

Builders in Florida who grew accustomed during the industry's recent boom times to selling out their developments even before a shovel went into the ground are noticing a stark shift in the marketplace and could find themselves in trouble if they don't take steps to manage investors who are nearing closing day with neither the intention nor the means to close on those sales.

"Get control over those investors before they close," Robert J. Kanjian, president of **Building Solutions LLC** in West Palm Beach, warned builders attending the **Southeast Building Conference** earlier this month in Orlando, Fla. "Get your sales team's head out of the sand. What are investors going to do? Can they close? Today, you want the closing," he said, and builders facing a problem with investors can "get ahead of them on that deal" by using assignment options.

Kanjian noted that the "good days" where deals were sold on lotteries and one development could rack up \$37 million in presales and sell out in four hours are over. With many sales off 50% or more from their peak, the big investor market that held steady in the state up to about last May "stopped sooner and deeper than expected," he said.

"Those people we sold to, we're dealing with that today, because most of them were investors," Kanjian said, and not the traditional garden variety of investor who purchases property to rent it for awhile and then eventually sell it.

The typical investor who populated Florida's go-go residential real estate market is "the same guy who thought investment in the Internet was a good deal a couple of years ago," Kanjian said. People started trading on their 401(k)'s and taking out equity lines to make relatively small deposits on properties they expected to be able to flip for a big profit.

A Problem With Pre-Sales

But two things happened on the way to the payoff: last year's hurricane season brought an end to the bullish psychology driving up prices and buyers no longer feel impelled to rush to a sales office on the day that the for-sale signs go up. And, compounding that piece of bad news, builders' costs went up 25%-30% after Katrina, Rita and Wilma blew through, to levels exceeding pre-sales prices.

For instance, he said, in West Palm Beach, where 300 to 500 condominium units are coming off the boards every day, the pre-sales price was averaging \$175 to \$200 a square foot. Today, the cost of completing those units is coming in at least at \$200 a square foot and many developers are realizing they may have paid too much for land.

Under that set of circumstances, "you need to be mining the backlog now," Kanjian said, and "you need to be finding out what investors are doing. They didn't put options in, so their homes aren't going to be the easiest to sell, although they may be the least expensive. Even if the investor wants to flip it, there aren't a lot of buyers," because people are waiting for prices to drop, Kanjian said, even if it isn't possible to build for the prices they want to pay.

Taking Back Contracts

Kanjian suggested that builders should use assignment agreements to take back contracts from investors who are not ready to close and initiate a resale program. Even though current prices are stagnating, they still typically exceed pre-sales levels, so that investors can undercut the builders on prices they are asking for their unsold inventory. However, this can work to the builder's advantage, if a deal is structured in which the original buyer is able to recover the deposit plus some cash out of the higher resale price.

If you don't let investors assign their contracts, they will try to flip them anyway, and start controlling the builder's sales price, he said. "I want to get them off the market. They're killing me when there are all of those for-sale signs in the community."

If prices do go down, investors could be hurt and forced to give up their deposits, but "we're not seeing it yet," Kanjian said.

To get this program off the ground, Kanjian suggested setting up someone in the office to act as a liaison who is responsible for assignments, "a person who understands the game." He added that it is possible to double the profit on a sale made last year. Plus, "you don't want to know you don't have a closing at the last minute. You want to know a few months in advance to plan for it."

Kanjian also emphasized that builders are relying on "salespeople who haven't been in a tough market before," and they need to "get those people prepared for the tough market we're in."



Kanjian also said that builders experiencing inventory problems should monitor Realtor® listings to ensure that their homes aren't competing with investor homes. "You want to know if you're selling a home for \$400,000 and it's listed for \$335,000 and 'bring all offers.'" The buyer will typically need to obtain permission from the builder to legally list the property.

If there is a silver lining to the predicament that Florida builders are now finding themselves in, Kanjian said, it is that more than a year into the slowdown "we haven't seen prices go down." This provides an opportunity to convey to the home-buying public the message that costs have gone up too much for builders to be able to sell their homes for less.

In the current down market, housing affordability constraints continue to grow, he said, and not just because of rising mortgage interest rates: property taxes and insurance now account for 40% of an average housing payment in Florida.

Florida's Insurance Crisis

There was a clear consensus among SEBC delegates that the crisis in property and builders' risk insurance is the most pressing problem facing the state's home building today. Outrageous quotes from insurance companies and severe lack of availability were the most common sources of growing frustration.

"With respect to insurance, we must think first in terms of availability, then affordability, then sustainability," said John Wiseman of [CORE Construction](#), the president-elect of the [Florida Home Builders Association](#) and chairman of [Florida Home Builders Insurance, Inc.](#)

"There are no easy answers to this dilemma," he said, "but I can tell our members that we will be taking part in an upcoming insurance summit with state leaders to explore solutions, and we are pursuing the creation of catastrophic funds at the federal and regional levels."