

Executive Summary

The Vendor Investor an Unintentional Partnership
By Larry Duncan, CAMTII, CAS, CAPS Emeritus

The pressure is on the asset manager to cut expenses and raise both physical and economic occupancy. When properties are in a cash bind they first look at operating costs. In doing so they place the vendor in the position of helping finance the business. Although it is not unknown to owner managed property they normally have more leeway in moving funds around to cover short falls whereas a fee manager is dependent upon the investor/s to support the portfolio. Ethically you should be completely honest with your vendors if this situation develops. You are asking the vendors who have and are providing products and services to your asset to become co-investors. Many times I have seen vendors go well beyond normal expectations if they know the rules.

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In the world of real estate ownership and management there are cycles and circles of economic well being. These movements are driven by forces from world events down to events on the very block where an asset is located. A downward shift of these financial factors can have a drastic effect on the operating capital available to the asset.

It could be a depressed market, an overbuilt market segment or a brand new competitor across the street or any number of other factors, but the result is a drop in revenue and a resulting cash crunch. The pressure is on the asset manager to cut expenses and raise both physical and economic occupancy. These goals are not always compatible. You must maintain the property to protect the value of the asset and you must turn vacant space into leased up units. It's a tough assignment when your site level income is not sufficient to cover current operation expenses.

When properties are in a cash bind they first look at operating costs. One way to relieve some of the pressure is to stretch out the Accounts Payable. In doing so they place the vendor in the position of helping finance the business. Five years ago I would have told you that pushing payables out to 45 to 60 days was unconscionable. Now in many markets it is not uncommon to see payables go past 120 days. Long before this, the vendor will have gone to the owner/manager and asked if there was a problem with their work or product and when can we get paid. This is a scenario seen more often with fee managed operations than those that are owner managed. Although it is not unknown to owner managed property they normally have more leeway in moving funds around to cover short falls whereas a fee manager is dependent upon the investor/s to support the portfolio. This is especially true where the investor/s have approved work to be done and it is now time to pay the bills.

Ethically you should be completely honest with your vendors if this situation develops. You are asking the vendors who have and are providing products and services to your asset to become co-investors. You can be assured that this was not their intention when they contracted to service your asset. These vendors are working in the same market as you and the things that affect your property affect all the other business that they service. They are running on narrow margins in order to keep your business. When you don't pay in a timely manner you put them at risk as well.

Consult with your suppliers and explain exactly what the circumstances are and what you are doing to correct them. Give them the option of standing beside you. Many times I have seen vendors go well beyond normal expectations if they know the rules. They will help get you through a cash squeeze and when you come out on the other side remember who stood by you. It is your reputation that is at stake if you get through the squeeze and then drop them over a half cent difference in price. At the same time do not judge them harshly if they are not in a position to become investors in your project.

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