

Berkshire Group

Recently, **Jonathan A. Schein**, senior vice president, managing director of business development at Institutional Real Estate, Inc., spoke with **Larry Ellman**, **Alan King**, **Chuck Leitner** and **David Olney** of Berkshire Group. The following is an excerpt of that conversation.

Schein: *How has Berkshire evolved over the years, and where is the company now in this evolution?*

Leitner: For most of its 45-year history, Berkshire has been known as a family-owned, entrepreneurial multifamily owner/operator. At one time, it was also operated as a publicly traded REIT, but during the past 10 to 15 years it returned to its roots and has evolved into what it is today — a privately owned, institutional real estate investment management company with particular experience in multifamily investments and operations. We have approximately \$6 billion of assets under management in a variety of funds and separate accounts. In the early 2000s, we launched our first institutional multifamily value-add, closed-end, commingled fund. Our current multifamily platform includes core, core-plus, value-add, debt and development. Additionally, in 2010 the company started an opportunistic real estate venture capital strategy — initially with family capital — investing in real estate operating companies outside of the multifamily space. Today, we consider ourselves a fully committed real estate investment management company, investing in multifamily with a vertically integrated operating platform and with an opportunistic investment capability in non-multifamily operating companies and direct investments.



Chuck Leitner is CEO of Berkshire Group, responsible for leading the company's investment activities and operations. He has more than three decades of experience in real estate and investments management. Leitner most recently served as CEO of the ULI Greenprint Center for Building Performance, and as a member of the advisory council for Strategic Value Partners. Previously, he spent 24 years at RREEF in a variety of roles, including Global Head and Chairman. Prior to RREEF, Leitner held positions with GE Capital and TIAA/CREF.



David Olney is managing director and head of multifamily investments. As senior leader of Berkshire Group's Multifamily Investments group, Olney drives investment strategy and oversees multifamily transactions, property development, portfolio management, research and performance reporting for the company and its affiliates. With Berkshire since 1986, he has nearly three decades of real estate experience, having previously served as president of Berkshire Realty Holdings, L.P.



Alan King is managing director, head of multifamily property operations for Berkshire Group, and president, Berkshire Communities, Berkshire's property management division. King oversees approximately 600 property management professionals in more than 20 markets. King previously served as divisional vice president for the Western Division of Berkshire. He has more than three decades of experience in multifamily property management, having previously held senior positions with Archon Residential, McNeil Real Estate and Johnstown Properties.



Larry Ellman is managing director and head of venture investments for Berkshire, responsible for executing and directing the Berkshire affiliate's investment activities, building and managing the organization, and developing third-party capital relationships. He has more than two decades of experience in U.S. real estate investment, including debt, entity-level, joint ventures, direct acquisitions and CMBS. Prior to joining Berkshire, Ellman held senior leadership positions with Citigroup and J.P. Morgan Real Estate.

Schein: *Was the focus and mission change 10 to 15 years ago the result of a "Eureka!" moment, or was it a more gradual evolution?*

Leitner: It was a combination of the two. The company went from being a

family business to a public company during the 1990s, but it stayed committed to the operating platform that has always been part of the culture. As the public market became challenging, the family decided to privatize the company through a buyout

with Blackstone and Goldman Sachs. However, it then needed to find another long-term source of capital to grow the business, and so our strategy shifted to become a funds management business layered on top of expertise and operating capability in multifamily. Given the state of multifamily and its acceptability as an asset class by institutional investors, the timing was right to start raising institutional capital in the early 2000s.

Olney: There was also a realization of our entrepreneurial, value-creation experience. Public REITs tend to focus more on quarter-over-quarter growth, whereas in the institutional funds model, the focus is more on total risk-adjusted investment returns.

Schein: *So why is multifamily a good investment relative to other property sectors? Why is it your sweet spot?*

Olney: According to NCREIF data multifamily has been recognized as having attractive risk-adjusted returns over the long-term horizon compared with other property sectors. It is a great real estate diversification strategy because increased exposure to multifamily in a diversified real estate portfolio may help to increase total return and reduce overall volatility.

Schein: *What types of investment strategies is Berkshire employing for the multifamily market?*

Olney: It depends on the time horizon of the investor, but we

employ a diverse range of strategies including: property acquisitions in major markets, either stabilized or value-add repositioning, equity joint venture investments in select development projects, and purchasing securitized portfolio debt positions through our agency lender relationships.

