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## Water's Effect on Real Estate Investing

### Greetings!

If you are a fan of Fox News you may have noticed the recent coverage on the Historic Draught in Southern California, and its unfortunate impact on local businesses. In Atlanta, we know this theme all too well having lived through the great draught of 2007 which continues to linger. You may not have noticed its impact, but it's there in every water bill you pay and a hot topic in the courtship conversation between the Metro Atlanta Chamber and prospective corporations. The impact of fresh water availability on communities is significant and episodic draughts have the potential to cripple economies. And guess what, this problem is only going to gain traction and be a growing factor between the "haves" and "have not" cities for future growth. The tension building between many states over access to fresh water is becoming the new normal, which outcome will make or break the ability of these states to compete. Take note of a few facts:

1. **More People. More Water Consumption:** A recent Columbia University Water Center study on water scarcity in the U.S. showed that it's not just climate change putting stress on water supply, it's also a surging population. Since 1950 there has been a 99 percent increase in population in the U.S. combined with a 127 percent increase in water usage.
2. **Lack of Raw Land to Absorb Water:** A major contributor to the growing water problem is the way we develop land. As we pave over more and more wetlands and forests, this new report shows that we are depleting our fresh water supplies. The consumption of raw land by U.S. suburban sprawl jumped 50% from 1980-1990 alone, according to the Department of Agriculture's Natural Resources Inventory. It's not only the arid West that is facing critical shortages. The rapidly suburbanizing Southeast, blessed with a seemingly inexhaustible water supply, is now flirting with its limits, as are many other formerly water-rich regions of the country. Wetlands act like sponges, absorbing precipitation and runoff and slowly releasing it into the ground. More than one-third of Americans get their drinking water directly from groundwater, and the remaining two-thirds who depend on surface water also are affected, given that about half of a stream's volume comes from groundwater.
3. **Ground Water Depletion Accelerating:** Estimated groundwater depletion in the United

States during 1900-2008 totaled approximately 1,000 cubic kilometers. During the 21<sup>st</sup> century thus far, the depletion rate averaged almost 25 cubic kilometers per year or almost triple the 9.2 cubic kilometers per year averaged during the 20<sup>th</sup> century.

4. **Demand to Exceed Supply:** Global demand for fresh water is projected to exceed supply by 40% by the year 2030.

**A Solution?** Many savvy governments are realizing that by changing policies to influence constituent behavior, there is a way to reverse the growing water problem, and the cities that are progressive in water management will be the clear winners in the future. For example, by using smart techniques, many cities are directing growth to communities where people already live and work, thus limiting the number of new paved and other impervious surfaces that cover the landscape, make existing communities more attractive, and discourage new infrastructure that alters natural hydrologic functions and increases taxpayer burdens. Atlanta is an example of one of these cities, adopting mixed-use high density zoning categories and enacting impervious surface requirements in their permitting process. Several cities have started charging a utility fee associated with impervious surfaces that prevent the infiltration of storm water into the soil, hoping to motivate property owners to limiting concrete, driveways and other hard surfaces.

**Cities to Watch:** When investing, pay attention to the major cities that are exposed to potentially severe water shortages in the not too distant future. The water shortages are due to many factors including global warming, rising sea levels, aging infrastructure, population growth and drought/weather patterns:

- Las Vegas, Nevada
- Salt Lake City, Utah
- Lincoln, Nebraska
- Cleveland, Ohio
- Miami, Florida
- Washington, D.C.
- El Paso, Texas
- San Antonio, Texas
- San Francisco, California
- Houston, Texas
- Los Angeles, California

Poor planning by these cities will force them to take drastic and expensive measures which translate to economic hardship for business and investors.

As we underwrite deals at TriStar, we are taking note of the growing water politics and impact on real estate investing, and have started underwriting deals with a "water dependency" factor. Aging apartments and commercial properties where the suites are not individually metered thus allowing landlords to pass through direct water usage, have the potential to be noncompetitive by exposing the investors to the chasm of increasing water invoices and unmotivated tenants to conserve. Real estate investment in areas that are tied to the success of local lakes and rivers may also render obsolete in the future.

Please see our sample investment target of the month.

**Investment Target of the Month**

**The Auction**- this property came to us via an online auction and sold for a little over \$2 million dollars. The bank had just extended the lease of a national retailer yet there was some vacancy left for a value add investor to buy with good returns. Some lessons to learn:

- **Due Diligence** -Auctions require significant due diligence prior to bidding. If you win there is no turning back unless you want to forfeit substantial earnest money.
- **Narrow Playing Field** - you can't participate in most auctions unless you can show proof of funds, in cash, to close. All cash buyers over the \$2 million range are not as abundant.
- **Buyer Profile** - when trading in the \$2 million and below price range, you have buyers who may overpay for an investment. This may be due to inexperience (new investor who wants to play in real estate) or a 1031 exchange buyer who may be more interested in *not* paying taxes rather than on investment returns.



The auctions can provide an opportunity for a savvy investor but only after tremendous efforts are made in advance. But even the successful bidder can eventually lose. Many winning bids are subject to further approval from Trustees or banks who act as fiduciaries for third parties. The motivations to sell can change based on rational or irrational motivations.

Please reach out to us if you have questions about investing through the auction process or with questions about one of our funds.

Sincerely,

TriStar Partners

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