



## Pretend and Extend: A Deep Dive into Commercial Real Estate Lending's Hidden Crisis

### CHAPTER 11:

### MULTIFAMILY: ARE WE NEXT? RISK EXPOSURE IN OVERLEVERAGED MID-TIER APARTMENT PORTFOLIOS

OCTOBER 20, 2025 | REAGAN SCHWARZLOSE, FRICS | MAI | CRE | CCIM

In suburban Atlanta, a 200-unit apartment complex acquired by a syndication group in 2021 for \$65 million exemplifies the growing stress in mid-tier multifamily portfolios. The deal was underwritten assuming 4% annual rent growth and refinanced with floating-rate debt at 3.5% interest. Today, with interest rates at 7.2% and actual rent growth stalling at 1.5% due to tenant pushback, the property's debt service coverage ratio has fallen to 0.95. The syndicator has made two capital calls totaling \$3 million while quietly negotiating the second maturity extension in eighteen months.

This scenario, playing out across thousands of similar properties nationwide, challenges the prevailing narrative that multifamily real estate remains insulated from the extend-and-pretend crisis that has consumed the office sector. While institutional investors continue positioning apartments as defensive assets, a closer examination of mid-tier multifamily portfolios reveals growing financial stress that mirrors the early stages of office sector distress.

The assumption that residential rental demand provides automatic protection from valuation deterioration ignores the leverage dynamics, interest rate sensitivity, and operational challenges facing properties acquired during the 2020-2022 peak pricing period. Many of these assets were underwritten using compressed capitalization rates, optimistic rent growth assumptions, and debt structures that have become unsustainable as market conditions have shifted.

#### Rising Debt Strain

The multifamily portfolios most vulnerable to extend-and-pretend behavior share common characteristics that distinguish them from institutional-quality assets: acquisition timing during peak pricing periods, aggressive leverage structures, and debt service obligations that depend on continued NOI growth to remain sustainable. Properties acquired between 2020 and 2022 often reflect purchase prices that assumed continued rent growth rates of 3% to 5% annually, assumptions that have proven optimistic in many markets.

Interest rate exposure represents the most immediate source of stress for overleveraged multifamily assets. Properties financed with floating-rate debt or interest-only structures during the low-rate environment now face dramatically higher carrying costs that were not anticipated in original underwriting. A property that was cash flow positive with debt service at 3% becomes cash flow negative when rates rise to 7%, creating immediate liquidity pressure for operators and sponsors.

Debt service coverage ratios across mid-tier multifamily portfolios show systematic deterioration from underwritten projections. Properties that were modeled to maintain DSCR above 1.25 increasingly operate below 1.10, with some assets requiring periodic capital contributions to meet debt service obligations. This trend appears particularly pronounced in secondary markets where rent

growth has lagged national averages while operating expenses have increased due to labor shortages and maintenance deferrals.

Regional market dynamics compound these challenges in markets where new supply has exceeded absorption or economic growth has slowed. Submarkets that experienced significant new construction during 2020-2022 now face competitive pressure that limits rent growth while concession packages reduce effective rental rates. Properties without significant competitive advantages find themselves unable to achieve the rent growth necessary to support their debt structures.

#### Syndicator Vulnerability

The syndicated equity structures that became popular during the low interest rate environment have created particular vulnerabilities when properties face financial stress. Many deals structured with high leverage ratios and limited operational reserves leave sponsors with few options when performance falls short of projections beyond requesting additional capital from investors or negotiating with lenders for accommodation.

Capital call frequency has increased markedly across mid-tier multifamily syndications as sponsors attempt to maintain debt service and fund necessary capital improvements. Investors who expected stable cash distributions increasingly receive requests for additional capital contributions to cover shortfalls in property performance. These capital calls often

coincide with maturity extension negotiations that defer recognition of underlying valuation problems.

The illiquid nature of syndicated equity creates additional pressure for extend-and-pretend behavior. Unlike publicly traded REITs that face immediate market pricing of performance issues, syndicated deals can maintain optimistic valuations in quarterly reports while negotiating extensions and capital calls privately with limited stakeholder oversight. This opacity enables sponsors to defer difficult decisions about asset disposition or recapitalization.

Limited partner investors in distressed syndications often face difficult choices between contributing additional capital to protect existing investments or accepting losses through foreclosure or workout scenarios. The complexity of these decisions, combined with limited liquidity options, creates incentives for temporary solutions that may not address underlying asset viability issues.

### **Lender Blind Spots**

Community banks and credit unions with concentrated multifamily exposure face similar pressures to avoid loss recognition that affected office sector lending. These institutions often maintain close relationships with local developers and sponsors that create cultural resistance to forcing difficult conversations about asset quality or debt restructuring needs.

The regulatory environment that enabled office sector extend-and-pretend behavior operates similarly in multifamily lending. Examiners focus on current payment status rather than forward-looking cash flow sustainability, enabling institutions to maintain favorable loan classifications for assets with declining fundamentals. Small balance multifamily loans often receive less sophisticated analysis than larger commercial credits, potentially missing early warning signs of distress.

