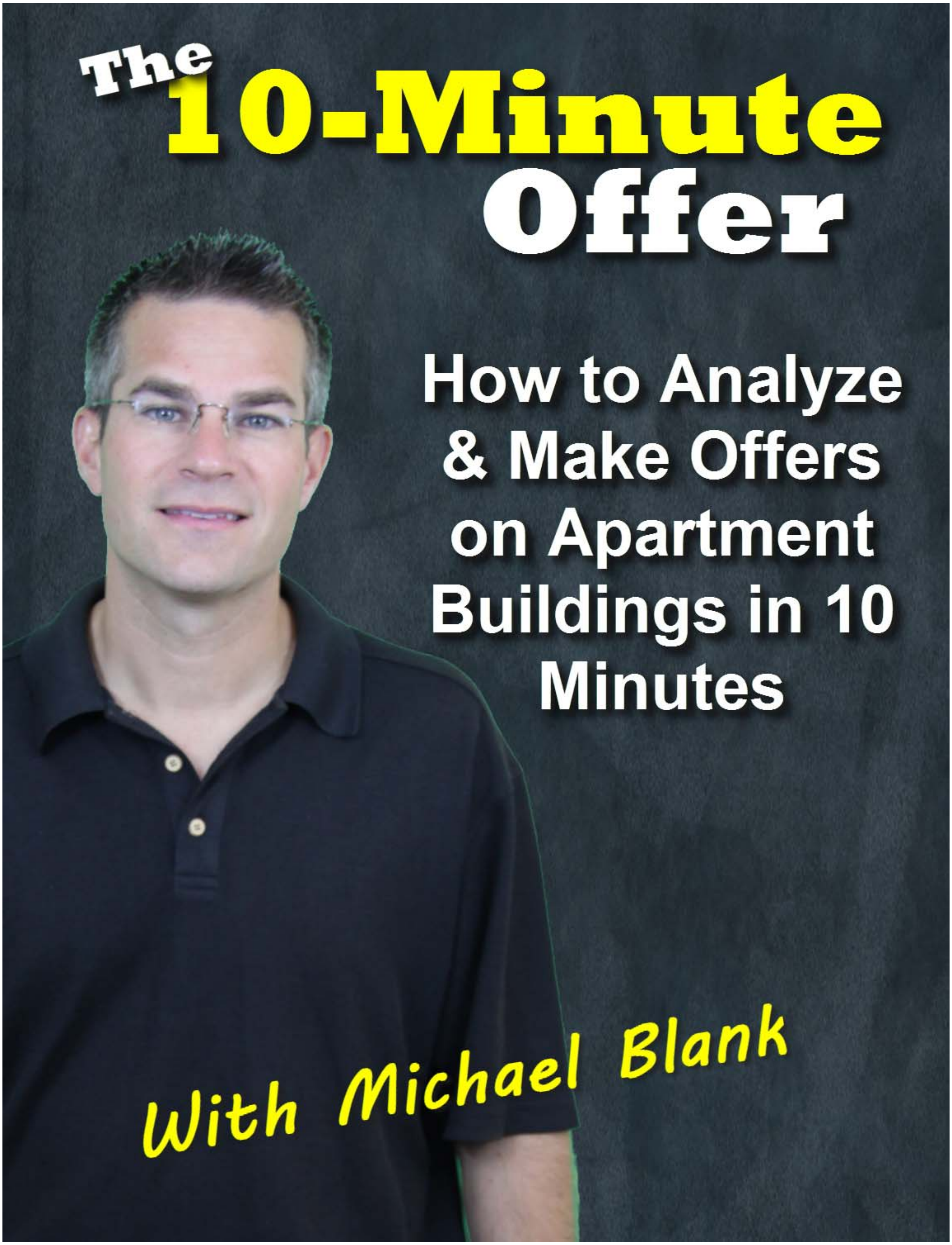
The
10-Minute
Offer
How to Analyze
& Make Offers
on Apartment
Buildings in 10
Minutes
With Michael Blank

Welcome to Your Complete Guide to Analyzing and Making Offers on Apartment Buildings in Just 10 Minutes

When I first got started with looking for multifamily properties, it took me 4 hours to answer the question "**what is the most I can offer for this particular deal?"** As you probably know, you gotta kiss a lot of frogs before you find a good deal and can put it under contract. The time it took to analyze deals was a real issue, and that impacted my ability to get deals done.

