

**EPISODE 659**

[INTRODUCTION]

**[0:00:00.0] 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]

**[0:00:24.4] WS:** This is your daily Real Estate Syndication Show. I'm your host Whitney Sewell. Today, our guest is Nathan Cloud, thanks for being on the show Nathan.

**[0:00:33.4] NC:** Looking forward to it.

**[0:00:35.9] WS:** Nathan worked on Wall Street as a senior equity trader for a proprietary trading firm, managing multiple portfolios and strategies. Since inception in 2019, Cloud Capital has sourced and closed 24 million dollars in multi-family assets. And their newsletter, it's read by over 1,000 investors every month. Nathan, welcome to the show, it's a pleasure to meet you and you've been willing to share your expertise, I'm grateful for that. Give us a little more about who you are and coming from Wall street and into Cloud Capital and maybe a little bit about that transition and let's dive into your super power.

**[0:01:11.8] NC:** First of all Whitney, I've been following your podcast for about a year now and I really appreciate you having me on. I think you provide a ton of value out there, specifically diving deep into so many different facets of this business. Thank you for all the value that you do. Yeah, I'm excited to be here.

So, the background — accounting background, went to school, interned for Big Four — honestly, I just wasn't passionate about accounting, it just was not my route in life. What I

always want to do is just work on Wall Street. After accounting went up there for six years where I worked for — it's a family office-type structure where our founder was a really successful gentleman. And so we managed his money. And so there are several different strategies that we used. Me, personally, I ran six different strategies from algorithms to discretionary strategy, short-term to all the way to a multi-week period. It was very short-term trading the nature where we were trying to return 15 to 20% a month.

Not just like a passive investing strategy. One thing that was so incredible about gumming out of school in your 20s and then really learning how to manage risk. I mean, if you want a dose in humility, it's losing thousands of dollars, when you're out of school. You know, 23, 24, 25. There would be some days where we lose 20 or 30k and you know, walking home you're thinking, "Wow, it really makes you appreciate risk and money." And that's really what's transitioned also and so you know, cloud capital and then how we approach risk too. I remember there was one time that, one day, market closed, went to the restroom, came back, and I was down over six figures.

That was a huge shot in the gut. That was a pretty significant loss for myself. There was a few other people that were on the wrong side of this trade but I remember, you know, trying to wiggle myself out of that trade. Got multiple six figure loss and walking back through Times Square and I remember I saw a trash can. I just couldn't hold it anymore. I threw up into the trash can in Times Square.

I was thinking, "What did I do? what lesson would I — was I learning? Was it a black swan event? Was there an error in judgment?" Earlier in my career, it just really set the stage in that foundation to have that appropriate amount of healthy respect for risk, humility, and then kind of how that transitioned into real estate was — I was having drinks with this investor banker one day from the financial district. And he starts talking about how he and his buddies were buying multi-family. And this was the first time I had heard about it, right?

You always hear about Forbes 500, they always own — 85 or 90% of them own real estate. The more we started talking, they said, "Yeah, me and my buddies, we buy 50 units, 80 units, a hundred units if we can. And these are the types of returns we're generating. That really started to spin the wheels to multi-family and three or four years later in that, did a first deal myself.

**[0:04:16.0] WS:** Nice. All right, yeah, that would — six figures coming back that quick and noticing that much. Being down that much, yeah, I'd be headed right back to the bathroom myself. That's horrible but you learned a lot. I mean, you learned a lot and you definitely learned a lot about risk and breaking those risks down and just having a better understanding, no doubt about it. I want to jump right in because you know, your super power, you mentioned before we started recording, just your team's super power is really underwriting and breaking down the risks, like you're talking about. I'd love to dive into that a little bit.

And you know, you help us think about deals, how you all think about them and understanding the risks in a very understandable manner. Even ways to express them to investors, as well. But help us get started a little bit on your process of underwriting and breaking those risks down?