Schein: *What does “major market” mean to Berkshire?*

Olney: We are looking at the top 20 to 25 markets around the country, including those in the Northeast, Mid-Atlantic, Southeast, Southwest, Pacific Northwest and California. We target two different types of markets. The first is markets with expected high job growth, such as the major Texas markets of Austin, Dallas and Houston,. The second is markets with some barriers to entry, where the development cycle is elongated, which creates a greater opportunity for supply/demand imbalance, and also where single-family housing costs are greater, making it more favorable to rent versus buy. These include markets such as Seattle, San Francisco, Los Angeles, Boston, New York and Washington, D.C.

Schein: *How does Berkshire add value through its vertically integrated property operations platform?*

Olney: When investing in a particular sector such as multifamily, an operator has deeper operational knowledge and is directly responsible for

management execution. This specialization and operational experience gives operators the potential to outperform allocators through more informed investment underwriting and more experienced property business plan execution capabilities.

Leitner: We believe Berkshire Communities, our operating platform, provides a fundamental advantage by being able to deliver extra value through maximizing revenues, and managing expenses and capital expenditures.

Schein: *What differentiates Berkshire Communities as an operating platform?*

King: Berkshire Communities is engaged from the beginning with every investment, and we have the ability to apply our experience and knowledge in the decision-making and underwriting process. In addition, our deep experience and history in the markets and submarkets where we are active allows us to easily identify both risks and opportunities. Our operational experience covers many facets to allow for better investment execution. Within Berkshire Communities, we have strong operational, marketing, redevelopment and training support teams. Because of our dedication to Berkshire-owned assets, we are singularly focused on driving property and portfolio performance, rather than on the profitability of the management company itself, which is often the case with companies focused on third-party management.

Schein: *How do you drive performance at the property level?*

King: We have tremendous in-house experience in applying revenue management systems, and decades of experience in multifamily. We have become extremely adept at managing to the ideal occupancy and rate-structure equilibrium necessary to provide top-tier revenue performance. Our years of experience have enabled us to optimize our strategies to manage through real estate cycles and seasonality in each market and submarket.



2020 Lawrence, Denver



Gatehouse 75, Charleston (Boston).

To manage expenses, we have implemented national purchasing programs and constant service contract reviews to maintain and minimize increases. We have an aggressive approach to property assessments to mitigate significant increases in property tax. We have a fully developed marketing platform that allows us to optimize marketing effectiveness.

Schein: *How has your model done at various stages of the real estate cycle?*

Olney: Berkshire has performed well over its tenure in both short- and long-term investing, helped by the fact that our property operational expertise can be applied over any time horizon.

We are not new to long-term, core investing. We have also executed on value-creation strategies, repositioning existing assets through accretive capital improvements, redevelopment, or through better operational management. When we came out of the last recession, we recognized the opportunity to overweight in real estate development, as we hit cycle lows across the country for land values and development; that has been a natural complement to our multifamily property operations. We have executed on equity joint-venture investments with national and regional developer partners and have built up a pipeline of almost 2,000 units, with many of those projects starting to deliver. These are high-quality assets in primary urban or close-in suburban locations in primary markets, close to employment centers, entertainment and public transporta-

tion. As a result, the completed projects have high rental demand.

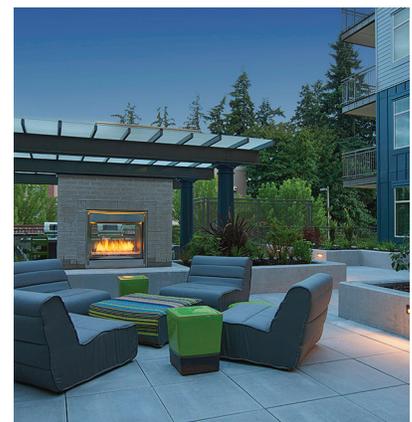
Leitner: What is really interesting about the multifamily sector, in particular, is that it lends itself to making a commitment to the operating platform and the vertically integrated approach. This model has existed for 45 years through a number of cycles, with the inherent expansion and contraction that is driven by cyclicity. We have typically had between 700 and 1,000 employees, depending on where we are in the cycle, so you have to be able to stay committed even on the downside. Through our public market activities, the family's commitment and investment in the business, and the ability to have a range of investment offerings with different time horizons, the company is positioned to stay committed to that operating model even with the volatility that comes with market cycles. With multifamily, you can manage your costs efficiently. As you buy properties, you staff up at the property level. As you sell properties, the staffing tends to move with the property, so you can manage your overhead appropriately. It is much harder to do this with commercial property because of how a commercial operating business is structured and staffed.

