Castle Lanterra Properties

The importance of evaluating market 'intangibles' when making real estate investment decisions

Recently, **Jonathan A. Schein,** senior vice president and managing director of global business development for Institutional Real Estate, Inc., spoke with **Elie Rieder,** founder and chief executive officer of Castle Lanterra Properties (CLP). Following is an excerpt of that conversation.

Tell us about CLP's approach to identifying growth markets.

We have a long-term controlled growth investment strategy, so we invest primarily in burgeoning submarkets with strong track records of job growth and industry diversification. Our strategy involves identifying compelling opportunities to acquire and modernize workforce multifamily communities in markets across the U.S.

With 65 percent of millennials renting, as opposed to 37 percent of Americans overall, we tend to seek markets with significant millennial in-migration. We don't limit ourselves by geography; our 7,000-unit portfolio includes multiple properties in nearly every region of the country.

Of course, the supply part of the equation is also important, and we look for markets with favorable supply/demand dynamics and, when there is a significant supply pipeline, a strong rate of absorption.

With this approach, we aim to unlock intrinsic value and provide our investors with above-market returns.

What do you take into consideration when evaluating an area's "human" elements, such as workforce and population trends?

We put a major focus on evaluating an area's intangible factors as part of our analysis. Generally, we always want to be buying properties that have proximity to job centers; a diverse economy; highly rated school districts; convenient access to mass transit; strong retail, entertainment and dining options; and high homeownership costs, which drive residents toward renting.

When we invest in a property, we also feel that we have a responsibility to the community itself — beyond the walls of the property we acquire. We take the notion of "doing well by doing good" to heart, and always try to work with local stakeholders to promote community programming and social events, including creating college internships and university scholarships for local residents.

In what ways does CLP look beyond the traditional snapshot of a property's fundamentals when determining intrinsic value?

Like any investor, a key part of making any deal work for us is the strength of the underlying numbers in the rent rolls, operating statements and pro formas. But we pride ourselves in taking this rigorous financial analysis and building off of it. Our executive team is highly experienced in evaluating opportunities, and they look at a wide range of intangible attributes that can determine a property's success or failure, including the makeup of the tenant base — tenants' income, jobs, lifestyle preferences, etc. And, importantly, our team is nimble enough to evaluate these considerations quickly to seize timely opportunities.

A property's fundamentals are also tied to the broader market, so factors like proximity to mass transit and the stability of the local economy are of paramount importance. Ultimately, after our holistic analysis of the property and the market, we need to see both solid underlying fundamentals and meaningful growth potential to make an investment.

Regatta Sloan's Lake

Regatta Sloan's Lake, a 369-unit rental property located in Denver, Colo., features first-class amenities, including an expansive resident clubhouse; two outdoor courtyards with a resort-style pool, outdoor movie wall and grill areas with fire pits; a fifth-floor amenity deck; a fitness room; and a dog wash room. The property is the centerpiece of a larger redevelopment of a 19-acre former hospital campus. When completed, it will include up to 150,000 square feet of office, retail and for-sale luxury condominiums. Just one block from Sloan's Lake and the 177-acre park surrounding it, the property offers immediate access to walking, jogging, biking, kayaking, fishing, boating and waterskiing.

Lumen Apartments

Lumen Apartments is a 108-unit rental community located in Everett, Wash., approximately 25 miles north of downtown Seattle. Built to Green Certification, the property features a 3,000-square-foot rooftop with views of Puget Sound and the Olympic Mountains, as well as controlled access to underground parking across two levels, and a cardio room. Retail tenants include the popular Mazatlan Mexican eatery, a health clinic and an engineering firm. Lumen Apartments is located in Snohomish County, which boasts a well-educated employed workforce of over 400,000 people.

How do supply/demand dynamics play into your investment decisions?

Even with all the development during this cycle, in most markets, there really hasn't been much construction of workforce housing. A significant number of residential developers have focused on the luxury market, which has become oversaturated, while governments put their energies behind increasing the affordable-housing stock. Meanwhile, few entities have developed accessibly priced apartments for middle-income families, so supply/demand dynamics for us are often favorable.

That said, we don't only invest in markets where demand for workforce housing outpaces supply; we also intentionally invest in areas with a high barrier to new development. As part of that process, we look at local regulations regarding new investment, and we evaluate the new development pipeline and how it can potentially affect pricing.

In addition to seeking markets with strong supply/demand dynamics and significant barriers to entry, we also mitigate downside risk by ensuring properties have low rents relative to market and buying below replacement cost.

Are homeownership costs a factor that you consider when investing in multifamily communities in an area?

Because homeownership and apartment renting are complementary, homeownership is always a key consideration when evaluating a market. Whenever we are considering a deal, we make sure to look at the gap between rents and home payments.

As a rule, home prices are prohibitive in essentially every major U.S. housing market, which is probably why there are more U.S. households renting than at any point in the past 50 years.

What's more, several factors seem likely to drive the continued dominance of the rental market. For one thing, the new tax-reform bill makes owning a home in some states less desirable than before by capping mortgage deductions; without the incentive of those deductions, we'll continue to see a growing number of high-income earners choosing to rent. Additionally, as baby boomers age, we can expect to see many of them downsize from their homes to rental apartments. From 2009 to 2015, the number of baby boomer renters jumped by 28 percent, and we expect that trend to continue in the years ahead. In addition, the number of renters in the U.S. is expected to grow by 7 million households through 2025, which should help drive favorable returns for multifamily properties in markets across the country.

CONTRIBUTOR

Elie Rieder is the founder and chief executive officer of Castle Lanterra Properties. An active real estate investor, owner and manager since 1998, Rieder was named to *Real Estate Forum*'s "50 Under 40" list in 2017 and was awarded Manager of the Year in 2017 for performance, innovation and strategy by *Real Estate Finance & Investment.* In his personal life, he volunteers his time and energy to numerous charitable organizations and community associations focused on providing food, shelter and education for underprivileged families, both locally and abroad.

CORPORATE OVERVIEW

Castle Lanterra Properties is focused on the acquisition and management of quality, income-producing multifamily properties within strategic growth markets throughout the United States. Through a rigorous value-enhancement program that includes thoughtful renovations, operational improvements and ancillary income development, CLP aims to reposition each asset with the goal of maximizing NOI, elevating its competitive position within the market, and generating attractive risk-adjusted returns for its investment partners.

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