**[0:05:10.5] NC:** Yeah, sure. I think that knowing how to — and there's not really a right or wrong way in how each sponsor capital raise or operator, et cetera, breaks down a deal and how they evaluate it. I think the main thing is one, they are always learning. But two, that you have a process, that you're basically going through to say "Hey, what are the characteristics of a good deal for us in our equity and our targeted returns." And then how can you repeat that process? Because just like you, we looked at 520 deals, forgot it, 520 or 540 in 2019 across six different states. We were underwriting in Texas and in Phoenix and Florida, in Georgia in the Carolinas.

There just starts to be similarities that come across in these deals that you can notice as well. And say, "Wow, there is something different about this deal." Or that "this deal underwrites — it seems too good to be true." All of a sudden have a six and a half, 17 IRR, this should probably be around 15 to 14 and a half." There's something in my assumptions that are incorrect.

Let's kind of start from the top. We get the broker a win, right? Or a broker approaches us about an off-market deal — and we can talk about all the market deals versus on-market deals for an entire podcast. There's many lines of thought. We get the broker a win, it starts from the market first, and there's nothing fancy about what we do. Everybody's doing the same exact thing with employment growth, population drivers, et cetera. Our target markets are Austin, Dallas, Atlanta, and a few secondary markets in those areas. We're looking at the same target markets that

most people are looking at that are really demanding those key demand drivers. Then we're going to jump into a sub-market, right?

Initially we're looking at median incomes, are they 40 to 45, 50? Are they lower than 30k. Our risk right there in median incomes is, let's say it's a great value add deal, but it's in a lower socioeconomic area, right? With median incomes of 33,000. We know, just inherently, even though there's a \$150 rent bump that could be achieved where brokers are promoting. Can our tenant base really afford that rent bump? The answer is probably not, right? We can probably only proforma those rents at 50% of what we think might be achievable just in order to remain conservative. Because as you know, the best deals typically underwrite in the hood.

And then we're going to go into crime rate, what's the crime rating, the place into the median income. Proximity to interstates, are we three to five minutes from the nearest highways or interstates — which, really easy to get to work. School rating, there's a lot of three bedrooms as supposed to ones. Families typically tend to migrate to these apartment buildings, right? How close are we to the grade schools?

Supply/demand in balances, right? Everybody talks about new construction but I think there's different ways to thinking about new construction. Let's say that for some market, let's say median incomes are around 38 to 42 grand. Let's say that a new development is happening a mile away from our deal, right? By a really top-tier developer in the city. We're not going to be catering to the same tenant so that gives me a lot of confidence, this area could be growing. Whereas if we're in a great sub market, 75k median incomes and there's also two new deals with two new high profile developers, I see that as risk and a really high sub-market.

That's the sub-market. Then break them down into the deal. Current owner, is he sophisticated, is he out of state, is he self-managing the deal? Who is his property manager? Do we know them, chances are, we do? If we don't, that could be an additional layer of opportunity for us to jump in. What type of debt does he have on this deal? How many times has this property traded the cycle? Has it traded twice, has it traded none or has it traded three or four times? Like most of these deals in DFW. All the value-add get sucked out of these deals and it's basically being traded to the same guru group over and over again.

We just don't have a big competitive advantage in that. That's just high-level, what we're thinking about before we even model the deal out.

**[0:09:24.3] WS:** Nice, no that's awesome, you just laid out so many things there that I know that — it's great reminders, great hearing those things again. You know, what's a good place you're finding a lot of these data and information that's helping you analyze, say, the market or sub-market and things like that?

**[0:09:42.1] NC:** I have a folder, it's basically called underwriting and then there we have five or six different websites that have to do with crime. We have Google maps, what we do is I pay a VA to essentially go in there and outline every single sub-market along with median incomes to growth ridge, et cetera. I'm just full of Google maps and there's like a custom feature where you can have different layers. We're layering in median incomes, crime, new developments, half the progress is Chick-fil-As, Starbucks, Home Depots, Lowe's et cetera.

You can find all this information for free, essentially but we just, I guess take it a different step and different direction and then layer all that data into Google maps. And then we just follow the CoStar, Real Capital Analytics, and then Yardi. But those are a bit more costly.

