EPISODE 1045

[INTRODUCTION]

[0:00:0.0] 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]

[0:00:01.6] WS: This is your Daily Real Estate Syndication Show. I'm your host, Whitney Sewell. Today our guest is Jacob Vanderslice. Jacob has some amazing experience not just in a real state in general, but in commercial real estate, he's launched a fund, a couple of funds. They have over 195 million in real eat as our focus today, really in this conversation is mostly about their self-storage Fund, why they are in self-storage and why they're doing a fund, some of the pros and cons of a fund, even some of the structure behind their fund and what they learned from their first fund doing the next fund, but an amazing guest. You're gonna learn a lot. No doubt about it. I enjoyed the show, he talked about creating the Salesforce to scale your portfolio or how it's helped them to scale, even to see self-storage industry during this economy of change things that are happening right now, but I learned a lot, I learned a lot about funds and how they've done it, and I know that you will do.

[0:01:20.6] WS: Jacob, welcome to the show. You have an amazing background, just in commercial real estate, you're a perfect guest, and so I'm looking forward to hearing about your dispersion where you all are at right now, and you're a commercial real estate business, but I wanna go back just a little bit. Tell us that, any skill sets or anything you learn, anything, maybe a previous job, anything you wanna share that helps you to move into this space or have you been in it forever

[0:01:43.5] JV: Whitney, first of all thanks for having us on today. Very gracious of you. Love the show. Excited to be here. I would say most of our expertise has been making mistakes and not so much from the wins, we've been investing full-time in real estate for 15 years, we got started doing a lot of single family residential, a lot of us kinda got started going to a joint venture with an institutional capital back in 13 and 14 on a large rental portfolio, got into commercial real estate and 13 and 14 as well, doing adaptive reuse retail, and those have been some of the more fun projects we've done, unfortunately, they're not very scalable, but basically taking an old warehouse, beautiful building, ragtime construction, converting into multi-tenant retail, we sent out the holding it for cash flow, we're selling it and then we got a self-storage in 2015, and we like the asset class because it's been really historically defensible with recessions and downturns, it's scalable as repeatable, it's predictable, and we are the platform from there, and now we own 30 sales storage dailies and nine different markets, mainly in the Midwest and Southeast, and were just real estate entrepreneurs at heart, and self-storage is been good to us.

[0:02:44.9] WS: Nice, well, let's time in there a little bit with you, is vast experience in this industry, and you mentioned even starting with like a JV, single family portfolio, some different things like that, moving up to different types of commercial real estate. Maybe before we dive into a few specific things about self-storage, why have you land it on self-storage now, are focusing on that instead of other asset classes...

[0:03:07.4] JV: Well, to begin, to answer that question, one of the many mistakes we've made over the years in real estate, both in residential and commercial, is being too transactional and the enticement of selling quickly for a good multiple is certainly there. The problem when you sell too quickly is you've got a tax problem, first of all, you've got the downtime problem on your cash, and then you've got the risk and the new investment to read employ your equity into. So we've shifted our focus more so in the last three or four years to being long-term cash flow investors, and with cash flow comes appreciation and wealth creation, and we've found self-storage to be a great vehicle for that. We like the granularity of the revenue streams within sales, stories were relying on thousands of people to pay us 50 to 200 a month, for example, we have a couple of retail tens here in Denver, and they're all in monthly payments between place, friend and Cam might be up to 20000 and they're gonna pay or they're not gonna pay, if they don't pay, it's gonna take a year to retire space, and it's gonna cost a lot of money for 10 improvement allowance and capital improving costs and sell series have that.

[0:04:13.2] JV: And the chances you're gonna have 20000 where the times blow out, but at the same time is very low, so we like that aspect of it, and mainly we're just focused on cash flow and predictable durable revenue streams, and that's been an asset class that we found creates that

[0:04:27.5] WS: I appreciate you providing just the level of detail there around just the mistakes of being too transactional, and I think earlier on in this business with many folks get in, you're thinking about that transaction, right. Often that's where you're making money early in the business, or Alesi seems that way to get started, but I love the thought of that long-term cash flow, but thinking through that really, what does that do for not only your wealth creation, but all of your investors as well, I know recently, we've had a big focus internally to structuring deals in a way where we can hold them much longer, we've had many investors reach out and say, Hey, would instead of selling this in five years, what if we just handled it right, why don't we just had this on a long-term and not knowing obviously what taxes are gonna look like five years from now, or 10, 31 change, and not knowing where those things were going... We got some options. Right. We want some options. And that makes a ton of sense to me. And so let's dive in there a little bit though, as far as self-storage, were you all doing single asset funds at one time and then you move to a fund...

