



NEAL BAWA



ANNA MYERS

# BUYING RIGHT

  
Deal Analysis



Multifamily University

# Acquisitions Timeline



**Underwriting** as an iterative process of analyzing a multifamily property. At each step you learn more, and assumptions can change...

# Underwriting: Where Will Our Adventures Take Us Today?



## Our Agenda

- Key Underwriting Terms – NOI, Cap Rate, DCR, CoC
- The OM, Rent Roll & T12
- Underwriting Models
- Things You Need to Underwrite a Property
- Your Turn – Underwriting Lab
- Calculating Returns : CoC to IRR
- Deal Structure : What % Do You Take?
- Due Diligence & Rehab Budgets
- Value-Add Examples
- Rent Comps
- Sales Comps
- Game Time!



# Net Operating Income (NOI)



A multifamily investment is a business:

- **Operating Income**
  - Rental Income
  - Laundry, parking and other sources of income
- **Operating Expenses**
  - Property tax, insurance
  - Repair and maintenance
  - Management, marketing, administration
- **Debt Service**

**NOI =**

**Annual Operating Income**

**(LESS)**

**Annual Operating Expenses**

\*NOI does not include debt service



# Capitalization Rate (Cap Rate)

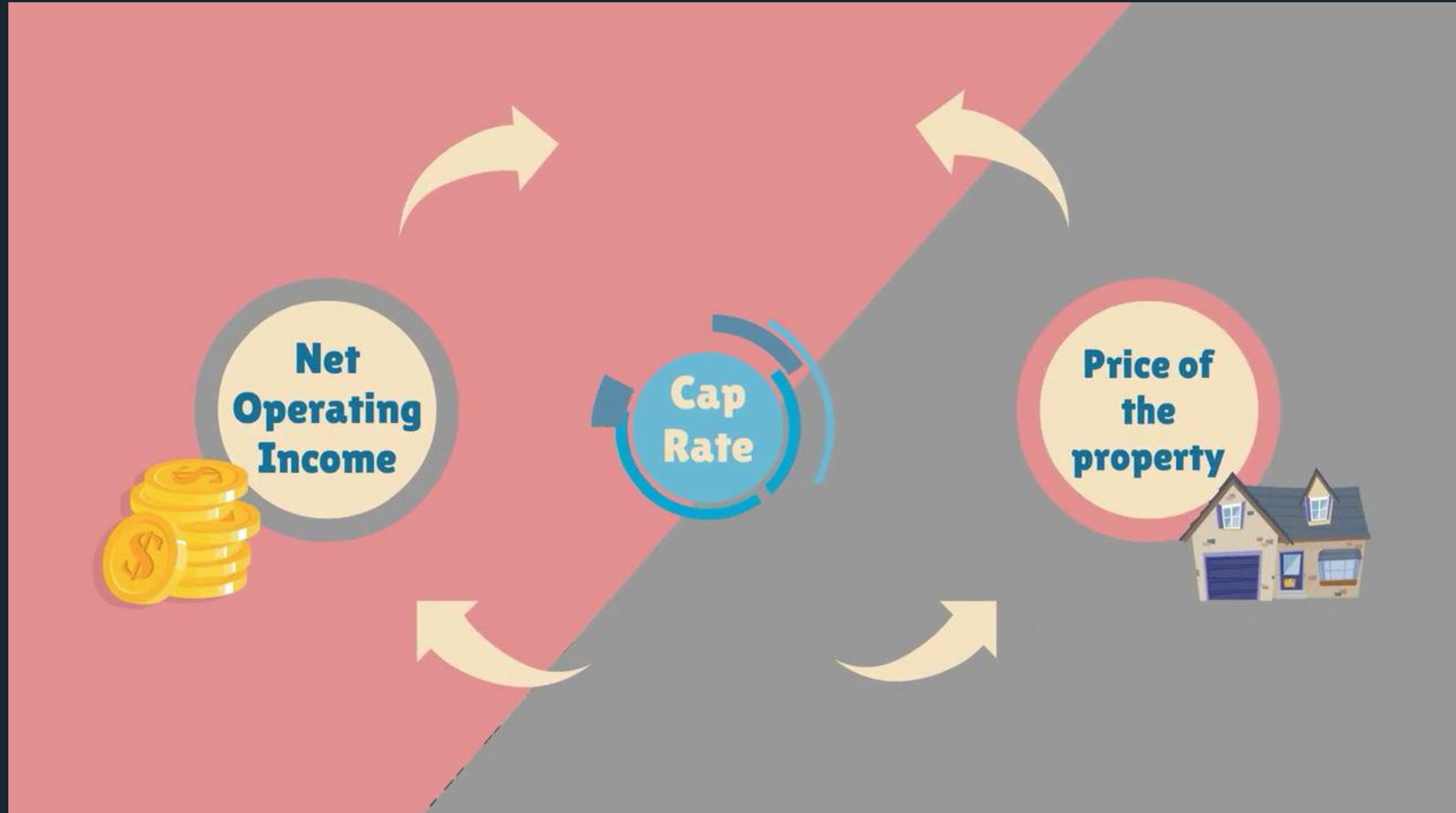


- This is a measure of the relative return the Net Operating Income (NOI) yields on the purchase price on an annual basis

$$\text{CAP RATE} = \frac{\text{Net Operating Income (NOI)}}{\text{Purchase Price}}$$

# Capitalization Rate (Video)

➔ Go to: [Video Link](#)



# Example: Cap Rate Calculation



What is the Cap Rate of the following property?

- Purchase Price = \$10M
- Annual Income = \$1.3M
- Annual Expense = \$500,000
- Debt Service = \$480,000

$$\text{NOI} = \$1,300,000 - \$500,000 = \$800,000$$

$$\text{CapRate @ 10M} = \frac{800,000}{10,000,000} = 0.08 = 8\%$$

How will it change if the price is reduced to \$8M?

$$\text{CapRate @ 8M} = \frac{800,000}{8,000,000} = 0.10 = 10\%$$



**HIGHER CAP RATE =  
CHEAPER PROPERTY**

# Cap Rates: Main Factors



1. **Risk:** Higher Risk ▶ Higher Cap Rate
2. **Lending Environment:** Easier to get money ▶ Lower Cap Rate
3. **Liquidity In The Financial Markets:** Rising Market ▶ Lower Cap Rate
4. **Tax Codes:** Favorable code create tax shelters ▶ Higher Demand ▶ Lower Cap Rate
5. **Appreciation:** When real estate prices are expected to rise, investors are willing to pay based on a lower Cap Rate



# Debt Coverage Ratio (DCR)



- The ratio between cash flow and mortgage payment



$$\text{DCR} = \frac{\text{Net Operating Income (NOI)}}{\text{Debt Service}}$$

- Also known sometimes as “Debt Service Coverage Ratio” (DSCR)

# Example: DCR Calculation



What is the DCR of the following property?

