

EPISODE 1172

[INTRODUCTION]

0:00:01.6

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.

0:00:24.6

Sam Rust (SR): So, this is your daily Real Estate Syndication Show. I'm your host, Sam Rust. With us today is Neil Bertrand. Neil is a 25-year multi-family veteran, has operated across all multi-family asset classes and types, he's currently a co-GP in 433 units, and is a part of the re-group, which is developing 1.4 billion and new mixed-use developments across Texas. And specifically focusing on the Austin MSA. Neil, welcome to the show, thanks for joining us today.

0:00:24.6

Neil Bertrand (NB): Sam, thank you for having me. So, as I was doing some background research on you, Neil, and trying to make sure I was prepared for this interview, notice that you went to Liberty University and you graduated with a Bachelor of Science in Real Estate, and often a lot of people who are in the real estate space didn't necessarily point that direction initially as they started their career path, my degree was in business management, I went into sales and then migrated towards real estate and that arc is a somewhat familiar story, you might be more unique, and it seems like you knew what you wanted to do from a pretty early age, what sparked your interest in real estate and what led you to get your degree in that?

0:01:33.6

NB: So, it's an interesting story, when my wife and I met, I was actually a semi-professional musician and doing a lot of touring, can't really sustain 28 years of marriage if you live on the road 10 months out of the year. So, I decided to look for something else. My wife was actually already in property management and suggested I give it a try, and I did, I went to work almost

immediately with one of the largest companies in the country at the time, which was Ledic who are now called, I believe, Envolve, and just really gravitated towards the numbers side of things. And I've always loved the architecture of apartments and office buildings, and it just seemed like a right fit, there were so many different, there's so many different avenues in real estate. You want a career, there's acquisitions, there's asset management, property management, there's the lending side, there's just so many different avenues to pursue.

0:02:33.6

SR: That's fascinating. I have to ask, what kind of music did you play or what instruments did you play?

0:02:33.6

NB: My main instrument is base, I do play some piano and very little guitar, at the time, I play whatever you hired me to play, so I was in heavy metal bands, funk bands, bluegrass bands, wherever the money was.

0:02:49.6

SR: That's fantastic. Well, I'm guessing the pivot to real estate, it served you well.

0:02:54.6

NB: Yes it has, it's fantastic.

0:02:56.6

SR: So, as I look through your background, meal, you've worked for four different top 50 NMHC real estate companies, and you've been in a variety of roles, you've been in asset management, you've been a VP of Acquisitions, you're involved in development, you've worked in conventional senior lytic housing all sorts of things worked on all sides of the pie, I guess is what I'm getting at, what is the single most important, a lot of our audience is passive investors, they're trying to figure out how to evaluate sponsors, when you look at all those roles that come together to create a successful syndication or a successful project. If you could pick out one. What would it be and why?

0:03:34.0

NB: I think probably the most important thing that determines the success of a property is the

underwriting, it's not really overlooked, there's two types of underwriters and two types of underwriting models, the ones that are built for speed. So, you can go through as many deals as possible, kind of like a back-of-the-napkin approach, and then there are the underwriting models that take about an hour and a half to complete all the data entry and then start tweaking the numbers. The difference with those two is speed may allow you to go through more deals faster, but the more detailed underwriting when you are drilling down into every aspect of how to make that property successful and why it works, why it doesn't work. I mean, right down to the unit mix compared to the comps, and you've got 232 bedrooms, they've got 48, you can't be a little higher on your risk and they can because their availability can fluctuate and be wider, definitely the underwriting, 'cause that's where it really all starts.

0:04:34.0

SR: Underwriting is a really broad subject in and of itself, Neil. There's so many, as you just said, there's two main different schools of thought. There's speed versus thoroughness, maybe if we were gonna highlight one aspect. But there are a lot of assumptions that go into underwriting, and I think the job of a good underwriter is to flush out those assumptions, be able to back it up with hard data and introduce a level of conservatism into the overall business plan. You're obviously underwriting deals, both as a career and also on the side, you're co-GP and over 400 units in Texas. When somebody gives you a model and says, hey Neil, I have this project, I'd love you to look at the underwriting, where do you go first? What are one of the first, two or three things that you look for that tell you a lot about the underwriter?

