EPISODE 1362

[INTRODUCTION]

Ronald Rohde (RR): It's tough. you know I get a lot of conversations with clients, as well as with the lender saying, “Close quickly, close as soon as you get the appraisal and no delays. I can only lock in this rate because banks are unilaterally just raising their interest rate”, even though the market is maybe 5% right now. But lenders are just pulling back from their original term sheet or original parameters and saying five and a half because our bank has a 90% probability that they're going to raise the rate half a point before the end of the year.

[INTERVIEW]

Sam Rust (SR): This is your daily Real Estate Syndication Show. I'm your host, Sam Rust. Joining us today is Ron Rohde who is the founder of a commercial real estate law firm in Texas that focuses on helping investors buy commercial real estate to build wealth. Ron became a real estate investor before becoming a lawyer and currently combines his career and passion for helping people achieve their goals. Ron, thanks for joining us today. Welcome to the show.

RR: Thanks for having me, Sam.

SR: You got your undergrad from Cornell and then you go to Miami for your JD. That's not a typical path. What's the story behind that?

RR: Well, for me, it was you know, going to New York, going to the snow and then looking for the complete opposite, too much snow, and then go for the sand and the beach.

SR: Yeah, that's two very diverse locations. And then what brought you out to Texas and get started? I know you mentioned before we got on there that you focus a lot on the industrial

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realm. And you mentioned in your bio that you focused on investing before getting into practice. What was that journey like?

RR: I'm originally from North Texas. So for me, I always knew that I wanted to come back home, so to speak, raise a family, do that thing. But I was practicing in Florida for a little bit. I got a job opportunity to come back to Dallas. So, I took it. My parents have always been investors, so they invest in commercial residential notes. They've done it all on the spectrum of investing. I've learned from that. Yeah, I just came back, did that job. I was general counsel for a real estate developer doing ground-up multifamily construction. We were doing a build for rent before it was cool. We built like 68 duplexes out in Houston. So that was a fun project. I had my own firm for five years. It's been fun. I love helping people who use commercial real estate or real estate investing to grow on their journey and just exciting for me to talk to people every day.

SR: So, you mentioned industrial investments. Are you joining in on other syndicators? Are you sourcing your own deals? What does that look like?

RR: Yeah. We have a couple of partners. I mean, all the stuff that we buy is not just me personally, but we're not doing formal, you know, Reg D offerings 506. Usually just a couple of buddies will put pull together. So, right now we have about 100,000 square feet of single-tenant, net-leased buildings across DFW, all fully leased. We're looking to renew one of them right now. So, that guy, he knows he's in for an eye-opener, but now should increase the cash flow a bit. I sold all the residential stuff, transitioned into industrial and I've loved it. It's been fortuitous. Maybe I should have gone into multifamily like you guys but am happy with industrial so far.

SR: So, in the industrial space, you tend to have longer leases. It's kind of a double-edged sword. It can be good in a stable environment. In an inflationary environment, maybe not so good. But you're turning over a lease now. I'm curious if it's been a tenure tenant or something approximating that, their lease may have gone up 50%-75% on a per square foot basis. What's tenant retention like when you get to that? Because I would imagine that in industrial especially

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single tenant, like what you're investing in is fairly sticky. But there's got to be, as you mentioned, some sticker shock as well. What's your experience with that?

RR: I'll comment on the first part of your statement. I definitely agree with what you're saying, it's absolutely correct. You know the difference between something like multifamily or retail, you have opportunities to mark to market your rents a lot more frequently. On the flip side, for multifamily in a gross lease, you have to have some way to control your expenses in an inflationary environment because you can get nailed on property taxes, insurance, and that sort of thing. So, for triple net, yes, you cap your upside in terms of a longer lease term in an inflationary environment. But you're also capping your downside because we pass through property taxes, insurance, and maintenance. So, our downside is also really capped, or there's a floor. Just given the full picture of why we made the decision or what the pros and cons are for this triple-net, yes, you kind of have a band of gain. It kind of projects out like this. Your upside is capped for the next couple of years but your downside is also kept assuming the tenant stays and is solvent.

