MULTIFI

THE

MULTIFAMILY ROADMAP

HOW TO THINK, INVEST, AND PROFIT BIG

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CHAPTER 1

WHAT IS MULTIFAMILY?

THE BASICS

01

MULTIFAMILY

mul·ti·fam·i·ly
/ˌməltēˈfam(ə)lē/
adjective

denoting or relating to accommodation designed for occupation by more than one family.

MULTIFAMILY

Multifamily is an asset class of real estate referring to residential dwellings with multiple units for tenants (or families!) within one or several buildings in a single complex. In order to qualify, there must be four adjacent housing units-- horizontally or vertically, though some refer to two or more units as multifamily.

Multifamily can be anything that has a minimum of four units and up. On a smaller scale, many investors start off buying a duplex and living in one unit while creating a secondary income from the other unit.

Multifamily investing is a powerful tool to diversify an investment portfolio and offer a highly scaleable model. Real estate provides multiple vehicles for building wealth: appreciation, cash flow, tax efficiency, and principal paydown.

TYPES OF MULTIFAMILY

APARTMENT BUILDINGS

Apartments buildings are multiple units that are all generally owned by one owner or corporation, not individual unit owners. The owner leases the units to tenants and maintains the common areas and the expenses of operating the asset.

DUPLEXES

Duplexes are two separate houses or units that typically sit side by side with private entrances. There are no common areas or shared spaces in the interior of a duplex.

TRIPLEX/QUADRUPLEX

Triplexes and quadruplexes (fourplexes) are similar to duplexes, but they have three or four units respectively.

TOWNHOUSES

Townhouses are similar to detached single family homes (SFHs), however they are typically attached to one or more neighboring townhouses. They usually have their own private entrances and sometimes have multiple levels. Multiple townhouses sitting side by side are often referred to as "row houses".

CONDOMINIUMS

Condominiums are generally similar to apartment buildings, however each unit is owned by a separate owner and the common areas are owned collectively by the individual unit owners under the umbrella of an association.

MULTIFAMILY

CONDOMINIUM
con·do·min·i·um
/ˌkändəˈminēəm/
noun
noun: condominium; plural noun: condominiums

1. A building or complex of buildings containing a number of individually owned apartments or houses. Each of the individual apartments or houses in a condominium complex. The system of ownership by which condominiums operate, in which owners have full title to the individual apartment or house and an undivided interest in the shared parts of the property.

TOWNHOUSE
town·house
/ˈtounˌhous/
noun
noun: town house; plural noun: town houses; noun: townhouse; plural noun: townhouses

1. A tall, narrow, traditional row house, generally having three or more floors. A multi-story house in a modern housing development which is attached to one or more similar houses by shared walls.

DUPLEX
du·plex
/ˈd(y)oopleks/
noun

1. A house divided into two apartments, with a separate entrance for each.

02

CHAPTER 2

WHY INVEST?

A SHORT LIST OF BENEFITS

02

INVEST

in·vest
/in'vest/
verb

expend money with the expectation of achieving a profit or material result by putting it into financial schemes, shares, or property, or by using it to develop a commercial venture.

INVEST

Multifamily investments continue to be a long time favorite asset class for the wealthy. It's one of the best strategies to build generational wealth for many reasons. High net worth individuals utilize this asset class in their portfolio often and continue to seek the many benefits of these investment opportunities. It Is easily one of the best tools to hedge against Inflation today.

1. STABILIZED ASSET CLASS

Over the years, investing in apartment buildings has proven its stability as an investment. Four decades have passed and the multifamily market has enjoyed several years of rapid growth and seems poised to continue to grow in the future.

In addition to the increasing demand, the population growth of ages 20-34 years in the US is set to exceed 60,000,000 in the next 25 years making apartments a worthy investment.

Historically, multifamily, as an asset class, has the highest Sharpe Ratio of any other sector. This means that multifamily has the highest potential return for the least amount of relative risk, making It one of the best Investment vehicles available.

2. SCALABILITY

Multifamily allows you to increase the number of doors you own with very little effort. Because of the concentration of units, scalability is easily one of the best benefits to be realized. The time, energy, and effort required to purchase 100 single family rentals is far greater than the resources required to buy one multifamily asset with 100+ units. Being able to repeat this process on a larger scale makes it easier to grow quicker through multifamily investing.