**[0:10:28.3] WS:** That path of progress or growth like you're talking about, is there a place where you find that like where the Chick-fil-As are coming in and things like that?

**[0:10:35.4] NC:** What you can do is you can actually go in your Google Map and in my layer, it's called 'path of progress', and you can just search our VAs, search for Chick-fil-As that automatically, they all pop up. Starbucks, they all pop up, et cetera. Whatever you want to look for. We typically like to stay away from dollar generals.

**[0:10:55.1] WS:** That's funny. Is there a specific underwriting model or template that you like to use or did you build your own?

**[0:11:04.7] NC:** This is in my opinion, we have an analyst that sits in Chicago, talking to a lot of sponsors, this is the most underutilized and under-discussed, I think, you know, topic in all multi-family, right? We all know, it's a great asset class. It has tax advantages, depreciation, et cetera.

We know that high-level, it is a good asset class. But, what really happens when we start to dig down into the details and into the numbers, it's all about how you model the deal out.

Because every OM, okay. If we're going to sit down a deal like we did, we're going to have more or less the same target returns. Close to 15 IRR, up or down. Around a seven and a half to eight and a half cash-on-cash and then somewhere around like a 175 to 19 [inaudible]. That's just where the market's trading. But, as a passive investor and as another sponsor that's thinking about co-GP-ing with another group, do I trust the sponsor? — One. Do I know them? Do they have a good track record? But two, what type of model they use?

Are they outsourcing this to some 23 or 24 year olds that work at rate? Or somebody they met on UpWork? Or do they actually go through at a grueling thousand-hour process of creating their own proprietary models? I told you, that's a really long-winded answer but it's something I'm really passionate about. We use our own proprietary models and it helped — the background, in the building models and building algorithms. But it's still hard to learn real estate and how specifically revenue streams and revenue streams out. And how to really go through the art of a deal and underwriting it with correct assumptions.

So we use our own proprietary model, also, we'll send it out to anybody, I think it's a shortcut when you go in and you buy somebody's. But also, just not grounded in reality. Typically, if you're going to go and buy a deal with fancy highlights and inputs. The realities of that deal are going to be far different than what those numbers are actually projecting. But we can talk about that for an hour.

**[0:13:01.6] WS:** Right, well, I'd love to know how you just went underwriting, how you're prepared for a potential downturn or something like COVID and all that, you know, how you all prepared for this. And what does that look like in your underwriting model? And also so, you know, as a limited partner or somebody that's listening, when they're looking at these models, of course, you get these from so many different operators, you know, and you see so many different models.

What are those key things that you do so you're prepared for that kind of downturn and things we can be looking for?

**[0:13:33.8] NC:** So, how were we prepared for it? We weren't, you know? A lot like everybody else, but just like any type of investment, you can go in with a very conservative assumption. And I know that a lot of listeners laughed at me saying that our underwriting is conservative. But, there are certain things that you can adjust for, you can always underwrite your deals too. I just wrote an article on LinkedIn a few days ago actually about our underwriting and how it changed in COVID.

But a few of the really big things that we're underwriting to change-wise is, so vacancy, we typically underwrite to a 7%, especially in the first year or two. We might blend that up to 6%. But typically we're remaining constant at 7%, no matter if our subject properties at 95, 96% occupied. They can see, it went from seven to around 10%. nine and 10% in year one and then we'll blend that back to 7% of your three or four. COVID's going to be a pretty big issue for the next year. Maybe 18 months but after a vaccine or something of that nature, "This too will pass." Vacancy, we increased our assumptions, year one, rent growth, we have zero percent and then year two, we're back at 1.5. And then we blend it out at two. We're never going to underwrite a deal at 3% rent growth for perpetuity. That can really skew the numbers.

Also, our delinquencies are going to go up to around .5, .8 — about one and a half percent that first year, then it trails off to 1% and then about .5 to .8 — in line with pre-COVID assumptions. But the biggest thing is our terminal exit rate. I mean a lot of sponsors are talking about they're increasing in their terminal exit. I don't think that necessarily would be prudent. If we are going to exit this deal, in five to seven years, COVID is not going to be an issue. And we do have a 50 to 70 basis points increase but it is not going to be a factor in five or seven years as COVID was.

