Keeping it private

The ups and downs of investing in private real estate

By BERNADETTE STARZEE

Ted Weiss likened the current local commercial real estate market to the stock market of a few years ago, when the Dow slid to 6,500 points, creating the ultimate buyers market.

With nowhere to go but up, today "you could almost throw a dart and hit a property that would be a good investment," he said.

Weiss, whose Melville-based real estate firm T. Weiss Realty specializes in Class A office and industrial space in the Melville-Huntington area, is currently working on several deals to acquire new Suffolk County properties.

"The long-term prospects are excellent," Weiss said, noting there hasn't been overbuilding of office space on Long Island in years. And though tight credit is hindering many investors, T. Weiss Realty is well-positioned to make acquisitions. "Our properties are performing, we're not overleveraged, and our money is looking for a place to go, where it's not sitting in zero-interest investments," he said.

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The global financial crisis and real estate downturn have resulted in widespread risk aversion. But according to an analysis by National Real Estate Investor, including private real estate in a portfolio with other investments allows an investor to diversify and mitigate risk, since private real estate has a low or negative correlation with the performance of stocks, bonds and public real estate investment trusts.

National Real Estate Investor reported that over the past decade private real estate returns have outperformed the S&P 500, the Dow Jones Industrial Average, the Russell 2000, and the Barclays Capital Government Bond indices. Further, private real estate has delivered high and steady annual income returns, with a 6.9 percent average annual income return from 2000 to 2010.

However, private real estate is not for every investor. "It depends on your risk profile," said Howard Landsberg, a partner in the real estate group for WeiserMazars, an accounting firm with an office in Lake Success.

"If you buy, say, a small shopping center in Deer Park, there's a lot of exposure – if one or two stores become vacant, you will have to come up with the money," Landsberg said. "You also have to manage it or hire a management company, which would take away from your income."

Investing in real estate investment trusts, on the other hand, provides a diverse portfolio of real estate. For instance, you might buy stocks in an REIT of 100 supermarkets on the East Coast. "It spreads the risk out, and the REIT is professionally managed," Landsberg said. He acknowledged, however, that the upside might not be as good.

"Diversification is still a good philosophy, but in this market, there are great opportunities in private real estate for people with cash," said John Magnani, managing director of the commercial division of Daniel Gale Sotheby's International Realty in Manhasset. It's not first-time buyers who are looking for deals at this point, but "sophisticated investors who over the last couple of years may have liquidated assets or accrued capital just for the purpose of driving a hard bargain and purchasing investment property in all or mostly cash," Magnani said.

Banks want buyers to put 30 to 40 percent down, he said, and the buyer has to prove to the bank it's a good investment. "Banks drag their feet, and in some cases, you have to move quickly," he said. "I just handled the sale of an office building in Port Washington in which the sellers took $150,000 less than the asking price because the buyer had all cash and was ready to close in 30 days."

Buyers are not buying to flip now, but to hold the property well into the future, Magnani said. "Prices are down and rents have not gone down dramatically, so you will get a better return on rents if you buy in this market," Landsberg said.

Still, at least in the short term, the soft rental market is a significant consideration. "Retail strip centers on Long Island have been strong for years, but now when you look around, you see a vacancy or two at a lot of centers," Landsberg said. On the other hand, Landsberg noted, "Multifamily housing is tremendous on Long Island, because there's not much of a product."

Industrial property, he said, is generally strong here, with lower risk than office space in this market, because of a "good supply-demand balance."