

# QUARTERLY UPDATE

## CWS CAPITAL PARTNERS LLC

*CWS Capital Partners LLC*

# CWS

### CALENDAR OF EVENTS

**November 2017**

CWS Capital Partners  
Semi-Annual Conference Call

**November 23 & 24, 2017**

Thanksgiving Holiday and Day After  
CWS Offices Closed

**December 25 & 26, 2017**

Christmas Holiday and Day After  
CWS Offices Closed

**January 1, 2018**

New Year's Day  
CWS Offices Closed

**January 16, 2018**

4th Quarter 2017 Est. Tax Payment Due

**January 26, 2018**

4th Quarter 2017  
Quarterly Distributions Mailed

**March 15, 2018**

Year 2017 K-1's Mailed

**April 17, 2018**

2017 Federal & State Tax Filing Deadline  
1st Quarter 2018 Est. Tax Payments Due

**April 27, 2018**

1st Quarter 2018  
Quarterly Distributions Mailed

**May 8, 2018**

CWS Annual Partners Meeting  
Hotel Irvine (Irvine, CA)



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## HOUSTON: BACK FROM THE ABYSS

*By Gary Carmell*



Some time has passed since the devastating flooding that took place in Houston. This has allowed us to wrap our arms around the damage and to formulate some initial thoughts on the impact of the flooding on the apartment market. I also think it is important for our investors to know what CWS did to prepare for the event and the actions we took during and after. My experience in having been in the apartment business for nearly 30 years is that the best property management companies tend to outperform more so by not losing rather than aggressive attempts at winning. In other words, it's easy to ride a rising tide but much more difficult to recover quickly from issues when they arise. And issues arise more often than we would like. Having a deep organization with well trained and competent people in many important disciplines (e.g. capital projects, risk and safety, property management, training, I.T., human resources, accounting, asset management, etc.) can allow a company to better prepare for and recover from challenges such as personnel leaving, catching underperformance and financial red flags early, identifying and managing through physical problems at properties, and dealing with emergencies like what we experienced in Houston. Before going into the specifics of our preparation

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and response, I thought I would briefly discuss our current thinking about the apartment market. The first observation is that the amount of damage to the apartment stock was far less than initially estimated. Reports I had read at the outset pegged the damaged apartment stock at about 10%. One report I read estimated that it's probably closer to 2 or 3%, which is what CWS experienced, while a more recent one from RealPage, which is probably more credible given its large property management software penetration in major markets, estimates that up to 43,000 units, or 6%, were damaged. What is probably most important, however, is the economic demand or the number of displaced people that can afford the available apartments. Although the flow of traffic to apartments has increased, the economic demand is such that many displaced individuals are not able to afford the higher rents at communities like those owned by CWS. There also may be a delayed effect on demand as large numbers of people are still in hotels or living with friends and family and need some time to get back on their feet to re-form their households again. Despite less demand than we thought from the hurricane, we are definitely seeing an improving market.



Marquis on Memorial

Last quarter I touched on Houston and thought that the revenue downturn would bottom for our portfolio in about 12 months (now about 9 months). I may have been a bit too pessimistic in the wake of Hurricane Harvey. For the first time in about two years we are seeing our average rents starting to rise in our same store portfolio as well as improving occupancy. Not surprisingly, we are observing strength in the western suburbs where a lot of flood damage took place. While there are some pockets of strength as well in the more urban, inner loop, it's not across the board as that area did not sustain much damage and commuting times make it difficult for someone to easily move from the western suburbs to the inner loop and downtown, especially with kids in school.

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I would expect occupancies and rents to continue their uptrend over the next year. Two wild cards from an expense standpoint are property taxes and insurance. There has been talk of the city wanting to add a one year surcharge of up to 9% on property owners to help cover the costs associated with Harvey. In addition, insurance costs are expected to go up given the losses incurred by insurance companies. It was already challenging buying properties in Houston as large numbers of buyers were eagerly targeting Houston as it was still perceived to be a soft apartment market but on the cusp of an upswing. Most of these buyers were hoping to purchase from owners who may have been under financial pressure to sell. This has not materialized as the downturn was not significant enough to produce any meaningful amount of distress. We were fortunate to buy two properties in the last year even though we had a much bigger appetite.

It's still early to tell the full impact of the displacement of Houstonians on the apartment market, but the early signs are relatively encouraging and we are fairly optimistic that 2018 should see revenue growth re-emerging in our portfolio.



Marquis on Memorial

From a property damage standpoint, three properties had flooding such that 168 ground floor units were taken off line. We estimate the totality of our insured loss will be approximately \$26 million. This includes loss of rent coverage which allows for the properties to continue collecting income while we repair and re-lease the units. We are very pleased that our insurance brokers suggested a few years ago that we aggregate our flood coverage in Houston and not rely on per property coverage. This was really helpful. For example, another owner had \$10 million of flood coverage per property but they estimate their loss to be \$12 million before including the loss of rents for one of their properties, leaving them with a \$2 million+ gap. Our aggregate coverage was \$50 million for the Houston properties which served us well as some properties had more

*Continued on Page 4*

than \$10 million of damage (important if we had secured similar coverage as the other owner) but the aggregate loss was substantially less than \$50 million.

All of the properties that sustained material damage have loans on them from Fannie Mae. Fannie Mae also happens to be our largest lender. They reached out to us to have a call to go over our damage assessment and how we were handling the situation. We discussed with them all of the actions that we took in response to the hurricane and subsequent flooding as well as the preparatory actions that we carried out. They were so impressed with how quickly we were able to mobilize our internal teams, external contractors, the insurance company adjuster, and building consultant as well as the steps we took to help our residents that they asked us to do a write-up that they could distribute internally as a model for how they believe their borrowers can handle crises. We were happy to do this for Fannie Mae and my colleague **Justin Leahy** put together a terrific summary of the key actions that we took as part of our response and preparation plan. I am going to take liberty with what Justin wrote and reproduce much of it here.

