The Principles of War Applied To Real Estate Investing

By Joe Manausa, MBA

There are fundamental concepts that apply to the real estate investment industry that have also been found true consistently on the battlefield throughout history. Prudent investors could strengthen their positions by taking a lesson from our military history and doctrine.

This brief paper attempts to explain how investors can alter their strategic plans by using the same analytical techniques as would be applied by our modern warriors.

When I was a cadet at West Point, I was taught (early and often) that the art of war is ruled by 9 key principles. All of these principals must work in harmony with each other, meaning a commander who leans too heavily on one will be burned by another. The nine **Principles of War**, as defined by the US Army include:

PRINCIPLE	DEFINITION
Mass	Concentrate combat power at the decisive place and time
Objective	Direct every military operation towards a clearly defined, decisive, and attainable objective
Offensive	Seize, retain, and exploit the initiative
Surprise	Strike the enemy at a time, at a place, or in a manner for which he is unprepared
Economy of force	Allocate minimum essential combat power to secondary efforts
Maneuver	Place the enemy in a position of disadvantage through the flexible application of combat power
Unity of command	For every objective, ensure unity of effort under one responsible commander
Security	Never permit the enemy to acquire an unexpected advantage
Simplicity	Prepare clear, uncomplicated plans and clear, concise orders to ensure thorough understanding

The remainder of this paper will review each principle in order to demonstrate ideas and methods that real estate investors could implement in order to deliver better returns to their principals.

Mass – In warfare, resources are often scarce and they are always limited to some degree. The prudent commander knows how to “pick his fights” so that he can bring the appropriate amount of force to win the battle. Should the commander allocate too little of his force, he risks loss of personnel and equipment. Conversely, if he allocates too much to a battle, he leaves himself vulnerable on other fronts.

This is also true for the real estate investor. Regardless of the size of an investment pool, the key to maximizing returns is to concentrate the investor’s resources towards a strategy that allows this critical principle to bring about the best results for the investor. The principle of mass is so important to the real estate investor that I will focus on this principal in the closing of the document.

Objective – In war, how often do we see the larger, better trained force struggle to gain the upper hand? The United States in Vietnam. The Soviet Union in Afghanistan. There are numerous other examples.

If every war and every battle started with a clearly defined and attainable goal, this would not be the case. Unfortunately for past and future battlefield leaders, they are put in harm’s way by political leaders who have not truly considered the consequences of their actions.

This does not have to be the case for real estate investors, but it most often is. Whether working with large institutional investors, or a young family making their first real estate investment, it is a rare case when I meet with one who has a clearly defined, decisive and attainable objective.

There are many fund managers who have raised hundreds of millions of dollars for the purpose of investing in distressed real estate, but I have yet to meet a fund manager that truly understands what they will find on the street (battlefield).

Because of this, I recommend that institutional investors reach out to the few analytical real estate brokers around the country who can help them understand how a long-term real estate portfolio is going to perform. Specifically, I would recommend these fund managers define their goals in terms of ROI (Return on Investment) rather than with cap rates or cash on cash returns, as these methods are often misleading and are built with performance metrics that are most likely best-case scenarios with the "blind leading the blind."

Offensive – The leader who gains momentum on the battlefield, and is able to sustain it, has an advantage over his adversary. By maintaining an offensive posture, a battlefield commander dictates to the enemy instead of the other way around.

The real estate investor's enemy is "the market." To beat the market, the investor must take his tactical position and be able to exploit opportunities as they arise. Investors who have bulky and cumbersome processes are often times unable to meet the time demands of the best deals in the market.

An offensive posture is one that is continually seeking specific properties while maintaining the support structure to decisively respond to found opportunities. If institutional investors want to compete with the locals for the best values, they must utilize speed in their offensive. Their ability to close fast must be a weapon utilized to overcome being second to the fight.

Surprise – The commander on the battlefield employs surprise to seize an objective before the enemy can react effectively. Whether this is in the form of an offensive maneuver or a defensive employment, the warrior wants to maintain a tactical advantage by doing something the opposition was not expecting.

For the real estate investor, surprise can be attained by creating opportunities that were not obvious to the other players in the market. This could be in the form of a property redevelopment to a higher and better use, or through the use of massive funding to buy a bulk of tax deeds.