I've since then learned that I was wasting my time.

Maybe I can help you learn this lesson sooner than I did and give you some tips on how you can do this in 10 minutes or less.

When you first get a marketing package from one of your commercial real estate brokers, it can be overwhelming. Some of these packages are 20 pages or more! I found myself reading every page, and of course I wanted to be detail-oriented in my analysis. I was examining the financials with a fine tooth comb, comparing the reported real estate taxes with what's published online, doing rental comps for the area and comparing them to the reported rents, and doing other research.

Did I mention this was a waste of time?

Your goal at this stage is not to begin due diligence on this property but to assess the fair market value of the building **based on the information you were given**.

Many times, the marketing packages are not only incomplete but they're overly optimistic with the income and expenses. You can use this to your advantage to start the negotiating process. If we get a positive reaction, we can then delve into the deal a bit more. But only if there's a nibble!

Here is a better way to do this.

The 10-Minute Offer

Step # 1: Adjust the Income - 4 minutes

If the marketing package contains actual financials, look for the gross scheduled income and adjustments for vacancies, concessions, and bad debt etc. If these adjustments are greater than 10%, then use that number, otherwise use 10% as a vacancy factor.

If you have a rent roll as well, compare the bottom-line income in the rent roll with the financials in the marketing package, and use the lower of the two.

If you only have the ProForma financials, then use those numbers.

Keep track of any adjustments you make to the income because you're going to be communicating those to the broker later.

Step # 2: Adjust the Expenses - 3 minutes

This is going to be easy. If the reported or ProForma expenses are greater than 55% then use that number, otherwise use 55%. Often, when the reported expenses are less than 55%, they're missing something. For example, the expenses may be missing a management fee (because the current owner is managing the property himself), or perhaps its missing insurance or some other expense. Don't spend a lot of time on this, but see if you can find SOME expense that is missing from the broker's marketing package. You're going to use that as an argument that the expenses are unrealistically low.

Now, determine your Adjusted Net Operating Income (NOI) by subtracting your adjusted expenses from your adjusted income.

Adjusted Net Operating Income (NOI) = Adjusted Income – Adjusted Expenses

Step # 3: Use the advertised cap rate to come up with a revised fair market value - 3 minutes

Usually, the marketing package advertises a certain cap rate for the property.

"Awesome deal at a 8.6% cap!"

If the cap rate is not that obvious, you can quickly deduce it by taking the NOI from the package and dividing it by the asking price.

Cap Rate = Net Operating Income / Asking Price

Make a note of that cap rate, because you're going to use it to your advantage shortly.

Now, determine your adjusted NOI from Steps 1 and 2 and divide it by the advertised cap rate. This will give you the adjusted price for the property.

Typically this number will be lower than the asking price. That's because the income and expenses in the marketing package were overly optimistic to begin with!

Make note of the adjusted price. Your offer price should be below that to give you some negotiating room.

Step # 4: Get back to the broker with your analysis and informal offer price

Compose an email to the broker in which you explain your adjustments to the income and expenses. Explain that after applying the broker's cap rate, the adjusted price is X, and that you'd be happy to make an offer at the price if the seller would be amenable to that.

Send your broker something like this:

Hey Rob -- I looked over the package you sent me. Everything looks good: it's what we talked about on the phone. I made a few adjustments to the underwriting in the package though.

For starters, I don't have the actual financials, so I had to rely on the ProForma numbers, and we both know those are going to be better than actuals, right? Well, that's all I have *at the moment, except you also sent me the rent roll. The rent roll income is about $30,000 less than what you have in the ProForma, so that's what I'm using for the underwriting.*

WRT the expenses, I don't have the actuals, but the ProForma expenses in the package only added up to like 35% of income. For example, it looks like the insurance expenses are missing, and there are hardly any repairs in the P&L. Based on experience and looking at actual financials from similar listings in the area, I know those are way low. I normally use 55% of income for the expenses, and that's what I'm using here.

