Securitized Products Special Topics

NYC Multifamily: Rent Increases to Support Cashflows Amid Regulatory Restrictions

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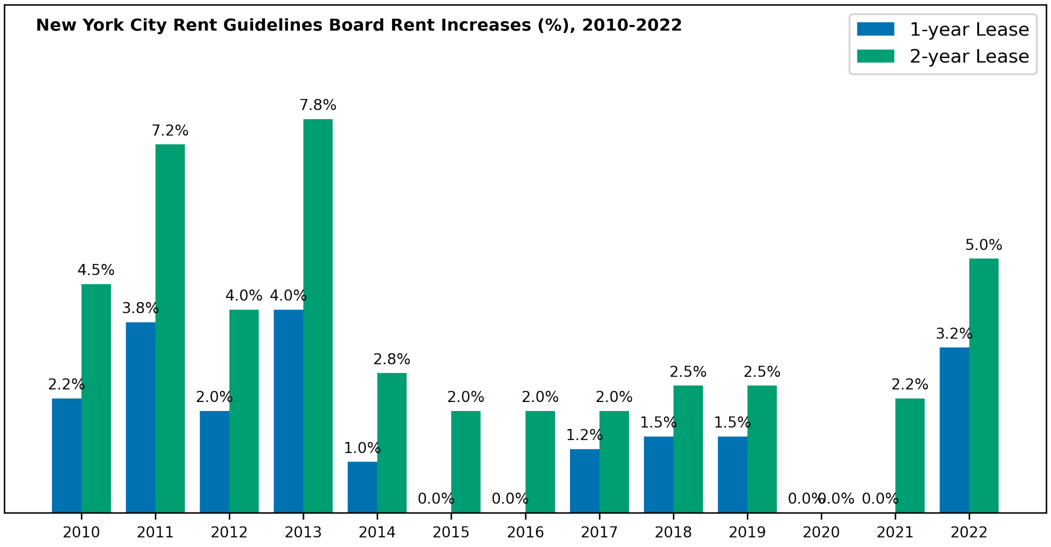
Approved Increases to Stabilized Rents Are Largest in a Decade

The relatively large rent increases New York City recently approved for regulated apartments should support property cashflows in a sector with shifting revenue drivers. Landlords are relying much less on capital expenditure-driven rent increases. In turn, sponsor business plans likely no longer assume any meaningful unit deregulations, of the kind that hobbled at the time Stuyvesant Town (now in FNA 2017-M14 and FNA 2019-M25) or Riverton Apartments (now part of the $506.3 million JPMCC 2021-NYAH Portfolio).

New York City's Rent Guidelines Board ("RGB") adopted a 3.25% annual rent increase on one-year rent stabilized leases, and 5% on two-year leases. It marks elevated levels compared to the rent increases the board approved over the past decade (Figure 1).

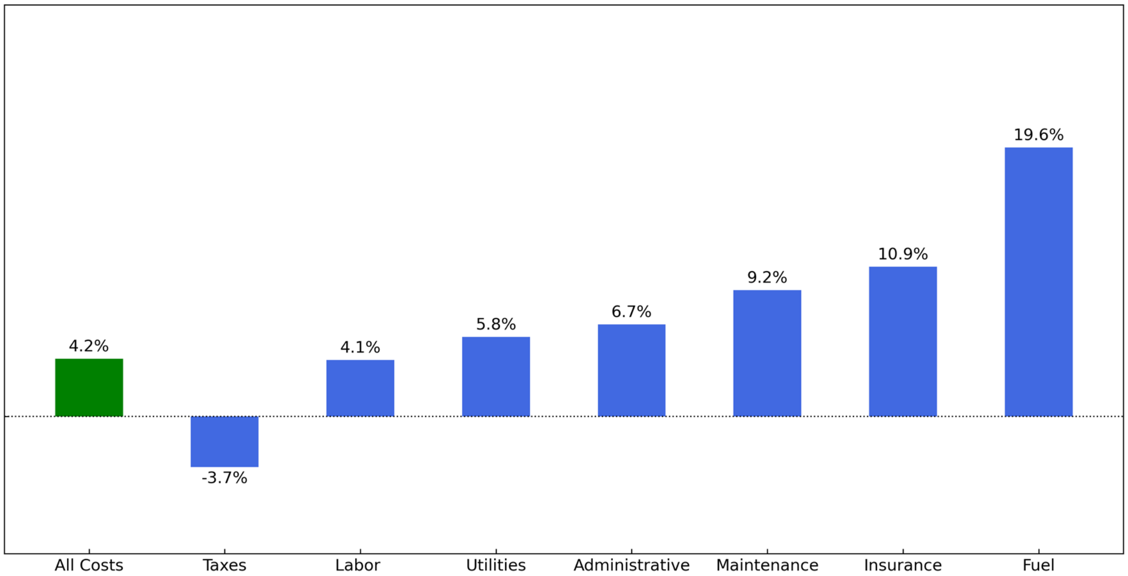
Figure 1. New York City Rent Guidelines Board Rent Increases, 2010-2022



Source: Rent Guidelines Board and Academy Securities

The adopted rent increases may not fully address any inflationary pressures landlords are facing, echoing the limitations of step-up leasing provisions in a high inflation environment we recently discussed.[1] But with some rent stabilized properties benefiting from J-51 tax exemptions or abatements, property taxes at least, a major expense item, should remain stable even amid the high inflation (Figure 2). The number of housing units newly receiving J-51 abatements and exemptions increased 279.5% in 2021, to 7,362, according to NYC Department of Housing Preservation and Development.