To your second point, yeah, this particular building is leased to a larger, I would call them a large regional, they're not publicly traded, but they have audited financials. They have several $100 million in revenue every year. So, this cost, as a percentage of their total expenses is pretty small. And for us, they've actually been tipping their hand. I don't know if their real estate negotiation and their operations we're on the same page because they're in the process of almost about to renew. They just installed a $40,000 fuel tank to re-supply trucks. I mean, they spent $40,000 in insurance both installation insurance and operational for that fuel tank. It's above ground, thankfully. But they requested all the permissions. They gave us all the plans and all that process. And they did that right before they - I mean, you're going to install, you're going to spend 100 grand on this fuel tank - right before lease negotiations? Not going to help a ton when your real estate guy says, oh, we can find cheaper space. Like yeah, but you just installed 100K.

SR: The sunk costs will be working in your benefit at that point.

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RR: Again, they're a good tenant. They've spent a lot on their build-out, and they're putting more money into their office right now. So, I guess the bigger picture, you know, what we're trying to do is look, you have a renewal, it's at fair market value, you're gonna send the option to extend and we just really have to figure out what the number is. I think by taking one more variable off, kind of makes it a little bit easier because then we're really looking at apples to apples. And to your point, you said tenure, this is a five-year. They did one five-year with two five-year renewals at fair market. So, that's really what we have. You know, they say we'll agree on another five years but what's the rate? What's market? And now we can look at comparable spaces that are offering five-year terms. So, they can't just show us like a 10-year lease that's a lower base. In this environment, it's crazy. I'm going to show them a one-year lease and be like that's comparable to a five-year because no landlords want to even sign long-term leases that lock them in.

SR: Especially in DFW. I know a lot of folks that are investing in industrial multimillion square foot portfolios. And it's just ridiculous what has happened. It traditionally was very stable and not very sexy. Like you said, the floor is high, the ceiling is a little low. And you're just coupon clipping but coupons have been extremely big over the last couple of years, especially in Texas.

RR: For sure. And that's the thing, you know, we kind of play in that smaller space because just to add on to our thesis, they're building tons of new construction. But it's all these bomber buildings, it's all 500,000 square feet, 300,000 square-foot buildings. They're not building replacement product for 100K or below. And so, those tenants that don't need a full 100 and prefer a single-tenant, maybe with a yard and they kind of have that utility being a single tenant, there's just no replacement product. It's just not as cost-effective. So, we hope that's just going to put upward pressure on the rents because we're completely below the new construction stuff at a million square feet.

SR: Certainly. So, I was looking at your background. As you mentioned, you've worked for a couple of different law firms, and you struck out and started your own law firm. It looks like you

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went full-time in October of 2020. What pushed you to go in that direction? Strike out on your own?

RR: Yeah, you know, I think for me, it all relates back to the investing and what I want to do with my time. Hopefully, I'm thankful enough that I kind of realized, your time is your most valuable asset. And for me, having my own firm allows me the flexibility to (a) provide the type of legal service that I specifically want to provide to my type of investor clients as well as having the freedom like, on a Thursday, you know, I'm going to duck out of the office for two hours. I've got to drive to talk to a tenant trying to get them to re-sign on this different property. I can just do that at the drop of a hat. I mean, I scheduled it today. But if I was with a larger firm, I may not have that flexibility to pursue or take care of my own investments.

SR: That's fantastic. I noticed that you're also starting a YouTube channel, why YouTube? What kind of content are you trying to deliver? And what's the thesis behind that?

RR: Yeah, definitely a plug for that. Smash the "like" button. Subscribe. So, this was during COVID, kind of locked down and back at home. I kind of did a survey of different social media. I knew I needed to get online. I needed to get that digital presence whether it was like paid Google ads, or Facebook or Instagram, Snapchat, I don't know. But, I settled on YouTube, really, because for the longer format. People these days, and in my experience, they go to Google, they type in something, they would rather watch a video from a friendly face like yourself to learn how to do something as opposed to reading a 2500 word article. That's just not convenient. That's not what people like to do. They like to put the air pods in and listen to a podcast type of thing and learn about something. So, that's what drove me to it plus the fact that Google owns YouTube, and they prioritize Google feeds over to YouTube. So, that's kind of a win-win on that side. It's been two years since the YouTube journey but it's been great. I get a lot of great interaction and feedback from people that watched the videos.

