PODCAST TRANSCRIPTION SESSION NO. 81: ALLEN SHAYANFKER

Welcome to the Lend Academy Podcast, Episode No. 81. This is your host, Peter Renton, Founder of Lend Academy.

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Peter Renton: Today on the show, I am delighted to welcome Allen Shayanfker, he is the CEO and Co-Founder of Sharestates. Sharestates are a relatively new real estate platform, they've been in business really just for barely two years, but I've been hearing their name around a lot so I wanted to get Allen on the show to talk about his company, talk about what makes them different and they certainly are very different, I think, to many of the other real estate platforms out there. We talk about how they source deals, who their investors are, their approach to achieving scale and much more. I hope you enjoy the show!

Welcome to the podcast, Allen.

Allen Shayanfker: Thank you, thank you very much, Peter.

Peter: Okay, why don't we get started by giving everybody a little bit of background about yourself and how the arc of your career has gone up until the time you started Sharestates.

Allen: Sure, so my family actually came from a foreign background, Persian Iranian Jewish, moved here in 1988, left everything behind for various reasons, primarily religious, moved to the US in 1988 and started from scratch so I grew up in a working class family, mother and father both working, grew up kind of on the other side of the tracks, I guess you could say, started my first job at the age of 14 making $5.15 an hour at a Dunkin' Donuts/Baskin Robbins and then continued to work (laughs)...yeah, it was a fun time and then continued to work multiple jobs throughout high school, college; everything from a movie theater to the restaurant industry.

Ultimately went to law school, had a couple of internships at various law firms and then over a Shabbat dinner on a Friday night was trying to figure out what I was going to do post graduating law school and whether I was going to start my own firm or a business of some kind and that's where the idea for Sharestates came about.

Peter: Interesting, interesting. So tell us about that dinner a little bit. What was the conversation that really prompted you to go in this direction?

Allen: So my two partners today, Raymond and Rodney Davoodi have actually been in the real estate industry for about 15 years and back in 2008/2009, they had this concept for what was basically a real estate crowdfunding company, but the regulations weren't there, the market wasn't there, real estate in general just wasn't doing well at that time so they decided to put it off.

Originally, the idea was to start this equity-based crowdfunding platform where they would essentially do their own projects and bring in their close network of friends. One of my partners asked me...if you could buy a piece of a building on your credit card for $1,000 or a couple of thousand dollars and have the benefit of cash flow and rental income, etc. moving forward, would you do that as a way to get involved in the real estate game on kind of a smaller scale?

Of course, my answer was yes, I've always grew up wanting to own real estate, just didn't really know how I was going to get there and know how I was going to finance something like that so I started jumping into the regulation a bit more. This was in 2012/2013, had a couple of dozen interactions with the SEC, New York Attorney General's Office, figured out all of the compliance and regulatory issues and said...hey, guys, we could actually make this a viable business, but let's pivot a little bit and instead of doing our own projects, let's kind of make this a marketplace or matchmaking system where we could provide debt and equity financing to other real estate speculators and developers and that'll make it more scalable for us. So let's find investors, let's find real estate professionals that need financing and kind of put them together rather than just doing our own deals.

Peter: Right, right. On your website it says that our founders have been crowdfunding for over a decade, do you mean that you were starting to crowdfund before Sharestates for your own deals, is that what you mean there?

Allen: Yeah, so real estate crowdfunding is kind of a buzz word now. It really came out of the JOBS Act which President Obama put into effect in 2012, but the core concept of real estate crowdfunding is real estate syndication and that's been around for decades, if not centuries. So my partners have been arranging debt and equity financing for various clients of theirs over the last 15 years just inherently in their other real estate operation.

So whether it was their title insurance clients, whether it was their own projects, etc., the core concept of bringing together a crowd of people, whether it was 5, 10, 15, 20 or otherwise has been there for a long time. The term crowdfunding is a buzz word now and it's the process of taking that old school method online and making it more efficient and more cost effective, but it's been there for as long as I can remember.

Peter: Right, right. Okay, so why don't you just, for the listeners, describe your company, what part of the market you focus on and how it works?

Allen: Sure, so today Sharestates is primarily a debt-focused platform, we're mostly on the East Coast, most heavily in the northeast working with one to four family residential fix & flip properties, small to mid-balance commercial properties really all for a short-term bridge product where our loans are going out for 12 to 18-month periods on value add development projects that need some sort of TLC or rehab work and then our borrowers are going to traditional financing sources by banks to take us out.