3. LOWER VACANCY RISK

The more units you have, the less risk there is in one tenant moving out. Having only one unit (ex- a single family rental), if your tenant moves out, you are at a 100% vacancy. However, if you have 100 units and a tenant moves out, you are at a 1% vacancy.

4. DEMAND DRIVERS

Multifamily rentals tend to be in high demand regardless of the home buying market. Of course, you must buy with the correct market fundamentals to ensure your tenant base and financials are strong. Market trends show that millennials are either delaying or not purchasing a home, opting to live in multifamily residences instead.

5. CONTROLLABLE MARKET VALUES
Multifamily value is directly determined by the Net Operating Income (NOI) of a property. There are many creative avenues to drive up NOI (ex: increasing income, reducing bad debt, reducing the loss to lease, or decreasing expenses), therefore resulting in a higher market value of the asset.

6. DEBT LEVERAGE
Most people think of multifamily as having the highest barriers to entry considering the relatively large purchase price.

When buying a single family home or a smaller property, the bank often requires your personal creditworthiness, income, and a balance sheet of the buyer in addition to a personal guarantee.

Although counter intuitive, financing larger deals is often easier.

When financing larger multifamily assets, the lender focuses on the merits of the property itself. The lender uses the subject properties historical financial performance to determine risk and leverage. Experienced buyers with a track record sign what's called "non recourse" debt meaning that there is no personal guarantee. These types of loans are reserved only for buyers with significant experience.

7. TAX ADVANTAGES
Thanks to generous IRS rules and regulations, real estate investments are able to take advantage of tax savings vehicles unavailable to other investments. The utilization of cost segregation along with depreciation often allows for tax advantaged returns. Many high net worth investors view periods of uncertainty in the market to be opportune times to take advantage of real estate investments.

Consult with your CPA to understand the full benefits that you can take advantage of.

INVEST

LEVERAGE
lev·er·age
/ˈlev(ə)rij, ˈlēv(ə)rij/
verb

1. Use borrowed capital for (an investment), expecting the profits made to be greater than the interest payable. "a leveraged takeover bid"

2. Use (something) to maximum advantage.

SCALABILITY
scal·a·bil·i·ty
/ˌskāləˈbilədē/
noun
noun: scaleability

1. The capacity to be changed in size or scale.the ability of a computing process to be used or produced in a range of capabilities.

03

CHAPTER 3

EMERGING MARKETS

WHERE TO FIND OPPORTUNITY

03


EMERGE
e·merge
/ə'mərj/
verb
1. move out of or away from something and come into view.
2. become apparent, important, or prominent.
3. (of facts or circumstances) become known.

EMERGING MARKETS

Many of the indicators of an emerging market include: job growth, population growth, and developing infrastructure throughout the market. While referencing the Emerging Market Graph, an emerging market tends to fall somewhere soon after the Buyer Market II stage.

The Buyer's Market II stage in an emerging market is typically where some of the best multifamily deals can be found. Ideal planned exits should aim to be between Seller's Market I and Seller's Market II whenever possible.

Choosing the "right" multifamily apartment complex is critical to develop the best strategy. Operators should remain steadfast in their conservative investment philosophy which will lead to them turning away more deals than they are accepting. During tight market conditions, syndicators could be turning away 400+ deals for every one deal they acquire. Passive investors benefit greatly from having a knowledgeable operator who will only present the very best deals to their investor base. This is one of the key value add components an experienced operator brings to the table.

