Ep #289: Frank Rolfe - Investing in Affordable Housing

Full Episode Transcript

With Your Host

Dr. David Phelps

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David Phelps: Good day everyone, it's Dr. David Phelps of the Freedom Founders mastermind community and dentist freedom blueprint podcast. Today, I'm doing a catch up call with a gentleman that I have known for, gosh, probably a good decade now, he and his partner. And we have been, my wife and I, and a number of people in freedom founders have been investors in a multiple number of their funds. So with me today is Mr. Frank Ralph. Frank, how are you doing, sir?

Frank Rolfe: Hey, I'm doing great.

David Phelps: So Frank, as I said, we've known each other for a number of years. In fact, when did you and Dave kind of partner up after the downturn? Was it 09' ish?

Frank Rolfe: Yeah, we startedback in 09'. I think, bought our first property jointly in 2010. I think April of 2010.

David Phelps: All right. So people that don't know are probably wondering, what are we talking about here? So we're talking about mobile home park communities.

Frank Rolfe: That's correct.

David Phelps: Right? And you and Dave kind of separately, on your own, have been involved in mobile home park communities for a couple of decades, and you partnered up, but I think... So people know who you are, you're an economist, trained, educated from Stanford. You made a pretty big play in the billboard industry and probably other things I don't even know about for a number of years, and then somehow tripped into a mobile home community not far from where I am right now, here in Dallas, Texas called Glen Haven.

Frank Rolfe: That's correct.

David Phelps: A couple of decades ago.

Frank Rolfe: That's correct.

David Phelps: You kind of remember telling the story. In fact, Frank, you probably don't remember because you've done... You and David have done so many mobile home universities. So taking people on boot camps around the country to different parks that you guys have bought together. But this is a number of years ago. My wife and I joined you guys on a bus tour in Dallas, and you took us to Glen Haven, and I remember you telling the story about how you just... Taking a tiger by the tail. I mean, there was just so many things, obviously jumping in first time, that you had no idea you were getting involved in, right? You talked about the electric and sewer master meter, so that's a big mess you wanted to untangle. And then, talk a little bit about some of the grade A tenants you had to probably have to deal with on that first park.

Frank Rolfe: Yeah. What happened on that one, David, was the... Back in the mid 90s' when I got in, Dave got in and even Sam Zell got into the industry, no one really knew what they were doing very well. We had no idea what made a park tick. All we'd do is, we would buy these old beat up stuff and trying to bring it back to life. So Glen Haven was in such poor condition. It was actually a trophy park back in the 50s' when it was built. I think it was built in 51' but it had gone downhill so badly that, back in the far corner of the park, there was an amateur wrestling ring with makeshift stands made of particle board and plywood, and they would have Saturday night wrestling back there. And my audience was just a bunch of misfits at that time. I had literally carnival workers. I had, in some cases, street people.

So what I had to do was, I had to bring the park back to life physically and spiritually, and I had to get rid of folks who couldn't pay rent or would not follow the rules. And over the years, it morphed into a relatively nice, mostly family community, but it was definitely hard to scrabble back in the 90s'.

David Phelps: Now, I assume that you didn't keep the Saturday night wrestling matches as part of the lure to the park.

Frank Rolfe: That was not... No, that was not an amenity I wanted to provide the customers. No, the wrestling ring came down almost day one. But yeah, I had to find other amenities people actually would utilize, like picnic tables and green spaces and not that kind of stuff.

David Phelps: Right. Got it. Got it. All right. So you and Dave were somewhat, I guess, competitors for a decade and then you figured out how collaboration might go, particularly with timing of the downturn of 2008, you guys really teamed up. And I think, knowing both of you, how well you compliment each other, I think it's a unique thing when that can work out. And you guys certainly appeared, atleast from my vantage point, to really operate well together. And I don't know... Today, it’s ranked what number on the mobile home?