Peter: Okay, obviously, you're in a competitive market. I know that there's dozens, but there is probably I would say five to ten platforms that are really doing well and you guys are one of those five to ten platforms, what would you say differentiates you from your serious competitors?

Allen: So I think our backgrounds and our access to deal flow are pretty much the two biggest factors for us. Most of the other platforms that are out there today that are doing well are being run by people that have a finance or technology background, whereas we came from the other side which is just purely a real estate background. So coming into this business, we knew everything from how to originate a deal, to getting an application, to generating a term sheet, negotiating that term sheet, getting that signed with a deposit, taking it through processing, taking it through preliminary underwriting, taking it through final underwriting and then of course, closing and settling the loan and then post closing.

So we were able to actually build our technology around that and make a pretty fluid and seamless process, whereas I think what some of the other platforms' experienced was…coming from a technology or finance background they built these beautiful platforms that were aesthetically very pleasing and functionally worked well, but they had to go back and kind of piecemeal, add different things to it to kind of complete that A to Z process and we just kind of had an advantage there. Aside from that, it's really our general ability to generate deal flow.

So we came into this industry with a book of business, primarily from my partners, Ray and Rodney, who got started doing their own real estate projects and eventually became a service company for speculators and developers, both on the title side as well as the syndication side. So right off the bat, we had access to hundreds of millions of dollars worth of transactions that we could kind of cherry pick and then make available on our platform for both our accredited investors as well as our institutional investors.

Peter: Right, right, I think that's so critical. I mean deal flow is probably one of the major challenges for all platforms really, whether it's small business, real estate or consumer. Can you just tell us a little bit about…I know you've got this company called The Atlantis Organization which your co-founders are also co-founders of that, can you just tell us maybe a little bit about that and what kind of deals you cherry pick from...I presume that's what you're talking about as far as where these deals are coming from...how you're able to cherry pick?

Allen: Sure, so Ray and Rodney actually started The Atlantis Organization back in 2005. Prior to that they were developers and speculators just like anybody else, doing fix & flips, some ground up condo construction, some small multi-family buy and holds, that sort of stuff and in 2005 when they started their title insurance company, they pretty much put everything they had into it.

For those that aren't familiar with title insurance, it's probably one of the most difficult businesses to scale and grow because everybody, and I really mean everybody, has a relationship. So you've got an uncle, a friend, a colleague, somebody that's in the title insurance world and those people drive business to the title insurance companies. So really at the end of the day, for somebody to be able to scale that business, it's all about what auxiliary services can you provide, how can you go above and beyond just providing a title insurance policy so they branded themselves as a suite of real estate solutions and they called that The Atlantis Organization so it meant providing brokerage services, providing networking events and connecting clients to one another.

Sometimes they'd have a client who sold an asset and had some capital to place and another client that was looking for financing and they would connect these guys without really monetizing it, but more so for business development. Ultimately, it allowed them to capture a pretty large marketshare and because of the way they grew their business, about 50% to 60% of their client base ended up being speculator and developer businesses who are the very people that need the type of financing that Sharestates provides today.

Peter: Right.

Allen: So because we have that pipeline we could then go in and we were able to see what the appetite from the investor community was...are you looking for one to four family residential, are you looking for mixed use, are you looking for commercial or retail and we could then approach existing clients of ours and say...hey, guys, you've been dealing with us for over a decade, you love our service, you love everything that we do for you, well now we can also provide this additional service which is to provide you with your short term financing.

Peter: Got it, no that makes perfect sense. Are you saying that the bulk of your deals today are coming through Atlantis?

Allen: Originally when we launched the platform, yes, a bulk of our deals were coming through Atlantis. Over the last year in 2016, we've made it a pretty heavy focus of ours to actually diversify our deal flow sources to a few different avenues so we have a sales team now...without giving away our trade secret...

Peter: Sure

Allen: ...we have very targeted campaigns and plans for how we go about generating deal flow and I think the numbers kind of speak for themselves. Our full launch was in February of 2015 and really over the last year and a half or so, a little over a year and a half, we've managed to originate about $200 million worth of volume across almost 300 projects and we're well on track to probably do more than double that in 2017.

Peter: Okay, that's quite impressive. Can you just talk about it…you said you're mainly doing bridging, short term financing, can you give us some idea of the loan term. Are these like 6 months, 12 months, 18 months; what is the range of interest rates you're offering as well?

