REAL ESTATE IN THE POINTES
PARTNERS IN REAL ESTATE

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EXECUTIVE SUMMARY

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PROPOSED:

That income-producing Multi-Family Housing (hereinafter, MFH or Apartments) be acquired … and then, optionally, managed through the formation of separate Michigan LLCs (Limited Liability Companies), one for each property. Each acquisition (and LLC) will be made by two (2) to four (4) participant Buyers.

Procedurally, once a property is identified, scrutinized and targeted for acquisition the **Buyers/Investors will move jointly together for acquisition and closing**. The buying groups will consist of 2 to 4 individuals. **Some will have been previously acquainted while others may have been newly introduced and matched through this office.** Thereafter… and at the group's option … each Buyer may secure membership units (synonymous with shares) in a newly formed Michigan LLC for the purpose of owning and operating the house. Each member's units will be a percentage which directly reflects his or her capital contribution toward the property's total cost.

NOTE: Multi-family housing to be defined as a 2-Unit House, 3-Unit House, or a 4-Unit House. Collectively, sometimes referred to as Apartments.

RATIONALE

WHY MULTI-FAMILY HOUSING IS A GOOD INVESTMENT

In Multi-family investing, it's good to be a landlord. Interest rates and apartment vacancies have remained low over the past several years and are projected to remain this way for years to come. Further, investors can shield some of the cash flows generated by income producing property on their tax returns due to depreciation, and private equity real estate investors are able to access an expanding pool of attractive debt capital today. That explains why nearly 60% of all commercial lending dollars, which will reach $700 billion in 2020, according to the Mortgage Bankers Association (MBA), will go to Multi-family projects.

In fact, continued low interest rates prompted the MBA to raise its 2020 forecast on Multi-family lending activity to $390 billion - a record high. At the start of 2019 the annual yield on 10-year Treasury notes was predicted to move upwards of 3%. Instead, long-term rates have stayed closer to 1.5%, with expectations that private equity real estate will have continued access to this low-cost capital.

Mortgage bankers aren't the only professionals looking forward to a productive year for Multi-family housing. National Real Estate Investor's sentiment survey, released in November 2019, ranks it the most attractive type of commercial real estate investment. Here are a few reasons why Multi-family housing will continue to be a good investment in 2020 and beyond.

1. **Multi-family Money Is Readily Available.** Banks are providing more debt capital for apartments, which makes getting approved for mortgage loans easier than for other property types. New figures from the Mortgage Bankers Association's Annual Report on Multi-family bank-lending indicate lending grew to $100 billion in 2018. But Multi-family projects have an even bigger source of capital, one not available for office, retail or other commercial real estate projects. The mortgage bankers report that 42% of Multi-family loan capital, or $142 billion out of $339 billion in 2018, came from the government sponsored enterprises Fannie Mae and Freddie Mac. By encouraging a liquid loan market, Fannie and Freddie have made it easier to buy and sell Multi-family housing.

2. **Multi-family Loans Carry Less Risk.** Debt accounts for 60% to 80% of the capital stack (a description of the totality of capital invested in a project, including risk elements) in most private equity real estate deals, with investors contributing the remainder. While all types of commercial real estate stand to gain from an extended stretch of low interest rates, Multi-family housing has one big advantage from the lenders' standpoint: Rental income comes from a diversified pool of tenants, which makes Multi-family lending a lower-risk proposition. Office or retail properties are built around a few anchor tenants, which are not always easy or cost-effective to replace. A loss of rental income can be extended and the cost to re-tenant can be substantial. Multi-family vacancies tracked by CBRE (a national broker of commercial sales and leases) are at their lowest since 2000 and well-occupied properties produce higher cash flows.

3. **Apartments Provide Steady Income.** The average five year cash flow of Multi-family projects in the NCREIF (National Council of Real Estate Investment Fiduciaries) Property Index is 8.58%, an enviable rate for a dividend stock.

4. **Rental Demand Remains Strong.** Multi-family housing has gained a comparative edge in tenant demand. Regardless of the state of the economy, people need a roof over their heads. What's more, momentum has shifted from condo to apartment development. Homeownership has

dropped to 1970s and 1980s levels in the United States, the Federal Reserve Bank of St. Louis reports. Downsizing baby boomers are losing interest in owning, many millennials delayed or abandoned home buying plans, and Generation Z, now coming of age and the largest cohort to ever live, is entering the housing market with rentals first.