[0:05:25.0] WS: A larger fund structure. Tell me about that thought process. And transition a little bit.

[0:05:29.3] JV: Yeah, we've historically done single asset syndications over the years, both within self-storage and outside of self-storage, and we launched our first self-storage fund in the middle of 19... Were relatively small fund, only 10 million in equity, 30 million in total cost, we close that fund out in August of 20, we watched her most recent fund in January, that's a 30 million capital raise for about 17 million of the way through that into this month, which is June will be at 50 million in total debt and equity deployed, and we still do single loss in sinica ions outside of our fund, but the reason we like the fund structure a little more is really two-fold. First of all, we like the geographic diversification that a multi-Property Strategy offers versus a single asset strategy, inevitably in a 10 property portfolio, two deals might be behind forecast, six were on forecast into her head. And they kind of balance each other out. And we also like the geographic diversification, so you've got a cash flow diversification and geographic diversification, and investors and us or participating in a wider asset-based, and if one deal really falter or gets behind the other deals kinda prop it up, that's why be like the fund structure.

[0:06:35.4] WS: Yes. No doubt, no. Everything you just say it, I'm like, Okay, it makes so much sense. Right, and what about the transition for say, you're investor base often, a lot of times investors say, Well, I don't know what kind of deals you're gonna be buying, or I hear that push back from a lot of people that are trying to start through our first fund or they're worried about investors instead of having that single asset syndication where they see the deal, they know the market, they know the business plan, all of those things, they can do a little more research, but now, hey, I'm just trusting the operator more than ever... Right, and I say You're trusting the operator anyway, even if it's a single asset syndication. But how do you combat that? How did you get the first Fun rolling, and how did you express that trust with your investors?

[0:07:15.1] JV: The point you made is exactly correct, it is easier to educate and make an investor feel comfortable on a specific asset they can try by is a specific location, they can see pictures of the property, it's tougher to pitch investors on a strategy... Granted, our strategy as a box, we're only buying self-storage, only buying certain types of cell storage facilities, our first fund, we've invested a Donohue for over 10 years, and lots of folks are always good for 200 grand and whatever deal that we're doing, and they kinda help seed it and get off the ground. And then once you start making acquisitions and you can report on some geometric like cash flow, occupancy growth, revenue growth, that kind of starts to snowball, and it's tougher to launch a fund, whether it's your first fund or your fifth fan without any assets and it... Yet that's been tougher to get that first equity in, but once you're half way through, people can see a store performance, they can understand what you've acquired so far, they can make sense of the strategy, and given that they can understand the deals that you've bought, it's less of a feeling of kind of being a blind pool 'cause they understand...

[0:08:15.0] JV: So yeah, I just basically see capital A couple of deals and this performance granted it wasn't very long, a matter of months or quarters, and then it just kind of stole from there.

[0:08:23.3] WS: Do you track like repeat investors in a fund versus obviously numerous single syndication on some people, we've talked about like, we're doing a fund, do you think about what an investor may put 100000 in every deal, you do it, a single asset syndication, but then you do it fund and there's a psychology behind it. Right, well, I've already put 00000 in that fund, but you may have five deals in that fund where they may have put 500000 out if you did single asset indications as opposed to one fund, how have you reached out to investors to encourage them to continue to investing in this fund, obviously, it's a lot bigger than just one asset.

[0:09:01.0] JV: The first rule of raising capital is you need to be known, liked and trusted. That's very important. And investors often... A lot of people say this, and I totally agree with it. If someone puts 10000 to a fund that maybe has a two-year capital deployment period, and that person is getting distributions, they're getting Chris communication, the sponsor is available for any questions they might wanna ask, eight out of 10 times that investor is gonna put additional equity and some folks will get one quarterly distribution, then double down, so I would say most of our investors are repeat, and the new ones that have come in, it's very likely they'll put an additional equity as time goes by.

