NATIONAL MULTIFAMILY HOUSING COUNCIL

Transcript

Code 53

Multifamily Expert Insights: An Interview With RailField Partners

Jon Siegel:

Our business plan is always how do we believe in communities and how do we improve them, and how do we get involved in communities that we believe in?

Alison Johnson:

Welcome back to Code 53, the apartment podcast. I'm your host, Alison Johnson, with NMHC. On this show, we bring you into conversation with apartment industry executives, leading experts in the multifamily sector and a diverse group of practitioners all to help you learn everything it takes to create communities, from business strategy to design to finance and leadership.

Today on Code 53, we bring you into a discussion with two multifamily practitioners with unique backgrounds, both who have capitalized on their experience while keeping their focus on a commitment to improve the properties and neighborhoods in which their residents live and work. Coming up, Ken Bacon and Jon Siegel, the leaders of RailField Partners, on how their commitment and approach shapes their capital stack strategy and preservation of affordable housing.

announcer:

The Code 53 podcast is brought to you by NMHC, the National Multifamily Housing Council, the place where the leaders of the apartment industry come together to guide their future success. From owners to managers and developers, NHCs members create thriving communities by providing apartment homes for 40 million people, contributing 3.4 trillion dollars annually to our nation's economy.

Alison Johnson:

RailField Partners is a multifamily investor that prioritizes community. Ken Bacon is co-founder and managing partner. He spent 19 years at Fannie Mae, rising to lead the entire multifamily business after managing the American Communities Fund and the affordable lending and community development initiatives of Fannie Mae.

Jon Siegel is co-founder and chief investment officer of RailField Partners. Jon, like Ken, was an innovative multifamily leader at Fannie Mae with responsibility for identifying, structuring, negotiating and closing large-scale transactions with many of the nation's largest lenders and property owners. We are lucky to have them here together with us today. Ken Bacon and Jon Siegel, welcome to Code 53, the apartment podcast.

Ken Bacon:

Thanks for having us.

Alison Johnson:

Your firm stands proudly in the multifamily space with a commitment to improve the communities in which your residents live and work. How much of your business model is intentionally aligned with the mission that you both served as leaders at Fannie Mae?

Jon Siegel:

I worked at Fannie Mae with Ken and I worked before Fannie Mae at a company called NHP, which was the largest owner of apartments in the country at the time in the '90, and it had a similar mission to Fannie Mae. It was actually federally chartered also. And so I think in my entire career in multifamily, I had been involved in market rate business but with a mission overlay, and so it was natural as we evolved this business when we said, "Okay, what's our strategy going to be?" I think the first thing we started with was there's a certain thing that we believe in, the mission of housing, and that was a big piece of everything we did at Fannie Mae. It still plays a big part in everything we do today.

Alison Johnson:

I've heard you say on other podcasts that your mantra is workforce housing. What does that mean, practically speaking, to your residents?

Jon Siegel:

Yeah, so we define workforce housing as between 60 and 120% of area median income, and that is really... The 60% end, we would call that affordable housing. It could even be a tax credit property. And when you get to 120% of area median income, you're talking more... It might be a higher-end property, but still catering to what we would still call middle class workforce people.

And so depending on the property... And we like to say we operate with three strategies, really, of affordable housing, value-add or workforce housing and then what we would call core plus. And then all of those, the application of how we implement our strategy of workforce housing differs where when you're at the affordable end, we may actually even go as far as to provide services for our residents, to be supportive in their lives. In the middle, we may be more focused on providing good quality, clean, affordable housing. And at the higher end, providing the best possible product. Again, it runs through everything that we do.

Alison Johnson:

Ken, let's bring you in here. You spent 19 years at Fannie Mae serving as executive vice president and head of the multifamily business before moving into the private sector. Your work history is deeply rooted in affordable lending and community development initiatives. How does RailField pull your personal multifamily mission together?

Ken Bacon:

I'd say in a couple of ways. Number one, as Jon said, we do workforce housing. I used to joke at Fannie Mae that I wanted to come back on the other side of the table to be a borrower. And that's what I did, but I did so with purpose.

So I didn't become a developer of luxury housing. I didn't go into low-income housing. I went into what I call the middle, the workforce housing, because to me, the real tragedy in America today... Look, homelessness is a serious problem that we need to pay attention to, but the real problem in America to me today with respect to housing is that you can go to college, you can get a job as a teacher, policeman, a civil servant, in other words what used to be a middle class job, and not only can you not afford to buy a house, you struggle to pay rent. And to me, if you look at your kids going to school, if you're in a big city, you think the fact that your teachers have to commute a hour and a half or that they're living in cramped quarters, that's a real tragedy to me. That affects the quality of life. That affects the type of communities you live in.

