EPISODE 781

[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 Kevin Riordan, thanks for being on the show Kevin.

[0:00:32.0] KR: Thanks Whitney, thanks for having me.

[0:00:35.1] WS: Kevin has worked for over 30 years in the commercial real estate industry, he has focused on making investments via mortgages, mezzanine debts, CMBS and both at large pension plan, TIAA and as well as a commercial mortgage reads, he took public in 2009 called is it CreXus Investment Corp?

[0:00:53.4] KR: That's right, CreXus Investment Corp. Right.

[0:00:56.1] WS: He currently serves on the facility at Montclair State University teaching a variety of real estate finance courses. Kevin, you're a great guest for our show and pleasure to have you on the show. Just bringing your level of experience and expertise to our listeners. Give us a little more about who you are and what you do exactly in the space and let's dive in.

[0:01:15.5] KR: Sure. Thanks Whitney again for having me on. My background from an education perspective is on accounting finance person. I did the route which at the time was a big eight route, now it's a big four route but did the CPA worked and then got an opportunity to work at a real estate developer in syndications in the early 80s which was kind of a dual different game back then, it was much more of a tax game. It got to work in that environment and I started actually working on putting some transactions together, creating the structures and the forecast and what not.

I really liked it but my role is going to be rather more limited to the accounting side and I enjoy the investment side. I made the move to get over to TIA in 86 and it was a great run over there and I worked form, I always tell students because they like to say hey, professor Riordan, what did you do and I kind of like to give a little like okay, here's what it works.

I had an office in New Jersey at the real estate company. But I thought the opportunity was so good in New York City to work for TIA that I took a job as an assistant investment analyst, sitting in a cubicle. You give up your law office, give up the privacy between the cubicles and that turned out to be great. Over 20 years, I rose to the level of senior managing director.

I ran a book of about 80 billion dollars of commercial real estate investments as well as residential mortgage investment. It was a very good run and then things changed, obviously, this is always senior management and then I was fortunate to land on a company that was well capitalized but they weren't in the commercial space and they wanted to get the commercial space.

They hired me to create that platform. Interestingly, I thought we would do it through a private fund initiative and when it has turned and said no, we're going to do it public. Okay, president seal of a public company, I was like no, that doesn't happen every day and the road show, we raised initially about 300 million equity, I did ring the bell at the exchange, we did a follow on, we had about a billion dollar company and it was making Whitney, those investments that you described earlier, mortgages, CNBS, mezzanine and so it's really a – it was kind of a bank within a wrapper of a writ.

That's the way I like to think of it. Bank within a wrapper of a writ. We did that and eventually, the company got acquired and I pursued this new career in education, besides being on the faculty and maker state university I also teach at Columbia University, I teach real estate finance in the Graduate School of Engineering.

Kind of hopefully, it's not too winded.

[0:03:56.5] WS: No, that's awesome, I appreciate you just diving in there a little bit, just to share what you've done. It's incredible. Background and taking it public as well. Not everyone gets to do something like that, you know? But you know, I think you can really help us though, just thinking about what lenders think when lending money, right? And we can get to some maybe some steps or traps that you know, that can help us improve that process but just you know, even as you know, a lot of listeners are up and coming sponsors, right?

Just learning how to walk that walk, right? To get to the institution al level. Why don't you get us started a little bit about just what lenders think when lending money and help us to just understand that better.

[0:04:38.3] KR: Great. When we use the word lender, it sounds like such a generic term. Okay, we lend money for the real estate asset and we get paid back, it's so generic. But really, there are so many different slices of lending and it's a function first of all, the kind of property that the sponsors bringing forward for financing, that's one element and then the other side too is then the lender itself is what type of an institution is it?

How is it capitalized, how is it regulated, how is it not regulated? Historically, you had three places or two places go to for money. You had four on the short-term side, you had the banks and commercial banks savings banks, right? From the short-term side. That's where I kind of started getting my chops and then I worked for a pension fund which was long term money.

Those were the primary places to get money, short term banks, long term, life company. That began to evolve over time primarily because as the market blew up in the early 90s, CMBS need a foothold, Wall Street got a foothold and alternative means of financing, using leverage, using the capital markets became a foothold.

Now, Whitney, you have a bunch of different type of lenders, you know? You still have traditional banks, you have life companies and now you have all alternative lenders in between. You as a sponsor coming forward and saying, where do I go? Which one do I go to and obviously, it's a function of price, that's going to always determine how much you want to pay but really, the thing is going to be from the sponsorship side is what kind of asset am I bringing forward for financing?

