

Real estate funds might be just the investment you've been looking for

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Company News



Experts in investment and financial advisors suggest that residential and commercial real estate historically have been good additions to wealth-building portfolios. Real estate tends to be stable. Furthermore, depending on the asset class and age, such investments can offer a steady cash flow during the hold period and a return on investment when the property is sold.

But along with the benefits of real estate ownership come asset and property management responsibilities. These can range from keeping up with day-to-day operations and maintenance to strategic improvements to the property. Most investors don't have the time or, more importantly, experience to make this type of commitment.

One solution is investing in a real estate fund. Putting money into this type of financial instrument can provide the benefits and returns of real estate ownership without the direct responsibility of owning and operating a property.

What Is A Real Estate Fund?

Real estate funds are pooled finances from multiple investors, which are used to buy, hold and eventually sell certain types of real estate. These funds are managed by skilled, third-party professional managers, known as sponsors. The sponsors seek out and acquire properties dictated by the funds' purpose and mission.

In addition to potential positive rates of return, real estate funds can benefit investors in other ways.

- **Diversification:** Capital raised by the fund is used to acquire multiple assets, potentially in several geographic regions, rather than just one property in a single location. The diversification can help spread the investment risk across a variety of properties with hundreds of units each.
- **Vertical integration:** In addition to offering investment proficiency, experienced sponsors have knowledgeable and skilled teams dedicated to hands-on operations and in-depth management of the assets. This can allow more control over asset performance and the investment itself.
- **Tax benefits:** Those putting money into real estate funds are passive investors, and as a result, can take advantage of pass-through depreciation opportunities.

Finding The Right Fund

While real estate funds can be an ideal investment opportunity, performing due diligence before committing money to them is an important step. Some issues on which to focus include:

Financial Goals

Knowing the sponsor's financial goals means investing in the right fund, with the understanding that results are realized with the asset's sale. As an example, funds specializing in value-added properties that require substantial repairs might offer a conservative income stream at the start but a greater rate of return when sold.

The Target Assets

An investor needs to understand the fund's target class of assets and why they would represent good investments. Pro forma financials can help clarify the issue, as can information about previous cash flow and market performance.

Demographic And Economic Trends

It's important to understand the trends impacting the real estate assets. At this time, multifamily funds (and their properties) are well-positioned because of demographic demand, such as younger adults waiting longer to buy homes and older adults wishing to downsize. From an economic standpoint, available capital and low interest rates support investments in multifamily assets.

The Sponsor

People investing their money into real estate funds are also "buying" the sponsor's service, experience, knowledge, industry relationships and trustworthiness. As such, the investor should have access to the following:

- **Experience and track record:** The sponsor must be transparent about previous investments and rates of return. Understand the length of time the sponsor has been in business, the experience gained and how they honed their processes.
- **Knowledge and focus:** The sponsor's know-how and experience should match the real estate in which the fund is

investing. If the fund's purpose is to acquire value-added multifamily, the fund's sponsor must have experience in buying, managing and maintaining such assets.

- Funding conditions: The sponsor should share what kind of governance and controls are in place to ensure when and how funds are being used. Other issues to consider include 1) what happens if the sponsor needs additional funds for unplanned events, and 2) understanding the acquisition, hold and selling timelines as well as how payouts and disbursements will be managed.

Real estate funds can offer the benefits of real estate investment without the challenges of direct ownership. Generally, these funds can provide rates of return at a lower risk than individual property investment. However, due diligence into the fund's purpose, assets and sponsorship is essential to ensure that the investor reaches his or her financial goals.

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