*Volume 40, No. 3, October 30, 2026*

# QUARTERLY UPDATE

## CWS CAPITAL PARTNERS LLC

*CWS Capital Partners LLC*

CWS

### CALENDAR OF EVENTS

**November 26-27, 2026**
Thanksgiving Holiday and Day After
CWS Offices Closed

**December 25, 2026**
Christmas Holiday
CWS Offices Closed

**January 1, 2027**
New Year's Day Holiday
CWS Offices Closed

**January 15, 2027**
4th Quarter 2026
Est. Tax Payment Due

**January 29, 2027**
4th Quarter 2026
Quarterly Reporting & Distributions

**March 15, 2027**
Year 2026 K-1
First Batch Target Mail-by Date

**April 15, 2027**
2026 Federal/State Tax Filing Deadline
1st Quarter 2027 Est. Payments Due

**April 30, 2027**
1st Quarter 2027
Quarterly Reporting & Distributions

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# THE 5% (DIS)SOLUTION: REVISITING A 16-YEAR-OLD IDEA THROUGH THE LENS OF THE STOCKDALE PARADOX

*By Gary Carmell*



During the Global Financial Crisis, I remember thinking that borrowing rates for apartment owners dropping to 5% or less could solve a lot of looming problems. At the time, apartment owners across the country were dealing with frozen capital markets, weak fundamentals, declining occupancies, and significant refinancing risk. While every downturn has multiple causes and consequences, my basic thesis was straightforward: if borrowing costs eventually fell to approximately 5%, many of the refinancing problems facing apartment owners would largely resolve themselves.

As it turned out, they did.

What followed was one of the most favorable periods for apartment ownership in modern history. The economy recovered, employment improved, and household formations accelerated. The single-family housing market spent years rebuilding from the damage inflicted by the subprime crisis while mortgage underwriting became substantially more

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restrictive. Millions of Americans who might otherwise have become homeowners remained renters instead. Apartment demand strengthened, capital flowed into the sector, and interest rates continued a decline that had already been underway for decades. Cap rates compressed, asset values increased, and apartment owners benefited from a powerful combination of improving fundamentals and declining capital costs.

17 years later, I find myself thinking about that same subject.

Only this time, 5% means something entirely different.

Today, a 5% Treasury yield is no longer a solution. It may be one of the most significant challenges facing apartment owners.

## When the Solution Becomes the Problem

The apartment industry today faces a very different reality than the one we confronted in the aftermath of the Global Financial Crisis starting in 2010. The issue is not the complete absence of debt capital. Financing remains available from banks, insurance companies, Fannie Mae, Freddie Mac, debt funds, and other lenders. The issue is the dramatically higher cost of that capital and the resulting impact on refinance proceeds.

The mathematics are simple but profound. As Treasury yields rise, mortgage coupons rise. As mortgage coupons rise, debt service consumes a larger portion of property cash flow. Because lenders size loans based largely on debt service coverage requirements, higher rates generally translate into lower loan proceeds. The result is that many apartment owners are discovering that replacement loans today may be significantly smaller than the loans they obtained only a few years ago.

The challenge is particularly frustrating because in many cases the underlying properties are not failing operationally. Occupancies may still be healthy. Collections may still be strong. Management teams may still be performing well. Yet refinancing becomes difficult because the capital markets have changed far faster than property fundamentals.

## The Refinance Gap: Then Versus Now

The table at the top of page 3, shows how higher interest rates have decimated loan proceeds as compared to the trough in rates in 2021. This example shows a 10-year apartment loan underwritten in 2021 versus one today. If someone had locked in a 10-year loan in 2021, then the borrower would not be facing a maturity for another four to five years. On the other hand, the Sword of Damocles is still hanging over their head because if rates don't change then property Net Operating Income would have to grow by approximately 42% to generate the same loan proceeds as in 2021! If this does not happen, which is the most likely scenario, then they will either need to infuse capital to refinance the property or sell to avoid this.