0:05:20.0

NB: The first thing I'm going to look at is, are the sales comps accurate and are the market comps accurate? When you're comparing the sales comps, and it's going to depend on where you are in the age of the asset, have they chosen similar aged assets, similar sized assets, and how recent were those sales, our market, our industry in real estate as a whole fluctuates greatly. Literally, just three to four years ago, I was submitting LOI's, properties built in 1996 at 165 a door. I'm doing it on the assets that are built in 1984 for 165 a door, so that's how fast it changes. On the market survey side, and keep in mind, with my property management background, and it gives me an advantage, right, because I know immediately what to go look for on the market side, or is the subject property really passed against accurate comp and where did they place the subject property? Because, really, the property you're underwriting, you always want it in the middle, you

wanna hedge yourself against the property that's better than you and can command higher rent, and then you wanna hedge yourself against properties that may not have quite the amenity package or the level of upgrade. So, you get a good balance. And then I wanna look at on that market survey, did they just pull a CoStar report, your Yardi Matrix, Report and Trump those rents in, or did they go to the website and get the actual rents because there's always discrepancy there, and then have they plugged in a blanket rent increase across the board, that right there if you have a 200-unit property and you say, well, the market is, these rents are \$75 below market, I'm just gonna drop in \$75 across the board. You've automatically boned your underwriting because wouldn't of that 20, 75 are already fully upgraded units at market rent. You just plug the \$75 increase on top of that. So, now your return scheme. The other thing that I will go and look at is the performance assumptions, and even myself, having my background in property management, I always stress test the deal and really just kind of say, okay, let me push on the expenses a bit because everything is kind of variable until we go in with due diligence, but I also wanna see what they've got plugged in for income and expenses. Really, it's, kind of a rule of thumb coming from working with private equity companies and large institutional groups is 3% rent increase is kind of your max that you should assume anything over that, like a private equity group is gonna break you over the call, if you are telling them that you're gonna get 5% rent growth three years out, they're not buying it, and you need to be, you need to think that way as well.

0:08:02.2

NB: The best piece of advice I got, I've ever received in terms of underwriting and deal analysis was your IRR, your cash-on-cash, all of it mean nothing. And this is coming from a guy who was my mentor. He started in the business the year I was born, so he saw the crash, he saw the 70s, he saw the crash of the 80s, he's seen everything. At the end of the day, can you make the mortgage payment and keep that property if something happens in the economy, and Covid was an excellent proving ground for that point, right? We can project all the returns we want, but what happens when you have an economic downturn or a pandemic of that. And so that's another thing, can this property sustain itself after IOS expired in the markets turn, if there's something that happens where it's gonna put a financial squeeze on the asset.

0:08:56.7

SR: Yeah, those performance indicators are really important now in our circles, we hear stress testing all the time, and I think investors, they are used to that term and they'll ask the question,

but I don't feel like they know exactly what they should be looking for all the time. So, it sounds like one of the numbers that you pay close attention to, it would be break even occupancy. What other numbers are you paying attention to in your stress testing a property, are you changing your exit cap rates? What are you going into?

0:09:25.7

NB: Yes, so, I'm working with the cap rate, I'm looking at both the in-place cap rate and the T12 adjusted cap rate. One of the other numbers I look at, it's basically, in that T3 scenario, obviously everybody's gonna push their market rent before they list the deal, 90 days out, everybody's got a potential range, it just looks beautiful. I will circle back to the rent roll, drill down and find all the move ins for the last 90 days and see what they were actually leased at, either they were leased at that market rent or they weren't. That gives me a level of comfort in the underwriting when I'm looking at rents. The other thing is, if there is a \$150 delta between the subject rent and the comps, I'm not plugging 115 at my underwriting, I'll plug in 100 and see if the deal still works, you have got to leave that window there, at all times you've gotta leave some sway room.

