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WHAT COMPRESSING CAP RATES SUGGEST ABOUT INVESTOR SENTIMENT

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Introduction

Select investors throughout the Sunbelt and Mountain West are demonstrating a willingness to pursue multifamily acquisitions aggressively. This results in higher pricing and lower going-in cap rates.

These days, we're seeing trades in the low-to-mid 4s on trailing 12-month numbers. In one scenario, EMBREY recently sold a Denver asset at a 4.12% in-place cap.

What's even more intriguing is that this is happening in an environment where the U.S. 10-year Treasury rate has averaged about 4.4% in 2025.

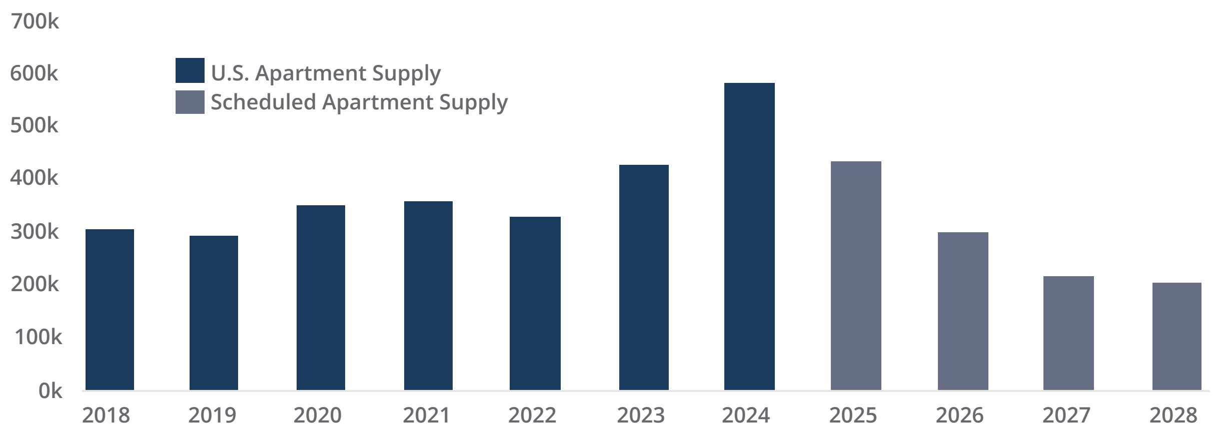
The Drivers Behind the Decision-Making

The current scenario is unusual enough to warrant a deeper investigation. The following six factors support cap rate compression in the multifamily sector.

#1—Near-Term Rent Growth Recovery

Nationally, record multifamily deliveries of 589,000 units in 2024 put downward pressure on rents. But what came online in 2024 generally broke ground in 2021-2022 (**see our previous research piece on supply here**). Since that time, the number of multifamily starts has steadily declined, with anticipated deliveries expected to fall to below 300,000 units by 2026.

Delivery Volumes Scheduled to Ease



Source: RealPage Market Analytics

Coupled with strong renter demand, fewer deliveries will likely mean we are entering a cycle of rent growth increases in the near term. Taking this further, positive rent growth expectations and near-term yield growth support a decline in going-in cap rates.

#2—Attractive Debt Availability

Thanks to consistent agency lending and private debt proliferation, bridge and permanent financing are becoming considerably more attractive in 2025. Commercial lenders are also back in the market as loans are paid off and balance sheets expand.

CBRE reported that the agencies loaned $22 billion to multifamily assets in Q1 2025, a 15% year-over-year increase. In the same period, the Mortgage Bankers Association reported that loan originations for multifamily assets increased by 39% from the previous year.

We benefitted from a tremendous market response on a recent refinance of a core EMBREY asset. During the competitive bidding process, we saw leverage increase by 3% and spreads decrease by 30 basis points.

As investors secure higher debt proceeds at lower cost, they increase their purchasing power while maintaining required investor returns.

#3—Fiscal Policy Changes

The recent U.S. House of Representatives' passage of H.R. 1 – the "One Big Beautiful Bill Act" – extends the 2017 Tax Cuts and Jobs Act conditions. The legislation, now in the Senate, also restores the 100% bonus depreciation rate for properties put in service from 2025 through 2028.

The potential for increased renter purchasing power and higher after-tax returns often leads to increased property values and lower cap rates.

#4—"Safe" Asset Preferences

The recent surge in deal volume underscores the thesis that economic uncertainty drives demand for reliable hard investments like real estate, especially multifamily properties.

According to MSCI Real Assets, apartment sales stood at $30 billion in Q1 2025, a 7% year-over-year increase. Single-asset deal volume has returned to pre-COVID levels, and discussions with brokers point to a significant increase in transactions through the remainder of the year.

Investors understand that multifamily properties and their diversified rent rolls offer cash-flowing hedges in the face of economic uncertainty. Greater demand for this asset type should mean higher valuations.

#5—Long-Term Treasury Rates

Even with the recent rise in 10-year Treasury rates, investors have reason to believe factors such as the slowing of Quantitative Tightening, moderate economic growth, stable inflation, decreasing short-term rates, and resilient foreign demand for U.S. bills and bonds could all lead to downward pressure on long-term rates.

Furthermore, many market analysts, including Witten Advisors, believe that the spread between the 10-year and multifamily cap rates will be significantly lower going forward than during the post-GFC cycle, when it was pushed higher due in part to Quantitative Easing. The confluence of these factors may be leading some investors to accept lower current yields on multifamily investments.

#6—Dry Powder

As of late 2024, available dry powder estimates ranged from $394 billion to $3 trillion globally, reported by JLL and Colliers, respectively. This historically unprecedented amount of liquidity is driving some investors to pursue a first-mover advantage, generating higher property valuations.

More than Cap Rates

To be clear, aggressive pricing doesn't necessarily equate to lower total returns.

Additionally, while investors might be willing to accept lower current yields today, the above builds confidence in a stabilizing multifamily sector. The takeaway is that it's time to prepare capital allocations for the next cycle.

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Garrett Karam leads investment and capital markets activity for EMBREY. As a seasoned industry professional, he sets strategic direction and drives performance alongside a talented in-house investments team, with a focus on maximizing returns and building long-term relationships.

Interested in learning more about EMBREY's current investment opportunities? Click here or email garrett@embrey.com