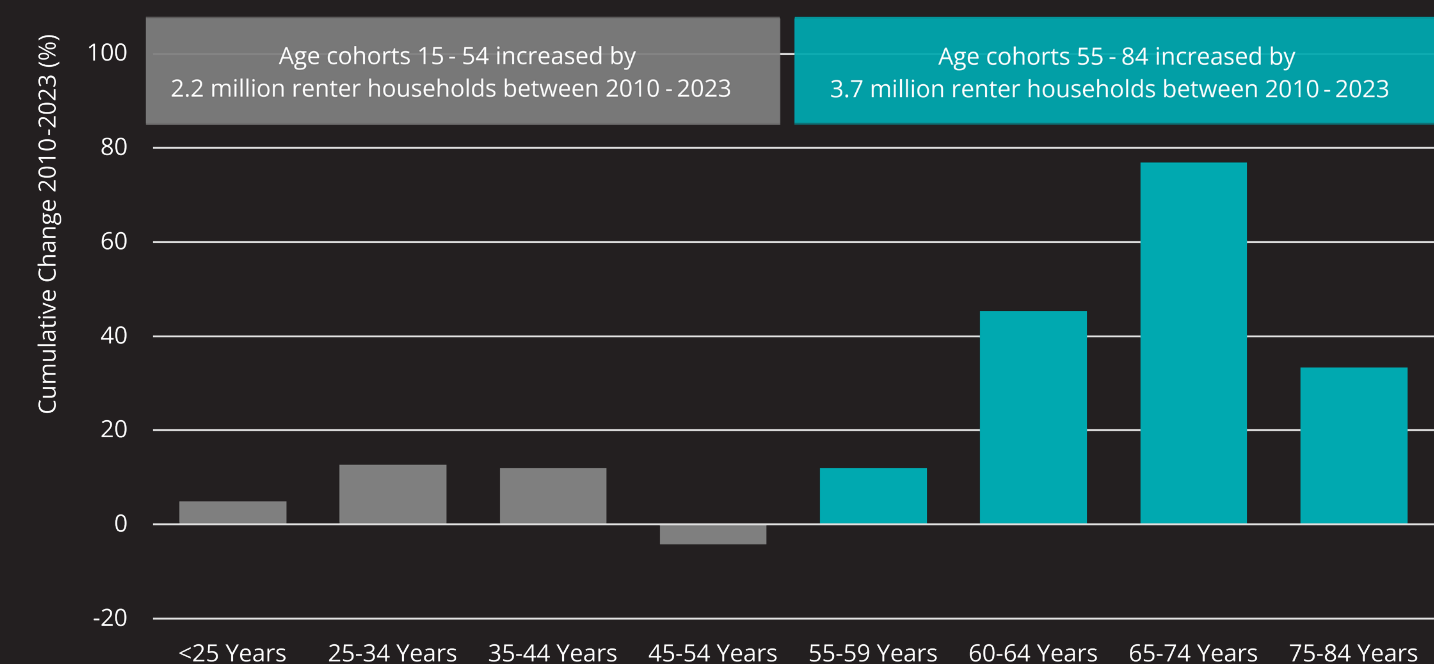
Near Record Multifamily Absorption in 2024[14]



The Number of Renter Households Earning $50k+ Has Doubled Since 2010[16]



The US Renter Base is Expanding in More Mature Age Cohorts[18]