Is this a deep transitional redevelopment play that is going to require some patience by a lender, some real deep underwriting, some hands on work back and forth possibly between future funding's and so forth, a lot of touch and feel. That kind of situation may not be proponent to a life company nor may be for bank.

It might be good for an alternative lender in between, okay? Likewise, you may be in a position where I've got a – you're thinking of your investors too, return profile do we what to have for them, I've got an asset, now I want to get permanently financed so I might go to a bank or might go CMBS, might to go lenders. This whole different reason why you would pick one or the other, right? This whole different reason why you would pick one or the other, right?

Let's say you do pick the CMBS route, let's say you pick the CMBS route because the pricing is so good, capital markets are so favorable, pricing is good, let's put servicing aside for the issue because that's a big Achilles heel in CMBS but want to go CMBS and they'll do a financing. CMBS will be much more obliging to you if you want to get some additional financing through a mezzanine lender so that you can give more return of equity to your partners.

It's a much more favorable environment to do that kind of transaction. On the other hand, you may want to have that relationship with someone like me at a life company and you know you can call me or something's not working right and you call me like walk it down the hall, and say hey, and say hey, I just got a call from so and so. Maybe just want to put it on the shelf, lock it up in the life company's a better place to be.

It's a kind of between, it goes back and forth, where's the appropriate place and then what's the asset you have and then finally, of course, what kind of financing do you want to retain. CMBS is boxed in a bit by the rating agencies in terms of what kind of assets they allow to have in the pool. Life companies can be a lot more liberal, although they could be a lot more, used to be an old commercial like Mars to cat, finicky, very finicky cat.

Life companies can be very finicky, they can be like, we're not going to do any of this for the next year and you may have the greatest asset in the world, right? It may be a homerun but the fact is, they may just have too much of that kind of asset and they're not going to do it.

You may look good, your asset may look good, your performance looks good but they just have too much of it because they're limited by portfolio concentrations, that's regulatory oversight, that's rating agency oversight, there's a lot of other things that affect lenders that you don't see but they should be able to give you direct responses as to I can't do it because of this. I can't do it because of that, okay? Not just like I'm not interested.

[0:09:20.8] WS: You know, it's interesting, you call it a life company. Could you just talk about the difference, I know you just did, you went through the differences and those little bit like CMBS and life companies. I don't know that I've ever heard it called like a life company before.

Could you just elaborate on that a little bit because I bet that's you know, something different from us listeners as well.

[0:09:37.8] KR: Okay sure, life, when I'm talking about life companies, I am talking to a place like TIA, even though it is a pension fund is regulated, it's a real-life company. Its counterpart is in the business are prudential, are met life, principle financial out in doing. Those are all life companies and you know, I had relationships with all those companies, pack life out in California.

I still know the guys who run those groups and some of those companies and a life company will do more long term financing. Why? Because their liability side is long. They can do longer assets, remember, the mortgage of your lending you is an asset to the life company so they want to get a return over a long period of time.

Then liability structures are longer so therefore they can give you long money when I say long money, minimum five years and then go out 10 years. That's what a life company is, they are not the – they do opportunity things to do buckets of transitional, construction stuff but that's not their bread and butter. Their bread and butter is more long term, put it on the shelf, get paid, you keep paying and hopefully everything works, that's life company world.

They're regulated by the NAIC, National Association of Insurance Commissioners and they have a lot of – they deal with statutory accounting, not gap accounts, there's a lot of different things with behind the scenes and life company but that's basically their long term fixed rate money, that's where they are. Commercial mortgage back securities, the wall street vehicle, looks like a life company, it's long term, fixed rate financing, it looks like that and it is that, it is that to a borrower but the difference between a life company and CMBS is the servicing aspect.

Wall street will make the loan but then sell it and then you're sold into a place where now it you have a servicing issue Whitney and this like I said is the Achilles heel, it's sometimes hard to get an answer. It's hard for people to make decisions because there's a whole big legality around the trust and so forth. That's the CMBS and then the bank side is also, the banks are actually very interesting right now, banks traditionally were short term, floating rate money, construction money, transitional money, that kind of stuff.

