Financial Advisory

In a Tough Real Estate Environment, Are Partial Interest Properties Worth a Closer Look?

BY CHRISTOPHER MILLER, MBA
SPECIALIZED WEALTH MANAGEMENT

Writing about the current Coronavirus/social unrest-fueled economy is challenging since all my articles are composed almost two months in advance. As I sit at my desk in early June, I am trying to envision what our economy will look like in mid-July. Maybe some miracle will happen and the economy will look like it did back in January. Perhaps, driven by hundreds of small-business failures, we will be in the beginning stages of a recession. In the case of the former situation, we can talk about how to best prepare for the next recession. If the latter example comes true, we'll discuss the best properties to buy in a slowing economy.

My opinion, as I said in my May article, is that the best properties to buy in both situations are the same: Necessity Retail and Essential Multifamily. My clients are mostly experienced investors who have owned and operated real estate for close to 30 years or more. At this stage in their life, they are not seeking to make their fortunes: they have already done well and are looking to keep what they have – while maintaining income and growth potential. This more conservative approach serves them well.

THE CASE FOR GETTING OUT OF CALIFORNIA

I am currently in the process of sending some mailing business out of state because all the print shops in California seem to be closed. How many other businesses in the state are doing the same thing? How much of this business will come back to California in time? Even if "most" of it does – that still leaves lost revenue hurting our bottom line here.

For years, my investors have been looking outside of California for better growth opportunities. Our current economic situation may work two ways – by stifling growth in our state, and providing more growth in others as businesses and workers flee in search of more opportunities.

Please turn to page CS-19

Christopher Miller is a Managing Director with Specialized Wealth Management and specializes in tax-advantaged investments including 1031 replacement properties. Chris' real estate experience includes work in commercial appraisal, in institutional acquisitions for a national real estate syndicator and as an advisor helping clients through over four hundred 1031 Exchanges. Chris has been featured as an expert in several industry publications and on television and earned an undergraduate business degree and an MBA emphasizing Real Estate Finance from the University of Southern California. Chris began his real estate career in 1998. Call him toll-free at (877) 313 – 1868.

Continued from page CS-16

WHAT IS KEEPING MANY FROM LEAVING

"Let's buy outside of California," sounds like a good plan, but many investors find that much easier said than done. Managing a property in town is hard enough. How do I manage a property that is a 2 (or more) hour plane flight away? Showing units or arranging repairs just can't be done from such distance – is it possible to find an out of town property manager that I can trust enough?

A POTENTIAL SOLUTION IN PARTIAL INTEREST PROPERTIES

Partial interest properties are one option for investors looking to move their capital to another state. Though such an arrangement, we can buy part of a larger, institutional-grade asset such as a 300-unit apartment complex in the Atlanta suburbs or a CVS Pharmacy in Dallas. Within my selection of properties, the offering investment companies will also stay on as the manager after your purchase. So, you are hiring a management company: a much larger entity. It is easier for us to do our homework on them: their management track records are available for review, and I have been working with some of them for almost 20 years. Sometimes finding service providers means calling numbers out of the phone book and interviewing them from there. In the case of partial interest properties, it is more like hiring a contractor that a trusted neighbor has used with success for over a decade.

In addition to providing an easier way to invest out of state, partial interest properties can also offer:

DIVERSIFICATION POTENTIAL

This crisis has taught us the danger of putting all our eggs in one basket. Companies that own hotels, movie theatres or malls are in serious financial trouble now. (As I have said in past articles – those that own hotels shouldn't be surprised; they always get hammered in a recession.) More diversified companies who focus on necessity retail and essential multifamily are performing better.

Through partial interest properties, we can invest – for example - $2 million of equity into some apartments in Dallas, another apartment property in the Washington DC suburbs and a nationwide portfolio of net-leased necessity retail properties. We can diversify our portfolio by geographic region, tenant, industry and even by property manager. Such diversity is hard to replicate when buying "on our own," particularly if we need to hire multiple managers in many states.

PERHAPS MORE GROWTH POTENTIAL

As I said earlier, and as I have been saying for many years, I think there is a good case to be made for better appreciation when buying outside of California. First, to get good appreciation you'll want to buy at a lower price – and CAP Rates (a measure of purchase price relative to income generated) are usually much more attractive to buyers in other states. Next, many believe that California has seen all the explosive growth that we are going to – we have simply run out of room to put everyone. The last 30 years have been great for California. Now it may make more sense to look for other areas of the country with the potential to grow like we did over the next 30 years. Finally, the regulatory environment in California certainly isn't doing us any favors. How is California addressing the pressure on retailers from online sales or the financial trouble that many of our restaurants and other "mom and pop" businesses are facing? There's currently a measure on November's ballot to repeal Prop 13 for commercial properties and significantly raise taxes on all those businesses! (in commercial leases, any expenses are often just passed directly to tenants.)

Over the past few months, business has slowed across much of the real estate market. Many expect that to change towards the end of the year as investors look to revise their holdings based on "our new reality." If you have any questions, please call my office at (877) 313-1868.