13 Ways to Free Up Money: Add Liquidity to (Your) Illiquid Real Estate
by John V. Kamin

During 2005 and 2006, we kept urging members who owned multiple properties to "Sell your worst property now, but keep the best". The strategy worked well, clients tell us. Some sold their worst properties, others sold their worst and a few other properties, and still others sold everything and got into commercial property instead (to sidestep rent control).

The strategy worked. Property owners avoided being trapped into illiquid unresalable real estate when the market changed. You do not ever want to be trapped into a forced-sale situation with illiquid real estate. So, during the best of times, you always unload (at least some of the hardest-to-sell) parcels, so that you'll have some liquidity and cash to buy as the upcycle changes to a glut or a downcycle. During downturns, cash talks, but loose talk (without cash) simply walks.

Real estate by its very nature is illiquid, unmovable, subject to property taxes, other expenses and subject to new regulations by a changing group of enthusiastic regulators.

How Can You Enhance Liquidity of Illiquid Real Estate?

There are ways. But you must start at the very beginning, to avoid being trapped without cash, in property selection.

Fact: while all real estate is illiquid some of the time, different kinds of real estate have different degrees of illiquidity. For example, three bedroom, two bath houses near job markets are more easily resalable than very remote second homes.

Strategic Moves to Enhance Liquidity in Illiquid Real Estate

1. The first strategic step begins with buying real estate. Our <u>Forecaster</u> suggestion has been only to buy within commuting distance of major metro job centers where the 1,000,000 plus population is growing. Avoid the boondocks, the bolder-strewn wasteland, the cliffsides, the remote second homes, landlocked undeveloped parcels, and shrinking populations (Youngstown, OH).

If you want to go fishing, you have to go where the fish are. Fish like underwater structure, where small fish breed, and big fish go after the small fish. The fish don't go (usually) where the water is nice, clean with a sandy flat bottom without any structure or growing plants. Stick to the growth areas before you risk your property money, for faster, easier resale.

2. <u>Forecaster</u> members have been urged, when buying Pre-development Land (PDL) and other parcels to get frontage on the busy blacktop highways or on the exits to freeways. Simple enough. You don't want the parcel that's down the dirt road one mile from the highway. For one thing, while you may be able to get a prospect or two out to see it in a super-hot market, during a real estate downturn, prospects may not even to out to look at it. And the bidding competition for acquirers (to buy) will be small. (Fish where the fish are; go where the prospects are; stick to major metro job-growth centers, outlying commuter areas.)

3. For example, one <u>Forecaster</u> Research recommendation has been to go toward Highway 60 area exits in Pinal County, just past the Maricopa County line (Phoenix metro) and get that potential commercial frontage. Big construction - big developments

are going in. Pinal County has lower living costs and lower taxes than Phoenix metro (Maricopa County). But don't go past Florence Junction, or hit mountains at Apache Junction, that's too far. On the north are Indian reservations, on the east are mountains, on the west is Phoenix, and southwest is Sky Harbor, Phoenix, Airport. Prices are already soaring on that Forecaster 2003-2005 research, as predicted. But if you go to Yuma, Arizona, or Globe, Arizona, or Lordsburg, New Mexico, it's too far to commute, bidders are few and traffic is light. Stick to main metro areas, no more than one hour's drive; let metro areas grow toward your property. That will help enhance liquidity and resale on outlying metro fringe areas, blacktop highway frontage, make it easier to resell.

Numbers Game: Rental Cash Flow to Bottom Line

4. Another strategic move to enhance liquidity and illiquid real estate is to increase the cash flow, stick to rental properties (commercial or residential) that have monthly cash flow.

Got some empty units? Rent them out, make the best deals you can with tenants, but rent them. You can charge a higher rent, but give them one month's free rent after six months of paid rent, on month-to-month leases. Enhance the cash flow on properties that resell based upon a multiple of cash flow. I might not suggest that you put a family member or a second cousin in those empty units, but do what you must to get a tenant in there, so the prospective buyers can see some monthly cash. Then multiply that gross rental income yearly by 10x or 20x, whatever the going rate is there. Bluntly, enhance the monthly cash flow to enhance yearly cash flow which, in turn, will enhance sales multiple, to resell property.

Wood and Stucco ATMs?

5. Absolutely can't resell this year or next, for various reasons? Then you can "borrow out the money" using the equity in the property as collateral. Modern lenders can: a) give you a bigger first mortgage, b) give you a second or third mortgage, or both; c) give you a home equity loan or line of credit secured by the buildings and property. I try to avoid buying properties without buildings and without cash flow unless they happen to be in a unique location. This is called the "Use your property as an ATM" method, to get cash, while you cruise towards a future sale.

OPM = Other People's Money

6. When you first buy property, buy it with as much seller financing, or lender financing, as you can (unless you're getting a steep 20% to 40% discount for paying cash). Even if you could pay all cash, take the seller financing and/or mortgage instead, until you get a good handle on the property. Reselling a property with a big mortgage is usually easier, especially if the property loan is assumable by the new buyer. Loans can reduce risk and cash burn, if you bought the property mostly with someone else's money, rather than your own, if you decide to walk away from the deal after a couple of months. But if you suspect you might have to walk away, do a more thorough pre-purchase inspection. It's better to walk away from a deal undone, than from a deal you just blindly or hurriedly bought. Tighten your pre-purchase inspection, take longer to buy, so that you can sell faster. Gain negotiating power when you can point out specific have-to-be-fixed defects before you buy, rather than after.

