EPISODE 114

[INTRODUCTION]

Lance Pederson (00:00:00) - Everyone thinks I got to go raise money, so they just use a shotgun approach. Listen, you got to have a plan and it's got to be more focused. You can't do it all at once.

Tejas Gosai (00:00:11) - Ladies and gentlemen, welcome to Real Estate Investor MBA. My name is Tejas Gosai, and I've had the honor of helping hundreds of investors achieve the American dream by creating generational wealth through real estate. I've spent the past few years interviewing the most knowledgeable experts I could find in the business. To cut your learning time and conquer the hardest subjects in the game. Check out rei.mba, which my team and I have packed with over 75 interviews and free access to our real estate roadmap, webinars and publications. If you're listening, I am rooting for you and you're already on your way to financial freedom. Cheers and happy hunting!

[INTERVIEW]

Tejas Gosai (00:01:01) All right, Lance, let's get right to it. Welcome to the show. Thank you so much for being here.

Lance Pederson (00:01:03) - Yeah, thanks for having me. Appreciate it.

Tejas Gosai (00:01:05) - For sure. I see a bunch of books back there. You're a knowledgeable person. If you can give us a bit about your background, tell us how you got here.

Lance Pederson (00:01:14) - Sure. I'm really a lifelong entrepreneur. I started my first company. It was an IT services business back in 2000. Grew that to about 5 million in revenue seven years later, got into real estate. On the private lending side, small, balanced commercial real estate loans up in the Pacific Northwest. We had a debt fund, so kind of went through the whole global financial crisis and held on tight, and we pivoted to more of a capital allocation strategy. So we had a fund to funds and we would, you know, go find sponsors who were good deal guys and raise capital in the fund and allocate it initially as LPs into those deals. And then that sort of spawned an accidental business, which was the real estate fund administration company. We learned quickly that real estate guys might be great at finding real estate and operating it, but not so good at accounting, which was a problem for us since we had kind of a fund to fund set up.

Lance Pederson (00:02:07) - So I took an internal department and turned it into an external facing division, and started doing that and grew that to 3 billion in assets under administration. Our strategy was really to fund architecture and formation consultations with sponsors, you know, whether they're private lenders or real estate operators who are trying to figure out how can we kind of move to more of a pooled, you know, discretionary fund type of situation? So we did a lot of that, and that was sort of what I spent a good part of my time doing was meeting with guys and walking them through that process, you know, architecting the fund, modeling the fund, talking about how to make it so it's aligned. And at the same time, you know, what the economics are and the waterfall and, you know, all that good stuff. Yeah, exactly. So that's really my expertise is just on that fund management, fund administration fund architecture. I've got accounting skills and know the securities laws and got to marketing and all those things.

Lance Pederson (00:03:05) - So a unique, eclectic sort of mix of skills. I'm not good at much, but this is the thing I'm good at. A bit about me. So I'm an entrepreneur, like new things and that's my game.

Tejas Gosai (00:03:14) - So let's pick some of that apart. For the listeners, that might be first time, I manage a fund and it's called the Lehigh Valley Private Equity Fund. I'm in eastern Pennsylvania, hundreds of units and deal with a lot of the stuff that Lance is an expert in. Lance, I wish I met you like four years ago.

Tejas Gosai (00:03:32) - Yeah.

Tejas Gosai (00:03:33) - Because, you know, we had to just painstakingly try to figure a bunch of this out and, you know, some fund administration organizations, you know, they might be able to administer some parts of it, but they don't have the client in mind, or the interface is funny, things like that. So it's very cool to have a tech person on the program, but let's get into fund administration in the big stuff later. Please tell me about 2007 and eight, because that must have really been how you learn to get ahead of everybody else over the past 12, 13 years.

Tejas Gosai (00:04:02) - How did you get through that? Starting a debt fund right beforehand?

Lance Pederson (00:04:05) - Yeah. I mean. So the debt funds that we had, we're sort of legacy. What we ended up doing, which was quite interesting, was that we obviously knew there was distress in the market at the beginning of 2008, and part of the reason I came on board and partnered up with this particular company was that they wanted a credit facility. They were out trying to drum that up. We had Wells Fargo Capital Finance was interested, so we basically went through the whole underwriting process. It took six months and all the diligence and all those sorts of things. We ended up closing that, which was a $50 million facility the week before in September, like so early September, which is right before, like madness occurred, you know, Lehman Brothers.

