HARRISON STREET
ASSET MANAGEMENT

Apartment Alchemy

The Last One Percent

Part One of a Series on How We Invest

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Lorimer House | New York, NY

What Can Be Counted Who Doesn't Always Count; What Counts Can't Always Be Counted

In the institutional apartment market, sophisticated buyers almost always arrive at the same place. They tour the same property, read the same operating statements, study the same widely available market data, and build models that — assumption for assumption — look remarkably alike. By the final round the field is clustered within a point or two, each sharpening a pencil to win. Whether the asset trades at $50 million or $500 million, it comes down to who will stretch for the last one percent of price. Trillions of dollars in transactions usually comes down to very small increments.

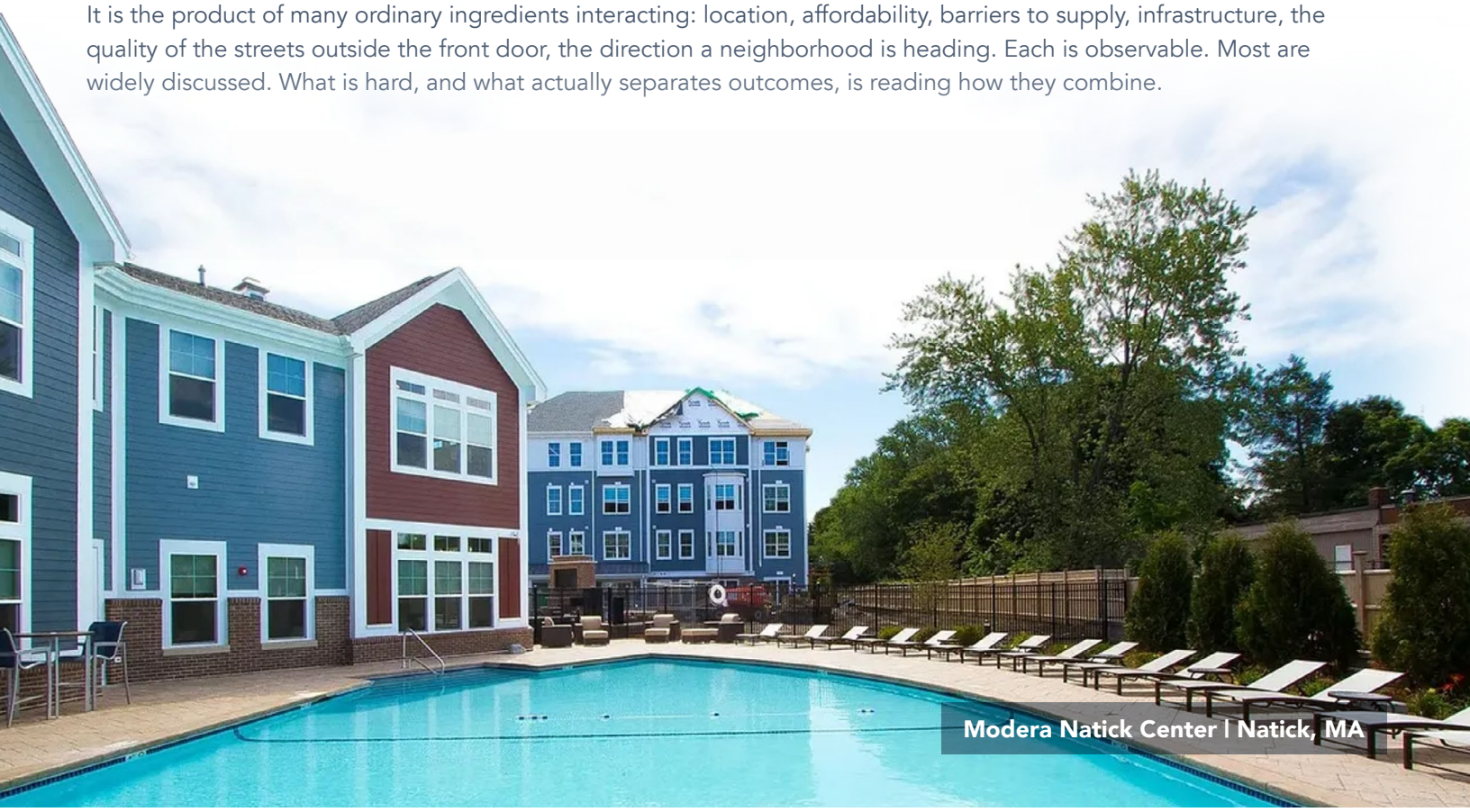
It is striking how much capital, analysis, and debate the industry pours into that final increment. It is more striking how little it explains.

