

# STARTER PROJECTS

One of the things we hear most often from people seeking coaching or advice on small development is “I just don’t know what I don’t know.” While this document attempts to demystify the process, the truth is, those anxieties are well-founded. Real estate development is something you can only really learn by doing and every project has its own risks and surprises. This is why it is important to start small. Through the perspective of a rooted small developer, ‘the neighborhood’ is the project, advanced in building-by-building increments. Consider the following a collection of options in your real estate portfolio, each supporting the others.

In the pool of real estate development these are reliable pathways to learn to swim in the shallow end. They correspond with some standard financing steps so you can keep the money part simple and reserve your brain space for things like zoning and construction.



## 1) BUY A 1-4 UNIT BUILDING FOR RENT

Buy an existing building with one to four legal units that already rent. You should be able to find information on the existing cash flow of the building like the rental rates, taxes, and utility costs. Use a pro-forma to determine if the property makes sense as an investment.

You can buy a 1-4 unit building with an FHA backed mortgage, and if you plan on moving in as an owner-occupier the minimum down payment is 3.5%. If you do not live in the building, you will need a down payment over 20%.

Look for a place in a walkable neighborhood that doesn’t need a lot of work. Any small improvements henceforth and your attentiveness as a landlord will help reduce tenant turnover and attract higher rents.

### *How does this make money?*

If the rent you collect is greater than your mortgage and operating expenses, your building now has a positive cash flow.

## 2) BUILD AN ACCESSORY DWELLING UNIT TO YOUR SINGLE FAMILY HOME.

This one comes with a major caveat, so before you start pinteresting backyard cottages, check your zoning. Few cities permit ADUs to be built in any practical way. If you happen to be in a jurisdiction that does, like Portland, you can help push the needle by showing the rest of the country how advantageous ADUs can be in a neighborhood landscape.

You can finance your ADU with cash, a construction loan, or a home equity line of credit. Get your permits and build the thing yourself or with the help of a contractor or handy friends.

Make sure your rental unit is built to legal requirements and find a tenant. Better yet, already have one in mind.

### *How does this make money?*

You are adding an income stream to your house. If the rent you collect is greater than your mortgage and property expenses, your house now has a positive cash flow.



FOOD TRUCKS AND TENTS IN A GOOD LOCATION CAN EVOLVE INTO BUILDINGS IF SUCCESSFUL. IN EACH CASE, SMALL DEVELOPERS ARE ACTIVATING SPACE AND CREATING VALUE IN THEIR NEIGHBORHOOD.

### 3) SEASONAL MARKET OR KIOSK

If you are interested in commercial space, this is a great way to learn the essentials at low cost, all while building trust in your community. Borrow or rent underutilized space from a landowner in a good location. Let's say you've got a few parking spaces in highly visible and accessible area that is hungry for retail. Your job is now to create value in that space. You can book vendors that pay a fee to be there and set up seating, food, or entertainment. Once you've mastered a temporary set-up, consider building a kiosk.

This kind of endeavor is best done with minimal cash and a DIY spirit. It will give you experience in creating value in underutilized space, understanding cash flow, and managing tenancy agreements.

#### *How does this make money?*

If you can rent out space for more than it costs you to be there, you have a positive cash flow. Additionally, if you own adjacent property, you could be increasing the value of the surrounding area.



### 4) BUILD NEW FOURPLEX

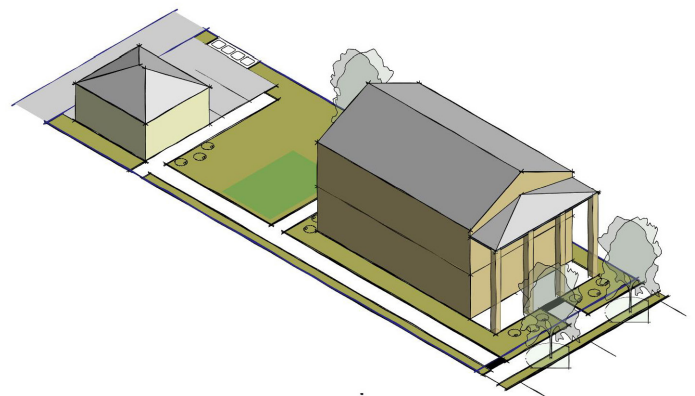
First, get pre-approved for a mortgage to determine your budget. You can include future rentals in your projected income. Then find land in a walkable area and pay less than 20% of your total budget for it. Put together some plans and cost estimates (likely involving a contractor) and take that to a local bank to get a construction loan. Again, this needs to be within the budget of your pre-approved mortgage.

Build a simple, flexible building.

Replace your construction loan to a permanent loan (i.e. a mortgage). The bank will have an appraiser assess the value of your new fourplex and determine the value of your mortgage.