That pocket of opportunity has moved to what I call “alternative lenders” now and they have popped up all over the place, they are through basically private equity firms, you know, KKR, Starwood, you know, ladder capital, all of these are alternative lenders doing some long term stuff that looks like CMBS and will do CMBS but they’ll also look like short term transitional guys. They’ve been a very interesting thing and I ran a panel about a year and a half ago and I had three guys who I knew pretty well, talking about the amount of business they were doing as construction lenders.

They were doing a lot less and from the regulatory environment, that looked good because there’s less construction lending so that means there’s less risk or if you looked around there are a lot of cranes going on. What was happening is the alternative lenders were picking up this risk and that’s sometimes you hear it out there Whitney, about whether there is a larger bubble of lending going on that is not under the microscope of the FED or the FDIC because those are non-regulated entities.

Most of my private equity, some go public so they are writ but they’re not regulated by the NAIC, the FDIC, the FED or anybody, there is this large group of other lenders that are kind of, maybe a little scary at times, we’ll see now given COVID what’s happening, we’ll see who is, I think Warren Buffet says, when the tide goes out, we see who is wearing clothes. Goes out, we see who is wearing clothes.

[0:13:49.6] WS: I like that, I appreciate you diving into that, Kevin and just giving us a great explanation. You know, let’s talk a little about how institutional investors just view up and coming sponsors?

[0:14:00.5] KR: Sure, that’s the other side to it and again, you have a – you want to go get financing or let’s say you even want to get equity, you want to get partnership money or something like that. This is – it’s a biography that you're creating for yourself, it’s a resume and I mean, it would be great if you have a lot of money that you’re coming from.

That would be great, I could walk in and I've got partners and money and that's good, right? Let's say it's like myself and maybe it's not working like that, okay? The way it's going to work is to attract record and it's going to have advances in what you're doing inside and not only the scope of the properties but also the size of the properties, okay? What you're going to try to develop is and what's really important as I remember meeting young developers back in the late 80s, early 90s, trying to gather business for TIA, they would talk about how they created their accounting systems, how they create a reporting systems, how they monitor their construction, how they did their credit analysis of the tenants they were putting in the buildings, okay? All of this was detailed check list and so, that's what you're going to be bringing if you're a newer person, because you're not going to have, Park Avenue, right? You don't have that, you've got hopefully, way workout with some friends and family, maybe you can buy a 20 unit multi-family to start and then you create some value and then you create capital out of that value and then you do a 60 unit, right?

And then you get to 120 unit. We start getting in north of a hundred, that starts getting interest of certain lenders, it's just sizing, right? There's a lot of things to look at and time is valuable and it takes time to do these, to get these transactions consummated.

So where would they rather spend the time? You might be the greatest guy in the world when you're 16 in the department. I mean they might love you but if that's only $4 million and they can do $20 million over here, well they're probably going to put their attention to the 20 with all things being equal just because of sizing. So again, from a new person standpoint you are building a track record and you're talking language of accountability in the systems you have.

From a portfolio perspective, from a tenant perspective, from accounting perspective that gives you credibility.

[0:16:36.2] WS: Wow, you are talking that language. Just when you are speaking with the lenders, they can understand your knowledge and then your scope, right? Like you were talking about earlier.

[0:16:44.2] KR: Yeah, as soon as start talking like them because they are faced with the same thing, right? Internally they are faced with that. You know how are they performing? How do they monitor? How do they deal with problems, right? So that is all their world, so you are talking their language a little bit. I mean it is obviously specific to what you are doing but that is the language they understand is process, they totally understand process.

They understand checks, they don't like authoritarianism. Now, a lot of places are entrepreneurial than some individual but they do like to have expertise around that so that the decisions are made not in a vacuum or made by a single person but there is a collective view as far but that is the outcome for whatever the situation is.

[0:17:35.1] WS: Wow, no that's awesome Kevin and I wanted to just spend a couple of minutes too on just helping the listener just improve that process of getting financing, maybe some traps or some steps that they need to be aware of while we just have a few minutes before we have to jump to a few final questions.

[0:17:50.9] KR: Sure, absolutely. So a trap bad credit in your background or you as a bad person is a trap, okay? That's the simple one. You may be the best developer, you may be a great landlord in some respects but if you have issues around bad publicity, bad headlines, people are not going to go there. That's just not worth it to them to defend the character or actions of some sponsor. So you know the first thing is you know, do your business above board, right?

