Elements of a Successful Real Estate Investment

Successful real estate investments generally have several things in common. We've identified five key elements you should look for in analyzing and operating any particular transaction. First and foremost, you need access to investment assets through networking and other "on the ground" relationships. Those potential assets must be vetted the investment fits with the fund's structure. The real estate investment must have a business plan that guides how the investment is managed. and structured.

Access to Investment Assets

Access to potential investment properties is acquired through networking and local market knowledge. For example, Ryan Wehner has an extensive network. The sponsor may approach property owners directly to solicit a sale. Likewise, the sponsor may cultivate relationships with brokers and other market participants who have local knowledge of the market.

Ability to Screen and Analyze Potential Investment Assets

It is usually not efficient to perform a full analysis of every potential offering. Experience and formal screening criteria contribute to identifying appropriate investment assets. The more experience the sponsor has, the easier it will be to decide on what assumptions are reasonable and to identify the risks.

Getting the Property Under Contract

Sellers and brokers seek the certainty of execution. Brokers steer sellers towards buyers who they know have historically closed transactions without re-trading and without delays. Reputation and track record in the local market induce brokers and sellers to enter into a contract. The better the reputation of the sponsor with the broker, the more likely it will be to be awarded a contract in a competitive environment. That said, Wehner Multifamily Properties welcomes the Bellaire Investment Group into its network of trusted associates.

Determine Funds to Place in Escrow as a Non-Refundable Deposit

The current market requires that approximately 1% of the purchase price be put in escrow as a non-refundable deposit against the purchase price. Buyers need to both have access to the funds to enter into a purchase contract; and certainty that they can pull the rest of the transaction together by the contractual closing date in order to not lose their deposit. Of course, it also assumes that the buyer is confident enough in their up-front analysis and limited due diligence that the transaction will make sense and will be able to close.

Create a Business Plan

Every real estate asset purchase requires a well-thought-out business plan. We generally purchase value-add multifamily, so the business plan will differ from other asset classes. For example, investment in core stabilized properties, the business plan may focus on how to keep the property in good physical condition and how to forecast and fund repairs that will inevitably occur over time. In value-add properties, the operator looks to raise the level of the property from, for example, Class C to Class B property. In addition to regular upkeep and saving for future repairs, there is usually a large component of capital expenditures (CapEx) that are planned up-front to reposition or stabilize the asset. Experts must inspect the property to determine what interior and exterior upgrades and changes are recommended in order to attract the intended tenant demographic and to increase rents. Local market knowledge and research are necessary to learn what rent levels the submarket can bear and what amenities and unit styles are essential to achieve those rent levels. The CapEx budget will be important in establishing how much debt and equity is needed initially at the time of purchase. In addition to the CapEx and operational aspects of the business plan, there is a long-term, strategic part of the plan that is produced up-front. The strategic aspect includes the time horizon for the investment and whether refinance or sale will be sought for future liquidity.

Determine Optimum Deal Structure

Lending sources offer various levels of leverage and terms vary significantly between lenders. Agency loans, bridge loans, and bank loans can all be used to finance the purchase of an investment property. Critical to the investment analysis is deciding how much leverage to put on the property and deciding between fixed and floating rate, long term or short term, and recourse or non-recourse. Some transactions may benefit from another layer of capital between equity and debt. It can be either preferred equity or mezzanine debt.

Qualification for Debt as Operator/Key Principle

Once a capitalization structure is decided on, the sponsor must qualify for the loan. Typical Key Principal/Guarantor requirements include:

- A net worth of 100% of the loan amount
- Liquidity equaling 10% of loan amount post-closing
- GSE’s (Agency lenders) require the KP/Guarantor to have experience operating multiple properties in the submarket. Bridge lenders often follow GSE requirements so that they can be more certain of a take-out/permanent loan at the maturity of the bridge loan. Bank lenders often require less experience, but they also typically require full recourse and offer low leverage (60% to 65% versus the GSE and bridge lenders’ 75% to 80%)

Equity Sources to Close Transactions

Personal investment, friends and family, a professional network of high-net-worth investors, and institutional investors are all sources of equity. When committing funds to a non-refundable deposit, the sponsor needs to be confident that the rest of the equity will be accessible by the closing date. In addition to the difference between the loan and the purchase price, the sponsor must consider how much equity is required for closing costs and fees as well as a reasonable amount of working capital and reserves for currently planned and future forecasted capital expenditures and repairs.

Property Management & Asset Management

Upon completion of the purchase of the property, the operation of the property and execution of the business plan is the focus of the sponsor’s attention. At Wehner Property Management, we understand value-add properties are never of the “fire and forget” variety. Other sponsors may have their own in-house property management resources, or they may utilize a third-party management company. Either way, ongoing attention to the property is essential by the sponsor. In addition to standard property management functions like collecting rent and making repairs, ongoing decisions need to be made regarding setting rent levels, marketing to prospective tenants, collections and evictions, as well as approving and supervising repairs, replacements, and CapEx projects.

Real estate investment can be tricky, which is why you need dedicated investment partners that will invest alongside you and manage your investment together with their own. Give Bellaire Real Estate Funds a call and find out what we can do for you.