SR: Your videos are pretty well done. I'm curious, are you bringing that production in-house? Are you working with a third party? How does that part of the process work?

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RR: I appreciate that. You probably selectively looked at good ones. Don't go too far back. If you go back in the years then it gets pretty embarrassing. I do a mix, you know, I've had third-party editors. I edit a lot myself. I have the software, I do the B roll and stock stuff. I don't know, I haven't found a happy medium for that. But I will say anything good is from a third-party guy. And if it's terrible, it's probably me. It's just tough. I follow some of the big YouTubers, and they talk about it. Some of the big guys with million subscribers, they still edit their own stuff, like Graham Stevenson. I mean, he still says he edits. He edits every single one of his videos, and you know, it's that kind of control or micromanaging. That's just one thing that he's still really likes to do. So, I'm torn. I go back and forth like time versus money. I do a little bit of both right now.

SR: I started my own podcast many years ago that was not connected to real estate. And my buddy and I did some of the editing ourselves. My buddy did more of it than I did. But being involved in that process, I think it's helpful. And then very quickly, I started having the time versus money argument in the back of your head. Maybe I know enough to be dangerous, and I can oversee someone else doing this work.

RR: For sure.

SR: I would be remiss, Ron, to let you go without at least touching on some stuff related directly to your profession. And one of the questions that I wanted to touch base on that might drive some value for folks is around loan terms, loan covenants and specifically especially when you're dealing with banks and credit unions. There's a lot of retraining going on out there with because of all the interest rate volatility So, from your perspective, you're working in commercial real estate day in day out, how can operators and investors protect themselves as best they can in such a volatile environment? And try to get to the closing table with the deal intact?

RR: Yeah, absolutely. It's the wild, wild west right now. I'd have no love or particular affinity for lenders.

SR: They are a necessary part of our business, right?

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RR: They're a necessary part and and I get it, they move things along. They really move in lockstep. To me, the ultimate example of herd mentality, they will do, they will loan what other lenders are loaning at, they're always curious what other people are doing, like, why can't you just do your own underwriting? Your own borrower? If you like the property, you can be the only one that pushes out a loan, and you'll be the only one that makes money. And they say, "no, you know, that's not what we want". Because what we're seeing is just a lot of uncertainty both on the rate as well as the bank's risk appetite. And those are the two things that really can kill a loan as well as killing DSCR for borrowers as understanding what the cost of that capital is. And maybe to a lesser degree, like some of the amortization is just pushing up those monthly payments. And then it bus, you know, like a one-two, or one-two- five, something like that.

What we're seeing, you know, even on the industrial space is probably a little bit of pulling back of LTV. We were pretty aggressive at 80 for a while. And you could get any kind of industrial with a halfway breathing tenant to get 80% LTV and you know, all the super low 3%, three and a half percent rates. But now it's tough. I get a lot of conversations with clients as well as with a lender saying, "close quickly, close as soon as we get the appraisal in. No delays, I can only lock in this rate because banks are unilaterally just raising their interest rate", even though market has maybe 5% right now - we'll date ourselves in June of 2022. It's like 5%. But lenders are just pulling back from their original term sheet or original parameters and saying five and a half because our bank has a 90% probability that they're going to raise the rate half a point before the end of the year. These are longer term, fixed debt. So, for seven-year term, they're wanting to hedge that something they think is very likely. So, for a seven-year fixed term, they're just bumping it to five and a half and you as a borrower, kind of pulls the rug out from you, right? May not hit your returns. Worst case, you can't even know covered debt service, you got to raise your equity, decrease your LTV, and suddenly you're at 68% LTV. I mean, I get it, it helps but it's not what you underwrote for and you still maybe need to do some value add. It's tough.