- Purchase Price = \$10M
- Annual Income = \$1.3M
- Annual Expense = \$500,000
- Debt Service = \$480,000
- NOI = \$1,300,000 - \$500,000 = \$800,000

$$\text{DCR} = \frac{\text{NOI}}{\text{Debt Service}} = \frac{800,000}{480,000} = 1.67$$



# Cash on Cash (CoC)



All In Cash =

- Down Payment +
- Closing Costs +
- Acquisition Fee



$$\text{CoC} = \frac{\text{NOI} - \text{Debt Service}}{\text{All In Cash}}$$

# Example: CoC Calculation



What is the CoC Return of the following investment?



- Purchase Price = \$10M
- Annual Income = \$1.3M
- Annual Expense = \$500,000
- Debt Service = \$480,000
- Down payment (25%) = \$2.5M
- Closing costs (1%) = \$100,000
- Acquisition Fee (5%) = \$500,000
- NOI = 1,300,000 – 500,000 = 800,000

$$\text{All In Cash} = \text{Down Payment} + \text{Closing Costs} + \text{Acquisition Fee} = \$3.1\text{M}$$
$$2,500,000 + 100,000 + 500,000$$

$$\text{CoC} = \frac{\text{NOI} - \text{Debt Service}}{\text{All In Cash}} = \frac{800,000 - 480,000}{3,100,000} = \frac{320,000}{3,100,000} = 10.3\%$$

# The Holy Trinity



- The first “make or break” filters for a deal
- Represents the interest of the various stakeholders of the deal

Cap  
Rate



**DEAL SPONSOR /  
GENERAL PARTNERS**

DCR



**BANK /  
DEBT PARTNERS**

CoC



**INVESTORS /  
EQUITY PARTNERS**



# Before You Start Analyzing Properties...

Formulating Your Investment Strategy

## WHAT ARE YOUR MARKET DEMOGRAPHICS?

- **Location:**
  - Primary, Secondary, Tertiary markets
  - Jobs
  - Population
- Median Household Income > 40k
- Landlord Friendly State? **YES Please!**
- Price to Rent Ratio? **14 to 23**
- Distance from Home < **3 hour by Car or Plane**

## ... AND PROPERTY CHARACTERISTICS?

- Class A, B or C
- Year Built
- Roof & Construction Type
- General Size (# units)
- Any special tenant focus?
  - Student, Senior, Government Funded
- Condition : Distressed, Heavy Lift or Cosmetic Only



# Our Value Add Strategy



## COMMUNICATE WITH YOUR TEAM AND BROKER

1. We buy B and C Class apartment communities, primarily 1975 vintage and younger, 120+ units in very specific Metros and Neighborhoods;
2. We seek Value Add projects that are from cosmetic upgrades through heavy lift, assuming right local team is on the ground.
3. We implement a business plan to improve operations by increasing income and decreasing expenses through careful asset management
4. Our plan is to sell the property after it is stabilized at the optimum time in the market
5. Then we do it again: Rinse and Repeat



# Getting a Listing



- Looks like this.
- Sign the Confidentiality Agreement to get access to the property's docs.



## EXCLUSIVE OFFERING Maryland LIHTC Portfolio

Germantown, Olney, Silver Spring, Edgewater, North East | Maryland

Rare opportunity for investors to make a large scale investment in affordable housing. The Portfolio contains five senior communities with excellent amenities and access to public transportation.

- 438-unit portfolio in D.C. and Baltimore suburbs
- Developed under the tax credit program between 2004-2006
- In-place rents 12% below maximum allowable tax credit rents

Offering Summary

[SCHEDULE A TOUR](#)

[SIGN THE CA](#)

Sign the Electronic CA to view the Due Diligence

# What's In the Package: Things You'll Need



## OPERATING MEMORANDUM (AKA. OM)

- Tells you quite a bit about the property
- This is a marketing brochure!!



## RENT ROLL



## T12 (AKA. Trailing 12 Months' Income & Expenses)

- There's also T3, T6



# Offering Memorandum (OM)



## PROPERTY ADDRESS

Use to Research Crime, Flood Zones...



## YEAR BUILT & RENOVATED

- Is it older than 1970? Additional Risk
- Was it recently renovated - how many units not renovated?



## ASKING PRICE

Not always listed



## TYPE OF CONSTRUCTION

And roofs



## UTILITIES

Who pays what?



## KEYWORDS

To look out for...



## NO. OF UNITS

Confirm with rent roll – Unit types and sizes

[OM Samples – Click Here](#)



# Look For Things That Matter to You



## LOCATION

- What are you near?
- What's happening around the area (new employers, new metro rails, etc)?
- What are the demographics in the immediate vicinity?
- What is the current tenant profile of this property?



## SOURCES

- Google Maps & Street View, Google Earth
- Crime Mapping – check several sources
- Better Business Bureau
- Zillow, RedFin, Trulia
- Local Tax Assessor's Office
- News – use alerts, local papers, follow major employers' news
- Broker – Brokerage reports
- Property Management Companies
- CoStar, AxioMetrics
- Local REIA clubs



# Rent Roll



**Sometimes, they're in PDF form.  
You'll want to convert into Excel.**

- Actual average rents / unit type
- Loss to Lease
- How long have tenants been at property
- What are the "proven" rents that are on record?
- And more

[Rent Roll Samples – Click Here](#)



# Trailing Expense: T12



## WHAT IS IT?

- Profit & Loss info about the Revenue & Expenses (There's also T3, T6)

## PAY ATTENTION:

- Trends – are there unexpected expenses out of norm?
- Missing expenses
- Anything in particular looking high / out of place

**T12 TELLS A LOT IN A STORY OF THE PROPERTY**

[T12 Samples – Click Here](#)



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# Income: Putting It Together