Frank Rolfe: Yeah, our macro portfolio is ranked right now. We're fifth largest in the US but this year we'll probably drop to sixth, because back in 2018, we did one of the... What we believe to be, one of the 10 largest sales in industry history to a private equity group known as Strive. So we sold 102 properties and one transaction to Strive, so that took us down a lot, kind of about 10,000 lots. So that put us neck and neck with UMH and then UMH has been on an acquisition binge. So I think this year we'll probably drop to sixth, but we'll still definitely be in the top 10.

David Phelps: So let's talk a little bit about where we are in the market cycle. And I think that's what any savvy investor, who's been around for a while, is always trying to figure out. When is it time to acquire or when's it time to liquidate?

Frank Rolfe: Sure.

David Phelps: You and Dave, you've been talking to us as investors all along, you guys are great communicators and have always let us know kind of what's your strategy, what you're looking at. So kind of bring us up to date with where we are right now.

Frank Rolfe: Yeah. Well, where we are in the cycle of the industry is, there's still a lot of opportunity in filling our many vacant lots and raising rents, so that's our primary focus right now. We've got about 3000 lots I think, in the macro portfolio to fill and we feel our rents can easily go probably another a $100 a month without really pressing any of the market rents or the customer's ability to pay, so that's the primary focus. So to that end, the last year, 2019, we set all kinds of records on that. We sold 1,200 homes, we rented another 600 homes. I think we had a net fill rate of 750 homes. And I think we sold about 21, $22 million of homes. So we did a really good job on filling occupancy last year. We anticipate, actually, we're going to try and beat those records this year.

So we're going to try and break all of our records again this year, so that part of the puzzle is going well. The rent raises, we raise all our rents traditionally annually, so that's moving along. Property conditions have never been higher. That's been a part of the process, that's how we were able to sell and rent so many homes as we made the home and the parks very attractive to people, so they think they're getting a good value. So really, things are doing good. We had a banner year operationally last year, and we hope to repeat that again this year.

David Phelps: Well, operations is something that you guys really, I think, fine tune over the years, very, very well. And you talk about it and make a big point to anybody who's gone to your bootcamp that, on the buy side, the due diligence is something that you have. And that's where you make... Anybody that makes a good investment versus speculating on, gee, should I buy this? Should I invest in this or not? Understanding what the due diligence looks like. You guys really, I think formulated that, you scaled it, you've written books, you teach on it. Talk a little bit about that and how important that is, no matter where you're on in the market cycle.

Frank Rolfe: Sure. Well, I think a couple of hundred years ago, Ben Franklin said that diligence is the mother of good luck, and he's totally correct. I mean, we do our best and we take all of the luck out of the picture. So we try and verify all the income and expenses to the last penny as best we can, plus any other operational problems. So there's basically four areas of diligence we focus on. One is infrastructure. One is density. One is the location. And the fourth, which is kind of odd, are the actual age of the homes because we want customers with homes that are, for the most part, paid for, because it makes the customer more stable and also allows us to raise the rents higher over time, because that's the direction rents are going.

We basically dice and splice the park, starting from scratch, to make sure we've taken to the best of our ability, all the risk out. Now, you can't take all the risk out. You still have weather related events, you can have flooding, you can have tornadoes, you can have a major employer close. We don't know at any given moment what the future is of this plant or that plant. But in, so doing, we've been able to keep ourselves out of trouble now for several decades.

David Phelps: You've always made it a point to focus on what you consider the affordable niche, versus higher end, upper end, that other operators might focus on. Why don't you just... Again, I know you've talked about this, but just kind of give our listeners a little bit of the reason why you like the affordable housing niche.

Frank Rolfe: Yeah. We like the affordable housing because we think that's the future of America, is the need for affordable housing, which is basically housing people who have, typically household incomes of anywhere from 25 to 40, 40, $50,000 a year. The upper end of the industry, we find risky because the problem is, and there's been lots of articles recently, called the silver tsunami. We don't know where the boomers are going to want to go in retirement. I'm a boomer, and I know that the attitudes of my peers are different than those of their parents and grandparents. And so on the higher end of the industry, the question is, will boomers want to retire into extremely small mobile home parks in areas which are maybe not where people want to live today. And so, that's a risk factor that we can't really solve in diligence. So we prefer the affordable side because the affordable, it just grows constantly. Whereas on that retirement and the upscale portion of the industry, we think there's actually a degree of risk to that.

