



MULTIFAMILY & SYNDICATION FUNDAMENTALS

Let's start the boot camp with the basics



Multifamily University



Our Goal for this Module

The Agenda

- ✓ Let's start with the big WHY and the HOW?
- ✓ Let's introduce you to the 2+ trillion-dollar U.S. MultiFamily market
- ✓ Talk about latest market trends driving MultiFamily growth
- ✓ Explain how groups of investors buy MultiFamily properties together
- ✓ Talk about all the basics and key terms of a syndication
- ✓ Discuss top reasons to invest in MultiFamily
- ✓ To go through the Lifecycle of a MultiFamily project
- ✓ Review

The big WHY and HOW

The 3 questions you must ask yourself when using Other People's Money



WHY

Why are investors looking to expand their portfolio beyond stocks and bonds?



WHY

Why must you help them seek higher yields?



HOW

How can you help them invest in real estate in a way that you benefit from the investment, without becoming the property manager, or rehabber?



The answer is staring us in the face

America's Social Security and retirement planning system was designed for a different reality, and there are 3 reasons for this

Reason #1: Life Expectancy



49 yrs. in 1900

You worked until the day you died

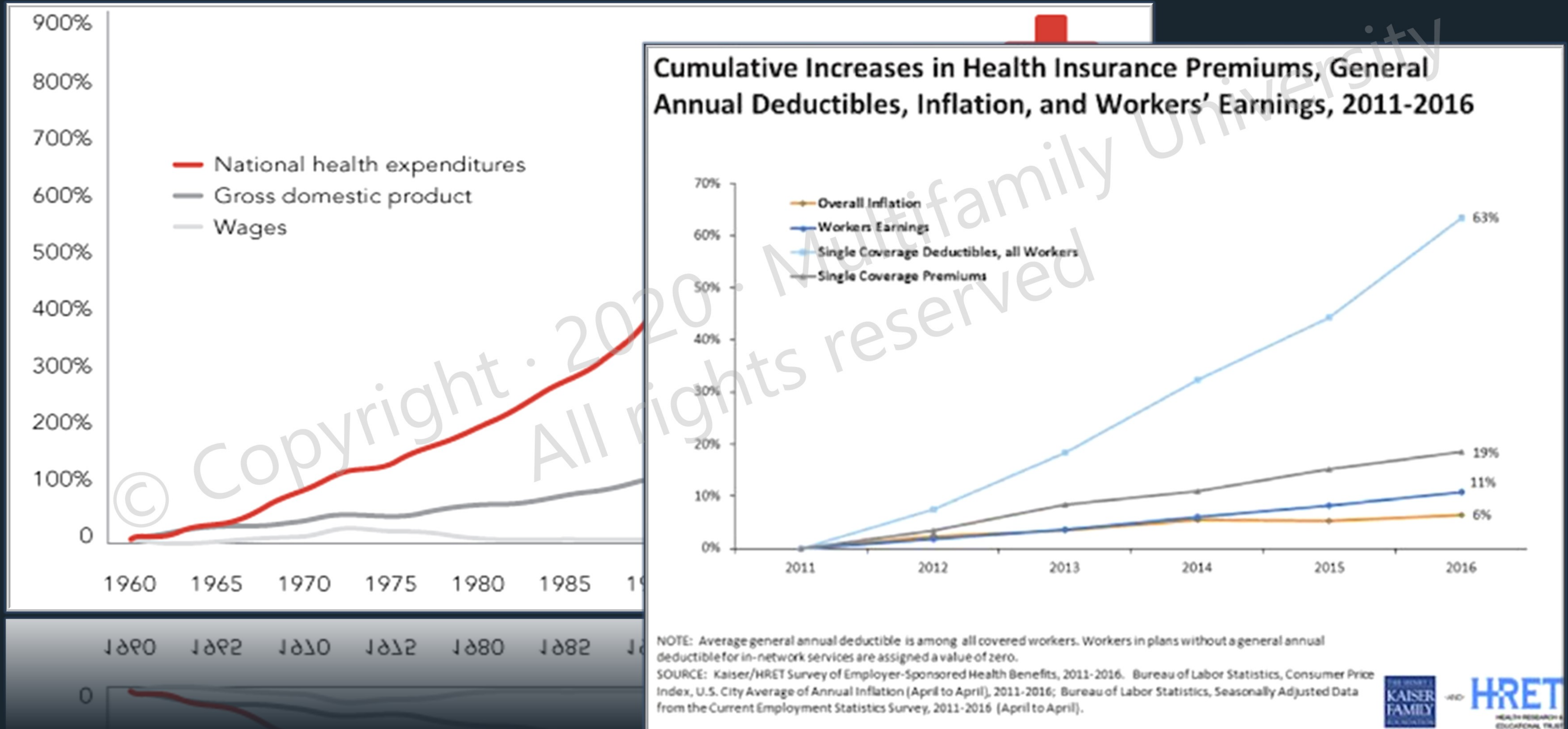
69 yrs. in 1960

Your retirement had to last a few years

79 yrs. and rising fast today

Your retirement has to last decades

Reason #2: Healthcare costs are rising far faster than inflation



Reason #3: Stock market returns adjusted for inflation are just too low to get ahead

What's the actual annual growth over the last 19 yrs., adjusted for inflation?



| Year and Return (%) | | Date Range | |
|---------------------|-------|---|---------------------|
| 2019 | 28.14 | Jan 1 | 2001 to Dec 31 2019 |
| 2018 | -6.20 | <input checked="" type="checkbox"/> Adjust for <u>Inflation</u> | |
| 2017 | 19.42 | <input checked="" type="checkbox"/> Include Dividends | |
| 2016 | 9.66 | <button>Calculate</button> | |
| 2015 | 0.58 | "Average" return: | 6.29 % |
| 2014 | 12.94 | Annualized return (= True CAGR): | 4.70 % |
| 2013 | 30.50 | Standard Deviation: | 17.23 % |
| 2012 | 13.91 | \$1.00 grew to: | \$ 2.39 |
| 2011 | -0.87 | | |
| 2010 | 13.14 | | |
| 2009 | 23.75 | | |
| 2008 | 27.28 | | |

Bottom line - \$1 invested in the stock market only doubled in the last 19 years, when adjusted for inflation