Tejas Gosai (00:04:45) - That was 2007. That was.

Lance Pederson (00:04:47) - 2008. Right? And so that was and eight. That was when Lehman Brothers went down. So we closed a week before that. I mean, the terms were great.

Lance Pederson (00:04:54) - So we ended up pledging all the loans into the new facility. And then along with the equity investors that we converted those to debt. So this is where we learned a lot. So we ended up having, we converted all the equity members into node holders. And then we had this debt facility. So it's basically debt on debt right? The theory was we had it was really cheap debt at the time with the credit facility. So we're like what? We're going to crush it. You know this is going to be great. Really. There's the capital structure. In the end, that ended up really undoing us because our portfolio held up really well. I mean, our average loan-to-value was a conservative sort of 53%, 54%. I mean, it was not easy, right? Just trying to hang on with all the borrowers and work through a lot of stuff. But ultimately, in 2011, the capital markets were still basically seized up and frozen. Wells Fargo Capital Finance got absolutely slaughtered. All their other clients, just their loans were bad.

Lance Pederson (00:05:46) - That went bad, right? So like they basically said, we're not going to renew this facility. And there was no one else in the market at the time. So we basically had a cliff maturity, the whole credit facility, plus all of the investors because they were three-year notes. So cliff maturity across the board. Not great. So that's sort of where I earned my MBA and just fund architecture. Right. Like it's not always the assets. It could be the structure that you know that the undoing which a lot of people are experiencing now with like multifamily syndications or whatever, right? Like you really have to be mindful of making sure that everything lines up. We weren't got a little greedy.

Tejas Gosai (00:06:39) - What year? What year was that when you got out of 2011?

Lance Pederson (00:06:43) - 2011. So we continue to lend, but we just kind of tore the origination platform down, got rid of our loan officers, and it was basically more of a one-off sort of situation. So that was a good move on our part.

Lance Pederson (00:06:54) - And the skills sort of translated. And that's where we parlayed sort of the learning about the funds on our own and then started helping other guys initially private lenders, you know, because a lot of private lenders were doing fractionalized or whole loans or whatever.

Tejas Gosai (00:07:05) - So let's break that apart. So some folks may have there might be first-time listeners. They don't know what that means, just from that 2011 to what almost now period. Right. You've just developed an entire suite to be able to deal with this. You said 3 billion assets under management.

Lance Pederson (00:07:23) - Yeah. I mean assets administration. So from the fund administration standpoint. Right. So we basically all of our collective clients, you know, the equity invested into their funds or if it was, you know, notes or whatever, you know, $3 billion. So that's all high net worth. That's not there's like no institutional capital in there. So a lot of moving parts. Right. These are all coming in $75,000 average investments into these deals. So really we're kind of I think one of the first people to sort of embrace the sub-institutional real estate space, because that's the issue with many fund administrators, is they've got all these institutional clients, really big clients.

Lance Pederson (00:07:59) - You know, they don't want to be managing $10 million, you know, just a little $20 million real estate fund. It's it's just not worth their effort. So that's kind of where we got in. I actually exited those two companies two years ago. So now I'm on my own, you know, kind of doing much of the same. But sans fund administration, it's a tough business. You know, it's hard to source talent. I mean, obviously the many people that are going into accounting is far and few between these days. And then to find fund accountants that have any kind of experience in fund accounting is hard. So you got to train them yourself.

Tejas Gosai (00:08:30) - And so then that was two years ago. That's 2021 post-Covid. You probably saw some writing on the wall. An opportunity.

Lance Pederson (00:08:40) - I think for me, you know, so we ended up taking the the fund administration platform. We ended up creating our own tech. So we built sort of investor management tools, onboarding tools, you know, all of that sort of stuff to support, you know, the professional services side.

Lance Pederson (00:08:56) - So it really became more of a software company. And then we launched a marketplace to try to match, you know, high net worth individuals or affluent individuals with, you know, our clients, you know, other funds, other syndicators, whatever it might be. It's called Verivest. We just we got to the point where the competition, amount of venture capital coming in, right, with some of these larger companies that were sort of doing the same thing we were, but had $100 million of capital behind them. And here we had bootstrapped the whole thing ourselves. So it ended up getting to the point where I had three other partners in the business, and they weren't as enthusiastic about seeking growth capital. And for me, I just felt like we were, you know, we were at a gunfight with a butter knife, you know, like it just. And so at that point, the vision, sort of my vision for where we were headed and what we could pull off weren't in alignment.