**[0:15:27.2] WS:** Talk about the rent growth again a little bit. You said you will start with zero percent. That is because of COVID, I assume or you probably were modeling that before COVID? Or is that something that's now we see, "Okay, we shouldn't expect any rent growth over the next year so that is the way we are modeling now."

**[0:15:43.6] NC:** Pre-COVID we were underwriting to about either a zero or 1% rent growth but also we are doing value add deals. So we are bumping rents from a dollar square foot to a

dollar 15 a square foot in the next 16 to 18 months. So there is a huge rent increase bump in that but we'll sometimes increase our rents one percent with, in place rents, you know anticipating leases that are never going to get renewed.

Post-COVID, right now, where underwriting to zero percent rent growth. And then also, if we thought we were going to achieve a \$100 rent bump, we are going to go to \$70, \$65 just to remain conservative. Because one thing we don't want to do is compound error in the first year or two upon stabilization because if you get income wrong in the first 16 to 18 months of your model, it just compounds that error until you sell.

**[0:16:37.1] WS:** Yes, some big issues there, right? Or you start from the very beginning in the whole. So what about reserves? What kind of reserves do ya'll like to have in place?

**[0:16:48.4] NC:** So to begin, one with what the lender is asking us, or telling us, I guess we should say. What we need to require. And then two, what we call comfortable with. So we have been underwriting to 300. We have been underwriting about a year and a half below 250 and now we are just underwriting 300 for reserves.

**[0:17:04.3] WS:** So when you say 300, like 300 per door?

**[0:17:07.1] NC:** Correct.

**[0:17:07.9] WS:** Yeah, okay and then is that anything separate from what the lender might require, just like an emergency fund or anything like that?

**[0:17:16.7] NC:** So now as you are aware it's changed on the lenders end with what they are requiring. You know in April and in March — and then it is really difficult to do a deal because the lenders and the agencies — even though they stayed high on their percentage change. And that leverage at 75% they still said, "Well you are going to have to have 12 months and if the loan is six million and below 18 months." So 12 months of PNI reserves, interest, and taxes, which made it extremely difficult to deal.



And that's why you didn't see hardly any deals at the market for about two to two and a half month period. And so they just came out and said we're just going to require that 12 months in some cases nine of just PNI and so we don't have to raise that additional 50% of equity that is going to retire. Even though it drops off right after you achieve like a 125 or a 135 DSCR per year, even though it drops off and you can turn that capital back. I mean, it just makes it a whole heck of a lot different and difficult to raise. You know an additional 15 or 20% of equity in your passives.

**[0:18:16.6] WS:** Yeah, okay so you know in your underwriting process, what are a couple other risks that you might see and even in reviewing other people's deals? Or things like that that you know is a red flag?

**[0:18:31.4] NC:** Red flags and then a few errors that I see are kind of different questions, I think. But let us just start from the rent roll. So, one, I don't know if I have necessarily trust the performa and the rents that are on the OM that a broker is receiving. You can either enter that into your model or you can have, like, a formulaic-equation, just like a redIQ where — or there are two or three other softwares that do it. So in our model we have a specific tab just devoted to the rent roll.

And so we input the rent roll that it automatically sets out every single floor plan. All the effective rents, concessions, et cetera. and it breaks everything down categorically. So I can look and see exactly what is in the rent roll for the last month. And there might be a variation with what the OM is showing or what we have been represented by the broker or anyone else. And as you know, income drives these returns. We can manage our expenses but incomes is what drives these returns.

So it is going to be a huge differentiator, if my effective in place rents are let's say 92 cents as opposed to 94 and 95 cents with what different material is supporting. So getting that actual correct rent in the rent roll is extremely important. Across the T12, 10 or 50% of the deals — and you need to go and check their math with the additions and subtraction. The NOIs are incorrect or the expenses are overstated.