So in RailField, that's what we very much wanted to do. And while a lot of people might do it, we like to think the way we structure our deals, who we work with reflects those values.

Alison Johnson:

As you look at federal engagement and housing finance from your perch at RailField, help our listeners understand the impact of Fannie Mae's duty to serve efforts in the multifamily market to date. How should we think about the future of these commitments to affordable housing preservation investments?

Ken Bacon:

Well, first of all, with respect to multifamily in general, it's useful to have someone in the marketplace who sets standards and who provides liquidity on a constant basis. The setting standards is important because people tend to cluster around what is going to be eligible for financing by the GSEs. So if the GSEs take the lead on something, that will have a huge impact on the market.

So when they have a duty to serve, when they say that "We're going to prioritize affordable," that we'll have... whether it's the green mortgage that was developed when I was there, whether it's the increased emphasis on recent years that they want a certain percentage of their business to be affordable, that signals the market, and it also signals the market in a tangible sense because that's saying there will be capital available to do this.

And that's very helpful because you could say all the nice things you want about housing, about any type of social good, but if there isn't capital behind it's not going to happen. So providing capital, saying, "We're going to provide capital, but we're going to give priority to those deals that fulfill a certain mission," is just beneficial to the market and to the country at large.

Alison Johnson:

There has been a growing trend and awareness around social impact and affordable housing being a component of meeting ESG for several investors in the marketplace right now. Do you see investors growing in their interest in ESG reporting?

Ken Bacon:

Yeah, I'd say that when we started, you'd always have to be careful. You don't want to give the impression that there was no one interested. But certainly, there tended to be more specialized investors. And what we're seeing now, we've had a family office that said they wanted to do this. We've had some of the pension plans indicate that they're devoting more money to this and some of the banks. So we've had some people the last few years who said explicitly, "We want to do affordable deals. And by the way, we still want a decent return, but we also don't want that return to come at the expense of affordability." In other words, they're saying that "We'd like to keep this deal affordable a little bit longer." Maybe we'll have a longer hold period or they're doing something to make their commitment tangible.

Jon Siegel:

Yeah, I think we have a fund that has a big bank as the LP in it that is really... Based on that, we have to do 51% of the units have to be affordable to 80% of area median income. So they're certainly putting their money where their mouth is on that.

I think if you use affordable housing, specifically we're seeing a lot more tangible around that. And when you see more what you'd say ESG, there's a lot more talk around just more squishy ESG and a little less concrete, because I think it's just, in multifamily especially, it's a little harder to measure.

So you can say, "We're looking to do social impact." And so by doing that, affordable housing is something that's very tangible when you say... And then when you say additional environmental type areas, it's harder to put a definition around that, and we hear a lot of talk about it but don't see as much action outside of a green mortgage from Fannie Mae or something like that.

Alison Johnson:

We definitely hear from our members that the activities around sustainability and efficiency, they're harder metrics and outcomes to achieve, not harder in the hard way around, but science-backed decisions can really happen more easily in the E space. But when it comes to social investments, social impacts and outcomes, when you're thinking about the health and wellness not only of your employees and your staff, but the residents and their ability to afford the communities that you're operating, those are more difficult measures and sometimes measures outside the space of private capital, right?

Jon Siegel:

Yeah, yeah.

Alison Johnson:

Things that are not a constant.

Jon Siegel:

An example of that might be there's a group, a susu, that sets up a program so that residents can build credit by paying rent, because rent hasn't historically been part of somebody's credit report. They are trying to do that, and it helps the residents build credit. And I know that then the GSEs have been very aggressive in trying to roll that out, and I know that at least on one property, we did a loan on and they actually paid for us to sign up for a susu, and I think that's happening a lot now. So I think people are trying to come up with different applications that work and then trying to then find ways to support it.

Alison Johnson:

Part of the premise of our podcast is to explain the complexities of investing in and building apartment communities. For many, the process around how an investment idea moves from feasibility analysis to closing equity and debt participation can be quite perplexing. Tell us how RailField's commitment to improvement of properties and neighborhoods shapes your approach to capital stack strategies.

Jon Siegel:

The commitment, and we always say RailField, we believe in communities, that permeates everything for us, so that starts at the beginning. So if you think of the life cycle of a deal, from our overarching strategy of the company to sourcing deals means looking at both markets, specific property types, then to "Okay, how are we going to capitalize it? What's the debt and equity going to look like to the business plan?" and then to the implementation of it. That flows through all of that.