[0:09:37.8] WS: Nice. So it's a continual communication of the find how you're moving forward, all those things. No doubt about it.

[0:09:43.9] JV: Honest and transparent communication. We have a quarterly report that we kick out, and it covers pretty much any key metric that someone who wanna know at the facility level as well as the fun level, and we report more on the data than we do on the good and play good stuff people don't really wanna hear about much, we just kind of put a green box since they were head of forecaster on forecast, and if we're behind forecast a on revenue growth or occupancy, grow their expense, maybe our OPEX was 10% higher than we underwrote any given quarter. We talk about why that happened, what we're doing to correct it, and folks like to see that, and if you're communicating all of the metrics all we get in the bed, that helps establish trust and credibility and transparency with our capital base.

[0:10:22.0] WS: How has the fund helped you to scale?

[0:10:24.4] JV: First of all, one of the parts we like about the fund in addition to the things I mentioned earlier is one set of documents, so you're not creating a new LLC, you're not creating a new PPM or offering documents every time you buy a deal, and it's one set subscription documents and one set of term, so investors come in under the same terms with the same expectations, and that really has been a great opportunity for us to be more efficient with our capital raising and our strategy and spend less time on the administrative side and more time on the real estate side and the execution side, so even though funds are a strategy versus the single asset, I think they're a little bit easier to manage and especially easier to capitalize once you've got some track record behind you.

[0:11:04.9] WS: What about... How has your, I guess, thought process behind, say, structure of the fund change after you've done one or two now, I'm not sure how many you've done after even one to... I think you learn a lot that the structure refined, any lessons learned there that you could share as far as maybe things you know what, we didn't realize this on the first fund, but we're doing this on the next one, or have done it...

[0:11:23.9] JV: So our first fund was a fairly simplistic capital structure, we had a 8% preferred return, the return on capital, and then 7030 with no beta upside, no hurdles beyond that, and we found in our prior fund that our investors really enjoyed dividend yield and distribute cash flow as you know, and a lot of your listeners probably know, prefer return accumulate whether it's paid or not, and eventually, hopefully prefer return gets paid as low as the syndication or fun generates enough net in. We strive to be able to pay for for return quarterly and pay occurrence, it doesn't accumulate along the way. So you have fun. One was a pre-7030 and our most recent fund fund to... The only difference in the capital structure was we have different share classes based on invested capital, so over a million dollars invested is 80, 20, over 500, Kansas, 75, 25 and under 50 is 70, 30 with a 100 minimum. And we layered that end incentivize folks basically to write bigger checks and get additional better economics. We also gave all of our existing investors in any of our deals and automatic bump to the next class of shares regardless of their invested capital, so if an investor came in for 100K, it was in a prior funder syndication, that person was automatically increased to the next class of shares, which is 75-25, so that's really the only difference on our next fund, which we're gonna launch next year, we're considering doing a preferred equity components, all of our equity right now is common equity and preferred equity, as you...

[0:12:47.4] JV: I'm sure you know and your listeners is kind of junior to the debt and senior to the common equity, typically gets a lower yield, but it's a safer... A piece of the capital stack, so that's one additional component you might layer in on the next round, we've had a lot of folks ask about it, we got bell to do that because it's not within our documents, so that certainly in consideration.

[0:13:04.9] WS: I appreciate you sharing just that level of detail, it's incredible. Now, listener, if you were thinking about a fund, you need to be taking all those things to heart and thinking about what Jacobs saying there from great experience, no doubt about it. But what about just from the investor's standpoint, investing in self-storage during just the economy of change...