So what we do is we have another model or another tab that is usually in the model. And we throw in the T12 and then I put every single line item with the formula to my specific chart of accounts. And then I also have an error check. So I can check their income, I can check their expenses, and check their NOI. And again 10 or 15% of the time there is going to be a variant to that and so that is going to be a question for the broker.

**[0:20:18.6] WS:** Wow, so I want to change gears just a little bit because you mentioned, I know in your bio, you said like your newsletter is read by over a thousand investors every month. And there are probably a lot of listeners that dream of having a list of that many investors, right? So I would love for you to highlight a little bit on your steps to gaining an investor list of that size. And that is a whole other conversation. We can probably do a whole show just on that and that would be great.

But maybe you can highlight just a few things. Because I know that probably caught a lot of their attention, it did mine. And I would love for you just elaborate a little bit on that.

**[0:20:53.4] NC:** First of all, we are a very small firm and I think you're overstating us. One, you've done a lot more deals than I have. You have a wider investor base and there is a lot of difference in people that actually subscribe or read your newsletter as opposed to people who actually invest in your deal as you know. It is completely different.

So a few of the steps that we took to really grow that base out is utilize some virtual assistants. And what they will do is they will go into — they'll use LinkedIn sales navigator. And a lot of people are doing this exactly. We are not doing anything revolutionary at all, right? We are going in, we are trying to target our investor avatar of somewhat accredited investors, connecting with them across LinkedIn. Don't sell anything, you know, don't pitch anything — that typically doesn't. But we track data and stats and all of that stuff. I think Google sheets.

You just connect with them and overtime, when you are putting out content on LinkedIn, et cetera, Maybe shoot them an email that's not salesy at all. They know about multi-family for the most part right? And this has really blown up in the last five years or so, everybody has become a syndicator. Actually search in LinkedIn for people with syndicator in the title and it was like, 9,000. So you know they are getting inundated with this information. So don't sell. You let the

brand come speak for itself and the articles that you publish in your website, your team, et cetera.

And then slowly but surely, we have been doing this for over a year. So you know a thousand seems like a lot but one those aren't actual investors. Not everybody is going to invest in the deal, even if they want to — it might not be a good fit for mine. But we have been hammering this out for over a year to grow that base. So it is really — I guess probably not that impressive considered it has taken us over a year.

**[0:22:40.0] WS:** Well that is pretty impressive. I mean I know there are listeners, like I said, who are dreaming of having a list that size. And I guess, you know tell, me a little about that process before we have to move to a few final questions. So you use LinkedIn Sales Navigator, that is probably something a lot of listeners haven't heard of before. I have briefly heard of it but I have never used it personally. And so what does that do for you and then what is that follow up process a little bit, you know with somebody that you connect with through LinkedIn?

**[0:23:07.6] NC:** So you go to LinkedIn Sales Navigator, you can build lists with the navigator, search for certain titles, et cetera. And then you can connect with these individuals. So that is the first step of the funnel, right? And so you need to connect with them and, two, you might wait a week or two weeks or three weeks, et cetera. — and then you might shoot them a brief follow-up email. And then if there is interest to say, "Look Whitney, would love to jump on a quick call with you or engage with some of your content."

"Let me look at the investor presentation, let me cruise through the website, read a few articles, yeah I am interested and may sign up in the newsletter." But that process takes two months. Two to three months in fact. The first time you connect, they might sign up for the newsletter but again, I mean, we are extremely active.

I mean, everything is about the process and how you deconstruct the deal. Growing your investor list, it is a process too and it is daily. And then every day at 7 AM, we're working on this until 8:30 in the morning. Trying to grow this list and really get our message out. So it's amazing, it doesn't come overtime. I created a system, yeah. I mean this just like anything I wish it was easier, right? I wish getting the deal was easier, you know? I wish all of market deals came to

me more than they do. I wish we had more assets under management but it is just a process and it takes time.

**[0:24:22.1] WS:** If it was easy everyone would do it. So you reach out to those people. Is that something that, say, virtual assistants can handle quite a bit for you?