Resell Cheap By Buying Cheap?

7. Before finalizing your purchase of property, keep your mind focused on buying cheap or cheaper. Forecaster reports urged members when buying Pre-development Land, to buy the third lot frontage from the corner (at a cheaper price rather than the gas station corner intersection). That way, if the PDL land indeed develops into a strip mall, shopping center or cluster of offices, you'll be in cheaper and can still get a high price because you'll own the key third or fourth lot from the corner (necessary for a bigger development). Got it? Rather than tying up $900,000 to buy the gas station corner, buy the third or fourth lot in at $200,000 - same size or bigger lot. Potential reward is greater, but risk and cash cost is much less.

8. By buying cheaper, if things do not go as planned, you can add liquidity with little or no loss, because you're in a position to sell cheaper. But the corner guys who overpaid won't want to cut their $900,000 outlay and resell at $550,000 if development is slow in coming or shifts elsewhere.

E.G. One commercial acreage parcel I bought in New Mexico next to a steakhouse on the main east/west highway just outside of town, indeed, development was shifted. Road builders located a new east/west Interstate Freeway about a mile north, and much of the commercial traffic moved in that direction. Sure, the property went up 2000%, over several decades; but it should have gone substantially higher if the highway shift had not occurred.

"Beautiful Slums"?

9. Want to enhance liquidity and resale possibilities? As soon as you get possession, do what one Forecaster member near Detroit does when she gets foreclosed properties. She immediately rents two dumpsters and throws out everything in the old houses, and I mean everything.

Then she hires the painters, plasterers, repaints everything, repairs everything except the big ticket items, so she can resell at a big profit, hopefully in a year. Buyer-prospects like to look at cleaned-up improved buildings, not trash-filled junkers from former tenants, clutter.

10. Get the chainsaw out, have the guys cut down all that overgrown landscaping, haul everything away, to improve appearance. (Virtually every rental property I have ever bought had overgrown landscaping that accumulates trash, accumulates monthly maintenance costs, gives hiding places to thieves and others of criminal dubious intent.) Just chop it, to make it more liquid, more resalable.

Dump, paint, repair and haul away. You may increase liquidity by 50% by these simple but less costly moves, and you'll certainly increase the sales price and profits you get!

Speak Up Often

11. When you want to sell the property, "tell the world". Don't just put up a little sign, or tell a neighbor. Talk to 10 or 12 brokers and realtors every month (different ones). Make sure you're listed in the Multiple Listing Service. Make up flyers with "7 Great Reasons to Buy This Property!" and include a photo and your contact information,

including property address, your address and your phone number, even if listed with broker. List 10 exciting features. Stress 12 terrific benefits to buyers.

Example: Many brokers promised me they'd make up a selling brochure on out-of-state properties. But after three months, six months, even after one year, they have not kept their promises. So, I just make up my own brochures and hand them out to everyone (including the listing broker). They failed. Then, if broker hasn't come up with decent solid offers within a three or six month listing, I move on to the next broker. No long (renewed time-after-time) listings if the broker is just sleeping in his chair, waiting for someone else in the MLS service to bring him a buyer.

Contrarian Hunger

You want a hungry broker, not someone who is going to leave the sales work to others. If he's not going to do the work, why should you pay him a commission and automatically renew the listing?

On one midwest property, not long ago, I dealt with 10 different brokers. Most of them were disasters. I finally found a developer myself for the one acre property who paid me 50% more than every one of the brokers said I could get for it.

E.G. Many brokers are trained to knock down the seller's price after they get the listing. Some actually take classes in this training. Though they're supposed to be representing you, the seller, they are mostly representing themselves and often represent the buyer. Be very careful with whom you list, and keep your listings short. No results equals no "automatic" listing renewal. If you get good results, you may consider renewing the listing.

Talk Is Cheap, Written Offers Only

12. Always get verbal offers in writing. Do not negotiate over the phone with unwritten offers. 99% of the time they're worthless (not worth the paper they're not written on). At least get a Letter of Intent if not an offer.

13. Dress up the front and back of the property, whatever can be seen from the street, with large, colorful potted planter. E.G. Five gallon pots of blooming geraniums in colorful orange or yellow planters. In the winter, display a potted Christmas tree with lights. Remember, when you sell the property, you can take these pots of blooming plants home with you or to your next sale property. Dress up the property with portable blooming colors on the outside, next to the large (minimum 3' x 6') "For Sal" sign that you commissioned. If it's a vacant lot, string some colored balloons around the sign to distinguish it from other "For Sal" signs in the area, to grab prospective buyer and broker attention.

Summary: Although all real estate by its very nature is illiquid, some properties are far more illiquid than others; you have to start early when buying, before buying, in property selection, to enhance liquidity.

There are many ways to enhance liquidity and cash, and enhance resale, even if past owners and brokers have failed to sell the property. More in future issues.

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