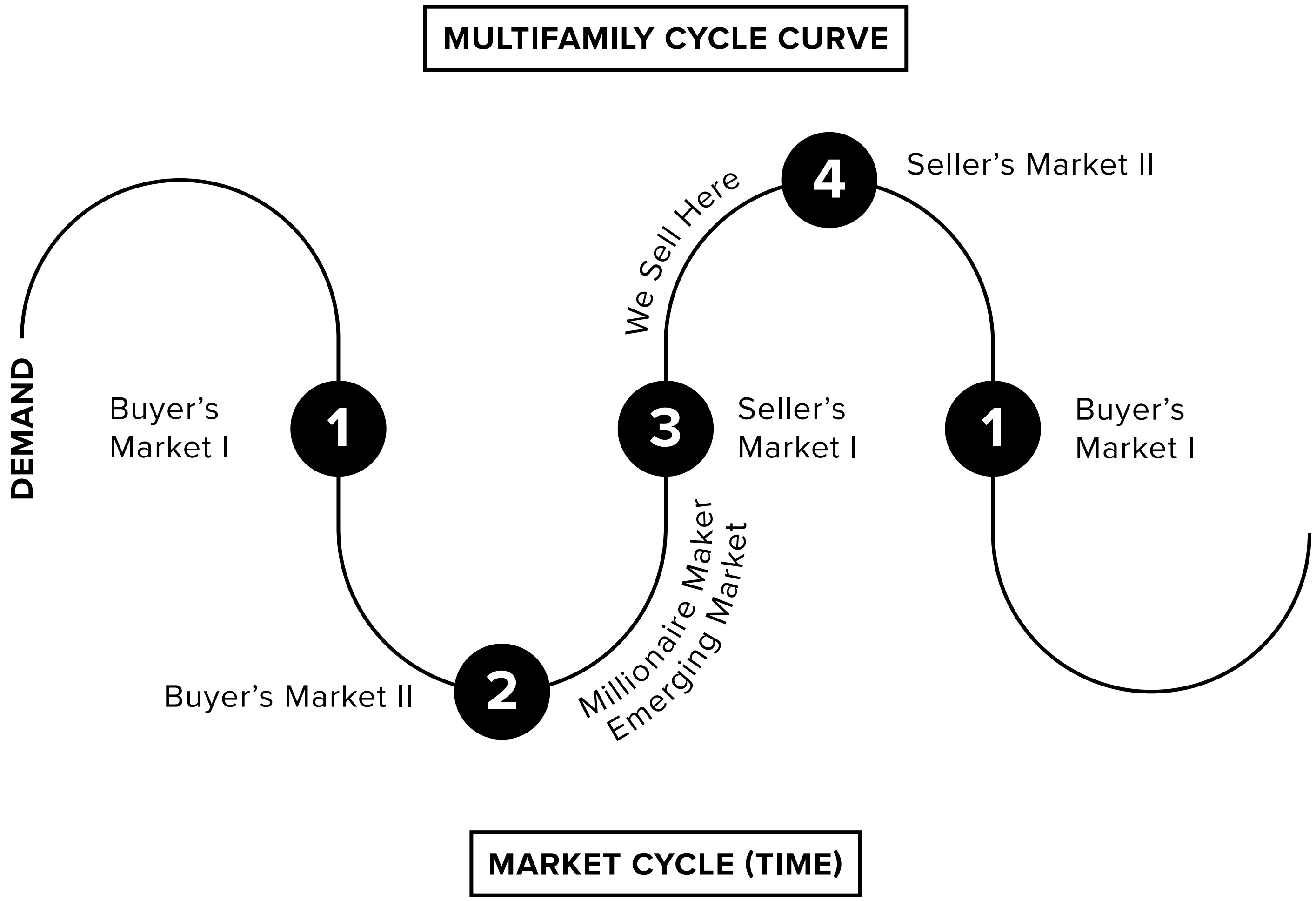
There are many indicators and many resources used to determine an Emerging Market in the US. Market data analytics include:

- Job Growth (local & regional)
- Population Growth
- Local Economic Trends
- Local Chamber of Commerce Predictions & Reports

Below is an example of the type of information gleaned from a normal market study that would prompt an interest in a property in the area:

- Strong economy which performed well in previous recessions and recovered faster
- Low state income tax that attracts businesses
- 7-8% average unemployment that is trending downward
- Average apartment occupancy of 90% and growing (with many cities higher)
- Increasing rent growth – Projected 3% or higher in most large cities
- High demand for rentals throughout the state
- New apartment construction low and absorption high
- New construction (medical centers, schools, governmental, infra-structure, sports stadiums, as well as big box retail centers)
- Influx of major corporations
- Oil / natural gas sectors booming

EMERGING MARKETS



BUYERS MARKET I
Market still oversupplied
Prices and rents falling
Time on market increasing
New construction stagnant
Unemployment reaches height
Foreclosures rise sharply

BUYERS MARKET II
Market absorbs oversupply
Time on market decreases
Job market increasing
Existing properties rehabbed
Prices and rents begin to slowly increase

SELLERS MARKET I
Supply dwindles
Property selling
Time on market at lowest point
Property prices and rent rising

SELLERS MARKET II
Time on market increases
Supply increases
Seller waits but still gets inflated prices
Construction pipeline excessive
Business and job growth slow