**[0:24:30.7] NC:** Yes and no. So one, I think they are great at data entry. Just like everything, it takes time to find a really good team and to find a really good VA. So I think they are incredible at the data entry aspect. In terms of the messaging et cetera., and then customizing it, it is just better coming from you. Again, it is just every single day for an hour and a half to two hours, you know I am having calls, discussions, emails, LinkedIn messages et cetera. But I am not selling, you know?

I mean, you just can't sell and especially if you're asking someone for 50 or a 100K they can make that judgment on their own.

**[0:25:05.6] WS:** Right, so what's a way you have improved your business recently that we could apply to ours?

**[0:25:10.6] NC:** One thing that we did about a month a half ago, which was honestly way too late. I wished I had watched your show and somebody would have pointed this out but an investor portal. An investor portal, I think is, absolutely crucial in your business. Just an ease of use is streamline, et cetera., so you don't have to have a million Google docs formulas or folders, right? So adding in an investor's platform or portal was actually a great step for the business.

**[0:25:36.6] WS:** What is your best source for meeting new investors right now?

**[0:25:39.3] NC:** It would honestly be LinkedIn and also my marketing guy is really good. His name is Trevor, you should look him up. He's been incredible in this process. You know I am not a marketing guy, I do spreadsheets and finance. I am not marketing at all. It's a huge weakness but he is really good at that and so he's crafted some documents at the current for the brand that are pretty world class with what the budget that we had so far to work with.

And so he has been an instrumental part of the team and then we're also connected with foreign investors and Trevor has built this funnel that connects with foreign investors and then drips them back towards.

**[0:26:16.2] WS:** Wow, nice. So what is the number one thing that's contributed to your success?

**[0:26:20.3] NC:** One, I don't know if I can get to cold call capitals success yet. We have only done one deal. We want to be in this game for a long time. I think transparency with our investors is starting to actually build up that investor list and saying, "Look these are the returns that we could promise but this is actually how the market is trading" and we get the question all the time, "Well this guy is saying these returns over here." Well, you know, who would you probably have a little more trust in?

Somebody had promised a 30% premium or somebody that's coming in and say, "Hey this is where the market is trading, this is how we are going to preserve your capital" et cetera. So probably transparency to really resonate with the investors but we are a long way, if you can call it, from our success.

**[0:27:05.2] WS:** And how do you like to give back?

**[0:27:06.8] NC:** Honestly, I have not done a good job at that at all, right? I mean that is one of the things that we talked about a year ago when we are trying to really formulate our mission statement and how we are going to give back. We haven't done a good job about that so far at all. You are blowing it out of the water with your calls on the backend.

**[0:27:27.4] WS:** Well, you'll get there, no doubt about it. And I am grateful for your time today Nathan, grateful for you just being willing to share your expertise and really walking through some underwriting stuff that we need to have in front of our minds or on the forefront when we are going through deal analysis and just understanding risk and even sharing your story about life. That is important to you now from some stuff you learned very early on.

But, no doubt. So important, grateful for your time, a pleasure to meet you. Tell the listeners how they can get in touch with you and learn more about you?

**[0:28:00.5] NC:** So the website is [cloudcapitalllc.com](http://cloudcapitalllc.com) and then the email is [nathan@cloudcapitalllc.com](mailto:nathan@cloudcapitalllc.com) and so feel free to visit the website and give me a quick call. I am always happy to jump on a 10 or 15 minute call with investors or just talk about the state of the real estate market. And Whitney, thank you so much for having me on. I really do appreciate it. You have done a lot of big things with this show and I think you are just getting started.

[END OF INTERVIEW]

**[0:28:26.5] 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]

**[0:29:07.0] ANNOUNCER:** Thank you for listening to the Real Estate Syndication Show, brought to you by Life Bridge Capital. Life Bridge Capital works with investors nationwide to invest in real estate while also donating 50% of its profits to assist parents who are committing to adoption. Life Bridge Capital, making a difference one investor and one child at a time. Connect online at [www.LifeBridgeCapital.com](http://www.LifeBridgeCapital.com) for free material and videos to further your success.

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