TALES FROM THE TRENCHES

BY BARRY C. MCGUIRE

HAPPY TALE

Two of our members partnered up and thought they would like to try the 'fix and flip' strategy. It was their first step outside their previous portfolio of three conservative 'buy and hold' properties. They were a little nervous about the usual things. Can we find something with enough hidden value? What about contractors? How do you find reliable tradespeople who will bid jobs at reasonable cost and finish on time? When do you start to market and should we do it on our own or use a realtor? How do we finance this? They did as much diligence as they could and started looking for properties.

They found a condo in a decent area in a decent building. The 20-year old unit was tired and dirty. Not one thing had ever been changed or painted by the previous owner. When viewing the unit, the owner's fuzzball of a dog happily greeted them by running around the unit and showing them her favourite scratching places on the rugs and woodwork. This condominium unit did not show well, but our members thought it had real potential. They went away, did some numbers and more diligence on this particular building. $20,000 worth of renovations would give them an estimated $40,000 profit.

Before making an offer they had chatted to their banks about a mortgage to buy the property and do the fix ups. They got the usual answer of 80% of the lower of purchase price or appraised value. The bank didn't want to talk too much about doing a loan based on the after repaired value with holdbacks until those repairs were done. In fact, the bank wasn't too enthusiastic about the concept at all. One member ran into a close relative who was bubbling over about his bank offering a line of credit at an introductory rate of prime minus one. The trick was that the line of credit had to be borrowed immediately and not repaid for at least three months. "Really," says our member, "I can help you with this problem!"

They quickly came to an arrangement for a loan big enough to buy the unit **AND** pay for the renovations essentially 120% financing. Since they expected the whole process to take about four months anyway, they agreed with the relative they had to pay four months worth of interest. That gave the relative some certainty about how much money he was going to make and satisfied the bank's minimum three-month borrowing requirement. The loan was set up as a 1st mortgage at 75% LTV at 7% and a second mortgage at 10% for the balance. Our members paid legal fees but no other lender fees or 'points'. Anyone who has borrowed private money knows this is an excellent deal.

Our members are cautious types so they chatted with their financial advisor to see what he thought of the deal. Here's what the financial advisor said. "This looks good; you guys have a track record in property ownership. If this renovation works out, tell me about the next one and I will provide the financing. If that second one works out, I will seriously consider advising my client base that they can invest with you guys and make some money." With financing now in place the offer was made, accepted and the renovation is now in progress.

SUMMARY:

1. Renovation deals are still out there.
2. Mainline lenders are still cautious.
3. Inexpensive private money is available, just ask.