			<b>Seller T12</b>
<b>GROSS POTENTIAL RENTS (GPR)</b>	<b>INCOME</b>		
<b>ECONOMIC VACANCY</b>	<b>Gross Potential Rents</b>		\$1,765,800
<b>LOSS TO LEASE</b>	- Economic Vacancy	22.5%	\$396,800
<b>PHYSICAL VACANCY</b>	Loss to Lease	15%	\$267,800
<b>BAD DEBT</b>	Vacancy	3%	\$57,000
<b>CONCESSIONS</b>	Bad Debt	3%	\$60,000
<b>UTILITY REIMBURSEMENT (RUBS)</b>	Concessions	1%	\$12,000
<b>OTHER INCOME</b>	<b>Net Rental Income</b>	78%	\$1,369,000
<b>EFFECTIVE GROSS INCOME (EGI)</b>	Utility Reimbursement	4%	\$72,000
	Other Income	5%	\$82,000
	<b>Effective Gross Income (EGI)</b>		\$1,523,000



# Expenses: Putting It Together



PROPERTY MANAGEMENT
PAYROLL
GENERAL / ADMIN
ADVERTISING / MARKETING
MAKE-READY
REPAIRS & MAINTENANCE
CONTRACT SERVICES
UTILITIES
PROPERTY TAXES
INSURANCE
RESERVES

OPERATING EXPENSES				
	<u>Item</u>	<u>Total/Year</u>	<u>Per Unit/Year</u>	<u>% of EGR</u>
	Property Management	\$38,485	\$428	3.00%
	Payroll	\$108,000	\$1,200	
	General & Administrative	\$18,000	\$200	
	Advertising & Marketing	\$13,500	\$150	
	Unit Turnover	\$18,000	\$200	
	Repairs & Maintenance	\$45,000	\$500	
	Contract Services	\$15,750	\$175	
	Utilities	\$69,750	\$775	
	Utility Reimbursements (RUBS)	\$31,500	\$350	
	Property Taxes	\$126,000	\$1,400	
	Insurance	\$31,500	\$350	
	Capital Expense Reserves	\$31,500	\$350	
	<b>Total</b>	<b>\$546,985</b>	<b>\$6,078</b>	<b>42.64%</b>



# Expenses: Rule of Thumb



<b>TAXES</b>	80% of Purchase Price x Mill Rate = Taxes
<b>INSURANCE</b>	\$250 / Door
<b>REPAIRS &amp; MAINTENANCE</b>	\$300-600 / Door
<b>GENERAL / ADMIN</b>	\$100-250 / Door
<b>MANAGEMENT</b>	% of Total Collected Income. Typically 4% for larger properties
<b>MARKETING</b>	\$100-250 / Door
<b>UTILITY</b>	Use Last Year's & Annualize this year's. Take highest value
<b>CONTRACT SERVICES</b>	\$200-400 / Door
<b>PAYROLL</b>	\$700 - \$1,000 / Door**
<b>CAPITAL EXPENDITURES</b>	\$250-300 / Door

*These numbers are general rules of thumb – each market may vary significantly from these ROT.*

# Pro Forma: Your Business Plan



- T-12 data is called the “actuals”
- The Pro Forma is your business plan of what your income and expenses are Projected to be over the next 5 to 10 years, based on your Research and Rules of Thumbs
- Key to your Proforma are your INCOME assumptions...

Rental Income	Year 1	Year 2	Year 3	Year 4	Year 5
GPR					
LTL					
Total GR					
Concessions					
Vacancy					
Employee Units					
Model					
Bad Debt					
Other Income					
EGI					
Expenses	Year 1	Year 2	Year 3	Year 4	Year 5
Payroll					
Maintenance					
Contract Services					
Turn/ Make Ready					
Advertising					
Admin					
Utilities					
Mgmt. Fees					
Taxes					
Reserves					
Insurance					
Total Expenses					
NOI					
Debt Service					
Asset Mgmt. Fee					
Cash Flow					

# Value-Add: Forcing Appreciation



Updating Exteriors & Renovating Units can **add tremendous value**

## 1. Figure Out Your “Value Add” Business Plan

- What level of renovations for interior?
- What level of renovations for exterior?
- Other Opportunities?

## 2. Determine your Cap Ex Budget and Timeline


- **Exterior:** Roofs, Repaving, New Signage, Green Program...
- **Interior:** As tenants move out, renovate unit and raise rent to market



# Underwriting Models

- [Multifamily University Deal Analyzer v1.6](#)
  - Good, basic teaching model. Great place to start.
  - [Watch Demo on How to Use](#)
- [Multifamily University Quick Deal Analyzer](#)
  - Quick and Dirty to find out if you should dive deeper
- [Multifamily University + Enodo Deal Analyzer v2](#)
  - More advanced model Includes Multiple Scenarios, Supports Refinance and Waterfalls. Best for underwriters with some experience. Does not require Enodo Subscription
- Additional Value Add Deal Analyzer Recommended for Beginner & Intermediate to more Advanced:
  - [Michael Blanks Underwriting Model](#) (\$129)
  - [Spencer Burton ACRE](#) (Free but pay something)
  - [Rob Beardsley Lonestar Capital](#) (Free but Join Newsletter to Download)

**MULTIFAMILYU QUICK DEAL ANALYZER**



[become a multifamily expert](#)

	Avg Cash on Cash	IRR	EMx	Avg Annualized
Project	12.0%	27.4%	2.9X	38.3%
Investor	8.4%	17.3%	2.0X	20.8%

OVERVIEW & ASSUMPTIONS		DISPOSITION & RETURNS	
<b>Purchase &amp; Sale Assumptions</b>		<b>\$/Unit</b>	
Purchase Price	\$ 9,500,000	Sale Price	\$ 97,813
Cap Rate (Year 1)	8.9%	Disposition Costs	\$ (2,445)
Closing Costs	3.50% \$ 332,500	Disposition Fee	\$ -
Reserves at Close	\$675/unit \$ 117,450	Debt Defeasance	\$ (39,414)
Hold Period	5 Years	Net Proceeds	\$ 55,954
Sale / Exit Cap Rate	6.0%		
Sale Costs	2.5%		
<b>Operating Assumptions</b>			
Revenue Growth Rate	3.0%		
Expense Growth Rate	3.0%		

RENT ROLL							
Unit Type	Count	SF	Current (\$)	Market (\$)	Premium Count (Optional)	Premium Incr (Optional)	Premium Market Rent (\$)
1 bd / 1 ba	18	596 SF	\$ 700	\$ 725	14	\$ 75	\$ 800
2 bd / 1.5 ba	102	930 SF	\$ 795	\$ 825	76	\$ 100	\$ 925
3bd / 1.5 ba	54	1125 SF	\$ 875	\$ 925	40	\$ 125	\$ 1,050
<b>Total</b>	<b>174</b>	<b>166,338 SF</b>	<b>\$ 140,940</b>	<b>\$ 147,150</b>	<b>130</b>	<b>\$ 13,650</b>	<b>\$ 123,500</b>

