Altus Group

Generating cash flow and optimizing multi-family operations

Finding ways to sustain performance through all market conditions

Optimizing multi-family through all market conditions

How to optimize your cash flow

The commercial real estate industry has had its share of challenges in recent times with high interest rates and rising costs. A constant need for housing has made the multi-family sector a much more resilient asset class, despite facing many of the same economic headwinds.

Everyone needs a place to live, and multi-family properties will always need to be owned and managed. Market tides will eventually turn with a lowering of interest rates and growing immigration.

That spotlights the multi-family sector as a wise investment with significant opportunity. Multi-family is the answer to increasing trends for higher density in urban markets, reduced access to land and rising costs of home ownership. Multi-family also offers attractive lifestyle options and greater amenities than ever before.

As the sector becomes more active, large institutions are targeting it as a desirable investment, able to generate income and strong cash flow each month. There's a sharper focus on cash flow analysis, recognizing that when you maximize cash flow, you maximize the value of your property. And in today's markets that focus has never been more critical with investors looking to cut expenses, improve efficiencies and maximize cash flow wherever possible.

How does your own multi-family asset stack up to other properties, and where can it improve? Are you making decisions that maximize your investment return? Read on to learn more about how to measure performance and improve cash flow using four strategies to make the most of multi-family.

What is a multi-family property?

Multi-family properties are typically occupied by individuals or families on a yearly lease. Each unit must have a kitchen and bathroom, and a separate entrance.

Townhomes and low-rise, mid-rise and high-rise apartment buildings are all examples of multi-family. They may range in size from two units in a rural or suburban area to a large property with hundreds of units in a core urban area.

Student housing, seniors' housing and affordable housing are all considered multi-family, but this guide focuses on market rental properties.

What's inside

SECTION 1

Evaluate your performance to uncover opportunities

Where does your multi-family portfolio stand today? Are you positioned for future success?

You don't know for sure unless you track how your investment is doing and compare that to how your competitors are doing. When you know where you stand, and benchmark your assets against the industry, you can find opportunities to improve.

Each property is unique, and it's important to measure your asset's performance against **comparable "same store" properties**, both in type (such as townhomes or high-rise, or Class A or B) and geography. Are your expenses in line with or higher than others? How does your vacancy rate stack up? Digging into the data allows you to see which areas you can focus on to maximize value.

From an operational viewpoint, your most important Key Performance Indicators (KPIs) are:

- **Reputation/Brand Management:** Your reputation and your brand affect your ability to attract renters. Social media chatter, particularly on review sites, has a particularly strong effect on your reputation.

- **Facility Management:** Resident satisfaction is the driving force behind lease renewals. A building that's clean and well-run plays a big role in tenant satisfaction.

- **Customer Service:** An operations team that is responsive and active delivers the customer service that helps retain renters.

- **Vacancy Rate:** The percentage of available units in your property that are unoccupied. A low rate (below 5%) is good for landlords and means rents will likely rise.

Your most important financial KPIs are:

Know your ABCs

Class A
The highest quality. Luxury apartments in newer, upscale buildings with highest rental rates.

Class B
A step below A. Older buildings but generally well maintained. Renovations may turn a Class B into a Class A.

Class C
The lowest quality. More than 20 years old and may be located in less desirable locations or may not be well maintained.

- **Cash Flow:** The monthly rent per unit multiplied by the number of units gives you gross monthly cash flow; subtract expenses (including property tax) for actual cash flow. Your ability to increase cash flow by charging premium rent is dictated by the building quality, the unit condition and the amenities you offer.

- **NOI % of Revenue:** Net Operating Income (all revenue from property minus operating expenses) expressed as a percentage of total revenue. While it's best to compare your asset's performance with "like" properties, the national average in the U.S. in Q4 2023 was 55.9%.

- **Rent and Gross Rent Potential:** The amount of rental income actually generated or that can be generated from a property based on rent from similar properties in the area (market rent), when all the units are occupied and all tenants pay all their rent.

