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Guest Column

2012 And Beyond: Hold Onto the Wheel and Pay Attention


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By Billy Procida

If you've made it this far and you've still got a boat and a crew... Bravo! If you've taken on water or even lost your boat, not so good but now is when you've got to pull yourself onto whatever driftwood you can find and start kicking. There's still more money out there than deals and deal makers so go make deals. Sorry for the boating analogy, but I became a boater earlier this year.

The major storm we made it through was truly the perfect storm in that it involved the banks, the government and the consumer. It should be mostly over now. That said, we've been spun around and battered and the weather report remains murky and unpredictable. We also still have to watch out for that rogue wave, whether it's Greek debt, a Middle East uprising or good old Mother Nature. Or closer to home things, like **MF Global**, which nobody saw coming and took down a lot of legendary sea-worthy captains.

So what's the forecast? Let's keep in mind that "forecast" is a fancy word for "educated guess." I'll try and share what I see through my 30-year-old set of binoculars and what strategy I will be implementing during the next 12 months and beyond.

While I believe the U.S. has generally stabilized, the world and particularly the stock market and capital markets will remain susceptible to those unexpected events (rogue waves). The U.S., however, is managing those events better than other countries as recently evidenced by MF Global, which everybody pretty much shrugged off.

So where does one focus in a volatile storm? The obvious: stay close to home, close to land and close to friends who can help you out of a jam.

Our pick is therefore is also obvious, New York and New Jersey real estate. On a national leve, that means a 100-mile perimeter of the country's major cities where jobs exist and where recovery will generally occur first.

Why New York and New Jersey? Generally, no matter what happens internationally, the U.S. will remain the world's tallest midget. Or, said another way, in the land of the blind, the one-eyed man is king. The more volatile the world gets, the more attractive the U.S. looks. When most of the world thinks of the U.S., they think of New York City. Pretty simple, our region's population is growing, they ain't making anymore land so it's simple supply and demand in the near term.

Real estate as an investment class presents its challenges because it is a very hands-on asset class with lots of moving parts and each asset has its own unique characteristics. So I underscore that real estate as in investment has a lot to do with who touches it, because as I've said before real estate is more like raising a child than most other investments. They rarely do what you ask them to do and they always spend your money without you knowing it. Those of you with teenage kids know what I mean.

Depending on your circumstances, different strategies can be perused. There are two basic ways to go: on your own or with others. The good thing about real estate is that to own it and work on it, you generally don't need a license or any experience. That presents both a challenge and opportunity. Me, I like going with others, particularly those with specific expertise that help manage risk and add value.

There are plenty of opportunities out there in both the stabilized and value-added markets. Value-added is a fancy way of saying you're going to use skills and creativity to work some magic to fix something the last guy or girl couldn't. All of the big and public funds are focused on the $20 million and up space, so that's a pretty crowded and very efficient market. The only way you're getting an asset there is by paying the most, and in real estate, where the unexpected always happens, you don't want to pay the most.

The sub-$10 million market is being completely overlooked by these large private equity funds and public real estate entities. So more than 90% of the big money is chasing 1% of the real estate because most real estate is sub-$10 million. I think smart money should focus on the sub-$20 million space, which is less efficient because the large brokers who do a great job tend to shy away from it, especially if it involves the brain damage that smaller assets often have.

So here's my general overview: Not so long ago, most real estate traded (was sold or valued) far above replacement cost. Now most is selling well below replacement cost. For this reason we will see very little new supply. The lack of adding new supply bodes well for existing properties as the creation of new supply lags two to three years after the recovery starts. What's the conclusion? Stay local, diversified and realistic as the magic you think you can work. This will continue to be tempered by a flat market, so yields above 5% can only be made through hard work and careful management of your budget and schedule combined with creative marketing and appropriate asking prices and rents.

As for areas and asset classes, Manhattan will remain stable and the most pursued, thus while a safer place to put your money, yields will be less than other areas. You're not stealing anything in Manhattan. A good thing, though, if you need to monetize your position in Manhattan you can do it quickly. Existing buildings in the outer, outer boroughs and Northern Jersey will also remain stable and a good source of cash flow. I'd stay away from rural area land anywhere right now.

Multifamily. Lots of folks and money are chasing it, thus it is tending to be over-priced. But with rates low, even 5% cap rates produce some cash flow. Just be careful of your projections and due diligence as cap expenditures and unexpected expenses can kill you.

Retail. I'm still a believer in neighborhood retail and small strips. Small businesses are always popping up, especially in down markets, and they starts mall so there's a ys vacant space as long as the property shows weD. The growth ol the immigrant corrl'T'IJnity also pt'oducessmallshops that cater io the ethric groups in particular markeiS. Be caretJI ol tr ple-net-lease deals because they tend to be overpricedon a per se basis and rely on the aeclit of a public COfT'IPany. We've seen too many retailers crater wittout much notice so that coupon clipper can easily become a cash drain if)QU have to replace a tenant or get caught up in a berirnJptcy.

Industria Long-term. I beli-.oe we wil contr.ue io needa place to store the goods we consume. As the market recovers, we will consume more, thus absorbing m:Jfe space. Since new conslructi:lnin this asset class is near i'npossible, existi"lg space is a good commod'ly to oontrd.

Office. Again, no roore olfice space is getting built in the near i.Jture. Too suburban mat not be good. Look lor assets near couthouses, universities, rail hubs and other job-generatng areas.

For safe housing. ThE!fe's still a market out there but steer clear of ground up. Stick with finishing haH-built properties and fiXEM'upPE!fS whete)QU can buy the existing vertical at a dscount. That way you can be competitive. Just be careful io check that the vertical you're buying was built right and have realistic sales expect.atbns.

Land. It will be some tme till dirt can proruce value. If you venture 00\\n that road, be p(epared io hold and carry. land eats a lot and doesnt prcxiJce tT'IJch.

Hot markets to watch? Northern Betgen County. With Goldstar, Sama...,g and Panaaonic planti"lg the flag and the mega Fort Lee Town Square (lormerty known as Centuria or the Helmsley site) fnally under the right sponsorship and reedy to break ground, get ready to see ell asset classes inaease and continued growth in the Korean population.

RoddandCOU"lly. Long the step child of Bergen and Westchestet' its comparative pricing makes it a oompelling area for growth.

Alee I hope gets hot Paterson. N.J. With a rnajo(train station and so cbse to Manhattan, Patterson is a great opportu'lty. But to be successful. it will require the entire ndustry s locus. It won't happen soon. but someday it wilL

Take forecasts for what they're worth. They'e guidance. And remember that no plan is periecl It's a about who you surround yotnell with and the swiftness with which you adjust)QUr plan.

\Whatever ccuse you plot, remember it is the skiD and teamwork of the captain and crew and the collective care of their vessel thai wi determine yr:u tate. So keep your hands on the wheel.

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