EPISODE 464

[INTRODUCTION]

[00:00:00] ANNOUNCER: Welcome to The Real Estate Syndication Show. Whether you are a seasoned investor or building a new real estate business, this is the show for you. Whitney Sewell talks to top experts in the business. Our goal is to help you master real estate syndication.

And now your host, Whitney Sewell.

[INTERVIEW]

[0:00:24.1] WS: This is your daily Real Estate Syndication show. I'm your host Whitney Sewell. Today, our guest is Fernando Angelucci, thanks for being on the show Fernando.

[0:00:33.4] FA: Thanks for having me Whitney.

[0:00:35.1] WS: I'm looking forward to this and just a little bit of our conversation – he's got properties in almost half of the states in the United States. It's pretty incredible and looking to grow so I'm looking forward to this conversation and in the types of properties that he is investing in and why as supposed to some asset classes that some of the rest of us are focused on.

Looking forward to this conversation and obviously he's an expert in this business and very successful. A little about Fernando. As the founder and president of Titan Wealth Group, he leads the firm's finance and acquisitions departments. Titan Wealth Group operates nationwide sourcing off market investment properties for Titan Wealth Group's acquisition, as well as serving a network of thousands of active real estate investors nationwide and worldwide.

Prior to founding Titan Wealth Group, he worked for Dow Chemical rolling out a flagship product estimated to gross one billion dollars in global revenues. With an engineering background, Fernando's able to approach real estate investing with a keen analytical mindset that allows Titan Wealth Group to identify opportunities and project accurate pictures of future performance.

Fernando, thank you again for your time in sharing your expertise on the show with us today or myself and the listeners. Tell them a little more about who you are, maybe where you're located and your all's focus and let's jump in.

[0:01:55.5] FA: Yeah, I'm currently located in Chicago, Illinois. We now primarily invest in self-storage properties and there's a whole history behind that, I'll kind of keep it short but you know, when I was an engineer working for Dow, I was really tired of the nine to five life. Well, for me it's more of a five AM to nine PM life. I immediately started investing in single family homes on the side.

Within about 13 months, I was able to replace my income and leave the nine to five life to be a full time real estate investor. From there, I quickly grew into doing flips for single family, buying single family rentals and buying multi-family rentals, and I kept having problems with the eviction process, you know?

Chicago is a city where the laws are extremely tenant friendly and if you do everything by the book, it can take six to eight months to get a bad tenant out of one of your properties and not to mention the amount of damage that they cause on the back end so I was looking for another avenue that would solve those types of problems for me while still providing a very consistent passive income to me and my investors and that's when I actually, I came across self-storage.

I was at a real estate expo that I had attended and all the problems that I had been having, you know, the speaker, it just seemed like he was speaking to me. We got started, in the beginning, we started off by wholesaling self-storage facilities just to make sure we were running the numbers correctly.

The way I look at it is if I can wholesale self-storage facility, that means that I'm getting it at a price that makes sense and investors are willing to pay me more than what I got under contract for. Once we did a few of those, then we started feeling comfortable and taking on our own acquisitions and then since then we've been growing extremely fast.

[0:03:44.3] WS: Chicago, I mean, the tenant issues, evicting taking six months. I mean, I could see why that would push a lot of landlords into a different asset class or looking for something else. That happened to you – if you just bought a duplex, thinking you're just getting started and that happens to you, you're thinking, "Okay, this is not for me."

[0:04:02.3] WS: Right, especially, you know, in Chicago where a lot of people enter the buy and hold multi-family markets. Usually in CND areas and I was no different. I started buying properties on the south side of Chicago which in and itself brings a lot of hardship in managing that type of tenant. Low income tenant. Half of the time they're on some type of section eight program, vouchers.

It is very difficult to manage that. I know a lot of really good investors that they have that management in place. But for me, you know, I like to go with the path of least resistance and that was self-storage. I started – I'm a very analytical person, I like data, I like looking at historical performance so that's one of the things that I actually prepared for the show here, just looking at a little bit of performance over the last 10, 20 years.