- **Operating Expense per Unit**: Expenses may include repair, maintenance, utilities, contract services, insurance, taxes, salaries and more. Compare expenses to a comparable asset, and make sure you benchmark the same expenses in terms of unit and square foot averages.

Other typical industry benchmarks, as outlined by the National Multifamily Housing Council (NMHC) in Washington, DC, are:

- **In-Place Rent Per Square Foot:** Average rent per occupied square foot for all in-place leases, including both new leases and renewals.

- **Year-Over-Year Change in Revenue (per available square foot):** The change from one year to the next in average effective rent per available square foot (less excluded units) on in-place leases.

- **Year-Over-Year Change in Executed Rent:** The average quarterly effective rent per square foot on new leases compared to the same quarter in the previous year. Quarters are based on a rolling three-month reporting period, not the calendar or fiscal year.

- **Rent Change – Renewals:** The percent change in effective rent for a renewed lease on the same unit.

- **Renewal Conversion Rate:** The number of leases that renewed, divided by the number of expirations based on the lease end date. "Expirations" cover all leases that end during the period, including early move-outs, skips and evictions count. Month-to-months are included in the period once they either renew or give notice, based on the move-out date.

If you own multiple assets, it may be easier to analyze your portfolio if you hold consistent unit types. For example, you'll be better able to compare and analyze the performance of your 10 buildings with consistent one-bedroom units than if you have 15 (or more) different variations of the same in your database.

Garbage in, garbage out

If you're making decisions based on data – and you should – what are you doing to make sure the data is accurate? A computer only processes what it is given, so incorrect or incomplete data will result in faulty or misleading results.

Standardize your systems to make the most of your multi-family investment and collect accurate data:

- Ensure consistent policies and procedures.
- Invest in training the people who perform them, so they understand why consistency is important.
- Build "guideposts" into the system that support entering the right data.
- Keep an inventory of all maintenance and other supplies so you understand what you bought, where it is and where/how it was used.
- Track your fixed assets and know how many fridges, HVAC units and other property you have, where it is and the scheduled or actual installation.

Standardizing your systems also helps you compare multi-family assets to other portfolios, such as office or industrial investments. This allows you to maintain consistent investment benchmarking and make better investment decisions.

Having a good grasp of your KPIs helps you evaluate the performance of your assets and make decisions for your cash flow and the long-term health of your investment. Look at all the angles to estimate how a renovation may change your cash flow:

- The cost of the renovation.
- The effect of the renovation on rental uplift.
- The effect of the renovation on your vacancy rate.
- The length of time the units will be vacant.

Say you have a property that's a class B or C in an area with numerous class A competitors. You decide to add value to be more competitive by putting $3,000 into every unit to upgrade the appliances. First, you need to estimate whether that value-add is worth it. What can you get for that renovated unit over time? How long does it take to get a return? How many days are units vacant while you do the upgrade, and what's the revenue loss? What's the sweet spot – the right amount to spend on a unit without overengineering a renovation so you never see a full return?

Now that you understand your own KPIs and how your multi-family portfolio stands up to your competitors and the industry, you can look for gaps in your performance. Use your analysis to find ways to maximize your cash flow. Find savings by digging into every process and every expense, as we'll look at in Section 2.

SECTION 2

Analyze every process and expense to search for savings

There's no secret to creating value in multi-family, although no one says it's easy:

Maximize revenue and cash flow. This includes charging higher rents, or earning ancillary revenue through extra or premium parking, storage units, pet deposit fees and retail offerings. If you're building a portfolio, you may be able to take advantage of funding for new affordable housing you create.

Minimize vacancies. Low vacancy rates can justify higher rents. Run the numbers to understand what happens if vacancies go down 10%, or rents increase 5%. Even a small change may speed up leasing velocity.

Minimize operating costs. Again, run the numbers to understand where there are opportunities to save.

The pandemic showed that everything is open to change. Be ready to pivot. How can you uncover and meet changing preferences?