Calculator: http://www.moneychimp.com/features/market_cagr.htm

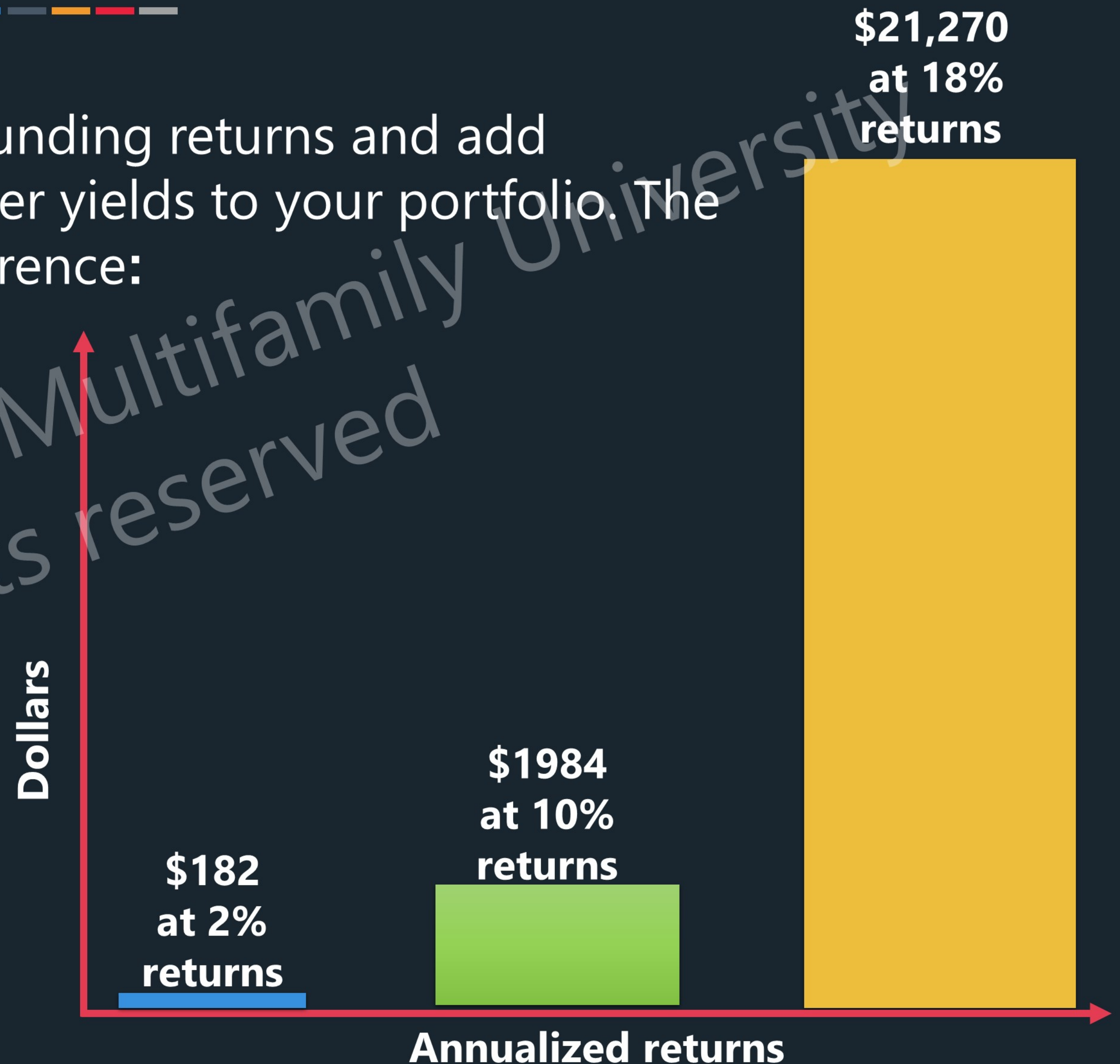
So what must you do to get your investors ahead?



Understand the Magic of compounding returns and add investments with potentially higher yields to your portfolio. The math shows the astonishing difference:



If you invest \$100 for 30 years at different levels of returns, what do you end up with?



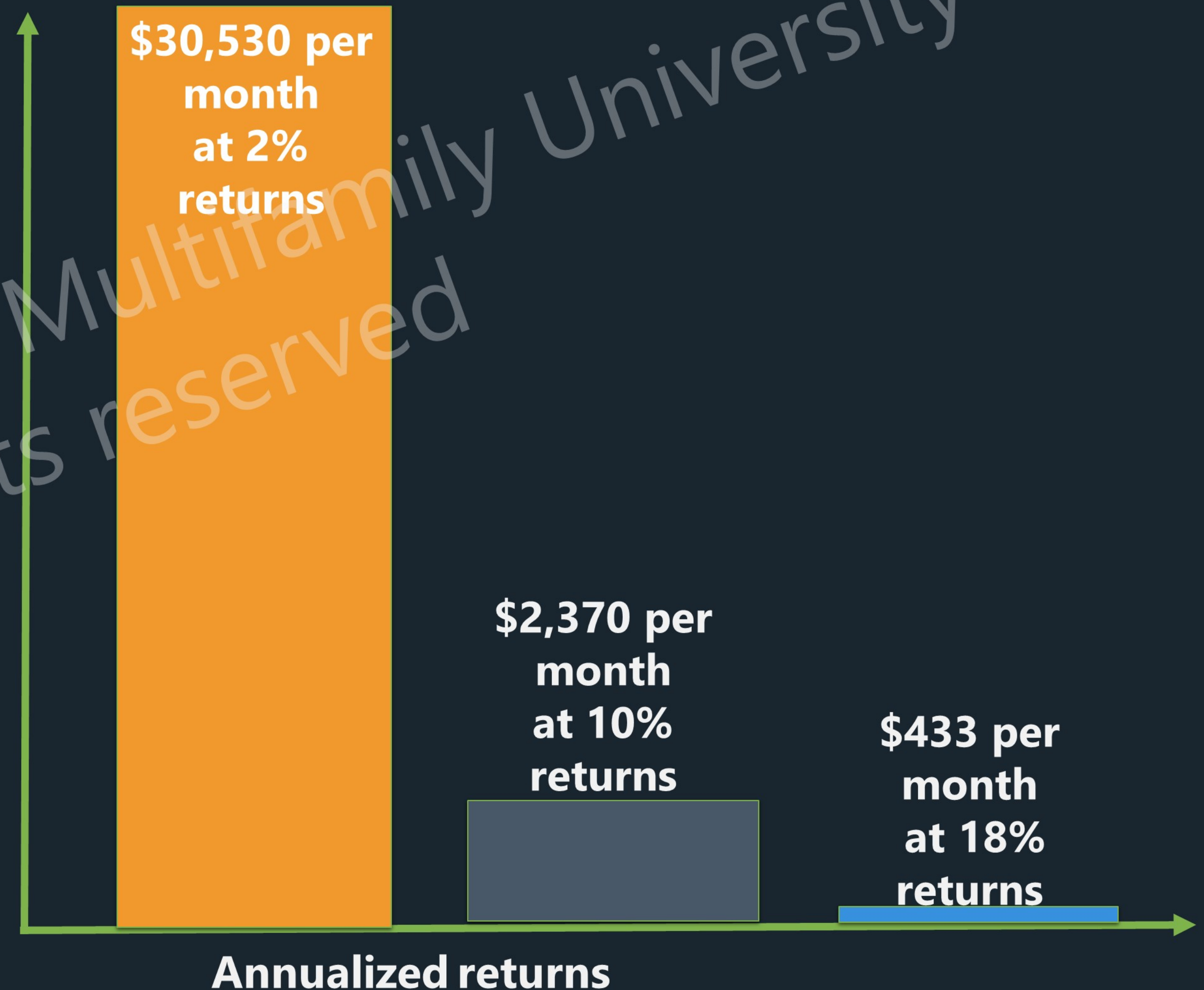
Looking at it from the end goal in mind



To have \$15,000 per month in passive income 20 years from now, how much do you need to save each month?



Dollars



AN INTRO TO MULTIFAMILY

LET'S LEARN THE BASICS



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What does the term MultiFamily mean?



The term Multifamily generally mean 5+ units. Reaches true economies of scale at 150 units

(1 to 4 units are treated mostly as Single Family and get residential)

How are MultiFamily properties valued?



Valued based on Net Operating Income, not based on comparables

Terms like Cap rate and Net Operating Income will be defined later in the boot camp

E.g. In a 200-unit complex, the management successfully raises rents by \$25 per unit. The value of the property goes up by \$857K.

=

200 units x \$25 x 12 months
7% Cap Rate

= \$857,000 VALUE INCREASE EVERY TIME.

About Multifamily Loans



Loans are based on the property's operating income and occupancy, not on your income or credit.

Lenders scrutinize each property in great detail, helping protecting investors

The Boot camp Resource kit contains the list of the top Multifamily focused lenders in the country.



How long is an investment for?



2 to 7-year investments are common. This is not a fix and flip business. Your investors must be prepared to invest for that timeframe

Classes of Multifamily Buildings

Class A, Class B, Class C



A

Most prestigious buildings, affluent tenants with above average rents.

Buildings are generally newer, have high quality standard finishes, great amenities, no deferred maintenance, exceptional accessibility.

Low cash flow & upside for investors. Cap rates of 4.0 to 5.5%. Most buyers are institutional investors. Cash flow is most sensitive to recessions.

B

Buildings competing for a wide range of users with average rents for the area.

A bit older than Class A. Finishes are fair to good with some deferred maintenance and amenities are adequate.

Better cash flow than Class A buildings, cap rates of 5.5 to 7.5%. A mix of institutional and private buyers.

C

Buildings typically 35+ years old & located in less desirable locations.

Always in need of renovation / updating.

Lower rents & higher level of mismanagement offer value-add opportunities for savvy managers. Cap rates >7%. Highest cash flow and great upside now, but higher classes will appreciate more in the long run.