I want to particularly acknowledge the head of our risk management and safety program **Shanna Berrien** and our insurance brokers at Epic for the incredible job they have done, not only in response to the challenges we faced, but also for their preparation in terms of the coverages that we had and the safety teams we had in place to help minimize our financial exposure and to be able to act quickly and effectively to protect lives and properties.

### **Customer Service/Resident Care**

Due to the magnitude of this storm, along with the uncertainty of the situation, CWS' residents were understandably concerned. CWS took the following steps to ensure its residents remained informed, as well as helped affected residents find alternative housing arrangements.

- CWS Froze Unit Availability and Pricing – CWS stopped leasing in all available units within our Houston portfolio when the storm hit. This ensured that any affected residents would have housing options available to them. Additionally they froze rental rates at each of their assets for existing residents.
- \$500 Resident Credit – CWS offered residents residing in uninhabitable units a \$500 moving assistance credit. Residents did not have to relocate to another CWS property to receive the credit.
- Rent Forgiveness – CWS determined that no rent was due on units that did not have habitable conditions. These conditions include power failure caused by flooding and not having access to potable water. Further, if a property wasn't safely accessible due to flooding, CWS abated rent for those periods. If a resident had already paid rent, CWS



- refunded residents for the items above.
- Varying Lease Terms – CWS allowed affected residents to sign leases with varying lease terms. This helped provide residents flexibility to potentially move back into their affected property once reconstruction has been completed.
  - Resident Hotline – CWS immediately set up a customer care hotline in the Austin headquarters for resident questions. This hotline was staffed with other managers in the CWS portfolio to ensure property resident communications both during and after the storm.
  - In-Person Customer Care Center – CWS set up a customer care operation at a non-flooded CWS asset for affected residents to have the ability to communicate in person with CWS representatives. This was set up to assist residents with any relocation needs to other CWS communities that could be offered.
  - On-Site Customer Care Centers – At affected properties (once the water receded) there were CWS representatives set up to assist residents in terminating their leases, answer questions, and in some cases to give hugs and just listen.
  - Other General Communication – CWS used a multitude of platforms to communicate with residents during this difficult time. From social media, to emails, as well as direct phone calls, CWS has been over-communicating to ensure their residents remain informed.

CWS has taken the stance to “Bend Over Backwards” to help our residents through this tough time.

### **Remediation/Renovation**

CWS moved quickly to begin the remediation process to help mitigate further cost to the assets before significant mold growth caused further damage. While some properties remained under water longer than others, CWS was able to get remediation/demolition crews on to each property within 24 hours of the water receding to begin carpet and sheetrock removal, water extraction, and to place blowers and dehumidifiers. A full update on the affected properties is as follows:

Marquis at The Woodlands – Eight of 13 buildings, as well as the leasing office, sustained flood damage. In total, 50 ground floor units were deemed uninhabitable out of 280 units total at the property. At this time all the affected units have had damaged sheetrock, flooring, and cabinets removed. The rebuild has begun and most of the damaged sheetrock has been replaced. Unit interior selections have been made for longer lead-time materials such as cabinets, countertops, and appliances. We anticipate having construction completed and the units back on line for leasing around late January 2018.

Marquis on Memorial – Eight of 10 buildings sustained flood damage. In total, 39 ground floor units were deemed uninhabitable out of 104 units total at the property. At this time all the affected units have had damaged sheetrock, flooring, and cabinets removed. The rebuild has begun and to date the sheetrock has been replaced in the stairwells to the second floor units with the sheetrock repairs on the first floor units to begin shortly. We anticipate construction will be completed on the second floor stairwells by the end of November, and the first floor units should be completed by the end of March 2018.

Marquis at Cinco Ranch – All buildings sustained flood damage including the leasing office. In total 78 ground floor units were deemed uninhabitable out of 260 units total at the property. The demolition and remediation process was more complex than initially expected and was completed on October 16th. At that time all damaged units were handed over to the construction team to begin the rebuild process. Unit interior selections have been made for longer lead-time materials such as cabinets, countertops, and appliances. We anticipate having construction completed and the units back on line no later than April 2018.

Marquis Lofts at Hermann Park – CWS secured large diesel pumps prior to the water receding to ensure rapid draining of the basement flooding. Once the water was fully pumped out, CWS had contractors lined up to repair the damaged mechanical systems. At this time the property is fully functional and is 100% back on line.

As evidenced above, CWS has been very aggressive with regard to the demolition/removal of damaged materials to prevent further costs. CWS is hopeful to have all down units repaired and back in service within 3 months, possibly sooner. CWS takes the habitability and long-term viability of our assets very seriously. The storm recovery is a top priority of CWS and we have been putting a multitude of corporate and local resources to work on this.

We are very proud of how we were able to come together to serve our displaced residents, work quickly to remediate, demolish, and begin reconstruction of our impaired units, as well as the comprehensive coverage we had for this event which should end up having very little financial impact on the properties that were impacted. We also set up a non-profit with one of our largest investors to help provide financial support for CWS employees impacted by the flooding. To date we have distributed over \$40,000 from this fund. The esprit de corps of CWS really shined through during these trying times and we were able to pull together and do what was necessary to help our residents and get right to work repairing our properties. I hope this recap shines a little light on some of the things that make the CWS culture so special.