Do your business above board. Number two, be transparent. Now, things can go wrong at a property, right? I am just talking from a business perspective I am not speaking anything else. This goes more business perspective, loss a tenant or there was a calamity at the property some kind of natural disaster, something like that and that causes headlines, right? So what I would say to the sponsor be upfront, the problem is identified, the steps were taken and the risks were mitigated and what was the outcome.

So that gives someone comfort that if there is a situation, remember they don't want to be in your business Whitney, they really don't. They really want to give you money and get a coupon, they want to get paid monthly and get paid back. That's the fix they want, okay? So you demonstrate the ability to manage through process, to manage through problems with thought they will respect that. So be a good guy, this sounds funny but I think you know what I am saying about that.

But being a problem mediator and fixer is important and to demonstrate that track record of how you did that.

[0:19:43.4] WS: Yeah, do your business above board, all right? Do what you say you're going to do, be transparent, all of those things you mentioned it says a lot no matter what business you're in, right?

[0:19:52.3] KR: And you just said it, say what you are going to do. So for example, if you said, "Hey, we are going to take this site, we are going to do this, we are going to do that and that" and it comes out well, none of that happened, right? That's not going to be good on your reputation and I'll tell you, I will say this, lenders talk. They go to conferences together, they'd swap – I wouldn't say they swap notes but they swap something about deals and sometimes they know that someone did a deal.

They go, "Wow, why did you do that for? I passed on that" I'm like, "Where do you see that?" and you know they'll have some reason or stuff like that but only in good nature but of course, you know they do compare notes, you know? And it's no, it starts getting no when borrowers start shopping their deal around like, "Oh 14 people said no to this piece of crap," or whatever, you know? And now, you are at my door and people know that. So there is a little, like anything, right Whitney? There is a little close circle of people.

[0:20:55.5] WS: Kevin, how do you prepare for a downturn?

[0:20:58.8] KR: So the first thing you do is you try to horde as much cash as you can. That is the first thing you do, so how do you do that? You probably postpone some capital improvements that has the least immediate effect on tenants unless of course you have to replace an HVAC unit and they have no HVAC and you live someplace that is very hot, you know what I'm saying. So that's the first thing, we postpone a capital improvement.

The second thing is you probably and this is really important is if you have bodies in the building, however you want to call them, tenants, bodies, you want to keep your bodies. So how do you do that? You've got to get close to your tenants that goes back to one of the things I said earlier, how do you know about how your tenants are? What is your credit work on your tenants? Why that part is important? I know who they are.

I know who makes the decisions, I know their financial wear with all. So you get close to your tenants, you understand their problems, okay? You try to work with them but the most important thing Whitney is to keep them there, okay? Maybe forbearance if you have to go that way with them but maybe you believe in them and some way you can recapture it later but a dark building is not worth as much as having buildings with people in the building, okay? So horde your cash, postpone capital improvements, get close to your tenants.

[0:22:28.4] WS: Great answer. What do you see happening in the next six to 12 months in the real estate market?

[0:22:33.4] KR: By property type, I really question the long term, I question CBD office quite a bit. I know that they want people to get back to that but anecdotally, I see so many folks that just like, "Hey, if I can just keep doing this, what you and I are doing and I don't have to go travelling and I don't have to go commuting, well that's great for me." So that is not a good prognosis on CBD office nor is that a good prognosis on all the insularly retail that supports it around the buildings.

I worked in New York City for 30 years, right? So I know, you know you stepped on something, the street there and it's all retail, right? It's all, you know, a lot of food places, some shopping.

So that has that secondary bad effect. So I am a little concerned about what we are doing right now to have a larger impact on the CBD office. I think apartments, I still hear people wanted to move into the city. I am a little surprise of that because more of it only because of pricing.

That’s really what it is not if you have a kid or young child, that group has been exiting quicker and it’s been creating some bubbles around health surprises. We have it in Montclair there. I am only 12 miles from New York City by the way. I am 12 miles west of New York City and there’s been a bit of a bubble here in the resi pricing. So that’s another thing and then the final thing is I can’t get my head around retail, big shopping malls. That is really problematic.

I mean the whole department, the whole thing about anchors, right? It is an anchor in the negative sense today. It drags you down, it creates a big, you know Gordon Taylor, JC Penny, right? I mean Gordon Taylor is going out of business. JC Penny is BK, I mean Sears, those are big empty boxes, right? And what do you do with those now? You’re not going to put a movie theater in because we can’t go there. You can’t go to a food court unless we are 25 feet from each other.