Allen: Sure, so the average loan that we issue is on a 12-month term with an option to extend for six months, I'd say the average life cycle of our loans today are probably about nine to ten months and we've had maybe 25 loans or so actually take advantage of the extension clause. Our interest rates are typically between 9% and 12%. We're actually actively working on sourcing cheaper sources of capital so within the next 60 days or so we should be dropping our bottom line interest rate down to 7.5%.

Peter: Okay, so tell us a little bit about then…you wrote your first loan in February 2015, is that correct?

Allen: So we actually had our beta launch in July of 2014 and I think our first actual loan was written in November 2014, but then our full launch was February of 2015 and that's when we really started to pick up speed.

Peter: Right, so you would have had many loans that have gone through your system now. Can you give us...are all the loans in good standing? I mean, just describe sort of the health of your loan book.

Allen: Sure, so after 300 some odd loans we have done about 50 of them have come full term and been paid off totaling about $80 million plus in return of principal and interest. To date, we have zero loss of principal. We of course have had some loans go past due in which case most of them have been worked out and I think we've had a total of about four loans actually move into a default or foreclosure status. We actually had to file foreclosure in I think four instances, two of which were worked out prior to the foreclosure action actually being completed. Those loans ended up being more lucrative between default interest rates, late fees, etc. than had the loan actually performed in ordinary course...

Peter: Right.

Allen: ...and the other two are currently ongoing where we have I believe a 40% to 50% loan-to-value ratio so we're very well collateralized there and we anticipate that those two loans will also work out prior to actually being foreclosed on so we're in a healthy place.

Peter: So what is the typical loan-to-value then of your deals?

Allen: Across our entire platform, our loan-to-value ratio is about…fluctuates between about 55% to 60%.

Peter: Wow, that's pretty low. So let's talk about the other side of the platform, the investor side. Can you just describe who is actually investing in your loans today and you mentioned another deal...I know you're not going to tell me who or what, but give us an idea of who is doing it today and who you're focusing on for the future?

Allen: Yeah, so when we first launched our platform our focus was almost entirely on the crowd. We realized pretty early on in that process that the crowd being our accredited investors were ultimately our long term goal, but in order to scale and gain legitimacy and basically a healthy balance sheet that would make sure we're going to be around for the long term that we would need to diversify with institutional capital as well.

So in May of 2015, we brought on our first institutional investors that was the Ranger Capital Group. They came in on the fractional investment side of our platform which was amazing for us because that allowed us to basically match individual accredited investors and that institution together allowing them to invest in the same deal flow side by side and ultimately issue loans to our borrowers. Since then we've gone on to bring on about eight different institutions, some of which we've disclosed, some of which we're under confidentiality agreements and we can't disclose, but we've totaled about $1.25 billion in total capital commitments.

So moving into 2017, we have a ton of funding, it's just a matter of growing our originations in a scalable and responsible way. We don't want to sacrifice any of our underwriting criteria and loan criteria in order to just grow for the sake of growing so we are taking a very methodical approach to that. I'd say today about 80% of our overall capital is institutional and 20% is accredited investor crowd and I'd say long term…our goal is always to diversify our capital sources.

Just like any investor wants to diversify their portfolio, we want to make sure that we have a healthy group of investors that we could go to which is going to encompass both accredited investors and various institutions so that we're never basically left trying to chase capital in any sort of an economic downturn or otherwise.

Peter: Right.

Allen: That's going to be our focus for the remainder of 2017, and I think as this industry matures and as the institutional world realizes more and more that this is actually a relatively safe product that also provides some form of yield and liquidity, depending on how you actually invest that capital, you know, we can start garnering interest from pension funds and insurance companies, etc.

Peter: That makes sense so it seems like when you go to the homepage of your website, which I'm on right now, it seems like you're obviously, at least online anyway, you're focusing on individual investors because you say...invest in real estate with as little as $1,000. That's clearly an individual investor play so the individual investor, at least from your outreach online, sounds like you're still very much focused on the individual.

Allen: Yeah so our primary goal and our primary company initiative is to grow the individual accredited investor base. Going back to what I said earlier, we realize that the best way to do that would be to build a very healthy company that people who would know would be around for the long term. So it's a difference of…as an individual investor do you want to invest in a company that has issued maybe $10 or $20 million in loans, might not have a great balance sheet, you don't know if they're going to be around long term, what happens if that company goes belly up, who's going to service my loan, etc.