MULTIFAMILY

TREND
trend
/trend/
verb
gerund or present participle: trending

1. Change or develop in a general direction.

ECONOMIC INDICATOR
ec·o·nom·ic in·di·ca·tor
noun
noun: economic indicator; plural noun: economics indicator

1. A statistic used to gauge future trends in a nation's economy.

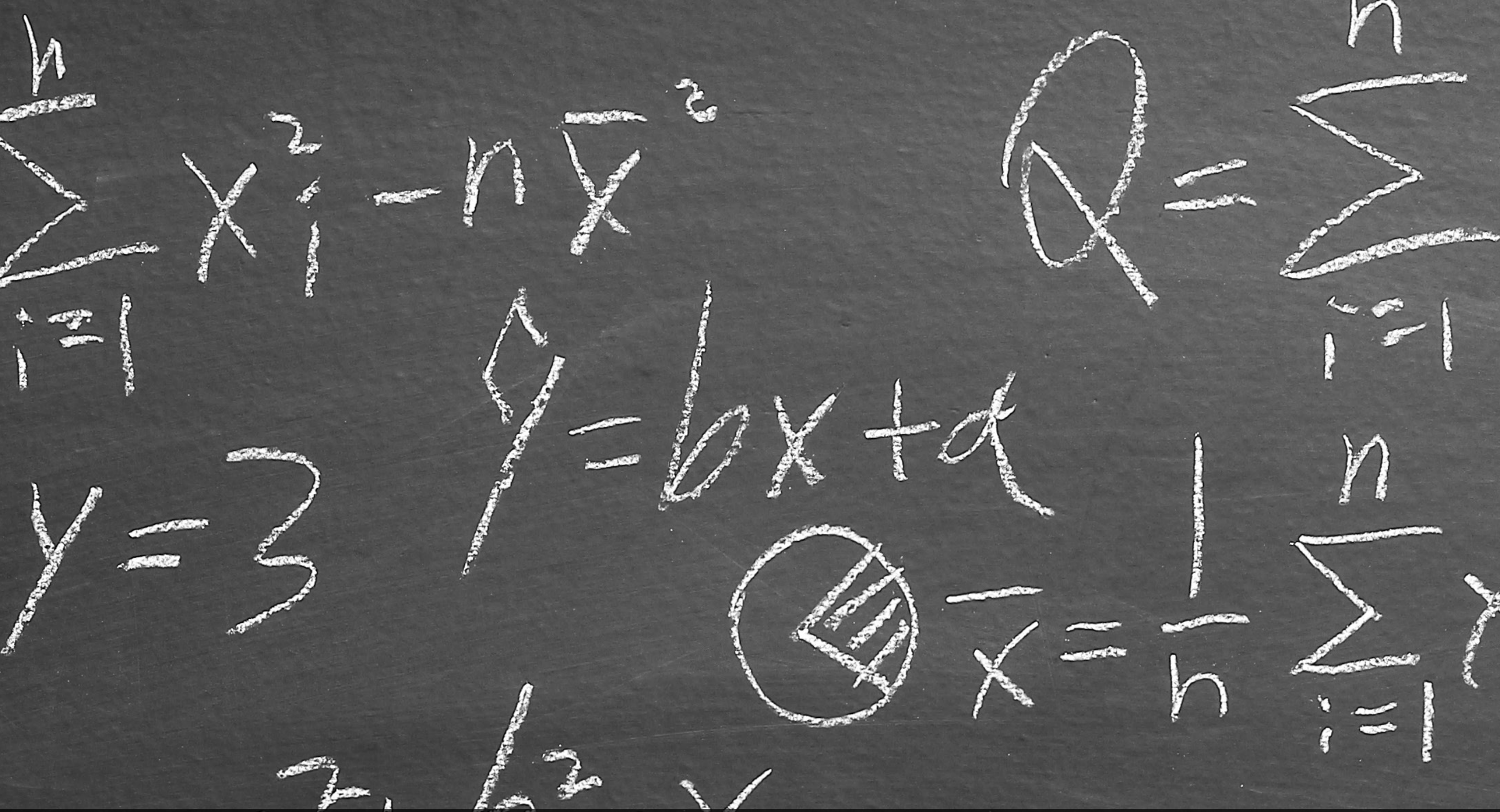
04

CHAPTER 4

FOUR FORMULAS

THE MOST IMPORTANT FORMULAS

04



FORMULA

for·mu·la

/ ˈfôrmyələ/

noun

1. a mathematical relationship or rule expressed in symbols.

