## The Pull of Secondary and Tertiary Markets in 2018

*By* **Kenneth A. Munkacy**

"Smile cities" on the coasts—gateway cities with global renown—have dominated the multifamily building boom of the past decade. High-end luxury development in primary markets on the coasts—and Chicago on the "third coast"—have been inundated with new units and institutional capital.

Where does that leave smaller cities and smaller yet sophisticated investors?

Private investors, such as family offices, have been crowded out of gateway markets, edged out of many deals by major institutional investors and foreign capital. This wall of capital has driven up prices and lowered the yield.

Many privately-held investors have begun to wonder: "Where do we go from here?" The answer, for many of us, lies in the robust activity now taking place in secondary and tertiary markets. And there's even more coming, as a result of continued low interest rates, increasing price disparity and improving valuations.

The question becomes: which markets are the hidden gems?

### Follow the Jobs—and the Workers

Look for markets that have impressive fundamentals: strong job creation, small business growth, well-ranked schools and high quality of life indexes. Many of these cities are attracting new parent millennials and household formation rates are rising.

One little-known fact: new professionals and young families are beginning to migrate inward from the coasts. They are choosing cities with similar attributes, but lower costs of living: Salt Lake City, Utah, instead of San Francisco, Raleigh-Durham, N.C., instead of Washington, D.C., Columbus, Ohio, instead of Chicago.

It's no coincidence that many of these cities offer respected research universities, large healthcare networks and plenty of jobs in the "STEM" (science, technology, engineering and math) fields.

Many of these cities and suburbs are also developing live-work-play entertainment and dining districts, offering tax incentives to employers for headquarter moves and making infrastructure improvements. In these small yet increasingly sophisticated markets, you'll find unexpected amenities such as eco-friendly public buses, bike lanes and high-speed internet systems.

### Filling the Primary Market Gap

Opportunity also lies in primary markets where institutional investors have left gaps. Because most recent new construction has focused on high-end apartment development, some major cities are experiencing huge demand for workforce housing. That means private investors can find opportunities by seeking out class-B or class-C multifamily properties, affordable housing, student housing or senior independent living investments.

### Be Where the Institutional Investors Won't Tread

Larger markets attract larger investors because they are perceived as more stable, with less volatility; such markets attract institutional and foreign investors due to historical familiarity.

Many times they avoid smaller markets because it doesn't make sense for them to invest out of their comfort zone and establish new relationships; in addition, most deals won't be big enough and the transaction volume is limited.

The real estate market door is open for family offices and smaller investor partnerships. Head to markets away from the major coastal cities where there's plenty of potential for new employment growth and household formation, new residents and new investors alike. ■

**Kenneth A. Munkacy** is senior managing director of Kingbird Properties, a real estate investment firm that is a wholly-owned subsidiary of Grupo Ferré Rangel, a fourth-generation family office that seeks value-added opportunities in the U.S. and Latin America.
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