Lance Pederson (00:09:47) - And so it just was one of those things where sort of time to to go out on my own and do my own thing.

Tejas Gosai (00:09:52) - I mean, you earned your stripes, your training and all that work for a bunch of money, which is the right thing to do. And then you're figuring out your next place. So bring us up to date right now. What are you working on?

Lance Pederson (00:10:03) - So with all the fund formation stuff I've just the last few weeks launched, it's called Fund Launch Accelerator. So it's for real estate guys, operators or private lenders who think they want to start a fund, much like you sort of mentioned yourself. Just you're having to feel your way through it. So it's a ten-week course where I basically walk them through step by step. A lot of it's just the educational part, but, you know, just the exercises of like, what are the fun structures you can use? You know, what? You know, basically trying to get to the point where they've got an actual term sheet, you know, the business points of what this fund would look like, that line up once with their strategy and their targeted investors.

Tejas Gosai (00:10:38) - You know what? Let's talk about that for a second. So there's Reg-D funds, accredited investors. There's unaccredited funds that allow different folks in. So you're talking about that as a couple pieces and then like what the waterfall is. If you could explain that. Like, you know, those are some of the that's pretty much like a menu of things that you're like, hey, I want this type of fund or this type of fund, and you help them create that.

Lance Pederson (00:11:02) - So I've done like over privately one on one, you know, helped over 200 real estate entrepreneurs in the last 13 years create their own funds. I've got a process that I take everybody through. But the issue with it was is that your decision was pay me, you know, 25 or $30,000 now, okay. You don't know anything about a fund. So. Okay. You want to fund? 30 grand, right. So that's they don't even necessarily know enough to know whether they should make the investment. And that's sort of what you end up doing.

Lance Pederson (00:11:32) - So, you know, a large percentage of people I walk through it, they end up getting to where they never launched the fund. You know, I just don't think they. They didn't know what they're getting into. And no matter how much I try to talk them out of it, they're like, well, I want a fund. So to me, that was just really inefficient. So this is sort of my response. I've known it for a long time that I needed something where they could get enough information to where they could actually make a decision at a lower price point. And then, you know, you get into week 4 or 5 of the program and you start to realize, like, okay, I see how this could work and how this would fit in the bigger picture for my business. Now I'm ready to make that $25,000 investment or whatever it is, and then they can engage me, and then I'll basically hold their hand through the rest of the process. But, you know, my objective in all cases where they go through the course and kind of self-guided and find their own securities attorney to create the docs based upon the work that we do, you know, is that I want people to hit the ground running where they know exactly who they're targeting, what their message is like, what's their differentiation? And the way the fund's been structured, it's aligned and it's interesting and it solves the target investor's problems.

Lance Pederson (00:12:36) - And they have, you know, and they can articulate that differentiation and pitch it, and they can sell it because they've made the decisions. They know why the fund was structured in certain ways. And therefore when they're getting objections from investors, they can overcome those objections instead of sitting there like, I don't know, the attorney put that in there, I'm not really sure why. And then narrowing it down just to a handful of tactics that they're going to because everyone thinks, I got to go raise money, so they just use a shotgun approach and just start, you know, doing all sorts of stuff. And they wonder why it doesn't work. You know, where I'm kind of like, listen, you got to have a plan and it's got to be more focused. That's always been my intent is like focus on what is going to move the needle, and then you can layer in other tactics and other strategies and things like that at a later time. But you can't do it all at once.

Lance Pederson (00:13:20) - I mean, even I'm going to go social media or something can mean a lot. I mean, Twitter is way different than Facebook and Facebook's different than Instagram and, you know, but to many guys it's just it's just social media. So why, you know, let's just let's do social media. And I'm like, not quite.

Tejas Gosai (00:13:36) - I love what you're sharing. Again, I wish I met you years ago. We definitely had to bring in experts. And luckily my partner Jeff is in his 60s and he has managed very successful fund. We ran into every problem that we could. We actually rushed to get our fund off the ground in February 2020 like it was right whenever everything was hitting. We actually paused. Start launching the fund until 2021 midway through the year. So that was a really good lesson in like, had we launched, we would have been, you know, would have been shot in the foot immediately. It would have been a terrible process. So, you know, and our educators, our attorneys, our folks really helped us align all that.