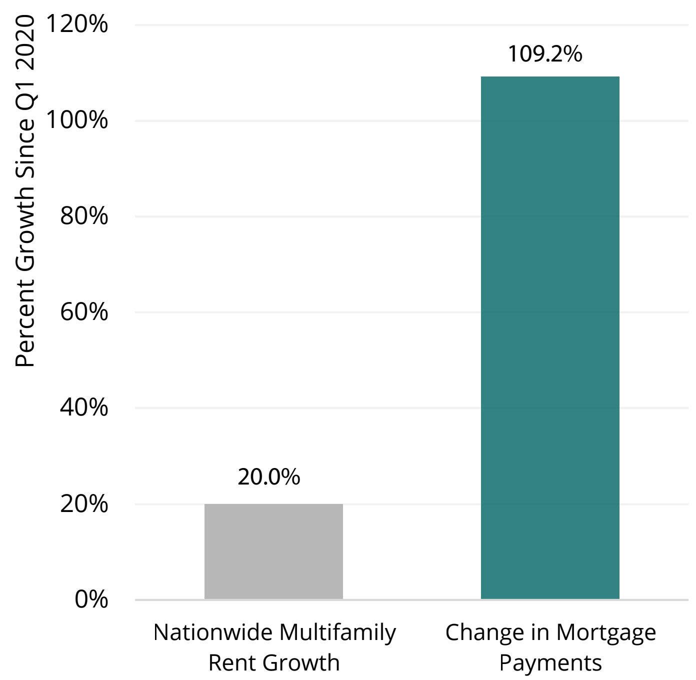


Affordability Constraints Increasingly Pervasive

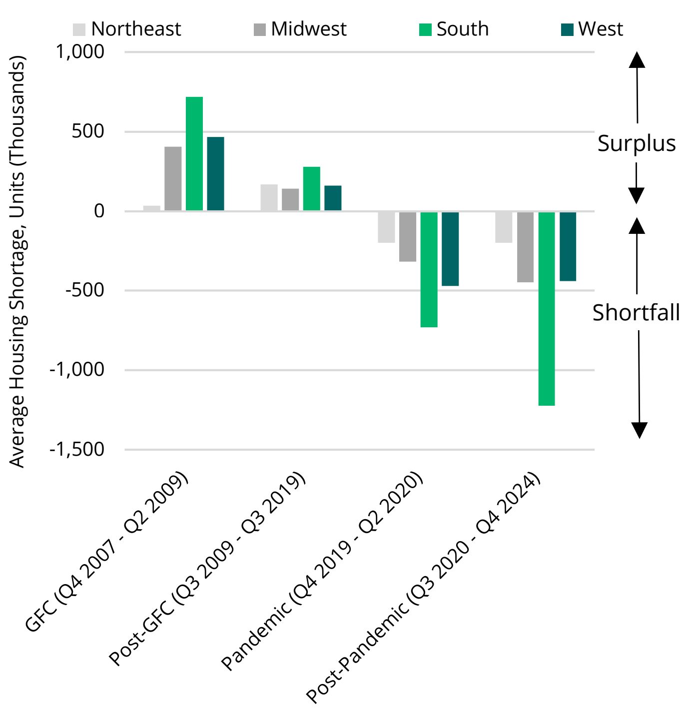
With the expansion of the renter cohort at record pace, we believe all residential rental segments will benefit as starts reach very low levels. Prospective buyers that are delaying purchases leaves an increasing number of renters left to grapple with a market that lacks sufficient options—but particularly low-cost options, adding to demand pressures that are aggravating affordability challenges. The "Missing Middle" renter segment—9.5 million households earning between 51% and 80% of Area Median Income (AMI)—falls into a particularly difficult position, earning too much for federal assistance but struggling to afford market-rate rents.[21]

But this affordability squeeze is not limited to only moderate-income renters; cost burdens have risen across nearly all income levels in recent years. Currently, nearly half of all renters are cost-burdened, with one in four allocating more than 50% of their income toward rent. Notably, 53% of the new renter households formed last year spent more than 30% of their income on housing, the persistent and growing strain on affordability in the rental market, yet construction and replacement costs continue to climb making it difficult to produce new supply at levels that match income comfortably.[22]

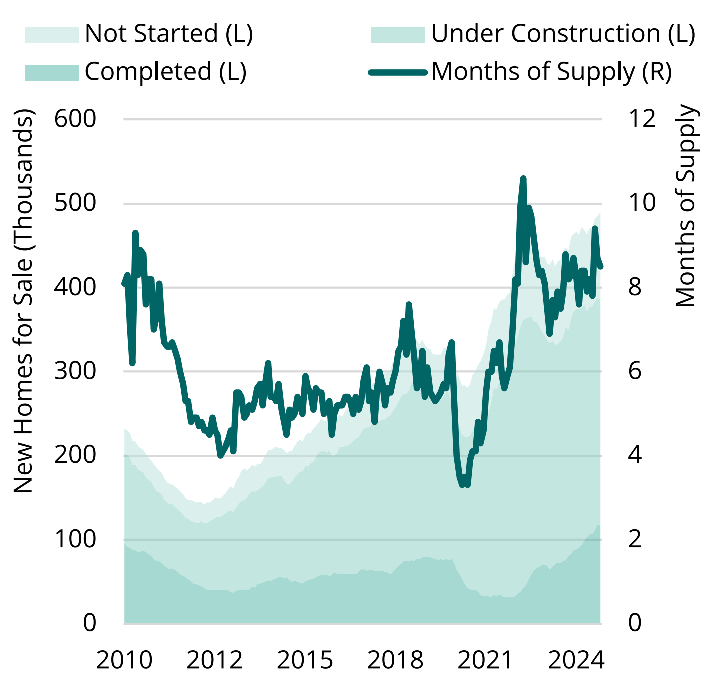
Mortgage Payments Have Grown Five Times Higher than Rent Since 2020



Housing Shortage Across Regions[23]



Inventory of Unsold, Newly Built Homes Piling Up[26]



Where We See the Opportunity Set

Within the broader rental residential space, we view particularly prime opportunities to target the Sunbelt region broadly, but with an emphasis on multifamily, workforce housing, and SFR. These markets and asset classes are backed by powerful long-term trends, including demographic shifts, evolving lifestyle preferences, and receding supply, that support resilient performance and strong fundamentals.

Rapid-Growth Sunbelt Markets Poised to Outperform

While new construction has temporarily softened fundamentals in the Sunbelt, we believe demonstrated strength in demographic and economic drivers are positioning the region for longer-term outperformance. Florida, Texas, Georgia, and the Carolinas have outpaced the US for decades in household formation, job creation, and wage growth, which has fueled outsized rental demand and rent growth. Once the supply overhang clears, we expect these markets to reassert pricing power given robust absorption that in some metros hit all-time records in 2024, and already we note rising occupancies in much of the Sunbelt.