Look for ways **technology** can support you, particular in streamlining, standardizing or improving internal processes to gain efficiencies and reduce costs. Some of the best places to invest for long-term gain include:

- **Self-guided and virtual tours**, which increase your reach and allow continued strong leasing activity even when offices are closed. This is a change from previous industry norms, where sales offices were open seven days a week, with highest leasing activity on weekends.
- **Online leasing applications**. As we'll talk about in Section 3, this is something prospects prefer. You can deliver by understanding the type of units most in demand. Offer online payments and e-signatures. Aim for a paperless transaction. Ensure your tools are integrated making for less dual entry.
- **Other online technology**, such as Artificial Intelligence and predictive analytics.
- **Energy efficiency** throughout the building can reduce long-term operating costs. Consider energy efficient washers and dryers, lighting and other areas.
- **Financial processes** such as rent collection can move online for more efficient processing allowing on-site teams to focus more on issues that require a personal touch..
- **Bulk high-speed internet** in the building will always be desirable to residents, but make sure you can get the rents you need to cover the extra costs.
- **Other bulk purchases** might make sense to take advantage of economies of scale across properties.
- **"Smart home" features** such as programmable thermostats, door locks and light switches can also help attract new tenants. Beware of security issues if someone gives out a door code, for instance, or extra maintenance costs.
- **Look for ways to reduce identity fraud risk** with comprehensive verification technology.

Automate, optimize and integrate the technology services you need to run the building. Having the technology in place gives you visibility into unit and property performance so you can make better, more informed decisions. You can also ensure consistency across properties and more easily integrate new assets to your portfolio.

Connect your Property Management System technology needs to your own KPIs and what's best for your business. Do you want to drive efficiencies, manage expenses or reduce turnover? You may have different needs if you're managing a residential property vs. investing in it.

Depending on your needs, choose from "**single stack**" (one single connected tool that addresses all of your needs), "**multi-stack**" (a mix of hardware and software offering the *best of breed* in each area) or a hybrid of the two. Be aware that "Integration with other applications" is the top challenge for such systems, as cited by 43% of respondents to the 2024 CRETT Multifamily Technology Benchmark Survey & Report.*

Single stack

+ PROS

- Can mean better integration and synergy between the tools and technologies you use.
- May offer better pricing.

– CONS

- You're placing all your bets on one company. If they go down, so does your tech stack!
- No one business model is exactly the same. Expecting a one-size-fits-all tech stack isn't realistic.

Multi-stack

+ PROS

- More control over specific requirements.
- You can choose the combination that best meets your needs across all areas.
- When you need to change out or update the solution, you can plug in new components as needed.

– CONS

- Requires managing multiple vendors.
- Individual costs may add up.
- Time spent deciding on features.
- Can end up with a mixed bag of tools that don't necessarily integrate perfectly.
- May mean more training/resources.

*The Center for Real Estate Technology & Transformation (CRETT) is a subsidiary of the National Multifamily Housing Council (NMHC)

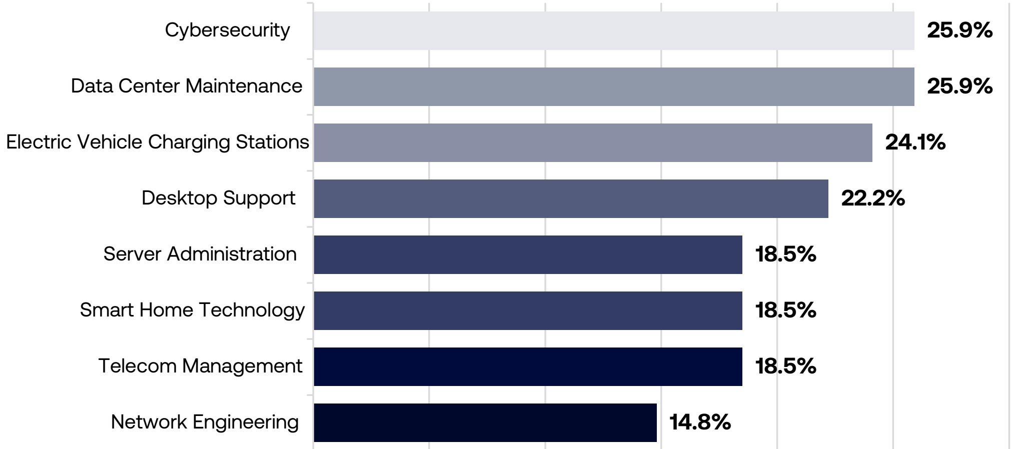
Is technology and innovation important to you? Set up a steering committee!

