From Foreclosed to Fortunes

Hard money lenders can give distressed-property investors a boost

By Yanni Raz

Commercial mortgage brokers and hard money lenders are always looking for new business. One potential avenue can be found by looking at the remnants of the housing collapse.

The real estate meltdown left many properties in foreclosure. Many lending institutions used questionable techniques to drive sales, ultimately leading to a bubble that inevitably burst, leaving many homeowners underwater in their family houses. Once these properties were returned to the banks, neighborhoods were gutted, and these homes sat empty — sometimes for years.

As the real estate market recovered, investors began realizing how desperate banks were to unload these properties. After all, they don't do the banks much good simply sitting there unused. A paradox was created, however, because the same lending institutions that originally financed these properties tightened up their purse strings, essentially halting property lending for anyone with a less-than-perfect credit score. This vicious cycle has continued, save for one key dynamic — the emergence of hard money lenders.

Investing in distressed properties

With banks having caches of properties currently in foreclosure, they'd love nothing more than to sell these properties and recoup the lost capital. Those with investment capital in hand have never had an issue acquiring these locations.

But what are the options when attempting to purchase distressed properties if you don't currently have the necessary funds? Honestly, there aren't many.

Distressed properties are often sold far below their market value, making them a prime opportunity for investment. Specializing in these properties can be lucrative, provided that the buyer understands how hard money lenders can assist in the financing of said property. As real estate values continue to climb, acquiring and flipping these locations can do wonders for one's investment portfolio.

Leveraging hard money

Hard money lenders allow investors to acquire capital for use on properties, although they often lend amounts that are 20 percent to 30 percent below the property's value. This is the lenders' built-in protection against default. Considering, however, that distressed properties are also acquired at far below the market price, it's no wonder that these lenders have seen incredible growth in recent years.

Once a property is acquired, owners can make small modifications and put it up for sale. Provided that the property sells in a reasonable amount of time, the owners are able to take advantage of the location's distressed nature, repay the loan and still walk away from the transaction with a substantial profit.

Understanding the nature of hard money is the key to taking advantage of the market's cache of distressed properties. And anytime someone acquires a hard money loan, they must understand these important nuances and details.

Secured loans

Hard money loans are secured by the property itself. Acting as collateral, the lenders have security in knowing that they have a tangible asset at their disposal in the unlikely event of default.

These companies work directly with borrowers to research and appraise the property, giving the buyer the opportunity to see all relevant information on a particular property before borrowing. This is a signal of the company's desire to simply finance the property, because they have little to no interest in repossession. In other words, many reputable lending houses will put you in a position to succeed.

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Loan amounts and expertise

The loan amounts are another element that offer security to a lender. Any hard money borrower can usually expect to receive 70 percent of the property's value in the form of a hard money loan. This 30 percent difference is an added layer of protection for the lender. Because distressed properties are often sold for amounts far below the market value, however, this dynamic can actually work in favor of the borrower.

In addition, many reputable hard money lenders focus on distressed property lending and are experts in the field. This works in the borrower's benefit, because these companies usually have a great understanding of the marketplace and a property's recovering value — and they have the experts to help assess the location.

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Distressed properties offer a wonderful opportunity to property investors. Because banks are interested in simply recovering their lost capital and moving on from the transaction, those who understand how hard money works can leverage these lenders, acquire distressed properties at prices far below market and resell them for incredible profits. ■