You're advertising a 8.5% cap rate for this deal. I'm not 100% sure if that's fair for this area, but let's assume it is. If you apply an 8.5% cap rate to the adjusted Net Operating Income, the valuation of the building is $1.75M, quite a bit away from the $2.4M asking price.

If you see something awry with my underwriting, let me know. I could make an offer at asking price, but I don't want to waste your time if we both know the actual NOI will be lower than what you have in the ProFormas once we get into due diligence. So I'd rather be a bit more realistic upfront.

I'm not sure how set your seller is on the asking price, but I'd be pleased to put in an offer at $1.75M if he would consider it.

Let me know what you think. I look forward to hearing from you.

What have you done?

You've spent no more than 10 minutes analyzing the deal to come up with an offer price. You used the information you were given, plus some rules of thumb. But you didn't launch an investigation to get better numbers. At least not yet.

You got back to the broker quickly with feedback. Brokers tell me that only 25% of their buyers get back to them with feedback. So if you do, you've elevated yourself to the top 25% of that broker's list of buyers. A good place to be, no?

You've started the negotiation process. Yes, you have. It starts informally, but it started. The broker may not respond, or he may say that the seller wants asking or that there are multiple offers at a higher price. Or you may get a counter. And now you're in the game!

Just in case you weren't paying attention ...

You Just Made An Offer!

So, don't waste your life away analyzing deals. Work smarter, not harder. If you do, you'll be able to look at more deals and increase your chances of finding a deal that will actually work.

The 10-Minute Offer in Action

Let’s take a closer look at what this looks like in real life.

When a deal comes in from your broker, you want to answer the question "**what is the MOST I can pay for this apartment building deal and why?"** in 10 minutes and get back to the broker with feedback.

We're going to use the **Syndicated Deal Analyzer** as a way to demonstrate the process.

The Syndicated Deal Analyzer is a simple-to-use excel software tool to help you perform the 10-Minute Analysis. Yet it's also sophisticated enough to handle more advanced questions like:

- What do the 10-year profit and loss projections and returns look like?
- How should I structure the deal with my investors, and how will that impact the returns?
- How much can I pay myself for syndicating the deal?
- How can I model more complicated scenarios like a value-add or re-position deal?
- What are the estimated closing and due diligence costs?
- How will information uncovered due diligence impact the returns? and
- What's more profitable? A sale in year 5, or a cash-out refinance in year 3, and then a sale in year 7?

You won't need to worry about them for the 10-Minute Analysis, and therefore we won't cover these topics in this short e-book. But they're important once you get PAST the 10-Minute Analysis and the seller actually gets back to you with a counter offer.

But for now, let's focus on efforts on the 10-Minute Analysis. Remember, our goal in this initial stage is to

1. Not spend more than 10 minutes analyzing a deal;
2. Get back to the broker as quickly as possible; and
3. Start the negotiation process.

Let's Get Started …!

When you get a deal from one of your brokers, they will usually supply at least a rent roll, i.e. a summary of what each unit is currently getting in rent. Or they may supply a "ProForma", which is what they **should** be getting. And maybe they'll supply some of the expenses. Here is what this could look like:

101		$500		1 bed/bath
102		$498		1 bed/bath
103		$498		1 bed/bath
104	Vacant		$750	1 bed/bath
201		$750		1 bed/bath
202		$524		2 bed/bath
203	Vacant	$498		1 bed/bath
204		$524		1 bed/bath
301		$655		2 bed/bath
302		$750		1 bed/bath
303		$700		1 bed/bath
304		$498		1 bed/bath

** Occupancy Rate 90%

$7145.00 monthly x 9 = $64,305.00

** Beginning 5/1/2010 Building has been managed by (Owner)

Expenses

JP Morgan Chase	$3,220.00 x 6 = $19,320.00
WSSC (Water)	600.00 x 6 = 3,600.00
Pepco (increase rate)	100.00 x 6 = 600.00
Allied Waste	469.00 x 6 = 2,214.00
Cleaning (grass/snow/hallways)	50.00 x 6 = 300.00
6-Month Expenses	$26,034.00

[** Renovations/Labor Costs 5,000.00 (Unit 104)]

Regardless of how complete the information is that is supplied, we want to be able to analyze it and get back to the broker quickly with our feedback.

