

## Shave and a Haircut...Two Bits

Frank and Sandy are new real estate investors. A few days ago I received a very excited phone call from them. They had found a great deal in Calhoun and wanted me to look at the property.

Over the phone the numbers sounded rock solid. The house was twelve years old. It had three bedrooms and two bathrooms. In 2004 the house appraised for approximately \$94,000. Frank and Sandy's contract price was \$65,300. Their exit strategy was to buy, rehab, and then sell the property.

I met Frank and Sandy later that day at their target house. My jaw dropped open as I pulled in the driveway. I quickly realized that I had forgotten to ask one vital question during our phone call. What was the all important question? "*How much is the estimated rehab?*"

One of the biggest mistakes new investors make is to take on a rehab project that is **WAY** beyond their experience level. I think this happens to all of us at one point or another. This was the case with Frank and Sandy's target property.

Let me try to describe the property at which I was looking:

First, the phrase "*deferred maintenance*" came to mind. The owners had put off painting and re-roofing the house *for years*. The gutters were hanging from the house and reminded me of some sort of wild theme park up and down ride. The homeowners must have been preparing for hurricane season because one of the front windows was covered by a sheet of rotten plywood.

Second, the phrase "*natural landscaping*" came to mind. Honestly, I never knew holly bushes could grow to twenty-seven feet! I had to wonder how much the homeowners were saving on gas because they sure weren't using their lawn mower. Still, this had to be one of the safest houses in the neighborhood; with the front bushes growing *into* the front porch, no burglar could *see* the front door, let alone break in to it.

Third, the word "*landfill*" came to mind. You would think the county would have some sort of rule requiring the homeowners to take their kitchen garbage to the dump more than once a year.

Fourth, the word "*aromatic*" came to mind. When I opened the car door the funky smell from all of the garbage leaped into my car and went straight up my nose. Honestly, I must have been overcome by emotion because I teared up more than I did when they cancelled The Dukes of Hazard.

Without even getting out of the car, I estimated the rehab to be *at least* \$25,000, an amount that immediately killed the deal. Why? Because this house was a money pit. As the numbers stood, there was no way to earn a profit ( $\$94,000 - \$25,000 - \$65,300 = \mathbf{\$3,700}$  **gross profit**).

From the \$3,700 gross profit, you would have to subtract things like holding costs, realtor commissions, taxes, advertising expenses, etc. As Kim says, there was no slick left on the table.

Could this deal have been saved? Absolutely, *if* the homeowners would have agreed to sell their property for about \$51,000 instead of \$65,300. At \$51,000 there is enough slick left on the table to earn a profit.

Usually we advise newer investors to avoid properties needing major repairs. Instead, they should work with properties needing mainly paint and carpet. We refer to these types of deals as properties needing a shave and a haircut.

So what does “shave and a haircut...two bits” mean?

When I was a kid there was a popular saying that went, “Shave and a haircut...two bits.” Please understand that I’ve been on this earth for a few decades. You’ve heard of generation X and Y? Well I’m from generation FBG. This stands for generation Fat, Bald, and Grey. (Yes, Sandell, you can be *bald* and *grey* at the same time – just look at my head!) Back when I was young, a man could get a shave and a haircut for...yep, you guessed it, two bits.

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