0:10:28.7

SR: Yeah, I tell investors that all the time that you don't wanna maximize, there's a difference between what you think will happen and what you can underwrite will happen. I'm not sure about Austin, although I would surmise that rent growth has been really strong over the last 18 months, and we're probably looking at north of 5% rent growth in 2022, and if we had to guess, I think if the markets were invested in it's gonna be double digit in your markets, it might be close to double digit, but are we gonna model that? Absolutely not, because if you model that at the front side of our project, you can totally skew your numbers, and so there's a challenge because there's a lot of groups out there right now that maybe have cheaper capital, maybe they're willing to get a little bit more aggressive in underwriting, but as a result, they're just, they're inflating their models, and it's becoming more and more challenging to find deals that pencil. Are you finding that dynamic playing out in your markets?

0:11:11.7

NB: Yes, because we look for two types of assets, we have an in-house fund, and the target returns for our funders, they're all unicorns, it's 20% IRR, eight, nine cash on cash. We really wanna maximize things for our investors. We're still looking at fifteen ROI deals, eight cash on cash, but it's really getting harder and harder to find deals that makes sense, especially when

you've got assets built in the 60s that are on the market for 130,000 a door, I don't even look at that. It doesn't make sense at all.

0:11:42.3

SR: It's a wild world out there right now, you mentioned that sales comps or something that you really look at, Neil, I'm just curious, if you've ever worked in a non-disclosure state, it might be a little wonky for some of our listeners, but there's a handful of states out there that don't disclose sales prices, so everything is a little bit, it's harder to come by a good sales comps. Do you have experience and how have you overcome that itself?

0:11:42.3

NB: A Yardi matrix is actually a great tool, they've done a great job of getting the sales price information and having it in their system, and when you've been around for 25 years, you know people and you can just make a phone call and, hey, between us guys, I'm working on this deal, would you pay for years and they're like, don't tell anybody, but here's what I paid. 25 years in the business and the connections, it's kind of a great thing to have. But in that, one of our target metrics too is, is we wanna exit every deal minimum 25k higher than we came in, so all in, we've gotta exit, 25k higher, and that's another thing I'm looking at with the sales comps, is that possible? Is that delta there? If the sales comps have all recently sold for 10, 15 higher than what my deal is listed for, and I've got appreciation revenue growth in there, I have that comfort level that if we connect it to 25 a door, it's a good deal.

0:13:01.3

SR: Yeah, so one of the metrics that you pay really close attention to is that per door sales figure, I've heard you mention that in a bunch of different contexts, but that's something that you track pretty closely.

0:13:11.3

NB: Because it's also a good indication of where the market's going, like I mentioned earlier, just three years ago, a 1996 deal was 165 a door and now it's a 1984 deal. And I watched that happen for a myriad of reasons, but I saw it coming.

0:13:24.3

SR: This is a little bit of a tangent, possibly new, I'm just personally curious, insurance costs have

been going through the roof, and I'm sure in Texas, you guys are ahead of where we are in Colorado and Idaho, what have you guys done to combat, the combination of property taxes and insurance all just shooting through the roof, it's been a distressing trend that we've seen over the last couple of years.

0:13:46.3

NB: It's challenging, it's one of the reasons that we stay away from coastal cities, literally like we have a deal in Jacksonville and our insurance is just, it's really heavy there that it's like, Houston, if you're close to the goal for New Orleans, those cities, you're literally looking at 11-1200 a unit for insurance, if not four. I underwrite literally to about 500 in the big four in Texas. So that's just one of the things too. It's a cost of doing business. Luckily for us in Texas, being a high in migration state, and the people coming in, people coming from New York or Chicago or California, a \$1500 a month two-bedroom apartment is music to their ears, right? \$2000 a month, two-bedroom apartment is music to their ears. And that's kind of one of the things that continues to make some of these deals possible. The taxes, insurance and payroll, all really stress test your deal.