5. **Multiple Options for Multiple Price Points.** Demand is also strong for older Class B and Class C Multi-family housing (Classes segmented with respect to amenities, level of deterioration, etc.). Owners often seek private equity real estate partners to provide capital for value-add renovations that will justify higher rents. These buildings can be efficiently managed without major renovations, making them profitable investments. Also, communities offer subsidies to landlords who house teachers, police and other median-income tenants. The City of Grosse Pointe Park offers these for student and educators, for example.

6. **Improvements Unlock Hidden Value.** Reinvesting in a property through capital improvements and property enhancements can have a nearly immediate payback because then they can command higher rents. Renters are generally willing to pay more if the improvements are of something that they value and receive a benefit from using daily such as appliance upgrades, in-unit smart home technologies such as Nest cameras and thermostats and package locker systems.

7. **Rentals Extend Record of High Returns.** In successive five-year periods, Multi-family properties in the NAREIT (National Association of Real Estate Investment Trusts) index have outperformed other commercial real estate shares. At the same time, the apartment sector has been less volatile than its office, industrial or retail peers throughout a quarter-century of returns, generating superior absolute and risk-adjusted performance.

8. **Rents Keep Pace with Inflation**. Year-long lease terms position apartments to benefit from improving market conditions. When wages rise, rents can move higher as well, while commercial properties are locked into multiyear leases. Staggering lease expirations through the peak spring and summer rental periods when rent prices can be maximized is a good strategy.

9. **A Refi Can Offer Immediate Payback.** Investors don't have to wait until a building sells to realize gains. By refinancing their loans, they can borrow against the property's higher value without incurring the taxes on capital

gains that come with a sale. Multi-family property owners can refinance as often as they choose during their ownership, collecting tax-free distributions every time.

The above advantages are intrinsic to Multi-family properties.

Why Millennials Aren't Buying Homes

Affordability, high student debt and less loan availability are just a few of the reasons that millennials aren't buying homes at the rate of previous generations. Urban Institute (the Washington D.C. based research think-tank) reports that 37% of millennials own homes in 2015 – a full eight percentage points lower than Generation X and baby boomers at the same age.

1. **Affordability**
   Buying a home won't be easy for millennials as the affordability gap continues to widen. According to the National Association of Realtors (NAR), the home affordability index for first-time buyers in 2018 dipped to 92.5. A value of 100 means that a family with median income has exactly enough income to qualify for a median-priced home. In 2015, the index was 109.3. The index is an average across the U.S., so there are areas of the country that are more affordable. The question is whether or not millennials are willing to relocate and leave jobs, friends and family in order to buy a home.
2. **Not Married (or Partnered) Yet**
   In 2018, less than 60% of people aged 25 to 34 lived with either a spouse or partner versus 80% in 1967. The changing dynamic of getting married and having children means that millennials are staying at home longer and delaying the purchase of their first home. The average age of a first-time mom is 26.6 as of 2016 according to the Centers for Disease Control (CDC), although the age increases for college-educated women and women in urban areas.

   Additionally, people are getting married later, with the average marriage age at 27.4 for women and 29.5 for men, according to 2017 figures from the U.S. Census Bureau. "Life events such as getting married or having children are typical triggers to buying a home. The longer this age group lives with parents or independently, the more homeownership will be delayed," stated Bank of America in a report about millennial home buying trends.

   Later marriage and delays in having children has helped increase the percentage of millennials living at home or with relatives to 22.5% in 2018, up nine percentage points since 2005.

3. **High Levels of Student Debt**
   In 2018, student debt in the U.S. hit $1.5 trillion and has become a burden on millennials trying to enter the housing market. That same group has also had to contend with stingy wages and raises in much of the job market, putting added strain on paying off those loans. According to the 2018 NAR report, more than 50% of homebuyers under age 36 said that student debt delayed their home buying. Apartment List (a free service which assists in finding apartments) estimates that while college grads without student debt need 7.6 years to save for a 20% down payment in 2018, those with debt need to save more than four years longer.

4. **Tighter Lending**
   Banks have tightened credit underwriting to reduce risk and have double-downed on the 20% down payment rule for homebuyers. But as house prices rise, it is taking millennials longer to accumulate enough cash to put down on a home. "Remember that the bulk of the current 25 to 34-year-old cohort started their careers during the financial crisis and early stages of the recovery, when the economy and labor market were fragile," Bank of America noted.

   While mortgage affordability programs may offer loans with less than 20% down payments, lenders will often charge higher interest rates on these loans to offset the greater default risk. Additionally, most of these mortgages will require that millennials take out private mortgage insurance, making monthly payments even higher.