DEBT STRUCTURE (Optional)		ESTIMATED CASH FLOWS			
Loan to Value	75.0%	<b>Revenues</b>	<b>Input (Annual)</b>	<b>Year 1</b>	<b>\$/Unit</b>
Loan Amount	\$ 7,125,000	GPR	\$ 1,765,800	\$ 10,148	\$ 2,002,339
Interest Rate	3.75%	Loss to Lease	\$ (49,680)	\$ (286)	\$ -
Amortization	30 Years	Vacancy	\$ (141,264)	\$ (812)	\$ (160,187)
Interest Only Period in Years	3 Years	Other Income	\$ 125,000	\$ 718	\$ 140,689
Debt Coverage Ratio (DSCR) Yr 1	3.2X	EGR	\$ 1,699,856	\$ 9,769	\$ 1,982,841

DEAL STRUCTURE (Optional)		ESTIMATED CASH FLOWS (Continued)			
Sponsor Compensation	30% 70% Investors	<b>Expenses</b>			
Hurdle / Investor Pref	0.0%	Management	5.0%	\$ (84,993)	\$ (488)
Acquisition Fee	3.0%	Payroll	\$ 35,296	\$ (35,296)	\$ (203)
Asset Mgt Fee	2.0%	Admin	\$ 11,996	\$ (11,996)	\$ (69)
Renovation Mgt Fee	0.0%	Marketing	\$ 600	\$ (600)	\$ (3)
Disposition Fee	0.0%	Maintenance	\$ 14,390	\$ (14,390)	\$ (83)
		Contract Services	\$ 10,743	\$ (10,743)	\$ (62)
		Utilities	\$ 35,696	\$ (35,696)	\$ (205)
		Insurance	\$ 6,400	\$ (35,696)	\$ (205)
		Property Taxes	\$ 9,321	\$ (9,321)	\$ (54)
		Other	\$ 1,864	\$ (1,864)	\$ (11)
		<b>Total Op Exp</b>	<b>\$ (849,928)</b>	<b>\$ (4,885)</b>	<b>\$ (991,420)</b>
		Op Ex Ratio	50%	50%	50%
		<b>Net Op Inc</b>	<b>\$ 849,928</b>	<b>\$ 4,885</b>	<b>\$ 991,420</b>
		Asst Mgt.	\$ (33,997)	\$ (195)	\$ (39,657)
		Reserves	\$ (50,996)	\$ (293)	\$ (59,485)
		Debt Service	\$ (267,188)	\$ (1,536)	\$ (420,029)
		<b>Cash Flow</b>	<b>\$ 497,748</b>	<b>\$ 2,861</b>	<b>\$ 472,249</b>

RENOVATION COSTS (Optional)		MARKET DEMOGRAPHICS (Optional)	
Item	\$	\$/Unit	
Interior	\$ 650,000	\$ 5,000	
Exterior	\$ 350,000	\$ 2,011	
Contingent (10%)	\$ 100,000	\$ 575	
<b>Total</b>	<b>\$ 1,100,000</b>	<b>\$ 6,322</b>	
Renovation Mgt Fee	\$ -	\$ -	
<b>Total Costs</b>	<b>\$ 1,100,000</b>	<b>\$ 6,322</b>	
			Median Household Income
			Population Growth
			YOY Job Growth

SOURCES & USES					
Sources	\$	\$/Unit	%	Uses	\$
Debt	\$ 7,125,000	\$ 40,948	62.9%	Property	\$ 9,500,000
Equity	\$ 4,209,950	\$ 24,195	37.1%	Construction	\$ 1,100,000
				Reserves	\$ 117,450
				Acq Fee	\$ 285,000
				Closing Costs	\$ 332,500
<b>Total</b>	<b>\$ 11,334,950</b>	<b>\$ 65,143</b>	<b>100.0%</b>	<b>Total</b>	<b>\$ 11,334,950</b>



# Underwriting Logistics



## HOW DO YOU DECIDE WHICH DEALS TO UNDERWRITE?

Filter with Demographics

## SOURCES FOR CITY & MICRO-NEIGHBORHOOD DEMOGRAPHICS

For METRO :

- Yardi Reports, CoStar Market Report, [Local Market Monitor](#)
  - [www.localmarketmonitor.com](http://www.localmarketmonitor.com) : [SAMPLE REPORTS](#)

[neighborhoodscout.com](http://neighborhoodscout.com)

For MICRO-NEIGHBORHOOD :

- City-data.com, InvestReal.com, [Neighborhood Scout](#)
  - [www.](http://www.) : [SAMPLE REPORTS](#)



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# Things You Need to Underwrite a Property



BESIDES the OM, T12 and Rent Roll –  
what do you need to underwrite a property?

**SOURCES:**  
Property  
Managers  
&  
Boots on the  
Ground

## PROPERTY SPECIFIC

### INCOME & EXPENSES

- Market Rent
- Premium Rent Post Renovation
- Additional Sources of Other Income?
- Validation of Operating Expenses
  - Property Tax, Insurance Quotes

### CAPEX BUDGET

- Condition of Property (roofs, mechanicals)
- Renovation plan for Units & Cost
- Renovation plan for Exterior & Cost
- Missing Amenities or Hidden Upsides to increase Rent



# Things You Need to Underwrite a Property

## FOR THE MARKET AND NEIGHBORHOOD

- Market Vacancy
- Forecasted Rent Growth
- Sales Comps
- Rent Comps
- New construction / Incoming Units



**SOURCE:**  
“Full Underwriting Report”  
from CoStar

Underwriting Report

**100 Knight Way**

Weatherly Walk

194 Unit Apartment Building

Fayetteville, Georgia - Fayette County Neighborhood

PREPARED BY



Megan Turner



[SAMPLE  
REPORTS](#)

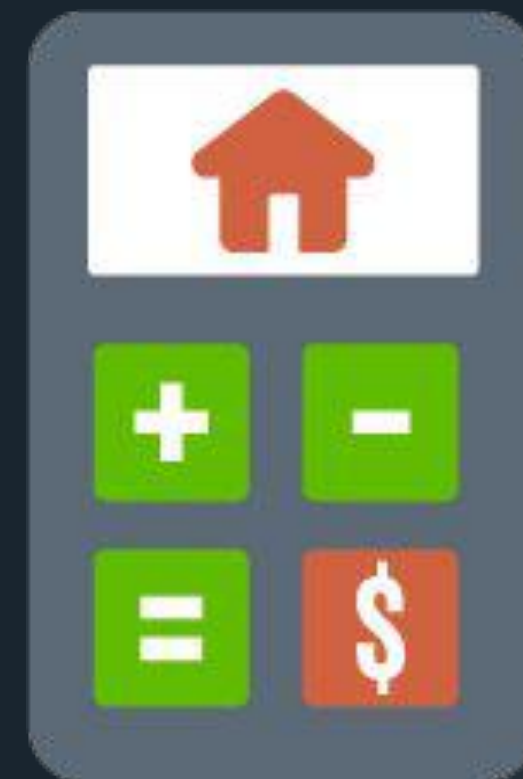


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# Things You Need to Underwrite a Property

## FINANCE TERMS TO UNDERWRITE THE DEAL

- Max Loan Amount
- Term for Loan
- Interest Rate
- Max LTV
- Minimum DSCR
- Interest Only Period
- Prepayment Terms
- Include Capex in Loan?