[0:13:22.9] JV: Well, I'd like to say I'd rather be lucky than good, and we were lucky we were in self-storage in 2020 and not more scaled up in our retail line of business because we got through it, a lot of our tenants suffered, and thankfully, we kept everybody except for one person, but self-storage did great during the pandemic and it continues to, and the reds or portfolio at the end of the 21 had a record occupancy growth from 21, 0-2020 to this year. And self-storage really benefits from disruption amiss like a pandemic or a recession, whatever might happen, because people get displaced and need places to keep their stuff. It's out of sight, out of mind. Hits your credit card every month, and it's been good to us in the downturn of 2020. Obviously, we're all coming out of it right now, things are looking much better and other operators are reporting the same results, we've had great occupancy growth and great revenue growth, so we're fortunate to be in an asset class that made it through as opposed to maybe a hospitality or to a degree, office and retail, self-storage. hanging there pretty well.

[0:14:16.2] JV: Yeah, no, that's great. And you briefly mentioned like read, how does something like this compete with a read... So deal flow has been one of our big challenges in 2021, and a lot of operators that are in real estate, we have capital allocations were maybe focused on hospitality, retail, other asset classes, they got a little more beat up till I wanted to put out... And now they're in the self-storage business, so if it's a widely marketed deal by a professional broker, there's a call for offers, we can almost never compete because we're trying to blend current deal with capital appreciation at the same time, we wanna distribute cash flow, but we also want upside. A lot of folks out there are only looking for you, they wanna eliminate during the life of the deal and sell it for a break even, and that's the requirement. Others don't care about cash flow, they're banking on appreciation and cap rate compression, and we're kind of trying to achieve both, so FAS been a challenge. If it's a class, A multi-story climate-controlled deal on a primary market, we can't compete, we can't come close to the res public storage Extra Space, keep smart.

[0:15:11.4] JV: They're very aggressive right now. Most of our deals are in secondary, in tertiary markets, which are very overused words these days, 'cause we're all doing deals in those markets, but we found those markets are a good blend of capital preservation, yield and appreciation. We've also found that the reds aren't as competitive there, they're not as active in those markets, places like pencil, Florida, suburban Charlotte, suburban Memphis, Tennessee, Columbus, Ohio, Detroit, Grand Rapids markets like the mortuary, and we're not seeing as much re-competition, and so we try to fly to load their radar, and if we're going to and to with them, we can't get the deal.

[0:15:46.0] WS: It's good to just know that too, like, Hey, you're competing with and help think through what market you're in, what market there, and maybe that's interesting and maybe you could provide a little more light there too, on just like picking the right location, how are you picking those locations for the find or not?

[0:16:01.6] JV: Sale storage is very local supply-sensitive, so we track supply ratios in the 1 and 5 mile tree radius, nationally, there's about seven square feet per capsular age across the US. Once you're getting into some markets that are over 10 or 12, you start to see a decline in occupancy in revenues, and then Under 7, under 5, unless you start to see a much more volume occupancy and more boy in revenues and place rates. So we try to focus on markets with balance supply ratios, and markets with a subjective and objective low risk and the introduction of new supply, that might be Because zoning is not receptive to self-storage, the city is not resettle storage. We also try to ideals at on a low replacement costs, so if a competitor does build a facility nearby, they're asking rants need to be incrementally higher than our asking rents to achieve the sand Elon cost, but supply is really one of the big risks right now in self-storage and I think supply peak for the most part, in Q1 of 2020, there was a lot of new construction in 2019, so I never wanted supply and then beyond that, just good nuts and bolts, demographics and real estate, you don't want an oppressive tax regime, you don't wanna be in a municipality or a state that has a public lining population, you want density, you want rooftops and land, good locations, just like any other real estate deal applies for self-storage.

[0:17:16.6] WS: And one thing I'm in to ask you earlier about the funds, and you were talking about the challenge of deal flow right now, I think that's almost anyone in this business at the moment, or just the challenge of finding deals, good deals, I want something you can move forward on, but what... Operating a fund specifically, you raise all the money, you have this money, any risk of not being able to deploy it right now with just the challenge of not having good deals.

[0:17:39.4] JV: Yeah, the day that our capital raising and our deal flow is it saying is probably gonna be never, it's always too much of one and not enough of the other, and then the overnight that the pendulum shifts, we get a deal in our contract, we gotta hit the gas on capital raising. So we try to raise our capital kind of incrementally use, make acquisitions, what we're not doing is going out and raising 30 million on January 1st and having it sit in the bank and then hoping to get it deployed, and so we try to balance our capital calls with their purchases, that stuff to do, it's tough to do that. We've got investors who are about to sign documents, investors who have signed documents, maybe if you can't fund on time and in everywhere in between, and figuring out that cadence is certainly a challenge.