David Phelps: Yeah. I would agree with you that, we still have to see where that's going to settle out. So you don't currently have any funds that are open right now, the last one was MAC 2, I believe, a couple of years ago.

Frank Rolfe: Yeah. I believe that's correct. I don't handle that. I'm field operations guy, I'm out in the field every day. Eric handles that, but I believe that's correct.

David Phelps: Are you able to give us any insights as to you and Dave and the team, as far as your strategy going forward? You talked about everything you're doing with current assets, banner year last year, the same for this year, even better, breaking records. What about ongoing acquisitions? Are you in an acquisition mode at all right now, or are you pretty much going to liquidity events as you build out?

Frank Rolfe: Well, sure. Well, what we did back in 18', we did the 102 properties sell off, which was one of the key components. Well, there were two. One, it was a great deal for us. Portfolio, we got good pricing and we thought the timing was good to take money off the table. The other portion of that was that, in any point in the cycle, we always like to remain cautious. So as part of that sale, which we did, because there had been two large... Three large portfolio sales right before that, and we did not want to miss out on those buyers. The other portion was, we ended up with a non compete that ends next year, so that was important to the buyer that we wouldn't be out there trying to undercut or do anything with the properties that we sold them. So we've devoted last year and this year, basically to operations. And then next year the non compete will burn off. So for this year, again, we're focused really on operations.

David Phelps: So the non competes are really the big reason why you're focused on operations. So again, I know you can't say for sure because things can change in a matter of days or weeks in the market, but are you... I guess I'll just ask you personally, are you still having fun doing what you do?

Frank Rolfe: Well, you know what? That's a great question. At this point I'm spending... I think last year I did a hundred thousand miles of driving from park to park. This year, I will probably drive roughly the same mileage, maybe a little less. And yes, I really enjoy it. I enjoy going out to the properties, walking the properties, meeting with the managers, seeing what's going on. I think I like it of course, because we're winning, so it's always fun to go onto property where things are looking better than when we bought it and where we're filling lots of homes.

David Phelps: Right.

Frank Rolfe: So yes, I fully intend to... In fact, this summer, they're going to be... There's a group in Ireland, an Irish filmmaker doing a feature length movie on the American mobile home park industry where he's going to make the movie based around riding along with me.

And we did the first trials of that a few months ago, and then he went and got funding from the country of Ireland to produce the movie. That's how they do documentaries over in Europe. And so he's supposed to come back this summer and we're going to drive around together for, I don't know, a month or something. But yeah, I enjoy doing it. And coming up at a theater at some point in the future, you'll be able to see kind of how it works, driving around parks all day. But yeah, I enjoy doing it.

David Phelps: Interesting. So it seems like this bull run market that we've had since coming out of the downturn, what? 12 years ago, and say 2012 odd up, it just seems like it just keeps perpetuating. It just keeps rolling, rolling. I think we all believe that at some point there has to be some kind of a correction reset. We don't know when that will happen, what that looks like, what triggers it. But based on that and your experience in market cycles, Frank, is there still opportunity for operators like yourself, in your asset class, other asset classes, kind of where do you see things in general right now, as an operator in acquisition?

Frank Rolfe: Well, yeah. As an economics major, I would be a little afraid in much of the investment sectors in the US right now, but definitely not in our little niche because, when the market crashes, as it no doubt will at some point, that's when we do our best. So we're a full on contrarian play. So, as there becomes more need for affordable housing because of people losing jobs or whatever the case may be, that's what we cater to. So we're not really afraid of that. Our biggest problems in our industry would be mass prosperity. So if suddenly incomes doubled or Americans, like it happened back in the 60s', that would be a problem for the industry, but we don't really see any issues like that out there. So we're feeling pretty good about our positioning right now.

I mean, I don't really know of any mega trend that is not in positive for our industry, which is just a matter of luck. It's not like we were geniuses and we created it all and have been lobbying behind the scenes for America to turn out the way it has.

David Phelps: Right.