PRODUCT	Fixed – 10 yrs
Purchase Price	\$61,000,000
Loan Amount	\$40,840,000
Term	10 Years
Interest Only	5 Years
Amortization	30 Years
Recourse	Non-Recourse
Maximum LTV	70% LTV ~ 66.9% actual
Minimum DSCR	1.25x DSCR
Prepayment	Defeasance
Index	10 YR UST
Spread	2.50%
<b>TOTAL RATE</b>	<b>3.25%</b>

**SOURCE:**  
Lenders,  
Debt Brokers,  
Community  
Banks

Watch : [Webinar on Multifamily Lending with John Brickson of Old Capital Lending](#)

# Your Turn: Underwriting Lab



## UPLOAD ANALYZER into Excel or GOOGLE SHEETS

- Use Financials provided in Student Folder - [UW Lab -The Hamlins](#)
- It is partially filled out for you. For this lab, only fill in the ORANGE shaded cells



## FILL IN ANALYZER

- Go as far as you can – work in teams or solo
- Work on this exercise as homework. A solution is posted in the folder. Note that the demographic data in the solution may be different than yours.
- Note if you were to do current rent comp evaluation, it would also be different from when these comps were put into the model.

# Underwriting Logistics



ONCE YOU HAVE UNDERWRITTEN THE DEAL...

HOW DO YOU KNOW WHICH DEALS ARE “GOOD” TO MAKE OFFERS ON?

- What is your investment criteria?
- What do you want to return to your investors?
  - 8 - 10% Cash on Cash
  - 15 to 17% IRR for 5 yr deal (will be lower for longer deals)
  - >18.5% Simple Annualized Return
  - >1.9x Equity Multiple over 5 Years



# Calculating Returns: Evaluating the Deal



## KEY INVESTMENT METRICS

- Cash on Cash (CoC)
- Simple Annualized Return

➔ Go to: [Lab Cash on Cash](#)



# Calculating Returns: Evaluating the Deal



## KEY INVESTMENT METRICS

- Internal Rate of Return (IRR)
- Equity Multiple (EM)

➔ Go to: [Demo IRR & EM](#)



# Offer Price: How Did You Come Up With It?



You have a deal that looks good – How do you know what to offer?

## 1. GO BACK TO YOUR INVESTMENT GOALS

- Adjust the offer price until returns meet your objectives.

## 2. CREATE DIFFERENT PRICE SCENARIOS AND NOTE RETURNS FOR EACH

- Initial offer should be a lower price – not the only one that works for you.



## GP / LP Compensation Parameters

GP %	30%
LP %	70%
Asset Mgmt Fee (% of total income)	2.0%

## Return Summary

LP AVERAGE ANNUAL RETURN	20.67%	0
LP TOTAL IRR	17.27%	
LP AVG CASH FLOW %	9.27%	

	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5	TOTAL
Cash Flow Before Tax Flow	-\$5,774,488	\$696,899	\$836,083	\$950,837	\$787,295	\$821,143	
- Asset Mgmt Fee		\$48,504	\$51,809	\$54,790	\$56,159	\$57,563	\$268,826
NET PROJECT CASH FLOW	-\$5,774,488	\$648,394	\$784,274	\$896,048	\$731,135	\$763,580	
- Cash Flow To GP		\$194,518	\$235,282	\$268,814.25	\$219,341	\$229,074	\$1,147,029
NET LP CASH FLOW		\$453,876	\$548,992	\$627,233	\$511,795	\$534,506	\$2,676,401
LP CASH FLOW RETURN %		7.86%	9.51%	10.86%	8.86%	9.26%	
Net Sales Proceeds							\$11,624,294
Total LP Cash flow							\$2,676,401
Remaining Initial Capital to be Returned							\$3,098,087
Net Sales after Initial Capital Returned							\$8,526,207
GP Cut from Net Sales							\$2,557,862
LP TOTAL RETURN (Sale Yr 5)							\$5,968,345
LP CASH FLOW (INCLUDING SALES)	-\$5,774,488	\$453,876	\$548,992	\$627,233	\$511,795	\$9,600,938	

# DEAL STRUCTURE : WHAT % DO YOU TAKE?

Three ways to structure the deal for Limited and General Partners



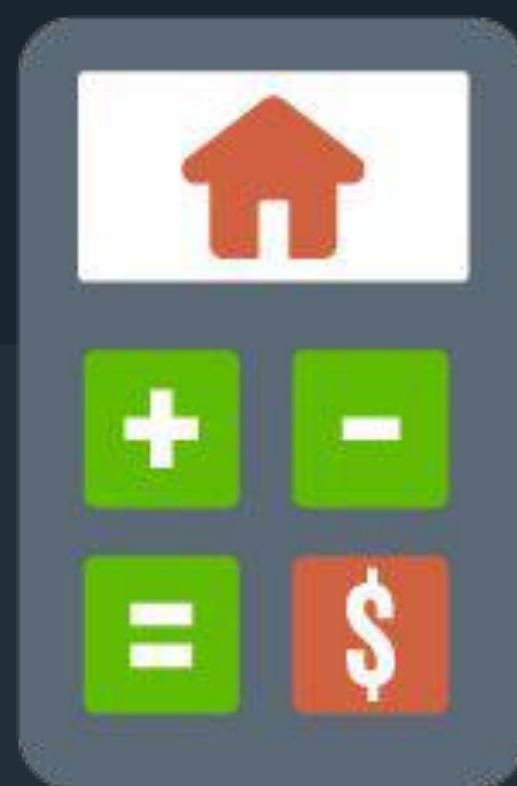
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# Syndicate Splits: Straight Returns



## pa·ri pas·su

- /ˌpärēˈpäsōo/
- Pari-passu is a Latin phrase meaning "equal footing" that describes situations where two or more assets, securities, creditors or obligations are equally managed without preference.