Let's crack open our Syndicated Deal Analyzer and let's start in the "Summary" tab. Let's fill in the information we were provided with:

- The asking price is $515,000, and the broker is advertising the property as an "9 cap on actuals". He says this is a good deal because this is an "8-cap market" and the rents are under market.
- For the Gross Scheduled Income, take a look at the rent roll that was supplied. They reported rent of $7,145 per month, which is $85,740 per year.

So far in the Syndicated Deal Analyzer we have this (with the three things we modified highlighted):

PURCHASE		
# Units	12	
Asking Price	$515,000	
Purchase Price	$515,000	
Price Per Unit	$42,917	
Earnest Money Depost (EMD)	$5,150	1%
Down Payment	$154,500	30%
1st Mortgage	$360,500	
Interest Rate	6.00%	
Term / Amortization	25	
2nd Mortgage	$0	
Interest Rate	5.25%	
Term / Amortization	10	
Closing Costs	$39,895	7.7%
Acquisition Fee	$0	0.0%
Repairs	$0	
Total Member Capital Needed to Close	$194,395	
Cap Rate at Re-Sale	8.00%	
INCOME & EXPENSES (Year 1)		
Gross Scheduled Income	$85,740	
- Vacancy	($8,574)	10%
- Concessions, Loss to Lease, Bad Debt	$0	0%
= Effective Rental Income	$77,166	
+ Other Income	$0	
Gross Operating Income	$77,166	
Expenses	$38,583	50%
Net Operating Income	$38,583	
Debt Service	$27,872	
Cash Flow After Debt Service	$10,711	

Using the 50% Rule to Estimate Expenses

If you look at the expenses that were supplied by the broker, they will look unnaturally low. That's because they are. For example, you can tell that they're missing any type of management fees.

This particular expense report is not the exception. **Most** financial reports are overly optimistic or exaggerated.

For this phase of the analysis, the initial, 10-minute analysis, we will simply ignore the expenses that were supplied and we will just use the rule of thumb that expenses are 50% of income. If the owner pays all utilities, we will use 55%.

If the expenses reported by the seller are higher than our rule of thumb, we'll use that instead.

In our example, with the 12-unit, the utilities are all paid by the tenants except water, so we will go with 50%.

The only other thing we need to check in our 10-minute analysis is the "Cap Rate at Re-Sale". By default, the Syndicated Deal Analyzer has this set at 8%, but you need to adjust this based on what you think you could sell the asset.

In our case, we will keep the 8% cap rate because from what we know, the cap rate in this area is 8%.

Now our Syndicated Deal Analyzer should look like this:

PURCHASE		
# Units	12	
Asking Price	$515,000	
Purchase Price	$515,000	
Price Per Unit	$42,917	
Earnest Money Depost (EMD)	$5,150	1%
Down Payment	$154,500	30%
1st Mortgage	$360,500	
Interest Rate	6.00%	
Term / Amortization	25	
2nd Mortgage	$0	
Interest Rate	5.25%	
Term / Amortization	10	
Closing Costs	$39,895	7.7%
Acquisition Fee	$0	0.0%
Repairs	$0	
Total Member Capital Needed to Close	$194,395	
Cap Rate at Re-Sale	8.00%	
INCOME & EXPENSES (Year 1)		
Gross Scheduled Income	$85,740	
- Vacancy	($8,574)	10%
- Concessions, Loss to Lease, Bad Debt	$0	0%
= Effective Rental Income	$77,166	
+ Other Income	$0	
Gross Operating Income	$77,166	
Expenses	$38,583	50%
Net Operating Income	$38,583	
Debt Service	$27,872	
Cash Flow After Debt Service	$10,711	

If you scroll down a but under the "KEY INDICATORS" section, the cap rate based on the net operating income and asking price is 7.5%, already quite a bit lower than the advertised 9% cap rate by the broker. We will use this to our advantage in a bit.