When we're looking at self-storage versus other asset classes, there's a study done by [inaudible 0:04:59], looking at the 2017 value of $100,000 invested in 1994. If you put that $100,000 in the SMP 500, by 2017, that would have grown to roughly half a million dollars.

If you put em in apartments, that $100,000 would have grown to about 1.7 million dollars. If you put them in self-storage, that $100,000 would have grown to little over four million dollars. When you look at those returns over those periods of time, you see that, you know, the SMP returned about seven and a half percent, apartment buildings on average, returned about 13.3% and then self-storage returned about 17.4% as an average annual return. Now, 4% may not seem like a lot.

But when you factor compounding interest, that's how you're able to almost double the return in real dollars over that period of time. Now, you know, that's a pretty large period of time, 1994 to 2017, but let's talk about recession tolerance. Between '07 and '09, in the same study, we saw that the SMP 500, they lost about 22% in value. The apartment sector did much better. It only lost about 7%, but during that time in self-storage space, they lost about 3.8% in valuations and the reason why is self-storage is an asset class that caters to those in transition.

That's true of people who are, let's say, downsizing on their home because they can no longer afford a 2,400 square foot mortgage. Maybe they go down to 1,200 square foot home but they have these sentimental possessions that they're not just going to get rid of. If your child – for example, this is an example that I have in my own family.

My father – I'm a grown man but my father still has all the drawings I made for him when I was three, four years old. He's never going to throw those away and that's – the same thing is true when someone's downsizing. Self-storage also caters to the two largest population groups in the nation. You have the baby boomers right now, historically starting to retire but I think it's about 10,000 baby boomers a day retire. They're looking to downsize in property and they're also – on the older end of that age are going into retirement homes.

That is a much more confined space. Yet, they have a lot ofsentimental value in the things that they have and they don't want to get rid of them so they usually put them in self-storage. It makes a lot more sense to cut 1,200 square feet off of your housing size and then just go pay for an extra hundred square feet that you need monthly. The second group that self-storage caters to quite a bit is the millennials and the Gen Xers.

The trend of moving to the suburbs is no longer what is driving a lot of development and housing right now. What we're finding in the groups that are you know, aged 18 to 34 is they're actually moving closer to the city centers because they want to be around the action. They want to be around the great food scenes. They want to be around the event space.

[0:08:02.2] WS: They're not looking for the farm life.

[0:08:03.6] FA: Right. What they're doing is they're opting for smaller housing, maybe 700 square feet to a thousand square feet in these high rises, these condos, and then they're using a self-storage space, maybe a hundred square feet, 150 square feet, it's kind of like an exterior closet, and any time they say they want to go hike or they want to go kayaking or they have clothes for the winter when it's the summer, they can go to that unit, you know, pay an extra 80 bucks a month or a hundred bucks a month for that additional square footage and it allows them to live closer to city center at as more reasonable price range.

Those are the two main things that got me really attracted to this space. Then when I actually started getting involved, I noticed that the leverage that was being offered to me from banks was far superior to any other asset class that I had pursued leverage on before.

I started to dig in to see why that was. You know, I'm talking, the worst case scenario loans I've gotten so far were 80% loan to value. The last three properties I've closed, they actually appraised at a good enough value that I was able to not only close them with no down payment but I actually was able to pull cash out at closing by purchase up.

The banks were paying me to buy an asset that had positive cash flow. I don't know of any other investors that have done that in other asset classes. I wanted to dig deep and see why was that the case and when you start digging into the data, I looked at Intech solutions which is an aggregator, I look at Wells Fargo securities and what we found was self-storage had a much lower default rate compared to any other asset class.

Let's just use January of 18 is the most recent data I have. Self-storage, their loans on average across everyone surveyed were defaulting at a rate of about .04%. Multi-family in the same stretch was defaulting at a rate of 1.83%. That's a huge order of magnitude difference. Then when you actually look at the default data, when that rare default did occur in self-storage, the amount of loss experienced by the bank was actually much lower than all other asset classes as well.

