

Debt Load Wallops Apartments

Rate rise burdens landlords with new costs as early '20s boom goes sour

BY REBECCA PICCIOTTO

Few investors are feeling more pain from rising interest rates than America's apartment landlords.

These property owners face a bill of more than \$1.8 trillion in debt over the next decade. From this year to 2028, about \$757 billion of those loans are coming due, according to the Mortgage Bankers Association. That is the most of any commercial real-estate sector.

Nearly \$300 billion of those loans are maturing in 2026 alone. This follows a recordsetting 2025, when \$310 billion in loans came due, the highest the sector had seen in a single year since the Mortgage Bankers Association started tracking. Another \$223 billion is due next year.

Now, after the Federal Reserve raised rates a quarterpoint and with bond yields rising, that debt is about to become a much bigger burden. Landlords are having to refinance when borrowing rates are roughly twice the level of five years ago, when many of these loans were made.

When apartment-mortgage rates tumbled to historic lows of around 3% in 2020 and 2021, multifamily buildings were the hottest investment in commercial real estate. Office and retail properties suffered after urban downtowns were hollowed out by remote work. The lodging business took a hit when travel activity drooped during the pandemic, while soaring operating costs and plunging occupancy rates caused hundreds of senior housing facilities to close.

Apartment rents, meanwhile, were surging at double digits nationwide. Multifamily became a refuge for real-estate investors amid the doom spiral in other sectors. "There was a sense of relative euphoria," said Mike Wolfson, Newmark's managing director for multifamily capitalmarkets research. "But things turned very quickly."

New apartment construction flooded the market, mostly concentrated in the Sunbelt. Cities such as Phoenix, Denver, Atlanta and Austin, Texas, were inundated with new luxury apartments and not enough people to fill them.

\$300B

Value of apartment owners' loans that are maturing this year

Fast forward, and many of the same apartment landlords riding high are now preparing to sell at a loss, hand back the keys to their lenders or reconfigure their balance sheets to shoulder millions more in mortgage payments after refinancing.

The financial strain is already causing developers to pare back on new construction and instead buy distressed properties at a sharp discount.

"The chickens are coming home to roost for a lot of people," said Sean Burton, chief executive of the multifamily firm Cityview.

At times, landlords' loan distress has become renters' problem, too. To pay off their debts, apartment owners might try to increase rents or add new fees. Or they may cut back on building repairs and other upkeep to reduce expenses. The Tenant Union Federation, a national tenant group, has organized several rent strikes in financially distressed buildings where landlords had deferred maintenance or raised rents to pay their mortgage.

For years, debt-saddled investors have survived on lenders' willingness to extend the life of the loans. Creditors and borrowers hoped that rent growth would rebound, the Federal Reserve would cut rates and lenders would get their money back.

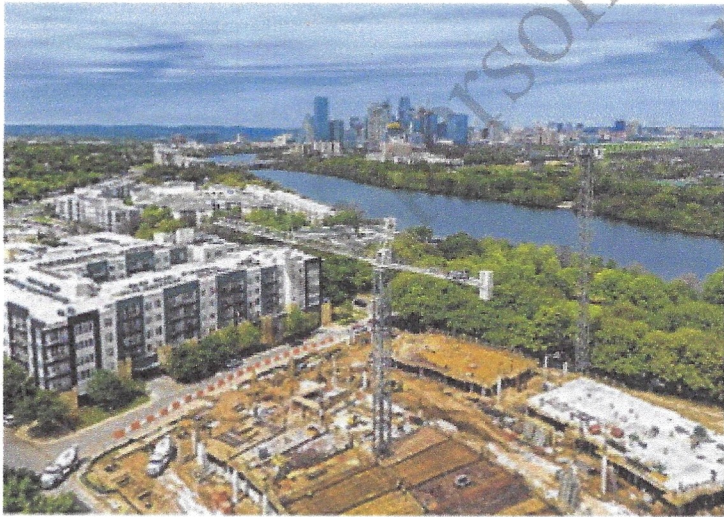
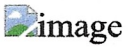
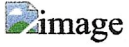
That hasn't worked out, and lenders' patience is running dry.

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Even big investors such as Blackstone are feeling the pain.



New construction has flooded the market in the Sunbelt. A project in Austin, Texas, in 2024. BRANDON BELL/ GETTY IMAGES



An apartment complex under construction in Atlanta. ELIJAH NOUVELAGE/ BLOOMBERG NEWS

"Lenders have gotten a lot more aggressive," said Ryan Cotton, **Bain Capital's** head of real estate. "That could lead to some real turbulence as you see distress start to manifest."

Creditors were already putting pressure on smaller firms that have been struggling with this historic debt balance. But now, even real estate's biggest investors aren't immune from rising rates.

In June, Blackstone defaulted on a \$90 million loan from Ares Real Estate for an apartment building in northern Dallas that the firm bought at the peak of the market in 2021 before interest rates rose.

"No one is spared here," said Bob Hart, CEO of Tru-America Multifamily Investments, who is working through his own pile of shortterm apartment debt. "We're seeing a lot of 'time's up' situations."

Time is up for one of Hart's properties in Raleigh, N.C. He acquired the property five years ago and its loan is coming due. If he wants to keep the property, he would have to refinance the loan from its current 3.5% rate to today's 6% level. He said he is considering selling rather than writing "a large check to rebalance it."

The surge in debt coming due, along with other rising costs, is playing a role in recent industry consolidation. Multifamily giants Av a l o n B a y Communities and Equity Residential in May agreed to combine in a \$ 69 billion merger. Part of the rationale, the firms said, was to rely less on expensive debt and use more of their revenue to finance projects.