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| | 2021 | Today | |
|---|---|---|---|
| Net Operating Income | $3,000,000 | $3,150,000 | |
| 10-Year Treasury Yield | 1.50% | 5.24% | |
| Spread | 2.00% | 1.25% | |
| Interest Rate | 3.50% | 6.49% | |
| Amortization | 30 | 30 | |
| Debt Service Coverage Ratio | 1.25 | 1.25 | |
| Debt Yield | 6.74% | 9.47% | 40.5% |
| | | | |
| Loan Proceeds | $44,500,000 | $33,300,000 | -25.2% |

The situation is even more challenging for loans coming due in 2027 as virtually all fixed-rate loans originated between five and ten years ago had rates that were quite a bit lower as this chart shows of the 10-year Treasury yield. The same pattern holds for the 5-year yield as well.




***Many refinance challenges today are not the result of deteriorating operations. They are the result of the same cash flow supporting significantly less debt in a higher-rate environment.***

This single chart may do more to explain today's refinancing challenges than several pages of narrative.

Now, I do think I should back up a bit and recognize that in a free market system, capital will form to take advantage of favorable risk-reward situations. It's this financing gap that has resulted in a tremendous amount of money having been raised inside private, non-regulated debt fund vehicles. These funds provide much more leverage than Fannie Mae and Freddie Mac to help close the refinancing gap but naturally it comes at a higher interest rate and has more fees associated with them.

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We have almost always avoided these loans when acquiring properties due to their short-term nature and higher risk, but we have had to tap into this market from a refinance perspective as the financing gap with Fannie and Freddie would have necessitated far too much of a capital infusion to refinance with them. We have refinanced six properties utilizing debt funds with two more in process. We also paid off one of them with the fortuitous sale of one of our properties in Atlanta.

We have leaned into this financing primarily for newly constructed properties that when stabilized, generated yields-on-cost that were less than projected due to the need to offer heavy rent concessions. This is particularly the case for a saturated market like Austin, which has a large number of newly constructed communities needing to fill their apartments and the fastest way to do this is through very generous pricing incentives. Three of our debt fund loans were for properties we developed in Austin.

With the big run-up in long-term rates and a still challenging operating environment, it's now getting to the point where debt funds may not be able to fully bridge the gap and will still require capital infusion from sponsors and their investors. This is the case for the two properties we are in the process of refinancing with debt funds (one in Atlanta and one in Seattle).

**Has the Forty-Year Interest Rate Tailwind Ended?**

The refinancing challenge becomes even more significant when viewed within the context of a larger question that investors must ask themselves: what if the forty-year trend of steadily declining interest rates has ended?

For much of my professional career, real estate investors benefited from what amounted to a structural tailwind. Beginning in the early 1980s, interest rates generally trended downward through recessions, financial crises, geopolitical shocks, and economic recoveries. Each cycle typically began at a lower interest-rate starting point than the one before it. Refinancing often meant lower borrowing costs. Higher leverage could often be supported. Asset values generally benefited.

Many investment models became conditioned to expect that reality.

I am increasingly skeptical that this environment still exists.

Could interest rates decline from current levels? Certainly. Predicting interest rates has humbled far smarter people than me. But I increasingly believe the burden of proof belongs to the bond bulls rather than the bond bears. Government debt levels are substantially higher than they were a decade ago. Fiscal deficits remain significant. Inflation proved much harder to tame than many expected following the pandemic. Labor shortages, supply chain restructuring, energy investment requirements, geopolitical tensions, and demographic shifts all suggest that the inflationary pressures of the future may prove different than those of the past.

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If the long-term decline in interest rates has indeed been interrupted or reversed, the implications for real estate investors are meaningful. The industry would need to adapt to a world in which capital no longer becomes progressively cheaper over time.




***For forty years, falling interest rates supported real estate values. Whether that trend remains intact may be one of the most important questions facing investors today.***

The next rate threshold I'm keeping an eye on is 5.44%, which was the previous peak in April 2002 now that the trend line has been broken in which for nearly 40 years we had lower highs and lower lows. Now we need to be alert to higher lows and higher highs in rates.