Based on our adjusted expenses, what would the purchase price need to be?

Go to the top of the Summary tab and begin to reduce the purchase price until the cap rate becomes 9%. What is that purchase price?

Right, the answer is about $430,000. **We would need to purchase the property for no more than $430,000 to maintain the cap rate that was advertised by the broker.** Here is what we should have in the Syndicated Deal Analyzer:

PURCHASE		
# Units	12	
Asking Price	$515,000	
Purchase Price	$430,000	
Price Per Unit	$35,833	
Earnest Money Depost (EMD)	$4,300	1%
Down Payment	$129,000	30%
1st Mortgage	$301,000	
Interest Rate	6.00%	
Term / Amortization	25	
2nd Mortgage	$0	
Interest Rate	5.25%	
Term / Amortization	10	
Closing Costs	$37,557	8.7%
Acquisition Fee	$0	0.0%
Repairs	$0	
Total Member Capital Needed to Close	$166,557	
Cap Rate at Re-Sale	8.00%	
INCOME & EXPENSES (Year 1)		
Gross Scheduled Income	$85,740	
- Vacancy	($8,574)	10%
- Concessions, Loss to Lease, Bad Debt	$0	0%
= Effective Rental Income	$77,166	
+ Other Income	$0	
Gross Operating Income	$77,166	
Expenses	$38,583	50%
Net Operating Income	$38,583	
Debt Service	$23,272	
Cash Flow After Debt Service	$15,311	
KEY INDICATORS		
Cap Rate	8.97%	
Cash on Cash Return	9.19%	
Debt Coverage Ratio	1.66	
Gross Rent Multiplier	5.02	

Without spending a whole lot of time analyzing the financials of the deal, you can quickly get back to the broker and say:

"Look, you brought this deal to me because you said it was a 9-cap with some upside, and that satisfies my investment criteria. But when I look at the expenses, I noticed that they were pretty low. For example, they didn't include any kind of management fees and there was no insurance. Since the building is separately metered, which is great, based on my property manager who manages buildings like this in the same are, the expenses are normally about 50% of income for an average building. If I use that for my

expenses, then to maintain a cap rate of 9%, I would need to purchase somewhere around $420,000, considerably lower than asking. But you said it was a 9 cap and the expenses were really low. Is the seller willing to consider something like that?"

And now you were able to quickly get back to the broker with a rational explanation of why your offer price would need to be lower and you now also started the negotiation process. All by spending less than 10 minutes with the Syndicated Deal Analyzer.

If you'd like to see this in action, then watch this video where I go through the 10-Minute Analysis step by step.

In the video I also go beyond the 10-minute analysis to cover:

- Understanding Investor Returns (And How to Structure the Deal)
- How Much to Compensate Yourself as the Syndicator
- Fine Tuning the P&L Projections (A Necessity for Value-Add Deals!)
- Estimating Acquisition and Closing Costs
- Determining the Most Profitable Exit Strategy
- Reviewing the Deal and Creating the Deal Package

Watch the Video Now.

Thanks for your interest, and I look forward to staying in touch!

Michael Blank

http://www.TheMichaelBlank.com

About Michael

My passion is being an entrepreneur and helping others become (better) entrepreneurs.

I helped start a software company that eventually went public. I flip houses, own commercial real estate and operate pizza restaurants. I enjoy starting and growing companies, I love making sense of chaos and taking calculated risks. I especially enjoy the "art of the deal": raising private money and putting deals together.

I enjoy in equal measure teaching. I have taught computer science courses, financial literacy classes to adults and children, and courses on how to buy apartment buildings. Because of my experiences as an entrepreneur in different businesses, I feel I can help others gain the knowledge and confidence to take the first steps as an entrepreneur, or to become better at what you're already doing as an entrepreneur.