You look at multi-family. When a bank disposed of those loans, they usually experience a loss of somewhere around 4.3, 4.4%. Self-storage, the loss per default was at 1.5% range. Again, three times lower than multi-family. Then I started to see why banks were giving me such great leverage is because they use self-storage to offset the riskier loans they are giving.

Specifically, banks that were doing new construction loans and single family fix and flip loans, they loved our product. It did take a little bit of, you know, convincing them by showing them this data and showing them where the data sources came from but very quickly, if a bank was not familiar with self-storage, very quickly they started fighting for our loans.

[0:11:02.4] WS: Do you know if those numbers are all commercial properties or is that like from a duplex to any multi-family or –

[0:11:09.5] FA: It's commercial multi-family so five plus units.

[0:11:12.2] WS: Okay, yeah.

[0:11:13.6] FA: Another thing that I really like about self-storage is the fact that the market is extremely fragmented. What do I mean by that? When you look at the apartment space, a large percentage of the housing stock in the multi-family space is owned by large operators. When you look at self-storage, it's the exact opposite.

19% of all the facilities owned in the US are owned by the six largest companies. Another 9% are owned by the next 100 largest operators leaving 72% of the facilitates in the US are owned by what I say, 'mom and pop operators'. These are operators, they have two or less facilities.

That means I have a much easier time finding off market properties. I can negotiate cap rates that would make multi-family investors cry. Right now, my average across my portfolio on the day of acquisition is a 9.8% cap rate and then when we do the value ad, we're usually adding another four to 5% on to that internal cap rate, you know?

If you tell a multi-family investor, you're buying an asset and you can assume that you can pick it up at a 9.8 or a 10% cap rate, they're going to laugh at you. Especially in the environment we're in right now where we're seeing heavy cap rate compression and there's a lot of competition from the big boys with the deep pockets, right?

[0:12:33.2] WS: I wonder how many more, what the number of properties are though that are self-storage versus, you know, multi-family though that are on the market or just all together.

[0:12:42.0] FA: As of 2017, the self-storage almanac estimated the total number of facilities in the US could be somewhere between 44 and 52,000. There is much less when it comes to the number of facilities. But, at the same time, you know, on average, nine out of 10 facilities that come across my desk are off market. There's no brokers involved.

And there's nothing wrong with brokers but they are very good at their job. Their job is to get as many eyes on a facility as possible to raise the price to market, right? When you're the only person negotiating at the table, you have a much better chance of securing that asset at a range, again, that would make some brokers gawk. The fragmented market is something I really like.

The biggest thing for me which is a huge headache was you know, there's no tenants, toilets or trash. Because of that, we have much lower break even occupancies. For example, in my multi-family properties, I would have to keep an occupancy of anywhere between 80 to 85% to pay the bills.

[0:13:50.6] WS: What type of multi-family properties were you operating then?

[0:13:54.0] FA: These were 12 to 24 unit properties primarily, is where I was kind of my bread and butter. We did some stuff smaller as well. Just for the sake of this conversation. When I did an assessment of our portfolio in the self-storage space, our leveraged assets, we need to be in the mid to high 60% range to break even. For our un-leveraged assets, ones we purchased cash, we'd need only around a low to mid 30% occupancy range, took me a break even territory.

Again, it just becomes – it's because of the low overhead. I have minimal utilities, if any. I have some properties where they have no utilities running to them. There's no carpet cleaning, there's no painting, there's no leaky faucets, there's no winter HVAC failures, there's no water heaters exploding.

Self-storage is pretty simple, you know? When we're looking at the first generation and some of the second generation facilities, we're talking concrete slab with corrugated metal steel walls and ceilings. There's not much you can do to really mess that up, right?

The second thing that I love is kind of along the same vein is easy ‘evictions’, right? The reason that I use air quotes here is because they’re not evictions. With landlords and multi-family, you have to go through the landlord tenant law which is where the evictions lie. In self-storage we’re guided by lien law, or what’s called property law.

When you store your possessions at my facility, we are entering in to a contract that states, if you don’t pay me, I can lien your property and and if you don’t pay me in enough time, I could sell your property to satisfy that lien. A typical, let’s talk about some of my last multi-family deals. I had a deal. It took 8 months to get a tenant out of one of our units. We unfortunately inherited that tenant when we purchased that property and she was in bed with all the tenants’ rights, lawyers and they kept playing games on us.