### STRAIGHT RETURNS:

- Set ratio where investor and sponsor share the returns with no prefs - 70/30, 80/20, 85/15...
- Sponsor makes amount specified in split ratio (30, 20 or 15)



# Syndicate Splits: Returns with Pref



## PREF WITH TRUE UP

- 70/30 split with 8 Pref is most common.
- Investor gets first 8% each year, but sponsor is “made whole”



## PREF WITH NO TRUE UP

- Same 70/30 split with 8 Pref where first 8% goes to investor
- Sponsor makes 30% of the profits AFTER the 8%

## For any model, HURDLES can be added:

- If deal achieves specified goal, ratio changes above that
  - After 20% hurdle, any profits above that is split is 50/50 – applies on sale as bonus to sponsor for exceeding numbers



# Syndicate Splits: Comparing All Three



	Straight Returns 70 / 30	70/30 8% Pref w True Up	70/30 8% Pref w No True Up
Sample Returns for \$100	\$100	\$100	\$100
8% pref for 5 years	N/A	\$40	\$40
Profit after Pref	\$100	\$60	\$60
Profit to LP after Pref	N/A	\$30	\$42
Total Profit to LP	\$70	\$70	\$82
Total Profit to GP	\$30	\$30	\$18
Go to: <a href="#">Demo &amp; Lab</a>	<p>GP gets whatever % was established as their share: pari passu</p> <p>More common splits for this model are 80/20 or 85/15 for the current deals to hit attractive returns for investors</p>	<p>8% pref x 5 years= \$40 to LP. Then the remaining profit of \$60 is split so that the total to GP is \$30% of profits, assuming project has profits above the pref.</p>	<p>8% pref x 5 years= \$40 to LP. After pref, LP gets additional \$42 which is 70% of \$60 profits. The \$18 remainder of profits goes to GP because there is no true up</p>

# Value-Add: Exit Strategy



$$\text{Current Value} = \frac{\text{NOI}}{\text{Cap Rate}}$$

## WHEN IS IT BEST TO SELL THE PROPERTY?

- Business Plan / Investment Goal Achieved
- Market Conditions, Loan Conditions
- Consider leaving some renovations for next owner

## EXIT CAP RATE

- Take the Cap Rate, add an "accelerator" expressed in bps per year
- EXAMPLE - What will be Exit Cap Rate in Y3?
- Cap Rate at Purchase = 6%
- Cap Rate Accelerator = .10 bps
- Exit Cap Rate yr 3 =  
 $6.00\% + .10 + .10 + .10 = 6.3\%$



# Value-Add: Example



## WE BUY A BUILDING...

- Purchase Price = \$10M
- Annual Income = \$1.1M
- Annual Expense = \$500,000
- NOI = \$1,100,000 - \$500,000 = **\$600,000**

$$\text{CapRate @ 10M} = \frac{600,000}{10,000,000} = 0.06 = \mathbf{6\%}$$

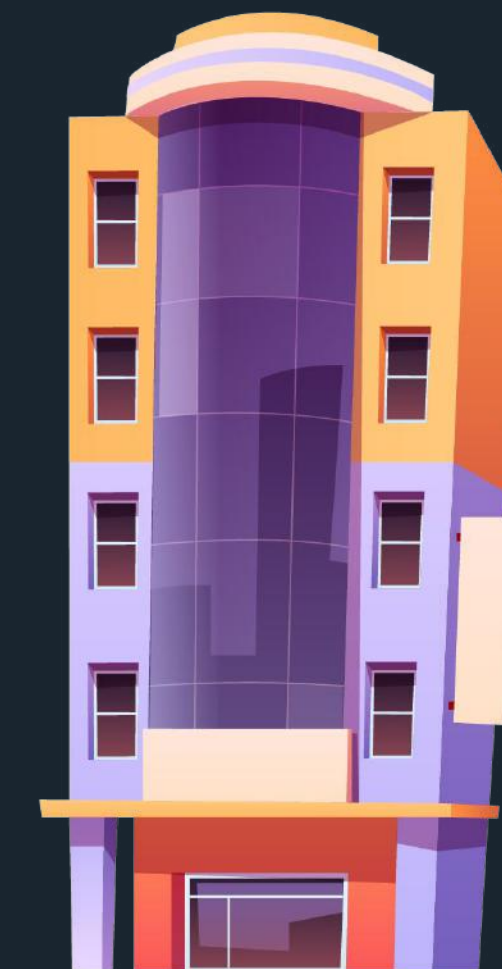


## If we implement Value Add business plan over 2 years...

- Annual Income = \$1.25M
- Annual Expense = \$450,000
- Exit Cap Rate = 6.2%
- NOI = \$1,250,000 - \$450,000 = **\$800,000**

$$\text{Property Value} = \frac{\text{NOI}}{\text{Cap Rate}} = \frac{800,000}{.062} = \mathbf{\$12,903,226}$$

**\$2.9M Value Added**



# Value-Add: Example



We're managing our 200 unit building....

- Purchase Price = \$10M
- Annual Income = \$1.1M
- Annual Expense = \$500,000
- NOI = \$1,100,000 - \$500,000 = **\$600,000**

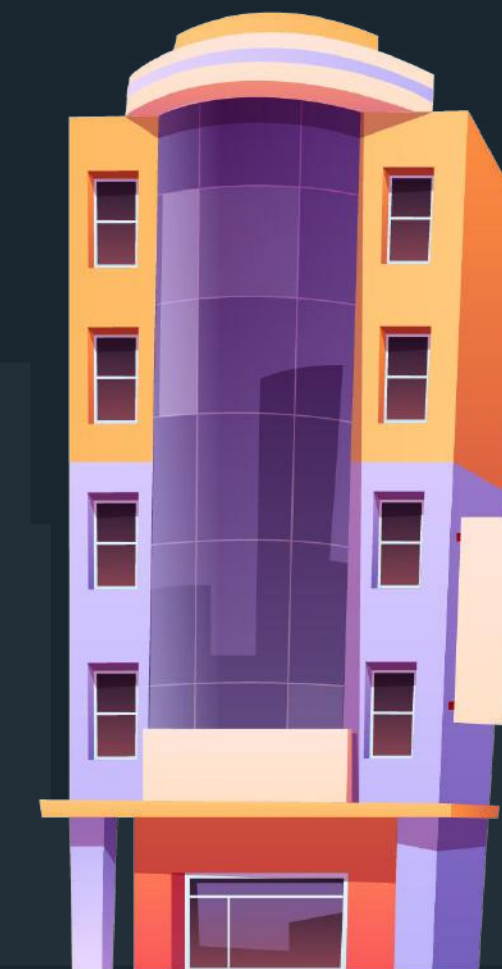
$$\text{CapRate @ 10M} = \frac{600,000}{10,000,000} = 0.06 = \mathbf{6\%}$$

We're not paying attention. Expenses are creeping up...