Tejas Gosai (00:14:18) - And so let me say, a lot of people do want to just start a fund or syndicate large piece of multifamily. I like that you're talking about social media because historically, funds and finding accredited investors through the internet that didn't exist until.

Lance Pederson (00:14:34) - 2013 with the Jobs Act. So in September of 2013, when you could actually check the 506 C box and actually publicly advertise and solicit.

Tejas Gosai (00:14:42) - And that's what started like the whole industry to go bananas and, you know, become what it is right now. So that's cool. I don't think people realize also those fundamentals that you're talking about, like our fund, we have a 1.5% management fee. We have an 80/20 waterfalls. Some folks are 70/30. So just for the listeners, that's how much the investor gets paid and then the managers get paid as an incentive to have a higher return. There's things like target returns and preferred returns and all those pieces that you don't get to change without spending a lot of money, right?

Lance Pederson (00:15:17) - Yeah. I mean, it's it's certainly difficult, especially if you, you know, I mean, obviously it's a bit easier to change it if it's in investor's favor, but you can't go the other direction really without getting them to sign off on it.

Lance Pederson (00:15:29) - And that's where I think a lot of people get sunk is just they're not making informed decisions. And then those decisions are the very things that are sort of making it even harder. I mean, I don't care what the environment's like. There's always a headwind when it comes to raising capital into a blind pool fund, for obvious reasons. It's just you're basically as an investor, you're abdicating complete decision-making authority to another group. Right. And so and then you don't necessarily know what all the investments are in the fund. It becomes less blind over time. But it's not easy. So then if you've got your structures all weird, and I think a lot of guys, especially real estate guys or anyone, there's some amount of creativity that comes along with it to be good. This is not an area where you want to be creative, right? So like getting cute with how you've structured it and think that you've reinvented the wheel and you're being innovative. I'm like, we want it to look vanilla, right? Like we want it to look, you know, you squint at it, it looks basically like what everyone else's is.

Lance Pederson (00:16:21) - Right? But if you're searching for differentiation in how you've structured your fund, you're sunk before you even get started, because your differentiation needs to come from how you execute your strategy, what that strategy is, how you execute it, risk mitigation, all those sorts of things because If I'm going to abdicate my decision-making to you about which investments to make, that's what I'm more interested in. Prove to me that you're differentiated in that regard, and just make sure that the structure isn't completely one-sided, and you can do whatever you want to do, you know, want the mandate to be narrow enough to where you can maintain focus, you know, all these sorts of things, but don't get cute on the structure because I've never seen it work. I've never seen anyone who came up with something they thought was brilliant and genius really catch on because it forces people, the investors, to think they're going to want to think anyway. But if you're forcing them to think about things that they shouldn't be thinking about, their answer will probably be no.

Tejas Gosai (00:17:14) - I'm happy you're bringing that up because we're a fund and only accredited investors. They are. For those that may not know accredited investors, you make over 100,000 or 200,000 jointly or have a million in net worth. And then there's some stipulations for other folks that can invest in a fund, but that's to have an informed, educated population that invests in the fund. So, you know, that informed, engaged population also invest in other vehicles. Having something weird over here that doesn't make sense, along with like six other investments that are clean. And you're a fiduciary, right? That's the biggest thing here. You want to make sure that you're mitigating risk and that you're giving the best return while doing everything ethical and code-worthy. Yeah. So good things. I want to switch gears for a second and talk about now, because over the past 12 months, you know, we've seen interest rates. We've seen the Fed trying to hammer towards 2%. So much wars going on and geopolitical stuff. And before I hear your thoughts, we've had to change some of our model.

Tejas Gosai (00:18:15) - We've had to double down on multifamily and we've had to aggressively find seller-financed deals, which are around five and 6% like all these things I never imagined doing. And we're able to perform, you know, we have a good outlook, but you talk to a lot of funds and a lot of folks, and you've seen what they've dealt with and how they're functioning right now. Let's talk about that today. And then let's talk about like the future of what you see.