## Apartment Fundamentals Face Their Own Challenges

Complicating matters is the fact that apartment fundamentals themselves look very different today than they did in 2010. Back then, development activity had largely collapsed. New supply was limited, homeownership had become difficult, and apartment demand steadily absorbed available inventory.

Today's environment is more complex. The Sunbelt in particular has experienced one of the largest construction waves in apartment history. Markets such as Austin, Phoenix, Nashville, Charlotte, Dallas, Tampa, and others benefited enormously from migration, job growth, and demographic trends. Developers responded rationally by producing new housing. In some markets they produced a great deal of it.

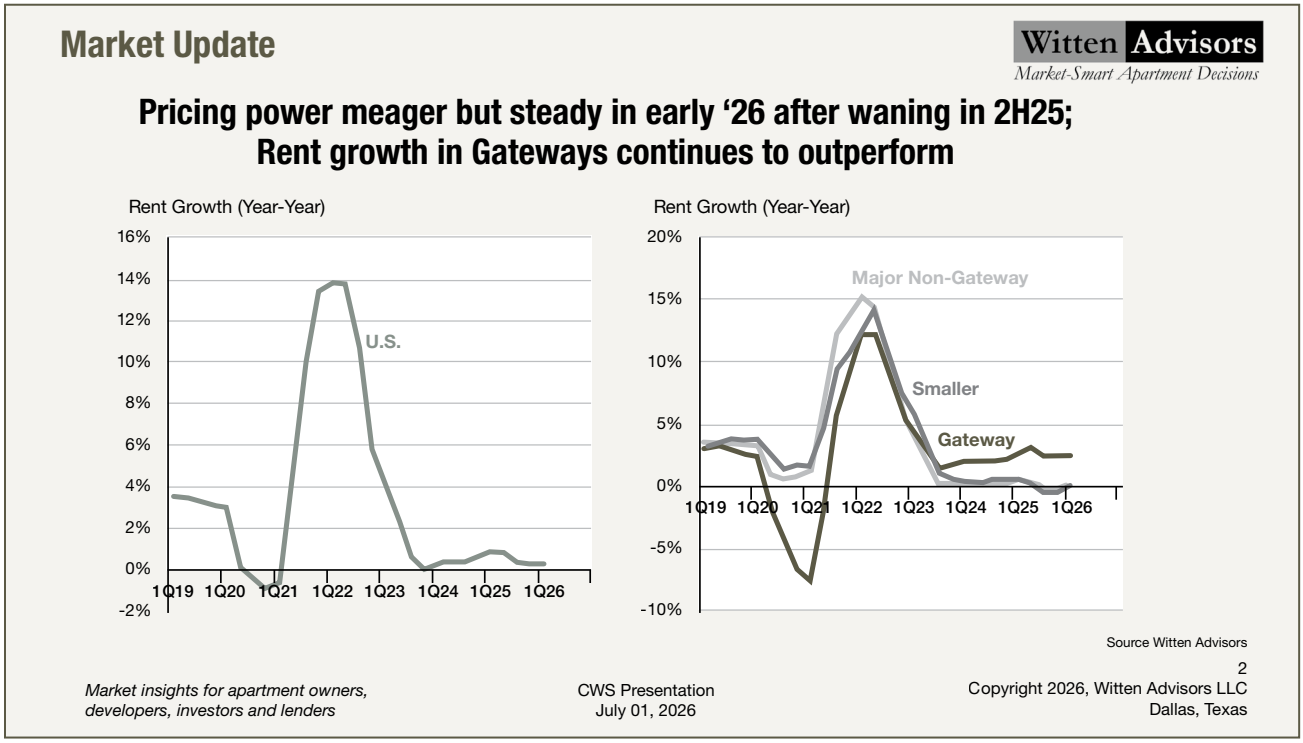
As often happens, success eventually sowed the seeds of its own challenges.