- Annual Income = \$1.2M
- Annual Expense = \$680,000
- Exit Cap Rate = 6.2%
- NOI = \$1,200,000 - \$680,000 = **\$520,000**

$$\text{Property Value} = \frac{\text{NOI}}{\text{Cap Rate}} = \frac{520,000}{.062} = \mathbf{\$8,387,096}$$

**\$1.6M Value Lost**





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# DUE DILIGENCE AND REHAB BUDGETS

Let's Get Physical – Both Before and After Buying the Property

# Due Diligence: What Is It?



It's the process of doing **financial and physical inspections** of the property to understand the property condition and determine the internal and external rehab budget. It is conducted both before and after making an offer.



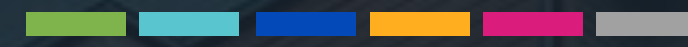
Due diligence is always conducted in partnership with a local property manager. This is usually the same property manager that went in with you to **walk the property** during the offer stage. Having a PM that knows the area, property type and typical rehab levels is critical to your success



Age of the property affects everything. The Due diligence for a property built in the late 80s is a lot simpler than a property built in the 60s and 70s



# Physical Due Diligence



The PM and you will **walk through every single unit** at the property. The PM comes ready with a checklist that is used to determine the condition of each unit and build a rehab budget. Each unit's key areas are graded, with kitchen being the biggest focus.



**Key common areas to walk** are roofs, parking areas, pools, clubhouse, laundry rooms, gyms, boiler rooms, chiller rooms, HVAC units etc. it's also important to walk the 'drive-in to clubhouse' to see issues with tree trimming, road surfaces, broken blinds. Walk around the entire property.



**Roofs and HVAC** are really important elements. Make sure that your PM is bringing in specialists for those. For properties in the 60's and 70's, you also need a plumbing specialist and a foundation specialist.



# Physical Due Diligence: Cost and Time



A lot of property managers **will not charge you** for physical due diligence if you go with them, should you win your bid. Others will charge \$20 to \$35 per unit, which is a reasonable fee.

**Rule of thumb** is that every 100-120 units takes a day. So one day for a property of that size, two days for a property up to 240 units, and 3 days for a property that is larger.

**Never accept a reason to not enter a unit.** E.g. keys are missing or tenant did not want us to enter. Always schedule the PM to come back. Generally, those are the units with big damage – mold, water damage (or they have 3 ferocious pitbulls in there).



# Physical Due Diligence: Best Practices



**Read the property's reviews** on Google, Yelp and Apartment.com. Do they suffer from cockroaches? Bedbugs? Is the water shut off often (all buildings have a single shut off – big issue). Do roofs leak? Is there condensation during wet weather?

**There are now iPad apps such as INSPECTOR.** These allow you to take pictures of units as you go, and allow you to quickly add unit numbers and tap sub-categories such as Kitchen Cabinet to rank the condition. Highly recommended.

**Always walk at least 5 properties in a one-mile radius** to understand their level of rehab. Over-rehabbing and under-rehabbing are two very common problems that should be avoided.



# External Rehab: Typical Areas to Focus On



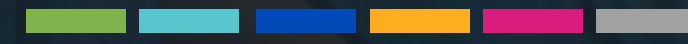
**Best bang for the buck for external rehab** comes from painting, repaving parking lots, installing LED lighting, upgrading clubhouses and pool areas, building dog runs.

**Allocate money for Roofing and HVAC upgrades and plumbing fixes.** These are inevitable costs. Note that the bank will force you to keep a Capex budget per unit per year, so some of the Capex can come from that budget.

Tree trimming, security cameras, property fencing and monument signs are **other good upgrades with both functional and aesthetic benefits.**



# Rent Growth

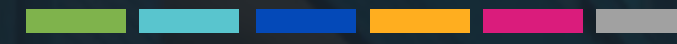


## RENT GROWTH IN A MARKET IS BASED ON...

- Supply/Demand
- Population Growth
- Job Growth
- Supply
  - Cost of Alternatives
  - Single Family Home Prices
  - Rent Vs Buy Ratio



# Rent Growth



## SOURCES FOR PROJECTED RENT GROWTH

- Yardi Historical Market Reports
- Local Market Monitor Method





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# HOW TO FIND RENT COMPARABLES

No Method is Perfect, But If You Do Them Together, They're Pretty Darn Accurate

# Rent Comp Research



## Rental Comparable Analysis or Rent Comps is an Iterative Process

**Step One:** Online research for STAGE ONE of your analysis

- Build list of similar properties (Sources: Broker, PM's, Online Research)
  - Year Built or Vintage
  - Distance from property
  - Number of Units
  - Unit Types and Sizes in terms of Square Footage
  - Classic or Renovated? If renovated, when?
  - Amenities
- Once properties identified, use paper/excel to build out comparison matrix
  - [See Rent Comp & Amenities Tab in Resources for MultifamilyU UW File](#)



# Method #1: PadMapper



**Padmapper** is a google Maps mashup that provides rent comps in an easy to use visual interface.

1. Go to [Padmapper](#).
2. **Select the city that you want rent comps for.** Then draw a shape using the DRAW button on the top right. Drawing is recommended to target the specific area of the subject property.
3. In the FILTERS box, select APARTMENT, select EXCLUDE AIRBNB and select LONG TERM. Create an excel table for yourself with the following information:
  - Property address
  - Rent Price
  - Number of beds and baths
  - Size (Square feet)
  - \$\$ per square foot
  - Number of units (if available, you can also google the property address to get this info)
  - Amenities, if any (hardwood floors, pool, steel appliances, all-bills-paid etc.)
  - Rating of 1 to 5 from the pictures, 1 being best.
  - Click on the apartment address. In the next screen, you can also see a Google Street view.



# Method #2: craigslist



You can get rent comps manually on **craigslist**. Do not underestimate the value of this process. Just create a table for yourself with the following information and plug in the zip code that you want comps for.