5. **The Lure of Bright Lights**
   Millennials continue to flock to cities. Pew Research found in 2018 that 88% of millennials live in metropolitan areas. Whether it's a social movement or the lure of greater work opportunities, millennials are moving towards regions with a higher proportion of renters compared to homeowners, pushing up rental prices in the urban centers where they prefer to live. So far, millennials seem unwilling to commute or own a backyard. According to BuildZoom, new home sales within five miles of the centers of the 10 most densely populated cities have exceeded 2000 levels but sales are about 50% below 2000 levels 10 miles outside the city.

   Much has been made of millennials and their spending habits in the big cities: new clothes, Amazon Prime, the latest iPhone, daily Starbucks. However, Bureau of Labor Statistics data debunks this notion: Expenditures on apparel and entertainment fell 1.4% from 2004 to 2015. The biggest decrease in millennials' shopping basket:

> spending on "owned shelter," which dropped 2.6%. Meantime, spending on rental shelter had the largest increase, rising 3.2%.

Housing prices continue to rise in the U.S. and while millennials are delaying home ownership, evidence suggests ownership is not out of reach. While some financial constraints remain, such as student debt and down payments, social changes in how young adults are living have pushed home ownership to record low levels and have seen the average age of millennials staying at home rise.

In summary, **the acquisition of Multi-Family housing has a wide appeal. For those who are interested in being an occupant-owner (living in one unit and renting the other units) … or, for those strictly looking for an investment … benefits can be richly earned.**

By being part of a Buyer's group, the barriers to entry to becoming a Landlord are significantly lowered, while at the same time spreading any associated risk.

One example of the many scenarios which may emerge from this buying approach, is:

a. A Multi-Family house becomes available for sale.
b. The current down payment requirement is 25% of the sales price.
c. A millennial has been restricted from buying due to lack of down payment funds.
d. By participating in a Group structure with … for this example 3 other parties… the millennial need only come up with funds equal to 25% of the overall 25% down payment.
e. Further for this example, let's say the acquired house is a 4-unit building … the millennial occupies one of the units and pays rent to him/herself and the 3 other members of their acquiring LLC.
f. Later on, when selling the property, the millennial will have built equity, instead of simply wasting dollars on rent.

Note: Further, another important benefit to all 4 of the owners/landlords is that one of them is always living on-site to monitor the property.

Whether one is a well-heeled or has just enough for a small down payment, being part of a purchasing group makes good sense. It increases one's purchasing power and mitigates risk.

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STRUCTURE OF PROPOSED MULTI-FAMILY HOUSING ACQUISITIONS

Each of the targeted properties will be profiled and subjected to the usual scrutiny of visitation, professional inspection, examination of tenant histories and leases, and follow the ***ad hoc Landlords***TM methodology.

Once a property is deemed desirable for purchase, and an acquisition is executed, the group may wish to form a new Michigan LLC to serve as the vehicle through which the parties (of 2 to 4) will own and operate the property. If everyone in the Group agrees, the house will be transferred into, and become an asset of, the LLC. Shares/units of the LLC will reflect each member of the groups individual percentage of ownership which will be equal in percentage to the amount of capital he/she has contributed to the total purchase.

Those wishing to have opportunities made available to them for analysis will, first, enter into a Buyer's Agency Agreement with this office. Thereafter, a search for available houses will be conducted and pertinent data will be disseminated to all those wishing to become part of a buying group.

When a group has been formed and expressed a full interest (*i.e.*, 100% is spoken for) in a specific property a CONTRACT FOR THE SALE OF REAL ESTATE will then be executed and submitted to the appropriate Seller.

Optionally, and upon acceptance by the Seller and the setting of a closing date, this office is able to provide additional and essential fee-based services (both short and long-term), such as:

- Guidance in forming a Michigan LLC (if desired by the buying group)
- Advertising for rentals
- Provision of best-practice Lease
- Collection (and subsequent distribution to members) of rental income
- Year-end earnings summary for use by members for individual tax preparation
- Coordination of contractor repairs
- More (as may be required)

Please see attached GROUPINGS PER PROPERTY and PROCESS FLOW & PARTICIPANT REQUIREMENTS (Examples/Graphics).

Consider being part of a landlord group in owning a Multi-Family House. Building equity (and value) with your dollars is always better than rent!

For more information, or if you wish to become involved in this Michigan-based Real Estate opportunity, please contact ***ad hoc Landlords*** TM:

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