Geographic concentration in local lending institutions

creates additional challenges when entire markets experience simultaneous stress. Banks with significant exposure to specific metropolitan areas or property types may resist recognizing problems that would require substantial provisioning across multiple loans simultaneously. This concentration risk proved particularly problematic in markets that experienced rapid rent growth during the pandemic followed by significant corrections.

Portfolio management practices at smaller institutions may lack the analytical sophistication necessary to identify early warning indicators of multifamily distress. Unlike office properties where vacancy is immediately observable, multifamily distress often manifests through more subtle indicators like increasing concessions, deferred maintenance, or tenant turnover that require careful analysis to detect.

### **Deferred Maintenance and Tenant Pushback**

The operational reality facing many multifamily properties differs significantly from the assumptions underlying their original underwriting and current valuations. Operating expense growth has consistently exceeded projections due to labor cost increases, utility rate escalation, and regulatory compliance requirements that were underestimated in deal modeling.

Tenant resistance to rent increases has proven stronger and more persistent than anticipated, particularly in markets where household income growth has lagged housing cost inflation. Properties that assumed they could push rents 4% annually now face tenant turnover, collection issues, and bad debt expenses when attempting to implement planned increases.

Deferred maintenance practices adopted to preserve cash flow create long-term asset value deterioration that compounds future refinancing challenges. Properties that reduce capital expenditures to maintain debt service coverage often experience

accelerated physical deterioration that requires larger future investments while simultaneously reducing competitive positioning in rental markets.

The combination of income pressure and expense growth creates operational stress that manifests in declining property conditions, tenant satisfaction, and market positioning. These operational challenges ultimately affect property values in ways that may not be immediately apparent in quarterly valuation reports but become evident when refinancing or disposition becomes necessary.

### **Triage Frameworks Are Urgent**

The multifamily sector must develop systematic approaches to identifying and addressing distressed assets before problems compound into sector-wide instability. Sponsors should segment portfolios based on refinancing probability, operational sustainability, and hold period assumptions rather than treating all assets as equally viable long-term holds.

Asset-level analysis should incorporate realistic interest rate assumptions, conservative rent growth projections, and current market positioning rather than relying on optimistic recovery scenarios. Properties that cannot maintain positive cash flow under current market conditions require immediate attention rather than temporary extensions that defer inevitable recognition.

Lender portfolio reviews should focus on concentration risks, borrower financial capacity, and asset-level sustainability rather than current payment performance alone. Early identification of potential problems enables proactive management rather than reactive crisis response when multiple assets simultaneously require attention.

### **The Path Forward**

The multifamily sector can avoid following the office sector's path toward widespread extend-and-pretend behavior through early recognition of developing

problems and proactive management of distressed assets. This requires honest assessment of current market conditions rather than hope that previous growth patterns will resume.

Four Corners Valuations provides independent analysis that cuts through syndication marketing and lender optimism to deliver realistic assessments of multifamily asset sustainability. Our field-integrated approach identifies operational and financial red flags before they become portfolio-threatening problems, enabling proactive management rather than reactive crisis response.

The cost of delay in addressing multifamily distress increases daily as interest rates remain elevated and operational challenges compound. Early action provides more options and better outcomes than waiting for problems to resolve independently through market recovery that may not materialize.



**Reagan R. Schwarzlose**

FRICS | MAI | CRE | CCIM

CEO | Principal

+1-480-440-2842 Ext. 06

rschwarzlose@fourcv.com

www.fourcv.com

### Licensed Professionals

Our licensed valuation professionals are available to support clients in the following states:



Alabama	Illinois	Oklahoma
Alaska	Indiana	Pennsylvania
Arizona	Kentucky	South Carolina
Arkansas	Maryland	Tennessee
California	Massachusetts	Texas
Colorado	Michigan	Utah
Connecticut	Missouri	Virginia
Delaware	North Carolina	Washington
District of Columbia	North Dakota	West Virginia
Florida	New Jersey	Wisconsin
Georgia	New York	
Hawaii	Nevada	
Idaho	Ohio	

Affiliations:



+1.480.440.2842  
www.fourcv.com

Four Corners Valuations delivers exceptional valuation and advisory services across the US and globally, offering a unique blend of local expertise and international experience. Utilizing advanced technology and superior data sources, we ensure accurate and comprehensive valuations for developers, investors, lenders, and other stakeholders. With licensed professionals across the United States and experienced in more than 60 countries, we are dedicated to excellence and committed to guiding our clients towards informed and successful decisions.

**OFFICE LOCATIONS**

**USA**

Chicago - Dallas - Houston - Los Angeles - Phoenix - Tucson - Washington, DC

**INTERNATIONAL**

Argentina - Barbados - Brazil - Chile - Ecuador - Guatemala - India - Israel  
Mexico - Morocco - Panama - Paraguay - Peru - Philippines - Puerto Rico  
Spain - Taiwan - UAE

**VALUATIONS • MARKET / FEASIBILITY STUDIES • LITIGATION SUPPORT • CONSULTING**  
ESTATES • BANKRUPTCY • PROBATE • DIVORCE • DAMAGED PROPERTY • PARTNERSHIP SOLUTION • MINORITY INTEREST ESTIMATES