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My advice, I guess for everybody is, it doesn't matter how much your representative at the lender says it's locked in, until they go to committee until they have that approval, I would really continue to factor in a fudge factor. Maybe we're seeing more financing contingencies come back because those are real deal killers. And you know, you can say if I don't get interest rates below five and a half, I'm going to kill the deal. I think, most sellers will probably sign that because they're laughing, they're like okay, yeah, rates are at 5%. Right now, you're fine. Five and a quarter maybe you'll still close. Five and a half you'll still close but it may give a hedge and let you get that earnest money back even if you're past the inspection period, due diligence inspection period.

SR: You touched on something that I've seen firsthand. Speed is of utmost importance right now. Hopefully, no one's executing on a refinance right now for purchases getting your third parties done and in order and avoiding all stickiness along the way from the buyers and will only serve you well. Lenders are pretty quick to toss overboard the people that are difficult to work with. Power is in their hands now. It's not in the borrower's hands anymore.

RR: That's a great lesson too. I have a former boss, like a mentor. He was telling me you know back in like 2012, 2013, 2014, lending was really, really dry. I mean, we were doing new construction multifamily, we could not get construction loans like above 55% LTC. And it was just insane how little the lenders were pushing out because they were scared, Everybody was. But fast forward to 2019, 2020. Lenders were bending over backward, giving you 80%, 85%. They just wanted to push money out. If you are building a multifamily, blank check. It doesn't matter what your feasibility says, your demand, your business plan, your rents. They're just pushing money out.

My mentor said, it's your duty as a real estate investor, you had to turn the screws back on the lenders because they won't hesitate to screw you over. And you have to screw them over back when the tide turns. Pick up that 80% refinance, non-recourse and just lever up your property since, okay, good luck now. I've got my money tax-free. If I can't raise the rents the next couple of years, you can have the property back, no problem. I've got nothing. I've got all my money out. It's an interesting approach. But I definitely have more understanding of where it comes

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from now that I see a lot of these borrowers getting pinched up and put in really bad positions by the lenders that just shrug their shoulders and say, sorry. And we'll say, well, we're going to remember that because in three years, in four years, when you're chasing us for loans, and you're begging us to give you a shot, I'll be like, no, we remember, we remember 2022.

SR: That's certainly true. These things go in cycles. And we have just seen it flip, pretty crazy speed, I would say. Not as a veteran in the industry but just looking at past cycles. It feels like there have always been tipping points. But this one has been just very quick and there are a lot of competing factors. What's going to win? Interest rates or inflation? Particularly when it comes to multifamily and I think the jury's still out on that.
If you're up for it, Ron, I have a couple of questions here. We'd love to just do a lightning round on a couple of legal things, if you're up for it?

RR: All right.

SR: All right. What's a common mistake that you see borrowers make when they're interacting with lenders?

RR: I think not having a clear understanding of who's going to PG. There's a lot of misconception...

SR: When you say PG, can you define that?

RR: For purposes of answering this question, I'm typically talking recourse, private lenders, just kind of bank lenders, not your Fannie product. This applies to more tried and true commercial lenders. Not knowing or having that information of who's going to provide a personal guarantee (PG). Because again, that's the space that we were in. Our sweet spot is $10 to $25 million, $10 to $30 million, lots of personal guarantees, it's fine. But then you take other partners in, there's uncertainty about who's going to provide a personal guarantee. It just rubs borrowers the wrong way. When they say, hey, you know, Sam's putting in money, but he's not gonna guarantee it. Because it does put a lot of obligations on you as an individual that, you know,

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reporting and just, you apply for more loans, and you got to disclose it, and they may want to talk to the other lender. That's a big mistake. I see people don't understand. They say things like, I, Ron, just want to personally guarantee and the lenders are like, well, who else owns it? If Sam is in on this deal, I want him as a guarantor.

SR: All right, what's a term in PSAs that you wished got a little bit more attention or buyers spent a little bit more time and thought negotiating?

