FINDING THE NEW RENO

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Standard Management Company has been praised and congratulated by its investors for acquiring a substantial amount of property in Reno, Nevada shortly before the TESLA announcement. This was at a time when most real estate professionals had discounted TESLA's pre-development activities in Reno believing that they only put pressure on Texas and California to make more concessions and encourage the company to locate in those states.

Being perfectly honest that was our conclusion as well. However in doing our homework in preparation for deciding on these purchases we determined that Amazon and Apple had already made major commitments to Reno and that the City had many basic advantages probably the most important being Nevada's low tax rate and general business incentives. There was a trend of Bay area high tech of relocating some of their facilities from Northern California to Reno.

We were able to apply our 58 year history of real estate investing and lending to make decisions in favor of a number of acquisitions that presented themselves both on market and off. During that 58 year period we acquired properties in 15 states and 27 metropolitan areas. While the real estate business is one where you make your profit when you buy not when you sell, we make two mistakes; we did not buy enough and in many cases sold too soon.

When asked how I have acquired my wealth through real estate and how it was done is very simple. I made ever mistake you could possible make, tried to do it only once and lived a long time. Therefore if you want to get rich in real estate you simple make a lot of mistakes and live a long time. Many of you have heard the real estate joke where developers were having a big conference and were complaining how difficult it was to find good opportunities to invest and develop. Finally in the back of the room one developer said “oh I've found the great place, everything I am buying is increasing in value and we are doing very well”. A friend asks “where is it?” He said “do you think we are going to tell you?”

I am not able to predict where the next opportunity will be but I am going to share with you some of the strategies and experiences we have had on this long road to real estate success. Our pass includes 1920's high rise bank buildings in downtown Los Angeles, office buildings and high rise apartments in Atlanta Georgia, industrial shopping centers, apartments and a MHP in Central Ohio, industrial and agriculture in the San Joaquin Valley and projects in Albuquerque and Dallas and many other locations.

As a result we have learned with taxes having such a high impact on economic development both personal and business, if you look at a State's overall tax picture and business incentives you can often predict in what direction the area is going. Next would be schools. These are both macro factors in that they affect somewhat of a larger area.

Most importantly in making a decision on a particular acquisition is the micro factors. These include if you are looking at an apartments such things as school system ratings, poverty ratio, the age of the property, maintenance efficiencies, occupancy and the conditions of cars in the parking.

The next opportunity may be within your own backyard or that may be the worst place to invest. Obviously the data and knowledge about the market may be easier to acquire close to home but we have found that the one constant is change while your neighborhoods' improving or declining State prospects are improving or declining and so on.

With retail there is a different set factors such as how many cars per day go by the property and co-tenancy. Multi-family may be on a very busy street but with appropriate sound barriers, and construction can be very successful. A shopping center without traffic seldom succeeds. There are numerous tests that can be undertaken with in-house underwriting namely population trends and activities based on bank deposits, employment, post office receipts and activities etc. The key statistics with respect to property ratio, schools, residential and many other of these indicators are readily available on the internet for free.

Underwriting also has to be done on site regarding the condition of the building, quality of tenancy and operating efficiencies. If you are looking at a project and have not found anything wrong, you simple have not looked far enough.

Real estate is finding problems and determining whether or not you can solve them. Some of the best opportunities can be low cap rate properties that are inefficiently operated and where there is opportunity to value-add which can bring the income above the existing cap rate. We have found that in purchasing property in the neighborhoods that we want and meeting our goals of positive leverage we need a 5 to 5 ½% in cap rate today. However if there is opportunities to upgrade units that will bring substantial rent increases our return can exceed that 5 to 5 ½ as a result of upgrade improvement return anywhere from 15 to 25% and sometimes higher. We can bring the cap rate up in the first 5 years usually to 7% or better increasing the value of the properties by at least 40%. As to the properties you already own, spending capital on them can create a better return than you can find spending that more in acquiring a new property.

Regardless of the general economy there are always some areas that are improving and some that are declining. Obviously in a recession it is easier to find a good buy but the risk of catching a fallen knife is greater. One partner has the ability to find the best buy and improve it and the other has the ability to fund the equity required. When I started out 50 years ago there were opportunities far in excess of our reserves to purchase. We never looked at a property unless it was a 9 cap or better. Today the reverse is true. We have almost unlimited capital offered to us continuously and have a pool of over 100 investors which is constantly growing, however we do not advertised, we do not used Wall Street, we work almost entirely on word of mouth. Funds are almost unlimited but the number of opportunities is much harder to find. In the beginning it would take only perhaps 10 potential property inspections to find a good deal, today the ratio is probably over 100 to 1. 100 come in and probably 80 are immediately rejected in a two week period, then we underwrite 20 that's reduced to 5, then we make offers on 5 and if we are lucky we get one. It is a gigantic fondling process.

While real estate is not rocket science it is just 6th grade arithmetic, it takes a lot of due diligence, work, and time to find a project that makes sense. Once it is found then there is a lot of effort involved in getting the proper financing as the financing you get often determines the success of the project. With interest rates so low, we have shifted to financing that has a long maturity. There are others who view a short term floating rate debt as the way to maximize cash on cash. It depends on how conservative you are. So far while we have been expecting rising interest rates for a number of years, we have had a longer period of low interest rates than almost everyone expected so those who went for floating rate and short terms have come out better. However I remember when first mortgage rates were as high as 13% and you do something relying on low rates you could be in deep trouble. The Chinese say that luck is preparation. While we say it is much better to be lucky than smart a lot of preparation and due diligence is required to be successful continuously. Be careful not to over improve. Appreciation versus high cap rate. Good luck and if you find the next Reno give me a call.