Switching out sensors and smoke detectors so that we kept failing our inspection so she was able to push out that process into eight months eviction timeline. Now, not only are we talking about the eight months of lost rent but then when she left, she costs $20,000 worth of damage to the unit. She destroyed all the drywall, cut all the electrical, poured concrete down the plumbing. I mean it was a true nightmare.

[0:16:12.0] WS: I would say is part of that is you are investing in the wrong city or the wrong story.

[0:16:15.9] FA: Correct, wrong areas, right? So now let’s look at self-storage and how that works. On the fifth day you get a notice that says, “You have to pay me and then a manager puts an over lock onto the unit. So now there is two locks onto the unit. If they don’t pay me within a 30 to 45 day period from the day of that five day notice, I start the lien process. I put two notifications into a local newspaper saying, “Here is the units that we are going to be auctioning off. Here is the date to settle any issues. If you like to participate in the auction, here is the link to the website we do online auctions.”

And within 45 days of that tenant becoming late, we sell all of their stuff off. We recoup all of our lost rent and then someone goes in there with a large push broom, sweeps up the dust and we get a new tenant the same day.

[0:17:03.7] WS: Are there states that have unfriendly or I guess landlord laws for self-storage operators?

[0:17:09.3] FA: No, so the worst days that we see is they just have a little bit longer timeline. So 60 days as oppose to a 30 day lien process but for the most part, this is one of those – when landlords are being attacked in the news it is always, "Oh somebody, you know, we put out an old lady that couldn't pay her rent," and there's this heartthrob portion of it and that is why the law becomes so difficult against landlords in states like Illinois, California, New York.

But you are not going to get that same type of heartthrob type situation when you have someone say, "Hey, this person didn't pay on their unit for 30 days and we auctioned off their suitcases that they had in there." Who is going to really feel for that person, right? So that is why I think overtime – and this is me just speculating, I think over time landlord-tenant law has become so strict and restrictive whereas self-storage law has been pretty unchanging if you will.

I mean the process is very easy. The way the laws read, they are extremely in the property owner's favor. So for example when somebody rents a unit from me they are already agreeing to the fact that they mandatory have to get renter's insurance for this stuff and that we have no liability as expressed or implied in protecting their stuff above and beyond providing a space for you to store your stuff. If the property burns to the ground, if it gets hit by a hurricane, anything like that that is not on us.

That is on you guys, they're on the tenant. So we have much less liability with this asset class than you would when there is an expressed and implied warranty of habitation, right? There is no warranty of habitation with self-storage because you are not allowed to live in our units.

[0:18:55.3] WS: You'd better not be, right?

[0:18:56.2] FA: Right, exactly. So there is a lot of similarities but at the same time, some heavy contrast. Another thing that I like is because there is less people involved there is less moving parts. That equals less management. So for a facility – for example, I am looking at a portfolio right now. Five properties, they're all within about a 50 mile radius of each other. All we need is one full time person to manage that portfolio. Now say we had a portfolio of five apartment buildings that were spread within a 50 mile radius of each other. How many people do you need to run that facility, right?

So that's why our operational costs are much lower. On average, we're experiencing, like I said, we are experiencing expense ratios in 19 to 25% range whereas when we were doing multifamily, our expense ratios were on the good side 35%, but usually it would be closer to the 45, 50% expense ratio.

[0:19:54.3] WS: Tell me something you don't like about self-storage?

[0:19:56.4] FA: Yeah, so there is a current trend right now. I will try to remember her name, I think it is Marie Condo, about de-cluttering your life, getting rid of things that are just taking up space in your house that don't bring you joy, just get rid of those things. So that is one of the people that are fighting us at that same time, if we just put a little bit of spin on it, we could say, "Hey, get rid of these items in your home but just move them into a self-storage facility."

[0:20:21.7] WS: You don't have to get rid of them permanently, right?