2. a fixed form of words, especially one usedin particular contexts or as a conventional usage.

FOUR FORMULAS

THE FOUR FORMULAS USED TO CALCULATE MULTIFAMILY

1. **NET OPERATING INCOME**
   Net Operating Income = Effective Gross Income - Operating Expenses

This is a key indicator of the cash flow of the property before taxes and debt service. This determines the profitability and the market value of the property. This is the number that buyers focus on increasing to force the appreciation of the asset. NOI can be increased by decreasing expenses, increasing income, or both.

2. **CAPITALIZATION RATE OR CAP RATE**
   Capitalization Rate= Net Operating Income / Market Value

The Capitalization Rate is the rate at which the Net Operating Income (remaining income after all expenses have been paid) repays the purchase price on an annual basis.

For example, if you purchased commercial real estate for $15,000,000 and your Net Operating Income is $1,500,000, your Cap Rate would be 10%.

Cap Rate (10%) = Net Operating Income ($1,500,000) / Market Price ($15,000,000)

A Cap Rate is one of many considerations when evaluating a multifamily asset. It is an indirect measurement of how fast an investment returns all principle. This is used to demonstrate the return if there were no leverage on the asset (bank loan).

In the example above, the purchased investment will be fully capitalized after 10 years. If the capitalization rate were 5%, the payback period would be 20 years.

Many investors use entry cap as their main point of reference, however experienced investors will typically use several cap rates and many other data points to properly evaluate a deal thoroughly and to fully understand the opportunity and strengths/weaknesses of the asset.

Other cap rates buyers consider are operating cap rates, buyers entry adjusted cap rates, seller's exit cap rate, and exit cap rates (what cap rate you sell the property at).

Seasoned buyers will stress test the cap rate at exit. The stronger the market, the lower the cap rate.

FOUR FORMULAS

<u>THE FOUR FORMULAS USED TO CALCULATE MULTIFAMILY</u>

3. CASH ON CASH RETURNS

Cash on Cash Return = (Annual Pretax Cash Flow / Actual Cash Invested) x 100%

The Cash on Cash Return (CoC) evaluates how quickly an investor will recover the out of pocket expenses that are invested in the property (equity injection, closing costs, capex, etc).

To find the CoC, simply divide the annual pretax cash flow by the actual cash invested (down payment, closing costs, etc) and multiply by 100%.

4. DEBT SERVICE COVERAGE RATIO (DSCR)

Debt Service Coverage Ratio = Net Operating Income / Debt Service

The Debt Service Coverage Ratio is a ratio that expresses how many dollars of income there are for every dollar of debt. This calculation is very important to understand if the property can produce enough income to cover the debt adequately. Anything over and above the mortgage is profit.

Agency lenders (Fannie Mae and Freddie Mac) typically like to see a minimum of 1.25x on most assets.

Most assets in a hot market are what we call "debt coverage constrained". This means that there is not enough debt coverage to borrow the fully allowed loan to cost. For example, you may be allowed to borrow up to 80% of the cost of the property, but due to debt coverage constraints of 1.25x min, you may only get a loan for 70%. This means you'll need 30% in equity instead of 20%.

FOUR FORMULAS

MARKET VALUE
mar·ket val·ue
/ˈmärkət ˌvalyoo/
noun
noun: market value; plural noun: market values

1. the amount for which something can be sold on a given market.

CAPITALIZE
cap·i·tal·ize
/ˈkapədlˌīz/
verb

1. Take the chance to gain advantage from.

synonyms: take advantage of, profit from, make the most of, exploit

2. Provide (a company or industry) with capital. finance, fund, underwrite, provide capital for, back.

3. Realize (the present value of an income); convert into capital. Reckon (the value of an asset) by setting future benefits against the cost of maintenance.

05

CHAPTER 5

BUSINESS PLANS

COMMON BUSINESS PLANS

05

PLAN

plan

/plan/

noun

1. A detailed proposal for doing
2. or achieving something.

- a scheme for the regular payment of contributions toward a pension, savings account, or insurance policy.

"a personal pension plan"

2. an intention or decision about what one is going to do.