[0:18:16.5] WS: Yeah, no doubt about it. Well, I just think you just find more light there on, Hey, we don't raise it all up front, We're not just opening it completely day one, and I think it's very smart. So how do you communicate that with investors to say, Hey, here it's closed temporarily, or we're gonna open it back up at a specific point. How do you do that?

[0:18:34.4] JV: Well, one of the main reasons we don't get to capitalize out of the gates is we wanna turn prefer return on what an investor funds or shortly thereafter, and obviously if somebody funds the entire capital stack on day one, there's no income to pay, prefer return accumulates and that's not a good thing for them or for the fund, so we'll typically say, Okay, we're raising 6 million in equity Forex acquisition, now that capital stack is full, but our next acquisition they're after is 35, 40 days later, I get another 4 million grown then, so that's how we communicate in where folks are coming in and win.

[0:19:06.6] WS: Okay, wow.

[0:19:07.9] JV: Such great information about operating fund Jacob, very grateful for your transparency and helping us and the listeners, what about just preparing for a downturn? How do you prepare for a downturn when operating a fund like this in the current environment and with self-storage will, downturns are always the top of our minds, and I was in real estate during the financial crisis, I got beat up pretty badly. I learned so much, I would do it again. And back in 2015, we thought we were overdue for a correction, I bought a new construction, multi-family was coming out of the ground and Denver apartments for arguable getting over-supplied, and we were wrong, that correction was not coming any time soon in the pandemic hit, and we thought that was gonna be a massive correction and with the exception of a few asset classes, it is the opposite, presidential real estates on fire, there's so much equity out there chasing cash flow and yield, so in terms of preparing for the next downturn, we've done a fair amount of development, self-storage and residential and a number of other asset classes, development is great, but it's risky, and you're forecasting out revenue is two years from now, you've got hard cost risk, you've got revenue risk.

[0:20:07.6] JV: So within our fund structure, as we're focused on only buying existing self-storage facilities with Lean and place cash flow that we can add value to with operational efficiencies over time, just growing in a line, controlling the expenses, growing revenue, and our main line of defense for our correction is that we're buying these things with existing income, and if we screw up our pro forma, we don't grow in AI, we don't go a revenue like we think we can, it's still a rational dividend yield and still a good bet service coverage ratio to make our lenders happy if there's a massive Boogie of that, which I'm not sure how much worse you could get the 2020... We think we're pretty well defended against that, and we're also implementing fairly conservative leverage, we're levering most of our properties, it's 65% of cost, and we're getting some very attractive dead terms these days, our next acquisition is gonna be a fixed rate and 375% for 10 years, and that's full term interest only payments, so the loan never advertises and Amortization is good, but you can't distribute amortization, and if you're having a cash flow problem, you still have to make that payment, you're paying down principal, but it's substantially higher than an interest only payment so we're very focused on dividend yield, distribute-able cash flow, so we're buying occupied properties and we're financing them with conservative leverage that we think is very attractive and probably not leverage we're gonna see for a while.

[0:21:25.9] WS: What about any predictions that you may have for the real estate market, our industry over the next six to 12 months?

[0:21:31.3] JV: Not a good predictor. 'cause every time I predict, I'm wrong. I think that the deal flow is gonna remain very challenging for obviously entering or already in an inflationary environment, and I think the controlling hard cash flowing assets with a fixed cost to capital on the debt side is a great defense against inflation, especially in self-storage, obviously I'm biased, but all of our leases or month a month, so if inflation kicks up even more, our rents are gonna go up and our bed services go... Stay the same. So we're excited about that, but I think there's a flood of equity out there, and to a degree, not desperation, but a majorly high desire for investors to rotate out of the publicly traded equities markets, which are very much higher right now, and cash flowing part assets. So I see the competition remaining fire for their foreseeable future.