0:14:44.3

NB: Yeah, and we've seen payroll just in the last six months to keep our high-performing leasing managers and maintenance guys, it's been a little bit more of a battle out there that we're having to push pay 10-12% in some cases, and really just stay current with the market, it's been a little crazy out there. So, we talked a little bit about underwriting, Neil and some of the things – looking at your breakeven occupancy, looking at those market comps, the sales comps as a passive investor – one other aspect that I feel goes pretty underrated or is not looked at very closely is the property management side of things. Maybe people will ask and you'll get, hey, with X firm that has been in the market for 15 years, and that's as far as the conversation goes, how can passive investors truly do some due diligence on that property management partner? What things should they be looking for? What questions should they be asking when they're considering who to place their funds with?

0:15:38.5

NB: You know, I wish I had an easy answer there. Every management company is different, and one of the big, key things, when you're looking at a property management company is, there are two types. There are companies that specialize in a certain asset class, and then there are those that manage all the asset classes. For those that manage all the asset classes, how good are they

at it? For real, I was having lunch with a couple of investors new to the business, and they were asking me for management company recommendations, and the name of a very good management company came up, and my feedback to them was, I visited their Facebook page and looked at the asset classes they are always promoting and talking about, we just got management of this deal, are any of those, the asset class that you're buying, chances are it's not, so those are the kind of things to watch for. And there's companies, here in Dallas is a great company that literally their wheelhouse are the properties that no one else wants to talk in high crime areas, rough clientele, and they manage those really well, so it's really about does that property management company specialize in a particular asset class and locations, and does that align with what the property you're investing in, is it a 'the deal'? Are you investing in a 1965-built CDO that is going to be managed by a company who 80% of the portfolio is classic properties because I'm gonna be completely honest with everyone, I work for free management companies, 70% of their time is spent on the largest client and attracting new business, right? So, if you're not the largest client, you're not getting a lion share of attention. And that's just the way it is, that's with every industry. Who's their largest client? Who's taking attention away from your deal, but again, and I'm kind of going down the rabbit hole here, but really, it's are they experts in that asset class and in that market? Like, we get approached for fee management and cities that we have no experience in, we're gonna say no, we are not going to guinea pig that person's asset in a market where we don't have relationships, we don't have knowledge of the market, you really want them to be local area experts, experts in the asset class. The other thing I would encourage people to do is, and this is going to sound really silly, but make a list of their properties, go to those property Facebook page, Facebook pages, and look at the reviews and the posts, and how they interact and handle reputation management. That is a huge thing because 85% of renters will now go to a Facebook page and read reviews before they even call a property. And it's not that they're looking for bad, you can have the bad reviews, but it's how you handle those bad reviews and overcome them. If a post starts with a bad review and ends with the person, or the original poster saying, all taken care of, thank you so much. That's evident that the property management company is involved and proactive.

0:18:42.3

NB: Yeah, people wanna see activity, they don't wanna see a ton of bad reviews and no response from management. They want signs that the management is engaged. And I think people understand too, especially in 70s product that you're never gonna get to a five-star rating, it's just not the nature of the property itself or the clientele, but being in the mid-threes is a really solid

goal with engagement. That leads me to a question, Neil. Every firm goes through its own life cycle, and a lot of folks that start out in the syndication world, they're starting from zero, and so they're getting one deal, a couple of deals, and then some groups are fine with the 300 to 500-unit range, call it, but some are growing beyond that, at what point does it make sense, in your opinion, to vertically integrate? I know that your company, the Regroup, is vertically integrated on the property management side, when does that start to become a reality or something that you should do in your life cycle as an organization?