Institutional investors have the advantage of creating rapidly evolving "best practices" from multiple markets that will likely beyond the experience level gained in a singular local market. The key to surprise for the investor is to use creativity to gain an advantage in the market.

Economy of Force – In order to achieve mass on the battlefield, the military leader must put “enough” of his forces in the “correct” position. The flip side of this is that he must not allocate too many of his troops to secondary efforts, thus leaving himself the ability to mass when necessary.

This implies that he has great command and control over all of his forces, knowing what he needs to commit at the present time while leaving him the ability to commit to greater opportunities as they arrive.

The real estate investor must be able to use mass (allocate a lot of capital) in order to take advantage of timely opportunities, but simultaneously have his capital working effectively in the market. Without clearly defined goals, it is easy for the real estate investor to lose his economy of force.

Maneuver – It has been said that it is by maneuver that a superior general defeats a stronger adversary. The military leader positions his forces to take advantage of opportunities gained through mass, surprise, and economy of force.

The real estate investor finds maneuver to often times be the counter to mass. Large institutional investors have the capital to take advantage of more opportunities, so regional investors use maneuver to take decisive action and get the better deals before the larger investors can react.

The prudent fund manager will spend a lot of time determining his plan of action for maneuver. If he has a lot of capital to get into play, then he needs the ability to decentralize decision making to ensure that he is not out-maneuvered by the smaller players in the market.

Unity of Command – Successful military leaders know that too many cooks spoil the pot. The concept of unity of command simply means that for every mission or every endeavor, there should be somebody specifically in charge managing and leading the action.

This is also true for the real estate investor. Small investors must decide how the relationship between their real estate broker and their property manager(s) will be managed. Will they be on equal footing and reporting to the investment group? Or will one answer to the other? Perhaps they will independently report up the chain of command to a leader in the investor group.

The key to unity of command is to identify the person responsible for the ultimate success or failure of every single acquisition or campaign that the investor will undertake.

Security – The military commander views security as the flip-side of surprise, which means never allowing the enemy to gain an unpredicted advantage. Knowing the enemy might try to employ surprise, security anticipates this by employing measures to "not be surprised."

The real estate investor studies the market, understanding the dynamic between supply and demand in every local market. The investor is secure in knowing that markets move in a predictable manner, and by keeping a finger on the pulse of supply and demand, he is secure in his investments.

Simplicity – The warrior knows that things can go awry in the heat of battle, so all battle plans and preparations are made to be as simple as possible. The KISS principal is something every successful commander employs.

The real estate investor can keep things simple by understanding the business model and sticking to it. Keeping focused on the objective and ensuring that all goals are understandable to all involved parties is how the investor ensures the KISS principal is not violated.

Conclusion

Most local real estate battlefields are a mix of mass dueling with maneuver. The large institutional investors have the ability to bring large chunks of money to the table, while the small local investors are able to figure out the deals before they hit the general market.

The local real estate investors understand supply and demand, and they have identified realistic goals that can be attained with the resources that they have.

Currently, I have not seen the institutional investors arrive with any understanding of supply and demand, and their objectives are somewhat vague and seemed to be created from a defensive posture. Rather than exploiting the opportunities that do exist in the market, they sit back waiting (as if fearing to make a mistake) and creating objectives that will never be realized.

Fund managers must understand that ROIs are exceeding 30% in most local markets, and there are always enough local investors to consume that supply. If they continue to defensively demand an unrealistic return on their investment, they will continue to sit on their capital, while their competition exploits the opportunities in the market.

Institutional investors have not shown an ability to mass as fast as local investors can maneuver, thus they (fund managers) should assume the cream of the market will go to the local investors who can get there first. Fortunately, below the cream lies sufficient ROI to achieve market-leading goals.

The principle of mass requires action at some point, so fund managers must determine their entry point into the market. Billions of dollars are waiting to be invested into the Florida housing market, so institutional investors with warrior-minded leaders need to take the reins.

They must clearly identify decisive, attainable goals. They must take the offensive and use mass to diminish the ability of their competition to maneuver and thus push the smaller competitors out of the way.

With the 9 principles of war as their guideposts, these fund managers are poised to make history in the real estate market.

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