Because the outcomes are not clustered at all. One deal returns 9%. The next returns 18%. The community that looked like every other community in the room compounds into something no model predicted.

We have watched it happen firsthand. A few years ago we sold an asset in a prime submarket where every serious bidder had underwritten to roughly a 9% IRR — efficient pricing by any definition, a room full of professionals agreeing on value. The buyer sold it two years later at a 25% IRR. Lucky or brilliant? Probably a little of both. But here is the part that matters: had any bidder known a 25% outcome was on the table, they would gladly have paid well beyond the last one percent. The price was never the disagreement. The future was.

That is the whole puzzle in a single deal. If everyone sees the same asset and arrives at the same number, outperformance is not coming from the number. It is coming from a view — about a location, a neighborhood, the way a place will evolve over a decade — that the spreadsheet never fully captured.

We have come to call the pursuit of that view **Apartment Alchemy**. Not because there is anything mystical about it — there isn't — but because in a well-covered sector like multifamily, value is rarely the product of one brilliant assumption. It is the product of many ordinary ingredients interacting: location, affordability, barriers to supply, infrastructure, the quality of the streets outside the front door, the direction a neighborhood is heading. Each is observable. Most are widely discussed. What is hard, and what actually separates outcomes, is reading how they combine.



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Price and Value are Not the Same Thing

Our industry is exceptionally good at price. We refine assumptions to the second decimal, debate exit caps to the basis point, and stress-test income to the dollar. That discipline is real, and we are not arguing for less of it. But price is what the model produces, and the model is only as complete as the assumptions inside it. Value is something larger — and some of the inputs that ultimately determine it never fit cleanly into a cell.

The future desirability of a neighborhood. The scarcity created by what cannot be built nearby. A new transit line, a new employer, the slow maturation of a place into somewhere people genuinely want to live. These are not soft considerations; they are frequently the difference between a 9% outcome and a 25% one. They are simply hard to model, so they are often left out of the model entirely — the things that count rarely fit in a cell.

This is also where the idea of "edge" gets misunderstood. Edge is usually imagined as proprietary data or a superior model. But in a sector like multifamily, where institutional-quality third-party data is deep and widely available, nearly every institutional investor today has extraordinary information and capable models. That is not equally true across real estate sectors; in less-transparent markets, proprietary information can itself be a meaningful advantage. But in multifamily, the information itself is rarely the advantage. The advantage is in which questions you choose to ask of it — and in being willing to hold a view about the next decade that the current operating statement does not yet support.

None of this is a license to overpay. Over the years we have lost deals because we would not pay the final increment, and many of those decisions were correct. The point is not that conviction always means paying more. The point is that the decision should never be driven by the spreadsheet alone, because the spreadsheet does not contain everything that will determine how the investment performs.

Where Outcomes are Actually Decided

By the time a competitive process reaches its final round, the math is finished. Every credible bidder has built the model, stress-tested the assumptions, and landed on roughly the same number. What remains is not arithmetic. It is conviction — how completely you understand the ingredients that will shape a place over the next decade, and whether you believe in that future strongly enough to act on it.

Sometimes that conviction tells you to pay the last one percent. Sometimes it tells you to walk away from a deal that pencils perfectly. Both can be exactly right. The discipline is never in the increment; it is in knowing which ingredients are present, which are missing, and whether the price in front of you reflects them.

That is what the rest of this series is about. In the papers that follow, we take the ingredients one at a time — what makes a location durable, why we study neighborhoods before buildings, where rent growth is really going to come from, and how we decide where the next dollar belongs. The last one percent is where every deal ends. It is almost never where the outcome is decided.



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