In a 2024 technology industry benchmark survey, NMHC found that 50% or fewer of small to large companies had staff dedicated to vetting new technology. However, 59% or more of larger companies had a technology/innovation steering committee to help drive technology decisions.

Other areas to investigate that may minimize operating costs:

- **"Decouple" costs** from the building and allocate them proportionately to renters, where possible.
- **Outsource processes** that are non-core to your business, such as accounting, procurement and IT. In the NMHC survey mentioned earlier, 74% of respondents said they outsource part of their IT functions.
- **Centralize critical functions** like leasing, administration and facilities to increase efficiencies.
- **Outsource other services**, such as on-site package management, cleaning and sanitization, or maintenance and snow removal.
- **Have suppliers regularly rebid contracts** to keep prices competitive.

What IT functions do you outsource?



Source: CRETT 2024 Multifamily Technology Benchmark Survey Report

To outsource or not to outsource?

Two roles are mandatory at your property:

1. Someone who is in charge and focused on customer service and creating a community feel.
2. A facilities manager who understands and takes care of the building and the grounds, the equipment and any amenities.

Hire good people who keep on top of everything, from a stray gum wrapper on the floor to dirt in the hallways. Their efforts keep repairs and maintenance from going up and contribute to tenant satisfaction and retention. The rest are candidates for outsourcing.

Also look for cost savings in an untraditional place: **property taxes**, which are among the largest expenses in an operating budget:

- Review property taxes annually and mid-cycle to identify opportunities for tax savings and correct any tax growth assumptions.
- Appeal your property tax bill each year. This may help you slow or stop automatic increases and keep your rents competitive.
- Look into tax incentives for **energy** efficient equipment and changes you have made.

Now that you have an in-depth view of how to minimize expenses and efficiently run the building, you're well on your way to maximizing cash flow. However, remember that **people** will determine your ultimate success. Don't make decisions at the expense of residents or prospects. We'll look more closely at this in Section 3.

Test, and test again

Invest in software that allows you to track results and check options to ensure the long-term value of your assets. For example, plug in how much money you want to invest in renovations per unit to your model and run the numbers to see what rent will justify the expense.

Check the effect of letting occupancy or rents drop during a situation like a pandemic, then measure what might happen if you reduce concessions when the market stabilizes.

Calculate the effect of rent increases or decreases, or changes in maintenance schedules.

SECTION 3

Fine-tune your prospect and resident experience

People *need* a place to live, but they **want** to live in a place where their comfort matters to building managers who act promptly on any issues. Keeping turnover low directly affects your cash flow. So how are you and your building management team delivering the customer service that keeps renters renewing year after year?

The process begins with how you treat prospective renters. Utilizing a mix of new technologies with personalized services has quickly become standard practice.

How many of these innovations are you using?

- Virtual tours, integrated with chat bots and lead management processes.
- Personal follow-up from the team.
- Simplified online leasing, restricting inputs to just those needed. Using better integration and best-in-breed tools with tenant screening and verification tools.
- Streamlined business intelligence tools for predictive analytics and actionable KPIs.
- Ringing doorbells for units, to provide overall better security coverage.
- Smart home solutions for remote access and maintenance alerts.

Add value with amenities

Once your prospects move in, success comes from a clear understanding of what they want.

The National Apartment Association in Arlington, Virginia surveys hundreds of thousands of residents each year about why they lease in one building over another. The overwhelming answer;

- **A clean building** with well-maintained and functioning elevators, amenities, appliances, heating and air conditioning.
- **Responsive service** with repairs made promptly and good communication on the status of any requests.