The results are evident today in the form of higher concessions, slower rent growth, increased competitive pressure, and lower net effective rents in many submarkets. At the same time, operating expenses continue to face pressure from insurance costs, property taxes, labor expenses, maintenance costs, and ongoing government intervention in housing. None of these headwinds are insurmountable, but together they create a significantly different operating environment than the one apartment owners enjoyed for much of the last decade.

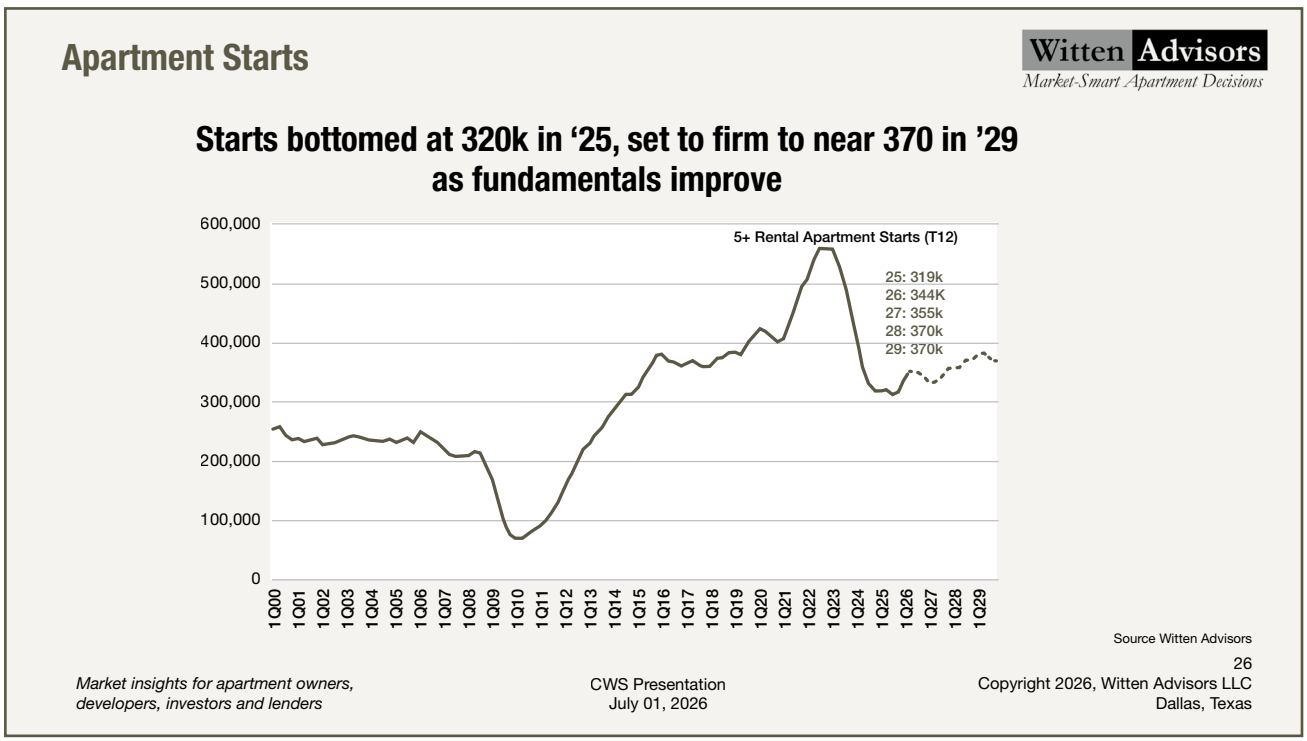
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One can see from this chart how rent growth came crashing down after the Covid burst and, apart from gateway cities like San Franciso and New York, they have yet to start growing again.




The lack of rent growth has been due to unprecedented supply that has finally tapered off. And while Witten Advisors is expecting apartment starts to rise going forward, I'm skeptical given how difficult the financing market is.