D = don't buy

Older in rough areas. Not our market

Top downsides and risks of Multifamily Investing



It's illiquid

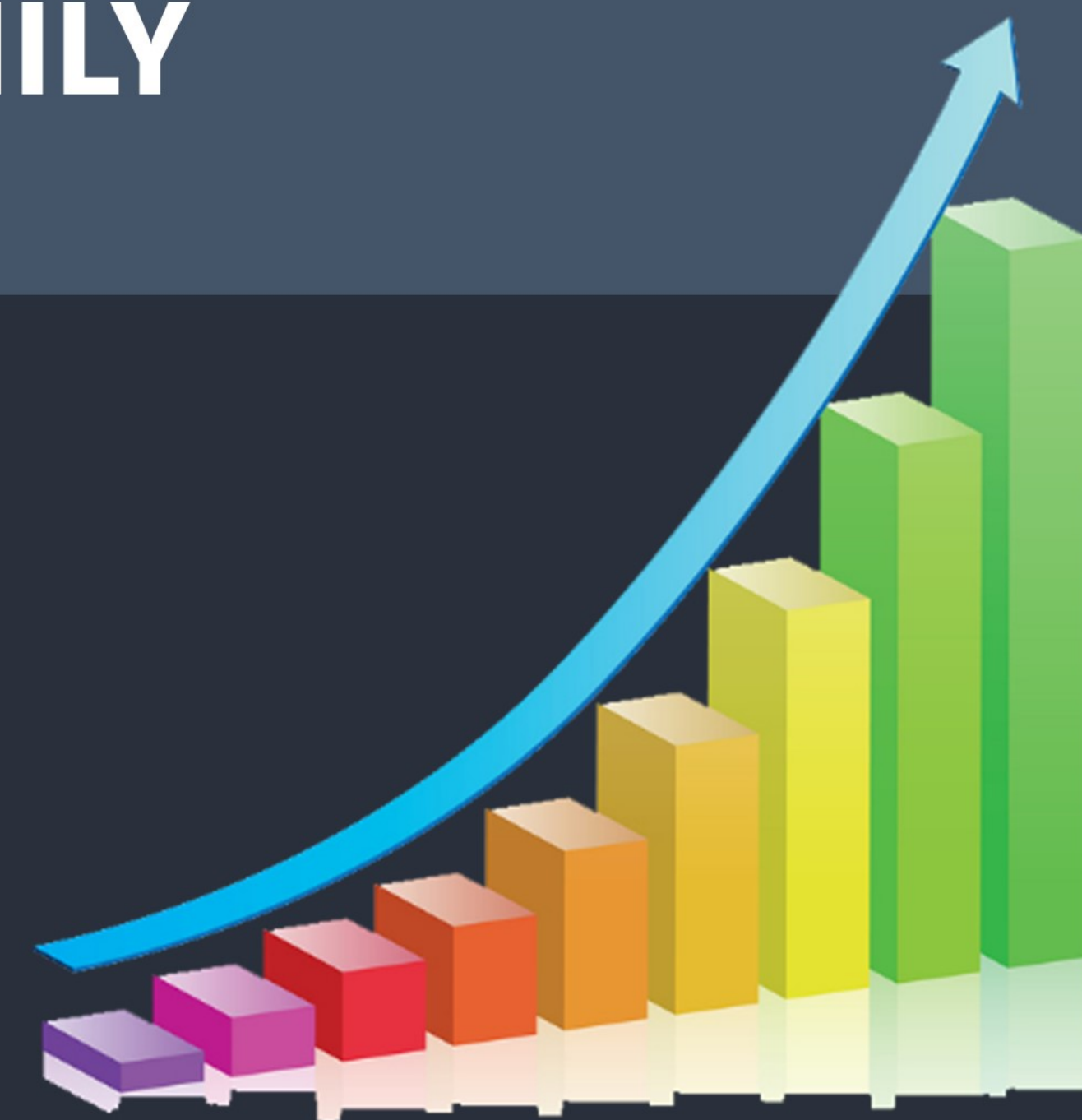
Lack of control over the investment, must trust you as the promoter

Harder to use 1031 benefits than single family



MULTIFAMILY TRENDS

WHAT IS DRIVING THE GROWTH IN MULTIFAMILY



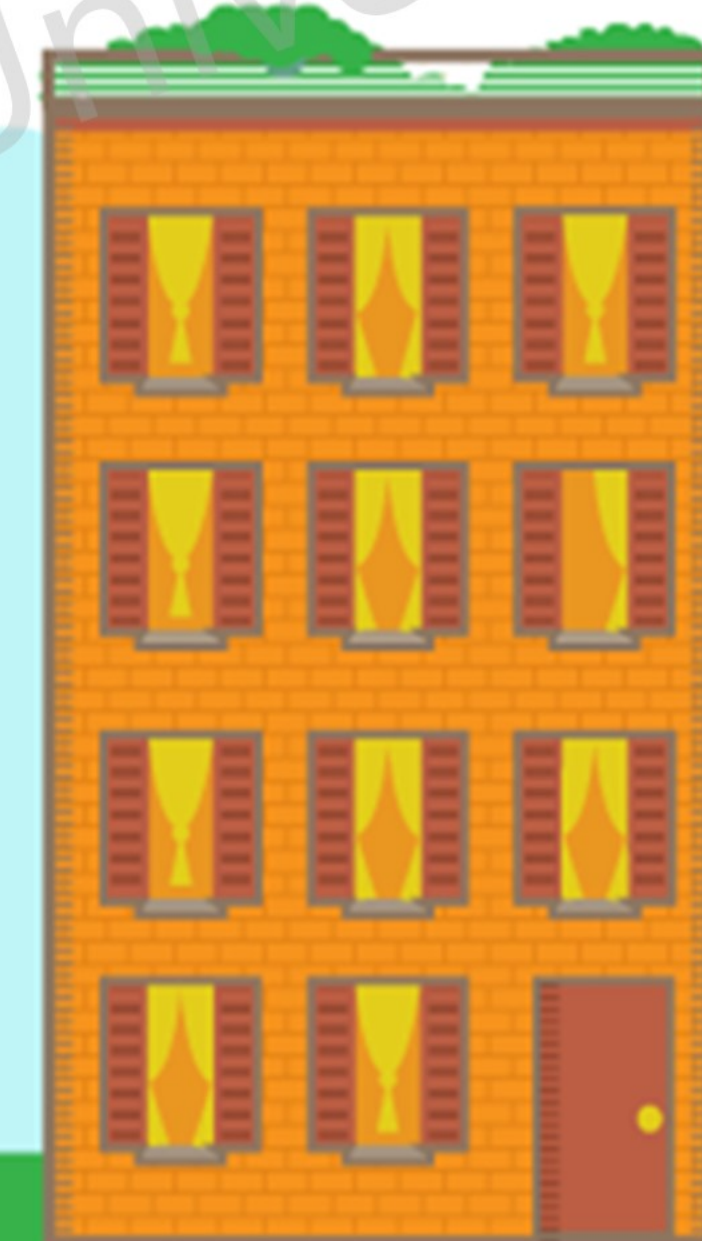
A Fundamental Change is taking place across America



RENT IS THE NEW BUY

AMERICANS PREFER TO RENT

THE NATIONAL ASSOCIATION OF REALTORS SUGGESTS 5 TO 6 MILLION NEW RENTER HOUSEHOLDS WILL BE CREATED WITHIN THE NEXT 10 YEARS. IT SEEMS AMERICANS AREN'T IN A RUSH TO BUY. IN FACT, DESPITE ELIGIBILITY FOR A MORTGAGE AND ATTAINING THE NECESSARY FUNDS TO PURCHASE, MOST RENTERS ARE STAYING PUT. WE TAKE A LOOK AT WHY IT'S A RENTER'S MARKET, AFTER ALL.



This change is driving long term demand for Multifamily Properties



ONLY **HALF** OF ALL RENTERS SAID THEY ANTICIPATED BECOMING HOMEOWNERS IN THE NEXT 5 YEARS.

**OWNERSHIP ISN'T
IN THE CARDS**

DO YOU ANTICIPATE BECOMING A HOMEOWNER IN 5 YEARS?