Use technology to support your efforts in meeting resident wishes. Here are some of the ways you can improve the resident experience:

- Accept online rent payment.
- Make it easy to renew a lease online.
- Offer an online communications portal where residents can submit maintenance requests and track action.
- Provide lockers or use a third-party service to accept packages.

Other ideas may include outdoor areas that can be used for kitchens/barbecues or patios. Offer bike storage. You might also offer online on-demand yoga or fitness instruction that residents can access from their units.

When making decisions that affect the building as a whole, consider if they maximize your investment return:

- Does a change enhance the building value, improve your revenue stream, or maintain your competitive position?
- Can you test a new service with low up-front cost?
- As you develop the building, how will the changes you make affect property taxes?
- Will new amenities allow you to get a higher rent, or will they just spruce up an ’80s-era gym?
- Can you repurpose non-productive space to introduce a new offering?
- Can tenants step up to larger suites to accommodate work from home, such as one-bedroom-plus-den or two-bedroom units?

With a plan to minimize expenses, efficiently run the building, and provide the customer service that helps keep turnover low, you’re pulling out all the stops to maximize cash flow.

In Section 4, we’ll look at how to maintain performance and future-proof your assets.

SECTION 4

Future-proof your assets

How do you ensure the long-term value of your multi-family portfolio?

BENCHMARKING. Use the activities discussed in Section 1 to determine where to focus your efforts. Check your benchmarks at a regular interval – say, quarterly or annually, to match your reporting period, or with a significant event like a new budget year – and stick to it.

Benchmarking questions to answer include:

- Are my expenses higher than other properties in the area?
- Does my expected rent growth align with my competitors?
- Are the returns for this property too low compared to similar quality assets?
- How are my suburban properties doing compared to my urban assets?
- How do the suburban properties I have in one city compare to the suburban properties in another?

Quantify your savings to see how your efforts have made a difference and how you can better use your resources:

- Track and add up the savings from automating manual processes, like online payments, or eliminating costs, like mailing invoices.
- Check savings in time and effort due to technology; your vendor can help with this.
- Tie efficiencies or process changes, like virtual tours, directly to rent growth.
- Track increases in prospect visits with self-guided tours, again linking directly to rent growth.

FORECASTING. This can be done by asset managers, portfolio managers or appraisers. Today's decisions can affect your portfolio for years, so define your priorities and strategies and forecast your financial position for the next year, two years and five years.

Forecasting questions to answer include:

- How does my property's cash flow look over the next three years if I maintain the status quo?
- How did the property perform in prior years, and as markets improve will I be able to match or improve on that performance?
- What happens if rents don't normalize until next year? Or the year after that?
- How will a new property opening nearby affect cash flow in the future?
- If I invest $10,000 per unit today, what will my cash flow look like over the next three years, and what will the value look like at the end?
- Will a partial renovation increase value, or will it cost too much for the return I'll get?

As mentioned, a well-maintained building is key to tenant retention. Future-proof your assets by staying on top of maintenance and connecting it to building diagnostics so you understand the effects of your choices:

Explore **predictive maintenance**. This estimates equipment maintenance requirements to avoid anticipated problems based on historical and real-time data. This approach may offer cost savings over routine preventive maintenance, because tasks are performed only when necessary.