Lance Pederson (00:18:40) - Today as we as we record this, it's in October 2023. Like it's a very interesting dynamic right now with Fed's response to tamping down inflation. Right? So the biggest thing I'm seeing is just when you have treasuries, you know, risk-free ostensibly at 5% return, that makes it really hard to raise capital because investors they're smart. I mean like they're looking at the risk premium that they can earn in something other than that versus the risk-free rate. And so a lot of those options and especially said multifamily like the flip side is now the interest rates on loans is super high.

Lance Pederson (00:19:14) - Right. So even finding a deal that pencils and then when you even do it's like a good deal. You've got this high-interest rate. So you can't really employ leverage. It puts investors situation where I'll just park it in the treasuries and wait, you know, to live, to fight another day. So transaction volume’s way down. You know that's where we stand. So like we've got a class B industrial property, 300,000 square foot facility up in Madison, Wisconsin under contract. It's a slam dunk deal, but the debt financing is like it's just getting a term sheet on debt at reasonable terms is just been completely painful. Something we never even had to worry about before, you know, is becoming a sticking point. And so many of the guys I'm talking to in the business doesn't matter what they are self-storage, mobile home parks, anything, getting that, that's killing deals. And so, I mean, it's hard enough on the equity side. I mean, and everyone's reporting that to stiff headwinds for the reasons I've laid out.

Lance Pederson (00:20:04) - So you're just seeing where there's like nothing happening. It's like a ghost town, you know, as far as, you know, transaction volumes. Because as always in the real estate biz, whenever we sense that there's going to be some distress ahead, everybody sort of licking their chops and super excited, just like they did with Covid, like, oh my gosh, there's going to be all this distress and they get all amped up. And so that's what everyone's waiting for, all this stuff to start falling out of the trees and

Tejas Gosai (00:20:28) - Blood on the streets, right?

Lance Pederson (00:20:30) - Yeah. Blood on the streets. We're going to dance on the grapes or whatever, you know, which of course, to me now, being in the business, as long as I've had, I'm like, whatever. Like, don't catch me ever saying that. Like, now I know that's going to happen. But as always, it usually happens in slow motion and it never happens as fast as you think it's going to happen.

Lance Pederson (00:20:47) - And I'm a believer that there's good deals to be done in up markets and in down markets, like if you're good at what you do, like you can find good deals in times like this, it's harder to find them, but it's not impossible. That's my take in terms of the future, right? It appears as though inflation seems to have worked. And my hope here is, is that the Fed realizes that it's more or less worked. Don't get too hung up on it, because I don't think that we can hang out where we're at right now for too much longer, without all sorts of knock-on effects. The banks are all probably no one wants to land. No one wants to do anything. Like I get what they're trying to do. They want inflation to be tamped down. But we need to ease off of this. But I'm also not like, let's not make it free again. Don't go. Keep going. Guard rail to guard rail. I think the market can be perfectly efficient if interest rates are in between 5% and 6%.

Lance Pederson (00:21:33) - But it doesn't work at eight.

Tejas Gosai (00:21:36) - No, it does not work at eight. Thanks. For sharing that. Yeah, it is nutty for just some of the funds that got into a bunch of assets last year or the year before and took variable rates. You know, those guys can't produce a return at all. They're doing capital calls. It's not cool. Does the Fed have it under control? Because I mean I still think they're pissed. And they're like, you know we need that 2%. We're not near the 2%. And so going up to eight just now is nuts and hope we don't go any higher. But even if we plateau, you said it right, it's a very slow process. Like it's not like we're going to have rates in six months. That makes sense. It might take a year or more.

Lance Pederson (00:22:18) - Oh yeah. And I think it will mean I think it'll take another 24 months. And you know, and that's probably the prudent policy once again to ensure that it doesn't mean they're terrified of, you know, on stagflation.

Lance Pederson (00:22:28) - And, you know, so like I understand where they're coming from. And once again, let's never forget a lot of this is psychological. And I think the reason why they're taking such a hard stance is because the American public doesn't seem to be paying attention in the economy, continues to be I mean, I think I just saw it on Wall Street Journal this morning. At least it got the alert right. Like the economy's still humming along. Right. And I think that's where they're trying to get it to. Where like is anyone paying attention? It's the psychology. They're just saying tighten your belts, just don't spend as much. Let's force distributors and all the people, if you keep buying the stuff and at the prices that they're selling it for, then they're going to keep raising the rates because they're capitalists. Right? Right. You know, I think that's where they get nervous. So it's just like if we could see any slowdown or anything, I think that's what they're looking for. It just doesn't seem to ever show up.