BUSINESS PLANS

There are typically two major approaches to multifamily in the B / C asset class space. They can each be utilized individually or they can be blended together to optimize the opportunity.

TURN KEY VS. MANAGEMENT / YIELD PLAY

VALUE ADD
A value add opportunity is a business plan that places emphasis on adding value to the property through renovations. For example, adding new amenities may cause an increase in market rent.

Renovating the interiors of units lead to higher rent premiums and occupancy rates which is also considered adding value.

MANAGEMENT / YIELD PLAY
Often times properties are poorly managed or mismanaged when the transaction occurs. In this instance, the buyer will focus on increasing operating efficiencies and realizing as much yield as possible on the asset.

For example, if an asset has market rents on all units $100 below market rent, then the new owner may come in and focus on turning over those leases by increasing the rents by a minimum of $100, therefore yielding more income for the asset.

Both are important factors in the syndication life cycle since they affect the NOI.

MANAGEMENT
man·age·ment
/ˈmanijmənt/
noun
noun: management

1. The process of dealing with or controlling things or people.
   "The management of elk herds"

2. The responsibility for and control of a company or similar organization.
   “The management of a great metropolitan newspaper"

synonyms: administration, running, managing, organization; More

3. The people in charge of running a company or organization, regarded collectively.

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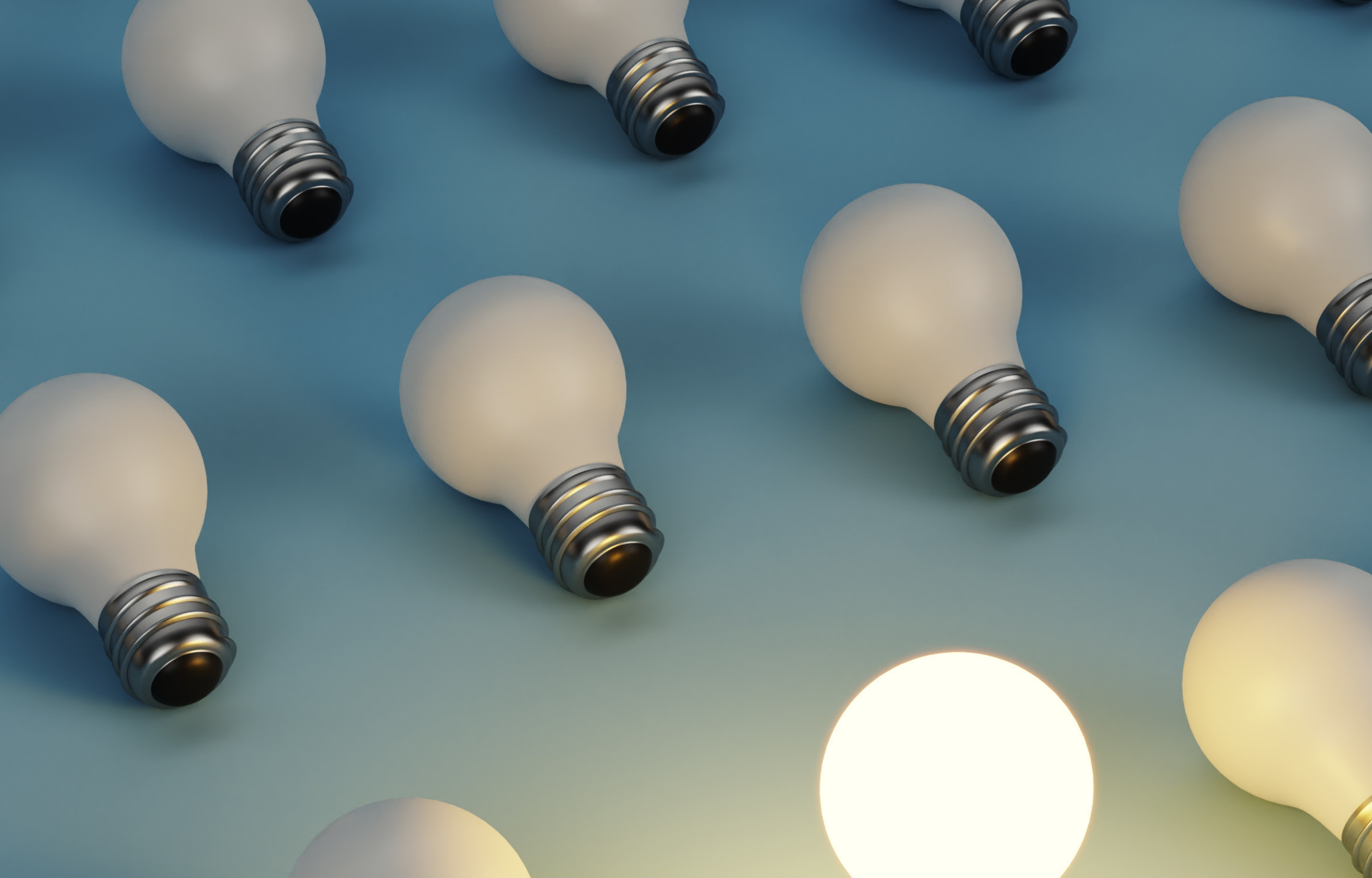
CHAPTER 6