Schein: *What are some logical variations on the platform that you see as opportunities to add value?*

Leitner: We started the Berkshire Ventures business about five years

ago with family office capital. The themes have been related to Berkshire in a couple of ways. First, we are starting with family capital, so there is synergy in terms of who is investing in the strategy. Secondly, the primary focus for this business is on operating companies, carrying through the perspective that operating experience is crucial for investment success. We also focus on sectors that have some thematic relationship to what we have been doing on the multifamily side.

Ellman: Since we got into the ventures business in 2010, we have been investing on behalf of the founders of Berkshire. Our focus is on opportunistic and high-yield strategies through investments in operating companies at the entity and platform levels, and in GP positions in the real estate assets associated with these companies. We are focused on finding high-potential, young and growing real estate companies outside of the multifamily business, with management teams that are experts in their regions and sectors and with strong performance histories. Since we started, we have made three platform investments: a senior housing platform where we have a majority ownership position in a company that develops, buys and manages assisted living properties in the Northeastern U.S.; a hotel investment company that acquires hotels across the country, primarily assets in need of repositioning and renovation; and a medical office platform, primarily focused on acquisitions of well-leased operating properties.



Elan Redmond, Redmond, Wash.



Berkshire Medical District, Dallas

When working with our operating platforms, we take an active role in areas such as setting strategy, establishing capital relationships and capital structure, and helping to develop institutional processes. As a result we want to align ourselves with operators who see us as a value add — more than just financial investors.

Schein: *Do you limit your investments to multifamily companies?*

Ellman: Thematically, we are more focused on areas where we can leverage our skills and experience. Businesses that have investment or operating similarities to multifamily are obvious fits, as well as platforms where we can leverage our operating experience more broadly. At the same time, we are opportunistic investors, and if we see the potential for good risk-adjusted returns with a high-quality team and business plan, we are fairly open in terms of sector strategy.

Leitner: The thematic connections can be very broadly interpreted, such as working with a strong operator. Because of our business model, we know a good operator when we see one and, as Larry said, can add value beyond the capital we provide. Our operational experience can help that operator become more scalable and grow. For each of these investments, we put together very dynamic boards that Larry, the Krupp brothers and I sit

on. There is a lot of interaction around how to make that operator better and that is a thematic connection in its own right. It doesn't necessarily have to be directly related to multifamily for us to be excited about an opportunity where we think we can add value to through our process, our institutional framework and our perspective.

Schein: *Could you delve into some of the recent changes at Berkshire?*

Leitner: Berkshire continues to evolve from a family-owned owner/operator to an investment management company investing on behalf of institutional clients. Last year, we unveiled

new branding and have positioned Berkshire as a fully committed fiduciary and investment manager with particular experience in multifamily and opportunistic venture investing. At the same time, we also maintained our owner/operator heritage, an important part of our culture and how we add value. While the closely held private ownership of the company remains firmly in place, we recently evolved our corporate governance structure and established a new Berkshire Group Board of Directors, which includes Joe Azrack, Ron Blankenship and Jeanne Myerson, in addition to me and Berkshire co-founders George and Douglas Krupp. We also have added an in-house research capabilities, appointing Gleb Nechayev to lead economic and market research. Gleb sits on our investment committee and will also focus on developing a comprehensive Berkshire house view, combining extensive proprietary data from our operating platform with economic and market data to provide insights to help drive strategy and performance. Overall, we are focusing on our organizational structure so institutional clients can be assured we are fully committed to servicing them and the business of delivering returns for those investors. ♦

CORPORATE OVERVIEW

Berkshire Group is a real estate investment management company known for its vertically integrated operating platform and experience in the multifamily sector. Berkshire deploys capital primarily through equity, debt and development in the multifamily arena, as well as through opportunistic ventures in other real estate sectors such as senior housing, lodging, and medical offices. Over more than four decades, Berkshire's team of industry leaders has gained a reputation for being able to identify opportunities and effectively manage through various economic environments, establishing a long-term track record of solid performance based on thoughtful, leading edge strategies, and operational experience. The company has experience across the multifamily real estate spectrum in disciplines including acquisitions, asset and property management, debt, development, and redevelopment. Berkshire, a registered investment advisor, is headquartered in Boston and has offices in Atlanta, New York, Baltimore, Dallas, Houston and San Francisco. As of March 31, 2015, Berkshire Group had \$5.7 billion in real estate assets under management.

CORPORATE CONTACT

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