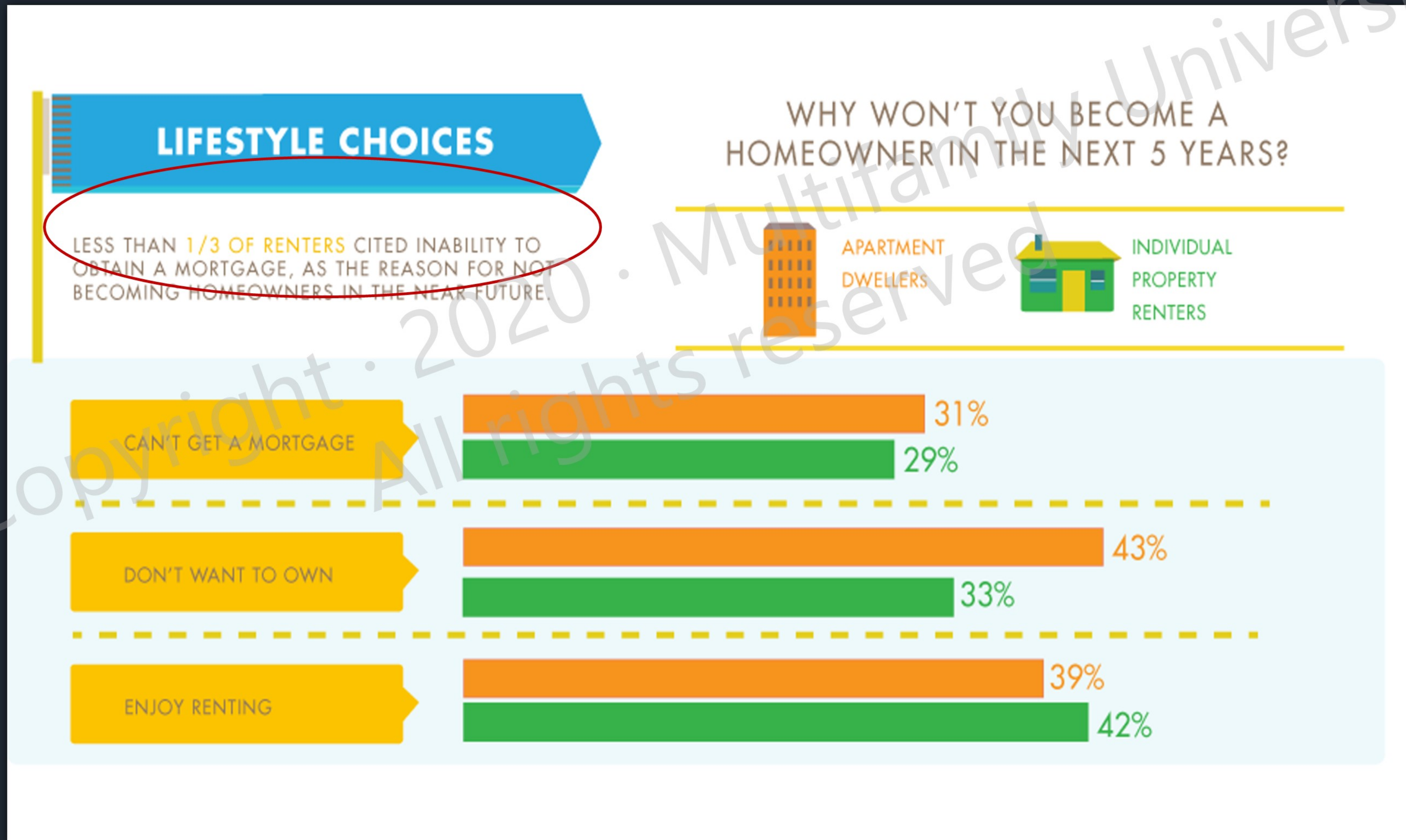
APARTMENT
DWELLERS



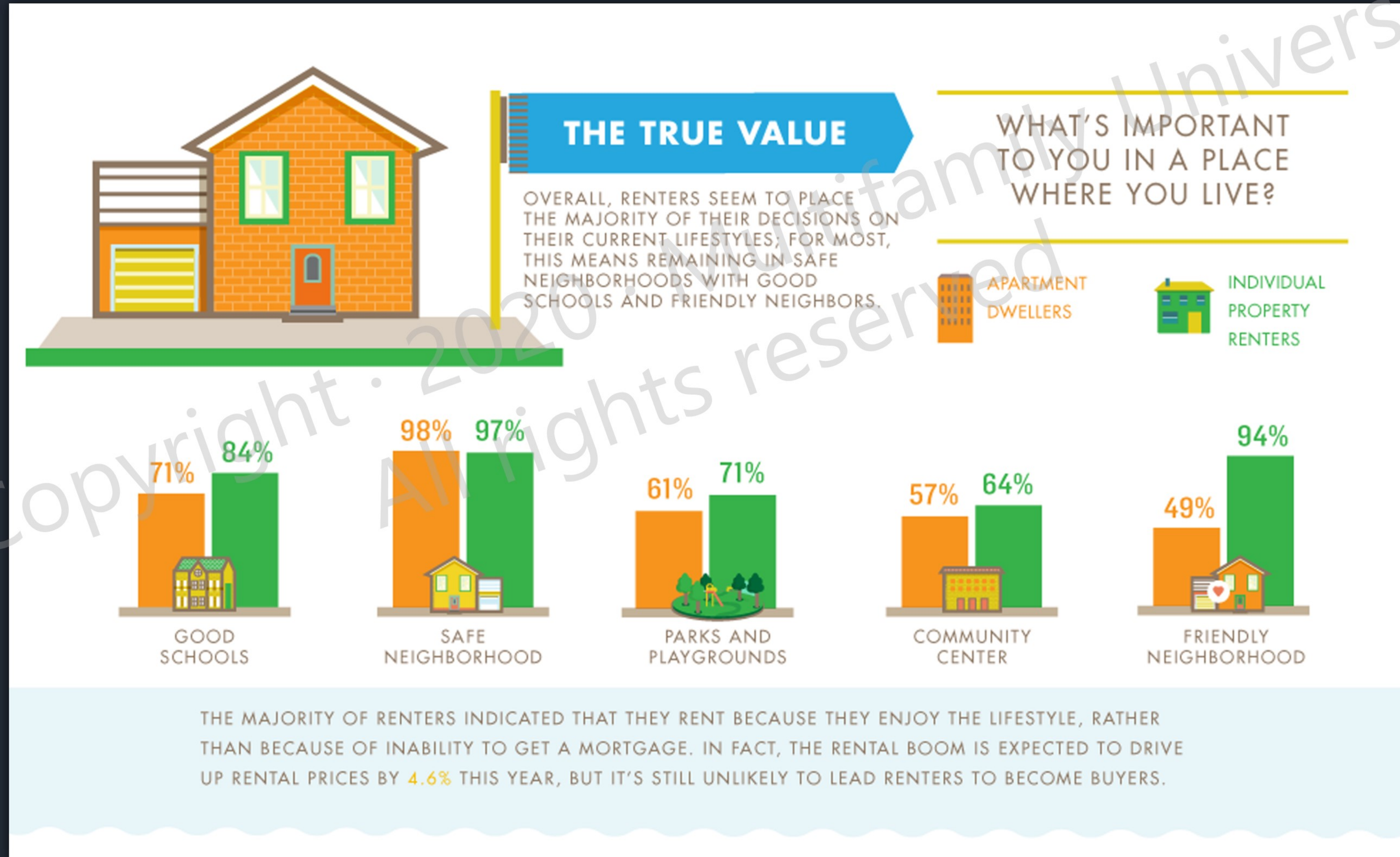
INDIVIDUAL
PROPERTY
RENTERS



They are not buying homes, even if they qualify for mortgages

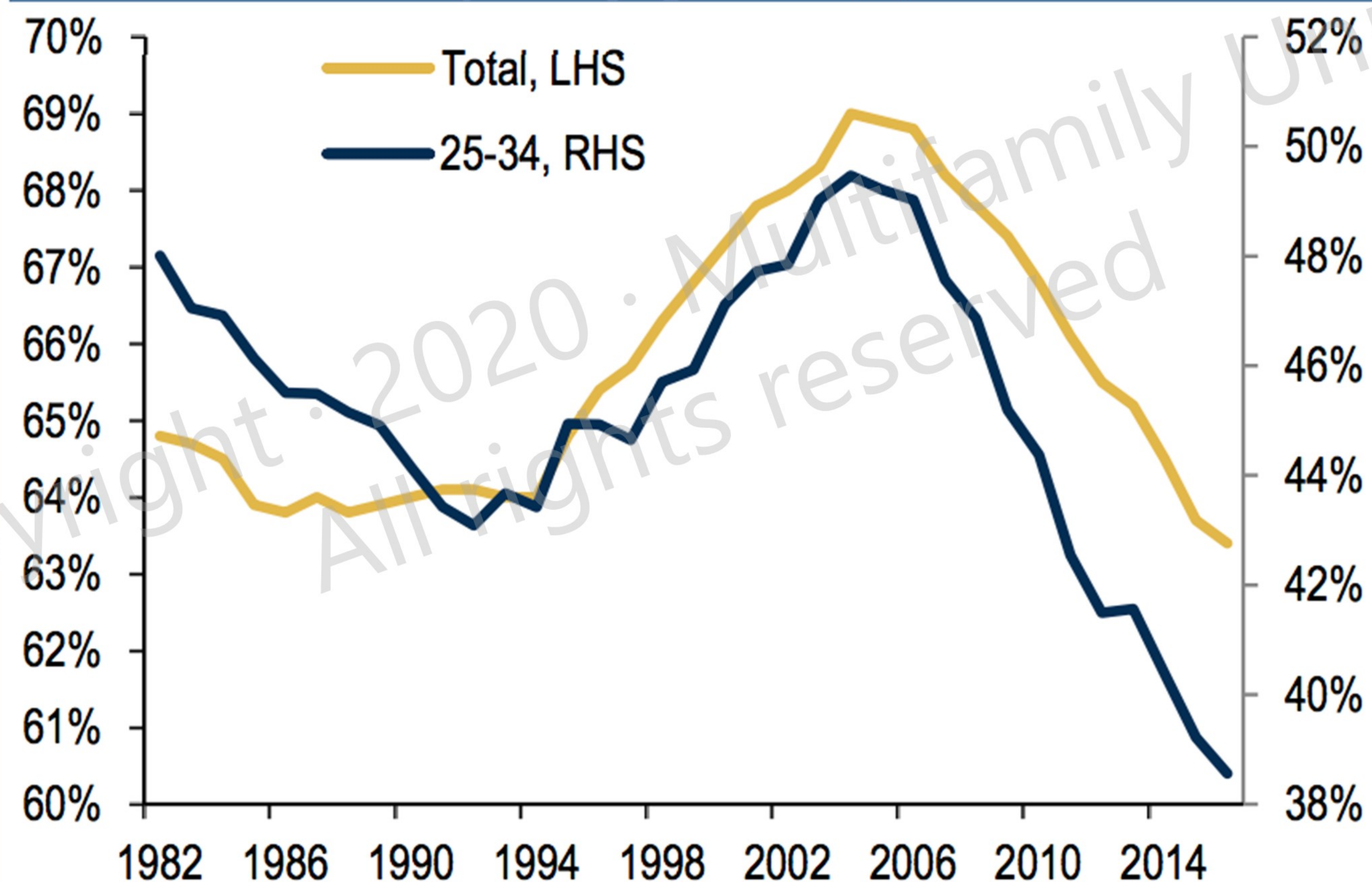


Renters are liking the freedom of the renting lifestyle



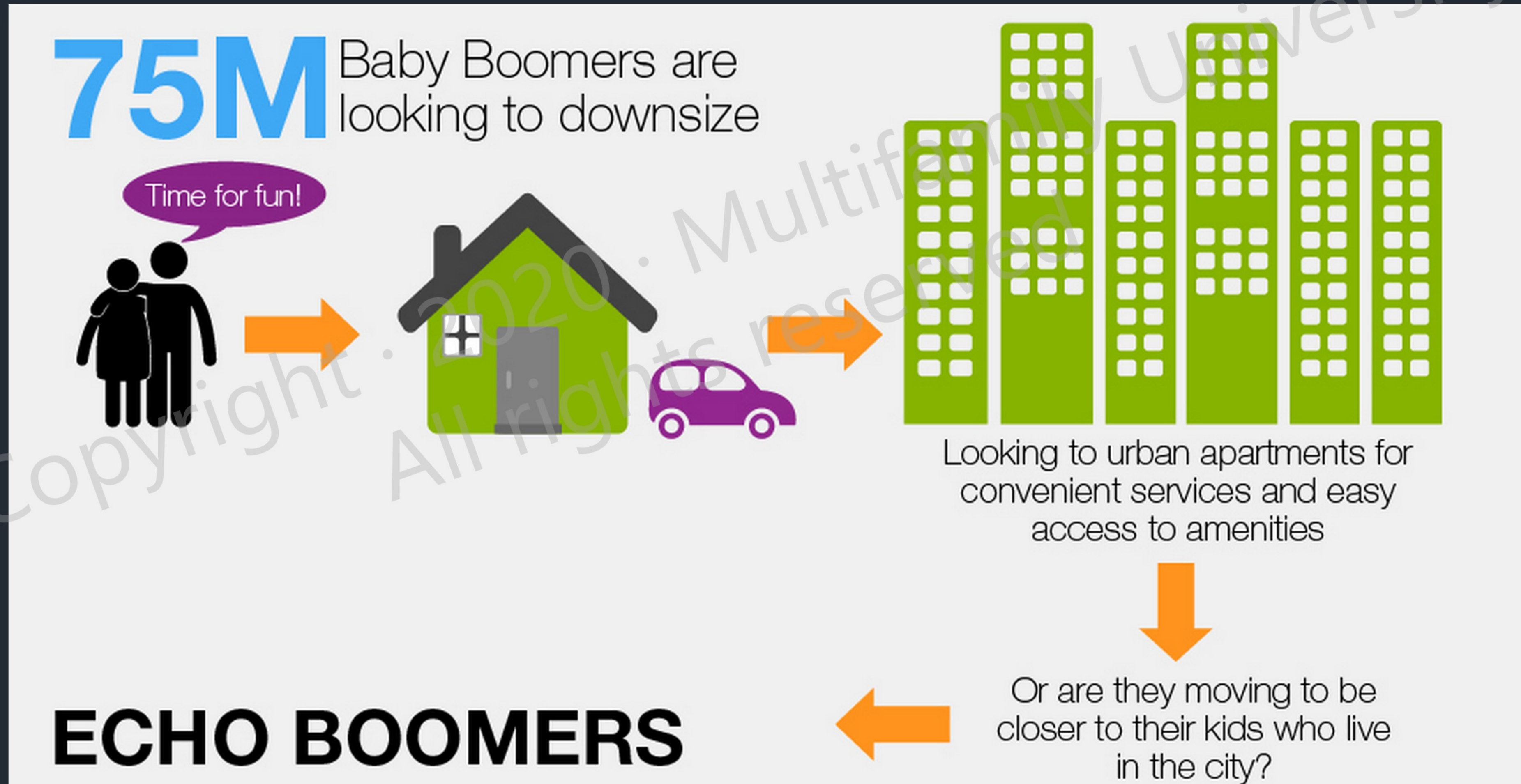
Millennials clearly are not buying homes at the same rate as the previous generations

Chart 3: Homeownership rate by age cohort (%)



Source: Census Bureau

The Baby Boomer generation is beginning to downsize to urban apartments



The Trends represent opportunity



As you can see the trends indicate that the Multifamily market could have a decade long runway in front of it.

Now let's create an inventory of reasons that your investors would invest





LAB ACTIVITY

Create a full catalog of reasons for Multifamily Investment

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LAB ACTIVITY

Create a full catalog of reasons for Multifamily Investment

- Each team gets 15 minutes to search the Internet to find all the reasons why people invest. Neal did not provide many of the key reasons.
- Select a team leader who documents the reasons.
- After 15 minutes, the full list is submitted to Anna/Eric, who will grade the reasons, and create the full catalog.
- The reasons catalog will be used by Neal on day 3, during the RAISING MONEY workshop, and provided to all attendees.