If you care to read on, here is more about my story.

I'm an entrepreneur at heart, but it took me a while for me to figure that out.

I have a computer science degree and after several years of working for larger companies (including AOL) I took the leap and joined a software startup called webMethods. We started by developing software products that sold for $100's per license and later sold sophisticated business integration software that sold for millions. We went from a group of three out of our CEO's basement to 1,300 employees worldwide. WebMethods had one of the most successful IPO's in 2001.

Because we were growing so quickly, I spent very little time programming software and most of my time interviewing and managing people. I had a development team in California as well as in Virginia. I spent six months in Germany developing a product with a partner.

After about four years, I felt like I wanted to start and run my own software company one day, but I only had experience with software development. I wanted to learn marketing and sales. I convinced my CEO to support my experiment, and so I spent the next two years in marketing, dreaming up and executing innovative lead generation programs.

I then convinced our President to let me try my hand at actually selling software. I read every sales book I could get my hands on and attended a high-tech sales boot camp. I then created a target list and started hitting the phones. By the time I left a year later, I had sold $50,000 of software and had a $400,000 pipeline. It was the hardest job I have ever had, but I learned stuff about selling I still use to this day.

By this point, the culture of the company had changed radically from the good ol' start up days, and I felt my excitement waning. After 8 awesome years, I parted ways with an experience I will never forget.

I took some time off to travel with my wife, and when I came back, I networked with venture capitalists and software entrepreneurs, searching for that next software product to bring to market.

Despite my best efforts, I just couldn't find anything that excited me.

As they say, when one door closes, another one opens.

I read the book "Rich Dad Poor Dad" and I was like, "Man, where has this been all my life?! Passive income is what I need, not money in the bank!"

So I abandoned my plans for the next software IPO and decided to pursue “passive income” through real estate and the restaurant business.

On the real estate side, I decided to flip houses. I read books and signed up with a local mentor. From my first direct mail campaign, I purchased two properties that I rehabbed and sold for a $110,000 profit. After doing a few more deals, I took a couple years off because I was getting busy with the pizza restaurants. I things settled down a bit, I rehabbed 30 properties from 2010 to 2012, financed by loans from private individuals.

At the same time I got started with the real estate, I also launched my restaurant venture. I signed up with zpizza, a high-end pizza franchise out of Newport Beach, CA. In 2006 I opened up our first location in Alexandria, VA. Within two years, we had 6 locations. We had bought two existing locations and improved the sales by 50%, but the recession hammered all locations, especially these two, and I was fortunate to sell them both for a hefty loss in 2009.

In 2007 I launched my apartment investment career by attending a Dave Lindahl boot camp. I subsequently began searching for deals in Texas, and after evaluating nearly 60 deals, I nearly bought an 81-unit in College Station (home of Texas A&M University) but decided against it because I was getting too busy with the zpizza restaurants. I also learned that investors really prefer something more local, something they could drive to if they wanted to.

In 2011, I bought a 12-unit apartment building in an up-and-coming area of NE Washington, DC. Not only was this my first apartment building but it was also the first deal I syndicated with a handful of investors. Read more about my experience here.

In 2012 I bought two zpizza restaurants with another group of investors, bringing us back up to six units.

Aside from my entrepreneurial ventures, I enjoy teaching and motivating others to move beyond their comfort zones to live the lives they were meant to live.

I developed and taught an adult education class for a couple of years that was loosely based on Rich Dad Poor Dad - we used the Cashflow 101 game as a learning tool, and people loved it.

I spear headed the roll out of the Good Sense financial counseling program at our local church and continue to help people become better with their personal finances.

I teach and coach others how to purchase their own apartment building with money raised from private individuals. Teaching others while doing my own deals allows me to constantly learn and improve myself also.

Other things you may not know about me: I hold a Masters degree in Computer Science from the College of William and Mary. I'm fluent in German (I'm actually from there) and conversational in Spanish. I play tennis competitively, love to travel, and started bow hunting several years ago. I live in Ashburn, VA with my wife and four children.