Over the past five years, Bridge target markets added 2.5 million households, capturing 60% of U.S. renter household growth—highlighting strong multifamily demand.[24] These markets are expected to outperform the U.S. baseline, driving 86% of projected population growth over the next five years, fueled by quality of life, strong job markets, business expansion, and migration from higher-cost metros.[25]

The Strength of Multifamily and SFR Assets in a Constrained Submarkets

While we believe that opportunity in residential rental is across all asset types, in our view, market rate multifamily and workforce housing offer stability in the face of ongoing affordability challenges, combining defensive qualities with strong cash flow potential. With new development concentrated in high-end Class A properties, Class B units account for a shrinking portion of inventory, even as demand from middle-income renters, including the "Missing Middle," deepens. Given that most new supply remains out of reach for these households even as thousands of naturally occurring affordable housing (NOAH) units are lost each year to obsolescence, preserving and improving NOAH remains critical. NOAH preservation not only helps address the housing shortage but also offers investors stable tenant demand and limited competition from new supply.

We also see a strong opportunity in the single-family rental (SFR) segment, which we believe is optimized through a combination of build-to-rent (BTR) and scattered site homes to infill as appropriate. In the BTR space, where assets are often available at sizeable discounts to retail prices. High mortgage rates have dissuaded would-be homebuyers and left nearly 500,000 new homes on the market—up 50% since 2019[27]—with a clearance timeline of 8.5 months versus 5-6 months in the last cycle.[28] Inventory is rising particularly fast in Florida, Texas, and the Southeast,[29] prompting homebuilders to consider bulk sales, creating favorable conditions for lower-basis BTR acquisitions with immediate upside.

Across all these opportunities, the broader takeaway is clear: investors who are committed to markets with demonstrated economic and demographic tailwinds and focus on asset classes that serve unmet renter demand will be best positioned for long-term success. With long-term fundamentals tilted highly in favor of residential rental real estate, we see substantial upside in well-located multifamily, workforce housing, and SFR that aligns with the realities of today's housing market.

Endnotes

1 NCREIF, as of Q4 2024.
2 Green Street, as of Q4 2024.
3 NCREIF, as of Q4 2024.
4 Preqin, as of February 2025. Preqin ranks investment managers based on self-reported returns and this ranking does not imply an endorsement of Bridge or any fund managed by Bridge. Preqin rankings are compiled using public domain information and data reported to Preqin by the participants and is not independently verified by Preqin. Details of Preqin's methodology are available on www.Preqin.com. Although submitting data to Preqin does not require payment of fees, Bridge pays subscription fees for access to certain Preqin databases. Preqin generates quartile rankings for individual funds according to their investment strategy, geographic focus, and vintage year. Each fund universe constitutes funds of similar types, geographic foci, and vintage years, enabling quartile rankings to be assigned using a combination of both the net IRR and multiple rankings of each constituent fund – with equal weights placed on both. Past performance is not necessarily indicative of future results.
5 Green Street, as of Q4 2024. Projected value growth based on the CAGR between 2005 and 2019.
6 Preqin, Multifamily Closed End Value Add Funds of $200M+, Pre-GFC & GFC (2006-2009), Post-GFC Recovery (2010-2012), Expansionary Period (2013-2015), as of February 2025.
7 RealPage, as of Q4 2024.
8 RealPage, as of Q4 2024.
9 U.S. Census Bureau via FRED, New Residential Construction, as of December 2024.
10 RealPage, as of Q4 2024.
11 U.S. Census Bureau, Housing Vacancy Survey, as of Q4 2024.
12 US Census Bureau via FRED, Housing Vacancy Survey, as of Q4 2024.
13 US Census Bureau via FRED, Housing Vacancy Survey, as of Q4 2024.
14 RealPage, as of Q4 2024.
15 US Census Bureau, American Community Survey, 2010 and 2023.
16 US Census Bureau, American Community Survey, 2010 and 2023.
17 US Census Bureau, American Community Survey, 2010 and 2023.
18 US Census Bureau, American Community Survey, 2010 and 2023.
19 National Association of Realtors, The Average Age of First-time U.S. Homebuyers Is 38, an All-time High, Nov 5, 2024.
20 Moody's Analytics, as of Q4 2024. Mortgage payment assumes 20% down payment on a median existing home price.
21 U.S. Census Bureau and the Department of Housing and Urban Development ("HUD"), 2023 American Housing Survey: Housing Costs - Renter-occupied Units (created by the AHS Table Creator).
22 US Census Bureau, American Community Survey, 2023.
23 U.S. Census Bureau, Housing Vacancy Survey, as of Q4 2024.
24 RealPage, as of Q4 2024.
25 Moody's Analytics, Baseline Scenario, as of February 2025.
26 US Census Bureau via FRED, New Residential Sales, as of December 2024.
27 US Census Bureau via FRED, New Residential Sales, as of December 2024.
28 US Census Bureau via FRED, New Residential Sales, as of December 2024.
29 JBREC, US Housing Analysis and Forecast, as of November 20, 2024

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