Figure 2. Costs Change for Buildings with Rent Stabilized Apartments, April 2021 to March 2022



Source: Rent Guidelines Board and Academy Securities

Rent Increases Take Center Stage Following Tenant-friendly Regulation

RGB's new rent increases come as rent stabilized property cashflows now face several stricter regulatory limitations, following the passage of the Housing Stability and Tenant Protection Act of 2019. Such limitations put a greater focus on the RGB-approved rent increase to grow revenue in New York's rent regulated apartments.

- **Smaller Individual Apartment Improvement-driven rent increases.** Historically landlords relied on capital expenditure pass-throughs to tenants as a way increase rents, and potentially deregulate units. Capital expenditures can be building-wide or individual apartment improvements. In 2019 the Housing Stability and Tenant Protection Act of 2019 reduced landlords' ability to increase rents based on an Individual Apartment Improvement ("IAI"). Before the law passage apartment improvements used to permit a rent increase of (i) 1/40th of the improvement cost for buildings with 35 units or less and (ii) 1/60th of the improvement cost for buildings with >35 units. After, rent increases are limited to (i) 1/168th of the improvement

1 "Inflation-Resistant Leases: Rent Steps Offer Some Revenue Protection, though Not Much," CMBS Special Topics, Academy Securities, June 8, 2022

cost for buildings with 35 units or less and (ii) 1/180th of the improvement cost for buildings with >35 units. The legislation also capped the work which qualifies under an IAI to $15,000 for three improvements in any 15 years.

- **Capped Major Capital Improvements ("MCI").** Following the passage of the 2019 act, MCI-driven rent can increase by an annual maximum of 2%. The MCI increase is temporary and should be removed after 30 years.
- **Increased deregulation protection.** The 2019 act restricted the deregulation of occupied apartments. It also limited high-rent high-income or high-rent vacancy deregulation. From 1994 to 2019 about 6,662 units deregulated after meeting the high rent high income thresholds, according to the RGB. About 170,000 units were deregulated because of high rent vacancy during that period. In comparison, the rent stabilized housing stock saw a net addition of 1,015 units in 2021. Indeed, the confluence of deregulation restrictions in the 2019 act likely removed stabilized-to-market conversions as a meaningful revenue driver for rent stabilized properties. Recent deal documents explicitly allude to that. For example, the sponsor of the JPMCC 2021-NYAH Portfolio notes that its business plan does not call for unit deregulation, and investors should not expect any conversions.

A Few Troubled Situations on Regulated Properties

The new rent increases may also support the handful of troubled multifamily rent stabilized loans. The vast majority of the large stabilized loans are performing (Figure 3). But a few loans did run into trouble during the pandemic. For example, 35 Claver Place ($21.3 million, WFCM 2018-C48), transferred to special servicing in November 2020. All 44 units in the Clinton Hill, Brooklyn, building are rent stabilized. In turn, the 350 East 52nd Street loan ($32.1 million, WFCM 2018-C46) transferred to the special in October 2021. The loan's borrower is entangled in litigation surrounding rent increases under the J-51 tax abatement. We also identified are few troubled situations on recently built properties benefitting from 421a property tax exemption. For example, 1209 DeKalb ($46 million, COMM 2015-LC23) moved to the special in November 2020 for maturity default. The property's 11-year tax exemption is starting to phase out 20% annually beginning in 2023. The property will be subject to full real estate taxes starting in the 2027/2028 tax year.

Figure 3. Large Rent Stabilized Loans

Loan	Deal	Loan Balance ($MM)	Units	DQ Status	Maturity
Jackson Park	JAX 2019-LIC	725.0	1,871	Current	October 2029
NYAH Portfolio	JPMCC 2021-NYAH	506.3	3,531	Current	June 2024
555 10th Avenue	CGCMT 2020-555	350.0	598	Current	December 2029
Yorkshire & Lexington Towers	BBCMS 2022-C16, BMO 2022-C2, CGCMT 2022-GC48	317.7	827	Current	June 2027
Manhattan Multifamily Portfolio	BX 2019-MMP	270.3	637	Current	August 2022
20 Exchange Place	FREMF 2017-KL1E	268.3	767	Late(WL)	February 2027
Acuity Portfolio	CFK 2020-MF2	244.0	1,132	Current	March 2027
416-420 Kent Avenue	CGCMT 2020-420K	238.0	857	Current	November 2030
The Aire	JPMCC 2013-C16, JPMBB 2013-C17	201.4	310	Current	November 2023
Chelsea Centro	FREMF 2020-K1517	178.8	356	Current	October 2034
The West Coast	FREMF 2015-K42	165.0	318	Current	December 2024
80 Lafayette	FREMF 2015-K46	161.3	262	Current	March 2025
TriBeCa House	COMM 2018-HOME	160.0	503	Current	March 2028
The Fairfax	FREMF 2020-K1518	145.0	312	Current	January 2035

Source: NYS Homes and Community Renewal, MCIA and Academy Securities

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