Frank Rolfe: It's just, our industry fell into place, so it's kind of our... It's been 50 years, it's kind of like... I live in Missouri and we're all excited the Chiefs won the Super Bowl. It's been 50 years since they did, and that's kind of how our industry is. It was in the dumpster for about 50 years, so it's kind of refreshing to see it's finally getting its time of fame once again.

David Phelps: The environment today, trillions of dollars looking for a place for more yield. And it seems like... And you mentioned just a minute ago, other asset classes probably top heavy right now. And Warren Buffet, certainly someone that I can't compare to, but he's obviously a contrarian and is kind of waiting for the next downturn. What would you tell an average investor, who's not a Warren Buffet but still wants to be invested but doesn't want to take a lot of risk? I mean, can you stay invested in intangible assets today? Do you stay with a buy and hold strategy if you're more of a passive investor? Do you have any kind of general thoughts on that?

Frank Rolfe: Yeah. I read a lot of books and I've read a lot of books on, for example, the great depression and what worked back then and what worked back then, the industries that worked were kind of the essentials. Shoes were big during the depression and then hope, which is a hard industry to quantify, which back then, resulted in bootlegging and things like that. I mean, we're obviously very immersed in the concept of essentials and low cost essential. So I think in the world of real estate, we're kind of the dollar store, and we have great confidence in that one finite niche. One thing I see when I drive around, as everybody does, is how the world has changed. And I drive by retail that's going empty, office that's empty. Lots of things have changed, but housing is kind of something everyone has to have, and they can't float you into the clouds in housing. I mean, it's very nuts and bolts.

So we really like our little niche. Beyond that, we just really invest just in mobile home parks. So we prefer that. I mean, there's other sectors. Storage fared fairly well in the last recession, which was a shocker. No one knew how it would do because people thought that everyone would pull their stuff out of storage units and sell it on eBay and shut down their $100 a month expenditure. What they found is that, people actually had more demand for storage in the downturn to try and protect their items as everything became unstable. The problem is that storage, because you can build them, you always are having to battle new construction. Our industry, we're just protected from new construction by the hatred of city government.

David Phelps: Right.

Frank Rolfe: So that's why we just, we're more comfortable in our little niche.

David Phelps: Whenever there's a long market cycle run like we've had, low interest rates, credit is wide open, again, like it was 12 years ago, a lot of new operators in all asset classes come out of the woodwork and they've never seen a downturn. It's a time for people that are investing their money and doing it through other people through funds or syndications need to really maybe, at least tap the brakes a little bit and be very wary. And as you mentioned earlier, the due diligence. You guys do the due diligence on the actual assets. If you're not a boots on the ground, as you and Dave are, and you're invested through somebody, then you've got to really do some due diligence on that actual operator. Particularly where we are today with so much money chasing deals, it's easy for, it seems like almost anybody, to raise at least a certain amount of funds today for whatever they want to invest in.

Frank Rolfe: Yeah. I think there's an old saying that, when the tide goes out, you find out who's swimming naked, and that's kind of true in our industry. A lot of people have jumped in, who don't have a lot of depth in management experience or how to do diligence on it. And I think the one item you really have to watch closely, if we do have a recession in 2021 or whenever that may be, is the financing market, because that's the first thing that leaves the building, is financing. A bank conduit agency, although we don't know an agency that's never... They haven't had a recession since agency started, but that would be another key item I would be watching out for, because if you lose the financing ability, if you're an operator who doesn't have a good track record and banking criteria tightens and they only want to finance people who know what they're doing, then you could have a real problem.

David Phelps: Is the financing that's available today, for operators that are in acquisition mode or refinancing, is it pretty lenient today? Are covenants pretty lenient? What are you seeing in that? What's available today?

Frank Rolfe: Yeah, it's actually... Right now, it's the most attractive financing we've ever seen. And the reason is, number one, the markets have been very, very stable for the last four years. But the other thing is that, our industry has the lowest default rate in real estate. So a lot of lenders favor what we do because they feel safe themselves being positioned in that niche of affordable housing. There's a bank, for example, in Illinois that we've done some loans with. They had not a single mobile home park loan, not too long ago, and I think now they're up to a hundred million a year or something of mobile home park loans. So people really, really liked that. They liked that space. And as a result, through performance, good performance, we now can get loans on mobile home parks through Fannie Mae and Freddie Mac at the same rates as giant office buildings. So the financing right now is very good.