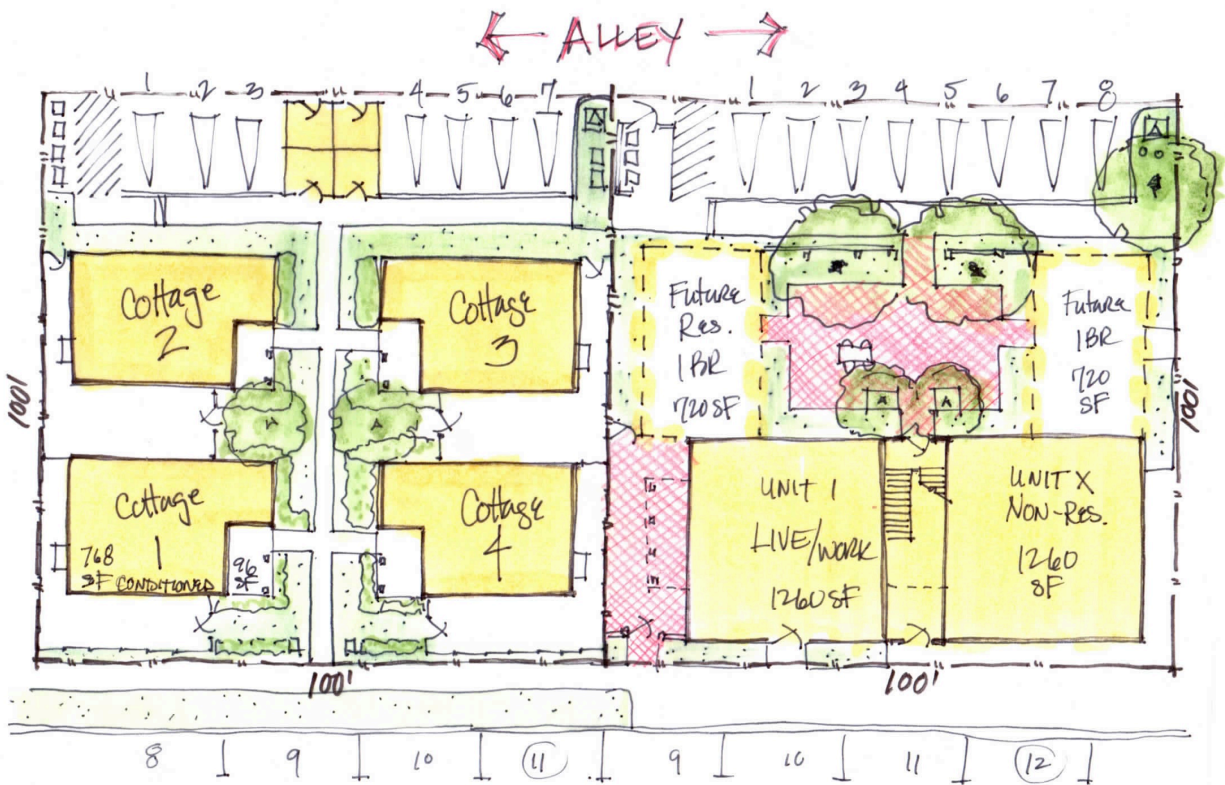
#### *How does this make money?*

If the rent you collect is greater than your mortgage and operating expenses, your fourplex now has a positive cash flow.



A DESIGN FOR A FOURPLEX. DRAWING BY BROWN DESIGN STUDIO, RENDERING BY KRONBERG WALL ARCHITECTS.





COTTAGE COURT (LEFT) AND 4-PLEX (RIGHT). NOTE THAT BOTH EXAMPLES ARE 1-4 UNIT PROJECTS THAT MEET THE REQUIREMENTS FOR AN FHA-BACKED MORTGAGE. EACH IS "A HOUSE" IN MORTGAGE TERMS. FIGURE COURTESY OF ANDERSON | KIM ARCHITECTS

## 5) ONE STORY COMMERCIAL BUILDING REHAB

Identify an undervalued commercial space and a tenant. If you are an investor-owner of the commercial space, it's best to have a tenant in mind before buying. You'll need to buy it with cash or get a construction loan to do improvements (value determined by the viability of your tenant, typically 3-5 year personally guaranteed construction loan).

If you are a business owner who will occupy some or all of this building and you have a couple years of operating history, you can get a Small Business Administration 7A (SBA 7A) loan to buy or build the building with a minimum 10% down payment. You must have a credible business plan that demonstrates that within 5 years, you will use at least 51% of the floorspace for your business to qualify.

### *How does this make money?*

Once you own the space, create more value than you paid for by filling it with a great business (or multiple businesses). If your building and tenants act as good neighbors, it can encourage others to follow suit. The services provided by the tenants are an amenity for the neighborhood, which creates more value in your property. Additionally, if you own adjacent property, you could be increasing the value of the surrounding area (i.e. your buildings).





## 6) 1-3 UNIT FIXER UPPER

First, be a handy-person or have a network of handy-people that will offer high quality work for low rates or barter.

Find a vastly undervalued building that requires some major gutting and overhaul.

Go get a FHA 203(k) Purchase/Rehab mortgage (which allows you to take out more than the price of the house to cover anticipated reno costs). If you intend to be an owner-occupier, you need a minimum 3.5% down payment. Or, you can get a construction loan\*\*\* (as in the Build New Fourplex section) and replace it with a mortgage later.

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Whenever possible, we recommend living in the neighborhood or building which you are developing. The insights and relationships gained by living on site are invaluable. All of these options are time-tested ways that people like you have created value in their neighborhoods and opportunities for more people to live, do business, and give back locally.

Then spend the rest of your waking hours bringing this property up to rentable quality as soon as possible.

### *How does this make money?*

If you can manage to pay less in buying and fixing this building than you can collect in rent, you will have a building with positive cash flow. There is also the option to “fix & flip” where you resell the property once it’s in good condition. We highly recommend a “buy & hold” approach instead where you keep the building and rent it out, earning money slowly over the long run.