SEIZING OPPORTUNITY

STEPS TO EVALUATE THE DEAL

06



EVALUATE

e·val·u·ate

/əˈvalyəˌwāt/

verb

form an idea of the amount, number, or value of; assess.

SEIZING OPPORTUNITY

There are some basic steps to evaluating a multifamily real estate deal:

SCRUTINIZE THE OPPORTUNITY
The first step when presented with a deal opportunity is to review all the materials presented.

Typically a sponsor will provide an Offering Memorandum which will include detail oriented information about the entire offering. This is a good time to take note of the depth of information.

Consider the factors that you believe are important to the deal-- location, anticipated hold period, risk adjustment, market factors, etc.

LOCATION
Try to understand why this location is a great opportunity. What makes this specific market better than another market?

ANTICIPATED HOLD PERIOD:
What is the anticipated exit on the property? Typically most deals will have a 5-7 year hold period. Determine if the hold period is comfortable for your investment criteria.

Remember, these are not highly liquid investments.

RISK ADJUSTMENT
Typically deals with higher returns than others are risk adjusted returns. This means that the more risk in the deal, the more potential reward.

All investing comes with some level of risk.

As a passive investor, you want to make sure you are choosing deals that are appropriate for your investment goals. You will not have the ability to ask for or make changes to the deal.

MARKET FACTORS
Is this deal overly dependent on any one factor? Has the sponsor used conservative metrics when underwriting the deal?

Remember that no deal goes exactly as planned, so there needs to be plenty of room for a margin of error.

Good sponsors would have evaluated the deal from many angles prior to the offering.

SEIZING OPPORTUNITY

LOOK AT THE DEAL STRUCTURE

Determine if this investment meets your preferred deal structure.

Seasoned investors may look for a preferred equity position on their investment. This hedges the risk for their downside on the asset and incentivizes the sponsor to perform. Although it requires more sophisticated financial skills to underwrite a deal with pref and hurdle structures, it is often times the deal structure high net worth investors look for before investing capital.

Other investors have a higher risk tolerance and have no issues with a straight equity split with no pref.

Know which one you want to see and invest accordingly. If the investment meets your preferred structure, then review the projected returns of the project. This determines how your money is working for you and what your potential ROI is.

When reviewing the returns, make note of the equity split after the pref (if any).

Some sponsors will split 95 / 5 which means that the LP gets the lion's share of the deal, however, make sure you understand why the sponsor is willing to work for such a small return. This can indicate either inexperience or an asset that is being purchased above where it should be. This is not always the case, but experienced sponsors typically only go after great opportunities where there is enough profit margin for both the LP and the GP to make money.

UNDERSTAND THE ASSUMPTIONS

When underwriting a deal, there are some amount of unknown quantities.

As a deal sponsor, risk can be mitigated by collecting as much market data as possible and making certain conservative assumption. Using that as a base model, the GP should adjust the numbers to understand various scenarios and how they impact the deal and returns.

For example, there is no way to know the vacancy of an asset post acquisition. The best way to overcome this unknown is to look at various market data and understand what comparable assets in this market are doing.

So, if three other assets in the area have 5.5%, 5%, and 5.7% vacancy rates, it would make sense to use an assumption of 5-6% vacancy to be conservative.

SEIZING OPPORTUNITY

EVALUATE THE SPONSOR
Once these points are checked off your list, then look at who the offering is from. What is the experience of the sponsor team?

There are many attributes that lead to a successful team including a corporate background, financial experience, management experience, risk management, real estate experience, etc.