[0:20:24.8] FA: Right, another very interesting development in the self-storage space is technology. You know, where other asset classes have adopted technology rather quickly, self-storage has been one of those where it is taking quite a while for operators to adopt technology. So in just recently are we seeing man-less facilities where there's a kiosk system to use to rent and purchase your unit, to purchase renter's insurance and a lock and then you can use an app on your phone to open the gate, open your individual unit.

You know, these are – it is interesting the technology that's breaking into the space but again, it is one of those things where self-storage is a very hands off type of business that I think a lot of operators have been hesitant to adopt these technologies, which in turn causes these technologies to be pretty expensive when they break into the market. There is an example – there is this one system that one of the largest providers of self-storage doors and dividers provides, which allows all units in your facility to be controlled with a phone app.

Right now, it is a little cost prohibitive because it costs about 300 to 350, 400 bucks a unit to install that but overtime as more investors adopt that technology and there is a scale associated with the vendor, we are going to start seeing those prices drop, right?

Another thing I really like in self-storage versus multifamily is that it has a very high sticky factor. So what I mean by sticky factor is say I have a $150 unit. I can increase the rent on that $150 unit by $20 a month and that will be equivalent of a 13% increase to the bottom line. Now a renter is not going to take the time and then not only the cost to move to a new facility to save that 20 bucks. You know, if we are talking a solid 10 by 15 unit 150 square feet that means you are going to have to rent a truck, pay for the gas, pay for the time off to move there and for.

Maybe get some helpers in moving in and out if they are not able bodied. You know you are looking at $500 to a $600 cost to move to a facility over a $20 increase. It just makes more sense to stay there for an extra two or three years and absorb that. Now imagine if you tried to raise your monthly rent on one of your apartment units by 13%. Your tenants would immediately move out. I mean, when we were in the multifamily business and we are raising rents by 3% a year, we would get mass exodus from our units, because one of the things about self-storage versus multi families is that it is highly localized. For example, I am here in Chicago. I am in the near south side.

[0:23:16.2] WS: Again, don't buy in Chicago.

[0:23:18.4] FA: Right but what I can do is if I didn't like where I was living, I'd be willing to move to the north side of Chicago or the north-west side of Chicago. I am willing to go five to 10 miles away to get a good deal on an apartment, right? Whereas with self-storage, usually what we find is 90% of our tenant base comes from a three mile radius around our property. No one is going to drive 50 miles to go save an extra five to 10 bucks on a unit.

Our tenants are much more sticky if you will and then the last thing that I really like about self-storage is the fact that you have multiple profit centers not just rent, right? I have a list here just some of the most common profit centers, ancillary profit centers that we had in self-storage, you can do car storage, boat storage, RV storage. We could sell locks, we could sell renter's insurance and take a premium, you know maybe 60% of our renter's insurance premiums come right back to us as the operator who is selling and pushing that product.

We could sell moving supplies, packaging supplies. We can do FedEx, we can have printing services. We can add cell towers on our land, billboards that we can rent out. Truck rentals, private mailboxes, wine storage. The list goes on and that way I am not beholden to one way of making an income.

You know, everyone that likes to talk about passive investments and talk about building a portfolio, they say, "You know it is all about multiple streams of income." Now what if I told you that you can make five or 10 different streams of income off of just one real estate asset? That is much better than buying multifamily and the medical office and industrial property and single family homes and Airbnb's and so it's just one of those things where the more and more I looked at it, I just couldn't not get into the space.

[0:24:57.7] WS: How do you feel about the growing competition right now as far as lots of people trying to get into self-storage business right now or do you feel that that's extremely competitive or how do you feel?

[0:25:07.9] FA: Yeah, I mean I love it. So I break apart competition into two brackets. There is the REITs or the pseudo REITs, so these are the guys with the deep pockets and they are driving up rents in areas. I like when they come into an area near me. You know, I specialize in class B and class C properties and secondary and tertiary markets.

So when a large REIT competitor moves into town they immediately raise all their rents for the entire market and all I have to do is I just piggyback off of their marketing so I don't even have to pay for advertising and I just undercut their price by about five bucks per unit and now I am getting free leads coming my way because someone's price sensitive and they're shopping.