RR: Yeah, so this is a new one. It's kind of futuristic. But we're seeing a lot more focus on intellectual property. The term in PSAs is personal property, right? Anything that's not real property is classified as personal property. Maybe I'll get a little bit burnt, so, when you buy, most traditional of those PSAs, it's real property. You're buying the dirt and improvements. Okay, we get it. That's easy. Personal property, that's your golf car, your inventory, equipment, tools onsite. Okay, fine, we get that too, furniture, office, that's fine. But then now we have intellectual property which is the goodwill of the name. Maybe you have a website that's just generic. It could the website. It doesn't have to be beautiful view villa apartments, right? It can just be the property address with information about the location. You may have apartments.com listings, definitely Google my business listings, emails, phone numbers. I wish people would spend a little bit more time just being very clear with, say, us about not in the LOI but do you want any of this intellectual property that's out there? Because I have had a lot of clients, they're not necessarily looking to reposition an asset with a new name. And if you're not doing a new name, then by default, you should be absorbing the existing intellectual property on the internet, the digital property. And they don't put as much of a focus and I have too many gray hairs chasing down sellers to get passwords, to get emails, the GoDaddy domain hosting that has the website files. They sent a reset to your email and you know, these people are busy and I get it and if it's post closed, you have very little leverage to try to get it after closing. But then my clients are really chasing me, being like, Ron, we really want this. This is valuable to us because we're not going to a full rebrand. We want to keep it. Now we need to access the website. The guy says you can have it but they don't have the password. So that's something that I think is very 21st century or if you're savvy. You don't need to claim it but you should just understand that it's out there and tell me do you want it or not? Because

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if you do, we're going to take some steps and make it an affirmative obligation. If you don't care, then actually, we may ask them to shut it down. But you still maybe want to buy the website and redirect it to your new website. There are all sorts of things to consider. It takes 30 minutes on the buyer side. But I see a lot of people asking that question, they're like, huh? what? Because how do you how do you handle that? Do you guys have a methodology that decides?

SR: So, we are working on formalizing a process. We've had a couple of deals here recently that had more developed internet property rights, you know, all those things, domains, and et cetera, et cetera. You know, we take Oakley have been in value add and buying from legacy owners. And those two things, 70s product and people, have been for 20 years. They probably don't have a website. But we're starting to see that more and more, negotiating that and getting everything upfront. If you don't have it, by the time you put your signature to the closing statement, the amount of pain you have to go through to get. As you testified, we're too young for gray hair, both of us, we can't have that. But you end up with some if you're not careful. And we have one, our very first deal with a website. This was like a year and a half ago, there was one piece and I think it was the GoDaddy registration. But when we went to renew, we weren't the owner. It just was a disaster. You know, such a small detail but if we don't keep an eye on those small details, they can become a big pain in the butt. So, it's a really good exhortation for operators as technology continues to push into our industry.

RR: Yeah, absolutely.

SR: Fantastic. Well, Ron, what's one habit that 's contributed to your success? Daily, weekly, monthly, something that you do regularly that would be beneficial for our audience.

RR: I work out consistently. Another perk of owning the company is you know, I tried to duck out a little bit early, get to the gym, get home for dinner. For me, I work out in the evenings, not the morning kind of thing. But it's consistent. And it doesn't matter. I'm able to prioritize it at a time. That's just a muscle. And I think whatever your habit is, doesn't matter. You need to

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practice that muscle and practice making something, anything a priority, and then just doing it every day.

SR: Definitely working out is important. I think having a daily or even a multiple time a week habit of doing anything is tremendously helpful. It's about building the skill of diligence, and whether that's reading, working out or spending time with family, any of those things are productive when you force yourself to do that on a regular basis. Fantastic. Well, Ron, really appreciate you joining us on the show today. If folks are interested, I know we mentioned your YouTube channel. We'll throw the link in the show notes. But how can they reach out to you?

RR: Yeah, definitely, YouTube is great. Website is www.RonaldRohdeLaw.com. There's plenty of emails on there.

SR: Fantastic. Well, thanks again, Ron. Thank you to our listeners for tuning in to another episode of The Real Estate Syndication Show. I'm your host Sam Rust signing off.

[END OF INTERVIEW]

[OUTRO]

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