David Phelps: So a lot of availability of Fannie and Freddie, longterm fixed, 20, 25 year amortization fully.

Frank Rolfe: Correct. Yes. In fact, it came out of nowhere. There was almost no Fannie, Freddie activity in the mobile home park sector just a few years ago, and today it's 50% of all loans and dollar value that have originated in the US in mobile home parks are Fannie Mae, Freddie Mac. So they came out of nowhere and they came out of nowhere because they were forced to by Congress under the duty to serve act. So we are, in fact, the only real estate sector, which has no ceiling on the dollar value of number of loans they can do annually. So they've been very aggressive in their lending, but so far so good. And I don't know of any defaults in Fannie Mae, Freddie Mac. They probably have some somewhere, but they still underwrite them very strongly because they, like anybody, are a little dubious of trailer parks. So they get an appraisal, they'll do 70% of appraised value. They won't do anything wacky, very sensible leverage. They've been a very big part of the lending scene.

David Phelps: So, when we have another correction... I know that you and Dave were oftentimes in relationships with a lot of lenders. You ended up taking defaulted parks that lenders took back and back then, there wasn't longer term fix rates of financing, so you had operators that were over leveraged. They were poor managers. They couldn't refinance when it came time for those shorter term loans that came due. And so you guys were right there and picked off all those properties. With longer term financing in place, do you think that's not going to be as big a deal after the next correction, or do you think we'll still see quite a bit of troubled operators?

Frank Rolfe: We keep our finger on the pulse of the REO market and the really good REOs in the last cycle were not where the park had gone down the drain, it's when the borrower has. They called them term defaults. So let's say the guy had gone out and bought a McMansion and defaulted audit during the 2007 downturn at home prices, now he's not bankable, but the park is. So they were not able to get new financing. Those were our favorites because you could literally buy parks that were in great operational capacity at huge discounts, so we liked that. The defaults you see today, if you talk to those who handled the defaults for the banks, the servicers, they're a different breed. These are typically defaults that were born of bad due diligence. I talked to one recently, horrific story, the guy that bought a mobile home park without any knowledge of what he was doing.

And he had, what's called a packaging plant, which is a standard feature. It's a private sewer disposal facility that the park owner owns. The problem was, it was broken and it had been pouring sewage for years into a waterway of some type.

David Phelps: Oh my gosh.

Frank Rolfe: And now, the cost to repair the sewage plant and to clean it up is more than the entire park is worth, so that's the kind of stuff. People who didn't know what they were doing with lenders who didn't know what they were doing, which is double compounding stupidity play. But that's been most of the defaults—a lot of the defaults. The REO we've seen, is not stuff you'd want to buy, it's stuff that you're more interested in the story to figure out, how in the world did that happen? It's like crime scene stuff. The plane has crashed, why did it crash?

Let's learn from that, but I don't really want to buy the crashed plane that burned up. So no, I've not really seen any attractive REO yet, no. Will there be some in the future? Well, perhaps, but I don't know if we'll ever be able to replicate the REOs that we saw over the last decade, because it was fueled by crazy buying prior to the great recession and then the whammy of the great recession after that. So I'm not sure we'll see that one, two punch again right now.

David Phelps: Yeah. Very good. Well, Frank, it's great to catch up with you. I appreciate always the information updates that you provide. It's interesting just to kind of, as you said, ride along with you. In this case, just right along with what you and Dave have been doing over the last decades and gain a little bit of insights for all of us who are investors in our own rights, and just trying to perform our due diligence and figure out, where the plays are, where the safety positions are and when it's time to jump back in. So we'll definitely be staying in touch. And as this year unfolds, I'm happy to be one of your longterm investors and we'll see what happens then in 2021, when your non-compete goes away and we'll be ready to roll with you.

Frank Rolfe: All right. Thanks a lot. Thanks for having me.

David Phelps: Thank you, Frank.

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