Now on the lower rung, you have the newer investors coming into the space. I don't really look at anyone of these people as competitors. I always look at everyone as a potential partner. You know, these are investors that they want to learn how to get into the business, maybe they are buying their very first facility. Maybe they need help on their very first facility and they end up calling me in the markets that I am a heavy presence in and either bringing me deals, bringing me capital just to show them how to do the deals. Again, like I said before, self-storage is a hyper fragmented market. So to get to the point of competition that you are seeing in multifamily it's going to take the big REITs they have to buy another 60, 70% of the market, which is not going to happen. It is just impossible to get to that many owners in such a short period of time.

[0:26:34.6] WS: All right Fernando, just a couple more questions before we run out of time but you know, how are you all prepared for this potential downturn that everybody talks about?

[0:26:42.1] FA: Yes, so the reason I went into self-storage was motivated partly because of that. Like I said in downturns, self-storage performed better than any other real estate asset class.

[0:26:51.7] WS: What is a way you all have recently improved your business that we could apply to ours?

[0:26:55.5] FA: I think it is very important to get a common vision across your entire organization. So we actually hired an EOS implementer from – the book is *Traction* from Gino Wickman. As soon as they brought that in, our company started growing by 200%. It was just important to get the entrepreneurs in the company organized. You know with entrepreneurs, they usually are very gregarious and sometimes when you have a bunch of them in the same room they'd start butting heads.

So it is great to bring in a third party that has no course in the race to say, "Hey guys, here is what I am hearing your common goal is, how do we apply that so we are all moving in the same direction?"

[0:27:35.4] WS: Yeah and what is your best advice for caring for an investor so they want to come back to the next opportunity?

[0:27:41.0] FA: Yeah, so with our deals, what we do is we never will cash an investor out. So once they put out their money into our deal, there will be a capital event to return their capital but then they stay in equity owner in that deal for a lifetime. So our model is not to ever – if we can help it, not to ever sell any properties and just to keep adding for passive income and we think our investors should come along on that ride with us.

[0:28:06.1] WS: Nice and what is the number one thing that's contributed to your success?

[0:28:09.6] FA: I am going to have to say standing on the shoulders of giants. You know nothing here that I've said today I came up with myself. It's all been my mentors and my coaches that I have surrounded myself with. If you surround yourself with people that are performing at a higher level than you are, you're eventually going to rise to meet them at that level.

[0:28:30.1] WS: And how do you like to give back?

[0:28:31.7] FA: We love to do volunteer events. It's actually part of our mission in the self-storage company. We give back to the local communities that are patroning our facilities. So we do local events supporting baseball teams, soccer teams, the police force in the area. We do a lot of food drives. I come from Brazil where food stability is not guaranteed and then what we have noticed is even here in our own soil and in our own backyard there is people that they don't know where the next meal is going to come from.

So no sense in sending money to a different country when you have people in your own backyard, other Americans that are insecure about where their food is going to come from.

[0:29:11.3] WS: Well Fernando thanks for giving back in that way and I appreciate you giving back to the listeners and myself. I wonder how many you've convinced from multifamily or from mobile home parks or some other asset class to self-storage but tell them how they can get in touch with you.

[0:29:24.8] FA: Yeah, so the easiest way is to just Google my name, Fernando Angelucci. You can find our websites, our Facebook, our social media handles. I also give out my cellphone number to people and I will do it right now, it's area code 630-408-8090 that is my number. Shoot me a text message or give me a call I will answer any questions they have I'd be more than happy to help.

[0:29:49.2] WS: Awesome, Fernando that's a wrap. Thank you very much.

[END OF INTERVIEW]

[0:29:51.7] WS: Don't go yet, thank you for listening to today's episode. I would love it if you would go to iTunes right now and leave a rating and written review. I want to hear your feedback. It makes a big difference in getting the podcast out there. You can also go to the Real Estate Syndication Show on Facebook so you can connect with me and we can also receive feedback and your questions there that you want me to answer on the show.

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[OUTRO]

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