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Tips for Buying and Managing Multi-Family Real Estate

By Bryan Haines, Vice President, Commercial Real Estate

Owning multi-family real estate has historically proven to be a sound investment, and it continues to be, even with the changing economic environments. However, buying and holding multi-family real estate as an investment is a business—in order to be successful, you need to approach it as you would any other business venture. You should have a business plan that analyzes your strengths, weaknesses, opportunities, and threats. Without developing a sound plan, you open yourself to unnecessary risks down the road.

A successful plan begins with a mission statement clearly expressing your purpose and the benefits of what you intend to create, such as your required return on investment (ROI). This is "the why" and it forces you to identify your short- and long-term objectives. By setting your goals, you'll be better-equipped to determine how many properties you want to hold, the boundaries of your geographic footprint, how much liquidity you will need and how much debt you are comfortable with. In addition to establishing a timeline for reaching your objectives and evaluating goals, you should clearly define your exit strategy. How you are going to exit the deal? What is your end game? Your business plan should also address the following:

- Market analysis and research. Define your competition, your available resources, and where you fit in the market
- Cash flow requirements. Understand and outline your current and future capital and operating needs
- Current market trends, rates and revenue projections
- Criteria that properties must fall within and how long you intend to hold properties

Remember that your goals may evolve over time and your strategy will evolve with them, and that's okay. By creating and maintaining a detailed business plan you are much more likely to achieve both your short- and long-term goals, understand the opportunities available to you, and allow you to withstand changing market conditions over the lifetime of your investment.

Smart buying decisions are key

Establishing criteria for your decisions, as outlined in your plan, will help guide you in your research. Doing your due diligence is of paramount importance in making smart buying decisions. Oftentimes, you will need to utilize outside sources to help you evaluate investment opportunities. For example, a strong accountant can help analyze the numbers and confirm that the cash flow meets your business plan criteria and the property will generate your desired return on investment (ROI). Be sure to consider whether you have sufficient capital to buy and maintain the property or how much you will have to borrow. Confirm that the rent roll accurately depicts the current tenant base. Look closely at the operating expenses—are they within the industry norm? As a rule of thumb, these are normally about 50% of gross rent.

In addition to the financial analysis you will also need to investigate the building and surrounding area. A property inspector can help determine if there are any deferred maintenance items. An environmental engineer can help reveal if there are any environmental issues. A good title company will help you understand if there are any title issues with which to be concerned. Lastly, be mindful of issues unique to the surrounding area that could affect the building. These could run the gamut from new development, other recent real estate sales, retail options in the vicinity, or access to transit options.

Remain objective

Before buying investment real estate, be aware of the most common error investors make when buying: becoming emotionally attached to real estate. Your plan revolves around hitting your goals and making money, not owning a building because you like it. If you overpay for a property, it can negatively affect all other aspects of your plan; such as your ROI, hold time of the property, liquidity, ability to withstand a downturn, and future growth of your real estate portfolio. Overspending can also eat up your funds that could have been put toward another opportunity.

In many respects, buying real estate as an investment is like buying any other type of investment. You need to formulate a plan, do plenty of research, and make well-reasoned decisions. Don't be pressured into a purchase you're not ready to make; take your time to get all the answers before you buy. If the property doesn't fit your business plan, be willing to let it go, and move on. Furthermore, don't try to time the market. It's no more successful a strategy with real estate than it is with the stock market.

Managing your properties

To ensure success with multi-family real estate, you not only need a plan for buying properties, but for managing them as well. Get organized and be sure you have systems in place to track income, operating and capital expenses, security deposits, and maintenance orders. In addition to accountants, there is also software that can help track your income and expenses, rental payments, and security deposits. Software solutions are also available to help you communicate with your tenants electronically as well as to schedule and track maintenance requests. A great source of information for managing multi-family properties is the Minnesota Multi Housing Association (MHA), which provides classes and resources to help you with everything from maintenance and tenant issues to the most current law changes affecting compliance issues.

Be sure to budget for maintenance and have a plan as to when you will make major repairs. At acquisition, establish when major items—such as windows, roof, boilers, etc.—will need to be replaced. Ensure you budget enough reserves to replace these items in a timely manner. Failing to plan for capital improvements can cost you the building, so review maintenance issues annually and follow your plan. Remember, you want the building's value to appreciate, so plan on making improvements every year—a well-maintained building will help attract quality tenants.

One of the most important priorities for maintaining a building's value is maintaining a solid tenant base. Once again, the MHA can help you with your due diligence by providing you with best practices for background checks and the leasing application process for your tenants.

As the building owner, be responsive and provide high-quality service to your tenants. A good rule of thumb is to respond to all requests within 24 hours. This includes inquiries about leasing, maintenance requests and other tenant questions. Not only should you treat your renters with respect, but you should extend those same values toward your business partners, clients, and associates. Effective real estate investors take care in presenting their business in a positive, professional manner.

Expertise you can rely on

If you are looking for connections to help you with your multi-family real estate plan and goals (accountants, inspectors, environmental engineers, etc.) or would like more information about financing multi-family real estate, contact me or one of my commercial real estate colleagues at 952-831-6600.

About the Author

Bryan Haines | Vice President, Commercial Real Estate
email: bryanh@fidelitybankmn.com | phone: (952) 830-7230

Bryan Haines has over 18 years of experience in a Commercial Real Estate-focused banking career. His exceptional analytical skills and meaningful relationships with established real estate investors have helped him develop and maintain portfolios in excess of $50 million. Bryan gradated from Gustavus Adolphus College with a Bachelors in Mathematics. He is also a graduate of the University of Wisconsin Graduate School of Banking.