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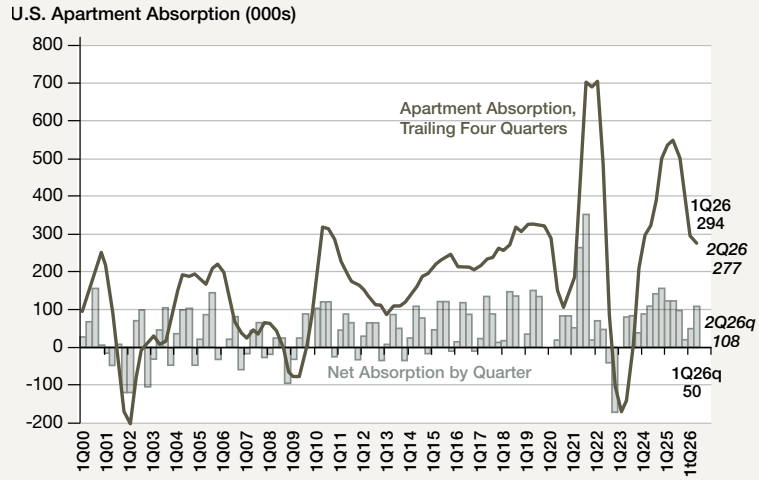
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Pricing incentives have done what they are supposed to do, which is stimulate apartment demand. Fortunately, demand has generally kept up with supply but at the cost of owner pricing power.

**Market Update**

Witten Advisors
*Market-Smart Apartment Decisions*

**1Q26 quarterly leasing firmed to 50k** ***(from 20k in the final three months of '25)*****;**
**Annual demand ebbed to~294k in 1Q26**




Source Witten Advisors

4

*Market insights for apartment owners, developers, investors and lenders*

CWS Presentation
July 01, 2026

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## The Stockdale Paradox and the Brutal Facts

Admiral James Stockdale, who survived more than seven years as a prisoner of war in Vietnam, famously observed that successful people are capable of confronting the brutal facts of their situation while never losing faith that they will ultimately prevail.

That idea has always resonated with me because it applies remarkably well to investing.

The brutal facts today are fairly clear. Some apartment owners will need to contribute additional equity when loans mature. Some properties will trade below prior expectations. Some lenders will become increasingly conservative. Some investment assumptions made during the extraordinarily low-rate environment of 2020 through 2022 will prove too optimistic. Some assets will require more time than originally anticipated to reach their potential.

Those realities deserve acknowledgment rather than denial.

Yet that is only half of the Stockdale Paradox.

## What If the Public Markets Are Already Pricing in Most of the Bad News?

One of the more fascinating developments of the past several years has been the stark divergence between apartment REITs and the broader stock market. While technology companies and artificial intelligence beneficiaries have captured the imagination of investors, apartment REITs have spent much of the last several years under pressure from concerns

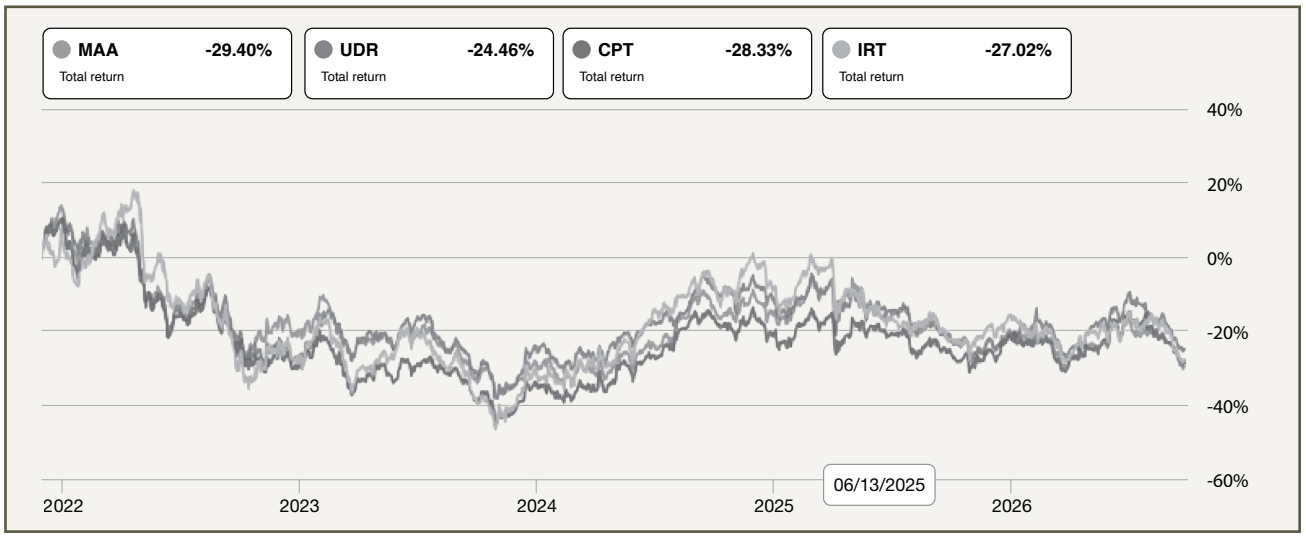
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surrounding interest rates, slowing rent growth, and new supply.