Tejas Gosai (00:23:14) - Yeah. Pain. My mentor is like sadly we need more pain. Lots of pain. And that's not good for American people. But that is what has to happen to try to solve this. And it's just like the beginning of this. You know, we still got a we're in the middle of an election madness as well. So who knows what's going to happen in three months at this point? I mean, it could be 12%, God forbid, but like, you just don't know.

Lance Pederson (00:23:40) - Yeah. You just you just don't know. I don't I don't expect that. I think that they've you know, my hunch is they'll let it hang out here and wait for the pain to be more visible. But, you know, my opinion is the pain's there. It's just it's not revealing itself in certain places. And you always have this dynamic just where lots of these things lag. It's the same thing with just Covid response to Covid, with printing all this money and giving money out.

Lance Pederson (00:24:03) - Like it just like, you know, hindsight's 2020, but it doesn't take a rocket scientist to figure out that it's probably going to create all sorts of inflation, inflationary environment. There's way more money floating around in the system. That's what happens when you print money, right? It's inflation. It's a hidden tax. So not surprise. It's just that I think it's surprises us that it just it takes longer to feel the effects of these sorts of decisions. You know, six, nine, 12 months, 15 months.

Tejas Gosai (00:24:28) - Very much value your opinion because you've now survived like four weird cycles in the past 15 years. So what do you say to somebody who still wants to get into real estate right now, or wants to go start a fund and has capital or opportunities? How do you keep them motivated?

Lance Pederson (00:24:47) - Yeah, I mean, I think to the degree that people have a legitimate strategy and by that I mean like they know how to source transactions even though the wells might be dry right now. Like if you have a legitimate acquisition strategy, like you've got markets you operate in, you have relationships with brokers or whatever it might be like, you've got something that's viable, then you're just going to have to realize, like, this is just part of what comes with being a real estate guy.

Lance Pederson (00:25:12) - It's like a forest fire, you know, like it's not good when it happens, but it is good in the long run. It clears things out or whatever. So I think that's what I'd say to a guy who are seasoned. I'd say to people who are doing something else right now and don't have that, I'd probably just stick to whatever it was that you were doing and not jump in now, probably not the right time to be deciding to make a career switch, because once again, you'll be frustrated and probably quit anyway. Like even if even getting into like commercial brokerage or anything like, I mean, this is as frustrating as it gets for those guys, so probably want to hang on to doing whatever it is that you're doing now and wait till the sun comes out and there's a little bit more activity where a blind man can find what he's looking for, I don't know.

Tejas Gosai (00:25:57) - Get a lot of information, make knowledgeable decisions. Lance. You're awesome. How does somebody get a hold of you?

Lance Pederson (00:26:03) - Yeah, LinkedIn is probably the best way just to look me up.

Lance Pederson (00:26:05) - Lance Pederson. P-E-D-E-R-S-O-N. Feel free to connect. And yeah, I've got all sorts of stuff going on. I do a lot of stuff with the high net worth. I'm a partner in passive advantage and we're building like LP deal analyzer tools for multifamily syndications and we're going to add like funds and other things. So, you know, I kind of work both sides. I mean, I'm in the middle a bit, you know, I'm trying to help people realize, like, let's let's make it so it's a little bit more aligned both directions. And so, you know, I teach the guys how to create funds. That makes sense. And on the flip side, I'm teaching passive investors like here's how. You make sure that these deals are good and these guys are good. And, you know, so that everyone's educated to make it a bit more of an efficient market, but not too efficient so that we continue to get those premiums on returns.

Tejas Gosai (00:26:50) - Love it. Thanks so much for being here.

Tejas Gosai (00:26:51) - Appreciate your time and we'll have you back on in the future.

Lance Pederson (00:26:55) - Yeah. Sounds good. Thank you.

Tejas Gosai (00:26:56) - Awesome. It's Real Estate Investor MBA. I'm Tejas, this is Lance. Everything's online iTunes Spotify. Stitcher. Love you. Cheers. Thanks a lot.

[END OF INTERVIEW]