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Michael Barry on Last Week's Poll Question

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Barry

WILL FANNIE'S AND FREDDIE'S PROBLEMS AFFECT THE MULTIFAMILY SECTOR?

As if Bear Stearns wasn't bad enough, now mortgage giants Freddie Mac and Fannie Mae are getting shaky, and once again a bailout seems imminent. What might this mean for the multifamily sector? Most of our readers (66%) think Freddie's and Fannie's problems will hurt the multifamily sector. Only a third of this week's respondents don't think the crisis will have much of an impact. Michael Barry, president of Applied Property Co., remains cautiously optimistic on the subject. Here are his thoughts:

"If Fannie and Freddie were not a going concern, their problems would have a huge impact on the multifamily financing sector. After the past couple of days, where they lost a dramatic percentage of their value and then popped back up and strengthened, we haven't seen a dramatic immediate effect on lending for multifamily properties. Of course, the implications of the agencies disappearing would have a huge negative impact on the multifamily financing sector.

"There was quite a bit of panic when Fannie and Freddie publicized their problems, but hopefully the fear that they will not be a going concern has passed, as evidenced by their stock prices yesterday and today. They've definitely strengthened from their lows on Tuesday. It seems that the general sense of the market is that Fannie and Freddie have issues to work through, but the issues aren't large enough to threaten the going concern of the two companies. The bottom line is, there's been a little disruption, but I don't think it'll have a significant impact on the financing of multifamily properties.

"Multifamily rental typically goes countercyclical to the for-sale market, so the past 18 months have been very good for the multifamily sector. Massive layoffs and a recession would obviously affect the entire marketplace, which isn't a good thing because when major economic centers are shedding jobs rather than increasing the workforce, that has an impact on multifamily, which tends to congregate around centers of commerce. But the multifamily marketplace has been strong. Last year was a good year, and so far this year has been good, although I say that with caution.

"Supply and demand factor in. For a while, all supply was focused on for-sale housing, especially developing or converting condos in the multifamily sector. So, the supply of new rental housing over the past few years has been very low, and the demand never really went away and at this point in time there's increased demand. The supply and demand factor affecting multifamily rentals have been positive for owners and developers.

"When you finance a multifamily building, a combination of factors determine your financing rate. When you have a disruption such as you have with Fannie and Freddie, spreads widen, but when the underlying treasuries or the instrument that the spread is based on are reducing in yield, the end rate doesn't change much. So in instances where you'll have a drop in treasury rates but a widening of spreads, the net effect is that the borrower is more or less in the same spot as they were with slightly higher treasury rates and an equally contracted spread. Overall, the interest rates I'm seeing for refinancings haven't changed much over the past couple of weeks. If Fannie and Freddie were to cease to operate or were to curtail their operations dramatically, that would have a huge negative impact, though. Spreads would certainly widen dramatically, and there may or may not be a corresponding move in the treasury to offset that effect."