FAMILY WEALTHREPORT

Q&A: Investing In Real Estate With Waypoint Residential

Here is a Q&A with Scott Lawlor, founder and chief executive of the real estate investment manager Waypoint Residential.

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Q: First of all, could you please talk briefly about your firm: what led you to found it and where is it based/where does it have a presence?

Following the financial crisis we looked at various parts of the real estate market and based on our initial research we thought that there were some interesting dynamics in the multi-family housing sector. So we decided to explore this deeper and once we got into it, we realized it was even more interesting than we first thought and formed Waypoint Residential five years ago to take advantage of this market opportunity. The dynamics we observed have played out and the apartment sector has been on a terrific run for the last five years and we think it still has a long way to go.

Waypoint is based in Boca Raton, with offices in Stamford, CT, Chicago, Dallas and Atlanta, and properties throughout the Sunbelt and Midwest.

Q: Do you have any measures which demonstrate how you have grown so far? Any targets for future growth?

Thus far we've done 50 deals with a total value of $1.4 billion. Our focus is on growing the organization and expanding geographically. We will be opening a Chicago office this year and a western office, possibly in Denver or Phoenix, sometime in 2017. We are also looking to grow within the rental housing sector itself, in some areas of specialization, such as student housing and senior housing.

Q: How does Waypoint fit in in the marketplace; who are your clients?

We don't think there are very many real estate investment managers who are focusing on the private capital community in the way that we are and to the extent that we are. Whether it's a wealth manager or a family office wanting an allocation to real estate, we provide an alternative that doesn't exist elsewhere – the ability to build and customize a diversified, income producing, tax-efficient real estate portfolio. For this market exposure, you had to previously go into discretionary institutioanl funds, publicly traded or non-traded REITs or the ad hoc syndicated deal that comes across your desk. I don't know of any other real estate investment managers that are providing an institutional caliber real estate investment management capability to private investors.

Q: Within real estate investing, where are your areas of focus?

To date we've been focused on conventional multifamily in the Sunbelt region of the US and recently expanded into the Midwest with a deal in Chicago. We're doing both ground-up development deals and buying value-add properties where we can bring to bear our operating capabilities that improve the performance of the real estate to create value for the investors. We've been looking closely at the student housing sector and believe it can become an important line of business for us, and then we may look at senior housing. Geographically, we're looking to expand further west, so maybe a year from now I would define the geography as a Miami to Chicago to Phoenix triangle.

Q: How does the way Waypoint invests in real estate compare/contrast to more "traditional" approaches?

From an investing perspective, we are more willing to play outside the center of the fairway when it comes to real estate risk. We look at smaller markets where institutions don't play, we look at sub-markets that we think the institutional community doesn't yet understand, and we're comfortable in deals where there is some form of distress.

From a capitalization perspective, we are a little more conservative than others. We use less leverage, even though debt is cheap, because we are really trying to create long-term, very reliable cash flows for our investors, not necessarily maximizing our IRR.

Q: Do you have any results to back up your strategy?

We look at overall return, current return and operating performance as measures of success. From an IRR perspective, we have sold or recapitalized 14 investments, and the weighted average IRR to investors has been 26 percent. From a current return perspective, every property has distributed at or higher than the promised distribution every month. We're currently distributing at about 7.9 percent across the poprtfolio. As for the operating track record, this year's budgets are are aproximately 1.5 percent higher than the 2016 underwritten NOIs that were in our PPMs that we sent to investors when we initially acquired the deals two to three years ago.

Q: How do clients tend to use real estate as part of their overall investment portfolio?

They use real estate to get some diversification away from the securities markets, which are very volatile, and they use it to generate current return. They also like to invest because it's very efficient from a tax perspective because depreciation offsets the current return. We also allow our investors to defer capital gains by using a 1031 exchange into a subsequent investment.

Q: What kind of investor profile is best suited to these types of investments?

We serve a wide range of investors. From high net worth individuals to family offices, wealth mangers and registered investment advisors. We have investors who put $100,000 into our deals and we have some who invest much more. Our investors are also international, so beyond the US we also serve clients in Latin America and Europe.

Q: How do you identify and source them (investments)?

We have both an acquisition team and a development team whose jobs are to source our deals. This is a group of about a half dozen folks that average 25 years of experience who are on the road looking at deals every day.

Q: What are the biggest risk factors associated with the areas of real estate that you focus on – for the firm and clients – and how do you mitigate these?

You can take the risk out of investing in the multifamly space just like other property types by how you manage your capital stack, how much leverage you use, and whether you're able to have a long-term view. It would be very risky to say you want to do a deal with 80 percent loan to value that you have to sell in 2 years in order for it to work. In that case you're making a bet that the market will stay hot and that two years from now you'll be able to sell. We don't do that. We use 60 percent debt so we know we can ride out the downturn if need be. If you have flexibility around your holding period and a capital stack that will let you endure cycles during that holding period then you take quite a bit of risk out of it. This allows you to ride out downturns and capitalize on upturns.

Q: What trends, including geography, are you seeing in the real estate investing sector, and how do you see the industry developing over the next five years?

From a capital perspective, all the great things happening in the apartment space have attracted a lot of capital and made it very competitive, so as a result we avoid the places where you have 50 firms bidding. As I mentioned, we play outside the center of the fairway when it comes to deals.

I have a strong belief that all the terrific market drivers in the apartment sector have a long long way to go. There will be cycles, and there will almost certainly be a recession at some point over the next five years, but we'll be able to ride it out. More importanly, in the apartment sector, all of the things that are driving the market – shifts in the home ownership pattern, demographics, and other cultural trends have nothing to do with the next cycle. It doesn't matter if GDP growth is 4 percent or 1 percent, or if the jobs report is 250 thousand a month or 100 thousand a month. These have nothing to do with the demographic and other cultural shifts driving the sector, which is well positioned to keep going for a long time.

Q: Please share any other thoughts you have on this topic and how it pertains to family offices/high net worth investors.

I think it's important for investors to focus on three things when it comes to thinking about investing in multifamily real estate. First, we're conservative with regards to leverage and apartments offer less volatility than other sectors such as office buildings or retail. Second, we're very focused on current return. If you can distribute at 600 basis points over the treasury with a conservative risk profile, that's very attractive. And lastly, tax treatment. The ability to offset current income with depreciation and to defer taxes is very important high net worth investors.