BUYING TOGETHER

HOW GROUPS OF INVESTORS CAN BUY MULTIFAMILY COMPLEXES



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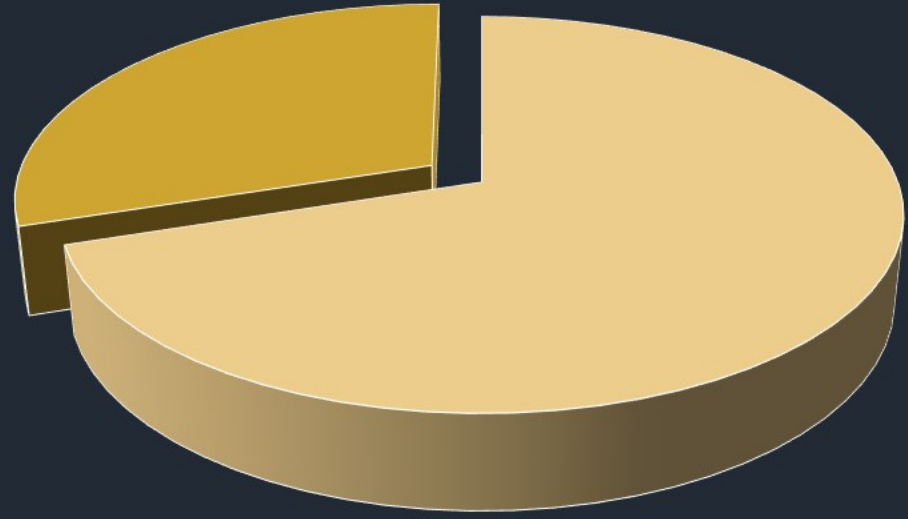
The concept of group buying through Syndication



MultiFamily complexes are expensive, so are commonly purchased by groups of investors using a mechanism called Syndication.

The resource kit contains contact info of a strong Syndication attorney that can lead you through the process.

If you want to become a syndicator, it's important for you to know that the rules of the Syndication process are governed by the SEC, for the protection of investors.



How does the Syndication work?



An experienced Multifamily syndication team finds an asset to purchase and offers the opportunity to their pre-screened investors, who then choose to participate or not in the acquisition.

Individuals, self-directed retirement plans, Family trusts or entities (LLCs) invest varying amounts and receive a proportional equity share of the cash flow and value gain.

The syndication team finds, contracts to purchase, performs all due diligence on the asset, organizes the offering and pools investor funds, and manages the property until sale..

Governing rules of a Syndication?



The resource kit contains contact info of a strong Syndication attorney that can lead you through the process.



Federal and state securities laws typically apply to real estate syndication transactions. Normally, securities may only be sold if the securities are registered with the SEC or otherwise exempt.

Traditionally, most real estate syndications have taken the form of a private placement exemption under Regulation D (Reg D).

Governing rules of a Syndication?



The resource kit contains contact info of a strong Syndication attorney that can lead you through the process.



Reg D has 2 commonly used exemptions, each of which requires the investors to be either an accredited investor or a sophisticated investor. Let us examine each type.

506(b) vs 506(c) offering



| | 506(b) Offering | 506(c) Offering |
|--------------------------------------|---|---|
| Communications with Investors | Companies may not advertise their security offering. Generally, companies may approach potential investors if there is a substantive, pre-existing relationship. | General advertising permitted. Companies may advertise via social media, email, or offline. No substantive, pre-existing relationship with potential investors required. |
| Eligible investors | Accredited investors and up to 35 non-accredited investors who meet sophistication requirements. | Only accredited investors. |
| Accreditation Process | Self-certification via a questionnaire is the general standard. | Companies must take reasonable steps to verify accredited investor status. Self-certification via a questionnaire is not permissible. The SEC issues examples of reasonable steps for verification. |

The resource kit contains contact info of a strong Syndication attorney that can lead you through the process.

506(b) vs 506(c) offering



Accredited investor

Sophisticated investor

Income

an individual that has made \$200,000 or more on an annual basis for the past two out of three years and is likely to make that same amount this year. If it is a couple qualifying together that amount is raised to \$300,000. If they do not meet the income requirements, they can qualify using a net worth of over \$1 million excluding their primary residence.

The SEC mentions sophisticated Investor as someone with enough financial and business knowledge to be capable of making an educated decision about an investment, although he may not meet the Accredited Investor requirements.

If the SEC were to ask why you thought this person was sophisticated you should be able to point to an internal set of standards so you can prove that caution was taken when making these decisions.

The resource kit contains contact info of a strong Syndication attorney that can lead you through the process.



Management of the property

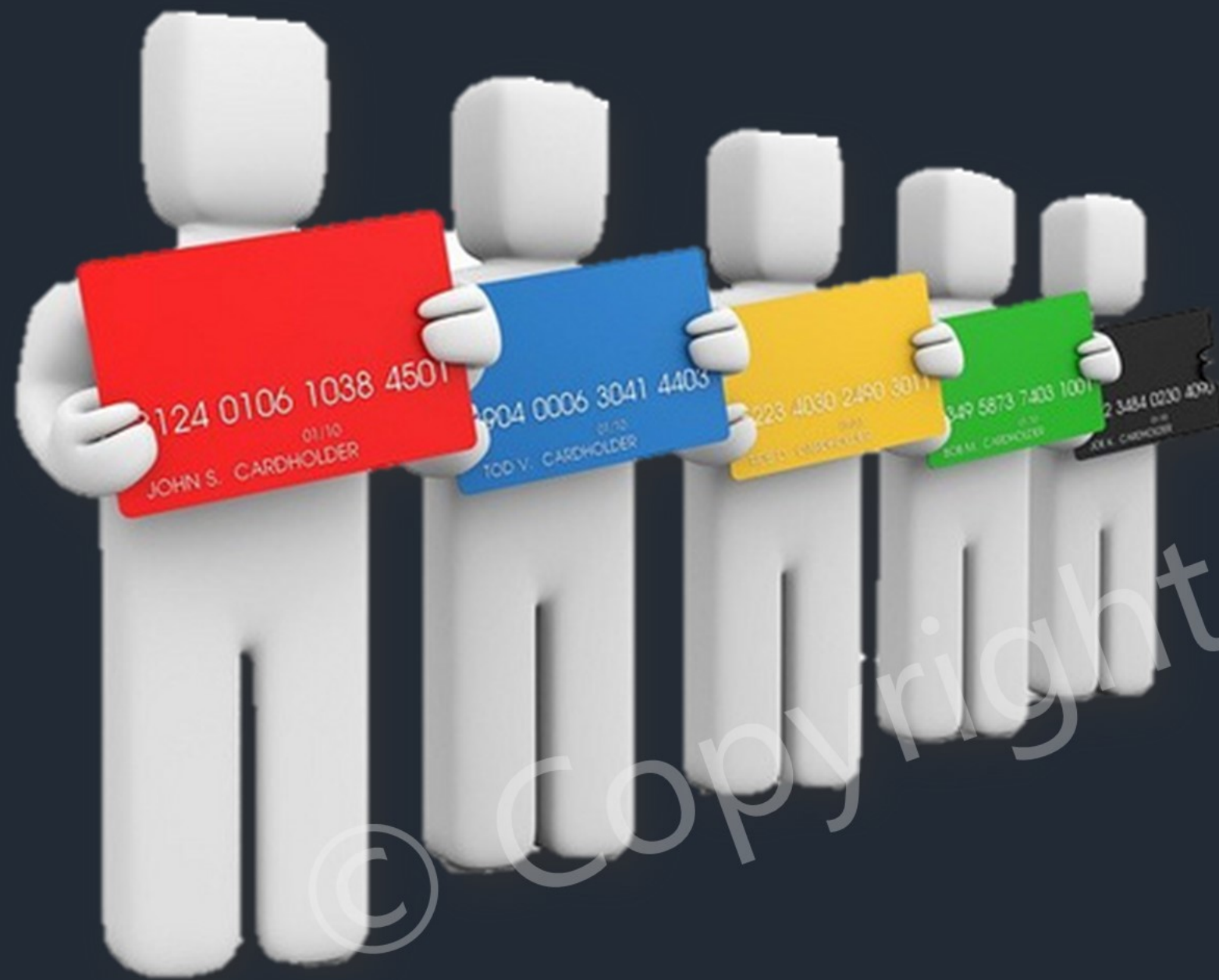


The management team assigns an asset manager and a property management company to run the property.