0:19:42.8

NB: That's a very interesting question, and there's a lot of answers to that. It's going to depend on the end goal, one of the other factors is, is gotta get permission from your lender, the change management companies who on your team is the property management expert, because they're not going to let you take management away from a sound reputable management company for you to go ahead and guinea pig, your new startup property management company. Who's your property management expert? Are you generating between the asset management fees and the property management fees that you would take in? Are you generating enough to hire the level of staff necessary to effectively run those assets? If you're 3,000 to 5,000 units, you've probably got anywhere from 7 to 12 deals under your belt, you're gonna need two regional managers, you're gonna need HR and accounting, do you bring those in-house do you outsource those to a third-party company? There's a lot of questions and you've really gotta sit down and write it out on paper, and then again, the other thing to ask yourself is why are you taking management in-house? Can you really do a better job than the property management company you chose, and if they're so bad, why did you pick them? Do you really wanna be a proper manager or do you want to continue to analyze deals, raise an equity network and build your portfolio? Because property management is death by 1,000 paper cuts. Once you veer into that lane, it's hard to get out and get back to keeping up the networking, raising the equity analyzing deals. You've gotta ask yourself, is this what I wanna do? Most people don't wanna be property managers, I think they get to a point where by bad advice, they selected the wrong management companies or they expected that management company to treat them like they were their only client. There's a lot of reasons why a management company is a "bad management" company, and some of those are, yes, they are, and the others are you didn't underwrite well the deal to begin with, and it was due. But to take the management in-house, really, it's going to be you've gotta have the people that know what they're doing. In the state of Texas, do you know what water, if you have a boiler system on your property, the temperature that water has to be in the tank? 120 degrees. Do you

know what it has to be coming out of the faucet? 104 degrees. Are you ready to invest time into making sure that you are on top of OSHA EPA, state, county, city compliance ordinances, fair housing, all of these things? It's a different animal.

Two cities in America were the first to add transgender to their list of protected classes, Tampa and (inaudible), this was five, six years ago. You don't know that and someone makes a transgender person feel offended, you're getting sued. And if that property is in Tampa or Florida, now you've got a fair housing complaint on top of it. So, ask yourself, how much do you really wanna be involved in that? If you don't, but you wanna have more control of your assets then you need to go find a stellar team that can do all of these things, that has those numbers and that has that knowledge, can spit out those numbers like I just did.

0:22:53.8

SR: It's so heavy in operations, and honestly, it's not that profitable of a business, especially as a sponsor, if you're bringing that in-house, in my experience, you're doing that because you don't have a lot of options, or you've mastered operations and you have somebody that can head it up and just kind of set it and forget it with a team, but you're gonna make way more for your time and effort by going and growing your portfolio than you are by bringing that in-house as a general rule of thumb.

0:23:21.8

NB: Yeah, I mean, in-house management, it really it's like you said, it's not a huge profit business, I've got some friends that have 14-15000 units, they're vertically integrated, and basically what they do with their property management profit is schmooze brokers all day.

0:23:38.9

WS: And, hey, that money comes back 10 and 20 fold. It does.

0:23:41.9

WS: And they built a team of operations expert and the experts, and they compensate people really well, but that's what you have to do.

0:23:50.9

SR: Awesome, well, as we draw down towards a close here, Neil, the real estate market, highly volatile, there's a lot of conflicting signals in the marketplace, we're coming off of an 18-month

bull run, basically, once we got through the Spring of 2020, as you're looking for do you guys are heavy into the development, which I think is an interesting play, it's something that we're getting into a life bridge Capital as well, but what are you watching for on the horizon that tells you that change is a foot.

0:24:19.9

SR: There are a lot of people who got into syndication in a market where anyone can close a deal, right, you've got groups out there that have literally 15 to 18 GPs, are you making money? You've got deals that were, like I mentioned earlier, underwritten on these four-tab underwriting models, and honestly, the main reason a lot of these people survived the pandemic was because of stimulus payments and things like Texas rent relief, those options not been on the table.

