Single Family Rental REITs – Consolidating for Success

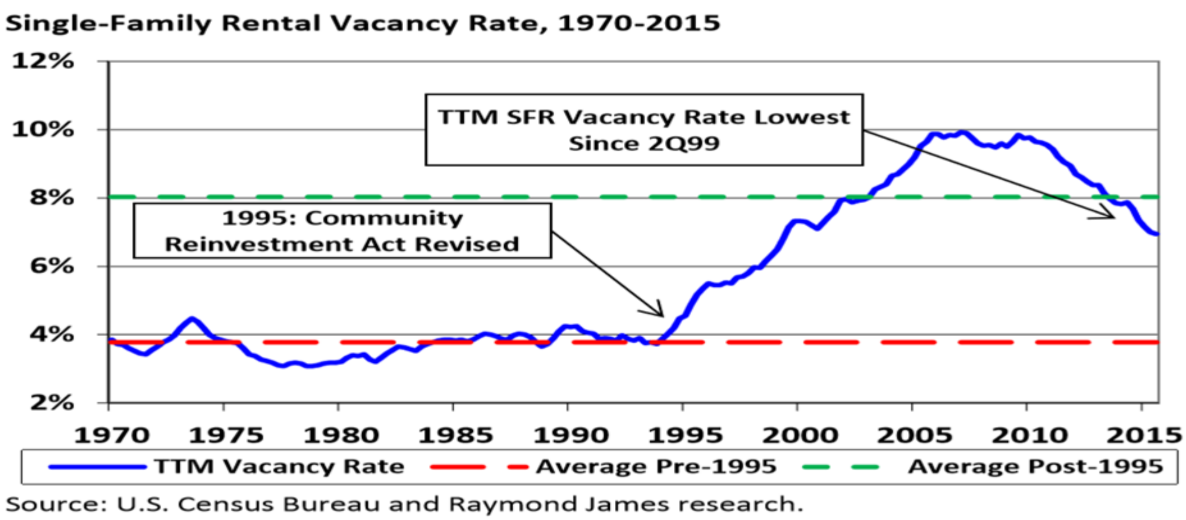
By Grant Lowton, CFA

Single-family rental (SFR) homes are dwellings where the occupants rent, rather than own, their place of residence. This investment universe, which has grown substantially since the 2008 financial crisis, has been dominated by small investors and individuals.

The rate of rental increases in the SFR market has to date been suboptimal as many owners of these dwellings are not primarily driven by a profit motive. In addition, the assets have not been managed efficiently in terms of cost control.

This situation has presented an opportunity for professionally run, larger scale SFR REIT managers. Accordingly, estimates indicate that almost 500000 homes have been purchased by publicly traded firms and other larger financial institutions in the US over the last few years.

However, even SFR REIT investors have grappled with the issue of transforming strong demand for their stock (see diagram below) into profitability.



Even in an environment of increasing demand and declining vacancy rates, there have been operational hurdles for SFR professional investors. In short, for example, it is easier to manage a block of apartments than a portfolio of single family homes scattered over a single or multiple suburbs in a city.

Redefining Listed Property Investing

Scale is the solution to this problem!

SFR REITs have focused on increasing their scale through consolidation within the industry. Effectively, a larger number of homes under management results in the diversification of tenant risk as well as improved operational (cost) efficiencies. *Impediments become more statistically predictable and therefore easier to manage. It is not incidental that this is one of the key benefits of investing in REITs generally.*

2015 saw further consolidation with mergers between Colony and Starwood Waypoint (the combined REIT entity called Colony Starwood, ticker SFR) and American Homes 4 Rent (AMH) acquiring American Residential Properties (ARPI). The prospects are for continued meaningful earnings accretion over time.

To this end, AMH recently achieved same-home revenue growth of 5.4%, a core NOI margin of 62.1% (3.5% above the previous quarter) and a core FFO increase of 30% y/y. These numbers reflect the considerable progress that has already been made.

It is not only operational profitability, but home price appreciation that will substantially contribute to returns for investors. Due to limited supply, house price inflation is likely to outstrip general CPI inflation by a significant margin over the years ahead. This will boost the value of AMH's underlying portfolio of assets.

Residential industry experts believe that SFR industry consolidation is what has been required to really propel SFR REITs to success. Increased scale and efficiency mean that SFR REITs can generate returns that come close to those previously achieved by multifamily REITs. Many investors are not aware of the continual move towards SFR living and the associated investment opportunity. Since the late 2000s, three quarters of renter household formation in the US (4.4 million homes) has been in the form of SFR homes.

SFR REITs are a great investment opportunity which we at Reitway Global are benefitting from through our holding in AMH.

For more information about Reitway Global Property Funds, please visit our website at www.reitwayglobal.com or contact us at 021 551 3688.