- Property address
- Number of units
- Price
- Size (Square feet)
- \$\$ per square foot
- Amenities, if any (hardwood floors, pool, steel appliances, all-bills-paid etc.)
- Rating of 1 to 5 from the pictures, 1 being best.



# Method #3: RENTRANGE®



**RentRange** provides fantastic rental property analysis reports for \$14 a report, which is fantastic value for money. Information provided include:

- Rent estimate
- Vacancy levels
- Rental saturation
- Comps
- Rental trends by Bed count



## Method #4: Apartments.com™



**Apartments.com** is owned by CoStar. They interact with property managers and owners regularly to confirm their data. It is also a paid subscription service for property managers – overall data is very accurate for rental rates as well as availability and amenity details

- Input your market name
- In the filter bar at the top, set type to “apartments”
- You can further filter by “lifestyle”, price, #bedrooms
- Advanced Filters include Amenities to hone in on very close comps
- Fill in your matrix with data for similar properties



# Rent Comp Research: Next Steps



**Step Two:** Confirm online research by calling apartment community to verify info.

- Pretend you are a prospective tenant looking to rent...Year Built or Vintage
  - Pricing for each size unit (may require multiple calls)
  - Incentives or Rent Specials
  - Upgrades / Renovations (difference in pricing?)
  - Amenities for the property
  - Additional Charges – parking, pets, utilities

## WHAT'S NEXT?

Once in LOI or for sure during your Due Diligence period – VISIT the actual comp properties to do an additional level of confirmation of pricing





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# HOW TO FIND SALES COMPARABLES

Brokers that You Have Relationships With are Your Best Bet for Multifamily

# Method #1: Zillow<sup>®</sup>



Go to: [Zillow.com](https://www.zillow.com)

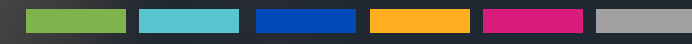
Type in the city or zip code that you want apartment sales comps for.

- In the LISTING TYPE box, uncheck everything except RECENTLY SOLD.
- In the price box, select 0 to 20,000,000
- In the beds box, select 6+
- In the Home type box, select APARTMENTS

Everything you are looking at are **sales comps for small apartments**. The list is, unfortunately, not comprehensive, but short of buying paid tools, this is a decent start.



# Method #2: Our Favorite – Leverage Broker Relationships



A lot of the bigger multifamily brokers have access to expensive tools like LoopNet, REIS, Costar or Axiometrics. These products have very detailed rent and sales comps.



If you have a relationship with a broker, they can send this information over to you. Its only a few minutes of work for them.

# Top 3 Common Pitfalls You Need to Avoid



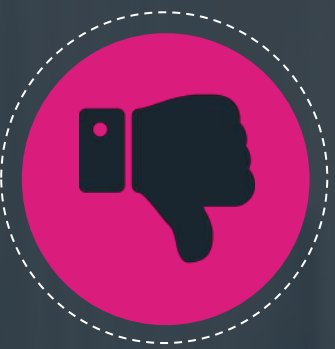
## NOT DOING SUFFICIENT ANALYSIS

- Accepting Offering Memorandum Financials as FACT
- Insufficient Property or Market Research



## RELYING ON APPRECIATION OF MARKET

- “Value Add” is the name of our game. There must be “forced appreciation” to move the needle. We Buy for Cash Flow.



## TOO MUCH RISK

- Taking on too much risk with your debt and/or inadequate cash reserves.



# Game Time!



Go to: [Game Time](#)

Rehab IRR NOI  
Delinquency  
Exit Cap Rate

**Apartment Analysis**  
**Economic Vacancy**

loss to lease Revenue  
Rent Growth  
CapEx DSCR **t12** Concessions  
Expense  
Cash on Cash  
Loan to Value rent roll **Cap Rate**  
**Underwriting**  
**MultifamilyU**  
**Monopoly**



# Exit Strategies: Flexible Options

Our Preferred Strategy is to Hold For 5 Years, Debt-free

	12 MONTH HOLD	24 MONTH HOLD	5 YEAR HOLD	5 YEAR HOLD (NO DEBT)
<b>Details</b>	<ul style="list-style-type: none"> <li>• Sell at Certificate of Occupancy</li> <li>• Pay off Const. Loan at time of Sale (12 months)</li> </ul>	<ul style="list-style-type: none"> <li>• Sell after 2nd Lease Up</li> <li>• Pay off Const. Loan at time of Sale (24 months)</li> </ul>	<ul style="list-style-type: none"> <li>• Refinance end of yr 2</li> <li>• Pay off Const. Loan</li> <li>• Hold for 3 more years</li> </ul>	<ul style="list-style-type: none"> <li>• Sell 3 fourplexes at Certificate of Occupancy</li> <li>• Pay off Const. Loan</li> <li>• Hold remaining 5 fourplexes for 4 more years DEBT-FREE</li> </ul>
<b>AAR</b>	52.05%	34.46%	21.56%	22.93%
<b>IRR</b>	55.69%	31.94%	24.41%	18.58%
<b>EM</b>	1.56x	1.72x	2.08x	2.15x

# Bonuses: Four Recent Grocapitus Projects



Underwriting Walkthroughs + Investment Summary



## WEATHERLY WALK

- Value-Add Multifamily Class B
- Atlanta, GA
- [Underwriting Walkthrough](#)
- [Investment Summary](#)



## STORAGE DEPOT

- Value-Add Self-Storage with New Construction
- West Memphis, AR
- [Underwriting Walkthrough](#)
- [Investment Summary](#)



## FALLS AT CRISMON FALLS

- New Construction Multifamily with Short-Term Rentals
- Mesa, AZ
- [Underwriting Walkthrough](#)
- [Investment Summary](#)



## UNIVERSITY OAKS

- New Construction Quadplexes with Multiple Exits
- Houston, TX
- [Underwriting Walkthrough](#)
- [Investment Summary](#)



# Commercial Financing: Basic Terms



## DEBT SERVICE

Includes Principal & Interest



## LTC VS LTV

Loan-to-Cost vs Loan-to-Value



## AMORTIZATION



## DSCR / DEBT YIELD



## INTEREST ONLY PERIOD



## APPRAISAL



➔ Go to: [Lab LTC, LTV, DSCR & Debt Yield](#)



# Opportunities in Multifamily Investing



RENOVATION RENTAL PREMIUMS



DECREASING OPERATING COSTS



COMPRESSION OF CAP RATE



ORGANIC RENTAL GROWTH



LOCATION GROWTH – PATH OF SUCCESS



# Risks in Multifamily Investing