0:24:47.6

WB: We would have been picking up their deals and foreclosure, I think we're going to see coming ahead or people who overpaid the free money running out. Unfortunately, some of the residents have gotten used to not working and you can evict me when the government says you can. So, I think we're going to see people, there's a few things that are gonna happen. I think you're going to see the people who didn't do their homework try to sell out their GP and exit the deal, or pretty much just get out the deal to try and save their reputation and say their investors' money, they won't be selling for much above what they purchased. One thing I learned from my mentor was anytime there's an economic downturn or a pandemic, there's always opportunity for people who have the capital and are ready to move forward with it. I think there are gonna be people who they won't lose their properties, they won't get foreclosed on, but they're going to have to, for lack of a better term, not necessarily short sell, but sell for exit and for reputation, your reputation sake. And I think that's where some of the groups will come in, like our group and be able to capitalize on those opportunities. We're already looking at doing.

There's not a crash and there's not a huge downturn coming, but there is a shakeup. I always say the best thing about real estate investing is anyone can do it, and the worst thing about real estate investing is anyone can do it. So, the people that come in and they keep their nose down and they learn, are the people that survive, and the people that are only interested in speaking engagements and speaking in conferences, and they wanna look like the expert, but they don't do the homework or the people who are gonna be buying their deals off of the courthouse steps, or if they're lucky, will be buying it before it gets there. Honestly, I've already, I've already got a long

list of properties that are on the watch list, on the loan watch list in pre-foreclosure. I'm watching those deals. I don't wanna say, we wanna help people save their reputation, so we don't want to be able to go to foreclosure, we wanna take it off their hands before they get there, but those types of things are coming.

0:26:48.3

SR: Definitely, the rising tide of the last 10 years, I think the next 10 years are gonna be operations, I've said that many times on this podcast, but I think the good assets are gonna flow from those who didn't have a plan to those who do and can execute on it.

0:27:00.3 S2: Yeah, that's what it's been. And unfortunately, I remember being a kid taking martial arts, and there was a sign on the door that says, he who knows, watches and doesn't speak. He who doesn't know, speaks. And so, what I've seen is, and like I said, people came in, they haven't seen an economic real estate cycle, and there were people who were literally only in the business for two to three years, and the minute C ovid was taking place in-house was announced, their hosting webinars about how to navigate the pandemic. Meanwhile, you've got guys like Robert faith who literally founded at Starwood and grey Star and is responsible for 70000 units who waited a month before releasing a statement. And who do you think I'm listening to? And what do you think we should all listen to the guy that built 700, literally 700,000 units in several countries in 23 years. I want his advice.

0:27:56.4

SR: Yeah, and he's gonna be deliberate, he's gonna have a plan, he's gonna watch the condition, it's just such a volatile situation, I did get a kick in March 15th, 2020, we're getting webinars from newer folks trying to share what we're gonna do to survive the pandemic.

0:28:08.4

NB: And it's like, this is unprecedented, but it really boils down, if I got one really great piece of advice, I think is learn. Okay, don't worry about being the guru, don't want by being the guy on stage, yeah, looks great, but you don't know what's going on behind the scenes, you don't know how many leads are on the property, you don't know how many cash calls they're making, learn. Read everything you can take courses from higher and take courses from The Apartment Association, learn the underwriting, learn the asset management, learn the operations, learn how to monitor those operations, right. You may not wanna do it day-to-day, but you better know

what's going on, learn.

0:28:48.4

SR: That's a fantastic place to leave it for today. Neil, thank you for joining us. If folks wanna learn more about what you're doing at the re-group and some of the developments that you guys are working on, how can they get in touch with you?

0:28:57.4

NB: Sure, you can reach me at Neil.REIT.com. You can visit us online at REITgroupinvestors.com And if I'm brave enough, my cell is 972-849-5707.

0:28:57.4

SR: Awesome, well, hit Neil up. He's learned a lot. Putting it into practice. Really appreciate you joining us today, Neil. Thank you to our listeners for joining us on another episode of the real estate syndication show. Have a fantastic rest of your day.

0:29:27.1

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.

[END]