You can’t do that so the people who are going to be super creative around that will be – I mean I think those people will make money but I don’t have that vision right now. I just don’t.

[0:25:05.2] WS: Well you know Kevin, I believe anyone that’s successful in business and just in this space has a high level of self-discipline. How did you gain such a high level of self-discipline?

[0:25:13.9] KR: Oh wow. I didn’t go way to school, I lived at home. We didn’t have much money, so I went to college living at home and I’ve always kind of sometimes fall back on that. I just feel like I wanted to do better and it’s funny, when I was thinking about this the other day, you know my background like I said, I lived at home and then I got mays like I lived and grew up in Jersey City, it wasn’t the best of neighborhoods but my parents sent me to a decent high school.

And college worked out okay even though I lived at home but it was just like, I just want to do better. I just want to do better and I tell the students all the time, it is not going to fall on your lap, you know? You got to pick up a pen, I mean I use that, you know, they pick up the phones and whatnot but you know what I mean? You got to work at it and something so basic like working at your resume, working at your skills, you just got to work at those.

And I still Whitney today, I teach and I learn something every day still at school even teaching the kids. So that's another thing, I think you can't get too complacent around that.

[0:26:24.6] WS: What about some daily habits that you are very disciplined about that have helped you achieve success?

[0:26:29.9] KR: I work out. It keeps even this and I read the papers. I read the papers a lot and I really, really watch like some, maybe a syndicated TV like Stranger Things or something like that but I don't watch any of that kind. My kids and my wife will talk about all of these people like, "Who? I have no idea what you are talking about" you know? So I think it's just kind of where I spend my time and I like reading history. I like reading history books.

I like to get challenged in reading, you know somebody can really write and I would say to your readers, if you want to read stuff that is challenging, read the original writings of Alexander Hamilton. Read those writings, okay? Read his report on manufacturers, read his report to congress on credit of the treasury, okay? And think about it, his writings report at night under a flame, drinking a lot of wine but he's still writing it in long hand and you read this thing and then just sit back and think about who that is that wrote that.

[0:27:38.8] WS: That is some really neat advice right there. I'll have to pull that out, that's so neat to think through that and who that person is writing that at that time. Number one thing that's contributed to your success?

[0:27:50.3] KR: I hate to say luck but anticipating, anticipation, right? So I recognize in '85 that the syndication business as structured back then is going to change and they want to keep me in accounting. So that is going to change the whole outcome for the company and because of that, it is going to limit the outcome of the company and I made the move to go to TIA. By the way, that company was gone in three years. So anticipatory is important.

When I was at the Life Company in the early 90s I went to, I was a CPA, I went to a seminar and the person said, “Lending is going to change significantly, it is going to be in the capital markets going forward” and this was ’93. TIA was just starting to think about it and I now have to say this nicely, I really sold myself that I am the person to be doing this for you and I picked up by an individual at the company who said, “I want you to do this.”

So that was the right place, the right time but the foresight of where the business was going and that was again, so it is anticipatory and then it’s just having a plan if you can see it.

[0:29:05.1] WS: How do you like to give back?

[0:29:07.6] KR: Teaching is my giveback. I help kids, you know I mean I am through the teaching thing but they have to see me. I am call to take in 30 with the kids going to interview this afternoon and he wants to talk to me. That’s like, okay. That’s not like my job or anything, I just do that you know? So that’s how I do it.

[0:29:25.2] WS: No, that’s great Kevin. It’s been a pleasure to meet you and to have you on the show Kevin. It’s a great show and just helping us to think through some of these things how a lender thinks especially as a new sponsor. I mean I remember it is hard to know those things, right? It is hard to build those relationships and you’re brand new and you just don’t understand. There are so many things you haven’t been exposed to yet and just appreciate you bringing some of those things out today.

And helping the listeners and myself just have a better understanding of that relationship and the track record that you know being transparent and a problem solver and all of those things. Just being above board, doing what you say you’re going to do and how important that is and even I love your answer too just about what to do. You know they are preparing for a downturn and some of those things we need to be thinking about, are we prepared?

Can we do those things and perform? Kevin, how can the listeners get in touch with you and learn more about you?

[0:30:13.7] KR: So I'm at Montclair State University, which is in Montclair, New Jersey. So the easiest way is my email, which is my last name riordank@montclair.edu and we also have a public relations people up there too. So you can always find me through them.

[END OF INTERVIEW]

[0:30:38.2] 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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