Be sure to consider the property management company in this equation since they will be the most hands on day to day.

ASK QUESTIONS
At this point, you should have reviewed the offering memorandum (maybe even multiple times!) and have a very solid understanding of the deal.

The sponsor will usually host a conference call or webinar to add even more color to the offering.

Make sure you ask a deal sponsor any and all questions you have. Don't be shy!

This is your money and a good sponsor will be used to answering all kinds of questions.

MAKE A DECISION
Once you have all the answers you need and feel 100% ready, then let the deal sponsor know you are ready to go for it!

If you don't like the deal for any reason, it's a good idea to give the sponsor feedback on WHY you don't like it. It won't offend a good GP, but rather it will help them steer opportunities that are a better fit your way.

If you decide to move forward, fill out the soft commitment form the sponsor sends and let them know the amount of your commitment.

DOCUMENTS

DO NOT EVER WIRE MONEY TO ANYONE WITHOUT COMPLETED DOCUMENTS.

This seems like a no brainer, but you'd be surprised at how often this happens. Your deal sponsor should send you documents (typically a Private Placement Memorandum (PPM), subscription agreement, and operating agreement.

This often happens via an investor portal or an electronic signature service (DocuSign) for your convenience.

You can review the documents and have your attorney review them if you prefer (remember that these are not red lined documents since every investor must receive the same documents, so don't waste money having them red lined).

After you have completed signing documents and you have received a fully executed copy for your records, you can follow the wire instructions to send your funds.

Until your wire is completed, most sponsors will not consider you invested and you could risk losing your spot to another investor, so it's important to complete these steps in a timely manner.

Once your wire is received, the GP will confirm receipt.

You will also need to submit your bank info at some point to receive returns.

Experienced GPs will often distribute monthly payments to LPs. The first 3-6 months of any investment may not have a distribution or it may be irregular, but after that initial transition period, monthly deposits should be rather seamless.

You will also likely receive monthly updates and quarterly financials for you property so you can keep up with the progress of the business plan.

From here on out, just kick back and relax because this is truly the passive part!

SEIZING OPPORTUNITY

DECISION
de·ci·sion
/dəˈsiZHən/
noun

1. A conclusion or resolution reached after consideration.

2. The action or process of deciding something or of resolving a question.

3. A formal judgment.

4. The ability or tendency to make decisions quickly; decisiveness.

DOCUMENTS
doc·u·ment
/ˈdäkyəmənt/
noun
plural noun: documents

1. A piece of written, printed, or electronic matter that provides information or evidence or that serves as an official record.

SUMMARY

WRAPPING UP

SUMMARY

In conclusion, multifamily is often one of the best stabilized, risk adjusted returns in real estate.

The key to successful investing in multifamily is understanding the deal and choosing a strong general partner.

Historical trends point to low default rates and high returns. Projections for the future of real estate investing continue to indicate that this asset class will remain strong.

Many investors achieve financial freedom through investing in real estate. It is a great vehicle not only to build wealth, but to generate cash flow.

HAPPY INVESTING!

ABOUT THE AUTHOR

VEENA JETTI | MULTIFI
FOUNDER | PARTNER
Multifamily Owner / Operatpr & Philanthropist.

Veena Jetti

"Creating relationships and helping others succeed is at the core of my values. I love to be surrounded by strong, successful, like minded individuals." - Veena Jetti

Veena Jetti is a founding partner of MultiFi, a unique commercial real estate firm that specializes in curating conservative opportunities for investors.

Veena brings a dynamic perspective to targeting, acquiring, managing, and operating assets using best practices combined with cutting edge technologies. Her professional expertise includes driving corporate strategy and business development opportunities.

After graduating from the University of Illinois at Chicago with a degree in Finance at 20 years old, she pursued her passion for real estate. Veena has over a decade of real estate experience and over $1B+ in real estate assets over her career in both the startup world as well as the corporate world.

Because of her diverse background, she is often a panelist and speaker for various podcasts, global conferences, and radio shows.

Aside from professional endeavors, Veena is a passionate philanthropist. She has founded and served on the board for a national non-profit organization. In 2017, she was one of only three women to receive the Politico Woman of the Year award for the significant amount of time and focus she spent on aiding in a grassroots Hurricane Harvey disaster response. She continues to be involved in helping companies and charitable organizations develop better disaster recovery protocols for future emergencies.