Dedicated to distress

By Abraham Tekippe July 06, 2012

(Crain's) — As banks work to clear their books of bad real estate loans, David Ruttenberg is racing against the clock — and the competition — to capitalize on Chicago's distressed residential market.

Over the past three years, Mr. Ruttenberg, 31, and his team at Marc Realty Residential LLC have acquired nearly 60 multifamily buildings on the city's North Side, many of them failed condominium conversions. The firm, a joint venture between Chicago-based investment firm Marc Realty LLC and Chicago Apartment Finders, isn't stopping there.

With 600 units and counting, **including two recent acquisitions in Albany Park and Bucktown** , Mr. Ruttenberg now is eyeing the Chicago suburbs. Though it's harder to find distressed opportunities in the suburbs, demand for suburban apartments is strong and development has been limited so far.

"In most of the suburban markets, it's impossible to build; your yield-to-cost is going to be so low on new construction that most of the suburbs are just going to do zero construction for the foreseeable future," said Mr. Ruttenberg, principal and director of acquisitions and finance at Marc Realty Residential. "There's constrained supply and increasing demand, and those are obviously metrics that everyone likes."

In the first half of 2012, Marc Realty Residential averaged about one acquisition every 20 days, with this year on track to be the venture's biggest yet, according to Mr. Ruttenberg. While the partnership has finished a few failed condo projects it acquired, it operates most of its properties as rentals, with Chicago Apartment Finders handling leasing and management.

"The segment that we like to focus on is the $1 million to $5 million deal size," said Mr. Ruttenberg, who also serves as director of real estate investments at Chicago Apartment Finders. "I feel like that's where it's obviously too small for the really big players. . . .and it's too big for the one-off, non-real estate professional."

A native of Highland Park, Mr. Ruttenberg — no relation to Chicago developer David "Buzz" Ruttenberg — earned his bachelor's degree in quantitative economics from Tufts University in 2003 before getting a master's in real estate economics and finance from the London School of Economics and Political Science the next year. Before joining Chicago Apartment Finders in 2008, he spent two years as a principal at Citerra Capital LLC, a real estate investment firm based in Chicago.

Although Marc Realty had completed some residential deals before teaming up with Chicago Apartment Finders in late 2009, the partnership helped the firm establish a bigger presence in the market while giving Chicago Apartment Finders the capital it needed to build its portfolio.

In a recent conversation with Crain's, Mr. Ruttenberg discussed Chicago's housing market and the venture's long-term investment strategy as the economy continues to recover.

Here are edited excerpts from that interview:

Crain's: Does Marc Realty Residential focus exclusively on distressed properties?

Mr. Ruttenberg: Of the 50 to 60 or so properties that we've purchased, the majority are from banks either in

REO, note-purchased or short-sale. We are doing some purchases from estate sales. One of the buildings we bought — someone inherited a property, had no debt on it, but it was in such physical distress that it wasn't occupiable. So I consider that a distressed deal. Buildings don't have to be financially distressed to qualify as distressed; sometimes they're physically distressed. In that case, we utilize our construction team . . . and we utilize our general contracting company to rehab those products and bring them back to high-quality buildouts.

What are your investment criteria?

The way we look at a property is the first year is spent stabilizing the property, and then we want years two through 10 to run smoothly and we want year two to have a double-digit yield after debt service. . . .And we hope that years three, four, five, six, seven, eight, nine and 10 are going to have higher yields than the second year as buildings stabilize even further and the economy might pick up.

Obviously there's a limited supply of these distressed assets. When do you think that supply will start to run out?

I think there's another three years of the distressed market. 2007 was the height of the bubble. . . .All the five-year loans would have a 2012 maturity, so this year you're going to see a lot of maturity defaults. The owners might have been able to keep the payments current, but that doesn't necessarily mean they can refinance, because their loan base is just too high. That means that going into 2015, 2016, you're going to see the 2012 maturity-date properties hit the market for resale. The foreclosure process is a minimum of nine months, and we've seen properties go over five years.

While the condo market is far from recovering, there have been signs here and there that things may be turning around. What is your outlook for the market?

There's still so much supply, so I don't envision much new-construction condominium product to hit the market for a few years. A lot of the developers are talking about going back and building — guys that were building six-flat, 12-flat buildings are looking to acquire land and build new construction in Lincoln Park and some of the healthier markets. Some of the markets like Rogers Park, a lot of the South Side markets and the far North Side — Edgewater, Rogers Park, parts of Uptown — I don't think there's going to be a condo market there for a very long time.

Do you think you'll ever end up converting some of these apartment buildings into condos or back into condos in some cases?

It's not what we're planning on, but it would be really nice if the condo market came back and we could convert a lot of these units. A lot of these units that we have are condo-quality and would be very easy to convert. It would just be a function of the market being ready for that.