The delinquency rate for multifamily loans in commercial mortgage-backed securities jumped from 1% in October 2023 to 7.1% this year, the biggest increase of any major property type, a Morgan Stanley report found. About 3% of the loans coming due this year that cannot be extended are in some kind of distress, the highest level over the past five years, according to Trepp.

Some lenders have reasons besides interest rate hikes to get more aggressive with their borrowers. For one, rent growth is expected to regain momentum next year. Real-es--tate data firm CoStar expects rents to increase by 1.9% by the end of this year, a sharp increase from its previous forecast of 0.5%.

That gives lenders renewed hope for some struggling properties—and a better reason to take back the keys. Banks also have stronger balance sheets than they did several years ago, giving them more of a cushion to take on multifamily risk.

"They are starting to believe that we can take some of the real estate back and make a play for that recovery" of rent growth, said Cotton of Bain Capital.

Apartment values fell about 3.5% in the past month and are more than 20% below their 2022 peak, according to Green Street. Syndicator firms that went big on multifamily during the pandemic are now barely afloat.

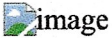
S2 Capital, a Dallas-based syndicator firm, has racked up \$400 million in loan defaults on its Sunbelt apartment portfolio. Earlier this summer, CEO Scott Everett dissolved the multifamily fund and informed investors that they wouldn't see their money back. He is being personally sued by his lenders and recently put his Dallas home up for sale for \$45 million. The firm plans to sell six of the properties in default for \$290 million and is working to refinance hundreds of millions more of distressed loans. Everett said he expects the lawsuit to be resolved by the end of this month.

Meanwhile, cash-flush buyers are circling these distressed properties. Burton of Cityview is one of them.

Cityview is buying directly from lenders who have assumed control of properties, something the firm hasn't done in years, Burton said. Cityview is getting a roughly 40% discount for a newly renovated apartment complex in the Dallas metro area that was foreclosed on.

"It's some of the best buying opportunities I've seen in my career," he said.

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Apartment Loans Are a Deal for Buyers

One pool of multifamily apartment mortgages issued in 2021 is already 53% delinquent

A batch of 2021-era apartment loans is in trouble. The Federal Reserve interest-rate increase might force owners and their lenders to sell underperforming properties and give bargain hunters a chance to buy real estate at low prices. *Note*

The distress rate in commercial real-estate collateralized loan obligations, a type of securitized real-estate lending, hit 28% in August, from 19% in July, data from CRED IQ shows. These floating-rate loans are sometimes used to finance risky purchases such as a property that needs to be renovated before it can be fully leased. Cash flows might be volatile until a building is refurbished and filled with new tenants. *Note*

Most of the recent rise in distress in the CRE CLO market is driven by loans that were issued in 2021, when property values were at all-time highs and borrowing costs were at all-time lows. *Note*

One portfolio, known as FS Rialto 2021-FL3, is particularly troubled. It started out with 26 floating-rate mortgages, but many of the performing loans have been paid off, Morningstar analysis shows.

What is left are 18 mortgages against apartment buildings and one hotel where things haven't gone to plan. According to CRED IQ, 53% of the outstanding loan balance is delinquent.

Last week's rate rise is a blow to these borrowers. Some of them are multifamily syndicators: gung-ho investors who loaded up on floating-rate debt during the pandemic and spent tens of millions of dollars on apartment buildings, often in Sunbelt cities. Their business plan was to renovate the units, raise the rents and flip the buildings for a profit.

The timing of the Fed rate increase is tricky. CRE CLO loans are often structured with an initial three-year maturity, with two one-year extension options. This means many of the loans that were issued in 2021 are approaching their final maturity date. *Note*

Some of the assets look deeply distressed. Real-estate investor Ashcroft Capital borrowed against five apartment buildings in Georgia and Texas. Average rents during the first quarter were \$1,423 per unit, far below the \$1,953 projected by the lender, a recent Morningstar analysis shows. Rent growth expectations were too bullish, and income generated from the properties only covers 57% of the mortgage payment.

The Morgan is a 1984 apartment building in Austin that was bought by CAF Capital Partners in 2021. Occupancy is 65%.

The Austin apartment market is oversaturated, so competition among landlords to attract tenants is fierce. The income generated from rents and other fees at the Morgan covers 15% of the mortgage payment, loan performance documents show. The borrower has paused the renovation work.

"It has reached a point where upgrading units in workforce apartments doesn't necessarily drive a monthly rent premium," says Alex Killick, a managing director at CWC Capital Asset Management, a real-estate financial services company.

Owners of troubled real estate who have a plan to raise operating income might get a loan modification, says Rich Hill, a senior managing director at Principal Asset Management. For owners who have been hanging on for lower interest rates but don't have a solid turnaround plan, "things are past the point of no return." Note

In the case of the properties in the FS Rialto 2021-FL3 loan pool, more than 90% of the mortgages have already been modified or received some kind of forbearance, according to Morningstar. Five of the properties now face foreclosure proceedings, based on CRED IQ analysis. Pickings have been slim for investors looking to buy distressed property at cheap prices in recent years. Note
Lenders extended or modified loans to avoid taking a loss in a distressed sale. Only owners of troubled office buildings were willing to take a hit.

But recently, troubled assets have started to hit the market. In the second quarter, 4.7% of all multifamily apartment deals were distressed sales, up from 1.5% in the same period last year, data from MSCI shows.

The first rate increase in three years, and hints of more to come, is likely to tip more apartment owners over the edge. Then there will be more opportunities to buy properties at attractive prices.

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