Or would you rather invest in a company that's done a billion dollars in loans and maybe 80% of their capital is coming from institutional partners but you know that they're profitable, they're profitable month over month, they have a healthy balance sheet, there's really no risk of them going belly up and they're going to be there long term to continue servicing your loans and give you access to new deal flow. So our online initiative, all of our marketing, everything is really targeted around growing our registered user base, that is the individual, and then the institutional side of things is a little bit more manual, you know, that's more direct outreach.

Peter: Sure.

Allen: We have capital market executives that are actually reaching out to private equity companies, hedge funds, pension funds, insurance companies, etc. and setting up those relationships.

Peter: Right, so I just want to go back to something you just said there, that is you're saying, profitable on a month by month basis. Is that where you guys are at today? I mean, you started less than two years ago it sounds like, but just tell us a little bit about the status of cash flow positive, profitable, or what have you.

Allen: Yes, definitely. So we actually became profitable in August of 2015. We've been profitable month over month with the exception of February 2016 where we had a slightly slower month because we were short on capital commitments from institutional partners. We had a couple of deals that should have gone through by then, but did not so that got pushed back into March/April, but aside from February, we actually have been profitable month over month. We don't have any debt on the books; we're still a self-funded company, we actually bootstrapped this with what started as a $25,000 loan in 2014 or 2013, and that grew to about $250,000 loan before we turned a profit in August of 2015.

Peter: Okay, interesting. You mentioned raising money, you haven't raised any outside equity, but I see that you're currently raising equity on SeedInvest. Can you just tell us the thought process behind that?

Allen: Yeah, definitely. So we have been self-funded to date. This round that we're doing through SeedInvest will actually be our first capital raise round, we're calling it our Series A. Really the primary purpose of that capital raise is to put additional equity capital on our balance sheet to qualify us for essentially warehouse lines or revolving credit lines and ultimately for roughly every $2 to $3 million that we raise in equity capital that'll qualify us for about $15 million in a revolving line. We can take that revolving line, pre-fund our loans and then make them available on the platform to our crowd or to our institutional partners.

Given that we're profitable, we could very much just wait and let our balance sheet stack up organically over the next 12 months, but ideally what we'd like to do is really scale our originations and in order for us to do that we need these revolving facilities. So we have a healthy offering at a $35 million pre-money valuation and that capital is essentially just going to go into a reserve account which will qualify us for those revolving lines and that capital won't really be used for operational purposes.

Peter: Okay, so then you're not going the VC route at all, you've decided to give up that kind of capital or are you going to do that in addition to the SeedInvest?

Allen: I don't think that we're going to actually be going the VC route today, that might change in the future, reason for that being that when you go the VC route, at least in our experience and from the conversations we've had, two things happen. One, they want to make a sizable investment usually in the ballpark of $10 to $30 million depending on who you're dealing with and that comes with obviously giving up a larger chunk of the company, but also much of the management. Ultimately, we don't want to end up in a situation where we have a VC that's forcing us to grow because VCs are obviously looking for those crazy multiples.

They want to invest in a technology company that they're going to get a 200 or 300 times multiple on three years from now or four years from now, whatever that might be, and you end up in a position where you're forced to sacrifice underwriting criteria just to grow loan origination volume or otherwise. We just wanted to maintain control so we figured going with this smaller path which kind of fulfills our immediate need which is to have that equity capital for our revolving lines also gives us the benefit of maintaining control and allowing us to do what we've been doing since day one which is methodically grow the company, make sure that we're retaining control, make sure that the wheels aren't falling off the bus so to speak, and that we have a healthy operating company that is going to be around for the long term.

Peter: That makes sense, that makes sense. You mentioned your billion plus dollars in commitment so I'm just curious about...what is really constraining your growth? You've got this unique deal flow, you've got these big investment commitments, are you growing just as fast as you want to and there's nothing constraining your growth or where do you stand on sort of the marketplace side of the deal flow versus investor?

Allen: That's actually exactly what it is. There is really nothing constraining our growth at this point. We have access to I'd say comfortably about $500 to $600 million worth of originations annually where we stand currently. We do have the capital backing us up; it's just a matter of putting the right processes in place and growing the internal infrastructure so that we can support a healthy process moving forward.