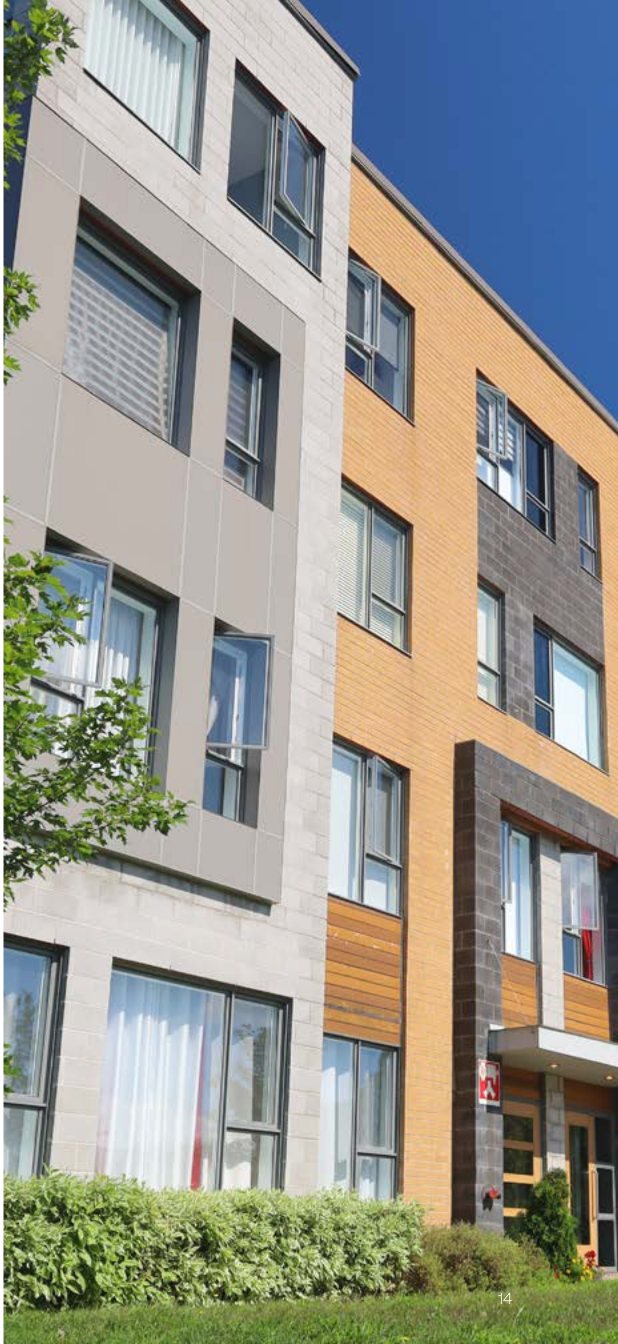
Preventive maintenance happens on a regular schedule based on time (monthly, yearly) or usage (number of hours or cycles) to lessen the likelihood of equipment failure.

Be cautious of **deferred maintenance**. You need to keep up with lifecycle replacement of major elements of your asset (such as a cooling tower or roof replacement). Deferring required maintenance or replacement too long may end up in catastrophic failure and can be a real hit to your bottom line.

Looking to streamline processes?

Altus Group's One11 Advisors help clients optimize their structure, operations and technology to deliver lasting efficiency. It's an advisory service focused uniquely on real estate owners, operators, investors and managers of investments.

Learn more about One11 Advisors



To sum up

Here's how you can support your property's success as a multi-family property investor:

- Apply creative thinking to all challenges. Don't restrict yourself to ways you've responded in the past, or what others are doing. Remember how quickly and imaginatively the industry had to respond in recent years.
- Think about how to pivot strategies to address new challenges. A virtual sales center is one effective response to the pandemic that is here to stay.
- Understand the scope of renovations and whether they're needed to increase revenue or stay competitive.
- Make investments for long-term gains. For example, capital spent now on energy efficiency will pay off in reduced utility bills.
- Constantly question if there are better ways to manage the property.
- Make the most informed decisions based on having the right data, technology and operational processes in place.

Congratulations! You've used the four strategies described in this guide to closely measure your multi-family asset's performance and find ways to track and reduce operating costs. You're working hard to minimize vacancies and you're taking action to maximize revenue. It all adds up to maximizing cash flow – and ultimately, the value of your property.

As we said at the beginning, everyone needs a place to live. Multi-family is a resilient asset class with lots of opportunity, and your actions will contribute to a wise investment in the sector.

Altus Group

Get the most out of multi-family

One11 Advisors offers strategic, operational, and technological solutions for real estate organizations – to optimize performance and minimize risk.

Learn more about One11 Advisors