[0:22:18.1] WS: Alright, well, taking a pivot, just a little bit on a few final questions, Jacob, any daily habits that you have or depend about that have helped you achieve success?

[0:22:26.0] JV: Well, my discipline is diminished since we've had our kids, we've got a three-year-old or an 20 months, my old boys and... Congratulations, thank you. I try to work out, so I get to my road bike as often as I can, let of hiking and climbing in the summer time, the Golf Course as often as I can, but my main work management tool is my calendar. I live and die by my calendar. I block time off with... I have a task I have to complete. A lot of our investors and associates are accustomed to scheduling calls with us so that they call you out on the blue, you can't pick up the phone, you call them back, they can't... So really, calendar management has been kind of a critical component to just allocating your time during your day properly, and I see you do the same thing too, is scheduling your podcast, so it's a great tool every day of the week, it's just numerous appointments. They are scheduled.

[0:23:09.2] WS: Yes, we have to go By God, just like what you said, you have to... Man, have to live by that calendar

[0:23:14.0] JV: In my mind, mushy, because if it's not on my calendar, I forget about it, so I'm probably too relying on it.

[0:23:19.2] WS: Yeah, my assistant, I say if it's something, even if it just involves me, you better put it on there so nothing else even gets scheduled during that time. I like the point you made that even investors like that's an important meeting week, take it very seriously if an investor wants to talk, but like you said, they call it, we can't answer, then we call them, they can answer... If it's just scheduled, we can usually make it happen a lot faster, but what about your best source for meeting new investors right now?

[0:23:44.5] JV: So we're doing a couple of things. LinkedIn has been a great resource for us. One of our guys... In our marketing department does a lot of stuff on LinkedIn, so that's been really positive. We're in a couple different masterminds, we have a number of physician investors, Denis investors, and his networking and really establishing credibility and being educational and demonstrating to investors that we understand our space, we know what we're doing, we're not new in the real estate fund world or the self-storage world, and a lot of word of mouth too, and a lot of referrals, if someone comes in for 100K, they get a few distributions, they like your communication. They'll tell their friends about it. And it just kind of snowballs from there.

[0:24:19.7] WS: What's the number one thing that's contributed to your success?

[0:24:22.7] JV: Failures, absolutely failures, just learning what not to do on deals, not so much what to do, but what not to do, and one example is just kind of chasing shiny objects... I'm absolutely the shiny object guy in my office, he using that phrase, but that's the best phrase to use and describe it, we built a house out of shipping containers about six or seven years ago, we lost a lot of money on it, we learned a lot, we but our couple of sub-storage deals in our prior fund and we attempted to completely remotely manage them with no on-site employees, learn some hard lessons there, you can still do it, but you have to do it differently, so really just making mistakes along the way, and applying those mistakes to future deals and always just having capital preservation and the next down turn of the top of your mind and what your portfolios positioning looks like when and if that happens. So yeah, we learn from screwing up...

[0:25:08.6] WS: Who is it? I wish I knew who said this, but it's like, fail fast, right? Yeah, faster, you do that, you're probably gonna fail, at least partially, maybe, hopefully, it's not too big, but you're gonna learn and then you can move past that, I appreciate just your transparency 'cause that's all of us, whether we admit it or not... Right, and how do you like to give back...

[0:25:25.9] JV: So I did think Brothers Big Sisters for about eight years with my little money was nine to almost 18... A lot of time and effort went into that. It was a great experience considering getting another little here, but unfortunately, I've got my own two little... So when they're a bit older, I'll get back into it. We're also involved with a non-profit here in Denver called The Story member, they do a lot of historic preservation work around town, they prevented some beautiful old buildings from getting torn down and having sterol family and Retail builds on them, so those are two examples right there.

[0:25:55.2] WS: Jacob, appreciate your time, it is your level of transparency and detail that you've provided around operating a fund and self-storage and just the economy right now, a numerous aspects. A great interview and tell the listeners how they can get in touch with you and are more about you.

[0:26:09.8] JV: A couple of different ways. LinkedIn is one, Jacob Vanderslice. Email me at jacobverslice@vanwestparters.com or go to our website, VanWestpartners.com.

0:26:18.6 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 for free material and videos to further your success.