We want to make sure that our borrowers have great customer service, our investors have great customer service, that whatever reports or financial reporting that our investors or borrowers might need is prepared in advance and is ready to go. So at this point, what we've been doing is just hiring...I guess you could say it's an HR thing, we just want to make sure that our processing team can handle the load, our underwriting team can handle the load, our investor relations teams can handle the load etc. By example, we've gone from…including my co-founders and employees, we've gone from five employees in May of 2015 to about 40+ employees including our technology team today.

Peter: Right.

Allen: So we're growing very quickly and we want to make sure that we constantly have the right people in place.

Peter: Okay, that's interesting. I've got another question around...you mentioned you've got a technology team, how are using tech to really scale up your business because obviously you want to make this sort of as least labor intensive as possible. Obviously these deals are somewhat labor intensive just because every deal is unique, but how are you using technology then to really try and become more efficient?

Allen: So the technology piece of our company was more focused on the investor earlier on. Again, going back to what I said earlier, we came into this industry with a book of business of borrowers and what we were lacking this time last year was investor capital, whether it was from the crowd or institutions. So our primary initiative in building our technology earlier on was making sure that our online platform is accessible and working and user friendly for the crowd while also being functional for our institutional investors.

I can confidently say that today, our investor side of the technology is probably 90% to 95% of the way there; it's never going to be 100% complete because we're always going to be adding new tools, new functions, new modules like auto invest for the crowd etc., but it's working very well and that brings efficiencies to the table. So we can take investors' $1,000 investment, we can market to a crowd and have everything electronically signed, etc. If it wasn't for that piece, we wouldn't be dealing with the crowd or it wouldn't be possible.

Our initiative over the last few months and going into 2017 now is going to be building out the borrower side of the technology so making sure that the loan application, the term sheet generation, the processing and underwriting can be as automated as possible. While I think that one day, maybe a few years from now, the entire borrower function can be automated, we're not quite there today mainly because the real estate industry in general is just pretty antiquated and certain things just can't be automated.

For example, certain counties when it comes to things like title insurance or comes to searching the county records, are not in an online database. You have to physically go or there, has to be someone that physically has to go to the county and pull records. In a state like New York where you have ACRIS in New York City, everything is online, you can kind of automate that, but in South Carolina that might not be the case. So as the real estate industry catches up from a technology standpoint, we will keep automating more and more of that. Our goal is maybe sometime by 2020, we could have an almost automated process, but it certainly is going to depend on a lot of moving parts.

Peter: Right, right, understood. Okay, we're just about out of time, but I want to get the sense of what you're working on now as you look to 2017, is it geographic expansion, I mean, what are the sort of your big goals for the next 12 months?

Allen: Yeah, I'd say that we have three big goals. Number one is really scaling up our crowd marketing. We've done again pretty limited marketing to date so we want to place a heavier emphasis and focus on growing the individual investor base.

We would like to start looking at, as I mentioned before, really automating as much of the borrower side of this business as possible so there's a huge initiative on the technology side to push out a platform that'll, from the borrowers' perspective, be seamlessly automated so they'll be able to log into the system, submit their applications, get a term sheet, electronically sign that, see a dashboard where they're going to be able to track the loan processing of their loan, see when appraisals are coming in, see when title insurance abstracts are coming in, credit reports, background checks, etc.

I'd say our third initiative is going to be geographic expansion. Today, we're in eight states and I'd like to be in at least five to six more new states at some point through 2017.

Peter: Okay, great. Well on that note, I'll have to let you go. I really appreciate you coming on the podcast today, Allen.

Allen: Awesome. Thank you very much, I appreciate it.

Peter: Okay, see you.

Allen: Take care.

Peter: Today, we live in a very competitive market, whether you're talking consumer lending, small business lending, real estate. Online real estate is, I think probably the most competitive of all and to me it's refreshing and quite astounding in some ways to talk with a company that has gone from being founded to really being cash flow positive and profitable in less than 12 months.

I think it's so important for all companies today, with…VCs are no longer throwing money around like they were a couple of years ago and I know that valuations are down in many industries and for many companies, so having a path to profitability I think is so critical today and I'd like to see more platforms, particularly if you're a newer platform, really focusing on that because that gives you options. It gives you options to grow the business the way you want and really it allows you to be self-sustaining which I think there's a lot of companies in this industry that would love to be there right now.

Anyway on that note, I will sign off. I very much appreciate your listening and I'll catch you next time. Bye.

(closing music)

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