Investors have no involvement in day to day running of the property. No tenants or toilets.

Cash flows are typically disbursed quarterly to investors, who often receive preferred returns before the management team is paid.

Partner Types – General Partner



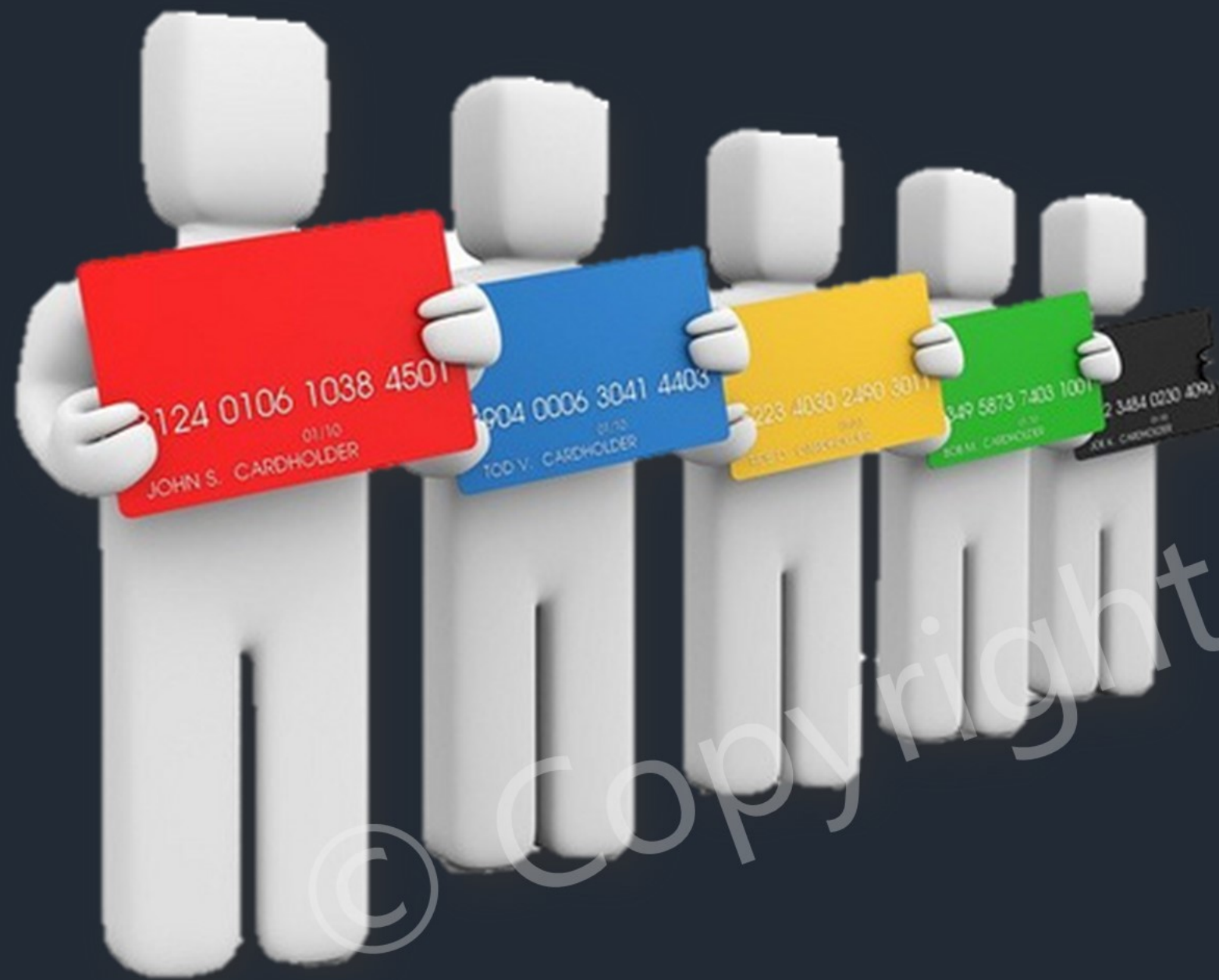
General Partner: When a team of individuals work together to put a property under contract with the intention of managing that property, the members of that team are commonly referred to as General Partners. The GPs typically stay in the deal from beginning to end and receive a chunk of the profits. They are also often known as Promoters.

Partner Types – Asset Manager



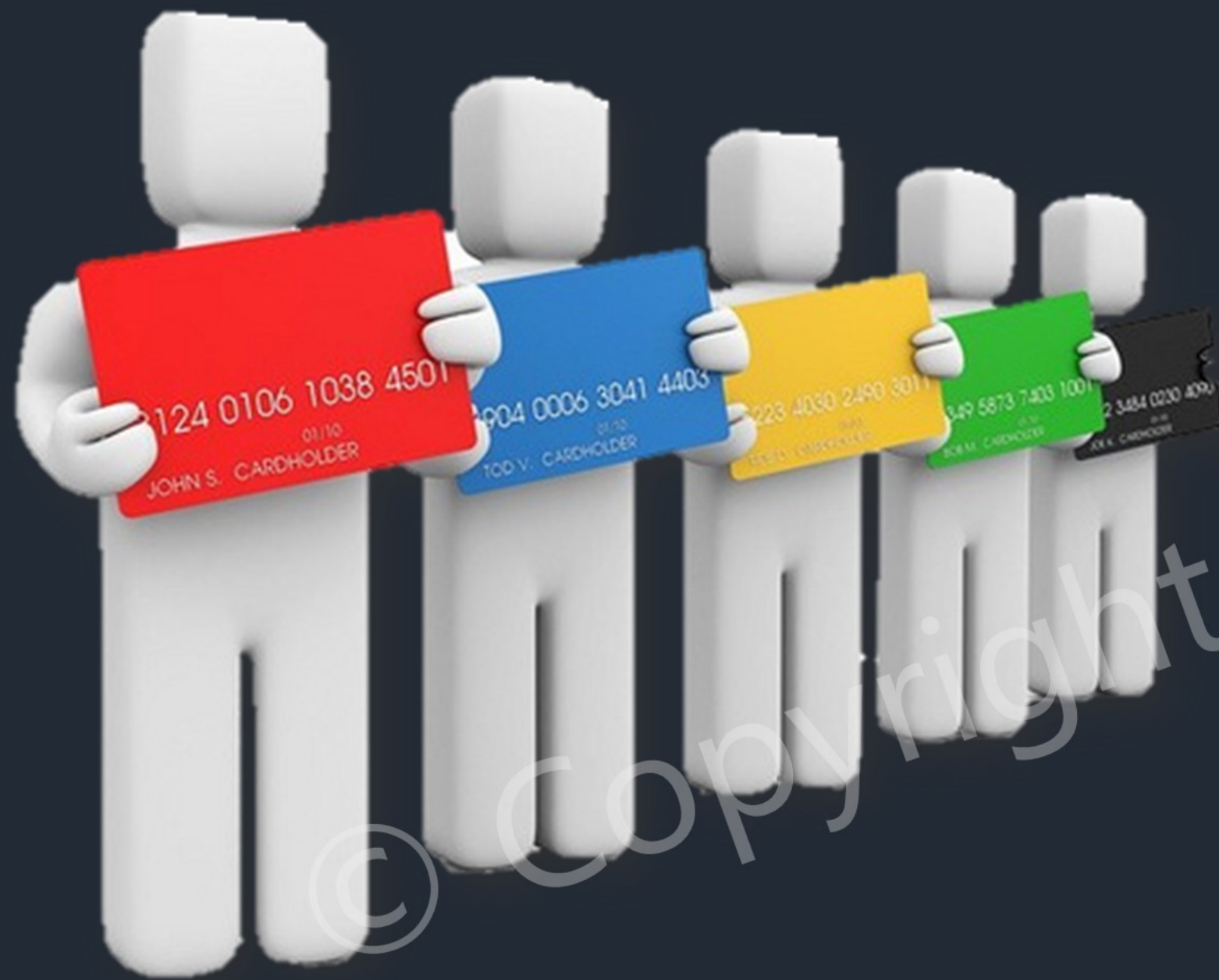
The phrase **Asset Manager** is also often used to refer to GPs, though it has a slightly different meaning. The Asset Manager could be the same as the GP, could be a salaried employee, or could be a local partner.