The result has been a substantial gap in performance.

The following chart shows the total return for four apartment REITs since December 2021. One can see that they are down between 24% and 29%. As a frame of reference, the S&P 500's total return has been approximately 78%.




***Apartment REITs have materially underperformed the broader stock market. Whether this reflects apartment undervaluation, stock market overvaluation, or some combination of both remains an open question.***

The chart is not intended to prove that apartments are cheap. It may actually prove the opposite. The point is that public investors are already expressing a strong opinion about future apartment performance. Public REIT valuations today imply far more skepticism than most private-market transactions would suggest.

The Stockdale Paradox requires us to hold competing possibilities in our minds simultaneously. It is entirely possible that apartment values have further to fall. It is equally possible that public REITs have already discounted much of that bad news. It is even possible that the recent enthusiasm surrounding portions of the stock market has created relative opportunities elsewhere. None of us know with certainty which of these outcomes will ultimately prove correct.

What we can observe is that pessimism toward apartments appears significantly greater today than it was just a few years ago.

Historically, that has not always been a bad starting point for long-term investors.

## Why I Remain (Cautiously) Optimistic

Despite everything I have written thus far, I remain optimistic about apartments over the long term. People continue to need housing. Household formations continue. Homeownership remains financially challenging for many Americans. Most importantly, the very forces creating

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many of today's difficulties are also creating some of tomorrow's opportunities.

Higher interest rates are making development increasingly difficult. Construction starts have already fallen significantly. Existing supply will eventually be absorbed. Markets will rebalance. Cycles will turn just as they always have.

CWS has operated through inflationary environments, recessions, savings-and-loan crises, the Global Financial Crisis, the pandemic, and everything in between. No two cycles look exactly alike, but they all share one common characteristic: eventually they end.

That does not mean the path forward will be easy. It simply means that periods of challenge often create opportunities for disciplined and patient investors.

**The Real Solution**

Perhaps the most important lesson from revisiting my article from sixteen years ago is that there never was a permanent 5% solution. Every cycle presents a new problem. In 2010, weak fundamentals and frozen capital markets created the challenge. Today, refinancing gaps, elevated supply, rising expenses, and higher interest rates create a different challenge. Tomorrow's challenge will undoubtedly be something else.

The real solution has never been a particular interest rate.

The real solution is adaptability.

It is maintaining liquidity when others become overextended. It is operating properties exceptionally well when margins become compressed. It is remaining realistic when others become euphoric and remaining optimistic when others become discouraged.

That, ultimately, is the essence of the Stockdale Paradox.

The refinancing challenges are real. The supply overhang is real. The headwinds are real.

But so are the opportunities.

In 2010, 5% was the solution. In 2026, 5% may be the dis-solution. Yet successful investing has never depended entirely on accurately forecasting interest rates. It has depended on the ability to navigate uncertainty, maintain discipline through difficult periods, and recognize opportunity when pessimism becomes excessive.

Today, pessimism is rising.

History suggests that is precisely when thoughtful investors should pay the closest attention.

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