Specifically to the capital stack, we have a couple of partners. We tend to be a group that... We like to say we're a small institutional company. We're not huge, but we all have institutional backgrounds, and so we tend to work primarily with institutions or family offices. A lot of people in the industry, especially of our size or with our strategy, might be more syndicators and going out and syndicating equity. We've never done that before. We have invested with pension funds and banks and lots of different institutional investors, and each one of them has their own investment strategy.

And so where we find the sweet spot where we overlap tends to be in the lower end of our 60% of area median income to where we work with some pension funds in the middle of the stack there, 80 to a hundred percent of area median income, or we work with some families at the higher end. But in all of that, our business plan is always how do we believe in communities and how do we improve them, and how do we get involved in communities that we believe in? And so it's more obvious, I guess, when you talk about an affordable property and you say, "Hey, we're going to focus the rents here." But when you get to a more straightforward value-add property, it's the same equation. And as we grow as a business and we execute little strategies within multifamily, we still always try to stay true to our belief in communities.

Alison Johnson:

You're listening to Code 53, the apartment podcast. I'm your host, Alison Johnson, and we continue now with Ken Bacon and Jon Siegel, the leaders of RailField Partners.

Let's pivot to the here and now. NMHC's annual Apartment Strategies Conference was held a few weeks ago, and much of the discussion on the stage and in the hallways was about a resilient, but slowing investment market. I won't go so far as to call it negative, rather there was a lot of cautious optimism for a soft landing. With news published daily about companies and the GSEs preparing for potential recession-driven losses in multifamily, what is your outlook on the market? And what trends should our listeners be looking out for right now?

Jon Siegel:

I would agree with your assessment of the vibe there. I think when I look at the market, and after talking to a hundred people at the conference, I'm long-term bullish on multifamily as a sector. The demographics are still good. All of the trends are good. There's a ton of demand even though we have a little burst of new construction. So over the long term, I think multifamily is a great place to be, and I think most everybody still believes that.

What we have is the example of... used to say about companies in the old days. It's a good company with a bad balance sheet, and I think that's what multifamily is, at least in the short term here, is we have the increase in interest rates that changed everything.

On the acquisition side, doing investments, we have this bid-ask spread. We made a list at NMHC of the biggest words that we heard the most, sort of a bingo of all the words, and bid-ask spread was probably the number one or variable rate loans. As I said to our guys when we were going through our pipeline earlier today, we seem to be getting last year's deals in this year's market. People just haven't adjusted their pricing expectation, and we're the same way. We had a property that we wanted to sell last year. And then when we found out we could get 20% less for it, we were like, "Eh, I don't think I really want to sell."

I was telling people I think that 2023 is what I call the year of acceptance. We go through the stages of grief that we're all... everybody's like, "Oh, it'll be great in the second half of the year." I'm not sure what's going to happen on June 29th that's going to make everything better on July 1st, but I think people over the year are going to start to accept that okay, the properties might be worth a little bit less. I have a loan that maybe I need to get out of somehow and I need to do something. I think we're in a weird place here for 2023, but part of having gray hair now is that I've seen this movie before, and it usually has a happy ending.

Alison Johnson:

We haven't even touched upon the fact that more than 500,000 new units are about to deliver this year that have been pent up.

Jon Siegel:

Yep.

Alison Johnson:

So aside from what's happening in the capital markets, there's definitely... the new supply-

Jon Siegel:

Yes.

Alison Johnson:

... is going to influence a lot too.

Jon Siegel:

Yeah, yeah. I think we're seeing a lot of new supply, but again, I think that that's probably a short term and it's short-term pain. We have a property in the Dallas market that there's just a lot of new construction around there, and it's fighting every day to try to maintain its occupancy. But I think development over... is a long lead time item, and so there's not a lot of new development now that's getting planned today. Once all this stuff comes out of the ground, which is a year or two, we'll be back to normal.

Ken Bacon:

There's one fundamental difference, too, between now what I consider the macro environment. If you look in the late '80s, the savings and loan crisis, if you look at 2008, those were downturns that were in part caused by excesses in real estate. We haven't had that this time, so that's one thing that makes us very different. If you look at some of the past recessions, there was a lot of madness that went on in the real estate markets, and we haven't had that.

So yeah, there might be some temporary imbalances where some new product is coming on, but this is not a situation where there's just been widely speculative building and you're going to have a lot of empty apartments. I don't think that's the case.

Alison Johnson:

Ken Bacon and Jon Siegel of RailField Partners, thank you both so much for being our guest today on Code 53, the apartment podcast.

Ken Bacon:

Thank you.

Jon Siegel:

Thank you for having us.

Alison Johnson:

And thanks to everyone downloading and sharing this podcast. Subscribe and meet us right back here on Code 53, the apartment podcast.