Partner Types – Equity Partner



Equity Partner: An Equity Partner is part of the GP team. However, their role and focus is to help raise money. Mostly, the equity partner helps the GP raise money, find investors, help to sign docs. Some equity partners also manage the investors and their tax docs for the entire duration of the project. Equity partners receive a chunk of the project, but there are strict restrictions on how their deal share can be structured. Examples are...

Partner Types – Key Sponsor or Key Principal



Key Sponsor or Key Principal: A key sponsor or Principal is someone with a high net worth and a resume/track record of managing the type of asset being purchased.

GP vs LP vs Equity partner vs Key Sponsor



- A key sponsor's net worth typically has to be at least as high as the loan amount on the property (other GPs net worth can also be used)
- And the key sponsor has to have 10% of the loan amount liquid in his bank account on the day of closing (other sponsor's liquidity can also be used).
- For small properties, the GP (you or your team) can act as the key sponsor. For larger properties, you would need a key sponsor, and they would take a percentage of the deal for signing on the loan.
- Some banks want the key sponsor to put some of their own money in the deal

Partner Types – Key Sponsor or Key Principal



Limited Partner: An LP or Limited Partner is the passive investor. While passive investors do not have any say in the running or disposition of the project, they typically provide most of the equity for the project.

Let's use a case study to Understand these terms



John and Joe get together and put a 100 unit building in Boston under contract for \$5 Million.

John and Joe live in California so they ask Ken, a friend of theirs who lives in Boston to help to manage the property.

Brad helps John and Joe raise the money for the down payment.

The down payment comes from Jason, Audrey and Keith.

The bank loan is for \$3.5 Million. John and Joe's net worth is not that high, so they bring in Ken to get them up to that mark.

Limited Partner (LP)

Equity Partner

General Partner (GP)

Asset Manager

Key Sponsor or Principal

What are typical fees charged In a syndication project?



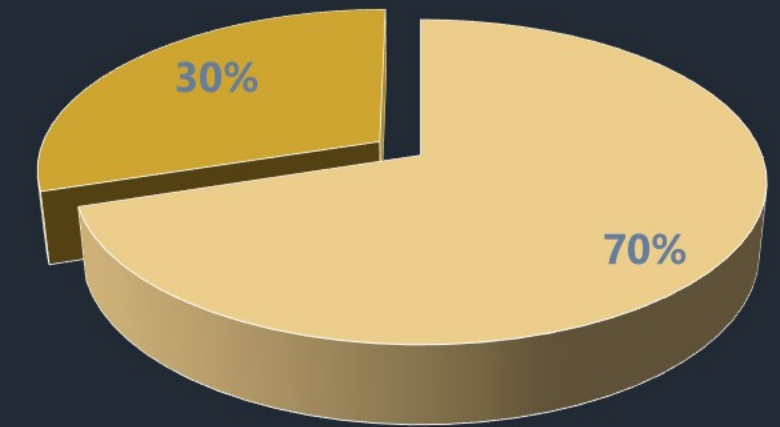
Acquisition and loan fees,

Promoters charge an acquisition fee for the property. These fees are paid when the property is purchased. Sometimes a Refi fee is also charged.



Share of rent profits

Promoters receive a percentage of the rent profits



Asset management fees

Asset management fees of 2% of Effective Gross Income are quite common. Some syndicators charge 1% of the equity amount instead.



Upside (profit) on sale

At the sale of the asset, investors are repaid their initial investment 1st, then net profits (after accounting for investor capital, debt and selling costs) are commonly split between investors and Promoters in some ratio. If returns are higher than a threshold, then returns ABOVE that threshold are split in a different ratio.



Discussion time



How much money would you (as the General Partner or GP) need to put into the project yourself?

Does the equity partner invest his own money into the property?

Does the key sponsor invest his own money into the property?

What about due diligence expenses and travel expenses and legal expenses? Do they come out of the acquisitions fees

Can you pay someone a fee to raise the money (equity)?

What kind of LLC structure is created for such projects?



LAB ACTIVITY – HOW MUCH DO GPs MAKE

Let's figure out the amount of money a general partner team makes on a typical project

- The property purchase price is 10 million
- Total LP equity is 3 million
- Acquisition fees are 2%
- Gross rents are 1 million a year, and they go up by 2% a year
- Asset management fee is 1.5%. For simplicity assume that total asset management fees were \$75,000 over 5 years.
- Splits between limited partners and general partners are 70/30
- LP Investors received total cash flow of 1.2 million over 5 years.
- The project was sold after exactly 5 years, and the total profit after paying buying and selling costs and all fees was \$3.8 million.



LAB ACTIVITY – HOW MUCH DO GPs MAKE

Let's figure out the amount of money a general partner team makes on a typical project

Exercise 1: Calculate total returns for General partners assuming THERE IS NO Pref for investors, just straight 70/30 split

Exercise 2: Assume there were 3 general partners and each had $\frac{1}{3}$ rd of the GP pie. How much money did each GP make over 5 years on this one deal?

Exercise 3: What was the Average Annualized Return for the LP investors.



LAB ACTIVITY – HOW MUCH DO GPs MAKE

Let's figure out the amount of money a general partner team makes on a typical project

Exercise 4: What was the GP's Return-on-equity-raised. In other words, for every dollar that the syndicator raised, how many cents did the GP make?

Exercise 5: For every dollar that the LPs made, how many cents did the GPs make? Was it 30 cents? Was it more?

Exercise 6: If each LP investor invested \$100K, and the syndicator's marketing cost to find the investor was \$2,000, was this a good deal for the syndicator?



LIFECYCLE OF A MULTIFAMILY PROJECT

LET'S WALK THROUGH AN ENTIRE PURCHASE TO SALE LIFECYCLE



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Multifamily Project Phases



Note that every Multifamily real estate project has a life and character of its own, but the goal is to understand the broad strokes of a Multifamily project lifecycle .

The 4 Phases of the Project



Pre-offer

1



Metro research – jobs, path of progress, pricing trends.



Team creation – Realtors, inspectors, Property managers, Contractors



Opportunity search within target areas



Walk comparably sized properties for sale in target areas



Opportunity found, first offer made based on seller's financials

Post offer

2



Due diligence #2 – Verification of financials, rents, occupancy levels, delinquency, Staff competency



Due diligence #3 – walk comparable properties on sale to ensure that our pricing and assumptions are sound, and the property is a good buy



Repair credit negotiated. Price reduction negotiated after financial verification. If seller does not agree, restart at Phase 1.



Team promotes the opportunity to their investors, through webinars and detailed Investor Summary and financial projection documents



Lawyers create legal entities (LLCs) to protect investors and management team. Purchase completed typically within 75 days and property handed over.



Post purchase

3



Management makes changes to property management team – Retrain or Replace



Management make upgrades to amenities, interiors and exterior to enhance satisfaction & curb appeal



Management transitions out or evicts undesirable tenants, and brings in better tenants with higher rents



Repair budget is used to improve the asset, increasing rents, lowering expenses, and enhancing profitability



Investors receive checks for available cash flow, and receive financials & a property report from the team.

Sale

4



Management runs complex for 3-5 years. With market appreciation & better management, the property's income increases steadily.



Typically, by Year 5 or before, the property's Net Operating income reaches the exit projections.



Management puts property up for sale, and aims to complete the sale within a 6-month timeframe.



Investors receive their principal back, along with profits.

Questions on this module?

